

Bhagawati Steel Industries Private Limited

Ratings

Facility	Amount (Rs. in Million)	Ratings ¹	Rating Action
Long Term Bank Facilities	248.72	CARE-NP BBB- [Triple B Minus]	Reaffirmed
Short Term Bank Facilities	2,808.92	CARE-NP A3 [A Three]	Reaffirmed
Total Facilities	3,057.64 (Three Billion Fifty-Seven Million and Six Hundred Forty Thousand Only)		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has reaffirmed rating of 'CARE-NP BBB-' assigned to the long-term bank facilities and 'CARE-NP A3' assigned to the short-term bank facilities of Bhagawati Steel Industries Private Limited (BSPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of BSPL continue to derive strength from its established track record of operations along with experienced promoters and management team in the related field, low gearing levels with adequate debt service coverage indicators, diverse product range catering to wide spectrum of industries, established marketing setup and brand with strong customer base, locational advantage and demand of steel products in the country. The ratings also take comfort from rebound in financial performance in FY23 (Unaudited, FY refers to the twelve-month period ending mid-July) after a subdued FY22.

The ratings are however constrained by the company's working capital intensive nature of operations, raw material price volatility and foreign exchange fluctuation risk, exposure to volatile interest rates and its presence in highly competitive nature of steel industry.

Going forward, the ability of BSPL to sustain growth in the operations while maintaining the profit margins and rationalization of its debt through efficient working capital management will be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Strengths

Established track record of operations along with experienced management team

BSPL has an operational track record of almost three decades in manufacturing pipes, tubes and other allied steel products. The promoters of BSPL have an experience of more than three decades in the steel industry. BSPL is managed under the overall guidance of its three-member Board of Directors (BoD) which includes experienced businessmen/industrialist with wide experience in the manufacturing sector. Mr. Sumit Kumar Agrawal is the Chairman and the managing director of BSPL and has more than 30 years of experience in various types of business and industries.

Improved financial performance in FY23, albeit on a low base of FY22

During FY23, BSPL's Total Operating Income (TOI) rebounded by ~95% growth year-on-year (y-o-y) to Rs. 3,578 Mn mainly on an account of increased execution of orders at hand catering mainly to government projects coupled with higher sales realization. With increase in the total operating income, PBILDT of the company also rebounded to 13.94% from 8.68% in FY22 to 13.94% in FY23. Consequently, PAT margin of the company improved to 7.49% in FY23 vis-à-vis 3.88% in FY22.

Also, the company has unexecuted order book at hand of Rs. 3,152 Mn as on mid-October 2023, which provides reasonable revenue visibility for FY24. The company's ability to sustain the revenue growth momentum going forward while maintaining profitability will be critical from analytical perspective.

Sustained low gearing levels with adequate debt service coverage indicators

Overall gearing ratio of the company improved to 0.54x at the end of FY23 vis-à-vis 0.62x at the end of FY22 mainly on account of accretion of profits to reserve. The improvement in operational performance leading to higher PBILDT in FY23 also led to improved interest coverage of 4.48x in FY23 from 4.12x in FY22 despite substantially higher interest expense in FY23 amid higher interest rates. Similarly, Total debt/ Gross Cash Accruals improved to 1.76x in FY23 compared to 4.70x in FY22 supported by improved cash accruals. Although debt levels could increase, in line with growing scale of operations, capital structure and coverage indicators are likely to remain steady as the company does not have any major debt funded capex plans over the medium term.

Diverse product range and locational advantage for the company

The company is into manufacturing mild steel (MS) black pipes & galvanized (GI) pipes and their variants along with tubular pole, telescopic pole, structure, shutter profile etc. The company is also involved in selling galvanized plain sheets (GP Sheet), hot rolled coil (HRC) sheet and cold rolled coil (CRC) sheet by cutting it in different sizes. In addition to steel products, the company also provide engineering services as well such as installation, commissioning, testing and follow-ups. BSPL sells its product all over Nepal through direct marketing network. Most of the sales revenue comes through direct domestic sales, followed by tender based sales. Also, with plant site located in Chhatapipra, Simara, only ~15 Kms from Indo-Nepal borders and Birgunj dry-port, the factory's proximity to the border remains a positive point leading to savings in huge freight cost as majority of raw materials used by BSPL are imported from India.

The company sells its products under the brand name of "BST" all over Nepal. The company's established brand presence ensures regular demand and aid in the differentiation of products with the competitors thereby, reducing the impact of competition induced volatility in prices over the years. The company is an approved vendor of various Government Departments and reputed business group.

Key Rating Weaknesses

Working Capital Intensive Nature of Operations

BSPL is involved in manufacturing of wide range of steel products, and is required to maintain adequate inventory of raw material for smooth running of its production processes and meet immediate demand of customers. The company had net-operating days of 123 days in FY23, which improved from 208 days in FY22, marked by average inventory holding period of 81 days in FY23. Average collection period sustained to 55 days in FY23, while creditors period decreased to 13 days in FY23 vis-à-vis 17 days in FY22. Furthermore, being a manufacturer, it is critical for the company to maintain minimum inventory levels to meet immediate demand of its customers; all this led to high working capital requirements which were largely met through bank borrowings. The average utilisation of fund-based working capital limit against sanctioned amount was around 32.64% during last 12 months period ended mid-July, 2023.

Exposure to volatile interest rate risk

The company's interest rates are based on a floating interest rate regime, where a certain premium is added to the quarterly base rate and interest rate is changed accordingly on quarterly basis. The base rates of the banks and financial institutions (BFIs) in Nepal remain quite volatile as they are impacted by available liquidity in the system which leads to change in interest rates. Therefore, funding taken by the firm from BFIs is subject to volatile interest rate.

Raw material price volatility risk and foreign exchange fluctuation risk

The prices of major raw materials for BSPL which are mainly imported from India are market linked and determined on a periodic basis, thus exposing the company to the volatility in the prices having bearing on its profitability margins. The raw material consumption cost contributed around 83% of the TOI of the company in FY23. The general volatility in the iron and steel prices also has an impact on the price of the final products. Any sudden spurt in these raw material prices might not be passed on to the end customers, instantly, on account of competitive nature of the industry, which could lead to decline in profitability margins.

Furthermore, the total raw material requirement is met through imports and also the prices of the few products are linked to USD, for which the company is exposed to the foreign exchange fluctuation risk. The ability of the company to pass through changes in raw material prices to the customers and managing the foreign exchange fluctuation risks related to raw materials is critical for the company to maintain its profitability.

Highly competitive nature of steel industry

The iron and steel industry are intensely competitive and fragmented marked by the presence of both larger players and numerous smaller players in the unorganized segment. The demand of iron & steel products is considered cyclical as it depends upon the capital expenditure plan of major players in the end-user industry. Furthermore, the value addition in the steel products like M.S. Black, galvanized pipes & related products is low, resulting low product differentiation in the market. Further, with increase in the capacities of the existing plants and new capacities coming into operation competition has intensified which has resulted into substantial decline in profitability margins of the industry players.

Industry Outlook

Demand of steel products in the country is expected to grow in the medium-term despite near-term industry headwinds. Nepalese economy is developing and growing, and is in phase of investment in infrastructure sectors, power sector and tourism sector. Sustained demand for steel is likely given the need of construction materials in developing public as well as private infrastructures, road, bridges and other public facilities. Furthermore, the government's continued emphasis on infrastructure development, namely development of roads, hydropower, airports and other infrastructures etc. is likely to benefit the steel manufacturers like BSPL. This is also evident in the budget presented by finance minister of Nepal for FY24, where Government of Nepal has allocated Rs. 131 Bn towards the physical infrastructure and transport sector. However, with the construction sector in Nepal impacted by slower pace of economic growth coupled with relatively lower infrastructure spending by the government, the outlook of steel industry in Nepal looks challenging in the near term, particularly if actual government spending continues to be much lower than budgeted.

About the Company

Bhagawati Steel Industries Private Limited (BSPL) is a private limited company incorporated in 1991. The company is involved in manufacturing of pipes, sheets, door and window frames, shutter profiles, side channels, truss, poles and towers, suspension and motorable bridge and related products. BSPL has its manufacturing plant in Chhatapipra, Bara, Nepal with total installed capacity of 85,500 Metric Tons Per Annum (MTPA).

Brief financials of BSPL for the past three years ended FY23 are given below:

(Rs. Million)

For the year ended Mid-July	FY21	FY22	FY23
	(Audited)	(Audited)	(Unaudited)
Income from Operations	3,220	1,835	3,578
PBILDT Margin (%)	13.31	8.68	13.94
Overall Gearing (times)	1.61	0.62	0.54
Interest Coverage (times)	9.83	4.12	4.48
Current Ratio (times)	1.44	1.96	2.65
Total Debt/Gross Cash Accruals (times)	4.08	4.70	1.76

Annexure 1: Details of the Facilities Rated

Nature of the Facility	Type of the Facility	Amount (Rs. in Million)	Rating
Long Term Bank Facilities	Term Loan	249.72	CARE-NP BBB-
Short Term Bank Facilities	Fund Based Limit	1,183.92	CARE-NP A3
Short Term Bank Facilities	Non-Fund Based Limits	1,625.00	CARE-NP A3
Total		3,057.64	

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