Nepal Overseas Marketing Company Private Limited (NOPL): [ICRANP] LBB+/A4+ (Assigned)

February 3, 2021

Summary of rated instruments:

Instrument*	Rated Amount (NPR Million)	Rating Action
Long-term; fund-based limits	195.0	[ICRANP] LBB+ (Assigned)
Short-term; fund-based limits	400.0	[ICRANP] A4+ (Assigned)
Short-term; non-fund based limits	300.3	[ICRANP] A4+ (Assigned)
Total	**895.3**	

** Instrument details are provided in Annexure-1.*

Rating action

ICRA Nepal has assigned the long-term rating of [ICRANP] LBB+ (pronounced ICRA NP L double B plus) to the NPR 195-million long-term loans of Nepal Overseas Marketing Company Private Limited (NOPL). ICRA Nepal has also assigned the short-term rating of [ICRANP] A4+ (pronounced ICRA NP A four plus) to the NPR 400-million fund-based and NPR 300.3-million non-fund based limits of NOPL.

Rationale

The assigned rating factors in the long track record of NOPL (operating since 1983) and its experienced promoter group. The rating also factors in the healthy pace of revenue growth maintained by NOPL in the recent years (CAGR 12% between FY2016 and FY2020, notwithstanding the de-growth in FY2020 due to the Covid-19 pandemic), which coupled with steady operating margins, has resulted in a steady improvement in operating profit in the recent years (notwithstanding a marginal moderation in FY2020). Furthermore, strong brand recognition of NOPL's major product lines remains a positive for incremental revenue growth of the company. The rating also takes comfort from the established supply chain of NOPL with well-diversified customer profile, reducing the customer-concentration risk. Further, the rating takes note of the steady retention of profits (albeit nominal) by the company in the last two to three years, supporting its capitalisation profile. Moreover, the working capital intensity (NWC/OI)[1] of NOPL has improved in FY2020 because of the reduction in inventory and debtor days post the Covid-19 crisis. The rating action also factors in the adequate debtor security mechanism through bank guarantees, mitigating receivable risks to a large extent.

The ratings are, however, constrained by concentrated product profile of NOPL. Approximately 75% of the company's FY2020 sales (~70% in FY2019) comprised products from the top two brands (mainly diapers from Unicharm and cosmetic products from Johnson & Johnson). Any impact on the sales and margins of these products could have a significant effect on NOPL's financial profile, including its debt coverage indicators. The ratings remain constrained by the absence of long-term dealership agreement between foreign suppliers of these brands and the company as well as the intensely competitive FMCG trading landscape with competing foreign brands and low entry barriers. NOPL's gearing has increased in the last two to three years because of the debt-funded capex undertaken for the construction of its corporate office, which coupled with the revenue de-growth in FY2020 has affected its liquidity position and debt coverage metrices. The ratings also remain constrained by the relatively lower economies of scale of the company.

Going forward, NOPL's ability to diversify its product line and revenue stream, improve its scale of operation and generate economies of scale will remain the key rating sensitivities.

[1] *NWC/OI of average of ~20% in last two years ending FY2020*

Key rating drivers

Credit strengths

Long track record of operations and experienced promoters – NOPL is in the import and distribution-based business since 1983 and is among the established players in this business segment in the country. A long track record, experienced promoters and good traction with the supplier and the ultimate consumers remains a positive for the future growth of the company.

Healthy revenue growth over years – NOPL registered healthy sales at a CAGR[2] of ~12% between FY2016 and FY2020, despite a 15% decline in revenues in FY2020, largely because of pandemic-related lockdowns and curb in economic activities. The revenue growth is driven by its major product lines that have strong brand recognition and growing demand in the domestic market. On a steady operating margin, the growth in sales has resulted in concomitant growth in OI levels, supporting the profitability and debt coverage metrices.

Working capital intensity moderated by supplier credit; debtor risk minimised by adequate security mechanism – Despite having a sizeable debtor and inventory days between 40 days and 60 days each, during the last two years ending in FY2020, the working capital intensity of NOPL has been moderated by supplier credit of ~40–50 days over the same period. As a result, the working capital intensity remains relatively cushioned as reflected in the NWC/OI[3] of 21% and 17% in FY2019 and FY2020, respectively. Further, the debtors remain largely secured (by way of bank guarantee), which minimises the recovery risk to a large extent and remains a rating positive.

Established sales channel and moderate sales concentration among top dealers – The company, over the years, has established a strong sales channel comprising over 300 distributors spread across the country. Further, the sales of the company remain fairly diversified across its customers with the top 10 customers accounting for ~35% of its sales in FY2020. The company's prior distribution experience (for the reputed brands like Gillette, Procter and Gamble, Unilever etc.) along with its current strong product lines also remains a source of comfort.

Credit challenges

Moderate financial profile – NOPL has a leveraged capital structure with debt-equity ratio of 1.7 times in FY2020 (against 2.1 times in FY2019). The recent improvement in gearing ratio is on account of reduction in inventory and debtor days post the Covid-19 crisis, the sustainability of which remains to be seen. Increase in the term loan in the last two to three years to finance the construction of corporate office has increased the company's gearing level. Although the construction of corporate office is expected to support the revenue profile of NOPL through rental income, the same remains to be materialised. At present, the debt utilisation level remains high vis-à-vis the OI as reflected in TD/OPBDITA[4] of 6.1 times for FY2020. Furthermore, total outside liability to total net worth (TOL/TNW) ratio remains relatively high at ~2.2 times as of mid-July 2020. With an increase in gearing in the recent years, the debt coverage indicators have also moderated with interest coverage and DSCR[5] declining to 2.4 times and 1.2 times, respectively in FY2020 from ~3.2 times and ~2.8 times, respectively in FY2017.

Decline in revenues due to impact of Covid-19 on concentrated portfolio – Given the effect of Covid-19 pandemic, NOPL witnessed ~15% decline in revenues in FY2020 against 15% growth in FY2019. With pandemic-linked lockdown and curb on economic activities, the monthly sales in the last four months of FY2020 shrunk by almost 50% compared to the same period in FY2019. Although sales recovered in the first half of the current financial year (FY2021), with the continued effect of Covid-19, sales were lower than the pre-pandemic level at ~NPR 762 million in H1 FY2021 against sales of NPR

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[2] *CAGR-Compound Annual growth rate*
[3] *NWC-Net working Capital, OI-Operating Income*
[4] *TD-Total Debt, OPBDITA-Operating Profit before depreciation, interest tax and amortization*
[5] *DSCR-Debt service coverage ratio*

1,026 million for H1 FY2020. The long-term continuation of the declining revenue trend could impact the overall financial profile of NOPL.

Moreover, the company's revenues remain concentrated towards the sales of MamyPoko pants (baby diaper), which contributed ~60% of total revenue in FY2020 (51% in FY2019). This is followed by Johnsons & Johnson's products which contributed around 15–17% of the revenues in the last two financial years. Given the concentration, any impact on these product lines could have a corresponding impact on NOPL's financial profile.

Absence of long-term exclusive arrangement with suppliers – Although the goods are imported as per the terms of the agreement with the suppliers, the agreements are not long term and exclusive. This exposes the company to the risks arising from discontinuation of the relationship by its major supplier brand or company.

Intense competition due to low entry barrier – The import-based distribution business of NOPL remains exposed to competition arising from the import of many similar products under multiple brands and distributed by the competitors. Further, domestic production of similar products amid the low entry barrier is increasing competition in this business segment.

Analytical approach: For arriving at the ratings, ICRA Nepal has applied its rating methodology as indicated below.

Links to applicable criteria:
Corporate Credit Rating Methodology

About the company

Nepal Overseas Marketing Company Private Limited (NOPL), established in 1983 as a proprietorship firm and later converted into a private limited company in 1997, is a national importer and distributor of consumer goods products for brands like MamyPoko pants, Johnsons & Johnsons, Stayfree, Sofy, Cello Techno Tip among others. Products are distributed by NOPL in a business to business (B2B) model through its sales channel comprising 300+ distributors spread across the country.

The entire equity stake in NOPL is held by three members of the Agrawal family—Mr. Pawan Kumar Agrawal (~60%), Mr. Ramji Agrawal (~20%) and Mrs. Meera Agrawal (20%). Mr. Pawan Kumar Agrawal, also the Managing Director of the company, oversees the regular operations of the company.

Key financial indicators

Particulars	FY2018 (Audited)	FY2019 (Audited)	FY2020 (Audited)
Operating Income-OI (NPR Million)	1,811.7	2,084.6	1,781.6
OPBDITA/OI (%)	4.1%	3.7%	4.1%
Total Debt/Tangible Net Worth TNW (times)	2.2	2.1	1.7
Total Outside Liabilities/ TNW (times)	3.4	3.1	2.2
Total Debt/OPBDITA (times)	5.8	6.4	6.1
Interest Coverage (times)	2.2	1.9	2.4
Debt service coverage ratio (times)	-	1.3	1.2
NWC/OI	21%	21%	17%

Source: Company data

Annexure-1: Instrument Details

Instrument	Limit (NPR in Million)	Ratings
Long-term limits		
Long term; fund-based limits (Term Loan)	195.0	[ICRANP] LBB+ (Assigned)
Total long-term limits (A)	**195.0**	
Short-term limits		
Short term; fund-based limits (Cash credit)	130.0	[ICRANP] A4+ (Assigned)
Short term; fund-based limits (TR loan)	220.0	[ICRANP] A4+ (Assigned)
Short term; fund-based limits (Demand loan)	50.0	[ICRANP] A4+ (Assigned)
Short term; non-fund based limits (LC)	270.0	[ICRANP] A4+ (Assigned)
Short term; non-fund based limits (Standby LC)	30.0	[ICRANP] A4+ (Assigned)
Short term; non-fund based limits (Bank guarantee)	0.3	[ICRANP] A4+ (Assigned)
Total fund-based (B)	**700.3**	
Grand total (A+B)	**895.3**	

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About ICRA Nepal Limited:

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