United Distributors (Nepal) (P.) Ltd.: [ICRANP] A2+ assigned

September 04, 2023

Summary of rating action:

Instrument (Amounts NPR in million)	Rated amount	Rating action
Short-term loan limits (fund-based and non-fund-based limits)	6,000	[ICRANP] A2+; assigned
Total	**6,000**	

Rating action

ICRA Nepal has assigned a short-term rating of [ICRANP] A2+ (pronounced ICRA NP A two plus) to the short-term loans (including non-fund-based limits) of United Distributors (Nepal) (P.) Ltd. (UDN).

Rationale

The assigned rating factors in the company's healthy operational profile as the national distributor of various established FMCG products/brands. The resultant diverse product portfolio and wide distribution network have resulted in gradual revenue scalability over the years, in addition to a healthy operating profit margin (OPM). While the revenue/margins have reported slight moderation during FY2023 amid the economic slowdown, the long term demand outlook for the FMCG segment is expected to remain adequate. The rating also takes comfort from UDN's healthy financial profile with total outsider liabilities to tangible net worth (TOL/TNW) of 0.9 times and total debt (TD) to OPBDITA of 1.1 times as of mid-July 2023. Hence, the company's interest coverage ratio (ICR) also remained good at 4.8 times during FY2023, despite the impact of high interest rates during the year. The company's long track record, its experienced promoters/management team and its association with the established Vishal Group also remain the rating positives. ICRA Nepal also takes major comfort from the company's improved liquidity profile in recent years with reduced working capital cycle (mainly on back of gradual reduction in debtor days over the years, along with increased support from creditors during FY2023), thus leading to reduced reliance on bank debts as reflected in adequate unutilised drawing power as of mid-July 2023.

Nonetheless, the rating mainly remains constrained by the company's equity market investments and relatively higher capex in the recent years, vis-à-vis the company's net worth. In recent years, these investments were mainly made using internal accruals, which coupled with UDN's increased dividend outflow during FY2023 raises concern on incremental liquidity profile. Similarly, the rating also considers the increased share of aged debtors during FY2023, along with high sales concentration among the top-10 dealers. The company's operations also remain exposed to regulatory risks as well as intense competition from distributors of other large MNCs. Going forward, UDN's ability to report adequate revenue growth whilst protecting margins, and controlling the working capital intensity will remain the key rating sensitivities.

Key rating drivers

Credit strengths

Sizeable revenue base with healthy margins – UDN is a national importer and distributor of diverse range of FMCG products under different reputed brands like P&G, Britannia, SC Johnson, and Kellogg's, among others. Given the company's long track record (>20 years), association with strong FMCG brands and a diverse sales network/product portfolio, UDN has been able to report sizeable revenue base (~NPR 13.8 billion in FY2023). Despite slight moderation amid largely stagnant revenues, the company's OPM also remained healthy at 10.1%. The positive demand outlook for the FMCG segment augurs well for incremental revenue perspective.

Comfortable financial profile – The company's reliance on debt remains controlled as reflected in TD/OPBDITA of 1.1 times as of mid-July 2023, while the TOL/TNW also remained satisfactory at 0.9 times as on the same date. While the ICR has reported recent moderations to 4.8 times for FY2023 (7.2 times in FY2021), this was mainly on account of spiked interest rates and the impact of increased regulatory cash margin requirement for imports during Q4-FY2022 and H1-FY2023. Considering the removal of high cash margin requirements and slight moderation in borrowing rates, UDN's overall financial profile is expected to remain largely satisfactory over the near to medium term.

Improved working capital cycle – UDN's working capital cycle improved over the years (~69 days in FY2023 over ~126 days in FY2019) mainly on account of control over debtor days, along with extended credit support by the suppliers, especially during FY2023. Thus, the reduced reliance on bank debts in recent quarters has led to liquidity buffer in the form of unutilised drawing power at ~32% as of mid-July 2023, which remains a major positive. However, the sustainability of the increased creditor support will remain a key monitorable.

Strong promoter profile and experienced management team – The company is a part of the Vishal Group, which is one of the established business houses of Nepal, having long and diverse presence in sectors such as manufacturing, trading, and financial services. The experienced background of UDN's promotors and management team have been reflected in its business performance over the years.

Credit challenges

High portion of net worth in long-term investments and high commitment to shareholder returns – Despite having a sizeable net worth base, ~28% of UDN's TNW as of mid-July 2023 was employed towards fixed asset creation in last five years, mainly warehouse construction (without availing term debt for the same). Additionally, ~27% of the company's TNW was utilised towards equity investments, mostly towards promoter shares of listed/unlisted companies, which are generally less liquid, in addition to the exposure towards market cyclicality. The resultant funding mismatch could create pressure over the company's liquidity profile, in case of unanticipated elongation in working capital cycle. Further, UDN's dividend payout increased to ~68% in FY2023 (out of profits for FY2022), against the average of ~47% in earlier three years and thus the incremental dividend payout trends shall remain a key rating monitorable.

Increased chunk of aged debtors and high sales concentration – UDN has reported a spike in the chunk of aged debtors during FY2023, with ~21% debtors being in >90 days category as of mid-July 2023 as against ~16% a year ago. This might impact the company's liquidity profile as debtors above 90 days are generally considered ineligible for bank financing, however, majority of which is due to the extended credit facility provided to modern trade outlets (MTO). The company's high reliance on large MTOs and some associated entities, along with relatively longer credit float to these also remains a rating concern. UDN also has high reliance on top-10 customers (~39% contribution in FY2023 revenues as against ~40% in FY2022).

Regulatory risks and intense competition – Amid the depleting forex reserves, the central bank imposed import ban on non-essential/luxurious items (including certain segments of UDN) from April 26, 2022 to December 16, 2022, which marginally impacted UDN's revenues. In addition, a higher cash margin requirement of 50-100% was also imposed by the central bank for certain segments as against 2-3% applicable for UDN earlier. This impacted the company's net margins through increased finance costs. Additionally, the FMCG trading sector in Nepal is also exposed to intense competition from distributors of other large FMCG companies.

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

Link to the applicable criteria:
Corporate Credit Rating Methodology

About the company

Established in 2003, United Distributors (Nepal) (P.) Ltd. (UDN) is the national importer and distributor of different FMCG products under established brands like P&G, Britannia, Amul, and SC Johnson, among others. UDN has a distributed network of around 35,000 outlets (varies based upon brand/products) within the country. The company is among the flagship units of the Vishal Group, an established family-based business house in Nepal. UDN's shareholders include Mr. Anuj Agrawal, Mr. Vivek Agrawal, Mr. Nikunj Agrawal, Mr. Vishal Agrawal, holding a total of 50% stake, while the remaining stake is held by 10 more individuals.

Key financial indicators

	FY2019	FY2020	FY2021	FY2022	FY2023
	Audited	**Audited**	**Audited**	**Audited**	**Provisional**
Operating income-OI (NPR million)	9,267	9,709	12,118	13,810	13,773
OPBDITA/OI (%)	8.1%	10.4%	10.9%	10.5%	10.1%
Total debt/Tangible net-worth-TNW (times)	1.8	1.3	0.6	0.9	0.4
Total outside liabilities/ TNW (times)	2.0	1.7	0.9	1.2	0.9
Total debt/OPBDITA (times)	4.3	2.8	1.6	2.1	1.1
Interest coverage (times)	2.3	3.1	7.2	6.0	4.8
DSCR (times)	1.2	1.4	6.1	4.9	4.1
Net-working capital/OI (%)	34%	31%	25%	27%	18%
Current ratio	1.0	1.1	1.4	1.3	1.3

Source: Company data

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About ICRA Nepal Limited

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