Jagdamba Cement Industries Private Limited: Ratings downgraded to [ICRANP] LB+/A4

December 18, 2023

Summary of rating action

Instrument (Amount in NPR million)*	Last rated limits	Current rated limits	Rating Action
Long-term loan limits	289	769	[ICRANP] LB+; downgraded from [ICRANP] LBB+
Short-term loan limits	1,164	469	[ICRANP] A4; downgraded from [ICRANP] A4+
Total	**1,453**	**1,238**	

** Instrument details are provided in Annexure-1*

Rating action

ICRA Nepal has downgraded the long-term loan rating of Jagdamba Cement Industries Private Limited (JCIPL or the company) to [ICRANP] LB+ (pronounced ICRA NP L B Plus) from [ICRANP] LBB+ (pronounced ICRA NP L double B plus) and also downgraded its short-term loan rating to [ICRANP] A4 (pronounced ICRA NP A four) from [ICRANP] A4+ (pronounced ICRA NP A four plus).

Rationale

The ratings downgrade is mainly on account of the sharp deteriorations in the company's operational and financial profile during FY2023 amid the major demand slowdown, which led to ~46% drop in revenues while the operating profit margins (OPM) depleted to 3.5% (8.4% in FY2022). This led to a significant moderation in the debt servicing and coverage indicators with DSCR of 0.5 times for FY2023 (1.3 times for FY2022) and total debt to OPBITDA of 20.6 times in FY2023 (4.8 times in FY2022). Amid the likely continuation of the weak demand outlook over the near to medium term, the pressure on the company debt coverage indicators is likely to accentuate further. JCIPL's liquidity profile has also witnessed major pressures with sustained overutilization of its drawing power amid the sharp elongation in working capital cycle. Incrementally, the company's margins will remain exposed to the inherent cyclicality in the cement industry, changing clinker price dynamics and the volatility in the interest rates, as seen in the recent years. Amid the challenging outlook, the promoters have not infused fresh funds into the company yet, which raises concerns given the expectations of liquidity pressures over the near to medium term. The company's ability to receive timely/adequate funding support from the promoters and the trends in its working capital intensity and debt coverage indicators would remain the key rating sensitivities.

Nonetheless, the ratings continue to factor in the company's experienced promoter profile, comprising of individuals from two major business houses of Nepal i.e. the Saurabh Group and the Shanker Group. The ratings also consider the company's long track record of operations (since 2001), its good brand recall, established sales channel and the experienced board/management team.

Key rating drivers

Credit strengths

Experienced promoters/management – The company is a part of the Saurabh/Shankar Group, with more than 25 years' experience in manufacturing construction materials, mainly cement and steel. Shankar Group's main unit, Jagdamba Steels, has been in the business of manufacturing structural steel since 1994. The Group's extensive track record and the experienced background of its promoters/management and the extensive sales/logistics network developed over the years, remains a positive. JCIPL derives a major chunk of its clinker requirements from the mine-based cement company of the Group viz. Sarbottam Cement Limited, which somewhat reduces the concern arising from the fact that JCIPL is a standalone grinding unit. The company has also entered into production facilities sharing agreement with Sarbottam Cement Limited (~19% of revenues during FY2023 was garnered from this arrangement), which has been generating higher margins compared to the margins in self-production.

Long track record in the industry – JCIPL has been in operation since 2001 and currently has a licensed grinding capacity of 1,000 tonnes per day (TPD). The company's operational profile remains supported by its long track record, established sales channel and brand name of "Jagdamba".

Credit challenges

Stretched financial profile – The company witnessed a sharp revenue degrowth of ~46% in FY2023, amid the industrywide demand slowdown triggered by the general economic slowdown. Amid the increasing competition, the sales realization also declined (by ~6%), while the direct costs were largely steady. This, along with major drop in sales volume led to sharp deterioration in OPM to 3.5% for FY2023 compared to 8.4% for FY2022. Amid the company's high reliance on bank borrowings (gearing of 3.0 times as of mid-July-2023), total debt to OPBITDA metrics weakened to 20.6 times for FY2023 (5.9 for FY2021). Hence, the company reported subpar debt servicing indicators with DSCR of 0.5 times for FY2023 (3.0 times in FY2021), which is likely to persist over the medium term as the demand outlook is expected to remain muted. Furthermore, the recent conversion of a part of its working capital loans to term loans (as required by the Central Bank's working capital guidelines) would be accentuating the impact, thus likely to necessitate sizeable promoter support.

Weak liquidity profile – JCIPL also reported a major spike in working capital intensity (net-working capital to operating income ratio) to ~50% from ~39% in 9MFY2022 (when last rated), mainly due to elongated debtor days (211 days in FY2023). While the absolute debtor volume has slightly declined, the drop has not been commensurate to the decline in revenue. The elongated working capital cycle has necessitated higher working capital debt (including permanent working capital loans) thereby resulting in overutilization of its drawing power, surpassing even the net current assets (~106% of net current assets as of mid-July 2023 as against ~86% of net current assets as of mid-April 2022, when last rated). The resultant weak liquidity profile hence remains a major rating concern.

Intense industry competition – The cement industry in Nepal is highly fragmented, also comprising of several large players (mainly the greenfield units) and hence JCIPL remains exposed to stiff competition from other large/established cement manufacturers/brands. The pricing flexibility has gradually lowered in the recent years as the capacity creation within the country is much higher than the current demand levels. Given the challenges in passing the increased cost to consumers (amid competitive pressure), any significant upward movement in input prices could further impact the company's margins.

Vulnerability to cyclicality and seasonal demand; risk of regulatory changes – The cyclical/seasonal nature of the cement industry creates uncertainty over demand and cash cycles for JCIPL. This may impact the company's capacity utilisation, revenues, and profit margins. Resulting volatility in cash flow could pose challenges, especially during the periods of weak demand, like the present. Moreover, the cement industry in Nepal remains protected from cheaper imports with duty safeguards and a substantial freight cost involved in the import of cement. Any changes in Government duty structure may have a bearing on the performance of the industry players. Any other regulatory change affecting raw material prices and availability could also impact the overall cement industry.

Link to the previous detailed rating rationale:
Rationale_Jagdamba Cement_BLR-Surveillance_June-2022

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

Link to the applicable criteria:
Corporate Credit Rating Methodology

About the company

Incorporated in February 2001, Jagdamba Cement Industries Private Limited (JCIPL) is involved in the production and sales of cement, with a licensed grinding capacity of 1,000 TPD. The shares of the company are held by seven individuals from two business houses of Nepal viz. the Shankar Group and the Saurabh Group. JCIPL produces Ordinary Portland Cement (OPC) and Pozzolana Portland Cement (PPC). Its factory is located at Gonaha VDC-07 in Bhairahawa District.

Key financial indicators

	FY2019 (Audited)	FY2020 (Audited)	FY2021 (Audited)	FY2022 (Audited)	FY2023 (Provisional)
Operating income-OI (Revenues in NPR million)	3,794	2,440	2,922	2,682	1,447
OPBDITA/OI (%)	7.7%	9.3%	6.8%	8.4%	3.5%
Total debt/Tangible net-worth-TNW (times)	2.2	2.4	2.3	2.2	3.0
Total outside liabilities/ TNW (times)	3.5	3.8	3.7	2.9	3.9
Total debt/OPBDITA (times)	3.1	5.1	5.9	4.8	20.6
Interest coverage (times)	2.5	2.5	3.5	1.8	0.4
DSCR (times)	2.3	2.4	3.0	1.3	0.5
Net-working capital/OI (%)	24%	39%	30%	33%	50%
Current ratio	1.1	1.1	1.0	1.1	1.1

Source: Company data

Annexure-1: Instrument Details

Instrument (Amount in NPR Million)	Last rated limit	Current rated limits	Ratings
Fund-based facilities, long-term loans (A)	**289**	**769**	**[ICRANP] LB+; downgraded from [ICRANP] LBB+**
Short-term Loan Limits (B)	**1,164**	**469**	[ICRANP] A4; downgraded from [ICRANP] A4+
Fund based; Overdraft	45	-	
Fund based; Trust receipt (TR)/ Short term demand loans	300	355	
Fund based; Cash Credit (CC)	800	95	
Fund based; TR (within CC)	(400)	-	
Non-fund-based; Letter of credit	12	12	
Non-fund-based; Bank guarantee	7	7	
Grand total (A+B)	**1,453**	**1,238**	

Analyst Contacts:

Mr. Sailesh Subedi (Tel No. +977-1-4519910/20)
sailesh@icranepal.com

Mr. Rajib Maharjan (Tel No. +977-1-4519910/20)
rajib@icranepal.com

Mr. Aslesh Adhikari (Tel No. +977-1-4519910/20)
aslesh.adhikari@icranepal.com

Relationship Contacts:

Ms. Barsha Shrestha (Tel No. +977-1-4519910/20)
barsha@icranepal.com

About ICRA Nepal Limited:

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For more information, visit www.icranepal.com

ICRA Nepal Limited,
Sunrise Bizz Park, 6th Floor, Dillibazar, Kathmandu, Nepal.
Phone: +977-1-4519910/20
Email: info@icranepal.com
Web: www.icranepal.com