# Shreenagar Agritech Industries Limited: [ICRANP-IR] B- and [ICRANP] LB-/A4 assigned

**December 28, 2023**

## Summary of rating action:

| Instrument* | Rated Amount (NPR million) | Rating Action |
|---|---|---|
| Issuer Rating | NA | [ICRANP-IR] B-; assigned |
| Long-term loan limits | 988 | [ICRANP] LB-; assigned |
| Short-term loan limits | 320 | [ICRANP] A4; assigned |
| **Total rated loan limits** | **1,308** | |

** Instrument details are provided in Annexure-1*

## Rating action

ICRA Nepal has assigned an issuer rating of **[ICRANP-IR] B-** (pronounced ICRA NP Issuer Rating B Minus) to Shreenagar Agritech Industries Limited (SAI or the company). Issuers with this rating are considered to have a high risk of default regarding timely servicing of financial obligations. The rating is only an opinion on the general creditworthiness of the rated entity and not specific to any debt instrument. ICRA Nepal has also assigned a long-term rating of **[ICRANP] LB-** (pronounced ICRA NP L B Minus) to the long-term loan limits of SAI and a short-term rating of **[ICRANP] A4** (pronounced ICRA NP A Four) to its short-term loan limits.

## Rationale

The assigned ratings are mainly constrained by the company's modest financial profile as evident from its high leverage levels and borderline debt servicing metrics. While the equity infusions during the last 12-15 months had led to slight moderations in SAI's leverage levels, sizeable term debt additions (mainly related to acquisition of poultry-based group company) during last two quarters, partially offset the impact. The company also faces integration challenges after the recent acquisition, marking the start of vertical integration of its feed manufacturing business, which has been rather sluggish after the pandemic. Given these challenges, along with the intense industry competition, the company's debt servicing metrics are likely to remain under pressure over the medium term, mainly factoring the added repayment burden associated with the recently converted permanent working capital loans. SAI's liquidity profile also remains stretched with significantly long working capital cycle and sustained overutilization of drawing power. ICRA Nepal also takes note of the one instance of delayed servicing of debt obligations by the company in last 12 months, albeit settled within August 2023 with regular repayments thereafter. Inherent risks associated with poultry industry (including risks of disease outbreaks like bird flu), volatility in revenue due to economic downturns, fluctuations in raw material prices, volatile realizations, and agro-climatic risks (for the feed manufacturing segment), also remains the rating concerns.

Nonetheless, the rating action factors in the company/promoters' long track record (around two decades) in the poultry-based businesses. The company's plans to diversify further into the value chain of the poultry industry could also result in operational synergies. The promoter's ability to infuse sizeable equity in last few years, along with the recent induction of strong institutional promoters also remains the rating positives. Going forward, the company's ability to overcome the integration challenges, attain adequate revenue/margins and improve its capitalisation/coverage and liquidity profile will remain the key rating sensitivities.

## Key rating drivers

### Credit Strengths

**Long track record of operations, with plans to have integrated presence in poultry industry** – The company has been in the feed manufacturing (mostly pellet feed) industry since 2004 and its promoters also have presence in other verticals of the poultry industry, through separate companies. The company recently acquired the entire assets of its sister concern viz., Shreenagar Agro Farm (SAF), which was in the core poultry business. SAF utilised the proceeds to settle its debts, after which the entire company was acquired by SAI, for poultry licensing purposes. The company has plans to further diversify into the entire value chain of the poultry industry to hatchery, cold storage, meat processing and distribution, etc., which could provide diverse revenue growth prospects.

**Recent equity infusions and entry of strong institutional promoters** – SAI has increased its equity base by ~3.9 times from mid-July 2022 till December 20, 2023, majority of which was injected by the existing promoters. Additionally, SAI has also been able to recently inbound strong institutional promoters like Shikhar Insurance Company Limited (rated at [ICRANP-IR] A+ with ~11% stake in SAI) and Citizen Life Insurance Company (rated at [ICRANP-IR] BBB with ~6% stake), which also remains a positive.

### Credit challenges

**Modest financial profile** – The company's working capital cycle has remained significantly stretched over the years, which has increased its reliance on debt. This has led to high leverage levels (total outsider liabilities to net worth of 3.5 times as of mid-October 2023) despite recent equity injections. Though the company's operating profit margins (OPM) has generally remained progressive, recent term debt additions have led to stretched total debt to OPBDITA of ~7 times and borderline DSCR of 1.0 time for Q1FY2024. The company's ability to significantly scale-up its revenues, while maintaining or improving the OPM as reported in Q1FY2024, will remain crucial for its incremental financial profile.

**Stretched liquidity profile** – SAI has reported a gradual spike in working capital intensity (net working capital to operating income ratio) over the years, which stood significantly elevated at ~82% for Q1FY2024, amid the general economic slowdown/tight liquidity scenario. Given the weak internal accruals and sizeable fund blockage in form of working capital, liquidity pressures have mounted in the recent quarters, as evident from the sustained overutilisation of drawing power from mid-April 2023 onwards (range of 102-105%, including the permanent working capital loans). The stretched liquidity profile had also led to inability in timely serve the interest obligations which were due on mid-July 2023 (albeit regularised in August 2023 through equity infusions and slight improvement in revenue and working capital cycle). Going forward, incremental trends in working capital cycle, any fluctuations in raw material prices and interest rate volatility could impact its liquidity profile.

**Financial and operational challenges after the recent acquisition of poultry-based group unit** – The company incurred ~NPR 800 million towards acquisition of SAF, which was ~75% debt funded. Additionally, the acquisition also brought in accumulated losses of NPR 366 million into the books of SAI, which offset the impact of recent equity infusions, thus leading to increased leverage levels in Q1FY2024. Furthermore, the company will be facing operational integration challenges regarding the diversification of business into new vertical. Though the recent acquisition has reflected in improved revenue trajectory and higher margins during Q1FY2024, sustainability of the same remains to be seen.

**High competition and fragmented industry** – The feed manufacturing and poultry industry remain characterised by the presence of many players and hence remains highly competitive. The industry also has many unorganised localised players resulting from low entry barriers and low complexity of the work involved. These factors not only limit the pricing flexibility but also keep the capacity utilisation (very weak at ~9-10% during last two fiscals) and profit margins in check for the overall industry, including SAI. Amid the intense competition, the company's high reliance on the top-10 customers (~55% of FY2022 revenues) also remains a rating concern.

**Inherent risk in the poultry sector** – The poultry industry is exposed to inherent risks such as diseases outbreak (bird flu, *ranikhet,* etc.), relatively unpredictable output and volatile realisations, which can fluctuate the financial profile of the players in the industry, including SAI. The company's ability to withstand these circumstances would remain crucial for sustainable business performance. SAI's margins also remains sensitive to the prices of raw material (maize, soya, etc.) used in feed production. While the increased raw material prices used to be partly absorbed in the finished good (feed) pricing so far, the margins would now remain exposed to pricing trends of chicken meat/eggs, considering the company's forward integration plans. The company's margins are also susceptible, given the industry fragmentation and multiple competitors.

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

**Links to applicable criteria:**
Corporate Credit Rating Methodology
Issuer Rating Methodology

## About the company

Incorporated in November 2004 and converted into a public limited company in June 2023, Shreenagar Agritech Industries Limited (SAI) has been producing and supplying feed for segments like poultry, cattle and aquaculture farmers/entrepreneurs throughout the country. The company produces three types of feeds viz., mash, pellet and extruded. Sunaulo is the brand name for poultry and cattle feed, whereas Himdana is the brand name for fish feed. At present, SAI has the production capacity of 135,780 metric tonnes per annum at its Rupandehi-based plant. With the recent acquisition of poultry unit of the group, the company has expanded its business vertical into this segment as well, with plans for further vertical expansion. SAI's major promoters include Mr. Satish Chandra Shrestha and family members/associated companies with joint stake of ~66% as of December 20, 2023, along with recent induction of promoters like Shikhar Insurance Company Limited (~11% stake) and Citizen Life Insurance Company (~6% stake), among others.

## Key financial indicators

| Amounts in NPR million | Audited | | | | | Provisional |
|---|---|---|---|---|---|---|
| | FY2019 | FY2020 | FY2021 | FY2022 | FY2023 | Q1FY2024 |
| Operating income-OI (Revenues in NPR million) | 1,259 | 886 | 668 | 785 | 808 | 275 |
| OPBDITA/OI (%) | 7.0% | 7.0% | 9.5% | 9.1% | 10.5% | 16.3% |
| Total debt/Tangible net-worth-TNW* (times) | 5.8 | 7.8 | 3.3 | 2.8 | 2.3 | 2.6 |
| Total outside liabilities/ TNW (times) | 7.5 | 10.4 | 4.5 | 3.8 | 2.6 | 3.5 |
| Total debt/OPBDITA (times) | 6.4 | 10.6 | 10.0 | 8.8 | 10.8 | 6.7 |
| Interest coverage (times) | 1.5 | 1.2 | 1.5 | 1.3 | 1.3 | 1.2 |
| DSCR (times) | 1.2 | 0.9 | 1.1 | 1.1 | 1.0 | 1.0 |
| Net-working capital/OI (%) | 33% | 58% | 91% | 81% | 104% | 82% |

*Source: Company data*

** TNW as of mid-October 2023 is excluding the revaluation reserves of NPR 336 million, added after acquisition.*

## Annexure-1: Instrument details

| Instrument (Amounts in NPR Million) | Rated Amount | Rating Action |
|---|---|---|
| **Long-term loan limits (A)** | **988** | **[ICRANP] LB-**; assigned |
| Fund-based facilities; Term Loans (including proposed limits) | 988 | |

| Instrument (Amounts in NPR Million) | Rated Amount | Rating Action |
|---|---|---|
| | | |
| **Short-term loan limits (B)** | **320** | **[ICRANP] A4**; assigned |
| Fund based; Overdraft | 100 | |
| Fund based; Short term loan | 45 | |
| Non-Fund-based; Letter of credit | 175 | |
| | | |
| **Total bank loan limits rated (A+B)** | **1,308** | |

## 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

## Relationship Contacts:

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

## About ICRA Nepal Limited:

ICRA Nepal Limited, the first credit rating agency of Nepal, is a subsidiary of ICRA Limited (ICRA) of India. It was licenced by the Securities Board of Nepal (SEBON) on October 3, 2012. ICRA Nepal is supported by ICRA Limited through a technical support services agreement, which envisages ICRA helping ICRA Nepal in areas such as rating process and methodologies, analytical software, research, training, and technical and analytical skill augmentation.

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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