Nepal Shalimar Cement Private Limited: Ratings reaffirmed and removed from ‘Issuer Not Cooperating’ category

June 03, 2024

Summary of rating action

Instrument (Amounts in NPR million)*	Last rated limits	Current rated limits	Rating Action
Long-term loan limits	276	740	[ICRANP] LB; reaffirmed and removed from ‘Issuer Not Co-operating Category’
Short-term loan limits	1,330	780	[ICRANP] A4; reaffirmed and removed from ‘Issuer Not Co-operating Category’
Total	**1,606**	**1,520**	

** Instrument details are provided in Annexure-1*

Rating action

ICRA Nepal has reaffirmed the long-term rating of Nepal Shalimar Cement Private Limited (NSCPL) at [ICRANP] LB (pronounced ICRA NP L B) and also reaffirmed the company’s short-term loan rating at [ICRANP] A4 (pronounced ICRA NP A four). The ratings have also been removed from ‘Issuer Not Cooperating’ category.

Rationale

The ratings are mainly constrained by the company’s weak operational and financial profile amid the major demand slowdown leading to ~47% drop in revenues during FY2023, while the operating profit margins (OPM) depleted to negative 2.9% from 6.6% in FY2022. This has further weakened the company’s capitalisation profile with gearing of 10.7 times as of mid-July 2023. The company’s liquidity profile also continues to remain under pressure with sustained overutilization of drawing power (~258% as of mid-July 2023) amid the sharp elongation in working capital cycle. Revenue degrowth and margin pressures has led to the company reporting sub-par debt service coverage indicators, and the shortfall were mainly met through increase in extent of overdrawing of drawing power (in absolute amount as well), despite the reduction in net working capital amount. 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 and hence timely/adequate funding support from promoters will remain crucial to ensure debt servicing. Any deviation vis-à-vis this assumption would have a downward pressure over the ratings. The company’s margins will also 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. The company’s debt servicing track record and the overall trends in its revenue, margin, 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 the Shalimar Group, which has established traction in manufacturing and selling of construction materials, among others. The ratings also consider the company's long track record of operations (since 2003) and its established sales channel.

Key rating drivers

Credit strengths

Long track record; experienced promoters/management – NSCPL has been in operation since 2003 and currently has a grinding capacity of ~0.5 million metric tonnes per annum (MTPA). It has developed adequate sales/logistics network over the years. The company is promoted by individuals from the Shalimar Group which has a long experience in manufacturing and selling construction materials (since 1940s).

Credit challenges

Stretched financial profile – The company witnessed sustained revenue degrowth at ~16% in FY2022 and ~47% in FY2023, amid the economic slowdown impacting the industry-wide demand in the highly fragmented sector. The reduced scalability, along with rise in clinker prices in FY2023 and the competition restrained commensurate decrease in cement realisations, led to the company reporting negative OPM of 2.3% for FY2023 as compared to 6.6% in FY2022. Amid this backdrop, the company's high reliance on bank borrowings and elevated interest costs over the years have depleted the company's net worth leading to elevated gearing levels of 10.7 times as of mid-July 2023. The company reported subpar debt servicing indicators with DSCR of 0.3 times for FY2023. However, significantly overdrawn working capital loans (working capital loan utilization was ~NPR 1,188 million as of mid-July 2023 as against ~NPR 1,104 million as of mid-July 2022, while the net current assets declined to ~NPR 554 million, from ~NPR 794 million over the same time) have aided in timely servicing of repayment obligations. The pressure in coverage indicators is likely to persist over the medium term as the demand outlook is expected to remain muted, thus likely to necessitate sizeable promoter support.

Weak liquidity profile – The company's working capital intensity (net-working capital to operating income ratio) has remained high over the years, with it increasing further to ~53% in FY2023 from ~31% in FY2021. The increase was mainly on account of elongated debtor days (176 days in FY2023). While the absolute debtor volume has slightly declined, the drop has not been commensurate to the decline in revenues. The elongated working capital cycle has necessitated higher working capital debt (including permanent working capital loans) thereby resulting in high overutilization of its drawing power, (~268% as of mid-July 2023 as against ~174% as of mid-July 2022). The resultant weak liquidity profile hence remains a major rating concern.

Intense industry competition – The cement industry in Nepal is highly fragmented, comprising of several large players (mainly the greenfield units) and hence NSCPL remains exposed to stiff competition from the large/established cement manufacturers/brands, which have been added in recent years. Accordingly, the pricing flexibility has gradually lowered over the 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 NSCPL. 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 rating rationale:

Rationale_Nepal Shalimar Cement_INC_BLR_November_2023

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 August 2003, Nepal Shalimar Cement Private Limited (NSCPL) is involved in the production and sales of cement, with current installed grinding capacity of 545,000 MTPA. The entire shares of the company are held by five individuals from the Shalimar Group. NSCPL produces Ordinary Portland Cement (OPC) and Pozzolana Portland Cement (PPC) under seven brands each and Portland Slag Cement (PSC) under eight brands. Its factory is located at Pipra, Simara in Bara district of Nepal.

Key financial indicators

	FY2019 (Audited)	FY2020 (Audited)	FY2021 (Audited)	FY2022 (Audited)	FY2023 (Audited)
Operating income-OI (Revenues in NPR million)	2,851	2,248	2,450	2,063	1,099
OPBDITA/OI (%)	5.9%	5.9%	2.9%	6.6%	-2.9%
Total debt/Tangible net-worth-TNW (times)*	1.9	2.6	3.1	4.4	10.7*
Total outside liabilities/ TNW (times)	2.8	3.3	4.0	5.1	11.4
Total debt/OPBDITA (times)	7.4	10.8	19.1	10.5	-43.6
Interest coverage (times)	1.7	0.9	0.6	0.9	-0.2
DSCR (times)	1.3	0.7	0.4	0.6	0.3
Net Working Capital/OI (%)	27%	42%	31%	39%	53%
Current ratio	0.9	0.9	0.8	0.7	0.8

**Excluding revaluation reserves*

Source: Company data

Annexure-1: Instrument Details

Instrument (Amounts in NPR Million) *	Last Rated Amount	Current Rated Amount	Rating Action
Long-term loan limits (A)	**276**	**740**	[ICRANP] LB reaffirmed and removed from 'Issuer Not Co-operating Category'
Fund based; Term Loan, Hire Purchase Loans and Permanent Working Capital Loans	276	740	
Short term loan limits (B)	**1,330**	**780**	[ICRANP] A4; reaffirmed and removed from 'Issuer Not Co-operating Category'
Fund-based facilities; Overdraft/ Cash Credit Loan	15	165	
Fund-based facilities; Demand Loan	100	-	
Fund-based facilities; Trust Receipt (TR)/Short term loan/ Demand Loan	1,200	600	
Non-fund based; Letter of credit (within TR)	(1,200)	(600)	
Non-fund based facilities; Bank guarantee	15	15	
Grand total (A+B)	**1,606**	**1,520**	

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About ICRA Nepal Limited:

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