

PRESS RELEASE

SONAPUR MINERALS AND OIL LIMITED

November 2022

Rating

Instrument	Amount (NPR. Mn)	Ratings	Rating Action
Issuer Rating	NA	IRN BBB- (Is)	Assigned

Infomerics Credit Rating Nepal Limited (Infomerics Nepal) has assigned the issuer rating of IRN BBB- (Is) [Triple B Minus (Issuer)]. Issuers with this rating are considered to have the moderate degree of safety regarding timely servicing of financial obligations. Such issuers carry moderate credit risk.

Detailed Rationale

The issuer rating assigned to Sonapur Minerals and Oil Limited (SMOL) derive strength from experienced promoters and management team with long track record of operations, moderate capacity utilization supported by the increase in production resulting moderate financial risk profile. The rating also factors in the backward integration secured by adequate limestone reserves and proximity of the project to raw material sources. These rating strengths are partially offset by implementation & stabilization risk associated with the enhanced capacity, high sales concentration, risk of regulatory changes, susceptibility to volatility in input costs and realizations as well as cyclical & seasonality in cement industry. Going forward, the ability of the company to ramp up its operation with timely realization of envisaged benefits from enhanced project while improving its capacity utilization and managing its raw material price fluctuation remains crucial. Also, the company's ability to strengthen its capitalization and coverage indicators with successfully raising of its Initial Public Offering (IPO) at a planned premium level will remain a key rating sensitivity.

Detailed Description of Key Rating Drivers

Key Rating Strengths

Experienced promoters and management team with long track record of operations

SMOL has an operational track record of more than 14 years in cement manufacturing. SMOL is promoted by industrialists and traders of Nepal along with other shareholders. Mr. Ratanlal Tayal is the Chairman of the company with more than 38 years in business with involvement in varied sector. The promoters are also involved in other business of rosin and turpentine followed by trading of cycles, papers, cosmetics, fiber cables, etc. Further, the promoters are supported by a team of technically qualified and experienced professionals to run the day-to-day operations of the company.

Backward Integration; secured by adequate limestone reserves and proximity of the project to raw material sources

SMOL's operating efficiency remain supported by the backward integration in the form of captive limestone mines located at the proximity to the factory site. SMOL currently has a mining license for two limestone mines which is at the distance of ~38 kms from its existing clinker plant. The two Promoter companies have one mining license each and total estimated reserve of all four mines including Promoter companies is 34.61 Mn MT and these license are granted for a maximum period of 25 years by the Department of Mines and Geology. The estimated aggregate deposits of all the mines (including Promoter's) taken together is expected to further boost the operational profile of the company going forward.

Moderate capacity utilization supported by increase in production of cement

Capacity utilization for clinker stands at ~58% and cement stands at ~53% in FY22. Company has increased its production of cement by ~26% in FY21 over FY20 and further increased by ~50% in FY22 over FY21 with the increase in installed capacity of grinding unit. The company's ability to ramp up its operation with timely realization of envisaged benefits from enhanced project remains to be seen.

Moderate financial risk profile

SMOL's financial profile is marked by relatively stable operating margin with moderate coverage indicators as reflected in the EBITDA margin of 18.98% and interest coverage of 2.31x in FY22. The total operating income (TOI) of the company had increased by ~9% in FY21 to NPR 2,922 Mn which however has declined in FY22 to NPR 2,375 Mn. This was majorly on account of temporary shutdown of plant for necessary expansion related activities. Also, it was impacted by the pandemic and liquidity constraint induced demand slowdown affecting the average price realizations given the intense competition. Though the overall gearing ratio has slightly deteriorated to 2.10x in FY22 vis-à-vis 1.89x in FY21 along with the working capital utilization remaining on the higher side at ~99% during FY22, it still remains supported by the improvement in tangible net worth with plough back of profit into the business. The coverage indicators remain moderate with interest coverage of 2.31x and debt service coverage ratio of ~1.24x in FY22, which is further expected to improve on account of expected IPO proceeds.

Key Rating Weaknesses

Project implementation risk and stabilization risk

SMOL's capacity enhancement of grinding unit from 2,300 TPD has already been completed in February 2022 and capacity of clinker unit has increased from 1,000 TPD to 1,250 TPD in August 2020. SMOL has already tied up for NPR 2,512 Mn (i.e. 84% of total debt for the project) as on mid-November 2022, while the remaining is still open for participation. Although, the majority of capital expenditure has been completed, the company is still exposed to the risk associated with project implementation and satisfactory operations thereafter.

Vulnerability to cyclical trend and seasonal demand; risk of regulatory changes and raw material price volatility

The cement industry is highly cyclical in nature and depends largely on the economic growth of the country. Hence, the company is exposed to cyclical trends in supply and demand in the industry, impacting the capacity utilisation, revenues and margins. Also, the construction and development expenditures are largely carried out in a specific season impacting the overall demand of the cement in Nepal. Moreover, cement industry in Nepal are also benefitted by the high custom levied on import, also being a volumetric production, transportation cost also remains high. Hence, any changes in the government regulations will have a huge impact on overall cement industry. SMOL expects to meet 100% of its clinker requirements from its own clinkerization unit. Apart from clinker, the company procures iron ore, clay, fly ash, coal, gypsum etc. which are all dependent on the market and hence any volatility in the price has a direct bearing on profitability of the company. Therefore, any significant increase in the cost of input materials is likely to have an impact on the industry's overall margins.

High sales concentration

SMOL's sales concentration has increased in recent years with top 10 customers contributing ~54% of total sales in FY22 compared to ~45% in FY21. Further, ~18% of total sales was made from single customer during FY22, leading to higher customer concentration risk.

Intense competition in the Industry

Generally, the large cement producers with high brand recognition dominate the market. Due to the presence of large number of organized and unorganized players, the pricing power of the new entrants remains low, affecting the profitability amid competition. Currently there are more than 60 cement industry and more than 20 clinker manufacturing units operating in Nepal, with many additional units in a pipeline. Together with the new upcoming units and existing units after capacity expansion, is expected to reduce the pricing flexibility going forward.

Analytical Approach: Standalone

Applicable Criteria:

[Issuer Rating Methodology](#)

About the Company:

Incorporated in June 2008, Sonapur Minerals and Oil Private Limited was later converted to Sonapur Minerals and Oil Limited (SMOL) in July 22, 2022. The company is presently engaged in manufacturing and selling OPC under the brand name “Sona Cement” and PPC under the brand name “Sona Shree Cement”. The business operation of the company is managed by its Managing Director, Mr. Nipesh Tayal.

Financial Indicators (Standalone)

For the year ended* As on	FY20	FY21	FY22
	Audited	Audited	Audited
Total Operating Income (in NPR Mn.)	2,669	2,922	2,375
EBITDA Margin (%)	23.38	22.40	18.98
Interest Coverage Ratio (x)	2.00	3.48	2.31
Current Ratio (x)	0.87	0.87	0.76
Overall Gearing Ratio (x)	2.03	1.89	2.10

*Classification as per Infomerics Nepal standards

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