

Agni Incorporated Private Limited: [ICRANP] LA/ A1 (Assigned)

January 21, 2019

Summary of rated instruments

Instrument*	Rated Amount (NPR Million)	Rating Action
Short-term loans; Fund-based	4,202	[ICRANP] A1 (Assigned)
Long-term loans; Fund-based	(50)	[ICRANP] LA (Assigned)
Short-term loans; Non-fund based	4,040	[ICRANP] A1 (Assigned)
Total	8,242	

* Instrument details are provided in Annexure-1

Rating action

ICRA Nepal has assigned the long-term rating of [ICRANP] LA (pronounced ICRA NP L A) to the NPR 50-million long-term loans of Agni Incorporated Private Limited (AIPL or the company). ICRA Nepal has also assigned the short-term rating of [ICRANP] A1 (pronounced ICRA NP A One) to the short-term loans (including non-fund-based limits) of AIPL.

Rationale

The rating assignment factors in the company's long track record (>25 years) in the Nepalese automobile dealership industry and strong market positioning in the utility vehicles (UV) segment. The rating also takes into consideration AIPL's healthy sales growth trend, supported mainly by a strong demand for UV segment. The rating also takes comfort from the company's robust return indicators, comfortable capital structure and coverage indicators (interest cover of ~17x in FY2018).

The ratings, however, are constrained by the intense competitive pressures in the industry with the presence of many established players/brands. ICRA Nepal also takes note of AIPL's high dependence on top two models, which together accounts for over 90% of total sales. The ratings are also constrained by the recent increase in taxes for the passenger vehicle (PV) segment, along with the reduced regulatory cap on bank financing at 50%, which could slowdown demand growth. Moreover, the increasing cost of bank borrowings and slowdown in loan disbursements could deter prospective customers. The dealership business itself is characterised by high working capital intensity and hence the recent increase in interest rates across the banking sector might impact AIPL's profitability and debt coverage indicators. Going forward, AIPL's ability to diversify its revenue streams while sustaining growth and profitability along with judicious working capital management, will remain the key rating sensitivities.

Key rating drivers

Credit strengths

Established track record and strong market presence - AIPL is the sole authorised dealer of utility/passenger vehicles (part of PV segment), pickups (part of commercial vehicle (CV) segment) and tractors of Mahindra & Mahindra Limited for Nepal since 1991. Established track record and strong brand recall has resulted in strong market positioning for AIPL, especially in the UV/pickup segment. The demand basically emanates from the suitability of these vehicles for the Nepalese geography, durability, competitive pricing and low range of competing models. AIPL has adequate presence across the country through five own showrooms and 22 regional dealership outlets with ~60% of AIPL's total sales coming from these dealers in the last two fiscals.

Healthy sales growth and sizeable revenue base - AIPL was able to post healthy sales growth from FY2013 to FY2017 (CAGR 42%) which has led to a sizeable revenue base of ~NPR 16 billion for FY2017. However, FY2018 sales witnessed slight decline by ~1% mainly due to the tightening liquidity in the banking sector. In FY2018, the CV segment dominated the sales (~48%), followed by PVs (~47%) and tractors (~5%). Increasing development activities across the country

remains a positive for demand in CV segment. AIPL has reported significant sales growth in Q1FY2019 (~37% annualised growth). The sustainability of the same would remain a key monitorable.

Comfortable financial profile - AIPL's healthy operating margins (~14% for FY2018) results in strong coverage indicators with gearing of 0.2x as of mid-July 2018 and interest cover of ~17x during FY2018. Because of moderation in demand due to the tight liquidity in the banking system and adverse regulatory measure like increase in import taxes, the revenue growth is likely to remain muted and there could be moderation in operating margins. However, coverage indicators and capital structure are expected to remain at comfortable level. ICRA Nepal expects leverage to remain below 0.4x times over next two years.

Credit challenges:

Intense competitive pressure – The automobile dealership industry is highly fragmented with stiff competition from dealerships of incumbents like TATA (from TATA Motors Limited), Maruti Suzuki and Hyundai among others. Apart from the strong presence in pickup/UV variants, AIPL has limited market presence in other vehicle segments which remains an area of concern in terms of diversity of revenue streams.

Working capital intensive operations - Being a working capital-intensive industry, short-term working capital loans account for almost AIPL's entire debt. Given the expected increase in inventory holding period, the overall working capital requirement is expected to increase in the near to medium term which will result in moderation of coverage indicators. This is also evident from the elongated working capital cycle in recent periods (79 days for Q1FY2019 as against 53 days for FY2017) leading to higher working capital debt. Moreover, rising interest rate will also have bearing on net profitability of the company.

Increased taxes, reduced bank financing ratio and increasing borrowing rates could impact demand growth – The PVs have been a highly taxed commodity in Nepal with further sharp tax increment for FY2019. Additionally, a reduced loan to vehicle value (LTV) on bank financing at 50%¹ by the banking sector regulator could also deter prospective customers. Since PV sales are mostly bank financed, slower loan disbursements amid the current tight liquidity conditions in banking could impact sales growth. Moreover, bank interest rates have increased swiftly in the last two years, which, coupled with the inherent cyclicity in automotive demand, could constrain the revenue growth for AIPL. Nonetheless, AIPL's sales are CV-dominated, where revised tax and reduced bank financing norms are not applicable, which provides some comfort. The relatively low extent of impact in the CV segment is also evident from high sales growth in this segment in Q1FY2019 (57% volume growth) while PV segment reported 8% volume decline over the same period.

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

Links to applicable criteria:

[Corporate Credit Rating Methodology](#)

About the company

Incorporated in 1991, Agni Incorporated Private Limited (AIPL) is the sole authorised dealer of Mahindra automotive products (utility vehicles, passenger vehicles and tractors) for Nepal. Mr. Cabinet Shrestha, Ms. Susan Vaidya Shrestha and Mr. Arjun Prasad Sharma are the shareholders as well as the directors of the company. AIPL has its presence across the country through an extensive network comprising five showrooms/sales outlets of its own (four within Kathmandu valley and one in Birgunj) and 22 regional dealership outlets.

¹ 50% introduced in March 2017 vs. no caps earlier; later moderated to 65% in August 2017; now again reduced to 50% from October 2018.

Key financial indicators

	FY2016 (Audited)	FY2017 (Audited)	FY2018 (Provisional)	Q1FY2019 (Provisional)
Operating income-OI (NPR million)	13,363	16,375	16,259	5,555
Profit after tax (NPR million)	1,294	1,593	1,595	445
OPBDITA/OI (%)	14.0%	14.1%	14.0%	11.4%
Total debt/Tangible net-worth-TNW (times)	1.4	0.3	0.2	0.5
Total outside liabilities/ TNW (times)	2.0	0.7	0.4	0.6
Total debt/OPBDITA (times)	1.6	0.4	0.4	0.8
Interest coverage (times)	15.8	12.7	16.9	16.2
DSCR (times)	12.1	8.1	5.3	10.8
Net-working capital/OI (%)	28%	15%	21%	23%

Source: Company data

Annexure-1: Instrument Details

Instrument	Limit (Amount in NPR Million)	Rating Action
Non-fund based facilities, Short-term		
Letter of credit - LC	3,890	[ICRANP] A1
Bank Guarantee - BG	150	[ICRANP] A1
LC (within Demand loan - DL)	(900)	[ICRANP] A1
BG (within DL and LC)	(150)	[ICRANP] A1
Total non-fund based (A)	4,040	
Fund-based facilities, Short-term		
Trust receipt loans - TR loans	1,800	[ICRANP] A1
Demand loans – DL	1,150	[ICRANP] A1
Local bills purchase	1,252	[ICRANP] A1
TR loans (within LC)	(2,501)	[ICRANP] A1
Short-term loans (within LC and DL)	(1,300)	[ICRANP] A1
Overdraft (within LC)	(30)	[ICRANP] A1
Local bills purchase (within LC and DL)	(900)	[ICRANP] A1
Fund-based, Long-term – Hire purchase loans (within DL)	(50)	[ICRANP] LA
Total fund-based (B)	4,202	
Grand total (A+B)	8,242	

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About ICRA Nepal Limited:

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