

Rating Rationale

Motidan Construction Sewa Private Limited

Rating

Facility	Amount (Rs. In Million)	Rating ¹	Rating Action
Long Term Bank Facilities	283.00	CARE-NP BB [Double B]	Assigned
Short Term Bank Facilities	1,867.00	CARE-NP A4 [A Four]	Assigned
Total Facilities	2,150.00		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has assigned rating of ‘CARE-NP BB’ to the long term bank facilities and ‘CARE-NP A4’ to the short term bank facilities of Motidan Construction Sewa Private Limited (MCS).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of MCS are constrained by leveraged capital structure, debt funded capex plan of the company, tender based nature of operations in highly competitive construction industry, working capital intensive nature of business and exposure to volatile interest rate. The ratings, however, derives strength from experienced promoters & management in related field, established track record in executing diverse construction projects, healthy order book position with mid-term revenue visibility and ownership of sizable equipment. The ratings also factored in financial risk profile marked by growth in the revenue, profitability and satisfactory debt service coverage indicators, moderate counter party risk and escalation clause in majority of the contracts.

Ability of the company to successfully execute projects in time and recover contract proceeds; and ability of the company to manage healthy revenue growth and maintain profitability margins without deterioration in its financial risk profile will be key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Tender based nature of operations in highly competitive construction industry

The company receives its work orders from government departments and private entities with majority of works from government contracts. The contracts are tender-based and the revenues are dependent on the company’s ability to bid successfully for these tenders. The promoters’ long industry experience of 10 years mitigates risk of competition to some extent. Also, there are numerous fragmented and unorganized players operating in this industry which makes the civil construction space highly competitive and the ability of MCS to maintain its profitability margins and growth in future remain crucial. Further, the business also remains dependent on stability in government policies and fiscal position of the government.

¹Complete definitions of the ratings assigned are available at www.careratingsnepal.com

Leveraged capital structure and debt funded capex plan of the company

The capital structure of the company is leveraged with debt equity ratio of 2.69x and overall gearing ratio of 3.08x at the end of FY18 on back of term loans availed for purchase of equipment/ machinery and unsecured loan taken from promoter and others during FY18. The debt equity ratio and overall gearing ratio were 4.44x and 4.77x at the end of FY17. The company has been making regular investments to expand its infrastructure facilities in the past and expected to continue in future. The investment in equipment/ machinery increased by ~14% in FY18 as compared to ~77% in FY17. Purchase of fixed assets was mainly funded through bank finance resulting in increase of debt component. It is projected that the company will take additional loan of Rs. 460 Mn in short period, on account of purchase of equipment/machinery for the new projects proposed to be undertaken and for meeting its working capital requirements.

Working capital intensive nature of business

The operations of the company are working capital intensive in nature. MCS works with the government departments as well as private companies, payments for the contracts are received within 2-3 months generally. The credit period extended by suppliers of raw materials is on the basis of negotiation power of the company. Retention money of MCS was Rs. 20 Mn in FY18 as compared to Rs. 9 Mn in FY17. These factors lead to reliance of the company on bank finance to meet its working capital requirements. The average working capital utilization of the company was at a high level of ~93% for the last 12 months ending mid-March 2019.

Exposure to volatile interest rates

Nepalese banking sectors are fixing lending interest rate based on quarterly base rate and interest rate will be changed accordingly on quarterly basis. Due to tight liquidity in the market, the interest rate has been high and volatile during the last 12 months. Therefore, funding from Bank and Financial Institutions is exposed to volatile interest rate.

Key Rating Strengths***Experienced promoters & management team in the related field***

MCS is being promoted by Mr. Ram Bahadur Gautam and his family members holding 100% of total shares. Mr. Ram Bahadur Gautam, managing director, has extensive experience of more than 15 years in the field of construction business. Mr. Bikram Gautam, assistant managing director, is involved in the company for the past 4 years and is looking after the project procurement, financial and technical analysis. Further, the board is supported by experienced team across various functions.

Established track record in executing roads, bridges, buildings, irrigation works, and mining projects

MCS has an established track record of over 10 years in the construction of roads, bridges, cross drainage works, buildings, canals, and mining and transportation of Limestone projects and have executed several projects across the country in different terrains. The long track record has enabled the company to establish relations with its

customers thereby resulting into repetitive orders/ tenders from the government departments as well as private entities.

Healthy order book position with mid-term revenue visibility

MCS has executed contracts with aggregate contract value of Rs. 2,097 Mn till mid-March 2019 since its inception. As on mid-May 2019, the order book of the company amounts to Rs. 2,508 Mn (yet to be executed). Due to government initiative towards infrastructure projects, order book of the company is expected to increase in future. The order book of the company reflects revenue visibility for the next 2-3 years.

Ownership of sizable equipment

MCS has built up adequate asset base to execute its projects with total fixed asset of Rs. 404 Mn at the end of FY18. Efficient deployment of the resources and investment in machinery during the past years has helped in timely execution of projects and acquisition of new projects. The major equipment/ machinery of the company comprises of tipper/ truck, excavator, building equipment sets, canal equipment, loader, soil compactor, motor grader etc. which are essential for the construction projects.

Financial risk profile marked by growth in the revenue, profitability and satisfactory debt service coverage indicators

Financial risk profile of MCS is comfortable with increasing scale of operations and cash accruals during FY18. Consolidated total revenue of the company increased from Rs. 513 Mn in FY17 to Rs. 617 Mn FY18 (~20% growth Y-o-Y) due to increase in number of additional projects undertaken by MCS and execution of the same. The company has satisfactory total debt to gross cash accruals and interest coverage of 3.37x and 3.06x respectively in FY18 though it declined from 4.35x and 5.36x respectively in FY17. The company has healthy PBILDT margin which was 23.68% in FY18 as compared to 21.01% in FY17. During 9MFY19 (refers to 9 months' period ended mid-April 2019), total revenue of the company was Rs. 899 Mn with PBILDT margin of 10.58% and PAT margin of 1.44%. Till June 5, 2019, MCS has booked total consolidated revenue of Rs. 1,252 Mn.

Moderate counter party risk

Major revenue of MCS is generated from government contracts related to road works, building works, irrigation works etc. Payment of dues are generally realized within 2 to 3 months. The counter party risk is moderated by the fact that major contracts are obtained from government departments and it has been making timely payment to the company in past. MCS also generates revenue through contracts received from private companies majorly related to mining works such as excavation, collection and transportation of limestone and the payments are received in a timely manner.

Escalation clause in majority of the contracts

MCS procures its raw materials mainly from the local vendors which has risk of volatility in raw material prices. The company has inbuilt price escalation clauses in majority of contracts in order to insulate the company from any adverse fluctuation in raw material prices and labor expenses. Ability of the company to pass on increased price burden to the customers in a timely manner and maintain profitability margins is critical from credit perspective.

About the Company

MCS, incorporated in March 03, 2009 and based in Kathmandu, is a mid-scale construction company in Nepal. The company is promoted by Mr. Ram Bahadur Gautam and his family members with over 15 years of experience in civil construction business. The company is mainly involved in mining works, construction of roads, bridges, building, irrigation works etc. across Nepal. MCS also enters into joint venture (JV) with other companies in order to meet the eligibility criteria for the projects. The consolidated revenue of the company includes revenue from JV entities in proportion of the company’s stake in the JV.

Analytical approach:

CRNL has analyzed MCS’s credit profile by considering the consolidated financial statements (comprising MCS and its JV entities related to the construction works) owing to financial and operational linkages between MCS and JV entities. Brief financials of MCS for last three years ending FY18 and 9MFY19 are given below:

Brief Consolidated Financials (Rs. Million)	FY16	FY17	FY18	9MFY19
	(Audited)	(Audited)	(Audited)	(Provisional)
Income from Operations	224	513	617	899
PBILDT	54	108	146	95
PAT	11	19	24	13
Overall Gearing	2.17	4.77	3.08	3.26
Interest Coverage (times)	5.92	5.36	3.06	3.35

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Annexure 1: Details of the Facilities rated

Nature of the Facility	Type of the Facility	Amount (Rs. In Million)	Rating
Long Term Bank Facilities	Hire Purchase Loan	139.49	CARE-NP BB
Long Term Bank Facilities	Term Loan	29.25	CARE-NP BB
Long Term Bank Facilities (Proposed)	Hire Purchase Loan	114.26	CARE-NP BB
Short Term Bank Facilities	Working Capital Loan	181.00	CARE-NP A4
Short Term Bank Facilities (Proposed)	Working Capital Loan	49.00	CARE-NP A4
Short Term Bank Facilities	Bank Guarantee	1,637.00	CARE-NP A4
Total		2,150.00	