

## Rating Rationale

### Gajurmukhi Nirman Company Private Limited

#### Rating

Facility	Amount (Rs. In Million)	Rating <sup>1</sup>	Rating Action
Long Term Bank Facilities	266.46	CARE-NP BB [Double B]	Assigned
Short Term Bank Facilities	4,533.54	CARE-NP A4 [A Four]	Assigned
<b>Total Facilities</b>	<b>4,800.00</b>		

*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 Gajurmukhi Nirman Company Private Limited (GNC).

#### Analytical approach:

CRNL has analysed GNC’s credit profile by considering the Standalone financial statements.

#### Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of GNC are constrained by decline in total revenue of the company in FY20 (Unaudited, refers to 12 months’ period ended mid-July 2020), impact of Covid-19 on the business of the company, leveraged capital structure and moderate debt service coverage indicators of the company. The rating is also constrained by working capital intensive nature of business, planned debt funded capital expenditure, exposure to volatile interest rates and tender based nature of operations in highly competitive construction industry. The ratings, however, derive strength from long track record of operations and experienced promoters in the related field, improvement in PBILDT and cash accruals during FY20 and established track record of GNC in executing various construction works. The ratings also factor in GNC’s healthy order book position with mid-term revenue visibility along with escalation clause in majority of the contracts and moderate counter party risk. Ability of the company to successfully execute projects in time and recover contract proceeds and ability to manage healthy revenue growth and maintain profitability margins without deterioration in its financial risk profile will be key rating sensitivities. Further, ability to manage the impact of Covid-19 on the operations and financials of the company during FY21 will be the key rating sensitivity.

#### ***Impact of Covid-19 on the business of the company***

The global outbreak of Coronavirus disease 2019 (Covid-19) has affected Nepal as well. Government of Nepal (GoN) imposed countrywide lockdown since March 24, 2020 halting operations of most of the organizations and slowing down of the economic activities. The construction activities of the company were also subdued on account of the lockdown. Also, since construction activities in Nepal usually takes momentum on second half of the financial year and with country’s economy and construction sector being significantly impacted since March 2020, it had a negative impact on the revenue and profitability

<sup>1</sup>Complete definitions of the ratings assigned are available at [www.careratingsnepal.com](http://www.careratingsnepal.com)

of the company in comparison to the normal operations. The company's ability to achieve its projected revenue for FY21 and maintain profitability margins will be key rating consideration.

### **Detailed Description of the Key Rating Drivers**

#### **Key Rating Weaknesses**

##### ***Leveraged capital structure and moderate debt service coverage indicators of the company***

The capital structure of the company is marked with debt equity ratio of 2.08x and overall gearing ratio of 3.91x at the end of FY20 (vis-à-vis 2.87x and 5.71x respectively at the end of FY19). The gearing ratio improved in FY20 compared to FY19 mainly on account of increase in capital base of the company and accretion of profit to networth which was partially offset by increase in total loans of the company. Interest coverage ratio of the company was moderate at 2.33x in FY20. Total Outside Liabilities/ Tangible Networth (TOL/TNW) and Total debt/ Gross Cash Accruals of the company was at 4.69x and 9.24x in FY20.

##### ***Working capital intensive nature of business***

The operations of the company are generally working capital intensive in nature as the company primarily works with government departments and funds are released only after the work certification process is completed and finalization of the bills. GNC maintained construction materials as an inventory which was low around 4 days in FY20. Also, the cash flows of the company are blocked in retention money which is deducted by the client from running bills and gets refunded only on successful execution of the contracted work. The total operating cycle of the company was 79 days in FY19 which increased to 109 days in FY20. These factors lead to high reliance of the company on bank finance to meet its working capital requirements.

##### ***Planned debt funded capital expenditure***

The company has been making regular investments to expand its infrastructure facilities in the past and is expected to continue in future. GNC is expected to take additional loans for purchase of equipment/machineries for the new projects proposed to be undertaken in future. Company is expected to make capital expenditure of Rs. 50 Mn in FY21 which is expected to be funded through bank loans.

##### ***Exposure to volatile interest rates***

Nepalese banking sector fixes lending interest rate based on quarterly base rate and interest rate can 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 banks and financial institutions is subject to volatile interest rate.

##### ***Tender based nature of operations in highly competitive construction industry***

The company receives its work orders from government departments. All government contracts are tender based wherein the company has to quote the bid and hence it has to face the risk of successful bidding for

the same, which again comes with the risk of quoting a low price to sustain competition. Also, the promoter's reasonable industry experience in related field mitigates risk of competition to some extent.

### **Key Rating Strengths**

#### ***Long track record of operations and experienced promoters in the related fields***

The company has long track record of operations of more than 30 years in the construction of various infrastructure projects all over Nepal. GNC is majorly promoted by Mr. Deepak Gautam and his family members holding majority shares of the company. GNC has total number of 5 directors in its board. Mr. Deepak Gautam, Chairman, has been involved in construction sector since last 25 years. He looks after overall activities including policy & strategy making of GNC. The promoters have also been infusing funds into the company in the form of equity to fund the operational needs of the company. During FY20, promoters had infused funds in the form of equity of Rs. 20 Mn with increase in equity share capital to Rs. 24.50 Mn. Also, director's loan of Rs. 65 Mn was introduced during FY20 which shall be converted into equity share capital during FY21.

#### ***Decline in total revenue in FY20, however with improvement in PBILDT and cash accruals***

Total revenue of the company declined by ~19% in FY20 on account of lower execution of contracts in hand majorly due to impact of COVID-19. Despite decline in revenue, PBILDT of the company increased with improvement in margin from 19.26% in FY19 to 27.82% in FY20 mainly due to decline in direct costs of the company. However, PAT of the company declined to Rs. 15 Mn in FY20 due to increase in interest expenses with company availing term loans to fund capital expenditure as well as increase in working capital loans to fund operations of the company. Further, with capex done in FY20, depreciation of the company also increased with which Gross Cash Accruals (GCA) of the company improved marginally during FY20.

#### ***Established track record in executing various construction works***

GNC has an established track record of more than 30 years in the construction of road works, railway works, bridge works, building works, irrigation and river training works, etc. ranging from small sized to large sized projects across the country in different terrains either individually or through its JV entities. The long track record has enabled the company to establish relations with its customers thereby resulting into repeat tenders from the government departments. The company is also involved in the construction of National Pride Projects especially related to road associated works.

#### ***Healthy order book position with mid-term revenue visibility***

Till October 14, 2020, the unexecuted orders in hand of the company stood at Rs. 4,276 Mn. Also, the present order book to FY20 revenue on stand-alone basis is around 9.75x which provides healthy revenue visibility. The order book of the company is mainly concentrated in road works (~66%) coupled with other various projects such as railway projects, irrigation and river training projects, building works,

bridge works, etc. received from various government authorities (majorly) which further includes more than 20 National Pride Projects of Nepal as well and private entities. Timely completion of the projects and thereby increasing its scale of operations would be critical from the credit perspective for GNC.

**Escalation clause in majority of the contracts**

GNC procures its construction 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 construction material prices and labor expenses.

**Moderate counter party risk**

Revenue of GNC is generated via contracts from government departments related to road works, railway works, building works, water supply and sanitation works, bridge works etc. Average collection period of the company was high at 178 days in FY20 (vis-à-vis 148 days in FY19) which primarily includes amount receivable from JV entities for work done on government contracts, where GNC was engaged as sub-contractor. However, total debtor declined in absolute value terms, mainly due to decline in sales. However, the counter party risk is moderated by the fact that majority of the construction contracts are obtained from government departments and it has been making timely payment to the company in past.

**About the Company**

Gajurmukhi Nirman Company Private Limited (GNC) is Class “B” construction company of Nepal which was incorporated in the year 2000 with registered office based in Ilam, Nepal. The company is mainly involved in construction of roads, railways, bridges, buildings, irrigation and river training works, etc. In addition to doing projects independently, GNC also enters into Joint Ventures (JV) with other companies in order to meet the eligibility criteria for different construction projects.

Brief financials of GNC (standalone) for last three years ending FY20 are given below:

(Rs. Million)

For the year ended Mid July	FY18	FY19	FY20
	(Audited)	(Audited)	(Provisional)
Income from Operations	780	543	439
PBILDT	92	105	122
PAT	26	20	15
Overall Gearing (times)	7.14	5.71	3.91
TOL/ TNW (times)	12.35	8.57	4.69
Interest Coverage (times)	4.72	3.00	2.33

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**Annexure 1: Details of the Facilities rated**

<b>Nature of the Facility</b>	<b>Type of the Facility</b>	<b>Amount (Rs. In Million)</b>	<b>Rating</b>
Long Term Bank Facilities	Term Loan	266.46	CARE-NP BB
Short Term Bank Facilities	Working Capital Loan	300.00	CARE-NP A4
Long Term/ Short Term Bank Facilities	Non-Funded Loan	4,233.54	CARE-NP BB/ A4
<b>Total</b>		<b>4,800.00</b>	