

Apex Construction Company Private Limited

Ratings

Facilities	Amount (Rs. in Million)	Ratings ¹	Rating Action
Long Term Bank Facilities –Term Loan	100.47 (Reduced from 291.35)	CARE-NP BB [Double B]	Reaffirmed
Short Term Bank Facilities- Working Capital Loan	550.00 (Increased from 236.80)	CARE-NP A4 [A Four]	Reaffirmed
Long Term/Short Term Bank Facilities- Non-Funded Loan	2,849.53 (Reduced from 2,986.70)	CARE-NP BB/A4 [Double B/A Four]	Reaffirmed
Total Bank Facilities	3,500.00 (Three Billion Five Hundred Million)		

Details of instruments/facilities in Annexure-1

CARE Ratings Nepal Limited (CRNL) has reaffirmed rating of 'CARE-NP BB' to the long-term bank facilities and 'CARE-NP A4' to the short-term bank facilities of Apex Construction Company Private Limited (ACC).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of ACC continues to be constrained by its below average financial profile in FY20 (Unaudited, FY refers to 12 months period ended mid-July) coupled with planned debt funded capital expenditure and working capital intensive nature of business. The ratings are also constrained by decreased & concentrated order-book position, tender based nature of operations, risk of delay in project execution and exposure to volatile interest rates.

The ratings, however, continues to derive strength from experienced promoters and established track record of operations in execution of various construction contracts, moderate capital structure & debt service coverage indicators, moderate counter party risk and escalation clause in majority of the contracts.

Going forward, the ability of the company to profitably scale up its operations while successfully executing the projects on time and managing its working capital requirements to support growth will act as the key rating sensitivities. Furthermore, maintaining the order-book is also crucial and act as rating sensitivity.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Decreased order book position coupled with concentration towards road projects

The order book position of the company has decreased by 54% and stood at Rs. 1,739 Mn (share of ACC in joint ventures) as on July end 2021. The order book moderated as compared over previous year (mid-June 2020) and reflects short term revenue visibility, as it is around 1.59 times of total operating income (TOI) of FY21 (based on provisional results). The tenure of the orders undertaken by the company is up to 48 months. The order book is also concentrated in road works (accounting for ~81% of total work order) along with other various projects such as irrigation works, bridge works, airport works and railway works received from various government departments. Higher concentration on single road

¹Complete definitions of the ratings assigned are available at www.careratingsnepal.com and in other CRNL publications

segment constrained company in experience aspect on other projects which impact on increasing order book position and revenue in the upcoming years.

Below average financial profile

Total operating income (TOI) of the company decreased to Rs. 844 Mn in FY20 (decreased by ~42%) on back of impact on company operations for around 3 months in FY20 due to lockdown imposed by the government of Nepal. However, the company reported increase in TOI by 30% in FY21 (based on provisional results) over previous year and stood at Rs. 1,095 Mn on account of increase in execution of projects.

Furthermore, PBILDT margin of the company has been improving on y-o-y basis from 13.75% in FY20 to 14.56% in FY21. The improvement in margin was on account of execution of better margins contracts. However, high dependency on external funding and depreciation expenses have been restricting PAT margin which stood at around 2% in last two FYs (FY20 & FY21).

Working capital intensive nature of business

The operations of the company are working capital intensive in nature. ACC primarily works with the government departments and payments for the contracts are received generally within a month. However, ACC maintained very low level of construction materials as an inventory since the management procured construction materials mostly on need basis and the same was considerably utilized near the year-end. The credit period extended by suppliers of raw materials is normally upto 45 days. Retention money is normally being deducted by the employers from running bills which will get refunded to the contractor after certain period, usually 1 year, on successful execution of contracted work. These factors lead to reliance of the company on bank finance to meet its working capital requirements.

Tender based nature of operations in highly competitive construction industry

The company majorly undertakes government contracts, which are awarded through the tender-based system. The tender-based business is characterized by intense competition and the growth of the business depends on its ability to successfully bid for the tenders and emerge as the lowest bidder. Furthermore, the company participates in the tenders floated by various government agencies which can be lengthy at times.

The company mainly caters to orders received from various Government entities and other Government establishments. The high concentration on government contracts also makes the company susceptible to any changes pertaining to government policy in regard to awarding tenders to contractors. Moreover, the company is dependent on government spending for the total capital expenditure presented in the budget every year.

Planned debt funded capital expenditure

The company has been making regular investments to expand its execution capabilities in the past and expected to continue in future. The investment in equipment/ machineries was Rs. 63 Mn in FY20 and FY21. The purchase of fixed assets was mainly funded through bank finance without any infusion of equity resulting in increase of debt component. Furthermore, it is expected that the company will take additional loan for purchase of equipment/machineries for the new projects proposed to be undertaken in future.

Risk of delay in project execution

ACC's business is susceptible to the financial loss arising out of delay in project execution, as generally, there is a penalty clause for delay in contract execution. However, ACC has relied on the experience of its management team with strong

project execution skills which has enabled the company to build satisfactory standing in the industry as indicated by the repeat orders awarded by its clients.

Key Rating Strengths

Experienced promoters and established track record of operations

ACC was established in May 19, 1985 and was promoted by Mr. Rajan Kumar Bastola along with 3 other members namely Saksham Shrestha, Ramesh Bahadur Adhikari and Rupa Shahi Bastola. The company has established track record of operations of over three decades in construction of roads, bridges, buildings, airport projects, irrigation and water projects etc. Mr. Bastola, managing director, has long experience of over two decades in the field of construction business through his association with company and in individual capacity. He is responsible for overall operational management of the company. Similarly, other directors of the company have related experience in the field of construction contract business. Board of directors are further supported by an experienced team across various functions.

Moderate capital structure and debt service coverage indicators

Debt coverage indicators of the company stood moderate, marked by total debt to gross cash accruals (GCA) and interest coverage of below 8x and above 2x respectively in last two FYs (FY20 & FY21). As on Mid-July 2021, the capital structure of the company also stood moderate marked by overall gearing (including mobilization advance) of 1.76x. The same has improved from 2.72x on account of scheduled repayment of term loans and increase in networth base due to accretion of profits.

Escalation clause in majority of the contracts

The company has inbuilt price escalation clauses in majority of contracts from government departments in order to insulate the company from any adverse fluctuation in raw material prices and labor expenses. Any changes in price have to be informed beforehand and mutually decided between both parties. This enables the company to pass on increase in raw material prices to its customers. Ability of the company to pass on increased price burden to the customers in a timely manner and maintain profitability margins is critical from the credit perspective.

Analytical approach:

CRNL has analyzed the company's credit profile by considering the consolidated financial statements.

About the Company

Apex Construction Company Private Limited (ACC), incorporated on May 19, 1985 as a Class-A construction company of Nepal with registered office based in Kathmandu, Nepal. The company also enters into Joint Ventures (JVs) with other companies in order to meet the eligibility criteria for different construction projects for bidding and execution of contracts.

Financial Performance: Consolidated

For the year ended Mid July	<i>(Rs. Million)</i>		
	2019 (12m, A)	2020 (12m, UA)	2021 (12m, UA)
Income from Operations	1,453	844	1,095
PBILD Margin (%)	9.38	13.75	14.56
Overall Gearing (times)	3.40	2.72	1.76
Total Outstanding Liabilities/Tangible Net worth (times)	6.74	4.74	3.75

For the year ended Mid July	2019	2020	2021
	(12m, A)	(12m, UA)	(12m, UA)
Interest Coverage (times)	3.31	2.55	3.36
Current Ratio (times)	1.18	1.30	1.14
Total Debt/ Gross Cash Accruals (times)	5.03	7.71	4.29

A: Audited, UA: Unaudited

Annexure 1: Details of the Facilities Rated

Name of the Bank Facilities	Type of the Facility	Amount (Rs. In Million)	Ratings
Long Term Bank Facilities	Term Loans	100.47	CARE-NP BB
Short Term Bank Facilities	Working Capital Loans	550.00	CARE-NP A4
Long Term/ Short Term Bank Facilities	Non-Funded Loans	2,849.53	CARE-NP BB/ A4
Total		3,500.00	

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