

## Motidan Construction Sewa Private Limited

### Ratings

Facilities	Amount (Rs. in Million)	Ratings <sup>1</sup>	Rating Action
Long Term Bank Facilities	1,691.08	CARE-NP BB+ [Double B Plus]	Rating revised from CARE-NP BB
Short Term Bank Facilities	1,555.00	CARE-NP A4+ [A Four Plus]	Rating revised from CARE-NP A4
Long Term/ Short Term Bank Facilities	7,126.50	CARE-NP BB+ / A4+ [Double B Plus/ A Four Plus]	Rating revised from CARE-NP BB/A4
<b>Total Facilities</b>	<b>10,372.58</b>		

*Details of instruments/facilities in Annexure 1*

CARE Ratings Nepal Limited (CRNL) has revised the rating assigned to the long term bank facilities of Motidan Construction Sewa Private Limited (MCS) to 'CARE-NP BB+' from 'CARE-NP BB'. CRNL has also revised rating assigned to MCS' short-term facilities to 'CARE-NP A4+' from 'CARE-NP A4'.

### Detailed Rationale & Key Rating Drivers

The revision in the ratings assigned to the bank facilities of MCS takes into account the improving financial risk profile of the company marked by growth in total operating income (TOI) coupled with moderate profitability margins during FY21 (Audited, refers to the twelve-month period ended mid-July 2021). However, the ratings continue to be constrained by its leveraged capital structure, modest order book position and its presence in highly competitive industry coupled with tender based nature of operations. The ratings also factor in its exposure to volatile interest rates and government regulations and risk of delay in project execution.

The ratings, however, derive strength from experienced promoters and moderate track record of operations, moderate counter party risk and escalation clause in majority of the contracts.

*Going forward, the ability of the company to successfully execute projects and recover contract proceeds in a timely manner, profitably scale up the operations of the company leading to sustained revenue growth and rationalization of its debt through efficient working capital management would be the key rating sensitivities.*

### Detailed Description of the Key Rating Drivers

#### Key Rating Weaknesses

#### Leveraged capital structure and modest order book position

Capital structure of MCS stood leveraged with overall gearing ratio (including mobilization advance) of 3.06x as on mid-July 2021 which deteriorated marginally from 2.95x as on mid-July 2020 amid higher bank borrowings availed by MCS during FY21. Total debt of the company, which mainly comprises of hire purchase loans, equipment loans, mobilization advance & working capital borrowings, increased in FY21 to Rs. 1,367 Mn from Rs. 853 Mn in FY20. Increase in hire purchase loans was for funding purchase of construction machineries and working capital loans for funding the working capital needs of the company. Also, total outside liability to total net worth remained high at 5.23x as on mid-July 2021 (PY: 5.11x). However, the interest coverage and total debt to gross cash accruals stood moderate at 3.71x and 5.34x respectively in FY21 showing improvement from 3.15x and 6.85x in FY20 aided by increase in PBILDT with increase in TOI.

As on April 13, 2022, the unexecuted orders in hand of the company stood at Rs. 3,538 Mn, which is 1.06x of the income from contract of FY21, providing near term revenue visibility. The order book is concentrated and consists of various

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

construction projects; however, remain primarily concentrated towards road projects (~78%) and others include mining, building and water supply and canal projects by entering into JVs. Timely completion of the projects would be critical for the business prospects of the company and also has a direct bearing on its margins.

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

Majority of the MCS's projects are tender-based government contracts wherein the company has to quote a bid. With multiple players active in the industry, MCS's business is vulnerable to under bidding at a relatively low cost in order to secure the projects, in the highly competitive construction industry. Furthermore, the business also remains dependent on sustained capital expenditure by the government towards construction projects, overall stability in government policies and fiscal position of the government. Government of Nepal (GoN) has put certain restrictions on the contractors to participate in tenders such as prohibiting foreign companies to participate in tenders having value less than Rs. 3,000 Mn, which augurs well for domestic players. Furthermore, the GoN has also placed a cap on total active projects of construction companies at five, which could limit growth prospects.

### **Exposure to volatile interest rate**

Nepalese banking sector has a floating interest rate regime, where a certain premium is added to the quarterly base rate and interest rate is changed accordingly on quarterly basis. The base rates of the banks and financial institutions (BFIs) in Nepal remain quite volatile as they are impacted by available liquidity in the system which leads to change in interest rates. The volatility in interest rate is more evident currently on account of the ongoing liquidity stress in the economy. Furthermore, increased bank rates announced in the Monetary Policy for FY23 is likely to add to the upward pressure on interest rates going forward. Any significant rate hikes could put increased interest burden on the company, squeezing its profitability and impacting its liquidity position. Therefore, funding taken by the company from BFIs is subject to volatile interest rate.

### **Risk of delay in project execution**

Given the nature of projects awarded, MCS is exposed to inherent risk in terms of delays in certain projects undertaken by the company due to delay in procedural approvals and clearance of project sites, etc, thus exposing the company towards the risk of delay in projects resulting in a delay in the realization of revenue growth. Furthermore, the company ability to execute a project in timely manner would be led by its own operational efficiency and timely stage payments received from clients.

### **Key Rating Strengths**

#### **Experienced promoters and moderate track record of operations**

MCS is promoted by Mr. Ram Bahadur Gautam, Managing Director, who has been leading the company since its inception in March 2009. Mr. Gautam has experience of more than a decade in the construction sector which bodes well for the overall business prospects of the company in an increasingly competitive industry. He is responsible for planning business strategies of the company. Furthermore, the board is supported by an experienced team across various functions. The company has moderate track record of operations of over a decade in the construction of various infrastructure projects all over Nepal.

#### **Improving financial risk profile marked by increase in TOI and PAT margin**

MCS's TOI grew ~160% year-on-year to Rs. 3,329 Mn during FY21 boosted by execution of projects after being impacted by the pandemic during FY20 when total operating income had declined ~44% over FY19. The business generation of the

company is through bidding and tendering process and profitability margins are directly associated with the nature of contracts executed by the company. The PBILDT margin has remained moderate and was in between 9%-16% during the last 3 financial years (FY19-FY21). PBILDT margin declined to 11.97% in FY21 from 15.73% in FY20 amid increased input prices and increased execution of low margin projects. Furthermore, PAT margin of MCS improved by 59 bps to 3.22% in FY21. Consequently, GCA of the company increased to Rs. 256 Mn in FY21 from Rs. 125 Mn in FY20 mainly on account of increase in PAT and depreciation expense of the company.

### Moderate operating cycle

The working capital cycle of MCS appears to be moderate at 23 days, primarily because the company receives a high payable period of around 60-90 days from its suppliers. MCS's inventory holding was low at around 3 days in FY21 on account of better raw materials management, since most of the raw materials required by the company is procured by the company as and when required. The funds are released only after the work certification process is completed and finalization of the bill is done. Customer base includes government departments / bodies; therefore, the certification and realization of the bill generally takes the period of around two months. There is usually a delay in the recovery of debtors, and at times, the same exceeds more than three months. Consequently, average collection period of the company was moderate at around 88 days in FY21.

### Moderate counter party risk

Revenue of MCS is generated via contracts from both government departments and private parties. The order book is primarily concentrated towards road projects from government departments. Counter party risk remains moderate given the projects are from government departments, which have been making timely payment to the company in the past.

### Analytical Approach

CRNL has analysed MCSP's credit profile by considering the consolidated financial statements comprising MCSP and its joint venture entities related to the construction projects.

### About the Company

MCS is a class "A" construction company of Nepal incorporated on March 03, 2009 with its registered office based in Kathmandu, Nepal. The company is involved in mining works, construction of roads, bridges, building, irrigation works etc. across Nepal. In addition to doing projects independently, MCS also enters into Joint Ventures (JVs) with other companies in order to meet the eligibility criteria for different construction projects.

### Financial Performance

(Rs. Million)

For the Period	FY19 (A)	FY20 (A)	FY21 (UA)
Income from Operations	2,271	1,281	3,330
PBILDT Margin (%)	9.43	15.73	11.97
Overall Gearing (times)	2.68	2.95	3.06
Total Outstanding Liabilities/Tangible Net worth (times)	5.43	5.11	5.23
Interest Coverage (times)	4.33	3.15	3.71
Current Ratio (times)	1.20	1.22	1.18
Total Debt/Gross Cash Accruals (times)	4.09	6.85	5.34

A: Audited

**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 Loan	1,691.08	CARE-NP BB+ [Double B Plus]
Short Term Bank Facilities	Fund Based Limits	1,555.00	CARE-NP A4+ [A Four Plus]
Long Term/ Short Term Bank Facilities	Non Fund Based Limits	7,126.50	CARE-NP BB+ / A4+ [Double B Plus/ A Four Plus]
<b>Total</b>		<b>10,372.58</b>	

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