

Om Sai Ram Construction Private Limited

Ratings

Facilities	Amount (Rs. in Million)	Ratings ¹	Rating Action
Long Term Bank Facilities	162.90	CARE-NP BB [Double B]	Reaffirmed
Short Term Bank Facilities	5.00	CARE-NP A4 [A Four]	Reaffirmed
Long Term/ Short Term Bank Facilities	1,832.10	CARE-NP BB/ A4 [Double B/ A Four]	Reaffirmed
Total Facilities	2,000.00 (Two Thousand Million Only)		

Details of instruments/facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has reaffirmed the rating of 'CARE-NP BB' assigned to the long-term bank facilities and 'CARE-NP A4' assigned to the short-term bank facilities of Om Sai Ram Construction Private Limited (OSRC).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of OSRC continue to be constrained by its below average financial risk profile marked by fluctuating profitability margins though moderate coupled with modest order book position, working capital intensive nature of business and its presence in highly competitive construction industry coupled with tender based nature of operations. The ratings are also constrained by exposure to volatile interest rates and government regulations and risk of delay in project execution.

The ratings, however, derive strengths from experienced promoters and moderate track record of operations, moderate capital structure and debt service coverage indicators of the company, moderate counter party risk and escalation clause in majority of the contracts. The ratings also take cognizance of growth in total operating income (TOI) in FY21 (Audited, refers to the twelve-month period ended mid-July 2021).

Going forward, the ability of the company to successfully execute projects in time and recover contract proceeds; and ability to maintain profitability margins and manage its working capital requirements to support growth will be key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Fluctuating Total operating income and profitability margins coupled with modest order book position

During FY21, OSRC's TOI grew ~51% over FY20 to Rs. 513 Mn boosted by execution of projects after being impacted by the pandemic during FY20 when total operating income had declined ~50% 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 of the company has remained highly volatile and fluctuated between 13%-23% during the last 3 financial years (FY19-FY21). PBILDT margin declined to 19.07% in FY21 from 23.39% in FY20 amid increased input prices and increased execution of low margin projects. Consequently, PAT margin of OSRC declined to 3.59% in FY21 from 5.59% in FY20.

As on June 13, 2022, the unexecuted orders in hand of the company stood at Rs. 851 Mn, which is 1.66x of the income from contract of FY21, providing near-term revenue visibility. The order book is majorly concentrated towards building projects (~99%) and bridge 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.

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

Working capital intensive nature of business

The operations of the company are working capital intensive in nature marked by moderate inventory holding period and collection period. OSRC's inventory holding period was around 93 days in FY21 compared to 187 days in FY20 with major inventory being construction materials such as cement and rods. Furthermore, funds are released only after the work certification process is completed and finalization of the bill is done. Consequently, average collection period of the company was also moderate at 69 days in FY21, compared to 85 days in FY20. These factors lead to increased reliance of the company on borrowings to meet its working capital requirements.

Tender based nature of operations in highly competitive construction industry

Majority of the OSRC's projects are tender-based government contracts wherein the company has to quote a bid. With multiple players active in the industry, OSRC'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, OSRC 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**

OSRC is promoted by Mr. Bijay Kumar Shah, Managing Director, who has been leading the company since its inception from February 2010. Mr. Shah has experience of more than two decades in the construction sector which bodes well for the overall business prospects of the company in an increasingly competitive industry. He is responsible for execution of projects undertaken by the company. Further, the board is supported by an experienced team across various functions.

The company has moderate track record of operations of more than a decade in the construction of various infrastructure projects all over Nepal.

Moderate capital structure and debt service coverage indicators of the company

Capital structure of OSRC stood moderate with overall gearing ratio (including mobilization advance) of 2.00x as on mid-July 2021, which remained at similar level of 1.96 as on mid-July 2020 with the impact of increase in debt being offset by additional equity infusion of Rs. 50 Mn during the year. Total debt of the company, which mainly comprises of term loans, mobilization advance & working capital borrowings, increased in FY21 to Rs. 319 Mn from Rs. 198 Mn at in FY20 on account of increased equipment loans for funding purchase of construction machineries and working capital borrowings for funding working capital needs of the company. Also, total outside liability to total net worth and total debt to gross cash accruals remained moderate at 4.79x and 4.53x respectively as on mid-July 2021 (8.01x and 3.43x, respectively, as on mid-July 2020). Furthermore, the interest coverage was moderate at 4.06x in FY21 as compared to 4.35x in FY20.

Moderate counter party risk

Revenue of OSRC is majorly generated via contracts from government departments. The order book is primarily concentrated towards building 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.

About the Company

OSRC, incorporated on February 24, 2010, is a Class-A construction company of Nepal with registered office based in Satdobato, Lalitpur, Nepal. The company is involved in construction of both small and large scale projects mainly relating to road works, building works, bridge works, irrigation works etc. in different part of Nepal. In addition to doing projects independently, OSRC also enters into Joint Ventures (JVs) with other companies in order to meet the eligibility criteria for construction projects.

Financial Performance

	(Rs. Million)		
For the Period Ended / as at Mid-July,	FY19 (A)	FY20 (A)	FY21 (A)
Income from Operations	684	339	513
PBILDT Margin (%)	12.52	23.39	19.07
Overall Gearing (times)	2.11	1.96	2.00
Interest Coverage (times)	5.00	4.35	4.06
Current Ratio (times)	1.05	0.70	0.79
Total Debt/ Gross Cash Accruals (times)	3.43	3.43	4.53

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	162.90	CARE-NP BB [Double B]
Short Term Bank Facilities	Fund Based Limits	5.00	CARE-NP A4 [A Four]
Long Term/ Short Term Bank Facilities	Non-Fund Based Limits	1,832.10	CARE-NP BB/ A4 [Double B/ A Four]
Total		2,000.00	

Contact Us

Analyst Contact

Mr. Girish Bhatta

+977-01-4012630

girish.bhatta@careratingsnepal.com

Mr. Santosh Pudasaini

+977-01-4012629

pudasaini.santosh@careratingsnepal.com

Relationship Contact

Mr. Achin Nirwani

+977-9818832909

achin.nirwani@careratingsnepal.com

About CARE Ratings Nepal Limited:

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