

Shiva Shakti Infra Developers Private Limited

Ratings

| Facilities | Amount (Rs. in Million) | Ratings ¹ | Rating Action |
|---------------------------------------|--|---|---------------|
| Long Term Bank Facilities | 232.86 | CARE-NP BB- [Double B Minus] | Reaffirmed |
| Short Term Bank Facilities | 19.99 | CARE-NP A4 [A Four] | Reaffirmed |
| Long Term/ Short Term Bank Facilities | 3,747.15 | CARE-NP BB-/ A4 [Double B Minus/ A Four] | Reaffirmed |
| Total Facilities | 4,000.00 (Four 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 Shiva Shakti Infra Developers Private Limited (SSID).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of SSID continues to be constrained by its leveraged capital structure, 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 strength from experienced promoters and established track record of operations, moderate order book with mid-term revenue visibility, moderate counter party risk and escalation clause in majority of the contracts. The ratings also took cognizance of growth in total operating income in FY21 (FY refers to the twelve-month period ended mid-July).

Going forward, the ability of the company to profitably scale up its operations amidst high level of competition and manage its working capital requirements to support growth leading to improvement in solvency ratios will be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Below average financial risk profile marked by fluctuating profitability margins and leveraged capital structure

SSID's Total Operating Income (TOI) grew significantly ~162% year-on-year to Rs. 772 Mn during FY21 boosted by execution of projects after being impacted by the pandemic during FY20 when total operating income had declined ~5% 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 also remained highly volatile and fluctuated between 9%-21% during the last 3 financial years (FY19-FY21). PBILDT margin declined to 9.20% in FY21 from 20.67% in FY20 amid increased input prices and increased execution of low margin projects. Consequently, PAT margin of SSID declined to 0.98% in FY21 from 2.01% in FY20.

Capital structure of SSID stood leveraged with overall gearing ratio (including mobilization advance) of 4.67x as on mid-July 2021 which improved from 7.51x as on mid-July 2020 aided by equity infusion of Rs. 80 Mn during FY21. Total debt of the company, which mainly comprises of hire purchase loans, mobilization advance & working capital borrowings, increased in FY21 to Rs. 542 Mn from Rs. 437 Mn at in FY20. Increased hire purchase loans for funding purchase of

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

construction machineries and additional mobilization advance being received to finance the increased scale of operations. Also, total outside liability to total net worth and total debt to gross cash accruals remained high at 6.58x and 12.23x respectively as on mid-July 2021 (9.61x and 11.97x, respectively, as on mid-July 2020). However, the interest coverage was moderate at 2.89x in FY21 showing improvement from 2.66x in FY20.

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. SSID's inventory holding period was around 71 days in FY21 compared to 138 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 62 days in FY21, compared to 100 days in FY20. These factors lead to increased reliance of the company on borrowings to meet its working capital requirements. Attributed to high working capital requirements and delays in realisation of debtors sometimes led to cashflow mismatches which have resultant into instances of delays of less than 30 days in servicing of bank obligations in the past.

Tender based nature of operations in highly competitive construction industry

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

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, SSID 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 established track record of operations

SSID is promoted by Mr. Babu Ram Pathak, Chairman, who has been leading the company since its inception in August 1999. Mr. Pathak 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. Mr. Surendra Pathak, Managing Director, has experience of more than a decade in construction sector and look after overall operations of the company. Furthermore, the board is supported by an experienced team across various functions. The company has long track record of operations of more than two decades in the construction of various infrastructure projects all over Nepal.

Moderate order book position with mid-term revenue visibility

As on February 12, 2022, the unexecuted orders in hand of the company stood at Rs. 2,154 Mn, which is 2.79x of the income from contract of FY21, providing moderate revenue visibility. The order book is primarily concentrated towards road projects (~89%) and others include building, river training and water supply 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.

Moderate counter party risk

Revenue of SSID is majorly generated via contracts from government departments. 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.

About the Company

Shiva Shakti Nirman Sewa was incorporated on August 10, 1999 as a sole proprietorship firm which was later converted into private limited company as Shakti Infra Developers Private Limited (SSID) on July 22, 2018. It is a Class "A" construction company of Nepal with registered office in Makwanpur, Nepal. In addition to doing projects independently, SSID 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 Ended / as at Mid-July, | FY19 (A) | FY20 (A) | FY21 (A) |
|---|----------|----------|----------|
| Income from Operations | 309 | 295 | 772 |
| PBILDT Margin (%) | 14.10 | 20.67 | 9.20 |
| Overall Gearing (times) | 4.29 | 7.51 | 4.67 |
| Interest Coverage (times) | 2.79 | 2.66 | 2.89 |
| Current Ratio (times) | 1.29 | 1.94 | 1.88 |
| Total Debt/ Gross Cash Accruals (times) | 7.74 | 11.13 | 12.23 |

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 | 232.86 | CARE-NP BB- [Double B Minus] |
| Short Term Bank Facilities | Fund Based Limits | 19.99 | CARE-NP A4 [A Four] |
| Long Term/ Short Term Bank Facilities | Non-Fund Based Limits | 3,747.15 | CARE-NP BB-/ A4 [Double B Minus/ A Four] |
| Total | | 4,000.00 | |

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