

Bhimeshwor Drilling Tatha Nirman Sewa Private Limited

Ratings

Facilities	Amount (Rs. in Million)	Ratings ¹	Rating Action
Long Term Bank Facilities	95.83	CARE-NP BB [Double B]	Reaffirmed
Short Term Bank Facilities	177.31	CARE-NP A4 [A Four]	Reaffirmed
Long Term/ Short Term Bank Facilities	1,226.86	CARE-NP BB/ A4 [Double B/ A Four]	Reaffirmed
Total Facilities	1,500.00		

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 Bhimeshwor Drilling Tatha Nirman Sewa Private Limited (BDNS).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of BDNS continue to be constrained by its leveraged capital structure along with moderate debt service coverage indicators, concentrated though moderate 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, financial risk profile marked by improvement in Total Operating Income (TOI) and profitability in FY21 (Audited, refers to the twelve-month period ended mid-July 2021), moderate counter party risk and escalation clause in majority of the contracts. *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

Leveraged capital structure with moderate debt service coverage indicators

Capital structure of BDNS stood leveraged with overall gearing ratio of 3.19x as on mid-July 2021, which improved from 3.61x as on mid-July 2020 aided by increase in shareholders' fund by Rs. 69 Mn (including infusion of Rs. 40 Mn in the form of share application money pending conversion). Total debt of the company, which mainly comprises of term loans, working capital borrowings and mobilization advance, increased in FY21 to Rs. 921 Mn from Rs. 560 Mn in FY20 on account of increased hire purchase loans for funding purchase of construction machineries and working capital loans for funding working capital needs of the company, however, with decrease in mobilization advance in FY21. Also, total outside liability to total net worth and total debt to gross cash accruals remained high at 4.03x and 8.74x respectively as on mid-July 2021 (5.14x and 10.01x, respectively, as on mid-July 2020). However, the interest coverage was moderate at 3.21x in FY21 which deteriorated from 3.61x in FY20, due to increased interest expense amid higher bank borrowings of the company.

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

Concentrated though moderate order book position

As on July 16, 2022, the unexecuted orders in hand of the company stood at Rs. 5,377 Mn, which is around 3x of the income from contract of FY21, providing moderate revenue visibility. The order book is primarily concentrated towards water supply projects (~42%), road projects (~37%) and others include waste water treatment and building 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.

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. BDNS's inventory holding period was around 41 days in FY21 compared to 17 days in FY20 majorly due to piling up of construction materials as the company has to maintain inventory at various sites for smooth execution of project works. 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 95 days in FY21 which deteriorated from 80 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 BDNS's projects are tender-based government contracts wherein the company has to quote a bid. With multiple players active in the industry, BDNS'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, BDNS 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

BDNS is promoted by Mr. Sahadev Khadka, Managing Director, who has been leading the company since its inception from March 2011. Mr. Khadka has experience of around fifteen years in the construction sector which bodes well for the overall business prospects of the company in an increasingly competitive industry. He is responsible for overall management and the execution of projects undertaken by the company. Mr. Krishna Bahadur Khadka, director, has considerable experience in construction sector and look after the overall operations of the company. Furthermore, 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.

Growing scale of operations with improving profitability

During FY21, BDNS's TOI grew ~79% over FY20 to Rs. 1,752 Mn majorly on account of execution of final stage projects. The business generation of the company is through bidding and tendering process and profitability margins directly associated with the nature of contracts executed by the company. Similarly, PBILDT of the company increased to Rs. 182 Mn in FY21 from 89 Mn in FY20 along with increase in PBILDT margin to 10.38% in FY21 from 9.08% in FY20. Backed by higher sales, gross cash accruals of BDNS increased to Rs. 105 Mn in FY21 from Rs. 56 Mn in FY20. Also, PAT margin of the company increased to 3.68% in FY21 from 2.48% in FY20. The company's ability to sustain the growth momentum supported by timely execution of the projects at hand will be critical for its business growth going forward.

Moderate counter party risk

Revenue of BDNS is majorly generated via contracts from government departments. The order book is primarily concentrated towards water supply 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 BDNS's credit profile by considering the consolidated financial statements comprising BDNS and its joint venture entities related to the construction projects.

About the Company

Bhimeshwor Drilling Udhyog was incorporated on March 03, 2011 as a proprietorship firm which was later converted into private limited company as Bhimeshwor Drilling Tatha Nirman Sewa Private Limited (BDNS) on April 10, 2018. It is a Class-A construction company of Nepal with registered office based in Bhaktapur, Nepal. The company is mainly involved in construction of both small and large scale projects mainly relating to deep boring, drilling works and water supply works etc. in different part of Nepal. In addition to doing projects independently, BDNS 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 (UA)
Income from Operations	308	975	1,752
PBILDT Margin (%)	8.77	9.08	10.38
Overall Gearing (times)	3.09	3.61	3.19
Interest Coverage (times)	3.63	3.61	3.21
Current Ratio (times)	1.73	2.11	1.67
Total Debt/ Gross Cash Accruals (times)	13.40	10.01	8.74

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 Loan	95.83	CARE-NP BB [Double B]
Short Term Bank Facilities	Fund Based Limits	177.31	CARE-NP A4 [A Four]
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Total		1,500.00	

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About CARE Ratings Nepal Limited:

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