

Bikash & Brothers Construction Private Limited

Ratings

Facilities	Amount (Rs. in Million)	Ratings ¹	Rating Action
Long Term Bank Facilities	30.92	CARE-NP BB- [Double B Minus]	Assigned
Short Term Bank Facilities	144.00	CARE-NP A4 [A Four]	Assigned
Long Term/ Short Term Bank Facilities	1,325.08	CARE-NP BB -/A4 [Double B Minus/A four]	Assigned
Total Facilities	1,500.00 (One Thousand Five Hundred Million Only)		

Details of Facilities in Annexure 1

Care Ratings Nepal Limited (CRNL) has assigned the rating of 'CARE-NP BB-' to the long term bank facilities and the rating of 'CARE-NP A4' to the short term bank facilities of Bikash & Brothers Construction Private Limited (BBC).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of BBC are constrained by working capital intensive nature of operations marked by highly elongated average inventory holding and collection period in FY22 (Unaudited; FY refers to the twelve-month period ending mid-July) leading to increased reliance on borrowings. The ratings also factor in the concentrated revenue base albeit with reasonable order book position, the tender based nature of operations in highly competitive construction industry, risk of delay in project execution and exposure to volatile interest rates.

The ratings, however, derive strengths from BBC's experienced promoters and moderate operational track record in executing construction works, growing trend in scale of operations over FY20-FY22 albeit with volatile profitability, moderately leveraged capital structure with adequate debt service coverage indicators, low counter party risk coupled with escalation clause in majority of contracts.

Going forward, the ability of the company to successfully execute projects and recover contract proceeds in timely manner, profitably scale up the operations of the company leading to sustained revenue growth while maintaining profitability margins and improving its overall financial risk profile will be key sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Elongated operating cycle with increasing trend in collection period

The operations of the company are working capital intensive in nature marked by substantially high average collection period and inventory period at the end of FY22. BBC's average collection period elongated to 168 days in FY22 from 150 days in FY21. BBC's customer base includes majorly of government departments / bodies, with certification and realization of bills generally taking a period of around 2-3 months. However, a substantially elongated collection period is a concern, particularly amid the slowdown in government capital expenditures and revenue collection over the last year or so coupled with the ongoing liquidity stress in the banking industry. Furthermore, BBC's inventory period also stood very high at 234 days in FY22 (FY21: 162 days) which included inventory and various sites coupled with work in progress. Although counterparty risk remains low over the long-term, stretched operating cycle could put additional burden in the company's financial profile over the near-term. Average utilization of the working capital facilities has been high at around 90% over the last 12 months, as per banker. Amid increasing working capital intensity, the company's reliance on borrowings to meet its working capital

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

requirements is only likely to increase further. Hence, the company's ability to timely turnaround projects under work-in-progress coupled with swifter debtor realization will be critical from credit perspective.

Revenue base concentrated towards roads and building projects albeit with decent order book position

The company's revenue base is highly concentrated mainly towards roads and buildings (85.96% of total order book) mostly from various government departments including Provincial and local bodies. This exposes the company to revenue concentration risk in terms of business segment. Concentration of government orders exposes the company with risk related to allocation of fund or regulatory changes mainly in the Public Procurement Act and other related regulations. Although the company is looking to diversify its order book, the company's ability to successfully bid and execute these remains to be seen.

The company has unexecuted order books of Rs. 2,346 Mn (includes share of BBC through Joint Ventures) as on February 01, 2023. The order book of the company reflects mid-term revenue visibility for the next 2 to 3 years. Timely completion of the projects, including BBC's ability to regularly bill and realize projects under progress, 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 BBC's projects are tender-based government contracts (including provincial and local bodies) wherein the company has to quote a bid. With multiple players active in the industry, BBC'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. 5,000 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.

Risk of delay in project execution

Given the nature of projects awarded, BBC 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 further resulting a delayed realization of revenue growth. Furthermore, the company's ability to execute projects in timely manner would be led by its own operational efficiency and timely stage payments received from clients.

Exposure to volatile interest rates

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, with substantial upward pressure on interest rates in the last few quarters. A contractionary monetary policy for FY23 coupled with increasing inflation has only added to the upward pressure on interest rates, resulting in the rate hikes taken by BFIs in the first quarter of FY23. Any further 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.

Key Rating Strengths

Experienced promoters and moderate track record of operations

BBC is managed by Arun Kumar Shah, who has over 20 years of experience in the construction industry, leading the company since its inception in 2015. Prior to inception of BMC, Mr. Shah was associated with different companies in various capacities. The company has a moderate track record of 7 years in construction of roads (majorly), bridges, water supply projects and commercial buildings from small to large projects and have executed several projects across the country in different terrains either individually or through its JV.

Growing scale of operations over the period albeit with volatile profitability

Total operating income of the company increased at a compounded annual growth rate of 9% over FY19-FY22 and stood at Rs. 485 Mn in FY22 (Rs.689 Mn in FY22(unaudited), on the basis of consolidated financial statement, including revenue from JVs). Although the pace of growth moderated to ~2% in FY22 from ~60% in FY20 amid amendments in the Public Procurement Act by Government of Nepal which restricts number of contracts for any contractors to participate. The business generation of the firm is through bidding and tendering process and profitability margins directly associated with the nature of contracts executed. PBILDT of the company has increased to Rs.168 Mn with the margin of ~34.63% in FY22 from Rs.60 Mn with the margin of ~12.67% in FY21. Consequently, PAT margin of the company improved to ~18.43% in FY22 from ~3.37% in FY21 and GCA increased to Rs.115 Mn from Rs.44 Mn. The company's ability to maintain a steady profitability profile over a sustained period remains to be seen and will remain a key monitorable.

Moderately leveraged capital structure with adequate debt service coverage indicators

The capital structure of the company is moderately leveraged marked by overall gearing ratio (with mobilization advance) of 1.59x at the end of FY22 which improved from 3.00x at the end of FY21 majorly on account of improvement in net worth with accretion of profits to the reserves of the company resulting increase in net worth. Total debt comprises of hire purchase, mobilization advance and short term loan which stood at Rs. 261 Mn at the end of FY22 (FY21: Rs. 223 Mn) while total tangible net worth increased to Rs. 164 Mn (Rs. 75 Mn in FY21). Consequently, Total Outside Liabilities/Tangible Net Worth of the company also improved to 3.39x in FY22 from 7.88x in FY21 supported by increased networth of the company. Total debt/ GCA of the company also improved to 2.28x in FY22 as compared to 5.13x in FY21. Similarly, debt service coverage indicators also stood adequate, marked by interest coverage ratio of 7.17x in FY22 (FY21: 4.29x).

Moderate counter party risk and escalation clause in majority of contracts

Revenue of BBC is majorly generated via contracts from government departments and private sectors. The order book is primarily concentrated towards roads and buildings projects. Counter party risk remains moderate given the projects are from government departments, which have been making timely payment to the company in the past. This enables the company to pass increase in raw material prices to its customers. Ability of the company to pass increased burden to the customer in a timely manner and maintain profitability margins is a critical from credit perspective.

About the Company

Bikash & Brothers Construction Private Limited (BBC) is a Class "B" construction company in Nepal, incorporated on July 10, 2015, with registered office in Janakpur, Dhanusa, Nepal. The company has been involved over eight years in the business of construction of roads (majorly), bridges, water supply projects. It acts as the main contractor (majorly) for small to big size projects for Government projects and industrial/Commercial projects as well as acts as sub-contractor in some contracts.

Financial Performance

(Rs in Million)

For the period ended/ as at mid-July	FY20 (A)	FY21 (A)	FY22 (UA)
Income from operations	299	477	485
PBILDT Margin (%)	19.14	12.67	34.63
Overall Gearing (times)	3.40	3.00	1.59
Interest Coverage (times)	3.29	4.29	7.17
Current Ratio (times)	1.27	1.15	1.17
Total Debt/ Gross Cash Accruals	5.44	5.13	2.28

A: Audited; UA: Unaudited

Annexure 1: Details of the Facilities rated

Nature of the Facility	Type of the Facility	Amount (Rs. in Million)	Rating
Long Term Bank Facilities	Term Loan	30.92	CARE-NP BB- [Double B Minus]
Short Term Bank Facilities	Fund Based Limit	144.00	CARE-NP A4 [A Four]
Long Term/ Short Term Bank Facilities	Non Fund Based Limit	1,325.08	CARE-NP BB -/A4 [Double B Minus/A four]
Total		1,500.00	

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