

Narayanam Nirman Sewa Private Limited

Ratings

Facilities	Amount (Rs. in Million)	Ratings ¹	Rating Action
Long Term Bank Facilities	33.50	CARE-NP B+ [Single B Plus]	Assigned
Short Term Bank Facilities	1,236.50	CARE-NP A4 [A Four]	Assigned
Total Facilities	1,270.00 (One Billion and Two Hundred Seventy Million Only)		

Details of instruments/facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has assigned rating of 'CARE-NP B+' to the long term bank facilities and 'CARE-NP A4' to the short term bank facilities of Narayanam Nirman Sewa Private Limited (NNSPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of NNSPL are constrained by its small scale of operations with volatile operating income and profitability over the period, leveraged capital structure, and working capital intensive nature of operations marked by elongated inventory holding period in FY22 (Audited, FY refers to the twelve-month period ending mid-July). The ratings also factor in tender based nature of operations in the highly competitive construction industry, exposure to volatile interest rates, regulatory risk and risk of delay in project execution. The ratings, however, derive strengths from NNSPL's experienced promoters, moderate track record in executing various projects and order book position providing mid-term revenue visibility. The ratings also factor in moderate counter party risk and escalation clause in majority of 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 while maintaining profitability margins along with improving its overall financial risk profile will be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Weak financial risk profile marked by small scale of operations with volatile operating income over the period coupled with leveraged capital structure

NNSPL's scale of operations has remained small since its inception in 2015 marked by a total operating income (TOI) of Rs. 131 Mn during FY22. Furthermore, the rate of incremental growth in operating income has been volatile over FY20-FY22. The company had reported increase in operating income by ~185% year-on-year (y-o-y) in FY21 followed by decrease of ~64% y-o-y in FY22 amid lower execution of projects during FY22. The ability of the company to scale up to larger-sized contracts having better operating margins is constrained by its comparatively low net-worth of Rs. 38 Mn at the end of FY22, which although increased from Rs. 20 Mn at the end of FY21 supported by addition of Rs. 15 Mn advances by promoters.. Furthermore, the company had substantial work-in progress (~Rs. 187 Mn) at the end of FY22, which the company expects to bill in FY23. Despite lower income in FY22, PBILDT margin increased to 18.25 during FY22 from 6.43 during FY21 aided by execution of better margin contracts. Small scale of operations in a competitive industry limits the pricing power and benefits of economies of scale.

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

Furthermore, the capital structure of the company is leveraged with overall gearing ratio (with mobilization advance) of 4.97x as on mid-July 2022. Also, Total debt/ GCA of the company deteriorated to 17.22x in FY22 as compared to 8.21x in FY21 amid increased debt levels, majority of which is unsecured loans from promoters.

Working capital intensive nature of business

The operations of the company are working capital intensive in nature. Although the company's debtors outstanding had been nil in the past couple of years, its inventory holding period had increased substantially in FY22. NNSPL's inventory holding period stood at ~21 months in FY22. The company held inventory of Rs. 233 Mn in FY22 of which around 70% was work-in-progress. This led to net operating cycle of over six months in FY22. An elongated operating cycle could put additional burden in the company's financial profile over the near-term. Amid increasing working capital intensity, the company's reliance on borrowings to meet its working capital requirements could 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.

Tender based nature of operations in highly competitive construction industry

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

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, 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 increased base rates of BFIs in the first half 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.

Risk of delay in project execution

Given the nature of projects awarded, NNSPL 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 along with moderate track record of operations

NNSPL has five directors in its Board of Directors chaired by Mr. Jaya Bahadur Khatri, who is involved in construction sector for more than two decades. Mr. Santosh Kumar Regmi, Director, has experience of around 18 years and manages overall projects executed by the company. Furthermore, he is supported by an experienced team across various functions. The company has moderate track record of operations of around seven years in the construction of various infrastructure projects all over Nepal, which is likely to benefit it in successfully bidding for contracts and improve order book position over the near-term.

Moderate order book position with low counter party risk

As on January 31, 2023, the unexecuted orders in hand of the company stood at Rs. 1,179 Mn, which is 9x of the income from contract of FY22. The order book is majorly concentrated towards bridge projects (~55% of total order book) and other projects include building and road projects mostly from various government departments including Provincial and local bodies. 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. Timely completion of the projects would be critical for the business prospects of the company and also has a direct bearing on its margins. However, counter party risk over the long term remains low given the projects are from government entities, which have been making timely payment to the company in the past.

About the Company

Narayanam Nirman Sewa Private Limited (NNSPL) is a class "B" construction company of Nepal incorporated in year 2015 with its registered office based in Nepalgunj, Nepal. The company is involved in construction of building, bridges, roads etc. across Nepal. In addition to doing projects independently, NNSPL also enters into Joint Ventures (JVs) with other companies in order to meet the eligibility criteria for different construction projects.

Financial Performance

For the Period	(Rs. Million)		
	FY20 (A)	FY21 (A)	FY22 (A)
Income from Operations	128	363	131
PBILDT Margin (%)	7.52	6.43	18.25
Overall Gearing (times)	1.02	5.03	2.10
Total Outstanding Liabilities/Tangible Net worth (times)	5.90	8.70	7.79
Interest Coverage (times)	6.04	2.46	2.00
Current Ratio (times)	1.09	1.91	2.50
Total Debt/Gross Cash Accruals (times)	2.28	8.21	17.22

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	33.50	CARE-NP B+ [Single B Plus]
Short Term Bank Facilities	Fund Based Limits	9.00	CARE-NP A4 [A Four]
Short Term Bank Facilities	Non Fund Based Limits	1,227.50	CARE-NP A [A Four]
Total		1,270.00	

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About CARE Ratings Nepal Limited:

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