

## Him Sagarmatha Construction Private Limited

### Ratings

Facilities	Amount (Rs. in Million)	Ratings <sup>1</sup>	Rating Action
Long Term Bank Facilities	16.00	CARE-NP BB- [Double B Minus]	Assigned
Short Term Bank Facilities	331.30	CARE-NP A4 [A Four]	Assigned
Long Term/ Short Term Bank Facilities	852.70	CARE-NP BB-/A4 [Double B Minus/A four]	Assigned
Total Facilities	1,200.00 (One Thousand and Two 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 Him Sagarmatha Construction Private Limited (HSCPL).

### Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of HSCPL are constrained by its moderate scale of operations and leveraged capital structure. The ratings also factor in working capital intensive nature of business, 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 experienced promoters and established track record of operations in executing various construction works, adequate orderbook position with mid-term revenue visibility, moderate counter party risk and presence of 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, manage healthy revenue growth and maintain profitability margins without deteriorating its solvency and coverage indicators will be the key rating sensitivities.*

### Detailed Description of the Key Rating Drivers

#### Key Rating Weaknesses

##### Moderate scale of operations and leveraged capital structure

Although the total operating income (TOI) of HSCPL rebounded during FY23 (Unaudited, FY refers to twelve-month period ending mid-July) on account of greater number of project executions during FY23 than in FY22, the scale of operations remained moderate marked by TOI and gross cash accruals (GCA) of Rs. 287 million and Rs. 21 million respectively (FY22: Rs. 86 Mn and Rs. 9 Mn, respectively). Modest scale of operations in a competitive industry could limit the pricing power and benefits of economies of scale.

Capital structure of the company stood leveraged with overall gearing (including mobilization advance) of 2.79x at the end of FY23. Furthermore, total outside liabilities/tangible net worth (TOL/TNW) of the company also stood moderate at 3.26x as on mid-July, 2023 albeit improved from 4.70x on account of improvement in net worth due to accretion of profits in reserve.

#### Working capital intensive nature of business

HSCPL primarily works with various government departments and payments for the contracts are generally received only after the work certification process is completed and bills have been finalized. Lengthy certification processes normally lead to high work in progress and inventory levels. Consequently, operating cycle of the company stood at 56 days primarily on

<sup>1</sup>Complete definitions of the ratings assigned are available at [www.careratingsnepal.com](http://www.careratingsnepal.com) and in other CRNL publications.

account inventory holding period of 67 days in FY23. Furthermore, retention deposit is deducted by the clients from running bills which gets refunded to the contractor only after completion of defect liability period, usually varying from twelve months to five years after successful execution of the contracted work indicating HSCPL's need for reliance on external borrowings to manage its working capital requirements.

### **Tender based nature of operations in highly competitive construction industry**

Majority of the HSCPL'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, HSCPL'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, HSCPL 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.

### **Key Rating Strengths**

#### **Experienced promoters and established track record of operations**

HSCPL has two directors in its Board of Directors chaired by Mr. Surya Prasad Timilsina who has been leading the company since its inception in 1993. He has experience of more than a decade in the field of construction business which bodes well for the overall business prospects of the company in an increasingly competitive industry. Mr. Deepak Khadka, director, has a decade of experience in the field of manufacturing and trading of construction materials, namely aggregates and bricks. Furthermore, the board is supported by an experienced team across various functions. The company has a long track record of operations of over two decades in the construction of various infrastructure projects all over Nepal.

#### **Adequate orderbook position with mid-term revenue visibility**

As on January 16, 2024, the unexecuted orders in hand of the company stood at Rs. 1,910 Mn (share of HSCPL), which is 6.66x of income from contract during FY23, and reflects mid-term revenue visibility for HSCPL. However, the order book is primarily concentrated towards activities related to design, build and maintenance of bridge which exposes the company towards risk of sectoral concentration. Ability of the company to timely execute projects in hand, to regularly bill and realize revenue would be critical for the business prospects of the company and also has a direct bearing on its margins.

#### **Moderate counter party risk and escalation clause in majority of contracts**

Revenue of HSCPL is generated majorly via contracts from government departments with the company having a track record of operations in construction works majorly linked to construction of airport related works. Counter party risk remains moderate given the projects are from government departments.

HSCPL procures its construction materials mainly from the local vendors which exposes the company towards raw material price volatility risk. The risk is somewhat mitigated by the presence of escalation clauses in majority of the contracts which

insulates the company from any adverse fluctuation in construction material prices and labor expenses. This enables the company to pass on increase in raw material prices to its contractee. Ability of the company to pass on increased price burden to the other party on a timely manner and maintain profitability margins is critical from credit perspective.

### Industry Outlook

The construction sector in Nepal has been impacted by lower execution in the aftermath of the COVID-19 pandemic with slower pace of economic growth coupled with relatively lower infrastructure spending by the government. Furthermore, contractors' cash flows have also come under pressure as a result of highly inflated construction costs leading to shrinking margins over FY22-FY23. Furthermore, as government capital expenditure continues to remain substantially lower than budgeted amount, income prospects remain subdued over the near-term which coupled with delays in payments to contractors, has led to some stress in the construction sector in FY23 leading to the slippages in the construction portfolio of BFIs. However, as per the Fiscal Policy for FY24, the government has emphasized spending in infrastructure, energy and industries sector with allocation of budget of Rs. 131,596 Mn. (~8% of total budget) to Ministry of Physical Infrastructure and Transportation and Rs. 87,450 Mn. (~5% of total budget) to Ministry of Energy, Water Resources and Irrigation. The near-term operating environment for construction companies, including HSCPL, would hinge on the government's ability to spend on capital expenditure as budgeted, which has been on the lower side over FY22-FY23.

### About the Company

Him Sagarmatha Construction Private Limited (HSCPL) is a class "B" construction company in Nepal, incorporated on July 14, 1996, with registered office in Kathmandu-16, Nepal. HSCPL is mainly involved in projects associated with construction of bridge and roads. In addition to doing projects independently, HSCPL also enters into Joint Ventures (JVs) with other companies in order to meet the eligibility criteria for different construction projects.

### Financial Performance

(Rs. in Million)

For the period ended/ as at mid-July	FY21 (A)	FY22 (A)	FY23 (UA)
Income from operations	131	86	287
PBILDT Margin (%)	14.78	30.97	13.47
Overall Gearing (times)	2.66	3.94	2.79
Interest Coverage (times)	2.6	1.59	2.80
Current Ratio (times)	1.98	4.46	2.02
Total Debt/ Gross Cash Accruals	5.19	9.36	4.59

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	16.00	CARE-NP BB- [Double B Minus]
Short Term Bank Facilities	Fund Based Limit	40.00	CARE-NP A4 [A Four]
Short Term Bank Facilities (Proposed)	Fund Based Limit	291.30	CARE-NP A4 [A Four]
Long Term/ Short Term Bank Facilities	Non-Fund Based Limit	732.70	CARE-NP BB -/A4 [Double B Minus/A four]
Long Term/ Short Term Bank Facilities (Proposed)	Non-Fund Based Limit	120.00	CARE-NP BB -/A4 [Double B Minus/A four]
<b>Total</b>		<b>1,200.00</b>	

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