

Rating Rationale
BKOI Builders Private Limited

Rating

| Facility | Amount (Rs. In Million) | Rating ¹ | Rating Action |
|--|---|-------------------------------------|------------------|
| Long Term Bank Facilities | 325.59 | CARE-NP BB [Double B] | Reaffirmed |
| Short Term Bank Facilities | 540.00 | CARE-NP A4 [A Four] | Reaffirmed |
| Long Term/ Short Term Bank Facilities | 3,860.00 | CARE-NP BB/A4 [Double B/ A Four] | Reaffirmed |
| Total Facilities | 4,725.59 (Increased from 4,718.93) | | |

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has reaffirmed rating of ‘CARE-NP BB’ assigned to the long term bank facilities and ‘CARE-NP A4’ assigned to the short term bank facilities of BKOI Builders Private Limited (BBPL).

Analytical approach:

CRNL has analysed BBPL’s credit profile by considering the Standalone financial statements.

Detailed Rationale & Key Rating Drivers

The reaffirmation of the ratings assigned to the bank facilities of BBPL factors in decline in total revenue of the company in FY20 (Unaudited, refers to 12 months’ period ended mid-July 2020) mainly due to impact of Covid-19 on the business of the company coupled with increase in the working capital intensity. The ratings continue to be constrained by tender based nature of operations in highly competitive construction industry, planned debt funded capital expenditure and exposure to volatile interest rates. The ratings, however, derive strength from experienced promoters & management in related fields, improvement in PBILDT margin and cash accruals in FY20, moderate capital structure and debt service indicators of the company maintained during FY20 although there was substantial decline in total revenue and established track record in executing various construction works. The rating also factors in BBPL’s healthy order book position with mid-term revenue visibility along with escalation clause in majority of the contracts and moderate counter party risk. Ability of the company to successfully execute projects in time and recover contract proceeds and ability to manage healthy revenue growth and maintain profitability margins without deterioration in its financial risk profile will be key rating sensitivities. Further, ability to manage the impact of Covid-19 on the operations and financials of the company during FY21 will be the key rating sensitivity.

¹Complete definitions of the ratings assigned are available at www.careratingsnepal.com

Impact of Covid-19 on the business of the company

The global outbreak of Coronavirus disease 2019 (Covid-19) has affected Nepal as well. Government of Nepal (GoN) imposed countrywide lockdown since March 24, 2020 halting operations of most of the organizations and slowing down of the economic activities. The construction activities of the company were also subdued on account of the lockdown. Also, since construction activities in Nepal usually takes momentum on second half of the financial year and with country's economy and construction sector being significantly impacted since March 2020, it had a negative impact on the revenue and profitability of the company in comparison to the normal operations. The company's ability to achieve its projected revenue for FY21 and maintain profitability margins will be key rating consideration.

Detailed Description of the Key Rating Drivers**Key Rating Weaknesses*****Financial risk profile marked by decline in revenue, however growth in the profitability and cash accruals in FY20***

Total revenue of the company declined by ~55% in FY20 mainly due to lower execution of order book in hand which was impacted due to Covid-19 resulting into deferment of revenue to next year. Despite decline in total revenue, the company was able to slightly increase PBILDT with improvement in PBILDT margin from 16.62% in FY19 to 37.15% in FY20 majorly due to reduction in price of construction materials in FY20. However, PAT of the company declined by ~58% in FY20 due to increase in interest expenses with increase in short term loan for funding operational requirements of the company and its Joint Venture; and increase in depreciation expenses with purchase of additional fixed assets. Gross Cash Accruals of the company increased marginally during FY20.

Working capital intensive nature of business

The operations of the company are working capital intensive in nature as the company primarily works with government departments and funds are released only after the work certification process is completed and finalization of the bills. Payments for contracts are received in a timely manner within 1-2 months generally, however same has been increased to 3-4 months due to impact of the lockdown period. The total operating cycle of the company was 91 days in FY19 which increased substantially to 189 days in FY20. Further, there is huge amount of work-in-progress amounting to Rs. 278 Mn in FY19 which mainly includes works that are completed by the company, but not yet verified resulting in low revenue booking. These factors lead to reliance of the company on bank finance to meet its working capital requirements.

Tender based nature of operations in highly competitive construction industry

The company receives its work orders from government departments and private entities with majority of the order coming from government departments. The contracts are tender-based and the revenues are dependent on the company's ability to bid successfully for these tenders. The promoter's reasonable experience in related field mitigates risk of competition to some extent. Since there are numerous fragmented and unorganized players

operating in this industry which makes the civil construction space highly competitive, the ability of BBPL to sustain its profitability margins and growth in future remains crucial. Further, the business also remains dependent on stability in government policies and fiscal position of the government.

Planned debt funded capital expenditure

The company has been making regular investments to expand its machinery base in the past and is expected to continue in future. The purchase of fixed assets by the company was mainly funded through bank finance resulting in increase of debt component. Further, the company plans to take additional loan for purchase of equipment/machineries for the new projects proposed to be undertaken in future.

Key Rating Strengths

Experienced promoters in the related fields

BBPL is managed under the overall guidance of the company's three board of directors (BOD) who possess experience in related field. The company is promoted by Mr. Humnath Koirala, managing director, who has long experience of over 39 years in the field of construction business. Similarly, other directors of the company have related experience in construction business. BOD are further supported by an experienced team across various functions/ departments.

Established track record in executing various construction works

BBPL has an established track record of over 11 years in the construction of buildings, roads, bridges, reservoirs, irrigation and water projects ranging from small sized to large sized projects and have executed several projects (majority of which are building projects) across the country in different terrains either individually or through its joint venture (JV) entities.

Healthy order book position with mid-term revenue visibility

Till December 22, 2020; unexecuted orders in hand of the company stood at Rs. 3,235 Mn. Also, the present order book to FY20 revenue on stand-alone basis is around 10.47x which provides healthy revenue visibility. The order book is mainly concentrated in building works (accounting for ~82% of total work order) along with other various projects such as irrigation and water works, bridge works and road works received from various government authorities (majorly) as well as private entities. Timely completion of the projects and increasing its scale of operations would be critical from the credit perspective for BBPL.

Moderate capital structure and debt service coverage indicators of the company in FY20

The capital structure of the company is marked with moderate debt equity ratio of 1.87x and high overall gearing ratio of 4.06x at the end of FY20. Interest coverage ratio of the company was moderate at 2.02x in FY20. Total Outside Liabilities/ Tangible Networth (TOL/TNW) and Total debt/ Gross Cash Accruals of the company was also at moderate level of at 4.65x and 10.25x respectively at the end of FY20.

Moderate counter party risk

Revenue of BBPL is generated via contracts from government departments and private entities related to building works, road works, irrigation and water works etc. Average collection period has increased to 268 days at the end of FY20 from 124 days in FY19 on account of single major bill raised in FY19 to a private party, however BBPL was able to realized major amount till December 29, 2020. However, the counter party risk is moderated by the fact that majority of the construction contracts are obtained from government departments and they are making timely payment to the company in past.

Escalation clause in majority of the contracts

The company has inbuilt price escalation clauses in majority of contracts in order to insulate the company from any adverse fluctuation in construction material prices and labor expenses. This enables the company to pass on increase in construction cost to its customers. Ability of the company to pass on increased price burden to the customers in a timely manner and maintain profitability margins is critical from credit prospective.

About the Company

BKOI Builders Private Limited, incorporated on December 21, 1997, is a mid-scale construction company based in Kathmandu, Nepal. The company is promoted by Mr. Humnath Koirala who holds 62% of total shares of the company. The company has been involved in construction of both small and large scale projects such as buildings works, irrigation works, water supply works, road works etc. across Nepal. BBPL also enters into JV with other companies in order to meet the eligibility criteria for different construction projects. BBPL is being promoted by 5 shareholders who have infused total paid-up equity of Rs. 70 Mn as on July 15, 2020.

Brief financials of BBPL for last three years ending FY20 are given below:

(Rs. Million)

| For the year ended Mid July | FY18 | FY19 | FY20 |
|-----------------------------|-----------|-----------|---------------|
| | (Audited) | (Audited) | (Provisional) |
| Income from Operations | 833 | 875 | 394 |
| PBILDT | 115 | 145 | 146 |
| PAT | 44 | 36 | 9 |
| Overall Gearing (times) | 3.83 | 3.80 | 4.06 |
| TOL/TNW (times) | 5.69 | 5.05 | 4.65 |
| Interest Coverage (times) | 3.55 | 2.03 | 2.02 |

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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 | 325.59 | CARE-NP BB |
| Short Term Bank Facilities | Fund Based Limit | 540.00 | CARE-NP A4 |
| Long Term/Short Term Bank Facilities | Non-Fund Based Limit | 3,860.00 | CARE-NP BB/A4 |
| Total | | 4,725.59 | |