February 2021

Rating Rationale

Om Sai Ram Construction Private Limited

Rating

Facility	Amount (Rs. In Million)	Rating[1]	Rating Action
Long Term Bank Facilities	162.90	**CARE-NP BB [Double B]**	Assigned
Short Term Bank Facilities	5.00	**CARE-NP A4 [A Four]**	Assigned
Long Term/Short Term Bank Facilities	1,832.10	**CARE-NP BB/ A4 [Double B/ A Four]**	Assigned
Total Facilities	**2,000.00**		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has assigned rating of 'CARE-NP BB' to the long term bank facilities and 'CARE-NP A4' to the short term bank facilities of Om Sai Ram Construction Private Limited (OSRC).

Analytical approach:

CRNL has analyzed OSRC's credit profile by considering the standalone financial statements.

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of OSRC are constrained by impact of Covid-19 on the operations of the company leading to decline in revenue and gross cash accruals, however with growth in PBILDT margin during FY20 (Audited, refers to 12 months' period ended mid-July 2020) and leveraged capital structure and debt service coverage indicators of the company at the end of FY20. The rating is also constrained by small scale of operation, high counter party risk however, with improvement in portfolio from private to government clients and concentrated order book position on building projects. Further, rating is constrained by tender based nature of operations in highly competitive construction industry, working capital intensive nature of business, planned debt funded capital expenditure and exposure to volatile interest rates. The ratings, however, derive strength from experienced promoter in construction field, moderate order book position, track record of over 11 years in executing various construction works, healthy liquidity profile of the company, growth in operating income and escalation clause in majority of the contracts. Ability of the company to successfully execute projects in time and recover contract proceeds; and ability to maintain profitability margins with improvement in the capital structure will be key rating sensitivities.

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 operations of the company were

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

moderately disturbed during the lockdown period which has impacted the revenue of the company by extending some of the execution of the projects in FY21 resulting in deferment of revenue. Considering the impact of Covid-19 in the economy of Nepal, the Central Bank of Nepal has provided an extension for the repayment of debt obligations and rebate in interest rate by 2% for the fourth quarter ending mid-July 2020. 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 and gross cash accruals, however growth in PBILDT margin in FY20

Execution of order book in hand was impacted due to Covid-19 resulting into deferment of revenue to next year, however the company managed to book revenue of Rs. 339 Mn during FY20 with ~51% decline as compared to FY19. The company was able to improve PBILDT margin during FY20. Most of the projects of the company were in final stages of completion at the beginning of FY20 where the raw material utilization was on the lower side and with low execution of new projects in hand, lead to improved PBILDT margins. Gross Cash Accruals of the company decreased mainly on account of decrease in profitability.

Leveraged capital structure and debt service coverage indicators with history of dividend payment

The capital structure of the company is marked with debt equity ratio of 3.75x and overall gearing ratio of 4.66x at the end of FY20. The gearing ratio deteriorated mainly on account of increased mobilization advance and high letter of credit for import of construction equipment. However, interest coverage ratio of the company was comfortable at 4.35x in FY20. Total debt/ Gross Cash Accruals (GCA) of the company deteriorated and was high at 8.17x at the end of FY20.

High counter party risk however improvement in portfolio concentration from private to government clients

Revenue of OSRC is generated via construction contract from government departments and private parties. In past 11 years, OSRC generated around 38% of its total revenue from various building projects and one hydropower project belonging to private parties. Revenue billing and payment recovery of ORSC is dependent on availability of funds and liquidity of the private parties. Average collection period of the company was at 85 days at the end of FY20 (vis-à-vis 14 days at the end of FY19). However, OSRC is currently focusing on projects related to government parties due to delay in recovery from private parties. Accordingly, order book from government projects is ~79% of total work in hand which implies the realization from debtors in future will improve as government parties have been making timely payment to the company in past.

Small scale of operations with concentrated order book position on building projects

The company commenced its operations from February 2010 and the operating income stood relatively low in comparison to the other companies in the construction sector in FY20. The entire operations of the company and its order book are concentrated mainly in building projects which accounts for 77% of the total order book.

Tender based nature of operations in highly competitive construction industry

The company receives its work orders from government departments, private parties and other construction companies on sub-contract basis. Work order that comes from government contracts are all tender-based wherein the company has to quote the bid and hence it has to face the risk of successful bidding for the same, which again comes with the risk of quoting a low price to sustain competition. The promoter's reasonable industry experience in related field mitigates risk of competition to some extent. Further, the business also remains dependent on stability in government policies and fiscal position of the government.

Working capital intensive nature of business

The operations of the company are generally working capital intensive in nature as the company works with government departments and private parties. Funds are released only after the work certification process is completed and finalization of the bills. Average debtor days stood at 85 days at the end of FY20 which increased from 14 days at the end of FY19 majorly due to impact of Covid-19 resulted slower realization from private parties. These factors lead to reliance of the company on bank finance or mobilization advances from the customers to meet its working capital requirements.

Planned debt funded capital expenditure

The company has been making regular investments to expand its infrastructure facilities in the past and is expected to continue in future. OSRC is expected to take additional loans for purchase of equipment/machineries for the new projects proposed to be undertaken in future which is expected to be funded through bank loan and equity in the ratio of 70:30.

Key Rating Strengths

Experienced promoters in the related fields and moderate track record of operations

OSRC is promoted by Mr. Bijay Kumar Shah, Managing Director, who has been leading the company since its inception from February 2010. He manages overall projects executed by the company since 2010. Further, the board is supported by an experienced team across various functions.

Moderate order book position with mid-term revenue visibility and diversified projects

As on December 24, 2020, the unexecuted orders in hand of the company stood at Rs. 1,020 Mn. Also, the present order book to FY20 revenue is around 3.01x which provides medium term revenue visibility. The order book is primarily concentrated towards building works (~77%) and rest of the works includes bridge works, road works and irrigation works. Timely completion of the projects and thereby increasing its scale of operations would be critical from the credit perspective for OSRC.

Healthy liquidity profile of the company

The company has comfortable liquidity position on account of surplus funds available in the form of advance mobilization money which are interest free. The average working capital utilization of the company was at ~4% for last twelve months ending mid- January, 2021. Also given the inherent cyclicality in the construction industry, lower reliance on external financing remains a positive, especially given the rising interest rates for bank borrowings in the past and impact over business operations due to Covid-19 pandemic.

About the Company

Om Sai Ram Construction Private Limited (OSRC), incorporated on February 24, 2010, is a Class-A construction company of Nepal with registered office based in Satdobato, Lalitpur, Nepal. The company is involved in construction of both small and large scale projects mainly relating to road works, building works, bridge works, irrigation works etc. in different part of Nepal. In addition to doing projects independently, OSRC also enters into Joint Ventures (JVs) with other companies in order to meet the eligibility criteria for construction projects.

Brief financials of OSRC (Standalone) for last three years ending FY20 are given below:

(Rs. Million)

For the year ended Mid July	FY18	FY19	FY20
	(Audited)	(Audited)	(Audited)
Income from Operations	501	684	339
PBILDT Margin (%)	9.85	12.52	23.39
Overall Gearing (times)	2.62	2.11	4.63
Total Outstanding Liabilities/Tangible Net worth (times)	5.62	5.14	8.01
Interest Coverage (times)	6.55	5.00	4.35
Current Ratio (times)	1.04	1.05	1.00
Total Debt/ Gross Cash Accruals (times)	5.59	3.43	8.12

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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 Loans	162.90	CARE-NP BB
Short Term Bank Facilities	Fund Based Limits	5.00	CARE-NP A4
Long Term/ Short Term Bank Facilities	Non-Fund Based Limits	1,832.10	CARE-NP BB/ A4
Total		**2,000.00**	