

Rating Rationale

Kankai International Builders Private Limited

Rating

| Facility | Amount (Rs. In Million) | Rating ¹ | Rating Action |
|--|---|---|------------------|
| Long Term Bank Facilities | 51.66 | CARE-NP BB+ [Double B Plus] | Reaffirmed |
| Short Term Bank Facilities | 42.29 | CARE-NP A4+ [A Four Plus] | Reaffirmed |
| Long Term/ Short Term Bank Facilities | 2,906.05 | CARE-NP BB+/A4+ [Double B Plus/ A Four Plus] | Reaffirmed |
| Total Facilities | 3,000.00 (Increased from Rs. 2,147.75 Mn.) | | |

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 Kankai International Builders Private Limited (KIB).

Analytical approach:

CRNL has analyzed KIB’s credit profile by considering the consolidated financial statements (comprising KIB and its joint venture entities related to the construction works) owing to financial and operational linkages between the KIB and JV entities.

Detailed Rationale & Key Rating Drivers

The reaffirmation of the ratings assigned to the bank facilities of KIB factor in working capital intensive nature of business and its presence in highly competitive construction industry coupled with tender based nature of operation. The ratings are also constrained by exposure to volatile interest rates and risk of delay in project execution.

The ratings, however, derive strength from experienced promoters & management team coupled with established track of operations, moderate order book position, moderate financial risk profile, moderate counter party risk and escalation clause in majority of the contracts.

Going forward, the ability of the company to profitably scale up its operations amidst high level of competition, maintaining its financial risk profile and recover contract proceeds will be key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

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

Working capital intensive nature of business

The company works with government departments either directly or through subcontract basis. Payments for government contracts are mostly received within few days after presenting the bill. Additionally, due to delay in approval of bills by government departments, KIB has been facing some delay in sales realization. However, inventory holding period of the company stands at lower side on account of available of standby vehicles with the company to transport materials as and when required. Also, KIB has high retention money due to the nature of the business. 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 mainly caters to orders received from various Government entities and other Government establishments either directly or on sub-contract basis. The high concentration on government contracts also makes the company susceptible to any changes pertaining to government policy in regard to awarding tenders to contractors. The tender-based business is characterized by intense competition and the growth of the business depends on its ability to successfully bid for the tenders and emerge as the lowest bidder. Furthermore, the business also remains dependent on stability in government policies and fiscal position of the government.

Risk of delay in project execution

KIB's business is susceptible to the financial loss arising out of delay in project execution, as generally, there is a penalty clause for delay in contract execution. However, KIB has relied on the experience of its management team with strong project execution skills which has enabled the company to build satisfactory standing in the industry as indicated by the repeat orders awarded by its clients.

Key Rating Strengths***Experienced promoters & established track record of operations***

KIB is being promoted by Mr. Ram Prasad Mainali and his family members. Mr. Ram Prasad Mainali, Chairman, has been leading the company since its inception from 1987. He looks after day-to-day operations of the company. Board of Directors are further supported by an experienced team across various functions/ departments.

KIB started operations in 1987 and has over 3 decades in the construction of roads, bridges, water and sanitation projects, civil construction and irrigation projects etc. The long track record has enabled the company to establish relations with its customers thereby resulting into repetitive orders/ tenders from the government departments.

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

As on March end, 2021, the unexecuted orders in hand of the company stood at Rs. 8,467 Mn. on consolidated basis and Rs. 2,979 Mn. on standalone basis. The tenure of the orders undertaken by the company is up to 36 months, thereby providing revenue visibility in short to medium term. The order book is diversified towards water supply & sanitation works (~65%), irrigation works (~20%), road works (~10%) & bridge works (~5%). Timely completion of the projects and thereby increasing its scale of operations with building up new order books would be critical from the credit perspective.

Moderate financial risk profile

For the period FY18-FY20 (Audited, refers to 12 months’ period ended mid-July 2020), KIB’s total operating income grew from Rs. 1,330 Mn. in FY18 to Rs. 1,561 Mn. in FY20 reflecting a compounded annual growth rate of around 6%. The growth in revenue of the company was mainly in FY20 due to execution of different projects. Profitability margins of the company has been improving on y-o-y basis in the last 3 FYs from 7.68% in FY18 to 9.87% in FY20. The improvement in margins was mainly attributed to economies of scale and execution of better margins contracts. Though profitability margins improved, it continued to remained at moderate levels.

The capital structure of the company is comfortable marked by debt equity ratio of 0.67x and overall gearing ratio of 0.76x at the end of FY20. As on July 15, 2020, overall gearing ratio of the company improved over previous balance sheet date mainly on account of scheduled repayment of long term loan. Though, the capital structure improved, interest coverage ratio of the company moderated and stood 6.38x in FY20 as against 7.66x in FY19. The moderation was on account of increase in finance expenses which was increased on account of higher utilization of average working capital borrowings. As on July 15, 2020, TOL/ TNW of the company stood high and deteriorated from 3.10x in FY19 to 3.43x in FY20 due to increase in sundry creditors. Total debt/ GCA of the company stands at 1.62x at the end of FY20.

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 raw material prices 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 perspective.

About the Company

Kankai International Builders Private Limited (KIB) is a private limited company, incorporated in July 26, 1987 with registered office based in Jhapa, Nepal. KIB is an ISO 9001:2015 certified on December 2020. In addition to doing projects independently, KIB also enters into Joint Ventures (JVs) with other companies in order to meet the eligibility criteria for different construction projects.

Brief financials of KIB (Consolidated) for last three years ending FY20 are given below:

| For the year ended Mid July | (Rs. Million) | | |
|--|-------------------|-------------------|-------------------|
| | FY18 (Audited) | FY19 (Audited) | FY20 (Audited) |
| Income from Operations | 1,330 | 1,517 | 1,561 |
| PBILDT Margin (%) | 7.68 | 8.51 | 9.87 |
| Overall Gearing (times) | 0.90 | 1.01 | 0.76 |
| Total Outstanding Liabilities/Tangible Net worth (times) | 2.08 | 3.10 | 3.43 |
| Interest Coverage (times) | 5.37 | 7.66 | 6.38 |
| Current Ratio (times) | 1.45 | 1.17 | 1.15 |
| Total Debt/ Gross Cash Accruals (times) | 2.51 | 2.32 | 1.62 |

| | | |
|--|--|---|
| Analyst Contact Mr. Nibesh Manandhar nibesh.manandhar@careratingsnepal.com Tel No.: +977-01-4445473 | Group Head Ms. Shalini Sanghai shalini.sanghai@careratingsnepal.com Tel No.: +977-01-4012629 | Relationship Contact Mr. Achin Nirwani achin.nirwani@careratingsnepal.com Tel No.: 9818236069/+977-01-4012628/29/30 |
|--|--|---|

Disclaimer

CRNL's ratings are opinions on credit quality and are not recommendations to sanction, renew, disburse or recall the concerned bank facilities or to buy, sell or hold any security. CRNL has based its ratings on information obtained from sources believed by it to be accurate and reliable. CRNL does not, however, guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. Most entities whose bank facilities/instruments are rated by CRNL have paid a credit rating fee, based on the amount and type of bank facilities/instruments.

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 | 51.66 | CARE-NP BB+ |
| Short Term Bank Facilities | Working Capital Loans | 42.29 | CARE-NP A4+ |
| Long Term/ Short Term Bank Facilities | Non-Funded Loans | 1,707.00 | CARE-NP BB/ A4 |
| Long Term/ Short Term Bank Facilities (Proposed) | Non-Funded Loans | 1,199.05 | CARE-NP BB+/ A4+ |
| Total | | 3,000.00 | |