

Kumar Shrestha Nirman Sewa Private Limited

Ratings

Facilities	Amount (Rs. in Million)	Ratings ¹	Rating Action
Long Term Bank Facilities –Term Loan	498.20 (Reduced from 632.94)	CARE-NP BB+ [Double B Plus]	Reaffirmed & Removal from issuer not cooperating
Short Term Bank Facilities- Working Capital Loan	420.00 (Increased from 360.00)	CARE-NP A4+ [A Four Plus]	Reaffirmed & Removal from issuer not cooperating
Long Term/Short Term Bank Facilities- Non-Funded Loan	8,281.80 (Increased from 8,020.00)	CARE-NP BB+/A4+ [Double B Plus/A Four Plus]	Reaffirmed & Removal from issuer not cooperating
Long/Short Term Bank Facilities- Non-Funded Loan (Enhanced)	1,800.00	CARE-NP BB+/A4+ [Double B Plus/A Four Plus]	Assigned
Total Bank Facilities	11,000.00 (Eleven Billion) (Increased from 9,012.94)		

Details of instruments/facilities in Annexure-1

CARE Ratings Nepal Limited (CRNL) has reaffirmed rating of ‘CARE-NP BB+’ to the long term bank facilities and ‘CARE-NP A4+’ to the short term bank facilities of Kumar Shrestha Nirman Sewa Private Limited (KSNS).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of KSNS continues to be constrained by its fluctuating scale of operations, leveraged capital structure, low order book position and exposure to volatile interest rates. The ratings are also constrained by tender based nature of operations and risk related to delay in project execution. Additionally, the ratings also factor in planned debt funded capital expenditure leading to expected moderation in overall gearing.

The ratings, however, continues to derive strength from experienced promoters and long track record of operations in execution of various construction contracts, moderate profitability and debt service coverage indicators, moderate counter party risk and escalation clause in majority of the contracts. The ratings also factors in ownership of sizeable equipment & machineries providing execution capabilities to the company and moderate operating cycle.

Going forward, the ability of the company to profitably scale up its operations while successfully executing the projects on time and managing its working capital requirements to support growth will act as the key rating sensitivities. Furthermore, increasing the orderbook portfolio is also crucial and act as rating sensitivity.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Leveraged capital structure of the company however improved year on year basis

As on Mid-July 2021, the capital structure of the company stood leveraged on account of high dependence on working capital borrowings. Though, there has been an improvement in the overall gearing of the company (including mobilization advance) from 3.76x at the end of FY20 to 2.84x at the end of FY21, it continued to remain high. Overall

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

gearing ratio improved mainly on account of increase in networth which was partially offset by additional term loans taken by the company for purchase of machineries/ equipment and increase in mobilization advance money (against bank guarantees) along with increase in working capital borrowings. Working capital loans of the company significantly increased by ~81% in FY21 majorly to fund the growing operations coupled with delay in realisation leading to additional requirements of funds. Furthermore, the company is paying regular dividend in last 2 years leading to lower accretion of profits to reverses.

Low order book position with short term revenue visibility, however diversified in various projects

The order book position of the company stood at Rs. 5,157 Mn (share of KSNS in joint ventures) as on mid-August 2021. The order book reflects near to short term revenue visibility, as it is around 1.56 times of FY21 total operating income (TOI). The tenure of the orders undertaken by the company is up to 30 months. The order book of the company is diversified over various projects such as civil works, road works, irrigation and water works (river training works, canal works, embankment construction etc.), infrastructure projects and railway work received from various government authorities.

Tender based nature of operations in highly competitive construction industry and fluctuating scale of operations

The company receives its work orders from government departments and private entities constituting with majority of the order coming from government contracts. 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. The company mainly caters to orders received from various Government entities and other Government establishments. 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. KSNS has to participate in the tenders floated by various government agencies which can be lengthy at times. Moreover the company is dependent on government spending for the total capital expenditure presented in the budget every year.

Planned debt funded capital expenditure with ownership of sizeable equipment and machineries

The company has been making regular investments to expand its execution capabilities in the past and expected to continue in future. The investment in equipment/ machineries was Rs. 217 Mn in FY20 and Rs. 28 Mn in FY21 with total fixed asset of Rs. 1,375 Mn at the end of FY21 (on standalone basis). The purchase of fixed assets by the company was mainly debt funded. Furthermore, it is expected that the company will take additional loan for purchase of equipment/machineries for the new projects proposed to be undertaken in future which is expected to impact overall gearing ratio of the company.

Risk of delay in project execution

KSNS'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, KSNS 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

Long track record of operations and experienced promoters in the related fields

The company has long track record of operations of over 4 decades in construction of various infrastructure projects all over Nepal. KSNS is promoted by Mr. Prem Kumar Shrestha and his family members. Mr. Prem Kumar Shrestha,

Managing Director, has extensive experience of over 4 decades in the field of construction contract business and is responsible for day to day operations of the business. He is assisted by his sons Mr. Sushil Kumar Shrestha (Executive Director) and Mr. Sujeet Kumar Shrestha (Director) who have significant experience in the construction sector. Board of Directors are further supported by an experienced team across various functions/ departments.

Moderate profitability margins and debt service coverage indicators

During FY21, total revenue of the company improved by 46% to Rs 3,306 Mn mainly due to increase in execution of the contracts in hand during FY21 which were hampered during FY20 due to Covid-19 recurring lockdown. Profitability margins of the company are directly associated with technical aspect of the contract. The company undertakes contracts which are complex in nature and due to experience in construction field, PBIDLT margin of the company are moderate. However high dependence on external borrowings and depreciation expenses, PAT margin of the company remained low at around 3% in last two year ending FY21.

Debt coverage indicators of the company stood moderate, marked by total debt to gross cash accruals (GCA) and interest coverage of below 9x and above 3x respectively in last three FYs (FY19, FY20 & FY21).

Moderate operating cycle which were supported by advance mobilization

KSNS primarily works with the government departments and payments for the contracts are received generally within a month. Also, KSNS maintained construction materials as an inventory for around 2 months which are required to keep at various sites for smooth execution of contracts. Average credit period provided by the suppliers is generally upto 2 months. Retention money is deducted by the clients from running bills which will get refunded to the contractor after certain period, usually 1 year, on successful execution of contracted work. This has resulted moderate operating cycle of 49 days in FY21. Accordingly, the average working capital utilization of the company was at ~77% for last four quarters ending mid- July, 2021.

Also, company receives maximum 20% of the contract amount as advance mobilization money and the same are interest free which were fully utilized for execution of construction contracts and funding its working capital needs which had helped to fund without any extra finance cost.

Moderate counter party risk

Revenue of KSNS is generated via contracts majority from government departments through tender and subcontract basis. Average collection period of the company was at 31 days in FY21 (vis-à-vis 48 days in FY20) reflecting timely collection of amount dues form government department. Also, the counter party risk is moderated by the fact most of the construction contracts are obtained from government departments and it has been 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 from government departments in order to insulate the company from any adverse fluctuation in raw material prices and labor expenses. Any changes in price have to be informed beforehand and mutually decided between both parties. 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 the credit perspective.

Analytical approach:

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

About the Company

Kumar Shrestha Nirman Sewa Private Limited (KSNS), incorporated on February 28, 1998 as a Class-A construction company of Nepal with registered office based in Kanchanpur, Nepal. The company also enters into Joint Ventures (JVs) with other companies in order to meet the eligibility criteria for different construction projects for bidding and execution of contracts.

Financial Performance: Consolidated

For the year ended Mid July	<i>(Rs. Million)</i>		
	2019 (12m, A)	2020 (12m, A)	2021 (12m, UA)
Income from Operations	4,227	2,265	3,306
PBILDT Margin (%)	8.45	15.44	11.99
Overall Gearing (times)	4.04	3.76	2.84
Total Outstanding Liabilities/Tangible Net worth (times)	7.04	5.51	3.63
Interest Coverage (times)	5.03	3.55	4.54
Current Ratio (times)	1.50	1.33	1.59
Total Debt/ Gross Cash Accruals (times)	7.94	8.74	8.73

A: Audited, UA: Unaudited

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 Loans	498.20	CARE-NP BB+
Short Term Bank Facilities	Working Capital Loans	420.00	CARE-NP A4+
Long Term/ Short Term Bank Facilities	Non-Funded Loans	10,081.80	CARE-NP BB+/ A4+
Total		11,000.00	

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