Divya Jyoti Construction Private Limited

Ratings

Facilities	Amount (Rs. in Million)	Ratings[1]	Rating Action
Long Term Bank Facilities	14.52	CARE-NP B+ [B Plus]	Assigned
Short Term Bank Facilities	40.00	CARE-NP A4 [A Four]	Assigned
Long Term/Short Term Bank Facilities	600.48	CARE-NP B+/A4 [B Plus/A Four]	Assigned
Total Facilities	655.00 (Six Hundred and Fifty Five Millions Only)		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has assigned the ratings of 'CARE-NP B+' to the long term bank facilities and 'CARE-NP A4' to the short term bank facilities of Divya Jyoti Construction Private Limited (DJCL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of DJCL are constrained by small scale of operations with low profitability, working capital intensive of the business, and its presence in highly competitive construction industry coupled with tender based nature of operations. 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, moderate capital structure & debt service coverage indicators 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 and manage its working capital requirements to support growth will be crucial and act as the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Small scale of operations with low profitability margins

DJCL is a relatively small player in business of construction. The ability of the company to scale up to larger-sized contracts having better operating margins is constrained by its comparatively low capital base of Rs 10 Mn as on mid-July, 2021 and total operating income of Rs. 164 Mn in FY21 (unaudited; FY refers to 12 months' period of mid-July 2020 to mid-July 2021). The small scale of operations in a competitive industry limits the pricing power and benefits of economies of scale. Furthermore, DJCL's total operating income has been fluctuating over the past three years (FY19-FY21.). TOI has registered a decline on y-o-y basis in FY20 and registers a growth in FY21.

The company's profitability margins have been historically on the lower side owing to intense market competition. This apart, interest burden on working capital borrowing also restricts the net profitability of the company. For FY21, PBIDLT margins stood at 5.28% with low PAT margin. The margins of DJCL is lower compared with other players as it derives a substantial amount of revenue from low margin contracts.

Leveraged capital structure

The capital structure of DJCL was leveraged with overall gearing ratio (including mobilization advance) of 1.82x at the end of FY21 which deteriorated from 1.00x at the end of FY20. Total debt of the company which mainly comprises of hire purchase loans, mobilization advance & working capital borrowings increased in FY21 on account of higher reliance on working capital loan to finance increased working capital requirements contributed by delayed payments and contract period extension by the government. Also, total outside liability to total networth and total debt to gross cash accruals

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

remained high at 3.16x and 13.60x respectively at the end of FY21 (~vis-à-vis 3.72x and 10.77x respectively at the end of FY20) however, the interest coverage stood moderate at 1.95x in FY20 & FY21

Working capital intensive business

The operations of the company are working capital intensive in nature marked by high operating cycle of 112 days and below unity current ratio as on FY21. The operating cycle remained high on account of high average inventory days of 160 as on FY21 contributed by majority projects being at initial stage which were delayed due to pandemic and extension of contracts by the government despite average receivable days of 10 days and average creditors days of 57 days at the end of FY21. Due to elongated operating cycle, the working capital utilization of DJCL remained high at around ~95%. Current ratio remained weak at below unity and quick ratio of 0.12x for FY21.

Tender based nature of operations in highly competitive construction industry

The company receives its entire work orders from government departments related majorly to road works along with bridge works, building works, water supply and sanitation works, hydro works, site improvement works and irrigation & river training works. 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

DJCL'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, DJCL 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

DJCL is promoted by Mr. Shivaram Bhandari and Mrs. Indu Bhandari. Mr. Shivaram, Managing Director, holds 25 years of experience in construction management and manages overall affairs of the company. Mrs. Indu Bhandari, Director, is looking after the accounts and finance department. By virtue of long experience of the promoters; the company has been able to attract experienced professionals from the industry, who adequately support the directors.

Moderate order book position

As on mid-October 2021, the unexecuted order of the company stood at Rs. 363 Mn (including share of DJCL in JV's) which is approximately 2.22 times of its operating income for FY21. The tenure of the order undertaken by the company is up to 16 months giving near-term revenue visibility. The order book is majorly concentrated to road works (~89% of outstanding work) with diversification into bridge work (~7% of outstanding work) and water supply & sanitation work (~3% of outstanding work).

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.

Analytical approach:

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

About the Company

Divya Jyoti Construction Pvt. Ltd. (DJCL) was incorporated in 2014 and took over the business Bandhu Nirman Sewa which was established in 1993. DJCL is a "C" class construction company with registered office based in Neelkantha-03, Dhading. The company is mainly involved in construction of road, bridge, civil & hydro mechanical, irrigation, water supply & sanitation, etc. DJCL also enters into Joint Ventures (JVs) with other companies in order to meet the eligibility criteria for different construction projects.

Brief financials of DJCL (Standalone) for last three years ending FY21 are given below:

(Rs. Million)

For the Period Ended / as at Mid-July,	2019 (12m, A)	2020 (12m, A)	2021 (12m, UA)
Income from Operations	**222**	**82**	**164**
PBILDT Margin (%)	**5.78**	**6.98**	**5.28**
Overall Gearing (times)	**0.96**	**1.00**	**1.82**
Total Outstanding Liabilities/Tangible Net worth (times)	**3.14**	**3.72**	**3.16**
Interest Coverage (times)	**4.03**	**1.95**	**1.95**
Current Ratio (times)	**1.24**	**0.97**	**0.97**
Total Debt/ Gross Cash Accruals (times)	**4.77**	**10.77**	**13.60**

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**	**14.52**	**CARE-NP B+ [B Plus]**
Short Term Bank Facilities	**Working Capital Loans**	**40.00**	**CARE-NP A4 [A Four]**
Long Term/ Short Term Bank Facilities	**Non-Funded Loans**	**600.48**	**CARE-NP B+/ A4 [B Plus/A Four]**
Total		**655.00**	

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About CARE Ratings Nepal Limited:

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