

Padma Colony Private Limited

Ratings

Facilities	Amount (Rs. in Million)	Ratings ¹	Rating Action
Long Term Bank Facilities	78.39	CARE-NP B [Single B]	Assigned
Short Term Bank Facilities	949.22	CARE-NP A4 [A Four]	Assigned
Total Facilities	1,027.62 (One Billion Twenty Seven Million Six Hundred and Twenty Thousands Only)		

Details of Facilities in Annexure 1

Care Ratings Nepal Limited (CRNL) has assigned the rating of 'CARE-NP B' to the long term bank facilities and the rating of 'CARE-NP A4' to the short-term bank facilities of Padma Colony Private Limited (PCPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of PCPL are constrained by project implementation and funding risk associated with its under-development housing projects, intense competition and fragmentation in the housing industry impacting saleability, inherent risk associated with the real estate industry and exposure to volatile interest rates.

The ratings, however, derive strength from experienced promoter and established track record of operations in the industry, strategic location of the proposed housing projects, and sluggish demand in the near term on account of tightened monetary policy.

Going forward, the ability of the company to timely complete the project within estimated cost and time, achieving envisaged sales coupled with timely collection of customer receipts will be key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Project implementation risk and funding risk associated with under development projects

PCPL is currently developing two housing projects, one at Ramkot, Kathmandu (Phase V with 300 units) and another at Itahari, Sunsari (Phase VI with 200 units) with estimate costs of Rs. 3,500 Mn and Rs. 2,180 Mn respectively. In Phase V, around 90% of the land acquisition has been completed with the site development works ongoing, whereas the company has completed around half of the land acquisition in Phase VI. Civil construction works are expected to commence from the beginning of 2024. The funding for both the projects are yet to be fully tied up, leading to funding risk associated with the projects. The projects will be funded in the debt to equity in the ratio of 80:20, where the debt portion will be funded as working capital loan, and the equity will be infused by the promoters as per the progress of the projects.

Dependence on outside debt for financing the projects with relatively higher debt mix

The costs of both the projects are proposed to be funded in the debt to equity ratio of 80:20, thus creating higher dependence on outside debt for financing the projects. The company has planned to start the booking of houses only after 80% of project completion, which will be roughly two years from the date of start of construction. Until then, the company's capital structure is expected to remain leveraged.

Inherent risk associated with the intensely competitive and fragmented real estate industry

For real estate sector, with consumers becoming more discerning, ready-to-move-in homes are expected to be a major demand driver in the coming period. However, as developers continue to focus on reducing their present inventory, before launching

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

new projects, the demand trend in the industry plays a crucial role. The developer's track record, quality of construction and delivery timelines will be crucial aspects that home buyers will consider in their purchase decisions. Furthermore, Budget 2022/23 and the Finance Act have increased the capital gains tax on real estate transactions to 7.5% from 5%. Although Government Economic Survey 2020/21 shows increasing trend in real estate transaction, this has remained sluggish in FY22 amid the economic slowdown and credit crunch in the banking sector. Furthermore, the real estate industry in Nepal is highly fragmented with the presence of a large number of organized and unorganized players spread across various regions. In addition to many well-established players, there are many independent players in the market, which offer houses at competitive prices, thereby posing threat to companies like PCPL.

Cyclical and seasonality associated with real estate industry and exposure to volatile interest rate

The life cycle of a real estate project is long and the state of the economy at every point in time, right from land acquisition to construction to actual delivery, has an impact on the project. The sector is capital intensive, and is extremely vulnerable to the economic cycles. Currently, slowdown in sales and increased input costs has increased liquidity concerns for highly leveraged players. The company is exposed to the cyclical nature associated with real estate sector which has direct linkage with the general macroeconomic scenario, interest rates and level of disposable income available with individuals. The real estate sector is sensitive to the economic cycle and interest rates. Adverse movement in interest rate affects the real estate players in both ways - by hampering demand as well as increasing the cost of construction. With elevated interest rates, the real estate sector is expected to witness slowdown in the coming fiscals. With cost of ownership elevated amid higher interest rates, a lot of the buyers postpone their purchase decisions, which could impact the salability of upcoming projects.

Key Rating Strengths

Experienced promoter and established track record of operations in the industry

PHPL is promoted by Mr. Raju Prasad Kadel, Chairman, who is also the Chairman of Padma Group of Companies. In addition, Mr. Kadel is also the Chairman in Padma Hospitality Private Limited [CARE-NP A4], Padma Merchant Company Private Limited, Dhunibesi Adarsha Multiple College and Jagadguru Kripalu Pratisthan, and Senior Vice President in Media Alliance Nepal. Padma Group of Companies was started by Mr. Kadel with a real estate venture called Padma Colony Phase I in 2003, and is now a group of more than fifteen companies in six sectors. PCPL has successfully developed and sold two housing projects, namely Padma Colony Phase I and Padma Colony Phase II.

Strategic location of the proposed housing projects

Padma Colony Phase V is situated in Ramkot, Kathmandu, around 6 km from the Kathmandu Ringroad. Kathmandu being the capital city has access to numerous educational institutions, hospitals, financial institutions, shopping malls, retail shops, and other job opportunities within close proximity. Also, with the increasing tendency of the people to live far from the hustles of the city, while having close enough access to better services and facilities, Ramkot fits the bill as a favorable location for residential purpose. Similarly, Padma Colony Phase VI is located in Itahari, Sunsari, which is the second most populous city in Eastern region of Nepal. Situated at a distance of 25 km North of the provincial capital of Biratnagar, 16 km South of Dharan and 92 Km west of Kakarbhitta, Itahari serves as one of the major stopping point in the East-West Highway as well as the North-South Koshi Highway. Strategic location reduces salability risk associated with both the projects.

Industry Outlook

Real estate has been one of the major sectors for financial institutions lending over the years. The increase in the demand for land and building, especially in urban areas has been recognized due to inelastic supply of land and absence of viable investment opportunity. The investment in apartments and colonies has been increasing due to change in people preference towards ready to move homes as compared to self-constructed houses. However, the real estate loan to value ratio (Real estate loan to Fair Market value of mortgage) which was 40% inside Kathmandu valley and 50% outside valley has been further tightened by Monetary Policy 2022/23 thus reducing the loan to value ratio to 30% within Kathmandu valley and

40% outside Kathmandu valley, limiting the investment of fund towards real estate sector. With the limitation created in real estate loan and residential housing loan coupled with higher funding cost on account of the ongoing liquidity crisis, the demand of real estate sector is likely to remain muted over the near-term, although expected to improve over the medium term as the economy recovers.

About the Company

Padma Colony Private Limited (PCPL) was incorporated on November 19, 2008 under the Company Act, 2008. The company is engaged in real estate business. PCPL acquires land, develops residential colonies and sells the individual housing units in the market. The company has already developed and sold two housing projects (Phase I and II), and has two projects under development (Phase V and VI).

Annexure 1: Details of the Facilities rated

Nature of the Facility	Type of the Facility	Amount (Rs. in Million)	Rating
Long Term Bank Facilities	Fixed Term Loan	78.39	CARE-NP B
Short Term Bank Facilities	Fund Based/ Non Fund Based Limits	949.22	CARE-NP A4
Total		1,027.61	

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About CARE Ratings:

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Our parent company, CARE Ratings Limited commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI).

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