

Buddha Himali Construction Private Limited

Ratings

Facilities	Amount (Rs. in Million)	Ratings ¹	Rating Action
Long Term Bank Facilities	24.24	CARE-NP B+ [Single B Plus]	Assigned
Short Term Bank Facilities	975.76	CARE-NP A4 [A Four]	Assigned
Total Facilities	1,000.00 (One Thousand Million 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 Buddha Himali Construction Private Limited (BHC).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of BHC are constrained by the company's leveraged capital structure with low capital base and high gearing level at the end of FY22 (Audited; FY refers to the twelve-month period ending mid-July). The ratings also factor in the tender based nature of operations in highly competitive construction industry, risk of delay in project execution and timely recovery of contract proceeds, particularly amid the ongoing slowdown in infrastructure spending by the government.

The ratings, however, derive strengths from experienced promoter in the related field with long track record in execution of various construction works, moderate order book position with diversified order book, moderate counter party risk and escalation clause in majority of contracts.

Going forward, the ability of the company to successfully execute projects and recover contract proceeds in timely manner, manage healthy revenue growth and maintain profitability leading to improvement in its financial risk profile will be key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Low capital base with leveraged capital structure

BHC's ability to scale up to larger-sized contracts having better operating margins is constrained by its comparatively low net worth of Rs. 29 Mn at the end of FY22, although increased from Rs. 14 Mn at the end of FY21. Modest scale of operations in a competitive industry limits pricing power and benefits of economies of scale. However, the risk is partially mitigated by the fact that the scale of operations is growing steadily. Capital structure of the firm stood moderately leveraged as reflected from moderate overall gearing (including mobilization advance) of 2.82x on mid-July 2022 (PY: 2.38x). Furthermore, Total Outside Liabilities (TOL)/ Tangible Net Worth (TNW) of the company stood high at 8.88x as on mid-July 2022 which improved from 10.05x as on previous balance sheet date.

Tender based nature of operations in highly competitive construction industry

The company receives its majority work orders from government departments and local authorities. All contracts are tender-based for which BHC has to participate in the tenders, 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 at low price through e-bidding to sustain the competition. BHC enters into construction contracts either individually or through JV entities in order to meet eligibility criteria for these contracts.

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

There are numerous fragmented and unorganized players operating in this industry which makes the industry highly competitive and the ability of BHC to sustain its profitability margins and growth in future remain crucial. Furthermore, the business also remains dependent on stability in government policies and fiscal position of the government. Government of Nepal (GoN) has put certain restrictions on the contractors to participate in tenders such as prohibiting foreign companies to participate in tenders having value less than Rs. 5,000 Mn, which augurs well for domestic players. Furthermore, the GoN has also placed a cap on total active projects of construction companies at five, which could limit growth prospects.

Risk of delay in project execution and timely realization of proceed of contracts

Given the nature of projects awarded, BHC is exposed to inherent risk in terms of delays in certain projects undertaken by the company due to delay in procedural approvals and clearance of project sites, etc., thus exposing the company towards the risk of delay in projects further resulting a delayed realization of revenue growth. Furthermore, the company's ability to execute projects in timely manner would be led by its own operational efficiency and timely stage payments received from clients. Although counter party risk over the medium term remains moderate given the projects are from government departments, which have been making timely payment to the company in the past, timely debtor realization, particularly at times of economic downturn, remains a key challenge for the construction sector. Presence of escalation clause in majority of the contracts enable the company to pass increase in raw material prices to its customers. Ability of the company to pass increased burden to the customer in a timely manner and maintain profitability margins is critical from a credit perspective.

Exposure to volatile interest rates

The company's interest rates are based on a floating interest rate regime, where a certain premium is added to the quarterly base rate and interest rate is changed accordingly on quarterly basis. The base rates of the banks and financial institutions (BFIs) in Nepal remain quite volatile as they are impacted by available liquidity in the system which leads to change in interest rates. Therefore, funding taken by the company from BFIs is subject to volatile interest rate.

Key Rating Strengths

Experienced promoter in the related field with long track record in operations

BHC was promoted by four directors chaired by Mr. Vijay Roka, who has an experience of more than two decades in the construction sector. Mr. Dhan Bahadur Budha, Director, also has an experience of over two decades in the construction field. Mr. Him Bahadur Budha, Director, is responsible for overall function of the company and has experience in several fields including construction. The company has a track record of 20 years in construction of commercial buildings, water supply projects, river training and road upgrading from small to large size projects and has executed several projects across the country in different terrains either individually or through its Joint Venture (JV) entities. Long track record has enabled the company to gain experience thereby resulting in efficient execution of projects.

Moderate order book position with diversified order book.

The unexecuted order book of the company as on March 27, 2023 was Rs. 523 Mn (share of BHC only), providing moderate revenue visibility. The tenure of the orders undertaken by the company is up to 12-24 months. The order book of the company is diversified with most of the outstanding works in water supply projects (~35.21% of the total order book), followed by building projects (~28.85% of the total order book), road upgrading (~23.97% of the total order book) and river training (~11.98 % of the total order book).

Moderate counter party risk and escalation clause in majority of contracts

Revenue of BHC is majorly generated via contracts from government departments, provincial bodies and local government. The order book is primarily concentrated towards road projects from government departments. Counter party risk remains moderate given the projects are from government departments, which have been making timely payment to the company in the past. Presence of escalation clause in majority of the contracts enable the company to pass increase in raw material

prices to its customers. Ability of the company to pass increased cost burden to its customers in a timely manner and maintain profitability margins is critical from credit perspective.

Industry Outlook

The construction sector in Nepal has been impacted by lower execution in the aftermath of the covid-19 pandemic with slower pace of economic growth coupled with relatively lower infrastructure spending by the government. Furthermore, contractors' cash flows have also come under pressure as a result of highly inflated construction costs leading to shrinking margins over FY22-H1FY23. Increasing trend in fuel price, which is a key input for road construction, building materials and other construction equipment, has added to the margin pressure. Furthermore, as government capital expenditure continues to remain substantially lower than budgeted amount, income prospects remain subdued over the near-term which coupled with delays in payments to contractors has led to some stress in the construction sector in H1FY23 leading to the slippages in the construction portfolio of BFIs. Near term operating environment for construction companies, including RCPL, remains challenging and will remain a key monitorable aspect.

About the Company

Buddha Himali Construction Private Limited (BHC) is an 'A' class construction company in Nepal established in 2003 and based in Kathmandu, Nepal. BHC is involved in different projects like hospital buildings, road projects and water supply projects among others. In addition to doing projects independently, BHC also enters into Joint Ventures (JVs) with other companies in order to meet the eligibility criteria for different construction projects.

Financial Performance

For the period ended/ as at mid-July	FY20 (A)	FY21 (A)	FY22 (A)
Income from operations	106	240	536
PBILDT Margin (%)	3.41	4.60	5.73
Overall Gearing (times)	-	2.36	2.82
Interest Coverage (times)	-	7.94	3.99
Current Ratio (times)	1.11	1.01	1.15
Total Debt/ GCA	-	4.37	4.56

A: Audited

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 Loan	24.24	CARE-NP B+ [Single B plus]
Short Term Bank Facilities	Fund Based Limit	975.76	CARE-NP A4 [A Four]
Total		1,000.00	

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