

## C.C.S. Nepal Private Limited

### Ratings

Facilities	Amount (Rs. in Million)	Ratings <sup>1</sup>	Rating Action
Short Term Bank Facilities	<b>1,270.00</b> <b>(Decreased from 1,350.00)</b>	<b>CARE-NP A4</b> <b>[A Four]</b>	<b>Reaffirmed</b>
<b>Total Facilities</b>	<b>1,270.00</b> <b>(One Thousand Two Hundred Seventy Million Only)</b>		

*Details of instruments/facilities in Annexure 1*

CARE Ratings Nepal Limited (CRNL) has reaffirmed the rating of 'CARE-NP A4' assigned to the short term bank facilities of C.C.S. Nepal Private Limited (CCS Nepal).

### Detailed Rationale & Key Rating Drivers

The rating assigned to the bank facilities of CCS Nepal continues to be constrained by its leveraged capital structure and elongated operating cycle. The ratings also factor in the decline in Total Operating Income (TOI) in FY22 (Audited; FY refers to twelve-month period ending mid-July) amid slower than expected execution of projects in hand. High collection period during FY22 remains a key concern as delayed debtor realization trend in the construction sector continues to spill over into FY23, impacted mainly by the lower-than-expected government capital expenditures so far, this fiscal. A sustained high collection and inventory period could add to the financial burden of the company over the near-term. The ratings also factor in the tender based nature of operations in highly competitive construction industry, exposure to volatile interest rates with high interest outlay and regulatory risk and risk of delay in project execution. The ratings also take cognizance of concentrated order book position and limited revenue visibility.

The rating, however, derives strength from support and expertise derived from a strong ultimate parent company, moderate track record of operations in Nepal, steady historical performance of the company and favorable industry outlook for the telecommunications sector in the country over the medium term.

*Going forward, the ability of the company to sustain healthy growth in business, maintaining adequate profitability and liquidity, and lower borrowing levels leading to improved capital structure will be key rating sensitivities.*

### Detailed Description of the Key Rating Drivers

#### Key Rating Weaknesses

#### Leveraged capital structure and declining income in FY22

CCS Nepal's TOI decreased by 19.71% year-on-year to Rs. 1,096 Mn in FY22. Execution of the projects in hand is being impacted by the slowdown in government capital expenditure. Furthermore, the company had Rs. 1,139 Mn accrued receivable of progress income at the end of FY22 (FY21: Rs. 1,376 Mn), which is likely to be booked over FY23-FY24. Although the company's PBILDT margins improved by 548 bps to 17.67% during FY22, it has historically remained quite volatile as expenses related to projects keep fluctuating based on the prices of construction materials and the availability of sub-contractors. The company reported net profit of Rs. 61 Mn during FY22 compared to Rs. 49 in FY21. With improvement in profitability in FY22, Gross Cash Accruals (GCA) improved to Rs. 62 Mn in FY22 compared to Rs. 43 Mn in FY21. The ability of the company to sustain scale of operations, by successfully bidding for tenders, and maintaining adequate profitability margins remains critical for its financial health.

Overall gearing ratio of CCS Nepal was high at around 3.99x at the end of FY22, although improving from 5.65x at the end of FY21 mainly on account of lower debt levels at FY22 end amid declining scale of operations. The company's total debt/GCA also stood high at 18.37x in FY22 (FY21: 29.37x). Similarly, interest coverage was moderate at 1.74x during

<sup>1</sup>Complete definitions of the ratings assigned are available at [www.careratingsnepal.com](http://www.careratingsnepal.com) and in other CRNL publications

FY21, albeit improved marginally from 1.55x in FY21. Total Outside Liabilities (TOL)/ TNW of the company stood high at 4.99x at the end of FY22 (FY21: 7.17x). The debt levels of the company are directly linked to the projects in progress and a higher debt level is usually indicative of a large project with substantial reciprocal revenue inflow for the company. However, the amount of current debt remains high, commensurate to the company's net worth, resulting in a leveraged capital structure.

#### **Concentrated order book position and limited revenue visibility**

The company has unexecuted order book of Rs. 3,259 Mn as on March 31, 2023, which is 2.97x of its TOI for FY22. The company's order book position is highly concentrated towards a single project which accounts for around 66% of the total unexecuted order book. The company's revenue visibility is mainly limited to the projects at hand, which is likely to be completed within the next twelve months or so. Revenue concentration risk, however, is partly offset by the credit strength and track record of the counterparty, which is a state-owned telecommunication operator. Hence, counterparty risk remains low. The scale of operations, after completion of the current projects, remains unpredictable and would depend on the company's ability to successfully bid for newer projects.

#### **Elongated operating cycle with increasing trend in collection and inventory period**

The operations of the company are working capital intensive in nature marked by high collection and inventory period at the end of FY22. CCS Nepal's average collection period elongated to 77 days in FY22 from 28 days in FY21. CCS Nepal's customer base primarily includes government departments/ bodies; therefore, the certification and realization of the bill generally takes the period of around 3-4 months. The funds are released only after the approval from authorities at various levels and the work certification process is completed. Average inventory cycle of the company (including accrued receivable of progress income) stood substantially high at around 538 days in FY22 (FY21: 399 days). Although counterparty risk remains low over the long-term, stretched operating cycle could adversely impact the liquidity position of the company over the near-term. The company has been relying on borrowings from the bank to meet its working capital requirements. Average utilization of working capital limits for the last 12 months ended February 2023 stood high at more than 85% against its sanctioned limits. Amid increasing working capital intensity, the company's reliance on borrowings to meet its working capital requirements is likely to increase going forward. Hence, the company's ability to timely turnaround projects under work-in-progress coupled with swifter debtor realization will be critical from credit perspective.

#### **High interest outlay and exposure to volatile interest rate**

Sustained requirement for short-term working capital borrowings pertaining to the ongoing projects has led to a high interest expense for CCS Nepal, increasing to Rs. 111 Mn during FY22 from Rs. 108 million during FY21. 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**

##### **Strength and expertise derived from strong parentage and moderate track record of operations**

CCS Nepal's ultimate parent China Communication Services Corporation Limited (China Comservice) is one of the major network builders for the telecommunication operators in China. CCS Nepal, being a wholly owned subsidiary, is closely managed and monitored by the parent as all the key management personnel are appointed and supervised by the parent.

Furthermore, CCS Nepal is in the same line of business as its parent and thus has access to the long-established expertise and heritage as well as the innovative technical capabilities and solutions of the parent entity. CCS Nepal, with support and supervision from its parent, is establishing itself as an integrated service provider to the telecommunications, media and technology industries in Nepal. CCS Nepal is operating in Nepal for more than a decade and is amongst the major vendors in the niche telecommunication infrastructure development and service business in the country. An established presence in the niche segment with proven track record at both domestic as well as at parent level bodes well for the company's prospects of successfully bidding for newer projects going forward.

### Moderate track record of operations and steady historical performance

CCS Nepal is operating in Nepal for around a decade. Currently, it is amongst the major vendors in the niche telecommunication infrastructure development and service business in the country. The company has till date completed various projects for leading telecommunication operators in the country. An established presence in the niche segment with proven track record at both domestic as well as at parent level bodes well for the company's prospects of successfully bidding for newer projects going forward.

CCS Nepal's historical financial performance has remained steady. The company had accumulated profits from business of Rs. 188 Mn by FY21. This has steadily increased to Rs. 249 Mn by the end FY22. Boosted by the incremental revenues from ongoing projects, the company is likely to sustain moderate levels of PAT during FY23 as well, hence maintaining a steady accretion of profits to reserves, which is likely to translate into a steady growth in the company's net worth.

### About the Company

C.C.S. Nepal Private Limited (CCS Nepal), incorporated on June 07, 2021 as a private limited company, is a 100% subsidiary of China Communications Services International Limited, which is a wholly owned subsidiary of China Communication Services Corporation Limited. CCS Nepal provides comprehensive network construction services including communications network consultation, planning, design, engineering, construction and supervision.

### Financial Performance

(Rs. Million)

For the Period	FY20 (A)	FY21 (A)	FY22 (A)
Income from Operations	1,606	1,366	1,096
PBILDT Margin (%)	6.30	12.19	17.67
Overall Gearing (times)	3.99	5.65	3.99
Total Outstanding Liabilities/Tangible Net worth (times)	6.93	7.17	4.99
Interest Coverage (times)	2.88	1.55	1.74
Current Ratio (times)	1.14	1.14	1.20
Total Debt/Gross Cash Accruals (times)	14.65	29.37	18.37

A: Audited

### Annexure 1: Details of the Facilities Rated

Name of the Bank Facilities	Type of the Facility	Amount (Rs. In Million)	Ratings
Short Term Bank Facilities	Fund Based Limits	1,270.00	CARE-NP A4 [A Four]
<b>Total</b>		<b>1,270.00</b>	

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### About CARE Ratings Nepal Limited:

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