

P.K. Nirman Sewa Private Limited

Ratings

Facilities	Amount (Rs. in Million)	Ratings ¹	Rating Action
Long Term Bank Facilities	197.20	CARE-NP BB- [Double B Minus]	Assigned
Short Term Bank Facilities	1,302.80	CARE-NP A4 [A Four]	Assigned
Total Facilities	1,500.00 (One Thousand Five Hundred Million Only)		

Details of instruments/facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has assigned rating of 'CARE-NP BB-' to the long term bank facilities and 'CARE-NP A4' to the short term bank facilities of P.K. Nirman Sewa Private Limited (PKNS).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of PKNS are constrained by its modest scale of operations with low capital base and concentrated portfolio. The ratings also factor in its stretched payable days leading to relatively lower margins vis-à-vis peers of comparable scale in the industry, tender based nature of operations in the highly competitive construction industry, exposure to volatile interest rates and regulatory risk and risk of delay in project execution.

The ratings, however, derive strength from experienced promoter, moderate track record of operations and improving financial profile of the company marked by increasing Total Operating Income (TOI) and moderate capital structure. The ratings also factor in 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 a timely manner, profitably scale up the operations of the company leading to sustained revenue growth while maintaining profitability margins along with improving its overall financial risk profile will be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Concentrated portfolio with low capital base

As on May 31, 2023, the unexecuted orders in hand of the company stood at Rs. 613 Mn, which is 1.28x of the income from contract of FY22, providing near term revenue visibility. The order book is primarily concentrated towards road projects which exposes company towards risk of sectoral concentration. Concentration of government orders exposes the company with risk related to allocation of fund or regulatory changes mainly in the Public Procurement Act and other related regulations. Timely completion of the projects, including PKNS's ability to regularly bill and realize projects under progress, would be critical for the business prospects of the company and also has a direct bearing on its margins.

The company's ability to substantially scale up to larger sized contracts having better operating margins is constrained by its comparatively low paid-up capital of Rs. 10 Mn as on mid-July 2022. Small scale of operations in a competitive industry limits the pricing power and benefits derived from economies of scale decrease in operational profit with corresponding decrease in overall revenue. Though, the risk is partially mitigated by the fact that the scale of operations is growing steadily.

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

Stretched payable days

PKNS has high creditors days leading to negative net operating cycle. Average creditors days of the company elongated to 138 days in FY22 from 70 days in FY21. Elongated creditor days suggest the company is funding its working capital requirements from payables and is reflective of a stretched liquidity position of the company. Total Outside Liabilities (TOL)/ TNW of the company stood relatively high at 4.51x at the end of FY22 amid high creditors coupled with low capital base of the company. Sustained stretched payable days could adversely impact its margin profile. The company's PBILDT margins are relatively lower compared to other peers of similar scale in the road construction sector.

Tender based nature of operations in highly competitive construction industry

Majority of the PKNS's projects are tender-based government contracts wherein the company has to quote a bid. With multiple players active in the industry, PKNS's business is vulnerable to under bidding at a relatively low cost in order to secure the projects, in the highly competitive construction industry. Furthermore, the business also remains dependent on sustained capital expenditure by the government towards construction projects, overall 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.

Exposure to volatile interest rate

PKNS's interest expenses 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. Thus, funding taken by the firm is exposed to volatile interest rate.

Risk of delay in project execution

Given the nature of projects awarded, PKNS 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 resulting in a delay in the realization of revenue growth. Furthermore, the company ability to execute a project in timely manner would be led by its own operational efficiency and timely stage payments received from clients.

Key Rating Strengths**Experienced promoter and moderate track record of operations**

PKNS is promoted by Mr. Prakash Bishwokarma, Chairman/ Managing Director, who has been leading the company since its inception in December 2015. Mr. Bishwokarma has experience of over a decade in the construction sector which bodes well for the overall business prospects of the company in an increasingly competitive industry. He is looking after the execution of projects undertaken by the company. Furthermore, he is supported by an experienced team across various functions. The company has moderate track record of operations of over seven years in the construction of various infrastructure projects all over Nepal.

Growing scale of operations with moderate capital structure

During FY22, PKNS' TOI grew 13.75% year-on-year to Rs. 480 Mn with execution of larger sized projects during FY22. The business generation of the company is through bidding and tendering process and profitability margins are directly

associated with the nature of contracts executed by the company. PBILDT margin of the company improved by 93 bps to 11.54% in FY22 with higher execution of high margin projects. Amid higher depreciation expenses, PAT margin of the company declined by 91 bps to 2.81% during FY22. Gross Cash Accruals (GCA) of the company increased by ~26% to Rs. 45 Mn during FY22.

Capital structure of PKNS stood moderate with overall gearing ratio (including mobilization advance, normally interest free) of 1.28x as on mid-July 2022, deteriorating from 0.56x as on mid-July 2021. Overall gearing ratio (excluding mobilization advance) stood at 0.96x as on mid-July 2022, deteriorated from 0.56x as on mid-July 2021. Gearing levels deteriorated in FY22 amid increasing term loans for procurement of construction equipment and advance mobilization received by the company. Interest coverage ratio of the company was satisfactory at 18.57x in FY22 which improved from 11.94x in FY21 majorly on account of increased PBILDT. Total debt/ GCA of the company stood moderate at 1.93x in FY22 (PY:0.85x).

Moderate counter party risk

Revenue of PKNS is generated majorly via contracts from government departments. 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.

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 FY22-9MFY23. 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 9MFY23 leading to the slippages in the construction portfolio of BFIs. Near term operating environment for construction companies, including PKNS, remains challenging and will remain a key monitorable aspect.

About the Company

P.K. Nirman Sewa Private Limited (PKNS) is a class "A" construction company of Nepal incorporated on December 03, 2015 with its registered office based in Dang, Nepal. The company is involved in construction of roads, building, bridges, river training works etc. across Nepal. In addition to doing projects independently, PKNS also enters into Joint Ventures (JVs) with other companies in order to meet the eligibility criteria for different construction projects.

Financial Performance

(Rs. Million)

For the Period	FY20 (A)	FY21 (A)	FY22 (A)
Income from Operations	255	422	480
PBILDT Margin (%)	14.24	10.61	11.54
Overall Gearing (times)	2.24	0.56	1.28
Total Outstanding Liabilities/Tangible Net worth (times)	3.69	2.88	4.51
Interest Coverage (times)	4.56	11.94	18.57
Current Ratio (times)	1.43	0.82	0.83
Total Debt/Gross Cash Accruals (times)	3.39	0.85	1.93

A: Audited

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 Loan	197.20	CARE-NP BB- [Double B Minus]
Short Term Bank Facilities	Non Fund Based Limits	1,302.80	CARE-NP A4 [A Four]
Total		1,500.00	

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About CARE Ratings Nepal Limited:

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