

## Kankai International Builders Private Limited

### Ratings

Facilities	Amount (Rs. in Million)	Ratings <sup>1</sup>	Rating Action
Long Term Bank Facilities	97.52	<b>CARE-NP BB+ [Double B Plus]</b>	<b>Reaffirmed</b>
Short Term Bank Facilities	402.48 (Increased from 42.90)	<b>CARE-NP A4+ [A Four Plus]</b>	<b>Reaffirmed</b>
Long Term/ Short Term Bank Facilities	5,000.00 (Increased from 2,859.58)	<b>CARE-NP BB+ / A4+ [Double B Plus/ A Four Plus]</b>	<b>Reaffirmed</b>
<b>Total Facilities</b>	<b>5,500.00 (Five Thousand Five Hundred Million only)</b>		

*Details of instruments/facilities in Annexure 1*

CARE Ratings Nepal Limited (CRNL) has reaffirmed the rating of 'CARE-NP BB+' assigned to the long-term bank facilities and 'CARE-NP A4+' assigned to the short-term bank facilities of Kankai International Builders Private Limited (KIB).

### Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of KIB continue to be constrained by working capital intensive nature of 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 government regulations and risk of delay in project execution. The ratings also take cognizance of the decline in total operating income (TOI) and profitability of the company in FY22 (Audited, FY refers to the twelve-month period ending mid-July), which however is expected to improve steadily over the medium term supported by healthy order book position of the company currently. The ratings continue to derive strengths from experienced promoters and established track record of operations, moderate capital structure, moderate counter party risk and escalation clause in majority of the contracts.

*Going forward, the ability of the company to successfully execute projects in time and recover contract proceeds; and ability to maintain profitability margins and manage its working capital requirements to support growth will be key rating sensitivities.*

### Detailed Description of the Key Rating Drivers

#### Key Rating Weaknesses

#### Decline in Total Operating Income and profitability in FY22

During FY22, KIB's TOI declined ~9% over FY21 to Rs. 1,633 Mn amid lower projects executed by the company during FY22 with slowdown in construction activities in the country mainly owing to lower government capital expenditures. Similarly, profitability margins of the company, which tend to fluctuate owing to the nature of the contracts executed in that particular year, declined in FY22 with decline in PBILDT margin by 166 bps to 7.24%. Consequently, PAT margin of the company also declined by 180 bps to 2.21% in FY22. Furthermore, with decline in net profitability, gross cash accruals (GCA) of the company declined by ~35% to Rs. 82 Mn in FY22. Despite moderation in financial performance of the company in FY22, the near-term business prospect of the company is supported by a strong orderbook position of the company, which is likely to result in sequential improvement in FY23.

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

**Working capital intensive nature of business**

The operations of the company are working capital intensive in nature marked by increasing trend in inventory holding period and collection period. Average inventory holding period of the company increased to 37 days in FY22 from 10 days in FY21 majorly due to piling up of construction materials as the company has to maintain inventory at various sites for smooth execution of project works. The funds are released only after the work certification process is completed and finalization of the bill is concluded. Customer base includes government departments/ bodies; therefore, the certification and realization of the bill generally takes the period of around a month. Consequently, average collection period elongated to 64 days in FY22 compared to 32 days in FY21. These factors lead to increased reliance of the company on borrowings to meet its working capital requirements.

**Tender based nature of operations in highly competitive construction industry**

Majority of the KIB's projects are tender-based government contracts wherein the company has to quote a bid. With multiple players active in the industry, KIB'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**

KIB'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.

**Risk of delay in project execution**

Given the nature of projects awarded, KIB 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 promoters and established track record of operations**

KIB is being promoted by Mr. Ram Prasad Mainali and his family members. Mr. Ram Prasad Mainali, Chairman, has been leading the company since its inception in July 1987 and has experience of more than three decades in the construction sector which bodes well for the overall business prospects of the company in an increasingly competitive industry. He looks after overall management of the company. Board of Directors is further supported by an experienced team across various functions/ departments. The company has established track record of operations of more than three decades in the construction of various infrastructure projects all over Nepal.

**Moderate capital structure and strong order book position**

Capital structure of KIB stood moderate with overall gearing ratio (including mobilization advance) of 2.17x as on mid-July 2022, slightly improved from 2.55x as on mid-July 2021 mainly due to decrease in mobilization advance at the end of FY22. Overall gearing ratio (excluding mobilization advance) improved to 0.34x as on mid-July 2022 from 0.76x as on mid-July 2021. Total debt to GCA improved to 0.69x in FY22 from 1.62x in FY21. Also, interest coverage ratio of the company stood satisfactory at 11.77x in FY22, improved from 6.38x in FY21. However, total outside liability (TOL) to total net worth remained high at 5.09x at the end of FY22, deteriorated from 3.43x at the end of FY21.

As on March 07, 2023, the unexecuted orders in hand of the company stood at Rs. 9,139 Mn, which is more than 5 times its income from contract in FY22, providing decent mid-term revenue visibility. The order book is majorly towards road projects (~64%) and others include water supply, irrigation, bridge and building projects by entering into JVs. One road project, however, accounts for ~43% of the total order book position. Order book with substantial contribution from a single project links the company's performance to the same and any delays in execution of the project can materially impact the company's envisaged revenue flow and consequently its financial health. Timely completion of the projects would be critical for the business prospects of the company and also has a direct bearing on its margins.

**Moderate counter party risk and escalation clause in majority of contracts**

Revenue of KIB is generated majorly via contracts from government departments. The order book is primarily concentrated towards road and water supply 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 covid19 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-FY23. 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 FY23 leading to the slippages in the construction portfolio of BFIs. Near term operating environment for construction companies, including KIB, remains challenging and will remain a key monitorable aspect.

**About the Company**

Kankai International Builders Private Limited (KIB) is a private limited company, incorporated in July 26, 1987 with registered office based in Jhapa, Nepal. KIB is an ISO 9001:2015 certified company, certified in December 2020. In addition to doing projects independently, KIB also enters into Joint Ventures (JVs) with other companies in order to meet the eligibility criteria for different construction projects.

**Analytical Approach**

CRNL has analysed KIB's credit profile by considering the consolidated financial statements comprising KIB and its joint venture entities related to the construction projects.

## Financial Performance

(Rs. Million)

For the Period Ended / as at Mid-July,	FY20 (A)	FY21 (A)	FY22 (A)
Income from Operations	1,561	1,857	1,683
PBILDT Margin (%)	9.87	8.90	7.24
Overall Gearing (times)	1.32	2.55	2.17
Interest Coverage (times)	6.38	11.77	5.83
Current Ratio (times)	1.38	2.25	1.84
Total Debt/ Gross Cash Accruals (times)	1.62	0.69	1.63

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	97.52	CARE-NP BB+ [Double B Plus]
Short Term Bank Facilities	Fund Based Limits	402.48	CARE-NP A4+ [A Four Plus]
Long Term/ Short Term Bank Facilities	Non-Fund Based Limits	5,000.00	CARE-NP BB+/ A4+ [Double B Plus/ A Four Plus]
<b>Total</b>		<b>5,500.00</b>	

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### About CARE Ratings Nepal Limited:

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