

## Motidan Construction Sewa Private Limited

### Ratings

Facilities	Amount (Rs. in Million)	Ratings <sup>1</sup>	Rating Action
Long Term Bank Facilities	1,691.08	CARE-NP BB+ [Double B Plus]	Reaffirmed
Short Term Bank Facilities	2,405.00 (Increased from 1,555.00)	CARE-NP A4+ [A Four Plus]	Reaffirmed
Long Term/ Short Term Bank Facilities	9,403.92 (Increased from 7,126.50)	CARE-NP BB+ / A4+ [Double B Plus/ A Four Plus]	Reaffirmed
<b>Total Facilities</b>	<b>13,500.00</b> <b>(Thirteen 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 Motidan Construction Sewa Private Limited (MCS).

### Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of MCS continue to be constrained by its leveraged capital structure and elongated operating cycle with increasing trend in collection period in FY22 (Audited; FY refers to the twelve-month period ending mid-July). The ratings also factor in its presence in highly competitive construction industry coupled with tender based nature of operations, exposure to volatile interest rates and government regulations and risk of delay in project execution. The ratings also take cognizance of decline in Total Operating Income (TOI) of the company in FY22 although rebound likely in FY23 supported by improved execution of contracts during the year. The ratings continue to derive strengths from experienced promoters and long track record of operations, moderate order book position, moderate counter party risk and escalation clause in majority of the 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 and rationalization of its debt through efficient working capital management would be the key rating sensitivities.*

### Detailed Description of the Key Rating Drivers

#### Key Rating Weaknesses

##### Leveraged capital structure

Capital structure of MCS stood leveraged with overall gearing ratio (including mobilization advance) of 3.28x and 3.03x (excluding mobilization advance) as on mid-July 2022, deteriorated from 3.14x and 2.70x, respectively as on mid-July 2021 amid increase in bank borrowings to fund its work capital requirements. Also, total outside liability (TOL) to tangible net worth and total debt to gross cash accruals stood high at 4.16x and 7.64x, respectively, as on mid-July 2022 (4.76x and 4.45x, respectively, as on mid-July 2021). Furthermore, the interest coverage ratio of the company was moderate at 2.12x in FY22 (PY: 3.65x). Limited gearing headroom could limit the financial flexibility of a company. MCS' ability to rationalize debt levels will remain critical from analytical perspective.

##### Elongated operating cycle with increasing trend in collection period

The operations of the company are working capital intensive in nature marked by high collection period in FY22. The funds are released only after the work certification process is completed and finalization of the bill is done. Customer base mainly

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

includes government departments/ bodies; therefore, the certification and realization of the bill generally takes a period of around three months. Recovery of debtors, at times, exceeds three months as has been the case over FY22-FY23. Average collection period of MCS increased to 170 days in FY22 from 93 days in FY21 mainly due to subdued collection during FY22 with slowdown in construction activities in the country mainly owing to lower government capital expenditures. Slow debtor realization has continued into FY23 resulting in sustained high short-term borrowings of the company. A sustained high collection period could add to the financial burden of the company over the near-term, which could be a challenge from credit perspective.

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

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

### **Risk of delay in project execution**

Given the nature of projects awarded, MCS 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. Although counter party risk over the medium term remains low given the projects are majorly from Government departments, which have been making timely payment to the company in the past, timely debtor realization, particularly at times of economic downturn, remain key challenge for the construction sector.

### **Key Rating Strengths**

#### **Experienced promoters and long track record of operations**

MCS has three directors in its Board of Directors led by Managing Director, Mr. Ram Bahadur Gautam, who has been leading the company since its inception in March 2009. Mr. Gautam has experience of more than a decade in the construction sector which bodes well for the overall business prospects of the company in an increasingly competitive industry. He is responsible for planning business strategies of the company. Furthermore, the board is supported by an experienced team across various functions. The company has long track record of operations of over a decade in the construction of various infrastructure projects all over Nepal.

#### **Moderate order book position**

The company has unexecuted order book of Rs. 2,536 Mn, providing near term revenue visibility. The order book position of the company is mainly towards road projects, mining, canal and water supply works. Timely completion of the projects, including MCS'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 current unexecuted orderbook, however, is relatively small vis-à-vis MCS's scale of operations. MCS' future business prospect hinges on its ability to successfully bid for newer projects.

### Fairly steady financial profile

MCS's TOI grew at compounded annual growth rate of ~45% during FY20-FY22, however declined ~13% year-on-year to Rs. 2,709 Mn 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. Despite decline in TOI, PBILDT margin of the company improved by 111 bps to 13.65% in FY22 supported by execution of high margin contracts. Consequently, PAT margin of the company improved by 9 bps to 3.37% in FY22. However, Gross cash accruals (GCA) of MCS decreased by ~12% to Rs. 221 Mn in FY22 owing to lower net profits during FY22. During FY23 MCS' operating income is expected to have increased by lower double digit growth rate amid improved executions.

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

Revenue of MCS 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. 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 MCS, remains challenging and will remain a key monitorable aspect.

### About the Company

Motidan Construction Sewa Private Limited (MCS) is a class "A" construction company of Nepal incorporated on March 03, 2009 with its registered office based in Kathmandu, Nepal. The company is involved in mining works, construction of roads, bridges, building, irrigation works etc. across Nepal. In addition to doing projects independently, MCS 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 MCS's credit profile by considering the consolidated financial statements comprising MCS and its joint venture entities related to the construction projects.

### Financial Performance

(Rs. Million)

For the Period	FY20 (A)	FY21 (A)	FY22 (A)
Income from Operations	1,281	3,123	2,709
PBILDT Margin (%)	15.73	12.54	13.65
Overall Gearing (times)	2.95	3.14	3.28

For the Period	FY20 (A)	FY21 (A)	FY22 (A)
Total Outstanding Liabilities/Tangible Net worth (times)	4.22	4.76	4.16
Interest Coverage (times)	3.15	3.65	2.12
Current Ratio (times)	1.22	1.23	1.29
Total Debt/Gross Cash Accruals (times)	5.67	4.45	7.64

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	1,691.08	CARE-NP BB+ [Double B Plus]
Short Term Bank Facilities	Fund Based Limits	2,405.00	CARE-NP A4+ [A Four Plus]
Long Term/ Short Term Bank Facilities	Non Fund Based Limits	9,403.92	CARE-NP BB+ / A4+ [Double B Plus/ A Four Plus]
<b>Total</b>		<b>13,500.00</b>	

#### Contact Us

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#### About CARE Ratings Nepal Limited:

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