

PRESS RELEASE

SWIKAR CONSTRUCTION & DEEP TUBEWELL PRIVATE LIMITED January 2023

Ratings

Instruments/ Facilities	Amount (NPR. Mn)	Ratings	Rating Action
Long Term Bank Facilities	267.35	IRN B+	Assigned
Short Term Bank Facilities	177.65	IRN A4	Assigned
Long Term/Short Term Bank Facilities	1,320.00	IRN B+ / A4	Assigned
Total	1,765.00		

Details of facilities are in Annexure 1 below

Infomerics Credit Rating Nepal Limited (Infomerics Nepal) has assigned long term rating of IRN B+ (Single B Plus) to the long term bank facilities of NPR 267.35 Mn, short term rating of IRN A4 (A Four) to the short term bank facilities of NPR 177.65 Mn and IRN B+ (Single B Plus) /A4 (A Four) to the long term/short term bank facilities of NPR 1,320 Mn.

Detailed Rationale

The ratings assigned to the bank facilities of Swikar Construction & Deep Tubewell Private Limited (SCDPL) derive strength from its experienced promoters and management team in construction fields with moderate track record of operations along with escalation clauses in the major contracts, moderate but concentrated order book position and average financial risk profile. These rating strengths, however, are constrained by SCDPL's existence in a competitive industry with a policy cap in number of contracts executed at a time. Further, the ratings also note SCDPL's susceptibility to interest rate volatility, counter-party risk, modest scale of operations and exposure to project execution risks. Going forward, the ability of the company to diversify its order book, widen the scope of work and successfully execute current projects in hand while managing revenue growth, improving profit margins and net worth base will remain a key rating sensitivities.

Detailed Description of Key Rating Drivers

Key Rating Strengths

Experienced promoters and management team with moderate track record of operations

SCDPL is led by Mr. Sahadev Khadka, Managing Director, who has been leading the company since its inception in 2014 and has more than a decade of experience in the field of construction business. Similarly, Mr. Krishna Bahadur Khadka, Director, also has relevant experience in the construction contract business. Furthermore, the board is aptly supported by an experienced team across various departments.

Moderate order book position with mid-term revenue visibility

Till December end 2022, the unexecuted orders in hand of the company stood at ~NPR 1,762 Mn (including SCDPL's share in JVs). The order book of SCDPL is considerable vis-à-vis the operating income of FY22. SCDPL's order book position remains comfortable as of December end, 2022 with an unexecuted order in hand of ~4.42 times the operating income in FY22. Furthermore, the order book reflects mid-term revenue visibility as the major projects are in their initial phase and scheduled to last for next two years.

Average financial risk profile

The average financial profile of SCDPL is marked by an improvement in the total operating income (TOI), moderately leveraged capital structure and comfortable coverage indicators. The TOI has increased to NPR 398 Mn in FY22 vis-à-vis NPR 162 Mn in FY21 and NPR 157 Mn in FY20. Furthermore, despite the fall in EBITDA margins in FY22, the absolute value has improved to NPR 25 Mn in FY22 vis-à-vis NPR 23 Mn in

FY21 and NPR 15 Mn in FY20 in line with the increment in TOI. Further, the overall gearing of SCDPL has marginally improved to 2.45x in FY22 vis-à-vis 2.69x in FY21 on account of the repayment of term loans and improvement in the tangible net-worth base of the company. The interest coverage ratio also remained comfortable at 3.59x in FY22 which however was slightly deteriorated from 3.62x in FY21. Going forward the ability of SCDPL to scale up its operation while improving its margins will remain crucial.

Escalation clauses in major contracts

Escalation clauses are included in the majority contracts of SCDPL, which protect it against any adverse changes in prices of key construction materials. This is crucial, especially considering the current global inflationary trend. Nevertheless, the coverage provided by the escalation clauses is capped, meaning that some portion of the risk associated with price volatility is still retained by the company. From a credit rating perspective, the company's ability to pass on rising price burdens to customers promptly is an important factor in assessing its overall financial strength and creditworthiness.

Key Rating Weaknesses

Project execution and concentration risk

SCDPL's business model has some inherent risk and the projects are susceptible to delays in procedural approvals, site clearances and other operational issues exposing the company to the risk of delay in project execution leading to delays in realization of revenues. Additionally, the company's high concentration of projects in a single road segment, representing ~62% of unexecuted orders, further aggravates execution risk, especially considering the company's limited track record in the road segment. Nevertheless, presence of experienced promoters with past exposure in such segment provides comfort to an extent. Furthermore, given the policy of limiting outstanding government contracts at a time, the timely execution of the order in hand remains critical.

Counter party risk

The majority of SCDPL's revenue originates from governmental projects, for which the company serves in the capacity of contractor as well as sub-contractor. The company's counterparty risk remains high as ~86% of the outstanding order in hand is attributable to private employers (for sub-contracted projects). Nevertheless, these private employers are group companies which provides comfort to an extent.

Existence in a competitive industry with policy cap in number of contracts

The company receives the majority of its work from governmental agencies which are subject to a competitive bidding process. Further, the business also remains dependent on stability in government policies and fiscal policies. Moreover, recent regulation of Government limits contractors to participate in a maximum of five contracts at a time. Thus, SCDPL's ability to obtain new projects while maintaining profit margins remains crucial. Nevertheless, the recent Government initiative of prohibiting foreign companies to participate in a contract up to NPR 3,000 Mn (previously NPR 1,000 Mn) remains positive to the domestic contractors. Further, the foreign companies must form a joint venture with a Nepalese company in order to take the contract up to NPR 10,000 Mn, this is also expected to enhance technical capacity of Nepalese contractors going forward.

Interest rate and defect liability risk

The Interest rates on deposits and borrowing remain a significant factor in the Nepalese economy. In line with NRB's directives, the BFIs typically charge an interest rate on loans by adding a premium to the base rates which is revised on a quarterly basis. The interest rates charged by BFI's have been historically volatile over the past 2-3 years and thus borrowing from banks and financial institutions exposes SCDPL to the risk of

¹ Bank and Financial Institutions

interest rate volatility. Further, SCDPL is susceptible to financial losses arising out of defects identified by the client during the defect liability period as per the terms of the construction contracts.

Analytical Approach: Standalone

Applicable Criteria:

[Corporate Credit Rating Methodology](#)

About the Company:

Swikar Construction & Deep Tubewell Private Limited (SCDPL) is a Class “D” construction company of Nepal which was incorporated on December 7, 2014. The registered office of the company is located at Butwal -15, Rupandehi and the company is promoted by Mr. Sahadev Khadka, Chairman and Mr. Krishna Bahadur Khadka, Director. In addition to doing projects independently, SCDPL also works as a sub-contractor and in Joint Ventures (JVs) with other companies in order to meet the eligibility criteria for different construction projects.

Financial Indicators (Standalone)

For the year ended* As on	FY20	FY21	FY22
	Audited	Audited	Audited
Total Operating Income (in NPR Mn.)	157	162	398
EBITDA Margin (%)	9.82	14.27	6.37
Interest Coverage Ratio (x)	3.64	3.62	3.59
Current Ratio (x)	1.44	3.87	1.56
Overall Gearing Ratio (x)	1.33	2.69	2.45

* Classification as per Infomerics Nepal standards

Annexure:1 Detail of Facilities:

Name of Instruments/ Facilities	Type of Facilities	Amount (NPR Mn.)	Ratings
Fund Based Bank Facilities-Term Loan	Long Term	27.31	IRN B+
Fund Based Bank Facilities-Term Loan (Proposed)	Long Term	240.04	IRN B+
Fund Based Bank Facilities-Working Capital (WCL)	Short Term	20.00	IRN A4
Fund Based Bank Facilities-WCL (Proposed)	Short Term	157.65	IRN A4
Non Fund based Bank Facilities- LC/BG ²	Long Term/ Short Term	920.00	IRN B+/A4
Non Fund based Bank Facilities- BG/LC (Proposed)	Long Term/ Short Term	400.00	IRN B+/A4
Total Facilities		1,765.00	

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About Infomerics Credit Rating Nepal Limited:

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