

PRESS RELEASE

MAHABIR ENGINEERING AND CONSTRUCTION PRIVATE LIMITED

November 2023

Ratings

Instruments/ Facilities	Amount (NPR. Mn)	Ratings	Rating Action
Long Term Bank Facilities	195.00	IRN B-	Assigned
Short Term Bank Facilities	201.95	IRN A4	Assigned
Long Term/Short Term Bank Facilities	1,033.05	IRN B-/ A4	Assigned
Total	1,430.00		

Details of facilities are in Annexure 1 below

Infomerics Credit Rating Nepal Limited (Infomerics Nepal) has assigned the long term rating of IRN B- (Single B Minus) to the long term bank facilities of NPR 195.00 Mn, the short term rating of IRN A4 (A Four) to the short term bank facilities of NPR 201.95 Mn and IRN B-/A4 (Single B Minus/A Four) to the long term/short term bank facilities of NPR 1,033.05 Mn.

Detailed Rationale

The ratings assigned to the bank facilities of Mahabir Engineering and Construction Private Limited (MEC) derives strength from its experienced promoter and management team in construction fields with long track record of operations along with moderate counter-party risk and high order book position with mid-term revenue visibility. These rating strengths, however, are constrained by MEC's below-average financial profile and existence in a competitive industry with a policy cap in number of contracts executed at a time. Further, the ratings also note MEC's exposure to project execution risks, interest rate volatility risk and defect liability risks. Going forward, the ability of the company to successfully and efficiently execute current projects in hand while improving its overall financial profile will remain the key rating sensitivities.

Detailed Description of Key Rating Drivers

Key Rating Strengths

Experienced promoter with long track record of operations

MEC is led by Mr. Anil Gupta, Managing Director, who has been involved with the company since its inception and has around two decades of experience in the construction sector. Additionally, the board is aptly supported by an experienced management team across various departments.

Moderate counter party risk with escalation clause in majority of the contracts

MEC's primarily operates as contractor for governmental projects related to buildings, roads, bridges and other infrastructure development projects. The counter party risk remains moderate given that the projects are from government departments and agencies, which have been making payments to the company in the past. Furthermore, price adjustment clauses included in the majority of the contacts protects the company against adverse changes in the price of construction materials. This is crucial, especially considering the current global inflationary trend. Nevertheless, the coverage provided by the escalation clauses is capped, thus the company still retains a portion of the raw material price volatility risk. From a rating point of view, the company's ability to pass on rising price burdens to customers (employers) promptly while maintaining profit margin remains critical.

High order book position with mid-term revenue visibility

As of mid-September 2023, the company possesses confirmed orders in hand valued ~NPR 1,223 Mn. MEC's

order book position remains high at 7.52 times the total operating income in FY23. Furthermore, the order book reflects mid-term revenue visibility as all ongoing projects are set to complete within the next three years.

Key Rating Weaknesses

Below Average financial profile

The below average financial profile of MEC is marked by its leveraged capital structure along with declining revenue and interest coverage ratios. MEC has experienced a continuous decline in its Total Operating Income (TOI) over the past 3 years. The TOI of MEC declined to NPR 178 Mn in FY23 from NPR 310 Mn in FY22 and NPR 431 Mn in FY21. The decline in MEC's TOI is primarily due to inability of the company to execute the projects in hand despite its high order book position. Despite the sustained decline in TOI, MEC has been able to improve its EBITDA Margins to ~22% in FY23 from ~19% in FY22 and ~16% in FY21. However, in absolute terms, the EBITDA of the company has declined to NPR 40 Mn in FY23 vis-à-vis NPR 57 Mn in FY22 and NPR 67 Mn in FY21. The interest coverage of MEC has declined from 1.70x in FY22 to 0.91x in FY23 due to increased cost of borrowings and high reliance on external financing as reflected by the overall gearing of 5.26x in FY23 vis-à-vis 3.91x in FY22 and 3.53x in FY21. Going forward, the ability of MEC to timely execute the current order in hands while improving its overall financial profile remains crucial.

Project execution risk

MEC's business model carries inherent risks, including potential delays in project execution due to procedural approvals, site clearance and operational issues exposing the company to the risk of delay in project execution leading to delays in realization of revenues. This is underscored by the declining TOI of the company over the past 3 years despite an order book position of ~NPR 1,223 Mn as of mid-September, 2023 as several projects have faced execution challenges due to various technical reasons and geographical constraints. Going forward, the ability of MEC to expedite its order in hand while securing necessary time extensions for its problematic projects remains crucial.

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, the recent regulation of Government limits contractors to participate in a maximum of five contracts at a time. Thus, MEC'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 5,000 Mn (previously NPR 3,000 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.

Defect Liability and Interest Rate Risk

MEC 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. The defect liability period of MEC's outstanding contract ranges up to one year. The Interest rates on deposits and borrowing remains a significant factor in the Nepalese economy. In line with NRB's directives, the BFIs typically charge interest rate on loans by adding a premium to the base rate which are revised on a quarterly basis. The interest rates charged by BFIs have been historically volatile over the past 2-3 years and thus borrowing from banks and financial institutions exposes MEC to risk of interest rate volatility.

¹ 12th amendment to public procurement regulation as published in Nepal gazette on July 04, 2022

Analytical Approach: Standalone

Applicable Criteria:

[Corporate Credit Rating Methodology](#)

About the Company:

Mahabir Engineering and Construction Pvt. Ltd. (MEC) was established as a privately held corporation on November 6, 2000 with its registered office in Kathmandu, Nepal. The company is led by managing director, Mr. Anil Gupta who has around two decades of experience in the field of construction. Since the operation, company has been able to establish as a construction company specializing in bridges, roads and civil works of government projects. The company is solely owned by Mr. Anil Gupta.

Financial Indicators (Standalone)

For the year ended* As on	FY21	FY22	FY23
	Audited	Audited	Unaudited
Total Operating Income (in NPR Mn.)	431	310	178
EBITDA Margin (%)	15.56	18.50	22.49
Interest Coverage Ratio (x)	1.83	1.70	0.91
Current Ratio (x)	1.03	1.14	1.39
Overall Gearing Ratio (x)	3.53	3.91	5.26

Earnings before Interest Tax Depreciation Amortization (EBITDA)

* Classification as per Infomerics Nepal standards

Annexure:1 Detail of Facilities:

Name of Instruments/ Facilities	Type of Facilities	Amount (NPR Mn.)	Ratings
Long Term Bank Facilities- Fund based	Long Term	195.00	IRN B-
Short Term Bank Facilities- Fund based	Short Term	201.95	IRN A4
Long Term/ Short Term- Non Fund based	Long Term/ Short Term	970.60	IRN B-/A4
Long Term/ Short Term- Non Fund based (Proposed)	Long Term/ Short Term	62.45	IRN B-/A4
Total Facilities		1,430.00	

Analyst Contacts

Mr. Dipesh Pote Shrestha

Tel No.+977-1-4483304/4485906

dipesh.shrestha@infomericsnepal.com

Mr. Anil Adhikari

Tel No.+977-1-4483304/4485906

anil.adhikari@infomericsnepal.com

Relationship Contact

Mr. Rabin Pudasaini

Tel No.+977-1-4483304/4485906

rabin.pudasaini@infomericsnepal.com

About Infomerics Credit Rating Nepal Limited:

Infomerics Credit Rating Nepal Ltd. is Nepal's third Credit Rating Agency licensed by the Securities Board of Nepal (SEBON) on March, 2022. Infomerics Nepal is a subsidiary of Infomerics Valuation and Rating Private Limited (Infomerics India) which is a SEBI registered and RBI accredited Credit Rating Agency licensed in 2015. Infomerics Nepal aims to provide investors with objective analysis and evaluation of credit worthiness of Banks, NBFCs, Large Corporates and Small and Medium Scale Units (SMUS) via its rating and grading services. Thus, it is playing a key role in serving the financial markets by reducing the information asymmetry among varied lenders and investors and facilitating borrowers/issuers to various fundraising opportunities/avenues. Infomerics observes and maintains ethical standards in its activities. For more information, visit <https://infomericsnepal.com/>

Infomerics Credit Rating Nepal Limited

Tanka Prasad Marga, Baneshwor Height, Kathmandu

Phone: +977-1-4483304/4485906

Email: info@infomericsnepal.com

Web: www.infomericsnepal.com

Disclaimer: Ratings assigned by Infomerics Nepal are an opinion on the credit risk of the issue / issuer and not a recommendation to buy, hold or sell securities. Infomerics Nepal reserves the right to change, suspend or withdraw the credit ratings at any point in time. Ratings assigned by Infomerics Nepal are opinions on financial statements based on information provided by the management and information obtained from sources believed by it to be accurate and reliable. The credit quality ratings are not recommendations to sanction, renew, disburse or recall the concerned bank facilities or to buy, sell or hold any security. We, however, do not guarantee the accuracy, adequacy or completeness of any information, which we accepted and presumed to be free from misstatement, whether due to error or fraud. We are not responsible for any errors or omissions or for the results obtained from the use of such information. Most entities whose bank facilities/instruments are rated by us have paid a credit rating fee, based on the amount and type of bank facilities/instruments. In case of partnership/proprietary concerns/Association of Persons (AOPs), the rating assigned by Infomerics Nepal is based on the capital deployed by the partners/proprietor/ AOPs and the financial strength of the firm at present. The rating may undergo change in case of withdrawal of capital or the unsecured loans brought in by the partners/proprietor/ AOPs in addition to the financial performance and other relevant factors

Infomerics Ratings
Nepal