Rabina Construction Private Limited: Ratings reaffirmed

September 11, 2023

Summary of rating action:

Instrument (Amounts in NPR Million)	Last rated limits	Current rated limits	Rating action
Fund based; long term loan limits	160.6	264.8	[ICRANP] LB-; reaffirmed
Fund based; short term loan limits	190.0	201.4	[ICRANP] A4; reaffirmed
Non-fund based; short term loan limits	2,213.8	2,196.3	
Total Loan Limits	**2,564.4**	**2,662.5**	

Rating action

ICRA Nepal has reaffirmed the long-term rating of **[ICRANP] LB-** (pronounced as ICRA NP L B minus) to the long-term loan limits of Rabina Construction Private Limited (RCPL or the company), and a short-term rating of **[ICRANP] A4** (pronounced ICRA NP A four) to the company's short-term loan limits (including non-fund-based limits).

Rationale

The ratings continues to remain constrained by RCPL's modest financial profile with increased total outsider liabilities to tangible net worth (TOL/TNW) of 2.4 times in FY2022 (1.8 times in FY2021). While the total debt to OPBDITA remained largely steady at 4.8 times in FY2022, incremental pressures are likely amid the sharp drop in standalone revenues in FY2023 (~40%). Thus, the effect of negative operating leverage, along with the term debt added in FY2022 and the recent conversion of a part of working capital loans to permanent working capital loans (as required by regulations), are likely to create a major pressure on the company's borderline debt servicing indicators (DSCR of 1.2 times in FY2022). Mounting liquidity pressures on the company is also evident from the instances of overutilization of drawing power as seen in recent years (230% as of mid-July 2022). Amid the continuation of high interest rate outlook and the stretched working capital cycle, RCPL is likely to face major pressures in servicing the near term bank obligations. Rating concerns also arises due to high concentration on the building segment projects and large number of projects running behind schedule.

Nonetheless, the ratings continue to take comfort from RCPL's experienced promoter profile in the Nepalese construction industry, with track record of more than three decades. The company's comfortable order book position also offers near term revenue visibility, provided RCPL is able to scale up its operations, as envisaged. The ratings also factor in the positive business outlook for contractors, given the Government of Nepal's (GoN) impetus to the infrastructural development of the country, amid the large infrastructure deficit. Going forward, improvement in the company's pace of project execution leading to adequate revenue/margins and thus the improvement in its financial and liquidity profile, will remain the key rating sensitivity.

Key rating drivers

Credit strengths

Established traction in the industry and low counterparty credit risks – RCPL has been operating in the Nepalese construction industry since 1987 as a 'Class A' contractor as per the classification norms of the industry. Additionally, most of the current projects being handled by RCPL relates to the public sector, wherein majority employers are government entities, thus leading to low counterparty payment default risk, despite the consistently long debtor recovery period.

Comfortable order book position – The company's pending order book position remains comfortable at ~NPR 1.6 billion as of mid-July 2023 (i.e. ~3.5 times of FY2022's revenues). RCPL also has sufficient headroom in its bidding capacity (NPR 2.4 billion as of mid-July 2023), which could support its medium-term growth potential.

Credit challenges

Modest financial profile – RCPL has been reporting gradual increase in debt levels over the years, with major addition during FY2022, mainly for land purchase. This has resulted in spiked gearing ratio and TOL/TNW to 1.8 times and 2.4 times respectively as of mid-July 2022 (vs. 1.1 times and 1.8 times respectively as of mid-July 2021). Despite steady improvement in margins over the years, higher debt additions vis-à-vis the growth in operating profit has led to declining debt service indicators over the years, which remained borderline during FY2022 with DSCR of 1.2 times (1.6 times in FY2021). RCPL has reported a major revenue drop (standalone) during FY2023 (~40%), which is likely to pressurise these indicators amid the recent addition to repayment obligations through permanent working capital loans.

Stretched liquidity profile – The company's dependence on bank borrowing to support its working capital remains has also been increasing over the years leading to overutilisation of drawing power in recent years (230% as of mid-July 2022), as opposed to cushion available in earlier years. Amid the continuation of high interest rate outlook and the mounting debt burden, liquidity pressures are expected to persist over the near to medium term. The company's working capital intensity (net working capital to operating income ratio) also continues to remain high at ~30% for FY2022, despite recent improvement.

High concentration on single segment and project execution risks – All pending projects of RCPL are from the building construction segment leading to high sectoral concentration risks. Any major increase in prices of construction materials could create pressure on its margins. Additionally, ~56% of the pending order book (by value) as of mid-July 2023, were running behind schedule, leading to execution risks. These concerns are accentuated by the limited progress in the pending contracts during FY2023, leading to the revenue drop. Any further significant delays in the completion of such projects could subject the company to reputational risks, decline in fresh bidding capacity, revenue volatility etc. The company also heavily relies on the government's capital expenditure, which has witnessed recent slowdowns, thus remaining a rating concern.

Regulatory risks and stiff competition – The company is also exposed to regulatory risk arising from frequent changes in Public Procurement Act and associated regulations. The construction sector in Nepal is very competitive, given the presence of a large number of players. Hence, the resultant uncertainty about future revenue inflows amid the bidding requirements for public projects (major part of RCPL's portfolio) also remains the rating concern.

Link to the last rating rationale:
Rationale_Rabina Construction_Fresh BLR_July 2022

Analytical approach: For arriving at the ratings, ICRA Nepal has applied its rating methodologies as indicated below.

Links to applicable criteria:
Corporate Credit Rating Methodology
Rating Methodology for Construction Entities

About the company

Incorporated in 1987, Rabina Construction Private Limited is a closely held company wherein the entire paid-up capital is held by two individuals with largest stake of 75% being held by its managing director Mr. Ram Gopal Shrestha. The company is a "Class-A" contractor as per GoN's classification norms and is primarily focused on construction of buildings and deals mostly in public sector projects.

Key Financial Indicators

	Audited				
	FY2018	FY2019	FY2020	FY2021	FY2022
Operating Income-OI (Sales; NPR million)	261	338	321	296	467
OPBDITA/OI (%)	8%	11%	13%	14%	15%
Total Debt/ Tangible Net Worth (TNW; times)	0.4	0.5	0.5	1.1	1.8

	Audited				
	FY2018	FY2019	FY2020	FY2021	FY2022
Total Outside Liabilities/TNW (times)	0.7	1.0	1.0	1.8	2.4
Total Debt/OPBDITA (times)	2.5	1.8	1.9	4.7	4.8
OPBDITA/Interest (Interest coverage; times)	4.7	4.7	3.4	3.3	2.2
DSCR (times)	4.1	3.2	2.1	1.6	1.2
Net Working Capital/OI (%)	47%	39%	40%	46%	30%

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About ICRA Nepal Limited:

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