Chilime Engineering and Services Company Limited: [ICRANP-IR] BBB assigned

September 19, 2023

Summary of rating action

Instrument	Rated Amount (NPR million)	Rating Action
Issuer Rating	NA	[ICRANP-IR] BBB; assigned

Rating action

ICRA Nepal has assigned an issuer rating of [ICRANP-IR] BBB (pronounced ICRANP issuer rating triple B) to Chilime Engineering and Services Company Limited (ChesCo or the company). Issuers with this rating are considered to have moderate degree of safety regarding timely servicing of financial obligations. The sign of + (plus) or – (minus) appended to the rating symbol indicates their relative position within the rating categories concerned. The rating is only an opinion on the general creditworthiness of the rated entity and not specific to any debt instrument.

Rationale

The assigned rating derives comfort from the company's strong ownership profile with 100% holding of Chilime Jalavidhyut Company Limited (CJCL; a 51% subsidiary of Nepal Electricity Authority (NEA)). Apart from the indirect equity ownership in ChesCo, NEA also has its senior staff (representing CJCL) in the board of directors of ChesCo, which further enhances its linkage with NEA. The rating also factors in the company's healthy financial profile with steady revenue growth (CAGR ~12% in the last four fiscal years ending mid-July 2023) and healthy operating margins (rangebound 16-24% in the same period) albeit, on a low base. Further, the ongoing projects of the associated group companies along with work-in-hand of ~3 times its FY2023 operating revenue, provide medium-term revenue visibility for the company. The rating also positively factors in ChesCo's comfortable liquidity position with no external debt and adequate on-balance sheet cash which is likely to improve further after proposed equity raising plans (assuming full subscription of IPO and infusion of promoter equity). ICRA Nepal also notes the increasing public and private sector investments in the infrastructure projects which augur well for the demand of engineering and technical services.

Nonetheless, the rating remains constrained by ChesCo's limited track record (operating since 2016) and small scale of operations. Although revenue from services provided to group companies supports ChesCo's revenue profile, it also exposes the company to revenue concentration risk. Moreover, the company remains human-resource intensive which translates into high operating leverage. As such, the ability of the company to maintain adequate liquidity on an ongoing basis will remains essential. To that extent, the company's incremental capex and dividend plans will remain key monitorable.

Going forward, the company's ability to enhance its scale of operations and improve the operating leverage, diversify its clientele, and maintain healthy liquidity position will remain among the key rating sensitivities.

Key rating drivers

Credit strengths

Strong ownership profile and linkage with NEA – ChesCo is a wholly-owned subsidiary of Chilime Jalavidhyut Company Limited (CJCL), which in turn is a 51% subsidiary of state-owned Nepal Electricity Authority. CJCL owns and operates the 22.1-MW Chilime Hydropower Project and multiple hydropower projects are under different stages of development by its subsidiaries. The board of directors in ChesCo comprises of senior staff from NEA (representing CJCL) which remains a positive for the governance aspect of ChesCo. Its strong ownership and linkages with NEA have been factored in the assigned rating.

Healthy financial indicators and revenue visibility – ChesCo reported steady growth in revenue with CAGR of ~12% in the last four fiscal years ending mid-July 2023, along with healthy operating margins; albeit on a low base. Financial indicators also remain supported by low debt and comfortable liquidity so far. The near-term revenue visibility also remains strong with adequate work-in-hand (3.2 times the operating revenue of FY2023). Revenue prospects are further bolstered by sizeable number of projects under sister companies, at different stages of development.

Credit challenges

Small scale and revenue concentration risk – The company is in the early stages of operations and has a small scale so far. Further, the company derives a significant portion of its revenue by offering services to the hydropower projects under group entities, which raises concentration risk. The company's ability to scale up its operations and diversify its client base will remain essential for the longer-term financial sustainability, which remains to be seen.

High proposed capex could lower liquidity cushion – The company near term capex plans include construction of corporate office by utilising the current on-balance sheet liquidity and fresh equity proceeds. This could lower the liquidity cushion available with the company to some extent. As the company's business remains human resource intensive and has a high operating leverage, the ability to maintain adequate liquidity cushion will remain essential for meeting the operational requirement. Material depletion in liquidity cushion could weaken the company's ability to withstand liquidity shocks arising from seasonality in revenue and/or delayed recovery from debtors.

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

Links to applicable criteria:
Issuer Rating Methodology
Corporate Credit Rating Methodology

About the company

Chilime Engineering and Services Company Limited (ChesCo) was incorporated in 2016 with the objective of giving complete engineering and technical solutions for hydropower/infrastructure project development in Nepal. The company provides consultancy services across different stages of project life cycle, from project identification, development, commissioning and including operations and maintenance services. The company is a 100% subsidiary of Chilime Jalavidhyut Company Limited (CJCL) at present. The registered office of the company is at Dhumbarahi-04, Kathmandu.

Annexure-1: Instrument details

Particulars	Audited			Provisional
(Amount in NPR million)	FY2020	FY2021	FY2022	FY2023
Operating income-OI (sales in NPR million)	112	119	121	155
OPBDITA/OI (%)	17.4%	15.6%	24.0%	21.7%
Total debt/Tangible net worth (TNW; times)	0.0	0.0	0.0	0.0
Total outside liabilities/TNW (times)	0.2	0.2	0.1	0.1
Total debt/OPBDITA (times)	0.0	0.0	0.0	0.0
Interest coverage (times)	-	-	-	-
DSCR (times)	-	-	-	-
NWC/OI (%)	22%	17%	27%	6%
Current ratio	5.3	5.3	8.4	6.2

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About ICRA Nepal Limited:

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