Fewa Construction Private Limited: [ICRANP] LB+/A4 assigned

March 18, 2024

Summary of rating action

Instrument (Amounts in NPR Million) *	Rated Amount	Rating Action
Fund based; long term limits	478	[ICRANP] LB+; assigned
Fund based; Short-term loan limits	277	[ICRANP] A4; assigned
Non-fund based; Short-term loan limits	1,498	
Total Loan Limits	**2,253**	

** Instrument details are provided in Annexure-1.*

Rating action

ICRA Nepal has assigned a long-term rating of [ICRANP] LB+ (pronounced ICRA NP L B plus) to the long-term loan limits of Fewa Construction Private Limited (FCPL or the company) and a short-term rating of [ICRANP] A4 (pronounced ICRA NP A Four) to its short-term loan limits.

Rationale

The ratings are mainly constrained by FCPL's weak financial profile characterised by a high gearing (total debt/tangible net worth; TD/TNW) of 4.0 times and total outsider liabilities to tangible net worth (TOL/TNW) of ~17 times as of mid-July 2023. These concerns are further accentuated by the steady decline in the company's operating profit margins (OPM) in recent years to 3.5% in FY2023 (11.1% in FY2019), despite largely healthy revenue growth in the interim (notwithstanding the revenue drop in FY2023). Thin OPM, steady increment in debt levels, with further debt-funded capex plans, are likely to create a major pressure on the company's sub-par debt servicing indicators (ICR of 0.8 times for FY2023). FCPL's liquidity also remains stretched with overutilisation of drawing power, partly on account of sustained high dividend payout in recent years, despite the margin pressures and rising debt levels. Further, the ratings are constrained by the company's limited sector diversification, primarily civil works of hydropower projects, along with intense competition in the sector.

Nonetheless, the ratings factor in FCPL's established track record in the Nepalese construction sector (mainly in case of hydropower projects execution) and its experienced promoter. The ratings also favourably consider the company's comfortable pending order book position as of mid-January 2024 (6.5 times of its standalone operating income in FY2023), which provides medium-term revenue visibility. Going forward, the company's ability to scale-up its operations in line with capex plans and improve the margins and capitalisation profile will remain a key rating sensitivity.

Key ratings drivers

Credit strengths

Long track record of operations and comfortable order book position – The company has been in operation since 1996 in the Nepalese construction sector, earlier as a proprietorship firm. The promoter, over the years, has garnered significant experience in the domestic construction industry, mainly in execution of multiple hydropower projects (ranging from 1 MW to 44 MW). The company has also been able to secure sizeable new hydropower contracts in recent times, resulting in a comfortable pending order book position vis-à-vis its operating revenue as of mid-January 2024 (~6.5 times of FY2023's revenue), providing medium-term revenue visibility.

Credit challenges

Weak financial profile – FCPL's financial profile remains weak with steady increase in debt levels and high dividend payout in recent years (largely offsetting the impact of equity injection in FY2022), leading to a gearing of ~4.0 times (regulatory cap of 4 times) and TOL/TNW of 16.7 times as of mid-July 2023. Though FCPL reported healthy revenue growth from FY2019 to FY2022 (CAGR of 18%), the company reported steady drop in OPM levels to 5.4% for FY2022 from 11.1% for FY2019, which raises concerns regarding the profitability aspects of the recently added/executed large contracts. Amid the major revenue decline of ~47% during FY2023 (mainly on account of completion of a major contract while other projects in pipeline have reported slow progress), the OPM further dropped to 3.5%. This has created a sharp pressure on the debt coverage/service metrics as reflected in total debt to OPBITDA of 14.6 times and interest coverage ratio of 0.8 times in FY2023 (4.4 times and 2.6 times, respectively, in FY2022). While the debt servicing was aided by receipt of insurance claims leading to DSCR of 2.8 times for the year, the company's ability to report adequate revenue/margins will remain critical for its debt servicing capabilities.

Stretched liquidity – The company has reported sizeable funding mismatches in capex addition during recent years, which has led to high dependence on bank borrowings to support its working capital requirements, leading to largely sustained overutilisation of drawing power (~105% as of mid-July 2023). FCPL's high-value capex plans (for recently added hydropower projects) would also impede its ability to absorb any liquidity shocks. Further, the company still carries sizeable advances from its past employer, relating to support received after the flood significantly damaged its then ongoing project. While the recovery under the contractor's all-risk insurance was nominal at ~38% of claims, the same has been booked as non-operating revenues by FCPL during FY2022 and FY2023. Any withdrawal of support by the employer is likely to create a major strain on the company's liquidity and financial profiles.

Intense competition and sectoral concentration risks – The construction sector in Nepal is highly competitive, given the presence of a large number of players. The company primarily focuses on the civil works of hydropower projects, exposing it to sectoral concentration risks. Further, the company's pending order book remains concentrated, with total 10 contracts in hand and ~79% pending work (by value) from two hydropower projects (same promoter group) as of mid-January 2024. Hydropower projects generally tend to report slow physical progress and high reliance on debt financing. Hence, any major slowdown in top projects and liquidity scenarios in the banking sector would impact the company's revenue trajectory.

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

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

About the company

Established as a private firm in November 1996, the firm's business was taken over by Fewa Construction Private Limited (FCPL) in July 2023. FCPL is a class-A contractor as per the classification norms of the Government of Nepal. The company primarily deals in the civil construction of hydropower projects across different regions of Nepal. FCPL is a closely held company wherein the entire equity stake is held by Mr. Bishnu Raj Koirala (100%).

Key Financial Indicators (Standalone)

Amount in NPR million	Audited				
	FY2019	FY2020	FY2021	FY2022	FY2023
Operating Income-OI (Revenues in NPR million)	519	1,055	1,583	2,245	1,190
OPBDITA/OI (%)	11.1%	10.6%	9.9%	5.4%	3.5%
Total Debt/ Tangible Net Worth (TNW; times)	1.6	1.1	2.3	2.5	4.0
Total Outside Liabilities/TNW (times)	3.9	11.3	19.3	12.9	16.7
Total Debt/OPBDITA (times)	2.6	1.1	1.8	4.4	14.6
OPBDITA/Interest (Interest coverage - ICR; times)	4.3	6.8	8.9	2.6	0.8
DSCR (times)	3.7	3.3	3.4	3.4*	2.8*
Current Ratio	0.9	0.8	0.9	0.8	0.9
Net Working Capital/OI (%)	19.8%	-13.7%	-4.9%	-3.0%	0.1%

**DSCR is higher than ICR for these years on account of non-operating income (receipt of insurance claims).*

Annexure-1: Instrument details

Instrument (Amount in NPR Million)	Rated Amount	Rating Action
Long-term loan Limits (A)	**478**	[ICRANP] LB+; assigned
Term loans	469	
Hire purchase loan	9	
Short-term loan limits (B)	**1,775**	[ICRANP] A4; assigned
Fund-based; (Cash credit, Demand loan, Trust receipt)	277	
Non-fund based; (LC, BG, APG, PBG)	1,498	
Total Loan Limits (A+B)	**2,253**	

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About ICRA Nepal Limited

ICRA Nepal Limited, the first credit rating agency of Nepal, is a subsidiary of ICRA Limited (ICRA) of India. It was licensed by the Securities Board of Nepal (SEBON) on October 3, 2012. ICRA Nepal is supported by ICRA Limited through a technical support services agreement, which envisages ICRA helping ICRA Nepal in areas such as rating process and methodologies, analytical software, research, training, and technical and analytical skill augmentation.

Our parent company, ICRA Limited, was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment information and credit rating agency. Today, ICRA and its subsidiaries together form the ICRA Group of Companies.

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