Prithivi Engineers & Builders Private Limited: Ratings reaffirmed

June 10, 2024

Summary of rating action

Instrument	Last Rated Amount (NPR million)	Current Rated Amount (NPR million)	Rating action
Fund based; long-term limits	39.80	39.80	[ICRANP] LBB; reaffirmed
Fund based; short-term limits	10.00	10.00	[ICRANP] A4; reaffirmed
Non-fund based, short-term limits	1,325.32	1,325.32	[ICRANP] A4; reaffirmed
Total	**1,375.12**	**1,375.12**	

* Limit details are provided in Annexure-1

Rating action

ICRA Nepal has reaffirmed the long-term rating of [ICRANP] LBB (pronounced ICRA NP L double B) to the long-term limits of Prithivi Engineers & Builders Private Limited (PEBPL or the company). ICRA Nepal has also reaffirmed the short-term rating of [ICRANP] A4 (pronounced ICRA NP A four) to the short-term limits of the company.

Rationale

The ratings reaffirmation continues to derive comfort from the company's adequate financial indicators (albeit on a small scale), characterised by its stable operating margins and low gearing (partly supported by suppliers' credit and, therefore, low reliance on bank financing) resulting in comfortable debt coverage indicators. The ratings also factor in PEBPL's diversified portfolio of construction projects (encompassing road, building and irrigation sector), despite its small scale. The ratings also favourably factor in the adequate order book, with the value of pending contracts to be executed equivalent to ~1.3 times of the standalone FY2023 operating income (which was materially higher than FY2022 level due to sizeable execution), providing near-term revenue visibility. The ratings also consider the company's good project execution ability as seen in FY2023. The ratings also take comfort from the positive business outlook for contractors, given the Government of Nepal's (GoN's) impetus towards infrastructural development, amid the large infrastructure deficit in Nepal. The ratings also consider the low counterparty default risk, as most of the projects-in-hand are related to the bodies and agencies of the GoN.

The ratings are, however, constrained by PEBPL's relatively small scale of operations compared with its Class-A contractor peers, which renders the company's financial metrices vulnerable to fluctuations arising from factors such as dividend outflow, capital expenditures, change in debt levels, etc. Ratings concern also arise from geographical concentration risk, given the company's projects mostly located in Madhesh Pradesh (Province 2). Limited liquidity headroom given negative working capital drawing power, high dependence upon creditor support and mobilization advances remains a concern to incremental liquidity profile, despite being partly cushioned by on-balance sheet liquidity vis-à-vis the current scale of operations. The ratings also factor in PEBPL's exposure to regulatory risks, as the company primarily deals in public projects. Given the company's high reliance on the Government's capital expenditure, any slowdown in Government spending could affect the growth outlook and liquidity profile for the company.

Going forward, the company's ability to diversify and scale-up its operations while protecting its operating margins will remain a key rating sensitivity. PEBPL's ability to manage its liquidity in the event of limited creditor support will also remain a key rating monitorable.

Key rating drivers

Credit strengths

Adequate and diversified order book position – PEBPL's order book remains adequate as of mid-May 2024, with pending value of the contracts to be executed equivalent to 1.3 times (despite sizeable y-o-y growth) of the company's standalone FY2023 operating income, providing a near-term revenue assurance. Further, the company's pending order book is well diversified across segments like roads, buildings, water-supply projects, etc.

Low bank debt on account of adequate creditor support – PEBPL has maintained a low-debt level in the recent years. The timely recovery of receivables coupled with adequate mobilisation advances from customers supports the company's operational liquidity. PEBPL's financial profile remains good with a gearing and total debt/OPBDITA[1] of 0.5 times and 0.6 times respectively as of mid-July 2023. Low bank debt levels translated into healthy interest coverage and DSCR[2] at ~14 times and ~5 times, respectively in FY2023.

Low counterparty risk – The projects being handled by PEBPL are mostly related to public sector, where the employer is either the GoN, its ministries, or related agencies. As of mid-May 2024, most of the pending order book comprised government contracts, which signifies low counterparty credit risk. Although the payment from the government agencies witnesses occasional delays, resulting in liquidity pressure for the contractors, the ultimate payment remains largely assured, which is a positive.

Credit challenges

Small scale of operations with geographical concentration risk – PEBPL, established in 2007 as a private limited company, has over one and a half decade of an operational track record in the Nepalese construction sector. The company's scale of operations and its operating income, though steady, remains on a lower side compared with the industry peers, limiting its bidding capacity for the large projects as well as its economies of scale. Further, the entire project portfolio of PEBPL lies in Madhesh Pradesh (Province 2) of the country, giving rise to geographical concentration risk. Any change in the dynamics of the region could affect PEBPL's financial and operational profiles.

Liquidity risk – PEBPL's liquidity position is stretched, evident in its weak current ratio of 0.8 times as of the end of FY2023. This is attributed to relatively moderate profitability and reserves, coupled with a high reliance on supplier credit and mobilization advances for working capital management. The company also lacks working drawing power against its net current assets, reducing its ability to absorb liquidity shocks in case of sectoral slowdowns. Despite some on-balance sheet liquidity, absence of material liquidity headroom could strain the liquidity during delayed receipt of payment from employers.

Intense competition for public-sector projects and slowdown in Government capex – The construction sector of Nepal is highly competitive, given the presence of multiple large and small players. Moreover, the bidding requirement for public projects (majority of PEBPL's portfolio) creates an uncertainty regarding the company's future revenue inflow.

Public sector capex has witnessed a slowdown in recent years. Slowdown in capital spending by the public sector, coupled with operational disturbances in public projects (especially related to site clearance, etc.), could significantly impact the revenue profile of contractors like PEBPL.

Regulatory risk – PEBPL, concentrated in the public construction sector, remains exposed to the risk of regulatory changes, mainly in the Public Procurement Act and the related regulations. This risk remains further heightened with frequent regulatory changes brought in by amendments. Any future amendments imposing stricter provisions for timely

[1] *OPBDITA – Operating profit before depreciation, interest, taxes and amortisation*
[2] *DSCR-Debt Service coverage ratio*

completion and/or provisions of liquidated damages could have a substantial impact on public-contract focused players like PEBPL.

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

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

Link to previous rating rationale
Rationale-Prithivi Engineers & Builders Private Limited November 2022

About the company

Prithivi Engineers & Builders Private Limited (PEBPL) was incorporated in 2007 as a private construction company. The company mainly deals in civil construction work, primarily related to roads, water-supply projects and buildings in the public sector. It is classified as a Class-A contractor as per the classification norms of the Government of Nepal. The company is primarily involved in public contracts within Nepal, which makes up the entire contracts-on-hand in mid-May 2024.

PEBPL is a closely held company where the entire equity stake is held by four individuals, with Mr. Keshav Bahadur Dahal, Chairman and Managing Director holding ~84% stake, followed by Mr. Manahari Niraula (6.5%), Mr. Keshav Raj Dahal (5.5%) and Mr. Jeevan Ranabhat (4.1%).

Key Financial Indicators:

Particulars	Audited				
	FY2019	FY2020	FY2021	FY2022	FY2023
Operating Income-OI (NPR Million)	289.0	137.3	229.5	282.1	396.0
OPBDITA/OI (%)	7.3%	14.8%	10.9%	9.7%	13.4%
Total Debt/Tangible Net Worth-TNW (times)	0.8	0.9	0.4	0.2	0.5
Total Outside Liabilities/ TNW (times)	5.0	4.1	3.3	2.8	2.8
Total Debt/OPBDITA (times)	0.9	1.2	0.6	0.4	0.6
Interest Coverage	5.6	6.8	10.3	15.9	14.3
DSCR (times)	2.0	2.8	2.2	3.0	4.5
Current Ratio	0.9	0.8	0.9	0.9	0.8
Net Working Capital/OI (%)	-4%	-18%	-23%	-14%	-16%

Annexure-1: Instrument Details

Instrument	Current Rated Amount (NPR million)	Rating action
Fund based; long term limits (Hire Purchase loan)	39.80	[ICRANP] LBB; reaffirmed
Fund based; short term limits (Overdraft)	10.00	[ICRANP] A4; reaffirmed
Non-fund based; short-term limits (Bid Bond Guarantee/Advance Payment Guarantee/Performance Bank Guarantee/Supply Credit Guarantee)	1,325.32	[ICRANP] A4; reaffirmed
Total	**1,375.12**	

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About ICRA Nepal Limited:

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