

## Classic Tech Private Limited

### Ratings

Facilities*	Amount (Rs. in Million)	Ratings <sup>1</sup>	Rating Action
Long Term Bank Facilities	1050.00	CARE-NP B [Single B]	Revised from CARE-NP BB- and removed from Issuer not cooperating Category
Short Term Bank Facilities	450.00	CARE-NP A4 [A Four]	Reaffirmed and removed from Issuer not cooperating Category
<b>Total Facilities</b>	<b>1,500.00</b>		

\*Details of instruments/facilities in Annexure 1

In the absence of minimum information required for the purpose of credit rating, CARE Ratings Nepal Limited (CRNL) was earlier unable to express an opinion on the rating of Classic Tech Private Limited (CTPL) and in line with the extant SEBON guidelines, CRNL had moved the ratings to 'ISSUER NOT COOPERATING' category. However, the company has since submitted the requisite information to CRNL. CRNL has subsequently carried out a full review of the ratings and revised the rating assigned to the long-term bank facilities of CTPL to 'CARE-NP B' and reaffirmed the rating of 'CARE-NP-A4' assigned to its short-term bank facilities.

### Detailed Rationale & Key Rating Drivers

The revision of ratings assigned to the bank facilities of CTPL factors in its stretched liquidity profile which had resulted in instances of delays in timely debt servicing by the company. The rating continues to factor in its moderate scale of operations coupled with revenue concentration risk in the increasingly competitive retail internet business. The ratings also factor in the gradual dilution in CTPL's market share in a competitive industry with highly concentrated market, capital intensive nature of industry, technological risk associated with internet broadband business and government policy towards Internet Service Providers (ISPs). Moreover, the ratings also take cognizance of the National telecommunications authority's (NTA) demand of settlement of arrears of Royalty of 4% and Rural Telecom Development Fees (RTDF) of 2% on the revenue from monitoring and technical support provided to its customers from ISPs. Following the Supreme court ruling in favour of the NTA on May 12, 2024, this is likely to add liquidity pressure on the company to meet the demand.

The ratings, however, derive strength from CTPL's long established track record of operations with moderate market share in the internet service industry and experienced promoter and management team in the related field. The ratings also factor in the steady improvement in CTPL's operational performance aided by decrease in major cost i.e. bandwidth charges, albeit with declining trend in average revenue per customer in the industry.

*Going forward, the ability of the company to achieve revenue growth while improving profitability margins and maintaining its capital structure will be the key rating sensitivities. Additionally, any substantial debt-funded capital expenditure that would materially impact the overall financial risk profile of the company will also be a key rating sensitivity. The company's capacity to withstand the increasingly competitive business environment in the broadband internet sector and maintain a low leverage profile despite higher capital expenditure plans also remains crucial.*

### Detailed Description of the Key Rating Drivers

#### Key Rating Weaknesses

#### Stretched liquidity profile

The creditor days remain stretched primarily due to long pending dues towards its suppliers majorly pertaining to its bandwidth purchases in the past. Further, it also has to invest huge amounts on network devices and customer premises

<sup>1</sup>Complete definitions of the ratings assigned are available at <https://www.careratingsnepal.com/> and in other CRNL publications

equipment (CPE) and other accessories. Generally, the company imports the above equipment by opening letter of credit (LC), however full recovery of the same from the customers happen on due course of time which results into high reliance on working capital loans. During FY24, CTPL had inventory turnover of 205 days and debtor turnover of 62 days with creditor turnover of 297 days. Hence, the company's operating cycle came out at negative 30 days in FY24. Consequently, average working capital utilization remained over 90%. Further, there have been instances of delays in debt servicing by the company in the past and a clean debt servicing track record will remain critical from credit perspective.

### **Capital and technology intensive nature of industry**

It is an inherent nature of telecom industry which requires huge capital investments and long gestation period necessitating substantial funding support. Rolling out fiber network in a new locality is a capital-intensive business. Rolling out a fixed broadband network is a time-consuming process that requires significant capital investments over time. Further, designing a dense network (i.e., a high number of subscribers per coverage area) is crucial in order to maintain capital expenditure per subscriber at sustainable levels. A significant amount of capital expenditure may be incurred before achieving scale. Further, the laying of a door-to-door last mile network is complicated, time consuming and capital intensive given the constraints in accessing the residences of customers. Going forward, the company is likely to moderate its capital expenditure. However, to remain competitive in the ISP business, continual capital expenditures are likely in the future as well. Although some of this requirement is expected to be partly supported by operating cash flows, but any major project related Capex would require outside debt. Sustained high debt levels would translate in moderate debt coverage indicators.

### **Increasing competition in the industry with concentrated market**

Nepal's ISP industry is experiencing robust growth, driven by increasing internet penetration, the expansion of 4G networks, and rural connectivity initiatives. Despite the presence of approximately 62 ISPs in the market, which might imply a congested environment, the actual distribution of fixed broadband internet subscribers reveals a highly concentrated market. As on December 15, 2024, the top 20 ISPs collectively account for 97.34% of the market share. Within this group, the top 5 ISPs hold 72% of the market share, while the top 7 ISPs, including CTPL with 5.77% share, account for 84%. Notably, the leading ISP alone commands around 32% of the market share, highlighting significant market dominance by a few large players. Hence, CTPL faces significant challenges such as intense competition from well-established players, market saturation, and resource constraints. The larger players can afford to lower prices and provide favourable payment terms due to economies of scale and may even commence price wars, which in turn can squeeze up the profit margins of CTPL if it engages or can erode the customer base and make customer retention even more so difficult. So, it's imperative that CTPL focuses on product and service differentiation through exceptional customer service and unique offerings, formation of strategic partnerships and continuous investment in innovative technologies.

### **Concentrated revenue in terms of customer base**

Retail segment income of CTPL constitutes the major component of its total income at around 85%. However, the company is looking to increase contributions from enterprise internet and intranet, reseller etc. Further analysis of service-wise revenues revealed that in FY24, internet services to retail customers, support and maintenance services to retail customers, and services to other ISPs contributed 42%, 42%, and 8% respectively to the company's total revenues. A more diversified revenue base and clientele could help absorb pricing pressure and maintain margins particularly given the intense competition in the retail segment. In the retail segment, the ability of the company to retain customers and foster loyalty, thereby reducing churn through competitive pricing, implementation of loyalty programs with rewards and incentives to encourage repeat purchases and brand advocacy, and reliable and disruption free connection and relatively fast connection speeds while maintaining its profitability would be key to its future prospects.

### **Government policy towards Internet Service Providers**

The cost of infrastructure provided by the government to ISP's is on an increasing trend. Effective from mid-July 2019, the Nepal government had levied Telecommunication Service Charge (TSC) of 13% on internet subscription in addition to the existing 13% Value Added Tax (VAT) and subsequently reduced to 10% effective from mid-July 2022. The service charge was adjusted in the cost of the ISP's without increasing the consumer prices. The ISPs have been using the NEA's infrastructure including the transmission lines and electricity poles to expand their internet services in rural areas. The company remains exposed to any hike in the fees by the NEA for its infrastructure being used by the ISPs, which is likely to take upward the cost of internet use.

### **Exposure to technology risk associated with broadband internet business**

The broadband internet industry is rapidly advancing with significant technological developments, including the expansion of fiber-optic networks for enhanced speed and reliability, the rollout of 5G networks offering speeds up to 100 times faster than 4G, and the integration of AI to optimize performance and enhance customer experience. These innovations are driving the industry towards faster, more reliable, and widely accessible internet connectivity. However, companies must timely upgrade to the latest technologies to avoid operational impacts. Fixed broadband providers are investing in faster services, upgrading from ADSL to VDSL, and rolling out fiber optic cables. Rapid technological changes and continuous R&D spending mean new technologies may have short lifecycles, posing risks to the industry.

### **Key Rating Strengths**

#### **Experienced promoter and established track record of operations with moderate market share in internet service industry**

CTPL is the seventh largest ISP in Nepal based on total number of subscribers. As on December 15, 2024 CTPL had around 5.77% market share in Nepal's internet service industry with a customer base of 0.17 Mn out of 2.99 Mn total number of active subscribers. CTPL has a widespread coverage in the country with its presence in 75 districts of Nepal (out of 77 districts). It has 28 branches inside valley and around 104 branches spread across the country.

CTPL is promoted by Mr. Pramesh Kharel, Chairman/Managing director, having managerial and technical experience of over a decade in the internet service industry. He is supported by an experienced team across various functions.

#### **Steady operational performance**

CTPL's Total Operating Income (TOI) have increased at a compounded annual growth rate (CAGR) of around 7.6% over FY20-FY24. However, TOI of CTPL contracted by around 3% y-o-y to Rs. 921 Mn in FY24. The company's PBILDT margins remained steady between the range of 16% to 22% over FY20-FY23. However, PBILDT margin improved to 28% during FY24 on account of 27% y-o-y decrease in bandwidth costs, which accounts for approximately 79% of the cost of sales. The net profit increased by around 58% y-o-y to Rs. 51 Mn in FY24 (FY 22: Rs. 32 Mn). CTPL has integrated previously siloed support teams, including Network Build, Infra Support, and Field Workers into a fully integrated unit. This restructuring has enhanced operational efficiency and reduced employee benefit expenses by approximately 28%, from 234 Mn in FY23 to 168 Mn in FY24. However, the applicability of Royalty and RTDF on income from maintenance and support charges (which contributed to around 42% of TOI in FY24) is likely to moderate the margins of the company going forward.

#### **Moderately leveraged capital structure with adequate gearing level and debt coverage indicators**

The capital structure of CTPL stood moderately leveraged with debt-to-equity ratio and overall gearing ratio relatively steady at 2.45x and 2.69x respectively at the end of FY24 (FY23: 2.44x and 2.86x respectively) despite the increased net borrowings on account of improved tangible networth backed by equity infusion of Rs. 100 Mn in FY23 and Rs. 30 Mn in FY24 coupled

with accretion of profit. CTPL interest coverage ratio improved to 4x in FY24 (FY23: 3.67x) on account of substantial increase in PBILDT. Total debt to Gross Cash Accrual improved to 4.21x at the end of FY24 (FY23: 3.94x) supported by improved gross cash accruals.

### About the Company

CTPL was incorporated on July 16, 2009 as a private limited company named as a Zero Point Remit Private Limited and later converted to an Internet Service Provider on August 29, 2010 and Network Service Provider on March 31, 2014. CTPL provides dedicated speed internet service to individual houses with Fiber Optical Internet as FTTH Internet service. CTPL is the seventh largest ISP in Nepal in terms of fixed broadband internet subscriber base and has been operational in the industry for around 14 years.

### Financial Performance

(Rs. in Million)

For the Period Ended Mid-July,	FY22 (A)	FY23 (A)	FY24 (A)
Income from Operations	872	951	921
PBILDT Margin (%)	19.31	21.66	28.26
Overall Gearing (times)	5.87	2.86	2.69
Interest Coverage (times)	4.77	3.67	4.00
Total Debt/ Gross Cash Accruals (times)	4.43	3.94	4.21

A: Audited

### Annexure 1: Details of the Facilities Rated

Name of the Bank Facilities	Type of the Facility	Amount (Rs. in Million)	Ratings
Long Term Bank Facilities	Term Loan	1050.00	CARE-NP B
Short Term Bank Facilities	Fund Based Limits	400.00	CARE-NP A4
Short Term Bank Facilities	Non-Fund Based Limits	50.00	CARE-NP A4
<b>Total</b>		<b>1,500.00</b>	

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