

## Daulat Ram Engineering Services Private Limited

April 03, 2019

### Ratings

Facilities	Amount (Rs. Crore)	Ratings <sup>1</sup>	Rating Action
Long-term Bank Facilities	10.62 (reduced from Rs.22.72 crore)	<b>CARE BB+; Stable (Double B Plus; Outlook: Stable)</b>	<b>Reaffirmed</b>
Long-term / Short-term Bank Facilities	90.00	<b>CARE BB+; Stable/CARE A4+ (Double B Plus; Outlook: Stable /A Four Plus)</b>	<b>Reaffirmed</b>
<b>Total Bank Facilities</b>	<b>100.62 (Rupees One Hundred Crore and Sixty Two Lakh Only)</b>		

Details of instruments/facilities in Annexure-1

### Detailed Rationale & Key Rating Drivers

The ratings for the bank facilities of Daulat Ram Engineering Services Pvt. Ltd. (DRESPL) continue to remain constrained on account of its working capital intensive nature of operations, vulnerability of its profit margins to fluctuations in raw material prices, its operations in a competitive tender driven industry and customer concentration risk. The ratings also factor in the decline in DRESPL's total operating income (TOI) during 11MFY19 (FY refers to the period from April 1 to March 31) owing to the slowdown in execution, particularly for large sized orders taken in FY18.

The ratings however, continue to derive strength from the wide experience of the promoters, its established track record of operations and its moderately comfortable capital structure and debt coverage indicators. The ratings also factors in revenue visibility provided by its healthy order book, albeit moderation in execution during FY19.

The ability of DRESPL to increase its scale of operations and profit margins supported by timely dispatches of orders with further improvement in debt coverage indicators and liquidity position would remain the key rating sensitivities.

### Detailed description of the key rating drivers

#### Key Rating Weaknesses

**Working capital intensive nature of operations:** The operations of DRESPL are highly working capital intensive in nature with investment required in both inventory [due to time taken for manufacturing as well as procedure of pre-inspection and trials by Indian Railways (IR)] and receivables (due to credit period of around 60-90 days offered for various products). DRESPL's products are customized for their applications and its largest customer, IR, has a procedure of inspecting and checking of products prior to their dispatch, translating into a considerable inventory holding requirement. Further, DRESPL needs to offer a credit period of around 60-90 days and the payment is generally received with a lag of around 15-20 days post expiry of the credit period, translating into elongated receivables. DRESPL's working capital cycle lengthened from 133 days in FY17 to 173 days in FY18, primarily due to an increase in average inventory holding led by a slow pace of execution in orders, particularly for the large sized order for diesel-electric locomotives (DELs) taken in FY18. The utilization of DRESPL's working capital limits also remained almost full for the last 12 months ended December 2018.

**Vulnerability of profit margins to fluctuations in raw material prices:** The primary raw material used by DRESPL are copper, aluminum and steel (MS) for various equipment that it manufactures. The prices of these raw materials are volatile in nature and hence, DRESPL'S profitability is exposed to risk to such extent. Further, even as DRESPL derives some revenue from export of its products, it does not hedge its foreign exchange exposure, which exposes it to adverse movement in forex rates to a certain extent. However, some imports, particularly of technically important components, do provide natural hedge to a certain extent.

**Competitive and tender driven nature of industry:** A majority of IR's procurement is tender-driven and DRESPL needs to participate in those tenders to gain business from its largest customer. This translates into competition from various small and medium scale players present at the regional level for the company and hence, it needs to continuously innovate and improve its product offering while pricing it competitively. This limits the profitability of the company to a certain extent. However, with focus on better margin products, DRESPL was able to improve its profitability in FY18, with a PBILDT margin of 20.56% during the year, compared with 13.28% in FY17.

**Customer concentration risk:** The products of DRESPL are used primarily by Indian Railways for its diesel and electric locomotives and passenger coaches. Any slowdown in investment by Indian Railways may adversely impact DRESPL's

<sup>1</sup>Complete definitions of the ratings assigned are available at [www.careratings.com](http://www.careratings.com) and in other CARE publications.

scale of operations and profitability. However, due to the distributed nature of railway procurement, the orders are placed by various divisional offices and independent factories (locomotive and coach factories) and hence, the client concentration reduces to that extent. Also, DRESPL has well-established and long standing relationship with various procurement centers of Indian Railways and has regularly received repeat business from them.

#### Key Rating Strengths

**Experienced promoters with established track record:** The promoters of DRESPL have a rich experience in the area of locomotive equipment manufacturing. The promoters collectively look after the operations of DRESPL and are responsible for all the strategic decisions. They are suitably aided by professionals at various levels for management of daily operations of the company.

**Improvement in operating profitability during FY18 due to focus on better margin products:** DRESPL reported a decline of 11% y-o-y in its total operating income in FY18 on the back of change in business strategy to focus on better margin products. This translated into improvement in DRESPL's operating profitability, which along with stable interest costs resulted in better PAT margin and higher cash accruals. DRESPL's capital structure remained moderately comfortable with an overall gearing of 0.87x as on March 31, 2018 (1.11x as on March 31, 2017). DRESPL's debt coverage indicators also remained moderately comfortable marked by interest coverage of 3.15x and total debt/GCA of 3.70x in FY18.

**Healthy order book; albeit focus on high value items translated into reduction in TOI during 11MFY19:** As on January 20, 2019, DPRL had a sizeable order book of around Rs.356.17 crore consisting of large value orders including DELs (Rs.181.08 crore) and diesel-electric tower cars (DETCs; Rs.31.15 crore), which provides good revenue visibility in the medium-term. However, in 11MFY19, DRESPL's TOI reduced sharply to around Rs.50.00 crore, on account of DRESPL's focus on execution of DELs, for which it kept certain execution capacity idle and did not take up adequate small sized orders. As the production and dispatch of DELs was delayed due to various reasons, including non-availability of components for the same. Going forward, DRESPL's ability to maintain its scale of operations (so as to adequately absorb overheads) would depend on its ability to timely deliver as per its orders and to secure fresh orders at adequate profitability.

**Liquidity analysis:** DRESPL's liquidity remained moderate despite higher cash accruals and reduction in outstanding receivables, as the increase in overall working capital requirements translated into sizeable inventory as at the end of FY18. On an overall basis, DRESPL's working capital cycle elongated from 133 days in FY17 to 173 days in FY18. Its working capital limits remained fully utilized for the trailing 12 months ended February 2019.

**Analytical Approach:** Standalone.

#### Applicable Criteria

[Criteria on assigning Outlook to Credit Rating](#)

[CARE's Policy on Default Recognition](#)

[CARE's methodology for manufacturing companies](#)

[Criteria for Short Term Instruments](#)

[Financial ratios – Non- Financial Sector](#)

#### About the Company

Raisen, Madhya Pradesh based Daulat Ram Engineering Services Pvt. Ltd. (DRESPL) was incorporated in 1997 by Mr. Chandra Prakash Sharma. Initially, the company was engaged in repair, reconditioning and rehabilitation of dynamic braking resistors for Indian Railways. Later, DRESPL commenced manufacturing of motors, traction motors and alternators, auxiliary generator, traction motors, oil cooling blower and many other engineering products which find its application in railway locomotives. It supplies its products to various diesel locomotive manufacturing units of Indian Railways including DMW – Patiala, DLW – Varanasi, CLW – Chittaranjan and to Bharat Heavy Electricals Limited (BHEL) for onward supply to Indian Railways. DRESPL also exports its products to private railway entities in USA, which contributed 3.5% of its revenue in FY18. The company has also commenced manufacturing and installation of escalators at various railway stations as well as manufacturing of vacuum toilet systems for rail coaches. In FY18, DRESPL also received its first order for supplying 22 fully built diesel locomotives to Indian Railways.

Brief financials of DRESPL are tabulated below:

Brief Financials (Rs. crore)	FY17 (A)	FY18 (A)
Total operating income	120.09	107.25
PBILDT	15.95	22.05
PAT	3.38	8.56
Overall gearing (times)	1.11	0.87
Interest coverage (times)	2.51	3.15

A: Audited

Further, during 11MFY19, DRESPL reported a total operating income of Rs. 50.00 crore.

**Status of non-cooperation with previous CRA:** Not Applicable

**Any other information:** Not Applicable

**Rating History for last three years:** Please refer Annexure-2

**Note on complexity levels of the rated instrument:** CARE has classified instruments rated by it on the basis of complexity. This classification is available at [www.careratings.com](http://www.careratings.com). Investors/market intermediaries/regulators or others are welcome to write to [care@careratings.com](mailto:care@careratings.com) for any clarifications.

**Analyst Contact:**

Name: Mr. Harshveer Trivedi

Tel: 079 4026 5610

Mobile: 85111 90020

Email: [harshveer.trivedi@careratings.com](mailto:harshveer.trivedi@careratings.com)

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## Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Term Loan	-	-	January 2024	10.62	CARE BB+; Stable
Fund-based - LT/ ST-CC/PC/Bill Discounting	-	-	-	50.00	CARE BB+; Stable / CARE A4+
Non-fund-based - LT/ ST-Bank Guarantees	-	-	-	40.00	CARE BB+; Stable / CARE A4+

## Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016
1.	Fund-based - LT-Term Loan	LT	10.62	CARE BB+; Stable	1)CARE BB+; Stable (04-Apr-18)	1)CARE BB; Stable (28-Apr-17)	-	1)CARE BB (12-Feb-16) 2)CARE BB- (07-Apr-15)
2.	Fund-based - LT/ ST-CC/PC/Bill Discounting	LT/ST	50.00	CARE BB+; Stable / CARE A4+	1)CARE BB+; Stable / CARE A4+ (04-Apr-18)	1)CARE BB; Stable / CARE A4 (28-Apr-17)	-	1)CARE BB / CARE A4 (12-Feb-16) 2)CARE BB- (07-Apr-15)
3.	Non-fund-based - LT/ ST-Bank Guarantees	LT/ST	40.00	CARE BB+; Stable / CARE A4+	1)CARE BB+; Stable / CARE A4+ (04-Apr-18)	1)CARE BB; Stable / CARE A4 (28-Apr-17)	-	1)CARE BB / CARE A4 (12-Feb-16) 2)CARE BB- / CARE A4 (07-Apr-15)

**CONTACT****Head Office Mumbai**

**Ms. Meenal Sikchi**  
Cell: + 91 98190 09839  
E-mail: [meenal.sikchi@careratings.com](mailto:meenal.sikchi@careratings.com)

**Ms. Rashmi Narvankar**  
Cell: + 91 99675 70636  
E-mail: [rashmi.narvankar@careratings.com](mailto:rashmi.narvankar@careratings.com)

**Mr. Ankur Sachdeva**  
Cell: + 91 98196 98985  
E-mail: [ankur.sachdeva@careratings.com](mailto:ankur.sachdeva@careratings.com)

**Mr. Saikat Roy**  
Cell: + 91 98209 98779  
E-mail: [saikat.roy@careratings.com](mailto:saikat.roy@careratings.com)

**CARE Ratings Limited**

(Formerly known as Credit Analysis & Research Ltd.)

Corporate Office: 4th Floor, Godrej Coliseum, Somaiya Hospital Road, Off Eastern Express Highway, Sion (East), Mumbai - 400 022  
Tel: +91-22-6754 3456 | Fax: +91-22-6754 3457 | E-mail: [care@careratings.com](mailto:care@careratings.com)

**AHMEDABAD**

**Mr. Deepak Prajapati**  
32, Titanium, Prahaladnagar Corporate Road,  
Satellite, Ahmedabad - 380 015  
Cell: +91-9099028864  
Tel: +91-79-4026 5656  
E-mail: [deepak.prajapati@careratings.com](mailto:deepak.prajapati@careratings.com)

**BENGALURU**

**Mr. V Pradeep Kumar**  
Unit No. 1101-1102, 11th Floor, Prestige Meridian II,  
No. 30, M.G. Road, Bangalore - 560 001.  
Cell: +91 98407 54521  
Tel: +91-80-4115 0445, 4165 4529  
Email: [pradeep.kumar@careratings.com](mailto:pradeep.kumar@careratings.com)

**CHANDIGARH**

**Mr. Anand Jha**  
SCF No. 54-55,  
First Floor, Phase 11,  
Sector 65, Mohali - 160062  
Chandigarh  
Cell: +91 85111-53511/99251-42264  
Tel: +91- 0172-490-4000/01  
Email: [anand.jha@careratings.com](mailto:anand.jha@careratings.com)

**CHENNAI**

**Mr. V Pradeep Kumar**  
Unit No. O-509/C, Spencer Plaza, 5th Floor,  
No. 769, Anna Salai, Chennai - 600 002.  
Cell: +91 98407 54521  
Tel: +91-44-2849 7812 / 0811  
Email: [pradeep.kumar@careratings.com](mailto:pradeep.kumar@careratings.com)

**COIMBATORE**

**Mr. V Pradeep Kumar**  
T-3, 3rd Floor, Manchester Square  
Puliakulam Road, Coimbatore - 641 037.  
Tel: +91-422-4332399 / 4502399  
Email: [pradeep.kumar@careratings.com](mailto:pradeep.kumar@careratings.com)

**HYDERABAD**

**Mr. Ramesh Bob**  
401, Ashoka Scintilla, 3-6-502, Himayat Nagar,  
Hyderabad - 500 029.  
Cell : + 91 90520 00521  
Tel: +91-40-4010 2030  
E-mail: [ramesh.bob@careratings.com](mailto:ramesh.bob@careratings.com)

**JAIPUR**

**Mr. Nikhil Soni**  
304, Pashupati Akshat Heights, Plot No. D-91,  
Madho Singh Road, Near Collectorate Circle,  
Bani Park, Jaipur - 302 016.  
Cell: +91 – 95490 33222  
Tel: +91-141-402 0213 / 14  
E-mail: [nikhil.soni@careratings.com](mailto:nikhil.soni@careratings.com)

**KOLKATA**

**Ms. Priti Agarwal**  
3rd Floor, Prasad Chambers, (Shagun Mall Bldg.)  
10A, Shakespeare Sarani, Kolkata - 700 071.  
Cell: +91-98319 67110  
Tel: +91-33- 4018 1600  
E-mail: [priti.agarwal@careratings.com](mailto:priti.agarwal@careratings.com)

**NEW DELHI**

**Ms. Swati Agrawal**  
13th Floor, E-1 Block, Videocon Tower,  
Jhandewalan Extension, New Delhi - 110 055.  
Cell: +91-98117 45677  
Tel: +91-11-4533 3200  
E-mail: [swati.agrawal@careratings.com](mailto:swati.agrawal@careratings.com)

**PUNE**

**Mr. Pratim Banerjee**  
9th Floor, Pride Kumar Senate,  
Plot No. 970, Bhamburda, Senapati Bapat Road,  
Shivaji Nagar, Pune - 411 015.  
Cell: +91-98361 07331  
Tel: +91-20- 4000 9000  
E-mail: [pratim.banerjee@careratings.com](mailto:pratim.banerjee@careratings.com)

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