Oriental Structural Engineers Private Limited (Revised)

February 3, 2020

Ratings

Facilities	Amount (Rs. crore)	Rating1	Rating Action
Long-term Bank Facilities	894.44 (enhanced from 784.06)	CARE A; Stable (Single A; Outlook: Stable)	Rating revised from CARE A- (Single A Minus) and removed from credit watch
Long-term/Short-term Bank Facilities – LC/BG	1535.00 (enhanced from 1250.00)	CARE A; Stable / CARE A1 (Single A; Outlook: Stable /A One)	Rating revised from CARE A- /A2+(Single A Minus/ A Two Plus) and removed from credit watch
Total Facilities	2,429.44 (Rupees Two thousand four hundred and forty nine crore and forty four lakh only)		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings of OSE were placed under "Credit watch with developing implications" in Dec'19 following an Income Tax search on the Oriental Group. Subsequently, CARE has held detailed discussions with the OSE management, one of the InvIT investors and also examined legal and tax opinions on the expected tax liability of the InviT transaction concluded by OSE in June 2019. CARE understands that so far no tax demand has been raised and there has not been any adverse action or significant seizure of documents or freezing of accounts of OSE that would have potentially interrupted the normal operations of the company. The removal of 'credit watch with developing implications' takes into account our assessment of the legal /tax opinions on the matter and the fact that there has been no material adverse outcome so far on account of the tax raid. While an enquiry of this nature may take a long time to conclude, CARE will closely monitor the situation and if any material adverse outcome arises of the tax assessment, the same would be suitably factored in time and therefore, would remain a key rating sensitivity.

CARE has also revised the credit ratings assigned to the bank facilities of Oriental Structural Engineers Pvt Ltd (OSE). The same takes into account the enhanced liquidity position of the company on account of the establishment of Oriental Infra Trust (OIT) (InviT) leading to a net inflow of Rs. 871.75 crs to the company. OSE along with Oriental Tollways Pvt Ltd (OTPL), the holding company of the road SPVs of the group, holds 60.45% of the InvIT units and would therefore benefit from a regular stream of interest and dividend distribution from OIT. The resultant accretion to Net worth of the company which stands at Rs.2511.13 crs as on 30th September 2019 (Rs. 1722.10 as on cr 31st March 2019) has led to a comfortable capital structure with gearing at 0.47x as on 30th September 2019. Further, post InvIT, the overall investment in underlying SPVs has reduced by Rs. 829.58 cr as on 30th September 2019. Additionally, there is satisfactory progress on the 3 HAM projects of the company which also form part of the order book and OSE has already met approximately 50% of the equity commitment in its 3 HAM projects as on 30th September 2019. Besides, CARE expects that the InvIT would be a vehicle by which OSE can monetize its operational road assets on a continuing basis, thereby providing significant financial flexibility going forward. The ratings also positively factor in the moderate financial performance of the company during FY19 and H1FY20 with a topline growth of 13.43% y-o-y and operating profitability of 17.50%, moderate order book position providing a revenue visibility of 1.52x which is likely to increase as the company would be expected to bid for more projects under the HAM model in the next 1 year. The company enjoys a long and established track record in the construction industry with experienced promoters and management team.

The rating strengths, however, are tempered by, risks pertaining to the EPC business, fixed-time fixed-price nature of contracts for the group's HAM projects, and susceptibility of margins to the volatility associated with input costs. The overall tightness in the lending environment currently being witnessed for the construction industry may have a negative bearing for all players in the industry.

Rating Sensitivities:

Positive factors:

[1] *Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*

- Increase in scale of operations by 15%-20% and sustained profitability at current levels
- Improvement in order book position with a revenue visibility of 2.5x-3x with quality counterparties
- Continued monetisation of assets thereby providing financial flexibility to the company
- Further improvement in gearing levels and maintaining a healthy liquidity position on an on going basis.

Negative factors

- Adverse implications of the Income Tax search
- Increased financial support to SPVs impacting cash flow cushion and liquidity of OSE
- Delays in the progress of ongoing work orders leading to under achievement of revenues
- Elongation in operating cycle beyond 100 days

Detailed description of the key rating drivers

Key Rating Strengths

Establishment of InvIT leading to improved liquidity

OSE has formed an infrastructure investment trust (InvIT) by transferring 5 operational SPVs (1 Annuity road project, 4 Toll road projects) for a total enterprise value of Rs.11,638 crore. From the InvIT proceeds, the OSE group has received a consideration of Rs.540 crs by selling its share under 'offer for sale' to the InvIT. OSE has received a net inflow of Rs. 871.75 crs which also includes unwinding of unsecured group loans. The cash inflow from the InvIT has improved the liquidity position of the company substantially (refer liquidity section below). Additionally, the company is expected to distribution income from the surpluses of the trust.

Further, as a result of InvIT transaction the net worth of the company has improved to Rs. 2511.13 cr as on 30th September 2019 leading to comfortable gearing of 0.47x as against overall gearing of 0.71x as on 31st March 2019.

Going forward, InvIT would be a vehicle by which OSE can monetize its operational road assets on a continuing basis, thereby providing significant financial flexibility to the company.

Moderate financial performance during FY19

During FY19, OSE's (standalone) operating income increased by 13.43% Y-o-Y to Rs.2764.05 crore and PAT declined by 10% Y-o-Y to Rs.199.91 crore (after adjusting one time write off of Rs. 78.95 crore). PBILDT margin declined to 17.50% in FY19 as compared to margin of 19.10% in FY18 an account of write-offs of Rs. 112.08 crore. Further, various orders have picked up pace such as Binjhabahal-Telebani, Rajiv Chowk project, Agra-Etawah and Purvanchal expressway projects in FY20 providing substantial revenue visibility for FY20 and FY 21. During H1FY20 (Prov.), the company has reported total income of Rs.1,112.29 crore and PAT of Rs.75.56 crore.

Moderate order book position

OSE has a moderate unexecuted EPC and coal mining order book position of 4,205 crore (Rs.3821 crore EPC and Rs.384 crore coal mining) as on September 30, 2019, which translates into 1.52x of FY19 total income. Order book position of the company has declined as compared to Rs.8,626 crore of unexecuted orders as on June 30, 2018 on account of cancellation of some works in the order book viz. Amravati-Chikali road work (Order worth Rs. 949.21 crore), an ITNL project was cancelled by NHAI and Villupuram-Puduchery HAM project (Order worth Rs. 949.21 crore) by NHAI. However, the company is planning to bid for new orders in the road segment either in EPC mode or under Hybrid Annuity Model.

Experienced promoters and management and long track record of operations

OSE has a long track record of almost four decades in the construction industry with main expertise and experience in roads and highways segment.

Track record of timely execution of projects

OSE has executed several major infrastructure projects in the past. OSE has track record of completing majority of its projects in timely manner including its road BOT projects under SPVs.

Key Rating Weaknesses

Investment requirement in HAM projects and support towards BOT projects

The company has met part equity commitment for Rajiv Chowk Sohna, Binjhabahal Talebani and Kallagam projects through the proceeds of Invit Issue. Further, the remaining equity requirement amounting to Rs.166.18 crore for the HAM projects will be met from internal accruals in FY20- FY21. Also, with the transfer of five SPVs to the Invit, the company has underlying HAM projects in which debt is tied up and part equity has already been infused. The company also has three operational toll

projects where support required from OSE is likely to be limited. However, going forward, if the company undertakes more HAM projects, there will be an increase in the equity requirements in the SPVs.

Susceptibility of margins to the volatility associated with input costs
The fixed-time fixed-price nature of the EPC contracts for the in-house projects exposes the company's margins to the volatility associated with input costs.

Inherent challenges associated with the construction sector along with challenging fund raising environment for the sector
The construction sector is facing hurdles in fund raising with delayed enhancement of working capital limits, delay in financial closure and equity raising plans on account of challenging business environment for the sector and weakened financial health of the banking sector. The inherent risk involved in the construction industry including aggressive bidding, traffic risk, interest rate risk, volatile commodity prices and delay in project progress due to resistance towards land acquisition and regulatory clearances have collectively affected the credit profile of developers in the past.

Liquidity Analysis: Adequate
As on November 13, 2019, the Company had cash and bank balance of Rs. 1.43 crore, mutual fund investment of Rs. 25 crore and FDR of Rs. 58 crore. Average utilization of fund based limits during the 12 months period ending December 2019 remained moderate at 39.77%. Moreover in the period July'19 – Dec'19, which is the period post invIT, the CC utilization has reduced to an average 6.20%.
Further, the company is generating cash accruals in the range of Rs. 250-300 cr annually which adequately covers its repayment obligations of Rs. 100-Rs. 110 cr and also the balance equity investments of Rs.166.18 crs in the ongoing 3 HAM projects which are required to be infused in FY 20 and FY 21 . Moreover, the company would also receive distribution income from OIT annually which would further enhance its liquidity.

Analytical approach: Standalone

Applicable Criteria
Criteria on assigning Rating Outlook and Credit Watch
CARE's Policy on Default Recognition
Criteria for Short Term Instruments
Rating Methodology-Construction Sector
Rating Methodology-Consolidation Factoring Linkages in Ratings
Financial Ratios – Non-Financial Sector

About the Company

OSE, incorporated in June 1971, is engaged in the construction of roads and highways, rigid and flexible pavements for roads, airfields, bridges and earthwork. The company is promoted by Mr K S Bakshi along-with other promoter directors Mr P S Sethi and Mr A S Bakshi. Dabur group holds a minority stake in the company.
OSE has presence in infrastructure sector with specialization in roads and highways segment. OSE has a significant presence in road BOT and HAM projects. OSE along with its wholly-owned subsidiary, Oriental Tollways Private Limited (OTPL) has a portfolio of 7 road projects under various Special Purpose Vehicles (4 BOT Toll and 3 HAM), of which 4 BOT projects are operational and 3 HAM projects are under execution. . During FY15, OSE had also forayed into the coal mining segment.
In June 2019, OSE has sold 5 assets to Oriental Infra Trust (Invit). OSE and its wholly-owned subsidiary, Oriental Tollways Private Limited (OTPL) are sponsors of Oriental InfraTrust and hold 60.45% stake in InvIT and rest is held by the investors.

Covenants of rated instrument / facility: *Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3*

Brief Financials (Rs. crore)	FY19 (A)	FY18 (A)
Total operating income	2,764.05	2,436.69
PBILDT	404.81	465.37
PAT	120.96	221.97
Overall gearing (times)	0.71	0.90
Interest coverage (times)	2.73	4.35

A: Audited

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

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

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-Cash Credit	-	-	-	250.00	CARE A; Stable
Non-fund-based - LT/ ST-BG/LC	-	-	-	1535.00	CARE A; Stable / CARE A1
Fund-based - LT-Term Loan	-	-	December 2031	644.44	CARE A; Stable

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 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017
1.	Fund-based - LT-Cash Credit	LT	250.00	CARE A; Stable	1)CARE A- (Under Credit watch with Developing Implications) (13-Dec-19)	1)CARE A-; Stable (05-Oct-18)	1)CARE A-; Stable (26-Dec-17) 2)CARE BBB+; Stable (05-May-17)	1)CARE A- (27-Apr-16)
2.	Non-fund-based - LT/ ST-BG/LC	LT/ST	1535.00	CARE A; Stable / CARE A1	1)CARE A- / CARE A2+ (Under Credit watch with Developing Implications) (13-Dec-19) 2)CARE A-; Stable / CARE A2+ (05-Apr-19)	1)CARE A-; Stable / CARE A2+ (05-Oct-18)	1)CARE A-; Stable / CARE A2+ (26-Dec-17) 2)CARE BBB+; Stable / CARE A2 (05-May-17)	1)CARE A- / CARE A2+ (27-Apr-16)
3.	Fund-based - LT-Term Loan	LT	644.44	CARE A; Stable	1)CARE A- (Under Credit watch with Developing Implications) (13-Dec-19) 2)CARE A-; Stable (05-Apr-19)	1)CARE A-; Stable (05-Oct-18)	1)CARE A-; Stable (26-Dec-17) 2)CARE BBB+; Stable (05-May-17)	1)CARE A- (27-Apr-16)
4.	Fund-based - ST-Term loan	ST	-	-	-	-	1)Withdrawn (26-Dec-17) 2)CARE A2 (05-May-17)	1)CARE A2+ (27-Apr-16)

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities

Long term loan	Detailed explanation
A. Financial covenants	• DSCR>=1.25x for the tenor of facility • Total Debt/EBITDA <=3.5x • Long term external liability (excluding equipment loan) to be capped at Rs. 1000 cr • Long term external liability (i.e. long term debt+ equipment Loan+ guarantees for claims/arbitration to NHAI) to be capped at Rs. 1500 cr • Total Debt/ TNW to be <= 1.0x
B. Non Financial Covenants	• Banks facilities to be utilized for the purpose as per RBI's guidelines • Promoters to directly/indirectly have at least 51% unencumbered shares of both economic and voting interest in the share capital of the borrower and also have the management control of the borrower

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. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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