

## Velji Ratna Sorathia Infra Private Limited

August 18, 2020

### Ratings

Facilities	Amount (Rs. Crore)	Ratings <sup>1</sup>	Rating Action
Long-term Bank Facilities	19.50	<b>CARE BBB; Stable (Triple B; Outlook: Stable)</b>	Removed from credit watch with negative implications; Rating reaffirmed
Long-term/Short-term Bank Facilities	120.50	<b>CARE BBB; Stable/ CARE A3 (Triple B; Outlook: Stable / A Three)</b>	Removed from credit watch with negative implications; Ratings reaffirmed
Total	<b>140.00 (Rupees One hundred Forty crore only)</b>		

*Details of instruments/facilities in Annexure-1*

### Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Velji Ratna Sorathia Infra Private Limited (VRSIPL) were placed under credit watch in light of the company (earlier firm) being alleged as a beneficiary in e-tender scam of Madhya Pradesh (MP).

Subsequently, CARE has held detailed discussion with VRSIPL's management to understand the impact of punitive actions and financial implications consequent to above. CARE also takes cognizance of the fact that all the tenders, in which VRSIPL was alleged as a beneficiary, are cancelled by the nodal agency and bank guarantee for the orders is also released. The removal of 'credit watch with negative implications' takes into account the fact so far no disciplinary action has been taken by any of the nodal agencies of MP and there has not been any adverse impact of proceedings on operational & financial performance of the company till date. Furthermore, VRSIPL has been awarded new projects in MP & other states by state as well as central government authorities during 5MFY21( refers to the period April 01 to August 05) and payments has also been released for ongoing projects of VRSIPL. 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, the same would be suitably factored in time and therefore, would remain a key rating sensitivity.

The ratings continue to derive strength from extensive experience of the promoters and its established presence of over four decades in the construction industry, ownership of sizeable fleet of equipment & machinery, healthy order book with low counterparty credit risk reflecting good revenue visibility, comfortable capital structure and moderate scale of operations & debt coverage indicators during FY20 (refers to the period April 1 to March 31).

The ratings continue to remain constrained on account of working capital intensive nature of its operations resulting in stretched liquidity position, geographical concentration of its order book, construction risk associated with timely execution of orders in hand, susceptibility of its profitability to volatile raw material prices and its presence in a highly competitive and fragmented construction industry.

The ratings are further constrained on account of expected slowdown in construction industry owing to COVID-19 and risk aversion among lenders for the construction industry.

CARE also takes cognizance of the company availing the moratorium granted by its lenders as a COVID-19 relief measure (as permitted by the Reserve Bank of India) on equipment loans and a part of its working capital facilities.

### Rating Sensitivities

#### Positive Sensitivities

- Timely execution of its orders on hand and consequent increase in total operating income (TOI) by 15% along with PBILDT margin above 11.50% on a sustained basis.
- Improvement in liquidity through lower utilization of working capital facilities or healthy liquidity cushion in the form of free cash & bank balances/ investments.

#### Negative Sensitivities

- Any adverse action by any authority w.r.t. e-tender scam in MP.
- Any delay in execution of ongoing orders resulting in lower than envisaged TOI and profitability.
- Increase in working capital intensity which in turn increases its gross current asset days to more than 200 days.

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

## Detailed description of the key rating drivers

### Key Rating Strengths

**Vast experience of promoters:** VRSIPL was promoted by Late Mr. Velji Ratna Sorathia and his family members. The company is currently managed by, Mr. Haresh Sorathia, Managing director (third generation of the family), who has a rich experience of more than a decade in the construction industry. He is at the helm of operations and is supported by a team of engineers & project managers.

**Long track record of operations:** VRSIPL has an established track record of over four decades in the construction industry. Earlier, the company used to execute small to mid-size irrigation & pipeline projects, however, during last three years, VRSIPL has scaled up its order book and diversified its order book by bidding for building and road construction contracts. VRSIPL is a registered 'AA' class contractor with Public Works Department (PWD) of Government of Gujarat, Rajasthan & Madhya Pradesh.

**Healthy order book position with low counterparty credit risk reflecting good revenue visibility:** VRSIPL has a healthy order book of Rs.1120 crore (2.56x of TOI for FY20) as on July 5, 2020 translating into good revenue visibility in the medium term. Further, VRSIPL has low counterparty credit risk as majority of the outstanding orders are from government authorities. Since last review the company bagged three new orders amounting to Rs.43 crore in MP.

Furthermore, the counterparty credit risk in the present order book is low as almost all the orders are from government entities (including urban local bodies, state governments and central government undertakings) including government corporations.

Furthermore, VRSIPL's outstanding order book is well diversified with strong presence in road segment (61%) followed by water supply & irrigation projects (22%) and dam, bridge & building construction projects (17%). Execution of orders on hand within envisaged cost and timelines remains crucial from the credit perspective. Further, movement in orders, in which VRSIPL has been declared as lowest bidder, as envisaged will also be a key monitorable.

**Ownership of sizeable equipment & machinery:** During the last three years ending FY20, VRSIPL has added equipment & machinery required for timely and efficient execution of road and other projects. Consequently, gross block of VRSIPL stood at around Rs.168 crore as on March 31, 2020 (Rs.137.94 crore as on March 31, 2019). However, debt funded investment in fleet of machinery has led to increase in interest cost and deterioration in debt coverage indicators.

**Comfortable capital structure and moderate debt coverage indicators:** VRSIPL's capital structure continued to remain comfortable with below unity overall gearing of 0.89x as on March 31, 2020 (0.85x as on March 31, 2019). After change in its constitution to a private limited company during FY20, a part of partners' capital was converted into unsecured loan and the same was subordinated to bank borrowings in line with sanction terms. Hence, considering unsecured loans as a part of net-worth, the overall gearing remained comfortable as on March 31, 2020.

Debt coverage metrics remained moderate in FY20 (Provisional) marked by PBILDT interest coverage of 5.57x (FY19: 6.39x) and total debt to gross cash accruals of 2.52x (FY19: 2.70x) on account of increase in interest cost and total debt.

**Moderate scale of operations albeit improvement in profitability:** During FY20 (Provisional), VRSIPL's TOI declined marginally to Rs.438 crore (FY19: 467 crore) owing to forced lockdown by the government due to COVID-19 which in turn hampered the project execution and also the company was not able to raise invoices for work done. Further, with the continuation of lockdown due to COVID-19 during Q1FY21, the construction activities were impacted for around 1-1.5 months. However, with resumption of operations from May 2020 along with adequate labour & raw material availability, VRSIPL was able to scale up project execution & it reported TOI of Rs.110 crore till August 5, 2020. (Provisional; refers to the period April 1 to August 5, 2020).

Further, VRSIPL's PBILDT margin improved by 140 bps y-o-y to 11.23% during FY20 (Provisional), primarily on account of reduction in sub-contract expenses. During FY20, VRSIPL reported healthy gross cash accruals of around Rs.34 crore (FY19: Rs.29.47 crore).

### Key Rating Weaknesses

**Working capital intensive nature of operations:** VRSIPL's operations has high working capital intensity primarily due to funding requirement for security deposits, retention amount and margin money towards various contracts & non-fund-based facilities along with moderate receivable levels. Consequently, VRSIPL's working capital cycle elongated to 57 days during FY20 (FY19: 38 days) on account of increase in receivables days.

However, with resumption of operations, certification of pending work and release of payments, receivables (including retention money) reduced to Rs.86 crore as on June 30, 2020 from Rs.121 crore as on March 31, 2020.

**Geographical concentration of revenue profile:** Out of total order book of Rs.1120 crore, around 74% is in the state of MP which exposes VRSIPL's growth prospectus to the macro and socio-political upheavals in the region. However, VRSIPL is favorably placed for its contracts in MP as it has in-house managerial resources and better control on execution due to proximity of orders.

**Susceptibility of its profitability to volatile raw material prices:** Since execution of VRSIPL's orders usually ranges from 12- 36 months, its profitability remains susceptible to volatile raw material prices in case of any significant adverse variation in raw material prices or delay in project execution. However, presence of an inflation index-linked price escalation clause in most of the present orders on hand with an execution timelines beyond 12 months mitigates this risk to an extent.

**Presence in an intensely competitive & fragmented construction industry:** VRSIPL is a mid-sized player operating in an intensely competitive construction industry wherein contracts are awarded on the basis of relevant experience of the bidder, financial capability and most attractive bid price. The high competitive intensity also results in aggressive bidding, which exerts pressure on the margins. Notwithstanding above, interest rate risk, delay in achieving financial closure/ availability of working capital limits and delays in project due to environmental clearance are other external factors that affect the credit profile of industry players.

**Impact of COVID-19 and execution risk:** Supply chain disruptions and reverse migration of labourers following nationwide lockdown to combat COVID-19 pandemic has resulted in moderation of construction activities across India. While the government is taking numerous steps to ease the impact including extension of time in projects, scaling up of operations is envisaged to take time due to onset of monsoon in the Indian subcontinent.

VRSIPL is also exposed to execution risk owing to delay in obtaining various regulatory clearances in some projects resulting in time overrun. Moreover, some of the projects in VRSIPL's order book are approaching scheduled completion timelines or has exceeded scheduled completion timelines, which will necessitate ramping up execution and/or an extension of time (EOT) from the client. Hence, receipt of requisite clearances and EOT in a timely manner remains crucial from the credit perspective.

#### **Liquidity: Stretched**

VRSIPL's liquidity position remained stretched with almost full utilisation of its fund based working capital limits during the trailing twelve months ended June 2020, increase in working capital intensity of its operations and modest free cash & bank balance. The average utilisation of non-fund based working capital facilities also remained high at 90% during the trailing twelve months ended June 2020. As on June 30, 2020, VRSIPL has free cash and bank balance of around Rs.0.17 crore (apart from lien marked balance of Rs.28.14 crore).

Going forward, VRSIPL is envisaged to report cash accruals of about Rs.25-28 crore, as against scheduled debt servicing obligations (principal installment) of around Rs.14-16 crore in FY21. However, higher than envisaged working capital requirement or lower than expected cash accruals due to moderation in project execution may exert pressure on its liquidity.

#### **Analytical Approach: Standalone**

##### **Applicable Criteria:**

[Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings](#)

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

[CARE's Policy on Curing period](#)

[Criteria for Short Term Instruments](#)

[Rating Methodology – Construction Sector](#)

[Financial Ratios-Non Financial sector](#)

[Liquidity Analysis of Non-Financial Sector Entities](#)

##### **About the company**

Constituted in 1974 as a partnership firm, Vadodara-based VRSIPL (erstwhile known as Sorathia Velji Ratna & Company) was promoted by Late Mr. Velji Ratna Sorathia. The company is currently managed by third generation of the family with Mr. Haresh Sorathia as the managing director. The firm changed its constitution from partnership firm to private limited company w.e.f. September 3, 2019.

During the initial years, the company was engaged in construction of overhead tanks and underground sump works. Over the years, VRSIPL has expanded the business and now executes roads, buildings, dams, canal, bridge and water supply projects on EPC basis.

Brief Financials of the firm (Rs. crore)	FY19 (A)	FY20 (P)
Total operating income	466.81	437.79
PBILDT	45.89	49.16
PAT	17.22	19.43
Overall gearing (times)	0.85	0.89
PBILDT Interest coverage (times)	6.39	5.57

A: Audited; P: Provisional (CA certified)

**Status of non-cooperation with previous CRA:** BWR BB+; Stable/ BWR A4+; ISSUER NOT COOPERATING, based on best available information. Brickworks in its press release dated January 28, 2020 had revised the ratings from BWR BBB; Stable/ BWR A3 for lack of requisite information.

**Any other information:** Not Applicable

**Rating History (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	-	-	-	19.50	CARE BBB; Stable
Non-fund-based - LT/ ST-Bank Guarantees	-	-	-	120.50	CARE BBB; Stable / CARE A3

#### 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 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Fund-based - LT-Cash Credit	LT	19.50	CARE BBB; Stable	-	1)CARE BBB (Under Credit watch with Negative Implications) (02-Mar-20) 2)CARE BBB+; Stable (03-Apr-19)	-	1)CARE BBB+; Stable (08-Mar-18)
2.	Non-fund-based - LT/ ST-Bank Guarantees	LT/ST	120.50	CARE BBB; Stable / CARE A3	-	1)CARE BBB / CARE A3 (Under Credit watch with Negative Implications) (02-Mar-20) 2)CARE BBB+; Stable / CARE A3+ (03-Apr-19)	-	1)CARE BBB+; Stable / CARE A3+ (08-Mar-18)

#### Annexure 3: Complexity level of various instruments rated for this company

Sr. No.	Name of the Instrument	Complexity Level
1.	Fund-based - LT-Cash Credit	Simple
2.	Non-fund-based - LT/ ST-Bank Guarantees	Simple

**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.

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#### About CARE Ratings:

CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

#### Disclaimer

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