

Press Release

Sheth Construction Company

March 18, 2021



Rating Upgraded

Total Bank Facilities Rated*	Rs.48.00 Cr.
Long Term Rating	ACUITE BBB- / Outlook: Stable (Upgraded from ACUITE BB+)
Short Term Rating	ACUITE A3 (Upgraded from ACUITE A4+)

* Refer Annexure for details

Rating Rationale

Acuité has upgraded the long-term rating to '**ACUITE BBB-**' (**read as ACUITE triple B minus**) from '**ACUITE BB+**' (**read as ACUITE double B plus**) and the short-term rating to '**ACUITE A3**' (**read as ACUITE A three**) from '**ACUITE A4+**' (**read as ACUITE A four plus**) on the Rs.48.00 Cr bank facilities of Sheth Construction Company (SCC). The outlook is '**Stable**'.

The upgrade in the rating reflects the improvement in the profitability margins in FY2020, comfortable financial risk profile marked by comfortable debt protection metrics, adequate liquidity position marked by judicious utilization of the working capital facilities and healthy revenue visibility over the medium term.

The rating is also upgraded since the previous rating downgrade was on account of information risk. However, the client has co-operated and provided the required documents and information.

About the Firm

Mumbai – based, SCC was established in the year 1975. The firm is promoted by Mr. Shashikant Sheth, Mrs. Usha Sheth, Mr. Pankaj Sheth, Mr. Ashish Sheth, Mr. Pratik Sheth, Mr. Miral Sheth and Mr. Abhay Sheth. The firm undertakes civil construction contracts for Municipal Corporation of Greater Mumbai (MCGM) and Surat Municipal Corporation (SMC) for construction of roads, buildings, storm water drainage/sewerage, water supply arrangement, garden development, club/swimming pool construction, pumping station and reservoirs. SCC is registered as a Class IA contractor with MCGM and Class AA contractor with SMC.

Analytical Approach

Acuité has taken a standalone view of the business and financial risk profile of SCC to arrive at the rating.

Key Rating Drivers

Strengths

- **Established track record of operations and experienced management**

SCC has been executing civil construction contracts in Mumbai and Surat for more than four decades. The promoter, Mr. Shashikant Khimchand Sheth, possesses more than three decades of experience in the civil construction industry. Before promoting SCC, the promoter was an Assistant Engineer at Municipal Corporation of Greater Mumbai (MCGM). He was later joined by Mrs. Usha Sheth, Mr. Pankaj Sheth, Mr. Ashish Sheth, Mr. Pratik Sheth, Mr. Miral Sheth and Mr. Abhay Sheth as partners in the firm. The partners' extensive experience is also reflected through the healthy order book position at Rs.274.32 crore as on January 31, 2021 to be executed in next 36 months. Hence, the healthy order book provides modest revenue visibility for the firm over the medium term.

Acuité believes that the partner's extensive experience will help the firm to maintain long-standing relations with its customers such as MCGM and SMC and suppliers and is expected to support its business risk profile over the medium term.

- **Comfortable financial risk profile**

SCC's financial risk profile is comfortable marked by adequate net worth, improving gearing (debt to equity ratio) & total outside liabilities to total net worth (TOL/TNW), and comfortable debt protection metrics. The gearing stood at 1.08 times as on March 31, 2020 as against 1.13 times as on March 31, 2019. TOL/TNW stood at 2.00 times as on March 31, 2020 as against 2.23 times as on March 31, 2019. Tangible net worth of the firm

stood modest at Rs.23.00 crore as on March 31, 2020 as against Rs.21.55 crore as on March 31, 2019. The total debt of Rs.24.85 crore as on March 31, 2020 mainly consists of long-term debt of Rs.0.56 crore, short-term debt of Rs.7.26 crore and unsecured loans stood at Rs.17.04 crore. Debt protection metrics of interest coverage ratio and net cash accruals to total debt stood comfortable at 4.62 times and 0.31 times respectively in FY2020; while DSCR stood at 4.31 times in FY2020. The firm reported cash accruals of Rs.7.59 crore in FY2020 against moderate repayment obligations of Rs.0.10 crore. Further, annual cash accruals are expected to be in the range of about Rs.5.80 crore-Rs.8.32 crore in the medium term against moderate repayment obligations in the range of Rs.0.12 crore-Rs.0.33 crore.

Acuité believes that the financial risk profile of the firm is expected to remain comfortable on account of modest net worth backed by healthy cash accruals vis- à-vis moderate debt repayment obligations and comfortable debt protection metrics.

- **Improvement in margins**

Despite the decline in revenues, the operating margin of the firm has improved and stood at 13.13 percent in FY2020 as against 10.98 percent in FY2019. The profitability margins of the firm has improved and stood at 10.19 percent in FY2020 as against 7.96 percent in FY2019. This is majorly due to increase in employing labours on a contractual basis as and when required for a contract instead of sub-contracting, effective inventory management and decrease in material costs.

Weaknesses

- **Working capital intensive operations**

SCC's working capital operations are intensive marked by Gross Current Asset days (GCA) of 206 days in FY2020 against 204 days in FY2019. This is majorly due to high receivable days. The debtors' days were recorded at 160 days in FY2020 against 175 days in FY2019; high since the firm has booked ~45-50 percent of the revenues in the Q4FY20 and there was slow realization from debtors in the month of March, 2020 because of lockdown imposed due to COVID 19. The inventory days were recorded at 12 days in FY2020 against 2 days in FY2019. Further, the inventory holding policy followed by the firm is generally 15-20 days to cater to spot orders. However, working capital bank lines remains utilized at ~50-70 percent for last trailing 11 months ended February, 2021.

Acuité believes that the working capital operations are expected to remain high with respect to the receivable cycle and which will remain a key rating sensitivity factor.

- **High dependence on government orders, mitigated by established relations and efficient liaison**

SCC does civil construction work mainly for Municipal Corporation of Greater Mumbai (MCGM) and Surat Municipal Corporation (SMC), which indicates that the firm's revenues are highly dependent on number and value of tenders floated by these government authorities. Moreover, any further delays in the project execution of current projects, along with the delayed receipt from the authorities and site-related issues are likely to result in higher working capital requirements. However, this risk is mitigated as SCC has established relations with the respective departments which resulted in timely realizations and winning of tenders at regular intervals.

- **Highly competitive and fragmented industry**

The firm operates in a highly fragmented and competitive civil construction industry with large number of players executing small and mid-sized projects, because of low entry barriers. Further, the contracts are awarded through competitive bidding or tender process leading to pressure on the volume of the work or winning number of projects, pricing and profitability of the firm.

- **Tender based business**

The nature of business is tender based and the firm faces intense competition in the industry. The firm's success ratio of winning the bids is to the tune of 40-50 percent. The firm generates its entire revenue from government projects.

- **Risk of withdrawal associated with partnership nature**

SCC was established as a partnership firm in 1975. Any substantial withdrawal of capital by the partners is likely to have an adverse impact on the capital structure.

Rating Sensitivities

- Growth in revenue with sustainability of the profitability margins.
- Any deterioration of its financial risk profile and liquidity.
- Any elongation of the working capital cycle leading to deterioration in debt protection metrics.

Material Covenants

None

Liquidity: Adequate

SCC has an adequate liquidity position as reflected by adequate net cash accruals against moderate repayment obligations. The firm generated cash accruals of Rs.6.94 crore – Rs.7.59 crore during the last three years through 2018-20 against moderate repayment obligations in the range of Rs.0.10 crore – Rs.0.27 crore. It is expected to generate cash accruals in the range of Rs.5.80 crore – Rs.8.32 crore over the medium term, against moderate repayment obligations in the range of Rs.0.12 crore – Rs.0.33 crore. Unencumbered cash and bank balances stood at Rs.0.12 crore as on March 31, 2020 with a current ratio of 1.85 times in the same period. Liquid investments stood at Rs.10.19 crore as on March 31, 2020. The working capital limits remained utilized at ~50-70 percent for last trailing 11 months ended February, 2021.

Acuité believes that liquidity profile is expected to remain adequate on account of adequate cash accruals against moderate repayment obligations.

Outlook: Stable

Acuité believes that SCC will maintain a 'Stable' outlook over the medium term owing to its experienced management and long track record of operations. The outlook may be revised to 'Positive' if the firm demonstrates substantial and sustained growth in its revenues from the current levels while maintaining its margins. Conversely, the outlook may be revised to 'Negative' in case the firm registers lower than expected growth in revenues and profitability or deterioration in its working capital management or larger-than-expected debt-funded capex leading to deterioration in its financial risk profile and liquidity.

About the Rated Entity - Key Financials

	Unit	FY20 (Actual)	FY19 (Actual)
Operating Income	Rs. Cr.	67.72	79.99
PAT	Rs. Cr.	6.90	6.37
PAT Margin	(%)	10.19	7.96
Total Debt/Tangible Net Worth	Times	1.08	1.13
PBDIT/Interest	Times	4.62	3.91

Status of non-cooperation with previous CRA (if applicable)

Not Applicable

Any other information

Not Applicable

Applicable Criteria

- Default Recognition - <https://www.acuite.in/view-rating-criteria-52.htm>
- Financial Ratios and Adjustments - <https://www.acuite.in/view-rating-criteria-53.htm>
- Entities in Infrastructure Sector - <https://www.acuite.in/view-rating-criteria-51.htm>

Note on complexity levels of the rated instrument

<https://www.acuite.in/view-rating-criteria-55.htm>

Rating History (Upto last three years)

Date	Name of Instrument / Facilities	Term	Amount (Rs. Cr.)	Ratings/Outlook
10-Dec-2020	Cash Credit	Long Term	8.00	ACUITE BB+ (Downgraded; Indicative)
	Bank Guarantee	Short Term	40.00	ACUITE A4+ (Downgraded; Indicative)
26-Sep-2019	Cash Credit	Long Term	8.00	ACUITE BBB-/ Stable (Reaffirmed)

Date	Name of Instrument / Facilities	Term	Amount (Rs. Cr.)	Ratings/Outlook
	Bank Guarantee	Short Term	40.00	ACUITE A3 (Reaffirmed)
26-Aug-2019	Cash Credit	Long Term	6.00	ACUITE BBB- (Indicative)
	Bank Guarantee	Short Term	28.00	ACUITE A3 (Indicative)
	Proposed Bank Guarantee	Short Term	12.00	ACUITE A3 (Indicative)
	Proposed Cash Credit	Long Term	2.00	ACUITE BBB- (Indicative)
	Cash Credit	Long Term	6.00	ACUITE BBB-/ Stable (Assigned)
07-Dec-2018	Proposed Cash Credit	Long Term	2.00	ACUITE BBB-/ Stable (Assigned)
	Bank Guarantee	Short Term	28.00	ACUITE A3 (Assigned)
	Proposed Bank Guarantee	Short Term	12.00	ACUITE A3 (Assigned)
	Cash Credit	Long Term	6.00	ACUITE BBB-/ Stable (Assigned)
05-Jun-2018	Proposed Cash Credit	Long Term	2.00	ACUITE BBB-/ Stable (Assigned)
	Bank Guarantee	Short Term	28.00	ACUITE A3 (Assigned)
	Proposed Bank Guarantee	Short Term	12.00	ACUITE A3 (Assigned)

***Annexure – Details of instruments rated**

Name of the Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Cr.)	Ratings/Outlook
Cash Credit	Not Applicable	Not Applicable	Not Applicable	8.00	ACUITE BBB-/ Stable (Upgraded from ACUITE BB+)
Bank Guarantee*	Not Applicable	Not Applicable	Not Applicable	40.00	ACUITE A3 (Upgraded from ACUITE A4+)

*Sublimit of BGs on behalf of JVs to the extent of Rs.3.50 crore.

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About Acuité Ratings & Research:

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