

## Press Release

### Sheth Construction Company

June 16, 2022



### Rating Downgraded

Product	Quantum (Rs. Cr)	Long Term Rating	Short Term Rating
Bank Loan Ratings	40.00	-	ACUITE A4+   Downgraded
Bank Loan Ratings	8.00	ACUITE BB+   Stable   Downgraded	-
Total Outstanding Quantum (Rs. Cr)	48.00	-	-
Total Withdrawn Quantum (Rs. Cr)	0.00	-	-

### Rating Rationale

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

#### Rationale for rating downgrade

The rating downgrade of SCC takes into account stagnating revenue of the firm and elongation in working capital cycle which has stretched its liquidity profile. The withdrawal of capital by partners also acts as a credit negative for the firm. However, the rating continues to draw comfort from the experience of the partners and the firms average financial risk profile. Any further stretch in working capital cycle or withdrawal of capital by partners will remain a key rating sensitivity.

#### About the Company

SCC established in the year 1975 is a Mumbai based partnership firm that 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. 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. SCC is registered as a Class IA contractor with MCGM and Class AA contractor with SMC.

#### Analytical Approach

Acuite 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 of the firm of Rs.207 crore as on May 31, 2022 to be executed in the 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.

### Average financial risk profile

Financial risk profile of SCC is average marked by low networth, moderately high gearing and average debt protection metrics. The net worth of the firm has declined to Rs.16 Cr as on 31 March, 2022 (Provisional) as against Rs.17 Cr as on 31 March, 2021 on account of capital withdrawal made by the partners during the year. The gearing (debt-equity) has therefore increased to 1.79 times as on 31 March, 2022 (Provisional) as against 1.34 times as on 31 March, 2021. The gearing of the firm is expected to marginally improve over the medium term on account of absence of any debt funded capex plans in the future. The total debt of Rs.29 Cr as on 31 March, 2022 (Provisional) consists of long term bank borrowings of Rs.2 Cr, short term working capital limit of Rs.8 Cr and unsecured loans from partners of Rs.19 Cr.

The interest coverage ratio stood at 6.28 times for FY2022 (Provisional) as against 5.52 times for FY2021. The DSCR stood at 9.67 times for FY2022 (Provisional) as compared to 5.12 times for FY2021. The Net Cash Accruals to Total debt stood at 0.18 times for FY2022 (Provisional) as against 0.26 times for FY2021. The Total outside liabilities to Tangible net worth has increased to 2.97 times for FY2022 (Provisional) as against 2.60 times for FY2021.

Acuité expects SCC's ability to improve its financial risk profile over the medium term will remain a key rating sensitivity factor.

## Weaknesses

### Stagnating revenue albeit stable operating margin

SCC reported revenue of Rs.52 Cr for FY2022 (Provisional) as against Rs.53 Cr in FY2021. The revenue growth remained subdued on account of disruptions caused by Covid 19 related lockdowns. The execution halted entirely during Q1 FY2022, which gradually resumed from Q2 FY2022 onwards. Out of the total unexecuted order book of Rs.207 Cr as on 31<sup>st</sup> May 2022, top five orders contribute ~89 percent and timely completion of work on these orders will remain key to the scale of operations of the firm.

Despite the decline in revenues, the operating margin of the firm have remained stable and stood at 13.14 percent in FY2022 (Provisional) as against 11.12 percent in FY2021, due to an increase in employing labours on a contractual basis as and when required for a contract instead of sub-contracting and further decrease in material costs. On the other hand, the firm reported net profit of Rs.4.66 Cr in FY2022 (Provisional) as against Rs.5.22 Cr in FY2021.

Acuité expects SCC's ability to improve its scale of operations while maintaining profitability over the medium term will remain a key rating sensitivity factor.

### **Elongation in working capital cycle**

SCC's working capital cycle has elongated marked by increase in Gross Current Assets (GCA) of 275 days for FY2022 (Provisional) as against 213 days for FY2021. This is primarily on account of high receivable days which increased to 220 days in FY2022 (Provisional) as against 185 days in FY2021. This is primarily since the firm has booked revenue of ~55 percent in Q4 FY2022. Apart from that, it also consists the amount of retention money which are held in various contracts, of which 50 percent is released immediately after the project completion and remaining 50 percent is released after a period of 3 years. Further, inventory days increased to 25 days in FY2022 (Provisional) as against 6 days. This has increased the firms dependence on external borrowings has increased and the average bank limit utilization for 6 months' period ended April 2022 stood high at ~93 percent. SCC's creditor days stood at 375 days in FY2022 (Provisional) as against 397 days in FY2021.

Acuité believes SCC's ability to improve its working capital cycle 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.

### **Rating Sensitivities**

- Any further withdrawal of capital leading to deterioration in financial risk profile
- Ability to improve scale of operations while maintaining profitability
- Ability to improve working capital cycle

### **Material covenants**

None

### **Liquidity Position - Stretched**

SCC has stretched liquidity position marked by reducing net cash accruals and elongated working capital cycle. The firm generated cash accruals of Rs.8 Cr - Rs.5 Cr during FY2020 to FY2022 (Provisional) against its repayment obligation of Rs.0.10 Cr – Rs.0.53 Cr during the same period. Going forward the NCA are expected in the range of Rs.7 Cr – Rs.9 Cr for period FY2023-FY2024 against repayment obligation of Rs.0.60 Cr – Rs.0.67 Cr for the same period. The working capital operations of the company are highly intensive marked by its gross current asset (GCA) days of 275 days for FY2022 (Provisional) as against 213 days for FY2021 due to an

increase in its overall inventory and debtors cycle during the same period. The average bank limit utilization for 6 months' period ended April 2022 therefore stood higher at ~93 percent. Current ratio stands at 1.97 times as on 31 March 2022 (Provisional). The firm has maintained cash & bank balance of Rs.0.14 crore in FY2022 (Provisional).

Acuité believes that liquidity profile of SCC is likely to remain stretched over the medium term on account of its high dependency on bank borrowings for working capital requirement.

### 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.

### Key Financials

Particulars	Unit	FY 21 (Actual)	FY 20 (Actual)
Operating Income	Rs. Cr.	52.52	67.72
PAT	Rs. Cr.	5.22	6.90
PAT Margin	(%)	9.93	10.19
Total Debt/Tangible Net Worth	Times	1.34	1.08
PBDIT/Interest	Times	5.52	4.62

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

Not applicable

### Any other information

None

### Applicable Criteria

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

### Note on complexity levels of the rated instrument

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

### Rating History

Date	Name of Instruments/Facilities	Term	Amount (Rs. Cr)	Rating/Outlook
18 Mar 2021	Bank Guarantee	Short Term	40.00	ACUITE A3 (Upgraded from ACUITE A4+)
	Cash Credit	Long Term	8.00	ACUITE BBB-   Stable (Upgraded from ACUITE BB+)
10 Dec 2020	Bank Guarantee	Short Term	40.00	ACUITE A4+ (Downgraded and Issuer not co-operating*)
	Cash Credit	Long Term	8.00	ACUITE BB+ (Downgraded and Issuer not co-operating*)
26 Sep 2019	Cash Credit	Long Term	8.00	ACUITE BBB-   Stable (Reaffirmed)
	Bank Guarantee	Short Term	40.00	ACUITE A3 (Reaffirmed)

26 Aug 2019	Bank Guarantee	Short Term	28.00	ACUITE A3 (Issuer not co-operating*)
	Proposed Bank Guarantee	Short Term	12.00	ACUITE A3 (Issuer not co-operating*)
	Cash Credit	Long Term	6.00	ACUITE BBB- (Issuer not co-operating*)
	Proposed Cash Credit	Long Term	2.00	ACUITE BBB- (Issuer not co-operating*)
07 Dec 2018	Cash Credit	Long Term	6.00	ACUITE BBB-   Stable (Assigned)
	Proposed Bank Guarantee	Short Term	12.00	ACUITE A3 (Assigned)
	Proposed Cash Credit	Long Term	2.00	ACUITE BBB-   Stable (Assigned)
	Bank Guarantee	Short Term	28.00	ACUITE A3 (Assigned)
05 Jun 2018	Cash Credit	Long Term	6.00	ACUITE BBB-   Stable (Assigned)
	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

Lender's Name	ISIN	Facilities	Date Of Issuance	Coupon Rate	Maturity Date	Quantum (Rs. Cr.)	Rating
Bank of India	Not Applicable	Bank Guarantee/Letter of Guarantee	Not Applicable	Not Applicable	Not Applicable	34.00	ACUITE A4+   Downgraded ( from ACUITE A3 )
Bank of India	Not Applicable	Cash Credit	Not Applicable	Not Applicable	Not Applicable	8.00	ACUITE BB+   Stable   Downgraded ( from ACUITE BBB- )
Not Applicable	Not Applicable	Proposed Short Term Bank Facility	Not Applicable	Not Applicable	Not Applicable	6.00	ACUITE A4+   Downgraded ( from ACUITE A3 )

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### About Acuité Ratings & Research

Acuité is a full-service Credit Rating Agency registered with the Securities & Exchange Board of India (SEBI). The company received RBI Accreditation as an External Credit Assessment Institution (ECAI) for Bank Loan Ratings under BASEL-II norms in the year 2012. Acuité has assigned ratings to various securities, debt instruments and bank facilities of entities spread across the country and across a wide cross section of industries. It has its Registered and Head Office in Kanjurmarg, Mumbai.

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