

Press Release

SPK And Co

October 18, 2021

Rating Reaffirmed; Outlook Revised



Total Bank Facilities Rated*	Rs. 400.00 Cr.
Long Term Rating	ACUITE BBB+/ Outlook: Positive (Reaffirmed & Outlook revised from Stable)
Short Term Rating	ACUITE A2 (Reaffirmed)

* Refer Annexure for details

Rating Rationale

Acuite has reaffirmed its long term rating of '**ACUITE BBB+**' (read as **ACUITE triple B 'Plus'**) and short term rating of '**ACUITE A2**' (read as **ACUITE A 'two'**) to the Rs.400.00 Cr bank facilities of SPK and Co(SPK). The outlook is revised to '**Positive**' from '**Stable**'.

Revision in Outlook

The revision in outlook reflects the strong liquidity marked by high unencumbered cash and bank balance and liquid investments in form of fixed deposits. Besides, Liquidity is supported by healthy net cash accruals vis-a-vis minimal repayment obligations and no instance of withdrawal of capital by partners in last 5 years. Instead, ~Rs.150 Cr have been infused in FY2020 to strengthen the business. The revision is also supported by consistent performance of its operational metrics over the past 2-3 years.

The reaffirmation in ratings continues to take into account SPK's experienced promoters, established track record and healthy order book position. The rating also factors in its healthy financial risk profile and efficient working capital cycle. These strengths are, however, partially constrained by its significant geographical concentration in revenue profile, inherent risk of susceptibility to tender based operations and risk of withdrawal of partner's capital.

About the Firm

SPK is a Madurai (Tamil Nadu) based partnership firm established in 2010. SPK is promoted by Mr. S. Nagarajan, Mr. S Balasubramani, Mr. S Pathinettampadi Karuppasamy, Mr. S Eswaran and Mrs. S Nagarathinam. SPK undertakes Infrastructure Works, primarily construction and maintenance of roads in Tamil Nadu. It registered as a Class-1 contractor Tamil Nadu State Government department.

Analytical Approach

Acuite has considered the standalone business and financial risk profiles of the SPK to arrive at this rating.

Key Rating Drivers

Strengths

- **Partners' extensive experience in civil construction industry; established track record of operations & healthy order book providing long term revenue visibility**

SPK, registered as a Class-1 EPC contractor with Tamil Nadu State Government department, has established presence in executing projects related to construction and maintenance of road work primarily for Tamil Nadu Road Sector Project (TNRSP) and Tamil Nadu Road Infrastructure Development Corporation (TNRIDC). SPK was established in 2010 by the managing partner, Mr.S.Nagarajan, joint managing partner, Mr.S.Balasubramani and other partners Mr.S.Pathinettampadi Karuppasamy, Mr.S.Eswaran and Mrs.S.Nagarathinam. All the partners have nearly two decades of experience in the civil construction industry and it is closely-held family business. The Partners are well supported by the other professional team. Timely execution of projects helped SPK establish a strong market position. Over the years, the firm has developed the technical capability to be the sole bidder for large engineering, procurement, and construction (EPC) contracts from National Highways Authority of India and state road development agencies. With the partner's extensive industry experience and timely execution of its past projects, SPK has been able to establish long-standing relationship with its key principals. SPK has registered growth in operating income of around 24.29 per cent in FY2021 (provisional) over FY2020. The total operating income has grown at a CAGR of 9 percent over the last 3 years ending FY2021. While the Earnings before Interest,

Depreciation and Tax (EBITDA) margins have remained range bound between 12-15 percent over the same period.

As on March 31, 2021, SPK has an unexecuted order book position of approx. Rs.2,344.17 Cr; estimated to be executed over the next 24-36 months providing long-term revenue visibility. The outstanding order book is ~3x of the FY2021 revenue. Acuite believes that the partner's extensive industry experience, established relation with its principal contractors and healthy order book will aid SPK's business risk profile over the medium term.

• **Tender based nature of operations; funded projects ensuring timely receivables**

SPK executes only tender-based projects funded by central government, state government bodies or international agencies with low reliance on work received as a sub-contract from other civil construction entities. The funded projects either have budgetary support or are funded by a consortium of banks. Once the tender is allotted, Earnest Money Deposit (EMD) of around 0.5-2.00 per cent (varies on basis of department, nature, tenure and size of contract work) is deposited against the BG followed by performance guarantee of 2-10 percent. As per the part of Atmanirbhar Bharat 3.0 package, there is relaxation of Earnest Money Deposit (EMD) and Performance Security on government tenders. The firm raises bills on monthly basis. SPK has the option of availing mobilization advance, but avails limited amount from the same. The retention money is usually maximum 5 per cent of the contract value which is to be released after a defect liability period of 4-5 years; of which 2.5 percent is released against after 2-3 years. Since, the nature of operations is tender based, the business depends on the ability to bid for contracts successfully. SPK has success rate of 80-90 per cent in bidding. In last 11 months ending July 2021, SPK has billed for Rs.774 Cr of work done and demonstrated its ability to collect payment of 95-100 per cent of its work done amounting to Rs.755 Cr from the respective authorities. Acuite expects the operations of the firm to remain efficient on account of timely collection of work billed on monthly basis to its respective authorities.

• **Healthy financial risk profile**

SPK financial risk profile is healthy, marked by a healthy partner's capital, low gearing and improving debt protection metrics. The healthy profitability levels vis-à-vis lower reliance on debt and lower finance cost has led to healthy debt protection metrics. The interest coverage ratio (ICR) and debt service coverage ratio (DSCR) stood at 14.65 times and 10.06 times, respectively in FY2021 (Prov) as against 15.18 and 2.61 times, respectively in the previous year.

The partner's capital stood at Rs.441.11 Cr as on 31 March, 2021 (Prov) as against Rs.39549 Cr as on 31 March, 2020 and Rs.172.37 Cr as on March 31, 2019. This improvement is on the account of healthy accretion to reserves in FY2021 (Prov). The gearing level (debt-equity) has improved and stood at 0.14 times as on 31 March, 2021 (Prov) and the previous year too; the improvement from 0.58 times as on March 31, 2019. TOL/TNW (Total outside liabilities/Total net worth) stands at 0.37 times as on 31 March, 2021 (Prov) against 0.35 times in previous year.

The total debt of Rs.63.66 Cr as on 31 March, 2021 (Prov) consist of long-term debt of Rs.31.95 Cr, Unsecured loans (USL) from directors/promoters of Rs.1.71 Cr, short-term debt of Rs.30.01 Cr. NCA/TD (Net cash accruals to total debt) stood at 1.07 times in FY2021 (Prov) as against 1.11 times in FY2020. Acuite expects the financial risk profile to remain healthy over the medium to long term on account of healthy capital structure and stable operations of the firm.

• **Efficient working capital management**

SPK's working capital operations are efficiently managed as evident from Gross Current Assets (GCA) of 71-82 days during last 3 years historically ended through FY2021 due to prudent inventory management, and efficient collection of trade receivables supported by reputed clientele owing to a healthy realisation cycle. Given that large proportion of orders are either from strong counterparties such as NHAI or ADB/World Bank funded projects, the realisation is timely debtors were 13-35 days during last 3 years March 31, 2021 (Prov). Working capital management is also supported by efficient utilisation of resources and low inventory around 3-26 days during the last 3 years ending through March 31, 2021 (Prov). The firm focuses on the easy mobilisation of its resources, thereby improving the turnaround time and reducing the idleness of machinery and equipment. Furthermore, the firm benefits from the ability to stretch its payables 66-196 days during the last 3 years ended through as on March 31, 2021 (Prov). This results in low reliance on bank lines at below 30 percent over 12 months through May 2021. Acuite believes that SPK's operation continues to be efficiently managed supported by healthy partners' capital, efficient collection mechanism and just in time inventory levels.

Weaknesses

• Exposure to risks related to the tender-driven nature of the business, and customer and geographic concentration in revenue

Revenue is primarily from orders from government agencies with an increased focus of the central government on the infrastructure sector, especially roads and highways; SPK is expected to reap benefits over the medium term. However, most of its projects are tender-based and face intense competition, thus requiring the firm to bid aggressively to get contracts, which restricts the operating margin to a moderate level. Also, given the cyclical nature inherent in the construction industry, the ability to maintain profitability margin through operating efficiency becomes critical. Further, civil construction industry is highly fragmented and intensely competitive, with several players executing small projects. Revenue growth should remain susceptible to the level of investments being made in the civil construction segment in Tamilnadu, and the extent of competition for the tenders. Operations continue to be focused on road projects, which contribute the bulk of the firm's revenue, unlike EPC players with a presence in multiple segments, such as commercial, residential, and industrial construction and infrastructure (irrigation, dams, and power). Acuite believes that the ability of the firm to maintain the scale of operations along with profitability would be the key rating sensitivity factor over the medium term.

• Risk of capital withdrawal

SPK's constitution as a partnership firm is exposed to discrete risks, including the possibility of withdrawal of capital by the partners. Moreover, the partnership nature partially limits the flexibility to raise the funds vis-à-vis a limited firm.

Liquidity Position: Strong

The firm has strong liquidity marked by healthy net cash accruals to its maturing debt obligations and efficient working capital management. SPK generated cash accruals of Rs.54 to 69 Cr during the last 3 years through 2019-21, while its maturing debt obligations were in the range of Rs.6-7 crore during the same period. The cash accruals of the firm are estimated to remain around Rs.70-85 Cr during 2022-24 while their repayment obligations are estimated to be around Rs.6-7 crore during the same period. This will be sufficient to meet the incremental capex and working capital requirements. SPK's working capital operations are efficiently managed as evident from Gross Current Assets (GCA) of 7 -85 days during last 3 years historically ended through FY2021 (Prov) further backed by timely receipt of revenue from government authorities. This results in low reliance on bank lines at below 30 percent over 12 months through May 2021. The firm maintained unencumbered cash and bank balances of Rs.92.30 Cr and further liquid investments of about Rs.150-180 Cr as on 31 March 2021 (Prov). The current ratio stands comfortable at 3.36 times as on 31 March 2021 (Prov). Acuite believes that the liquidity of the firm is likely to remain strong over the medium term on account of healthy cash accruals against its repayment obligations and its internal accruals, and liquid surplus to be sufficient to meet its incremental working capital requirements.

Rating Sensitivities

Negative

- Any further deterioration in working capital cycle and liquidity profile of the firm.
- Any deterioration in Revenue profile and leverage position of the firm.
- Any weakening of financial risk profile of the firm.
- Withdrawal of capital

Outlook: Positive

Acuite believes that SPK will continue to benefit over the medium term due to extensive experience of its promoters, healthy order book, healthy financial risk profile and efficient working capital management. The outlook may be revised to 'Stable', if the firm withdraws capital or is unable to convert partnership firm to private limited company as per specified timelines. Conversely, the outlook may be revised to 'Negative' in case of any sharp decline in its revenues or significant volatility in its profitability or any significant stretch in its working capital management leading to deterioration in the financial risk profile or any large debt-funded capex or further investments made in its group/associate entities.

About the Rated Entity - Key Financials (Standalone)

	Unit	FY21 (Provisional)	FY20 (Actual)
Operating Income	Rs. Cr.	705.77	567.85
PAT	Rs. Cr.	57.54	50.75
PAT Margin	(%)	8.15	8.94
Total Debt/Tangible Net Worth	Times	0.14	0.14
PBDIT/Interest	Times	14.65	15.18

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

None

Any other information

None

Material Covenants

None

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 Services Sector - <https://www.acuite.in/view-rating-criteria-50.htm>
- Infrastructure Entities - <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
18-Aug-2020	Secured Overdraft	Long Term	80.00	ACUITE BBB+/Stable (Assigned)
	Proposed Bank Facility	Long Term	70.00	ACUITE BBB+/Stable (Assigned)
	Bank Guarantee	Short Term	100.00	ACUITE A2 (Assigned)
	Bank Guarantee	Short Term	28.65	ACUITE A2 (Assigned)
	Proposed Bank Facility	Short Term	121.35	ACUITE A2 (Assigned)

*Annexure – Details of instruments rated

Lender's Name	Name of the Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Cr.)	Ratings/Outlook
Tamilnad Mercantile Bank Ltd	Secured Overdraft	Not Applicable	Not Applicable	Not Applicable	80.00	ACUITE BBB+/Positive (Reaffirmed; Outlook revised)
Not Applicable	Proposed Bank Facility	Not Applicable	Not Applicable	Not Applicable	70.00	ACUITE BBB+/Positive (Reaffirmed; Outlook revised)
Tamilnad Mercantile Bank Ltd	Bank Guarantee	Not Applicable	Not Applicable	Not Applicable	100.00	ACUITE A2 (Reaffirmed)

Karur Vysya Bank	Bank Guarantee	Not Applicable	Not Applicable	Not Applicable	28.65	ACUITE A2 (Withdrawn)
Not Applicable	Proposed Bank Facility	Not Applicable	Not Applicable	Not Applicable	150.00	ACUITE A2 (Reaffirmed)

Contacts

Analytical	Rating Desk
<p>Aditya Gupta Vice President – Corporate Ratings Tel: 022-49294041 aditya.gupta@acuite.in</p> <p>Neha Agarwal Assistant Manager – Rating Operations Tel: 040-4004 2327 neha.agarwal@acuite.in</p>	<p>Varsha Bist Senior Manager - Rating Desk Tel: 022-49294011 rating.desk@acuite.in</p>

About Acuité Ratings & Research:

Acuité Ratings & Research Limited is a full-service Credit Rating Agency registered with the Securities and 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. Since then, it has assigned more than 8,850 credit 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.

Disclaimer: An Acuité rating does not constitute an audit of the rated entity and should not be treated as a recommendation or opinion that is intended to substitute for a financial adviser's or investor's independent assessment of whether to buy, sell or hold any security. Acuité ratings are based on the data and information provided by the issuer and obtained from other reliable sources. Although reasonable care has been taken to ensure that the data and information is true, Acuité, in particular, makes no representation or warranty, expressed or implied with respect to the adequacy, accuracy or completeness of the information relied upon. Acuité is not responsible for any errors or omissions and especially states that it has no financial liability whatsoever for any direct, indirect or consequential loss of any kind arising from the use of its ratings. Acuité ratings are subject to a process of surveillance which may lead to a revision in ratings as and when the circumstances so warrant. Please visit our website (www.acuite.in) for the latest information on any instrument rated by Acuité.