

Press Release SPK And Co

January 11, 2023



Rating Reaffirmed

Product	Quantum (Rs. Cr)	Long Term Rating	Short Term Rating
Bank Loan Ratings	150.00	ACUITE BBB+ Positive Reaffirmed	-
Bank Loan Ratings	250.00	-	ACUITE A2 Reaffirmed
Total Outstanding Quantum (Rs. Cr)	400.00	-	-
Total Withdrawn Quantum (Rs. Cr)	0.00	-	-

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 '**Positive**'.

Rationale for the rating

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-I 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 de-growth in operating income of around 29 per cent in FY2022 over FY2021. While the Earnings before Interest Depreciation and Tax (EBITDA) margins have remained range bound between 11.5-15 percent over the past three years. As on March 31, 2022, SPK has an unexecuted order book position of approx. Rs.1869 Cr; estimated to be executed over the next 24-36 months providing long-term revenue visibility. The outstanding order book is ~3.7x of the FY2022 revenue. Acuité 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. Acuité 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 27.28 times and 12.37 times, respectively in FY2022 as against 12.37 and 9.00 times, respectively in the previous year. The partner's capital stood at Rs.450.99 Cr as on 31 March, 2022 as against Rs.427.17 Cr as on 31 March, 2021 and Rs.395.37 Cr as on March 31, 2020. This improvement is on the account of healthy accretion to reserves in FY2022. The gearing level (debt-equity) has improved and stood at 0.12 times as on 31 March, 2022. TOL/TNW (Total outside liabilities/Total net worth) stands at 0.37 times as on 31 March, 2022 against 0.49 times in previous year.

Efficient working capital management

SPK's working capital operations are efficiently managed as evident from Gross Current Assets (GCA) of 85 -121 days during last 3 years historically ended through FY2022 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 28-42 days during last 3 years March 31, 2022. Working capital management is also supported by efficient utilisation of resources and low inventory around 1-26 days during the last 3 years ending through March 31, 2022. 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 31-73 days during the last 3 years ended through as on March 31, 2022. This results in low reliance on bank limits at below 30 percent over 12 months through August 2022. Acuité 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 tenderbased 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 cyclicity 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). Acuité 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 visàvis a limited firm.

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.
- Anyweakening of financial risk profile of the firm. Withdrawal of capital

Material covenants

None

Liquidity: Adequate

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.53 to 60 Cr during the last 3 years through 2020-22, while its maturing debt obligations were in the range of Rs.5-6 crore during the same period. The cash accruals of the firm are estimated to remain around Rs.55-67 Cr during 2023-25 while their repayment obligations are estimated to be around Rs.5-6 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 85-121 days during last 3 years historically ended through FY2022 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 August 2022. The firm maintained unencumbered cash and bank balances of Rs.83.31 Cr as on 31 March 2021 (Prov). The current ratio stands comfortable at 3.42 times as on 31 March 2022. Acuité 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.

Outlook: Positive

Acuité believes that SPK will maintain 'Positive' outlook over the medium term due to extensive experience of its promoters, healthy order book, healthy financial risk profile and efficient working capital management. The rating may be upgraded if the firm registers expected or higher-than expected growth in revenues and profitability. Conversely, 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 and any significant decline in revenue impacting their financial and liquidity profile.

Other Factors affecting Rating

None

Key Financials

Particulars	Unit	FY 22 (Actual)	FY 21 (Actual)
Operating Income	Rs. Cr.	493.17	693.09
PAT	Rs. Cr.	51.31	42.79
PAT Margin	(%)	10.41	6.17
Total Debt/Tangible Net Worth	Times	0.12	0.14
PBDIT/Interest	Times	27.28	12.37

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

None

Any other information

None

Applicable Criteria

- Default Recognition :- <https://www.acuite.in/view-rating-criteria-52.htm>
- Rating Process and Timeline: <https://www.acuite.in/view-rating-criteria-67.htm>
- Infrastructure Sector: <https://www.acuite.in/view-rating-criteria-51.htm>
- Application Of Financial Ratios And Adjustments: <https://www.acuite.in/view-rating-criteria-53.htm>

Note on complexity levels of the rated instrument

In order to inform the investors about complexity of instruments, Acuité has categorized such instruments in three levels: Simple, Complex and Highly Complex. Acuite's categorisation of the instruments across the three categories is based on factors like variability of the returns to the investors, uncertainty in cash flow patterns, number of counterparties and general understanding of the instrument by the market. It has to be understood that complexity is different from credit risk and even an instrument categorized as 'Simple' can carry high levels of risk. For more details, please refer Rating Criteria "Complexity Level Of Financial Instruments" on www.acuite.in

Rating History

Date	Name of Instruments/Facilities	Term	Amount (Rs. Cr)	Rating/Outlook
18 Oct 2021	Proposed Bank Facility	Short Term	150.00	ACUITE A2 (Reaffirmed)
	Proposed Bank Facility	Long Term	70.00	ACUITE BBB+ Positive (Reaffirmed)
	Secured Overdraft	Long Term	80.00	ACUITE BBB+ Positive (Reaffirmed)
	Bank Guarantee	Short Term	28.65	ACUITE A2 (Withdrawn)
	Bank Guarantee	Short Term	100.00	ACUITE A2 (Reaffirmed)
18 Aug 2020	Proposed Bank Facility	Short Term	121.35	ACUITE A2 (Assigned)
	Bank Guarantee	Short Term	100.00	ACUITE A2 (Assigned)
	Proposed Bank Facility	Long Term	70.00	ACUITE BBB+ Stable (Assigned)
	Bank Guarantee	Short Term	28.65	ACUITE A2 (Assigned)
	Secured Overdraft	Long Term	80.00	ACUITE BBB+ Stable (Assigned)

Annexure - Details of instruments rated

Lender's Name	ISIN	Facilities	Date Of Issuance	Coupon Rate	Maturity Date	Complexity Level	Quantum (Rs. Cr.)	Rating
Tamilnad Mercantile Bank Limited	Not Applicable	Bank Guarantee (BLR)	Not Applicable	Not Applicable	Not Applicable	Simple	100.00	ACUITE A2 Reaffirmed
Not Applicable	Not Applicable	Proposed Long Term Bank Facility	Not Applicable	Not Applicable	Not Applicable	Simple	70.00	ACUITE BBB+ Positive Reaffirmed
Not Applicable	Not Applicable	Proposed Short Term Bank Facility	Not Applicable	Not Applicable	Not Applicable	Simple	150.00	ACUITE A2 Reaffirmed
Tamilnad Mercantile Bank Limited	Not Applicable	Secured Overdraft	Not Applicable	Not Applicable	Not Applicable	Simple	80.00	ACUITE BBB+ Positive Reaffirmed

Contacts

Analytical	Rating Desk
Gnanreddy Rakesh Reddy Analyst-Rating Operations Tel: 022-49294065 rakesh.reddy@acuited.in	Varsha Bist Senior Manager-Rating Operations Tel: 022-49294011 rating.desk@acuited.in

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.

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. Ratings assigned by Acuité 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. Ratings assigned by Acuité 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.acuited.in) for the latest information on any instrument rated by Acuité.