Rating Rationale 15 Sept 2020

RKEC Projects Limited

Brickwork Ratings reaffirms the long term rating and upgrades the short term rating for the bank loan facilities of Rs. 300.00 Crore of RKEC Projects Limited

Particulars

Facilities	Amount (Rs. Crs)		Tenure	Ratings*	
	Previous	Present		Previous (07 Nov 2019)	Present
Fund Based Cash credit (CC) Demand Loan (Covid Emergency Credit Line) Proposed CC	50.00 - 25.00	**37.50** **3.75** **48.75**	Long Term	BWR BBB/Stable	**BWR BBB/Stable Reaffirmed**
Non Fund Based Bank Guarantee (BG) ILC/FLC (BG Sublimit) Proposed BG	150.00 (50.00) 75.00	**210.00** **(50.00)** **-**	Short Term	BWR A3+	**BWR A2 Upgraded**
Total	**300.00**	**300.00**	**Rupees Three Hundred Crores Only**		

*Please refer to BWR website www.brickworkratings.com/ for definition of the ratings; Details of Bank facilities are provided in Annexure I

Ratings Action/Outlook

The reaffirmation of the long term rating and upgradation of the short term rating factor the improved operational performance during FY20, medium-term revenue visibility through a healthy order book position and moderate financial risk profile. Brickwork Ratings (BWR) continues to factor in the extensive experience of the promoters of RKEC Projects Limited (RPL or the company) in the Engineering, Procurement and Construction (EPC) contract industry, established operational track record and demonstrated execution capabilities, long standing relationships with reputed clientele and promoters' resourcefulness to support business operations. However, the ratings are constrained by the moderate scale of operations, company's dependence on government contracts and geographically, sectorally and client-wise concentrated nature of unexecuted orders. Project execution risk, uncertainty inherent in the tender-based contract execution business, the vulnerability of profitability to margin-based competitive bidding and fluctuation in construction material prices and the working-capital-intensive nature of business operations continue to be rating constraints. As clients are mainly government bodies and public-sector entities, any delay in the release of payments and retention money withheld by clients can impact the company's cash flows.

BWR takes note of the potential impact of the Covid-19 pandemic on the business and financial profiles of RPL during FY21. With the commencement of the nationwide lockdown due to the current Covid-19 pandemic 24 March 2020 onwards, there has been a moderation in construction activities. Post the part-relaxation of the lockdown 21 April 2020 onwards, the company has resumed construction activities at its sites. Currently, operations are at 85-90% capacity and are expected to gradually reach targeted operational levels. Nevertheless, the timely scale-up of operations, steady progress across projects and efficient management of the company's working capital position remain key monitorables. The impairment of debtors is not expected, considering the reputation of clientele. No orders/tenders were reported to have been cancelled due to Covid and the company received orders worth ~Rs. 273 cr during Apr-Aug 2020. Revenue and profitability are expected to be impacted in FY21, given the lost workdays in Q1FY21 due to the lockdown and uncertain business environment owing to Covid-19. However, the government's push for infrastructure development through the implementation of the National Infrastructure Pipeline and liquidity support by the RBI are seen as positives for the industry. BWR takes into account the possible delay in project execution by 1-2 months on average due to the Covid-19-induced lockdown and will continue to monitor the impact of the pandemic on the company's credit profile.

Brickwork Ratings (BWR) takes cognizance of the Covid-19 regulatory package and related guidelines issued by the Reserve Bank of India (RBI). BWR also takes note of the guidance provided by the SEBI vide its Circular dated 30 March 2020 in this regard. BWR notes that RPL availed relief under the aforementioned package for the period March-August 2020, including Covid Emergency Line of Credit, and deferred scheduled payments for the period in line with the RBI guidelines. However, the entire portion of deferred principal/interest was paid off during the month of Aug 2020. BWR will continue to monitor the developments in the case of any prolonged impact of Covid 19 and analyse the impact, if any, on RPL's credit profile.

BWR believes RPL's business risk profile will be maintained over the medium term. The outlook may be revised to Positive if a sustained increase in the scale of operations, along with improved margins, a further improvement in the capital structure, an improved segment/geography/client-wise diversification and the timely realisation of receivables results in an improved working capital management. The outlook may be revised to Negative in case the company is unable to complete the projects without time and cost overruns, especially in view of the Covid-19 disruptions. Further, any deterioration in the capital structure due to debt-financed capital expenditure and/or crystallisation of contingent liabilities/delay or non realisation of receivables resulting in high utilisation of working capital funding, thus weakening the company's financial risk profile may exert a downward pressure on the ratings.

Key Rating Drivers

Credit Strengths:

- **Experienced management and established track record:** The main promoters of RPL, a closely held family business, have over 3 decades of experience in the EPC business. RPL, with an established operational track record of around fifteen years, is an enlisted contractor with the Ministry of Defence as 'Super Special Class' civil contractor for Military Engineering Services [MES], 'S-02' contractor for Director General Navy Projects [DGNP] to undertake Civil engineering works, Electrical engineering works and Miscellaneous contracts, 'Civil category CIV-IV class' for Defence Research Development

Organisation [DRDO]. RPL is also registered as 'Special Class - Civil' contractor for R&B Department, Government of Andhra Pradesh and 'Super Class' civil contractor for Public Works Department, Government of Odisha. RPL is certified for ISO 9001:2015 [Quality Management], ISO 14001:2015 [Environmental Management] and OHSAS 18001:2007 [Occupational Health and Safety Management]. The company has expertise in the construction of marine structures, bridges & flyovers, highways, buildings, survey works under unmanned aerial systems etc. Thus, the company has demonstrated its project execution capability in the sector and has been able to win repeat orders from various government agencies based on its track record.

- **Established clientele:** RPL has diverse and reputed clientele including Military Engineering Services, Director General Navy Projects, Defence Research Development Organisation; National Highways Authority of India, Indian Railways, Rashtriya Ispat Nigam Limited, etc., and various ports like Jawaharlal Nehru Port Trust [JNPT], Cochin Port Trust [CoPT], Mumbai Port Trust [MbPT], Adani Port and Special Economic Zone Limited, Vedanta Limited, Public Works Department, Government of Odisha, R&B Department, Government of Andhra Pradesh. The company has been associated with these clients for a long time, and the successful execution of the projects has also helped it in getting repeat orders. Due to reputed client profiles, the company has low counterparty credit risk although at times, there can be delays in the realisation of some bills.
- **Revenue visibility through healthy order book:** The company had orders worth ~Rs. 923 Cr as on 31 Aug 2020, to be completed within the next 2-3 years. During Apr-Aug 2020 period, the company received orders worth ~Rs. 273 cr, of which, work orders for ~Rs. 143 cr are awaited.
- **Moderate financial risk profile - Standalone :** Contract receipts increased from Rs. 243.99 Cr in FY19 to Rs. 297.93 Cr in FY20. Operating profit increased from Rs. 45.46 Cr to Rs. 71.31 Cr and net profit from Rs. 24.13 Cr to Rs. 27.86 Cr over the same period. The net and operating profit margins for FY20 were comfortable at 9.35% and 23.93%, respectively, compared with 9.89% and 18.63% for FY19, respectively. The earlier projected revenue and profitability for FY20 were not achieved as the company could not raise bills for some of the completed works due to the Covid-19-induced lockdown. Total debt increased from Rs. 49.57 Cr as on 31 March 2019 to Rs. 69.57 Cr as on 31 March 2020, primarily due to an increase in short term borrowings. Tangible net worth (TNW) increased from Rs. 95.96 Cr as on 31 March 2019 to Rs. 118.02 Cr as on 31 March 2020 due to the accretion of net profit. The gearing continued to be comfortable marked by the D/E ratio of 0.55 times and TOL/TNW of 1.61 times as on 31 March 2020. ISCR and DSCR were adequate at 4.64 times and 2.96 times, respectively, as on 31 March 2020.

Credit Challenges:

- **Geographical, segmental and customer concentration:** The order book continues to be strong, but concentrated both geographically, sectorally and client-wise. West Bengal alone accounts for ~65% (FY20 - 57%) of the overall unexecuted orders. This makes a substantial portion of the company's operations vulnerable to social, political, economic and environmental changes in the state. In terms of sectors, marine structures orders accounted for ~50% (FY20 - 35%) of the unexecuted order book. The top five projects constitute ~80% of the total unexecuted order book, of which ~30% is from NHAI. This exposes the company to customer concentration risk. However, almost all the orders are from government bodies/reputed private players, which minimises counterparty risk.

- **Working-capital-intensive nature of operations:** The company's operations are working-capital-intensive, as marked by almost full utilisation of the sanctioned working capital facilities of ~Rs. 37.50 Cr. This is mainly due to the high cost of construction material, high labour cost, advance to suppliers and delays in getting payments from government departments, among others. Although, the company has been able to lower the days receivables from 123 days as on 31 March 2019 to 81 days as on 31 March 2020, the days inventory increased to 103 days and the days payables contracted to 113 days as on 31 March 2020, against 57 days and 185 days respectively as on 31 March 2019, thereby stretching the working capital cycle to 71 days as on 31 March 2020. However the company has sufficient financial flexibility to increase the working capital limits, if required.
- **Execution risks:** The company's operations are susceptible to many external factors such as timely clearances from various regulatory bodies, the handover of sites, the mobilisation of funds, the change in governments policies and directives, cost escalation due to departmental delays, labour unrest and climatic vagaries. The effect of any of these could be substantial on the company's timeline of the completion of projects, working capital utilisation level and overall profitability. The onset of Covid-19 has added an unprecedented execution risk for EPC contractors in general and the company in particular. The company has been able to check the shortage of labourers to a large extent during the lockdown by providing for their food, shelter and other essential needs. However, the lockdown led to the loss of man-days of work, which will eventually lead to a delay in project execution and billing and a probable cost escalation. Although most of the company's contracts have a provision for Force Majeure and cost escalation due to unforeseen circumstances, approvals from various departments may take some time.
- **Susceptibility of profitability to volatility in raw material prices:** The company has limited control over the prices of raw materials such as cement and steel used by it during the project execution. The current contracts of the company are a mix of fixed price and those with a price escalation provision. In the case of the fixed-price contracts, the company has to bear the cost escalation of raw materials, which affects its profitability. In the current scenario of the complete breakdown of the supply chain due to the Covid-19-induced lockdown, the company may have to face supply constraints and elevated raw material prices for some time.
- **Industry competition:** Although the company has a long track record of over three decades, it is exposed to competition and is susceptible to risks inherent in tender-based business. Since all of the operations are tender-based, the business depends on the ability to bid for tenders successfully. Additionally, the majority of the orders are from government agencies, resulting in high dependence on timely clearances for tenders and payments. Revenue and profitability are expected to remain susceptible to risks inherent in tender-based operations and a competitive landscape.

Analytical Approach and Applicable Rating Criteria
RKEC Projects Limited has entered into Joint Venture agreements under the name 'RKEC and Suryadevara JV', 'RKEC and CQEC JV', M/s RKEC-RANSS JV and M/s RKEC NG BHOIR and Samudra JV. The jointly controlled entity (AOP) M/s. RKEC and Suryadevara JV was formed for execution of railway work which participated jointly by the company and AOP. During FY 19 the company has formed a jointly controlled entity (AOP) M/s RKEC and CQEC JV for execution of NHAI work which is participated jointly by the company and JV. Further during FY20, the Company has formed two new jointly controlled entity (AOP) M/s RKEC-RANSS JV for execution of Tirupati Smart City Corporation Limited work and M/s RKEC NG BHOIR and Samudra JV for execution of Dredging work at JNPT. The consolidated financials of RPL comprise revenues of RPL and the four Joint Ventures. While assigning the ratings, BWR has adopted a standalone approach as the contract receipts are almost fully reflected in the standalone financials only. BWR has applied its rating methodology as detailed in the Rating Criteria detailed below (hyperlinks provided at the end of this rationale).

Rating Sensitivities
The ability of the company to ensure satisfactory and timely execution of the ongoing projects within estimated costs, achieve geographical/segment/client diversification, enhance its scale of operations, improve its profitability margins, strengthen its credit risk profile, ensure effective and timely realization of receivables and manage its working capital efficiently would remain the key rating sensitivities. RPL has outstanding contingent liabilities amounting to Rs. 154.88 Cr as on 31 Mar 2020 which includes an amount of Rs. 125.01 Cr on account of collateral for bank guarantees and capital cost of machinery imported and an amount of Rs. 29.88 Cr on account of sales tax/entry tax/service tax/labour cess/income tax and legal cases filed against the company. Trade receivables of Rs. 106.53 Cr as on 31 Mar 2020, includes an amount of Rs. 69.10 Cr on account of suspended/delayed contracts. Any crystallization of the above contingent liabilities, recovery of receivables and the impact of the same on the financial risk profile of the company would be the key rating sensitivity factors.

Positive:
- An improvement in the scale of operations and profitability on a sustained basis with the timely completion and delivery of projects
- Geographical, sectoral and client-wise diversification of operations
- Specific credit metrics that could lead to an upgrade include TOL/TNW less than 1.50 times on a sustained basis.

Negative
- Delays in the execution of ongoing orders, a reduction in fresh order inflows or a stretch in the receivables cycle of the company, especially in view of any prolonged impact of Covid-19.
- Deterioration in financial risk profile on account of stretch in working capital cycle or any large, debt-funded capital expenditure
- Material impact on the financial risk profile due to any crystallization of contingent liabilities or non realization of receivables

Liquidity Position - Stretched : RPL's utilization of fund based working capital facilities of Rs. 37.50 Cr is above 95% over the last 12 months, reflecting the working capital intensity of operations. EBITDA for FY20 (~Rs. 67 Cr) comfortably covers the interest and finance charges of FY18-20 (~Rs. 25 Cr). Net cash accrual at ~Rs. 28 Cr for FY20 is adequate for long term debt repayments of ~Rs. 4 Cr for FY21. Cash & cash equivalents are at ~Rs. 3 Cr as on 31 Mar 2020. Cash conversion cycle is 71 days as on 31 Mar 2020 mainly due to high Days Inventory on account of pandemic outbreak. Current Ratio is adequate at 1.34 times as on 31 Mar 2020. The Company has availed the Covid-19 related RBI Moratorium Package for the rated bank loan facilities including Covid Emergency Line of Credit, as a prudent measure to preserve/ build-up liquidity. However, the entire portion of deferred principal/interest was paid off during the month of Aug 2020.

About the company :

RKEC Projects Limited, an NSE listed company, was incorporated in April 2005 as a private limited company, at Visakhapatnam, Andhra Pradesh. Subsequently, in 2016, the company was converted into a public limited company and listed on NSE in 2017. RPL is an enlisted contractor with the Ministry of Defence as 'Super Special Class' civil contractor for Military Engineering Services [MES], 'S-02' contractor for Director General Navy Projects [DGNP] to undertake Civil engineering works, Electrical engineering works and Miscellaneous contracts, 'Civil category CIV-IV class' for Defence Research Development Organisation [DRDO]. It is also registered as 'Special Class - Civil' contractor for R&B Department, Government of Andhra Pradesh and 'Super Class' civil contractor for Public Works Department, Government of Odisha.

Shri. G Radhakrishna is the Chairman & Managing Director. Smt. G Parvathi Devi, Shri. G Venkata Ram Mohan, Smt. G Sita Ratnam, Shri. Lucas Peter, Vice Admiral Satish Soni [Retd.] and Brig. J K Rao are the other directors.

Key Financial Indicators - Standalone

Key Parameters	Units	31 Mar 2019	31 Mar 2020
Result Type		**Audited**	**Audited**
Operating Revenue	Rs. Cr	243.99	297.93
EBITDA	Rs. Cr	45.46	71.31
Profit After Tax	Rs. Cr	24.13	27.86
Tangible Net Worth	Rs. Cr	95.96	118.02
Total Debt/Tangible Net Worth	Times	0.52	0.55
Current Ratio	Times	1.49	1.34

On a provisional basis, the company has achieved a standalone revenue of ~Rs. 53 Cr for the period Apr-Aug 2020.

Key Financial Indicators - Consolidated

Key Parameters	Units	31 Mar 2019	31 Mar 2020
Result Type		Audited	Audited
Operating Revenue	Rs. Cr	225.77	303.98
EBITDA	Rs. Cr	43.66	65.05
Profit After Tax	Rs. Cr	22.43	25.81
Tangible Net Worth	Rs. Cr	94.25	114.27
Total Debt/Tangible Net Worth	Times	0.53	0.57
Current Ratio	Times	1.40	1.30

Key Covenants of the facility rated: The terms of sanction include standard covenants normally stipulated for such facilities.

Status of non-cooperation with previous CRA – Not Applicable

Rating History for the last three years [including withdrawal and suspended]

<table>
<tr><th rowspan="2">Sl. No.</th><th rowspan="2">Facilities</th><th colspan="3">Current Rating (Sep 2020)</th><th colspan="3">Rating History</th></tr>
<tr><th>Type</th><th>Amount (Rs. Cr)</th><th>Rating</th><th>07 Nov 2019[3]</th><th>2018</th><th>2017</th></tr>
<tr><td>1</td><td>Cash Credit</td><td rowspan="3">Long Term</td><td>37.50</td><td rowspan="3">BWR BBB/ Stable</td><td rowspan="3">BWR BBB/ Stable</td><td rowspan="5"><u>20 Feb 2018[1]</u>
BWR BBB-/ Stable/A3
<u>03 Sep 2018[2]</u>
BWR BBB/ Stable/A3+</td><td rowspan="5">-</td></tr>
<tr><td>2</td><td>Demand Loan (Covid ECL)</td><td>3.75</td></tr>
<tr><td>3</td><td>Proposed CC</td><td>48.75</td></tr>
<tr><td>4</td><td>Bank Guarantee</td><td rowspan="2">Short Term</td><td>210.00</td><td rowspan="2">BWR A2</td><td rowspan="2">BWR A3+</td></tr>
<tr><td>5</td><td>ILC/FLC (BG Sublimit)</td><td>(50.00)</td></tr>
<tr><td colspan="3">Total</td><td>300.00</td><td colspan="4">Rupees Three Hundred Crores Only</td></tr>
</table>

[1]*Rated amount: Rs. 135.00 Cr;* [2]*Rated amount: Rs. 200.00 Cr;* [3]*Rated amount: Rs. 300.00 Cr*

Complexity Levels of the Instruments:
For more information, visit www.brickworkratings.com/download/ComplexityLevels.pdf

Hyperlink/Reference to applicable Criteria

General Criteria
Infrastructure Sector
Approach to Financial Ratios
Short Term Debt

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RKEC Projects Limited

ANNEXURE I : Details of Bank Facilities rated by BWR

Sl. No.	Name of the Bank	Type of Facilities	Long Term (Rs. Cr)	Short Term (Rs. Cr)	Total (Rs. Cr)
1	**Bank of Baroda [erstwhile Vijaya Bank]**	Cash Credit	37.50	-	37.50
		Demand Loan (Covid Emergency Credit Line)	3.75	-	3.75
		Proposed Cash Credit	48.75	-	48.75
		Bank Guarantee	-	210.00	210.00
		ILC/FLC (Sublimit of BG)	-	(50.00)	(50.00)
TOTAL - Rupees Three HundredCrores Only					**300.00**

Note: Besides the above mentioned facilities, the company has equipment/vehicle loans of Rs. 8.12 Cr (as on 31 March 2020) with various banks/NBFCs, which are not rated by BWR.

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