January 06, 2023

KCC Buildcon Private Limited: Ratings reaffirmed; outlook revised to Positive

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Cash Credit	300.00	300.00	[ICRA]A(Positive) reaffirmed; Outlook revised to Positive from Stable
Short-term – Non-fund based Bank Guarantee	1500.00	1500.00	[ICRA]A2+ reaffirmed
Total	**1800.00**	**1800.00**	

**Instrument details are provided in Annexure-I*

Rationale

The outlook revision on the long-term rating to Positive reflects ICRA's expectation that KCC Buildcon Private Limited's (KCC) credit profile is expected to improve over the near to medium term, in the backdrop of healthy ramp-up in execution as well as likely monetisation of its five hybrid-annuity mode (HAM) projects. ICRA notes that KCC has signed a definitive agreement with Cube Highways and Infrastructure V Pte. Ltd (Cube Highways) for divestment of its equity stake in five under-construction HAM special purpose vehicles (SPVs), the proceeds from which will be deployed towards deleveraging its balance sheet as well as equity investments in future HAM projects. The ratings continue to favourably factor in the healthy growth in its scale of operations, driven by ramp-up in the pace of execution and robust outstanding order book position comprising primarily road projects from the National Highways Authority of India [NHAI, rated [ICRA]AAA(Stable)] under engineering, procurement and construction (EPC) and HAM model, resulting in low counterparty credit risk. KCC has reported an operating income (OI) of Rs. 2,530 crore in FY2022, indicating a strong compounded annual growth rate (CAGR) of ~40% during FY2017-FY2022. It reported an OI of ~Rs. 1,443 crore in H1 FY2023 (against Rs. 1,020 crore in H1 FY2022) and its revenue is expected to grow by ~30% in FY2023. Further, the operating profitability remained healthy in the range of 13-14.5% over the past five years. The ratings are supported by its sizeable order book position of ~Rs. 7,388 crore as on September 30, 2022, which is ~2.9 times of the OI in FY2022, providing medium-term revenue visibility. The ratings draw comfort from the company's healthy financial risk profile with a comfortable capital structure. This apart, the ratings derive strength from KCC's execution track record and extensive experience of its promoters in the construction sector.

The ratings are, however, constrained by the execution risk associated with construction contracts, as ~60% of the orders are in the early stages of execution (less than 20% progress), along with its exposure to HAM projects, which will require sizeable investments from KCC. This apart, sizeable debt repayments, and additional working capital requirement with increase in scale of operations will lead to high dependence on external borrowings over the medium term. However, it is expected to be mitigated by the abovementioned asset monetisation plan, which will unlock the capital over the medium term. The ratings note the stiff competition in the construction sector, which could put pressure on the new order inflows and the company's exposure to sizeable contingent liabilities in the form of bank guarantees, mainly for contractual performance, mobilisation advance and retention money. Nonetheless, ICRA draws comfort from its execution track record and absence of invocation of guarantees in the past. ICRA notes that there is a recent litigation against the company/KCC's senior management. Any material adverse outcome of the same could have a bearing on its operations and remains a key rating monitorable.

KCC has undertaken multiple build-operate-transfer (BOT) road projects, which are housed under SPVs. It has two BOT-annuity road projects and seven HAM-based road projects. Three of these projects (two BOT annuity projects from Madhya Pradesh Road Development Corporation Limited (MPRDC) and one HAM project from the Ministry of Road Transport and Highways (MoRTH)) are operational, while the remaining six HAM projects are under implementation, awarded by NHAI. KCC has extended corporate guarantee (CG) for the full debt tenure for the two BOT annuity projects (debt outstanding of Rs. 93.75 crore, as on October 31, 2022) and two under implementation HAM Projects until receipt of one/two semi-annuities. ICRA has fully consolidated the two operational annuity project SPVs (for which CG has been extended for full tenure) and has done limited consolidation for the remaining SPVs.

The Positive outlook on the long-term rating reflects ICRA's opinion that KCC's financial risk profile will improve significantly from the divestment of its equity stake in five SPVs, which besides reducing the committed promoter contribution towards under-construction projects, will unlock the capital infused post achievement of commercial operation date (COD) in these projects. This apart, ICRA expects KCC's favourable operational track record in the road construction segment, its reputed clientele and healthy order book position to support improvement in its credit profile over the medium term.

Key rating drivers and their description

Credit strengths

Sizeable order book position with reputed client profile – KCC has a sizeable order book position of ~Rs. 7,388 crore as on September 30, 2022, which is ~2.9 times of the OI in FY2022 and ~2.1 times of the projected OI in FY2023 providing healthy medium-term revenue visibility. The current order book comprises mainly road construction orders from the NHAI, which is a reputed counterparty.

Healthy scale of operations and comfortable financial risk profile – KCC's healthy order book position and ramp-up in execution pace resulted in a strong revenue growth of ~52% in FY2022, at a CAGR of ~40% during FY2017–FY2022. It reported an OI of ~Rs. 1,443 crore in H1 FY2023 (against Rs. 1,020 crore in H1 FY2022, and Rs. 2,530 crore in FY2022) and the revenue is expected to grow by ~30% in FY2023. The company has been able to sustain its operating margins in the range of 13-14.5% over the past five years. While KCC's interest coverage remained comfortable at 4.7 times in FY2022 (4.8 times in FY2021) and its Total Debt/TNW improved to 0.57 times as on March 31, 2022 (from 0.77 times as on March 31, 2021), its TOL/TNW has remained moderate at 1.7 times as on March 31, 2022 (compared to 1.7 times as on March 31, 2021). KCC's financial profile is supported by additional cushion available from the definitive agreement signed with Cube Highways for divestment of its equity stake in five under-construction HAM SPVs. The total equity requirement in these five projects is estimated at Rs. 620 crore, of which 40% could be infused by Cube Highways (at KCC's discretion) in under-construction stage with initial infusion of 60% by KCC and approvals from the NHAI and respective lenders. Subsequently, Cube Highways will take over these projects six months post achievement of COD in phases as per provision of Concession Agreement. Going forward, with increased scale of operations, healthy profitability, lower dependence on external debt, its financial risk profile is anticipated to remain comfortable.

Healthy track record in construction industry – Over the years, KCC has demonstrated a consistent track record of project execution and has built resources including plant, equipment and manpower. It has a team of qualified and technical personnel, who have been associated with the company for many years. The experience of KCC's promoters and team, along with its established track record of operations, supports its operational risk profile.

Credit challenges

Exposure towards HAM projects, and associated investment commitments – With six under-construction HAM projects, the company is exposed to the project implementation risks including sizeable equity commitment required over the next two to three years. The appointed dates have been declared for five projects while is awaited for one of the projects The total equity requirement towards these six HAM projects is estimated at around Rs. 700 crore to be infused during FY2022-FY2025, of which ~43% has been infused by KCC till November 30, 2022. The company plans to meet the remaining portion of investments from the cash flows from operations and expected fund inflows from its tie-up with Cube Highways for five HAM projects.

Execution risk associated with construction contracts and concentrated order book – Like any construction company, KCC remains exposed to the execution risk as ~45% of order book as on September 30, 2022 are yet to be started and further around 15% of the order book is in the nascent stages of execution (less than 20%). The company's order book is vulnerable to segment concentration (all orders in road segment).

Competitive nature of industry and sizeable non-fund based exposure – KCC is exposed to the inherent cyclicality in the construction industry and intense competition in the tender-based contract award system, resulting in volatility in new order inflows, revenues and pressure on margins. It is vulnerable to sizeable contingent liabilities in the form of bank guarantees (~Rs. 1,176 crore as on March 31, 2022), mainly towards performance guarantee, mobilisation advance and retention money.

Liquidity position: Adequate

The cash flow from operations are expected to be adequate to meet the debt servicing obligations of around Rs. 100.7 crore in FY2023 and Rs. 77.4 crore in FY2024. KCC has Rs. 79.9 crore of unencumbered fixed deposits, cash balances as on March 31, 2022. Further, there was a cushion available to the extent of Rs. 110 crore in the unutilised fund-based working capital bank limits as on September 30, 2022. KCC has ~Rs. 240 crore and ~Rs. 282 crore of equity commitments towards the under-construction HAM projects in FY2023 and FY2024, respectively. This is likely to be supported by healthy cash flow from operations and expected fund inflows from tie-up with Cube Highways for five HAM projects.

Rating sensitivities

Positive factors – The ratings could be upgraded if there is a sustained growth in scale of operations, while maintaining healthy order book position and operating profitability, and if the scheduled/planned monetisation of assets leads to significant reduction in leverage resulting in improvement in credit metrics and liquidity position. Specific credit metrics that could lead to a rating upgrade includes consolidated[1] TOL/TNW below 1.2 times on a sustained basis.

Negative factors – The outlook may be revised back to stable if there is inadequate progress on asset monetisation plans. Negative pressure on the ratings could arise if significant delays in project execution leads to sizeable decline in scale and profitability. Higher-than-expected funding commitment towards BOT/HAM projects, or any considerable debt-funded capital expenditure, or a significant increase in working capital intensity resulting in deterioration in its liquidity position, could put pressure on the ratings. Specific credit metrics that could lead to a rating downgrade includes consolidated TOL/TNW increasing over 1.75 times on a consistent basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Construction Entities Rating Approach - Consolidation
Parent/Group Support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has consolidated financials of KCC with its subsidiaries (Refer Annexure II). ICRA has fully consolidated the SPVs where KCC has extended corporate guarantee for the full tenure of the debt. For other SPVs, ICRA has undertaken limited consolidation factoring in the expected funding requirements (equity/ cost over-run support/ operational shortfall).

[1] *Consolidation of KCC and its SPVs where debt is fully guaranteed, i.e., KCC Lateri Expressway Pvt Ltd, and KCC Roads Construction Pvt Ltd.*

About the company

KCC Buildcon Private Limited (KCC) originally started its business as a partnership firm named Kundu Construction Company in 1999. In 2009, Kundu Construction Company was converted into a private limited company as KCC Buildcon Private Limited.

KCC is involved in the execution of road/ highway projects, bridges and other civil construction works at various locations across India.

Key financial indicators (audited)

KCC	FY2021	FY2022
Operating income	1662.7	2589.9
PAT	94.5	162.0
OPBDIT/OI	14.2%	13.0%
PAT/OI	5.7%	6.3%
Total outside liabilities/Tangible net worth (times)	1.72	1.68
Total debt*/OPBDIT (times)	1.51	1.06
Interest coverage (times)	4.8	4.7

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore

Source: Company data; ICRA research

**Total debt Includes lease liabilities*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2023)				Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding as on Mar 31, 2022 (Rs. crore)	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021	Date & rating in FY2020
					Jan 06, 2023	Dec 15, 2021		
1	**Fund-based – CC**	Long term	300.00	-	**[ICRA]A(Positive)**	**[ICRA]A(Stable)**		
2	**Non-fund based - BG**	Short term	1500.00	--	**[ICRA]A2+**	**[ICRA]A2+**		

&= Under Watch with Developing Implications

Complexity level of the rated instruments

Instrument	Complexity Indicator
Fund-based facilities	Simple
Non-fund based facilities	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Fund-based Cash Credit	NA	NA	NA	300.00	[ICRA]A(Positive)
NA	Non-fund based – Bank Guarantee	NA	NA	NA	1500.00	[ICRA]A2+

Source: Company

Please click here to view details of lender-wise facilities rated by ICRA

Annexure II: List of entities considered for consolidated analysis

Company Name	KCC Ownership	Consolidation Approach
KCC Roads Construction Private Limited	100%	Full Consolidation
KCC Lateri Expressway Private Limited	100%	Full Consolidation
KCC Talgaon Kalmath Highways Private Limited	100%	Limited Consolidation
KCC Dhangaon Boregaon Expressway Pvt Ltd	100%	Limited Consolidation
KCC Chittoor Highways Private Limited	100%	Limited Consolidation
KCC Dak Package I Expressway Private Limited	100%	Limited Consolidation
KCC Walajahpet Expressway Private Limited	100%	Limited Consolidation
KCC Katra Expressway Private Limited	100%	Limited Consolidation
KCC Bethamangala Expressway Private Limited	100%	Limited Consolidation

Source: KCC annual report

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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