

March 15, 2024

Cherian Varkey Construction Company Private Limited: Ratings downgraded and outlook revised to Negative

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term – Fund-based CC	84.0	84.0	[ICRA]BBB+ (Negative); Rating downgraded from [ICRA]A- (Stable) and outlook revised to Negative from Stable
Long-term/Short-term – Non-fund based – Bank guarantee	200.0	200.0	[ICRA]BBB+ (Negative) / [ICRA] A2; Rating downgraded from [ICRA]A- (Stable) / [ICRA]A2+ and outlook revised to Negative from Stable
Total	284.0	284.0	

*Instrument details are provided in Annexure-I

Rationale

The ratings downgrade and revision in outlook to Negative for Cherian Varkey Construction Company Private Limited (CVCC) factor in its weakened coverage metrics owing to steady decline in operating margins as well as deterioration in working capital cycle, thereby necessitating increased bank borrowings and hence higher interest expenses. CVCC's working capital cycle has deteriorated owing to delay in realisation of payments from departments of the Kerala Government, resulting in built-up in receivable as well as inventory days. The increased working capital requirement is funded by bank borrowings, leading to interest cover of 3.2 times and 1.9 times in FY2023 and 9M FY2024, respectively, as compared to over 5 times prior to FY2022. The coverage metrics are likely to remain muted, with interest cover expected to remain below 3 times in the medium term. ICRA notes that the company's scale of operation remains modest with revenues of Rs. 251.3 crore in FY2023, which is substantially lower than the pre-pandemic levels (Rs. 409 crore in FY2019). Decline in scale of operations and consequent impact on fixed cost absorption resulted in a steady decrease in operating margins to 10.1% in FY2023 from 14.9% in FY2019. The company has billed Rs. 159 crore in 9M FY2024 and the revenues are estimated to be above Rs. 250 crore in FY2024. The ratings are constrained by high project and geographical concentration risks with top five projects contributing to 78% of the outstanding order book, and all orders remaining confined to Kerala, as on September 30, 2023.

The ratings, however, favourably factor in CVCC's healthy order book position of Rs. 969.2 crore as on September 30, 2023, providing medium-term revenue visibility. The ratings consider the established operational track record of CVCC in executing projects in roads, bridges and building segments. The building segment accounts for 58% of the order book, with roads and bridges segment constituting the remaining share. CVCC has unencumbered cash balance of Rs. 101 crore as on December 31, 2023, which provides support to its liquidity position and credit profile. The ratings note the stiff competition in the construction sector, which could put pressure on 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.

The Negative outlook reflects ICRA's opinion that CVCC's operating performance is likely to remain under pressure in the near to medium term, given the delay in securing requisite approvals and payment realisation. Going forward, the company's ability to materially improve its working capital cycle and coverage metrics remains important from the credit perspective.

Key rating drivers and their description

Credit strengths

Established operational track record in civil construction industry – CVCC has expertise in the execution of roads, bridges, and building segments. Although it has presence in RMC supply and housing projects construction, the civil construction segment contributed to more than 90% of CVCC's revenues over the past five years. The company has an adequate employee base and own fleet of machinery supporting its project execution.

Heathy order book position – CVCC has an order book of Rs. 969.5 crore as on September 30, 2023, which translates to 5.1 times of FY2023 revenues providing healthy medium-term revenue visibility. However, timely receipt of approvals and payments from the authorities remains critical for revenue growth.

Credit challenges

Modest scale of operations – CVCC has modest scale of operations with revenues of Rs. 254.1 crore in FY2023, which significantly declined from above Rs. 400 crore levels in FY2019 owing to slow order execution. The company has billed Rs. 159 crore in 9M FY2024 and the revenues are estimated to be above Rs. 250 crore in FY2024.

Deterioration in financial risk profile amid high working capital intensity – The company's profitability fell to 10.1% in FY2023 from above 15% levels during the pre-Covid period. Further, the interest coverage declined to 3.2 times and 1.9 times in FY2023 and 9M FY2024 from above 5 times during the pre-Covid period owing to an increase in interest expenses. Given the increased working capital intensity, the working capital limit utilisation is expected to remain high, with resultantly higher interest expenses. Consequently, the interest coverage ratio is likely to remain below 3 times in the medium term. Going forward, company's ability to materially improve its working capital cycle and coverage metrics remains important from the credit perspective.

Modest order book profile – Although CVCC's order book remained healthy at Rs. 969.9 crore as on September 30, 2023, ~59% of the order book remains in the nascent stages and is yet to commence the first billing. Any delay in receipt of requisite approvals could adversely impact the revenues and profitability as witnessed during the past two years. Also, the order book is largely from state government departments exposing the billings to funding availability with these departments and constraining its liquidity position. CVCC's operations are restricted to Kerala, resulting in high geographical concentration risk. It faces high project concentration risk with top five projects accounting for 78% of the order book as on September 30, 2023. Any delay in execution or payment receipts from these projects can affect its revenues and liquidity position as witnessed over the past two years.

Liquidity position: Adequate

The company's liquidity position is adequate, supported by free cash balances of Rs. 101 crore as on December 31, 2023. The average utilisation of fund-based facilities remained high at 76% in the past 14 months ending January 2024. Given the absence of any major capex plans and low repayment obligations, CVCC's liquidity position is likely to remain adequate over the near term.

Rating sensitivities

Positive factors – The outlook could be revised to Stable if there is a material improvement in liquidity position, supported by reduction in the cash conversion cycle.

Negative factors – Pressure on the ratings could arise if the company is unable to improve revenues and/or earnings. Inability to improve the working capital cycle, thus affecting the liquidity position, could put pressure on the ratings.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Construction
Parent/Group support	Not applicable
Consolidation/Standalone	Standalone

About the company

Cherian Varkey Construction Company Private Limited (CVCC) is a Kochi-based construction contractor. It was established in 1975 as a proprietorship concern by Mr. Cherian Varkey. Reconstituted in 2000 as a private limited company, CVCC undertakes contracts primarily in the infrastructure segment for construction of roads, bridges, metro projects, etc, and buildings for private players. Its major clients include government departments in Kerala such as Kerala PWD, Kerala State Construction Corporation and private players. Apart from its contracts division, it has a ready-mix concrete manufacturing division, and a housing division that undertakes small-scale real estate projects. CVCC is closely held by the family of the company's founder, Mr. Cherian Varkey.

Key financial indicators (audited)

CVCC	FY2022	FY2023
Operating income	245.2	254.1
PAT	13.7	15.2
OPBDIT/OI	12.9%	10.1%
PAT/OI	5.6%	6.0%
Total outside liabilities/Tangible net worth (times)	0.9	0.9
Total debt/OPBDIT (times)	2.7	4.4
Interest coverage (times)	5.2	3.2

Source: Company, ICRA Research; All ratios as per ICRA's calculations; Amount in Rs. crore

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

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument		Current rating (FY2024)			Chronology of rating history for the past 3 years			
		Type	Amount rated (Rs. crore)	Amount outstanding as on March 31, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021
					Mar 15, 2024	Jan 30, 2023	Oct 29,2021	Jul 31,2020
1	Cash credit	Long term	84.0	84.0	[ICRA]BBB+ (Negative)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)
2	Bank guarantee	Long term and short term	200.0	200.0	[ICRA]BBB+ (Negative) / [ICRA] A2	[ICRA]A- (Stable)/[ICRA] A2+	[ICRA]A- (Stable)/[ICRA] A2+	[ICRA]A- (Stable)/ [ICRA]A2+

3	Unallocated	Long term and short term	0.0	0.0	-	-	[ICRA]A-(Stable)/[ICRA]A2 +	-
---	-------------	--------------------------	-----	-----	---	---	-----------------------------	---

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term – Fund-based CC	Simple
Long-term/Short-term – Non-fund based – Bank guarantee	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 facilities	NA	NA	NA	84.0	[ICRA]BBB+ (Negative)
NA	Non-fund based facilities	NA	NA	NA	200.0	[ICRA]BBB+ (Negative) / [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: Not Applicable

ANALYST CONTACTS

Rajeshwar Burla
+91 40 6939 6443
rajeshwar.burla@icraindia.com

Vinay Kumar G
+91 40 6939 6424
vinay.g@icraindia.com

Ashish Modani
+91 22 6114 3414
ashish.modani@icraindia.com

Doddapanani Srisai Bhavya
+91 40 6939 6421
doddapanani.bhavya@icraindia.com

RELATIONSHIP CONTACT

L. Shivakumar
+91 22 6114 3406
shivakumar@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)
info@icraindia.com

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.

For more information, visit www.icra.in

ICRA Limited



Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001
Tel: +91 11 23357940-45



Branches



© Copyright, 2024 ICRA Limited. All Rights Reserved.

Contents may be used freely with due acknowledgement to ICRA.

ICRA ratings should not be treated as recommendation to buy, sell or hold the rated debt instruments. ICRA ratings are subject to a process of surveillance, which may lead to revision in ratings. An ICRA rating is a symbolic indicator of ICRA's current opinion on the relative capability of the issuer concerned to timely service debts and obligations, with reference to the instrument rated. Please visit our website www.icra.in or contact any ICRA office for the latest information on ICRA ratings outstanding. All information contained herein has been obtained by ICRA from sources believed by it to be accurate and reliable, including the rated issuer. ICRA however has not conducted any audit of the rated issuer or of the information provided by it. While reasonable care has been taken to ensure that the information herein is true, such information is provided 'as is' without any warranty of any kind, and ICRA in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness or completeness of any such information. Also, ICRA or any of its group companies may have provided services other than rating to the issuer rated. All information contained herein must be construed solely as statements of opinion, and ICRA shall not be liable for any losses incurred by users from any use of this publication or its contents.