

October 26, 2020

Afcons Infrastructure Limited: Long-term rating downgraded to [ICRA]A+ and short-term rating downgraded to [ICRA]A1; rating continues to remain on negative outlook

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-Convertible Debenture Programme	300	300	[ICRA]A+(Negative); downgraded from [ICRA]AA-(Negative)
Fund based - Term Loan	1,200	1,200	[ICRA]A+(Negative); downgraded from [ICRA]AA-(Negative)
Fund based - Cash Credit (long-term)	1,400	1,400	[ICRA]A+(Negative); downgraded from [ICRA]AA-(Negative)
Non-fund based - BG/LC (long-term)	13,250	13,250	[ICRA]A+(Negative); downgraded from [ICRA]AA-(Negative)
Fund based – Short term loans	712	712	[ICRA]A1; Downgraded from [ICRA]A1+
Non-fund based - BG/LC (short-term)	1,238	1,238	[ICRA]A1; Downgraded from [ICRA]A1+
Commercial Paper	900	900	[ICRA]A1; Downgraded from [ICRA]A1+
Total	19,000	19,000	

*Instrument details are provided in Annexure-1

Rationale

The downgrade of Afcons Infrastructure Limited's (AIL) ratings reflect the overall deterioration of the credit profile of Shapoorji Pallonji Group and increase in the linkages between AIL and its parent company - Shapoorji Pallonji and Company Private Limited (SPCPL)¹. AIL has awarded certain sub-contract works related to station work in metro projects to SPCPL considering their long track record in building construction. In these orders, AIL has extended mobilisation advances² to SPCPL. This is in addition to the regular dividend payouts and SPCPL's borrowing against pledge of shares of AIL in the past. The rating also factors in the increase in total indebtedness of AIL owing to increase in work in progress due to contractual variations and elongation in receivable cycle for few clients. The same has got funded through mobilization advances and stretching its payables, resulting in increase in total outside liabilities to tangible net-worth ratio (TOL/TNW)³ from 4.05x as on March 31, 2019 to 4.69x as on March 31, 2020. The interest coverage also remains moderate at 2.28 times as on March 31, 2020. Nevertheless, during H1 FY2021, the company realised long-pending receivables from some of the projects resulting in improved cash flow position and was also able to square-off certain outside liabilities towards sub-contractors. Notwithstanding the contingencies built-in, fixed price contracts with SP Group companies (9% of AIL order book)

¹ Ratings of SPCPL have been revised to [ICRA]BBB+ and has been put on watch with negative implications via press release dated October 5, 2020 ([link to rationale](#))

² As per disclosure made in related party transactions schedule in FY2020 annual report; mobilisation advance extended to SPCPL stood at 20% of the sub-contract value

³ Ratio adjusted for arbitration receivables realized against submission of bank guarantees which the company has classified as 'advances from customers' pending final settlement of the claim

exposes AIL's profitability to any sharp movement in input costs and also likely elongation of receivable cycle from these projects. The increasing focus on executing overseas projects also exposes the company to exchange rate and geo-political risks. Going forward, any material deterioration in the working capital cycle and/or instances of financial support extended to group companies will be key rating sensitivities.

ICRA has taken note of a recent encashment of bank guarantee by one of AIL's clients in Q2FY2021, a bank guarantee of Rs. 25.8 crore was encashed by one of AIL's clients for a completed project whereas a court stay has been brought by AIL on invocation of another bank guarantee of Rs. 117.5 crore. AIL has also received an unfavourable arbitration outcome for an ongoing project which has been challenged by the company. AIL has substantial quantum of receivables/ unbilled revenues due from these clients. Delay in resolution and/or adverse outcome in the aforesaid projects would impact AIL's liquidity and credit profile. ICRA will continue to monitor developments on this front.

The rating, however, favourably factors in AIL's well established presence in the infrastructure segment, its presence in diversified segments, proven track record of sound project execution and engineering skills. AIL's consistent focus on quality construction and timely delivery has resulted in acquiring diverse and reputed clientele across segments and geographies, which is an indication of its strong execution capabilities. The ratings also take comfort from the healthy order book position of ~Rs. 27,183 crore as on June 30, 2020 (2.7x FY2020 revenues) which provides strong revenue visibility in the near to medium term. The rating also derives strength from AIL's adequate liquidity position with sufficient unencumbered cash balances and sizeable undrawn bank limits.

Key rating drivers

Credit strengths

- **Strong execution capabilities** – AIL has a well-established track record in the infrastructure segment and has strong engineering skills in executing complex infrastructure projects across diverse segments. The company's strong and reputed clientele across segments and geographies alleviates counter-party credit risk. The ratings also derive strength from the expertise of its managerial and technical personnel heading the key business verticals.
- **Healthy order book position** – AIL's order book stood at ~Rs. 27,183 crore as on June 30, 2020 translating into 2.7 times the revenues of FY2020 providing strong revenue visibility in the near to medium term. The order book is well diversified across segments – surface transport (rail, road and bridges - accounting for 35% of order book as on June 30, 2020), metro (22%), tunnelling and hydro projects (19%), marine and industrial (16%), and oil and gas (8%). Further, the order book is geographically well diversified and spread across eleven states accounting for 68% of order book and eleven countries accounting for 32% of the order book.
- **High financial flexibility** – AIL derives strong financial flexibility from its sufficient unencumbered cash balances and sizeable undrawn bank limits.

Credit challenges

- **Weakening credit profile of promoter group:** The financial risk profile of Shapoorji Pallonji group continued to weaken, which coupled with increased linkages between AIL and SPCPL has raised credit concerns for the former. In addition to the regular dividend payouts and SPCPL's borrowing against pledge of shares of AIL in the

past, AIL has now extended mobilisation advances to SPCPL as it has sub-contracted part of the metro works (related to station buildings) to SPCPL.

- **Increase in total indebtedness** – Due to significant increase in AIL’s work in progress on account of contractual variations, high amount of arbitration receivables yet to be realised and elongation of receivable cycle for few clients, which are funded through mobilization advances and stretching its payables, has resulted in an increase in total outside liabilities to tangible net-worth ratio. While ~25% of AIL’s total receivables as on March 2020 are arbitration receivables which are awarded and yet to be realised, ~34% of unbilled revenue is towards contractual variations. AIL’s TOL/TNW has increased from 4.05x as on March 31, 2019 to 4.69x as on March 31, 2020. The interest coverage also remains moderate at 2.28 times as on March 31, 2020. During H1 FY2021, the company realised long-pending receivables from some of the projects resulting in improved cash flow position and was also able to square-off certain outside liabilities towards sub-contractors. Going forward, any material deterioration in the working capital cycle thereby adversely affecting AIL’s liquidity profile and will be a key rating sensitivity.
- **Contracts from SP Group on fixed-price basis and likely elongation in receivables** - Orders aggregating to Rs. 2,423 crore accounting for ~9% of AIL’s order book as on June 30, 2020 are received from SP Group, of which 74% are on fixed-price basis exposing it to cost over-run risks. The ability of the company to execute the project within the budgeted costs would remain important in order to maintain its profitability. Furthermore, the receivables from SP Group are likely to get elongated on account of group’s overall tight liquidity position.

Liquidity Position: Adequate

AIL’s liquidity profile is remains adequate with liquid cash & bank balance of ~Rs. 400 crore as on September 30, 2020. The average fund based utilisation for past twelve months stood at 63% and the unutilized limits stood at Rs. 742 crore as on September 30, 2020. AIL has debt repayment obligations of Rs. 51 crore falling due in H2FY2021 which can be comfortably met through cashflow from operations.

Rating sensitivities

Positive triggers – The crystallisation of scenarios for rating upgrade is unlikely over the medium term. The outlook may be revised to ‘Stable’ if there is significant growth in revenue, improvement in profitability along with improvement in the working capital intensity especially through realisation of stuck money in variations, thereby resulting in reduction in overall outside liabilities.

Negative triggers – Downward pressure on the rating could emerge if the cash accruals are lower than expected or delay in resolution of disputed receivables and/or elongation in receivable cycle adversely impacts the liquidity position of AIL. The rating may also get impacted if there is further weakening of the financial profile of its parent – Shapoorji Pallonji and Company Private Limited and/or any form of additional financial support extended to SP Group (including significantly higher than anticipated dividend payouts).

Analytical approach:

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Construction Entities
Parent/Group Support	NA
Consolidation / Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of AIL. As on March 31, 2020, the company had 12 subsidiaries that are enlisted in Annexure-2.

About the company:

Afcons Infrastructure Limited (AIL), incorporated in 1976 as Asia Foundations and Constructions Limited, is a reputed construction company and is part of the Shapoorji Pallonji (SP) Group. The SP Group holds the majority stake of 97.42% in AIL as on September 2018. The company operates in several segments such as marine works (including construction of jetties and dry docks), offshore oil and gas, bridges and flyovers, road construction, hydro and tunnelling, pipe laying and general civil engineering works. AIL commenced operations as a civil construction firm in 1959 and was initially involved in the construction of specialized foundation activities, such as pile foundations, diaphragm walls, geotechnical investigations, drilling and grouting. AIL entered the marine segment in 1963 and subsequently undertook design and build contracts. Over the years, AIL has also increased its presence geographically and has executed projects across all major Indian states in addition to overseas projects in Madagascar, Oman, the UAE, Qatar, Yemen, Mauritius, Bahrain, Algeria, Jordan, Liberia, Kuwait, Bangladesh, Kazakhstan, Gabon and executing projects in Bangladesh, UAE, Kuwait, Ghana, Tanzania, Zambia, Guinea, Mozambique, Mauritius and Mauritania.

Key financial indicators (Consolidated, Audited)

	FY2019	FY2020
Operating Income (Rs. crore)	8736	10004
PAT (Rs. crore)	234	248
OPBDIT/OI (%)	8.21%	8.91%
PAT/OI (%)	2.68%	2.48%
Total Outside Liabilities/Tangible Net Worth (times)	4.21	4.87
Total Debt/OPBDITA (times)	2.28	1.87
Interest Coverage (times)	2.52	2.28

Source: Company, ICRA research

*FY2019: 4.05; FY2020: 4.69 - adjusted for arbitration receivables realized against submission of bank guarantees which the company has classified as 'advances from customers' pending final settlement of the claim

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Rating (FY2021)				Rating History for the past 3 years				
		Type	Amount Rated	Amount O/s	Current rating 26-Oct-20	FY2020		FY2019		FY2018
						28-Feb-2020	08-Jul-2019	24-Jan-2019	04-Jan-2019	08-Jan-2018
1	NCD	Long Term	-	-		-	-	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
2	NCD	Long Term	300	200	[ICRA]A+ (Negative)	[ICRA]AA- (Negative)	[ICRA]AA&	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
3	Term Loan	Long Term	1200	474	[ICRA]A+ (Negative)	[ICRA]AA- (Negative)	[ICRA]AA&	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
4	Cash Credit	Long Term	1,400	-	[ICRA]A+ (Negative)	[ICRA]AA- (Negative)	[ICRA]AA&	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
5	Non-fund based (BG/LC)	Long Term	13,250	-	[ICRA]A+ (Negative)	[ICRA]AA- (Negative)	[ICRA]AA&	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
6	Short term loans	Short Term	712	-	[ICRA]A1	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
7	Non-fund based (BG/LC)	Short Term	1,238	-	[ICRA]A1	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
8	CP	Short Term	900	-	[ICRA]A1	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

&: Rating under watch with developing implications

Complexity level of the rated instrument:

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument Details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount	
					Rated (Rs. crore)	Current Rating and Outlook
INE101I08065	NCD	06-Sep-16	8.60%	06-Sep-21	100	[ICRA]A+ (Negative)
INE101I08073	NCD	23-Feb-17	8.65%	23-Feb-22	100	[ICRA]A+ (Negative)
-	NCD	Yet to be placed	-	-	100	[ICRA]A+ (Negative)
NA	CP	-	-	7 to 365 days	900	[ICRA]A1
NA	Term Loan 1	Jun-15	9.60%	Apr-22	150	[ICRA]A+ (Negative)
NA	Term Loan 2	Feb-17	9.40%	Mar-24	200	[ICRA]A+ (Negative)
NA	Term Loan 3	Mar-14	3.41%	Mar-21	35	[ICRA]A+ (Negative)
NA	Term Loan 4	Mar-19	9.30%	Mar-26	240	[ICRA]A+ (Negative)
NA	Term Loan 5	Jun-19	9.30%	Jun-26	50	[ICRA]A+ (Negative)
NA	Term Loan 6	-	-	-	50	[ICRA]A+ (Negative)
NA	Proposed Term Loan	-	-	-	475	[ICRA]A+ (Negative)
NA	Cash Credit	-	-	-	1,400	[ICRA]A+ (Negative)
NA	Short Term Loan	-	-	-	712	[ICRA]A1
NA	Non-fund based BG/LC	-	-	-	13,250	[ICRA]A+ (Negative)
NA	Non-fund based BG/LC	-	-	-	1,238	[ICRA]A1

Source: Company

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Hazarat and Company Private Limited	100%	Full consolidation
Afcons Corrosion Protection Private Limited	100%	Full consolidation
Afcons Hydrocarbons Engineering Private Limited	100%	Full consolidation
Afcons (Mideast) Constructions and Investments Private Limited	100%	Full consolidation
Afcons Infrastructures Kuwait for Building, Road and Marine Contracting WLL	49%	Full consolidation
Afcons Construction Mideast LLC	49%	Full consolidation
Afcons Gulf International Projects Services FZE	100%	Full consolidation
Afcons Mauritius Infrastructure Limited	100%	Full consolidation
Afcons Overseas Singapore Pte Limited	100%	Full consolidation
Afcons Infra Projects Kazakhstan LLP (Step Down Subsidiary)	100%	Full consolidation
Afcons Saudi Constructions LLC	100%	Full consolidation
Afcons Overseas Project Gabon SARL (Step Down Subsidiary)	100%	Full consolidation

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