



B.G. Shirke Construction Technology Private Limited

Analyst Contacts

Samridhi Chowdhary
SAMRIDHI.CHOWDHARY@ICRAINDIA.COM
 +91-22-3047 0041

Shubham Jain
SHUBHAMJ@ICRAINDIA.COM
 +91-124-4545 306

Rohit Inamdar
ROHIT.INAMDAR@ICRAINDIA.COM
 +91-124-4545 847

Relationship Contacts

L. Shivakumar
SHIVAKUMAR@ICRAINDIA.COM
 +91-22-3047 0005

Website
www.icra.in

Rating

ICRA has retained the grading assigned to B.G. Shirke Construction Technology Private Limited (BGS) at CR2+ grade indicating strong contract execution capacity. The prospects of timely completion of projects without cost overruns and the ability to pay liquidated damages for non-conformance are high but not as high as in CR1.

This grading indicates the relative contract execution capacity with respect to contracts with values of up to Rs. 1000 crore¹ (increased from Rs. 500 crore) and aggregate value of works to be executed within a year of up to Rs. 2000 crore (increased from Rs. 1400 crore), with a permissible variation of +/- 10%.

Key Financial Indicators

	2008-09	2009-10	2010-11
OI	1,049.34	1,148.63	1,258.50
OPBDIT	155.67	180.05	212.66
PAT	53.73	67.12	95.20
Net Cash Accruals	76.43	86.45	110.15
Tangible Net worth	122.43	176.34	256.83
Total Debt	254.79	298.86	336.99
OPBDIT/OI	14.84%	15.67%	16.90%
PAT/OI	5.12%	5.84%	7.56%
PBIT/Average (TD+TNW+DTL)	34.27%	37.94%	38.19%
Gearing (times)	2.08	1.69	1.31
Gearing excluding mobilisation advance	3.70	3.20	2.50
OPBDIT/Interest (times)	3.01	2.90	3.51
NCA/Total Debt	30.00%	28.93%	32.69%
Total Debt/OPBDITA	164%	166%	158%
Debtor Days	40	33	39
Inventory Days	113	123	174

Note: Amounts in Rs. Crore, OI: Operating Income; OPBDIT: Operating Profit before Depreciation, Interest and Tax; PAT: Profit after Tax; PBIT: Profit before Interest and Tax; DTL: Deferred Tax Liability; GCF: Gross Cash Flows; NWC: Net Working Capital

¹ 100 lakh = 1 crore = 10 million

Business & Background

B.G. Shirke Construction Technology Private Limited (BGS) was established in 1955 as a partnership firm by the name of B.G. Shirke & Company. While building construction is its main line of business, BGS is also engaged in the manufacture of structural components and capital equipment such as manufacturing and erection of transmission towers and manufacturing of post harvest equipment. The company's manufacturing facility is located in Pune, Maharashtra. Traditionally, major operations of the company have been in the State of Maharashtra but the company has entered into the States of Karnataka, Andhra Pradesh and Delhi and ventured into construction of roads and highways sectors as well. The existing clients of BGS include Maharashtra Housing & Area Development Authority (MHADA), City & Industrial Development Corporation of Maharashtra Limited (CIDCO), Delhi Development Authority (DDA), Maharashtra State Road Development Corporation Limited (MSRDC) and Karnataka Public Works Department (KPWD).

In the twelve month period ending March 2011 the company reported a profit after tax (PAT) of Rs. 95.20 crore on an operating income of Rs. 1258.50 crore as compared to PAT of Rs. 67.12 crore on an operating income of Rs. 1148.63 crore in the corresponding period last year.

Operating Performance

Long track record in the construction industry: BGS has an established track record in the construction business with an experience spanning over more than five decades. The company is mainly engaged in building construction and has undertaken various projects involving the use of prefabricated construction technology. Within the building construction segment, the company has executed residential, commercial and industrial projects in addition to projects such as airports and sports complexes.

Strong relationship with MHADA: BGS has a high success ratio in tenders invited by the Maharashtra Housing and Area Development Authority (MHADA). In order to encourage the use of non-conventional construction technology, the Government of Maharashtra (GoM) has created a new category of construction companies, which employ such technologies, and has mandated organisations like MHADA and City & Industrial Development Corporation of Maharashtra Limited (CIDCO) to award a certain amount of construction work to companies registered under this category. BGS enjoys the first-mover advantage, as it is currently the only construction company to qualify under this category and has been awarded certain contracts directly by MHADA and CIDCO. The main strength of the company is the demonstrated ability to execute large building projects expeditiously through the use of prefabricated construction technology. BGS also draws strength from its backward integration into the manufacture of prefabricated structures. Going forward, BGS is likely to face increasing competition with respect to MHADA projects, given that other builders are also setting up pre-fabricated manufacturing facilities. Nevertheless, BGS has a long track record of successful implementation of projects awarded by MHADA, which is expected to enable it to maintain a healthy bid success ratio in the pre-fabricated construction segment.

Pre-fabricated construction technology allows for faster execution and healthy profitability: BGS has used pre-fabricated construction technology for constructing buildings, especially under the mass-housing scheme. This technology is based on the construction of the building structure by using pre-cast beams and columns and construction of floor and walls by using Siporex slabs and blocks. The pre-fabricated construction technology allows for faster execution and cost savings beyond a particular scale. The company's first-mover advantage and demonstrated ability to execute sizeable projects using pre-fabricated construction technology has led to steady improvement in its profitability. Moreover, the expertise in pre fabricated technology has facilitated the association with MHADA leading to healthy order volumes.

Adequate in house resource capabilities to execute lump sum turnkey contracts: BGS has the capability to execute work on a turnkey basis. The company derives significant benefit from its ability to produce building materials and structural components in house. These include Siporex blocks, pre-fabricated steel doors, window panes and window frames. In-house manufacturing of the major raw materials reduces dependence on the external players and improves the profitability. The group has developed a proprietary building material called Siporex, which has given BGS a competitive edge in low-income housing projects of the Maharashtra Government. This material has enabled the company to employ precast and formwork techniques for mass construction competitively.

Healthy order book giving visibility to sales in the short to medium term

Figure 1: Order book movement



The order book of the civil construction projects has shown a steady growth over the last four years. BGS had an unexecuted order-book of Rs. 3,619 crore as on March 31, 2011, valued at 2.85X construction segment turnover. In the first half of the current fiscal, there has been a further addition of Rs. 648 crore of orders. The unexecuted order-book as on September 30, 2011 was about Rs. 3,628 crore, largely stable at the last year levels. The Order Book/Turnover ratio has been in the range of 2.0 – 2.8X over the last four years. The management has typically been in favor of maintaining a low Order Book/Turnover ratio as it believes in limited order book backlog. The current order book is at a 2.9X FY2011 construction turnover operating income which though not significantly high, but indicates some execution challenges for the company. The order book of the company is fairly concentrated with top 5 projects forming 49% of the order book and top 10 projects forming 74% of the order book. This is on account of a few large orders in the order book. This increases the revenue concentration risk for the company. Some of the major projects currently being executed by the company are:

SI No.	Client	Order Value (Rs. Crore)	Scope of Work
1	Delhi Development Authority (DDA),	915.0	18600 EWS houses at three locations in Delhi, namely Rohini, Narela and Dwarka
2	Andhra Pradesh Rajiv Swagruha Corporation Limited (APRSCL)	447.5	6216 Flats Integrated Thematic Township at Jawaharnagar, Shameerpet Andhra Pradesh
3	MHADA, Vikhroli	309.8	Redevelopment of Transit Camp by constructing Transit ,EWS & MIG
4	MHADA, Malwani	301.7	Mass Housing project
5	MHADA, Tungwa - Powai	271.6	Traning Center, EWS, MIG & HIG Tenements
6	P.W.P.&IW.T . Department Belgaum	265.5	Suvarna Soudha (administrative building) at Belgaum
7	and Army Welfare Housing Organization (AWHO), Delhi	253.5	Residential project
8	DB Realty, Chandivali	242.3	SRA buildings of orchid Hills
9	Pimpri Chinchwad Municipal Corporation (PCMC), Bigadi	200.8	City slum rehabilitation project comprising of 4880 tenements at Nigadi
10	MHADA, Sion	174.1	Transit settlement, LIG, MIG and HIG tenements

Gradual diversification in order-book position traditionally dominated by MHADA and CIDCO: BGS enjoys a strong and loyal client base, with a long association with most of its client having executed repeat orders. The notable among these are MHADA, CIDCO, PCMC and Wipro Ltd. The company's association with MHADA and CIDCO dated back to over three decades. While MHADA continues to remain the largest client for BGS, the company has been able to expand its client base with addition of clients like DDA, APRSCL, PCMC, KPWD Suvarna Saudha, and AWHO. Consequently, the share of MHADA and CIDCO in the total order book of the company has reduced from a level of about 50% as of March 31, 2008 to about 36% as of September, 2011. There has not been any instance of guarantees being revoked in the past reflecting adequacy of construction in these projects. Majority of contracts are item rate contracts covered under escalation clauses where cost overruns are mitigated to a large extent.

Sectoral concentration continues: Being a civil contractor, BGS is engaged in the construction of residential, commercial, industrial, airport terminal structures as well as roads & bridges. However, overall, construction of residential projects continues to remain the mainstay of the company. As on September 2011, the unexecuted

order-book (including projects in pipeline) for residential projects stood at Rs. 3434 crore vis-vis total order-book of Rs. 3662 crore (94% attributed to residential projects). The key characteristic is that these projects mainly pertain to construction of tenements for EWS section rather than construction of high end residential projects. This stems from company's long association with public sector entities like MHADA, CIDCO, PCMC. This insulates the company from the downturn in the real estate sector to an extent.

Figure 2: Sectoral distribution of order-book - June 2010

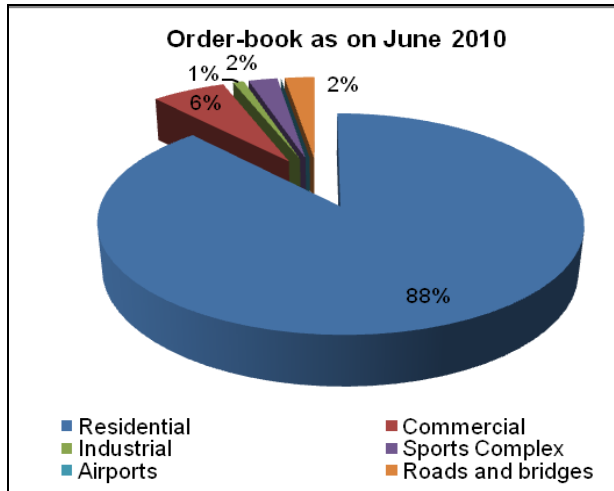


Figure 3: Sectoral distribution of order-book – September 2011

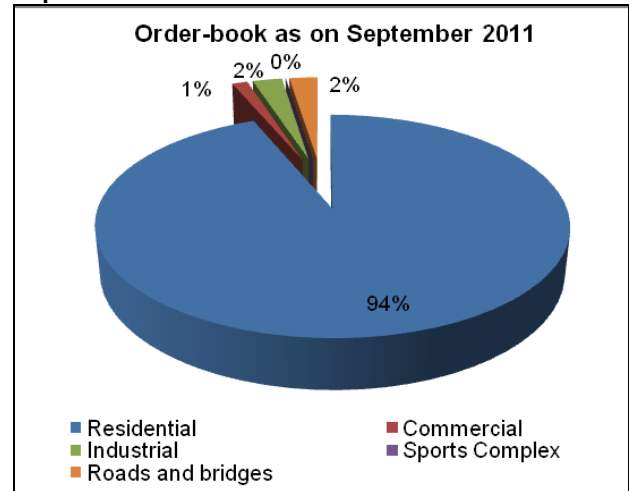
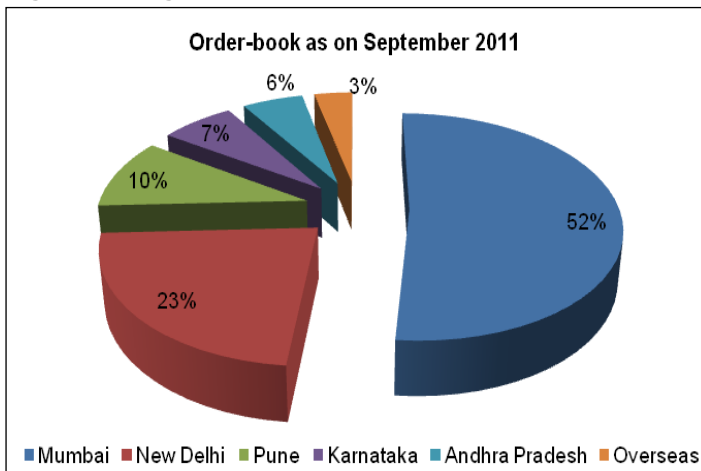


Figure 4: Geographic distribution of order-book



Gradual geographical diversification in geographic presence: BGS traditionally focused on the western region of the country primarily Mumbai and Pune, which together attributed to over three quarters of the order-book till FY 2007. However, BGS has increased its geographic spread in the last few years by venturing into other markets as well. As of September 30, 2011, Mumbai and Pune attributed to ~60% of the company's order-book. However it is to be noted that the number of projects outside Mumbai and Pune (Rest of India) remains low, with the company executing 8 projects in Rest of India as against 40 in Mumbai and Pune together. Moreover, the two main projects, namely, DDA and Rajiv Swagruha attribute to over

70% of the quantum of work outside Mumbai and Pune. Thus the order book concentration in terms of number of orders (and repeatability of orders) remains skewed towards Mumbai and Pune.

Delayed execution in many projects; situation further aggravated in recent past: Some of the projects under execution by the company have witnessed delays. The major reasons for delays are the delay in handing over of land by the awarding authority. Many projects are redevelopment project, wherein the existing residents are to be rehabilitated, then existing buildings to be demolished and new buildings to be constructed. The rehabilitation of the existing residents is the responsibility of MHADA and it usually entails delays. While delays in redevelopment projects have been a norm, the company has witnessed delays in some other projects as well which accentuates this issue. As on date the two largest projects being undertaken by the company (namely, DDA and Rajiv Swagruha), which together attribute to ~30% of orders in hand are running behind schedule owing to the land and client related issues. While time extensions are allowed in such cases where in the

delays are not attributable to client; the delays lead to increase overheads because of inefficient utilization of resources and also increase working capital requirements due to build up of inventory/receivables.

Financial Performance

Healthy Growth in Turnover and Profitability: The operating revenues have increased from Rs. 549.0 crore in FY 2007 to Rs. 1258.5 crore in FY 2011 reporting a healthy compounded annual growth rate (CAGR) of 23%. The growth rate however was subdued in the last two years on account of the high base as well as the delay in execution of some of the large projects being undertaken by the company. The operating margins of the company have increased steadily over the years from 9.12% in FY2007 to 16.90% in FY2011. It is to be noted that there was a jump in the profitability levels from FY 2009. This has been on account of larger share of higher margin yielding projects (primarily mill land redevelopment projects) in the total turnover of the company as well as rising economies of scale. The mill land development projects yield high realizations for MHADA and as a result the company is given a higher rate. With the increase in operating profitability, the PAT margins too have shown significant improvement, increasing from 1.86% to 7.56% in the same period (FY 2007 to FY 2011). This has been aided by the fact that with the increase in turnover, the debt of the company has not increased significantly; thereby the interest expense in proportion to the turnover has declined. The improvement in profitability has translated into high return indicators for the company.

Working capital intensity of operations aggravated by delayed payments in certain projects: BGS' working capital intensity had shown a steady improvement till FY 2010 aided by the reduction in debtor days. MHADA, which is the primary client for the company, is prompt in making payments and the receivables are realised in about 10 days. The increase in the number of MHADA projects in the portfolio helped keeping the receivables levels under control. However, in the recent past the company has been facing build-up of receivables as well as unbilled revenues (due to delays in bill certification) owing to delayed payments from APRSCL, which is an entity promoted by the Government of Andhra Pradesh, due to the liquidity constraints. This, in turn, lead to deterioration in the working capital intensity of operations from 11% in FY 2010 to 17% in FY 2011. The working capital intensity further aggravated to 44% in the first half of the current fiscal primarily on account of APRSCL project due to significant increase in inventory levels (largely uncertified works) and reduced creditors level. It is to be noted that while this project was initially valued at Rs. 786 crore, the scope of work was reduced on account of the poor liquidity condition of the client (APRSCL) and the project size was brought down to Rs. 450 crore. BGS expects APRSCL to secure external funding in the near term which would enable it to clear outstanding payments. Going forward, receiving payments in a timely manner in this project remains critical for the company.

Steady decline in gearing: There has been a steady decline in the gearing of the company from 3.7X as on March 31, 2007 to 1.31X as on March 31, 2011. This is driven by the robust accretion to reserves. While the funding requirement for working capital increased considerably in FY 2011, the healthy accretion to reserves enabled strengthening of capital structure. The total debt reported a significant increase in the current fiscal on account of rising working capital intensity leading to deterioration in gearing to 1.85X as on September 30, 2011, however it remains below the historical levels of over 2X as seen till FY 2009.

High contingent liability on account of guarantee of debt in group companies: The company has given corporate guarantees for group companies – Ganesh Shipping Inc. Panama (Rs. 167.58 crore), Five Stars Bulk Carriers Ltd. (Rs. 280.89 crore) and Future First Aviation service (Rs. 25.15 crore). Adjusting for the same, the gearing increases from 1.31x to 4.83x as on March 31, 2011. As mentioned, a large part of the corporate guarantee is towards the two shipping companies. While the shipping industry is currently going through a downturn, given the decline in freight rates coupled with rising cost pressures; the currently favorable financial profile of the shipping companies on a consolidated basis in FY 2011 as reflected by healthy portability levels (OPM of 58%), and coverage indicators (NCA/Total Debt of 34% and OPBDIT/Int of 7.93X) reduces the risk of guarantee invocation.

Management & Systems

BGS was promoted by Late Mr. B.G. Shirke who was a civil engineer by qualifications and is now managed by his son Mr. Vijay Shirke. Mr. B.G. Shirke was awarded the Padmashri in 2003. He was also a recipient of numerous other awards such as the Maratha Chamber of commerce award (1983), Sir Vishveshwaraiya Award

(1995) and the FIE Foundation National Award (1998). While the company is largely promoter driven, the various functions are managed by experienced professionals. The management has demonstrated the capability to retain key personnel and develop a strong engineering team. The people at the middle and top management are professionally qualified with long experience in the construction industry. The members of its senior management have, on an average, been with the company for 15-20 years. There has been a steady growth in the manpower base of the company in line with the growth in the order book and operating income. Out of the total manpower of 1989 as on March 31, 2011, 644 is technical staff (32%)

Prospects

The two most prominent projects under execution (DDA, Delhi and Andhra Pradesh Rajiv Swagruha) are currently witnessing delays on account of client related issues, which has lead to significant built-up in receivables and inventory position. Going forward, any further delays in the same can further impact the working capital intensity of the company thereby leading to pressure on its liquidity position. Nevertheless, some comfort can be drawn from the initiatives taken by APRSCL to improve its liquidity position by arranging external financing which will result in smoothening of work flow for the project and consequently also reduce the working capital requirements for BGS. Further, considering BGS' close relationship with MHADA and CIDCO and focus on mass housing segment, the order inflow for the company is expected to remain healthy resulting in stable growth in its turnover over the medium term.

Key Issues

The reaffirmation of the grading takes into account the BGS's established position and experience in the construction industry; healthy order-book position with unexecuted orders of Rs. 3,628 crore on September 30, 2011 providing visibility to sales in the near term; adequate resource base; gradual diversification in its geographic presence and backward integration in the value chain through the presence of group companies in the manufacture of prefabricated building components as well as construction equipment.

The grading continues to draw strength from the competitive advantage enjoyed by the company space of pre-fabricated construction space in the state of Maharashtra. In order to encourage the use of non-conventional construction technology, the Government of Maharashtra (GoM) has created a new category of construction companies, which employ such technologies, and has mandated organisations like the Maharashtra Housing and Area Development Authority (MHADA) and City & Industrial Development Corporation of Maharashtra Limited (CIDCO) to award a certain amount of construction work to companies registered under this category. BGS enjoys the first-mover advantage, as it is currently the only construction company to qualify under this category and has been awarded certain contracts directly by MHADA and CIDCO. While the competition is set to increase given the advent of other builders in prefabricated structures, BGS' long track record with MHADA and backward integration into the manufacture of prefabricated structures through group companies alleviate the risk to large extent.

While reaffirming the grading, ICRA has taken cognizance of the delays witnessed in two large projects undertaken by the company, which has lead to significant build up of receivables and inventory. Going forward, BGS' ability to complete the projects in a timely manner and reduce its working capital intensity will remain critical from grading perspective.

January 2012



ICRA Limited

An Associate of Moody's Investors Service

CORPORATE OFFICE

Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002
Tel: +91 124 4545300; Fax: +91 124 4545350
Email: info@icraindia.com, Website: www.icra.in

REGISTERED OFFICE

1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001
Tel: +91 11 23357940-50; Fax: +91 11 23357014

Branches: **Mumbai:** Tel.: + (91 22) 24331046/53/62/74/86/87, Fax: + (91 22) 2433 1390 **Chennai:** Tel + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294, Fax + (91 44) 2434 3663 **Kolkata:** Tel + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008, Fax + (91 33) 2287 0728 **Bangalore:** Tel + (91 80) 2559 7401/4049 Fax + (91 80) 559 4065 **Ahmedabad:** Tel + (91 79) 2658 4924/5049/2008, Fax + (91 79) 2658 4924 **Hyderabad:** Tel +(91 40) 2373 5061/7251, Fax + (91 40) 2373 5152 **Pune:** Tel + (91 20) 2552 0194/95/96, Fax + (91 20) 553 9231

© Copyright, 2012 ICRA Limited. All Rights Reserved.

Contents may be used freely with due acknowledgement to ICRA.

All information contained herein has been obtained by ICRA from sources believed by it to be accurate and reliable. Although 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. 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.