Sadbhav Infrastructure Project Limited
February 20, 2019

Ratings

Instruments	Amount (Rs. crore)	Ratings[1]	Rating Action
Long-term Non-Convertible Debentures	892.00	**CARE A (SO); Stable [Single A (Structured Obligation); Outlook: Stable]**	**Revised from CARE A+ (SO); Stable [Single A Plus (Structured Obligation); Outlook: Stable]**
Total Instruments@	**892.00 [Rupees Eight Hundred and Ninety Two Crore only]**		

Details of instruments in Annexure-1
@backed by unconditional and irrevocable corporate guarantee extended by Sadbhav Engineering Limited (rated 'CARE A; Stable/CARE A1')

Detailed Rationale & Key Rating Drivers

The revision in rating of the non-convertible debentures (NCDs) issue of Sadbhav Infrastructure Project Limited (SIPL) follows similar revision in the rating of Sadbhav Engineering Limited (SEL) from which it derives credit enhancement on account of unconditional and irrevocable corporate guarantee extended by SEL for its NCDs.

The revision in long term rating of Sadbhav Engineering Ltd (SEL) takes into account delay in rationalization of debt levels of Sadbhav group[2] primarily due to various issues related to land acquisition and clearances leading to delay in project execution of some of the projects and higher working capital intensity on a sustained basis despite recovery of old debtors and up-streaming of some cash flow from Sadbhav Infrastructure Project Ltd (SIPL; rated CARE A-; Stable; CARE A2+). SEL's management had articulated about their deleveraging plans by December 2018 through recovery of sizeable amount from old debtors pertaining to its completed build-operate-transfer (BOT), Engineering Procurement and Construction (EPC) road and irrigation projects as well as through various long-term fund raising plans at SIPL level.

The ratings, however, continue to derive strength from established track record of SEL in road construction segment along with its healthy and diversified order book. The ratings also factor financial flexibility of the Sadbhav group derived from good performance of most of the operational SPVs of SIPL during FY18 (refers to the period April 1 to March 31) and 9MFY19 marked by generation of decent cash surplus (post debt servicing) on aggregate basis and up-streaming of surplus cash from some of these projects. The ratings also take cognizance of receipt of large arbitration award in three special purpose vehicles (SPVs) of Sadbhav group, which once realized is expected to provide some cash flow cushion to the Sadbhav group.

The ratings are, however, constrained on account of stretched current asset days of SEL leading to high working capital borrowing, higher debt repayment obligations in the medium term, Sadbhav group's exposure to inherent risks associated with BOT projects, and inherent challenges faced by the construction sector (including the current challenging fund raising scenario for the sector).

SEL's inability to improve its current high working capital intensity leading to delay in rationalization of its working capital borrowings and improvement in its debt coverage indicators shall be key rating sensitivities. Extent of change in scope as well as significant delay in project progress in its various on-going projects adversely impacting the working capital intensity of the Group shall also be a key rating sensitivity. Further delay in materialization of long-term fund-raising plans by Sadbhav group leading to further moderation in its cash flow cushion shall be closely monitored.

Detailed description of the key rating drivers of SEL

Key Rating Strengths:

Established track record in the Indian road construction sector: SEL has a sound track record of over two decades in the Indian road construction sector. SEL has successfully completed construction of more than 7,551 lane km of road projects since its establishment with majority of the BOT projects completed in a timely manner.

Healthy and diversified order book: SEL had a healthy and diversified order book of Rs.12,872 crore (3.67 times of its contract receipts for FY18 [refers to the period April 1 to March 31]) as on December 31, 2018. The order book is diversified across four broad segments: EPC of road projects, EPC of BOT projects, mining and irrigation. The order book of the company is also geographically diversified with presence across various states of the country. Further, relatively less risky

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[1] *Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*
[2] *Combining SEL (standalone) and Sadbhav Infrastructure Project Limited (SIPL; standalone) financials*

HAM projects constitute around 54% of its order book. The contribution of road & highway segment in the total order book of the company which is its core strength has gradually increased to 78% as on December 31, 2018 as compared to 45% as on March 31, 2015.

***Financial flexibility of Sadbhav Group arising from good performance of operational SPVs of SIPL during FY18 and 9MFY19 marked by generation of cash surplus and up-streaming of it*:** During the past two years, SIPL has successfully refinanced debt in nine of its operational SPVs. The same has led to substantial reduction in interest rate, staggered installment repayments utilizing its tail period and tie up of funds for the first major maintenance thereby resulting in self-sustainable operations of these SPVs. Post refinancing, the average cost of debt in nine of its operational SPVs has reduced to around 9.27% per annum. Furthermore, there has been notable growth in toll collection of SPVs portfolio during FY18 and 9MFY19 due to growth in traffic in some of the stretches nearer to Golden Quadrilateral (GQ) and Haryana apart from hike in service fees by 18% with effect from April 2018 in MBCNL. The same has been reflected from steady increase in cash surplus (post debt servicing and stipulated reserve requirement) from operational SPVs during FY18 and 9MFY19 as against large cash deficit during FY17. Surplus cash generated in operational SPVs has been partly up streamed to meet funding requirement of Sadbhav group. Furthermore, sanctioned loan facilities of MBCNL has an option of top-up loan up to Rs.520 crore wherein Rs.150 crore has already been drawn till December 2018 and up streamed to SIPL while balance amount is eligible for disbursement in tranches upon debt syndication and achievement of targeted revenue for consecutive three months. This is expected to result in up-streaming of cash flow for SIPL which has been suitably factored in its credit risk assessment. However, successful tie-up and disbursement of balance top-up debt in MBCNL and its up-streaming to SIPL within envisaged timelines will be crucial from the credit perspective in light of pending debt syndication for amount to be drawn and current challenging business environment.
Sadbhav group’s overall gearing stood moderate at 0.82 times as on March 31, 2018 which stood stable at 0.78 times as on December 31, 2018 as compared to 1.02 times as on March 31, 2017. Financial flexibility of the group is also derived from listing of equity shares of both SEL and SIPL on stock exchanges and large operational portfolio of BOT road projects.

Various initiatives undertaken by the Government of India (GOI) to improve the prospects of the road construction sector: GOI through National Highways Authority of India (NHAI; rated ‘CARE AAA; Stable’) has taken various steps to improve the prospects of the road sector. These include premium rescheduling for stressed projects, bidding of tenders only after 80% land has been acquired for the project, release of 75% of arbitration award against submission of bank guarantee and 100% exit for developers after two years of project completion and NHAI funding for projects that are stuck at advanced stages of completion. Furthermore, NHAI has made some favourable changes in the clauses of model concession agreement and introduced HAM based BOT projects to reduce the equity commitment of the developers. After witnessing steady increase in pace of award during last three years, CARE Ratings expects decline in project award activity during FY19; albeit with some moderation in competition in the industry. EPC is envisaged to be the preferred mode of award till improvement in fund raising environment and bidding appetite of the developers.

Key Rating Weaknesses:

Delay in rationalization of debt levels primarily due to various execution hurdles and higher working capital intensity on a sustained basis despite realization of significant portion of old debtors: Seven ongoing HAM projects of Sadbhav Group constituted Rs.3,983 crore in SEL’s total order book as on March 31, 2018. All these projects except one HAM project with EPC value of Rs.780 crore was scheduled to be completed by September 2019. Delay in execution of some of ongoing HAM projects is due to hindrances in land acquisition, utility shifting, delay in other clearances, etc. Consequently, these SPVs have now applied for Extension of Time (EOT)/ de-scoping/de-linking of these projects. As and when such request of these SPVs is approved it can result in improvement in the project progress. NHAI has recently approved de-scoping in one of its projects. Furthermore, SEL envisages realization of some GST receivables and receipt of construction grant in five of its ongoing HAM projects aggregating Rs.320 crore and mobilization advance aggregating Rs.180 crore in projects where appointed date has already been received. Timely receipt of the aforesaid amount aggregating to Rs.500 crore leading to rationalization of debt levels shall be key rating monitorable.
SEL’s management had articulated about its plans to significantly improve its collection efficiency through realization of old dues pertaining to change in scope from authority, up-streaming of surplus funds from its two operational SPVs and release of payment from its largely completed EPC road and irrigation projects. The management had articulated about reduction in debtors from above projects by ~Rs.400 crore by September 2018 from June 2018 levels and by another Rs.200 crore by December 2018. SEL has realized around Rs.350 crore of its old debtors during H1FY19 and another Rs.165 crore during Q3FY19. It has further recovered loans & advances of around Rs.90 crore during H1FY19 through up-streaming of cash flows from some of its SPVs.
However, the working capital intensity continued to remain high on a sustained basis. This was mainly on account of new debtors pertaining to escalation portion and change of scope in some of its ongoing HAM projects apart from GST

receivables as well as due to relatively higher time required for term debt disbursement in its HAM SPVs owing to challenging fund raising environment prevailing in the construction sector.
This has resulted in increase in combined total debt by Rs.150 crore during H1FY19 from Rs.2,310 crore as on March 31, 2018 and the same has also largely continued as on December 31, 2018 as against the previous articulation of the company to reduce it by December 31, 2018. However, overall gearing continued to remain moderate as stated above.

Liquidity Analysis: Higher repayment obligations and working capital utilization; albeit partly offset by its good financial flexibility: The utilization of SEL's fund-based working capital borrowings during trailing 12 months-ended December 2018 remained high. Combined debt coverage indicators are expected to remain moderate in the medium term in light of higher redemption obligations of SIPL leading to refinancing risk. However, SIPL has demonstrated its track record of refinancing its high repayment obligations in the past which provides some comfort from credit perspective.

Exposure of the group to inherent risks associated with BOT projects along with subdued performance of two of its SPVs: Sadbhav group's exposure in the form of investment and loans & advances to its various SPVs further increased to 112% of the group's net worth as on March 31, 2018. The under construction HAM projects of the group have equity commitments of around Rs.1,000 crore spread over FY20 – FY22. The equity commitments for these HAM projects and shortfall in two operational SPVs are expected to be fulfilled through up-streaming of cash flows from MBCNL and other operational SPVs apart from cash accrual of SIPL. However, in case of delay in debt syndication of large portion of sanctioned top up loan of MBCNL, reliance on debt guaranteed by SIPL can increase. Piramal Housing Finance Ltd has extended sanction of Rs.600 crore based on valuation matrix of under construction HAM with corporate guarantee of SIPL upto COD of respective HAM projects. Going forward, SIPL's ability to materialize various long-term fund raising plans to rationalize its debt levels in a time bound manner as articulated by its management will be crucial.

Challenging environment for the construction industry: The construction sector is facing hurdles in fund raising due to delay in enhancement of working capital limits (including non-fund based limits), delay in financial closure and equity raising plans on account of challenging business environment for the sector and weakened financial health of the banking sector. Appointed date of some of the HAM projects of SIPL has also been delayed due to challenging scenario. The inherent risk involved in the construction industry including aggressive bidding, traffic risk, interest rate risk, volatile commodity prices and delay in project progress due to resistance towards land acquisition and regulatory clearances have collectively affected the credit profile of the developers in the past.

Analytical approach: Combined
CARE has taken a combined view of SEL (standalone) and SIPL (standalone) for analytical purpose. This is because majority of the long-term debt raised in SIPL is backed by unconditional and irrevocable corporate guarantee of SEL. Further, SEL and SIPL have operational and financial linkages for funding shortfall as well as up-streaming of cash flow of SPVs.

Applicable Criteria
Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
Criteria for Short Term Instruments
Rating Methodology - Factoring Linkages in Ratings
Rating Methodology - Infrastructure Sector Ratings
Financial Ratios – Non-Financial Sector

About the company – SIPL
SEL had floated a 100% subsidiary, SIPL, in January 2007, as a holding company for its BOT projects. During FY11, SEL diluted 22.22% of its stake through issue of fresh equity of Rs.300 crore and compulsory convertible cumulative preference shares (CCCPS) of Rs.100 crore to private equity (PE) investors. Proceeds of PE were utilized by SIPL for fulfilling its equity commitment in BOT projects. During September 2015, SIPL raised Rs.425 crore through Initial Public Offer (IPO) of its equity shares. Sadbhav Group has a portfolio of 25 BOT projects (eleven operational, one partly operational and thirteen under construction HAM projects).

Brief Financials – SIPL (Standalone) - (Rs. crore)	FY17 (A)	FY18 (A)
Total operating income (TOI)	312	384
PBILDT	182	268
PAT	41	68
Overall gearing (times)	0.91	0.95
Interest coverage (times)	1.40	1.64

A: Audited; As per IND-AS accounting standard;
Based on un-audited results for 9MFY19, SIPL reported TOI of Rs.274 crore (9MFY18: Rs.308 crore) and profit after tax (PAT) of Rs.49 crore (9MFY18: Rs.57 crore).

About the Guarantor - SEL

Incorporated in 1988, SEL has evolved as one of the prominent developers and EPC contractors in India. SEL had floated a wholly-owned subsidiary – SIPL as a holding company of BOT projects in 2007. Sadbhav Group has a portfolio of 25 BOT projects (eleven operational, one partly operational and thirteen under construction HAM projects). SEL operates majorly across four distinct business areas in the infrastructure sector viz. EPC of its own BOT road projects, cash contract-based road and metro rail EPC projects, irrigation and mining. During FY18, these segments contributed 34%, 49%, 9% and 7%, respectively, in SEL's contract receipts booked on a standalone basis.
During FY17, son of late Mr Vishnubhai Patel (founder of Sadbhav group), Mr Shashin Patel, became the Chairman and Managing Director of SEL and Chairman and Non-Executive Director of SIPL. Mr Vasistha Patel who is the Executive Director of SEL became the Managing Director of SIPL.

Brief Financials – SEL (Standalone) - (Rs. crore)	FY17 (A)	FY18 (A)
Total operating income (TOI)	3,395	3,535
PBILDT	432	445
PAT	186	221
Overall gearing (times)	1.07	0.80
Interest coverage (times)	2.83	2.33

A: Audited; As per IND-AS accounting standard;

Based on un-audited results for 9MFY19, SEL reported TOI of Rs.2,609 crore (9MFY18: Rs.2,456 crore) and profit after tax (PAT) of Rs.158 crore (9MFY18: Rs.151 crore).

Brief Financials – Sadbhav Group - (Rs. crore)	FY17	FY18
TOI	3,659	3,862
PBILDT	565	657
PAT	227	288
Overall gearing (times)	1.02	0.83
Interest coverage (times)	2.42	2.20

Based on provisional results for 9MFY19, Sadbhav group reported TOI of 2,832 crore (9MFY18: Rs.2,720 crore) and PAT of Rs.207 crore (9MFY18: Rs. 207 crore).

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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About CARE Ratings:

CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Debentures-Non Convertible Debentures	December 16, 2014	12.14%	Nov 18, 2019	112.00	CARE A (SO); Stable
Debentures-Non Convertible Debentures	January 09, 2015	11.75%	April 13, 2020	120.00	CARE A (SO); Stable
Debentures-Non Convertible Debentures	September 21, 2016	10.30%	April 26, 2022	300.00	CARE A (SO); Stable
Debentures-Non Convertible Debentures	April 20, 2018	10.20%	May 2023	360.00	CARE A (SO); Stable

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016
1.	Fund-based - LT-Term Loan	LT	-	-	-	-	-	1)Withdrawn (02-Feb-16)
2.	Bonds	LT	-	-	1)Withdrawn (18-Sep-18)	1)CARE A+ (SO); Stable (08-Jan-18)	1)CARE A+ (SO) (14-Oct-16)	1)CARE A+ (SO) (01-Mar-16)
3.	Debentures-Non Convertible Debentures	LT	112.00	CARE A (SO); Stable	1)CARE A+ (SO); Stable (18-Sep-18)	1)CARE A+ (SO); Stable (08-Jan-18)	1)CARE A+ (SO) (14-Oct-16)	1)CARE A+ (SO) (01-Mar-16)
4.	Debentures-Non Convertible Debentures	LT	120.00	CARE A (SO); Stable	1)CARE A+ (SO); Stable (18-Sep-18)	1)CARE A+ (SO); Stable (08-Jan-18)	1)CARE A+ (SO) (14-Oct-16)	1)CARE A+ (SO) (01-Mar-16)
5.	Debentures-Non Convertible Debentures	LT	300.00	CARE A (SO); Stable	1)CARE A+ (SO); Stable (18-Sep-18)	1)CARE A+ (SO); Stable (08-Jan-18)	1)CARE A+ (SO) (14-Oct-16)	-
6.	Fund-based/Non-fund-based-LT/ST	LT/ST	400.00	CARE A-; Stable / CARE A2+	-	1)CARE A-; Stable / CARE A2+ (28-Nov-17)	-	-
7.	Debentures-Non Convertible Debentures	LT	360.00	CARE A (SO); Stable	1)CARE A+ (SO); Stable (18-Sep-18) 2)Provisional CARE A+ (SO); Stable (16-Apr-18)	-	-	-