December 13, 2022

UMSL Limited (Erstwhile Utkal Manufacturing & Services Limited): Ratings assigned for enhanced bank limits

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund Based Limits – Term loans	--	36.61	[ICRA]BBB+ (Positive); assigned
Fund Based Limits – WC limits	120.00	110.00	[ICRA]BBB+ (Positive); outstanding
Short Term Non Fund Based	168.00	273.00	[ICRA]A2; outstanding/assigned for enhanced amount
Unallocated	--	172.00	[ICRA]BBB+ (Positive)/[ICRA]A2; assigned
Total	**288.00**	**591.61**	

*Instrument details are provided in Annexure-1

Rationale

The rating action factors in ICRA's expectation that UMSL Limited (UMSL) would continue to record a healthy operating performance in the near-to-medium term in the backdrop of the company's robust order book of ~Rs. 1,300 crore, which is ~4.2 times of the operating income (from civil construction business) of FY2022. These orders are expected to be executed over the next 24 months, providing healthy revenue visibility. Given the higher operating margin of these orders, compared to historical trends, UMSL's business return and debt coverage indicators are likely to improve, going forward.

The ratings also continue to positively factor in the long track record of the company in the logistics and civil construction business, and a reputed client profile consisting of government and semi-government agencies, thereby reducing the counterparty credit risks. These strengths are, however, offset by the increased concentration of the order book in water supply and roads segments (construction segment). Besides, intense competition and a tender-based contract awarding system keep the operating margins under check. The company also remains exposed to the geographical concentration risk as more than 90% of its projects are concentrated in Odisha. It is also exposed to the project execution risk as around 80% of the order book, as on September 30, 2022, recorded less than 25% execution. ICRA, however, draws comfort from UMSL's top management, having significant experience in the water pipeline laying projects, technical expertise from its JV partner for these projects and an established presence in Odisha as an EPC contractor since many years.

The ratings continue to be constrained by the company's modest scale of operations and debt coverage indicators in the recent past. In FY2022, UMSL reported a marginal growth in the operating revenues to ~Rs. 388 crore from ~Rs. 370 crore in FY2021. Further, the margins remained under pressure as the company focused on finishing its legacy projects having lower profitability and order sizes. Consequently, the company's financial risk profile remained modest with some moderation seen in debt coverage indicators in FY2022 (interest coverage and Total Debt/OPBDITA of around 2.1 times and 3.5 times, respectively in FY2022 compared to 2.2 times and 0.9 times, respectively in FY2021).

Going forward, UMSL's ability to scale up execution of the current order book, manage working capital requirement along with the availability to tie up adequate bank lines would be the key factors for determining the financial risk profile of the company. The company is in discussion with the lenders for enhancement of its non-fund based working capital limits. Timely sanction of the same would remain a key rating monitorable.

Key rating drivers and their description

Credit strengths

Long track record of the company in logistics solutions and civil construction – UMSL's promoters have experience of around three decades in the road transportation of minerals and metal products. The company caters to the logistics requirements of its Group company, Indian Metal & Ferro Alloys Limited (IMFA), which is India's largest fully-integrated producer of ferro alloys. In addition, the company has been undertaking construction of roads, buildings, bridges, canals etc for the past several years, which contributed ~80% to the company's total revenues in FY2022. This segment has increased at a healthy pace, as corroborated by a CAGR of 17% since FY2014. UMSL has been hiring renowned professionals from the industry in the recent years at various leadership positions across business verticals and project divisions, which augur well for the future growth prospects of the company.

Major part of client portfolio comprises government and semi-government agencies, which reduces counterparty risks – The client portfolio of UMSL mainly comprises various government and semi-government agencies like Rural Water and Sanitation Department, Road Construction Department, Building Construction Department, National Highway Authority of India, IRCON, World Bank-funded projects etc, resulting in low counterparty credit risk.

Addition of large orders in FY2022 to improve revenue visibility as well as diversify order book into new sectors – UMSL witnessed more than 80% growth in its construction order book to ~Rs.1,300 crore as on September 30, 2022 from Rs.704 crore as on June 1, 2021 with inflow of new work orders in Q4 FY2022, providing healthy revenue visibility for the next two fiscals. The new orders largely comprise projects involving laying of pipelines for water supply (under the Jal Jeevan Mission) and construction of a six-lane road section of the National Highway in Odisha (subcontracted from Adani Roads), having execution timelines of 18-24 months. This apart, with the projects awarded under the Jal Jeevan Mission, the company's order book concentration in the roads segment reduced, which earlier comprised a major portion of the order book. However, the concentration continues to remain high in few focused sectors as on date.

Favourable capital structure – The capital structure of the company has remained conservative over the past few years, primarily on the back of a gradual build-up of net worth and fair valuation of the company's gross block upon transition to Ind AS in FY2019, increasing UMSL's tangible net worth significantly. The gearing of the company stood at 0.2 times and TOL/TNW at 0.5 times as on March 31, 2022.

Credit challenges

Intense competition, tender-based contract awarding system keep margins under check – ICRA notes that the civil-construction industry is intensely competitive due to its fragmented nature with presence of many players. This coupled with the lowest bidding system keeps margins of all players, including UMSL, under check. The margin is also exposed to volatility in raw material prices. ICRA, however, notes that the built-in price variation clause in most of the contracts mitigates the said risk to an extent. The profitability is expected to improve, going forward, given the higher operating margin of the new large orders than the historical trends.

High working capital intensity – The high working capital intensity is inherent in the civil construction industry, which is generally led by high trade receivables, work-in-progress and other current assets (margin money and security deposits). The working capital intensity of UMSL remained higher as reflected in NWC/OI of 33% in FY2022. This was partly due to the elongated receivables cycle during the year, as the company awaited clearance of final bills for its completed projects. The ongoing working capital requirements are expected to remain at similar levels, as seen in the past, given no major changes in the client profiles and the terms of business, apart from the non-requirement of earnest money deposits (EMD) while bidding for new projects, which may reduce the incremental requirement for margin money deposits required for EMD bank guarantees. Despite limited reliance on term debt, the debt coverage indicators remained modest with an interest coverage and Total Debt/OPBDITA of around 2.1 times and 3.5 times, respectively in FY2022 compared to 2.2 times and 0.9 times, respectively in FY2021, largely due to dependence on working capital borrowings. However, going forward, with an expected increase in the scale of operation and profits, the debt-coverage indicators are expected to improve steadily.

Any delay in execution of contracts could adversely impact revenue growth and liquidity position – The current orders have an average tenure of 24 months. However, delays, if any, in receipt of clearances from the awarding authorities or delays in project execution by the company could have a potential impact on its future revenue growth and liquidity position. Further, the order book is highly concentrated, with the top five work orders accounting for 85% of the order book. This increases the risk of revenue booking in case of any delay in order execution or payments from the department. In addition, higher encumbered fixed deposit balances primarily for margin money as well as for the projects in Odisha adversely impacted the liquidity position in the past. However, the same is getting released with the completion of old projects.

Exposure to geographical risks – More than 90% of the orders in terms of contract value, to be executed by the company, are in Odisha, exposing it to geographical concentration risks. ICRA, however, notes that the company in the process of adding more contracts outside the state, which would mitigate the said risk to some extent. Also, the company expects to maintain a mix between private and government clients, going forward.

Liquidity position: Adequate

UMSL's liquidity is expected to remain adequate, as reflected in its comfortable liquidity position with cushion in available fund-based limits of Rs. 25 crore as of September 2022 and free cash and bank balances of ~Rs. 2 crore as on March 31, 2022. The debt repayment of Rs. 9 crore in the current fiscal can be comfortably met through expected net cash accruals. The construction business involves high usage of non-fund based limits, with an average six month utilisation of ~60% and cushion of ~Rs.90 crore in non-fund based limits as of September 2022, is expected to be adequate to support order book addition and execution in the near term. This apart, the company is in discussion with the lenders for enhancement of its non-fund based working capital limits and timely sanction of the same would support order book addition and execution in the medium term.

Rating sensitivities

Positive factors – Ramp-up in execution of the current order book, resulting in a significant increase in revenues and profitability as well as prudent management of working capital requirements, would be credit positives. Specific triggers for ratings upgrade would be an interest cover of more than 3.5 times on a sustained basis.

Negative factors – Pressure on the ratings could arise if there are significant delays in project execution, leading to a decline in its scale, operating profitability or a deterioration in its liquidity position. Specific triggers for downgrade would be DSCR below 1.6 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Construction Entities
Parent/Group Support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of UMSL.

About the company

UMSL Limited (formerly Utkal Manufacturing & Services Limited), incorporated in 1991, is an EPC and logistics company having its registered office in Visakhapatnam (Andhra Pradesh) and corporate office in Bhubaneswar (Odisha). It was initially involved in providing specialised logistics solutions to various companies. After the demerger of the ferro-alloys division in FY2010, the company diversified into the construction segment, which has been contributing a large share to the revenues over the past few years. Through this segment, UMSL is involved in infrastructure development (construction of roads, highways, bridges, pipelines etc) with its geographical span extending to Odisha (infrastructure and water pipeline projects), Jharkhand and Chhattisgarh (infrastructure projects).

Key financial indicators (audited)

Consolidated	FY2021	FY2022
Operating Income (Rs. crore)	370	388
PAT (Rs. crore)	23	10
OPBDIT/OI (%)	8.0%	7.1%
PAT/OI (%)	6.3%	2.6%
Total Outside Liabilities/Tangible Net Worth (times)	0.3	0.5
Total Debt/OPBDIT (times)	0.9	3.5
Interest Coverage (times)	2.2	2.1

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 (FY2023)					Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding (Rs. crore)*	Date & rating in FY2023		Date & rating in FY2022	Date & rating in FY2021	Date & rating in FY2020
					Dec 13, 2022	Dec 08, 2022	Sep 23, 2021	Aug 24, 2020	Dec 13, 2019
1	**Fund Based Limits – Term loans**	Long Term	36.61	25.2	[ICRA]BBB +(Positive)	-	-	-	-
2	**Fund Based Limits – WC limits**	Long Term	110.00	-	[ICRA]BBB +(Positive)	[ICRA]BBB +(Positive)	[ICRA]BBB +(Stable)	[ICRA]BBB+ (Negative)	[ICRA]BBB+ (Stable)
3	**Non Fund Based**	Long Term	-	-	-	-	[ICRA]BBB +(Stable)	[ICRA]BBB+ (Negative)	[ICRA]BBB+ (Stable)
4	**Non Fund Based**	Short Term	273.00	-	[ICRA]A2	[ICRA]A2	[ICRA]A2	[ICRA]A2	[ICRA]A2
5	**Unallocated**	Long/Short Term	172.00	-	[ICRA]BBB +(Positive) /[ICRA]A2	-	-	-	-

**Outstanding as on March 31, 2022*

Complexity level of the rated instrument

Instrument	Complexity Indicator
Fund Based Limits – Term loans	Simple
Fund Based Limits – WC limits	Simple
Short Term Non Fund Based	Very Simple
Unallocated	Not Applicable

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-1: Instrument details

ISIN No.	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Fund Based Limits – Term loans	FY2019	NA	FY2029	36.61	[ICRA]BBB+ (Positive)
NA	Fund Based Limits – WC limits	NA	NA	NA	110.00	[ICRA]BBB+ (Positive)
NA	Short Term Non Fund Based	NA	NA	NA	273.00	[ICRA]A2
NA	Unallocated	NA	NA	NA	172.00	[ICRA]BBB+ (Positive)/[ICRA]A2

Source: Company

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

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Isaya Construction Pvt. Ltd.	100%	Full Consolidation
Raila Enterprises Pvt. Ltd.	100%	Full Consolidation

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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.

For more information, visit www.icra.in

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