HPL Electric & Power Limited
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11th April, 2020

The Manager,
Listing Department,
National Stock Exchange of India Ltd.
"Exchange Plaza", C-1, Block G,
Bandra-Kurla Complex, Bandra (E),
Mumbai – 400 051
Symbol: HPL

BSE Limited
25th Floor, New Trading Ring, Rotunda
Building, Phiroze Jeejeebhoy Towers,
Dalal Street, Fort,
Mumbai – 400 001

Scrip Code: 540136

Subject: Disclosure under Regulation 30 of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015

Dear Sir

This has reference to Regulation 30 of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, we wish to inform that the company has received an intimation through Email dated 10th April, 2020 from the India Ratings and Research Pvt. Ltd. regarding the revision of the ratings to various instruments/bank facilities of the company. The copy of the same is enclosed herewith for your reference.

This is to further mention that the Company respectfully protests and disagrees with the revision in the rating by India Ratings and Research Pvt. Ltd. and is in the process of getting the above rating reviewed from India Ratings and Research Pvt. Ltd.

Kindly take the same on record.

Thanking You

Yours Faithfully
For HPL ELECTRIC & POWER LIMITED

Vivek Kumar
Company Secretary

Encl: As above

India Ratings & Research
A Fitch Group Company

India Ratings Downgrades HPL Electric & Power to 'IND BBB+'; Outlook Stable

31

MAR 2020

By Ankur Rustagi

India Ratings and Research (Ind-Ra) has downgraded HPL Electric & Power Limited's (HPL) Long-Term Issuer Rating to 'IND BBB+' from 'IND A-'. The Outlook is Stable. The instrument-wise rating actions are as follows:

Instrument Type	Date of Issuance	Coupon Rate	Maturity Date	Size of Issue (billion)	Rating/Outlook	Rating Action
Fund-based working capital limits	-	-	-	INR4.75 (reduced from INR4.95)	IND BBB+/Stable/IND A2	Downgraded
Non-fund-based working capital limits	-	-	-	INR7.45	IND BBB+/Stable/IND A2	Downgraded
Commercial Paper (CP)	-	-	Up to 365 days	INR3.2	IND A2	Downgraded
Term loan*	-	-	March 2024	INR0.4	IND BBB+/Stable	Downgraded & Assigned
Proposed long-term loans**	-	-	-	INR0.25 (reduced from INR0.65)	Provisional IND BBB+/Stable	Downgraded

* Downgraded to 'Provisional IND BBB+'/Stable and assigned final rating following the receipt of sanction letter by Ind-Ra.
** The ratings are provisional and shall be confirmed upon the sanction and execution of the loan documents for the above facilities by HPL to the satisfaction of Ind-Ra.

Analytical Approach: Ind-Ra continues to take a consolidated view of HPL and its subsidiary, Himachal Energy Private Limited ('IND BBB+'/Stable), to arrive at the ratings, due to the strong operational, legal and strategic linkages between the two companies.

The downgrade reflects HPL's sustained elongated working capital cycle and continued spending on capex leading to higher-than-expected net leverage (net debt/EBITDA) on trailing 12-month (TTM) basis of 4.1x for 9MFY20 (FY19: 3.7x, FY18: 4.4x) and gross interest coverage (EBITDA/interest expense) remaining moderate at 2.1x (2.3x, 2.2x).

KEY RATING DRIVERS

Working Capital Cycle Remains Stretched: The consolidated net working capital deteriorated at a pace faster than that expected by Ind-Ra with net working capital cycle as a percentage of sales at 65% on a TTM basis in 9MFY20 (FY19: 57.8%, FY18: 58.2%). Ind-Ra had expected the benefits of inventory rationalisation and channel financing to shorten the working capital cycle; however, the same is yet to play out. According to the management, the increase in inventory and debtors in 9MFY20 was account of the delay in inspection by the state public utilities (SPUs) and delayed payments, given their weak financial profiles. Additionally, the slowdown in the commercial real estate markets has not helped, as the offtake in the switchgear and cables segment has been lower.

On a TTM basis, debtor days and inventory days rose to 154 in 9MFY20 (FY19: 148, FY18: 165) and 195 (191, 220), respectively, while the payable days continued to decline to 73 (77, 114). The management has been focusing on improving its collections and increasing the non-SPU sales, wherein the debtor days are lower; however, the share of SPUs continues to remain high, burdening the overall working capital cycle. Any movement of inventory days will depend on the timely inspections from SPUs and the share of better paying states such as Gujarat, West Bengal, and private utilities will determine the future movement of debtor days. At end-9MFY20, HPL had receivables of INR4.7 billion (FY19: INR4.7 billion, FY18: INR4.7 billion), inventory of INR4.5 billion (INR4.1 billion, INR4.2 billion) and payables of INR2.0 billion (INR2.2 billion, INR2.9 billion). Ind-Ra will continue to monitor the working capital movement, a further stretch in which could be negative for the ratings.

Credit Profile Deterioration: The consolidated net adjusted financial leverage (net adjusted debt/EBITDA) increased to 4.1x in 9MFY20 (annualised) given the longer working capital cycle, leading to increased short-term borrowings. Additionally, HPL had, over FY15-FY19, incurred an annual capex of INR500 million-600 million, on tooling, moulds, the launch of new product ranges; however, the same has not resulted in meaningful sales increase leading to a reduction in the net fixed asset turnover to 2.7x in FY19 from 3.3x in FY15 (FY18: 2.6x). During 9MFY20, the consolidated interest coverage declined to 2.1x (FY19: 2.3x, FY18: 2.2x). Earlier, to manage its interest cost, HPL used its CP, which has discontinued and could lead to an increase in interest costs. Additionally, HPL uses a significant amount of non-fund-based limits for the import of raw material (through letters of credit) and for submitting performance bank guarantee/bid bonds. Hence, any increase in the non-fund-based charges could adversely impact the interest coverage ratios.

Ind-Ra believes unless HPL is able to shorten its working capital cycle, its credit metrics will remain stretched. At end-December 2019, the consolidated gross debt stood at INR5.7 billion (FY19: INR5.3 billion, FY18: INR4.9 billion) with short-term debt of INR5.2 billion (INR5.0 billion, INR4.6 billion) and long-term debt of INR0.5 billion (INR0.3 billion, INR0.3 billion). The company can also draw down an additional long-term debt of INR0.4 billion during the year. However, the overall slowdown in the macro economy could further impact the overall liquidity and cash collections, leading to further stress on the debt metrics.

Liquidity Indicator - Stretched: HPL's long working capital cycle has led to high working capital borrowings. Its average utilisation against drawing power of fund-based working capital limit was 96% while that of non-fund-based limits was 73% during the 12 months ended February 2020. To improve liquidity, HPL has availed long-term loans amounting INR400 million in 9MFY20 to meet the capex requirements and has received approval for increasing its fund-based and non-fund-based limits from a consortium lead bank. Any delay in the sanction of these increased limits could negatively impact HPL's ability to acquire fresh orders.

HPL's cash and cash equivalents remained moderate at INR0.3 billion at end-December 2019 (FY19: INR0.3 billion, FYE18: INR0.1 billion). The company does not have any major debt repayments in the medium term. HPL has a repayment of INR49 million in 4QFY20 and of INR155 million in FY21. Its cash flow from operations turned positive at INR0.3 billion in FY19 (FY18: negative INR0.3 billion, FY17: negative INR0.6 billion) due to an improvement in working capital cycle in Q4FY19. However, the company's free cash flow remained negative at INR0.4 billion in FY19 (FY18: negative INR1.0 billion, FY17: negative INR1.2 billion) due to continued capex (9MFY20: INR0.5 billion, FY19: INR0.6 billion, FY18: INR0.6 billion). HPL made dividend payment (including dividend tax) of INR16 million in 9MFY20 (FY19: INR78 million, FY18: INR116 million) and is likely to continue issuing regular dividends.

Declined Order Book and Revenue: HPL's revenue declined 5% yoy to INR7.6 billion in 9MFY20 (FY19: INR11.6 billion, FY18: INR10.4 billion). The decline in the overall revenue despite a 5% yoy growth in the company's meter segment was due to a decline in the revenue from the switchgear (21% yoy) and cables (34%) segments. While the decline in the switchgear segment was caused by subdued demand in the real estate, industrial and infrastructure markets, the decline in the cables segment was caused by the price rise implemented by the company in 1QFY20 to improve margins.

The company's order book, largely dominated by the metering segment, contracted to INR3.7 billion at end-December 2019 (end-May 2019: INR5.8 billion) as the overall ordering from across India slowed down. Ind-Ra expects the share of smart meters to increase in the new orders leading to better margins and higher revenue. Also, as against the aggregator model followed under the Energy Efficiency Services Limited tender route, the majority of the new orders come directly from state utilities which could benefit the company in negotiating better payment terms. However, any slowdown in the order booking could result in a decline in revenue booking and margins. HPL, however, is hopeful that given the budget allocation made in the current budget towards meters, the ordering activity should pick up 2QFY20 onwards, thus providing healthy revenue visibility. The government has recommended replacing all electricity meters (around 250 million) with prepaid smart meters within three years which could result in substantial ordering activity. However, HPL's ability to participate in the ordering activity will be contingent of the availability of sufficient working capital limits that are constrained by its long working capital cycle.

Improved EBITDA Margin: HPL's EBITDA margins increased to 12.8% in 9MFY20 (9MFY19: 11.5%, FY19:11.5%), led by the higher share of high-margin smart meters and a reduction in raw material prices. EBIT margins in the meters segment stood at 15.9% in 9MFY20 (FY19: 15.1%, FY18: 15.6%). Additionally, the margins were supported by HPL's decision to lower its sales in the cables segment as it is a low-margin segment (9MFY20: 4.0%, FY19 4.4%: FY18: 6.0%). During 9MFY20, the margins in the switchgear and lighting segment stood at 18.5% (FY19: 18.9%, FY18: 18.1%) and 10.7% (11.4%, 11.6%).

However, if the raw material prices were to rise again (key raw materials are copper, polycarbonate), coupled with rupee depreciation, it could negatively impact the margins. Ind-Ra expects the margins to remain at the 9MFY20 level in FY20, and to hover around 12% in the medium term, considering the likely increase in raw material prices and the execution of repeat orders (which tend to have lower margins), leading to lower gross margins. The company will, however, continue to derive scale benefits and product mix benefit as the use of smart meters increases.

Diversified Revenue Base: The meter segment accounted for 57.5% of HPL's revenue in 9MFY20 (FY19: 52.6%, FY18: 50.6%), followed by the switchgear segment (17.4%, 19.6%), the lighting segment (18.6%, 18.3%) and the cables segment (6.6%, 9.5%). This diversification provides a natural edge to HPL's overall business profile compared to single-product companies.

Marginal Deterioration in Standalone Performance: During 9MFY20, HPL's standalone revenue was INR7.4 billion (9MFY19: INR7.7 billion, FY19: INR11.0 billion) with EBITDA margin of 12.0% (10.4%, 10.6%). Standalone net leverage and interest coverage marginally deteriorated to 4.3x in 9MFY20 (FY19: 3.9x, FY18: 4.45x) and 2.1x (2.2x, 2.1x).

RATING SENSITIVITIES

Positive: A substantial increase in the consolidated revenue and EBITDA, an improvement in the net working capital cycle and a decline in debt leading to overall improvement in the liquidity and consolidated credit profile could lead to a positive rating action.

Negative: A decline in the consolidated revenue and EBITDA, further deterioration in the net working capital cycle and an increase in debt, leading to further deterioration in liquidity and consolidated credit profile could lead to a negative rating action.

COMPANY PROFILE

Incorporated in 1992, HPL manufactures electronic meters, low-voltage switchgears, protection devices, cables and lighting units.

FINANCIAL SUMMARY

Particulars (Consolidated)	9MFY20	FY19	FY18
Revenue (INR billion)	7.6	11.6	10.4
EBITDA (INR billion)	1.0	1.1	1.3
EBITDA margin (%)	12.8	11.5	10.6
Gross interest coverage (x)	2.1	2.3	2.1
Net financial leverage (x)	4.1	3.7	4.4
Source: HPL, Ind-Ra			

RATING HISTORY

Instrument Type	Current Rating/Outlook			Historical Rating/Outlook		
	Rating Type	Rated Limits (billion)	Rating	21 August 2019	29 March 2019	16 August 2017
Issuer rating	Long-term	-	IND BBB+/Stable	IND A-/Negative	IND A-/Negative	IND A/Stable
Fund-based working capital limits	Long-term/Short-term	INR4.75	IND BBB+/Stable/IND A2	IND A-/Negative/IND A1	IND A-/Negative/IND A1	IND A/Stable/IND A1
Non-fund-based working capital limits	Long-term/Short-term	INR7.45	IND BBB+/Stable/IND A2	IND A-/Negative/IND A1	IND A-/Negative/IND A1	IND A/Stable/IND A1
Commercial paper	Short-term	INR3.2	IND A2	IND A1	IND A1	IND A1
Term loan	Long-term	INR0.65	IND BBB+/Stable	Provisional IND A-/Negative	-	-

COMPLEXITY LEVEL OF INSTRUMENTS

For details on the complexity level of the instruments, please visit https://www.indiaratings.co.in/complexity-indicators.

SOLICITATION DISCLOSURES

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Applicable Criteria

Corporate Rating Methodology
Parent and Subsidiary Rating Linkage

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