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HPL Electric & Power coming with an IPO to raise upto Rs 416.70 crore

HPL Electric & Power

HPL Electric & Power is coming out with a 100% book building; initial public offering (IPO) of 2,06,28,571 shares of Rs 10 each in a price band Rs 175-202 per equity share.

Not more than 50% of the issue will be allocated to Qualified Institutional Buyers (QIBs), including 5% to the mutual funds. Further, not less than 15% of the issue will be available for the non-institutional bidders and the remaining 35% for the retail investors.

The issue will open for subscription on September 22, 2016 and will close on September 26, 2016.

The shares will be listed on BSE as well as NSE.

The face value of the share is Rs 10 and is priced 17.50 times of its face value on the lower side and 20.20 times on the higher side.

Book running lead managers to the issue are SBI Capital Markets, ICICI Securities and IDFC Securities.

Compliance Officer for the issue is Vivek Kumar.

Profile of the company

The company was incorporated as 'HPL-Socomec Private Limited' on May 28, 1992 as a private limited company under the Companies Act 1956, with the Registrar of Companies, National Capital Territory of Delhi and Haryana at New Delhi (the RoC). Pursuant to a resolution of its Board of Directors dated January 21, 2010 and a resolution of its shareholders dated February 18, 2010, the name of the company was changed to HPL Electric & Power Private Limited and a fresh certificate of incorporation was issued upon change of name by the RoC on March 10, 2010. Further, pursuant to conversion of the company to a public limited company, the name of the company was changed to 'HPL Electric & Power Limited' and a fresh certificate of incorporation consequent upon change of name on conversion to public limited company was issued by the RoC on December 14, 2015.

The company supplies its products through a network of authorized dealers or distributors to institutional, non-institutional and corporate customers. It supplies switchgears, lighting equipment and wires and cables, primarily through its pan-India authorized dealer network. The company's authorized dealers or distributors further sell its products to over 15,000 retailers in India. In addition, it supplies its products to Power Utilities, which primarily includes supply of meters under direct contractual arrangements to electricity boards and power distribution companies, as well as through project contractors. Further, the company supplies its portfolio of products to developers of residential and commercial building projects, OEMs and to industrial customers through a mix of direct sales and supply through its authorized dealer network.

The company also operates two tool rooms at Gurgaon (Haryana) and Kundli (Haryana), within its R&D Centres, where it has in-house component designing and tool designing facilities. The company currently owns and operates seven manufacturing facilities located across the states of Haryana and

Himachal Pradesh, having in-house testing capabilities, including one manufacturing facility owned and operated by its Subsidiary.

The Indian electrical equipment industry is immensely diversified, comprising manufacturing capabilities for high technology equipment on one hand, to low technology electrical components. The electrical equipment industry contributes 9.9% in value to the entire Indian manufacturing sector, translating to 1.4% of India's GDP. The Indian electrical equipment industry is estimated at grow at a CAGR of 8-12% during 2016-2020, varying across electrical equipment. Low tension (LT) electrical equipment such as switchgears, energy meters and wires and cables are expected to witness a faster growth in comparison to generation equipment. Further, the generation equipment segment is targeted to reach a size of Rs 125,000 crore and the transmission and distribution equipment (T&D Equipment) segment is targeted to reach a size of Rs 375,000 crore by 2022.

The Indian electrical equipment industry comprises power generation equipment and T&D Equipment. The power generation equipment includes boilers, turbines and generators, whereas T&D Equipment includes transformers, switchgears, transmission towers, wires and cables, energy meters and other equipment such as capacitors, instrument transformers and surge arrestors. T&D Equipment is further classified into high tension (HT) and LT electrical equipment. LV electrical equipment include LV switchgears such as air circuit breakers, moulded case circuit breakers (MCCB), changeover switches; LV control gear such as contactors, relays and capacitors; energy meters for household electricity metering purposes, panel meters for industrial metering purposes and utility meters; LT wires and cables used as part of industrial and commercial wiring; building wires and flexible wires used as part of residential wiring; lighting products such as compact fluorescent lamps (CFL), LED lamps, incandescent lamps; and residential and commercial protection devices such as miniature circuit breakers (MCB) and residual current device.

The electrical equipment industry, however, continues to face severe credit shortages, enormous delays, and non-adherence of payment terms by customers, primarily power utilities, resulting in severe cash flow problems across the industry. Further, the depreciating Rupee has made imports of critical raw materials and inputs for electric equipment manufacture more expensive. Moreover, due to the continued threat from imports of electrical equipment in the Indian market, domestic manufacturers have been forced to absorb this additional cost to remain competitive. Domestic manufacturers have in the past offered stiff competition from imports, particularly from China in the area of power plant equipment, engineering, procurement and construction services and substation contracts, including in areas of power generation turbo-machinery, HT switchgear, MCBs and lighting products.

Pros and strengths

Pan-India sales and distribution network: The company sells its products to institutional, non-institutional and corporate customers, including to developers of residential, commercial and industrial building projects, panel builders and OEMs, primarily through a network of over 2,400 authorized dealers or distributors who further sell its products to over 15,000 retailers, as on March 31, 2016, present throughout India. Additionally, the company supplies its products to Power Utilities, through direct contractual arrangements. For fiscal 2016, its revenue from sales to Power

Utilities contributed to 45.21% of its net consolidated revenue from operations and the balance revenue from operations was from sales through its authorized dealer network. Further, the company has over 90 branch offices and representative offices across India, as on March 31, 2016, which carry out marketing activities. Since the company invoices its products to its authorized dealers and recover the value of products sold directly from them prior to onward sales to the end-customer, this makes the company's revenue recovery process more efficient and reduces its credit cycle.

Robust manufacturing facilities: The company manufactures all its products within dedicated manufacturing facilities for each product vertical, as well as several components used in its products, with product customization capabilities for its institutional and corporate customers. It also undertakes testing of its products at its in-house testing facilities to ensure their quality. All its manufacturing facilities have been accredited with management system certificates for compliance with ISO 9001 requirements. Further, certain of its manufacturing facilities have been accredited with environmental system certificates for compliance with ISO 14000 requirements and with OHSAS 18001 certifications for implementing occupational health and safety management systems at such facilities. Presently, the company has seven manufacturing facilities located across the states of Haryana and Himachal Pradesh, including one manufacturing facility owned and operated by its Subsidiary. The company's manufacturing process capabilities include design and product development, component design, tool making and commercial production. As on March 31, 2016, its aggregate installed capacity for manufacture of meters was nine million, including that of the Himachal Energy Manufacturing Facility, switchgears was 16.51 million, for lighting equipment was 26 million and wires and cables was 194.40 million meters. The company has consistently undertaken expansion of its manufacturing facilities in the past with a view to capture increasing demand in the future. The company's manufacturing facilities enable it to expand its operations with ease to meet future demand at minimized cost of expansion. Additionally, the company's manufacturing facilities are equipped to manufacture customized products for its institutional customers and undertake modifications in its products for OEMs and other corporate customers.

Large product portfolio: Since its incorporation in 1992 as a B2B focused manufacturer of switchgears and allied electrical accessories, the company has significantly expanded its product portfolio. Its product portfolio comprises industrial and commercial electric equipment as well as domestic electric equipment, catering to requirements of a diversified customer base. Key products under its four product verticals include a range of air circuit breakers, MCCBs, MCBs, on-load changeover switches, control gear, modular switches, LED and non-LED bulbs and tubes, LED luminaires for domestic, commercial and industrial use, single and three phase meters, LTCT meters, prepayment meters, net metering, smart metering and transformer metering solutions with remote communication capabilities, domestic and industrial wires and specialty cables. Although the technical specifications for its products are largely standardized, it may undertake certain customization of certain products for its institutional and corporate customers. For instance, the company manufactures meters in accordance with specifications prescribed by the Power Utilities. It also undertakes modifications to its products for certain OEMs. The company's dedicated efforts towards expanding its product portfolio and its ability to identify its customers' requirements contribute significantly to its position in the electric equipment industry and has resulted in it becoming a one-stop shop for low voltage electric equipment. Further, the company's ability to adapt its electric equipment offerings to match the needs of its consumers across a wide range of industries gives it a competitive advantage in the market for electric equipment.

Established brand in the electric equipment industry: The company is established manufacturer of electric equipment in India and it manufactures and sells its products under the umbrella brand 'HPL'. It had the largest market share in the market for electricity energy meters in India, with one of the widest portfolios of meters in India, in fiscal 2015. The company's focus on maintaining quality across its product verticals and on continuous technological upgradation of its electric equipment offerings, together with its extensive sales and marketing efforts have enabled it to develop a strong brand recognition in the electric equipment industry. It enjoys significant brand recall and customer loyalty, particularly in the market for LV switchgear, allowing it to expand its presence across other ranges of domestic and industrial switchgear products. Further, the pre-qualifications and approvals the company has obtained from various Governmental Agencies that include central and state public works departments, municipal corporations and public sector undertakings, amongst others, reinforce the trust that its customers have in its products and their quality.

Risks and concerns

Significant portion revenue from Power Utilities: The company earns a significant portion of its revenue from sales of its products to Power Utilities, particularly its electronic metering solutions, pursuant to direct contractual arrangements with them. For fiscal 2016, fiscal 2015 and fiscal 2014, its revenue from sale to Power Utilities was 45.21%, 31.81% and 38.80% of the net consolidated revenue from operations for the respective periods. In particular, its sales to Power Utilities are based on submission of bids and grant of contracts, which may require it to offer its products at competitive prices to them. Even if its bid is successful, it may not receive orders within expected timelines or at all, which may negatively impact its annual production and sales plans. Submission of bids to Power Utilities also require it to provide bid guarantees to the Power Utilities, which are returned either upon receipt of an order from such Power Utility or in case its bid is unsuccessful. In case of a delay in closure of the bidding process or in receipt of an order for its products from the Power Utility, its bid guarantee will be blocked with the Power Utility, which may affect its working capital requirements.

High working capital requirements: The company's business requires significant amounts of working capital including for financing its raw material purchases and manufacturing its products before it receives payments from its customers. Further, the company's working capital requirements may increase if, contractual or sales terms do not include advance payments or if under such contractual arrangements, payment is stipulated at the time of delivery of the final product to its customer. The company's working capital requirements may also increase in the event it undertakes a larger number of orders due to the growth of its business. Moreover, Long working capital cycles, particularly due to delay in payments from its customers further increase its working capital requirements. Although, its annual sales policy and contract caps the credit cycle of such authorized dealers at 60 days, its authorized dealers may take up to 150 days to make payments. Further, the number of holding days required for realizing its trade receivables have increased during fiscal 2016, as compared to holding days required for realizing its trade receivables during fiscal 2015. It may be unable to adequately finance its working capital requirements on account of various factors, including extraneous factors such as increased interest rates, insurance or other costs, or borrowing and lending restrictions.

Geographical constraints: The company manufactures and supplies its products to customers in different geographies within and outside India from its facilities located in northern India, primarily in the state of Haryana and through one manufacturing facility located at Himachal Pradesh. Since, its entire revenue is currently from products manufactured at its manufacturing facilities located in Haryana and Himachal Pradesh, any disruption to its manufacturing facilities may result in production shutdowns. For instance, there have been communal agitations in various parts of Haryana in February 2016, due to which there was significant loss to infrastructure, shutdown of business and industry and damage to property in Haryana. Additionally, if its manufacturing facilities in Haryana or Himachal Pradesh are harmed or rendered inoperable by natural or man-made disasters, it may adversely affect its business, financial condition, result of operations and cash flows.

Stiff competition: The company operates in an increasingly competitive market. Increasing competition may result in pricing pressures and decreasing profit margins or lost market share or failure to improve its market position, any of which could substantially harm its business and results of operations. The company faces competition from other manufacturers, traders, suppliers and importers of electric equipment in relation to its offerings, in the organized and unorganized sectors. Suppliers in the electric equipment industry compete based on key attributes including technical competence, product quality, strength of sales and distribution network, pricing and timely delivery. While the company competitors in the organized sector focus more on technology and quality of their products, their unorganized counterparts supply their products at extremely competitive prices, which it may be unable to effectively compete with.

Outlook

HPL Electric & Power is an established electric equipment manufacturing company in India, manufacturing a diverse portfolio of electric equipment, including, metering solutions, switchgears, lighting equipment and wires and cables, catering to consumer and institutional customers in the electrical equipment industry. It currently manufactures and sells its products under the umbrella brand ‘HPL’, which has been registered in India since 1975. However, the company earns a significant portion of its revenue from Power Utilities and any delay in payment or disputes with these Power Utilities may have a material adverse effect on the company’s business and financial condition. The company has long working capital cycles and significant working capital requirements.

The issue has been offered in a price band of Rs 175-204 per equity share. The aggregate size of the offer is around Rs 361 crore to Rs 417 crore based on lower and upper price band respectively. Minimum application is to be made for 70 shares and in multiples thereon, thereafter. On performance front, the company has reported 7.40% growth in its topline at Rs 1244.99 crore in FY16 as compared to Rs 1159.23 crore in FY15, supported by strong growth of 15-16 percent in the revenue from sale of meters, lighting equipment and wires and cables. Moreover, the company’s restated profit after tax increased by 5.75%, from Rs 34.62 crore in fiscal 2015 to Rs 36.62 crore in fiscal 2016. The company’s balance sheet looked more attractive in 2016 as its quick ratio improved in FY16 at 0.76x as compared to 0.74x in FY15 and 0.71x in FY14, indicating the company’s liquid assets increasing to cover its short-term debt obligations.

The company seeks to continue to enhance brand awareness and customer loyalty through its promotion and marketing efforts. The company's pan-India presence and scale of operations allows it to increasingly focus on branding and promotional activities and enhance its visibility in the electric equipment industry. The company has reported a continuous growth in net sales from past 3-4 years and has generated RoE of 10% from past several years. The company is an established brand in the electric equipment industry and Pan-India sales and distribution network and large product portfolio make it a value play and a long term prospect.

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