July 28, 2022

Esmart Energy Solutions Limited: Ratings Reaffirmed, rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term: Fund based-Term Loan	38.00	35.25	[ICRA]BBB-(stable); reaffirmed
Long-term: Fund based – Cash Credit	2.00	7.00	[ICRA]BBB-(stable); reaffirmed/ assigned
Short-term: Non-fund based	20.00	60.00	[ICRA]A3; reaffirmed/ assigned
Total	**60.00**	**102.25**	

**Instrument details are provided in Annexure-1*

Rationale

The reaffirmation of the ratings continues to factor in Esmart Energy Solutions Limited's (EESL) proven track record in the energy efficiency sector, promoters' established experience in the electrical industry and a sound business model, which ensures relatively stable visibility of revenues and cash flows in the near to medium term for the executed contracts. Further, the ratings factor in EESL's comfortable capital structure (on provisional basis) with a gearing of 0.5 times as on March 31, 2022, and healthy coverage indicators with interest coverage of 13.0 times in FY2022, NCA/Total Debt of 87% and Total Debt/OPBDITA of 1.1 times in FY2022. The ratings also derive comfort from the strong order book position and presence of DSRA in the form of a quarter's principal and interest, along with unsecured loans, which supports the credit profile.

The ratings are, however, constrained by EESL's modest scale of operations and high working capital intensity owing to elongated receivable cycle and high inventory requirements. Given the projects undertaken are related to street light replacements, the counterparties are municipal bodies, wherein the payment cycle remains elongated due to the long approval process and slow recovery depending on the actual financial health of the municipal corporation. Further, the ratings are constrained by EESL's capital-intensive nature of business, wherein the company has moderate medium-term capex plan for future projects. Its ability to timely execute the same, with limited leveraging, to keep the capital structure and coverage indictors under check remains a key monitorable, going forward. ICRA also notes the ongoing litigation with Uniglobal Ventures LLP, Paisalo Digital Limited (erstwhile SE Investment) wherein EESL had given a corporate guarantee to Paisa Lo for the loan taken by Uniglobal Ventures LLP and the corporate guarantee was invoked. The same is under litigation and is an ongoing commercial dispute. ICRA, hence, will continue to monitor the developments in this regard and access its impact if any, on the credit profile of EESL, in case any material liability falls on EESL in case of unfavourable ruling against the company.

The Stable outlook reflects ICRA's expectations that EESL will benefit from the extensive experience of its promoters and its ability to execute upcoming projects in a timely manner, to scale-up its business profitably, through judicious funding mix. The promoters demonstrated past track record of supporting the entity in case of need and the stated objective of continuation of the same, going forward, remains a source of comfort.

Key rating drivers and their description

Credit strengths

Promoters proven experience in electrical industry, with demonstrated track record of operations – EESL is promoted by Mr. Suresh Shah, who has been associated with the electrical industry for more than four decades. The experienced management team with requisite professional set-up is led by CA Anand Prakash Rai, CEO of the company. The company, over the last five years, has successfully executed more than 12 projects for different municipal corporations across India.

Lack of upfront capex remains the unique selling proposition (USP); healthy operating margin – The company's operating margins have remained healthy in the range of 50-60% during the last three years owing to its sound business model, which is expected to provide long-term operational benefits. EESL follows an energy savings-based model, wherein the company finances the upfront capital cost of the project. It recovers the investment, along with operating costs through monthly payments from the customer under multi-year contracts, under a deemed savings approach. The lack of upfront capex requirements and savings from the energy efficiency projects for customers remain the key USP for EESL's projects.

Comfortable capital structure and healthy debt coverage indicators – EESL's capital structure remained comfortable with a gearing of 0.5 times as on March 31, 2022 (0.7 times as on March 31, 2021), due to healthy accretion to reserves. The debt coverage indicators stood healthy with interest coverage of 13.0 times in FY2022 (8.6 times in FY2021), NCA/Total Debt of 86.7% (50.2% in FY2021) and Total Debt/OPBDITA of 1.1 times as on March 31, 2022 (1.5 times in FY2021). Its total debt stood at Rs. 57.2 crore as on March 31, 2022, and consisted of term loans of Rs. 26.9 crore, interest-free unsecured loans of Rs. 30.3 crore and Rs. 0.04 crore of working capital borrowings. Its net worth increased to Rs. 112.4 crore as on March 31, 2022, from Rs. 72.8 crore as on March 31, 2020, supported by healthy cash accruals.

Diversified geographical presence and strong revenue book position – The company has strong relations with municipal corporations across India with presence in Delhi, Odisha, Punjab, Gujarat, Uttar Pradesh, Maharashtra and West Bengal. It had a strong revenue book of Rs. 891 crore as on March 31, 2022 spanning over next 10 years. In addition, EESL has submitted bids in Madhya Pradesh, Karnataka and Punjab for various projects, which would further improve its revenue book and geographical presence.

Credit challenges

Modest scale of operations – The company recorded healthy revenue growth during the last three years, with its top-line growing to Rs. 98.9 crore in FY2022 from Rs. 49.6 crore in FY2020 owing to additions of new projects over the years. The revenues are further expected to increase, going forward, with further additions of projects. Despite a healthy revenue growth over the years, the scale of operations remains modest at the absolute level.

High working capital intensity owing to elongated receivable cycle and inventory requirements – The company's working capital intensity was high at 63.5% in FY2022 owing to elongated receivable cycle and high inventory requirements. Given the exposure to municipal corporations, the payment period generally remains in the range of 90-120 days from the date of billing. It had high debtor days of 82 days with absolute receivables of Rs. 22.2 crore as on March 31, 2022, owing to slow recovery from municipal corporations, along with receivables for more than one year due to customer-specific issues for a few projects. However, the debtor days have improved as on March 31, 2022, from the earlier levels of 138 days in FY2021 owing to improved collections from the municipal corporations and will remain a key rating monitorable. The inventory period for the company remained high at 68 days for FY2022 (80 days in FY2021) as the funds are blocked for the entire construction period (generally four to five months) for a particular project. EESL imports raw materials such as LED diodes from Singapore and the US, lenses from Italy and other electrical components from South Korea and Singapore. The quantities ordered are small at a time and the payments are done upfront. Local purchases involve job work and purchase of electrical components with a credit period of 30-60 days.

Capital-intensive nature of business with moderate medium-term capex planned – Given the nature of upfront capex, which EESL must undertake, the business remains capital intensive. Further, it has moderate medium-term capex plans due to its upcoming bidding pipeline. Hence, the funding requirements would remain high in the near to medium term. The company expects to fund the entire capex by internal accruals. However, if required, it may opt for additional term loans. The generation of adequate internal accruals for FY2023 and FY2024 will remain crucial to meet its capex targets and reliance on debt is expected to be limited. Nonetheless, comfort can be drawn from the support extended by the promoters through unsecured loans and by the guarantees provided by SIDBI for term loans under partial-risk sharing facility for energy efficiency.

Foreign exchange fluctuation risk – EESL is exposed to foreign exchange fluctuation risks as the company imports few raw materials for manufacturing LED lights and the revenue profile is all local currency-based.

Liquidity position: Adequate

The company's liquidity position is adequate with free cash and liquid investments of ~Rs. 2.8 crore as on March 31, 2022. It has also maintained DSRA for three months of principal plus interest for majority of the term loans. Further, the average utilisation of fund-based limits is moderate at 70% of the sanctioned limits for the last 15 months ending in June 2022. Further, support can be drawn from the enhancement of working capital limits to Rs. 7.0 crore from Rs. 2.0 crore in March 2022. Also, enhancement of non-fund based limits to Rs. 60.0 crore from the earlier Rs. 15.0 crore draws further comfort towards submitting BG for future projects, with blocking 100% cash margin. EESL had interest-free unsecured loans to the extent of Rs. 30.3 crore as on March 31, 2022, from promoters, which are subordinated to bank loans, supporting its liquidity profile. It has sizeable long-term repayments and moderate capex plans in the near to medium term, which is expected to be funded by internal accruals. Comfort, however, can be drawn from the past support extended by the promoters in case of any exigency and the stated objective of continuing the same.

Rating Sensitivities

Positive factors – ICRA could upgrade EESL's ratings if it is able to scale-up its operations, while maintaining profitability levels, along with significant improvement in liquidity profile, through better receivables management. Further, timely completion of the planned projects without any cost and time overruns could also be a positive trigger.

Negative factors – Pressure on EESL's ratings could arise, in case of weakness in collections, adversely impacting its liquidity profile, or if any delay in execution of upcoming projects affects the top-line or profitability.

Analytical Approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology
Parent/Group support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of EESL. As on March 31, 2022, the company had five subsidiaries, which are all enlisted in Annexure-2.

About the Company

Esmart Energy Solutions Limited (EESL) was incorporated as Shah Investments Financials, Developments & Consultants Private Limited (SIFDCPL) as a private limited company under the Companies Act 1956 on November 29, 1979. SIFDCPL was mainly involved in investment activities, hire purchase, leasing, development of industrial units etc. SIFDCPL changed its name to Esmart Energy Solutions Limited in 2013 and entered the ESCO (Energy Saving Company) business with its own energy efficient LED light manufacturing set-up at Nashik, Maharashtra. EESL now focuses only on ESCO activities, security and surveillance, providing IT-based LED lighting solutions in municipal corporations on sharing the savings of energy basis.

EESL is primarily following the ESCO model, wherein EESL is replacing conventional streetlights with LEDs at its own costs with zero investment from municipal corporations. The subsequent reduction in energy and maintenance cost of a municipal corporation is used as revenue sharing for EESL. Most of the contracts are typically of 7-10 years, where EESL agrees on deemed energy saving and also provides maintenance of lights at no additional cost (in most cases). The company usually ensures 85% of energy saving efficiency.

Key financial indicators (Consolidated)

EESL Consolidated	FY2021	FY2022*
Operating income (Rs. crore)	85.8	98.9
PAT (Rs. crore)	18.6	25.3
OPBDIT/OI	56.0%	54.2%
PAT/OI	21.6%	25.5%
Total outside liabilities/Tangible net worth (times)	1.2	0.9
Total debt/OPBDIT (times)	1.5	1.1
Interest coverage (times)	8.6	13.0

*PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation * Provisional*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding as of Mar 31, 2022 (Rs. crore)	Current Rating (FY2023)	Chronology of Rating History for the past 3 years		
					Date & Rating in	Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020
					July 28, 2022	May 21, 2021	-	-
1	Cash Credit	Long-term	7.0	-	[ICRA]BBB-(Stable)	[ICRA]BBB-(Stable)	-	-
2	Term Loans	Long-term	35.25	26.9	[ICRA]BBB-(Stable)	[ICRA]BBB-(Stable)	-	-
3	Bank Guarantee	Short term	60.00	-	[ICRA]A3	[ICRA]A3	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long Term - Fund Based/ CC	Simple
Long Term - Fund Based TL	Simple
Short Term – Non-Fund Based – Bank Guarantee	Very Simple

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: www.icra.in

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Cash Credit	NA	NA	NA	7.00	[ICRA]BBB- (Stable)
NA	Term Loan-I	April 2019	NA	FY2025	5.52	[ICRA]BBB- (Stable)
NA	Term Loan-II	April 2019	NA	FY2025	5.55	[ICRA]BBB- (Stable)
NA	Term Loan-III	April 2019	NA	FY2025	5.82	[ICRA]BBB- (Stable)
NA	Term Loan-IV	November 2020	NA	FY2025	8.57	[ICRA]BBB- (Stable)
NA	Term Loan-V	March 2022	NA	FY2027	9.79	[ICRA]BBB- (Stable)
NA	Bank Guarantee	NA	NA	NA	60.00	[ICRA]A3

Source: *Company*

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

Annexure II: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Super Wealth Financials Private Limited	97.48%	Full Consolidation
US Instrument Private Limited	51.27%	Full Consolidation
Green Hydrocarbons India Private Limited	77.50%	Full Consolidation
DIMA Electro LLP	98.00%	Full Consolidation
DIMA Cable LLP	98.00%	Full Consolidation

Source: *Company*
Note: *ICRA has taken a consolidated view of the parent (EESL), its subsidiaries and associates while assigning the ratings.*

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ABOUT ICRA LIMITED

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