April 21, 2023(Revised)

Hindustan Aeronautics Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based limits	10,000.00	4,000.00	[ICRA]AAA (Stable); reaffirmed
Non-fund-based limits	2,050.00	2,050.00	[ICRA]A1+; reaffirmed
Total	**12,050.00**	**6,050.00**	

**Instrument details are provided in Annexure-I*

Rationale

The ratings reaffirmation factors in the improvement in Hindustan Aeronautics Limited's (HAL) working capital position, healthy order inflows with an outstanding order book worth Rs. 82,000 crore as on March 31, 2023, providing high revenue visibility in the medium to long term, while indicating HAL's strong competitive and strategic positioning. HAL realised significant payments from its clients in FY2022, which continued in 9M FY2023. Consequently, the external debt has been fully repaid with a healthy cash balance and liquid investments of Rs. 16,113 crore as on December 31, 2022.

The ratings continue to draw comfort from the diversified revenue mix of HAL, covering the sale of products, spares and services for multiple aircraft programmes. It has a strong financial profile, characterised by healthy profit margins, and return indicators, nil borrowings, and a strong liquidity profile. These strengths are offset to some extent by HAL's continued high dependence on the defence sector, which contributes to the bulk of its revenues. ICRA notes that while the company is trying to diversify its revenue base by increasing the share of orders from other clients and exports, however, their contribution remains low.

The ratings factor in the majority ownership held by the Government of India (GoI) in HAL and its strategic position as a dominant supplier of aircrafts, helicopters, engines, avionics, and accessories as well as main provider of maintenance, repair, and overhaul (MRO) services to the Indian defence forces. The company faces limited competition from the private sector due to high capital intensity and long gestation periods for developing manufacturing capabilities in the sector. Though competition from the private sector is likely to intensify in the medium term, HAL's established track record and large manufacturing capacities with adequate pool of trained manpower and focus on research and development (R&D) will continue to be strong mitigating factors. The GoI's increased focus on indigenisation with the Make in India policy and mandatory offset policy for defence procurement by GoI, augur well for the company's future growth.

The ratings also factor in the company's exposure to risk of time and cost overruns as orders have stiff execution timelines and predefined margins. Any material cost overruns attributable to delays on HAL's front could impact its overall profitability. However, the liquidity profile remains supported by the healthy cash balances and strong financial flexibility with adequate access to bank credit to tide over times of delays in collection receipts. The ratings consider HAL's exposure to high dependence on contracts received from the Ministry of Defence (MoD), which contributes to more than 90% of the revenues. The company remains susceptible to timely receipt of funds or change in prioritisation in the defence budget, which can have an adverse impact on its growth potential, sales momentum, and liquidity position. HAL manages its working capital intensity partly by aligning its payables to contract receivables and availing mobilisation advances, reflecting in high total outside liabilities/tangible net worth (TOL/TNW) ratio of 1.7 times as on March 31, 2023. Nevertheless, long-standing relationship with key vendors/OEMs with back-to-back arrangements and majority orders being backed by MoD, wherein advances are provided without any financial bank guarantees, provides comfort.

ICRA notes that the company also has significant contingent liabilities, primarily relating to sales tax demands from various states, aggregating to Rs. 1,558 crore as on March 31, 2022. Any crystallisation of these liabilities or significant future outflows in terms of buy-back of shares/dividends, that can adversely impact its liquidity, remains a key monitorable.

The Stable outlook on the [ICRA]AAA rating reflects ICRA's opinion that HAL will continue to benefit from its strategic importance to the Indian defence forces, strong financial flexibility, high entry barriers and long track record of operations.

Key rating drivers and their description

Credit strengths

Majority ownership held by GoI; strategically important to the Indian defence forces – The GoI is HAL's majority shareholder, holding a 75.15% stake as on March 31, 2023. HAL is a defence PSU, which was conferred Navaratna status in 2007. It is of strategic importance to the Indian defence forces comprising the Indian Army, Indian Airforce, Indian Navy, and Indian Coast Guard, on account of it being the sole domestic supplier of aircrafts, helicopters, engines, avionics, and other accessories. It occupies a leadership position in the Indian aerospace and defence industry. Over the years, it has showcased its research, design, and development capabilities with the successful development of military aircraft and helicopters. It also provides MRO services for these indigenous and license manufactured aircraft and helicopters, as well as for aircraft and helicopters procured directly by the Indian defence services. The company faces limited competition from the private sector due to the high capital intensity and long gestation periods for developing manufacturing capabilities in the sector.

Strong order book with healthy future order pipeline – The company has healthy order inflows with an outstanding order book of Rs. 82,000 crore as on March 31, 2023, providing high revenue visibility in the medium to long term, while also indicating HAL's strong competitive and strategic positioning. Further, there is a strong visibility of future orders with new orders anticipated for LUH, LCH, Su-30, HTT-40 in the near to medium term.

Strong financial profile and continued improvement in working capital position – HAL has a strong financial profile, characterised by healthy profit margins, and return indicators, nil borrowings, and a strong liquidity profile. It realised significant payments from its clients in FY2022, which continued in 9M FY2023. Consequently, the external debt has been fully repaid with a healthy cash balance and liquid investments of Rs. 16,113 crore as on December 31, 2022.

Credit challenges

High dependence on contracts from MoD – More than 90% of the company's revenue is derived from sales to the Indian defence forces. ICRA notes that while the company is trying to diversify its revenue base by increasing the share of orders from other clients and exports, however, their contribution remains low.

Susceptibility to time and cost overruns in order execution – The company's operations and profitability remain exposed to time and cost overruns as orders have stiff execution timelines and predefined margins. Any material cost overruns attributable to delays on HAL's front could impact its overall profitability. HAL manages its working capital intensity partly by aligning its payables to contract receivables and availing mobilisation advances, as reflected by high total outside liabilities/tangible net worth (TOL/TNW) ratio of 1.7 times as on March 31, 2023. Nevertheless, long-standing relationship with key vendors/OEMs with back-to-back arrangements and majority orders being backed by MoD, wherein advances are provided without any financial bank guarantees, provides comfort.

Environment and Social Risks

Environmental considerations: HAL, operating in the defence equipment manufacturing industry, requires various raw materials and entails sizeable energy and water requirements for running its multiple facilities. To safeguard the environment against the impact of its operations, and possible regulatory action for violation of applicable environmental laws, it has tied up with various State Pollution Control Board (SPCB) authorities for appropriately disposing/recycling solid hazardous waste.

Social considerations: HAL has a dependence on human capital and hence, retaining talent, maintaining healthy employee relations, as well as supplier ecosystem remain essential for disruption-free operations. Going forward, the company's ability to manage risks related to safety in the areas of process, and occupational health, while developing safety leadership capabilities, will remain a key factor from the social consideration perspective.

Liquidity position: Strong

HAL's liquidity is strong, as evidenced by its cash balance and liquid investment of Rs. 16,113 crore as on December 31, 2022, undrawn working capital facilities worth Rs. 4,000 crore and absence of debt repayment obligations over the near term. Further, the capex commitments are expected to be met through internal accruals and no debt-funded capex is envisaged in the near term.

Rating sensitivities

Positive factors – Not applicable.

Negative factors – Negative pressure on HAL's ratings could arise in the case of an adverse impact on liquidity due to stretched debtors or crystallisation of contingent liabilities leading to significant dependence on external borrowings. Any change in strategic importance of HAL to the GoI reflecting in lower order inflows and revenues could also increase pressure on ratings.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating approach – implicit support from parent or Group Rating approach consolidation
Parent/Group support	Parent/Group Company: Government of India (GoI) The assigned ratings factor in the strategic importance that HAL holds for the GoI, which is expected to extend timely financial support to the rated entity, should there be a need
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of HAL. As on March 31, 2022, the company had 14 joint ventures and two subsidiaries, which are all enlisted in Annexure II.

About the company

HAL, a defence public sector undertaking (DPSU), was established on October 1, 1964, when Hindustan Aircraft Limited and Aeronautics India Limited were amalgamated. The principal business of HAL is to undertake design, development, manufacturing, maintenance, repair, overhaul, and servicing of products like aircraft, helicopters, engines and other related systems like avionics, instruments, and accessories. It also engages with the Indian Space Research Organisation (ISRO) to contribute to the space programmes of the country. The GoI remains HAL's largest shareholder, with a current shareholding of around 75%. HAL was conferred with the Navratna PSU status in June 2007. Its primary consumers are the Indian Defence Forces comprising the Indian Air Force, Indian Army, Indian Navy, along with the Indian Coast Guard. The company has five production complexes – Bangalore complex, MiG complex (located in Nasik and Koraput), Helicopter complex (located in Bangalore and Barrackpore), Accessories complex (located in Kanpur, Lucknow, Hyderabad, Kasargod and Korwa), and a Design complex (R&D centres) jointly located with the related manufacturing divisions.

Key financial indicators (audited)

HAL Consolidated	FY2021	FY2022	9M FY2023
Operating income	22,755	24,620	14,433
PAT	3,234	5,080	2,970
OPBDIT/OI	23.5%	22.0%	23.7%
PAT/OI	14.2%	20.6%	20.6%
Total outside liabilities/Tangible net worth (times)	2.4	2.0	NA
Total debt/OPBDIT (times)	0.0	0.0	0.0
Interest coverage (times)	20.6	93.0	NA

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs. crore; NA – not available

Source: Company

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2024)				Chronology of Rating History for the Past 3 Years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding as on December 31, 2022 (Rs. crore)	Date & Rating in	Date & Rating in FY2023	Date & Rating in FY2022		Date & Rating in FY2021
					Apr 21, 2023	Jan 25, 2023	Jan 14, 2022	Apr 29, 2021	July 02, 2020
1	**Fund-based limits**	Long term	4,000.00	Nil	**[ICRA]AAA (Stable)**	**[ICRA]AAA (Stable)**	**[ICRA]AAA (Stable)**	**[ICRA]AA+ (Positive)**	**[ICRA]AA (Stable)**
2	**Non-fund-based limits**	Short term	2,050.00	NA	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**
3	**Commercial Paper**	Short term	-	Nil	-	**[ICRA]A1+; Withdrawn**	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**

Complexity level of the rated instruments

Instrument	Complexity Indicator
Fund-based limits	Simple
Non-fund-based limits	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: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Fund-based limits	NA	NA	NA	4,000.00	[ICRA]AAA (Stable)
NA	Non-fund-based limits	NA	NA	NA	2,050.00	[ICRA]A1+

Source: Company

Annexure II: List of entities considered for consolidated analysis

Company Name	HAL Ownership	Consolidation Approach
Naini Aerospace Limited	100.00%	Full Consolidation
Indo Russian Helicopters Limited	50.5%	Full Consolidation
BaeHAL Software Ltd.	49.0%	Equity Method
Indo Russian Aviation Ltd.	48.0%	Equity Method
Safran HAL Aircraft Engines Pvt. Ltd.	50.0%	Equity Method
Samtel HAL Display System Ltd.	40.0%	Equity Method
HAL-Edgewood Technologies Pvt. Ltd.	50.0%	Equity Method
HALBIT Avionics Pvt. Ltd.	50.0%	Equity Method
Infotech HAL Ltd.	50.0%	Equity Method
HATSOFF Helicopter Training Pvt. Ltd.	50.0%	Equity Method
TATA-HAL Technologies Ltd	50.0%	Equity Method
International Aerospace Manufacturing Pvt. Ltd.	50.0%	Equity Method
Multi-Role Transport Aircraft Ltd.	50.0%	Equity Method
Aerospace & Aviation Sector Skill Council (AASSC)	50.0%	Equity Method
Helicopter Engines MRO Private Ltd.	50.0%	Equity Method
Defence Innovation Organisation	50.0%	Equity Method

Source: HAL

Corrigendum

Rationale dated April 21, 2023 has been revised with inclusion of environment and social risks on page number 2 and 3

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