VA Tech Wabag Limited

February 22, 2019

Summary of rating action

Instrument*	Previous Rated Amount (Rs. Crore)	Current Rated Amount (Rs. crore)	Rating Action
Long Term: Fund based facilities	500.0	500.0	[ICRA]A+ (Negative); revised from [ICRA]AA- (Negative)
Long Term / Short term: Non fund based facilities	3058.5	3058.5	[ICRA]A+ (Negative) / [ICRA]A1+; revised from [ICRA]AA- (Negative) / [ICRA]A1+
Long Term / Short term: Proposed facilities	441.5	441.5	[ICRA]A+ (Negative) / [ICRA]A1+; revised from [ICRA]AA- (Negative) / [ICRA]A1+
Total	**4000.00**	**4000.00**	

Rationale

The downward revision of the long term rating and the reaffirmation of the 'Negative' outlook factors in the continued delays in receipt of receivables from Andhra Pradesh and Telengana state discoms (APGENCO & TSGENCO) for the Balance of Plant (BoP) orders being executed, though, post the State Elections, the company is hopeful of receiving the retention money from TSGENCO in next 2 months. The reaffirmation of short term rating also takes into account of likely receipt of advances with large sized orders received by the company in last few months. The ratings also consider the pressure on margins on consolidated basis and higher interest cost because of working capital borrowings in Indian operations.

The company's reliance on working capital debt has been minimal traditionally, indicating its ability to execute projects through customer advances and back-to-back credit period from suppliers. While the company's working capital intensity in NWC/OI (Net working capital / Operating Income) has increased from 17% in FY 2014 to 36% in FY2018, the same has been funded partly through usage of cash available and borrowings. This increase has largely been due to the execution of the BoP contracts and the resultant accumulation of receivables / retention monies. This has resulted in an increase in the consolidated net debt levels, though the gearing level still remains comfortable.

The ratings also take into account the vulnerability of the profitability to competitive pressures, incidence of liquidated damages, warranty payouts and potential adverse litigation/arbitration outcomes. The various provisions[1] made towards doubtful debts, liquidated damages, warranties & contract losses have thus restricted the consolidated operating margin over the years. Though there has been a noticeable improvement in the profitability of some European entities, through various cost rationalization measures, large losses in other subsidiaries and JVs in the last few years have stressed the consolidated profitability.

The rating however continues to reflect the healthy consolidated order book position of the company at Rs 8,361 crore (excluding framework orders) as of December 2018, aided by company's established position in the water infrastructure business with its strong technical capabilities arising out of execution track record, ownership of product and process patents as well as experienced promoters & management. The ratings also take into account the favourable long-term

[1] Provisions for bad debts, LDs and warranties made year on year based on the company's accounting policy

demand prospects for water/waste-water projects in the company's target markets. Though the overall receivables position has increased essentially on account of the BOP projects in power segment, the company has stated its intention of focusing only on the core business in water and waste treatment EPC business wherein ICRA notes that its execution capabilities & ability to manage the receivables has been very satisfactory.

Outlook: Negative

ICRA believes Wabag's credit profile will remain weighed down by the receivables from the APGENCO / TSGENCO orders and the associated working capital borrowings. The outlook may be revised to 'Stable' if there is significant progress for collections on the receivables as well as in terms of the receipt of advances on the orders received.

Key rating drivers

Credit strengths

Established position of the Company as the market leader in the domestic water/waste-water treatment project execution business – Wabag group has a strong technological background, with the Austrian subsidiary having technical know-how/patents and with technically experienced key management personnel. Hence the company has grown into a large multinational player in the water space with a large presence in many geographies. The long term potential for water & waste treatment projects from municipal and industrial users is also favourable in the company's target markets which include Middle East, North Africa, Eastern/Central Europe apart from India.

Healthy orderbook position at consolidated level – Wabag's orderbook continues to be healthy following from its technological competitiveness and leading market position in India and key overseas geographies. The company has a diverse orderbook with projects across EPC, O&M, Municipal and Industrial segments and has a good geographical mix of orders. The company has secured Rs 3567 crore of new order in the 9 month period till December 2018 which provides strong revenue visibility given that the earlier larger orders which contributed majority of the revenues – such as Petronas – have reached completion stage

Credit challenges

Significant increase in the overall working capital intensity due to large receivables from APGENCO / TSGENCO – The Company's debtor levels continue to remain high due to delays in payments by some clients and higher amounts held as retention for completed projects. Further, the pending amounts with APGENCO for the BoP projects have resulted in a worsening of the ageing profile of the receivables. The back-to-back credit arrangement for supplies mitigates the risk to an extent. The company had cash balances of Rs 409 crore in March 2016 owing to the healthy accretion over the years and management of working capital requirements through creditor support. However, this has declined to Rs 190 crore in March 2018 and hence the net debt levels have increased.

With exclusion of the long pending receivables from the Drawing Power calculation for the working capital facilities, the company would be required to fund the gap through either customer inflows from other ongoing projects or medium to long term funding in the form of NCDs.

Margins vulnerable to provision outgo and risks associated with overseas operations – Stringent contractual terms like liquidated damages and warranty obligations restrict the profitability. In addition, some of the key overseas subsidiaries have been impacted by high cost of operations which has in turn had an impact on consolidated profitability. The Indian operations have also seen a decline in the profitability owing to the execution of low margin orders like APGENCO and increase in competitive pressures in the recent years following the attractiveness of the sector. However, with the BoP projects having been mostly completed and with sizeable new orders in the orderbook, the management expects the profitability to improve going forward.

High Total Outside Liabilities and Contingent liabilities relative to the Net Worth of the Company – Though the company has had minimal borrowings traditionally, the working capital has been funded mostly through supplier credit and hence the overall outside liabilities continues to remain high relative to the net worth position. Also, the contingent liabilities have been typically higher due to issuance of guarantees towards contract performance and borrowings of subsidiaries. However, the contingent liability exposure has moderated following the extinguishment of liabilities towards the Oman project.

Liquidity Position:

The company's liquidity position has been affected owing to the large amounts pending from the Balance of Plant contracts of APGENCO / TSGENCO. However, the company is hopeful of receiving the retention money from TSGENCO in next 2 months and the rest for APGENCO project to come in two tranches over the next 18 month period. The increase in working capital intensity has also resulted in depletion of the healthy cash reserves held by the company till recently. The liquidity profile of the company would be thus contingent on timely receipt of the retention amounts on BoP projects as well as progress on the receipt of advances for the large sized orders won by the company in last few months.

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 VA Tech Wabag Limited.

About the company:

Incorporated in 1996, Wabag is in the business of providing turnkey solutions for water and waste water treatment to municipal and industrial segments. The company undertakes turnkey contracts for design, engineering, procurement, construction, erection, commissioning and operation and maintenance of water and waste water treatment plants. The company has seen considerable changes in its ownership pattern since its inception as a water division of Blacke Durr Cooling Towers Ltd – a part of Deutsche Babcock AG, Germany (DBAG) in October 1996. Following the acquisition of DBAG by VA Tech AG, Austria in April 1999, VA Tech Wabag GmbH, Austria (Wabag Austria) was incorporated and its Indian operations became known as VA Tech Wabag Limited, (Wabag) being a 100% subsidiary of Wabag Austria. Later, Wabag, Austria was taken over by Siemens AG, Germany in July 2005 and as a result, Wabag Austria (excluding India operations) became a part of Siemens AG, Germany. In September, 2005, the company's management team and ICICI Ventures bought out the majority stake (82.9%) in Wabag's India operations. Subsequently in September 2007, Wabag India acquired its ex-parent, i.e., Wabag Austria from Siemens. With this acquisition Wabag Austria and its subsidiaries became subsidiaries of the company and Wabag on a consolidated basis has presence across North Africa, Middle East, Far East-China, and South East/Central/Eastern Europe.

In 9month FY2019, on a consolidated basis the company reported net profit of Rs. 54.8 crore on an operating income of Rs. 2102.4 crore as against net profit of Rs. 83.6 crore on an operating income of 2422.8 crore in the corresponding period of FY 2018.

Key financial indicators (audited)

	FY 2017	FY 2018
Operating Income (Rs. crore)	3207.9	3457.3
OPBDIT (Rs. crore)	296.6	291.8
PAT (Rs. crore)	112.2	144.5
OPBDIT/ OI (%)	9.2%	8.4%
PAT/OI (%)	3.5%	4.2%
Total Debt/ TNW (times)	0.32	0.41
Total Debt/ OPBDIT (times)	1.06	1.64
Interest coverage (times)	5.64	5.06

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

		Current Rating (FY2019)						Chronology of Rating History for the past 3 years				
					Date & Rating			Date & Rating in FY2018			Date & Rating in FY2017	Da Rat FY2
	Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs Crore)	Feb 2019	Jul 2018	Jul 2018	Mar 2018	Oct 2017	Oct 2017	Feb 2017	Feb
1	Fund based facilities	Long Term	500.0	-	**[ICRA]A+ (Negative)**	**[ICRA]AA- (Negative)**	**[ICRA]AA- (Negative)**	**[ICRA]AA- (Stable)**	**[ICRA]AA- (Stable)**	**[ICRA]AA- (&); Rating watch with developing implications**	**[ICRA]AA- (Stable)**	**[IC (St**
2	Non fund based facilities	Long Term / Short Term	3058.5	-	**[ICRA]A+ (Negative) / [ICRA]A1+**	**[ICRA]AA- (Negative) / [ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+; Rating watch with developing implications**	**[ICRA]A1+**	**[IC**
3	Unallocated	Long Term / Short Term	441.5	-	**[ICRA]A+ (Negative) / [ICRA]A1+**	**[ICRA]AA- (Negative) / [ICRA]A1+**	**[ICRA]A1+**	-	-	-	-	-

Complexity level of the rated instrument:

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

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	Cash Credit	NA	NA	NA	500.0	[ICRA]A+ (Negative)
NA	Bank Guarantees / Letter of Credit	NA	NA	NA	3058.5	[ICRA]A+(Negative) / [ICRA]A1+
NA	Unallocated, Short Term	NA	NA	NA	441.5	[ICRA]A+(Negative) / [ICRA]A1+

Source: VA Tech Wabag Limited

Annexure-2: List of entities considered for consolidated analysis

Company has consolidated the subsidiaries/step down subsidiaries using full consolidation/proportionate consolidation and used equity method for associates and JVs

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About ICRA Limited:

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