November 01, 2022

Finolex J-Power Systems Limited: Ratings assigned

Summary of rating action

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Long term- Fund based- Working capital limits	105.00	[ICRA]BBB-(Stable); assigned
Long term – Term loan	11.46	[ICRA]BBB-(Stable); assigned
Short term- Non-fund based	39.00	[ICRA]A3; assigned
Long term/Short term-unallocated Limits	5.58	[ICRA]BBB-(Stable)/[ICRA]A3; assigned
Total	**161.04**	

**Instrument details are provided in Annexure-I*

Rationale

The assigned ratings take into account Finolex J-Power Systems Limited's (FJPS) operational synergies with its parent entities – Japan-based J-Power Systems Corporation (JPS)and Finolex Cables Limited (FCL) - and the benefits derived from their technical strengths and market presence. JPS is a wholly-owned subsidiary of Sumitomo Electric Industries or SEI, rated A2 by Moody's Investors Services. The parent entities have demonstrated a track record of financial support in the form of regular equity infusion, besides corporate guarantees for availing bank facilities. The company manufactures underground cables for the extra-high voltage (EHV) segment, which is a niche segment that is less competitive than overhead cables because of the specific requirement in terms of quality, technical parameters and high gestation period.

The ratings consider the favourable medium-term demand prospects from various end-user sectors, especially state utilities, metro rail corporations and private players that have captive power plants. The company reported a healthy order book position of Rs. 254.5 crore as on August 31, 2022, with L1 pipeline of over Rs. 120-130 crore, providing strong medium-term revenue visibility. The company's capital structure remains comfortable with a gearing of 0.5 times as on March 31, 2022, supported by equity infusion by the parent companies on a regular basis, notwithstanding the cash losses in the previous years.

The ratings, however, are constrained by the weak financial profile with revenues remaining in the range of Rs. 30-90 crore in the last five years, mainly due to the weak order book position on account of high gestation period, lumpy order flows and hurdles in execution. FJPS reported losses at the operating and cash level and weak coverage indicators in the past five years and has needed liquidity support from its parent entities regularly. Nevertheless, an improved order book position provides revenue visibility in the near to medium term that would also enable the company to turn profitable in FY2024.

The ratings consider the vulnerability of FJPS's profitability to raw material price variations, where the execution timeline may be longer (within 6-18 months), as a significant part of its contracts are fixed price in nature. Considering the project nature of the business, the company's revenues exhibit lumpiness with an elongated working capital cycle due to the long execution period of projects, milestone-based payments and the retention money requirement. FJPS faces competition from few large and established players in the cable industry.

The Stable outlook reflects ICRA's opinion that FJPS's revenue and accruals will be supported by its comfortable order book along with expectations of a healthy order inflow in the near to medium term. Also, continued financial and operational support is expected from the parent companies.

Key rating drivers and their description

Credit strengths

Strong operational synergies with parent and track record of financial support–FJPL, being a joint-venture (JV, 51:49) between Japan based J-Power Systems corporation (JPS) and Pune-based Finolex Cables Limited (FCL), receives financial support in the form of regular equity infusions as well as corporate guarantees for its bank facilities. The parent companies have already infused Rs. 209.5 crore in the last five years till FY2022. Further, in FY2023, Rs. 22.5 crore of equity infusion is planned by October-November 2022. Apart from the financial support, the company gets technical support from J-Power Systems Corporation and execution support from Finolex Cables Limited. Further, the parent companies also provide co-guarantee for certain projects where such bank guarantees are required.

Presence in niche segment along with strong demand prospects- The company manufactures underground cables in the EHV segment, which is a niche segment and remains less competitive than overhead cables mainly due to the specific qualifications in terms of quality, technical parameters and time of execution. Further, the gestation period remains high in this segment with around 5-8 years to get the concrete orders and 1-1.5 years to get the cables approved for certain quality parameters, also known as pre-qualification (PQ) tests that entail rigorous long duration tests. The high gestation period makes the business capital-intensive which acts as an entry barrier for new players. The demand prospects in this segment remains strong with large tenders expected from various state utilities, especially in cyclone-driven areas, for converting overhead cables to underground cables in the next few years. Further, as per the Revamped Distribution Sector Scheme (RDSS), a healthy demand of cables is expected from the Government, providing significant growth opportunities to the company.

Order book position provides healthy revenue visibility- – FJPL's order book stood at Rs. 254.5 crore as on August 31, 2022, along with an L1 pipeline of over Rs. 120-130 crore, providing strong medium-term revenue visibility. The order intake in 5M FY2023 was healthy at Rs. 176.5 crore. Currently, the company is witnessing healthy demand from various end-user sectors, especially state utilities, metro rail corporations and private players which need captive power plants. However, the completion of the projects within the agreed timelines while maintaining the desired quality parameters is critical to minimise the liabilities arising from project delays and performance issues.

Comfortable capital structure supported by funds infused by parent companies- The capital structure of the company remained comfortable with gearing of 0.5 times as on March 31, 2022, supported by regular equity infusion by the parent companies. The parent companies have infused Rs. 209.5 crore in the last five years till FY2022 along with Rs. 22.5 crore of equity, planned to be infused by October-November 2022.

Credit challenges

Weak financial risk profile with losses at operating level- The financial profile is characterised by a weak operating income, which remained in the range of Rs. 30-90 crore in the last five years mainly due to a weak order book position on account of high gestation period which limited the order inflow. Further, at the operating level, the company has been reporting losses. The coverage indicators also remained weak due to the losses at the operating level. Nevertheless, the operating income is expected to improve in FY2023 with a healthy order book position. However, for FY2023, the revenues were lumpy with the company achieving a turnover of Rs. 24 crore till August 31, 2022 due to delays in receiving necessary approvals even as it expects to scale up significantly in H2 FY2023. The order book position as of August 22 was Rs. 254 crore i.e., 3 times the FY2022 operating income, providing comfortable revenue visibility in the near to medium term.

High working capital intensity in EPC business- The working capital intensity remains inherently high in the EPC business due to the long execution period of projects, milestone-based payments and the retention money requirement. As a result, the company's overall debtor days remained high at around 183 days in FY2022, though improved from the previous fiscal (PY: 390 days). The debtor days are on the higher side as the receivables include retention money of projects and contract assets.

The working capital position is, however, supported to some extent by creditor days. A high working capital intensity is further evident from the net working capital/operating income of 121.9% in FY2022 (PY: 217%). This also led to full utilisation of working capital limits and therefore any additional working capital requirement is expected to be supported by funding from parent companies along with timely enhancement in working capital limits.

Competition from large established players- Though the company works in a niche segment and manufactures cables in the high-voltage range of 66kV to 500 kV, it faces competition from a few large and established players. For 220kV, the company faces major competition from KEI Industries Limited, KEC International Limited, LS cable and Systems, Universal Cables. For 400kV cables, the company has Universal Cables Limited as a rival. Nevertheless, the company has created its own niche in this segment with specialisation in EHV cables along with state-of-the-art facility with VCV line which provides better quality output.

Margins vulnerable to volatile raw material prices- Aluminum and copper, the key raw materials for cable manufacturing, forms a major part of the raw material cost. Given the long order execution period of about 6-18 months, the operating margin remains vulnerable to the volatility in the prices of key raw materials, particularly for contracts that are generally fixed price in nature. Nonetheless, the risk is mitigated to some extent by the commodity price hedging undertaken by the company.

Liquidity position: Stretched

FJPL's liquidity is stretched, reflected in the high utilisation of the working capital limit in the last 12 months. The liquidity of the company is supported by the equity infusion by parent companies, as and when required. Timely enhancement of working capital limits and fund infusion by the parent companies to support its liquidity position remain the key rating monitorables.

Rating sensitivities

Positive factors – ICRA could upgrade the ratings if FJPL demonstrates an improvement in its revenues, profits, coverage metrics, on a sustained basis, while improving its liquidity position.

Negative factors – ICRA could downgrade FJPL's ratings if any further delay in the execution of orders in hand reduces the turnover and profitability. Additionally, any weakening of the liquidity position or a stretch in the receivable position could have a negative impact on the ratings. This apart, ICRA could downgrade FJPL's ratings if there is a major deterioration in the parent company's financial profile or weakening of linkage with the parent company.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating approach-Implicit support from parent or group
Parent/Group support	Operational and financial support from being a part of Sumitomo Electric Industries Ltd., being the ultimate parent
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the standalone financials of FJPS

About the company

Finolex J-Power System Limited (FJPS) is a joint venture (51:49) between Japan-based J-Power Systems Corporation (JPS) and Pune-based Finolex Cables Limited (FCL). FJPL was formed to manufacture and sell high-voltage and extra high-voltage power cables (underground cables), ranging from 66kV to 500kV grade, and other power accessories along with providing turnkey solution cables to the Asian market. However, as of now, the company is working towards catering to the Indian market and will later focus on the larger Asian market. It has the exclusivity to manufacture EHV cables with FJPL under the joint venture agreement.

Key financial indicators (audited)

FJPSL Standalone	FY2021	FY2022
Operating income	49.8	86.3
PAT	-31.3	-27.2
OPBDIT/OI	-26.0%	-10.3%
PAT/OI	-63.0%	-31.6%
Total outside liabilities/Tangible net worth (times)	0.5	0.7
Total debt/OPBDIT (times)	-5.3	-9.3
Interest coverage (times)	-1.3	-0.9

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2023)				Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding as on Jul 30, 2022 (Rs. crore)	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021	Date & rating in FY2020
					Nov 01, 2022	-	-	-
1	**Fund based-Working capital limits**	Long term	105.00	-	[ICRA]BBB-(Stable)	-	-	-
2	**Term loan**	Long term	11.46	11.46	[ICRA]BBB-(Stable)	-	-	-
3	**Non-fund based**	Short term	39.00	-	[ICRA]A3	-	-	-
4	**Unallocated**	Long term/Short term-	5.58	-	[ICRA]BBB-(Stable)/[ICRA]A3	-	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long term- Fund based- Working capital limits	Simple
Long-term – Term loan	Simple
Short term- non-fund based	Very Simple
Long term/Short term-Unallocated Limits	NA

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	**Long term- Fund based- Working capital limits**	NA	NA	NA	105.00	[ICRA]BBB-(Stable)
NA	**Long-term – Term loan**	FY2022	NA	FY2025	11.46	[ICRA]BBB-(Stable)
NA	**Short term- non-fund based**	NA	NA	NA	39.00	[ICRA]A3
NA	**Long term/Short term- Unallocated Limits**	NA	NA	NA	5.58	[ICRA]BBB-(Stable)/[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 – Not Applicable

ANALYST CONTACTS

Sabyasachi Majumdar
+91 124 4545 304
sabyasachi@icraindia.com

Girishkumar Kadam
+91 22 6114 3441
kinjal.shah@icraindia.com

Anupama Arora
+ 91 124 4545 303
anupama@icraindia.com

Menka Sabnani
+91 79 4027 1562
menka.sabnani@icraindia.com

RELATIONSHIP CONTACT

Jayanta Chatterjee
+91 80 4332 6401
jayantac@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

ICRA Limited

Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001
Tel: +91 11 23357940-45

Branches