

October 03, 2023

## Aquatech Water Solutions Private Limited: Rating downgraded to [ICRA]BBB-(Stable); outlook revised to Stable from Negative

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term – Fund-based – Term Loan	40.0	5.3	[ICRA]BBB-(Stable) downgraded from [ICRA]BBB (Negative); Outlook revised to Stable from Negative
Long-term – Unallocated	-	14.7	[ICRA]BBB-(Stable) downgraded from [ICRA]BBB (Negative); Outlook revised to Stable from Negative
<b>Total</b>	<b>40.00</b>	<b>20.00</b>	

\*Instrument details are provided in Annexure-I

### Rationale

The rating action for Aquatech Water Solutions Private Limited (AWSPL) factors in lower than anticipated internal accrual generation and consequent moderation in liquidity buffer and coverage metrics in recent quarters. This is due to continued low-capacity utilisation of its plant resulting in subdued variable income coupled with considerable scaling up expected in the current fiscal; and reduction in fixed revenue by 36-37% from May 2023 onwards. ICRA notes the partial prepayment of debt by the company, leading to lower interest cost, though coverage metrics continue to remain moderate in light of lower accrual generation. ICRA expects the plant capacity utilisation to remain lower than earlier expectations during the current fiscal, translating into some revenue degrowth in FY2024. The rating also remains constrained by the high client concentration risk with all revenue generated by a single customer (HNPCL) and a single project.

However, the rating draws comfort from the strong ring-fencing mechanism around debt repayments with a debt service reserve account (DSRA) holding funds equivalent to two quarters of interest and principal obligations, along with one quarter of instalment being retained either in the escrow account or as fixed deposit. AWSPL's revenues are routed through the escrow account, which prioritises debt repayments over operational expenses, providing additional comfort to its credit profile. The rating notes the existence of the take-or-pay arrangement for fixed charges, ensuring a stable stream of revenues, aiding AWSPL to meet its debt obligations and operational costs.

The Stable outlook on the long-term rating factors in ICRA's expectation that the company will be able to maintain adequate liquidity and generate cash accruals to service its debt obligations.

### Key rating drivers and their description

#### Credit strengths

**Long-term revenue visibility due to 25-year contract and take-or-pay arrangement for part revenues** – AWSPL has established a 25-year contract (from May 2014) for supplying treated water to HNPCL's power plant in Visakhapatnam, Andhra Pradesh. According to the contract, HNPCL will pay a pre-specified fixed charge for the entire tenure of the contract, even in case of minimal offtake from AWSPL. According to the contract, the fixed charges will remain the same for the initial nine years (May 2014 to May 2023), after which there will be a downward revision by ~36–37%. Further, a variable charge will be paid on the quantity of water treated, to be escalated at the rate of 8.5%, and primarily linked with AWSPL's capacity utilisation. Revenue from the variable component in recent times has remained significantly lower than the initially anticipated level owing to the lower offtake by HNPCL.

**DSRA and ring-fencing arrangement by lender supports overall credit profile** – According to the sanction letter, AWSPL is required to maintain two quarters of repayments in the DSRA. Apart from this, the company maintains one quarter of repayment either in the escrow account or fixed deposit, as stipulated by the lender. AWSPL's receipts from HNPCL are routed through the escrow account where statutory payments, debt repayments and DSRA replenishment are prioritised over operational expenses. Further, there is a cash sweep mechanism, where 50% of the surplus goes towards debt prepayment, after meeting operational and capital expenses.

**Significantly long tail period lends flexibility to refinance current debt or raise additional funds** – While the scheduled repayment tenure is until FY2028, the contract period is until FY2040. The company has a tail period of 12 years to refinance its current debt at a lower cost or a longer tenure or raise additional debt to fund its capital requirements or expansion plans.

### Credit challenges

**Low-capacity utilisation leads to modest capitalisation and coverage indicators** – AWSPL's capacity utilisation has remained around 25% in the last six months. This has resulted in lower operating income leading to modest capitalisation and coverage indicators with Total Debt/OPBITDA of 2.5x and DSCR of 1.1x in FY2023. Nevertheless, the waterfall mechanism ensuring debt repayment and DSRA top-up being prioritised over operational expenses provide comfort.

**Significant client concentration risk; HNPCL's stabilisation issues impact AWSPL's capacity utilisation** – AWSPL derives 100% of its revenues from HNPCL, exposing it to client concentration risks. Its revenues were impacted by low-capacity utilisation because of the stabilisation issues at HNPCL's power plant. Thus, the company's revenue growth is incumbent upon HNPCL ramping up its power plant. As per the Hon'ble Supreme Court's direction in February 2022 on the status of the power purchase from HNPCL, along with the tariff petition filed by HNPCL, the Andhra Pradesh Electricity Regulatory Commission (APERC) issued the tariff order in August 2022.

**Modest scale of operations with limited scope of expansion** – The water treatment plant is the only project executed by AWSPL and it operates at an installed production capacity of 12.5 million litres per day. The company's operations are constrained by low-capacity utilization; and being a captive plant, it has limited scope for expansion or obtaining other customers. Owing to its single unit within HNPCL's manufacturing plant, AWSPL is also exposed to high asset concentration risk.

### Liquidity position: Adequate

AWSPL's liquidity is adequate supported by unencumbered cash and cash equivalents of Rs. 3.1 crore as on August 14, 2023, which includes DSRA of two quarters of interest and principal payments and one quarter of principal repayment in the form of fixed deposit. In addition, there is a tight ring-fencing mechanism prioritising debt repayment and DSRA replenishment over operational expenses, ensuring adequate liquidity for debt repayments.

### Rating sensitivities

**Positive factors** – The rating may be upgraded in case of increase in AWSPL's revenue driven by improved capacity utilisation of the project, aiding improvement in the company's liquidity and coverage metrics.

**Negative factors** – Negative pressure on AWSPL's ratings could arise if the capacity utilisation decreases further, leading to lower variable revenue and coverage against scheduled debt repayment over the next financial year. Additionally, increase in counterparty risk, i.e., deterioration in HNPCL's credit profile or dilution of the ring-fencing arrangement with lenders may trigger a rating downgrade.

## Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	<a href="#">Corporate Credit Rating Methodology</a>
Parent/Group support	Not applicable
Consolidation/Standalone	Standalone

## About the company

AWSPL is started by Aquios Development Pte Limited (Aquatech Group holding 49% stake in the company) in 2013 to build and operate a water treatment plant for HNPCL in Palavalasa (Visakhapatnam, Andhra Pradesh). The total project cost was Rs. 57.8 crore, funded through a Rs. 40-crore bank debt, Rs. 10.4-crore promoter debt and Rs. 7.4-crore equity. The total tenure of the contract with HNPCL is for 25 years, starting from May 2014. Currently, the company has only one project and plans to execute more contracts for other Hinduja Group companies. The construction, operations and maintenance have been subcontracted to the associate company, Aquatech Systems Asia Private Limited (ASA).

Established in 1981 and based out of Pennsylvania, USA, Aquatech International Inc. (AIC), the flagship company of the Aquatech Group, is a global leader in water purification technology for industrial and infrastructure markets with a focus on desalination, water recycle and reuse, and zero liquid discharge (ZLD). The company has significant presence in North America, Europe, West Asia, India and China, and is expanding its presence around the world through its subsidiaries. AIC has successfully executed more than 1,000 water management projects in over 60 countries. ASA is the Indian subsidiary of AIC and jointly manages the West Asian and the Asia Pacific markets with AIC.

## Key financial indicators (audited)

AWSPL – standalone	FY2022	FY2023
Operating income	14.0	14.7
PAT	2.1	2.7
OPBDIT/OI	59.5%	59.8%
PAT/OI	15.0%	18.4%
Total outside liabilities/Tangible net worth (times)	2.8	2.0
Total debt/OPBDIT (times)	3.6	2.5
Interest coverage (times)	2.5	3.0

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	Type	Current rating (FY2024)		Chronology of rating history for the past 3 years				
		Amount rated (Rs. crore)	Amount outstanding as of August 30, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023		Date & rating in FY2022	Date & rating in FY2021
				Oct 3, 2023	Jan 23, 2023	Jul 28, 2022	Sep 09, 2021	Oct 06, 2020
1	Term loans	Long term	5.3	5.3	[ICRA]BBB-(Stable)	[ICRA]BBB (Negative)	[ICRA]BBB (Negative)	[ICRA]BBB (Negative)
2	Unallocated Limits	Long term	14.7	--	[ICRA]BBB-(Stable)	-	-	

## Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term fund-based – Term Loan	Simple
Long-term – Unallocated Limits	Not applicable

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	Term Loan	FY2019	11.60%	FY2028	5.30	[ICRA]BBB-(Stable)
NA	Unallocated Limit	NA	NA	NA	14.70	[ICRA]BBB-(Stable)

Source: Company

#### Annexure II: List of entities considered for consolidated analysis – Not applicable

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