

Aquatech Water Solutions Private Limited

February 01, 2019

Summary of rating action

| Instrument* | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action |
|----------------------|-----------------------------------|----------------------------------|--|
| Fund-based Term Loan | 40.00 | 40.00 | [ICRA]BBB(SO)@; Rating reaffirmed and placed on rating watch with negative implication |
| Total | 40.00 | 40.00 | |

*Instrument details are provided in Annexure-1

Rationale

The rating reaffirmation of Aquatech Water Solutions Private Limited (AWSPL) reflects the debt repayment structure with the debt service reserve account (DSRA) holding funds equivalent to two quarters of interest and principal obligations and one quarter of instalment being retained either in the escrow account or fixed deposit. AWSPL's revenues are routed through the escrow account, which prioritises debt obligation payments over operational expenses, providing additional comfort to the credit profile. The rating favourably factors in the project's revenue visibility with an assured offtake contract for 25 years (from May 2014) with Hinduja National Power Corporation Limited (HNPCL), promoted by the Hinduja Group of companies. The rating also notes the existence of the 'take or pay' arrangement for fixed charges, ensuring a stable stream of revenues, adequate to meet the debt obligations and the operational costs. Due to lower billing for the variable component, the DSCR reduced to 1.0x in FY2018 compared to ICRA's earlier expectation of 1.2x. Nevertheless, there exists a tail period of 13 years for the project, lending it flexibility to raise additional funds and refinance debt, if required. The company has subcontracted the plant's operations and maintenance to its associate company, Aquatech Systems Asia Private Limited (ASA, rated [ICRA]BBB(S)(Stable)), benefitting from the technical expertise, and the direct and indirect financial support in the form of extended credit period for the supplies.

With HNPCL being its sole customer, AWSPL is exposed to single client concentration risks. There were instances of delayed payment realisations in the past; however, the receivable cycle has reduced to 70-80 days at present, compared to over 150 days in FY2017. AWSPL's capacity utilisation has reduced to a sub-35% level in FY2019, because of operational issues faced by HNPCL (due to coal availability and power purchase agreement (PPA) dispute with APDISCOM). Going forward, AWSPL's ability to improve its capacity utilisation and streamline its receivable cycle remains the key sensitivity factor. Any adverse ruling on HNPCL's PPA agreement with APDISCOM, slippages in receivables from customer and a revision in AWSPL's 'take or pay' arrangement with HNPCL remain key monitorables.

Outlook: Rating on Watch with Negative Implication

ICRA has placed AWSPL's rating on rating Watch with Negative Implication, as any adverse outcome for HNPCL on the PPA-related dispute with APDISCOM will materially increase the counterparty risk for AWSPL. Moreover, the lower capacity utilisation constrains AWSPL's billing on the variable component, thereby impacting the profitability and the DSCR indicators. The outlook can be revised to Stable in case of AWSPL's improved capacity utilisation and billing for HNPCL, and the stabilisation of operations of HNPCL.

Key rating drivers

Credit strengths

Strong 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. Further, a variable charge is paid on the quantity of water treated, which is escalated at the rate of 8.5%, ensuring revenue growth and expansion in profit margins. The variable component is primarily linked with AWSPL's capacity utilisation. The revenue from the variable component in the recent times has remained lower than the initially anticipated level.

DSRA and ring-fencing arrangement by lender support 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 also 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 also a cash sweep mechanism, where 50% of the surplus, post meeting operational expenses and capital expenses, goes towards debt prepayment.

Established contract with HNPCL mitigates counterparty risk - The company has entered into a contract with HNPCL, a special purpose vehicle (SPV) promoted by the Hinduja Group to supply treated water. HNPCL has developed a coal-based sub-critical thermal power project of 1,040 MW (2 x 520) at Palavalasa Village, Visakhapatnam. Despite a delay in project commencement by HNPCL (due to Hudhud cyclone and stabilisation issues), it had paid the fixed-charges to AWSPL in the past, enforcing the 'take or pay' arrangement.

Significantly long tail period lends flexibility to refinance current debt or raise additional funds - While the scheduled repayment tenure is until FY2027, the contract period is until FY2040. The company has a tail period of 13 years to refinance its current debt at a lower cost or a longer tenure, or raise additional debt to fund capital requirements or expansion plans.

Credit challenges

Significant client concentration risk; HNPCL's stabilisation issues impact AWSPL's capacity utilisation - AWSPL derives 100% of its revenues from HNPCL, exposing the former to single client concentration risks. AWSPL's revenues were impacted due to low capacity utilisation because of the stabilisation issues in HNPCL's power plant. Thus, the company's revenue growth is incumbent upon HNPCL ramping up its power plant.

Delays in payment from HNPCL could stretch working capital cycle - Due to stabilisation issues in the power plant (owing to disputes with APDISCOM with respect to tariffs), there were delays in the receipt of fixed and variable charges from HNPCL in the past. These delays ranged between three to six months in the past, which subsequently impacted AWSPL's working capital cycle. Nevertheless, the debt repayments were timely due to the ring-fencing of cash flows by lenders. Moreover, the receivable cycle has reduced to 70-80 days at present. Further, the company plans to make its receivables LC-backed and streamline its collections in the medium term.

Liquidity position

AWSPL's liquidity position remains comfortable with the DSRA holding amounts equivalent to two quarters of debt repayment obligations and another quarter of principal in the form of fixed deposits. The reduction in receivables outstanding from its customer has also improved the overall cash flows.

Analytical approach

| Analytical Approach | Comments |
|---------------------------------|--|
| Applicable Rating Methodologies | Corporate Credit Rating Methodology |
| Parent/Group Support | Not applicable. |
| Consolidation/Standalone | The rating is based on the standalone credit profile of the entity and the overall credit profile is supported by ring fencing of cash flows via a predefined cash-flow waterfall mechanism. |

About the company

Aquatech Water Solutions Private Limited is an SPV started by Aquios Development Pte Limited (part of the Aquatech Group) in 2013 to build and operate a water treatment plant for HNPCL in Palavalasa. The total project cost was Rs. 57.8 crore, funded through 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 sub-contracted to the associate company, 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, the Middle East, India and China and is expanding its presence across 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 manages the Middle Eastern and the Asia-Pacific markets jointly with AIC.

Key financial indicators (audited)

| | FY2017 | FY2018 |
|------------------------------|--------|--------|
| Operating Income (Rs. crore) | 14.8 | 14.5 |
| PAT (Rs. crore) | 1.0 | 0.4 |
| OPBDIT/OI (%) | 61.8% | 60.1% |
| RoCE (%) | 13.0% | 13.2% |
| Total Debt/TNW (times) | 4.7 | 4.4 |
| Total Debt/OPBDIT (times) | 5.4 | 5.5 |
| Interest Coverage (times) | 1.6 | 1.6 |

Note: Total debt includes promoter loan of Rs. 10.4 crore, which is subordinate to bank debt

Source: Company data, ICRA research

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 | | |
|-------------|-----------|-------------------------|--------------------|----------------|---|------------------|------------------|
| Instrument | Type | Amount Rated | Amount Outstanding | Date & Rating | Date & Rating in | Date & Rating in | Date & Rating in |
| | | (Rs. crore) | (Rs. crore)* | Feb 2019 | FY2018 | FY2017 | FY2016 |
| 1 Term Loan | Long Term | 40.00 | 37.30 | [ICRA]BBB(SO)@ | Sep 2017 [ICRA]BBB (SO)(Stable) | - | - |

@: Rating on Watch with Negative Implication; *: as on March 2018

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 |
|---------|-----------------|-----------------------------|-------------|---------------|--------------------------|--|
| - | Term Loan | Mar-2016 | 11.5% | Mar-2027 | 40.00 | [ICRA]BBB(SO)@ <i>Source: AWSPL</i> |

Annexure-2: List of entities considered for consolidated analysis: Not applicable

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