August 30, 2022

# Techno Electric & Engineering Company Limited: Ratings reaffirmed

## Summary of rating action

| Instrument* | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action |
|---|---|---|---|
| **Fund Based Facilities** | 198.00 | 198.00 | [ICRA]AA(Stable) reaffirmed |
| **Non-Fund Based Facilities** | 424.00 | 424.00 | [ICRA]AA(Stable) reaffirmed |
| **Fund Based Facilities** | (334.00)** | (334.00)** | [ICRA]AA(Stable) reaffirmed |
| **Non-Fund Based Facilities** | (210.00)^^ | (210.00)^^ | [ICRA]AA(Stable) reaffirmed |
| **Non-Fund Based Facilities** | 1305.00 | 1305.00 | [ICRA]A1+ reaffirmed |
| **Fund Based Facilities** | (50.00)*** | (50.00)*** | [ICRA]A1+ reaffirmed |
| **Total** | **1,927.00** | **1,927.00** | |

**Instrument details are provided in Annexure-1*
***sublimit of Rs. 424 crore long term non- fund based and Rs. 305 crore short term non-fund-based facilities*
*^^sublimit of Rs. 160 crore long term fund based and Rs. 90 crore short term non-fund-based facilities*
****sublimit of Rs. 90 crore short term non-fund-based facilities*

## Rationale

The rating reaffirmation factors in Techno Electric & Engineering Company Limited's (TEECL) established track record in the EPC[1] business, backed by its strong execution capabilities, along with expertise in the design, engineering and commissioning of extra-high voltage (EHV) installations, as well as specialty industrial systems. Over the years, the margins from TEECL's EPC business have been better than its peers, which reflects the company's ability to deliver projects on time, while tightly controlling costs and efficiently managing the working capital. Moreover, by selectively bidding for projects having a strong sponsor, and/or secured funding lines, TEECL is able to mitigate counterparty credit risks, and also achieve a faster cash collection cycle. The receivable period deteriorated somewhat in FY2020 as the pandemic affected many TEECL customers, leading to a temporary rise in working capital blockage in the EPC business. Although the receivable days have improved, the same remain elevated in FY2022.

The ratings further derive strength from TEECL's comfortable financial profile, supported by consistent positive free cash flow generation, low debt levels, strong liquidity profile, and healthy return on capital employed. Over the years, TEECL has channelised bulk of the underlying free cash flows in retiring debt, which declined from Rs. 668 crore in FY2013 to negligible levels at present.

The ratings further incorporate TEECL's opportunistic investments for the development of BOOT/BOOM[2] transmission line projects, which has helped generate incremental business for the EPC segment. Moreover, timely exit from such investments at attractive valuations has helped the company to have an asset-light business model, in turn freeing up capital for redeploying in other growth opportunities.

The ratings are, however, constrained by the company's exposure to sectoral and client concentration risks, with orders from the transmission & distribution (T&D) sector and flue gas desulphurisation (FGD) systems only, and the top three clients accounting for 69% of the order book as on June 30, 2022. The performance of the industrial EPC segment, which typically yields superior margins, has started to pick up in a limited way, especially in the contracts for installation of the FGD systems, and the company's ability to diversify the order book across multiple sectors and clients remains a key rating driver.

[1] EPC: Engineering, Procurement & Construction
[2] BOOT: Build own operate transfer; BOOM: Build own operate maintain

The ratings are also tempered by the uncertain regulatory regime and sticky debtors for the wind business in Tamil Nadu, and TEECL's sizeable exposure to the debt securities of companies with weak credit profiles, exposing the company to counterparty risks associated with their timely recoverability. However, ICRA observes that the company has been able to gradually bring down its exposure to such illiquid securities. Its ability to fully exit from the PMS bond portfolio without any significant impairment would remain a key monitorable.
In FY2021, TEECL announced the setting up of a 40-MW hyperscale data centre in Chennai to gain a foothold in this rapidly growing segment which has benefitted from the exponential growth in data consumption following the pandemic. ICRA notes that the company is expected to retain only a minority shareholding in this business segment with an aggregate investment of Rs. 500-700 crore across four data centres (Chennai, Kolkata, Delhi NCR, Navi Mumbai) to be set up over the next 2-3 years. The company is therefore expected to remain largely debt free with limited exposure to the project specific risks. Given its limited experience in this segment, its ability to collaborate with a global strategic equity partner in a timely manner and its ability to collaborate with a reputed global data centre operator will remain key monitorables.

The Stable outlook on the long-term rating reflects TEECL's healthy revenue visibility in the EPC business, its reputed client profile, strong liquidity, and healthy profitability from operations.

## Key rating drivers and their description

### Credit strengths

**Demonstrated track record in EPC business -** TEECL has a long track record of operating as an EPC contractor in the power generation, transmission, distribution, and industrial segments for 59 years. In addition, TEECL has experience in the execution of substation/transmission projects under BOOT/BOOM[3] models. TEECL's EPC service delivery capabilities range from providing turnkey customised packaged solutions, with a high service component (including design and engineering), executing turnkey captive power plant projects (of up to 100 MW), sub-station/switchyard projects of up to 765 kv, distribution system management projects, as well as specialised industrial jobs, like design of high intensity power systems for aluminium smelter pots, fuel oil systems, and off-site piping systems, among others. Over the years, the company has made a footprint in the overseas markets as well in the transmission and distribution segment.

TEECL was one of the early entrants in the 765 kv substation segment in India. In addition, TEECL has been a frontrunner in the roll-out of emerging power transmission technologies like STATCOM (Static Synchronous Compensator). In FY2020, the company forayed into the delivery of electromechanical solutions like FGD installation at thermal power plants. Moreover, TEECL has ventured into the fast-growing data centre segment by embarking on a project to set up a 40-MW hyperscale data centre in Chennai.

**Operating margins in EPC business remain better than peers -** TEECL's operating margins from the EPC business has been in the range of 15-20% between FY2015 and FY2022. ICRA notes that TEECL's margins are considerably higher than its peers, which demonstrates strong execution capability, and its strategy to be present in segments which has a minimum threshold level of design and engineering complexity, leading to less competitive pressures. Despite the slowdown in order inflow from Power Grid in recent years, and the company increasingly focussing on the distribution, generation, and industrial segments, its operating margins from the EPC business have seen a steady improvement between FY2018 and FY2021. Input cost pressures have resulted in slight moderation in margins in FY2022; however, the price variation clauses in the contracts will help recover these costs to an extent.

**Reputed client profile in EPC business; selective bidding for projects backed by assured funding lines limits counterparty risks -** By selectively bidding for projects having a strong sponsor, and/or secured funding lines, TEECL is able to mitigate counterparty credit risks and also achieve a faster cash collection cycle. However, ICRA notes that the increasing share of orders from SEBs[4] compared to Power Grid has increased the working capital deployment in the EPC business from a receivable

[3] BOOT: build, own, operate, transfer; BOOM: build, own, operate, maintain

[4] State Electricity Boards

period[5] of 147 days in FY2017 to 247 days in FY2020, leading to a rise in working capital blockage. The same have moderated to 210 days in FY2022.

**Comfortable financial profile -** Over the years, TEEC has been able to generate a steady stream of free cash flows, supported by a combination of high margins in the EPC segments, efficient working capital deployment, and asset monetisation initiatives. Notwithstanding company's plans to return ~Rs 500 crore to the shareholders (through buyback/ dividends), ICRA expects TEECL's free cash flows to remain positive in the medium term. Consistent positive free cash flow generation has helped the company build a sizeable liquidity pool, which has been parked in liquid investments and high-yield PMS investments. As on March 31, 2022, TEECL had a cash & liquid investment[6] balance of Rs. 813.4 crore. TEECL's business return metrics also remained healthy, with its core-RoCE[7] in a range of 20-28% between FY2017 and FY2022.

**Investments in BOOT/BOOM transmission line projects generated incremental business for EPC segment -** TEECL entered the asset-intensive BOOT/BOOM transmission segment in CY2010 by leveraging on its core EPC capabilities, and has been able to generate incremental business for the EPC segment. TEECL has commissioned three BOOT/BOOM projects entailing an investment of ~Rs. 1,950 crore. However, in line with the company's strategy of following an asset-light model, it has exited all its BOOT/ BOOM transmission projects at attractive valuations, in turn freeing up capital for redeploying in other growth opportunities.

## Credit challenges

**Exposure to sectoral and client concentration risks -** TEECL has high client and sectoral concentration risks. ICRA notes that in the last 4-5 years, the share of orders from Power Grid Corporation of India Limited declined to 9% in end-June 2022 from 80% in end-September 2016. Notwithstanding this decline, TEECL's client concentration remains high, with the top three clients accounting for 69% of the order book as on June 30, 2022. With the receipt of significant FGD orders in Q1 FY2023, the share of FGD orders stood at 48% of the unexecuted order book as on June 30, 2022, while the balance was from the transmission & distribution segment, leading to sectoral concentration risks. The company has forayed into the data centre business, and this is expected to diversify its EPC order book to an extent.

**Uncertain regulatory regime and sticky debtors for the wind business in Tamil Nadu impacting business performance -** TEECL's 111.9-MW wind assets in Tamil Nadu have encountered multiple regulatory headwinds over the years. These include: a) capping of the effective tariff at lower of the APPC[8] rate or 75% of the preferential tariff, and b) a sharp 31% reduction in the preferential wind tariff in Tamil Nadu from Rs. 4.16/unit in FY2019 to Rs. 2.86/unit in FY2020. TEECL had approached APTEL to seek redressal on the issue of capping of its PPA tariff, and received a favourable order on the matter from APTEL on May 31, 2019. However, TANGEDCO challenged the APTEL order in Supreme Court, on which a final judgment is awaited. Subsequently, APTEL passed an order dated January 28, 2021 setting aside TNERC's[9] order for reducing the preferential wind tariff in Tamil Nadu from Rs. 4.16/unit to Rs. 2.86/unit. Following this order, TEECL raised arrear bills accumulating to Rs. 35.85 crore for FY2020 and FY2021 related to the tariff differential (Rs. 3.12/unit eligible tariff vs. billing rate of Rs. 2.15/unit for the period April 2019 to January 2021).

The delays in collections from TANGEDCO has further weighed down on the performance of the wind business. As on March 31, 2022, the receivables from the wind division stood at Rs. 174.5 crore, reflecting overdue payments of 2.0 years.

**Sizeable exposure to debt securities of companies with weak credit profile –** From FY2018, TEECL started partly parking its surplus funds in a portfolio management scheme (PMS) having a concentrated investment pool of debt securities. ICRA notes that a sizeable share of the underlying debt securities is in companies with weak credit profiles, exposing the company to risks associated with timely recoverability. However, ICRA observes that the company has been able to gradually bring down its

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[5] Including retention money and unbilled revenue
[6] excluding PMS securities
[7] Return on capital employed
[8] Average pooled power purchase cost
[9] Tamil Nadu Electricity Regulatory Commission

exposure to such illiquid securities and its ability to fully exit the PMS bond portfolio without any significant impairment would remain a key monitorable.

## Liquidity position: Strong

TEECL's liquidity is assessed as strong, supported by its ability to generate positive free cash flows across business cycles. As on March 31, 2022, TEECL had a cash & liquid investment balance of Rs. 813.4 crore, which along with its largely undrawn fund-based working capital lines provides a sizeable liquidity cushion. While the company has announced buyback/dividends of Rs 500 crore in aggregate over FY2023-25, the liquidity is expected to remain strong, aided by healthy cash accruals, and the company's asset-light approach towards the construction of data centres. TEECL's on-balance sheet liquidity is expected to strengthen further with the company at an advanced stage of selling its 40-45 MW installed wind capacity, which is expected to result in an inflow of around Rs. 150-160 crore.

### Rating sensitivities

**Positive factors –** The ratings may be upgraded if the sectoral and client concentration risks decline, driven by a sustainable uptick in order inflows from the industrial segment. A significant increase in the scale of operations, while maintaining healthy debt protection metrics, and a comfortable liquidity position may also support an upgrade.

**Negative factors –** The ratings may be downgraded if a sustained period of weak earnings and fresh order inflows leads to a decline in profits and cash accruals. The ratings may be under pressure if there is a significant increase in the receivable position, or if there are any further loans/advances to unrelated parties, and/or if there are any potential execution challenges in the ongoing projects, leading to BG invocation, and a consequent material deterioration in the liquidity profile. A large debt-funded growth plan, which leads to a marked deterioration in the debt protection metrics, and consistently negative free cash flows after meeting the scheduled debt repayments may also trigger a downgrade.

### Analytical approach

| Analytical Approach | Comments |
|---|---|
| **Applicable Rating Methodologies** | Corporate Credit Rating Methodology<br>Rating Methodology for Construction Entities<br>Rating Methodology for Wind Power Producers |
| **Parent/Group Support** | Not Applicable |
| **Consolidation/Standalone** | For arriving at the ratings, ICRA has considered the consolidated financials of TEECL. As on March 31, 2022, the company had 6 subsidiaries which are all enlisted in Annexure-2. |

### About the company

TEECL is an established EPC company having core engineering skills and light construction capabilities in the power generation, transmission and distribution, and industrial segments. Today, the company has positioned itself as a turnkey provider of specialized packaged solutions, with a high service component (including design and engineering), and has also developed expertise in executing turnkey jobs in the areas of sub-station/switchyard projects of up to 765 kv (AIS/GIS[10]), distribution system management, captive power plant projects (of up to 100 MW), as well as specialized industrial jobs, like design of high intensity power systems for aluminium smelter pots, fuel oil systems, and off-site piping systems, among others. Over the years, the company has made a footprint in the overseas markets as well, by bagging orders in Afghanistan and the African region.

[10] Air insulated substations and gas insulated substations

TEECL was one of the early entrants in the 765 kv substation segment in India. In addition, TEECL has been a frontrunner in the roll-out of emerging power transmission technologies like STATCOM (Static Synchronous Compensator). In FY2020, the company forayed into the delivery of electromechanical solutions like FGD installation at thermal power plants. Moreover, TEECL has ventured into the fast-growing data centre segment by embarking to set up a 40-MW hyperscale data centre in Chennai.

Apart from the EPC business, TEECL owns wind power assets of 129.9 MW in Tamil Nadu (111.9 MW) and Karnataka (18 MW), which leads to some revenue diversification. However, the receivables in the wind division, especially from TANGEDCO, has remained elevated over the years.

### Key financial indicators (Audited)

| Consolidated | FY2021 | FY2022 |
|---|---|---|
| **Operating Income (Rs. crore)** | 889.2 | 1073.9 |
| **PAT (Rs. crore)** | 183.6 | 260.3 |
| **OPBDIT/OI (%)** | 24.5% | 20.7% |
| **PAT/OI (%)** | 20.6% | 24.2% |
| **Total Outside Liabilities/Tangible Net Worth (times)** | 0.4 | 0.4 |
| **Total Debt/OPBDIT (times)** | 0.2 | 0.0 |
| **Interest Coverage (times)** | 23.1 | 39.5 |

*PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation*

## 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 Mar 31, 2022 (Rs. crore) | Date & rating on | Date & rating in FY2022 | Date & rating in FY2021 | Date & rating in FY2020 |
| | | | | | Aug 30, 2022 | May 31, 2021 | - | Nov 29, 2019 |
| 1 | Fund Based Facilities | Long Term | 198.00 | 0.00 | [ICRA]AA(Stable) | [ICRA]AA(Stable) | - | [ICRA]AA(Stable) |
| 2 | Non-Fund Based Facilities | Long Term | 424.00 | NA## | [ICRA]AA(Stable) | [ICRA]AA(Stable) | - | [ICRA]AA(Stable) |
| 3 | Fund Based Facilities | Long Term | (334.00)** | NA | [ICRA]AA(Stable) | [ICRA]AA(Stable) | - | [ICRA]AA(Stable) |
| 4 | Non-Fund Based Facilities | Long Term | (210.00)^^ | NA | [ICRA]AA(Stable) | [ICRA]AA(Stable) | - | [ICRA]AA(Stable) |
| 5 | Non-Fund Based Facilities | Short Term | 1305.00 | 667.00## | [ICRA]A1+ | [ICRA]A1+ | - | [ICRA]A1+ |
| 6 | Fund Based Facilities | Short Term | (50.00)*** | NA | [ICRA]A1+ | [ICRA]A1+ | - | [ICRA]A1+ |

*Amount in Rs. crore; NA: Not Available; ##Combined utilization of short-term and long-term non-fun based limits was Rs. 667.00 crore as on March 31, 2022*

***sublimit of Rs. 424 crore long term non- fund based and Rs. 305 crore short term non-fund based facilities*
*^^sublimit of Rs. 160 crore long term fund-based and Rs. 90 crore short term non-fund based facilities*
****sublimit of Rs. 90 crore short term non-fund based facilities*

## Complexity level of the rated instrument

| Instrument | Complexity Indicator |
|---|---|
| **Long-Term Fund Based Facilities** | Simple |
| **Long-Term Non-Fund Based Facilities** | Very Simple |
| **Long-Term Fund Based Facilities (Sub-limit)** | Simple |
| **Long Term Non-Fund Based Facilities (Sub-limit)** | Very Simple |
| **Short-Term Non-Fund Based Facilities** | Very Simple |
| **Short-Term Fund Based Facilities (Sub-limit)** | 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: 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 | Fund Based Facilities | - | - | - | 198.00 | [ICRA]AA(Stable) |
| NA | Non-Fund Based Facilities | - | - | - | 424.00 | [ICRA]AA(Stable) |
| NA | Fund Based Facilities | - | - | - | (334.00)** | [ICRA]AA(Stable) |
| NA | Non-Fund Based Facilities | - | - | - | (210.00)^^ | [ICRA]AA(Stable) |
| NA | Non-Fund Based Facilities | - | - | - | 1305.00 | [ICRA]A1+ |
| NA | Fund Based Facilities | - | - | - | (50.00)*** | [ICRA]A1+ |

***Source:*** *Company*

***sublimit of Rs. 424 crore long term non- fund based and Rs. 305 crore short term non-fund based facilities*
*^^sublimit of Rs. 160 crore long term fund-based and Rs. 90 crore short term non-fund based facilities*
***sublimit of Rs. 90 crore short term non-fund based facilities

## Annexure-2: List of entities considered for consolidated analysis:

| Company Name | TEECL Ownership | Consolidation Approach |
|---|---|---|
| Techno Infra Developers Private Limited | 100.00% | Full Consolidation |
| Techno Digital Infra Private Limited | 100.00% | Full Consolidation |
| Techno Green Energy Private Limited | 100.00% | Full Consolidation |
| Techno Wind Power Private Limited | 100.00% | Full Consolidation |
| Rajgarh Agro Products Ltd | 96.10% | Full Consolidation |
| Techno Power Grid Company Limited | 100.00% | Full Consolidation |

***Source:*** *TEECL annual accounts FY2022*

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## 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

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