October 30, 2023

Esmart Energy Solutions Limited: Ratings reaffirmed, rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term: Fund based – Term Loan	35.25	62.19	[ICRA]BBB-(stable); reaffirmed and assigned for enhanced amount
Long-term: Fund based – Cash Credit	7.00	7.00	[ICRA]BBB-(stable); reaffirmed
Short-term: Non-fund based	60.00	60.00	[ICRA]A3; reaffirmed
Total	**102.25**	**129.19**	

**Instrument details are provided in Annexure-I*

Rationale

The reaffirmation of the ratings continues to factor in Esmart Energy Solutions Limited's (EESL) proven track record in the energy efficiency sector, the established experience of its promoters in the electrical industry and a sound business model. Moreover, the company's strong revenue book position ensures relatively stable visibility of revenues and cash flows in the near to medium term for the executed contracts as well as for the upcoming planned projects. The financial profile of the company continues to remain healthy, with improvement in capital structure (on a provisional basis) witnessed on conversion of unsecured loans in equity to 0.2 time in FY2023 from 0.55 time in FY2022. The debt protection metrics also continue to be healthy with interest coverage at 11.7 times, NCA/total debt of 138% and Total Debt/OPBDITA of 0.64 time in FY2023 on a provisional basis, owing to healthy profitability levels in business.

The ratings are, however, constrained by EESL's moderate scale of operations and high working capital intensity owing to the elongated receivable cycle and high inventory requirements. The company is engaged in street light replacement projects wherein its clients are municipal bodies, who elongate the payment cycle due to a long approval process and slow recovery depending on the actual financial health of the municipal corporation. Further, the ratings are constrained by EESL's capital-intensive nature of business, wherein it has a medium-term debt-funded capex plan for future projects. Going forward, its ability to timely execute the same without any cost overrun and achieve financial closure at favourable terms with limited leveraging to keep the capital structure and coverage indicators under check remains monitorable. EESL is also exposed to foreign exchange (forex) fluctuation risks as it imports certain raw materials for manufacturing LED lights and the revenue profile is all local currency-based. However, the quantum of imports remains minimal as compared to the scale of operations of the company. ICRA also notes the ongoing litigation with Uniglobal Ventures LLP and Paisalo Digital Limited (erstwhile SE Investment), wherein EESL had given a corporate guarantee to Paisalo for the loan taken by Uniglobal Ventures LLP and the corporate guarantee was invoked. The same is under litigation and is an ongoing commercial dispute. ICRA, hence, will continue to monitor the developments in this regard and assess its impact, if any, on the credit profile of EESL, in case any material liability falls on it, or in case of any unfavourable ruling against the company.

The Stable outlook reflects ICRA's expectations that EESL will continue to benefit from the extensive experience of its promoters, its track record of executing projects in a timely manner and healthy profitability levels owing to its its sound business model.

Key rating drivers and their description

Credit strengths

Established experience of promoters with demonstrated track record of operations – EESL is promoted by Mr. Suresh Shah, who has been associated with the electrical industry for more than four decades. The experienced management team with the requisite professional set-up is led by Mr. CA Anand Prakash Rai, the CEO of the company. The company, over the last five years, has successfully executed more than 12 projects for different municipal corporations across India.

Lack of upfront capex remains EESL's USP; healthy operating margin – The company's operating margins have remained healthy in the range of 45-60% during the last three years owing to its sound business model, which is expected to provide long-term operational benefits. EESL follows an energy savings based model, wherein the company finances the upfront capital cost of the project. It recovers the investment, along with operating costs through monthly payments from the customer under multi-year contracts, under a deemed savings approach. The lack of upfront capex requirements and savings from the energy efficiency projects for customers remain the key USP for EESL's projects.

Comfortable capital structure and healthy debt coverage indicators – EESL's capital structure remained comfortable with a gearing of 0.2 time as on March 31, 2023, (0.6 time as on March 31, 2022) on a provisional basis, due to healthy accretion to reserves and conversion of unsecured loans to equity in FY2023. The debt coverage indicators stood healthy with interest coverage of 11.7 times (11.1 times in FY2022), NCA/total debt of 138% (70.6% in FY2022) and total debt/OPBDITA of 0.6 time as on March 31, 2023 (1.2 times in FY2022) on a provisional basis. Its total debt stood at Rs. 30.2 crore as on March 31, 2023, and consisted of term loans of Rs. 20.9 crore, interest-free unsecured loans of Rs. 3.5 crore and Rs. 5.8 crore of working capital borrowings. Its net worth increased to Rs. 143.2 crore as on March 31, 2023, from Rs. 95.4 crore as on March 31, 2022, supported by healthy cash accruals and conversion of unsecured loans to equity.

Diversified geographical presence and strong revenue book position – The company has strong relations with municipal corporations across India with presence in Delhi, Odisha, Punjab, Gujarat, Uttar Pradesh, Maharashtra and West Bengal. It had a strong revenue book of more than Rs. 900 crore as on March 31, 2023, extending over the next 10 years. In addition, EESL has submitted bids in Karnataka, Maharashtra and Punjab for various projects, which would further improve its revenue book and geographical presence once the same materialises.

Credit challenges

Moderate scale of operations – The company recorded modest revenue growth of 5% to Rs. 104.6 crore in FY2023 owing to limited addition of new projects in FY2022. At an absolute level, the revenue continues to be at a moderate level. Going forward, the revenues are expected to increase at a faster rate, with new order inflow from additional states, wherein the company is at different levels of order bid stage. However, the growth will be contingent on actual order inflow and the timely execution of projects.

High working capital intensity owing to elongated receivable cycle and inventory requirements – The company's working capital intensity was high at 51.7% in FY2023 owing to an elongated receivable cycle and high inventory requirements. Given the exposure to municipal corporations, the payment period generally remains in the range of 90-120 days from the date of billing. It had a debtor cycle of 74 days with absolute receivables of Rs. 21.1 crore as on March 31, 2023, owing to the slow recovery from municipal corporations, along with receivables for more than one year due to customer-specific issues for a few projects. However, the debtor days have improved over the years, from the earlier levels of 80 days in FY2022 owing to improved collections from the municipal corporations and will remain a key rating monitorable. The inventory period for the company remained high at 77 days for FY2023 (61 days in FY2022) as the funds are blocked for the entire construction period (generally four to five months) for a particular project. EESL imports raw materials such as LED diodes from Singapore and the US, lenses from Italy and other electrical components from South Korea and Singapore. The quantities ordered are small at a time and the payments are done upfront. Local purchases involve job-work and the purchase of electrical components with a credit period of 30-60 days.

Capital-intensive nature of business with moderate medium-term capex planned – Given the nature of upfront capex, which EESL must undertake, the business remains capital-intensive. Further, it has medium-term capex plans due to its upcoming bidding pipeline. Hence, the funding requirements would remain high in the near to medium term. The company expects to fund the entire capex by a mix of debt and internal accruals. The generation of adequate internal accruals for FY2024 and FY2025 will remain crucial to meet its capex targets. Nonetheless, comfort can be drawn from the support extended by the promoters through unsecured loans and by the guarantees provided by the Small Industries Development Bank of India (SIDBI) for term loans under a partial risk sharing facility for energy efficiency.

Exposed to project execution risk given the debt funded capex – Given the medium-term capex plans due to its upcoming bidding pipeline, it remains exposed to project execution risk. The capex is proposed to be funded through a mix of term loans and internal accruals. With the onboarding of the debt, the capital structure and debt-coverage metrics are likely to moderate over FY2024–FY2025. Though the capex will aid in capacity enhancement, EESL's ability to scale up and garner commensurate returns from its planned capex and timely commencement of the projects without any cost overrun will remain critical.

Liquidity position: Adequate

The company's liquidity position is adequate with free cash and liquid investments of ~Rs. 8.8 crore as on March 31, 2023. Further, the average utilisation of fund-based limits is moderate at 77% of the sanctioned limits for the last 12 months ending in August 2023. It has sizeable long-term repayments, however, the same is expected to be covered by cash accruals. The capex requirements are expected to be funded by internal accruals and additional term loans. Nonetheless, comfort can be drawn from the past support extended by the promoters in form of unsecured loans; a large part of the same was also converted to equity in FY2023.

Rating sensitivities

Positive factors – ICRA could upgrade EESL's ratings if it is able to scale up the operations, while maintaining profitability levels, along with significant improvement in liquidity profile, through better receivables management. Further, timely completion of the planned projects without any cost and time overruns could also be a positive trigger.

Negative factors – Pressure on EESL's ratings could arise in case of weakness in collections, adversely impacting its liquidity profile, or if any delay in execution of upcoming projects affects the top line or profitability. Any large debt-funded capex impacting the coverage metrics materially will also be a negative factor for the rating.

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 EESL. As on March 31, 2022, the company had five subsidiaries, which are all enlisted in Annexure-II.

About the company

EESL was incorporated as Shah Investments Financials, Developments & Consultants Private Limited (SIFDCPL), a private limited company under the Companies Act 1956, on November 29, 1979. SIFDCPL was mainly involved in investment activities, hire purchase, leasing, development of industrial units and others. SIFDCPL changed its name to Esmart Energy Solutions Limited in 2013 and entered the Energy Saving Company (ESCO) business with its own energy efficient LED light-manufacturing facility at Nashik, Maharashtra. EESL now focuses only on ESCO activities, security and surveillance, providing IT-based LED lighting solutions to municipal corporations on sharing-the-savings-of-energy basis.

EESL primarily follows the ESCO model, wherein it replaces conventional streetlights with LEDs at its own cost with zero investment from municipal corporations. The subsequent reduction in energy and maintenance cost of a municipal corporation is used as revenue sharing for EESL. Most of the contracts are typically of 7-10 years, where EESL agrees on deemed energy saving and provides maintenance of lights at no additional cost (in most cases). The company usually ensures 85% of energy-saving efficiency.

Key financial indicators (audited)

	FY2022	FY2023*
Operating income	99.5	104.6
PAT	17.9	16.8
OPBDIT/OI	48.1%	45.2%
PAT/OI	18.0%	16.0%
Total outside liabilities/Tangible net worth (times)	1.1	0.6
Total debt/OPBDIT (times)	1.2	0.6
Interest coverage (times)	11.1	11.7

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

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2024)				Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of Mar 31,2023 (Rs. crore)	Date & Rating in	Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021
					October 30, 2023	July 28, 2022	May 21, 2021	-
1	Cash Credit	Long-term	7.00	-	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	-
2	Term Loans	Long-term	62.19	20.9	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	-
3	Bank Guarantee	Short term	60.00	-	[ICRA]A3	[ICRA]A3	[ICRA]A3	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long Term - Fund Based/ CC	Simple
Long Term - Fund Based TL	Simple
Short Term – Non-Fund Based – Bank Guarantee	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: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Cash Credit	NA	NA	NA	7.00	[ICRA]BBB-(Stable)
NA	Term Loan-I	FY2021	NA	FY2025	5.19	[ICRA]BBB-(Stable)
NA	Term Loan-II	FY2023	NA	FY2027	8.10	[ICRA]BBB-(Stable)
NA	Term Loan-III	FY2023	NA	FY2028	11.20	[ICRA]BBB-(Stable)
NA	Term Loan-IV	FY2023	NA	FY2028	8.94	[ICRA]BBB-(Stable)
NA	Term Loan-V	FY2023	NA	FY2028	6.27	[ICRA]BBB-(Stable)
NA	Term Loan-VI	FY2023	NA	FY2028	5.19	[ICRA]BBB-(Stable)
NA	Term Loan-VII	FY2023	NA	FY2028	6.80	[ICRA]BBB-(Stable)
NA	Term Loan-VIII	FY2023	NA	FY2028	5.50	[ICRA]BBB-(Stable)
NA	Term Loan-IX	FY2023	NA	FY2028	5.00	[ICRA]BBB-(Stable)
NA	Bank Guarantee	NA	NA	NA	60.00	[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

Company Name	Ownership	Consolidation Approach
Super Wealth Financials Private Limited	97.48%	Full Consolidation
US Instrument Private Limited	51.27%	Full Consolidation
Green Hydrocarbons India Private Limited	77.50%	Full Consolidation
DIMA Electro LLP	98.00%	Full Consolidation
DIMA Cable LLP	98.00%	Full Consolidation

Source: *Company*

Note: *ICRA has considered the consolidated profile of the parent (EESL), its subsidiaries and associates while assigning the ratings.*

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About ICRA Limited:

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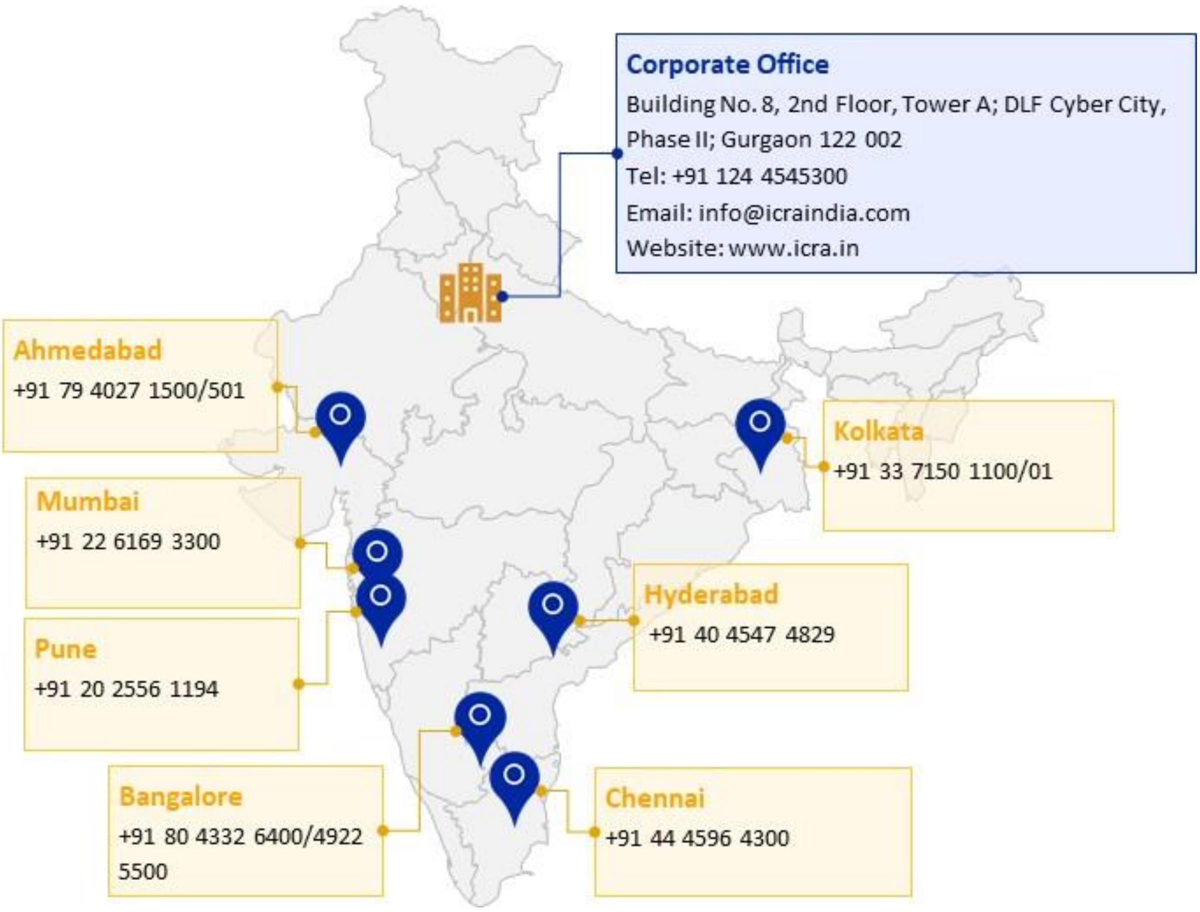

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