ICRA

March 28, 2017

# ISGEC Hitachi Zosen Limited

| Instrument* | Rated Amount (in crore) | Rating Action |
|---|---|---|
| Fund based limits | 140.0 (enhanced from Rs 100.0 crore) | Reaffirmed at [ICRA]AA(Stable) (SO) |
| Non Fund based limits | 280.0 (enhanced from Rs 175.0 crore) | Reaffirmed at [ICRA]AA(Stable) (SO) |
| Non Fund based limits | 25.0 | Assigned at [ICRA]BBB+(Stable) |
| Fund based / Non fund based limits | 40.0 (enhanced from Rs 25.0 crore) | Reaffirmed at [ICRA]AA(Stable) (SO) |
| Unallocated limits | 65.0 | Assigned at [ICRA]BBB+(Stable) |
| **Total** | **550.0** | |

*Instrument Details are provided in Annexure-1

**Rating Action**

ICRA has reaffirmed the long term rating at [ICRA]AA(SO)( pronounced ICRA double A structured obligation)[1] to the Rs 140 crore[2] (enhanced from Rs 100 crore) fund based working capital bank facilities, Rs 280 crore (enhanced from Rs 175 crore) non fund based working capital bank facilities and Rs 40 crore (enhanced from Rs 25 crore) fund based / non fund based working capital bank facilities of ISGEC Hitachi Zosen Ltd (IHZL). ICRA has also assigned a long term rating of [ICRA]BBB+(pronounced ICRA triple B plus) to Rs 25 crore non fund based working capital bank facilities and Rs 65 crore unallocated limits of IHZL. The letters SO in parenthesis suffixed to the rating symbol stand for Structured Obligation. An SO rating is specific to the rated issue, its terms, and its structure. SO rating does not represent ICRA's opinion on the general credit quality of the issuer concerned. The outlook on the long term rating is 'Stable'.

**Rating Rationale for SO Rating**

The SO (Structured Obligation) ratings take into consideration the corporate guarantee extended by ISGEC Heavy Engineering Limited (IHEL) (rated at [ICRA]AA (stable) and [ICRA]A1+) for Rs 140 crore fund based limits, Rs 280 crore non fund based limits and Rs 40 crore fund based / non fund based limits of ISGEC Hitachi Zosen Limited (IHZL). The above ratings address the servicing of the loan to happen as per the terms of the underlying loan and guarantee arrangement and the ratings assume that the guarantee will be duly invoked, as per the terms of the underlying loan and guarantee agreements, in case there is a default in payment by the borrower.

[1]For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications
[2] 100 lakh = 1 crore = 10 million

**Guarantor's profile – ISGEC Heavy Engineering Limited**

ISGEC Heavy Engineering Limited (formerly Saraswati Industrial Syndicate Limited), a public company under the ISGEC Group, is engaged in the manufacturing of Heavy Engineering equipments and providing ~~related~~ EPC/ Turnkey services. Its product portfolio comprises Pressure Vessels, Heat Exchangers, Mechanical and Hydraulic presses, Iron and Alloy Steel Castings, Boilers, Power Plant, Sugar machinery and Air pollution control equipments. The company was established in 1946 by the Puri family. Their initial business activity was manufacturing of spares for sugar mills to complement its sugar mills operations. In the course of its history, the company diversified into a range of engineering products, and in 1964 it established a joint venture with John Thompson of the UK to form "ISGEC JOHN THOMPSON" to manufacture boilers. In 1981, it acquired majority shares in UP STEELS. Both these companies were subsequently amalgamated into ISGEC Heavy Engineering Limited.

The company also has technical collaborations with Foster Wheeler of USA for technology related to manufacturing of CFBC Boilers upto 99.9 MW and for Pulverized Coal Fired Subcritical (60 MW to 1000 MW) and Supercritical (550 MW to 1000 MW) Boilers. During FY 2011-12, IHEL completed a capacity expansion for manufacturing of pressure parts required for Boilers.

IHEL incorporated a Joint Venture 'ISGEC Hitachi Zosen Limited' along with Hitachi Zosen Corporation, Japan in March 2012. The JV is engaged in the manufacturing of specialized & critical process equipments and caters to the requirements of oil refining, fertilizer & petrochemical industries.

The company bought technical drawings and the brand Morando for manufacturing of Vertical Turning Lathes (VTL) during FY 2011-12. IHEL also acquired the technology to manufacture Electrostatic Precipitators (ESP) from Envirotherm GmbH, Germany, and signed technology agreements with M/s TEI, USA, for the manufacturing of Breech Lock Exchangers and with Foster Wheeler, Spain, for the supply of design for Feed Water Heaters and Surface Condensers in the same financial year.

During FY 2012-13, the company's machine building division developed presses suitable for non-automobile applications such as white goods, tiles, etc. Further, the company's steel casting unit developed the capability of manufacturing crushing shell castings for the mining & mineral processing industry.

In FY 2013-14, the boiler division of IHEL has ventured into new products including Heat recovery steam generators, Waste heat recovery boilers and Pin hole grate boilers. The division has also ventured into Repair and maintenance business for the first time. The company has commissioned first domestic order for Pulverized coal fired boiler and the first Electrostatic precipitator in accordance with the technology acquired from Envirotherm Gmbh, Germany.

For the year ended March 2016, IHEL reported a net profit of Rs 173.99 crore on an operating income of Rs 3878.78 croreThe rating action derives comfort from the company's strong parentage and management with CWPD

**Detailed Rationale for Long Term Rating [ICRA]BBB+(stable)**

The ratings derive strength from the established position of the company's shareholders ISGEC Heavy Engineering Limited (IHEL) (Rated [ICRA]AA(stable)/[ICRA]A1+) and Hitachi Zosen Corporation (HZC); and the support extended by them in areas of design, technology, manpower and bidding/marketing. ICRA also factors in the company's healthy order book and sufficient geographical diversification with export orders comprising 26% of its current order book. The rating takes into consideration IHZL's locational advantage of being a port based facility which enables it to manage its working capital cycle and logistics more efficiently. IHZL's rating also considers the fact that its foreign currency denominated loans is fully hedged.

Nevertheless, the assigned ratings are constrained by the exposure of IHZL's profitability to fluctuations in the prices of key raw materials (given the fact that equipment supply contracts are typically of fixed price nature). This risk is exacerbated by the long manufacturing cycle of the company, which is typically around 15-18 months. Further, cyclical trends in consuming industries may affect future order inflows, although this risk is partly mitigated by the geographical diversification of the company's order book. The ratings also remain constrained by competitive pressures from both domestic and international players.

**Key rating drivers**

**Credit Strengths**

- Established position of the company's shareholders ISGEC Heavy Engineering Limited (IHEL) and Hitachi Zosen Corp (HZC) in the capital goods industry.
- Strong financial profile and credit profile of shareholders IHEL (Rated [ICRA]AA(stable)/A1+) and HZC (Rated BBB by Rating and Information Inc, Japan and Japan Credit Rating Agency)
- Locational advantage of being a port based facility which enables IHZL in managing its working capital efficiently & controlling logistics costs.
- Satisfactory order book position
- Presence of irrevocable and unconditional corporate guarantee from IHEL (Rated [ICRA]AA(stable)/A1+) covering the Rs. 460.0 crore bank facilities. This has resulted in structured obligation rating for the above mentioned bank facilities.
- Ability to avail unsecured loans from parent entities at competitive interest rates.
- Substantial equity funding with equity capital of Rs. 100 crore has resulted in a healthy capital structure.
- Satisfactory policy of hedging entire exposure.

**Credit Weakness**

- Competitive pressures from other domestic and international players.
- Substantial share of revenues from exports business has resulted in vulnerability to foreign exchange fluctuations. However, the company has hedged its position by utilizing currency forwards.
- Working capital intensive nature of operations due to substantial work-in-progress inventory (on account of long manufacturing cycle).
- Weak outlook of capacity addition in the oil refining/petrochemical industry may result in a slowdown in new orders received going forward

**Detailed description of key rating drivers highlighted above:**

The rating factors in the linkages between IHZL and its parent entities and the support extended by the latter in the form of technical know-how, marketing support, managerial expertise etc. IHZL's order book has also improved over time as the operations of the JV have stabilized. The JV also benefits from the locational advantage of being situated close to a port which helps it to optimize on logistics costs. Further, ICRA also takes note of the prudent working capital management and forex policies followed by the management.

The rating is, however, constrained due to the relatively nascent stages of operation, competition and the slowdown in the refining/petrochemical industry

**Analytical approach:** Not Applicable

**Links to applicable Criteria**
Corporate Credit Rating –A Note on Methodology

**About the Company:**
ISGEC Hitachi Zosen Limited (IHZL) is a Joint Venture (JV) incorporated in March 2012 with an equity share capital of Rs. 100 crore. IHZL has a 51% shareholding of ISGEC Heavy Engineering Limited (IHEL), India and 49% shareholding of Hitachi Zosen Corporation (HZC), Japan. The JV is engaged in the manufacturing of specialized & critical process equipments for oil refining, fertilizer & petrochemical industries.

IHZL benefits from the technological capability and customer base of its shareholding entities, IHEL and HZC, which are also responsible for the bidding/marketing function of the company. Collaboration with HZC has given it access to the technology for building critical process equipment in India and substantially enhanced the stature of the group in providing essential & critical inputs for the heavy engineering sector. ISGEC Heavy Engineering Limited (IHEL) has leased its manufacturing facility at the port city of Dahej, Gujarat to the JV. IHZL expanded its manufacturing capacity of the facility at Dahej from earlier 8,000 MT/year to 13,000 MT/year in July 2014.

In FY 2016, the company reported a Net Operating Income (OI) of Rs 279.43 crore and profit after tax (PAT) of Rs. 11.50 crore, as against OI of Rs 332.82 crore and net profit of Rs. 11.29 crore for FY 2015.

**Status of non-cooperation with previous CRA:** Not Applicable

**Any other information:** Not Applicable

## Rating History for last three years:

## Table: Rating History

| S.No | Name of Instrument | Current Rating (FY2017) | | | Chronology of Rating History for the past 3 years | | |
|---|---|---|---|---|---|---|---|
| | | Type | Amount outstanding (Rs. Crore) | Date & Rating | Date & Rating in FY2017 | Date & Rating in FY2016 | Date & Rating in FY2016 |
| | | | | March 2017 | July 2016 | February 2016 | May 2015 |
| 1 | Fund based limits | Long Term | 140.00 | [ICRA]AA(SO) (Stable) | [ICRA]AA (SO)(Stable) | [ICRA]AA (SO)(Stable) | [ICRA]BBB- (Stable) |
| 2 | Non Fund based limits | Long Term | 280.00 | [ICRA]AA (SO)(Stable) | [ICRA]AA (SO)(Stable) | [ICRA]AA (SO)(Stable) | [ICRA]A3 |
| 3 | Fund / Non Fund based limits | Long Term | 40.00 | [ICRA]AA (SO)(Stable) | [ICRA]AA (SO)(Stable) | | |
| 4 | Non Fund based limits | Long Term | 25.00 | [ICRA]BBB+ (Stable) | | | |
| 5 | Unallocated | Long Term | 65.00 | [ICRA]BBB+ (Stable) | | [ICRA]BBB- (Stable) | [ICRA]A3 |

**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**
**Details of Instrument**

| Name of the instrument | Date of issuance | Coupon rate | Maturity Date | Size of the issue (Rs. Cr) | Current Rating and Outlook |
|---|---|---|---|---|---|
| Cash Credit | | | | 140.0 | [ICRA]AA(Stable) (SO) |
| LC/BG | | | | 320.0 | [ICRA]AA(Stable) (SO) |
| LC/BG | | | | 25.0 | [ICRA]BBB+(Stable) |
| Unallocated | | | | 65.0 | [ICRA]BBB+(Stable) |

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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.
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