

October 06, 2020

## Aquatech Water Solutions Private Limited: Rating reaffirmed

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loan	40.00	40.00	[ICRA]BBB(Negative); reaffirmed
<b>Total</b>	<b>40.00</b>	<b>40.00</b>	

\*Instrument details are provided in Annexure-1

### Rationale

ICRA maintains the Negative outlook on the rating of Aquatech Water Solutions Private Limited (AWSPL), due to persisting uncertainty in Hinduja National Power Corporation Limited's (HNPCL) power purchase agreement (PPA) related dispute with Andhra Pradesh Distribution Company (APDISCOM). Due to the dispute, the HNPCL is operating at suboptimal capacities leading to low volume offtake from AWSPL resulting in subdued variable income, thereby impacting profitability and coverage indicators of AWSPL.

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 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 repayments 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 HNPCL. 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. There also exists a tail period of 12 years for the project, lending it flexibility to raise additional funds and refinance debt, if required. ICRA notes that AWSPL was operational throughout the period of nation-wide lockdown imposed in India, and continued to receive timely payments from HNPCL. The company has subcontracted the plant's operations and maintenance to its associate company, Aquatech Systems Asia Private Limited (ASA, rated [ICRA]BB+(Stable)/[ICRA]A4+) benefitting from the technical expertise as well as extended credit period for the supplies.

The rating strengths are partially offset by low utilization levels in AWSPL's plant owing to low offtake from HNPCL. AWSPL's capacity utilisation has reduced to a sub-20% level in H1FY2021, because of operational issues faced by HNPCL. The company is in talks with the counter-party to compensate for the low volume offtake, which upon fructification could augment revenues and thereby profit margins and return indicators. 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 30-40 days at present, compared to over 150 days in FY2017. Going forward, AWSPL's ability to improve its capacity utilisation remains the key sensitivity factor. Any adverse ruling on HNPCL's PPA agreement with APDISCOM, slippages in receivables from customer, revision in AWSPL's 'take or pay' arrangement with HNPCL or dilution in ring fencing terms from the lenders remain key monitorables

## 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. 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 support profitable operation. The variable component is primarily linked with AWSPL's capacity utilisation. The revenue from the variable component in the recent times has remained significantly 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 prioritized 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.

**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 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.

**Low capacity utilization leading to modest capitalization and coverage indicators**- AWSPL's capacity utilization has remained below 35% since inception due to persisting operational issues in HNPCL. This has resulted in lower operating income leading to stretched capitalization and coverage indicators with gearing of 3.9 times, DSCR of 0.9 times in FY2019. DSCR is likely to remain below 1.1 times in the near term; nevertheless, waterfall mechanism ensure debt repayment and DSRA top-up is prioritized over operational expenses provides comfort. As on August 31, 2020, AWSPL had adequate funds in DSRA account to take care of next 10 months of debt repayment obligations.

**Modest scale of operations with limited scope for expansion**- The water treatment plant is the only project executed by AWSPL and it operates at an installed capacity of 12 million litres per day. The company's operations are constrained by low capacity utilization and being a captive plant, limits scope for expansion or obtaining other customers. Because of its single unit within HNPCL manufacturing plant, the company is also exposed to high asset concentration risk.

## Liquidity position: Adequate

AWSPL maintains a DSRA of two quarters of interest and principal payments and one quarter of repayment in fixed deposit. Apart from this, there is a tight ring fencing mechanism prioritizing debt repayment and DSRA replenishment over operational expenses, ensuring adequate liquidity for debt repayments.

## Rating sensitivities

**Positive triggers** – The outlook can be revised to stable in case of improved clarity regarding HNPCL’s PPA with APDISCOM. Upward revision in tariff by HNPCL, which will improve DSCR will be a credit positive.

**Negative triggers** – Increase in counterparty risk i.e. deterioration in credit profile of HNPCL or increase in receivables from HNPCL above 60 days on sustained basis; or dilution of ring fencing arrangement with lenders. Deterioration in operating performance, which could impact cash flows or any adverse revision in take or pay arrangement with its key customer

## Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">Corporate Credit Rating Methodology</a>
Parent/Group Support	NA
Consolidation/Standalone	Standalone

## 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 West Asian and the Asia-Pacific markets jointly with AIC.

### Key financial indicators (audited)

	<b>FY2019</b>	<b>FY2020</b>
Operating Income (Rs. crore)	13.9	14.5
PAT (Rs. crore)	0.6	1.3
OPBDIT/OI (%)	59.2%	59.5%
PAT/OI (%)	4.0%	9.0%
Total Outside Liabilities/Tangible Net Worth (times)	4.8	4.2
Total Debt/OPBDIT (times)	5.5	4.8
Interest Coverage (times)	1.5	1.7

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

**Any other information: None**

### Rating history for past three years

	Instrument	Current Rating (FY2020)			Rating History for the Past 3 Years			
		Type	Amount Rated	Amount Outstanding	Rating	FY2020	FY2019	FY2018
					06-10-2020	04-11-19	01-02-19	26-09-17
1	Term Loan	Long Term	40.00	30.6	[ICRA]BBB(Negative)	[ICRA]BBB(Negative)	[ICRA]BBB(SO)@	[ICRA]BBB (SO)(Stable)

Amount in Rs. crore

### 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](http://www.icra.in)

### Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA <i>Source: AWSPL</i>	Term Loan	Mar 2016	11.5%	Mar 2028	40.00	[ICRA]BBB(Negative)

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

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