

August 12, 2022

## Hindustan Construction Company Limited: Provisional [ICRA]B (Stable) assigned

### Summary of rating action

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Optionally Convertible Debentures (OCD)	300.0	Provisional [ICRA]B (Stable); Assigned
Non-Convertible Debenture (NCD)	900.0	Provisional [ICRA]B (Stable); Assigned
<b>Total</b>	<b>1,200.0</b>	

Rating in the absence of pending actions/documents

[ICRA]D

\*Instrument details are provided in Annexure I

### Rationale

The assigned rating factors in Hindustan Construction Company Limited's (HCC) strong order book position (order book to OI ratio of 3.3 times after adjusting for slow moving and stuck orders), which provides medium-term revenue visibility. The rating favourably factors in HCC's diversified order book across segments, geographies and clientele. In the past, it faced liquidity pressure as substantial amount of receivables were stuck in arbitration or under claims pending with the clients, which impacted its operations and resulted in delays in debt servicing. However, post implementation of the resolution plan (RP) by the lenders, the company's operational and financial performance is expected to improve.

The rating, however, is constrained by HCC's elongated working capital cycle, primarily due to sizeable receivables/work in progress being stuck in arbitration or under claims pending with the clients, leading to high NWC/OI of 78% as on March 31, 2022. However, the company has been able to manage the working capital requirements, partly by availing extended credit period from suppliers/sub-contractors and mobilisation advances from clients. Its financial performance remained weak with erosion in net worth due to losses during the last four years and high working capital intensity resulting in an elevated leverage level (TOL/TNW, which stood at 21.5 times as on March 31, 2022). Post RP implementation, Rs. 2,852 crore of debt along with Rs. 6,508 crore of awards and claims will be transferred to a new entity, i.e. Prolific Resolution Private Limited (PRPL, rated Provisional [ICRA]B (Stable)), which will help in improvement of the working capital cycle. Further, ICRA draws comfort from the cushion available in the form of unutilised arbitration BG/court BG that could be used to realise some of the awards pending in the higher courts post RP implementation. Going forward, any material deterioration in the working capital cycle from the anticipated levels over the medium term can affect its liquidity position/credit profile and will be a key rating sensitivity. ICRA notes that HCC has provided guarantees for the entire debt getting transferred at PRPL, and hence crystallisation of those guarantees will impact its credit profile.

The rating notes the stiff competition in the construction sector and the company's exposure to sizeable contingent liabilities in the form of bank guarantees, mainly for contractual performance, mobilisation advance and security deposits. The rating is constrained by execution risks as about 49% of the order book as on March 31, 2022 is in preliminary/early stage of execution with less than 25% progress.

ICRA notes that HCC has sizeable claims awarded by arbitration tribunal/courts but pending in higher courts, which can be realised in the interim by providing bank guarantees (BG) post RP implementation. While the company's operating margin is expected to improve in the near to medium term, the coverage indicators are likely to remain subdued on account of a leveraged capital structure. HCC is planning to monetise some of its non-core investments to deleverage its capital structure and improve its liquidity position. Going forward, the timely monetisation of the non-core assets and improvement in the working capital intensity remains remain crucial to boost its financial performance and liquidity position.

The Stable outlook reflects ICRA's opinion that the company will continue to benefit from its healthy order book position, strong execution capabilities, and improved liquidity position post RP implementation.

## Key rating drivers and their description

### Credit strengths

**Strong and diversified order book position; expected improvement in financial profile post implementation of RP** – The company had a strong order book position of Rs. 15,967 crore as on March 31, 2022. Adjusting for slow moving and stuck orders, OB/OI ratio was adequate at 3.3 times of the operating income in FY2022, providing healthy medium-term revenue visibility. Timely commencement and execution of these orders is critical to sustain the revenue visibility, going forward. HCC's current outstanding order-book is well-diversified with projects spread across India, from multiple segments such as transportation, hydro power, nuclear, and water projects. The transportation segment formed 52% of the unexecuted order book as on March 31, 2022, given the company's technical expertise in this segment. Further, the order book is fairly diversified in terms of projects and clients, with the top three clients contributing 39% to the total unexecuted order book and the top 10 orders accounting for 68% the unexecuted order book as on March 31, 2022. HCC's financial profile and liquidity position are expected to improve considerably post the implementation of the proposed RP. The RP is in the advance stage with the pending documentation expected to be completed shortly as per the management's commentary. Post RP implementation, Rs. 2,852 crore of debt along with Rs. 6,508 crore of awards and claims will be transferred to a new entity, i.e. PRPL (rated Provisional [ICRA]B (Stable)), which will help in improving HCC's working capital intensity and coverage metrics. Additionally, it will be able to secure fresh orders, given the unutilised BG available to bid for new projects, which is expected to drive the operating margins.

**Established track record and extensive experience of management team in civil construction sector** – HCC has an established track record of operations of over ten decades, supported by experienced management and demonstrated capabilities in executing relatively complex hydro and tunnelling projects at geographically diverse locations. It has proven its execution capabilities by constructing large value and technologically complex long-duration projects. The company has a fleet of well-maintained specialised equipment in its portfolio, a qualified and experienced senior management and technical collaborations, boosting its project execution capabilities. It is one of the oldest infrastructure development companies in India, founded by Seth Walchand Hirachand in 1926.

### Credit challenges

**Elongated working capital cycle and stretched liquidity position** – As a substantial amount of receivables is stuck in arbitration or under claims pending with the clients, HCC's working capital intensity remained high with NWC/OI of 78% as on March 31, 2022. However, the company has been able to manage the working capital requirements, partly by availing extended credit period from suppliers/sub-contractors and mobilisation advances from clients. Its financial performance remained weak, with erosion in net worth due to losses during the last four years and high working capital intensity resulting in an elevated leverage level (TOL/TNW, which stood at 21.5 times as on March 31, 2022). Post RP implementation, Rs. 2,852 crore of debt along with Rs. 6,508 crore of awards and claims will be transferred to a new entity, i.e. Prolific Resolution Private Limited (PRPL, rated Provisional [ICRA]B (Stable)), which will help to improve its working capital cycle. ICRA draws comfort from the cushion available in the form of unutilised arbitration BG/court BG that could be used to realise some of the awards pending in the higher courts post RP implementation. Going forward, any material deterioration in the working capital cycle from the anticipated levels over the medium term can affect its liquidity position/credit profile and will be a key rating sensitivity. ICRA notes that HCC has provided guarantees for the entire debt getting transferred at PRPL, and hence crystallisation of those guarantees will impact its credit profile.

**High execution risk** – HCC's revenue remains exposed to time and cost overrun risks, given the complex nature of the projects being executed. Moreover, ~49% of its outstanding order book is in the preliminary stage with less than 25% progress. Out of the 10 projects with less than 25% progress, two projects worth Rs. 973 crore are yet to start and Rs. 3,158-crore orders are

stuck/slow moving. HCC’s ability to achieve scheduled progress within the budgeted costs and timelines would remain important to achieve meaningful profits. Any material deviation from the anticipated billing would increase its dependence on realisation of claims to meet its debt servicing requirements.

**Dependence on asset monetisation** – The company plans to monetise some of its non-core investments to deleverage its capital structure and improve its liquidity position. Going forward, timely monetisation of the non-core assets and an improvement in the working capital intensity remain crucial to boost its financial performance and liquidity position.

**Heightened competition, input cost spike could exert pressure on profitability** – The domestic civil construction industry is fragmented and highly competitive, evident from the moderate bid to success ratios. Garnering the adequate number of projects and ensuring their movement remains the key for optimal use of resources and ultimately profitability. The competition has further increased because of the relaxation in the bidding criteria. This, coupled with the increase in input cost, could exert pressure on HCC’s profitability. ICRA notes that there is a built-in price escalation clause in most of the contracts, which protects the operating margin from raw material price fluctuation risk to some extent.

**Sizeable contingent liabilities and risk of BG invocation** – Notwithstanding HCC’s strong execution capabilities, any sizeable invocation of performance guarantees (BG) would affect the company’s liquidity and financial risk profile. In this regard, ICRA takes comfort from the condition in RP wherein, any number of BGs devolved up to six months post RP implementation are to be considered for conversion into OCDs and to be repaid as per the existing OCD payment terms. Further, with creation of adequate liquidity buffer, the company would be able to provide cash support to its various projects that have been stuck due to the lack of fund availability for its working capital requirements. This will get the stuck projects moving with efficient execution rate resulting in reduction in BG invocation risk.

### Liquidity position: Stretched

HCC had unencumbered cash and bank balance of ~Rs. 307 crore as on June 30, 2022. It has near-term debt obligation including interest of ~Rs. 307 crore in FY2023. Timely realisation of claims, asset monetisation, and improvement in the working capital intensity will remain crucial for the company to improve its liquidity.

### Rating sensitivities

**Positive factors** – ICRA could upgrade the rating upon demonstration of material improvement in its working capital intensity, operating profitability, debt coverage metrics, and the liquidity profile while maintaining its overall scale of operations.

**Negative factors** – Negative pressure on HCC’s rating could arise if delay in asset monetisation or inability to improve working capital cycle or continued pressure on earnings impacts the company’s liquidity or the overall financial profile.

### Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">Corporate Credit Rating Methodology</a> <a href="#">Construction Entities Methodology</a> <a href="#">ICRA’s Policy on Assigning Provisional Ratings</a>
Parent/Group Support	Not Applicable
Consolidation/Standalone	Consolidation

## Pending actions/documents required to be completed for conversion of provisional rating into final

The assigned rating is provisional and would be converted into final upon:

1. Finalisation/ signing of the term sheet by all the lenders for the restructured loan (proposed NCD/OCD)

### Validity of the provisional rating

In case the debt instrument/borrowing facility for which a provisional rating has been assigned is subsequently issued, the provisional rating would have to be converted into a final rating within 90 days (validity period) from the date of issuance of the debt instrument. If considered appropriate, the validity period may be extended by a further 90 days for converting the provisional rating into final, in circumstances where the rated entity expressly indicates its intention to complete the pending actions/documents over the near term. Under no circumstances shall the validity period be extended beyond 180 days from the date of issuance. For further details, refer to ICRA's Policy on Provisional Ratings available at [www.icra.in](http://www.icra.in).

If neither the pending actions/documents nor the issuance is completed after one year of the assignment of the provisional rating, ICRA would withdraw the provisional rating. However, the validity period may be extended beyond one year, subject to the conditions outlined in ICRA's Policy on Provisional Ratings available at [www.icra.in](http://www.icra.in).

### Risks associated with the provisional rating

In case the issuance is completed, but the pending actions/documents are not completed by the entity within 90 days (validity period) from the date of issuance, the provisional rating will be converted into final upon the review of the required actions/documents to the extent these are completed by the end of the validity period. This implies that the provisional rating may even be revised at the end of the validity period, while being converted into final, to a level commensurate with the rating in absence of the pending actions/documents (as disclosed earlier in the rationale). ICRA may consider extending the validity period in accordance with its Policy on Provisional Ratings available at [www.icra.in](http://www.icra.in).

### About the company

Incorporated in 1926, Hindustan Construction Company Limited (HCC) is the flagship company of the Hindustan Construction Company Group (HCC Group) and is involved in engineering and construction of infrastructure projects such as dams, tunnels, bridges, hydro, nuclear and thermal power plants, expressways and roads, marine works, water supply, irrigation systems and industrial buildings across the country. The HCC Group's principal business areas can be classified into four broad verticals: 1) Engineering and Construction (E&C), 2) Infrastructure Development, 3) Real Estate and 4) Urban Development and Management. While the E&C vertical is undertaken by HCC, the rest of the activities are carried out through separate subsidiary companies. It is one of the oldest infrastructure development companies in India, founded by Mr. Seth Walchand Hirachand.

### Key financial indicators (audited)

Standalone	FY2021	FY2022
Operating income (Rs. crore)	2589.7	4666.3
PAT (Rs. crore)	-566.5	-153.1
OPBDIT/OI (%)	11.6%	16.9%
PAT/OI (%)	-21.9%	-3.3%
Total outside liabilities/Tangible net worth (times)	15.4	21.5
Total debt/OPBDIT (times)	14.3	8.2
Interest coverage (times)	0.4	0.8

Source: Company data; 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 July 31, 2022 (Rs. crore)	Date & Rating in	Date & Rating in	Date & Rating in	Date & Rating in
				August 12, 2022	FY2022	FY2021	FY2020
<b>1</b> <b>Optionally Convertible Debentures</b>	Long-term	300.0	-	Provisional [ICRA]B (Stable)	-	-	-
<b>2</b> <b>Non-Convertible Debenture</b>	Long-term	900.0	-	Provisional [ICRA]B (Stable)	-	-	-

**Complexity level of the rated instrument**

Instrument	Complexity Indicator
<b>Optionally Convertible Debentures</b>	Simple
<b>Non-Convertible Debenture</b>	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](http://www.icra.in)

**Annexure-I: Instrument details**

ISIN No.	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Optionally Convertible Debentures	-	-	-	300.0	Provisional [ICRA]B (Stable)
NA	Non-Convertible Debenture	-	-	-	900.0	Provisional [ICRA]B (Stable)

Source: Company

**Annexure-II: List of entities considered for consolidated analysis**

Company Name	Ownership	Consolidation Approach
Prolific Resolution Private Limited	100.00%	Full Consolidation

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

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### Branches



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