KEC International Limited

December 28, 2018

Summary of rating action

Instrument	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based Limits	1,800	1,800	[ICRA]AA- (Stable); reaffirmed
Non-fund Based Limits	11,200	11,200	[ICRA]AA- (Stable) / [ICRA]A1+; reaffirmed
Short term Fund based facility	0	1000	[ICRA]A1+ reaffirmed
Non-convertible Debenture (NCD) Programme	250	250	[ICRA]AA- (Stable); reaffirmed
Total	**13,250**	**14,250**	

*instrument details are provided in Annexure-1

Rationale

The ratings reaffirmation takes into account KEC International Limited's (KEC) position as an established engineering, procurement and construction (EPC) company with a strong market position in the power transmission EPC segment. The company's order book, which stood at ~Rs. 20,135 crore (two times the OI in FY2018) as on September 30, 2018, reflects healthy revenue visibility in the near-to-medium term. The order intake for the transmission and distribution business remained strong in H1 FY2019 and this coupled with the order inflows in the Railway division (Rs. 1745 crore in H1 FY2019 vis-à-vis Rs. 115 crore in H1 FY 2018) supported the growth in the company's order-book position. The ratings also take into account that its profitability levels are expected to be sustained on the strengths of its strong market position with execution capabilities as well as an increasing scale of new business areas such as EPC for Railways. The ratings further continue to take into account KEC's diversified geographical presence with 40–50% of its revenues earned from overseas projects, including the market entry into new geographies such as South-east Asia and African regions over the last 12 months. With the acquisition of SAE Towers in September 2010, KEC also gained access to the American markets as well as to the EPC opportunities in Brazil, with manufacturing capacities in Brazil and Mexico. The long-term demand prospects for the power transmission and distribution project business in India as well as in key foreign countries, where KEC operates, remain favourable.

The ratings, however, are constrained by the significant increase in the working capital intensity (NWC/OI) as on September 30, 2018, especially for the EPC orders in Railway business due to a decline in creditors, inventory requirements for manufacturing of structures required and higher advances to suppliers. While the receivables have remained high for the company, the advances to suppliers have increased by almost Rs. 230 crore (as on end September 2018 vis-à-vis March 2018) driven by the requirements of the suppliers in the Railway business. In addition, its inventory requirements increased during the current fiscal due to higher commodity prices as well as higher requirements for the Railways segment. Consequently, the working capital borrowings (including acceptances) increased to ~Rs. 3850 crore as on end September 2018 from ~Rs. 2975 crore as on end March 2018. The ratings continue to remain constrained by the exposure of KEC's profitability to price volatility of the key raw materials, particularly for international EPC contracts that are fixed price in nature. However, the company has a strong price hedging mechanism for commodities such as aluminium and zinc, thereby minimising its risks to a certain extent. Given its business in many overseas countries, the operations remain exposed to geo-political risks and counterparty credit risk to some extent. With respect to credit risks from the overseas customers in regions such as Africa and Central Asia, most of the projects are funded by multilateral funding agencies and in some cases the payments from overseas customers are backed by a letter of credit (LC).

With growing scale of operations and higher working capital requirements in current fiscal, the company's working capital limit utilisation has increased and as a result, timely enhancement in the working capital limits and ability to control the working capital requirements remains a key monitorable. Nonetheless, it has adequate liquidity position backed by the buffer available in the undrawn limits against the drawing power as well as unutilised bill discounting (purchase bills) limits.

Outlook: Stable

The outlook may be revised to Positive in case of any significant reduction in the working capital requirement in a sustained manner. The outlook may be revised to Negative in case of any further increase in the working capital intensity of the company or any material decline in the profitability level.

Key rating drivers:

Credit strengths

Healthy order-book position provides revenue visibility for the near-to-medium term - KEC's order book was robust at Rs. 20,125 crore as on September 30, 2018 on a consolidated basis, i.e. two times the revenues of FY2018. In H1 FY2019, the company obtained orders of about Rs. 7,932 crore, of which transmission and distribution (T&D) order inflows accounted for about 63%. The company also witnessed healthy order inflows from the Railways segment that accounted for 22% of the orders obtained in H1 FY2019.

Diversified geographical presence across the globe with a substantial portion of revenues earned from the overseas projects - The company has a wide geographical presence with about 45-50% of its current order book contributed by foreign countries. It has an established presence in the Middle East, Africa, Brazil, SAARC and South-east Asia region.

Healthy profitability levels supported by improvement in execution efficiency, faster turnaround and lower execution cycle - The operating profitability levels continues to remain healthy (OPBDITA/OI of 11.1% in FY2018 and 10.4% in H1 FY2019) supported by the enhancement of the execution efficiency with faster turnaround, and improved margins from the Railway business.

Favourable long-term demand prospects for power transmission and distribution infrastructure - In the domestic market, Power Grid Corporation of India Limited (PGCIL), private sector transmission lines developers and state transmission entities are the key customers for transmission and distribution. The demand for transmission line and substation is expected to remain favourable in the long-term, given the strong need for augmentation in the existing inter-regional transmission capacity owing to inadequacy/capacity constraints as well as the need to manage regional differences in power generation and power requirements. In terms of international markets, the underdeveloped markets of Africa, SAARC, the Middle East and Latin America present a favourable market potential for setting up transmission lines and substation infrastructure. (Source: Industry).

Credit challenges

Increase in short-term borrowing levels, with higher working capital requirement - The company's working capital intensity has significantly increased in the current financial year on account of higher receivables, coupled with a decline in creditors and higher advances to suppliers. While receivables continue to remain high in the current fiscal, the advances to suppliers have increased by Rs. 232crore (Rs. 338 crore as on end September 2018 vis-à-vis Rs. 106 crore as on March 2018) driven by the requirement of the key suppliers in the Railway business. In addition, the inventory requirements increased during the current fiscal due to higher commodity prices and higher requirement for the Railways segment. Consequently, the working capital borrowings (including acceptances) increased to ~Rs. 3850 crore as on end September 2018 from ~Rs. 2975 crore as on end March 2018.

Operating margins remain vulnerable to price volatility of key raw materials, particularly for fixed-price international EPC contracts - The key raw materials for tower manufacturing (steel and zinc), the cost of several other bought-out components required for installation of transmission line projects make up for KEC's raw material cost. Given the fact that order execution takes about 18-24 months, the operating profitability remains vulnerable to volatility in the prices of key raw materials, particularly in the case of international contracts that are normally fixed price in nature. However, the risk is mitigated to some extent owing to the commodity price hedging undertaken by the company.

Operations exposed to currency risks and counterparty credit risks - Overseas sales/projects continue to contribute significantly to KEC's overall revenues. Therefore, its operations are exposed to currency risks and counterparty credit risks as well as geo-political risks. The currency risk, however, is mitigated to some extent by the natural hedge (expenses incurred in foreign currency), forward contracts and utilisation the foreign currency-denominated working capital borrowings.

Liquidity position

The company's liquidity position remains comfortable with free cash and liquid investments of Rs. 270 crore as on end September 2018 along with ~Rs. 500-crore undrawn line of credit, which is supported by a cushion of ~Rs. 700 crore in the drawing power. In addition to the fund-based facilities, it also has access to ~Rs. 300-crore unutilised bill discounting facility, which can be used for vendor discounting, if required. Further, KEC has ongoing plans for an enhancement of the working capital limits, which will provide further cushion to the current liquidity position.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology
Parent/Group Support	Not applicable
Consolidation/Standalone	The ratings are based on the consolidated financial profile of the company. The list of companies that are consolidated to arrive at the rating are given in Annexure 2 below.

About the company:

KEC was established in 1945 and was taken over by R. P. Goenka (RPG) Enterprises in 1982 and renamed KEC International Limited in 1984. The company is mainly in the business of executing power transmission and distribution, Railways, civil and solar projects on an EPC basis. It also manufactures power and telecom cables. KEC is one of the largest power transmission EPC companies in the world with presence in about 60 countries, a strong presence in India, the Middle East, Africa, South Asia the Americas and Central Asia. In September 2010, KEC acquired SAE Towers LLC, headquartered in Houston (USA) and mainly involved in the business of design, manufacture and supply of transmission towers. At present, KEC has three tower-manufacturing facilities in India (Nagpur, Jaipur and Jabalpur) and one tower-manufacturing facility each in Mexico and Brazil, with a combined manufacturing capacity of 311,200 metric tonne per annum. KEC also has cable-manufacturing (power and telecom) facilities in Mysore and near Vadodara.

Key financial indicators (Audited)

	FY2017	FY2018
Operating Income (Rs. crore)	8584.4	10058.0
PAT (Rs. crore)	304.8	460.4
OPBDIT/OI (%)	10.9%	11.1%
RoCE (%)	18.9%	27.1%
Total Debt/TNW (times)	1.3	0.9
Total Debt/OPBDIT (times)	2.3	1.6
Interest Coverage (times)	2.8	3.3

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Current Rating (FY2019)					Chronology of Rating History for the past 3 years				
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs.crore)*	Date and Rating		Date and Rating in FY2018		Date and Rating in FY2017		Date and Rating in FY2016
					December 2018	July 2018	January 2018	September 2017	December 2016	October 2016	December 2015
1	Fund-based Limits	Long Term	1,800	1,309	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]A+(Positive)	[ICRA]A+(Stable)	-	[ICRA]A+(Stable)
2	Non-fund Based Limits	Long Term /Short Term	11,200	8,393	[ICRA]AA-(Stable)/ [ICRA]A1+	[ICRA]AA-(Stable)/ [ICRA]A1+	[ICRA]AA-(Stable)/ [ICRA]A1+	[ICRA]A+(Positive) / [ICRA]A1+	[ICRA]A+(Stable)/ [ICRA]A1+	-	[ICRA]A+(Stable)/ [ICRA]A1
3	NCD programme	Long Term	250	250	[ICRA]AA-(Stable)	[ICRA]AA-(Stable) outstanding	[ICRA]AA-(Stable)	[ICRA]A+(Positive)	[ICRA]A+(Stable)	[ICRA]A+(Stable)	-
4	Short term Fund based facility^	Short Term	1000	718	[ICRA]A1+	-	-	-	-	-	-

***as on end October 2018; ^includes bill discounting facility**

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: Instrument Details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook

-	Fund-based Limits	-	-	-	1,800	[ICRA]AA- (Stable)
-	Non-fund Based Limits	-	-	-	11,200	[ICRA]AA- (Stable)/ [ICRA]A1+
-	Bill Discounting	-	-	-	1000	[ICRA]A1+
INE389H07037	NCD programme-I	October 2016	Nil	FY 2021	150	[ICRA]AA- (Stable)
INE389H07045	NCD programme-II	October 2016	Nil	FY2022	50	[ICRA]AA- (Stable)
INE389H07052	NCD programme-III	October 2016	Nil	FY2022	50	[ICRA]AA- (Stable)

Source: KEC International Limited

Annexure-2: List of companies considered for consolidation

Company Name	Ownership	Consolidation Approach
RPG Transmission Nigeria Limited	100%	Fully consolidated
KEC Global FZ-LLC-Ras UL Khaimah	100%	Fully consolidated
KEC Investment Holdings, Mauritius	100%	Fully consolidated
KEC Global Mauritius	100%	Fully consolidated
KEC Power India Private Limited	100%	Fully consolidated
KEC Bikaner Sikar Transmission Private Limited	99.99%	Fully consolidated
SAE Towers Holdings LLC	100%	Fully consolidated
SAE Towers Brazil Subsidiary Company LLC	100%	Fully consolidated
SAE Towers Mexico Subsidiary holding Company LLC	100%	Fully consolidated
SAE Towers Mexico S de RL de CV	100%	Fully consolidated
SAE Towers Brazil Torres de Transmission Ltda	100%	Fully consolidated
SAE Engenharia E ConstrucaoLtda	100%	Fully consolidated
SAE Engineering and Construction Services, S de RL de CV	100%	Fully consolidated
SAE Towers Limited	100%	Fully consolidated
SAE Prestadora de Servicious Mexico, S de RL de CV	100%	Fully consolidated
KEC International (Malaysia) SDN BHD	100%	Fully consolidated

Source: KEC International Limited

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About ICRA Limited:

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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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