March 30, 2023

# Hical Technologies Private Limited: Ratings downgraded to [ICRA]BB+/[ICRA]A4+; outlook revised to Negative

## Summary of rating action

| Instrument* | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action |
|---|---|---|---|
| **Long-term-Term loan** | 16.20 | 16.20 | [ICRA]BB+; rating downgraded from [ICRA]BBB- and outlook revised to Negative from Stable |
| **Long-term-Cash credit (sublimit of PCFC)** | (5.00) | (5.00) | [ICRA]BB+; rating downgraded from [ICRA]BBB- and outlook revised to Negative from Stable |
| **Short-term-EPC/PCFC** | 40.00 | 40.00 | [ICRA]A4+; rating downgraded from [ICRA]A3 |
| **Short-term – Non-fund based limits** | 3.00 | 3.00 | [ICRA]A4+; rating downgraded from [ICRA]A3 |
| **Long-term/Short-term unallocated** | 0.80 | 0.80 | [ICRA]BB+/ [ICRA]A4+; rating downgraded from [ICRA]BBB-/ [ICRA]A3 and outlook revised to Negative from Sable |
| **Total** | **60.00** | **60.00** | |

**Instrument details are provided in Annexure-I*

## Rationale

For arriving at the ratings, ICRA has consolidated the financials of the Hical Group, comprising Hical Technologies Private Limited (HTPL), Yagachi Technologies Private Limited (YTPL) and Hical NSE Electronics Pvt Ltd (HNSE), referred to as the Group as these entities have strong operational and financial linkages, and share a common management.

The ratings downgrade takes into account the weaker-than-expected recovery in the earnings of the Group in FY2022 and 9M FY2023 leading to adverse leverage indicators. The rating action also reflects the Hical Group's stretched liquidity position, characterised by high utilisation of working capital limits and elevated inventory holding. The utilisation of working capital limits remained high due to delays in recovering receivables/debtors following the pandemic. The requirement of minimum order quantity and large delivery lead times for the import of electronic components kept the inventory holding elevated. This has led to a deterioration of the working capital intensity to 51% in FY2022 from 37-40% in FY2019/ FY2020. Due to high utilisation of working capital limits, and negative free cash flows, the company remains exposed to cash-flow timing mismatches, going forward. The credit metrics of the Group declined in FY2022 (Total Debt to OPBIDTA[1] rising to 18.7 times in FY2022 from 3.2 times in FY2020 and interest coverage declining to 1.8 times in FY2022 from 4.2 times in FY2020). ICRA believes that while some improvement is expected in FY2023, however, the credit metrics are expected to remain suppressed in FY2023 as well. In addition, ICRA notes that while a pick-up in order inflows and execution were witnessed in Q4 FY2023, and the Group is targeting a revenue growth of 20-25% YoY in FY2024, the company's ability to effectively manage liquidity during this period of growth remains a key monitorable from the credit perspective. The ratings are also constrained by HTPL's high sector and customer concentration risks, with the top-five customers accounting for more than 50% of its revenue in FY2022. The Group remains exposed to the risk of high foreign currency fluctuations and has booked forex losses of ~Rs. 4-5 crore in FY2023 because of steep depreciation in the INR against forward contracts.

However, the ratings favourably factor in the established track record of the company and the promoters' extensive experience in designing and manufacturing of electromechanical components, automated test equipment, data acquisition and control

[1] *Operating Profit Before Interest, Depreciation, Taxes, and Amortization*

systems, precision machining components, sheet metal mechanical integration, cable harness, and systems integration. The ratings note the Hical Group's diversified product profile in the aerospace, automotive and industrial segments and its renowned international client base across geographies. The order book position was healthy at a level of more than Rs. 200 crore as on January 31, 2023, supporting the revenue visibility.

The Negative outlook on the [ICRA]BB rating reflects ICRA's opinions that while the revenues and profits are expected to improve in FY2024, the relatively higher scheduled debt repayment obligations, limited headroom in working capital limits, and organic growth plans are expected to keep the liquidity profile under pressure in the near term.

## Key rating drivers and their description

### Credit strengths

**Extensive experience of promotors -** The company's promotors have extensive experience of more than 25 years in designing and manufacturing electromechanical components, automated test equipment, data acquisition and control systems, precision machining components, sheet metal mechanical integration, cable harness, and systems integration. The top management personnel are high-qualified technicians and are involved in the Group's day-to-day operations. The extensive experience of the promoters has helped the Group to gradually grow the business through acquisition of new customers and repeat orders from the existing customers.

**Diverse products across aerospace, automotive and industrial segments** - HTPL has an established track record in manufacturing electromagnetic components like transformers (planar, helical, toroid, foil wound and hybrid), inductors, solenoids, and motors catering to the aerospace, defence and industrial verticals. Also, the Group manufactures tie rod, ball housing, shaft joints, shaft and pipe joint assembly, pinch bolt yoke assembly, etc, catering to the automotive segment.

**Reputed client base -** The Hical Group's customer profile consists of global aerospace majors such as Hamilton Sundstrand Corporation (UTAS), Goodrich Aerospace Services Pvt. Ltd. (UTAS), Thales Solutions Asia Pte Limited, ScioTeq BVBA, Korry Electronics Co., Eaton Aerospace, Hs De Puerto Rico, Inc. and Moog Controls (India) Private Limited, etc. In the industrial division, the company caters to customers such as ST Microelectronics Pte Limited, Accudyne Industries India Pvt Ltd, Vacuumschmelze Gmbh & Co., Raychem RPG Pvt Ltd, TE Connectivity Limited, Tyco Electronics UK Ltd.

### Credit challenges

**Lower-than-expected recovery of earnings and elevated debt levels led to leverage indicators being significantly weaker than expected in FY2023 -** The Group's revenue declined by over 26% to Rs. 100.36 crore in FY2022 from Rs. 136.58 crore in FY2020 owing to a weak demand environment in the aerospace division globally amid the pandemic. Consequently, the Group's earnings plummeted in FY2021/FY2022. While there has been a recovery in earnings in FY2023, the same remained lower than expected, leading to adverse leverage indicators (Total debt to OPBITDA for FY2023 being revised up to 6.0-6.5 times from 2.5-3.0 times expected earlier). The coverage and capitalisation indicators have also deteriorated significantly with interest coverage at 1.8 times and DSCR[2] at 1.3 times in FY2022 and TOL/TNW[3] at 1.8 times as on March 31, 2022, owing to a significant decline in absolute earnings. However, there has been a pick-up in order inflows lately, and the order book position was healthy at a level of more than Rs. 200 crore as on January 31, 2023 supporting the revenue visibility. While the revenues and profits are expected to improve meaningfully from Q4 FY2023, the relatively higher debt repayment obligations in the near term are expected to keep the liquidity profile under pressure.

**High utilisation of working capital limits lead to limited headroom available for undrawn lines and stretched liquidity** – There has been high utilisation of working capital limits averaging at 91% from October 2021 to February 2023 and the peak utilisation

[2] *Debt Service Coverage Ratio*

[3] *Total Outside Liabilities/ Tangible Net Worth*

reached 99% in February 2023. Due to high utilisation of working capital limits, and negative free cash flows, the company remains exposed to the risk of cash flow timing mismatches. The company has obtained additional fund-based working capital limits of around Rs. 17 crore (increasing to Rs. 57 crore from Rs. 40 crore) in FY2022 to fund its working capital requirements. ICRA notes that the ability to bring in additional working capital would be essential to fund future revenue growth and will be a key credit monitorable.

**Increase in working capital intensity due to delay in customer collections and long lead times for inventory procurement lead to negative free cash flows -** The net working capital has increased due to rise in inventory levels (as the Group imports electronic components of minimum order quantity and large delivery lead times) and with slower recoverability from the debtors (delay in customer collections). This has led to negative free cash flows in FY2022, and is likely to continue in FY2023 as well. The net working capital intensity increased to 51% in FY2022 from 37-40% in FY2019/FY2020, owing to the high receivable days and inventory levels. The receivables have also been higher given the low bargaining power of the Group with the large aerospace companies. Nonetheless, the renowned clientele reduces the counterparty risks to an extent. Going forward, the working capital intensity is expected to remain elevated in FY2023 as well, as the company scales up its execution in Q4 FY2023 after a lacklustre performance in 9M FY2023.

**High customer and sector concentration risks -** Most of HTPL's customers are in the aerospace segment, thereby indicating the sector concentration risk. As a result, the Group is exposed to any cyclicality or downturns in the industry as witnessed in FY2021 and FY2022. This apart, the company's customer concentration continued to be high in FY2022, with the top-five customers accounting for more than 50% of its revenue in FY2022. Nonetheless, the long track record of repeat orders across segments and the Group's diversification into the industrial and automotive segments are expected to mitigate the risk to some extent.

**Exposure to foreign currency fluctuation risk -** With imports accounting for approximately 50-60% of the raw material requirement in FY2022, the company's margins remain exposed to fluctuations in foreign exchange rates. However, with export sales accounting for around 80-90% of its revenue, such risks are partly mitigated due to the natural hedge from export earnings. However, the Group booked forex losses of ~Rs. 4-5 crore in FY2023 because of steep depreciation in the INR against forward contracts.

## Liquidity position- Stretched

HTPL's average utilisation of working capital limits stood high at 91% between October 2021 and February 2023, and the peak utilisation reached 99% in February 2023. Therefore, the Group's liquidity position remains stretched. The Group has a planned capex in FY2023 and FY2024 for the development of land in Aerospace Park, Bengaluru. The Group also has high repayment obligations of Rs. 4.95 crore in FY2023 and Rs. 5.78 crore in FY2024, which, along with high working capital-intensive nature of operations, would constrain the free cash flows.

## Rating sensitivities

**Positive factors** – The outlook would be revised to Stable, if a sustained growth in revenues and profits leads to an improvement in liquidity and leverage metrics.

**Negative factors** - Pressure on the ratings may arise, if any further reduction in the company's profitability and cash accruals or further increase in the working capital intensity weakens its liquidity position. Specific credit metrics that could lead to a downgrade of ratings include Total/OPBIDTA of more than 4 times, on a sustained basis.

## 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 consolidated the financials of HTPL, its associate YTPL and its Joint Venture HNSE, given the strong operational and financial linkages among the companies. |

## About the company

HTPL (formerly known as Hical Aerospace Private Limited) was established in 2011 and had taken over the manufacturing and engineering division from Hical Infra Private Limited (formerly known as Hical Technologies Private Limited), which was established in 1990. It primarily manufactures high reliability electro-mechanical products like transformers, inductors, solenoids, motors, electromagnetic assemblies and provides advanced integration and engineering services to leading aerospace, railways, auto, medical and specialty industrial companies across the world. It is a 100% export-oriented unit and supplies to its customers in Europe, the US and Asia. YTPL, established in 2008, manufactures electromagnetics, electronic assemblies and plastic moulding components. YTPL's shareholding is 29.5% held by HTPL, while the balance 70.5% is held by HTPL's promoters. Hical NSE Electronics Pvt Ltd is a Joint Venture between Hical Technologies Pvt Ltd, India (51%) & NSE Industries, France (49%). This JV has been established to cater to the Indian offset requirements.

### Key financial indicators -Consolidated**

| HTPL + YTPL + HNSE | FY2021 | FY2022 |
|---|---|---|
| **Operating income** | 120.7 | 125.6 |
| **PAT** | (1.8) | (1.5) |
| **OPBDIT/OI** | 5.9% | 2.3% |
| **PAT/OI** | (1.4%) | (1.1%) |
| **Total outside liabilities/Tangible net worth (times)** | 1.5 | 1.8 |
| **Total debt/OPBDIT (times)** | 6.9 | 18.7 |
| **Interest coverage (times)** | 2.6 | 1.8 |

*PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation;**consolidation done by ICRA based on elimination of inter-group transactions based on available disclosures*

### Key financial indicators -Standalone

| HTPL | FY2021 | FY2022 |
|---|---|---|
| **Operating income** | 82.4 | 100.4 |
| **PAT** | (3.6) | (1.6) |
| **OPBDIT/OI** | 1.7% | 7.3% |
| **PAT/OI** | (4.4%) | (1.6%) |
| **Total outside liabilities/Tangible net worth (times)** | 1.2 | 2.2 |
| **Total debt/OPBDIT (times)** | 26.8 | 8.5 |
| **Interest coverage (times)** | 0.8 | 4.5 |

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 of Mar 31, 2022 (Rs. crore) | Date & rating in FY2023 | Date & rating in FY2022 | Date & rating in FY2021 | | | Date & rating in FY2020 |
| | | | | | March 30, 2023 | Dec 09,2021 | Nov 17,2020 | Sep 29,2020 | Sep 09,2020 | Nov 28,2019 |
| 1 | Cash Credit (Sublimit of PCFC) | Long Term | (5.00) | - | [ICRA]BB+(Negative) | [ICRA]BBB - (Stable) | [ICRA]BBB - (Stable) | [ICRA]BBB - (Stable) | [ICRA]BB+(Stable ) ISSUER NOT COOPERATING* | [ICRA]BBB - (Stable) |
| 2 | Term Loan | Long Term | 16.20 | 15.84 | [ICRA]BB+(Negative) | [ICRA]BBB - (Stable) | [ICRA]BBB - (Stable) | [ICRA]BBB - (Stable) | [ICRA]BB+(Stable ) ISSUER NOT COOPERATING* | [ICRA]BBB - (Stable) |
| 3 | EPC/PCFC | Short term | 40.00 | - | [ICRA]A4+ | [ICRA]A3 | [ICRA]A3 | [ICRA]A3 | [ICRA]A4+ ISSUER NOT COOPERATING* | [ICRA]A3 |
| 4 | Non-fund based limits | Short term | 3.00 | - | [ICRA]A4+ | [ICRA]A3 | [ICRA]A3 | [ICRA]A3 | [ICRA]A4+ ISSUER NOT COOPERATING* | [ICRA]A3 |
| 5 ` | Unallocated | Long Term / Short Term | 0.80 | - | [ICRA]BB+(Negative) / [ICRA]A4+ | [ICRA]BBB - (Stable)/ A3 | [ICRA]BBB - (Stable)/A3 | [ICRA]BBB - (Stable)/A3 | [ICRA]BB+(Stable ) /A4+ ISSUER NOT COOPERATING* | [ICRA]BBB - (Stable)/A3 |

## Complexity level of the rated instruments

| Instrument | Complexity Indicator |
|---|---|
| Long Term - Fund Based Term Loan | Simple |
| Long Term Interchangeable – Cash Credit | Simple |
| Short Term Fund Based | Very Simple |
| Short Term Non-Fund Based | Very Simple |
| Long Term/Short Term - Unallocated | NA |

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 (Sublimit of PCFC) | - | - | - | (5.00) | [ICRA]BB+(Negative) |
| **NA** | Term Loan | FY2017 | - | FY2027 | 16.20 | [ICRA]BB+(Negative) |
| **NA** | EPC/PCFC | - | - | - | 40.00 | [ICRA]A4+ |
| **NA** | Non-fund based limits - | - | - | - | 3.00 | [ICRA]A4+ |
| **NA** | Unallocated | - | - | - | 0.80 | [ICRA]BB+(Negative)/ [ICRA]A4+ |

*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 |
|---|---|---|
| Hical Technologies Private Limited | 100.0% | Full Consolidation |
| **Associate** | | |
| Yagachi Technologies Private Limited | 29.5% | Full Consolidation; as the balance equity stake is held by the promoters of HTPL, support to the associate can go from HTPL in future |
| **Joint Venture** | | |
| Hical NSE Electronics Private Limited | 51.0% | Full Consolidation |

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