

Rating Rationale

October 17, 2023 | Mumbai

Bharat Heavy Electricals Limited

Ratings Reaffirmed

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Rating Action

Total Bank Loan Facilities Rated	Rs.60000 Crore
Long Term Rating	CRISIL AA-/Negative (Reaffirmed)
Short Term Rating	CRISIL A1+ (Reaffirmed)

Note: None of the Directors on CRISIL Ratings Limited's Board are members of rating committee and thus do not participate in discussion or assignment of any ratings. The Board of Directors also does not discuss any ratings at its meetings.

1 crore = 10 million

Refer to Annexure for Details of Instruments & Bank Facilities

Detailed Rationale

CRISIL Ratings has reaffirmed its "CRISIL AA-/Negative/CRISIL A1+" ratings on the bank facilities of Bharat Heavy Electricals Limited (BHEL).

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The outlook remains "Negative" as the earnings before interest, tax, depreciation and amortisation (EBITDA) margin, adjusted for provision, improved this fiscal but remained slightly negative and the likelihood that profitability may remain constrained this fiscal due to execution of old orders in thermal segment and continued stretched working capital cycle in this fiscal.

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Revenue grew by 10% in fiscal 2023 with increasing order book and better execution. The EBITDA prior to provisioning improved but remained slightly negative on account of high metal prices and execution of old orders. The operating margin was 3.6% in fiscal 2023 with reversal of provision claims of Rs 847 crore. The profitability is expected to remain modest this fiscal due to execution of old thermal orders with fixed price contracts. A significant improvement in profitability is expected in fiscal 2025 due to higher execution of newer orders with better profitability and payment terms. Turnaround in profitability of core operations will remain a key rating sensitivity factor.

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The working capital cycle continues to be on the higher side due to sizeable receivables (including contract assets) owing to backend payment structure. Furthermore, timely payments to micro, small and medium enterprises limit flexibility to fund the working capital by stretching payables. The receivables (including contract assets) are expected to reduce in fiscal 2025 due to achievement of milestones in major thermal projects. The management's focus on improving collections along with various cost rationalisation measures could partially support cash balance and will be key monitorable.

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CRISIL Ratings has noted the various initiatives taken by BHEL such as Quality First, strategies to control raw material cost, focus on cash collection and diversifying revenue base away from the power sector. However, these efforts are yet to fructify and could be visible in terms of financial performance only over the medium term and would thus be a key monitorable.

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The ratings continue to reflect the leading market position of BHEL in the power generation and electrical equipment markets, and strong, but moderating, financial risk profile. These strengths are partially offset by structural issues in the power sector (which contributes 79% to revenue), large working capital requirement and exposure to intense competition.

Analytical Approach

CRISIL Ratings has moderately consolidated the business and financial risk profiles of BHEL's joint venture (JV), Raichur Power Corporation Ltd (RPCL), and has not considered any other subsidiary or JV. CRISIL Ratings has factored in net provisions to arrive at the operating profit before depreciation, interest and taxes.

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Please refer Annexure - List of entities consolidated, which captures the list of entities considered and their analytical treatment of consolidation.

Key Rating Drivers & Detailed Description

Strengths:

- Leading position in the power generation and electrical equipment markets**
 BHEL is the leading player in India's power and industrial electrical equipment market, accounting for over 50% of the country's installed capacity of conventional power projects. The government entity status, along with superior execution capabilities, support its dominant market presence. The company is well poised to benefit from any structural recovery in the power sector. However, timely execution of orders and realisation of receivables remain critical as operational challenges persist.
- Healthy order book**
 The company has a healthy order book of Rs 1,01,461 crore (excluding taxes) as on June 30, 2023, providing revenue visibility over the medium term. Some of the large orders received this fiscal were the Vandhe Bharat project (80 trainsets), thermal orders from NTPC and Adani, and hydro project orders from NHPC. The company is also focusing on non-coal business orders such as railways, defence, nuclear, emission control, transmission and rural electrification segments. Order inflow and profitability remain key monitorables.
- Strong, but moderating, debt protection metrics**
 The financial risk profile, though moderating over the years, remains comfortable, backed by large networth and nil term debt. Liquidity, supported by available cash balance, unutilised bank limits and commercial papers (Rs 5,000 crore), is sufficient to fund working capital and capital expenditure requirements over the medium term.

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Weaknesses:

- **Structural issues in the power sector**

The power segment has traditionally contributed to 70-80% of BHEL's revenue. Profitability remains exposed to volatility in the power sector and structural issues such as excess capacity restricting further expansions, delays in land acquisition and environmental clearances, availability of fuel and funding, and weak financial position of many state power utilities, which are key clients. Over the past several years, such issues have slowed the execution of certain projects. Although BHEL has been focusing on diversifying revenue by expanding into segments such as transportation, transmission, renewables, emission control and defence in the past few years, its performance would remain sensitive to the power sector, which forms majority of the revenue and order book.

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- **Large working capital requirement**

BHEL continues to have sizeable receivables, resulting in high working capital intensity. The risk of doubtful receivables is largely mitigated by the provisioning policy of BHEL, and because around 80% exposure is to either central or state public sector undertakings. However, the company continues to have substantial exposure of around 41% (including contract assets) to comparatively weaker state utilities such as Tamil Nadu Generation and Distribution Corporation Ltd and Telangana State Power Generation Corporation Ltd as on March 31, 2023. Thus, the ability to reduce receivables on a sustained basis remains a key monitorable.

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- **Exposure to intense competition**

BHEL operates in an increasingly competitive market as several domestic companies have entered the boiler-turbine-generator space through strategic JVs with international players, increasing the industry capacity to over 30 gigawatt (GW). BHEL has remained competitive because of its significant presence in the supercritical technology-based thermal power business, driven by its collaborative approach, capability enhancement and accelerated project delivery. Nonetheless, a few large orders in the past 2-3 years saw aggressive bidding and competition between supercritical equipment manufacturers, which will keep pricing and profitability range bound.

Liquidity: Strong

Liquidity is driven by net cash and cash equivalent (net off short-term borrowings) of around Rs 1,400 crore as on March 31, 2023, and unutilised commercial paper limits (Rs 5,000 crore). The company has nil term debt and liquidity available in the form of unutilised limit and surplus cash, which will be sufficient to cover debt obligation and meet incremental working capital requirement.

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Environment, social and governance (ESG) profile

CRISIL Ratings believes BHEL's Environment, Social and Governance (ESG) profile supports its already strong credit risk profile. The sector has a moderate environmental and social impact, primarily driven by high water consumption, and direct impact on the health and well-being of its customers.

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BHEL's focus on addressing these ESG risks support its already strong credit risk profile.

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Key ESG highlights:

- BHEL has set up nearly 34,895 megawatt peak (MWp) of capacity of solar power plants, which has helped the organisation in reducing its electricity consumption. This large-scale solarisation has helped in reducing carbon footprint of 26,964 MTCO₂-equivalent during fiscal 2023.
- BHEL has installed 126 rainwater harvesting systems and 22 effluent treatment plants (ETPs) and 16 sewage treatment plants (STPs) to manage grey water sustainably.
- The lost time injuries frequency rate is zero and the company has addressed 100% of the customer grievances.
- Its governance structure is characterised by 33% of its board comprising independent directors and split in the Chairman and CEO positions. BHEL has a committee at the board level to address investor grievances.

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There is growing importance of ESG among investors and lenders. The commitment of BHEL to ESG principles will play a key role in enhancing stakeholder confidence, given its high share of market borrowing in its overall debt and access to both domestic and foreign capital markets.

Outlook: Negative

CRISIL Ratings believes BHEL's profitability may remain constrained by the increased input cost pressure along with continued high working capital requirement, which may weaken the financial risk profile.

Rating Sensitivity factors

Upward factors

- Sustained improvement in operating revenue, with operating profit (pre-provision) above 6%, on the back of higher-than-expected order execution along with efficient raw material consumption and cost control
- Sustained net cash of over Rs 3,000 crore, driven by higher accrual from operations or reduced working capital intensity

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Downward factors

- Weakening of the business risk profile through low order intake or delay in execution of orders, resulting in reduced scale of business
- Continued operating losses at pre-provision levels in fiscal 2024 and lack of visibility of achieving more than 4% pre-provision operating margin for fiscal 2025
- Weakening of financial flexibility due to reduction in net cash position to below Rs 1,000 crore, either because of lower-than-expected cash accrual, high dividend payout or increased working capital intensity

About the Company

BHEL is an integrated power plant equipment manufacturer. The "Maharatna" public sector enterprise is one of the largest engineering and manufacturing companies in India. The Government of India holds 63.17% of equity in BHEL.

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BHEL has operations in the power and industry segments. The power group supplies power plant equipment such as turbo generators, boilers, turbines and accessories, and erects all types of plants based on gas, coal, hydro, nuclear and solar power. The industry group caters to diverse sectors such as process industries, transportation, power transmission and distribution, and defence. BHEL designs, engineers, manufactures, constructs, tests, commissions and services a wide range of products. It has 16 manufacturing units, three active JVs and operates in more than 150

project sites. It has a widespread overseas footprint with references in 83 countries.

Key Financial Indicators (CRISIL Ratings-adjusted numbers)

As on/for the period ended March 31	Unit	2023	2022
Operating income	Rs crore	23390	21233
Profit after tax (PAT)	Rs crore	439	404
PAT margin	%	1.9	1.9
Adjusted debt/adjusted networkth	Times	27186	26900
Interest coverage	Times	2.2	2.7

Any other information: Not applicable

Note on complexity levels of the rated instrument:

CRISIL Ratings` complexity levels are assigned to various types of financial instruments and are included (where applicable) in the 'Annexure - Details of Instrument' in this Rating Rationale.

CRISIL Ratings will disclose complexity level for all securities - including those that are yet to be placed - based on available information. The complexity level for instruments may be updated, where required, in the rating rationale published subsequent to the issuance of the instrument when details on such features are available.

For more details on the CRISIL Ratings` complexity levels please visit www.crisilratings.com. Users may also call the Customer Service Helpdesk with queries on specific instruments.

Annexure - Details of Instrument(s)

ISIN	Name of instrument	Date of allotment	Coupon rate (%)	Maturity date	Issue size (Rs crore)	Complexity level	Rating assigned with outlook
NA	Cash Credit	NA	NA	NA	9,000	NA	CRISIL AA-/Negative
NA	Letter of credit & Bank Guarantee	NA	NA	NA	51,000	NA	CRISIL A1+

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Annexure - List of entities consolidated

Names of Entities Consolidated	Extent of Consolidation	Rationale for Consolidation
Raichur Power Corporation Ltd	Moderate	Business and financial linkages

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Annexure - Rating History for last 3 Years

Instrument	Current			2023 (History)		2022^		2021^		2020^		Start of 2020
	Type	Outstanding Amount	Rating	Date	Rating	Date	Rating	Date	Rating	Date	Rating	
Fund Based Facilities	LT	9000.0	CRISIL AA-/Negative	30-03-23	CRISIL AA-/Negative	22-07-22	CRISIL AA-/Negative	18-06-21	CRISIL AA-/Negative	24-07-20	CRISIL AA/Negative	CRISIL AA/Stable
Non-Fund Based Facilities	ST	51000.0	CRISIL A1+	30-03-23	CRISIL A1+	22-07-22	CRISIL A1+	18-06-21	CRISIL A1+	24-07-20	CRISIL A1+	CRISIL A1+

All amounts are in Rs.Cr.

Annexure - Details of Bank Lenders & Facilities

Facility	Amount (Rs.Crore)	Name of Lender	Rating
Cash Credit	1	Axis Bank Limited	CRISIL AA-/Negative
Cash Credit	18	Canara Bank	CRISIL AA-/Negative
Cash Credit	1	IndusInd Bank Limited	CRISIL AA-/Negative
Cash Credit	1	Indian Overseas Bank	CRISIL AA-/Negative
Cash Credit	1	ICICI Bank Limited	CRISIL AA-/Negative
Cash Credit	4500	State Bank of India	CRISIL AA-/Negative
Cash Credit	1	The Federal Bank Limited	CRISIL AA-/Negative
Cash Credit	6	Bank of Baroda	CRISIL AA-/Negative
Cash Credit	500	IDBI Bank Limited	CRISIL AA-/Negative
Cash Credit	1	Kotak Mahindra Bank Limited	CRISIL AA-/Negative
Cash Credit	1	YES Bank Limited	CRISIL AA-/Negative
Cash Credit	1000	Punjab National Bank	CRISIL AA-/Negative
Cash Credit	1368	Union Bank of India	CRISIL AA-/Negative
Cash Credit	1600	HDFC Bank Limited	CRISIL AA-/Negative
Cash Credit	1	RBL Bank Limited	CRISIL AA-/Negative
Letter of credit & Bank Guarantee	999	Axis Bank Limited	CRISIL A1+
Letter of credit & Bank Guarantee	1815	Indian Bank	CRISIL A1+
Letter of credit & Bank Guarantee	1500	Punjab National Bank	CRISIL A1+
Letter of credit & Bank Guarantee	1500	Exim Bank	CRISIL A1+

Letter of credit & Bank Guarantee	23500	State Bank of India	CRISIL A1+
Letter of credit & Bank Guarantee	1100	Bank of Baroda	CRISIL A1+
Letter of credit & Bank Guarantee	3000	HDFC Bank Limited	CRISIL A1+
Letter of credit & Bank Guarantee	3347	ICICI Bank Limited	CRISIL A1+
Letter of credit & Bank Guarantee	3000	IDBI Bank Limited	CRISIL A1+
Letter of credit & Bank Guarantee	40	The Hongkong and Shanghai Banking Corporation Limited	CRISIL A1+
Letter of credit & Bank Guarantee	699	IndusInd Bank Limited	CRISIL A1+
Letter of credit & Bank Guarantee	479	Indian Overseas Bank	CRISIL A1+
Letter of credit & Bank Guarantee	699	YES Bank Limited	CRISIL A1+
Letter of credit & Bank Guarantee	399	Kotak Mahindra Bank Limited	CRISIL A1+
Letter of credit & Bank Guarantee	6600	Canara Bank	CRISIL A1+
Letter of credit & Bank Guarantee	499	The Federal Bank Limited	CRISIL A1+
Letter of credit & Bank Guarantee	399	RBL Bank Limited	CRISIL A1+
Letter of credit & Bank Guarantee	1425	Union Bank of India	CRISIL A1+

Criteria Details

Links to related criteria
CRISILs Approach to Financial Ratios
Rating criteria for manufacturing and service sector companies
CRISILs Bank Loan Ratings - process, scale and default recognition
Rating Criteria for Engineering Sector
CRISILs Criteria for rating short term debt
CRISILs Criteria for Consolidation

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