

December 05, 2019

Hero Solar Energy Pvt Ltd: Rating revised

Summary of rating action

Instrument	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-Convertible Debenture Programme (NCD)	175.0	375.0	[ICRA]A (Negative); rating revised from [ICRA]A+ (Negative)
Proposed NCD	300.0	100.0	[ICRA]A (Negative); rating revised from [ICRA]A+ (Negative)
Term Loans	200.0	200.0	[ICRA]A (Negative); rating revised from [ICRA]A+ (Negative)
Total	675.0	675.0	

**Instrument details are provided in Annexure-1*

Rationale

In order to arrive at the rating, ICRA has relied on its *Rating Methodology for Holding Companies* (link shared below). Within this framework, ICRA has combined the business and financial risk profiles of the ultimate renewable energy holding company of the Hero Group in India – Hero Future Energies Pvt Ltd (HFEPL) – and Hero Wind Energy Pvt Ltd (HWEPL) and Hero Solar Energy Pvt Ltd (HSEPL), along with their special purpose vehicles (SPVs), which are respectively the wind and solar holding companies of the Group's Indian renewable energy operations. The rating also factors in the support from a strong parent – Bahadur Chand Investments Private Limited (BCIPL) – which is rated [ICRA]AA(Stable)/[ICRA]A1+.

While revising the rating, ICRA has noted that the actual operating performance of the company's was lower than the expected renewable energy portfolio during FY2018-FY2019 and there were higher operating expenses, which affected its revenues and cash flows. The overall non-SPV debt of the holding company remained high, impacting the Group's capital structure. Moreover, most of this debt is short to medium term in nature and the ability of the company to obtain refinancing for the same in a timely manner remains critical from a credit perspective. The outlook on the long-term rating continues to be Negative, given the ongoing challenges in the renewable energy segment, high debt levels and the near-term refinancing requirements.

Nevertheless, ICRA factors in the equity commitment of \$150 million made by Masdar, which is ultimately owned by the Government of Abu Dhabi. As on date, Masdar has already infused \$120 million, which would be primarily deployed for future equity commitments related to under-construction projects. The company also plans to repay the holding company debt of ~Rs. 150 crore through the equity infused by the strategic investor. ICRA further continues to positively factor in the large size and scale of operations of the Hero Group. The Group entities have commissioned and are operating more than 1,200 MW of wind and solar assets in India (built largely through organic route). This apart, the Group has an under-construction pipeline of ~900 MW, which is expected to take the overall Group capacity to more than ~2,000 MW in the next few years.

Apart from this, the rating action continues to factor in the strong sponsor strength, given that HWEPL and HSEPL are a part of HFEPL, which in turn is promoted by BC IPL and Brijmohan Lal Om Prakash (BMOP), a partnership firm and ultimate holding company of the Hero Group. The Group's operations have been supported by consistent fund infusion from the parent in the past as well as a \$125-million equity infusion by the International Finance Corporation (IFC) and IFC GIF, members of the World Bank Group in FY2018 and FY2019, respectively. The management team comprises experienced technocrats and investment/finance professionals. The portfolio of the operational assets is spread over multiple geographies, and is diversified among various counterparties (including discoms, Group captives, open access customers and central offtakers) and developed by varied EPC/O&M contractors, thus offering the benefits of diversification. The payment cycle from counterparties remains typical of what has been observed across the renewable energy industry. While in the case of certain offtakers such as Group captives, open access customers, Maharashtra discoms, central offtakers, etc. the payments remain regular, others such as discoms of Rajasthan, Andhra Pradesh, Hubli Electricity Supply Company Limited (HESCOM), etc. do not have a consistent payment cycle. This has led to promoters resorting to working capital (WC) funding in some of these SPVs or SPVs drawing their own WC facilities or even infusing temporary liquidity to meet debt obligations. Finally, ICRA has taken comfort that most of the operational projects have entered into long-term power purchase agreements (PPAs) with different counterparties, which mitigates demand risk to a large extent.

Despite these strengths, ICRA takes cognisance of the expansion plans of the Group with ~900 MW of projects under construction and in different stages of development. This exposes the company to execution-related risks such as time and cost overrun, which are generally associated with greenfield projects. It also creates large funding requirements, given the pipeline of under-construction projects as well as any requirements in case additional capacity is won through auctions or in case of acquisitions. ICRA takes note that though more than 1,200-MW capacity has been commissioned by the Group, only about 35% of the operational capacity has more than three years track record, indicating that the asset fleet is relatively young. ICRA also notes that the renewable energy sector in India is at present facing execution headwinds, given the regulatory delays in PSA tariff adoption, delays in land acquisition as well as lack of availability of ISTS transmission infrastructure. This in turn may affect the company's ability to achieve the financial closure for the under-implementation projects and execution of such projects in a timely manner. While the projects in the renewable energy space in India have now been awarded through competitive bidding (leading to a fall in tariffs and improvement in tariff competitiveness, in turn mitigating offtake risk for developers), these have led to viability-related challenges for IPPs. In this scenario, the ability of the Group to keep actual costs within budgeted levels and achieve operational parameters in line with estimates drawn at the time of bidding would be very critical. Finally, ICRA takes note of the operating risks associated with renewable power projects due to uncertainty in resource availability. This has an impact on the cash flows as the tariffs are single part in nature and the revenues are linked to actual generation only.

Key rating drivers

Credit strengths

Strong sponsor strength and experience of management lends comfort – The company enjoys strong sponsor strength as it is ultimately promoted by BC IPL (rated [ICRA]AA(Stable)/A1+), the holding company for Hero Motocorp (rated [ICRA]AAA/A1+). Further, there has been an equity infusion of \$125 million by IFC and IFC GIF, which are arms of the World Bank and rated AAA by Moody's. Moreover, the company has secured a commitment of \$150 million from Masdar, which is ultimately owned by the Government of Abu Dhabi.

Well-diversified asset base – The Group has a commissioned renewable energy capacity of ~1,300 MW. Its assets are spread across high renewable energy potential states, the prominent among which are Rajasthan, Karnataka, Andhra Pradesh, Madhya Pradesh, Tamil Nadu, Maharashtra, etc., resulting in geographic diversification of the asset base. The projects are also well diversified across a number of offtakers such as group captive, open access users, Central offtakers and a number of discoms. In terms of technology mix, about half of the commissioned capacity is based on solar, with wind making up the other half. Similarly, the portfolio is well diversified across various EPC/O&M players such as Gamesa, Inox, Regen and Suzlon.

Minimum demand risk for operational assets with long-term PPAs in place – The PPAs for the operational projects have been signed with state distribution utilities on long-term basis for two-thirds of operational capacity. Central agencies comprise about one-fifth of the operational capacity and group captive customers and open access customers are at negotiated tariffs for ~12% operational capacity, thereby mitigating offtake risk to a large extent. Among state distribution utilities, the operational portfolio is well diversified with no state distribution utility accounting for more 13% of the total capacity. This too mitigates counterparty risk to a certain extent.

Credit challenges

Risks associated with developing greenfield projects – The Group has won projects aggregating over ~900 MW under auctions conducted by Central and state agencies. The ability of the Group to execute these projects without time and cost overruns, mitigate funding, regulatory, industry risks, etc. and achieve satisfactory operational performance post commissioning shall be critical.

Credit risks arising out of exposure to state distribution utilities – The counterparty profile of the Group's projects includes exposure to Group captive and open access customers, state distribution utilities including those of Karnataka, Madhya Pradesh, Rajasthan, Maharashtra, Andhra Pradesh, etc and central offtakers. While in the case of certain offtakers such as Group captives, open access customers, Maharashtra discoms, Central offtakers, etc. the payments remain regular, others such as discoms of Rajasthan, Andhra Pradesh, HESCOM, etc. have irregular payment cycles. Receivable pattern from distribution utilities will thus remain a key rating sensitivity. However, post the commissioning of the under-construction projects, the counterparty risk profile is expected to improve as the majority the new projects would be selling power to Central offtakers.

Vulnerability to weather conditions – As is a feature with wind and solar power plants, cash flows are directly linked to prevalent wind conditions and insolation levels at site. Further, the tariff is single part in nature, which accentuates the resource availability risk.

Underperformance in generation profile of Group assets – Despite more than 35% of the asset portfolio having a generation track record of more than three years, the overall generation for the company has remained lower than the expected levels. The underperformance in generation is attributable to stabilisation issues, low resource availability, lower machine/equipment availability, etc. Moreover, the overall cash flows in FY2019 at the Group level was adversely impacted due to lower-than-estimated top line, and a significant rise in the overall expenses and capital charges.

Leveraged capital structure at holding company level suppressing profitability and cash flows – Overall, the debt level on the books of HFEPL (consolidated) as on March 31, 2019 remained at Rs. 9,250 crore, which included Compulsory compulsory convertible preference shares (CCPS) of Rs. 1,384 crore. The non-project debt outstanding on the books of HFEPL (Consolidated) remained at ~Rs. 1,790 crore at the end FY2019 and the same is primarily being used to fund

equity/sponsor commitments in various SPVs in addition to fulfilling working capital requirements, and thirdly acting as a bridge finance facility for under-construction projects. Most of the holding company debt is short to medium term in nature and would need refinancing. The ability of the company to obtain refinancing for the same in a timely manner is critical from a credit perspective.

Liquidity Position: Adequate

The liquidity profile of the Group remains **adequate** as at present the holding company (at a consolidated level) has high cash balances of ~Rs. 1,100 crore. However, most of this available liquidity is expected to be utilised for funding the present project pipeline and supporting the currently operational projects in case of any cash flow mismatch. However, ICRA takes comfort from the presence of overdraft limit of Rs. 99 crore, out of which ~Rs. 70 crore is unutilised. These OD limits are over and above the working capital limits in various projects. Moreover, many of the projects have Debt service reserve at the project level.

Rating sensitivities

Positive triggers – Given the Negative outlook, a rating upgrade in the near term is unlikely. However, positive triggers would include improvement in operational performance of the portfolio on a sustained basis, easing out of regulatory uncertainties, deleveraging of capital structure, and significant improvement in liquidity profile and cash flows in a sustained manner.

Negative triggers – The ratings could be downgraded in case of deterioration of the operational performance of project assets, adverse impact on liquidity profile and cash flows, further leveraging of capital structure, and time/cost-related delays in commissioning under-construction projects.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Holding Companies Rating Methodology for Wind Power Producers Rating Methodology for Solar Power Producers
Parent/Group Support	<p>Group: Hero Group</p> <p>We expect HSEPL's parent, Hero Future Energies Pvt. Ltd. (HFEPL) to be willing to extend financial support to HSEPL, should there be a need, given the high strategic importance that HSEPL has for HFEPL</p>
Consolidation / Standalone	<p>The rating is based on consolidated financials of the following</p> <ul style="list-style-type: none"> - Hero Future Energies Pvt Ltd - Hero Wind Energy Pvt Ltd - Hero Solar Energy Pvt Ltd - Clean Wind Power (Devgarh) Pvt Ltd - Clean Wind Power (Satara) Pvt Ltd - Clean Wind Power (Manvi) Pvt Ltd - Clean Wind Power (Pratapgarh) Pvt Ltd - Clean Wind Power (Ratlam) Pvt Ltd - Vayu Urja Pvt Ltd - Clean Wind Power (Piploda) Pvt Ltd - Clean Wind Power (Bableshtar) Pvt Ltd - LNJ Power Ventures Ltd. - Bhilwara Green Energy Ltd - Clean Wind Power (Bhavnagar) Pvt Ltd - Clean Wind Power (Jaisalmer) Pvt Ltd - Clean Wind Power (Anantpur) Pvt Ltd - Clean Solar Power (Dhar) Pvt Ltd - Clean Solar Power (Bellary) Pvt Ltd - Rajkot (Gujarat) Solar Energy Pvt Ltd - Clean Solar Power (Chitradurga) Pvt Ltd - Clean Solar Power (Tumkur) Pvt Ltd - Clean Solar Power (Gulbarga) Pvt Ltd - Clean Solar Power (Jaipur) Pvt Ltd - Clean Solar Power (Bhadla) Pvt Ltd - Clean Solar Power (Jodhpur) Pvt Ltd

About the company

HSEPL is the solar holding company of the Hero Group and is 100% owned by HFEPL, which also owns a 100% stake in the wind holding company of the Hero Group – HWEPL – and is the holding company of the Hero Group for renewable energy. HSEPL, through its 100% subsidiaries, has commissioned projects with an aggregate capacity of over 650 MW and has under-construction projects with an aggregate capacity of 840 MW. In total, the operational and under-construction/implementation capacity of HSEPL is ~1,490 MW.

Key financial indicators (Standalone)

	FY2018	FY2019
Operating Income (Rs. crore)	66.8	59.5
PAT (Rs. crore)	1.4	-268.6
OPBDIT/OI (%)	-10.0%	-3.9%
RoCE (%)	3.2%	-11.8%
Total Debt/TNW (times)	1.14	1.96
Total Debt/OPBDIT (times)	-153.49	-532.42
Interest coverage (times)	-0.09	-0.02

While reviewing the ratings, ICRA has considered the consolidated financials of HFEPL.

Key financial indicators (Consolidated) (HFEPL)

	FY2018	FY2019 (P)
Operating Income (Rs. crore)	627.7	1076.9
PAT (Rs. crore)	-257.3	-659.1
OPBDIT/OI (%)	58.9%	68.9%
RoCE (%)	5.2%	1.6%
Total Debt/TNW (times)	81.44	-20.54
Total Debt/OPBDIT (times)	21.80	12.46
Interest coverage (times)	0.79	0.90

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

Current Rating (FY2020)								Chronology of Rating History for the past 3 years		
Instrument		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs Crore)	Date & Rating			Date & Rating in FY2019	Date & Rating in FY2018	Date & Rating in FY2017
					05-Dec 2019	11-Jun 2019	04-Apr 2019			
1	NCD	Long Term	375.0	375.0	[ICRA]A (Negative)	[ICRA]A+ (Negative)	[ICRA]A+ (stable)	-	[ICRA]A (stable)	[ICRA]A (stable)
2	Proposed NCD	Long Term	100.0	Nil	[ICRA]A (Negative)	[ICRA]A+ (Negative)	-	-	-	-
3	Medium term loan	Long term	200.0	200.0	[ICRA]A (Negative)	[ICRA]A+ (Negative)	-	-	-	-

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
INE316W07013	NCD 1 Tranche 1	Dec-21-2016	9.995%	Jun-21-2021	87.50	[ICRA]A (Negative)
INE316W07013	NCD 1 Tranche 2	Dec-21-2016	9.995%	Jun-21-2022	87.50	[ICRA]A (Negative)
INE316W07021	NCD 2 Tranche 1	Jun-6-2019	11.84%	Dec-6-2021	100.0	[ICRA]A (Negative)
INE316W07039	NCD 2 Tranche 2	Jun-6-2019	11.84%	Jun-6-2022	100.0	[ICRA]A (Negative)
Proposed NCD	NCD	N/A	N/A	N/A	100.0	[ICRA]A (Negative)
N/A	Medium Term loan	March 2019	-	FY2021	200.0	[ICRA]A (Negative)

Source: HSEPL

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