Harsha Engineers International Limited

March 13, 2024

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term / Short-term Bank Facilities	483.87 (Enhanced from 447.87)	CARE AA-; Stable/ CARE A1+	Reaffirmed

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

Ratings assigned to bank facilities of Harsha Engineers International Limited (HEIL) continue to derive strength from its established operations in bearing cage business with state-of-the-art manufacturing facilities ensuring high quality standards and its status as the largest manufacturer of bearing cages in India. Ratings are also strengthened by HEIL's geographically diversified manufacturing facilities and its long-standing relationship with reputed clientele in the bearing industry. Ratings further draw comfort from its growing scale of operations with healthy profitability margins, strong financial risk profile marked by comfortable capital structure and debt coverage indicators, and strong liquidity.

However, the long-term rating is constrained due to its concentrated clientele dominated by three large players in the global bearing industry resulting in HEIL's limited bargaining power and profitability susceptible to volatility associated with raw material prices and foreign exchange rate fluctuation. Inherent cyclicality due to HEIL's linkages with the end-user automobile industry and subdued performance of its European subsidiary with near-term demand impact of high inflation and recessionary scenario in European region also constrain ratings. HEIL's long-term rating is further constrained by its presence in the competitive and fragmented solar engineering, procurement, and construction (EPC) business which has low entry barriers and long pending receivables associated with its solar power EPC business.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Volume-backed increase in its scale of operations through greater client and product profile diversification with total operating income (TOI) of more than ₹2,000 crore with improvement in its profit before interest, lease rentals, depreciation and taxation (PBILDT) margin to more than 18% and return on capital employed (ROCE) of more than 20% on a sustained basis.
- Significantly improved performance of its overseas subsidiaries aiding its consolidated performance on a sustained basis.

Negative factors

- Volume-based decline in its scale of operations marked by TOI of less than ₹1,200 crore on a sustained basis.
- Reducing PBILDT margin to less than 12% on a sustained basis.
- Elongating operating cycle to beyond 150 days affecting its liquidity.
- Significantly deteriorating capital structure and debt coverage indicators.

Analytical approach: Consolidated, as HEIL has extended stand-by letter of credit for bank facilities raised in its overseas subsidiaries which are also engaged in the similar line of business. The companies considered in HEIL's consolidation are given in **Annexure-6**.

Outlook: Stable

CARE Ratings Limited (CARE Ratings) believes that HEIL shall continue to benefit from its established operations in bearing cage business and its comfortable financial risk profile, which is expected to continue due to its steady cash accruals, and strong liquidity, which shall be available for funding of capex and working capital requirements in near to medium term.

Detailed description of the key rating drivers:

Key strengths

One of the largest domestic bearing cage manufacturers with state-of-the-art manufacturing facilities

HEIL has experience of more than three decades in the bearing cage industry. Since its inception in 1986, HEIL is the largest manufacturer of precision bearing cages in the Indian organised sector in terms of capacity. As articulated by the management, it is among world's leading manufacturers of precision bearing cages with a market share of approximately 6.5% in the organised segment of the global brass, steel, polyamide bearing cages in terms of revenue, enjoying a dominant market share of over 50% in the domestic market.

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

On a consolidated basis, the company is planning to undertake capex of around ₹350 crore through FY24-FY26 which shall be majorly funded through Initial Public Offer (IPO) proceeds and internal accruals with minimum reliance on term debt. In FY23, the company has formed a wholly-owned subsidiary company, Harsha Engineers Advantek Limited, which is setting-up a green-field project with an investment outlay of ₹250 crore spread over FY24-FY26.

Geographically diversified manufacturing facilities and advance in-house tooling design setup

The company has its principal production facilities at Changodar and Moraiya, near Ahmedabad in Gujarat. It also has a production facility through subsidiary in Changshu, China, and Ghimbav Brasov in Romania. Having four geographically diversified manufacturing facilities enables it to cater to requirements of its existing multinational clientele in those geographies more efficiently. It supplies its products to over 25 countries across five continents.

HEIL is a technology-driven company with a focus on research and development, allowing it to develop products suited to its customers' requirements. It has the expertise to design and develop advance tooling in-house which enables it to manufacture complex products. HEIL has a capability to produce bearing cages with diameters between 20 mm and 2,000 mm. Presently, it has more than 7,000 active SKUs. HEIL is a Total Productive Maintenance (TPM) certified company, issued by the Japan Equipment Maintenance Association. Since 2009, HEIL has also undertaken six-sigma initiatives to achieve higher efficiency and reduce operational costs.

Long-standing relationship with the world's three largest bearing manufacturers, though concentrated clientele

HEIL supplies bearing cages to leading global bearing manufacturers such as Timken, Schaeffler (including FAG) and SKF at their various worldwide locations (including India). It has long-term sales contracts with some of its customers. However, given the dominant position of these bearing companies, HEIL's bargaining power with them is relatively low. Sales to aforementioned three customers constituted 70-75% of HEIL's standalone net sales during past three years ended FY23.

Growing scale of operations with healthy profitability margins

HEIL operates two business segments, mainly bearing cages manufacturing and end-to-end solar power EPC. Over last three years ended FY23, solar EPC share remains low at around 5-7%.

The scale of operations marked by TOI remained largely stable in FY23 over FY22, as volume growth of around 8-9% in domestic bearing cages segment was offset by decline in overseas volumes apart from decline in average price realisation backed by softening of commodity prices. With the growth in sales volume of bearing cages, the operating profit (PBILDT) has increased by around 10% from ₹184 crore in FY22 to ₹204 crore in FY23. The company's operating profitability was also supported by profit reported in solar EPC business after incurring operating losses in FY20, FY21, and FY22.

In 9MFY24, TOI remained largely stable over 9MFY23 as 7-8% decline in revenue from bearing cages segment was offset by significant growth in solar EPC revenue. The decline in revenue of bearing cages segment was due to decline in average sales realisation followed by decline in commodity prices and slowdown in demand from overseas market, especially in Europe and China. PBILDT margin also declined by almost 200 bps y-o-y to 13.50% in 9MFY24 (9MFY23: 15.56%) with the decline in volume of bearing cages segment. CARE Ratings expects the company's TOI to remain at around ₹1,350-₹1,400 crore in FY24 with PBILDT margin of 13-14%. Going forward, HEIL's PBILDT margins are expected to improve to around 14.5-15% in FY25-FY26 with growth in scale of operations leading to better absorption of fixed overheads and increase in share of relatively high margin products such as bronze bushing and larger diameter cages.

Comfortable capital structure and debt coverage indicators

HEIL's financial risk profile is supported by healthy net worth of around ₹1,000 crore and comfortable gearing of 0.18x (gross debt basis) as on March 31, 2023. In September 2022, HEIL came out with an IPO and raised ₹455 crore through fresh issue, out of which ₹270 crore was utilised for part repayment/pre-payment of loans thereby improving company's overall debt profile. Total debt/ PBILDT improved from 2.09x as on March 31, 2022 to 0.89x as on March 31, 2023, and is expected to remain below unity in foreseeable future. The overall gearing ratio (gross debt basis) stood low at 0.18x as on March 31, 2023, and it is expected to remain below 0.50x in near to medium term.

Liquidity: Strong

Post infusion of equity through IPO, the company's liquidity improved significantly. Apart from equity infusion, the liquidity is also supported by steady cash accruals and positive cash flow from operations. HEIL's average utilisation of fund-based working capital limits remained low at around 30% for the trailing 12 months ended November 2023. Sizable unutilised limits provide sufficient cushion for additional working capital requirements to support the future growth in its operations. In addition, HEIL has healthy free cash and bank balance of ₹279 crore as on March 31, 2023, and around ₹320 crore as on February 29, 2024.

With an overall gearing of 0.18x as on March 31, 2023, the issuer has adequate gearing headroom to raise additional debt for its capex. HEIL's operating cycle stood high at 150 days in FY23, mainly because of long pending receivables related to its solar EPC business.

Key weaknesses

Near term impact of high inflation and recessionary scenario in European region

HEIL's operations are diversified geographically, as it derives nearly 35-40% of its revenue from India and balance from overseas markets. European region and China contribute majority to consolidated income of 35-40% and 13-15%, respectively. Present high inflation and recessionary trend in Europe and America may impact sales volumes in the near term while Indian business continues to grow. CARE Ratings expects Indian revenue to grow at around 10% in FY24, while income from outside India is expected to decline by 10-12% during the year.

The performance of European and Chinese operations impacted in 9MFY24 due to inflationary scenario in Europe and lower demand in China. European operations earned a total income of ₹168 crore (₹171 crore in 9MFY23) and reported a loss-before-tax of ₹10 crore (loss of ₹2 crore) in 9MFY24. Chinese operations earned a total income of ₹65 crore (₹92 crore in 9MFY23) and reported loss-before-tax of ₹6 crore (PBT of ₹2 crore) in 9MFY24.

Long pending receivables under solar EPC business

As HEIL (erstwhile Harsha Abakus Solar Private Limited) had executed a large solar power EPC project for NLC India Ltd (100 MW) in FY18, its solar EPC business segment reported huge increase in its TOI to ₹449 crore during the year from TOI of ₹102 crore in FY17. Although the project was successfully commissioned by it on May 05, 2018 (as articulated by the management), absence of power evacuation infrastructure (which was not under HEIL's scope) led to delay in the project commissioning by around two months. Hence, NLC blocked the balance payment. As on March 31, 2023, HEIL had ₹37.28 crore of debtors outstanding for more than three years related to solar EPC business whereby there is lack of clarity about the quantum and timelines for its actual collection.

Competitive and fragmented solar power EPC business with low entry barriers

As EPC business does not require any significant investment or gestation period, unlike manufacturing facilities, it entails high competition. These low entry barriers have resulted in numerous organised and unorganised players entering the solar EPC industry, leading to increased competition and pressure on profitability. However, HEIL has now decided to restrict itself to smaller-size ground-mounted projects with capacity up to 4-5 MW and solar rooftop projects, which is expected to restrict its working capital requirement.

Inherent cyclicality in its operations due to significant linkages of its prospects with that of the automobile industry

HEIL's bearing cages have major application in the bearings manufactured for the automobile sector and hence its fortunes are susceptible to slowdown in the demand of inherently cyclical automobile industry. However, over the years, HEIL has gradually increased its exposure to industrial bearing and segments other than automobile in its sales mix to around 50% which is expected to mitigate this risk to some extent.

Risk associated with volatile raw material prices and foreign exchange rate fluctuations

The main raw materials used in the bearing cage manufacturing process are cold-rolled and cold-annealed steel strips and brass tubes, castings, strips, and scrap. All these raw materials are mostly procured from domestic sources. High degree of volatility is associated with the price of its key raw materials resulting in susceptibility of its profitability. However, HEIL has price-escalation clause in its sales contracts with three key customers, mitigating the risk of increase in raw material prices to some extent; albeit it takes effect with some time lag.

On a standalone basis, HEIL's export sales constitute around 50% of its total sales, qualifying as a net exporting entity. Although HEIL hedges its foreign exchange exposure through currency options, forward cover, use of packing credit in foreign currency and in-built exchange rate fluctuation clause in some of the contracts entered with its customers, it continues to remain susceptible to inherent foreign exchange fluctuation risk.

Environment, social, and governance (ESG) risks

Factors	Compliance and action adopted by company
Environmental	• Being an engineering product company, the company does not have significant emission or waste generation. • HEIL has a captive solar power plant to meet part of its power requirement. The company has recently installed hybrid wind and solar power plant for captive use, thereby meeting 40% of total power requirement through renewable energy. • HEIL has ISO 14001 Certified Environmental Management System.
Social	• Board of Directors have constituted Corporate Social Responsibility (CSR) Committee, which has developed a CSR policy through which the company strives to assist underprivileged children with multiple challenges to have a better quality of life and promote education including special education and employment enhancing vocational skills among differently-abled.
Governance	• HEIL has a diversified board, and its Board of Directors consists of 50% independent directors (5 out of 10). Various policies, including whistle blower policy, is in place in line with the requirement.

Applicable criteria

Consolidation
Definition of Default
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Rating Watch
Manufacturing Companies
Financial Ratios – Non financial Sector
Auto Components & Equipments
Short Term Instruments

About the company and industry

Industry classification

Macro-economic Indicator	Sector	Industry	Basic Industry
Consumer discretionary	Automobile and auto components	Auto components	Auto components & equipment

HEIL, formerly known as Harsha Abakus Solar Private Limited (HASPL), was initially incorporated in December 2010 to undertake solar EPC business through a joint venture (JV) between Harsha Engineers Limited (HEL, which housed the bearing cage manufacturing business since 1972) and Abakus Solar AG (of Germany) with initial equity participation in the ratio of 76% and 24%, respectively. Post that, HEL gradually increased its stake in HASPL to 96.87%, which it later divested to HEL's promoters (Rajendra Shah and Harish Rangwala families), who increased their equity stake in HASPL to 99.99% by March 31, 2017. Post the scheme of corporate restructuring with an appointed date of April 01, 2020, the group has merged HEL (bearing cage manufacturing business) in to HASPL, and subsequently renamed HASPL as HEIL. Consequently, HEIL houses both businesses, i.e., manufacturing bearing cages and solar EPC business.

Brief Financials (₹ crore)	FY22 (A)	FY23 (A)	9MFY24 (UA)
Total operating income	1,337	1,381	1,034
PBILDT	184	204	139
PAT	92	123	75
Overall gearing (times)	0.86	0.18	NA
Interest coverage (times)	7.50	12.86	NA

A: Audited; UA: Unaudited; NA: Not available; Note: 'these are latest financial results available'

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years: Please refer to Annexure-2

Covenants of rated instrument / facility: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of various instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based - LT/ ST-Cash credit	-	-	-	-	277.00	CARE AA-; Stable/ CARE A1+
Non-fund-based - LT/ ST-BG/LC	-	-	-	-	206.87	CARE AA-; Stable/ CARE A1+

Annexure-2: Rating history for last three years

Sr. No.	Name of the Instrument/ Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021
1	Non-fund-based - LT/ ST-BG/LC	LT/ ST	206.87	CARE AA-; Stable/ CARE A1+	-	1)CARE AA-; Stable/ CARE A1+ (28-Mar-23)	1)CARE A+; Stable/ CARE A1+ (07-Mar-22)	1)CARE BB / CARE A4 (CW with Positive Implications) (26-Mar-21) 2)CARE BB; Stable / CARE A4 (08-Sep-20)
2	Fund-based - LT/ ST-Cash credit	LT/ ST	277.00	CARE AA-; Stable/ CARE A1+	-	1)CARE AA-; Stable/ CARE A1+ (28-Mar-23)	1)CARE A+; Stable/ CARE A1+ (07-Mar-22)	-
3	Fund-based - LT-Term loan	LT	-	-	-	1)Withdrawn (28-Mar-23)	1)CARE A+; Stable (07-Mar-22)	1)CARE BB (CW with Positive Implications) (26-Mar-21)
4	LT/ST Fund-based/Non-fund-based-EPC / PCFC / FBP / FBD / WCDL / OD / BG / SBLC	LT/ ST	-	-	-	-	-	1)Withdrawn (08-Sep-20)
5	Fund-based/Non-fund-based-LT/ST	LT/ ST	-	-	-	-	-	1)Withdrawn (08-Sep-20)
6	Non-fund-based - LT-Bank guarantee	LT	-	-	-	-	-	1)Withdrawn (08-Sep-20)
7	Fund-based - LT-Term loan	LT	-	-	-	-	-	1)Withdrawn (26-Mar-21) 2)CARE BB; Stable (08-Sep-20)

LT: Long term; LT/ST: Long term/Short term

Annexure-3: Detailed explanation of covenants of the rated instruments/facilities: Not applicable

Annexure-4: Complexity level of various instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Fund-based - LT/ ST-Cash credit	Simple
2	Non-fund-based - LT/ ST-BG/LC	Simple

Annexure-5: Lender details

To view the lender wise details of bank facilities please click here

Annexure-6: List of all the entities consolidated

Sr No	Name of the entity	Extent of consolidation	Rationale for consolidation
1	Harsha Precision Bearings Components China Company Limited (HPBCL)	Full consolidation	Subsidiary; operational linkages
2	Harsha Engineers Europe SRL (HESSRL)	Full consolidation	Subsidiary; operational linkages
3	HASPL Americas Corporation (HAC)	Full consolidation	Subsidiary; operational linkages
4	Harsha Engineers Advantek Limited @	Full consolidation	Subsidiary; operational linkages
5	Cleanmax Harsha Solar LLP	Proportionate consolidation	JV; operational linkages
6	Sunstream Green Energy One Private Limited	Proportionate consolidation	Associate; operational linkages

@ With effect from March 14, 2023

Note on the complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

Contact us

Media Contact	Analytical Contacts
Mradul Mishra Director **CARE Ratings Limited** Phone: +91-22-6754 3596 E-mail: mradul.mishra@careedge.in	Ranjan Sharma Senior Director **CARE Ratings Limited** Phone: +91-22-6754 3453 E-mail: Ranjan.sharma@careedge.in
Relationship Contact Saikat Roy Senior Director **CARE Ratings Limited** Phone: 91 22 6754 3404 E-mail: saikat.roy@careedge.in	Hardik Manharbhai Shah Director **CARE Ratings Limited** Phone: +91-22-6754 3591 E-mail: hardik.shah@careedge.in Krunal Pankajkumar Modi Associate Director **CARE Ratings Limited** Phone: +91-79-4026 5614 E-mail: krunal.modi@careedge.in

About us:

Established in 1993, CARE Ratings is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India, it has been acknowledged as an External Credit Assessment Institution by the RBI. With an equitable position in the Indian capital market, CARE Ratings provides a wide array of credit rating services that help corporates raise capital and enable investors to make informed decisions. With an established track record of rating companies over almost three decades, CARE Ratings follows a robust and transparent rating process that leverages its domain and analytical expertise, backed by the methodologies congruent with the international best practices. CARE Ratings has played a pivotal role in developing bank debt and capital market instruments, including commercial papers, corporate bonds and debentures, and structured credit.

For the detailed Rationale Report and subscription information, please visit www.careedge.in