HFCL Limited

August 30, 2024

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	1,000.34 (Reduced from 1,044.54)	CARE A; Stable	Reaffirmed
Short-term bank facilities	2,131.63 (Enhanced from 1,984.13)	CARE A1	Reaffirmed

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

Ratings reaffirmation for bank facilities of HFCL Limited (HFCL) continues to derive strength from its long and established track record in the industry with experienced management team, strong order book position providing revenue visibility and its diversified customer base and product portfolio. Furthermore, the rating continues to consider HFCL's healthy operational profile, sustained profitability levels and comfortable capital structure. HFCL is well-placed to benefit from increasing demand for high-speed 5G connectivity, fuelled by government initiatives such as BharatNet Phase III, implementation of FTTH, hyper-scaling of data centres and PLI scheme considering increasing level of digitisation. CARE Ratings limited (CARE Ratings) also takes a note of HFCL's exemption from the anti-dumping duties imposed by the European Commission on Indian optical fibre cable (OFC) manufacturers in the European markets in Q1FY25. However, rating strengths are tempered by elongated working capital cycle due to inherent working capital-intensive operations, risk associated with large-sized/tender-based orders, project risk emanating from significant investments in the next two years, susceptibility to volatile raw material prices and prevalent competition in the industry.

Care Ratings however believes, that going forward, the company's operating cycle would rationalise given its conscious strategy to increase the mix of product-based sales in total revenue and the near completion of some of its large sized turnkey projects, especially defence projects where milestone-linked payments are expected to be release in the FY25 and FY26, leading to an expected improvement in collections, which remains a key monitorable.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Substantially improving scale of operations and improving capital structure and coverage indicators, with total debt (including acceptances) to profit before interest, lease rentals, depreciation, and taxation (PBILDT_ in the range of 2-2.5x on a sustained basis and/or interest coverage indicators above 4x on sustained basis.
- Improving average collection period to less than 100 days on a sustained basis.

Negative factors

- Substantially declining operating profitability due to global supply–demand mismatch, which could result in operating margin sliding below 12% on sustained basis.
- Slower-than-anticipated realisation of outstanding debtors having an impact on the company's liquidity profile.
- Total debt (including acceptances) to PBILDT exceeding 3x on sustained basis.

Analytical approach: Consolidated

CARE Ratings has considered a consolidated view of HFCL Limited and its subsidiaries owing to significant business, operational, financial, and management linkages between the parent and subsidiaries. Details of subsidiaries consolidated are listed in Annexure - 6

Outlook: Stable

The 'Stable' outlook for bank facilities of HFCL signifies CARE Ratings' expectation that HFCL is likely to sustaining its healthy financial risk profile supported by its operational profile in the medium term. Continuous conscious strategy of HFCL to increase mix of product-based sales in total revenues is likely to keep margin profile healthy in the medium term.

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

Detailed description of key rating drivers:

Key strengths

Healthy operational profile despite some moderation across the industry, supported by diverse revenue profile
HFCL reported a total revenue from operations of ₹1158.24 crore in Q1FY25 (₹995.19 crore in Q1FY24) and ₹4,474.03 crore in FY24 (₹4762.45 crore in FY23). In FY24, the revenue from turnkey segment grew by 24% on a year-on-year basis, yet revenue declined by 6% compared to the previous year largely attributable to the industrywide low demand of optic fibre cables accounting to 42% of contribution from telecom products in the total revenue against 56% in FY23. The industry faced several acute challenges, including elevated inventory levels, lower investments by operators and an uncertain economic environment and geopolitical disturbances. Hence, the export sales witnessed moderation in revenue contribution from 17.2% in FY23 to 11.21% in FY24. On June 14, 2024, European Commission exempted HFCL, the only Indian OFC manufacturer from anti-dumping duties. Hence, it is expected that the company will benefit from the exemption going forward, subsequently improving the revenue contribution from export.

In Q1FY25, revenue was supported by the introduction of new telecom equipment products which contributed ~₹400 crore to the total revenue, due to which the revenue mix improved to 61:39 as on June 30, 2024, from 42:58 as on March 31, 2024. This shift from project-led revenue to product-led revenue will facilitate the company in lowering working capital requirements, drive quicker realisation and margin expansion. Going forward, with the anticipated higher contribution from the telecom segment, margins are expected to improve along with the revenue mix, as the PBILDT margin stood at 15.86% for Q1FY25 (Q1FY24: 13.27%) and 13.20% in FY24 (FY23: 13.39%). The company is expected to benefit from the roll out of BharatNet Phase III project, which is anticipated to significantly boost product-led revenue and engineering, procurement and construction (EPC). Going forward, change in revenue mix through the onset of BharatNet and the increase in debt to support the operations for the project will be a key monitorable.

Strong order book providing revenue visibility and diverse customer base
HFCL has a strong order book of ₹7,685 crore as on March 31, 2024, (PY: ₹7,010 crore) on a consolidated basis giving a medium-term revenue visibility. The company has diversified its revenue in turnkey segment and product segment entailing OF/OFC, telecom equipment and defence products and has also been awarded new contracts for telecom systems supply and implementation services from Delhi Metro Rail Corporation and BSNL etc. totalling to ₹2,343 crore in FY24. In Q4FY24, HFCL became the first Indian company to secure order worth ₹623 crore for indigenously manufactured 5G networking equipment from Reliance Jio (RJio). As on June 30, 2024, the total order book stood at ₹6,776 crore (₹6,585 crore as on June 30, 2023), of which, ₹2,070 crore came from the private sector and ₹4,706 crore from the government sector. Going forward, the BharatNet Phase III project presents a huge opportunity as it will strengthen the demand for OFC, telecom and networking products, system integration services, and annuity revenue through O&M. Hence, HFCL's ability to leverage this, will be a key monitorable.

Long and established track record with highly experienced management team and strong association with RJIL
Mahendra Nahata, the company's Managing Director, has a business experience of over 35 years in the telecom sector. He is also on the Board of RJIL since 2010 and is associated with forums related to the industry. He is assisted by the management team comprising highly experienced officials in their respective domains.
The company also has a strong association with RJIL, with HFCL being responsible for execution of RJIL's network expansion plans for the Northern region. HFCL has been associated with RJIL since the start of network roll out of RJIL and has been responsible for their network planning, design and implementation for the Northern region. RJIL contributed around 63% to the total revenue of HFCL in FY18, which decreased to 24% in FY24, this however was higher in FY23 at 43% considering higher off-take of OF/OFC products by RJIL (Revenue contribution by RJIL in FY22: 28% and FY21: 24%). Going forward, with an increase in project executions in the Northern region and the growth in 5G adoption, revenue is expected to increase.

Established relationship with reputed clients
HFCL has established long-standing relationships with reputed corporate houses in public and private sectors. Apart from telecom projects, HFCL has expanded its business has become a leading material supplier and turnkey contractor for defence and railway communication projects. Turnkey contract and service business segment normally deals in capex undertaken by different companies and government, resulting in single high value orders from few customers with longer execution period. Many of these contracts are tender-based, awarded through bidding process. In FY24, sales contribution from top five customers at a standalone level stood at 47% (FY23: 39%).

In the product segment, the company has been expanding its customer base in domestic and international market. Sales contribution from top five customers stood at 17% at the standalone level in FY24 against 35% in the previous year.

Comfortable financial risk profile
The company has a comfortable financial risk profile marked by a strong tangible net worth position of ₹3855.52 crore in FY24 considering accretion of profit and infusion of funds. To support its expansion programs and R&D initiatives, HFCL raised funds of ₹600 crore and ₹352 crore in December 2021 and August 2023 respectively by way of qualified institutional placement (QIP). The company also raised funds of ₹73.20 crore through preferential issue to promotors and senior leadership in FY24. The company's overall gearing and interest coverage stood comfortably as on March 31, 2024, at 0.38x (FY23: 0.47x) and 3.87x (FY23: 4.07x) respectively. Going forward, debt coverage metrics are expected to moderate in the medium term, as the company avail fresh term loans to support its capital expenditures for capacity augmentation and backward integration and due to the increase in the working capital borrowings to fund increasing scale of operations. Healthy net worth base from expectedly improving operating profitability supported by increase in product revenue should prevent significant deterioration in the capital structure in the near future.

Key weaknesses

Large working capital requirements
Due to decrease in revenue contribution from the product segment at 42% in FY24 from 56% in the previous year and concurrent rise in share from turnkey segment at 58% in FY24 from 44% in FY23, the average collection period increased from 182 days in FY23 to 203 days in FY24. The turnkey division has longer execution period (2-3 years apart from warranty period and O&M) due to which, payments are spread over a long period. Sales in the product segment is on a running order basis and hence has a shorter release period (average credit period of 90 days). Total debtors in absolute terms increased to ~₹2750 crore as on March 31, 2024, as against ~₹2,330 crore as on March 31, 2023.

BSNL, Reliance, L&T comprise almost 60% of overall debtors as on March 31, 2024. Outstanding debtors for defence projects, where BSNL is the implementing agency, funded by department of telecommunication (DOT) amounting to ~₹800 crore is expected to be released within the next two years and remains a monitorable.

Inventory built up in FY23 and FY24 also elongated working capital cycle, which increased to 198 days in FY24 from 159 days in FY23. Going forward, with the rise in the share of revenue from product segment, working capital cycle is expected to rationalise in the medium term.

Average utilisation of the fund-based working capital limits stood at ~88% for 12-months ending June 2024. The company has a high reliance on the non-fund-based working capital limits for the procurement of materials and bank guarantee requirements in the EPC segment.

Project Risk
HFCL plans to incur a large capex in the medium term for capacity augmentation of optical fibre capacity from 12 mn fkm as on June 30, 2024, to proposed 26.94 mn fkm; OFC capacity from 25.60 mn fkm as on June 30, 2024, to proposed 30.25 mn fkm; and backward integration into preform with a capacity of 300 MT to smoothen the company's supply chain capabilities.
The company is planning to set-up a new plant in Poland to address the increasing OFC demand in European markets, with an initial capacity of 3.25 mn fkm, further scalable to7 mn fkm capacity, which is under progress. The total project cost is estimated to be ~₹1500-1600 crore to be met through a mix of debt and internal accruals. Successful completion of all capex with no cost and time overrun, and the company being able to derive expected benefits from these projects, will be a key rating monitorable.

Intense competition in the industry and susceptibility to raw material price volatility
The demand in cable business majorly depends on operational/capital expenditure from telecom companies. Delays or deferrals of such expenditure would impact revenue visibility of companies catering to this business. EPC business continues to face competition due to presence of many players. HFCL is making efforts to expand its product basket. It is also foraying into exports, where large-sized global players have established presence, and stiff competition in that segment may limit its pricing flexibility. However, the company is focused on gaining traction in new geographies and value-added services to mitigate pricing pressure in relatively commoditised OF/OFC segment. The main raw materials required is optical fibre. The company is partially backward integrated for it and is also in the process of expanding its OF capacities. At present, some of the OF requirement is met from external vendors. The company is insulated against volatility in optical fibre prices partially due to backward integration but remains susceptible to volatility in prices of other raw materials procured from external sources and time lag in pass through of escalated costs.

Liquidity: Adequate

HFCL's liquidity position is marked by adequate gross cash accrual generation of ₹468 crore as on March 31, 2024 (PY: ₹435 crore). The free cash and bank balance as on March 31, 2024, stood at around ₹24 crore apart from the lien marked cash and bank balance of ₹309 crore. The company's cash flow from operations reduced in FY23 and FY24 majorly considering increase in debtors and inventory, which will ease as the demand picks up. The company has consolidated debt repayments of ₹102 crore and ₹123 crore in FY25 and FY26 respectively, which is expected to be comfortably met through the cash accruals. The company also intends to pay inter corporate debentures (ICDs) amounting to ₹40 crore in FY25. Consolidated repayments also include repayments of its subsidiary HTL Limited, where HFCL has guaranteed bank facilities by giving irrevocable and unconditional corporate guarantee. Owing to the working capital intensive operations, average working capital utilisation for 12-months ended June 2024 stood at 88%.

Assumptions/Covenants: Not applicable

Environment, social, and governance (ESG) risks

HFCL recognises the importance of environmental sustainability and continues to invest in minimising its environmental impact. For a greener tomorrow, the company undertakes several initiatives under the areas of energy, water and waste management.

Environmental: Saved approximately ₹6 crore through environmental sustainability efforts. Achieved a 16% reduction in annual energy consumption and an 18% reduction in total waste generation during FY24. Installed Sewage Treatment Plants (STPs) with capacities of 35 KLD/Day at Hyderabad and 30 KLD/Day Goa facilities. Increased in waste recovery by 74% in FY24 compared to the previous year. Transitioning from conventional microwave lamps to LED UV variants, resulting in a reduction of 5,022 metric tonnes of emissions and saving 6.2 million units of energy annually. 14001-certified Environmental Management System, which ensuring the high standards of sustainable practices.

Social: HFCL engages in various healthcare, education, elderly care, and societal welfare programs. They operate nine Mobile Medical Units with HelpAge India and Wockhardt Foundation, providing preventive healthcare in remote areas. They partner with the National Heart Institute and St. Stephen's Hospital for heart and corrective surgeries for the underprivileged. Under Project Samarth, they offer educational grants to specially-abled children and computer skills training to underprivileged youth. They promote digital learning through smart classrooms and have established a facility for over 100 abandoned elderly individuals. HFCL also supports elderly care through the Amritam Charitable Trust and provides food and shelter for stray animals.

Governance: HFCL's governance framework provides direction for responsible and credible conduct across its operations. The Board has five committees (audit, nomination, remuneration and compensation, stakeholder relationship, CSR and risk management) that support the Board's decision-making processes. Each committee has its own terms of reference and operates under a clearly defined charter. All board proceedings are logically segregated, and specific matters are delegated to committees. The board committee consists of one executive director, two non-executive director and four independent directors.

Applicable criteria

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

About the company and industry

Industry classification

Macro-economic indicator	Sector	Industry	Basic industry
Telecommunication	Telecommunication	Telecom - equipment & accessories	Telecom - equipment & accessories

HFCL (erstwhile Himachal Futuristic Communications Limited) was incorporated 1987 to set up a plant in Solan (Himachal Pradesh) for assembling telecom equipment. The company is an established leader in offering fully integrated communication network solutions. It manufactures OF, OFC, cable accessories and high-end telecom transmission and access equipment and specialises in providing turnkey solution to telecom service providers, railways, defence, smart city and surveillance projects. As on June 30, 2024, the company has OF capacity of 14 mn fkm and OFC capacity of 25.60 mn fkm.

Brief Financials (₹ crore) Consolidated	March 31, 2023 (A)	March 31, 2024 (A)	Q1FY25 (UA)
Total operating income	4762.45	4474.03	1168.74
PBILDT	637.82	590.52	185.37
PAT	317.71	337.52	110.65
Overall gearing (times)	0.47	0.38	-
Interest coverage (times)	4.07	3.87	4.38

A: Audited UA: Unaudited; Note: these are latest available financial results

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years: Annexure-2

Covenants of rated instrument / facility: Annexure-3

Complexity level of 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-Cash Credit		-	-	-	495.00	CARE A; Stable
Fund-based - LT-Term Loan		-	-	31/01/2031	505.34	CARE A; Stable
Non-fund-based - ST-BG/LC		-	-	-	2131.63	CARE A1

CareEdge RATINGS

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 2024-2025	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
1	Fund-based - LT-Term Loan	LT	505.34	CARE A; Stable	-	1)CARE A; Stable (07-Jul-23)	1)CARE A; Stable (06-Jul-22)	1)CARE A; Stable (29-Mar-22) 2)CARE A-; Negative (07-Jul-21)
2	Fund-based - LT-Cash Credit	LT	495.00	CARE A; Stable	-	1)CARE A; Stable (07-Jul-23)	1)CARE A; Stable (06-Jul-22)	1)CARE A; Stable (29-Mar-22) 2)CARE A-; Negative (07-Jul-21)
3	Non-fund-based - ST-BG/LC	ST	2131.63	CARE A1	-	1)CARE A1 (07-Jul-23)	1)CARE A2+ (06-Jul-22)	1)CARE A2+ (29-Mar-22) 2)CARE A2 (07-Jul-21)
4	Debentures-Non Convertible Debentures	LT	-	-	-	1)Withdrawn (07-Jul-23)	1)CARE A; Stable (06-Jul-22)	1)CARE A; Stable (29-Mar-22) 2)CARE A-; Negative (07-Jul-21)

LT: Long term; ST: Short term

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

Annexure-4: Complexity level of instruments rated

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

Annexure-5: Lender details

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

Annexure-6: List of entities consolidated

Sr No	Name of the entity	Extent of consolidation	Rationale for consolidation
1.	HTL Limited	Proportionate	Operational, financial, and managerial linkages
2.	Polixel Security Systems Private Ltd	Full	
3.	Radeff Private Limited	Proportionate	
4.	Nimpaa Telecommunications Private Limited (Jointly controlled entity)	Proportionate	
5.	HFCL Technologies Private Ltd	Full	
6.	BigCat Wireless Pvt. Limited (Jointly Controlled Entity with 50% voting right)	Proportionate	
7.	Moneta Finance (P) Ltd	Full	
8.	HFCL Advance Systems (P) Ltd	Full	
9.	DragonWave HFCL India Private Limited	Full	
10.	HFCL B.V. (Wholly owned Subsidiary on 07th October 2021) – Netherland	Full	
11.	HFCL Inc. (Wholly owned Subsidiary on 08th October 2021) – United States of America	Full	

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

Contact us

Media Contact	Analytical Contacts
Mradul Mishra Director **CARE Ratings Limited** Phone: +91-22-6754 3596 E-mail: mradul.mishra@careedge.in **Relationship Contact** Saikat Roy Senior Director **CARE Ratings Limited** Phone: 91 22 6754 3404 E-mail: saikat.roy@careedge.in	Ravleen Sethi Director **CARE Ratings Limited** Phone: 91-120-4452016 E-mail: ravleen.sethi@careedge.in Akhil Kumar Associate Director **CARE Ratings Limited** Phone: 91-120-4451986 E-mail: akhil.kumar@careedge.in Bhoomika Sharma Analyst **CARE Ratings Limited** E-mail: Bhoomika.Sharma@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