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Mumbai

CRISIL Research assigns IPO grade 1/5 to Tarapur Transformers Ltd.

CRISIL Research has assigned a CRISIL IPO Grade "1/5" (pronounced "one on five") to the proposed initial public offer (IPO) of Tarapur Transformers Ltd. This grade indicates poor fundamentals relative to other listed equity securities in India. However, this grade is not an opinion on whether the issue price is appropriate in relation to issue fundamentals. The grade is not a recommendation to buy/sell or hold the graded instrument, or a comment on the graded instrument's future market price or its suitability for a particular investor.

The IPO grade assigned to Tarapur Transformers Ltd reflects the weak position of the company in a highly competitive power transformer industry, dominated by large established players. The power transformer segment is expected to show strong growth due to the government's focus on increasing power generation and on improving distribution efficiency. However, Tarapur Transformers Ltd is expected to face challenges in establishing itself successfully in this segment. Despite having considerable experience in power transformer repairing and distribution transformer manufacturing, the company is inexperienced in manufacturing higher range of power transformers. The execution team required for scaling up of operations is also in the process of being recruited. The grading also considers negative operating cash flows for the last 3 years due to long working capital cycle brought about by high receivables days. The working capital position is further strained due to delays in payment from State Electricity Boards (SEBs).

The IPO Grading assigned reflects inadequate corporate governance structure as well. Nik-San Engineering Company (P) Ltd, a promoter group company, operates in a similar line of business as that of Tarapur Transformers Ltd. The two companies do not have a formal non-compete agreement, which poses a potential conflict of interest. In addition, Tarapur Transformers Ltd sources its key raw material (transformer core) from its parent company – Bilpower Ltd. However, no formal arms-length pricing agreement for this purpose is in place. Further, the extent of engagement of independent directors falls below the expected level.

About the company and the issue

Tarapur Transformers Ltd repairs, upgrades and manufactures power and distribution transformers. It is a 71 per cent subsidiary of Bilpower Ltd, which manufactures laminations and motor stampings. Tarapur Transformers Ltd is a registered vendor for various SEBs across the country, and is also registered with many private companies for supply and repair of power transformers. The company has three operating plants.

Through the IPO proceeds, the company proposes to fund the expansion of its Pali unit and also plans to undertake an acquisition to diversify into an allied segment.

Of the total requirement of Rs 700 million, the debt component (including amount already spent) is Rs 220 million. The balance amount of Rs 470-480 million will be raised through IPO proceeds.

About CRISIL IPO Grading

CRISIL IPO (Initial Public Offering) Grading is an opinion on the fundamentals of the graded issue that reflects CRISIL's independence and expertise. This opinion is expressed as a relative assessment in relation to other listed equity securities in India. The assessment is based on a grading exercise carried out by industry specialists from CRISIL Research. A CRISIL IPO Grade 5/5 indicates strong fundamentals and a CRISIL IPO Grade 1/5 indicates poor fundamentals. CRISIL IPO Grading reflects its assessment of the graded company's equity fundamentals as distinct from an assessment of debt fundamentals. A CRISIL IPO Grade should not be construed to mean a comment on the price of the graded security nor is it a recommendation to invest or not to invest in the graded security.

Media Contact	Analytical Contact
Mitu Samar Head, Market Development & Communications CRISIL Limited Tel: +91-22- 3342 1838 Mobile: +91- 98200 61934 Fax: +91-22- 3342 3001 E-mail: msamar@crisil.com	Chetan Majithia Head, CRISIL Equities Tel: +91-22- 3342 4148 E-mail: chetanmajithia@crisil.com

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