Mecklai Financial
WHERE RISK MEETS ITS MATCH

Integrated Risk Management Solution for EPC Company

Business Context

- An EPC contractor engaged in design, testing, manufacture and supply of galvanized towers; manufacture of conductors; and construction services
- Current order book over INR 3,000 cr
- About 30% of the revenue was through export projects; imported procurement was roughly 20% of the revenue; additionally, cost of part of domestic procurement is USD linked
- Entire export business and about 35% of domestic business was under Firm Price contracts; the balance revenue is under contracts with a Price Variation clause

Risk Management Issues

- All projects and supply contracts are for long tenors, averaging 24 months. Since entire export business is under Firm Price contract, company is exposed to FX and Commodity risk over the longest tenor
- On Firm Price projects, company is exposed to contingent risk during Bid to Award period (about 3-6 months), during which FX and Commodity prices could move adversely
- While significant FX exposure is naturally hedged, the timing mismatch was not managed actively
- FX and commodity risk was not actively managed, keeping cash flows at a mercy of market movement.

Mandate Given to Mecklai

- Articulate FX and Commodity risk profile (including FX risk implied in domestic purchases) based on whether the contracts were Firm Price or with PV clause
- Draft an integrated risk management policy for FX and Commodity price risk
- Create the implementation framework with an automated MIS

The Solution

- Objectives of Treasury clearly articulated
- FX and Commodity Risk Profile developed
- For the natural hedge, optimal approach was defined ensuring that the import payment rate is always lower than the effective export realization rate
- Systematic hedging approach for FX risk on net exports, independent of any market view
- Process for monitoring commodity risk during Bid to Award Period and building in that impact while managing the risk after award of contract
- Data interface between business and treasury, MIS formats defined for seamless implementation.

The Impact

- Economic Impact – Risk is identified and monitored from its inception, reducing dramatically the risk of project cost overrun and diminution of margins; natural hedge management ensures positive cash flow impact.
- Decision support – Structured approach provides decision support on FX hedge timing and amount. Strategy for commodity risk provides decision support on bid rate calculation and subsequent commodity hedging after the award.
- Operations – Effective data interface and automated MIS minimized operational risk by ensuring accurate risk identification and transparent reporting and performance evaluation

82, Free Press House | Free Press Journal Marg | Nariman Point | Mumbai 400 021 | India

telephone +91-22-61940202 | email mumbai@mecklai.com | website www.mecklai.com

registered office Mecklai Financial Services Limited | 101 Mahatma Gandhi Road | Mumbai 400 023 | India