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India Ratings Downgrades THDC India and its NCDs to 'IND AA'/Stable; Off RWE

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India Ratings and Research (Ind-Ra) has downgraded THDC India Limited's (THDC) Long-Term Issuer Rating to 'IND AA' from 'IND AA+' while resolving the Rating Watch Evolving (RWE). The Outlook is Stable. The instrument-wise rating actions are as follows:

Instrument Type	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (million)	Rating/Outlook	Rating Action
Non-convertible debentures (NCDs)	6 September 2019	8.75	6 September 2029	INR15,000	IND AA/Stable	Downgraded; off RWE
NCDs	3 October 2016	7.59	3 October 2026	INR6,000	IND AA/Stable	Downgraded; off RWE

ANALYTICAL APPROACH: Ind-Ra has factored in the moderate-to-strong strategic and operational linkages between THDC and its parent NTPC Limited (NTPC; 'IND AAA'/Stable; holding 74.5% stake) to arrive at the ratings. The remaining stake is held by the government of Uttar Pradesh (UP).

The downgrade factors in Ind-Ra's expectation of deterioration in THDC's financial profile over the medium term, owing to significant bunching of debt-led capex; delays in project commissioning leading to an increase in project costs, and the non-finalisation of tariffs for its key under construction (UC) hydro projects.

Ind-Ra had placed THDC's ratings on RWE on 4 February 2020, following an in-principle approval accorded by NTPC's board of directors, on 27 January 2020, for the acquisition of the government of India's (GoI) entire equity stake in THDC (i.e. 74.5% of paid-up share capital of THDC). The resolution of the RWE follows the completion of the GoI's stake sale to NTPC, and the emerging clarity on the linkages between THDC and NTPC.

KEY RATING DRIVERS

Delays in Commissioning; Increase in UC Project Costs: THDC's UC portfolio stood at 2,764 megawatt (MW; 1.7x the operational portfolio) at end-December 2020. Ind-Ra had previously expected the commissioning of projects to reduce the building-up of debt, as EBITDA generation would have picked-up with the project commissioning. However, there has been a delay in project commissioning with the estimated date of commercial operations for Tehri Pumped Storage Plant (TPSP)/ Vishnugad Pipalkoti (VP)/ Khurja Super Thermal Power Project (KSTPP) being revised to December 2022 (previously June 2022); June 2023 (December 2021), and February 2024 (September 2023), respectively.

Moreover, the cumulative cost for the four UC projects: TPSP (1,000MW; project cost: INR48 billion); VP (444MW; INR38.6 billion), KSTPP (1,320MW; INR110.9 billion) and Amelia coal block (INR15.9 billion) has risen to INR213 billion (from INR181 billion at previous review), due to the time overruns.

Net Leverage Likely to Increase: Ind-Ra believes the company's high capex, coupled with cost and time overruns, are likely to result in a higher-than-Ind-Ra's previously-expected net leverage (net debt/EBITDA) over a longer term. The equity of INR25.6 billion for TPSP and VP has been fully funded and hence, the remaining capex of INR27.8 billion will entirely be funded from debt. Furthermore, Ind-Ra believes capex on KSTPP would entail an additional debt drawdown of INR71.6 billion over the next three-four years. This is against the agency's expectation of an annual EBITDA of INR13 billion-14 billion from the operational projects. Thus, Ind-Ra expects the leverage to substantially increase over FY22-FY25 to over 5.5x (FYE20: 3.7x; FYE19: 2x), before moderating on the back of additional cash flows as the UC projects commence operations. Ind-Ra believes the leverage would be higher than the negative rating trigger of 4x outlined by the agency earlier. THDC has incurred a cumulative capex of INR76.5 billion up to December 2020 on these projects, and any further delay in the commissioning timelines or an increase in the project costs further would lead to the leverage remaining elevated for longer than anticipated by the agency.

THDC has also entered into joint ventures with the governments of UP and Rajasthan to build ultra-mega renewable energy solar parks of around 3,500MW (2,000MW in UP and 1,500MW in Rajasthan), which could entail further cash outflows. The company is also engaged in a lawsuit with a contractor, for which it has submitted INR4.5 billion as a bank guarantee to the Delhi High Court. The total amount under contention is over INR10 billion. In case of a negative ruling against THDC, additional cash outflows or debt drawdown could be seen, though the management expects the same to be passed on.

Tariffs Not Finalised; Risks Remain Elevated: Ind-Ra believes given the increased project cost, the tariff per unit for the hydro projects will remain high under the Central Electricity Regulatory Commission's (CERC) framework. While the tariff for the operational plants - Tehri Hydro-electric Project (THEP) and Koteshwar Hydro-electric Project (KHEP) stood at INR5/ kilowatt hour (kWh) and INR4.5/kWh for FY20, the levelised tariff for THPP, VP and KSPTT is expected at INR6/kWh, INR4.5/kWh and INR3.6/kWh, respectively.

While the regulator has introduced tariff rationalisation measures, such as providing flexibility to the developers to determine tariff by back-loading of tariff after increasing the project life to 40 years; increasing the debt repayment period to 18 years, and introducing escalating tariff of 2%, the management is yet to take a decision on the same. Additionally, Ind-Ra believes that if TPSP is allowed to operate as a grid asset it could have multiple income streams from wheeling charges and generation, thereby lowering the tariff. The management expects the policy regarding the same to be finalised before the commissioning of TPSP. However, any delay in the policy finalisation, or increased tariffs due to cost escalations, could pose a challenge in placement in the merit order despatch.

Moderate-to-Strong Linkages with NTPC: Prior to THDC's change in shareholding to NTPC from the GoI, Ind-Ra had factored into the ratings, the linkages of THDC with the GoI; the GoI had infused equity of INR3.6 billion during FY13-FY20. However, post the stake sale, the linkages are derived from NTPC. Ind-Ra has assessed the strategic and operational linkages to be moderate-to-strong. The equity commitment of the UC hydro projects has already been funded till FY20. For the other UC projects, especially KSTPP, the technical, operational and financial support from NTPC will be forthcoming, given the companies are in the same line of business. Additionally, THDC has two nominee directors from NTPC on its board. Ind-Ra expects NTPC to also support THDC, if required.

PPA Risks Mitigated: Power purchase agreements (PPA) have been signed for TPSP, VP and KSTPP with the discoms of Delhi (cumulative tied capacity: 768MW), Rajasthan (465MW), UP (957MW), Uttarakhand (600MW) and with other northern discoms; having an excess PPA tie up of 450MW in KSTPP. However, these PPAs were entered into during FY06-FY12 and the ability of these states to buy power at high tariffs would continue to be a key monitorable.

Debt Tie-up Partially Complete: The debt for VP has been completely tied with the World Bank on a guarantee by the GoI, while TPSP has been funded by a mix of domestic loans (INR7 billion); NCDs (INR16.2 billion) and foreign currency loan of EUR83 million (yet to be drawn); the balance (around INR5 billion) is yet to be tied up from the banking system or from additional bond issuances. As per the management, the debt for KSTPP and Amelia coal block will be funded by a mix of NCDs and bank loans; INR6 billion out of already-issued NCDs has been utilised for KSTPP, while the rest is yet to be tied up. If there is a delay in the debt tie up for the UC projects, the commissioning timelines could get extended and the project cost might see an increase. The GoI has provided a guarantee on the USD548 million term loan from the World Bank for the VP project, which will continue as is, despite the change in the ownership.

Operations Under Cost-Plus Model: THDC operates its hydropower plants under the cost-plus return on equity framework, outlined by the CERC, thus ensuring a reasonable recovery of costs, the pass-through of forex risks and a guaranteed return on equity. The new hydro and thermal plants being set up by THDC would also be covered under the CERC regulations, thus reducing the operating cash flow risk. The company has also signed PPAs for majority of the capacity during FY06-FY12; however, any increase in the capital cost could lead to higher tariffs, leading to difficulties in operationalising these PPAs.

Efficient Operations: THDC's two operational plants – THEP and KHEP – continued to achieve better than normative levels of operational performance in FY20. This is reflected through higher availability and higher-than-design energy generation levels over eight years-ended FY20. During FY20, the plant availability factors of THEP and KHEP were 82.8% (FY19: 84.5%) and 76% (68%) compared with the normative availability of 80% and 68%, respectively; the same was increased from 77.0% and 67.0%, respectively, for the tariff block of FY19-FY24.

Furthermore, the actual generation at both plants remained above design energy over FY14-FY20 (FY20: 4,245 million units (FY19: 4,397 million units). Higher availability and higher generation than design energy led to a healthy capacity incentive, secondary energy and deviation settlement charges, which totalled INR1 billion in FY20 (FY19: INR1.17 billion). Ind-Ra expects THDC to continue earning healthy incentive income, though slightly reduced on account of the higher normative plant availability factor, over the control period of FY19-FY24.

Liquidity Indicator - Adequate: THDC's cash flow from operations declined to INR4.6 billion in FY20 (FY19: INR13.6 billion) due to an increase in receivables. The cash balance also reduced to INR252 million at FYE20 (FYE19: INR454 million); higher cash flow generation in FY19 was supported by additional EBITDA on account of tariff acceptance for the block FY14-FY19.

THDC's liquidity is supported by a fund-based working capital limit of INR10 billion, which was utilised at around 52% over the 12 months ended December 2020. THDC has repayments of INR1.6 billion in 4QFY21; INR5.3 billion in FY22 and INR3 billion in FY23. Ind-Ra expects the debt service coverage ratio for THDC to remain strong over 2x for FY21-FY23, given the interest on the UC projects gets capitalised. Furthermore, Ind-Ra expects the company's funding tie up to remain comfortable, given THDC's presence in the capital market and multiple banks. The company reduced cash outflow on dividends to INR1.5 billion in FY20 (FY19: INR5.1 billion) on account of the planned capex and increase in receivables. As per the management, dividend distribution over the medium term is expected to be in line with the capex outlay, ensuring the company is able to meet the equity requirement of the projects by way of internal accruals. While Ind-Ra does not envisage any additional equity infusions, any shortfall is anticipated to be funded by NTPC.

Continued Elevated Receivables: THDC receivables increased to INR22 billion (FY19: INR17 billion) on account of the delays by counterparties, in line with the overall power sector. The receivables, however, reduced to INR20 billion at end-9MFY21, on account of the partial receipt of dues (amounting to INR9 billion) from the Atmanirbhar Bharat scheme; another tranche of around INR9 billion is expected in 4QFY21.

The bulk of the increase in receivables came in from the discoms of UP, Jammu and Kashmir and Delhi as the debtors increased to INR12.3 billion at end-December 2020 (March 2020: INR14.5 billion; March 2019: INR12.3 billion), INR2.5 billion (INR2.8 billion; INR2.2billion) and INR2.6 billion (INR2.2 billion; INR1.9 billion) respectively. Furthermore, over 50% of the receivables are due for over six months. While Ind-Ra expects the company’s working capital position to benefit from the receipt of funds from the Atmanirbhar Bharat scheme, a delay in the receipt of or continued delays in payments by discoms could lead to lower free cash flows.

RATING SENSITIVITIES

Positive: The timely completion of UC projects, along with the successful operationalisation of their PPAs, leading to the net leverage sustaining below 4x, and/or the strengthening of the linkages with NTPC could lead to a positive rating action.

Negative: A further build-up of dues from buyers, time and cost overruns in the UC projects; and/or an inability to operationalise the PPAs for the UC projects; and/or any additional debt-funded capex, leading to higher-than-Ind-Ra expected deterioration in the net leverage; and the weakening of linkages with NTPC, could lead to a negative rating action.

COMPANY PROFILE

Incorporated in 1988, THDC is a Miniratna Category-I and Schedule-A central public sector enterprise. THDC has two operational hydropower plants in Uttarakhand: THEP (1,000MW) and KHEP (400MW). In addition, it has two wind power projects in Gujarat: Patan (50MW) and Devbhumi Dwarka (63MW), one small hydro project in UP- Dhukwan (24MW) and a solar project of 50MW in Kerala .

FINANCIAL SUMMARY

Particulars	FY20	FY19
Revenue (INR million)	21,231	27,680
EBITDA (INR million)	15,235	21,348
EBITDA margin (%)	71.8	77.1
Interest coverage (x)	6.3	12.1

Net leverage (x)	3.7	2.0
Source: Ind-Ra, THDC		

RATING HISTORY

Instrument Type	Current Rating/Outlook			Historical Rating/Outlook/Rating Watch		
	Rating Type	Rated Limits (billion)	Rating/Rating Watch	4 February 2020	9 October 2018	13 October 2017
Issuer rating	Long-term	-	IND AA/Stable	IND AA+/RWE	IND AA+/Stable	IND AA+/Stable
NCDs	Long-term	INR21	IND AA/Stable	IND AA+/RWE	IND AA+/Stable	IND AA+/Stable

COMPLEXITY LEVEL OF INSTRUMENTS

For details on the complexity level of the instruments, please visit https://www.indiaratings.co.in/complexity-indicators.

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Applicable Criteria

Corporate Rating Methodology
Parent and Subsidiary Rating Linkage

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