July 06, 2023

Druk Green Power Corporation Limited: Ratings reaffirmed.

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Issuer rating	-	-	[ICRA] BBB+ (Stable); reaffirmed

**Instrument details are provided in Annexure-I*

Rationale

The rating reaffirmation takes into account the strong credit profile of Druk Green Power Corporation Limited (DGPC), which owns and operates hydropower projects (HPPs) with aggregate operational capacity of 2,326 MW in Bhutan (including Mangdechhu project which is to be consolidated under DGPC in CY2023 as indicated by management). DGPC is a strategically important Royal Government of Bhutan (RGoB) enterprise, which is responsible for meeting the domestic power requirements of the country and also contributes almost a quarter to the Government's revenues (excluding grants) in the form of royalty, tax and dividend payments. Thus, it benefits from the stable regulatory environment, concessional funding (low cost and long tenured loans availed by RGoB made available to DGPC) and beneficial offtake arrangements with PTC India Ltd (PTC; GoI-nominated agency for cross-border trade with Bhutan) for export of power.

DGPC, by virtue of its parentage, enjoys strong linkages with the Government of India (GoI), which has supported the development for various projects (aggregate 1,416 MW) by providing the entire funding (70% through loan and 30% through grants) and also ensuring complete offtake of surplus power (after meeting domestic demand) through PTC India. The surplus generated and upstreamed as dividends in addition to royalty and tax payments is an important source of revenue for the Government of Bhutan while ensuring self-sufficiency for Bhutan in meeting its domestic power requirements.

The projects have delivered strong operational performance by consistently generating in excess of design energy as well as operating within the normative parameters (auxiliary consumption, etc.), which coupled with a cost-plus domestic tariff and higher export tariffs have resulted in healthy profitability metrics, conservative capital structure and strong debt protection metrics, even as they are expected to moderate in CY2023 with takeover of Mangdechhu project by DGPC. DGPC's export tariff (Rs 2.23-2.55/unit for its various own plants) is extremely competitive in the Indian power market and is comparable to the prevailing solar tariff and is much lower than the conventional thermal tariffs in India. Export tariff for Mangdechhu project is higher and less competitive in the Indian power market, at Rs 4.12/unit, however, it also has a firm PPA with PTC for surplus energy. The counterparty credit risk is mitigated by the strong credit profile of PTC and Bhutan Power Corporation Limited (BPCL; fellow subsidiary of DGPC responsible for transmission and distribution of power in Bhutan). Although the financial profile of the discoms that are the ultimate beneficiaries of DGPC's power in India is weak, the payments from PTC have been timely. This was evidenced over CY2020-CY2022 as well, when despite the weak collections of discoms in India on account of relaxations/deferment of payments by their customers during the Covid-19 lockdown, the payments from PTC remained timely. As domestic consumption was higher in CY2022, DGPC was adversely impacted from lower export of power to India where the realised tariff is higher than the approved domestic tariff (Nu 1.34/unit effective September 01, 2022).

Although DGPC benefits as an RGoB enterprise, the assigned rating is ultimately constrained by the susceptibility of its operations to potential changes in tax/royalty or other such demands to support the Government in times of economic slowdown. By virtue of its 100% holding and presence in the company's board, the RGoB has complete control over the operations of DGPC. As such, the operations of the company are vulnerable to any change in Government regulations/policies. In addition, DGPC is exposed to hydrology risks (single part tariff linked to generation), exchange rate variation risk (no hedging instrument available in Bhutan although the overall exposure is lower than the annual operating profits of the company) and project implementation and offtake risks with the 118-MW Nikachhu HPP, 600 MW Kholungchhu HPP and various smaller projects (Energy Security Phase-1 and Phase-2 projects), all being developed by DGPC's 100% subsidiaries. The projects have seen multiple time and cost overruns. While Nikachhu is expected to commissioned soon by Dec-2023, Kholungchhu is yet to achieve financial closure, and may take another 5-6 years once execution resumes.

The Stable outlook on the rating reflects ICRA's opinion that DGPC's operations will continue to be supported by efficient operations of its HPPs and a stable sovereign credit profile.

Key rating drivers and their description

Credit strengths

Strategically important Government enterprise – DGPC is a wholly-owned RGoB enterprise responsible for the operation and development of HPPs in Bhutan. It is of strategic importance to the RGoB as it meets the entire domestic power demand of Bhutan and contributes almost a fourth of the Government's own revenues through income tax, royalty energy, and dividend contributions. Going forward, DGPC would play a key role in the development of future hydropower assets in Bhutan. Therefore, it would continue to maintain its dominant position in the nation's power sector.

Support from Government of India (GoI) – The project portfolio of DGPC (with the exception of Basochhu and Dagachhu) has been developed under a bilateral arrangement between the RGoB and the GoI, wherein the latter has provided the entire funding for these projects in the form of loans and grants. With the exception of the Dagachhu HPP, the entire surplus power (after meeting domestic demand) has been contracted with PTC at export tariffs, which are higher than the approved domestic tariff (on cost-plus basis). The export tariffs of Rs. 2.23/unit and Rs 2.55/unit (for various DGPC-owned plants) are extremely competitive in the Indian power market. Export tariff of Rs 4.12/unit is higher and less competitive for the Mangdechhu project which is to be incorporated within DGPC in 2023.

Efficient operations of hydropower stations, supported by good hydrology – DGPC plants, at an aggregate level, have consistently generated in excess of the design energy in each of the last 13 years, supported primarily by increased generation from Tala HPP (of capacity 1,020 MW). The auxiliary consumption of the plants has remained within normative parameters. The oldest plant, Chhukha HPP (336-MW plant commissioned in 1988), has continued to operate at high PLFs despite completing more than 33 years of operations. In CY2022, the company achieved 7,228 MU, 13.2% higher than the aggregate design energy of 6,387 MUs.

Healthy client profile leads to timely realisation of dues; limits counterparty risks – DGPC exports power to PTC and domestically to BPCL. PTC has signed power sale agreements (PSAs) with power distribution companies in India. The presence of PTC as an intermediary has resulted in low counterparty credit risks for DGPC despite the financially weak state distribution companies being the ultimate beneficiaries. The average receivable days stood below 35 days during CY2015–CY2022 for DGPC. The collections from PTC remained timely over CY2020-CY2022, despite the weakened cash flows of the ultimate beneficiaries in India on account of the Covid-19 lockdown. Collections from the domestic offtaker, BPCL, also remained timely over CY2020-CY2022.

Credit challenges

Capitalisation and coverage indicators are expected to moderate but will still remain comfortable– The long track record of operations, high generation (higher than design energy), healthy export tariffs and cost-plus domestic tariffs have resulted in healthy profitability metrics for DGPC. This coupled with the lack of new project development so far (equity funding for commissioned 126-MW Dagachhu HPP and under-construction 118-MW Nikachhu HPP substantially funded through funding from ADB availed through on-lending from the RGoB) has aided the increase in net worth and repayment of debt. This has resulting in low gearing (total debt/total net worth of 0.45 times as on December 31, 2022), robust coverage indicators (interest coverage of 15.6 times and debt service coverage ratio of 5.4 times in CY2022) and cash/liquid funds of Nu. 838.5 crore as on December 31, 2022 at a consolidated level.

However, with new relatively smaller renewable projects (part of Energy Security Phase-1 & Phase-2 programme), expected to be funded by DGPC, for which the company is expected to avail Rs 1,400 crore term loan in 2023, capitalisation and coverage indicators are expected to moderate significantly going forward. Further, there will be addition of sizeable debt pertaining to Mangdechhu project, which has been taken over by DGPC, and will be incorporated in DGPC's financials CY2023 onwards. This will also lead to deterioration in debt indicators with sizeable near-term interest and principal repayments. At a consolidated level, gearing is expected to moderate to ~1 times over the next 3 years, while DSCR is expected to be ~3.0-3.5 times in CY2023 and then moderate to ~1.5-2.0 times in CY2024-CY2025 as repayments for the Nikachhu project and proposed Rs 1400 crore SBI loan also commence in CY2024. Further, Kholongchhu project (now 100% with DGPC post acquisition of SJVN's 50% stake in Q1CY2023) is expected to entail addition of more debt at a consolidated level and incremental equity investments as well, for which financial closure is pending.

Exposure to sovereign credit risks – DGPC benefits as an RGoB enterprise. However, the assigned rating is ultimately constrained by the susceptibility of its operations to the potential changes in tax/royalty or other such demands to support the Government in times of economic slowdown. By virtue of its 100% holding and presence in the company's board, the RGoB has complete control over the operations of DGPC. Hence, the company's operations are vulnerable to any change in Government regulations/policies.

Exposure to hydrology risks – HPPs in Bhutan have a single-part tariff with no deemed generation clause. This exposes these projects to significant hydrology risks (volatility in revenues if the hydrology is inadequate as the revenues are directly linked to unit sales). However, comfort is drawn from the higher-than-design energy generation consistently achieved by the company in the last 13 years.

Project implementation and offtake risks – DGPC is exposed to project implementation and offtake risks in its under-construction 118-MW Nikachhu HPP, which is being developed by its wholly-owned subsidiary Tangsibji Hydro Energy Limited (ThyE). ICRA notes that the project has faced multiple time overruns due to adverse geological conditions along with the weak profile of its EPC contractors. The project is currently expected to commission by December 2023. DGPC has extended guarantee for INR loans up to COD for Nikachhu HPP and has also given an undertaking to meet the debt servicing of its loans. ICRA takes note of DGPC's adequate liquidity profile and expects it to service the debt obligations for Nikachhu HPP's loans that are falling due for repayment from June 2024 onwards as it has demonstrated such support in the past as well. Further, there are ~100 MW smaller renewable projects currently under implementation within Druk Hydro Energy Ltd (~100% DGPC subsidiary), which also expose DGPC to under-construction and offtake risks.

Liquidity position: Adequate

DGPC's consolidated liquidity is adequate with robust cash flow from operations, which are adequate to meet its sizeable expected debt servicing (Nu. ~600–820 crore principal repayments and interest annually in CY2023–CY2026) and significant capital expenditure requirements as well in the near term (for Energy Security Phase-1 & Phase-2 projects for which Nu. 1400 crore loan from SBI is expected to be availed in CY2023). DGPC is expected to raise debt via commercial papers to pay dividends of Nu. ~450 crore announced for CY2023.The working capital intensity is low, aided by very low receivable days. Also, the company had standalone cash and liquid investments of only Nu. 71.0 crore as on March 31, 2023 (Nu. 643 crore as on Dec 31, 2022) due to outflow of Nu ~350 crore towards acquisition of SJVN stake in Kholongchhu and also towards routine capex in Q1CY2023.

Rating sensitivities

Positive factors – ICRA may upgrade DGPC's rating if the sovereign credit profile of Bhutan improves.

Negative factors – Negative pressure on DGPC's rating may arise if there is a significant reduction in generation on account of poor hydrology or plant breakdown, etc., as HPPs in Bhutan have a single-part tariff with no deemed generation clause. Any deterioration in the sovereign credit profile of Bhutan would also trigger a downgrade.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology
Parent/Group support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of DGPC; subsidiaries and joint ventures as on December 31, 2022 are all enlisted in Annexure-2

Note (for analyst reference only):

About the company

DGPC is a wholly-owned enterprise of the RGoB through Druk Holdings & Investments (the Government company for holding all Government-owned enterprises in Bhutan). The company was incorporated in January 2008 through the amalgamation of the Chhukha, Kurichhu and Basochhu hydropower projects. The Tala hydropower project was subsequently taken over in April 2009. Mangdechhu project is to be taken over by DGPC in 2023. The current standalone operational capacity of the company is 2,336 MW. DGPC is the sole hydropower operator in Bhutan responsible for supplying power for meeting the domestic requirements of Bhutan Power Corporation Ltd (a fellow subsidiary, which is also an RGoB-owned enterprise). The offtake arrangements for DGPC's plants obligate PTC India Limited to offtake the entire surplus power from these plants after meeting the domestic requirements. DGPC exports more than two-thirds of its power to PTC through firm PPAs.

DGPC has also developed the 126-MW Dagachhu hydropower project (commissioned in March 2015) in an SPV with Tata Power Trading Company Limited (a 26% stake) and National Pension and Provident Fund (a 15% stake). Moreover, it has formed a 100% subsidiary, Tangsibji Hydro Energy Limited, for the development of the 118-MW Nikachhu hydroelectric project, which is slated for commissioning in June 2023. DGPC is also developing 600 MW Kholongchhu project through Kholongchhu Hydro Energy Ltd (100% subsidiary) for which financial closure is pending, and various smaller hydro/renewable projects through Druk Hydro Energy Ltd (100% subsidiary).

Key financial indicators (audited)

Consolidated	CY2020	CY2021	CY2022 (Prov)
Operating income	1769.6	1614.5	1553.5
PAT	530.6	560.5	438.4
OPBDIT/OI	62.1%	67.0%	61.2%
PAT/OI	30.0%	34.7%	28.2%
Total outside liabilities/Tangible net worth (times)	0.5	0.5	0.5
Total debt/OPBDIT (times)	1.7	1.9	2.3
Interest coverage (times)	18.3	18.5	15.6

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2024)				Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as on March 31, 2023 (Rs. crore)	Date & Rating on	Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021
					July 06, 2023	Apr 29, 2022	-	Jan 28, 2021
1	Issuer Rating	Long term	-	-	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)	-	[ICRA]BBB+ (Stable)

Complexity level of the rated instruments

Instrument	Complexity Indicator
Issuer Rating	Not Applicable

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Issuer Rating	NA	NA	NA	NA	[ICRA] BBB+ (Stable)

Source: Druk Green Power Corporation Limited, ICRA research

Annexure II: List of entities considered for consolidated analysis

Company	Ownership	Consolidation Approach
Dagachhu Hydro Power Corporation Limited	59.00%	Full Consolidation
Tangsibji Hydro Energy Limited	100.00%	Full Consolidation
Bhutan Hydropower Services Limited	100.00%	Full Consolidation
Bhutan Automation Engineering Limited	51.00%	Equity Method
Khlongchhu Hydro Energy Limited	50.00%	Equity Method

Note: ICRA has taken a consolidated view of the parent (DGPC), its subsidiaries and Joint Ventures while assigning the ratings

ANALYST CONTACTS

Sabyasachi Majumdar
+91 124 4545304
sabyasachi@icraindia.com

Anupama Arora
+91 124 4545303
anupama@icraindia.com

Rohan Rustagi
+91 124 4545383
rohan.rustagi1@icraindia.com

RELATIONSHIP CONTACT

L. Shivakumar
+91 22 6114 3406
shivakumar@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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ICRA Limited

Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001
Tel: +91 11 23357940-45

Branches