

July 01, 2019

## Karnataka Power Corporation Limited: Rating downgraded and outlook revised to negative; limits enhanced

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based Long-term Loan	5514.36	6538.00	[ICRA]BB+; downgraded from [ICRA]BBB- and outlook revised to Negative from Stable
Fund-based Cash credit	2076.00	2610.00	[ICRA]BB+; downgraded from [ICRA]BBB- and outlook revised to Negative from Stable
Non-fund based	100.00	100.00	[ICRA]BB+; downgraded from [ICRA]BBB- and outlook revised to Negative from Stable
Fund-based Short-term loan	12809.64	15752.00	[ICRA]A4+; downgraded from [ICRA]A3
<b>Total</b>	<b>20500.00</b>	<b>25000.00</b>	

\*Instrument details are provided in Annexure-I

### Rationale

ICRA's revision of ratings assigned to Karnataka Power Corporation Limited (KPCL) factors in the continued rise in receivables from the state electricity distribution companies (discoms) in Karnataka, which increased to Rs. 17,577 crore as on March 31, 2019 from Rs. 15,575 crore as on March 31, 2018. This along with the support extended to Raichur Power Corporation Limited (RPCL; joint venture with Bharat Heavy Electricals Limited (BHEL), which operates a 1600-MW coal-based power project, has significantly increased the company's dependence on short-term borrowings, adversely affecting its capital structure, profitability and debt coverage metrics. ICRA notes that KPCL's high receivable from the Karnataka discoms is because of the delay in the realisation of electricity bill payments from Government entities and the receipt of subsidy from the Government of Karnataka (GoK) to discoms, primarily related to free power supply to agriculture consumers. While ICRA takes note of the receipt of the past power purchase dues, amounting to ~Rs. 3,766 crore, from the state discoms, under the scheme approved by the GoK in FY2018 and FY2019, which were used to repay short-term borrowings and clear coal purchase payables, the overall short-term debt for KPCL increased to ~Rs. 17,000 crore as on March 31, 2019 from Rs. 14,251 crore as on March 31, 2018. Moreover, there was no equity infusion from GoK over the past three years.

ICRA takes note of the non-commencement of mining operations at the reallocated coal mines in Maharashtra for supply to the 1000-MW (units 1 and 2) Bellary Thermal Power Station (BTPS), because of issues over selection of the mining contractor. The fuel supply for this plant is currently met by Singareni Collieries Company Limited (SCCL). In the recently commissioned capacity of 2300 MW, (comprising 700 MW unit-3 of BTPS and 1600 MW under RPCL), the standing committee on coal linkages has recommended these plants for allocation of long-term linkage. The fuel requirement for this capacity is being met through bridge linkage from SCCL, which is expected to be shifted to long-term linkage from Coal India Limited (CIL), post September 2021. While the cost competitiveness of the new capacity of 2300 MW is adversely affected by the high capital cost, primarily due to delays in the execution of these projects, the cost-plus tariff structure for sale of power to the discoms with availability-linked payment of capacity charges and expected availability of coal from domestic sources would mitigate these risks to some extent. Further, the rating also factors in the significant increase in the share of renewable (mainly wind and solar) capacity in the installed generation capacity in Karnataka (49% as on March 31, 2019), which is likely to lead to frequent backdowns for the thermal units and in turn may affect

their operating efficiencies. ICRA also takes note of the company's sizeable capital expansion plans, which entails large debt funding, including the gas-based power generation project of 370 MW, water pipeline for BTPS to augment water availability and implementation of flue gas de-sulphurisation (FGD) system to comply with the new environmental norms for the coal-based power plants.

However, the ratings continue to factor in KPCL's 100% ownership by GoK and the strategic importance of the company to the state power sector as it accounts for 31% of the state's installed power generation capacity as of March 2019. The rating draws strength from the limited demand risks for KPCL's power generation business attributed to the presence of long-term power purchase agreements (PPAs) with the Karnataka discoms. Also, the tariff risks remain limited, given the presence of two-part cost-plus tariff structure with availability-linked payment of capacity charges and pass-through of fuel cost variations, subject to adhering to normative operating parameters approved by the Karnataka Electricity Regulatory Commission (KERC). The company has tied-up fuel supply agreements with SCCL and CIL for coal supply, providing assurance on fuel supply. Further, the rating draws comfort from the well-established regulatory processes in Karnataka with tariff norms approved for KPCL as well as the regular and timely issuance of tariff orders for discoms by KERC. ICRA also takes note of the improvement in availability of coal-based plants in FY2019, which has led to improved recovery of fixed charges from the discoms compared to that of FY2018, wherein lower-than-normative plant availability affected revenues and profitability.

### Outlook: Negative

The Negative outlook on the rating assigned to KPCL reflects the large build-up of receivables from the state discoms and the continued dependence on short-term debt. The outlook may be revised to Stable if the company is able to improve the collection efficiency of payments from discoms and reduce its dependence on short-term debt. However, the rating may be downgraded if the receivable position continues to increase, leading to higher dependence on short-term debt. The support extended by the state government to KPCL in clearing the past receivables from discoms remains a key rating sensitivity.

### Key rating drivers

#### Credit strengths

**State-owned power generation company with regulated business** - KPCL is a GoK-owned power generation utility that supplies electricity to the five discoms of Karnataka under long-term PPAs. KPCL occupies an important role in the state power sector by accounting for 31% of the installed power generation capacity in Karnataka as on March 2019.

**Limited demand and tariff risks** - The presence of long-term PPAs with the state discoms in Karnataka mitigates demand risks. The regulated nature of the business with two-part cost-plus tariff structure allows the company to pass on the variations in cost to the discoms, subject to adherence to normative operating parameters.

**Fuel supply tied-up with CIL and SCCL** - The fuel supply for the Raichur Thermal Power Station (RTPS) is tied-up under long-term linkage with SCCL and subsidiaries of CIL, thereby limiting fuel availability risks. Also, the standing linkage committee under Ministry of Coal has recommended the new units under BTPS and YTPS for allocation of long-term coal linkage, thereby limiting fuel supply risks.

**Established regulatory processes in Karnataka** - The operations of KPCL are supported by well-established regulatory processes in Karnataka, with presence of multi-year tariff regulations for generation utilities. Also, the tariff orders for discoms are issued in a timely manner by the regulator.

**Improvement in operating performance in FY2019** – The plant availability of the thermal power stations improved in FY2019 over FY2018, leading to higher recovery of fixed charges. Also, the generation from hydel units witnessed a significant growth in FY2019 over FY2018, led by improved water availability.

## Credit challenges

**High receivable position constraints KPCL's financial profile** - KPCL faces significant counterparty credit risks as evident from the large build-up of receivables from the discoms, with outstanding dues of Rs. 17,577 crore (including interest claimed on delayed payments) as on March 31, 2019. This in turn leads to high dependence on short-term borrowings, which constrains the capital structure, profitability and debt coverage metrics.

**Funding support to RPCL** - The support extended to JV company, RPCL, has also led to higher dependence on short-term borrowings for KPCL. The operations of 1600 MW coal-based plant under RPCL were constrained by pending auxiliary plant works, resulting in under-recovery in fixed charges from the discoms.

**Delay in commencing coal production from reallocated coal mines** - The coal production from the reallocated coal mines for fuel supply to the two 500 MW units of BTPS is yet to commence owing to the dispute over selection of the mine contractor. The fuel supply for these units is being met through interim arrangements with SCCL. The resolution of the dispute remains crucial for long-term fuel security of the 1000 MW capacity under BTPS.

**Growing share of renewable energy in state electricity consumption mix may lead to frequent backdowns for thermal units** - The demand for thermal generation declined in Karnataka in FY2019 amid significant increase in the share of renewable (mainly wind and solar) capacity in the installed power generation capacity in the state (49% as on March 31, 2019). This is likely to lead to frequent backdowns for the thermal units and in turn may affect their operating efficiencies.

**Hydel power project exposed to risk of water availability** - The generation by the hydro power projects of KPCL remained exposed to hydrology risks, wherein adverse variations in water availability would result in lower generation from these projects. This in turn makes the discoms dependent on relatively high cost power. Nonetheless, the hydel power stations reported a 71% growth in generation in FY2019 over FY2018.

**Significant capital expansion plans for KPCL** - KPCL's capacity expansion plans remain significant, including gas-based power project of 370 MW, investments towards water pipeline for BTPS and complying with revised environmental norms for thermal units. This will entail large debt funding requirement for the company.

## Liquidity position

The liquidity profile of the company remains weak owing to the high receivable position from the discoms in Karnataka. The receivables are being funded through short-term debt from banks and financial institutions. The capex funding is met through fresh equity and long-term debt.

## Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">Corporate Credit Rating Methodology</a> <a href="#">Thermal Power Producers</a>
Parent/Group Support	The assigned rating factors in the systemic importance that KPCL has in the state power sector, which we expect should induce the GoK to extend timely financial support to the rated entity, should there be a need.
Consolidation/Standalone	The rating is based on the consolidated financial profile of the company.

## About the company

KPCL is the state-owned power generation company of Karnataka. It is responsible for developing and operating power generation stations including thermal, hydro, and renewable. As of March 2019, the installed power generation capacity of KPCL stood at 8738 MW, comprising hydel power generation capacity of 3680 MW, thermal capacity of 5020 MW and renewable energy capacity of 39 MW. The thermal generation capacity of the company includes a 1600-MW thermal power project under a JV (73:27) with BHEL. IFCI held a 20% stake in this JV, which was bought out by KPCL in FY2019. The five state-owned distribution companies of Karnataka namely Bangalore Electricity Supply Company Limited (BESCOM), Mangalore Electricity Company Limited (MESCOM), Hubli Electricity Supply Company Limited (HESCOM), Gulbarga Electric Supply Company Limited (GESCOM) and Chamundeshwari Electricity Supply Corporation Limited (CESC) source power from KPCL under the allocated power purchase agreements and as per the tariff regulations approved by KERC.

## Key financial indicators (audited)

	FY2017	FY2018
Operating Income (Rs. crore)	8600.72	6840.87
PAT (Rs. crore)	487.88	63.69
OPBDIT/OI (%)	20.85%	20.05%
RoCE (%)	9.76%	6.89%
Total Debt/TNW (times)	1.93	1.95
Total Debt/OPBDIT (times)	10.27	13.52
Interest coverage (times)	1.16	0.81

**Status of non-cooperation with previous CRA: Not applicable**

**Any other information: None**

## Rating history for last three years

		Current Rating (FY2020)			Chronology of Rating History for the past 3 years				
Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs Crore)	Date & Rating	Date & Rating in FY2019	Date & Rating in FY2018		Date & Rating in FY2017	
				July 2019	June 2018	July 2017	June 2017	May 2016	
1	Term loans	6538.00	6538.00	[ICRA]BB+ (Negative)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Negative)	[ICRA]BBB- (Negative)	[ICRA]BBB- (Negative)	[ICRA]BBB- (Stable)
2	Fund-based	2610.00	-	[ICRA]BB+ (Negative)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Negative)	[ICRA]BBB- (Negative)	[ICRA]BBB- (Negative)	[ICRA]BBB- (Stable)
3	Non-fund-based limit	100.00	-	[ICRA]BB+ (Negative)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Negative)	[ICRA]BBB- (Negative)	[ICRA]BBB- (Negative)	[ICRA]BBB- (Stable)
4	Term loan	15752.00	15752.00	[ICRA]A4+	[ICRA]A3	[ICRA]A3	[ICRA]A3	[ICRA]A3	[ICRA]A3

## Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website [www.icra.in](http://www.icra.in)

### Annexure-1: Instrument Details

ISIN No	Instrument Name	Date of Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Long-term loans	February-2009	NA	March-2029	6538.00	[ICRA]BB+ (Negative)
NA	Fund-based limit	NA	NA	NA	2610.00	[ICRA]BB+ (Negative)
NA	Short-term loans	NA	NA	NA	15752.00	[ICRA]A4+
NA	Non-fund- based limit	NA	NA	NA	100.00	[ICRA]BB+ (Negative)

Source: KPCL

### Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Raichur Power Corporation Limited	73%	Full Consolidation
KPC Gas Power Corporation Limited	100%	Full Consolidation

## ANALYST CONTACTS

**Sabyasachi Majumdar**  
+91 124 4545304  
[sabyasachi@icraindia.com](mailto:sabyasachi@icraindia.com)

**Girishkumar Kadam**  
+91 22 6114 3441  
[girishkumar@icraindia.com](mailto:girishkumar@icraindia.com)

**Vikram V**  
+91 40 40676518  
[vikram.v@icraindia.com](mailto:vikram.v@icraindia.com)

## RELATIONSHIP CONTACT

**L Shiva Kumar**  
+91 22 6114 3406  
[shivakumar@icraindia.com](mailto:shivakumar@icraindia.com)

## MEDIA AND PUBLIC RELATIONS CONTACT

**Ms. Naznin Prodhani**  
Tel: +91 124 4545 860  
[communications@icraindia.com](mailto:communications@icraindia.com)

## Helpline for business queries:

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

[info@icraindia.com](mailto:info@icraindia.com)

## About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit [www.icra.in](http://www.icra.in)

## ICRA Limited

### Corporate Office

Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002

Tel: +91 124 4545300

Email: [info@icraindia.com](mailto:info@icraindia.com)

Website: [www.icra.in](http://www.icra.in)

### Registered Office

1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001

Tel: +91 11 23357940-50

### Branches

Mumbai + (91 22) 24331046/53/62/74/86/87

Chennai + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,

Kolkata + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,

Bangalore + (91 80) 2559 7401/4049

Ahmedabad+ (91 79) 2658 4924/5049/2008

Hyderabad + (91 40) 2373 5061/7251

Pune + (91 20) 2556 0194/ 6606 9999

© Copyright, 2019 ICRA Limited. All Rights Reserved.

Contents may be used freely with due acknowledgement to ICRA.

ICRA ratings should not be treated as recommendation to buy, sell or hold the rated debt instruments. ICRA ratings are subject to a process of surveillance, which may lead to revision in ratings. An ICRA rating is a symbolic indicator of ICRA's current opinion on the relative capability of the issuer concerned to timely service debts and obligations, with reference to the instrument rated. Please visit our website [www.icra.in](http://www.icra.in) or contact any ICRA office for the latest information on ICRA ratings outstanding. All information contained herein has been obtained by ICRA from sources believed by it to be accurate and reliable, including the rated issuer. ICRA however has not conducted any audit of the rated issuer or of the information provided by it. While reasonable care has been taken to ensure that the information herein is true, such information is provided 'as is' without any warranty of any kind, and ICRA in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness or completeness of any such information. Also, ICRA or any of its group companies may have provided services other than rating to the issuer rated. All information contained herein must be construed solely as statements of opinion, and ICRA shall not be liable for any losses incurred by users from any use of this publication or its contents