

Power Finance Corporation Limited

Instrument	Amount rated	Rating	Rating Action
Short term borrowing programme 2015-16	Rs. 16,000 crore * (enhanced from Rs. 10,000 crore)*	[ICRA]A1+	Assigned

**Rs. 16,000 crore short term borrowing programme is interchangeable with long term borrowings, subject to total short term and long term borrowings in FY16 not exceeding Rs. 60,000 crore*

ICRA has assigned the rating of [ICRA]A1+ (pronounced ICRA A one plus) to the Rs. 16,000 crore* (enhanced from Rs. 10,000 crore) short term borrowing programme of Power Finance Corporation Limited (PFC)[†]. ICRA has a rating of [ICRA]AAA on the various long-term bond and bank borrowing programmes, an outstanding rating of MAAA (pronounced M triple A) to the fixed deposit programme and a rating of [ICRA]A1+ (pronounced ICRA A one plus) for its commercial paper/short-term debt programme of the corporation.[†]

The highest-credit-quality ratings continue to reflect PFC's majority sovereign ownership and its strategically important role in the implementation of various Government of India (GoI) schemes—such as Ultra Mega Power Projects (UMPPs) and Integrated Power Development Scheme (IPDs)—for the development of the country's power sector. Further, PFC, as one of the major power sector financiers, remains strategically important for the Government of India (GoI), given the latter's objective of augmenting power capacities across the country. The ratings continue to draw comfort from PFC's adequate earning profile supported by its strong financial flexibility and ability to borrow funds at competitive rates and low credit and intermediation costs.

These strengths are partly offset by the corporation's exposure to a single sector, its high concentration of weaker-credit-quality State power utilities and the vulnerability of its exposure to private sector borrowers. PFC's exposure to state sector utilities (70% of portfolio in Sep-15) is primarily to generation companies, while its exposure to the more vulnerable distribution entities (net of state government guarantees) of states with weaker credit profiles is limited[†]. Counter party risks of PFC's state power generating borrowers remains a credit concern given that such state generating entities could find their cash flows impacted by the weak fiscal health of the distribution entities. ICRA however notes the approval of UDAY (Ujwal DISCOM Assurance Yojana) on November 5, 2015 by GoI, a scheme with an objective to turnaround the financial health of state owned distribution companies. The scheme proposes a phased takeover of discom debt by state governments and steps to improve operational efficiencies, reduce cost of power purchase and enforce financial discipline of DISCOMs through an alignment with state finances. The scheme also envisages the states taking over the future losses of discoms from FY 2016-17 onwards in a graded manner. ICRA believes that the timely implementation of the scheme, which is optional, by State Governments remains extremely critical for ensuring the credit quality of not only the distribution companies, and also for the generation industry by enabling the discoms to offtake power as well as make timely payments. Furthermore health of the discoms would also be dependent upon adequate and timely tariff revision by SERCs including periodic pass-through of fuel cost fluctuations and timely & adequate subsidy releases by State Governments.

* Rs. 10,000 crore short term borrowing programme is interchangeable with long term borrowings, subject to total long term borrowings not exceeding Rs.60,000 crore

[†] For complete rating scale and definitions, please refer ICRA's website www.icra.in or other ICRA Rating Publications.

[†] PFCs exposure to the states of Tamilnadu, Rajasthan, Uttar Pradesh, Madhya Pradesh, Punjab, Haryana and Bihar accounted for ~15% of its total portfolio in Mar-15, while the exposure et of net of state government guarantees was ~2%

The scheme however could result in a weakening in the profitability or impact the credit growth for PFC over the next 2 years. Close to 18% of PFCs' exposures are to state discoms could come under the purview of the scheme and could get re-priced at lower rate once state governments take the debt from their respective discoms. However ICRA expects PFC to continue to maintain reasonable profitability. At the same time the package is expected to reduce the vulnerability of PFCs exposures to discoms and also reduce counter party risks on its exposure to the IPP segment.

As on Sep-15 PFCs exposure to the private sector i.e. Independent Power Producers (IPP) stood at 16% of its total advances. Several of PFCs IPP exposures have high vulnerability, being impacted by the sectoral concerns with respect to fuel availability, disputed/competitive power sale tariffs and environmental & land acquisition issues. Close to 62% of PFC's IPP exposures (or ~10% of its total advances) as on September 30, 2015 are classified as re-structured. A large share of the re-structuring however is on account of a shift in project commercial date of operations, and excluding these PFC's share of re-structured assets would be lower. ICRA favorably notes the sustained coal output growth by Coal India Ltd as seen in last 18 month period till Sept 2015 and also the possible easing of counter party risks for IPPs incase of successful implementation of the Uday scheme. At the same time significant under-recoveries due to negative price bidding in the coal auction by some of PFCs borrowers (3% of advances) affected by the coal block de-allocation is an area of concern. Going forward, it would be important for the corporation to maintain a strict control over collections from the IPP segment.

As on March 31, 2015, PFC's debt as percentage of shareholder funds was at a moderate 5.8 times³, and going forward, its ability to maintain this ratio at a prudent level given the concentrated nature of its exposures would be an important rating consideration. PFC enjoys a comfortable asset-liability matching profile with low cumulative mismatches in the short term. Un-hedged foreign currency borrowings of PFC stood at ~26% of its shareholder funds as on March 31, 2015, which exposes it to foreign currency variations. PFC adopts an accounting policy of amortizing exchange differences on long term foreign currency items over their tenure. Total un-amortized foreign currency item translation losses of PFC as on March 31, 2015 stood at Rs. 381 crore or 1.2% of shareholder funds. If these were to be charged entirely in the P&L the NIMs of the corporation could come down by around 15 bp (NIMs as on March 31, 2015 were 4.5%[‡]). Repayments on a majority of PFCs un-hedged foreign currency borrowings are largely staggered between FY 16-FY18 and such losses could crystallize unless there is a reversal in foreign currency rates by then. Going forward ability of the corporation to manage its foreign currency risks would have an important bearing over the stability of its earnings profile.

About the Corporation

PFC was set up in 1986 as specialised development financial institution to fund projects in the domestic power sector. GoI hold a 67.8% stake in the corporation as on September 30, 2015. PFC provides loans for a range of power-sector activities, including generation, distribution, transmission, and plant renovation and maintenance. PFC finances State sector entities such as State Electricity Boards and State Generating Companies, as well as IPPs. In addition, the corporation has been appointed the nodal agency to develop 16 UMPPs in the country.

As per audited results for the financial year ended March 31, 2015, PFC reported a profit after tax (PAT) of Rs. 5959.33 crore on an asset base of Rs. 2,28,664 crore, as against a PAT of Rs. 5417.75 crore on an asset base of Rs. 1,94,164 crore in the previous financial year. During the half year ended September 30, 015 the corporation reported a profit after tax of Rs. 3271.5 crore against Rs. 2856.8 crore during the corresponding period in the previous financial year. As on September 30, 2015 PFC had a gross NPA% of 1.23% and a net NPA% of 1.00%.

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[‡] As per ICRA's computation



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