

January 24, 2020

Andhra Pradesh Power Finance Corporation Limited: Rating reaffirmed

Summary of rating action

| Instrument* | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action |
|--------------------------------------|--------------------------------------|-------------------------------------|---------------------|
| Non-convertible Debenture Programmes | 4,053.30 | 4,053.30 | [ICRA]D; reaffirmed |
| Total | 4,053.30 | 4,053.30 | |

*Instrument details are provided in Annexure-1

Rationale

The reaffirmation of rating on NCD programme at [ICRA]D considers delays in the interest servicing of the rated bonds in the past because of the dispute between Telangana State Power Finance Corporation (TSPFC) and Andhra Pradesh Power Finance Corporation Limited (APPFCL) on the distribution of assets and liabilities, following the bifurcation of the erstwhile state of Andhra Pradesh (AP) in June 2014. While the servicing of the interest of the rated bonds has been on time since May 2019, timely servicing of the instruments is likely to remain uncertain till final resolution of the on-going dispute between the two states.

ICRA also notes that despite the delays in interest servicing, the Trustee to the bondholders has not invoked the guarantee extended by the Government of Andhra Pradesh (GoAP) towards the rated debt as per the terms of the structured payment mechanism.

Key rating drivers and their description

Credit Strengths

GoAP Ownership: APPFCL is fully owned by Government of Andhra Pradesh (GoAP). Considering APPFCL's critical role in extending financial assistance to power sector entities of the state, ICRA expects it to receive timely management and financial support from GoAP, when required.

Credit Challenges

Past delays in debt servicing of the NCDs: The rated bond programmes are unconditionally and irrevocably guaranteed by the GoAP. There have been delays in interest servicing of the rated bonds, in the past, because of the ongoing dispute between TSPFC and APPFCL on the distribution of assets and liabilities following the bifurcation of the erstwhile state of Andhra Pradesh in June 2014. ICRA notes that, though the payment of interest is on time since January 2018 for the APPFCL's share, there have been instances of delay for the TSPFC portion till April 2019. While the servicing of the interest of the rated bonds has been on time since then, track record of principal servicing remains to be seen. Also, till final resolution of the on-going dispute, the timely servicing of these instruments is likely to remain uncertain.

Guarantee not being invoked for the NCD programmes: Despite the event of delay in paying interest dues in the past, the Trustee to the bondholders has not invoked the guarantee extended by the GoAP towards the rated debt as per the terms of the structured payment mechanism. SBI Cap Trustee Company Limited is the debenture Trustee for the instruments from March 2017.

Modest financial risk profile of APPFCL: APPFCL earnings profile is characterized by nominal net profits; it reported a net profit of Rs. 0.01 crore in H1FY2020 (a net profit of Rs. 0.04 crore in FY2019 and a loss of Rs. 0.03 crore in FY2018). The company's cash flows are dependent on the transfers from the GoAP for meeting its operational requirements and for debt servicing. As of September 2019, APPFCL's borrowings stood at of Rs. 6,325.7 crore, all in the form of debentures guaranteed by GoAP, while net-worth stood at Rs. 16.9 crore. The company's exposure is fully towards the state power distribution companies via the GoAP managed pooled accounts.

Liquidity position - Stretched

APPFCL is dependent on the GoAP for servicing its borrowings. The GoAP has availed the Ways and Means Advances and/or the Overdraft facilities from the Reserve Bank of India on several occasions during FY2019 and FY2020 (till July 2019). Based on the aforementioned indicators, the liquidity position of the state government can be implied to have been stretched during the recent times.

Rating sensitivities

Positive triggers: The rating could be upgraded in case of resolution of the ongoing dispute between GoAP and Government of Telangana (GoTS) over the distribution of assets and liabilities and a track record of regular payment of interest and principal.

Negative triggers: Not applicable.

Analytical approach

| Analytical Approach | Comments |
|---------------------------------|---|
| Applicable Rating Methodologies | Rating Methodology for State Governments Rating Methodology for Non-Banking Finance Companies Policy on Default Recognition |
| Parent/Group Support | Parent: Government of Andhra Pradesh |
| Consolidation/Standalone | Standalone. |

About the company

APPFCL was incorporated in July 2000 by the GoAP with the main objective of providing debt and equity funding to enterprises engaged in the power sector in the state. APPFCL is registered as a non-banking finance company with the Reserve Bank of India. APPFCL reported a PAT of Rs. 0.01 crore in H1 FY2020 on a loan book of Rs. 6,325.7 crore as on September 30, 2019.

Key financial indicators (APPFCL - audited)

| | FY2018 | FY2019 |
|--------------------------------------|---------|---------|
| Total Income | 293.9 | 215.2 |
| Profit after tax | -0.0 | 0.0 |
| Net worth | 16.9 | 16.9 |
| Total managed portfolio | 2,260.1 | 2,260.1 |
| Total managed assets | 2,375.5 | 2,408.1 |
| Return on average managed assets (%) | - | - |
| Return on average net worth (%) | - | - |
| Gross NPA (%) | NA | NA |
| Net NPA (%) | NA | NA |
| Net NPA / Net worth (%) | NA | NA |

Amounts in Rs. Crore; Source: Company & ICRA Research

About GoAP's finances

GoAP's revenue expenditure has consistently exceeded its revenue receipts during FY2016 to FY2018, leading to sustained revenue deficit during these years. Its revenue deficit worsened FY2016 to Rs. 8,964.0 crore (1.3% of GSDP) in FY2017 and further to a substantial Rs. 16,205.9 crore (2.0% of GSDP) in FY2018 from Rs. 7,306.4 crore (1.2% of Gross State Domestic Product or GSDP) in. Moreover, GoAP's fiscal deficit in each of these years (3.7% in FY2016, 3.2% in FY2017 and 4.0% in FY2018) was higher than the threshold of 3% of GSDP recommended by the Fourteenth Finance Commission.

GoAP's revised estimates (RE) for FY2019 and the budget estimates (BE) for FY2020 indicate an improvement in its revenue deficit to Rs. 11,711.2 crore and further to Rs. 1,836.0 crore, respectively (refer Exhibit 1). In FY2020 BE, the GoAP has projected a considerable YoY expansion of 55.8% in its revenue receipts and 42.9% in its revenue expenditure. In particular, the state government has projected the grants from the Centre in FY2020 BE to be nearly thrice the amount that it expects to have received in FY2019 RE, which may prove optimistic. Regardless, after the introduction of the goods and services tax (GST), the state GST (SGST) collections in AP have been favourable relative to many other states, as suggested by the low receipt of GST compensation by the GoAP in FY2018 and FY2019.

The increase in GoAP's revenue expenditure in FY2020 is led mainly by sharply higher allocation to the agriculture and education sector, reflecting the introduction of various welfare schemes in July 2019. Despite the expected reduction in the revenue deficit in FY2019 RE and FY2020 BE, GoAP's fiscal deficit is expected to remain above the cap of 3% in both these years.

Reflecting the increase in GoAP's fiscal deficit, its debt outstanding rose by 12.8% to Rs. 182,380.7 crore in FY2018 from Rs. 161,755.0 crore in FY2017. Additionally, the guarantees extended by the GoAP quadrupled to Rs. 35,964.1 crore in FY2018 from Rs. 9,664.9 crore in FY2017, led by an increase in guarantees extended to sectors including agriculture, housing and urban development and power. Accordingly, its leverage (debt +guarantees) level has deteriorated to 27.0% of GSDP in FY2018 from 24.6% of GSDP in FY2017.

ICRA shall take note of the actual Central transfers received by the GoAP in FY2020. The Central Tax devolution that the state government receives in FY2020 will be contingent on the realisation of the tax collections projected by the Government of India (GoI) in the FY2020 Union Budget, which could be negatively impacted by the recent cut in corporate tax rates and the overall slowdown in the economy. Moreover, the grants projected by the GoAP in FY2020 appear to be optimistic.

Additionally, the GoAP had constituted the Eleventh Pay Revision Commission for its employees in May 2018, which is yet to submit its report. Revision in scale for employees and pensioners is likely to bloat the GoAP's expenditure, going forward

Key fiscal indicators (GoAP)

| | FY2018 | FY2019 RE | FY2020 BE |
|-------------------------------------|------------|------------|------------|
| Revenue | | | |
| Revenue Receipts* | 1,04,981.7 | 1,14,627.8 | 1,78,639.9 |
| State's Own Tax Revenue | 49,812.7 | 58,125.3 | 75,438.0 |
| State's Own Non-Tax Revenue* | 3,733.4 | 4,335.1 | 7,297.2 |
| Share in Central Taxes | 28,674.9 | 32,710.7 | 34,833.2 |
| Grants from Centre | 22,760.7 | 19,456.7 | 61,071.5 |
| Capital Receipts ^{&} | 54.3 | 56.3 | 57.5 |
| Expenditure | | | |
| Revenue Expenditure [#] | 1,21,187.6 | 1,26,339.1 | 1,80,475.9 |
| Capital Outlay | 13,490.7 | 20,398.2 | 32,293.4 |
| Net Lending | 2,730.2 | 1,565.9 | 1,188.7 |
| Revenue & Fiscal Balance | | | |
| Revenue Balance | -16,205.9 | -11,711.2 | -1,836.0 |
| Fiscal Balance | -32,372.6 | -33,619.0 | -35,260.6 |
| Leverage | | | |
| Debt [@] | 1,82,380.7 | 2,08,346.1 | 2,43,725.3 |
| Guarantees | 35,964.1 | NA | |

*Adjusted for sale of land, debt relief from Government of India and double entries of interest on loans of departmental commercial undertakings.

& Adjusted for sale of land; Amount in Rs. crore

#Adjusted for double entries of interest on loans of departmental commercial undertakings.

@Includes internal debt; loans from the Centre; provident fund etc

Source: State Budget, Finance Accounts and ICRA research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

| | Instrument | Current Rating (FY2020) | | | | Rating History for the Past 3 Years | | |
|---|------------|-------------------------|--------------|--------------------|-----------|-------------------------------------|-----------|-----------|
| | | Type | Amount Rated | Amount Outstanding | Rating | FY2019 | FY2018 | FY2017 |
| | | | | | 24-Jan-20 | 23-Nov-18 | 09-Oct-17 | 27-Sep-16 |
| 1 | NCD | Long Term | 4,053.3 | 4,053.3 | [ICRA]D | [ICRA]D | [ICRA]D | [ICRA]D |

Amount in Rs. crore

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

Annexure-1: Instrument details

| ISIN | Instrument Name | Date of Issuance / Sanction | Coupon Rate | Maturity Date | Amount Rated (Rs. crore) | Current Rating and Outlook |
|--------------|---------------------------|-----------------------------|-------------|---------------|--------------------------|----------------------------|
| INE847E09011 | Non-convertible Debenture | 15-11-2010 | 8.49% | 15-11-2020 | 42.0 | [ICRA]D |
| INE847E09029 | Non-convertible Debenture | 15-11-2010 | 8.74% | 15-11-2022 | 1,011.3 | [ICRA]D |
| INE847E08DK6 | Non-convertible Debenture | 15-12-2011 | 9.60% | 15-12-2023 | 149.2 | [ICRA]D |
| INE847E08DJ8 | Non-convertible Debenture | 15-12-2011 | 9.10% | 15-12-2021 | 5.0 | [ICRA]D |
| INE847E08DM2 | Non-convertible Debenture | 30-01-2012 | 9.97% | 30-01-2024 | 586.9 | [ICRA]D |
| INE847E08DL4 | Non-convertible Debenture | 30-01-2012 | 9.85% | 30-01-2022 | 157.2 | [ICRA]D |
| INE847E08DO8 | Non-convertible Debenture | 08-06-2012 | 9.64% | 08-06-2024 | 249.4 | [ICRA]D |
| INE847E08DN0 | Non-convertible Debenture | 08-06-2012 | 9.50% | 08-06-2022 | 64.7 | [ICRA]D |
| INE847E08DQ3 | Non-convertible Debenture | 09-11-2012 | 9.75% | 09-11-2022 | 1,787.6 | [ICRA]D |

Source: Andhra Pradesh Power Finance Corporation Limited

Annexure-2: List of entities considered for consolidated analysis

Not applicable

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