Association of Power Producers

MEETING WITH EXPERT COMMITTEE

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26th August 2020

RBI Circular on Resolution Framework for COVID-19 related stress dated 06.08.2020

APP Members

Focus: Power Sector

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- Power Sector value chain comprises:
  - Generation
  - Transmission
  - Distribution
- Huge stress in distribution*
  - Losses – ~Rs. 61,000 Cr
  - Debt – ~Rs. 4,78,000 Cr.
  - Regulatory Assets – ~Rs. 50, 000 Cr. - Impairs Discoms' ability to pay power generation companies
- **Presentation covers issues related to power generation only**

*Source: PFC - Report on Performance of State Power Utilities 2018-19

Focus: Private investment in Generation

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- Generation segment comprises :
  - **Thermal**
    - **Coal**
    - **Gas**
  - Hydro
  - Nuclear
  - Renewable
    - Solar
    - Wind
    - Biomass
    - Others
- **Presentation covers issues related to private sector thermal generation**

Status of stressed private sector investments in thermal generation

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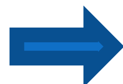
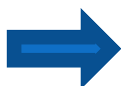
Coal Based Capacity
~ 75,000 MW (75 GW)



Category	Stressed Capacity (GW)	Investment (Rs. Crore)
No Coal, No PPA – Completely stranded	8.3 GW	50,000
Projects with partial PPA and coal – Partially stranded, cash flows inadequate to meet debt service fully	11.3 GW	68,000
Projects with PPA and coal but suffering due to under-recovery of costs/revenues (change in law items and huge backlog of receivables – **Rs 71,745 Cr**)	34.5 GW	2,10,000
Total	**54.1 GW**	**3,28,000**

Gas Based Capacity
~ 11,000 MW (11 GW)



Almost entirely stranded due to non-availability of gas (Investment of Rs. 42,000 Crore)

Majority of the private investment 65,000 MW; Rs. 3,70,000 Cr., ~30 private players in the power generating sector is stressed due to one or more of the above factors

Stress further accentuated due to FGD Implementation mandated by MOEF / Supreme Court

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- Private coal based generation projects (~75 GW) to implement mandatory capex for Flue Gas Desulphurization (FGD)
- Capex of ~Rs. 56,000 Crore
  - Debt : Rs. 39,000 Crore
  - Equity : Rs. 17,000 Crore
- **Challenges in meeting equity requirement due to existing stress**
- **Existing Lenders reluctant to provide any debt funding**

FGD execution is a massive challenge

Credit Ratings : Stress is visible

- Out of 36 outstanding ratings of private thermal generators
  - 20 are below investment grade
  - 6 are barely in investment grade
- **72% outstanding ratings highlight existence of acute stress, independently confirmed by credit rating agencies – CRISIL, ICRA, CARE and India Ratings**

Stress independently confirmed by credit rating agencies

RBI Circular on 'Resolution Framework for COVID-19 Related Stress' dated 06.08.2020

Objectives

- Revival of real sector activities
- Mitigate impact of COVID 19 on the borrower

Issues towards approach to resolution

- "One size fits all " approach can not work
- Issues across sectors are distinct
- Infrastructure sectors require a distinct approach when compared to Aviation/Hospitality/Travel
- Even within Infrastructure, Power Sector requires "A la Carte" approach, distinct from other infrastructure sectors, such as, Roads

RBI Circular on 'Resolution Framework for COVID-19 Related Stress' dated 06.08.2020

Key Issues

- **Overlooks the fatal impact of COVID-19 on already stressed projects which do not fall under the eligibility criteria of the circular.**
- Provides a common solution across all sectors, i.e. extension of residual tenor by not more than 2 years, **without considering that power sector in view of its distinct attributes, would require longer timeframe for resolution – since PPAs are usually for 25 years**
- Valuation/cash flows of projects differ widely based upon crucial parameters such as PPA tie ups, tariffs and coal supplies – **absolute sectoral benchmarks may not give a true representative picture– a set of single values for prescribed financial parameters will not work**

Electricity sector value chain is Regulated and dominated by Government Instrumentalities - Cannot be equated with other sectors.

Fuel supply, its transportation, transmission of generated power and finally, the payment for power is controlled by Government owned monopolies.

‘Stressed’ vs ‘Non Stressed’ – Key Differentiator

- In Private Sector, of the ~**75 GW** Coal based Capacity, **54 GW (73%) is stressed.**
- In Public Sector (i.e. Central & State) - Have either “sovereign” or “state” back-up
  - **147 GW** Coal based Capacity – **‘NIL’ is stressed**

Key Differentiators are:

- Security of Fuel and offtake embedded in Section 62 tariff determination
  - Public sector projects secure PPAs and coal linkage despite higher tariffs
- Regulated Tariffs (Cost plus –increases pass through without any Regulatory Intervention)
- Payment security mechanism under Tripartite Agreement (RBI, States, Central generator)

Many of the systemic risk factors are likely to be resolved over the next 3-4 years:

- Supply side – slowing of new thermal capacity addition and demand set to increase with higher household electrification and push for Electric Vehicles and large scale railway electrification
- Fuel - Coal availability is set to increase with commercial coal mining, and the Government is actively considering decoupling the access to coal and PPA.

Keeping the above in mind, extension of residual tenor of loan by a longer period of ~6 years (keeping a minimum tail period of 1 year) may be considered for the power sector.

Sector specific financial parameters to be recommended by the Expert Committee

- Objective of restructuring
  - Long-term viability
  - Minimum Investment grade rating
  - Security to Lenders
  - Reduction of NPAs
- Thermal tariffs already in Rs. 4.0 – 6.0 / kWh – Off-taker Discoms reluctant to honour PPAs /schedule power from such projects and pay for the same
- Off-takers enjoy low tariffs of Rs. 2.5 – 3.0 / kWh for 25 years from solar and wind projects
- Hence tariff increase is not an option for restoring viability
- Comprehensive definition of Restructuring under para 13 (footnote 7) of RBI circular dated 7th June 2019 needs to be adopted, **which includes changes in loan maturity; reduction in rate of interest; additional credit facility; enhancement of limits; modification of terms of securities, i.e. conversion of debt into equity / other securities**

Restructuring needs to be multi-dimensional and in totality

Sector specific financial parameters to be recommended by the Expert Committee

- Financial parameters to be recommended need to take into account the following:
  - **Debt levels and related parameters should ensure that the debt quantum remains sustainable in the long term**
  - **Thermal Projects which have major untied capacity and lack of fuel tie up should be assessed based on realistic future tariff assumptions.**

Suggested normative financial parameters for private power gencos which do not have major untied capacity and lack of fuel tie up:

- Average DSCR of 1.20
- Minimum Interest Coverage Ratio of 1.75
- Debt to Equity : around 2.33 : 1 (i.e. 70:30)

For projects which have major untied capacity and lack of fuel tie up, the above parameters have to be kept flexible with the banks given discretion within certain limits.

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8 Issues regarding RBI Circular which need to be addressed

1. Eligibility and Applicability
2. Stipulation of Inter-Creditor Agreement
3. Provisioning requirements
4. Timeline for RP implementation
5. Review of RP by Expert Committee and CRAs
6. Conversion into other securities and valuations
7. Debt funding of FGDs
8. DSRA stipulations

Eligibility and applicability

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Existing Stipulation

- The circular allows **only those accounts eligible for restructuring which were classified as Standard, and were not in default for more than 30 days as on 1st March 2020.**

Suggestion & Rationale

- **To allow all COVID-19 affected accounts which are Standard as on 1st March 2020 (i.e. all accounts which were not in default for more than 89 days).**
  - *Will help stressed accounts, which has the highest risk due to Covid , but not NPA as on 1st March 2020*
  - *7th June RBI circular provision making any loan NPA if restructured, without change in control, majorly disincentivizes banks and discriminates against existing promoters*

- **To include Restructured accounts which are timely servicing their debt obligations but are in Monitoring period.**
  - *Due to timely servicing of debt obligations, these accounts are as good as Standard accounts hence, in case these are impacted by Covid , this circular should be made applicable to such restructured accounts.*

- **To include Projects under Implementation.**
  - *Suitable relief measures like DCCO extension for unprecedented impact of Covid , shifting of repayment schedule should be considered.*

Stipulation of Inter-Creditor Agreement

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Existing Stipulation

- The circular stipulates signing of ICA within 30 days of from the date of invocation

Suggestion & Rationale

- **Bilateral Restructuring may be permitted.**
  - *In case of Holding Companies, the borrowings are normally done on multiple banking arrangements where repayment terms, security structure, etc. are different for Lenders. Therefore, Bilateral Restructuring may be permitted.*

Provisioning Requirements and Timeline for RP implementation

Existing Stipulation

- Circular mandates repayment of 30% of residual debt for reversal of entire provisioning
- The circular provides 180 days for RP implementation, and imposes additional provisioning (20%-35%) for failure to abide by this timeline

Suggestion & Rationale

- **Lenders should be allowed to reverse entire 10% provisioning upon payment of 10% of residual debt, in line with 7th June circular**
  - *Current provisions re: reversal of provision appear to dis-incentivize lenders to proceed with restructuring pursuant to the circular*
- **Timeline for implementation of RP to be extended to 270 days.**
  - *significant procedural time taken to finalize broad contours of RP and then its implementation given the board approval process with large no of banks in consortium lending as also time taken for allotment of securities, registration, etc.*

Review of Resolution Plans (RPs) by Expert Committee (EC) & rating by Credit Rating Agencies (CRAs)

Existing Stipulation	• Resolution Plans to be evaluated by Credit Rating Agencies • Expert Committee to submit sector specific parameters (leverage / liquidity / debt servicability, etc.) and to vet Resolution Plans for accounts with exposure > Rs.1500 Cr
Suggestion & Rationale	▪ **Lenders be allowed to implement RP if same has been agreed by lenders more than 75% by value and 60% by numbers, notwithstanding rating assigned to RP.** ▪ Valuation of power sector companies depends on PPA tie-up, tariffs and coal supplies. Hence, EC may abstain from considering absolute sectoral benchmarks (like Rs. Cr / MW etc). Further, banks should have some flexibility with normative financial ratios to be prescribed generally ▪ **Definition of Restructuring under Para 13 of 7th June circular to be adopted and address issues, if any, relating to Drawing Power of WC. Banks to approach restructuring on the basis of sustainable debt for a given project.** Unsustainable debt to be dealt with as enabled by the RBI circular. ▪ **For Projects with tied offtake and fuel : Avg. DSCR: 1.2; Min ICR: 1.75; DER : ~2.33:1; for other projects banks to be given flexibility within certain limits**

Conversion into other securities and valuation

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Existing Stipulation

- The portion of debt converted into other security will be valued at Rs. 1 (in the books of the Bank)

Suggestion & Rationale

- **Valuation of such other securities may be guided RBI's Master Circular on Prudential Norms for Classification, Valuation and Operation of Investment Portfolio by Banks dated July 1, 2015.**

  - *Current stipulation would require banks to make 100% provisioning on part of debt converted into such other securities like Preference Shares etc. Hence, it would restrict the options available with banks.*

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Conversion into other securities and valuation

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Existing Stipulation

- In case of conversion of portion of debt into equity or other marketable , non-convertible debt securities
  - Coupon & amortization schedule for non-convertible debt securities to be similar to existing term loan

Suggestion & Rationale

- **Lenders should be given due flexibility to decide coupon and amortization schedule of non-convertible debt securities in alignment with expected cashflows, keeping overall yield of such securities similar to term loan.**

  - *Where regular cash flows are not fully adequate, NCDs may be issued with different repayment schedule as also with varying coupon , providing redemption premium, etc. to ensure the yield while keeping cash flow profile in view, so that the structure is sustainable*

Additional Suggestions re: Debt Funding for FGDs

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Suggestion
&
Rationale

Debt Funding for Flue Gas Desulphurization (FGD)

- Existing lenders in a consortium to provide proportionate debt funding.
- PFC/REC to step in where existing lender(s) are unable to provide debt funding due to regulatory constraints.
- Debt : Equity ratio for FGD to be higher than 70:30 norm considering deleveraging already achieved through repayments of original project debt.
- To use corpus mobilized through Clean Environment Cess (~Rs. 86,000 Crore)

- *Implementation of Flue Gas Desulphurization (FGD) is mandatory for all coal based plants.*
- *Securing debt finance has become a key challenge.*
- *Delays in implementation due to lack of debt funding would have grave consequences*

Additional Suggestions re: DSRA

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Suggestion
&
Rationale

Debt Service Reserve Account (DSRA)

- **Lenders not to insist on Loan covenant relating to DSRA till FGD implementation and allow gradual DSRA build up thereafter**

  - *Implementation of Flue Gas Desulphurization (FGD) is mandatory for all coal based plants.*
  - *Most IPPs are facing financial stress and are unable to build DSRA though required under loan agreements*
  - *COVID-19 has further delayed outcomes of key regulatory matters and impaired ability to build DSRA.*
  - *Available internal generation would need to be utilized to meet equity requirement of FGD, making immediate DSRA build-up impossible*

Summary

- Resolution of stress in private sector thermal generation companies require a flexible approach targeted at ensuring long-term viability.
- All the levers available for restructuring under the RBI Circular dated 7th June 2019 need to be used
- Need to squarely address FGD implementation challenges

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Thank you