

West Bengal State Electricity Distribution Company Limited

October 29, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-Convertible Bond Series - I	250.00	250.00	[ICRA]BBB- (Negative) revised from [ICRA]BBB(Stable)
Non-Convertible Bond Series - II	250.00	250.00	[ICRA]BBB- (Negative) revised from [ICRA]BBB(Stable)
Non-Convertible Bond Series - III	500.00	500.00	[ICRA]BBB- (Negative) revised from [ICRA]BBB(Stable)
Total	1000.00	1000.00	

*Instrument details are provided in Annexure-1

Rating action

ICRA has revised the long-term rating assigned to the non-convertible bond programmes of West Bengal State Electricity Distribution Company Limited (WBSEDCL or the company)¹ accumulating to Rs. 1000-crore² from [ICRA]BBB (Pronounced [ICRA] Triple B) to [ICRA]BBB- (Pronounced [ICRA] Triple B Minus). The outlook on the long-term rating has been revised to Negative from Stable.

Rationale

The revision in the long-term rating and change in outlook reflect WBSEDCL's increased regulatory uncertainty arising from the delay in release of tariff order for FY2019. ICRA notes that WBSEDCL's effective approved tariff of Rs. 7.12/unit³ has not undergone any revision since October 2016, and with the average power purchase cost steadily increasing from Rs. 3.50/unit⁴ in FY2017 to Rs. 3.73/unit in FY2018, the utility has continued to pile-up fresh-regulatory assets during FY2018⁵. In the current fiscal, with Coal India Limited (CIL) increasing domestic coal prices from January 2018 onwards, the effect of which would fully flow-in during FY2019⁶, and with domestic e-auction coal prices and short-term power prices remaining at elevated levels, ICRA expects WBSEDCL's power purchase cost to increase further in the current fiscal, the early effects of which are noticeable from the upward revision in the monthly fuel cost adjustment (MFCA) by West Bengal Power Development Corporation Limited (WBPDCCL)⁷ from an average level of 46 paisa/unit in FY2018 to 80 paisa per unit in April – August of FY2019. With WBSEDCL's tariff levels remaining flat, rising power purchase costs are expected to exert pressure on the utility's cash-flows going forward.

The gap between WBSEDCL's average cost of supply (ACS) and effective approved tariff (including monthly variable cost adjustment, MVCA) had remained high during the period FY2014 to FY2016, ranging between Rs. (0.95-1.87)/unit.

¹ For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications

² 100 lakh = 1 crore = 10 million

³ Includes monthly variable cost adjustment of 23 paisa/unit levied from July 2016

⁴ Figures exclude arrears power purchase costs, and reflects current period costs only

⁵ WBSEDCL's ACS stood at an estimated Rs. 7.60/unit in FY2018 against an approved tariff of Rs. 7.12/unit, leading to a gap of Rs. 0.48/unit

⁶ Linkage coal prices from CIL for the power sector has increased by an estimated 11% between December 2017 and January 2018 for G11 grade coal consumed by a plant located at a distance of 276-350 km from the mine-head

⁷ WBPDCCL accounted for ~56% of WBSEDCL's power purchase mix in FY2018

Consequently, around 85% of the utility's outstanding regulatory assets had been created during this period. The annual performance review orders (APR) from the year FY2014 is awaited still, thereby accentuating regulatory uncertainties, and consequently, WBSEDCL had to resort to rising borrowing levels to fund the cash-flow timing mismatches. ICRA notes that in the past few years, WBSEDCL has been frequently borrowing against approved regulatory assets, which have helped the utility tide over the revenue account deficits. However, with all regulatory assets created till FY2013 being already crystallised through tariff, and with the APR orders from FY2014 being awaited, the incremental borrowing against approved regulatory assets would remain challenging, and this is expected to adversely impact the liquidity profile. Moreover, with WBSEDCL's normative working capital remaining nil, and given the constraint in the recoverability of carrying cost on regulatory assets created since FY2014 in the absence of the corresponding APR orders, the utility has witnessed an under-recovery in interest cost incurred on working capital. WBSEDCL's interest cost on working capital has steadily increased from Rs. 220.7 crore in FY2013 to Rs. 783.5 crore in FY2018, and with the company's working capital borrowings expected to increase in the near to medium term, the timely release of pending APR orders, and passing the carrying cost through tariff, would remain critical from the regulatory risk perspective.

WBSEDCL has an outstanding regulatory asset balance of Rs. 11,910 crore as on March 31, 2018. In the tariff order for FY2018, regulatory assets of Rs. 522.3 crore have been allowed to be crystallised through tariff, and at this rate of crystallisation, it would require a prolonged recovery period. In this context, ICRA understands that the Government of West Bengal is considering a proposal to take over 75% of the outstanding regulatory asset balance, amounting to around Rs. 7500 crore⁸. Timely support from the State Government for crystallisation of the outstanding regulatory assets would remain extremely critical from the credit perspective, and ICRA would reassess the credit profile of WBSEDCL following a greater clarity on the timing and the quantum of support.

WBSEDCL has been exporting 250-MW power to Bangladesh, which had generated healthy profits of Rs. 209 crore in FY2018 and Rs. 312 crore in FY2017. However, with the existing contract expiring in September 2018, and renewal of the agreement being made for a lower quantum and reduced tariff, WBSEDCL's profits from trading sales is expected to be considerably lower from H2 FY2019 onwards, which has also been a factor constraining the rating.

WBSEDCL's rating, however, continues to derive strength from its status as a fully-owned Government of West Bengal entity, which imparts financial flexibility, and its regulated nature of operations, based on a "cost-plus" tariff regime. WBSEDCL's rating also derives strength from its favourable consumption mix, as indicated by a low share (less than 5%) of agricultural consumers, and an operational MVCA regime, allowing for a mechanism for pass-on of rising power purchase cost. ICRA notes that between FY2011 and FY2018, WBSEDCL's consumer base has almost doubled from 85 lakh to 181 lakh. This expansion has been largely in the low and medium voltage (L&MV) categories, being led by large rural electrification programmes. This has led to a significant increase in rural electrification coverage in West Bengal from 55% in FY2011 to 99.8%⁹ in FY2018. In addition, the utility has been able to ensure 24 hours of power supply in the rural areas.

Given the large increase in the L&MV consumer base, WBSEDCL's distribution losses have steadily increased from 23.8% in FY2009 to a peak level of 28.0% in FY2014. WBSEDCL's distribution losses remained sticky between FY2015 and FY2017, ranging in a narrow band of 27.5% - 27.7%, but subsequently, there has been a noticeable annual reduction of 0.8% in FY2018, supported by a recovery in demand from high voltage and extra-high voltage (HV&EHV) consumers, and various loss-reduction initiatives by the company. Notwithstanding the same, WBSEDCL's distribution loss of 26.7% in FY2018 was significantly higher than the normative allowed loss of 17.5% during the period, leading to under-recoveries

⁸ In FY2017 and FY2018, GoWB had provided grant accumulating to Rs. 2647.09 crore, which has been largely utilised to repay State Government loans; the utility's external borrowings from banks/FIs have not declined following the release of this grant

⁹ Source: FY2018 Budget speech of the Department of Power & Non-Conventional Energy Sources, Government of West Bengal

in the power purchase cost¹⁰. However, unlike the high distribution loss levels, WBSEDCL's collection efficiency has remained at healthy levels, and has improved steadily from 96.0% in FY2015 to 98.8% in FY2018. ICRA notes that a reduction in distribution loss, coupled with improving collection efficiency, has led to a reduction in WBSEDCL's AT&C loss from 29.0% in FY2017 to 27.6% in FY2018 (1.4% annual reduction), in turn supporting an 11% year-on-year (YoY) rise in revenue collected for sale of power during FY2018. Going forward, supported by various system strengthening schemes to minimise losses, WBSEDCL has targeted an AT&C loss reduction of around 3% annually between FY2019 and FY2022, and its ability to adhere to the stated loss reduction trajectory would remain critical from the profitability perspective.

WBSEDCL's debt protection metrics have remained constrained. The company's total debt to EBITDA¹¹ (adjusted for regulatory income and other non-cash notional income) stood at 14.2 times in FY2018. Moreover, WBSEDCL remains exposed to significant refinancing risks. During FY2018, WBSEDCL had a cash-flow deficit of Rs. 1528 crore after meeting scheduled debt servicing commitments¹², which has been funded through a mix of incremental working capital borrowings, short term loans, and borrowings against approved regulatory assets. Given that WBSEDCL has large lumpy debt repayments falling due in FY2019 and FY2020, in an environment of rising power purchase costs, the utility is expected to increasingly rely on working capital borrowings to fund such cash-deficits for meeting scheduled debt repayments in the near to medium term. ICRA notes that over the years, WBSEDCL has demonstrated healthy financial flexibility, given its status as a Government of West Bengal owned entity, which mitigates the refinancing risks to an extent. Going forward, the company's ability to arrange alternate funding channels to tide over cash-flow timing mismatches would remain critical from the liquidity perspective.

Outlook: Negative

ICRA believes that WBSEDCL's credit profile would continue to remain constrained because of the consistent gap between ACS and approved tariff, and lumpy debt repayments falling due in FY2019 and FY2020. The outlook may be revised to 'Stable' if the financial position improves on the back of adequate tariff revisions, and a demonstrated track-record of adherence to the stated loss reduction trajectory.

Key rating drivers

Credit strengths

Status of the company as a fully owned Government of West Bengal owned entity, which gives financial flexibility – WBSEDCL enjoys healthy financial flexibility, given its status as a State Government owned entity. In the current fiscal, the company has successfully increased the working capital facilities from Rs. 5500 crore to Rs. 6500 crore.

Regulated nature of operations, wherein, tariffs are based on "cost-plus" principles – WBSEDCL operates under a "cost-plus" based tariff regime. The company's regulated return on equity stands at Rs. 372.4 crore at present, and subject to adhering to normative parameters, the company would be able to generate steady returns.

Presence of an MVCA regime leads to a mechanism for pass-on of higher power purchase costs – WBSEDCL has an operational MVCA regime, which allows a mechanism for prompt pass-on of increases in power purchase costs. Given that the power purchase cost accounts for around 80% of the total cost of operations (including capital charges) for a power distribution company, an operational MVCA mechanism augers well for WBSEDCL. At present, WBSEDCL has been

¹⁰ In July 2013, through a regulatory change, the West Bengal Electricity Regulatory Commission has restricted the disallowed power purchase cost for WBSEDCL to the allowed return on equity plus net UI receivable

¹¹ Earnings before interest tax depreciation amortisation

¹² Indicates funding deficit after covering for operating costs and debt service commitments, but before meeting capex commitments

levying an MVCA of 23 paisa/unit in addition to the approved tariff of Rs. 6.89/unit, leading to an effective tariff of Rs. 7.12/unit.

Favourable consumption mix reflected by a low share from agricultural consumption – WBSEDCL's share of sale from agricultural consumers remain low, at less than 5% by volumes, which leads to low cross-subsidy. Moreover, WBSEDCL has achieved almost 100% consumer metering.

High level of collection efficiency - WBSEDCL's collection efficiency has improved consistently from 96.0% in FY2015 to 98.8% in FY2018, and has played a critical part in the reduction in AT&C loss from 30.7% in FY2015 to 27.6% in FY2018.

Consistent funding support from the State and Central Governments for various capital projects – Between FY2016 and FY2018, WBSEDCL has incurred a cumulative capex of Rs. 6733 crore, of which ~58% has been funded by grant inflows from the State and Central Governments. ICRA notes that given the company's stiff loss reduction targets, the funding support from Government funded schemes towards capital projects targeted towards loss reduction would aid the company.

Credit challenges

Weak debt protection metrics – WBSEDCL's debt protection metrics have remained weak. The total debt to EBITDA (adjusted for regulatory income and other non-cash notional income) stood at an adverse 14.2 times in FY2018. Given the company's rising borrowing levels, debt protection metrics is expected to remain weak in the near to medium term.

Regulatory uncertainty because of delay in release of tariff order and true-up orders – WBSEDCL has been exposed to considerable regulatory uncertainty, given that the tariff order for FY2019 is pending, and APR orders are awaited from FY2014 onwards. This has led to a large pile-up of regulatory assets. Moreover, WBSEDCL's tariff levels have remained flat since October 2016, and with power purchase costs on a rising trend, fresh build-up in regulatory assets is likely to increase.

Exposure to refinancing risks, given the lumpy debt repayments, and revenue account deficits – WBSEDCL has large debt repayments falling due in FY2019 and FY2020. Given the pressure on its cash-flows for meeting scheduled debt service commitments, the company would remain exposed to refinancing risks. Going forward, WBSEDCL's ability to arrange fresh credit lines to tide over the cash-flow timing mismatches would remain a key rating sensitivity.

Elevated distribution loss levels, being considerably higher than normative levels, adversely impacting profitability – Notwithstanding an improvement in FY2018, WBSEDCL's distribution loss remains considerably higher than the normative level of 17.5%, leading to under-recoveries in power purchase costs and sub-optimal returns.

Trading profits from power export expected to decline going forward – Trading profits from the export of power to Bangladesh has been a source of healthy profits for WBSEDCL over the previous years. However, WBSEDCL's trading profits are expected to decline considerably from H2 FY2019, following a reduction in the contracted quantity, and a downward revision in the tariff rates with Bangladesh.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

Links to applicable criteria:

[Corporate Credit Rating Methodology](#)

[Rating Methodology for Power Distribution Utilities](#)

About the company:

WBSEDCL was incorporated on February 16, 2007, post unbundling of the erstwhile West Bengal State Electricity Board (WBSEB), in line with the requirement under the Electricity Act 2003. The erstwhile WBSEB has been divided into a) West Bengal State Electricity Distribution Company Limited and b) West Bengal State Electricity Transmission Company Limited (WBSETCL) in accordance with a transfer scheme notified by the Government of West Bengal dated January 25, 2007. As a part of the transfer scheme, the functions and business of power transmission and load dispatch activities have been transferred to and vested with WBSETCL, and that of power distribution and activities related to hydro-power undertakings have been transferred to and vested with WBSEDCL, which has ~1,063.5 MW of hydro-power capacity, including a 900-MW pumped storage hydro power plant (primarily for meeting peak power loads). WBSEDCL is a power distribution licensee for almost the entire state of West Bengal, except for certain areas, which are catered to by private distribution licensees. WBSEDCL accounts for about 80% of the power supply in the state and caters to almost 181 lakh customers (including ~4,671 high voltage customers).

In FY2018, the company reported a net loss of Rs. 40.3 crore on an operating income of Rs. 20,687.9 crore, as compared to a net loss of Rs. 25.3 crore on an operating income of Rs. 19,908.3 crore in the previous year.

State Profile – Government of West Bengal

West Bengal's performance on certain social indicators such as literacy rate (77.1% in 2011), infant mortality rate (25 per 1,000 live births in 2016) and Human Development Index (0.57 in 2012), are superior relative to the respective national averages (74.0%, 34 per 1,000 live births and 0.55). The poverty level in the state (29.7%) was largely in line with the national average (29.5%) in 2012. However, the per capita income in the state at Rs. 83,125.8 (base year FY2012; current prices¹³), was significantly lower than the national average (Rs. 1,03,869.6) in FY2017.

The Government of West Bengal's (GoWB's) fiscal performance continues to be unfavourable, with a muted own tax effort, a substantial proportion of committed expenditure, sustained revenue deficits and high indebtedness. Moreover, the capital expenditure in the state averaged a modest 1.4% of gross state domestic product (GSDP) in FY2016 and FY2017.

The GoWB expects its revenue deficit to correct sharply to Rs. 17.2 crore in its budget estimates (BE) for FY2019 from Rs. 11,021.7 crore in its revised estimates (RE) for FY2018. Nevertheless, the actual figures for previous years indicate that the sharp improvement expected by the GoWB in its revenue account may be optimistic. The GoWB's fiscal deficit was estimated to rise from Rs. 25,385.4 crore in FY2017 to Rs. 29,698.4 crore in FY2018 RE, before narrowing to Rs. 23,805.4 crore in FY2019 BE. However, the GoWB's fiscal deficit, which was below the cap of 3.0% of GSDP recommended by the FFC in FY2017, is estimated to remain within this cap in FY2018 RE and FY2019 BE, according to the Medium Term Fiscal Policy Statement for FY2019.

The leverage levels (debt¹⁴ + guarantees) of the GoWB stood at a relatively unfavourable 36% of GSDP and 6.9 times States Own Tax Revenues in FY2017.

Going forward, ICRA shall take note of the buoyancy of the Goods and Services Tax collections, the impending pay revision, and the impact of the evolving macroeconomic scenario on the pace of growth of own and Central tax revenues on various fiscal indicators and the overall credit profile of the state government.

¹³ Source: Central Statistical Organisation (CSO).

¹⁴ Includes internal debt; loans from the Centre; provident fund etc.

Key standalone financial indicators of WBSEDCL (audited)

	FY2017	FY2018
Operating Income (Rs. crore)	19,908.3	20,688.0
PAT (Rs. crore)	-25.3	-40.3
OPBDIT/OI (%)*	2,555.9	2,323.5
RoCE (%)*	6.3%	5.3%

Total Debt/TNW (times)**	0.9	0.9
Total Debt/OPBDIT (times)*	4.9	5.7
Interest coverage (times)*	1.6	1.7

*includes regulatory income and other non-cash notional income booked during the year; adjusting for non-cash revenues, and including non-operating income, the total debt/EBITDA stood at 14.2 times in FY2018; **grant and consumer contribution included in capital reserves

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

Instrument	Current Rating (FY2019)				Chronology of Rating History for the Past 3 Years			
	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2018	Date & Rating in FY2016	Date & Rating in FY2014	
				29-Oct-18	5-Jul-17	29-Mar16	31-Mar14	
1 Non-Convertible Bond Series - I	Long Term	250.00	250.00	[ICRA] BBB- (Negative)	[ICRA] BBB (Stable)	[ICRA] BBB (Stable)	[ICRA] BBB+ (Stable)	
2 Non-Convertible Bond Series – II	Long Term	250.00	250.00	[ICRA] BBB- (Negative)	[ICRA] BBB (Stable)	[ICRA] BBB (Stable)	[ICRA] BBB+ (Stable)	
3 Non-Convertible Bond Series - III	Long Term	500.00	500.00	[ICRA] BBB- (Negative)	[ICRA] BBB (Stable)	[ICRA] BBB (Stable)	[ICRA] BBB+ (Stable)	
4 Issuer Rating	-	-	-	-	Withdrawn	IrBBB (Stable)	IrBBB+ (Stable)	

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 No	Instrument Name	Date of Issuance	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE411L07015	August 2010	9.34%	August 2025	250.00	August 2010	[ICRA]BBB- (Negative)
INE411L07023	October 2010	9.34%	October 2025	250.00	October 2010	[ICRA]BBB- (Negative)
INE411L07031	August 2011	10.85%	August 2026	500.00	August 2011	[ICRA]BBB- (Negative)

Source: Company

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