CRISIL
An S&P Global Company

Rating Rationale

April 30, 2020 | Mumbai

U. P. Power Corporation Limited

Rating Reaffirmed

Rating Action

Rs.4235.4 Crore Bond	**CRISIL A+(CE)/Stable (Reaffirmed)**
Rs.5170 Crore Bond	**CRISIL A+(CE)/Stable (Reaffirmed)**
Rs.264.6 Crore Bond	**CRISIL A+(CE)/Stable (Withdrawn)**
Rs.323.0 Crore Bond	**CRISIL A+(CE)/Stable (Withdrawn)**

1 crore = 10 million
Refer to annexure for Details of Instruments & Bank Facilities

Detailed Rationale

CRISIL has reaffirmed its 'CRISIL A+(CE)/Stable' rating on the bonds of U. P. Power Corporation Limited (UPPCL). CRISIL has withdrawn its ratings on the company's bonds of Rs 587.6 crore (see Annexure: Details of ratings withdrawn) on confirmation from the debenture trustee that they have been fully redeemed. The rating withdrawal is in line with CRISIL's policy.

The rating continues to factor in the strength of the unconditional, irrevocable guarantee provided by the Government of Uttar Pradesh (GoUP) and the trustee-administered escrow and payment mechanism for the bonds. The rating also reflects adequate liquidity for UPPCL bonds, in the form of a debt service reserve account (DSRA).

UPPCL is adhering to a defined T structure where electricity receivables are escrowed into a bond servicing account on a daily basis so as to adequately fund the account by T-15 days prior to the entire debt servicing requirement for that quarter. While collections from the customers have reduced substantially over the last one month due to the Covid-19 outbreak, the same remains sufficient to fund the bond servicing account on a daily basis. Any substantial delay in receiving collections, leading to non-adherence to the T structure and hence utilisation of the DSRA to meet the debt servicing requirements, remains a rating monitorable.

The rating also factors in GoUP's healthy revenue surplus and own tax buoyancy with its large economic base. These strengths are partially offset by UPPCL's sizeable debt with moderate economic management, delayed traction in power sector reforms, weak socio-economic parameters, and below-average financial performance.

The Covid-19 pandemic is expected to impact overall state finances. Inflow of various tax revenue for the state (accounts for about 35% of revenue receipts), including state GST, sales tax, VAT on petroleum products, stamps and registration duties, motor vehicle tax etc will be lower due to the nationwide lockdown. Furthermore, allocations for expenditure, especially in social sectors such as health, sanitation, drinking water, and subsidised distribution of food are expected to go up.

Analytical Approach
For arriving at its rating, CRISIL has applied its criteria on rating instruments backed by guarantees. In addition to the state guarantee, the payment mechanism provides for an enhanced liquidity cushion through presence of DSRA and a subsidy-trapping mechanism in case the DSRA is utilised. This liquidity buffer mitigates the risk of delayed payment, if any, from the state government, thereby lowering the risk for the instrument.

Key Rating Drivers & Detailed Description
Strengths:
*** Presence of unconditional and irrevocable guarantee provided by GoUP, trustee-administered escrow and payment mechanism, and adequate liquidity**
The bond issue benefits from the credit enhancement provided by a well-defined T-structured guarantee trigger mechanism, adequate liquidity buffer, and a mechanism to trap the subsidy receipts to replenish the DSRA in case it is utilised.

The primary cash flow to be harnessed for bond servicing will come via escrow of electricity receivables of around Rs 20 crore per day to bond servicing account where fixed deposits will be maintained on a daily basis in such a manner so that the entire servicing required in a quarter are collected by T-15 days; any excess amount will be transferred back to revenue account of UPPCL, thereby providing adequate cover. In the event of a shortfall in primary cash flows, the structure will be backed by the legal recourse to the state government via a trustee-monitored guarantee invocation framework.

In addition, the rating is further supported by the presence of a 2-quarter DSRA as a liquidity cushion, which lowers the risk of any delay in receipt of payment from the state government. In the event of DSRA utilisation, the structure provides for trapping of subsidy receipts (around Rs 10,100 crore for fiscal 2020) that are a steady budgeted monthly inflow from the state and would first be used to top up the DSRA, well before the next payment cycle. The additional liquidity buffer enhances the strength of the payment structure and provides adequate protection from administrative delays. However, utilisation of DSRA, non-promptness in receipt of funds from the state government, or non-compliance with the timelines of the T-structure by the trustee would continue to be key rating sensitivity factors.

*** Large economy base with healthy revenue surplus and own tax buoyancy**
Uttar Pradesh is the third-largest Indian state in terms of gross state domestic product (GSDP) with consistent revenue surpluses for the past 10 years, benefitting primarily due to high share in central tax devolutions and healthy levels of own tax revenue. Because of its large population base, Uttar Pradesh gets the largest share tax devolutions of 17.93% as recommended by the 15th Finance Commission; which is a marginal decrease from the earlier share of 17.96% (recommended by the 14th Finance Commission) and remains a key driver contributing to 35-40% of the overall revenue receipts.

Also, being a consumption-driven state, its revenue is expected to benefit from collections under GST, which witnessed robust growth in fiscal 2019. This led to reduced GST compensation requirement from the Central government. However, for fiscal 2020 (revised estimates), the collections are expected to remained subdued, thereby increasing the need of higher GST compensation. The revenue receipts have grown at a three-year compound annual growth rate of 13.3% between fiscals 2016 and 2019, whereas revenue expenditure rose by 12.3%. The committed expenditure, although elevated at 55% (in fiscal 2019) of revenue expenditure, has been coming down over time. Revenue surplus to revenue receipts ratio is, however, expected to decline to 7.1% (revised estimates) in fiscal 2020 from 8.6% in fiscal 2019, but still remain healthy.

Weaknesses:
*** Weak socio-economic parameters**
Uttar Pradesh has relatively weak demographic and socio-economic positioning with low per capita income. The contribution from the secondary sector has been on a decline, with high dependency on the primary sector. The state also has the fourth-

highest population density and low literacy and urbanisation rates. The low social indices will necessitate considerable outlays by the state for eventual convergence to national average level over a longer term.

*** High indebtedness with moderate economic management**
Total debt plus guarantee to GSDP was 38% in fiscal 2019 compared to 34.6% in fiscal 2018. The increase was mainly due to rise in state guarantees and is expected to remain elevated over the medium term. The gross fiscal deficit (GFD) to GSDP is expected to increase to 2.98% in fiscal 2020 (revised estimates) from 2.3% in fiscal 2019; though will remain within the 3% limit as per Fiscal Responsibility and Budget Management norms. There was no utilisation of ways and means advances (WMA) till February for fiscal 2020.

To help the state manage short-term liquidity, the Reserve Bank of India recently increased the WMA limit to 60% over and above the level as on March 31, 2020 (increase for Uttar Pradesh to Rs 5,680 crore from Rs 3,550 crore), which will be applicable till September 30, 2020. This will help the state to manage its short term liquidity and plan its borrowing programme.

State's power reforms have led to a reduction in aggregate technical & commercial (AT&C) losses over the previous fiscal. However, the initiatives are yet to fully catch up with the targets stipulated in the Ujjwal DISCOM Assurance Yojana (UDAY) memorandum. CRISIL believes the announcement of the industry policy, steps being taken to reform the power sector, and presence of the same government at the Centre and state will aid in synergies and benefit Uttar Pradesh over medium to long term. However, traction in improvements, leverage levels, and continuation of high fiscal deficit will remain key monitorables.

*** Below-average financial performance of UPPCL**
The state's power reforms have lagged as discoms (distribution companies) have not met both the operational and financial targets laid under UDAY. The AT&C losses of 30.09% and gap in average cost of supply and average revenue requirement (ACS-ARR) of Rs 0.08/kilowatt-hour in the nine months of fiscal 2020 are higher than the targets stipulated in the UDAY memorandum.

The company's performance remains weak with net loss of Rs 7,675 crore in fiscal 2019, though lower than the losses of Rs 8,118 crore in fiscal 2018. However, the EBITDA level losses have increased to Rs 595 crore from Rs 237 crore. The company, along with the state government, has undertaken a number of measures, including regular monitoring of progress under UDAY, setting up of bijli thanes to tackle power theft, and focusing on rural electrification and metering; benefits of which are yet to translate into improvement in UPPCL's financial position. The power sector will remain critical for the state government and will be well-supported through increasing subsidies from the state government. Any change in government's stance towards the sector will be a key monitorable.

Liquidity Adequate
Cash and equivalents stood at Rs 1,625 crore as on March 31, 2019. The company's bonds are serviced by discoms' receivables and Rs 20 crore is escrowed each day to service the debt obligation for these rated instruments. Additionally, the bonds' liquidity is supported by DSRA equivalent to two rolling quarters of debt servicing amount (Rs 1,134 crore as on April 6, 2020). Further support from the state government in the form of subsidies and access to finance from non-banking finance companies due to its critical utility role and state government ownership support liquidity.

Outlook: Stable
CRISIL believes UPPCL bonds will continue to benefit from its strong payment structure and support from GoUP in the long term.

Rating Sensitivity factors

Upward factors:
* Sustained improvement in the power sector and reform orientation of the state
* Reduction in indebtedness below 20% of GSDP

Downward factors:
* Steady increase in fiscal deficit beyond 3% of GSDP
* Significant adverse impact on GoUP's fiscal performance over the medium term
* Decline of liquidity buffers or non-adherence to payment structure

Adequacy of credit enhancement structure

The guarantee provided by GoUP is unconditional, irrevocable, and covers the entire rated amount for bonds. A trustee-monitored payment mechanism is in place to ensure timely payment of the interest and principal obligations. UPPCL is adhering to a defined T structure where electricity receivables are escrowed into bond servicing account on a daily basis so as to adequately fund the account by T-15 days prior to the entire debt servicing requirement for that quarter, and additional liquidity cushion in the form of DSRA for two quarters.

Unsupported ratings: CRISIL BB

CRISIL has introduced 'CE' suffix for instruments having explicit Credit Enhancement feature in compliance with SEBI's circular dated June 13, 2019.

Key drivers for unsupported ratings

For arriving at the unsupported rating, CRISIL has considered the business and financial risk profiles of UPPCL. Business risk profile continues to be strong due to monopoly in the power distribution business in the designated service area and its critical role to the state economy. The ACS-ARR gap has reduced post-UDAY while AT&C losses have remained high; though the same has improved over the years. Financial risk profile remains weak due to a highly leveraged capital structure and large losses. Though the risk is mitigated by the presence of financial flexibility and access to banking facilities.

About the Company

UPPCL was formed on January 14, 2000, by unbundling the Uttar Pradesh State Electricity Board into three separate entities: UPPCL, holding the transmission & distribution business; Uttar Pradesh Rajya Vidyut Utpadan Nigam Ltd that houses thermal generation; and Uttar Pradesh Jal Vidyut Nigam Ltd, which holds the hydro generation business The transmission business was subsequently carved out of UPPCL into an independent government company in 2007, Uttar Pradesh Power Transmission Company Ltd.

The five discoms under UPPCL include Dakshinanchal Vidyut Vitran Nigam Ltd (Agra discom), Madhyanchal Vidyut Vitran Nigam Ltd (Lucknow discom), Purvanchal Vidyut Vitran Nigam Ltd (Varanasi discom), Paschimanchal Vidyut Vitran Nigam Ltd (Meerut discom), and Kanpur Electricity Supply Company.

Key Financial Indicators- UPPCL Standalone:

Particulars	Unit	2019*	2018
Revenue	Rs cr	55,327	46,425
Profit after tax	Rs cr	-7,675	-8,118
PAT margin	%	-13.87	-17.48
Adjusted debt/adjusted networth	Times	8.27	12.86
Interest coverage	Times	NM	NM

NM: Not meaningful
**Provisional*

Government of Uttar Pradesh- reported financials:

Particulars	Unit	2019**	2018**
Revenue receipts	Rs cr	3,29,977	2,78,775
Revenue surplus	Rs cr	28,250	12,552
Gross fiscal deficit	Rs cr	35,203	27,810
GFD/GSDP	%	2.3	2.0
Debt^/GSDP	%	38	34.6
RR/Interest	Times	10.3	9.57

^ including guarantees
***Accounts*

List of covenants
Salient features of the bond backed by the State Government guarantee:

- The NCD will have quarterly interest and repayments
- The tenure will be for 10 years repayments commencing from the end of 7th quarter
- Upfront creation of liquidity facility in the form of DSRA for next two-quarter of principal and interest payments (in the form of cash), additional DSRA augmentation within 15 days after end of 5th quarter to take care of enhanced servicing requirements.
- Standing instruction from one collection account (or Designated Receipt Account) of the borrower having an average daily inflow of atleast Rs 10 cr. for daily transfer into the Bond Servicing Account.
- This account will be free from any encumbrance or escrow towards any existing or future lenders or creditors.
- Subsidy received from state government will be deposited in a separate account called Subsidy Receipt Account. This arrangement would be agreed upon with the state government. If DSRA is dipped into, the default escrow on this Subsidy Receipt Account will get activated and all funds received in this account would be trapped and first used to top up the DSRA.

Transaction Structure:
Assuming T is the bond issuance day and T1, T2 and T3 are subsequent bond payment dates, one quarter apart:

Date	Particulars
From T1-90 to T1-15	UPPCL Bond Servicing account to be funded daily. The funds to be transferred in such a manner so that the entire servicing required in a quarter, are collected by T-15 days (i.e. in 75 days)
T1-14	Debenture Trustee will monitor the sufficiency of the balance
T1-14 to T1-10	Trustee will inform GoUP and Rating Agency of any shortfall. This would be a soft call on the guarantee.
T1-9	Trustee will ask GoUP to make good the shortfall as per terms of the guarantee by T-3 day. This will be a stronger call on the guarantee with a notice being sent by Trustee.
T1-2	If shortfall still persist then Trustee will transfer funds from DSRA into the UPPCL Bond Servicing account
T1	Meet the Bond payment
	If DSRA is utilized, it will trigger a default escrow on the Subsidy Receipt Account on next working day, by which the subsidy would start getting trapped till DSRA is not fully replenished.
T1+76 to T1+80 *(or T2-14 to T2-10)*	Trustee will call upon GoUP to make good the entire shortfall i.e towards T1 and T2 payments. This would be a soft call on the guarantee.

T1+81 *(or T2-9)*	Trustee will notify GoUP to make good the shortfall (including the amounts of any previous shortfalls) as per terms of the guarantee by T2-3 day. This will be a stronger call on the guarantee with a notice being sent by Trustee.
T1+88 *(or T2-2)*	If shortfall still persist then Trustee will transfer funds from DSRA into the UPPCL Bond Servicing account
T2	Meet the Bond payment
T2+1	The Trustee will send a final notice to the state government stating its intention to invoke the guarantee within 10 days if the shortfall is not paid.
T2+11	Expiry of notice period, the Trustee will invoke the state guarantee the next day to the extent of meeting the 2 quarter-DSRA shortfall
T3	Meet the Bond payment
After T3	If a payment default happens on T3, then one day after that, there will be an invocation of guarantee calling for acceleration on entire outstanding facility.

Any major change in the salient features or transaction structure in the final documents would be a rating sensitivity factor.

Any other information: Not applicable

Note on complexity levels of the rated instrument:
CRISIL complexity levels are assigned to various types of financial instruments. The CRISIL complexity levels are available on www.crisil.com/complexity-levels. Users are advised to refer to the CRISIL complexity levels for instruments that they consider for investment. Users may also call the Customer Service Helpdesk with queries on specific instruments.

Annexure - Details of Instrument(s)

ISIN	Type of instrument	Date of allotment	Coupon	Maturity date	Issue Size (Rs cr)	Rating Assigned with Outlook
INE540P07194	Bonds	05-12-2017	9.75%	20-10-2020	529.2	CRISIL A+(CE)/Stable
INE540P07202	Bonds	05-12-2017	9.75%	20-10-2021	529.2	CRISIL A+(CE)/Stable
INE540P07210	Bonds	05-12-2017	9.75%	20-10-2022	529.2	CRISIL A+(CE)/Stable
INE540P07228	Bonds	05-12-2017	9.75%	20-10-2023	529.2	CRISIL A+(CE)/Stable
INE540P07236	Bonds	05-12-2017	9.75%	18-10-2024	529.2	CRISIL A+(CE)/Stable
INE540P07244	Bonds	05-12-2017	9.75%	20-10-2025	529.2	CRISIL A+(CE)/Stable
INE540P07251	Bonds	05-12-2017	9.75%	20-10-2026	529.2	CRISIL A+(CE)/Stable
INE540P07269	Bonds	05-12-2017	9.75%	20-10-2027	529.2	CRISIL A+(CE)/Stable
INE540P07285	Bonds	27-03-2018	10.15%	20-01-2021	646.0	CRISIL A+(CE)/Stable
INE540P07293	Bonds	27-03-2018	10.15%	20-01-2022	646.0	CRISIL A+(CE)/Stable
INE540P07301	Bonds	27-03-2018	10.15%	20-01-2023	646.0	CRISIL A+(CE)/Stable
INE540P07319	Bonds	27-03-2018	10.15%	19-01-2024	646.0	CRISIL A+(CE)/Stable
INE540P07327	Bonds	27-03-2018	10.15%	20-01-2025	646.0	CRISIL A+(CE)/Stable
INE540P07335	Bonds	27-03-2018	10.15%	20-01-2026	646.0	CRISIL A+(CE)/Stable
INE540P07343	Bonds	27-03-2018	10.15%	20-01-2027	646.0	CRISIL A+(CE)/Stable
INE540P07350	Bonds	27-03-2018	10.15%	20-01-2028	646.0	CRISIL A+(CE)/Stable
NA^	Bonds	NA	NA	NA	3.8	CRISIL A+(CE)/Stable

Annexure - Details of Instrument(s) withdrawn

ISIN	Type of instrument	Date of allotment	Coupon	Maturity date	Issue Size (Rs cr)
INE540P07186	Bonds	05-12-2017	9.75%	18-10-2019	264.6
INE540P07277	Bonds	27-03-2018	10.15%	20-01-2020	323.0

Annexure - Rating History for last 3 Years

	Current			2020 (History)		2019		2018		2017		Start of 2017
Instrument	Type	Outstanding Amount	Rating	Date	Rating	Date	Rating	Date	Rating	Date	Rating	Rating
Bond	LT	9405.40 30-04-20	CRISIL A+ (CE)/Stable			07-09-19	CRISIL A+ (CE)/Stable	11-04-18	CRISIL A+ (SO)/Stable	29-12-17	CRISIL A+ (SO)/Stable	--
						30-04-19	CRISIL A+ (SO)/Stable	08-03-18	CRISIL A+ (SO)/Stable| Provisional CRISIL A+ (SO)/Stable	24-11-17	Provisional CRISIL A+ (SO)/Stable	

All amounts are in Rs.Cr.

Links to related criteria

CRISILs Approach to Financial Ratios

Criteria for rating instruments backed by guarantees

Rating Criteria for State Governments

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