NDPL

NDPL\ DERC \2010-11

June 17, 2010

Mr. A K Singh,
Director Tariff,
Delhi Electricity Regulatory Commission,
Viniyamak Bhawan,C-Block, Shivalik,
Malviya Nagar,
New Delhi -110 017

Sub: ICRA places NDPL Credit Rating under Rating Watch with Negative Implications. Ref: Report dated 16th June, 2010.

Dear Sir,

With reference your letter NO. F11(57))/DERC/2010-11/2492 dated 28th May, 2010 on liquidity position of the NDPL and further to our reply dated 4th June, 2010, we enclose here with latest report issued by ICRA based on FY 09-10 audited financial statements of the company.

We regret to inform that, as a part of their periodic surveillance audit, the credit rating agency ICRA has placed NDPL's Borrowings under Rating Watch with Negative Implications vide their report of yesterday.

"The rating action factors in a significant build-up of Regulatory Assets, following a substantial increase in power purchase cost over the cost anticipated at the time of the last tariff order and uncertainty in recovery of such costs through appropriate tariff hikes." says the Report.

It further says: "In ICRA's view, an 8-10% tariff hike will be required to enable NDPL to recover the bulk of these Regulatory Assets in next 2 years. The hike required could even be higher if the current tariff is not commensurate in relation to the power procurement cost for FY 2010-11."

Going forward, in ICRA's view, the liquidity position of NDPL would be dependent on the extent to which the Hon'ble Commission allows for the tariff hikes required and the timeline within which such tariff orders are issued.

ICRA's report also mentions about the same concern which has been raised by one of the lead banker of NDPL that company's revenue and profit after tax for the FY 09-10 includes Rs. 672 Cr. as Tariff adjustment account recoverable in future tariff which has impacted the liquidity position and witnessed pressure on cash flow of the company.

The main reasons highlighted by ICRA in their report for placing our rating under watch with negative implications are:

1) Significant build-up of Regulatory Assets recoverable

2) Substantially higher power purchase cost compared to the cost anticipated by the Hon'ble Commission at the time of the last tariff order.

3) Uncertainties on determining whether the tariff order will allow sufficient power tariff hikes to enable the company to recover the Regulatory Assets in a timely manner.

4) Uncertainty in recovery of such Regulatory Assets through appropriate tariff hikes

5) Increase in amount yet to be receivable from future tariff which has mounted to Rs. 1015 Cr. as at 31 March, 2010.

Despite our superlative commercial and operational performance vis a vis the Regulatory targets set for us to achieve, paradoxically the financial health of NDPL has deteriorated due to the Tariff determination issues as also highlighted by ICRA.

ICRA Report further says: "ICRA will finalize the rating once the final tariff order for FY 2010-11 is out and the impact on NDPL's cash flows can be ascertained."

In view thereof, we request you to please take cognizance of this latest ICRA report and their concerns on the liquidity and cash flow position of NDPL at the time of Tariff determination exercise which is underway.

Thanking you
Yours faithfully

For North Delhi Power Limited

Hemant Goyal
(DGM- Finance)

Cc:

Mr. Berjinder Singh,
Chairman, DERC

Mr. Shyam Wadhera,
Member- DERC

Mr. S R Sethi,
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North Delhi Power Limited

Rating History

Instrument	Rating Outstanding	Previous Ratings	
	March 2010	**July 2009**	**March 2008**
Rs. 13.75 billion, term loans programme	LAA@ (Rs. 13.75 billion)	LAA (Rs. 12.20 billion)	LAA- (Rs. 8.62 billion)
Rs. 1.45 billion, fund-based limit	LAA@ (Rs. 1.45 billion)	LAA (Rs. 1.45 billion)	LAA- (Rs. 1.25 billion)
Rs. 3.25 billion non-fund based limit	A1+@ (Rs. 3.25 billion)	A1+ (Rs. 3.25 billion)	A1+ (Rs. 2.4 billion)
Rs. 2.3 billion, commercial paper programme	A1+ @ (Rs. 2.3 billion)	A1+ (Rs. 800 million)	A1+ (Rs. 800 million)

The @ symbol implies that the rating is under rating watch with negative implications

ICRA has placed the long long-term rating of LAA (pronounced L double A) assigned to Rs. 13.75 billion term loans and Rs. 1.45 billion fund-based limits of North Delhi Power Limited (NDPL) under rating watch with negative implications†. ICRA has also placed A1+ (pronounced A one plus) rating assigned to Rs. 3.25 billion, non-fund based limits and the Rs. 2.3 billion, Commercial Paper Programme of NDPL, under rating watch with negative implications†.

The rating action factors in a significant build-up of regulatory assets‡ following a substantial increase in power purchase cost over the cost anticipated at the time of the last tariff order and uncertainty in recovery of such costs through appropriate tariff hikes. This has resulted in some pressure on the company's liquidity as evidenced by increase in power purchase creditors and increase in debt levels for funding the aforesaid receivables. The delays in finalization of the tariff order for FY 2010-11 has added to the uncertainties on determining whether the tariff order will allow sufficient power tariff hikes to enable the company to recover the regulatory assets in a timely manner. In ICRA's view, an 8-10% tariff hike will be required to enable NDPL to recover the bulk of these assets in the next 2 years. The hike required could be even higher, if the current tariff is not commensurate in relation to the power procurement costs for FY 2010-11. ICRA will finalise the ratings once the final tariff order for FY 2010-11 is out and the impact on NDPL's cashflows can be ascertained. While maintaining the rating at the current level, ICRA has taken note of improving efficiency parameters, as reflected in its ability to reduce the aggregate technical and commercial (AT&C) losses to levels well below the target laid down under the current tariff regime and the cost plus nature of the tariff setting process, which will allow eventual recovery of all costs, notwithstanding temporary mismatches. ICRA has also taken note of NDPL's efforts to control purchase costs through a variety of measures including setting up a captive gas-based power plant and signing power purchase agreements (PPAs) with a number of power projects, which are likely to become operational in the medium term and supply power at more reasonable rates. ICRA also draws comfort from its status as a 51% subsidiary of The Tata Power Company Limited (TPCL), which is rated LAA and A1+ with a positive outlook (on long-term rating) by ICRA.

NDPL, which is a 51:49 joint venture (JV) of TPCL and the Government of Delhi (GoD), is engaged in the distribution of power in the Northern and North-Western parts of Delhi. Until FY 2002, the entire business of generation, transmission and distribution of power in Delhi was being carried out by the erstwhile Delhi Vidyut Board (DVB). However, the Delhi government enacted a legislation called the Delhi Electricity Reforms Act (DERA) in FY 2002 to unbundle the DVB into separate companies for carrying out generation, transmission and distribution related activities. As part of the unbundling exercise, the entire state was divided into three regions, namely, Central-East, South-West and North-North-West. It was proposed that the distribution of power in each of these regions would be handled by a separate discom, each of which would be a 51:49 JV of a private player and the GoD. The three distribution regions were then

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

‡ Regulatory assets/ tariff adjustments are representative of the income receivables from future tariff.

offered to private companies for 51% equity participation by way of bids. The condition of the bids was the percentage of ATC loss reduction committed by the bidders. Based on these bids, the Tata group won the North-North West circle and NDPL commenced commercial operations on July 1, 2002. ICRA has taken note of the state government support to the reform process, as evidenced in NDPL starting operations with a relatively clean balance sheet; takeover of unfunded pension liabilities of the DVB employees by GoD and assured transitory support to the transmission company, namely, Delhi Transco Limited (DTL).

Until FY 2009-10, NDPL has reported healthy profitability, as the tariffs of the company were being fixed on a cost plus basis. Since the commencement of commercial operations, NDPL has brought down the AT&C losses to below 15% in the FY 2010 from, which were more than 50% in FY 2003. This has enabled, NDPL to earn its stipulated 16% return on equity but also incentives for over-performance on loss reduction targets, thus boosting its bottom line. However, cost of the power procured by the company during the peak season witnessed significant increase over the last year. Despite the cost plus nature of tariff setting regime, increased reliance on costlier power to meet growing demands coupled with the time lag in the cash recovery of these costs, has resulted in significant pressures on cashflows and increase in the regulatory assets. The increased regulatory assets and ongoing capex (to set up a 108 MW gas-based power plant) in turn exerted pressure on the liquidity position of the company.

The tariff order for the current year is currently pending for release. In ICRA's view, any mismatch in the actual and approved power costs for the current year could lead to further additions in these regulatory assets. On the other hand, ICRA has also taken note of NDPL's efforts to control its power procurement costs by setting up its own gas-based power plant and signing power purchase agreements (PPAs) with upcoming power generation capacities. These capacities, once operational, are expected to provide power at reasonable rates. However, a sizable portion of these capacities is expected to be available only in the latter part of the current year and may also be subjected to implementation delays. In the short-to-medium term, if the tariff rates remain incommensurate in relation to increasing power purchase costs and the recovery of regulatory assets remains unattended, the liquidity of the company would remain affected.

In 2009-10, NDPL reported an operating income (OI) of Rs. 32.77 billion as against an OI of Rs. 24.63 billion in 2008-09. Of the total income of Rs 32.77 billion for the FY 2009-10, around Rs 6.72 billion were in the form of deferred receivables / tariff adjustments§ and has impacted the liquidity position of the company. Over the same period company reported PAT on accrual basis to Rs 3.51 billion in FY 2009-10 from Rs 1.71 billion in FY 2008-09, though its cash accruals (after adjusting for increase in tariff adjustment Rs. 6.72 billion) witnessed pressure. The working capital intensity of the company also witnessed increase from -0.1% in FY 2008-09 to 8.2% in FY 2009-10. This increase was mainly on account of increase in the regulatory assets (reported as a part of debtors) from Rs 10.15 billion as on 31st March 2010 as against Rs 3.22 billion on 31st March 2009. Reflecting the impact of the receivables on the liquidity position, the company's creditors increased to Rs 2693 million in FY 2009-10; as against Rs 1142 million in FY 2008-09.

Going forward, the liquidity position of NDPL would be dependent on the extent to which the regulator allows for the tariff hikes required and the timeline within which the tariff orders are issued. ICRA will finalise the ratings once the final tariff order for FY 2010-11 is out and the impact on NDPL's cash-flows can be ascertained.

June 2010

§ Regulatory assets/ tariff adjustments are representative of the income receivables from future tariff.

Key Financial Indicators

Particulars	31.03.07	31.03.08	31.03.09	31.03.10
Net Sales	19635.38	21879.48	23589.85	32768.53
Operating Income (OI) (Note 1- a)	20251.57	24924.06	24626.55	33925.77
Operating Profit before Depreciation, Interest and Tax (OPBDIT)	5173.04	3688.00	3762.64	4588.25
Profit after Tax	1857.91	2816.02	1714.88	3507.20
Equity Capital	3680.00	3680.00	5520.00	5520.00
Total Debt	7714.45	8015.02	8945.57	14309.20
Tangible Net Worth (Note 1-b)	6736.35	8761.77	9569.44	13078.26
PAT/OI (%)	9.17	11.30	6.96	10.34
Net Working Capital/OI (%)	-10.6%	1.9%	-0.1%	8.2%
PBIT/(Total Debt + Tangible Net Worth) (%)	24.3%	13.2%	15.9%	13.0%
OPBDIT/Interest & Finance Charges (Times)	9.09	4.91	5.04	4.84
Retained Cash Flow) / Total Debt (Times)	0.64	(0.01)	0.30	(0.03)
Total Debt /Tangible Net Worth	1.15	0.91	0.93	1.09
Total Debt/(Tangible Net Worth + Deferred Tax Liability) (Times)	1.01	0.81	0.82	1.09

Amounts in Rs. Million

Note 1: Including Regulatory Asset (subject to recoverable in future tariff) as under:

	31.03.07	31.03.08	31.03.09	31.03.10
a) Regulatory Asset included in Operating Income	(1056.60)	4327.50	40.50	6726.80
b) Cumulative Regulatory Assets	(1143.90)	3183.60	3224.10	10156.30

Source: Audited Financial Results

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