

Essar Power Hazira Limited (Revised)

September 05, 2022

Ratings

Facilities	Amount (Rs. crore)	Rating ¹	Rating Action
Long Term Bank Facilities- Term loan	783.00	CARE A- (CWP); (Single A Minus) (Under Credit Watch with positive implications)	Placed on Credit watch with Positive Implications
Total Facilities	783.00 (Rs. Seven Hundred Eighty-Three Crore Only)		

Details of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

CARE Ratings Ltd. has placed the ratings of Essar Power Hazira Limited (EPHL) on 'Credit watch with Positive implications' following the announcement of signing of a definitive agreement with ArcelorMittal Nippon Steel India Ltd (AMNSL) for sale of certain Ports and Power infrastructure assets which are primarily captive to Hazira steel plant operations for value amounting to USD 2.4 billion (~ Rs.19,000 crore). As a part of the transaction deal, EPHL is also proposed to be sold to AMNSL. EPHL was conceptualized as a captive asset of AMNSL (erstwhile Essar Steel India Limited) as power sourced from EPHL caters to about one-third of power requirement of the steel plant and is one of the cheapest sources of power. The power plant is highly integrated with AMNSL and is strategically important for its seamless functioning. The entity is expected to benefit from the business/financial synergies and linkages with AMNSL post the aforementioned acquisition and change in management control. The transaction is subject to completion of certain corporate and regulatory approvals applicable for respective assets. CARE is monitoring developments with regards to the acquisition and shall review the rating when greater clarity emerges.

The ratings assigned to the bank facilities of Essar Power Hazira Limited (EPHL) takes into consideration strong revenue visibility as entire capacity is tied up with ArcelorMittal Nippon Steel India Limited (AMNSL) as a take or pay arrangement. The rating also factors in operational tie up with AMNSL as entire fuel and water requirement being in the scope of AMNSL, competitive tariff structure, satisfactory operating performance during fiscal FY22 and plant availability factor (PAF) above normative levels, aiding recovery of fixed tariff. Further, the rating also draws comfort from the fact that cash flows of EPHL are ring-fenced, since all the payments (including return to shareholders) are routed through the trust and retention account which is regulated by the lenders of the company.

The above rating strengths are, however, partially offset by limited track record of operations post takeover of steel plant by AMNSL, moderate liquidity and linkages with group companies with instances of inter-corporate deposits (ICDs) extended to the parent company, Essar Power Ltd (EPL).

Rating Sensitivities:

Positive Factors - Factors that could lead to positive rating action/upgrade:

- Sustenance of strong liquidity along with maintaining the stipulated DSRA
- Substantial reduction in debt levels due to prepayment of term loans as a result of acquisition by AMNSL, leading to improvement in overall gearing to 0.5x

Negative Factors- Factors that could lead to negative rating action/downgrade:

- Inability to maintain plant availability consistently above 90%
- Any increase in receivable days significantly beyond 30 days on sustained basis
- Increase in exposure to group companies which could impact the liquidity

Detailed description of the key rating drivers

Key Rating Strengths

Satisfactory operating performance and improved profitability leading to generation of surplus cash flows

EPHL has maintained plant availability in the range of 90-96% since its commissioning. The company reported healthy operating performance during FY22, with plant availability factor (PAF) above normative levels, aiding recovery of fixed tariff. The company has achieved cost reduction in various overheads out of its operational efficiency and it reflects in the improvement in PBILDT level by ~Rs.20crore as well as growth in PBILDT margin by ~ 635bps during FY22. As per PPA, AMNSL

¹Complete definitions of the ratings assigned are available at www.careratings.com and in other CARE publications.

is required to pay the fixed charges for the tied-up capacity on a take or pay basis, subject to declaration of plant availability by EPHL. Since December 2019, AMNSL has been paying the fixed charges on fortnightly basis within the month. The company is generating monthly surplus cash exceeding ~R.8crore, post servicing of monthly interest payment and quarterly principal repayment.

Firm offtake arrangement with strong off-taker exhibiting revenue visibility, competitive tariff structure and regulatory benefits

AMNSL is a joint venture between Arcelor Mittal and Nippon Steel, two of the world's leading steel companies. The joint venture company acquired the stressed assets of erstwhile Essar Steel India Limited in December 2019 and has turned it around since then. EPHL has long term power purchase agreement (PPA) with AMNSL for 270MW at a fixed tariff of Rs.416crore per annum and it has the sole right to extend or terminate the contract. In July 2020, EPHL extended the PPA till Nov 2041. EPHL has executed an agreement for additional capacity of 30 MW at a tariff of Rs.1.125 per unit. As the fuels used by EPHL are the waste products generated from the steel plant with limited market value, the cost of power for AMNSL remains highly competitive at Rs.1.95 per unit as against other sources of power. EPHL enables AMNSL to earn Group captive benefits on account of no cross-subsidy charge and lower electricity duty. In turn, the presence of combination of long-term and short-term off-take arrangements provides EPHL with healthy revenue visibility.

In case of default in payment by AMNSL, only EPHL has the right to terminate the PPA. EPHL has the right to ask AMNSL to step-in and take over the project and pay a maximum of the outstanding debt of EPHL or the fair value of the project, whichever is higher.

Operational integration with AMNSL with entire fuel & water supply in the scope of the off-taker

The company primarily uses waste products generated by AMNSL steel plant as fuel. In case AMNSL fails to supply fuel and water for the operation of EPHL resulting in failure of the latter to supply power, then it will be considered as an event of AMNSL default and EPHL will be entitled to fixed charges as per PPA. CARE draws comfort from the operational integration of EPHL with AMNSL in form of fuel and water supply to EPHL free of cost, and complete offtake of electricity generated by EPHL. Waste generated by EPHL in the power generation process is also handed back to AMNSL who is responsible for disposal of the same.

Key Rating Weakness

Limited track record of operations post takeover of steel plant by AMNSL

The track record of operations post acquisition of Essar Steel India Limited (ESIL) by AMNSL is limited. Receivables are being collected on timely basis by EPHL since 2017-18, barring Rs.126crore which were admitted in ESIL's NCLT process in August 2017. EPHL has received ~20.50% of the admitted claim and has written off the balance admitted claim. While EPHL faced irregularities in payment from ESIL, the payment from AMNSL has remained timely since the acquisition of the steel plant in December 2019 by AMNSL.

Moderate debt coverage indicators and financial risk profile

The financial risk profile was moderate with interest coverage ratio at 4.0 times (PY:3.2 times) and total debt to PBILDT ratio at 2.1 times for FY22 (PY:2.7 times). The management expects prepayment of the entire loan by the year end FY23 post the completion of acquisition by AMNSL.

Liquidity: Adequate

The liquidity is adequate with cash and cash equivalent of Rs.68crore and DSRA of Rs.53crore as on September 01, 2022 along with timely payment of fixed capacity charges by AMNSL. It reported cash accruals of Rs. 252crore in FY22. The company doesn't have any working capital lines. However, the lenders have permitted utilisation of DSRA as floating DSRA. There are no capital expenditure plans in the near future.

Analytical approach: Standalone

Applicable Criteria

[Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings](#)

[CARE's Policy on Default Recognition](#)

[Rating Methodology - Infrastructure Sector Ratings](#)

[Financial ratios – Non-Financial Sector](#)

[Liquidity Analysis of Non-Financial Sector Entities](#)

[Rating Methodology – Thermal Power Producers](#)

About the Company

Essar Power Hazira Limited had set up a 300 MW captive power plant in Hazira, Gujarat, at a project cost of Rs.2154crore. The company is part of the Essar group that has a diversified presence across the core sectors. Entire shareholding of EPHL held by Essar Power Limited (EPL)- 74% equity and 100% CCPS, shall be sold to AMNSL as part of the acquisition of EPHL by AMNSL.

Post-sale, entire equity and CCPS shall be held by AMNSL. EPHL utilizes waste gases and solid waste products generated from AMNSL's steel plant, thereby, improving its carbon footprints while AMNSL disposes off the wastes from EPHL. EPHL act as a balancing power plant for AMNSL by enabling it to avoid any grid disturbance and subsequent penalties.

Brief Financials (₹ crore)	FY21 (A)	FY22 (A)	Q1FY23(UA)
Total operating income	427.03	417.95	NA
PBILDT	327.23	346.83	NA
PAT	128.67	160.10	NA
Overall gearing (times)	1.12	0.76	NA
Interest coverage (times)	3.19	3.99	NA

A: Audited; UA-Un-audited; NA: not available

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

Covenants of rated instrument / facility: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of various instruments rated for this company: Annexure 4

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based-Long Term		-	-	October 2026	783.00	CARE A- (CWP)

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021	Date(s) and Rating(s) assigned in 2019-2020
1	Fund-based-Long Term	LT	783.00	CARE A- (CWP)	-	1)CARE A-; Stable (03-Nov-21)	-	-

*Long term/ short term

Annexure-3: Detailed explanation of covenants of the rated facilities-

- Debt to equity ratio not exceeding 71:29
- DSCR to be at least 1.15

Annexure 4: Complexity level of various instruments rated for this Company

Sr. No.	Name of Instrument	Complexity Level
1	Fund-based-Long Term	Simple

Annexure 5: Bank Lender Details

To view the lender wise details of bank facilities please [click here](#)

Note on complexity levels of the rated instrument: CARE has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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About CARE Ratings Limited:

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With an established track record of rating companies over almost three decades, we follow a robust and transparent rating process that leverages our domain and analytical expertise backed by the methodologies congruent with the international best practices. CARE Ratings Limited has had a pivotal role to play in developing bank debt and capital market instruments including CPs, corporate bonds and debentures, and structured credit.

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