

Press Release

Meghalaya Energy Corporation Limited

January 17, 2023



Rating Assigned

Product	Quantum (Rs. Cr)	Long Term Rating	Short Term Rating
BOND	630.00	ACUITE A- CE Stable Assigned	-
Total Outstanding Quantum (Rs. Cr)	630.00	-	-
Total Withdrawn Quantum (Rs. Cr)	0.00	-	-

Rating Rationale

Acuite has assigned the long-term rating of **ACUITE A- (CE) (read as ACUITE A minus (Credit Enhancement))** on the existing bonds of Rs.389.30 Cr and the proposed bonds of Rs.240.70 Cr of Meghalaya Energy Corporation Limited. The outlook is 'Stable'.

Rationale for the rating

The rating takes into cognizance an unconditional and irrevocable guarantee by the Government of Meghalaya (GoMe) backed up by a structured payment mechanism, thereby ensuring timely debt servicing for both the existing and proposed bonds issue (rated instrument). Acuite also derives comfort from the stable fiscal position of the Government of Meghalaya, which is expected to provide timely funding support to MeECL, as and when necessary. Further, the rating takes into account a gradual improvement in the business position of the entity coupled with a cost plus based tariff mechanism. These strengths are partly offset by the below average financial risk profile of the company and the inherently regulated nature of operations in the electricity business. Acuite has also noted the weak liquidity position of MeECL on a consolidated basis which is reflected in the ongoing challenges faced by its subsidiaries to service outstanding non-guaranteed debt from financial institutions.

About the Company

The Meghalaya Energy Corporation Ltd. (MeECL) is a Government Company, wholly owned by the Government of Meghalaya, incorporated in the year 2009 and inherited its business from the erstwhile Meghalaya State Electricity Board (MeSEB) in the year 2010. It has wholly owned three subsidiary Companies namely, Meghalaya Power Generation Corporation Ltd. (MePGCL), Meghalaya Power Transmission Corporation Ltd. (MePTCL) and Meghalaya Power Distribution Corporation Ltd. (MePDCL) responsible for Generation, Transmission and Distribution of Electricity respectively throughout the State as State Utilities.

Standalone (Unsupported) Rating

ACUITE C

Analytical Approach

To arrive at the rating, Acuite has considered the consolidated business and financial risk

profile of MeECL with its wholly owned subsidiaries namely, Meghalaya Power Generation Corporation Ltd. (MePGCL), Meghalaya Power Transmission Corporation Ltd. (MePTCL) and Meghalaya Power Distribution Corporation Ltd. (MePDCL) and notched up the rating by factoring in the Credit Enhancement available in the form of guarantee extended by the Government of Meghalaya which is embedded within a well defined Structured Payment Mechanism.

Extent of Consolidation - Full

Key Rating Drivers

Strengths

Support from the government of Meghalaya

MeECL is a wholly-owned undertaking of the GoMe and a strategically important entity of the power sector infrastructure for the state of Meghalaya. The ownership structure provides adequate financial flexibility. It is also the nodal agency of the government for undertaking power generation, transmission and distribution activity in the state. Being the power generation, transmission and distribution licensee by MSERC, MeECL is mandated to ensure the generation of power from its installed capacity and for undertaking Rural Electrification (RE) task in the state with the objective of providing access of electricity to all rural households in line with the National Rural Electrification Policy. MeECL's credit profile is also supported by its access to funds at low cost and its ability to mobilise financial resources from several financial institutions and multilateral development institutions. The rating factors in the financial flexibility of MeECL.

Acuité believes that MeECL, being a 100 per cent undertaking of GoMe, shall continue to benefit from the financial, operational and management support as and when required. The GoMe has demonstrated financial support by way of loans and grants to MeECL on a regular basis. Any changes in the ownership pattern of MeECL or any event that impinges GoMe's overall credit profile shall remain a key rating sensitivity.

Unconditional and irrevocable guarantee backed by a structured payment mechanism

The existing listed bonds and proposed bonds of Rs. 630.00 Cr has an unconditional and irrevocable guarantee from the GoMe. The guarantee also has a 'T-7' structure payment mechanism to ensure the timely debt servicing of the debt issue and redemption. MeECL has to maintain a DSRA of two quarters throughout the tenure of the issue and a bond redemption reserve account. As on 31 March 2022 (Provisional), the DSRA balance amounted to Rs. 11.41 Cr, and the balance in the bond redemption reserve account was Rs. 77.73 Cr for the issued bonds of Rs. 389.30 Cr.

The structured payment mechanism, as enshrined in the trust deed, to ensure that the following timelines are followed with 'T' as the due date for payment:

The company shall, remit the Bond Payment Amounts to the Bond Servicing Account, such that the Bond Servicing Account is fully funded to the extent of the amounts due on the subsequent Due Date falling at the end of such Payment Period ("Due Amount") no later than 15 (fifteen) days prior to such relevant Due Date (as defined in the Debenture Trust Deed)) **(T-15 days)** ("Funding Date").

The Account Bank shall independently monitor the adequacy of credit in the Bond Servicing Account. In the event the company has not funded the Bond Servicing Account to the extent of the Due Amount, above on or prior to any Funding Date, the Account Bank shall intimate the same to the Debenture Trustee on the day falling 14 days prior to the relevant Due Date **(T-14 days)** and the Debenture Trustee shall on receipt of such intimation issue a notice to the company and GoMe in writing in the form set out in Schedule II ("Shortfall Intimation Notice") on the day falling 12 days prior to the relevant Due Date **(T-12 days)** ("Shortfall Demand Date") to fund the Bond Servicing Account such that it is funded for no less than the Due Amount no later than 10 days prior to each Due Date **(T-10 days)**

("Shortfall Payment Date"). The GoMe irrevocably and unconditionally undertakes to fund the Bond Servicing Account.

Upon failure of the Government of Meghalaya (GoMe) and the company to ensure that the Due Amount is collected and/or funded in the Bond Servicing Account on or prior to each Shortfall Payment Date, the Debenture Trustee shall call upon the Guarantee given by the GoMe in terms of this Deed by issuing the Demand Notice on the day falling immediately after the relevant Shortfall Payment Date **(T-9 days)** requiring the GoMe to make good the shortfall in the Bond Servicing Account by such amounts such that the Bond Servicing Account is funded for no less than the Due Amount no later than 7 (seven) days prior to each Due Date **(T-7 day)** ("Final Funding Date").

'Cost plus' tariff mechanism

The billing of MeECL are regulated and required the Annual Revenue Requirement (ARR) under 'cost-plus' based tariff mechanism. The regulator, Meghalaya State Electricity Regulatory Commission (MSERC) allows a post-tax return on equity of 15 per cent and other uncontrollable expenses are allowed to be passed through in tariff through Annual Performance Review (APR) process. Acuité derives comfort from the cost plus based tariff mechanism.

Weaknesses

Challenges in servicing non-guaranteed debt in subsidiaries

Acuité has noted that there have been delays by MeECL's subsidiaries in servicing debt obligations to Power Finance Corporation (PFC) and Rural Electrification Corporation Limited (REC), which are not guaranteed by the GoMe. Acuité has hence constrained the unsupported rating of the entity and believes that timely servicing of their debt obligations would be a key monitorable. The liquidity position of consolidated MeECL will continue to remain a point of concern.

However, Acuité derives comfort from the continuous support provided by the Government of Meghalaya (GoMe) and unconditional and irrevocable guarantee given by GoMe along with a structured payment mechanism for the bonds of Rs.630 Cr.

Weak financial risk profile

The company's weak financial risk profile is marked by reducing networth. The tangible net worth of the company has been eroded due to continuous accumulated losses. The networth stood at negative Rs.1636.34 Cr as on March 31, 2022 (Provisional). Any significant improvement in the financial position of MeECL is unlikely in the near to medium term.

Regulated nature of operations

MeECL continues to be exposed to regulatory uncertainty, given that the revenues are influenced by the regulatory framework governing the power sector. The company operates through a cost-plus return on equity model laid down by MSERC. Any change/ reduction in return on equity or a tightening of the MSERC norms could result in lower operating cash flows. Acuité believes that the delay in finalisation of the tariff could result in cash flow mismatch in the medium term.

Assessment of Adequacy of Credit Enhancement

The structure provides for adequate covenants to safeguard the interest of the investors and has adequate buffers and triggers available to initiate timely corrective action and effectively mitigate the risk arising out of any funding gap in MeECL.

ESG Factors Relevant for Rating

Not Applicable

Rating Sensitivities

- Timely support from the Government of Meghalaya
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- Periodical tariff revision
- Improvement in financial risk profile
- Any deterioration in liquidity position

Material covenants

None

Liquidity Position: Stretched

The company's liquidity is stretched on account of accumulated losses driven by weak operating efficiencies and lack of adequate tariff revision. There are delays in servicing of non-guaranteed debt, borrowed from PFC and REC in the subsidiaries. The current ratio stood below unity at 0.30 times as on March 31, 2022 (Provisional), on account of high other current liabilities due to deferred revenue, security deposits, retention money, liabilities for capital supplies and interest accrued.

However, the state government of Meghalaya has given unconditional and irrevocable guarantee for the bonds of Rs.630 Cr and in addition to this, GoMe has given guarantee to some loans borrowed from PFC and REC; which provides financial flexibility to the company. Further, MeECL has unencumbered bank deposits of Rs.159.96 Cr, investment for bond redemption reserve of Rs. 77.73 Cr and cash and bank balances of Rs.86.04 Cr as on March 31, 2022 (Provisional).

Acuité believes that going forward the liquidity position of the company will improve backed by the gradually improving business risk profile with continuously enhancing generation capacity and declining AT&C losses.

Outlook: Stable

Acuité believes that the company will maintain 'Stable' outlook over the medium term due to an improvement in its operational parameters including AT&C losses. The outlook may be revised to 'Positive' in case of an improvement in its liquidity profile and an adequate revision in tariffs which will translate into higher revenues and sustenance in the profitability margins. Conversely, the outlook may be revised to 'Negative' in case of any significant deterioration in its leverage and liquidity position.

Other Factors affecting Rating

None

Key Financials

Particulars	Unit	FY 22 (Provisional)	FY 21 (Actual)
Operating Income	Rs. Cr.	1134.02	1159.14
PAT	Rs. Cr.	(518.24)	(442.99)
PAT Margin	(%)	(45.70)	(38.22)
Total Debt/Tangible Net Worth	Times	(1.99)	(2.54)
PBDIT/Interest	Times	(0.12)	(0.05)

Status of non-cooperation with previous CRA (if applicable)

None

Any other information

None

Applicable Criteria

- Default Recognition :- <https://www.acuite.in/view-rating-criteria-52.htm>
- Service Sector: <https://www.acuite.in/view-rating-criteria-50.htm>
- Application Of Financial Ratios And Adjustments: <https://www.acuite.in/view-rating-criteria-53.htm>
- Consolidation Of Companies: <https://www.acuite.in/view-rating-criteria-60.htm>
- Group And Parent Support: <https://www.acuite.in/view-rating-criteria-47.htm>
- Explicit Credit Enhancements: <https://www.acuite.in/view-rating-criteria-49.htm>

Note on complexity levels of the rated instrument

In order to inform the investors about complexity of instruments, Acuité has categorized such instruments in three levels: Simple, Complex and Highly Complex. Acuite' s categorisation of the instruments across the three categories is based on factors like variability of the returns to the investors, uncertainty in cash flow patterns, number of counterparties and general understanding of the instrument by the market. It has to be understood that complexity is different from credit risk and even an instrument categorized as 'Simple' can carry high levels of risk. For more details, please refer Rating Criteria "Complexity Level Of Financial Instruments" on www.acuite.in.

Rating History:

Not Applicable

Annexure - Details of instruments rated

Lender's Name	ISIN	Facilities	Date Of Issuance	Coupon Rate	Maturity Date	Complexity Level	Quantum (Rs. Cr.)	Rating
Not Applicable	INE760I07011	Bond	11 Jun 2019	11.64	10 Jun 2029	Simple	40.30	ACUITE A- CE Stable Assigned
Not Applicable	INE760I07029	Bond	28 Aug 2019	11.45	27 Aug 2029	Simple	50.00	ACUITE A- CE Stable Assigned
Not Applicable	INE760I07037	Bond	14 Feb 2020	11.45	13 Feb 2030	Simple	100.00	ACUITE A- CE Stable Assigned
Not Applicable	INE760I07045	Bond	21 Dec 2020	11.01	20 Dec 2030	Simple	50.00	ACUITE A- CE Stable Assigned
Not Applicable	INE760I07052	Bond	11 Jan 2021	11.01	10 Jan 2031	Simple	50.00	ACUITE A- CE Stable Assigned
Not Applicable	INE760I07078	Bond	18 Feb 2021	10.96	17 Feb 2031	Simple	49.00	ACUITE A- CE Stable Assigned
Not Applicable	INE760I07060	Bond	15 Jan 2021	11.01	14 Jan 2031	Simple	50.00	ACUITE A- CE Stable Assigned
Not Applicable	Not Applicable	Proposed Bond	Not Applicable	Not Applicable	Not Applicable	Simple	240.70	ACUITE A- CE Stable Assigned

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About Acuité Ratings & Research

Acuité is a full-service Credit Rating Agency registered with the Securities & Exchange Board of India (SEBI). The company received RBI Accreditation as an External Credit Assessment Institution (ECAI) for Bank Loan Ratings under BASEL-II norms in the year 2012. Acuité has assigned ratings to various securities, debt instruments and bank facilities of entities spread across the country and across a wide cross section of industries. It has its Registered and Head Office in Kanjurmarg, Mumbai.

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