HC stay order on renewable tariffs renegotiation in AP, a welcome relief

Rs. 9,000 Cr of project debt at potential risk if state government implements its proposals

Acuité Ratings believes that the recent stay granted by the Andhra Pradesh high court on the state government's move to renegotiate tariffs for renewable energy projects is a relief for the investors and lenders in the sector. An analysis undertaken by Acuité indicates that a debt exposure of around Rs. 9,000 Cr will be at potential risk if the state goes ahead with its proposal and cuts tariffs on operational projects to bring it to current auction levels. Further, it will not only impact the investment pipeline of Rs. 60,000 Cr in renewable projects in the state over the next 3-5 years, but also will send a wrong signal to the investor community regarding the sustainability of renewable projects in India. This along with increasing receivables from the distribution companies can lead to funding challenges in the renewable energy sector, a key focus area of the Central Government. The latter had put a target of 175 GW of renewable energy capacity in the country by 2022.

An analysis undertaken by Acuité Ratings on publicly available data indicates that around 2.1 GW of renewable capacity (or 27 per cent of the currently installed capacity) in Andhra Pradesh (AP) has tariffs exceeding Rs. 3.5 per unit and where the state proposes to renegotiate tariffs to Rs.2.4 per unit, the same as the current auction levels. This will not only bring down the revenues upto 40 per cent for these projects, but also make their operations and debt levels unsustainable.

The stay order on the AP government's proposal to renegotiate the PPAs along with the renewable energy tariffs is expected to address the near term concerns of the developers, investors and lenders in the sector. However, they would keenly await the court's final verdict on this matter. Any validation of the state government's proposal will set a precedent for other state utilities, thereby opening up the entire sector to tariffs revision and PPA renegotiation risks. Over and above the move by the AP government, there have been recent instances wherein the states have tried to renegotiate the tariffs subsequent to the completion of the auction. This not only weakens the entire bidding process, but also leads to lower private sector confidence, causing tenders to be undersubscribed or cancelled.

On July 1, 2019, the newly-elected state government of Andhra Pradesh reportedly ordered review of power purchase agreements (PPAs) signed by the state discoms for purchase of wind and solar power in the state. According to the order, the state government has established a High-Level Negotiation Committee (HLNC) panel to review and renegotiate the PPAs. The state government's point of contention has been the issue of high priced PPAs entered in the last few years and the state discoms facing huge power purchase dues leading them to financial distress. Subsequent to the directive, several renewable power producers challenged the Andhra Pradesh government's move to renegotiate PPAs by filing a petition in the Andhra Pradesh high court. Following the petitions filed by Indian Wind Power Association and individual project developers, the Andhra Pradesh high court stayed the state's move to cut tariffs until August 22.

Andhra Pradesh has significant potential to attract renewable energy investments, given the intensity of its solar irradiation and the availability of high quality wind power sites. It is estimated that, as on June 2019, Andhra Pradesh had 7.9 GW of grid based aggregate renewable capacity with wind sources accounting for 52 per cent (4.1 GW), solar at 42 per cent (3.3 GW) and biomass contributing the balance. A significant part of the above capacity has been commissioned over the last 3 years (2016-19) and Acuité estimates that the gross investment made in the renewable sector during this period amounts to Rs. 30,000 Cr (5GW), out of which a part is currently under implementation. The installed renewable capacity in AP comprises of around 10 per cent of the total such capacity in India. With a near term target of another 10 GW renewable capacity by 2021-22, the state's share at the national level is expected to increase further. This would entail an additional investment of Rs. 60,000 Cr over the next 3-4 years.

India has made significant gains in terms of installed renewable energy capacity having the fourth highest installed wind power capacity and the fifth largest solar capacity at the end of 2018. With replacement of carbon-based fuels with green energy, a significant agenda for the current government, ambitious targets had been put in place for solar as well as wind energy capacity. Several steps have been taken by the government in this regard to support the renewable sector, which include providing fiscal and promotional incentives such as capital subsidy, accelerated depreciation, waiver of Inter State Transmission System (ISTS) charges and losses, viability gap funding (VGF), green energy corridor projects for effective evacuation of power generated through renewable sources and its grid integration and permitting Foreign Direct Investment (FDI) up to 100 per cent under the automatic route. Further, to ensure cost competitiveness renewable energy projects are awarded through transparent bidding process (e- reverse auction).

FDI in the country's renewable energy sector has accordingly seen a sustained rise over the past few years with 2017-18 witnessing a sharp jump of 54 per cent y-o-y to USD $1.2 billion from USD $0.8 billion in 2016-17. In fact, during 2018-19 too, investment into the sector through the FDI route continued and rose to USD $1.4 billion, albeit at a lower growth rate of 20 per cent y-o-y. Cumulatively, foreign investors have infused USD $7.8 billion from FY2001 till FY2019 in the sector. Thus, it broadly reflects the confidence of investors into the country's growing renewable energy sector and also the thrust provided by the government's various policies. The key foreign investors in India's renewable sector include names such as Softbank, Abu Dhabi Investment Authority (ADIA) and GIC Singapore.

Around 45 per cent (~36 GW) of India's renewable capacity is based on wind energy followed by solar energy, which constitutes about 37 per cent (~29 GW) of the capacity, with the other sources making up the remaining. This displays the extent of importance to which the wind and solar sectors play in India's renewable energy basket. In fact, over the last few years there has been a significant increase in the percentage contribution of renewable energy to total installed capacity, having increased from 15 per cent as on March 2016 to 22 per cent as on March 2019. During 2019-20, around 30 GW of solar energy and 10 GW of fresh wind energy projects are expected to be put up for tender.

However, lately there has been a slowdown in capacity additions; to put things into perspective, the solar sector saw a dip in capacity additions during 2018-19 as the issues pertaining to GST, safeguard duty imposition on imports of solar modules and frequent tender cancellations impacted the sector. Similarly, wind sector which has been trying to align to the tariff-based competitive bidding (TBCB) model from the earlier feed-in tariffs (FiTs) has been unable to pick up since 2016-17 when it had added 5.5 GW. Moreover, issues such as land acquisition, tariff caps and tepid power demand growth have further led to a slowdown in capacity addition.

The stay provided by the high court of Andhra Pradesh on state government's tariff renegotiation proposal is expected to provide some assurance to investors and lenders in the short term at this critical juncture for the sector. Acuité will continue to monitor further developments in this regard. The burden of increased receivables from the power distribution companies in AP and other states also needs to be addressed to improve the investment climate in the renewable sector. Clearly, investor confidence in the regulatory and the legal framework would be the key for a sustainable growth of the sector as envisaged by the government.

About Acuité Ratings & Research Limited:
Acuité Ratings & Research Limited *(Erstwhile SMERA Ratings Limited)* is a full-service Credit Rating Agency registered with the Securities and 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. Since then, it has assigned more than 6000 credit 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 Mumbai.

Media Contact:

Suman Chowdhury President – Ratings Ph: + 91-9930831560 suman.chowdhury@acuite.in	Karan Mehrishi Lead Economist Ph: + 91-9910810569 karan.mehrishi@acuite.in

Disclaimer: *This release is sent to you for the sole purpose of dissemination through your newspaper / magazine / media / website / agency. The release may be used by you in full or in part without changing the meaning or context thereof but with due credit to Acuité. However, only Acuité has the sole right of distribution of its releases through any media. Acuité has taken due care and caution for writing this release. Information has been obtained by Acuité from sources which it considers reliable. However, Acuité does not guarantee the accuracy, adequacy or completeness of information on which this release is based. Acuité is not responsible for any errors or omissions or for the results obtained from the use of this release. Acuité has no liability whatsoever to the users / distributors of this release.*