"TATA Power Analyst Conference Call to Discuss the Supreme Court Order for CGPL"

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MAIN SPEAKERS: **MR. ANIL SARDANA – MD AND CEO, TATA POWER CO. LTD.**
MR. RAMESH SUBRAMANYAM – CFO, TATA POWER CO. LTD.

Moderator: Ladies and Gentlemen, good day and welcome to the TATA Power Analyst Conference Call to discuss the Supreme Court order for CGPL. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' and then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Anil Sardana, MD and CEO, TATA Power. Thank you and over to you, Sir.

Anil Sardana: Thank you and good afternoon. Welcome to this call on specific subject of the recent verdict that we got on the compensatory tariff issue for CGPL. We will be happy to take your questions, of course most of the stuff is in public domain, but yet it is always be nice to engage with you, so most welcome to ask your questions.

Moderator: Thank you very much. Ladies and Gentlemen, we will now begin with the question and answer session. The first question is from the line of Bhavin Vithlani from Axis Capital. Please go ahead.

Bhavin Vithlani: My question in one of the sections of the judgment, what we see is that the CERC has the power to adjudicate for the competitively bid tariff and they are referring to the section 71, so does this mean that now CERC is free to give us a CT on the basis of hardship as we had given before and if yes, what is the modus operandi from here on?

Anil Sardana: Thank you Bhavin for raising that point. We are at this stage conferring with the senior legal experts to have a better understanding of what it means in our case. While you are right, there is no doubt that the Supreme Court order has certainly upheld the fact that the regulators have powers under 79(1)B for matters and cases which are even without under section 63. They have even said that these are for such matters where there are no clear guidelines and considering the fact that, imported coal has no clear guidelines. There could be an interpretation to say that applies. However, whether the older order applies or the matter has to be seen fresh, we are working with senior experts to form a clear view, what are our possible options in the days ahead.

Bhavin Vithlani: In this case, do you approach the Supreme Court to see the clarification whether they actually meant it in the way that we are interpreting or you approach the CERC who in turn approaches the Supreme Court for clarification?

Anil Sardana: Bhavin you are right, that is exactly what I meant by saying that we are consulting the senior legal experts because it is for them to advise us on what could be the possible options, and what could be the right options.

Bhavin Vithlani: With this judgment, are you actually changing any of your growth plans or would the entire growth plans that you had envisaged earlier goes on as normally expected?

Anil Sardana: Bhavin, there are two-three things which are very important related to this order. Number one, we had always mentioned that we are not taking compensatory tariff in to our account and to that extent, therefore, it does not disturb our financials nor does it change any outlook. All the plans that we had made and presented in the past, all had this assumption that this tariff order is not yet applicable, so nothing changes as far as way forward is concerned, of course, company will become more conscious in terms of conserving cash just in case it has to continue to support the Mundra going forward.

Bhavin Vithlani: One last question, when I look at the third quarter numbers where we saw an under recovery of 70 paisa, we also understand there is always a lead lag in terms of pass through of the imported coal prices because the changes happens once in six months, also there was some under recovery on the fixed charges because of the availability, so what is the number of the under recovery if we were to assume business as usual which is the lag impact in terms of pass through was ironed out and the lag impact in terms of pass through of the under recovery and fixed charges were ironed out?

Anil Sardana: Bhavin you rightly stated a lot of factors determined quarterly under recovery and also the fact that when we report under recovery it is not netted with the fixed cost, that is based on the result that we finally declare in terms of how much is the impact because of the net overall impact of under recovery as there will be a positive on the fixed cost and there will be under recovery on the fuel cost, but just to give you an idea that at the present coal prices and the present dollar exchange rate which exists, the under recovery factor on an annualized basis will be anywhere between 55 to 60 paisa only on account of fuel cost.

Moderator: Thank you. We have the next question from the line of Hamsini Karthik from Smart Investor. Please go ahead.

Hamsini Karthik: As we discussed much of the facts are in front of us, I just like to understand is there any internal measures that you would be looking at to ensure higher recoveries from CGPL given that the verdict stands as where it is, is there a possibility of replacing foreign coal with domestic coal or something like that to improve the profitability there?

Anil Sardana: Hamsini, the options certainly will include some of the factors that you mentioned. We will certainly look at all options first and foremost to see how under recovery factor reduces. After the APTEL order, if you recall they had said only Indonesian coal will be subjected to compensatory force majeure concept, we had therefore, stopped sourcing coal from various options that we were earlier pursuing in terms of distress coals from US, Colombia, Africa, so one, is that we will start looking at all of those options, number two, we will also look at options where we can have a long term sourcing of coal without transfer pricing mechanism coming into play, so there are countries which are not part of this arrangement that we sort of assume is there between Australia, South Africa and Indonesia, therefore, we could go to those countries and do a long term sourcing on a cost plus basis, which would mean that our under recovery will again get contained. We will also look at the options of what you said, swapping it partly with domestic coal from inter-regions so that we can use all three routes to bring coal to Mundra jetty. All of those options will now be pursued. It is certainly a part and parcel of our effort that we are trying to do, so there is no doubt one will work on all this concept.

Hamsini Karthik: Good, Sir, another question, six months back when the Welspun acquisition was getting laid out, we had also intended our increased exposure in renewable energy, where does that stand today, how much is the commitment today as against what it was about six-eight months back given that today the requirement to conserve cash is perhaps a little higher than what was earlier?

Anil Sardana: Very good point, I guess we have always repeated that we are looking at all options to ensure that we monetize the non-core assets, so that the situation that you very aptly described gets controlled and contained, so that effort is now moving at much faster pace and we will share with you sooner that we sort of close some of those options, so certainly yes, what you said is right, there is all-out effort to make sure that there is all the option of cash that lying in various portfolios or various areas is encashed and we monetize that and bring it back into the mainstream.

Hamsini Karthik: Sir, just to understand if you could throw some color on what you consider as non-core at the moment?

Anil Sardana: The non-core very clearly has been described as these are Telecom assets that we have had. These are also crossholdings that we hold in different TATA companies, all those are non-core and they certainly can fetch us good value.

Hamsini Karthik: Just one last question, Sir, until now you have been a little reluctant if I can put it that way in participating in coal mine bids, would you look at it from a fresh perspective now and about a year or so back about six to 12 months back, you were also open to acquiring good coal set plans which were backed by strong PPAs, does that agenda continue given that you have had too much or we have seen prolonged period of dispute with respect to coal set plans for TATA power?

Anil Sardana: On the coal mines, let me divide that issue in two parts, domestic as well as international. In the domestic, our stand in terms of the fact was, that the way the entire process was is not going to yield practical aspects of fetching the mines and then developing them, I think our stand today when we look at in retrospect gets vindicated because you have not seen much progress on ground, and therefore, we will continue to watch that phase and see as to what way it pans out and what way it gets developed in days ahead. As far as international mines are concerned, we will certainly look at all possibilities whether through investment route or otherwise if there are possibilities other than these three countries that I described in the first answer, which are part of an arrangement where every month they come back with the similar price of coal, so therefore, countries which can offer a recuse from transfer pricing concept, it can allow us a cost plus regime either on a long-term basis or through investment basis, we will certainly be very open to do that because that can reduce our under recovery to a significant extent.

Hamsini Karthik: The last point on how open you would be to acquire any of the thermal power projects which are under stress at the moment, is that still in your radar or you would like to keep away from that?

Anil Sardana: Hamsini, it is certainly in our radar, we had announced a platform if you recall where we are now fully, yes, ICICI and three other partners and that is fully sort of in place and we are moving ahead with those options in terms of search of plants where we could turn them around and we have the possibility of truly gainfully putting them to use, so that effort is certainly on.

Moderator: Thank you. We have the next question from the line of Pulkit Patni from Goldman Sachs. Please go ahead.

Pulkit Patni: Sir, my first question is I understand there is some extra land that we have at the Mundra site. Now, given this recent supreme court order would it be fair to assume that our expansion is not likely to come anytime in the next few years, and if not, then what could be the alternate use for us, that is my first question?

Anil Sardana: Yes, you are right, we have excess land at Mundra and we had plans to add extra units. I guess that plan will not change because of the Supreme Court order, but will change because of the demand-supply situation. Today, as you know, that demand for additional new capacity is not there and it is not showing up, therefore, we are more watching from that space than the space of this order. In fact, if at all this order will only give rational for us to expedite that additional unit because it helps to cross subsidy some of the under recovery, but we are going to wait till the time that we find that there is extra demand that can absorb that kind of a far requirement.

Pulkit Patni: My second question is irrespective of where you now source coal from for CGPL, whether it comes from domestic or international, would it again be fair to assume that it will come through the Mundra jetty only or could there be a land route that we could explore in case the coal is going to be procured domestically?

Anil Sardana: Pulkit, the way the plant is sited being coastal and in the extreme western area, I do not think so any road transportation will make any sense. It is the sea route which is going to be the most competitive option and of course, if one was to assume that there is coal in the neighborhood and say Thar desert tomorrow or on the other side of the fence, yes, then one can assume that there could be road transportation because it will be just about few 100 miles, but as of now, I do not see those steep changes. My personal belief is that it will be all sea route that we will adapt for the present.

Moderator: Thank you. We take the next question from the line of Prakash Goel from ICICI Securities. Please go ahead.

Prakash Goel: I have two questions, one with respect to the in the current environment, if we sift to the earlier low grade, high grade coal kind of mix, how much cost can we save on that account?

Anil Sardana: Prakash, there are different permutation and different situations that emerge based on, number one, the area from where we are able to source the coal for blending, and number two, the exchange rate. Now, there are times when we have actually blended 70% low-grade coal and that was the most economical point, and at present we are contemplating using something like 30% low-grade coal which today should be the optimum point, so it all depends on source, its calorific value, its parameters, and what is the most optimum combustion in which our heat rate will not deteriorate, at the same time, we will have the benefit of low coal prices, so there are various combinations. We have an algorithm for that and we use that to determine it from time to time.

Prakash Goel: But undoubtedly, your flexibility with respect to mix has increased because earlier the compensatory tariff calculation method which was suggested by CERC that has reduced your flexibility meaningfully?

Anil Sardana: Absolutely right, you are bang on. Earlier in fact our flexibility to even source from other than Indonesia had reduced after the APTEL order, so now that flexibility has enhanced and we will source coal from all locations possible where the landed cost of the coal in terms of per kilocalorie is the lowest.

Prakash Goel: Second is with respect to the credit rating, any update on that or because of this judgment things will change because given our borrowings that could have significant implication on the financials of the company?

Ramesh Subramanyam: Prakash, this Ramesh Subramanyam here. Remember that we have neither accounted in the financial statement the compensatory tariff nor the cash flows where that is taken into account for all the lenders calculation, so our leverage particularly does not have an direct impact on this at all because the cash flows were taken without the compensatory tariff, so the debt etc., everything stands as it is and all we have to do is to really work on as Mr. Sardana said to adjust to this reality and work out our alternative plans for future.

Prakash Goel: In my number, Sir, the interest liability for a year is somewhere around 4000 crore versus your annual EBITDA even if we skewed the coal side would be significantly higher than that, how would you go about repaying the loan because you have various cost of loan across the various geographies?

Ramesh Subramanyam: If you also see the fact that because of our coal mine ownership although this issue of price is a standalone issue for CGPL, on an overall basis, you can see that even if you saw that in the December quarter results and you would see that in March quarter also that the coal companies also have a mirror which is positive, so in that sense our cash flows get balanced to some extent because of that and yes the overall fact is that the leverage is high that we are clearly aware and as Mr. Sardana just mentioned in the first question that we are trying everything to ensure that our leverage comes into control by optimizing on some of the non-core assets that we have and I am sure that you will see in the near future attempts to correct that situation and that situation was already contemplating that whether or not we get this input order, we will have to take those steps for the future.

Prakash Goel: Just want to simplify my question, whether you would bring the money back from the coal mines holding companies to India to pay back the loan at India which is highly more expensive than the overseas foreign currency loan which is significantly cheaper, so how would we go about that, that is what I wanted to understand?

Ramesh Subramanyam: That I think would be decided time to time depending on how given exchange rate and coverage, whether it makes sense to bring here or not because both loans are on a rupee to rupee basis not very different, remember the cost of funds in India are going down drastically compared to what it was earlier, therefore, that gap has reduced Prakash considerably, so we have lot of flexibility in deciding what to do with the money which is coming from the coal mine.

Moderator: Thank you. We have the next question from the line of Dipesh Agarwal from Ambit Capital. Please go ahead.

Dipesh Agarwal: Sir, what is the maximum proportion of domestic coal can Mundra's boiler support?

Anil Sardana: Again, that will depend on the extent of ash it has, and therefore, one will have to look at all those options. Fortunately in the eastern most coast particularly in the MCL area, there are some high GCV mines where we can actually reduce the quantity of ash and look at the possibility of bringing it by small sea route. Now extent will depend on again as I said finally seeing as to what is the washability characteristics and how much ash we can reduce because we won't want to boil more than 12% ash in our Mundra boiler, so that is the blend ratio will get determined based on that.

Dipesh Agarwal: Is it fair to say anything more than 50% would not be possible?

Anil Sardana: Certainly, unless you get an amazing high GCV and low ash content coal, which I doubt exists in the Indian system.

Dipesh Agarwal: Lastly, if tomorrow TATA decides to walk out of the project would there be any significant penalties or any thought on this?

Anil Sardana: We have not contemplated any such option as of today, so we have not built that scenario to say that we will want to walk out of this. We will want to resolve this issue. Till date, we were focusing on a particular direction, now we are looking at other options and you will find that with the time they will be able to resolve this issue.

Moderator: Thank you. We have the next question from the line of Sanjay Jain from Motilal Oswal Securities Ltd. Please go ahead.

Sanjay Jain: Just had one question, is there any dividend policy we have from the coal mining assets that we have in Indonesia, or is there a 100% payout of PAT from those mines or how does it work?

Anil Sardana: If you go by the past trend, that is the way it has been, so yes the payout has been 100% of what the PAT has been unless we have had some ongoing CAPEX and need for funding, otherwise, that has been the policy till date.

Sanjay Jain: Sustenance CAPEX in the mining is mostly covered by the depreciation they have in their P&L?

Anil Sardana: Till date, there has been only one occasion that the extent of CAPEX were larger, but yes you are right, now that has been the prevailing situation.

Moderator: Thank you. We have the next question from the line of Mohit Kumar from IDFC Securities. Please go ahead.

Mohit Kumar: My first question Sir, we had a plan to merge and bring this Indonesian mines under the CGPL, are you going to pursue this now or is it not right now?

Ramesh Subramanyam: Well, Mohit that background was at that time the lenders of Mundra were also insisting for a cash flow arrangement which would automatically make CGPL self-reliant. The idea was once upon a time raised by the lenders and then we had decided accordingly and in fact we had contemplated that for a couple of years before finally the lenders also later on backed out of that discussion, therefore, it was stopped, so right now, there is no such plan.

Mohit Kumar: I am saying in case you try to procure domestic coal through a linkage policy which may come in near future, will it be construed as change in law?

Anil Sardana: I would say the other way round, instead of saying this as a change of law, there may be an argument by the procurers to say that if there is any commercial advantage, they must become the beneficiary of that, so instead of saying change in law where you are saying we could have the benefit, I am saying there could be the other argument to say they could say, they should be the beneficiary, so therefore, that part is not settled. By the way, the scheme for Ultra Mega which was there originally in the Ministry of Power, had this provision that there could be times when Indian coal situation improved, and therefore, the blending should be permitted. We are still looking at those provisions and seeing as to what does it means in the overall context of undertaking that exercise.

Moderator: Thank you. We have the next question from the line of Abhishek Bhattad from Axis Bank. Please go ahead.

Abhishek Bhattad: I just wanted to know one question whether if there is no tariff which you get for the compensatory part whether the Mundra plant will be sustainable to serve the interest on a standalone level, one, and second, if not then what is the annual support which will be required from TATA power for repayments or under recovery on an annual basis, is there any ballpark figure which you have in mind?

Ramesh Subramanyam: Abhishek on a standalone basis CGPL will be able to sustain its own interest substantially, but the curve becomes very steep when coal prices suddenly jump up and therefore, the deficit is really a factor of coal prices, but it substantially serves the interest, it may not serve the repayment, but it substantially covers the interest.

Abhishek Bhattad: For the repayment and under recovery what will be the annual support estimated required from TATA power?

Ramesh Subramanyam: Depending on the coal prices could anywhere be between 400 to 1000 crores depending on what coal price you take because in the previous year, for example, it was less than 500 crores, so it is purely a factor of where the coal prices are.

Moderator: Thank you. We have the next question from the line of Sumit Kishore from J.P. Morgan. Please go ahead.

Sumit Kishore: I just had one question, what is the debt repayment schedule at least for FY18, 19, and 20 for CGPL?

Ramesh Subramanyam: It is around 400 crores per annum, you can write to Kasturi and you will get the exact number.

Moderator: Thank you. We have the next question from the line of Hamsini Karthik from Smart Investor. Please go ahead.

Hamsini Karthik: Sir, I had missed out this one question on my earlier queue, you have just mentioned you have a rough annual repayment structure of about 400 crores, has it seen an escalation post the order, if you could sort of help me get a sense of how the number has moved?

Ramesh Subramanyam: The repayment number, Hamsini, will not move because of the order, nothing has changed.

Hamsini Karthik: Are we well in course to do that, Sir, by ourselves or would be probably now look at another round of debt funding as well for operational support?

Anil Sardana: We do not intend doing any further debt funding for CGPL, at the same time, we certainly will look at debt restructuring of some of our loans, but that is all that we will pursue, nothing more.

Moderator: Thank you. We have the next question from the line of Bhavin Vithlani from Axis Capital. Please go ahead.

Bhavin Vithlani: If you could help us with the balance sheet of CGPL in terms of outstanding debt, domestic, foreign and how much is the debt from TATA Power standalone?

Ramesh Subramanyam: CGPL standalone is about 11,000 crores.

Bhavin Vithlani: Does this also include debt from the TATA power standalone?

Ramesh Subramanyam: No, that is about 4000 crores which is separate.

Bhavin Vithlani: How would the cost of debt be where I understand billion dollars of FX debt, so if you could help us with the cost of debt?

Ramesh Subramanyam: The average would be around between 10.25 to 10.6.

Bhavin Vithlani: On the 11,000 crores?

Ramesh Subramanyam: Yes. 4000 crores is shareholder loan which effectively does not have any interest component to be borne by CGPL.

Bhavin Vithlani: Under Ind-AS is it mandatory to charge interest cost or it has been shown as a separate structure so that the interest component need not be debited?

Ramesh Subramanyam: This the latter which you mentioned is correct, it does not qualify for interest compulsorily under Ind-AS, the way we have structured.

Bhavin Vithlani: In earlier discussion, I got disconnected, what would be non-core assets that look to monetize?

Ramesh Subramanyam: What we are talking about is some of the crossholdings within the group like the Telecom investments mainly, then we have couple of investments, they are not really pertained to power business, it does not belong to the power value chain, so those we call as non-core.

Moderator: Thank you. We have the next question from the line of Dhruv Uchal from Motilal Oswal Securities Ltd. Please go ahead.

Dhruv Uchal: Sir, just specifically going in to the Mundra equation, you said that EBITDA can sufficiently fund the interest cost, but I was just looking at the calculations, I believe you will have an under recovery about 50 to 60 paisa per unit, your EBITDA will be around 600-700, since the interest cost only on your outstanding, I mean if third party debt will be more about 1000 crores, just understanding the equation, I believe you will still be requiring support from your parent?

Anil Sardana: No, I said substantially.

Dhruv Uchal: Okay, not the full amount. Secondly, on your non-core assets just going again with specific here, we have a lot of crossholdings and other things, but the maximum value is from your stake in TATA sons, are you also considering that or how is it?

Ramesh Subramanyam: If your question is whether it is non-core, yes, but whether we are considering that, that we cannot say because these are things which are in due course board decides from time to time, but yes they include certainly, but that is not the only large portions, there are other pieces also.

Moderator: Thank you. Ladies and Gentlemen, that was the last question, I would now like to hand the conference over to Mr. Sardana for closing comments. Thank you and over to you, Sir.

Anil Sardana: Thank you for all for having joined this call. I would still suggest that in case you have any questions feel free to write to our IR team and they will be most pleased to respond you back. There are some information that some of you sought which if it is addressed to Mr. Kasturi, he will make sure that you get the response. Thank you once again for being on the call. Look forward to your joining the call for Q4 of FY17. Good day.

Moderator: Thank you very much members of the management. Ladies and Gentlemen, on behalf of TATA Power Co. Ltd., that concludes this conference. Thank you for joining us and you may now disconnect your lines.