

Uncertain Future

Mundra UMPP faces fuel cost risks

Tata Power Company Limited's (Tata Power) generation capacity crossed the 6,000 MW mark with the commissioning of the second unit of the Mundra ultra mega power project (UMPP). The company commissioned the first 800 MW unit of the 4,000 MW project in March 2012 and the second unit in July 2012. The Mundra UMPP is the country's first such project to commence operations.

Project background

In 2006, Tata Power had emerged as the lowest bidder by offering a 25-year levelised tariff of Rs 2.26 per kWh to win the Mundra UMPP. The project is being developed by Coastal Gujarat Power Limited (CGPL), Tata Power's wholly owned subsidiary. It comprises five 800 MW units based on supercritical technology. Once fully commissioned, the UMPP will meet about 2 per cent of the country's energy

needs. It will supply power to five states – Gujarat (1,805 MW), Maharashtra (760 MW), Rajasthan (380 MW), Punjab (475 MW) and Haryana (380 MW).

The total cost of the project is around Rs 180 billion, which has been funded in a debt-equity ratio of 75:25. The debt has been raised through rupee loans and external commercial borrowings from lenders including the State Bank of India, the Export Import Bank of Korea, the International Finance Corporation and the Asian Development Bank.

The Mundra UMPP requires 10-12 million tonnes per annum (mtpa) of imported coal. To meet the coal requirement, Tata Power acquired 30 per cent equity stake each in PT Kaltim Prima Coal (KPC) and PT Arutmin Indonesia, and a trading company owned by PT Bumi Resources Tbk in 2007. The company also signed an offtake agreement with KPC to pur-

chase about 10.1 mtpa of coal till 2021, which is extendable. However, the project started facing fuel challenges following a change in the Indonesian coal pricing regime in early 2011. The country's government issued the Indonesian Coal Price Regulation (ICPR), which required benchmarking coal prices against a set of international and domestic indices. This led to an increase in the landed price of coal, thereby affecting the economics of projects based on Indonesian coal, including the Mundra UMPP.

ICPR's impact on project

After the notification of the ICPR, Tata Power cannot procure coal on the contracted terms, which has impacted the project's viability. The company is trying to mitigate the effect of the price rise by blending high quality Indonesian coal with eco-coal, which is cost competitive. Despite this, it is not able to achieve break-even for the project. As per the "Tata Power Limited Q1-FY13 Results Conference Call" document, the company needs a tariff hike of 40 paise per unit under the power purchase agreement to break-even and a hike of 65 paise per unit to generate reasonable returns. This would



Mundra UMPP's commissioning schedule

Unit	Month of commissioning
1	March 2012
2	July 2012
3	February 2013
4	August 2013
5	November 2013

Sources: Central Electricity Authority; Tata Power

increase the tariff to around Rs 2.76 per unit and Rs 2.91 per unit respectively.

For the year ended March 2012, Tata Power reported a consolidated loss of Rs 10.88 billion as compared to a profit after tax of Rs 20.6 billion in the previous year. These losses have been mainly on account of the provisions for impairment of the Mundra project, reversal of forex gains and deferred stripping costs by Indonesian coal companies. In 2011-12, the company had booked an impairment of Rs 18 billion for the Mundra project and Rs 6.59 billion as deferred stripping costs. As per the "Analyst Conference Call - September 2012" document, the Mundra UMPP would incur monthly losses of Rs 400 million in 2012-13.

Meanwhile, Tata Power reported a consolidated profit of Rs 1.46 billion in April-June 2012, which is significantly lower (about 66 per cent) than the Rs 4.3 billion registered in the corresponding quarter of 2011-12. During the April-June 2012 quarter, Tata Power blended high grade coal with eco-coal in a 60:40 ratio, which resulted in high fuel costs. Anil Sardana, managing director, Tata Power says, "Up to 70 per cent of eco-coal is being blended to offset some of the cost impact of the steep increase in international coal prices. We plan to maximise this to reduce the overall cost of fuel."

Tata Power needs a tariff hike of 40 paise per unit under the PPA to break-even and 65 paise per unit to generate reasonable returns. This would increase the tariff to around Rs 2.76 per unit and Rs 2.91 per unit respectively.

Tata Power's consolidated results (Rs billion)

	2010-11	2011-12	Q1 2011-12	Q2 2012-13
Total revenues	198.61	262.70	59.48	73.16
Net profit	20.60	(10.88)	4.30	1.46

Source: Tata Power

Company outlook

Against the backdrop of imported fuel price uncertainty and its impact on the project, Standard & Poor's [S&P] Ratings Services revised its outlook on Tata Power from "stable" to "negative" on July 9, 2012. However, Tata Power's long-term corporate credit rating and issue rating on senior unsecured notes remained unchanged at "BB". According to an official statement by S&P, "The outlook revision reflects our expectation that Tata Power's cash flow and financial risk profile could deteriorate over the next six to nine months because the company has breached a debt-equity ratio covenant on loans to its Mundra project." For 2011-12, Tata Power had booked impairment in CGPL's assets due to the depreciation of the Indian rupee against the US dollar, thereby increasing CGPL's foreign currency debt. The reduction in CGPL's equity and its higher debt resulted in the breach of the debt-equity ratio covenant.

S&P may revise the outlook depending on the outcome of Tata Power's negotiations with lenders on the breach of the loan covenant. The outlook would be upgraded to "stable" if the company secures a waiver from its lenders on the breach of covenant and the UMPP's construction adheres to timelines and meets budget projections. However, in the absence of waivers, CGPL will not be able to avail of the loan facility once its drawdown reaches the currently approved level of 83 per cent of the total loan. So far, lenders have not reduced disbursements to the project and Tata Power is expected to

receive waivers for the project. Sardana says, "To support CGPL's cash flows, the company is in discussions with lenders to finalise a structure for transferring coal SPV dividends and is looking forward to a favourable outcome."

Going forward, the company plans to undertake a restructuring process, through which it would transfer 75 per cent of its equity in Indonesia-based coal mining companies to CGPL (subject to regulatory approval) to ensure cash flows for the project.

CGPL approaches CERC for tariff revision

In July 2012, CGPL submitted a petition to the Central Electricity Regulatory Commission (CERC) seeking a tariff revision for power generated from the Mundra UMPP. The CERC initially asked the company to hold meetings with the discoms procuring power from the project. The discoms, led by Gujarat Urja Vikas Nigam Limited, reportedly disagreed to revise tariffs stating that CGPL had considered the variable element of fuel cost in the tariff-based competitive bidding process. They further argued that a tariff increase after the award of the tender would be unfair to bidders who had lost out to Tata Power. Sardana says, "The last meeting was held on September 27, 2012, where all the parties presented their views on the issue and were asked to submit their responses to the regulator. Formal hearings will commence soon after the respondents (procurers) submit their response to the petition."

The regulator's decision on the issue would pave the way for other imported coal-based projects that have been demanding a tariff hike including Reliance Power's Krishnapatnam UMPP. The Mundra UMPP's fate hangs in the balance till the CERC gives its final verdict on tariff revision. ▀

Neha Bhatnagar