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Highlights of Electric Power Companies' Financial Results for Fiscal Year Ended March 2021

The following is Japan Credit Rating Agency, Ltd. (JCR)'s perception of the current status and highlights for rating concerning the financial results for the fiscal year ended March 2021 (FY2020) and earnings forecasts for FY2021 of Japan's ten electric power companies (former general electricity utilities; collectively, the "Companies"): Tokyo Electric Power Company Holdings, Incorporated ("TEPCO"), Chubu Electric Power Company, Incorporated ("Chubu Electric Power"), The Kansai Electric Power Company, Incorporated ("KEPCO"), The Chugoku Electric Power Company, Incorporated ("Chugoku Electric Power"), Hokuriku Electric Power Company ("Hokuriku Electric Power"), Tohoku Electric Power Company, Incorporated ("Tohoku Electric Power"), Shikoku Electric Power Company, Incorporated ("Shikoku Electric Power"), Kyushu Electric Power Company, Incorporated ("Kyushu Electric Power"), Hokkaido Electric Power Company, Incorporated ("Hokkaido Electric Power") and The Okinawa Electric Power Company, Incorporated ("Okinawa Electric Power").

1. Industry Trend

Power demand in FY2020 did not slump as much as feared last spring when the first wave of the COVID-19 pandemic was hitting Japan. According to the actual data on demand published by the Organization for Cross-regional Coordination of Transmission Operators, Japan (OCCTO), nationwide demand fell 1.4% from the previous year, with no areas showing a drop of over 3%. Looking at the data chronologically, it remained stagnant until July, and the decline rate has since been tending to decrease; in fact, there were months in summer and winter when demand was greater than a year before. JCR presumes that temperature effects such as heat and cold waves pushed up demand when economic activities were recovering, offsetting the decline in demand resulting from the pandemic. By sector, demand was robust in the household sector but weak in commercial and industrial sectors, including food services and tourism. By area, the decline rate was relatively higher in populated areas.

Currently, recovery in power demand is slow, but, as a general trend, JCR assumes that the pandemic will affect power supply and demand only temporarily. Nationwide demand for April 2021 was 0.4% less than a year before. As of May 31, areas subject to the state of emergency are expanding, and the commercial sector in particular keeps facing the tough situation. Given a rising rate of infection with new variants, attention should be paid to its impact on power demand for a while. That said, economic activities are becoming more stable than last year, and vaccination has rolled out in Japan, which, along with other factors, suggest that power demand will pick up gradually.

In terms of competition, growth in the sales share of new power suppliers will likely be sluggish for the near future. In February 2021, it came to 20.9% in the low-voltage sector and 25.8% in the high-voltage sector, as opposed to 16.8% and 23.1% a year before; total share including the extra high-voltage sector was 19.8%, versus 16.2% a year before. Electricity wholesale prices plunged in 2020 as the recession pushed down fuel prices. While price competition intensified, growth rate in the sales share of new power suppliers increased. However, power demand grew sharply from the end of 2020 to beginning of 2021 due to the cold wave, and electricity wholesale prices surged. This forced retail power suppliers to purchase electricity from the wholesale market with a huge negative spread, worsening business conditions for many of them; some even faced a severe cash flow problem and went bankrupt. As such, new power suppliers' shares peaked out in December and are now at a bit lower level. Even though power supply and demand is not likely to tighten frequently, it is projected that retail suppliers will revise channels to procure electricity to some extent, including making more negotiated transactions for stable procurement.

Last winter's tight power supply and demand situation in a way reaffirmed the importance of stable supply. Primary factors behind such a tough situation include: i) suspension of nuclear power stations with high output; ii) facility failure at coal-fired thermal power stations; iii) fuel shortage at LNG thermal power stations; iv) drop in water flow rate; and v) decrease in renewable energy power generation due to unusual weather. Moreover, the suspension and retirement of inefficient thermal power stations in recent years is considered to have had remote impacts, too. Even though these events happened one after another by coincidence, the future remains uncertain. The above events are independent from each other and not likely to occur simultaneously, but, as far as i) to v) are concerned, it must be noted that they could happen at any time. According to “Aggregation of Electricity Supply Plans for FY 2021” announced by OCCTO, there are multiple areas where the estimated reserve margin for FY2021 is below the target of 8%. Based on the lessons learned here, power companies should work to ensure stable supply capacity so that they can supply electricity without trouble even when demand surges.

Last winter’s tight power supply and demand situation appears to have caused a stir in the formulation of the sixth basic energy plan, which is scheduled to be announced this year. Countries around the world renewed their environment policies in 2020, setting even higher targets for greenhouse gas reductions. In Japan, too, Prime Minister Suga has declared that Japan pledges to reach carbon neutral by 2050 and achieve a decarbonized society. Of the principle of 3E+S (energy security, economic efficiency and environment, plus safety) in the aforementioned energy plan, it is most likely that more attention will be paid to “environment.” However, as mentioned earlier, the importance of stable supply cannot be ignored, either. Excessive reliance on renewable energy and reduction of coal-fired thermal power generation as a base load source could be burdensome in terms of not only stability in supply but economic efficiency. There are areas where alternative power sources cannot be secured in neighboring areas, and hasted retirement of inefficient coal-fired thermal power stations in an uncompromising manner could have side effects. Therefore, it must be closely examined whether the plan provides realistic solutions in light of domestic situations that are different from Europe where the use of renewable energy is advancing.

Moves toward the restart of nuclear power stations are slow. There were no new developments after the Nuclear Regulation Authority (NRA) granted permission to make changes in reactor installation at Onagawa Nuclear Power Station Unit 2 in February 2020. Meanwhile, as regards Ikata Nuclear Power Station Unit 3, a temporary injunction on its operation has been dissolved, and the unit is expected to restart once the construction of specialized safety facilities is completed. Also, Takahama Nuclear Power Station Units 3 and 4 and Sendai Nuclear Power Station Units 1 and 2, where the construction of such facilities was not completed by the specified deadline, have resumed their operation. On a separate note, Mihama Nuclear Power Station Unit 3, which was in operation for over 40 years, is expected to restart, though for a short period.

There have been governance issues, too. TEPCO received stringent orders from NRA in regards to a rash of incidents at Kashiwazaki-Kariwa Nuclear Power Station, including the partial loss of nuclear material protective equipment function. Moreover, the Japan Fair Trade Commission conducted on-site inspections on Chubu Electric Power, KEPCO and Chugoku Electric Power for suspected anti-trust operations. As such, power companies are once again urged to strengthen their business management structures.

2. Financial Results

Volume of power sales declined for many of the Companies. By company, it dropped for eight companies excluding Hokuriku Electric Power and Kyushu Electric Power (including Kyuden Mirai Energy Company, Incorporated). While the pandemic had a large impact, competition remains tough as an underlying factor, especially in the low-voltage sector.

Business results for FY2020 do not look good on the whole. Ordinary income for the Companies combined dropped 19.3% over the year to 759.2 billion yen, first fall in two years. As negative factors here, sales volume and profitability resulting from a time lag in fuel cost adjustment decreased, while the operating rate of nuclear power stations at KEPCO, Shikoku Electric Power and Kyushu Electric Power dropped and the Fukushima Prefecture offshore earthquake affected Tohoku Electric Power. As regards the tight power supply and demand situation, its impacts varied depending on the difference in supply capacities. Meanwhile, Chubu Electric Power, Kyushu Electric Power, Hokkaido Electric Power and Okinawa Electric Power attained a higher ordinary income, thanks primarily to the revised depreciation method for Kyushu Electric Power achieving a particularly high growth rate and improved management efficiency for Hokkaido Electric Power.

Financial standing improved a little. Profits accumulated with the posting of net income, bringing combined equity ratio as of the end of FY2020 to 22.8%, as opposed to 22.1% a year before. However, large capital expenditures for safety measures for nuclear power stations, construction/replacement of thermal power stations, measures for aging power transmission and distribution facilities, etc. are likely to continue, and, given the cash flow generation capacity, JCR assumes that interest-bearing debt is hardly likely to decrease.

3. Highlights for Rating

Overall results for FY2021 are not likely to improve on the whole as it is still unpredictable when the COVID crisis will tail off. While TEPCO and Tohoku Electric Power have not yet determined their forecasts for ordinary income, Shikoku Electric Power and Kyushu Electric Power forecast a higher income as they expect a rise in the operating rate of nuclear power stations, and the remaining six project a lower income probably due largely to decreases in sales volume and profitability resulting from a time lag in fuel cost adjustment, as with the previous year. That said, as a result of revisions to the Regulation on Accounting in Telecommunications Services, levies and subsidies under the Renewable Energy Special Measures Act will be excluded from net sales from FY2021, which will likely result in lower net sales levels. However, because the costs will also be deducted by the same amount, overall earnings will not be affected.

As points of attention, JCR continues to look at power sales volume. The Companies are expected to engage in sales activities appealing added values and focus on profitability by, for instance, offering the electricity and gas package, introducing price plans tailored to lifestyles of individual households and proposing energy-saving operation systems in the high-voltage and extra high-voltage sectors, and their outcomes will be examined. Moreover, based on the lessons learned from last winter's tight power supply and demand situation, there is a possibility that the price action and sales methods of new power suppliers will be modified, thus halting excessive competition. JCR will closely watch changes in the sales share of new electric power, especially in the low-voltage sector.

Next is the profit level excluding gains/losses resulting from the time lag in fuel cost adjustment. The Companies' simple aggregation has been falling from the recent peak marked in FY2018. For drastic profit improvement, nuclear power stations into which a large amount of capital has been invested need to be restarted. It has been estimated that, once they start operating again, fuel costs will be cut significantly. It will thus be vital for the Companies to make steady progress in obtaining NRA's permission and executing safety works and to effectively utilize non-operating assets. Attention will also be paid to their cost-cutting efforts. In fact, the Companies are working to reduce material procurement expenses and control repair and personnel expenses by streamlining operations, thereby producing certain results.

Last is trends in free cash flow. Capital expenditures have not been fully covered by operating cash flow, and interest-bearing debt keeps growing. With an increase in equity capital through profit accumulation, financial indicators have improved slightly or remained almost flat from the previous year. As there remain capital requirements, including investments in safety measures essential to restarting nuclear power stations and replacement of thermal power stations, financial structure will likely improve only slowly over the medium term. That said, the power industry is one of a few that can raise funds steadily even in the midst of the pandemic. Therefore, there is less concern about financing than right after the Fukushima Daiichi nuclear disaster.

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(Chart) Consolidated Financial Results

(JPY 100 mn, %, equity content of hybrid securities not considered)

	FY	Net Sales	YoY Change	Ordinary Income	YoY Change	Net Income	Equity Ratio
TEPCO (9501)	FY2019	62,414	-1.5	2,640	-4.5	507	24.3
	FY2020	58,668	-6.0	1,898	-28.1	1,808	25.8
	FY2021F	-	-	-	-	-	-
Chubu Electric Power (9502)	FY2019	30,659	1.0	1,918	69.8	1,634	34.4
	FY2020	29,354	-4.3	1,922	0.2	1,472	35.7
	FY2021F	23,600	-	1,300	-	950	-
KEPCO (9503)	FY2019	31,842	-3.7	2,115	3.9	1,300	21.0
	FY2020	30,923	-2.9	1,538	-27.3	1,089	20.9
	FY2021F	25,000	-	1,000	-	700	-
Chugoku Electric Power (9504)	FY2019	13,473	-2.2	398	214.1	900	19.7
	FY2020	13,074	-3.0	300	-24.5	145	19.4
	FY2021F	9,700	-	200	-	150	-
Hokuriku Electric Power (9505)	FY2019	6,280	0.8	232	249.1	134	20.2
	FY2020	6,394	1.8	123	-46.8	68	21.2
	FY2021F	5,200	-	100	-	50	-
Tohoku Electric Power (9506)	FY2019	22,463	0.1	999	52.1	630	18.3
	FY2020	22,868	1.8	675	-32.5	293	18.5
	FY2021F	17,700	-	-	-	-	-
Shikoku Electric Power (9507)	FY2019	7,331	-0.6	279	11.2	180	23.6
	FY2020	7,192	-1.9	51	-81.4	29	22.8
	FY2021F	5,500	-	180	-	130	-
Kyushu Electric Power (9508)	FY2019	20,130	-0.2	400	-23.8	-4	12.3
	FY2020	21,317	5.9	556	39.0	321	12.7
	FY2021F	15,100	-	700	-	450	-
Hokkaido Electric Power (9509)	FY2019	7,484	-0.5	326	8.1	267	12.0
	FY2020	7,407	-1.0	411	26.1	361	13.8
	FY2021F	5,750	-	230	-	200	-
Okinawa Electric Power (9511)	FY2019	2,042	-0.6	93	78.4	67	37.7
	FY2020	1,905	-6.7	113	21.7	83	37.8
	FY2021F	1,624	-	65	-	47	-
Total	FY2019	204,123	-1.1	9,403	18.8	5,618	22.1
	FY2020	199,107	-2.5	7,592	-19.3	5,675	22.8

(Source: Prepared by JCR based on financial materials of above companies)

<Reference>
Issuer: Tokyo Electric Power Company Holdings, Incorporated
Long-term Issuer Rating: A Outlook: Stable

Issuer: Chubu Electric Power Company, Incorporated
Long-term Issuer Rating: AA Outlook: Stable

Issuer: The Kansai Electric Power Company, Incorporated
Long-term Issuer Rating: AA- Outlook: Positive

Issuer: The Chugoku Electric Power Company, Incorporated
Long-term Issuer Rating: AA Outlook: Stable

Issuer: Hokuriku Electric Power Company
Long-term Issuer Rating: AAp Outlook: Stable

Issuer: Tohoku Electric Power Company, Incorporated
Long-term Issuer Rating: AA Outlook: Stable

Issuer: Shikoku Electric Power Company, Incorporated
Long-term Issuer Rating: AAp Outlook: Stable

Issuer: Kyushu Electric Power Company, Incorporated
Long-term Issuer Rating: AA- Outlook: Stable

Issuer: Hokkaido Electric Power Company, Incorporated
Long-term Issuer Rating: AA-p Outlook: Negative

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