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Highlights of Electric Power Companies' Financial Results for Fiscal Year Ended March 2020

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 2020 (FY2019) and earnings forecasts for FY2020 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 and Impact of COVID-19 Pandemic

Power demand is currently dull. According to a report by the Organization for Cross-regional Coordination of Transmission Operators, Japan, nationwide demand for April was 3.6% less than a year before. As it appears, demand in industrial and commercial sectors declined due to a fall in the operating rates of factories, temporary closure of commercial facilities, etc. triggered by the coronavirus disease (COVID-19) pandemic. Even though economic activities are beginning to pick up as the state of emergency was lifted in May, whether power demand will return to the pre-pandemic level is unpredictable at this point. As a general trend, demand will likely be affected by the pandemic only for a short term; yet, close attention should be paid to factors like the possibility of sluggish demand lasting longer and any changes in demand characteristics due to shifts in lifestyles after the pandemic is successfully controlled. The impact of the pandemic on trends not only in demand but supply should also be noted, i.e. impact on the further penetration of renewal energy sources, construction of facilities for implementing measures against severe accidents, which is the key to and restarting nuclear power stations, and progress in the reviews by the Nuclear Regulation Authority (NRA) on conformity to new regulatory requirements.

In terms of competition, the sales share of new power suppliers is rising but at a slower pace now. In January 2020, it came to 15.7% in the low-voltage sector and 24.0% in the high-voltage sector, as opposed to 11.9% and 24.4% a year before; total share including the extra high-voltage sector was 16.0%, versus 14.6% a year before. As a factor behind this, the focus of competition is shifting from acquiring cost-conscious customers to providing services to meet customer needs. In order to curb the decline in sales volume, power companies have been engaged in marketing efforts to increase added value by, for instance, introducing rate plans to suit the lifestyle of individual households in the low-voltage sector and proposing a switch to operating systems with higher energy-saving effects in the extra high-voltage and high-voltage sectors.

Business environment for coal-fired thermal power generation is becoming increasingly tougher. Power companies are upgrading their power stations to achieve better efficiency with controlled CO_2 emissions. That said, there are moves overseas, especially in EU, demanding the discontinuation of coal-fired thermal power stations, while there are financial institutions in Japan that have announced the suspension of providing new loans for these facilities. Because of recent years' delays in the restart of nuclear power stations to follow those already in operation, there are no major changes in the moves to utilize highly economical coal-fired thermal power generation, albeit environmental issues. JCR considers that, in order to keep this system as a future base load source, options to construct new stations and upgrade existing ones should remain available. As the political and financial aspects are not necessarily aligned, direction of coal-fired thermal power generation will probably be the focus when formulating the next basic energy plan.

As regards nuclear power stations, moves toward restart are hardly making progress, while some issues have been identified once again. Looking back at the past year, a money scandal involving a power company surfaced in September 2019, and it cannot be denied that this incident fed public distrust in Japan's nuclear power policy. In 2020, while NRA's permission to make changes in reactor installation at Onagawa Nuclear Power Station Unit 2 was granted, provisional injunction of Ikata Nuclear Power Station Unit 3 was ruled again. Moreover, the installation of severe accident countermeasure facilities at Sendai Nuclear Power Station Units 2 and 3 missed the prescribed deadline, necessitating the suspension of operation. From the perspective of ensuring profits and cash flow, restart and safe operation of nuclear power stations is essential. As such, JCR views that risks associated with nuclear power stations, which have been rather decreasing in recent years, still remain a serious challenge for power companies.

2. Financial Results

Volume of power sales has been on the decline. Combined total for the Companies for FY2019 fell 2.9% over the year to 718.7 billion KWh, which was the ninth consecutive decrease since the Great East Japan Earthquake. Looking individually, all of the Companies but Hokkaido Electric Power reported a lower volume. Factors behind this long-term decline include temperature effects, as well as structural ones such as energy efficiency awareness among customers, energy saving of power-consumption equipment and constant switching of customers to new power suppliers.

Actual results for FY2019 do not look good. On the positive side, combined ordinary income came to 940.3 billion yen, turning upward with an 18.8% year-on-year growth. Many of the Companies improved profitability resulting from a time lag in fuel cost adjustment with a constant decline in fuel prices and benefited from a change in the depreciation method from the declining balance method to the straight-line method, which more than offset the decline in sales and other negative factors. Consequently, all of the Companies but TEPCO and Kyushu Electric Power achieved income growth. That said, as positive factors include one-time ones, it cannot be necessarily concluded that earnings power is increasing. In any case, nine companies other than Kyushu Electric Power attained a net income; Kyushu Electric Power posted a slight net loss due to the partial reversal of deferred tax assets.

Financial standing on the other hand improved. Profits accumulated with the posting of net income, bringing combined equity ratio as of the end of FY2019 to 22.1%, as opposed to 21.0% a year before. However, the Companies intend to continue large capital expenditures for safety measures for nuclear power stations, construction/replacement of thermal power plants, measures for aging power transmission and distribution facilities, etc., and, given current cash flow generation capacity, JCR assumes that interest-bearing debt is hardly likely to decrease. Moreover, in comparison with the level before the Great East Japan Earthquake, financial structure is still on the road to full recovery.

3. Highlights for Rating

Business results for FY2020 are unpredictable. All of the Companies but Okinawa Electric Power have not finalized their ordinary income forecast because of uncertain factors associated with the pandemic. Okinawa Electric Power did not incorporate the impact of the pandemic in its forecast due to extreme difficulty of calculation. For FY2020, attention should be paid to how business performance will be affected by a decline in power demand in industrial and commercial sectors, suspension of operation at some nuclear power stations, etc.

JCR is looking at three factors. First is trends in power sales volume. While the competition environment is now fairly stable, a lower sales volume continued to hinder business improvement in for FY2019, drawing attention to the measures taken to maintain and increase this volume. The Companies are striving to expand sales outside their respective service areas through wholesale to other retail power suppliers, electricity and gas package sales and alliance with other electric power companies, in addition to making their own marketing efforts as mentioned above. However, it must be noted that the wholesale margin is low and profitability is falling due to low resource prices. Also, even though the Companies, being in the process industry, need to secure a certain level of power sales volume, they should probably focus more on business development in balance with profitability, rather than being excessively concerned about sales volume and market shares.

Second is the profit level excluding gains/losses resulting from the time lag in fuel cost adjustment. For FY2019, majority of the Companies reported lower levels. In terms of costs, reduction of fuel costs is effective, and the restart of nuclear power stations is getting particular attention. 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. They will also be expected to continue cost-cutting efforts. In fact, they are focusing on reducing material procurement expenses and controlling repair and personnel expenses by streamlining operations.

Third is free cash flow. Equity capital is expected to keep building up with profit accumulation for a while. Yet, capital expenditures have not been fully covered by operating cash flow, making interest-bearing debt keep growing on the whole. As long as safety measures essential to restarting nuclear power stations require large amounts of investment, financial structure may improve only slowly over the medium term. That said, the power industry is one of a few that can raise funds by issuing corporate bonds 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 1) Consolidated Financial Results

(JPY 100 mn, %)

	FY	Net Sales	YoY Change	Ordinary Income	YoY Change	Net Income	Equity Ratio
TEPCO (9501)	FY2018	63,384	8.3	2,765	8.5	2,324	22.6
	FY2019	62,414	-1.5	2,640	-4.5	507	24.3
	FY2020F	-	-	-	-	-	-
Chubu Electric Power (9502)	FY2018	30,350	6.4	1,129	-12.1	794	29.7
	FY2019	30,659	1.0	1,918	69.8	1,634	34.4
	FY2020F	-	-	-	-	-	-
KEPCO (9503)	FY2018	33,076	5.6	2,036	-6.2	1,150	20.9
	FY2019	31,842	-3.7	2,115	3.9	1,300	21.0
	FY2020F	-	-	-	-	-	-
Chugoku Electric Power (9504)	FY2018	13,769	4.7	126	-58.7	114	17.0
	FY2019	13,473	-2.2	398	214.1	900	19.7
	FY2020F	-	-	-	-	-	-
Hokuriku Electric Power (9505)	FY2018	6,229	4.5	66	149.2	25	19.9
	FY2019	6,280	0.8	232	249.1	134	20.2
	FY2020F	-	-	-	-	-	-
Tohoku Electric Power (9506)	FY2018	22,443	8.3	657	-25.7	464	17.9
	FY2019	22,463	0.1	999	52.1	630	18.3
	FY2020F	-	-	-	-	-	-
Shikoku Electric Power (9507)	FY2018	7,372	0.8	251	-10.3	169	23.6
	FY2019	7,331	-0.6	279	11.2	180	23.6
	FY2020F	-	-	-	-	-	-
Kyushu Electric Power (9508)	FY2018	20,171	2.9	525	-28.7	309	13.3
	FY2019	20,130	-0.2	400	-23.8	-4	12.3
	FY2020F	-	-	-	-	-	-
Hokkaido Electric Power (9509)	FY2018	7,522	2.6	301	55.4	223	11.1
	FY2019	7,484	-0.5	326	8.1	267	12.0
	FY2020F	-	-	-	-	-	-
Okinawa Electric Power (9511)	FY2018	2,054	4.8	52	-37.7	37	37.8
	FY2019	2,042	-0.6	93	78.4	67	37.7
	FY2020F	1,918	-6.1	93	-0.1	70	-
Total	FY2018	206,376	6.2	7,912	-7.1	5,614	21.0
	FY2019	204,123	-1.1	9,403	18.8	5,618	22.1

(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: Negative

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

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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