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Highlights of Electric Power Companies' Financial Results for Fiscal Year Ended March 2019

The following are 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 2019 (FY2018) and earnings forecasts for FY2019 of 10 former general electricity utilities: 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

The market shares by new entrants were 12.7% for low voltage sector, 22.9% for high voltage sector, and 14.6% for the entire market including extra high sector in terms of nationwide electricity sales volume in February 2019. Although their sales shares reached a certain level, there are movements such as stop or slowing down of their rising shares in parts of regions for low voltage sector. In the high voltage sector, the rise of their shares started to stop in many regions around summer of 2018. It is considered that the background to these movements include the electric power companies' aggressive sales activities and restrictions on procurements of power sources facing new entrants, and trend that has been continuing since full liberalization of electricity retail sales is changing.

Concerning Japan's energy policy, under the 5th Basic Energy Plan announced in May 2018, the central government plans to nurture renewable energy into a major power source for the long future vision toward 2050. Based on this policy, the electric power companies set forth their plans to further promote their developments of renewable energy. In the domestic new development, in particular, many companies set forth their plans to focus on offshore wind power which is considered to have relatively large room for development. Detailed designing for new systems such as "baseload power market" and "capacity market" is progressing toward electricity system reform. While there are systems that promote competition in the retail market, some of these systems can lead to investment recovery for the electric power companies. It is necessary to closely watch the trend of these markets, but JCR sees that it is less likely that these systems to be introduced will have a significant impact on their business bases in light of the discussions that have been made to date.

From a perspective of securing profit and cash flow, restart of nuclear power plants or their stable operation remains an important issue facing a nuclear operator. At the moment, there are 9 nuclear power units which obtained required approval and authorization in Nuclear Regulation Authority ("NRA")'s reviews on the conformity to the requirements, and the number has not increased from the end of March 2018, which shows that the pace of restart has not increased. NRA's reviews have steadily progressed for some of the plants, but it is considered difficult to reach restart within FY2019 in light of the current conditions. In April 2019, NRA decided a policy to issue order to stop operations of nuclear power plants, if the companies fail to establish facilities for measures against severe accidents by the deadline under the laws and regulations. This decision may have an impact on an operator which has a plant in normal operation from a perspective of stable operation. In general, risks facing nuclear operators cannot be said to have been reduced.

2. Financial Results

The 10 companies' total electricity sales volume, which decreased 2.7% year-on-year to 740.1 billion KWh for FY2018, has been decreasing for 8 years in a row since the occurrence of the Great East Japan Earthquake. While there are changes in the volume due to effects from air and water temperatures, there have been no changes to the structural factors such as established users' saving consciousness, energy saving of power-consumption equipment, and continued shift of existing customers to new entrants. Based on their total volume of electricity sales including their wholesale to other retail electricity sales operators such as new entrants and contributions to a wholesale power exchange, Japan Electric Power Exchange ("JEPX"), the declining pace may have been lower. Total ordinary income of the 10 companies for FY2018 declined 7.1% year-on-year to 791.2 billion yen. Many companies worsened time lag gains (losses) of fuel cost adjustment due to the increased fuel price, and operators who have higher ratio of LNG-fired thermal power in composition of power sources, in particular, decreased a relatively large amount of income.

Eight companies out of the 10 companies announced the forecasts for the profits for FY2019, and the number increased from 5 when they released financial results for both FY2016 and FY2017. At the beginning of past fiscal years, many have not announced their forecasts due to factors including difficulty in assuming the time of restart of nuclear power plants, but they estimated their profits based on assumptions of their continued normal operations or failure to realize restart during the term for FY2019. Some companies will increase their accounting profits thanks to their shift of depreciation methods from the declining balance method to the straight-line method as well as improvement of time lag gains (losses) of fuel cost adjustment. Meanwhile, their business environment remains severe, and many companies will continue to see a decline of their electricity sales volume against the backdrop of structural factors as described above, excluding effects from air and water temperatures. In addition, given that competition across boundaries of their supply areas is intensifying, their profit margins will shrink due to price reduction.

Many companies advanced their equity capital recovery thanks to continued recording of net income. Equity ratio of the 10 companies in total increased to 21.0% as of March 31, 2019 from the recent bottom of 14.2% as of March 31, 2013. JCR sees that it will be unlikely that they will reduce interest-bearing debt, because they are required to make investments in safety measures for nuclear power plants, construction or replacement of thermal power plants, measures for aging power transmission and distribution facilities. Considering the level before the Great East Japan earthquake as a goal, their financial structure is still on the road to recovery except some operators. Their business risks are on the rise along with progress of electricity system reform, and further enhancement of financial bases remains an issue facing the electric power companies.

3. Highlights for Rating

There were companies which decreased their profits excluding time lag gains (losses) of fuel cost adjustment for FY2018. Although there are different factors for individual companies such as lower nuclear use rate, water shortage, increased repair costs, and so on, there are effects from the decreased electricity sales volume. Although a significant improvement of time lag gains (losses) of fuel cost adjustment is expected and changes in the depreciation method will become a factor for the profit increase up to several tens of billions of yen for multiple companies in FY2019, the amount of increase as a whole is not necessarily large. Factors for the profit decrease include a decline of electricity sales volume, burden of depreciation expenses due to start of operations of new thermal power plants, increasing repair cost, etc. In general, the electric power companies forecasted their business performance in a conservative manner. JCR sees that this is because they don't hold an optimistic view on the electricity sales volume, which is core of their profits, and its profitability.

It is also necessary to pay attention to their total sales volume including wholesale, etc under the fully liberalized energy retail market. Along with the increasing shares by new entrants for the electricity sales volume, the electric power companies are increasing their wholesale to other retail electricity sale operators and contributions to JEPX. It is important to secure a certain level of the total electricity sales volume to promote investment recovery, while retaining the operation rates of their owning facilities. As margin from wholesale in general is thin as compared with margin from retail, if the wholesale ratio to the total electricity sales volume increases, it will lower the overall profitability. It is also necessary to use certain funds for competition in order to keep customer bases in terms of the retail electricity sales volume. There is a possibility that their profitability will gradually decline, although they can curb the decline of the sales volume through various kinds of marketing policies.

JCR sees at the moment that these negative impacts on the profit in terms of electricity sales are covered to some extent by an increase of revenue from wheeling service, cost reduction through higher management efficiency, etc. The market share increase for electricity sales volume by new entrants is now leveling off, but these negative impacts on the profit in terms of electricity sales will become larger, depending on progress of future shift of existing customers to new entrants. It is therefore necessary to closely watch trend of total electricity sales volume including wholesale and changes in profitability of electric power business. Given that cost competitiveness of power sources is an important element to keep profitability, JCR will also continue to pay attention to their roadmap to normalization of composition of power sources through restart of nuclear power plants.

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(Chart 1) Consolidated Financial Results

(JPY100 mn, %)

	FY	Net Sales	YoY	Ordinary Income	YoY	Net Income	Equity Ratio
TEPCO	FY2017	58,509	9.2	2,548	12.0	3,180	21.1
(9501)	FY2018	63,384	8.3	2,765	8.5	2,324	22.6
	FY2019F	-	-	-	-	-	
Chubu Electric Power	FY2017	28,533	9.6	1,285	5.8	743	31.3
(9502)	FY2018	30,350	6.4	1,129	-12.1	794	29.7
	FY2019F	30,500	0.5	1,850	63.8	1,650	
KEPCO	FY2017	31,336	4.1	2,171	10.7	1,518	20.8
(9503)	FY2018	33,076	5.6	2,036	-6.2	1,150	20.9
	FY2019F	32,500	-1.7	2,000	-2.4	1,400	
Chugoku Electric Power	FY2017	13,149	9.5	307	57.5	207	18.2
(9504)	FY2018	13,769	4.7	126	-58.7	114	17.0
	FY2019F	13,710	-0.4	360	183.8	250	
Hokuriku Electric Power	FY2017	5,962	9.9	26	32.8	-4	19.8
(9505)	FY2018	6,229	4.5	66	149.2	25	19.9
	FY2019F	6,300	1.1	-	-	-	
Tohoku Electric Power	FY2017	20,713	6.2	884	-15.5	472	17.3
(9506)	FY2018	22,443	8.3	657	-25.7	464	17.9
	FY2019F	23,900	6.5	730	11.0	450	
Shikoku Electric Power	FY2017	7,317	6.9	280	75.8	196	23.5
(9507)	FY2018	7,372	0.8	251	-10.3	169	23.6
	FY2019F	7,340	-0.4	240	-4.5	170	
Kyushu Electric Power	FY2017	19,603	7.3	736	-21.8	866	13.4
(9508)	FY2018	20,171	2.9	525	-28.7	309	13.3
	FY2019F	20,850	3.4	800	52.5	550	
Hokkaido Electric Power	FY2017	7,330	4.3	194	54.1	165	10.5
(9509)	FY2018	7,522	2.6	301	55.4	223	11.1
	FY2019F	7,700	2.4	340	12.7	280	
Okinawa Electric Power	FY2017	1,961	9.0	83	11.4	62	37.7
(9511)	FY2018	2,054	4.8	52	-37.7	37	37.8
	FY2019F	2,065	0.5	72	37.9	55	
Total of 10 Companies	FY2017	194,418	7.7	8,517	6.2	7,409	20.6
	FY2018	206,376	6.2	7,912	-7.1	5,614	21.0

Source: 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: Stable

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: Positive

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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