Azure Power

Q2 Fiscal 2022 Earnings Conference Call

December 13, 2021 at 8:30 a.m. Eastern Time

CORPORATE PARTICIPANTS

Ranjit Gupta – *Chief Executive Officer*

Murali Subramanian – *Chief Operating Officer*

Pawan Kumar Agrawal – *Chief Financial Officer*

Vikas Bansal – *Investor Relations*

PRESENTATION

Vikas Bansal
Thank you. Good morning everyone, and thank you for joining us today. On Friday evening, the company issued a press release announcing results for the second quarter of fiscal 2022 ended September 30, 2021. A copy of the press release and the presentation are available on the Investors' section of Azure Power's website at azurepower.com.

With me today are Ranjit Gupta, CEO; Murali Subramanian, COO; and Pawan Kumar Agrawal, CFO. Ranjit will start the call by going through key highlights and business updates. Murali with then follow with an update on our projects under construction, operational innovations, and an industry update. Pawan will then provide an update on the quarter and then we will wrap up the call with Ranjit providing Q3 FY'22 and FY'22 guidance. After this, we will open up the call for questions.

Please note, our Safe Harbor statements are contained within our press release, presentation materials and available on our website. These statements are important and integral to all our remarks. There are risks and uncertainties that could cause our results to differ materially from those expressed or implied by such forward-looking statements. So, we encourage you to review the press release we furnished in our Form 6-K and presentation on our website for a more complete description.

Also contained in our press release, presentation materials and annual report are certain non-GAAP measures that we reconcile to the most comparable GAAP measures, and these reconciliations are also available on our website, in the press release, presentation materials and annual report.

It is now my pleasure to hand it over to Ranjit.

Ranjit Gupta

Thank you Vikas, and a very good morning everyone.

I am happy to report that we have steadily transitioned from work from home to our office desks this quarter while following Covid appropriate protocols. Worldwide we do see disruptions continue due to Covid and its variants but hope that severity remains contained.

On the ESG front, we have taken number of significant steps this quarter towards improving our ESG standards. We have been focusing on reducing our Scope 1 emissions and have adopted an Electric Vehicle policy. As part of this policy, any new vehicle that the company purchases going forward for common company use will only be EV. Further, we have adopted our Social Accountability Policy to enshrine socially acceptable & responsible practices in our workplace. Through our social accountability policy, we have committed compliance to SA 8000 standard requirement for ourselves and our vendors. We have already conducted internal audits to ascertain compliance to SA 8000 principles and are planning external audit certification in the month of January 2022. SA 8000 certification will reaffirm our commitment to maintain labor and working conditions as per international standards. We continue to strive hard to improve our ESG performance and keep demonstrating our leadership.

Beyond ESG, my most important business update is signing of 600 MW of PPA from the SECI Manufacturing capacity of 4 GW. We further understand that SECI has signed 7,000 MW of PSAs with the state of Andhra Pradesh, which will translate to another 2,333 MWs of PPAs getting signed for Azure very soon. These are heartening and significant developments post elongated period of wait on these projects. Tariffs of INR 2.54/- for the 600 MW PPAs and INR 2.42/- for PPAs to be signed under Andhra Pradesh PSAs, are significantly value accretive. We expect returns comfortably above the upper end of our threshold targets. Given the work we have already done with land acquisition and securing transmission connectivity, we will strive to complete these projects before time.

Apart from the SECI Manufacturing PPA, we received Letter of Awards for 120 MW wind project and 150 MW Wind–Solar hybrid project with SECI, subsequent to quarter end. These are first steps beyond solar for Azure and we firmly believe that as the industry moves towards providing dispatchable renewable energy to the grid, wind & storage will be two important technology additions in our portfolio. We have already developed significant organizational capabilities for these in-house and are looking forward to implementation on the ground with our teams already working on developing large wind sites across the country.

Further, we are actively developing our capabilities in new operating areas for renewable energy, be it energy transition for corporates or new technologies like green hydrogen. The Government has already announced the National Hydrogen Mission and proposed policies related to Green Hydrogen adoption. I firmly believe that Energy Storage and Green Hydrogen are going to change India's energy consumption scenario quite dramatically within this decade. Azure aims to be at the forefront of these new businesses and has taken concrete steps in this direction.

On operational front, while Murali will talk in detail, I am extremely proud of our procurement and construction teams given the challenges this year, from Covid disruptions in the first quarter followed by volatile supplies and module pricing more recently. We had 31% more MWs operating in Q2 this year than we did at the same time last year. There has been an 28% year on year increase in EBITDA from our Operating Assets and a 32% increase in Cash Flow to Equity from Operating Assets during the quarter. We continue to see steady improvement in these metrics owing to our continuous efforts at project sites. I also commend the stellar work done by the Capital team in raising the lowest cost Green Bond and refinancing older projects driving down our cost of debt by almost 200 basis points in these projects.

The Government continues to support the Renewable Energy sector in India. India recently announced 150GW of installed Renewable Energy capacity in the country including Hydro. Hon'ble Prime Minister at his address during COP26 meeting in Glasgow provided 5 resolve that India has undertaken to contribute towards global fight against climate change. These include (1) increased non-fossil energy capacity target of 500GW by 2030, (2) to meet 50% of the country's energy requirement through renewable energy by 2030, (3) reduce economy's carbon intensity down to 45% by 2030, (4) reduce 1 billion tonnes of carbon emissions from the total projected emissions by 2030, and (5) achieve Net Zero emissions by 2070.

These announcements along with India's goal of self-reliance in energy by 2047, i.e., 100th year of Indian independence, clearly demonstrate the vast growth opportunity this sector presents for Azure. We are looking at our addressable market size of ~40 GW per annum going into this decade considering India's target of 500 GW by 2030. Investments in new renewable energy generating assets will top USD 250 billion just within this decade.

In consonance with this ambitious target, the Government has recently taken a series of very significant reform measures to strengthen operating framework and boost investor confidence in the sector. After landmark judgement from the Appellate Tribunal for Electricity allowing compensatory tariff for solar power curtailments in the state of Tamil Nadu, Ministry of Power, recently brought a notification reinforcing "Must Run" status for RE power plants and allowing developers to sell unscheduled power due to curtailment because of technical constraints, directly on exchanges. It also specified rules to simplify the process of recovery of costs incurred by Developers due to Change in Law post project bidding. The rules provide for pre-defined formula to determine the onetime charges or impact on tariffs due to Change in Law and lays down fixed time period for approvals. These are big developments that are aptly timed and addresses issues that have been in discussions lately.

Government is also actively working on enhancing transmission capacity in the country. Ministry of Power recently notified rules that paves the way for overhauling of transmission system planning and provides for easier access to transmission network across the country, termed as General Network Access in the ISTS system. This provides flexibility to the States as well as the generating stations to acquire, hold and transfer transmission capacity as per their requirements. In addition, Net Zero and RE100 announcements by Corporates is driving a resurgence in interest in Energy Transition through round-the-clock RE contracts.

On our organizational update, as you all know, around the end of this quarter, Mr. Alan Rosling joined our Board as the new Chairman and replaced Mr. Barney Rush, who served as Director on the Board for 6 years, including last 2 years as Chairman. We were privileged to have worked with Barney Rush on the Board. We express our gratitude to Barney for his leadership and guidance in strengthening Azure Power. Mr. Rosling brings an inspiring mix of great leadership and hands on industry experience himself and we at Azure management are already deeply working with him in taking our company towards greater accomplishments together.

We continue to look for suggestions from our investors and stakeholders on how we can further improve our disclosures and make it easier for you to understand and value our business.

With that, I would like to turn it over to Murali.

Murali Subramanian
Thank you Ranjit.

As we last reported, the second wave of COVID impacted construction activities at our sites. Subsequently however, both Covid and the supply situation improved significantly. Our Construction and Procurement teams worked very hard to ensure we adhere to committed timelines on our projects.

We commissioned 158 MW AC and 188 MW DC capacities during the quarter. As of today, we have completed and commissioned 500 MW out of 600 MW in our Rajasthan 6 project, and balance 100 MW to be commissioned in this month. We also commissioned 150 MW in our Rajasthan 8 project subsequent to quarter end and are in advanced stages to commission balance capacities in the project in the current quarter. Even though construction work on 300 MW Rajasthan – 9 was impacted due to supply related challenges but the team has rallied, and we are confident that we will meet the promised timelines.

We have provided some highlights of our ESG accomplishments on page 6. As Ranjit mentioned earlier, we are extremely proud to adopt our EV policy this quarter which provides a direction towards reducing our Scope 1 emissions. We have committed to shift to 100% EV by 2030 under the policy. Further, to encourage adoption of EV at personal level, we are providing interest cost subsidy to our staff and am happy to report that we have already seen 2 EVs purchased by the company and 1 EV by our staff since adoption. We are hopeful that this policy will prove to be useful in expeditious transition to EV. We also obtained Carbon Neutrality status through offsetting of carbon emissions in our operations and together with our path towards EV, we hope to reduce that requirement in coming years.

I am happy to report we have also recently won the Greentech Effective Safety Culture Award for 2021 from Greentech Foundation and OHS Award from Grow Care India in these areas, which signifies the efforts we have put in to ensure safety culture is embedded across our project locations and sites. Further, we also successfully completed surveillance audits for our ISO 9001 and ISO 14001 certification, signifying our continuous focus and improvement on our quality and environment management systems.

Our carbon free generation has avoided about 0.9 million tons of CO_2 equivalent this quarter, bringing the total to 11.5 million tons equivalent since inception. We remain net carbon neutral. We are in process of planting 30,000 trees in the immediate vicinity of our 600 MW Rajasthan 6 project site during this year. We have committed to plant 50 trees for every MW we construct. We also remain actively engaged with the communities where we operate and provide pro-active support towards medical and health facilities especially on the pandemic front.

We have also constituted a new Sustainability Committee of the Board to continuously strive to implement and monitor best practices to enhance our sustainability efforts.

On the technology front, Azure continues to be an early adopter: we were among the first companies in India to install a large-scale project based on monoperc panels, and we are also constructing a large scale project using bifacial tracker technology where we are expecting yields in excess of 30% for our Rajasthan 9 project. These are industry leading efforts to ensure our projects are built and operated with the best returns metrics.

Further on operations side, all our projects are now fully connected with our central monitoring system which has accessibility through mobile app as well. We are phasing out laptops at our sites and have provided tablets to our site engineers who are always connected with the Head Office staff and monitor granular level performance of each of our plants on real time basis. This also helps us in predictive monitoring of our plants to tackle any challenge in its infancy.

Looking at industry and regulatory updates on page 8, India’s big announcements at COP26 and the fact that we recently reached 150 GW installed renewable energy capacity continues to ensure solid environment filled with growth opportunities in India.

As we discussed during our previous call, we have developed organizational capabilities to implement our plans in wind and hybrid space. Our recent wins in this regard, the 120 MW Wind project and 150 MW Hybrid project, both with SECI, provides us an opportunity to kick start this process of diversifying our portfolio and move line with the industry which is increasingly looking at dispatchable power as the sustainable way forward in Indian RE. We want to assure you again that we shall only bid for projects at commercially viable tariffs, one which provide returns above our cost of capital.

With that, I will turn it over to Pawan to discuss the quarterly results.

Pawan Kumar Agrawal

Thank you Murali.

I am happy to report that, we have exceeded upper end of our revenue guidance for this quarter, with revenues, excluding rooftop, at USD 56.9 Mn against the guidance range of USD 49 to 51.7 million.

We saw significant contribution from sale of our carbon credits this quarter, amounting to USD 5.5 Mn. However, even after excluding this contribution, the revenue is at the upper end of the guidance range.

Significant developments during the quarter, and in the period subsequent to the quarter end, have assured all of us, of the tremendous opportunities in the sector, that we, at Azure, are well placed to leverage.

Ours is a simple business, that needs strong and impeccable execution, which we have been focusing at. Our first PPA execution, under the 4 GW project, is one such example, for which we have been working hard with SECI and other stakeholders. With these projects in motion, I believe we have widened the road for our stakeholders on value accretion.

Turning to page 12, as of September 30, 2021, we were operating 2,210 Megawatts on a PPA or AC basis, which is 31% higher than what we were operating a year before. Our portfolio was stable at 6,955 MWs at the quarter end, which further increased to 7,225 MW subsequent to the quarter end with our recent wins.

While these portfolio MW numbers excludes rooftop portfolio, which is in the process of getting transferred to Radiance, our financial numbers continue to consolidate rooftop, till the transfer process is completed.

On page 13, after adjusting primarily for stock compensation expense, our EBITDA has been $48.7 mn, or 29% higher, against 25% increase in revenues, from the same quarter in the prior year. Turning to G&A, on page 13, our G&A increased by 6% in line with our expectation we communicated earlier.

All our recent refinancing, both domestic as well as overseas, have resulted in substantial savings in interest costs for us, improving our equity returns. Over 70% of our project debt at present, including our outstanding bonds, have fixed interest rates period of at least 2-3 years. As we refinance our project debt on completion of new projects this year, we will endeavor to have almost 100% of project debt to be under fixed rates. Refinancing at lower costs and fixed rates reflects strong credit profile of the group, supported by strong sponsors such as CDPQ and OMERS.

Further, we expect that India may not see much impact from global interest rate increase apprehensions in a longer term. As India progresses economically, and with events like India's sovereign debt inclusion in global bond indices, we expect India to significantly gain from long term inflow of global capital, much larger than previous years, which may be expected keep the rates in check.

Turning to stock compensation expenses, for 2Q'22, our share price decreased from US$ 26.92 as on June 30, 2021 to US$ 22.00 as on September 30, 2021, resulting in reversal of SAR expense of US$ 3.3 million.

Despite challenges in past few quarters, our DSO has been fairly consistent at around 116 days on an average in recent quarters. We believe there will be further improvement in the future, with commissioning of projects with high credit worthy counterparties, and expected improvement in collections due to favorable awards in Karnataka. We are also hopeful of a favorable judgement soon in Andhra Pradesh.

On page 15, you can see that EBITDA from operating assets increased by about 28% YoY and that Cash Flow to equity from operating assets rose about 32%.

Net debt for operating assets was about $1.2 Billion and EBITDA for the last 12 months was about $194 million resulting in a Net Debt/EBITDA ratio for operating assets of 6.2x as on September 30, 2021.

Finally looking at page 16, providing balance sheet information, we had about USD 128.3 million of cash and cash equivalents, and our Net Debt stood at approximately USD 1.41bn. As a reminder, the hedging assets of USD 17.2 million included in Other Assets on our balance sheet, should be netted against our total debt, as this is directly linked to the foreign exchange hedges we put in place related to our Green Bonds.

During the current quarter, we have used part of this asset related to our first green bond to reduce the leverage on the green bonds at the time of refinancing.

Now, I pass on to Ranjit to provide some commentary on our guidance.

Ranjit Gupta

Thanks Pawan. We have achieved significant results this quarter despite all the challenges we have been through in this year in terms of physical disruptions. We are happy to report that we have been able to achieve higher revenue compared to our guidance for this quarter.

We would reiterate here our numbers for the current fiscal, and will keep the markets posted, in our coming updates. For 3Q 22, we expect the revenue to be between INR 4,100 and 4,300 million and the PLF to be between 19.5% to 20.5%.

With this, we will be happy to take questions.

QUESTIONS AND ANSWERS