

June 28, 2023^(Revised)

Tamil Nadu Generation and Distribution Corporation Ltd: Rating reaffirmed

Summary of rating action

| Instrument* | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action |
|--------------------------------|--------------------------------------|-------------------------------------|------------------------------------|
| Non-convertible bond programme | 3,335.80 | 3,335.80 | [ICRA]A- (CE) (Stable); reaffirmed |
| Total | 3,335.80 | 3,335.80 | |

*Instrument details are provided in Annexure-1

| | |
|--|----------|
| Rating Without Explicit Credit Enhancement | [ICRA]BB |
|--|----------|

Note: The (CE) suffix mentioned alongside the rating symbol indicates that the rated instrument/facility is backed by some form of explicit credit enhancement. This rating is specific to the rated instrument/facility, its terms and its structure and does not represent ICRA's opinion on the general credit quality of the entity concerned. The last row in the table above also captures ICRA's opinion on the rating without factoring in the explicit credit enhancement

Rationale

The rating of Tamil Nadu Generation and Distribution Corporation Limited (TANGEDCO/the entity) is based on the strength of the unconditional and irrevocable guarantee extended by the Government of Tamil Nadu (GoTN) to the rated instrument over its entire tenure. The Stable outlook on this rating reflects ICRA's outlook on the rating of the guarantor, GoTN.

Adequacy of credit enhancement

The rating of the instrument is based on the credit substitution approach whereby the rating of the guarantor has been translated to the rating of the said instrument. The guarantee is legally enforceable, irrevocable, unconditional, covers the entire amount and tenure of the rated instrument and has a well-defined invocation and payment mechanism. Given these attributes, the guarantee provided by GoTN is adequately strong to result in an enhancement in the rating of the said instrument to [ICRA]A-(CE) against the rating of [ICRA]BB without explicit credit enhancement. In case the rating of the guarantor was to undergo a change in future, the same would reflect in the rating of the aforesaid instrument as well.

Salient covenants of the rated facility

- » TANGEDCO has opened an escrow account (in nature of trust and retention account) with the designated bank and shall credit the adequate funds in the escrow account for servicing the bondholders at least five working days prior to the service date (T) for the payment of principal and/or interest. In case TANGEDCO does not deposit the sufficient funds in the escrow account, at least five working days prior to the forthcoming due date (T-5), or put them in investments (investments in highest rated debt instruments or deposits of banks, which are rated AA for long term or A1+ for short term by ICRA, and are further lien to the trustee or bondholders with a maturity date of T-1 working day), TANGEDCO shall intimate in writing to the Deputy Secretary of Government (Budget/Finance) and/or designated official of GoTN, with a copy to the trustee and ICRA, indicating the forthcoming service date (T), amount payable to the bondholder as interest and /or principal on the said date and also request GoTN to ensure that adequate funds are available in the escrow account for servicing the bondholders on the forthcoming due date
- » Notwithstanding the obligation of TANGEDCO to intimate GoTN and the trustee about the clear fund balance in the escrow account, 45 working days prior to the service date (T), the trustee shall send notices to the Finance Secretary and/or designated official of GoTN and TANGEDCO, with a copy to ICRA, indicating the forthcoming service date (T), amount payable to the bondholders as interest and /or principal on the said date and also request GoTN to ensure that adequate funds are available in the escrow account for servicing the bondholders as per the payment mechanism

- » *The trustee will monitor the balance in the escrow account, including invested funds at 30, 15 and 5 working days prior to every service date (T) for the payment of interest and /or principal. In the event the balance in the designated account, after taking into account the invested funds as provided, are inadequate, by (T-5) working days, the trustee shall forthwith invoke the guarantee issued by GoTN*

The rating without credit enhancement of [ICRA]BB factors in the weak financial profile of TANGEDCO, with continued losses owing to the inadequate tariffs in relation to the cost of supply due to the significant lag in tariff order issuance and subdued utilisation of its generation assets. The large cash losses and significant reliance on external borrowings have resulted in a highly leveraged capital structure and weak debt protection metrics. While the approved tariff hike, as per the latest tariff order issued in September 2022, is expected to substantially reduce the losses at the PAT level in FY2023, any further improvement from FY2024 onwards would be subject to subsequent tariff hikes commensurate with the movement of power purchase costs. Further, the liquidation plan for the regulatory assets recognised in the tariff order would also determine the financial position of the discom in the upcoming years.

Further, ICRA takes note of the default for six days for an amount of Rs. 49.31 lakh of principal due on the loan availed from Tamil Nadu Power Finance and Infrastructure Development Corporation Limited (TNPFC) in FY2022 with the dues being paid subsequently, as mentioned by the auditor in the annual report. This does not impact ICRA's rating on TANGEDCO's bond programme, as it backed by a guarantee from GoTN.

Key rating drivers and their description

Credit strengths

State ownership and support - TANGEDCO came into existence following the debundling of the erstwhile Tamil Nadu Electricity Board (TNEB) in 2010. It is responsible for the generation and distribution of power in Tamil Nadu and is strategically important to the state power sector. It is held entirely by the GoTN, which has supported the distribution company (discom) through regular infusion of funds in the form of equity/interest-free unsecured loans/loss funding support. The rated bond programme is supported by an unconditional and irrevocable guarantee provided by GoTN towards debt servicing.

Improving operating efficiency – The AT&C losses (including open access wheeling) has improved to 11.91% in FY2022 from 12.09% in FY2021 and 12.39% in FY2020. The improving operating efficiency would reduce the quantum of power required to meet the demand. However, the sustainability of the improvement needs to be observed.

Credit challenges

Issuance of tariff orders with a considerable lag – The tariff order for the control period from FY2023 to FY2027 for TANGEDCO was issued in September 2022. This order came with a significant lag after the earlier tariff order had been issued in August 2017. As a result, the tariff rates have been inadequate to cover for the rising power purchase costs. This, compounded with rising overheads, increase in employee costs and financial expenses, has resulted in continued losses for the company. Going forward, annual hikes in the tariff rates in line with the cost of supply remains crucial to improve its profitability.

High financial risk profile – The financial profile of TANGEDCO, on a standalone basis, remains weak as it continues to incur substantial losses owing to the inadequate tariff rates, subdued utilisation of its generation assets and the high cost of power purchase. Sizeable cash losses and significant reliance on external borrowings have resulted in a highly leveraged capital structure (debt to OPBDITA of 65x in FY2022) and weak debt protection metrics. The borrowing levels have also increased significantly over the last three years to Rs. 1,55,381 crore (PY: Rs. 1,45,322 crore) as on March 31, 2022. The approved tariff hike, as per the latest tariff order issued in September 2022, is expected to substantially reduce the losses at the PAT level in FY2023. However, any further improvement from FY2024 onwards would be subject to subsequent tariff hikes commensurate with the movement of power purchase costs. Further, the liquidation plan for the regulatory assets recognised in the tariff order would also determine the financial position of the discom in the upcoming years.

Key rating drivers and their description (Guarantor)

Credit strengths

Healthy socio-economic indicators – The state’s performance on various socio-economic and demographic indicators, such as per-capita income (Rs. 2,41,131 in FY2022), literacy rate (80.3% in 2011), urbanisation rate (48.5% in 2011) and poverty rate (22.4% in 2012), was favourable compared to the respective national averages (Rs. 1,48,524 per capita income, 74.0% literacy rate, 31.2% urbanisation rate and 29.5% poverty rate)

Moderate self-reliance – Around 53% of the Government of Tamil Nadu’s (GoTN’s) revenue expenditure was covered through own revenues during FY2020-2022, higher than some states, indicating moderately healthy self-reliance.

Credit challenges

Committed expenditure and spending on key subsidies dominate revenue expenditure – During FY2020-2022, around 60% of the GoTN’s revenue spending has been on committed expenditure, and food and power subsidies, which is higher than some states. Such spending has contributed to the large revenue deficits of the GoTN in recent years.

Unfavourable quality of expenditure – The GoTN’s quality of expenditure (capital expenditure as a proportion of total expenditure) remained around 12% during FY2020-2022, lower than many states.

Rising leverage levels (debt¹+guarantees) – Reflecting the sustained fiscal deficits and support extended to the power sector, the GoTN’s leverage levels (excluding GST compensation loans) have deteriorated to 31.5% of GSDP in FY2022 from 23.7% of GSDP FY2018.

Liquidity position

For the [ICRA]A-(CE) (Stable) rating: Adequate

The GoTN has not availed the ways and means advances (WMA) and overdraft (OD) facilities from the RBI during FY2016 to FY2023. Additionally, the GoTN had an investment of Rs. 2,396 crore in auction treasury-bills and Rs. 18 crore in government securities at end-March 2023. Based on these indicators, the liquidity position of the state government can be inferred to be adequate during the recent years.

For the [ICRA]BB rating: Stretched

The liquidity position of TANGDECO is stretched due to continued losses along with high repayment obligations and capex plans. However, the GoTN’s continued support backs the liquidity profile to some extent. The GoTN has also provided unconditional and irrevocable guarantee to the rated instrument over its entire tenure.

Rating sensitivities

For the [ICRA]A-(CE) (Stable) rating

The rating assigned to the Rs. 3,335.8-crore non-convertible bond programme of TANGDECO would remain sensitive to any movement in the rating or outlook of the guarantor, i.e. GoTN.

¹ Includes internal debt, loans from the Centre, provident fund etc.

Analytical approach

| Analytical Approach | Comments |
|---------------------------------|--|
| Applicable rating methodologies | Corporate Credit Rating Methodology Rating Methodology for Power Distribution Utilities Explicit third-party support |
| Parent/Group support | The rated facilities of TANGEDCO are backed by an unconditional and irrevocable guarantee from the GoTN |
| Consolidation/Standalone | The rating is based on the standalone financial profile of the company |

About the company

Under the reorganisation and transfer scheme of TNEB under the Tamil Nadu Electricity (Reorganization and Reforms) Transfer Scheme 2010 issued by the GoTN with effect from November 1, 2010, TNEB has been reorganised into TNEB Limited (the holding company), Tamil Nadu Generation and Distribution Corporation Limited (TANGEDCO) and Tamil Nadu Transmission Corporation Limited (TANTRANSCO). TANGEDCO is engaged in the business of generation and distribution of power in the entire state of Tamil Nadu as a regulated monopoly. As on March 31, 2022, TANGEDCO had an installed capacity of about 7,175 MW, which largely consisted of thermal power plants (~60%) and hydel capacity (~30%) apart from gas-based capacity and a few windmills. TANGEDCO also sources a significant portion of its requirement from central power sector utilities, such as National Thermal Power Corporation Limited (NTPC), Neyveli Lignite Corporation Limited (NLCIL) and Nuclear Power Corporation of India Limited (NPCIL), besides independent power producers in the state. Other sources from where power is purchased include captive generating units, co-generation units and windmills.

About the guarantor - GoTN

The GoTN's revenue receipts as a proportion of the state's GSDP have declined to 10.0% in FY2022 from 10.7% in FY2017, led by the state's own tax revenues (SOTR), state-owned non-tax revenues (SONTR) and Central tax devolution. However, during this period, the grants from the Centre relative to GSDP increased on account of the GST compensation grants.

The GoTN's revenue expenditure increased to 12.2% of GSDP in FY2022 from 11.7% of GSDP in FY2017, largely led by an increase in interest payments. Reflecting these trends, the GoTN's revenue deficit has more than doubled to 2.3% of GSDP in FY2022 from 1.0% of GSDP in FY2017. With low capital spending of 1.2-1.7% of GSDP during FY2017-FY2022, the GoTN was able to curtail its fiscal deficit below the FC-targets in four out of these six years. With the sustained fiscal deficits and support extended to the power sector, the GoTN's leverage level (excluding GST compensation loans) worsened to 31.5% of GSDP in FY2022 from 23.1% in FY2017.

In the Budget Estimate (BE) for FY2024, the GoTN has forecast its revenue deficit to widen to Rs. 37,540 crore from Rs. 30,476 crore in the revised estimates (RE) for FY2023. With a 24.0% expansion in capital expenditure, the GoTN's fiscal deficit is budgeted to rise to Rs. 92,075 crore in FY2024 BE from Rs. 74,525 crore in FY2023 RE. As per the Medium-Term Fiscal Plan statement, the GoTN's fiscal deficit in FY2023 RE and FY2024 BE would remain under the net borrowing limit recommended by the 15th Finance Commission for these years.

ICRA would analyse the GoTN's provisional actuals for FY2024 to assess the performance of their key fiscal indicators relative to FY2023 BE. The financial health of the GoTN's power sector entities and their impact on the state's finances would continue to be a key monitorable.

Key financial indicators (audited)

| TANGEDCO Standalone | FY2021 | FY2022 |
|--|-----------|-----------|
| Operating income (Rs. crore) | 63,388.5 | 70,447.4 |
| PAT (Rs. crore) | -13,407.3 | -11,954.6 |
| OPBDIT/OI (%) | 0.4% | 3.4% |
| PAT/OI (%) | -21.2% | -17.0% |
| Total outside liabilities/Tangible net worth (times) | -3.2 | -3.1 |
| Total debt/OPBDIT (times) | 594.1 | 65.4 |
| Interest coverage (times) | 0.02 | 0.21 |

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation

Key financial indicators of GoTN

| | FY2022 | FY2023 RE | FY2024 BE |
|------------------------------|----------|-----------|-----------|
| Revenue receipts* | 2,05,957 | 2,44,160 | 2,68,866 |
| Revenue expenditure* | 2,52,495 | 2,74,636 | 3,06,406 |
| Revenue balance | -46,538 | -30,476 | -37,540 |
| Capital outlay & net lending | 35,297 | 44,049 | 54,534 |
| Fiscal balance | -81,835 | -74,525 | -92,075 |

Note: Amounts in Rs. crore; * Adjusted for double entries of interest on loans of department commercial undertakings (DCUs)

Source: State Budget; Finance Accounts and ICRA Research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

| Instrument | Type | Current rating (FY2024) | | Chronology of rating history for the past 3 years | | | |
|------------|-----------|--------------------------|---|---|-------------------------|-----------------------------------|-------------------------|
| | | Amount rated (Rs. crore) | Amount outstanding as on Mar 31, 2023 (Rs. crore) | Date & rating | Date & rating in FY2023 | Date & rating in FY2022 | Date & rating in FY2021 |
| | | | | Jun 28, 2023 | Jun 29, 2022 | Jun 30, 2021 | Jun 29, 2020 |
| 1 Bonds | Long-Term | 3,335.80 | 2,216.93 | [ICRA]A- (CE) (Stable) | [ICRA]A- (CE) (Stable) | [ICRA]A- (CE) (Stable) | [ICRA]A- (CE) (Stable) |
| 2 Bonds | Long-Term | 80.70 | -- | -- | -- | [ICRA]A- (CE) (Stable); withdrawn | [ICRA]A- (CE) (Stable) |

Complexity level of the rated instruments

| Instrument | Complexity Indicator |
|------------|----------------------|
| Bonds | Simple |

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or

complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: [Click Here](#)

Annexure I: Instrument details

| ISIN | Instrument Name | Date of Issuance | Coupon Rate | Maturity | Amount Rated (Rs. crore) | Current Rating and Outlook |
|--------------|-----------------|------------------|-------------|--|--------------------------|----------------------------|
| INE340M08111 | Bonds | February 2014 | 10.50% | 30% - Feb 2022 30% - Feb 2023 40% - Feb 2024 | 633.50 | [ICRA]A- (CE) (Stable) |
| INE340M08129 | Bonds | June 2014 | 9.72% | 30% - Jul 2022 30% - Jul 2023 40% - Jul 2024 | 1000.00 | [ICRA]A- (CE) (Stable) |
| INE340M08137 | Bonds | December 2014 | 9.20% | 30% - Dec 2022 30% - Dec 2023 40% - Dec 2024 | 1000.00 | [ICRA]A- (CE) (Stable) |
| INE340M08145 | Bonds | May 2015 | 9.00% | 30% - Jun 2023 30% - Jun 2024 40% - Jun 2025 | 501.80 | [ICRA]A- (CE) (Stable) |
| INE340M08152 | Bonds | February 2016 | 10.00% | 30% - Feb 2024 30% - Feb 2025 40% - Feb 2026 | 50.00 | [ICRA]A- (CE) (Stable) |
| INE340M08160 | Bonds | December 2016 | 9.70% | 30% - Dec 2024 30% - Dec 2025 40% - Dec 2026 | 40.00 | [ICRA]A- (CE) (Stable) |
| INE340M08178 | Bonds | March 2017 | 9.25% | 30% - Mar 2025 30% - Mar 2026 40% - Mar 2027 | 73.10 | [ICRA]A- (CE) (Stable) |
| Not placed | Bonds | - | - | - | 37.40 | [ICRA]A- (CE) (Stable) |

Source: Company

Annexure II: List of entities considered for consolidated analysis

Not Applicable

Corrigendum

Rationale dated June 28, 2023 has been corrected with the revision as detailed below:

- In Annexure I, the issuance dates of three bonds (ISINs: INE340M08111, INE340M08129 and INE340M08152) have been corrected to February 2014, June 2014 and February 2016 from January 2014, May 2014 and January 2016 respectively

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