

November 22, 2019

Tamil Nadu Generation and Distribution Corporation Ltd: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-Convertible Bonds Programme	3335.8	3335.8	[ICRA]A-(CE) (Stable); reaffirmed
Non-Convertible Bonds Programme	80.7	80.7	[ICRA]A-(CE) (Stable); reaffirmed
Total	3416.5	3416.5	

*Instrument details are provided in Annexure-1

Rating Without Explicit Credit Enhancement	[ICRA]BB+
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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 above 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 related to the credit enhancement, as specified in the guaranteed documents

- » 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 5 working days prior to the service date (T), for payment of principal and/or interest. In case TANGEDCO does not deposit the sufficient funds into the escrow account, at least 5 working days prior to forthcoming due date (T-5) or put them in investments (deposits of Banks or investments in highest rated debt instruments which are rated AAA for long-term or A1+ for short-term by ICRA and are further lien to the Trustee or bond holders 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 bond holder 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 Government of Tamil Nadu 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, the Trustee shall send further notices to GoTN and TANGEDCO.

Key rating drivers and their description

Key Strengths

State ownership and support – TANGEDCO came into existence post the debundling of the erstwhile TNEB in 2010. It is responsible for 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 discom through regular infusion of funds in the form of equity or interest-free unsecured loans. The rated bond programmes are also supported by an unconditional and irrevocable guarantee provided by GoTN towards debt servicing.

Credit Weaknesses

High financial risk profile of TANGEDCO on standalone basis – Financial profile of TANGEDCO remains weak as it continues to incur substantial losses owing to the inadequate tariff rates, low capacity addition/utilisation over the years, moderately weak operational efficiency and the high cost of power purchase. Over the last three years (FY2016-FY2018), with the decline in contribution from own generating stations because of low capacity addition and weak generation parameters, the average cost of supply had increased substantially owing to the increased external power purchase outside the long-term PPAs. In terms of operational performance, even though the AT&C loss levels are relatively low compared to other discoms, the loss levels have remained higher than the benchmark. During FY2018, AT&C loss levels had increased due to decline in collection efficiency to 97.8% from 100.0% in FY2017, majorly due to delay in receipt of Government dues. This apart, the billing efficiency of TANGEDCO continues to remain low due to the loss levels.

Sizeable cash losses and significant reliance on external borrowings have resulted in a highly leveraged capital structure and weak debt protection metrics. The discom had reported cash losses of Rs. 5,503 crore in FY2018, which has increased further in FY2019, owing to the continuing gap between tariff income and revenue expenses. The gap between Average Cost of Supply and Average Rate of Realisation (ACS-ARR gap), has increased despite the rising subsidies over the years. The borrowing levels have also increased significantly over the last two years to about ~Rs. 1,20,000 crore as on March 31, 2019, which include loans of Rs. 88,999 crore from banks and financial institutions. TANGEDCO is currently in the process of submitting a tariff revision petition with TNERC, which upon approval, is expected to improve the

financial profile. TANGEDCO's ability to increase the tariff rates and maintain the cost of supply remains crucial to improve the return indicators and ICRA would continue to monitor the developments related to this.

Key rating drivers and their description (Guarantor)

Credit Strengths

Healthy socio-economic indicators: The state's performance on various socio-economic and demographic indicators¹, such as per-capita income (Rs. 1,66,934 in FY2018), literacy rate (80.3% in 2011), urbanization rate (48.5% in 2011) and poverty rate (22.4% in 2012) was favourable compared to the respective national averages (Rs. 1,14,958, 74.0%, 31.2% and 29.5%).

Self-reliant revenue structure: Nearly 62.0% of the Government of Tamil Nadu's (GoTN's) revenue expenditure² was covered through its own revenues (state own tax revenues or SOTR, and state own non-tax revenues or SONTR) in FY2018, indicating a healthy level of self-reliance.

Fiscal deficit within Finance Commission (FC) norms: The state has been able to curtail its fiscal deficit below the FC-recommended cap of 3.0% of gross state domestic product (GSDP) during FY2016 to FY2020 (based on the budget estimates or BE).

Credit Weaknesses

Decline in own tax effort: Following single-digit SOTR growth from FY2014 to FY2018, the GoTN's own tax revenues fell from 8.3% of GSDP in FY2013 to 6.4% of GSDP in FY2018, with the latter lower than the average of 6.7% for all 29 states³.

Substantial subsidy and welfare spending: The GoTN spends a considerable amount on subsidies (especially towards food and power) and welfare schemes, which appropriated a substantial 16.6% of the revenue receipts of the state in FY2018. However, the same is expected to decline to 13.4% in FY2019 revised estimates (RE) and further to 12.8% in FY2020 BE.

Sustained revenue deficits: The GoTN has recorded sustained revenue deficits since FY2014. While the size of the same increased from 0.2% of GSDP in FY2014 to 1.5% of GSDP in FY2018, it is expected to moderate to an estimated 0.8% of GSDP in FY2020 BE.

Rise in leverage levels (debt⁴+guarantees): Reflecting the sustained fiscal deficits and support extended to the power sector, the GoTN's leverage levels have deteriorated to 23.7% of GSDP or 3.7x SOTR in FY2018 from 21.0% of GSDP or 2.8x SOTR in FY2014.

¹ Source: Central Statistical Office (CSO), Census of India and Rangarajan Committee poverty estimates

² Revenue receipts and expenditure adjusted for double entries of interest from departmental commercial undertakings

³ Source: Reserve Bank of India (RBI) and CSO

⁴ Includes internal debt, loans from the Centre, provident fund etc

Liquidity position of GoTN (Guarantor): Adequate

The GoTN has not availed the Ways and Means Advances and/or the Overdraft facilities from the RBI during FY2018 and FY2020 (till September 2019). Moreover, the GoTN had a balance of Rs. 13,833 crore invested in the auction treasury-bills as on end September 2019. Based on the aforementioned indicators, the liquidity position of the state government can be inferred to be adequate during the recent times.

Rating sensitivities

The rating assigned to the Rs. 80.7-crore and the Rs. 3335.8-crore Non-Convertible Bonds Programmes of TANGEDCO would remain sensitive to any movement in the rating or outlook of the guarantor, i.e. GoTN.

Rating sensitivities (for GoTN)

Positive triggers: Sustained improvement in the revenue profile of the state government.

Negative triggers: Negative pressure on the ratings of GoTN could arise if the macroeconomic scenario adversely impacts the pace of growth of the tax revenues of the GoTN, both its own and the share in Central taxes. Impact of additional welfare schemes or increase in subsidy, including power and food spending, on the state government's overall fiscal health and leverage levels will also pressure the rating.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Power Distribution Utilities Approach for rating debt instruments backed by third-party explicit support
Parent/Group Support	The rated facilities of TANGEDCO are backed by an unconditional and irrevocable guarantee from the GoTN
Consolidation/Standalone	Standalone

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 Government of Tamil Nadu (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 the largest utility in the country in terms of number of consumers and one of the top few state utilities in terms of energy sales. As on March 31, 2019, TANGEDCO had an installed capacity of about 7,161 MW, which largely consisted of thermal power plants (~60%) and hydel capacity (~30%) apart from gas-based capacity and few windmills. TANGEDCO also sources a significant portion of its requirement from central power sector utilities such as National Thermal Power Corporation Limited, Neyveli Lignite Corporation Limited and Nuclear Power Corporation of India Limited besides independent power producers in the state. Other sources from where power is purchased include captive generating units, co-generation units and wind mills.

About the guarantor: Government of Tamil Nadu's Finances

TN is one of the more industrialised states in India and performs favourably on various socio-economic indicators compared to several other states.

The composition of the GoTN's revenue receipts is healthy, with a substantial three-fourth coming from its own revenue receipts, and a moderate one-fourth from central transfers. The state's revenue expenditure profile is characterised by substantial subsidy and welfare spending, along with a moderate committed expenditure. The GoTN's capital spending has traditionally been dominated by sectors such as transport, power and water supply, sanitation, housing and urban development.

The GoTN forecasts the pace of growth of its revenue receipts to ease considerably to 9.5% in the BE (budget estimate) for FY2020 from the high 23.8% in the RE (revised estimate) for FY2019, led by grants from the Centre (to 2.0% from 71.0%) and SOTR (to 13.3% from 17.5%). Moreover, the growth of its revenue spending is budgeted to ease to 6.1% in FY2020 from 19.3% in FY2019 RE; the latter was partly boosted by the full year impact of the revision in pay scales. In line with these trends, the GoTN expects its revenue deficit to narrow to Rs. 14,315 crore in FY2020 BE from Rs. 19,319 crore in FY2019 RE (refer Exhibit 1). The Medium-Term Fiscal Plan published by the GoTN along with its FY2020 Budget projected the fiscal deficit to remain below the cap of 3.0% of GSDP in both FY2019 RE and FY2020 BE. Reflecting the sustained fiscal deficits and the support extended to the power sector, the GoTN's leverage level worsened to 23.7% of GSDP in FY2018 from 23.1% of GSDP in FY2017.

ICRA shall take note of the impact of the evolving trends in Government of India's tax collections, which could be negatively impacted by the cut in corporate tax rates and the overall slowdown in economic growth, on the Central tax devolution to the GoTN, its overall revenue receipts and fiscal balances. In addition, ICRA shall observe the impact of any additional welfare spending on various fiscal indicators and the overall credit profile of the state government.

Key financial indicators - TANGEDCO (audited) (Amounts in Rs. crore)

	FY2017	FY2018
Operating Income (Rs. crore)	43,964	43,687
PAT (Rs. crore)	-6,142	-7,583
OPBDIT/OI (%)	8.8%	4.0%
Total Debt/ TNW (times)	-2.6	-2.4
Total Debt/OPBDIT (times)	25.3	61.9
Interest Coverage (times)	0.5	0.2

Key fiscal indicators of the GoTN (Amounts in Rs. crore)

	FY2018	FY2019 RE	FY2020 BE
Revenue			
Revenue Receipts	1,45,238	1,79,743	1,96,845
State's Own Tax Revenue	93,737	1,10,178	1,24,813
State's Own Non-Tax Revenue	9,722	13,824	12,451
Share in Central Taxes	27,100	30,639	33,978
Grants from Centre	14,679	25,102	25,603
Capital Receipts	2	-	-
Expenditure			
Revenue Expenditure	1,66,832	1,99,062	2,11,160
Capital Outlay	20,203	26,192	31,251
Net Lending	-1,955	9	-1,390
Revenue & Fiscal Balance			
Revenue Balance	-21,594	-19,319	-14,315
Fiscal Balance	-39,840	-45,520	-44,176
Leverage			
Debt	3,10,429	3,54,496	3,97,496
Guarantees	36,131	-	-

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	Amount Rated (Rs. crore)	Amount Outstanding (Rs. Crore)	Current Rating	Chronology of Rating History for the past 3 years										
					Month-year & Rating in FY 2019					Month-year & Rating in FY 2018				Month-year & Rating in FY2017	
					22-Nov 2019	14-Feb 2019	01-Feb 2019	08-Oct 2018	07-Jun 2018	07-Feb 2018	29-Mar '17	11-Jan 2017	15-Nov 2016	25-May 2016	
1	Bonds	150.0	-		Withdrawn	Provisional [ICRA]BBB + (SO) (Stable)	Provisional [ICRA]BBB + (SO) (Stable)	Provisional [ICRA]BBB + (SO) (Stable)	Provisional [ICRA]BBB + (SO) (Stable)	Provisional [ICRA]BBB + (SO) (Stable)	-	-	-	-	
2	Bonds	3,335.8	3,298.9	[ICRA]A- (CE) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) – 2633.5	
											Provisional [ICRA]A- (SO) (Stable) – 50.5	Provisional [ICRA]A- (SO) (Stable) – 150.5	Provisional [ICRA]A- (SO) (Stable) – 702.3		
3	Bonds	80.7	32.3	[ICRA]A- (CE) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	[ICRA]A- (SO) (Stable)	

4	Bonds	Long Term	530.9	-	-	-	-	-	Withdrawn	[ICRA] A- (SO) (Stable)	[ICRA] A- (SO) (Stable)	[ICRA] A- (SO) (Stable)	[ICRA] A- (SO) (Stable)	[ICRA] A- (SO) (Stable)
5	Bonds	Long Term	400.0	-	-	-	-	-	Withdrawn	[ICRA] A- (SO) (Stable)	[ICRA] A- (SO) (Stable)	[ICRA] A- (SO) (Stable)	[ICRA] A- (SO) (Stable)	[ICRA] A- (SO) (Stable)

Amount in Rs. crore

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE340M09010	Bonds	Jan 2011	8.65%	20% - Feb 2017, 20% - Feb 2018, 20% - Feb 2019, 20% - Feb 2020, 20% - Feb 2021	80.70	[ICRA]A- (CE) (Stable)
INE340M08111	Bonds	Jan 2014	10.50%	30% - Feb 2022, 30% - Feb 2023, 40% - Feb 2024	633.50*	[ICRA]A- (CE) (Stable)
INE340M08129	Bonds	July 2014	9.72%	30% - July 2022, 30% - July 2023, 40% - July 2024	1000.00*	[ICRA]A- (CE) (Stable)
INE340M08137	Bonds	Dec 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	Jan 2016	10.00%	30% - Feb 2024, 30% - Feb 2025, 40% - Feb 2026	50.00*	[ICRA]A- (CE) (Stable)
INE340M08160	Bonds	Dec 2016	9.70%	30% - Dec 2024, 30% - Dec 2025, 40% - Dec 2026	40.00*	[ICRA]A- (CE) (Stable)
INE340M08178	Bonds	Mar 2017	9.25%	30% - Mar 2025, 30% - Mar 2026, 40% - Mar 2027	73.10*	[ICRA]A- (CE) (Stable)

*Part of the Rs 3335.80 crore Bond Programme rated by ICRA

Source: TANGEDCO

Annexure-2: List of entities considered for consolidated analysis

Not applicable

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