Adani Gas Limited

October 15, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loans	394.00	420.18	[ICRA]A+(Stable) reaffirmed; rating on watch with developing implications removed
Long Term Fund Based - CC	0.00	30.00	[ICRA]A+(Stable) reaffirmed; rating on watch with developing implications removed
Short Term Non-fund Based - BG/LC	153.00	665.00#	[ICRA]A1+ reaffirmed; rating on watch with developing implications removed
Short Term Fund Based - BD/Short term loan	25.00	55.00	[ICRA]A1+ reaffirmed; rating on watch with developing implications removed
Short Term Fund Based/ Non-Fund Based	105.00	0.00	-
Long Term/Short Term Unallocated	24.00	30.82	[ICRA]A+(Stable)/A1+ reaffirmed; rating on watch with developing implications removed
Total	**701.00**	**1201.00**	

* - Instrument details are provided in Annexure-1

- Contains Rs. 75 crore interchangeability with FB limits

Rating action

ICRA has reaffirmed the long-term rating at [ICRA]A+ (pronounced as ICRA A plus) on the Rs. 420.18-crore[1] (enhanced from Rs. 394.00 crore) term loans and the Rs. 30.00-crore (enhanced from nil) fund based facilities of Adani Gas Limited (AGL or the company). ICRA has also reaffirmed the short-term rating at [ICRA]A1+ (pronounced ICRA A one plus) on the Rs. 55.00-crore (enhanced from Rs. 25.00 crore) short-term fund based facilities and the Rs. 665.00-crore (enhanced from Rs 228.00 crore) non-fund based facilities of AGL. ICRA has also reaffirmed the ratings of [ICRA]A+/[ICRA]A1+ to the unallocated limits of Rs. 30.82-crore (enhanced from Rs. 24.00 crore). The rating watch with developing implications has been removed and 'Stable' outlook has been assigned. The short-term non-fund based facility (of Rs. 665.00 crore) includes a facility of Rs. 75.00 crore which is interchangeable as a fund based facility[2].

Rationale

The ratings reaffirmation continues to factor in the healthy financial risk profile of AGL characterized by adequate return metrics and debt protection metrics supported by stable cash generation from its ongoing business. The ratings favourably factor in the significant improvement of 17% in AGL's marketed gas volumes during FY2018, strong contribution margins and the balanced revenue mix of AGL amongst compressed natural gas (CNG) and piped natural gas (PNG) consumers which together continue to lend stability to the revenue model. The ratings also take into account the healthy competitive advantage of CNG and PNG (domestic) over liquid fuels as well as the expected jump in gas volumes post operationalisation of the city gas distribution (CGD) network in the newly awarded 13 GAs which will drive the growth in scale going forward.

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[1] *100 lakh = 1 crore = 10 million*

[2] *For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications*

The ratings, however, are constrained by execution and funding risks associated with the large planned capital expenditure (capex) over eight years for operationalisation of CGD network in the 13 newly awarded geographical areas (GAs) to AGL as well as the large planned equity commitment by AGL for IOAGPL's nine newly awarded GAs. The ratings are also constrained by the large outstanding advances of Rs 359 crore as on March 2018 given out to former parent - Adani Enterprises Limited (AEL). ICRA notes that the company's management has plans to bring back the advances over the medium term to support the equity requirement towards the capex plans of AGL. The ratings also factor in AGL's significant indirect exposure to JV company – Indian Oil Adani Gas Private Limited (IOAGPL) in the form of corporate guarantees for its CGD operations. Further, any significant upward revision in domestic gas price or change in gas allocation policy could impact the competitive advantage over liquid fuels/LPG and would be a rating sensitivity.

The removal of rating watch follows the National Company Law Tribunal (NCLT) approval for the demerger of AGL from its parent company - AEL and AGL's planned listing on the stock exchange by November 2018.

Outlook: Stable

ICRA believes that given the favourable demand outlook, availability of low-cost domestic gas for CNG and PNG (domestic), and healthy contribution margin, the operating income as well as operating profit of AGL is expected to show moderate growth over the next few years. The outlook may be revised to 'Positive' if there is an improvement in the volumes or contribution margin leading to better profit margins or if there is any significant improvement in the coverage indicators. The outlook may be revised to 'Negative' if the capital structure deteriorates due to the planned capex, if there is any major unplanned execution delay in the new GAs attracting penalties from PNGRB or if the volume build-up in the new GAs is lower than expected.

Key rating drivers

Credit strengths

Healthy sales mix renders stability to revenue model - AGL has a healthy mix of CNG and PNG sales with CNG accounting for ~52% of FY2018 volumes while PNG accounts for the remaining 48%. Gas sales volumes reported a healthy growth of 17% in FY2018 as volumes picked up in Faridabad and Ahmedabad PNG - Industrial as well as CNG segments. Though the contribution of Faridabad to the total sales of AGL has been increasing at a steady pace, Ahmedabad continues to remain the major contributor for AGL forming ~64% of the sales volume in FY2018 (down from 68% in FY2017).

Prospects for volume growth remain buoyant as healthy competitive advantage over liquid fuels continues - AGL's pricing strategy takes into account its own gas purchase cost, its margins and the need for its CNG and PNG to be competitive vis-à-vis the fuels they replace. Low prevailing domestic gas prices have ensured that CNG and PNG (domestic) prices continue to remain competitive against competing fuels. On a relative basis, CNG remains more competitive against automobile fuels viz. petrol and diesel as compared to the competitiveness of PNG (domestic) against LPG, which is pegged down by the existing subsidy on LPG.

Operating income and profitability grew significantly on the back of increased outreach - The operating income increased by 19% in FY2018, driven by a 17% growth in sales volumes accompanied by an increase in average realisations. The growth in sales was majorly witnessed in the CNG and PNG (industrial) segments. The operating income of AGL stood at Rs. 1,301 crore in FY2018 as compared to Rs. 1,091 crore in the previous year and this coupled with improved contribution has led to an increase in the operating margins as well as the net margins.

Improved gearing and debt servicing indicators - The overall debt level of the company declined significantly in FY2018 as its outstanding Commercial Paper of Rs. 150 crore matured during the year. Additionally, the net worth of the company improved due to healthy internal accruals during the year. Consequently, the gearing improved to 0.7 times in FY2018 from 1.1 times in FY2017. The interest coverage indicator as well as the Debt/OPBDITA metrics also improved in

FY2018. Also, as per the commitment given by AGL, it reduced the inter-corporate loans & advances to AEL and brought down the outstanding to a level of Rs. 359 crore in FY2018 from Rs. 485 crore in FY2017. The management expects to receive the balance amount from AEL over the next 2-3 years to meet the capex planned to be incurred for the newly awarded GAs.

Credit challenges

Project execution and funding risks associated with the GAs awarded in the ninth CGD bid round - In the ninth CGD bid round concluded in August 2018, AGL got awarded 13 new GAs by the PNGRB. The company expects the total capex requirement for these 13 GAs to be tentatively in the range of Rs. 7,500-8,000 crore. However, the year-wise phasing of capex over the course of eight minimum work programme (MWP) years and the debt-equity mix are yet to be finalised by the company. Though this presents a growth opportunity for AGL, it also poses an execution risk and any significant delay or under-achievement of the MWP target attracting major penalties and/or encashment of the Rs. 356 crore performance guarantees submitted by AGL towards these new GAs by PNGRB will be a key rating sensitivity. Also, given the significantly large funding requirement, company's ability to tie-up long-term funding at acceptable interest rates will also be a rating sensitivity.

Large equity commitments to be made by AGL in IOAGPL for the newly awarded GAs - As of March 2018, IOAGPL had received authorisation from PNGRB to implement CGD network in nine GAs. AGL had contributed Rs. 124 crore to the JV as equity as of March 31, 2018 and an estimated additional contribution of around Rs. ~350 crore (50% contribution in the JV's equity capital) would be required over the duration of project implementation. Additionally, in August 2018, IOAGPL got awarded nine new GAs for CGD implementation by the PNGRB. The company expects a total capex requirement for these nine GAs, as per preliminary estimates, to be about Rs. 8,000 crore. AGL would be required to contribute significant equity commensurate to its stake in IOAGPL depending on the debt-equity mix finalised for the timely achievement of MWP milestones.

Indirect exposure to IOAGPL by way of a corporate guarantee for its non-fund based facility - IOAGPL has a non-fund based facility of Rs. 5,000 crore, which has been submitted to the regulator as a performance guarantee to meet the MWP for the seven GAs (not including the two GAs awarded in February-March 2018) that were awarded to IOAGPL. AGL has extended a corporate guarantee to IOAGPL of 50% of the facility. The progress on most of the GAs is ahead of schedule and is expected to meet the MWP requirements, mitigating the risk of encashment. However, in case of delays, should the guarantee be encashed by PNGRB, the financial profile of AGL could be adversely affected and this would be a key rating sensitivity. Additionally, for the GAs awarded in the ninth CGD bid round, IOAGPL has also submitted performance guarantee of Rs. 382 crore and timely achievement of the MWP milestones would be critical to avoid encashment.

Ability to tie-up gas sources for the PNG (industrial) requirement at competitive prices would be critical - Post the directive of the Government of India on allocation of 100% domestic gas to CNG and PNG (domestic) segments, AGL has been receiving the same from GAIL. For its PNG (industrial) and PNG (commercial) gas requirement, the company has adequate gas tie-ups for the short term in place. However, ability of AGL to secure additional gas requirements at competitive prices in the long term would continue to remain critical.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below**.**

Links to applicable criteria:

Corporate Credit Rating Methodology

Rating Methodology for City Gas Distribution Companies

About the company

Adani Gas Limited, incorporated in 2005, is in the city gas distribution (CGD) business which involves marketing and distribution of natural gas (piped and compressed). AGL currently supplies piped natural gas (PNG) to industrial, commercial, domestic customers and compressed natural gas (CNG) to transport sector in the areas of Ahmedabad, Vadodara and Faridabad. It has also recently started its operations in Khurja (Uttar Pradesh). AGL has also set-up pipeline infrastructure in cities of Udaipur, Jaipur, Noida and Lucknow based on erstwhile issued State Governments' NOC. However, its permissions for operations in these cities remain sub-judice.

For the year FY2018, the company reported a net profit of Rs. 172.9 crore on an operating income of Rs. 1,301.5 crore, as compared to a net profit of Rs. 101.2 crore on an operating income of Rs. 1,091.3 crore in the previous year.

Key financial indicators (audited)

	FY2017	FY2018
Operating Income (Rs. crore)	1,091.3	1,301.5
PAT (Rs. crore)	101.2	172.9
OPBDIT/OI (%)	25.8%	28.1%
RoCE (%)	15.1%	21.3%
Total Debt/TNW (times)	1.1	0.7
Total Debt/OPBDIT (times)	2.7	1.6
Interest coverage (times)	6.4	8.1

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Current Rating (FY2019)				Chronology of Rating History for the past 3 years					
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2018			Date & Rating in FY2017		Date & Rating in FY2016
					Oct 2018	Jan 2018	Jul 2017	Jul 2017	Feb 2017	Sep 2016	Jul 2015
1	Term Loans	Long Term	420.18	420.18	[ICRA] A+ (Stable)	[ICRA] A+ &; Placed on watch with developing implications	[ICRA] A+ (Stable)	[ICRA] A+ (Stable)	[ICRA] A+ (Stable)	[ICRA] A+ (Stable)	[ICRA] A+ (Stable)
2	Fund Based Limits - CC	Long Term	30.00	0.0	[ICRA] A+ (Stable)	-	-	-	[ICRA] A+ (Stable)	[ICRA] A+ (Stable)	[ICRA] A+ (Stable)
3	Non-Fund Based Limits – BG/LC	Short Term	665.00#	618.10	[ICRA] A1+	[ICRA] A1+ &; Placed on watch with developing implications	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+
4	Fund Based Limits – BD/short term loan	Short Term	55.00	0.0	[ICRA] A1+	[ICRA] A1+ &; Placed on watch with developing implications	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	-
5	Unallocated	Long Term/ Short Term	30.82	-	[ICRA] A+ (Stable)/ A1+	[ICRA]A+ &/A1+ &; Placed on watch with developing implications	[ICRA]A+ (Stable)/A1+	[ICRA]A+ (Stable)/ A1+	-	-	-

- Contains Rs. 75 crore interchangeability with FB limits

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
NA	Term Loan – 1	FY2017	8.35%	FY2025	221.43	[ICRA] A+(Stable)
NA	Term Loan – 2	FY2018	8.50%	FY2026	124.95	[ICRA] A+(Stable)
NA	Term Loan – 3	FY2018	8.65%	FY2025	73.80	[ICRA] A+(Stable)
NA	Fund based – CC	NA	NA	NA	30.00	[ICRA] A+(Stable)
NA	Fund based – BD/Short term loan	NA	NA	NA	55.00	[ICRA] A1+
NA	Non-fund based – BG/LC	NA	NA	NA	665.00#	[ICRA] A1+
NA	Long Term/Short Term Unallocated	NA	NA	NA	30.82	[ICRA]A+(Stable)/ A1+

Source: Adani Gas Limited

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About ICRA Limited:

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Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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