ICRA

September 03, 2020

Adani Gas Limited: Rating upgraded to [ICRA]AA-/A1+; removed from watch with positive implications and Stable outlook assigned

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loans	383.79	410.27	[ICRA]AA-; upgraded from [ICRA]A+; rating watch with positive implications removed and Stable outlook assigned
Long Term Fund Based - CC	30.00	75.00	[ICRA]AA-; upgraded from [ICRA]A+; rating watch with positive implications removed and Stable outlook assigned
Short Term Non-fund Based - BG/LC	1,265.00	1,100.00	[ICRA]A1+ reaffirmed; rating watch with positive implications removed
Short Term Fund Based - BD/Short term loan	55.00	75.00	[ICRA]A1+ reaffirmed; rating watch with positive implications removed
Long Term/Short Term Unallocated	67.21	140.73	[ICRA]AA-/A1+; upgraded from [ICRA]A+/A1+; rating watch with positive implications removed and Stable outlook assigned
Total	**1,801.00**	**1,801.00**	

** - Instrument details are provided in Annexure-1;*

Rationale

The rating upgrade for Adani Gas Limited (AGL) takes into consideration the completion of the acquisition of 37.4% stake in AGL by Total Holdings SAS (Total), a 100% subsidiary of Total SA, following which Total has been classified as a co-promoter of AGL. ICRA expects the operational synergies from this transaction to be significant over the long-term. Total SA being among the leading liquefied natural gas (LNG) players in the world, AGL should benefit from a favourable long-term LNG sourcing tie-up for its operations. Moreover, with Total being an equal shareholder as the Adani Group after this transaction, the equity requirement for the newly awarded 15 geographical areas (GAs) in the city gas distribution (CGD) bid round 9 and 10 will be contributed equally by both these promoter groups. ICRA believes that Total's strong credit profile (Moody's Aa3(Negative)/P1) coupled with Adani Group's financial flexibility lends considerable support to AGL in terms of its ability to raise capital to meet the capex funding requirements.

The rating continues to factor in the healthy financial risk profile of AGL, characterised by adequate return metrics and debt protection metrics supported by stable cash generation from its ongoing business. The rating favourably factors in the improvement of 8% YoY in AGL's marketed gas volumes in FY2020, strong contribution margins and the balanced revenue mix of AGL among compressed natural gas (CNG) and piped natural gas (PNG) consumers, which together continue to lend stability to the revenue model. The rating also takes into account the healthy competitive advantage of CNG and PNG (domestic) over liquid fuels as well as the expected jump in gas volumes following the operationalisation of the CGD network in the newly awarded GAs in bid rounds 9 and 10 of the CGD, which will drive the growth in scale. The rating also favourably factors in the receipt of the advances of Rs. 359 crore given to Adani Enterprises Limited (AEL) as on September 30, 2019, which will support the equity requirement towards the capex plans of AGL.

The rating, however, is constrained by the execution and funding risks associated with the large ongoing capex planned over the next seven to eight years for the operationalisation of the CGD network in the 15 newly awarded GAs (13 GAs in the 9th round and two GAs in the 10th round) to AGL. ICRA notes the minimum work programme (MWP) associated with each of the Gas, achieving which will be critical. The rating factors in the adverse impact on the gas sales volume as well as infrastructure creation witnessed in Q1 FY2021, following the phased nationwide lockdown announced by the Government of India (GoI). However, ICRA notes that a rapid recovery in sale volume was witnessed over June–July 2020. The rating also takes into consideration the large planned equity commitment by AGL towards its joint venture (JV), Indian Oil Adani Gas Private Limited's (IOAGPL's) newly awarded 10 GAs (nine GAs in the 9th round and one GA in the 10th round). The ratings factor in AGL's significant indirect exposure to 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/liquefied petroleum gas (LPG) and would be a rating sensitivity.

Key rating drivers

Credit strengths

Co-promoted by Adani Group and Total (an oil and gas major) – The transaction of acquisition of 37.4% stake in AGL by Total was completed in April 2020, with Total now becoming a co-promoter of AGL with equal representation on the company's board as the Adani Group. Total is among the leading LNG players in the world and AGL should benefit from a favourable long-term LNG sourcing tie-up for its operations. Also, Total's strong credit profile (Moody's Aa3(Negative)/P1) coupled with Adani Group's financial flexibility lends considerable support to AGL in terms of its ability to raise capital to meet the capex funding requirements.

Healthy sales mix renders stability to revenue model – AGL has a healthy mix of CNG and PNG sales with both segments accounting for 50% volumes each in FY2020. Gas sales volumes reported a growth of 8% YoY in FY2020 to reach 1.60 mmscmd, as volumes picked up in Khurja even as volumes in Ahmedabad and Faridabad continued to remain almost stable. The volume growth is also attributable to the volume build-up from CNG operations in the GAs awarded in the 9th CGD bid round. Ahmedabad remained the major contributor for AGL, forming 58% of the sales volume in FY2020. In Q1 FY2021, given the phased nationwide lockdown announced by GoI to curb the spread of Covid-19, the sale volume dipped to 0.71 mmscmd. However, ICRA notes that after a sharp decline in April-May 2020, the volume improved rapidly over June-July 2020.

Buoyant prospects for volume growth due to healthy competitive advantage over liquid fuels – 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 alternative fuels. Low prevailing domestic gas prices have ensured that CNG and PNG (domestic) prices continue to remain competitive against alternative fuels. On a relative basis, CNG remains more competitive against automobile fuels, viz. petrol and diesel compared to the competitiveness of PNG (domestic) against LPG, which is pegged down by the existing subsidy on it.

Healthy financial profile – While the operating income (OI) grew at 9% YoY in FY2020, the operating profit improved at a faster rate given that the gross contribution has remained healthy and has been on an uptrend over the past few years. Given the high operating profitability (31.7% in FY2020) and internal accruals, the net worth of the company improved significantly resulting in an improved gearing of 0.3 time as on March 1, 2020. The Total Debt/OPBDITA metrics also improved to 0.7 time in FY2020. Also, AGL had outstanding advances of Rs. 359 crore to AEL as on September 30, 2019, about Rs. 48 crore of which was received back in Q3 FY2020 and the rest in Q1 FY2021. This will aid in meeting the equity requirement for the capex planned to be incurred for the newly awarded 15 GAs.

Credit challenges

Project execution and funding risks associated with GAs awarded in 9th and 10th CGD bid rounds – In the 9th and 10th CGD bid rounds concluded in August 2018 and March 2019, respectively, AGL was awarded 15 new GAs by PNGRB. The company expects the total capex requirement for these 15 GAs to be tentatively in the range of Rs. 5,000–5,500 crore covering the MWP of initial five years, to be funded by a mix of debt and equity. ICRA notes that AGL has successfully tied up debt funding for the initial five years. Though this capex presents a growth opportunity for AGL, it also poses significant execution risk. Any significant delay or under-achievement of the MWP target in respective GAs attracting major penalties and/or encashment of the performance guarantees submitted by AGL towards the new GAs will be a key rating sensitivity.

Large equity commitments towards IOAGPL for newly awarded GAs – Till the 8th CGD bid round, IOAGPL had received authorisation from PNGRB to implement a CGD network in nine GAs. AGL had contributed Rs. 291.0 crore to the JV as equity as on March 31, 2020 and an estimated additional contribution of around ~Rs. 225-250 crore (50% contribution in the JV's equity capital) would be required over the duration of the project implementation. Additionally, IOAGPL was awarded nine new GAs for CGD implementation by PNGRB in the 9th round and one GA in the 10th round. The company expects a total capex requirement for these new GAs to be about Rs. 6,800 crore for the initial five years. AGL would be required to contribute equity commensurate to its stake in IOAGPL, depending on the debt-to-equity ratio as per the financial plan finalised for the timely achievement of MWP milestones.

Indirect exposure to IOAGPL by way of corporate guarantee for its non-fund based facility – As on March 31, 2020, IOAGPL had a non-fund based facility of Rs. 6,635 crore, which was submitted to the regulator as a performance guarantee to meet the MWP for the nine GAs that were awarded to IOAGPL till the 8th CGD bid round. AGL has extended a corporate guarantee to IOAGPL for 50% of the facility. The progress on most of the GAs is on schedule, 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 9th and 10th CGD bid rounds, IOAGPL has submitted a performance guarantee of Rs. 432 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 – Following the GoI directive on the allocation of 100% domestic gas to CNG and PNG (domestic) segments, AGL has been receiving the same from GAIL Ltd. For its PNG (industrial) and PNG (commercial) gas requirements, the company has adequate gas tie-ups in place for the medium term. However, its ability to secure additional gas requirements at competitive prices in the long-term would continue to remain critical. In addition to its successful track record, the presence of Total as a co-promoter of AGL mitigates this risk to a large extent.

Liquidity position: Adequate

AGL's liquidity position remains adequate with annual fund flow from operations of Rs. 431.2 crore in FY2020 and surplus cash and liquid investments of Rs. 89.5 crore as on March 31, 2020. The company also had a sanctioned fund-based working capital facility of Rs. 150.0 crore as on June 30, 2020, the average utilisation of which remained very low over the past 12 months. The liquidity is also supported by the receipt of advances given to AEL. However, the liquidity position remains affected by the moderate to high scheduled repayments over the next five years.

Rating sensitivities

Positive triggers – Given the large capex being undertaken simultaneously in several GAs, an upgrade over the medium-term is less likely. Stabilisation of operations in the new GAs would be essential for consideration of a rating upgrade.

Negative triggers – Negative pressure on the rating can arise if the Net External Debt/OPBDITA increases over 3.0 times on a sustained basis or if any significant penalty is levied by PNGRB for non-achievement of the MWP.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for City Gas Distribution Companies
Parent/Group Support	Not applicable
Consolidation/Standalone	The rating is based on the standalone financial profile of the company

About the company

Adani Gas Limited, incorporated in 2005, is in the CGD business, which involves marketing and distribution of natural gas (piped and compressed). At present, AGL supplies PNG to industrial, commercial and domestic customers; and CNG to the transport sector in Ahmedabad, Vadodara (both in Gujarat), Faridabad (Haryana) and Khurja (Uttar Pradesh). AGL has also received authorisations to establish the CGD network in the 15 new GAs from the 9th and 10th bid rounds combined. AGL has also entered into a 50:50 JV with Indian Oil Corporation Limited, with the JV, IOAGPL, engaged in the implementation of the CGD network in several other GAs across India.

For FY2020, the company reported a net profit of Rs. 436.2 crore on an OI of Rs. 1,874.6 crore, compared to a net profit of Rs. 228.7 crore on an OI of Rs. 1,719.0 crore in the previous year.

Key financial indicators (audited)

	FY2019	FY2020
Operating Income (Rs. crore)	1,719.0	1,874.6
PAT (Rs. crore)	228.7	436.2
OPBDIT/OI (%)	26.4%	31.7%
RoCE (%)	24.5%	39.2%
Total Outside Liabilities/TNW (times)	0.9	0.7
Total Debt/OPBDIT (times)	0.9	0.7
Interest coverage (times)	5.1	14.5
DSCR (times)	1.9	5.8

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

	Instrument	Current Rating (FY2021)				Rating History for the past 3 years					
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Rating	FY2020		FY2019	FY2018		
					03-Sep-2020	13-Dec-2019	23-Oct-2019	15-Oct-2018	29-Jan-2018	19-Jul-2017	10-Jul-2017
1	Term Loans	Long Term	410.27	410.27	[ICRA] AA- (Stable)	[ICRA] A+%; Rating on watch with positive implications	[ICRA] A+%; Rating on watch with positive implications	[ICRA] A+ (Stable)	[ICRA] A+&; Rating on watch with developing implications	[ICRA] A+ (Stable)	[ICRA] A+ (Stable)
2	Fund Based Limits - CC	Long Term	75.00	0.00	[ICRA] AA- (Stable)	[ICRA] A+%; Rating on watch with positive implications	[ICRA] A+%; Rating on watch with positive implications	[ICRA] A+ (Stable)	-	-	-
3	Non-Fund Based Limits – BG/LC	Short Term	1100.00	674.00	[ICRA] A1+	[ICRA] A1+%; Rating on watch with positive implications	[ICRA] A1+%; Rating on watch with positive implications	[ICRA] A1+	[ICRA] A1+&; Rating on watch with developing implications	[ICRA] A1+	[ICRA] A1+
4	Fund Based Limits – BD/short term loan	Short Term	75.00	0.00	[ICRA] A1+	[ICRA] A1+%; Rating on watch with positive implications	[ICRA] A1+%; Rating on watch with positive implications	[ICRA] A1+	[ICRA] A1+&; Rating on watch with developing implications	[ICRA] A1+	[ICRA] A1+
5	Unallocated	Long Term/ Short Term	140.73	-	[ICRA] AA- (Stable)/A1+	[ICRA] A+%/ A1+%; Rating on watch with positive implications	[ICRA] A+%/ A1+%; Rating on watch with positive implications	[ICRA] A+ (Stable)/A1+	[ICRA] A+&/ A1+&; Rating on watch with developing implications	[ICRA] A+ (Stable)/A1+	[ICRA] A+ (Stable)/A1+

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 click here

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	NA	FY2025	175.86	[ICRA]AA-(Stable)
NA	Term Loan – 2	FY2018	NA	FY2026	99.96	[ICRA]AA-(Stable)
NA	Term Loan – 3	FY2018	NA	FY2025	59.45	[ICRA]AA-(Stable)
NA	Term Loan – 4	FY2020	NA	FY2028	75.00	[ICRA]AA-(Stable)
NA	Fund based – CC	NA	NA	NA	75.00	[ICRA]AA-(Stable)
NA	Non-fund based – BG/LC	NA	NA	NA	1100.00	[ICRA]A1+
NA	Fund based – BD/Short term loan	NA	NA	NA	75.00	[ICRA]A1+
NA	Long Term/Short Term Unallocated	NA	NA	NA	140.73	[ICRA]AA-(Stable)/A1+

Source: Adani Gas Limited

Annexure-2: List of entities considered for consolidated analysis – Not applicable

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About ICRA Limited:

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