Green Gas Limited

April 23, 2018

Summary of rated instruments

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Proposed Term Loan	200.00	[ICRA]A+ (Stable) assigned
Total	**200.00**	

**Instrument details are provided in Annexure-1*

Rating action

ICRA has assigned a long-term rating of [ICRA]A+ (pronounced ICRA A plus) for the Rs. 200.00 crore proposed term loan of Green Gas Limited (GGL). The outlook on the long-term rating is Stable.

Rationale

The rating takes into account the favourable demand outlook for Compressed Natural Gas (CNG) in the two cities (Lucknow and Agra) operated by GGL, current marketing exclusivity for Lucknow in the city gas distribution (CGD) business (up to 2021), infrastructure exclusivity in Lucknow (up to March 2031) and Agra (up to November 2029) , favourable regulatory support for CNG and domestic Piped Natural Gas- [PNG(d)] segment evident in allocation of domestic gas to meet the entire demand under the segments and the company's secure gas tie-up with GAIL (India) Limited (GAIL - rated [ICRA]AAA(Stable)) to meet its existing natural gas demand. There has been a significant push by GoI towards use of CNG as a vehicular fuel to reduce pollution and reliance on petrol and diesel as preferred fuels. In-line with the same, GoI has ensured low price domestic gas allocation to meet the entire CNG demand to keep supply side bottlenecks at bay and keep CNG cost competitive against petrol and diesel. The rating also factors in healthy financial risk profile characterised by healthy return indicators, robust capitalisation and coverage indicators owing to nil debt. The rating also considers the strong promoter profile (Indian Oil Corporation Limited-IOCL-rated [ICRA]AAA(Stable)/[ICRA]A1+ and GAIL) of GGL.

The rating is however constrained by relatively small scale of operations of the company, susceptibility of performance on regulatory framework for CGD entities, material shortfall in achieving the target for PNG (d) connections under the authorisation for Lucknow and significant capex plans of the company which is expected to result in an increase of PNG in the sales mix going forward which is expected to result in moderation in returns and credit profile of the company. GGL has lined up significant capex plans for Rs. 250-300 crore per annum for next 2-3 years, which is planned to be funded by debt and internal accruals. While the large scale of the capex and the gestation period associated with build-up of sales volumes, are expected to have some moderating impact on the company's return and credit metrics from current levels, especially considering the company's ambitious plans to increase the penetration of the PNG (d) segment which is a lower margin segment, nevertheless on an absolute basis, these metrics would continue to be healthy due to low leverage. GGL is also significantly behind the Minimum Works Program (MWP) defined in its authorisation for Lucknow Geographical Area (GA). While the company has filed a protest with PNGRB requesting for rationalisation of the MWP targets, any adverse ruling by PNGRB may result in encashment of performance bank guarantee which though is relatively smaller in amount of ~Rs. 3 crores. In case GGL participates and wins additional cities/geographical areas (GAs) in upcoming rounds for CGD networks, ICRA will evaluate the impact of the same on the credit risk profile of the company on the basis of associated regulatory, marketing and funding risks.

Outlook: Stable

The outlook on the rating is Stable in anticipation of healthy demand outlook for CNG, which would continue to contribute majority of cash generation of the company over the medium term.

Key rating drivers

Credit strengths

Strong parentage being owned by GAIL and IOCL: GGL is a joint-venture set-up by GAIL and IOCL with each owning 49.97% each. The parent companies are dominant players in the oil & gas sector and have extensive experience and understanding of the domestic gas sector. 4 out of total 6 board members of GGL are from the parent companies. Any significant dilution in ownership by GAIL or IOCL could be a key rating sensitivity.

Favourable outlook for CNG driven by significant cost advantage over liquid fuels and the push by the GoI promoting use of cleaner fuel: The outlook on CNG consumption is also due to significant cost advantage over petrol and diesel. Additionally, the GoI has been pushing for higher usage of clean fuel like CNG in the vehicular usage and PNG (d) in the domestic cooking usage by allocating lower cost domestic gas for these segments. This bodes well for the CGD companies as it ensures availability of natural gas to meet the demand of these segment and enables competitiveness of CNG and PNG against alternative fuels.

Consumer mix tilted towards CNG, which is a relatively high margin segment: Nearly ~96% GGL's sale are derived from the CNG segment which is has relatively higher profitability vis-à-vis the PNG segment. As a result, the company has been able to maintain healthy profitability with operating margins of nearly 37% and net margins of 23% in FY2017. The operating profit of the company increased to Rs.71 crore in FY2017 vis-a-vis Rs54 core in FY2016 owing to an increase in sales volumes and higher sales realisation during the year for CNG. The return indicators have also remained healthy with RoCE at ~38% and RoNW of 19% for FY2017.

Protection afforded by the regulations under the PNGRB Act as per which authorised incumbents will enjoy monopoly with regard to network provision, further supported by pre-tax RoCE of 21%: Post the expiry of marketing exclusivity period of 5 years, the PNGRB regulations ensure a normative pre-tax RoCE of 21% for the incumbents through adequate network tariff and compression charges on the regulated assets owing to physical exclusivity of 25 years in place (starting 2021 for Lucknow and 2014 for Agra). Thus, regulations ensure fixed returns post expiry of exclusivity period. Additionally, third-party marketers face entry barriers like investment in CNG stations, tying up firm gas supplies, gas availability at competitive prices etc.

Robust credit profile marked by strong networth, healthy cash accruals and nil debt: The credit profile of the company remains robust owing to strong networth driven by healthy cash accruals. The capitalisation and coverage indicators are robust owing to healthy profitability and nil debt on the balance sheet of GGL

Secure gas tie-up with GAIL for its existing operations: GGL's sales mix comprises of 0.19 mmscmd of CNG sales and 0.01 mmscmd of PNG sales. GGL has secured gas tie-up with GAIL gas to meet its entire gas requirement and since most of the sales are derived from CNG, domestic gas allocation for the same results in assured gas supplies.

Credit challenges

Modest scale of operations limited to cities of Agra and Lucknow: The scale of operations remains moderate vis-à-vis some other large CGD companies as the network penetration has remained lower in the cities. GGL reported operating income of Rs. 193 crore in FY2017 and Rs.183 crore in 9M FY2018 (provisional). The company's CNG network comprises of 31 CNG stations (13 in Agra and 18 in Lucknow) as on March 31, 2018 and ~41,565 domestic PNG connections as on March 31, 2018, which indicate material expansion in the network as reflected by 19 CNG stations as on March 31, 2017 and ~16,200 PNG (d) connections as on March 31, 2017. The benefits from the recent expansion in the network are likely to accrue over the medium term, which may help the company to expand its volume and revenue base. Further, going forward the company's sales volume may also grow following the significant network expansion planned by the company.

Weak economics of PNG-industrial (PNG (I)) against major liquid fuels like furnace oil and Low Sulphur Heavy Stock (LSHS): The PNG(I) segment must compete with other liquid fuels like Naphtha, LSHS and Fuel oil for its usage. Owing to soft crude oil prices in the recent years, PNG(I) has exhibited weak economics against competing liquid fuels as PNG(I) requirement is met through costlier re-gasified liquified natural gas (RLNG) against domestic gas allocation for CNG and PNG (d). While the contribution of PNG(I) segment to the sales of GGL remains negligible, going forward the segment may witness moderate growth especially if prices of crude oil and liquid fuels continue to reflect a rising trend.

Expected moderation in return and capitalisation indicators owing to significant capital outlay plan and gestation period associated with volume ramp-up: In the past, the company has been able to meet capex requirements largely through internal accruals over the last few years. However, going forward, the company plans to fund its capex plans through a debt-equity ratio of 70-30. The large capex is expected to result in moderation of return indicators as these projects have a gestation period of 2-3 years. The capitalisation indicators are also expected to moderate given significant debt funding being undertaken by the company for the upcoming capex.

Highly regulated nature of the CGD sector; especially related to MWP targets set by PNGRB: CGD entities are regulated by PNGRB and the regulator defines the targets for PNG (d) connections, compression capacity and steel/PE pipeline network to be laid by the CGD entities in first five years of operations. If the entities fail to meet these targets, their performance guarantees can be encashed by PNGRB. There are regulations relating to setting of network tariff and compression charges which result in weak pricing power to the CGD entities. The highly regulated nature of the sector exposes GGL to regulatory risk and any unfavourable change in the regulations may negatively impact the credit profile of the entity.

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

Green Gas Limited (GGL) was set-up as a JV by Indian Oil Corporation Limited (IOCL) and GAIL (India) Limited (GAIL) in 2005. The company is the exclusive distributor of Piped Natural Gas (PNG), Compressed Natural Gas (CNG) and developing city gas distribution (CGD) infrastructure in the cities of Lucknow and Agra both located in the state of Uttar Pradesh. The authorization for setting up CGD network in Agra was received in November 2009 and for Lucknow in February 2016. By end of March 2018, the company has set-up 31 CNG stations with a total compression capacity of 3,92,388 kg/day. In the PNG segment company has around 41,565 domestic, 63 commercial and 22 industrial connections. The total pipeline network comprises of 725 KM inch steel pipeline and 1935 KM inch of MDPE pipeline.

Key financial indicators (Audited)

	FY2016	FY2017
Operating Income (Rs. crore)	178.7	193.1
PAT (Rs. crore)	34.4	44.8
OPBDIT/ OI (%)	30%	37%
RoCE (%)	35.3%	37.7%
Total Debt/ TNW (times)	0.0	0.0
Total Debt/ OPBDIT (times)	0.0	0.0
Interest coverage (times)	164.2	1,495.2
NWC/ OI (%)	-7%	-7%

Source: ICRA estimates; OI: Operating Income; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net-Worth + Deferred Tax Liability - Capital Work - in Progress); NWC: Net Working Capital

Status of non-cooperation with previous CRA: CRISIL in its press release dated November 3, 2016 withdrew the long-term rating and suspended the short-term rating of Green Gas Limited as the company had not provided the information required to maintain a valid rating.

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
				April 2018	-	-	-
Proposed Term Loan	Long Term	200.00	-	[ICRA]A+ (Stable)	-	-	-

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
-	Proposed Term loan	-	-	-	200.00	[ICRA]A+ (Stable)

Source: Green Gas Limited

ANALYST CONTACTS

K Ravichandran
+91 44 4596 4301
ravichandran@icraindia.com

Anoop Bhatia
+91 124 4545 315
anoopb@icraindia.com

Varun Gogia
+91 124 4545 373
varun.gogia@icraindia.com

RELATIONSHIP CONTACT

L. Shivkumar
+91 22 6169 3300
shivkumar@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
naznin.prodhani@icraindia.com

Helpline for business queries:

+91-124-2866928 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

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.

For more information, visit www.icra.in

ICRA Limited

Corporate Office
Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002
Tel: +91 124 4545300
Email: info@icraindia.com
Website: www.icra.in

Registered Office
1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001
Tel: +91 11 23357940-50

Branches

Mumbai	+ (91 22) 24331046/53/62/74/86/87
Chennai	+ (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,
Kolkata	+ (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,
Bangalore	+ (91 80) 2559 7401/4049
Ahmedabad	+ (91 79) 2658 4924/5049/2008
Hyderabad	+ (91 40) 2373 5061/7251
Pune	+ (91 20) 6606 9999