GAIL Gas Limited

March 25, 2021

Ratings

Facilities/Instruments	**Amount (Rs. crore)**	**Ratings**	**Rating Action**
Long Term Bank Facilities	250.00	CARE AAA (CE); Stable* [Triple A (Credit Enhancement); Outlook: Stable]	Reaffirmed
Total Bank Facilities	**250.00 (Rs. Two Hundred Fifty Crore Only)**		

Details of Instrument/facilities in Annexure-1

**based on the credit enhancement in the form of corporate guarantee from GAIL (India) Limited (GAIL) which is an unconditional, irrevocable and continuing manner till all 'obligations' have been repaid in full to the satisfaction of the lender.*

Unsupported Rating [1]	CARE AA (Double A)

Note: Unsupported Rating does not factor in the explicit credit enhancement

Detailed Rationale & Key Rating Drivers for the credit enhanced debt

The rating assigned to the long-term bank facilities of GAIL Gas Limited (GGL) takes into account credit enhancement in the form of corporate guarantee from GAIL (rated CARE AAA; Stable/ CARE A1+) which is an unconditional, irrevocable and continuing manner till all 'obligations' have been repaid in full to the satisfaction of the lender.

Detailed Rationale & Key Rating Drivers of GAIL

The ratings assigned to bank facilities of GAIL continue to derive strength from the majority ownership by the Government of India (GoI), its leadership position in the natural gas transmission segment, diversified revenue stream and a favourable demand situation of natural gas in India. The ratings also factor in the company's strong financial risk profile with a favourable capital structure. The ratings, however, remain susceptible to volatility associated with prices of petrochemicals, LPG and other liquid hydrocarbons, besides the risk associated with un-hedged LNG.

Key rating sensitivity (GAIL)

Positive: Not applicable

Negative

- Reduction in shareholding of government of India below 51%.
- Higher than expected debt leading to a pressure on the capital structure and thereby increasing overall gearing above 1x.

Key Rating drivers of GAIL Gas Limited

The rating assigned to the bank facilities of GGL factors in its strong parentage and support from GAIL, its professional management team and growth in the scale of operations in next two three years coupled with increasing geographical presence. The rating also derives strength from its requirement of gas sourcing being completely tied up with GAIL, the GoI's impetus on promoting natural gas, GGL's monopolistic position in authorized GAs, which is expected to continue even after the end of the marketing exclusivity periods therein considering the entry barriers, and the favourable demand outlook of the city gas distribution (CGD) business.

The rating is, however, constrained by the regulatory risk associated with CGD operations, GGL's aggressive capital expenditure plans and concentrated product mix with moderately diversified geographical mix and customer mix.Going forward, GGL's ability to procure gas at the envisaged price and ability to pass on periodic increase in gas prices in order to maintain the profitability, completion of the capex plan within the envisaged time and cost, a possible change in gas allocation policy and continuance of promoter support from GAIL would remain key rating sensitivities.

Detailed description of the key rating drivers (GAIL)

Key Rating Strengths

Majority ownership by GoI and experienced management team:

GAIL is a Maharatna company incorporated in August 1984. It is an integrated natural gas company, with a presence in transmission of natural gas and LPG, gas processing, city gas distribution, petrochemicals etc. It is of strategic importance to

[1] *As stipulated vide SEBI circular no SEBI/ HO/ MIRSD/ DOS3/ CIR/ P/ 2019/ 70 dated June 13, 2019*

Government of India (GoI) with its leadership position in natural gas transmission and distribution segment. As on December 30, 2020, GOI owns 51.76% stake in the company while the balance is held by various institutions and general public.
The company is being managed by professional and experienced management team having a relevant experience in the industry. The current Chairman and Managing Director of the company, Mr. Manoj Jain is a Mechanical Engineering Graduate and MBA in Operations Management and has a rich and diverse experience of more than 34 years in the areas of business development, petrochemicals, pipeline integrity management and gas marketing activities.

Leadership position in natural gas transmission business
GAIL is the market leader in the transmission of natural gas in the country with over 12,400 Km of pipeline network, out of total pipeline network in India of ~17,500 Km (i.e. 70.86% of country's pipeline) as on March 31, 2020 with natural gas handling capacity of 253 Million Metric Standard Cubic Meter Per Day (MMSCMD). Further, pipeline of around 6,700 Km is under construction & approved by GAIL out of total under construction & approved pipe line being laid in India of around 17000 km. Further, company earns stable cash flows from transmission business, though it accounts only around 7% of total revenue in FY20. However, the PBIT margin during FY20 for the segment stood at high of 58% against 55% during FY19. GAIL gets around 12% internal rate of return (IRR) for its transmission business on back of regular tariff hikes for its pipelines. GAIL's integrated pipeline network of HVJ, Dahej-Vijaipur (DVPL) and Vijaipur-Dadri (GREP) accounts for over 65 per cent of the its's gas transmission volume.

LNG import tie-up in USA, Russia and Qatar
Over the years, GAIL has developed adequate tie ups for supply of natural gas both domestically and internationally. The company sourced around 50% of its total gas requirement through domestic sources which include ONGC (Administrative Price Mechanism (APM) & Non APM), Panna-Mukta and Tapti (PMT) at APM & Production Sharing Contracts (PSC) prices, Ravva, Ravva satellite, etc. The remaining ~50% gas requirement is sourced through imported gas - Regasified Liquefied Natural Gas (RLNG) (Long-term RLNG, Mid Term RLNG and Spot). GAIL has long term LNG contract of around 14 Million Metric Tonne Per Annum (MMTPA) from USA, Russia and Qatar. GAIL has long term contract to buy 5.8 MMTPA of LNG from the U.S. and up to 2.5 MMTPA of LNG annually on a delivered basis from Russia's Gazprom while another 5 MMTPA from RasGas Company Limited (RasGas), Qatar. Going forward, capacity utilisation of the company is not only dependent on the company's ability to market the available gas but securing the additional gas supply for its increasing pipeline infrastructure would also be important.

Diversified revenue stream
GAIL has presence in different products, besides leadership position in transmission of natural gas and LPG. The company has established presence in various other business segments like city gas distribution, petrochemicals, liquid hydrocarbons, exploration & production and telecom. This diversified business segments helps in spreading operating risk of the company.

Strong financial profile marked by increase scale of operation and healthy capital structure
During FY20, GAIL's operating income moderated marginally by 1.92% to Rs. 76,201.45 from Rs. 77,796.70 crore in FY19 mainly on account of dip in income from petrochemicals (on account of dip in sales realisations) and LPG and other liquid hydrocarbon (both on account of dip in sales realisations and sales volume) segment. The company's PBILDT margin improved by 193 bps to 16.8% as against 14.87% in FY19 mainly on account of reduced operating expenditure specifically employee cost and gas cost. The PAT margins of GAIL improved significantly by 405 bps to 12.47% in FY20 as against 8.42% during FY19 on account of adoption of lower tax rates pursuant to Section 115BAA of Income Tax Act, 1961. The company enjoys a comfortable capital structure with an overall gearing of 0.14x as on March 31, 2020 (PY: 0.05x) and adjusted overall gearing of 0.16x on March 31, 2020 (PY: 0.12x). Also, the debt coverage indicators including total debt to GCA and interest coverage ratio stood comfortable for the company for FY20 at 0.69x (PY: 0.24x) and 41.49x (PY: 72.65x) respectively.
9MFY21: The company has reported a total operating income (TOI) of Rs. 42,307 crore in 9MFY21 as against Rs. 55,177 crore in 9MFY20 (decline of -23.32%) with a PBILDT margin of 14.79% (9MFY20: 15.16%). The decline in TOI is on account of weak performance across segments affected due to COVID 19 and lower price realization in petrochemicals, liquid hydrocarbons and natural gas segments. However, the company has witnessed improvement on Q-o-Q basis across all segments with revival in demand by easing of lockdown and increase in economic activity.

Key Rating Weakness
Risk related to un-hedged US LNG contract
GAIL has long term contracts to buy 5.8 MMTPA of LNG from the U.S. out of its total 14 MMTPA long term contract. GAIL's US LNG price is linked with Henry Hub (HH) price while the sale price is linked to three-month Brent prices. In order to mitigate the fluctuations in the HH based LNG prices and crude oil prices, the company procures gas from USA through destination swaps and commodity hedging leading to reduction in shipping cost for the gas imported to India from USA. Furthermore, GAIL

had sold/hedged most of its US LNG purchases under the long-term deals but up to 30% remains an open position and thus is exposed to market demands.

Susceptibility to volatile commodity prices associated with petrochemicals, LPG and other Liquid hydrocarbons
Petrochemicals, LPG and liquid hydrocarbons are directly exposed to changes in the commodity prices. With the change in crude oil and petroleum prices, the realizations from petrochemical will also vary. GAIL had lower revenue in petrochemical sector and liquid hydrocarbons in FY20 on account of dip in average sales realisation by around Rs. 17600/MT and Rs. 4753/MT respectively. Further, due to lower sales realisation GAIL had losses at PBIT level in petrochemical sector of Rs. 245.5 crore as against profit of Rs. 384.9 crore in FY19.

Industry Outlook
India's natural gas market is characterised by a supply deficit, primarily due to low domestic production and inadequate transmission and distribution infrastructure. The domestic demand for natural gas far exceeds domestic supply, resulting in a deficit and increased reliance on LNG. Domestic production of natural gas (gross) has fallen at a CAGR of 0.8% during FY16-20. Net production was 32.7 BCM during FY16 whereas it has declined to 31.2 BCM during FY20. The reason for the decline in production of natural gas over the years is due to the natural decline in output from the ageing fields coupled with lower than expected natural gas production from the Krishna Godavari Basin as well. Production of natural gas has fallen by 5.1% during FY20 compared with the 0.7% fall during FY19.
Natural gas consumption has increased by 5.2% during FY20 compared with the 2.7% growth rate achieved during FY19. The government has been encouraging the use of natural gas given its clean burning activities and aims to convert India into a "Gas Based Economy" by 2030. Besides, as of now, India uses only ~6.2% of its energy requirement through gas and government wants to improve it to around 15% by 2030.

Liquidity: Strong
Liquidity position of GAIL remained strong a total cash and bank balance of Rs. 1675 crore as on September 30, 2020 as against Rs. 1250.17 crore as on March 31, 2020. Its operating cycle remained comfortable at 22 days in FY20 as against 14 days in FY19. The company is also undertaking major expansion projects while maintaining high cash reserves. Being a renowned player in the gas utility industry, GAIL also enjoys low cost of borrowing from capital markets as compared with other competitors. Further, GAIL (standalone) has total cash and bank balance of Rs. 1922.46 crore as on December 31, 2020 on standalone level along with non-current investment in subsidiary, JV and associates of Rs. 5537.5 crore.

Analytical approach: The ratings are based on credit enhancement in the form of corporate guarantee from GAIL rated CARE AAA; Stable/ CARE A1+. CARE has considered consolidated financials of GAIL with notching based on linkages with Government of India.
Unsupported ratings: Standalone financials of Gail Gas Limited

Applicable Criteria
CARE's Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
CARE's criteria for Short Term Instruments
CARE's methodology for financial ratios (Non-Financial sector)
CARE's methodology for liquidity analysis (Non- Financial sector)
CARE's methodology for Factoring Government Linkages in Ratings
CARE's methodology for Credit Enhanced debt
CARE's methodology for Factoring Linkages in Ratings
Rating Methodology – Infrastructure Companies

About the Company: GAIL
GAIL (India) Ltd. (GAIL), India's principal gas transmission and Distribution Company, was set up by the Government of India (GoI) in August 1984 to create natural gas transportation and distribution infrastructure for development of the natural gas sector across the country. The company's activities range from gas transmission and distribution to processing (for fractionating liquefied petroleum gas (LPG), propane, Special Boiling Point (SBP) solvent and pentane), transmission of LPG, production and marketing of petrochemicals like High density polyethylene (HDPE) and Linear low-density polyethylene (LLDPE) and leasing bandwidth in telecommunications. Being the owner of largest gas pipeline infrastructure in India, GAIL has leveraged its position to extend its presence in power, liquefied natural gas (LNG) re-gasification, city gas distribution (CGD) and Exploration & Production (E&P) through various equity and joint venture participations.

Brief Financials (Rs. crore)	FY19 (A)	FY20 (A)
Total operating income	77,797	75,983
PBILDT	11,566	12,300
PAT	6,553	9,515
Overall gearing (times)	0.05	0.15
Interest coverage (times)	72.65	39.81

A: Audited

About the Company – GAIL Gas Limited

GAIL Gas Limited (GGL), a wholly owned subsidiary of GAIL (India) Limited [rated CARE AAA; Stable/ CARE A1+], was incorporated on May 27, 2008 for the implementation of City Gas Distribution (CGD) projects. GGL is engaged in the business of supplying piped natural gas (PNG) to domestic and commercial sectors and compressed natural gas (CNG) to the transport sector in areas authorized to them by Petroleum and Natural Gas Regulatory Board (PNGRB). GGL has been authorized by PNGRB for implementing CGD projects in Madhya Pradesh (Dewas), Haryana (Sonepat), Uttar Pradesh (Meerut), Taj Trapezium Zone (TTZ) (Firozabad, Fetehpur Sikri, Bharatpur, Govardhan and Vrindavan) except Agra and Mathura (where the company is only doing PNG commercial business), Uttarakhand (Dehradun District), Odisha (Ganjam, Nayagarh and Puri Districts), Jharkhand (Giridih and Dhanbad Districts), Karnataka (Dakshina Kannada Districts), Odisha (Sundargarh and Jharsuguda district) Jharkhand (Seraikela-Kharsawan District), Jharkhand (West Singhbhum District), Madhya Pradesh (Raisen, Shajapur and Sehore Districts) and Uttar Pradesh (Mirzapur, Chandauli and Sonbhadra Districts).

Brief Financials (Rs. crore)	FY19 (A)	FY20 (A)
Total operating income	5,342	5,110
PBILDT	159	263
PAT	81	156
Overall gearing (times)	0.12	0.22
Interest coverage (times)	73.76	28.17

A: Audited

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating History for last three years: Please refer Annexure-2

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Term Loan-Long Term	-	-	Dec 31, 2032	250.00	CARE AAA (CE); Stable
Un Supported Rating-Un Supported Rating (Long Term)	-	-	-	0.00	CARE AA

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Debentures-Non Convertible Debentures	LT	-	-	-	-	1)Withdrawn (03-Jul-18)	1)CARE AA; Stable (21-Mar-18) 2)CARE AA; Stable (21-Apr-17)
2.	Term Loan-Long Term	LT	250.00	CARE AAA (CE); Stable	-	1)CARE AAA (CE); Stable (06-Mar-20) 2)CARE AA; Stable / CARE A1+ (11-Dec-19)	1)CARE AA; Stable / CARE A1+ (10-Jul-18)	-
3.	Un Supported Rating-Un Supported Rating (Long Term)	LT	0.00	CARE AA	-	1)CARE AA (06-Mar-20)	-	-

Annexure 3: Complexity level of various instruments rated for this Company

Sr. No.	Name of the Instrument	Complexity Level
1.	Term Loan-Long Term	Simple
2.	Un Supported Rating-Un Supported Rating (Long Term)	Simple

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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