Gujarat State Petronet Limited

October 08, 2018

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Rating Action
Long-term Bank Facilities	1,169.96 (Enhanced from 400.00)	**CARE AA+; Stable (Double A Plus; Outlook: Stable)**	Reaffirmed
Short-term Bank Facilities	100.00	**CARE A1+ (A One Plus)**	Reaffirmed
Long-term / Short-term Bank Facilities	2,800.00	**CARE AA+; Stable / CARE A1+ (Double A Plus; Outlook: Stable / A One Plus)**	Reaffirmed
Total	**4,069.96 (Rupees Four Thousand Sixty Nine Crore and Ninety Six Lakh only)**		

Details of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings for the bank facilities of Gujarat State Petronet Ltd. (GSPL) continue to derive strength from its established position as one of the largest players in the gas transmission business in India together with its leadership position in Gujarat, strategic location with connection to all major natural gas supply sources; along-with GSPL's synergies with Gujarat State Petroleum Corporation (GSPC) group which has presence across the energy (gas) value chain. GSPL's open access operating model and healthy profitability further acts as strong credit positives. The ratings also continue to factor in the increasing demand for natural gas from various consumer segments. The ratings of GSPL are further underpinned by its acquisition of majority stake in Gujarat Gas Limited (GGL; rated CARE AA; Stable/ CARE A1+), India's largest city gas distribution (CGD) company, which is expected to bring better synergies between the two companies; albeit this will lead to some moderation in GSPL's debt coverage indicators as this acquisition is largely funded through debt [total acquisition cost of Rs.3,267 crore is funded through loan of Rs.2,800 crore from Gujarat State Financial Services Ltd (GSFS) and balance through internal accruals]. However, as articulated by GSPL's management, CARE understands that there would be no further major debt funded acquisition by GSPL after the above-mentioned acquisition of GGL and that its Total Debt/ PBILDT would be under 3.50x in the foreseeable future.

The long-term rating of GSPL is, however, constrained due to moderate revenue visibility upon scheduled expiry of part of its Gas Transmission Agreements (GTAs) in the near to medium term [however, as per past experience, this is an ongoing process and over the years, the company has seen renewal of its contracts], project implementation and stabilization risks associated with its on-going capital expenditure programme especially the two very large sized projects being implemented through Joint Ventures (JVs), its vulnerability to regulatory risk and refinancing risk associated with loan availed from GSFS.

Ability of GSPL to renew the expiring GTAs, execution of ongoing projects (including those within its JVs) as per envisaged time and cost parameters while maintaining its profit margins & capital structure would be the key rating sensitivities. Furthermore, undertaking any additional major debt funded acquisition, non-adherence to maintaining a Total Debt/PBILDT of below 3.50x and its inability to refinance the term loan availed for stake acquisition in GGL in a timely manner as previously envisaged would be the key credit monitorables.

Detailed description of the key rating drivers

Key Rating Strengths

Presence of GSPC group across the natural gas value chain: GSPL is promoted by GSPC, which is engaged in oil and gas exploration and production as well as trading of gas. GSPC's allotted blocks are spread in India and it has an established presence in its gas trading business in Gujarat, which is the largest gas-consuming state in the country. GSPC along with its subsidiaries and associates operates across the natural gas value chain with presence in bulk gas trading, gas transmission and city gas distribution (CGD) through GGL and Sabarmati Gas Ltd. Accordingly, it provides significant synergies to the operations of GSPL for transportation of gas.

Strategic location in highest natural gas consuming state: GSPL commenced its operations with transmission of gas being provided by GSPC. Over a period of time, GSPL has however, invested significantly in developing its pipeline network which are now connected to major gas supply sources in Gujarat including designated collection points near the natural gas fields of Cairn Energy, GSPC and GSPC-Niko (all located in Hazira), re-gassified LNG from Shell's terminal at Hazira, Petronet LNG Ltd.'s terminal at Dahej along with the Panna-Mukta-Tapti gas fields. Further, Gujarat is the primary

[1]*Complete definitions of the ratings assigned are available at www.careratings.com and in other CARE publications.*

origination or entry point for both domestic natural gas produced in the Arabian Sea and imported LNG for Western and Northern India, owing to its strategic location and oceanic access to LNG exporting countries in the Middle East and Asia. Furthermore, it is also the highest natural gas consuming state with around 40% of total domestic gas consumption. All these factors translate into steady utilization of GSPL's transmission lines.

Operating on an open access basis: GSPL is a pure gas transmission company operating on an open access basis; and it does not purchase or sell natural gas. Open access enables natural gas consumers to separately negotiate their natural gas supplies from a number of suppliers. In addition, operating on an open access basis allows GSPL to target both natural gas suppliers and users resulting in increased revenues from a broader customer base. Operating as a transmission only entity helps GSPL to minimize risks associated with fluctuations in natural gas prices. However, GSPL won authorization for establishing and operating a CGD network development in Amritsar and Bhatinda in FY16 and FY17 respectively in Punjab, due to which it would be marginally exposed to natural gas price fluctuations once it commences its operations in these regions.

Gas Transmission Agreements (GTA) provide medium-term revenue visibility: GSPL enters into gas transmission agreements with its customers which typically provide for commercial terms such as quantity, quality, schedule, payment terms, security terms, events of default and remedies for the transportation arrangements, the tenure of which ranges from 1 year to 15 years. Majority of GTAs also provide for 'ship or pay' for a minimum off-take requirement generally covering around 90% of contracted volume, which require customers to pay transportation tariff regardless of the volume of natural gas actually transported. GSPL has various contracts on hand with reputed clients located in the region, which includes large industries and city gas distribution entities which use natural gas either as feedstock, fuel or supply it for further distribution. Total contracted value on hand as on August 1, 2018 was 41.67 mmscmd which provides a medium term visibility to its revenue stream. Further, majority of GTAs which expired during FY18 have been largely renewed.

Low level of competition because of regulatory business: GSPL, with its 2518 km as on March 31, 2018 long pipeline network, is presently the second largest gas transmission pipeline network operator in the country (after GAIL). GAIL's market share is around 70% in gas transmission business, with primary focus towards serving Western and Northern India. In contrast, GSPL has an extensive network in Gujarat, covering 25 out of 33 districts in the state. GSPL follows leading strategy and develops pipeline network in newer markets after a thorough research and potential for gas demand from various segments of users. Furthermore, for laying any pipeline, GSPL and other players would have to undergo bidding process to obtain authorization from PNGRB which ensures no duplication of pipeline and low level of competition.

Increasing demand for natural gas: In India, natural gas contributes around 6% of the overall energy mix where major consuming sectors include fertilizers, petrochemicals and sponge iron (as feedstock) along with power and CGD (as fuel). Natural gas sales increased y-o-y by around 5% in FY18. Power & fertilizer sector have always been the biggest contributor to India's total natural gas demand, but the contribution of natural gas in total installed power generating capacity is relatively low compared with other countries. To increase production to meet future demand and reduce the uncertainty for various stakeholders, new policy based on revenue sharing model has also been devised for the marginal fields along with providing pricing freedom for deep-water and ultra deep-water blocks. Further, there is clarity on pricing of gas under the administered pricing mechanism (APM) with revision every six months linked to international market prices. Further, infrastructure facilities for unloading, storage and re-gasification of imported LNG is also being improved by expansion at existing terminals and greenfield capacities being established at various locations across the country.

Comfortable financial risk profile: GSPL's total operating income increased by 26% y-o-y in FY18 on the back of increase in volume of gas transportation owing to reduction in domestic as well as international gas prices which led to improved competitiveness of gas vis-à-vis other fuels. It continued to operate at healthy PBILDT margin of 86.80% in FY18. Further, its capital structure was comfortable with an overall gearing of 0.60x as on March 31, 2018.

Synergetic benefit from GSPL's investments in GGL; albeit expected moderation in debt coverage indicators going forward: GSPL's acquisition of additional stake of 28.40% in GGL is envisaged to provide synergetic benefits to both the companies as they are part of the same value chain of natural gas business. CGD is one of the largest category of industry segments catered to by GSPL which is envisaged to grow further in view of the increased thrust of the government and regulatory authorities to expand the CGD network across the country. According to the company management, GGL's business being complementary to GSPL, the proposed transaction would facilitate better synchronization of its gas transmission network with GGL's network. Further, Gujarat being nearly 1/3rd of the gas consumption market in India, the acquisition of stake is expected to bring better synergies between the businesses of GSPL and GGL as CGD network provides last mile connectivity to the end users of natural gas. GGL is also GSPL's largest customer with approximately 14% share in its total sales.

The total acquisition cost of around Rs.3,267 crore is funded through loan of Rs.2,800 crore from GSFS and the balance through internal accruals. The healthy level of free cash & bank balance earlier available with GSPL is expected to moderate on account of this acquisition. The loan from GSFS is proposed to be prepaid/ repaid within 3 years through internal accruals to the extent possible and re-financing with a long term debt.However, due to the predominantly debt funded stake purchase, GSPL's overall gearing ratio, Total Debt/ PBILDT and debt coverage indicators are expected to witness moderation compared to previous levels. But, GSPL's management has articulated to CARE that no further major debt-funded acquisition plans are in the pipeline and that the company shall endeavour to maintain a Total Debt/PBILDT within 3.50x for the foreseeable future.

Key Rating Weaknesses

Risk associated with its large-size capex and investment plans being implemented through its two JVs: GSPL has planned to undertake capex over the next five years towards expansion of existing pipeline network, laying new spur lines, capacity augmentation and for establishing CGD network in Amritsar and Bhatinda. Further, in July 2011, PNGRB had awarded the GSPL led JVs to lay pipelines on three routes. viz. Mehsana-Bhatinda (~1,670 km), Bhatinda-Jammu-Srinagar (~740 KM) and Mallavaram-Bhilwara Pipeline (~1,881 km). GSPL has formed two SPVs namely - GSPL (India) Gasnet Limited (GIGL) for implementation of the first two routes and GSPL (India) Transco Limited (GITL) for the third one. GSPL owns 52% stake in these projects with the balance being held by Indian Oil Corporation Ltd. (IOCL; 26%), Bharat Petroleum Corporation Ltd. (BPCL; rated CARE AAA; Stable/CARE A1+; 11%) and Hindustan Petroleum Corporation Ltd. (HPCL; 11%).

The total project cost for the two JVs was originally estimated at around Rs.13,000 crore to be funded in a debt to equity ratio of 70:30. Some of the segments out of the above projects are already awarded and some more are likely to be awarded in the near to medium term. Execution of these projects within envisaged time and cost parameters and realising envisaged benefits therefrom would be very critical for GSPL.

Apart from the above JV projects, GSPL is also expected to undertake own capex of around Rs. 1500-2,000 crore over the next 4-5 years.

Exposure to regulatory risk: GSPL's high pressure and low pressure pipeline network had been authorized by Petroleum and Natural Gas Regulatory Board (PNGRB). PNGRB had issued provisional tariff order for GSPL's high pressure and low pressure pipeline network. Subsequent to the order brought out by PNGRB, which was sought to be implemented on retrospective basis from November 2008, Appellate Tribunal for Electricity (APTEL) held that the date of applicability of transportation tariff determined by PBGRB should be from date of authorization. Further, APTEL in its order dated November 25, 2014 has directed PNGRB to reconsider the tariff proposal submitted by GSPL and incorporate various communication/representations made by GSPL in this connection from time to time. Hence, GSPL remains exposed to regulatory risk.

On September 27, 2018, PNGRB has issued orders for final initial unit natural pipeline tariff for GSPL's high pressure and low pressure pipeline network.

Analytical approach: Standalone with planned investments in JV entities and guaranteed debt

Majority of GSPL's income and cash flows are generated from its core gas transmission business. Hence, a standalone approach has been considered for analysis. However, the equity support envisaged to be provided by GSPL for their project implementation in its two JVs, primarily for construction of their gas transmission pipelines, along with other planned investments has been suitably factored in the analysis. Also, GSPL has provided corporate guarantee for certain non-fund based bank guarantee limits to its JV entities, which have also been considered in the analysis.

Apart from those mentioned above, GSPL is not expected to impart any extraordinary support to any of its group entities including its subsidiary companies. Any change in this stance would be a key rating sensitivity.

Applicable Criteria

Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
Criteria for Short Term Instruments
Rating Methodology: Factoring Linkages in Ratings
Rating Methodology - Infrastructure Sector Ratings
Financial ratios – Non-Financial Sector

About the Company

Incorporated in December 1998, GSPL is promoted by GSPC, a Government of Gujarat (GoG) owned company, which is primarily engaged in oil and gas exploration and production (E&P) as well as gas trading business through transmission and distribution network of its subsidiaries including GSPL. GSPC held 37.65% equity stake in the company as on June 30, 2018. By virtue of provisions in the Articles of Association of GSPL, the right to appoint majority of its Directors vests with GSPC, hence GSPL is a subsidiary of GSPC. Furthermore, it is a Government Company as per Section 2 (45) of the

Companies Act, 2013. GSPL's primary business objective is to connect various supply sources and users of natural gas in Gujarat through its gas pipeline network. GSPL is the leader in natural gas transmission business in Gujarat and is the second largest player in India. It currently owns and operates around 2,518 km of gas transmission pipeline in the state of Gujarat as on March 31, 2018. GSPL also sells electricity generated through its 52.50 MW wind mills.

Brief Financials (Rs. crore)	FY17 (A)	FY18 (A)
Total operating income	1,110	1,394
PBILDT	971	1,210
PAT	497	668
Overall gearing (times)	0.14	0.60
Total Debt/PBILDT	0.65	2.53
Interest coverage (times)	16.29	34.17

A: Audited

During Q1FY19, based on its unaudited published results, GSPL registered total operating income of Rs.397 crore with PAT of Rs.144 crore as against total operating income of Rs.313 crore with PAT of Rs.153 crore during Q1FY18.

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

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

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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Annexure-1: Details of Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Term Loan	-	-	March 2027	1,169.96	CARE AA+; Stable
Fund-based - ST-Term loan	-	-	-	100.00	CARE A1+
Non-fund-based - LT/ ST-Bank Guarantees	-	-	-	2800.00	CARE AA+; Stable / CARE A1+

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 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016
1.	Fund-based - LT-Term Loan	LT	1,169.96	CARE AA+; Stable	-	1)CARE AA+; Stable (28-Mar-18) 2)CARE AA+; Stable (05-Oct-17)	1)CARE AA+ (18-Oct-16)	1)CARE AA+ (21-Oct-15)
2.	Fund-based - ST-Term loan	ST	100.00	CARE A1+	-	1)CARE A1+ (28-Mar-18) 2)CARE A1+ (05-Oct-17)	1)CARE A1+ (18-Oct-16)	1)CARE A1+ (21-Oct-15)
3.	Non-fund-based - LT/ ST-Bank Guarantees	LT/ST	2800.00	CARE AA+; Stable / CARE A1+	-	1)CARE AA+; Stable / CARE A1+ (28-Mar-18) 2)CARE AA+; Stable / CARE A1+ (05-Oct-17)	1)CARE AA+ / CARE A1+ (18-Oct-16)	1)CARE AA+ / CARE A1+ (21-Oct-15)

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CIN - L67190MH1993PLC071691