



CRISIL

Rating Rationale

May 31, 2011
Mumbai

'AA/Positive' Rating to Perpetual Debentures of Tata Power: CRISIL

Releases Criteria on Corporate Sector Perpetual Instruments; a First by any Rating Agency in India

CRISIL has assigned its 'AA/Positive' rating to The Tata Power Company Limited's (Tata Power's) issue of Rs.15 billion unsecured, listed, subordinated, perpetual debentures. Perpetual debentures, a kind of hybrid instrument, combine features of both debt and equity – CRISIL has accorded 50 per cent equity content to this instrument. It implies that CRISIL, in its analysis of Tata Power's capital structure and financial ratios, will treat 50 per cent of the principal amount as equity and the other half as debt. CRISIL has also reaffirmed its ratings on the company's existing debt instruments and bank facilities at 'AA/Positive/P1+'.

Says *Mr. Pawan Agrawal, Director, CRISIL Ratings*, "The rating of this instrument is based on an expectation that the embedded flexibility to defer distribution payments is unlikely to be used by the issuer." This expectation is based on an analysis of the key features of the instrument, as well as CRISIL's understanding of the management's intent. Therefore, this perpetual instrument is rated at the same level as other traditional long-term bonds issued by Tata Power. "The 50 per cent equity-content treatment to this instrument emanates from the presence of a strong replacement capital covenant and the instrument's deeply subordinated position in issuer's capital structure", adds *Mr. Agrawal*.

Such perpetual hybrid instruments provide several benefits to issuers. They allow a better balancing of capital structure, enhance financial flexibility, expand the choice of instruments that can be issued to access debt markets, and enable diversification in the investor base. For investors, such instruments offer a relatively higher return to compensate for the highly complex nature, a subordinated position, and a potential uncertainty over timing of maturity and risk of distribution deferral.

Considering the emerging interest in such newer instruments by Indian debt market participants, CRISIL has released its detailed criteria for rating of perpetual securities issued by corporate sector entities. Says *Mr. Arun Panicker, Chief Analytical Officer, CRISIL Ratings*, "CRISIL has become the first Indian rating agency to publish its comprehensive analytical framework for rating such securities in the public domain. This highlights CRISIL's commitment towards enabling innovation in Indian market, enhancing transparency in the market place by providing participants with an opinion on risks in newer domains, building investor confidence in our risk assessment capabilities, and facilitating development of Indian debt markets." The detailed criteria document is available at our website www.crisil.com.

CRISIL Complexity Levels are assigned to various types of financial instruments. The CRISIL Complexity Levels are available on www.crisil.com/complexity-levels. Investors are advised to refer to the CRISIL Complexity Levels for instruments that they propose to invest in. Investors can also call the CRISIL Helpline at +91 22 3342 3047 / + 91 22 3342 3064 with queries on specific instruments.

Rated instrument details

Rs.15 Billion Perpetual Non-Convertible Debentures	AA/Positive (Assigned)
Non-Convertible Debentures Aggregating Rs.22 Billion*	AA/Positive (Reaffirmed)
Rs.18.25 Billion Cash Credit/Working Capital Demand Loan	AA/Positive (Reaffirmed)
Rs.0.7 Billion Over Draft/ Working Capital Demand Loan	AA/Positive (Reaffirmed)
Rs.1.5 Billion Term Loan	AA/Positive (Reaffirmed)
Rs.30.7 Billion Letter of Credit/Bank Guarantee	P1+ (Reaffirmed)
Rs.5 Billion Short-Term Debt Programme	P1+ (Reaffirmed)

*Outstanding amount as on March 31, 2011.

Salient features of the instrument

- No defined maturity date
- Fixed coupon/ distribution rate of up to 11.6% per annum
- First call option at the end of year 10
- Up to 200 basis points (bps) step-up after 10 years
- Optional deferral of coupon linked to non-payment of dividend, subject to a six month lookback period
- A dividend stopper clause that restricts payout of dividend on equity shares if the distributions on the perpetual instrument are deferred and in arrears
- Existence of a replacement capital covenant (RCC) which ensures that the instrument can be redeemed by issuance of similar or higher equity-content instrument(s). The RCC will apply for 30 years and will cease to be applicable if, among other covenants, the credit rating of Tata Power is upgraded to 'AA+' by CRISIL.

CRISIL has categorised this instrument as highly complex.

References

1. Recent rating rationale for traditional debt ratings, "*CRISIL reaffirms ratings on The Tata Power Company Ltd.*", dated May 6, 2011
2. CRISIL's criteria for Corporate Sector Hybrids (Including Perpetual Securities), dated May 2011
3. Credit FAQ, "*Tata Power's Perpetual Debentures*", dated May 2011

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