

Nayara Energy Limited

November 16, 2018

Summary of rated instruments

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Commercial Paper Programme	200.00	[ICRA]A1+; Assigned
Total	200.00	

*Instrument details in Annexure-1

Rating action

ICRA has assigned a short-term rating of [ICRA]A1+ (pronounced ICRA A one plus) to the Rs. 200 crore¹ commercial paper programme of Nayara Energy Limited (Nayara)².

Rationale

While arriving at the rating, ICRA has taken a consolidated view of Nayara Energy Limited and its two subsidiaries, Vadinar Oil Terminal Limited (VOTL; 97.63% stake) and Vadinar Power Company Limited (VPCL; 100% stake).

The rating takes into account the high complexity of the company's refinery in Vadinar (Gujarat) which enables the refinery to process low cost heavy/ultra-heavy crude oil grades and produce higher grade products leading to healthy gross refining margin (GRM) that has been consistently higher than the industry average. The rating also considers the strategic coastal location of the refinery which helps the company save on freight costs for both, crude oil imports and petroleum products exports. The company further benefits from the presence of a captive oil terminal and a 1,010 MWe captive power plant which provides it with cost advantages. Further, the rating takes into account the favourable outlook for domestic petroleum products demand growth and healthy prospects for exports given the refinery's ability to meet stringent product specifications. The rating favourably considers the company's healthy liquidity profile characterised by sizeable cash and cash equivalent balances of Rs. 3,966 crore as of June 30, 2018, steady cash accruals from operations, and adequate unutilised working capital limits. In addition, the company has completed refinancing its debt over the past one year that has led to elongation of tenure of term loans and reduction in the average cost of borrowing.

The rating also takes into account the strong ownership of the company, post the acquisition from the erstwhile owners in August 2017, with the shareholding now divided between Rosneft Singapore Pte Ltd. (49.13% stake; a subsidiary of PJSC Rosneft Oil Company, a major Russian oil and gas company, rated 'Baa3' with stable outlook by Moody's); and Kesani Enterprises Company Limited (49.13% stake), a consortium led by Trafigura Pte Limited (a Singapore based commodity trading company) and United Capital Partners (a Russia-based investment group). The change in ownership has been accompanied by change in key management personnel as well as the company's board composition that includes highly experienced and reputed names in the energy and commodities sector. The presence of major global entities as shareholders gives Nayara access to newer markets for its products as well as for crude procurement along with enhancing its fund-raising ability at competitive rates. ICRA has taken note of the US sanction on Rosneft. However, Nayara's shareholding structure is compliant with the US sanctions as Rosneft's shareholding in Nayara is below 50%.

¹ 100 lakh = 1 crore = 10 million

² For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications

ICRA, however, notes that the company's profitability would remain vulnerable to the import duty differential, commodity prices cycles, and forex movements. Nonetheless, the company has a board approved hedging policy which largely alleviates the risk associated with pricing and currency movements. The company's operations are also exposed to asset concentration risk being a single-location refinery, though the company has adequate insurance policies to cover for business interruption and property damage. Also, the loss-free track record due to robust operational practices offers comfort. Further, the company's gearing and debt protection metrics remain moderate and the short term working capital requirements may further increase in the near term as the company has ceased to procure crude from Iran (due to the US sanctions) wherein the credit terms used to be favourable. Any sizeable debt-funded capex undertaken by the company would remain a key rating sensitivity.

Key rating drivers

Credit strengths

Efficient refining operations with high capacity utilisation; higher-than-average refinery complexity – The company's refining operations have remained healthy with consistently high capacity utilisation (104% in FY2018). Nayara's refinery has a high complexity with a Nelson Complexity Index³ of 11.8 implying the refinery's ability to process a wide range of crude oil grades including low-cost heavy/ultra-heavy grades and producing high quality premium products, thereby widening the refinery's gross refining margin (GRM). Nayara's GRM has been consistently higher than the Singapore refining benchmark. In FY2018, the company reported a GRM of ~US\$9.0 per barrel⁴ as against the Singapore benchmark of US\$7.2 per barrel.

Location advantages of being a coastal refinery; cost benefits arising from captive terminal and power plant – The company's refinery is located at Vadinar in Gujarat and enjoys proximity to the Kandla port leading to freight cost savings for import of crude oil and export of petroleum products. The refinery has a fully-integrated set-up with a captive oil storage and handling terminal and a captive power plant both of which provide various operational advantages. The terminal under VOTL is an all-weather port located at Deendayal Port Trust and has a 32-meter draft with an intake capacity of 27 million metric tonne per annum. It is equipped with one Single Buoy Mooring (SBM) unit, two product jetties, multiple gantries and storage tankers and is capable of handling Very Large Crude Carriers (VLCCs). The company operates a coal-based power plant to fulfil refinery's power and steam requirements. Both, the terminal and the power plant, provide significant cost savings to the company.

Strong shareholders profile – The company benefits significantly from its shareholders' (Rosneft, Trafigura and UCP) well-established position who acquired Nayara along with its subsidiaries in August 2017 for an enterprise value of US\$12.9 billion. The company also stands to gain from Rosneft's strong business profile as the world's largest public oil company in terms of reserves and production and its preferential access to oil and gas resources and Trafigura's expertise being one of the world's largest traders by volume of crude oil and petroleum products. Out of the 12 directors on the company's board, four nominees are from Rosneft and two nominees are from Trafigura and UCP, each.

Healthy liquidity profile – The company has a healthy liquidity profile characterised by sizeable cash and liquid investments of Rs. 3,966 crore as of June 30, 2018 and steady cash accruals from operations. Further, the liquidity position is supported by adequate unutilised working capital limits.

³ Nelson Complexity Index is an indicator of the sophistication of a refinery in terms of its processing and refining ability

⁴ Company reported GRM is on CP (Current Price) basis

Credit weaknesses

Profitability exposed to volatility in crude oil prices and forex rates, besides the level of import duty differential -

Given the nature of the business, the company's profitability would remain vulnerable to the movement in the commodity price cycles and the volatility in crude prices. However, the company has a board approved hedging policy in place whereby it hedges the crack spreads for various distillates on a case-to-case basis and hedges its entire crude inventory exposure which protects it from any crude price fluctuations during the shipment and storage period. The company's profitability is also exposed to the forex rates given the business is largely dollarized on sales, crude procurement and forex debt though the risk is largely mitigated because of the natural hedge provided by the nature of the company's operations. With refining business being low value-add in nature, the extent of differential in import duties between the petroleum products and crude oil, especially for domestic sales, will be crucial to the company's margins as the domestic sales are at Refinery Transfer Pricing (80% Import Parity Price + 20% Export Parity Price) and any decline in import duty of a petroleum product could adversely impact the profitability.

Asset concentration risk for being a single location refinery – The company's operations are exposed to asset concentration risk being a single location refinery. However, the company has adequate insurance policies to cover any risk related to property damage and business interruption. Further, the risk is mitigated to a large extent due to robust operational practices implemented by the company, which has resulted in a loss-free track record of the refinery over more than 10 years.

Moderate leverage levels and debt protection metrics – The company's gearing levels and debt coverage metrics remain moderate as of March 31, 2018 owing to sizeable debt on its books. However, after the acquisition, the company's management has taken steps to complete refinancing of existing debt with lower borrowing costs and extended tenure of repayment. ICRA notes the company's commitment to deleverage the balance sheet and improve the debt coverage metrics over the medium term.

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 Downstream Oil Companies](#)

About the company:

Nayara Energy Limited (Nayara), formerly known as Essar Oil Limited (EOL), was incorporated in 1989. It was rebranded as Nayara Energy Limited after it was acquired by Russian oil major PJSC Rosneft Oil Company (rated Baa3 / Stable by Moody's) through a direct subsidiary, and a consortium of commodity trading company Trafigura and Russia-based private investment group United Capital Partners (UCP) in August 2017 for an enterprise value of US\$12.9 billion. Nayara is engaged in oil refining and marketing and owns India's second largest single-location oil refinery (Vadinar, Gujarat) with a capacity of 20 million metric tonnes per annum (equivalent to ~405,000 barrels per day). The refinery has access to a deep-draft port capable of receiving VLCC tankers. Nayara is also involved in retail marketing of motor spirit and high-speed diesel and has been ramping up its marketing operations with 4,833 operational outlets and 2,688 under-construction outlets as of September 30, 2018.

Key financial indicators (audited)

	FY2017	FY2018
Operating Income (Rs. crore)	60,869	70,815
PAT (Rs. crore)	-2,755	577
OPBDIT/ OI (%)	13.8%	10.2%
RoCE (%)	3.9%	8.5%
Total Debt/ TNW (times)	1.5	1.3
Total Debt/ OPBDIT (times)	3.2	3.8
Interest coverage (times)	2.2	2.1

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years:

Current Rating (FY2019)					Chronology of Rating History for the past 3 years			
Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2018	Date & Rating in FY2017	Date & Rating in FY2016	
1 Commercial Paper Programme	Short-Term	200.00	-	Nov 2018 [ICRA]A1+	NA	NA	NA	

Source: Nayara Energy Limited

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
NA	Commercial Paper Programme	-	-	7-365 days	200.00	[ICRA]A1+

Source: Nayara Energy Limited

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