July 29, 2020

Indian Oil Corporation Limited: Rating assigned to bond programme

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-Convertible Debenture Programme	8000.00	8000.00	[ICRA]AAA(Stable); Outstanding
Non-Convertible Debenture Programme	0.00	2000.00	[ICRA]AAA(Stable) assigned
Commercial Paper	40,000.0	40,000.0	[ICRA]A1+; Outstanding
Total	**48,000.0**	**50,000.0**	

**Instrument details are provided in Annexure-1*

Rationale

The ratings factor in IOC's high financial flexibility arising from its large sovereign ownership (51.5% stakes owned by the GoI), significant portfolio of liquid investments (~ Rs. 19,036 crore as on March 31, 2020 including GoI bonds and investments in GAIL (India) limited (GAIL, rated [ICRA]AAA(stable)/[ICRA]A1+), Oil & Natural Gas corporation (ONGC, rated [ICRA]AAA(Stable)/[ICRA]A1+) and Oil India limited (OIL) as on March 31, 2020), and ability to raise funds from the domestic/foreign banking system and capital markets at competitive rates. Besides, the ratings of the company continue to reflect its dominant and strategically important position in the Indian energy sector, its integrated business model and its role in fulfilling the socio-economic objectives of the GoI.

The ratings take into account the diversified location base of the company's refineries (11 refineries on a consolidated basis). The ratings also reflect integration of IOC in marketing, pipelines, and petrochemicals segments which enables reducing the earnings volatility related to the crude oil refining segment. The ratings also factor in the vulnerability of the company's profitability to the global refining margin cycle, import duty protection, and INR-USD parity levels. IOC is also exposed to project implementation risks as it is in the midst of implementing large projects spanning the entire downstream value chain, though the risk is largely mitigated by the company's proven track record of successfully implementing several large projects. The Gross Refining Margins (GRMs) of the company weakened materially to $0.08/bbl in FY2020 as against $5.4/bbl in FY2019, owing to the significant inventory losses of Rs. 16,184 crore (~$2.56/bbl) incurred in FY2020. The core GRMs of the company were also impacted due to weak crack spreads which along with large inventory losses resulted in very low GRM and thus cash generation from the refining operations. The GRMs are expected to remain weak in FY2021 as well driven by lower capacity utilisation of refineries and weak crack spreads as the global economic activity is expected to remain subdued owing to the Covid-19 pandemic. The operations of the company have normalised to a large extent post the relaxations in lockdowns resulting in refineries operating at around 90% capacity utilisation and petrochemical plants also operating at near full capacity. In the marketing segment, the marketing margins have reverted to normal levels post the hike in excise duty by GoI and with the auto fuel sales slowly picking up, the marketing segment is expected to provide support to the cash generation of the company.

IOCL will continue to be subjected to regulatory risks related to the pricing of sensitive petroleum products in an elevated crude oil price environment, however the past track record of the GoI to ensure low under-recovery levels for PSU OMCs provides comfort from the credit perspective. Any adverse change in the GoI's policy in this regard, resulting in a weakening of key credit metrics of IOCL will be a key rating sensitivity. As per ICRA's estimates, subsidy requirement for FY2021 will be Rs 90 billion, assuming Indian basket crude price of $35/bbl and INR/USD of 76.0. With lower crude oil prices, the working capital requirements of the company should ease somewhat in FY2021.

The Stable outlook on the [ICRA]AAA rating reflects ICRA's opinion that IOCL will continue to benefit from its dominant position in the domestic energy sector and its strategic importance to the GoI.

Key rating drivers and their description

Credit strengths

Strategic importance for the GoI in the domestic energy sector - IOC, being the largest oil refining and marketing company in India, commands considerable economic importance. The company holds significant strategic importance for GoI as it helps in meeting the socio-economic objectives of the government through control on prices of sensitive products like subsidised liquefied petroleum gas (LPG) and superior kerosene oil (SKO). The company is also the largest contributor to the government exchequer. Thus, the sovereign support is expected to continue going forward as well.

Dominant position in the domestic refining and marketing business - The company dominates the domestic refining sector with a share of ~32.6%. The company is also the leading public oil marketing company with a ~39.9% market share (including private players) as of end of FY2019 (as per consumption data from Petroleum Planning & Analysis Cell, PPAC). The company has the largest marketing network spanning across the country and actively undertakes multiple branding and customer loyalty initiatives.

Diversified location base of the refineries - The company owns and operates nine refineries spread across the country besides having a majority stake in Chennai Petroleum Corporation Limited (CPCL), which provides it control over an additional two refineries, taking the aggregate to eleven. Seven out of its nine refineries are located in inland areas. The most recently set up refinery at Paradip, being situated at the coast, has improved IOC's diversification from the perspective of land-locked vis-à-vis coastal presence.

Integration in marketing, pipelines, and petrochemicals segments reducing cyclicality associated with the refining segment – IOC's large marketing operations generate largely stable profits, although subject to risks related to regulatory developments and inventory gains/losses to some extent. Further, a large pipeline infrastructure owned by the company also results in stable cash generation for the company. The forward integration of IOC into petrochemical segment provides operational synergies, like conversion of surplus products in the country such as naphtha, into higher value petrochemicals (like HDPE, PP etc), which also lead to higher margins. Overall, significant integration across segments reduces the risks related to refining operations.

Considerable liquidity and financial flexibility derived from its investment portfolio and significant sovereign ownership: IOC continues to enjoy high financial flexibility, that has enabled it to borrow from the domestic and overseas banking system and capital markets at competitive rates, to fund its large working capital requirements and for project finance. The same is supported by IOC's strong parentage arising from the GoI's 51.50% stake. The company's investments in ONGC, GAIL, and Oil India with current aggregate market value of ~Rs. 8,015.0 crore as on March 31, 2020 besides unsold stock of GoI Special Oil bonds and GoI securities of ~Rs. 11,021 crore as on March 31, 2020 provide considerable financial flexibility.

Credit challenges

Vulnerability of the company's profitability to the global refining margin cycle, import duty protection, and INR-USD parity levels - Given the nature of the business, the company would remain exposed to the movement in the commodity price cycles and the volatility in the crude prices. Any adverse changes in the import duty on its products would also have an impact on the company's domestic sales. The company's profitability is also exposed to the forex rates (INR-US$) given the business is largely dollarized on sales, crude procurement and foreign currency loans.

Exposed to regulatory risks related to under-recoveries in an elevated crude oil price environment; consistent fall in consumption of kerosene to partly offset the risk – Higher crude oil prices, if sustained, lead to material increase in gross under-recoveries (GURs) as was witnessed in H1 FY2019 and consequently raise the working capital requirements and short-term debt levels of OMCs, thereby negatively impacting their profitability. ICRA expects GURs for OMCs to moderate from Rs. 245 billion in FY2020 to ~Rs. 90 billion in FY2021 (at crude price of US$35/bbl and INR/USD of 76.0). Additionally, through a direct intervention by the Government of India (GoI) in October 2018 the OMCs were directed to reduce selling prices of Motor Spirit (MS) and High-Speed Diesel (HSD) owing to elevated prices of these auto fuels. Accordingly, the regulatory risks for IOC related to pricing of sensitive petroleum products and auto fuels remains in an elevated crude oil price environment, however the past track record of the GoI to ensure low under-recovery levels for PSU OMCs provides comfort from the credit perspective. Any adverse change in the GoI's policy in this regard, resulting in a weakening of key credit metrics of IOCL will be a key rating sensitivity

Significant project implementation risks, partly mitigated by the long-demonstrated history of IOC in implementing projects across refining, marketing, petrochemicals and pipelines segments: The company has significant capex plans spanning the entire downstream value chain with an outlay of ~Rs. 2,000 billion over next 6-7 years. The capex plans include the ongoing up-gradation of refineries for production of BS-VI compliant fuel, brownfield expansion of refineries, setting up of nearly 6,500 km of pipeline infrastructure, investments in setting up of retail infrastructure, setting up of petrochemical plants etc. Besides the company is also planning to set-up a mega refinery under a JV with other two PSU OMCs along with ADNOC and Saudi-Aramco on the west coast of India for nearly $60 billion (IOC's share of $15 billion). Any material time or cost overruns in the group projects could lead to an increase in the company's borrowing levels and moderation of credit metrics. However, the risk is largely mitigated by the company's proven track record of successfully implementing several large projects.

With the company increasing its upstream portfolio it is exposed to geological, technology and execution risks that are inherent in E&P activities – The company currently has upstream portfolio of 22 blocks (domestic and overseas) and has been actively trying to expand the same. However, increasing presence in the upstream sector exposes the company to geological, technological and execution risks that are inherent in E&P activities.

Liquidity position: Strong

IOCL's liquidity profile is expected to remain strong aided by adequate cash flow generation expected in FY2021 and sizeable short-term investments of ~Rs. 11,021 crore (including the GOI oil bonds and government securities) as on March 31, 2020. The company enjoys strong access to capital markets and high financial flexibility due to sovereign ownership.

Rating sensitivities

Positive triggers -NA

Negative triggers – Downward pressure on IOCL's ratings could arise in the event of i) weakening in linkage with the GoI reduction in GoI's stake to below 51% ii) material increase in the net under-recoveries in a scenario of elevated crude oil prices or change in the under-recovery mechanism/pricing regime and delay in the under-recovery payout by the GoI.

Analytical approach:

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Downstream Oil Companies
Parent	Government of India: The ratings factor in implicit support from GoI in terms of support of the Gross Under Recoveries for LPG and SKO being borne by the GoI thus supporting the profitability of PSU OMCs.
Consolidation	For arriving at the ratings, ICRA has considered the consolidated financials of IOCL. ICRA has factored in the rated entity's support to fund the equity component of the investment in its JV projects, any cost overruns and, and debt servicing support in the initial stage of operations. The subsidiaries and JVs of IOCL that have been considered are enlisted in Annexure 2.

About the company:

IOC is currently the largest corporate entity in India by sales. Government of India has 51.5% equity stake in the company. The company and its subsidiaries have a total refining capacity of 80.7 MMTPA, which is 32.5% (as on March 31, 2020) of the total domestic refining capacity. The company accounted for 39.9% of the total petroleum products sold within the country in FY2019. IOC also enjoys a dominant presence in the domestic crude and product transportation business, controlling significant share in the country's total downstream pipeline capacity. The company has interests across the gas value chain as well, from LNG import terminals to city gas distribution networks (CGD). The company currently operates CGD networks in Agra and Lucknow through Green gas Limited (joint venture with GAIL (India) Limited); besides, the company is also implementing CGD projects in Chandigarh, Allahabad, Panipat, Daman, Ernakulam, Udhamsingh Nagar, and Dharwad through IndianOil-Adani Gas Private Limited - a JV with the Adani group.

Key financial indicators (Consolidated, audited):

	FY2019	FY2020
Operating Income (Rs. crore)	5,28,148.9	4,84,362.3
PAT (Rs. crore)	15,889.47	-3,242.41
OPBDIT/OI (%)	7.03%	1.14%
RoCE (%)	15.47%	-0.96%
Total Outside Liabilities/Tangible Net Worth (times)	1.9	2.4
Total Debt/OPBDIT (times)	2.6	23.4
Interest Coverage (times)	7.5	0.8
DSCR	0.9	0.1

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; DSCR= (Net Profit After Tax + Gross Interest + Depreciation) / (Gross Interest + long term & short term Repayment + Dividend on Preference Shares)

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2021)					Rating History for the Past 3 Years			
		Type	Amount Rated	Amount Outstanding	Rating		FY2020		FY2019	FY2018
					29-Jul-2020	26-May-2020	27-Feb-2020	10-Jan-2020	27-Feb-2019	11-Jan-2018
1	NCD	Long Term	2,000.0	Un-placed	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-	-	-
2	NCD	Long term	8,000.0	7,995.0	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-	-
2	Commercial Paper	Short Term	40,000.0	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

Amount in Rs. crore

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
INE242A08445	Non-Convertible Bonds	January 14, 2020	6.44%	April 2023	2000.0	[ICRA]AAA (Stable)
INE242A08452	Non-Convertible Bonds	March 6, 2020	6.39%	March 6, 2025	3000.0	[ICRA]AAA(Stable)
INE242A08460	Non-Convertible Bonds	May 27, 2020	5.05%	Nov 25, 2022	3000.0	[ICRA]AAA(Stable)
Un-placed	Non-Convertible Bonds	-	-	-	2000.0	[ICRA]AAA(Stable) assigned
NA	Commercial Paper	NA	NA	7-365 days	40,000.0	[ICRA]A1+

Source: IOC

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Chennai Petroleum Corporation Limited	51.90%	Full Consolidation
Indian Catalyst Private Limited	100.00%	Full Consolidation
IndianOil (Mauritius) Limited	100.00%	Full Consolidation
Lanka IOC PLC	75.10%	Full Consolidation
IOC Middle East FZE	100.00%	Full Consolidation
IOC Sweden AB	100.00%	Full Consolidation
IOCL (USA) Inc	100.00%	Full Consolidation
IndOil Global BV	100.00%	Full Consolidation
IOCL Singapore PTE Limited	100.00%	Full Consolidation
Indian Oiltanking Limited	49.38%	Equity Method
Lubrizol India Private Limited	26.00%	Equity Method
Indian Oil Petronas Private Limited	50.00%	Equity Method
Green Gas Limited	49.97%	Equity Method
Indian Oil Skytanking Private Limited	50.00%	Equity Method
Suntera Nigeria 205 Limited	25.00%	Equity Method
Delhi Aviation Fuel Facility Private Limited	37.00%	Equity Method
Indian Synthetic rubber Private Limited	50.00%	Equity Method
Indian Oil Ruchi Biofuels LLP	50.00%	Equity Method
NPCIL-Indian Oil Nuclear Energy Corporation Limited	26.00%	Equity Method
GSPl India Transco Limited	26.00%	Equity Method
Indradhanush Gas Grid Limited	20.00%	Equity Method

GSPL India Gasnet Limited	26.00%	Equity Method
IndianOil Adani Gas Private Limited	50.00%	Equity Method
Mumbai Aviation Fuel Farm Facility Private limited	25.00%	Equity Method
Kochi Salem Pipelines Private Limited	50.00%	Equity Method
Indian Oil LNG Private Limited	50.00%	Equity Method
Hindustan Urvarak & Rasayan Limited	29.67%	Equity Method
Ratnagiri Refinery & Petrochemicals Limited	50.00%	Equity Method
Avi-Oil India Private Limited	25.00%	Equity Method
Petronet VK limited	50.00%	Equity Method
Petronet LNG Limited	12.50%	Equity Method
Petronet India Limited	18.00%	Equity Method

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