March 19, 2021

ONGC Mangalore Petrochemicals Limited - Rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Commercial Paper	1,300.0	1,000.0	[ICRA]A1+; reaffirmed
Fund-Based Limits	1,750.0	2,050.0	[ICRA]A1+; reaffirmed
Non-Fund Based Limits	300.0	300.0	[ICRA]A1+; reaffirmed
Total	**3,350.0**	**3,350.0**	

Rationale

For arriving at the ratings, ICRA has considered a consolidated view of Mangalore Refinery and Petrochemicals Limited (MRPL) and ONGC Mangalore Petrochemicals Limited (OMPL) owing to the impending merger of these companies which is expected to be completed by Q2 FY2022. The reaffirmation of ratings favourably factors in the majority ownership of Oil and Natural Gas Corporation (ONGC; [ICRA]AAA(Stable)/[ICRA]A1+) and ONGC's continued support to MRPL, which is expected to be sustained given its strategic importance to ONGC's forward integration plans. The capacity utilisation levels at MRPL refinery were low in 9M FY2021 at ~66% due to the severe weakness in demand for petrol and diesel amid a lockdown across the country following the COVID-19 pandemic, however, overall demand for key petroleum products has started recovering from Q3 FY2021. Apart from the impact of the pandemic in YTD FY2021 and the water-led disruptions in H1 FY2020, the operational performance of MRPL's refinery has remained healthy in the past with utilisation levels consistently above 100% and the healthy ramp up of operations at its polypropylene unit. The GRM levels have been weak in FY2020 and FY2021 owing to weak crack spreads for the light and middle distillates. There is no significant recovery expected in the GRMs as the refining cycle is expected to remain weak going forward. The ratings also take into account the strong financial flexibility of MRPL due to its strong parentage besides which the company has sizeable unutilised working capital limits. The ratings also factor in the location advantage enjoyed by the company being located close to the Mangalore port as well as its diversified crude sourcing.

In January 2021, MRPL completed the acquisition of ONGC's 49% stake in ONGC Mangalore Petrochemicals Limited (OMPL) for a cash consideration of Rs. 1,217 crore thereby acquiring a 99.99% stake in the subsidiary. However, the merger between MRPL and OMPL is awaiting approvals from the Ministry of Corporate Affairs and is expected to be completed by Q2 FY2022. The merger will diversify MRPL's revenues and lower its exposure to the refining cycle. The merger is also expected to lead to operational synergies with optimisation of streams across MRPL and OMPL. The same will allow the company to decide the optimum product mix and suitable crude procurement to generate maximum profitability. However, the consolidation with OMPL, will add to MRPL's total debt obligations thereby moderating the debt coverage indicators of the combined entity. OMPL reported its first year of profitable operations in FY2019, since its commissioning in FY2015 owing to healthy paraxylene-naphtha spreads, however, the company's performance in FY2020 and 9M FY2021 has been adversely impacted by weak spreads for paraxylene and benzene. MRPL's total debt stood at Rs. 15,188 crore at a standalone level and at Rs. 22,738 crore (when combined with OMPL) as of December 31, 2020.

The low throughput levels coupled with weak cracks spreads for the light and middle distillates led to operating losses of Rs.104 crore for MRPL on a standalone level in 9M FY2021. At a consolidated level, the operating losses amounted to Rs. 137 crore. However, GRMs in Q4 FY2021 would be aided by recovery in demand for petrol and diesel and upswing in crude prices leading to inventory gains. The ratings also consider the asset concentration risk from being a single location refinery and the sensitivity of profits to the import duty differential, commodity price cycles and the INR-USD exchange rates.

Key rating drivers and their description

Credit strengths

Strong sponsor profile resulting in high financial flexibility - MRPL has a strong parentage with about 72% of its equity held by ONGC and about 17% by Hindustan Petroleum Corporation Limited ([ICRA]AAA (Stable)/ [ICRA]A1+). MRPL is strategically important to ONGC and is essentially managed by ONGC through its nominee directors and senior management. The chairman of ONGC acts as the chairman of MRPL's board of directors. ONGC had also extended loans to MRPL at favourable terms for part-funding of the large-size capital expenditure undertaken for refinery expansion. The company enjoys high financial flexibility on account of the parentage of ONGC.

Healthy operational profile - MRPL's refinery has been operating at more than 100% capacity utilisation for the last few years. The refinery has witnessed a healthy ramp up in operations since the commissioning of the Phase-III expansion and its polypropylene unit. However, in FY2020 the capacity utilization was lower than past years as there was loss of production owing to plant shutdowns due to water shortage and landslides. In 9M FY2021 capacity utilisation remained sub-optimal owing to the muted demand due to Covid-19 pandemic, however, there has been recovery in demand and utilisation levels in Q3 FY2021 and the current quarter.

Location advantages of being a coastal refinery for sourcing of crude as well as exports - The company's refinery is located on the western coast of the country close to the Mangalore port. The company's location is logistically advantageous for sourcing of crude as well as export of products.

Diversification of revenues as a result of merger with OMPL – The merger with OMPL, which is expected to be completed by Q2 FY2022, will diversify revenues and lower the exposure to the refining cycle. The combined entity will run its operations on an integrated basis leading to operational synergies. The company will optimise its product mix and crude procurement leading to higher profitability.

Credit challenges

Vulnerability of profits to the import duty differential on the domestic sales, commodity price cycles and forex fluctuations - Given the nature of the business, the company remains exposed to the movement in the commodity price cycles and the volatility in the crude prices. The company's GRM levels witnessed a considerable decline in FY2020 owing to weak crack spreads for light and middle distillates and high inventory losses and the weakness continued in 9M FY2021 due to the impact of the pandemic. Any adverse changes in the import duty on its products would also have an impact on the company's domestic sales. Besides, crude oil and most of petroleum products are priced in US$/bbl or US$/MT, which along with significant foreign currency debt, leads to vulnerability of the profits to foreign currency movements (especially INR-USD levels).

Weak financial performance of its subsidiary, OMPL – OMPL reported healthy revenue growth of 52% YoY in FY2019 largely driven by the increase in product realisations, though the growth in sales volumes remained muted owing to sub-par plant utilisation levels. In FY2020, OMPL recorded a significant decline of 42% YoY in operating income driven by both, decline in plant throughput and average realisation and a decline of 52.1% in operating income in 9M FY2021 owing to weakness in the paraxylene-naphtha spreads. OMPL has been operating with weak profitability levels since commissioning due to – a) inadequate supply of feedstock from MRPL which has resulted in lower-than-estimated plant utilisation levels, and b) relatively subdued crack spreads of its products and c) higher fuel costs due to non-availability of natural gas. The paraxylene-naphtha spreads witnessed sharp improvement in FY2019 following a tight supply situation due to shutdown of certain paraxylene capacities as well as healthy product demand. As a result, the company's operating profits grew 217% YoY in FY2019. However, the spreads underwent a significant correction in FY2020 with sizeable new capacities coming on stream in China along with lower utilization levels leading to operating losses of Rs. 531 crore in FY2020 as against operating profit of Rs. 988 crore in FY2019. The company also incurred forex losses of ~Rs. 174 crore in FY2020 which along with high depreciation led to a net loss of Rs. 1,400.4 crore in FY2020. In 9M FY2021, OMPL managed to contain its operating losses to Rs. 49 crore in an operating environment where paraxylene spreads reached five-year lows. The company produced higher volumes of reformate, a product used in Motor Spirit (MS) blending, and this production optimisation supported the company's profitability to some extent. Natural gas line from Cochin to Mangalore is commissioned and OMPL has started using natural gas from beginning of

February 2021. The plant utilisation levels have recovered to a large extent in Q4 FY2021. Further, OMPL has high debt levels (~Rs. 7,550 crore as of December 31, 2020) that would lead to moderation in the combined entity's debt coverage indicators.

Asset concentration risk as a single location refinery - MRPL has refining operations only at Mangalore, Karnataka and derives all its revenues from the same. The operations at one location expose it to asset-concentration risks related to natural calamities, accident at the plant etc. Nonetheless, the risk is partly mitigated by various insurance covers that address these risks.

Liquidity position: Adequate

The liquidity of MRPL is expected to remain adequate given sufficient buffer in the form of unutilised working capital limits. Even though the company has incurred large cash losses in FY2020 and has large repayment obligations going forward, the same are expected to be met partly from accruals and partly refinanced. The ability to the company to raise funds from banks and capital markets at fine rates provides comfort from a liquidity perspective.

Rating sensitivities

Negative factors - Downward pressure on MRPL's ratings could arise i) in case the credit profile of the ONGC Group weakens or ii) the linkage between ONGC and MRPL weakens, or iii) any significant deterioration in MRPL's standalone financial risk profile.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Downstream Oil Companies
Parent/Group Support	Parent - Oil and Natural Gas Corporation Limited We expect MRPL's parent, ONGC [rated [ICRA]AAA(Stable)/[ICRA]A1+], to be willing to extend financial support to MRPL, should there be a need, given the high strategic importance that MRPL holds for ONGC for meeting its diversification objectives
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of Mangalore Refinery and Petrochemicals Limited. As on March 31, 2020, the Company had 1 subsidiary and 1 JV, that are enlisted in Annexure-2.

About the company:

ONGC Mangalore Petrochemicals Limited (OMPL) was originally incorporated as Mangalore Petrochemicals Limited on December 19, 2006. The name of the company was subsequently changed to ONGC Mangalore Petrochemicals Limited on April 30, 2007. OMPL has been promoted by Mangalore Refinery & Petrochemicals Limited (51% equity stake) and Oil and Natural Gas Corporation Limited (49% equity stake). It has set up a project in Mangalore Special Economic Zone (MSEZ) adjacent to the MRPL refinery, to manufacture about 913 KTPA (kilo tonnes per annum) of Paraxylene and about 283 KTPA of Benzene. The project also includes a captive power plant of 72 MW capacity which can utilise natural gas, LSHS (low sulphur heavy stock) or diesel as fuel. The project cost was estimated at about Rs. 5,750 crore which was funded in debt-to-equity ratio of 65:35 though it witnessed cost overruns of about Rs. 1,160 crore. OMPL declared its Commercial Operation Date (COD) as April 1, 2014, though the plant was initially in trial runs and commercial production commenced in October 2014. On July 8, 2015, MRPL announced that its board has approved the Scheme of Amalgamation of OMPL with itself. The No Objection Certificate (NOC) for the merger was received from the MoPNG (Ministry of Petroleum and Natural Gas) in April 2018. In January 2021, MRPL acquired ONGC's 49% stake in OMPL, thereby increasing its stake in the subsidiary to 99.99%. The merger between MRPL and OMPL is awaiting approval from the Ministry of Corporate Affairs and is expected to be completed by Q2 FY2022.

Key financial indicators (audited)

OMPL	FY2019	FY2020
Operating Income (Rs. crore)	8,568	4,954
PAT (Rs. crore)	23	-1,400
OPBDIT/OI (%)	11.5%	-10.6%
PAT/OI (%)	0.3%	-28.3%
Total Outside Liabilities/Tangible Net Worth (times)	10.0	9.8
Total Debt/OPBDIT (times)	6.6	-11.0
Interest Coverage (times)	1.7	-1.0

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

About the parent (MRPL):

Mangalore Refinery & Petrochemicals Limited (MRPL) was set up as a joint venture (JV) between the AV Birla Group and Hindustan Petroleum Corporation Limited (HPCL). MRPL operates a refinery at Mangalore (Karnataka), with a nameplate capacity of 15 million metric tonne per annum (MMTPA). The refinery project was initially implemented in two phases during a period of administered pricing, where the regulatory framework provided assured returns on capital employed. However, since the deregulation of the refining sector in 1998, the company had been exposed to low and volatile international refining margins, which affected its operating profitability quite significantly. Together with high debt service commitments, this resulted in MRPL posting large losses in the past. Oil and Natural Gas Corporation Limited (ONGC) acquired a 51% stake in MRPL in March 2003, and later increased its stake to 72%. With a change in management, funds infusion by ONGC and upturn in the refining margin cycle, the company made a financial turnaround in the subsequent period. The refining capacity was enhanced to 15 MMTPA from 11.82 MMTPA in March 2012 with the commissioning of Phase-III. It also commissioned a 440 KTPA polypropylene unit. In July 2015, MRPL's board approved the merger of its subsidiary, OMPL, with itself, which is currently in process. MRPL had acquired a controlling stake in OMPL in February 2015 by increasing its stake to 51% from 3%, while the remaining stake was held by ONGC. In January 2021, MRPL increased its stake in OMPL to 99.99% by acquiring ONGC's stake in the subsidiary.

Key financial indicators (audited)

MRPL Consolidated	FY2019	FY2020
Operating Income (Rs. crore)	62,103	51,055
PAT (Rs. crore)	332	-2,708
OPBDIT/OI (%)	3.2%	-3.5%
PAT/OI (%)	0.5%	-5.3%
Total Outside Liabilities/Tangible Net Worth (times)	1.5	2.2
Total Debt/OPBDIT (times)	4.5	-6.7
Interest Coverage (times)	4.2	-2.4

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2021) Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating 19-Mar-21	Date & Rating 28-Oct-20	Chronology of Rating History for the Past 3 Years: Date & Rating in FY2020 28-Feb-20	Date & Rating in FY2019 23-Jan-19	Date & Rating in FY2018 29-Dec-17
1	Fund Based - Working Capital Facilities	Short term	2,050	NA	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+&	[ICRA]A1+&	[ICRA]A1+&
2	Non-fund based - Working Capital Facilities	Short term	300	NA	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+&	[ICRA]A1+&	[ICRA]A1+&
3	Commercial Paper	Short term	1,000	NA	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+&	[ICRA]A1+&	[ICRA]A1+&
4	Fund Based – Working Capital Facilities (Cash Credit)	Long Term	750	NA	-	-	[ICRA]AA+&; withdrawn	[ICRA]AA+&	[ICRA]AA+&

& under watch with developing implications

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 click here

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	Fund Based – Working Capital Facilities (Cash Credit)	--	--	--	2,050.0	[ICRA]A1+
NA	Non-Fund Based Limits	--	--	--	300.0	[ICRA]A1+
NA	Commercial Paper*	--	--	--	1,000.0	[ICRA]A1+

*Source: Company; *not placed yet*

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
ONGC Mangalore Petrochemicals Limited	51.00%*	Full Consolidation
Shell MRPL Aviation Fuels and Services Limited	50.00%	Limited Consolidation

*Source: Company; *ownership as of March 31, 2020; at present MRPL's ownership in OMPL is 99.99%*

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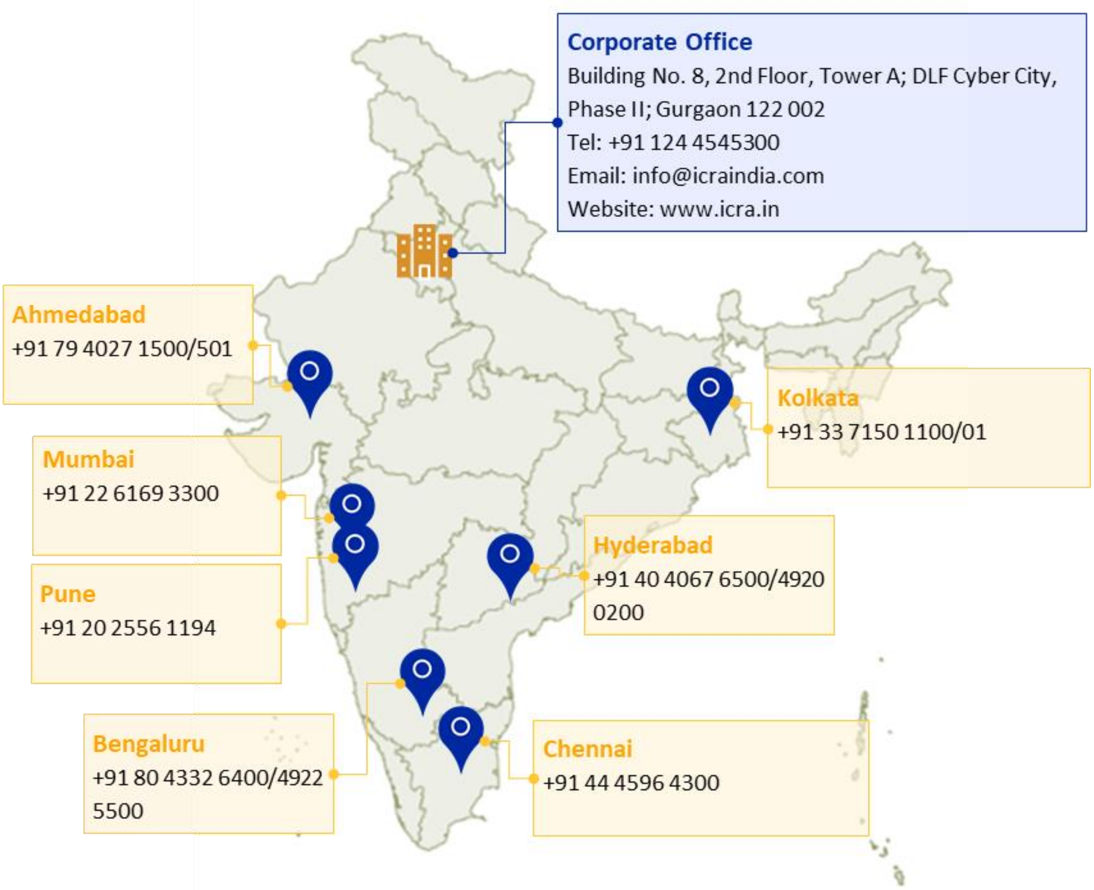

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