

HPCL-Mittal Energy Limited

Instrument	Amount Rated (Rs. Crore)	Rating Action
Long-term Bond Programme	1020	Upgraded to [ICRA]AA (Positive) from [ICRA]AA- (Stable)
Long-term Bond Programme	500	[ICRA]AA- rating withdrawn
Commercial Paper Programme	1000	[ICRA]A1+ rating withdrawn

The rating assigned to the Rs. 1020¹ crore long-term bond programme of HPCL-Mittal Energy Limited (HMEL) has been upgraded to [ICRA]AA (pronounced ICRA double A) from [ICRA]AA- (pronounced ICRA double A minus).² The outlook on the long-term rating has been revised to Positive from Stable. The rating of [ICRA]AA- (stable) assigned to Rs. 500 crore bond programme of HMEL has been withdrawn as the bond has been completely repaid on the maturity. The [ICRA]A1+ (pronounced ICRA A one plus) rating assigned to the Rs. 1000 crore commercial paper programme of HMEL has also been withdrawn at the request of the company as there is no amount outstanding against the rated instrument.

The revision in the long-term rating reflects favourable outlook on gross refining margins (GRMs) and anticipated healthy cash accruals of HMEL over the medium-term. The revision also factors in stabilised refining operations with improvement in operational indicators for the last two years along with material improvement in profitability, capital structure, and debt protection metrics of the company on a consolidated basis in FY2016. Although due to high capital cost, HMEL requires to achieve relatively higher break-even GRMs for adequate debt servicing; the risk has moderated lately due to the company's efforts through refinancing/repayment of loans leading to lower repayment burden over the medium-term and longer tenure of repayments. The positive outlook reflects ICRA's expectations of further improvement in the company's key debt coverage metrics in the near to medium term on the back of anticipated increase in profits and cash accruals following completion of ongoing expansion project.

The rating continues to take into account the high complexity level of the refinery, long and established track record of Hindustan Petroleum Corporation Limited (HPCL) in the domestic refining and marketing business, smooth product off-take with HPCL in line with take or pay agreement, fiscal incentives from the Government of Punjab (GoP), and favourable location of the refinery, as it is situated in the petroleum products-deficit and the high growth northern region. However, the rating is constrained by the elevated capital structure due to erosion in the networth resulting from past losses and vulnerability of the company's profitability to the global refining margin cycle, import duty protection, and INR-USD parity levels. The rating also considers the sensitivity of profits to crude oil price volatility as inventory losses/gains are likely to be higher for landlocked refineries like HMEL in a scenario of sharp fall/rise in crude oil prices because of high inventory holdings. The rating also factors in the residual project implementation and integration risks related to the ongoing expansion project to increase refining capacity to 11.3 million metric tonnes (MMT) from current 9 MMT.

In arriving at the rating of HMEL, ICRA has taken a consolidated view of HMEL and HMPL, because of the synergies between them. HMPL has entered into a Pipeline Usage agreement with HMEL, with pipeline charges ensuring adequate debt servicing for HMPL, even if there is no crude oil offtake by HMEL but the pipeline is made available by HMPL. Further, HMPL plays a strategic role for the parent as it is critical for the receipt and transportation of crude oil to ensure smooth operations of HMEL refinery, situated at Bathinda, Punjab.

HMEL has reported steady improvement in operational parameters such as capacity utilisation and fuel and loss (F&L). Its capacity utilisation increased to 119% in FY2016 and 122% in 5M FY2017 from 81% in FY2015. Further, its fuel & loss (F&L) decreased 11.4% in FY2016 and ~10.4% in 5M FY2017 (against design of 10.9%). As per company estimates, HMEL reported high GRMs of ~US\$14.27/bbl in FY2016 due to healthy crack spreads globally resulting from low crude oil prices and higher demand of liquid fuels; while the GRMs were low at US\$3.04/bbl in FY2015 due to inventory loss. Following high crack spreads as well as inventory gains, HMEL reported GRMs of ~US\$20.05/bbl in Q1 FY2017. Going forward, in line with moderation in global

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

crack spreads, the GRMs of HMEL may moderate from the current high levels. Nevertheless, the core GRMs of HMEL could continue to be high at US\$ 10-11 /bbl in FY2017.

HMEL reported an operating profit of Rs. 4348 crore in FY2016 as against an operating loss of Rs. 1185 in FY2015 driven by improved GRMs. The interest expenses of the company declined by 15.0% (yoy) to Rs. 1481 crore in FY2016 on account of lower debt levels and refinancing of the borrowings at lower interest rates. In line with the company turning operationally profitable and lower interest expenses, the company reported a net profit of Rs. 1718 crore in FY2016 as against a net loss of Rs. 1589 crore in FY2015.

HMEL's total debt (standalone) stood at Rs. 18,798 crore as on March 31, 2016 against Rs. 23,558 crore as on March 31, 2015 due to lower working capital borrowings due to lower crude prices and repayment of loans raised for funding cash losses in the previous years. Total gearing of HMEL decreased to 3.68 times as on March 31, 2016 from 8.14 times as on March 31, 2015. The total gearing (on a consolidated basis) would be about 4.43 times as on March 31, 2016 from 10.71 times as on March 31, 2015. The interest coverage of HMEL improved to 2.94 times in FY2016 from negative 0.68 time in FY2015 on account of healthy operating profit, reduced interest expenses, and lower debt. Total debt/OPBDITA also improved to 4.32 times in FY2016 from negative 19.88 times in FY2015.

With regards to project to expand capacity from 9 MMTPA to around 11.3 MMTPA, the expansion project is progressing as per schedule and the company has spent around Rs. ~1300 crore till June-2016 out of total capex of ~Rs. 3000 crore. The project is expected to be commissioned by Q1 FY2018.

HMEL has low repayment liabilities over the FY2017 and FY2018 post refinancing of significant part of Rupee denominated term loans through the foreign currency borrowings leading to reduction in cost of debt. The liquidity position of the company is expected to be comfortable due to healthy cash generation, adequate bank lines, and high financial flexibility owing to strong sponsors. Sustenance of healthy cash generation over the medium term and its use for deleveraging the balance sheet would be a key rating sensitivity for upgrade of the rating. Conversely, significant debt-funded capital expenditure plans leading to deterioration in the capital structure and debt protection metrics could be sensitivity for revision in the rating outlook to Stable from Positive.

Company Profile

HMEL incorporated as Guru Gobind Singh Refinery Limited (GGSRL) in 2000, is a joint venture between HPCL and MEIL, Singapore - a L. N. Mittal group company. Both the JV partners hold a stake of 48.804% in the company each, the rest 2.39% is held by financial institutions (IFCI, SBI and HDFC Standard Life). In February 2012, HMEL commercially commissioned its green field refinery complex with 9 MMTPA capacity at Bathinda (Punjab) along with captive power plant of 165 MW. To meet the crude receipt & storage facilities as well as to transport the crude for the company, its wholly owned subsidiary HPCL-Mittal Pipelines Ltd (HMPL) has set up a Crude oil terminal (COT) and Single Buoy Mooring (SBM) at Mundra Port, Gujarat and a cross-country pipeline for transportation of crude oil from Mundra to Bathinda.

November 2016

For further details please contact:

Analyst Contacts:

Mr. K. Ravichandran, (Tel. No. +91-44-45964301)
ravichandran@icraindia.com

Anoop Bhatia, (Tel. No.+91 124 4545 315)
anoopb@icraindia.com

Prashant Vasisht, (Tel. No.+91 124 4545 322)
prashant.vasisht@icraindia.com

Relationship Contacts:

Mr. L. Shivakumar, (Tel. No. +91 22 6114 3406)
shivakumar@icraindia.com



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**Registered Office****ICRA Limited**

1105, Kailash Building, 11th Floor, 26, Kasturba Gandhi Marg, New Delhi 110001
Tel: +91-11-23357940-50, Fax: +91-11-23357014

Corporate Office**Mr. Vivek Mathur**

Mobile: +91 9871221122

Email: vivek@icraindia.com

Building No. 8, 2nd Floor, Tower A, DLF Cyber City, Phase II, Gurgaon 122002
Ph: +91-124-4545310 (D), 4545300 / 4545800 (B) Fax; +91- 124-4050424

Mumbai**Mr. L. Shivakumar**

Mobile: +91 9821086490

Email: shivakumar@icraindia.com

3rd Floor, Electric Mansion
Appasaheb Marathe Marg, Prabhadevi
Mumbai—400025,
Board : +91-22-61796300; Fax: +91-22-24331390

Kolkata**Mr. Jayanta Roy**

Mobile: +91 9903394664

Email: jayanta@icraindia.com

A-10 & 11, 3rd Floor, FMC Fortuna
234/3A, A.J.C. Bose Road
Kolkata—700020
Tel +91-33-22876617/8839 22800008/22831411,
Fax +91-33-22870728

Chennai**Mr. Jayanta Chatterjee**

Mobile: +91 9845022459

Email: jayantac@icraindia.com

5th Floor, Karumuttu Centre
634 Anna Salai, Nandanam
Chennai—600035
Tel: +91-44-45964300; Fax: +91-44 24343663

Bangalore**Mr. Jayanta Chatterjee**

Mobile: +91 9845022459

Email: jayantac@icraindia.com

'The Millenia'
Tower B, Unit No. 1004, 10th Floor, Level 2 12-14, 1 & 2,
Murphy Road, Bangalore 560 008
Tel: +91-80-43326400; Fax: +91-80-43326409

Ahmedabad**Mr. L. Shivakumar**

Mobile: +91 9821086490

Email: shivakumar@icraindia.com

907 & 908 Sakar -II, Ellisbridge,
Ahmedabad- 380006
Tel: +91-79-26585049, 26585494, 26584924; Fax:
+91-79-25569231

Pune**Mr. L. Shivakumar**

Mobile: +91 9821086490

Email: shivakumar@icraindia.com

5A, 5th Floor, Symphony, S.No. 210, CTS 3202, Range
Hills Road, Shivajinagar, Pune-411 020
Tel: + 91-20-25561194-25560196; Fax: +91-20-
25561231

Hyderabad**Mr. Jayanta Chatterjee**

Mobile: +91 9845022459

Email: jayantac@icraindia.com

4th Floor, Shobhan, 6-3-927/A&B. Somajiguda, Raj
Bhavan Road, Hyderabad—500083
Tel:- +91-40-40676500