

July 10, 2017

ONGC Videsh Limited

Summary of rated instruments

Instrument*	Rated Amount (in crore)	Rating Action
Long Term Bond Programme	370.00	[ICRA]AAA (Stable) reaffirmed
Fund Based Limits	50.00	[ICRA]AAA (Stable) reaffirmed
Non Fund Based Limits	1544.55 (reduced from Rs 1549.10 crore)	[ICRA]A1+ reaffirmed
Short Term Limits-Unallocated	405.45 (reduced from Rs 500.90 crore)	[ICRA]A1+ reaffirmed
Total	2,370.00	

*Instrument details are provided in Annexure-1

Rating action

ICRA has reaffirmed the [ICRA]AAA (pronounced ICRA triple A) rating outstanding on the Rs. 370.00 crore long-term bond programme and the Rs 50.00 crore fund based limits of ONGC Videsh Limited (ONGC Videsh). ICRA has also reaffirmed the [ICRA]A1+ (pronounced ICRA A one plus) rating outstanding on the Rs 1544.55 crore (reduced from Rs 1549.10 crore) non-fund based facilities and the Rs 405.45 crore (reduced from Rs 500.90 crore) unallocated short term facilities of ONGC Videsh. The outlook on the long term rating is stable.

Rationale

In reaffirming the ratings, ICRA has taken a consolidated view of ONGC Videsh along with ONGC, considering that the company is wholly-owned by ONGC and is of strategic importance to ONGC by virtue of its status as its overseas E&P arm. With the issue of acquiring energy security assuming importance for India as well as ONGC, ONGC Videsh has participation either directly or through wholly-owned subsidiaries/joint venture companies in 38 projects spread across 17 countries, of which fourteen are producing properties; that includes the ones in Brazil, Colombia, Russia (Sakhalin-I, Imperial Energy and Vankorneft), Sudan and South Sudan, Syria, Venezuela, Vietnam, Azerbaijan and Myanmar. Out of 38 projects, ONGC Videsh is operator in 10 projects and joint operator in 6 projects. A substantial part of the operations of ONGC Videsh have so far been funded in the form of either equity or loans advanced by ONGC. ONGC converted about Rs 14,000 crore of its unsecured loans to ONGC Videsh into equity during FY2013 to FY2017 collectively in order to keep the latter's gearing at a relatively healthy level. Accordingly ICRA believes that ONGC would continue to support its subsidiary through equity or loans in the future as well. ICRA, however, notes that ONGC Videsh is faced with increasing challenges to add reserves at competitive cost and grow production, and is exposed to geological, technology and execution risks that are inherent in E&P activities. Moreover, it is exposed to significant geopolitical risks because of its presence in some countries with a history of political instability and commodity price risk. ICRA notes that disruptions at three producing projects viz. Al Furat Project in Syria as well as in Block 5A and GPOC Projects in South Sudan have dampened the production and going forward production from these fields is expected to remain disrupted depending upon how long these problems persist. Additionally softening of international crude oil prices have adversely impacted the revenues and cash accruals of ONGC Videsh given that the company derives more than 75% of its revenues from operations from the sale of crude oil. ONGC Videsh has large capex plans for the exploration and development of its existing

blocks as well as acquisition of participating interests in new properties. The large capital expenditure plan of ONGC Videsh would entail incurrence of new project implementation risks and additional debt. In CY2016 ONGC Videsh completed the acquisition of 26% stake (in two tranches of 15% and 11%) in CJSC Vankorneft, which is the owner of Vankor Field and North Vankor license. Vankor is Russia's second largest field by production and is currently producing oil at average level of approximately 0.4 million bopd. The acquisition has been almost entirely funded (~US \$1.9 billion, after closing adjustments of purchase consideration) by foreign currency debt. Although this additional debt will not weaken the key credit metrics of ONGC (consolidated) materially, further large debt funded acquisitions, if any, which impacts its capital structure and coverage metrics adversely, could put pressure on its credit profile especially in view of the pressure on the net cash accruals of ONGC Ltd in the domestic operations emanating from low domestic gas prices and high dividend payout. Moreover ONGC has large commitments towards capex and equity investments in PSUs/group ventures, which could warrant higher debt levels in the absence of adequate internal cash generation.

Key rating drivers

Credit strengths

- Strategic importance of ONGC Videsh to ONGC, as ONGC Videsh is the fully-owned subsidiary through which the overseas E&P strategy of the company is executed; besides, ONGC has amply demonstrated its commitment to ONGC Videsh by way of funding assistance, additional equity infusion and extension of managerial support
- Improvement in overseas oil & gas production and reserves addition by ONGC Videsh Limited in recent years
- Balanced geographical mix of ONGC Videsh with respect to participation in 38 E&P projects in 17 countries. However, the bulk (85%) of the joint venture investments are in just three countries viz. Mozambique, Russia and Brazil.

Credit weaknesses

- Geological, technology and execution risks that are inherent in E&P activities
- Commodity price risk associated with crude oil; significant decline in crude oil prices since July 2014 has adversely impacted the revenues and cash accruals
- Significant presence in countries with a history of unstable regimes, change in fiscal terms and resource nationalisation expose the company to geopolitical risk, although the risk is partially mitigated by GoI support and participation by way of JV with oil companies including foreign majors
- Event risks associated with the acquisition-driven growth strategy of the company, although the risk is partially mitigated by a three-tier approval mechanism for such deals
- Moderate financial risk profile on a standalone basis because of increase in debt levels; nevertheless, the risk is largely mitigated, as almost all the debt is guaranteed by ONGC; availment of additional debt to fund any new acquisitions could stress the financial risk profile of ONGC Videsh further, however the additional debt is expected to be guaranteed by ONGC and consolidated ONGC gearing and debt coverage are expected to remain comfortable
- With escalation in the cost of services, ONGC Videsh's F&D costs have been high; nevertheless with low prices of crude oil the cost of E&P services have declined owing to which F&D costs are expected to trend downward
- Disruptions in producing blocks in Syria and South Sudan have dampened the production

Key rating sensitivities

- ⊖ Any large debt funded acquisition(s) materially weakening the key credit metrics

Description of key rating drivers:

ONGC Videsh was set up in 1965 as a wholly-owned overseas E&P arm of ONGC. The overseas exploration and production strategy of ONGC is executed through ONGC Videsh to bridge the widening energy-supply gap from domestic production.

Over the years, ONGC Videsh has been acquiring participating interests in overseas oil and gas assets and has participation either directly or through wholly-owned subsidiaries/joint venture companies in 38 projects in 17 countries. However the top 3 investments (Mozambique, Russia and Brazil) accounted for about 85% of total investments.

In CY2016, ONGC Videsh completed the acquisition of 26% stake (in two tranches of 15% and 11%) in JSC Vankorneft, which is the owner of Vankor Field and North Vankor license. Vankor is Russia's second largest field by production and is currently producing oil at a level of approximately 0.4 million bopd. The acquisition has been almost entirely funded (~US \$1.9 billion, after closing adjustments of purchase consideration) by foreign currency debt. ONGC Videsh's production increased from 8.92 MMTOE FY2016 to 12.80 MMTOE in FY2017 primarily due to the contribution of the Vankor fields. Through a series of acquisitions, ONGC Videsh has built up moderate reserves which stood at 128.20 MMTOE (O+OEG) as on March 31, 2017.

ONGC Videsh's investments also suffer from geo-political risks as some of the invested countries have exhibited history of unstable regimes, resource nationalisation, changes in fiscal laws, etc. As compared to this, highly rated E&P companies/integrated oil companies have a relatively more diversified presence in stable & unstable regions. Over the long term, the company's mission is to produce 20 MMTPA by 2020 and 60 MMTPA by 2030 through organic as well as inorganic initiatives. This strategy could expose ONGC Videsh to significant event, geological, execution and geo-political risks in the host countries. ICRA, however, draws comfort from the safeguards built in the three-tier approval process (vetting by ONGC Videsh's Board, ECS and CCEA) for overseas acquisitions. ONGC Videsh's status as a GoI company helps it obtain feedback from the Government's diplomatic network. The due diligence exercise of ONGC Videsh on target assets is also detailed, involving an in-house team, external reservoir consultants, investment banks and legal experts.

ONGC Videsh holds stakes in blocks in Syria and South Sudan which have been impacted by political unrest. Syria has been in the grip of a civil war since February 2011 and in the same year the European Union imposed a series of sanctions on Syria. As a result of these sanctions, Shell declared that the foreign partners are subject to force majeure. In the absence of details, the accounting of revenue and expenditure has not been carried out from December 2011 onwards. Since then the situation in Syria has deteriorated further with widespread civil war and accordingly uncertainty remains with regard to the revenue flows from this project. In the case of South Sudan, violence owing to civil war forced the company to shut its oilfields and evacuate all personnel from the country in December 2013. It remains unclear as to when production can be recommenced in its projects in South Sudan.

Besides the geopolitical risk an upstream company is exposed to geological, technology and execution risks that are inherent in E&P activities especially considering the vastly different geographies and geologies ONGC Videsh has exposure to.

With escalation in the cost of services, ONGC Videsh's F&D costs have been high. However with low prices of crude oil the cost of E&P services have declined owing to which F&D costs are expected to trend downward. With relatively high additions of OEG owing to the Vankor acquisition, ONGC Videsh's F&D costs declined in FY2017 and stood at US\$ 5.31/BOE (based on proved developed reserve addition).

As most of the revenues are derived from the sale of crude oil, ONGC Videsh remains exposed to the commodity price risk associated with crude oil. The significant decline in crude oil prices since July 2014 has adversely impact the revenues and cash accrual of the company. Nevertheless, the operating income increased to Rs 11,870 crore in FY2017 from Rs 10,923 crore in FY2016 owing to increase in production. The operating profitability increased from 57.3% in FY2016 to 64.7% in FY2017 owing to higher realizations of crude oil. The company recognized an impairment of Rs 3,047 crore in FY2016 due to low global oil prices. Accordingly the consolidated net profit increased from a loss of Rs. 3,640 crore in FY2016 to a profit of 697 crore in FY2017.

ONGC Videsh's gearing increased from 0.79 times as on March 31, 2016 to 0.96 times as on March 31, 2017 as foreign currency debt for funding the acquisition of PI in the Vankor block has been added on the books of ONGC Videsh during FY2017. The risk is, however, mitigated by the fact that almost all the debt on the company has been mobilised from its parent ONGC or guaranteed by ONGC. Due to increase in profitability the debt coverage indicators have improved with NCA/TD increasing from 1.9% in FY2016 to 11.0% in FY2017. Though foreign currency debt for funding the acquisition of PI in the Vankor block has been added on the books of ONGC Videsh during FY2017, nevertheless, backing of ONGC guarantee for the debt are comforting factors. Additionally the consolidated ONGC gearing and debt coverage are expected to remain comfortable.

ONGC has amply demonstrated its commitment to ONGC Videsh by way of funding assistance, additional equity infusion and extension of managerial support. ONGC converted about Rs 14,000 crore of its unsecured loans to ONGC Videsh into equity during FY2013 to FY2017 collectively in order to keep the latter's gearing at a relatively healthy level. ONGC's loans outstanding to ONGC Videsh stood at Rs. 5,759 crore as on March 31, 2016 out of which Rs 5,000 crore was converted into equity in FY2017.

Going forward, ICRA expects ONGC Videsh's revenues to move in line with international crude oil prices. However, the profitability is expected to remain muted as realisations on crude oil are expected to remain weak in line with the movement in international prices. Even as additional debt is availed on the books of ONGC Videsh for the Vankor acquisition, the consolidated gearing and coverage indicators of ONGC are expected to remain comfortable.

Analytical approach: For arriving at the ratings, ICRA has taken a consolidated view of ONGC Videsh along with ONGC, considering that the company is wholly-owned by ONGC and is of strategic importance to ONGC by virtue of its status as its overseas E&P arm. Additionally for arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

Links to applicable criteria:

[Corporate Credit Ratings - A Note on Methodology](#)
[Upstream Oil Companies](#)

About the company:

ONGC

ONGC has a strong credit profile backed by its large proved reserves; globally competitive cost structure; strong financial risk profile; significant sovereign ownership and strategic importance to the country. ONGC has access to an extensive E&P infrastructure such as drilling & workover rigs and onshore and offshore production facilities that are spread across many regions in India. This is a source of significant competitive advantage, as reflected by the company's last three year average finding & development cost of US\$ 21.34/BOE (based on proved reserves), which is low among global E&P companies. ONGC also compares favourably against global independent E&P companies on the reserve life index (of 10.4 years as on March 31, 2016 based on proved developed reserves); full cycle costs (US\$ 38.25/BOE in FY2016) and leverage parameters. These are strong protective factors in an industry that is characterised by depleting assets; significant technical challenges (in reserve replacement) and unpredictable prices. The reserve replacement ratio in India (based on proved developed reserves addition) of ONGC was 53% in FY2016 and the company accreted 25.66 MMT oil equivalent of proved developed reserves of hydrocarbons in the same period in India.

The financial risk profile of ONGC is also favourable even on a consolidated basis (including the debt of ONGC Videsh and MRPL), with the long term gearing of the group at around 0.25 time as on March 31, 2016. The company also enjoys significant financial flexibility on the strength of its large liquid investments estimated at Rs. 33,708 crore as on March 31, 2016 with investments in IOCL and GAIL accounted for at book value (market value was around Rs 15,341 crore as on March 31, 2017) and its superior standing among lenders and equity investors. These strengths are partially offset by the regulatory risks governing subsidy sharing and control on gas prices; risks inherent in the overseas expansion strategy and risks associated with large capex plans.

Although the recent debt contracted for acquisitions will not weaken the key credit metrics of ONGC (consolidated) materially, further large debt funded acquisitions which impacts its capital structure and coverage metrics adversely, could put pressure on the ratings especially in view of the pressure on the profitability and net cash accruals of ONGC Ltd in the domestic operations emanating from low domestic gas prices and high dividend payout. Moreover ONGC has large commitments towards capex and equity investments in PSUs/group ventures, which could warrant higher debt levels in the absence of adequate internal cash generation.

On a consolidated basis, the company reported a group net profit of Rs 20,498 crore on revenues from operations of Rs 1,42,149 crore in FY2017 as against Ind-AS restated group net profit of Rs 12,875 crore on revenues from operations of Rs 1,35,664 crore in FY2016

ONGC Videsh Limited

ONGC Videsh Limited (ONGC Videsh) is a wholly owned subsidiary of the Oil and Natural Gas Corporation Limited (ONGC). ONGC Videsh was incorporated as Hydrocarbons India Private Limited on March 5, 1965. The company was rechristened as ONGC Videsh Limited on June 15, 1989. The primary business of the company is to prospect for oil and gas acreages abroad. This includes acquisition of oil and gas fields in foreign countries as well as exploration, production, transportation and sale of oil and gas. ONGC Videsh has participation either directly or through wholly-owned subsidiaries/joint venture companies in 38 projects spread across 17 countries of which fourteen are producing properties.

The company reported a group net profit of Rs 701 crore on total income of Rs 11,813 crore (including share of profit from equity accounted entities) in FY2017 as against restated Ind-AS FY 2016 group net loss of Rs 3,633 crore on total income of Rs 11,520 crore.

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years:

Table:

S. No.	Instrument	Current Rating (2017)			Chronology of Rating History for the past 3 years			
		Type	Amount Rated (Rs. crore)	Date & Rating	Date & Rating in FY2017	Date & Rating in FY2016	Date & Rating in FY2015	
				July 2017	May 2016	May 2015	February 2015	
1	Long Term Bond Programme	Long Term	370.00	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	
2	Fund-Based Limits	Long Term	50.00	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	
3	Non-Fund Based Limits	Short Term	1544.55	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	
4	Unallocated	Short Term	405.45	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	

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

Name of the instrument	Date of Issuance/ Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
Long Term Bond Programme	6 th January 2010	8.54% payable annually	6 th January 2020	370.00	[ICRA]AAA(Stable)
Long term Fund Based Limits	-	-	-	50.00	[ICRA]AAA(Stable)
Non-Fund Based Limits	-	-		1544.55	[ICRA]A1+
Short term-Unallocated				405.45	[ICRA]A1+

Source: ONGC Videsh Limited

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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