August 25, 2017

Focus Energy Limited

Summary of rated instruments

Instrument*	Rated Amount (Rs. crore)	Rating Action
Long term fund based limits-Term loans	177.5	[ICRA]BBB-(Stable) assigned
Long term fund based limits	78.0	[ICRA]BBB-(Stable) assigned
Short term non-fund based limits	93.0	[ICRA]A3 assigned
Total	**348.5**	

*Instrument details are provided in Annexure-1

Rating action

ICRA has assigned the ratings of [ICRA]BBB- (pronounced ICRA triple B minus) and [ICRA]A3 for Rs 348.5 crore[1] bank facilities of Focus Energy Limited (FEL)[2]. The outlook on the long-term rating is Stable.

Rationale

The ratings take into consideration the discovered gas reserves of Focus' RJ-ON/6 block; revenue visibility due to gas sale agreement with GAIL (India) Limited and support extended by group and parent companies and increase in the 2P reserves of the Rajasthan block post reserve audit by independent auditors. However, the ratings are constrained by the geological risks inherent in exploration and production (E&P) activities; residual project implementation risks in the development of discovered RJ-ON/6 block to ramp up production volume for next phases of production though the decade long experience of the company in exploration and production of the Rajasthan block is a key mitigant to the aforementioned risk; risks involved in timely commissioning of pipeline projects to connect the field to the national grid and elevated leverage levels due to large debt-funded capital expenditure (capex) plans. Moreover, the company's key credit metrics viz RoCE and coverage indicators are moderate, albeit they should improve modestly with the commencement of gas sales from subsequent phases of the development project. ICRA also notes that with the delay in ONGC's decision to participate in the development project, the company has been funding ONGC's share (30%) and further delays in payment of cash calls by ONGC could weaken the liquidity position of the company.

Going forward, timely monetisation of the reserves and extent of dependence on debt for capex would remain key monitorables.

[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*

Key rating drivers

Credit strengths

- **The discovered gas reserves of RJ-ON/6 block with successful commencement of gas production from the second phase:** The company entered into oil & gas E&P activities and signed production sharing contract (PSC) with GoI for the block RJ-ON/6 (pre-NELP block) in 1998. The PSC for the block was signed on 30th June, 1998 between Government of India (GoI), Ministry of Petroleum and Natural gas; Focus Energy Limited; and Oil & Natural Gas Corporation (ONGC). Initially, Focus was holding 100% participating interest (PI) in the block. In Jan 2006, Focus assigned 90% of its participating interest in RJ-ON/6 block to its affiliates iSevices Investment Ltd., Mauritius-65% and Newbury Oil Company Ltd., Cyprus -25% while retaining a 10% with Focus. In May 2006, the gas discovery was made in well SGL#1, which was declared as "Commercial" by the Management Committee in Jan-2008. Subsequently, in June 2008, as per terms of the PSC, ONGC notified Focus as to its intention to opt for 30% PI option in the SGL field. As ONGC exercised the rights to acquire 30% PI, the revised PI in SGL Field of Focus Energy Ltd (Operator) is 7% while iServices Investments Ltd. has 45.50%, Newbury Oil Company Ltd. 17.50% and ONGC 30%. Thus, iServices Investments and Newbury Oil together hold 63% stakes in SGL Field of RJ-ON/6 block. Indus Gas Limited is the holding company of Newbury Oil and iServices Investments. In June 2008, Indus Gas raised around £ 25 million through IPO for 8.33% stake in the company, in Alternate Investment Market (AIM), a market operated by London Stock Exchange.

  The first stage of gas supply had commenced in July 2010 to the Rajasthan Rajya Vidyut Utpadan Nigam Ltd (RRVUNL). The second stage of supply of gas was for a quantity of 0.95 MMSCMD (without CO_2) and RRVUNL began drawal of gas in March 2013.
- **Revenue visibility due to gas sale agreement with GAIL (India) Limited with "take or pay" payment guarantees, which provides comfort from debt servicing point of view:** Focus along with other partners entered into Gas Sale Purchase Agreement (GSPA) with GAIL in August 2009. The sale was in two stages with first stage without CO_2 removal of 0.2 MMSCMD and second stage of enhanced volume of 0.95 MMSCMD after CO_2 removal. The first stage of supply had commenced in July 2010 to the ultimate buyer namely Rajasthan Rajya Vidyut Utpadan Nigam Ltd (RRVUNL) but owing to delays in off take from the second stage of the development project, the company enforced take or pay obligations on GAIL from October 1, 2012. Post commissioning and stabilisation of its 160 MW power plant, RRVUNL is now drawing gas at the rate of about 0.85-0.95 MMSCMD (without CO_2) of gas.
- **Financial flexibility from the support extended by group companies and modest investments:** To meet its capex requirements, group companies have provided unsecured loans to Focus Energy Limited of Rs 380.8 crore as on March 31, 2016 as against Rs 633.7 crore as on March 31, 2015. Additionally investments of Focus in real estate properties and its liquid investments totalling about Rs. 100 crore as on March 31, 2016 provide financial flexibility to the company.
- **Increase of the proved plus probable (2P) reserves post reserve audit by independent auditors:** Independent international auditor Senergy has upgraded the company's reserves in its latest audit report of July 2016 due to which the 2P reserves of the SGL block have been upscaled to 582 bcf from 416 bcf earlier. At the current rate of gas production of 42 MMSCFD (with CO_2) and 1.3 tcf of 2P reserves the reserve life index of the block works out to about 82 years indicating significant potential for monetisation.

Credit weaknesses

- **Residual project implementation risks in the development of discovered RJ-ON/6 block to ramp up production volume for the next phases of production:** During the next phase of the development of the RJ-ON/6 block the company plans to supply 0.75 MMSCMD (without CO2) of gas for another 160 MW power plant of RRVUNL, which is expected to be commissioned by Q4 FY2019. Subsequently, beginning April 2019, the company plans to supply about 0.63 MMSCMD gas through pipeline to the national grid post which the gas quantity is planned to be scaled up. For the next phases of the development of the RJ-ON/6 block, the company plans to drill additional production wells besides setting up of gas handling facilities such as gas gathering station etc. Though the company is exposed to residual project implementation risks to ramp up production volumes, the decade long experience of the company in exploration and production of the Rajasthan block partly mitigate the same.
- **Successful ramp up of gas volumes will be sensitive to the timely connection of the field with the national grid to diversify the customer base:** The company plans to supply gas to the national grid for which it is in discussions with Gujarat State Petroleum Corporation (GSPC)/ Gujarat State Petronet Limited (GSPL) for connecting the Rajasthan field to the Mehsana-Bhatinda pipeline for which a number of options are being considered. The company is also in discussion with GAIL for connecting the gas from the block to Bhilwara. Accordingly the modalities such as route, capex and funding are still to be finalised. Successfully connecting to the national grid could open up multiple customers and increase offtake and accordingly timely connection of the field to the grid remains crucial.
- **Geological risks inherent in exploration and production (E&P) activities:** The different stages of exploration and production activities are geological & geophysical activity, exploratory drilling, developmental drilling and finally production. At any of the aforementioned stages the company remains vulnerable to any geological surprises which might adversely impact the exploitation of oil and gas reserves. This risk is mitigated to an extent by the long track record of the company in exploration and production in the Indus basin.
- **Large debt-funded capital expenditure (capex) plans to keep the leverage at elevated levels:** The total additional development capex of RJ-ON/6 is expected to be around $ 2016 million till FY2028. Focus has availed term loans of US$ 40 million and an overdraft limit of Rs 50 crore to meet its share of capex. Other than bank loans, group companies have provided unsecured loans of Rs 380.8 crore as on March 31, 2016 as against Rs 633.7 crore as on March 31, 2015. To part fund the capex the company plans to avail additional term loans of $ 30 million. Focus had also provided unsecured loans of around $ 6.9 million (as on March, 31 2016) to Indus. Besides, Focus has also been funding the 30% share of the development and maintenance capex of ONGC till now which stood at about Rs 200 crore till FY2016 end. Any further carry of ONGC's share in the capex by Focus can adversely affect latter's liquidity position as the next phases of the development of RJ-ON/6 is undertaken. Though the company has large debt obligations as well as capex commitments, nevertheless the promoter's substantial stake in AIM listed Indus provides financial flexibility to raise cash.

- **Moderate credit metrics:** The company's operating income in FY2016 at Rs 69.5 crore was higher than FY2015 operating income of Rs 56.1 crore on account of higher shoe sales and higher hydrocarbon sales. The operating margin at 46.7% in FY2016 was in line with FY2015 margins of 46.8%. The net profit was higher in FY2016 at Rs 1.4 crore as against Rs 1.1 crore in FY2015. The gearing of the company increased from 1.4x at FY2014 end to 5.0x at FY2015 end and was 3.7x at FY2016 end. The RoCE was stable at 0.5% in FY2016 vis-a-vis 0.6% in FY2015. As per provisional and unaudited results for FY2017, the operating income of the company increased from Rs 69.5 crore in FY2016 to Rs 74.7 crore in FY2017. The operating margins were stable at 47.6% in FY2017. The RoCE was stable at 0.7% in FY2017. The gearing increased from 3.7x as at FY2016 end to 4.5x as at FY2017 end. The debt coverage metrics are subdued with total debt/OPBDIT of 16.9x in FY2016 and 19.3x in FY2017. Accordingly the company's key credit metrics viz RoCE and coverage indicators are moderate, albeit they should improve modestly with the commencement of gas sales from subsequent phases of the development project

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 Upstream Oil companies

About the company:

Focus Energy Limited (earlier known as Phoenix Overseas Limited) was earlier involved in exports of shoes and commodities to Russia. The shoe operations of the company have reduced significantly and currently the company is active mainly in the field of oil & gas exploration and production. The company has stakes in five blocks in India viz. RJ-ON/6, GK-ON/4, RJ-ONN-2003/2, RJ-ON/2010/2 and CB-OSN-2004/1. Focus has 7% participating interest in SGL field of RJ-ON/6 block, which has discovered gas reserves. Indus Gas, a group company of Focus Energy, is listed on Alternate Investment Market (AIM), London Stock Exchange and has 63% stake in SGL field of RJ-ON/6 block through its wholly owned subsidiaries.

Key Financial Indicators

	FY2016 (Audited)	FY2017 (Provisional)
Operating Income (Rs. crore)	69.5	74.7
PAT (Rs. crore)	1.4	3.9
OPBDIT/ OI (%)	46.7%	47.6%
RoCE (%)	0.5%	0.7%
Total Debt/ TNW (times)	3.7	4.5
Total Debt/ OPBDIT (times)	16.9	19.3
Interest coverage (times)	45.8	-
NWC/ OI (%)	57.7%	209.6%

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

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 (FY2018)			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**
				August 2017	**December 2016**	**August 2015**	**November 2014**
1	Fund based limits-Term loans	Long term	177.5	[ICRA]BBB- (Stable)	[ICRA]BBB+ (Stable) suspended	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)
2	Fund based limits	Long term	78.0	[ICRA]BBB- (Stable)	[ICRA]BBB+ (Stable) suspended	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)
3	Non-fund based limits	Short term	93.0	[ICRA]A3	[ICRA]A2 suspended	[ICRA]A2	[ICRA]A2

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	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
-	Long term fund based limits-Term Loan 1	Feb 12, 2010	3M Libor+4.5%	May 30, 2021	52.0	[ICRA]BBB- (Stable)
-	Long term fund based limits-Term Loan 2	Mar 15, 2016	3M Libor+4.1%	Jan 25, 2025	62.8	[ICRA]BBB- (Stable)
-	Long term fund based limits-Term Loan 3	Apr 5, 2016	3M Libor+4.1%	Jan 25, 2025	62.7	[ICRA]BBB- (Stable)
-	Long term fund based limits	-	-	-	78.0	[ICRA]BBB- (Stable)
-	Short term non-fund based limits	-	-	-	93.0	[ICRA]A3

Source: the company

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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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