

July 01, 2020

## Bharat Oman Refineries Limited: Rating assigned to NCD programme; reaffirmed for CP programme

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Commercial Paper	300.0	300.0	[ICRA]A1+; reaffirmed
Non-convertible Debenture	0.0	1000.0	[ICRA]AAA& (watch with developing implications); assigned
<b>Total</b>	<b>300.0</b>	<b>1300.0</b>	

\*Instrument details in Annexure

### Rationale

The assigned ratings favourably consider the majority ownership of Bharat Petroleum Corporation Limited (BPCL) in Bharat Oman Refineries Limited (BORL), with BPCL's stake increasing from 50% to 63.38% in March 2020, post conversion of warrants. ICRA notes the strategic importance of BORL to BPCL and the proximity of the refinery to the petroleum product-deficit northern and central regions. BORL also has a take-or-pay agreement with BPCL for marketing of its key products, which BPCL uses to cater to the aforementioned regions. Additionally, the strong credit profile of the parent provides high financial flexibility to BORL. BORL has strong operational linkages with BPCL and has also received financial assistance from the latter in the form of corporate guarantees and advances. Moreover, the Board of BORL comprises, among others, top level executives of BPCL.

The ratings also draw comfort from the strong operational performance of the refinery operations of BORL, characterised by robust gross refining margins (GRMs), distillate yield and capacity utilisation levels, resulting in strong cash generation. BORL's refinery has NCI<sup>1</sup> of 11.3, which has ensured high levels of GRMs. They have remained above US\$ 9 per barrel for the past four fiscals till FY2019. The GRMs for FY2020, however, have declined to US\$ 5.6 per barrel owing to weak crack spreads and steep fall in crude oil prices in Q4 FY2020, resulting in huge inventory losses. ICRA also notes that in Q1FY2021, the capacity utilisation declined owing to demand erosion because of Covid-19 pandemic induced lockdowns; however, there has been steady improvement in utilisation levels with the easing of lockdowns. Nevertheless, ICRA expects the GRM levels to improve with the recovery in demand of petroleum products, inventory gains due to increase in crude oil prices, and lower fuel and losses due to subdued crude oil prices.

ICRA, however, notes that the company's profitability is vulnerable to the global refining margin cycle, import duty protection, and INR-USD parity levels. The ratings also consider the asset concentration risk, as the company has a single location refinery, and the sensitivity of profits to crude oil price volatility, as inventory losses/gains are likely to be higher for landlocked refineries such as BORL in a scenario of sharp fall/rise in crude oil prices because of high inventory holdings. The company has a moderate financial profile with high leverage. The decline in profitability in FY2019 and FY2020 has moderated BORL's debt coverage metrics. Nonetheless, the company is expected to meet the debt servicing requirements through internal accruals and/or refinancing. Further, should the need arise, ICRA expects the parent to provide support as it has done in the past.

<sup>1</sup> Nelson Complexity Index

ICRA has placed BORL's long-term rating 'on watch with developing implications', following the GoI's decision to divest 52.98% stake in BPCL and transfer management control. The Government has sought expressions of interest from potential acquirers by July 31, 2020. ICRA will reassess the impact of divestment on the long-term credit profile of BORL once adequate clarity emerges on the new buyer and the transaction structure.

## Key rating drivers

### Credit strengths

**Strong sponsor profile** - BORL has a strong parentage, with 63.38% stake held by BPCL, which has a long and established track record in the domestic refining and marketing business. In March 2020, 361.11 million share warrants, out of the 1147.19 million held by BPCL, were converted into equity shares, thus increasing BPCL's equity stake in BORL to 63.38%, from 50% previously. BORL has strong operational linkages with BPCL, including a take-or-pay agreement with the latter for off-take of petroleum products. BPCL relies on BORL's output to cater to the demand in the petroleum product-deficit northern and central regions. Further, BPCL has provided financial support to BORL in the form of advances and corporate guarantees in the past, thereby leading to high financial flexibility for BORL.

**Healthy operational profile** - BORL's refinery has been consistently delivering high distillate yield of around 83% with a fuel and loss component of around 7.5% over the past few years. The refinery's capacity utilisation has been consistently above 100% over the past few years, except in FY2019, when it dropped to 89% at 7.8 MMTPA from 6.0 MMTPA owing to the shutdown undertaken for the capacity expansion. During FY2020, the capacity utilisation remained healthy at 103% in line with the previous trends. However, in Q1FY2021, the capacity utilisation moderated because of demand erosion owing to Covid-19 pandemic induced lockdowns. However, there has been steady improvement in utilisation levels with the easing of containment measures and ICRA expects the performance to improve with recovery in demand of petroleum products.

**Healthy GRM levels because of high refinery complexity** – BORL's refinery had high complexity, with an NCI of 10.3 and the same was further raised to 11.3 during the capacity expansion in FY2019. The high complexity allows the refinery to process a wider range of crude oil grades. As the refinery is able to process a higher proportion of heavy and sour crude grades, it is able to generate higher GRMs. BORL has a consistently maintained a healthy premium over benchmark Singapore GRMs.

**Favourable location of refinery to cater to northern and central regions** - BORL's refinery caters to the petroleum products-deficit northern and central regions of the country, where the demand has been growing at a healthy rate. The demand in the northern and central regions surpasses the combined capacity of the refineries situated in these regions, and hence, the products are transported from the western part of the country to cater to the local demand.

### Credit weaknesses

**Vulnerability of profits to international refining margin cycle, forex fluctuations, and import duty differential; sensitivity to crude oil prices with inventory losses higher for inland refineries** – 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 declined in FY2020 owing to inventory losses arising from a steep decline in crude oil prices in Q4 FY2020 and weak crack spreads. Any adverse changes in the import duty on its products would also have an impact on the company's domestic sales, though the import duty differential has remained at the same level over the last few years and is not typically subject to frequent changes. The company's profitability is also exposed to the forex rates (INR-US\$), given that the company imports its crude requirement, prices products on trade/import parity basis and goes for forex

borrowings. As BORL’s refinery is not in a coastal region, it is relatively more vulnerable to crude oil price volatility as inventory gains/losses are likely to be higher for such refineries in a scenario of sharp fall/rise in crude oil prices because of high inventory holdings.

**Asset concentration risk** - BORL has refining operations only at Madhya Pradesh and derives all its revenues from the same. The one-location operations exposes the company to asset-concentration risks and the associated force majeure risks. Nonetheless, the risk is partly mitigated by various insurance covers that address these risks.

**Moderate financial profile** – BORL’s financial profile is moderate, characterised by a gearing of 2.3 times as of March 31, 2020. While the company’s profitability and cash accruals have remained healthy (except in FY2019 due to decline in GRM levels and shut down for capacity expansion and in FY2020 due to weak crack spreads and large inventory losses), the company’s high debt levels have moderated the company’s debt coverage metrics. However, the company enjoys a high degree of financial flexibility by virtue of it being a subsidiary of BPCL, which allows it to raise funds at fine rates and is expected to generate steady cash accruals in the medium term.

**Uncertainty associated with BPCL’s divestment process:** ICRA notes the proposed divestment of the government of India’s stake in BPCL, for which a number of large international and domestic players could be the prospective buyers. While there is uncertainty regarding the impact of the transaction on the standalone credit profile of BORL, given the favourable location and the high quality of the asset, it is expected that BORL will continue to avail the benefits that it currently does. Nonetheless, the impact of the BPCL’s privatisation on BORL’s credit profile will remain a key monitorable.

### Liquidity Position: Strong

BORL has a healthy liquidity profile, supported by moderate utilisation of working capital limits and generation of healthy cash accruals. The company enjoys a high degree of financial flexibility and has been able to successfully refinance its borrowings in the past. The company has ~Rs. 1,700 crore of debt repayment obligations falling due in FY2021, which are expected to be met through internal accruals and partly through refinancing.

### Rating Sensitivities

#### Positive triggers – Not Applicable

**Negative triggers** – a) Any change in shareholding of BPCL resulting in weaker credit profile or weakening of the credit risk profile of BPCL, b) weakening of linkages of BORL with the parent, and c) any significant deterioration in BORL’s standalone financial profile could lead to downward revision in ratings.

### Analytical approach:

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">Rating Methodology for Downstream Oil Companies</a>
Parent/Group Support	Parent - Bharat Petroleum Corporation Limited We expect BORL’s parent, BPCL to remain willing to extend financial support to BORL, should there be a need, given the high strategic importance that BORL holds for BPCL and the strong operational linkages between the two companies
Consolidation / Standalone	For arriving at the rating, ICRA has considered the standalone financial profile of BORL.

## About the company:

### Bharat Oman Refineries Limited

Bharat Oman Refineries Limited (BORL) was formed as an equal joint venture between BPCL and Oman Oil Company and was incorporated in 1994. In March 2020, ~Rs. 650 crore worth of warrants were converted to equity and BPCL's share increased to 63.4%. BORL commissioned its refinery with a capacity of 6 million tonnes per annum (MMTPA) in June, 2011 at Bina, Madhya Pradesh. The capacity of the refinery was expanded to 7.8 MMTPA in October 2018. The company also has a single point mooring (SPM) system and a crude oil terminal in Vadinar and a 937-km cross-country pipeline from Vadinar, Gujarat to Bina. The facilities at Bina also include a 99 MW captive power plant, which supplies steam and power to various processing units. The company has a take-or-pay agreement with BPCL for the off-take of BORL's liquid fuel products.

### Bharat Petroleum Corporation Limited

Bharat Petroleum Corporation Limited (BPCL) is a government-owned company (52.98% equity stake as on March 31, 2020) with the 'Maharatna' status. The company was formed as Bharat Refineries Limited (BRL) in 1976 by the merger of Burmah Shell Oil Storage and Distribution Company of India and Burmah Shell Refineries Ltd. The company was renamed as BPCL in 1977. BPCL is the second largest oil marketing company, with domestic sales volumes of over 43.36 MMT (million metric tonne) and third-largest refining company in India with total refining capacity of 38.30 MMT. The company operates a 12 MMTPA refinery in Mumbai and a 15.5 MMTPA refinery in Kochi. Further, it has a majority stake in the 3 MMTPA refinery of Numaligarh Refinery Limited in Assam and 7.8 MMPTA refinery of Bharat Oman Refineries Limited in Bina, Madhya Pradesh. The company has 16250 retail outlets and 2,241 km of product pipelines for marketing of its products.

## Key Financial Indicators - Audited

	FY2019	FY2020
Operating Income (Rs. crore)	23,905.9	30,386.1
PAT (Rs. crore)	106.7	-803.5
OPBDIT/ OI (%)	7.6%	7.6%
RoCE (%)	6.6%	-4.0%
Total Debt/ TNW (times)	2.3	2.3
Total Debt/ OPBDIT (times)	5.5	9.2
Interest coverage (times)	2.7	1.2
NWC/ OI (%)	13%	1%

**Status of non-cooperation with previous CRA: Not applicable**

**Any other information: None**

### Rating history for last three years:

	Instrument	Current Rating (FY2021)				Rating History for the Past 3 Years		
		Type	Amount Rated	Amount Outstanding	Rating	FY2020	FY2019	FY2018
					01-Jul-2020	16-Dec-2019	20-Nov-2018	28-Sep-2017
1	NCD	Long Term	1000.0	-	[ICRA]AAA& (Watch with developing implications)	-	-	-
2	Commercial Paper	Short Term	300.0	-	[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](http://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
--	Commercial Paper	--	--	7-365 days	300.0	[ICRA]A1+
-	Non-Convertible Debentures^	-	-	-	1000.0	[ICRA]AAA& (Watch with developing implications)

Source: Bharat Oman Refineries Limited; ^ Yet to be placed

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