Indian Oil Corporation Limited

January 11, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-Convertible Bonds - Series-VIIIB	1,070.00	1,070.00	[ICRA]AAA (Stable); Reaffirmed
Non-Convertible Bonds- Series- IX	1,600.00	0	[ICRA]AAA (Stable) Withdrawn
Non-Convertible Bonds- V	31.60	0	[ICRA]AAA (Stable) Withdrawn
Commercial Paper	40,000.00	40,000.00	[ICRA]A1+; Reaffirmed
Total	**42,701.60**	**41,070.00**	

**Instrument details are provided in Annexure-1*

Rating action

ICRA has reaffirmed the long-term rating of [ICRA]AAA (pronounced ICRA triple A) assigned to the Rs. 1,070 crore[1] bond programme of Indian Oil Corporation Limited (IOC). ICRA has also withdrawn the [ICRA]AAA rating assigned to the Rs. 1,631.6 crore bond programmes (Bond Series V and IX) of IOC as the company has fully redeemed these instruments and there is no amount outstanding against these rated instruments. ICRA has also reaffirmed the short-term rating of [ICRA]A1+ (pronounced ICRA A one plus) assigned to Rs. 40,000.00 crore commercial paper programme of IOC. The outlook on the long-term rating is 'Stable'.

Rationale

The reaffirmation of the ratings reflects IOC's high financial flexibility arising from its large sovereign ownership (56.98% stakes owned by the GoI), significant portfolio of liquid investments (worth ~Rs. 33,700 crore currently), and ability to raise funds from the domestic/foreign banking system and capital markets at competitive rates. Besides, the ratings of the company continue to reflect its dominant and strategically important position in the Indian energy sector, its integrated business model and its role in fulfilling the socio economic objectives of the GoI. Although, regulatory risks for IOC related to pricing of sensitive petroleum products have increased with the recent spike in crude oil prices, the past track record of the GoI to ensure low under-recovery levels for PSU OMCs provides comfort from the credit perspective.

The ratings take into account the diversified location base of the company's refineries (11 refineries on a consolidated basis). The ratings also reflect integration of IOC in marketing, pipelines, and petrochemicals segments (contributing 20%, 17% and 21% respectively in total EBITDA[2] for FY2017) reducing cyclicality associated with the refining segment (contributing 37% of EBITDA in FY2017). The ratings also factor in the vulnerability of the company's profitability to the global refining margin cycle, import duty protection, and INR-USD parity levels. IOC is also exposed to project implementation risks as it is in the midst of implementing large projects spanning the entire downstream value chain, though the risk is largely mitigated by the company's proven track record of successfully implementing several large projects.

[1] *100 lakh = 1 crore = 10 million*

[2] *EBITDA: Earnings before Interest, Taxes, Depreciation, and Amortisation*

Outlook: Stable

The stable outlook on the rating reflects ICRA's expectation of continued GoI support owing to strategic and economic importance of IOC for the government. The outlook may be revised to Negative in case of material deterioration in credit metrics owing to large debt-funded capital expenditure (capex) plans or an adverse change in gross under-recoveries (GURs) sharing mechanism leading to significant burden on PSU oil marketing companies (OMCs) including IOC.

Key rating drivers

Credit strengths

Strategic importance for the GoI in the domestic energy sector - IOC, being the largest oil refining and marketing company in India, commands considerable economic importance. The company holds significant strategic importance for GoI as it helps in meeting the socio-economic objectives of the government through control on prices of sensitive products like subsidised liquefied petroleum gas (LPG) and superior kerosene oil (SKO). The company is also the largest contributor to the government exchequer. Thus, the sovereign support is expected to continue going forward as well.

Dominant position in the domestic refining and marketing business - The company dominates the domestic refining sector with a share of 32.6%. The company is also the leading public oil marketing company with a ~45% market share (including private players) as of end of FY2017. The company has the largest marketing network spanning across the country and actively undertakes multiple branding and customer loyalty initiatives.

Diversified location base of the refineries - The company owns and operates nine refineries spread across the country besides having a majority stake in Chennai Petroleum Corporation Limited (CPCL), which provides it control over an additional two refineries, taking the aggregate to eleven. Six out of its nine refineries are located in inland areas. The most recently set up refinery at Paradip, being situated at the coast, has improved IOC's diversification from the perspective of land-locked vis-à-vis coastal presence.

Integration in marketing, pipelines, and petrochemicals segments reducing cyclicality associated with the refining segment – IOC's large marketing operations generate largely stable profits, although subject to risks related to regulatory developments and inventory gains/losses to some extent. Further, a large pipeline infrastructure owned by the company also results in stable cash generation for the company. The forward integration of IOC into petrochemical segment provides operational synergies, like conversion of surplus products in the country such as naphtha, into higher value petrochemicals (like HDPE, PP etc), which also lead to higher margins. Overall, significant integration across segments reduces the risks related to refining operations.

Demonstrated support of GoI to ensure the profitability of OMCs in the years of high under-recoveries - The GoI has provided dedicated support to cushion the OMCs from high under-recoveries especially in years of high crude oil prices like FY2012 and FY2013. In FY2015, the GoI institutionalised a subsidy sharing framework wherein large part of the under recoveries were borne by it through budgetary allocation. Further, materially lower under-recoveries in the last two years have led to improvement in liquidity due to fall in debt levels and lower interest burden. IOC's net under-recoveries have declined from Rs. 1,201 crore in FY2015 to nil in FY2016 and FY2017.

Considerable liquidity and financial flexibility derived from its investment portfolio and significant sovereign ownership - IOC continues to enjoy high financial flexibility, that has enabled it to borrow from the domestic and overseas banking system and capital markets at competitive rates, to fund its large working capital requirements and for project finance. The same is supported by IOC's strong parentage arising from the GoI's 56.98% stake. The company's investments in ONGC, GAIL, and Oil India with current aggregate market value of ~Rs. 22,350 crore, besides unsold stock of GoI Special Oil bonds and GoI securities of ~Rs. 11,350 crore as on March 31, 2017 provide considerable financial flexibility.

Credit challenges

Vulnerability of the company's profitability to the global refining margin cycle, import duty protection, and INR-USD parity levels - Given the nature of the business, the company would remain exposed to the movement in the commodity price cycles and the volatility in the crude prices. Any adverse changes in the import duty on its products would also have an impact on the company's domestic sales. The company's profitability is also exposed to the forex rates (INR-US$) given the business is largely dollarized on sales, crude procurement and foreign currency loans.

Increase in regulatory risk related to under-recoveries due to spike in crude oil prices; consistent fall in consumption of kerosene to partly offset the risk – Higher crude oil prices, if sustained, would lead to material increase in gross under-recoveries (GURs) and consequently raise the working capital requirements and short-term debt levels of OMCs, thereby negatively impacting their profitability. ICRA expects GURs for OMCs to increase from Rs. 197 billion in FY2017 to ~Rs. 220-250 billion in FY2018 (assuming average Indian basket crude price of US$56-59/bbl) and to ~Rs. 300-350 billion in FY2019 (at crude price of US$65-70/bbl). If PSU OMCs are directed to share a part of higher GURs, it could be a key negative for their profitability. Although regulatory risks for OMCs (including IOC) related to pricing of sensitive petroleum products have increased with the spike in crude oil prices, the past track record of the GoI to ensure low under-recovery levels provide comfort from the credit perspective.

New project implementation risks, partly mitigated by the long demonstrated history of IOC in implementing projects across refining, marketing, petrochemicals and pipelines segments - The company has significant capex plans spanning the entire downstream value chain with an outlay of ~Rs. 1,800 billion over next 6-7 years. The capex plans include the ongoing up-gradation of refineries for production of BS-VI compliant fuel, brownfield expansion of refineries, setting up of nearly 6,500 km of pipeline infrastructure, investments in setting up of retail infrastructure, setting up of petrochemical plants etc. Besides, the company also plans to setup a mega refinery in a JV with other two PSU OMCs on the west coast of India for nearly $40 billion (IOC's share of $20 billion). Any material time or cost overruns in the group projects could lead to an increase in the company's borrowing levels and moderation of credit metrics. However, the risk is largely mitigated by the company's proven track record of successfully implementing several large projects.

With the company increasing its upstream portfolio it is exposed to geological, technology and execution risks that are inherent in E&P activities – The company currently has upstream portfolio of 17 blocks (domestic and overseas) and has been actively trying to expand the same. However, increasing presence in the upstream sector exposes the company to geological, technological and execution risks that are inherent in E&P activities.

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 Downstream Oil Companies

About the company

IOC is currently the largest corporate entity in India by sales. Government of India (GoI) has 56.98% equity stake in the company. The company and its subsidiaries have a total refining capacity of 80.7 MMTPA, which is 34% (as on March 31, 2017) of the total domestic refining capacity. The company accounted for 40% of the total petroleum products sold within the country in FY2017. IOC also enjoys a dominant presence in the domestic crude and product transportation business, controlling significant share in the country's total downstream pipeline capacity. The company has interests across the gas value chain as well, from LNG import terminals to city gas distribution networks (CGD). The company currently operates CGD networks in Agra and Lucknow through Green gas Limited (joint venture with GAIL (India) Limited); besides, the company is also implementing CGD projects in Chandigarh, Allahabad, Panipat, Daman, Ernakulam, Udhamsingh Nagar, and Dharwad through IndianOil-Adani Gas Private Limited - a JV with the Adani group.

In FY2017, as per audited results, the company reported a net profit of Rs. 19,745.3 crore on an operating income of Rs. 355,310.1 crore, as compared to a net profit of Rs. 12,167.8 crore on an operating income of Rs. 346,044.7 crore in the previous year.

Key financial indicators (audited)

	FY 2016	FY 2017
Operating Income (Rs. crore)	346,044.7	355,310.1
PAT (Rs. crore)	12,167.8	19,745.3
OPBDIT/ OI (%)	7.4%	9.7%
RoCE (%)	17.8%	21.1%
Total Debt/ TNW (times)	0.6	0.6
Total Debt/ OPBDIT (times)	2.3	1.8
Interest coverage (times)	7.3	9.2
NWC/ OI (%)	-4.9%	-4.6%

Source: ICRA estimates; 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: None

Rating history for last three years:

	Instrument	Current Rating (FY2018) Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs Crore)	Date & Rating Jan 2018	Chronology of Rating History for the past 3 years: Date & Rating in FY2017 Jan 2017	Date & Rating in FY2016 Dec 2015	Date & Rating in FY2015 Jul 2014
1	Commercial Paper	Short Term	40,000.00	NA	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**
2	Non-Convertible Bonds - Series-VIIIB	Long Term	1,070.00	1,070.00	**[ICRA]AAA (Stable)**	**[ICRA]AAA (Stable)**	**[ICRA]AAA (Stable)**	**[ICRA]AAA (Stable)**
3	Non-Convertible Bonds- Series- IX and V	Long Term	0	0	**[ICRA]AAA (Stable) Withdrawn**	**[ICRA]AAA (Stable)**	**[ICRA]AAA (Stable)**	**[ICRA]AAA (Stable)**

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 Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE242A07207	Non-Convertible Bonds Series-VIIIB	10-Sep-08	11.00%	10-Sep-18	1,070.00	[ICRA]AAA (Stable)
NA	Commercial Paper	NA	NA	7-365 days	40,000.00	[ICRA]A1+

Source: Indian Oil Corporation 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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