Hindustan Petroleum Corporation Limited

January 08, 2019

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-Convertible Debenture Programme	3,000	3,000	[ICRA]AAA (Stable); Reaffirmed
Commercial Paper	15,000	15,000	[ICRA]A1+; Reaffirmed
Cash Credit Limits	4,000	4,000	[ICRA]AAA (Stable); Reaffirmed
Fund based Limits	24,000	24,000	[ICRA]AAA (Stable); Reaffirmed
Non-fund Based Limits	17,000	17,000	[ICRA]A1+; Reaffirmed
Issuer Rating	-	-	[ICRA]AAA (Stable); Reaffirmed
Total	**63,000**	**63,000**	

*Instrument details are provided in Annexure-1

Rationale

The reaffirmation of ratings takes into account HPCL's strategic importance in the domestic energy sector, its strong parentage with Oil and Natural Gas Corporation Limited ([ICRA]A1+) owning 51.1% equity stake, its established brand name and leading position in the domestic oil marketing business. The ratings favourably consider the coastal location of the company's refineries which provides logistical advantages for import of crude oil and export of petroleum products. The ratings also factor in the strong operational efficiencies of the company with both its refineries (Mumbai and Vishakhapatnam) operating at more than 100% utilisation levels and maintaining healthy energy consumption levels. HPCL is undertaking modernisation and capacity expansion at both its refineries and the same is expected to improve the profitability from the company's refining operations upon completion. The company has witnessed steady growth in its marketing volumes (CAGR of 4.5% over the last 5-year period) driven by its growing network of retail outlets, strong demand indicators for motor spirit and diesel, and its established presence in this business segment. The liquidity profile of HPCL is robust backed by anticipated healthy cash flow from operations, a sizeable portfolio of liquid investments and adequate availability of working capital bank limits.

HPCL will continue to be subjected to regulatory risk on the pricing of sensitive petroleum products as seen in the recent intervention by the Government of India (GoI) in October 2018 to reduce selling prices of Motor Spirit (MS) and High Speed Diesel (HSD). Nonetheless, the GoI has been ensuring that the net under recoveries borne by Public Sector Undertaking (PSU) oil marketing companies (OMCs) are within manageable levels by absorbing most of the gross under-recoveries (GURs) itself with the rest shared by upstream companies. Any adverse change in the GoI's policy in this regard, resulting in a weakening of key credit metrics of HPCL. will be a key rating sensitivity.

HPCL is also exposed to project implementation risks as it is in the midst of implementing large projects spanning the entire downstream value chain on its own books as well as through subsidiaries and joint ventures (JV). The scale of HPCL's expansion plans would lead to some moderation in its debt coverage metrics over the next 3-4 years, but ICRA expects the same to remain comfortable. Nonetheless, any material time or cost overruns that could lead to larger-than-estimated funding requirements would be a key rating sensitivity.

Outlook: Stable

ICRA believes HPCL will continue to benefit from its position in the domestic energy sector, its strategic importance to the GoI and its strong parentage. The outlook may be revised to 'Negative' if there is a significant increase in net under-recoveries due to change in government policies on pricing/subsidy sharing on sensitive petroleum products, or if there is a material time/cost overrun in the ongoing group projects leading to weakening of HPCL's credit metrics. Any sizeable mergers & acquisitions undertaken by HPCL would be a rating sensitivity.

Key rating drivers

Credit strengths

Demonstrated support of the GoI to ensure the profitability of OMCs in the past despite high under-recoveries – The GoI has provided dedicated support to cushion the OMCs from high under-recoveries in the past by institutionalising a subsidy sharing framework wherein large part of the under recoveries are borne by it through budgetary allocation. In H1 FY2019, the gross under-recoveries for HPCL increased to Rs. 545 crore from Rs. 330 crore in H1 FY2018 due to the increase in crude prices and depreciation of INR against US Dollar which would be met through budgetary support from the GoI. Notwithstanding change in majority ownership in favour of Oil and Natural Gas Corporation Limited (ONGC), ICRA believes HPCL will continue to be of strategic importance to the GoI as it will continue to play a key role in fulfilling socio-economic policies of the GoI. Any adverse change in the GoI's policy in this regard will be a key rating sensitivity.

Locational advantages of being a coastal refinery for sourcing of crude as well as exports – HPCL owns and operates two refineries, one in Mumbai and the other in Visakhapatnam. Since both the refineries are located in coastal regions, the company enjoys logistical benefits in terms of lower costs and time taken to transport the imported crude to the refineries and to export refined products to dealer locations. This also lowers the company's inventory requirement to a significant extent when compared to other OMCs with inland refineries.

Established brand name and position in the domestic refining and marketing business – The company is one of the three leading public OMCs with a ~20% market share (including private players) as of end of FY2018. The company has the second-largest marketing network spanning across the country and actively undertakes multiple branding and customer loyalty initiatives.

Healthy refining operations with steady GRM levels – HPCL has reported refinery utilisation levels above 100% for the past few years. The company's GRMs have remained stable driven by operational efficiencies and effective crude procurement strategies. However, in H1 FY2019, the company's GRMs declined to US$ 5.93/bbl from US$ 6.75/bbl in H1 FY2018 owing to significantly higher crude prices and adverse movement in light distillate cracks on YoY basis.

Healthy financial flexibility – The company enjoys high financial flexibility that allows it to raise debt and access capital markets at competitive rates to fund its capex and working capital requirements. The same is supported by HPCL's strong parentage arising from the ONGC's 51.1% stake.

Credit challenges

Vulnerability of the company's refining segment's profitability to the global refining margin cycle, crude price volatility, import duty protection, and INR-US$ 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 forex loans.

Moderate financial profile - Although HPCL has demonstrated healthy credit metrics in FY2018 and H1 FY2019, its key credit metrics, such as Total Debt/OPBDITA, interest coverage and RoCE[1], over a longer period have been moderate. Moreover, with large capital outlay on the ongoing projects, its metrics would not see any meaningful improvement over the next 3-4 years till the investments start yielding healthy returns.

Significant capex planned over next four-year period – The company is in the midst of aggressive capex plans of ~ Rs. 75,500 crore (including equity investments of ~Rs. 12,000 crore in JVs) outlined for the period between FY2019 and FY2023. HPCL's capex plans include the implementation of major projects such as the capacity expansion at both its refineries, expansion of its pipeline network and setting up of new pipelines. The company would also have significant equity contribution towards key JV projects including the refinery-cum-petrochemical complex in Rajasthan (74% stake) and the setting up of an LNG terminal in Gujarat (50% stake). Any material time or cost overruns in the group projects could lead to an increase in the company's borrowing levels and weakening of credit metrics.

Liquidity Position:

HPCL's liquidity profile remains highly comfortable aided by healthy cash flow generation and sizeable cash and cash equivalents (Rs. 5,777 crore on standalone books as of September 30, 2018). Further, the company has adequate fund based and non-fund based working capital limits, a sizeable part of which is unutilised. The company also enjoys high financial flexibility owing to its strong parentage.

Analytical approach:

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Downstream Oil Companies
Parent/Group Support	Parent: Oil and Natural Gas Corporation Limited The assigned rating factors in the systemic importance that HPCL holds, which we expect should induce the government/ONGC to extend timely policy/financial support to the rated entity, should there be a need
Consolidation / Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of HPCL. ICRA has factored in the rated entity's support to fund the equity component of the investment in its JV projects, any cost overruns and, and debt servicing support in the initial stage of operations. The subsidiaries and JVs of HPCL that have been considered are enlisted in Annexure 2.

About the company:

HPCL is a public sector enterprise that owns and operates two refineries, one in Mumbai with a 7.5 million metric tonnes per annum (MMTPA) capacity and one in Visakhapatnam with a 8.3 MMTPA capacity. The 'Navratna' status company was incorporated in 1952 as Standard Vacuum Refining Company of India Limited. HPCL has a 49% stake in a JV with Mittal Energy Investments Pte. Limited for operating a 11.3 MMTPA refinery in Bhatinda, Punjab. HPCL also has a 16.95% equity stake in Mangalore Refinery and Petrochemicals Ltd. (MRPL), which operates a 15 MMTPA refinery in Mangalore. Majority shareholding of HPCL (51.1%) is held by ONGC which had been acquired from the GoI in January 2018.

[1] Return on capital employed

Key financial indicators (Consolidated - audited)

	FY2017	FY2018
Operating Income (Rs. crore)	187,493	219,510
PAT (Rs. crore)	8,236	7,218
OPBDIT/OI (%)	5.8%	4.9%
RoCE (%)	26.4%	22.0%
Total Debt/TNW (times)	1.1	0.9
Total Debt/OPBDIT (times)	2.0	2.0
Interest coverage (times)	17.9	17.5

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

		Current Rating (FY2019)						Chronology of Rating History for the Past 3 Years	
	Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating January 2019	Date & Rating in FY2018 March 2018	December 2017	Date & Rating in FY2017 -	Date & Rating in FY2016 -
1	NCDs	Long term	3,000	-	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-	-	-
2	Commercial Paper	Short term	15,000	-	[ICRA]A1+	[ICRA]A1+	-	-	-
3	Cash Credit	Long term	4,000	-	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-	-	-
4	Fund Based Limits	Long term	24,000	-	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-	-	-
5	Non-Fund Based Limits	Short term	17,000	-	[ICRA]A1+	[ICRA]A1+	-	-	-
6	Issuer Rating	-	-	-	[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
NA	NCDs	Yet to be placed	-	-	3,000.0	[ICRA]AAA (Stable)
NA	Commercial Paper	-	-	7-365 days	15,000.0	[ICRA]A1+
NA	Cash Credit Limits	-	-	-	4,000.0	[ICRA]AAA (Stable)
NA	Fund Based Limits	-	-	-	24,000.0	[ICRA]AAA (Stable)
NA	Non-Fund Based Limits	-	-	-	17,000.0	[ICRA]A1+
NA	Issuer Rating	-	-	-	-	[ICRA]AAA (Stable)

Source: Hindustan Petroleum Corporation Limited

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Prize Petroleum Co. Ltd.	100.00%	Full Consolidation
HPCL Biofuels Ltd.	100.00%	Full Consolidation
HPCL Middle East FZCO	100.00%	Full Consolidation
HPCL Rajasthan Refinery Limited	74.00%	Limited Consolidation
HPCL Shapoorji Energy Private Ltd.	50.00%	Limited Consolidation
Ratnagiri Refinery and Petrochemicals Limited	25.00%	Limited Consolidation
HPCL Mittal Energy Ltd.	48.99%	Limited Consolidation
Bhagyanagar Gas Ltd.	24.99%	Limited Consolidation
Aavantika Gas Ltd.	49.98%	Limited Consolidation
Petronet India Ltd.	16.00%	Limited Consolidation
Petronet MHB Ltd.	32.72%	Limited Consolidation
Godavari Gas Private Limited	26.00%	Limited Consolidation
Hindustan Colas Pvt. Ltd.	50.00%	Limited Consolidation
South Asia LPG Co. Pvt. Ltd.	50.00%	Limited Consolidation
Mumbai Aviation Fuel Farm Facility Pvt. Ltd.	25.00%	Limited Consolidation

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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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