September 20, 2022

Chennai Petroleum Corporation Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-Convertible Debenture Programme	1000.0	1000.0	[ICRA]AAA(Stable) reaffirmed
Non-Convertible Debenture Programme	1000.0	1000.0	[ICRA]AAA(Stable) reaffirmed
Commercial Paper	7500.0	7500.0	[ICRA]A1+ reaffirmed
Total	**9500.0**	**9500.0**	

**Instrument details are provided in Annexure-I*

Rationale

The ratings reflect the majority ownership (51.9%) of Indian Oil Corporation Limited (IOC; rated [ICRA] AAA(Stable)/[ICRA]A1+) in Chennai Petroleum Corporation Limited (CPCL) and the strong business linkages between them, particularly for sourcing imported crude oil and product offtake. ICRA believes IOC would support CPCL to meet its financial obligations, should the need arise. CPCL remains strategically important to IOC as the latter meets its product requirement for the South Indian market from the former.

The ratings also reflect CPCL's established position in the refining business and strong operational efficiencies operating at high utilisation levels in Q4 FY2022 and Q1 FY2023. Further, after a significant decline in FY2020, the gross refining margins (GRM) started to witness a steady improvement. Over the last few quarters, the GRMs have remained strong as the crack spreads of most products improved on account of rising demand and inventory gains, resulting in healthy EBITDA generation for the company. The GRM improved to $25.0/bbl in Q1 FY2023 and $8.9/bbl in FY2022 from $7.1/bbl in FY2021. While the GRM is likely to moderate, going forward, the profit generation for the current fiscal is likely to remain healthy.

The rating, however, also considers the vulnerability of the company's profitability to the global refining margin cycle, import duty protection and INR-USD parity levels. The rating also factors in CPCL's moderate capital structure. The company is also exposed to project implementation risks as CPCL is in the midst of an investment/capex cycle; however, the risk is significantly mitigated by CPCL's track record of implementing several large projects. The company is setting up a 9-MMTPA refinery project at Cauvery Basin Refinery, Nagapattinam district, at an estimated cost of Rs.31,580 crore, in a JV with IOC and other seed equity investors. CPCL's equity investment for the project is estimated at Rs. 2,570 crore towards its 25% contribution.

The Stable outlook on the [ICRA]AAA rating reflects ICRA's opinion that CPCL will continue to benefit from its strategic importance to the IOC Group and its favourable geographic location.

Key rating drivers and their description

Credit strengths

Strong parentage - IOC has a controlling stake in the company with a 51.9% shareholding. CPCL derives significant operational benefits as part of the IOC Group for sourcing imported crude oil and product offtake. IOC had also extended financial support to CPCL in FY2016 by subscribing to Rs. 1,000.0-crore non-convertible preference shares on a private placement basis. However, in June 2018, with the improvement in financial performance in the preceding two fiscals, CPCL repaid Rs. 500.0 crore of non-convertible preference shares to IOC. ICRA believes due to CPCL's strategic position within the IOC Group in South India, it would support CPCL to meet its financial obligations, should the need arise.

IOC, being the largest oil refining and marketing company in India, commands considerable economic importance. IOC holds significant strategic importance for the 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 IOC Group is also the largest contributor to the Government exchequer. Thus, the sovereign support is expected to continue, going forward.

The IOC Group dominates the domestic refining sector with a share of over 30%. It is also the leading public oil marketing company with a healthy market share in the petroleum products sold in the country (including private players). The IOC Group has the largest marketing network spanning across the country and undertakes multiple branding and customer loyalty initiatives.

Low demand risk due to locational advantage; integrated operations of Group mitigate cyclicality risk in refining segment of consolidated entity – CPCL benefits from being the only refinery company for the IOC Group in South India, resulting in low demand risk. Over the last decade, IOC has implemented several pipeline projects to evacuate products from CPCL in a cost-effective manner and to strengthen its presence in the southern market.

Financial flexibility with lenders - Due to its extensive track record and strong parentage, CPCL enjoys high financial flexibility with its lenders, allowing it to avail debt at a short notice at low interest rates.

Credit challenges

Leveraged capital structure and project implementation risks - CPCL's financial risk profile is characterised by a leveraged capital structure. While the debt outstanding increased as on March 31, 2022 compared with March 31, 2021, the gearing witnessed some moderation to 3.1 times as on March 31, 2022 against 5.7 times as on March 31, 2021 due to the improvement in the net worth position with a better operating performance. While the GRM is likely to moderate, going forward, the profit generation for the current fiscal is likely to remain healthy, improving the net worth position and capital structure.

The company is also exposed to project implementation risks as CPCL is in the midst of an investment/capex cycle; however, the risk is significantly mitigated by CPCL's track record of implementing several large projects.

Vulnerability of profitability to global refining margin cycle, import duty protection and INR-USD parity levels – CPCL has limited pricing flexibility and its margins are vulnerable to the movements in international crude prices and crack spreads, import duty differentials and foreign exchange rate (INR-US$). This was reflected in FY2019 and FY2020, when the company's margins contracted because of inventory losses and weak crack spreads. However, in the past, the impact of foreign exchange (forex) rates volatility on profitability has been limited.

Further, over the last few quarters, the GRMs have remained strong as the crack spreads of most products improved on account of rising demand and inventory gains, resulting in healthy EBITDA generation. The strong operational efficiencies with CPCL operating at high utilisation levels in Q4 FY2022 and Q1 FY2023 also supported the EBITDA.

Liquidity position: Adequate

The company's fund flow from operations had remained positive in FY2022 and is likely to be healthy in FY2023 given the healthy GRM. It has a repayment obligation of ~Rs. 1,359 crore in FY2023 and is in the midst of an investment/capex cycle. However, the liquidity is expected to remain adequate, supported by cash accruals, unutilised working capital limits and the ability to raise funds at a short notice for refinancing, if required, benefiting from the strong financial flexibility with lenders due to its parentage

Rating sensitivities

Positive factors – Not applicable.

Negative factors – Downward pressure on CPCL's ratings could arise if there is sustained weakening of the credit profile of CPCL, or if the credit profile of its parent, IOC, weakens, or if the linkages between IOC and CPCL deteriorate.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	[Corporate Credit Rating Methodology](#) [Rating Methodology for Entities in the Oil & Gas (Downstream)](#) [Rating Approach - Implicit parent or group support](#)
Parent/Group support	**Parent – Indian Oil Corporation Limited** ICRA expects CPCL's parent, IOC, to remain willing to extend financial support to CPCL, (rated [ICRA]AAA(Stable)/[ICRA]A1+), should there be a need, given the high strategic importance that CPCL holds for IOC and the strong operational linkages between the two companies
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of CPCL. As on March 31, 2022, the company had two joint ventures, which are all enlisted in Annexure-2.

About the company

CPCL, earlier known as Madras Refineries Limited (MRL), was established in December 1965 as a joint venture of the Government of India (GoI), Amoco Inc. of US (Amoco), and the National Iranian Oil Company (NIOC), with their initial equity contributions in the venture being in a ratio of 74:13:13. In 1985, Amoco divested its equity holding in favour of the GoI. CPCL came out with a public issue in 1994, wherein the GoI divested part of its equity stake. In FY2001, the GoI sold its stake in CPCL to IOC as part of its efforts to insulate standalone refineries from market volatility, following the dismantling of the administered pricing mechanism (APM). As on June 30, 2022, IOC held 51.9% equity stake in CPCL, with NIOC and others holding 15.4% and 32.7%, respectively. CPCL currently operates a 10.5-mmtpa refinery in Manali, near Chennai. Being a standalone refinery, CPCL's products, barring a few industrial feedstock and fuels, have always been sold by oil marketing companies. After IOC's acquisition of a majority stake in CPCL, the bulk of the latter's output is sold through IOC.

Key financial indicators (audited)

CPCL Consolidated	FY2021	FY2022
Operating income	22,444.8	43,375.4
PAT	231.7	1,336.4
OPBDIT/OI	9.2%	6.5%
PAT/OI	1.0%	3.1%
Total outside liabilities/Tangible net worth (times)	8.6	5.9
Total debt/OPBDIT (times)	4.4	3.3
Interest coverage (times)	5.5	6.9

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore; Note: Amount in Rs. crore; All calculations are as per ICRA Research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2023)				Chronology of rating history for the past 3 years			
		Type	Amount rated (Rs. crore)	Amount outstanding as on June 30, 2022 (Rs. crore)	Date & rating in FY2023	Date & rating in FY2022		Date & rating in FY2021	Date & rating in FY2020
					Sep 20, 2022	Sep 20, 2021	Apr 16, 2021	Jun 12, 2020	Jan 06, 2020
1	NCD	Long-term	1000.0	810.0	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-
2	NCD	Long-term	1000.0	775.0	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-	-
3	Commercial Paper	Short term	7500.0	0.0	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

Complexity level of the rated instruments

Instrument	Complexity Indicator
NCD	Very Simple
Commercial Paper	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: www.icra.in

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
INE178A08029	**NCD**	17-Jul-2020	5.78%	17-Jul-2025	810.0	[ICRA]AAA(Stable)
INE178A08037	**NCD**	23-Jun-2021	5.44%	24-Jun-2024	775.0	[ICRA]AAA(Stable)
NA	**NCD**	Not issued	NA	NA	415.0	[ICRA]AAA(Stable)
NA	**Commercial Paper**	NA	NA	NA	7500.0*	[ICRA]A1+

*Source: Company; * Commercial Paper -Nil O/s as on June 30, 2022.*

Annexure II: List of entities considered for consolidated analysis

Company Name	CPCL Ownership	Consolidation Approach
Indian Additives Ltd.	50.00%	Equity Method
National Aromatics and Petrochemicals Corporation Ltd.	50.00%	Equity Method

Source: Company annual report FY2022

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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.

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