

Nayara Energy Limited

December 13, 2022

Ratings

| Facilities/Instruments | Amount (₹ crore) | Rating ¹ | Rating Action |
|--|---|---|---|
| Long-term bank facilities | 16,145.76 (Reduced from 17,149.50) | CARE AA-; Stable (Double A Minus; Outlook: Stable) | Reaffirmed and removed from Credit watch with Developing Implications; Stable outlook assigned |
| Short-term bank facilities | 14,855.00 | CARE A1+ (A One Plus) | Reaffirmed |
| Total bank facilities | 31,000.76 (₹ Thirty-one thousand crore and seventy-six lakh only) | | |
| Non-convertible debentures | 256.84 | CARE AA-; Stable (Double A Minus; Outlook: Stable) | Reaffirmed and removed from Credit watch with Developing Implications; Stable outlook assigned |
| Non-convertible debentures | 2,285.00 | CARE AA-; Stable (Double A Minus; Outlook: Stable) | Reaffirmed and removed from Credit watch with Developing Implications; Stable outlook assigned |
| Total long-term instruments | 2,541.84 (₹ Two thousand five hundred forty-one crore and eighty-four lakh only) | | |

Details of instruments/facilities in Annexure-1.

Detailed rationale and key rating drivers

CARE Ratings Limited (CARE Ratings) has reaffirmed the ratings assigned to the bank facilities and debt instruments of Nayara Energy Limited (Nayara) and removed it from 'Credit Watch with Developing Implications' (CWD). CARE Ratings has observed that the overall operations and finances of the company have remained unimpacted by the ongoing conflict between Russia and Ukraine and the related political and economic developments. The ratings were earlier placed on CWD following the geo-political events and the resultant economic impact due to sanctions being put on Russia and certain Russian entities and persons.

The ratings continue to derive strength from the strong operating profile of the company as it operates India's second-largest single-location refinery with a high Nelson Complexity Index (NCI), the strategic location of its refinery along with captive port terminal and power plant, the healthy throughput levels in FY22 (FY refers to the period from April 1 to March 31) and H1FY23, the long-term benefits being derived from forward-integration in the form of a sizeable and growing presence in the fuel retailing space, and the improvement in the gross refining margins (GRMs) in FY22 and the current fiscal (until H1FY23), resulting in improved financial performance of the company. The ratings continue to consider the strong risk management systems put in place by Nayara to hedge

¹ Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

against fluctuations in currency and crude oil prices, while its presence in retail provides stability to the company's revenue stream and insulates the business from vagaries of fluctuations in the refining segment.

These ratings strengths are, however, tempered by the negative impact of the ongoing Russia-Ukraine conflict on the credit profile of Rosneft Oil Company (Rosneft; one of the key shareholders of Nayara), Nayara's exposure to the fluctuations in crack spreads, the moderate (although improving) debt metrics, the competitive industry scenario as well as inherent government regulation risk in the Indian oil and gas sector, apart from risks associated with execution and stabilisation of the ongoing petrochemicals project.

Rating sensitivities

Positive factors – Factors that could lead to positive rating action/upgrade:

- The refinery operating at healthy throughput and gross refining margin (GRM) levels.
- Growth in the retailing business and significant improvement in return on capital employed (ROCE) on a sustained basis.
- Sustained improvement in the overall gearing
- Timely completion of the petrochemicals project within the estimated costs and economic ramping-up of the operations.

Negative factors – Factors that could lead to negative rating action/downgrade:

- Sustained fall in the throughput and GRMs or any adverse impact of the geopolitical situation on the operations of the company.
- Deterioration in capital structure, with the company incurring capex through higher-than-expected borrowings, affecting the overall gearing.

Detailed description of the key rating drivers

Key rating strengths

Strong operating profile: Nayara's refinery has one of the highest complexities across refineries in India – an NCI of 11.8 – which enables the company to process heavier grades of crude oil, resulting in higher margins as compared with low-complexity refineries. The refinery has a capacity of 20 million metric tonne per annum (MMTPA), which constitutes around 8% of India's refining capacity. It can process crude oil with a blend of 15-60 American Petroleum Institute gravity (API; a measure of how heavy or light petroleum liquid is compared with water). Since its commencement, the refinery has consistently achieved crude throughput more than its rated capacity of 20 million metric tonne (MMT), except in the cases of planned shutdown. The company remains exposed to concentration risk being a single-location refinery; however, the strong operational track record and adequate insurance policies in place mitigate the risk to a large extent. Going forward, though the throughput levels are expected to be impacted in Q3FY23 (because of the maintenance related planned shutdown), the operating profile is expected to remain strong thereafter, in the medium term.

Improved operational performance during FY22 and H1FY23: Owing to the pandemic, the demand for oil products declined in the first half of FY21, while there was an oversupply of oil during that period. This led to a reduction in prices by more than half, thereby resulting in a worsening of throughputs and product cracks after Q4FY20. In line with the industry trend, Nayara also witnessed a strong rebound in its operational performance, with the throughput improving to 101% in FY22 (85% in FY21 due to planned shutdown and covid impact) and 103% in H1FY23. On the back of healthy demand for petroleum products globally, the product cracks have also remained healthy, leading to an improvement in the GRM reported by the company during FY22 and H1FY23. All this has resulted in healthy growth in the scale of operations and improved profitability margins for the company. The operating income grew by a healthy 48% in FY22 on a y-o-y basis and by 34% in H1FY23 (UA) as compared with the same period last year. The growth in operating income was also supported by a surge in crude oil prices and an increasing retail presence of the company. Although the retail margins of the company were impacted in H1FY23 because of its inability to pass on the high crude oil prices to the customers, Nayara reported an improvement in the overall profitability margins on the back of healthy product cracks and improved GRMs. The profit before interest, lease rentals, depreciation and taxation (PBILD) and profit-after-tax (PAT) margins stood at 13.01% and 7.06%, respectively, during H1FY23, as compared with 2.67% and (-)0.41% in the same period last year.

Advantageous location along with a captive port terminal and power plant: Nayara's refinery is located at Vadinar, Gujarat, which is strategically located to cater to the demand of domestic and export markets. The company operates a captive all-weather port with a natural 32-m draft (deepest in India, allowing 365-day intake) and a Single Buoy Mooring (SBM) with a crude oil intake capacity of 27 MMTPA. The SBM is capable of handling very large crude carriers (VLCC) and is located in the Gulf of Kutch, which also houses SBMs of Indian Oil Corporation, Reliance Industries Limited, etc, forming a gateway to about 70% of the total crude imports by India. The port is equipped with two jetties capable of handling vessels up to the size of 100,000 deadweight tonnage for a total product off-take of 14 MMTPA each. Nayara also operates a captive power plant within the refinery premises, which is equipped with oil, gas, liquid and coal-fired boilers and turbines capable of generating a total of 1,010 MWe of co-generative thermal power. The company only utilises its coal-based 510 MWe unit to power its refinery and keeps the remaining units as a backup.

Growing retail operations: Nayara has a sizeable and growing presence in fuel retailing, with over 6,000 operational retail outlets as on September 30, 2022. The company has also built two greenfield rail-fed fuel depots at Wardha (Maharashtra) and Pali (Rajasthan) and hired depots to store its own products for increasing supply-chain efficiency, reducing logistic costs and its dependency on public sector undertakings (PSUs). Owing to outlets being operated primarily through the dealer-owned-and-dealer-operated (DODO) model, the capex requirement of the company is minimal. Its presence in the retail segment insulates the company from vagaries of volatility in the crack spread and GRMs in the refining segment, although the segment has been facing challenges in recent times in view of the high crude prices and elevated refinery transfer prices amid increased crack spreads. However, with declining crude oil prices, the gap in the Retail Selling Price and Refinery Transfer Price is expected to narrow down which should support company's margins from the segment

Key rating weaknesses

Significant deterioration in the credit profile of Rosneft: Nayara's shareholders comprise Rosneft Singapore Pte Limited and Kesani Enterprises Company Limited, a consortium led by Trafigura and UCP, together holding 49.13% share each in Nayara.

Rosneft is one of the world's largest public oil and gas companies in terms of reserves and production of liquid hydrocarbons. Rosneft is the leader in the Russian oil refining sector, owning 13 major refineries in key regions of Russia and ownership stakes in several refineries outside Russia, as well as a wide range of retail sites in 66 regions of Russia, Abkhazia, Belarus, and Kirghizia. Nayara has benefitted from Rosneft's position and expertise in the oil and gas sector, being one of the largest oil and gas players in the world. Rosneft infused funds amounting to \$490 million in Nayara Energy Singapore Pte Limited (NESPL), the Singapore based subsidiary of NEL in Q3FY22 and Q4FY22.

Trafigura, founded in 1993 and headquartered in Amsterdam, Netherlands, is one of the largest physical commodities trading groups in the world. Trafigura's trading business is supported by industrial and financial assets, including a majority ownership of global zinc and lead producer Nyrstar, which has mining, smelting and other operations located in Europe, the US and Australia; a significant shareholding in global oil products storage and distribution company Puma Energy; global terminals, warehousing and logistics operator Impala Terminals; Trafigura's Mining Group; and Galena Asset Management.

The UCP investment group is one of the largest financial investment groups in Russia. It was established in 2006 to manage the assets of its partners and co-investors. UCP has accumulated a wealth of investment experience while simultaneously proving the reliability and effectiveness of its investment strategies in turbulent market environments.

Recently, Rosneft has witnessed a sharp deterioration in its credit profile consequent to economic sanctions placed on Russia due to the ongoing conflict between Russia and Ukraine. However, it may be noted that Rosneft was already under sectoral sanctions ever since it became a shareholder of Nayara and there has not been any announcement of fresh sanctions on Rosneft. Consequently, the operations of Nayara are not impacted by the recently announced economic sanctions on Russia. The company does not have any major operational dependence on Russia or Russian entities, including Rosneft, as it sources crude oil from several countries such as Iraq, Egypt, countries in the Middle East and Latin America, etc, while major export destinations include Singapore, the Far East and the Middle East. However, CARE Ratings believes that Rosneft's flexibility to support Nayara, if required, in future may get impacted due to the weakening of the credit profile of Rosneft.

Moderate (although improving) debt metrics: Nayara's financial profile is marked by a moderately leveraged capital structure and moderate (though improving) debt credit metrics. The overall gearing (including finance lease) stood at 1.87x as on March 31, 2022, almost at the same level as last year (1.88x). The overall gearing

ratio, however, stood at 1.30x as on September 30, 2022, supported by accretion of healthy profits generated by the company during H1FY23 (UA). The interest coverage ratio improved to 2.76x in FY22 as compared with 1.68x in FY21, on the back of improved profitability generated by the company during the year. The interest coverage ratio improved significantly to 10.34x in H1FY23 (UA) as compared with 1.67x in the same period last year on the back of healthy profitability generated by the company during the period. Going forward, CARE Ratings believes that the company will report an improvement in gearing and debt metrics (compared to the FY22 levels) due to healthier profitability, irrespective of the debt drawdown for the ongoing petrochemicals project which entails a total project cost of ₹6,539 crore, to be funded through debt of ₹4,016 crore (fully tied-up) and the remaining from internal accruals and fund infusions. The company has spent around ₹2,626 crore on the project up to September 30, 2022, funded through debt of ₹1,375 crore and the rest through internal accruals and infusions and achieved physical progress of over 80%. The Scheduled Commercial Operation Date (SCOD) of the project is August 2023. The timely completion of the project and economic ramping-up of the same will remain crucial from the credit perspective.

Exposure to the volatility of crude prices, crack spreads, and foreign exchange rates: The oil prices and crack spreads are a function of many dynamic markets and fundamental factors such as global demand-supply dynamics, geo-political stability in countries with oil reserves, Organization of the Petroleum Exporting Countries (OPEC) policies, exchange rates, etc. The company, as per its policy, hedges its inventory exposure through forward contracts on a regular basis. The hedging helps the company mitigate and manage the price risk. Furthermore, the company imports the majority of its crude requirements, which are priced in US Dollar, leading to volatility associated with forex movements. The susceptibility to forex fluctuation is mitigated to a large extent, as the company exports nearly 40-50% of its products. Even domestic sales to oil manufacturing companies (OMCs) are linked in US Dollar, which further mitigates the risk.

Competitive industry and regulatory risk: The company faces stiff competition from PSU oil marketing companies, which own around 90% of the retail outlets in the country. However, post-deregulation of Motor Spirit (MS) and especially High-Speed Diesel (HSD), the company has been expanding its retail presence and remains committed to increase the same, going forward. Furthermore, the company is exposed to regulatory risk, as any interference by the Government of India (GoI), may affect its profitability. However, Nayara's sales consist of a sizeable proportion of exports, which offsets the impact to an extent. Though, the GoI has recently imposed windfall taxes on export of certain products like HSD and ATF, such tax incidence is likely to be self-correcting if the product margins normalise. Considering the above, the rating remains sensitive to any regulatory intervention.

Industry outlook

The global oil and gas industry is at an inflection point, with governments placing greater priorities on climate change, emerging alternative sources of energy and likely disruption in mobility with the adoption of gas, hydrogen, and electric-based transportation systems. While all these factors will impact industry growth prospects in the long term, the immediate outlook remains bright. However, declining global demand, expectations of restricted supplies because of the ongoing geo-political tension, etc, are expected to keep crude oil volatile in the near term. The prices of crude oil, which were already recovering from the COVID-19 impact since November 2020, increased dramatically in Q4FY22 due to the Russia-Ukraine conflict. In the immediate succeeding quarter, since several OPEC+ members were not able to meet their production share, the prices continued to remain elevated (average prices in Q1FY23 stood at US\$ 112.8 per barrel as compared with US\$ 99.5 per barrel in Q4FY22 and US\$ 79.4 per barrel in Q3FY22). However, with concerns about world economic growth, the crude oil price declined to US\$ 99 per barrel in Q2FY23 and further plummeted to US\$ 87 per barrel in the first week of December.

The outbreak of the COVID-19 pandemic had led to GRMs of global refiners plummeting to the lowest levels in a decade, as demand for refined products crashed, thereby impacting the crack spreads, while a significant decline in crude oil and refined products prices resulted in substantial inventory write-downs in FY21. The Singapore benchmark GRMs reduced to just US\$ 3.25 per barrel in FY20 and further to US\$ 1.20 per barrel in FY21, amid weak demand and high fluctuation in prices. Such low yearly GRMs were last seen in FY10. However, with the impact of the COVID-19 pandemic receding and global economies coming back on the recovery path, the GRMs have improved significantly. The Singapore benchmark improved to US\$8.60 per barrel in FY22 and further improved to US\$ 21.5 in Q1FY23 and US\$ 7.1 in Q2FY23. The Singapore benchmark GRMs are expected to remain healthy in the near future considering increased demand of diesel globally due to winter season

Liquidity: Strong

The company, as on September 30, 2022, had cash and cash equivalents of around ₹4,214 crore. Besides this, the company has undrawn fund-based working capital limits of over ₹1400 crore, which provides an additional liquidity cushion. The company has long-term debt repayments of ₹2,111 crore in FY23, which is expected to be comfortably met from its internal accruals. NEL has a planned capex of around ₹4,382 crore in FY23 (towards the polypropylene project, routine, and maintenance capex), which is proposed to be met through a mix of debt (₹2,519 crore) and internal accruals.

Analytical Approach: Standalone**Applicable criteria**

[Policy on default recognition](#)

[Financial Ratios – Non financial Sector](#)

[Liquidity Analysis of Non-financial sector entities](#)

[Rating Outlook and Credit Watch](#)

[Short Term Instruments](#)

[Manufacturing Companies](#)

[Policy on Withdrawal of Ratings](#)

About the company

Incorporated in 1989, Nayara (formerly known as Essar Oil Limited) is an oil and gas company engaged in refining and marketing. It owns India's second-largest single location refinery – at Vadinar, Gujarat – having a capacity of 20 MMTPA (equivalent to 140 million barrels) and high complexity of 11.8, which allows it to process any kind of crude. The company also has a presence in oil retailing, with over 6,000 operational retail outlets in various parts of India and has plans to expand it further.

| Brief standalone financials (₹ crore) | FY21 (A) | FY22 (A) | H1FY23 (UA) |
|---------------------------------------|----------|----------|-------------|
| Total operating income | 63,566 | 94,048 | 75,835 |
| PBILDT | 3,506 | 4,919 | 9,870 |
| PAT | 467 | 1,030 | 5,357 |
| Overall gearing (times) | 1.88 | 1.87 | 1.30 |
| Interest coverage (times) | 1.68 | 2.76 | 10.34 |

A: Audited; UA: Unaudited; Financials are reclassified as per CARE Ratings' standards.

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for the last three years: Please refer Annexure-2

Covenants of the rated instruments/facilities: Detailed explanation of the covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of the various instruments rated for this company: Annexure-4

Annexure-1: Details of instruments/facilities

| Name of the Instrument | ISIN | Date of Issuance | Coupon Rate (%) | Maturity Date | Size of the Issue (₹ crore) | Rating Assigned along with Rating Outlook |
|--|--------------|-------------------|-----------------|-------------------|-----------------------------|---|
| Debentures-Nonconvertible debentures | INE011A07107 | December 16, 2020 | 8% | December 15, 2025 | 256.84 | CARE AA-; Stable |
| Debentures-Nonconvertible debentures | INE011A07115 | August 13, 2021 | 8.75% | August 13, 2024 | 2285.00 | CARE AA-; Stable |
| Fund-based - LT-Cash Credit | - | - | - | - | 2000.00 | CARE AA-; Stable |
| Fund-based - ST-Bill Discounting/ Bills Purchasing | - | - | - | - | 855.00 | CARE A1+ |
| Non-fund-based - LT-Bank Guarantee | - | - | - | - | 4947.03 | CARE AA-; Stable |
| Non-fund-based - ST-BG/LC | - | - | - | - | 14000.00 | CARE A1+ |
| Term Loan-Long Term | - | - | - | March 31, 2039 | 5182.73 | CARE AA-; Stable |
| Term Loan-Long Term | - | - | - | March 31, 2036 | 4016.00 | CARE AA-; Stable |

Annexure-2: Rating history for the last three years

| Sr. No. | Name of the Instrument/Bank Facilities | Current Ratings | | | Rating History | | | |
|---------|--|-----------------|------------------------------|----------|---|--|--|---|
| | | Type | Amount Outstanding (₹ crore) | Rating | Date(s) and Rating(s) assigned in 2022-2023 | Date(s) and Rating(s) assigned in 2021-2022 | Date(s) and Rating(s) assigned in 2020-2021 | Date(s) and Rating(s) assigned in 2019-2020 |
| 1. | Non-fund-based - ST-BG/LC | ST | 14000.00 | CARE A1+ | - | 1)CARE A1+ (17-Mar-22) 2)CARE A1+ (05-Mar-22) 3)CARE A1+ (30-Jul-21) | 1)CARE A1+ (23-Mar-21) 2)CARE A1+ (11-Aug-20) 3)CARE A1+ (02-Apr-20) | - |

| | | | | | | | | |
|----|--|----|---------|------------------|---|--|---|---|
| 2. | Fund-based - LT-Cash Credit | LT | 2000.00 | CARE AA-; Stable | - | 1)CARE AA-(CWD) (17-Mar-22) | 1)CARE AA; Stable (23-Mar-21) | - |
| | | | | | | 2)CARE AA (CWN) (05-Mar-22) | 2)CARE AA; Stable (11-Aug-20) | |
| | | | | | | 3)CARE AA; Stable (30-Jul-21) | 3)CARE AA; Stable (02-Apr-20) | |
| 3. | Term Loan-Long Term | LT | 5182.73 | CARE AA-; Stable | - | 1)CARE AA-(CWD) (17-Mar-22) 2)CARE AA (CWN) (05-Mar-22) 3)CARE AA; Stable (17-Sep-21) 4)CARE AA; Stable (30-Jul-21) | 1)CARE AA; Stable (23-Mar-21) 2)CARE AA; Stable (11-Aug-20) 3)CARE AA; Stable (02-Apr-20) | - |
| 4. | Term Loan-Long Term | LT | 4016.00 | CARE AA-; Stable | - | 1)CARE AA-(CWD) (17-Mar-22) 2)CARE AA (CWN) (05-Mar-22) 3)CARE AA; Stable (30-Jul-21) | 1)CARE AA; Stable (23-Mar-21) 2)CARE AA; Stable (11-Aug-20) 3)CARE AA; Stable (02-Apr-20) | - |
| 5. | Fund-based - ST-Bill Discounting/ Bills Purchasing | ST | 855.00 | CARE A1+ | - | 1)CARE A1+ (17-Mar-22) 2)CARE A1+ (05-Mar-22) 3)CARE A1+ (30-Jul-21) | 1)CARE A1+ (23-Mar-21) 2)CARE A1+ (11-Aug-20) 3)CARE A1+ (02-Apr-20) | - |

| | | | | | | | | |
|----|--------------------------------------|----|---------|------------------|---|---|--|---|
| 6. | Debentures-Nonconvertible debentures | LT | - | - | - | 1)Withdrawn (05-Mar-22) | 1)CARE AA; Stable (23-Mar-21) 2)CARE AA; Stable (02-Apr-20) | - |
| 7. | Debentures-Nonconvertible debentures | LT | 256.84 | CARE AA-; Stable | - | 1)CARE AA-(CWD) (17-Mar-22) 2)CARE AA (CWN) (05-Mar-22) | 1)CARE AA; Stable (23-Mar-21) 2)Provisional CARE AA; Stable (11-Aug-20) | - |
| 8. | Debentures-Nonconvertible debentures | LT | 2285.00 | CARE AA-; Stable | - | 1)CARE AA-(CWD) (17-Mar-22) 2)CARE AA (CWN) (05-Mar-22) 3)CARE AA; Stable (30-Jul-21) | - | - |
| 9. | Non-fund-based - LT-Bank Guarantee | LT | 4947.03 | CARE AA-; Stable | - | 1)CARE AA-(CWD) (17-Mar-22) 2)CARE AA (CWN) (05-Mar-22) | - | - |

*Long term/Short term.

Annexure-3: Detailed explanation of the covenants of the rated instruments/facilities

Not applicable

Annexure-4: Complexity level of the various instruments rated for this company

| Sr. No. | Name of Instrument | Complexity Level |
|---------|--|------------------|
| 1. | Debentures-Non-convertible debentures | Simple |
| 2. | Fund-based - LT-Cash Credit | Simple |
| 3. | Fund-based - ST-Bill Discounting/ Bills Purchasing | Simple |
| 4. | Non-fund-based - LT-Bank Guarantee | Simple |
| 5. | Non-fund-based - ST-BG/LC | Simple |
| 6. | Term Loan-Long Term | Simple |

Annexure-5: Bank lender details for this company

To view the lender-wise details of the bank facilities, please [click here](#).

Note on the complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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About us:

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