OCTOBER 14, 2016

CARE REVISES THE RATINGS ASSIGNED TO THE BANK FACILITIES AND NCD ISSUE OF GUJARAT STATE PETROLEUM CORPORATION LIMITED WHILE CONTINUING TO PLACE THEM UNDER 'CREDIT WATCH'

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Remarks
Long-term Bank Facilities	15,717.04	**CARE A+ [Single A Plus] (Credit watch)**	**Revised from CARE AA [Double A] (Credit watch)**
Short-term Bank Facilities	6,000.00	**CARE A1 [A One] (Credit watch)**	**Revised from CARE A1+ [A One Plus] (Credit watch)**
Total Facilities	**21,717.04 (Rs. Twenty one thousand seven hundred seventeen crore and four lakh only)**	-	-
Instruments			
Non-Convertible Debentures	4,000.00	**CARE A+ [Single A Plus] (Credit watch)**	**Revised from CARE AA [Double A] (Credit watch)**
Subordinated Non-Convertible Debentures*	1,000.00	**CARE A [Single A] (Credit watch)**	**Revised from CARE AA- [Double A Minus] (Credit watch)**
Subordinated Non-Convertible Debentures$	1,000.00	**CARE A [Single A] (Credit watch)**	**Revised from CARE AA- [Double A Minus] (Credit watch)**
Total Instruments	**6,000.00 (Rs. Six thousand crore only)**		

* These debentures have tenure of sixty years with a call option after 10 years from the issue date and every year thereafter without put option. There is a provision for step up of 200 bps in the coupon after 10 years. The coupon (payable semi-annually) has an optional deferral clause which is linked to non-payment of dividend on the equity shares of the company with a look back period of six months. There is a dividend stopper clause that restricts dividend payment on equity shares in case the coupon payment on the debentures being rated is deferred. There is a replacement capital covenant (RCC) which ensures that the instrument can be redeemed by issuance of similar or higher equity-content instrument(s). The RCC will apply for 30 years and will cease to be applicable if, among other covenants, the rating on the subordinated debentures is upgraded. Considering the terms of the issue, CARE has accorded 50 per cent equity content to this instrument.

$ These debentures have tenure of sixty years with a call option after 12 years from the issue date and every year thereafter without put option. There is a provision for step up of 200 bps in the coupon after 12 years. The coupon (payable semi-annually) has an optional deferral clause which is linked to non-payment of dividend on the equity shares of the company with a look back period of six months. There is a dividend stopper clause that restricts dividend payment on equity shares in case the coupon payment on the debentures being rated is deferred. There is a replacement capital covenant (RCC) which ensures that the instrument can be redeemed by issuance of similar or higher equity-content instrument(s). The RCC will apply for 30 years and will cease to be applicable if, among other covenants, the rating on the subordinated debentures is upgraded. Considering the terms of the issue, CARE has accorded 50 per cent equity content to this instrument.

[1] *Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*

Rating Rationale

The revision in the ratings of the bank facilities/instruments of Gujarat State Petroleum Corporation Ltd. (GSPC) is on account of inordinate and continuous delay in commencement of commercial production of gas from its Deen Dayal West (DDW) block in KG basin even after announcing trial production nearly two years back; which has resulted in lower than previously envisaged production and sale of gas, increase in size of capital expenditure and adverse impact on its debt coverage indicators especially in the backdrop of scheduled debt repayment falling due in the medium term. The revision in ratings is also due to moderation in profitability of its gas trading business and significant write-off which has resulted in GSPC incurring a net loss in FY16 (refers to the period April 1 to March 31) and deterioration in its capital structure.

The ratings, however, continue to draw strength from Govt. of Gujarat (GoG[1]) holding controlling stake in the company and extending need-based support to it, GSPC group's long and established track record with presence across the energy value chain - Exploration & Production (E&P), gas trading, gas transmission, city gas distribution and power generation. The ratings also take in to account GSPC's strong position in natural gas trading business, relatively favourable pricing of gas notified for its DDW block and the company management's plans to increase production of gas from the afore-said block on a sustainable basis by employing a new drilling technology and thereby announce commercial operations date (COD) by February 2017.

The ratings, however, continue to remain constrained on account of inherent risks involved in the E&P business which is accentuated by the fact that a large part of GSPC's capex has been debt-funded, inherent price fluctuation risk related to its gas trading business and exchange rate fluctuation risk related to the unhedged foreign currency loans.

Further delay in commencement of commercial production from its allotted blocks (mainly in DDW block) than envisaged as per revised timelines, adverse deviation from the envisaged production level of gas, absence of meaningful improvement in its profitability & capital structure, timely need-based financial support from GoG and any material development w.r.to stake sale (full/part) in its DDW Block would be the key rating sensitivities.

The ratings continue to remain on 'Credit Watch' in view of the impending possible impact of the envisaged scheme of business restructuring of GSPC on its credit profile. CARE is in the process of evaluating the impact of the same on the credit quality of GSPC. As such, CARE would await further developments to unfold, to enable it to assess the situation. CARE would arrive at the credit quality upon emergence of clarity about effect of business restructuring on the financial risk profile of GSPC.

Background

Incorporated in 1979 as Gujarat State Petrochemicals Corporation Ltd., the company's name was changed to its present form, Gujarat State Petroleum Corporation Ltd. (GSPC) in 1994, with a thrust to expand in energy sector. GSPC is a state-owned entity with Government of Gujarat (GoG) holding 86.89% equity stake as on March 31, 2016.
GSPC is engaged in gas trading as well as oil and gas exploration and production business. GSPC's gas trading business is presently concentrated in Gujarat, which is the largest gas-consuming state in the country. GSPC has working interest in 23 domestic blocks out of which 16 blocks are producing and balance 7 blocks are under exploration / development stage. Out of 7 blocks under exploration / development, GSPC has made substantial investment in KG block. GSPC won KG-OSN-2001/3 offshore block under NELP-III and signed a production sharing contract with Government of India (GoI) in February 2003 and it is appointed as operator with 80% Participating interest (PI) while Jubilant Offshore Drilling Pvt. Ltd. (Jubilant) and Geo Global Resources (India) Inc. (GGR) with PI of 10% each. The block spread over 1850 square kilometers in the hydrocarbon-rich KG basin off the east coast of Andhra Pradesh. In 2005, GSPC announced a significant natural gas discovery in the KG block and the entire block was named as Deen Dayal (DD) Block. The DD Block is a high temperature high pressure (HTHP) tight and deep gas field involving several separate fault blocks including Deen Dayal West (DDW), Deen Dayal North(DDN), Deen Dayal East(DDE), DDW-Downthrown and DDNE-BRU. In the first phase, GSPC is developing DDW area of the DD block. The Field Development Plan (FDP) for DDW area was submitted to the DGH in June 2009 and was approved by the management committee in November 2009. Estimated reserves in DDW block is at around 1.6 trillion cubic feet (TCF) and trial production has commenced from October 2014.

During FY16 (refers to the period from April 1 to March 31), GSPC reported a total operating income of Rs. 10,724 crore (FY15: Rs. 11,035 crore) and reported a net loss of Rs.804 crore (FY15: PAT of Rs.24 crore). As per provisional results for Q1FY17, GSPC has reported a total operating income of Rs.2120 crore with a PAT of Rs.198 crore.

[1] *Debt of entities carrying a guarantee from Govt. of Gujarat has outstanding credit rating of CARE A+ (SO)*

Scheme of business restructuring in GSPC

The Board of Directors of GSPC at their meeting held on December 04, 2015 had approved a scheme of business restructuring in the company which shall be submitted for approval of the Honourable High Court of Gujarat upon receipt of necessary approvals (especially its lenders). As per the scheme, GSPC has proposed to demerge its 80% participating interest in KG-OSN/2001/3 Block together with related assets and liabilities from GSPC to GSPC Offshore Ltd. whereas all remaining businesses (i.e. E & P blocks other than KG Block, Gas trading business, Investment in subsidiaries and associates) shall be transferred to GSPC Energy Ltd. Accordingly, upon transfer of its entire businesses to above-said two new companies, GSPC shall be dissolved automatically. Subsequently, GSPC Energy Ltd. is proposed to be renamed as Gujarat State Petroleum Corporation Ltd or GSPC Ltd. Post restructuring, GSPC Energy Ltd. is proposed to be a holding company of GSPC Offshore Ltd. Government of Gujarat shall continue to control entire business of GSPC directly or indirectly. GSPC is currently awaiting the consent of its lenders before filing a demerger scheme with H'ble High Court.

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CIN - L67190MH1993PLC071691