Press Release
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Refiners stare at Rs 25,000 crore inventory loss

Compounding woe, demand destruction to plunge GRMs in the first quarter

For oil refiners, the Covid-19 pandemic is delivering two blows: inventory loss of over Rs 25,000 crore in the January-March quarter because of a 70% fall in crude oil prices, and a likely plunge in gross refining margins (GRMs) in the first quarter (April-June) of fiscal 2021 because of demand destruction.

Crude prices nosedived from an average[1] $55 per barrel in February to $33 in March and closed at around $20 end of March as demand slumped because of the pandemic. On April 12, 2020, OPEC+[2] managed to strike a deal for a record production cut of 9.7 million barrel per day. Yet crude prices have hovered low because of the pandemic-induced plunge in demand across the globe.

This has caught refiners on the wrong foot. As things stand, India has a total refining capacity of ~250 million metric tonne per annum and refiners keep an inventory of 20-50 days of crude on average to avoid disruption in operations.

The rapid fall in crude oil prices would mean inventory loss of $10-20 per barrel. The final figure of inventory loss will be estimated based on the price prevailing on March 31, 2020. The loss would be offset once crude oil prices rebound, but the process would take time given that the slump in global demand is expected to prolong.

Says Sachin Gupta, Senior Director, CRISIL Ratings, "Inventory losses would be more for refineries located away from the coast because they have to stock crude oil for longer periods. That means refiners will have to borrow more working capital to fund the crude oil purchased earlier."

In addition to these inventory losses, the operating performance of refiners is expected to remain weak in the first quarter of fiscal 2021 due to lower volumes and lower GRMs.

With demand culled further because of the extension of nationwide lockdown up to May 3, 2020, refineries are staring at a halving of utilisation during the April-June quarter. Refineries that replenished their products inventory are staring at significant curtailment of operations. Our base-case assumes the lockdown lasting for up to 1.5 months, with another 1 to 1.5 months required to resume and stabilise operations.

Additionally, refining margins on high-yield products such as aviation turbine fuel (ATF), motor spirit (MS) and high-speed diesel (HSD) have plummeted and are expected to remain weak over the near term. That will affect the operating metrics of refiners.

However, oil marketing companies would fare better than standalone refiners because of higher marketing margins for some products. For example, retail prices of petrol haven't fallen in tandem with crude oil prices, which implies higher marketing margins.

Says Nitesh Jain, Director, CRISIL Ratings, "Lower throughput and lower margins resulting from suppressed demand outlook will hurt the credit metrics of oil refiners. Though strong government/parent support will lend a shoulder, and continue to support the overall credit profiles of refiners."

Revival in demand and improvement in GRMs will be key monitorables in the road ahead.

[1] Average of daily prices of respective month for the Indian Basket of crude oil; source www.ppac.gov.in
[2] OPEC+ is a group of 24 oil-producing nations, made up of the 14 members of Organisation of the Petroleum Exporting Countries members (OPEC), and 10 other non-OPEC members, including Russia.

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