

## HINDUSTAN PETROLEUM CORP

OIL & GAS

6 JUN 2017

Quarterly Update

**BUY**

Target Price: Rs 670

### Refining margin boosts PAT

HPCL's Q4FY17 PAT at Rs 18 bn was significantly higher than our/street estimate of Rs 10 bn led by strong GRM at USD 8/bl (vs. USD 5.5/bl expected). Despite declining by 4.4% QoQ in Q4FY17, marketing volume rose 3% in FY17. Marketing margin at Rs 4,600/tn rose 13% in FY17—higher than IOC's Rs 4,400/tn (incl inventory gain).

**Outlook strong:** Daily revision in fuel prices will stabilize earnings of marketing business, as inventory gain/loss will become zero. Also, government is aiming to address Kerosene under-recoveries through cut in state quotas and monthly price hikes. After this, OMCs would function in a fully deregulated market (growing at 6% p.a.), wherein they can expand their margins/earnings. Remain positive on GRM and marketing

CMP : Rs 568  
Potential Upside : 18%

#### MARKET DATA

No. of Shares : 1,016 mn  
Free Float : 49%  
Market Cap : Rs 576 bn  
52-week High / Low : Rs 584 / Rs 275  
Avg. Daily vol. (6mth) : 3.6 mn shares  
Bloomberg Code : HPCL IB Equity  
Promoters Holding : 51%  
FII / DII : 17% / 10%

### Remain positive on GRM and marketing margin

- ♦ **Refining margin:** Likely to remain firm over CY17-18, as global demand growth at ~1.4 mbpd in CY17/18 each (as per EIA) will surpass incremental refining capacity addition of ~0.7mbpd
- ♦ **Marketing margin:** OMCs have demonstrated their pricing power by successfully tweaking retail fuel prices to pass on the impact of volatile crude/foreign exchange. In the long run, auto fuel margin should approach margin realized by other deregulated industrial fuels (~3x that of auto fuels). OMCs' volume and marketing margin will grow at 3-5% each even after assuming that private players take away 8-10% market share

### Quarterly highlights

- ♦ Refining throughput at 4.6mntn was flat QoQ; whereas GRM at USD 8/bl benefited from inventory gains
- ♦ Pipeline throughput rose 4% QoQ, whereas marketing volume declined 4.4% QoQ

#### Financial summary (Standalone)

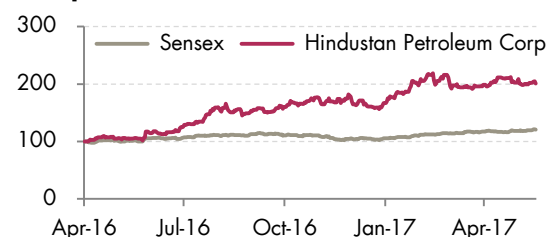
Y/E March	FY16	FY17	FY18E	FY19E
Sales (Rs bn)	1,777.0	1,870.2	1,822.3	1,870.1
Adj PAT (Rs bn)	37.3	62.1	57.5	60.5
Con. EPS* (Rs.)	-	-	54.8	55.9
EPS (Rs.)	36.6	61.0	56.6	59.5
Change YOY (%)	36.3	66.6	(7.3)	5.1
P/E (x)	15.5	9.3	10.0	9.5
RoE (%)	21.9	32.4	26.0	23.4
RoCE (%)	12.5	16.9	14.4	14.2
EV/EBITDA (x)	9.4	7.0	7.7	7.4
DPS	11.5	19.2	17.8	18.7

Source: \*Consensus broker estimates, Company, Axis Capital

#### Key drivers

	FY17	FY18E	FY19E
Throughput (mntn)	17.8	17.8	17.8
GRMs (USD/bl)	6.2	5.5	5.5
Mktg volume (mntn)	35.2	36.3	37.4
Mktgmgn (Rs/te)	4,592	4,824	5,072

#### Price performance



## Exhibit 1: Quarterly highlights

	Q4FY16	Q1FY17	Q2FY17	Q3FY18	Q4FY17
<b>Profit &amp; Losses</b>					
Total Income	421,952	448,408	421,025	485,556	515,248
Raw material costs	346,073	380,827	378,405	424,074	450,847
Gross profit	75,879	67,580	42,621	61,482	64,401
Employee Expenses	4,607	6,145	6,051	6,104	11,161
Other Expenses	44,659	25,167	23,961	27,345	24,380
Operating expenses	49,266	31,312	30,012	33,449	35,541
EBITDA	26,613	36,268	12,609	28,033	28,860
Depreciation	6,754	6,108	6,160	6,336	6,749
EBIT	19,860	30,160	6,450	21,698	22,111
Other Income	4,079	2,753	5,469	2,878	4,047
Interest	1,913	1,395	1,164	530	2,268
PBT	22,025	31,518	10,755	24,046	23,890
Total tax	6,495	10,534	3,741	8,143	5,702
PAT	15,529	20,984	7,013	15,903	18,188
<b>Segmental Analysis</b>					
<b>Refining segment</b>					
Crude throughput (mnte)	4.7	4.5	4.0	4.7	4.6
GRM, reported (US\$ /bl)	7.5	6.8	3.2	6.4	8.0
<b>Pipeline segment</b>					
Pipeline EBITDA (Rs mn)	2,203	2,427	2,151	2,333	2,438
Pipeline throughput (mnte)	4.2	4.7	4.1	4.5	4.7
<b>Marketing segment</b>					
Petroleum product sale (mnte)	9.05	8.92	8.18	9.27	8.86
Marketing margins (incl IG) - Rs/tn	6,144	5,544	4,089	4,719	4,855
Marketing margins (clean) - Rs/tn	7,249	4,311	4,089	4,719	4,855

Source: Company, Axis Capital

## Exhibit 2: SoTP

	Valuation base		Multiple (x)		Enterprise Value	
	Matrix	Value	Multiple	Value (x)	(Rs bn)	(Rs/sh)
<b>Business segments</b>						
Refining business	EBITDA (Rs mn)	35,487	EV/EBITDA	5.0	177	174
Marketing business	EBITDA (Rs mn)	50,499	EV/EBITDA	7.0	353	348
Pipeline business	EBITDA (Rs mn)	13,822	EV/EBITDA	7.0	97	95
<b>Total (a)</b>					<b>628</b>	<b>617</b>
<b>Investments</b>						
Oil India	NoSH (mn)	18	CMP	311	6	5
MRPL	NoSH (mn)	297	CMP	134	40	39
Bhatinda Refinery	EBITDA (Rs mn)	33,162	EV/EBITDA	5.0	166	163
Other investments	Investment (Rs mn)	8,369	P/BV	0.75	6	6
<b>Total (b)</b>					<b>218</b>	<b>214</b>
<b>Total Enterprise Value (a+b)</b>					<b>845</b>	<b>831</b>
Less: Net debt					162	159
<b>Total Equity Value</b>					<b>684</b>	<b>672</b>

Source: Company, Axis Capital

## Financial summary (Standalone)

### Profit & loss (Rs bn)

Y/E March	FY16	FY17	FY18E	FY19E
Net sales	1,777.0	1,870.2	1,822.3	1,870.1
Other operating income	-	-	-	-
<b>Total operating income</b>	<b>1,777.0</b>	<b>1,870.2</b>	<b>1,822.3</b>	<b>1,870.1</b>
Cost of goods sold	(1,568.5)	(1,634.2)	(1,585.4)	(1,617.1)
Gross profit	208.5	236.1	236.9	253.0
<i>Gross margin (%)</i>	<i>11.7</i>	<i>12.6</i>	<i>13.0</i>	<i>13.5</i>
Total operating expenses	(129.1)	(130.3)	(140.6)	(153.2)
<b>EBITDA</b>	<b>79.4</b>	<b>105.8</b>	<b>96.2</b>	<b>99.8</b>
<i>EBITDA margin (%)</i>	<i>4.5</i>	<i>5.7</i>	<i>5.3</i>	<i>5.3</i>
Depreciation	(26.5)	(25.4)	(25.9)	(26.8)
<b>EBIT</b>	<b>52.9</b>	<b>80.4</b>	<b>70.4</b>	<b>73.1</b>
Net interest	(6.5)	(5.4)	(4.4)	(3.8)
Other income	11.4	15.1	17.4	18.4
<b>Profit before tax</b>	<b>57.8</b>	<b>90.2</b>	<b>83.4</b>	<b>87.7</b>
Total taxation	(20.5)	(28.1)	(25.9)	(27.2)
<i>Tax rate (%)</i>	<i>35.5</i>	<i>31.2</i>	<i>31.0</i>	<i>31.0</i>
Profit after tax	37.3	62.1	57.5	60.5
Minorities	-	-	-	-
Profit/ Loss associate co(s)	-	-	-	-
Adjusted net profit	37.3	62.1	57.5	60.5
<i>Adj. PAT margin (%)</i>	<i>2.1</i>	<i>3.3</i>	<i>3.2</i>	<i>3.2</i>
Net non-recurring items	-	-	-	-
Reported net profit	37.3	62.1	57.5	60.5

### Balance sheet (Rs bn)

Y/E March	FY16	FY17	FY18E	FY19E
Paid-up capital	3.4	10.2	10.2	10.2
Reserves & surplus	176.3	193.3	229.1	266.8
Net worth	179.7	203.5	239.3	276.9
Borrowing	219.5	219.3	216.3	215.9
Other non-current liabilities	143.3	169.0	169.0	169.0
<b>Total liabilities</b>	<b>695.6</b>	<b>784.4</b>	<b>812.3</b>	<b>852.8</b>
Gross fixed assets	558.5	617.7	594.5	614.0
Less: Depreciation	(217.7)	(243.0)	(268.9)	(295.6)
Net fixed assets	340.9	374.7	325.7	318.4
Add: Capital WIP	18.5	18.1	102.5	148.0
Total fixed assets	359.4	392.8	428.2	466.4
Total Investment	105.8	109.2	109.2	109.2
Inventory	132.1	185.8	181.0	185.7
Debtors	37.6	40.6	39.6	40.6
Cash & bank	0.2	0.3	3.7	5.1
Loans & advances	54.9	49.4	44.4	39.4
Current liabilities	153.2	192.9	187.9	191.1
Net current assets	77.3	89.7	87.2	86.2
Other non-current assets	-	-	-	-
<b>Total assets</b>	<b>695.6</b>	<b>784.4</b>	<b>812.3</b>	<b>852.8</b>

Source: Company, Axis Capital

### Cash flow (Rs bn)

Y/E March	FY16	FY17	FY18E	FY19E
Profit before tax	57.8	90.2	83.4	87.7
Depreciation & Amortisation	26.5	25.4	25.9	26.8
<i>Chg in working capital</i>	<i>(28.7)</i>	<i>(12.3)</i>	<i>5.8</i>	<i>2.4</i>
<b>Cash flow from operations</b>	<b>23.7</b>	<b>60.0</b>	<b>71.8</b>	<b>71.3</b>
<i>Capital expenditure</i>	<i>(59.4)</i>	<i>(58.8)</i>	<i>(61.2)</i>	<i>(65.0)</i>
<b>Cash flow from investing</b>	<b>(52.8)</b>	<b>(62.2)</b>	<b>(61.2)</b>	<b>(65.0)</b>
<i>Equity raised/ (repaid)</i>	<i>-</i>	<i>6.8</i>	<i>-</i>	<i>-</i>
<i>Debt raised/ (repaid)</i>	<i>16.2</i>	<i>(0.3)</i>	<i>(2.9)</i>	<i>(0.4)</i>
<i>Dividend paid</i>	<i>(14.1)</i>	<i>(23.5)</i>	<i>(21.7)</i>	<i>(22.9)</i>
<b>Cash flow from financing</b>	<b>13.3</b>	<b>(1.0)</b>	<b>(24.7)</b>	<b>(23.2)</b>
Net chg in cash	(15.8)	(3.2)	(14.1)	(16.9)

### Key ratios

Y/E March	FY16	FY17	FY18E	FY19E
<b>OPERATIONAL</b>				
FDEPS (Rs)	36.6	61.0	56.6	59.5
CEPS (Rs)	62.7	86.0	82.0	85.8
DPS (Rs)	11.5	19.2	17.8	18.7
Dividend payout ratio (%)	31.4	31.4	31.4	31.4
<b>GROWTH</b>				
Net sales (%)	(14.0)	5.2	(2.6)	2.6
EBITDA (%)	40.1	33.2	(9.0)	3.7
Adj net profit (%)	36.3	66.6	(7.3)	5.1
FDEPS (%)	36.3	66.6	(7.3)	5.1
<b>PERFORMANCE</b>				
RoE (%)	21.9	32.4	26.0	23.4
RoCE (%)	12.5	16.9	14.4	14.2
<b>EFFICIENCY</b>				
Asset turnover (x)	5.4	5.2	4.7	4.5
Sales/ total assets (x)	2.6	2.5	2.3	2.2
Working capital/ sales (x)	-	-	-	-
Receivable days	7.7	7.9	7.9	7.9
Inventory days	28.4	38.4	38.3	38.3
Payable days	20.2	26.2	26.0	25.8
<b>FINANCIAL STABILITY</b>				
Total debt/ equity (x)	1.3	1.1	1.0	0.8
Net debt/ equity (x)	1.0	0.9	0.7	0.6
Current ratio (x)	1.5	1.5	1.5	1.5
Interest cover (x)	8.1	15.0	16.1	19.4
<b>VALUATION</b>				
PE (x)	15.5	9.3	10.0	9.5
EV/ EBITDA (x)	9.4	7.0	7.7	7.4
EV/ Net sales (x)	0.4	0.4	0.4	0.4
PB (x)	3.2	2.8	2.4	2.1
Dividend yield (%)	2.0	3.4	3.1	3.3
Free cash flow yield (%)	(5.0)	(0.4)	1.8	1.1

Source: Company, Axis Capital

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