

Hindustan Petroleum Corporation Ltd.



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Marketing margins & improved GRM drive performance

CMP INR 303	Target INR 343	Potential Upside 13.2%	Market Cap (INR Mn) 461,109	Recommendation ACCUMULATE	Sector Oil & Gas
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Result highlights

Revenues came in at INR 679.3 bn, up 11.7% YoY and declining QoQ by 5.8% with crude throughput of 4.6 MMT (4.56 MMT in Q3FY19, 4.63 MMT in Q4FY19). Gross margins improved considerably to 13.7% (+211 bps YoY, +838bps QoQ) on the back of inventory gains of INR 34.1 bn as against losses of INR 50.3 bn in Q3FY19. GRM for the quarter came at 4.51/bbl v/s \$7.07/bbl in Q4FY18 due to higher crude prices and weak product cracks. Employee expenses declined to some extent both on a YoY (-6.5%) and QoQ (-6.6%) basis, while other expenses increased by 62.7% QoQ (+2% YoY), although it was negated to some extent by forex gains of INR 2.48 bn as v/s forex losses of INR 840 mn in Q4FY18 due to rupee appreciation leading to EBITDA at INR 51.6 bn (+76.8% YoY). OPM stood at 7.6% (+280 bps YoY, +627 bps QoQ). Finance cost increased by 27.2% QoQ (+5.4% YoY) which was negated by higher other income at INR 5.23 bn (+52.5% YoY, +32.7% QoQ) leading to PAT at INR 29.7 bn with NPM of 4.4% (+150 bps YoY, +403 bps QoQ). The board has declared a final dividend of INR 9.40/share on a FV of INR 10.

MARKET DATA

Shares outs (Mn)	1,523
Equity Cap (INR Mn)	15,238
Mkt Cap (INR Mn)	461,109
52 Wk H/L (INR)	325/163
Volume Avg (3mK)	7,827
Face Value (INR)	10
Bloomberg Code	HPCL IN

KEY FINANCIALS

Particulars (INR mn)	FY17	FY18	FY19	FY20E	FY21E
Revenue from Operations	18,74,263	21,95,096	27,54,734	28,72,822	30,92,017
EBITDA	1,08,130	1,07,130	1,15,671	1,17,747	1,29,833
PAT	82,358	72,183	66,906	71,556	79,292
EPS Diluted (INR)	54.05	47.37	43.91	46.96	52.03
OPM	5.8%	4.9%	4.2%	4.1%	4.2%
NPM	4.4%	3.3%	2.4%	2.5%	2.6%
P/E (x)	5.6	6.4	6.9	6.4	5.8

Source: Company, KRChoksey Research

Highlights

Higher GRM from inventory gains; higher throughput YoY

Reported GRM stood at \$4.51/bbl from inventory gains of INR 34.1 bn (v/s inventory losses of INR 50.3 bn in Q3FY19) due to weak light product spreads and slower demand. Excluding inventory impact, core GRM came in at \$2.1/bbl as against \$6.6/bbl in Q4FY18. Crude throughput remained flat (-0.6% YoY, +0.9% QoQ) to 4.6 MMT. On a yearly basis, both refineries together registered a record throughput of 18.44 MMT (+0.8%). With IMO regulations from Apr'20, we expect an increase in the middle distillates products (diesel) especially from the Vizag refinery to cater to demand post IMO 2020 norms giving thrust to the GRMs. In addition, recovery in the gasoline cracks along with upgradation of refineries to comply with BS VI norms may drive GRMs up in the coming quarters. We estimate GRM levels between \$7-8/bbl over FY20-21E, while crude throughput is estimated at 21.8/23 MMT for FY20/21E.

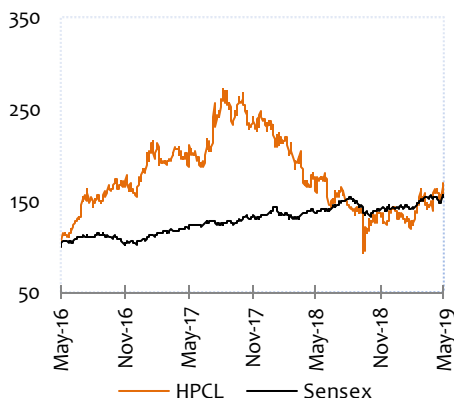
Domestic market sales increase; exports decline

Total market sales registered a strong growth of 10.11 MMT (+6.9% YoY, +3.79% QoQ), however exports declined 73.3% QoQ (+33.3% YoY) to 0.08 MMT which led to decline in revenues (-5.3% QoQ) to some extent. Although marketing margins on auto fuels improved allowing to recoup the earlier inventory losses during Q3, we believe now in the post election period, OMCs will be in a better position to protect marketing margins at normal levels, with HPCL with >70% of marketing operations as the largest beneficiary.

Higher NPM from forex gains and other income; High debt levels a concern

Net income came in strong on the back of forex gains for the quarter at INR 2.4 bn (v/s forex loss of INR 843 mn in Q4FY18). In addition, other income was up 52.2% YoY and 32.7% QoQ to INR 5.22 bn leading to NPM of 4.4% (+150 bps YoY, +403 bps QoQ). However, like other

SHARE PRICE PERFORMANCE

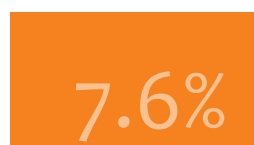


MARKET INFO

SENSEX	39,435
NIFTY	11,884

SHARE HOLDING PATTERN (%)

Particulars	Mar19	Dec18	Sep18
Promoters	0	0	0
FIIIs	18.6	19.15	20.17
DIIIs	17.09	17.64	16.54
Others	64.31	63.22	63.28
Total	100	100	100



Revenue CAGR between FY19 and FY21E



EBITDA CAGR between FY19 and FY21E

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OMCs, finance cost increased by 27.2% QoQ (+5.4% YoY) to INR 1.8 bn from high debt raised. HPCL's debt surged from INR 205.3 bn in FY18 to INR 260.3 bn in FY19, primarily on account of pending govt dues for LPG/kerosene subsidies amounting to INR 80 bn leading to D/E ratio of 0.9x in FY19 from 0.8x in FY18. The management had indicated raising another INR 70-80 bn for FY20 which will further increase finance costs thereby causing a drag on cash flows.

Capex plans in-place

HPCL's capex plans include expansion at Vizag refinery to 15 MMTPA (from 8.3 MMTPA currently) and Mumbai refinery to 9.5 MMTPA (from 7.5 MMTPA currently) with investments of INR 210 bn and INR 50 bn, respectively which are expected to commission in FY21. Guidance for FY20 stands at INR 140 bn (INR 110 bn in FY18) which also includes capex for bottom upgradation of refineries for BS-VI compliance effective from Apr'20 and strengthening its pipeline network. HPCL's other projects also include its greenfield JV project of setting up a 9 MMTPA integrated refinery and petroleum complex at Barmer, Rajasthan which is expected to require an addition total investment of INR 430 bn.

Valuation & Outlook:

Among the three OMCs, we have a positive outlook on HPCL given its earnings growth visibility on the back of its capex plans and improvement marketing margin environment. The stock underperformed in FY19 due to volatile crude prices and uncertainty during the on-going election period keeping marketing margins under pressure. Now with a stable government at the Centre, OMCs stand a chance for higher flexibility allowing them to protect marketing margins in the light of any volatility in crude prices. We have revised our estimates factoring in the same. We expect revenues to grow at a CAGR of 7.6% over FY19-21E and EBITDA to grow at a CAGR of 5.9% over FY19-21E. At a CMP of INR 303, HPCL is trading at 6.0/5.3x of FY20/21E EV/EBITDA. We maintain our EV/EBITDA-based target price of INR 343. (potential upside – 13.2%). **We maintain BUY rating on the stock.**

QUARTERLY PERFORMANCE (INCOME STATEMENT)

Particulars (INR mn)	Q4FY19	Q3FY19	Q4FY18	Q-o-Q (%)	Y-o-Y (%)
Net Revenue from Operations	6,76,286	7,18,139	6,05,199	-5.8%	11.7%
Other operating income	3,095	2,980	2,898	3.9%	6.8%
Revenue from operations	6,79,381	7,21,118	6,08,098	-5.8%	11.7%
Cost of Materials Consumed	1,57,649	1,83,720	1,48,984	-14.2%	5.8%
Purchases of Stock-in-trade	4,62,742	4,48,577	3,97,957	3.2%	16.3%
(Increase)/Decrease in inventories	-34,177	50,342	-9,399	NM	NM
Cost of Goods Sold	5,86,214	6,82,638	5,37,541	-14.1%	9.1%
Gross Profit	93,168	38,480	70,557	142.1%	32.0%
Gross Margin (%)	13.7%	5.3%	11.6%	838 bps	211 bps
Employee benefit expense	7,310	7,830	7,821	-6.6%	-6.5%
Other expenses	34,195	21,018	33,509	62.7%	2.0%
Total Expenditure	41,505	28,848	41,330	43.9%	0.4%
EBITDA	51,662	9,632	29,226	436.4%	76.8%
EBITDA Margin (%)	7.6%	1.3%	4.8%	627 bps	280 bps
Depreciation	8,285	7,393	7,254	12.1%	14.2%
EBIT	43,378	2,239	21,973	1837.5%	97.4%
Finance Cost	1,872	1,472	1,776	27.2%	5.4%
Other Income	5,225	3,937	3,427	32.7%	52.5%
Profit before Tax (PBT)	46,731	4,704	23,624	893.5%	97.8%
Tax Expense	17,032	2,228	6,145	664.3%	177.2%
Profit after Tax (PAT)	29,699	2,476	17,479	1099.7%	69.9%
Net Profit Margin (%)	4.4%	0.3%	2.9%	403 bps	150 bps
EPS Basic (INR)	19.49	1.62	11.47		

Source: Company, KRChoksey Research

ANALYST

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INCOME STATEMENT

Particulars (INR mn)	FY17	FY18	FY19	FY20E	FY21E
Revenue from Operations	18,74,263	21,95,096	27,54,734	28,72,822	30,92,017
Cost of Goods Sold	16,36,424	19,44,872	24,80,370	25,85,540	27,79,723
Gross Profit	2,37,839	2,50,224	2,74,364	2,87,282	3,12,294
Gross Margin (%)	12.7%	11.4%	10.0%	10.0%	10.1%
Employee benefit expenses	29,694	28,926	29,728	35,042	37,706
Other expenses	1,00,015	1,14,169	1,28,965	1,34,493	1,44,755
Total Operating Expense	1,29,709	1,43,095	1,58,693	1,69,535	1,82,460
EBITDA	1,08,130	1,07,130	1,15,671	1,17,747	1,29,833
EBITDA Margin (%)	5.8%	4.9%	4.2%	4.1%	4.2%
Depreciation	27,764	28,344	30,853	33,767	35,516
EBIT	80,366	78,785	84,818	83,980	94,318
Finance Cost	6,092	6,179	7,856	7,824	8,029
Other Income	14,510	15,279	14,133	13,318	12,858
PBT before share of profits	88,784	87,885	91,095	89,474	99,147
Share of profit of associates & JVs	23,190	13,216	9,297	17,895	19,829
Profit before Tax (PBT)	1,11,974	1,01,101	1,00,392	1,07,369	1,18,976
Total Tax expense	29,616	28,919	33,486	35,813	39,684
Profit after Tax (PAT)	82,358	72,183	66,906	71,556	79,292
PAT Margin (%)	4.4%	3.3%	2.4%	2.5%	2.6%
EPS Basic (INR)	54.05	47.37	43.91	46.96	52.03

Source: Company, KRChoksey Research

BALANCE SHEET

Particulars (INR mn)	FY17	FY18	FY19	FY20E	FY21E
SOURCES OF FUNDS					
Share Capital - Equity	10,163	15,242	15,242	15,242	15,242
Reserves	2,00,551	2,40,082	2,88,765	3,41,171	3,99,244
Total Shareholder's funds	2,10,714	2,55,324	3,04,007	3,56,413	4,14,486
Long term funds	1,81,151	96,564	1,21,283	1,09,155	1,03,698
Short term funds	2,84,588	4,12,925	5,05,767	5,22,334	5,54,201
Total Debt	4,65,738	5,09,490	6,27,050	6,31,489	6,57,898
Other non-current liabilities	63,562	69,185	76,076	76,167	76,335
TOTAL SOURCES OF FUNDS	7,40,014	8,33,998	10,07,133	10,64,069	11,48,719
Net Block	3,87,437	4,27,057	5,11,602	5,36,187	5,71,615
Other non-current assets	85,092	98,251	1,26,330	1,30,768	1,40,634
Total non-current assets	4,72,529	5,25,308	6,37,933	6,66,955	7,12,249
Cash & Cash equivalents	1,364	13,052	2,185	6,627	21,653
Other Current Assets	3,29,297	3,58,358	4,32,466	4,58,744	4,88,282
Total Current Assets	3,30,661	3,71,410	4,34,651	4,65,371	5,09,935
Total Current Liabilities	63,176	62,719	65,451	68,257	73,465
Net Current Assets	2,67,485	3,08,691	3,69,200	3,97,114	4,36,470
TOTAL APPLICATION OF FUNDS	7,40,014	8,33,998	10,07,133	10,64,069	11,48,719

Source: Company, KRChoksey Research

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CASH FLOW STATEMENT

Particulars (INR mn)	FY17	FY18	FY19E	FY20E	FY21E
Profit before Tax (PBT)	1,11,974	1,01,101	1,00,392	1,07,369	1,18,976
Operating profit before working capital changes	1,17,726	1,20,919	1,39,101	1,48,960	1,62,521
Cash Generated from/(used in) operations	1,24,347	1,30,342	1,34,880	1,30,290	1,62,509
Less: Income Tax Paid (net of refunds)	-21,803	-19,970	-33,486	-35,813	-39,684
Net Cash generated from/(used in) operating activities	1,02,544	1,10,372	1,01,395	94,477	1,22,824
Net Cash Used In Investing Activities	-53,039	-73,980	-1,29,553	-53,716	-75,930
Net Cash Used in Financing Activities	-42,387	-44,230	29,250	-36,319	-31,869
Net Increase/(Decrease) in Cash and Cash Equivalents	7,118	-7,837	1,091	4,442	15,026
Cash & Cash Equivalents at the beginning	-23,640	-16,522	1,215	1,987	6,430
Cash and Cash Equivalents at the end	1,115	1,215	1,988	6,430	21,455
Add: Bank Balance	249	11,837	198	198	198
Cash & Bank Balances	1,364	13,052	2,185	6,627	21,653

Source: Company, KRChoksey Research

RATIOS

Particulars	FY17	FY18	FY19	FY20E	FY21E
<u>Profitability</u>					
Return on Assets (%)	10.3%	8.0%	6.2%	6.3%	6.5%
Return on Capital (%)	20.6%	17.1%	15.0%	13.8%	14.2%
Return on Equity (%)	39.1%	28.3%	22.0%	20.1%	19.1%
<u>Margin Trend</u>					
Gross Margin (%)	12.7%	11.4%	10.0%	10.0%	10.1%
EBITDA Margin (%)	5.8%	4.9%	4.2%	4.1%	4.2%
Net Margin (%)	4.4%	3.3%	2.4%	2.5%	2.6%
<u>Liquidity</u>					
Current Ratio	1.0	0.8	0.8	0.8	0.8
Quick Ratio	0.1	0.1	0.1	0.1	0.2
Debtor Days	8	9	9	9	9
Inventory Days	36	31	33	33	33
Creditor Days	25	26	25	25	25
Working Capital Days	20	14	17	17	17
<u>Solvency</u>					
Total Debt / Equity	0.9	0.8	0.9	0.7	0.6
Interest Coverage	13.2	12.8	10.8	10.7	11.7
<u>Valuation Ratios</u>					
EV/EBITDA	5.9	6.1	6.2	6.0	5.3
P/E	5.6	6.4	6.9	6.4	5.8
P/B	2.2	1.8	1.5	1.3	1.1

Source: Company, KRChoksey Research

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Date	CMP (INR)	TP (INR)	Recommendation	Our Rating	Upside
27-May-19	303	343	ACCUMULATE	Buy	More than 15%
11-Feb-19	232	343	BUY		
28-May-18	311	428	BUY	Accumulate	5% – 15%
12-Feb-18	466	650	BUY	Hold	0 – 5%
				Reduce	-5% – 0
				Sell	Less than – 5%

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