

Chennai Petroleum Corporation Ltd.



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Inventory losses wash out profits

CMP INR 242	Target INR 296	Potential Upside 22.3%	Market Cap (INR Mn) 36,141	Recommendation BUY	Sector Oil & Gas
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Result highlights

Chennai Petro reported revenue of INR 98.7 bln (+14.9% YoY, -17.8% QoQ). Crude throughput was down by 21.6% QoQ and 16.9% YoY to 2.279 MMT. Gross Margins declined to -0.7% (-1,392 bps YoY, -727 bps QoQ) impacted significantly due to inventory losses of INR 4.87 bn on account of decrease in crude prices as against inventory gains of 3.91 bn in Q3FY18 and 2.63 bn in Q2FY19. GRM for the quarter stood at -\$0.2/bbl as against \$4.85/bbl in Q2FY19 and \$8.58/bbl in Q3FY18. Fall in the gross margins was only marginally negated from lower operating expenses on a YoY basis (-66 bps YoY), however it increased on a QoQ basis (+59 bps) leading to an EBITDA of -INR 4.2 bn (-154.4% YoY, -197.2% QoQ). OPM fell by 1,326 bps YoY and 786 bps QoQ to -4.3%. Loss for the quarter came in at INR 3.67 bn, down 195.1% YoY and 1,459.5% QoQ further aggravated by lower other income (-86.7% YoY, -50.3% QoQ) and higher finance cost (+7.3% YoY, +3.5% QoQ). However, the quarter witnessed forex gains of INR 750 mn as against -INR 1.88 bn losses in Q2FY19. Loss margin stood at 3.7% (-822 bps YoY, -395 bps QoQ).

MARKET DATA

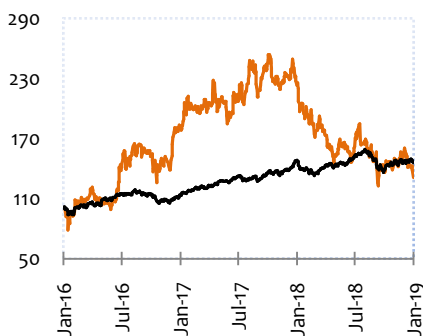
Shares outs (Mn)	148
Equity Cap (INR Mn)	1489
Mkt Cap (INR Mn)	36141
52 Wk H/L (INR)	429/221
Volume Avg (3m K)	543.8
Face Value (INR)	10
Bloomberg Code	MRL IN

KEY FINANCIALS

Particulars (INR Mn)	FY16	FY17	FY18	FY19E	FY20E
Revenue from Operations	2,58,456	2,76,914	3,25,280	4,01,333	4,10,308
EBITDA	13,476	19,376	20,855	9,834	14,545
PAT	7,615	11,198	9,315	2,092	3,748
EPS Diluted (Rs.)	51.14	75.20	62.56	14.05	25.17
OPM (%)	5.21%	7.00%	6.41%	2.45%	3.54%
NPM (%)	2.95%	4.04%	2.86%	0.52%	0.91%
P/E (x)	4.73	3.22	3.87	17.22	9.61

Source: Company, KRChoksey Research

SHARE PRICE PERFORMANCE



— Emmbi Industries Ltd — SENSEX

MARKET INFO

SENSEX	35593
NIFTY	10652

Disappointing operating margins on account of lower GRM

CPCL reported EBITDA at -INR 4.2 bn (-154.4%, -197.2% QoQ). Reported GRM for 9M stood at \$3.92/bbl with GRM for the quarter at -\$0.20/bbl majorly driven by inventory losses which stood at INR 4.87 bn as against gains of INR 3.91 in Q3FY18 and INR 2.63 bn in Q2FY19. Further, crude throughput was down at 2.28 MMT, down 16.9% YoY and 21.6% QoQ likely due to the slower ramp-up of the resid upgradation project. Although crude prices remain volatile, there has been some recovery in the last month as a result of which we can expect to see little recovery in the GRMs Q4FY19 onwards. CPCL is a plain refiner and thus any quick changes in the global prices cannot be ruled out leading to significant inventory losses and thus impacting the profitability.

Near term outlook bleak; performance in long term could improve

The company has proposed setting up a greenfield refinery in Nagapattinam district in Tamil Nadu. The proposed refinery will have a capacity of 9 MMTA and the estimated cost is INR 356.9 bn (earlier estimated at INR 274.6 bn) which would be funded with a mix of debt and equity. The refinery is a part of the govt's plan to help meet the BS-VI regulations across the southern region. Post the implementation of the BS-VI norms, CPCL will be ensured of a strong demand for its products coming from the southern states which could lead to improvement in revenues. However, this turnaround will be visible only post FY23 and thus the near-term prospects depend purely on the crude prices volatility, exchange rates as well as the global demand-supply scenario.

SHARE HOLDING PATTERN (%)

Particulars	Dec 18	Sep 18	Jun 18
Promoters	67.29	67.29	67.29
FIIIs	9.03	8.43	9.03
DIIIs	12.92	12.52	11.59
Others	10.76	11.77	12.1
Total	100	100	100

8.02%

Revenue CAGR between FY 18 and FY 20E

-16.5%

EBITDA between FY 18 and FY 20E

ANALYST

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The global outlook on light distillate cracks have weakened due to slower demand which could further put pressure on the refining margins. We have revised downwards, our GRM estimates (FY19E - \$3.9/bbl, FY20E - \$6/bbl) from the recent change in the crude price volatility potentially leading to inventory losses.

Valuation & Outlook:

The scenario in the refining segment looks weak in the near term on account of weak product cracks which have put pressure on the refining margins. With respect to CPCL, prospects could improve post the set up of its new refinery which will help cater to the demand in the southern region. However, the refinery to be set up will result in a high capex resulting in increased finance cost from higher debt. Also, we have lowered our estimates of GRMs for FY20E and subsequently reduced our EBITDA and EBITDA margin estimates. We expect revenues to grow at a CAGR of 8.02% over FY18-20E while EBITDA to de-grow at 16.5% over FY18-20E owing to pressure on margins. Our estimates of GRMs for FY19/20E stand at \$3.9/bbl and \$6.0/bbl respectively. At a CMP of INR 242, the stock is trading at EV/EBITDA multiple of 7.5x of FY19E EBITDA and 5.5x of FY20E EBITDA, a discount to its past valuations. **We valued the company by assigning a EV/EBITDA multiple of 6x on the FY20E EBITDA and arrive at a target price of INR 296 (potential upside – 22.3%) from our earlier estimate of INR 456 . We maintain our BUY rating on the stock.**

KEY METRICS QUARTERLY PERFORMANCE

Particulars	UoM	Q3FY19	Q2FY19	Q3FY18	QoQ (%)	YoY (%)
Throughput	MMT	2.279	2.906	2.744	-21.6%	-16.9%
GRM	USD/bbl	-0.20	4.85	8.58	-104.1%	-102.3%

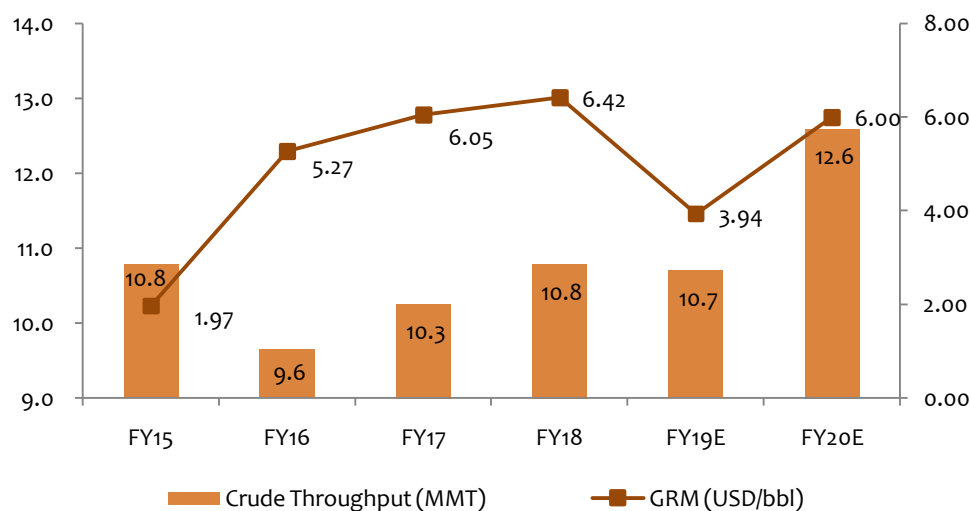
Source: Company, KRChoksey Research

KEY MODEL ASSUMPTIONS for FY19E/FY20E

Particulars		FY15	FY16	FY17	FY18	FY19E	FY20E
Throughput	MMPA	10.782	9.643	10.257	10.789	10.706	13.05
GRM	USD/bbl	1.97	5.27	6.05	6.42	3.94	6.0
Oil Price	USD/bbl	84.4	44.0	56.0	57.8	72.0	73.0
USD/INR		61.0	64.3	66.0	60.7	64.0	66.0

Source: Company, KRChoksey Research

Year-wise crude throughput and GRM



Source: Company, KRChoksey Research

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QUARTERLY PERFORMANCE – INCOME STATEMENT

Particulars (INR mn)	Q3FY19	Q2FY19	Q3FY18	QoQ (%)	YoY (%)
Revenue from operations	98,658	1,20,041	85,852	-17.8%	14.9%
Cost of Materials Consumed	88,565	1,10,684	77,208	-20.0%	14.7%
Purchases of Stock-in-trade	5,920	4,115	1,210	43.9%	389.4%
(Increase)/Decrease in inventories of FG, WIP and SIT	4,872	-2,634	-3,912	-285.0%	-224.6%
Cost of Goods Sold (COGS)	99,357	1,12,165	74,506	-11.4%	33.4%
Gross Profit	-699	7,876	11,346	-108.9%	-106.2%
Gross Profit Margin (%)	-0.7%	6.6%	13.2%	-727 bps	-1392 bps
Employee benefit expense	1,098	1,128	1,234	-2.7%	-11.1%
Other expenses	2,406	2,426	2,384	-0.8%	0.9%
Total Operating Expenditure	3,503	3,554	3,618	-1.4%	-3.2%
EBITDA	-4,202	4,322	7,728	-197.2%	-154.4%
EBITDA Margin (%)	-4.3%	3.6%	9.0%	-786 bps	-1326 bps
Depreciation and Amortization Expense	1,105	1,076	851	2.7%	29.9%
EBIT	-5,308	3,246	6,877	-263.5%	-177.2%
Other Income	99	199	739	-50.3%	-86.7%
Finance Cost	1,091	1,055	1,017	3.5%	7.3%
Foreign Exchange gain/(loss)	750	-1,882	615	-139.8%	21.9%
Profit before exceptional items and tax	-5,550	508	7,215	-1192.6%	-176.9%
Impairment of non-current assets	4	3	7	50.0%	-42.6%
Profit before Tax (PBT)	-5,554	505	7,208	-1199.0%	-177.1%
Tax Expense	-1,882	235	3,346	-900.0%	-156.3%
Profit after Tax (PAT)	-3,672	270	3,862	-1459.5%	-195.1%
Net Profit Margin (%)	-3.7%	0.2%	4.5%	-395 bps	-822 bps
EPS Basic (INR)	-24.64	1.81	25.92	-1459.5%	-195.1%

Source: Company, KRChoksey Research

Particulars (INR mn)	FY16	FY17	FY18	FY19E	FY20E
Revenue from Operations	2,58,453	2,76,915	3,25,273	4,01,333	4,10,308
Total Direct Expenses	2,32,553	2,45,204	2,91,074	3,78,663	3,83,638
Gross Profit	25,900	31,712	34,199	22,670	26,670
Gross Margin (%)	10.0%	11.5%	10.5%	5.6%	6.5%
Employee benefit expenses	3,570	5,129	5,818	4,330	3,856
Other expenses	8,858	7,104	7,834	11,344	8,269
Total Operating Expense	12,428	12,232	13,652	15,674	12,125
EBITDA	13,472	19,479	20,548	6,996	14,545
EBITDA Margin (%)	5.2%	7.0%	6.3%	1.7%	3.5%
Depreciation	2,737	2,786	3,402	4,255	4,662
EBIT	10,735	16,693	17,146	2,741	9,883
Finance Cost	3,517	2,728	3,209	4,090	4,621
Other Income	364	303	688	486	410
Profit before Tax (PBT) before exceptional items	7,582	14,268	14,625	-862	5,672
Impairment of non-current assets	0	618	43	7	0
Profit before Tax (PBT)	7,582	13,650	14,582	-869	5,672
Total Tax expense	168	3,353	5,453	-116	1,924
Profit after Tax (PAT)	7,414	10,298	9,129	-752	3,748
PAT Margin (%)	2.9%	3.7%	2.8%	-0.2%	0.9%
EPS Basic (INR)	49.76	69.15	61.31	-5.01	25.16

Source: Company, KRChoksey Research

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INCOME STATEMENT

Particulars (INR mn)	FY16	FY17	FY18	FY19E	FY20E
EQUITY AND LIABILITIES					
Equity					
Share capital	1,490	1,490	1,490	1,490	1,490
Reserves and surplus	23,198	32,921	38,480	37,090	37,356
Total Equity	24,689	34,411	39,970	38,580	38,846
Non-current liabilities					
Long term borrowings	20,033	23,243	8,259	4,955	5,699
Long term provisions	510	1,331	2,326	4,013	4,103
Other non-current liabilities	309	646	2,122	2,122	2,122
Total non-current liabilities	20,852	25,221	12,708	11,091	11,924
Current Liabilities					
Short Term Borrowings	25,605	31,734	20,630	33,008	37,959
Other Financial Liabilities	28,317	20,769	65,016	80,085	83,825
Short term provisions	740	1,366	878	1,083	1,107
Other Current liabilities	4,189	2,727	3,858	4,760	4,867
Total current liabilities	58,851	56,597	90,382	1,18,936	1,27,758
SOURCES OF FUNDS	1,04,391	1,16,229	1,43,060	1,68,607	1,78,528
ASSETS					
Non-current assets					
Net Block	57,985	66,454	73,233	85,093	93,242
Investment in Joint Ventures	1,194	1,399	1,524	1,524	1,524
Financial Assets	825	813	828	828	828
Other non-current Assets	923	975	596	708	721
Total non-current assets	60,927	69,641	76,181	88,154	96,315
Current Assets					
Inventories	31,753	32,071	47,591	58,276	59,579
Other Financial Assets	8,153	10,779	16,190	20,108	20,563
Cash and Bank balances	389	169	87	63	19
Other current assets	3,170	3,569	3,010	2,007	2,052
Total current assets	43,464	46,587	66,879	80,454	82,213
APPLICATION OF FUNDS	1,04,391	1,16,229	1,43,060	1,68,607	1,78,528

Source: Company, KRChoksey Research

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CASH FLOW STATEMENT

Particulars (INR mn)	FY16	FY17	FY18	FY19E	FY20E
Profit before Tax (PBT)	7,783	13,861	14,769	1,976	5,672
Operating profit before working capital changes	13,662	19,796	21,526	10,320	14,955
Net Cash generated from/(used in) operating activities	22,924	5,968	43,504	14,589	15,176
Net Cash Used In Investing Activities	-11,416	-11,693	-10,181	-16,115	-12,811
Net Cash Used in Financing Activities	-11,518	5,506	-33,405	1,502	-2,409
Net Increase/(Decrease) in Cash and Cash Equivalents	-10	-219	-82	-24	-44
Cash and Cash Equivalents at the beginning of the year	399	389	169	87	63
Cash and Cash Equivalents at the end of the year	389	169	87	63	19

Source: Company, KRChoksey Research

RATIOS

Particulars	FY16	FY17	FY18	FY19E	FY20E
Profitability					
Return on Assets (%)	7.3%	9.6%	6.5%	1.2%	2.1%
Return on Capital Employed(%)	15.3%	18.6%	25.3%	7.3%	12.0%
Return on Equity (%)	30.8%	32.5%	23.3%	5.4%	9.6%
Margin Trend					
EBITDA Margin (%)	5.2%	7.0%	6.4%	2.5%	3.5%
Net Margin (%)	2.9%	4.0%	2.9%	0.5%	0.9%
Liquidity					
Current Ratio	0.7	0.8	0.7	0.7	0.6
Quick Ratio	0.1	0.2	0.2	0.2	0.2
Debtor Days	11	14	18	18	18
Inventory Days	45	42	53	53	53
Payable Days	35	22	50	50	50
Cash Conversion Cycle	21	34	21	21	21
Solvency					
Total Debt / Equity	1.8	1.6	0.7	1.0	1.1
Interest Coverage	3.1	6.1	5.4	1.4	2.1
Valuation Ratios					
EV/EBITDA	6.03	4.69	3.11	7.52	5.48
P/E	4.73	3.22	3.87	17.22	9.61
P/B	1.46	1.05	0.90	0.93	0.93

Source: Company, KRChoksey Research

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Chennai Petroleum Corporation Ltd.				Rating Legend	
Date	CMP (INR)	TP (INR)	Recommendation	Our Rating	Upside
30-Jan-19	242	296	BUY	Buy	More than 15%
14-May-18	297	456	BUY	Accumulate	5% – 15%
22-Jan-18	426	510	BUY	Hold	0 – 5%
10-Nov-17	429	500	BUY	Reduce	-5% – 0
07-Sep-16	305	370	BUY	Sell	Less than – 5%
24-Mar-16	203	369	BUY		
04-Mar-16	187	323	BUY		
16-Nov-15	190	327	BUY		

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