

Bharat Petroleum Corporation

15 November 2017

Reuters: BPCL.NS; Bloomberg: BPCL IN

Earnings Rise In The Backdrop Of Inventory Gains

Bharat Petroleum Corporation or BPCL's reported earnings at Rs23.5bn for 2QFY18 were up 216.6% QoQ and 80.6% YoY, 28% above expectations, primarily because of: 1) Inventory gain of Rs 6.84bn because of higher gross refining margin or GRM of US\$7.97/bbl versus US\$4.88/bbl in 1QFY18 and US\$3.08/bbl in 2QFY17. 2) Increase in market sales of naphtha and rise in pet-coke sales (Kochi refinery). However, the earnings growth was partially negated by: 1) Depreciation and amortisation expenses at Rs6.4bn, up 8.7% QoQ and 41.6% YoY. 2) Interest costs at Rs2.3bn, up sharply by 31% QoQ and 129% YoY. We have rolled forward our target price based on September 19 estimates and retained Accumulate rating on BPCL with a target price of Rs489 (from Rs478 earlier).

Earnings above expectation with muted sales: BPCL reported 6.7% QoQ decline in net sales to Rs533bn in 2QFY18. Refinery throughput was 7mnmt in 2QFY18 versus 6.42mnmt in 1QFY18 and 6.39mnmt in 2QFY17. The decline in sales, despite higher throughput, was on account of lower market sales at 9.79mnmt in 2QFY18 versus 10.04mnmt in 1QFY18. High speed diesel or HSD sales declined from 5.23mnmt in 1QFY18 to 4.57mnmt in 2QFY18, leading to lower market sales. However, EBITDA margin expanded to 6.6% in 2QFY18 from 2.2% in 1QFY18 because of higher GRM. Net profit stood at Rs23.5bn in 2QFY18, up 216.6% YoY and 80.6% on QoQ basis.

GRM benefit from Hurricane Harvey led to inventory gain: GRM in 2QFY18 stood at US\$7.97/bbl versus US\$4.88/bbl in 1QFY18 and US\$3.08/bbl in 2QFY17. Hurricane Harvey caused refinery shutdowns and refineries to operate at lower capacity, thereby driving Singapore GRM from US\$6.65/bbl in the first week of July 2017 to US\$11.01/bbl during the first week of September 2017. For 2QFY18, the company reported inventory gains of around US\$1.47/bbl compared to inventory loss in 1QFY18 of US\$-1.98/bbl and US\$-0.75/bbl in 2QFY17. BPCL is currently processing 62% high sulphur crude oil (including Mumbai and Kochi refineries) and plans to run on 100% high sulphur crude oil at Kochi refinery, if feasible. The Kochi refinery is a complex refinery which is able to process high sulphur crude oil and will be able to generate additional GRM of US\$2/bbl. Considering the fact that the expanded Kochi refinery has been commissioned and will start running at full capacity in the coming quarters, we expect operating expenses to increase, leading to overall increase in GRM by about US\$1.5/bbl.

Rise in depreciation to continue: Depreciation at Rs6.4bn was up 8.7% QoQ and 41.6% YoY and as per management guidance; it is expected to increase further before touching a sustainable level. Interest costs at Rs2.3bn were up 31.3% QoQ and 129.3% YoY. Rising depreciation and interest costs raise concerns over sustainability of earnings.

Capex to exert pressure on earnings: The management has maintained its capex guidance of Rs78bn for FY18 out of which Rs30.6bn has been incurred in 1HFY18. The company plans to incur a capex of Rs81bn in FY19.

Retain Sell rating: Weak GRM environment, planned capex and interest costs set to increase in the coming quarters will exert pressure on cash flow and lead to increased debt. We maintain our concern over cash flow and probable decline in RoE/RoCE with the rise in planned capex. We have rolled forward our target price based on September 19 estimates and retained Accumulate rating on BPCL with a target price of Rs489 (from Rs478 earlier).

ACCUMULATE

Sector: Oil & Gas

CMP: Rs493

Target Price: Rs489

Downside: 1%

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Key Data

Current Shares O/S (mn)	2,169.3
Mkt Cap (Rsbn/US\$bn)	1,069.6/16.3
52 Wk H / L (Rs)	552/389
Daily Vol. (3M NSE Avg.)	4,494,846

Price Performance (%)

	1 M	6 M	1 Yr
BPCL	0.9	1.6	17.7
Nifty Index	0.2	7.8	25.6

Source: Bloomberg

Y/E March (Rsmn)	2QFY17	1QFY18	2QFY18	QoQ (%)	YoY (%)	2QFY18E	Var. (%)
Net sales	446,927	571,322	533,252	(6.7)	19.3	632,131	(15.6)
Cost of goods	(400,693)	(517,643)	(456,201)	(11.9)	13.9	(565,075)	(19.3)
Employee benefits expenses	(6,615)	(8,087)	(8,887)	9.9	34.3	(7,303)	21.7
Other expenses	(25,806)	(33,278)	(32,888)	(1.2)	27.4	(31,838)	3.3
EBITDA	13,813	12,315	35,276	186.5	155.4	27,915	26.4
EBITDAM (%)	3.1	2.2	6.6	-	-	4.4	-
Depreciation and amortisation	(4,524)	(5,892)	(6,406)	8.7	41.6	(5,827)	9.9
EBIT	9,289	6,423	28,870	349.5	210.8	22,088	30.7
EBITM (%)	2.1	1.1	5.4	-	-	3.5	-
Other income	10,223	6,502	8,004	23.1	(21.7)	6,624	20.8
Interest expenses	(1,024)	(1,789)	(2,348)	31.3	129.3	(1,623)	44.7
Extraordinary/exceptional items	-	-	-	-	-	-	-
Profit before tax	18,488	11,136	34,526	210.0	86.7	27,089	27.5
Tax expense	(5,437)	(3,690)	(10,952)	196.8	101.4	(8,669)	26.3
<i>Effective tax rate (%)</i>	29.4	33.1	31.7	-	-	32.0	-
PAT	13,051	7,446	23,574	216.6	80.6	18,420	28.0
NPM (%)	2.9	1.3	4.4	-	-	2.9	-

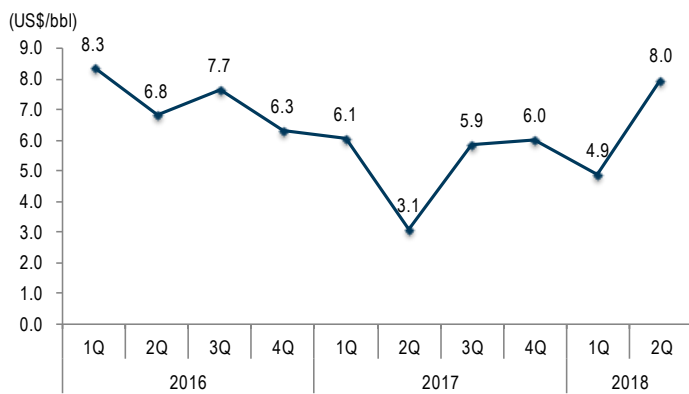
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 1: Key financials

Y/E March (Rsmn)	FY16	FY17E	FY18E	FY19E	FY20E
Revenues	1,869,065	2,073,515	2,201,707	2,442,870	2,604,991
YoY (%)	(22)	11	6	11	7
EBITDA	163,711	139,346	148,098	164,962	174,437
YoY (%)	71	(15)	6	11	6
PAT	91,093	91,183	96,837	107,520	112,277
YoY (%)	90	0	6	11	4
EPS (Rs)	42	42	45	50	52
RoE (%)	34	30	28	27	24
EV/EBITDA (x)	7	9	9	8	8
P/E (x)	12	12	11	10	9

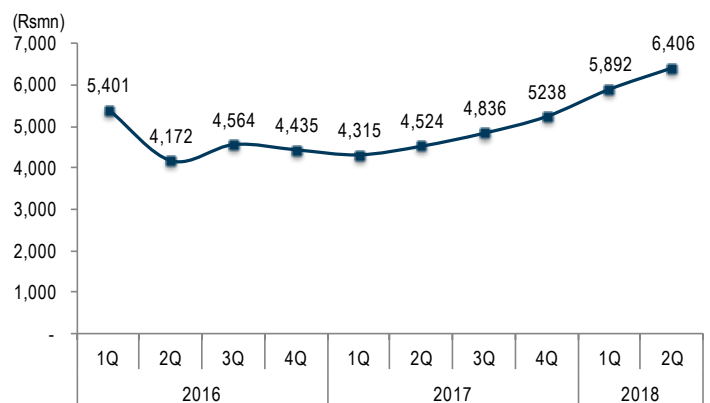
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Gross refining margin



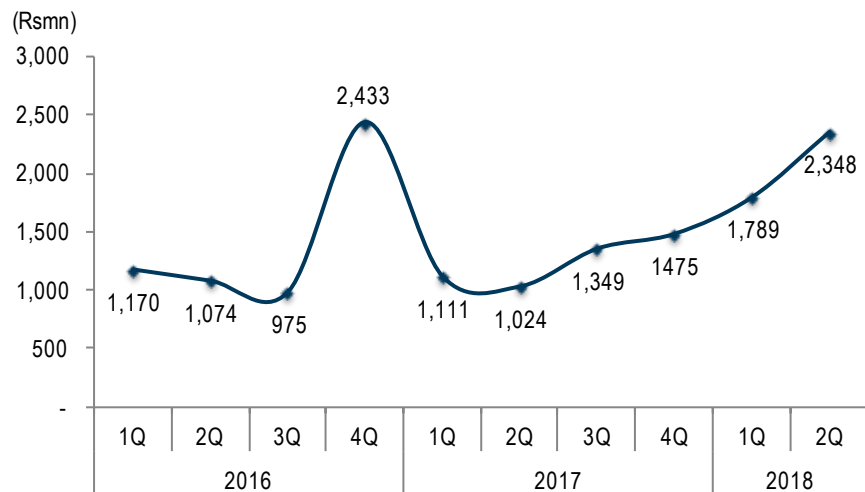
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Depreciation



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: Interest costs



Source: Company, Nirmal Bang Institutional Equities Research

Consolidated financials

Exhibit 5: Income statement

Y/E March (Rsmn)	FY16	FY17E	FY18E	FY19E	FY20E
Net sales	1,869,065	2,073,515	2,201,707	2,442,870	2,604,991
growth (%)	(22.3)	10.9	6.2	11.0	6.6
Operating expenses	1,627,766	1,854,655	1,968,528	2,186,800	2,330,173
Staff cost	31,724	31,208	32,768	34,407	36,127
Other expenses	45,865	48,306	52,313	56,701	64,254
Total expense	1,705,354	1,934,168	2,053,609	2,277,908	2,430,554
EBITDA	163,711	139,346	148,098	164,962	174,437
growth (%)	70.6	(14.9)	6.3	11.4	5.7
EBITDA margin (%)	8.8	6.7	6.7	6.8	6.7
Depreciation & amortisation	24,286	20,728	25,753	31,135	36,001
EBIT	139,425	118,618	122,345	133,827	138,436
Other income	17,409	26,340	31,495	32,669	33,647
Interest paid	11,321	4,651	5,525	6,493	7,035
Others	8,296	-	-	-	-
PBT	137,217	140,307	148,314	160,003	165,047
Tax	41,299	44,275	46,628	47,633	47,921
Effective tax rate (%)	30.1	31.6	31.4	29.8	29.0
Net profit	95,918	96,032	101,686	112,369	117,127
Minority interest	4,825	4,850	4,850	4,850	4,850
Reported Net profit	91,093	91,183	96,837	107,520	112,277
% growth	89.6	0.1	6.2	11.0	4.4
EPS (FD)	42	42	45	50	52
% growth	89.6	0.1	6.2	11.0	4.4
DPS	10	21	21	21	21
Payout ratio (%)	27.4	55.7	52.6	47.6	45.7

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Balance sheet

Y/E March (Rsmn)	FY16	FY17E	FY18E	FY19E	FY20E
Equity	7,231	14,462	21,692	21,692	21,692
Reserves	273,105	310,065	346,171	400,191	458,968
Net worth	280,336	324,526	367,863	421,883	480,660
Loans	288,930	312,537	331,024	380,412	418,799
Net deferred tax liabilities	19,769	20,519	21,269	22,019	22,769
Minority Interest	15,727	20,577	25,427	30,276	35,126
Liabilities	604,762	678,159	745,583	854,590	957,354
Net block	324,629	409,421	438,668	494,533	560,531
Capital WIP	221,188	177,957	202,957	227,957	237,957
Goodwill	610	610	610	610	610
Investments	33,319	125,536	155,965	187,606	221,793
Cash	133,650	97,316	79,976	75,976	73,146
Inventories	154,969	172,876	195,801	218,744	227,063
Debtors	24,235	42,311	46,288	50,186	54,168
Loans and advances	30,675	35,686	38,250	40,817	43,387
Other current assets	9,139.7	7,218.5	7,738.0	8,258.5	8,780.1
Total current assets	219,018	258,092	288,077	318,005	333,399
Liabilities	276,500	303,076	331,266	359,561	379,393
Provisions	51,152	87,697	89,403	90,536	90,689
Total current liabilities	327,652	390,773	420,669	450,097	470,082
Net current assets	(108,634)	(132,681)	(132,592)	(132,092)	(136,683)
Total assets	604,762	678,159	745,583	854,590	957,354

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Cash flow

Y/E March (Rsmn)	FY16	FY17E	FY18E	FY19E	FY20E
Profit after tax	95,918	96,032	101,686	112,369	117,127
Depreciation	24,286	20,728	25,753	31,135	36,001
Other income	(17,409)	(26,340)	(31,495)	(32,669)	(33,647)
Interest	11,321	4,651	5,525	6,493	7,035
Working capital changes	(11,821)	24,047	(89)	(500)	4,592
Others	(7,846)	7,258	750	750	750
Operating cash flow	94,450	126,377	102,131	117,578	131,858
Capital expenditure	(119,611)	(62,290)	(80,000)	(112,000)	(112,000)
Investments	(1,723)	(92,216)	(30,429)	(31,641)	(34,187)
Other income	17,409	26,340	31,495	32,669	33,647
Cash flow from investments	(103,925)	(128,166)	(78,934)	(110,972)	(112,541)
Equity	-	-	-	-	-
Debt	34,007	23,607	18,488	49,388	38,388
Interest expenses	(11,321)	(4,651)	(5,525)	(6,493)	(7,035)
Dividends	(26,326)	(53,500)	(53,500)	(53,500)	(53,500)
Cash flow from financing	(3,639)	(34,544)	(40,538)	(10,606)	(22,147)
Total cash generation	(13,114)	(36,333)	(17,341)	(4,000)	(2,830)
Opening cash balance	146,764	133,650	97,316	79,976	75,976
Closing cash & bank balance	133,650	97,316	79,976	75,976	73,146

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 8: Key ratios

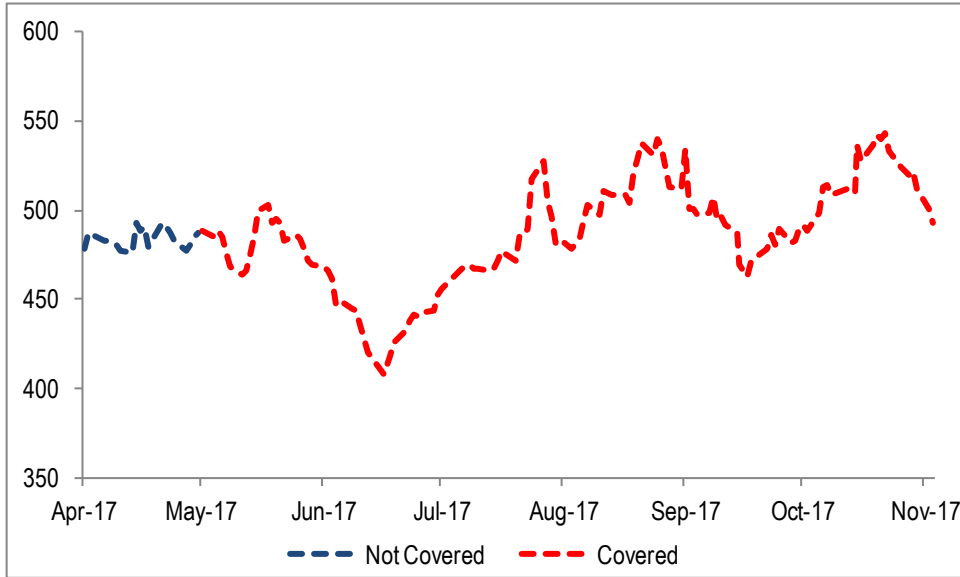
Y/E March (Rsmn)	FY16	FY17E	FY18E	FY19E	FY20E
Profitability and return ratios					
EBITDA margin (%)	8.8	6.7	6.7	6.8	6.7
EBIT margin (%)	7.5	5.7	5.6	5.5	5.3
Net profit margin (%)	5.1	4.6	4.6	4.6	4.5
RoE (%)	34.2	29.6	27.6	26.6	24.4
RoCE (%)	32.0	22.0	19.8	18.4	16.8
Working capital & liquidity ratios					
Receivables (days)	5	7	8	7	8
Inventory (days)	35	34	36	37	36
Payables (days)	62	60	61	60	59
Current ratio (x)	0.67	0.66	0.68	0.71	0.71
Valuation ratios					
EV/sales (x)	0.7	0.6	0.6	0.6	0.5
EV/EBITDA (x)	7.5	9.2	8.9	8.3	8.1
P/E (x)	12	12	11	10	9
P/BV (x)	3.8	3.3	2.9	2.5	2.2

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price	Target price (Rs)
12 May 2017	Accumulate	738	717
16 August 2017	Accumulate	479	478
15 November 2017	Accumulate	493	489

Rating track graph



Disclaimer

Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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