

Bharat Petroleum Corporation

31 May 2018

Reuters: BPCL.NS; Bloomberg: BPCL IN

Strong Earnings Despite Weak Adjusted GRM

Bharat Petroleum Corporation or BPCL's reported earnings of Rs26.7bn for 4QFY18 were up 45.2% QoQ and 24.7% YoY, 72.5% above our expectation, primarily because of: 1) Increase in crude oil throughput from 6mmt in 4QFY17 and 7mmt in 3QFY18 to 7.85mmt in 4QFY18. 2) Rise in market sales (domestic) from 9.26mmt in 4QFY17 and 10.65mmt in 3QFY18 to 10.73mmt in 4QFY18, up 16% YoY and 1% QoQ. 3) Decline in employee benefit expenses by 33.4% QoQ to Rs9bn in 4QFY18. However, the rise in earnings was capped on account of: 1) Decline of adjusted gross refining margin or GRM from US\$5.85/bbl in 4QFY17 to US\$5.57/bbl in 4QFY18. 2) Interest expenses at Rs2bn rising 49% QoQ and 10% YoY. 3) Depreciation and amortisation expenses at Rs 7bn rising 41.5% QoQ and 9.4% YoY.

The inability of oil marketing companies or OMCs to increase product prices recently amid a rising crude oil price environment has raised concerns about the ability of OMCs to hike prices to compensate for the rise in crude oil prices. This also raises concerns on the pricing freedom of OMCs to set prices based on the given formula. Inability to increase prices is expected to negatively impacting their marketing margins. We have revised our SOTP-based valuation of BPCL and retained Accumulate rating on it with a revised target price of Rs436 (from Rs513 earlier).

Strong revenues backed by higher domestic sales and refining throughput: BPCL reported revenues of Rs760bn, an increase of 15.2% QoQ and 8.4% YoY. Higher revenues were driven by: 1) Rise in domestic sales from 9.26mmt in 4QFY17 and 10.65mmt in 3QFY18 to 10.73mmt in 4QFY18, up 16% YoY and 1% QoQ. 2) Higher refining throughput at 7.85mmt in 4QFY18 versus 6mmt in 4QFY17 and 7.27mmt in 3QFY18. Increase in throughput is on account of commissioning of additional capacity at Kochi refinery. Throughput of Kochi refinery increased from 11.79mmt in FY17 to 14.29mmt in FY18.

Adjusted GRM disappoints because of commissioning of Kochi refinery: GRM in 4QFY18 stood at US\$6.5/bbl versus US\$6.01/bbl in 4QFY17. However, adjusted GRM declined to US\$5.57/bbl in 4QFY18 from US\$5.85/bbl in 4QFY17. BPCL reported inventory gain of US\$0.94/bbl in 4QFY18 versus US\$0.15/bbl in 4QFY17. Kochi refinery's adjusted GRM declined from US\$5.03/bbl in 4QFY17 to US\$4.96/bbl in 4QFY18 on account of commissioning of additional capacity. Kochi refinery shall take five to six months to stabilise after which it should deliver higher GRM. Mumbai refinery's GRM stood at US\$6.2/bbl in 4QFY18 versus US\$6.8/bbl in 4QFY17. EBITDA stood at Rs37bn, up 68.2% QoQ and 16.7% YoY, supported by decline in employee benefit expenses by 33.4% QoQ to Rs9bn in 4QFY18.

Rising depreciation and interest costs raises concerns: Depreciation at Rs7bn in 4QFY18 was up 41.5% QoQ and 9.4% YoY. Interest costs at Rs 2bn increased 48.7% QoQ and 9.6% YoY. Rise in interest costs was on account of the rise in consolidated net debt from Rs296bn in FY17 to Rs356bn in FY18. The management expects a capital expenditure of Rs78bn in FY19 (Rs28bn - Kochi refinery, Rs7.2bn - marketing, Rs8bn - upstream, Rs4.2bn - Mumbai refinery, and Rs30.6bn - others). Earnings stood at Rs27bn, up 45.2% QoQ and 24.7% YoY.

Retain Accumulate rating with a revised target price of Rs436: 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 decline in RoE/RoCE with the rise in planned capex. We have revised our SOTP-based valuation of BPCL and retained Accumulate rating on it with a revised target price of Rs436 (from Rs513 earlier).

ACCUMULATE

Sector: Oil & Gas

CMP: Rs400

Target Price: Rs436

Upside: 9%

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Key Data

Current Shares O/S (mn)	2,169.2
Mkt Cap (Rsbn/US\$bn)	868.2/12.9
52 Wk H / L (Rs)	552/360
Daily Vol. (3M NSE Avg.)	6,035,458

Price Performance (%)

	1 M	6 M	1 Yr
BPCL	3.3	(20.6)	(19.2)
Nifty Index	(1.2)	3.8	10.3

Source: Bloomberg

Y/E March (Rsmn)	4QFY18	3QFY18	QoQ (%)	4QFY17	YoY (%)	4QFY18E	Var. (%)
Net sales	760,670	660,232	15.2	701,952	8.4	743,641	2.3
Cost of goods	(676,603)	(594,632)	13.8	(626,125)	8.1	(673,277)	0.5
Employee benefits expenses	(9,571)	(14,368)	(33.4)	(7,766)	23.2	(7,921)	20.8
Other expenses	(37,280)	(29,109)	28.1	(36,178)	3.0	(36,902)	1.0
EBITDA	37,216	22,123	68.2	31,883	16.7	25,541	45.7
EBITDAM (%)	4.9	3.4	-	4.5	-	3.4	-
Depreciation and amortisation	(7,413)	(5,238)	41.5	(6,774)	9.4	(7,113)	4.2
EBIT	29,803	16,885	76.5	25,109	18.7	18,428	61.7
EBITM (%)	4	3	-	4	-	2	-
Other income	8,329	6,624	25.7	7,274	14.5	7,101	17.3
Interest expenses	(2,194)	(1,475)	48.7	(2,002)	9.6	(2,402)	(8.7)
Extraordinary/exceptional items	-	-	-	-	-	-	-
Profit before tax	35,939	22,034	63.1	30,381	18.3	23,127	55.4
Tax expense	(9,202)	(3,616)	-	(8,943)	-	(7,632)	-
Effective tax rate (%)	26	16	-	29	-	33	-
PAT	26,736	18,418	45.2	21,438	24.7	15,495	72.5
NPM (%)	3.5	2.8	-	3.1	-	2.1	-

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 1: Key financials

Y/E March (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Revenues	1,878,546	2,012,507	2,201,707	2,442,870	2,604,991
YoY (%)	(22)	7	9	11	7
EBITDA	129,771	135,125	148,098	164,962	174,437
YoY (%)	35	4	10	11	6
PAT	80,889	95,070	101,686	112,369	117,127
YoY (%)	69	17.5	6.9	11	4
RoE (%)	29	31	28	27	24
EV/EBITDA (x)	8.4	8.9	8.1	7.6	7.4
P/E (x)	10	9	9	8	7

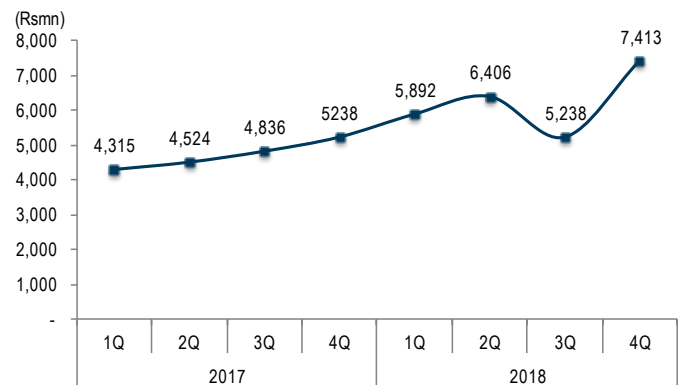
Source: Company, Nirmal Bang Institutional Equities Research

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	FY17	FY18E	FY19E	FY20E
Net sales	1,878,546	2,012,507	2,201,707	2,442,870	2,604,991
Growth (%)	(21.9)	7.1	9.4	11.0	6.6
Operating expenses	1,590,746	1,714,110	1,968,528	2,186,800	2,330,173
Staff cost	29,621	36,691	32,768	34,407	36,127
Other expenses	128,409	126,582	52,313	56,701	64,254
Total expense	1,748,775	1,877,382	2,053,609	2,277,908	2,430,554
EBITDA	129,771	135,125	148,098	164,962	174,437
Growth (%)	35.2	4.1	9.6	11.4	5.7
EBITDA margin (%)	6.9	6.7	6.7	6.8	6.7
Depreciation & amortisation	20,719	21,076	25,753	31,135	36,001
EBIT	109,052	114,048	122,345	133,827	138,436
Other income	19,469	29,911	31,495	32,669	33,647
Interest paid	6,805	6,964	5,525	6,493	7,035
Others	400	-	-	-	-
PBT	121,316	136,996	148,314	160,003	165,047
Tax	40,427	41,926	46,628	47,633	47,921
Effective tax rate (%)	33.3	30.6	31.4	29.8	29.0
Net profit	80,889	95,070	101,686	112,369	117,127

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Balance sheet

Y/E March (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Equity	6,556	13,113	21,692	21,692	21,692
Reserves	271,377	295,085	346,171	400,191	458,968
Net worth	277,933	308,198	367,863	421,883	480,660
Loans	228,839	331,150	331,024	380,412	418,799
Net deferred tax liabilities	30,720	40,548	21,269	22,019	22,769
Minority Interest	16,783	19,582	25,427	30,276	35,126
Liabilities	554,274	699,477	745,583	854,590	957,354
Net block	251,896	444,518	438,668	494,533	560,531
Capital WIP	127,452	117,627	202,957	227,957	237,957
Goodwill	610	610	610	610	610
Investments	169,793	149,007	155,965	187,606	221,793
Cash	20,368	6,380	9,976	5,976	3,146
Inventories	146,437	211,968	195,801	218,744	227,063
Debtors	22,169	48,038	46,288	50,186	54,168
Loans and advances	632	782	38,250	40,817	43,387
Other current assets	124,860.5	111,935	77,738.0	78,258.5	78,780.1
Total current assets	294,098	372,722	358,077	388,005	403,399
Liabilities	300,798	380,628	331,266	359,561	379,393
Provisions	9,145	10,757	89,403	90,536	90,689
Total current liabilities	309,943	391,385	420,669	450,097	470,082
Net current assets	(15,845)	(18,663)	(62,592)	(62,092)	(66,683)
Total assets	554,274	699,477	745,583	854,590	957,354

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Cash flow

Y/E March (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Profit after tax	80,889	95,070	101,686	112,369	117,127
Depreciation	20,719	21,076	25,753	31,135	36,001
Other income	(10,458)	(11,093)	(31,495)	(32,669)	(33,647)
Interest	6,805	6,964	5,525	6,493	7,035
Working capital changes	3,313	(17,733)	(89)	(500)	4,592
Others	9,923	(3,723)	39,174	750	750
Operating cash flow	111,190	90,562	140,555	117,578	131,858
Capital expenditure	(101,843)	(95,592)	(80,000)	(112,000)	(112,000)
Investments	(1,385)	(69,048)	(30,429)	(31,641)	(34,187)
Other income	10,902	12,051	31,495	32,669	33,647
Cash flow from investnents	(92,327)	(152,589)	(78,934)	(110,972)	(112,541)
Equity	-	-	-	-	-
Debt	30,326	126,072	1,000	49,388	38,388
Interest expenses	(10,166)	(10,839)	(5,525)	(6,493)	(7,035)
Dividends	(33,477)	(67,193)	(53,500)	(53,500)	(53,500)
Cash flow from financing	(13,316)	48,039	(58,026)	(10,606)	(22,147)
Total cash generation	5,548	(13,989)	3,596	(4,000)	(2,830)
Opening cash balance	14,820	20,368	6,380	9,976	5,976
Closing cash & bank balance	20,368	6,380	9,976	5,976	3,146

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 8: Key ratios

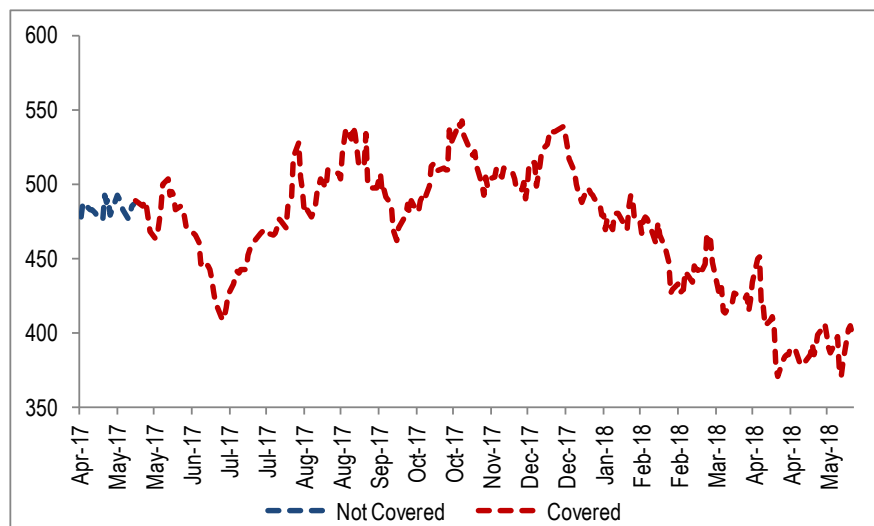
Y/E March (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Profitability and return ratios					
EBITDA margin (%)	6.9	6.7	6.7	6.8	6.7
EBIT margin (%)	5.8	5.7	5.6	5.5	5.3
Net profit margin (%)	4.3	4.7	4.6	4.6	4.5
RoE (%)	29.1	30.8	27.6	26.6	24.4
RoCE (%)	22.4	18.0	17.8	16.8	15.4
Working capital & liquidity ratios					
Receivables (days)	4	9	8	7	8
Inventory (days)	34	45	36	37	36
Payables (days)	69	81	61	60	59
Current ratio (x)	0.95	0.95	0.85	0.86	0.86
Valuation ratios					
EV/sales (x)	0.6	0.6	0.5	0.5	0.5
EV/EBITDA (x)	8.4	8.9	8.1	7.6	7.4
P/E (x)	10	9	9	8	7
P/BV (x)	3.2	2.9	2.4	2.1	1.8

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
12 February 2018	Accumulate	475	513
31 May 2018	Accumulate	400	436

Rating track graph



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ACCUMULATE -5% to 15%

SELL < -5%

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