

Hindustan Petroleum Corporation

2 November 2018

Reuters: HPCL.BO; Bloomberg: HPCL IN

Earnings Decline Driven By Weak Gross Refining Margin

Hindustan Petroleum Corporation's (HPCL) 2QFY19 profit declined 36.5% QoQ and 37.1% YoY to Rs10.9bn. The decline in earnings on YoY basis was because of: 1) Lower gross refining margin or GRM of US4.7\$/bbl in 2QFY19 versus US7.2\$/bbl in 1QFY19 and US7.7\$/bbl in 2QFY18. 2) Decline in domestic sales from 9.64mmmt in 1QFY19 to 8.82mmmt in 2QFY19. 3) Interest expenses at Rs2bn increased by 5.1% QoQ and 28.4% YoY. 4) Other income declining by 20.4% YoY to Rs4bn. However, refining throughput at 4.76mmmt in 2QFY19 increased from 4.52mmmt in 1QFY19 and 4.64mmmt in 2QFY18. The HPCL stock is under review and we will shortly come out with an update on our estimates and recommendation.

Revenues increase primarily driven by higher crude oil prices: HPCL posted revenues of Rs733bn for the quarter, an increase of 35% YoY and flat on QoQ basis. Higher revenues were because of: 1) Rise in average crude oil price from US50\$/bbl in 2QFY18 and US72\$/bbl in 1QFY19 to US74\$/bbl in 2QFY19. 2) Increase in refining throughput from 4.64mmmt in 2QFY18 and 4.52mmmt in 1QFY19 to 4.76mmmt in 2QFY19.

EBITDA performance impacted because of lower GRM: HPCL reported EBITDA of Rs21bn for 2QFY19, a decline of 33.5% QoQ and 27% YoY. Weak EBITDA performance was primarily because of: 1) Poor GRM at US4.7\$/bbl in 2QFY19 versus US7.2\$/bbl in 1QFY19 and US7.7\$/bbl in 2QFY18. 2) Other expenses at Rs37.6bn in 2QFY19 rising by 52.1% YoY. Other expenses included a foreign currency translation loss of Rs8.9bn in 2QFY19 as compared to a gain of Rs0.2bn in 2QFY18.

Decline in other income and rise in interest expenses adds to pressure on earnings: Interest expenses at Rs2bn rose 28.4% YoY and 5.1% QoQ. Other income declined 20.4% YoY to Rs4bn in 2QFY19. HPCL posted profit after tax of Rs10.9bn, down 37.1% YoY and 36.5% QoQ. However, further earnings decline was mitigated by: 1) Lower income tax expenses with effective tax rate of 31.6% in 2QFY19 as compared to 33.9% in 1QFY19 and 33% in 2QFY18. 2) Higher refining throughput at 4.76mmmt in 2QFY19. 3) Employee expenses declining by 6.3% QoQ and 2.7% YoY to Rs 6.8bn in 2QFY19.

We will come out with our recommendation soon: While we remain concerned about the increase in capex over the next five years, rise in interest costs and concerns over product pricing freedom, we note the sharp decline in the stock price in the recent past. We are reviewing our estimates and recommendations and will come out with an update shortly.

UNDER REVIEW

Sector: Oil & Gas

CMP: Rs229

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Key Data

Current Shares O/S (mn)	1,523.8
Mkt Cap (Rsbn/US\$bn)	349.7/4.8
52 Wk H / L (Rs)	452/163
Daily Vol. (3M NSE Avg.)	9,991,236

Price Performance (%)

	1 M	6 M	1 Yr
HPCL	(5.6)	(24.6)	(48.2)
Nifty Index	(5.7)	3.3	(0.6)

Source: Bloomberg

Y/E March (Rsmn)	2QFY19	1QFY19	QoQ (%)	2QFY18	YoY (%)	2QFY19E	Var. (%)
Net sales	733,761	732,199	0.2	543,358	35.0	761,901	(3.7)
Cost of goods	(667,981)	(656,832)	1.7	(482,463)	38.5	(688,575)	(3.0)
Employee benefit expenses	(6,891)	(7,353)	(6.3)	(7,081)	(2.7)	(7,501)	(8.1)
Other expenses	(37,670)	(36,107)	4.3	(24,759)	52.1	(36,833)	2.3
EBITDA	21,220	31,907	(33.5)	29,055	(27.0)	28,992	(26.8)
EBITDAM (%)	2.9	4.4	-	5.3	-	3.8	-
Depreciation and amortisation	(7,385)	(7,064)	4.5	(6,804)	8.5	(7,170)	3.0
EBIT	13,835	24,843	(44.3)	22,251	(37.8)	21,822	(36.6)
EBITM (%)	1.9	3.4	-	4.1	-	2.9	-
Other income	4,134	3,056	35.3	5,194	(20.4)	3,081	34.2
Interest expenses	(2,007)	(1,909)	5.1	(1,563)	28.4	(1,937)	3.6
Profit before tax	15,962	25,990	(38.6)	25,882	(38.3)	22,966	(30.5)
Tax expenses	(5,042)	(8,798)	-	(8,535)	-	(7,579)	-
Effective tax rate (%)	31.6	33.9	-	33.0	-	33.0	-
PAT	10,920	17,192	(36.5)	17,347	(37.1)	15,387	(29.0)
NPM (%)	1.5	2.3	-	3.2	-	2.0	-

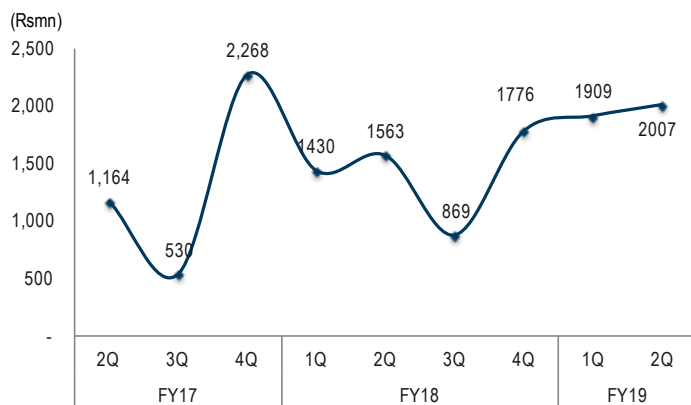
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 1: Key financials

Y/E March (Rsmn)	FY17	FY18	FY19E	FY20E	FY21E
Revenues	1,858,239	2,182,914	2,451,728	2,603,497	2,771,164
YoY (%)	5.8	17.5	12.3	6.2	6.4
EBITDA	108,953	107,222	133,136	143,109	153,767
Margin (%)	5.9	4.9	5.4	5.5	5.5
PAT	82,358	72,183	77,004	79,112	81,813
YoY (%)	113.2	(12.4)	6.7	2.7	3.4
EPS (Rs)	54.1	47.4	50.6	51.9	53.7
RoE (%)	39.1	28.3	25.3	22.4	20.2
EV/EBITDA (x)	4.6	4.4	3.7	3.7	3.9
P/E (x)	5.6	5.4	5.1	5.0	4.9

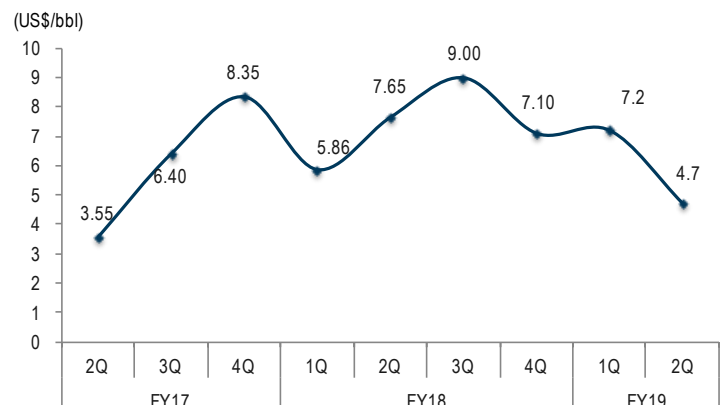
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Interest costs



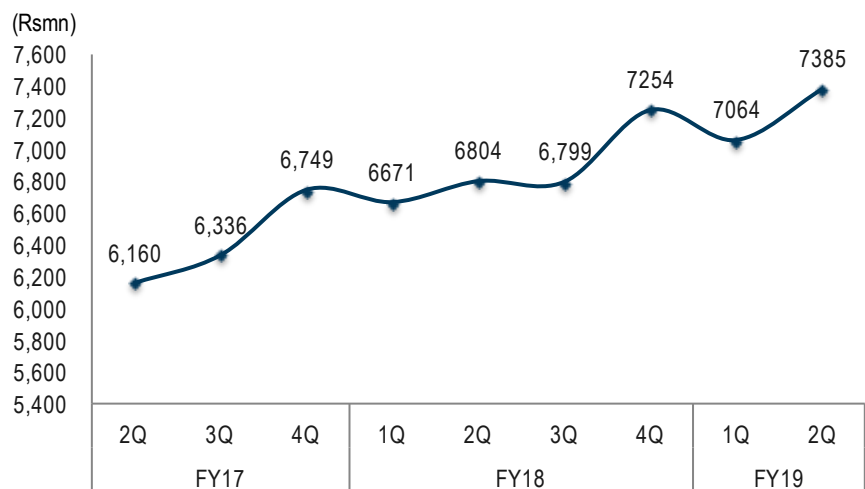
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Gross refining margin



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: Depreciation



Source: Company, Nirmal Bang Institutional Equities Research

Consolidated financials

Exhibit 5: Income statement

Y/E March (Rsmn)	FY17	FY18	FY19E	FY20E	FY21E
Net sales	1,858,239	2,182,914	2,451,728	2,603,497	2,771,164
% growth	5.8	17.5	12.3	6.2	6.4
Operating costs	1,679,721	1,998,372	2,237,405	2,375,143	2,527,889
Staff expenses	29,694	28,926	30,372	31,891	33,485
Other expenses	39,872	48,394	50,814	53,355	56,022
EBITDA	108,953	107,222	133,136	143,109	153,767
EBITDA (%)	5.9	4.9	5.4	5.5	5.5
% growth	36.8	(1.6)	24.2	7.5	7.4
Depreciation	27,920	28,437	22,323	25,711	27,716
EBIT	81,033	78,786	110,813	117,397	126,052
EBIT (%)	4.4	3.6	4.5	4.5	4.5
Net interest expenses	6,092	6,179	10,141	14,194	16,576
Other income	12,370	12,055	14,431	15,051	12,816
Other adjustments	(24,664)	(16,440)	-	-	-
Earnings before tax	111,974	101,101	115,103	118,254	122,292
Tax-total	29,616	28,919	38,099	39,142	40,479
Rate of tax (%)	26.4	28.6	33.1	33.1	33.1
Net profit	82,358	72,183	77,004	79,112	81,813
% growth	113.2	(12.4)	6.7	2.7	3.4

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Balance sheet

Y/E March (Rsmn)	FY17	FY18	FY19E	FY20E	FY21E
Share capital	10,162	15,242	15,242	15,242	15,242
Reserves and surplus	200,552	240,082	288,743	337,740	389,438
Net worth	210,714	255,324	303,985	352,982	404,680
Loans	221,301	219,525	246,118	281,118	316,118
Deferred tax liability	61,493	91,751	92,584	93,584	94,584
Capital employed	493,507	566,600	642,686	727,683	815,382
Net fixed assets	387,438	427,057	485,067	559,856	682,640
Investments	60,698	73,066	74,566	76,066	77,566
Current assets, loans	355,055	396,594	378,000	396,860	369,379
Inventories	186,292	186,122	159,893	167,584	176,057
Debtors	40,917	55,870	58,542	62,166	66,169
Cash and bank	64,402	94,928	99,392	106,438	65,980
Others	63,445	59,673	60,173	60,673	61,173
Less: Current liabilities	309,683	330,116	294,945	305,098	314,203
Current liabilities	268,106	293,269	251,465	259,742	268,713
Provisions	41,577	36,847	43,480	45,356	45,490
Net current assets	(19,030)	(28,451)	(16,338)	(14,675)	(10,804)
Total capital employed	493,507	566,600	642,686	727,683	815,382

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Cash flow

Y/E March (Rsmn)	FY17	FY18	FY19E	FY20E	FY21E
Profit after tax	82,358	72,183	77,004	79,112	81,813
Depreciation	27,764	28,344	21,823	25,211	27,216
Other income	(12,370)	(12,055)	(14,431)	(15,051)	(12,816)
Interest	6,092	6,179	10,141	14,194	16,576
Working cap. changes	(23,794)	9,421	(12,113)	(1,662)	(3,872)
Others	17,798	(293)	1,000	1,000	1,000
Operating cash flow	97,849	103,778	83,424	102,804	109,917
Capex	(88,825)	(67,303)	(80,000)	(100,000)	(150,000)
Investments	(608)	(12,368)	(1,500)	(1,500)	(1,500)
Other income	12,370	12,055	14,431	15,051	12,816
Cash flow from investments	(77,063)	(67,616)	(67,069)	(86,449)	(138,684)
Equity	-	-	-	-	-
Debt	7,933	(1,776)	26,593	35,000	35,000
Interest expenses	(6,092)	(6,179)	(10,141)	(14,194)	(16,576)
Dividends	(41,857)	(27,939)	(28,344)	(30,115)	(30,115)
Cash flow from financing	(26,628)	(5,635)	(11,892)	(9,309)	(11,691)
Total cash generation	(5,842)	30,526	4,463	7,046	(40,458)
Opening cash balance	70,244	64,402	94,928	99,392	106,438
Closing cash balance*	64,402	94,928	99,392	106,438	65,980

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 8: Key ratios

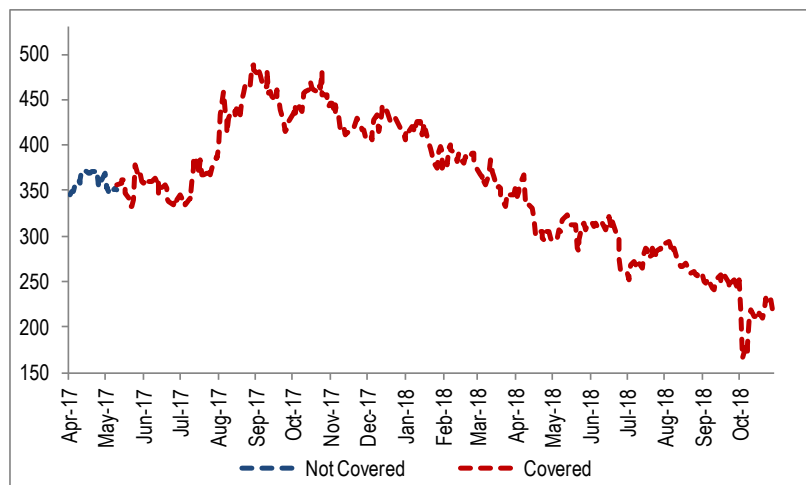
Y/E March (Rsmn)	FY17	FY18	FY19E	FY20E	FY21E
Profitability and return ratios (%)					
EBITDA margin (%)	5.9	4.9	5.4	5.5	5.5
EBIT margin (%)	4.4	3.6	4.5	4.5	4.5
Net profit margin (%)	4.4	3.3	3.1	3.0	3.0
RoE (%)	39.1	28.3	25.3	22.4	20.2
RoCE (%)	22.0	20.7	24.6	22.2	19.2
Working capital and liquidity ratios					
Receivable (days)	8	9	9	9	9
Inventory (days)	25	24	24	23	23
Payable (days)	17	17	17	17	17
Current ratio (x)	0.9	1.0	1.0	1.0	1.0
Quick ratio(x)	0.6	0.6	0.6	0.6	0.6
Valuation ratios					
EV/sales (x)	0.3	0.2	0.2	0.2	0.2
EV/EBITDA (x)	4.6	4.4	3.7	3.7	3.9
P/E (x)	5.6	5.4	5.1	5.0	4.9
P/BV (x)	1.7	1.4	1.1	1.0	0.9

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price	Target price (Rs)
12 May 2017	Sell	567	482
29 May 2017	Sell	567	482
7 August 2017	Sell	432	321
10 November 2017	Sell	431	321
12 February 2018	Sell	393	358
23 May 2018	Sell	312	272
9 August 2018	Sell	282	249
2 November 2018	Under Review	229	-

Rating track graph



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BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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