

Indian Oil Corporation

13 August 2018

Reuters: IOC.BO; Bloomberg: IOCL IN

Strong Earnings Driven By Inventory Gains, But Interest Expenses Up

Indian Oil Corporation (IOCL) reported earnings of Rs68bn for 1QFY19, up 30.9% QoQ and 50.2% YoY, primarily because of: 1) Higher gross refining margin or GRM of US\$10.21/bbl in 1QFY19 versus US\$9.2/bbl in 4QFY18 and US\$4.3/bbl in 1QFY18, mainly on account of higher inventory gains of Rs 59bn in 1QFY19 as compared to Rs24bn in 4QFY18 and an inventory loss of Rs28bn in 1QFY18. 2) Rise in refinery throughput from 17.2mmt in 4QFY18 and 17.5mmt in 1QFY18 to 17.7mmt in 1QFY19. 3) Employee benefit expenses at Rs23.6bn in 1QFY19 declined 19.5% QoQ and 1.9% YoY. 4) Domestic product sales at 21.6mmt in 1QFY19 were up 4% YoY. 5) Pipeline throughput at 22.8mmt in 1QFY19 increased 7% on YoY basis. However, with the rise in debt from Rs34.9bn in 1QFY18 to Rs44.7bn in 1QFY19, interest expenses at Rs10.3bn increased 43.6% YoY. We have retained Sell rating on IOCL with a target price of Rs137.

Revenues rise on account of higher crude oil prices, product sales and refinery throughput: IOCL's net sales at Rs1,497bn in 1QFY19 increased 9.5% QoQ and 42.0% YoY. Revenues increased because of: 1) Sharp rise in average crude oil price from US\$50/bbl in 1QFY18 and US\$64/bbl in 4QFY18 to US\$72/bbl in 1QFY19. 2) Higher domestic product sales at 21.6mmt in 1QFY19 versus 20.8mmt the previous quarter and same quarter last year. 3) Rise in refinery throughput from 17.5mmt in 1QFY18 and 17.2mmt in 4QFY18 to 17.6mmt in 1QFY19. Rise in refinery throughput could be attributed to the rise in capacity utilisation at 102.4% in 1QFY19 as compared to 101.6% in 4QFY18.

Higher inventory gains and lower employee expenses lead to strong EBITDA performance: EBITDA stood at Rs126bn, up 57.2% YoY and 14.1% QoQ. Strong EBITDA performance was on account of: 1) Higher GRM of US\$10.21/bbl in 1QFY19 versus US\$9.2/bbl in 4QFY18 and US\$4.3/bbl in 1QFY18, mainly on account of higher inventory gains of Rs59bn in 1QFY19 as compared to Rs24bn in 4QFY18 and an inventory loss of Rs28bn in 1QFY18. 2) Employee benefit expenses at Rs23.6bn declined 19.5% QoQ and 1.9% YoY. EBITDA margin at 8.4% in 1QFY19 improved 81bps YoY and 34bps QoQ.

Rise in debt led to higher finance costs and impacted earnings negatively: Debt numbers are not comparable on QoQ basis as IOCL debt increases in 4Q due to payment of dividends and other activities. Debt in 1QFY19 stood at Rs 44.7bn, an increase from Rs 34.9bn in 1QFY18. As a result of rise in debt, interest expense at Rs 10.3bn in 1QFY19 increased by 43.6% YoY.

Retain Sell rating with a target price of Rs137: Given our concerns on the likely decline in GRM, increase in capex over the next five years, rise in interest costs and concerns over product pricing freedom, we expect the upside in earnings to be capped. We believe that with likely low earnings growth and a decline in RoE and RoCE, the stock will get de-rated. We have retained Sell rating on IOCL with a target price of Rs137.

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SELL

Sector: Oil & Gas

CMP: Rs161

Target Price: Rs137

Downside: 15%

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Key Data

Current Shares O/S (mn)	9,711.8
Mkt Cap (Rsbn/US\$bn)	1,560.2/22.3
52 Wk H / L (Rs)	231/150
Daily Vol. (3M NSE Avg.)	10,215,710

Price Performance (%)

	1 M	6 M	1 Yr
IOCL	1.0	(15.2)	(22.0)
Nifty Index	3.1	7.7	16.9

Source: Bloomberg

Y/E March (Rsmn)	1QFY19	4QFY18	QoQ (%)	1QFY18	YoY (%)	1QFY19E	Var. (%)
Net sales	1,497,469	1,367,326	9.5	1,054,342	42.0	1,512,601	(1.0)
Cost of goods	(1,248,256)	(1,141,125)	9.4	(878,246)	42.1	(1,273,260)	(2.0)
Employee benefit expenses	(23,686)	(29,419)	(19.5)	(24,141)	(1.9)	(30,301)	(21.8)
Other expenses	(99,769)	(86,570)	15.2	(71,960)	38.6	(89,085)	12.0
EBITDA	125,758	110,212	14.1	79,995	57.2	119,955	4.8
EBITDAM (%)	8.4	8.1	-	7.6	-	7.9	-
Depreciation and amortisation	(17,879)	(19,336)	(7.5)	(17,213)	3.9	(20,303)	(11.9)
EBIT	107,879	90,876	18.7	62,782	71.8	99,652	8.3
EBITM (%)	7.2	6.6	-	5.9	-	6.5	-
Other income	5,853	2,481	135.9	12,276	(52.3)	2,481	135.9
Interest expenses	(10,311)	(13,029)	(20.9)	(7,180)	43.6	(8,000)	28.9
Extraordinary/exceptional items	-	-	-	-	-	-	-
Profit before tax	103,422	80,328	28.7	67,878	52.4	94,133	9.9
Tax expenses	(35,110)	(28,148)	-	(22,393)	-	(31,064)	-
<i>Effective tax rate (%)</i>	34	35	-	33	-	33	-
PAT	68,311	52,180	30.9	45,485	50.2	63,069	8.3

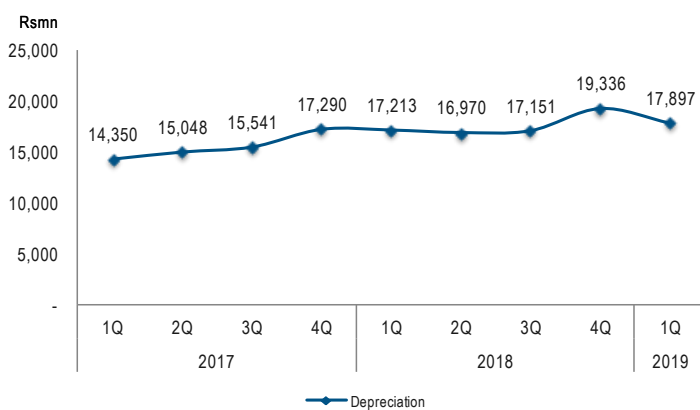
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 1: Key financials

Y/E March (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Revenues	3,460,447	3,553,101	4,480,501	4,985,437	5,329,306
YoY (%)	(22.1)	2.7	26.1	11.3	6.9
EBITDA	234,429	340,132	320,926	344,134	352,377
YoY (%)	136.5	45.1	(5.6)	7.2	2.4
PAT	120,225	198,495	179,763	191,164	195,047
YoY (%)	144.8	65.1	(9.4)	6.3	2.0
EPS (Rs)	12.4	20.4	18.5	20	20.1
RoE (%)	13.8	20.0	21.0	21.1	20.2
EV/EBITDA (x)	9.8	7.2	7.0	7.0	7.1
P/E (x)	12.9	7.9	8.7	8.2	8.1

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Depreciation



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: GRM



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	3,460,447	3,553,101	4,480,501	4,985,437	5,329,306
Growth YoY (%)	(22.1)	2.7	26.1	11.3	6.9
Operating costs	2,850,235	2,751,190	3,985,930	4,450,824	4,768,302
Staff expenses	75,018	102,040	78,443	84,802	91,679
Other expenses	300,765	359,738	95,202	105,676	116,948
EBITDA	234,429	340,132	320,926	344,134	352,377
EBITDA growth (%)	136.5	45.1	(5.6)	7.2	2.4
EBITDA margin (%)	6.8	9.6	7.2	6.9	6.6
Depreciation	56,984	68,486	67,605	67,755	67,905
EBIT	177,445	271,646	253,321	276,379	284,472
EBIT (%)	5.1	7.6	5.7	5.5	5.3
Net interest expenses	34,690	37,213	25,405	32,574	35,774
Other income	21,865	45,125	42,616	42,616	42,616
Other adjustments	(16,098)	-	-	-	-
Earnings before tax	180,718	279,558	270,533	286,421	291,314
Tax- total	56,584	75,704	86,905	91,392	92,402
Rate of tax (%)	31.3	27.1	32.1	31.9	31.7
Net profit	124,133	203,854	183,628	195,029	198,912

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Balance sheet

Y/E March (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Share capital	23,697	47,393	48,559	48,559	48,559
Reserves and surplus	876,099	973,568	827,370	875,186	933,886
Net worth	899,796	1,020,961	875,929	923,745	982,445
Loans	689,711	830,598	686,057	816,057	946,057
Minority interest	14,260	19,046	21,873	25,738	29,603
Deferred tax liability	69,708	68,887	97,558	98,258	98,958
Total capital employed	1,673,475	1,939,492	1,681,418	1,863,799	2,057,064
Net fixed assets	1,262,513	1,327,352	1,517,344	1,704,589	1,891,685
Goodwill	10	10	791	791	791
Investments	315,680	442,143	186,610	186,610	186,610
Current assets loans	737,350	966,105	1,131,451	1,200,201	1,259,694
Inventories	422,567	658,843	564,509	622,285	647,537
Debtors	76,845	88,992	108,253	118,717	126,512
Cash and bank	7,349	3,295	31,967	29,475	45,919
Loans and advances	120,506	93,254	310,984	320,984	330,984
Current investments	110,084	121,722	115,737	108,739	108,742
Less: Current liab. & prov.	642,080	796,119	1,154,778	1,228,392	1,281,716
Current liabilities	540,149	605,453	797,413	865,381	918,704
Provisions	101,931	190,665	357,365	363,011	363,011
Net current assets	95,270	169,986	(23,328)	(28,191)	(22,022)
Miscellaneous	-	-	-	-	-
Total capital employed	1,673,475	1,939,492	1,681,418	1,863,799	2,057,064

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Cash flow

Y/E March (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Profit after tax	124,133	203,854	183,628	195,029	198,912
Depreciation	56,984	68,486	67,605	67,755	67,905
Other income	(7,375)	69,421	(42,616)	(42,616)	(42,616)
Interest	13,963	10,768	25,405	32,574	35,774
Working capital changes	33,856	(76,220)	6,723	(4,628)	10,275
Others	34,682	5,370	700	700	700
Operating cash flow	256,242	281,680	241,444	248,814	270,950
Capital expenditure	(160,479)	(137,802)	(195,000)	(255,000)	(255,000)
Investments	2,241	(65,382)	-	-	-
Other income	22,134	26,821	42,616	42,616	42,616
Cash flow from investments	(136,104)	(176,363)	(152,384)	(212,384)	(212,384)
Equity	-	-	-	-	-
Debt	(44,699)	46,420	90,000	130,000	130,000
Interest expenses	(39,496)	(28,021)	(25,405)	(32,574)	(35,774)
Dividends	(34,703)	(127,768)	(124,986)	(136,348)	(136,348)
Cash flow from financing	(118,897)	(109,370)	(60,390)	(38,922)	(42,122)
Total cash generation	1,241	(4,053)	28,671	(2,492)	16,444
Opening cash balance	6,108	7,349	3,295	31,967	29,475
Closing cash & bank balance	7,349	3,295	31,967	29,475	45,919

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 (%)	6.8	9.6	7.2	6.9	6.6
EBIT margin (%)	5.13	7.65	5.65	5.54	5.34
Net profit margin (%)	3.5	5.6	4.0	3.8	3.7
RoE(%)	13.8	20.0	21.0	21.1	20.2
RoCE (%)	11.2	14.7	16.6	16.2	15.1
Working capital & liquidity ratios					
Receivables (days)	8	9	9	9	9
Inventory (days)	54	87	52	51	50
Payables (days)	69	80	73	71	70
Current ratio (x)	1.15	1.21	0.98	0.98	0.98
Valuation ratios					
EV/sales (x)	0.7	0.7	0.5	0.5	0.5
EV/EBITDA (x)	9.8	7.2	7.0	7.0	7.1
P/E (x)	12.9	7.9	8.7	8.2	8.1
P/BV (x)	1.8	1.6	1.8	1.7	1.6

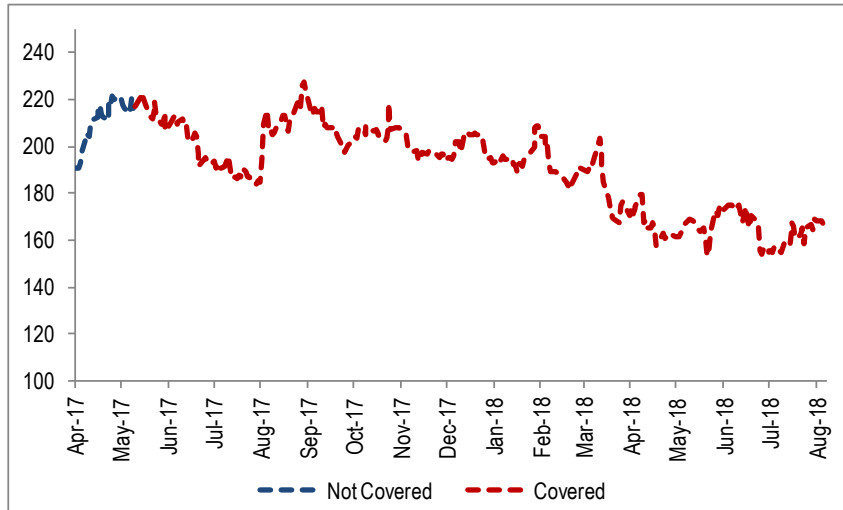
Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price	Target price (Rs)
12 May 2017	Sell	425	396
29 May 2017	Sell	425	396
4 August 2017	Sell	388	357
31 October 2017	Sell	414	357
1 February 2018	Accumulate	418	414
24 May 2018*	Sell	154	137
13 August 2018	Sell	161	137

*Price after 1:1 bonus issue

Rating track graph



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BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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