

Indian Oil Corporation

5 November 2018

Reuters: IOC.BO; Bloomberg: IOCL IN

Earnings Disappoint On Account Of Weak GRMs And One-Off Item

Indian Oil Corporation (IOCL) reported earnings of Rs33bn for 2QFY19, down 53.6% QoQ and 10.0% YoY, primarily because of: 1) Lower gross refining margin or GRM of US\$6.70/bbl in 2QFY19 versus US\$10.20/bbl in 1QFY19 and US\$7.84/bbl in 2QFY18, mainly on account of poor Singapore GRM and lower inventory gains of Rs20.8bn in 2QFY19 as compared to Rs58bn in 1QFY19 and Rs33.8bn in 2QFY18. 2) Employee benefit expenses at Rs38.3bn in 2QFY19 increased 53.3% QoQ and 62.1% YoY. However, further decline in earnings was mitigated by: 1) Rise in refining throughput to 17.82mmt in 2QFY19 as compared to 17.7mmt in 1QFY19 and 16.1mmt in 2QFY18. 2) Strong market sales of 19.82mmt in 2QFY19 as compared to 19mmt in 2QFY18.

The IOCL stock is under review and we will shortly come out with an update on our estimates and recommendation.

Revenues rise on account of higher crude oil prices and refinery throughput: IOCL's net sales at Rs1,549bn in 2QFY19 increased 2.1% QoQ and 40.1% YoY. Revenues increased because of: 1) Sharp rise in average crude oil price from US\$50/bbl in 2QFY18 and US\$72/bbl in 1QFY19 to US\$74/bbl in 2QFY19. 2) Rise in refinery throughput from 16.1mmt in 2QFY18 and 17.7mmt in 1QFY19 to 17.8mmt in 2QFY19. Rise in refinery throughput on YoY basis could be attributed to lower refining throughput in 2QFY18 on account of refinery shutdowns.

Lower inventory gains, weak GRM and higher employee expenses led to EBITDA decline: EBITDA stood at Rs72bn, down 1.9% YoY and 44.6% QoQ. Weak EBITDA performance was because of: 1) Lower GRM of US\$6.7/bbl in 2QFY19 versus US\$10.2/bbl in 1QFY19 and US\$7.84/bbl in 2QFY18. 2) Lower inventory gains of Rs20.8bn in 2QFY19 as compared to Rs58bn in 1QFY19 and Rs33.8bn in 2QFY18. 3) Employee benefit expenses at Rs38.3bn rose 53.3% QoQ and 63.3% YoY. Employee benefit expenses increased because of one-time contribution for the superannuation benefit scheme amounting to Rs12.6bn. EBITDA margin at 4.7% in 2QFY19 declined 199bps YoY and 393bps QoQ.

Higher finance costs and depreciation impacted earnings negatively: Interest expenses at Rs13.5bn in 2QFY19 increased 17.2% QoQ and 74.9% YoY. Depreciation and amortisation expenses rose 22.2% YoY to Rs20.7bn. Net profit stood at Rs33.2bn, down 10% YoY and 53.6% QoQ.

We will come out with our recommendation soon: Given our concerns on the rise in capex over the next five years, increase 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. However, we note that IOCL stock price has declined sharply in the recent past. The stock is under review and we will shortly come out with an update on our estimates and recommendation.

Under Review

Sector: Oil & Gas

CMP: Rs148

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Key Data

Current Shares O/S (mn)	9,711.8
Mkt Cap (Rsbn/US\$bn)	1439.8/19.9
52 Wk H / L (Rs)	214/105
Daily Vol. (3M NSE Avg.)	10,675,510

Price Performance (%)

	1 M	6 M	1 Yr
IOCL	(3.7)	(8.0)	(28.5)
Nifty Index	(4.1)	(1.5)	1.2

Source: Bloomberg

Y/E March (Rsmn)	2QFY19	1QFY19	QoQ (%)	2QFY18	YoY (%)	2QFY19E	Var. (%)
Net sales	1,549,689	1,518,138	2.1	1,106,371	40.1	1,526,715	1.5
Cost of goods	(1,316,001)	(1,258,208)	4.6	(933,683)	40.9	(1,302,274)	1.1
Employee benefit expenses	(38,320)	(25,003)	53.3	(23,640)	62.1	(25,754)	48.8
Other expenses	(122,999)	(104,304)	17.9	(75,315)	63.3	(107,433)	14.5
EBITDA	72,369	130,623	(44.6)	73,733	(1.9)	91,254	(20.7)
EBITDAM (%)	4.7	8.6	-	6.7	-	6.0	-
Depreciation and amortization	(20,743)	(19,614)	5.8	(16,970)	22.2	(19,791)	4.8
EBIT	51,626	111,009	(53.5)	56,763	(9.1)	71,463	(27.8)
EBITM (%)	3.3	7.3	-	5.1	-	4.7	-
Other income	10,940	8,473	29.1	5,878	86.1	8,477	29.1
Interest expenses	(13,512)	(11,530)	17.2	(7,726)	74.9	(11,587)	16.6
Extraordinary/exceptional items	-	-	-	-	-	-	-
Profit before tax	49,054	107,952	(54.6)	54,915	(10.7)	68,354	(28.2)
Tax expenses	(15,787)	(36,193)	-	(17,951)	-	(22,557)	-
<i>Effective tax rate (%)</i>	32%	34%	-	33%	-	33%	-
PAT	33,266	71,759	(53.6)	36,964	(10.0)	45,797	(27.4)

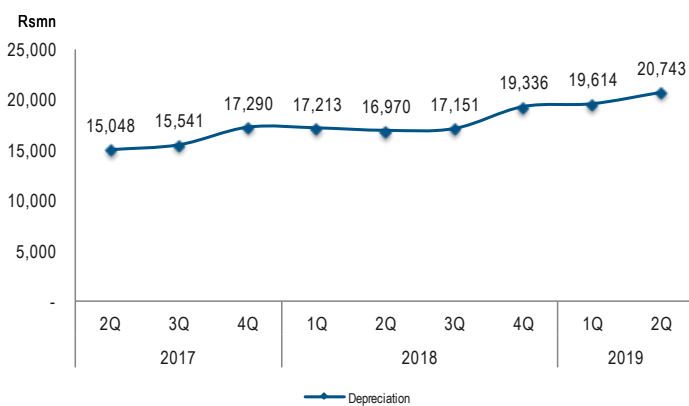
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 1: Key financials

Y/E March (Rsmn)	FY17	FY18	FY19E	FY20E	FY21E
Revenues	35,38,471	41,98,702	58,93,204	63,95,777	67,99,743
YoY (%)	2.3	18.7	40.4	8.5	6.3
EBITDA	3,40,425	4,15,976	3,62,453	3,62,238	3,50,920
YoY (%)	45.2	22.2	(12.9)	(0.1)	(3.1)
PAT	2,03,854	2,26,264	1,82,542	1,70,254	1,49,153
YoY (%)	64.2	11.0	(19.3)	(6.7)	(12.4)
EPS (Rs)	21.0	23.3	18.8	17.5	15.4
RoE (%)	20.0	19.9	15.4	14.0	12.1
EV/EBITDA (x)	3.6	3.0	3.9	4.3	4.8
P/E (x)	5.7	6.1	7.9	8.5	9.7

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)	FY17	FY18	FY19E	FY20E	FY21E
Net sales	35,38,471	41,98,702	58,93,204	63,95,777	67,99,743
Growth YoY (%)	2.3	18.7	40.4	8.5	6.3
Operating costs	29,29,421	35,64,753	52,92,580	57,77,365	61,76,528
Staff expenses	1,02,628	1,06,807	1,12,147	1,17,755	1,23,642
Other expenses	1,65,997	1,11,166	1,26,023	1,38,420	1,48,652
EBITDA	3,40,425	4,15,976	3,62,453	3,62,238	3,50,920
EBITDA growth (%)	45.2	22.2	(12.9)	(0.1)	(3.1)
EBITDA margin (%)	9.6	9.9	6.2	5.7	5.2
Depreciation	68,677	76,679	83,962	93,962	1,03,962
EBIT	2,71,748	3,39,297	2,78,492	2,68,277	2,46,959
EBIT (%)	7.7	8.1	4.7	4.2	3.6
Net interest expenses	37,213	38,105	48,657	56,783	67,811
Other income	27,432	31,749	42,616	42,616	43,469
Other adjustments	(17,591)	(11,562)	-	-	-
Earnings before tax	2,79,558	3,44,502	2,72,451	2,54,110	2,22,616
Tax- total	75,704	1,18,239	89,909	83,856	73,463
Rate of tax (%)	27.1	34.3	33.0	33.0	33.0
Net profit	2,03,854	2,26,264	1,82,542	1,70,254	1,49,153

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Balance sheet

Y/E March (Rsmn)	FY17	FY18	FY19E	FY20E	FY21E
Share capital	47,393	94,787	94,787	94,787	94,787
Reserves and surplus	9,73,568	10,43,951	10,89,049	11,21,859	11,33,568
Net worth	10,20,961	11,38,738	11,83,836	12,16,646	12,28,355
Loans	6,32,706	6,56,498	8,38,291	9,78,291	11,68,291
Minority interest	19,046	21,512	25,881	30,250	30,250
Deferred tax liability	68,887	1,23,679	1,24,379	1,25,079	1,25,079
Total capital employed	17,41,599	19,40,427	21,72,387	23,50,266	25,51,974
Net fixed assets	13,27,352	14,31,823	15,77,753	17,10,791	18,33,829
Goodwill	10	10	10	10	10
Investments	3,20,403	3,33,408	3,48,408	3,63,408	3,78,408
Current assets loans	10,87,845	11,91,481	13,13,327	13,96,523	15,16,216
Inventories	6,57,241	7,05,679	7,85,975	8,37,160	8,79,018
Debtors	88,992	1,06,965	1,40,730	1,52,294	1,58,772
Cash and bank	1,20,567	1,19,595	1,14,419	1,21,255	1,78,322
Loans and advances	28,644	28,308	29,723	31,209	32,770
Current investments	1,92,402	2,30,934	2,42,481	2,54,605	2,67,335
Less: Current liab. & prov.	9,94,011	10,16,296	10,67,111	11,20,466	11,76,490
Current liabilities	7,71,087	8,49,575	8,92,054	9,36,657	9,83,490
Provisions	2,22,925	1,66,721	1,75,057	1,83,810	1,93,000
Net current assets	93,834	1,75,185	2,46,216	2,76,056	3,39,727
Miscellaneous	-	-	-	-	-
Total capital employed	17,41,599	19,40,427	21,72,387	23,50,266	25,51,974

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Cash flow

Y/E March (Rsmn)	FY17	FY18	FY19E	FY20E	FY21E
Profit after tax	2,03,854	2,26,264	1,82,542	1,70,254	1,49,153
Depreciation	68,677	76,679	83,962	93,962	1,03,962
Other income	(45,023)	(43,310)	(42,616)	(42,616)	(43,469)
Interest	37,213	38,105	48,657	56,783	67,811
Working capital changes	11,136	(82,322)	(76,208)	(23,003)	(6,604)
Others	49,735	62,567	(4,190)	(1,300)	(6,369)
Operating cash flow	3,25,592	2,77,982	1,92,146	2,54,078	2,64,484
Capital expenditure	(1,34,238)	(1,80,274)	(2,25,000)	(2,25,000)	(2,25,000)
Investments	(78,936)	(13,005)	(15,000)	(15,000)	(15,000)
Other income	45,023	43,310	42,616	42,616	43,469
Cash flow from investments	(1,68,151)	(1,49,968)	(1,97,384)	(1,97,384)	(1,96,531)
Equity	-	-	-	-	-
Debt	47,191	23,792	1,81,793	1,40,000	1,90,000
Interest expenses	(37,213)	(38,105)	(48,657)	(56,783)	(67,811)
Dividends	(1,27,736)	(1,14,672)	(1,33,075)	(1,33,075)	(1,33,075)
Cash flow from financing	(1,17,758)	(1,28,985)	61	(49,858)	(10,886)
Total cash generation	39,683	(971)	(5,176)	6,837	57,067
Opening cash balance	80,884	1,20,567	1,19,595	1,14,419	1,21,255
Closing cash & bank balance	1,20,567	1,19,595	1,14,419	1,21,255	1,78,322

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 (%)	9.6	9.9	6.2	5.7	5.2
EBIT margin (%)	7.7	8.1	4.7	4.2	3.6
Net profit margin (%)	5.6	5.3	3.0	2.6	2.1
RoE (%)	20.0	19.9	15.4	14.0	12.1
RoCE (%)	17.7	20.2	14.6	12.9	11.1
Working capital & liquidity ratios					
Receivables (days)	9	9	9	9	9
Inventory (days)	82	72	54	53	52
Payables (days)	96	87	62	59	58
Current ratio (x)	1.1	1.2	1.2	1.2	1.3
Valuation ratios					
EV/sales (x)	0.3	0.3	0.2	0.2	0.2
EV/EBITDA (x)	3.6	3.0	3.9	4.3	4.8
P/E (x)	5.7	6.1	7.9	8.5	9.7
P/BV (x)	0.7	0.6	0.6	0.6	0.6

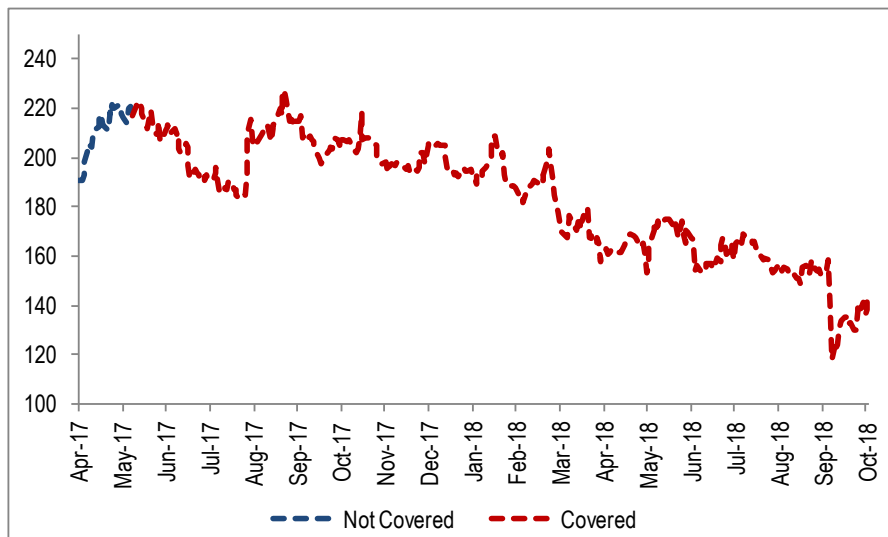
Source: Company, Nirmal Bang Institutional Equities Research

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
5 November 2018	Under Review	148	-

*Price after 1:1 bonus share issue

Rating track graph



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BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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