

BUY

TP: Rs 240 | ▲ 63%

INDIAN OIL CORP

Oil & Gas

01 November 2019

GRMs remain a drag, other segments outperform

IOCL's Q2FY20 EBITDA at Rs 36bn (-47% YoY) was well below estimates. Key Q2 highlights: (a) adj. GRM at US\$ 3.55/bbl disappointed, (b) adj. EBITDA for the marketing business beat estimates at Rs 41bn (Rs 1,900/mt); (c) pipeline/petchem EBITDA outperformed at Rs 16bn/Rs 7.7bn. We trim FY20/FY21/FY22 earnings by 12%/7%/8% on reduction in GRM estimates (by ~US\$ 1/bbl). Our Sep'20 TP stands revised to Rs 240 (from Rs 265). IOCL could gain the most from IMO 2020, which may fuel earnings upgrades.

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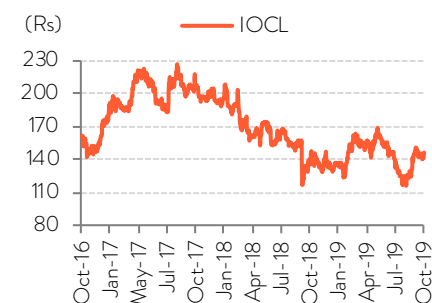
GRMs remain a drag; all hopes of recovery pinned on IMO: IOCL's GRMs (at US\$ 3.55/bbl) remain a drag on its earnings, underperforming the Singapore benchmark (US\$ 6.5/bbl). Low light-heavy crude spreads could be a major factor behind this underperformance. However, a relatively large diesel slate in IOCL's refining portfolio puts it in an advantageous position in the runup to IMO regulations (from Jan'20), which are expected to push diesel spreads above US\$ 20/bbl (from ~US\$ 14 currently).

Ticker/Price	IOCL IN/Rs 147
Market cap	US\$ 20.1bn
Shares o/s	9,712mn
3M ADV	US\$ 27.0mn
52wk high/low	Rs 171/Rs 116
Promoter/FPI/DII	51%/7%/41%

Source: NSE

Paradip utilisation normalises: Paradip refinery utilisation has normalised to ~100% now. Commissioning of the 680ktpa polypropylene (PP) facility in Jul'19 could enhance GRMs at the refinery.

STOCK PERFORMANCE



Marketing earnings improve: Marketing business EBITDA at Rs 41bn was in line with expectations, as IOCL gains traction in ATF and industrial product sales (while ceding bulk diesel market share to other players). Pipeline business EBITDA outperformed at Rs 16bn (flat YoY) on better volumes (21.8mmt, +2% YoY). Petchem margins beat estimates at US\$ 209/mt (-38% YoY). Petchem volumes remained muted at 0.53mmt (-20% YoY), but could improve on commissioning of the new PP plant at Paradip.

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	4,214,918	5,281,489	5,650,641	6,717,679	7,332,399
EBITDA (Rs mn)	416,275	352,227	365,139	428,493	464,442
Adj. net profit (Rs mn)	221,911	173,837	187,412	218,281	237,128
Adj. EPS (Rs)	23.4	18.9	20.4	23.8	25.8
Adj. EPS growth (%)	11.7	(19.1)	7.8	16.5	8.6
Adj. ROAE (%)	20.6	15.4	16.5	18.4	18.8
Adj. P/E (x)	6.3	7.8	7.2	6.2	5.7
EV/EBITDA (x)	4.9	5.8	6.4	5.2	5.0

Source: Company, BOBCAPS Research

BOB Capital Markets Ltd is a wholly owned subsidiary of Bank of Baroda

Important disclosures, including any required research certifications, are provided at the end of this report.



FIG 1 – IOCL SALES VOLUME GROWTH VS. INDUSTRY

Petroleum products (mmt)	IOCL Q2FY20 YoY growth (%)	Industry Q2FY20 YoY growth (%)	IOCL H1FY20 YoY growth (%)	Industry H1FY20 YoY growth (%)
LPG	11.3	9.6	5.3	4.3
MS	6.3	8.0	7.6	9.0
HSD	(2.1)	(0.2)	(0.5)	1.1
SKO	(30.2)	(31.5)	(21.3)	(22.4)
ATF	5.0	0.3	2.3	(0.5)
FO/LSHS	(6.9)	(3.6)	(4.8)	(4.6)
Others	8.0	(0.7)	0.3	(4.3)
Total	1.6	0.7	1.0	0.4

Source: Company, Industry, BOBCAPS Research

FIG 2 – QUARTERLY PERFORMANCE

Y/E Mar (Rs mn)	Q2FY20	Q2FY19	YoY (%)	Q1FY20	QoQ (%)	H1FY20	H1FY19	YoY (%)
Net sales	11,16,897	13,20,348	(15.4)	13,15,125	(15.1)	24,32,021	26,15,098	(7.0)
EBITDA	35,722	67,620	(47.2)	83,500	(57.2)	1,19,222	1,93,378	(38.3)
EBITDA margin (%)	3.20	5.12	-	6.35	-	4.90	7.39	-
Adjusted EBITDA	65,330	60,150	8.6	76,570	(14.7)	1,41,900	1,31,140	8.2
Depreciation and Amortisation	20,975	18,091	15.9	20,929	0.2	41,904	35,970	16.5
Interest	13,083	11,878	10.1	15,091	(13.3)	28,173	22,189	27.0
Other income	6,481	10,407	(37.7)	6,314	2.6	12,794	16,260	(21.3)
PBT	8,145	48,057	(83.1)	53,794	(84.9)	61,939	1,51,479	(59.1)
Provision for tax	2,511	15,588	(83.9)	17,833	(85.9)	20,344	50,699	(59.9)
Effective Tax Rate (%)	30.82	32.44	-	33.15	-	32.84	33.47	-
Adjusted PAT	5,634	32,469	(82.6)	35,961	(84.3)	41,595	1,00,781	(58.7)
Other comprehensive income	(39,617)	17,849	-	6,272	731.6	-	(2,598)	-
Total income	(33,983)	50,319	-	42,233	(180.5)	41,595	98,183	(57.6)
NPM (%)	0.50	2.46	-	2.73	-	1.71	3.85	-
EPS (Rs)	0.6	3.4	(82.5)	3.8	(84.3)	4.4	10.6	(58.7)

Source: Company, BOBCAPS Research

FIG 3 – SEGMENT PERFORMANCE

	Q2FY20	Q2FY19	YoY (%)	Q1FY20	QoQ (%)	H1FY20	H1FY19	YoY (%)
Refining								
Refining throughput (mmt)	17.54	17.82	(1.6)	17.30	1.4	34.84	35.48	(1.8)
GRM (US\$/bbl)	1.28	6.79	(81.1)	4.69	(72.7)	2.96	8.45	(65.0)
Normalised GRM (US\$/bbl)	3.55	5.14	(30.9)	3.60	(1.3)	3.57	4.81	(25.8)
Refining EBITDA (Rs mn)	(20,270)	20,800	-	16,590	-	(3,680)	78,970	-
Refining EBITDA (US\$/bbl)	(2.2)	2.3	-	1.9	-	(0.2)	4.4	-
Inventory gains/(loss) (Rs mn)	(15,340)	30,160	-	9,770	-	(5,570)	89,340	-
Inventory gains/(loss) (US\$/bbl)	(1.7)	3.3	-	1.1	-	(0.3)	5.0	-
Exchange fluctuation gain/(loss) (Rs mn)	(5,200)	(15,040)	65.4	(120)	-	(5,320)	(24,380)	-
Adj. EBITDA	270	5,680	(95.2)	6,940	(96.1)	7,210	14,010	(48.5)
Adj. EBITDA (US\$/bbl)	0.0	0.6	(95.2)	0.8	(96.2)	0.4	0.8	(48.6)
Operating costs (US\$/bbl)	2.9	2.9	2.4	2.8	5.3	2.9	2.7	8.0

	Q2FY20	Q2FY19	YoY (%)	Q1FY20	QoQ (%)	H1FY20	H1FY19	YoY (%)
Marketing								
Total Marketing sales (mmt)	21.42	20.40	5.0	21.60	(0.8)	43.03	42.08	2.3
Domestic	18.95	18.65	1.6	20.52	(7.6)	39.47	39.10	1.0
Exports	1.25	1.75	(28.7)	1.08	15.0	2.31	2.98	(22.4)
Marketing EBITDA (Rs mn)	38,130	42,100	(9.4)	45,650	(16.5)	83,780	85,790	(2.3)
Marketing EBITDA (Rs/mt)	1,780	2,064	(13.8)	2,113	(15.8)	1,947	2,039	(4.5)
Inventory gains/(loss) (Rs mn)	3,560	13,920	(74.4)	2,560	39.1	6,120	33,400	(81.7)
Inventory gains/(loss) (Rs/mt)	166	682	(75.7)	118	40.2	142	794	82.1
Exchange fluctuation gain/(loss) (Rs mn)	(6,150)	(11,160)	44.9	1,040	691.3	(5,110)	(19,870.0)	(74.3)
Adj. EBITDA	40,720	39,340	3.5	42,050	(3.2)	82,770	72,260	14.5
Adj. EBITDA (Rs/mt)	1,901	1,929	(1.5)	1,946	(2.3)	1,924	1,717	12.0
Pipeline								
Pipeline throughput (mmt)	21.75	21.37	1.8	21.90	(0.7)	43.65	44.22	(1.3)
Pipeline EBITDA (Rs mn)	15,870	16,100	(1.4)	16,230	(2.2)	32,100	32,370	(0.8)
Pipeline EBITDA (Rs/mt)	730	754	(3.2)	741	(1.5)	735	732	0.5
Petrochemicals								
Volumes (mmt)	0.53	0.66	(20.2)	0.53	-	1.05	1.30	(18.9)
Petrochemicals EBITDA (Rs mn)	7,740	15,620	(50.4)	6,860	12.8	14,600	31,920	(54.3)
Petrochemicals EBITDA (US\$/mt)	209	338	(38.1)	187	11.5	198	359	(44.8)
Others (Rs mn)	730	(16,590)	-	4,490	83.7	5,220	(19,420)	-
Total Adjusted EBITDA (Rs mn)	65,330	60,150	8.6	76,570	(14.7)	1,41,900	1,31,140	8.2

Source: Company, BOBCAPS Research

Valuation methodology

Diversified earnings give IOCL a big advantage over peers. At 7x/6x FY21E/FY22E EPS, valuations look attractive given improving ROE over the next three years. Lower exposure to the marketing business renders IOCL's earnings more resilient than peers. Maintain BUY.

We trim FY20/FY21/FY22 earnings estimates by 12%/7%/8% on reduction in GRM assumptions (by ~US\$ 1/bbl). Our Sep'20 SOTP-based target price stands revised to Rs 240 (from Rs 265). IOCL could gain the most from IMO 2020 regulations, which may fuel earnings upgrades

Our SOTP valuation comprises the following:

- Refining business valued at 6.5x Sep'21E EBITDA,
- Marketing business valued at 5x Sep'21E EBITDA,
- Petrochemicals business valued at 7.5x Sep'21E EBITDA, and
- Pipeline business at 5x Sep'21E EBITDA.

FIG 4 – SOTP VALUATION SUMMARY

	EV (Rs bn)	Value (Rs/sh)	Comments
Refining	892	97	6.5x Sep'21E EBITDA
Marketing	789	86	5x Sep'21E EBITDA
Petrochemicals	474	52	7.5x Sep'21E EBITDA
Pipeline	411	45	5x Sep'21E EBITDA
Total core business EV	2,566	242	-
Less: Net Debt	514	56	-
Equity value of operational segments	2,052	223	-
Add: Total investments	153	18	Listed holdings at 20% discount to CMP and others at investment value
IOCL Equity value	2,205	240	~9.3x FY22E EPS

Source: BOBCAPS Research

FIG 5 – REVISED ESTIMATES

(Rs mn)	FY20E			FY21E			FY22E		
	Old	New	Var (%)	Old	New	Var (%)	Old	New	Var (%)
Revenue	56,81,340	56,50,641	(0.5)	67,36,189	67,17,679	(0.3)	73,56,318	73,32,399	(0.3)
EBITDA	3,99,236	3,65,139	(8.5)	4,24,061	4,48,514	5.8	4,65,420	4,89,873	5.3
EBITDA margin (%)	7.0	6.5	-	6.3	6.7	-	6.3	6.7	-
PAT	2,12,916	1,87,412	(12.0)	2,34,175	2,18,281	(6.8)	2,57,917	2,37,128	(8.1)
EPS (Rs)	23.2	20.4	(12.0)	25.5	23.8	(6.8)	28.1	25.8	(8.1)

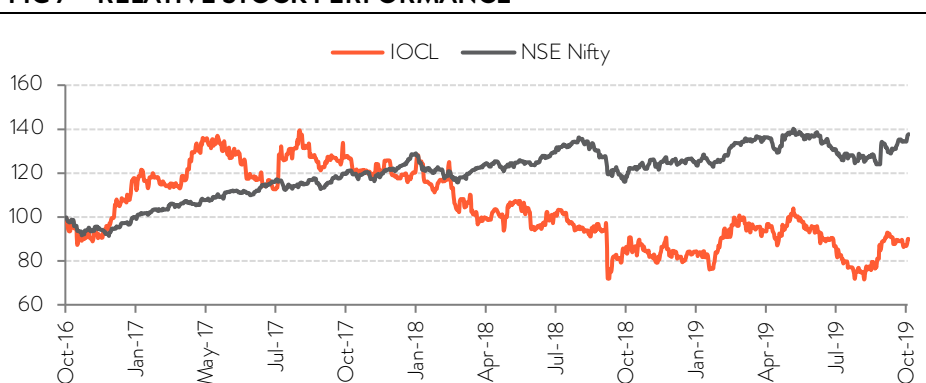
Source: BOBCAPS Research

FIG 6 – KEY ASSUMPTIONS

	FY20E	FY21E	FY22E
Average petchem product spreads (US\$/mt)	600	700	700
Oil (US\$/bbl)	75.0	80.0	80.0
GRMs (US\$/bbl)	5.0	6.0	6.0
Singapore GRMs (US\$/bbl)	5.0	5.5	5.5
Refinery throughput (mmt)	76.8	81.8	86.8
Pipeline throughput (mmt)	100.1	107.3	114.5
Market sales (mmt)	86.9	90.7	94.8
USDINR	72.0	74.0	74.0

Source: BOBCAPS Research

FIG 7 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- IOCL’s earnings are sensitive to GRMs and marketing margins on product sales. These tend to be more volatile for the company considering its high inventory days.
- Further market share losses on fuel product sales could result in below-expected volumes and affect marketing business earnings.
- Adverse pipeline tariff orders or regulations by PNGRB mandating third-party use of IOCL’s pipelines could hurt pipeline business earnings.
- Below-expected petrochemical spreads would hit profitability of the business

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue	4,214,918	5,281,489	5,650,641	6,717,679	7,332,399
EBITDA	416,275	352,227	365,139	428,493	464,442
Depreciation	(76,635)	(85,065)	(85,739)	(94,368)	(102,422)
EBIT	339,640	267,162	279,400	334,125	362,021
Net interest income/(expenses)	(38,448)	(48,880)	(66,003)	(82,082)	(90,590)
Other income/(expenses)	34,199	27,143	39,207	41,651	47,295
EBT	335,391	245,425	252,605	293,693	318,726
Income taxes	(118,239)	(86,531)	(63,651)	(74,006)	(80,315)
Min. int./Inc. from associates	4,759	14,942	(1,541)	(1,407)	(1,283)
Reported net profit	221,911	173,837	187,412	218,281	237,128
Adjusted net profit	221,911	173,837	187,412	218,281	237,128

Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Accounts payables	365,817	411,941	457,191	545,694	596,031
Other current liabilities	513,541	573,909	602,973	718,582	786,728
Provisions	166,721	123,860	183,452	213,741	232,241
Debt funds	626,750	933,278	835,785	985,906	1,025,451
Other liabilities	123,679	165,097	158,231	158,231	158,231
Equity capital	94,787	91,810	91,810	91,810	91,810
Reserves & surplus	1,043,951	1,032,882	1,054,237	1,129,941	1,212,487
Shareholders' fund	1,138,738	1,124,692	1,146,048	1,221,752	1,304,297
Total liabilities and equities	2,956,757	3,351,551	3,436,804	3,875,741	4,137,510
Cash and cash eq.	4,963	10,647	53,648	76,114	90,101
Accounts receivables	106,965	157,977	173,579	206,041	224,567
Inventories	705,679	771,265	781,667	935,833	1,026,930
Other current assets	259,256	364,641	368,466	439,029	480,547
Investments	448,061	439,277	497,616	577,616	577,616
Net fixed assets	1,280,970	1,373,725	1,334,022	1,377,247	1,437,830
CWIP	150,853	234,010	227,796	263,851	299,908
Intangible assets	10	10	10	10	10
Total assets	2,956,757	3,351,551	3,436,804	3,875,741	4,137,510

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Net income + Depreciation	298,546	258,901	273,151	312,648	339,550
Changes in working capital	(53,147)	(158,351)	104,076	(22,791)	(14,158)
Other operating cash flows	20,593	14,276	(46,074)	(41,651)	(47,295)
Cash flow from operations	265,992	114,826	331,154	248,207	278,097
Capital expenditures	(104,472)	(175,911)	45,917	(79,281)	(96,640)
Change in investments	(11,188)	8,784	(58,339)	(80,000)	0
Other investing cash flows	34,199	27,143	39,207	41,651	47,295
Cash flow from investing	(81,461)	(139,985)	26,785	(117,630)	(49,345)
Equities issued/Others	47,394	(2,977)	0	0	0
Debt raised/repaid	(5,957)	306,528	(97,492)	150,120	39,546
Dividends paid	(136,949)	(127,679)	(142,527)	(166,002)	(180,336)
Other financing cash flows	(88,154)	(145,030)	(74,017)	(92,711)	(74,133)
Cash flow from financing	(183,666)	30,842	(314,036)	(108,593)	(214,923)
Changes in cash and cash eq.	865	5,683	43,903	21,984	13,829
Closing cash and cash eq.	4,963	10,647	54,550	75,632	89,942

Per Share

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20E	FY21E	FY22E
Reported EPS	23.4	18.9	20.4	23.8	25.8
Adjusted EPS	23.4	18.9	20.4	23.8	25.8
Dividend per share	12.0	11.5	13.3	15.5	16.8
Book value per share	120.1	122.5	124.8	133.1	142.1

Valuations Ratios

Y/E 31 Mar (x)	FY18A	FY19A	FY20E	FY21E	FY22E
EV/Sales	0.5	0.4	0.4	0.3	0.3
EV/EBITDA	4.9	5.8	6.4	5.2	5.0
Adjusted P/E	6.3	7.8	7.2	6.2	5.7
P/BV	1.2	1.2	1.2	1.1	1.0

DuPont Analysis

Y/E 31 Mar (%)	FY18A	FY19A	FY20E	FY21E	FY22E
Tax burden (Net profit/PBT)	66.2	70.8	74.2	74.3	74.4
Interest burden (PBT/EBIT)	98.7	91.9	90.4	87.9	88.0
EBIT margin (EBIT/Revenue)	8.1	5.1	4.9	5.0	4.9
Asset turnover (Revenue/Avg TA)	148.1	167.4	166.5	183.7	183.0
Leverage (Avg TA/Avg Equity)	2.6	2.8	3.0	3.1	3.2
Adjusted ROAE	20.6	15.4	16.5	18.4	18.8

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
YoY growth (%)					
Revenue	18.6	25.3	7.0	18.9	9.2
EBITDA	22.5	(15.4)	3.7	17.4	8.4
Adjusted EPS	11.7	(19.1)	7.8	16.5	8.6
Profitability & Return ratios (%)					
EBITDA margin	9.9	6.7	6.5	6.4	6.3
EBIT margin	8.1	5.1	4.9	5.0	4.9
Adjusted profit margin	5.3	3.3	3.3	3.2	3.2
Adjusted ROAE	20.6	15.4	16.5	18.4	18.8
ROCE	12.7	9.0	10.2	11.7	11.8
Working capital days (days)					
Receivables	8	9	11	10	11
Inventory	74	61	58	53	55
Payables	33	29	30	29	30
Ratios (x)					
Gross asset turnover	2.5	3.4	3.2	3.5	3.6
Current ratio	0.7	0.8	0.8	0.8	0.9
Net interest coverage ratio	8.8	5.5	4.2	4.1	4.0
Adjusted debt/equity	0.5	0.8	0.7	0.7	0.7

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

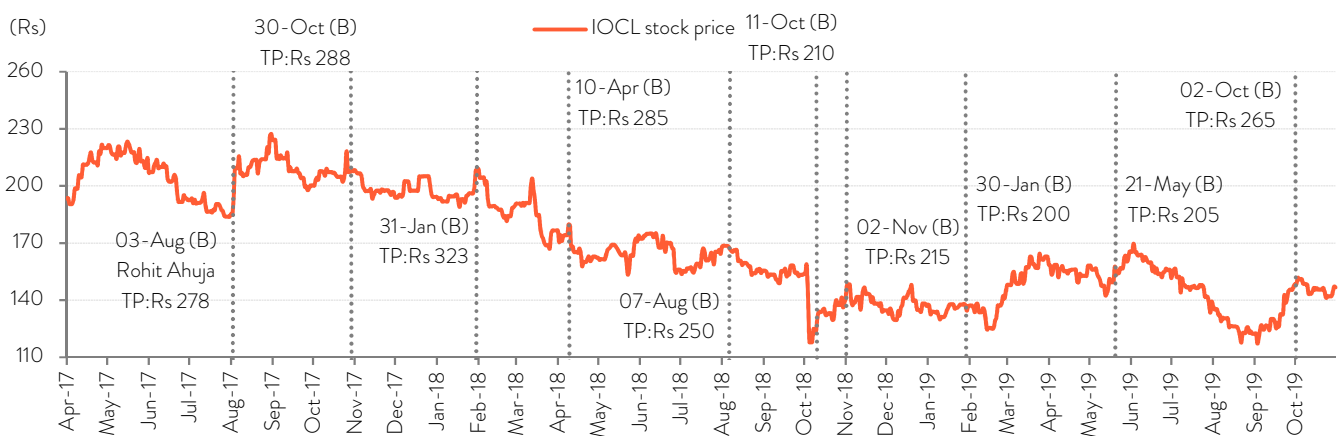
ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

HISTORICAL RATINGS AND TARGET PRICE: INDIAN OIL CORP (IOCL IN)



B – Buy, A – Add, R – Reduce, S – Sell

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