

HPCL

BUY

Higher inventory gains led profits; multiple triggers ahead

Summary

HPCL's Q3FY21 result was a beat to our and consensus forecast at all parameters primarily led by higher inventory gains and lower interest costs and higher other income. Reported GRM came at US\$1.9/bbl but after adjusting to inventory gains it comes to -US\$1/bbl, below our estimate. Petroleum product sales volume/crude throughput declined 2%/4% YoY to 10.4/4.0mmt. However, strong marketing margin on auto fuels led growth during the quarter. HPCL has guided for addition of 2mmt of refining capacity at Mumbai from CY22 and ~5mmt refining capacity by end CY21. Also, it expects Rajasthan Refinery of 9mmt to complete by CY23 and Chhara LNG terminal by CY22. We expect HPCL to benefit from higher throughput and GRM in FY22/23 along with stable marketing margin. To factor the beat and lower interest costs, we raise EBITDA for FY21/22/23 by 11.9%/7.4%/11.1% respectively and raise our TP to Rs285. Maintain BUY.

Key Highlights and Investment Rationale

Higher inventory gains and lower finance costs improves profit

The company reported inventory gains of Rs13.2bn (Rs 6.1bn on crude and Rs 7.1bn on products), ahead of our expectation. Lower cracks across products led to losses in refining segment. However, interest cost was significantly lower by 50% QoQ due to a) lower debt and b) forex gains led by rupee appreciation. Also, other income grew 77% YoY to Rs5.7 bn which propelled net profit 215% YoY to Rs235 bn, above our estimates.

Timeline visibility of capacity expansion across refining units

Management guided for expansion at its Mumbai refinery to be completed by Q1FY22 to 9.5mmt from current 7.5mmt while Vizag refinery is expected to be completed by CY21 to 15mmt from current 8.3mmt. This will increase the total capacity of both the plants to 24.5mmt from 15.8mmt currently. Further, 9mmt Rajasthan refinery is expected to be completed by 2023 while Chhara LNG terminal to commission by CY22. Company has guided for a capex of Rs120 bn for FY21 (Rs88 bn already invested) and Rs 140bn for FY22 (Rs 50bn for Marketing, Rs 55bn for refinery and R&D, Rs 20bn for CGD and Rs 15bn for JV & subsidiaries).

Raise TP to 285; Maintain BUY

The company completed 35% of buyback announced till Jan'21 and purchased back 40.7mn shares at Rs8.8 bn. Monetization of Pipeline assets, narrowing gap between refining and marketing volumes, upcoming petchem capacity at HMEL and Rajasthan along with growing LNG portfolio are few key triggers. We maintain BUY with a revised SOTP based TP of Rs285 (Rs 251 for core business at EV/EBITDA and Rs35 for its investments in MRPL and Oil India).

TP	Rs285
CMP	Rs225
Potential upside / downside	+26%
Previous Rating	BUY

V/s Consensus

EPS (Rs)	FY21E	FY22E	FY23E
IDBI Capital	57.5	42.7	44.3
Consensus	40.2	41.5	48.8
% difference	43.0	2.9	(9.2)

Shareholding Pattern (%)

Promoters	51.6
FII	15.9
DII	20.7
Public	11.8

Price Performance (%)

	-1m	-3m	-12m
Absolute	1.0	20.6	(2.7)
Rel to Sensex	(4.3)	(4.3)	(27.1)

Q3FY21 Result Review

Key Stock Data

Bloomberg / Reuters	HPCL IN / HPCL.BO
Sector	Oil & Gas
Shares o/s (mn)	1,483
Market cap. (Rs mn)	3,34,146
Market cap. (US\$ mn)	4,582
3-m daily avg Trd value (Rs mn)	838.8
52-week high / low	Rs 245 / 155
Sensex / Nifty	50,732 / 14,924

Relative to Sensex (%)



Financial snapshot

Year	FY19	FY20	FY21E	FY22E	FY23E
Revenue	2,739,809	2,675,998	2,276,981	3,068,908	4,162,011
EBITDA	120,209	59,975	133,952	116,930	123,671
EBITDA (%)	4.4	2.2	5.9	3.8	3.0
Adj. PAT	60,287	33,319	87,617	65,102	67,455
EPS (Rs)	39.6	21.9	57.5	42.7	44.3
EPS Growth (%)	(5.2)	(44.7)	163.0	(25.7)	3.6
PE (x)	5.8	10.5	4.0	5.4	5.2
Dividend Yield (%)	6.9	4.2	10.0	7.4	7.7
EV/EBITDA (x)	4.8	11.3	5.0	6.3	6.6
RoE (%)	23.1	11.7	28.0	18.5	17.4
RoCE (%)	12.8	3.1	10.0	7.0	6.2

Source: Company; IDBI Capital Research

Concall highlights:

- **Petroleum products:** Expect 4-5% growth in Q4 which will translate to 94-95% of FY20 sales on a full year basis.
- **New Outlets:** Commissioned 1,543 new retail outlets and expect 2000 outlets to open in FY21 and similarly in FY22. Total RO's currently stands at 18,019. Further, 77 new LPG dealership added in Q3FY21 reaching to 6,160. Company started dispensing CNG in 170 new outlets during Q3 which reached to a total of 650 outlets. Also HPCL now operates EV charging facility of 51 outlets.
- **Capex:** For FY21, Rs 120bn of capex was planned, of which Rs 88bn is already completed. For FY22, Rs 140bn is planned. Ou of which, Rs 50bn for Marketing, Rs 55bn for refinery and R&D, Rs 20bn for CGD and Rs 15bn for JV & subsidiaries.
- **Expansion plan:** Mumbai refining capacity expansion of 2mmt in Q1FY22 to reach to 9.5mmt while Vizag refining capacity expansion to complete by CY21 (except bottom up-gradation unit) which would increase the total capacity to 14mmt and bottom up-gradation unit is likely to be over by Q2CY21 which would enhance the total capacity to 15mmt. This would result in higher GRM as well. Rajasthan refinery to be complete by CY23 while Chhara LNG terminal to complete by CY22.

Further, Petrochemical unit at HMEL to complete by CY22 and Rajasthan refining unit will have 35% linkages to the petrochemicals.
- **Post expansion volumes:** Post expansion, in 2024, HPCL would operate with a total capacity of 44.8mmt while current sales volume is nearly 40-41mmt. In 2024, difference in refining and sales volume to remain higher.
- **Buyback programme:** Company has already done 35% of the buyback worth Rs 8.85bn i.e. 4.07crs shares.
- **Pipeline:** Monetization – Currently total pipeline of 3700kms while construction is ongoing for 1,600kms. Looking for various ways to create value for these assets.
- **Rajasthan Refinery:** Project will be completed by 2023, where HPCL holds 74% stake. Total project cost, as per earlier plan, is around Rs430bn funded in the ratio of D/E of 2:1, which will be reviewed after some time. Total equity contribution is Rs 100bn of which Rs 40bn is already contributed. Crude mix is designed so that it can use 2.5mmt of Rajasthan crude and rest imported crude
- **Chhara LNG terminal:** Completion is expected by end of 2022. HPCL has not signed any contrac tofr third party offtake as it already has huge requirement of gas.
- **Govt. dues:** As of March '20 subsidy was around Rs 80bn which has come down to Rs 40bn as of Jan '21.

Exhibit 1: Actual vs estimates

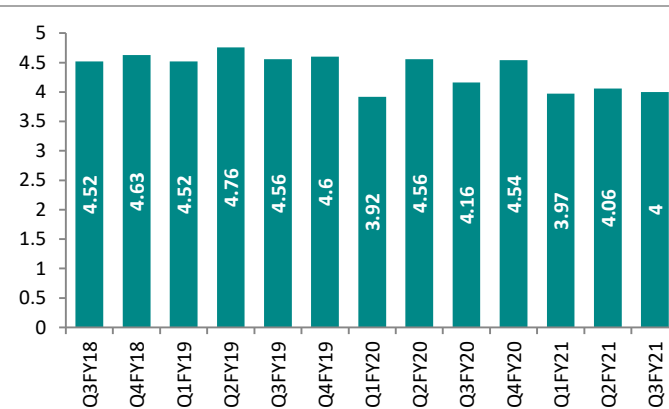
(Rs mn)	Actual	Estimated	% Variance
Net sales	686,592	614,210	11.8
EBITDA	33,015.2	28,386.0	16.3
EBITDA margin (%)	4.8	4.6	18.7bps
Adj net income	23,546	14,366	63.9
FDEPS (Rs)	15.5	9.4	63.9

Source: Company; IDBI Capital Research

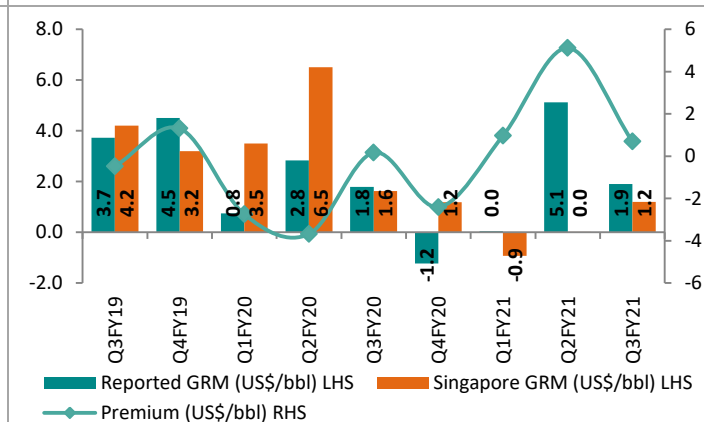
Exhibit 2: Change in estimates

Key parameters (Rs mn)	FY21E			FY22E			FY23E		
	Old	New	% Chg	Old	New	% Chg	Old	New	% Chg
Revenue	1,829,009	2,276,981	24.5	2,384,011	3,068,908	28.7	2,908,622	4,162,011	43.1
EBITDA	119,663	133,952	11.9	108,834	116,930	7.4	111,338	123,671	11.1
EBITDA margin (%)	6.5	5.9	(66)	4.6	3.8	(76)	3.8	3.0	(86)
Net profit	73,708	87,617	18.9	59,448	65,102	9.5	59,258.0	67,455	13.8
FDEPS (Rs)	48.4	57.5	18.9	39.0	42.7	9.5	38.9	44.3	13.8

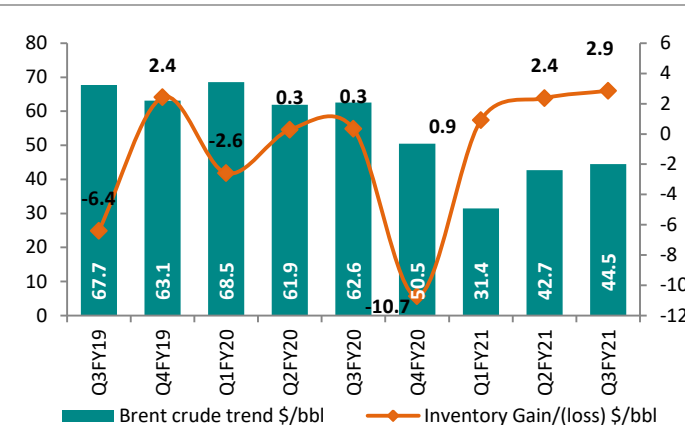
Source: Company, IDBI Capital Research

Exhibit 3: Refining Throughput (mmt)


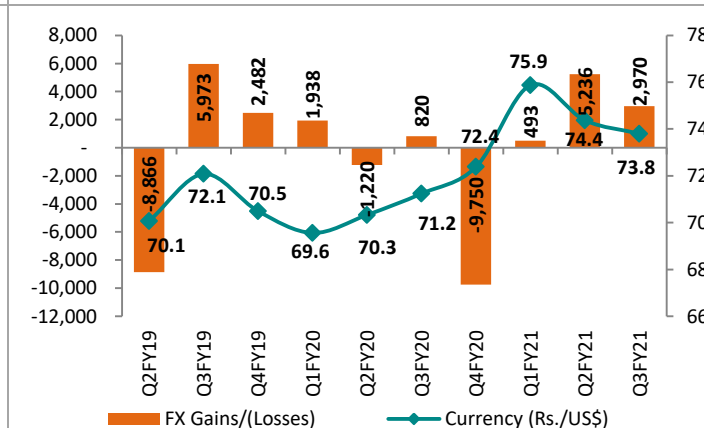
Source: Company; IDBI Capital Research

Exhibit 4: Reported GRM & Premium (\$/bbl)


Source: Company; IDBI Capital Research

Exhibit 5: Brent crude trend & Inventory gains/(losses)


Source: Company; IDBI Capital Research

Exhibit 6: FX gains/(losses) & currency movement


Source: Company; IDBI Capital Research

Exhibit 7: Quarterly highlights

(Rs mn)

	Q3FY20	Q4FY20	Q1FY21	Q2FY21	Q3FY21	% Chg YoY	% Chg QoQ
Net sales	707,496	661,549	377,209	517,733	686,592	-3.0%	33%
Expenditure	688,827	658,865	333,672	481,694	653,577	-5%	36%
EBITDA	18,669	2,684	43,536	36,039	33,015	77%	-8%
<i>EBITDA margin (%)</i>	2.6	0.4	11.5	7.0	4.8	217bps	-215bps
Depreciation	8,659	8,114	8,661	8,683	8,811	2%	1%
EBIT	10,011	(5,430)	34,875	27,356	24,205	142%	-12%
Interest	2,524	3,374	3,217	2,604	1,274	-50%	-51%
Other income	3,202	4,241	5,133	2,932	5,678	77%	94%
Fx gains/(losses)	820	(9,750)	493	5,236	2,970	262%	-43%
PBT (before exceptional items)	11,508	(14,313)	37,284	32,920	31,579	174%	-4%
Exceptional items	--	(10,029)	--	--	--	--	--
PBT (before exceptional items)	11,508	(24,343)	37,284	32,920	31,579	174%	-4%
Tax	4,036	(24,611)	9,146	8,146	8,032	99%	-1%
Reported PAT	7,472	268	28,138	24,775	23,546	215%	-5%
Adjustments	--	(8,762)	--	--	--	--	--
Adjusted PAT	7,472	(8,494)	28,138	24,775	23,546	215%	-5%
Adjusted EPS (Rs)	4.9	(5.6)	18.5	16.3	15.45	215%	-5%
Crude throughput (MMT)	4.2	4.5	4.0	4.1	4.00	-4%	-1%
Product sales (MMT)	10.6	9.6	7.6	8.4	10.40	-2%	23%
Reported GRM (US\$/bbl)	1.8	(1.2)	0.0	5.1	1.90	6%	-63%
Core GRM (US\$/bbl)	1.4	9.5	(0.9)	2.8	(0.96)	--	--

Source: Company; IDBI Capital Research

Financial Summary

Profit & Loss Account

(Rs mn)

Year-end: March	FY20	FY21E	FY22E	FY23E
Net sales	2,675,998	2,276,981	3,068,908	4,162,011
<i>growth (%)</i>	<i>(2.3)</i>	<i>(14.9)</i>	<i>34.8</i>	<i>35.6</i>
Operating expenses	(2,627,690)	(2,155,279)	(2,964,840)	(4,051,845)
EBITDA	59,975	133,952	116,930	123,671
<i>growth (%)</i>	<i>(50.1)</i>	<i>123.3</i>	<i>(12.7)</i>	<i>5.8</i>
Depreciation	(33,044)	(35,016)	(41,388)	(49,268)
EBIT	26,931	98,935	75,542	74,403
Interest paid	(10,817)	(9,116)	(10,555)	(12,280)
Other income	9,642	27,003	21,816	27,817
Pre-tax profit	15,726	116,823	86,803	89,940
Tax	10,647	(29,206)	(21,701)	(22,485)
<i>Effective tax rate (%)</i>	<i>(67.7)</i>	<i>25.0</i>	<i>25.0</i>	<i>25.0</i>
Minority Interest	-	-	-	-
Net profit	26,373	87,617	65,102	67,455
Exceptional items	(6,946)	-	-	-
Adjusted net profit	33,319	87,617	65,102	67,455
<i>growth (%)</i>	<i>(44.7)</i>	<i>163.0</i>	<i>(25.7)</i>	<i>3.6</i>
<i>Shares o/s (mn nos)</i>	<i>1,524</i>	<i>1,524</i>	<i>1,524</i>	<i>1,524</i>

Cash Flow Statement

(Rs mn)

Year-end: March	FY20	FY21E	FY22E	FY23E
Pre-tax profit	15,726	116,823	86,803	89,940
Depreciation	33,044	35,016	41,388	49,268
Tax paid	(17,229)	(26,056)	(18,519)	(19,272)
Chg in working capital	8,607	33,911	(30,253)	(45,547)
Other operating activities	14,386	(9,187)	(6,261)	(10,538)
Cash flow from operations (a)	54,533	150,507	73,158	63,853
Capital expenditure	(137,847)	(100,000)	(120,000)	(120,000)
Chg in investments	(9,319)	(1,251)	(1,804)	(1,832)
Other investing activities	5,509	18,303	16,816	22,817
Cash flow from investing (b)	(141,657)	(82,948)	(104,988)	(99,015)
Equity raised/(repaid)	-	-	-	-
Debt raised/(repaid)	114,340	-	75,000	70,000
Dividend (incl. tax)	(17,251)	(42,056)	(31,249)	(32,379)
Chg in minorities	-	-	-	-
Other financing activities	(9,790)	(9,116)	(10,555)	(12,280)
Cash flow from financing (c)	87,299	(51,172)	33,196	25,342
Net chg in cash (a+b+c)	175	16,387	1,366	(9,820)

Balance Sheet

(Rs mn)

Year-end: March	FY20	FY21E	FY22E	FY23E
Net fixed assets	654,341	719,325	797,937	868,668
Investments	71,667	72,384	73,108	73,839
Other non-curr assets	41,174	41,586	42,002	42,422
Current assets	372,926	342,654	438,973	559,805
Inventories	191,412	163,036	219,480	297,375
Sundry Debtors	39,227	33,412	44,979	60,943
Cash and Bank	1,132	17,518	18,884	9,064
Marketable Securities	53,449	53,983	55,063	56,164
Loans and advances	83,447	71,076	95,683	129,642
Total assets	1,140,108	1,175,948	1,352,020	1,544,734
Shareholders' funds	289,624	335,184	369,038	404,114
Share capital	15,242	15,242	15,242	15,242
Reserves & surplus	274,382	319,942	353,796	388,872
Total Debt	384,330	384,330	459,330	529,330
Secured loans	222,872	239,018	328,549	411,627
Unsecured loans	161,458	145,312	130,781	117,703
Other liabilities	290,927	298,812	306,824	314,965
Curr Liab & prov	175,229	157,622	216,828	296,324
Current liabilities	145,744	133,439	183,561	250,860
Provisions	29,484	24,184	33,267	45,464
Total liabilities	850,485	840,764	982,982	1,140,620
Total equity & liabilities	1,140,108	1,175,948	1,352,020	1,544,734
Book Value (Rs)	190	220	242	265

Source: Company; IDBI Capital Research

Financial Ratios

Year-end: March	FY20	FY21E	FY22E	FY23E
Adj. EPS (Rs)	21.9	57.5	42.7	44.3
Adj EPS growth (%)	(44.7)	163.0	(25.7)	3.6
EBITDA margin (%)	2.2	5.9	3.8	3.0
Pre-tax margin (%)	0.6	5.1	2.8	2.2
ROE (%)	11.7	28.0	18.5	17.4
ROCE (%)	3.1	10.0	7.0	6.2
Turnover & Leverage ratios (x)				
Asset turnover (x)	2.5	2.0	2.4	2.9
Leverage factor (x)	3.8	3.7	3.6	3.7
Net margin (%)	1.2	3.8	2.1	1.6
Net Debt/Equity (x)	1.1	0.9	1.0	1.1
Working Capital & Liquidity ratio				
Inventory days	26.1	26.1	26.1	26.1
Receivable days	5.4	5.4	5.3	5.3
Payable days	15.7	18.0	18.0	18.0

Valuation

Year-end: March	FY20	FY21E	FY22E	FY23E
PER (x)	10.5	4.0	5.4	5.2
Price / Book value (x)	1.2	1.0	0.9	0.9
PCE (x)	5.3	2.9	3.3	3.0
EV / Net sales (x)	0.3	0.3	0.2	0.2
EV / EBITDA (x)	11.3	5.0	6.3	6.6
Dividend Yield (%)	4.2	10.0	7.4	7.7



Notes

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