

Oil and Gas June 19, 2020

CMP	220
Sensex	34336

Stock Statistics

Bloomberg code	HPCL IN
Equity Cap (INR mn)	1500
Face Value (INR)	10
Free float (%)	49
INR / USD	76.3
Market cap (INR bn)	330
Market cap (USD bn)	4.4
52 Wk High/Low (INR)	329/155

Shareholding Pattern (%) – 'Mar-20

Promoter	50.1
Foreign Institutional Investor	17.7
MF / FI / UTI / Banks	14.9
Public & Others	17.3

Analyst
Nirav Jimudia

✉: nirav@anvilresearch.com

HPCL Ltd Investment Rationale:

- 55% of the inventory losses covered in 1Q:** Steep fall in crude prices from \$ 54/bbl in February to \$30/bbl in March led to industry inventory losses of Rs.201 bn of which our calculation suggest for April-may cumulative recovery is Rs.110 bn. HPCL share being 23%, we expect HPCL would have recovered Rs.25 bn on Marketing side and another Rs.0.7 bn on refining. Cumulative recovery is Rs. 32 bn (of the Rs.41 bn incurred in 4Q) for HPCL.
- Auto fuels volumes recovering to Pre-COVID levels:** With steep fall in marketing volumes to 40% in April and 70% in May to Pre-Covid levels, auto volumes have recovered to 83% in 1st Wk of June and expected to reach 90% by June end. This coupled with increase in prices from June 7 (12 consecutive increases), our calculation shows Diesel Marketing Margins have recovered to Rs.2.91/L and Petrol to Rs.3.42/L. Recent commentary from OMC's suggest it is possible that current weakness in refining margins could be recovered through Marketing division which we believe can help OMC's to withstand weak refining cycle & report healthy profits in F21e.
- Every \$1/bbl fall in GRM, OMC's can recover through Rs 0.3/L increase in Marketing Margin:** F20 adjusted Refining margin were \$4.3/bbl (Inventory loss of Rs.30 bn or \$3.3/bbl). We assume \$3/bbl GRM for F21e on the back of weak refining cycle globally. Our understanding suggest due to covid-19, Refining utilization has fallen to 72% globally (Peak was 82% Pre Covid-19) and current weak Singapore GRM Margins (around \$-0.5-0.5)/bbl band keeps these 10% refining capacity out of the system. Any improvement in Refining margins on back of improved consumption would encourage these players to come back and put pressure on the Margins. However, OMC's can pass on the weaker refining margins through increase in Marketing Margins. Our calculation suggest every \$1/bbl fall in GRM's can be equally compensated thru Rs.0.3/L increase in auto fuel Margins.
- Pass on Euro-6 capex in auto fuels a positive:** OMC's have spend almost \$4.3 bn for transition from Euro-IV to Euro-VI and recent management commentary of HPCL suggest they have started passing on cost of this capex in auto fuels which is positive as additional opex is incurred in terms of removing sulphur through infuse of hydrogen which has a cost attached to it. (Current hydrogen prices at Rs. 20/kg).
- Mumbai and Vizag Refinery Expansion to get complete in CY21e:** Mumbai refinery project of Rs. 50 bn for expansion from 7.5 to 9.5 MMTPA and Vizag refinery expansion from 8.33 to 15 MMTPA (Entire refinery revamp with bottom upgradation) at a capex of Rs. 210 bn will get complete in CY21 and start contributing to earnings from FY23e. HPCL has spent Rs. 80 bn on refineries capex in F20 and similar amount is expected to be spend in F21e.
- HPCL, a play on recovery in auto fuel Margins:** Refining capacity of HPCL is 17 MMT however on the marketing side, volumes are almost 40 MMT. BPCL Refining/Marketing ratio is 70% and for IOC it is almost 100%. If BPCL/IOC are covering their weak refining margins through increase in marketing margins, it would benefit HPCL the most as its Refining/Marketing ratio is 43%.
- Valuation:** We expect HPCL to do EBIDTA/PBT/PAT of Rs.100/71/53 bn for FY21e translating into EPS of Rs.35/sh. Assuming dividend payout of 50% for F21e, Stock is currently trading at 8% dividend yield and ROE of 15%. Stock is trading at P/BV of 0.9x F21e.

Exhibit 1: OMC's CONTROL ~90% OF THE FUEL OUTLETS:

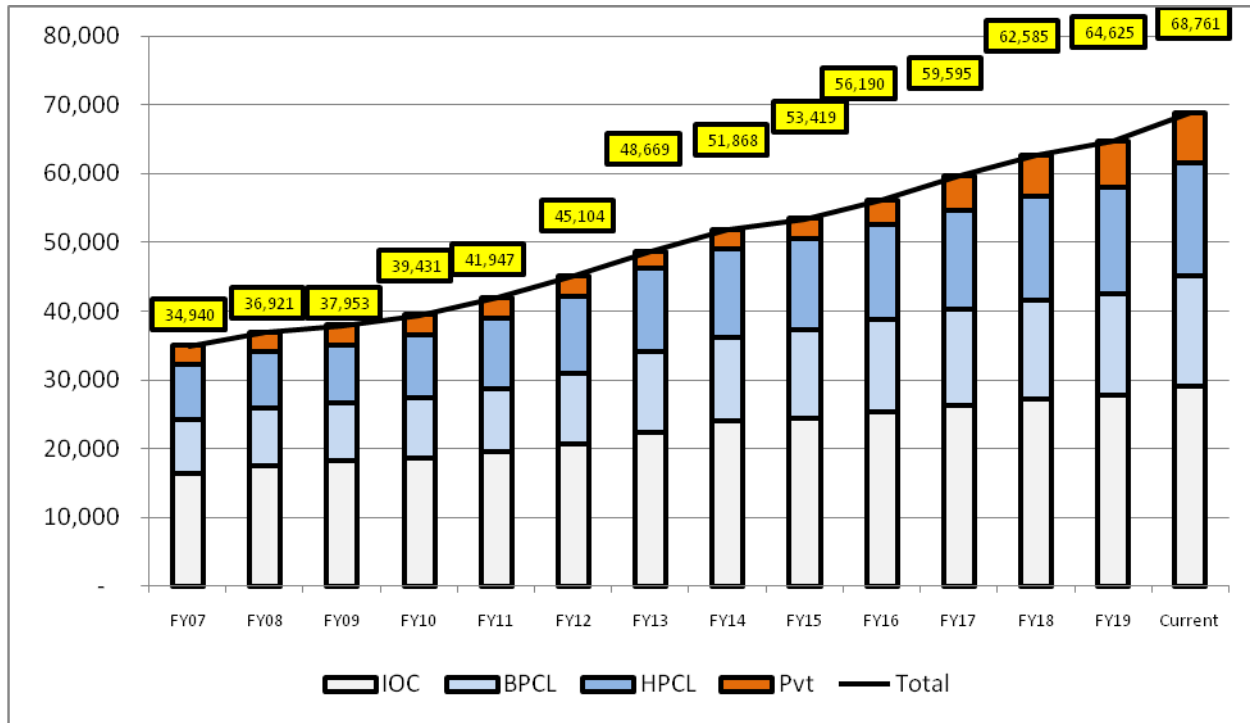


Exhibit 2: MARKETING INFRASTRUCTURE OF OMC's Vs PVT PLAYERS- OMC's WAY AHEAD

Particulars	Units	IOCL	BPCL	HPCL	RIL	Nayara	Shell	Others	Total
POL terminals/Depots	No	120	78	84	18	3		6	309
ATF stations	No	119	61	43	31			1	255
RO's	No	29,029	16,073	16,388	1,400	5,680	184	7	68,761
Urban	No	20,532	13,373	12,552	1,273	3,727	156	7	51,620
Rural	No	8,497	2,700	3,836	127	1,953	28		17,141
SKO Agencies	No	3,882	1,001	1,638					6,521
LPG distributors	No	12,399	6,099	6,074					24,572
LPG bottling Plants	No	91	51	50				3	195
LPG bottling Capacity	MMT	10	4	4				0	19
LPG active consumers	Cr	13	7	8					28

Exhibit 3: HPCL- AUTO FUEL MARKET SHARE MAINTAINED IN LAST 15 YEARS

Diesel Market Share maintained at 22% despite private competition

Particulars	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19
IOC	55.1%	53.9%	50.9%	53.3%	53.4%	54.0%	53.7%	53.0%	52.7%	51.5%	49.6%	49.7%	48.0%	46.6%	45.0%	44.4%
BPCL	24.3%	23.0%	21.3%	23.1%	24.1%	24.4%	23.8%	24.3%	25.2%	26.1%	26.8%	26.5%	25.9%	25.1%	24.8%	24.5%
HPCL	20.1%	19.3%	18.3%	18.4%	20.0%	20.9%	21.1%	20.6%	21.9%	22.4%	23.4%	22.8%	22.6%	22.3%	21.9%	21.7%
Pvt	0.5%	3.8%	9.5%	5.2%	2.5%	0.7%	1.4%	2.2%	0.2%	0.0%	0.2%	1.0%	3.4%	6.0%	8.3%	9.4%
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

Petrol Market Share maintained at 25% despite private competition

Particulars	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19
IOC	44%	45%	43%	41%	44%	45%	45%	45%	45%	44%	44%	44%	43%	43%	41%	41%
BPCL	31%	30%	29%	28%	29%	29%	28%	28%	28%	28%	28%	28%	28%	27%	27%	26%
HPCL	25%	25%	24%	26%	23%	25%	25%	25%	26%	26%	26%	26%	26%	25%	25%	25%
Pvt	0%	1%	5%	5%	5%	1%	2%	2%	2%	2%	2%	2%	3%	5%	7%	8%
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

Exhibit 4: BREAK UP OF RETAIL OUTLETS IN RURAL AND URBAN AREAS

Rural RO's	Units	FY15	FY16	FY17	FY18	FY19	FY19 % Share
IOCL	No	6,230	6,691	7,051	7,529	7,857	49%
BPCL	No	2,184	2,353	2,492	2,621	2,702	17%
HPCL	No	2,664	2,847	3,056	3,310	3,478	22%
RIL	No	108	127	127	127	127	1%
Nayara	No	385	385	1,168	1,570	1,811	11%
Shell	No	9	10	11	14	20	0%
Total	No	11,580	12,413	13,905	15,171	15,995	100%

Urban RO's	Units	FY15	FY16	FY17	FY18	FY19	FY19 % Share
IOCL	No	18,175	18,672	19,161	19,318	19,845	41%
BPCL	No	10,625	11,086	11,491	11,720	12,101	25%
HPCL	No	10,569	10,955	11,356	11,626	11,962	25%
RIL	No	212	823	1,094	1,186	1,273	3%
Nayara	No	1,106	1,715	2,331	2,784	3,317	7%
Shell	No	68	72	74	86	125	0%
Total	No	40,755	43,323	45,507	46,720	48,623	100%

Exhibit 5: FINANCIALS- 11 YEAR SNAPSHOT:

Particulars	Units	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20e	FY21e
Gross Margins-Reported	Rs/Cr	11,342	11,800	13,048	14,561	17,410	17,379	22,922	23,608	24,829	27,279	22,186	24,278
Inventory Gain	Rs/Cr	1,160	1,383	1,611	890	1,577	(2,011)	(1,217)	2,130	272	300	(1,293)	-
Refining Gross	Rs/Cr	1,319	2,407	1,376	1,320	2,225	1,908	5,116	5,231	5,920	4,342	835	2,628
Pipeline Margins Gross (assumption)	Rs/Cr	780	800	721	890	800	920	920	980	1,000	1,000	1,000	1,000
(Under) Compensation	Rs/Cr	(1,230)	(1,510)	(11)	(232)	(476)	(497)	(8)	-	-	-	-	-
Marketing Margins	Rs/Cr	9,313	8,720	9,351	11,692	13,284	17,059	18,111	15,267	17,637	21,566	21,644	20,650
Marketing Volumes	MMT	26	27	29	30	31	32	34	35	37	39	40	35
Marketing Margins-Gross	Rs/MT	3,618	3,211	2,237	3,284	4,241	5,338	5,294	4,335	4,791	5,574	5,460	5,900
Marketing Margin + Invent	Rs/Cr	10,473	10,103	10,962	12,582	14,861	15,048	16,894	17,397	17,909	21,866	20,351	20,650
Gross Marketing Margin	Rs/MT	4,069	3,720	3,719	4,150	4,799	4,708	4,938	4,940	4,865	5,652	5,134	5,900
Reported EBITDA	Rs/Cr	3,404	3,929	3,807	4,144	5,989	5,603	7,912	11,027	10,614	11,442	5,124	10,007
Less:													
Refinery EBITDA	Rs/Cr	453	1,643	578	260	1,198	853	3,988	4,040	4,836	3,296	(1,108)	1,732
Pipeline EBITDA	Rs/Cr	585	600	541	668	600	690	690	735	750	750	750	750
Inventory Gain / (loss)	Rs/Cr	1,160	1,383	1,611	890	1,577	(2,011)	(1,217)	2,130	272	300	(1,293)	-
Other Income	Rs/Cr	786	723	850	1,102	974	1,226	1,138	1,515	1,794	1,635	1,838	1,650
PBDIT	Rs/Cr	4,190	4,652	4,656	5,247	6,963	6,829	9,050	12,542	12,409	13,077	6,962	11,657
Interest													
Normal Interest	Rs/Cr	523	258	440	326	710	707	640	536	567	726	1,082	1,100
Interest due to delayed compensation	Rs/Cr	381	626	1,258	1,512	795	-	-	-	-	-	-	-
Total	Rs/Cr	904	884	1,698	1,838	1,505	707	640	536	567	726	1,082	1,100
PBDT	Rs/Cr	3,286	3,768	2,959	3,409	5,459	6,122	8,410	12,006	11,842	12,351	5,880	10,557
Depreciation	Rs/Cr	1,164	1,407	1,713	1,932	2,188	1,971	2,667	2,535	2,753	3,013	3,304	3,450
PBT	Rs/Cr	2,122	2,361	1,246	1,477	3,270	4,151	5,744	9,471	9,089	9,339	2,576	7,107
Extraordinary (Exp)/ Income	Rs/Cr	(500)	(15)	0	(3)	(665)	(100)	-	(450)	232	-	(1,003)	-
Adjusted PBT	Rs/Cr	1,622	2,346	1,246	1,475	2,606	4,051	5,744	9,021	9,322	9,339	1,573	7,107
Tax Exp	Rs/Cr	275	807	308	570	882	1,337	1,875	2,812	2,999	3,310	(1,065)	1,827
Tax/PBT Ratio	%	16.9%	34.4%	24.7%	38.6%	33.8%	33.0%	32.7%	31.2%	32.2%	35.4%	-67.7%	25.7%
PAT	Rs/Cr	1,347	1,539	938	905	1,724	2,714	3,868	6,209	6,322	6,029	2,638	5,281
EPS	Rs/Sh	9.0	10.3	6.3	6.0	11.5	18.1	25.8	41.4	42.1	40.2	17.6	35.2
Dividend Paid	Rs/Cr	406.4	474.1	287.8	287.8	524.9	829.6	1,456.1	3,477.7	2,321.3	2,385.0	1,477.1	2,640.3
Balance Transferred to B/S	Rs/Cr	940.6	1,065.1	650.6	616.9	1,198.9	1,884.6	2,412.1	2,731.1	4,001.0	3,643.5	1,160.6	2,640.3
Dividend Payout	%	30.2%	30.8%	30.7%	31.8%	30.4%	30.6%	37.6%	56.0%	36.7%	39.6%	56.0%	50.0%
DPS	Rs/Sh	2.7	3.2	1.9	1.9	3.5	5.5	9.7	23.2	15.5	15.9	9.8	17.6

Exhibit 6: Marketing Margins Snapshot:

Particulars	Units	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20e	FY21e
Marketing EBIDTA- Without Inventory	Rs/Cr	1,205	303	1,077	2,327	2,614	6,071	4,451	4,122	4,757	7,095	6,775	7,525
Gross Marketing Margins-Derived	Rs/Cr	9,313	8,720	9,351	11,692	13,284	17,059	18,111	15,267	17,637	21,566	21,644	20,650
Marketing Cost	Rs/Cr	8,107	8,417	8,274	9,366	10,670	10,989	13,660	11,145	12,880	14,471	14,869	13,125
Marketing Cost	Rs/MT	3,150	3,099	2,807	3,089	3,446	3,438	3,993	3,164	3,499	3,740	3,751	3,750
Marketing EBIDTA -With Inventory Effect	Rs/Cr	2,365	1,686	2,688	3,217	4,191	4,060	3,234	6,252	5,029	7,395	5,482	7,525
Gross Marketing Margins-Derived	Rs/Cr	10,473	10,103	10,962	12,582	14,861	15,048	16,894	17,397	17,909	21,866	20,351	20,650
Marketing Cost	Rs/Cr	8,107	8,417	8,274	9,366	10,670	10,989	13,660	11,145	12,880	14,471	14,869	13,125
Marketing EBIDTA -With Inventory Effect	Rs/MT	919	621	912	1,061	1,354	1,270	945	1,775	1,366	1,911	1,383	2,150
Marketing Cost	Rs/MT	3,150	3,099	2,807	3,089	3,446	3,438	3,993	3,164	3,499	3,740	3,751	3,750
Gross Margins	Rs/MT	4,069	3,720	3,719	4,150	4,799	4,708	4,938	4,940	4,865	5,652	5,134	5,900
Key Parameters													
Exchange Rate	Rs/\$	47	46	48	54	61	61	65	67	65	70	71	75
Gross Margins-Marketing adjusted for Inventory Loss	\$/bbl	12	11	11	10	11	11	10	10	10	11	10	11
Inventory Gain/ (Loss)	\$/bbl	3	4	5	2	4	(4)	(3)	4	1	1	(2)	-
Refining GRM	\$/bbl	3	5	3	2	3	3	7	6	7	5	1	3

Exhibit 7: VALUATION BASED ON FY21e EARNINGS

Particulars	times	EBIDTA	EV (Rs/bn)
Refining	5.0	1,732	87
Marketing	6.5	7,525	489
Pipeline	4.5	750	34
HMEL Refinery @ 50%	6.0	1,800	108
Total EBIDTA		10,007	717
Bonds	Rs/bn		51
Debt	Rs/bn		307
Net EV	Rs/bn		461
Value Per Share	Rs/sh		308
E&P	Rs/sh		-
Value of Investment @ 20% discount	Rs/sh		8
Value	Rs/sh		316

Anvil Share & Stock Broking Pvt Ltd is registered as below:

SEBI Regn No.:- U67120MH1997PTC109640

Cash Segment – BSE Regn No. – INB011209950

NSE Regn No. – INB231046831

F&O Segment - BSE Regn No. – INF011209950

NSE Regn No. – INF231046831

Under SEBI (Research Analyst) Regulations, 2014 – INH000000818

This report is intended for distribution to institutional investors. Recipients who are not institutional investors should seek advice of their independent financial advisor prior to taking any investment decision based on this report or for any necessary explanation of its contents.

Analyst Certification – The views expressed in this research report accurately reflect the personal views of the analyst about the subject securities or issues and no part of the compensation of the research analyst was, is or will be directly or indirectly related to the specific recommendations and views expressed by research analyst in this report. The research analysts, strategists or research associates principally responsible for preparation of most research receive compensation based upon various factors including quality of research, investor client feedback, stock picking, competitive factors and firm revenues.

DISCLAIMER:

We, **Anvil Share & Stock Broking Pvt Ltd**, **our Analysts** & **our Associates** hereby solemnly declare & disclose that we:

- ✓ Do not have any financial interest of any nature in the company referred in this research report
- ✓ Do not individually or collectively hold 1% or more of the securities of the company referred in this research report
- ✓ Do not have any other material conflict of interest in the company referred in this research report
- ✓ Do not act as a market maker in securities of the company referred in this research report
- ✓ Do not have any directorships or other material relationships with the company referred in this research report
- ✓ Do not have any personal interests in the securities of the company referred in this research report

Do not have any past significant relationships with the company referred in this research report, including Investment Banking or other advisory assignments or relationships.