

RETAIL EQUITY RESEARCH

Hindustan Petroleum Corporation Ltd.
Oil Marketing & Distribution

BSE CODE: 500104

NSE CODE: HINDPETRO

Bloomberg CODE: HPCL:IN

SENSEX: 34,474

09th October, 2018**HOLD**
 Rating as per Large Cap 12 months investment period
 CMP Rs. 178 TARGET Rs. 187 RETURN 5%↑

Inventory gains drive higher GRM; firming crude oil prices a concern ...

Hindustan Petroleum Corporation Ltd. (HPCL) is engaged in refining, transportation and marketing of petroleum products.

- While crude oil refining throughput rose merely by 1% YoY in Q1FY19, pipeline throughput surged by 17% YoY and marketing volumes grew by 5% YoY.
- Net sales increased by 26% YoY, EBITDA grew strongly by 96% YoY mainly due to higher refining margins led by inventory gains.
- We maintain lower GRM of USD6.5/bbl for FY19E/20E due to higher crude oil prices & weakening rupee. As a result, we expect EBITDA margin to moderate to 3.4% in FY19E and 3.3% in FY20E.
- Higher crude oil prices coupled with weaker rupee is likely to further hurt marketing margins in the run-up to election in key states later this year.
- Considering crucial state elections later this year and general elections next year, reinforces worries about OMCs ability to maintain their marketing margins in a considerably higher crude oil price environment.
- However, recent sharp correction in the stock price has factored in most of the negatives. Hence, we maintain 'HOLD' rating on the stock with a revised target price of Rs 187 using the sum of the part (SOTP) valuation methodology.

Higher crude oil prices drive revenue

HPCL reported 26% YoY increase in net sales in Q1FY19 driven largely by higher crude oil prices. While domestic marketing sales volume rose by 5% YoY to 9.63 MMT, crude oil throughput surged 17% YoY to 5.45 MMT. Marketing sales volume growth was led by increased sales of motor spirit (Petrol) (↑ 6.9% YoY), high speed diesel (↑ 2.7% YoY), LPG (↑ 11.3%), aviation turbine fuel (↑ 9.9%) and lubes (↑ 22.9% YoY). The company's refineries processed 4.52 MMT of crude during Q1FY19, up by 1%. Going ahead, we maintain crude throughput at 18.3 MMT for FY19E/FY20E.

Inventory gains boosts EBITDA

EBITDA surged by 96% YoY on account of higher refining margins mainly due to inventory gains coupled with increased refining throughput and sales volume. Average gross refining margin, the difference between the cost of crude oil processed and the prices of refined products, rose 22% by YoY to \$7.15 per barrel primarily due to higher crude oil prices which rose significantly (from \$ 49.8/bbl in Q1FY18 to \$ 73.0/bbl in Q1FY19) leading to inventory gains in refining and marketing segment which in-turn boosted gross refinery margins. The company registered total inventory gain of Rs 1,934 crore during the quarter. While the refining segment reported inventory gain of Rs7.7bn, marketing segment saw robust inventory gain of Rs11.4bn. Consequently, EBITDA margin expanded by 167bps YoY to 4.7% in Q1FY19. Going ahead, we maintain lower GRM of USD6.5/bbl for FY19E/20E due to higher crude oil prices & weakening rupee. As a result, we expect EBITDA margin to moderate to 3.4% in FY19E and 3.3% in FY20E. Although operating performance remained strong, forex loss (Rs538 crore), decline in other income (↓ 46% YoY), increase in interest costs (↑ 34% YoY) and higher tax charges (↑ 90% YoY) capped profitability growth at 86% YoY.

Other highlights

HPCL commissioned 65 new retail outlets during Q1FY19 taking the total retail network to 15,127 as of June 2018. Also, it added 141 new LPG distributorships during the quarter taking the total to 4,990 as of June 2018. Further, HPCL has outlined an investment of over Rs8,400 crore across refineries & petrochemicals, marketing, pipelines and natural gas segment.

Outlook & Valuation

Although the OMCs have so far passed on the rise in crude oil prices to consumers, we maintain a cautious stance on the stock as fears that the OMCs will freeze retail fuel prices ahead of assembly elections in key states (Madhya Pradesh, Rajasthan, Chhattisgarh) later this year and general election next year remains an overhang. This raises worries about OMCs' ability to maintain marketing margins. While we increase our revenue estimates by 16%/24% in FY19E/20E (higher domestic market sales volume), we reduce EBITDA margin estimates by 30bps/60bps YoY to factor in weak GRMs. However, recent sharp correction in the stock price after the government's decision to reduce petrol & diesel retail selling prices by Rs 2.50 per litre and asking the OMCs to absorb Rs 1 per litre price cut, has factored in most of the negatives. Hence, we maintain 'HOLD' rating on the stock with a downward revised target price (TP) of Rs 187 using the sum of the part (SOTP) valuation methodology wherein we value HPCL at 4.5x FY20E EV/EBITDA.

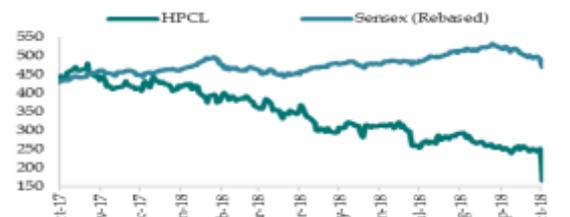
Company Data

Market Cap (Rs. cr)	27,207
Enterprise Value (Rs. cr)	47,820
Outstanding Shares (cr)	152.4
Free Float	49%
Dividend Yield	6.8%
52 week high	Rs. 484
52 week low	Rs.163
6m average volume (cr)	0.6
Beta	0.4
Face value	Rs. 10

Shareholding (%)	Q3FY18	Q4FY18	Q1FY19
Promoters	51.1	-	-
FII's	24.8	23.4	21.1
MFs/Insti	12.0	12.9	15.7
Public	6.9	7.0	7.0
Others	5.2	56.7	56.2
Total	100.0	100.0	100.0

Price Performance	3 Month	6 Month	1 Year
Absolute Return	(33%)	(50%)	(60%)
Absolute Sensex	(3%)	3%	8%
Relative Return*	(30%)	(53%)	(68%)

*over or under performance to benchmark index



Standalone (Rs. cr)	FY18	FY19E	FY20E
Sales	2,19,333	2,94,067	3,10,720
Growth (%)	17.3%	34.1%	5.7%
EBITDA	10,672	10,118	10,244
Margin (%)	4.9	3.4	3.3
PAT Adj	6,357	5,240	4,986
Growth (%)	2.4%	-17.6%	-4.8%
Adj.EPS	41.7	34.4	32.7
Growth (%)	2.4%	-17.6%	-4.8%
P/E	4.3	5.2	5.5
P/B	1.1	1.0	0.9
EV/EBITDA	4.4	5.3	5.8
RoE (%)	28.7	20.6	17.7
D/E	0.9	1.0	1.1

Quarterly Financials (Standalone) Profit & Loss Account

Particulars (Rs cr)	Q1FY19	Q1FY18	YoY Growth %	Q4FY18	QoQ Growth %
Sales	67,629	53,469	26.5	60,810	11.2
EBITDA	3,191	1,628	96.0	2,923	9.2
EBITDA Margin (%)	4.7	3.0	167	4.8	(9)
Depreciation	706	667	5.9	725	(2.6)
EBIT	2,484	961	158.5	2,197	13.1
Interest	191	143	33.5	178	7.5
Other Income	306	570	(46.4)	343	(10.8)
Exceptional Items	-	-	-	-	-
PBT	2,599	1,388	87.2	2,362	10.0
Tax	880	464	89.8	614	43.2
PAT	1,719	925	85.9	1,748	(1.6)
Minority Interest/P&L from associates	-	-	-	-	-
Reported PAT	1,719	925	85.9	1,748	(1.6)
Adjustment	-	-	-	-	-
Adj PAT	1,719	925	85.9	1,748	(1.6)
No. of shares (cr)	152.4	101.6	50.0	152.4	-
EPS (Rs)	11.3	9.1	23.9	11.5	(1.6)

Source: Company, Geojit Research

Sum of the parts (SOTP) valuation

Particulars	Methodology	Multiple	Year	Value	Value Per Share (Rs.)
HPCL	EV/EBITDA	4.5x	FY20E	46,096	302
Less: Net debt				26,254	172
Total					130
Investments				10,799	71
- MRPL	Market Price			1,914	13
- Oil India	Market Price			524	3
- HMEL	Net Profit	10.0x	FY18	8,361	55
			20% holding discount to investments		-14
			Target Price		187

Change in estimates

Year / Rs cr	Old estimates		New estimates		Change %	
	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
Revenue	2,53,522	2,49,917	2,94,067	3,10,720	16.0	24.3
EBITDA	9,328	9,653	10,118	10,244	8.5	6.1
Margins (%)	3.7	3.9	3.4	3.3	(30.0)	(60.0)
PAT	4,863	4,885	5,240	4,986	7.8	2.1
EPS	31.9	32.0	34.4	32.7	7.8	2.1

Source: Company, Geojit Research

Standalone Financials

Profit & Loss Account

Y.E March (Rs cr)	FY16	FY17	FY18	FY19E	FY20E
Sales	,77,701	1,87,024	2,19,333	2,94,067	3,10,720
% change	-14.0%	5.2%	17.3%	34.1%	5.7%
EBITDA	7,939	10,577	10,672	10,118	10,244
% change	4.5	5.7	4.9	3.4	3.3
Depreciation	2,653	2,535	2,753	3,047	3,411
EBIT	5,286	8,042	7,919	7,071	6,832
Interest	654	536	567	780	945
Other Income	1,144	1,515	1,849	1,529	1,554
PBT	5,777	9,021	9,202	7,820	7,441
% change	39.1%	56.2%	2.0%	-15.0%	-4.8%
Tax	2,050	2,812	2,845	2,581	2,456
Tax Rate (%)	35.5%	31.2%	30.9%	33.0%	33.0%
Reported PAT	3,726	6,209	6,357	5,240	4,986
Adj*	-	-	-	-	-
Adj PAT	3,726	6,209	6,357	5,240	4,986
% change	36.3%	66.6%	2.4%	-17.6%	-4.8%
No. of shares (cr)	33.9	101.6	152.4	152.4	152.4
Adj EPS (Rs)	24.4	40.7	41.7	34.4	32.7
% change	36.3%	66.6%	2.4%	-17.6%	-4.8%
DPS (Rs)	9.6	22.8	17.0	13.0	13.0

Cash flow

Y.E March (Rs cr)	FY16	FY17	FY18	FY19E	FY20E
Pre-tax profit	5,777	9,021	9,202	7,820	7,441
Depreciation	2,653	2,535	2,753	3,047	3,411
Changes in W.C	(1,440)	612	982	(4,211)	(456)
Others	1,007	(7)	79	(749)	(609)
Tax paid	(1,214)	(2,179)	(1,997)	(2,581)	(2,456)
C.F.O	6,783	9,983	11,018	3,326	7,332
Capital exp.	(4,710)	(5,889)	(6,702)	(8,685)	(10,785)
Change in inv.	72	95	(267)	-	-
Other invest.CF	283	484	(422)	1,529	1,554
C.F - investing	(4,354)	(5,310)	(7,391)	(7,156)	(9,232)
Issue of equity	-	-	-	-	-
Issue/ repay debt	(1,294)	684	(1,073)	6,000	5,700
Dividends paid	(1,749)	(4,177)	(2,792)	(2,378)	(2,378)
Other finance.CF	(675)	(522)	(458)	(780)	(945)
C.F - Financing	(3,719)	(4,015)	(4,324)	2,842	2,377
Chg. in cash	(1,290)	658	(697)	(988)	478
Closing cash	8	34	1,194	206	684

Balance Sheet

Y.E March (Rs cr)	FY16	FY17	FY18	FY19E	FY20E
Cash	8	34	1,194	206	684
Accounts Receivable	3,758	4,064	5,573	7,479	7,903
Inventories	13,211	18,576	18,420	24,615	25,696
Other Cur. Assets	5,517	5,133	6,687	8,810	9,342
Investments	10,579	10,919	11,105	11,105	11,105
Gross Fixed Assets	35,735	41,165	45,757	50,457	57,257
Net Fixed Assets	33,108	36,132	37,972	39,625	43,013
CWIP	1,853	1,810	3,985	7,971	11,956
Intangible Assets	-	-	-	-	-
Def. Tax (Net)	(4,919)	(5,896)	(6,569)	(6,569)	(6,569)
Other Assets	1,546	1,796	1,871	1,871	1,871
Total Assets	64,660	72,568	80,238	95,111	1,05,000
Current Liabilities	22,722	30,781	35,217	41,229	42,810
Provisions	-	-	-	-	-
Debt Funds	14,395	21,250	20,991	26,991	32,691
Other Liabilities	9,573	190	82	82	82
Equity Capital	339	1,016	1,524	1,524	1,524
Reserves & Surplus	17,631	19,331	22,424	25,286	27,894
Shareholder's Fund	17,970	20,347	23,948	26,810	29,418
Minority Interest	-	-	-	-	-
Total Liabilities	64,660	72,568	80,238	95,111	1,05,000
BVPS (Rs)	117.9	133.5	157.1	175.9	193.0

Ratios

Y.E March	FY16	FY17	FY18	FY19E	FY20E
Profitab. & Return					
EBITDA margin (%)	4.5	5.7	4.9	3.4	3.3
EBIT margin (%)	3.0	4.3	3.6	2.4	2.2
Net profit mgn.(%)	2.1	3.3	2.9	1.8	1.6
ROE (%)	21.9	32.4	28.7	20.6	17.7
ROCE (%)	18.7	25.8	22.6	17.4	14.5
W.C & Liquidity					
Receivables (days)	6.9	6.9	8.4	8.4	8.4
Inventory (days)	30.0	40.3	33.7	33.1	32.6
Payables (days)	20.2	26.1	27.5	27.5	27.5
Current ratio (x)	1.0	0.9	0.9	1.0	1.0
Quick ratio (x)	0.4	0.3	0.4	0.4	0.4
Turnover & Levg.					
Gross asset T.O (x)	4.2	4.9	5.0	6.1	5.8
Total asset T.O (x)	2.6	2.5	2.6	3.1	2.9
Int. covge. ratio (x)	8.1	15.0	14.0	9.1	7.2
Adj. debt/equity (x)	0.8	1.0	0.9	1.0	1.1
Valuation ratios					
EV/Sales (x)	0.2	0.2	0.2	0.2	0.2
EV/EBITDA (x)	4.1	3.7	4.4	5.3	5.8
P/E (x)	7.3	4.4	4.3	5.2	5.5
P/BV (x)	1.5	1.3	1.1	1.0	0.9

Recommendation Summary (last 3 years)



Source: Bloomberg, Geojit Research

Dates	Rating	Target
28.Aug.14	BUY	121
23.Jan.15	BUY	154
15.May.15	BUY	161
08.Jun.15	BUY	154
13.Aug.15	BUY	221
16.Oct.15	BUY	215
24.Nov.15	BUY	207
15.Mar.17	HOLD	373
14.Sep.17	HOLD	468
07.Jun.18	HOLD	341
09.Oct.18	HOLD	187

Investment Rating Criteria

Large Cap Stocks;

Buy	-	Upside is above 10%.
Hold	-	Upside is between 0% - 10%.
Reduce	-	Downside is more than 0%.
Neutral	-	Not Applicable

Mid Cap and Small Cap;

Buy	-	Upside is above 15%.
Accumulate	-	Upside is between 10% - 15%.
Hold	-	Upside is between 0% - 10%.
Reduce/Sell	-	Downside is more than 0%.
Neutral	-	Not Applicable

To satisfy regulatory requirements, we attribute 'Accumulate' as Buy and 'Reduce' as Sell. The recommendations are based on 12 month horizon, unless otherwise specified. The investment ratings are on absolute positive/negative return basis. It is possible that due to volatile price fluctuation in the near to medium term, there could be a temporary mismatch to rating.

For reasons of valuations/return/lack of clarity/event we may revisit rating at appropriate time. Please note that the stock always carries the risk of being upgraded to BUY or downgraded to a HOLD, REDUCE or SELL.

Neutral - The analyst has no investment opinion on the stock under review.

Geojit Financial Services Limited has outsourced the preparation of this research report to DION Global Solutions Limited whose relevant disclosures are available hereunder. However, Geojit's research desk have reviewed this report for any untrue statement of material fact or any false or misleading information.

General Disclosures and Disclaimers

CERTIFICATION

I, Abhishek Kumar Das, employee of Dion Global Solutions Limited (Dion) is engaged in preparation of this report and hereby certify that all the views expressed in this research report (report) reflect my personal views about any or all of the subject issuer or securities.

Disclaimer

This report has been prepared by Dion and the report & its contents are the exclusive property of the Dion and the client cannot tamper with the report or its contents in any manner and the said report, shall in no case, be further distributed to any third party for commercial use, with or without consideration.

Geojit Financial Services Limited has outsourced the assignment of preparation of this report to Dion.

Recipient shall not further distribute the report to a third party for a commercial consideration as this report is being furnished to the recipient solely for the purpose of information.

Dion has taken steps to ensure that facts in this report are based on reliable information but cannot testify, nor make any representation or warranty, express or implied, to the accuracy, contents or data contained within this report. It is hereby confirmed that wherever Dion has employed a rating system in this report, the rating system has been clearly defined including the time horizon and benchmarks on which the rating is based.

Descriptions of any company or companies or their securities mentioned herein are not intended to be complete and this report is not, and should not be construed as an offer or solicitation of an offer, to buy or sell any securities or other financial instruments. Dion has not taken any steps to ensure that the securities referred to in this report are suitable for any particular investor. This report is not to be relied upon in substitution for the exercise of independent judgment. Opinions or estimates expressed are current opinions as of the original publication date appearing on this report and the information, including the opinions and estimates contained herein, are subject to change without notice. Dion is under no duty to update this report from time to time.

Dion or its associates including employees engaged in preparation of this report and its directors do not take any responsibility, financial or otherwise, of the losses or the damages sustained due to the investments made or any action taken on basis of this report, including but not restricted to, fluctuation in the prices of securities, changes in the currency rates, diminution in the NAVs, reduction in the dividend or income, etc.

The investments or services contained or referred to in this report may not be suitable for all equally and it is recommended that an independent investment advisor be consulted. In addition, nothing in this report constitutes investment, legal, accounting or tax advice or a representation that any investment or strategy is suitable or appropriate to individual circumstances or otherwise constitutes a personal recommendation of Dion.

REGULATORY DISCLOSURES:

Dion is engaged in the business of developing software solutions for the global financial services industry across the entire transaction lifecycle and inter-alia provides research and information services essential for business intelligence to global companies and financial institutions. Dion is listed on BSE Limited (BSE) and is also registered under the SEBI (Research Analyst) Regulations, 2014 (SEBI Regulations) as a Research Analyst vide Registration No. INH100002771. Dion's activities were neither suspended nor has it defaulted with requirements under the Listing Agreement and / or SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 with the BSE in the last five years. Dion has not been debarred from doing business by BSE / SEBI or any other authority.

In the context of the SEBI Regulations, we affirm that we are a SEBI registered Research Analyst and in the course of our business, we issue research reports / research analysis etc that are prepared by our Research Analysts. We also affirm and undertake that no disciplinary action has been taken against us or our Analysts in connection with our business activities.

In compliance with the above mentioned SEBI Regulations, the following additional disclosures are also provided which may be considered by the reader before making an investment decision:

1. Disclosures regarding Ownership

Dion confirms that:

- (i) It/its associates have no financial interest or any other material conflict in relation to the subject company (ies) covered herein at the time of publication of this report.
- (ii) It/its associates have no actual / beneficial ownership of 1% or more securities of the subject company (ies) covered herein at the end of the month immediately preceding the date of publication of this report.

Further, the Research Analyst confirms that:

- (i) He, his associates and his relatives have no financial interest in the subject company (ies) covered herein, and they have no other material conflict in the subject company at the time of publication of this report.
- (ii) He, his associates and his relatives have no actual/beneficial ownership of 1% or more securities of the subject company (ies) covered herein at the end of the month immediately preceding the date of publication of this report.

2. Disclosures regarding Compensation:

During the past 12 months, Dion or its Associates:

(a) Have not managed or co-managed public offering of securities for the subject company (b) Have not received any compensation for investment banking or merchant banking or brokerage services from the subject company (c) Have not received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject (d) Have not received any compensation or other benefits from the subject company or third party in connection with this report.

3. Disclosure regarding the Research Analyst's connection with the subject company:

It is affirmed that I, Abhishek Kumar Das employed as Research Analyst by Dion and engaged in the preparation of this report have not served as an officer, director or employee of the subject company

4. Disclosure regarding Market Making activity:

Neither Dion /its Research Analysts have engaged in market making activities for the subject company.

Copyright in this report vests exclusively with Dion.

Please ensure that you have read the "Risk Disclosure Documents for Capital Market and Derivatives Segments" as prescribed by the Securities and Exchange Board of India before investing.

Geojit Financial Services Ltd. (formerly known as Geojit BNP Paribas Financial Services Ltd.), Registered Office: 34/659-P, Civil Line Road, Padivattom, Kochi-682024, Kerala, India. Phone: +91 484-2901000, Website: www.geojit.com. For investor queries: customer-care@geojit.com, For grievances: grievances@geojit.com, For compliance officer: compliance@geojit.com.

Corporate Identity Number: L67120KL1994PLC008403, SEBI Stock Broker Registration No INZ000104737, Research Entity SEBI Reg No: INH200000345, Investment Adviser SEBI Reg No: INA200002817, Portfolio Manager: INP000003203, Depository Participant: IN-DP-325-2017, ARN Regn.Nos:0098, IRDA Corporate Agent (Composite) No.: CA0226