

**BUY**

TP: Rs 135 | ▲ 28%

**INDIAN OIL CORP**

| Oil & Gas

| 02 August 2021

## Q1 muted but core refining earnings have bottomed out

- Q1 earnings reflect a muted refining performance but recovery in marketing margin
- Refining margins have bottomed out; earnings to be supported by post-Covid recovery and project completions over medium term
- Prefer HPCL over IOCL as the former is geared to deliver earnings growth earlier over FY23-FY24

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**Refining remains muted in Q1:** IOCL's adj. refining segment EBITDA loss widened to Rs 14.3bn in Q1FY22 (from Rs 12.2bn in Q4FY21) on the back of 5% lower throughput and a marginal decline in core GRM. Asian gasoline spreads did not materially capture benefits of the driving season in the West following the resurgence of Covid-19 in India and Asia.

**Marketing improves:** Adj. marketing segment EBITDA improved to Rs 56.6bn from Rs 34.1bn in Q4 with a recovery in marketing margin to Rs 3,010/t (from Rs 1,637/t in Q4) despite a 10% QoQ decline in sales volume. While IOCL sees further possibility of upside over Q1 marketing EBITDA, we remain conservative and have a forecast of Rs 2,000/t based on historical trends.

**Positive on OMCs:** We are positive on OMCs given our expectation of gradual improvement in refining margin, sustained marketing margin and further growth from refinery project completions. We remain conservative and factor in only a US\$ 3.5/bbl rise in benchmark refining margin over the next three years to US\$ 3.8/bbl by FY24. Refining earnings growth will be further supported by delivery on refining and petrochemical expansion and upgrade projects. Amongst OMCs, we expect HPCL to demonstrate this upside first as it delivers on Vizag expansion as well as its HMEL Bhatinda polymer addition and Vizag residue upgrade projects over FY22-FY24.

**Maintain BUY:** At 4.9x FY23E EV/EBITDA, IOCL is trading at a significant discount to BPCL, after adjusting for its investments. We have a BUY on IOCL and HPCL but prefer the latter as we expect it to demonstrate earnings growth from project completions ahead of IOCL. At this juncture, we continue to value IOCL based on FY23E EBITDA and do not capture the benefit of future projects achieving commercial operation beyond this period. Our Mar'22 TP remains at Rs 135 wherein we value the refining and marketing business at 5.5x FY23E EV/EBITDA, a marginal discount to our target multiple of 6.0x for OMC peers.

For details, please refer to our report [OMCs: Prefer HPCL over BPCL and IOCL, 5 Jul 2021](#).

## Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	IOCL IN/Rs 106
Market cap	US\$ 13.4bn
Free float	17%
3M ADV	US\$ 28.2mm
52wk high/low	Rs 118/Rs 72
Promoter/FPI/DII	52%/6%/43%

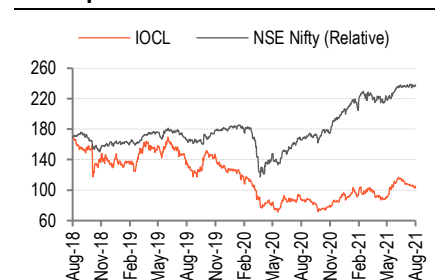
Source: NSE | Price as of 2 Aug 2021

## Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	36,39,497	51,96,102	52,91,033
EBITDA (Rs mn)	4,17,047	2,93,832	3,60,468
Adj. net profit (Rs mn)	2,16,382	1,31,322	1,69,581
Adj. EPS (Rs)	23.6	14.3	18.5
Consensus EPS (Rs)	23.6	16.9	19.4
Adj. ROAE (%)	20.9	11.4	13.7
Adj. P/E (x)	4.5	7.4	5.7
EV/EBITDA (x)	5.0	7.3	6.0
Adj. EPS growth (%)	168.4	(39.3)	29.1

Source: Company, Bloomberg, BOBCAPS Research

## Stock performance



Source: NSE



**Fig 1 – Quarterly performance**

Y/E March (Rs mn)	Q1FY22	Q1FY21	YoY (%)	Q4FY21	QoQ (%)
Net sales	11,86,705	6,23,990	90.2	12,37,140	(4.1)
<b>EBITDA</b>	<b>1,09,868</b>	<b>56,498</b>	<b>94.5</b>	<b>1,47,024</b>	<b>(25.3)</b>
EBITDA margin (%)	9.26	9.05	-	11.88	-
Depreciation and amortisation	26,342	23,545	11.9	25,795	2.1
Interest	12,570	11,713	7.3	10,729	17.2
EBT	70,957	21,239	234.1	1,10,501	(35.8)
Other income	7,028	5,047	39.3	(990)	(810.1)
PBT	77,985	26,286	196.7	1,09,511	(28.8)
Provision for tax	18,571	7,177	158.7	21,698	(14.4)
Effective tax rate (%)	23.81	27.31	-	19.81	-
<b>PAT (adjusted)</b>	<b>59,414</b>	<b>19,108</b>	<b>210.9</b>	<b>87,813</b>	<b>(32.3)</b>
Other comprehensive income	18,441	18,323	-	13,231	(39.4)
<b>EPS (Adjusted)</b>	<b>6.5</b>	<b>2.1</b>	<b>210.9</b>	<b>9.6</b>	<b>(32.3)</b>

Source: Company, BOBCAPS Research

**Fig 2 – Segment performance**

Segment	Q1FY22	Q1FY21	YoY (%)	Q4FY21	QoQ (%)
<b>Refining</b>					
Refinery throughput (mt)	16.72	12.93	29.3	17.59	(5.0)
GRM reported (US\$/bbl)	6.58	(1.98)	432.3	10.59	(37.9)
<b>Normalised GRM (US\$/bbl)</b>	<b>2.24</b>	<b>4.42</b>	<b>(49.4)</b>	<b>2.51</b>	<b>(10.8)</b>
Refining EBITDA reported (Rs mn)	24,920	(35,230)	170.7	63,780	(60.9)
Refining EBITDA (US\$/bbl)	2.8	(4.9)	156.3	6.8	(59.3)
Inventory gain/(loss) (Rs mn)	42,723	(45,880)	193.1	76,000	(43.8)
Inventory gain/(loss) (US\$/bbl)	4.7	(6.4)	174.1	8.1	(41.5)
Exchange fluctuation gain/(loss) (Rs mn)	(3,510)	(170)	nm	(40)	nm
<b>Adj. EBITDA (Rs mn)</b>	<b>(14,293)</b>	<b>10,820</b>	<b>(232.1)</b>	<b>(12,180)</b>	<b>(17.3)</b>
<b>Adj. EBITDA (US\$/bbl)</b>	<b>(1.6)</b>	<b>1.5</b>	<b>(205.1)</b>	<b>(1.3)</b>	<b>(22.1)</b>
<b>Operating costs (US\$/bbl)</b>	<b>3.4</b>	<b>2.9</b>	<b>18.6</b>	<b>3.8</b>	<b>(9.7)</b>
<b>Marketing</b>					
<b>Marketing sales (mt)</b>	<b>18.82</b>	<b>15.48</b>	<b>21.6</b>	<b>20.82</b>	<b>(9.6)</b>
Domestic	17.24	14.24	21.1	19.44	(11.3)
Exports	1.57	1.25	25.8	1.37	14.7
Marketing EBITDA (Rs mn)	54,250	77,010	(29.6)	34,430	57.6
Marketing EBITDA (Rs/t)	2,883	4,975	(42.0)	1,654	74.3
Inventory gain/(loss) (Rs mn)	-	13,920	(100.0)	-	-
Inventory gain/(loss) (Rs/t)	-	899	(100.0)	-	-
Exchange fluctuation gain/(loss) (Rs mn)	(2,390)	980	(343.9)	350	(782.9)
<b>Adj. EBITDA (Rs mn)</b>	<b>56,640</b>	<b>62,110</b>	<b>(8.8)</b>	<b>34,080</b>	<b>66.2</b>
<b>Adj. EBITDA (Rs/t)</b>	<b>3,010</b>	<b>4,012</b>	<b>(25.0)</b>	<b>1,637</b>	<b>83.9</b>
<b>Pipeline</b>					
Pipeline throughput (mt)	19.90	15.00	32.7	21.80	(8.7)
<b>Pipeline EBITDA (Rs mn)</b>	<b>15,740</b>	<b>11,500</b>	<b>36.9</b>	<b>16,080</b>	<b>(2.1)</b>
Pipeline EBITDA (Rs/t)	791	767	3.2	738	7.2

Segment	Q1FY22	Q1FY21	YoY (%)	Q4FY21	QoQ (%)
<b>Petrochemicals</b>	-	-	36.7	-	(12.6)
Volumes (mt)	0.66	0.48	173.2	0.75	(11.5)
<b>Petrochemicals EBITDA (Rs mn)</b>	<b>19,890</b>	<b>7,280</b>	<b>105.7</b>	<b>22,480</b>	<b>0.2</b>
Petrochemicals EBITDA (US\$/t)	411	200	113.1	411	(77.2)
<b>Others (Rs mn)</b>	<b>2,110</b>	<b>990</b>	<b>(13.6)</b>	<b>9,270</b>	<b>14.9</b>
<b>Total Adjusted EBITDA (Rs mn)</b>	<b>80,087</b>	<b>92,700</b>	<b>29.3</b>	<b>69,730</b>	<b>(5.0)</b>

Source: Company, BOBCAPS Research

## Earnings call highlights

- Refining margin muted:** IOCL's Q1FY22 core refining margin dipped marginally QoQ by US\$ 0.3/bbl to US\$ 2.2/bbl. The Asian gasoline crack did not capture the upside seen in US spreads and increased only modestly by US\$ 2.2/bbl to US\$ 7.6/bbl in Q1, before easing to US\$ 7/bbl in July. Diesel crack remained muted at US\$ 4.5/bbl in Q1 and US\$ 4-5/bbl in July (from US\$ 3.8/bbl in Q4). Cracks could recover with opening up of the economy and a return of consumption in FY22.
- Fuel consumption weak:** A comparison with pre-Covid (Jul'19) levels shows that MS or petrol consumption was up 3-5% in Jul'21, diesel was down 11% and ATF fell 53%, whereas LPG consumption increased 7.5%. Muted diesel consumption reflects restrictions on public travel (both rail and road) but could revert to pre-Covid levels by Diwali (Nov'21). Recovery in ATF could take longer, and management expects a return to pre-Covid levels only by end-FY22.
- Upside to marketing EBITDA possible:** IOCL suggested that marketing EBITDA could carry sustainable upside even beyond the Rs 54bn reported in Q1. Lower Q4 EBITDA of Rs 34bn reflected the impact of one-off year-end provisions.
- Petchem margin eases QoQ:** While the polymer spread was down 10% QoQ, MEG dropped 55% and PTA was flat. Cracks have eased further in July. Management expects petrochemical margins to improve with recovery in demand post Covid.
- Polypropene (PP) utilisation remains low:** IOCL's plan of importing propylene to improve utilisation of the new PP plant at Paradip refinery was found unviable. Utilisation remains low at ~60%.
- FY22 capex guidance maintained at Rs 285bn:** The company is not envisaging any delays to projects planned for completion in FY22, viz.: (i) Paradip-Hyderabad pipeline, (ii) Koyali-Ahmednagar-Sholapur pipeline, (iii) augmentation of the Paradip-Haldia-Durgapur LPG pipeline and its extension to Patna and Muzaffarpur, (iv) Ennore natural gas pipeline, and (v) MEG plant at Paradip.
- Petronas JV expanded to cover fuel and natural gas retailing:** Management is exploring options for new retail stations, award of dealership for amenities at highway petrol pumps and transfer of existing petrol pumps, among others.
- Monetisation plan limited to two hydrogen plants in FY22:** IOCL plans to test the InvIT concept with monetisation of two hydrogen plants at the Gujarat refinery in FY22 and may consider another five in FY23 if successful.

## Valuation methodology

We are positive on OMCs given our expectation of gradual improvement in refining margin and marketing margin holding up. While sustainability of marketing margin is a key risk with the rise in oil prices, we expect crude to retract and remain range bound around US\$ 65/bbl. Divestment of BPCL will be a key catalyst for the sector as it will help establish a value for the marketing business in an attractive growth market like India.

We have a BUY on IOCL with a Mar'22 TP of Rs 135, carrying a potential upside of 28%. We value IOCL's refining and marketing business at 5.5x FY23E EV/EBITDA, a marginal discount to our target multiple of 6.0x for OMC peers. With inland refineries, IOCL needs to maintain a higher level of inventory for its operations, which tends to increase earnings volatility relative to peers. Expansion projects are not factored in as they are still some time away.

**Fig 3 – Valuation summary**

Business segments	EV (Rs bn)	Value (Rs/sh)	Comments
Refining	324	35	5.5x FY23E EBITDA
Marketing	924	101	5.5x FY23E EBITDA
Petrochemicals	342	37	6x FY23E EBITDA
Pipeline	387	42	6x FY23E EBITDA
Others	40	4	6x FY23E EBITDA
<b>Total core business EV</b>	<b>2,017</b>	<b>220</b>	
Less: Net Debt	956	104	
<b>Equity value of core business</b>	<b>1,062</b>	<b>116</b>	
Investments	181	20	Listed holdings at 20% discount to CMP and others at investment value
<b>Total equity value for IOCL</b>	<b>1,243</b>	<b>135</b>	

Source: BOBCAPS Research

**Fig 4 – Key assumptions**

Parameter (Rs bn)	FY21	FY22E	FY23E	FY24E
<b>Consolidated EBITDA</b>				
Refining	66	0	59	81
Marketing	215	160	168	177
Petrochemicals	61	61	57	57
Pipeline	57	62	65	67
Others	6	6	7	7
CPCL EBITDA	10	5	5	6
<b>Consolidated EBITDA</b>	<b>417</b>	<b>294</b>	<b>360</b>	<b>395</b>
YoY growth (%)	-	(29.5)	22.7	9.7
Refining throughput (mt)	62.4	67.4	70.0	70.9
YoY growth (%)	(10.1)	8.0	3.9	1.3
Domestic marketing sales (mt)	69.4	74.9	79.0	83.5
YoY growth (%)	(11.7)	7.9	5.6	5.7
Pipeline throughput (mt)	76.0	85.5	89.1	92.7
YoY growth (%)	(19.4)	12.5	4.2	4.0

Parameter (Rs bn)	FY21	FY22E	FY23E	FY24E
USDINR exchange rate	74.2	75.0	76.5	78.0
Crude price (US\$/bbl)	67.5	65.0	65.0	65.0
GRM (US\$/bbl)	5.6	3.0	4.5	5.0
Marketing EBITDA (Rs/t)	2,927	2,000	2,000	2,000
Petrochemicals EBITDA (US\$/t)	303	286	247	229

Source: Company, BOBCAPS Research

## Key risks

OMC valuations are highly sensitive to refining and marketing margins. Key downside/upside risks to our estimates for OMCs are as follows:

- A slower/faster recovery in global economies could lead to below/above-expected refining margins and petrochemical spreads. An adverse/favourable change in global demand-supply balance for the refining or petrochemical product chain could also lower/increase margins vs. our current assumptions.
- Oil prices have surged close to US\$ 75/bbl levels and expose OMCs to the risk of under-recovery on marketing margins for retail sales of petrol/diesel, especially in the wake of recent sharp hikes in excise duties on these fuels.
- Market share losses on fuel product sales could result in below-expected volumes and affect marketing business earnings.
- Refiners are exposed to the requirement of additional investments to lower their carbon footprint, including potential investments in green hydrogen.
- IOCL's earnings carry relatively higher volatility considering its higher inventory days than other OMCs.
- Adverse pipeline tariff orders or regulations by PNGRB mandating third-party use of IOCL's pipelines could hurt pipeline business earnings.

## Sector recommendation snapshot

Stock	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Bharat Petroleum Corp	BPCL IN	13	458	518	HOLD
Hindustan Petroleum Corp	HPCL IN	5	273	345	BUY
Indian Oil Corp	IOCL IN	13	106	135	BUY

Source: BOBCAPS Research, NSE | Price as of 2 Aug 2021

## Financials

### Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Total revenue</b>	<b>48,37,630</b>	<b>36,39,497</b>	<b>51,96,102</b>	<b>52,91,033</b>	<b>54,64,317</b>
EBITDA	1,62,318	4,17,047	2,93,832	3,60,468	3,95,267
Depreciation	(1,02,734)	(1,09,415)	(1,11,136)	(1,24,400)	(1,40,904)
EBIT	59,584	3,07,633	1,82,696	2,36,068	2,54,363
Net interest inc./(exp.)	(65,787)	(35,891)	(54,406)	(59,756)	(61,946)
Other inc./(exp.)	33,818	23,799	32,021	35,197	34,516
Exceptional items	1,13,046	0	0	0	0
EBT	27,615	2,95,540	1,60,312	2,11,508	2,26,933
Income taxes	53,007	(89,885)	(40,221)	(53,185)	(57,037)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	23,493	10,727	11,231	11,258	11,037
<b>Reported net profit</b>	<b>(8,931)</b>	<b>2,16,382</b>	<b>1,31,322</b>	<b>1,69,581</b>	<b>1,80,934</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>80,622</b>	<b>2,16,382</b>	<b>1,31,322</b>	<b>1,69,581</b>	<b>1,80,934</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Accounts payables	2,75,763	3,72,480	3,38,705	3,39,536	3,47,457
Other current liabilities	5,64,560	7,06,279	5,60,750	5,64,054	5,80,355
Provisions	1,12,335	1,08,992	58,729	68,989	72,007
Debt funds	12,67,576	10,93,624	12,56,548	13,08,379	13,46,526
Other liabilities	1,14,393	1,39,645	1,40,140	1,40,508	1,40,992
Equity capital	91,810	91,810	91,810	91,810	91,810
Reserves & surplus	8,62,169	10,26,570	11,02,181	11,98,115	13,00,124
Shareholders' fund	9,53,979	11,18,381	11,93,992	12,89,925	13,91,934
<b>Total liab. and equities</b>	<b>32,97,368</b>	<b>35,49,159</b>	<b>35,59,359</b>	<b>37,22,596</b>	<b>38,91,406</b>
Cash and cash eq.	22,960	24,747	18,577	19,028	21,894
Accounts receivables	1,32,595	1,38,003	1,27,242	1,29,576	1,33,838
Inventories	6,70,108	8,34,275	6,82,988	6,84,734	7,01,647
Other current assets	3,17,328	1,71,213	1,77,977	1,81,083	1,86,755
Investments	3,55,709	4,47,168	4,47,168	4,47,168	4,47,168
Net fixed assets	14,70,211	15,70,838	16,59,358	18,26,818	20,02,776
CWIP	3,28,448	3,62,905	4,46,039	4,34,178	3,97,317
Intangible assets	10	10	10	10	10
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
<b>Total assets</b>	<b>32,97,368</b>	<b>35,49,159</b>	<b>35,59,359</b>	<b>37,22,596</b>	<b>38,91,406</b>

### Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Cash flow from operations</b>	<b>21,997</b>	<b>5,38,883</b>	<b>1,36,649</b>	<b>2,66,362</b>	<b>2,88,197</b>
Capital expenditures	(1,90,925)	(2,44,498)	(2,82,790)	(2,80,000)	(2,80,000)
Change in investments	85,414	(91,460)	0	0	0
Other investing cash flows	33,818	23,799	32,021	35,197	34,516
<b>Cash flow from investing</b>	<b>(71,693)</b>	<b>(3,12,159)</b>	<b>(2,50,769)</b>	<b>(2,44,803)</b>	<b>(2,45,484)</b>
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	3,34,299	(1,73,952)	1,62,924	51,831	38,148
Interest expenses	0	0	0	0	0
Dividends paid	(56,394)	(1,50,734)	(55,710)	(73,648)	(78,925)
Other financing cash flows	(2,15,896)	99,750	736	709	930
<b>Cash flow from financing</b>	<b>62,009</b>	<b>(2,24,936)</b>	<b>1,07,950</b>	<b>(21,108)</b>	<b>(39,847)</b>
<b>Chg in cash &amp; cash eq.</b>	<b>12,313</b>	<b>1,787</b>	<b>(6,170)</b>	<b>451</b>	<b>2,866</b>
<b>Closing cash &amp; cash eq.</b>	<b>22,960</b>	<b>24,747</b>	<b>18,577</b>	<b>19,028</b>	<b>21,894</b>

### Per Share

Y/E 31 Mar (Rs)	FY20A	FY21A	FY22E	FY23E	FY24E
Reported EPS	(1.0)	23.6	14.3	18.5	19.7
Adjusted EPS	8.8	23.6	14.3	18.5	19.7
Dividend per share	5.2	14.0	5.2	6.9	7.3
Book value per share	103.9	121.8	130.0	140.5	151.6

### Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21A	FY22E	FY23E	FY24E
EV/Sales	0.4	0.6	0.4	0.4	0.4
EV/EBITDA	10.9	5.0	7.3	6.0	5.7
Adjusted P/E	12.0	4.5	7.4	5.7	5.4
P/BV	1.0	0.9	0.8	0.8	0.7

### DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21A	FY22E	FY23E	FY24E
Tax burden (Net profit/PBT)	(94.4)	73.2	81.9	80.2	79.7
Interest burden (PBT/EBIT)	(143.4)	96.1	87.7	89.6	89.2
EBIT margin (EBIT/Revenue)	1.2	8.5	3.5	4.5	4.7
Asset turnover (Rev./Avg TA)	145.6	106.3	146.2	145.3	143.5
Leverage (Avg TA/Avg Equity)	3.2	3.3	3.1	2.9	2.8
<b>Adjusted ROAE</b>	<b>7.8</b>	<b>20.9</b>	<b>11.4</b>	<b>13.7</b>	<b>13.5</b>

### Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22E	FY23E	FY24E
<b>YoY growth (%)</b>					
Revenue	(8.4)	(24.8)	42.8	1.8	3.3
EBITDA	(53.9)	156.9	(29.5)	22.7	9.7
Adjusted EPS	(53.6)	168.4	(39.3)	29.1	6.7
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	3.4	11.5	5.7	6.8	7.2
EBIT margin	1.2	8.5	3.5	4.5	4.7
Adjusted profit margin	1.7	5.9	2.5	3.2	3.3
Adjusted ROAE	7.8	20.9	11.4	13.7	13.5
ROCE	2.8	9.6	5.8	7.0	7.1
<b>Working capital days (days)</b>					
Receivables	11	14	9	9	9
Inventory	63	100	61	55	55
Payables	27	37	26	25	25
<b>Ratios (x)</b>					
Gross asset turnover	2.8	1.9	2.4	2.2	2.0
Current ratio	0.7	0.7	0.7	0.7	0.7
Net interest coverage ratio	0.9	8.6	3.4	4.0	4.1
<b>Adjusted debt/equity</b>	<b>1.3</b>	<b>1.0</b>	<b>1.0</b>	<b>1.0</b>	<b>1.0</b>

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

## Disclaimer

### Recommendation scale: Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

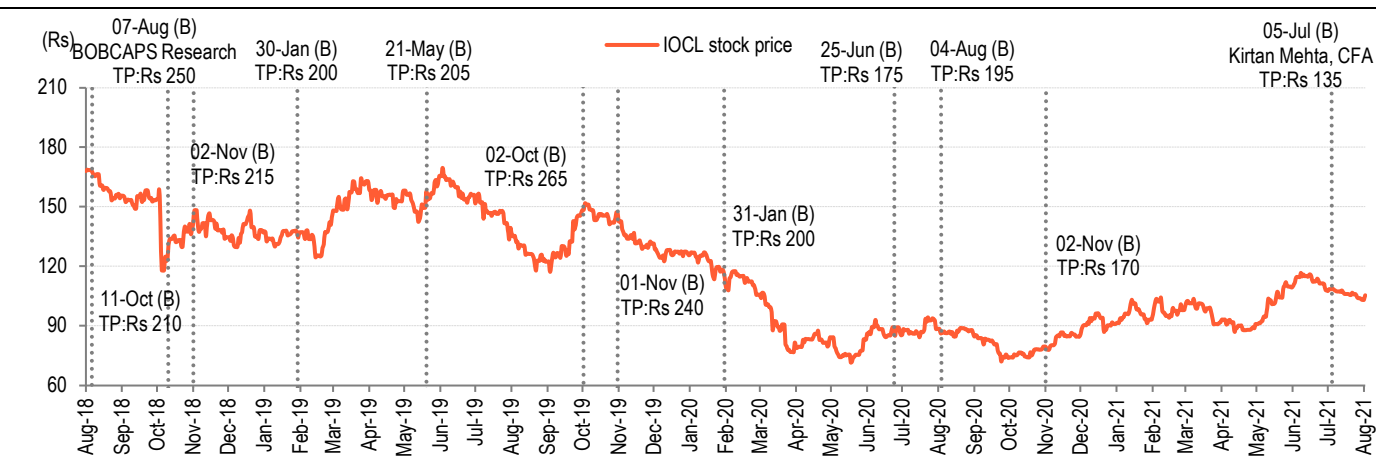
**HOLD** – Expected return from -6% to +15%

**SELL** – Expected return <-6%

**Note:** Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

### Ratings and Target Price (3-year history): INDIAN OIL CORP (IOCL IN)



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

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