Sharekhan by BNP PARIBAS

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Bharat Petroleum Corporation Limited

Stellar Q4; Privatisation key for valuation re-rating

Oil & Gas	Sharekhan code: BPCL	Result Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 468**	
Price Target: **Rs. 520**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

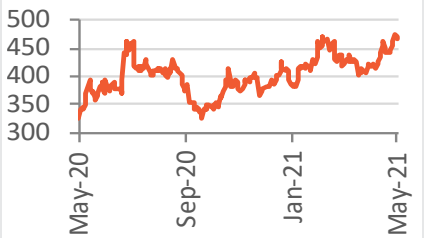
Company details

Market cap:	Rs. 1,01,467 cr
52-week high/low:	Rs. 488/313
NSE volume: (No of shares)	109.9 lakh
BSE code:	500547
NSE code:	BPCL
Free float: (No of shares)	102.0 cr

Shareholding (%)

Promoters	53.0
FII	12.4
DII	23.3
Others	11.3

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	12	3	23	44
Relative to Sensex	9	0	9	-15

Sharekhan Research, Bloomberg

Summary

- Q4FY2021 operating profit/adjusted PAT at Rs. 5,058 crore/Rs. 3,924 crore, up 17.5%/28.3% q-o-q and beat of 41%/65% versus our estimates, led by higher-than-expected inventory gain of Rs. 3,578 crore, core GRM of $2.5/bbl, and other income.
- Reported GRM at $6.6/bbl was fueled by inventory gain of $4.2/bbl; market share gain in diesel by 26 bps y-o-y to 24.4%. Refinery throughput stood at 8.4 mmt (up 16% q-o-q) and marketing sales volume was at 11.8 mmt (up 4% q-o-q).
- Q1FY2022 refinery throughput and marketing sales volume are expected to be impacted by lockdowns; however, core earnings are likely to improve over FY2022E-FY2023E with cyclical recovery in GRM and potential improvement in marketing margin (private players would hold 40% market share in auto fuel post privatisation of BPCL).
- Privatisation (expected by December 2021 with possibility of one quarter delay) remains the key to re-rating trigger for BPCL and could create long-term value for investors. Hence, we maintain a Buy on BPCL with an unchanged PT of Rs. 520.

Bharat Petroleum Corporation Limited's (BPCL) Q4FY2021 operating profit at Rs. 5,058 crore (versus adjusted operating loss of Rs. 789 crore in Q4FY2020 and up 17.5% q-o-q) was 41%/65% above our/street estimates of Rs. 3,578 crore/Rs. 3,072 crore. Large beat in operating profit was on account of higher-than-expected core GRM of $2.5/bbl (outperformed Singapore complex GRM of $1.8/bbl) and massive inventory gain of Rs. 3,642 crore (as compared to inventory loss of Rs. 4,902 crore in Q4FY2020 and versus our estimate of Rs. 1,435 crore). Reported GRM of $6.6/bbl (as compared to $2.5/bbl in Q3FY2021 and versus our estimate of $3.3/bbl) was fueled by inventory gain of $4.2/bbl or Rs. 1,813 crore (versus estimate of Rs. 794 crore). Refinery throughput was also better than expectations at 8.4 mmt (up 15.9% q-o-q and 1.7% beat versus our estimate). Marketing sales volume of 11.8 mmt (up 4% q-o-q) was 7% above our estimate and BPCL gained market share in diesel (volume growth of 5.2% y-o-y versus industry growth of 4.1% y-o-y). Adjusted PAT at Rs. 3,924 crore (versus adjusted net loss of Rs. 601 crore; up 28.3% q-o-q) was 83%/127% above our/street estimate of Rs. 2,146 crore/Rs. 1,730 crore, led by better-than-expected GRM, inventory gain, and higher other income (up 43.9% y-o-y). We have adjusted reported PAT of Rs. 11,940 crore for exceptional income of Rs. 6,993 crore (Rs. 9,422 crore gain from sale of stake in NRL partially offset by one-time expense of Rs. 397 crore related to employee share-based expenses and Rs. 2,033 cost for impairment of investment in subsidiary Bharat PetroResources Limited). Q1FY2022 refinery utlisation rate (at 85%-86% currently versus 122% in Q4FY2021) and marketing sales volume (auto fuel demand down by 25% versus normal level) would be impacted by lower petroleum product demand given lockdown in April 2021-May 2021, but we expect V-shaped recovery as lockdown norms ease and vaccination drive gains pace. Overall, BPCL's core earnings are expected to improve over FY2022-FY2023 with cyclical recovery in refining margin and structurally better marketing margin [as post BPCL privatisation, private players would hold close to ~40% auto fuel market share and oil marketing companies (OMCs) resumed daily price revision of auto fuels]. Management has said that BPCL opened data room (from April 10, 2021) for bidders and privatisation process is expected to get completed by December 2021 (with possibility of one quarter delay). We believe BPCL's privatisation could unlock value and re-rate valuation. Hence, we maintain our Buy rating on BPCL with an unchanged PT of Rs. 520.

Key positives

- Better-than-expected core GRM at $2.5/bbl and outperformed Singapore Complex GRM of $1.8/bbl in Q4FY2021.
- Board recommended final dividend of Rs. 58/share and, thus, FY2021 total dividend at Rs. 79/share implies 17% dividend yield.
- BPCL gained market share in diesel with volume growth of 5.2% y-o-y versus industry growth of 4.1% y-o-y in Q4FY2021.

Key negatives

- Blended marketing margin declined by 31% q-o-q to Rs. 2,485/tonne.

Our Call

Valuation – Maintain Buy on BPCL with an unchanged PT of Rs. 520: We have fine-tuned our FY2022-FY2023 earnings estimates, as lower volume assumption in Q1FY2022 gets partially offset by lower interest cost (debt down by 37% in FY2021). We believe privatisation (although could be delayed by three months) could re-rate BPCL as valuation of marketing assets could get aligned to that of global peers and create long-term value for investors. Hence, we maintain our Buy rating on BPCL with an unchanged PT of Rs. 520. At the CMP, the stock trades 14.5x its FY2022E EPS and 13.6x its FY2023E EPS.

Key Risks

Prolonged weakness in refining margins and impact on petroleum demand, given COVID-19 and any further delay in the government's efforts for privatisation.

Valuation (Standalone) Rs cr

Particulars	FY19	FY20	FY21	FY22E	FY23E
Revenues	2,97,275	2,84,383	2,32,545	3,64,175	3,66,087
OPM (%)	4.0	2.3	7.6	3.1	3.3
Adjusted PAT	7,132	3,764	13,227	6,323	6,775
y-o-y growth (%)	-10.6	-47.2	251.4	-52.2	7.1
Adjusted EPS (Rs.)	36.3	19.1	67.2	32.1	34.4
P/E (x)	12.9	24.4	7.0	14.5	13.6
P/B (x)	2.5	2.8	1.7	1.7	1.6
EV/EBITDA (x)	10.7	21.9	6.5	10.2	9.9
RoNW (%)	20.1	10.8	30.1	11.5	12.0
RoCE (%)	23.3	9.9	26.3	13.2	13.3

Source: Company Data; Sharekhan estimates

Large earnings beat led by higher-than-expected inventory gain, core GRM, and other income

Q4FY2021 operating profit at Rs. 5,058 crore (versus adjusted operating loss of Rs. 789 crore in Q4FY2020 and up 17.5% q-o-q) was 41%/65% above our/street estimates of Rs. 3,578 crore/Rs. 3,072 crore. Large beat in operating profit was on account of higher-than-expected core GRM of $2.5/bbl (outperformed Singapore complex GRM of $1.8/bbl) and massive inventory gain of Rs. 3,642 crore (as compared to inventory loss of Rs. 4,902 crore in Q4FY2020 and versus our estimate of Rs. 1,435 crore). Reported GRM of $6.6/bbl(as compared to $2.5/bbl in Q3FY2021 and versus our estimate of $3.3/bbl) was fueled by inventory gain of $4.2/bbl or Rs. 1,813 crore (versus estimate of Rs. 794 crore). Refinery throughput was also better than expectation at 8.4mmt (up 15.9% q-o-q and 1.7% beat versus our estimate). Marketing sales volume of 11.8mmt (up 4% q-o-q) was 7% above our estimate and BPCL gained market share in diesel (volume growth of 5.2% y-o-y versus industry growth of 4.1% y-o-y). Adjusted PAT at Rs. 3,924 crore (versus adjusted net loss of Rs601 crore; up 28.3% q-o-q) was 83%/127% above our/street estimate of Rs. 2,146 crore/Rs. 1,730 crore led by better-than-expected GRM, inventory gain, and higher other income (up 43.9% y-o-y). We have adjusted reported PAT of Rs. 11,940 crore for exceptional income of Rs. 6,993 crore (Rs. 9,422 crore gain from sale of stake in NRL, partially offset by one-time expense of Rs. 397 crore related to employee share-based expenses and Rs. 2,033 cost for impairment of investment in subsidiary Bharat PetroResources Limited).

Q4FY2021 results conference call highlights

- **Update on privatisation:** BPCL has opened a virtual data room (from April 10, 2021) and has started the process of answering questions from bidders. Under the privatisaion process, the next steep includes discussion with the senior management of BPCL (Post May 28, 2021) and to have a physical inspection of the assets that are currently not being done due to travel restrictions. Post that, there will be the submission of final bids and final share purchase agreement. The process of divestment may complete by December 2021 with the possibility of delay of one quarter based on the current COVID situation. Moreover, management has stated that there is communication from the government to divest stake in Bharat PetroResources Limited.
- **Update on PDPP Projects:** Out of three major units of PDPP project, two units have been commissioned in Q4FY2021 and the third unit will be commissioned soon. For the first two units, stabilisation is going on and production ramp-up is expected in H2FY2022. Post stabilisation of the project, incremental GRM contribution would be $1/bbl.
- **Capex guidance:** The company has guided for capex of Rs. 12,000 crore in FY2022 versus capex spending of Rs. 11,064 crore in FY2021. Out of Rs. 12,000 crore capex, Rs. 3,000 crore would be spent on refining, Rs. 4,000 crore on marketing, Rs. 500 crore in gas, Rs. 1,000 crore on petchem, Rs. 1,300 crore for equity in BPRL, and the remaining Rs. 1,800 crore on other projects.
- **Management view on stake sale in IGL and Petronet:** BPCL has no intention to sell its stake in IGL (22.5% stake) and Petronet LNG (12.5% stake). Even if this happens, the company will look at getting exemption of the requirement of a mandatory open offer to shareholders of both these companies.
- **Focus on green energy:** BPCL has commissioned 629 CNG retail outlets as of now and targets to commission another 800 retail outlets in FY2022. Apart from this, the company has 40 EV charging stations and seven battery swapping stations, but investment for the same is very small as of now. Furthermore, BPCL is also setting up 2G ethanol refinery in Odisha.
- **Refinery utilisation rate and crack spreads:** Refinery utilisation rate in Q4FY2021 was 122% in Q4FY2021 versus 105% in Q3FY2021. In May 2021, refinery rate has dropped to 85%-86% due to lower petroleum product demand because of the lockdown. In Q4FY2021, crack spread on MS improved to $5.66/bbl versus $2.97/bbl in the previous quarter; and for HSD, crack spread stood at $5.78/bbl in Q4FY2021 against $3.35/bbl in Q3FY2021. Management guided that crack spreads have further improved in Q1FY2021 as global petroleum demand is rising given opening up of major economies globally and focus on vaccination drive.
- **Borrowings:** As on March 31, 2021, gross debt of BPCL at a standalone level stood at Rs. 26,315 crore versus Rs. 41,875 crore as of March 2020. The figure excludes lease liability of Rs. 7,845 crore (Rs. 5,943 crore as on March 31, 2020) on account of implementation of IND AS 116.
- **Retail outlets:** BPCL has commissioned total of 2,444 outlets in FY2021, taking the total outlets of the company to 18,637 as of March 31, 2021.

- The board of directors have recommended a final dividend of Rs. 58/share (including one-time special dividend of Rs. 35/share). With this, total dividend for FY2021 is at Rs. 79/share, which implies dividend yield of 16.8%. BPCL has paid 79% of the total proceeds received from sales of stake in NRL (Rs. 9,876 crore) and treasury shares (Rs. 5,525 crore).
- BPCL has divested its entire holding in Numaligarh Refinery Limited (NRL) for a consideration of Rs. 9,876 crore. The company has also signed a 15-year product supply agreement (for the eastern region) with NRL.
- BPCL has signed a sale purchase agreement to acquire 36.6% stake in Bharat Oman Refinery Limited (BORL) from its partner for ~Rs. 2,399 crore. Management has stated that all the formalities with respect to the transaction are expected to get completed by June 15, 2021. With this, BORL will become a wholly owned subsidiary of BPCL.
- The Bina Refinery GRM stood at $8/bbl in Q4FY2021 versus $2.14/bbl in Q3FY2021) and reported PAT of Rs. 145 crore versus net loss of Rs. 200 crore in Q3FY2021. FY2021 GRM stood at $6.2/bbl.
- GRM for Numaligarh Refinery stood at $45/bbl in Q4FY2021 (including benefit of excise duty) as compared to $37/bbl in Q3FY2021 and reported PAT of Rs. 900 crore in Q4FY2021 versus Rs. 830 crore in Q3FY2021. FY2021 GRM stood at $37.2/bbl for NRL.
- Outstanding dues from the government stand at only Rs. 300 crore.

Results — Rs cr

Particulars	Q4FY21	Q4FY20	YoY (%)	Q3FY21	QoQ (%)
Net Sales	**76,882**	**68,991**	**11.4**	**66,731**	**15.2**
Total Expenditure	71,824	69,610	3.2	62,426	15.1
Reported operating profit	5,058	-619	NA	4,306	17.5
Adjusted operating profit	**5,058**	**-789**	**NA**	**4,306**	**17.5**
Other Income	1,664	1,157	43.9	1,515	9.9
EBITDA	6,722	538	NA	5,820	15.5
Interest	478	579	-17.4	251	90.3
Depreciation	1,000	947	5.5	994	0.6
Exceptional income/(expense)	6,993	-1,081	NA	-419	NA
Reported PBT	12,237	-2,069	NA	4,156	194.4
Adjusted PBT	5,244	-914	NA	4,576	14.6
Tax	297	-708	NA	1,379	-78.4
Reported PAT	11,940	-1,361	NA	2,778	329.9
Adjusted PAT	**3,924**	**-601**	**NA**	**3,058**	**28.3**
Equity Cap (cr)	209	209		209	
Reported EPS (Rs.)	57.1	-6.5	NA	13.3	329.9
Adjusted EPS (Rs.)	18.8	-2.9	NA	14.6	28.3
Margins (%)			**BPS**		**BPS**
Adjusted OPM	6.6	-1.1	NA	6.5	12.6
Adjusted NPM	5.1	-0.9	NA	4.6	52.2

Source: Company data; Sharekhan Research

Key operating metrics

Particulars	Q4FY21	Q4FY20	YoY (%)	Q3FY21	QoQ (%)
GRM ($/bbl)	6.6	0.8	785.3%	2.5	168.8%
Inventory gain ($/bbl)	4.2	-6.6	NA	1.2	237%
Core GRM ($/bbl)	2.5	7.4	-66.7%	1.2	100%
Refining throughput (mmt)	8.4	8.4	0.0%	7.2	15.9%
Market sales (mmt)	11.8	11.2	5.0%	11.4	4.0%
Refining inventory gain/(loss) – Rs. crore	1,813	-2,965	NA	502	261.2%
Marketing inventory gain/(loss) – Rs. crore	1,829	-1,937	NA	269	579.9%
Forex gain/(loss) – Rs. crore	29	-1,211	NA	76	-61.8%

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector view - Recovery in GRM to mid-cycle level, decent volume growth, and better auto fuel marketing margins bode well for earnings of OMCs

India's consumption of petrol and diesel is expected to grow at a decent rate annually in the medium term, as penetration for two-wheelers and passenger cars improves and GDP growth normalises. We believe OMCs' auto fuel marketing margins would soon normalise to historical levels, as they have started daily auto fuel price revisions. Moreover, gradual reduction of global petroleum product inventories (given an improvement in oil demand and a reduction in refinery run-rates) could improve core refining margin to mid-cycle level of $3-4/bbl over CY2021E-CY2022E. Privatisation of BPCL (is successful) could play a crucial role to align marketing margins on petrol to global standards. All the above factors bode well for sharp earnings growth for Indian OMCs.

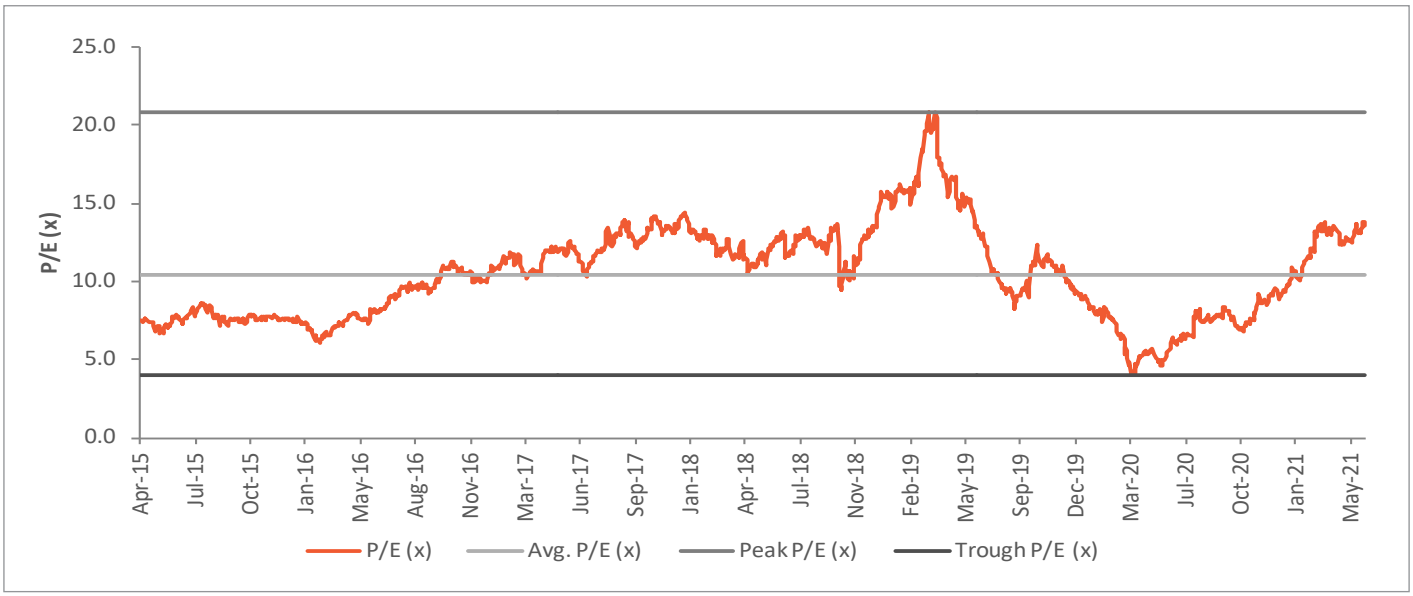
■ Company outlook - Core earnings to improve with cyclical recovery in GRM and normalised marketing margin

We believe the likely decline in refinery utilisation and marketing sales volume in Q1FY2022 (due to lockdown in several states given rising COVID-19 cases) is temporary and core earnings are expected to improve in FY2022. Further, OMCs have resumed daily auto fuel price revision and the same would help to normalise auto fuel marketing margin soon. GRMs are also expected to recover as crack spreads on major petroleum products would improve with higher demand, given rising vaccination drive and opening of economies globally.

■ Valuation - Maintain Buy on BPCL with an unchanged PT of Rs. 520

We have fine-tuned our FY2022-FY2023 earnings estimates, as lower volume assumption in Q1FY2022 gets partially offset by lower interest cost (debt down by 37% in FY2021). We believe privatisation (although could be delayed by three months) could re-rate BPCL, as valuation of marketing assets could get aligned to that of global peers and create long-term value for investors. Hence, we maintain Buy on BPCL with an unchanged PT of Rs. 520. At the CMP, the stock trades 14.5x its FY2022E EPS and 13.6x its FY2023E EPS.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

BPCL is the second largest OMC in India and is engaged in the business of crude oil refining and marketing of petroleum products. The company has a standalone refining capacity of 27.5mmt and retail fuel outlets of 18,637. The company also holds stake in exploration and production (E&P) blocks in Mozambique and Brazil. The company holds stakes in city-gas distribution and LNG import businesses through its joint venture companies.

Investment theme

The government's stake sale to private players would unlock real value of BPCL and could trigger re-rating of the company as valuation of its refining and marketing assets could get re-aligned to global peers. Additionally, expectation of cyclical recovery in GRM, higher marketing margin, and lower interest cost are likely to lead to strong core earnings over FY2022E-FY2023E.

Key Risks

- Prolonged weakness in refining margins and impact on petroleum demand given COVID-19 situation.
- Any further delays in the government's efforts for privatisation of BPCL.

Additional Data

Key management personnel

K. Padmakar	Chairman and Managing Director
N. Vijayagopal	Director - Finance
Arun Kumar Singh	Director – Marketing & Refineries

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp of India	5.7
2	ICICI Prudential Asset Management	2.9
3	HDFC Asset Management Co Ltd	2.2
4	Employee Benefit Trust	2.0
5	SBI Funds Management Pvt Ltd	1.8
6	Vanguard Group Inc/The	1.5
7	BlackRock Inc	1.3
8	Nippon Life India Asset Management	1.2
9	Mirae Asset Global Investments Company	1.0
10	Franklin Resources Inc	0.9

Source: Bloomberg