

Institutional Equity Research

Castrol India

Oil & Gas | India

4QCY21 Result Update | 21 February, 2022

CMP* (Rs)	115
Upside/ (Downside) (%)	21
Bloomberg Ticker	CSTR.L IN
Market Cap. (Rs bn)	114

BUY 

1 Year Target Price: Rs139

Attractive Valuation; Upgrade to BUY

Castrol's (CSTR.L) 4QCY21 revenue grew by 17% YoY and 2% QoQ to Rs10.9bn (10% below our estimate). Despite the 9% increase in crude prices QoQ, the overall cost of raw material for CSTR.L remained largely unchanged. This led to an expansion in gross margin to 49.8% (up 20bps QoQ but down 960bps YoY). Reported EBITDA grew by 3% YoY and 1% QoQ to Rs2.7bn (3% below our estimate). EBITDA margin largely remained flat QoQ but contracted sharply by 316bps YoY to 24.4%. Net profit grew by 1% QoQ and remained flat YoY at Rs1.9bn (3% below our estimate). The company declared a final dividend of Rs3/share (paid interim dividend of Rs2.5/share), on a total dividend of Rs5.5/share, and the implied dividend yield is ~5%. CSTR.L's stock price has corrected more than 23% in the last 3 months, which is inversely proportional to the 19% rise in crude prices. We believe the stock price is factoring a higher crude price scenario (>US\$90/bbl) for the long term. However, we believe in the long term, crude prices will correct from the 7-year high level mainly due to 1) the US-Iran nuclear deal that could bring back 2% additional global oil supply, and 2) OPEC+ countries stick to pump 400k bpd additional oil every month till Sept'22. **Hence, we have tweaked down the 1-year Target Price to Rs139 (earlier Rs146) and upgraded our rating on the stock to a BUY from HOLD.**

Lubricant Demand Sees Recovery

The management indicated that volumes have recovered in 4QCY21 as economic activities resumed; volume stood at 51.5mn ltrs vs. 50mn ltrs in 3QCY21. In terms of volume mix, ~45% was from two-wheelers, ~20-25% from CVs, ~20-25% from passenger cars and the rest pertains to industrials. The delay in agriculture activities and slowdown in tractor sales impacted lubricants' volume from commercial vehicles. We expect lubricants' demand from personal mobility to remain strong, while a revival in demand from the CV segment would depend on the overall recovery in the Indian economy. However, the overall lubricants' demand in the long run is expected to remain soft due to the higher drain interval period to change lubricants. In the long term, an increasing rate of penetration/registration of electric 2W vehicles (mostly scooter segment) could be a drag on volume growth.

Outlook & Valuation

CSTR.L's alliance with Jio-BP retail network provides a long-term volume growth opportunity and scope for market share gain, while a focus to diversify the revenue stream is also a step in the right direction. Thus, we expect the company to clock a volume CAGR of 5% over CY21-CY23E. However, base oil prices are set to be at elevated levels due to the higher crude oil prices and will impact CSTR.L's gross and EBITDA margins. Apart from the implication of base oil prices, forex also plays an important role in margins. Higher crude prices will drag EBITDA margin to 25.8%/27.3% in CY22E/CY23E respectively, compared to the average EBITDA margin of 29% over CY15-CY19. To some extent, the net profit margin would be impacted. **Thus, we lower our PE valuation multiple to 15x (earlier 15.5x) and reduce the target price to Rs139 (earlier Rs146). At 15x CY23E EPS, CSTR.L's valuation looks attractive and is at a discount of 20% to its historical average 1-year forward PE multiple of 18x, and the stock also offers a decent dividend yield of ~5% in CY22E. Further, the balance sheet is robust with net cash of Rs13.2bn (12% of the current market cap). Hence, we upgrade our rating on CSTR.L to a BUY from HOLD, with a reduced target price of Rs139.**

Key Financials

Y/E Dec (Rs mn)	CY19	CY20	CY21	CY22E	CY23E
Revenue	38,768	29,969	41,921	45,931	47,109
EBITDA	11,530	8,142	10,660	11,836	12,858
EBITDA Margin (%)	29.7	27.2	25.4	25.8	27.3
Net Profit	8,274	5,830	7,581	8,428	9,167
Net Profit Margin (%)	21.3	19.5	18.1	18.3	19.5
EPS (Rs)	8.4	5.9	7.7	8.5	9.3
RoE (%)	65.3	41.9	49.6	49.2	51.5
RoCE (%)	68.5	44.1	52.0	51.5	53.6
PE (x)	13.7	19.5	15.0	13.5	12.4
EV/EBITDA (x)	9.0	12.4	9.5	8.3	7.5

Source: Company, RSec Research

Please refer to the last page for change in rating guideline and time horizon for target price.

Recos/View	Old	Revised	Change
Recos	HOLD	BUY	↓
Price Target (Rs)	146	139	↓
↑ Upgrade ↔ Maintain ↓ Downgrade			

Share price (%)	1 mth	3 mth	12 mth
Absolute performance	(7.7)	(14.2)	(10.5)
Relative to Nifty	(4.0)	(11.2)	(25.8)

Shareholding Pattern (%)	Dec-21	Sep-21
Promoter	51.0	51.0
Public	49.0	49.0

Change of Estimates (% change)	CY21E	CY22E
Revenue	0.8	1.1
EBITDA	(1.7)	(1.2)
PAT	(1.3)	(0.8)
EPS	(1.3)	(0.8)

1 Year Stock Price Performance



Note: * CMP as on February 18, 2022

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Quarterly Performance							
Y/E Dec (Rs mn)	4QCY21	4QCY20	YoY (%)	3QCY21	QoQ (%)	RSec Est	Deviation from our est. (%)
Revenue	10,906	9,352	16.6	10,732	1.6	12,096	(9.8)
Inc/dec in stock	385	(240)	(260.4)	(134)	(387.3)	-	
Raw material cons	4,634	3,657	26.7	5,089	(8.9)	6,356	(27.1)
Purchase of traded goods	457	381	19.9	454	0.7	-	
Other expenditure	2,771	2,978	(7.0)	2,698	2.7	3,012	(8.0)
Total Expenditure	8,247	6,776	21.7	8,107	1.7	9,368	(12.0)
EBITDA	2,659	2,576	3.2	2,625	1.3	2,728	(2.5)
Depreciation	209	223	(6.3)	204	2.5	204	2.5
EBIT	2,450	2,353	4.1	2,421	1.2	2,524	(2.9)
Interest	5	8	(37.5)	6	(16.7)	5	0.0
Other Income	124	153	(19.0)	84	47.6	84	47.6
Profit before Extra-Ordinary & Tax	2,569	2,498	2.8	2,499	2.8	2,603	(1.3)
Profit After Tax	1,886	1,877	0.5	1,859	1.5	1,952	(3.4)
EPS (Rs)	1.9	1.9	0.5	1.9	1.5	2.0	(3.4)
Margin Analysis (%)	Change in bps		Change in bps				
EBITDA Margin	24.4	27.5	(317)	24.5	(8)	22.6	183
NPM	17.3	20.1	(278)	17.3	(3)	16.1	116

Source: Company, RSec Research

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Conference Call – Key Takeaways

- **Base Oil (Raw Material):** Base oil prices are still volatile. In CY22, the management expects base oil prices will unlikely soften from the current level mainly due to 1) rising crude prices on geopolitical tensions; and 2) inflationary pressure. However, the company will intervene timely to increase product prices to protect margins.
- **New Launch & Expansion:** Launched Castrol Express Oil Change Service in Oct'21 at Jio-BP Mobility stations. Around 25 of these express oil change facilities are operational and offer swift and reliable oil change service to consumers. The company expanded the Castrol auto service network to 94 centers in 40+ cities across India.
- **Sustainability Agenda 2021:** CSTRL introduced the new optimized packaging design for a small bottle with 20% less plastic consumption. The company also worked to reduce the logistic footprint with reduced temperature blending for select variants. It conducted energy audits at each plant to switch to renewable energy, from non-renewable energy.
- **Capex Guidance:** Capex would be ~25% higher in CY22, compared with CY21. The additional spending would be directed to strengthen the distribution and supply network by developing a vehicle service & maintenance network, which will help to improve sales volume in the long term.
- **No Buyback Plan:** The dividend payout ratio has improved to 72% in CY21, compared with 62% in CY19. Available cash will be utilized to expand new areas (auto service and Jio-BP quick lubes change) and to grow organically. Despite a higher ratio of "sales/cash" in the industry, there is no proposal at the board level for a share buyback.
- **Market Share:** CSTRL has a 20% market share in the bazaar segment, which has increased by 100bps in the last 2 years.
- **Volume:** Volume was subdued in 4QCY21 and stood at 51.5mn ltrs vs. 50mn ltrs in 3QCY21. In terms of volume mix, ~45% was from 2W and 3W, ~20-25% CVs, ~20-25% from passenger cars, and the rest pertains to industrials. Margins are better in passenger vehicles and thus a moderation was seen from commercial vehicles to passenger vehicles. However, commercial vehicles are also important for its portfolio. During 4QCY21, volume was subdued mainly due to 1) OEMs being impacted due to the chips shortage; 2) slowness in industrial volume; and 3) softer demand from tractors in 2HCY21, compared to 2HCY20.
- **EV:** CSTRL is continuously working with OEMs in the four-wheeler space and is already supplying to 2 leading OEMs. Globally, its parent company, CASTROL, has been a leading supplier (>50%) for OEMs for four-wheeler EV fluids. EV is an evolving space and forms a relatively small part of CSTRL's portfolio and remains considerably small for 5-10 years. The company expects electrification to happen first for scooters and three-wheelers, and then for motorcycles. However, CSTRL has more contribution from motorcycles in EV fluids. Currently, it has ~45% market share in the two-wheeler segment, of which scooters constitute ~5-10%.

Key Risks

- Higher oil prices and rupee depreciation
- Delay in revival of automobile sector especially CV sales

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Estimate Change & Revision in Target Price

In CY21, CSTR hiked prices three times and going forward, it has guided for timely price interventions, if base oil prices continue an uptrend. Considering its strategic pricing, we have raised our revenue estimates by 0.8% and 1.1% for CY22E and CY23E, respectively. In the context of higher crude prices, our assumption for the average Brent price has increased to US\$80/US\$75 per bbl, from US\$75/US\$72 per bbl in CY22E/CY23E. Thus, we reduce our EBITDA estimates by 1.7% and 1.2% for CY22E and CY23E, respectively. Higher crude prices will drag the EBITDA margin to 25.8%/27.3% in CY22E/CY23E, compared to the average EBITDA margin of 29% over CY15-CY19. To some extent, the net profit margin would be impacted. **Thus, we lower our PE valuation multiple to 15x (earlier 15.5x) and reduce the target price to Rs139 (earlier Rs146). At 15x CY23E EPS, CSTR's valuation looks attractive and is at a discount of 20% to its historical average 1-year forward PE multiple of 18x, and the stock also offers a decent dividend yield of ~5% in CY22E. Further, the balance sheet is robust with net cash of Rs13.2bn (12% of the current market cap). Hence, we upgrade our rating on CSTR to a BUY from HOLD, with a reduced target price of Rs139.**

Revised vs. Old Estimates

Y/E Dec (Rs mn)	CY22E			CY23E		
	Old	Revised	Change (%)	Old	Revised	Change (%)
Revenue	45,561	45,931	0.8	46,601	47,109	1.1
EBITDA	12,042	11,836	(1.7)	13,016	12,858	(1.2)
EBITDA margin (%)	26.4	25.8	(67)bps	27.9	27.3	(64)bps
Net Profit	8,539	8,428	(1.3)	9,245	9,167	(0.8)
Net Profit margin (%)	18.7	18.3	(40)bps	19.8	19.5	(39)bps

Source: RSec Research

ESG Analysis

While analyzing 20 key criteria (10 points each) under ESG Matrix, we have assigned an overall score of 61% to CSTR. Under **"Environmental Head"**, we have assigned a 45% score, as the company is into the manufacturing of lubricants which pose a great danger to the environment. Under **"Social Head"**, we have assigned 66% score, as the company has received many awards/accolades for its customer excellence, due representation of women in a managerial position and CSR spend. Under **"Governance Head"**, we have assigned a 68% score, as it's a part of BP Group, which maintains a very high standard for corporate governance

For detailed report on our ESG analysis of CSTR, please click here ([please refer to page no.5 for detailed ESG analysis](#)).

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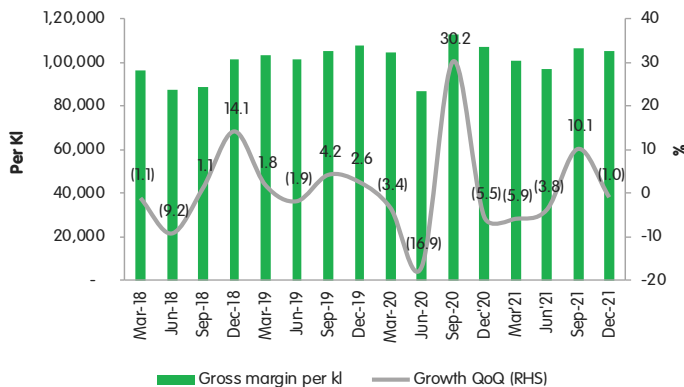
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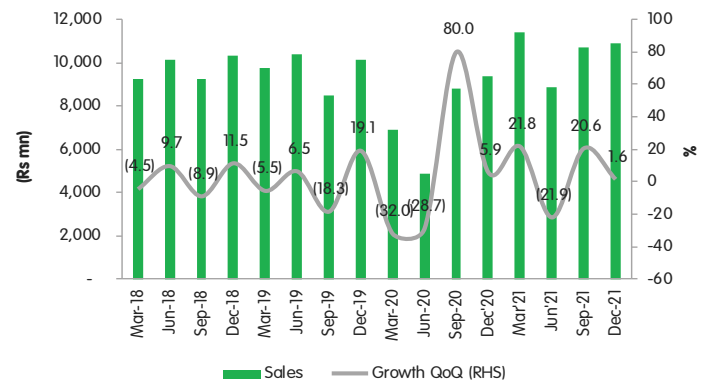
BUY 

1 Year Target Price: Rs139

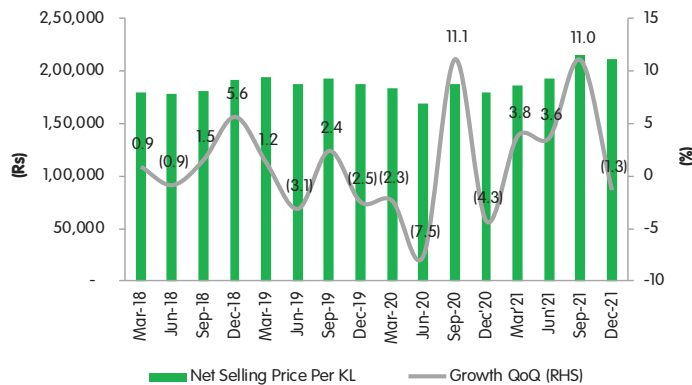
Key Charts

Exhibit 1: Gross Margin Trend


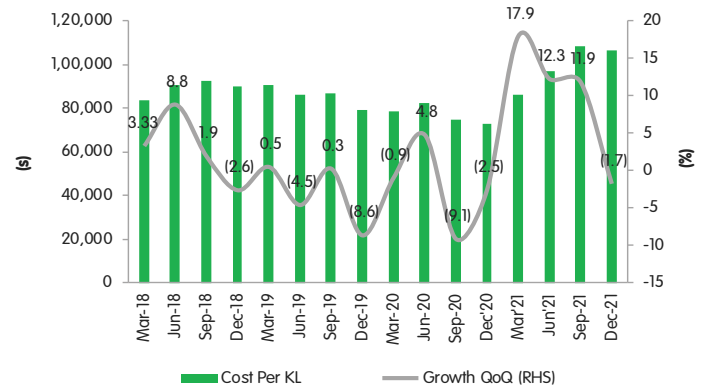
Source: Company, RSec Research

Exhibit 2: Sales Performance Trend


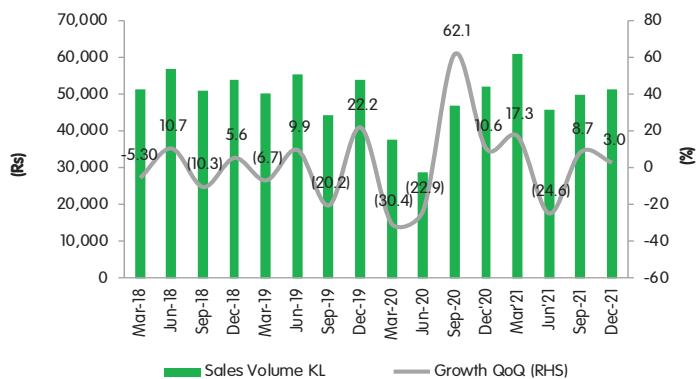
Source: Company, RSec Research

Exhibit 3: Net Selling Price Trend


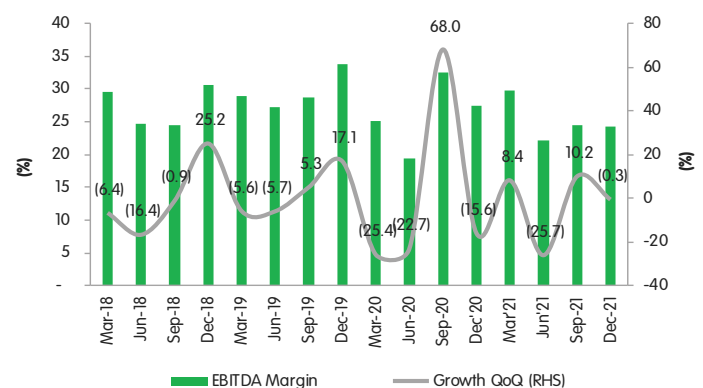
Source: Company, RSec Research

Exhibit 4: Cost Trend


Source: Company, RSec Research

Exhibit 5: Sales Volume Trend


Source: Company, RSec Research

Exhibit 6: EBITDA Margin Trend


Source: Company, RSec Research

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Profit & Loss Statement

Y/E Dec (Rs mn)	CY19	CY20	CY21	CY22E	CY23E
Revenue	38,768	29,969	41,921	45,931	47,109
Growth (%)	(0.7)	(22.7)	39.9	9.6	2.6
Cost of materials	(14,883)	(11,739)	(18,791)	(18,771)	(18,659)
Employee cost	(2,131)	(2,198)	(2,320)	(2,459)	(2,607)
Other expenses	(10,224)	(7,890)	(10,150)	(12,864)	(12,986)
EBITDA	11,530	8,142	10,660	11,836	12,858
EBITDA Margins (%)	29.7	27.2	25.4	25.8	27.3
Growth (%)	7.7	(29.4)	30.9	11.0	8.6
DDA	(697)	(866)	(827)	(1,042)	(1,172)
EBIT	10,833	7,276	9,833	10,795	11,686
Other Income	648	620	484	754	824
Finance cost	(12)	(42)	(24)	(42)	(38)
PBT	11,469	7,854	10,293	11,506	12,472
Tax	(3,195)	(2,024)	(2,712)	(3,078)	(3,305)
PAT	8,274	5,830	7,581	8,428	9,167
Net Profit Margins (%)	21.3	19.5	18.1	18.3	19.5
Growth (%)	16.8	(29.5)	30.0	11.2	8.8
No of equity shares (Mn)	989	989	989	989	989
EPS	8.4	5.9	7.7	8.5	9.3
Dividend Per share	5.5	5.5	5.5	7.0	7.5

Balance Sheet

Y/E Dec (Rs mn)	CY19	CY20	CY21	CY22E	CY23E
Shareholder's funds	13,670	14,142	16,456	17,787	19,536
Share capital	4,946	4,946	4,946	4,946	4,946
Reserves & Surplus	8,724	9,197	11,510	12,842	14,590
Current Liabilities	8,618	9,792	10,584	11,321	11,279
Trade Payable	4,718	5,455	6,206	6,943	6,901
Other Current Liabilities	3,229	3,496	3,646	3,646	3,646
ST Provisions	671	841	732	732	732
Total Liabilities	22,288	23,934	27,040	29,108	30,815
Non-Current Asset	2,855	3,151	3,226	3,352	3,118
Net Fixed Assets	1,997	2,093	2,012	2,225	2,053
Capital Work-in-progress	273	435	500	500	500
Deferred Tax Assets (Net)	585	622	714	628	565
Current Assets	19,433	20,783	23,814	25,756	27,697
Inventories	3,047	3,669	4,917	3,901	4,001
Trade receivables	4,820	1,805	3,117	3,775	3,872
Cash & cash equivalents	9,461	12,741	13,002	15,066	16,741
ST Loans & advances	1,872	2,261	2,471	2,707	2,777
Other current assets	234	308	306	306	307
Total Asset	22,288	23,934	27,040	29,108	30,815

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BUY 

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Cash Flow Statement

Y/E Dec (Rs mn)	CY19	CY20	CY21	CY22E	CY23E
PBT (Reported)	11,469	7,854	10,293	11,506	12,472
Depreciation	697	866	827	1,042	1,172
Interest Expenses	12	42	24	42	38
Other adjustments	-11	83	172	-172	0
Operating Cash flow before WC change	12167	8845	11316	12418	13682
Changes in Working capital	68	3,065	-2,068	945	-246
Cash from Operating activities after WC	12,235	11,910	9,248	13,362	13,436
Tax Paid	(3,195)	(2,024)	(2,712)	(3,078)	(3,305)
Cash Flow from Operating activities	9,040	9,886	6,536	10,285	10,131
Purchase of Fixed assets	(755)	(1,125)	(811)	(1,254)	(1,000)
Cash Flow from Investing Activities	(755)	(1,125)	(811)	(1,254)	(1,000)
Interest paid	(12)	(42)	(24)	(42)	(38)
Dividend Paid	(6,250)	(5,440)	(5,440)	(6,924)	(7,418)
Cash Flow from financing activities	(6,262)	(5,482)	(5,464)	(6,966)	(7,457)
Total Increase/(decrease) in cash	2,023	3,280	261	2,064	1,674
Opening cash & cash equivalents	7,438	9,461	12,741	13,002	15,066
Closing Cash & cash equivalent	9,461	12,741	13,002	15,066	16,741

Key Ratio

Y/E Dec (Rs mn)	CY19	CY20	CY21	CY22E	CY23E
Valuation Ratio (x)					
P/E	13.7	19.5	15.0	13.5	12.4
P/CEPS	12.7	17.0	13.5	12.0	11.0
P/BV	8.3	8.0	6.9	6.4	5.8
Dividend Yield(%)	4.8%	4.8%	4.8%	6.1%	6.5%
EV/Sales	2.7	3.4	2.4	2.1	2.1
EV/EBITDA	9.0	12.4	9.5	8.3	7.5
Per share data (Rs)					
EPS	8.4	5.9	7.7	8.5	9.3
Cash EPS	9.1	6.8	8.5	9.6	10.5
DPS	5.5	5.5	5.5	7.0	7.5
Book Value	13.8	14.3	16.6	18.0	19.8
Returns (%)					
RoCE	68.5	44.1	52.0	51.5	53.6
RoE	65.3	41.9	49.6	49.2	51.5
Turnover Ratio (x)					
Asset Turnover	1.8	1.3	1.6	1.6	1.6
Inventory Days	66.5	103.8	87.2	64.0	66.5
Receivable days	45.4	22.0	27.1	30.0	30.0
Payable days	115.7	169.6	120.5	135.0	135.0
Cash Conversion Cycle	(4)	(44)	(6)	(41)	(39)

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Change in Ratings

We have changed our rating system and included **HOLD** recommendation. We have **BUY, HOLD and SELL** recommendation now.

We have also shifted to **1Year Target Price** from **2Year Target Price**.

Rating History

Date	Reco	CMP	TP
01-Nov-2021	BUY	140	146
21-Oct-2020	BUY	112	169

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BUY 

1 Year Target Price: Rs139

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Rating Guides

Rating	Expected absolute returns (%) over 12 months
BUY	≥10%
HOLD	0% to <10%
SELL	<0%

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