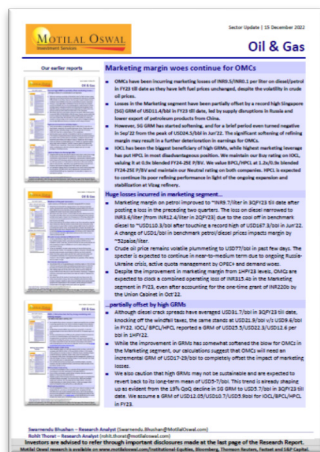
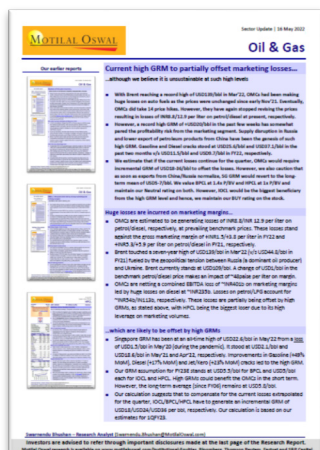


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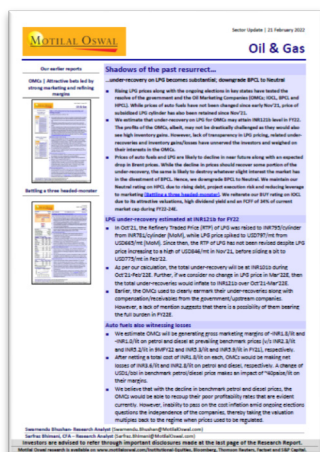
Marketing margin woes continue for OMCs



Current high GRM to partially offset marketing losses



Shadows of the past resurrect



OMCs in a sweet spot...

...as long as crude prices remain soft

- As OMCs stopped changing auto fuel prices since 6th Apr'22, they made an average loss of INR0.68/10.1/lit on petrol/diesel till Dec'22. However, a sharp decline in benchmark prices after that has resulted in gross marketing margins improving to INR9.0/INR11.8 per liter as of May'23.
- Although Singapore GRM (SG GRM) declining to USD3.3/bbl in 1QFY24'td (v/s USD10.8/bbl in FY23) should impact refining performance, our calculations suggest that to compensate for 1USD/bbl decline in SG GRM, gross marketing margins for auto-fuels needs to rise by INR0.65/INR0.59/INR0.42 per liter for IOCL/BPCL/HPCL.
- The current dip in oil prices makes a strong investment case for OMCs. However, any rise in oil prices or cut in retail prices poses a big threat to this thesis.
- HPCL should benefit the most from strong marketing margins; however, it continues to suffer from rising debt and projected execution risk. Hence, we maintain our neutral rating on stock. We reiterate our BUY rating on IOCL, valuing it at 0.9x FY25E P/BV and neutral rating on BPCL, valuing it at 1.2x FY25E P/BV.

Demand concern overshadows the impact of oil production cuts

- OPEC+ has been very proactive in ensuring high oil prices. It has cut oil production by 2mnobpd effective Nov'22 citing uncertainties around global economic and oil market outlook, followed by an additional 1.66mnobpd cut starting May'23.
- Despite these production cuts, Brent has declined below USD75/bbl over the past few days v/s USD93.1/bbl in Oct'22 when the first round of production cut was announced. The decline can be attributable to demand concerns amid rising interest rates and banking crises in the US and Europe.
- Declining crude prices bode well for OMCs, with gross marketing margins at INR9.0/INR11.8 per liter currently (v/s INR2.2/-INR5.9 per liter in FY23) for petrol/diesel. However, we caution that the next OPEC+ meeting is to be held on 4th Jun'23 and further production cuts might cause a spike in oil prices, thus impacting marketing margins adversely. Alternatively, with upcoming state and general elections, the OMCs may cut retail prices, thereby reducing their marketing margins.

Marketing segment gains to offset weak GRMs

- While marketing margins have been improving, concerns have started emerging on the refining segment as SG GRM has declined sharply to ~USD3.3/bbl during 1QFY23'td from USD10.8/bbl in FY23. IOCL has the highest exposure to refining among OMCs and it will be the most hit by declining GRMs.
- However, the SG GRM appears to have bottomed out and is likely to rebound to its long-term mean of USD5-7/bbl. We assume a GRM of USD5/bbl for IOCL and HPCL and USD5.5/bbl for BPCL in FY24-25E.
- Additionally, our calculations reveal that to compensate for 1USD/bbl decline in SG GRM, gross marketing margins for auto-fuels needs to increase by INR0.65/INR0.59/INR0.42 per liter for IOCL/BPCL/HPCL. Hence, we expect marketing segment gains to offset weak GRMs, if margins stay at current levels.

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Valuation and view

- **IOCL** is set to commission various projects over the next two years driving growth further. Refinery projects, currently underway, are expected to be completed as follows: Panipat refinery (25mmtpa) by Sep'24, Gujarat refinery (18mmtpa) by Aug'23, and Baruni refinery (9mmtpa) by Apr'23, according to the earlier guidance. **IOCL is likely to be hit the most among its peers from a decline in refining margin.** We value the stock at 0.9x FY25E P/BV to arrive at our TP of INR105. **We reiterate our BUY rating on the stock.**
- **BPCL:** Capex is pegged at INR100b for FY24E (refining: INR13b; marketing: INR23b; petchem: INR26b; equity investment in its JV subsidiary: INR18b; and the remainder in other smaller projects, including CGDs). It is expected to be at similar levels in FY25. We value the stock at 1.2x FY25E P/BV to arrive at our TP of INR370. **We maintain our Neutral rating on the stock.**
- **HPCL:** Completion of various ongoing projects is expected to drive growth over the next three to five years such as: Bhatinda refinery and Visakhapatnam refinery expansions as well as the new Rajasthan (Barmer) refinery in FY24E. **Despite the growth potential, we maintain our Neutral rating given the project execution risk at Visakhapatnam and rising debt levels.** We value the stock at 0.9x FY25E P/BV to arrive at our TP of INR265.

Exhibit 1: Valuation snapshot for OMCs

Company	Rating	TP (INR)	EPS (INR)			P/E ratio (x)			P/BV ratio (x)			EV/EBITDA ratio (x)			RoE (%)		
			FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
IOCL	Buy	105	8.3	12.0	11.9	10.0	6.9	7.0	0.8	0.8	0.7	6.0	5.8	5.8	8.3	11.2	10.5
BPCL	Neutral	370	23.1	37.3	40.6	15.8	9.8	9.0	1.4	1.3	1.2	5.6	4.5	4.4	9.0	13.5	13.6
HPCL	Neutral	265	-46.7	48.2	44.4	NA	5.3	5.7	1.1	1.0	0.9	NA	7.9	8.0	-18.8	19.8	16.0

Source: MOFSL

Exhibit 2: Singapore GRM softens to USD2/bbl in May'23 to date from the peak of USD24.5/bbl in Jun'22

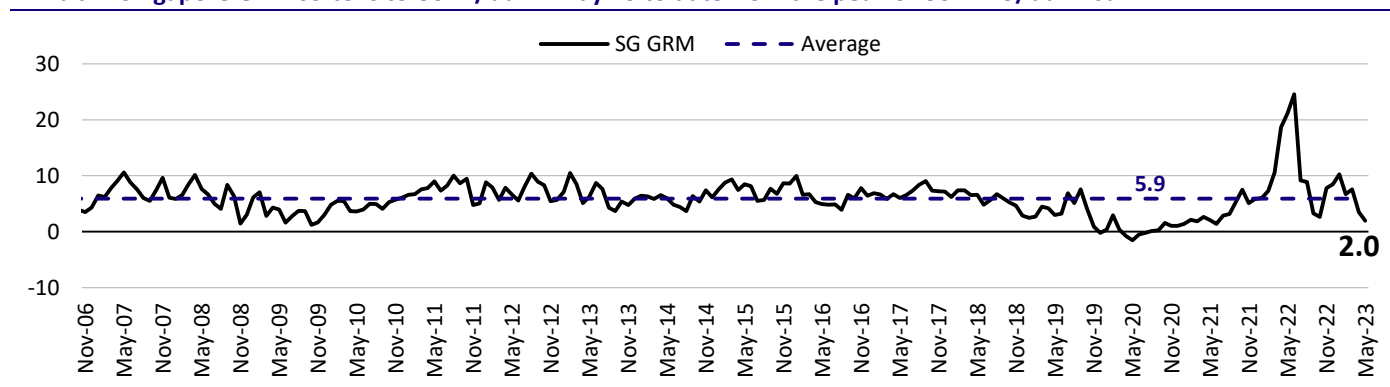
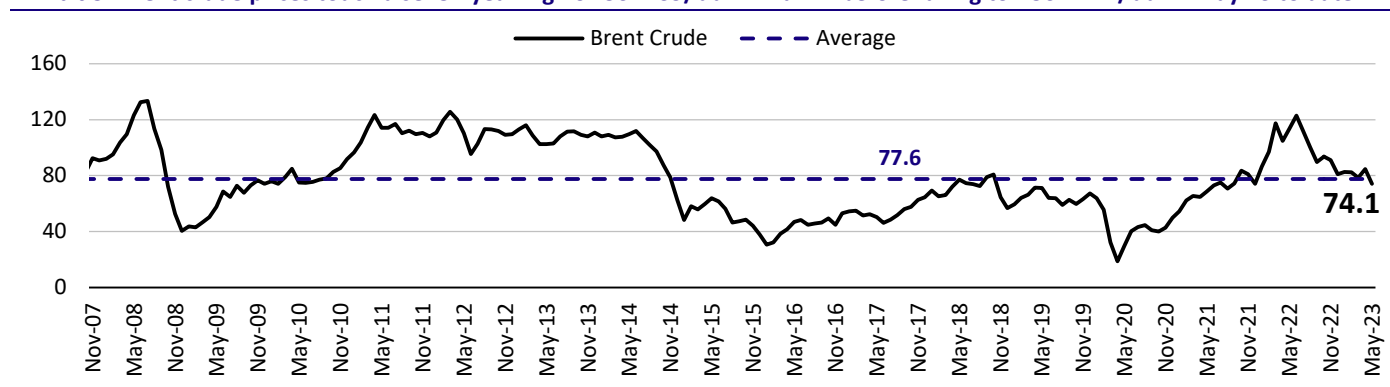
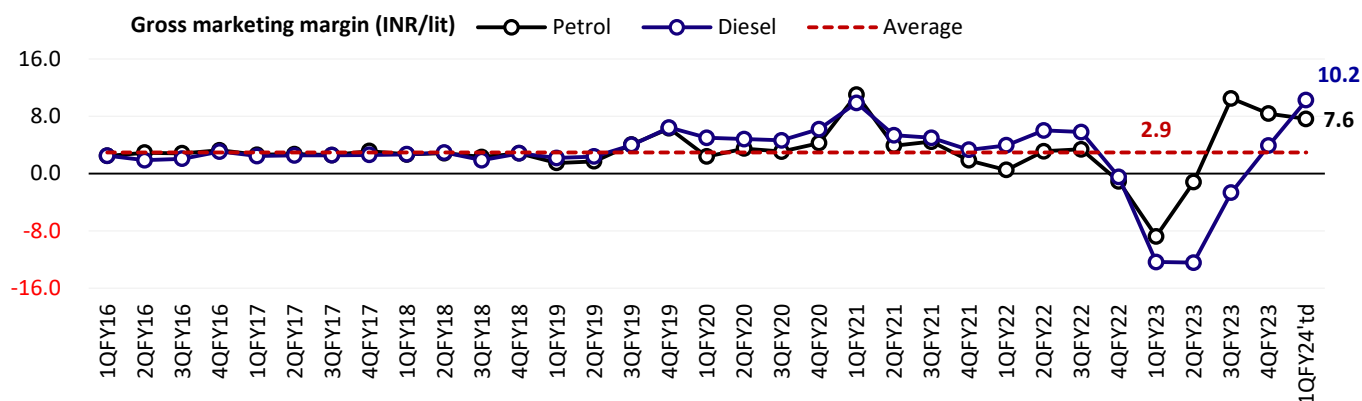


Exhibit 3: Brent crude prices touch a seven-year high of USD139/bbl in Mar'22 before falling to ~USD74.1/bbl in May'23 to date



Source: Reuters, MOFSL

Exhibit 4: Gross marketing margin on Auto fuels at INR7.6/INR10.2 for petrol/diesel in 1QFY24 to date

Source: IOCL, Bloomberg, MOFSL

Exhibit 5: Oil, product prices, and cracks (USD/bbl)

(USD/bbl)	May-22	Feb-23	Mar-23	Apr-23	May-23'td	YoY (%)	MoM (%)
Oil							
WTI	109.6	76.8	73.4	79.4	71.1	-35.1	-10.5
Brent	113.4	82.5	78.4	84.7	74.1	-34.7	-12.5
Dubai	108.1	82.1	78.5	83.4	76.1	-29.6	-8.7
Arab Light-Heavy	1.4	4.1	3.8	1.8	1.6	10.7	-11.4
Gas							
Henry Hub (USD/mmBtu)	8.1	2.4	2.3	2.2	2.1	-74.4	-3.8
Oil to Gas	13.9	34.5	34.0	39.2	35.6	155.5	-9.1
Exchange rate (USD:INR)							
	77.3	82.6	82.3	82.0	81.8	5.8	-0.2
Product cracks (v/s Dubai)							
LPG	-37.2	-20.6	-29.8	-33.6	-33.1	Loss	Loss
Gasoline	32.9	14.1	15.7	13.2	8.4	-74.6	-36.8
Diesel	35.7	17.6	17.2	7.8	3.5	-90.1	-54.9
Jet/kerosene	34.9	24.7	20.7	13.7	11.2	-67.8	-18.2
Naphtha	-9.9	-3.5	-4.6	-10.1	-11.2	Loss	Loss
Fuel oil	-3.0	-18.1	-11.1	-10.1	-8.3	Loss	Loss
SG GRM	21.1	6.7	7.6	3.5	2.0	-90.6	-43.6

Source: Reuters, Bloomberg, MOFSL

IOCL – Financial summary and assumptions (TP: INR105) – BUY

Exhibit 6: Key assumptions

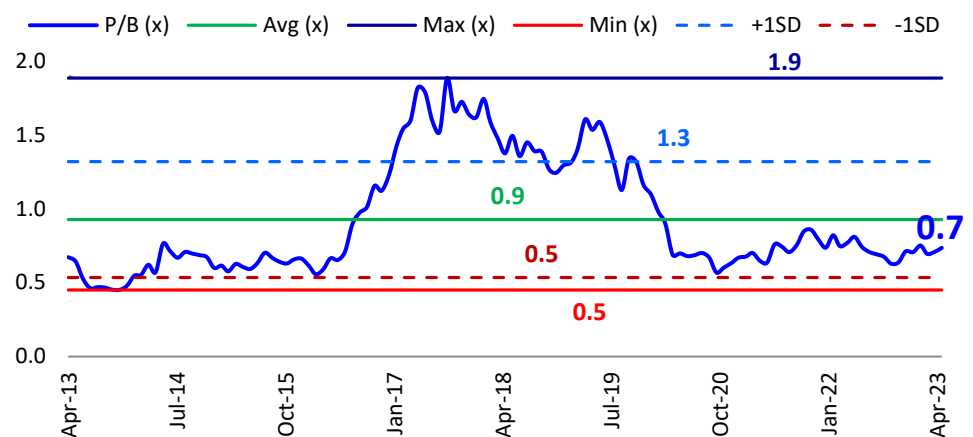
Y/E March	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Exchange rate (USD:INR)	64.5	70.0	70.9	74.3	74.5	80.4	84.4	83.0
Brent Crude Oil (USD/bbl)	57.6	70.1	61.2	44.4	80.5	96.1	90.0	90.0
Domestic direct sales refined products (MMT)	77	80	79	68	74	83	87	90
YoY (%)	4	4	-1	-13	8	13	4	4
Reported GRM (USD/bbl)	8.5	5.4	0.1	5.6	11.3	19.3	5.0	5.0
Singapore GRM (USD/bbl)	7.3	4.9	3.2	0.5	5.0	10.7	6.0	6.0
Premium/(discount) (USD/bbl)	1.2	0.5	(3.1)	5.1	6.3	8.6	(1.0)	(1.0)
Refining capacity utilization (%)	100	104	100	90	98	104	104	104
Total refinery throughput (MMT)	69.0	71.8	69.4	62.4	67.7	71.9	72.0	72.0
YoY (%)	6	4	-3	-10	9	6	0	0
Marketing margin (INR/liter)								
Blended gross marketing margin including inventory	4.4	5.3	6.2	6.8	4.7	(0.8)	4.2	4.2
Consolidated EPS	16.0	12.2	1.7	15.4	18.2	8.3	12.0	11.9

Exhibit 7: Financial summary

(INR b)

Y/E March	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Sales	4215	5282	4838	3639	5893	8,108	9,833	10,371
EBITDA	416	352	168	406	477	375	389	392
Adj. PAT	226	173	24	218	257	117	169	168
Adj. EPS (INR)	16.0	12.2	1.7	15.4	18.2	8.3	12.0	11.9
EPS growth (%)	11.0	-23.7	-86.0	801.4	18.2	-54.7	45.0	-0.7
BV/share (INR)	80.6	79.6	67.6	79.2	94.6	103.2	110.1	117.0
Ratios								
Net D:E ratio	0.5	0.8	1.3	0.9	0.9	0.8	0.7	0.7
RoE (%)	21.0	15.3	2.3	21.0	21.0	8.3	11.2	10.5
RoCE (%)	14.3	10.6	2.4	10.0	12.4	8.6	7.7	6.8
Payout (%)	84.0	88.5	NM	91.1	80.9	38.3	42.0	41.7
Valuations								
P/E ratio (x)	3.9	4.5	9.2	3.6	4.5	10.0	6.9	7.0
P/BV ratio (x)	1.0	1.0	1.2	1.0	0.9	0.8	0.8	0.7
EV/EBITDA ratio (x)	3.4	4.8	11.8	4.5	4.1	6.0	5.8	5.8
Div. yield (%)	20.7	17.2	7.9	22.3	23.4	3.8	6.1	6.0
FCF yield (%)	29.4	3.2	NA	58.3	1.0	16.8	14.1	13.6

Exhibit 8: The one-year forward P/B ratio for IOCL is at ~22% discount to its long-term average



Source: Company, MOFSL

BPCL – Financial summary and assumptions (TP: INR370) – Neutral

Exhibit 9: Key assumptions

Y/E March	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Exchange rate (USD:INR)	64.5	70.0	70.9	74.3	74.5	80.4	84.4	83.0
Crude cost (USD/bbl)	57.1	70.1	61.2	44.4	80.5	98.3	90.0	90.0
Domestic market sales (MMT)	41.2	43.1	43.1	38.7	42.5	48.1	50.0	52.0
YoY (%)	9	5	0	-10	10	13	4	4
Reported GRM (USD/bbl)	6.9	4.6	2.5	4.1	9.1	19.4	5.5	5.5
Singapore GRM (USD/bbl)	7.3	4.9	3.2	0.5	5.0	10.7	6.0	6.0
Premium/(discount) (USD/bbl)	(0.4)	(0.3)	(0.7)	3.6	4.2	8.7	(0.5)	(0.5)
Refinery throughput (MMT)	28.5	31.0	31.9	26.4	32.1	38.3	40.0	40.0
YoY (%)	12	9	3	-17	21	20	4	0
Marketing margin (INR/liter)								
Blended gross marketing margin including inventory	4.0	4.8	4.7	6.9	5.3	(1.0)	4.1	4.2
Consolidated EPS	46.8	40.7	23.8	63.2	52.0	23.1	37.3	40.6

Source: Company, MOFSL

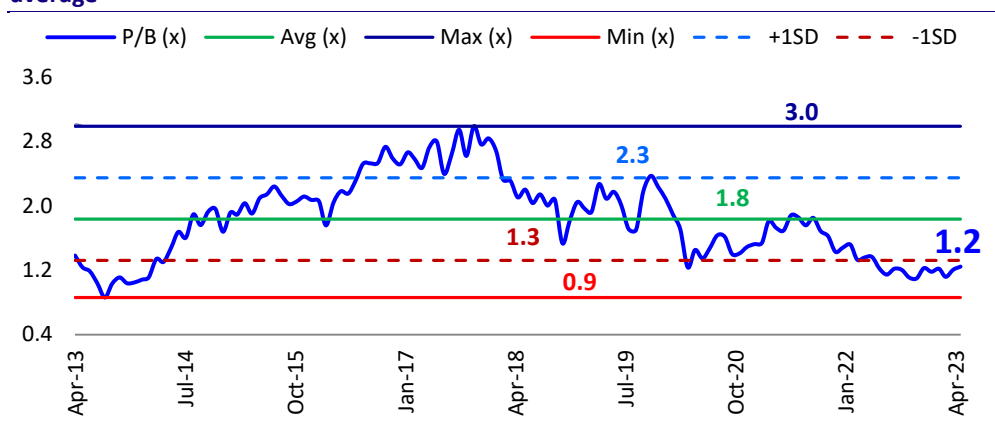
Exhibit 10: Financial summary

(INR b)

Y/E March	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Sales	2,358	2,982	2,846	2,302	3,468	4,716	4,224	4,248
EBITDA	152	158	100	211	189	136	169	172
Adj. PAT	98	85	50	132	109	48	78	85
EPS (INR)	46.8	40.7	23.8	63.2	52.0	23.1	37.3	40.6
EPS growth (%)	3.0	-12.9	-41.6	165.6	-17.8	-55.6	61.3	8.8
BV/share (INR)	175.0	185.2	174.6	255.9	248.0	264.7	285.7	308.6
Ratios								
Net D:E ratio	1.0	1.1	1.5	0.6	1.0	0.8	0.7	0.6
RoE (%)	29.0	22.6	13.2	29.4	20.6	9.0	13.5	13.6
RoCE (%)	13.7	11.8	9.1	15.9	10.9	6.1	8.2	7.9
Payout (%)	52.5	54.6	110.2	95.5	28.7	27.9	43.5	43.6
Valuation								
P/E ratio (x)	7.8	8.9	15.3	5.8	7.0	15.8	9.8	9.0
P/BV ratio (x)	2.1	2.0	2.1	1.4	1.5	1.4	1.3	1.2
EV/EBITDA ratio (x)	4.7	4.5	7.2	3.6	4.0	5.6	4.5	4.4
Div. yield (%)	6.1	5.5	4.8	21.7	4.4	1.8	4.5	4.9
FCF yield (%)	4.7	NA	NA	18.9	NA	22.8	9.0	14.0

Source: Company, MOFSL

Exhibit 11: The one-year forward P/B ratio for BPCL is at ~33% discount to its long-term average



Source: Company, MOFSL

HPCL – Financial summary and assumptions (TP: INR265) – Neutral

Exhibit 12: Key assumptions

Y/E March	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Exchange rate (USD:INR)	64.5	70.0	70.9	74.3	74.5	80.4	84.4	83
Brent crude (USD/bbl)	57.6	70.1	61.2	44.4	80.5	96.1	90.0	90.0
Market sales (MMT)	37	39	40	37	39	43	45	47
YoY (%)	6	5	2	(8)	7	10	4	4
GRM (USD/bbl)	7.4	5.0	1.0	3.9	7.2	11.2	5.0	5.0
Singapore GRM (USD/bbl)	7.3	4.9	3.2	0.5	5.0	10.7	6.0	6.0
Premium/(discount) (USD/bbl)	0	0	(2)	3	2	0.5	(1.0)	(1.0)
Total Refinery throughput (MMT)	18.3	18.4	17.2	16.4	14.0	18.9	24.0	24.0
YoY (%)	3	1	-7	-4	-15	35	27	0
Refining capacity utilization (%)	116	117	109	104	88	84	98	98
Blended marketing margin including inventory (INR/liter)	3.6	4.3	4.0	6.3	4.3	(0.6)	4.5	4.5
Consolidated EPS	47.4	43.9	23.9	70.0	47.9	-46.7	48.2	44.4

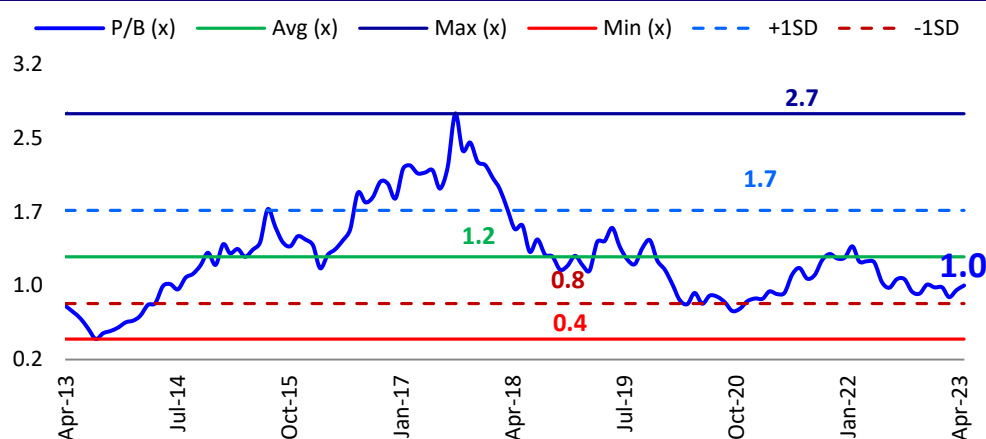
Source: Company, MOFSL

Exhibit 13: Financial summary

Y/E March	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Sales	2195	2755	2691	2332	3499	4327	4257	4271
EBITDA	107	115	57	160	102	-60	137	140
Adj. PAT	72	67	36	107	73	-71	73	68
Adj. EPS (INR)	47.4	43.9	23.9	70.0	47.9	-46.7	48.2	44.4
EPS growth (%)	-12.4	-7.3	-45.6	192.8	-31.6	PL	LP	-7.7
BV/share (INR)	167.5	199.5	203.3	249.8	271.6	225.0	261.5	294.5
Ratios								
Net D:E ratio	0.8	0.8	1.3	1.1	1.1	1.9	1.7	1.6
RoE (%)	31.0	23.9	11.9	30.9	18.4	-18.8	19.8	16.0
RoCE (%)	15.8	12.9	12.0	14.9	8.3	-6.7	7.4	6.4
Payout (%)	42.8	43.8	77.2	31.0	27.9	0.0	24.2	25.8
Valuations								
P/E ratio (x)	5.4	5.8	10.6	3.6	5.3	NA	5.3	5.7
P/BV ratio (x)	1.5	1.3	1.2	1.0	0.9	1.1	1.0	0.9
EV/EBITDA ratio (x)	5.4	5.6	13.8	5.1	8.1	NA	7.9	8.0
Div. yield (%)	6.4	6.0	3.7	8.5	5.3	0.0	4.6	4.5
FCF yield (%)	11.2	NA	NA	16.1	9.8	NA	1.8	2.2

Source: Company, MOFSL

Exhibit 14: The one-year forward P/B ratio for HPCL is at ~17% discount to its long-term average



Source: Company, MOFSL

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Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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