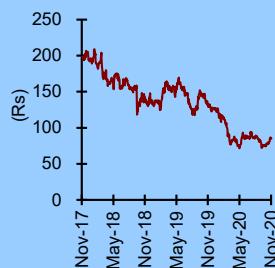


Sector update

Oil & Gas and
Petrochemicals

IOCL (ADD)

Target price: Rs87



INDIA

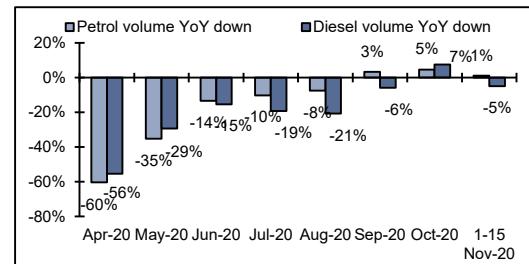
Refining & marketing

Oil rise prompts price hikes to keep marketing margins high

For the first time in FY21-TD in Oct'20, consumption of petroleum products was up 2.5% YoY; diesel was up 7.4% YoY and petrol up 4.5% YoY. This meant that despite Oct refinery utilisation being highest in FY21-TD, auto fuel inventories fell further in Oct'20. Consumption of diesel was down 5% YoY, but on a high base and petrol was up modestly in 1-15 Nov. Recent oil price rebound has led to auto fuel retail price hikes to keep net marketing margins high; oil price rise will also mean inventory gains in Q3FY21E. With GRM continuing to be weak, despite recovery in diesel cracks, strong marketing margins are needed to ensure integrated margins at reasonable level. Retail price hikes augur well for OMCs. We reiterate ADD on IOC given its cheap valuation and high dividend.

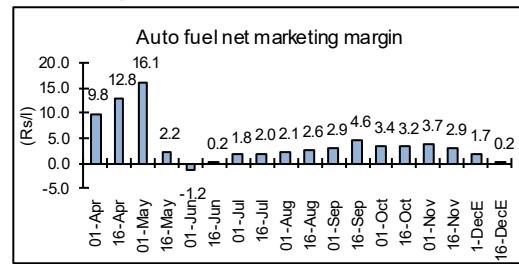
- **Diesel consumption up YoY in Oct but down in 1-15 Nov:** In Oct'20, for the first time in FY21-TD, consumption of petroleum products was up 2.5% YoY (down 16% YoY in FY21-TD), diesel up 7.4% YoY (down 21% YoY in FY21-TD) and petrol up 4.5% YoY (down 17% in FY21-TD); strong diesel growth is on low base of Oct'19, when it was down 7.3% YoY. Industrial fuels demand was up 5.2% YoY driven by rise in fuel oil, naphtha and bitumen demand by 12-49% YoY. Diesel consumption is down 5% YoY but on a high base and petrol modestly up YoY in 1-15 Nov. **Diesel consumption's 2-year CAGR is higher at 1.8% in Nov vs minus 0.2% in Oct'20.**
- **Demand rise & exports exceeding output surplus led to auto fuel inventory fall:** Strong auto fuel demand growth helped absorb production rise from refinery utilisation rising to FY21-TD peak of 88% in Oct'20. Together with auto fuel exports exceeding production surplus, it helped further reduce auto fuel inventories. Petrol and diesel inventories were down 0.2-1.4mmt MoM in Oct'20; diesel inventory fall in Oct'20 is the steepest in FY21-TD.

Auto fuel consumption up 4.5-7.4% YoY in Oct'20 but flat/down YoY in 1-15 Nov



Source: PPAC, Reuters, I-Sec research

More price hikes required to prevent net margin fall to Rs0.23/l on 16-Dec'20



Source: PPAC, Reuters, I-Sec research

- **Further price hikes needed to keep auto fuel marketing margins high:** Auto fuel net marketing margin is at Rs4.2/l in FY21-TD, Rs3.34/l in Q3FY21-TD and Rs3.59/l on 25-Nov'20. However, rise in international auto fuel prices would have meant net margin fall to Rs1.05/l on 1-Dec'20 and minus Rs0.45/l on 16-Dec'20. Hike in petrol and diesel retail price by Rs0.53-0.95/l during 20-24 Nov'20 has meant net margin is now estimated at Rs0.23-1.73/l on 16-Dec and 1-Dec'20. Further price hikes are required and we are hopeful of the same to ensure net margins remain at Rs2.0-2.5/l. Rise in international oil and product price will also lead to inventory gains in Q3FY21E. We estimate OMCs' product inventory gain at Rs4.5-8.8bn in Q3-TD.
- **Singapore GRM weak despite diesel cracks recovery as petrol cracks correct:** Singapore GRM is up QoQ in Q3-TD but down MoM to US\$1.1/bbl in Nov-TD from 8-month high of US\$1.6/bbl in Oct. Diesel cracks are down 28% QoQ to US\$3.0/bbl in Q3-TD, but up 45% MoM to US\$3.6/bbl in Nov-TD driven by 20% fall in US inventory from 37-year high in end-Jul'20 to just 0.3% above 5-year average level. However, petrol cracks are down 2% QoQ to US\$4.3/bbl in Q3-TD and are at 6-month low of US\$3.25/bbl in Nov-TD, hit by demand recovery reversal in the US and Europe.

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Price hikes likely to keep marketing margins high

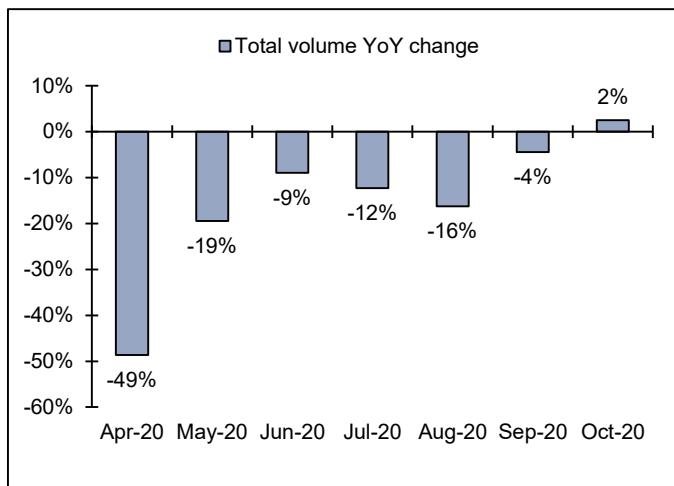
Strong demand absorbed high throughput to drive inventory fall

Total demand up 2.5% & auto fuel demand up 4.5-7.4% YoY in Oct'20

In Oct'20, for the first time in FY21-TD, consumption of:

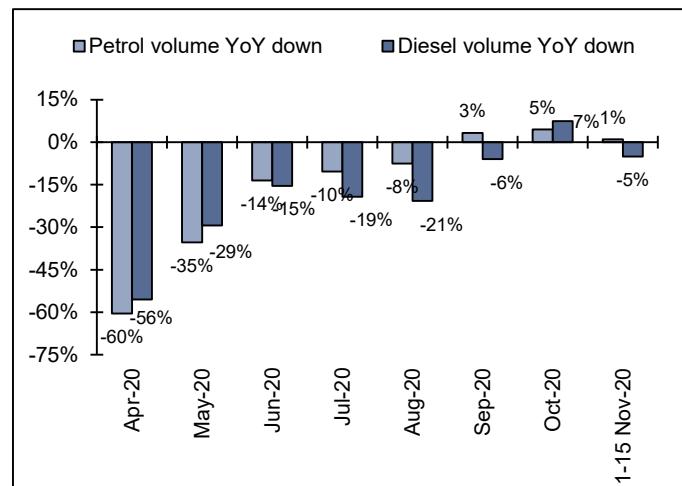
- Petroleum products was up 2.5% YoY vs 16% YoY fall in FY21-TD.
- Diesel was up 7.4% YoY vs 21% YoY decline in FY21-TD. Strong rise in diesel consumption is on low base of Oct'19, when it was down 7.3% YoY.
- Petrol was up 4.5% YoY vs 17% YoY fall in FY21-TD.

Chart 1: Total petroleum products consumption up in Oct'20 for the first time in FY21-TD



Source: PPAC, I-Sec research

Chart 2: Auto fuel demand up 4.5-7.4% YoY in Oct'20; down/flat in 1-15 Nov'20



Source: PPAC, Reuters, I-Sec research

Diesel demand down 5% YoY in 1-15 Nov on high base; petrol up

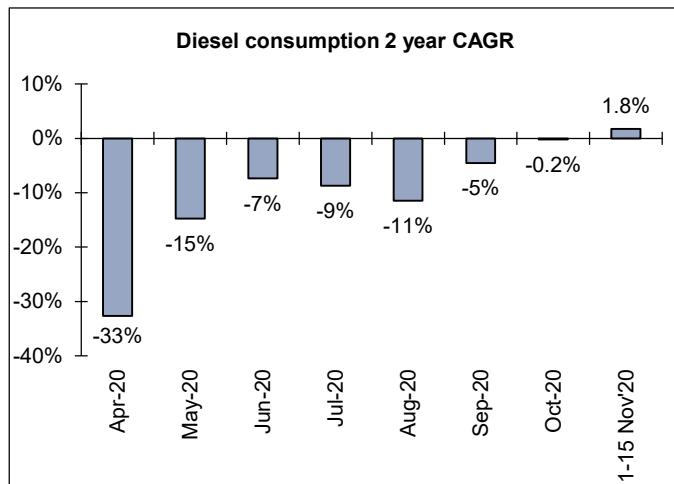
Diesel consumption is down 5% YoY while petrol is marginally up YoY during 1-15 Nov'20. The fall in diesel consumption is however on a high base of Nov'19 when consumption was up 9% YoY.

2-year diesel CAGR at 1.8% in 1-15 Nov'20 vs minus 0.2% in Oct'20

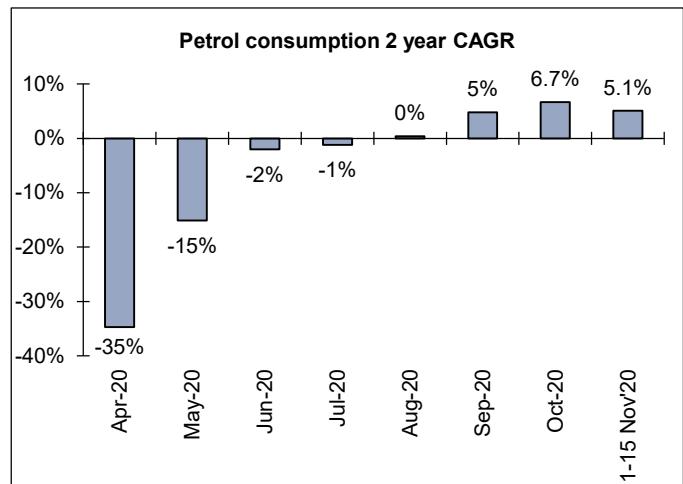
In our view, one should look at 2-year diesel consumption CAGR in Oct'20 and 1-15 Nov'20 given that rise in diesel consumption in Oct'20 was on a low base (down 7.3% YoY in Oct'19) and the fall in 1-15 Nov'20 is on a high base (up 9% YoY in Nov'19). 2-year diesel consumption CAGR is 1.8% in 1-15 Nov'20 vs minus 0.2% in Oct'20.

2-year petrol CAGR at 5.1% in 1-15 Nov'20 vs 6.7% in Oct'20

2-year petrol consumption CAGR at 5.1% in 1-15 Nov'20 is lower than 6.7% in Oct'20. Petrol consumption growth of 4.5% YoY in Oct'20 was on a base of 8.9% YoY rise in Oct'19, while the rise of 1% YoY in 1-15 Nov'20 is on a base of 9.3% YoY rise in Nov'20.

Chart 3: Diesel consumption CAGR at 1.8% in 1-15 Nov'20 vs minus 0.2% in Oct'20

Source: PPAC, Reuters, I-Sec research

Chart 4: Petrol consumption CAGR 5.1% in 1-15 Nov'20 vs 6.7% in Oct'20

Source: PPAC, Reuters, I-Sec research

Consumption of transportation and industrial fuels up 2-5% YoY in Oct

In Oct'20 consumption of:

- Transportation fuels (petrol, diesel, jet fuel and lubes) was up 2.4% YoY with jet fuel down 49.2% YoY

Table 1: Transportation & industrial fuel volumes up 2-5% YoY in Oct'20

	Oct-20	Oct-19	YoY change
Transportation fuels	10.3	10.1	2.4%
Industrial fuels	4.0	3.8	5.2%
Subsidised fuels	2.6	2.5	1.7%
Others	0.9	1.0	-5.2%
Total	17.8	17.3	2.5%

Source: PPAC, I-Sec research

- Industrial fuels was up 5.2% YoY driven by rise in fuel oil, naphtha and bitumen consumption by 12%, 15% and 49% YoY, respectively; petcoke was down 16% YoY.
- Other fuels was down 5.2% YoY.
- Subsidised fuels such as LPG and kerosene was up 1.7% YoY.

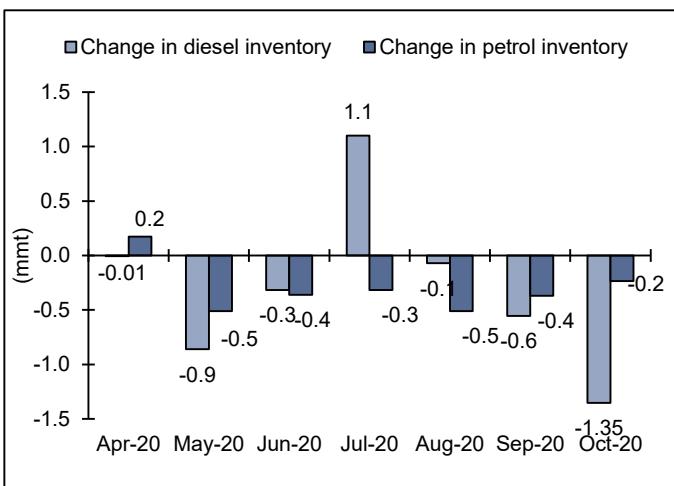
Auto fuel inventory down on demand rise & exports exceeding surplus

Strong auto fuel demand growth in Oct'20 helped absorb production rise from refinery utilisation being at the highest level in FY21-TD of 88% in Oct'20. Strong auto fuel demand growth together with auto fuel exports exceeding production surplus helped further reduce auto fuel inventories. Both petrol and diesel inventories are down 2.1mmt from levels in Mar'20 with fall in inventories being 0.2-1.35mmt MoM in Oct'20. **Implied diesel inventory fall of 1.35mmt in Oct'20 is the steepest in FY21-TD.**

Other products' inventories up in Oct'20 but rise most modest in FY21

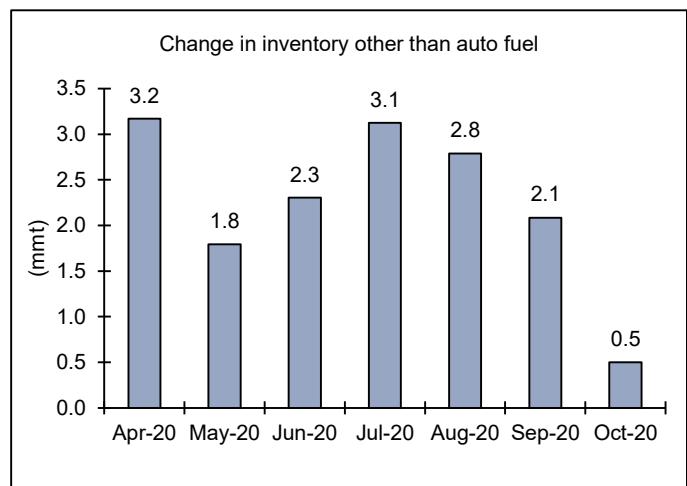
Inventories of products other than auto fuels have risen every month in FY21-TD driven mainly by rise in FO and petcoke inventories. Other products' inventories were up even in Oct'20 but the rise at 0.5mmt MoM was the most modest in FY21-TD.

Chart 5: Petrol & diesel inventories down 0.2-1.35mmt MoM in Oct'20; diesel fall in Oct steepest



Source: PPAC, I-Sec research

Chart 6: Other products' inventories were up even in Oct'20 but rise was most modest in FY21



Source: PPAC, I-Sec research

Oil price rise prompts price hikes to keep marketing margins high

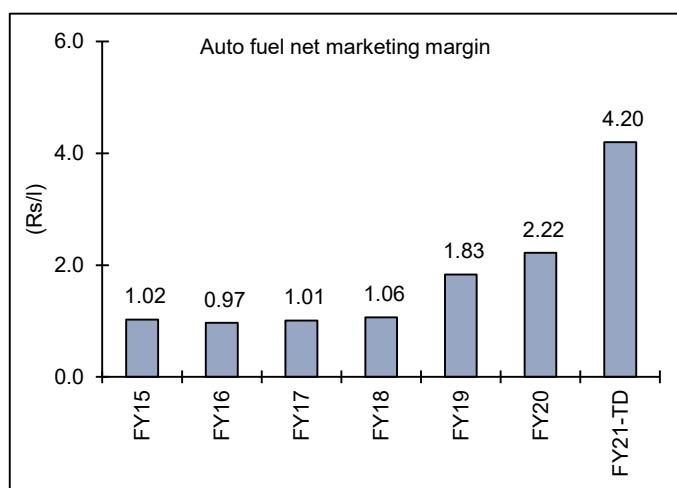
International oil price rise will lead to inventory gains in Q3FY21E

The newsflow on multiple vaccines for Covid-19 with high efficacy has led to recovery in oil prices. Rise in international oil and product prices may lead to inventory gains for OMCs in Q3FY21E. **We estimate OMCs' product inventory gain at Rs4.5-8.8bn in Q3-TD based on international prices up to 25-Nov'20 and at Rs7.1-13.8bn at latest prices.** Crude inventory gains that boost GRM are also likely.

Net margin at Rs1.05/l on 1-Dec & in the red later if no price hikes

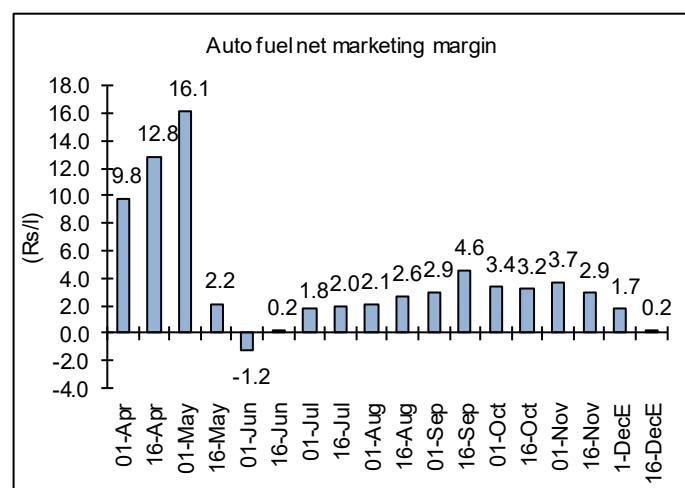
Auto fuel net marketing margins are estimated at Rs4.2/l in FY21-TD, Rs3.34/l in Q3FY21-TD and Rs3.59/l on 25-Nov'20. Net margin would have declined to Rs1.05/l on 1-Dec'20 and minus Rs0.45/l on 16-Dec'20 due to rise in international oil prices had retail price not been hiked.

Chart 7: OMCs' auto fuel net marketing margin is at Rs4.2/l in FY21-TD vs Rs2.22/l in FY20



Source: PPAC, Reuters, I-Sec research

Chart 8: OMCs' net margin to fall from Rs3.59/l to Rs1.73-0.23/l on 1-Dec & 16-Dec if no further hikes



Source: PPAC, Reuters, I-Sec research

Price hikes during 20-24 Nov'20 boosted net margin to Rs0.23-1.73/l

Hike in petrol and diesel retail price by Rs0.53-0.95/l during 20-24 Nov'20 has meant net margin is now estimated at:

- Rs-1.73/l on 1-Dec'20 based on international prices in 16-25 Nov'20.
- Rs0.23/l on 16-Dec based on international prices on 25-Nov'20.

Price hikes need to continue to keep marketing margins high

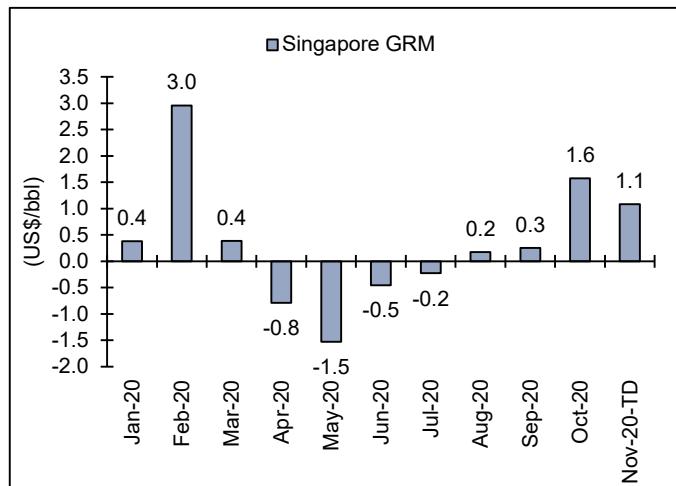
After price hikes during 20-24 Nov'20, there was no price hike on 25-Nov'20. Retail price hikes need to continue to ensure net marketing margin are at Rs2.0-2.5/l in order to compensate for the weakness in GRMs. CFO of IOC, in an interview, when asked about margin marketing outlook had also commented that any weakness in refining margins is being made up through high marketing margins and the situation may continue. We are, therefore, hopeful that retail price hikes will soon restart.

GRM remains weak despite diesel recovery as petrol cracks fall

Singapore GRM up QoQ but down from 8-month high in Nov'20-TD

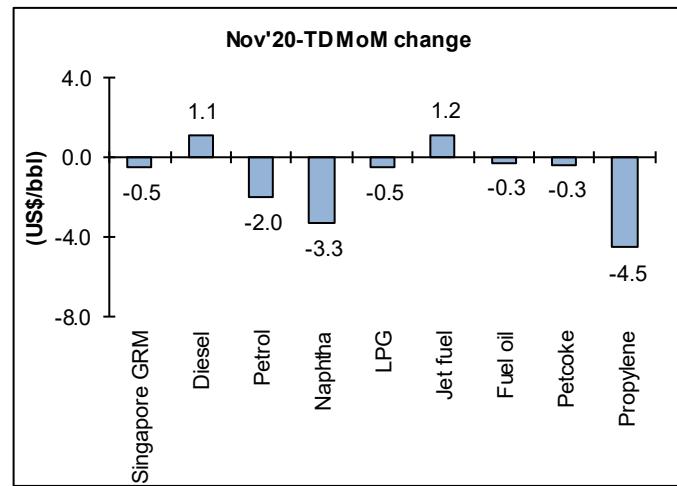
Reuters' Singapore GRM, which is minus US\$0.02/bbl in FY21-TD, is up QoQ at US\$1.36/bbl in Q3FY21-TD from US\$0.06/bbl. However, Singapore GRM is down MoM to US\$1.08/bbl in Nov'20-TD from 8-month high of US\$1.57/bbl in Oct-20.

Chart 9: Singapore GRM down to US\$1.1/bbl in Nov'20-TD from 8-month high in Oct'20



Source: Reuters, I-Sec research

Chart 10: All product cracks except diesel and jet fuel down MoM in Nov'20-TD



Source: Reuters, I-Sec research

All cracks except diesel and jet fuel down MoM in Nov'20-TD

MoM fall in Singapore GRM in Nov'20-TD is due to:

- Fall in petrol cracks by US\$2.0/bbl MoM
- Fall in naphtha cracks by US\$3.3/bbl MoM
- Fall in fuel oil cracks by US\$0.3/bbl MoM
- Fall in propylene cracks by US\$4.5/bbl MoM
- Fall in LPG cracks by US\$0.5/bbl MoM
- Fall in petcoke cracks by US\$0.3/bbl MoM

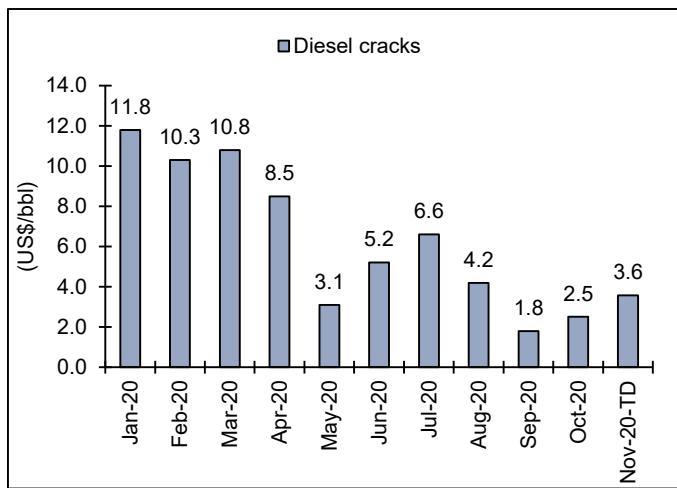
Diesel and jet fuel cracks are up US\$1.1-1.2/bbl MoM in Nov'20-TD

Diesel cracks down QoQ but up 45% MoM in Nov-TD on inventory fall

Diesel cracks at US\$3.0/bbl are down 28% QoQ in Q3FY21-TD. However, diesel cracks have recovered to US\$3.6/bbl in Nov'20-TD, up 45% MoM from US\$2.5/bbl in Oct'20 and up 100% from low of US\$1.8/bbl in Sep'20. **Diesel cracks are over US\$4/bbl in the last six days and at US\$4.46/bbl on 25-Nov'20.** Diesel cracks recovery has been driven by:

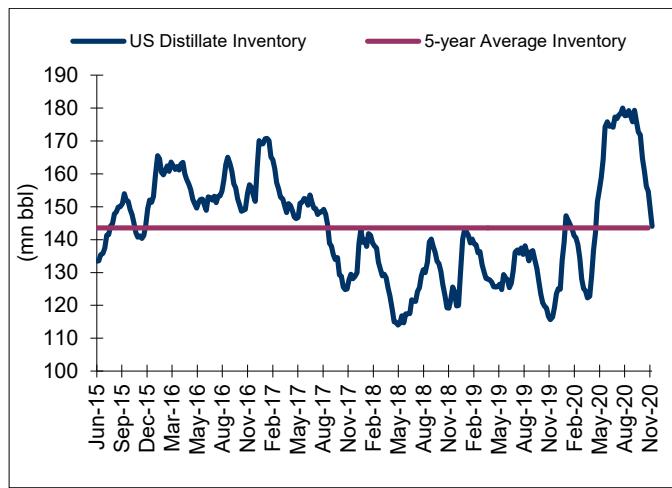
- Decline in US distillate inventory by 20% from 37-year high level in end-Jul'20 to just 0.3% above 5-year average level.

Chart 11: Diesel cracks are at US\$2.5-3.6/bbl in Oct-Nov'20-TD from a low of US\$1.8/bbl in Sep'20



Source: Reuters, I-Sec research

Chart 12: US distillate inventory down 20% from recent high; just 0.3% above 5-year average now



Source: EIA, I-Sec research

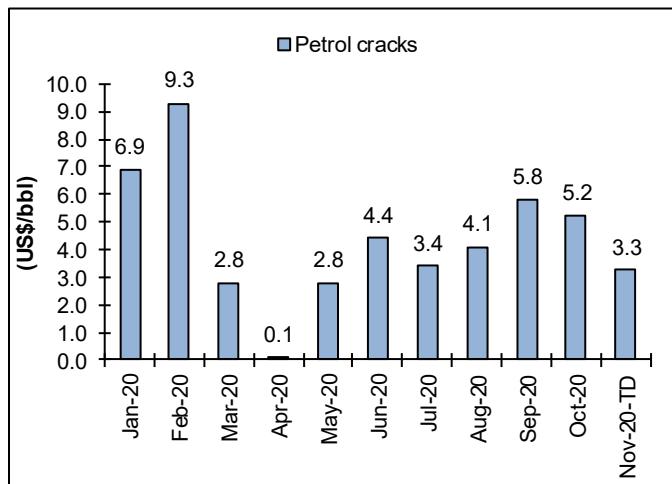
- India diesel consumption was up 7.4% YoY in Oct'20 vs fall of 6% YoY in Sep'20; US diesel consumption decline at 6.7% YoY in Oct'20 and 6.5% YoY in Nov'20-TD was less steep than 8.8% YoY fall in Sep'20.
- US distillate yield, which surged to 36% in Apr'20, is now back to year-ago level of 25.5% in Oct'20. Distillate yield at 25.1% in Nov'20-TD is 1.1pct lower YoY.

Petrol cracks down 2% QoQ in Q3-TD & at 6-month low in Nov'20-TD

Petrol cracks touched 7-month high of US\$5.8/bbl in Sep'20 but fell to US\$5.2/bbl in Oct'20. Petrol cracks are now down 38% MoM to US\$3.3/bbl in Nov'20-TD and 2% QoQ to US\$4.3/bbl in Q3FY21-TD, hit by the second wave of Covid-19 infections causing demand recovery reversal in the US and Europe as follows:

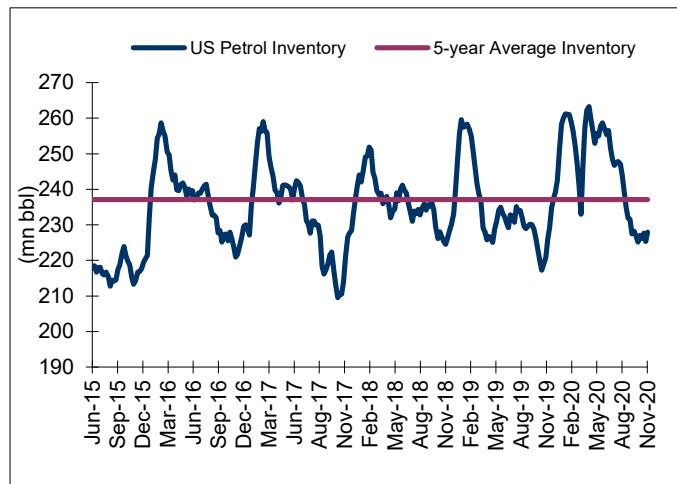
- In US, gasoline demand was down 9.3% YoY in Oct'20 and 8.1% YoY in Nov'20-TD vs 7.7% YoY decline in Sep'20.
- In Spain, petrol demand was down 15.6% YoY in Oct'20 vs 6.6% YoY decline in Sep'20.

Chart 13: Petrol cracks at 6-month low of US\$3.3/bbl in Nov'20-TD, down from US\$5.8/bbl in Sep'20



Source: Reuters, I-Sec research

Chart 14: US gasoline inventory at 3.8% below 5-year average level



Source: EIA, I-Sec research

Oct'20 PPAC data update

Demand up YoY in Oct'20; diesel recovery reversal in Nov'20

Consumption up YoY for the first time in FY21-TD in Oct'20

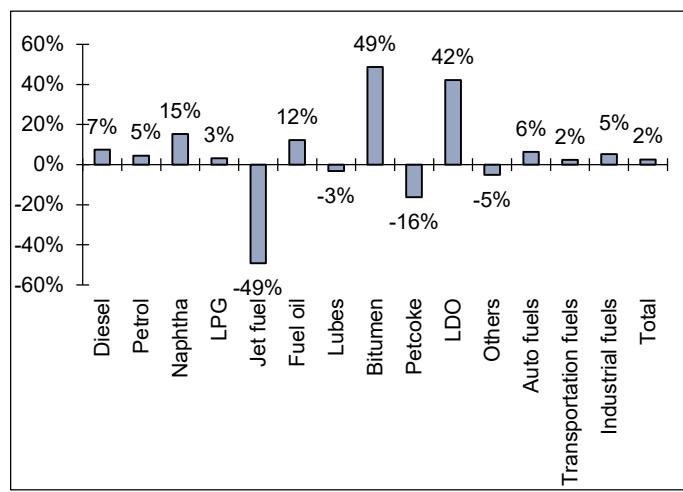
In Oct'20, total petroleum product consumption was up 2.5% YoY, the first monthly YoY rise in FY21-TD. Petrol and diesel consumption was up YoY in Oct'20. Industrial fuel consumption was up 5.2% YoY in Oct'20 vs 7.5% YoY fall in Sep'20.

Total volumes up 2.5% YoY; petrol and diesel up 4.5-7.4% YoY

As per data released by the Petroleum Planning & Analysis Cell (PPAC) of the Petroleum Ministry for Oct'20, Indian consumption of:

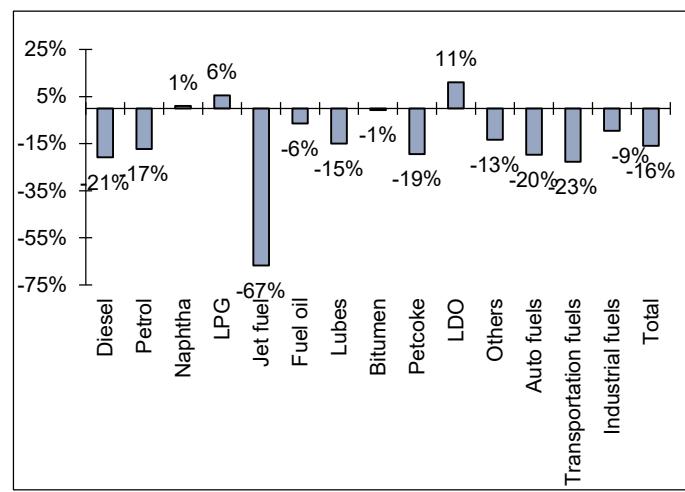
- Petroleum products was up 2.5% YoY (down 4.3% YoY in Sep'20)
- Diesel was up 7.4% YoY (down 6% YoY in Sep'20).
- Petrol was up 4.5% YoY (3.3% YoY in Sep'20).
- Petcoke was down 16.3% YoY (23.3% YoY in Sep'20).
- Jet fuel was down 49.2% YoY (52% YoY in Sep'20).
- LPG was up 3.2% YoY (4.8% YoY in Sep'20).

Chart 15: Oct'20 total consumption up 2.5% YoY; petrol and diesel up 5-7% YoY



Source: PPAC, I-Sec research

Chart 16: FY21-TD consumption of petrol and diesel down 17-21% and total 16%; LPG up 6% YoY



Source: PPAC, I-Sec research

Consumption of all products except kerosene & lubes up MoM

Indian petroleum product consumption was up 15% MoM and 2.5% YoY in Oct'20. In Oct'20 consumption of:

- Diesel was up 27% MoM and 7.4% YoY.
- Petrol was up 8% MoM and 4.5% YoY.
- Jet fuel was up 13% MoM but down 49% YoY.
- Fuel oil was up 9% MoM and 12% YoY.
- Petcoke was up 4% MoM but down 16% YoY.

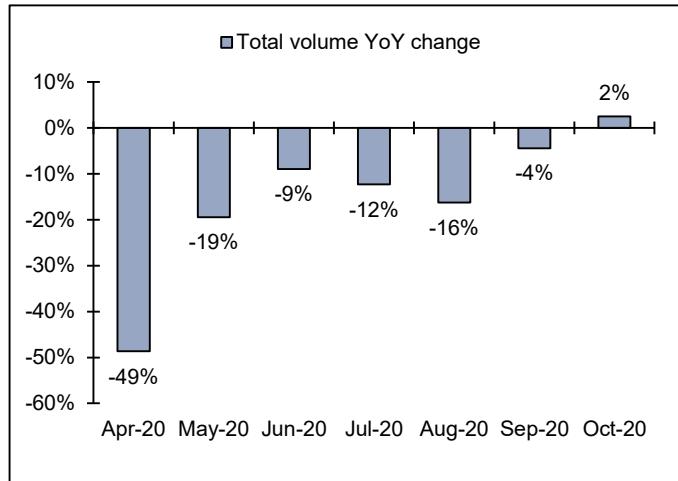
- Kerosene was down 17% MoM and 18% YoY.
- Lubes was down 9% MoM and 3% YoY.

Diesel consumption down 5% YoY in Nov'20-TD; petrol marginally up

As per press reports in Nov'20-TD:

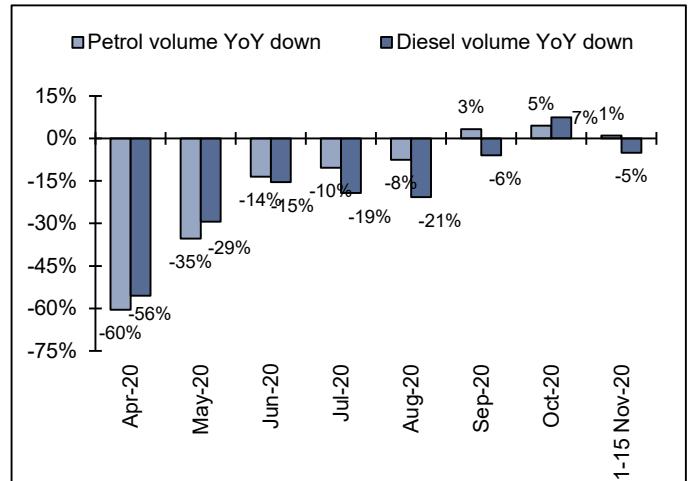
- Petrol consumption was marginally up YoY.
- Diesel consumption was down 5% YoY.

Chart 17: Total petroleum products consumption up for the first time in FY21-TD in Oct'20



Source: PPAC, I-Sec research

Chart 18: Auto fuel demand recovery reversed in Nov'20-TD



Source: PPAC, Reuters, I-Sec research

FY21-TD total consumption down 16% and auto fuels down 17-21%

In FY21-TD, Indian consumption of:

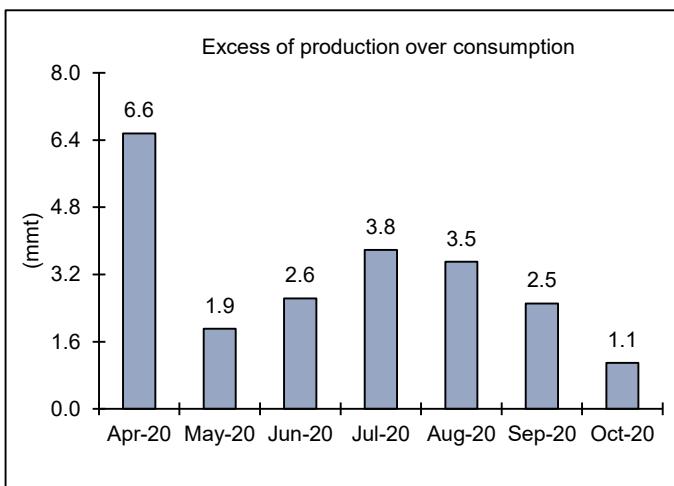
- Petroleum products is down 16% YoY.
- Diesel is down 21% YoY.
- Petrol is down 17% YoY.
- Jet fuel is down 67% YoY.
- LPG is up 6% YoY.
- Naphtha is up 1% YoY.

Auto fuel net exports exceeded production surplus in Oct'20

Excess of production over consumption narrowed in Oct'20

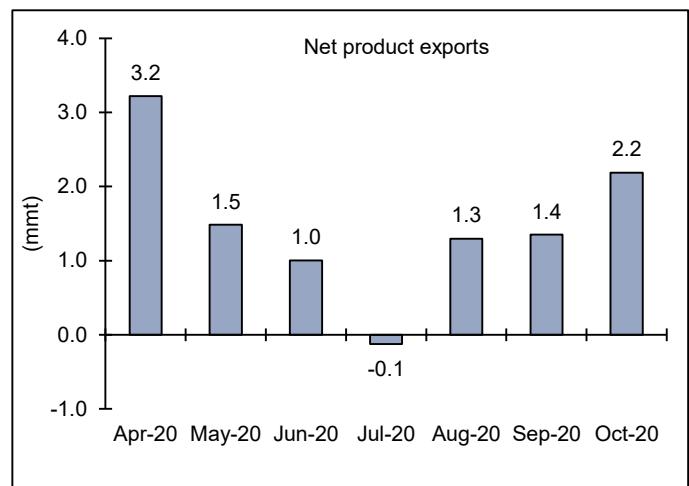
India's petroleum product consumption declined 8.9mmt (49%) YoY in Apr'20 while production was down 5.1mmt (24%) YoY. Excess of production over consumption thus surged by 3.8mmt (141%) YoY to 6.6mmt in Apr'20. Excess of production over consumption contracted from 6.6mmt in Apr'20 to 1.9mmt in May'20 but surged to 2.6-3.8mmt in Jun-Jul'20 before narrowing marginally MoM to 3.5mmt in Aug'20. Excess of production over consumption narrowed further MoM to 2.5mmt in Sep'20 and to 1.1mmt in Oct'20.

Chart 19: Excess of production over consumption down MoM in Aug-Oct'20 after rise in Jun-Jul



Source: PPAC, I-Sec research

Chart 20: Net exports rise in Aug-Oct'20 after first net imports in at least 112 months in Jul'20

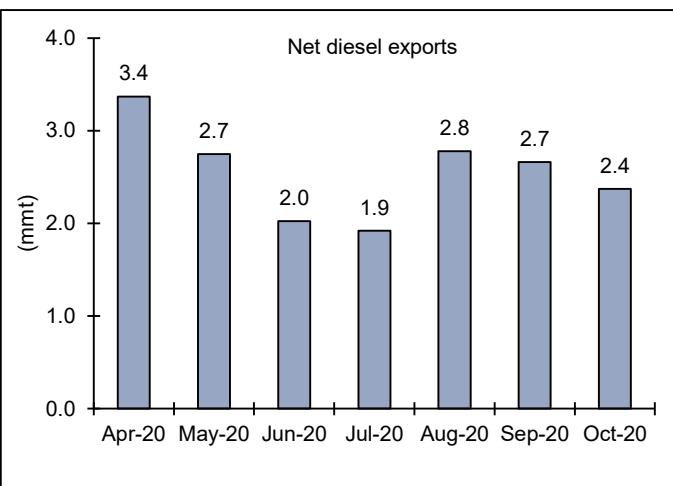


Source: PPAC, I-Sec research

Diesel net exports exceeded production surplus in Oct

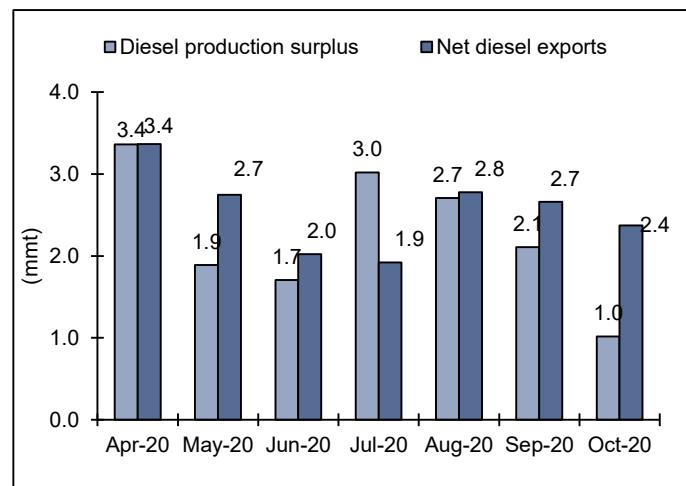
In Oct'20, diesel production exceeded consumption by 1mmt while net exports stood at 2.4mmt suggesting fall in diesel inventory by 1.4mmt MoM.

Chart 21: Net diesel exports rise to 2.8-2.4mmt in Aug-Oct'20 after secular fall from Apr to Jul



Source: PPAC, I-Sec research

Chart 22: Diesel inventory down in Oct'20 with exports at 2.4mmt vs production surplus of 1mmt



Source: PPAC, I-Sec research

Petrol net exports exceeded production surplus in Oct

In Oct'20, petrol production exceeded consumption by 0.5mmt while net exports stood at 0.7mmt suggesting fall in petrol inventory by 0.2mmt MoM.

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