

Tupras (TUPRS TI)

Buy: Weakness driven by poor refining margins and unplanned shutdowns

- ▶ Weak middle distillate cracks and unplanned shutdowns led to weak 1Q16 results
- ▶ Performance likely to improve sharply on seasonal increase in margins, strong demand and higher capacity utilisation
- ▶ Cut target price to TRY83 (from TRY90); maintain Buy rating

Very weak 1Q16 results: Tupras reported extremely weak 1Q16 EBITDA of TRY398m, which was 32% and 40% lower than our and consensus estimates, respectively. Excluding inventory related losses, EBITDA declined by 32% y-o-y in USD terms. A large part of the miss is explained by a 40% y-o-y fall in company's net refining margin, which was in-line with a 37% y-o-y fall in benchmark Med-Urals gross refining margin (GRM). The weakness in margins was on the back of poor middle distillate cracks, which fell to their multi-year quarterly low in 1Q16 due to oversupply and higher inventory levels globally. Tupras' operations were also negatively impacted by lower utilisation of residuum upgrade unit (RUP) due to a fire, which kept the unit under shutdown for almost two months. As a result, there is no change in refined product yields in 1Q16 vs last year when RUP was not operating and the company likely didn't seem to gain any major benefit from the unit, which was commissioned in 2H15. On a positive side, Tupras was able to run its refineries at 100% capacity utilisation rate despite unplanned shutdowns vs 85% in 1Q15 and Turkish fuels demand maintained its growth trend across all major products: diesel (+8% y-o-y), jet fuel (+17.6% y-o-y), and gasoline (+7% y-o-y). Company's free cash flow improved to TRY163m (vs negative FCF in 1Q15) but was largely led by working capital release while capex declined 31% y-o-y.

Performance likely to improve on seasonality and full capacity utilisation: Owing to extremely poor middle distillate cracks in 1Q16, Tupras' management cut its FY2016e net margin guidance to USD5.5-6.0/b range from USD5.8-6.3/b earlier. However, the company maintained unchanged its guidance for capacity utilisation at 100% and expects middle distillate cracks to strengthen during the peak summer season. We note that, so far, diesel cracks have improved by over 10% q-o-q in 2Q16 but they remain roughly 30% lower than the historical quarterly average. Moreover, with RUP returning to full utilisation, we expect Tupras to fully capture the benefits of higher margins in peak summer season in 2Q and 3Q.

Maintain Buy with TP cut to TRY83 (from TRY90): Our forecast for Tupras' net refining margin is now at USD5.1/b vs USD5.4/b earlier. As a result, our FY2016e EBITDA falls by 11% compared with our earlier estimate. We expect Tupras to benefit from full utilisation of RUP for the rest of the year and strong domestic Turkish fuel demand. Our lower estimates drive the cut in our TP to TRY83 (from TRY90), which implies 25% upside; we maintain a Buy rating.

EQUITIES OIL & GAS

Turkey



MAINTAIN BUY

TARGET PRICE (TRY)

83.00

PREVIOUS TARGET (TRY)

90.00

SHARE PRICE (TRY)

66.65

(as of 06 May 2016)

UPSIDE/DOWNSIDE

+24.5%

MARKET DATA

Market cap (TRYm)	16,690	Free float	100%
Market cap (USDm)	5,699	BBG	TUPRS TI
3m ADTV (USDm)	47.8	RIC	TUPRS.IS

FINANCIALS AND RATIOS (TRY)

Year to	12/2015a	12/2016e	12/2017e	12/2018e
HSBC EPS	10.18	8.96	9.88	9.12
HSBC EPS (prev)	-	10.42	-	-
Change (%)	-	-14.0	-	-
Consensus EPS	8.39	9.76	9.70	9.41
PE (x)	6.5	7.4	6.7	7.3
Dividend yield (%)	9.8	8.1	8.9	8.2
EV/EBITDA (x)	6.0	6.3	5.8	5.5
ROE (%)	35.3	26.1	26.1	21.9

52-WEEK PRICE (TRY)



Source: Thomson Reuters IBES, HSBC estimates

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Financials & valuation

Financial statements

Year to	12/2015a	12/2016e	12/2017e	12/2018e
Profit & loss summary (TRYm)				
Revenue	36,893	34,910	45,260	56,575
EBITDA	3,784	3,510	3,605	3,625
Depreciation & amortisation	-486	-536	-522	-522
Operating profit/EBIT	3,298	2,974	3,083	3,103
Net interest	-349	-174	-95	-274
PBT	2,225	2,819	3,110	2,869
HSBC PBT	2,225	2,819	3,110	2,869
Taxation	339	-564	-622	-574
Net profit	2,550	2,244	2,475	2,284
HSBC net profit	2,550	2,244	2,475	2,284
Cash flow summary (TRYm)				
Cash flow from operations	-155	3,295	3,215	2,994
Capex	-961	-800	-650	-600
Cash flow from investment	-959	-800	-650	-600
Dividends	6	-1,628	-1,346	-1,485
Change in net debt	3,035	-867	-1,219	-909
FCF equity	-1,043	2,194	2,132	2,067
Balance sheet summary (TRYm)				
Intangible fixed assets	59	59	59	59
Tangible fixed assets	15,970	15,951	15,768	15,559
Current assets	8,675	5,712	8,288	10,686
Cash & others	3,028	339	1,557	2,465
Total assets	25,470	22,489	24,881	27,070
Operating liabilities	6,988	6,935	8,187	9,566
Gross debt	9,919	6,364	6,363	6,363
Net debt	6,892	6,025	4,806	3,897
Shareholders' funds	8,305	8,921	10,050	10,849
Invested capital	14,688	14,448	14,371	14,272

Ratio, growth and per share analysis

Year to	12/2015a	12/2016e	12/2017e	12/2018e
Y-o-y % change				
Revenue	-7.1	-5.4	29.6	25.0
EBITDA	379.5	-7.2	2.7	0.6
Operating profit	521.1	-9.8	3.7	0.7
PBT	1111.7	26.7	10.3	-7.7
HSBC EPS	74.8	-12.0	10.3	-7.7
Ratios (%)				
Revenue/IC (x)	3.0	2.4	3.1	4.0
ROIC	31.4	16.3	17.1	17.3
ROE	35.3	26.1	26.1	21.9
ROA	13.4	10.5	11.6	9.9
EBITDA margin	10.3	10.1	8.0	6.4
Operating profit margin	8.9	8.5	6.8	5.5
EBITDA/net interest (x)	10.8	20.2	37.8	13.2
Net debt/equity	82.4	67.0	47.4	35.6
Net debt/EBITDA (x)	1.8	1.7	1.3	1.1
CF from operations/net debt		54.7	66.9	76.8
Per share data (TRY)				
EPS reported (diluted)	10.18	8.96	9.88	9.12
HSBC EPS (diluted)	10.18	8.96	9.88	9.12
DPS	6.50	5.38	5.93	5.47
Book value	33.16	35.62	40.13	43.32

Key forecast drivers

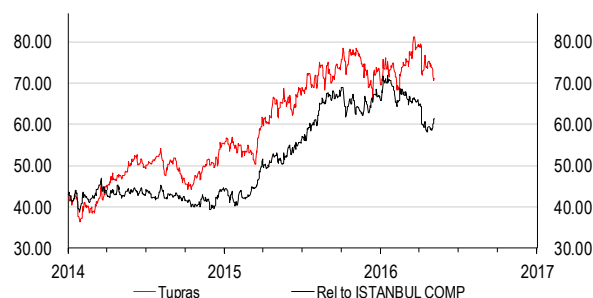
Year to	12/2015a	12/2016e	12/2017e	12/2018e
Med-Urals refining margin (USD)	4.8	4.0	3.5	3.5
Tupras Net Refining Margin(USD)	6.5	5.1	5.3	5.3
USD/TRY (Average)	2.72	2.95	3.00	3.00

Valuation data

Year to	12/2015a	12/2016e	12/2017e	12/2018e
EV/sales	0.6	0.6	0.5	0.4
EV/EBITDA	6.0	6.3	5.8	5.5
EV/IC	1.6	1.5	1.4	1.4
PE*	6.5	7.4	6.7	7.3
PB	2.0	1.9	1.7	1.5
FCF yield (%)	-6.5	13.7	13.3	12.9
Dividend yield (%)	9.8	8.1	8.9	8.2

* Based on HSBC EPS (diluted)

Price relative



Source: HSBC

Note: Priced at close of 06 May 2016

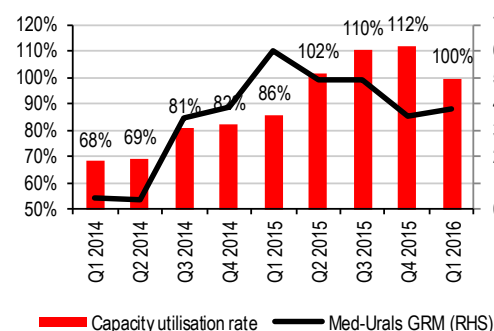
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Tupras financial forecast revisions (TRYm)

	2016e			2017e			2018e		
	New	Old	Change	New	Old	Change	New	Old	Change
Sales	34,910	35,489	-2%	45,260	45,260	0%	56,575	56,575	0%
EBITDA	3,510	3,950	-11%	3,605	3,605	0%	3,625	3,625	0%
Net income	2,244	2,609	-14%	2,475	2,475	0%	2,284	2,284	0%

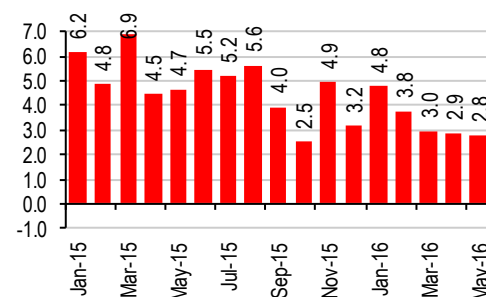
Source: HSBC estimates

Tupras' CUR was at 100% despite maintenance shutdowns in 1Q16



Source: Tupras

Reuters Med-Urals gross refining margins (USD/b)



Source: Thomson Reuters Datastream

Valuation and risks

Valuation

We update our model with 1Q16 results. We value Tupras using a DCF (50% weight) and multiples-based approaches (25% weight each to PE and EV/EBITDA). Our DCF valuation for Tupras is TRY90.0 per share (from TRY94.5). This is derived using a benchmark Med-Urals refining margin of USD4.0/bbl for 2016 and USD3.5/b thereafter, a risk-free-rate assumption of 9.5%, an equity risk premium of 5.5%, and a beta of 0.91, resulting in a CoE of 14.5%. We use cost of debt of 5.0%, leading to a WACC of 11.1% (unchanged). Our DCF model also assumes a terminal growth rate of 3%.

Our EV/EBITDA valuation method yields a valuation of TRY66.4 (from TRY75.8) per share based on the one-year forward sector average multiple of 5.0x (unchanged) and our 2016-2017e time-weighted EBITDA estimate.

We arrive at a PE-based valuation of TRY85.5 (from TRY95.1) per share using the one-year forward multiple of 7.0x (unchanged) and our time-weighted 2016-2017e net income estimate. On relative valuation multiples, we think Tupras should trade in line with its peer average on forward-looking multiples.

The weighted average of these three valuation methods, rounded to the nearest whole number, results in a fair value target price of TRY83 (from TRY90). Our target price implies upside of 24.5%. We maintain our Buy rating and highlight that the stock offers attractive dividend yield and despite likely weaker margins the company is likely to post strong financial performance in 2016e thanks to the low base effect (launch of the residue upgrade unit in mid-2015).

Risks

The downside risks to our estimates and rating include lower-than-expected refining margins and fuel demand in the company's key market Turkey, fiscal and regulatory related risks

Disclosure appendix

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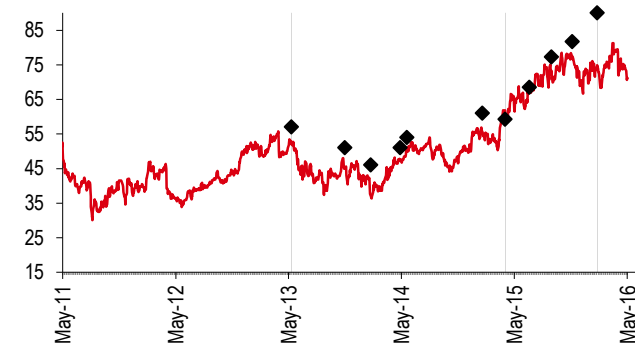
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Hold	40%	(25% of these provided with Investment Banking Services)
Sell	15%	(18% of these provided with Investment Banking Services)

For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see "Stock ratings and basis for financial analysis" above.

Share price and rating changes for long-term investment opportunities

Tupras (TUPRS.IS) share price performance TRY Vs

HSBC rating history



Source: HSBC

Rating & target price history

From	To	Date
Overweight	Neutral	15 May 2013
Neutral	Hold	06 April 2015
Hold	Buy	29 January 2016
Target price	Value	Date
Price 1	57.00	15 May 2013
Price 2	51.00	04 November 2013
Price 3	46.00	27 January 2014
Price 4	51.00	02 May 2014
Price 5	54.00	23 May 2014
Price 6	61.00	23 January 2015
Price 7	59.20	06 April 2015
Price 8	68.50	24 June 2015
Price 9	77.20	03 September 2015
Price 10	81.70	09 November 2015
Price 11	90.00	29 January 2016

Source: HSBC

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