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Mr. Ajmera's column as on 16th July, 2016

Reliance Q1FY17 results beat street expectations; domestic bourses can make new highs..

Domestic bourses performance

Indian market were buoyantduring the week. Nifty and Sensex moved up by 2.62% and 2.60% respectively. Raslly was witnessed in sectors like Metals, Construction and Finance. IT and Pharmaceuticals sectors were the notable losers this week.

Infosys Ltd tumbled the most in a single day since April 2013 after paring its annual sales outlook. Tata Consultancy Services Ltd (TCS), Asia's largest technology exporter, decreased the most in five months. Coal India Ltd, the world's largest miner of the fuel, and power generator NTPC Ltd both fell for a second day this week. The reason for NTPC's fall seems to be sell off by its employees of the shares issued under ESOP.

The S&P BSE Sensex decreased 0.38%, or 105.61 points on Friday, to 27,836.50 at the close, paring the weekly advance to 2.6%.

The CPI and WPI year-on-year data released this week in India at 5.77% and 1.62% respectively boosted equity markets higher and strengthened Rupee at 66.85 against Dollar. Commodities traded in a range this week with Gold trading around Rs.31,000/10gms and Silver around Rs.47,500/kg. On sector check, Metals (+8.8%) and PSU Bank (+6.7%) outperformed the week while IT dragged by 2.1% after poor quarterly numbers by Infosys.

The Sensex has risen 6.6% this year. Overseas funds bought $48 million of local shares on 13 July, taking this year's net inflows to $3.2 billion.

Reliance Q1FY17 result highlights

A robust performance by its refining segment, which accounts for almost two-thirds of Reliance Industries (RIL)'s gross revenue, helped the company clock its sixth consecutive quarter of net profit growth, in contrast to general Street anticipation of a profit decline. The gross refining margins (GRM) of $11.5 a barrel, as seen in the December' 2015 quarter, are at the highest levels seen by RIL in over seven years. "Though regional refining margins trended downwards, our high-conversion refining system was able to take advantage of higher margins on middle distillates and wider discounts on sour crude oils," Mukesh Ambani said.

GRM is the profit earned by processing a barrel of crude oil (total value of output minus cost crude oil).

Revenue on standalone basis increased 7 percent to Rs 53,496 crore during the quarter from Rs 49,957 crore in the preceding period, aided by refining business. "We maintained earnings growth trajectory in Q1. We continued to harness the power of our integrated energy and materials business portfolio," Mukesh Dhirubhai Ambani, Chairman and Managing Director, Reliance Industries said.

Profit was estimated at Rs 6,500 crore and gross refining margin at USD 9.8 a barrel for the quarter, according to average of estimates of analysts. Reliance said the benchmark Singapore complex margin averaged USD 5 a barrel in Q1FY17, declined compared to USD 7.7 a barrel in Q4FY16 on the back of weak light distillate cracks and sharp decline in fuel oil cracks. However, middle distillate cracks remained firm with recovery in gasoil cracks. Operating profit (earnings before interest, tax, depreciation and amortisation) rose by 1 percent quarter-on-quarter to Rs 10,817 crore in Q1.

Refining income increased 21.4 percent sequentially to Rs 48,946 crore with its earnings before interest and tax (EBIT) showing 3.4 percent growth but margin declined 240 basis points. Revenue from its petrochemical business came in at Rs 19,409 crore for the April-June quarter against Rs 19,548 crore in January-March period. Segment's earnings before interest and tax grew by 6.65 percent to Rs 2,901 crore and margin expanded by 100 basis points to 15 percent compared with preceding month.

PTA (purified terephthalic acid) and PET (polyethylene terephthalate) plants at Dahej, which were disrupted due to water shortage, are currently operating at full capacity, Reliance said, adding fibre intermediate production in Q1 was up 6 percent YoY to 1.5 million metric tonnes while polyester production remained stable at 0.51 million metric tonnes. Its KG-D6 field produced 0.28 million barrels of crude oil and 28.05 billion cubic feet of natural gas in the quarter gone by, a reduction of 35 percent and 23 percent respectively year-on-year. Fall in oil and gas production was mainly on account of natural decline in the fields. Panna-Mukta fields produced 1.7 million barrels of crude oil and 17.0 billion cubic feet of natural gas in Q1, an increase of 8 percent and 2 percent respectively on Y-o-Y basis. This was due to restoration of production from Mukta-A field, better than expected gains from work-overs of Panna-B wells and production coming from development of Mukta-B field, Reliance said. Post cessation of production in Tapti in March 2016, the company handed over processing facilities and export pipelines to ONGC.

Retail business recorded continued growth momentum and strong profitability in Q1. Revenues grew by 45.8 percent YoY to Rs 6,666 crore, led by growth in digital, fashion & lifestyle and petroleum products. As on June 30, 2016, it operated 3,383 stores across 679 cities with an area of over 13 million square feet. Reliance Jio Infocomm, which holds Pan-India unified licence and has total liberalised spectrum holdings of 846.10 MHz, now has over 1.5 million test users on its network. The test program will be progressively upgraded into commercial operations in coming months, the company said. Reliance's consolidated net profit increased 2.4 percent sequentially to Rs 7,089 crore and revenue grew by 8.9 percent to Rs 64,990 crore in the quarter gone by. Outstanding debt stood at Rs 1,86,692 crore as of June compared to Rs 180,388 crore as of March 2016, Reliance said, adding cash and cash equivalents were at Rs 90,812 crore compared to Rs 89,966 crore in same period.

After consistently falling for some quarters, the share of other income in Reliance Industries' total net profit of Rs 7,113 crore in the June quarter has substantially jumped to 34.5 per cent or Rs 2,378 crore. On year-on-year basis, this was a massive 50.12 per cent spike from Rs 1,584 crore the company reported in the June 2015 quarter when its net profit stood at Rs 5,916 crore. The same stood at Rs 1,953 crore in the March 2016 quarter on a total net profit of Rs 6,925 crore. When asked whether the company has been increasing its play in the treasury market or has it booked some profits from its massive investments, RIL deputy chief financial officer V Srikanth told that the numbers reflect the higher yields the market has been returning during the quarter.

While refusing to share the specifics of the company's investment in government bonds, Srikanth said RIL for long has been parking its surpluses, which stood at almost Rs 97,000 crore as of end June, in government bonds, mutual funds, fixed deposits and other fixed income instruments. And the same continued in the reporting quarter as well.

RIL, which is one of the biggest players in the treasury markets, was netting over 40 per cent of its total net profit from treasury gains or other income which started declining after the banking regulator began to frown upon corporates' large influence in the money and government debt markets.

Reliance, which has the highest cash balance, is also one of the highly indebted companies in the country. Its debt rose to Rs 1,86,692 crore as of June from Rs 1,80,388 crore as of March 2016 while the cash balance inched up marginally to Rs 90,812 crore from Rs 89,966 crore from March 2016.

Accordingly, the company's interest payout jumped to Rs 1,206 crore from Rs 915 crore a year ago and from Rs 842 crore from the March quarter.

About the forex components of the debt pile, Srikanth said over 90 per cent of RIL bet is in US dollars while almost the entire Rs 47,000 crore debt of Rel Jio is rupee-denominated.

RIL, which operates the world's largest oil refinery with a 63 mt annual capacity, today reported a hefty 18.1 per cent jump in June quarter net profit at Rs 7,113 crore or Rs 24.1 per share on account of highest refining margin in the past eight years and robust petrochemical earnings.

Global Markets

After finally eclipsing year-old record highs, the US stock market will be tested again next week, when the onslaught of company earnings could help investors assess the impact of Britain's vote to exit the European Union. Investors were expecting to see evidence of a second-half profit rebound, but US companies are already sounding more cautious, thanks to worries about global economic weakness and renewed dollar strength since the June 23 vote. Market bulls have been hoping stronger profits could spur further gains in stocks this year, or at least keep the gains they've made so far. The recent rally that drove the S&P 500 above its May 2015 records has left the benchmark up 5.8 percent for the year so far.

Stocks

Infosys tumbled 8.81% to its lowest level since 12 January after the company predicted 10.8% to 12.3% growth in US dollar terms in the year to March, down from a previous range of 11.8% to 13.8%. The company also reported first-quarter sales that lagged estimates.

TCS, which kicked off the reporting season Thursday, fell 3%, ending a four-day advance. Net income increased to Rs.6,320 crore in the three months ended June, the Mumbai-based company said after trading ended. The results beat the Rs.6,060 crore mean of estimates compiled by *Bloomberg*. The company does not provide a sales guidance. Wipro Ltd, the third biggest, slid 2.81%.

Coal India retreated 1.48%, the most since 7 July. NTPC decreased 1.2%, the most since 5 July. RIL rose 0.6% to its highest level since 27 April.

LIC Housing Finance Ltd surged 3.7% to a record after the company's first-quarter profit rose 6.7% to Rs.3,360 crore. Net interest margin widen to 2.61% compared with 2.41% in the same period a year earlier. The whole housing finance sector looks promising.

Week ahead and Ajcon's view:

Investor are focusing on the June-quarter results season, which got underway on Thursday, for signs that the rally that pushed up the stocks valuation (PE multiples) to near a five-year high this week are supported by company earnings.

Investors are hopeful about passage of key bills including Goods & Services Tax (GST) Bill during the monsoon session of Parliament, with proceedings slated to begin from next week.

Shares of public sector oil marketing companies (PSU OMCs) will on Monday, 18 July 2016, react to a regular fuel price revision due during this weekend. PSU OMCs review fuel prices twice a month based on the trend in international oil market and currency movement. The first review takes place during the middle of the month and the last review at the month-end.

On the global front, meeting of Governing Council of European Central Bank (ECB) on monetary policy will be held in Frankfurt on Thursday, 21 July 2016, which will be followed by the press conference.

The recent rally is in the hope of passage of GST bill. Non passage of GST may affect domestic bourses adversely. We believe any disappointment in Q1FY17 earnings season may lead to correction in stocks. If earnings continue to grow along with good progress of monsoons, markets may make new high. We emphasize to focus on stock specific with good fundamentals. Our advise to investors is to book partial profits at every rally.

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