

Oil and Gas Lukoil

Confirmation of recommendation to Buy

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Debt/Equity

EV/Sales (x)

P/E (x)

EV/EBITDA (x)

Ticker			LKOH RM
Recommendation			BUY
Current price, ₽/share			5 450
12M target price, ₽/share			6 317
Upside			16%
Expected dividend, RUB/share			270
Expected dividend yield			5%
Ticker			LKOD LI
Recommendation			BUY
Current price, \$/share			84.30
12M target price, \$/share			97.56
Upside/Downside			16%
Expected dividend, RUB/GDR			4.2
Expected dividend yield			5%
No. of ordinary shares (mn)			715
Free float (%)			61.6%
3M av. daily turnover (₽ ths)			879
Market capitalisation (₽ bn)			3 897
Financials (P bn)	2018	2019E	2020F
Revenue	8 036	7 953	7 777
EBITDA	1 115	1 260	1 210
Net profit	621	666	712
EPS, ₽	1 305	1 398	1 496
Equity	4 074	4 546	5 052
Net debt	16	-101	-420
Valuation	2018	2019E	2020F
Net Debt/EBITDA (x)	0.01	-0.08	-0.35

LKOH RM price dynamic	Abs.	Relative MICEX
1M	8.9%	4.6%
3M	15.2%	12.9%
6M	30.3%	34.1%
Max 52 week	5 996	
Min 52 week	2 586	

0.13

0.49

3.51

0.12

0.48

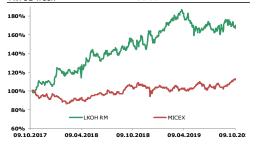
3.01

0.08

0.45

2.87

LKOD LI price dynamic	Abs.	Relative FTSE 100
1M	5.9%	2.9%
3M	12.0%	10.9%
6M	26.7%	31.6%
Max 52 week	83.28	
Min EQall	E0 60	



We recommend to Buy Lukoil's shares with 12M TP 6317rub. per share. We remain confident about the stability of cash flows generated by Lukoil amid continued uncertainty in the global oil market and note strong catalysts for stock growth in both the short and long terms. We expect shares to rise in the coming month due to the announcement of interim dividends and see the potential for further stock growth during the buyback period. We note the company's strong financial performance, ensured by a highly profitable oil production and a wide geography of exports, as a quarantee of a stable increase in Lukoil's market capitalization in the long term.

Strong 1H2019 results despite weak oil market conditions. Lukoil's statement results for 6M2019 demonstrates revenue growth of 7.9% yoy to 3 977bn rubles. EBITDA increased by 22.5% yoy to 630.2bn rubles. The growth was driven by higher sales volumes of crude oil and natural gas due to higher production volumes. The increase was also supported by the ruble devaluation resulting in higher average international prices for hydrocarbons in ruble terms, which partially offset the increase in the price of purchased crude oil by 5.7% yoy to 2.2tn rubles. Operating profit amounted to 421bn rubles (+ 28% yoy) and net profit strengthened by 20% yoy, amounting to 332bn rubles, which in our opinion is a strong result. Mostly the company's "dollar" revenue eliminates the negative effect of fluctuations of oil prices, due to which the sensitivity to the situation on energy markets for Lukoil shares is relatively lower. CFO in the reporting period increased by 25% yoy to 513bn rubles. Cash at the end of 1H2019 amounted to 506bn rubles, showing an increase of 3% since the beginning of the year and by 49% yoy. At the end of 2019, we expect EBIT to grow by 9% yoy to 841bn rubles and we see the potential to achieve a net profit level of 666bn rubles. FCF, according to our forecasts, will be positive and will reach 700bn by 2025.

Second wave of buyback. In August this year, Lukoil completed the \$3bn stock buyback program, planned for the period from September 2018 to December 2022. Repurchased stocks amounted to 4.96% of the authorized capital of the company. All repurchased shares were redeemed and the total number of issued ordinary shares of Lukoil decreased from 750mn to 715mn. In early October this year, Lukoil announced the launch of its second buyback program for the same amount of \$3bin, which will be sold until December 30, 2022. Given the current market price, the buyback volume of \$3bn is about 5.1% of Lukoil's authorized capital. We note mainly the positive impact of the buyback on LKOH shares, given that the offer price at the previous buyback assumed a premium to the market price of 5.4%. In addition, due to the higher EPS value and dividend per share due to buyback, Lukoil shares look even more attractive in comparison with the competitors.

A progressive dividend policy remains relevant. Lukoil, which has a dividend history of more than 20 years, has been continuously increasing the dividend for the last 6 years and striving to increase the dividend per share annually by at least the level of ruble inflation. Free cash flow dividend coverage ratio for 2018 amounted to 351%. At the end of last year, Lukoil allocated about a third of its net profit for payment, which corresponds to 250 rubles per share and a dividend yield of 5%. At the minimum guaranteed dividend level of 25% of net profit, according to our expectations, the company will maintain the growth of dividend per share, increasing the payout ratio if necessary. An impressive cash position with a fairly low debt burden (Debt/Equity 16% with an industry average of 37%), in our opinion, will allow the company to provide a high dividend yield. At the end of 2019 we expect an increase in the total dividend by 8% yoy to 270 rubles per share. Given that the company practices the payment of interim dividends, we expect good preconditions for the growth of shares over the next month in anticipation of the announcement of the dividend for 9M2019. Note that according to the results of 9M2018 Lukoil paid 95 rubles/share and 85 rubles/share for 9M2017. In the future, due to the ongoing buyback program, we expect a more significant increase in dividend per share.



Fig. 1. 1H2019 financial results

RUB bn	1H2018	1H2019	yoy
Revenue	3 687	3 976	8%
Operating expenses	-221	-223	1%
Cost of purchased oil	-2 079	-2 198	6%
Transportation costs	-134	-137	2%
Administrative expenses	-77	-99	29%
Depreciation and amortization	-185	-210	14%
Oil taxes	-401	-476	19%
Excise and export duties	-259	-213	-18%
Exploration costs	-1	-2	100%
Operating profit	330	418	27%
Financial income	8	12	50%
Financial expenses	-16	-23	44%
The share of profits in JV and assoc.	11	11	0%
Exchange difference	21	6	-71%
Other (expenses) income	-10	-10	0%
Profit before income tax	344	414	20%
Income tax	-67	-85	27%
Net profit	277	329	19%

Fig. 3. Smooth growth in production costs due to the continued low cost of purchased oil

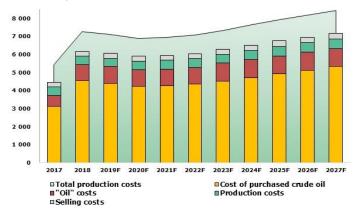


Fig. 5. Strong dividend history



Fig. 2. Key assumptions in forecasts

Lukoil

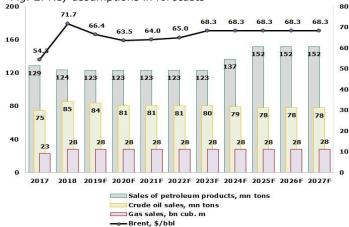


Fig. 4. Sustainability of revenues in the conditions of "cheap" oil due to increased sales of petroleum products

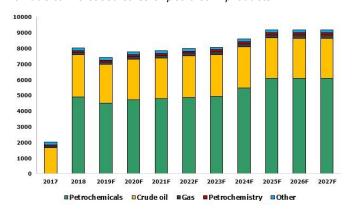


Fig. 6. Consistently positive FCF during 2019-27

1800		12%
1600		10%
1400		10%
1200		8%
1000		6%
800		0 70
600		4%
400		2%
200		2 /0
0	2019F 2020F 2021F 2022F 2023F 2024F 2025F 2026F 2027F	0%
12		
L	CAPEX CFO FCF → Net profit margin, %	

Fig. 7. The calculation of 12M target price

RUB bn	2020F	2021F	2022F	2023F	2024F	2025F	2026F	2027F
EBIT	899.430	900.014	919.312	742.223	972.376	1 242.047	1 009.206	764.633
+ Depreciation	310.890	321.050	330.502	342.482	357.135	374.625	395.139	418.892
- Capex	456.041	456.041	456.041	501.645	551.810	606.991	667.690	734.459
- Change in working capital	44.935	4.724	9.675	1.088	36.828	41.210	-4.368	-4.516
- Income tax expense	189.248	190.404	195.215	158.171	208.033	269.662	225.993	177.818
FCF	520.096	569.895	588.883	423.801	532.840	698.809	515.030	275.764
DCF	468.086	455.916	471.106	339.041	426.272	559.047	412.024	220.611
WACC	13%		•	•				

WACC	13%
First stage DCF	3 352.103
Terminal value	2 124.530
PV of Terminal value	1 699.624
Enterprise value (EV)	5 051.727
Net debt	535.318
Fair value	4 516.409
Number of common shares (mn)	715
Target price, ruble per share	6 317
Current price, RUB/share	5 450
Upside	16%
Rating	BUY

Source: Company data, Halyk Finance estimates, Bloomberg





Appendix 1. Forecasts of financial	indicators	, rub. mn,	except pe	er share.							
P&L	2017	2018	2019F	2020F	2021F	2022F	2023F	2024F	2025F	2026F	2027F
Revenues	5 936 705	8 035 889	7 952 970	7 777 330	7 851 392	8 000 694	8 078 141	8 597 617		9 178 553	9 183 623
Operating expenses	-456 765 -3 129 864	-464 467 -4 534 244	-445 718 -4 395 816	-488 564 -4 219 983	-487 783 -4 262 183	-487 003 -4 347 427	-486 226 -4 530 019	-511 701 -4 720 280	-538 871 -4 918 532	-538 357 -5 125 110	-537 844 -5 340 365
Cost of purchased crude oil Transportation expenses	-3 129 864	-4 534 244	-274 508	-4 219 983 -269 821	-4 262 183 -269 530	-4 347 427	-268 951	-4 720 280 -286 963	-4 918 532	-305 970	-305 779
Общехозяйственные расходы	-165 331	-192 433	-197 120	-205 399	-214 026	-223 015	-232 382	-242 142		-262 909	-273 951
Depreciation, depletion and amortisation	-325 054	-343 085	-419 120	-310 890	-321 050	-330 502	-342 482	-357 135	-374 625	-395 139	-418 892
Taxes other than income taxes	-606 510	-899 383	-951 026	-912 985	-922 115	-940 557	-987 585	-987 585	-987 585	-987 585	-987 585
Excise and export tariffs	-461 525	-556 827	-425 312	-466 640	-471 084	-480 042	-484 688	-515 857	-550 449	-550 713	-551 017
Exploration expenses	-12 348	-3 582	-3 629	-3 618	-3 607	-3 596	-3 585	-3 578	-3 571	-3 564	-3 557
EBIT	506 516	771 715	840 721	899 430	900 014	919 312	742 223	972 376			764 633
Finance income	15 151	19 530	27 505	33 086	36 999	42 000	45 600	57 132	83 848	110 000	126 428
Finance costs	-27 331	-38 298	-38 298	-26 822	-25 435	-26 064	-28 584	-30 474	-30 474	-31 733	-32 992
Share in JV result	16 864	25 243	22 244	22 244	22 244	22 244	22 244	22 244	22 244	22 244	22 244
Foreign exchange gain Other expenses	-19 948 32 932	33 763 -38 934	-20 664	-37 774	-38 152	-38 915	-39 304	-41 662	-44 578	-44 578	-44 578
Profit before income taxes	524 184	773 019	842 524	901 180	906 686	929 593	753 195		1 284 103		846 751
Current income taxes	-99 976	-137 062	-176 930	-189 248	-190 404	-195 215	-158 171	-208 033	-269 662	-225 993	-177 818
Deferred income taxes	-3 786	137 002	170 330	103 2 10	130 101	133 213	130 171	200 033	203 002	223 333	177 010
Total income tax expense	-103 762	-151 917	-176 930	-189 248	-190 404	-195 215	-158 171	-208 033	-269 662	-225 993	-177 818
Profit for the year	420 422	621 102	665 594	711 932	716 282	734 378	595 024		1 014 441	850 162	668 933
EPS, rub	588.0	868.7	930.9	995.7	1 001.8	1 027.1	832.2	1 094.5		1 189.0	935.6
Balance Sheet	2017	2018	2019F	2020F	2021F	2022F	2023F	2024F	2025F	2026F	2027F
ASSETS Cash and cash equivalents	330 390	492 650	636 238	699 960	800 000	900 000	930 000	1 461 595	2 000 000	2 500 000	2 571 414
Receivables	418 272	429 945	600 068	586 816	592 404	603 669	609 512	648 708	692 209	692 541	692 923
Other current financial assets	19 561	26 200	000 000	125 951	393 275	645 000	733 553	453 102	349 842	71 228	56 574
Inventories	398 186	381 737	458 433	505 390	510 263	519 540	538 207	559 345	581 615	598 295	615 679
Other taxes receivable	87 338	95 611	135 092	132 108	133 366	135 902	137 218	146 042	155 835	155 910	155 996
Other current assets	54 367	52 336	79 530	77 773	78 514	80 007	80 781	85 976	91 742	91 786	91 836
Total current assets	1 308 114	1 478 479	1 909 361	2 127 998	2 507 822	2 884 118	3 029 271	3 354 768	3 871 243	4 109 760	4 184 422
Property plant and equipment	3 575 165	3 829 164	3 985 241	4 130 392	4 265 383	4 390 924	4 550 089	4 744 766	4 977 134	5 249 687	5 565 256
Investments in associates and joint ventures	164 286	228 053	228 053	228 053	228 053	228 053	228 053	228 053	228 053	228 053	228 053
Other non-current financial assets	79 717	82 568	82 568	82 568	82 568	82 568	82 568	82 568	82 568	82 568	82 568
Deferred income tax assets	25 128	31 041	31 041	31 041	31 041	31 041	31 041	31 041	31 041	31 041	31 041
Goodwill and other intangible assets	41 304	41 765	41 765	41 765	41 765	41 765	41 765	41 765	41 765	41 765	41 765
Other non-current assets	32 501 3 918 101	41 312 4 253 903	41 312 4 409 980	41 312 4 555 131	41 312 4 690 122	41 312 4 815 663	41 312 4 974 828	41 312	41 312 5 401 873	41 312	41 312 5 989 995
Total non-current assets TOTAL ASSETS	5 226 215	5 732 382	6 319 341	6 683 129	7 197 944	7 699 781				9 784 186	
LIABILITIES AND EQUITY	3 220 213	3 732 302	0 313 341	0 003 123	, 13, 344	7 033 701	0 004 033	0 324 273	3 273 110	3 704 100	10 174 417
Current liabilities											
Accounts payable	559 977	547 128	661 244	648 785	655 040	666 950	690 913	718 049	746 638	768 049	790 366
Short-term debt	128 713	99 625									
Other taxes payable	118 484	123 974	123 974	123 974	123 974	123 974	123 974	123 974	123 974	123 974	123 974
Provisions	58 253	38 266	38 266	38 266	38 266	38 266	38 266	38 266	38 266	38 266	38 266
Other current liabilities	93 420	105 567	105 567	105 567	105 567	105 567	105 567	105 567	105 567	105 567	105 567
Total current liabilities	958 847	914 560	995 259	916 592	922 847	934 757	958 720		1 014 445		1 058 173
Long-term debt	487 647	435 422	469 110	406 093	406 093	374 612	280 101	280 101	280 101	217 154	217 154
Deferred income tax liabilities Provisions	237 980 47 962	258 836 47 923	258 836 47 923	258 836 47 923	258 836 47 923	258 836 47 923	258 836 47 923	258 836 47 923	258 836 47 923	258 836 47 923	258 836 47 923
Other non-current liabilities	3 380	2 115	2 115	2 115	2 115	2 115	2 115	2 115	2 115	2 115	2 115
Total non-current liabilities	776 969	744 296	777 984	714 967	714 967	683 486	588 975	588 975	588 975	526 028	526 028
Total liabilities	1 735 816	1 658 856	1 773 243	1 631 559	1 637 814	1 618 243			1 603 420		1 584 201
Equity											
Share capital	1 151	1 015	1 015	1 015	1 015	1 015	1 015	1 015	1 015	1 015	1 015
Treasury shares	-251 089	-134 810	-134 810	-134 810	-134 810	-134 810	-134 810	-134 810	-134 810	-134 810	-134 810
Additional paid-in capital	129 641	39 173	39 173	39 173	39 173	39 173	39 173	39 173	39 173	39 173	39 173
Other reserves	27 090	196 554	196 554	196 554	196 554	196 554	196 554	196 554	196 554	196 554	196 554
Retained earnings	3 576 158	3 963 628 4 065 560	4 436 200	4 941 672	5 450 232	5 971 640	6 346 505	6 839 542 6 941 476	7 559 795	8 112 400 8 214 336	8 480 313
	2 402 054		4 538 132	5 043 604	5 552 164 7 966	6 073 572 7 966	6 448 438 7 966	7 966	7 661 730 7 966	8 214 336 7 966	8 582 250 7 966
Total equity	3 482 951 7 448		7 066		/ 500	/ 500	/ 500	/ 500	/ 500	/ 500	
Total equity Non-controlling interests	7 448	7 966	7 966 4 546 098	7 966 5 051 570		6 081 538	6 456 404	6 949 442	7 669 696	8 222 302	8 590 216
Total equity	7 448	7 966 4 073 526	4 546 098		5 560 130	6 081 538 7 699 781					8 590 216 10 174 417
Total equity Non-controlling interests Equity TOTAL LIABILITIES AND EQUITY	7 448 3 490 399 5 226 215	7 966 4 073 526 5 732 382	4 546 098 6 319 341	5 051 570 6 683 129	5 560 130 7 197 944	7 699 781	8 004 099	8 524 273	9 273 116	9 784 186	10 174 417
Total equity Non-controlling interests Equity TOTAL LIABILITIES AND EQUITY Cash Flow Statement	7 448 3 490 399	7 966 4 073 526	4 546 098	5 051 570	5 560 130						
Total equity Non-controlling interests Equity TOTAL LIABILITIES AND EQUITY Cash Flow Statement Net cash flows from	7 448 3 490 399 5 226 215	7 966 4 073 526 5 732 382 2018	4 546 098 6 319 341 2019F	5 051 570 6 683 129 2020F	5 560 130 7 197 944 2021F	7 699 781 2022F	8 004 099 2023F	8 524 273 2024F	9 273 116 2025F	9 784 186 2026F	10 174 417 2027F
Total equity Non-controlling interests Equity TOTAL LIABILITIES AND EQUITY Cash Flow Statement Net cash flows from operating	7 448 3 490 399 5 226 215 2017 758 490	7 966 4 073 526 5 732 382 2018 873 914	4 546 098 6 319 341 2019F 792 380	5 051 570 6 683 129 2020F 855 448	5 560 130 7 197 944 2021F 763 803	7 699 781 2022F 800 492	2023F 846 315	8 524 273 2024F 1 372 967	9 273 116 2025F 1 439 584	9 784 186 2026F 1 528 194	2027F 1 106 893
Total equity Non-controlling interests Equity TOTAL LIABILITIES AND EQUITY Cash Flow Statement Net cash flows from operating investing	7 448 3 490 399 5 226 215 2017 758 490 -433 286	7 966 4 073 526 5 732 382 2018 873 914 -451 526	4 546 098 6 319 341 2019F 792 380 -456 041	5 051 570 6 683 129 2020F 855 448 -456 041	5 560 130 7 197 944 2021F 763 803 -456 041	7 699 781 2022F 800 492 -456 041	2023F 846 315 -501 645	2024F 1 372 967 -551 810	9 273 116 2025F 1 439 584 -606 991	2026F 1 528 194 -667 690	2027F 1 106 893 -734 459
Total equity Non-controlling interests Equity TOTAL LIABILITIES AND EQUITY Cash Flow Statement Net cash flows from operating investing financing	7 448 3 490 399 5 226 215 2017 758 490 -433 286 -247 395	7 966 4 073 526 5 732 382 2018 873 914 -451 526 -260 128	4 546 098 6 319 341 2019F 792 380 -456 041 -192 751	5 051 570 6 683 129 2020F 855 448 -456 041 -335 685	5 560 130 7 197 944 2021F 763 803 -456 041 -207 722	7 699 781 2022F 800 492 -456 041 -244 451	2023F 846 315 -501 645 -314 670	2024F 1 372 967 -551 810 -289 562	2025F 1 439 584 -606 991 -294 188	9 784 186 2026F 1 528 194	10 174 417 2027F 1 106 893 -734 459 -301 020
Total equity Non-controlling interests Equity TOTAL LIABILITIES AND EQUITY Cash Flow Statement Net cash flows from operating investing	7 448 3 490 399 5 226 215 2017 758 490 -433 286	7 966 4 073 526 5 732 382 2018 873 914 -451 526	4 546 098 6 319 341 2019F 792 380 -456 041	5 051 570 6 683 129 2020F 855 448 -456 041	5 560 130 7 197 944 2021F 763 803 -456 041	7 699 781 2022F 800 492 -456 041	2023F 846 315 -501 645 -314 670 30 000	2024F 1 372 967 -551 810 -289 562 531 595	9 273 116 2025F 1 439 584 -606 991	2026F 1 528 194 -667 690 -360 504	2027F 1 106 893 -734 459





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