

Analysts see further rerating in PSU stocks on divestment hope

Say some firms, especially BPCL, stand a good chance as the process gathers pace

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Stocks of listed public sector undertakings (PSUs) have had a good run at the bourses since the presentation of the Union Budget in February, when the government reiterated its commitment to pare stake in select state-owned companies. Since then, the S&P BSE PSU index has outperformed the S&P BSE Sensex by gaining over 20 per cent, against around 8 per cent rise in the frontline index, ACE Equity's data shows. What's more, there could be more gains in the offing as analysts expect further re-rating in the state-owned stocks.

The government plans to privatise two public sector banks (PSBs) and one general insurance company in FY22, and aims to raise ₹1.75 trillion in the process. Successful privatisation would ease the quasi-fiscal burden (not having to bail out loss-making state companies) and bring in revenues at a time of larger-than-expected fiscal deficit, says Jan Dehn, head of research at Ashmore Investment Management that has nearly \$100 billion worth of assets under management (AUM).

"There appears to have been a fundamental shift in thinking on divestment. Until 2019, there was no mention of privatisation. Recent signs suggest that the Modi administration is still quite positive about selling BPCL and Air India in FY22. The overall approach now appears to be to sell PSUs to a willing buyer with no strings attached. This is a big shift," he says.

Bharat Petroleum Corporation (BPCL), Air India, Shipping Corporation of India (SCI), Container Corporation of India (CONCOR), IDBI Bank, BEML, Pawan Hans, and Neelachal Ispat Nigam are some of the companies that are likely to see government cutting its stake, reports suggest.

That said, the divestment process, according to G Chokkalingam, founder and chief investment officer at Equinomics Research, will not be an easy affair as there are multiple stakeholders, including employee unions, whose concerns will have to be addressed.

"Investors will have to be patient until the entire divestment process gets



ILLUSTRATION: BINAY SINHA

GAINING GROUND

| | Price (₹) | Change (%) |
|-----------------------------------|-----------------|------------|
| S&P BSE SENSEX | 49,771.3 | 2.4 |
| Hindustan Copper | 124.3 | 93.5 |
| General Insurance Corp of India | 220.4 | 58.8 |
| BEML | 1,384.4 | 50.4 |
| MMTC | 42.8 | 47.7 |
| Rashtriya Chemicals & Fertilizers | 79.1 | 41.8 |
| Shipping Corp of India | 120.0 | 35.9 |
| Container Corp Of India | 561.4 | 23.7 |
| New India Assurance Co | 169.2 | 22.3 |
| S&P BSE PSU | 6,847.8 | 14.5 |
| Balmer Lawrie & Co | 137.7 | 12.9 |
| Bharat Petroleum Corp | 439.4 | 11.8 |

Price as on March 22; change since February 1, 2021; Compiled by BS Research Bureau

Source: Bloomberg, exchange

PAST DIVESTMENT HAPPENED AT PREMIUM VALUATION

BALCO: Sterlite bought stake in Balco at a total market-cap of ₹1,080 crore in March 2001, as compared to an estimated value of ₹600 crore to ₹1,070 crore (based on various valuation methods)

HINDUSTANZINC: Sterlite bought stake at a total market-cap of ₹1,711.5 crore in April 2002, compared to Hindustan Zinc's 2000 and 2001 average market-cap of ₹450 crore and ₹825 crore, respectively

IPCL: RIL bought stake for a total market-cap of ₹5,735 crore in May 2002, compared to IOCL's offer of ₹3,177 crore and Nirma Chemical's offer of ₹2,735 crore

IBP: IOCL bought stake for a total market-cap of ₹3,435.7 crore in February 2002, i.e ₹1,551 per share at a P/E ratio of 63 times

VSNL: Tata Group company bought stake at a ₹202 per share in February 2002 compared to market price of ₹158 as on February 01, 2002

Source: Antique Stock Broking report

over. Returns will not be outsized in the short term. Though operationally things will improve for the companies after divestment, synergies will take time to play out. As things stand, there is a good opportunity in select PSU stocks," he says.

At the bourses, some of these stocks have already seen a good run since the past few weeks. BEML, for instance, has gained around 48 per cent since the presentation of the Budget in February, while CONCOR, SCI and BPCL have surged between 12 per cent and 47 per cent.

Dhirendra Tiwari and Pankaj Chhaoharia of Antique Stock Broking remain positive on PSUs and expect the

divestment to lead to significant re-rating of the entire space as seen in 2002 when PSUs outperformed by around 70 per cent when then Union government, under Atal Bihari Vajpayee, divested its stake in select state-owned companies. State Bank of India (SBI), NTPC, Power Grid, HPCL, GAIL, Bharat Electronics, and NMDC are the companies they remain positive on.

The prized catch in the divestment ring, according to analysts, is BPCL, which analysts feel stands a good chance of rerating as the divestment process for the company gathers momentum.

Analysts at CLSA expect potential buyers to reduce capex at BPCL and sell

some non-core assets (E&P, investments) to increase upstream cash and service interest cost.

"Our expectation on reserve price is around ₹500/share and this includes a potential dividend of ₹50-60/share out of cash proceeds from the sale of its stake in Numaligarh refinery and BPCL trust share of 7.33 per cent. At this price, government stake should be worth \$6.9 billion and total payout to the acquirer would be between \$6.9 billion to \$10.3 billion, depending on what is the response to open offer," write Anubhav Aggarwal, Krati Sankhlecha and Sayantan Maji of CLSA in a March 16 note.