

**April 30, 2007**

**Rating Information**

Sector Rating Market Weight  
Target Price YE '07 INR2000

**Trading Data**

52-Wk Range INR806.00 - INR1625.00  
Market Cap. INR2,770,100 MM  
Shares Out. 1,801.1 MM  
Dividend Yield 0.7%  
Avg. Daily Vol. 28,713,000  
Float  
Source: BSAL Estimates

**Fundamental Data**

EV/EBITDA 16.6x  
Enterprise Value INR3,327,600 MM  
LT Debt to Total Cap. 45.4%  
Book Value INR378.60  
Long-Term Growth 121.8%  
Source: BSAL Estimates

**Price Performance**



Source: FactSet

Securities in this report priced as of:  
April 27, 2007

**Equity Research Analyst(s)**

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**Reliance Industries**

RIL.IN-INR1538.2-Outperform

**From Asset-Based Value to Earnings-Based Growth**

- **Share Price Target Raised to INR2,000 – 30% Upside.** We are increasing our 2007E year-end price target for RIL's shares by 26.6% to INR2,000 from our earlier estimate of INR1,580. Shares now hold 30% upside to our new price target. The share price target is equal to on our 2007E year-end sum of the parts valuation for RIL. We maintain our Outperform rating.
- **Value Adjustments Expected to Continue.** We expect to make adjustments to RIL's value estimates every six months as more information on D6, NEC-25 and D4 reserve and production potential become available.
- **Multiple Year Earnings Explosion.** After several years of +20% per annum strong earnings growth we expect earnings to rise sharply beginning FY2008 as D6's first oil and gas production starts during the 2Q 08, RPL begins operating in 4Q 08 and Reliance Retail Limited's (RRL) contributions grow.
- **RIL's Shares To Decouple From Indian Market.** We believe RIL's shares will begin to trade more independently of the Indian market starting the second half of 2007 as focus turns towards earnings growth. We estimate RIL's three year earnings CAGR of 30% against next year's market estimated EPS growth of 11%.
- **Upgrade to Our Refining and Chemical Margin Assumptions.** We increased RIL's forecast gross refining margin due to regional refining margin strength and a higher premium to the benchmark Singapore complex margin. Our assumed chemical margins have also been increased due to capacity delays in the Middle East. However, our EPS estimates have been reduced after factoring treasury shares, warrants and employee share options.

**Sector View:** We have a neutral view on the Asia-Pacific Refining sector, but are concerned about the negative impact of demand destruction, new capacity, and the introduction of alternative fuels on refining margins.

**IFRS EPS Estimates (All values in INR)**

	EPS	P/E
2008E <sup>(2) (1)</sup>	58.78	26.2x
Previous	61.20	25.1x
2009E	79.29	19.4x
Previous	64.30	23.9x
2010E	141.27	10.9x

(2) March year-end; Earnings estimates are not materially impacted by employee stock options

† All EPS estimates are net of stock options unless otherwise stated.

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We continue to rate RIL's share outperform with 30% upside to our new 2007 year-end price target of INR2,000, a 26.6% increase over our September 21, 2006 estimate of INR1,580. Our outperform rating is also supported by our expectations for a multi year earnings growth drive which could see net profit rise 122% from FY2007 to FY2010. We believe this earnings growth is significantly higher than that of the India market (expectations of the Indian market) and will see RIL's share price decouple from market and rise at a faster rate.

## Sum Of Parts Valuation Update

We have updated several core assumptions across each of RIL's business segments and factored in the impact of the new preferential warrants and RIL's treasury shares in deriving our INR2,000 per share 2007 year-end price target. A full report report on RIL will follow.

**Figure 1. RIL: Sum of the Parts Valuation**

	US\$ mn	INR mn	Basic INR/Share	Diluted INR/Share
<b>Downstream Operations:</b>				
- Core Refining & Chemicals	26,605	1,143,999	821	668
- Reliance Petroleum Ltd.	4,500	193,500	139	113
<b>Sub Total</b>	<b>31,105</b>	<b>1,337,499</b>	<b>960</b>	<b>781</b>
<b>Upstream Operations:</b>				
	<b>30,025</b>	<b>1,291,067</b>	<b>926</b>	<b>754</b>
<b>Others:</b>				
- Retail Operations	4,703	202,233	145	118
- Economic Zones	0	0	0	0
<b>Sub Total</b>	<b>4,703</b>	<b>202,233</b>	<b>145</b>	<b>118</b>
<b>Total</b>	<b>65,833</b>	<b>2,830,799</b>	<b>2,031</b>	<b>1,653</b>
<b>Adjustments:</b>				
- Cash	6,381	274,372	197	160
- Debt	(5,429)	(233,428)	(168)	(136)
- Working Capital	707	30,413	22	18
- Others	674	28,996	21	17
- Outstanding Warrants	3,913	168,240		98
- Treasury Shares	6,091	261,921		153
<b>Total</b>	<b>12,338</b>	<b>530,515</b>	<b>72</b>	<b>310</b>
<b>Total Value</b>	<b>78,170</b>	<b>3,361,313</b>	<b>2,103</b>	<b>1,963</b>

Source: Company Filings, Bear Stearns Asia Ltd. estimates.

## E&P Valuation Update

During the week of April 16-20 2007 we visited RIL's exploration and production (E&P) offices in Mumbai and Tranococean's Discovery Frontier drill ship which had just completed the R1 exploration well in RIL's prolific KG -DWN-98/2 (D6) block offshore India's east coast. The visit gave us a rare first hand look into RIL's upstream operations and a chance to speak directly with the company's geologists and geophysicists (G&G) about the prospects for D6, NEC-25 and D4. As a result of this visit we have made significant adjustments to our upstream earnings and valuation estimates. Other observations include;

- We estimate RIL's upstream operations are worth at the minimum some US\$30.0 billion up 53.1% from our earlier estimate of US\$19.6 billion.
- Determining the value of D6, NEC-25 and D4 is an extremely complex and a continually evolving exercise influenced by technical, political and economic factors.
- RIL's upstream operational center is world class, supported by 180 geologist and geophysicists and the latest technology such as dedicated project 3D visualization rooms and a real time drilling centers that rival the best in Houston and Calgary.
- D6's recoverable reserves are likely to be multiples of the 2006 11.3 Tcf 2P estimated by Gaffeny Cline and Associates (GC&A)

- Production peak and plateau should easily surpass the phase I development plan of 2.8 Bcf/d as well as subsea and gas processing plant capacity design of 4.2 Bcf/d.
- NEC-25 development schedule is likely to be pushed by back several years (we estimate to 2010 from an earlier estimate of 2009) but deeper gas targets offer the possibility of reserve adjustments.
- After seven years of analyzing D6's structures and plays, RIL's geologist and geophysicists are 'very confident' over the prospects of D4 which could rival D6.

**Figure 2. RIL: Upstream Valuation (LHS) & D6 Valuation (RHS)**

Upstream Value	US\$ mn	INR mn	Basic	Diluted	D6 Base Value	US\$ mn	INR mn	Basic	Diluted
			INR/Share	INR/Share				INR/Share	INR/Share
<b>Producing</b>					- Phase I - Gas (0-2.8 Bcf/d)	9,190	395,176	284	231
- MTP	680	29,250	21	17	- Phase II - Gas (2.8-5.0 Bcf/d)	3,073	132,152	95	77
- Yemen Block 9	60	2,561	2	1	- Phase III - Gas (5.0-9.2 Bcf/d)	0	0	0	0
<b>Total</b>	<b>740</b>	<b>31,810</b>	<b>23</b>	<b>19</b>	- Phase V - Oil	1,237	53,200	38	31
					- Phase VI - Condensate	790	33,967	24	20
<b>Development</b>					<b>Total</b>	<b>14,291</b>	<b>614,495</b>	<b>441</b>	<b>359</b>
- D6 Base	14,291	614,495	441	359	<b>D6 Upside Value</b>				
- D6 Risked Upside	2,936	126,255	91	74	- Phase I - Gas (0-2.8 Bcf/d)	1,869	80,360	58	47
- CBM	602	25,869	19	15	- Phase II - Gas (2.8-5.0 Bcf/d)	2,356	101,287	73	59
- NEC-25	2,095	90,090	65	53	- Phase III - Gas (5.0-9.2 Bcf/d)	6,820	293,273	210	171
<b>Total</b>	<b>19,923</b>	<b>856,709</b>	<b>615</b>	<b>500</b>	- Phase V - Oil	187	8,021	6	5
					- Phase VI - Condensate	513	22,079	16	13
<b>Exploration</b>					<b>Total</b>	<b>11,745</b>	<b>505,020</b>	<b>362</b>	<b>295</b>
- D4	8,613	370,375	266	216	- Probability	25%	25%	25%	25%
- Exploration Acreage	748	32,173	23	19	<b>Value</b>	<b>2,936</b>	<b>126,255</b>	<b>91</b>	<b>74</b>
<b>Total</b>	<b>9,362</b>	<b>402,548</b>	<b>289</b>	<b>235</b>	<b>Total</b>	<b>17,227</b>	<b>740,750</b>	<b>532</b>	<b>433</b>
<b>Grand Total</b>	<b>30,025</b>	<b>1,291,067</b>	<b>926</b>	<b>754</b>					

Source: Niko Resources, indianpetro.com, Bear Stearns Asia Ltd. estimates.

### Refining and Chemical Valuation Update

We made several adjustments to our core refining and chemicals valuation. Combined with the changes to our upstream assumptions, the changes have resulted in 18.1% to 145.4% increases in our net profit forecast over the FY2008 to FY2010 period. Our assumption changes include:

- We increased our Singapore complex refining margin forecast to US\$6.00/bbl from US\$5.50/bbl for 2007 / 2008 and RIL's premium over the Singapore benchmark margin to US\$5.00/bbl from US\$4.50/bbl.
- RIL's Jamnagar refining and chemical complex has been granted export-oriented unit (EoU) status, which we expect will allow RIL to maintain its current 15-17% corporate tax rate.
- We increased our realized chemical EBIT margin assumptions by 7.4% to 22.4% for FY2008 through FY2010 as our previous cautious estimates have given way to repeated capacity delays in the Middle East.
- RIL's new 2.0 mn tpa chemical cracker has been included in our core discounted cash flow.

We also assign a higher valuation to Reliance Petroleum Ltd. (RPL), equal to the IPO price, as the company is on track for early completion of its 580 Mbb/d refinery and RPL's share price is trading 35.0% above its IPO price.

### Retail Valuation Update

RRL's rollout of stores is gathering pace with 135 stores now open across 16 cities. RIL indicated that sales volumes are sustaining rates three times what RIL expected at this stage and Reliance Fresh stores are capturing 15-20% operating profit margins (above industry norms but in line with RIL expectations). We expect store openings to ramp up in FY2008 and more news flow to provide greater visibility. We increased our valuation of RRL to RIL to INR145 per share from INR130 per share due to the following changes in our assumptions:

- We now assume India's retail market size at US\$275 bn (previously US\$220 bn), which is mid-range between the low estimate (KPMG's US\$220 bn figure) and the high estimate (AT Kearney and Technopak's US\$350 bn estimate).
- Due to increasing competition, we lowered our forecast market share for RRL to 5.0% from 6.0%
- Our forecast net margin has been increased to 4.0% from 3.5% on the back of strong operating margins to date.

**Figure 3. RIL: Financial Summary**

Year End (INR bn)	— Gross —		— Cost of Goods Sold —			— Operating —		Net Income	EPS INR	DPS INR
	Revenue	Income	Margin	Expense	% Sales	EBITDA	Margin			
FY2010E	1,415	420	30%	995	70%	367	26%	241.93	141.27	24.56
FY2009E	1,076	276	26%	800	74%	249	23%	135.79	79.29	13.79
FY2008E	945	223	24%	723	76%	201	21%	100.66	58.78	10.22
<b>Changes From Original Estimates (January 19, 2006)</b>										
FY2010E	56%	96%	26%	43%	-8%	74%	12%	145%	100%	134%
FY2009E	18%	34%	14%	13%	-4%	25%	6%	51%	23%	45%
FY2008E	0%	10%	10%	-2%	-3%	11%	10%	18%	-4%	13%

Source: Company Filings, Bear Stearns Asia Ltd. estimates.

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Martin Foot

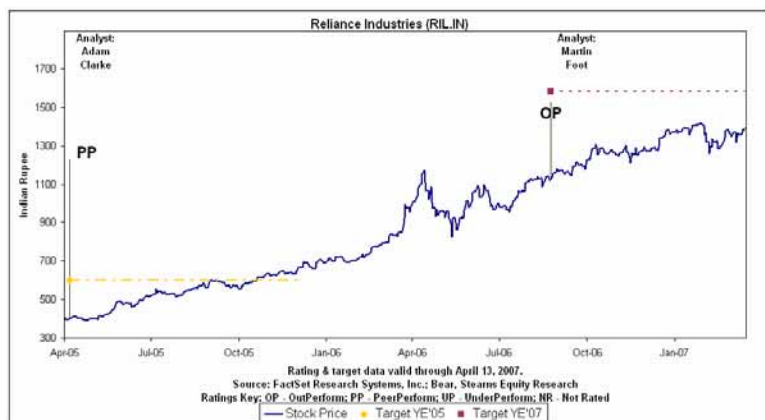
## Companies Analyzed

**Reliance Industries (RIL.IN)** - INR1538.2 (as of April 27, 2007 market close) - Outperform

Price Target ('07): INR2000

Risk(s) to Price Target - Oil and gas prices, refining and chemical margins, capex, and retail market

Valuation Methodology - DCF and Sum of the Parts



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Peer Perform (Neutral): 49.4 / 11.8  
Underperform (Sell): 9.0 / 7.2

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