



BPCL

STOCK INFO.	BLOOMBERG
BSE SENSEX: 13,033	BPCL IN
	REUTERS CODE
S&P CNX: 3,767	BPCL.BO

1 November 2006

Buy

Previous Recommendation: Buy

Rs409

Equity Shares (m)	300.0
52-Week Range (Rs)	503/291
1,6,12 Rel. Perf. (%)	5/-16/-55
M.Cap. (Rs b)	122.7
M.Cap. (US\$ b)	2.7

YEAR	NET SALES	PAT	EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/
END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
03/06A	775,161	5,373	14.9	-71.0	27.5	1.5	6.7	9.2	0.3	11.4
03/07E	903,542	12,502	34.6	132.7	11.8	1.3	14.1	17.7	0.2	6.3
03/08E	811,070	16,042	44.4	28.3	9.2	1.4	16.3	21.5	0.2	5.2

- BPCL has reported merged numbers. Net profit at Rs12.6b as against a loss of Rs188m, was primarily driven by oil bonds. Fuel marketing losses continue to hurt, though upstream sharing and product price discounts from refineries cushioned losses.
- GRM was down sharply at about US\$1/bbl for Mumbai refinery and less than US\$0.25/bbl for Kochi refinery, as a fall in global margins along with the negative impact of octroi and inventory losses impacted margins.
- Fuel marketing losses were up over 79% YoY at Rs36.3b. Upstream contribution of Rs13.4b cushioned the losses. Oil bonds of Rs32.1b was the key driver of 2QFY07 performance. Crude thruput of 5m tons was up 20% YoY as new capacity stabilized, while market sales was up 8.6% on the back of lower retail thruput by private players.
- As in the case of HPCL, we observe that the upstream share and oil bonds are ahead of what is warranted by the losses in 1HFY07. While this could be adjusted in 2HFY07, it could also signal a change in Government's approach towards OMCs.
- The stock is trading at 9.2x FY08E earnings and 1.4x FY08E book value. We believe valuations are cheap given their normalized earnings capability. We maintain **Buy**.

QUARTERLY PERFORMANCE (STANDALONE)

(Rs Million)

Y/E MARCH	FY06			FY07			FY06	FY07E
	1Q	2Q	2HE	1Q	2Q	2HE		
Gross Sales	186,543	189,565	475,388	254,338	288,323	534,155	851,496	1,076,816
Change (%)	28.1	28.3	173.5	36.3	52.1	12.4	21.1	26.5
Raw Material Consumed	54,638	76,843	192,179	105,979	120,207	111,703	323,660	337,889
Staff Cost	2,078	1,864	4,874	2,414	2,087	3,887	8,816	8,388
Finished Goods Purchase	98,807	98,057	192,980	105,801	118,179	378,515	389,844	602,495
Other Exp (incl Stock Adj)	26,141	31,979	69,027	42,753	30,712	32,459	127,147	105,924
EBITDA	-1,126	1,222	9,477	-2,609	17,138	7,592	9,573	22,121
Change (%)	-129.3	-74.0	186.8	nm	1,302.5	-19.9	-64.9	131.1
% of Net Sales	-0.6	0.6	2.0	-1.0	5.9	1.4	0.7	2.1
Depreciation	1,829	1,798	4,053	1,814	1,964	4,202	7,680	7,980
Interest	470	461	1,543	908	920	1,635	2,474	3,463
Other Income	890	1,503	2,260	1,091	2,207	1,233	4,653	4,531
PBT	-2,535	466	6,141	-4,240	16,461	2,987	4,072	15,208
Tax	258	278	620	25	3,876	697	1,156	4,598
Rate (%)	-10.2	59.7	10.1	-0.6	23.5	23.3	14.0	30.2
PAT	-2,793	188	5,521	-4,265	12,585	2,291	1,297	10,611
Change (%)	-250.3	-94.2	278.9	nm	6,594.1	-58.5	-86.6	718.4

E: MOST Estimates

BPCL has reported merged numbers. Net profit at Rs12.6b as against a loss of Rs188m, was primarily driven by oil bonds. Fuel marketing losses continue to hurt, though upstream sharing and product price discounts from refineries cushioned losses.

Oil bonds save the day

Fuel marketing losses were up over 79% YoY at Rs36.3b. While, upstream contribution of Rs13.4b cushioned the losses, oil bonds of Rs32.1b was the key driver of 2QFY07 performance.

As in the case of HPCL, we observe that the proportion of oil bonds and upstream share is higher than the original formula based on Rs735b of losses for FY07. While, the same could be adjusted in 2HFY07, we are not sure, if there is a change in the Government's approach in tackling OMCs' losses. Cashflow and profitability are particularly important given the large capex lined up to meet modernization requirement (in view of the time bound EURO norms implementation) of most refineries.

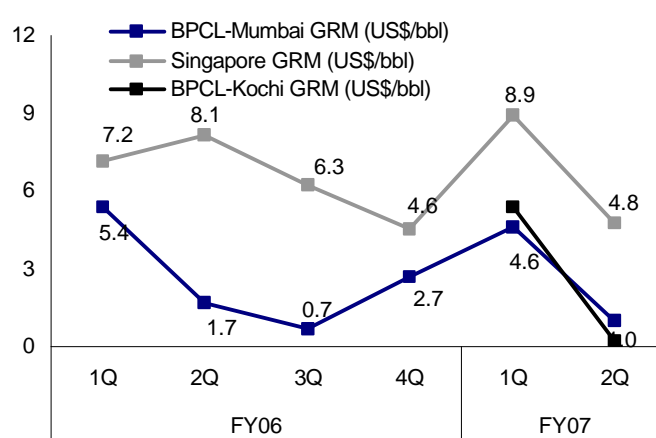
Refining margins suffer

2QFY05 refining margins were down sharply at about US\$1/bbl for Mumbai refinery and less than US\$0.25/bbl for Kochi, on account of lower global margins, impact of octroi, product price discounts and inventory losses.

Singapore complex margins were down at US\$4.75/bbl in 2QFY07. BPCL's Mumbai refinery suffers a penalty in the form of octroi on crude purchase. We estimate the negative impact of octroi during the quarter at US\$2.1/bbl on the GRM.

Refineries pass on discounts on LPG and kerosene to marketing division. We estimate impact of discounts at US\$0.7/bbl. The sharp fall in crude prices towards the end of the quarter led to an inventory loss of Rs3b on the crude stocks (split at Rs1b for Mumbai and Rs2b for Kochi), which would have pulled down margins by about US\$1.8/bbl, together accounting for the poor reported GRM.

QUARTERLY REFINERY-WISE MARGIN TREND (US\$/BBL)



Source: Company/ Motilal Oswal Securities

Refining thruput improves

Crude thruput was up about 20% YoY on the back of stabilization of new capacity. Marketing volumes too were up 8.6% YoY on the back of higher crude thruput and lower retail competition on account of private players winding down their retail volumes due to higher under recoveries.

Valuation and view

The stock is trading at 9.2x FY08E earnings and 1.4x FY08E book value. We believe valuations are cheap given their normalized earnings capability. We maintain **Buy**.

BPCL: an investment profile

Company description

Fortune 500 company, it is the second largest oil marketing company in India, with a refining capacity of 9m ton at Mumbai and a product sale of over 20.5m ton. It has merged its refining subsidiary Kochi Refineries with itself. Kochi Refineries owns 7.5m ton of refining capacity. BPCL also has a majority stake (63%) in Numaligarh Refineries, a 3m ton refinery in the North East

Key investment arguments

- ✍ Government has issued oil bonds, once again driving home the point that OMCs would not be allowed to report losses.
- ✍ Policy risk priced in. Valuations continue to reflect highly pessimistic earnings expectation.

Key investment risks

- ✍ Continued increase in crude prices, along with non-revision of retail prices of controlled products.
- ✍ Loss of market share to private players.

Recent developments

- ✍ Merger with Kochi refineries effected
- ✍ Oil bonds issued to compensate for 1HFY07 losses.

Valuation and view

- ✍ The stock is trading at 9.2x FY08E earnings and 1.4x FY08E book value. Valuations are cheap compared to normalized earnings capability.
- ✍ We maintain **Buy**.

Sector view

- ✍ Refining margins are on an upswing due to improved fundamentals, globally. We expect the upcycle to continue, at least over the next 18 months.

COMPARATIVE VALUATIONS

		BPCL	HPCL	IOC
P/E (x)	FY07E	11.8	11.1	14.4
	FY08E	9.2	8.6	11.3
P/BV (x)	FY07E	1.6	1.2	1.6
	FY08E	1.4	1.0	1.4
EV/Sales (x)	FY07E	0.2	0.2	0.3
	FY08E	0.2	0.2	0.4
EV/EBITDA (x)	FY07E	6.3	8.0	7.4
	FY08E	5.2	6.3	6.3

SHAREHOLDING PATTERN (%)

	JUN.06	MAR.06	JUN.05
Promoters	66.2	66.2	66.2
Domestic Institutions	13.8	13.6	14.5
FII's/FDIs	17.2	17.5	15.6
Others	2.8	2.7	3.7

EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY07	34.6	32.4	6.7
FY08	44.4	34.6	28.5

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
409	-	-	Buy

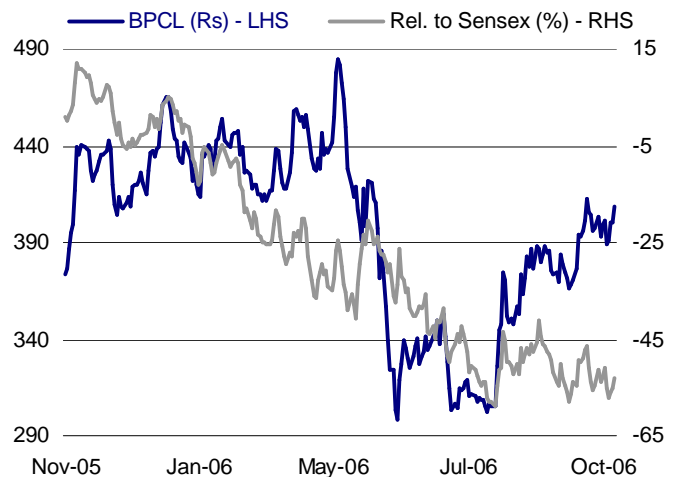
INCOME STATEMENT					
(Rs Million)					
Y/E MARCH	2005	2006E	2007E	2008E	2009E
Net Sales	644,268	775,161	903,542	811,070	726,308
Change (%)	19.5	21.1	24.7	-9.3	-9.3
Total Income	644,272	775,166	903,547	811,075	726,313
Finished Gds Purchase	286,850	334,949	456,647	395,792	338,244
Raw Materials Cons	286,956	363,185	359,065	337,430	310,971
Duties, Taxes, etc	33,009	59,794	59,765	46,748	48,824
EBITDA	37,453	17,233	28,065	31,101	28,269
% of Net Sales	5.8	2.2	3.1	3.8	3.9
Depreciation	8,806	9,458	9,582	9,386	9,746
Interest	2,495	3,052	3,739	966	652
Other Income	3,578	3,994	4,249	4,191	5,399
Extraordinary Items (net)	0	0	0	0	0
PBT	29,730	8,717	18,992	24,940	23,270
Tax	9,014	1,681	6,060	8,337	7,745
Rate (%)	30.3	19.3	31.9	33.4	33.3
Minority Interest	5,321	1,663	430	561	91
PAT	15,395	5,373	12,502	16,042	15,434
Adjusted PAT	15,395	5,373	12,502	16,042	15,434
Change (%)	-27.9	-65.1	132.7	28.3	-3.8

BALANCE SHEET					
(Rs Million)					
Y/E MARCH	2005	2006E	2007E	2008E	2009E
Share Capital	3,000	3,615	3,615	3,615	3,615
Reserves	73,551	80,425	89,120	100,298	110,824
Net Worth	76,551	84,040	92,735	103,913	114,439
Equity	3,350	2,725	2,725	2,725	2,725
Reserves	13,407	3,160	3,824	4,620	4,946
Minority interest	16,757	5,884	6,549	7,345	7,671
Loans	55,478	64,689	53,142	45,798	28,061
Deferred Tax	16,697	18,182	20,467	23,652	25,805
Capital Employed	165,485	172,795	172,892	180,708	175,976
Gross Fixed Assets	182,213	204,858	220,293	231,370	242,744
Less: Depreciation	74,119	82,948	92,390	101,637	111,243
Net Fixed Assets	108,094	121,910	127,903	129,733	131,501
Capital WIP	17,305	12,994	11,994	11,894	11,794
Investments	830	1,474	1,333	4,719	7,856
Curr. Assets, L & Adv.					
Inventory	83,558	56,526	52,041	47,861	43,283
Debtors	14,501	20,423	23,669	21,845	19,978
Cash & Bank Balance	10,052	15,375	22,971	31,333	26,134
Loans & Advances	30,466	32,243	33,801	34,344	35,011
Current Liab. & Prov.					
Liabilities	94,664	85,334	94,770	93,603	91,971
Provisions	4,658	2,817	6,050	7,419	7,610
Net Current Assets	39,255	36,417	31,662	34,361	24,825
Application of Funds	165,485	172,795	172,892	180,708	175,976

E: M OSt Estimates

RATIOS					
Y/E MARCH	2005	2006E	2007E	2008E	2009E
Basic (Rs)					
EPS	51.3	14.9	34.6	44.4	42.7
Cash EPS	80.7	410	611	70.3	69.7
Book Value	255.2	232.5	256.5	287.4	316.6
Dividend	12.0	0.0	9.0	12.0	0.0
Valuation (x)					
P/E	8.0	27.5	11.8	9.2	9.6
Cash P/E	5.1	10.0	6.7	5.8	5.9
EV / EBITDA	4.5	11.4	6.3	5.2	5.3
EV / Sales	0.3	0.3	0.2	0.2	0.2
Price / Book Value	1.6	1.8	1.6	1.4	1.3
Dividend Yield (%)	2.9	0.0	2.2	2.9	0.0
Profitability Ratios (%)					
RoE	21.7	6.7	14.1	16.3	16.3
RoCE	29.5	9.2	17.7	21.5	21.5
Turnover Ratios					
Debtors (No. of Days)	7	7	7	7	7
Asset Turnover (x)	3.0	3.6	2.6	2.6	2.6
Leverage Ratio					
Debt / Equity (x)	0.7	0.8	0.6	0.4	0.2

STOCK PERFORMANCE (1 YEAR)



N O T E S

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Disclosure of Interest Statement	BPCL
1. Analyst ownership of the stock	No
2. Group/Directors ownership of the stock	No
3. Broking relationship with company covered	No
4. Investment Banking relationship with company covered	No

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