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- Government finally decided to take some measures to tackle subsidy issues – Big positive for OMC’s and upstream companies
- Diesel price hike of Rs.5/ltr (including Rs.1.5/ltr excise duty), excise duty cut in petrol by Rs.5.3/ltr and restricting 6 subsidized LPG cylinders per household
- Overall under recovery declines by Rs.203bn to Rs.1684bn for FY13E. Government to benefit Rs.127bn for 2HFY13
- Maintain Buy on HPCL (TP Rs.360), GAIL (TP Rs.406) and Accumulate on IOC (TP Rs.320), BPCL (TP Rs.406), ONGC (TP Rs.327) OIL (TP Rs.573)

Positive outcome of CCEA meeting

The government finally decided to take some measure to tackle subsidy issues

Key Highlights -

- Diesel prices hiked by Rs.5/ltr, including excise duty hike of Rs1.5/ltr.
- However, government has not hiked petrol, kerosene and LPG rates.
- Reduced excise duty on petrol by Rs 5.50/ltr from existing rate of Rs.14.78/ltr.
- Government has also decided to restrict supply of subsidized cooking gas to 6 cylinders per household per year.
- Considering the Diesel price hike; inflation will be impacted by 0.58%

Overall under recovery for OMC’s to come down by Rs.203bn to Rs.1684bn for FY13E:

1. Diesel price hike of INR 5/ltr will help to reduce the under recovery by Rs.297bn for the OMC’s. However for FY13E, we have to consider 6 months impact which would be around Rs.148bn.

2. Capping of LPG Cylinders to 6 per household from average consumption of 8.4 per household, will bring down industry under recovery by Rs. 108 bn. However for FY13E, for 6 months saving would be Rs. 54 bn.

Exhibit 1: Industry Under recovery before Price hike and LPG capping

Particulars	Units	Before Price hike		After Price hike		Reduction in UR
		H1 FY13E	H2 FY13E	H1 FY13E	H2 FY13E	
Diesel Consumption	MMT	33.2	35.8	33.2	35.8	
Under Recovery	Rs/ltr	13.3	16.5	13.3	13.0	
Total Under Recovery	Rs/mn	517,146	694,663	517,146	546,047	148,616

Source: Industry, Emkay Research

Exhibit 2: Subsidy snapshot before policy measures

Particulars	Q1 FY13A	Q2 FY13E	H2 FY13E	FY13E
Diesel	287,345	229,801	694,663	1,211,809
LPG	104,610	64,440	212,544	381,594
Kerosene	76,200	70,626	147,692	294,518
Total (in mn)	468,155	364,867	1,054,899	1,887,921

Source: Industry, Emkay Research

Exhibit 3: Revised selling price of diesel

City	Rs./ltr
Mumbai	51.3
Delhi	46.3
Chennai	48.9
Kolkata	49.8

Source: Industry, Emkay Research

LPG cylinders capped at 6/household per year from average consumption of 8.4 currently

In India each house hold consumes ~8.4 cylinders per year. It has been capped at 6 per household per year which will bring down industry under recovery by Rs.108bn. However for FY13E, the 6 months saving would be Rs.54bn.

Exhibit 4: Impact of LPG cylinder cap.

Particulars	Units	Current			
Customers	Cr	12.7	12.7	12.7	12.7
Consumption	Mn/Tonne	15.1			
Consumption Per Customer	Tonne	0.1			
Consumption Per Customer	Kg	118.9			
Cylinder of 14.2 Kg	No	8.4	6	5	4
Total Cylinder Consumption	Mn Cylinder	1063	762	635	508
Per Cylinder Under Recovery	Rs/Cylinder	358	358	358	358
Total Industry Under Recovery	Rs/mn	380690	272796	227330	181864
Saving In Subsidy	Rs/mn		107894	153360	198826

Source: Industry, Emkay Research

In our view GAIL will be biggest beneficiary out of LPG measures taken by the government as GAIL contributes towards LPG under recovery only. Based on our calculation GAIL earnings would be increase by ~10% for FY13 to Rs.29.2 to Rs.32.1.

Excise Duty on Petrol cut by Rs. 5.3/ltr loss of Rs.110bn to the exchequer on annualized basis.

Exhibit 5: Calculation of decrease in excise duty on Petrol by Rs.5.3/ltr

	Before hike in excise	After hike in excise by Rs.1.5/ltr
Total consumption/Kiloliter/p.a	20.9	20.9
Excise duty/Ltr	14.78	9.48
Total Excise collection	309272	198369
Increase in Government collection on p.a basis		-110903
For H2 FY13 (Rs. mn)		-55451

Source: Industry, Emkay Research

OMC's will start making profits on MS from 2nd fortnight of September if international price stays at current level of \$120/bbl: Current under Recovery on MS is at Rs.5.80/ltr and cut in excise duty by Rs.5.3/ltr will make the losses of OMC's almost negligible at current levels. However, based on the current MS prices of \$120/bbl with exchange rate of \$55.58, Oil marketing companies will start making profits of about ~ Rs.0.3-0.5/ltr from the next fortnight.

Increase in excise duty on diesel by Rs. 1.5/ltr, gain of Rs.124bn to the exchequer on annualized basis.

Exhibit 6: Calculation of Increase in excise duty on Diesel

	Before hike in excise	After hike in excise by Rs.1.5/ltr
Total consumption/Kiloliter/p.a	82.8	82.8
Excise duty/Ltr	2	3.5
Total Excise collection	165600	289800
Increase in Government collection on p.a basis		124200
For H2 FY13 (Rs. mn)		62100

Source: Industry, Emkay Research

Net benefit of this measure for government comes at ~Rs.127bn for 2HFY13.

Exhibit 7: Net Benefit of this measure to the government

	Rs. mn
Reduction of excise on Petrol	-55451
Increase in excise on Diesel	62100
Subsidy reduction benefit (assuming 60% government share)	121200
Net benefit to government (Rs. mn)	127849

Source: Industry, Emkay Research

Our View

While OMC's and upstream companies would benefit from the move, we have not changed our estimates of both OMC's and upstream companies as we believe that government will compensate full losses of OMC's as seen in the FY12. Also for upstream companies like ONGC, OIL and GAIL the final sharing would be decided at the last quarter of FY13 as seen in FY12, which will decide the full year profitability. Currently OMC's are trading in the range of 0.9-1.3x FY13E P/BV. We maintain our Buy rating on HPCL (TP Rs.360), GAIL (TP Rs.406) and Accumulate on IOC (TP Rs.320), BPCL (TP Rs.406), ONGC (TP Rs.327) OIL (TP Rs.573).

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