



## Indian Oil Corporation

STOCK INFO. BLOOMBERG  
BSE Sensex: 20,310 IOCL IN

S&P CNX: 6,122 REUTERS CODE  
IOC.BO

15 November 2010

Buy

Previous Recommendation: Buy

Rs399

Equity Shares (m)	2,428.0
52-Week Range (Rs)	459/274
1,6,12 Rel. Perf. (%)	-2/10/15
M.Cap. (Rs b)	968.8
M.Cap. (US\$ b)	21.4

YEAR	NET SALES	ADJ. PAT	ADJ. EPS	EPS	P/E	P/BV	ROE	ROCE	EVI	EVI
END	(RS B)	(RS B)	(RS)	GR. (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
03/09A	2,861	26.0	10.9	-67.1	36.6	0.0	5.8	8.2	0.0	0.0
03/10A	2,501	107.1	44.1	304.8	9.0	1.7	21.9	16.0	0.6	10.7
03/11E	2,689	83.7	34.5	-21.8	11.6	1.7	15.3	13.7	0.5	8.2
03/12E	2,263	96.9	39.9	15.8	10.0	1.5	16.1	16.1	0.5	6.7

\*Consolidated

- In line:** IOC posted 2QFY11 EBITDA of Rs65.2b (against our estimate of Rs66.21). EBITDA was in line despite higher-than-expected government compensation of Rs72.2b (against our estimate of Rs61.3b) and higher GRMs of US\$6.58/bbl against our estimate of US\$4.3/bbl. This was offset by (1) lower marketing volumes at 16.9mmt (against our estimate of 18.1mmt) resulting in a shortfall of Rs3b, (2) higher staff costs of Rs16b (against our estimate of Rs9.8b) and (3) EBIT loss in the petchem segment of Rs5b. Reported 2QFY11 PAT was Rs52.9b, which was in line with our estimates, (v/s loss of Rs33.8b in 1QFY11 and profit of Rs2.84b in 2QFY10). 1HFY11 EBITDA was Rs36b and PAT was Rs19b (v/s full year FY10 EBITDA of Rs122b and PAT of Rs102b).
- Subsidy sharing ad hoc:** In 1HFY11, gross under-recovery was Rs174.2b (Rs64b in 2QFY11), of which upstream shared Rs58.1b and government compensated Rs72b, resulting in a net under-recovery of Rs43.9b. In 1HFY11, OMCs (HPCL, BPCL and IOC) shared 26% of the gross under-recovery (IOC typically shares 55% of this).
- Clarity on subsidy sharing towards end-FY11:** As the government did not compensate companies in 1QFY11, 2QFY11 compensation factors in 1QFY11 dues, though the subsidy sharing amount is ad hoc. As in previous years, subsidy sharing is likely to be finalized only towards the end of the year, in the 4QFY11 and hence quarterly sharing is no indication of the final sharing formula.
- Awaiting clarity on diesel deregulation and subsidy rationalization After partial deregulation in June 2010, the government has been silent about the next phase of deregulation. While expectations run high on diesel deregulation and subsidy rationalization, we believe the government is having second thoughts on the pace of deregulation due to (1) higher oil prices, (2) forthcoming elections in various states, and (3) impact on inflation.
- Valuation and view:** We model oil marketing companies (HPCL, BPCL and IOC) to share 11% of gross under-recoveries in FY11 and FY12. The stock trades at 11.6x FY11E cons EPS of Rs34.5 and 1.7x FY11E BV. **Buy.**

### QUARTERLY PERFORMANCE (STANDALONE)

(Rs Million)

Y/E MARCH	FY10				FY11				FY10	FY11E
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE		
<b>Net Sales</b>	<b>621,966</b>	<b>607,461</b>	<b>740,595</b>	<b>821,571</b>	<b>716,726</b>	<b>769,666</b>	<b>734,304</b>	<b>735,110</b>	<b>2,791,594</b>	<b>2,955,806</b>
Change (%)	-29.6	-29.6	5.2	37.9	15.2	26.7	-0.8	-10.5	-8.4	5.9
<b>EBITDA</b>	<b>41,409</b>	<b>4,314</b>	<b>3,457</b>	<b>72,986</b>	<b>-29,175</b>	<b>65,210</b>	<b>43,666</b>	<b>59,401</b>	<b>122,165</b>	<b>139,101</b>
% of Net Sales	6.7	0.7	0.5	8.9	-4.1	8.5	5.9	8.1	4.4	4.7
% Change	331.2	nm	-89.3	-15.3	-170.5	1,411.7	1,163.1	-18.6	195.0	13.9
Depreciation	7,598	7,805	7,996	8,872	10,346	11,178	11,200	11,237	32,271	43,961
Interest	3,340	3,477	4,091	4,357	5,712	5,079	4,935	4,571	15,265	20,297
Other Income	23,625	10,306	13,798	18,703	11,349	12,309	13,417	10,428	66,432	47,503
<b>PBT</b>	<b>54,096</b>	<b>3,337</b>	<b>5,168</b>	<b>78,460</b>	<b>-33,884</b>	<b>61,262</b>	<b>40,947</b>	<b>54,021</b>	<b>141,061</b>	<b>122,346</b>
Tax	17,267	493	-1,798	22,893	0	8,323	13,602	18,716	38,855	40,640
Rate (%)	31.9	14.8	-34.8	29.2	0.0	13.6	33.2	34.6	27.5	33.2
<b>PAT</b>	<b>36,828</b>	<b>2,844</b>	<b>6,966</b>	<b>55,567</b>	<b>-33,884</b>	<b>52,939</b>	<b>27,346</b>	<b>35,305</b>	<b>102,206</b>	<b>81,706</b>
Change (%)	787.2	nm	-76.5	-16.1	-192.0	1,761.5	292.6	-36.5	177.5	-20.1

E: MOSL Estimates

### Operational performance

- IOC reported GRM of US\$6.57/bbl (against our estimate of US\$4.3/bbl) v/s US\$3/bbl in 1QFY11 and US\$3.5/bbl in 2QFY10. We believe the significant improvement of IOC's GRM over Singapore GRM was led by inventory gains. We will try to get more details from the company.
- Total throughput as 12.1mmt v/s our estimate of 13.2mmt (down 8.6% YoY and 2.2% QoQ).

### IOC: 2QFY11 operational highlights

	FY10				FY11		2QFY11	
	1Q	2Q	3Q	4Q	1Q	2Q	YoY (%)	QoQ (%)
Product sales (mmt)	17.7	16.7	17.6	17.7	18.3	16.9	1.2	(7.6)
Throughput (mmt)	12.5	12.4	12.5	13.3	13.3	12.1	(2.2)	(8.6)
GRM (US\$/bbl)	7.4	3.5	3.7	3.4	3.0	6.6	89.7	119.4

Source: Company/MOSL

### Other key highlights

- Gross debt as on September 2010 was Rs442b (v/s Rs446b as on 31 March 2010).
- Other income includes gains from foreign exchange of Rs6.4b (1HFY11 Rs1.76b).
- Staff costs in 2QFY11 rose to Rs16b against Rs9.8b in 1QFY11.

### IOC's subsidy sharing: expect clarity by end-FY11

	FY10				FY11		2QFY11		FY10	1HFY11
	1Q	2Q	3Q	4Q	1Q	2Q	YoY (%)	QoQ (%)		
<b>Gross under-recovery</b>	<b>31.9</b>	<b>59.7</b>	<b>75.6</b>	<b>91.6</b>	<b>110.1</b>	<b>64.1</b>	<b>7.3</b>	<b>(41.8)</b>	<b>258.8</b>	<b>174.2</b>
<b>Less: Sharing</b>										
Upstream sharing	2.3	18.0	22.7	32.5	36.7	21.4	19	(41.8)	75.5	58.1
Oil bonds	-	-	44.8	106.9	-	72.2	nm	nm	151.7	72.2
<b>Net under/(over)recovery</b>	<b>29.6</b>	<b>41.7</b>	<b>8.0</b>	<b>(47.8)</b>	<b>73.4</b>	<b>(29.5)</b>	<b>nm</b>	<b>nm</b>	<b>31.6</b>	<b>43.9</b>
As percentage of gross	92.8	69.9	10.6	nm	66.7	(46.0)			12.2	25.2

Source: Company/MOSL

### Subsidy sharing ad-hoc: industry-wide under-recoveries, sharing (Rs b)

	FY08	FY09	FY10	1HFY11	FY11E	FY12E
Forex Rate (Rs/US\$)	40.3	46.0	47.5	46.2	45.3	44.5
Brent (US\$/bbl)	82.3	84.8	69.6	77.3	76.9	75.0
<b>Sharing (Rs b)</b>						
Oil Bonds/Cash	353	713	260	130	280	199
Upstream	257	329	145	105	165	119
OMC sharing	163	(9)	56	85	55	39
<b>Total</b>	<b>773</b>	<b>1,033</b>	<b>461</b>	<b>319</b>	<b>500</b>	<b>357</b>
<b>Sharing (%)</b>						
Oil Bonds	46	69	56	41	56	56
Upstream	33	32	31	33	33	33
OMC sharing	21	(1)	12	27	11	11
<b>Total</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>

Source: Company/MOSL

## Indian Oil Corporation: an investment profile

### Company description

A Fortune-500 company, IOC is the largest refining and marketing company in India. It operates eight refineries (including BRPL) and has a capacity of 49.7mtpa. It has a 52% stake in CPCL (10.5mmt refining capacity). It has a pipeline network of >10,300km (62mtpa capacity), 18,278 petrol/diesel outlets and interests in petrochemicals and upstream oil and gas. It is a public sector company, in which the government of India has 80.35% stake.

### Key investment arguments

- IOCL's profitability is determined by the quantum of under-recoveries and sharing mechanism, rather than fundamentals. But recently hopes were rejuvenated by the partial deregulation of automobile fuel. No further policy decision has been taken by the government.
- Growth would come from (1) expansion of the Panipat refinery from 12 to 15mtpa, (2) Rs144b naphtha cracker (commissioned) at Panipat and (3) setting up Rs256b integrated refinery (15mtpa)/petchem complex at Paradip.
- IOC's valuations should benefit from improvement in (1) earnings quality, (2) RoCE & RoE, (3) cash cycle

and (4) lower debt levels.

### Key investments risks

- Maintaining marketing share and margins on auto fuels in view of likely competition from private players.
- Planning of mega investments in view of ad-hoc subsidy sharing.
- Non commensurate increase in the retail fuel prices as oil price rises, leads to under-recoveries for the company and ad-hoc nature of subsidy sharing impacts the profits.

### Recent developments

- Auto fuel was partially deregulated and prices hiked of domestic fuels in June 2010.

### Valuation and view

- The stock trades at 11.6x FY11E cons EPS of Rs34.5 and 1.7x FY11E BV. Maintain **Buy**.

### Sector view

- Refining outlook is weak given low product demand and significant new capacity hitting the market. We expect refining margins to be subdued in the medium term and expect refinery closures guided by poor refinery economics will lead to rationalization in the demand-supply gap.

### Target Price and Recommendation

Current Price (Rs)	Target Price (Rs)	Upside (%)	Reco.
399	-	-	Buy

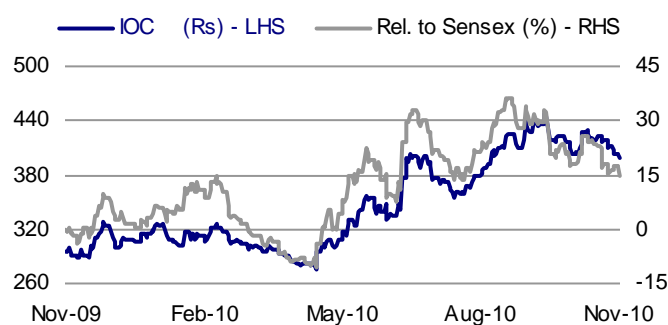
### Shareholding Pattern (%)

	Sep-10	Jun-10	Sep-09
Promoter	79.0	79.0	79.0
Domestic Inst	5.0	5.3	5.5
Foreign	1.1	0.7	1.0
Others	14.9	15.0	14.5

### EPS: most forecast v/s Consensus (rs)

	Most Forecast	Consensus Forecast	Variation (%)
FY11	34.5	48.1	-28.3
FY12	39.9	56.4	-29.3

### Stock performance (1 year)



## Financials and Valuation

INCOME STATEMENT (Consolidated)		(Rs Million)			
Y/E MARCH	2009	2010	2011E	2012E	
<b>Net Sales</b>	<b>2,861,047</b>	<b>2,501,053</b>	<b>2,689,348</b>	<b>2,262,972</b>	
<i>Change (%)</i>	<i>25.5</i>	<i>-12.6</i>	<i>7.5</i>	<i>-15.9</i>	
Finished Gds Purchase	1,424,305	1,007,775	1,428,900	1,001,306	
Raw Materials Cons	1,123,331	1,158,063	988,886	1,000,762	
Other Operating Costs	251,364	206,462	122,739	84,462	
<b>EBITDA</b>	<b>62,046</b>	<b>128,753</b>	<b>148,823</b>	<b>176,443</b>	
<i>% of Net Sales</i>	<i>2.2</i>	<i>5.1</i>	<i>5.5</i>	<i>7.8</i>	
Depreciation	31,894	35,552	47,193	52,989	
Interest	42,076	17,262	22,670	20,802	
Other Income	48,415	74,547	48,302	45,512	
Extraordinary Items (net)	0	0	0	0	
<b>PBT</b>	<b>36,491</b>	<b>150,486</b>	<b>127,262</b>	<b>148,164</b>	
Tax	12,533	40,499	42,265	49,205	
<i>Rate (%)</i>	<i>34.3</i>	<i>26.9</i>	<i>33.2</i>	<i>33.2</i>	
<b>PAT</b>	<b>23,958</b>	<b>109,987</b>	<b>84,997</b>	<b>98,959</b>	
Minority interest	2,036	-2,855	-1,267	-2,032	
<b>Group net profit</b>	<b>25,994</b>	<b>107,132</b>	<b>83,731</b>	<b>96,927</b>	
<i>Change (%)</i>	<i>-67.1</i>	<i>312.1</i>	<i>-21.8</i>	<i>15.8</i>	

BALANCE SHEET		(Rs Million)			
Y/E MARCH	2009	2010	2011E	2012E	
Share Capital	23,847	24,280	24,280	24,280	
Reserves	431,196	500,344	547,145	607,143	
<b>Net Worth</b>	<b>455,044</b>	<b>524,623</b>	<b>571,425</b>	<b>631,423</b>	
<b>Minority interest</b>	<b>15,723</b>	<b>18,330</b>	<b>19,597</b>	<b>21,628</b>	
Loans	473,469	494,726	440,904	293,030	
Deferred Tax	59,742	54,170	59,074	60,492	
<b>Capital Employed</b>	<b>1,003,977</b>	<b>1,091,849</b>	<b>1,090,999</b>	<b>1,006,573</b>	
Gross Fixed Assets	679,293	788,886	1,052,771	1,094,351	
Less: Depreciation	299,303	334,111	381,304	434,293	
<b>Net Fixed Assets</b>	<b>379,990</b>	<b>454,775</b>	<b>671,467</b>	<b>660,058</b>	
Capital WIP	192,148	227,678	34,595	73,015	
Investments	313,345	214,298	297,353	207,704	
Goodwill	4,542	224	224	224	
Cash & Bank Balance	10,052	15,984	47,382	29,748	
Inventory	285,182	410,765	365,720	312,448	
Debtors	47,817	56,062	78,181	68,831	
Loans & Advances	118,628	152,070	70,635	70,635	
Other assets	10,927	15,264	15,264	15,264	
<b>Curr. Assets, L &amp; Adv.</b>					
Liabilities	332,024	351,658	384,751	326,233	
Provisions	26,630	103,612	105,070	105,120	
<b>Net Current Assets</b>	<b>113,952</b>	<b>194,874</b>	<b>87,360</b>	<b>65,572</b>	
Misc. Expenses					
<b>Application of Funds</b>	<b>1,003,977</b>	<b>1,091,849</b>	<b>1,091,000</b>	<b>1,006,573</b>	

E:MOGL Estimates

RATIOS		(Rs Million)			
Y/E MARCH	2009	2010	2011E	2012E	
<b>Basic (Rs)</b>					
<b>EPS</b>	<b>10.9</b>	<b>44.1</b>	<b>34.5</b>	<b>39.9</b>	
Cash EPS	24.3	58.8	53.9	61.7	
Book Value	190.8	216.1	235.4	260.1	
Dividend	7.5	13.0	13.0	13.0	
<b>Valuation (x)</b>					
P/E		9.0	11.6	10.0	
Cash P/E		6.8	7.4	6.5	
EV / EBITDA		10.7	8.2	6.7	
EV / Sales		0.6	0.5	0.5	
Price / Book Value		1.7	1.7	1.5	
Dividend Yield (%)		3.3	3.3	3.3	
<b>Profitability Ratios (%)</b>					
RoE	5.8	21.9	15.3	16.1	
RoCE	8.2	16.0	13.7	16.1	
<b>Leverage Ratio</b>					
Debt / Equity (x)	1.0	0.9	0.8	0.5	

CASH FLOW STATEMENT		(Rs Million)			
Y/E MARCH	2009	2010E	2011E	2012E	
OP/(Loss) before Tax	36,491	150,486	127,262	148,164	
Depreciation	33,391	35,677	47,193	52,989	
Interest Paid	42,076	17,263	22,670	20,802	
Direct Taxes Paid	-10,146	-27,296	-37,361	-47,786	
(Inc)/Dec in Wkg. Capital	94,184	-182,446	138,911	4,154	
Oil Bonds	-403,830	0	-152,700	-110,351	
Other op activities	-5,686	-9,774	0	0	
<b>CF from Op. Activity</b>	<b>-213,520</b>	<b>-16,090</b>	<b>145,976</b>	<b>67,971</b>	
(Inc)/Dec in FA & CWIP	-133,081	-138,236	-70,802	-80,000	
(Pur)/Sale of Investments	316,448	174,184	69,644	200,000	
Other investing activities	114	0	0	0	
<b>CF from Inv. Activity</b>	<b>183,480</b>	<b>35,948</b>	<b>-1,158</b>	<b>120,000</b>	
Issue of Shares					
Inc / (Dec) in Debt	85,259	21,257	-53,821	-147,875	
Dividends Paid	-9,754	-10,907	-36,929	-36,929	
Interest Paid	-46,017	-24,276	-22,670	-20,802	
<b>CF from Fin. Activity</b>	<b>29,489</b>	<b>-13,925</b>	<b>-113,420</b>	<b>-205,605</b>	
<b>Inc / ( Dec) in Cash</b>	<b>-550</b>	<b>5,933</b>	<b>31,397</b>	<b>-17,634</b>	
Add: Opening Balance	10,602	10,052	15,985	47,382	
<b>Closing Balance</b>	<b>10,052</b>	<b>15,985</b>	<b>47,382</b>	<b>29,748</b>	

**N O T E S**



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**Indian Oil Corporation**

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|---|----|
| 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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