Company Focus

18 January 2008 | 16 pages

Reliance Industries (RELI.BO)

Target price change ☑
Estimate change ☑

Buy: Upgrading Target; 3Q In Line but Focus on E&P Upsides

- **New target of Rs3460, upside mainly from E&P** — E&P now accounts for Rs1291/share as we factor higher D-6 production (both gas and oil) and Citi's recent oil price upgrade. As we incorporate higher guidance on "pure exploration" capex, the E&P value is now based on EV/FCF of 15x (12x earlier) on further broad-basing of its discovered assets (KG-D4, KG-III-5).

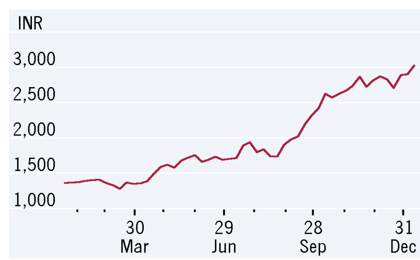
- **FY09-10E earnings up 4-9%** — Driven by higher oil forecasts and upgrade of D-6 oil & gas production esp. in FY10. We are also incorporating slightly higher differentials for the refinery post the upgrade by 1QFY09 to produce cleaner fuels. However, we still build in a material downturn in petrochemicals in FY10 (segmental EBITDA est. to be down 17% yoy).

- **3QFY08 in line, petchem takes a hit** — Petrochemical profitability (down 12% qoq) was primarily on account of higher feedstock prices (naphtha) and the planned shutdown of the PX unit. In contrast, refining continued to be strong (EBIT growth of 13% qoq) delivering US$7.6 spread over Singapore complex which more than offset the lower throughput due to shutdown.

- **Execution not in doubt, risks more on macro front** — Supply side in refining remains tight due to continued project delays and cost escalations; however, a full blown recession in US could impact distillate demand. On the E&P front, RIL continues to face rig shortages which, while not impacting the timeline for KG-D6 development, could potentially slow down its exploration efforts.

Buy/Low Risk	**1L**
Price (17 Jan 08)	Rs2,996.25
Target price	Rs3,460.00
from Rs2,860.00	
Expected share price return	15.5%
Expected dividend yield	0.5%
Expected total return	**16.0%**
Market Cap	Rs4,355,495M
	US$111,081M

Price Performance (RIC: RELI.BO, BB: RIL IN)



Statistical Abstract

Year to 31 Mar	Net Profit (RsM)	Diluted EPS (Rs)	EPS growth (%)	P/E (x)	P/B (x)	ROE (%)	Yield (%)
2006A	90,693	65.10	19.8	46.0	14.6	26.4	0.3
2007A	119,434	82.18	26.2	36.5	6.8	25.8	0.4
2008E	148,046	101.87	24.0	29.4	5.7	21.1	0.5
2009E	198,827	136.82	34.3	21.9	4.7	23.5	0.7
2010E	231,120	159.04	16.2	18.8	3.9	22.5	0.7

Source: Powered by dataCentral

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See Appendix A-1 for Analyst Certification and important disclosures.

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Fiscal year end 31-Mar	2006	2007	2008E	2009E	2010E
Valuation Ratios					
P/E adjusted (x)	46.0	36.5	29.4	21.9	18.8
EV/EBITDA adjusted (x)	30.6	22.1	19.7	15.4	13.4
P/BV (x)	14.6	6.8	5.7	4.7	3.9
Dividend yield (%)	0.3	0.4	0.5	0.7	0.7
Per Share Data (Rs)					
EPS adjusted	65.10	82.18	101.87	136.82	159.04
EPS reported	65.10	82.18	101.87	136.82	159.04
BVPS	205.28	439.56	524.55	638.87	773.16
DPS	10.00	11.00	15.00	20.00	22.00
Profit & Loss (RsM)					
Net sales	812,113	1,116,927	1,200,170	1,258,053	1,255,143
Operating expenses	-702,072	-962,438	-1,018,574	-1,020,628	-988,785
EBIT	**110,041**	**154,489**	**181,596**	**237,424**	**266,358**
Net interest expense	-8,770	-11,889	-12,056	-13,149	-12,853
Non-operating/exceptionals	5,770	2,604	8,829	12,423	21,638
Pre-tax profit	**107,041**	**145,205**	**178,368**	**236,698**	**275,143**
Tax	-16,347	-25,771	-30,323	-37,872	-44,023
Extraord./Min.Int./Pref.div.	0	0	0	0	0
Reported net income	**90,693**	**119,434**	**148,046**	**198,827**	**231,120**
Adjusted earnings	90,693	119,434	148,046	198,827	231,120
Adjusted EBITDA	144,050	202,641	224,797	282,221	315,246
Growth Rates (%)					
Sales	23.0	37.5	7.5	4.8	-0.2
EBIT adjusted	23.2	40.4	17.5	30.7	12.2
EBITDA adjusted	13.8	40.7	10.9	25.5	11.7
EPS adjusted	19.8	26.2	24.0	34.3	16.2
Cash Flow (RsM)					
Operating cash flow	**117,189**	**158,489**	**238,222**	**270,966**	**299,451**
Depreciation/amortization	34,009	48,152	43,201	44,797	48,887
Net working capital	-7,514	-9,097	46,975	27,342	19,444
Investing cash flow	**2,515**	**-401,158**	**-136,000**	**-131,000**	**-109,500**
Capital expenditure	-126,361	-343,737	-136,000	-131,000	-109,500
Acquisitions/disposals	128,876	-57,421	0	0	0
Financing cash flow	**-176,268**	**291,789**	**-36,567**	**-38,627**	**-40,806**
Borrowings	41,174	66,272	-747	-1,853	-764
Dividends paid	-15,885	-18,006	-24,524	-32,698	-35,968
Change in cash	**-56,565**	**49,120**	**65,655**	**101,339**	**149,145**
Balance Sheet (RsM)					
Total assets	**718,893**	**1,161,732**	**1,399,074**	**1,589,004**	**1,793,774**
Cash & cash equivalent	14,192	63,581	129,236	230,575	379,721
Accounts receivable	41,636	37,324	69,889	73,001	72,735
Net fixed assets	441,935	737,520	830,319	916,522	977,135
Total liabilities	**432,909**	**522,946**	**636,766**	**660,567**	**670,185**
Accounts payable	114,387	147,098	229,531	229,131	219,576
Total Debt	218,656	278,007	265,964	260,035	255,197
Shareholders' funds	**285,980**	**638,786**	**762,308**	**928,437**	**1,123,588**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	17.7	18.1	18.7	22.4	25.1
ROE adjusted	26.4	25.8	21.1	23.5	22.5
ROIC adjusted	21.2	20.1	18.2	21.7	22.3
Net debt to equity	71.5	33.6	17.9	3.2	-11.1
Total debt to capital	43.3	30.3	25.9	21.9	18.5

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Revising Earnings and Target Price

We are revising our FY08-10E earnings by 2-9% and increasing our TP to Rs3460.

Figure 1. RIL- Earnings Revision

Year to	Net Profit (Rs Mils.)		Diluted EPS (Rs)			Dividend Per Share (Rs)	
31-Mar	Old	New	Old	New	% Chg	Old	New
2008E	144,687	148,046	99.56	101.87	2.3%	15.0	15.0
2009E	190,914	198,827	131.37	136.82	4.1%	20.0	20.0
2010E	212,523	231,120	146.24	159.04	8.8%	22.0	22.0

Source: Citi Investment Research estimates

The main drivers of our earnings upgrade are as follows:

- Increase in refining margins. This is primarily due to higher expected differentials vis-à-vis Singapore complex spreads driven by the ongoing upgrade of the refinery, which will enable it to produce Euro IV compliant diesel (up to 40% of its total diesel production) for the export market from next quarter. Our main refining margin assumptions are detailed below:

Figure 2. Refining – Key Parameters

	Units	FY06	FY07	FY08E	FY09E	FY10E
Singapore complex spreads	US$/bbl	6.50	6.10	7.50	7.00	6.50
Gross Refining & Mktg Margin						
- new	US$/bbl	10.30	11.60	14.46	14.27	13.94
- old	US$/bbl	10.30	11.60	14.03	13.75	13.94
RIL clean GRMs	US$/bbl	10.30	12.40	14.90	14.50	14.00
Differentials	US$/bbl	3.80	6.30	7.40	7.50	7.50
Crude throughput	MMT	30.6	31.7	32.0	33.0	33.0

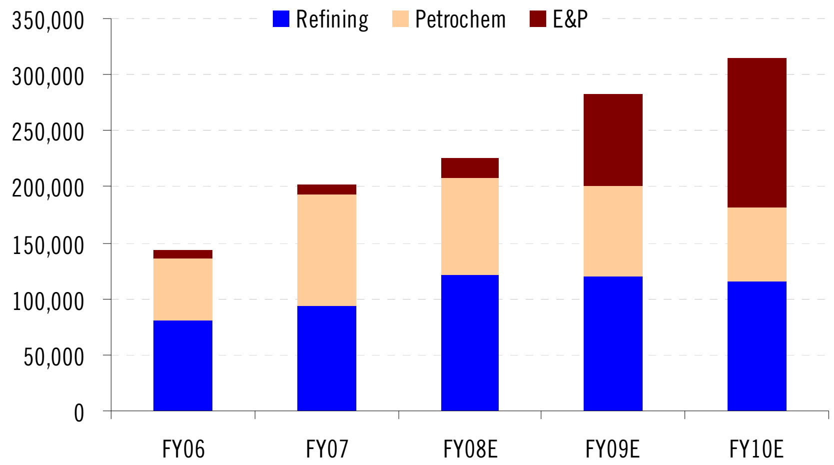
Source: Company Reports, Reuters, Citi Investment Research estimates

- Incorporating MA gas production (commencing in end-FY09 and peaking at 9mmscmd) in addition to the 40-80mmscmd from D1/D3 fields in KG D-6.

- Incorporating higher MA oil production plateau of 45kbpd (40kbpd earlier) to be achieved by end-FY09, in line with management guidance.

- Higher crude price assumptions (LT crude at US$75/bbl), in line with Citi's new global crude forecast.

Figure 3. Segmental EBITDA (Rs m)



Source: Citi Investment Research estimates

TP Increased to Rs3460

Our new SOTP-based target price is Rs3460 (Rs2860 earlier) as shown below.

Figure 4. RIL Sum-of-the-parts Valuation

	Rs m	Rs/share		Comments
		Old	New	
FY09E EBITDA forecast	216,271			Excluding contribution from KG basin
FY10E EBITDA forecast	200,275			
EV of Petrochem and Refining business	1,562,046	1,034	1,074	Valued at EV/E of 7.5x mid-FY10E (7.0x earlier)
Net Debt	17,201	86	12	Est. as on Sep-08, excl. ST Debt and net of liquid inv., incl. profit on recent RPL stake sale
Key investments				
Reliance Petroleum	604,828	416	498	PER of 9x contribution to consolidated profits in FY10E
E&P assets	1,413,326	972	1,291	Based on 15x steady state FCF (incl. D-6 oil and gas upside in FY11E)
Organized retail	190,971	131	137	Roll forward to Dec-08E
Total value of investments & other assets	2,209,125	1,520	1,927	
EV of businesses	1,502,182	1,034	1,074	
Net debt adjusted for key investments	(2,084,789)	(1,434)	(1,915)	
Value of treasury stock	565,325	389	471	At target price
Value for equity holders (Rs m)	4,152,296	2,857	**3,460**	
No. of shares (m)	1,454			

Source: Citi Investment Research estimates

The main drivers of our upgrade are as follows:

- Higher contribution from RIL's stake in RPL at Rs498 per share (Rs416 earlier) at 9x profit contribution (same as before), based on our earnings upgrade of RPL (refer to our note published earlier today) despite the reduction in RIL's stake post its 4% sale of RPL.

- Rolling forward core business (refining + petchem) to Sep-09E (Sep-08E) earlier. Since we now capture a part of the cyclical decline in petchem, our target EV/EBITDA is 7.5x (7.0x earlier), remaining at the higher end of the peers due to the diversified product portfolio and the strong operational performance in the refining segment. In particular, RIL's ability to generate significant spreads over Singapore complex deserves a premium, in our view.

- Incorporating cash from sale of 4% stake in RPL amounting to Rs42bn (net of tax) in net debt.

- Higher contribution of E&P at Rs1291 per share (refer to Figure 5) from Rs972 earlier, which is primarily driven by:

  - Higher crude estimates and changes to MA oil & gas production assumptions as already explained earlier.

  - Deduction of higher exploration capex of US$700m per year (US$200m earlier) from the operating cash flows, in line with management guidance.

  - EV/FCF multiple of 15x (12x earlier), justified by sustained exploration success in the last few months and in line with peer multiples (refer to Figure 7). Also, there has been further exploration success over the last 3-4 months in KG-D4 and shallow offshore KG-III-5, thus further broad-basing the E&P portfolio of discovered assets. This provides us further confidence.

  - The valuation of Rs1291 per share (US$47bn) translates to 56% premium to the NAV of Rs825 per share (refer to Figure 6). Our NAV also goes up from Rs661 earlier as we now incorporate 50% recovery of 3.7tcf in-place reserves in CBM blocks and assume 20% recovery (10% earlier) from the potential resources of 39tcf in KG-D6 (given continued discoveries in D6).

Figure 5. E&P – Valuation based on EV/FCF

	FY11E	
Operating cash flows (Rs m)	169,007	Assuming 80+9mmscmd gas and 45kbpd oil production
Operating cash flows (US$m)	4,225	
Less: Yearly exploration spend (US$m)	700	Based on management guidance in the analyst meeting
FCF (US$m)	3,525	
EV/FCF 12-mnth fwd (x)	15.0	
EV Mar-10E (US$ bn)	53	
EV Mar-10E (Rs bn)	2115	
Imputed Mar-10 PE (x)	13.5	
EV Dec-08E (Rs bn)	1878	
EV Dec-08E (US$m)	47	
Value per share (Rs)	**1291**	
Premium to NAV (%)	56%	

Source: Citi Investment Research estimates

Figure 6. Asset-wise NAVs

	Recovery assumed	2P+Best OGIP	Value	EV/boe	Value/share	Remarks
	tcf/mmboe	tcf/mmbo	US$m	US$	Rs	
KG-D6						
Dhirubhai-1&3 plus resources	18.3	23.2	14,331	4.8	395	Based on DCF assuming 70% recovery from 2P+Best OGIP of 23.2 tcf; including MA gas production
Potential undrilled prospects						
- Oil	560	800	5,600	10.0	139	@70% recovery of undrilled prospects in Pliocene & Cretaceous, EV/boe at 20% discount to Cairn
- Gas	7.8	39.0	6,791	4.8	168	Based on 20% recovery (10% earlier)
Sub-total			26,722		702	
Other Blocks						
KG III-6 (Prospects)	150	500	1,500	10.0	41	@ 30% recovery on 500mmbbl of prospective resource
NEC-25	1.9	3.7	1,499	4.5	41	@ 50% recovery of 2P OGIP of 3.7 tcf
CBM (3P OGIP)	1.9	3.7	1,499	4.5	41	@ 50% recovery of 3P OGIP of 3.7 tcf (10% earlier)
Total			**31,219**		**825**	

Source: Citi Investment Research estimates

Figure 7. Global E&P – Valuation Comps

Company Name	RIC Code	Rating	Mkt cap (US$m)	Share price 17-Jan-08	Target price	P/E (x) FY08E	P/E (x) FY09E	EV/EBITDA FY08E	EV/EBITDA FY09E	P/BV (x) FY08E	P/BV (x) FY09E	EV/FCF FY08E	EV/FCF FY09E
Majors													
BP	BP.L	2L	206,398	5.6	485	5.7	4.4	3.3	2.7	1.2	1.0	10.1	9.5
RD Shell Class A	RDSa.L	2L	138,752	19.8	1,632	4.7	5.1	1.2	1.1	1.0	0.9	7.9	6.6
RD Shell	RDSb.L	2L	104,820	19.4	1,632	4.6	5.0	1.0	0.9	1.0	0.9	6.3	5.1
Total	TOTF.PA	1L	190,154	54.2	3,679	9.6	9.3	4.8	4.6	2.8	2.5	20.4	21.8
ExxonMobil	XOM.N	1L	472,768	86.5	4,392	12.2	10.8	5.3	4.6	4.1	3.7	12.8	13.4
Chevron	CVX.N	1L	182,112	86.3	4,509	9.9	8.8	4.2	3.6	2.4	2.0	18.5	19.5
ConocoPhillips	COP.N	2M	123,310	77.1	3,803	8.4	7.3	4.6	3.7	1.4	1.3	10.7	13.5
European Integrateds													
BG	BG.L	3M	64,930	9.9	693	19.6	15.8	9.3	7.5	4.7	3.8	315.6	87.1
ENI	ENI.MI	1M	139,682	23.8	1,667	9.1	8.1	3.9	4.0	2.1	1.8	13.3	12.7
Repsol	REP.MC	2M	40,071	22.4	1,466	9.1	8.3	4.3	3.9	1.4	1.3	137.2	25.5
OMV	OMVV.VI	2H	21,430	48.7	3,161	8.8	8.6	5.4	5.1	1.7	1.5	nm	13.4
Norsk Hydro	NHY.OL	1M	12,465	54.1	688	6.7	7.4	4.4	3.7	1.1	1.3	6.7	25.0
StatoilHydro	STL.OL	2M	85,307	144.9	1,375	9.2	9.5	2.6	2.7	1.8	1.7	15.9	22.0
US Integrateds													
Hess	HES.N	2H	27,917	87.4	4,274	13.5	10.8	5.5	4.2	2.6	2.1	47.8	24.0
Marathon Oil	MRO.N	1M	35,834	50.5	3,215	9.2	7.9	4.2	4.0	2.0	1.7	16.0	26.1
Occidental	OXY.N	1M	58,060	70.1	3,607	12.5	9.9	5.4	4.6	2.5	2.2	13.7	13.2
Emerging Integrateds													
Lukoil	LKOH.RTS	2L	64,388	75.7	3,725	7	7.7	4.9	5.3	1.5	1.3	64.4	36.0
Gazprom	GAZP.RTS	1L	319,592	13.5	784	16.6	11.8	10.6	8.4	2.1	1.8	nm	50.8
Rosneft	ROSN.RTS	2L	90,932	8.6	372	15	15.5	9.2	9.5	3.3	2.8	17.2	65.9
PetroChina	0857.HK	2L	33,505	12.4	77	14	13.4	1.1	0.8	3.3	2.9	4.4	2.4
Sinopec	0386.HK	1L	20,082	9.3	72	13.3	12	2.6	2.5	2.6	2.2	nm	16.5
CNOOC	0883.HK	1L	69,102	12.2	82	16.9	13.9	10.1	8.7	4.1	3.4	51.2	28.2
CNPC (HK)	0135.HK	1H	2,672	4.3	34	8.7	7.3	9.5	8.7	1.4	1.3	38.0	20.0
CITIC Resources	1205.HK	3M	2,643	3.9	26	50.4	16.5	30.7	7.3	3.8	3.1	nm	9.0
ONGC	ONGC.BO	1L	68,246	1,251.1	1,400	12.1	10.7	5.9	5.0	3.4	2.9	12.0	11.0
PTT E&P	PTTE.BK	1L	17,291	156	241	17.2	12.7	7.4	5.5	4.6	3.6	nm	30.0
OGDC	OGDC.KA	2M	8,131	118.3	87	10.3	9.7	6.4	5.9	4.3	3.9	21.0	17.3
Woodside	WPL.AX	2M	29,554	48.9	1,701	54.4	55.1	13.3	9.9	14.8	12.9	nm	nm
Santos	STO.AX	1M	6,962	13.5	637	27.7	27	5.5	4.9	4.9	4.4	21.1	10.9
North American E&P													
Anadarko Petro	APC.N	1H	27,445	58.9	2,823	17.8	23.6	5.9	6.6	1.7	1.6	90.1	41.0
Apache	APA.N	2H	33,148	99.7	3,490	14.1	11.0	5.3	4.9	2.1	1.8	43.5	31.1
Canadian Nat'l	CNQ.TO	1H	36,029	68.4	3,369	14.9	18.3	7.0	8.4	2.8	2.5	354.8	60.3
Chesapeake	CHK.N	1H	18,238	38.5	1,764	12.8	10.8	5.4	4.8	1.0	1.0	nm	148.3
EOG	EOG.N	2H	21,797	88.6	3,529	22.7	18	8.9	7.3	3.0	2.6	nm	nm
Forest	FST.N	1H	4,072	46.2	2,431	17.4	16.9	7.1	5.8	1.5	1.5	176.2	nm
Nexen	NXY.TO	2H	15,373	29.8	1,148	12.5	12.9	5.4	5.3	2.8	2.3	nm	22.8
Noble	NBL.N	2H	13,075	76.3	2,588	16.3	15.9	6.7	6.8	2.6	2.3	109.4	40.4
Pioneer	PXD.N	2H	5,006	41.9	2,274	20	15.6	6.8	5.7	1.6	1.4	nm	97.5
Talisman	TLM.TO	2H	17,712	17.8	919	16.5	14.4	4.7	3.6	2.4	2.1	45.9	12.6
XTO	XTO.N	2H	25,933	53.6	2,078	15.4	16.1	7.4	6.2	2.0	1.7	22.3	15.6

Source: Citi Investment Research estimates. Powered by DataCentral

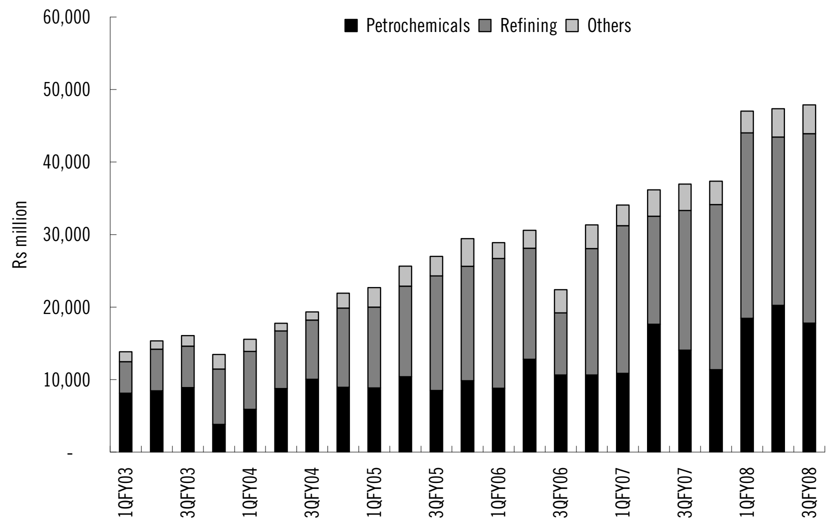
RIL 3QFY08 Results – Key Highlights

Figure 8. RIL 3QFY08 Results (Rupees in Millions)

Year to 31 Mar	3QFY07	2QFY08	3QFY08	% yoy	Comments
Net sales	**281,950**	**320,430**	**345,900**	**22.7%**	Absolute increase in prices
Expenditure:					
Inc/dec in stock	10,360	(9,200)	6,770	-34.7%	
Raw materials - external purchases	184,330	242,740	251,610	36.5%	
Staff cost	5,040	4,710	5,770	14.5%	
Other expenditure	30,420	24,370	23,420	-23.0%	
Total	(230,150)	(262,620)	(287,570)	24.9%	
EBITDA	**51,800**	**57,810**	**58,330**	**12.6%**	Sequentially flat as a strong refining quarter mitigated a relatively weak petchem performance
EBITDA margin	*18.4%*	*18.0%*	*16.9%*	*-151bps*	
Interest	(3,060)	(2,570)	(2,530)	-17.3%	
Depreciation	(12,740)	(11,290)	(12,130)	-4.8%	
Non-op income	1,200	1,680	2,410	100.8%	Net of exceptional income of Rs47.33bn on profit on sale of 4% stake in RPL
PBT	37,200	45,630	46,080	23.9%	
Tax	(4,370)	(5,270)	(5,268)		
PAT after current tax	32,830	40,360	40,812	24.3%	
Provision for deferred tax	(2,020)	(1,990)	(1,990)		
Tax rate (%)	*17.2%*	*15.9%*	*15.8%*	*-143bps*	
Net profit (reported)	**30,810**	**38,370**	**38,822**	**26.0%**	

Source: Company Reports and Citi Investment Research. Note: All numbers are post merger with IPCL.

Figure 9. RIL – Quarterly EBIT Break-up (Rupees in Millions)



Source: Company Reports and Citi Investment Research. Note: 1QFY08, 2QFY08 and 3QFY08 are merged with IPCL.

Figure 10. RIL 3QFY08 Segmental Profitability (Rupees in Millions)

Year to 31 Mar	3QFY07	2QFY08	3QFY08	%YoY	%QoQ	Comments
Revenues						
Petrochemicals	131,450	129,610	127,060	-3%	-2%	Lower qoq volumes on account of planned shutdown of PX unit
% of total	*37.9%*	*34.7%*	*31.9%*			
Refining	208,700	235,750	261,540	25%	11%	
% of total	*60.2%*	*63.1%*	*65.7%*			
Others	6,340	8,010	9,190	45%	15%	Driven by higher oil & gas prices
% of total	*1.8%*	*2.1%*	*2.3%*			
Intra - segment sales/transfers	48,960	39,350	38,990	-20%	-1%	
Excise Duties recovered	15,580	13,590	12,900	-17%	-5%	
Net sales	**281,950**	**320,430**	**345,900**	**23%**	**8%**	
PBIT						
Petrochemicals	17,880	20,250	17,780	-1%	-12%	Relatively lower margins across most segments of the petchem chain due to higher feedstock costs + volume decline
% of total	*43.9%*	*42.8%*	*37.1%*			
Margin	*13.6%*	*15.6%*	*14.0%*			
Refining	19,250	23,210	26,140	36%	13%	Sequentially strong GRMs partially offset by lower throughput
% of total	*47.2%*	*49.0%*	*54.6%*			
Margin	*9.2%*	*9.8%*	*10.0%*			
Others	3,640	3,900	3,960	9%	2%	
% of total	*8.9%*	*8.2%*	*8.3%*			
Margin	*57.4%*	*48.7%*	*43.1%*			
Total PBIT	**40,770**	**47,360**	**47,880**	**17%**	**1%**	

Source: Company Reports and Citi Investment Research. Note: All numbers are post merger with IPCL.

Figure 11. Refining – Key Parameters

	Units	Q2FY06	Q3FY06	Q4FY06	Q1FY07	Q2FY07	Q3FY07	Q4FY07	Q1FY08	Q2FY08	Q3FY08	Comments
Singapore complex spreads	US$/bbl	8.2	6	4.6	9	4.8	3.9	6.8	9.5	6.4	7.8	
RIL reported GRMs	US$/bbl	10.4	9.1	10.4	12.4	9.1	11.7	13.0	15.4	13.6	15.4	From company reports
Effective marketing discount	US$/bbl	-0.3	0.5	-0.3	-1.8	-0.5	-0.5	-	-0.6	-0.2	0.0	Profit of Rs80m due to trading gains on imports
RIL clean GRMs	US$/bbl	10.7	8.6	10.7	14.2	9.6	12.2	13.2	16.0	13.8	15.4	
Differential vis-à-vis clean GRMs	US$/bbl	2.5	2.6	6.1	5.2	4.9	8.3	6.2	6.5	7.4	7.6	Strong differentials maintained
Crude throughput	MMT	8	6.7	7.9	7.5	8.2	7.9	8.1	8.0	8.1	7.6	Lower on account of planned shutdown

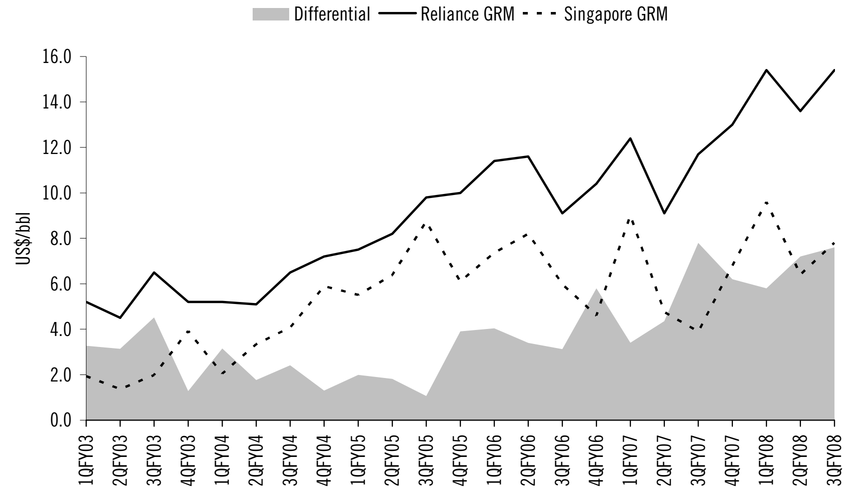
Source: Company Reports and Citi Investment Research

Figure 12. Refinery Product Sales (MMT)

	Q1FY06	Q2FY06	Q3FY06	Q4FY06	Q1FY07	Q2FY07	Q3FY07	Q4FY07	Q1FY08	Q2FY08	Q3FY08	%YoY	%QoQ	Comments
PSU	1.9	1.7	0.7	1.1	0.7	0.7	0.6	0.7	0.7	0.6	0.7	12.7%	4.6%	
Captive	1.6	1.7	1.2	1.8	1.7	1.7	1.7	1.8	1.6	1.4	1.2	-30.2%	-12.8%	
Retail	0.6	0.6	0.9	1.1	0.9	0.2	0.5	0.7	0.7	0.3	0.2	-68.6%	-41.4%	Retail sales continue to decline
Industrial sales/ Others	1.3	1.3	1.1	1.2	1.1	1.0	1.0	1.0	0.9	0.9	0.9	-5.1%	4.5%	
Exports	2.5	2.7	2.5	3.2	3.5	5.2	4.8	4.2	5.0	5.8	5.5	15.4%	-4.6%	
Total	**7.8**	**8.0**	**6.3**	**8.4**	**7.9**	**8.8**	**8.6**	**8.4**	**8.9**	**9.0**	**8.5**	**-1.0%**	**-5.3%**	qoq decline primarily due to lower throughput

Source: Company Reports and Citi Investment Research

Figure 13. Differential Between Reported GRMs and Singapore GRMs



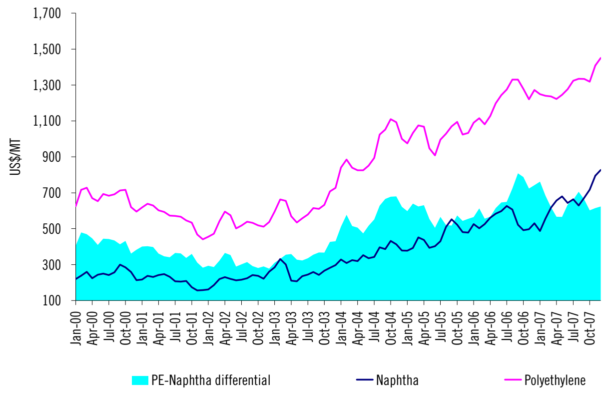
Source: Reuters, Company Reports, Citi Investment Research

Figure 14. RIL Operational Parameters – Petrochemicals and E&P Business

Year to 31 Mar	Units	Q2FY06	Q3FY06	Q4FY06	Q1FY07	Q2FY07*	Q3FY07*	Q4FY07	Q1FY08*	Q2FY08*	Q3FY08*	%YoY	%QoQ
Production													
Panna-Mukta													
- Crude	Tonnes	365,052	412,327	432,429	381,997	422,516	485,275	476,686	462,136	479,864	474,500	-2.2%	-1.1%
- Gas	mscm	299	331	483	347	360	476	479	482	532	486	2.1%	-8.6%
Tapti													
- Gas	mscm	605	573	579	522	420	629	657	576	672	1,052	67.2%	56.5%
Polyester (PFY, PSF, PET)	Tonnes	270,000	284,000	296,000	361,000	355,000	389,000	367,000	389,000	387,000	392,000	0.8%	1.3%
Fiber intermediates (PX, PTA, MEG)	Tonnes	813,000	712,000	900,000	886,000	1,112,000	1,076,000	1,123,000	1,152,000	1,214,000	1,114,000	3.5%	-8.2%
Polymers (PE, PP, PVC)	Tonnes	485,000	391,000	506,000	469,000	831,000	852,000	542,000	833,000	829,000	852,000	0%	2.8%
Industry demand													
Polyester (PFY, PSF, PET)	'000 Tonnes	465	463	491	512	454	509	565	543	616	581	14.2%	-5.7%
Polymers (PE, PP, PVC)	'000 Tonnes	1,130	899	1,085	977	1,030	1,081	1,280	1,114	1,214	1,254	16.0%	3.3%

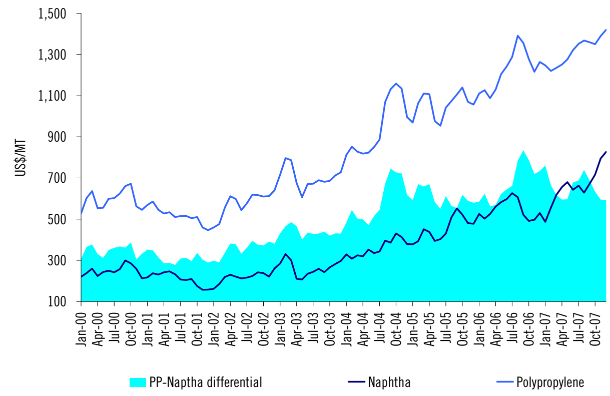
Source: Company Reports and Citi Investment Research. *Using post-IPCL merger figures for petrochemicals.

Figure 13. PE-Naphtha Differential (US$/MT)



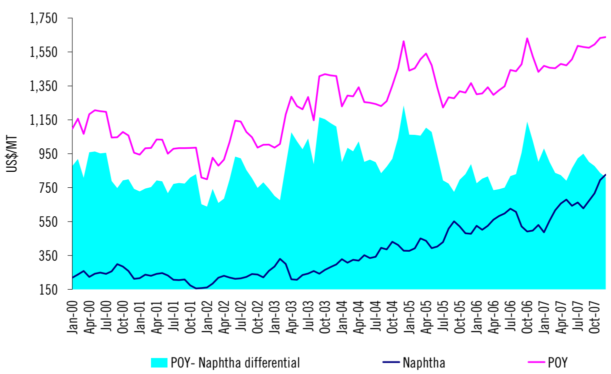
Source: DataStream

Figure 14. PP-Naphtha Differential (US$/MT)



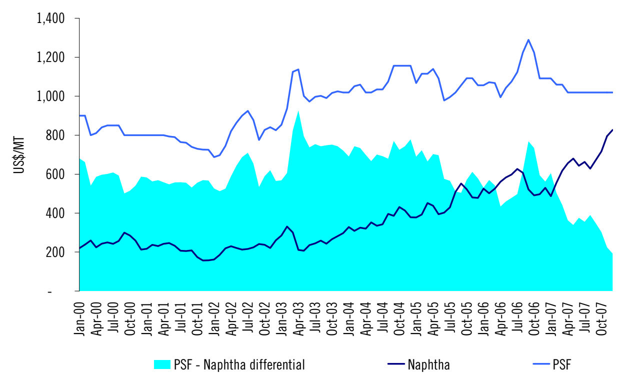
Source: DataStream

Figure 15. POY-Naphtha Differential (US$/MT)



Source: DataStream

Figure 16. PSF-Naphtha Differential (US$/MT)



Source: DataStream

Reliance Industries

Company description

Reliance Industries is a conglomerate with interests in upstream oil & gas (E&P), refining, and petrochemicals. It is building a super-size refinery project through its 75% subsidiary (RPL) and is now undertaking development of a large gas find in KG basin. RIL is foraying into organized retailing and has plans to undertake SEZ projects over the medium to long term.

Investment strategy

We rate RIL Buy/Low Risk with a target price of Rs3,460. We expect regional refining margins to remain robust due to project delays in the Middle East, with RIL enjoying an enhanced premium for its superior complexity. E&P business has delivered positive surprise and looks set to become more meaningful in the next 3-4 years as KG D6 field commences production and new discoveries are brought on stream. Upgrade of reserves in KG basin adds to the value, although the NAV of the gas find depends on development capex and the demand profile from anchor customers. Given the track record of exploratory success and the evolving portfolio (much beyond KG D6), RIL's E&P business needs to be valued as a going concern rather than a combination of assets. We have therefore valued E&P business (Rs1291/share) on more traditional EV/FCF multiple rather than the consensus NAV approach. Robust demand and delay in capacity additions is likely to push the downturn in petrochemicals cycle into FY10; this should be offset by diversity of products to some extent. Factors such as diversity of revenues, integration across product chains, and volume growth should help RIL tide over downturns in product cycles.

Valuation

Our target price of Rs3,460 is based on a sum-of-the-parts value:

1) RIL's core petrochem and downstream oil business is valued on an EV/EBITDA of 7.5x mid-FY10E (7.0x mid-FY09E earlier), at the higher end of the regional chemicals and refining peers. The increase in EV/EBITDA multiple is on account of the fact that we now capture the downturn in core businesses factored in FY10 (sharp decline in petrochemical and moderate decline in refining);

2) Total E&P assets including oil & gas prospects and other blocks are valued at Rs1291/share based on 15x steady state (FY11E) FCF. This is higher than EV/FCF multiple of 12x used earlier as we get more visibility on D6 upside, more discoveries (KG-D4, KG-III-5) in last 3-4 months even as we incorporate higher pure E&P capex (US$700m p.a.), as guided by management;

3) Investment in RPL valued at 9x profit contribution to consolidated profits;

4) Organized retail business value is rolled forward to Dec-08E and factored in at Rs137/share, as per Citi's retail analyst, Princy Singh; and

5) Treasury stock valued at RIL's target price.

Risks

We rate RIL Low Risk, as opposed to the Medium Risk suggested by our quantitative risk-rating system, which tracks 260-day historical share-price volatility. Diversified earnings and significant value contribution from the emerging E&P business and investment in listed subsidiaries have led to qualitative changes in the value constituents of the stock. Risks that could impede the stock from reaching our target price are: RIL's margins are exposed to the global petrochemical and refining cycles; the group could be asked to offer larger discounts on products sold to oil public sector units; delays in the key KG-D6 gas development and RPL refinery project; delays in the drilling programme for the new blocks (D9, D3, MN-D4); and the organized retail business would call for significant investment in non-core areas.

Appendix A-1

Analyst Certification

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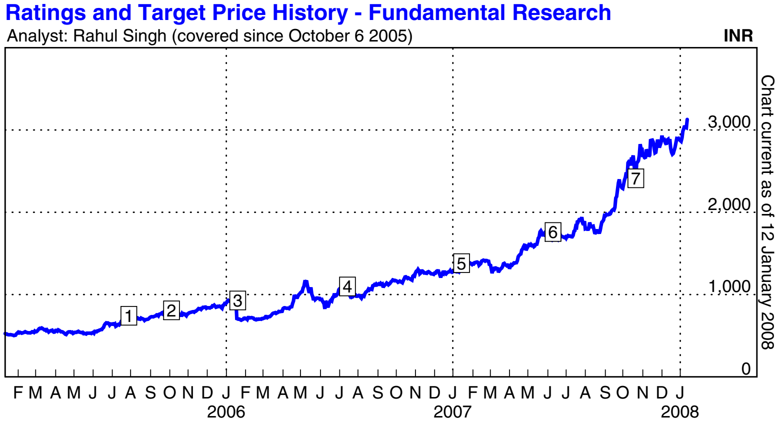
IMPORTANT DISCLOSURES

Reliance Industries (RELI.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Rahul Singh (covered since October 6 2005)



#	Date	Rating	Target Price	Closing Price
1:	28 Jul 05	1L	*598.65	NA
2:	5 Oct 05	1L	*697.31	801.95
3:	19 Jan 06	1L	*794.00	704.20
4:	14 Jul 06	*2L	*1,150.00	1,065.15
5:	15 Jan 07	2L	*1,450.00	1,364.65
6:	11 Jun 07	*1L	*2,005.00	1,668.20
7:	21 Oct 07	1L	*2,860.00	2,412.75

*Indicates change.

Covered
Not covered

Rating/target price changes above reflect Eastern Standard Time

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