EQUITY RESEARCH March 27, 2008

RESULTS REVIEW

Share Data

Market Cap	Rs. 148.68 bn
Price	Rs. 411.25
BSE Sensex	16,015.56
Reuters	BPCL.BO
Bloomberg	BPCL IN
Avg. Volume (52 Week)	0.13 mn
52-Week High/Low	Rs. 560/291.25
Shares Outstanding	361.54 mn

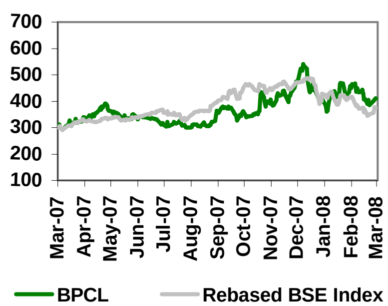
Valuation Ratios (Consolidated)

Year to 31 March	2008E	2009E
EPS (Rs.)	57.1	47.5
+/- (%)	(9.7%)	(16.8%)
PER (x)	7.2x	8.7x
EV/ Sales (x)	0.2x	0.2x
EV/ EBITDA (x)	6.0x	6.3x

Shareholding Pattern (%)

Promoters	64
FIIs	10
Institutions	20
Public & Others	6

Relative Performance



Bharat Petroleum Corporation Limited — Hold

Oil bonds brought respite to under recovery pressure

For the quarter ended Dec'07, Bharat Petroleum Corporation Limited (BPCL) reported the following set of numbers:

- Net sales increased 18.9% yoy to Rs. 289.7 bn led by oil bonds worth Rs. 20.8 bn issued by the Government of India (GoI) and higher sales volume (up 15.1% yoy to 7.47 MMT).
- EBITDA declined 34% yoy to Rs. 6.8 bn as a result of the higher cost of raw materials and purchases which more than offset the lower SG&A expenses and higher gross refining margins (GRMs) reported by the Company. Above all, huge under recoveries pressurised the margins.

In order to provide a respite to the oil marketing companies (OMCs) for the heavy under recoveries borne by them, the GoI hiked the prices of petrol and diesel by Rs. 2 and Rs. 1 per litre, respectively, in Feb'08. Further, talks are on to raise the proportion of oil bonds issued to the OMCs from the current scenario of 42.7% of the retail losses to 57%. If the new formula is approved, oil companies' burden will reduce to only 10%, while 57% would be borne by the government, and 33% by upstream companies. On the back of the above two measures undertaken by the GoI, the outlook of the Company seems to be improving. However, a rise in the global crude oil prices would always remain a downside risk.

At the current price of Rs. 411.25, the stock trades at a forward P/E of 7.2x for FY08E and 8.7x for FY09E. Based on our valuation and results analysis, we believe that the stock is fairly priced at the current levels and hence maintain Hold.

Key Figures (Consolidated)

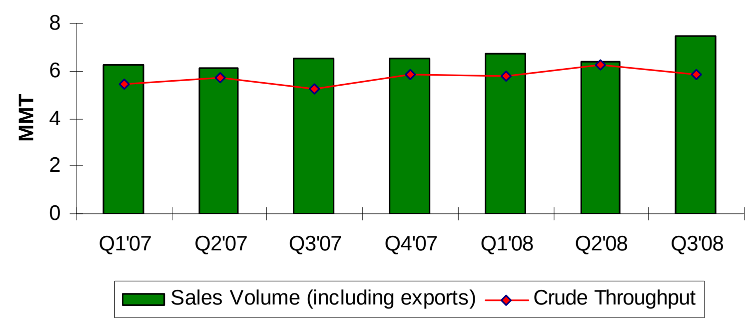
Quarterly Data	Q3'07	Q2'08	Q3'08	YoY%	QoQ%	9M'07	9M'08	YoY%
(Figures in Rs. mn, except per share data)								
Net Sales	243,533	254,246	289,678	18.9%	13.9%	739,823	784,799	6.1%
EBITDA	10,282	18,539	6,786	(34.0%)	(63.4%)	29,287	28,763	(1.8%)
Adj. Net Profit	4,686	10,462	2,620	(44.1%)	(75.0%)	13,995	15,730	12.4%
Margins(%)								
EBITDA	4.2%	7.3%	2.3%			4.0%	3.7%	
NPM	1.9%	4.1%	0.9%			1.9%	2.0%	
Per Share Data (Rs.)								
Normalised EPS	13.0	28.9	7.3	(44.0%)	(74.9%)	38.7	43.5	12.4%

Result Highlights

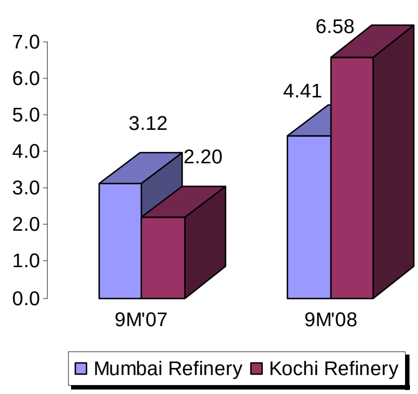
Oil bonds worth Rs. 20.8 bn provide a boost to the top line

For the quarter ended Dec'07, net sales increased 18.9% yoy to Rs. 289.7 bn led by higher sales volume of 7.47 MMT (including exports of 0.67 MMT). The quarter witnessed a 15.1% increase in sales volumes which was equally supported by a rise in crude thruput (up 11.2% yoy to 5.85 MMT). Oil bonds worth Rs. 20.8 bn, which were issued by the GOI to reimburse the OMCs for the under recoveries borne by them, also contributed to the increase in net sales.

Physical Performance



Gross Refining Margin ($/barrel)



Even though the Company witnessed an increase in net sales, EBITDA declined 34% yoy to Rs. 6.8 bn, and EBITDA margin went down 188 bps to 2.3%. The decrease in EBITDA was a result of the higher cost of raw materials and purchases, which more than offset the lower SG&A expenses and higher GRMs as reported by the Company. During the nine months ended Dec'07, BPCL's GRM witnessed an increase which was in-line with the global trends. In contrast to USD 3.12 per barrel in Apr-Dec'07, GRM during Apr-Dec'08 was USD 4.41 per barrel for the Mumbai refinery. Similarly, for the Kochi refinery, it stood at USD 6.58 per barrel as against USD 2.2 per barrel in Apr-Dec'07.

Adj. net profit also declined 44.1% yoy to Rs. 2.6 bn, and margin went down 102 bps to 0.9%. However, the fall in the net profit margin was lower than the decline in EBITDA margin which was supported by a lower effective tax rate.

Key Events

- Bharat Oman Refineries (BORL), a JV between BPCL and Oman Oil, is likely to come out with an initial public offer (IPO) next year. BORL is investing around Rs. 100 bn to set up a 6 mtpa refinery at Bina in Madhya Pradesh, which is likely to be commissioned by Dec'09. BPCL is looking for a strategic partner to offer a 26% stake, otherwise the Company might go for the IPO route for 48% equity.
- IT department sent a penalty notice to BPCL for Rs. 330 mn with respect to the non-payment of proper advance tax by the Company.
- BPCL is planning to foray into various sectors. The Company is in talks with Nippon Oil Corporation of Japan for a technology tie-up for developing polymer electrolyte fuel cell. In addition, BPCL is also planning to become an integrated manufacturer of biodiesel, and thereafter it may hive off the biodiesel business into a separate entity.

Key Risks

Key risks to our rating include:

- Change in the government's policy on the subsidy sharing mechanism
- Appreciation in rupee vis-à-vis dollar
- Unexpected increase in the global crude oil prices
- Competition from the entry of private players

Outlook

Despite a weak quarter, the outlook for the OMCs seems to be improving. After a long wait of more than a year, the government raised the price of petrol and diesel in Feb'08 by Rs. 2 and Rs. 1 per litre, respectively. Further, as per the recent discussions, the GoI is considering increasing the proportion of oil bonds in the package for OMCs to 57% in order to reduce the burden borne by them. Currently, the government reimburses only 42.7% of the retail losses of the OMCs in the form of oil bonds. The rest is shared by the companies (24%) and the upstream oil majors (33.3%) such as ONGC and OIL, which sell crude oil at reduced prices to the OMCs. If the new formula is approved, the oil companies' burden will reduce to only 10%, while 57% would be borne by the government, and 33% by upstream companies, thereby adding to the profitability. Hence, the outcome of the government's decision is likely to provide a trigger to the stock price in the short term.

GoI's decision on the issue of oil bonds holds a key trigger

However, we believe that the Company's margin will remain under pressure during FY09E as it is likely to shutdown its refineries in the beginning of the next fiscal for expansions (capacity expansion of 40,000 bpd at the Kochi refinery) and shutdowns. The shutdown is expected to result in 9.5% less crude processing during FY09E. As a result, the Company might have to resort to purchasing goods at a higher price from outside in order to meet the growing demand. Further, the possibility of the rise in crude prices will continue to be a downside risk.

Taking into account the recent price hikes announced by the GoI and increasing sales volume of the Company, we have upgraded our net sales estimates for FY08E and FY09E by 7.7% and 9.8%, respectively. However, to factor in the planned shutdowns, we have downsized our FY09E net profit by 13.2%. At the current price of Rs. 411.25, the stock trades at a forward P/E of 7.2x for FY08E and 8.7x for FY09E. Based on our valuation and results analysis, we believe that the stock is fairly priced at the current levels and hence maintain Hold.

Key Figures (Consolidated)

Year to March	FY05	FY06	FY07	FY08E	FY09E	CAGR (%)
(Figures in Rs. mn, except per share data)						(FY07-09E)
Net Sales	644,248	775,161	984,192	1,063,177	1,072,287	4.4%
EBITDA	37,759	17,041	45,196	42,361	40,492	(5.3%)
Adj. Net Profit	15,581	5,219	22,865	20,642	17,173	(13.3%)
Margins(%)						
EBITDA	5.9%	2.2%	4.6%	4.0%	3.8%	
NPM	2.4%	0.7%	2.3%	1.9%	1.6%	
Per Share Data (Rs.)						
Normalised EPS	51.9	14.4	63.2	57.1	47.5	(13.3%)
PER (x)	6.8x	29.5x	4.8x	7.2x	8.7x	

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