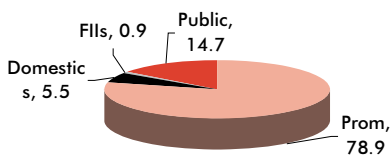
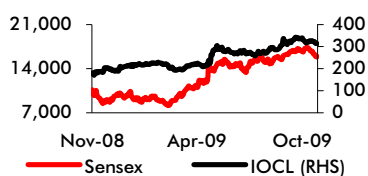


**HOLD**Price Rs305Target Price %Upside  
Rs340 11↑Market Capitalisation  
Rs762,620mn (US\$16,235mn)52 week range H/L (Rs) 395/165Shares o/s Daily vol  
(mn) (mn)  
2,427 1.55Reuters Bloomberg  
IOC.BO IOCL INPerfm(%) 1M 3M 12M YTD  
Absolute (6.8) 16.8 77.9 46.6  
Rel. to Sensex 0.5 15.1 9.5(11.1)BSE Sensex Nifty  
15,896 4,712

Source: Bloomberg

**Shareholding pattern (%)**

Source: Bloomberg

**Price performance**

Source: Bloomberg

Analyst  
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IOC, the lone OMC to post profit for the quarter, reported 2QFY10 PAT at Rs2.8bn. This was however lower than our expectation of Rs20bn, primarily on account of non-receipt of oil bonds. We had assumed a bond issue of Rs1.8bn in the quarter. Total revenue at Rs609bn, though recorded 3% improvement on a QoQ basis, was down 29% on a YoY basis. Cooking fuel under-recovery of Rs41bn in the quarter (Rs29bn in 1QFY10) resulted in a sharp fall in EBITDA from Rs50bn in 1QFY10 to Rs6.1bn in 2QFY10. Operating performance would have been worse, if not for an inventory increase of Rs43bn reported during the quarter. The upstream discounts received in lieu of purchase of crude oil/ LPG/ SKO were to the tune of Rs18bn for the quarter and Rs20.3bn for 1HFY10.

**TP unchanged; Maintain Hold**

We continue to believe that uncertainty on the subsidy share would continue to mar the sector and hence earnings are likely to remain very fluid. We maintain our Hold recommendation on the stock with a target price of Rs340 (March 2010). At the CMP of Rs310 the stock is trading at ~1.5x P/BV FY11E earnings.

**Under-recovery sharing mechanism still not coherent**

The ad hoc subsidy sharing mechanism has been the major overhang on the stock. As of 1HFY10, out of the total under-recovery of ~Rs92bn incurred by IOC, the company has received Rs20.3bn by way of upstream discounts, implying a pending oil bond issue of Rs71.7bn. We however, have mentioned in our earlier reports that in the past (*read: OMC - Castles in the air, dated 21 Oct 2009*), subsidy sharing has undergone considerable iterations before a final picture emerged at the end of the financial year. We still hold that view and that is a part of the reason we advise a cautious outlook on the stock. Given our outlook on crude prices we believe that OMCs will be sharing about 10% of the total under-recovery for FY10E, which according to our estimates would stand at Rs440bn.

**Refining environment still looking weak**

We believe that the rally in crude price has not factored in an expectation of recovery rather an exuberance about recovery. However we believe that it is a liquidity driven rally on the back of a buoyant equity market and weak dollar. The price rise is not closely correlated to demand and supply fundamentals. Given the firmness in crude prices coupled with benign product prices (due to low demand and high inventories), we expect GRMs to remain depressed. Hence we expect IOC's GRM to average US\$5.0-6.0/bbl for FY10E, from US\$5.4/bbl reported in 1HFY10.

**Exhibit 1: Key financials**

Rs, mn	FY07	FY08	FY09E	FY10E	FY11E
Total income	2,003,171	2,307,448	2,833,123	2,641,351	2,966,735
Gross profit	116,298	127,610	58,146	104,533	64,148
Net profit	78,675	79,128	25,994	49,035	25,652
Earning per share, Rs	33.0	33.2	10.9	20.2	10.6
Debt/ Equity	0.9	0.9	1.0	1.0	0.9
EBIDTA margin(%)	5.8	5.5	2.1	4.0	2.2
EV/EBIDTA	7.7	7.0	15.3	8.4	13.7
P/E (x)	18.8	18.7	56.9	15.1	28.9
RoE (%)	23.4	19.7	5.8	10.3	5.1
RoCE (%)	9.7	9.0	2.0	4.9	2.0

Source: Company, Ambit Capital research estimates

**Exhibit 2: Quarterly snapshot**

Rs, mn	2QFY10	2QFY09	YoY%	1QFY10	QoQ%
<b>Total Income</b>	<b>609,697</b>	<b>864,662</b>	<b>-29%</b>	<b>591,796</b>	<b>3%</b>
<b>Total expenditure</b>	<b>(603,557)</b>	<b>(923,553)</b>	<b>-35%</b>	<b>(541,806)</b>	<b>11%</b>
<b>EBITDA</b>	<b>6,140</b>	<b>(58,891)</b>	<b>NM</b>	<b>49,990</b>	<b>-88%</b>
% margin	1%	-7%		8%	-88%
Depreciation	(7,805)	(6,775)	15%	(7,598)	3%
Interest	(3,477)	(9,928)	-65%	(3,340)	4%
Other Income	8,481	5,212	63%	15,044	-44%
<b>PBT</b>	<b>3,339</b>	<b>(75,594)</b>	<b>NM</b>	<b>54,096</b>	<b>-94%</b>
<b>PAT</b>	<b>2,846</b>	<b>(75,684)</b>	<b>NM</b>	<b>36,829</b>	<b>-92%</b>
EPS	1.2	(31.2)	NM	15.2	-92%

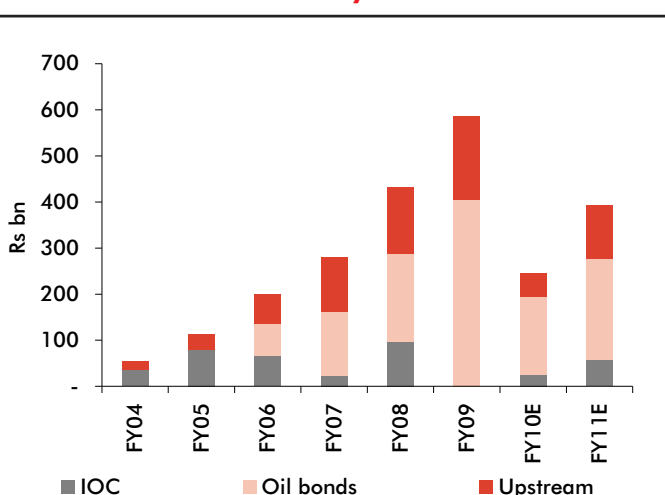
Source: Company, Ambit Capital research

**Exhibit 3: Operational performance**

mmt	2QFY10	2QFY09	YoY%	1QFY10	QoQ%
<b>Product sales</b>	<b>16.7</b>	<b>15.5</b>	<b>8%</b>	<b>17.7</b>	<b>-5%</b>
- Domestic	15.5	14.7	6%	16.6	-6%
- Export	1.2	0.8	44%	1.1	10%
Refinery Throughput	12.4	12.0	3%	12.5	0%
Pipeline throughput	15.5	14.3	9%	16.1	-4%

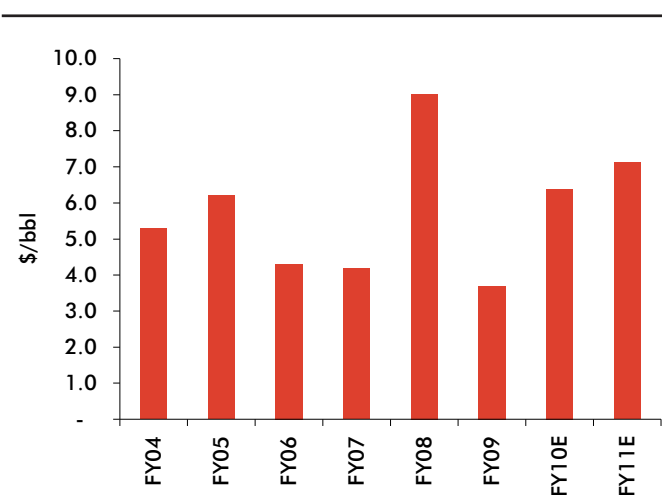
Source: Company

**Exhibit 4: IOC under-recovery trend**



Source: Company, Ambit Capital research

**Exhibit 5: IOC GRM trend**



Source: Company, Ambit Capital research

## Explanation of Investment Rating

<b>Investment Rating</b>	<b>Expected return (over 12-Month period from date of initial rating )</b>
Buy	>15%
Hold	5% to 15%
Sell	<5%

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