

Reliance Industries Ltd

Thoughts on the new 10-year bond

- As long expected by the market, Reliance Industries is issuing a new 10-year bond with an initial pricing guidance of T+365bp, z+367bp, 5.65%ytm area, as reported on Bloomberg. In our view, the initial pricing guidance offers small new issue concession given that it is ~30bps wider to the existing Reliance '20s (T+325bid, z+344) on z-spreads.
- While the new 10-year will be offering a higher carry if it prices around this pricing guidance, **we think it should not trade through Reliance '20s, even though we have seen cases where bonds on the same credit curve with having maturity difference trade almost flat in yields.**
- **We believe a switch even at flat yields, would make sense only when it releases some dollar capital as well, while Reliance '20s is currently 95bid on dollar price. Hence, we think investors could take some profit on the new bonds when the spreads between the two are within 5-10bps on z-spreads to each other.**
- That said, we think the Reliance curve is still trading slightly cheap relative to its global peers despite having a robust balance sheet and strong positive free cash flows position. We attribute this weakness to be in sympathy with the other Indian quasi-sovereigns, which have widened as a result of negative sentiment on the sovereign.
- We think the ~40-50bps in spreads and yields difference between Reliance '20s and PTTEPT '21s (z+289, 4.75%ytm) or Sinochem '20s (Baa1/BBB, z+295) looks slightly wide. EM investors could also consider Reliance '20s vs. other global oil & gas majors such as Pemex '22s (Baa1/BBB, z+226), Ecopetrol '19s (Baa2/BBB-, z+230) or Kazmunaigaz '21 (Baa3/BBB, z+361).
- We agree that an increase in sovereign issues such as twin deficits, inflation and fiscal health issues that may lead to negative ratings action on sovereign could also impact ratings of quasi-sovereign corporates such as Indian Oil and NTPC (they are standalone Ba1-rated).
- However, we believe Reliance Industries could still maintain its IG ratings despite negative ratings pressure on sovereign as was also the case when Indian sovereign ratings were HY by S&P till 2007 while Reliance has been an IG-rated credit from 2005 onwards. Moreover, further pressure on local currency should actually benefit the credit as most of its products are linked to the international prices.
- Reliance became a net cash company as of Dec-11 but subsequently announced a US\$2 bn share buyback program. Nevertheless, even after this bond issue, their net leverage would be ~0.4x. However, with US\$13 billion cash and a positive FCF profile, M&A remains key risk for the credit though we think the company will look to maintain its IG ratings.

Overweight

Moody's:	Baa2	Outlook:	Positive
S&P:	BBB	Outlook:	Positive
Fitch:	BBB-	Outlook:	Stable

Ticker
RILIN

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Table 1: Key financials for Reliance Industries

Reliance Industries											
<i>In INR bn (FYE March)</i>	FY08	FY09	FY10	FY11	4Q:09	2Q11	3Q11	4Q11	1Q12	2Q12	3Q12
Total Revenues	1,371	1,512	2,037	2,658	354	575	598	903	810	786	851
Petrochemicals	497	565	592	677	134	151	160	227	184	211	198
Refining	1,004	1,099	1,751	2,352	212	497	525	824	737	681	767
Oil and gas (KGD6)	27	36	126	173	8	43	42	42	39	36	28
EBIT	181	181	199	248	39	60	62	68	67	69	47
Petrochemicals	72	69	86	95	18	22	24	29	22	24	22
Refining	104	98	61	92	21	22	24	25	32	31	17
Oil and gas (KGD6)	15	21	52	67	4	17	15	16	15	15	13
EBITDA	239	238	309	390	58	94	95	107	99	98	73
Interest expense	(0)	(18)	(21)	(24)	(6)	(5)	(5)	(8)	(5)	(7)	(7)
Cash	45	227	139	301	222	294	318	424	458	615	745
Total Debt	507	762	646	841	739	682	702	674	670	714	745
Net Debt	462	535	507	540	517	388	384	250	213	99	0
EBITDA margins	17%	16%	15%	15%	16%	16%	16%	12%	12%	13%	9%
TD / EBITDA - LTM	2.1	3.2	2.1	2.2	3.1	1.9	1.8	1.7	1.7	1.8	2.0
ND / EBITDA - LTM	1.9	2.2	1.6	1.4	2.2	1.1	1.0	0.6	0.5	0.2	0.0
EBITDA / Interest expense	22016.9	13.1	15.0		9.7	17.3	17.4	13.7	18.2	14.9	10.5

Source: J.P. Morgan estimates, Company data.

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