HSBC
Global Research

Nat Resources & Energy
Oil & Gas
Equity – India

Neutral (V)

Target price (INR)	**200.00**
Share price (INR)	**195.35**
Potential total return (%)	**2.4**

Performance	1M	3M	12M
Absolute (%)	29.3	15.6	151.6
Relative^ (%)	16.1	21.8	109.8

Index^	BOMBAY SE SENSITIVE INDEX
RIC	RPET.BO
Bloomberg	RPET IN
Market cap (USDm)	21,946
Market cap (INRm)	879,075
Enterprise value (INRm)	898190
Free float (%)	

Note: (V) = volatile (please see disclosure appendix)

25 April 2008

Vishwas Katela*
Analyst
HSBC Securities and Capital markets (India) Private Limited
+9122 2268 1236
vishwaskatela@hsbc.co.in

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Reliance Petroleum (RPET)

Remain N (V): Good news priced in

- ***Reuters* reports a September 2008 commissioning of refinery, with trial runs starting in July**
- **News flow consistent with our forecast, but we believe already factored in the share price; retain target of INR200**
- **Key catalysts are refining margin movement, refinery start-up (capacity utilisation), cash reinvestment plan**

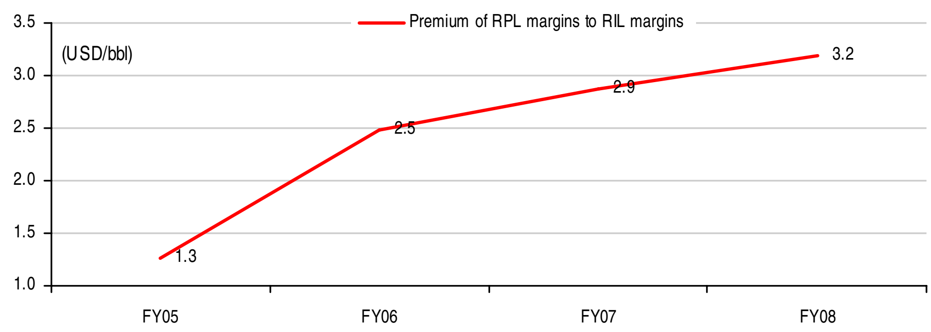
A *Reuters* report, quoting a Reliance Petroleum (RPL) source, supports our argument that RPL could be heading toward a start-up in July. As per the report, a company source stated, "Trial runs are planned to begin in July and should be over by end-August, so that the refinery can be commissioned … in September."

News positive, and consistent with our forecast, but priced in. We still believe there will be an early start-up, with 50% capacity utilization in FY09, although the commercial commissioning could be only in April 2009. However, we believe the stock price already factors in the positive news.

If it were operational now, RPL could have made refining margins of at least USD18.2/bbl in FY08, given Reliance Industries' margin of USD15/bbl (Figure 1). The premium could be higher, if we take into account RPL's product would be of more stringent specifications than Indian peers', and that the crude processed would be of heavier grade (implying lower feedstock cost).

Remain N (V) on valuation, retain DCF-based target of INR200. We find valuation could move by INR22/share for a USD1/bbl change in our long-term refining margins assumption. We believe RPL remains the best refining play in India, given its high complexity and that auto fuels, with stringent specifications, will remain in high demand. Catalysts: refining margin movement, refinery start-up (capacity utilisation), cash reinvestment plan.

Figure 1: RPL premium to RIL's refining margins would have consistently gone up (if RPL was operational)



Source: Petroleum Argus, HSBC estimates

Valuation: retain INR200 target and Neutral (V) rating

DCF-based

Our DCF-based target price for RPL is INR200/share. Our DCF is based on a weighted average cost of capital of 10.6%. We have used 10 years' explicit forecast period and a terminal growth rate of 5%. We retain our Neutral (V) rating. We continue to assume 50% capacity utilisation of RPL refinery in FY09e.

The valuation would be INR189 if the new refinery were to start operations in December 2008, implying a capacity utilisation of 10% in FY09e. Our sensitivity analysis shows that the DCF-based valuation for RPL's refinery would be INR186 even if it starts production in FY10e. Our target price is sensitive to our long-term refining margin assumption. A USD1/bbl decrease in long-term refining margin could lower valuation by INR22 to INR178/share.

Composite PE-PB approach

A composite PE-PB approach, where we apply a PE of 11x and a PB of 2.5x to FY10e earnings, gives a valuation of INR165/share for RPL after discounting to end-FY08e value.

Figure 2: Reliance Petroleum valuation based on composite PE-PB approach

INR/share			
FY10e EPS	21.7	FY10e BV	51.1
PE (x) for FY10e EPS	11	P/BV (x) for FY10e BV	2.5
PE (x) for FY09e	9.9	P/BV (x) for FY09e	2.3
Valuation range (INR/share)	215		115
Valuation (INR/share)			**165**

Source: HSBC estimates

Earnings summary

Figure 3 summarises our earnings estimates for RPL and the sensitivity of earnings to each USD1/bbl change in refining margins estimates during FY09-10e.

Figure 3: EPS estimates and sensitivity to refining margins for RPL

(INR/share)	FY09e	FY10e
Refining margins down by USD1/bbl	11.5	19.8
Base case	12.5	21.7
	-7%	**-9%**

Source: HSBC estimates

Risks to valuations

- Volatility of global commodities price could add both upside and downside risk to earnings in the form of feedstock cost fluctuation
- Refining margins being higher or lower than our expectations
- Refinery and petrochemical capacity ramp-up being slower or faster than our expectations
- Commencement of refinery operations being later or earlier than our expectations.

Disclosure appendix

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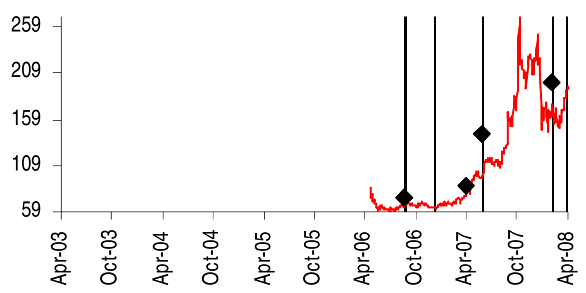
Underweight (Sell)	15%	(14% of these provided with Investment Banking Services)

Share price and rating changes for long-term investment opportunities

Reliance Petroleum Ltd (RPET.BO) Share Price performance INR Vs HSBC rating history



Source: HSBC

Recommendation & price target history

From	To	Date
N/A	Overweight	12 September 2006
Overweight	Neutral (V)	27 December 2006
Neutral (V)	Overweight	22 June 2007
Overweight	Overweight (V)	27 February 2008
Overweight (V)	Neutral (V)	21 April 2008
Target Price	**Value**	**Date**
Price 1	74.00	12 September 2006
Price 2	87.00	26 April 2007
Price 3	144.00	22 June 2007
Price 4	200.00	27 February 2008

Source: HSBC

HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price Date	Disclosure
RELIANCE PETROLEUM LTD	RPET.BO	195.35	23-Apr-2008	1, 5

Source: HSBC

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Issuer of report
HSBC Securities and Capital Markets (India) Private Limited
Registered Office
52/60 Mahatma Gandhi Road
Fort, Mumbai 400 001, India
Telephone: +91 22 2267 4921
Fax: +91 22 2263 1983
Website: www.research.hsbc.com

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