

BSE SENSEX 17,705	S&P CNX 5,327	CMP: INR623	Buy									
Bloomberg Equity Shares (m)	BPCL IN 361.5	YEAR	NET SALES	ADJ. PAT	ADJ. EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/
52-Week Range (INR)	785/530	END	(INR B)	(INR B)	(INR)	GR. (₹)	(X)	(X)	(%)	(%)	SALES	EBITDA
1,6,12 Rel. Perf. (%)	-11/7/-3	03/10A	1,238	16.3	45.2	157.6	13.8	1.7	11.9	3.9	0.4	16.6
M.Cap. (INR b)	225.1	03/11A	1,536	16.3	45.2	0.2	13.8	1.5	11.1	5.5	0.3	11.5
M.Cap. (USD b)	4.6	03/12E	1,963	16.9	46.8	3.6	13.3	1.4	10.6	7.0	0.2	8.8
		03/13E	1,795	19.1	52.8	12.8	11.8	1.3	11.1	7.6	0.2	8.0

Consolidated

Bharat Petroleum Corporation (BPCL) reported 2QFY12 EBITDA loss of INR27.1b (against our estimate of EBITDA of INR13.9b) mainly due to (1) nil government compensation v/s our estimate of INR33b, (2) lower-than-expected GRM of USD1.7/bbl (against our estimate of USD6.8/bbl) led by the impact of a duty cut in June 2011 on crude inventory (higher inventory in Kochi due to a shutdown) and (3) forex loss of INR8b. 2QFY12 net loss was INR32.3b against net profit of INR21.4b in 2QFY11 and loss of INR25.6b in 1QFY12.

Net under-recovery sharing of 67% in 2QFY12, 44% in 1HFY12; We model 4% for FY12

- Of the gross under-recovery of INR50b in 2QFY12, BPCL received INR16b upstream discount on crude purchases and the government did not compensate it during the quarter. The net subsidy burden was INR33b in 2QFY12.
- For FY12 and FY13 we model upstream share at 38.7%. We model government shares at 56% and 48% and OMC shares at 4% and 13% in FY12 and FY13 respectively, enabling OMCs to post RoE of at least 10%.

June 2011 duty cuts impact GRM

- 2QFY12 GRM was USD1.7/bbl (against our estimate of USD6.8/bbl) v/s USD2.8/bbl in 2QFY11 and USD3/bbl in 1QFY12. The lower-than-expected GRM was led by the government's duty cuts in June 2011, which impacted BPCL's crude inventory. The Kochi refinery had a higher crude inventory due to a shutdown in June 2011. We estimate the impact of the duty cut to be ~USD1.2/bbl on the reported GRM in 2QFY12.

Valuation and view

- Just as in earlier years, subsidy sharing is expected to be finalized towards the end of the year. In view of the likely ONGC FPO, we expect the government to spell out a sustainable subsidy sharing over the coming period.
- To account for lower GRM performance in 2QFY12, we cut our FY12 EPS by 13% to INR46.8. The stock trades at 13.3x FY12E EPS of INR46.8 and 1.4x FY12E BV. The key event to watch (besides subsidy sharing) is the start of commercial production at the Bina refinery at full utilization levels and GRM performance. Maintain **Buy** mainly due to promising E&P potential.

Quarterly Performance (Standalone)

Y/E March	(INR Million)								FY11	FY12E
	FY11				FY12					
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE		
Net Sales	342,415	353,168	366,655	452,515	461,177	422,819	477,205	537,607	1,514,753	1,898,807
Change (%)	34.3	30.5	14.0	20.5	34.7	19.7	30.2	18.8	23.9	25.4
EBITDA	-14,265	24,679	7,284	16,441	-21,861	-27,148	12,904	77,263	34,138	41,159
Change (%)	nm	nm	17.0	45.8	53.3	nm	77.2	369.9	43.5	20.6
% of Sales	-4.2	7.0	2.0	3.6	-4.7	-6.4	2.7	14.4	2.3	2.2
Depreciation	4,007	4,019	3,700	4,828	4,901	4,600	4,485	4,398	16,554	18,384
Interest	2,324	2,780	2,747	3,157	3,349	4,532	4,476	4,083	11,008	16,439
Other Income	3,415	5,522	3,308	5,305	4,492	3,987	3,342	2,943	17,550	14,765
PBT	-17,181	23,402	4,144	13,761	-25,619	-32,293	7,285	71,726	24,126	21,100
Tax	0	1,980	2,270	4,410	0	0	1,210	5,799	8,660	7,009
Rate (%)	0.0	8.5	54.8	32.0	0.0	0.0	16.6	8.1	35.9	33.2
PAT	-17,181	21,422	1,874	9,352	-25,619	-32,293	6,075	65,927	15,467	14,091
Change (%)	nm	nm	-50.6	32.9	49.1	nm	224.2	605.0	0.6	-8.9
Adj. PAT	-17,181	21,422	1,874	9,352	-25,619	-32,293	6,075	65,927	15,467	14,091

E: MOSL Estimates; 3QFY11 tax includes prior period provision (from FY03) of INR1b

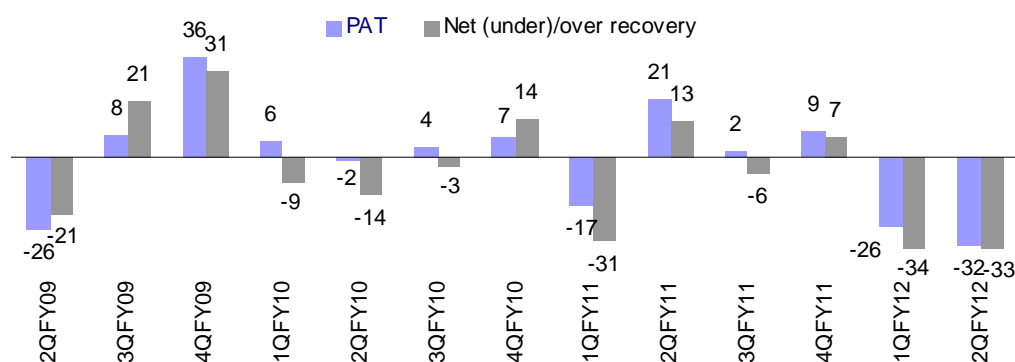
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Bharat Petroleum Corporation (BPCL) reported 2QFY12 EBITDA loss of INR27.1b (against our estimate of EBITDA of INR13.9b) mainly due to (1) nil government compensation v/s our estimate of INR33b, (2) lower-than-expected GRM of USD1.7/bbl (against our estimate of USD6.8/bbl) led by the impact of a duty cut in June 2011 on crude inventory (higher inventory in Kochi due to a shutdown) and (3) forex loss of INR8b. 2QFY12 net loss was INR32.3b against net profit of INR21.4b in 2QFY11 and loss of INR25.6b in 1QFY12.

Other key highlights

- The large GRM under-performance v/s the regional benchmark Reuters Singapore GRM in recent quarters was due to the difference in the product slate - BPCL is a diesel heavy refiner and cracks of diesel were down sequentially in 2QFY12.
- Product inventory adventitious loss in the quarter was INR240m v/s gain of INR12b in 1QFY12. A large 1QFY12 product inventory gain was led by the government raising prices towards the end of June.
- Refinery throughput was 5.4mmt, flat YoY and up 7.3% QoQ. Marketing volumes were down 10% sequentially led by seasonal factors and stood at 7mmt.
- Gross debt was INR247b as on September 2011 v/s INR190b on 31 March 2011.

Ad hoc subsidy sharing results in volatile quarterly profits (INR b)



Source: Company/MOSL

BPCL: 2QFY12 operational highlights (INR b)

	FY11				FY12		2QFY12 (%)	
	1Q	2Q	3Q	4Q	1Q	2Q	YoY	QoQ
Product Sales (mmt)	7.3	6.6	7.4	7.8	7.8	7.0	6.7	(10.1)
Throughput (mmt)								
Mumbai	3.3	3.4	2.9	3.4	3.3	3.1	(9.0)	(5.8)
Kochi	2.3	2.2	2.1	2.1	1.9	2.5	12.1	29.5
Total	5.6	5.6	5.0	5.6	5.2	5.6	(0.4)	7.3
Blended GRM (USD/bbl)	3.6	2.8	4.6	6.9	3.0	1.7	(41.3)	(45.4)

Source: Company/MOSL

BPCL's subsidy sharing: Net sharing at 44% in 1HFY12, we model 4% in FY12 (INR b)

	FY11				FY12		2QFY12 (%)		FY11	1H FY12
	1Q	2Q	3Q	4Q	1Q	2Q	YoY	QoQ		
Gross Under recovery	46.3	24.6	35.3	73.4	102.9	49.8	101.9	(51.6)	179.6	152.6
Less: Sharing										
Upstream Sharing	15.5	8.2	11.7	34.2	34.1	16.4	99.9	(51.8)	69.6	50.5
Oil Bonds/Cash	0.0	29.5	18.1	46.6	35.2	0.0	(100)	(100)	94.2	35.2
Net Under/(over)recov.	30.8	(13.1)	5.5	(7.4)	33.6	33.3	(355.4)	(0.7)	15.8	66.9
As a % of Gross	66.5	n m	15.6	n m	32.6	67.0			8.8	43.8

Source: Company/MOSL

We model OMC sharing at 4% in FY12, 13% in FY13

	FY08	FY09	FY10	FY11	FY12E	FY13E
Fx Rate (INR/USD)	40.3	46.0	47.5	45.6	47.0	46.0
Brent (USD/bbl)	82.3	84.8	69.6	86.3	110.0	95.0
Gross Under recoveries (INR b)						
Auto Fuels	426	575	144	375	696	256
Domestic Fuels	347	458	316	405	536	420
Total	773	1,033	461	780	1,232	676
Sharing (INR b)						
Oil Bonds/Cash	353	713	260	410	690	326
Upstream	257	329	145	303	493	262
OMC's sharing	163	-9	56	67	49	88
Total	773	1,033	461	780	1,232	676
Sharing (%)						
Government	46	69	56	53	56	48
Upstream	33	32	31	39	40	39
OMC's sharing	21	-1	12	9	4	13
Total	100	100	100	100	100	100

Source: Company/MOSL

Valuation and view

- Given the ad-hoc subsidy sharing we believe quarterly financials are not indicative of the likely full year performance. We now model OMC subsidy sharing at 4% in FY12 (v/s 8.8% in FY11) so that OMCs report ROE of at least 10%.
- We model Brent oil price of USD110/95/90/85/bbl in FY12/FY13/FY14/long-term respectively, in our estimates.
- Just as in earlier years, the government subsidy sharing is expected to be finalized towards the end of the year. Led by a delay in government compensation, we continue to model higher debt (leading to higher interest costs) over the next two quarters and expect most of the government compensation to come in 4QFY12. In view of a likely ONGC FPO, we expect the government to spell out a likely sustainable subsidy sharing formula over the coming period.
- E&P upside potential is BPCL's key differentiator vis-à-vis HPCL and IOC. BPCL's overseas E&P portfolio (Mozambique and Brazil assets) is likely to add substantial value as it completes its appraisal program and gives out the resource/reserve numbers. We await details on the timeframe of revenue contribution and reserve estimates.
- To account for lower GRM performance in 2QFY12, we cut our FY12 EPS by 13% to INR46.8. The stock trades at 13.3x FY12E EPS of INR46.8 and 1.4x FY12E BV. A key event to watch (apart from subsidy sharing) is the start of commercial production at the Bina refinery at full utilization levels and GRM performance. Maintain **Buy** mainly due to promising E&P potential.

BPCL: an investment profile

Company description

A Fortune 500 company, Bharat Petroleum Corporation (BPCL) has interests in oil refining and marketing of petroleum products. It is the third largest refining company in India with capacity of 12mmtpa at its Mumbai facility and 7.5mmtpa at Kochi. BPCL has majority stake (63%) in Numaligarh Refineries, a 3mmtpa refinery in the north-east. BPCL has investments in IGL (22.5%) and Petronet LNG (12.5%). BPCL is a public sector firm in which the government of India holds 54.93%.

Key investment arguments

- BPCL's profitability continues to be determined by the quantum of under-recoveries and sharing mechanism, rather than fundamentals.
- The Bina refinery's commercial production ramp-up is expected over the coming quarters. BPCL has 49% stake in the ~INR114b Bina refinery, which will have capacity of 6mmtpa.
- BPCL's E&P portfolio is likely to add substantial value as it completes its appraisal program and gives out the resource/reserve numbers.

Key investment risks

- Delay in the diesel de-regulation and ad-hoc subsidy sharing.
- Non-commensurate increase in the retail fuel prices as oil price rises, leads to under recoveries for BPCL and ad-hoc nature of subsidy sharing impacts the profits.

Recent developments

- The government initiated the process of decontrol of retail fuel prices, starting with petrol prices. The FPO of IOCL and ONGC could be key triggers to start the decontrol process for LPG, kerosene and diesel.

Valuation and view

- The stock trades at 13.9x FY12E EPS of INR46.8 and 1.4x FY12E BV. Maintain **Buy**.

Sector view

- We expect refining margins to remain range-bound amid a mixed trend in the global economy and supply-side situation. However, the ceiling will be capped in the near term due to new capacities coming on line in FY12 and FY13. We expect the demand-supply gap to correct only through refinery closure of simple refiners and continuous pick-up in global demand.

Target Price and Recommendation

Current Price (INR)	Target Price (INR)	Upside (%)	Reco.
623	-	-	Buy

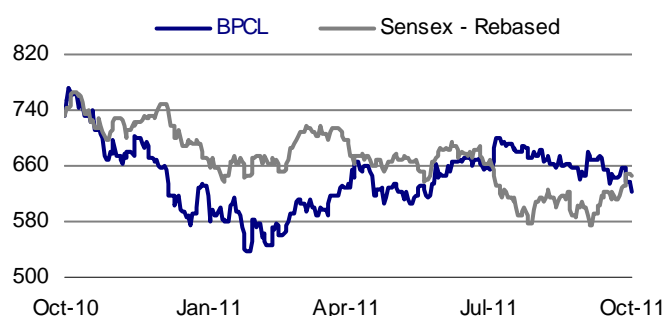
EPS: MOSL forecast v/s consensus (INR)

	MOSL Forecast	Consensus Forecast	Variation (%)
FY12	46.8	49.0	-4.4
FY13	52.8	59.3	-10.8

Shareholding pattern (%)

	Sep-11	Jun-11	Sep-10
Promoter	55.8	55.8	55.8
Domestic Inst	19.5	20.2	18.6
Foreign	7.5	6.8	8.3
Others	17.3	17.2	17.4

Stock performance (1 year)



Financials and Valuation

Income Statement (Consolidated)		(INR Million)			
Y/E March	2010	2011	2012E	2013E	
Net Sales	1,238,167	1,536,450	1,962,740	1,795,103	
Change (%)	-9.3	24.1	27.7	-8.5	
Finished Gds Purchase	567,667	701,497	935,023	781,865	
RM & Other exp	533,501	692,475	896,502	900,763	
Other operating expenses	106,461	99,865	78,417	57,455	
EBITDA	30,539	42,612	52,798	55,021	
% of Net Sales	2.5	2.8	2.7	3.1	
Depreciation	14,446	18,914	23,609	23,771	
Interest	11,247	12,468	17,050	13,952	
Other Income	23,652	17,252	14,177	11,024	
Extraordinary Items (net)	-777	0	0	0	
PBT	27,721	28,483	26,315	28,321	
Tax	10,235	11,062	8,490	8,323	
Rate (%)	36.9	38.8	32.3	29.4	
Minority Interest	876	1,071	893	893	
Exceptional Item					
PAT	16,610	16,350	16,932	19,105	
Adj. PAT	16,324	16,350	16,932	19,105	
Change (%)	157.6	0.2	3.6	12.8	

Ratios		(INR Million)			
Y/E March	2010	2011	2012E	2013E	
Basic (IIR)					
EPS	45.2	45.2	46.8	52.8	
Cash EPS	85.1	97.5	112.1	118.6	
Book Value	391.2	424.6	457.4	497.4	
Dividend	14.0	14.0	12.0	11.0	
Payout (incl. Div. Tax.)	21.5	39.4	30.0	24.4	
Valuation (x)					
P/E	14.4	14.4	13.9	12.3	
Cash P/E	7.6	6.7	5.8	5.5	
EV / EBITDA	16.6	11.5	8.8	8.0	
EV / Sales	0.4	0.3	0.2	0.2	
Price / Book Value	1.7	1.5	1.4	1.3	
Dividend Yield (%)	2.2	2.2	1.8	1.7	
Profitability Ratios (%)					
RoE	11.9	11.1	10.6	11.1	
RoCE	3.9	5.5	7.0	7.6	
Turnover Ratios					
Debtors (No. of Days)	6	7	5	5	
Asset Turnover (x)	4.4	4.8	5.5	4.7	
Leverage Ratio					
Debt / Equity (x)	1.9	1.6	1.3	1.2	

Balance Sheet		(INR Million)			
Y/E March	2010	2011	2012E	2013E	
Share Capital	3,615	3,615	3,615	3,615	
Reserves	137,814	149,893	161,749	176,202	
Net Worth	141,429	153,508	165,365	179,817	
Minority interest	9,396	9,975	10,868	11,761	
Loans	266,921	251,855	217,347	207,524	
Deferred Tax	11,477	13,074	13,404	13,706	
Capital Employed	429,223	428,412	406,984	412,808	
Gross Fixed Assets	302,023	344,851	363,912	393,699	
Less: Depreciation	134,524	152,581	176,190	199,961	
Net Fixed Assets	167,499	192,269	187,721	193,738	
Capital W/P	78,217	82,864	82,864	82,864	
Investments	119,323	84,600	116,199	121,199	
Intangibles	3,855	3,855	3,855	3,855	
Curr. Assets, L & Adv.					
Inventory	141,092	182,135	153,873	138,465	
Debtors	26,009	28,779	28,230	25,393	
Cash & Bank Balance	7,284	7,971	3,012	15,516	
Loans & Advances	74,480	86,421	86,421	86,421	
Current Liab. & Prov.					
Liabilities	160,917	206,051	221,089	218,501	
Provisions	27,652	34,462	34,135	36,174	
Net Current Assets	60,297	64,792	16,313	11,120	
Less: Miscellaneous exp.	33	33	33	33	
Application of Funds	429,223	428,412	406,984	412,809	

E: MOSL Estimates

Cash Flow Statement		(INR Million)			
Y/E March	2010	2011	2012E	2013E	
OP/(Loss) before Tax	28,499	28,632	26,315	28,321	
Depreciation	14,446	18,914	23,609	23,771	
Interest Paid	11,247	12,468	17,050	13,952	
Direct Taxes Paid	-10,469	-12,475	-8,160	-8,021	
Other operating items	-3,658	-13,028	0	0	
(Inc)/Dec in W/kg. Capital	-42,307	13,489	43,521	17,696	
CF from Op. Activity	-2,242	48,001	102,335	75,720	
(Inc)/Dec in FA & C/WP	-51,819	-43,057	-19,061	-29,788	
(Pur)/Sale of Investments	44,018	38,532	-31,599	-5,000	
CF from Inv. Activity	-7,801	-4,525	-50,660	-34,788	
Issue of Shares	2,350	0	0	0	
Net Inc / (Dec) in Debt	28,080	4,137	-34,507	-9,823	
Interest paid	-13,722	-13,967	-17,050	-13,952	
Dividends Paid	-3,506	-6,449	-5,076	-4,653	
Other Fi. Activities	-1,605	3,278	0	0	
CF from Fin. Activity	11,596	-13,001	-56,633	-28,428	
Inc / (Dec) in Cash	1,552	30,475	-4,959	12,504	
Cash (incl ST borrowings)	5,732	-22,504	7,971	3,012	
Closing Balance	7,284	7,971	3,012	15,516	

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BPCL

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| 2. Group/Directors ownership of the stock | No |
| 3. Broking relationship with company covered | No |
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