

7 March 2011

Produced by: The Royal Bank of Scotland N.V., (India) Office

Hold

Target price
Rs370.00

Price
Rs329.45

Equity | India | Energy

Flashnote

Hindustan Petroleum

Comments from RBS India Access

HPCL mgt presented at RBS's India Access conference. Key takeaways are: 1) LT strategy to increase both mrkt & refining capacity to 42mmt by FY17; 2) Bhatinda refinery to start comm. prod by Sep 2011, IPO likely by Nov 2011; 3) FY11 net under recoveries could be close to 12%; 4) Diesel decontrol unlikely in near term

Long term plan to raise marketing & refining capacity to 42mmt by FY17

- The company outlined its long term strategy to take both marketing & refining volumes to 42mmt by FY17 at total capex of Rs450bn. Currently, HPCL's refining volumes are lower than its market sales and the shortfall is sourced from standalone refiners like MRPL etc. Management expects to plug this gap by expanding its refining capacity through- Bhatinda refinery (rated capacity-9mmt), new Greenfield refinery in Maharashtra (rated capacity-9mmt) and Brownfield expansion of the Visakh refinery by 9mmt. The existing Mumbai refinery is likely to be converted into a speciality refinery producing speciality chemicals like solvents etc.
- It also plans to expand its retail outlet footprint by 30% during the next five years. Rural areas would be the focus of retail expansion due to better economics like low payback (1.5 yrs) etc

Bhatinda refinery-IPO likely in November 2011

- The management stated that the Bhatinda refinery (Joint venture project known as Hindustan Mittal Energy Ltd or HMEL) would achieve mechanical completion by May 2011, start commercial production by September 2011 and achieve 100% capacity utilisation by June 2012. The refinery has rated capacity of 9mmt but can be operated at 10.5mmt. Management plans to come out with an IPO of HMEL by November 2011, if markets remain stable.
- Management believes that the Bhatinda refinery GRMs would be at a premium of US\$6/bbl over the benchmark Singapore complex GRMs.

Retail product pricing & under recovery burden sharing

- The company expects current subsidy sharing mechanism to continue. For FY11, GOI would take a decision on the final share of under-recoveries only at the end of the year. It expects total FY11 compensation of 88% (upstream- 33% & GOI-55%), thus OMCs would have to

(Continued on page 2)

Key forecasts

	FY09A	FY10A	FY11F	FY12F	FY13F
Revenue (Rsm)	1247524	1076375	1274926	1471203	1648999
EBITDA (Rsm)	33536	25470	33203	45376	56966
Reported net profit (Rsm)	5749	13014	13703	11914	17988
Normalised net profit (Rsm)	5749	13014	13703	11914	17988
Normalised EPS (Rs)	17.0	38.4	40.5	35.2	53.1
Dividend per share (Rs)	5.25	12.0	13.0	14.0	15.0
Dividend yield (%)	1.59	3.64	3.95	4.25	4.55
Normalised PE (x)	19.4	8.57	8.14	9.36	6.20
EV/EBITDA (x)	6.31	10.2	9.74	7.53	5.78
Price/book value (x)	1.03	0.94	0.90	0.85	0.78
ROIC (%)	6.88	4.07	4.54	4.47	5.77

Post-goodwill amortisation and pre-exceptional items
Accounting standard: Local GAAP
Source: Company data, RBS forecasts

year to Mar, fully diluted

Analyst

Avadhoot Sabnis
+91 22 6715 5302
avadhoot.sabnis@rbs.com

83/84 Sakhar Bhawan, Nariman
Point, Mumbai 400 021, India

<http://research.rbsm.com>

Important disclosures can be found in the Disclosures Appendix.

bear 12%. Note that for 9M FY11, the OMCs have received total 78% compensation (OMC- 33% & GOI- 45%)

- The management is not disturbed by the seemingly low budget provision of Rs200bn for the GOI share of under-recoveries in FY12 as it would be revised upwards later as has been the case in the earlier years.
- Current under recoveries are as follows- Diesel- Rs11.16/ltr; Petrol- Rs3/ltr; Kerosene- Rs23.55/ltr; LPG- Rs289.4/cylinder.
- Management believes that it would be difficult to decontrol diesel in the near term given the high & volatile international crude oil prices, but expects some price hikes. Further they would look to raise petrol prices since the recent budget didn't contain any proposal to reduce under-recoveries on it.
- Management believes that direct transfer of cash subsidy is a step in the right direction but would be difficult to implement as states would oppose it.
- Management stated that both diesel & petrol have shown some price inelasticity with diesel volumes continuing to grow at 8-9% (in line with GDP growth) and petrol at 10-12% despite price hikes. Given the thin margins, retailing remains a volume driven business in management's view.

Other highlights

- As on date, HPCL has gross debt of Rs250bn and oil bonds of Rs80bn in its books. Its average cost of borrowing is 7.5%.
- Lubricant volumes are growing at 2% and HPCL has moved ahead of Castrol to become the no 2 player in the industry after IOC.
- Management stated that HPCL looks at a hurdle rate of 15% post tax IRR and the maximum debt-equity is 2:1 for approving any project .

Income statement

Rsm	FY09A	FY10A	FY11F	FY12F	FY13F
Revenue	1247524	1076375	1274926	1471203	1648999
Cost of sales	-1186638	-998090	-1195992	-1375744	-1538782
Operating costs	-27350	-52814	-45730	-50084	-53251
EBITDA	33536	25470	33203	45376	56966
DDA & Impairment (ex gw)	-9813	-11644	-13537	-21235	-23426
EBITA	23723	13826	19666	24141	33540
Goodwill (amort/impaired)	n/a	n/a	n/a	n/a	n/a
EBIT	23723	13826	19666	24141	33540
Net interest	-20828	-9038	-9834	-16613	-19076
Associates (pre-tax)	n/a	n/a	n/a	n/a	n/a
Forex gain / (loss)	n/a	n/a	n/a	n/a	n/a
Exceptionals (pre-tax)	n/a	n/a	n/a	n/a	n/a
Other pre-tax items	4227	16462	10930	11750	12149
Reported PTP	7122	21250	20762	19277	26614
Taxation	-1373	-8237	-7059	-7363	-8626
Minority interests	n/a	n/a	n/a	n/a	n/a
Exceptionals (post-tax)	n/a	n/a	n/a	n/a	n/a
Other post-tax items	0.00	0.00	0.00	0.00	0.00
Reported net profit	5749	13014	13703	11914	17988
Normalised Items Excl. GW	0.00	0.00	0.00	0.00	0.00
Normalised net profit	5749	13014	13703	11914	17988

Source: Company data, RBS forecasts

year to Mar

Balance sheet

Rsm	FY09A	FY10A	FY11F	FY12F	FY13F
Cash & market secs (1)	135881	90425	89676	89676	89676
Other current assets	154281	202221	205090	222014	242513
Tangible fixed assets	181324	237944	297728	321638	316162
Intang assets (incl gw)	n/a	n/a	n/a	n/a	n/a
Oth non-curr assets	7666	18734	14799	14899	14899
Total assets	479152	549324	607293	648227	663250
Short term debt (2)	195823	178495	191605	212444	212529
Trade & oth current liab	107088	151728	139457	153067	165015
Long term debt (3)	40156	60941	109959	107425	94892
Oth non-current liab	28218	39143	41638	44289	47766
Total liabilities	371285	430307	482658	517225	520202
Total equity (incl min)	107868	119017	124635	131003	143048
Total liab & sh equity	479152	549324	607293	648227	663250
Net debt	100099	149011	211888	230193	217745

Source: Company data, RBS forecasts

year ended Mar

Cash flow statement

Rsm	FY09A	FY10A	FY11F	FY12F	FY13F
EBITDA	33536	25470	33203	45376	56966
Change in working capital	28432	5580	-14728	-2918	-8154
Net interest (pd) / rec	-16602	7424	1096	-4864	-6927
Taxes paid	-1299	-6191	-4976	-5108	-5545
Other oper cash items	n/a	n/a	n/a	n/a	n/a
Cash flow from ops (1)	44068	32284	14595	32486	36341
Capex (2)	-36259	-68264	-73322	-45145	-17950
Disposals/(acquisitions)	0.00	0.00	0.00	0.00	0.00
Other investing cash flow	-2068	-15723	-8800	-100.0	0.00
Cash flow from invest (3)	-38327	-83987	-82122	-45245	-17950
Incr / (decr) in equity	1925	7590	9800	0.00	0.00
Incr / (decr) in debt	68113	3456	62127	18306	-12448
Ordinary dividend paid	-2080	-4738	-5150	-5546	-5943
Preferred dividends (4)	n/a	n/a	n/a	n/a	n/a
Other financing cash flow	-1995	-59.7	0.00	0.00	0.00
Cash flow from fin (5)	65963	6248	66777	12759	-18391
Forex & disc ops (6)	n/a	n/a	n/a	n/a	n/a
Incr/(decr) cash (1+3+5+6)	71704	-45455	-749.2	0.00	0.00
Equity FCF (1+2+4)	7809	-35980	-58727	-12659	18391

Lines in bold can be derived from the immediately preceding lines.
Source: Company data, RBS forecasts

year to Mar

Recommendation structure

Absolute performance, short term (trading) recommendation: A Trading Buy recommendation implies upside of 5% or more and a Trading Sell indicates downside of 5% or more. The trading recommendation time horizon is 0-60 days. For Australian coverage, a Trading Buy recommendation implies upside of 5% or more from the suggested entry price range, and a Trading Sell recommendation implies downside of 5% or more from the suggested entry price range. The trading recommendation time horizon is 0-60 days.

Absolute performance, long term (fundamental) recommendation: The recommendation is based on implied upside/downside for the stock from the target price and, except as follows, only reflects capital appreciation. A Buy/Sell implies upside/downside of 10% or more and a Hold less than 10%. For research produced by Nedbank Capital, a Buy implies upside in excess of 20%, A Sell implies an expected return less than 10%, and a Hold implies a return between 10% and 20%. For UK-based Investment Funds research, the recommendation structure is not based on upside/downside to the target price. Rather it is the subjective view of the analyst based on an assessment of the resources and track record of the fund management company. For research produced by Nedbank Capital and for research on Australian listed property trusts (LPT) or real estate investment trusts (REIT), the recommendation is based upon total return, ie, the estimated total return of capital gain, dividends and distributions received for any particular stock over the investment horizon.

Performance parameters and horizon: Given the volatility of share prices and our pre-disposition not to change recommendations frequently, these performance parameters should be interpreted flexibly. Performance in this context only reflects capital appreciation and the horizon is 12 months.

Market or sector view: This view is the responsibility of the strategy team and a relative call on the performance of the market/sector relative to the region. Overweight/Underweight implies upside/downside of 10% or more and Neutral implies less than 10% upside/downside.

Target price: The target price is the level the stock should currently trade at if the market were to accept the analyst's view of the stock and if the necessary catalysts were in place to effect this change in perception within the performance horizon. In this way, therefore, the target price abstracts from the need to take a view on the market or sector. If it is felt that the catalysts are not fully in place to effect a re-rating of the stock to its warranted value, the target price will differ from 'fair' value.

Distribution of recommendations

The tables below show the distribution of recommendations (both long term and trading). The first column displays the distribution of recommendations globally and the second column shows the distribution for the region. Numbers in brackets show the percentage for each category where there is an investment banking relationship. These numbers include recommendations produced by third parties with which RBS has joint ventures or strategic alliances.

Long term recommendations (as at 07 Mar 2011)

	Global total (IB%)	Asia Pacific total (IB%)
Buy	766 (13)	493 (3)
Hold	428 (7)	234 (1)
Sell	118 (1)	64 (0)
Total (IB%)	1312 (10)	791 (2)

Source: RBS

Trading recommendations (as at 07 Mar 2011)

	Global total (IB%)	Asia Pacific total (IB%)
Trading Buy	0 (0)	0 (0)
Trading Sell	0 (0)	0 (0)
Total (IB%)	0 (0)	0 (0)

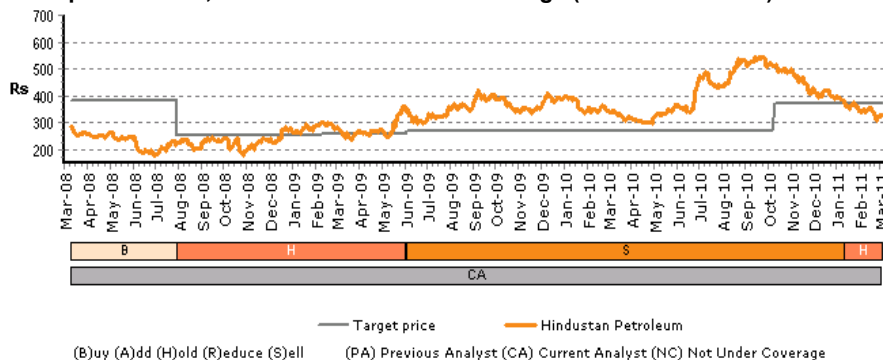
Source: RBS

Valuation and risks to target price

Hindustan Petroleum (RIC: HPCL.BO, Rec: Hold, CP: Rs329.45, TP: Rs370.00): Key upside risks to our investment case and PB-based target price are: 1) deregulation in the pricing of retail products; and 2) the government providing a transparent mechanism for subsidy sharing. Downside risk would be if the government provides lower-than-expected subsidy support.

HPCL coverage data (HPCL.BO, HPCL IN)

Stock performance, recommendations and coverage (as at 07 Mar 2011)



(B)uy (A)dd (H)old (R)educe (S)ell (PA) Previous Analyst (CA) Current Analyst (NC) Not Under Coverage

Avadhoot Sabnis started covering this stock on 28 Nov 03. Moved to new recommendation structure between 1 November 2005 and 31 January 2006. Source: RBS

Trading recommendation history

Date	Rec	Analyst
n/a	n/a	n/a

Source: RBS

Price perf (at Close 04 Mar 2011)

	(1M)	(3M)	(12M)
Price (Rs)	340.8	414.7	339.8
Absolute (%)	-3.3	-20.6	-3.0
Rel market (%)	-5.8	-14.2	-11.0
Rel sector (%)	-3.3	-22.2	-7.8

Source: Bloomberg
Market: Sensex
Sector: Integrated Oil & Gas

Regulatory disclosures

None

Global disclaimer

© Copyright 2011 The Royal Bank of Scotland N.V. and affiliated companies ("RBS"). All rights reserved.

This material was prepared by the legal entity named on the cover or inside cover page. It is provided for informational purposes only and does not constitute an offer to sell or a solicitation to buy any security or other financial instrument. While based on information believed to be reliable, no guarantee is given that it is accurate or complete. While we endeavour to update on a reasonable basis the information and opinions contained herein, there may be regulatory, compliance or other reasons that prevent us from doing so. The opinions, forecasts, assumptions, estimates, derived valuations and target price(s) contained in this material are as of the date indicated and are subject to change at any time without prior notice. The investments referred to may not be suitable for the specific investment objectives, financial situation or individual needs of recipients and should not be relied upon in substitution for the exercise of independent judgement. The stated price of any securities mentioned herein is as of the date indicated and is not a representation that any transaction can be effected at this price. Neither RBS nor other persons shall be liable for any direct, indirect, special, incidental, consequential, punitive or exemplary damages, including lost profits arising in any way from the information contained in this material. This material is for the use of intended recipients only and the contents may not be reproduced, redistributed, or copied in whole or in part for any purpose without RBS's prior express consent. In any jurisdiction in which distribution to private/retail customers would require registration or licensing of the distributor which the distributor does not currently have, this document is intended solely for distribution to professional and institutional investors.

Australia: Any report referring to equity securities is distributed in Australia by RBS Equities (Australia) Limited (ABN 84 002 768 701, AFS Licence 240530), a participant of the ASX Group. Any report referring to fixed income securities is distributed in Australia by The Royal Bank of Scotland NV (Australia Branch) (ABN 84 079 478 612, AFS Licence 238266). Australian investors should note that this document was prepared for wholesale investors only.

Canada: The securities mentioned in this material are available only in accordance with applicable securities laws and many not be eligible for sale in all jurisdictions. Persons in Canada requiring further information should contact their own advisors.

EEA: This material constitutes "investment research" for the purposes of the Markets in Financial Instruments Directive and as such contains an objective or independent explanation of the matters contained in the material. Any recommendations contained in this document must not be relied upon as investment advice based on the recipient's personal circumstances. In the event that further clarification is required on the words or phrases used in this material, the recipient is strongly recommended to seek independent legal or financial advice.

Denmark: Royal Bank of Scotland N.V. is authorised and regulated in the Netherlands by De Nederlandsche Bank. In addition, Royal Bank of Scotland N.V. Danish branch is subject to local supervision by Finanstilsynet, The Danish Financial Supervisory Authority.

Hong Kong: This document is being distributed in Hong Kong by, and is attributable to, RBS Asia Limited which is regulated by the Securities and Futures Commission of Hong Kong.

India: Shares traded on stock exchanges within the Republic of India may only be purchased by different categories of resident Indian investors, Foreign Institutional Investors registered with The Securities and Exchange Board of India ("SEBI") or individuals of Indian national origin resident outside India called Non Resident Indians ("NRIs"). Any recipient of this document wanting additional information or to effect any transaction in Indian securities or financial instrument mentioned herein must do so by contacting a representative of RBS Equities (India) Limited. RBS Equities (India) Limited is a subsidiary of The Royal Bank of Scotland N.V..

Italy: Persons in Italy requiring further information should contact The Royal Bank of Scotland N.V. Milan Branch.

Japan: This report is being distributed in Japan by RBS Securities Japan Limited to institutional investors only.

South Korea: This document is being distributed in South Korea by, and is attributable to, RBS Asia Limited (Seoul) Branch which is regulated by the Financial Supervisory Service of South Korea.

Malaysia: RBS research, except for economics and FX research, is not for distribution or transmission into Malaysia.

Netherlands: the Authority for the Financial Markets ("AFM") is the competent supervisor.

Russia: This Material is distributed in the Russian Federation by RBS and "The Royal Bank of Scotland" ZAO (general banking license No. 2594 issued by the Central Bank of the Russian Federation, registered address: building 1, 17 Bolshaya Nikitskaya str., Moscow 125009, the Russian Federation), an affiliate of RBS, for information purposes only and is not an offer to buy or subscribe or otherwise to deal in securities or other financial instruments, or to enter into any legal relations, nor as investment advice or a recommendation with respect to such securities or other financial instruments. This Material does not have regard to the specific investment purposes, financial situation and the particular business needs of any particular recipient. The investments and services contained herein may not be available to persons other than 'qualified investors' as this term is defined in the Federal Law "On the Securities Market".

Singapore: Any material in connection with equity securities is distributed in Singapore by The Royal Bank of Scotland Asia Securities (Singapore) Pte Limited ("RBS Asia Securities") (RCB Regn No. 198703346M). Without prejudice to any of the foregoing disclaimers, this material and the securities, investments or other financial instruments referred to herein are not in any way intended for, and will not be available to, investors in Singapore unless they are institutional investors (as defined in Section 4A(1) of the Securities and Futures Act (Cap. 289) of Singapore ("SFA") or relevant persons falling within Section 275 of the SFA and in accordance with the conditions specified therein or otherwise fall within the circumstances under Section 275 of the SFA. Further, without prejudice to any of the foregoing disclaimers, where this material is distributed to accredited investors or expert investors as defined in Regulation 2 of the Financial Advisers Regulations ("FAR") of the Financial Advisers Act (Cap. 110) of Singapore ("FAA"), RBS Asia Securities is exempted by Regulation 35 of the FAR from the requirements in Section 36 of the FAA mandating disclosure of any interest in securities referred to in this material, or in their acquisition or disposal. Recipients who do not fall within the description of persons under Regulation 49 of the Securities and Futures (Licensing and Conduct of Business) Regulations or Regulations 34 and 35 of the Financial Advisers Regulations should seek the advice of their independent financial advisor prior to taking any investment decision based on this document or for any necessary explanation of its contents.

Thailand: Pursuant to an agreement with Asia Plus Securities Public Company Limited (APS), reports on Thai securities published out of Thailand are prepared by APS but distributed outside Thailand by RBS Bank NV and affiliated companies. Responsibility for the views and accuracy expressed in such documents belongs to APS.

Turkey: The Royal Bank of Scotland N.V. is regulated by Banking Regulation and Supervision Authority (BRSA).

UAE and Qatar: This report is produced by The Royal Bank of Scotland N.V. and is being distributed to professional and institutional investors only in the United Arab Emirates and Qatar in accordance with the regulatory requirements governing the distribution of investment research in these jurisdictions.

Dubai International Financial Centre: This material has been prepared by The Royal Bank of Scotland N.V. and is directed at "Professional Clients" as defined by the Dubai Financial Services Authority (DFSA). No other person should act upon it. The financial products and services to which the material relates will only be made available to customers who satisfy the requirements of a "Professional Client". This Document has not been reviewed or approved by the DFSA.

Qatar Financial Centre: This material has been prepared by The Royal Bank of Scotland N.V. and is directed solely at persons who are not "Retail Customer" as defined by the Qatar Financial Centre Regulatory Authority. The financial products and services to which the material relates will only be made available to customers who satisfy the requirements of a "Business Customer" or "Market Counterparty".

United States of America: This document is intended for distribution only to "major institutional investors" as defined in Rule 15a-6 under the U.S. Exchange Act of 1934 as amended (the "Exchange Act"), and may not be furnished to any other person in the United States. Each U.S. major institutional investor that receives these materials by its acceptance hereof represents and agrees that it shall not distribute or provide these materials to any other person. Any U.S. recipient of these materials that wishes further information regarding, or to effect any transaction in, any of the securities discussed in this document, should contact and place orders solely through a registered representative of RBS Securities Inc., 600 Washington Boulevard, Stamford, CT, USA. Telephone: +1 203 897 2700. RBS Securities Inc. is an affiliated broker-dealer registered with the U.S. Securities and Exchange Commission under the Exchange Act, and a member of the Securities Investor Protection Corporation (SIPC) and the Financial Industry Regulatory Authority (FINRA).

- Material means all research information contained in any form including but not limited to hard copy, electronic form, presentations, e-mail, SMS or WAP.

The research analyst or analysts responsible for the content of this research report certify that: (1) the views expressed and attributed to the research analyst or analysts in the research report accurately reflect their personal opinion(s) about the subject securities and issuers and/or other subject matter as appropriate; and, (2) no part of his or her compensation was, is or will be directly or indirectly related to the specific recommendations or views contained in this research report. On a general basis, the efficacy of recommendations is a factor in the performance appraisals of analysts.

For a discussion of the valuation methodologies used to derive our price targets and the risks that could impede their achievement, please refer to our latest published research on those stocks at research.rbsm.com.

Disclosures regarding companies covered by us can be found on our research website at research.rbsm.com.

Our policy on managing research conflicts of interest can be found at <https://research.rbsm.com/Disclosure/Disclosure.Asp?MI=2>.

Should you require additional information please contact the relevant research team or the author(s) of this report.