



ENAM Securities
India Research

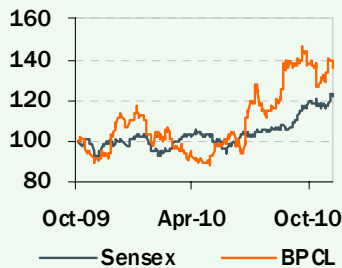
CMP: Rs 746
Target Price: Rs 830
Potential Upside: 11%
Absolute Rating: **BUY**

BPCL

Relative to sector: **Outperformer**

Amit Mishra, CFA
Sr. Vice President - Energy
Email: amit.mishra@enam.com
Tel: 9122 6754 7677

Relative Performance



Source: Bloomberg, ENAM Research

Stock data

No. of shares : 362 mn
Market cap : Rs 273 bn
52 week high/low : Rs 815/ Rs 489
Avg. daily vol. (6mth) : 1.8 mn shares
Bloomberg code : BPCL IB
Reuters code : BPCL.BO

Shareholding (%)	Sep-10	QoQ chg
Promoters	54.9	0.0
FIs	8.2	0.8
MFs / UTI	8.2	0.8
Banks / FIs	11.3	(1.7)
Others	17.4	0.0

Financial summary

Y/E Mar	Sales (Rs mn)	PAT (Rs mn)	Consensus EPS* (Rs)	EPS (Rs)	Change YoY (%)	P/E (x)	RoE (%)	RoCE (%)	EV/EBITDA (x)	DPS (Rs)
2010	1,238,167	17,387	-	48.1	167.8	15.5	11.9	9.9	17.6	13.7
2011E	1,474,680	12,652	48.5	35.0	(27.2)	21.6	8.2	8.2	12.3	9.8
2012E	1,469,719	12,155	56.4	33.6	(3.9)	22.5	7.5	7.7	11.8	11.7
2013E	1,475,013	15,227	58.8	42.1	25.3	17.9	8.9	8.7	10.5	11.7

Source: *Consensus broker estimates, Company, ENAM estimates

GOVERNMENT SUBSIDY PROPS EARNINGS

BPCL reported impressive Q2FY11 earnings of Rs 21 bn buoyed by government subsidy support of Rs 29.5 bn and forex gain of Rs 3 bn. The company suffered inventory loss of Rs 790 mn during the quarter.

Net cash inflow lower due to higher-than-expected working capital investments, dividend payout

The company sold bonds worth Rs 22 bn during H1FY11, to pay-off debt of Rs 12.3 bn, and incur a capex (including investments) of Rs 15.3 bn. Despite payment of Rs 16 bn from BORL, company's loans and advances reduced only by Rs 9 bn as BPCL provided further Rs 7 bn loans to its staff and subsidiaries including Rs 1.4 bn loan to BPRL (its E&P subsidiary). The company's net current assets rose by Rs 3 bn, while company paid dividend of Rs 5 bn during H1FY11.

E&P prospects could re-rate BPCL

BPCL's E&P investments and strategy to align with Anadarko and Petrobras have paid rich dividends. BPCL has already tasted success in its exploratory efforts in Brazil, Mozambique and Indonesia. Pace of exploration is set to kick-off from H2FY11. The co. has 10 blocks in Brazil in a high prospective zone which could add further upside to BPCL shareholders. Mozambique find size is huge and could mirror the world's largest gas fields depending on future exploratory efforts. Anadarko has already dedicated a rig for Mozambique for the next 14 months.

BPCL the best bet amongst OMCs; Maintain BUY

We believe with crude prices on the boil, chances of diesel dereg. have reduced considerably in the near-term. This may lead to some correction in OMCs and better performance by upstream stocks, e.g., RIL. However, we remain positive on BPCL, due to its stronger balance sheet and better E&P portfolio. BPCL is our preferred bet amongst OMCs with a target price of Rs 830/ share (potential upside of ~11% to CMP of Rs 746). We have not priced in diesel deregulation in our fair value calculations.

Results update

(Rs mn)	Quarter ended					12 months ended		
	Sep-10	Sep-09	% Chg	Jun-10	% Chg	Mar-11E	Mar-10	% Chg
Net Sales	354,348	270,923	30.8	342,325	3.5	1,474,680	1,238,167	19.1
EBIDTA	24,865	(950)	-	(14,059)	-	41,358	30,539	35.4
Other income	5,336	4,211	26.7	3,209	66.3	7,612	23,652	(67.8)
PBIDT	30,201	3,261	826.2	(10,850)	-	48,970	54,191	(9.6)
Depreciation	4,019	3,088	30.1	4,007	0.3	15,652	14,446	8.4
Interest	2,780	2,673	4.0	2,324	19.6	12,850	11,247	14.3
PBT	23,402	(2,500)	-	(17,181)	-	20,469	28,498	(28.2)
Tax	1,980	(912)	(317.1)	0	-	7,226	10,235	(29.4)
Minority Interest	0	0	-	0	-	591	876	(32.6)
Adjusted PAT	21,422	(1,588)	-	(17,181)	-	12,652	17,387	(27.2)
Extra ordinary income/ (exp.)	0	0	-	0	-	0	(1,064)	-
Reported PAT	21,422	(1,588)	-	(17,181)	-	12,652	16,324	(22.5)
No. of shares (mn)	362	362	-	362	-	362	362	-
EBIDTA margin (%)	7.0	(0.4)	-	(4.1)	-	2.8	2.5	-
PBIDT margin (%)	8.5	1.2	-	(3.2)	-	3.3	4.4	-
EPS - annualized (Rs.)	237.0	(17.6)	-	(190.1)	-	35.0	48.1	(27.2)

Source: Company, ENAM Research

Valuation: SoTP

	EV		Remarks
	(USD mn)	(Rs/sh)	
Refining fair value	2,212	292	FY12E refining EV/EBITDA at 7x
Valuation of subsidy burden	(3,289)	(434)	Wtd. average of EV/EBITDA of Marketing & Refining business
Marketing fair value	7,089	936	DCF based value; WACC of 10.1%; terminal growth rate 4%
Core business EV	6,013		
Investments			
- Nurmaliagarh Refineries Ltd	394	52	EV/EBITDA; 20% holding company discount
- Bharat PetroResources Ltd	434	57	DCF based value
- OIL stake	183	24	20% discount to current market value
- Indraprastha Gas	189	25	20% discount to current market value
- Petronet LNG	192	25	20% discount to current market value
- BOREL	318	42	Investments made to date
- Other investments	429	57	Investments made to date
EV of BPCL	8,151	1,077	
Net debt/ (Cash)	1,850	244	
BPCL fair value	6,301	832	

Source: ENAM Research

Operating performance: Quarterly trends

	Units	Q1FY10	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11
Total Refining throughput	MMT	4.2	5.0	5.5	5.7	5.7	5.6
Average GRMs	USD/bbl	3.2	3.8	1.3	3.7	3.6	2.7
Marketing sales	MMT	7.2	6.5	7.0	7.3	7.3	6.6

Source: Company, ENAM Research

Cash flow analysis: H1FY11

(Rs mn)	H1FY11
PAT	4,241
Depreciation	8,026
Capex	(8,335)
Working capital change	(3,014)
Deferred tax	1,200
Free cash flow	2,119
Sale of Investments	15,168
Debt repaid	(12,252)
Dividend paid (incl. dividend tax)	(5,920)
Gol payment	779
Net cash In/ (out)	(107)

Source: Company, ENAM Research

E&P: the game changer for BPCL**Brazil, the next big oil producer**

According to the latest World Energy Outlook released by IEA, Brazil will be the third largest contributor to the incremental global oil production over the next 25 years. Recent discoveries at fields such as Tupi (est. 8 bn bbl reserves, Santos basin) and Libra (est. 4-15 bn bbl reserves, Santos basin) are set to propel Brazil into the top 10 oil producing nations of the world. OPEC reportedly invited Brazil to join the group after these discoveries.

- **Huge capex plans:** Petrobras plans ~USD 250 bn expenditure (~20% of global E&P expenditure) on E&P activities over the next five years. The recent USD 70 bn public offer is a part of this plan. The company will use its cash flows and additional debt to fund the rest of the program. The investments of this stature by a single company in a single country over the next five years, signify the potential for Brazilian E&P sector.
- **Sinopec's acquisition of the Respol's Brazilian arm for USD 7.1 bn** was at a huge premium to the market consensus. This further reinforces our view that Brazilian E&P assets are going to attract a significant premium in the coming future.
- **BPCL present in 10 blocks in Brazil.** These include 2 blocks in Potiguar basin (10% stake), 4 blocks in Sergipe basin (20% stake), 3 blocks in Espirito Santos basin (15% stake) and 1 block in Campos basin (12.5% stake). First discovery made at the Wahoo-1 prospect in the Campos basin was followed by successes at Wahoo-2 and Wahoo-south prospects. Its reserve potential is estimated at ~ 200 mnboe which, we believe is significant for a company of BPCL's size (mkt cap ~ USD 6 bn). Recent discovery at Barra well in the Sergipe basin (70 sq. kms aerial extent) is also expected to hold reserves in significant quantities.

Mozambique: another goldmine

- Windjammer discovery at the Rovuma basin has been declared as the largest gas find in the world in Q1CY10. Though no reserve numbers have been given so far, comparisons with some of India's most prolific blocks (refer table below) point towards a huge reserve potential. This was followed by recent success in Barquentine prospect. The discoveries in Mozambique are also important considering their geographical proximity to gas hungry countries like India. Anadarko has dedicated a rig for further appraisal of discoveries at these prospects and plans to use floating LNG terminal for commercial exploitation of these gas reserves.

Rovuma basin vis-à-vis Indian blocks#

Prospect	KG-D6 Block	KG-D3	NEC-25*	Mozambique (Rovuma basin)	
				Windjammer	Barquentine
Average Net Pay (ft)	336	129	84	485	485
Block size (sq. kms)	7,645	3,288	10,755	10,700	

Source: DGH, Company, ENAM Research; # reserve potential contingent on others factors like porosity, permeability etc., * NEC-25 block size excluding relinquished area

Other E&P assets

- The Anadarko led consortium at the Nunukan block in Indonesia recently announced the hydrocarbon discovery at Badik-1 prospect in the Tarakan basin. BPRL has 12.5% PI in the JV. The operator of the block (Anadarko) has guided that it plans to carry out an appraisal program in the block to ascertain the potential.

We believe these developments have not only showcased BPCL management's astuteness, but have also created a strong possibility for re-rating of the stock going forward.

BPCL: E&P status update

Block	NELP round	Status	Stake(%)	Remarks
Brazil (JV)				
Campos	1	Exploration	12.5	Discovery-DST Wahoo #1; # 2A completed, rig to be shifted to Wahoo # 3
Espirito Santos	3	Exploration	15	2 exploration wells drilled
Sergipe	4	Exploration	20	Discovery at Barra well
Portiguar	2	Exploration	10	Exploration well to be drilled in CY11
Mozambique				
Rovuma basin		Exploration	10	Discoveries at Windjammer, Barquentine & Ironclad prospects
Indonesia				
Nunukan block		Exploration	12.5	Discovery at Badik-1 prospect
Australia				
WA-388P		Exploration	14	1st well dry
Block AC/P 32		Exploration	20	1st well dry
North Sea				
Block 48/2c, 1d		Exploration		Drill or drop by February 11

Block	NELP round	Status	Stake(%)	Remarks
India				
KG-DN-2002/1	4	Exploration	10	1st well dry. 5 wells planned. 2nd in FY11
MN-DWN-2002/1	4	Exploration	10	2 wells planed in FY11
CY-ONN-2002/1	4	Exploration	40	1st dry. Another well planned in FY11
CY-ONN-2004/1	6	Exploration	20	1 well planned in FY11
CY-ONN-2004/2	6	Exploration	20	1 well planned in FY11
RJ-ONN-2004/1	6	Exploration	11.1	6 wells finalized. 3 in FY11. 1st in December
KG-DWN-2004/2	6	Exploration	10	Seismic completed
KG-DWN-2004/5	6	Exploration	10	Seismic completed
RJ-ONN-2005/1	7	Exploration	33.3	Hiked from 25% due to default by other JV member
Oman				
Block 56		Exploration	12.5	Relinquished and written of US\$5.39mn

Source: Company, ENAM Research

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