

Reliance Industries

Set to close FY10 with a bang

Reliance Industries (RIL) is expected to report strong Q4FY10 results supported by an expansion in refining and petrochemical margins as well as higher gas output from the KG-D6 block. The Singapore GRM has improved sharply to US\$ 5/bbl so far in Q4FY10 from US\$ 1.9/bbl in Q3. Further, petrochemical prices have risen by ~10% during the quarter, which will result in margins improving by ~15% over naphtha. KG-D6 gas output too has stabilised at 58–60mmscmd during the quarter against 47mmscmd in Q3FY10. In view of the uptrend across segments, we are raising our estimates for FY10 while maintaining the status-quo for FY11 and FY12. We maintain Buy with an increased target of Rs 1,226.

GRMs moving north; expect strong recovery in H2FY11: The benchmark Singapore refining margin has rebounded to US\$ 5.1/bbl in Q4FY10 to date against US\$ 1.9/bbl in Q3FY10, driven by an intense winter season in the US and Europe. Gasoline and gasoil crack spreads have also increased substantially over the past couple of months, leading to higher GRMs. The light-heavy differential remains low, however, at US\$ 1.7/bbl due to the sharp production cut from OPEC and increased complex refinery capacity. Considering the improvement over the past couple of months, we are revising our GRM estimate for RIL to US\$ 9/bbl in Q4FY10 from US\$ 7/bbl earlier.

Petrochemical margins remain strong: RIL's petrochemical prices have increased substantially during the quarter led by strong domestic consumption. Polymer rates have improved by an average of ~10% QoQ, while polyester prices have risen ~9% QoQ so far in Q4FY10. Margins are also expected to improve significantly over naphtha by ~15% QoQ during the quarter. We are thus revising our petrochemical margin assumption for Q4 to 17% from 15% earlier.

KG-D6 gas output stabilises: We expect RIL's KG-D6 gas output to average 58–60mmscmd in Q4FY10 from 47mmscmd in Q3FY10. However, peak production of 80mmscmd is likely to be achieved only by Q3FY11, when expansion of the HVJ pipeline is concluded.

FY10 estimates and target price raised: We are revising our PAT estimates for FY10 upwards by 7% to incorporate the uptick in GRMs and petrochemical prices in the current quarter. Further, we are raising our estimate for other income due to increased cash levels following the sale of treasury stocks. Our FY11 and FY12 estimates remain largely unchanged. Based on our revised numbers, we are raising our target price to Rs 1,226 from Rs 1,206. RIL is currently trading at a P/E of 14.4x and 12.5x on FY11E and FY12E respectively. The stock is likely to run up in the near term on expectations of a strong Q4.

Financial highlights

(Rs mn)	FY09	FY10E	FY11E	FY12E
Revenue	1,512,240	1,986,313	2,556,043	2,675,469
Growth (%)	10.3	31.3	28.7	4.7
Adj net income	149,687	177,053	232,198	267,702
Growth (%)	(2.3)	18.3	31.1	15.3
FDEPS (Rs)	47.6	54.1	71.0	81.9
Growth (%)	(9.8)	13.9	31.1	15.3

Profitability and return ratios

(%)	FY09	FY10E	FY11E	FY12E
EBITDA margin	15.5	14.8	14.3	15.3
EBIT margin	11.8	10.6	10.5	11.4
Adj PAT margin	9.9	8.9	9.1	10.0
ROE	14.5	13.4	15.1	15.2
ROIC	9.4	10.3	12.8	14.8
ROCE	10.0	9.5	11.1	11.7

What's New? Target Rating Estimates

CMP	TARGET	RATING	RISK
Rs 1,010	Rs 1,226	BUY	MEDIUM

BSE	NSE	BLOOMBERG
500325	RELIANCE	RIL IN

Company data

Market cap (Rs bn / US\$ bn)	3,335.0/72.5
Outstanding equity shares (mn)	3,270
Free float (%)	53.4
Dividend yield (%)	0.7
52-week high/low (Rs)	1,245/559
3-month average daily volume	1,165,654

Stock performance

Returns (%)	CMP	1-mth	3-mth	6-mth
RIL	1,010	(0.6)	(6.9)	2.4
Oil and Gas	9,764	(1.6)	(6.8)	(0.2)
Sensex	16,994	6.6	(1.4)	5.4

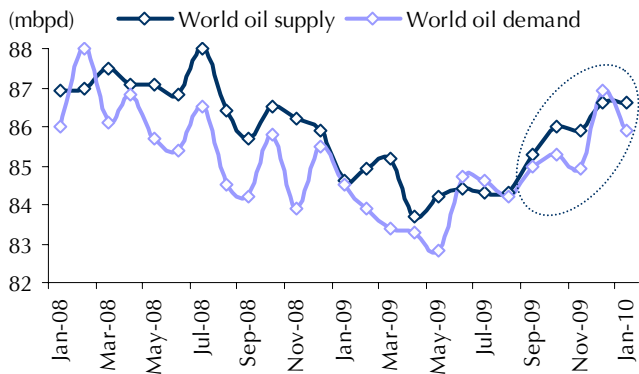
Valuation matrix

(x)	FY09	FY10E	FY11E	FY12E
P/E @ CMP	21.4	18.8	14.4	12.5
P/E @ Target	25.8	22.6	17.3	15.0
EV/EBITDA @ CMP	16.5	13.1	10.6	9.5





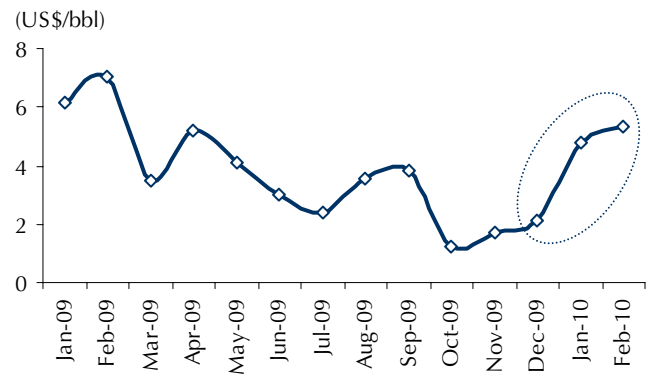
Fig 1 - World oil demand-supply



Source: Bloomberg

Sharp uptick in oil demand over the past quarter

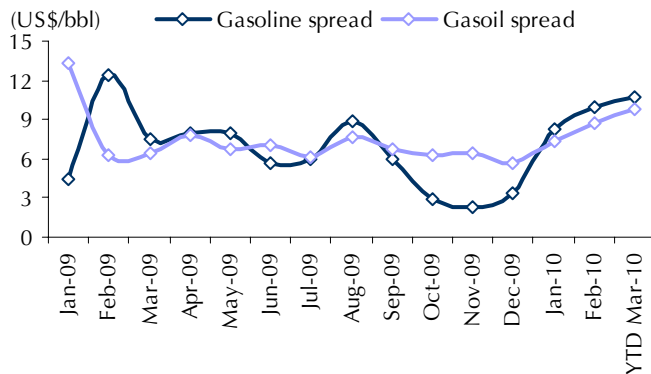
Fig 2 - Sharp improvement in Singapore refining margins



Source: Reuters

GRMs to cool-off slightly in coming months as the warmer season sets in, but expect a strong surge in H2FY11 in tandem with global recovery

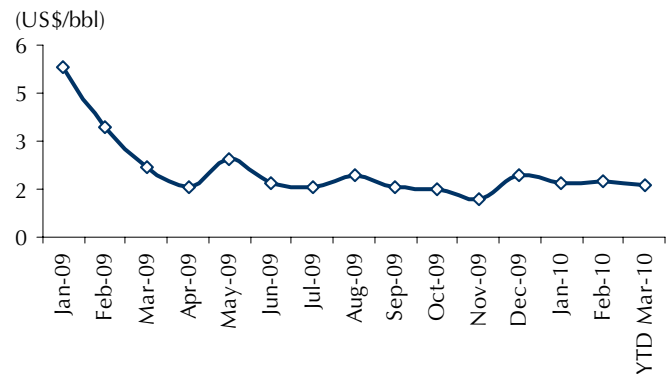
Fig 3 - Gasoline & gasoil crack spread over Dubai crude



Source: Bloomberg, RHH

Gasoline and gasoil crack spreads averaged US\$ 9.6/bbl and US\$ 8.6 respectively in Q4FY10 YTD, against US\$ 2.9 and US\$ 6.1 in Q3

Fig 4 - Light-heavy differential still much below Jul '08 peaks



Source: Bloomberg, RHH

Arab L-H differential improved marginally to US\$ 1.7/bbl in Q4FY10 YTD but is still far below the all-time high of US\$ 10 in July '08

Polymer and polyester prices have improved by 9-10% QoQ in Q4FY10

Fig 5 - Petrochemical prices on the rise

(Rs/kg)	Q4FY10	Q4FY09	% Chg YoY	Q3FY10	% Chg QoQ
PE	76.8	59.7	28.5	70.1	9.5
PP	74.1	63.0	17.7	64.8	14.4
PVC	53.7	41.9	28.0	48.7	10.3
POY	73.7	62.0	18.9	67.6	9.1
PSF	69.8	57.5	21.3	64.3	8.6
PTA	48.1	36.5	31.6	44.2	8.7
MEG	48.2	27.7	73.8	37.9	27.2
LAB	85.8	76.1	12.7	91.4	(6.2)

Source: RHH, Company



We revise our petrochem margin to 16.3% in FY10 from 15.7%; estimate of 15% for FY11 and FY12 unchanged

Fig 6 - Petrochemical margins over naphtha broadening

(Rs/kg)	Q4FY10	Q4FY09	% Chg YoY	Q3FY10	% Chg QoQ
PE	42.0	38.2	9.9	36.7	14.6
PP	39.4	41.5	(5.0)	31.4	25.6
PVC	18.9	20.4	(7.2)	15.3	24.1
POY	39.0	40.5	(3.7)	34.2	14.2
PSF	35.0	36.0	(2.7)	30.8	13.6
PTA	13.3	15.0	(11.2)	10.8	23.6
MEG	13.4	6.2	116.7	4.5	201.3
LAB	51.0	54.6	(6.5)	58.0	(12.0)

Source: RHH

Fig 7 - Revision of estimates

Key parameters	Q4FY10E			FY10E			FY11E		
	Old	New	% Chg	Old	New	% Chg	Old	New	% Chg
Revenues	597,341	592,006	(0.9)	1,991,772	1,986,313	(0.3)	2,574,615	2,556,043	(0.7)
EBITDA	87,653	101,030	15.3	300,768	314,020	4.4	384,405	389,775	1.4
EBITDA margin (%)	14.7	17.1	239bps	15.1	15.8	71bps	14.9	15.2	32bps
Adjusted net profit	47,806	59,788	25.1	165,148	177,053	7.2	225,907	232,198	2.8
Adjusted EPS (Rs)	14.6	18.3	25.1	50.5	54.1	7.2	69.1	71.0	2.8

Source: RHH



Consolidated financials

Profit and Loss statement

Y/E March (Rs mn)	FY09	FY10E	FY11E	FY12E
Revenues	1,512,240	1,986,313	2,556,043	2,675,469
Growth (%)	10.3	31.3	28.7	4.7
EBITDA	234,222	294,623	366,700	408,913
Growth (%)	1.2	25.8	24.5	11.5
Depreciation & amortisation	56,510	83,621	99,476	104,006
EBIT	177,712	211,003	267,224	304,906
Growth (%)	(2.0)	18.7	26.6	14.1
Interest	18,163	19,897	18,514	17,253
Other income	19,142	116,402	33,934	36,043
EBT	178,691	307,507	282,644	323,696
Income taxes	29,188	44,173	50,419	55,994
Effective tax rate (%)	16.3	14.4	17.8	17.3
Extraordinary items	-	-	-	-
Min into / inc from associates	(184)	21	28	-
Reported net income	149,687	263,313	232,198	267,702
Adjustments	-	86,261	-	-
Adjusted net income	149,687	177,053	232,198	267,702
Growth (%)	(2.3)	18.3	31.1	15.3
Shares outstanding (mn)	3,147.6	3,270.1	3,270.1	3,270.1
FDEPS (Rs) (adj)	47.6	54.1	71.0	81.9
Growth (%)	(9.8)	13.9	31.1	15.3
DPS (Rs)	7.1	7.0	7.5	8.5

Cash flow statement

Y/E March (Rs mn)	FY09	FY10E	FY11E	FY12E
Net income + Depreciation	226,813	346,934	331,674	371,709
Non-cash adjustments	(39,903)	(49,771)	46,614	3,535
Changes in working capital	(57,725)	(14,917)	(13,722)	4,468
Cash flow from operations	129,185	282,246	364,566	379,712
Capital expenditure	(277,320)	(65,800)	(97,957)	(97,978)
Change in investments	33,663	92,621	(9,214)	(11,057)
Other investing cash flow	(1,015)	-	-	-
Cash flow from investing	(244,673)	26,820	(107,171)	(109,034)
Issue of equity	151,648	(13,367)	-	-
Issue/repay debt	165,145	(55,144)	(34,942)	(34,937)
Dividends paid	(19,085)	(26,189)	(28,060)	(23,790)
Other financing cash flow	(13)	-	-	-
Change in cash & cash eq	182,207	214,366	194,392	211,951
Closing cash & cash eq	227,421	441,787	636,179	848,130

Economic Value Added (EVA) analysis

Y/E March	FY09	FY10E	FY11E	FY12E
WACC (%)	12.1	12.5	12.7	12.5
ROIC (%)	9.4	10.3	12.8	14.8
Invested capital (Rs mn)	1,780,250	1,733,825	1,708,657	1,697,670
EVA (Rs mn)	(48,582)	(38,037)	232	39,888
EVA spread (%)	(2.7)	(2.2)	0.0	2.3

Balance sheet

Y/E March (Rs mn)	FY09	FY10E	FY11E	FY12E
Cash and cash eq	227,421	441,787	636,179	848,130
Accounts receivable	48,450	63,575	81,752	85,561
Inventories	201,096	264,138	339,900	355,781
Other current assets	110,494	126,690	146,154	150,234
Investments	64,355	65,014	74,228	85,285
Gross fixed assets	1,545,870	2,145,870	2,245,870	2,345,870
Net fixed assets	1,057,299	1,573,679	1,574,202	1,570,196
CWIP	738,460	204,260	202,217	200,195
Intangible assets	13,143	13,143	13,143	13,143
Deferred tax assets, net	(95,513)	(107,032)	(118,579)	(130,126)
Other assets	36	23	17	17
Total assets	2,365,241	2,645,277	2,949,213	3,178,416
Accounts payable	345,011	453,169	583,150	610,397
Other current liabilities	12,559	16,496	21,227	22,219
Provisions	31,150	31,150	31,150	31,150
Debt funds	762,566	707,422	672,479	637,543
Other liabilities	1,389	1,410	1,439	1,439
Equity capital	31,476	32,701	32,701	32,701
Reserves & surplus	1,181,089	1,402,929	1,607,066	1,842,967
Shareholder's funds	1,212,565	1,435,630	1,639,767	1,875,668
Total liabilities	2,365,241	2,645,277	2,949,213	3,178,416
BVPS (Rs)	385.2	439.0	501.4	573.6

Financial ratios

Y/E March	FY09	FY10E	FY11E	FY12E
Profitability & Return ratios (%)				
EBITDA margin	15.5	14.8	14.3	15.3
EBIT margin	11.8	10.6	10.5	11.4
Net profit margin	9.9	8.9	9.1	10.0
ROE	14.5	13.4	15.1	15.2
ROCE	10.0	9.5	11.1	11.7
Working Capital & Liquidity ratios				
Receivables (days)	13	10	10	11
Inventory (days)	59	55	55	61
Payables (days)	86	94	94	104
Current ratio (x)	1.6	1.9	2.0	2.3
Quick ratio (x)	0.8	1.1	1.2	1.5
Turnover & Leverage ratios (x)				
Gross asset turnover	1.1	1.1	1.2	1.2
Total asset turnover	0.7	0.8	0.9	0.9
Interest coverage ratio	9.8	10.6	14.4	17.7
Adjusted debt/equity	0.6	0.5	0.4	0.3
Valuation ratios (x)				
EV/Sales	2.6	1.9	1.5	1.4
EV/EBITDA	16.5	13.1	10.6	9.5
P/E	21.4	18.8	14.4	12.5
P/BV	2.6	2.3	2.0	1.8



Quarterly trend

Particulars	Q3FY09	Q4FY09	Q1FY10	Q2FY10	Q3FY10
Revenue (Rs mn)	315,630	283,620	311,870	468,480	568,560
YoY growth (%)	(8.8)	(23.9)	(25.0)	4.8	80.1
QoQ growth (%)	(29.4)	(10.1)	10.0	50.2	21.4
EBITDA (Rs mn)	53,630	54,370	63,840	72,170	78,440
EBITDA margin (%)	17.0	19.2	20.5	15.4	13.8
Adj net income (Rs mn)	35,010	38,740	36,660	38,520	40,080
YoY growth (%)	(9.8)	(1.0)	(10.8)	(6.6)	(2.6)
QoQ growth (%)	(15.1)	1.3	3.4	5.9	9.3

DuPont analysis

(%)	FY08	FY09E	FY10E	FY11E	FY12E
Tax burden (Net income/PBT)	59.5	83.8	57.6	82.2	82.7
Interest burden (PBT/EBIT)	126.8	100.6	145.7	105.8	106.2
EBIT margin (EBIT/Revenues)	13.2	11.8	10.6	10.5	11.4
Asset turnover (Revenues/Avg TA)	93.7	74.9	79.3	91.4	87.3
Leverage (Avg TA/Avg equity)	190.4	195.2	189.2	181.9	174.3
Return on equity	17.8	14.5	13.4	15.1	15.2

Company profile

Reliance Industries (RIL) has a sophisticated 1.3mbpd oil refinery with an average Nelson complexity of 12.6, apart from an integrated petrochemicals unit. The company recently commissioned a 580kbp refinery unit in Jamnagar SEZ. RIL also holds more than 0.4m km² of oil and gas acreage across 57 blocks in India and overseas. The company also started gas production from the KG-D6 basin from April '09 and expected to touch peak production of 80mmcmd by Q3FY11.

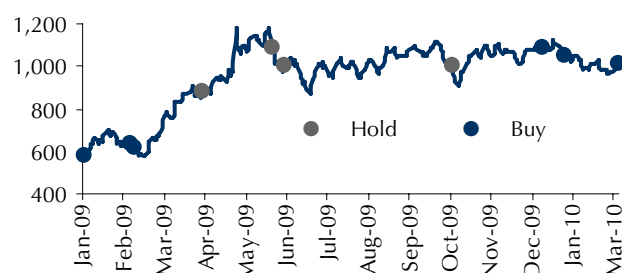
Shareholding pattern

(%)	Jun-09	Sep-09	Dec-09
Promoters	49.0	46.3	46.6
FIs	16.5	16.5	16.8
Banks & FIs	9.4	10.0	9.8
Public	25.2	27.1	26.8

Recommendation history

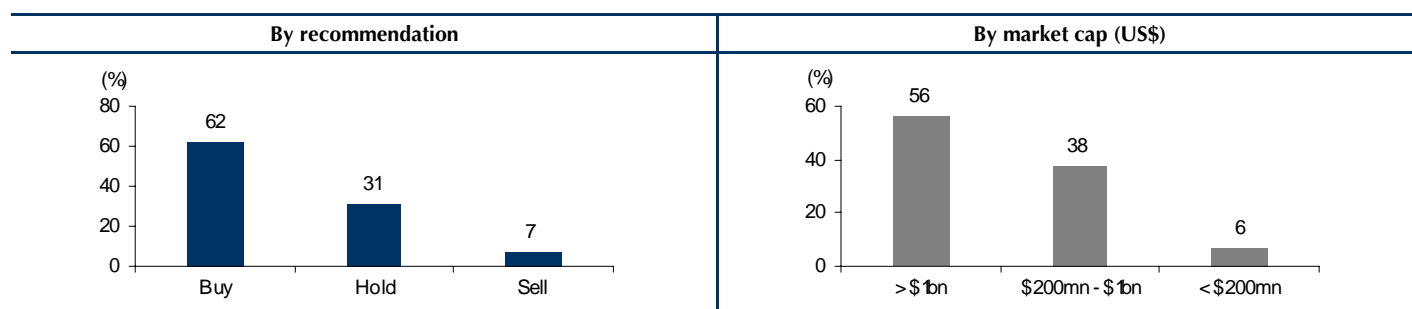
Date	Event	Reco price	Tgt price	Reco
23-Jan-09	Results Review	577	717	Buy
2-Mar-09	Company Update	633	717	Buy
3-Mar-09	Company Update	613	730	Buy
24-Apr-09	Results Review	881	854	Hold
15-Jun-09	Company Update	1,090	1,037	Hold
25-Jul-09	Results Review	1,007	935	Hold
30-Oct-09	Results Review	1,000	1,013	Hold
6-Jan-10	Quarterly Preview	1,070	1,246	Buy
23-Jan-10	Results Review	1,054	1,206	Buy
8-Mar-10	Company Update	1,010	1,226	Buy

Stock performance





Coverage Profile



Recommendation interpretation

Recommendation	Expected absolute returns (%) over 12 months
Buy	More than 15%
Hold	Between 15% and -5%
Sell	Less than -5%

Recommendation structure changed with effect from March 1, 2009

Expected absolute returns are based on share price at market close unless otherwise stated. Stock recommendations are based on absolute upside (downside) and have a 12-month horizon. Our target price represents the fair value of the stock based upon the analyst's discretion. We note that future price fluctuations could lead to a temporary mismatch between upside/downside for a stock and our recommendation.

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