

Indian Oil Corp

Weighed down by poor government support

Like for other OMCs, Q3FY10 proved to be a disappointing quarter for Indian Oil Corp (IOC) that reported lower-than-expected profits on poor government support. The government will now provide Rs 71bn as subsidy support to IOC as against its earlier commitment to bear the entire cooking fuel subsidy of Rs 124bn. This validates our supposition on the ineffectiveness of the current subsidy sharing mechanism once crude neared the US\$ 80/bbl mark. We therefore expect all OMCs, including IOC, to bear 20% of the subsidy burden, double than estimated earlier. Therefore, we are lowering our estimates and target price to Rs 300 (from Rs 312 previously) but maintain Hold on the stock.

Revenues in line: IOC's revenues remained flat YoY at Rs 704bn. This was marginally ahead of our estimates driven by a 4.1% increase in crude throughput to 12.5mmt and a 7.1% increase in petroleum product sales to 17.7mmt during the quarter.

Lower government support impacts margins: The government has announced a subsidy support of Rs 71bn to IOC for FY10 as against its earlier commitment to bear Rs 124bn of the total cooking-fuel subsidy. Of this, IOC has accounted for Rs 44.8bn in 9MFY10. However, the company has been reimbursed fully for its auto fuel under-recoveries of Rs 43bn for 9MFY10 (by way of upstream discounts). Consequently, IOC's own share of under-recoveries for 9MFY10 stood at Rs 79.4bn, below our estimates. Also, the company reported a consolidated GRM of US\$ 3.7/bbl in Q3FY10 compared to US\$ 3.4/bbl in Q3FY09, in line with our estimates. Consequently, IOC's net profit for Q3FY10 came in at Rs 7bn, much lower-than-anticipated.

Reservations over current subsidy sharing mechanism maintained: We had earlier assumed that the current subsidy sharing mechanism (100% auto fuel to upstream and 100% cooking fuel to government) would not work once crude oil nears US\$ 80/bbl. Consequently, we had distributed the entire subsidy burden among upstream, government, and OMCs in the ratio of 33%, 57% and 10%, respectively. However, given the lower contribution expected from the government, we are raising the contribution of OMCs to 20%.

Estimates, target price lowered; maintain hold: We have pruned our estimates for FY10 and FY11 by 16% and 20% respectively, to factor in IOC's higher subsidy burden. We have valued the stock on SOTP basis by assigning a P/BV of 1x on FY11E BV; IOC's investment in ONGC, GAIL, and Petronet has been valued at Rs 71. Our target price stands revised to Rs 300 (from Rs 312 earlier). Maintain Hold.

What's New?	Target	Rating	Estimates
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CMP	TARGET	RATING	RISK
Rs 301	Rs 300	HOLD	MEDIUM

BSE	NSE	BLOOMBERG
530965	IOC	IOCL IN

Company data

Market cap (Rs bn / US\$ bn)	718 / 15
Outstanding equity shares (mn)	2384.7
Free float (%)	21.1
Dividend yield (%)	1.3
52-week high/low (Rs)	395 / 190
3-month average daily volume	984,687

Stock performance

Returns (%)	CMP	1-mth	3-mth	6-mth
IOC	301	(2.2)	(4.2)	12.5
BSE Oil&Gas	9,939	(4.6)	2.4	7.4
Sensex	16,358	(6.0)	1.9	7.8

P/E Valuation matrix

(x)	FY09	FY10E	FY11E	FY12E
P/E @ CMP	32.5	10.8	11.6	9.8
P/E @ Target	32.4	10.8	11.5	9.8
EV/EBITDA @ CMP	20.3	11.3	12.3	10.8

Financial highlights

(Rs mn)	FY09	FY10E	FY11E	FY12E
Revenue	2,861,047	2,411,852	2,942,447	3,010,357
Growth (%)	25.5	(15.7)	22.0	2.3
Adj net income	22,094	67,377	63,231	74,283
Growth (%)	(72.2)	205.0	(6.2)	17.5
FDEPS (Rs)	9.3	27.8	26.0	30.6
Growth (%)	(72.2)	199.5	(6.2)	17.5

Profitability and return ratios

(%)	FY09	FY10E	FY11E	FY12E
EBITDA margin	2.0	4.3	3.3	3.6
EBIT margin	0.9	3.0	2.1	2.5
Adj PAT margin	0.8	2.8	2.1	2.5
ROE	5.0	14.0	11.9	12.7
ROIC	1.9	5.1	4.4	5.2
ROCE	5.5	9.3	8.9	10.1

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Result highlights

Fig 1 - Quarterly performance

(Rs mn)	Q3FY10	Q3FY09	% Chg YoY	Q2FY10	% Chg QoQ
Net sales	704,098	705,341	(0.2)	609,697	15.5
Expenditure	693,625	671,510	3.3	603,559	14.9
EBITDA	10,473	33,831	(69.0)	6,138	70.6
EBITDA margin (%)	1.5	4.8	(331 bps)	1.0	48 bps
Other income	6,783	18,177	(62.7)	8,481	(20.0)
Interest	4,091	15,054	(72.8)	3,477	17.6
Depreciation	7,996	7,275	9.9	7,805	2.4
PBT	5,168	29,678	(82.6)	3,337	54.9
Tax	(1,798)	93	-	493	-
PAT	6,966	29,585	(76.5)	2,844	145.0
EPS (Rs)	2.9	12.4	(76.5)	1.2	145.0
Crude Throughput (MMT)	12.53	12.04	4.1	12.41	1.0
Product Sales (MMT)	17.65	16.48	7.1	16.73	5.5

Source: Company, RHH

Fig 2 - Revised estimates

Key parameters (Rs mn)	FY10E			FY11E		
	Old	New	% Chg	Old	New	% Chg
Revenue	2,456,856	2,411,852	(1.8)	3,041,232	2,942,447	(3.2)
EBITDA	120,118	104,865	(12.7)	118,656	95,918	(19.2)
EBITDA margin (%)	4.9	4.3	(54 bps)	3.9	3.3	(64 bps)
Net profit	80,040	67,377	(15.8)	78,731	63,231	(19.7)
FDEPS (Rs)	33.0	27.8	(15.8)	32.4	26.0	(19.7)

Source: RHH

Fig 3 - Sharing of under-recoveries (UR)

(Rs mn)	Q1FY10	Q2FY10	Q3FY10	9MFY10	Q4FY10E	FY10E	FY11E	FY12E
Auto-fuel subsidy	2,291	17,991	22,748	43,029	30,710	73,739	223,425	239,065
Cooking-fuel UR	29,611	41,744	52,830	124,185	58,316	182,501	259,413	262,105
Total UR	31,902	59,735	75,578	167,214	89,026	256,240	482,838	501,170
Distribution								
Government	0	0	44,825	44,825	75,608	120,433	226,934	235,550
% of total	0.0	0.0	59.3	26.8	84.9	47.0	47.0	47.0
Upstream	2,291	17,991	22,748	43,029	41,530	84,559	159,337	165,386
% of total	7.2	30.1	30.1	25.7	46.6	33.0	33.0	33.0
IOC	29,611	41,744	8,005	79,360	(28,112)	51,248	96,567	100,234
% of total	92.8	69.9	10.6	47.5	(31.6)	20.0	20.0	20.0

Source: RHH, Company



Consolidated financials

Profit and Loss statement

Y/E March (Rs mn)	FY09	FY10E	FY11E	FY12E
Revenues	2,861,047	2,411,852	2,942,447	3,010,357
Growth (%)	25.5	(15.7)	22.0	2.3
EBITDA	58,146	104,865	95,918	109,181
Growth (%)	(54.4)	80.3	(8.5)	13.8
Depreciation & amortisation	31,894	32,844	33,759	34,674
EBIT	26,252	72,022	62,159	74,507
Growth (%)	(73.0)	174.3	(13.7)	19.9
Interest	42,076	25,904	25,091	23,485
Other income	52,315	58,098	61,003	64,053
EBT	36,491	104,215	98,071	115,076
Income taxes	12,533	35,815	33,880	39,664
Effective tax rate (%)	34.3	34.4	34.5	34.5
Extraordinary items	-	-	-	-
Min into / inc from associates	(2,036)	1,024	961	1,128
Reported net income	25,994	67,377	63,231	74,283
Adjustments	3,900	-	-	-
Adjusted net income	22,094	67,377	63,231	74,283
Growth (%)	(72.2)	205.0	(6.2)	17.5
Shares outstanding (mn)	2,384.7	2,427.9	2,427.9	2,427.9
FDEPS (Rs) (adj)	9.3	27.8	26.0	30.6
Growth (%)	(72.2)	199.5	(6.2)	17.5
DPS (Rs)	3.9	4.9	5.9	6.9

Cash flow statement

Y/E March (Rs mn)	FY09	FY10E	FY11E	FY12E
Net income + Depreciation	59,375	100,221	96,990	108,956
Non-cash adjustments	(396,669)	18,367	21,053	24,698
Changes in working capital	94,184	25,369	(19,722)	1,163
Cash flow from operations	(243,110)	143,957	98,320	134,818
Capital expenditure	(18,382)	(26,919)	(21,938)	(21,957)
Change in investments	297,975	(6,022)	(11,347)	(11,778)
Other investing cash flow	(112,540)	-	-	-
Cash flow from investing	167,054	(32,941)	(33,285)	(33,735)
Issue of equity	-	432	-	-
Issue/repay debt	85,259	(95,000)	(40,000)	(60,000)
Dividends paid	(9,754)	(13,960)	(16,803)	(19,647)
Other financing cash flow	-	-	-	-
Change in cash & cash eq	(550)	2,489	8,232	21,435
Closing cash & cash eq	10,052	12,541	20,773	42,208

Economic Value Added (EVA) analysis

Y/E March	FY09	FY10E	FY11E	FY12E
WACC (%)	11.8	12.4	12.8	12.8
ROIC (%)	1.9	5.1	4.4	5.2
Invested capital (Rs mn)	945,649	921,320	941,543	940,449
EVA (Rs mn)	(92,947)	(67,697)	(79,225)	(71,414)
EVA spread (%)	(9.8)	(7.3)	(8.4)	(7.6)

Balance sheet

Y/E March (Rs mn)	FY09	FY10E	FY11E	FY12E
Cash and cash eq	10,052	12,541	20,773	42,208
Accounts receivable	47,817	40,310	49,178	50,313
Inventories	285,182	240,407	293,296	300,065
Other current assets	128,976	128,061	128,735	129,474
Investments	313,239	319,261	330,607	342,385
Gross fixed assets	679,293	704,293	724,293	744,293
Net fixed assets	379,990	372,773	359,641	345,595
CWIP	191,889	193,808	195,746	197,703
Intangible assets	4,542	4,542	4,542	4,542
Deferred tax assets, net	(59,691)	(60,282)	(60,933)	(61,649)
Other assets	945	945	945	945
Total assets	1,302,940	1,252,365	1,322,530	1,351,581
Accounts payable	205,195	172,979	211,033	215,904
Other current liabilities	126,829	130,311	133,966	137,804
Provisions	26,630	44,967	66,034	90,611
Debt funds	473,469	378,469	338,469	278,469
Other liabilities	15,774	16,747	17,707	18,836
Equity capital	23,847	24,279	24,279	24,279
Reserves & surplus	431,196	484,614	531,041	585,677
Shareholder's funds	455,044	508,893	555,321	609,956
Total liabilities	1,302,940	1,252,365	1,322,530	1,351,580
BVPS (Rs)	190.8	209.6	228.7	251.2

Financial ratios

Y/E March	FY09	FY10E	FY11E	FY12E
Profitability & Return ratios (%)				
EBITDA margin	2.0	4.3	3.3	3.6
EBIT margin	0.9	3.0	2.1	2.5
Net profit margin	0.8	2.8	2.1	2.5
ROE	5.0	14.0	11.9	12.7
ROCE	5.5	9.3	8.9	10.1
Working Capital & Liquidity ratios				
Receivables (days)	6	7	6	6
Inventory (days)	41	41	37	40
Payables (days)	30	33	26	29
Current ratio (x)	1.4	1.4	1.4	1.5
Quick ratio (x)	0.2	0.2	0.2	0.3
Turnover & Leverage ratios (x)				
Gross asset turnover	4.4	3.5	4.1	4.1
Total asset turnover	2.3	1.9	2.3	2.3
Interest coverage ratio	0.6	2.8	2.5	3.2
Adjusted debt/equity	1.0	0.8	0.6	0.5
Valuation ratios (x)				
EV/Sales	0.4	0.5	0.4	0.4
EV/EBITDA	20.3	11.3	12.3	10.8
P/E	32.5	10.8	11.6	9.8
P/BV	1.6	1.4	1.3	1.2



Quarterly trend

Particulars	Q3FY09	Q4FY09	Q1FY10	Q2FY10	Q3FY10
Revenue (Rs mn)	705,341	599,377	591,796	609,697	704,098
YoY growth (%)	10.1	(16.6)	(33.1)	(29.5)	(0.2)
QoQ growth (%)	(18.4)	(15.0)	(1.3)	3.0	15.5
EBITDA (Rs mn)	33,831	89,582	49,990	6,138	10,473
EBITDA margin (%)	4.8	14.9	8.4	1.0	1.5
Adj net income (Rs mn)	29,585	66,230	36,828	2,844	6,966
YoY growth (%)	41.5	(1,698.6)	787.2	(104.0)	(76.5)
QoQ growth (%)	(142.0)	123.9	(44.4)	(92.3)	145.0

DuPont analysis

(%)	FY08	FY09	FY10E	FY11E	FY12E
Tax burden (Net income/PBT)	63.7	60.5	64.7	64.5	64.6
Interest burden (PBT/EBIT)	128.5	139.0	144.7	157.8	154.4
EBIT margin (EBIT/Revenues)	4.3	0.9	3.0	2.1	2.5
Asset turnover (Revenues/Avg TA)	209.0	228.6	188.8	228.5	225.1
Leverage (Avg TA/Avg equity)	272.1	280.9	265.1	242.0	229.5
Return on equity	19.8	5.0	14.0	11.9	12.7

Company profile

IOC is the 20th largest petroleum company in the world and the largest integrated oil marketing player in India, with a presence in refining, marketing, pipelines, petrochemicals and a limited interest in the upstream sector. IOC owns ~35% of India's refining capacity and commands ~50% market share in the country's auto and cooking fuel sales. In FY07, it reached a unique milestone by becoming the first and only Indian company to date to cross Rs 2,000bn in turnover.

Shareholding pattern

(%)	Jun-09	Sep-09	Dec-09
Promoters	78.9	78.9	78.9
FII's	0.9	0.9	0.8
Banks & FI's	5.5	5.5	5.3
Public	14.7	14.7	15.0

Recommendation history

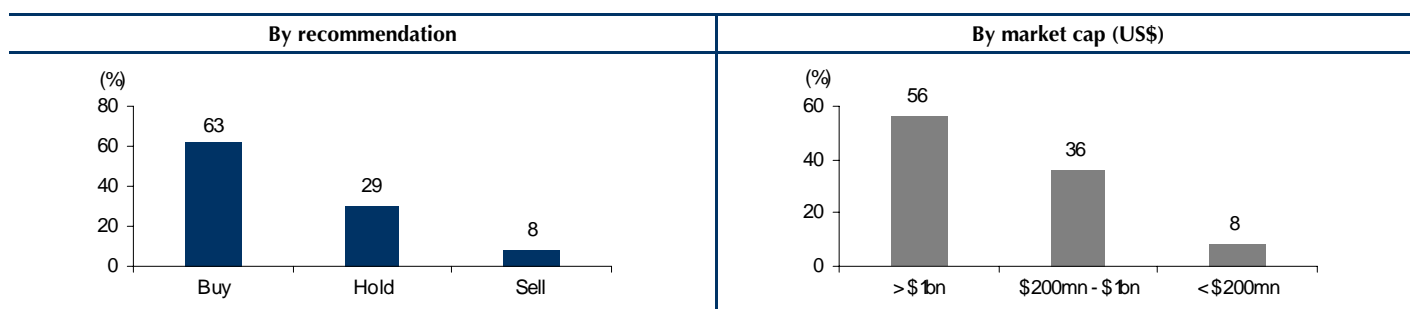
Date	Event	Reco price	Tgt price	Reco
20-Mar-09	Initiating Coverage	387	533	Buy
1-Jun-09	Results Review	609	627	Hold
30-Jul-09	Results Review	556	574	Hold
30-Oct-09	Results Review	311	335	Hold
29-Jan-10	Results Review	310	300	Hold

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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