

NOVEMBER 18, 2009

UPDATE

Coverage view: **Cautious**

Price (Rs): **2,132**

Target price (Rs): **1,750**

BSE-30: **17,051**

No surprises in AGM. There were no surprises or acquisition-related announcements at RIL's annual general meeting (AGM). We maintain our earnings estimates and see significant downside risks to FY2010E and FY2011E consensus earnings estimates due to (1) current very weak refining margins and (2) recent sharp correction in chemical margins. In our view, RIL stock is a SELL at current levels without any favorable developments on acquisitions or E&P.

Company data and valuation summary

Reliance Industries

Stock data

52-week range (Rs) (high,low)	2,535-1,021
Market Cap. (Rs bn)	3,106.8

Shareholding pattern (%)

Promoters	40.9
FIs	19.8
MFs	2.7

Price performance (%)

	1M	3M	12M
Absolute	(4.2)	9.8	87.1
Rel. to BSE-30	(2.5)	(4.7)	1.9

Forecasts/Valuations

	2009	2010E	2011E
EPS (Rs)	101.2	96.6	137.5
EPS growth (%)	(3.7)	(4.5)	42.4
P/E (X)	21.1	22.1	15.5
Sales (Rs bn)	1,418.5	1,737.3	1,900.6
Net profits (Rs bn)	153.1	158.7	225.9
EBITDA (Rs bn)	236.7	301.4	394.4
EV/EBITDA (X)	14.9	11.5	8.3
ROE (%)	13.6	10.9	13.8
Div. Yield (%)	0.5	0.5	0.7

Subdued AGM with no acquisition-related announcements

RIL did not make any acquisition-related announcement at its AGM contrary to Street expectations of announcement of or intent of a global acquisition. The key announcements were—(1) peak gas production from KG D-6 block to be achieved by 2HFY10, (2) oil production from KG block at ~8,000 b/d with peak production to be achieved by end-FY2010E, (3) renewed focus on a new 2 mtpa petrochemical complex at Jamnagar, announced in an AGM two years back and (4) commencement of exploratory drilling in Block 18 in Oman.

No change in earnings estimates; significant earnings downgrades possible

We maintain our FY2010E and FY2011E EPS estimates of Rs97 and Rs138. However, we believe that fundamentals need to improve significantly to achieve our below-consensus estimate of Rs97 for FY2010E. We see downside to our earnings estimates since current chemical and refining margins are well below our 2HFY10E assumptions. We foresee a sharp downgrade to consensus earnings estimates of Rs116. We believe our FY2011E estimate of Rs138 (consensus is at Rs156) looks equally challenging without a very steep recovery in refining and chemical margins; fundamentals appear very grim over the next 12-18 months.

Retain SELL with 12-month target price of Rs1,750

We retain our 12-month SOTP-based fair valuation of Rs1,750 and SELL rating. Key upside risks stem from (1) steep global economic recovery and (2) higher-than-expected E&P reserves. We see downside risks to our fair valuation from (1) weaker-than-expected chemical and refining margins and (2) further unfavorable developments in the ongoing RIL-RNRL legal dispute (Rs135/share). We note US\$1/bbl decline in refining margins impacts RIL's FY2010E EPS by 9.7% and FY2011E EPS by 7.1% and a US\$50/ton decline in chemical margins impacts RIL's FY2010E EPS by 7.6% and FY2011E EPS by 5.2%. We continue to find RIL stock expensive in light of the above-mentioned risks and note that the current stock price is already factoring in about 45tcf of new E&P discoveries.

QUICK NUMBERS

- **No acquisition-related announcements at AGM**
- **Significant risks to earnings**
- **Maintain SELL with target price of Rs1,750**

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Reliance Industries: Profit model, balance sheet, cash model, March fiscal year-ends, 2006-12E (Rs mn)

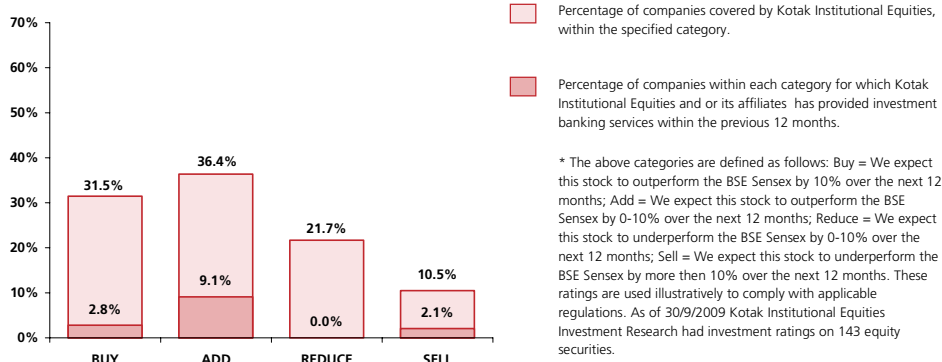
	2006	2007	2008	2009	2010E	2011E	2012E
Profit model (Rs mn)							
Net sales	809,113	1,114,927	1,334,430	1,418,475	1,737,271	1,900,615	1,955,552
EBITDA	139,991	198,462	233,056	233,139	297,817	390,796	423,469
Other income	6,829	4,783	8,953	20,599	28,093	23,414	20,906
Interest	(8,770)	(11,889)	(10,774)	(17,452)	(26,454)	(25,299)	(5,458)
Depreciation & depletion	(34,009)	(48,152)	(48,471)	(51,953)	(96,541)	(110,860)	(115,616)
Pretax profits	104,041	143,205	182,764	184,332	202,913	278,051	323,301
Extraordinary items	3,000	2,000	47,335	—	—	—	—
Tax	(9,307)	(16,574)	(26,520)	(12,634)	(28,537)	(63,152)	(74,408)
Deferred taxation	(7,040)	(9,196)	(8,999)	(18,605)	(15,700)	11,004	14,922
Net profits	90,693	119,434	194,580	153,093	158,676	225,902	263,815
Adjusted net profits	88,152	117,789	152,605	153,093	158,676	225,902	263,815
Earnings per share (Rs)	63	81	105	101	97	138	161
Balance sheet (Rs mn)							
Total equity	430,543	673,037	847,853	1,263,730	1,432,093	1,627,275	1,853,543
Deferred taxation liability	49,708	69,820	78,725	97,263	112,963	101,960	87,038
Minority interest	—	33,622	33,622	—	—	—	—
Total borrowings	218,656	332,927	493,072	739,045	623,376	382,410	117,736
Current liabilities	164,545	192,305	251,427	357,019	319,539	332,151	340,235
Total liabilities and equity	863,452	1,301,712	1,704,700	2,457,057	2,487,971	2,443,796	2,398,551
Cash	21,461	18,449	42,822	221,765	164,183	128,187	114,027
Current assets	224,283	286,566	402,721	325,358	386,953	400,667	404,188
Total fixed assets	626,745	899,403	1,081,638	1,693,869	1,720,769	1,698,876	1,664,271
Investments	(9,038)	97,294	177,519	216,065	216,065	216,065	216,065
Deferred expenditure	—	—	—	—	—	—	—
Total assets	863,452	1,301,712	1,704,700	2,457,057	2,487,970	2,443,795	2,398,551
Free cash flow (Rs mn)							
Operating cash flow, excl. working capital	119,520	164,285	180,718	174,508	222,282	292,099	330,757
Working capital	(32,188)	(13,075)	(31,071)	(37,983)	(99,076)	(1,101)	4,563
Capital expenditure	(94,273)	(247,274)	(239,691)	(247,128)	(165,675)	(73,025)	(71,990)
Investments	(32,364)	(105,760)	(78,953)	(10,392)	—	—	—
Other income	5,159	4,143	6,132	16,195	28,093	23,414	20,906
Free cash flow	(34,146)	(197,681)	(162,865)	(104,800)	(14,376)	241,387	284,235
Ratios (%)							
Debt/equity	45.5	44.8	53.2	54.3	40.3	22.1	6.1
Net debt/equity	41.1	42.3	48.6	38.0	29.7	14.7	0.2
RoAE	19.9	20.3	18.9	13.6	11.3	14.3	14.8
RoACE	13.8	13.9	12.7	11.2	9.5	11.2	12.5

Source: Company, Kotak Institutional Equities estimates

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Kotak Institutional Equities Research coverage universe

Distribution of ratings/investment banking relationships



Source: Kotak Institutional Equities

As of September 30, 2009

Ratings and other definitions/identifiers

Definitions of ratings

BUY. We expect this stock to outperform the BSE Sensex by 10% over the next 12 months.

ADD. We expect this stock to outperform the BSE Sensex by 0-10% over the next 12 months.

REDUCE. We expect this stock to underperform the BSE Sensex by 0-10% over the next 12 months.

SELL. We expect this stock to underperform the BSE Sensex by more than 10% over the next 12 months.

Our target price are also on 12-month horizon basis.

Other definitions

Coverage view. The coverage view represents each analyst's overall fundamental outlook on the Sector. The coverage view will consist of one of the following designations: **Attractive, Neutral, Cautious.**

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