



# Indian Oil Corporation

BSE SENSEX	S&P CNX
17,773	5,390
Bloomberg	IOCL IN
Equity Shares (m)	2,428.0
52-Week Range (INR)	360/247
1,6,12 Rel. Perf. (%)	-7/-20/-12
M.Cap. (INR b)	670.1
M.Cap. (USD b)	13.6

**CMP: INR276**

**Buy**

Year	Net Sales	Adj. PAT	Adj. EPS	EPS	P/E	P/BV	RoE	RoCE	EV/	EV/
End	(INR b)	(INR b)	(INR)	GR. (%)	(X)	(X)	(%)	(%)	Sales	EBITDA
03/10A	2,501	107.1	44.1	312.1	-	-	21.9	16.0	-	-
03/11A	3,081	78.3	32.3	-26.9	8.6	1.2	14.2	11.2	0.4	9.1
03/12E	4,133	70.7	29.1	-9.7	9.5	1.1	12.2	12.8	0.3	6.2
03/13E	3,768	79.2	32.6	12.1	8.5	1.0	13.0	12.4	0.3	5.9

\* Consolidated

- IOCL reported EBITDA of INR107.2b for 3QFY12 (v/s our estimate of INR8.7b), primarily due to net over-recovery of INR70b (v/s estimated net under-recovery of INR40.3b), led by higher government compensation.
- Adjusted PAT was INR86.6b v/s estimated loss of INR11.7b. Comparative PAT was INR16.3b in 3QFY11 and a loss of INR74.9b in 2QFY12. IOCL reported a PAT of INR24.9b due to one-time provision of INR61.7b towards entry tax for its Mathura refinery in UP. It made this provision as per Supreme Court directives for a stay on Allahabad High Court's order, which had directed IOCL to pay the entry tax. The Supreme Court had agreed to give conditional stay if IOCL deposits 50% of the liability and provides bank guarantee for the rest. However, the actual amount to be provided will be known only after the Supreme Court's ongoing hearing.
- Given the ad-hoc subsidy sharing, we believe quarterly financials are not indicative of the likely full-year performance. We now model OMCs' subsidy sharing at nil in FY12 (similar to FY09 v/s 2% earlier) and upstream sharing at ~40%, with the rest being borne by the government.
- 3QFY12 reported GRM stood at USD4.3/bbl v/s USD6.3/bbl in 3QFY11 and adj. GRM of USD2.8/bbl in 2QFY12. IOCL has restated its 2QFY12 GRM to USD2.76/bbl (v/s reported USD0/bbl). The restatement is on account of new PPAC directive to exclude exchange gain/(loss) on crude liabilities for the purpose of GRM calculation.

## Valuation and view

- We model Brent oil price of USD112/100/95/90/bbl in FY12/FY13/FY14/long-term. For FY12/13, we model upstream share at 40%/38.7% and OMCs' share at nil/9%, with the rest being borne by the government.
- We continue to believe that while reforms in the sector are extremely necessary over the long term, in the near-term, price hikes are inevitable.
- The stock trades at 9.5x FY12E EPS of INR29.1 and 1.1x FY12E BV. Key things to watch (apart from subsidy sharing) are positive contribution from its petchem division and GRM performance. **Buy.**

## Quarterly Performance (Standalone)

Y/E March	FY11				FY12				(INR Million)	
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE	FY11	FY12E
Net Sales	716,890	767,568	803,332	982,634	1,007,239	891,456	1,152,084	1,219,228	3,270,423	4,270,005
Change (%)	15.3	26.4	8.5	19.6	40.5	16.1	43.4	24.1	17.2	30.6
EBITDA	-29,175	65,210	27,276	53,234	-24,225	-53,618	107,247	137,158	116,544	166,563
% of Net Sales	-4.1	8.5	3.4	5.4	-2.4	-6.0	9.3	11.2	3.6	3.9
% Change	nm	1,411.7	689.0	-27.1	nm	nm	293.2	157.7	-4.6	42.9
Depreciation	10,346	11,178	11,778	12,165	12,235	12,638	12,839	13,164	45,467	50,877
Interest	5,712	5,079	7,233	8,675	10,376	14,840	15,652	13,646	26,698	54,514
Other Income	11,349	12,309	13,528	9,393	9,649	6,241	7,810	7,817	46,579	31,516
PBT	-33,884	61,262	21,793	41,788	-37,187	-74,855	86,566	118,165	90,958	92,689
Tax	0	8,323	5,445	2,736	0	0	0	27,807	16,504	27,807
Rate (%)	nm	13.6	25.0	6.5	nm	nm	nm	23.5	18.1	30.0
Adj. PAT	-33,884	52,939	16,348	39,052	-37,187	-74,856	86,566	90,358	74,454	64,882
Change (%)	nm	1,761.5	134.7	-29.7	nm	nm	429.5	131.4	-27.2	-12.9
Extraordinary Items							-61,682		0	-61,681
PAT	-33,884	52,939	16,348	39,052	-37,187	-74,856	24,884	90,358	74,454	3,201

E: MOSL Estimates

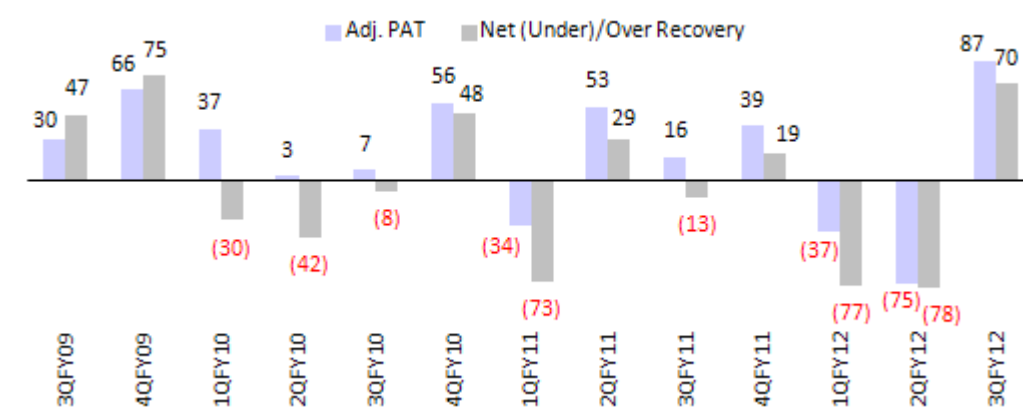
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### Reports net over recovery as govt. compensates together for two quarters (2QFY12 and 3QFY12)

- Of the gross under-recovery of INR177.6b in 3QFY12, IOCL received INR83.4b from upstream and INR164.2b from government. The net subsidy over recovery stood at INR70b in 3QFY12.
- Government compensation at INR164.2b was 2x of our est. because govt. compensation is for two quarters (2QFY12 and 3QFY12) v/s our assumption for only 1 quarter. In 2QFY12 govt had not given any compensation. In the first three quarters, govt. has now given INR450b to all the three OMC's (quarterly runrate of INR150b).

### Ad-hoc subsidy sharing resulting in volatile quarterly profits (INR b)



Source: Company/MOSL

### Other key highlights

- IOC's petrochemical division reported negative EBIT of INR1.7b. This was the fifth time in last six quarters the company reported negative EBIT.
- Gross debt increased to INR787b as on Dec-11 v/s INR733b in 2QFY12 and INR527b on 31 March 2011.
- 3QFY12 reported GRM stood at USD4.3/bbl as against USD6.3/bbl in 3QFY11 and adj. GRM of USD2.8/bbl in 2QFY12. IOCL has restated its 2QFY12 GRM to USD2.76/bbl (v/s reported USD0/bbl). The restatement is on account of new PPAC directive to exclude exchange gain/(loss) on crude liabilities for the purpose of GRM calculation.
- Product inventory adventitious gain in the quarter stood at INR10.3b (v/s gain of INR3.3b in 3QFY11 and loss of INR9.9b in 2QFY11).
- Refinery throughput stood at 14.2mmt (v/s est. of 14mmt), up 6% YoY and 9% QoQ. Marketing volumes were up 5% YoY and 9% QoQ to 19.3mmt.

### IOCL: 3QFY12 Operational highlights

	FY11				FY12		3QFY12		
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	YoY (%)	QoQ (%)
Product Sales (mmt)	18.31	16.92	18.42	19.27	19.26	17.69	19.29	4.7	9.0
Throughput (mmt)	13.28	12.13	13.32	14.23	14.31	13.05	14.17	6.4	8.6
GRM (USD/bbl)	3.00	6.58	6.33	7.85	4.71	2.76	4.31	-31.9	56.2

Source: Company/MOSL

**IOCL's subsidy sharing: Reports over recovery in 3QFY12 due to high govt. compensation (INRb)**

	FY11				FY12			3QFY12	
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	YoY (%)	QoQ (%)
Gross Under recovery	110.1	64.1	86.6	170.3	238.1	117.6	177.6	105.1	51.0
<b>Less: Sharing</b>									
Upstream Sharing	36.7	21.4	28.9	80.1	79.3	39.2	83.4	188.8	112.6
Oil Bonds	0.0	72.2	44.4	109.4	82.0	0.0	164.2	269.7	nm
<b>Net Under/(over)recovery</b>	<b>73.4</b>	<b>(29.5)</b>	<b>13.3</b>	<b>(19.2)</b>	<b>76.7</b>	<b>78.4</b>	<b>(70.0)</b>	<b>nm</b>	<b>nm</b>
<b>As a % of Gross</b>	<b>66.7</b>	<b>(46.0)</b>	<b>15.4</b>	<b>nm</b>	<b>32.2</b>	<b>66.7</b>	<b>(39.4)</b>		

Source: Company/MOSL

**We model OMCs' sharing at nil in FY12 and 9% in FY13 (INR b)**

	FY08	FY09	FY10	FY11	FY12E	FY13E
Fx Rate (INR/USD)	40.3	46.0	47.5	45.6	47.6	50.0
Brent (USD/bbl)	82.3	84.8	69.6	86.3	112.7	100.0
<b>Gross Under recoveries (INR b)</b>						
Auto Fuels	426	575	144	375	750	550
Domestic Fuels	347	458	316	405	566	505
<b>Total</b>	<b>773</b>	<b>1,033</b>	<b>461</b>	<b>780</b>	<b>1,316</b>	<b>1,055</b>
<b>Sharing (INR b)</b>						
Oil Bonds/Cash	353	713	260	410	789	552
Upstream	257	329	145	303	526	409
OMC's sharing	163	-9	56	67	0	94
<b>Total</b>	<b>773</b>	<b>1,033</b>	<b>461</b>	<b>780</b>	<b>1,316</b>	<b>1,055</b>
<b>Sharing (%)</b>						
Government	46	69	56	53	60	52
Upstream	33	32	31	39	40	39
OMC's sharing	21	-1	12	9	0	9
<b>Total</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>

Source: Company/MOSL

**Valuation and view**

- We model Brent oil price of USD112/100/95/90/bbl in FY12/FY13/FY14/long-term in our estimates. For FY12/13, we model upstream share at 40%/38.7%, OMCs' share at nil/9% and rest to be borne by Government.
- We continue to believe that over the long term, while reforms in the sector are extremely necessary, in the near-term, price hikes are inevitable. We believe that the political compulsion would ease post five state assembly elections making some room for tough decisions in the sector. While, as the headline inflation number has reduced from double digit levels to 7.4% in Dec-11 and moderating, we expect some price hikes to take place.
- The stock trades at 9.5x FY12E EPS of INR29.1 and 1.1x FY12E BV. Key event to watch (apart from subsidy sharing) is the positive contribution from its petchem division and the GRM performance. Maintain **Buy**.

## Indian Oil Corporation: an investment profile

### Company description

A Fortune-500 company, IOC is the largest refining and marketing company in India. It operates 8 refineries (incl BRPL) with a capacity of 49.7mmtpa and has a 52% stake in CPCL (10.5mmt refining capacity). The company controls a refining capacity of 65.7 mmtpa. It has a pipeline network of >10,300km (62mmtpa capacity), has 18,278 petrol/diesel outlets and has interests in petrochemicals and upstream oil and gas. IOC is a Public Sector Company with 80.35% Government of India stake.

### Key investment arguments

- IOC's profitability continues to be determined by the quantum of under-recoveries and sharing mechanism, rather than fundamentals.
- Growth would come from (1) Expansion of Panipat refinery from 12 to 15mmtpa, (2) INR144b Naphtha cracker (commissioned) at Panipat and (3) Setting up INR256b integrated refinery(15mmtpa) /petchem complex at Paradip.
- IOC's valuations should benefit due to improvement in (1) earnings quality, (2) RoCE & RoE, (3) cash cycle and (4) lower debt levels.

### Key investments risks

- Maintaining marketing share and margins on auto fuels in view of likely competition from private players.

- Planning of mega investments in view of ad-hoc subsidy sharing.
- Non commensurate increase in the retail fuel prices as oil price rises, leads to under recoveries for the company and ad-hoc nature of subsidy sharing impacts the profits.

### Recent developments

- Government has initiated the process of decontrol of retail fuel prices, starting with petrol prices. It is expected to gradually also decontrol diesel, LPG and kerosene prices in the coming months. The FPO of IOC and ONGC could be the key triggers to start the decontrol process for LPG, kerosene and diesel.

### Valuation and view

- Stock trades at 9.5x FY12E cons. EPS of INR29.1 and 1.1x FY12E BV. Valuations are attractive. **Buy.**

### Sector view

- Global economic environment (particularly Europe) will continue to weigh heavily on refining margins. While economic outlook continues to remain uncertain, we expect GRMs to remain range bound. However, the ceiling will be capped in the near term due to new capacities coming online in FY13 and FY14. We expect the demand-supply gap to correct only through refinery closure of simple refiners and continuous pick-up in global demand.

### Target price and recommendation

Current Price (INR)	Target Price (INR)	Upside (%)	Reco.
276	-	-	Buy

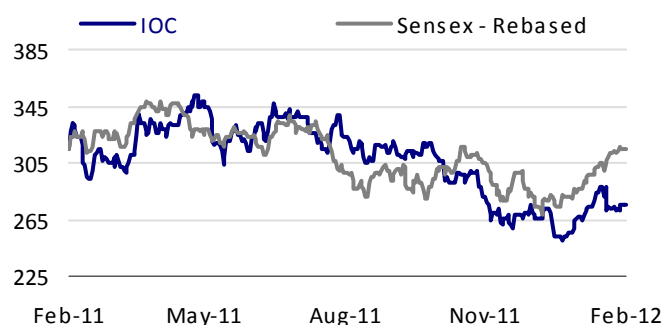
### EPS: MOSL forecast v/s consensus (INR)

	MOSL Forecast	Consensus Forecast	Variation (%)
FY12	29.1	25.7	13.2
FY13	32.6	35.6	-8.4

### Shareholding pattern (%)

	Dec-11	Sep-11	Dec-10
Promoter	79.0	79.0	79.0
Domestic Inst	5.2	5.1	4.8
Foreign	0.7	0.9	1.2
Others	15.1	15.0	15.0

### Stock performance (1 year)



## Financials and Valuation

Income Statement (Consolidated)			(INR Billion)		
Y/E March	2009	2010	2011	2012E	2013E
Net Sales	2,861	2,501	3,081	4,133	3,768
Change (%)	25.5	-12.6	23.2	34.1	-8.8
Finished Gds Purchas	1,424	1,008	1,276	1,967	1,804
Raw Materials Cons	1,123	1,158	1,445	1,738	1,659
Other Operating Cost	251	206	235	241	107
<b>EBITDA</b>	<b>62</b>	<b>129</b>	<b>125</b>	<b>187</b>	<b>198</b>
% of Net Sales	2.2	5.1	4.1	4.5	5.3
Depreciation	32	36	49	55	62
Interest	42	17	30	57	46
Other Income	48	75	55	32	28
Extraordinary Items (I	0	0	0	62	0
<b>PBT</b>	<b>36</b>	<b>150</b>	<b>101</b>	<b>46</b>	<b>119</b>
Tax	13	40	20	33	36
Rate (%)	34.3	26.9	20.1	71.2	30.2
<b>PAT</b>	<b>24</b>	<b>110</b>	<b>81</b>	<b>13</b>	<b>83</b>
Minority interest	2	-3	-3	-4	-3
<b>Group net profit</b>	<b>26</b>	<b>107</b>	<b>78</b>	<b>9</b>	<b>79</b>
<b>Adj. net profit</b>	<b>26</b>	<b>107</b>	<b>78</b>	<b>71</b>	<b>79</b>
Change (%)	-67.1	312.1	-26.9	-9.7	12.1

Balance Sheet			(INR Billion)		
Y/E March	2009	2010	2011	2012E	2013E
Share Capital	24	24	24	24	24
Reserves	431	500	551	560	614
<b>Net Worth</b>	<b>455</b>	<b>525</b>	<b>576</b>	<b>585</b>	<b>638</b>
Minority interest	16	18	20	24	28
Loans	473	495	578	645	592
Deferred Tax	60	54	70	71	72
<b>Capital Employed</b>	<b>1,004</b>	<b>1,092</b>	<b>1,244</b>	<b>1,325</b>	<b>1,331</b>
Gross Fixed Assets	679	789	1,009	1,150	1,260
Less: Depreciation	299	334	382	437	499
<b>Net Fixed Assets</b>	<b>380</b>	<b>455</b>	<b>626</b>	<b>713</b>	<b>761</b>
Capital WIP	192	228	143	113	133
Investments	313	214	186	196	196
Goodwill	5	0	0	0	0
Cash & Bank Balance	10	16	15	58	6
Inventory	285	411	549	588	553
Debtors	48	56	77	113	104
Loans & Advances	119	152	234	230	230
Other assets	11	15	15	15	15
<b>Curr. Assets, I &amp; Adv.</b>	<b>332</b>	<b>352</b>	<b>532</b>	<b>568</b>	<b>535</b>
Liabilities	332	352	532	568	535
Provisions	27	104	69	133	133
<b>Net Current Assets</b>	<b>114</b>	<b>195</b>	<b>288</b>	<b>303</b>	<b>241</b>
<b>Application of Funds</b>	<b>1,004</b>	<b>1,092</b>	<b>1,244</b>	<b>1,325</b>	<b>1,331</b>

E: MOSL Estimates

Ratios					
Y/E March	2009	2010	2011	2012E	2013E
<b>Basic (Rs)</b>					
Adj. EPS	10.7	44.1	32.3	29.1	32.6
Reported EPS	10.7	44.1	32.3	3.7	32.6
Cash EPS	23.8	58.8	52.6	51.7	58.2
Book Value	187.4	216.1	237.1	240.9	263.0
Dividend	7.5	13.0	9.5	0.0	9.0
<b>Valuation (x)</b>					
P/E			8.6	9.5	8.5
Cash P/E			5.3	5.3	4.7
EV / EBITDA			9.1	6.2	5.9
EV / Sales			0.4	0.3	0.3
Price / Book Value			1.2	1.1	1.0
Dividend Yield (%)			3.4	0.0	3.3
<b>Profitability Ratios (%)</b>					
RoE	5.8	21.9	14.2	12.2	13.0
RoCE	8.2	16.0	11.2	12.8	12.4
<b>Turnover Ratios</b>					
Debtors (No. of Days)	6.4	7.6	7.9	8.4	10.5
Asset Turnover (x)	4.4	3.4	3.4	3.8	3.1
<b>Leverage Ratio</b>					
Debt / Equity (x)	1.0	0.9	1.0	1.1	0.9

Cash Flow Statement					
(INR Billion)					
Y/E March	2009	2010	2011	2012E	2013E
OP/(Loss) before Tax	36	150	101	46	119
Depreciation	33	36	50	55	62
Interest Paid	42	17	30	57	46
Direct Taxes Paid	-10	-27	-40	-32	-35
(Inc)/Dec in Wkg. Cap	94	-182	-50	27	11
Oil Bonds	-404	0	0	0	0
Other op activities	-6	-10	-20	0	0
<b>CF from Op. Activity</b>	<b>-214</b>	<b>-16</b>	<b>71</b>	<b>153</b>	<b>203</b>
(Inc)/Dec in FA & CWI	-133	-138	-137	-111	-131
(Pur)/Sale of Investrn	316	174	54	-9	0
<b>CF from Inv. Activity</b>	<b>183</b>	<b>36</b>	<b>-83</b>	<b>-120</b>	<b>-131</b>
Inc / (Dec) in Debt	85	21	84	66	-52
Dividends Paid	-10	-11	-38	0	-26
Interest Paid	-46	-24	-33	-57	-46
<b>CF from Fin. Activity</b>	<b>29</b>	<b>-14</b>	<b>12</b>	<b>9</b>	<b>-124</b>
<b>Inc / ( Dec) in Cash</b>					
Add: Opening Balanc	11	10	16	15	58
<b>Closing Balance</b>	<b>10</b>	<b>16</b>	<b>15</b>	<b>58</b>	<b>6</b>

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### Indian Oil Corporation

- |   |    |
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| 2. Group/Directors ownership of the stock               | No |
| 3. Broking relationship with company covered            | No |
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