

Nat Resources & Energy
Oil & Gas
Equity – India

India Petroleum Insight

May 2012 – Further distortion in fuel pricing

- ▶ **Petrol price hike of INR7.60/litre is not only higher than the current loss but makes it c80% costlier than diesel in India**
- ▶ **Petrochemical margins have inched up despite weak global sentiment**
- ▶ **Fuel oil spreads have inched higher partly on the assumption that Saudi will use fuel oil internally and supply higher quantity of crude to offset lower Iranian exports**

24 May 2012

Kumar Manish*

Analyst
HSBC Securities and Capital Markets
(India) Private Limited
+91 22 2268 1238
kmanish@hsbc.co.in

Puneet Gulati*, CFA

Analyst
HSBC Securities and Capital Markets
(India) Private Limited
+91 22 2268 1235
puneetgulati@hsbc.co.in

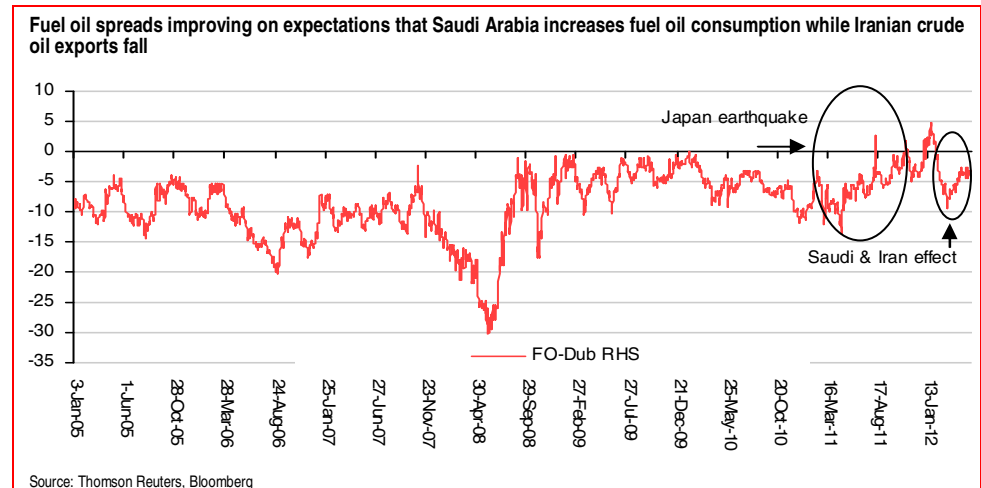
View HSBC Global Research at:
<http://www.research.hsbc.com>

*Employed by a non-US affiliate of HSBC Securities (USA) Inc, and is not registered/qualified pursuant to FINRA regulations

Issuer of report: HSBC Securities and Capital Markets
(India) Private Limited

Disclaimer & Disclosures

This report must be read with the disclosures and the analyst certifications in the Disclosure appendix, and with the Disclaimer, which forms part of it

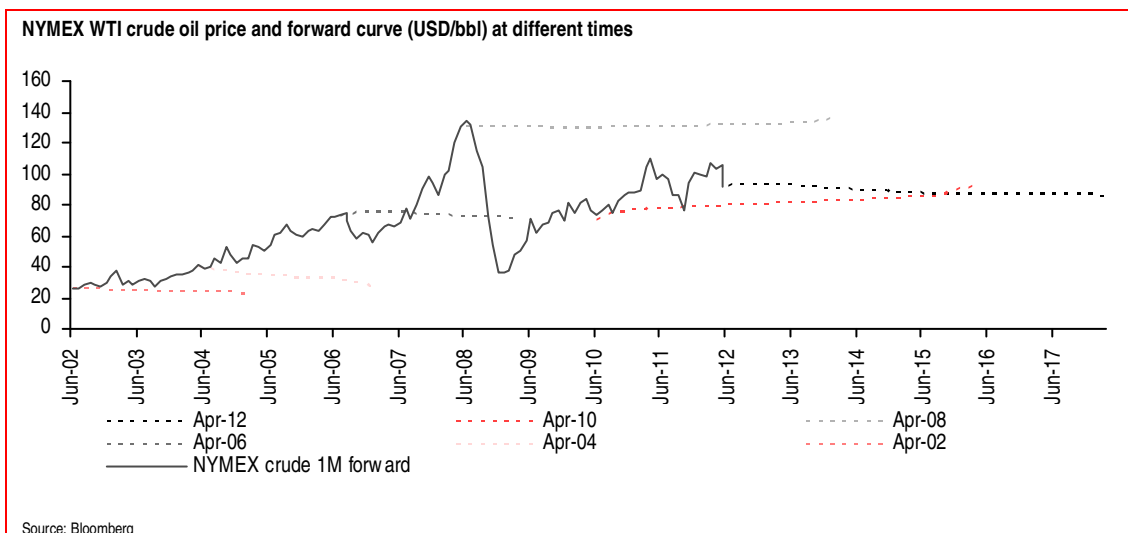
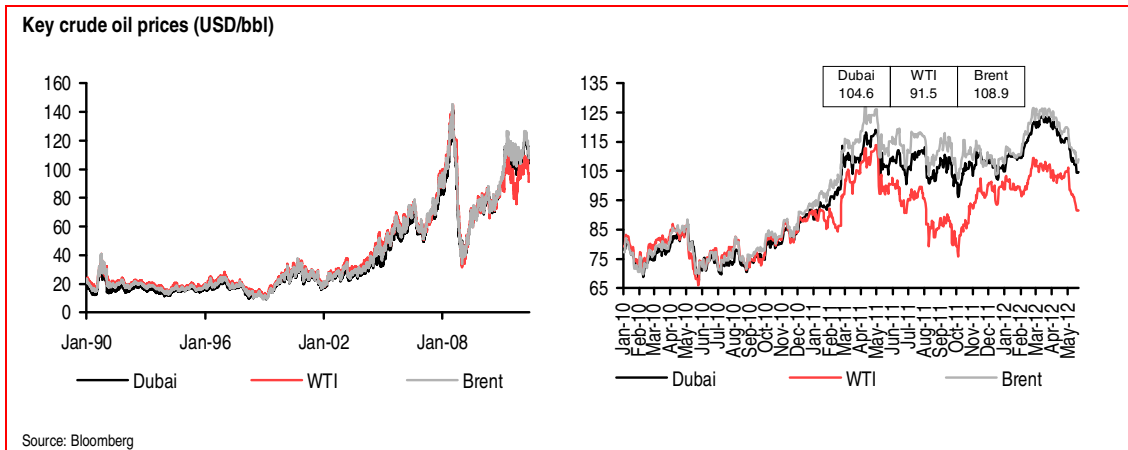


Key data points to watch

Particulars	Current	Apr'12	Mar'12	Apr'11
Brent Oil price (USD/bbl) ▼	107.6	120.8	125.1	123.3
Singapore Reuters Complex Refining Margin (USD/bbl) ▼	7.1	7.84	5.71	8.41
Arab Light – Arab Heavy (USD/bbl) ▼	3.3	3.50	2.40	4.54
Brent-Dubai (USD/bbl) ▲	5.1	3.10	2.86	7.71
Gasoline – Dubai crude oil spread (USD/bbl) ▼	11.0	18.54	15.13	15.33
Diesel – Dubai crude oil spread (USD/bbl) ▲	15.5	13.08	11.62	19.91
PE – Naphtha (USD/tonne) ▲		385	346	344
PP – Naphtha (USD/tonne) ▲		425	361	584
PSF – Naphtha (USD/tonne) ▼		525	527	989
Rig Count ▼		3,298	3,663	3,103
Particulars (March)		Mar'12	Feb'12	Mar'11
India domestic petrol sales (kbpd) ▲		388	359	348
India domestic diesel sales (kbpd) ▲		1,465	1,423	1,328
India crude oil production (kbpd) ▲		761	757	784
India natural gas production (mmscmd) ~		124	124	138

Source: Bloomberg, MoPNG, Thomson Reuters, HSBC estimates

Crude oil trend



Oil price indicators

Bullish ▲

US approved a new set of economic sanctions on Iran

Japan's 1Q GDP-prelim rose 1.0% q-o-q (Prior: 0.0%) - Japan's March Industrial production-final rose 14.2% y-o-y (Prior: 13.9%)

Libya is nearing its pre-conflict production of 1.6mmbbl/d but the new leadership struggles to impose order in the country. Increasing insecurity and disruptions delaying foreign expertise and investment as well as threatening oil output

Bearish ▼

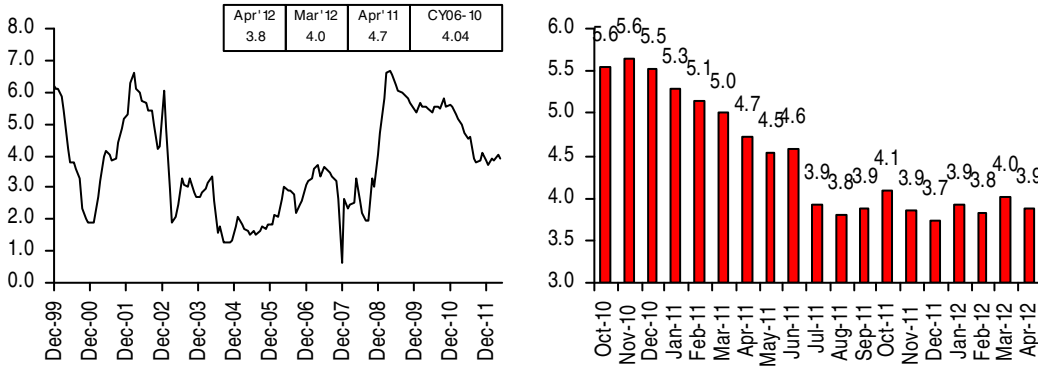
Greece will hold new elections after politicians failed to form a government following elections earlier this month, prolonging political uncertainty

US Crude inventories rose yet again in the eighth straight week by 2.1mmbbl, in line with consensus on increased stockpiles in Cushing and Oklahoma. Imports were down by 86mmbbl/d while production was slightly up by 13mmbbl/d (+8.8% y-o-y on a 4W average)

China's apparent middle distillate demand for April was down 0.3% y-o-y. China's gasoline demand shows a 6.8% y-o-y decline after adjusting for changes in refining inventory.

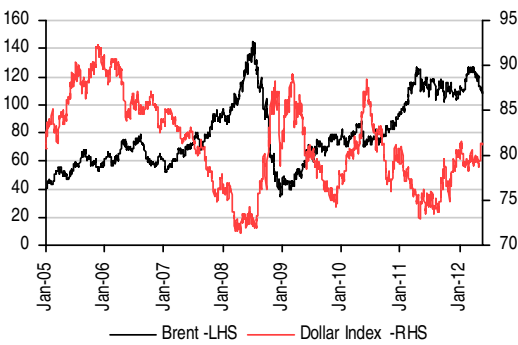
Source: HSBC, Thomson Reuters, Upstreamonline

OPEC surplus capacity



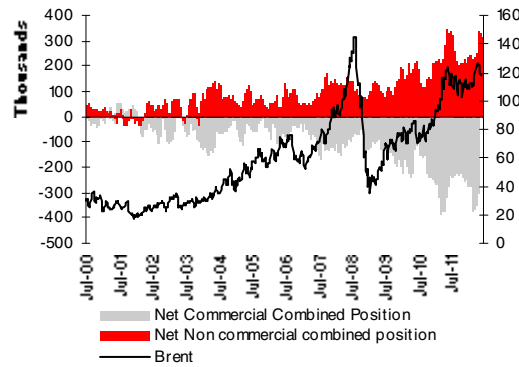
Source: Bloomberg. Note: Calculation of OPEC surplus capacity from Feb'11 excludes Libya

Brent price(USD/bbl) and dollar index continue to have negative correlation



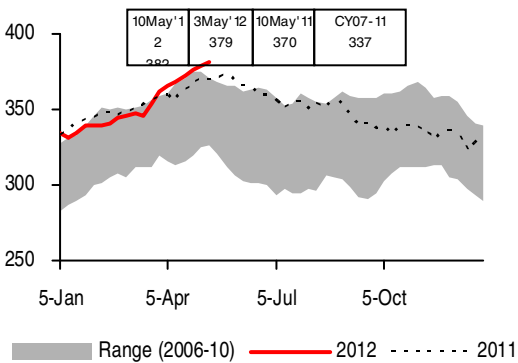
Source: Bloomberg

Net long combined non-commercial positions in crude oil slowly inched down



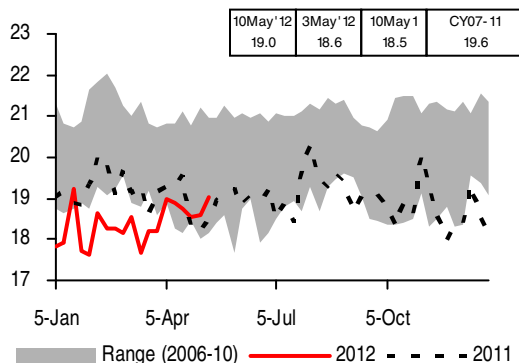
Source: CFTC

US total crude oil inventory (mn bbl) at all time peak



Source: DOE, Bloomberg

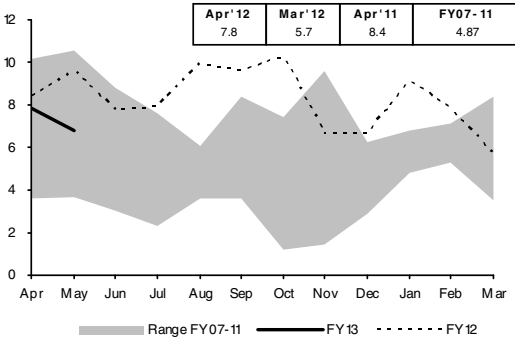
US total product demand (mbpd) rises but still below 2011 levels



Source: DOE, Bloomberg

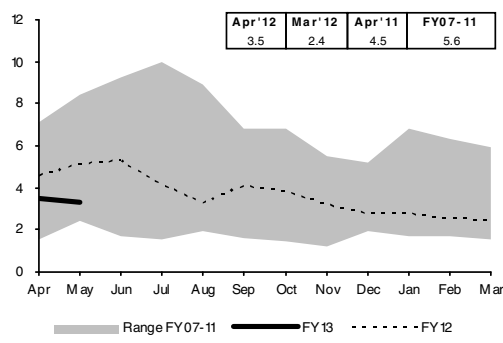
Refining margins

Reuters Singapore Complex GRM (USD/bbl) (Dubai cracking) below FY12 levels



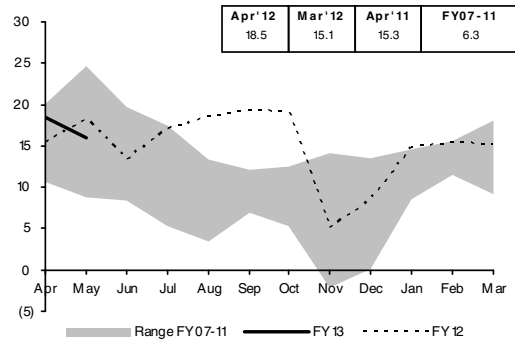
Source: Thomson Reuters. Note: May'12 till date is USD6.8/bbl

Arab Light – Arab Heavy (USD/bbl) below FY12 levels



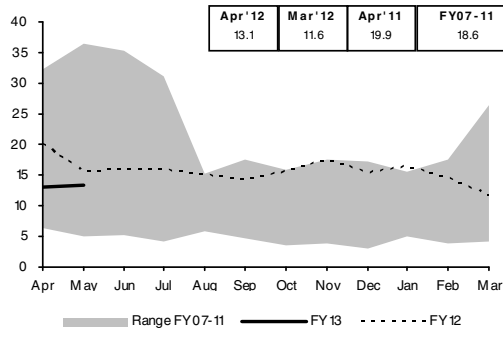
Source: Thomson Reuters. Note: May'12 till date is USD3.3/bbl

Petrol – Dubai crack spread (USD/bbl) declining a bit



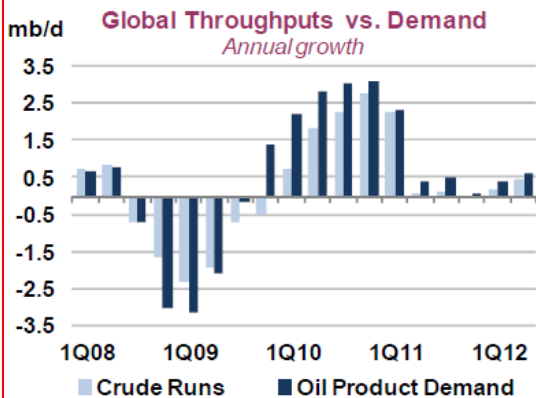
Source: Bloomberg. Note: May'12 till date is USD15.95/bbl

Diesel – Dubai crack spread (USD/bbl) below FY12 levels



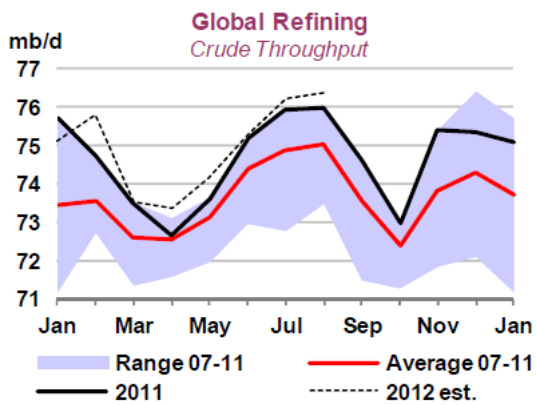
Source: Bloomberg. Note: May'12 till date is USD13.3/bbl

Global throughputs growth expected to grow at a lower rate due to weak demand



Source: IEA, HSBC

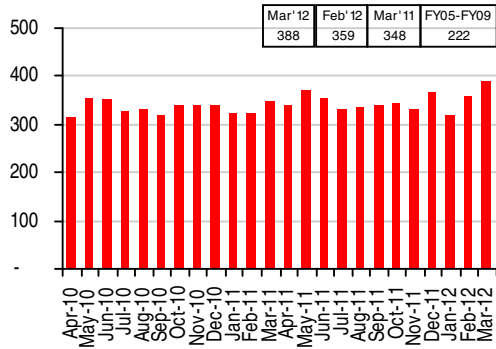
Global refining throughput expected to rise in July



Source: IEA, HSBC

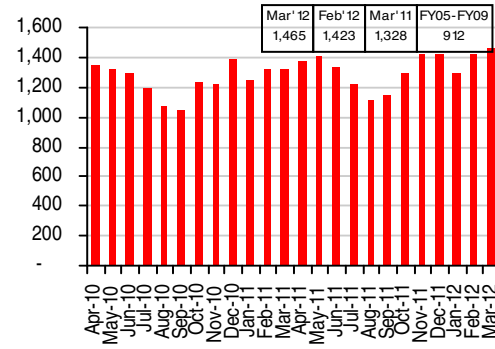
Product demand – India, China & US

INDIA domestic petrol sales (kbpd) rises 11.5% y-o-y as inventory levels were high on expectations of price hike



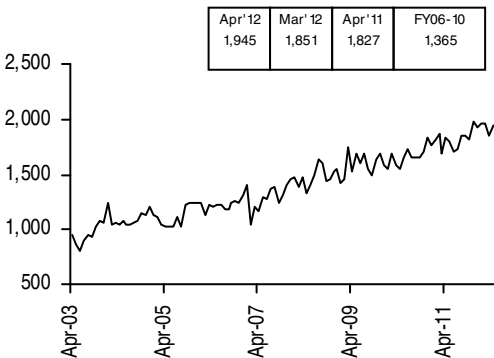
Source: MoPNG, HSBC estimates

INDIA domestic diesel sales (kbpd) rise 10.3% y-o-y as diesel continues to remain cheaper fuel compared to others



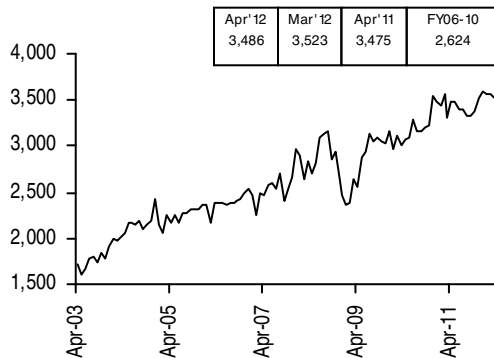
Source: MoPNG, HSBC estimates

CHINA domestic petrol demand (kbpd) growth was up 6.4% y-o- but after adjusting for refining inventory was down 6.8%yoy



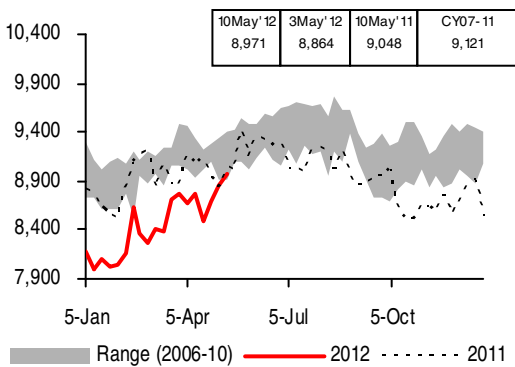
Source: Reuters, HSBC estimates

CHINA domestic diesel demand (kbpd) growth was flat 0.3% y-o-y for April '12



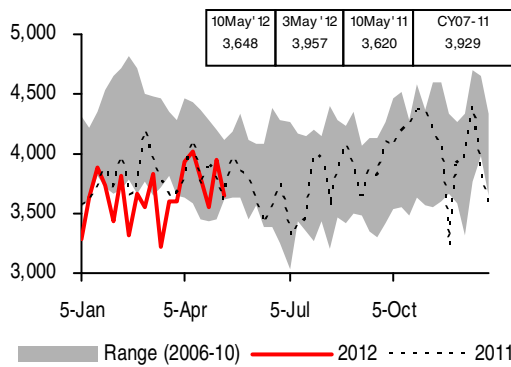
Source: Reuters, HSBC estimates

US total motor gasoline demand rises sharply but still below 2011



Source: Bloomberg, DOE

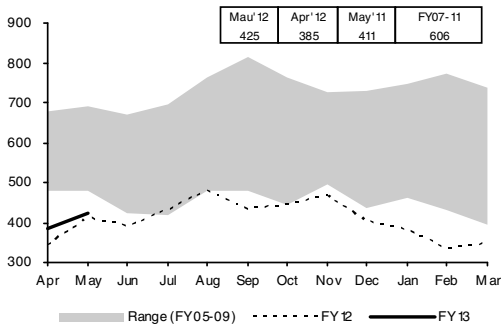
US total distillate demand (kbpd) continues to show high volatility



Source: Bloomberg, DOE

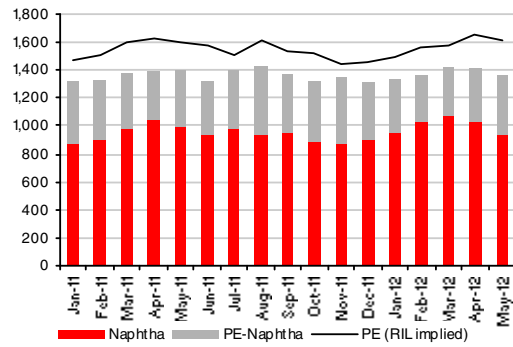
International petrochemical margins

Polyethylene – Naphtha (USD/tonne) remains weak



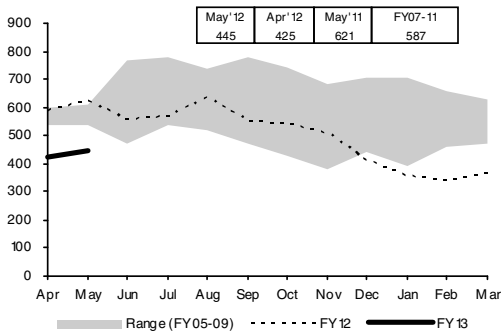
Source: CMAI, HSBC estimates

RIL (derived) selling price vs international price and spread



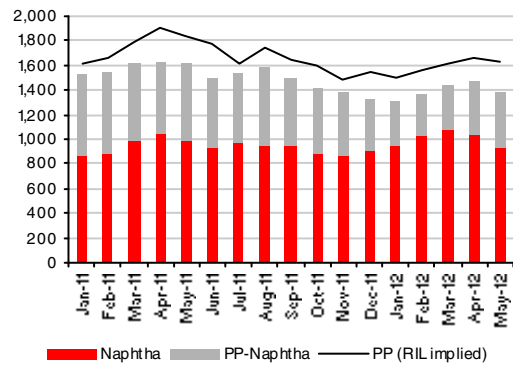
Source: CMAI, HSBC estimates, Note: May12 till date

Polypropylene – Naphtha (USD/tonne) below FY12 levels and 5 year average



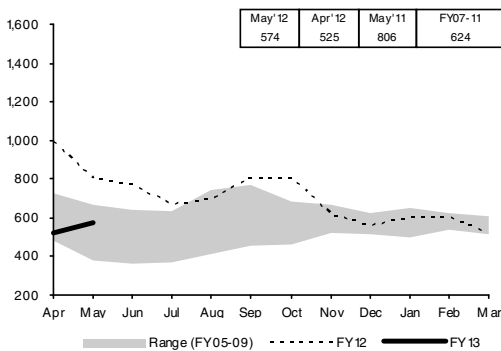
Source: CMAI, HSBC estimates

RIL (derived) selling price vs international price and spread



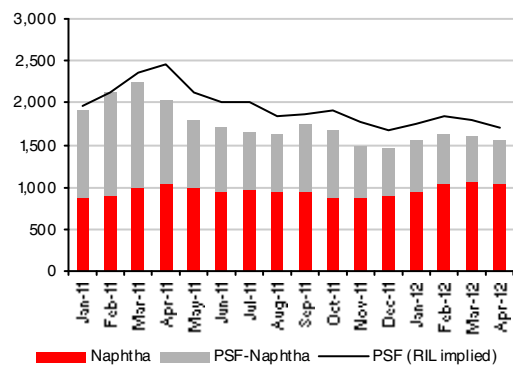
Source: CMAI, HSBC estimates, Note: May12 till date

PSF – Naphtha (USD/tonne stable but below FY12 levels)



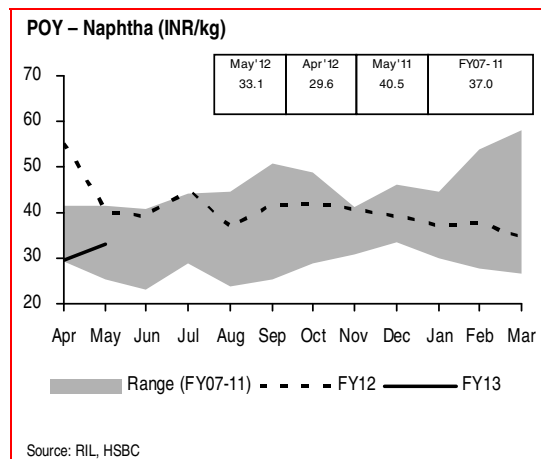
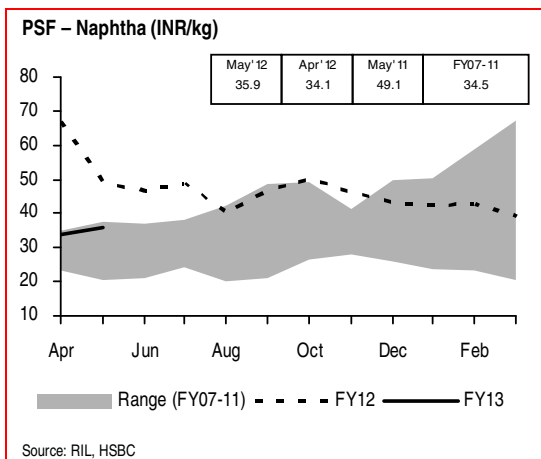
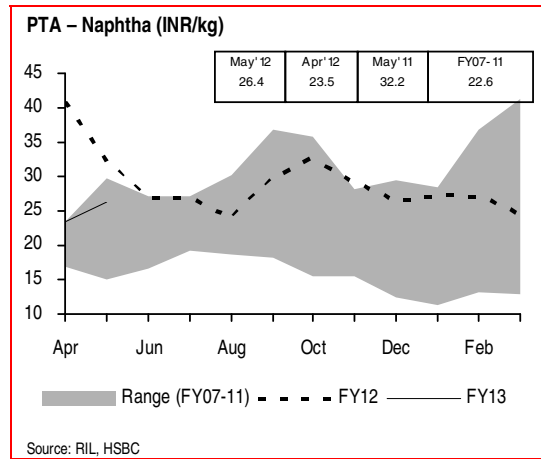
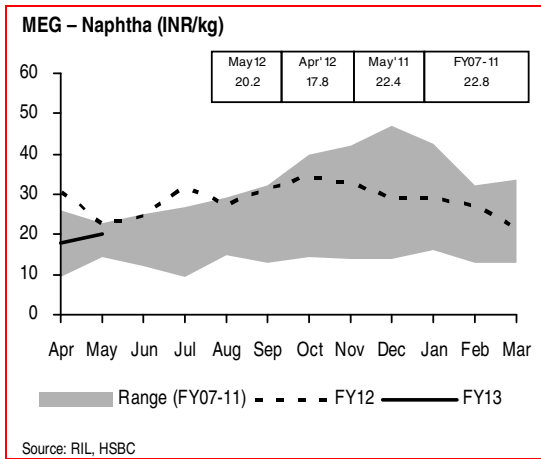
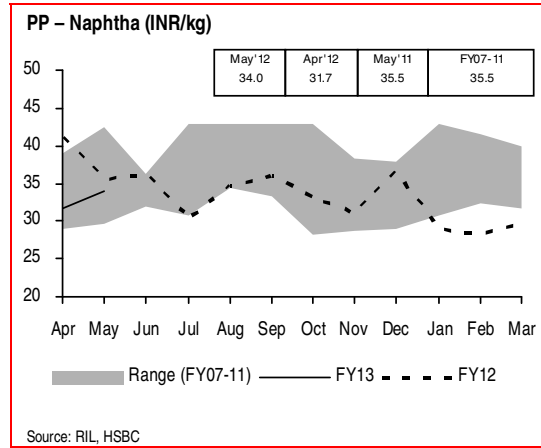
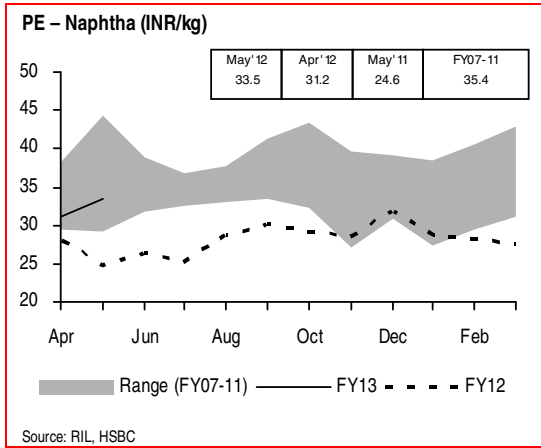
Source: CMAI, HSBC estimates Note: PSF=Polyester Staple Fibre

RIL (derived) selling price vs. international price and spread



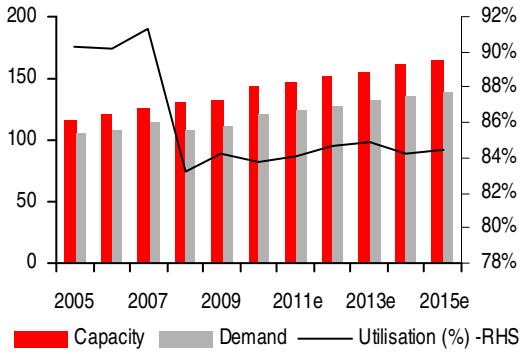
Source: CMAI, HSBC estimates, Note: Apr12 till date

Indian petrochemical margins



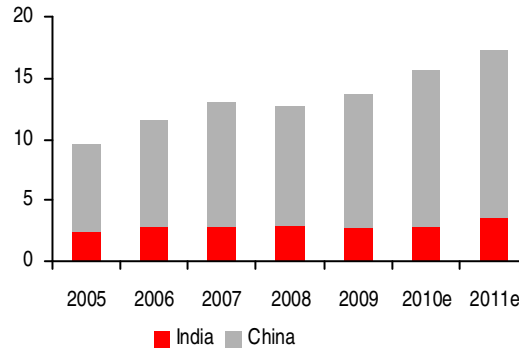
Petrochemical capacity & demand

Ethylene global demand supply (mn metric tonnes)



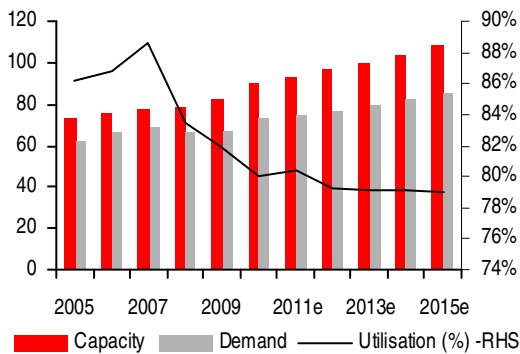
Source: CMAI, HSBC estimates

Ethylene domestic demand (mn metric tonnes)



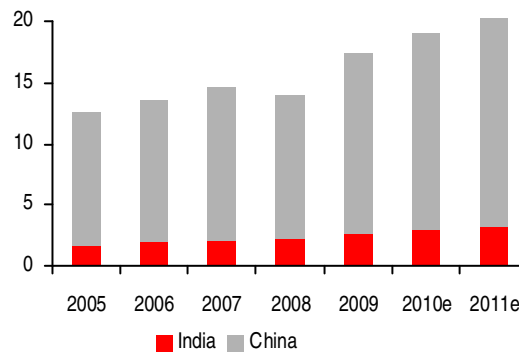
Source: CMAI, HSBC estimates

Polyethylene global demand supply (mn metric tonnes)



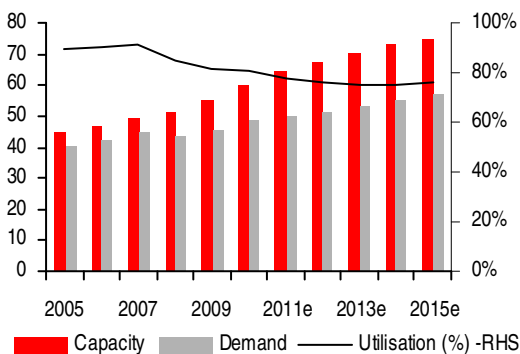
Source: CMAI, HSBC estimates

Polyethylene domestic demand (mn metric tonnes)



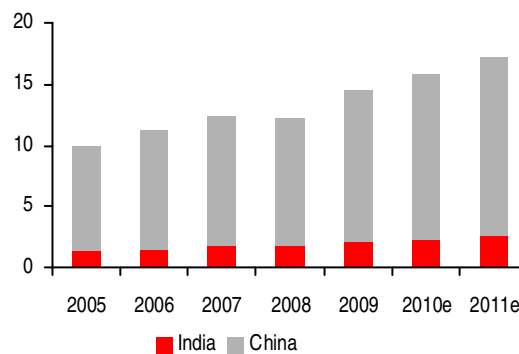
Source: CMAI, HSBC estimates

Polypropylene global demand supply (mn metric tonnes)



Source: CMAI, HSBC estimates

Polypropylene domestic demand (mn metric tonnes)



Source: CMAI, HSBC estimates

India under-recovery & inflation

Sensitivity of crude price and exchange rate to under-recovery for FY13 (INR bn)

INR/USD exchange rate	Brent price (USD/bbl)				
	80	90	100	110	120
48	184	313	665	1,017	1,367
50	209	446	813	1,179	1,546
52	235	579	960	1,341	1,723
54	316	712	1,108	1,504	1,900
56	435	845	1,255	1,666	2,099

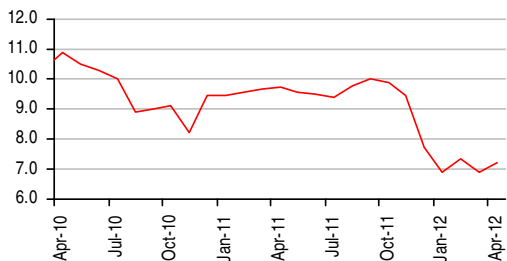
Source: HSBC estimates. Note: retail price increase will reduce the under-recovery. Note: When there is no under-recovery on either petrol or diesel, we ignore the profit made on the two products

Price increase required for NIL under-recovery (based on crude oil price of USD107.6bbl and INR/USD56 exchange rate)

Petroleum products	Units	Under-recovery	Price increase	Price increase in %
Diesel	INR/litre	11.79	13.3	32%
Petrol	INR/litre	-3.23	-3.90	-5%
LPG	INR/cylinder	318	318	80%
kerosene	INR/litre	30.0	31.0	200%

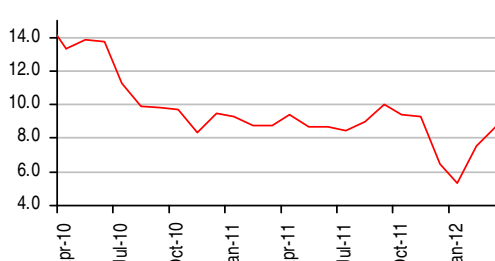
Source: HSBC estimates. Price increase based on Delhi taxes

Inflation (WPI, %)



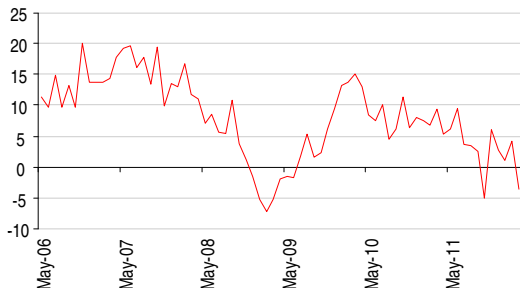
Source: HSBC

Inflation (CPI, %)



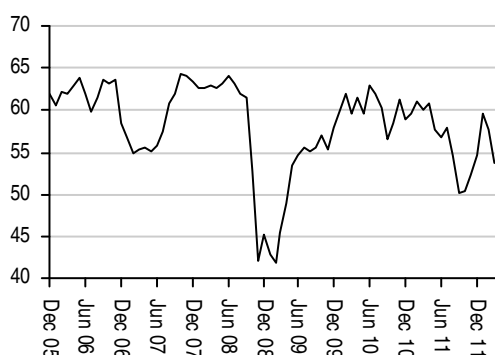
Source: HSBC

India Index of Industrial production in negative territory again



Source: HSBC

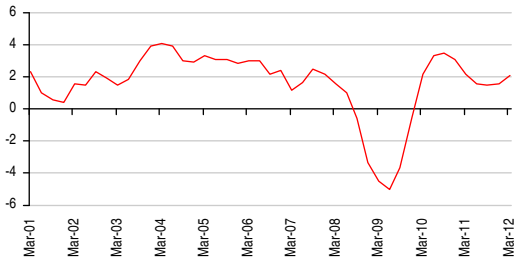
India Composite PMI stays stable m-o-m



Source: HSBC

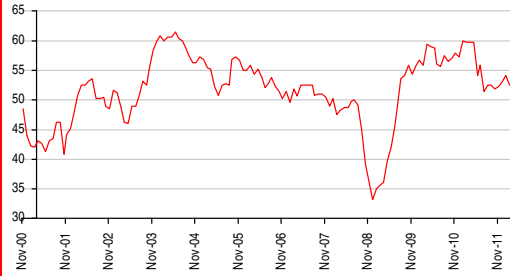
US economic indicators

US GDP growth slightly rises over previous quarter



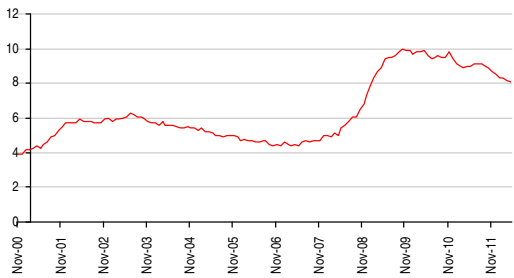
Source: Bloomberg

US ISM Manufacturing index improves m-o-m



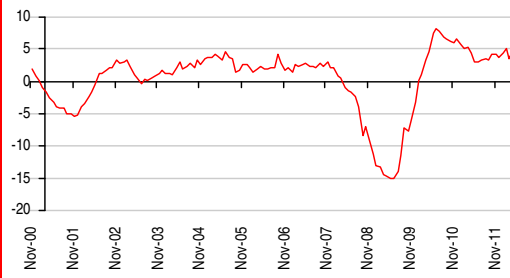
Source: Bloomberg

US unemployment rate slightly falls m-o-m at 8.1%



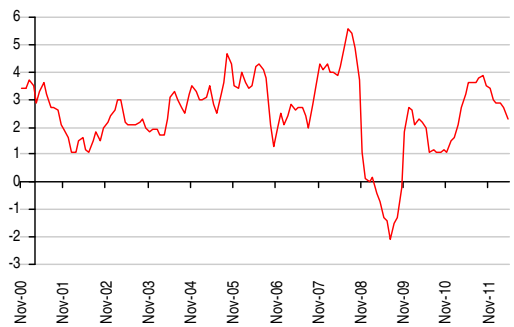
Source: Bloomberg

US industrial production slightly improves



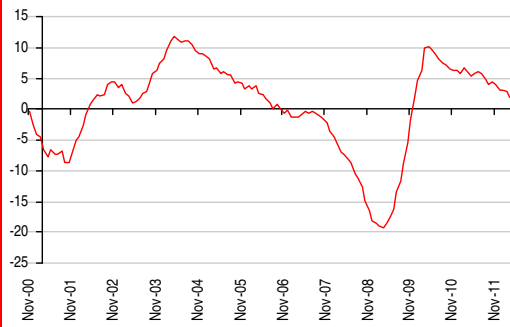
Source: Bloomberg

US CPI urban consumers declines m-o-m



Source: Bloomberg

US Leading economic indicators index declines m-o-m



Source: Bloomberg

Event calendar for May/June 2012 period

Monday	Tuesday	Wednesday	Thursday	Friday	Saturday	Sunday
21	22	23 EIA Crude oil Inventory data	24 GSPL Q4	25 BPCL Q4	26	27
28 OIL India Q4 IOC Q4	29 ONGC Q4 HPCL Q4	30 GAIL Q4 ONGC Analyst Meet EIA Crude oil Inventory data	31 GAIL Analyst Meet	1 June	2	3
4	5	6 EIA Crude oil Inventory data	7	8	9	10
11	12	13 IEA – Oil Market Report EIA Crude oil Inventory data	14	15	16	17
18	19	20 EIA Crude oil Inventory data	21	22	23	24

Source: Company, Bloomberg, HSBC

Disclosure appendix

Analyst Certification

The following analyst(s), economist(s), and/or strategist(s) who is(are) primarily responsible for this report, certifies(y) that the opinion(s) on the subject security(ies) or issuer(s) and/or any other views or forecasts expressed herein accurately reflect their personal view(s) and that no part of their compensation was, is or will be directly or indirectly related to the specific recommendation(s) or views contained in this research report: Kumar Manish and Puneet Gulati

Important disclosures

Stock ratings and basis for financial analysis

HSBC believes that investors utilise various disciplines and investment horizons when making investment decisions, which depend largely on individual circumstances such as the investor's existing holdings, risk tolerance and other considerations. Given these differences, HSBC has two principal aims in its equity research: 1) to identify long-term investment opportunities based on particular themes or ideas that may affect the future earnings or cash flows of companies on a 12 month time horizon; and 2) from time to time to identify short-term investment opportunities that are derived from fundamental, quantitative, technical or event-driven techniques on a 0-3 month time horizon and which may differ from our long-term investment rating. HSBC has assigned ratings for its long-term investment opportunities as described below.

This report addresses only the long-term investment opportunities of the companies referred to in the report. As and when HSBC publishes a short-term trading idea the stocks to which these relate are identified on the website at www.hsbcnet.com/research. Details of these short-term investment opportunities can be found under the Reports section of this website.

HSBC believes an investor's decision to buy or sell a stock should depend on individual circumstances such as the investor's existing holdings and other considerations. Different securities firms use a variety of ratings terms as well as different rating systems to describe their recommendations. Investors should carefully read the definitions of the ratings used in each research report. In addition, because research reports contain more complete information concerning the analysts' views, investors should carefully read the entire research report and should not infer its contents from the rating. In any case, ratings should not be used or relied on in isolation as investment advice.

Rating definitions for long-term investment opportunities

Stock ratings

HSBC assigns ratings to its stocks in this sector on the following basis:

For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The price target for a stock represents the value the analyst expects the stock to reach over our performance horizon. The performance horizon is 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, must exceed the required return by at least 5 percentage points over the next 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock must be expected to underperform its required return by at least 5 percentage points over the next 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands are classified as Neutral.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation of coverage, change of volatility status or change in price target). Notwithstanding this, and although ratings are subject to ongoing management review, expected returns will be permitted to move outside the bands as a result of normal share price fluctuations without necessarily triggering a rating change.

*A stock will be classified as volatile if its historical volatility has exceeded 40%, if the stock has been listed for less than 12 months (unless it is in an industry or sector where volatility is low) or if the analyst expects significant volatility. However, stocks which we do not consider volatile may in fact also behave in such a way. Historical volatility is defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility has to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Rating distribution for long-term investment opportunities

As of 24 May 2012, the distribution of all ratings published is as follows:

Overweight (Buy)	49%	(26% of these provided with Investment Banking Services)
Neutral (Hold)	37%	(25% of these provided with Investment Banking Services)
Underweight (Sell)	14%	(16% of these provided with Investment Banking Services)

Analysts, economists, and strategists are paid in part by reference to the profitability of HSBC which includes investment banking revenues.

For disclosures in respect of any company mentioned in this report, please see the most recently published report on that company available at www.hsbcnet.com/research.

* *HSBC Legal Entities are listed in the Disclaimer below.*

Additional disclosures

- 1 This report is dated as at 24 May 2012.
- 2 All market data included in this report are dated as at close 23 May 2012, unless otherwise indicated in the report.
- 3 HSBC has procedures in place to identify and manage any potential conflicts of interest that arise in connection with its Research business. HSBC's analysts and its other staff who are involved in the preparation and dissemination of Research operate and have a management reporting line independent of HSBC's Investment Banking business. Information Barrier procedures are in place between the Investment Banking and Research businesses to ensure that any confidential and/or price sensitive information is handled in an appropriate manner.

Disclaimer

** Legal entities as at 04 March 2011*

'UAE' HSBC Bank Middle East Limited, Dubai; 'HK' The Hongkong and Shanghai Banking Corporation Limited, Hong Kong; 'TW' HSBC Securities (Taiwan) Corporation Limited; 'CA' HSBC Securities (Canada) Inc, Toronto; HSBC Bank, Paris Branch; HSBC France; 'DE' HSBC Trinkaus & Burkhardt AG, Düsseldorf; 000 HSBC Bank (RR), Moscow; 'IN' HSBC Securities and Capital Markets (India) Private Limited, Mumbai; 'JP' HSBC Securities (Japan) Limited, Tokyo; 'EG' HSBC Securities Egypt SAE, Cairo; 'CN' HSBC Investment Bank Asia Limited, Beijing Representative Office; The Hongkong and Shanghai Banking Corporation Limited, Singapore Branch; The Hongkong and Shanghai Banking Corporation Limited, Seoul Securities Branch; The Hongkong and Shanghai Banking Corporation Limited, Seoul Branch; HSBC Securities (South Africa) (Pty) Ltd, Johannesburg; 'GR' HSBC Securities SA, Athens; HSBC Bank plc, London, Madrid, Milan, Stockholm, Tel Aviv; 'US' HSBC Securities (USA) Inc, New York; HSBC Yatirim Menkul Degerler AS, Istanbul; HSBC México, SA, Institución de Banca Múltiple, Grupo Financiero HSBC; HSBC Bank Brasil SA – Banco Múltiplo; HSBC Bank Australia Limited; HSBC Bank Argentina SA; HSBC Saudi Arabia Limited; The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch

Issuer of report

HSBC Securities and Capital Markets (India) Private Limited

Registered Office

52/60 Mahatma Gandhi Road

Fort, Mumbai 400 001, India

Telephone: +91 22 2267 4921

Fax: +91 22 2263 1983

Website: www.research.hsbc.com

This document has been issued by HSBC Securities and Capital Markets (India) Private Limited ("HSBC") for the information of its customers only. HSBC Securities and Capital Markets (India) Private Limited is regulated by the Securities and Exchange Board of India. If it is received by a customer of an affiliate of HSBC, its provision to the recipient is subject to the terms of business in place between the recipient and such affiliate. This document is not and should not be construed as an offer to sell or the solicitation of an offer to purchase or subscribe for any investment. HSBC has based this document on information obtained from sources it believes to be reliable but which it has not independently verified; HSBC makes no guarantee, representation or warranty and accepts no responsibility or liability as to its accuracy or completeness. Expressions of opinion are those of the Research Division of HSBC only and are subject to change without notice. HSBC and its affiliates and/or their officers, directors and employees may have positions in any securities mentioned in this document (or in any related investment) and may from time to time add to or dispose of any such securities (or investment). HSBC and its affiliates may act as market maker or have assumed an underwriting commitment in the securities of companies discussed in this document (or in related investments), may sell them to or buy them from customers on a principal basis and may also perform or seek to perform investment banking or underwriting services for or relating to those companies and may also be represented in the supervisory board or any other committee of those companies. The information and opinions contained within the research reports are based upon publicly available information and rates of taxation applicable at the time of publication which are subject to change from time to time. Past performance is not necessarily a guide to future performance. The value of any investment or income may go down as well as up and you may not get back the full amount invested. Where an investment is denominated in a currency other than the local currency of the recipient of the research report, changes in the exchange rates may have an adverse effect on the value, price or income of that investment. In case of investments for which there is no recognised market it may be difficult for investors to sell their investments or to obtain reliable information about its value or the extent of the risk to which it is exposed.

HSBC Securities (USA) Inc. accepts responsibility for the content of this research report prepared by its non-US foreign affiliate. All U.S. persons receiving and/or accessing this report and wishing to effect transactions in any security discussed herein should do so with HSBC Securities (USA) Inc. in the United States and not with its non-US foreign affiliate, the issuer of this report.

In the UK this report may only be distributed to persons of a kind described in Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001. The protections afforded by the UK regulatory regime are available only to those dealing with a representative of HSBC Bank plc in the UK. In Singapore, this publication is distributed by The Hongkong and Shanghai Banking Corporation Limited, Singapore Branch for the general information of institutional investors or other persons specified in Sections 274 and 304 of the Securities and Futures Act (Chapter 289) ("SFA") and accredited investors and other persons in accordance with the conditions specified in Sections 275 and 305 of the SFA. This publication is not a prospectus as defined in the SFA. It may not be further distributed in whole or in part for any purpose. The Hongkong and Shanghai Banking Corporation Limited Singapore Branch is regulated by the Monetary Authority of Singapore. Recipients in Singapore should contact a "Hongkong and Shanghai Banking Corporation Limited, Singapore Branch" representative in respect of any matters arising from, or in connection with this report. In Australia, this publication has been distributed by The Hongkong and Shanghai Banking Corporation Limited (ABN 65 117 925 970, AFSL 301737) for the general information of its "wholesale" customers (as defined in the Corporations Act 2001). Where distributed to retail customers, this research is distributed by HSBC Bank Australia Limited (AFSL No. 232595). These respective entities make no representations that the products or services mentioned in this document are available to persons in Australia or are necessarily suitable for any particular person or appropriate in accordance with local law. No consideration has been given to the particular investment objectives, financial situation or particular needs of any recipient. This publication is distributed in New Zealand by The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch.

In Japan, this publication has been distributed by HSBC Securities (Japan) Limited. In Hong Kong, this document has been distributed by The Hongkong and Shanghai Banking Corporation Limited in the conduct of its Hong Kong regulated business for the information of its institutional and professional customers; it is not intended for and should not be distributed to retail customers in Hong Kong. The Hongkong and Shanghai Banking Corporation Limited makes no representations that the products or services mentioned in this document are available to persons in Hong Kong or are necessarily suitable for any particular person or appropriate in accordance with local law. All inquiries by such recipients must be directed to The Hongkong and Shanghai Banking Corporation Limited. In Korea, this publication is distributed by The Hongkong and Shanghai Banking Corporation Limited, Seoul Securities Branch ("HBAP SLS") for the general information of professional investors specified in Article 9 of the Financial Investment Services and Capital Markets Act ("FSCMA"). This publication is not a prospectus as defined in the FSCMA. It may not be further distributed in whole or in part for any purpose. HBAP SLS is regulated by the Financial Services Commission and the Financial Supervisory Service of Korea.

© Copyright 2012, HSBC Securities and Capital Markets (India) Private Limited, ALL RIGHTS RESERVED. No part of this publication may be reproduced, stored in a retrieval system, or transmitted, in any form or by any means, electronic, mechanical, photocopying, recording, or otherwise, without the prior written permission of HSBC Securities and Capital Markets (India) Private Limited. MICA (P) 038/04/2012, MICA (P) 063/04/2012 and MICA (P) 206/01/2012