



Exploration upside in Brazil

We hosted BPCL at our investor conference in Singapore. The management indicated the possibility of further reserve accretion in Mozambique as the unexplored southern part of the block will be drilled in 2HCY12. Appraisal drilling in Barra and Wahoo in Brazil may establish reserves by mid-CY2013. The company intends to increase upstream capex from Rs8.5bn in FY12 to Rs20bn in FY14. We revise our target price upward to Rs865/share to factor in exploration upside from Brazil and upgrade our rating to BUY.

Mozambique may see further resource upgrades: Only the northern part of the block has been drilled until date. The Barracuda and Black Pearl prospects in the southern part of the block are scheduled for drilling in 2HCY12-1HCY13. Success in any of these wells would substantially increase recoverable reserve estimates that are at 30-60TCF currently.

Commerciality of Brazil discoveries to be known by mid-2013: Appraisal drilling in the 'Barra' discovery (34m net pay) with Petrobras is scheduled over 2HCY12-1HCY13. BPCL expects to have the estimates for recoverable reserve by mid-CY2013. Two appraisal wells at Wahoo scheduled in CY2012 will determine commerciality of the discovery. If the wells are found commercial, the first oil from Wahoo could come in 2017, ahead of the first gas from Mozambique.

Revise target price by 12%, recommend BUY: Exploratory and appraisal drilling is scheduled to accelerate with 10 new wells each in Mozambique and Brazil in FY13. BPCL's capex is scheduled to increase from Rs8.5bn in FY12 to Rs15bn in FY13 and Rs20bn in FY14. We value BPCL's stake in Mozambique at Rs227/share. Wahoo would contribute Rs36/share based on current estimates of recoverable resources. We note that BORL is expected to contribute 12% of BPCL's consolidated Ebitda in FY13. We revise our target price upward to Rs865/share to factor in higher recoverable reserve estimate from Mozambique and introduce exploratory upside from Brazil. Recommend BUY.

Company update

CMP	Rs751
12-mth TP (Rs)	865 (15%)
Market cap (US\$m)	4,853
Enterprise value(US\$m)	9,688
Bloomberg	BPCL IN
Sector	Oil & Gas

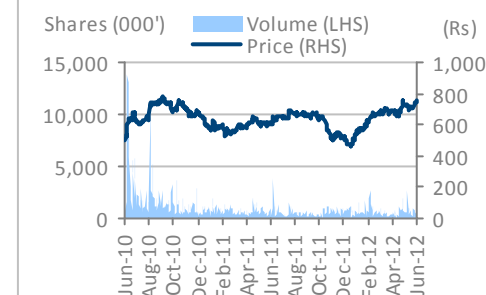
Shareholding pattern (%)

Promoter	54.9
FII	7.9
DII	19.6
Others	17.5
52Wk High/Low (Rs)	797/458
Shares o/s (m)	362
Daily volume (US\$ m)	7.5
Dividend yield FY13ii (%)	1.0
Free float (%)	45.1

Price performance (%)

	1M	3M	1Y
Absolute (Rs)	3.6	12.9	19.1
Absolute (US\$)	3.5	1.3	-1.7
Rel. to Sensex	-0.7	15.3	24.7
Cagr (%)		3 yrs	5 yrs
EPS		7.2	-18.3

Stock performance



Financial summary (Rs m)

Y/e 31 Mar, Consolidated	FY11A	FY12A	FY13ii	FY14ii	FY15ii
Revenues (Rs m)	1,536,450	2,119,638	2,125,611	2,344,774	2,531,247
EBITDA margins (%)	2.8	2.2	2.3	3.0	2.7
Pre-exceptional PAT (Rs m)	16,350	7,808	9,414	18,975	17,635
Reported PAT (Rs m)	16,350	7,808	9,414	18,975	17,635
Pre-exceptional EPS (Rs)	45.2	21.6	26.0	52.5	48.8
Growth (%)	0.2	(52.2)	20.6	101.6	(7.1)
IIFL vs consensus (%)			(40.5)	2.0	(16.2)
PER (x)	16.6	34.8	28.8	14.3	15.4
ROE (%)	11.1	5.0	5.8	11.0	9.5
Net debt/equity (x)	1.6	1.7	1.5	1.5	1.5
EV/EBITDA (x)	12.1	11.7	10.8	7.8	7.8
Price/book (x)	1.8	1.7	1.6	1.5	1.4

Source: Company, IIFL Research. Priced as on 19 June 2012

Resource estimate in Mozambique conservative: BPRL indicated that the consortium drilled 14 wells in the block with 12 hydrocarbon shows, based on which it arrived at the current reserve estimate of 30-60TCF. ENI, that is exploring the adjacent block, has announced reserve estimate of 47-52TCF based on only three exploratory wells. The consortium’s estimate in Mozambique is more concrete.

US\$14bn capex for first gas from Mozambique: The operator estimates that US\$8bn-9bn will be spent on development and US\$6bn for another LNG train. The total capex for development and the first LNG train is US\$14bn-15bn, which would be funded via equity and debt by the consortium members. The second LNG train will be funded from cash flows generated by the first train starting CY2018.

Barra reserve estimate by mid-CY2013: Two appraisal wells are scheduled to be drilled in this promising block in late CY2012. BPRL indicated that recoverable reserve estimates will be ready by mid-CY2013.

Further, appraisal drilling in two locations in BM-C-30 in the Campos basin will determine the commerciality of the block by mid-CY2013. First oil from the block may flow by CY2017 as it is relatively an easier development compared with Mozambique.

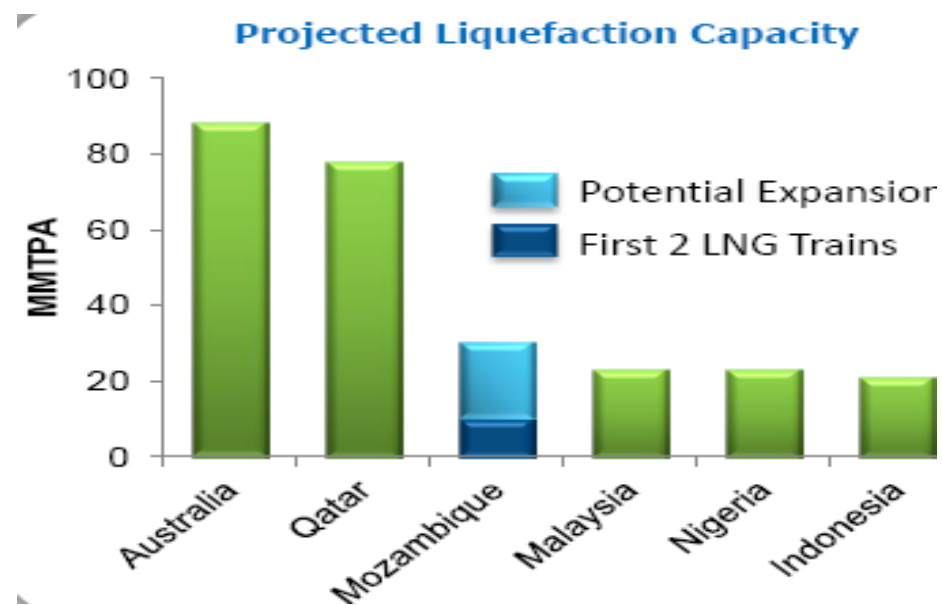
Upgrade to BUY with 15% upside: We see BPCL’s current price discounting 45TCF from Mozambique. Given likely acceleration in news flow from Brazil over FY13 and the possibility of reserve upgrade in Mozambique, we expect the stock to continue to outperform the Sensex over our target horizon. We upgrade BPCL to BUY with a target price Rs865.

Figure 1: SOTP valuation for BPCL – PT revised by 12% to Rs865/share

Valuation summary	Rs/share	Comment
Refining & Marketing	439	Valued using P/B multiple of 1x
E&P	262	Mozambique: 10% of 45TCF @ \$2.5/boe, Wahoo: 200mmbbls @ \$14/bbl
Bina refinery	50	Equity invested
Investments	57	P-LNG, Oil India & Indraprastha Gas valued @20% discount to CMP
Treasury stock	55	Valued @20% discount to CMP
Equity value	865	

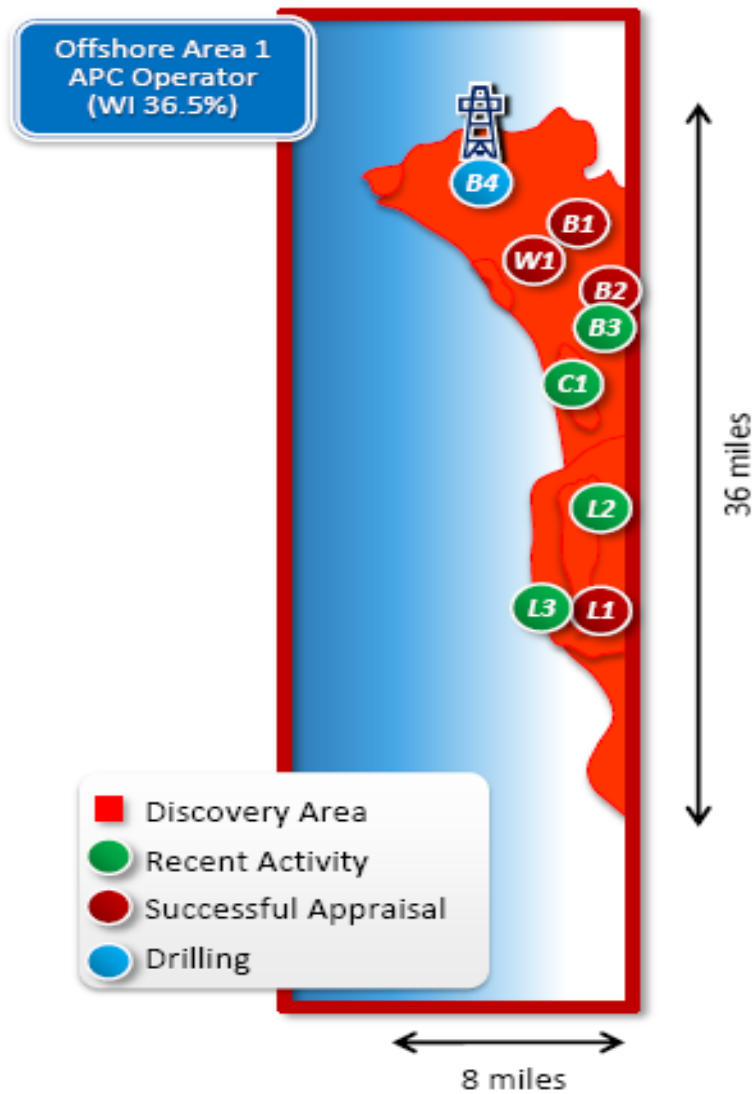
Source: Company, IIFL Research

Figure 2: 2 LNG trains of 5MTPA planned initially, expandable by four further trains



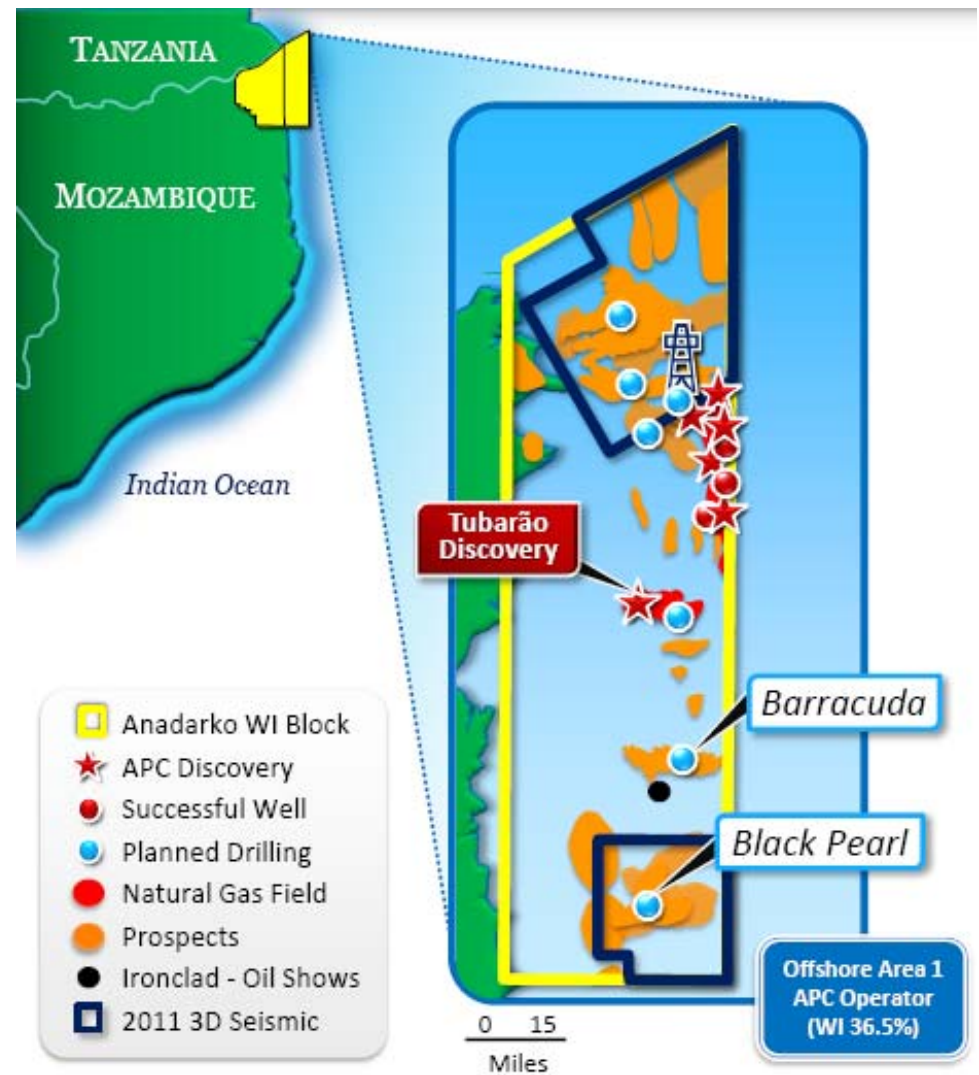
Source: Anandarko, IIFL Research

Figure 3: Snapshot of discoveries in the Mozambique block



Source: Anadarko, IIFL Research

Figure 4: Drilling in wells Barracuda and Black Pearl in 2H CY12 onwards may result in further reserve upsides



Source: Anadarko, IIFL Research

Assumptions

Y/e 31 Mar, Consolidated	FY11A	FY12A	FY13ii	FY14ii	FY15ii
Crude price (\$/bbl)	86.5	114.0	100.0	102.0	102.0
Under-recoveries (Rs bn)	782.0	1,385.0	1,445.0	1,615.4	1,813.2
Downstream share (%)	8.9	0.0	0.0	0.0	0.0
Crude processed (mmt)	21.7	22.9	23.1	23.1	23.1
Market sales (mmt)	31.9	34.6	36.0	37.5	37.5
Gross Refining Margin (\$/bbl)	4.5	3.2	3.6	4.0	4.0
USD/INR exchange rate	45.6	48.3	54.0	54.0	54.0

Source: Company data, IIFL Research

Financial summary

Income statement summary (Rs m)

Y/e 31 Mar, Consolidated	FY11A	FY12A	FY13ii	FY14ii	FY15ii
Revenues	1,536,450	2,119,638	2,125,611	2,344,774	2,531,247
Ebitda	42,762	46,369	48,873	69,460	68,872
Depreciation and amortisation	(18,914)	(24,108)	(23,876)	(25,716)	(27,023)
Ebit	23,849	22,261	24,997	43,744	41,849
Non-operating income	17,103	16,324	14,823	14,823	14,824
Financial expense	(12,468)	(22,591)	(21,197)	(21,897)	(22,597)
PBT	28,483	15,994	18,623	36,670	34,076
Exceptionals	0	0	0	0	0
Reported PBT	28,483	15,994	18,623	36,670	34,076
Tax expense	(11,062)	(7,482)	(8,711)	(17,153)	(15,940)
PAT	17,421	8,513	9,912	19,517	18,137
Minorities, Associates etc.	(1,071)	(705)	(497)	(543)	(501)
Attributable PAT	16,350	7,808	9,414	18,975	17,635

Ratio analysis

Y/e 31 Mar, Consolidated	FY11A	FY12A	FY13ii	FY14ii	FY15ii
Per share data (Rs)					
Pre-exceptional Eps	45.2	21.6	26.0	52.5	48.8
DPS	16.5	13.0	7.8	15.7	15.7
BVPS	424.6	439.2	457.5	494.2	528.3
Growth ratios (%)					
Revenues	24.1	38.0	0.3	10.3	8.0
Ebitda	40.0	8.4	5.4	42.1	(0.8)
Eps	0.2	(52.2)	20.6	101.6	(7.1)
Profitability ratios (%)					
Ebitda margin	2.8	2.2	2.3	3.0	2.7
Ebit margin	1.6	1.1	1.2	1.9	1.7
Tax rate	38.8	46.8	46.8	46.8	46.8
Net profit margin	1.1	0.4	0.5	0.8	0.7
Return ratios (%)					
ROE	11.1	5.0	5.8	11.0	9.5
Roce	9.5	8.6	8.2	11.5	10.7
Solvency ratios (x)					
Net debt-equity	1.6	1.7	1.5	1.5	1.5
Net debt to Ebitda	5.7	5.8	5.2	3.9	4.1
Interest coverage	1.9	1.0	1.2	2.0	1.9

Source: Company data, IIFL Research

Balance sheet summary (Rs m)

Y/e 31 Mar, Consolidated	FY11A	FY12A	FY13ii	FY14ii	FY15ii
Cash & cash equivalents	7,971	13,263	47,496	44,503	40,915
Inventories	182,135	210,971	204,872	225,631	243,647
Receivables	28,779	52,010	48,019	52,302	56,146
Other current assets	86,421	127,761	169,102	210,442	251,782
Creditors	206,051	281,053	296,705	326,768	352,860
Other current liabilities	34,462	19,243	9,571	10,541	11,383
Net current assets	64,792	103,710	163,214	195,568	228,247
Fixed assets	278,987	290,890	267,801	269,268	269,430
Intangibles	0	0	0	0	0
Investments	84,600	75,145	65,145	55,147	45,151
Other long-term assets	33	0	0	0	0
Total net assets	428,412	469,744	496,160	519,983	542,828
Borrowings	251,855	283,816	302,816	312,816	322,816
Other long-term liabilities	23,049	27,129	27,955	28,497	28,999
Shareholders equity	153,508	158,799	165,389	178,670	191,013
Total liabilities	428,412	469,744	496,160	519,983	542,828

Cash flow summary (Rs m)

Y/e 31 Mar, Consolidated	FY11A	FY12A	FY13ii	FY14ii	FY15ii
Ebit	23,849	22,261	24,997	43,744	41,849
Tax paid	(12,762)	(7,482)	(8,711)	(17,153)	(15,940)
Depreciation and amortization	18,914	24,108	23,876	25,716	27,023
Net working capital change	13,489	(33,625)	(25,271)	(35,348)	(36,267)
Other operating items	(3,952)	(3,214)	0	0	0
Operating cash flow before interest	39,538	2,048	14,891	16,960	16,665
Financial expense	(13,967)	(22,591)	(21,197)	(21,897)	(22,597)
Non-operating income	17,103	16,324	14,823	14,823	14,824
Operating cash flow after interest	42,674	(4,218)	8,517	9,886	8,893
Capital expenditure	(46,783)	(10,097)	(26,701)	(27,184)	(27,184)
Long-term investments	32,841	9,455	10,000	9,998	9,996
Others	(29,588)	(17,116)	26,241	0	0
Free cash flow	(856)	(21,976)	18,057	(7,300)	(8,295)
Equity raising	3,854	0	0	0	0
Borrowings	4,137	31,961	19,000	10,000	10,000
Dividend	(6,449)	(4,693)	(2,824)	(5,692)	(5,291)
Net chg in cash and equivalents	686	5,293	34,232	(2,993)	(3,586)

Source: Company data, IIFL Research

Key to our recommendation structure

BUY - Absolute - Stock expected to give a positive return of over 20% over a 1-year horizon.

SELL - Absolute - Stock expected to fall by more than 10% over a 1-year horizon.

In addition, **Add** and **Reduce** recommendations are based on expected returns relative to a hurdle rate. Investment horizon for **Add** and **Reduce** recommendations is up to a year. We assume the current hurdle rate at 10%, this being the average return on a debt instrument available for investment.

Add - Stock expected to give a return of 0-10% over the hurdle rate, ie a positive return of 10%+.

Reduce - Stock expected to return less than the hurdle rate, ie return of less than 10%.

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