

ONGC

ACCUMULATE

Upward revision in gas price a key near term trigger

Summary

ONGC's Q3FY21 revenue and EBITDA was in-line with our estimates, while PAT was below our estimates on the back of higher than expected tax rate and lower other income. Oil/Gas production volume declined 3%/6% YoY to 5.6mmt/5.8bcm. Effective tax rate came at 51% while other income was also down by 13% YoY to Rs12 bn. The company is forming a 100% subsidiary for natural gas/LNG sourcing and marketing. Along with the group companies ONGC needs 2.5-4mmt of natural gas. It expects production volume from KG basin to average 3.4mmscmd in FY22 and 8.5mmscmd in FY23 and peak production of 15mmscmd to reach in FY24. We expect US\$2.6/2.8/mmbtu APM gas price for FY22E/23E and any upwards revision due to change in gas pricing formula may have an upside risk. We raise our TP upwards to Rs106 from earlier Rs85 to factor-in improved business outlook and stronger performance by its other divisions. We downgrade the stock to ACCUMULATE from earlier BUY due to significant rise in valuation since our last report.

Key Highlights and Investment Rationale

Revenue/EBITDA impacted by lower volume, realisation; in line with estimate

Revenue for the quarter fell by 28% YoY to Rs 170.2bn. This was due to lower oil and gas price realizations and lower volume. Oil/Gas production volume declined 3%/6% YoY to 5.6mmt/5.8bcm. Average oil realization was down 28% YoY to US\$43.2/bbl while Gas realization was down 44% YoY to Rs 5.2/scm. However, due to higher survey cost, effective tax rate and lower other income led to below estimate PAT in Q3FY21.

Gas price set to rise; capex/volume guidance remained unchanged

The management has indicated that formula to revise APM gas price is set to change and that would lead to higher prices. Currently we are modeling US\$2.6/2.8/mmbtu APM gas price for FY22E/23E. Further, the company expects Rs290 bn of capex to achieve in FY21 and US\$4-4.5 bn in FY22. The management has guided for oil/gas production volume of 23mmt/25bcm in FY22E from 22-22.5mmt/23bcm in FY21E.

Increase TP to Rs106; Downgrade to ACCUMULATE from BUY

We value its standalone business on PER of 7x FY23E (Rs63), OVL on PER of 10x FY23E (Rs13), KG basin on NPV (Rs7), Investments at 30% haircut (Rs24), which gives us a TP of Rs106/share from Rs85/share earlier. However, due to significant rise in valuation in last three months, we downgrade the stock to ACCUMULATE from BUY. Though, upward revision in gas price poses upside risk.

TP	Rs106		
CMP	Rs98		
Potential upside / downside	+8%		
Previous Rating	BUY		
V/s Consensus			
EPS (Rs)	FY21E	FY22E	FY23E
IDBI Capital	6.8	7.5	8.2
Consensus	8.6	14.3	17.0
% difference	(6.3)	(42.6)	(47.0)

Shareholding Pattern (%)

Promoters	60.4
FII	7.7
DII	17.7
Public	14.2

Price Performance (%)

	-1m	-3m	-12m
Absolute	(6.3)	35.4	(4.7)
Rel to Sensex	(11.5)	15.9	(31.1)

Key Stock Data

Bloomberg / Reuters	ONGC IN/ONGC.BO
Sector	Oil & Gas
Shares o/s (mn)	12,580
Market cap. (Rs mn)	12,37,899
Market cap. (US\$ mn)	17,030
3-m daily average value (Rs mn)	2,311.6
52-week high / low	Rs108 / 52
Sensex / Nifty	52,154 / 15,315

Relative to Sensex (%)



Financial snapshot

Year	FY19	FY20	FY21E	FY22E	FY23E
Revenue	10,92,999	9,57,013	6,74,980	7,26,002	8,09,439
EBITDA	5,14,422	4,06,032	2,72,577	2,81,685	3,17,298
EBITDA (%)	47.1	42.4	40.4	38.8	39.2
Adj. PAT	2,72,509	1,66,782	1,02,508	1,02,905	1,13,356
EPS (Rs)	21.7	13.3	8.1	8.2	9.0
EPS Growth (%)	35.3	(38.8)	(38.5)	0.4	10.2
PE (x)	4.5	7.4	12.1	12.0	10.9
Dividend Yield (%)	7.1	6.1	3.8	4.2	4.6
EV/EBITDA (x)	2.8	3.4	4.9	4.9	4.4
RoE (%)	13.8	8.4	5.2	5.1	5.5
RoCE (%)	13.3	8.1	4.1	3.7	4.2

Source: Company; IDBI Capital Research

Concall Highlights:

- **New subsidiary for Gas business:** Prime intention of the new subsidiary is to bid for its own gas in the competitive bidding of KG basin. Along with that entire LNG sourcing and marketing of gas would be a part of the new subsidiary. ONGC's group companies like MRPL, OMPL, OPAL and HPCL combined need gas in the range of 2.5mmt-4mmt.
- **New gas pricing formula:** The Company expects new gas pricing formula to emerge which would lead to much higher gas price and expects it to be announced soon.
- **Capex/volume Guidance:** The company expects to achieve a capex of Rs290 bn for FY21 while keeps US\$4-4.5 bn for FY22E. Further, it expects oil/gas volume of 22-22.5mmt/23bcm in FY21E, growing to 23mmt/25bcm in FY22E.
- **OPAL capital Structure:** ONGC's equity contribution is just Rs10 bn in overall equity of Rs22.2bn, which is less than 50%. Also, the entity is highly leveraged with total capital of nearly Rs300 bn.
- **Debt level:** Standalone debt stands at Rs128.6 bn at the end of Q3FY21 vs Rs139.5 bn at end of FY20. However, at consolidated level debt/equity stands at 45%. ONGC converted lot of short term loans to long term loans which benefited in terms of lower interest cost.
- **Tax rate:** New tax structure is still under evaluation phase and may shift to new tax rate in FY22E.
- **KG DWN 98/2:** Total capitalized cost of KG Basin is Rs98 bn. Further, it expects it to achieve a production rate of 3mmscmd by May 2021 while guided for avg production of 3.4mmscmd for FY22 and 8.5mmscmd for FY23 and likely to achieve peak production of 15mmscmd in FY24.
- **Profitability of different group companies:** The management shared profitability for 9MFY21 for its different group entities as follow: Rs47.5 bn for ONGC, Rs8.7 bn for OVL, Rs76 bn for HPCL, Rs2.9 bn for PLL and loss of Rs10 bn for MRPL and loss of Rs5.3 bn for OPAL.

Exhibit 1: Actual vs Estimates

(Rs mn)	Actual	Estimated	% Variance
Net sales	1,70,238	1,70,402	0%
EBITDA	65,076	64,599	1%
EBITDA margin (%)	38%	38%	32
Adj net income	13,782	26,140	-47%
FDEPS (Rs)	1.1	2.1	-47%

Source: Company; IDBI Capital Research

Exhibit 2: Change in Estimates

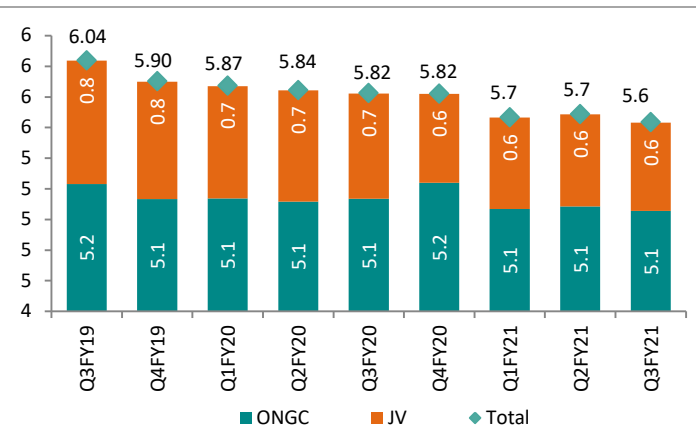
Key parameters (Rs mn)	FY21E			FY22E			FY23E		
	Old	New	% Chg	Old	New	% Chg	Old	New	% Chg
Revenue	6,34,364	6,74,980	6.4	7,24,611	7,26,002	0.2	8,06,427	8,09,439	0.4
EBITDA	2,39,749	2,72,577	13.7	2,69,347	2,81,685	4.6	3,02,647	3,17,298	4.8
EBITDA margin (%)	37.8	40.4	259	37.2	38.8	163	37.5	39.2	167
Net profit	85,741	1,02,508	19.6	94,269	1,02,905	9.2	1,03,100	1,13,356	9.9
FDEPS (Rs)	6.8	8.1	19.6	7.5	8.2	9.2	8.2	9.0	9.9

Exhibit 3: Quarterly performance

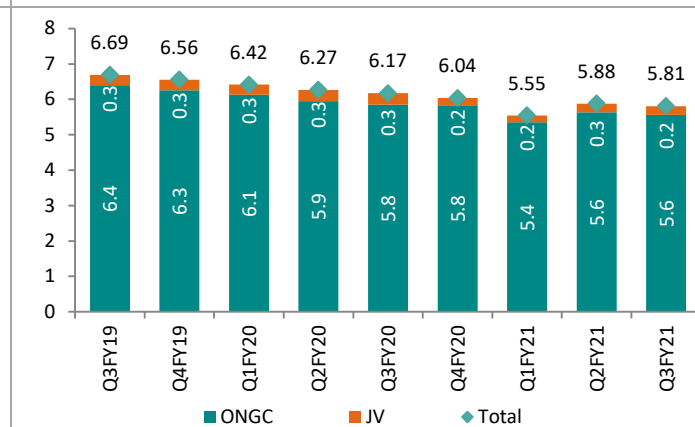
(Rs mn)

Rs mn	Q3FY20	Q4FY20	Q1FY21	Q2FY21	Q3FY21	% YoY	% QoQ
Revenue	2,37,101	2,14,562	1,30,113	1,69,171	1,70,238	-28%	1%
Decrease/(Increase) in Stock	-2,036	4,678	-1,115	-1,320	-464	-77%	-65%
Raw Material Cost	6,681	5,882	3,967	5,386	4,930	-26%	-8%
Employee Cost	6,674	6,115	4,985	6,161	5,621	-16%	-9%
Other Expenses	46,139	63,938	33,391	35,243	35,718	-23%	1%
Statutory Levies	56,671	48,070	29,809	39,349	40,973	-28%	4%
Survey Costs	2,331	3,950	5,590	1,878	3,638	56%	94%
Exploratory (Dry) Well Costs	14,846	26,434	5,679	12,582	14,748	-1%	17%
Total Expenditures	1,31,306	1,59,067	82,305	99,277	1,05,162	-20%	6%
EBITDA	1,05,795	55,495	47,808	69,894	65,076	-38%	-7%
EBITDA margin (%)	44.6	25.9	36.7	41.3	38.2	-14%	-7%
DD&A	53,019	49,986	38,223	36,795	44,270	-17%	20%
EBIT	52,776	5,509	9,585	33,099	20,806	-61%	-37%
Finance Charges	6,264	8,695	4,918	3,172	4,777	-24%	51%
Other Income	14,025	13,256	4,368	22,355	12,184	-13%	-45%
Exceptional Items	0	-48,991	0	-12,382	0	--	--
PBT	60,537	-38,920	9,035	39,900	28,212	-53%	-29%
Total Tax	18,273	-7,938	4,075	11,122	14,430	-21%	30%
Reported PAT	42,265	-30,983	4,960	28,778	13,782	-67%	-52%
Adjusted PAT	42,265	7,049	4,960	37,709	13,782	-67%	-63%
Adjusted EPS (Rs)	3.4	0.6	0.4	3.0	1.1	-67%	-63%
Crude oil Production (mmt)	5.8	5.8	5.7	5.7	5.6	-3%	-1%
Gas Production (bcm)	6.2	6.0	5.5	5.9	5.8	-6%	-1%
VAP Production (mmt)	0.9	0.9	0.7	0.8	0.8	-8%	-3%
Net oil realisation (USD/bbl)	59.7	49.0	28.7	41.4	43.2	-28%	4%
Gas Realisation (Rs/scm)	9.3	9.1	7.2	7.2	5.4	-42%	-24%

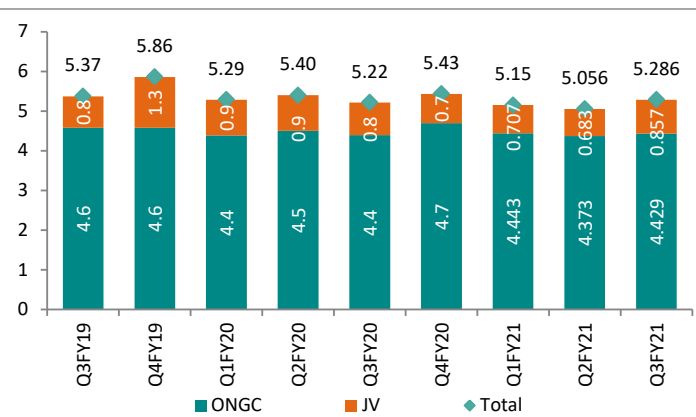
Source: Company; IDBI Capital Research

Exhibit 4: Oil production volumes (mmt)


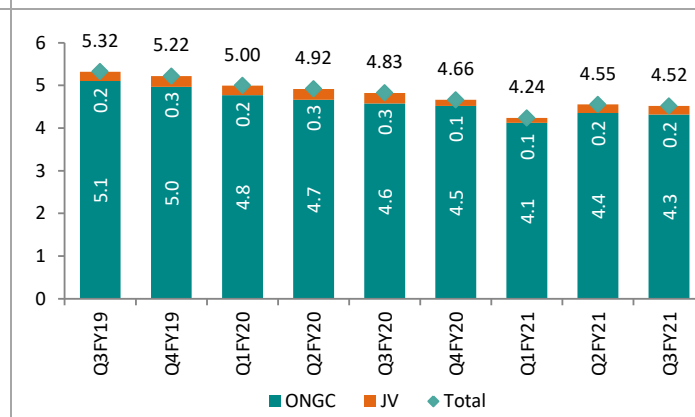
Source: Company; IDBI Capital Research

Exhibit 5: Gas production volumes (bcm)


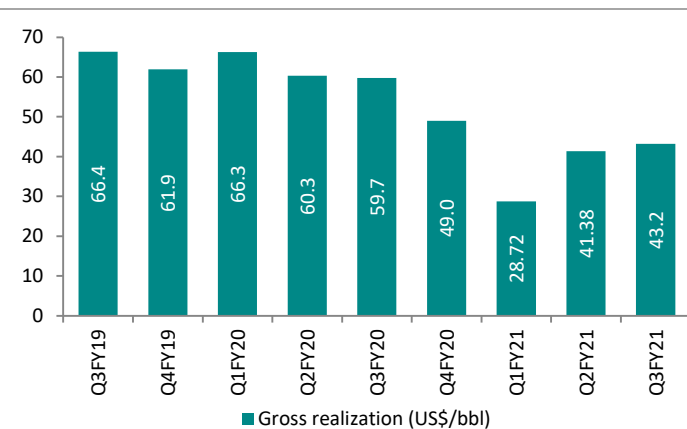
Source: Company; IDBI Capital Research

Exhibit 6: Oil sales volumes (mmt)


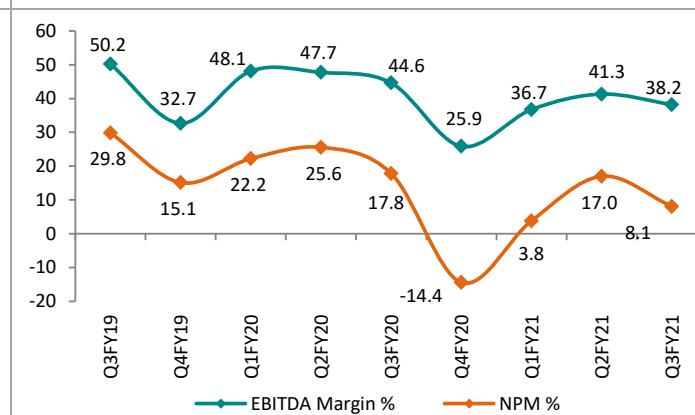
Source: Company; IDBI Capital Research

Exhibit 7: Gas sales volumes (bcm)


Source: Company; IDBI Capital Research

Exhibit 8: Net oil realization (US\$/bbl)


Source: Company; IDBI Capital Research

Exhibit 9: Margins (%)


Source: Company; IDBI Capital Research

Financial Summary

Profit & Loss Account

(Rs mn)

Year-end: March	FY20	FY21E	FY22E	FY23E
Net sales	9,57,013	6,74,980	7,26,002	8,09,439
<i>growth (%)</i>	<i>(12.4)</i>	<i>(29.5)</i>	<i>7.6</i>	<i>11.5</i>
Operating expenses	(5,56,104)	(4,07,782)	(4,49,965)	(4,98,071)
EBITDA	4,06,032	2,72,577	2,81,685	3,17,298
<i>growth (%)</i>	<i>(21.1)</i>	<i>(32.9)</i>	<i>3.3</i>	<i>12.6</i>
Depreciation	(1,86,169)	(1,61,437)	(1,79,905)	(2,00,038)
EBIT	2,19,864	1,11,140	1,01,780	1,17,260
Interest paid	(28,237)	(13,793)	(14,299)	(20,717)
Other income	61,050	57,967	59,526	65,394
Pre-tax profit	2,03,687	1,42,932	1,47,007	1,61,937
Tax	(69,242)	(48,597)	(44,102)	(48,581)
<i>Effective tax rate (%)</i>	<i>34.0</i>	<i>34.0</i>	<i>30.0</i>	<i>30.0</i>
Minority Interest	-	-	-	-
Net profit	1,34,445	94,335	1,02,905	1,13,356
Exceptional items	(32,337)	(8,172)	-	-
Adjusted net profit	1,66,782	1,02,508	1,02,905	1,13,356
<i>growth (%)</i>	<i>(38.8)</i>	<i>(38.5)</i>	<i>0.4</i>	<i>10.2</i>
<i>Shares o/s (mn nos)</i>	<i>12,580</i>	<i>12,580</i>	<i>12,580</i>	<i>12,580</i>

Cash Flow Statement

(Rs mn)

Year-end: March	FY20	FY21E	FY22E	FY23E
Pre-tax profit	2,52,677	1,42,932	1,47,007	1,61,937
Depreciation	1,86,169	1,61,437	1,79,905	2,00,038
Tax paid	(66,646)	(49,868)	(45,398)	(49,903)
Chg in working capital	1,26,655	39,474	24,448	12,261
Other operating activities	78,997	(44,175)	(45,227)	(44,677)
Cash flow from operations (a)	5,77,852	2,49,801	2,60,735	2,79,656
Capital expenditure	(3,33,247)	(2,07,634)	(2,82,971)	(2,69,566)
Chg in investments	(4,374)	-	-	-
Other investing activities	32,477	50,369	56,278	62,113
Cash flow from investing (b)	(3,45,740)	(1,57,265)	(2,26,693)	(2,07,452)
Equity raised/(repaid)	-	-	-	-
Debt raised/(repaid)	(1,34,847)	(30,000)	20,000	30,000
Dividend (incl. tax)	(87,504)	(56,601)	(61,743)	(68,014)
Chg in minorities	-	-	-	-
Other financing activities	(5,120)	(13,793)	(14,299)	(20,717)
Cash flow from financing (c)	(2,27,471)	(1,00,394)	(56,042)	(58,730)
Net chg in cash (a+b+c)	4,642	(7,858)	(22,001)	13,473

Balance Sheet

(Rs mn)

Year-end: March	FY20	FY21E	FY22E	FY23E
Net fixed assets	16,39,246	16,67,375	17,70,442	18,39,969
Investments	7,24,300	7,24,300	7,24,300	7,24,300
Other non-curr assets	3,33,402	3,36,736	3,40,103	3,43,504
Current assets	2,69,860	2,08,255	2,00,124	2,36,237
Inventories	85,666	60,577	65,144	72,598
Sundry Debtors	47,774	33,783	36,329	40,486
Cash and Bank	9,682	24,274	2,274	15,747
Marketable Securities	-	-	-	-
Loans and advances	5,117	3,619	3,891	4,337
Total assets	29,66,808	29,36,666	30,34,969	31,44,010
Shareholders' funds	19,43,381	19,81,115	20,22,277	20,67,620
Share capital	62,902	62,902	62,902	62,902
Reserves & surplus	18,80,479	19,18,214	19,59,376	20,04,718
Total Debt	1,39,491	1,09,491	1,29,491	1,59,491
Secured loans	22,451	-	-	-
Unsecured loans	1,17,040	1,09,491	1,29,491	1,59,491
Other liabilities	5,95,306	6,09,054	6,23,496	6,38,668
Curr Liab & prov	2,88,630	2,37,006	2,59,704	2,78,232
Current liabilities	2,77,655	2,27,993	2,49,829	2,67,652
Provisions	10,975	9,012	9,875	10,580
Total liabilities	10,23,427	9,55,551	10,12,692	10,76,390
Total equity & liabilities	29,66,808	29,36,666	30,34,969	31,44,010
Book Value (Rs)	154	157	161	164

Source: Company; IDBI Capital Research

Financial Ratios

Year-end: March	FY20	FY21E	FY22E	FY23E
Adj. EPS (Rs)	13.3	8.1	8.2	9.0
Adj EPS growth (%)	(38.8)	(38.5)	0.4	10.2
EBITDA margin (%)	42.4	40.4	38.8	39.2
Pre-tax margin (%)	21.3	21.2	20.2	20.0
ROE (%)	8.4	5.2	5.1	5.5
ROCE (%)	8.1	4.1	3.7	4.2
Turnover & Leverage ratios (x)				
Asset turnover (x)	0.3	0.2	0.2	0.3
Leverage factor (x)	1.5	1.5	1.5	1.5
Net margin (%)	17.4	15.2	14.2	14.0
Net Debt/Equity (x)	0.1	0.0	0.1	0.1
Working Capital & Liquidity ratio				
Inventory days	33	33	33	33
Receivable days	18	18	18	18
Payable days	47	52	52	50

Valuation

Year-end: March	FY20	FY21E	FY22E	FY23E
PER (x)	7.4	12.1	12.0	10.9
Price / Book value (x)	0.6	0.6	0.6	0.6
PCE (x)	3.5	4.7	4.4	4.0
EV / Net sales (x)	1.4	2.0	1.9	1.7
EV / EBITDA (x)	3.4	4.9	4.9	4.4
Dividend Yield (%)	6.1	3.8	4.2	4.6



Notes

Dealing	(91-22) 6836 1111	dealing@idbicapital.com
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Key to Ratings Stocks:

BUY: Absolute return of 15% and above; **ACCUMULATE:** 5% to 15%; **HOLD:** Upto $\pm 5\%$; **REDUCE:** -5% to -15%; **SELL:** -15% and below

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