

Sector: Oil & Gas
Result Update

	Change
Reco: Buy	↔
CMP: Rs. 96	
Price Target: Rs. 115	↔

↑ Upgrade ↔ No change ↓ Downgrade

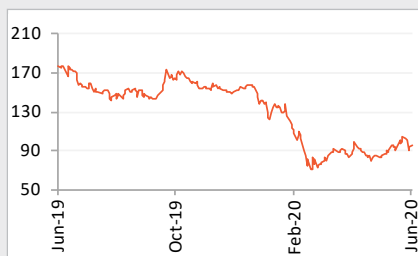
Company details

Market cap:	Rs. 10,361 cr
52-week high/low:	Rs. 182/66
NSE volume: (No of shares)	28.7 lakh
BSE code:	533106
NSE code:	OIL
Sharekhan code:	OIL
Free float: (No of shares)	47.0 cr

Shareholding (%)

Promoters	56.7
FII	6.6
DII	19.2
Public & others	17.5

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	9.5	20.4	-37.1	-45.3
Relative to Sensex	4.5	-2.5	-21.3	-33.4

Sharekhan Research, Bloomberg

Oil India Limited's Q4FY2020 adjusting PAT stood at Rs. 502 crore (down 38.6% y-o-y), which was above our estimate of Rs. 462 crore. The beat was on the account of higher-than-expected other income at Rs. 673 crore (which excludes one-time interest income of Rs. 321 crore on tax refund) and lower-than-expected DD&A expenses (down 40.4% y-o-y) partially by weak gas sales volume (down 14.4% y-o-y; down 11.2% q-o-q) and higher operating cost excluding provision (up 44% y-o-y). Oil sales volume at 0.75mmt (down 3.7% y-o-y; up 3% q-o-q) was in-line with our estimates and net oil realisation at \$52.2/bbl (down 15.5% y-o-y; down 17.5% q-o-q) was marginally ahead of our expectation at \$50.8/bbl. The management has guided for flat y-o-y oil & gas production for FY2021E and has guided for capex of Rs. 3,875 crore for FY2021E and Rs. 4,000 crore-4,200 crore for FY2022E. The company is optimistic to gradually increase its gas production to ~12mmscmd by 2023-2024 as compared to gas production level of 6.7mmscmd currently. Oil India is trading at an attractive valuation of 4.6x its FY2022E EPS (46% discount to its historical average one-year forward PE multiple of 8.5x) and offers high dividend yield of 9-10%. Hence, we maintain our Buy rating on Oil India with an unchanged SoTP-based PT of Rs. 115.

Key positives

- Sharply lower DD&A cost at Rs. 253 crore (down 40.4% y-o-y) due to the decline in depletion with improvement in 1P oil and gas reserves.
- Higher-than-expected net oil realisation at \$52.2/bbl (versus our expectation of \$50.8/bbl).
- Total dividend of Rs. 10.6/share for FY2020, which implies dividend yield of 11%.

Key negatives

- Lower-than-expected gas sales volume at 0.53bcm (down 14.4% y-o-y) in Q4FY2020.
- Sharply increase in other expenses excluding provision (up 44% y-o-y).

Our Call

Valuation – Maintain Buy rating on Oil India with an unchanged SoTP-based PT Rs. 115: We have increased our FY2021E-FY2022E EPS to factor-in lower tax rate of 25.2% (as the company has opted for lower tax rate under Section 115BAA of Income Tax Act), partially offset by lower gas production (amid weak demand due to COVID-19) and lower gas price for FY2021E. Development of gas fields (incremental production expected at 5mmscmd by 2023-2024), recovery in oil prices, and freeing of domestic gas prices would be key to the earnings recovery of Oil India over the next couple of years. Oil India is trading at an attractive valuation of 4.6x its FY2022E EPS (46% discount to its historical average one-year forward PE multiple of 8.5x) and offers high dividend yield of 9-10%. Hence, we maintain our Buy rating on Oil India with an unchanged SoTP-based PT of Rs. 115.

Key Risks

Lower-than-expected oil and gas production amid COVID-19 and prolonged weakness in hydrocarbon (oil and gas) prices could adversely impact earnings and our rating on the stock.

Valuation (Standalone)

Particulars	Rs cr				
	FY18	FY19	FY20E	FY21E	FY22E
Net sales	10,656	13,735	12,129	8,165	10,768
OPM (%)	36.7%	39.9%	21.4%	31.7%	35.3%
Adjusted PAT	2,668	3,617	3,208	1,510	2,274
y-o-y growth (%)	20.7%	35.6%	-11.3%	-52.9%	50.6%
Adjusted EPS (Rs.)	24.6	33.4	29.6	13.9	21.0
PE (x)	3.9	2.9	3.2	6.9	4.6
P/BV (x)	0.3	0.4	0.4	0.4	0.4
EV/EBDITA (x)	3.6	2.1	7.5	8.0	5.3
ROE (%)	9.4%	13.0%	12.3%	6.1%	8.9%
ROCE (%)	10.7%	14.5%	7.3%	7.4%	10.1%

Source: Company; Sharekhan estimates

Adjusted PAT above estimate given higher other income and lower DD&A gets partially offset by miss in operating profit: Oil India's adjusted operating profit at Rs. 473 crore (down 56.2% y-o-y; down 55.6% q-o-q) was substantially below our estimate of Rs. 914 crore. The sharp miss was on the account of higher-than-expected operating expenses excluding provisions (up 44% y-o-y; up 2.2x q-o-q) and lower-than-expected gas sales volume at 0.5bcm (down 14.4% y-o-y; down 11.2% q-o-q). We have adjusted operating profit for provision of Rs. 1,687 crore, which was included in other expenses. Oil sales volume at 0.75mmt (down 3.7% y-o-y; up 3% q-o-q) was in-line with our estimates and net oil realisation at \$52.2/bbl (down 15.5% y-o-y; down 17.5% q-o-q) was marginally ahead of our expectation at \$50.8/bbl. Upstream PSUs continue to bear zero subsidy burden on domestic LPG and PDS kerosene. Reported PAT of Rs. 926 crore has many one-offs related to tax reversals (as the company shifted to lower tax rate) and provision in other expenses. Adjusting for the same, PAT stood at Rs. 502 crore (down 38.6% y-o-y), above our estimate of Rs. 462 crore due to higher-than-expected other income at Rs. 673 crore (which excludes one-time interest income of Rs. 321 crore on tax refund) and lower-than-expected DD&A expenses (down 40.4% y-o-y, given the sharp decline in depletion).

Q4FY2020 conference call highlights

- ◆ **Baghjan gas blowout update:** Management has highlighted that the company is in the process of controlling the blowout situation in gas well at Baghjan field by the second week of July 2020. Oil India has witnessed cumulative production loss of 8,746mmt of crude oil and 11.25mmscm of natural gas since May 27, 2020, as operations were disrupted in 13 oil wells and 1 gas well due to blockades. As a result of blowout at Baghjan, the total gas production loss is at only 1% of overall gas production of the company. The company has no plans to relinquish the Baghjan oilfield.
- ◆ **Baghjan assets contribution:** Oil production from the field is at 10-12% of total oil production, while gas production is less than 2-3% of total gas production. The company expects gas production from Baghjan assets has potential to be ramped up to 5mmscmd pver next couple of years versus only 0.5mmscmd currently.
- ◆ **Oil and gas production guidance:** For FY2021E, management has guided to maintain oil and gas production at level similar to FY2020 (oil production of 3.1mmt and gas production of 2.8bcm). The MoU's targets with the government has not been finalised yet. The company expects huge potential for increase in gas production and targets to have incremental gas production of 5mmscmd and would reach ~12mmscmd by 2023-2024 as compared to 6.7mmscmd currently. The company's oilfield is witnessing 8-10% natural decline in production due to aging fields, while natural decline for gas production is only 1-2%.
- ◆ **Capex guidance:** Management has guided for capex of Rs. 3,875 crore for FY2021E and Rs. 4,000 crore-4,200 crore for FY2022E.
- ◆ **Domestic gas price outlook:** Management expects domestic gas price to get further reduced to \$1.9-2.1/mmbtu for H2FY2021 based on the trend for international benchmark gas prices. The breakeven cost for gas production is Rs. 2.1/mmbtu (including DD&A) for Oil India.
- ◆ **Debt levels:** Oil India's debt stood at \$1,178 million at standalone level and at \$1,678 million at consolidated level as on March 31, 2020.
- ◆ **KG asset update:** The assets have total three discoveries, out of which one has been relinquished and the assets hold total area of 350 square kilometers. The KG asset has seen write-off of one well with total amount of Rs. 330 crore. Oil India has made two high-pressure and high-temperature gas discoveries and approval for DGH for extended production testing has been received to understand the commercial viability of the discoveries without drilling appraisal wells.
- ◆ **Impairment of investments in overseas assets:** Given low crude oil and gas prices, Oil India had recognised impairment of investment of Rs. 512 crore for its US subsidiary, Rs. 669 crore for Netherlands subsidiaries, and Rs. 47 crore for loan to Nigeria subsidiary.
- ◆ **Oil and gas reserve:** Oil India's 1P reserves increased by 8 million tonne of oil equivalent in FY2020.

Results (Standalone)

Particulars	Rs cr				
	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)
Revenue	2,590	3,087	-16.1%	2,952	-12.3%
Total Expenditure	3,691	2,008	83.8%	1,856	98.9%
Reported operating profits	(1,101)	1,079	NA	1,096	-200.5%
Adjusted operating profit	473	1,079	-56.2%	1,064	-55.6%
Other Income	994	419	137.1%	135	634.3%
EBIDTA	(107)	1,498	NA	1,231	-108.7%
Interest	133	120	10.8%	122	9.0%
PBDT	(240)	1,379	NA	1,110	-121.6%
Depreciation & prov	253	424	-40.4%	424	-40.4%
Exceptional items	1,681	1,027	NA	(6)	NA
Reported PBT	(493)	955	NA	685	NA
Adjusted PBT	1,189	1,981	-40.0%	680	74.9%
Tax	(1,418)	136	NA	279	NA
Reported Profit After Tax	926	(209)	NA	406	127.8%
Adjusted PAT	502	818	-38.6%	401	25.3%
Adj. EPS (Rs.)	4.6	7.5	-38.6%	3.7	25.3%
Margins (%)			bps		bps
OPMs	18.3%	35.0%	(1,671)	36.0%	(1,778)
PAT	19.4%	26.5%	(711)	13.6%	581
Tax rate	40.7%	24.4%	1,629	35.6%	506

Source: Company

Key operating performance

Particulars	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)
Net oil realisation (\$/bbl)	52.2	61.8	-15.5%	63.3	-17.5%
Oil production volume (mmt)	0.76	0.78	-3.3%	0.75	1.5%
Oil sales volume (mmt)	0.75	0.78	-3.7%	0.73	3.0%
Crude oil business EBIT (Rs. crore)	360	862	-58.2%	875	-58.9%
Gas production volume (bcm)	0.65	0.70	-8.3%	0.70	-7.5%
Gas sales volume (bcm)	0.53	0.62	-14.4%	0.60	-11.2%
Gas business EBIT (Rs. crore)	57	157	-63.7%	107	-46.7%

Source: Company

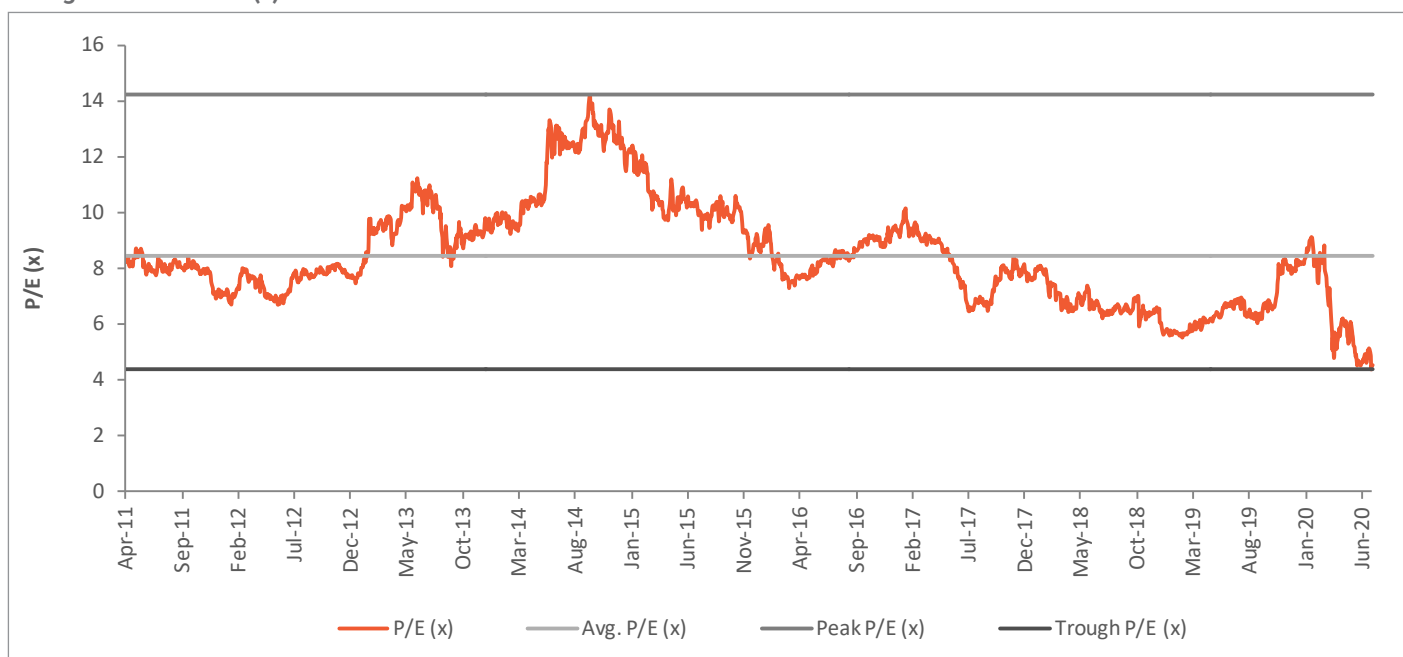
Outlook

Weak oil and gas realisation to impact performance in FY2021E; Recovery in oil and gas prices key to earnings revival: The sharp decline in oil prices to \$40-42/bbl (versus \$61/bbl in FY2020) amid weak oil demand and expectation of further potential cut in domestic gas prices (post the recent reduction in domestic gas prices by 26% to \$2.4/mmBtu for H1FY2021E) have impacted the earnings outlook for Oil India. Hence, recovery in oil and gas prices is key to revival in earnings of upstream PSUs. Oil production is likely to remain flat giving aging oilfields (natural oil production decline of 8-10% annually). However, management expects gas production to increase gradually to 12mmscmd by 2023-2024 from 6.7mmscmd currently. Any decision by the government on freeing of domestic gas price could act as key catalyst for Oil India.

Valuation

Maintain our Buy rating on Oil India with unchanged SoTP-based PT of Rs. 115: We have increased our FY2021E-FY2022E EPS to factor-in lower tax rate of 25.2% (as the company has opted for lower tax rate under Section 115BAA of Income Tax Act), partially offset by lower gas production (amid weak demand due to COVID-19) and lower gas price for FY2021E. Development of gas fields (incremental production expected at 5mmscmd by 2023-2024), recovery in oil prices, and freeing of domestic gas prices would be key to the earnings recovery of Oil India over the next couple of years. Oil India is trading at an attractive valuation of 4.6x its FY2022E EPS (46% discount to its historical average one-year forward PE multiple of 8.5x) and offers high dividend yield of 9-10%. Hence, we maintain our Buy rating on Oil India with an unchanged SoTP-based PT of Rs. 115.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

Oil India is an Indian national oil company that explores, develops, and produces crude oil and natural gas, transports crude oil, and produces LPG. The company is the second-largest E&P company in India in terms of production and reserves. More than 95% of Oil India's production comes from its upper Assam basin. The company holds domestic 2P (proved and probable) reserves of 76mmt for oil and 130bcm for gas as of March 31, 2019. The company's oil production stood at 3.1mmt and gas production stood at 2,801mmscm in FY2020.

Investment theme

The sharp correction in oil prices has raised concerns over profitability of upstream PSUs in the near term. However, the recent recovery in oil prices bodes well for earnings revival of Oil India. Any decision on freeing of domestic gas prices could act as key catalyst for Oil India. Attractive valuation of Oil India and high dividend yield of 9-10% keeps us positive on the stock.

Key Risks

- ◆ Lower-than-expected oil and gas production amid COVID-19 and prolonged weakness in hydrocarbon (oil and gas) prices could adversely impact earnings and our rating on the stock.
- ◆ High natural decline rates in the mature oil fields could impact the company's production.

Additional Data

Key management personnel

Sushil Chandra Mishra	Chairman & Managing Director
Harish Madhav	Director – Finance
P. Chandrasekaran	Director - Exploration & Development

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp of India	12.0
2	Indian Oil Corp Ltd	4.9
3	ICICI Prudential Asset Management	3.1
4	Reliance Capital Trustee Co Ltd	2.6
5	Hindustan Petroleum Corp Ltd	2.5
6	Bharat Petroleum Corp Ltd	2.5
7	Vanguard Group Inc/The	1.0
8	BlackRock Inc	0.8
9	ICICI Prudential Life Insurance Co	0.4
10	WisdomTree Investments Inc	0.4

Source: Bloomberg

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