Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Oil India Ltd

Robust Q3; Likely APM gas price cap a concern

Oil & Gas	Sharekhan code: OIL
Reco/View: Hold ↔	CMP: Rs. 241
Price Target: Rs. 260 ↑	

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX

	+	=	-
Right Sector (RS)		✓	
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING 47.68

Updated Dec 08, 2022

Severe Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

Company details

Market cap:	Rs. 26,096 cr
52-week high/low:	Rs. 306/168
NSE volume: (No of shares)	12.7 lakh
BSE code:	533106
NSE code:	OIL
Free float: (No of shares)	47.0 cr

Shareholding (%)

Promoters	56.7
FII	11.5
DII	16.0
Public & others	15.8

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	7.7	20.0	26.4	6.6
Relative to Sensex	7.4	21.9	24.8	-0.5

Sharekhan Research, Bloomberg

Summary

- Q3FY23 standalone PAT of Rs. 1,746 crore, rose 40% y-o-y, substantially above our estimate due to a sharp decline in exploratory cost write-off and lower provisions.
- Oil/Gas EBIT increased by 14%/79% q-o-q to Rs. 1,543 crore/Rs. 1,091 crore reflecting cost control and higher APM gas price (up 41% q-o-q to $8.57/mmBtu). Operational performance was mixed with in-line net oil realisation at $77/bbl but crude oil/gas sales volume at 0.77 mmt/0.61 bcm was 2%/4% below our estimate.
- Management guided for oil/gas production of 3.4mmt/3.3 bcm for FY24E, which implies a CAGR of 6%/4% over FY22-24E aims to further increase oil/gas production to 4 mmt/5 bcm. We believe that earnings of upstream PSUs would peak out in FY23 and decline going forward due to likely capping of domestic gas price and normalization a crude oil price.
- We maintain our Hold rating on Oil India with a revised PT of Rs. 260 as ad hoc tax policy changes create earnings uncertainty and valuation concerns. Dividend yield of ~7% limits meaningful downside from current levels.

Oil India Limited's (OIL) Q3FY23 standalone operating profit Rs. 2,855 crore (up 125% y-o-y; up 54% q-o-q) was 14% above our estimate of Rs. 2,507 crore due to sharply lower exploratory cost write-offs (down 65%/41% y-o-y/q-o-q) and lower provisions. Operational performance was mixed with in-line net oil realisation of $77/bbl (gross oil realisation of $88/bbl minus the SAED of $11/bbl) while oil/gas sales volume of 0.77 mmt/0.61 bcm, down 0.5%/7% q-o-q was 2%/4% below our estimate. Oil EBIT increased by 29%/14% y-o-y/q-o-q to Rs. 1,543 crore and gas EBIT grew by 79% q-o-q to Rs. 1,091 crore (versus negative EBIT of Rs. 108 crore in Q3FY22). Standalone PAT at Rs. 1,746 crore (up 40.2% y-o-y, up 1.5% q-o-q) was 9% above our estimate led by a beat in operating profit and a lower tax rate of 24.2% partially offset by lower other income (down 89% y-o-y).

Key positives

- A sharp increase of 14%/79% q-o-q in oil/gas EBIT.
- OIL declared second interim dividend of Rs. 10/share; DPS to Rs. 14.5/share (implies dividend yield of ~6% on CMP) so far in FY23.

Key negatives

- Miss of 2%/4% in oil/gas sales volume at 0.77 mmt/0.61 bcm, down 0.5%/6.9% q-o-q.

Management Commentary

- Oil production guidance of 3.2 mmt/3.4 mmt for FY23/FY24 and that for gas at 3 bcm/3.3 bcm for FY23/FY24. This implies an impressive 6%/4% CAGR in oil/gas production over FY22-24E. Company has ambitions to reach oil/gas production of 4 mmt/5 bcm.
- Standalone capex guidance of ~Rs. 4,000 crore for FY24, which includes 500-600 crore for equity contribution towards NRL capex. NRL has spent Rs. 8,000 crore for its refinery expansion to 9 mtpa (versus 3 mtpa currently) and the expansion is expected to get completed in FY25.
- Consolidated debt as on date is Rs. 17,500 crore which includes Rs. 11,244 crore/Rs. 2,300 crore for Standalone/NRL .
- Other expenses declined due to lower well write-offs and lesser CSR expenses, which are not linear. Forex loss also came at Rs. 49 crore versus 290 crore in Q2FY23.
- Profit from JVs/associates was lower as overseas assets in Nigeria and Russia did not perform well. Currency movement of USD/rubble also impacted profits of overseas assets.
- NRL Q3FY23 EBITDA/PAT at Rs. 1,122 crore/Rs. 799 crore versus Q2FY23 EBITDA/PAT at Rs. 1,070 crore/Rs. 728 crore. GRM at $13.48/bbl versus $13.84/bbl in Q2FY23.

Revision in estimates – We have increased our FY23-24 earnings estimate to factor lower cost assumption and oil/gas sales volume. We have also introduced our FY25 earnings estimate in this report

Our Call

Valuation – Maintain Hold on OIL with a revised PT of Rs. 260: We believe that earnings for upstream PSUs would peak-out in FY23 and expected to decline sharply going ahead due to likely capping of domestic gas price. Moreover, the ad-hoc cess rate has created earnings uncertainty and valuation concern for upstream PSUs. Lack of policy clarity would remain a key overhang Oil India until windfall taxes are removed and domestic gas price is market-linked. Hence, we maintain a Hold rating on Oil India with a revised PT of Rs. 260 (rollover of PE multiple to FY25E EPS). Decent dividend yield of ~7% limits material downside risk for Oil India. The stock trades (including earnings contribution from NRL) at 6.2x/5.2x its FY2024E/FY2025E EPS.

Key Risks

A sharp rise in crude oil & gas prices, removal of windfall tax and policy clarity on various duties is key upside risk and continued ad-hoc cess rate, sharp decline in oil price and likely capping of domestic gas price are downside risks.

Valuation Rs cr

Particulars	FY22	FY23E	FY24E	FY25E
Revenue	14,530	23,929	21,336	19,784
OPM (%)	37.0%	39.1%	31.1%	39.6%
Adjusted PAT	3,887	6,352	4,197	5,059
y-o-y growth (%)	182.3%	63.4%	-33.9%	20.5%
Adjusted EPS (Rs.)	35.8	58.6	38.7	46.6
PE (x)	6.7	4.1	6.2	5.2
P/BV (x)	0.9	0.8	0.8	0.7
EV/EBDITA (x)	6.5	3.5	4.7	3.9
ROE (%)	13.9%	20.3%	12.4%	14.1%
ROCE (%)	13.3%	20.8%	13.7%	15.4%

Source: Company; Sharekhan estimates

Q3 earnings beat led by lower exploratory cost write-offs/provisions

Q3FY23 standalone operating profit Rs. 2,855 crore (up 125% y-o-y; up 54% q-o-q) was 14% above our estimate of Rs. 2,507 crore due to sharply lower exploratory cost write-offs (down 65%/41% y-o-y/q-o-q) and lower provisions. Operational performance was mixed with in-line net oil realisation of $77/bbl (gross oil realisation of $88/bbl minus the SAED of $11/bbl) while oil/gas sales volume of 0.77 mmt/0.61 bcm, down 0.5%/7% q-o-q was 2%/4% below our estimate. Oil EBIT increased by 29%/14% y-o-y/q-o-q to Rs. 1,543 crore and gas EBIT grew by 79% q-o-q to Rs. 1,091 crore (versus negative EBIT of Rs. 108 crore in Q3FY22). Standalone PAT at Rs. 1,746 crore (up 40.2% y-o-y, up 1.5% q-o-q) was 9% above our estimate led by a beat in operating profit and a lower tax rate of 24.2% partially offset by lower other income (down 89% y-o-y).

Results (Standalone) Rs cr

Particulars	Q3FY23	Q3FY22	YoY (%)	Q2FY23	QoQ (%)
Revenue	**5,879**	**3,737**	**57.3**	**5,776**	**1.8**
Total Expenditure	3,024	2,469	22.5	3,928	-23.0
Operating profit	**2,855**	**1,267**	**125.3**	**1,848**	**54.5**
Other Income	102	969	-89.4	895	-89
Interest	201	175	15.0	211	-4.9
Depreciation	454	468	-3.0	424	7.1
PBT	**2,303**	**1,593**	**44.5**	**2,108**	**9.2**
Tax	557	348	59.9	388	43.7
Reported PAT	**1,746**	**1,245**	**40.2**	**1,721**	**1.5**
Equity Cap (cr)	108	108		108	
Reported EPS (Rs.)	16.1	11.5	40.2	15.9	1.5
Margins (%)			**BPS**		**BPS**
OPM	48.6	33.9	1464.8	32.0	1,656.6
NPM	29.7	33.3	-362.0	29.8	-8.9
Tax rate	24.2	21.9	231.9	18.4	579.4

Source: Company, Sharekhan Research

Key operating metrics

Particulars	Q3FY23	Q3FY22	YoY (%)	Q2FY23	QoQ (%)
Crude oil realisation ($/bbl)	88.3	78.6	12.4%	100.6	-12.2%
SAED ($/bbl)	11.2	0	NA	25.9	-56.8%
Net crude oil realisation ($/bbl)	77.1	78.6	-1.9%	74.7	3.3%
Gas price realisation ($/mmBtu)	8.6	2.9	195.5%	6.1	40.5%
Oil production volume (mmt)	0.81	0.75	7.0%	0.79	2.2%
Oil sales volume (mmt)	0.77	0.73	6.2%	0.78	-0.5%
Crude oil business EBIT (Rs. crore)	1,543	1,199	28.7%	1,357	13.8%
Gas production volume (bcm)	0.81	0.79	1.6%	0.82	-2.1%
Gas sales volume (bcm)	0.61	0.63	-3.5%	0.66	-6.9%
Gas business EBIT (Rs. crore)	1,091	-108	NA	609	79.2%

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Ad-hoc policy changes to impact earnings of upstream PSUs

The government's ad-hoc tax policy changes for the oil and gas sector in the volatile oil price environment has raised concerns over the earnings outlook of upstream PSUs and is divergence from government's earlier intent of doing away with oil subsidy mechanism. The government has introduced a windfall tax in the form of fixed cess rate, which is in addition to current ad valorem effective cess rate of 16.67% on realised oil price for upstream PSUs. A higher cess would be more detrimental to earnings of upstream PSUs in case of the falling crude oil price environment and pose risk to FY2024E-FY2025E earnings. Additionally, a likely capping of domestic gas price would further limit earnings growth for upstream PSUs.

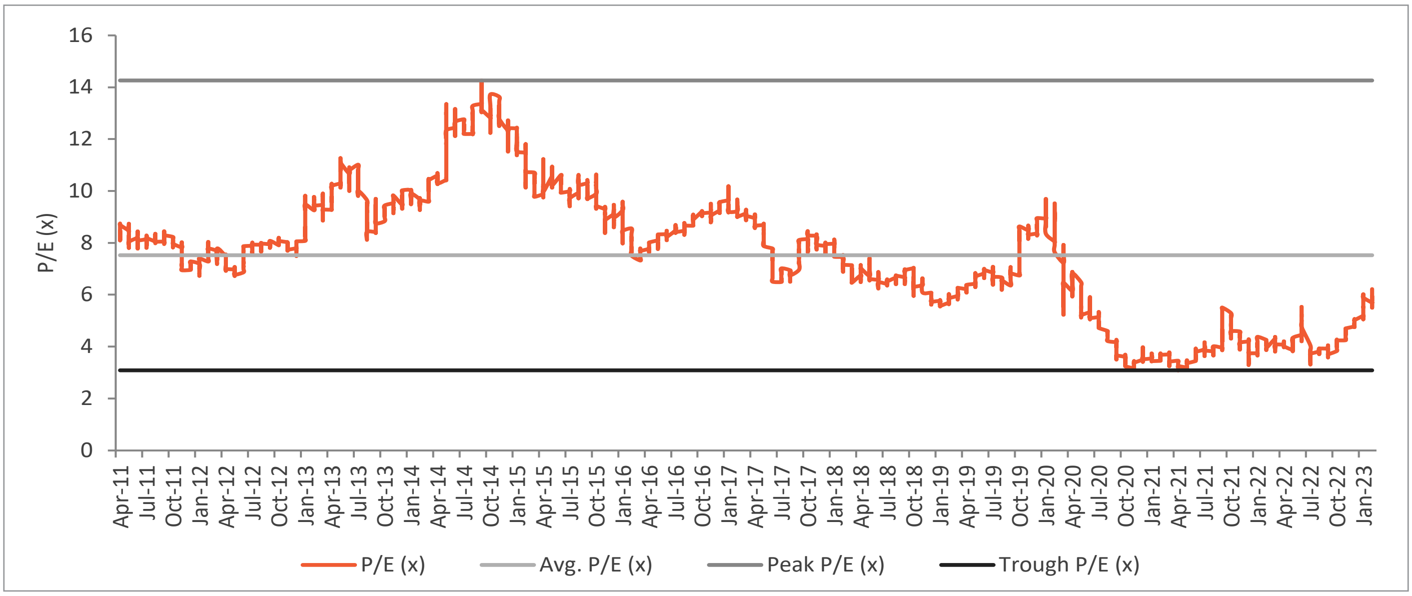
■ Company outlook - Muted earnings outlook

OIL's earnings outlook has been impacted due to windfall tax (in form of higher cess rate) imposed by the government and likely capping of APM gas price at $6.5/mmbtu. Management's guidance of ramp-up in oil & gas production is impressive but the poor track record and maturing oil & gas fields makes us remain conservative on volume growth over next of years.

■ Valuation - Maintain Hold on OIL with a revised PT of Rs. 260

We believe that earnings for upstream PSUs would peak-out in FY23 and expected to decline sharply going ahead due to likely capping of domestic gas price. Moreover, the ad-hoc cess rate has created earnings uncertainty and valuation concern for upstream PSUs. Lack of policy clarity would remain a key overhang Oil India until windfall taxes are removed and domestic gas price is market-linked. Hence, we maintain a Hold rating on Oil India with a revised PT of Rs. 260 (rollover of PE multiple to FY25E EPS). Decent dividend yield of ~7% limits material downside risk for Oil India. The stock trades (including earnings contribution from NRL) at 6.2x/5.2x its FY2024E/FY2025E EPS.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

OIL 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's production comes from its upper Assam basin. The company holds domestic 2P (proved and probable) reserves of 191mtoe (oil + gas) as of March 31, 2021.

Investment theme

The recent imposition of windfall tax on upstream PSUs and likely cap on domestic gas price has severely dented earnings outlook for upstream PSUs (including OIL). Higher cess rate would be more detrimental to the earnings of upstream PSUs in case of the falling crude oil price environment. Additionally, poor track record of growth in oil & gas production makes us cautious on improvement in operational parameters of Oil India. However, healthy dividend yield provides some comfort to the investors.

Key Risks

A sharp rise in crude oil & gas price, removal of windfall tax and policy clarity on various duties is key upside risk and continued ad-hoc cess rate, sharp decline in oil price and likely capping of domestic gas price are downside risk.

Additional Data

Key management personnel

Dr. Ranjit Rath	Chairman & Managing Director
Harish Madhav	Director – Finance
Dr. Manas Kumar Sharma	Director - Exploration & Development

Source: Bloomberg

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp of India	11.9
2	Indian Oil Corp Ltd	4.9
3	FMR LLC	2.9
4	Nippon Life India Asset Management Ltd.	2.7
5	Bharat Petroleum Corp Ltd.	2.5
6	Hindustan Petroleum Corp Ltd.	2.5
7	Vanguard Group Inc/The	1.0
8	ICICI Prudential Asset Management Co. Ltd	0.9
9	BlackRock Inc.	0.9
10	L&T Mutual Fund Trustee Ltd	0.4

Source: Bloomberg (old data)

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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