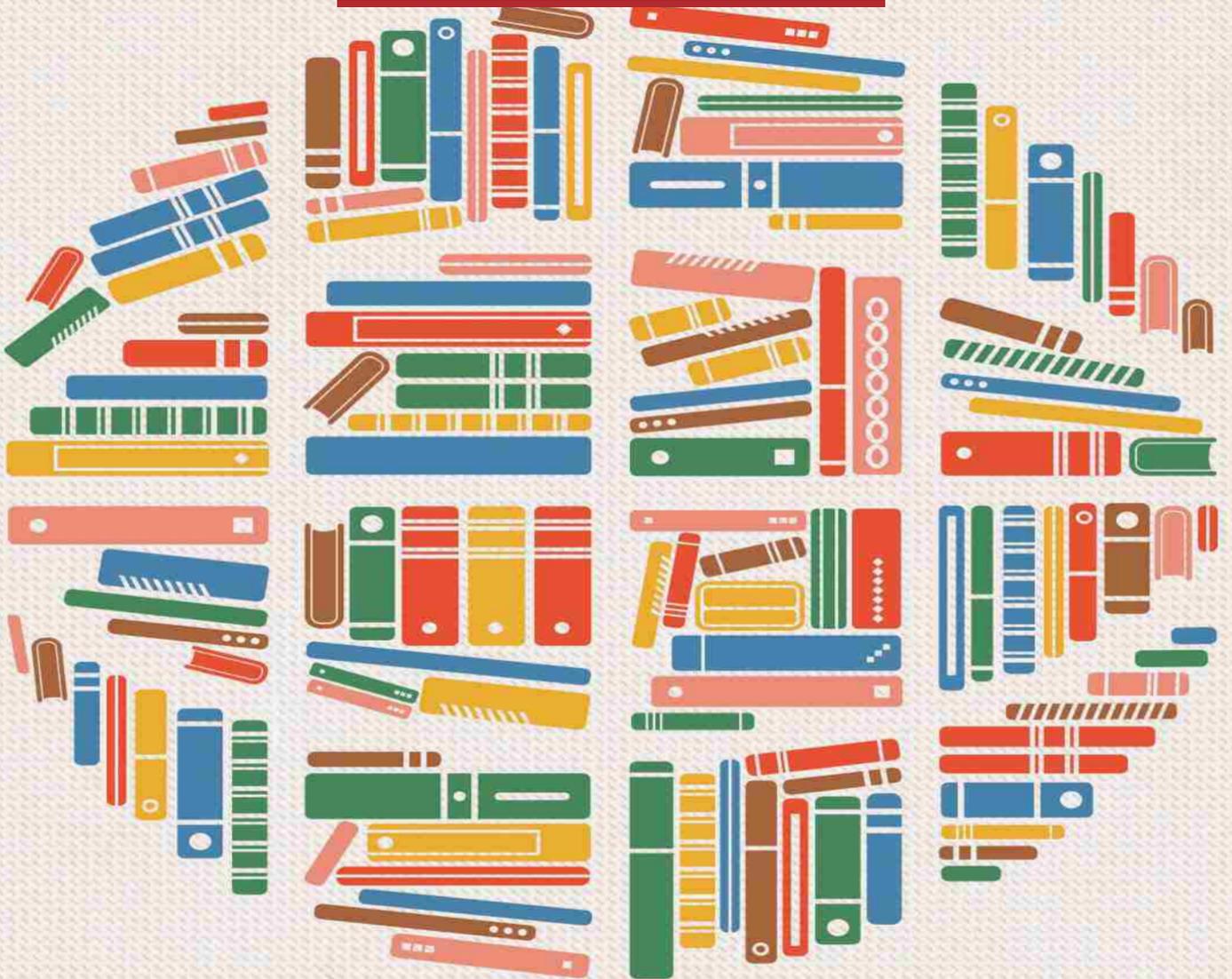


Stock TALES



Stock Tales are concise, holistic stock reports across wider spectrum of sectors. Updates will not be periodical but based on significant events or change in price.

CMP: ₹ 205

Target: ₹ 260 (27%)

Target Period: 12 months

June 19, 2023

BUY

B-80 field set to provide sustained CFs for further developmental activities...

About the stock: Hindustan Oil Exploration Company (HOEC) is India's first private player in the upstream oil & gas sector.

- HOEC holds a portfolio of 11 blocks with eight onshore and three offshore blocks of which it has operatorship in 10 blocks
- In FY23, standalone revenues were at ₹ 381 crore, up 192% YoY, due to commercialisation of B-80 block in Mumbai Offshore and better realisation from Dirok field. Standalone EBITDA came in at ₹ 195.3 crore, up 158% YoY. The company reported a PAT of ₹ 178.5 core, up 398% YoY

Key triggers for future price performance:

- All portfolio assets under revenue mode:** HOEC focuses on discovered oil & gas assets to reduce risk related to exploration. Its portfolio assets (B-80, Dirok, PY-1, Kharsang, Cambay) are all under revenue mode and developmental drillings have been planned to improve production from individual wells (PY-1 in FY24, then proceed with drillings in Dirok, Cambay, B-80)
- Stabilisation of B-80 well:** While B-80 would contribute bulk of profitability for HOEC, the well is being optimised to prolong the plateau of the field life and keep government share to one-third, which would lower cash flow volatility, going ahead. Currently, the gas: oil ratio is declining and thereby would improve product mix for the company in the medium to long term
- Capacity improvement in other assets:** Dirok is being connected directly to Duliajan hub via 35 km pipeline and together with drilling of three developmental wells is expected to improve gas production from current 35 mmscf to 55. Other assets like PY-1, 3 Cambay assets (Asjol, North Balol, Palej) contribute marginally to HOEC valuations. The management expects to unlock field potential by executing approved Field Development Planning (FDP) in the next two years

What should investors do? In the near term, the management plans to reduce the outstanding loans from banks from ₹ 250 crore to less than ₹ 100 crore in FY24, by utilising CFs generated due to higher B-80 production. On the developmental front, the company will initially spend ₹ 64 crore to drill wells in PY-1 (in Q4FY24). Then, in the medium to long term, it will proceed towards drilling more wells in blocks like Dirok (post FY24), B-80 (FY26-27), Cambay (post environmental clearance), etc. **We estimate revenue, EBITDA, PAT to grow 37%, 27%, 28%, respectively, during FY23-25E and FCF yield/RoCE improving to 6%,18%.**

- We initiate coverage under the Stock Tales format with a **BUY** rating

Target Price and Valuation: We value HOEC at ₹ 260 per share (based on DCF)



Particulars

Particular	Amount
Market Capitalization (₹ Crore)	2,711.3
Total Debt (FY23) (₹ Crore)	283.6
Cash and Investments (FY23)	58.6
EV (₹ Crore)	2,936.4
52 week H/L	212/116
Equity capital (₹ Crore)	132.3
Face value (₹)	10.0

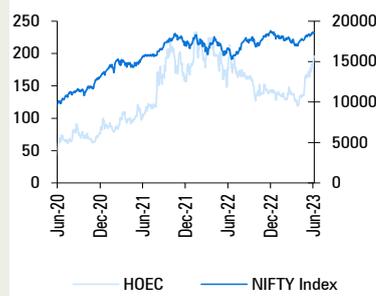
Shareholding Pattern

(in %)	Jun-22	Sep-22	Dec-22	Mar-23
Promoter	0.0	0.0	0.0	0.0
FII	0.8	0.8	0.6	0.6
DII	3.1	2.9	2.7	2.8
Others	96.1	96.4	96.7	96.6

Risks to our call

- Weather related disruption in B-80 well
- Sharp decline in crude oil prices

Price Performance



Research Analyst

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Key Financial Summary

(Year-end March)	FY21	FY22	FY23	5 Year CAGR (FY18-23)	FY24E	FY25E	2 Year CAGR (FY23-25E)
Revenues (₹ crore)	99.4	130.5	381.0	10.0	724.5	719.7	37.4
EBITDA (₹ crore)	49.8	75.7	195.3	2.3	333.8	314.3	26.9
Net Profit (₹ crore)	65.1	35.8	178.5	3.7	312.7	293.2	28.2
EPS (₹)	4.9	2.7	12.4		23.6	22.2	
P/E (x)	41.7	75.7	16.6		8.7	9.2	
Price / Book (x)	3.7	3.5	2.9		2.2	1.8	
EV/EBITDA (x)	55.3	38.6	15.0		8.3	8.7	
RoCE (%)	3.8	6.0	13.8		22.4	17.7	
RoE (%)	8.9	4.7	19.2		25.2	19.1	

Source: Company, ICICI Direct Research

Company Background

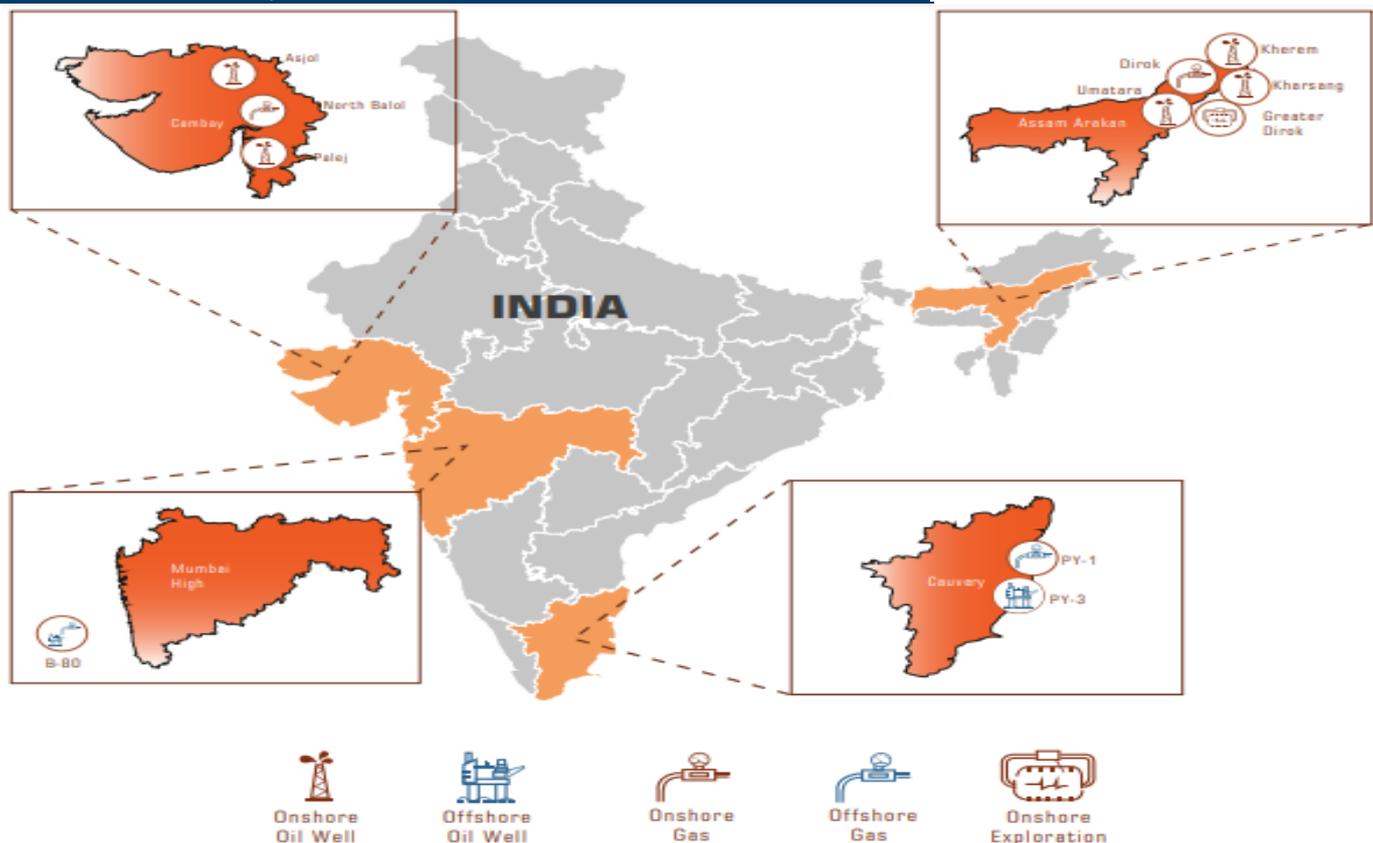
Hindustan Oil Exploration Company (HOEC) is India’s first private player in the upstream oil & gas sector. After its incorporation in 1983, the company was listed on the stock exchange in 1990. Headquartered in Vadodara, HOEC’s operating activities include exploration, development and production of crude oil and natural gas from oilfields.

HOEC assets are geographically spread across Arunachal Pradesh, Assam, Gujarat and Tamil Nadu with balanced portfolio of development and production assets. HOEC holds a portfolio of 11 blocks with eight onshore and three offshore blocks. The portfolio consists of 10 oil & gas blocks of discovered sources and one exploratory block. HOEC has operatorship in 10 out of 11 blocks. As of March 31, 2022, the estimated proved and probable (P+P) reserves were 41.15 MMBOE.

In FY23, average gross production was at 10101* barrels of oil equivalent per day (boepd) and HOEC’s net production was at 3759* boepd (number of days of production for B-80 is taken as 194). Major portion of the production came from Dirok and B-80. In terms of production, crude oil constitutes 19% while natural gas is 81% of total production.

HOEC’s net production was up 54% YoY in FY23. Net gas production grew 46% YoY while oil production grew 40% YoY with commencement of production from B-80. FY23 standalone revenues were at ₹ 381 crore, up 192% YoY, due to commercialisation of B-80 block in Mumbai Offshore and better realisation from Dirok field. Standalone EBITDA came in at ₹ 195.3 crore, up 158% YoY. The company reported a PAT of ₹ 178.5 core, up 398% YoY.

Exhibit 1: HOEC’s asset portfolio

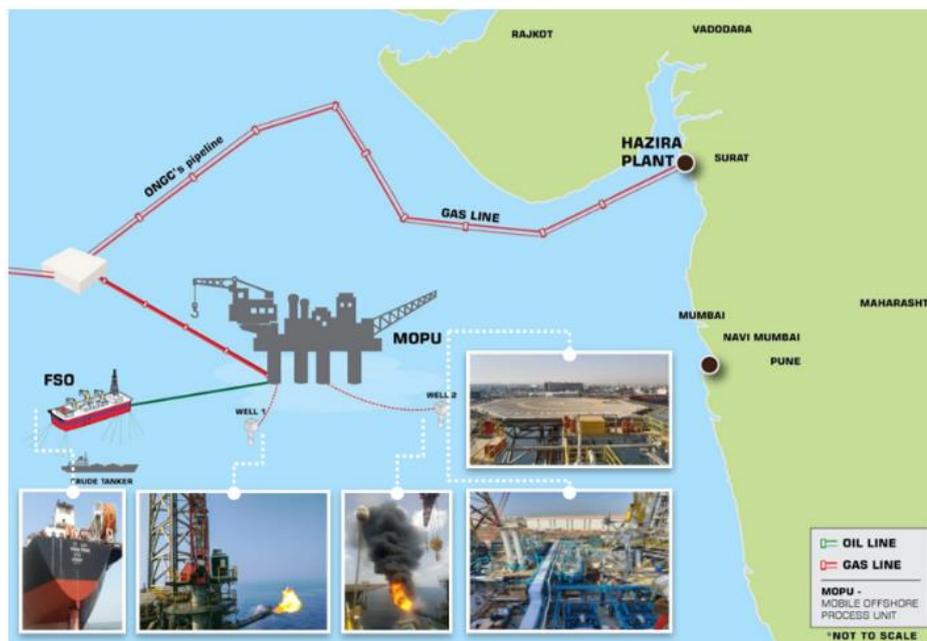


Source: Company, ICICI Direct Research

Investment Rationale

B-80 block to be key for growth in medium term

Exhibit 3: B-80 plant layout



Source: Company, ICICI Direct Research

HOEC was awarded the B-80 block in Discovered Small Field (DSF) bid round in 2016. It is an offshore asset in the Mumbai High basin. HOEC has 60% participating interest (PI) with operatorship in B-80. HOEC was the first operator to get its field development plan approved. The work undertaken during the project involves drilling of two new subsea wells, installing a Mobile Offshore Processing Unit (MOPU), installation of Single Point Mooring System (SPM) and mobilisation of Floating Storage & Offloading (FSO) vessel.

Commercial sales from B-80 to GSPC at Hazira, Gujarat began in June 2022. This involved sharing the facilities of ONGC and Gail through tariff agreements by HOEC and GSPC, respectively.

Q4FY23 HOEC production at B-80 was at ~17 mmscfd of gas and 1350 bopd of oil, with both wells (D1 and D2) operational. Gas export via ONGC and Gail pipeline resumed on November 4, 2022 while oil production commenced on December 8, 2022, which is stored in FSO and set for E-auction by inviting domestic refineries (hence, oil revenues set to be included in FY24). Gas sales agreement has been signed with GSPC and Indian Oil and the pricing is Brent linked. B-80 contributed about ₹ 144 crore of revenue in FY23 (Q3, Q4 were at ₹ 31 crore, ₹ 87 crore, respectively, indicating a significant ramp-up in volumes). Post stabilisation in operations from both wells, **we expect output to improve to 1600 boepd and 1900 boepd in FY24E and FY25E**, respectively (volume mix to change towards higher oil vs gas volumes in the medium to long term, thereby improving overall revenues). The management aims to optimise government revenue share at B-80 field and also maximise field life (maintain reservoir pressure).

Increase in capacity to drive production

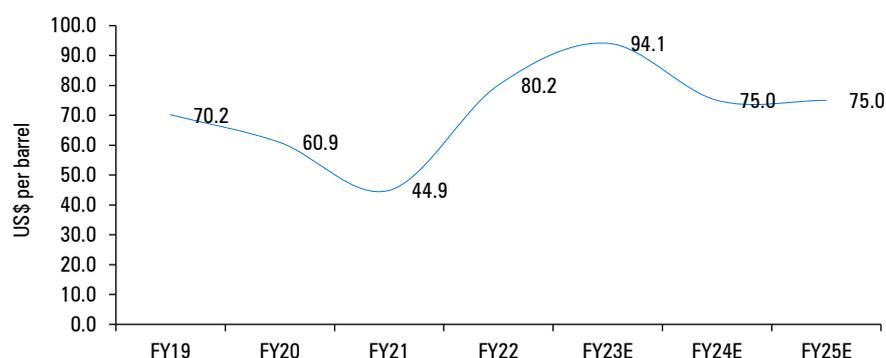
Dirok field emerged as a key asset in the portfolio of HOEC after commencement of commercial production with commissioning of Hollong Modular Gas Processing plant and 12" pipeline in FY18. HOEC incurred capital expenditure of ~₹ 280 crore (gross expenditure: ~₹ 700 crore) for exploration activities during phase 1 of development while development expenditure was in the range of ~₹ 127 crore (gross expenditure: ~₹ 455 crore). HOEC has 26.9% participating Interest (PI) with operatorship in Dirok field. At Dirok, net HOEC production for Q4FY23 was at 1717 boepd (8.1 mmscfd gas and ~137 bopd of oil).

For phase 2 of development, gross capex was planned in the range of ₹ 350 to ₹ 420 crore. The expansion of Hologong Modular Gas Processing plant will be the key as production capacity will increase from 35 mmscfd to 55 mmscfd. Also, a pipeline of 35 km will be laid from Kusijan to Duliajan for marketing of natural gas. Of the total capex budget, 30-40% will be spent on laying the pipeline. The development plan also involves drilling of three wells. Environmental clearance and permission for laying 18" pipeline has been obtained. Delivery of additional gas from Dirok for phase 2 is expected post stabilisation of B-80.

Seven premium gas sales agreement were signed, which increased the realisation to >US\$ 1/mmbtu over and above the government notified prices. As of Q4FY23, share of premium gas sales accounts for 25% of total Dirok sales. As of now, HOEC does not share the profit it earned from production in Dirok field under PSC regime with the government.

We expect net oil & gas production from Dirok at 2019/2030 boepd in FY24E and FY25E, respectively.

Exhibit 4: Brent Crude prices to remain rangebound in FY24-25E



Source: Bloomberg, ICICI Direct Research

Kharsang, PY-1 to lead increase in production

HOEC has 100% participating interest in the offshore PY-1 field in Tamil Nadu along with operatorship. As of FY23, the processing capacity of the field was at 55 mmscfd. PY-1 gas is sold under long-term fixed price contract at US\$ 3.7/mmbtu. Gail is the sole buyer for the gas produced in this field. Production from PY-1 field has declined and the offtake has also been negligible during the year due to customer shutdown. In order to revive the production, additional wells need to be drilled.

HOEC shares profit it earned from production in PY-1 field with the government as per production sharing contract (PSC) regime. The PSC has been extended to October 5, 2030. Revised FDP for PY-1 field has been approved and it includes drilling three new wells, which will sustain current production level for longer. HOEC has 100% stake in PY-1 field, which is going to benefit hugely as company can now explore upside potential with minimal costs.

Post the acquisition of Geopetrol International, HOEC has 30% participating interest, both directly and indirectly, in Kharsang, Arunachal Pradesh. This acquisition has helped HOEC to unlock potential of prospective oil reserves in Kharsang field. Phase 1 Development Plan is currently underway in this field, which involves drilling of 18 wells. Average gross production from Kharsang field for Q4FY23 was 424 boepd. After successful completion of planned Development phase 1, the production from this field is expected to increase to 1800 bopd. This increment in production will come from shallow established reserves. Revised FDP has been approved and mining lease for Kharsang has been granted till June 15, 2030. The company has a Production Sharing Contract with the government.

Newly added fields to contribute to production mix

Three Cambay blocks namely North Balol (HEOC-25% PI), Asjol (HOEC-50% PI) and Palej (HOEC-35%PI) also contribute to revenue mix, although marginally. Average gross production from these blocks was 73 boepd and 0.343 mmscfd of gas in Q4FY23. HOEC has operatorship in all three blocks. It has initiated planning for drilling new wells in the Cambay block to increase production. Approval for the development of two wells has been obtained for Asjol and North Balol. Hook up to Gas Collection Station (GCS) and early Production System (EPS) as part of the FDP will be executed over the next two years. Approval for environmental clearance has been initiated for the two fields. For Palej, ring fenced PSC has been submitted to the Ministry of Petroleum and Natural Gas (MoPNG).

Kherem block was awarded to HOEC in DSF bid round in 2016. The company has 40% participating interest in this block. It is a relatively smaller block with tested oil production of 402 bopd. Petroleum mining lease is still awaited for this field. It will be processed post forest clearance (FC), which is in the final stages. The work for two wells will be completed in three years from the date of PML.

In PY-3 offshore field, HOEC has 21% participating interest with ONGC being the operator. The production from this field was 3300 boepd in 2011. Since then, the field is under shutdown. The company has received approval for PSC extension and the tender is floated for drilling and other services. Government profit share from this field is at 30% as per PSC regime.

HOEC was awarded Umatara under DSF bid round in 2019. HOEC will be joint operator with IOC in Umatara with 10% Participating Interest. Environment Clearance has been approved and FDP approval is under implementation

Greater Dirok (AA-ONHP-2017/19) had been awarded under OALP Bid Round in 2019. HOEC is the operator and has 100% Participating Interest (PI) here. This is an exploratory block adjacent to Dirok. Preliminary Environmental Impact Assessment studies will be conducted for further development and regulatory process.

Incremental CFs to strengthen balance sheet

Volume growth is likely to grow strongly once B-80 is stabilised, as the company wants to focus on the longevity of the field. It expects to pay off its debt obligations by cash flows generated via B-80 field. We expect a healthy RoE and RoCE, going ahead.

Exhibit 5: Financial Summary

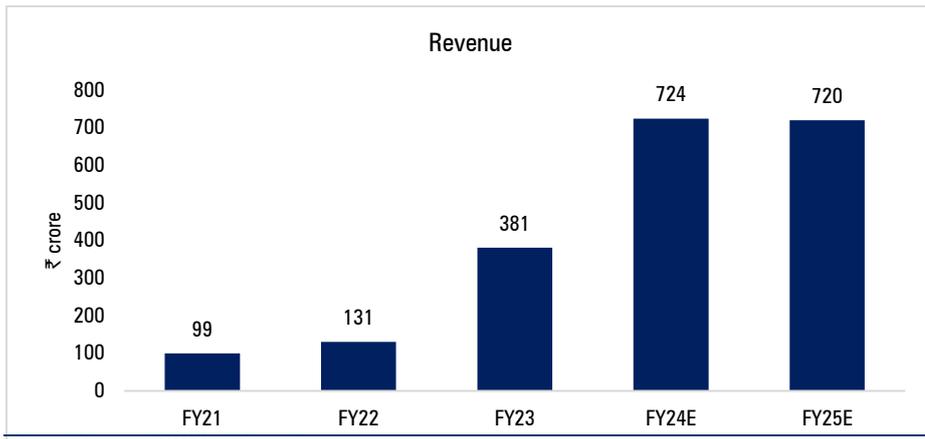
(Year-end March)	FY21	FY22	FY23	FY24E	FY25E
Volume (boepd)	2,460.0	2,441.0	3759*	4,675.0	4,714.9
Revenue (₹ crore)	99.4	130.5	381.0	724.5	719.7
Growth (%)		31%	192%	90%	-1%
EBITDA (₹ crore)	49.8	75.7	195.3	333.8	314.3
EBITDA Margin (%)	50%	58%	51%	46%	44%
PAT (₹ crore)	65.1	35.8	178.5	312.7	293.2
EPS (₹)	4.9	2.7	12.4	23.6	22.2
Balance Sheet					
Equity (₹ crore)	132.3	132.3	132.3	132.3	132.3
Net Worth (₹ crore)	730.2	766.0	929.7	1,242.4	1,535.6
Total Debt (₹ crore)	88.4	256.1	283.6	103.6	53.6
Cash (₹ crore)	46.0	45.4	58.5	41.5	43.4
Ratios					
ROE (%)	8.9	4.7	19.2	25.2	19.1
ROCE (%)	3.8	6.0	13.8	22.4	17.7

*- No of days of production of B-80 is taken as 194

Source : ICICI Direct Research

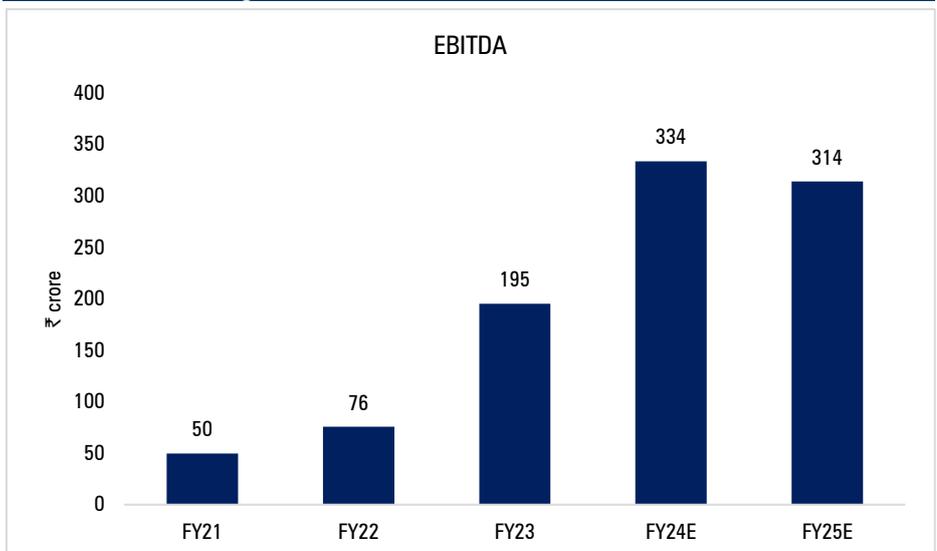
Financial story in charts

Exhibit 5: Revenue expected to grow at 37% CAGR YoY in FY23-25E



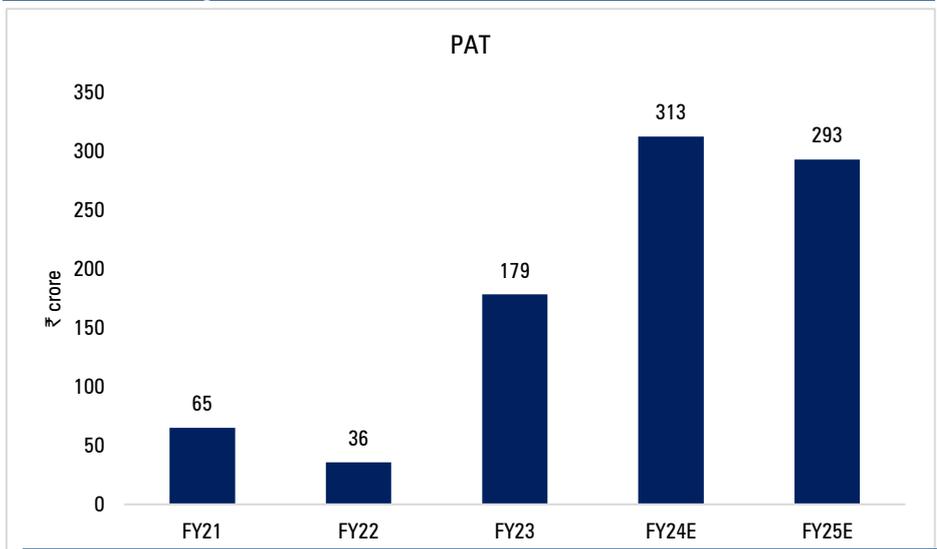
Source: Company, ICICI Direct Research

Exhibit 6: EBITDA to grow at CAGR of 27% over FY23-25E



Source: Company, ICICI Direct Research

Exhibit 7: PAT to grow at 28% CAGR over FY23-25E



Source: Company, ICICI Direct Research

Key risk and concerns

Volatility in oil prices impacting profitability

Oil prices are subject to global market dynamics and geo-political factors. HOEC is exposed to this price volatility as it does not have control over any of these macro factors. Fall in oil prices could cause huge impact on HOEC's profitability.

Lower than estimated production

Weather related disruptions could affect the oil & gas production from the offshore B-80 field.

Unsuccessful exploration activities

Exploration is an investment-heavy business with no assurance of exploration resulting in commercial discovery. In case of absence of commercial discovery, it will be a loss making venture.

Financial Summary

Exhibit 18: Profit & loss statement

(Year-end March)	FY22	FY23	FY24E	FY25E
Revenue	130.5	381.0	724.5	719.7
Growth (%)	31.2	192.0	90.1	-0.7
(Inc./Dec. in stock trade)	22.3	169.5	251.9	267.8
Raw material Costs	25.2	-2.0	109.1	108.2
Employee Costs	0.6	0.6	0.7	0.7
Other Expenditure	6.7	17.6	29.0	28.8
Op. Expenditure	54.8	185.8	390.7	405.5
EBITDA	75.7	195.3	333.8	314.3
Growth (%)	51.9	158.0	70.9	-5.8
Depreciation	14.8	27.7	32.8	32.8
EBIT	60.8	167.6	300.9	281.4
Interest	7.5	17.0	6.2	6.2
Other Income	-17.6	27.9	18.0	18.0
PBT	35.8	178.5	312.7	293.2
Growth (%)	-44.9	398.3	75.2	-6.2
Tax	0.0	0.0	0.0	0.0
Reported PAT	35.8	178.5	312.7	293.2
Growth (%)	-44.9	398.3	75.2	-6.2
EPS	2.7	12.4	23.6	22.2

Source: Company, ICICI Direct Research

Exhibit 19: Cash flow statement

(Year-end March)	FY22	FY23	FY24E	FY25E
Profit after Tax	35.8	178.5	312.7	293.2
Add: Depreciation	14.8	27.7	32.8	32.8
Add: Others	0.0	0.0	0.0	0.0
Cash Profit	50.7	206.2	345.5	326.0
Increase/(Decrease) in CL	36.6	104.5	199.2	-2.7
(Increase)/Decrease in CA	-46.1	-147.4	-179.2	-68.5
CF from Operating Acti	110.4	183.5	365.6	254.8
Purchase of Fixed Assets	174.9	65.9	102.7	102.9
(Inc)/Dec in Investments	30.0	-114.4	-100.0	-100.0
Others	0.0	0.0	0.0	0.0
CF from Investing Acti	-278.6	-183.1	-202.7	-202.9
Inc/(Dec) in Loan Funds	167.7	27.5	-180.0	-50.0
Less: Dividend Paid	0.0	0.0	0.0	0.0
Inc/(Dec) in Sh. Cap. & Res	0.0	-14.8	0.0	0.0
Others	0.0	0.0	0.0	0.0
CF from financing acti	167.6	12.7	-180.0	-50.0
Change in cash Eq.	-0.6	13.1	-17.0	1.9
Op. Cash and cash Eq.	46.0	45.4	58.6	41.5
Cl. Cash and cash Eq.	45.4	58.5	41.5	43.4

Source: Company, ICICI Direct Research

Exhibit 18: Profit & loss statement

(Year-end March)	FY22	FY23	FY24E	FY25E
Source of Funds				
Equity Capital	132.3	132.3	132.3	132.3
Preference Capital	0.0	0.0	0.0	0.0
Reserves & Surplus	633.7	797.4	1,110.1	1,403.4
Shareholder's Fund	766.0	929.7	1,242.4	1,535.6
Loan Funds	256.1	283.6	103.6	53.6
Deferred Tax Liability	0.0	0.0	0.0	0.0
Well Abandonment Fund	0.0	0.0	0.0	0.0
Source of Funds	1022.1	1213.3	1346.0	1589.2
Application of Funds				
Net Block	292.0	797.6	864.7	931.9
Capital WIP	511.4	26.6	29.3	32.2
Producing Properties	0.0	0.0	0.0	0.0
Pre-Producing Properties	0.0	0.0	0.0	0.0
Total Fixed Assets	803.4	824.2	894.0	964.1
Investments	59.8	174.2	274.2	374.2
Inventories	5.7	78.3	148.8	147.8
Debtor	13.6	42.9	81.5	81.0
Cash	45.4	58.6	41.5	43.4
Loan & Advance, Other C,	347.4	393.0	463.0	533.0
Total Current assets	412.2	572.7	734.8	805.2
Current Liabilities	138.0	221.1	420.3	417.6
Provisions	115.3	136.7	136.7	136.7
Total CL and Provisions	253.3	357.7	557.0	554.2
Net Working Capital	158.9	214.9	177.8	250.9
Miscellaneous expense	0.0	0.0	0.0	0.0
Application of Funds	1022.1	1213.3	1346.0	1589.2

Source: Company, ICICI Direct Research

Exhibit 19: Cash flow statement

(Year-end March)	FY22	FY23	FY24E	FY25E
Per share data (₹)				
Book Value	57.9	70.3	93.9	116.1
Cash per share	3.4	4.4	3.1	3.3
EPS	2.7	12.4	23.6	22.2
Cash EPS	3.8	14.5	26.1	24.7
DPS	0.0	0.0	0.0	0.0
Profitability & Operating Ratios				
EBITDA Margin (%)	58.0	51.2	46.1	43.7
PAT Margin (%)	27.5	46.8	43.2	40.7
Fixed Asset Turnover (x)	0.2	0.5	0.8	0.7
Inventory Turnover (Days)	16.0	75.0	75.0	75.0
Debtor (Days)	38.0	41.1	41.1	41.1
Current Liabilities (Days)	385.9	211.8	211.8	211.8
Return Ratios (%)				
RoE	4.7	19.2	25.2	19.1
RoCE	6.0	13.8	22.4	17.7
RoIC	6.2	14.5	23.1	18.2
Valuation Ratios (x)				
PE	70.1	15.4	8.0	8.6
Price to Book Value	3.3	2.7	2.0	1.6
EV/EBITDA	36.0	14.0	7.7	8.0
EV/Sales	20.9	7.2	3.6	3.5
Leverage & Solvency Ratios				
Debt to equity (x)	0.3	0.3	0.1	0.0
Interest Coverage (x)	8.2	9.8	48.4	45.3
Debt to EBITDA (x)	3.4	1.5	0.3	0.2
Current Ratio	1.6	1.6	1.3	1.5
Quick ratio	1.6	1.4	1.1	1.2

Source: Company, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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