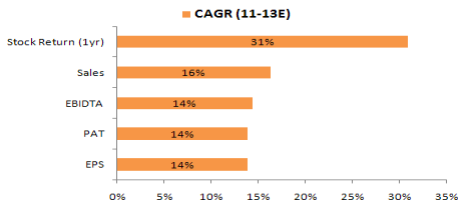




4Q FY11 Result Review

Industry Oil & Gas

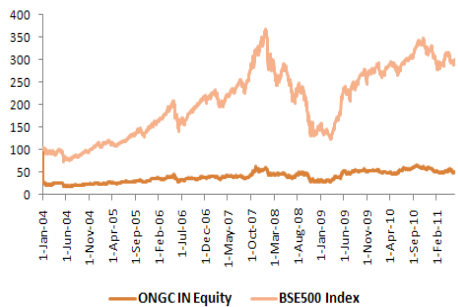


Price	282
Target Price	369
Last call	BUY (29-10-10 at ₹ 381)
Expected share price return	30.85%
Expected dividend yield	3.90%
Expected total return	34.75%

Market Data

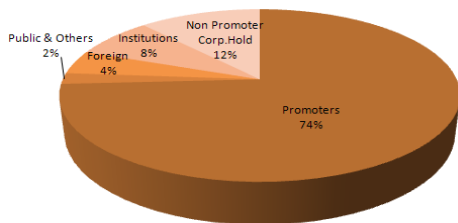
Market Cap.	₹ 2413bn/ US 53\$b
Share Cap. (mn)	85,555
52 Wk High/Low	368/261
Avg. Vol. (Weekly)	5858000

(Price Performance (RIC: ONGC.BO, BB: ONGC IN))



Shareholding Pattern

(As on 31 March, 2011) (%)



Financials (₹. Mn)	FY11	FY12E	FY13E
Net Sales	1219293	1477221	1647437
EBIDTA	527550	627453	689612
PBT	343189	436018	453925
PAT	224555	282551	291164
EPS (₹.)	26.2	33.0	34.0
EBIDTA Margin (%)	43.27%	42.48%	41.86%
PAT margin (%)	18.42%	19.13%	17.67%
Price/Earnings (x)	10.7	8.5	8.3
EV/EBIDTA	4.1	3.7	3.5
ROE (%)	14%	15%	14%
ROCE (%)	16%	18%	16%

ONGC (ONGC IN)

June 1, 2011

Higher subsidy burden dampens 4Q performance

BUY (CMP: ₹282)

Mkt Cap ₹2413bn; USD53bn

Despite better operating performance, ONGC reported lower 4Q PAT at ₹28bn down 26% YoY mainly on account of higher subsidy burden. Besides higher crude oil prices that led to higher under-recoveries for FY11, the Government also increased upstream contribution in subsidy sharing to 38.7% in FY11 v/s 33% as indicated earlier. The entire impact of the incremental subsidy burden was reflected in 4Q results. We have revised our oil price forecasts upwards for FY12E-13E to US\$95-90/bbl (up ~20%) and long term to US\$80/bbl (up ~7%), on the back of sustained economic recovery. However, we are cutting our EPS estimates for FY12-13 by 3-7% to ₹ 33-34/share and FV by 3% to ₹ 369/share mainly led by cut in production estimates based on recent guidance and updates. In the current scenario of high oil prices and lack of clarity on reforms, we believe upstream companies are better placed than downstream companies. We thus reiterate "BUY" with TP of ₹369/share.

4Q PAT down 26% YoY at ₹28bn led by higher subsidy burden- up ~2.5x YoY in 4Q

ONGC reported standalone PAT of ₹28bn for 4Q FY11, down 26% YoY. 4Q PAT is impacted by the subsidy burden which is higher by ~2.5x YoY, led by higher crude oil prices and adjustment for the increased share of upstream companies in subsidy burden i.e. at 38.7% now v/s 33% earlier. Net oil price realisation came in at US\$39/bbl for 4Q v/s US\$51/bbl for 4Q FY10 and US\$65/bbl for 3Q FY11. The 4Q PAT was largely in line with our expectation. FY11 standalone PAT was up 13% YoY to ₹189bn while consolidated PAT was up 16% YoY to ₹225bn. ONGC still managed to report YoY PAT growth in FY11 despite higher subsidy burden mainly due to i) higher gas prices (post the hike in APM prices in May 2010 and subsequent hike in non-APM prices too); and ii) Gas pool money of ₹19bn. Besides, higher oil prices and higher output in OVL too supported the consolidated earnings growth

Revising earnings forecasts down 3-7% for FY12-13 led by production cuts for ONGC & OVL

We are revising our oil price assumptions for FY12-FY13 up by ~20% and our long term price up by ~7% to US\$95-90/bbl and US\$80/bbl respectively, on the back of clearer trends of economic recovery driving crude oil prices. However, we are cutting our EPS estimates for FY12-13 by 3-7% to ₹ 33-34/share despite of higher oil prices assumptions mainly on account of revised production estimates that have been altered downwards (see table 7) for both ONGC and OVL in light of the latest guidance and trends from the company. Our FV now stands at ₹369/share down 3% as compared to our earlier estimate of ₹ 381/share.

CMP offers an excellent buying opportunity; Re-inforce "BUY"

ONGC's recent underperformance v/s market and peers reflects concerns on rising oil and product prices coupled with lack of clarity on subsidies & reforms. However, we believe there are various catalysts for the stock from here on. These include i) modest hike in diesel prices & LPG/ kerosene prices; ii) Reimbursement of royalty on Cairn crude (₹13bn paid on this account in FY11); and iii) Possibility of government reverting back to 1/3rd subsidy sharing formula in FY12E. ONGC's CMP discounts <US\$50/bbl effective long-term Brent price v/s US\$71/bbl assumed by us in our DCF value of ₹369/share. Further, the CMP does not even factor its 2P reserves entirely – CMP factors in ₹234/share of 2P reserves valuation v/s ₹321/share valued by us. At just 8.5x FY12E EPS (v/s historical avg of ~10x), ONGC's valuations are very compelling. Reiterate "BUY".

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Table 1: ONGC FY11 results (standalone)

₹-million	4Q FY11A	4Q FY10	% Chg	FY11	FY10	% Chg
Net sales	161,079	160,023	0.7	691,654	616,455	12.2
Total expenditure	81,357	65,843	23.6	281,466	244,912	14.9
EBDITA	79,723	94,180	-15.4	410,188	371,543	10.4
EBDITA margin	49.5%	58.9%		59.3%	60.3%	
Interest	160	561	-71.5	251	687	-63.4
Depreciation	47,877	44,480	7.6	159,430	146,588	8.8
Other Income	5,856	4,691	24.8	25,682	25,570	0.4
PBT	37,542	53,831	-30.3	276,189	249,838	10.5
Tax	9,633	16,066	-40.0	86,950	82,163	5.8
Recurring PAT	27,909	37,764	-26.1	189,239	167,676	12.9
Add :Extra-ordinary items	0	0		0	0	
PAT	27,909	37,764	-26.1	189,239	167,676	12.9
Recurring EPS (₹/sh)	3.3	4.4	-26.1	22.1	19.6	12.9
Reported EPS (₹/sh)	3.3	4.4	-26.1	22.1	19.6	12.9

Source: Company, Systematix Institutional Research

Table 2: ONGC FY11 results (Consolidated)

₹-million	FY11	FY10	% Chg
Net sales	1,219,293	1,034,389	17.9
Total expenditure	691,743	573,211	20.7
EBDITA	527,550	461,177	14.4
EBDITA margin	43.3%	44.6%	
Interest	4,374	5,564	-21.4
Depreciation	206,284	187,391	10.1
Other Income	26,271	36,192	-27.4
PBT	343,163	304,414	12.7
Tax	114,913	107,138	7.3
PAT	228,250	197,276	15.7
Less: Minority Interest	(3,690)	(3,240)	
PAT	224,559	194,035	15.7
Reported EPS (₹/sh)	26.2	22.7	15.7

Source: Company, Systematix Institutional Research

Table 3: ONGC's subsidy

₹mn	4Q FY11A	4Q FY10	% YoY Chg	3Q FY11	% QoQ chg
Subsidy	121,353	49,990	143%	42,220	187%
Subsidy (US\$/bbl)	70.1	28	153%	24	188%
Bonny Light (US\$/bbl)	108.9	79	38%	89	22%
	38.7	51.4	-25%	64.8	-40%

Source: Company, Systematix Institutional Research

Table 4: Sales Volumes

	4Q FY11A	4Q FY10	Change
Sales volumes			
Crude oil (mmt)	5.83	5.67	2.8%
Natural gas (bcm)	4.98	5.04	-1.2%
'000 tonnes			
LPG	286	291	-2%
Naphtha	411	403	2%
Ethane and propane	126	135	-7%
Kerosene	22	37	-41%

Source: Company, Systematix Institutional Research

Table 5: Valuation of ONGC

Price realisation	mmboe	USD/boe	USDm	₹/share
2P reserves	9,456	6.5	61,029	321
Net cash			4,943	26
Value of investments			4,183	22
			70,154	369
CMP (₹)				282
Upside (%)				30.9%

Source: Company and Systematix Institutional Research

Table 6: Even 2P reserves not entirely factored in current share price of ONGC

	DCF	Current price
Reserves and resources (mmboe)		
2P reserves	10,042	7,302
E&P valuation (₹/share)		
2P reserves	321	234
Net cash and value of investments	48	48
Sum of parts valuation	369	282

Source: Company and Systematix Institutional Research

Table 7: Change in Production estimates

Change in Production estimates		FY12	FY13
Oil production for ONGC (mmt)	Old	27.6	28.7
	New	27.6	27.8
	% Change	0.0%	-2.9%
Gas production for ONGC (bcm)	Old	26.4	28.5
	New	25.4	25.6
	% Change	-3.5%	-10.2%
Oil Production for OVL (mmt)	Old	6.6	9.0
	New	6.0	6.8
	% Change	-8.8%	-24.8%

Source: Company, Systematix Institutional Research

Table 8: Revised Oil Price

Revised Oil Price (US\$/bbl)	FY12	FY13	Long Term
Old	80	75	75
New	95	90	80
% Change	19%	20%	7%

Source: Company, Systematix Institutional Research

Table 9: Earnings Revision

Earnings Revision (₹/share)	FY12	FY13
Old	34.1	36.5
New	33.0	34.0
% Change	-3%	-7%

Source: Company, Systematix Institutional Research

Oil production cut in FY13 for OVL of ~25% is mainly driven by change in production estimates for Carabobo, which is expected to reach peak production of 400,000 bbl/day only in year 2017. We have thus now assumed a slower ramp up as compared to our earlier estimates...

Financials (Consolidated)

Table 10: ONGC's Profit & Loss Statement

₹-million	FY09	FY10	FY11A	FY12E	FY13E
Revenue	1,052,567	1,017,605	1,219,293	1,477,221	1,647,437
Total expenditure	(627,028)	(573,211)	(691,743)	(849,768)	(957,825)
EBITDA	425,539	444,393	527,550	627,453	689,612
Depreciation	(155,705)	(187,391)	(206,284)	(211,410)	(251,510)
Interest	(2,386)	(5,564)	(4,374)	(5,151)	(5,328)
Other Income	43,589	53,054	26,301	25,126	21,152
Extra-ordinary/prior period items	331	0	(4)	0	0
PBT	311,368	304,492	343,189	436,018	453,925
Tax	(109,870)	(107,138)	(114,913)	(151,014)	(159,143)
Reported Profit	201,498	197,354	228,276	285,004	294,782
Minority interest	(3,648)	(3,319)	(3,720)	(2,453)	(3,618)
Consolidated reported profit	197,850	194,035	224,555	282,551	291,164
Consolidated recurring profit	197,632	194,035	224,558	282,551	291,164
Outstanding shares	8,555	8,555	8,555	8,555	8,555
Reported EPS	23.1	22.7	26.2	33.0	34.0
y-o-y change		-2%	16%	26%	3%
Recurring EPS	23.1	22.7	26.2	33.0	34.0
y-o-y change	-1%	-2%	16%	26%	3%
EBITDA Margin	40.4%	43.7%	43.3%	42.5%	41.9%

Source: Company and Systematix Institutional Research

Table 11: ONGC's Cash flows

₹-million	FY09	FY10	FY11A	FY12E	FY13E
Net profit	201,498	197,354	228,276	285,004	294,782
Add: deferred tax	4,855	10,681	8,614	-11,694	153
Add: Depreciation	245,094	163,861	184,519	178,763	208,862
	451,447	371,896	421,408	452,072	503,798
Less: Change in working capital	9,141	-18,956	-68,657	170,879	17,683
Less: dividend	77,386	79,802	87,586	110,108	120,118
	364,921	311,051	402,479	171,085	365,997
Less change in investment	78,244	-1,864	-23,489	-137	50,000
Less: Capex	409,553	315,245	388,030	300,561	377,645
	-122,876	-2,330	37,938	-129,340	-61,648
Add: change in equity	0	0	0	2	0
Less: repayment of debt	-98,273	-217	-24,156	-39,340	-9,999
Change in cash balance	-24,603	-2,113	62,095	-89,997	-51,649

Source: Company and Systematix Institutional Research

Table 12: ONGC's Balance Sheet

₹-million	FY09	FY10	FY11A	FY12E	FY13E
Assets					
Gross fixed assets	784,248	866,131	1,000,436	1,094,724	1,179,520
Less: accumulated depreciation	599,292	624,335	659,512	703,956	750,248
Net fixed assets	184,956	241,796	340,924	390,768	429,271
Capital work in progress	165,222	178,005	201,513	155,225	131,225
Net fixed assets and Capital WIP	350,178	419,801	542,437	545,993	560,496
Producing properties	452,980	511,665	571,896	637,548	767,419
Exploratory wells in progress	82,359	80,125	102,379	159,223	183,631
Investments	34,803	51,593	33,561	38,492	88,492
Cash and bank balance	225,956	223,842	286,883	196,885	145,236
Current Assets					
Inventories	40,607	46,786	39,759	47,587	52,488
Sundry debtors	70,839	60,587	85,663	96,623	103,485
Other current assets	283,784	269,834	266,942	293,681	313,307
	395,230	377,207	392,363	437,891	469,280
Less: Current liabilities					
Sundry creditors	97,433	57,998	69,891	82,000	89,379
Dividend provision	35,189	35,290	37,430	47,055	51,332
Other liabilities	149,767	208,689	283,925	141,909	143,958
	282,390	301,977	391,246	270,963	284,669
Net current assets	112,840	75,230	1,117	166,928	184,611
Total assets	1,259,116	1,362,257	1,538,273	1,745,069	1,929,886
Liabilities					
Borrowings	65,591	62,669	62,912	102,252	112,251
Liability for abandonment costs	171,451	174,590	198,504	198,504	198,504
Deferred tax liability	92,231	102,912	111,526	99,832	99,985
Minority interest	14,114	16,432	20,018	22,470	26,088
Equity share capital	21,389	21,389	42,778	42,780	42,780
Reserves and surplus	894,340	984,264	1,102,534	1,279,231	1,450,277
	915,729	1,005,653	1,145,312	1,322,011	1,493,057
Total liabilities	1,259,116	1,362,257	1,538,273	1,745,069	1,929,886

Source: Company and Systematix Institutional Research

Table 13: ONGC's Valuations

₹-million	FY09	FY10	FY11A	FY12E	FY13E
Recurring EPS	23.1	22.7	26.2	33.0	34.0
PE	12.2	12.4	10.7	8.5	8.3
DPS	8.0	8.3	8.8	11.0	12.0
Yield	2.8%	2.9%	3.1%	3.9%	4.3%
Book Value	107	118	134	155	175
P/BV	2.6	2.4	2.1	1.8	1.6
EV/EBITDA	5.3	5.1	4.1	3.7	3.5
ROCE	17.8%	15.6%	15.7%	17.5%	16.4%
ROE	15.2%	13.3%	13.6%	14.9%	13.5%

Source: Company and Systematix Institutional Research

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BUY (B)	The stock's total return is expected to exceed 20% over the next 12 months.
ACCUMULATE (A)	The stock's total return is expected to be within 10-20% over the next 12 months.
HOLD (H)	The stock's total return is expected to be within 0-10% over the next 12 months.
SELL (S)	The stock's is expected to give negative returns over the next 12 months.
NOT RATED (NR)	The analyst has no recommendation on the stock under review.

Industry Views

ATTRACTIVE (AT)	Fundamentals /Valuations of the sector is expected to be attractive over the next 12-18 months.
NEUTRAL (NL)	Fundamentals /Valuations of the sector are expected to neither improve nor deteriorate over the next 12-18 months.
CAUTIOUS (CS)	Fundamentals /Valuations of the sector is expected to deteriorate over the next 12-18 months.

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