

Operational metrics improving, regulatory concerns remain

Results highlights

Strong earnings - surpassing expectations

ONGC reported adjusted net profit of INR57.6bn (one-off of INR18.9bn received from gas pool account), which was up 89% YoY and 7% QoQ. Earnings are 7% above our estimates due to lower than expected DD&A of INR36bn (down INR8bn QoQ). Net realisations improved to USD64.8/bbl as compared to USD62.8/bbl in 2QFY11. Subsidy payout stood at INR42.2bn, up 21% YoY and 40% QoQ on account of 15% QoQ rise in oil prices.

Operational metrics improving

ONGC reported strong operating performance with crude oil production (incl JVs) up 6% YoY and 3% QoQ due to higher oil production from Cairn's Rajasthan block. Gas production including JVs was down 2% YoY but up 2% QoQ as production resumed at PMT field post a platform shutdown in 2QFY11 and part of 3QFY11. ONGC maintained its MoU production target for FY11e at 27.4mmt and 23.8bcm for oil and gas respectively, rising to 28.2mmt and 25.5bcm in FY12e.

Key triggers

Key positive triggers in our view to watch out for the stock are: (i) clarity on oil price linked subsidy sharing mechanism; (ii) moderate diesel prices hikes to check rising under-recoveries and (iii) clarity on compensation of royalty paid on Cairn's share in Rajasthan block.

Valuation and outlook

We lower our EPS estimate for FY11e and FY12e to INR112/share (-9%) and INR121/share (-6%) respectively. This is on account of higher expected DD&A expense and lower realisations due to higher under-recoveries driven by increased oil price assumption and slower pace of diesel price hikes. We value ONGC based on the sum-of-the-parts valuation. We reiterate BUY on ONGC with a revised target price of INR1,458/share from INR1,552/share earlier.

3QFY financial highlights

INRm	3QFY11	3QFY10	Chg (%)	9MFY11	9MFY10	Chg (%)
Net Sales	185,864	153,145	21	504,456	452,744	11
EBITDA	113,138	91,430	24	304,348	273,675	11
EBITDA Margin (%)	61	60	2	60	60	(0)
PAT	57,618	30,536	89	148,117	129,911	14
EPS (INR)	26.9	14.3	89	69.2	60.7	14
Gross realisation (USD/bbl)	89	77	16	83	69	20
Discount to OMCs (USD/bbl)	24	19	28	24	12	106
Net realisations (USD/bbl)	65	58	12	59	57	2
DD&A	36,410	46,758	(22)	111,553	102,108	9

Source: Company, Antique

Current Reco	: BUY
Previous Reco	: BUY
CMP	: INR1,136
Target Price	: INR1,458
Potential Return	: 28%

Market data

Sector	:	Oil & Gas
Market Cap (INRbn)	:	2,423
Market Cap (USDbn)	:	53
O/S Shares	:	2,139
Free Float (m)	:	230
52-wk HI/LO (INR)	:	1473/996
Avg Daily Vol ('000)	:	1,311
Bloomberg	:	ONGC IN
Reuters	:	ONGC.BO

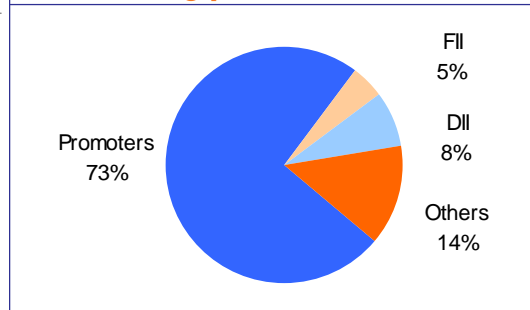
Source: Bloomberg

Returns (%)

	1m	3m	6m	12m
Absolute	(12)	(13)	(10)	3
Relative	(4)	(6)	(12)	(9)

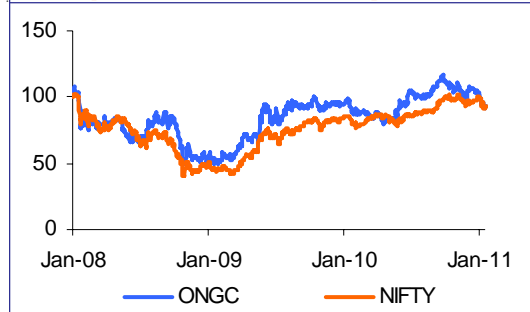
Source: Bloomberg

Shareholding pattern



Source: BSE

Price performance vs Nifty



Source: Bloomberg

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Results highlights

- One-offs during the quarter included INR18.9bn received from the Gas Pool Account in the form of TDRs and INR0.6bn of tax provision write back. We have adjusted INR13.2bn (net of taxes) in reported profit of INR70.8bn to arrive at our adjusted net profit of INR57.6bn. Management guided that INR4bn now remains with GAIL as part of the Gas Pool Account with rest received by ONGC in this quarter.
- Depreciation expense during 3QFY11 stood at INR36bn, down INR8bn QoQ and INR10bn YoY, largely due to lower dry well provisions. We believe DD&A expense to increase in 4QFY11 due to seasonality as well as charter of a deep water rig in Dec 2010.
- Other income shot up 153% QoQ to INR28.8bn due to disbursement from the Gas pool account as well as higher interest income on site restoration fund where accounted interest rates increased from 6% in 1HFY11 to 8.5% in 9MFY11. Interest on site restoration fund is accounted based on SBI deposit rate at last day of financial year, however, adjusted on a quarterly basis for interest rates at the quarter end. Hence, ONGC booked additional interest income of ~1.3bn.

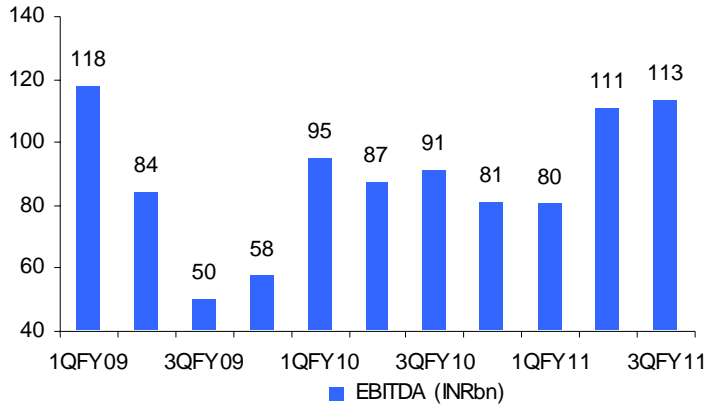
ONGC 3QFY11 conference call highlights

- ONGC maintained its production target for FY11e at 27.4mmt and 23.8bcm for oil and gas rising to 28.2mmt and 25.5bcm in FY12e, respectively.
- Total 96 wells were drilled in 3QFY11, of which 3 were deep water, 50 shallow water and remaining onshore wells. Of the above, 29 were exploratory wells with 3 being deep water, 7 shallow water and 19 onshore wells. The 3 deep water wells comprised of 2 appraisal wells and 1 exploratory well.
- OVL produced 5mmt of oil and 2bcm of gas for 9MFY11 (up 9% YoY). OVL production is expected to remain flat for FY12e over FY11 and material growth will only be seen in FY13e with incremental production from Myanmar and Venezuela's Carabobo project.
- Production of value added products declined YoY due to closure in Uran plant and lower gas production from Panna Mukta. Bombay high production slightly increased to 8.1mmt for 9MFY11 on account of efficient IOR and EOR techniques.
- Total royalty paid for Rajasthan block during 3QFY11 stand at INR5.5bn, of which royalty paid for Cairn's share was at INR3.8bn. For 9MFY11, total royalty on Rajasthan block is INR11.8bn (including Cairn's share of INR8.3bn).

Valuation and outlook

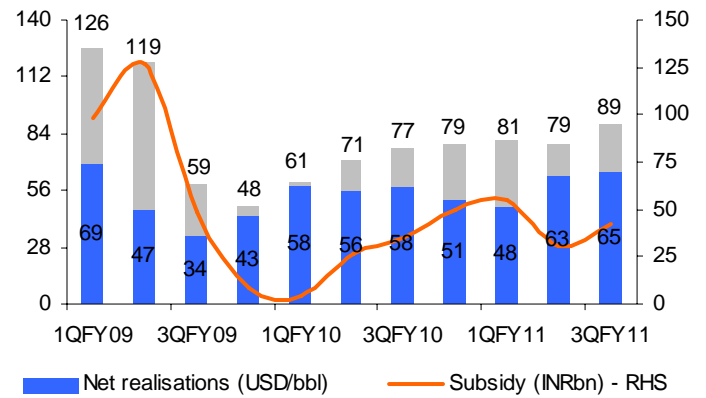
We lower our EPS estimate for FY11e and FY12e to INR112/share (-9%) and INR121/share (-6%) respectively. This is on account of higher expected DD&A expense and lower realisations due to higher under-recoveries driven by increased oil price assumption and slower pace of diesel price hikes. We value ONGC based on the sum-of-the-parts valuation. We reiterate BUY on ONGC with a revised target price of INR1,458/share from INR1,552/share earlier. We value the core business including OVL at INR1,421/sh, applying 11x multiple on FY12e EPS of INR121/sh, 30% share in Cairn MBA field's at INR25/sh, 11% stake in Venezuela's Carabobo project at INR27/sh and the listed investments at INR79/sh.

EBITDA up 24% YoY aided by higher production and improved realisations



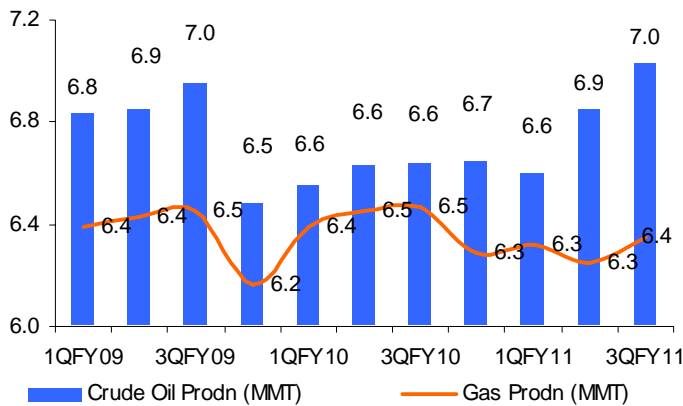
Source: Company, Antique

Realisations improved 3% QoQ to USD64.8/bbl on account of lower total under-recoveries



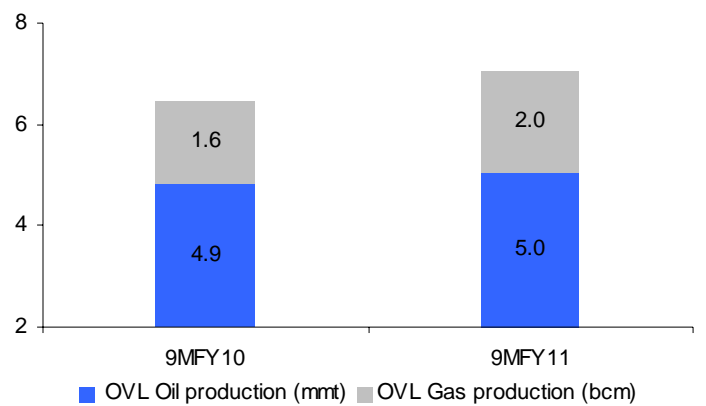
Source: Company, Antique

O&G production up 2% YoY and QoQ due to higher production from Rajasthan and PMT fields



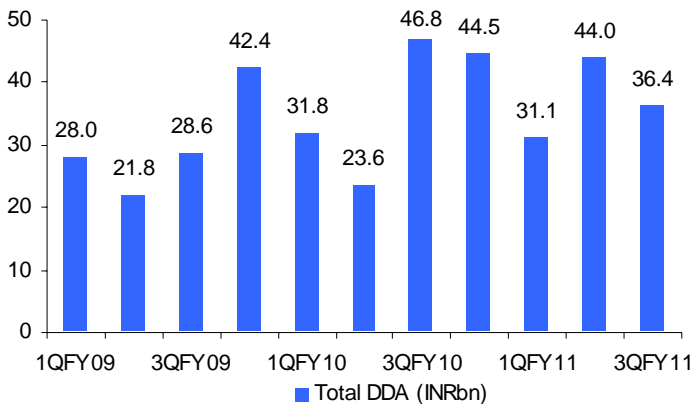
Source: Company, Antique

OVL 9MFY11 O&G production up 9% YoY



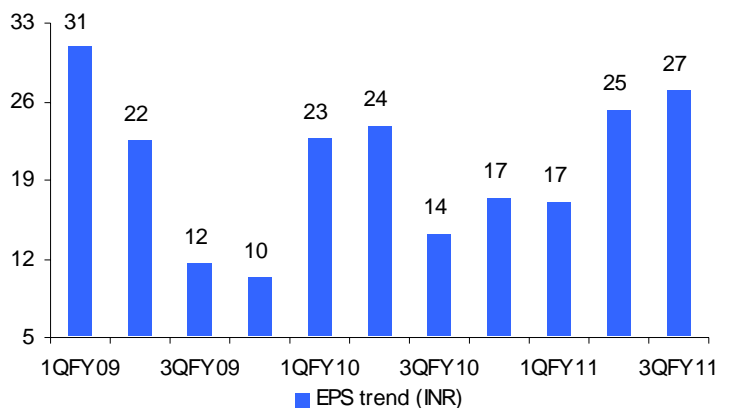
Source: Company, Antique

DD&A declined by INR8bn QoQ due to lower dry well expense



Source: Company, Antique

Earnings on a rising trend due to improving net realisations



Source: Company, Antique

Financials

Profit and loss account (INRbn)

Year ended 31st Mar	2008	2009	2010	2011e	2012e
Revenues	604	643	603	702	750
Expenses	(301)	(331)	(248)	(276)	(298)
EBITDA	303	312	355	426	452
Depreciation & amortisation	(98)	(121)	(147)	(148)	(147)
EBIT	205	191	208	277	304
Interest expense	(1)	(1)	(1)	(1)	(1)
Other income	48	49	42	36	34
Profit before tax	252	239	250	313	337
Tax	(85)	(79)	(82)	(103)	(111)
Profit after tax	167	160	168	210	227
Recurring EPS (INR)	78	75	78	98	106
Consolidated EPS (INR)	89	88	88	112	121

Balance sheet (INRbn)

Year ended 31st Mar	2008	2009	2010	2011e	2012e
Share Capital	21	21	21	21	21
Reserves & Surplus	685	766	851	981	1,128
Networth	706	787	872	1,003	1,150
Debt	125	160	160	160	160
Capital Employed	831	948	1,033	1,163	1,310
Gross Fixed Assets	1,232	1,371	1,579	1,780	1,980
Accumulated Depreciation	(825)	(905)	(1,052)	(1,201)	(1,348)
Net Assets	407	466	527	580	632
Capital work in progress	110	168	191	213	235
Investments	59	51	51	51	51
Current Assets Loans & Advances					
Inventory	39	41	38	45	48
Debtors	44	41	38	45	48
Cash & Bank	224	191	200	267	348
Loans & advances and others	347	274	274	274	274
Current Liabilities & Provisions					
Creditors	109	130	123	143	153
Other liabilities & provisions	222	81	86	86	88
Net Current Assets	322	335	342	401	477
Deferred tax assets/(liabilities)	(74)	(78)	(85)	(89)	(92)
Misc expenses	7	7	7	7	7
Application of Funds	831	948	1,033	1,163	1,310

Per share data

Year ended 31st Mar	2008	2009	2010	2011e	2012e
No. of shares (Mn)	2,139	2,139	2,139	2,139	2,139
BVPS (INR)	330	368	408	469	537
CEPS (INR)	124	131	147	168	175
DPS (INR)	32	32	33	32	32

Margins (%)

Year ended 31st Mar	2008	2009	2010	2011e	2012e
EBITDA	50	48	59	61	60
EBIT	34	30	35	40	41
PAT	28	25	28	30	30

Source: Company, Antique

Cash flow statement (INRbn)

Year ended 31st Mar	2008	2009	2010	2011e	2012e
PBT	252	239	250	313	337
Depreciation	83	80	147	149	148
Interest	(33)	(37)	(22)	(22)	(18)
Changes in working capital	(1)	7	2	8	6
Others	(4)	(2)	(3)	(3)	(3)
Tax paid	(83)	(64)	(75)	(99)	(108)
CF from operating activities	215	223	299	346	362
Capex	(136)	(147)	(232)	(223)	(222)
Investments	(6)	(15)	0	0	0
Others	9	(53)	0	0	0
Income from investments	30	41	24	24	21
CF from investing activities	(102)	(175)	(207)	(199)	(200)
Changes in share capital	0	0	0	0	0
Changes in Debt	(3)	0	0	0	0
Dividends & Interest paid	(78)	(81)	(83)	(80)	(80)
CF from financing activities	(82)	(81)	(83)	(80)	(80)
Net cash flow	31	(33)	9	67	81
Add: Opening balance	193	224	191	200	267
Closing balance	224	191	200	267	348

Growth indicators (%)

Year ended 31st Mar	2008	2009	2010	2011e	2012e
Revenue	6	6	(6)	16	7
EBITDA	7	3	14	20	6
PAT	10	(4)	5	26	8
EPS	10	(4)	5	26	8
Consolidated EPS	13	(1)	(0)	27	8

Valuation (x)

Year ended 31st Mar	2008	2009	2010	2011e	2012e
PE (x)	12.8	12.9	12.9	10.2	9.5
P/BV (x)	3.5	3.1	2.8	2.4	2.1
EV/EBITDA (x)	7.7	7.7	6.8	5.5	5.0
EV/Sales (x)	3.9	3.8	4.0	3.3	3.0
Dividend Yield (%)	3	3	3	3	3

Financial ratios

Year ended 31st Mar	2008	2009	2010	2011e	2012e
RoE	24	20	19	21	20
RoCE	25	20	20	24	23
Debt/Equity (x)	0.2	0.2	0.2	0.2	0.1
EBIT/Interest (x)	348.2	160.3	303.5	404.0	442.9

Source: Company Antique

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