

Viewpoint

Subsidy sharing concern seems unsubstantiated; maintain Positive view

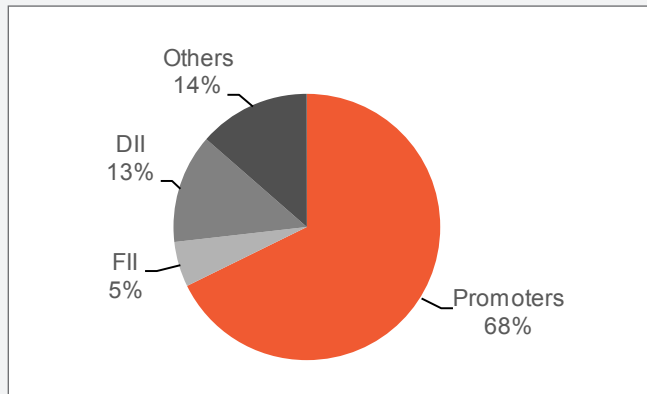
Oil and Natural Gas Corporation

View: Positive | CMP: Rs182

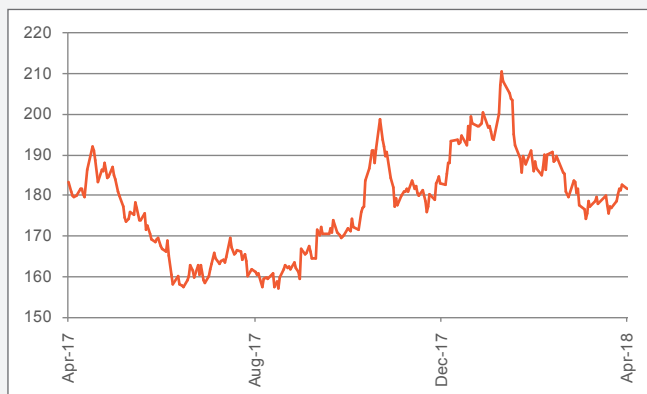
Company details

Market cap:	Rs232,923 cr
52-week high/low:	Rs213/155
NSE volume: (No of shares)	68.7 lakh
BSE code:	500312
NSE code:	ONGC
Sharekhan code:	ONGC
Free float: (No of shares)	414.3 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-0.6	-8.0	10.6	2.0
Relative to Sensex	-1.7	-7.1	4.6	-13.2

Key points

- Recent correction in stock price of ONGC provides good entry opportunity for investors:** LPG/kerosene under-recoveries have declined sharply to Rs. 162/cylinder (vs Rs. 240/cylinder in February 2018) and Rs. 13.4/litre (vs ~Rs. 14/litre in February 2018), respectively, despite elevated level of oil price at \$69-70/bbl. Based on the current LPG and kerosene under-recoveries, we estimate overall under-recoveries of Rs. 29,396 crore for FY2019E, which is higher than FY2019 fuel subsidy budget provisioning of Rs. 24,933 crore. Even if upstream PSUs bear excess under-recoveries, we expect minimum net oil realisation of \$66/bbl for Oil and Natural Gas Corporation (ONGC) assuming Brent oil price of \$70/bbl (average for April 2018 till date). Hence, the concern of negative impact on net oil realisation due to subsidy sharing seems unsubstantiated in our view and thus, the 8% correction in the stock price of ONGC in last three months provides good entry opportunity for investors.
- Strong gas production growth outlook and gradual revival in domestic gas prices would turnaround gas business:** ONGC reported robust growth of 5.8% in its gas production to 24.6bcm (billion cubic metres) in FY2018. ONGC management has guided for FY2019 gas production of 27.4bcm, which implies impressive growth of 11% over FY2018 gas production. Moreover, domestic gas price has increased to \$3.06/mmbtu on gross calorific value basis (\$3.44/mmbtu on net calorific value) for H1FY2019 on back of two consecutive price hikes of 16.5% and 5.9%. We model gas production volume CAGR of 6% over FY2018-FY2020E and gradual increase in gas realisation to \$3.6/mmbtu in FY2019E and \$4/mmbtu in FY2020E. Gradual revival in domestic gas price would a big positive for ONGC as it would turnaround the gas business, given total cost of ~\$3.3/mmbtu (opex at \$1.5/mmbtu and DD&A at \$1.8/mmbtu) for the gas business.
- Outlook – Robust earnings growth outlook for standalone business; higher oil price bodes well for OVL:** We expect strong earnings CAGR of 11% for standalone business over FY2017-FY2020E given our expectation of improvement in the oil & gas realisation and increase in the gas production. The sharp rise in the oil price

and higher oil production from acquisition of Russian oil assets bodes well for the earnings growth of ONGC Videsh Ltd (OVL). Overall, we expect the consolidated earnings of ONGC to report a CAGR of 15% over FY2017-FY2020E.

- ◆ **Valuation – Maintain Positive view on ONGC with 20% upside potential from current levels:**
The recent correction in the stock price of ONGC

has made ONGC's valuation of 7.7x FY2020E EPS attractive, given strong earnings growth outlook and likely expansion in RoE to ~12% over FY2019E-FY2020E vs. 9.5% in FY2017. We, thus, maintain our Positive view on ONGC and expect 20% upside from current level. Moreover, high dividend yield of ~4% is a cushion for investors.

Valuation (consolidated)

Particulars	Rs cr				
	FY16	FY17	FY18E	FY19E	FY20E
Revenue	124,074	125,785	147,285	164,673	171,614
Operating profit	45,981	47,392	57,480	64,084	66,555
OPM (%)	37.1	37.7	39.0	38.9	38.8
Adjusted PAT	20,818	19,907	23,052	28,880	30,079
% YoY growth	26.1	-4.4	15.8	25.3	4.2
Adjusted EPS (Rs)	16.2	15.5	18.0	22.5	23.4
P/E (x)	11.2	11.7	10.1	8.1	7.7
P/B (x)	1.2	1.1	1.0	1.0	0.9
EV/EBITDA (x)	5.5	5.8	4.9	4.4	4.2
RoNW (%)	11.0	9.5	10.2	12.2	12.0
RoCE (%)	11.4	10.5	11.4	13.6	13.5

Source: Sharekhan estimates; Company data

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