

Stock Update

Huge potential but weak track record; retain Hold

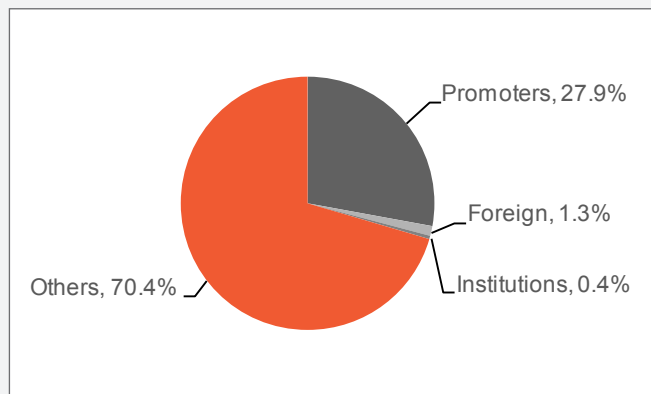
Selan Exploration Technology

Reco: Hold | CMP: Rs196

Company details

Price target:	Rs220
Market cap:	Rs330 cr
52-week high/low:	Rs222/154
NSE volume: (No of shares)	2.0 lakh
BSE code:	530075
NSE code:	SELAN
Sharekhan code:	SELAN
Free float: (No of shares)	1.2 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	26.1	18.4	13.1	6.4
Relative to Sensex	28.4	16.3	2.5	-4.0

Key points

- Large 2P reserve base but poor track record of production ramp-up is a cause of concern:** Selan Exploration Technology (Selan) holds 2P in-place reserves of 86.4mmboe (million barrels of oil equivalent) but the recovery rate is low at 2.9mmboe (3.4% of the 2P reserves). The company has chalked out a phased development plan for its major oil fields and targets additional production of 5.3mmboe. Majority of incremental production is expected to come from Bakrol (3.9mmboe) followed by Karjisan (0.62mmboe), Lohar (0.41mmboe) and Indrora (0.38mmboe) fields. We highlight here that the company has not been able to monetise its large reserve base and, thus, could not achieve its annual production target of 5lakh barrels (FY2017 production of 1.7lakh barrels was well below the target oil production). Thus, we remain cautious on production uptick in the near to medium term and maintain our Hold rating on Selan (trades at EV/boe of \$6.5/boe on 1P reserves, which is at 9% of premium to large domestic peers).
- Q1 results – Implied volume growth of 15.2% QoQ offsets the decline in oil price:** Selan's revenue increased by 3% QoQ to Rs.14.9 crore as implied volumes of 47,833 barrels (+15.2% QoQ; -4.4% YoY) offset the decline in Brent oil price to \$50.8/bbl (-7% QoQ; +8% YoY) and 3.8% QoQ appreciation in Indian Rupee to Rs.64.5. Operating profit declined by 16% QoQ to Rs.7.8 crore due to higher operating expenses, but PAT increased by 4.1x QoQ to Rs.3.4 crore on account of 50% QoQ decline in amortisation for development of hydrocarbon properties and lower effective tax rate (ETR) of 34.3% in Q1FY2018 (vs. 68% in Q4FY2017).
- Outlook – Reserve monetisation and production ramp-up challenges given execution headwinds:** Selan's current oil production run rate is much lower than expectation, as the company has struggled to increase production on account of ramp-up challenges in its major oil fields. Based on the above concern, we remain wary on any meaningful increase in oil production (from Q1FY2018 levels) in the next couple of years. We believe subdued production, range-bound oil prices and appreciation of Indian rupee would continue to act as an overhang on the stock. Moreover, low oil price environment poses risk to the development of oil fields of Selan.

- ♦ **Valuation – Maintain Hold with revised PT of Rs.220:** Selan's stock price has run up sharply by 19% in the past one month on hopes of ramp-up in oil production in the near to medium term based on the company's guidance on potential large oil reserves. However, we remain cautious on the production ramp-up given the poor track record to monetise large hydrocarbon reserves.

Moreover, Selan trades at EV/boe of \$6.5/boe (based on 1P reserves of 5.3mboe), which is at 9% premium to large domestic upstream PSUs. Hence, we do not see scope for further re-rating of the valuation multiple. Thus, we maintain our Hold rating on Selan with a revised price target (PT) of Rs.220 (valued at 6x FY2019E EV/EBITDA).

Result						Rs cr
Particulars	Q1FY18	1QFY17	YoY %	4QFY17	QoQ %	
Revenues	14.9	15.1	-1	14.6	3	
Total Expenditure	7.1	5.9	21	5.3	35	
Operating profit	7.8	9.1	-15	9.3	-16	
Other Income	2.0	2.1	-5	2.0	1	
Interest	0.0	0.0		0.0		
Depreciation	4.6	6.3	-27	8.6	-47	
PBT	5.2	4.9	6	2.6	99	
Tax	1.8	1.7	4	1.8	1	
RPAT	3.4	3.2	7	0.8	308	
Adjusted PAT	3.4	3.2	7	0.8	308	
Equity Cap (Rs cr)	16.4	16.4		16.4		
EPS (Rs)	2.1	1.9	7	0.5	308	
Margins (%)			BPS		BPS	
OPM	52.2	60.7	-855	63.6	-1,142	
NPM	22.7	21.1	158	5.7	1,701	
Tax rate	34.3	35.0	-67	68.0	-3,365	

Valuations (Standalone)					Rs cr
Particulars	FY2016	FY2017	FY2018E	FY2019E	
Net Sales	62.0	55.8	55.9	62.6	
Operating Profit	37.8	34.8	34.7	39.7	
Operating Profit Margin (%)	60.9	62.4	62.0	63.5	
Net Profit	12.9	8.7	11.5	13.5	
EPS (Rs)	7.9	5.3	7.0	8.2	
YoY change (%)	-54.4	-32.9	32.4	17.6	
PER (x)	24.9	37.2	28.1	23.9	
Price/BV (x)	1.1	1.1	1.1	1.1	
EV/EBIDTA(x)	5.8	6.1	5.6	5.1	
Net Cash/share	63.5	67.2	77.0	71.5	
Div Yield (%)	2.5	2.5	2.5	2.5	
RoCE (%)	6.1	4.1	5.0	5.8	
RoNW (%)	4.6	3.1	4.1	4.7	

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