

OIL AND GAS

Weak GRMs hurt OMCs; gas outshines

India Equity Research | Oil, Gas and Services

Our oil & gas coverage universe reported a dip of 12% YoY in PAT and 10% YoY in EBITDA, which are largely in line with our Q2FY20 estimates. Key takeaways: i) OMCs were outliers with a 49% YoY fall-off in PAT as GRMs tumbled 56% YoY, but marketing margins continued to outperform. ii) In contrast, CGD reported a stunning PAT uptick of 97% YoY fueled by steady volume growth and higher margins. iii) A 57% YoY plunge in LNG prices powered GSPL's transmission volumes by 12% YoY and PAT by 29% YoY. GAIL missed estimates due to a 75% YoY crash in trading margins and a one-time provision in transmission. iv) RIL posted strong PAT growth of 18% YoY, in line with our estimate, led by a 16% QoQ rise in GRMs and a 9% outperformance by RJIO due to lower opex. v) ONGC missed estimates as the Uran fire incident shaved off C2-C3 gas production, driving a 14.6% miss in value-added product revenue. vi) PLNG reported an uptick of 26% YoY in PAT, ahead of our estimates led by higher trading margins.

RIL: Refining surges; petchem better than expected

RIL's EBITDA increased by 4.9% YoY led by higher cracks across distillates as well as intermediate volumes for petchem. It beat estimate by 9% due to higher ARPU and lower opex. We expect IMO regulations to boost diesel crack spreads USD20/bbl-plus, from USD15.6/bbl in Q2. By Q4FY20, the company targets to commence commercial production of petcoke gasifier, which would boost GRM by another USD2/bbl.

CGD continues to be a bright spot with sustained demand growth

IGL and MGL hiked CNG/domestic PNG prices, which fed into margins as input APM price is flat. Industrial margins came under pressure for **Gujarat Gas** as LPG prices slid seasonally. Aggregate profits of gas transmission companies, **GAIL and GSPL**, fell off 37% YoY. **GSPL** met estimates with steady volume growth of 12% as lower input price (spot LNG) spurred power volumes. **GAIL** missed estimates as cargoes bound for fertiliser plants and linked to oil prices were sold on the spot market, leading to losses. **Petronet LNG's** volume remains robust at 4.8MMT (up 15.2% YoY) with higher trading margins.

OMCs: PAT halves, but marketing margins outperform

OMCs' PAT halved by 49% YoY as GRMs slid by 56% YoY, but marketing margins compensated for it somewhat. Although benchmark GRM rebounded QoQ, OMCs' GRM underperformed due to BS-6-related shutdown of secondary units and higher crude purchase costs. With BS-6 shutdowns largely complete and return of heavier crude grades, the spread versus benchmark should start narrowing from Q3FY20.

Outlook: GRM recovery imminent; sanguine prospects for gas

HPCL and RIL remain our top large-cap picks and GSPL among mid-caps. We expect GRM to rise as IMO norms boost light and middle distillate cracks. We estimate steady volume growth at GSPL, which is diversifying geographically (cross-country) via a JV.

Segmental industry actuals

	Q2FY20	Q2FY19	Q1FY20
Brent (\$/bbl)	62.0	76.0	68.4
USD/INR	70.3	70.1	69.6
Singapore GRM (\$/bbl)	6.5	7.6	4.7
OMC's Marketing margins (INR/ltr)	4.8	4.1	4.4
Oil Product Sales (MMT)	38.2	37.6	41.5
Gas Production (BCM)	6.3	6.4	6.4
Oil Production (MMT)	5.8	6.1	5.9
PLNG Dahej Utilisation	105.8%	108.5%	111.6%

*Oil product sale for OMCs**
*Oil and Gas production for ONGC**
 Source: Edelweiss research

Quarterly change (%)

	QoQ%	YoY%
Brent (\$/bbl)	(9.4)	(18.4)
USD/INR	1.1	0.4
Singapore GRM (\$/bbl)	39.8	(13.8)
OMC's Mkt. margins (INR/ltr)	8.1	17.8
Oil Product Sales (MMT)	(8.0)	1.6
Gas Production (BCM)	(2.3)	(1.5)
Oil Production (MMT)	(0.5)	(3.9)
PLNG Dahej Utilisation	(5.2)	(2.5)

Source: Edelweiss research

Earnings Snapshot

	EBITDA growth (%)		PAT growth (%)	
	YoY	QoQ	YoY	QoQ
OMC's (HP, BP, IOCL)	(38.0)	(41.6)	(49.1)	(54.8)
City Gas (IGL, MGL, GGL)	46.0	37.8	46.3	31.0
Gas transmission (GAIL, GSPL)	2.8	32.1	6.4	(6.8)
Gas utility (PLNG)	9.6	63.2	1.3	35.1
Reliance Industries	3.2	2.3	6.8	(2.5)
ONGC	2.6	22.2	(2.8)	47.6
Aggregate	(10.0)	(7.1)	(15.8)	(16.5)

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November 20, 2019

Table 1: Q2FY20 earnings summary

Stock		Q2FY20 (INR mn)	Q2FY19 (INR mn)	Y-o-Y (%)	Q1FY20 (INR mn)	Q-o-Q (%)	Comments / Key highlights
RIL	Revenues	14,85,260	14,33,230	3.6	15,69,760	(5.4)	RIL continued to deliver steady earnings with Q2FY20 consolidated PAT at INR112bn, EBITDA at INR221bn was broadly in line with estimate. Refining in Q2FY20 is in line with our estimate GRM (GRM: USD9.4/bbl, estimate: 9.3/bbl) offset by lower throughput. Petchem beat estimate 4% due to higher intermediate volumes
	EBITDA	2,21,520	2,11,080	4.9	2,13,150	3.9	
	Core PAT	1,12,620	95,160	18.3	1,01,040	11.5	
BPCL	Revenues	6,43,408	7,22,918	(11.0)	7,63,179	(15.7)	Core GRM (ex-inventory losses) of USD3.8/bbl led to the miss, dragged by the BSVI-related shutdown at Kochi and higher crude purchase costs. Core marketing margin (ex-inventory losses) of INR4.8/litre beat our estimate. Marketing volume, up 1.7% YoY, outgrew the industry.
	EBITDA	23,749	24,194	(1.8)	21,799	8.9	
	Core PAT	12,043	12,187	(1.2)	11,106	8.4	
Petronet LNG	Revenues	93,612	1,07,453	(12.9)	86,134	8.7	Volume at 4.8MMT, is in line of our estimate. Utilisation of the Dahej / Kochi terminal was 106%/15.4%; Dahej expansion (2.5MTPA) is fully contributing to volumes and continues to be on spot. Commissioning of the Kochi-Mangalore pipeline is delayed to February 2020.
	EBITDA	11,605	8,837	31.3	10,239	13.3	
	Core PAT	7,112	5,629	26.3	5,948	19.6	
GAIL	Revenues	1,80,399	1,92,753	(6.4)	1,83,106	(1.5)	Trading: margin declined 70% QoQ as oil-linked fertiliser volumes were sold at spot prices. Transmission EBITDA also missed estimate 8% led by one-time refund of HWJ tariff levied retrospectively. Petchem: With Pata plant running at 100% plus utilisation & metallocene production kicking in, EBITDA surpassed estimate. 3) LPG/LHC: EBITDA came in line as volume miss was offset by higher margin
	EBITDA	15,627	29,276	(46.6)	22,590	(30.8)	
	Core PAT	10,643	19,630	(45.8)	12,875	(17.3)	
GSPL	Revenues	6,356	5,983	6.2	5,126	24.0	Volumes at 39.2mmscmd (up 11.9% QoQ) are in line. While CGD volumes remain stable, power volumes soared led by lower spot LNG prices. EBITDA/scm at INR1.2/scm (+4.9% QoQ) met estimates as SUG costs have been eliminated.
	EBITDA	4,371	5,163	(15.3)	4,020	8.7	
	Core PAT	3,265	2,536	28.7	2,061	58.4	
Indraprastha Gas	Revenues	16,925	14,215	19.1	15,761	7.4	Gross margin at INR12.2/scm (up 9.5% YoY, 2.3% QoQ) continued to expand led by higher margins across segments; Volumes, up 9.5% YoY, came broadly in line; EBITDA margin rose 15.1% YoY & 4.4% QoQ to INR6.8/scm due to gross margin expansion.
	EBITDA	3,926	3,080	27.5	3,585	9.5	
	Core PAT	2,993	1,873	59.8	2,184	37.1	
HPCL	Revenues	6,08,633	6,75,180	(9.9)	7,09,889	(14.3)	Core marketing margin at INR5.7/litre outshone our estimate of INR4.6/litre, primarily driving the earnings outperformance. Core GRM at USD2.6/bbl significantly undershot our expectation due to higher crude procurement costs and the shutdown at secondary units. Refining throughput missed our estimate by 4.2% ahead of the BSVI shutdown at Vizag.
	EBITDA	23,189	21,220	9.3	16,439	41.1	
	Core PAT	10,523	10,920	(3.6)	8,110	29.8	
Indian Oil	Revenues	11,16,897	13,20,348	(15.4)	13,15,125	(15.1)	Core refining EBITDA turned negative, missing estimate due to Panipat shutdown & higher crude procurement costs; Core marketing EBITDA at INR34.6bn missed estimate with margin contracting to INR4.2/ltr (down 5.3% QoQ) from a high base; Petchem EBITDA belied estimate due to delay in PP commissioning at Paradip.
	EBITDA	35,722	67,620	(47.2)	83,500	(57.2)	
	Core PAT	5,634	32,469	(82.6)	35,961	(84.3)	
Mahanagar Gas	Revenues	7,836	6,965	12.5	7,575	3.4	Gross margin expanded 17.5% YoY led by higher CNG margins. CNG volume growth moderated to -0.1% YoY due to monsoon and supply disruption from ONGC. PNG volume growth moderated to 2.2% YoY as industrial volumes were affected by termination of connections by 13 customers.
	EBITDA	2,734	2,215	23.5	2,768	(1.2)	
	Core PAT	2,139	1,363	57.0	1,702	25.7	

Source: Edelweiss research

Table 1: Q2FY20 earnings summary (contd.)

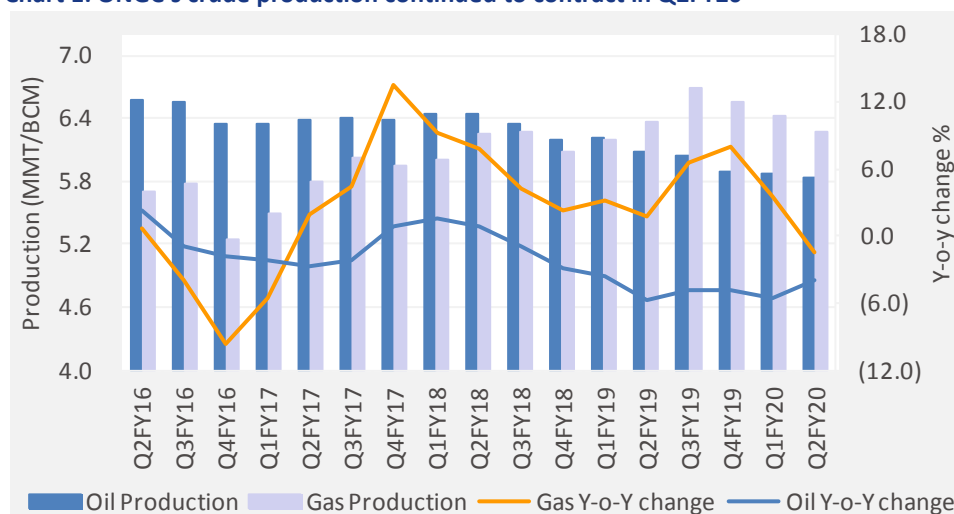
Stock		Q2FY20 (INR mn)	Q2FY19 (INR mn)	Y-o-Y (%)	Q1FY20 (INR mn)	Q-o-Q (%)	Comments / Key highlights
ONGC	Revenues	2,44,926	2,79,890	(12.5)	2,65,550	(7.8)	The miss was mainly driven by the Uran fire affecting C2-C3 gas production, resulting in a 14.6% miss in VAP (value-added product) revenue. While oil and gas production came in line, sales volumes (-1.9% YoY, +0.4% QoQ) missed the estimate by 1.6% as inventories rose temporarily. Oil and gas realisations are broadly in line with estimates.
	EBITDAX	1,32,900	1,57,894	(15.8)	1,51,124	(12.1)	
	Core PAT	62,631	82,664	(24.2)	59,738	4.8	
Gujarat Gas	Revenues	25,129	19,643	27.9	26,146	(3.9)	Volume at 9.3mmscmd (up 39.3% YoY) beat estimate by 3.4% led by strong industrial volumes; further of 1.5-2.0mmscmd upside potential due to similar rulings as Morbi in Surat, Ankleshwar, Bharuch & Vapi. Gross margin at INR6.5/scm missed estimate by 7.9% as the company cut prices to spur volumes.
	EBITDA	3,706	1,607	130.6	4,665	(20.6)	
	Core PAT	2,329	547	326.2	2,337	(0.3)	

Source: Edelweiss research

Production: Oil continues to contract at ONGC

ONGC saw a further decline in crude production in Q2FY20, down 3.9 % YoY at 5.8MMT, while gas production decreased 1.5% YoY to 6.3bcm.

Chart 1: ONGC's crude production continued to contract in Q2FY20



Source: PPAC, Edelweiss research

Refining: Benchmark increase broad-based across distillates

Singapore refining benchmark margin at USD6.6/bbl, up 89% QoQ and 8% YoY. The gasoline crack stood at USD8.2/bbl (up 32% QoQ) and Gasoil at USD15.6/bbl (up 22% QoQ) in Q2FY20, which is attractive for the OMCs in the next quarter. We expect GRMs to increase further from Q3FY20, heralding a surge in profitability across OMCs.

Chart 2: Benchmark refining margins surged 89% QoQ

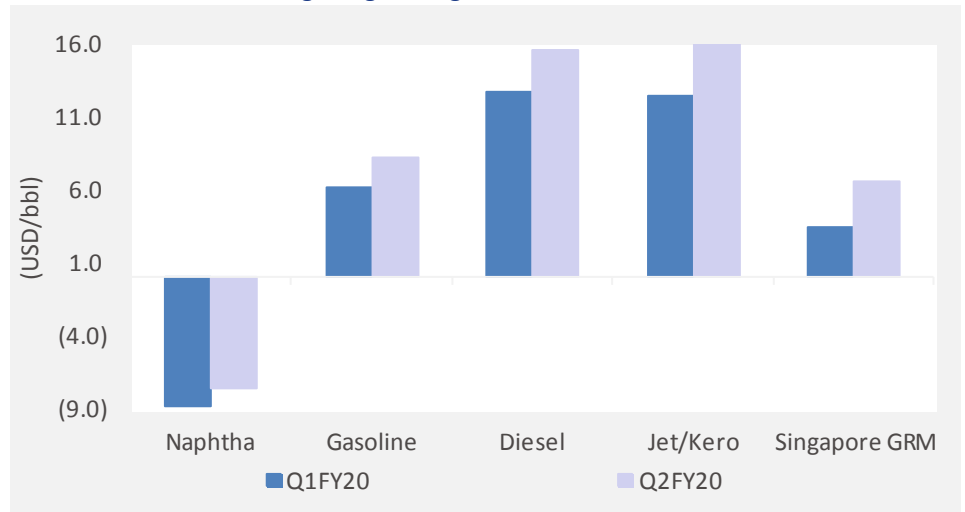
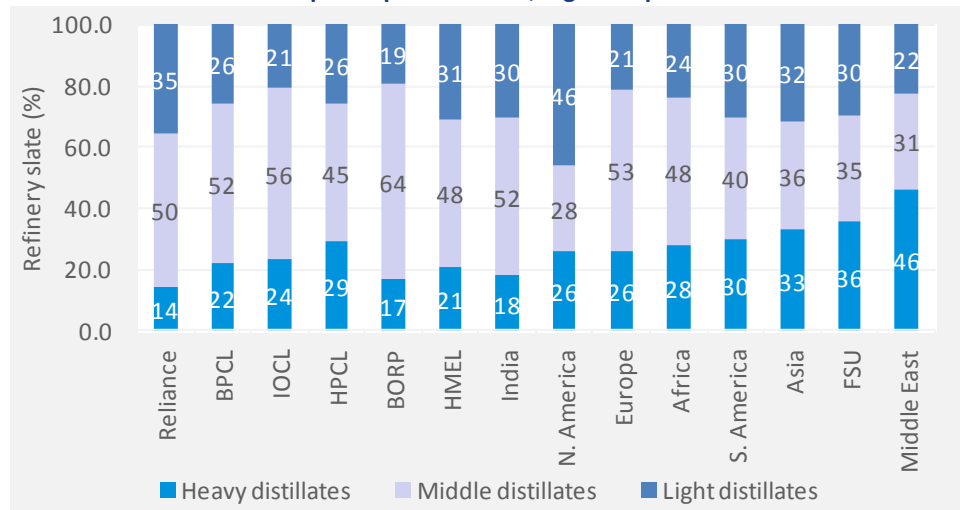
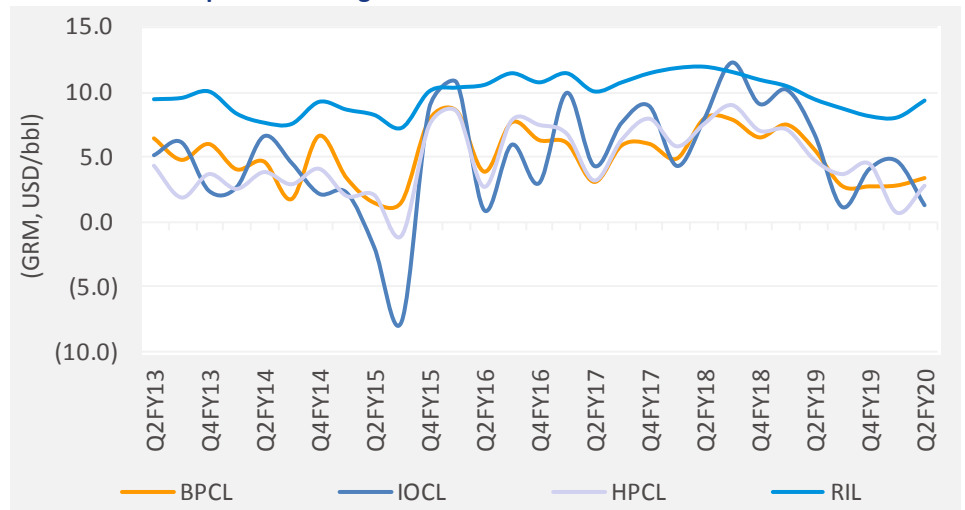


Chart 3: Indian refiners—Superior product slate, higher exposure to middle distillates



Source: MoPNG, Edelweiss research

Chart 4: GRM comparison among incumbents



Source: Edelweiss research

Table 2: Quarterly comparison across OMCs

	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	YoY (%)
Refining Throughput (MMT)										
IOCL	16.1	18.2	17.2	17.7	17.8	19.0	17.4	17.3	17.5	(1.6)
BPCL	7.0	7.3	7.9	7.7	7.6	7.5	8.2	7.5	7.7	1.2
HPCL	4.6	4.5	4.6	4.5	4.8	4.6	4.6	3.9	4.6	(4.2)
Throughput Growth (YoY %)										
IOCL	2.9	11.4	0.4	0.8	10.7	4.1	1.2	(2.2)	(1.6)	
BPCL	9.5	7.2	30.4	20.6	8.1	3.0	4.6	(3.7)	1.2	
HPCL	14.9	(3.0)	(0.2)	0.7	2.6	0.9	(0.6)	(13.3)	(4.2)	
GRM (\$/bbl)										
IOCL	8.0	12.3	9.1	10.2	6.8	1.2	4.1	4.7	1.3	(81.1)
BPCL	8.0	7.9	6.5	7.5	5.6	2.8	2.7	2.8	3.4	(39.3)
HPCL	7.6	9.0	7.1	7.2	4.8	3.7	4.5	0.8	2.8	(41.2)
Inventory Gains (\$/bbl)										
IOCL	1.0	6.2	3.0	6.8	3.3	(8.0)	2.7	1.1	(1.7)	(5.0)
BPCL	1.5	3.0	0.9	3.3	2.3	(3.3)	0.2	(0.9)	(0.4)	(2.7)
HPCL	2.1	2.9	0.5	3.4	2.1	(6.3)	2.4	(2.6)	0.3	(1.8)
Core GRM (\$/bbl)										
IOCL	6.9	6.1	6.1	3.4	3.5	9.1	1.4	3.6	3.0	(14.6)
BPCL	6.5	4.9	5.6	4.2	3.3	6.0	2.6	3.7	3.8	15.4
HPCL	5.6	6.1	6.6	3.7	2.7	10.0	2.1	3.3	2.6	(5.2)
Marketing sales volume (MMT)										
IOCL	18.0	19.7	19.7	20.5	18.6	20.3	20.5	20.5	19.0	1.6
BPCL	10.4	11.2	11.1	11.3	10.6	11.5	11.7	11.3	10.5	(1.0)
HPCL	8.8	9.4	9.5	9.7	9.1	9.7	10.1	10.1	9.4	2.8
Volume Growth (%)										
IOCL	4.1	4.1	6.0	3.5	3.7	3.1	4.4	0.3	1.6	
BPCL	8.7	6.9	9.9	7.1	2.1	2.0	5.2	0.5	(1.0)	
HPCL	7.3	1.7	6.8	5.0	4.2	3.2	7.0	3.8	2.8	
Normalised Gross Marketing margin (INR/ltr)										
IOCL	2.9	2.9	3.7	3.8	4.1	3.8	5.9	4.3	4.0	(2.8)
BPCL	3.9	3.1	4.4	3.7	4.3	4.2	6.2	4.5	4.8	11.3
HPCL	4.4	3.9	5.3	4.1	3.7	4.7	7.5	4.4	5.3	45.0
Inventory Gains (INR/ltr)										
IOCL	0.1	0.4	0.4	0.8	0.6	(1.1)	0.1	0.1	0.2	(74.2)
BPCL	0.1	0.4	0.1	1.1	0.4	(1.5)	0.2	(0.1)	0.1	(72.4)
HPCL	0.3	0.8	0.0	1.0	0.7	(1.7)	0.3	(0.0)	(0.0)	(101.7)

Source: Edelweiss research

Marketing: Margins recovered post elections

Q2FY20 saw a beat on marketing margins across OMCs, with margins continuing to trend above their long-term targets. The margin performance is in a sharp contrast to margins derived from Delhi auto fuel prices, which continued to remain negative during the quarter. There are two possible reasons for this: i) OMCs generate significantly higher margins in tier-2 cities/rural than metros; and ii) ATF/lubricants/other industrial margins are much higher than auto fuel margins.

Chart 5: Auto fuel margins in Delhi began to recover in Q2 after central elections

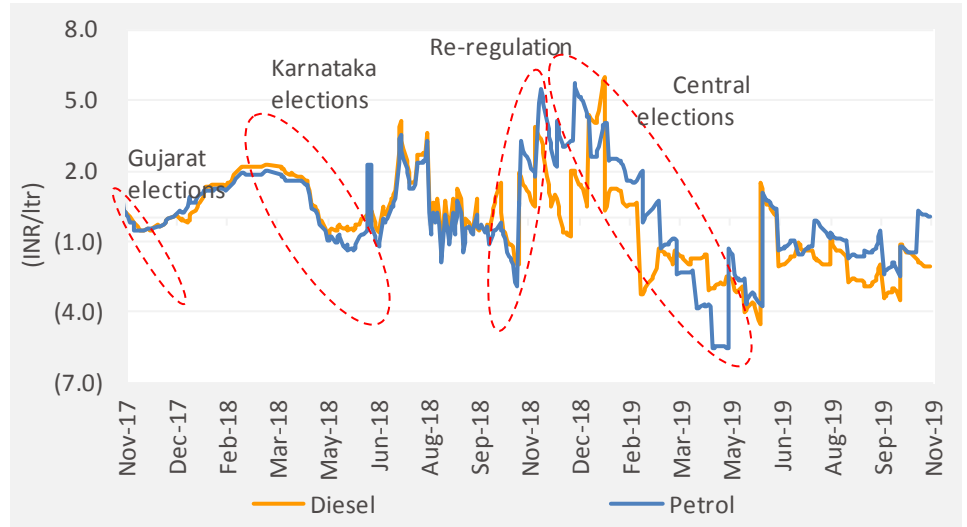


Chart 6: Q2FY20 petrol demand increased 10.1% YoY

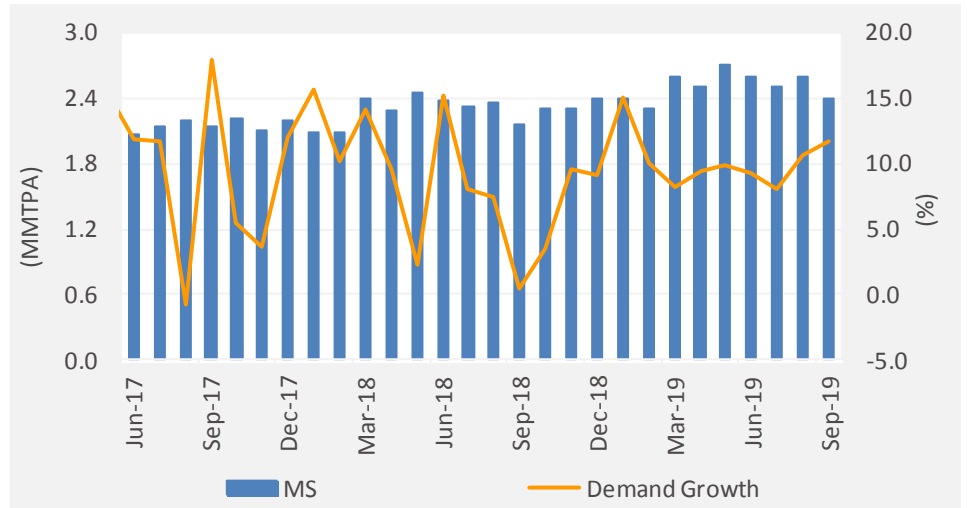
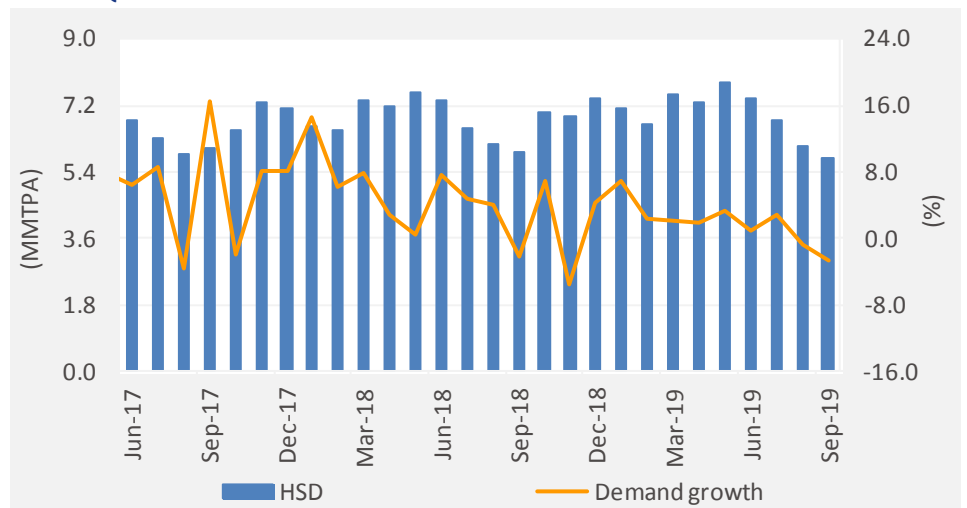
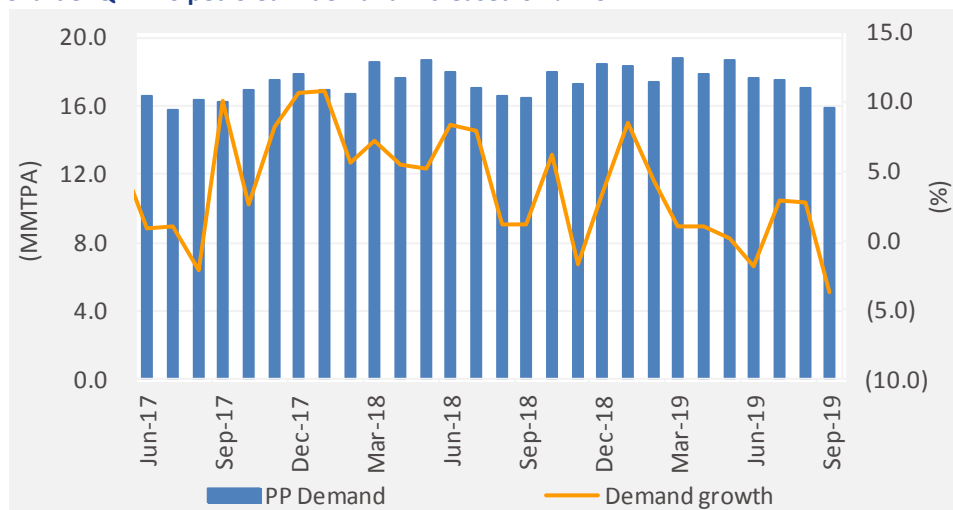


Chart 7: Q2FY20 diesel demand decreased 0.1% YoY



Source: Edelweiss research

Chart 8: Q2FY20 petroleum demand increased 0.7% YoY



Source: PPAC, Edelweiss research

Table 3: City gas comparison—Volume growth at GGL surged; IGL consistent while MGL slowed down sharply due to one-offs

	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Average
Overall volume growth (%)											
IGL	13.0	11.4	13.8	11.1	12.1	13.0	12.2	16.3	11.9	10.7	12.5
MGL	2.7	4.0	7.1	6.7	11.9	9.5	8.1	7.4	3.3	1.3	6.0
GGL	19.1	11.2	18.4	11.7	5.1	16.3	4.1	(3.8)	42.3	39.3	11.0
CNG growth (%)											
IGL	11.7	9.4	11.3	9.9	10.1	14.1	13.2	14.8	11.7	9.1	11.3
MGL	1.4	3.2	6.6	6.7	12.6	9.2	8.3	6.9	2.0	1.0	5.7
GGL	10.6	7.5	11.2	9.9	11.7	11.3	10.1	9.0	5.1	4.9	8.9
Residential PNG growth (%)											
IGL	5.3	18.2	16.7	24.0	12.5	5.0	10.7	12.9	14.8	20.9	12.8
MGL	12.7	11.4	9.9	9.0	13.1	11.8	13.3	11.0	9.4	4.5	10.3
GGL	14.3	5.0	9.1	10.0	(5.0)	16.7	4.2	3.6	18.4	23.9	8.9
Industrial/Commercial growth (%)											
IGL	12.5	15.9	20.0	15.2	28.9	26.9	13.0	30.2	17.2	12.8	16.6
MGL	1.7	2.4	7.2	5.0	7.8	8.9	2.5	7.3	4.3	0.2	4.7
GGL	22.3	13.1	21.9	12.4	4.2	17.8	2.4	(8.4)	55.8	51.1	12.2
EBITDA margin (INR/scm)											
IGL	6.3	6.1	5.6	6.3	6.0	5.9	6.1	6.1	6.5	6.8	6.1
MGL	8.7	8.1	8.0	7.0	8.1	8.1	8.8	7.9	10.3	9.9	8.0
GGL	4.8	3.8	3.5	3.7	4.2	2.9	5.3	4.3	5.6	4.3	4.1

Source: Company, Edelweiss research

Chart 9: Growth at IGL continues to be higher than MGL...

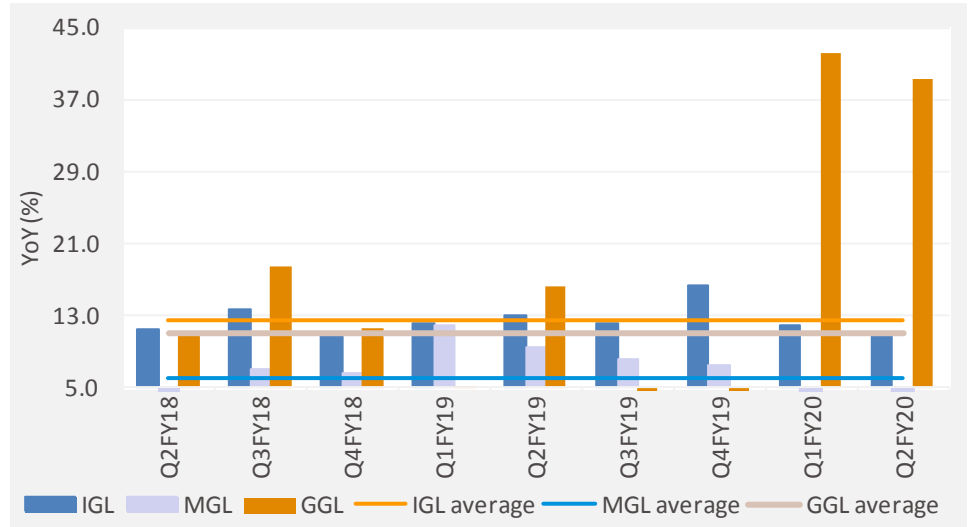
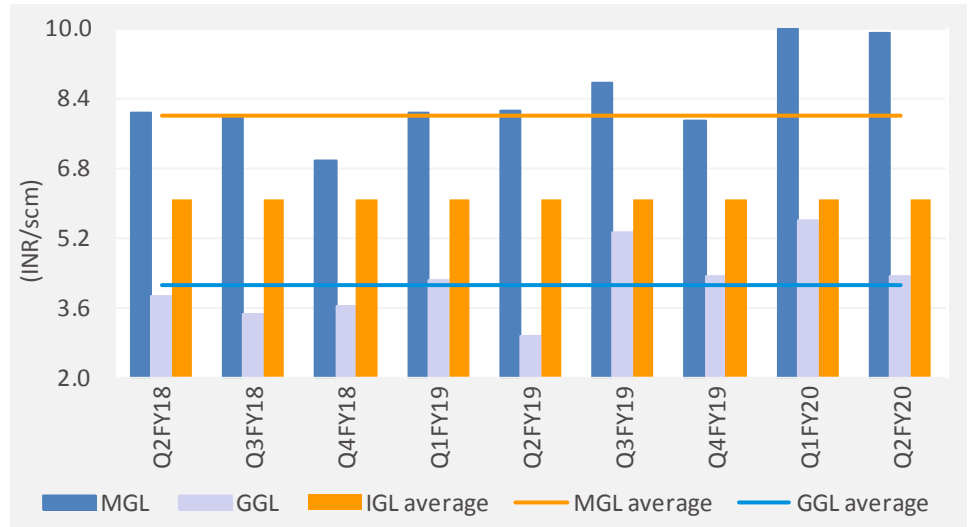


Chart 10: ...although EBITDA margins are 31% below MGL's



Source: Company, Edelweiss research

Table 4: Valuation Snapshot

Company	Market		Target Price (INR)	Mcap (USD mn)	Diluted EPS (INR)			P/E (x)			PB (x)			ROE (%)			Div yield		EPS CAGR FY19-21E
	Price (INR)	Reco			FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY20E	FY21E	
OnG																			
Reliance Industries Limited	1,510	BUY	1,716	133,450	67.0	87.9	103.0	22.5	17.2	14.7	2.1	11.9	12.8	11.5	0.5	24.0			
Bharat Petroleum Corporation Limited	519	BUY	632	15,697	39.7	42.0	50.7	13.1	12.4	10.2	2.5	21.5	21.7	23.8	3.4	13.0			
Hindustan Petroleum Corporation Limited	290	BUY	378	6,166	43.9	48.2	55.9	6.6	6.0	5.2	1.3	23.9	22.8	23.4	7.0	12.9			
Indian Oil Corporation Limited	133	BUY	190	17,459	18.9	19.9	30.7	7.0	6.7	4.3	1.0	15.0	15.8	22.2	7.0	27.4			
Oil and Natural Gas Corporation	133	BUY	190	23,374	24.6	21.5	26.0	5.4	6.2	5.1	0.7	15.3	13.1	14.3	4.9	2.9			
GAIL India Limited	125	BUY	174	7,867	14.5	13.9	18.0	8.6	9.0	6.9	1.2	14.9	12.6	15.5	4.6	11.4			
Gujarat State Petronet Limited	220	BUY	276	1,730	17.7	25.2	26.8	12.4	8.7	8.2	2.7	31.4	35.0	29.1	1.2	23.0			
Indraprastha Gas Limited	418	BUY	448	4,079	12.0	17.5	18.9	34.7	23.9	22.1	5.7	21.2	25.8	23.6	0.9	25.4			
Gujarat Gas Limited	194	BUY	242	1,866	6.1	10.8	13.0	32.0	18.0	14.9	4.5	20.6	28.6	26.9	1.5	46.4			
Mahanagar Gas Limited	1,045	BUY	1,168	1,439	55.3	69.4	79.1	18.9	15.0	13.2	3.7	24.3	26.3	25.9	3.0	19.6			
Petronet LNG	272	HOLD	254	5,689	14.4	18.1	20.8	18.9	15.0	13.1	3.9	21.8	26.4	29.0	4.6	20.4			
OnG - Mean								16.4	12.6	10.7	2.7	20.2	21.9	22.3	3.5	20.6			

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Coverage group(s) of stocks by primary analyst(s): Oil, Gas and Services

Bharat Petroleum Corporation, Cairn India, GAIL (INDIA), Gujarat Gas, Gujarat State Petronet, Hindustan Petroleum Corporation, Indraprastha Gas, Indian Oil Corporation, Mahanagar Gas Ltd, ONGC, Petronet LNG, Reliance Industries

Recent Research

Date	Company	Title	Price (INR)	Recos
15-Nov-19	ONGC	Uran fire drives earnings miss; <i>Result Update</i>	136	Buy
13-Nov-19	Mahanagar Gas	Stable margins offset volume blues; <i>Result Update</i>	1,003	Buy
08-Nov-19	Gail	Trading/transmission one-offs mar earnings; <i>Result Update</i>	127	Buy

Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

All price charts cannot be included given the large number of companies in our coverage. Specific charts may be available upon request.

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