

🐎 DARK HORSE - HINDUSTAN OIL EXPLORATION CO.LTD 🐎

Dated : 9th Nov. 2017

ACCUMULATE

Price ₹	112
Multibagger	
Upside	-
Div Yield	-
Tenure	2-3 years
Sensex	33250.93
Nifty	10308.95
Group/Index	B / S&P BSE SmallCap

Stock Details

M.cap (₹ in cr)	1461
Equity (₹ In cr)	130.49
52 wk H/L ₹	141.60/60.70
Face Value ₹	10.00
NSE code	HINDOILEXP
BSE code	500186

Key Valuation Ratios

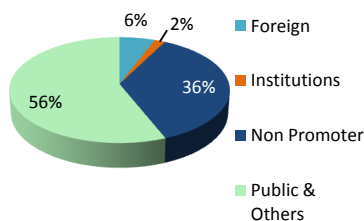
RONW	4.60%
P/E	93.33
P/BV	4.2
EV/EBIDTA	41.61

IN ₹

Key Financial Data

EV (₹ in cr)	1427.12
BV (₹ in cr)	26.81
NW (₹ in cr)	349.87
Adjst.EPS (TTM)	1.20

Share Holding Pattern



Investment Rationale

India's first Private oil & gas company, with strong portfolio of discovered resources, Debt free balance sheet with funds for Organic Growth, Presence in 4 of 6 Producing Basins in India (Mumbai offshore, Cauvery, Cambay & Assam-Arakan), Portfolio of 9 Blocks with discovered resources 5 Onshore (2 North East, 3 Gujarat) 4 offshore (2 West Coast & 2 East Coast) & Vision to emerge as the finest Independent Oil and Gas Company that beneficially transforms the interests of every stakeholder through Talent and Technology.

Growth Strategy

⇒ Focus on North East

- ☉ Ramp up production capacity to 36 mmscfd of gas & 1000 bopd condensate from 6 wells effective 1 April 18.
- ▲ Re assessment of Dirok recoverable reserves on going
- ▲ Revised Field Development Plan to be submitted to target Dirok upside potential
- ▲ Evaluate early production from Kherem

⇒ Enhance Cambay

- ▲ Infuse capital to enhance production from existing fields
- ▲ Acquire additional acreage through OALP and HELP bidding rounds

⇒ Revive Offshore

- ▲ PY-1 Re-entry campaign planned to enhance production in Q1 FY18
- ▲ Fast track development of B-80 to deliver First Oil
- ▲ PY-3 -revive 3000 bbls/d shut in from existing well (subject to Approvals)

Further, Focus of the company would be :

To operate and hold material working interests and maintain a balanced portfolio of assets

To increase production by re-development of existing producing assets

To continue evaluation of the existing assets and de-risk them appropriately

To seek new investment opp. wherein can leverage its technical talent and physical assets

To increase reserve base by establishing upside potential in existing assets

To operate in optimum cost environment and focus on value enhancement

To develop the existing discoveries by improving the speed of execution

Open Acreage Licensing (OAL) Program & Discovered Small Field (DSF) bid round 2 announced by the Government present excellent opportunities to grow the portfolio

Key Strengths

Debt free balance sheet & Investment cycle to cash 12-18 months . Ability to raise capital for inorganic growth.

Proven development and operating experience in both onshore and offshore with multiple JV partners

All 9 blocks (5 onshore and 4 offshore) have discovered resources with potential up side.

Delivered First Gas from Dirok (Assam) Field in a record 27 months within budget

1 day 5 day 1 month 3 months **1 year** 5 years max



Source: Google

Corporate Governance Transparency Ratio's

Year End	201703	201603	201503	201403
Tax Rate %	9.87	11.15	-	9.14
Receivable day	74.00	28.00	32.00	40.00
Div. Payout %	-	-	-	-

Initiatives bearing fruits

Specifically, in upstream oil and gas sector, the following three initiatives have made a major positive impact

- ⇒ **First**, in the area of exploration, the Government has funded a programme to acquire Nationwide 2D seismic data with ONGC and Oil India leading the implementation with the award of contracts. The National Data Repository platform being built by DGH is nearing completion and would usher in open acreage policy, where any one can pick a block, trigger a bid round and take up exploration and development.
- ⇒ **Second** major initiative has been in Natural Gas Sector. The objective is to increase the share of this low cost Green Fuel to one fourth in the primary energy mix at par with U.S.A. by replicating the Gujarat Model. Announcing premium for domestic gas in difficult areas, adding significant LNG regasification capacity, stepping up City Gas Bid rounds, extending the pipeline network especially in North East Region and priority allocation for CNG are concrete steps taken to build a Gas Driven Economy. Industry is looking for free market pricing for Natural Gas
- ⇒ **Third** and the most significant initiative is the announcement of Discovered Small Field Bid Round 2016 (DSF 2016). The DSF 2016 has been successfully concluded resulting in award of 31 contract areas to 22 companies (singly or in consortium), with 15 companies being new entrants to the oil and gas sector. HOEC has won two contract areas under DSF 2016

Growth Opportunity Prolific Dirok

⇒ Dirok field is endowed with Girujan, Tipam and Barail Formation ⇒ Reserves to be recast based on performance of all 6 wells in Dirok field ⇒ Potential exist for both increasing reserves and improving recovery factor on well performance ⇒ Revised Field Development Plan to be submitted to target Dirok upside potential

Next Focus Increasing production from PY-1

⇒ Significant resources exists in fractured granite basement reservoir ⇒ Planned to re-entre wells targeting Mercury hill and Earth tertiary sand in Q1 FY 18-19 ⇒ **Opportunities**- re-entry from existing wells realizing the production is immediate, Capital costs for re-entry and side tracking from the existing wells are marginal, Existing facilities can handle the increase in production without any additional cost, Potential up-side from Jupiter ,Pluto, Saturn & Venus to be drilled subsequently

Focus 'First Oil' B-80 (Mumbai High-DSF block)

⇒ In house estimate of resources is STOIP 40 million barrels & 26 bcf of gas ⇒ Tested production rates oil : 3737 bopd and gas 7.90 mmscfd, Two pay zones Panna 200 & 300 ⇒ **Planned under Phase -1 of FDP**- Drill two new wells, Install a mobile offshore process unit or FPSO, Connect to oil and gas lines of ONGC ⇒ **Project Status**- EC application process initiated, Market being scanned for a suitable MOPU or FPSO, Field Development Plan being finalized for submission in November 17, Rig in Mumbai High identified for drilling.

PY3 and PY1 Integration



PY-3 field was shut-in on 31 July 2011 when it was producing 3000+ bopd without any subsurface issues.

HOEC has 21% stake in PY-3 operates PY-1 Gas field with an offshore platform and onshore processing facilities close to PY-3 field

Alternate Integrated Field Development Plan (AIFDP) for PY-3 was submitted to stakeholders and awaiting approval

Field has potential to produce 7000+ bopd with an additional well and side track of one existing well

Integration of PY-1 and PY-3 facilities through a 6 Km offshore pipeline is feasible and most cost effective to revive production from PY-3.

Dirok Gas production
ramp up on track

Debt free balance sheet

Assam (AAP-ON-94/1):
Step-up Production

New Blocks: Kherem
(Arunachal Pradesh)

Business Operations- Q2FY18 HIGHLIGHTS

- ⇒ Company has strong financials- Debt free balance Sheet & self funding for organic growth, Gross working capital of ₹ 194 Crores including ₹ 153 Crores cash and cash equivalent.
 - ⇒ Targeting new production from offshore
 - ⇒ Dirok gas & condensate commercial sales commenced on 26 Aug.2017 and continuing
- Developed Cost Optimized Through Innovation-** Adoption of Modular Gas Processing (M-GPP) on Opex Model results in - Reduction in capitals costs & Reduction in Project lead time, Early Monetisation through a 4" parallel pipeline to connect to OIL India Gas Process facility at Kusijian, M-GPP contract on build, maintenance and operate (BMO) model awarded to Expro, UK , Off-Site Work on M-GPP Commenced

Assam : Attractive fiscal terms

- Past Cost (Exploration & Appraisal) carry of \$100 Million, HOEC entitled to higher revenue share in initial years
- No profit petroleum during initial years
- Field operating cost is below \$ 0.60 /mmbtu
- Cess and Royalty is paid by the licensee Oil India Limited
- Condensate to get International crude oil price
- Over 75 % operating margin at a price of \$ 2.89/mmbtu
- Oil India Limited & IOC to buy all the produced gas and condensate through the constructed pipeline

Graphical presentation HY1 FY 2017-18 & FY 2017 Results

Particulars	Results Snapshot					₹ in CRORES		
	Standalone Results Quarter Ended			% Change (Q-O-Q)	% Change (Y-O-Y)	Standalone Results Year Ended		% Change
	Q2 FY 18	Q1 FY 18	Q2 FY 17			FY 17	FY 16	
Revenue	8.40	3.72	5.60	125.81%	50.00%	25.50	48.72	-47.66%
EBITDA	10.50	5.90	5.20	77.97%	101.92%	49.62	22.53	120.24%
EBITDA %	125.00%	158.60%	92.86%	-	-	194.59%	46.24%	-
PBT	5.57	2.93	13.46	90.10%	-58.62%	40.02	5.65	608.32%
PBT%	66.31%	78.76%	240.36%	-	-	156.94%	11.60%	1253.31%
PAT	5.58	2.94	1.86	89.80%	200.00%	7.20	0.25	2780.00%
PAT %	66.43%	79.03%	33.21%	-	-	28.24%	0.51%	5402.49%
EPS	0.43	0.23	1	86.96%	-57.00%	2.76	0.38	626.32%

Asset Portfolio (Production / Development)

Block Name	Operator	Location	Oil/Gas	PI	Partner(s)
PY-1	HOEC	Offshore	Gas	100%	Nil
CB-ON-7	HOEC	Onshore	Oil	35%	GSPC, ONGC
North Balol	HOEC	Onshore	Gas	25%	GSPC, GNRL Oil & Gas Ltd.
Asjol	HOEC	Onshore	Oil	50%	GSPC
AAP-ON-94/1	HOEC	Onshore	Gas	27%	Oil India Limited, ONGC
MB/OSDSF/ B-80/2016	HOEC	Offshore	Oil & Gas	50%	Adbhoot Estates Pvt Ltd
AA/ONDSF/ Kherem/2016	HOEC	Onshore	Oil & Gas	40%	Oil India Limited, Prize Petroleum
CB-OS/1	ONGC	Offshore	Oil	38%	ONGC, TATA PETRODYNE LIMITED
PY-3	HEPI	Offshore	Oil	21%	TATA PETRODYNE LIMITED, Hardy Oil and Gas plc, ONGC

Producing Development Development Deferred PI = Participating Interest

Industry Structure & Development

OPEC 2017 production cut agreement prevents oil prices from a steep fall. U.S.A. shale oil industry prevents it from soaring too high. This provides the Oil markets with a virtual new floor and a ceiling. Industry expectation, therefore, is for oil prices to float within a range of US\$ 50 to US\$ 60 per barrel. This new reality requires oil companies to build a new business model where value is created by innovative management of cost and speed of execution. Energy vision of Government of India has four pillars - energy access, energy efficiency, energy sustainability and energy security and the goal is to reduce import dependence by 10% by 2022.

Ministry of Petroleum & Natural Gas (MoP&NG) has launched and progressed several reform measures to realize this goal. They include direct transfer of subsidies, 'GIVE IT UP' campaign on LPG, freeing petroleum product prices to speeding up strategic storage of petroleum and LNG projects to the most popular and effective Ujwala free LPG scheme to below the poverty line beneficiaries.

Gas Pricing

Natural Gas prices increased in U.S.A. (Henry Hub) from US\$ 1.96 in April 2016 to US\$ 2.87 in March 2017 per mmbtu and similar trend was reflected in the Alberta Hub and other bench mark prices relevant to Indian gas pricing. The new Government announced a revised gas pricing policy on October 18, 2014. This pricing formula was linked to weighted average prices of Henry Hub, NBP, Alberta Hub and Russia with appropriate reduction for the transport and treatment charges

SWOT Analysis

Strengths & Opportunities

- ▲ All the nine assets in portfolio have discovered resources with potential upside
- ▲ Have competent technical and professional talent with rich oil and gas experience
- ▲ Proven development and operating experience in both onshore and offshore with an ability to execute on fast track with low cost.
- ▲ Debt-free Balance sheet with required funds for organic growth and ability to raise capital for inorganic growth.

Threats, Risks and Concerns

- ▲ Volatility in the oil and gas prices since company does not undertake any oil price hedge.
- ▲ Foreign Exchange Exposure & Interest Rate Risk
- ▲ Cost inflation impacting both goods & services.

Company Overview

The Company's activities relate to exploration, development and production (based on exploration success) of hydrocarbons (crude oil and natural gas), which are natural resources. HOEC assets are geographically spread across Tamil Nadu, Gujarat and Assam with a balanced portfolio of development and production projects, both in onshore and offshore

Valuation Conclusion

HOEC future Plan to step up gas production to 25 mmscfd during FY 2017-2018; complete surface facilities with capacity of 36 mmscfd (1 mmscmd); recast the reserves on completion of sixth well and based on performance data, seek permission to increase production with total 6 wells, to invest in projects where "Investment to Cash" cycle is 12 to 18 months, HOEC will continuously look for ideas, opportunities, talent and technology that has the potential to improve oil & gas discovery and recovery rates.

Company's portfolio now consists of 9 assets and all of them have discovered resources with some upside potential, has capital requirements to implement its business plans and to continue the development of Dirok field in Assam, revisiting the development of PY-1 field, B-80, Kherem and other fields in the immediate future, which can be met through the existing working capital. It is now a debt-free company with adequate cash to fund organic growth.

Therefore, considering the above stated factors we recommend to accumulate the stock for long term perspective.

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