

March 7, 2022

Commodity prices surge amid geopolitical conflict...

Global oil & gas prices surged sharply amid concern over supply disruption following the geopolitical conflict in Europe. Russia is a major supplier of oil & gas to the world, Europe and it constitutes 12%, 31% of oil requirement, respectively. Similarly, for gas supply, the world and Europe are dependent on Russian supply for 17% and 33% of its total requirement, respectively. Brent oil prices are currently trending at multi-year highs whereas LNG futures are also trading at elevated level. Surge in oil & gas prices will benefit upstream and gas utility companies as realisation will be higher. On the CGD front, companies with higher industrial segment share in the sales mix will be adversely impacted if prices sustain at higher levels.

Upstream companies to benefit from higher realisation

- Brent oil prices are currently trading at US\$128/bbl, up ~65% compared to closing price of US\$77.5/bbl in Q3FY22
- Surge in oil prices will lead to better realisation, benefitting ONGC

Gujarat Gas to be impacted by higher LNG prices

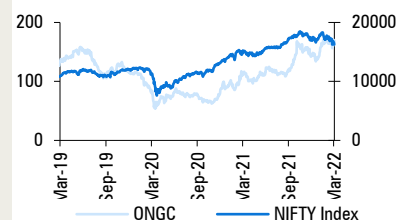
- In our CGD coverage universe, Gujarat Gas (GGL) has the highest share of industrial segment in its sales mix (more than 70% of total volume). Gas procurement for this segment is largely catered by LNG. Hence, overall margin sensitivity to LNG price changes is higher
- Spot LNG prices were relatively lower at the end of January. However, a sharp rebound was seen in spot LNG prices since the start of geopolitical tension and LNG futures are also trading at elevated levels
- If prices sustain at high levels, it will impact margins of GGL as the company's sourcing costs will be higher for incremental volumes
- The company had hiked prices for incremental volumes in Morbi Industrial area in January. We believe industrial volume growth will be limited for Gujarat Gas in the near term amid higher LNG prices. We estimate total sales volume at 11.1 and 13.4 mmscmd in FY23E and FY24E, respectively
- For Indraprastha Gas (IGL) and Mahanagar Gas (MGL), industrial volume contributes less in the sales mix (in the range of 8-14%) compared to Gujarat Gas. However, higher spot LNG prices will impact both CGD companies in the near term amid shortfall in APM allocation

Valuation and Outlook

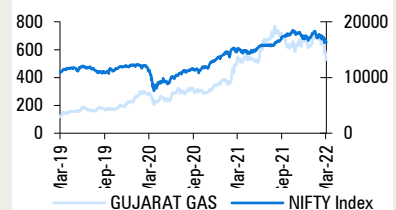
ONGC will gain from increase in oil prices amid geopolitical conflict. We revise rating from HOLD to BUY on ONGC amid favourable oil prices and value ONGC at ₹ 225 i.e. ₹ ~203 for core oil & gas business and ₹ ~21 for subsidiaries and other investments.

On the CGD front, we maintain our BUY rating on IGL with a target price of ₹ 395/share (standalone at ~₹ 357 i.e. 20x P/E on FY24E EPS and investments at ~₹ 39). We maintain HOLD rating on GGL and MGL. We value GGL at ₹ 530 i.e. 25x P/E on FY24E EPS and MGL at ₹ 775 i.e. 10x P/E on FY24E EPS.

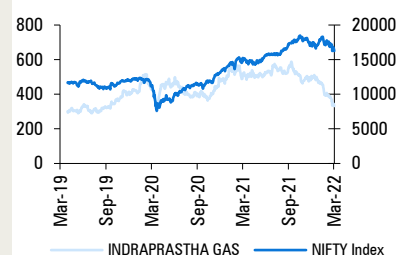
Price Chart (ONGC)



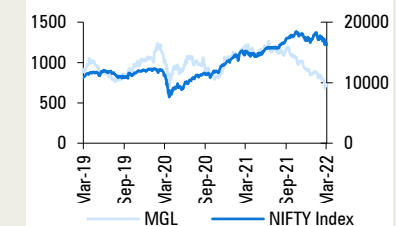
Price Chart (Gujarat Gas)



Price Chart (Indraprastha Gas)



Price Chart (Mahanagar Gas)



Key risks

- (i) Lower than expected oil prices & oil & gas production
- (ii) inability to pass on further increase in costs
- (iii) slower than expected sales volume growth
- (iv) better than estimated margins

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Exhibit 1: Valuation and target matrix

	CMP	FY24E EPS		Change	Target		Rating	Comments
		Old	New		Old	New		
ONGC	187.0	30.0	32.8	9%	185.0	225.0	Buy	Oil prices surged to multi-year highs amid concerns over supply disruption following geopolitical conflict. We build-in oil realisation at US\$78.5/bbl for FY24E as oil futures contract are trending at higher level. On account of favourable oil price trend, we revise our rating from HOLD to BUY
Indraprastha Gas	340.0	21.9	17.8	-19%	475.0	395.0	Buy	Shortfall in APM allocation and higher spot LNG prices will impact the company in the near term. We estimate gross margins at ₹ 11/scm and ₹ 11.6/scm in FY23E and FY24E, respectively. We retain BUY rating on Indraprastha Gas on account of better volume growth prospects in medium to long term
Gujarat Gas	500.0	28.0	21.1	-24%	700.0	530.0	Hold	Industrial segment constitutes more than 70% of total volume. Higher spot LNG prices are likely to limit the volume growth in near term. We estimate gross margins at ₹ 7/scm and ₹ 7.1/scm in FY23E and FY24E, respectively
Mahanagar Gas	708.0	98.4	81.4	-17%	885.0	775.0	Hold	Higher gas procurement costs due to surge in LNG prices and lower domestic gas allocation will affect margins of MGL in the near term. We estimate gross margins at ₹ 14.3/scm and ₹ 14.9/scm in FY23E and FY24E, respectively

Source: Company, ICICI Direct Research

Exhibit 2: Sensitivity of ONGC's standalone FY24E PAT to change in oil prices

	Base case				
	60.0	70.0	80.0	90.0	100.0
Oil price (US\$/bbl)	60.0	70.0	80.0	90.0	100.0
PAT (₹ crore)	30,138.1	35,695.7	41,253.3	46,810.8	52,368.4
EPS (₹)	24	28.4	32.8	37.2	41.6

Source: Bloomberg, ICICI Direct Research

Exhibit 3: ICICI Direct coverage universe

Sector / Company	CMP (₹)	TP (₹)	Rating	M Cap (₹ Cr)	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
					FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
BPCL (BHAPET)	338	450	Buy	70,740	91.0	43.4	39.8	3.7	7.8	8.5	5.7	6.0	5.9	14.8	14.7	13.2	34.9	19.0	16.1
GAIL (India) (GAIL)	162	180	Buy	71,934	11.0	22.4	17.8	14.7	7.2	9.1	11.8	5.6	6.8	8.7	18.5	13.1	10.5	18.5	13.4
Gujarat Gas (GUJGA)	500	530	Hold	34,420	18.5	14.3	15.2	27.0	35.1	32.8	16.8	20.9	19.3	31.7	22.1	21.2	28.5	19.1	18.1
HPCL (HINPET)	276	320	Hold	39,162	70.6	46.4	44.2	3.9	6.0	6.2	5.2	6.8	6.1	15.6	9.6	9.2	29.5	16.7	14.5
Indian Oil Corp (INDOIL)	112	150	Buy	1,02,828	23.8	25.4	19.2	4.7	4.4	5.8	2.7	2.5	2.8	13.3	13.9	10.6	19.8	18.3	12.9
Indraprastha Gas (INDGAS)	340	395	Buy	23,800	14.4	19.8	14.9	23.7	17.2	22.9	15.3	11.5	14.4	20.0	24.1	15.9	17.1	20.1	13.8
Mahanagar Gas (MAHGAS)	708	770	Hold	6,993	62.7	65.4	71.3	11.3	10.8	9.9	7.0	6.7	5.9	23.1	21.7	21.3	19.2	18.1	17.7
ONGC (ONGC)	187	225	Buy	2,39,983	8.9	32.3	36.8	20.9	5.8	5.1	7.8	4.3	3.0	4.5	14.5	20.3	5.5	17.4	17.5
Petronet LNG (PETLNG)	218	220	Hold	32,700	19.7	21.3	19.7	11.1	10.2	11.1	6.8	5.9	6.3	26.0	26.5	22.7	25.3	25.1	21.7
Reliance Industries (RELIND)	2,240	2,950	Buy	15,14,688	76.2	90.2	106.3	29.4	24.8	21.1	21.3	15.2	11.5	5.5	7.7	9.7	7.7	8.6	9.5

Source: Bloomberg, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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