

## CAIRN INDIA

OIL &amp; GAS

# HOLD

Target Price: Rs 270

### Merger near conclusion

Cairn management expects its impending merger with Vedanta to conclude by Mar '17. Extension of Production Sharing Contract (PSC) beyond 2020, which is currently sub judice, would kick-start investments in Rajasthan fields. Management expects its five key exploration projects in Rajasthan to generate IRR of 18% even with Brent at USD 45/bl.

**Hike estimates; Maintain HOLD:** We increase FY18 EPS by 41% due to (a) higher crude price assumption of USD 60/bl (USD 50/bl earlier), and (b) raising FX rate to INR 69.3/USD (67.3 earlier). However, CMP factors in long term crude at USD60/bl and Rajasthan peak volume at 200 kbpd. **Maintain HOLD with TP of Rs 270** (Rs 235 earlier). **Key upside triggers:** (a) PSC extension, (b) exploration capex leading to higher volumes, and (c) favorable commodity/ FX rates.

CMP : Rs 275  
Potential Upside : -2%

#### MARKET DATA

No. of Shares : 1,876mn  
Free Float : 40%  
Market Cap : Rs 515 bn  
52-week High / Low : Rs 286 / Rs 111  
Avg. Daily vol. (6mth) : 2.9 mn shares  
Bloomberg Code : CAIR IB Equity  
Promoters Holding : 60%  
FII / DII : 15% / 12%

### Analyst call highlights

- ◆ Cairn will spend at least USD 500 mn in Rajasthan fields over next 2 years. The five growth projects identified by management will require total capex of USD 1 bn, subject to extension of PSC
- ◆ Cairn may outsource development of few of its projects to global oil services contractors to improve cost efficiencies
- ◆ Q3 volume declined due to maintenance shutdown. Management likely to give clarity on FY18 volumes by Apr '17

### Q3FY17 highlights: EBITDA in line; higher tax hits PAT

EBITDA at Rs 11 bn was in line with our estimate. However, PAT at Rs 6 bn (vs. Rs 7.4 bn expected) was impacted by higher tax rate of 22% (8% expected). Cairn's realized crude price was at 7% discount to Brent (9% in Q2) as high heavy distillate (FO/ LSWR) cracks supported demand/ price of heavier crude grades (such as Cairn's crude).

**Basis for our TP:** We value Cairn at FY18 EV/EBITDA of 5x. Brent prices are assumed at USD60/bl and INR:USD at 69.3. We fully value cash and ascribe zero value to Inter Corporate Deposits.

#### Financial summary (Consolidated)

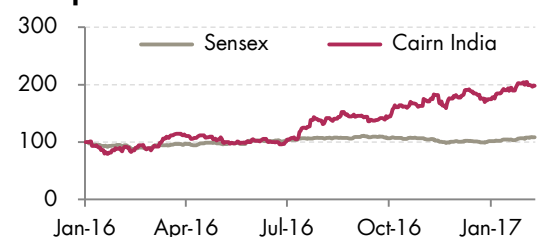
Y/E March	FY15	FY16	FY17E	FY18E
Sales (Rs mn)	146,462	86,256	85,095	105,684
Adj PAT (Rs mn)	71,126	13,300	27,653	33,289
Con. EPS* (Rs.)	-	-	10.3	13.1
EPS (Rs.)	37.9	7.1	14.7	17.8
Change YOY (%)	(42.8)	(81.3)	107.9	20.4
P/E (x)	7.2	38.7	18.6	15.5
RoE (%)	12.2	2.5	5.6	6.4
RoCE (%)	13.1	2.8	6.1	8.0
EV/EBITDA (x)	5.9	13.8	10.7	7.1
DPS	9.0	3.0	4.4	5.3

Source: \*Consensus broker estimates, Company, Axis Capital

#### Key drivers

	FY16	FY17E	FY18E
RJ avg output (kbpd)	167	162	165
Crude prices (US\$/ bl)	48	50	60
Discount	16.3%	13.0%	13.0%
INR:USD	65.4	67.6	69.3

#### Price performance



**Exhibit 1: Results update**

(Rs mn)	Q3FY16	Q2FY17	Q3FY17	YoY	QoQ
<b>Income from Operations</b>	<b>20,395</b>	<b>20,386</b>	<b>21,494</b>	<b>5%</b>	<b>5%</b>
Share of expenses in Producing oil & gas blocks	5,435	4,645	4,644	-15%	0%
(Increase) / Decrease In stocks	13	(186)	118	-	-
Employee Benefit Expenses	355	178	224	-37%	26%
Cess	6,842	4,951	5,300	-23%	7%
Other Expenses	642	396	353	-45%	-11%
Total expenses	13,288	9,984	10,639	-20%	7%
<b>EBITDA</b>	<b>7,107</b>	<b>10,402</b>	<b>10,855</b>	<b>53%</b>	<b>4%</b>
DD&A	10,120	7,818	7,260	-28%	-7%
Other Income	3,927	5,349	5,239	33%	-2%
Foreign Exchange Fluctuation Gain / (Loss)	(462)	644	(788)	71%	-
<b>EBIT</b>	<b>452</b>	<b>8,577</b>	<b>8,046</b>	<b>-</b>	<b>-6%</b>
Interest	159	193	290	83%	50%
<b>PBT (recurring)</b>	<b>293</b>	<b>8,384</b>	<b>7,756</b>	<b>-</b>	<b>-7%</b>
Unsuccessful & General exploration costs	47	11	18	-63%	59%
<b>PBT (reported)</b>	<b>246</b>	<b>8,373</b>	<b>7,738</b>	<b>-</b>	<b>-8%</b>
<b>Tax</b>	<b>(164)</b>	<b>586</b>	<b>1,700</b>	<b>-</b>	<b>190%</b>
<b>PAT</b>	<b>409</b>	<b>7,787</b>	<b>6,038</b>	<b>-</b>	<b>-22%</b>

Source: Company, Axis Capital

**Profit & loss (Rs mn)**

Y/E March	FY15	FY16	FY17E	FY18E
Net sales	146,462	86,256	85,095	105,684
Other operating income	-	-	-	-
<b>Total operating income</b>	<b>146,462</b>	<b>86,256</b>	<b>85,095</b>	<b>105,684</b>
Cost of goods sold	-	-	-	-
Gross profit	146,462	86,256	85,095	105,684
<i>Gross margin (%)</i>	<i>100.0</i>	<i>100.0</i>	<i>100.0</i>	<i>100.0</i>
Total operating expenses	(61,236)	(50,568)	(43,114)	(48,273)
<b>EBITDA</b>	<b>85,226</b>	<b>35,688</b>	<b>41,981</b>	<b>57,411</b>
<i>EBITDA margin (%)</i>	<i>58.2</i>	<i>41.4</i>	<i>49.3</i>	<i>54.3</i>
Depreciation	(25,695)	(35,227)	(31,596)	(32,885)
<b>EBIT</b>	<b>59,532</b>	<b>460</b>	<b>10,385</b>	<b>24,526</b>
Net interest	(203)	(708)	(750)	(750)
Other income	18,093	14,942	20,422	17,835
<b>Profit before tax</b>	<b>77,421</b>	<b>14,694</b>	<b>30,057</b>	<b>41,611</b>
Total taxation	(6,295)	(1,394)	(2,405)	(8,322)
<i>Tax rate (%)</i>	<i>8.1</i>	<i>9.5</i>	<i>8.0</i>	<i>20.0</i>
Profit after tax	71,126	13,300	27,653	33,289
Minorities	-	-	-	-
Profit/ Loss associate co(s)	-	-	-	-
Adjusted net profit	71,126	13,300	27,653	33,289
<i>Adj. PAT margin (%)</i>	<i>48.6</i>	<i>15.4</i>	<i>32.5</i>	<i>31.5</i>
Net non-recurring items	(26,330)	(10,263)	-	-
Reported net profit	44,796	3,037	27,653	33,289

**Balance sheet (Rs mn)**

Y/E March	FY15	FY16	FY17E	FY18E
Paid-up capital	18,749	18,749	18,749	18,749
Reserves & surplus	569,954	469,177	487,124	508,728
Net worth	588,702	487,926	505,872	527,477
Borrowing	-	-	-	-
Other non-current liabilities	12,718	11,028	11,028	11,028
<b>Total liabilities</b>	<b>601,420</b>	<b>498,954</b>	<b>516,901</b>	<b>538,505</b>
Gross fixed assets	383,817	311,639	313,882	323,977
Less: Depreciation	(130,853)	(161,860)	(193,455)	(226,341)
Net fixed assets	252,964	149,779	120,427	97,636
Add: Capital WIP	59,067	43,402	47,888	52,375
Total fixed assets	312,030	193,181	168,315	150,011
Total Investment	152,334	150,541	150,541	150,541
Inventory	3,439	4,683	4,683	4,683
Debtors	11,250	2,571	2,536	3,150
Cash & bank	8,517	23,855	66,701	105,996
Loans & advances	178,498	186,303	186,303	186,303
Current liabilities	66,923	66,002	66,002	66,002
Net current assets	137,056	155,232	198,044	237,952
Other non-current assets	-	-	-	-
<b>Total assets</b>	<b>601,420</b>	<b>498,954</b>	<b>516,901</b>	<b>538,505</b>

Source: Company, Axis Capital

**Cash flow (Rs mn)**

Y/E March	FY15	FY16	FY17E	FY18E
Profit before tax	77,421	14,694	30,057	41,611
Depreciation & Amortisation	25,695	35,227	31,596	32,885
<i>Chg in working capital</i>	<i>(89,632)</i>	<i>(2,839)</i>	<i>35</i>	<i>(614)</i>
<b>Cash flow from operations</b>	<b>(13,779)</b>	<b>33,736</b>	<b>59,283</b>	<b>65,560</b>
<i>Capital expenditure</i>	<i>23,829</i>	<i>83,622</i>	<i>(6,730)</i>	<i>(14,582)</i>
<b>Cash flow from investing</b>	<b>23,829</b>	<b>83,622</b>	<b>(6,730)</b>	<b>(14,582)</b>
<i>Equity raised/ (repaid)</i>	<i>(328)</i>	-	-	-
<i>Debt raised/ (repaid)</i>	-	-	-	-
<i>Dividend paid</i>	<i>(19,742)</i>	<i>(6,581)</i>	<i>(9,706)</i>	<i>(11,684)</i>
<b>Cash flow from financing</b>	<b>(20,069)</b>	<b>(6,581)</b>	<b>(9,706)</b>	<b>(11,684)</b>
Net chg in cash	(10,020)	110,777	42,847	39,294

**Key ratios**

Y/E March	FY15	FY16	FY17E	FY18E
<b>OPERATIONAL</b>				
FDEPS (Rs)	37.9	7.1	14.7	17.8
CEPS (Rs)	37.6	20.4	31.6	35.3
DPS (Rs)	9.0	3.0	4.4	5.3
Dividend payout ratio (%)	37.7	185.2	30.0	30.0
<b>GROWTH</b>				
Net sales (%)	(21.9)	(41.1)	(1.3)	24.2
EBITDA (%)	(37.7)	(58.1)	17.6	36.8
Adj net profit (%)	(42.8)	(81.3)	107.9	20.4
FDEPS (%)	(42.8)	(81.3)	107.9	20.4
<b>PERFORMANCE</b>				
RoE (%)	12.2	2.5	5.6	6.4
RoCE (%)	13.1	2.8	6.1	8.0
<b>EFFICIENCY</b>				
Asset turnover (x)	0.3	0.2	0.2	0.2
Sales/ total assets (x)	0.2	0.1	0.1	0.2
Working capital/ sales (x)	0.6	1.5	1.5	1.2
Receivable days	28.0	10.9	10.9	10.9
Inventory days	20.5	33.8	39.6	35.4
Payable days	54.8	75.0	87.9	78.5
<b>FINANCIAL STABILITY</b>				
Total debt/ equity (x)	-	-	-	-
Net debt/ equity (x)	-	-	(0.1)	(0.2)
Current ratio (x)	3.0	3.4	4.0	4.6
Interest cover (x)	292.7	0.6	13.8	32.7
<b>VALUATION</b>				
PE (x)	7.2	38.7	18.6	15.5
EV/ EBITDA (x)	5.9	13.8	10.7	7.1
EV/ Net sales (x)	3.5	5.7	5.3	3.9
PB (x)	0.9	1.1	1.0	1.0
Dividend yield (%)	3.3	1.1	1.6	1.9
Free cash flow yield (%)	2.0	22.8	10.2	9.9

Source: Company, Axis Capital

**Disclosures:**

The following Disclosures are being made in compliance with the SEBI Research Analyst Regulations 2014 (herein after referred to as the Regulations).

1. Axis Securities Ltd. (ASL) is a SEBI Registered Research Analyst having registration no. INH000000297. ASL, the Research Entity (RE) as defined in the Regulations, is engaged in the business of providing Stock broking services, Depository participant services & distribution of various financial products. ASL is a subsidiary company of Axis Bank Ltd. Axis Bank Ltd. is a listed public company and one of India's largest private sector bank and has its various subsidiaries engaged in businesses of Asset management, NBFC, Merchant Banking, Trusteeship, Venture Capital, Stock Broking, the details in respect of which are available on [www.axisbank.com](http://www.axisbank.com).
2. ASL is registered with the Securities & Exchange Board of India (SEBI) for its stock broking & Depository participant business activities and with the Association of Mutual Funds of India (AMFI) for distribution of financial products and also registered with IRDA as a corporate agent for insurance business activity.
3. ASL has no material adverse disciplinary history as on the date of publication of this report.
4. I/We, authors (Research team) and the name/s subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect my/our views about the subject issuer(s) or securities. I/We also certify that no part of my/our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report. I/we or my/our relative or ASL does not have any financial interest in the subject company. Also I/we or my/our relative or ASL or its Associates may have beneficial ownership of 1% or more in the subject company at the end of the month immediately preceding the date of publication of the Research Report. Since associates of ASL are engaged in various financial service businesses, they might have financial interests or beneficial ownership in various companies including the subject company/companies mentioned in this report. I/we or my/our relative or ASL or its associates do not have any material conflict of interest. I/we have not served as director, officer or employee in the subject company.

**Research Team**

Sr. No	Name	Designation	E-mail
1	Akhand Singh	Research Analyst	akhand.singh@axissecurities.in
2	Sankar Narayanan	Database Manager	sankar.narayanan@axissecurities.in

5. ASL or its associates has not received any compensation from the subject company in the past twelve months. ASL or its Research Analysts has not been engaged in market making activity for the subject company.

6. In the last 12-month period ending on the last day of the month immediately preceding the date of publication of this research report, ASL or any of its associates may have:

- i. Received compensation for investment banking, merchant banking or stock broking services or for any other services from the subject company of this research report and / or;
- ii. Managed or co-managed public offering of the securities from the subject company of this research report and / or;
- iii. Received compensation for products or services other than investment banking, merchant banking or stock broking services from the subject company of this research report;

ASL or any of its associates have not received compensation or other benefits from the subject company of this research report or any other third-party in connection with this report

**Term& Conditions:**

This report has been prepared by ASL and is meant for sole use by the recipient and not for circulation. The report and information contained herein is strictly confidential and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of ASL. The report is based on the facts, figures and information that are considered true, correct, reliable and accurate. The intent of this report is not recommendatory in nature. The information is obtained from publicly available media or other sources believed to be reliable. Such information has not been independently verified and no guaranty, representation of warranty, express or implied, is made as to its accuracy, completeness or correctness. All such information and opinions are subject to change without notice. The report is prepared solely for informational purpose and does not constitute an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments for the clients. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. ASL will not treat recipients as customers by virtue of their receiving this report.

DEFINITION OF RATINGS	
Ratings	Expected absolute returns over 12-18 months
BUY	More than 10%
HOLD	Between 10% and -10%
SELL	Less than -10%

**Disclaimer:**

Nothing in this report constitutes investment, legal, accounting and tax advice or a representation that any investment or strategy is suitable or appropriate to the recipient's specific circumstances. The securities and strategies discussed and opinions expressed, if any, in this report may not be suitable for all investors, who must make their own investment decisions, based on their own investment objectives, financial positions and needs of specific recipient.

This report may not be taken in substitution for the exercise of independent judgment by any recipient. Each recipient of this report should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this report (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. Certain transactions, including those involving futures, options and other derivatives as well as non-investment grade securities involve substantial risk and are not suitable for all investors. ASL, its directors, analysts or employees do not take any responsibility, financial or otherwise, of the losses or the damages sustained due to the investments made or any action taken on basis of this report, including but not restricted to, fluctuation in the prices of shares and bonds, changes in the currency rates, diminution in the NAVs, reduction in the dividend or income, etc. Past performance is not necessarily a guide to future performance. Investors are advised necessarily a guide to future performance. Investors are advised to see Risk Disclosure Document to understand the risks associated before investing in the securities markets. Actual results may differ materially from those set forth in projections. Forward-looking statements are not predictions and may be subject to change without notice.

ASL and its affiliated companies, their directors and employees may; (a) from time to time, have long or short position(s) in, and buy or sell the securities of the company(ies) mentioned herein or (b) be engaged in any other transaction involving such securities or earn brokerage or other compensation or act as a market maker in the financial instruments of the company(ies) discussed herein or act as an advisor or investment banker, lender/borrower to such company(ies) or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions. Each of these entities functions as a separate, distinct and independent of each other. The recipient should take this into account before interpreting this document.

ASL and / or its affiliates do and seek to do business including investment banking with companies covered in its research reports. As a result, the recipients of this report should be aware that ASL may have a potential conflict of interest that may affect the objectivity of this report. Compensation of Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions. ASL may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

Neither this report nor any copy of it may be taken or transmitted into the United State (to U.S. Persons), Canada, or Japan or distributed, directly or indirectly, in the United States or Canada or distributed or redistributed in Japan or to any resident thereof. If this report is inadvertently sent or has reached any individual in such country, especially, USA, the same may be ignored and brought to the attention of the sender. This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject ASL to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors.

The Disclosures of Interest Statement incorporated in this document is provided solely to enhance the transparency and should not be treated as endorsement of the views expressed in the report. The Company reserves the right to make modifications and alternations to this document as may be required from time to time without any prior notice. The views expressed are those of the analyst(s) and the Company may or may not subscribe to all the views expressed therein.

Copyright in this document vests with Axis Securities Limited.

Axis Securities Limited, Corporate office: Unit No. 2, Phoenix Market City, 15, LBS Road, Near Kamani Junction, Kurla (west), Mumbai-400070, Tel No. – 18002100808/022-61480808, Regd. off.- Axis House, 8th Floor, Wadia International Centre, PandurangBudhkarMarg, Worli, Mumbai – 400 025. Compliance Officer: AnandShaha, Email: compliance.officer@axisdirect.in, Tel No: 022-42671582.