

15 September 2016

Initiating Coverage (BUY)

DEEP INDUSTRIES

CMP

INR 193

Target Price

INR 287

Stock Details

Industry	Oil and Gas
Bloomberg Code	DEEPI:IN
BSE Code	532760
Face Value (Rs.)	10.00
Market Cap. (Rs. Mn)	581.08
52wk. High/Low (Adjusted) ((Rs.)	116.1 / 215.7

Shareholding Pattern Jun '15

Promoter (%)	44.46
FII (%)	3.86
DII (%)	8.10
Public - Other (%)	43.59
No. of Share Outstanding (mn)	40.09

Valuation Summary

	FY 15A	FY 16A	FY 17P	FY 18P
P/E (x)*	7.22	13.76	14.00	12.00
EV/EBITDA (x)	7.54	15.44	14.66	12.93
P/BV (x)	1.65	5.16	6.01	5.51

*TTM for Current Year

Based on Market Price as on 1st Apr is taken for Each FY

Key Financial

Rs. Mn	FY 15A	FY 16A	FY 17P	FY 18P
Net Sales	1012.6	1691.5	2198	2748
EBITDA	563	971	1274	1559
Net Profit	212	410	544	699
EPS (Rs.)*	7.3	14	18.6	24

*Un adjusted

Key Ratios

	FY 15A	FY 16A	FY 17P	FY 18P
EBITDA Margin (%)	54.9	57.4	57	55.9
EBIT Margin (%)	43	45.3	46.3	47.1
Net Pro. Margin (%)	20.7	24.2	24.3	25.1
Debt/Equity (x)	0.34	0.72	0.62	0.52
RoNW (%)	10.3	17.2	19.5	21.3
RoCE (%)	6.8	10.2	10.8	12.6

One Year Price / Volume



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We recommend 'BUY' on DEEP INDUSTRIES for a target of INR 287 - valuing the company at P/E of 12x FY18E Earning.

INVESTMENT RATIONALE:

- Well diversified portfolio.
- Long term client relationships.
- Service Business
- Customized solution provider in Oil and Gas value chain.
- Leadership in Gas Compression Business
- In a business with high entry barriers
- Dealing in a growing market
- Leading Solution provider for Coring, Air Drilling, Work over and Drilling and Rig Services to Oil-Gas companies in India
- Immense Opportunity due to Government Regulation
- Leveraging Technical Capabilities to Grab Opportunities
- Competition is low with the exit of few key players making the segment an attractive play for serious long term contenders.
- Low crude prices, soft metal prices and availability of skilled labor improves margin profile significantly.
- India has a stated policy of increasing energy reserves where the PSU's contribute significantly.
- 1st Mover advantage in Gas compression and De-hydration segment in India.

VALUATIONS AND VIEW:

It is a company focused on deploying fuel efficient, latest Equipment in the Oil and GAS Industry with a Vision to become an Integrated Solution provider with a focus on Domestic and International Market. **We value the business at 12x FY18E EPS and recommend a BUY rating on the stock with a target price of INR 287 per share.**

RISK & CONCERNS:

- **Client Concentration:** 50% of the order book consist of orders from ONGC

COMPANY BACKGROUND:

Deep Industries Limited started in the year 1991, with a primary objective of catering the ever increasing demand for Oil and Gas Industry. Since its inception, Deep Industries Limited has been serving the industry in various segments with the foremost being providing Air & Natural Gas Compressor Services on chartered hire basis, wherein company commands a healthy market position and is also the first company in India to offer such services. Apart from starting as a Service provider, Deep Industries Limited successfully forayed itself in Exploration and Production segment and having various Onshore Oil and Natural Gas blocks, Coal Bed Methane Blocks awarded under different rounds of NELP and CBM bidding. The Company has grown up to be a "One Stop Solution" provider for every need in Oil and Gas field operations by catering various equipment and services under rental and chartered-hire basis

Clients-

- ONGC
- Cairn
- Oil India Limited
- Selan Exploration
- Reliance
- Prize Petroleum
- Dilex Limited

INDUSTRY OVERVIEW:

The oil and gas sector is among the six core industries in India and plays a major role in influencing decision making for all the other important sections of the economy. Backed by new oil fields, domestic oil output is anticipated to grow to 1 MBPD by FY16. With India developing gas-fired power stations, consumption is up more than 160 per cent since 1995. Gas consumption is likely to expand at a Compound Annual Growth Rate(CAGR) of 21 per cent during FY08–17. Presently, domestic production accounts for more than three-quarters of the country's total gas consumption. According to data released by the Department of Industrial Policy and Promotion (DIPP), the petroleum and natural gas sector attracted FDI worth US\$ 6.67 billion between April 2000 and March 2016. Some of the major initiatives taken by the Government of India to promote oil and gas sector are:

- The Union Cabinet has approved the National Mineral Exploration Policy (NMEP), which will pave the way for auction of 100 prospective mineral blocks to attract private sector in exploration, besides involving state-run agencies.
- The government has launched a pilot programme, aimed at introducing compressed natural gas (CNG) as fuel for two-wheelers.
- The Ministry of Petroleum and Natural Gas is seeking to enhance India's crude oil refining capacity through 2040 by setting up a high-level panel, which will work towards aligning India's energy portfolio with changing trends and transition towards cleaner sources of energy generation.
- The Ministry of New and Renewable Energy (MNRE) plans to launch an integrated bio energy mission with an investment of Rs 10,000 crore (US\$ 1.48 billion) from FY 2017-18 to FY 2021-22, aimed at enhancing the use of bio-fuels like ethanol and biogas and reducing consumption of fossil fuels.
- The Hydrocarbon Sector Skill Council (HSSC), which was set up by the Government of India under its Skill India initiative, plans to train over 1.9 million people in the oil and gas sector over the next 10 years, to cater to the rising skill needs of the industry.

- The Union Cabinet has allowed state-owned oil firms to evolve their own crude oil import policies which involve freedom to choose source companies as well as pricing for their crude oil imports, thus allowing them to compete in the market effectively.
- In a major drive to enhance the petroleum and hydrocarbon sector, Government of India has introduced initiatives like the Hydrocarbon Exploration Licensing Policy (HELP), Marketing and Pricing freedom for new gas production, grant of extension to the Production Sharing Contracts and assigning the Ratna offshore field award to Oil and Natural Gas Corporation (ONGC) for development.
- Mr Dharmendra Pradhan, Minister of State (Independent Charge) for Petroleum and Natural Gas has released the Hydrocarbon Vision 2030 for North East India, with the objective of leveraging the north-eastern region's hydrocarbon potential, enhance access to clean fuels, improve availability of petroleum products, facilitate economic development and to involve local population in the economic activities in this sector.
- The Government of India plans to incentivise gas production from deep-water, ultra deep-water and high pressure-high temperature areas which are presently not exploited on account of higher cost and risk, and also to augment the investment in nuclear power generation in the next 15 to 20 years.
- The Government of India is in the process of identifying at least 50 potential blocks of 100 sq km and above to be given to companies for bringing private investment in the mineral exploration sector. The Ministry of Petroleum and Natural Gas has put up for comments a draft policy, to opt for revenue-sharing model while auctioning future oil and gas blocks for exploration to private companies, compared to production-sharing mode earlier, in order to make the process more transparent and market-oriented.
- The Ministry of Petroleum and Natural Gas has announced a new 'Marginal Fields Policy', which aims to bring into production 69 marginal oil and gas fields with 89 million tonnes or Rs 75,000 crore (US\$ 11.12 billion) worth of reserves, by offering various incentives to oil and gas explorers such as exemption from payment of oil cess and customs duty on machinery and equipment.
- Government of India entered into bilateral discussion with Norway to extend co-operation between the two countries in the field of oil and natural gas and hydrocarbon exploration.
- To strengthen the country's energy security, oil diplomacy initiatives have been intensified through meaningful engagements with hydrocarbon rich countries.
- PAHAL - Direct Benefit Transfer for LPG consumer (DBTL) scheme launched in 54 districts on November 11, 2014 and expanded to rest of the country on January 1, 2015 will cover 15.3 crore active LPG consumers of the country.
- 24 x 7 LPG service via web launched to provide LPG consumers an integrated solution to carry out all services at one place, through MyLPG.in, from the comfort of their home.
- The Government of India launched the 'Give It Up' campaign on LPG subsidy that helped it save Rs 140 crore (US\$ 20.75 million) as on July 22, 2015 with nearly 1.26 million Indians registering for the cause. As per recent statistics from oil ministry, as many as 30,000 to 40,000 households are giving up LPG subsidy each day.
- As part of the special dispensation for North East Region, for incentivising exploration and production in North East Region, 40 per cent subsidy on gas price has been extended to private companies operating in the region, along with ONGC and OIL.
- The Cabinet Committee on Economic Affairs (CCEA), chaired by Prime Minister Mr Narendra Modi, has approved a mechanism for procurement of Ethanol by Public Sector Oil Marketing Companies (OMCs) to carry out the Ethanol Blended Petrol (EBP) Program.

Peer Comparison

Company	CMP (Rs)	P/E*	Mcap (Rs Cr)	Div Yld (%)	NP Qtr (Rs Cr)	Qtr Profit Var (%)	Sales Qtr (Rs Cr)	Qtr Sales Var (%)	CMP/BV
Reliance Inds.	1,045	11.9	3,38,823.5	0.91	7,548.0	18.51	53,496.0	(18.72)	1.37
Essar Oil	166	20.3	659.0	NaN	364.0	47.98	10,909.0	(46.25)	5.24
Gujarat Gas	615	40.2	8,465.1	0.41	75.9	29.51	1,224.8	(26.70)	3.89
Deep Industries	193	11.2	563.3	0.52	16.3	142.35	64.4	136.21	2.09
Gagan Gases	9	52.3	4.2	-	(0.0)	(300.00)	0.1	(53.57)	4.70

FINANCIAL OVERVIEW

(in Million)	Q4 FY16 Performance Highlight							
	1Q FY16	2Q FY16	3Q FY16	4Q FY16	1Q FY17	YoY (%)	QoQ (%)	
Revenue	27.26	34.24	52.69	54.89	64.39	136.21%	17.31%	
Other Income	0.24	0.34	0.17	0.12	0.24			
Total Income	27.49	34.58	52.86	55.01	64.63	135.10%	17.49%	
Expenditure	-11.53	-15.49	-21.41	-24.49	-27.66			
As a % of Sales	42.30%	45.24%	40.63%	44.62%	42.96%			
Interest	-2.51	-3.75	-4.05	-4.72	-6.56	161.35%	38.98%	
PBDT	13.46	15.34	27.4	25.8	30.42			
As a % of Sales	49.38%	44.80%	52.00%	47.00%	47.24%			
Depreciation	-3.31	-3.52	-4.4	-9.2	-6.85			
PBT	10.16	11.82	23	16.6	23.57	131.99%	41.99%	
As a % of Sales	37.27%	34.52%	43.65%	30.24%	36.61%			
Tax	-3.43	-3.81	-9.67	-3.78	-7.26	111.66%	92.06%	
Net Profit	6.73	8.01	13.34	12.82	16.31	142.35%	27.22%	
As a % of Sales	24.69%	23.39%	25.32%	23.36%	25.33%			
Equity	29.2	29.2	29.2	29.2	29.2	0.00%	0.00%	
EPS (Rs)	2.31	2.74	4.57	4.39	5.59	141.99%	27.33%	
CEPS (Rs)	3.44	3.95	6.07	7.54	7.93			
OPM %	58.58	55.75	59.69	55.61	57.42			
NPM %	24.7	23.4	25.31	23.35	25.33			

Income Statement (Consolidated)

Y/E Mar (Rs mn)	FY 13A	FY 14A	FY 15A	FY 16A	FY 17P	FY 18P	FY 19P
Net Sales	653	908	1,013	1,691	2,199	2,749	3,298
Other Operating Income	18	12	13	-	37	39	47
Expenditure	293	387	463	729	965	1,233	1,580
EBITDA	378	533	563	962	1,271	1,554	1,765
Depreciation	101	120	121	204	239	247	255
EBIT	277	413	441	758	1,032	1,307	1,511
Interest Expenses	64	85	108	150	217	259	318
PBT	213	327	334	608	815	1,048	1,193
Tax	91	127	121	207	275	353	403
Other Income	-	-	-	9	3	4	7
Extraordinary Items	-	-	-	-	-	-	-
Net Income Before Adjustment	122	200	212	410	544	699	797
Minority Int./Income from Assoc.	0	(0)	(0)	(0)	-	-	-
Adjusted PAT	122	200	212	410	544	699	797

Balance Sheet (Consolidated)

Y/E Mar (Rs mn)	FY 13A	FY 14A	FY 15A	FY 16A	FY 17P	FY 18P	FY 19P
Equity share capita	263	263	292	292	292	292	292
Reserves & surplus	1,457	1,582	1,903	2,285	2,697	3,300	3,988
Share Warrants	-	90	-	-	-	-	-
Misc Expenditure	-	-	-	-	-	-	-
Net worth	1,720	1,935	2,195	2,577	2,989	3,592	4,280
Minority Interest	0	0	0	3	0	0	0
Share Application Money	-	-	-	-	-	-	-
Loan Funds	731	839	737	1,865	1,863	1,861	1,859
Net deferred tax liability	173	235	290	369	369	369	369
Other Long-term Liabilities	1	15	16	15	35	44	52
Long-term Provisions	-	-	-	-	-	-	-
Total Liabilities	2,627	3,026	3,241	4,829	5,258	5,868	6,562
Net block	2,472	2,893	3,209	4,984	4,732	4,906	5,073
Investment, Loan & Adv.	52	35	41	6	89	108	131
Total Current Assets	478	658	590	1,356	2,087	2,745	3,588
Current Liabilities & Provisions	377	561	601	1,518	1,652	1,893	2,232
Net Current Assets	101	97	(11)	(162)	435	852	1,355
Total Assets	2,627	3,026	3,241	4,829	5,258	5,868	6,562

Cash Flow (Consolidated)

Y/E Mar (Rs mn)	FY 16A	FY 17P	FY 18P	FY 19P
Operating Cash Flow	750	1,214	920	1,203
Cash Flow from Investments	(2,035)	(68)	(440)	(445)
Cash Flow from Financing	1,346	(174)	(116)	(196)
Net Changes in Cash	61	971	363	561
Opening Cash	-	171	1,143	1,506
Closing Cash Balance	61	1,143	1,506	2,067

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