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A STUDY ON FUNDAMENTAL ANALYSIS OF ONGC

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ABSTRACT

Fundamentals are associated with the economic health of a company. The fundamentals tell you about a company. We can say a company is having healthy fundamentals if it is growing at a nice pace, generating a profit, has limited debts and abundant cash. The analysis of a company's fundamentals involves getting deep into its financials, rather than day-to-day movement in its share price. Equity researchers normally do fundamental analysis in order to calculate the intrinsic value of a company's stock. If a company's stock is trading above the intrinsic value or fair value, then the stock is overvalued. If a company's stock is trading below the intrinsic value, then the stock is undervalued. However, if you watch the stock markets very closely, the share price of most companies never matches the fair value. Often, day traders and investors who would prefer short term investment options invest in those stocks, regardless of the companies' long term growth prospects. However, long term investors generally prefer to invest in companies with robust fundamentals and ignore near-term share price movements.

KEYWORDS: analysis, intrinsic value, stock market, share price.

INTRODUCTION

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OBJECTIVES

1. To study the economical factors which directly or indirectly affect on performance of ONGC.

2. To take an overview of industrial and company aspects of the company.

RESEARCH METHODOLOGY

The present is based on the secondary data sources which includes-

1. The annual report of ONGC for the year 2009-2010 to interpret the ratios of the company.

2. Books on portfolio management and financial management.

SCOPE AND LIMITATIONS OF THE STUDY

SCOPE

1) This study gives an overview on ONGC, which help to investors while investing.

2) This study consists of Economic-Industry-Company framework of analysis with the following aspects-

   a) Economic analysis consists of various variables such as inflation, interest rates, foreign exchange rates, infrastructure, monsoon, economic & political stability.

   b) Industry analysis consists of Demand, potential market, targeted Industrial growth.

   c) Company analysis consists of financial statement, analysis of financial statements, Companies prospects, growth, and Management board of company.

LIMITATIONS

1.For study only following limited variables has studied such as GDP, inflation rates, exchange rates, foreign exchange reserves, agriculture, industrial, service & allied sectors, currency markets, telecommunication sector & export growth.

2. The study is also limited only to competition, supply of raw materials and key business operations.

3. The study is restricted only to the financial statements and analysis of financial statements. For the purpose of interpretation, key ratios of the ONGC are studied for the period 2009-2010.

IMPORTANCE TO STUDY

This study provides a logical and systematic approach to estimate future profits. This study helps to know that the company's performance depends not only on its own efforts but also on the industry and economic factors.

This study helps an analyst to study the fundamental factors affecting the performance of different industries. Also industry analysis helps to evaluate the relative strength and weaknesses of particular company.

The financial statements of ONGC can be used to evaluate the financial performance of the company. Ratio analysis helps investors to determine the strength and weaknesses of the company. It also helps to him to assess whether the financial performance and financial strength are improving or deteriorating.

INTRODUCTION TO FUNDAMENTAL ANALYSIS

Fundamental analysis is based on the premise that every share has a certain intrinsic value at a period of time. This intrinsic value changes from time to time as a consequence of both internal and external factors. The theory of fundamental analysis submits that one should purchase a share when it is available below its intrinsic value and sell it when it rises above its intrinsic value. When the market value of share is below its intrinsic value it is under valued, whereas if the market value of a share is above its intrinsic value it is over valued. Fundamentalists thus seek to purchase underpriced shares and sell overpriced ones. They believe that although the market price may deviate from the intrinsic value in the short term, in the long term the market price will be equal to the intrinsic value.

STEPS IN FUNDAMENTAL ANALYSIS (EFFICIENT MARKET THEORY)

Fundamental analysts often use the efficient market theory in determining the intrinsic price of a share. This theory submits that in an efficient market all investors receive information instantly and that it is understood and analyzed by all the market players and is immediately reflected in the market prices. The market price, therefore, at every point in time represents the latest position at all times. The efficient market theory submits it is not possible to make profits looking at old data or by studying the patterns of previous price changes. It assumes that all foreseeable events have already been built into the current market price. The fundamental analysis is broken into three distinct parts:

1. the economy,

2. the industry within which the Company operates, and

3. The company.

The information has to be interpreted and analyzed and the intrinsic value of the share determined. This intrinsic value must, then, be compared against the market value the fundamentalists say, and only then can an investment decision be taken.

ECONOMIC ANALYSIS

Wise man once said, "No man is an island". No person can work and live in isolation. External forces are constantly influencing an individual's actions and affecting him. Similarly, no industry or company can exist in isolation. It may have splendid managers and a tremendous product. However, its sales and its costs are affected by factors, some of which are beyond its control - the world economy, price inflation, taxes and a host of others. It is important, therefore, to have an appreciation of the politico economic factors that affect an industry and a company.

THE POLITICAL EQUATION

A stable political environment is necessary for steady, balanced growth. If a country is ruled by a stable government which takes decisions for the long-term development of the country, industry and companies will prosper. There are certain issues which are to be considered on this particular ground-

Foreign Exchange Reserves

Inflation

(Interest Rates, Taxation, Government Policy, Domestic Savings and its Utilization, The Infrastructure)

The Economic CYCLE

The four stages of an economic cycle are:

Depression Recovery Boom Recession

THE INVESTMENT DECISION

Investors should attempt to determine the stage of the economic cycle the country is in. They should invest at the end of a depression when the economy begins to recover. Investors should disinvest either just before or during the boom, or, at the worst, just after the boom. Investment and disinvestments made at these times will earn the investor greater benefits. Joseph Schumpeter once said, "Cycles are not, like tonsils, separable things that might be treated by themselves but are, like the beat of the heart, of the essence of organism that displays them."

INDUSTRY ANALYSIS

The importance of industry analysis is now dawning on the Indian investor as never before. Previously, investors purchased shares of companies without concerning themselves about the industry it operated in. And they could get away with it three decades ago. This was because India was a sellers' market at that time and products produced were certain to be sold, often at a premium. All industries evolve through the following stages:

1. Entrepreneurial, sunrise or nascent stage
2. Expansion or growth stage
3. Stabilization, stagnation or maturity stage
4. Decline or sunset stage

COMPANY ANALYSIS

At the final stage of fundamental analysis, the investor analyzes the company. This analysis has two thrusts:

How has the company performed vis-à-vis other similar companies and

How has the company performed in comparison to earlier years.

Jean Paul Getty, one of the most successful stock market operators of all time, said, "Do not buy stock until you know all about it". The different issues regarding a company that should be examined are

The Company The Annual Report Ratios Cash flow

ABOUT ONGC (OIL AND NATURAL GAS CORPORATION LIMITED)

OIL AND NATURAL GAS CORPORATION LIMITED (**ONGC**)

(Incorporated on 23 June 1993) is a state-owned oil and gas company in India. It is a Fortune Global 500 companies ranked 152nd, and contributes 77% of India's crude oil production and 81% of India's natural gas production. It is the highest profit making corporation in India. It was set up as a commission on 14 August 1956. Indian government holds 74.14% equity stake in this company.

ONGC is one of Asia's largest and most active companies involved in exploration and production of oil. It is involved in exploring for and exploiting hydrocarbons in 26 sedimentary basins of India. It produces about 30% of India's crude oil requirement. It owns and operates more than 11,000 kilometers of pipelines in India. The liberalized economic policy, adopted by the Government of India in July 1991, sought to deregulate and de-license the core sectors (including petroleum sector) with partial disinvestments of government equity in Public Sector Undertakings and other measures. As a consequence thereof, ONGC was re-organized as a limited Company under the Company's Act, 1956 in February 1994. In the year 2002-03, after taking over MRPL from the A V Birla Group, ONGC diversified into the downstream sector. ONGC will soon be entering into the retailing business. ONGC has also entered the global field through its subsidiary, ONGC Videsh Ltd. (OVL). ONGC has made major investments in Vietnam, Sakhalin and Sudan and earned its first hydrocarbon revenue from its investment in Vietnam.

GLOBAL RANKING

• ONGC ranks as the Numero Uno Oil & Gas Exploration & Production (E&P) Company in the world, as per Platts 250 Global Energy Companies List for the year 2008 based on assets, revenues, profits and return on invested capital (ROIC).

• ONGC ranks 20th among the Global publicly-listed Energy companies as per ‘PFC Energy 50” (Jan 2008)

• ONGC is the only Company from India in the Fortune Magazine’s list of the World’s Most Admired Companies 2007.

ANALYSIS AND INTERPRETATION

ECONOMIC ANALYSIS

1. The economy of India is the eleventh largest economy in the world by nominal GDP.
2. The fourth largest by purchasing power parity (PPP).
3. India had established itself as the world's second-fastest growing major economy.
4. However, the year 2009 saw a significant slowdown in India's GDP growth rate to 6.8% as well as the return of a large projected fiscal deficit of 6.8% of GDP which would be among the highest in the world.
5. The fiscal year 2009-10 began as a difficult one. There was a significant slowdown in the growth rate in the second half of 2008-09, following the financial crisis that began in the industrialized nations in 2007 and spread to the real economy across the world. The growth rate of the gross domestic product (GDP) in 2008-09 was 6.7 per cent, with growth in the last two quarters hovering around 6 per cent.
6. The fiscal year 2009-10 has been a time of inflationary concerns. It was a year of a somewhat unusual inflation. While food inflation soared, inflation in the non-food sector was negligible. The Government was concerned that the upward pressure on prices should not escalate to all sectors.

POLITICAL ENVIRONMENT

The United Progressive Alliance (UPA) lead by the Indian National Congress (Congress) was re-elected to a second five year term in 2009. The UPA succeeded in gaining a stronger electoral mandate in 2009 and therefore has had to rely less on left leaning coalition partners in contrast to the coalition formed in 2004.

FOREIGN EXCHANGE RESERVES

Taking into account the valuation effect, India’s foreign exchange reserves recorded a decline of US $ 57.7 billion during 2008-09 to US $ 252.0 billion as at end-March 2009. Valuation loss arising out of depreciation of major currencies against the US dollar, at US$ 37.6 billion, accounted for 65.2 per cent of the total decline in foreign exchange reserves during 2008-09. However, in 2009-10 foreign exchange reserves recorded an increase of US$ 29.3 billion in H1 (April-September 2009) of which US$19.8 billion was on account of valuation gain.

INTEREST RATES

DOMESTIC DEPOSIT RATES

Deposit rates of SCBs softened during 2009-10. Interest rates offered by PSBs on deposits of maturity of one year to three years declined from the 8.00-9.25 per cent range in March 2009 to 6.00- 7.25 per cent in December 2009, while those on deposits of maturity of above three years came down from the 7.50 9.00 per cent range to the 6.25-7.75 per cent during the same period. The term deposit rates of private-sector banks and foreign banks on deposits of maturity of one year up to three years also declined from the 7.50-10.25 per cent and 2.50- 9.50 per cent range respectively in March 2009 to the 5.25-7.50 per cent and 2.25-7.75 per cent range in December 2009.

INFLATION

The first half of the financial year 2008-09 was marked by high wholesale price index (WPI)-based inflation, primarily due to the rise in global commodity and fuel prices. The subsequent global economic meltdown starting September 2008 reversed the trend and WPI inflation slipped into negative territory during June to August 2009. This was due to the decline in commodity prices globally and the base effect. As regards food inflation, the upswing noticed in the first quarter of 2008-09, continued during 2009-10 due to unfavorable south-west monsoon, the worst since 1972. Though the current specter of double-digit inflation in food articles is ascribable to supply-side constraints, it is necessary to ensure that the monetary policy stance does not lead to pressure.

INDUSTRY ANALYSIS

INDIAN OIL AND NATURAL GAS SECTOR

THE ORIGIN OF THE OIL INDUSTRY in India can be traced back to the last part of the 19th century when petroleum was discovered in Digboi in north-east India. After independence, the industry - which had Burmah Shell, Esso and Caltex as major players - was nationalized. Every activity - exploration, development, production, refining, marketing, distribution - was controlled by the various national oil companies. Since India’s economic liberalization program started, however, the Indian oil and gas sector has gone through some very fundamental changes.

FACTS

India is currently the fourth largest oil consumer in the Asia-Pacific region after Japan, China and South Korea. Estimated to increase at the rate of 7 % a year, the demand for petroleum products, in absolute terms, is expected to be 155 and 195 million tones respectively for the year 2006-07 and 2011-12. India is endowed with 26 sedimentary basins totaling around 1.72 million sq. km. of which offshore area amounts to 0.38 million sq. km. Most of the basins are under various stages of intensive/extensive exploration. The size of the Indian Oil & Industry is estimated to be US$ 90 Billion. The Oil & Gas sector is also one of the largest contributors to Central and State exchequer amounting to US$13.58 Bn. Apart from enhancing the domestic efforts in the sector Indian Companies are venturing overseas as well to give the country a sense of energy security and strategic positioning. In the upstream segment, we have OVL investing in

Sakhalin, Sudan, Myanmar, Vietnam, Libya, Syria, Iraq and Angola. Reliance has gone into Yemen. In the downstream, IOC has a presence in Sri Lanka and has expressed its interest in distribution in Singapore and Malaysia as well Middle East Markets. BPCL has also bid for retail outlets in Sri Lanka. GAIL is eyeing the Egyptian and UK markets also.

DE-REGULATION HISTORY

DE-REGULATION OF REFINERIES

Year 2000-01 FDI in refining sector raised from 49% to 100% Stand-alone refining companies aligned with existing integrated refining and marketing companies. In the Year 2002-02 ATF pricing decontrol was started. Oil Co-ordination Committee dismantled w.e.f. April 1, 2002. Dues of Oil companies under Oil Pool Accounts settled on provisional basis Majority of products made freely tradable Pricing of all products except LPG and Kerosene decontrolled

Pipeline transportation tariff decontrolled w.e.f. April 1, 2002.

In the Year 2003-04 Import of Gasoline, HSD and ATF allowed to companies having marketing rights Phased reduction in subsidies for LPG and Kerosene FDI in Marketing, E&P and Pipelines increased to 100% subject to certain approvals Marketing rights granted to private sector entities for marketing of transportation fuels through their own retail network.

REGULATORY OVERVIEW

GOVERNMENT POLICY

Market Determined Pricing Mechanism (MPDM) for most of the products w.e.f. April 1, 2002 except for LPG and Kerosene Refineries de-regulated w.e.f. April 1, 1998. The Oil Industry Pool Accounts dismantled w.e.f. April 1, 2002 Pipeline Transportation tariff decontrolled and based on commercial terms Private sector entities allowed marketing rights for transportation fuels subject to such entities investing Rs. 20 billion.

GROUND REALITIES

Despite Market Determined Pricing Mechanism (MDPM), prices still determined by Ministry of Oil & Natural Gas Subsidies on LPG and Kerosene shared by downstream companies (IOC, BPCL, HPCL), upstream companies (ONGC, GAIL) and fiscal budget

Subsidies on LPG and Kerosene slated to be completely phased out by March 2007

Marketing service obligations for rural and far flung areas for all the players Petroleum Regulatory Board to be set up by the Government

THE OPPORTUNITIES

The last 6-8 years have seen a radical restructuring of the Indian oil and gas sector. The recent initiatives enable private oil companies, both foreign and Indian, to explore new oil and natural gas reserves, develop proven reserves, and establish petroleum refineries and pipelines.

The Indian Government has earmarked US $ 12.91 Billion for Exploration & production and US $ 7.97 Billion for Downstream sector as per the Tenth Five year plan. As per the India Hydrocarbon Vision 2025, refining would have an investment of $ 50 Billion and the marketing infrastructure would involve and investment of US $ 29.34 Bn. The breakup for the marketing infrastructure is as follows:

Product Pipelines: US $ 4.56 Bn.

Product tankage and related facilities: US $ 3.47 Bn.

Retail outlets: US $ 20.2 Bn.

LPG Bottling Plants: US $ 1.08 Bn.

THE SIGNIFICANT FACTORS FUELING PRIVATE INVESTMENT IN THE INDIAN OIL AND NATURAL GAS SECTOR ARE

An investment is needed over the next 10 to 15 years to meet the projected early 21st century demand. With a view to meeting this growing demand, the new hydrocarbon policy aims at encouraging investment in oil and gas exploration and production. Additional refining capacity of 110 million tones per annum will be required in the near future. With such phenomenal growth in this sector, there is ample scope and opportunity for the transfer of technologies required and exports of capital goods, etc. to India. The technologies required will be for Upgrading, expansion, replacement and new refineries To meet the predominant demand for middle distillates and Also to improve the quality of petroleum products to make them environment friendly and globally competitive. Extensive oil and gas distribution infrastructure such as cross country pipelines, port terminals, tank ages and strategic reserves build up will have to be developed to meet the projected requirements. India is adopting more environmentally benign measures with regard to usage and quality of fuels. Lead phasing out and benzene reduction in gasoline, sulphur reduction and certain improvements of diesel are amongst the prominent measures that are under implementation. Such quality up gradation of fuels will call for adopting latest/state of the art technology requiring huge investments by way of providing reformulated gasoline producing units, hydro-crackers, hydro-theaters, hydro-desulphurisers, etc.

POLICY NEW INITIATIVES

The Indian petroleum sector has been opened to the private sector, both domestic and foreign for investments through joint ventures and strategic alliances. In exploration and production, Indian oil and natural gas fields have been opened up to the private sector as well as to foreign participation under production sharing contracts. The refining sector has been opened to the joint sector (public-private partnerships) as well as to the private sector for new refineries. Foreign investment is to be permitted up to 100% in exploration.

For petro product marketing, 100% FDI is permitted. All petro products taken out of the administered price mechanism from 1st April, 2002. All petroleum products, except MS, HSD, Kerosene, ATF and LPG have been decontrolled Sourcing and import of crude to joint and private sector refineries allowed under actual user licensing policy. The GoI has already tabled the Draft Petroleum and Natural Gas Board Bill in the Parliament, which proposes a Petroleum and Natural Gas regulator to regulate the downstream activities. A common Carrier Pipeline Policy allowing two or more companies to use a single pipeline for the transportation of products is also announced. At least 25% of the product carrying capacities of the pipeline will have to be shared with other interested companies by the parent pipeline laying company.

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