CRISIL RESEARCH

Independent Equity Research

Enhancing investment decision

Indepth analysis of the fundamentals and valuation

Dolphin Offshore Enterprises (India) Limited

CRISIL Independent Equity Research Team

Senior Director
S. Venkataraman

Analytical Contacts

Chetan Majithia	chetanmajithia@crisil.com	+91 (22) 6644 4148
Vishal Rampuria	vrampuria@crisil.com	+91 (22) 6691 3525
Sagar Parikh	sparikh@crisil.com	+91 (22) 6691 3502
Nihag Shah	ndshah@crisil.com	+91 (22) 6691 3533
Ravi Dodhia	rdodhia@crisil.com	+91 (22) 6691 3508
Sonali Salgaonkar	ssalgaonkar@crisil.com	+91 (22) 6691 3597
Sudnya Goel	sgoel@crisil.com	+91 (22) 6644 1983
Neeta Khilnani	nkhilnani@crisil.com	+91 (22) 6644 1882

Sector Contacts

Nagarajan Narasimhan	nnarasimhan@crisil.com	+91 (22) 6691 3536
Ajay D'Souza	adsouza@crisil.com	+91 (22) 6691 3567
Manoj Mohta	mmohta@crisil.com	+91 (22) 6691 3554
Sachin Mathur	smathur@crisil.com	+91 (22) 6691 3541
Sridhar C	SridharC@crisil.com	+91 (22) 6691 3546
Sudhir Nair	snair@crisil.com	+91 (22) 6691 3526

Business Development Contacts

Vishal Thakkar	tvishal@crisil.com	+91 98 201 86264
Vinaya Dongre	vdongre@crisil.com	+91 99 202 25174
Sagar Sawarkar	ssawarkar@crisil.com	+91 98 216 38322
Sejal Kothari	sakothari@crisil.com	+91 99 206 25746
Gayathri S	gayathris@crisil.com	+91 98 864 98175

CRISIL's Equity Offerings

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- IPO Grading
- White Labelled Research
- Valuation on companies for use of Institutional Investors, Asset Managers, Corporates

Other Services by the Research group include:

- CRISINFAC Industry research on over 60 industries and Economic Analysis
- Customised Research on Market sizing, Demand modelling and Entry strategies
- Customised research content for Information Memorandum and Offer documents

Explanation of CRISIL Fundamental and Valuation (CFV) matrix

The **CFV Matrix (CRISIL Fundamental and Valuation Matrix)** addresses the two important analysis of an investment making process – Analysis of Fundamentals (addressed through Fundamental Grade) and Analysis of Returns (Valuation Grade)

Fundamental Grade

CRISIL's Fundamental Grade represents an overall assessment of the fundamentals of the company graded in relation to other listed equity securities in India. The grade facilitates easy comparison of fundamentals between companies, irrespective of the size or the industry they operate in. The grading factors in the following:

- Business Prospects: Business prospects factor in industry prospects and company's future financial performance
- Management Evaluation: Factors such as track record of the management, strategy are taken into consideration
- Corporate Governance: Assessment of adequacy of corporate governance structure and disclosure norms

The grade is assigned on a five-point scale from grade 5 (indicating Excellent fundamentals) to grade 1 (Poor fundamentals)

CRISIL Fundamental Grade	Assessment
5/5	Excellent fundamentals
4/5	Superior fundamentals
3/5	Good fundamentals
2/5	Moderate fundamentals
1/5	Poor fundamentals

Valuation Grade

CRISIL's Valuation Grade represents an assessment of the potential value in the company stock for an equity investor over a 12-month period. The grade is assigned on a five-point scale from grade 5 (indicating strong upside from the current market price (CMP)) to grade 1 (strong downside from the CMP).

CRISIL Valuation Grade	Assessment
5/5	Strong upside (>25% from CMP)
4/5	Upside (10-25% from CMP)
3/5	Align (+-10% from CMP)
2/5	Downside (negative 10-25% from CMP)
1/5	Strong downside (<-25% from CMP)

Independent Research Report – Dolphin Offshore Ltd

'Good fundamentals and potential Upside'

Industry: Oil and Gas allied services
Date: September 22, 2009

CRISIL RESEARCH

Under-invested oil and gas industry provides strong prospects

The oil and gas industry provides a huge potential, as the Indian government is keen on energy security and the state-run Oil and Natural Gas Corporation (ONGC)'s planned capex of around Rs 800 Bn for the eleventh five-year plan is on target. Of this capex, around Rs 120-150 Bn is expected to be spent on oil-field services.

Grew from a diving and underwater services sub-contractor into an engineering, procurement and construction (EPC) contractor

Dolphin Offshore's competitive edge is its ability to offer underwater, on-water and above-water services. It has grown from a diving and underwater business to an EPC sub-contractor and now into a main EPC contractor, enabling it to bid for high-ticket projects.

Potential risk from inadequate client and geographic diversification

Earlier, Dolphin's business was from main EPC contractors or turnkey solution providers of ONGC projects. But now, with main contractor status, it bids directly for these projects. Its operations business (spanning diving, marine and fabrication) predominantly deals with ONGC, its key client. The main business area is on the country's west coast, with plans to enter other geographies.

Revenues to register a CAGR of 23%; margins to be maintained

The company's revenue comes from its diving, marine and fabrication business and from its EPC project business. With investments expected in the Bombay High region and shallow waters, we expect Dolphin's top line to post a CAGR of 23%, at Rs 6,608 Mn in FY12E from Rs 3,530 Mn FY09; and EBITDA margin of 18.4% from 19.1%; PAT margin of 7% down from 8.6%; adjusted RoE and EPS of 27% down from 47% and to Rs 27.5 from Rs 31.9, respectively.

High debtor days put pressure on working capital

The debtor days peaked to 266 days in FY08 due to issues such as change work orders from ONGC, resulting in increasing disputable amount. This has largely stressed the working capital. As the company wrote off Rs 398 Mn as bad debts in FY09, debtor days came down to 186 days. Going ahead, the debtor days are expected to be at around 150 days.

We assign Dolphin Offshore Ltd fundamental and valuation grades of 3/5 and 4/5, respectively

Dolphin's fundamental grade of **'3/5'** indicates its fundamentals are **'Good'** relative to other listed securities in India. This grading factors its well-experienced management and integrated services. However, it is tempered by the risk of client/geographic concentration and issues with working capital management. A valuation grade of **'4/5'** indicates **'Potential Upside'** (at Rs 315) to the current market price.

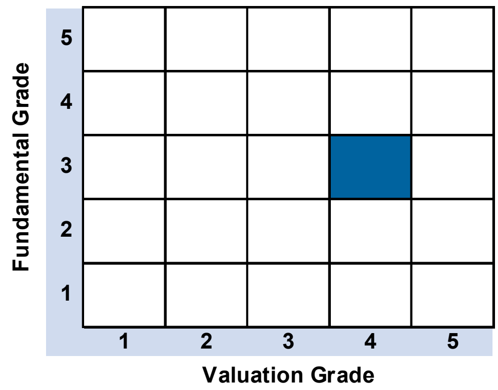
Key forecast (consolidated)

Rs (Mn)	FY08	FY09	FY10E	FY11E	FY12E
Sales	2,340	3,530	4,913	5,986	6,608
EBITDA	367	674	856	1,128	1,216
Net income	193	305	387	469	461
EPS*-Rs	20.2	31.9	26.9	28.0	27.5
EPS growth (%)	2%	58%	-16%	4%	-2%
BV per share (Rs)	67.3	110.1	88.2	102.0	105.8
PE (x)	13.0	8.2	9.7	9.4	9.5
P/BV (x)	3.9	2.4	3.0	2.6	2.5
RoCE (%)	18.4	21.1	24.0	24.5	23.2
RoE (%)	50.1	47.4	36.7	37.0	27.0

*Adjusted for FX losses and gains

Source: Company, CRISIL Equities Estimate

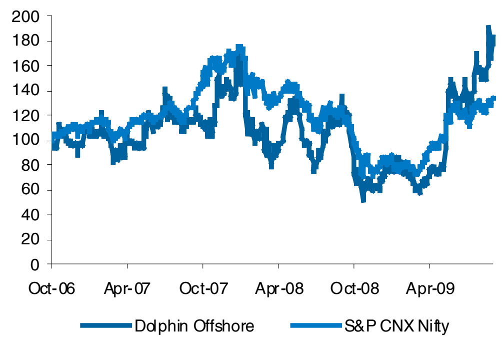
CFV matrix



Key stock statistics

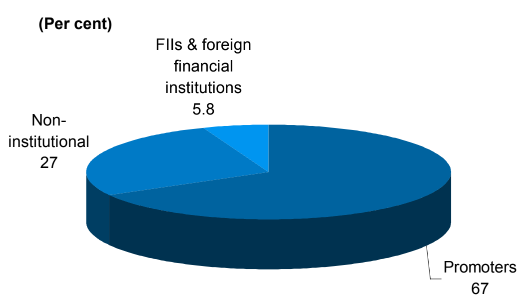
Fundamental Value (Rs per share)	315
Current Market Price (Rs per share)	262
Shares outstanding (Mn)	13.4
Market cap (Rs Mn)	3,506
Enterprise value (Rs Mn)	4,223
52 week range (Rs) (H/L)	313/103
P/E on EPS estimate (FY10E)	9.7
Beta	1.2
Free float (%)	32.9
Average daily volumes	20,390

Share price movement



- Indexed to 100

Shareholding as on June '09



Analytical contact

Chetan Majithia (Head, Equities) +91 22 66444148
Sudhir Nair (Head, Research) +91 22 66913526
Savio Monteiro +91 22 66444150

Email: clientservicing@crisil.com +91 22 66913561

Fundamental Grading — Grade: 3/5

Fundamentals are 'Good' relative to other listed securities in India

Dolphin's fundamental grade of **'3/5'** indicates its fundamentals are **'Good'** relative to other listed securities in India. This grade factors in the following aspects:

- The oil and gas industry's full potential is yet to be tapped—only 44% of the sedimentary basins are under exploration. Over the next few years, the exploration and development activities are expected to enormously grow. Energy security is primarily on the Indian government agenda, with its flagship ONGC's planned capex of around Rs 800 Bn for the eleventh five-year plan being on target (ONGC's capex for FY08 and FY09 stood at Rs 395 Bn as against planned capex of Rs 363 Bn). Of this, around Rs 300 Bn is to be spent on oil field equipment and services. This would translate into an investment potential of Rs 120-150 Bn for the oilfield services segment.
- Dolphin's key competitive strength is its ability to offer services under water (divers, diving equipments etc), on water (ship and rig repairs, offshore support vessels ("OSV") support, etc) and above water (fabrication, installation, etc). It has a domestic market share of 9%, but in its niche business, it is one of the largest players.
- The company has grown from an EPC sub-contractor to a main contractor. A large share of its revenues is from turnkey/EPC projects. These projects have a greater share of milestone- and project completion-based revenues, compared with daily charges from chartering diving equipments and OSV.
- Its subsidiary Dolphin Offshore Enterprises (Mauritius) Ltd is commissioning two boats (Beas Dolphin and Betwa Dolphin) and a construction barge (Vikrant Dolphin), which is expected to increase chartering revenues.
- Dolphin faces risk from client concentration, as its main customer is ONGC, either directly through EPC contracts or indirectly through operations (diving and marine services) for ONGC projects. It has high debtor days, mainly due to disputed balance amounts with ONGC from change works (work arising in between execution of the project which is not budgeted for) within a contract. This is straining the working capital of the company.
- The company also has geographic concentration risk, as most projects and operations are on the west coast at Bombay High. Dolphin plans to enter the Middle East market to diversify the seasonality risk (typically from June to December).
- The company has a strong order book of around Rs 6 Bn, providing revenue visibility of more than 1.5 times its FY09 sales.
- Overall, we expect the company to post a 23% CAGR over FY09–12 in turnover, due to high-ticket EPC projects. We expect the EBITDA margin to be maintained as it would be competitively bidding for projects. We also expect the PAT growth to come down over the next few years due to increasing depreciation and interest rates from the shipyard and fabrication unit, planned to be set up in Gujarat over the next 2-3 years. This would result in RoE dropping to 27% in FY12E from 47% in FY09; and EPS to Rs 27.5 from Rs 31.9.

- Dolphin's management brings to the board vast technical experience in oilfield services, with most of the top management being with the company since inception. However, a strong second-line management is yet to be put in place.

- It has a well-diversified board with members experienced in diverse fields. Disclosure is good and meets the minimum requirements. The company has eminent names as independent directors such as Dr. F.C. Kohli, S. Venkiteswaran, S Sundar, Bipin Shah and Arvind Parikh (please refer to the corporate governance section for their eminence).

Grading Rationale

Huge investments in the oil & gas industry to boost Dolphin's revenues

ONGC expects to spend around Rs 300 Bn on oilfield equipment and services in the eleventh plan (FY08-12)

The oil and gas industry's full potential is yet to be tapped—only 44% of the sedimentary basins are under exploration. Over the next few years, the exploration and development activities are expected to enormously grow with the New Exploration and Licensing Policy (NELP) projects being handed over to private players and joint ventures. Also, energy security is primarily on the Indian government agenda, with its flagship ONGC's planned capex of over Rs 800 Bn for the eleventh five-year plan (FY08 to FY12) being on target.

Chart 1: ONGC domestic capital expenditure plan

Rs Bn	FY08A	FY09E	FY10E	FY11E	FY12E
Total outlay	176.51	218.49	208.68	123.60	109.67
Oilfield equipments and services	64.46	67.41	88.17	46.59	41.34

Source: Company reports

Of this, around Rs 300 Bn is to be spent on oilfield equipment and services, typically in shallow water through revamping/project extensions. This would translate into an investment potential of Rs 120-150 Bn for the oilfield services segment, which is Dolphin's main business area.

Integrated services and main EPC contractor status

Dolphin has been awarded main EPC contractor status

Dolphin's key strength is its ability to offer services under water (diving services etc), on water (ship and rig repairs, OSV support etc) and above water (fabrication, installation etc), which gives the company an edge over its competitors. Although Dolphin's share in the domestic oilfield equipment and services is around 9%, in the niche area where it operates, Dolphin is one of the largest players.

Dolphin Offshore was awarded main/independent EPC contractor status in FY09 with ONGC's 2 projects (NQD replacement and ICP revamp project) having a combined value of Rs 3.02 Bn, expected to be executed over 18 months. The project mainly involves design engineering, procurement, fabrication, marine loadout and offshore hook-up and commissioning activities.

Prior to achieving the main contractor status, Dolphin was a sub-contractor to the turnkey/ main EPC players executing ONGC projects. Dolphin continues to be a sub-contractor, chartering the diving and marine vessels to various contractors like L&T, Punj Lloyd, Leighton, OSW etc. The EPC projects have resulted in steady growth in turnover, while the chartering of vessels/diving equipments has resulted in steady margins growth..

Advantages of a main contractor status with ONGC:

- Dolphin will be able to bid for high-ticket projects, increasing the turnover of the company.
- The company can now directly negotiate with ONGC over issues related to change works etc.
- Higher bargaining power with sub-contractors and equipment providers

The company has completed a number of projects over the last 30 years, ranging from diving and underwater services to EPC-related projects. The key projects are mentioned in the table below.

Table 1: List of projects executed/under execution

Year	Project	Company	Main contractor	Project cost (Rs million)	Scope of the job
1991	Underwater rack teeth repairs of Sagar Kiran	ONGC	Mazagon Docks	22.8	Towing this rig to the port, cleaning the spudcan, cutting away damaged parts and, after replacement, returning the rig offshore.
1991	Replacement of leg section of Sagar Jyoti	ONGC	Mazagon Docks	155.4	Towing this rig to the port, removing the damaged lower leg sections, replacing them, refitting the top leg section and returning the rig offshore.
1997	Repairs to spudcans of Sagar Ratna	ONGC	Cochin Shipyard Ltd	92.7	Repair of cracks and plating renewal work on the spudcan of the rig.
2004	Redevelopment of south pipelines and platform modifications (RSPPM)	ONGC	Iranian Offshore Engineering	2000*	This engineering, procurement and construction (EPC) job entailed jacket faces, pre-engineering surveys, fabrication and installation of riser clamps, installation of risers, correction of crossovers and free spans etc. A major portion of fabrication and installation work was subcontracted to Dolphin.
2005	Barge bumper boat landing and riser protector (BBBLRP)	ONGC	Naftogaz	1300*	The work involved pre–engineering, engineering, procurement, fabrication, loadout, transportation and installation.
2007	Clamp on	ONGC	L&T and Dolphin	1140.8 (621.7)	Modification of existing facilities in order to enhance production of crude oil.
2008	Offshore subsea works	OSW (Malaysia)	-	750*	Diving assistance in the oil & gas region of Malaysia
2008	NQD replacement and ICP revamp project	ONGC	Dolphin	3025.9	Design engineering, procurement, fabrication, marine loadout and offshore hook-up and commissioning activities

Note: * Dollars converted into rupees at a rate of Rs 45

Source: Company report

The current order-book size of the company stands at Rs 6.2 Bn, which provides a visibility of over 1.5 times the FY09 revenues. We expect the order book to see strong growth potential on the back of increased investments in the oil and gas sector. ONGC is the main client for Dolphin, with direct orders of 40-50 per cent and major part of the rest on sub-contracting basis. CRISIL Equities estimates the order book to grow to Rs 8.5 Bn by FY12 from the current order-book size.

Plans to set up fabrication unit and shipyard to strengthen its above-water business

Dolphin plans to set up a fabrication unit and shipyard with a capex of Rs 4.5 Bn

Dolphin is constructing 3 vessels (2 workboats and 1 construction barge), which are expected to be ready this year at a cost of approx Rs 500 mn. With the construction of these vessels, the company would augment its marine operations business. These vessels would be used either for the EPC operations or for chartering purpose, boosting the revenues of the company.

It is also planning to set up a fabrication unit and a shipyard at Jafrabad in Gujarat at a capex of Rs 4.5 Bn (Rs 1.5 Bn for fabrication unit and Rs 3 Bn for shipyard), to be funded through a mix of debt and internal accruals. This would result in the company strengthening its above-water services. These plans also fall in line with the integrated service strategy by the company.

Potential risk due to inadequate client and geographic diversification

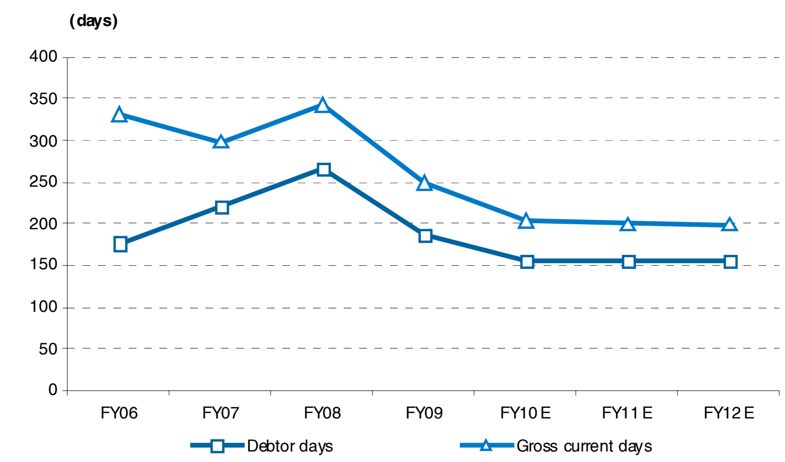
Dolphin operates in shallow water. Under the NELP, a number of new projects that are being bid are in deep water area where Dolphin has yet to enter. In the shallow water regions, a few players operate besides ONGC. However, Dolphin's main client is ONGC, either directly through EPC contracts or indirectly through diving and marine services to main contractors for ONGC projects; hence, the company faces risk from client concentration. Dolphin does not plan to diversify its client base to private players in the near future. This can pose a potential risk and affect its revenues in case of issues/ blacklisting with ONGC.

Dolphin's major operations are on the west coast in the Bombay High region. Though the company has assets deployed in the Middle East, China and Vietnam; it has yet to gain any significant presence abroad. It is planning to increase its presence in the Middle East. However, till then, the company faces seasonal risk, typically from June to December.

High debtor days putting pressure on working capital

The debtor days increased from 175 days in FY06 to a high of 266 days in FY08, mainly due to disputed balance amounts with ONGC from change works within a contract resulting in debtor days over six months increasing significantly. This is straining the working capital of the company.

Chart 2: Trend in debtor days and gross working capital days



Source: Company, CRISIL Equities Estimate

The company, in FY09, has written off Rs 398 Mn as bad debts occurring from these change orders. This has resulted in the debtor days slipping to around 186 days in FY09. We expect a further write-off in FY10 for other disputed amounts and hence, expect the debtor days to settle at around 150 days over the next 2-3 years. Also, after achieving the status of a main EPC contractor, it can negotiate directly with ONGC, which would help the debtor days to come down.

Financial Outlook

Revenues to grow by 23.2% CAGR over FY09 to FY12

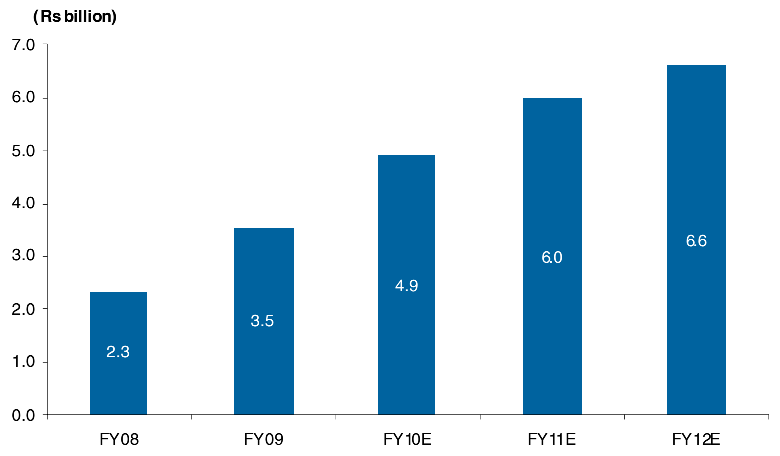
EPC projects and higher charter rates have helped revenues post a CAGR of 28.8% during FY06-09

During FY06 to FY09, sales grew at a CAGR of 28.8% to Rs 3.5 Bn. Being awarded the status of main contractor, Dolphin can now bid for high-ticket projects, either independently or in a consortium. Also, revenues rose on account of the growing charter rates over the last 2-3 years.

ONGC's huge capex plans for revamp/expansion of shallow water wells would result in a strong and continued opportunity for Dolphin. The company has a strong order book of around Rs 6 Bn, providing revenue visibility of more than 1.5 times its FY09 sales. Going ahead, we expect the order book to grow to Rs 8.5 Bn by FY12, from the current size of Rs 6.2 Bn, on the back of steady orders from ONGC. Hence, we forecast the topline to grow at a CAGR of 23.2 % to Rs 6.6 Bn during FY09 to FY12.

Revenues to grow at a CAGR of 23% from FY09-12

Chart 3: Sales forecast



Source: Company, CRISIL Equities Estimate

EBITDA margins to remain stable over next 2-3 years

Dolphin's EBITDA margins had grown from 12% in FY05 to 19% in FY09, on account of increasing investments in the oil and gas sector and also rising charter rates. We expect the EBITDA margins to decrease in FY10 to 17.4%, on account of falling charter rates, and stablise at 18.4% by FY12.

Capital expenditure to put presure on interest and depreciation rates

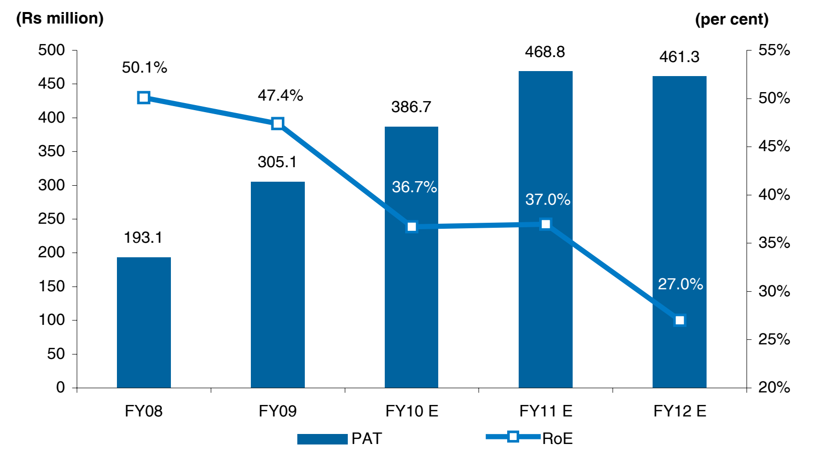
Dolphin is planning to set up a fabrication unit and shipyard with a capex of around Rs 4.5 Bn (Rs 1.5 Bn for fabrication unit and Rs 3 Bn for shipyard). This is expected to increase the interest and depreciation costs from Rs 146 Mn in FY09 to Rs 235 Mn by FY12 and from Rs 74.5 Mn in FY09 to Rs 283 Mn by FY12, respectively. The 3 new vessels are expected to be completed in FY10 would also increase depreciation costs.

PAT to grow at steady rate; RoE to drop significantly to 27% in FY12 from 47% in FY09

Dolphin's adjusted PAT (reported PAT adjusted for forex gains and losses and extraordinary gains and losses) has grown at 56% CAGR from FY06 to FY09. This has main been due to higher chartering costs, and the main contractor status. We forecast the bottomline to grow at a 15% CAGR to Rs 461 Mn over the next three years.

The company is constructing 3 vessels (2 workboats and 1 construction barge) in FY10 at a cost of approx Rs 500 Mn. It also plans to set up a fabrication unit and shipyard over the next few years. These moves may see the adjusted RoE to dip to 27% in FY12 from 47.4% in FY09. However, post this, we expect the RoE to grow.

Chart 5: RoE and PAT trends



Source: Company, CRISIL Equities Estimate

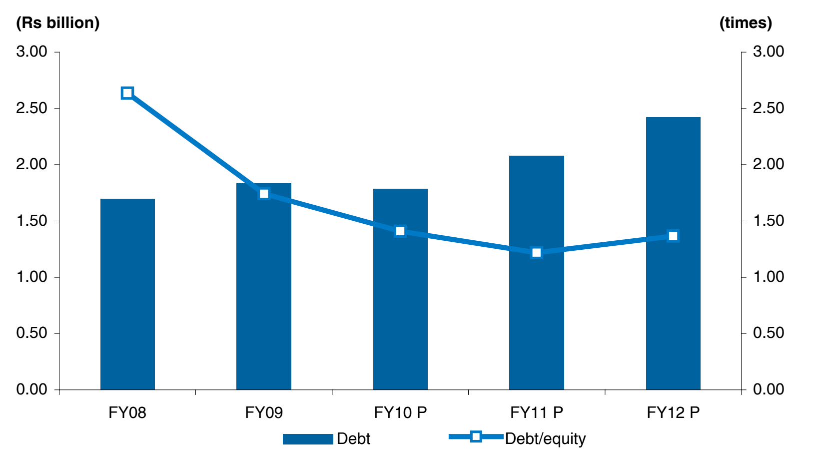
FCCB conversion to improve debt-to-equity ratio

FCCB conversion would reduce the debt-to-equity ratio to 1.4 times by FY12

Dolphin has around $12 Mn as FCCBs (issued around $15 Mn and $3 Mn have already been converted) as of FY09. Around $3.5 Mn has been converted in FY10 at a price of Rs 161, and the balance $8.5 Mn is expected to be converted in FY11. This conversion is expected to bring down the debt-to-equity ratio to 1.4 times by FY12.

The company plans to set up a fabrication unit and a shipyard in the next 3-4 years, and is expected to fund the same through debt and internal accruals. We estimate a 50% funding through debt resulting in the gearing levels rising by FY12.

Chart 4: Debt/equity trends



Source: Company reports, CRISIL Equities Estimate

Corporate Governance

Fairly good corporate governance practices

CRISIL Research's fundamental grading methodology includes a broad assessment of corporate governance and management quality, apart from other key factors such as industry and business prospects, and financial performance. In this context, CRISIL Research analyses shareholding structure, board composition, typical board processes, disclosure standards and related-party transactions. Any qualifications by regulators or auditors also serve as useful inputs, while assessing corporate governance.

Dolphin's board has a fair mix of directors experienced in various fields of business. Its processes and structures broadly conform to the minimum standards. CRISIL Research has assessed the company's disclosure levels, based on balance sheet disclosures, website information, etc, and is of the opinion that its corporate governance conforms to minimum disclosure requirements.

Board composition

Dolphin's board comprises 10 members, with six independent/non-executive directors, which is well above SEBI's minimum stipulated listing guidelines. It includes non-full time directors, who have sector as well as diversified technical, business and administrative experience. The board is represented by eminent people such as Dr. F C Kohli, former deputy chairman of TCS; S. Venkiteshwaran, a lawyer who has been associated with several international shipping litigations and arbitrations; S Sundar, an Indian Administrative Service officer and NTPC Chair professor in the regulatory studies at TERI university; Arvind Parikh, former director at Shell; and Bipin Shah, a chartered accountant who has held important positions in Hindustan Unilever Ltd.

Board processes

These appear to be well-structured, with audit, managing, remuneration, shareholder/investors grievance committees in place, supporting a good corporate governance and decision-making framework.

The audit committee is chaired by independent director S. Sundar. Further, the position of chairman is independent from that of the managing director/CEO.

Relatively good standards of disclosures and transparency

The company's quality of disclosure and transparency in reporting can be considered as good, judged by the level of information and details furnished in annual reports, website and other publicly available information. As per the auditors (Haribhakti & Co), the company disclosures are all in place.

Management Evaluation

We grade Dolphin's management as good

CRISIL's Fundamental Grading methodology includes a broad assessment of management quality, apart from other key factors such as industry and business prospects, and financial performance. Overall, we believe the management is fairly good.

Well-experienced management at the helm

Dolphin's management, led till the FY08 by Rear Admiral Kripal Singh, brings to the table sound business knowledge as well as long years of relevant experience. Currently headed by Satpal Singh (Managing Director) and Navpreet Singh (Joint Managing Director), Dolphin has grown from a Rs 0.7 Bn company in FY02 to a Rs 3.5 Bn company in FY09.

Slow scale-up into the bigger league

Operating for more than three decades now, Dolphin has been in a small niche space as a subcontractor. Much of the growth in revenues has been witnessed since FY05 onwards. It has only been in the past few years that Dolphin scaled up from low end of the value chain. For instance, Dolphin moved up from a sub-contractor to a main contractor only in FY08 after several years of service.

Dolphin's risk appetite has been low over the last few years, but lately top-line growth and new projects are being keenly focused upon. Its major risk stems from client/geographic concentration. ONGC is the major client and Dolphin does not have any plans to shift towards private players in the medium term. Predominantly operating in the west coast of the country, Dolphin is yet to move into other geographies.

Reasonable second-line management yet to evolve

Based on our interactions with the management, we believe that there are reasonably experienced people. The longevity of the management within the company has also been high. However, the second-level management is yet to be put in place. Given the significant growth the management is expecting over the next few years, the lack of a reasonably strong second-line management could act as a constraint.

Valuation Grading Grade:4/5

We expect an adjusted EPS of Rs 26.9 and Rs 28 in FY10 and FY11

Dolphin posted an adjusted EPS of Rs 31.9 in FY09. The company issued bonus shares in the ratio of 2:5 in the second quarter of FY10. On the expanded equity base, we expect the company to post an EPS of Rs 26.9 and Rs 28 in FY10 and FY11, respectively. It has outstanding FCCBs of $12 Mn (issued $15 Mn, 20% of which has been already converted in FY08) at a conversion price of Rs 161. This conversion is due by December 2010. In FY10, the company has converted another $3.5 Mn so far. Given that the stock is currently trading at above its issue price, FCCBs will be converted into equity shares.

We have used the discounted cash flow (DCF) approach to value Dolphin Offshore. Based on our approach, we have fundamentally valued the company at Rs 315 per share. Consequently, we initiate coverage on Dolphin with a valuation grade of **'4/5',** indicating a '**Potential Upside**'.

Key components of our valuations

We have considered discounted value of the firm's estimated free cash flow from FY10E to FY14E.

Table 2: WACC Calculation

Risk-free rate of return	7.0
Beta	1.2
Equity risk premium	6.0
Cost of equity	**13.0**
Cost of debt (post-tax)	**8.4**
WACC	**10.5**
Terminal growth rate	3.0

Source: CRISIL Equities

Our price objective of Rs 315 is derived by assuming a terminal growth rate of 3% and an equity risk premium of 6%.

Table 3: Sensitivity analysis

Terminal growth rate	WACC 9.5%	10.0%	10.5%	11.0%	11.5%
2.0%	327	297	270	246	225
2.5%	355	321	291	264	241
3.0%	388	349	**315**	285	259
3.5%	426	380	342	308	279
4.0%	470	418	373	335	302

Source: CRISIL Equities

Equity risk premium	BETA 1.0	1.1	1.2	1.3	1.4
5.0%	372	358	344	331	319
5.5%	358	343	329	316	303
6.0%	344	329	**315**	301	288
6.5%	331	316	301	287	274
7.0%	319	303	288	274	261

Source: CRISIL Equities

Peer comparison

Companies	Market cap (Rs million)	Revenues (Rs million) FY09	Revenues (Rs million) FY10	Revenues (Rs million) FY11	Net profit (Rs million) FY09	Net profit (Rs million) FY10	Net profit (Rs million) FY11	Adjusted EPS (Rs) FY09	Adjusted EPS (Rs) FY10	Adjusted EPS (Rs) FY11	Price / earnings (x) FY09	Price / earnings (x) FY10E	Price / earnings (x) FY11E
Dolphin Offshore	3,506	3,530	4,913	5,986	441.7	386.7	468.8	31.9	26.9	28.0	8.2	9.7	9.5
Consensus estimates													
Great Offshore	20,985	9,859	12,375	13,654	1,885	2,356	2,627	48.1	60.2	69.2	11.8	9.4	8.1
Garware Offshore	3,978	1,745	2,587	3,038	450	778	917	18.9	32.7	38.5	8.8	5.1	4.3

Note: Great Offshore and Garware Offshore are peers for the diving and marine business of Dolphin;

Source: CRISIL Equities Estimate, Bloomberg

Company Overview

Incorporated in 1979, Dolphin Offshore Ltd has emerged as a key player in the oilfield equipment and services segment of the oil industry, carving a niche in the field of support services. Dolphin provides diving and underwater services, marine operations and management services, turnkey marine construction services, fabrication services and ship-repair services, besides inspection, maintenance and modifications of offshore vessels.

It has presence in Saudi Arabia, Qatar, Kuwait, UAE, China, Vietnam and Iran through joint ventures and agency agreements via chartering services. It is planning to further increase its presence in the Middle East.

The company's revenues are expected to grow significantly in FY10, as it would receive deliveries of two workboats and a barge by the end of 2009. The increasing number of offshore vessels and higher number of ageing vessels will ensure that the demand for the company's services remains steady in the near term. However, the major share of its revenues is likely to come from the EPC projects, in which it has achieved the status of main EPC contractor, from a sub-contractor status.

Table 5: Timeline of growth

Year	Milestone
1979	Dolphin Offshore Enterprises (India) Ltd was incorporated as a private limited company.
1994	The company floated its IPO and became a full-fledged public limited company.
1995	Dolphin agreed to set up a joint venture with Sembawang Maritime Ltd to provide marine transportation and offshore logistic services.
2004	The company acquired Brahmaputra Dolphin.
2005	Dolphin expanded its reach to the Middle East by setting up agencies in Qatar, Abu Dhabi, Kuwait and Iran.
2006	The company acquired Procyon Offshore Services Pvt Ltd for Rs 145 Mn for its marine operations and management. This was a strategic move to gain tax benefits applicable to the shipping industry.
2006	The company signed a memorandum of understanding with IMPaC Offshore engineering, GmbH of Germany to set up a joint venture company to provide design, engineering services and business process outsourcing services for engineering work in India, Middle East and South East Asia.
2008	Two vessels owned by the company, namely Brahmaputra Dolphin and Ganga Dolphin were transferred to its wholly owned subsidiary Procyon Offshore Services Ltd, which would be solely responsible for all marine activities for the company.
2009	Beas Dolphin, a workboat has been constructed, and 2 other vessels namely, Betwa Dolphin (a workboat) and Vikrant Dolphin (a barge) are currently under construction are expected to be ready.

Source: Company reports

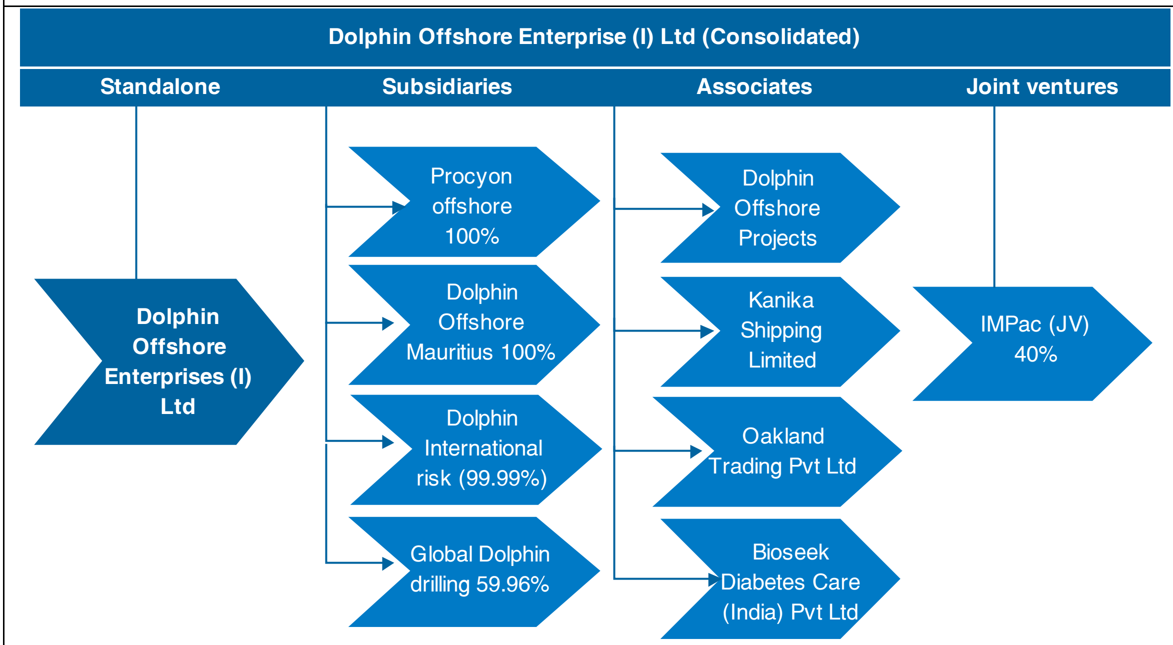
Business Overview

The company has four subsidiaries and one joint venture. In 2008-09, its standalone revenues accounted for 97.5 per cent of its consolidated revenues.

Dolphin Offshore acquired Procyon Offshore Services Ltd in 2006. This company provides marine operations and management services. The move was more to avail the benefits of taxation provided in the shipping industry. Currently, Procyon Offshore Services Ltd manages all vessels of Dolphin.

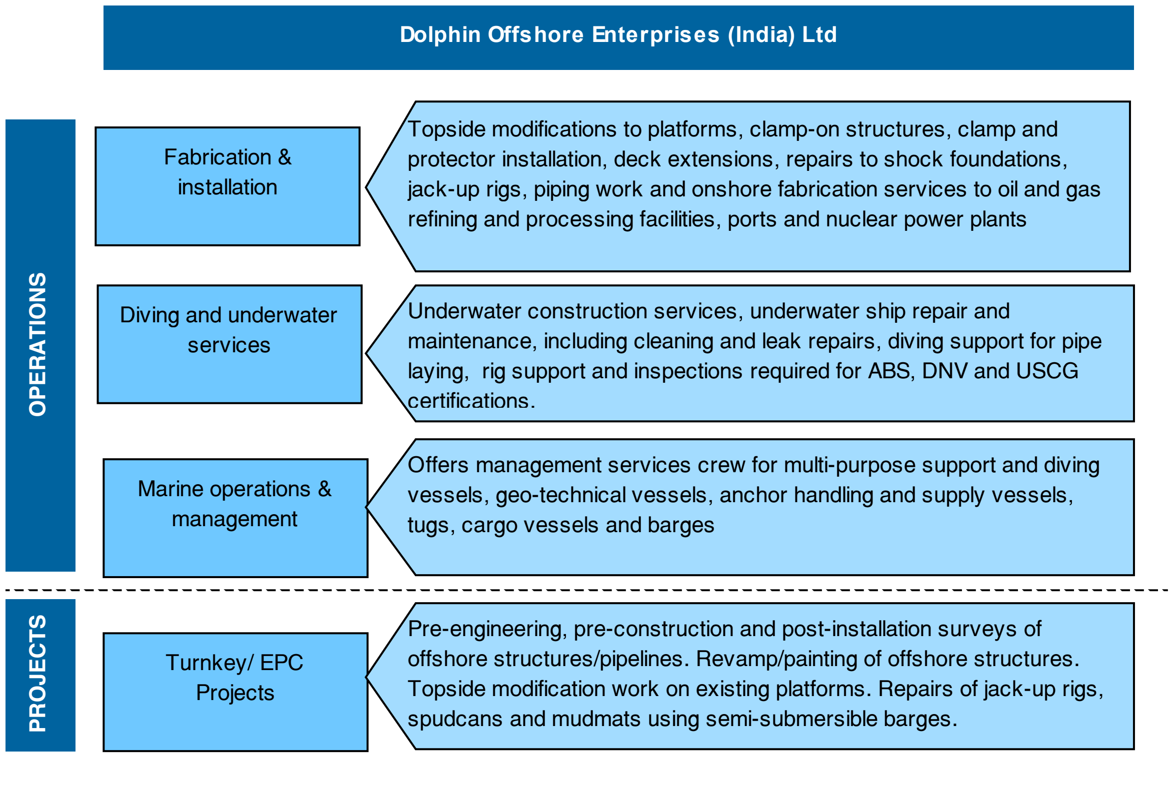
Dolphin Offshore has formed a joint venture with IMPaC Oil and Gas for providing integrated project/field development engineering, including overall consultancy, conceptual and feasibility studies, front end engineering design (FEED) and detailed engineering packages.

Chart 6: Business structure



Source: Company report, CRISIL Research

Table 7: Business Model



Source: Company reports, CRISIL Research

Main projects in FY09

The company is currently working on an EPC project for ONGC's MHS redevelopment project. Awarded in 2008, this project is being carried out for ONGC, with Dolphin Offshore working as sub-contractor to Larsen & Toubro Ltd (L&T). The job entails fabrication & installation of deck extension structure, fabrication & installation of piping, pipe support etc.

The company has achieved the main contractor status and is currently handling projects directly from ONGC such as, NQD and ICP projects with a combined value of Rs 3.02 Bn. This project is expected to be completed by FY10. The job involves design engineering, procurement, fabrication, marine loadout and offshore hook-up and commissioning activities.

ONGC is the major client

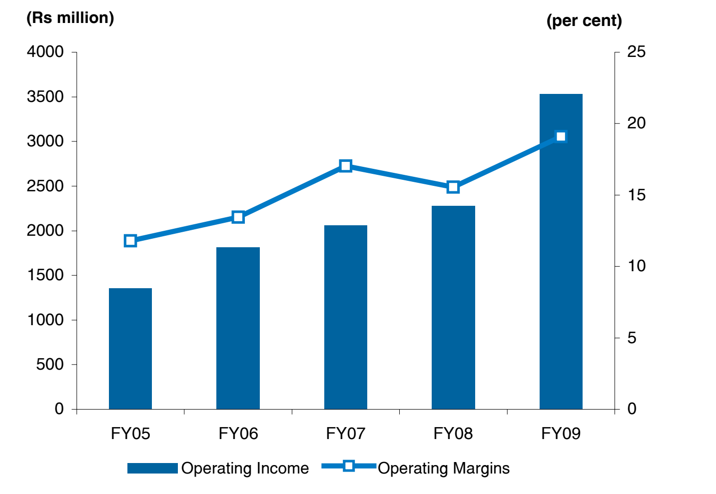
ONGC is a major client for the company. Most of its revenues, directly or indirectly, come from ONGC. Its other main clients include Larsen & Toubro Ltd, Leighton, Punj Lloyd Ltd, Hyundai Heavy Industries Co. Ltd, Indian Oil Corporation Ltd, Indian Coast Guard, Engineers India Ltd, N K K, British Gas Explortation & Production India Ltd, Aban Lloyd, Mazagon Dock Ltd, Naval Dockyard / Indian Navy, Cairn Energy Ltd and Essar Oil Ltd,

Revenue and margin drivers

Currently, as the company earns a major part of its revenues from turnkey projects, revenue can only be accrued on completion of the project, or on achieving certain milestones. Therefore, revenues reported in a period could involve the spillover of work from the pervious period and vice versa.

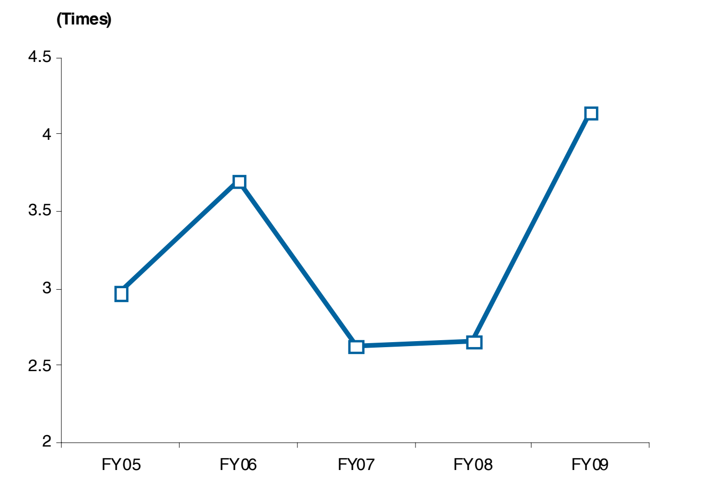
The company's margins are highly dependent on the rates of skilled personnel. As divers and offshore vessel officers in the industry usually work on a day-rate basis, the company's margins are vulnerable to changes in labour costs.

Chart 8: Operating income and margins



Source: Company reports

Chart 9: Asset turnover



Source: Company reports

Other plans

- The company plans to increase its reach in the Middle East to diversify the seasonality risk, mainly from June to December.
- It is planning to set up a fabrication unit and a shipyard in Gujarat; the fabrication unit is expected to be commissioned by end of FY11.
- The company also plans to set up an Underwater Training and Research Centre in co-operation with the Government of India and the Government of Norway.

The company has a number of vessels and diving assets that are chartered, or used, for its EPC projects. A list of equipments is mentioned below:

Table 1: List of equipments and vessels owned by Dolphin Offshore

Diving systems	
SDS 01	300 meter 10 man saturation diving system
SDS 02	200 meter 8 man saturation diving system
7 Air and mixed gas diving systems	
Underwater NDT equipment / cameras	
2 high pressure water blasters	
Various underwater tools and equipments	
Vessels	
Operational	
Brahmaputra Dolphin	Offshore supply vessel/ workboats
Ganga Dolphin	Offshore supply vessel/workboats
Kamrup	Offshore supply vessel/ Workboats
Everpower	Harbor tugs
Pioneer Star	Harbor tugs
SCH-3	Harbor tugs
Marina Venus	Harbor tugs
Marina Mercury	Harbor tugs
Time Skipper	Harbor tugs
Completed	
Beas Dolphin	Offshore supply vessel/workboats
Under construction	
Betwa Dolphin	Offshore supply vessel/ workboats
Vikrant Dolphin	Construction barge
Fabrication	
Fabrication yard near Navi Mumbai	

Note: The operational vessels under marine operations are under Procyon Offshore, Dolphin's subsidiary; the completed and under-construction vessels would be under Dolphin Offshore Mauritius, but will be managed by Procyon Offshore Ltd.

Source: Company, CRISIL Equities Estimate

Industry outlook

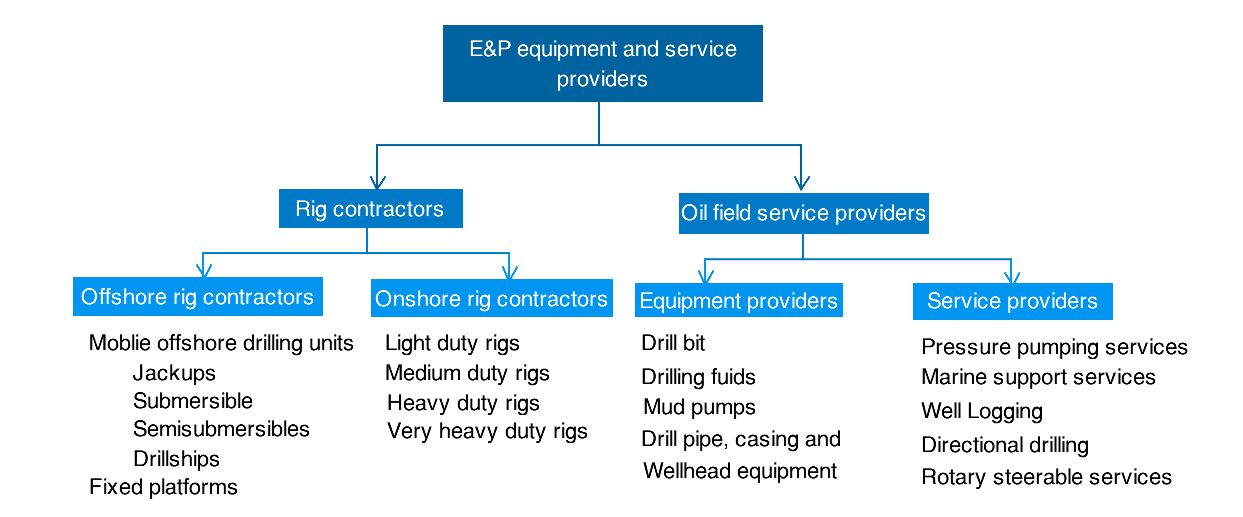
Rising crude oil prices, the key factor for spends in oil and gas exploration

Rising crude oil prices have been the key driver of E&P activities over the last 5 years. In addition, domestic E&P investments have also received a boost with higher acreage being made available under the various NELP rounds conducted so far. This, coupled with severe demand-supply mismatches, has increased the oilfield equipment and service rates.

Exploration and production (E&P) equipment and service providers are the ancillary industries that support E&P players. The equipment and service industry consists of two major sectors: contract drilling companies and oilfield service providers. Each sector comprises several sub-sectors and areas of specialised expertise.

They offer a wide range of services that oil producers generally do not source in-house; these services account for the largest share of an E&P player's capital expenditure. Rig contractors drill wells, whereas oilfield service companies assist the E&P players in drilling, evaluation and completion of wells.

Chart 10: Snapshot of E&P equipment and service providers



Source: CRISIL Research

Oilfield services providers

Oilfield service companies provide the tools and services required to expedite the drilling of wells. These companies assemble equipment, maintain it once in operation, and provide related products and services, including geological evaluations. Service providers encompass the group of companies that provide ancillary services (often of a highly technical nature) to the actual drilling.

Besides, they also provide equipment like drillbit, drilling fluids, drill pipes etc required in the drilling operations. Thus, their customers include oil and gas producers as well as drilling companies.

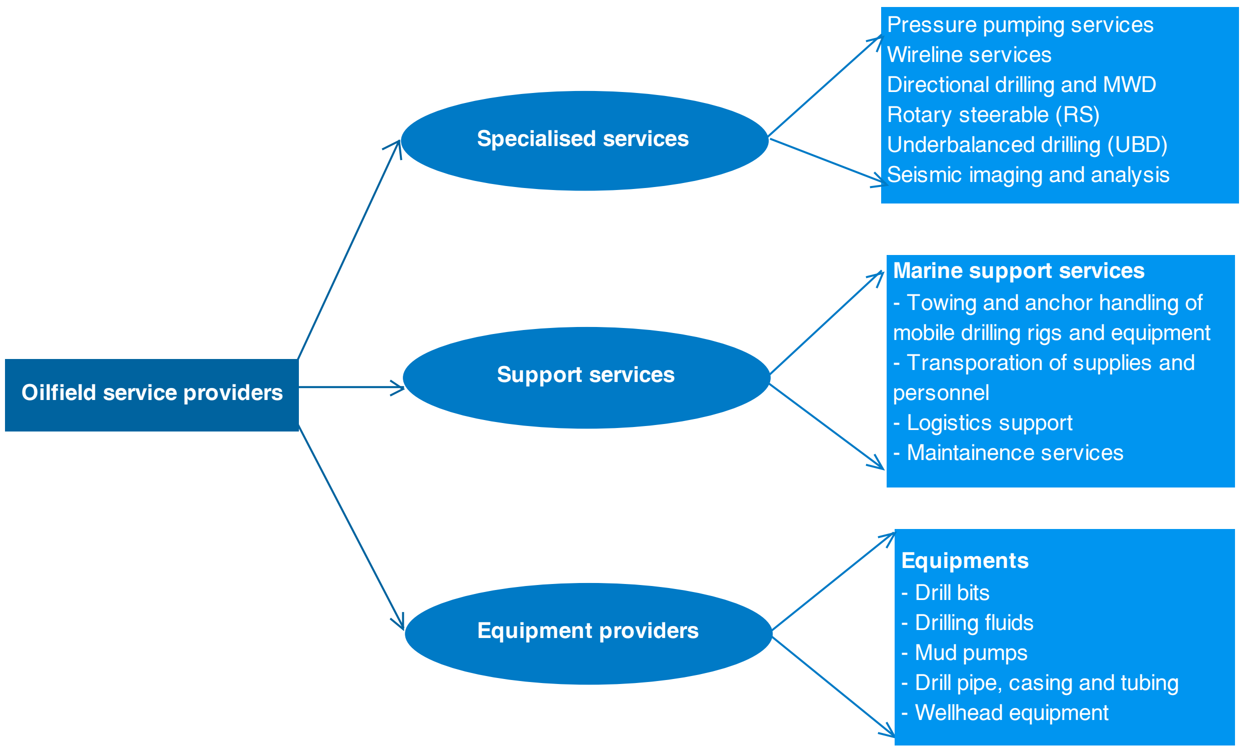
Mode of payment

The oilfield service providers also work on contract basis with contracts being either on day-work basis or on turnkey basis. The service providers charges usually consists of:

- Mobilisation charges
- Standby charges (above the rotary table: equipment which transfers power from the engine mounted on it to the drill pipe below)
- Charges for activities undertaken below the rotary table which could be charged on hourly basis and
- Demobilisation charges.

Besides the charges mentioned above, the service providers can also charge for any equipment or tool lost during the exploration and development activity.

Chart 11: Classification of oilfield service providers

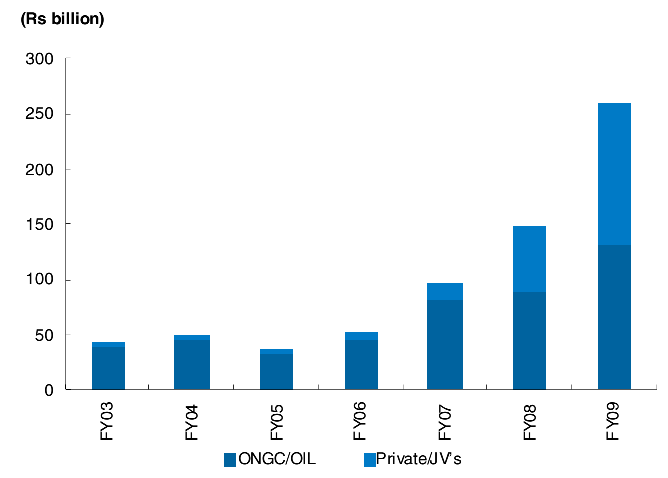
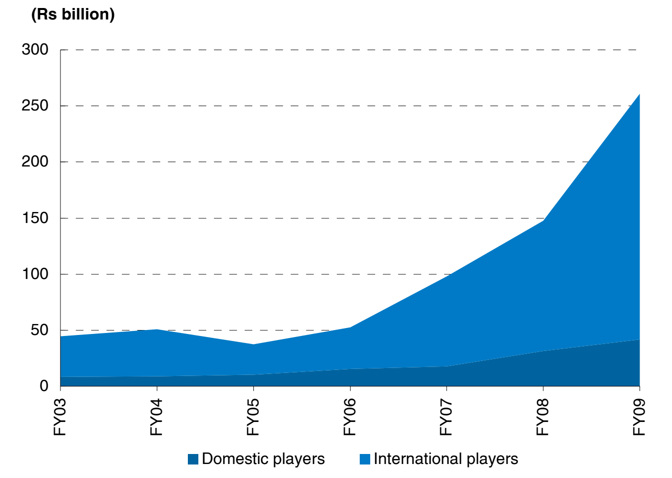


Source: CRISIL Research

Market Structure

Estimated industry size stands at Rs 261 Bn in FY09

The estimated market size of this segment in FY09 was around Rs 261 Bn (around $5.8 Bn). Historically, the capex spending of upstream in India has been dominated by public sector undertakings in accordance with their presence in the sector. However, with the sector being opened up to the private sector, and given their success in exploration, their share in upstream capex spending has been on the rise.

Chart 12: Increase in upstream investments in India by players	Chart 13: Beneficiaries of these investments in this segment by domicile
	
Source: Company reports, CRISIL Research	Source: Company reports, CRISIL Research

International players dominate the oilfield equipments and service industry

The industry is fairly consolidated with a few large players. However, smaller companies frequently develop expertise in a particular niche area, especially in oilfield services.

This industry can be divided on the basis of domicile of the players

- Domestic (around 20 per cent of market share)
- International (around 80 per cent of market share)

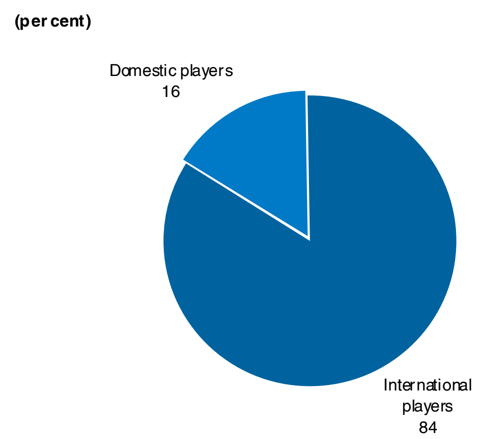
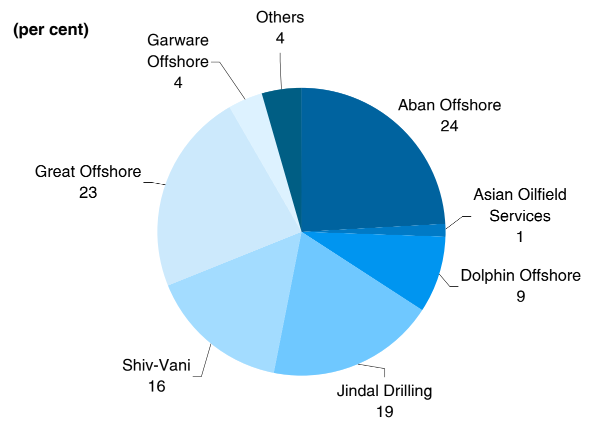
Chart 14: Total domestic market (FY09)	Chart 15: Share of domestic players (FY09)
	
Source: CRISIL Research	Source: BSE, CRISIL Research

Table 7: Company comparison

	Rig contractors		Service providers		
	Offshore rigs	Onshore rigs	Equipment providers	Specialised	Support
Domestic players					
Aban Offshore Ltd (AOL)					
Great Offshore Ltd					
Jindal Drilling and Industries Ltd					
Shiv-Vani Oil & Gas Exploration Services Ltd					
Dolphin Offshore Enterprises (India) Ltd					
Asian Oilfield Services Ltd					

Source: Bloomberg, company reports, CMIE

Review of the industry

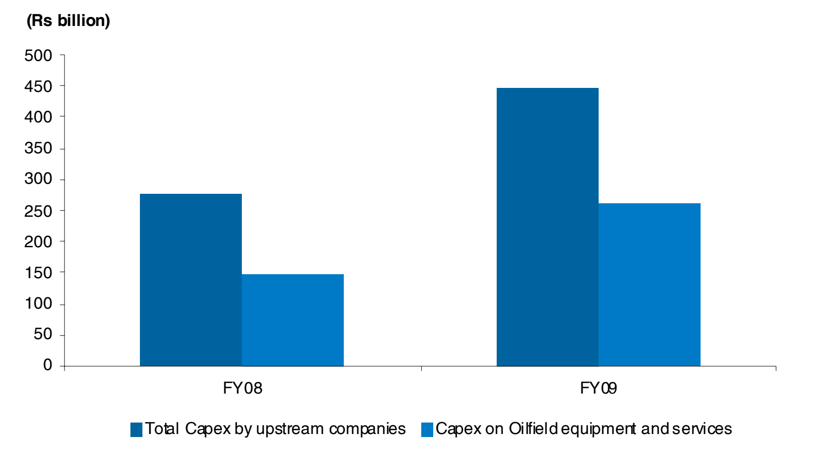
Market size has grown by 74% from FY08 to FY09

Higher crude prices led to a heightened interest in exploration, with huge investments made even in deep and ultra deep sea oil exploration. Historically, it has been observed that a change in exploration spends lags the change in crude oil price trend by almost 1 year. The global oil exploration spending cycle has been on an upturn since 2004, trailing the steady rise in crude oil prices during this period. Average crude oil prices (Dated Brent) reached record highs in 2008, moving from $91.9/bbl in January 2008 to $133.9/bbl in July 2008. However, prices cooled off in the ensuing period to reach $41.6/bbl in December 2008, as petroleum product demand contraction lowered the demand for crude.

On the domestic front, the estimated market size of this segment in FY09 was around Rs 261 Bn (around $5.8 Bn). This is an increase of around 74% as compared with the previous year FY08 (estimated – Rs 150 Bn (around $3.7 Bn)).

High crude oil prices augmented exploration activity, particularly in the first half of FY09. This, coupled with an increase in development activity in some major finds (especially Cairn's Rajasthan block & Reliance's Krishna-Godavari block) that were expected to commence production in FY10, enhanced the market size of this segment in FY09.

Chart 16: Capex of upstream investments



Source: Company reports, CRISIL Research

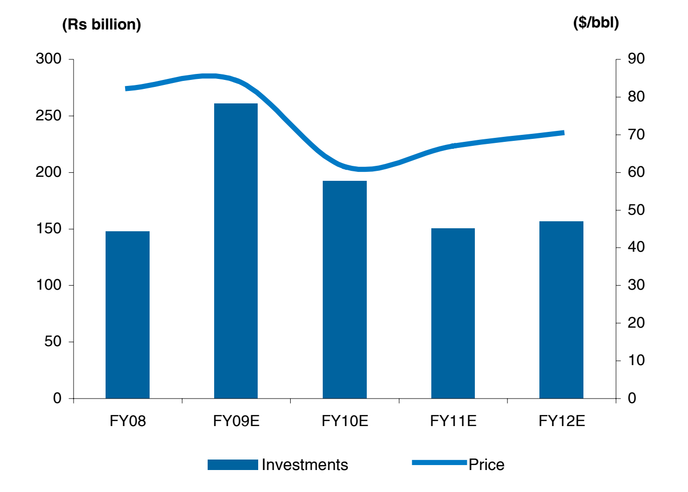
- Historically, the capex spending of upstream companies in India has been dominated by public sector undertakings (especially, ONGC and OIL) in accordance with their presence in the sector. However, with the sector being opened up to the private sector, and given their success in exploration, their share in upstream capex spending has been on the rise.

- Higher development activity by private players augmented their share to almost half of the total upstream capex spend in FY09.

Outlook of the industry

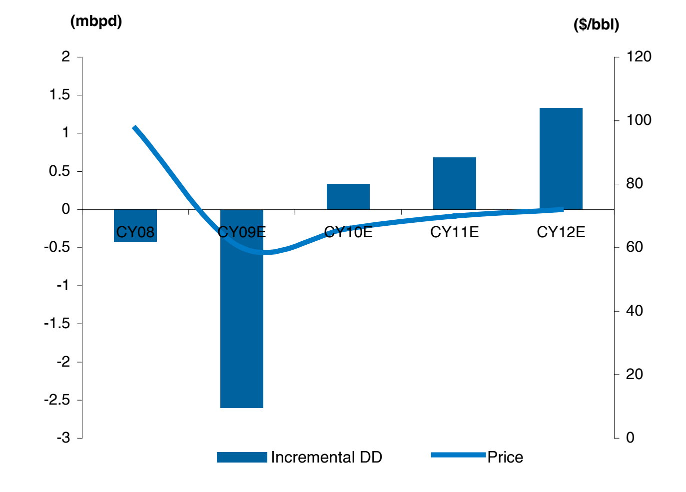
- The sharp decline in crude oil prices in the second half of FY09 led all major E&P companies to re-look at their capital expenditure plans; domestic E&P companies were no exception to this.
- Crude oil prices are expected to re-bound post 2009 with improving demand on the back of recovering global economic scenario. This is expected improve capital spending towards the end of the medium term.
- Medium-term yearly domestic E&P capital spending is expected to be lower than in FY09 on account of the following reasons:
  - Lower oil prices to reduce interests of E&P players in developing and producing from smaller and marginal oil fields.
  - Major development expenses that were part of the E&P capital expenditure spends made in FY09 would not be replicated over the medium term.
  - Costs of equipment and services too have declined, though not as sharply as has the price of oil in the past one year
- Higher number of gas discoveries, coupled with increasing exploration activity on blocks allocated under the recently completed rounds of NELP, and a largely unexplored domestic terrain would drive domestic E&P capital spends over the long term.

Chart 17: Incremental demand and oil price forecast over the medium term



Source: Company reports, Bloomberg, CRISIL Research

Chart 18: Oil prices and investments in E&P equipment and services



Source: Company reports, Bloomberg, CRISIL Research

- Despite the slowdown in the pace of E&P capital expenditure on the oilfield equipment and services industry by upstream majors in the country, domestic oil-field equipment and service providers would still have a massive opportunity before them as their estimated share of the total market was still low (below 20%) in FY09.

Annexure: Financials

Table 4: FINANCIAL STATEMENTS

Income statement

(Rs million)	FY 08	FY 09	FY 10 E	FY 11E	FY 12 E
Net sales	2,336.4	3,524.7	4,906.4	5,977.1	6,599.0
Operating income	2,340.1	3,529.7	4,913.3	5,985.5	6,608.3
EBITDA	366.5	673.7	855.8	1,128.0	1,216.3
Depreciation	77.3	74.5	143.8	229.2	283.1
Interest	136.7	145.9	154.3	189.1	234.8
Other income	140.7	11.0	19.5	30.0	40.0
PBT	242.1	598.8	577.2	699.7	678.4
PAT	152.2	441.7	386.7	468.8	461.3
Adjusted PAT	193.1	305.1	386.7	468.8	461.3

Balance Sheet

(Rs million)	FY 08	FY 09	FY 10 E	FY 11E	FY 12 E
Equity (Including reserves)	643.8	1,053.4	1,268.0	1,708.4	1,772.0
Debt	1,697.7	1,833.9	1,786.2	2,080.0	2,419.7
Current liabilities and provisions	877.9	1,019.5	1,287.3	1,483.9	1,617.3
Deferred tax liability/(asset)	46.9	16.0	21.8	35.8	49.3
Capital employed	**3,266.2**	**3,922.8**	**4,363.3**	**5,308.1**	**5,858.4**
Net fixed assets	1,030.8	1,454.9	1,517.6	1,792.4	2,118.3
Investments	2.7	1.6	28.6	175.5	72.2
Loans and advances	442.1	555.3	628.5	695.9	758.9
Inventory	2.0	3.4	5.0	6.0	6.6
Receivables	1,702.0	1,795.4	2,083.5	2,538.2	2,802.3
Cash & bank balance	86.7	112.2	100.0	100.0	100.0
Applications of funds	**3,266.2**	**3,922.8**	**4,363.3**	**5,308.1**	**5,858.4**

Ratios

	FY 08	FY 09	FY 10 E	FY 11E	FY 12 E
Sales growth	10.1%	50.8%	39.2%	21.8%	10.4%
EBITDA growth	-3.0%	83.8%	27.0%	31.8%	7.8%
EPS growth	-14.2%	190.3%	-41.7%	4.0%	-1.6%
Adjusted EPS growth	1.6%	58.0%	-15.7%	4.0%	-1.6%
EBITDA margin	15.7%	19.1%	17.4%	18.8%	18.4%
PAT Margin	6.5%	12.5%	7.9%	7.8%	7.0%
Adjusted PAT margin	8.3%	8.6%	7.9%	7.8%	7.0%
Return on capital employed (RoCE)	18.4%	21.1%	24.0%	24.5%	23.2%
Return on equity (RoE)	39.5%	68.6%	36.7%	37.0%	27.0%
Adjusted return on equity (RoE)	50.1%	47.4%	36.7%	37.0%	27.0%
Debtors days	266	186	155	155	155
Gross current days	343	248	204	200	199
Earnings per share (Rs)	15.9	46.2	26.9	28.0	27.5
Adjusted earnings per share (Rs)	20.2	31.9	26.9	28.0	27.5
Book value per share (Rs)	67.3	110.1	88.2	102.0	105.8
Debt-equity	2.6x	1.7x	1.4x	1.2x	1.4x
Current ratio	2.5	2.4	2.2	2.3	2.3
Interest coverage	0.4	0.2	0.2	0.2	0.2
Price-earnings	13.0x	8.2x	9.7x	9.4x	9.5x
Price-book	3.9x	2.4x	3.0x	2.6x	2.5x
EV/EBITDA	11.2x	6.3x	6.3x	5.5x	5.5x

Note: All ratios have been computed on adjusted PAT; interest costs are adjusted for FX losses and gains

Source: Company, CRISIL Equities Estimate

About CRISIL Limited

CRISIL is India's leading Ratings, Research, Risk and Policy Advisory Company

About CRISIL Research

CRISIL Research is India's largest independent, integrated research house. We leverage our unique, integrated research platform and capabilities spanning the entire economy-industry-company spectrum to deliver superior perspectives and insights to over 600 domestic and global clients, through a range of subscription products and customised solutions.

Mumbai

1061, Solitaire Corporate Park,
Andheri-Ghatkopar Link Road,
Andheri (East), Mumbai - 400 093
Phone: +91 (22) 6758 8000
Fax: +91 (22) 6758 8088

Bangalore

W-101, 1st floor, Sunrise Chambers, 22,
Ulsoor Road,
Bangalore - 560 042
Phone: +91 (80) 2558 0899/ 2559 4802
Fax: +91 (80) 2559 4801

Kolkata

Horizon, Block-B, 57,
Chowringhee Road,
Kolkata - 700 071
Phone: +91 (33) 2289 1949/ 2289 1950
Fax: + 91 (33) 2283 0597

Chennai

Thapar House,
43/ 44, Montieth Road,
Egmore, Chennai 600 008
Phone: +91 (44) 2854 6205/ 06
Fax: +91 (44) 2854 7531

New Delhi

The Mira,
G-1, 1st Floor, Plot No. 1 & 2
Ishwar Nagar, Near Okhla Crossing
New Delhi - 110 065
Phone: +91 (11) 4250 5100
Fax: +91 (11) 2684 2212/ 13

For further details
or more information, please contact:
Client Servicing
CRISIL Research
261/262, Solitaire Corporate Park
Andheri-Kurla Road, Andheri (E)
Mumbai - 400 093, India
Phone: +91 (22) 6691 3561/ 62
Fax: +91 (22) 6702 6954
E-mail: clientservicing@crisil.com/
research@crisil.com

CRISIL

www.crisilresearch.com