

Buy

Gail India



Industry: Oil & Gas

Result Update

Lower subsidy drives Q3FY13 performance

GAIL's Q3FY13 net profit of Rs12.8bn was significantly higher than our estimate of Rs10.3bn primarily on account of lower subsidy burden during the quarter. GAIL's subsidy burden for the quarter fell by 19.7% yoy to Rs70bn (qoq -10.9%) which was significantly lower than our estimate of Rs9.1bn. Net revenues at Rs124.7bn registered a jump of 10.8% yoy mainly on account of higher revenues in natural gas trading, LPG & OLHC and petchem segments. GAIL's gas transmission volumes during the quarter declined to 105mmscmd (lowest in last 14 quarters) due to fall in volumes from RIL's KG D6 while gas transmission tariff declined by 11.8% yoy to Rs969/tcm (qoq +3.7%). Petchem volumes increased sequentially by 26.7% while realizations improved by 4.8% qoq. However, petchem margins during the quarter declined by sequentially 783bps to 39.7% (yoy -443bps) on account of higher raw material costs. Gas trading segment reported a strong 22% sequential jump in EBIT to Rs2.9bn as the company was able to earn higher marketing on higher LNG volumes.

We lower our gas transmission assumption for FY13e and FY14e to 106 and 111mmscmd. Consequently, we lower our FY13e/FY14e earnings by 4.6/4.4% and. We maintain BUY rating on GAIL with a revised SOTP based price target of Rs407. At the CMP, the stock is trading at 8.5x and 6.2x FY14e earnings and EV/EBITDA respectively.

Net revenues for the quarter increased by 10.8% yoy to Rs124.7bn

Gas trading revenues increased by 10.6 yoy to Rs101.2bn (qoq +4.3%). GAIL's core natural gas transmission business revenues declined by 9% sequentially to Rs9.9bn (qoq +0.5%) as volumes declined of 11.8%/-0.9% yoy/qoq to 105mmscmd due to fall in volumes from RIL's KG D6. Gas transmission tariff declined by 11.8% yoy to Rs969/tcm (qoq +3.7%). Petchem revenues increased by 32.3% yoy to Rs12.8bn (qoq +66%) driven by 13.3% volume growth and 4.8% increase in realisations. LPG & OLHC revenues witnessed an increase of 32.3% yoy and 66% qoq due to lower subsidy burden during the quarter.

Operating profit increased by 12% yoy to Rs19.7bn

GAIL's operating profit of Rs19.7bn for the quarter was significantly higher than our estimate of Rs16.3bn mainly on account of lower subsidy burden during the quarter. GAIL's core gas transmission EBIT decreased marginally by 0.2% yoy to Rs6.2bn (qoq +2.4%) as increase in gas transmission tariff negated the fall witnessed in gas transmission volumes. Petchem margin during the quarter declined by 443bps yoy to 39.7% (qoq -783bps) on account of higher raw material costs. Consequently, petchem EBIT increased by 13.4% yoy to Rs4.4bn (qoq +5.1%) in spite of higher volume growth. Gas trading segment reported a strong 22% sequential jump in EBIT to Rs2.9bn as the company was able to earn higher marketing on higher LNG volumes.

PAT increased by 18% yoy to Rs12.9bn

Driven by lower subsidy burden during the quarter, GAIL's PAT for the quarter of Rs12.9bn was significantly higher than our (Rs10.3bn) and street estimates. EPS for the quarter stood at Rs10.1.

Stock Data

Current Market Price (₹)	336
Target Price (₹)	407
Potential upside (%)	21
Reuters	GAIL.BO
Bloomberg	GAIL IN

What's Changed

Target Price (₹)	430 to 407
F2013 EPS (₹)	37.5 to 35.9
F2014 EPS (₹)	41.4 to 39.6

Key Data

Market Cap (₹bn)	424
52-Week Range (₹)	401 / 303
Avg. Daily Trading Value (₹mn)	390
Promoters (%)	57
FII Holding (%)	16
DII Holding (%)	23
Public & Others Holding (%)	4

Fiscal YE	FY11	FY12	FY13e	FY14e
Total sales(Rs bn)	351	441	454	471
EBITDA margins(%)	18.5	16.2	16.7	18.0
PAT margins(%)	11.4	10.1	10.0	10.7
EPS(Rs)	31.6	35.0	35.9	39.6
P/E(x)	10.6	9.6	9.4	8.5
P/BV(x)	2.0	1.7	1.5	1.3
EV/EBITDA(x)	7.2	7.3	7.0	6.2
ROE(%)	20.6	19.3	17.2	16.7
ROCE(%)	16.2	14.2	12.3	12.2
Dividend yield (%)	2.2	2.6	2.6	2.6

Relative Price Performance



One Year Indexed

(%)	1 Month	3 Months	12 Months
Absolute	(11)	(7)	(15)
BSE Relative	(10)	(12)	(26)

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Actual v/s Estimates

Y/E, Mar (Rs. m)	Q3FY13	Q2FY13	qoq (%)	Q3FY12	yoy (%)	LKP Estimates	Deviation (%/bps)
Revenue	124,743	113,612	9.8%	112,598	10.8%	113,400	10.0%
EBITDA	19,722	13,803	42.9%	17,605	12.0%	16,347	20.6%
EBITDA (%)	15.8%	12.1%	366 bps	15.6%	17 bps	14.4%	139 bps
PAT	12,849	9,854	30.4%	10,914	17.7%	10,251	25.3%

Result Table

Y/E, Mar (Rs. m)	Q3FY12	Q2FY13	Q3FY13	yoy (%)	qoq (%)	9MFY12	9MFY13	yoy (%)
Net Revenue	112,598	113,612	124,743	10.8%	9.8%	152,000	185,664	22.1%
Raw Material Consumption	8,516	5,413	8,237	-3.3%	52.2%	9,009	9,316	3.4%
Purchase of gas for trading	77,229	84,609	86,557	12.1%	2.3%	101,583	128,040	26.0%
Employee Cost	1,983	1,736	1,683	-15.1%	-3.1%	3,172	3,561	12.3%
Other Expenditure	7,265	8,051	8,545	17.6%	6.1%	9,559	12,709	33.0%
Total Operating Costs	94,993	99,809	105,021	10.6%	5.2%	123,324	153,626	24.6%
EBITDA	17,605	13,803	19,722	12.0%	42.9%	28,677	32,038	11.7%
EBITDA (%)	15.6%	12.1%	15.8%	17 bps	366 bps	18.9%	17.3%	-206 bps
Depreciation	1,975	2,491	2,424	22.7%	-2.7%	3,226	3,789	17.5%
Interest	207	261	552	166.2%	111.3%	323	434	34.5%
Other Income	557	2,685	1,841	230.4%	-31.4%	2,416	2,297	-4.9%
PBT	15,980	13,736	18,587	16.3%	35.3%	27,544	30,111	9.3%
Tax	5,066	3,882	5,738	13.3%	47.8%	9,440	9,320	-1.3%
Tax Rate (%)	31.7%	28.3%	30.9%	-83 bps	261 bps	34.3%	31.0%	-223 bps
Adj PAT	10,914	9,854	12,849	18%	30%	18,104	20,791	14.8%
Rep PAT	10,914	9,854	12,849	17.7%	30.4%	18,104	20,791	14.8%
Shares outstanding (mn)	1,268	1,268	1,268			1,268	1,268	
Reported EPS (Rs)	8.6	7.8	10.1	17.7%	30.4%	14.3	16.4	14.8%

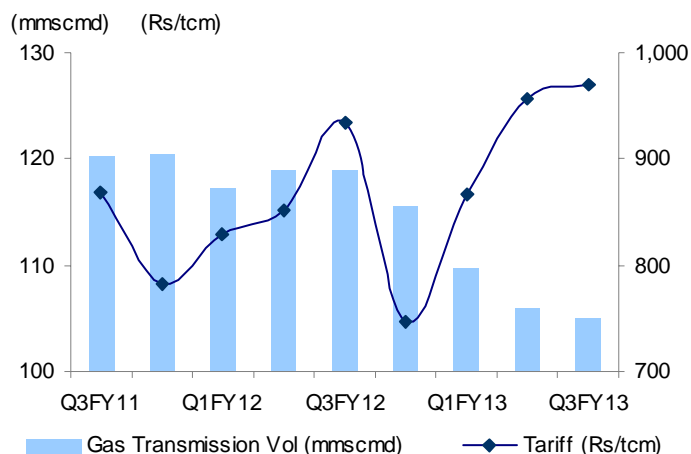
Operational Performance

Y/E, Mar (Rs. m)	Q3FY12	Q2FY13	Q3FY13	yoy (%)	qoq (%)	9MFY12	9MFY13	yoy (%)
Segment Revenue								
Natural Gas (Transmission)	10,872	9,845	9,894	-9.0%	0.5%	18,762	19,189	2.3%
LPG (Transmission)	1,216	-40	808	-33.5%	na	2,276	2,240	-1.6%
Natural Gas Trading	91,495	96,970	101,180	10.6%	4.3%	117,411	147,808	25.9%
Petrochemicals	8,780	8,798	11,070	26.1%	25.8%	13,585	15,746	15.9%
LPG & Liquid Hydrocarbons	9,654	7,695	12,772	32.3%	66.0%	15,182	18,026	18.7%
Others	344	758	435	26.2%	-42.7%	295	477	61.9%
Segment EBIT								
Natural Gas (Transmission)	6,208	6,049	6,195	-0.2%	2.4%	13,612	12,083	-11.2%
LPG (Transmission)	775	-489	133	-82.9%	na	1,520	1,412	-7.1%
Natural Gas Trading	3,230	2,447	2,986	-7.5%	22.0%	3,181	5,997	88.5%
Petrochemicals	3,875	4,182	4,395	13.4%	5.1%	5,562	6,474	16.4%
LPG & Liquid Hydrocarbons	3,055	665	5,920	93.8%	790.8%	4,085	5,806	42.1%
Others	-436	69	-834	na	na	-616	-1,153	na
EBIT Margins								
Natural Gas (Transmission)	57.1%	61.4%	62.6%	551 bps	118 bps	72.5%	63.0%	-958 bps
LPG (Transmission)	63.8%	na	16.4%	-4733 bps	na	66.8%	63.0%	-376 bps
Natural Gas Trading	3.5%	2.5%	3.0%	-58 bps	43 bps	2.7%	4.1%	135 bps
Petrochemicals	44.1%	47.5%	39.7%	-443 bps	-783 bps	40.9%	41.1%	18 bps
LPG & Liquid Hydrocarbons	31.6%	8.6%	46.4%	1471 bps	3772 bps	26.9%	32.2%	530 bps
Volume								
Gas Transmission Vol (mmscmd)	119	106	105	-11.8%	-0.9%	116	118	2.2%
LPG Transmission Vol (tmt)	870	813	733	-15.7%	-9.8%	1,587	1,613	1.6%
Petchem sales (tmt)	113	101	128	13.3%	26.7%	195	217	11.3%
LPG & OLHC sales (tmt)	361	361	340	-5.8%	-5.8%	703	727	3.4%

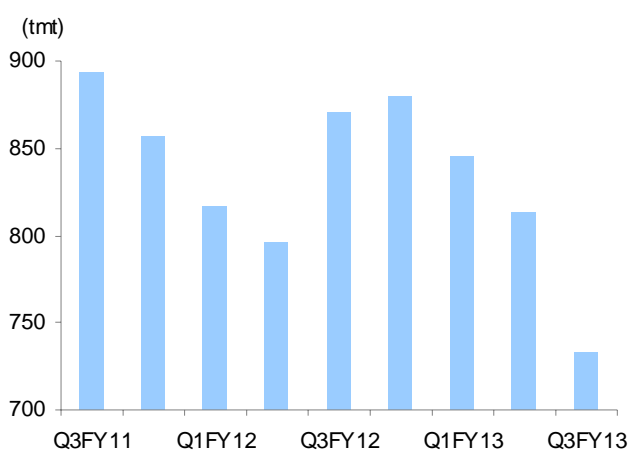
Revised Estimates

Rs mn	FY13e			FY14e		
	Old	New	% change	Old	New	% change
Sales	456,982	453,813	-0.7%	474,434	471,107	-0.7%
EBITDA	79,156	75,987	-4.0%	88,322	84,994	-3.8%
PAT	47,770	45,575	-4.6%	52,532	50,227	-4.4%
EPS	37.7	35.9	-4.6%	41.4	39.6	-4.4%
Transmission Vol	116.0	106.0	-8.6%	121.0	111.0	-8.3%

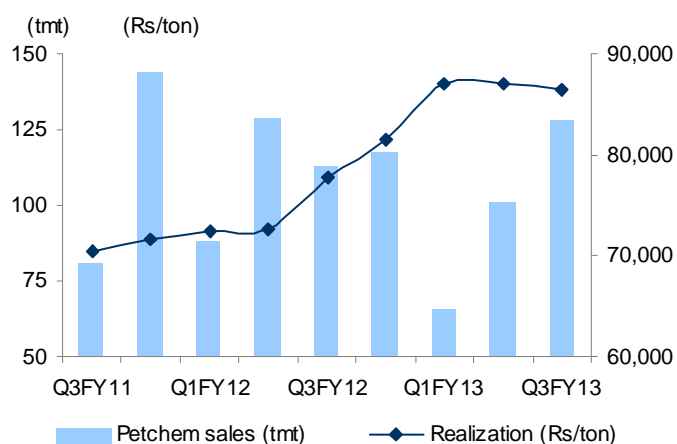
Gas Transmission



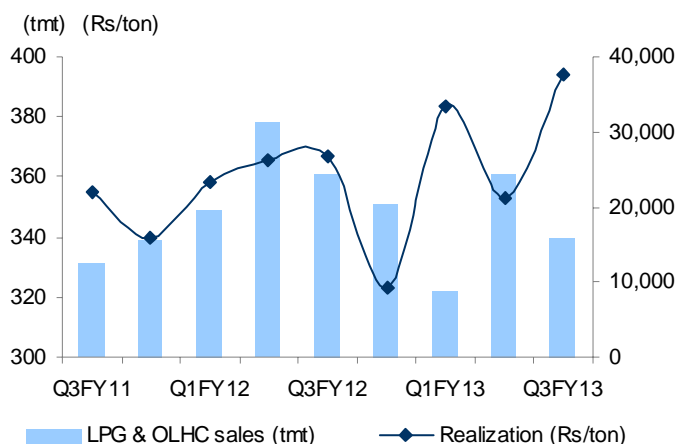
LPG Transmission



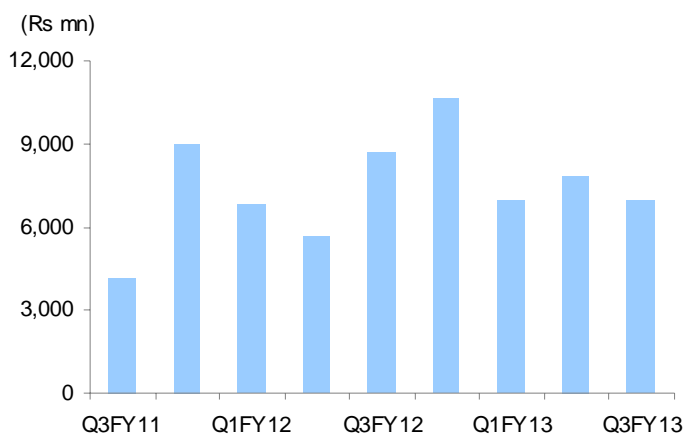
Petchem Sales



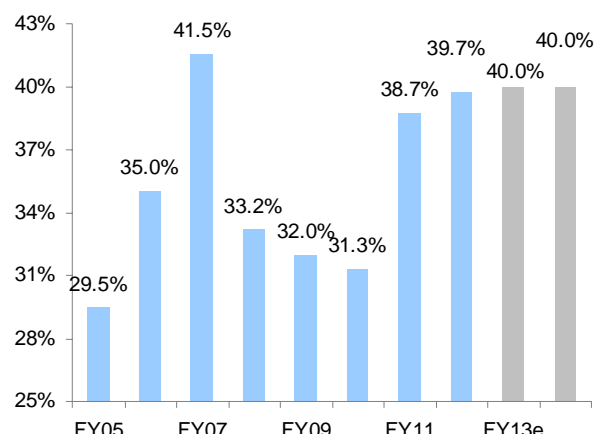
LPG & OLHC Sales



GAIL's subsidy burden



Upstream share in total under recovery (%)



Source: LKP Research

Valuation and view

In the near term, we believe that concerns relating to lack of growth in GAIL's key gas transmission segment could be an overhang on the stock. However, we expect back ended volume growth on account of start of LNG terminals and production from new gas fields. GAIL has very strong prospects given its dominant presence across different segments, in the gas sector in India. This we believe would help GAIL to benefit significantly from increasing gas supplies post 2015.

We lower our gas transmission assumption for FY13e and FY14e to 106 and 111 mmscmd. Consequently, we lower our FY13e/FY14e earnings by 4.6/4.4% and. We maintain BUY rating on GAIL with a revised SOTP based price target of Rs407. At the CMP, the stock is trading at 8.5x and 6.2x FY14e earnings and EV/EBITDA respectively.

SOTP valuation - FY14e basis

Business verticals	Method	Multiple	Value	EV (Rs mn)	Value (Rs/sh)
Gas & LPG Transmission	EV/EBITDA	7.5x	33,617	252,125	199
Gas Trading	EV/EBITDA	6x	9,616	57,697	45
Petrochemicals	EV/EBITDA	6x	19,413	116,480	92
LPG Business	EV/EBITDA	6x	16,209	97,251	77
Exploration Business	Book Value	1x	25,000	25,000	20
Total EV				548,554	432
Net Debt / (Cash)				101,060	80
Equity Value				447,494	353
Investments	25% discount				55
Target Price					407
CMP					336
Upside / (Downside)					21%

Financial Summary

Income statement

Y/E, Mar (Rs. m)	FY11	FY12	FY13e	FY14e
Net Sales	351,067	440,578	453,813	471,107
yoy (%)	29.9%	25.5%	3.0%	3.8%
Raw Materials Exp	20,492	23,000	26,224	26,725
Purch - traded goods	220,997	293,047	294,689	300,583
Employee Cost	8,179	6,553	7,848	8,083
Other Expenditure	32,139	40,520	43,168	44,824
Total Expenditure	286,097	369,018	377,826	386,112
EBITDA	64,970	71,561	75,987	84,994
EBITDA margin	18.5%	16.2%	16.7%	18.0%
yoy (%)	19%	10%	6%	12%
Depreciation	8,880	10,406	12,620	15,005
Core EBIT	56,090	61,155	63,367	69,989
Core EBIT margin	16.0%	13.9%	14.0%	14.9%
Other Income	5,574	6,062	6,562	7,062
EBIT	61,664	67,217	69,929	77,051
EBIT margin	17.6%	15.3%	15.4%	16.4%
Interest	3,779	3,664	4,738	5,142
PBT	57,886	63,552	65,191	71,909
Tax	18,181	19,540	20,044	22,109
Tax rate (%)	31.4%	30.7%	30.7%	30.7%
Adj PAT	39,705	44,012	45,147	49,800
Minority Interest/Associates	401	428	428	428
Adj PAT after MI	40,106	44,440	45,575	50,227
EOs	-104	4	0	0
Reported PAT	40,210	44,436	45,575	50,227

Key Ratios

Y/E, Mar	FY11	FY12	FY13e	FY14e
Profitability				
Gross profit margin	31.2%	28.3%	29.3%	30.5%
EBITDA margin	18.5%	16.2%	16.7%	18.0%
Core EBIT margin	16.0%	13.9%	14.0%	14.9%
APAT margin	11.4%	10.1%	10.0%	10.7%
Tax Rate	31.4%	30.7%	30.7%	30.7%
Per Share (Rs)				
EPS (Rs)	31.6	35.0	35.9	39.6
CEPS (Rs)	38.6	43.2	45.9	51.4
Book Value Per Share (Rs)	167.2	196.4	222.2	251.6
Dividend Per Share (Rs)	7.5	8.7	8.7	8.7
Valuations Ratios (x)				
PER	10.6	9.6	9.4	8.5
P/CEPS	8.7	7.8	7.3	6.5
P/BV	2.0	1.7	1.5	1.3
EV/EBITDA	7.2	7.3	7.0	6.2
EV/Sales	1.3	1.2	1.2	1.1
M-Cap/EBITDA	6.6	6.0	5.6	5.0
M-Cap/sales	1.2	1.0	0.9	0.9
Financial ratios				
ROCE	16.2%	14.2%	12.3%	12.2%
ROIC	28.7%	25.4%	20.0%	18.1%
ROE	20.6%	19.3%	17.2%	16.7%
Debt/Equity	0.33	0.45	0.43	0.41
Dividend yield (%)	2.2%	2.6%	2.6%	2.6%
Growth				
Net Sales	29.9%	25.5%	3.0%	3.8%
EBITDA	18.9%	10.1%	6.2%	11.9%
Core EBIT	20.8%	9.0%	3.6%	10.5%
APAT	20.0%	10.8%	2.6%	10.2%

Balance sheet

Y/E, Mar (Rs. m)	FY11	FY12	FY13e	FY14e
Equity share capital	12,685	12,685	12,685	12,685
Reserves & surplus	199,454	236,447	269,142	306,489
Networth	212,139	249,132	281,827	319,174
Minority Interest	5,472	9,820	9,820	9,820
Secured Loans	62,640	101,704	101,704	101,704
Unsecured Loans	6,401	10,393	20,393	30,393
Loan Funds	69,041	112,098	122,098	132,098
Total Liabilities	286,652	371,050	413,745	461,092
Gross Block	266,051	317,692	390,232	451,503
Less: Depreciation	106,429	116,119	128,739	143,744
Net block	159,622	201,573	261,494	307,759
Capital WIP	106,368	145,081	122,541	111,270
Investment	12,363	12,841	12,841	12,841
Current Assets	123,168	150,847	159,785	176,873
Inventories	10,586	17,257	17,775	18,452
Sundry debtors	21,022	22,691	23,373	24,264
Cash & bank balance	25,844	14,462	19,304	31,038
Other assets	129	7,146	7,361	7,641
Loans & advances	65,587	89,291	91,973	95,478
Current Liab & Prov	97,717	120,641	124,265	129,001
Current liabilities	55,414	72,946	75,137	78,000
Provisions	42,304	47,696	49,128	51,001
Net current assets	25,450	30,205	35,520	47,872
Net Def tax liability	-17,151	-18,650	-18,650	-18,650
Total Assets	286,652	371,050	413,745	461,092

Cash Flow

Y/E, Mar (Rs. m)	FY11	FY12	FY13e	FY14e
Profit after Tax	42,091	44,436	45,575	50,227
Add : Depreciation	8,243	10,406	12,620	15,005
Add : Non cash	6,954	10,568	0	0
changes in Inventory	-1,994	-6,670	-518	-677
changes in debtors	-5,953	-1,669	-682	-891
changes in other CA	0	-7,018	-215	-281
changes in L & A	0	-23,704	-2,682	-3,505
changes in CL & prov	1,336	22,924	3,624	4,736
Net changes in WC	-6,610	-16,136	-473	-618
CFO	50,678	49,274	57,722	64,614
Capital expenditure	-72,426	-90,354	-50,000	-50,000
Investments	-1,711	-478	0	0
CFI	-74,137	-90,832	-50,000	-50,000
Increase in debt	14,909	43,057	10,000	10,000
dividend paid	-11,093	-12,880	-12,880	-12,880
CFE	3,816	30,177	-2,880	-2,880
Net cash generated	-19,643	-11,381	4,842	11,734
Opening balance	45,486	25,844	14,462	19,304
Closing balance	25,844	14,462	19,304	31,038
Free Cash flow	-21,748	-41,080	7,722	14,614

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