

Institutional Equity Research

GAIL India

Oil & Gas | India

3QFY20 Result Update | February 11, 2020

CMP* (Rs)	122
Upside/ (Downside) (%)	26
Bloomberg Ticker	GAIL IN
Market Cap. (Rs bn)	549
Free Float (%)	48
Shares O/S (mn)	4510

BUY 

Target Price: Rs154

Operating Profit Beats Estimate; Maintain BUY

GAIL's EBITDA grew by 33% QoQ (down 23% YoY) to Rs20.7bn in 3QFY20 (beating consensus/ours estimate by 11%/20%) mainly due to strong performance across segments. The quarter is marked with: (1) Record volume, improved realisation and one of the lowest operating cost in gas and LPG transmission segment; (2) bounce back of gas trading margin of US\$0.21/mmbtu from the lows of US\$0.12/mmbtu in 2QFY20; (3) Petrochemical plant utilisation rose to 106% with sharp recovery in EBITDA/kg to Rs5 from Rs1.5 in 2QFY20; (4) Despite lowest LPG price realisation, segment reported rise in sequential EBITDA on the back of lower gas cost. Notably, the company – which has not accepted the new ETR – is in the process of evaluating its impact. We believe, new fertiliser plants and CGD's lined up on Urja-Ganga pipeline would be the major growth driver of GAIL's gas transmission and trading segment. **We maintain our BUY recommendation on the stock with a DCF-based Target Price of Rs154.**

Segmental Analysis

- **Natural Gas Transmission:** Volume increased by 2% YoY and 1% QoQ on the back of 5% YoY improvement in India's gas consumption led by higher demand from CGD, fertiliser and refinery sectors.
- **LPG Transmission:** Segmental EBITDA grew by 19% YoY and 13% QoQ to Rs1.1bn owing to 9% YoY rise in unit realisation, while LPG transmission volume improved by 4% QoQ.
- **Gas Trading:** Gas trading volume grew by 1% QoQ to 96mmscmd, while the improved EBIT margin of US\$0.21/mmbtu (+92% QoQ) on the back of more number of LNG cargoes sold outside India (higher demand of LNG due to winter season).
- **Petrochemical:** Disappointing financial performance continued with EBITDA falling by 24% YoY to Rs1.1bn mainly due to lower petrochemical prices led by less demand. However, utilisation at the petrochemical facility touched a high of 106% in 3QFY20.
- **LPG & OLHC Production:** Despite lower LPG price realisation, segment posted 16% QoQ growth in EBITDA on back of fall in APM gas price.

Attractive valuation

We believe hiving off of the pipeline business will take more than a year, which would be the key overhang for the stock. We expect GAIL's earnings to clock just 10% CAGR over the next 3 years. We expect the Company to witness a strong FCF generation of Rs115bn over FY20-FY22E. The stock provides high earnings visibility and healthy RoE/RoCE of 12%/13% over the next 3 years. At CMP, the stock trades at 6.1x of FY21E EBITDA, which is at discount to its long-term average of 7.4x (over the last 5 years). **We maintain our BUY recommendation on the stock with a DCF-based Target Price of Rs154.**

Quarterly Performance	3QFY20	3QFY19	YoY (%)	2QFY20	QoQ(%)
Net sales	177,688	197,890	(10.2)	180,411	(1.5)
Total expenditure	156,965	171,155	(8.3)	164,784	(4.7)
EBITDA	20,724	26,735	(22.5)	15,627	32.6
PBT	12,507	16,812	(25.4)	10,643	21.9
Tax	6,210	8,262	(24.8)	4,713	31.8
PAT	12,507	16,812	(25.6)	10,643	17.5

Source: Company, RSec Research

Share price (%)	1 mth	3 mth	12 mth
Absolute performance	(2.8)	(6.6)	(25.8)
Relative to Nifty	(1.0)	(7.6)	(36.3)

Shareholding Pattern (%)	Dec-19	Sept-19
Promoter	52.1	52.7
Public	47.9	47.3

Key Financials (Rs mn)	FY20E	FY21E	FY22E
Revenues	686,688	703,620	662,094
EBITDA	91,592	99,891	104,985
PAT	62,332	69,951	72,958
EPS	13.8	15.5	16.2
P/E	8.8	7.9	7.5
EV/EBITDA	6.7	6.2	5.9
ROE (%)	12.3	12.6	12.1

1 Year Stock Price Performance

Note: * CMP as on Feb 10, 2020

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Conference Call – Key Takeaways

Natural Gas Transmission

- Kochi-Mangalore gas pipeline is expected to be completed by Mar'20. The Management guided that Kochi terminal is now able to sell ~1MMTPA of LNG and after completion of pipeline another 1 MMTPA gas volume can be transmitted to Mangalore.
- GAIL incurred >Rs88bn capex for Jagdishpur-Haldia-Bokaro-Dhamra (JHBDPL) pipeline up to 9MFY20, out of total commitment of Rs130bn. It received grants to the tune of Rs3.2bn from the government so far.
- Urja-Ganga (JHBDPL) pipeline is completed till Matix fertilizer plant (Patna) and likely to charge gas transmission tariffs of Rs63/mmbtu. The company has guided gas transmission volume of 8mmscmd through this pipeline in the next 2 years. The gas consumption will be driven by the fertiliser plants and new CGD areas.
- Matrix/Ramgundam fertiliser plant is likely to start operation by 1QFY21, which will consume 2.5/2mmscmd of gas.

Natural Gas Trading

- Total gas sales stood at 96mmscmd out of which 12 LNG cargoes sold outside India in 3QFY20 vs. 9 in 2QFY20.
- Till 9MFY20, out of total 66 US LNG cargoes, GAIL has sold 34 out of India and 32 inside India.
- For FY21E, the company has allocated most cargoes barring only 8 unallocated.
- Segmental EBITDA increased by 106% QoQ on the back of more US LNG cargoes sold out of India on a higher demand in winter season.
- **Petrochemical:** The CCEA has approved transfer of operating controls of Brahmaputra Cracker and Petrochemical Limited towards GAIL and has provided feed stock subsidy of Rs46bn for 15 years to maintain 10% IRR of the plant. For the past period (FY16 to FY18), the government has provided stock subsidy of Rs9.3bn towards the same project. This has been accounted into the quarterly result.
- **Capex:** The company incurred Rs38bn capex till 9MFY20 and planned to spend another Rs27bn in 4QFY20E.
- **Dividend:** The Board of Director has approved the interim dividend of Rs6.4/share, which implies a dividend yield of 6%.
- **Clarification on AGR issue:** The company had received provisional assessment order towards annual license fee in respect of IP-II licensee from several financial years from the DoT, which had submitted a total outstanding of Rs1,837bn including interest and penalty computed on the entire revenue of the company. The company is of the view that the amount assessed in provisional assessment is legally untenable. Further, the company has also filed an impeachment application along with application of modification in the Supreme Court on 23rd January 2020.

Quarterly Performance

Rs mn	3QFY20	3QFY19	YoY (%)	2QFY20	QoQ(%)
Net sales	177,688	197,890	(10.2)	180,411	(1.5)
Total expenditure	156,965	171,155	(8.3)	164,784	(4.7)
EBITDA	20,724	26,735	(22.5)	15,627	32.6
EBITDA Margins (%)	11.7%	13.5%	-	8.7%	-
Depreciation	4,890	3,634	34.5	4,398	11.2
EBIT	15,834	23,101	(31.5)	11,229	41.0
Other Income	3,124	2,201	42.0	4,401	(29.0)
Interest	242	227	6.7	275	(12.1)
PBT	18,716	25,075	(25.4)	15,355	21.9
Tax	6,210	8,262	(24.8)	4,713	31.8
PAT	12,507	16,812	(25.6)	10,643	17.5
Reported PAT	12,507	16,812	(25.6)	10,643	17.5
Net Profit margins (%)	7.0%	8.5%	-	5.9%	-
Reported EPS	2.8	3.7	(25.6)	2.4	17.5

Source: Company, RSec Research

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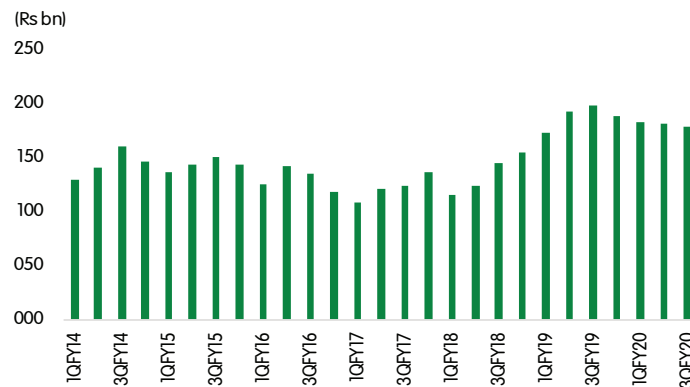
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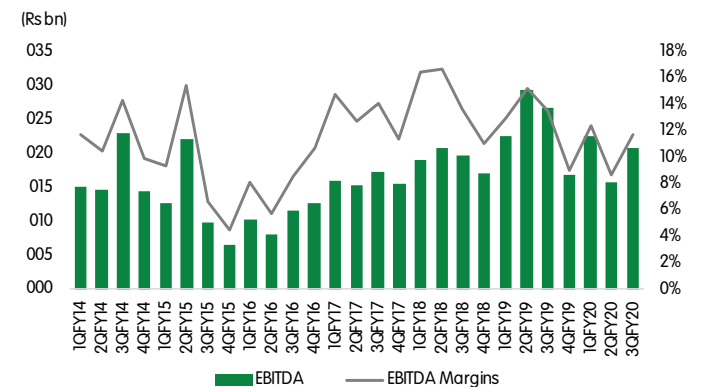
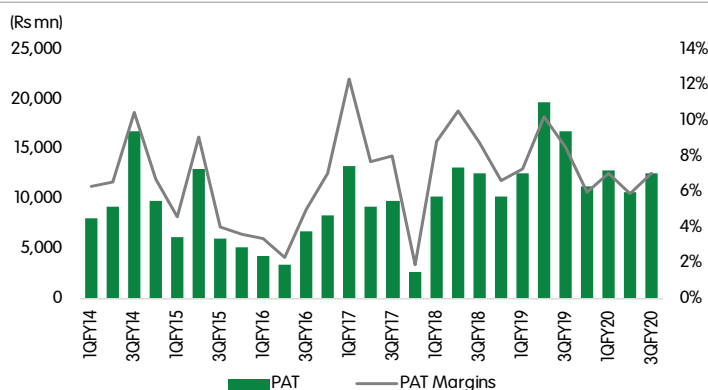
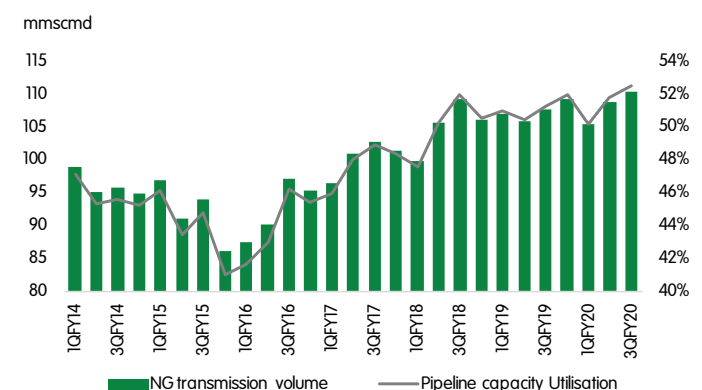
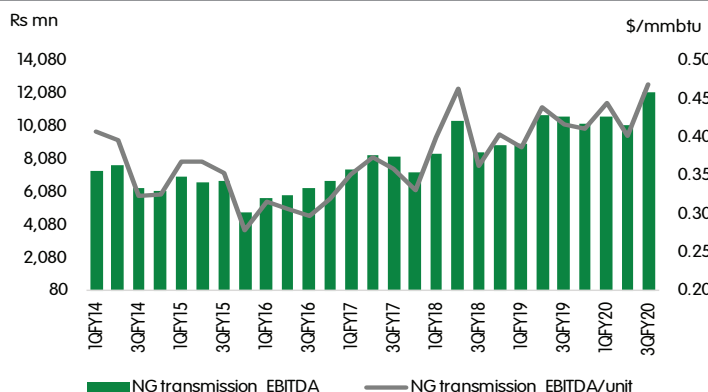
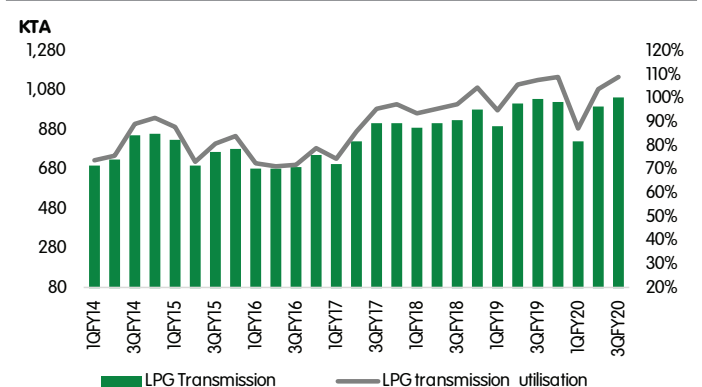
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Exhibit 1: GAIL's Quarterly Net sales


Source: Company, RSec Research

Exhibit 2: GAIL's Quarterly EBITDA & Margins

Exhibit 3: GAIL's Quarterly PAT & Margins

Exhibit 4: GAIL's Natural Gas transmission volume and pipeline capacity utilisation

Exhibit 5: GAIL's Natural Gas transmission EBITDA and Per unit EBITDA (\$/mmbtu)

Exhibit 6: GAIL's LPG transmission volume and utilisation


Source: Company, RSec Research

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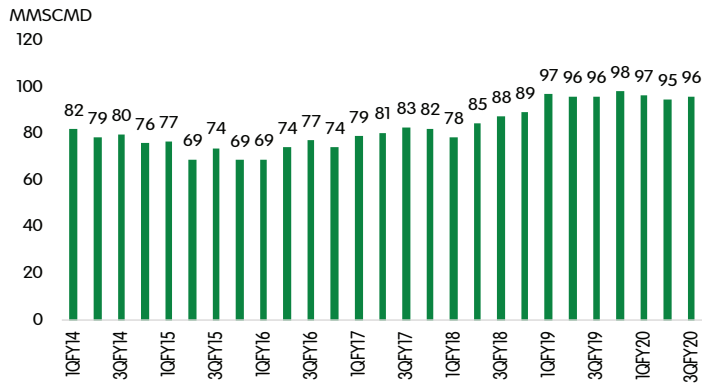
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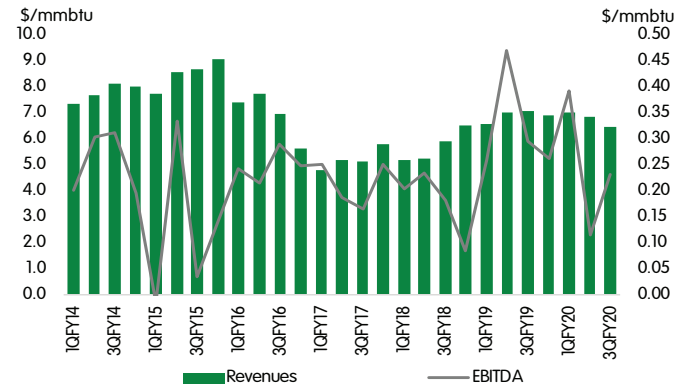
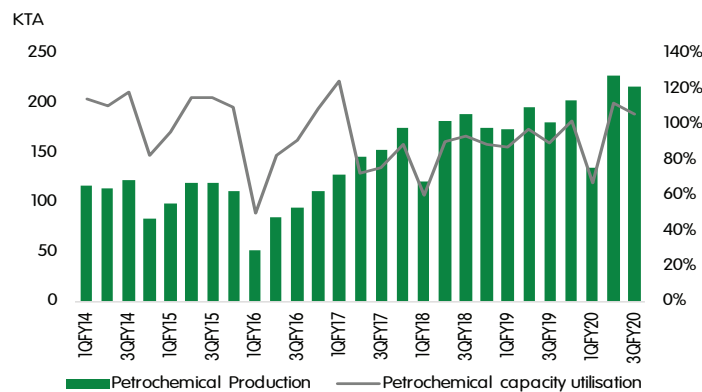
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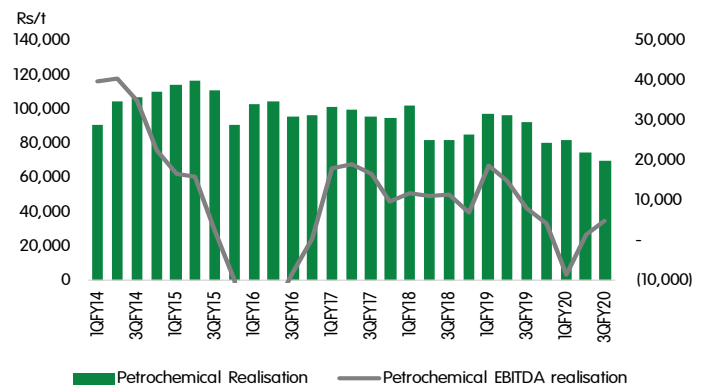
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Exhibit 7: GAIL's Gas Trading volume


Source: Company, RSec Research

Exhibit 8: GAIL's Gas trading revenue and EBITDA in per unit

Exhibit 9: GAIL's Petrochemical production volume and plant utilization


Source: Company, RSec Research

Exhibit 10: GAIL's Petrochemical revenue realisation and EBITDA realisation in per unit


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Profit & Loss account

Y/E Mar (Rs mn)	FY19	FY20E	FY21E	FY22E
Revenues	761,899	686,688	703,620	662,094
Expenses				
Cost of Materials Consumed	50,798	44,081	44,493	40,203
Purchases of stock-in-trade	548,080	475,604	480,052	433,764
(Inc)/Dec in inventories	(5,476)	-	-	-
Employee benefits expense	18,632	19,564	20,542	21,569
Other expenses	53,189	55,849	58,641	61,573
EBITDA	96,676	91,592	99,891	104,985
EBITDA margins	12.7%	13.3%	14.2%	15.9%
Growth (%)	24%	-5%	9%	5%
DDA	16,666	15,036	15,243	15,382
EBIT	80,009	76,555	84,648	89,603
Other income	12,143	8,210	10,347	10,687
Finance cost	1,592	1,657	1,728	3,013
PBT	90,560	83,109	93,268	97,277
Tax	32,784	20,777	23,317	24,319
PAT	57,776	62,332	69,951	72,958
Net Profit margins	7.6%	9.1%	9.9%	11.0%
Growth (%)	24.3%	7.9%	12.2%	4.3%
Group profit	65,528	68,322	78,783	82,057
EPS	12.8	13.8	15.5	16.2

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Balance sheet

Fig in Rs mn	FY19	FY20E	FY21E	FY22E
Shareholder's funds	460,501	505,226	554,440	604,672
Share capital	22,551	22,551	22,551	22,551
Reserves and surplus	437,490	482,216	531,430	581,662
Minority Interest	460	460	460	460
Non-current liabilities	116,973	111,973	112,123	112,273
LT borrowings	10,278	5,278	5,428	5,578
DTL (Net)	65,099	65,099	65,099	65,099
Other LT liabilities	25,645	25,645	25,645	25,645
LT provisions	15,952	15,952	15,952	15,952
Current liabilities	106,600	132,108	133,763	124,822
ST borrowings	10,429	10,429	10,429	10,429
Trade payables	38,761	40,760	41,351	38,158
Other current liabilities	49,860	73,368	74,432	68,685
ST provisions	7,551	7,551	7,551	7,551
Total Liabilities	684,074	749,307	800,326	841,767
Non current asset	573,588	611,842	649,888	704,506
Fixed assets	424,378	462,632	500,678	555,296
Non-current investments	106,257	106,257	106,257	106,257
LT loans and advances	18,464	18,464	18,464	18,464
Other non-current assets	24,488	24,488	24,488	24,488
Current assets	110,486	137,465	150,438	137,261
Inventories	25,026	19,565	19,849	18,316
Trade receivables	43,634	28,220	28,916	27,209
Cash and cash equivalents	14,251	62,106	74,098	64,161
ST loans and advances	8,240	8,240	8,240	8,240
Other current assets	19,335	19,335	19,335	19,335
Total Asset	684,074	749,307	800,326	841,767

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Cash Flow Statement

Y/E Mar (Rs mn)	FY19	FY20E	FY21E	FY22E
PBT before tax	98,312	89,157	102,158	106,434
DDA	16,666	15,036	15,243	15,382
Others	(9,084)	(6,048)	(8,890)	(9,157)
Receivables	(15,895)	15,414	(696)	1,707
Inventories	(5,704)	5,462	(284)	1,533
Trade payables and other liabilities	16,668	25,507	1,655	(8,941)
Direct taxes paid	(21,122)	(20,777)	(23,317)	(24,319)
Cash from operations	79,842	123,751	85,870	82,638
Purchase of fixed assets	(77,958)	(53,290)	(53,290)	(70,000)
others	8,812	-	-	-
Investing cash flow	(69,146)	(53,290)	(53,290)	(70,000)
Repayment of ST borrowings/ Net borrowing	(11,350)	(5,000)	150	150
Others	(10,213)	(17,606)	(20,737)	(22,726)
Cash flow from financing activities	(21,563)	(22,606)	(20,587)	(22,576)
Net inc/(dec) in cash & cash eq	(10,866)	47,855	11,993	(9,937)
Opening balance	13,773	2,967	50,821	62,814
Ending balance	2,906	50,821	62,814	52,877

Key Ratio

Y/E March	FY19	FY20E	FY21E	FY22E
Valuation Ratio (x)				
P/E	9.5	8.8	7.9	7.5
P/CEPS	5.4	3.8	5.0	0.0
P/BV	1.19	1.09	0.99	-
Dividend yield (%)	3.3%	3.2%	3.8%	4.1%
EV/Sales	0.81	0.90	0.88	0.93
EV/EBITDA	6.4	6.74	6.18	5.88
Per Share Data (Rs)				
EPS	12.8	13.8	15.5	16.2
Cash EPS	22.4	32.0	24.2	23.7
DPS	4.01	3.90	4.60	5.04
Book Value	102.1	112.0	122.9	134.1
Returns (%)				
RoCE	13.9%	12.4%	12.7%	12.5%
RoE	12.5%	12.3%	12.6%	12.1%
Turnover ratios (x)				
Asset Turnover (Gross Block)	1.11	0.92	0.88	0.79
Inventory / Sales (days)	15.25	13.74	13.81	14.11
Receivables (days)	21	15	15	15
Payables (days)	24	29	29	29

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Rating History

Date	Reco	CMP	TP
11-Nov-19	BUY	127	154
06-June-19	HOLD	317	336
29-May-19	BUY	349	386
15-Mar-19	BUY	353	388
28-Feb-19	BUY	336	382

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Rating Guides

Rating	Expected absolute returns (%) over 12 months
BUY	>10%
HOLD	-5% to 10%
REDUCE	>-5%

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