



Indian Equities
Oil & Gas

Quarterly Update

Gas Authority of India Ltd.

BUY

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CMP **Rs 371**
Target Price **Rs 422**
Sensex 16,158
Nifty 4,796

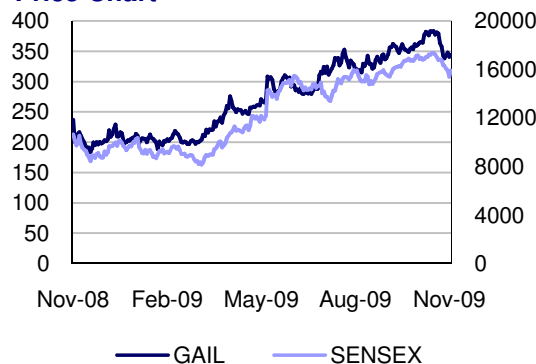
Stock Details

BSE Code	532155
NSE Code	GAIL
Reuters Code	GAIL.BO
Bloomberg Code	GAIL.IN
Market Cap (Rs Cr)	47047.92
Beta	0.70
52 W High / Low (Rs)	387.50 / 175.40
Avg Daily Volume	3,71,550
Face Value (Rs)	10

Shareholding Pattern (%)

Promoters	57.34
MF/Banks/Indian FIs	17.14
FII / NRIs / OCBs	15.29
Government	7.24
Non-Institutions	0.71
Indian Public	2.28

Price Chart



Performance Highlights

Increase in gas transmission volume: During Q2FY2010, natural gas transmission volume of Gas Authority of India Ltd. (GAIL) increased 30.4% yoy to 106.5mmscmd from 81.7mmscmd in Q2FY2009 leading to a 39.2% growth in gas transmission revenue to Rs 843.0cr. The volume increase was due to the increase in production from KG-D6 basin gas and higher volume of LNG at Dahej terminal. Although, the gas transmission revenue increased by 39.2%, due to lower revenues from the LGP segment, the net sales remained flat at Rs 6,202.2cr.

Higher subsidy burden dampens OPM by 700bps: In Q2FY2010, OPM declined by 700bps to 16.4% due to a 14.4% yoy increase in subsidy burden to Rs 458.54cr and increase in purchase of finished goods along with decline in EBIT margins of petrochemicals and LPG & liquid hydrocarbon.

Outlook and Valuation: At the current market price of Rs 371, GAIL is trading at P/E of 15.6x FY2010E earnings and 14.3x FY2011E earnings. On EV/EBIDTA basis, the stock is trading at 10.5x FY2010E and 9.9x FY2011E. Higher gas transmission volume due to increase in gas production of KG-D6 basin, higher volume from Dahej terminal and limited subsidy sharing is expected to improve GAIL's earnings. **Thus, we maintain our BUY recommendation on the stock with a target price of Rs 422.**

Exhibit 1: Quarterly Analysis

Particulars	Q2FY2010	Q2FY2009	YoY(%)	Q1FY2010	QoQ(%)
Net Sales	6202.2	6129.3	1.2	6021.4	3.0
Other Income	168.9	228.9	(26.2)	79.8	111.6
Total Income	6371.1	6358.2	0.2	6101.3	4.4
Total Expenditure	5184.9	4697.9	10.4	4955.9	4.6
EBIDTA	1017.3	1431.4	(28.9)	1065.5	(4.5)
EBIDTA Margin (%)	16.4	23.4	-	17.7	-
Interest	17.9	18.9	(5.6)	17.9	(0.4)
PBDT	1168.4	1641.4	(28.8)	1127.4	3.6
Depreciation	141.6	138.6	2.2	140.4	0.9
Profit before Tax	1026.8	1502.9	(31.7)	987.0	4.0
Tax	313.5	479.4	(34.6)	331.2	(5.3)
Profit After Tax	713.2	1023.5	(30.3)	655.8	8.8
PAT Margin (%)	11.5	16.7	-	10.9	-
EPS	5.62	8.07	(30.3)	5.17	8.8

Source: Company, Parsoli Research



Key Updates

Exhibit 2: Operational Performance

	Unit	Q2FY2010	Q2FY2009	YoY (%)	Q1FY2010	QoQ (%)
Natural Gas Transmission	mmscmd	106.5	81.7	30.4	96.7	10.2
LPG Transmission	tmt	728.0	650.0	12.0	741.0	(1.8)
Natural Gas Trading	mmscmd	81.1	79.1	2.5	79.9	1.4
Petrochemicals	tmt	88.0	75.0	17.3	92.0	(4.3)
LPG & Liquid Hydrocarbons	tmt	379.0	361.0	5.0	334.0	13.5

Source: Company, Parsoli Research

Higher transmission volume offsets fall in revenues from LPG & Liquid hydrocarbon

In Q2FY2010, GAIL's topline remained nearly flat at Rs 6,202.2cr due to decline in revenue from LPG & Liquid hydrocarbon segment

In Q2FY2010, GAIL reported marginal net sales growth of 1.2% yoy to Rs 6,202.2cr. Transmission volumes increased by 30.4% yoy to 106.5mmscmd on account of increased production of KG-D6 basin gas and higher volume of LNG from Petronet Dahej terminal. Despite the increase in gas transmission, the net sales of the company remained flat due to a decline in LPG & Liquid hydrocarbon revenue. LPG & Liquid hydrocarbon revenue declined 52.8% yoy to Rs 515.1cr. The volumes from the Petrochemical segment increased by 17.3% yoy to 88.0tmt but the revenue declined marginally to Rs 615.7cr on account of a 16.3% decline in price realization.

Exhibit 3: Segmental Revenue

	Q2FY2010	Q2FY2009	YoY (%)	Q1FY2010	QoQ (%)
Natural Gas Transmission	825.0	621.5	32.7	733.2	12.5
LPG Transmission	102.9	90.6	13.6	105.7	(2.6)
Natural Gas Trading	4969.1	4495.4	10.5	4641.7	7.1
Petrochemicals	615.7	628.7	(2.1)	622.6	(1.1)
LPG & Liquid Hydrocarbons	515.1	1090.2	(52.8)	683.9	(24.7)
Gailtel	3.4	6.5	(47.7)	3.8	(9.5)

Source: Company, Parsoli Research

OPM declines to 16.4%

The drop in performance was on the back of fall in EBIT margin of petrochemical and LPG and liquid hydrocarbon and higher subsidy burden

During Q2FY2010, GAIL reported 28.9% yoy decline in operating profit to Rs 1017.3cr with the operating margin declining by 700bps yoy to 16.4%. This drop in performance was on the back of a decline in EBIT margin of the Petrochemical and LPG & Liquid hydrocarbon segments. Petrochemical EBIT declined by 15.0% yoy to Rs 275.3cr in Q2FY2010. Although, the sales volume of petrochemical increased to



The subsidy burden for GAIL stood at Rs 458.5cr which was 14.4% higher than Q2FY2009

The cost of purchase of finished goods as a percentage of sales was 559bps higher to 64.7%

Other income for the company declined by 26.2% yoy to Rs 168.9cr

88.0tmt, however, the EBIT was impacted due to lower price realization. Petrochemical realizations stood at Rs 70.0/kg in Q1FY2010 as against Rs 83.6/kg in Q2FY2009. Due to LPG price fluctuations, LPG & Liquid hydrocarbon EBIT declined by 55.3% yoy leading to a loss of Rs 73.1cr. LPG & Liquid hydrocarbon realizations stood at Rs 13.6/kg in Q2FY2010 as against Rs 29.5/kg in Q2FY2009. Moreover, the cost of purchase of finished goods as percentage of sales was 559bps higher to 64.7%. Also, during the quarter, the subsidy burden for GAIL stood at Rs 458.5cr which was 14.4% higher as compared to Rs 400.8cr in Q2FY2009. This subsidy sharing mechanism was in continuation with the subsidy sharing mechanism in Q1FY2010 where the upstream share was limited to the auto fuel under recoveries only.

Exhibit 4: Cost Analysis **% of sales**

	Q2FY2010	Q2FY2009	bps	Q1FY2010	bps
Raw Materials Consumed	9.5	9.0	48.3	8.6	89.8
Stock Adjustment	0.2	(1.2)	141.7	0.6	(41.9)
Purchase of Goods	64.7	59.1	558.7	62.8	184.0
Employee cost	2.0	1.9	12.0	2.2	(14.7)
Other Expenditure	7.2	7.8	(65.6)	8.1	(87.9)
Total Expenditure	83.6	76.6	695.2	82.3	129.3

Source: Company, Parsoli Research

Exhibit 5: EBIT Margin **%**

	Q2FY2010	Q2FY2009	bps	Q1FY2010	bps
Natural Gas Transmission	74.6	63.6	1103.4	71.2	340.9
LPG Transmission	57.2	59.5	(230.0)	64.5	(729.9)
Natural Gas Trading	2.2	2.5	(25.4)	2.3	(6.6)
Petrochemicals	44.7	52.3	(757.2)	42.5	226.3
LPG & Liquid Hydrocarbons	(14.2)	52.8	(6694.5)	21.9	(3612.7)
Gailtel	(62.6)	(70.3)	776.3	(28.6)	(3400.2)

Source: Company, Parsoli Research

Lower other income further dampens the net profit by 30.3%

In Q2FY2010, GAIL's operating profit fell 28.9% yoy whereas PAT was down by 30.3% yoy. This was on an account of 26.2% yoy decline in other income to Rs 168.9cr. Thus, GAIL reported PAT of Rs 713.2cr.



GAIL's core business contributes 80.0% of the revenues

We maintain our BUY recommendation on the stock with a revised target price of Rs 422

Outlook and Valuation

With core business of transmission and trading of natural gas, GAIL is expected to grow at a rapid pace on the back of its capacity expansion plans and increase in natural gas production from KG-D6 basin. We expect GAIL to register growth at a CAGR of 18.3% in revenues and 8.1% in profit between FY2008 and FY2011E. The company is also investing in the E&P segment to secure gas supply for its LPG and petrochemical segments. Due to a weak demand of petrochemicals in the global market, the petrochemical segment of GAIL is expected to witness pressure on operating margin due to lower price realization. GAIL's core business contributes nearly 80.0% of the revenues. Going forward, we believe operating margin will gradually expand due to higher capacity utilization of the company's infrastructure as the gas supply has increased in the country.

GAIL is a diversified company with presence in natural gas/LPG transmission, petrochemicals/liquid hydrocarbons production, E&P and investments in various entities. We have valued the stock by using the sum-of-the-parts (SOTP) valuation methodology. At the current market price of Rs 371, GAIL is trading at P/E of 15.6x FY2010E earnings and 14.3x FY2011E earnings. On EV/EBIDTA basis, the stock is trading at 10.5x FY2010E and 9.9x FY2011E.

Exhibit 6: SOTP Valuation

Particulars	Fair Value (Rs)
Existing Business	375.8
Investments	46.4
Total Value	422.2

Source: Parsoli Research

GAIL's quarterly results were in line with our expectations and, going forward, with higher gas transmission volume due to increase in production from KG-D6 basin and Dahej terminal along with limited subsidy burden, we expect the company's earnings to improve in the long term. **Thus, we maintain our BUY recommendation on the stock with a target price of Rs 422.**



Financial Statements

Exhibit 7: Profit & Loss Statement					Rs cr
Particulars	FY2007	FY2008	FY2009E	FY2010E	FY2011E
Net Sales	16,047.2	18,008.2	23,776.0	26,612.6	29,844.1
<i>% chg</i>	11.0	12.2	32.0	11.9	12.1
Total Expenditure	13,132.8	14,110.6	19,716.3	21,694.2	24,165.1
<i>% chg</i>	2.6	7.4	39.7	10.0	11.4
EBIDTA	2,989.6	3,927.5	4,064.7	4,837.9	5,679.0
<i>Margin (%)</i>	18.6	21.8	17.1	18.2	19.0
Other Income	545.0	556.4	796.6	680.1	762.6
Depreciation & Amortization	575.4	571.0	559.9	690.2	931.7
Interest	107.1	79.6	87.0	343.3	600.0
PBT	3,199.7	3,855.0	4,204.0	4,484.5	4,909.9
<i>Margin (%)</i>	19.9	21.4	17.7	16.9	16.5
Total Tax	813.0	1,253.5	1,400.3	1,460.0	1,620.3
<i>(% of PBT)</i>	25.4	32.5	33.3	32.6	33.0
PAT	2,386.7	2,601.5	2,803.7	3,024.5	3,289.6
<i>% chg</i>	3.3	9.0	7.8	7.9	8.8
<i>Margin (%)</i>	14.9	14.4	11.8	11.4	11.0

Source: Company, Parsoli Research



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