

# GAIL

FEB 2016

GAIL											
Rating	Accumulate										
CMP	Rs 344										
Target Price	Rs 428										
Potential upside	24.60%										
<b>Shareholders</b>											
<table border="1"> <caption>Shareholders Data</caption> <thead> <tr> <th>Category</th> <th>Percentage</th> </tr> </thead> <tbody> <tr> <td>Promoters</td> <td>56%</td> </tr> <tr> <td>FII</td> <td>17%</td> </tr> <tr> <td>DII</td> <td>16%</td> </tr> <tr> <td>Public &amp; Other</td> <td>11%</td> </tr> </tbody> </table>		Category	Percentage	Promoters	56%	FII	17%	DII	16%	Public & Other	11%
Category	Percentage										
Promoters	56%										
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Public & Other	11%										
<b>Price performance</b>											
%	1m	3m	6m								
Absolute	-8	19	0								
Rel. to nifty	2	29	17								
<b>Stock details</b>											
Face value	10										
52 week H/L	418/260										
M cap	43603 cr										

- Operational in-line result, however beat came at PAT level on account of higher other income which grew by 83% qoq to Rs2.56bn (our est. Rs1.4bn) along with lower tax rate of 28%(our assumption 33%) compare to 34% in 1HFY16. EBITDA came in line with our est. at Rs11.5bn (our est. Rs11bn) and PAT came in at Rs 6.64bn (our est. Rs 4.7bn)

- Sequentially, transmission vol. grew by 8% to 97mmcmd and trading volume grew by 4.2% to 77mmcmd on back of higher offtake from standard power plant (~8mmcmd from 4.5mmcmd in previous qtr.). Gross trading margins has improved by 284bps qoq to 4.6% on account of correction in LNG prices which has been monetised by the company

- Due to stabilisation of Pata-2, petchem production has improved marginally by 10% qoq to 94k. However, company expect overall utilisation to improve in ensuing quarters as the technical problem has been solved during the quarter. Company has targeted ~120- 130kt/quarter production run rate in FY17E

- Outlook and Valuation: Post the benefits of Rasgas renegotiation, we expect turnaround in Petchem business. Moreover, post stabilization of Petchem plant, we expect gradual volume improvement which would add further to the earnings. Thus, we see almost double the earnings in FY17E to Rs28/share compare to FY16E. Also, other triggers are on card like 1) Upward pipeline Tariff revision and 2) correction in spot LNG price would improve the transmission and trading business earnings. We maintain our BUY reco with TP of Rs428. Currently stock trades at 12.1x FY17 EPS and 1.3x FY17 P/BV

## Key takeaways from GAIL's Q3 Concall

### On Transmission segment

Sequential improvement in volumes is mainly on the back of higher offtake from standard power plant (~8mmcmd from 4.5mmcmd in previous qtr.) and demand of spot LNG. Standard power plant volumes can go higher by ~3-4mmcmd from some AP and Maharashtra power plants which has not been off taking because of the pending issues on tax clarity from the government.

## Financial snapshot

Rs	FY14	FY15	FY16E	FY17E	FY18E
<b>Net sales</b>	575079	567420	541199	598485	599803
<b>EBITDA</b>	67011	46962	47831	67637	70720
<b>EBITDA Margin</b>	11.5	8.3	8.8	11.3	11.8
<b>APAT</b>	40302	29763	24330	35970	37572
<b>EPS</b>	31.8	23.5	19.2	28.4	29.6
<b>EPS %</b>	0.2	-26.2	-18.3	47.8	4.5
<b>ROE</b>	17.1	10.8	8.2	11.5	11.1
<b>P/E</b>	10	14.4	17.9	12.1	11.6
<b>EV/EBITDA</b>	7.6	9.4	10.5	6.8	6.3
<b>P/BV</b>	1.6	1.5	1.4	1.3	1.2

## Quarterly financial

Rs mn	Q3FY15	Q4FY15	Q1FY16	Q2FY16	Q3FY16	Yoyo%	QOQ%	9MFY16	9MFY15
<b>Revenue</b>	149694	142706	125653	141649	134516	-10.1	-5	401818	424714
<b>Expenditure</b>	139837	136272	115214	133205	122953	-12.1	-7.7	371373	384186
<b>as % of sales</b>	93.40%	95.50%	91.7	94	91.4		92.4	90.5	
<b>Consumption of RM</b>	126032	108711	103179	117748	108692	-13.8	-7.7	329619	345225
<b>as % of sales</b>	84.2	76.20%	82.1	83.1	80.8		82	81.3	
<b>Employee cost</b>	2.442	20.22	2482	2578	2630	7.7	2	7690	7042
<b>as % of sales</b>	1.6	1.4	2	1.8	2		1.9	1.7	
<b>other expenditure</b>	11362	25539	9553	12879	11632	2.4	-9.7	34064	31918
<b>as % of sales</b>	7.6	17.9	7.6	9.1	8.6		8.5	7.5	
<b>EBITDA</b>	9857	6434	10439	8444	11562	17.3	36.9	30445	40528
<b>Depreciation</b>	2510	2528	3077	3227	3330		3.2	9634	7214
<b>EBIT</b>	7347	3906	7361	5217		12.1	57.8	32.6	33314
<b>Other income</b>	1403	2593	786	3018	2569	83.1	-14.9	6372	8233
<b>Interest</b>	851	914	1636	1635	1583	86.1	-3.2	4854	2699
<b>PBT</b>	7899	5585	6511	6599	9218	16.7	39.7	22329	36630
<b>Total tax</b>	2487	477	2270	2194	2576	3.6	17.4	7040	11975
<b>Adjusted PAT</b>	5412	5108	4241	4405	6643	22.7	50.8	15289	24656
<b>APAT After MI</b>	5412	5108	4241	4405	6643	22.7	50.8	15289	24656
<b>Extra ordinary items</b>	-629	0	0					-629	
<b>Reported PAT</b>	6041	5108	4241	4405	6643	10	50.8	15289	25284
<b>Reported EPS</b>	4.8	4	3.3	3.5	5.2	10.1	51	12.1	19.9

Margins%										
EBITDA	6.6	4.5	8.3	6	8.6	30.5	44.2	7.6	9.5	
EBIT	4.9	2.7	5.9	3.7	6.1	24.7	66.2	5.2	7.8	
EBT	5.3	3.9	5.2	4.7	6.9	29.9	47.1	5.6	8.6	
PAT	3.6	3.6	3.4	3.1	4.9	36.6	58.8	3.8	5.8	
Effective tax rate	31.5	8.5	34.9	33.2	27.9	-11.2	-16	31.5	32.7	-116.1

### On Trading Segment

Trading margins has improved on account of correction in LNG prices which has been monetised by the company. While trading volumes were higher on account of higher off take from standard power plant and higher spot LNG demand from Fertiliser and Power plants.

### On Petchem segment

Due to stabilization of Pata-2 expansion Petchem production has improved marginally. However, company expects overall utilization to improve in ensuing quarters as the technical problem has been solved during the quarter. Company has targeted ~120-130kt per quarter production run rate in FY17E. During the quarter company has used spot LNG instead of RasGas volumes as a feed stock resulting in reduction in losses. However, as a customer company has signed its revised RasGas contract with its Petchem plant which it will going to utilise in ensuing quarters.

### On LPG segment

Improvement in margins were mainly on the back of reduction in APM gas price and higher volumes.

### Other Details

- Long term price of LNG currently at \$7.5/mmbtu,.
- During the quarter company has received 21 cargoes which comprises of 12 at Dahej and 9 at Dabhol
- Capex Guidance for FY17 at Rs15bn. For FY18/19 Rs40bn each with majority on transmission projects like KMBL pipeline,.
- Cash & Cash equi. at Rs8.5bn, Current Trade Receivable stood at Rs31bn and Long term receivable Rs10.5bn.
- Company has received Rs1bn consideration for transferring lakwa LPG recovery Unit to BCPL. However, It has not booked during the current quarter. Out of 8.5mntpa LNG of Ras Gas volume, companies share of volumes i.e. 4.8mntpa has already contracted by the company.

### Segmental highlights

- Transmission segment:- Transmission revenue declined by 9.7% qoq to Rs9bn during the quarter despite of 8% sequential improvement in transmission volume to 97mmscmd as transmission tariff fell by 16% qoq to Rs1.01/scm. Transmission segment volume increased mainly on the back of higher offtake from standard power plants (~8mmscmd from 4.5mmscmd in previous qtr.) and demand of spot LNG while transmission tariff declined as company has to give 50% discount for stranded power plant volumes.
- NG Trading segment:- NG trading trading volume increased by 4.2% sequentially to 77mmscmd due to higher offtake from standard power plants. Gross margin increased by 284bps qoq to 4.6% on account of correction in LNG prices which has been monetised by the company. LPG & OLHC Segment:- LPG and

LHC realization fell by 5.7% qoq to \$426/tonne due to correction in LPG prices. While EBITDA margin in LPG & LHC improved from 11.6% to 29.8% qoq mainly on the back of reduction in APM gas price and higher volumes. LPG volume increased by 15.3% qoq to 0.294mnt. .

- LPG transmission:- LPG transmission volume grew by 0.7% qoq to 0.692mnt while ♣ margin declined by 322bps qoq to 60.2%. Petchem segment:- Reported loss at operating level, however losses has reduced from ♣ Rs1.43bn in Q2FY16 to Rs0.66bn for the quarter as company has used spot LNG instead of RasGas volumes as a feed stock.

### Outlook and Valuation:

Post the benefits of Rasgas renegotiation; we expect turnaround in Petchem business. Moreover, post stabilization of Petchem plant, we expect gradual volume improvement which would add further to the earnings. Thus, we see almost double the earnings in FY17E to Rs28/share compare to FY16E. Also, other triggers are on card like 1) Upward pipeline Tariff revision and 2) correction in spot LNG price would improves the transmission and trading business earnings. We maintain our BUY reco with TP of Rs428. Currently stock trades at 12.1x FY17 EPS and 1.3x FY17 P/BV.

- FCF during the quarter was GBP 454 mn (vs. -GBP 29 mnYoY/ -GBP 225 mnQoQ) owing to favorable working capital (dispatches of newly launched XE, XF)

### India

- EBITDA margin for the standalone business at +4.6% (vs. -6.2% YoY/+5.8% QoQ) missed our estimate of 5%. Hence EBITDA at Rs 4.6 bn missed our estimate by 11%
- CV volume outlook on Indian trucks/cars is positive with HCVs seeing revival and should post healthy growth in FY17E as well (driven by replacement demand). The company now expects LCVs to post recovery and plans to refresh its existing product portfolio
- Cars: The company launched four new products in the Auto Expo 2016 – namely Zica (hatchback), Kite 5 (compact sedan), Nexon (compact UV) and Hexa (SUV). Management indicated it has received strong response for its launches and would help gain market share
- Discounts: Management indicated that discounts still remain high in the system and have nearly doubled from FY10-11 levels

### Segmental performance

Net sales	Q3FY15	Q4FY15	Q1FY16	Q2FY16	Q3FY16	Yoyo%	QOQ%Chg
<b>Natural gas transmission</b>	9180	8540	8610	9990	9020	-1.7	-9.7
<b>LPG Transmission</b>		1070	1240	1360	1120	1130	5.6
<b>Natural gas trading</b>		114620	108640	99020	112030	106020	-7.5
<b>Petrochemical</b>		11960	11660	5070	7960	7290	-39
<b>LPG and other LHC</b>		10540	10350	9290	7480	8260	-21.6
<b>Physical performance</b>							
<b>Natural gas transmission mmscm</b>	8656	7754	7917	8280	8932	3.2	7.9
<b>Natural gas trading mmscm</b>	6815	6183	6279	6808	7095	4.1	4.2

Petrochemical mmt	0.1	0.1	0.1	0.1	0.1	-25	0
LPG and other LHC mmt	0.3	0.3	0.3	0.3	0.3	-10.9	15.3
<b>Realisation per unit</b>							
Natural gas transmission Rs/scm	1.1	1.1	1.1	1.2	1	-4.8	-16.3
LPG Transmission Rs/ton	1384	1574	1974	1630	1633	18	0.2
Natural gas trading Rs/scm	16.8	17.6	15.8	16.5	14.9	-11.1	-9.2
petrochemical Rs/ton	106786	88333	101400	94762	86786	-18.7	-8.4
LPG and other LHC rs/ton	31939	34158	33417	29333	28095	-12	-4.2
Petchem\$/ton		1722	1419	1597	1460	1317	-23.5
LPG \$/tone		515	549	526	452	426	-17.2

<b>Opex</b>							
Natural gas transmission Rs mn	2360	3670	2850	2300	2730	15.7	18.7
LPG Transmission Rs mn	380	380	420	410	450	18.4	9.8
Natural gas trading Rs mn	114090	106680	95560	110070	101150	-11.3	-8.1
Petrochemical Rs mn	11680	12960	7170	9390	7950	-31.9	-15.3
LPG and other LHC	7980	7380	6400	6610	5800	-27.3	-12.3
Petchem \$/tone	1682	1577	2258	1722	1436	-14.6	-16.6
<b>Gross margin</b>							
Natural gas transmission	6820	4870	5760	7690	6290	-7.8	-18.2
LPG Transmission	690	860	940	710	680	-1.4	-4.2
LPG Transmission	530	1960	3460	1960	4870	818.9	148.5
Natural gas trading	280	-1300	-2100	-1430	-660	-335.7	-53.8
Petrochemical	2560	2970	2890	870	2460	-3.9	182.8
LPG and other LHC							
<b>EBITDA/Gross margin</b>							
Natural gas transmission	74.3	57	66.9	77	69.7	-456	-724
LPG Transmission	64.5	69.4	69.1	63.4	60.2	-431	-322
Natural gas trading mmscmd	0.5	1.8	3.5	1.7	4.6	413	284
petrochemical	2.3	-11.1	-41.4	-18	-9.1	-1139	891
LPG and other LHC	24.3	28.7	31.1	11.6	29.8	549	1815
<b>Key financials</b>							
<b>Income statement</b>							

Y/E Mar	FY14	FY15	FY16E	FY17E	FY18E
Net sales	575079	567420	541199	598485	599803
Expenditure	514337	518136	497201	530847	529084
EBITDA	67011	46962	47831	67637	70720
Depreciation	11762	9743	12930	14317	15357
EBIT	55249	37219	34901	53320	55363
Other income	8985	8609	8134	7607	8126
Interest expenses	3662	3613	6540	6999	7159
PBT	60573	42215	36495	53928	56331
Tax	20271	12452	12164	17958	18758
Extraordinary items	3450	629	0	0	0
Minority int/income from assoc	0	0	0	0	0
Reported net income	43752	30392	24330	35970	37572
Adjusted PAT	40302	29763	24330	35970	37572

## Balance sheet

Y/E Mar	FY14	FY15	FY16E	FY17E	FY18E
Equity share capital	12685	12685	12685	12685	12685
Reserves and surplus	258039	278511	289929	312988	337648
Net worth	270723	291195	302614	325672	350333
Minority interest	0	0	0	0	0
Loan funds	95261	80483	85483	87483	89483
Net deferred tax liability	25664	33087	33087	33087	33087
Total liabilities	391648	404765	421183	446242	472902
Net block	214767	277597	288667	295350	300993
Investment	41030	43224	43224	43224	43224
current assets	145039	164512	165051	187762	205185
cash and bank balance	26510	11416	15384	23499	39456
Other current assets	7366	31764	30296	33503	33576
current liabilities and provision	106465	124168	120359	128694	129099
Net current assets	38573	40344	44692	59068	76085
Misc.exp	0	0	0	0	0
Total assets	391648	404765	421183	446242	472902

Cash flow					
Y/E Mar	FY14	FY15	FY16E	FY17E	FY18E
PBT Ex other income	64023	42844	36495	53928	56331
Other non cash items	-9789	-3745	0	0	0
Chg in working cap	-8171	-19567	-381	-6261	-1061
Operating cash flow	44729	24993	43420	51025	59027
Capital expenditure	-383550	-18676	-25000	-25000	-25000
free cash flow	6179	6317	18420	26025	34027
investments	-3725	-337	0	0	0
other investing cash flow	9958	8816	0	0	0
investing cashflow	-32317	-10197	-25000	-25000	-25000
Equity capital raised	0	0	0	0	0
Loans taken /repaid	12043	-9113	5000	2000	2000
Dividend paid	-14991	-13321	-12912	-12912	-12912
other financing cash flow	0	0	0	0	0
financing cash flow	-9481	-29890	-14452	-17910	-18070
net chg in cash	2930	-15093	3968	8115	15956
opening cash position	23579	26510	11416	15384	23499
closing cash position	26510	11416	15384	23499	39456

key ratios					
Profitability	FY14	FY15	FY16E	FY17E	FY18E
EBITDA Margin	10.6	8.7	8.1	11.3	11.8
EBIT Margin	9.5	6.6	6.4	8.9	9.2
Effective tax rate	33.5	29.5	33.3	33.3	33.3
Net margin	7.6	5.3	4.5	6	6.3
ROCE	17.3	11.5	10.4	14	13.8
ROE	17.1	10.6	8.2	11.5	11.1
ROIC	23	14.8	9.9	16.4	16.6
Per share data	FY14	FY15	FY16E	FY17E	FY18E
EPS	34.5	23.5	19.2	28.4	29.6
CEPS	43.8	31.6	29.4	39.6	41.7
BVPS	213.4	229.6	238.6	256.7	276.2

DPS	10.4	6	8.7	8.7	8.7
<b>Valuations</b>	FY14	FY15	FY16E	FY17E	FY18E
PER	10	14.6	17.9	12.1	11.6
P/CEPS	7.9	11	11.7	8.7	8.2
P/BV	1.6	1.5	1.4	1.3	1.2
EV/Sales	0.8	0.8	0.9	0.8	0.7
EV/EBITDA	7.6	9.4	10.5	6.8	6.3
Dividend yield%	3	1.7	2.5	2.5	2.5
<b>Gearing ratio</b>	FY14	FY15	FY16E	FY17E	FY18E
Net debt/equity	0.1	0.1	0.1	0.1	0
Net debt/ebitda	0.4	0.6	0.6	0.3	0.1
Workgin cap cycle	7.6	18.7	19.6	21.7	22.3
<b>Growth%</b>	FY14	FY15	FY16E	FY17E	FY18E
Revenue	21.1	-1.3	-4.6	10.6	0.2
EBITDA	2.5	-29.9	1.9	41.4	4.6
EBIT	-0.5	-32.6	-6.2	52.8	3.8
PAT	8.8	-30.5	-19.9	47.8	4.5
<b>Quarterly</b>	Q3FY15	Q4FY15	Q1FY16	Q2FY16	Q3FY16
Revenue	149694	142706	125653	141649	134516
EBITDA	9857	6434	10439	8444	11562
EBITDA Margin%	6.6	4.5	8.3	6	8.6
PAT	6041	5108	4241	4405	6643
EPS	4.8	4	3.3	3.1	5.2
<b>Shareholding pattern%</b>	14-Dec	15-Mar	15-Jun	15-Sep	15-Dec
Promoters	56.1	56.1	56.1	56.1	56.1
FII's	19.8	18.8	18.6	16.4	16.5
DII's	13	14.2	14.5	16.6	16.6
Public and others	11.2	10.9	10.7	10.9	10.8