

# GAIL (India)

BSE SENSEX	S&P CNX	CMP: INR363	TP: INR385	Neutral
18,625	5,664			
Bloomberg	GAIL IN			
Equity Shares (m)	1,268.5			
52-Week Range (INR)	445/303			
1,6,12 Rel. Perf. (%)	-6/2/-23			
M.Cap. (INR b)	460.5			
M.Cap. (USD b)	8.6			

\*Adjustment for investments

- GAIL India's 2QFY13 EBITDA was in-line at INR13.8b, down 16% YoY and 27% QoQ. PAT declined 10% YoY and 13% QoQ to INR9.9b, higher than our estimate of INR8.4b due to (1) higher other income at INR2.7b (our estimate: INR1b), which includes INR1.9b of dividend income, (2) lower interest outgo at INR261m (our estimate: INR590m), led by capitalization of additional interest cost on account of forex rate change as per government circular, and (3) lower tax rate at 28%, as dividend income does not entail tax.
- Subsidy payout at INR7.9b (in-line) is provisional. As the government finalizes the subsidy towards the year-end, we expect higher subsidy in 2H. Comparable subsidy sharing was INR5.7b in 2QFY12 and INR7b in 1QFY13.
- Overall reported segmental EBIT (before subsidy) was INR21b, largely in line with our estimate of INR20b. Adjusted for revenue de-recognition in LPG transmission, the numbers were above estimates. Volume numbers were weaker than expected in transmission as well as petchem.
  - Despite lower transmission volumes at 106mmscmd (our estimate: 109mmscmd), EBIT was above estimate at INR6b, as gas volumes flowed through higher tariff pipelines, as indicated by the management.
  - LPG transmission EBIT was a negative INR489m due to de-recognition of INR1.2b revenue on account of tariff reduction by PNGRB.
  - Natural gas trading EBIT was INR2.5b, down 15% YoY and 51% QoQ. The sharp QoQ drop was due to one-time gain of INR2b in 1QFY13.
  - Petchem EBIT at INR4.2b (+114% QoQ) was boosted by higher volumes (+53% QoQ) and lower QoQ opex. 1QFY13 opex was higher due to capacity shutdown.
  - LPG & liquid hydrocarbon segment realizations were higher at USD776/MT v/s benchmark realizations of USD703/MT, resulting in EBIT of INR8.5b (v/s our estimate of INR6.9b).
- Adjusted for investments, the stock trades at 8.9x FY14E EPS of INR31.9. Our SOTP-based fair value stands at INR385/share.

Quarterly Performance											(INR Million)	
Y/E March	FY12				FY13				FY12	FY13E	FY13	Var. vs
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE			2QE	Est
Net Sales	88,674	96,990	112,598	104,546	110,886	113,612	113,255	112,124	402,807	449,878	111,932	1.5%
Change (%)	25.0	19.7	34.6	17.6	25.0	17.1	0.6	7.2	24.1	11.7	15.4	
EBITDA	15,556	16,482	17,605	7,338	18,991	13,803	16,768	15,730	56,981	65,293	13,935	-0.9%
% of Net Sales	17.5	17.0	15.6	7.0	17.1	12.1	14.8	14.0	14.1	14.5	12.4	
Change (%)	8.4	15.0	33.9	-42.3	22.1	-16.3	-4.8	114.4	4.5	14.6	-15.5	
Depreciation	1,782	2,008	1,975	2,143	2,169	2,491	2,540	2,670	7,907	9,870	2,185	
Interest	208	226	207	523	588	261	419	502	1,165	1,770	590	
Other Income	863	1,434	557	2,637	612	2,685	550	456	5,491	4,302	1,008	
PBT	14,429	15,682	15,980	7,309	16,846	13,736	14,359	13,013	53,400	57,955	12,168	12.9%
Tax	4,582	4,738	5,066	2,476	5,508	3,882	4,687	4,314	16,862	18,392	3,804	
Rate (%)	31.8	30.2	31.7	33.9	32.7	28.3	32.6	33.1	31.6	31.7	31.3	
PAT	9,847	10,944	10,914	4,833	11,338	9,854	9,672	8,700	36,538	39,563	8,364	17.8%
Change (%)	11.0	18.5	12.8	-38.3	15.1	-10.0	-11.4	80.0	2.6	8.3	-23.6	
Extraord.: Tax Prov. Write Back	0	0	0	-1,223	0	0	0	0	-1,223	0	0	
Adj PAT	9,847	10,944	10,914	4,833	11,338	9,854	9,672	8,698	36,538	39,563	8,364	17.8%
Adj. EPS	7.8	8.6	8.6	3.8	8.9	7.8	7.6	6.9	28.8	31.2	6.6	17.8%

E: MOSL Estimates

Harshad Borawake (HarshadBorawake@MotilalOswal.com); +91 22 3982 5432

1

## GAIL: segment-wise performance (INR m)

	FY12				FY13		2QFY13 (%)	
	1Q	2Q	3Q	4Q	1Q	2Q	YoY	QoQ
Exchange Rate (INR/USD)	44.7	45.8	51.0	50.2	54.2	55.5	21.2	2.4
<b>Gas Transmission Business</b>								
Volumes (mmscmd)	117	119	119	116	110	106	-11.3	-3.8
Gross Revenues	9,389	9,800	10,872	8,463	9,152	9,845	0.5	7.6
Opex	1,839	3,010	3,502	3,913	2,242	2,245	-25.4	0.1
<b>EBITDA</b>	<b>7,550</b>	<b>6,790</b>	<b>7,370</b>	<b>4,550</b>	<b>6,910</b>	<b>7,600</b>	<b>11.9</b>	<b>10.0</b>
Depreciation	1,030	1,228	1,162	1,302	1,237	1,551	26.4	25.4
<b>EBIT</b>	<b>6,520</b>	<b>5,562</b>	<b>6,208</b>	<b>3,248</b>	<b>5,673</b>	<b>6,049</b>	<b>8.7</b>	<b>6.6</b>
Average tariff (INR/mscm)	881	895	993	804	916	1,013	13.2	10.7
Opex (INR/mscm)	173	275	320	372	224	231	-15.9	3.0
EBITDA (INR/mscm)	708	620	673	432	691	782	26.1	13.1
Depreciation (INR/mscm)	97	112	106	124	124	160	42.4	29.0
EBIT (INR/mscm)	612	508	567	309	568	623	22.5	9.7
<b>LPG Transmission Business</b>								
Volumes ('000 MT)	817	796	870	879	845	813	2.1	-3.8
Gross Revenues	1,142	1,098	1,216	1,086	1,136	-40	-103.6	-103.5
Opex	332	258	316	406	296	310	20.2	4.8
<b>EBITDA</b>	<b>810</b>	<b>840</b>	<b>900</b>	<b>680</b>	<b>840</b>	<b>-350</b>	<b>-141.7</b>	<b>-141.7</b>
Depreciation	120	118	125	147	131	139	18.2	6.6
<b>EBIT</b>	<b>690</b>	<b>722</b>	<b>775</b>	<b>533</b>	<b>709</b>	<b>-489</b>	<b>-167.7</b>	<b>-169.0</b>
Average tariff (INR/MT)	1,398	1,380	1,397	1,235	1,344	-49	-103.5	-103.6
Opex (INR/MT)	406	324	363	462	350	382	17.7	9.0
EBITDA (INR/MT)	991	1,055	1,034	774	994	-431	-140.8	-143.3
Depreciation (INR/MT)	147	148	143	167	155	171	15.7	10.8
EBIT (INR/MT)	844	907	891	606	840	-602	-166.3	-171.7
<b>GAS Trading Business</b>								
Volumes (mmscmd)	83	84	85	85	83	81	-3.9	-2.9
Revenues	72,054	75,754	91,495	91,213	92,421	96,970	28.0	4.9
<b>EBIT</b>	<b>3,131</b>	<b>2,866</b>	<b>3,230</b>	<b>1,659</b>	<b>4,956</b>	<b>2,447</b>	<b>-14.6</b>	<b>-50.6</b>
Revenues (INR/mscm)	9,583	9,803	11,700	11,727	12,214	13,061	33.2	6.9
EBIT (INR/mscm)	416	371	413	213	655	330	-11.1	-49.7
<b>Petrochemicals Business</b>								
Volumes ('000 MT)	88	129	113	118	66	101	-21.7	53.0
Gross Revenues	6,369	9,376	8,780	9,629	5,741	8,798	-6.2	53.2
Opex	3,509	4,906	4,480	4,869	3,341	4,158	-15.2	24.5
<b>EBITDA</b>	<b>2,860</b>	<b>4,470</b>	<b>4,300</b>	<b>4,760</b>	<b>2,400</b>	<b>4,640</b>	<b>3.8</b>	<b>93.3</b>
Depreciation	426	430	426	451	442	458	6.7	3.7
<b>EBIT</b>	<b>2,434</b>	<b>4,041</b>	<b>3,875</b>	<b>4,309</b>	<b>1,958</b>	<b>4,182</b>	<b>3.5</b>	<b>113.6</b>
Realization (USD/MT)	1,618	1,588	1,523	1,627	1,605	1,570	-1.1	-2.2
Realization (INR/kg)	72	73	78	82	87	87	19.8	0.1
Opex (INR/kg)	40	38	40	41	51	41	8.3	-18.7
EBITDA (INR/kg)	33	35	38	40	36	46	32.6	26.3
Depreciation (INR/kg)	5	3	4	4	7	5	36.3	-32.2
EBIT (INR/kg)	28	31	34	37	30	41	32.2	39.6
<b>LPG &amp; Liquid Hydrocarbons Business</b>								
Volumes ('000 MT)	349	378	361	351	322	361	-4.5	12.1
Gross Revenues	14,958	15,553	15,016	17,203	17,723	15,551	0.0	-12.3
Opex	5,628	6,137	6,374	6,263	6,133	6,815	11.0	11.1
<b>EBITDA</b>	<b>9,329</b>	<b>9,416</b>	<b>8,641</b>	<b>10,940</b>	<b>11,590</b>	<b>8,737</b>	<b>-7.2</b>	<b>-24.6</b>
Depreciation	225	229	225	277	217	215	-5.8	-0.9
<b>EBIT</b>	<b>9,104</b>	<b>9,187</b>	<b>8,416</b>	<b>10,663</b>	<b>11,373</b>	<b>8,521</b>	<b>-7.2</b>	<b>-25.1</b>
Subsidy	6,819	5,666	5,361	13,980	7,000	7,857	38.7	12.2
<b>EBIT (Post-Subsidy)</b>	<b>2,285</b>	<b>3,521</b>	<b>3,055</b>	<b>-3,317</b>	<b>4,373</b>	<b>665</b>	<b>-81.1</b>	<b>-84.8</b>
Realization (USD/MT)	958	898	816	977	1,015	776	-13.6	-23.5
Realization (INR/MT)	42,858	41,146	41,594	49,010	55,041	43,079	4.7	-21.7
Opex (INR/MT)	16,127	16,236	17,658	17,842	19,047	18,877	16.3	-0.9
EBITDA (INR/MT)	26,731	24,910	23,937	31,168	35,994	24,201	-2.8	-32.8
Depreciation (INR/MT)	644	605	624	789	675	597	-1.4	-11.6
EBIT (INR/MT)	26,087	24,305	23,313	30,379	35,319	23,605	-2.9	-33.2
Subsidy (INR/MT)	19,539	14,989	14,851	39,829	21,739	21,764	45.2	0.1
EBIT post Subsidy (INR/MT)	6,548	9,316	8,462	-9,450	13,580	1,841	-80.2	-86.4

Source: Company, MOSL

### Key takeaways from 2QFY13 results concall

- **Capex:** 1HFY13 capex stood at INR27.7b and full-year FY13 capex is expected to be INR70b. Capitalization in 1HFY13 was INR16b and is expected at INR34b in FY13.
- **Petchem projects:** The management expects to commission Brahmaputra Cracker and Polymer Limited (GAIL stake: 70%) by December 2013 and Pata expansion by February 2014.
- **Dabhol LNG terminal to operate at 1.2mmt in year-1:**
  - The management has toned down its throughput expectations at Dabhol LNG terminal (GAIL stake: 32.9%) to 1.2mmt (v/s 2.2mmt earlier). However, it has indicated that the revised guidance is conservative (as Dabhol equipment is 10 years old) and that it will strive to reach 2.2mmt.
  - The breakwater contract is likely to be issued in the next few months (post high court ruling on case by RDS Projects Limited) and the company will try to complete the project within two years (likely by 2HCY15).
  - The re-gas charges at Dabhol terminal are likely to be ~INR40/mmbtu.

### Segment-wise revenue break-up (INR b)

	FY12				FY13		2QFY13 (%)	
	1Q	2Q	3Q	4Q	1Q	2Q	YoY	QoQ
A. Gas transmission	9.4	9.8	10.9	8.5	9.2	9.8	0.5	7.6
B. LPG Transmission	1.1	1.1	1.2	1.1	1.1	0.0	-103.6	-103.5
C. Natural Gas Trading	72.1	75.8	91.5	91.2	92.4	97.0	28.0	4.9
D. Petrochemicals	6.4	9.4	8.8	9.6	5.7	8.8	-6.2	53.2
E. LPG & Liq. HC (pre-subsidy)	15.0	15.6	15.0	17.2	17.7	15.6	0.0	-12.3
F. GAILTEL & unallocated	0.2	0.3	0.3	0.4	0.6	0.8	194.7	35.3
<b>Sub-total</b>	<b>104.1</b>	<b>111.8</b>	<b>127.7</b>	<b>128.0</b>	<b>126.7</b>	<b>131.9</b>	<b>17.9</b>	<b>4.1</b>
G. Less: Subsidy	6.8	5.7	5.4	14.0	7.0	7.9	38.7	12.2
<b>Segmental total</b>	<b>97.3</b>	<b>106.2</b>	<b>122.4</b>	<b>114.0</b>	<b>119.7</b>	<b>124.0</b>	<b>16.8</b>	<b>3.6</b>
Less: Intersegment	8.6	9.2	9.8	9.5	8.8	10.4	13.4	17.7
<b>Net Sales</b>	<b>88.7</b>	<b>97.0</b>	<b>112.6</b>	<b>104.5</b>	<b>110.9</b>	<b>113.6</b>	<b>17.1</b>	<b>2.5</b>

### Segmental EBIT Break-up (INRb)

	FY12				FY13		2QFY13 (%)	
	1Q	2Q	3Q	4Q	1Q	2Q	YoY	QoQ
A. Gas transmission	6.5	5.6	6.2	3.2	5.7	6.0	8.7	6.6
B. LPG Transmission	0.7	0.7	0.8	0.5	0.7	-0.5	nm	nm
C. Natural Gas Trading	3.1	2.9	3.2	1.7	5.0	2.4	-14.6	-50.6
D. Petrochemicals	2.4	4.0	3.9	4.3	2.0	4.2	3.5	113.6
E. LPG & Liq. HC (pre-subsidy)	9.1	9.2	8.4	10.7	11.4	8.5	-7.2	-25.1
F. GAILTEL & unallocated	-0.3	-0.8	-0.4	-0.4	0.1	0.1	nm	-14.2
<b>Total</b>	<b>21.5</b>	<b>21.6</b>	<b>22.1</b>	<b>20.0</b>	<b>24.8</b>	<b>20.8</b>	<b>-3.6</b>	<b>-16.0</b>
G. Less: Subsidy	6.8	5.7	5.4	14.0	7.0	7.9	38.7	12.2
<b>Reported EBIT</b>	<b>14.7</b>	<b>15.9</b>	<b>16.7</b>	<b>6.1</b>	<b>17.8</b>	<b>12.9</b>	<b>-18.7</b>	<b>-27.2</b>

### Operational Highlights ('000 tons)

	FY12				FY13		2QFY13 (%)	
	1Q	2Q	3Q	4Q	1Q	2Q	YoY	QoQ
A. Gas transmission	117	119	119	116	110	106	-11	-4
B. LPG Transmission	817	796	870	879	845	813	2	-4
C. Natural Gas Trading	83	84	85	85	83	81	-4	-3
D. Petrochemicals	88	129	113	118	66	101	-22	53
E. LPG & Liq. HC (pre-subsidy)	349	378	361	351	322	361	-4	12

Source: Company, MOSL

**Gas transmission: Volumes subdued at 106mmscmd v/s 109mmscmd in 1QFY13**

- Gas transmission EBIT was INR6b (up 8.7% YoY and 6.6% QoQ), v/s our estimate of INR5.5b. Comparable EBIT was INR5.6b in 2QFY12 and INR5.7b in 1QFY13.
- Gas transmission volumes averaged 106mmscmd in 2QFY13 (down 11% YoY and 4% QoQ). We expect GAIL's transmission volumes to decline in 3QFY13, as no additional gas is expected in the country (and KG-D6 decline continues), and rise again in 4QFY13, as the LNG terminals at Kochi and Dahej get commissioned. We model transmission volumes at an average of 107mmscmd in FY13 and 116mmscmd in FY14.
- Despite lower than expected volumes, natural gas flow in long-distance zones that have higher tariff resulted in higher than expected EBIT. Also, 1QFY13 EBIT was lower due to INR230m provisioning for Dadri-Bawana pipeline tariff revision.
- 1QFY13 transmission EBIT included one-time provision of INR230m for Dadri-Bawana pipeline, as PNGRB-determined tariff was 57% lower than GAIL's demand.

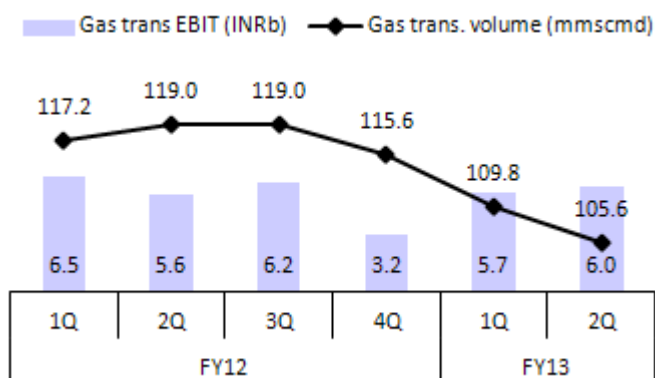
**LPG transmission: EBIT impacted by one-time tariff impact of INR1.2b**

- LPG transmission EBIT was a negative INR489m (down 167.7% YoY and 169% QoQ), v/s our estimate of INR686m. Comparable EBIT was at INR722m in 2QFY12 and INR709m in 1QFY13.
- 2QFY13 reported EBIT included one-time impact of INR1.2b due to de-recognition of revenue on account of tariff reduction by PNGRB. PNGRB had reduced GAIL's Vizag-Secunderabad and Jamnagar-Loni LPG pipeline tariff by 16% and 22%, respectively. Adjusted for this, LPG transmission EBIT was largely in-line.
- LPG transmission volumes stood at 813KT (v/s our estimate of 835KT); up 2% YoY and down 4% QoQ.

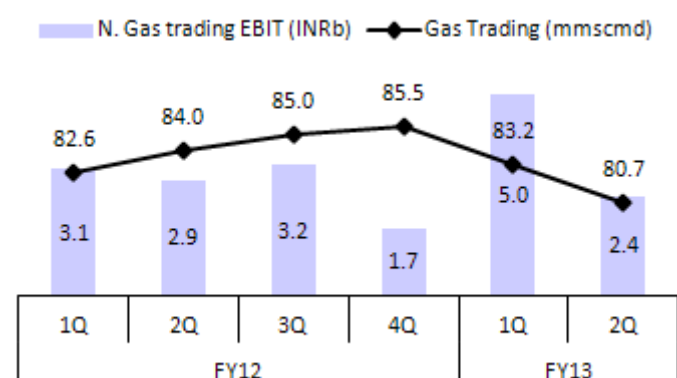
**Natural gas trading: Sharp QoQ drop as 1QFY13 included one-time inventory gains of ~INR2b**

- Gas trading EBIT was INR2.4b (down 14.6% YoY and 50.6% QoQ) v/s our estimate of INR3b. Comparable EBIT was INR2.9b in 2QFY12 and INR5b in 1QFY13.
- QoQ volume decline in trading volumes was led by lower gas supply from PMT fields.
- Sharp QoQ drop was led by higher 1QFY13 EBIT, helped by (a) higher spot LNG volumes of ~4mmscmd, (b) higher LNG realization, and (c) benefit of rupee depreciation.

Higher tariff boosted transmission EBIT



QoQ decline due to one-off gains in 1QFY13



Source: Company, MOSL

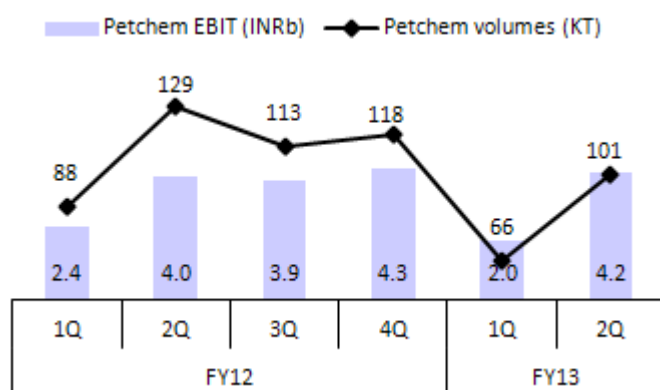
### Petrochemicals: Lower opex, higher volumes boost EBIT

- Petchem business EBIT stood at INR4.2b (up 3.5% YoY and 113.6% QoQ), v/s our estimate of INR3.7b. Comparable EBIT was INR4b in 2QFY12 and INR2b in 1QFY13.
- Petchem EBIT was boosted by lower opex and higher sales volume at 101KT (v/s our estimate of 105KT), down 22% YoY and up 53% QoQ. 1QFY13 volumes were lower and opex was higher due to 22 days maintenance shutdown.
- Realizations stood at INR87/kg (up 20% YoY and flat QoQ), in line with our estimate.
- Festive season in 3QFY13 is expected to boost petchem volumes; however, medium term outlook remains weak, led by lower global demand expectations amidst an uncertain economic environment.

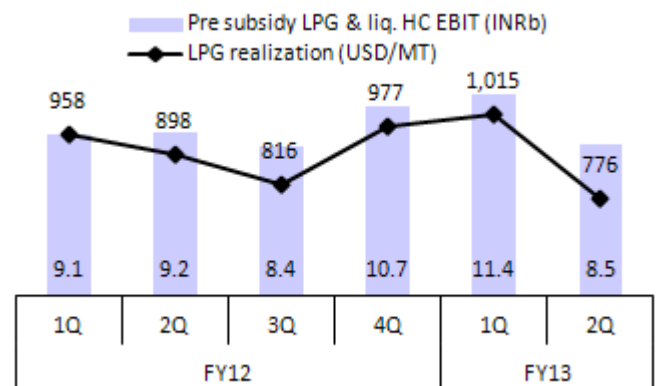
### LPG & liquid hydrocarbons: Realizations higher than estimated; subsidy in-line

- LPG and liquid hydrocarbon (before subsidy) EBIT stood at INR8.5b (down 7.2% YoY and 25.1% QoQ), higher than our estimate of INR6.9b, led by higher realizations. Comparable segmental EBIT was at INR9.2b in 2QFY12 and INR11.4b in 1QFY13.
- LPG and liquid hydrocarbon EBIT (post subsidy) stood at INR665m (v/s INR4.4b in 1QFY13 and INR3.5b in 2QFY13).
- LPG realization stood at USD776/MT (down 14% YoY and 24% QoQ) v/s benchmark (Saudi Aramco) realization of USD703/MT.

QoQ volume jump boosts petchem EBIT



Lower realization impacts LPG & liquid HC (pre-subsidy) EBIT



Source: Company, MOSL

### Valuation and view

- Key events to watch (1) Likelihood of transmission volume increase in the near-to-medium term, and (2) clarity on subsidy sharing.
- We expect GAIL's earnings to remain flat in the medium term, as headwinds on incremental gas availability continue. We model transmission volumes of 107/116mmsmcd in FY13/14.
- Adjusted for investments, the stock trades at 8.9x FY14E EPS of INR31.9. Our SOTP-based fair value stands at INR385/share. We have a Neutral rating due to: (1) low near-term visibility of transmission volume growth, (2) lower return ratios in the near term due to under-utilization of new capitalized pipelines, and (3) ad-hoc subsidy sharing risk.

**Our key earnings model assumptions are summarized below**

	FY09	FY10	FY11	FY12	FY13E	FY14E
<b>Exchange Rate (INR/USD)</b>	<b>46.1</b>	<b>47.5</b>	<b>46.0</b>	<b>47.9</b>	<b>53.9</b>	<b>53.0</b>
<b>Subsidy (INRb)</b>	<b>17.8</b>	<b>13.3</b>	<b>21.1</b>	<b>31.8</b>	<b>32.8</b>	<b>27.4</b>
<b>Natural Gas Transmission</b>						
Volume (mmsmd)	83	107	118	118	107	116
Average Tariff (INR/mscm)	860	813	880	894	939	896
<b>LPG Transmission</b>						
Volume ('000 MT)	2,744	3,160	3,337	3,362	3,362	3,362
Average Tariff (INR/MT)	1,390	1,415	1,422	1,351	886	1,125
<b>Petrochemicals</b>						
Petchem Sales ('000 MT)	423	409	420	448	385	402
Realization (INR/kg)	70	70	70	76	86	85
EBITDA (INR/kg)	33	36	32	37	42	42
EBIT (INR/kg)	31	32	28	33	37	34
<b>LPG &amp; Liq HC</b>						
Sales ('000 MT)	1,405	1,444	1,363	1,439	1,410	1,439
Realization (USD/MT)	748	606	788	910	898	870
EPS (INR)	22.7	24.8	28.7	28.8	31.2	31.9

Source: Company/MOSL

**Segmental EBIT Break-down (INR b)**

	FY09	FY10	FY11	FY12	FY13E	FY14E
Natural Gas Transmission	16.1	22.4	25.6	21.5	22.1	21.5
LPG Transmission	2.2	2.8	3.1	2.7	1.4	2.3
Natural Gas Trading	3.5	3.7	7.9	10.9	12.3	10.8
<b>Gas transmission and trading</b>	<b>21.8</b>	<b>28.9</b>	<b>36.6</b>	<b>35.1</b>	<b>35.8</b>	<b>34.6</b>
As a % of total	52	65	70	66	62	58
Petrochemicals	13.0	13.3	11.9	14.7	14.2	13.5
LPG & Liquid HC (pre-subsidy)	26.5	19.4	26.0	37.4	40.8	38.5
Other	(1.7)	(3.6)	(1.1)	(2.0)	0.2	0.0
<b>Total</b>	<b>59.6</b>	<b>58.0</b>	<b>73.4</b>	<b>85.2</b>	<b>90.9</b>	<b>86.6</b>
Less: Subsidy	17.8	13.3	21.1	31.8	32.8	27.4
<b>Total EBIT</b>	<b>41.8</b>	<b>44.7</b>	<b>52.3</b>	<b>53.4</b>	<b>58.1</b>	<b>59.2</b>

Source: Company, MOSL

**Our source-wise gas supply assumptions (mmscmd)**

	FY09	FY10	FY11	FY12	FY13E	FY14E
Existing (ONGC + Ravva)	48	50	50	50	50	50
PMT	12	16	14	13	10	11
KG Basin	-	17	28	24	15	15
RLNG	24	24	27	32	32	40
<b>Total</b>	<b>84</b>	<b>107</b>	<b>119</b>	<b>118</b>	<b>107</b>	<b>116</b>

Source: Company, MOSL

**SOTP based target price at INR385**

Business	INR/sh	Base Case		Remarks
		INR/sh	INR/sh	
<b>PE Multiple (x)</b>	<b>9.0</b>	<b>10.0</b>	<b>11.0</b>	
FY14E EPS	30.6	30.6	30.6	EPS adj. for dividend income
Core Business	276	306	337	Base case: 10x FY14 EPS (adj. for dividend income)
E&P	17	17	17	4 key blocks valued on in-place/contingent resources
Listed Investments	53	53	53	25% discount to CMP/target price
Unlisted investments	8	8	8	At Book Value
<b>Target price</b>	<b>355</b>	<b>385</b>	<b>416</b>	

Source: Company, MOSL

## GAIL (India): an investment profile

### Company description

GAIL is a major gas transmission, processing, distribution and marketing company in India, with interests in gas distribution, petrochemicals, LPG, and telecom. It owns ~8,500km of natural gas pipelines, two LPG transmission pipelines of 1,900km, 500KTA petchem capacity, ~1.4mt LPG/other hydrocarbons capacity and over 13,000km of optical fiber cable network. GAIL is also involved in city gas distribution, E&P and power businesses through JVs.

### Key investment arguments

- GAIL is in the middle of a capex cycle. It is executing pipeline projects totaling INR303b, to be completed by FY14. GAIL will double its petchem capacity by FY14. However, the risk of higher supplies from new capacities in the Middle East remains.
- Transmission business growth promise (>60% of its EBIT) is strong in the long term. However, concerns have emerged in the medium term, as RIL's KG-D6 ramp-up has halted. We model 3% volume CAGR through FY14, led by incremental LNG volumes. However, downside risk to our FY13 and FY14 estimates remains.
- GAIL's profitability ratios would be under pressure for the next 2-3 years due to underutilization of new pipelines. Earnings would be depressed due to non-commensurate increase in revenues and increase in interest and depreciation.
- GAIL operates a city gas distribution (CGD) network in several key cities through 12 JVs and plans to add 130 cities over 6-7 years. It has stake in 27 E&P blocks

in India and overseas, and has encountered hydrocarbon finds in five of its blocks.

### Key investment risks

- Lower than expected transmission volumes.
- Pressure on petchem sales volumes, led by increased imports to India.
- Increase in subsidies would impact LPG business.
- Regulation over capping of marketing margins.

### Recent developments

- Signed medium-term LNG supply contracts with GDF SUEZ (0.4mmtpa) and Gas Natural Fenosa (1bcm per year).
- Signed 20 year, 2.5mmtpa LNG supply deal with Gazprom; to commence from FY19.

### Valuation and view

- Our SOTP-based target price is INR385.
- Adjusted for investments, the stock trades at 8.9x FY14E EPS of INR31.9. Maintain **Neutral**.

### Sector view

- After strong growth in the last two years, gas availability in India will witness slower growth in the next two years due to KG-D6 issues and lack of large spare R-LNG importing facilities.
- In the short term, there is some negative sentiment owing to delay in ramp-up of domestic gas supplies.
- Policy and regulatory regime is likely to play a crucial role in the growth of the sector in India.

### Target Price and Recommendation

Current Price (INR)	Target Price (INR)	Upside (%)	Reco.
363	385	6.1	Neutral

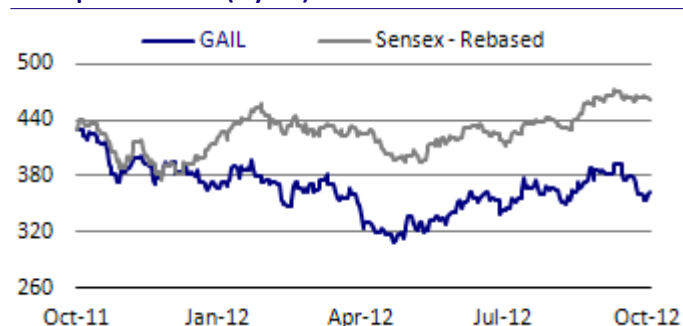
### Shareholding Pattern (%)

	Sep-12	Jun-12	Sep-11
Promoter	64.6	64.6	64.6
Domestic Inst	16.5	17.7	18.0
Foreign	16.0	14.6	14.3
Others	2.9	3.2	3.1

### EPS: MOSL forecast v/s consensus (INR)

	MOSL Forecast	Consensus Forecast	Variation (%)
FY13	31.2	31.1	0.4
FY14	31.9	32.6	-2.1

### Stock performance (1 year)



## Financials and Valuation

Income Statement				(INR Million)	
Y/E March	2010	2011	2012	2013E	2014E
Net Sales	249,337	324,586	402,807	449,878	476,993
Change (%)	-7.1	30.2	24.1	11.7	6.0
Purchases	154,300	220,059	286,791	337,408	295,736
Raw Materials	21,993	21,788	24,941	27,856	29,534
Change in Stocks	-206	-1,325	-4,978	744	0
Employee Costs	6,212	7,527	6,075	6,682	7,351
Power&fuel & othe	20,346	21,994	32,997	11,894	74,017
<b>EBITDA</b>	<b>46,691</b>	<b>54,544</b>	<b>56,981</b>	<b>65,293</b>	<b>70,356</b>
% of Net Sales	18.7	16.8	14.1	14.5	14.7
Depreciation	5,618	6,503	7,907	9,870	11,338
Interest	700	829	1,165	1,770	3,470
Other Income	5,411	5,186	5,491	4,302	3,348
Extraordinary Items (net)					
<b>PBT</b>	<b>45,784</b>	<b>52,398</b>	<b>53,400</b>	<b>57,955</b>	<b>58,896</b>
Tax	14,386	16,788	16,862	18,392	18,420
Rate (%)	31.4	32.0	31.6	31.7	31.3
<b>Reported PAT</b>	<b>31,398</b>	<b>35,610</b>	<b>36,538</b>	<b>39,563</b>	<b>40,476</b>
<b>Adjusted PAT</b>	<b>31,398</b>	<b>36,408</b>	<b>36,538</b>	<b>39,563</b>	<b>40,476</b>
Change (%)	8.9	13.4	2.6	8.3	2.3

Balance Sheet				(INR Million)	
Y/E March	2010	2011	2012	2013E	2014E
Share Capital	12,685	12,685	12,685	12,685	12,685
Reserves	155,305	179,849	203,560	229,173	255,402
<b>Net Worth</b>	<b>167,990</b>	<b>192,533</b>	<b>216,245</b>	<b>241,858</b>	<b>268,087</b>
Loans	14,804	23,100	53,469	92,659	127,659
Deferred Tax	13,896	16,332	17,686	20,005	22,360
<b>Capital Employed</b>	<b>196,689</b>	<b>231,966</b>	<b>287,400</b>	<b>354,521</b>	<b>418,106</b>
Gross Fixed Assets	210,377	221,444	263,066	335,137	461,542
Less: Depreciation	91,066	97,408	104,490	114,360	125,699
<b>Net Fixed Assets</b>	<b>119,311</b>	<b>124,036</b>	<b>158,576</b>	<b>220,777</b>	<b>335,843</b>
Capital WIP	23,305	58,462	79,425	91,175	34,328
Investments	20,730	25,825	35,489	35,489	35,489
<b>Current Assets</b>					
Inventory	6,317	8,551	14,197	16,491	15,229
Debtors	12,950	19,061	21,766	23,719	25,043
Cash & Bank Balar	41,715	21,314	9,313	12,182	12,226
Loans/Adv. & Othe	76,144	62,867	72,080	74,247	76,550
<b>Current Liab. &amp; Prov.</b>					
Liabilities	54,483	47,544	59,852	70,925	67,680
Provisions	49,301	40,605	43,595	48,635	48,922
<b>Net Current Assets</b>	<b>33,343</b>	<b>23,643</b>	<b>13,910</b>	<b>7,080</b>	<b>12,446</b>
Misc. Expenses	0	0	0	0	0
<b>Application of Funds</b>	<b>196,689</b>	<b>231,966</b>	<b>287,400</b>	<b>354,521</b>	<b>418,106</b>

E: MOSL Estimates

Ratios					
Y/E March	2010	2011	2012	2013E	2014E
<b>Basic (INR)</b>					
EPS	24.8	28.7	28.8	31.2	31.9
Cash EPS	29.2	33.2	35.0	39.0	40.8
Book Value	132.4	151.8	170.5	190.7	211.3
DPS	7.5	7.5	8.70	9.0	10.0
Payout	30.3	26.1	30.2	28.9	31.3
<b>Valuation (x)</b>					
P/E			9.9	9.1	8.9
Cash P/E			8.1	7.3	7.0
EV / EBITDA			6.8	6.6	6.8
EV / Sales			1.1	1.0	1.0
Price / Book Value			1.7	1.5	1.3
Dividend Yield (%)			2.4	2.5	2.8
<b>Profitability Ratios (%)</b>					
RoE	19.9	19.8	17.9	17.3	15.9
RoCE	25.2	24.8	21.0	18.6	16.1
<b>Turnover Ratios</b>					
Debtors (No. of Da	19	21	20	19	19
Fixed Asset Turnov	1.3	1.4	1.4	1.3	1.1
<b>Leverage Ratio</b>					
Debt / Equity (x)	-0.1	0.1	0.3	0.4	0.5

Cash Flow Statement					
Y/E March	2010	2011	2012	2013E	2014E
OP/(Loss) before T	45,784	52,400	53,400	57,955	58,896
Depreciation	5,619	6,504	7,919	9,870	11,338
Other op items	-1,397	-873	2,892	0	0
Direct Taxes Paid	-15,686	-14,839	-14,253	-16,073	-16,064
(Inc)/Dec in Wkg. t	12,454	-12,420	-5,081	9,699	-5,322
<b>CF from Op. Activity</b>	<b>46,774</b>	<b>30,773</b>	<b>44,877</b>	<b>61,451</b>	<b>48,848</b>
(Inc)/Dec in FA & C	-35,510	-46,290	-66,182	-83,822	-69,558
(Pur)/Sale of Inves	-3,358	-5,095	-9,653	0	0
Inc from Invst	4,705	4,090	4,420	0	0
<b>CF from Inv. Activity</b>	<b>-34,162</b>	<b>-47,295</b>	<b>-71,416</b>	<b>-83,822</b>	<b>-69,558</b>
Inc / (Dec) in Debt	1,962	7,215	27,069	39,190	35,000
Dividends Paid	-7,420	-11,094	-12,531	-13,950	-14,247
<b>CF from Fin. Activity</b>	<b>-5,459</b>	<b>-3,879</b>	<b>14,538</b>	<b>25,240</b>	<b>20,753</b>
Inc / (Dec) in Cash	7,154	-20,402	-12,000	2,869	44
Add: Opening Bala	34,562	41,715	21,314	9,313	12,182
<b>Closing Balance</b>	<b>41,715</b>	<b>21,314</b>	<b>9,313</b>	<b>12,182</b>	<b>12,226</b>



**N O T E S**

## Disclosures

This report is for personal information of the authorized recipient and does not constitute to be any investment, legal or taxation advice to you. This research report does not constitute an offer, invitation or inducement to invest in securities or other investments and Motilal Oswal Securities Limited (hereinafter referred as MOST) is not soliciting any action based upon it. This report is not for public distribution and has been furnished to you solely for your information and should not be reproduced or redistributed to any other person in any form.

Unauthorized disclosure, use, dissemination or copying (either whole or partial) of this information, is prohibited. The person accessing this information specifically agrees to exempt MOST or any of its affiliates or employees from, any and all responsibility/liability arising from such misuse and agrees not to hold MOST or any of its affiliates or employees responsible for any such misuse and further agrees to hold MOST or any of its affiliates or employees free and harmless from all losses, costs, damages, expenses that may be suffered by the person accessing this information due to any errors and delays.

The information contained herein is based on publicly available data or other sources believed to be reliable. While we would endeavour to update the information herein on reasonable basis, MOST and/or its affiliates are under no obligation to update the information. Also there may be regulatory, compliance, or other reasons that may prevent MOST and/or its affiliates from doing so. MOST or any of its affiliates or employees shall not be in any way responsible and liable for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. MOST or any of its affiliates or employees do not provide, at any time, any express or implied warranty of any kind, regarding any matter pertaining to this report, including without limitation the implied warranties of merchantability, fitness for a particular purpose, and non-infringement. The recipients of this report should rely on their own investigations.

This report is intended for distribution to institutional investors. Recipients who are not institutional investors should seek advice of their independent financial advisor prior to taking any investment decision based on this report or for any necessary explanation of its contents.

MOST and/or its affiliates and/or employees may have interests/positions, financial or otherwise in the securities mentioned in this report. To enhance transparency, MOST has incorporated a Disclosure of Interest Statement in this document. This should, however, not be treated as endorsement of the views expressed in the report.

Disclosure of Interest Statement	GAIL (India)
1. Analyst ownership of the stock	No
2. Group/Directors ownership of the stock	No
3. Broking relationship with company covered	No
4. Investment Banking relationship with company covered	No

## Analyst Certification

The views expressed in this research report accurately reflect the personal views of the analyst(s) about the subject securities or issues, and no part of the compensation of the research analyst(s) was, is, or will be directly or indirectly related to the specific recommendations and views expressed by research analyst(s) in this report. The research analysts, strategists, or research associates principally responsible for preparation of MOST research receive compensation based upon various factors, including quality of research, investor client feedback, stock picking, competitive factors and firm revenues.

## Regional Disclosures (outside India)

This report is not directed or intended for distribution to or use by any person or entity resident in a state, country or any jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject MOST & its group companies to registration or licensing requirements within such jurisdictions.

### For U.K.

This report is intended for distribution only to persons having professional experience in matters relating to investments as described in Article 19 of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (referred to as "investment professionals"). This document must not be acted on or relied on by persons who are not investment professionals. Any investment or investment activity to which this document relates is only available to investment professionals and will be engaged in only with such persons.

### For U.S.

MOST is not a registered broker-dealer in the United States (U.S.) and, therefore, is not subject to U.S. rules. In reliance on the exemption from registration provided by Rule 15a-6 of the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act") and interpretations thereof by the U.S. Securities and Exchange Commission ("SEC") in order to conduct business with Institutional Investors based in the U.S., Motilal Oswal has entered into a chaperoning agreement with a U.S. registered broker-dealer, Marco Polo Securities Inc. ("Marco Polo"). Any business interaction pursuant to this report will have to be executed within the provisions of this Chaperoning agreement.

This report is intended for distribution only to "Major Institutional Investors" as defined by Rule 15a-6(b)(4) of the Exchange Act and interpretations thereof by SEC (henceforth referred to as "major institutional investors"). This document must not be acted on or relied on by persons who are not major institutional investors. Any investment or investment activity to which this document relates is only available to major institutional investors and will be engaged in only with major institutional investors.

The Research Analysts contributing to the report may not be registered/qualified as research analyst with FINRA. Such research analyst may not be associated persons of the U.S. registered broker-dealer, Marco Polo and therefore, may not be subject to NASD rule 2711 and NYSE Rule 472 restrictions on communication with a subject company, public appearances and trading securities held by a research analyst account.



## Motilal Oswal Securities Ltd

Motilal Oswal Tower, Level 9, Sayani Road, Prabhadevi, Mumbai 400 025  
Phone: +91 22 3982 5500 E-mail: reports@motilaloswal.com