

**Sector: Oil & Gas**

Sensex:	16,836
CMP (Rs):	433
Target price (Rs):	534
Upside (%):	23.4
52 Week h/l (Rs):	459 / 273
Market cap (Rscr) :	54,900
6m Avg vol ('000Nos):	1,850
No of o/s shares (mn):	1,268
FV (Rs):	10
Bloomberg code:	GAIL IB
Reuters code:	GAIL.BO
BSE code:	532155
NSE code:	GAIL

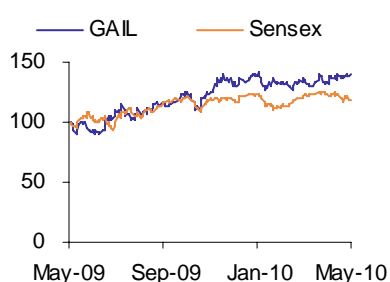
Prices as on 17 May, 2010

**Shareholding pattern**

<b>December '09</b>	<b>(%)</b>
Promoters	57.3
Institutions	38.5
Non promoter corp hold	0.8
Public & others	3.4

**Performance rel. to sensdex**

(%)	1m	3m	1yr
GAIL	9.9	2.7	22.7
ONGC	3.8	(9.3)	(10.4)
GSPL	6.7	(0.2)	48.1
Guj Gas	5.9	13.4	71.4

**Share price trend**


- ⊕ Net sales rise 5% yoy as higher transmission volumes and petrochemical realizations are offset by lower natural gas trading revenues
- ⊕ OPM jumps 340bps yoy on account of improved EBIT margins for key segments of natural gas transmission, petrochemicals and LPG and liquid hydrocarbons
- ⊕ Increased gas supplies in the country lends strong revenue and earnings visibility
- ⊕ Maintain our BUY rating and target price of Rs534

**Result table**

(Rs m)	Q4 FY10	Q4 FY09	% yoy	Q3 FY10	% qoq
<b>Net sales</b>	<b>65,690</b>	<b>62,578</b>	<b>5.0</b>	<b>62,057</b>	<b>5.9</b>
Material costs	(5,396)	(5,570)	(3.1)	(5,556)	(2.9)
Purchases	(38,569)	(39,356)	(2.0)	(37,043)	4.1
Personnel costs	(1,085)	(495)	119.3	(2,539)	(57.3)
Other overheads	(7,003)	(6,286)	11.4	(4,045)	73.1
<b>Operating profit</b>	<b>13,638</b>	<b>10,871</b>	<b>25.4</b>	<b>12,875</b>	<b>5.9</b>
<b>OPM (%)</b>	<b>20.8</b>	<b>17.4</b>	<b>339 bps</b>	<b>20.7</b>	<b>1 bps</b>
Depreciation	(1,389)	(1,410)	(1.5)	(1,409)	(1.4)
Interest	(200)	(306)	(34.5)	(142)	40.7
Other income	1,017	881	15.4	1,259	(19.3)
<b>PBT</b>	<b>13,066</b>	<b>10,037</b>	<b>30.2</b>	<b>12,583</b>	<b>3.8</b>
Tax	(3,956)	(3,737)	5.9	(3,983)	(0.7)
<b>Effective tax rate (%)</b>	<b>30.3</b>	<b>37.2</b>		<b>31.7</b>	
<b>Reported PAT</b>	<b>9,109</b>	<b>6,300</b>	<b>44.6</b>	<b>8,600</b>	<b>5.9</b>
<b>PAT margin (%)</b>	<b>13.9</b>	<b>10.1</b>	<b>380 bps</b>	<b>13.9</b>	<b>1 bps</b>
Ann. EPS (Rs)	5.7	4.0	44.6	5.4	5.9

Source: Company, India Infoline Research

**Segmental revenue performance**

Revenues (Rs mn)	Q4 FY10	Q4 FY09	% yoy	Q3 FY10	% qoq
Natural Gas trans	7,395	6,511	13.6	8,528	(13.3)
LPG transmission	1,225	992	23.4	1,161	5.5
Natural Gas Trading	46,646	47,430	(1.7)	45,274	3.0
Petrochemicals	8,223	6,813	20.7	7,927	3.7
LPG & Liquid HC	9,198	7,671	19.9	7,103	29.5
Gaitel	24	49	(51.7)	29	(16.8)

Source: Company, India Infoline Research

**Higher transmission volumes continue to drive revenue growth**

Gail (India) Ltd reported net sales of Rs65.7bn, an increase of 5% yoy. Transmission revenues were higher by 13.6% yoy primarily drive by 39% surge in volumes (increase in gas production from KG-D6). Natural gas trading revenues were lower by 1.7% yoy despite 8% increase in volumes. Petrochemical segment revenues jumped 20.7% yoy, primarily on account of higher realizations as product prices were higher in line with crude oil prices. Volumes for the petrochemical segment fell by 4.4% yoy. During Q4 FY10, Gail accounted for a subsidy burden of Rs3.4bn v/s nil in Q4 FY09. However, 3.5% higher volumes and better international prices lead to a robust growth in revenues for the segment.

### Strong EBIT margins for LPG and petrochemical segments drive 340bps yoy expansion in OPM

During Q4 FY10, GAIL reported an operating profit of Rs13.6bn up 25.4% yoy, while OPM jumped by 340bps yoy to 20.8%. Higher profitability was on account of improved EBIT margins for LPG and petrochemical segments. With feedstock prices remaining flat for Gail and sharp recovery in petrochemical prices, EBIT margin for the petrochemical segment expanded by 627bps yoy. LPG and liquid hydrocarbon segment witnessed a 15ppts yoy jump in EBIT margins on back of strong realizations for the segment. Margin expansion would have been higher had it not been for 10% higher dry well expenses.

As compared to a 25% yoy jump in operating profit, net profit for GAIL was up 44.6% yoy. This was on account of 15% yoy higher other income and 34.5% lower interest outgo.

### Cost analysis

As a % of net sales	Q4 FY10	Q4 FY09	bps yoy	Q3 FY10	bps qoq
Material costs	8.2	8.9	(69)	9.0	(74)
Purchases	58.7	62.9	(418)	59.7	(98)
Personnel Costs	1.7	0.8	86	4.1	(244)
Other overheads	10.7	10.0	62	6.5	414
<b>Total costs</b>	<b>79.2</b>	<b>82.6</b>	<b>(339)</b>	<b>79.3</b>	<b>(1)</b>

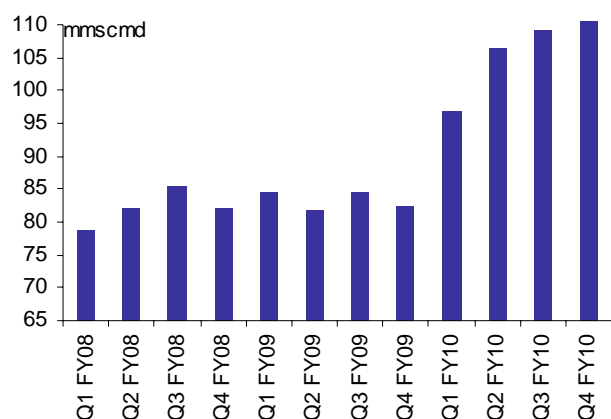
Source: Company, India Infoline Research

### Segmental performance

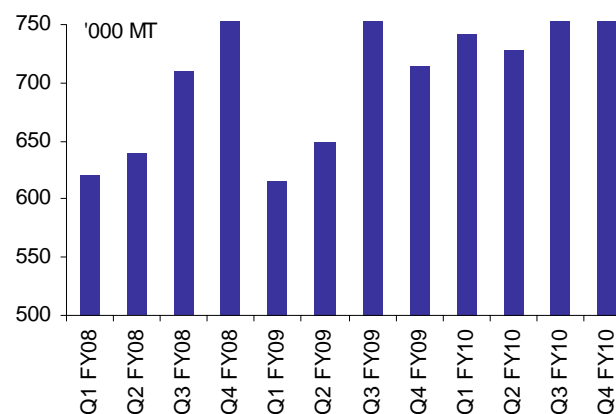
EBIT margin (%)	Q4 FY10	Q4 FY09	bps yoy	Q3 FY10	bps qoq
Natural Gas transmission	68.4	66.7	175	69.8	(138)
LPG transmission	71.2	64.4	672	55.0	1,615
Natural Gas Trading	0.8	1.2	(42)	2.6	(178)
Petrochemicals	54.3	48.1	627	43.1	1,127
LPG and Liquid Hydrocarbons	44.2	29.2	1,502	17.6	2,659
Gaitlet	(77.2)	(34.4)	(4,280)	(138.2)	6,103

Source: Company, India Infoline Research

### Trend in natural gas transmission volumes



### Trend in LPG transmission volumes



Source: Company, India Infoline Research

### Maintain our BUY rating on the stock

With the surge in gas supplies in the country from multiple sources including new finds, CBM blocks, imported LNG, GAIL is expected to witness a quantum jump in its transmission volumes. Although there would be a near term impact on earnings on account of revision in tariffs (retrospective effect), higher blended realizations would improve profitability for the company. We maintain our BUY rating on the stock with a one year price target of Rs534. The key risk to our call remains the overhang of an adverse change in the current subsidy sharing pattern.

**Valuation summary**

Y/e 31 Mar (Rs m)	FY09	FY10	FY11E	FY12E
Revenues	237,760	251,033	320,950	369,944
yoy growth (%)	32.0	5.6	27.9	15.3
Operating profit	40,647	47,760	59,499	71,536
OPM (%)	17.1	19.0	18.5	19.3
Pre-exceptional PAT	28,037	31,398	36,907	43,369
Reported PAT	28,037	31,398	36,907	43,369
yoy growth (%)	6.9	12.0	17.5	17.5
EPS (Rs)	22.1	24.8	29.1	34.2
P/E (x)	19.6	17.5	14.9	12.7
Price/Book (x)	3.7	3.3	2.9	2.5
EV/EBITDA (x)	13.0	11.0	9.6	8.1
Debt/Equity (x)	0.1	0.1	0.2	0.2
RoE (%)	20.2	19.9	20.6	21.2
RoCE (%)	26.2	25.2	26.4	25.9

Source: Company, India Infoline Research

**SOTP Valuation**

Particulars	Parameter	Rs mn
Natural Gas	10x EV/EBIDTA	395,190
LPG	6x EV/EBIDTA	123,600
Petrochemicals	7x EV/EBIDTA	93,485
E&P	EV/BOE	26,601
Total		638,878
Net Debt		26,668
Value		612,210
No of shares (mn)		1,268
Per share value (Rs)		483
Investment value (Rs)		52
Total (Rs)		534

Source: Company, India Infoline Research

**Recommendation parameters for fundamental reports:**

**Buy** – Absolute return of over +10%

**Market Performer** – Absolute return between -10% to +10%

**Sell** – Absolute return below -10%

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