RESULTS REVIEW

Share Data

Market Cap	Rs. 442.06 bn
Price	Rs. 522.75
BSE Sensex	19,854.12
Reuters	GAIL.BO
Bloomberg	GAIL IN
Avg. Volume (52 Week)	0.26 mn
52-Week High/Low	Rs. 549.9/248.6
Shares Outstanding	845.65 mn

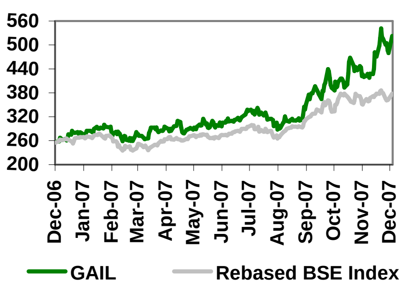
Valuation Ratios (Consolidated)

Year to 31 March	2008E	2009E
EPS (Rs.)	29.6	33.2
+/- (%)	(1.8%)	12.4%
PER (x)	17.7x	15.7x
EV/ Sales (x)	2.4x	2.1x
EV/ EBITDA (x)	11.8x	10.2x

Shareholding Pattern (%)

Promoters	57
FIIs	17
Institutions	18
Public & Others	7

Relative Performance



GAIL (India) Limited — Hold

Petrochemical and LPG business overtakes Gas transmission services

GAIL (India) Ltd.'s net sales for Q2'08 came in at Rs. 45.3 bn up by 22.2% yoy due to greater revenue contribution from the petrochemical and LPG business segments. EBITDA was higher by 49.1% yoy to Rs. 8.8 bn on account of margin expansion in petrochemical business and lower purchase & raw material cost coupled with lower subsidy allocation. Margins improved consequently by 350 bps to 19.4% in Q2'08. However, the increase was restricted due to a dry well expenditure write-off of Rs. 2.6 bn. The growth in net profit was obstructed by higher effective tax rate which limited the increase to 27.7% yoy at Rs. 5.7 bn.

On the back of outstanding performance of Petrochemical & LPG segments and on the expectation of gas transmission from KG basin to start by FY09, we have revised our revenue estimate for FY09 and expect the sales to grow at a CAGR of 14.2% for FY07-FY09E. The Company's plan for pipeline expansion and vertical spread in the gas value chain along with entry into city gas distribution will lead to growth opportunities in the long-term; however, the core business will remain under pressure in FY08-09 till the time the expansion programmes are in progress. At the current price, the stock trades at a forward P/E of 17.7x for FY08E and 15.7x for FY09E. Based on our valuation and analysis we believe that there is little room for an upside. Hence, we maintain Hold.

Result Highlights

The net sales for Q2'08 was Rs. 45.3 bn up by 22.2% yoy due to higher revenues from the petrochemical and LPG segments. The Petrochemical

Key Figures (Standalone)

Quarterly Data	Q2'07	Q1'08	Q2'08	YoY%	QoQ%	H1'07	H1'08	YoY%
(Figures in Rs mn, except per share data)								
Net Sales	37,070	42,457	45,289	22.2%	6.7%	77,854	87,746	12.7%
EBITDA	5,891	10,387	8,783	49.1%	(15.4%)	15,307	19,170	25.2%
Net Profit	4,484	6,852	5,725	27.7%	(16.4%)	10,405	12,578	20.9%
Margins(%)								
EBITDA	*15.9%*	*24.5%*	*19.4%*			19.7%	21.8%	
NPM	*12.1%*	*16.1%*	*12.6%*			13.4%	14.3%	
Per Share Data (Rs.)								
EPS	5.3	8.1	6.8	27.7%	(16.4%)	12.3	14.9	20.9%

Petrochemical & LPG continue to be the major contributors to revenue growth

segment recorded 36.7% yoy increase in sales to Rs. 6.4 bn whereas the sales from LPG & liquefied hydrocarbons was ahead by 81.1% yoy to Rs. 7 bn in Q2'08. Apart from these two segments, other business segments too reported increase in sales on yoy basis.

Physical Perfomance (H1'08 vs H1'07)	Volume	Inc/(Dec)%
Gas Transmitted (MMSCMD)	80.46	8%
Gas Sales (MMSCMD)	69.25	4%
LPG Transmission ('000 MT)	1,261	14%
Polymer Sales ('000 MT)	201	33%
LHC Sales ('000 MT)	711	8%

EBITDA was higher by 49.1% yoy to Rs. 8.8 bn on account of margin expansion in petrochemical business and lower purchase & raw material cost coupled with lower subsidy allocation. EBIT from petrochemical segment rose by 83.4% to Rs. 3.2 bn. Overall purchase cost to sales was lower at 56.1% (down 362 bps) and the cost of raw material to sales was lower at 9.9% (down 145 bps), when compared to the corresponding figures last year. In addition to the above, the subsidy provision was lower by 38.2% yoy to Rs. 2.6 bn. However, increase in EBITDA was arrested by a write-off of Rs. 2.6 bn related to dry well expenditure in the exploration and production segment in this quarter.

Segment Revenue (Gross sales)	Q2'07	Q2'08	Inc/(Dec)%
A. Transmission services			
I) Natural Gas	4,972	5,683	14.3%
II) LPG	816	896	9.8%
B. Natural Gas Trading	29,237	32,093	9.8%
C. Petrochemicals	4,683	6,402	36.7%
D. LPG & Liquified Hydrocarbons	3,884	7,033	81.1%
E. GAILTEL	63	76	21.9%
F. Unallocated	1,602	1,636	2.1%
Total	45,257	53,819	
Less: Inter segment sales	(6,513)	(6,725)	
Gross sales	**38,744**	**47,095**	**21.6%**

Higher effective tax rate compress the bottomline

The net profit increased to Rs. 5,725.4 mn as compared to Rs. 4,484 mn in Q2'07, as a result of increase in operating profits. However, the increase in effective tax rate to 35.6% in Q2'08 did not allow the net profit to rise in line with the operating profit despite lower interest charges.

Segment Results (EBIT)	Q2'07	Q2'08	Inc/(Dec)%
A. Transmission services			
I) Natural Gas	3,295	3,955	20.0%
II) LPG	449	521	16.1%
B. Natural Gas Trading	614	704	14.7%
C. Petrochemicals	1,743	3,195	83.4%
D. LPG & Liquified Hydrocarbons	(545)	2,234	NM
E. GAILTEL	4	14	236.6%
Total	**5,559**	**10,623**	

Key Events

- GAIL has pocketed the rights to market the gas jointly produced by Reliance Industries, British Gas, and ONGC from Panna-Mukta-Tapti fields.
- The Company has signed a gas transmission agreement with Reliance Gas Transportation Infrastructure Ltd (RGTIL) for transportation of natural gas from the exploration block in KG basin through GAIL's network and for booking capacity in Reliance Gas East-West pipeline.
- GAIL signed a memorandum of understanding with Reliance Industries Ltd for joint co-operation in petrochemicals in order to create a special purpose vehicle for setting up petrochemical complexes in West Asia, Russia, and Former Soviet Union countries (FSU).
- The Company plans to invest Rs. 140 bn in doubling its existing cross-country pipeline network by the end of 2011-12. The existing pipelines will be extended over 3,000 km and five new pipelines will be constructed in the five years time.
- GAIL is in talks with Qatar Petrochemical Co and Russia's Lukeoil as it looks forward to build a large petrochemical plant overseas.

Key Risks

- Increase in subsidy sharing can negatively affect the Company's profitability.
- 100% FDI has been allowed in laying pipelines business, which can increase competition in the industry and thus negatively affect our estimates.

Outlook

Transmission from KG basin expected to commence by FY09

GAIL strategically focuses on filling the gap existing between the demand and supply of gas and petrochemicals. In order to do that it plans to extend the cross-country pipeline network by another 3,000 km in the next five years. Further, it has signed an agreement with RGTIL for transmission of gas from KG basin and also intends to set up a pipeline manufacturing firm and construction company in a joint venture with strategic partners.

On the back of outstanding performance of Petrochemical & LPG segments and on the expectation of gas transmission from KG basin to start by FY09, we have revised our revenue estimate for FY09 and expect the sales to grow at a CAGR of 14.2% for FY07-FY09E. The Company's plan for pipeline expansion and vertical spread in the gas value chain along with entry into city gas distribution will lead to growth opportunities in the long-term; however, the core business will remain under pressure in FY08-09 till the time the expansion programmes are in progress. At the current price, the stock trades at a forward P/E of 17.7x for FY08E and 15.7x for FY09E. Based on our valuation and analysis we believe that there is little room for an upside. Hence, we maintain Hold.

Key Figures (Consolidated)

Year to March	FY05	FY06	FY07	FY08E	FY09E	CAGR (%)
(Figures in Rs mn, except per share data)						(FY07-09E)
Net Sales	127,030	148,788	165,423	187,755	215,919	14.2%
EBITDA	25,796	37,221	32,531	38,302	44,263	16.6%
Net Profit	20,389	24,391	25,453	24,997	28,086	5.0%
Margins(%)						
EBITDA	*20.3%*	*25.0%*	*19.7%*	*20.4%*	*20.5%*	
NPM	*16.1%*	*16.4%*	*15.4%*	*13.3%*	*13.0%*	
Per Share Data (Rs.)						
EPS	24.1	28.8	30.1	29.6	33.2	5.0%
PER (x)	8.8x	11.0x	17.4x	17.7x	15.7x	

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