Petronet LNG ---Maintain NEUTRAL

A weak quarter as expected; volumes should go up hereon **EPS: ▼ TP: ▼**

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- PLNG reported 3Q FY10 EPS of Rs.1.1, 7% below our estimate and down 31% QoQ. Gas sales volumes fell 26% QoQ.
- This correction was expected – a) the 1.5 MTPA supply to Dabhol ended in September and b) KG D6 gas hurt spot volume sales.
- Total volumes were better, but lower-than-expected gross margin kept EBITDA in line. Lower other income, higher depreciation and interest costs led to the earnings miss.
- The 2.5 MTPA additional supply from RasGas has commenced in January, and should increase PLNG's 4Q FY10 volumes sharply.
- Tight pipeline capacity and bottled up D6 gas can keep spot LNG sales in check. PLNG has enjoyed regas as well as trading profits on these.
- With a tolling model, PLNG relies on volumes and tariffs. In the absence of regulation/customer pushback, PLNG continues to take a 5% increase in tariff each year – a review is well past due. Increasing utilisation remains the key for stock price upsides, but that seems difficult in the near term. We reduce FY10E EPS 12% and target price to Rs71 (from 73).

Bbg/RIC	PLNG IN / PLNG.BO	Price (20 Jan 10 , Rs)	76.50
Rating (prev. rating)	N (N) [V]	TP (Prev. TP Rs)	71.00 (73.00)
Shares outstanding (mn)	750.00	Est. pot. % chg. to TP	(7)
Daily trad vol - 6m avg (mn)	2.0	52-wk range (Rs)	82.10 - 32.00
Daily trad val - 6m avg (US$ mn)	0.1	Mkt cap (Rs/US$ mn)	57,375.0/ 1,251.1
Free float (%)	50.0		
Major shareholders	GAIL IN, BPCL IN, IOCL IN, ONGC IN		

Performance	1M	3M	12M
Absolute (%)	7.6	2.4	107.9
Relative (%)	2.9	0.9	8.3

Year	3/08A	3/09A	3/10E	3/11E	3/12E
Revenues (Rs mn)	65,553	84,287	113,943	136,877	158,786
EBITDA (Rs mn)	8,661	9,013	9,577	12,817	13,750
Net profit (Rs mn)	4,747	5,184	4,554	5,960	6,578
EPS (Rs)	6.33	6.91	6.07	7.95	8.77
- Change from prev. EPS (%)	n.a.	n.a.	(12)	(3)	3
- Consensus EPS (Rs)	n.a.	n.a.	7.07	7.78	8.15
EPS growth (%)	51.5	9.2	(12.2)	30.9	10.4
P/E (x)	12.1	11.1	12.6	9.6	8.7
Dividend yield (%)	2.0	2.3	1.9	2.5	2.7
EV/EBITDA (x)	7.4	7.8	9.8	7.5	7.1
P/B (x)	3.5	2.9	2.5	2.1	1.8
ROE (%)	29.3	26.1	19.7	21.7	20.4
Net debt (net cash)/equity (%)	41.5	66.5	157.4	142.5	124.1

Note1:Petronet LNG is the largest importer of Liquefied Natural Gas in India. It has regassification facilities in Gujarat; which it is expanding and is setting up a new facility in Kochi. It also has long term gas sourcing contracts with Qatar..

PLNG earnings below estimates

Petronet was expected to have a poor quarter on volumes – a) its contractual supplies to Dabhol (1.5MTPA) ended in September, and b) increasing supply from KG D6 crowded out spot LNG purchases. Sales volumes fell 26% QoQ, but PLNG benefitted from 11 TBTU of direct purchases by customers (for which PLNG makes tolling margins). Though total regas volumes were higher than expected, gross regas margins were lower – PLNG 3Q FY10 EBITDA was in line with our expectations. Higher depreciation, lower other income and higher interest costs caused PAT to be 7% below our estimates. We reduce FY10E EPS 12% to Rs6 (9M delivered Rs4.1) and marginally reduce target price to Rs71.

Figure 1: Summary results

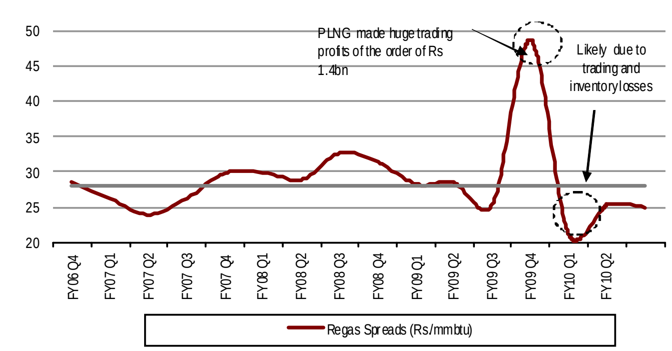
(Rs mn)	3QFY09	2QFY10	3QFY10	CS 3Q10E	QoQ (%)	YoY (%)	Vs. Est (%)
Sales	24,730	34,067	22,446	27,322	-34	-9	-18
Raw materials	22,576	31,189	20,026	24,879	-36	-11	-20
Staff cost	37	41	41	41	1	13	1
Other expenditure	262	299	291	299	-3	11	-3
EBITDA	1,855	2,537	2,088	2,103	-18	13	-1
Depreciation	258	430	466	430	8	80	8
EBIT	1,597	2,107	1,622	1,672	-23	2	-3
Other Income	222	191	167	191	-12	-25	-12
Interest	255	511	534	511	5	110	5
PBT	1,563	1,787	1,255	1,352	-30	-20	-7
Tax	513	580	423	460	-27	-17	-8
PAT	1,051	1,207	832	892	-31	-21	-7
EPS	1.40	1.61	1.11	1.19	-31	-21	-7
Sales Qty (TBTU)	85.07	113.47	84.32	90.47	-26	-1	-7

Source: Company data, Credit Suisse estimates

4QFY10 volumes to increase

3Q likely marked the low of PLNG volumes – management confirmed on CNBC that an additional 2.5MTPA supply from RasGas has commenced. This, by itself, will increase PLNG's base volumes by 50%. Tight pipeline capacity and bottled up KG D6 supply can keep spot LNG purchases in check in the near term. As GAIL expands its pipeline capacities, PLNG should be able to increase utilisation rates at Dahej.

Figure 2: Gross regas spreads remain low



Source: Company data, Credit Suisse estimates

Most inexpensive among the gas companies around?

On a P/E basis, PLNG appears to be relatively inexpensive – which may prove to attractive during these times. However, the company has large debt and capacity expansion/investment plans in petchem and power projects, which means free cash flow can be negative for some time. EV/EBITDA valuations appear more fully valued. Increasing utilisation remains the key for stock price upsides, which seems difficult in the near term. We maintain our NEUTRAL rating on PLNG.

Companies Mentioned *(Price as of 20 Jan 10)*
Petronet LNG Limited (PLNG.BO, Rs76.50, NEUTRAL [V], TP Rs71.00)

Disclosure Appendix

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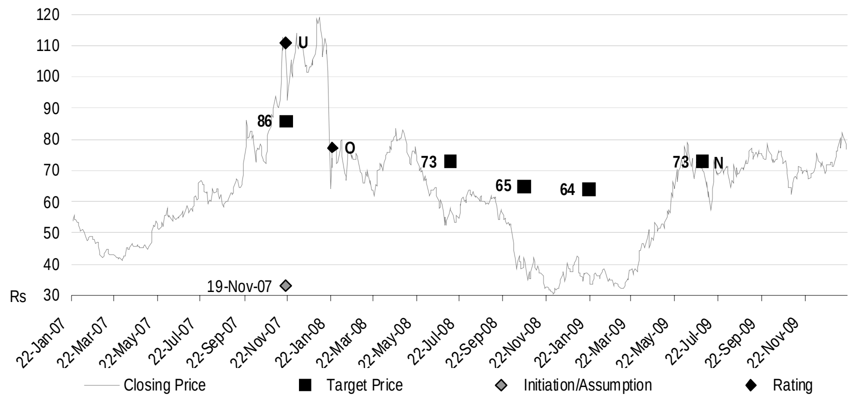
3-Year Price, Target Price and Rating Change History Chart for PLNG.BO

PLNG.BO Date	Closing Price (Rs)	Target Price (Rs)	Rating	Initiation/ Assumption
19-Nov-07	110.85	86	U	X
25-Jan-08	77.25		O	
8-Jul-08	56.1	73		
21-Oct-08	42.05	65		
20-Jan-09	36.8	64		
29-Jun-09	72.6	73	N	



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Price Target: (12 months) for (PLNG.BO)

Method: Our target price of Rs.71 per share for PLNG.BO is based on a discounted cash flow (DCF) using a weighted average cost of capital (WACC) of 14.8%. We see increased regasification capacity with the company, based on expansion of Dahej and the new plant at Kochi - and forecast long term utilisation at around 85%.

Risks: Risks to our target price of Rs.71 for PLNG.BO arise if a) domestic gas production is more than anticipated b) PLNG is unable to source gas from international sources in sufficient quantities and c) if prices of LNG are high, causing utilisations to be lower

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