Company Focus

23 November 2007 | 16 pages

GAIL (GAIL.BO)

Target price change ☑
Estimate change ☑

Buy: Leverage to KG Gas More Visible, Upgrade TP to Rs482

- **Maintain Buy with new target of Rs482** — GAIL is set to benefit from KG gas and other discoveries on East Coast, notwithstanding Reliance's captive pipeline. Though less leveraged than some of its smaller peers (viz. GSPL), GAIL's valuations are also undemanding and do not factor in potential value accretion from the proposed pipeline expansions.

- **Gearing up for the gas deluge** — GAIL will lay 5 new pipelines and upgrade 3 existing ones by 2011 at a cost of Rs180bn. Increasing visibility on East coast (KG, Cauvery, Mahanadi) implies meaningful utilisation of 140mscmd expansion is only a matter of time. Given the assured ~14% ROE, we incorporate value accretion of Rs36/share based on P/BV of 1.5x equity contribution (Rs90bn), discounted back by 4 years.

- **Earnings revised upwards** — Higher petrochem prices, reasonable subsidy burden and higher gas flow (from 77mscmd in FY07 to 126mscmd in FY10E) are the key reasons for earnings upgrades of 6-12% over FY08-09E. High crude prices will support absolute petrochem prices even as GAIL's gas feedstock has already moved to market prices.

- **Significant value in cash + investments** — We estimate the value of net cash and investments at Rs167/share (incl. Myanmar gas find) as on Mar-08, which provides downside support to the valuations. Exposure to more E&P blocks and evolution of city gas in the long term (3-5 years) could provide further upside.

Buy/Low Risk	**1L**
Price (22 Nov 07)	Rs426.20
Target price	Rs482.00
from Rs323.00	
Expected share price return	13.1%
Expected dividend yield	2.8%
Expected total return	**15.9%**
Market Cap	Rs360,417M
	US$9,177M

Price Performance (RIC: GAIL.BO, BB: GAIL IN)

Statistical Abstract

Year to 31 Mar	Net Profit (RsM)	Diluted EPS (Rs)	EPS growth (%)	P/E (x)	P/B (x)	ROE (%)	Yield (%)
2006A	23,101	27.32	18.2	15.6	3.6	24.8	2.3
2007A	20,467	24.20	-11.4	17.6	3.2	19.2	2.3
2008E	24,759	29.28	21.0	14.6	2.8	20.5	2.8
2009E	27,271	32.25	10.1	13.2	2.5	20.1	2.8
2010E	30,397	35.95	11.5	11.9	2.2	19.9	3.1

Source: Powered by dataCentral

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See Appendix A-1 for Analyst Certification and important disclosures.

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Fiscal year end 31-Mar	2006	2007	2008E	2009E	2010E
Valuation Ratios					
P/E adjusted (x)	15.6	17.6	14.6	13.2	11.9
EV/EBITDA adjusted (x)	9.3	10.7	9.2	8.2	7.2
P/BV (x)	3.6	3.2	2.8	2.5	2.2
Dividend yield (%)	2.3	2.3	2.8	2.8	3.1
Per Share Data (Rs)					
EPS adjusted	27.32	24.20	29.28	32.25	35.95
EPS reported	27.32	24.20	29.28	32.25	35.95
BVPS	117.94	134.72	150.80	169.85	191.50
DPS	10.00	10.00	12.00	12.00	13.00
Profit & Loss (RsM)					
Net sales	163,330	160,220	169,333	193,475	228,576
Operating expenses	-132,794	-135,234	-139,015	-159,667	-190,096
EBIT	**30,536**	**24,986**	**30,317**	**33,809**	**38,480**
Net interest expense	-1,173	-1,072	-888	-770	-700
Non-operating/exceptionals	4,155	4,607	5,443	5,371	5,032
Pre-tax profit	**33,518**	**28,521**	**34,872**	**38,410**	**42,813**
Tax	-9,666	-8,130	-10,113	-11,139	-12,416
Extraord./Min.Int./Pref.div.	-752	77	0	0	0
Reported net income	**23,101**	**20,467**	**24,759**	**27,271**	**30,397**
Adjusted earnings	23,101	20,467	24,759	27,271	30,397
Adjusted EBITDA	36,131	30,740	36,386	40,815	46,424
Growth Rates (%)					
Sales	20.3	-1.9	5.7	14.3	18.1
EBIT adjusted	11.6	-18.2	21.3	11.5	13.8
EBITDA adjusted	-1.9	-14.9	18.4	12.2	13.7
EPS adjusted	18.2	-11.4	21.0	10.1	11.5
Cash Flow (RsM)					
Operating cash flow	**35,212**	**11,809**	**39,800**	**34,119**	**38,256**
Depreciation/amortization	5,595	5,754	6,068	7,006	7,943
Net working capital	6,516	-14,412	8,972	-158	-85
Investing cash flow	**-12,355**	**-18,156**	**-25,000**	**-25,000**	**-25,000**
Capital expenditure	-5,761	-17,951	-25,000	-25,000	-25,000
Acquisitions/disposals	-6,594	-205	0	0	0
Financing cash flow	**-7,543**	**-15,480**	**-12,541**	**-13,163**	**-12,093**
Borrowings	-808	-5,787	-1,379	-2,000	0
Dividends paid	-9,643	-9,693	-11,163	-11,163	-12,093
Change in cash	**15,314**	**-21,827**	**2,259**	**-4,043**	**1,163**
Balance Sheet (RsM)					
Total assets	**169,418**	**167,757**	**191,776**	**207,739**	**229,729**
Cash & cash equivalent	44,959	26,604	37,032	32,989	34,997
Accounts receivable	7,535	7,907	9,407	10,749	12,699
Net fixed assets	81,716	93,913	112,845	130,839	147,895
Total liabilities	**69,685**	**53,828**	**64,250**	**64,105**	**67,790**
Accounts payable	15,202	14,484	15,208	15,968	16,767
Total Debt	19,166	13,379	12,000	10,000	10,000
Shareholders' funds	**99,733**	**113,929**	**127,526**	**143,634**	**161,939**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	22.1	19.2	21.5	21.1	20.3
ROE adjusted	24.8	19.2	20.5	20.1	19.9
ROIC adjusted	25.7	18.8	18.9	18.5	18.5
Net debt to equity	-25.9	-11.6	-19.6	-16.0	-15.4
Total debt to capital	16.1	10.5	8.6	6.5	5.8

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Earnings go up on all-round improvement

GAIL's 1HFY08 performance has been a result of 1) high petrochemical prices and production (post-expansion of HDPE), 2) high net LPG realisation (as subsidy formula has reverted to 1/3rd) and 3) recovery in gas transmission volumes from spot LNG, etc.

Our earnings upgrade of 6-12% over FY08-09E is therefore a function of:

1. Higher gas transmission volumes in FY09E, now at 98mscmd (82mmscmd in FY08E) on improved visibility on RIL's gas supplies from July 2008. A meaningful portion of the 40-80mmscmd from KG-D6 is likely to flow through GAIL's existing customers on HVJ/DVPL/GREP network due to the lack of readiness of new gas-based power projects to offtake gas.

2. Higher petrochemical prices esp. given that high crude/naphtha prices will likely keep absolute PE prices robust. Absolute PE prices are more critical determinant of GAIL's profitability vis-à-vis Ethylene-Naphtha spread as its feedstock prices (rich natural gas) are relatively sticky. GAIL is anyway paying market price of US$4.75/mmbtu for the feedstock gas and despite ONGC's demand for differential C2/C3 pricing, it is unlikely as long as GAIL is bearing petroleum subsidies.

3. Upstream's share of subsidies on retail petroleum products has reverted to 33% in FY08 after increasing to 40% in FY07. Even if we assume 35% sharing in our base case, GAIL's net LPG realisation is set to improve from US$242/tonne in FY07 to US$333/tonne in FY08 and beyond.

However, despite the upgrade, earnings growth at 10-11%pa will remain moderate over FY08-10E mainly due lower petrochemical and LPG profitability. Gas transmission contribution to EBITDA is likely to increase from 51% in FY07 to ~60%in FY10E.

Figure 1. GAIL- Earnings Revision

Year to	Net Profit (Rs Mils.)		Diluted EPS (Rs)			Dividend Per Share (Rs)	
31-Mar	Old	New	Old	New	*% Chg*	Old	New
2008E	23,347	24,759	27.61	29.28	*6.0%*	10.0	12.0
2009E	24,377	27,271	28.83	32.25	*11.9%*	9.0	12.0
2010E	-	30,397	-	35.94		-	13.0

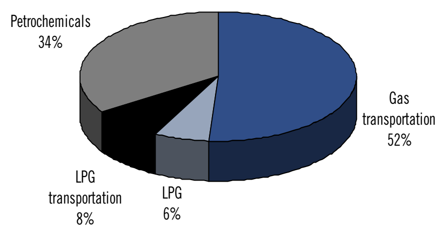
Source: Citi Investment Research estimates

Figure 2. Key Assumptions

Year to 31-Mar	2007	2008E	2009E	2010E
Volumes				
Gas transmission volumes (mmscmd)	77.3	82.2	98.5	126.0
LPG sales (mn tonnes)	1.04	1.05	1.11	1.17
Other liquid hydrocarbons ('000 tonnes)	290	300	316	333
HDPE/LDPE sales ('000 tonnes)	347	400	420	440
Realisation				
Transmission margin -HVJ/DVPL/GREP (Rs/'000scm)	1,060	1,060	1,010	960
Margins on Shipper volumes (Rs/'000scm)	634	634	634	634
Net LPG realisation (US$/t)	242	333	333	333
HDPE/LDPE (Rs/kg)	70.8	68.9	63.8	63.8
LPG transmission				
Volumes (mn tonnes)	2.49	2.63	2.78	2.94
Avg. transmission charge (Rs/t)	1,429	1,452	1,475	1,498

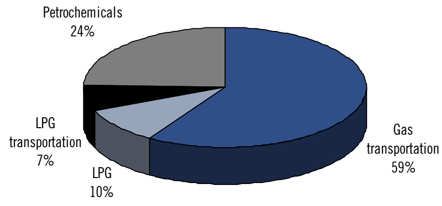
Source: Citi Investment Research estimates

Figure 3. EBITDA Break-up (FY2007)



Source: Citi Investment Research

Figure 4. EBITDA Break-up (FY2010E)



Source: Citi Investment Research

Valuation – Existing + New pipelines + investments

Given the increased potential of indigenous gas supplies from the East Coast basins (KG, Cauvery, Mahanadi) and GAIL's now visible pipeline plans, we now explicitly factor in potential value creation from the expansion plans. Though the increase in capacity by 140mmscmd will take some time to fill-up, it is a matter of time, maybe FY13-14E, by when KG D6 would plateau and other East Coast discoveries would have commenced production.

In addition, the Cost of Services method (COS), while assuring post-tax ROE of ~14% (similar to that assumed in arriving at HVJ/DVPL tariffs), also allows for upward adjustment of tariffs if volumes are lower than normative levels. This provides greater predictability in GAIL's return on equity on the pipeline capex. Our valuation approach therefore comprises the Existing Business value + New pipelines value accretion + value of investments & Myanmar gas.

1. **Existing business valued at Rs309/share**. We value existing business at EV/E of 6.5x FY08E, which does not incorporate any growth from the proposed pipeline assets. Though there are cyclical components to earnings (petrochemical, LPG), it is offset by the superior feedstock (natural gas) and subsidy on LPG which reduces its contribution to mid-cycle levels (net realisation on LPG is US$333/tonne vs. US$800/tonne at present). Existing business value at Rs309/share imputes PER of ~10x FY08E, which is reasonable given GAIL's low cost of equity. This also works out to P/BV of 1.6x FY08E based on adjusted book (adding back the excess depreciation on pipelines prior to FY05).

2. **Value accretion from new pipelines at Rs36/share.** Though the normative ROE is likely to be ~14%, we believe GAIL can earn an additional 100-200bps given the possibility of opex savings, etc. Given the low cost of equity for GAIL, the P/BV of 1.5x can be justified. The value accretion from equity investments in new pipelines (50% of Rs180bn) is therefore calculated as 1.5x equity contribution less the equity contribution itself i.e. Rs90bn. The resultant value is discounted back by 4 years, assuming reasonable pipeline utilisation by FY13.

3. **Value of investments at Rs137/share.** This includes value of investments in ONGC, other gas utilities (IGL, MGL, PLNG) and 10% interest in Myanmar gas find (OGIP of 10tcf, recovery of 70% and EV/boe of US$4.0).

Figure 5. Valuation Framework

EV/EBITDA	**6.5**	
Equity value of current business	309	On FY08E EBITDA
Value of investments	137	ONGC, Gas utilities, Myanmar
Value accretion from new pipelines	36	Based on P/B of 1.5x
Target price (Rs)	**482**	

Source: Citi Investment Research

Figure 6. Value of investments

Stake in ONGC (2.4%)	73	At CMP
Stake in IGL (22.5%)	6	At CMP
Stake in Petronet LNG (12.5%)	11	At CMP
Stake in Mahanagar Gas (50%)	12	Assuming MGL = IGL mkt cap
Stake in China Gas Holdings Ltd.	4	@ CMP = HK$3.55
Other investments (Dabhol, Fayum, etc.)	6	At book value
Myanmar gas (10% stake in A-1,A-3)	24	OGIP=10tcf, 70% recovery, EV/boe of US$4
Total (Rs)	**137**	

Source: Citi Investment Research

Though some of its peers viz. GSPL, Gujarat Gas are more leveraged to increasing gas supplies from East Coast, we believe that GAIL's complementary pipeline plans (to Reliance Group's proposed pipelines) make it strongly positioned to supply gas in the energy hungry West and South India besides serving parts of East/South markets. In this context, we believe that GAIL's valuations are still reasonable vis-à-vis its smaller peers (see table below). Though the valuation discount has been blamed on cyclical components in GAIL's EBITDA and low volume growth in the past, we believe it is now offset by 1) mid-cycle profitability of LPG due to subsidies, 2) high absolute petrochem prices due to high naphtha and GAIL's advantage of being a gas-based producer and 3) Improving leverage to KG gas.

Figure 7. Valuation Comparison

			Mkt cap	Share price	Target	P/E (x)		Price/CEPS (x)		EV/EBITDA (x)		P/BV (x)		Div. Yield (%)	
Company Name	**RIC Code**	**Rating**	**(US$m)**	**21-Nov-07**	**price**	**FY08E**	**FY09E**	**FY08E**	**FY09E**	**FY08E**	**FY09E**	**FY08E**	**FY09E**	**FY08E**	**FY09E**
GAIL	GAIL.BO	1L	9,074	421	482	14.4	13.1	11.6	10.4	9.4	8.1	2.8	2.5	2.8%	2.8%
Indraprastha Gas	IGAS.BO	1L	532	149	160	12.9	11.4	9.2	7.9	6.7	5.9	3.6	3.0	2.3%	2.7%
Gujarat Gas*	GGAS.BO	1L	554	339	350	16.6	13.5	12.8	10.5	10.2	8.4	4.0	3.2	0.9%	0.9%
Gujarat State Petronet	GSPT.BO	1M	1,044	73	74	54.7	36.8	16.2	12.0	13.5	10.4	3.7	3.4	0.5%	0.8%
Petronet LNG	PLNG.BO	3M	1,885	99	78	21.0	18.1	16.3	14.4	11.7	10.8	4.9	4.2	1.5%	1.5%

Source: Powered by dataCentral *Using CY07E and CY08E (31-Dec year-ending).

GAIL's Pipeline Plans firmed up now

GAIL was the original advocate of the National Gas Grid in 2003-04 when Reliance gas supplies promised to become more meaningful. Subsequent to that, RIL decided and got approval for some of the strategically important and lucrative pipeline routes namely Kakinada-Uran, Kakinada-Chennai-Tuticorin and Kakinada-Haldia.

GAIL had to accordingly scale down its pipeline plans. The Government approved plans for 5 new pipelines and upgrades of 3 existing pipelines (at a total cost of Rs180bn) is now complementary to Reliance's pipeline plans. Though none of GAIL's pipelines are originating from Kakinada, we believe that the energy-hungry North & Western regions plus parts of South and East India will be eventually served by GAIL's gas pipelines. Reliance's MOU with GAIL to interconnect the two pipeline networks reflects that.

Figure 8. GAIL's Pipeline Projects

	Pipeline	Existing capacity (mmscmd)	Proposed increase (mmscmd)	Length	Cost (Rs bn)
Phase I by 2009					
	DVPL/GREP Upgradation	24	54	1115	22
	Dadri-Bawana-Nangal	-	25	610	25
	Chainsa-Jhajjar-Hissar	-	25	310	10
Phase II by 2011					
	DVPL/GREP Upgradation	54	74	1115	30
	Vijaipur-Jagadishpur upgrade	12	24	571	20
	Dabhol-Bangalore	-	12	730	25
	Kochi-Mangalore-Bangalore	-	12	840	25
	Jagadishpur-Haldia	-	12	876	20
Total		**90**	**238**	**5,052**	**177**

Source: Company Reports

Figure 9. Projects Completed

Project	Project cost (Rs bn)	Date of commissioning
Dahej Uran (DUPL)	18.3	May-07
Dabhol-Panvel (DPPL)	13.3	May-07
Jagoti-Pithampur p/l	2.0	Apr-07
Vijaipur-Kota p/l	3.0	Jan-07
Kelarus-Malanpur p/l	1.1	July-06
Thulendi-Phulpur p/l	2.2	May-06

Source: Company Reports

Figure 10. GAIL's Pipeline Network

Source: Citi Investment Research

City Gas could create value, but will take time

GAIL has also been gradually spreading its wings in the evolving city gas market in India with 8 existing JVs (with typically a 22.5% stake in OMCs). In addition, it has also signed MOUs to 28 more cities along the existing/new pipeline routes. GAIL has also recently approached the Government with firm plans for granting approval to pursue city gas projects in 230 cities across the country. Among these, only IGL and Mahanagar Gas have a meaningful size and estimated to contribute Rs18/share to GAIL's SOTP. As pointed out in earlier reports as well, city gas projects would take off once the trunk pipelines are commissioned, led by supply push, superior economics vis-à-vis crude-based fuels and the infrastructure push by Reliance, GAIL and OMCs.

With gas supplies on the increase, CGD infrastructure rollout could get more front-ended. As per the report of the Working Group on Petroleum & Natural Gas for XIth Plan, city gas (incl. industrial piped gas) demand is likely to increase from 11mmscmd currently to 16mmscmd by FY12E and 23mmscmd by FY17E. In addition, more than 70 new cities have also been identified with estimated demand of 11mmscmd by FY12E and 15mmscmd by FY17E.

However, IGL and MGL have taken 5-6 years to reach the present scale despite being in arguably the most lucrative markets of Delhi and Mumbai respectively. Notwithstanding the opportunity, it is a bit pre-mature to factor any value accretion for GAIL from the new/proposed city gas projects at this stage.

GAIL

Company description

GAIL is the dominant gas transmission and distribution company in India. Its arterial HBJ pipeline is India's largest. GAIL's other business divisions are LPG pipelines, LPG fractionation and petrochemicals.

Investment strategy

We have a Buy/Low Risk (1L) rating as GAIL provides a unique investment opportunity as a dominant gas pipeline owner and transporter in India. Increasing gas supplies and the reduced potential for falling pipeline charges remain the key positives. GAIL is also building 5 new pipelines and upgrading 3 existing pipelines in order to gear up for the imminent increase in gas supplies from the East Coast. Assured ROE on pipeline investments reduces risks and provides visibility for value creation from the additional investments of Rs180bn over next 4-5 years. GAIL has lower exposure to petroleum subsidies than its peers, and we expect the company's exposure to continue to be manageable. This should offset the adverse impact of a gas price hike on GAIL's internal consumption. The company's exposure to petrochemicals (ethylene chain) benefits from high prices of liquid feedstock as its feedstock prices are relatively stable and much lower than naphtha.

Valuation

Our target price for GAIL of Rs482 is based on a) Existing Business Value of Rs303 based on EV/EBITDA of 6.5x FY08E, b) the value of investments/E&P assets (Rs137/share) and c) value accretion from new pipelines at Rs36/share (based on P/B of 1.5x. The existing business value at Rs303 imputes FY08E PER of 10.5x and P/BV of 1.6x, reasonable given its growth outlook and ROEs. Given the increased potential of indigenous gas supplies from the East Coast basins (KG, Cauvery, Mahanadi) and GAIL’s now firm pipeline plans, we now explicitly factor in potential value accretion from the expansion capex. The value accretion from equity investments in new pipelines (50% of Rs180bn) is therefore calculated as 1.5x equity contribution less the equity contribution itself i.e. Rs90bn. The resultant value is discounted back by 4 years, assuming reasonable pipeline utilisation by FY13.

Risks

We rate GAIL as Low Risk based on our quantitative risk-rating system. The main risks that could impede the stock from reaching our target price are as follows: (1) a further cut in transportation tariffs; (2) GAIL's petrochemical business is cyclical in nature; (3) changes in government policy for the oil & gas sector will likely remain a risk to earnings and stock sentiment; and (4) any change in pricing of C2/C3 fractions of the rich gas, which acts as feedstock for GAIL's petrochemical/LPG units, could impact earnings.

Valuation & Risks: Other Companies

Indraprastha Gas (IGAS.BO - Rs142.65; 1L)

Valuation: Our target price of Rs160 for IGL is based on DCF. We prefer to use DCF, as it captures the value of the projects over their lifetime. IGL's near-term cash flow is affected by its aggressive expansion. In our DCF analysis, we have used explicit forecasts for four years, a terminal growth rate of 2%, and a WACC of 10.9% (based on a stock beta of 0.6). Our target P/CEPS of 8.2x FY09E is still at a small discount to current multiples of other gas utilities, which we believe is very reasonable given the higher capital returns parameters and lower regulatory scrutiny on margins. We prefer to use P/CEPS as a comparison due to the utility nature of IGL's business and the high depreciation rates on its assets.

Risks: We rate IGL Low Risk based on our quantitative risk-rating system. The downside risks to our target price include: (1) stronger than anticipated growth in alternative modes of public transport could impact CNG demand; (2) delays in conversion of LCVs to CNG could also impact demand; (3) further deregulation/hike in administered gas prices, with no corresponding hike in CNG prices, could put pressure on margins; and (4) delays in implementation of projects in the NCR region could impact PNG volume growth.

Gujarat Gas (GGAS.BO - Rs331.80; 1L)

Valuation: Our DCF-based valuation for Ggas is Rs350, on which our target price is based. Our DCF assumes a WACC of 11.0%, four years of explicit forecasts, and a terminal growth rate of 3% thereafter. We prefer DCF to value the company given the utility nature of the business, which ensures steady cash flows. Discounted cash flows also capture the value of the business over a longer term, given the new investments being made in the business and the longer-term growth opportunity for the retail gas distribution business in India. Our target price equates to a P/E of 14x 2008E, in-line with the BSE Sensex multiples. We believe this is justified due to the stable earnings profile and visible earnings growth.

Risks: We assign a Low Risk rating to Ggas based on our quantitative risk-rating system. Government/regulatory interference in gas pipeline tariffs could impact Ggas' earnings. The gas business typically involves take-or-pay clauses and Ggas' inability to sell gas contracted could lead to financial losses, while suppliers' inability to supply could lead to one-off gains. Some of Ggas' supply agreements are denominated in US$ terms, and therefore subject to currency fluctuation risks. Most of Ggas' purchased gas prices are linked to market prices of fuels. Sharp fluctuations in gas prices which Ggas is unable to pass on to its consumers could impact margins. GSPL's commissioning of a parallel pipeline in the Hazira-Ankleshwar section has impacted Ggas' transmission business. Reduction of gas supplies from GAIL could impact margins and profits adversely. If any of these risk factors has a greater impact than we expect, Ggas' share price will likely have difficulty attaining our target price. If market prices of natural gas come off sharply amid increased availability, Ggas' margins and earnings could be higher than our expectations.

Gujarat State Petronet (GSPT.BO - Rs70.50; 1M)

Valuation: Our target price of Rs74 is based on our DCF fair value for Sep-08E. Our DCF is based on gas volumes tied up with Reliance (11-20mmscmd) and the capex associated with the deal (Rs6bn). We use DCF to value the company given the utility nature of the business, which ensures steady cash flows. Discounted cash flows also capture the value of the business over a longer term. Our DCF valuation is based on five years of explicit forecasts, 23% CAGR of committed volumes over FY07-12E, FY12E volumes of 45mmscmd, and terminal growth of 3%. We use a WACC of 10.5% (risk free 8.0%, risk premium 6.0%, beta of 0.75, target D/E ~40%). Also, on a price/cash earnings basis, we think GSPL is at a justifiable premium to other gas utilities (9.6x FY09E) given our high growth expectations of its gas transmission business (EPS CAGR of 28% over FY07-10E). We prefer P/CEPS to the more traditional P/E multiple as a valuation benchmark given GSPL's aggressive depreciation policy.

Risks: We assign a Medium Risk rating to GSPL based on our quantitative risk-rating system. The key downside risks to our target price include: 1) Government regulation of gas pipeline tariffs - with the setting up of the Petroleum and Natural Gas Regulatory Authority, pipeline tariffs across India could come under scrutiny. 2) Gas supplies - we assume a 23% CAGR in gas volumes for GSPL. If supplies are lower than our expectations, this could impact earnings and valuations. 3) Project risk - GSPL is implementing expansion of its pipeline network that is subject to time and cost over-runs that could impact earnings. If any of these factors has a greater impact than we expect, the stock could have difficulty achieving our target price.

Petronet LNG (PLNG.BO - Rs92.40; 3M)

Valuation: Our target price of Rs78 is based on 10% discount to our DCF-based fair value estimate of Rs87 for March 2008. We believe a 10% discount is justified given the back-ended nature of the returns from the project. We use a DCF-based valuation, as we think it captures the value of the projects over their lifetime, especially given that PLL's near-term cash flow is affected by its aggressive expansion. In our DCF analysis, we have used explicit forecasts for 10 years, a terminal growth rate of 2%, and a WACC of 11.5%. On our target price, the stock would trade at 9.3x FY10E P/CEPS, in-line with other gas utilities, which have more stable and visible earnings growth.

Risks: We assign a Medium Risk rating for PLL based on our quantitative risk-rating system. Upside risks to our target price include: (1) higher utilization or faster commissioning of regassification capacities than assumed by us, (2) better acceptability of higher-priced LNG by the domestic market, and (3) power plans, albeit preliminary, could add value over the medium to long term.

Appendix A-1

Analyst Certification

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IMPORTANT DISCLOSURES

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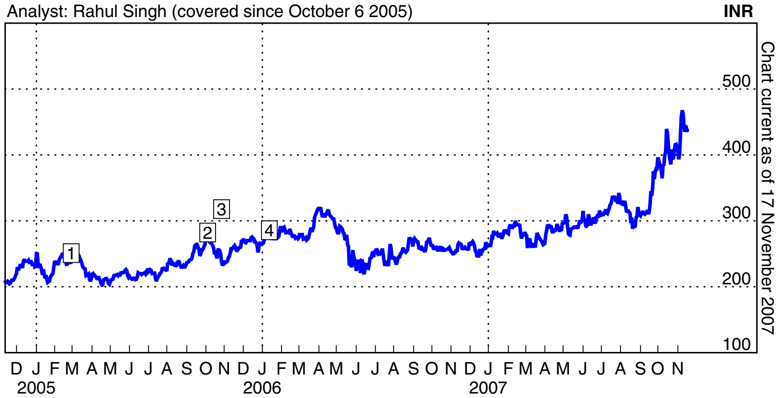
Ratings and Target Price History - Fundamental Research

Analyst: Rahul Singh (covered since October 6 2005)



Covered
Not covered

Rating/target price changes above reflect Eastern Standard Time

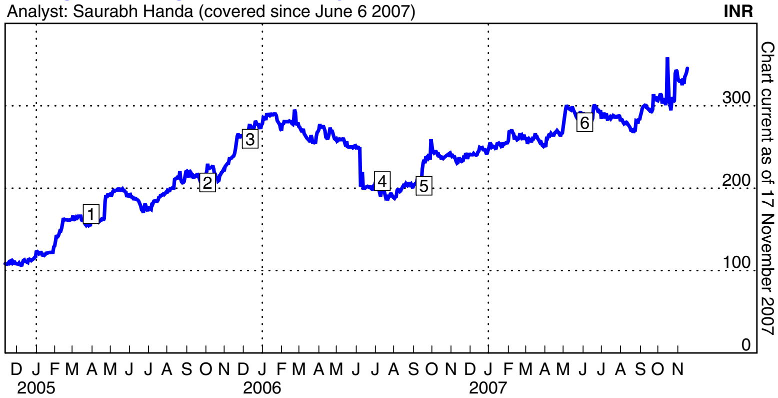
#	Date	Rating	Target Price	Closing Price
1:	28 Feb 05	2H	*275.00	241.00
2:	5 Oct 05	*1L	*329.00	275.95
3:	27 Oct 05	1L	*318.00	237.85
4:	12 Jan 06	1L	*323.00	282.70

*Indicates change.

Gujarat Gas (GGAS.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Saurabh Handa (covered since June 6 2007)



Covered
Not covered

Rating/target price changes above reflect Eastern Standard Time

#	Date	Rating	Target Price	Closing Price
1:	31 Mar 05	*2L	*172.00	168.71
2:	5 Oct 05	2L	*230.00	229.67
3:	13 Dec 05	2L	*300.00	276.12
4:	13 Jul 06	*1L	*250.00	198.34
5:	19 Sep 06	1L	*288.00	234.37
6:	5 Jun 07	1L	*350.00	287.75

*Indicates change.

Gujarat State Petronet (GSPT.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Saurabh Handa (covered since June 5 2007)

#	Date	Rating	Target Price	Closing Price
1:	31 Aug 06	1M	49.00	35.55
2:	28 Sep 06	1M	*55.00	38.35
3:	23 Jan 07	1M	*60.00	46.50
4:	13 Jun 07	1M	*72.00	54.80
5:	26 Oct 07	1M	*74.00	57.75

*Indicates change.

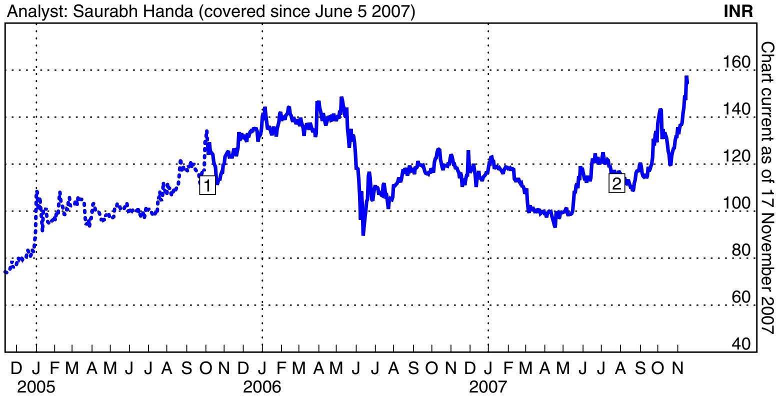
Covered
Not covered

Rating/target price changes above reflect Eastern Standard Time

Indraprastha Gas (IGAS.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Saurabh Handa (covered since June 5 2007)



#	Date	Rating	Target Price	Closing Price
1:	5 Oct 05	1L	156.00	128.50
2:	26 Jul 07	1L	*160.00	114.00

*Indicates change.

Covered
Not covered

Rating/target price changes above reflect Eastern Standard Time

Petronet LNG (PLNG.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Saurabh Handa (covered since June 6 2007)

#	Date	Rating	Target Price	Closing Price
1:	1 Apr 05	2H	49.00	42.05
2:	23 Sep 05	*1M	*74.00	58.75
3:	25 Sep 07	*3M	*78.00	86.30

*Indicates change.

Covered
Not covered

Rating/target price changes above reflect Eastern Standard Time

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