

Cut EPS and PO on cut in volumes and cash profit

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Cut in depreciation boosts 3Q and 9M profit; Retain Buy

3Q FY11 net profit of Gujarat State Petronet Ltd (GSPL) at Rs1.6bn is up 38% YoY. 3Q EBITDA is up just 4% YoY but profit growth is stronger due to depreciation being 96% YoY lower. Depreciation rate on pipelines has been cut from 8.33% to 4.75% w.e.f April 2010. Depreciation rate is likely to be further cut to 3.17% latest by FY12E. GSPL's 9M profit is 17% YoY higher despite EBITDA rise of just 7% YoY as depreciation is 15% YoY lower. We have cut GSPL's FY12E-13E EPS by 1-9% and PO by 13% due to cut in gas transmission volumes. Revised PO implies 41% potential upside. We retain Buy on GSPL.

3Q transmission tariff up 3% YoY and 10% QoQ; volumes flat

3Q EBITDA is 4% YoY higher driven by 3% YoY rise in tariff to Rs860/mscm. 3Q FY11 tariff is also 10% QoQ higher from Rs778/mscm in 2Q FY11. Transmission volumes at 35mmcmd are flat QoQ and YoY.

FY12-13E EPS cut by 1-9%; PO cut by 13% at Rs130/share

GSPL's gas growth in 9M is below expectation. We have consequently cut GSPL's gas transmission volumes for FY11E by 12% to 36mmcmd and for FY12-FY13E by 7-16% to 40.5-44.5mmcmd. We have also cut GSPL's FY11-FY13E depreciation by 39-54% following the cut in depreciation rate on pipelines. We are assuming depreciation rate on pipelines at 4.75% in FY11E and 3.17% in FY12-FY13E. The net impact of these changes is marginal rise in FY11E earnings and 1-9% cut in FY12E-FY13E EPS. GSPL is going to seek company law board permission to cut depreciation rate on pipelines to 3.17%. The permission may come before 4Q results are announced or in FY12E. If it gets permission in FY11E, FY11E EPS would be 7% higher at Rs8.9. We have also cut GSPL's PO by 13% to Rs130/share from Rs149/share to factor in impact of cut in volumes and cash profit.

Estimates (Mar)

(Rs)	2009A	2010A	2011E	2012E	2013E
Net Income (Adjusted - mn)	1,234	4,049	4,653	5,355	5,908
EPS	2.20	7.20	8.27	9.52	10.50
EPS Change (YoY)	21.4%	227.9%	14.9%	15.1%	10.3%
Dividend / Share	0.750	1.00	2.00	2.00	2.00
Free Cash Flow / Share	(5.37)	1.15	(1.63)	9.93	3.96

Valuation (Mar)

	2009A	2010A	2011E	2012E	2013E
P/E	42.04x	12.82x	11.16x	9.70x	8.79x
Dividend Yield	0.813%	1.08%	2.17%	2.17%	2.17%
EV / EBITDA*	13.83x	6.30x	5.97x	5.40x	4.89x
Free Cash Flow Yield*	-5.81%	1.24%	-1.77%	10.76%	4.29%

* For full definitions of *iQmethod*SM measures, see page 5.

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Refer to important disclosures on page 6 to 8. Analyst Certification on Page 4. Price Objective Basis/Risk on page 4. Link to Definitions on page 4. 11019757

Stock Data

Price	Rs92.30
Price Objective	Rs130.00
Date Established	11-Feb-2011
Investment Opinion	C-1-7
Volatility Risk	HIGH
52-Week Range	Rs81.95-Rs128.25
Mrkt Val / Shares Out (mn)	US\$1,135 / 562.1
Average Daily Volume	1,738,862
BofAML Ticker / Exchange	GJRSF / BSE
Bloomberg / Reuters	GUJS IN / GSPT.BO
ROE (2011E)	26.9%
Net Dbt to Eqty (Mar-2008A)	69.4%
Est. 5-Yr EPS / DPS Growth	NA / NA
Free Float	60.9%

Key Changes

(Rs)	Previous	Current
Price Obj.	149.00	130.00
2011E EBITDA (m)	11,069.3	9,839.2
2012E EBITDA (m)	12,906.5	10,871.7
2013E EBITDA (m)	12,936.9	11,995.8

11 February 2011

iQprofileSM Gujarat State Petronet Ltd

Key Income Statement Data (Mar)	2009A	2010A	2011E	2012E	2013E
(Rs Millions)					
Sales	4,875	9,920	10,561	11,520	12,583
Gross Profit	4,245	9,325	9,839	10,872	11,996
Sell General & Admin Expense	NA	NA	NA	NA	NA
Operating Profit	2,540	6,960	7,838	9,215	10,133
Net Interest & Other Income	(627)	(780)	(788)	(1,102)	(1,182)
Associates	NA	NA	NA	NA	NA
Pretax Income	1,914	6,180	7,051	8,113	8,952
Tax (expense) / Benefit	(679)	(2,131)	(2,397)	(2,758)	(3,044)
Net Income (Adjusted)	1,234	4,049	4,653	5,355	5,908
Average Fully Diluted Shares Outstanding	562	562	562	562	562

Key Cash Flow Statement Data

Net Income	1,234	4,049	4,653	5,355	5,908
Depreciation & Amortization	1,705	2,365	2,001	1,656	1,862
Change in Working Capital	1,521	(1,866)	1,145	2,564	(203)
Deferred Taxation Charge	145	261	987	1,136	1,253
Other Adjustments, Net	(3,042)	3,821	(2,291)	(5,129)	405
Cash Flow from Operations	1,563	8,630	6,496	5,582	9,227
Capital Expenditure	(4,579)	(7,984)	(7,413)	0	(7,001)
(Acquisition) / Disposal of Investments	NA	NA	NA	NA	NA
Other Cash Inflow / (Outflow)	0	(310)	0	(5,000)	(5,000)
Cash Flow from Investing	(4,579)	(8,294)	(7,413)	(5,000)	(12,001)
Shares Issue / (Repurchase)	2	5	0	0	0
Cost of Dividends Paid	(475)	(634)	(1,268)	(1,268)	(1,268)
Cash Flow from Financing	1,385	456	1,136	(1,268)	2,732
Free Cash Flow	(3,017)	646	(917)	5,582	2,226
Net Debt	10,535	10,854	13,039	13,725	17,768
Change in Net Debt	3,491	294	2,185	686	4,043

Key Balance Sheet Data

Property, Plant & Equipment	24,132	29,755	35,167	33,510	38,649
Other Non-Current Assets	356	666	666	5,666	10,666
Trade Receivables	544	753	1,447	1,578	1,724
Cash & Equivalents	975	1,742	1,961	1,275	1,232
Other Current Assets	4,130	5,058	3,106	5,992	6,144
Total Assets	30,137	37,973	42,346	48,021	58,415
Long-Term Debt	11,079	12,565	15,000	15,000	19,000
Other Non-Current Liabilities	1,144	1,405	2,392	3,528	4,781
Short-Term Debt	430	30	0	0	0
Other Current Liabilities	5,331	8,334	5,931	6,384	6,883
Total Liabilities	17,985	22,335	23,323	24,912	30,665
Total Equity	12,152	15,638	19,023	23,109	27,749
Total Equity & Liabilities	30,137	37,973	42,346	48,021	58,414

iQmethodSM - Bus Performance*

Return On Capital Employed	7.7%	17.1%	16.1%	16.0%	14.7%
Return On Equity	10.5%	29.1%	26.9%	25.4%	23.2%
Operating Margin	52.1%	70.2%	74.2%	80.0%	80.5%
EBITDA Margin	87.1%	94.0%	93.2%	94.4%	95.3%

iQmethodSM - Quality of Earnings*

Cash Realization Ratio	1.3x	2.1x	1.4x	1.0x	1.6x
Asset Replacement Ratio	2.7x	3.4x	3.7x	0x	3.8x
Tax Rate (Reported)	35.5%	34.5%	34.0%	34.0%	34.0%
Net Debt-to-Equity Ratio	86.7%	69.4%	68.5%	59.4%	64.0%
Interest Cover	2.9x	7.4x	7.8x	7.0x	7.2x

Key Metrics

* For full definitions of iQmethodSM measures, see page 5.

Company Description

Gujarat State Petronet (GSPL) was promoted in 1998 by Gujarat government-owned companies led by Gujarat State Petroleum Corp (38% stake). It has a 1,283km pipeline network in Gujarat. It transmitted 15mmcmd of gas in FY09. Volumes are set surge sharply in FY10E. It has agreement with Reliance to transmit 11mmcmd (may rise to 14-20mmcmd) of gas from Bharuch to Jamnagar. Its volumes are mainly from KG D6 gas, Dahej and Hazira LNG terminals. Its main customers are Reliance, Torrent and Essar

Investment Thesis

GSPL offers the strongest volume and earnings growth among gas utilities. Uncertainty in GSPL is also relatively less than for peers. GSPL offers the best pipeline connectivity in Gujarat, which is and will remain the largest gas consuming state in India. Most of the incremental gas in India will be from RIL. Only GSPL has a firm transportation agreement with RIL, which will mean 65-118pct rise in volumes over FY08 levels. Another volume driver may be gas discovery by GSPC, its parent. Buy

Stock Data

Price to Book Value 2.7x

GSPL 3Q FY11 result

Table 1: 3Q and 9M FY11 results

Rsmn	3Q FY11	3Q FY10	Change	9M FY11	9M FY10	Change
Net sales	2,795	2,685	4%	7,885	7,341	7%
Total expenditure	172	154	12%	517	424	22%
EBDITA	2,623	2,531	4%	7,368	6,916	7%
EBDITA margin	94%	94%		93%	94%	
Interest	259	218	19%	725	713	2%
Depreciation	25	596	-96%	1,472	1,732	-15%
Other Income	50	33	53%	148	127	17%
Extra-ordinary items	0	0	NM	0	38	NM
PBT	2,389	1,750	37%	5,319	4,635	15%
Current tax	399	569	-30%	1,059	1,486	-29%
Deferred tax	399	28	1348%	703	90	682%
PAT	1,591	1,154	38%	3,557	3,059	16%
Recurring PAT	1,591	1,154	38%	3,557	3,033	17%
EPS	2.8	2.1	38%	6.3	5.4	16%
Recurring EPS	2.8	2.1	38%	6.3	5.4	17%

Source: Company, BofA Merrill Lynch Global Research

GSPL's 3Q and 9M FY11 volumes and tariff

Table 2: GSPL's volumes and tariff in 3Q and 9M FY11

	3Q FY11	3Q FY10	Change	9M FY11	9M FY10	Change
Volumes (mmscmd)	35	35	1%	36	31	17%
Tariff (Rs/mscm)	860	831	3%	804	874	-8%

Source: Company, BofA Merrill Lynch Global Research

GSPL's FY12-13E EPS cut by 1-9%

Table 3: GSPL's FY12-13E EPS cut by 1-9%

Rs/share	FY11E	FY12E	FY13E
Revised EPS	8.3	9.5	10.5
Old EPS	8.2	10.5	10.6
Change	0%	-9%	-1%

Source: BofA Merrill Lynch Global Research

GSPL's PO cut by 13% at Rs130/share

Table 4: GSPL's PO cut by 13%

Rs/share	PO
Revised	130
Old	149
Change	-13%

Source: BofA Merrill Lynch Global Research

Price objective basis & risk Gujarat State Petronet Ltd (GJRSE)

Our PO of GSPL is Rs130/share. This includes Rs94/share as DCF value of GSPL existing gas pipeline network in Gujarat. PO also includes Rs36/share as value of Mallavaram-Bhilwara, Mehsana-Bhatinda and Bhatinda-Jammu pipeline for which it has won bid. WACC is 10pct based on 11.5pct cost of equity, 9.5pct cost of debt, 17pct tax and debt-equity of 67pct. We have assumed gas transmission volume CAGR of 11.6pct in FY10-FY13E. Gas transmission tariff is assumed to decline at a CAGR of 3% in FY10-FY13E. We prefer DCF to value GSPL. Downside risks: 1) Regulatory risk in the form of regulator requiring GSPL to cut tariff. 2) Lower than expected gas transmission volumes 3) NPV of Mallavaram-Bhilwara, Mehsana-Bhatinda and Bhatinda-Jammu pipelines being lower than assumed (bid details not available)

Link to Definitions

Energy

Click [here](#) for definitions of commonly used terms.

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11 February 2011

India - Engineering/Construction/Utilities Coverage Cluster

Investment rating	Company	BofA Merrill Lynch ticker	Bloomberg symbol	Analyst
BUY				
	Adani Enterprises Ltd.	ANIEF	ADE IN	Bharat Parekh
	Adani Power Ltd.	XADPF	ADANI IN	Bharat Parekh
	Bharat Heavy	BHHEF	BHEL IN	Bharat Parekh
	Essar Shipping, Ports & Logistics Ltd.	XESSF	ESRS IN	Bharat Parekh
	Gujarat State Petronet Ltd	GJRSF	GUJS IN	Vidyadhar Ginde
	GVK Power & Infrastructure Ltd.	GVPWF	GVKP IN	Deepak Agrawala
	IRB Infrastructure Developers Ltd.	XIRBF	IRB IN	Bharat Parekh
	IVRCL Infrastruc	IIFRF	IVRC IN	Bharat Parekh
	Jaiprakash Associates Limited	JPRKF	JPA IN	Bharat Parekh
	Jaiprakash Power Ventures Ltd.	XJSHF	JPVL IN	Bharat Parekh
	Lanco Infratech Ltd.	LNIFF	LANCI IN	Deepak Agrawala
	Larsen & Toub -G	LTORF	LTOD LI	Bharat Parekh
	Larsen & Toubro	LTOUF	LT IN	Bharat Parekh
	Mundra Port SEZ	XMANF	MSEZ IN	Bharat Parekh
	Nagarjuna Const	NGRJF	NJCC IN	Bharat Parekh
	NCC-GDR	XAKUF	NJGR LX	Bharat Parekh
	Reliance Infrastructure	RCTDF	RELI IN	Bharat Parekh
	Suzlon Energy	XZULF	SUEL IN	Bharat Parekh
NEUTRAL				
	GMR Infrastructure Ltd.	GMRLF	GMRI IN	Deepak Agrawala
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	Neyveli Lignite	NEYVF	NLC IN	Bharat Parekh
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	Gail Limited - G	GAILF	GAID LI	Vidyadhar Ginde
	NTPC Ltd	NTHPF	NATP IN	Bharat Parekh

iQmethodSM Measures Definitions

Business Performance	Numerator	Denominator
Return On Capital Employed	$\text{NOPAT} = (\text{EBIT} + \text{Interest Income}) * (1 - \text{Tax Rate}) + \text{Goodwill Amortization}$	$\text{Total Assets} - \text{Current Liabilities} + \text{ST Debt} + \text{Accumulated Goodwill Amortization}$
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	$\text{Net Debt} = \text{Total Debt, Less Cash \& Equivalents}$	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	$\text{EV} = \text{Current Share Price} * \text{Current Shares} + \text{Minority Equity} + \text{Net Debt} + \text{Other LT Liabilities}$	
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

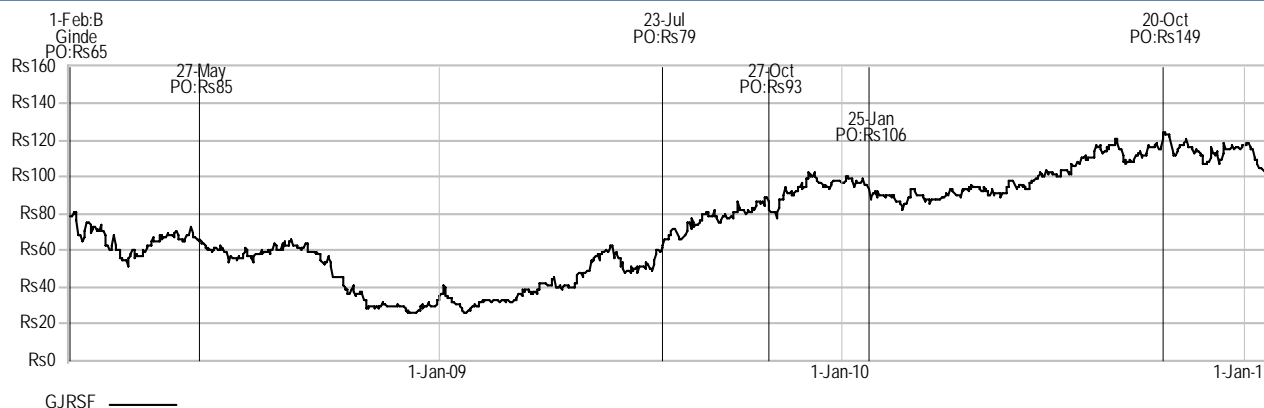
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GJRSF Price Chart



B : Buy, N : Neutral, S : Sell, U : Underperform, PO : Price objective, NA : No longer valid, NR: No Rating

Prior to May 31, 2008, the investment opinion system included Buy, Neutral and Sell. As of May 31, 2008, the investment opinion system includes Buy, Neutral and Underperform. Dark Grey shading indicates that a security is restricted with the opinion suspended. Light grey shading indicates that a security is under review with the opinion withdrawn. The current investment opinion key is contained at the end of the report. Chart is current as of January 31, 2011 or such later date as indicated.

Investment Rating Distribution: Utilities Group (as of 01 Jan 2011)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	74	39.57%	Buy	30	46.15%
Neutral	56	29.95%	Neutral	33	63.46%
Sell	57	30.48%	Sell	17	33.33%

Investment Rating Distribution: Global Group (as of 01 Jan 2011)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	2011	53.86%	Buy	874	48.31%
Neutral	925	24.77%	Neutral	444	52.30%
Sell	798	21.37%	Sell	276	36.75%

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