February 26, 2010

Petronet LNG Limited (PETLNG)

Rs 71

De-risked business at discounted valuation…

Rating Matrix		
Rating	:	**Strong Buy**
Target	:	Rs 88
Target Period	:	12 months
Potential Upside	:	24%

YoY Growth (%)

	FY09	FY10E	FY11E	FY12E	FY13E
Revenues	28.6	28.9	29.1	33.8	36.3
EBITDA	4.1	-2.0	22.3	8.4	20.6
Net Profit	9.2	-19.8	17.3	5.4	14.4

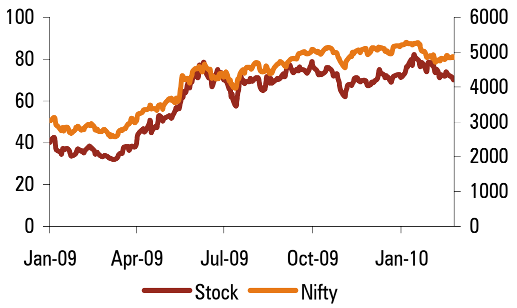
Stock Metrics

Bloomberg Code	PLNG IN
Reuters Code	PLNG.BO
Face value (Rs)	10
Promoters Holding	50%
Market Cap (Rs cr)	5325
52 week H/L	82.9 / 31.6
Sensex	16254
Average volumes	794027

Comparative return matrix (%)

Company	1M	3M	6M	12M
Petronet LNG	-7	2	1	113
Gujarat Gas	0	0	31	131
GSPL	-9	-12	12	169
Indraprastha Gas	4	21	29	104

Price movement (Stock vs. Nifty)



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Petronet LNG is India's premier company in the hydrocarbon sector involved in receiving and regasification of LNG to meet the increasing demand for natural gas in the country. We expect Petronet's LNG regasification volume to increase at 16.2% CAGR over FY09-13E to 11.3 MMTPA on account of the increase in Dahej capacity and commissioning of the Kochi terminal. We believe that concerns on regasification charges are overdone and would not come under regulatory purview at least in the next two or three years. We expect Petronet LNG to report a CAGR of 32% and 3.2% in revenues and net profit, respectively, over FY09-13E. We are initiating coverage on Petronet LNG with a STRONG BUY rating and a price target of Rs 88.

Gas deficit to persist despite increase in domestic gas production

The increasing demand for natural gas in India would outpace the supply over FY09-14E despite the increase in domestic gas production from the KG and Mahanadi basin. Petronet LNG would benefit from the natural gas deficit in India by enhancing its LNG regasification capacity.

LNG regasification volume to increase at 16.2% CAGR over FY09-13E

The increase in Dahej regasification capacity from 5 MMTPA to 10 MMTPA in FY10 and commissioning of the new 2.5 MMTPA Kochi terminal in FY13E would increase Petronet's LNG regasification volume at 16.2% CAGR over FY09-13E. We expect Petronet LNG's volume to increase from 6.2 MMTPA in FY09 to 11.3 MMTPA in FY13E.

Concerns on regulation of regasification charges overdone

We believe concerns on regulation of regasification charges are overdone. Our interaction with the management suggests PNGRB would not bring regasification charges under purview at least for the next two or three years. On a conservative basis, we expect blended net regasification margin to decline from Rs 32.8/mmbtu in FY09 to Rs 29/mmbtu in FY13E.

Valuations

Petronet LNG's business of receiving and regasification of LNG along with back-to-back long-term purchase and sales agreement offers a lot of safety for investors. We have valued Petronet LNG based on the DCF methodology to arrive at a price target of Rs 88 (WACC – 10.5%, terminal growth – 2%). We recommend **STRONG BUY** rating on the stock, with a potential upside of 24%.

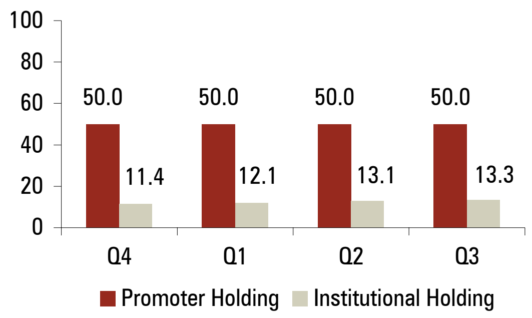
Exhibit 1: Key Financials

Year to March 31	FY08	FY09	FY10E	FY11E	FY12E	FY13E
Operating Revenues (Rs Crore)	6555.3	8428.7	10867.4	14031.0	18777.4	25591.4
EBITDA (Rs Crore)	866.2	901.3	883.6	1080.9	1172.0	1412.9
Net Profit (Rs Crore)	474.7	518.4	415.7	487.7	514.0	588.0
Shares in Issue (In Crore)	75.0	75.0	75.0	75.0	75.0	75.0
EPS (Rs)	6.3	6.9	5.5	6.5	6.9	7.8
P/E (x)	11.2	10.3	12.8	10.9	10.4	9.1
Price/Book Value (x)	3.3	2.7	2.4	2.1	1.9	1.6
EV/EBITDA (x)	7.6	7.7	8.2	7.6	7.6	5.9
RONW (%)	29.3	26.1	18.5	19.1	17.9	18.1
ROCE (%)	23.9	18.7	16.3	15.3	14.4	16.4

Source: Company, ICICIdirect.com Research

Shareholding pattern (Q3FY10)	
Shareholder	**% holding**
Promoters	50.0
Institutional investors	13.3
Other investors	10.0
General public	26.8

Promoter and institutional holding trend (%)



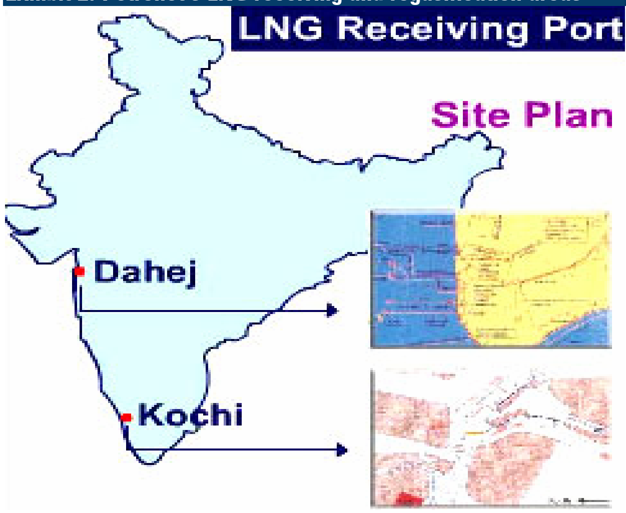
Company Background

Petronet LNG Ltd, India's premier company in the hydrocarbon sector, was set up by the Government of India to meet the increasing demand for natural gas and enhance the energy security of the country. Petronet LNG was incorporated on April 2, 1998 to import LNG and set up LNG terminals in the country.

Petronet LNG is a joint venture between GAIL, ONGC, IOC and BPCL, with each of them having a 12.5% stake in the company. GAZ de France (GdF), the French national company, with vast experience in the import of LNG is Petronet LNG's strategic partner and holds 10% equity in the company.

Petronet LNG commissioned India's first LNG receiving and regasification terminal at Dahej with a capacity of 5 MMTPA in April 2004. This has been expanded to 10 MMTPA in July 2009. Petronet has signed a sale & purchase agreement (SPA) with RasGas for 7.5 MMTPA LNG for a period of 25 years. Petronet is constructing another LNG terminal at Kochi with a capacity of 2.5 MMTPA (expandable to 5 MMTPA), expected to be commissioned by Q1FY13. The company has signed an agreement with Exxon Mobil for the supply of 1.5 MMTPA LNG from the Gorgon project of Australia for the LNG terminal at Kochi over a period of 20 years. Petronet LNG also plans to set up an integrated power plant with a capacity of 1068 MW at Dahej. The company is currently in the process of land acquisition, preparing a detailed feasibility report and acquiring environmental clearances.

Exhibit 2: Petronet's LNG receiving and regasification areas



Source: Company, ICICIdirect.com Research

Exhibit 3: Glossary & Conversion factors

1 MMSCM	=	36359 MMBTU
1 MMSCMD	=	0.255 MMTPA
1 MMTPA	=	3.9 MMSCMD
1 MMTPA	=	52000000 MMBTU
MMBTU		million metric british thermal unit
MMSCM		million metric standard cubic meter
MMSCMD		million metric standard cubic meter per day
MMTPA		million metric tonne per annum
TBTU		trillion british thermal unit

Source: ICICIdirect.com Research

Investment Rationale

Petronet LNG is India's premier company in the hydrocarbon sector involved in receiving and regasification of LNG to meet the increasing demand for natural gas in the country. Petronet LNG's back-to-back long-term purchase and sales agreement offers a lot of safety for investors. We expect Petronet's LNG regasification volume to increase at 16.2% CAGR over FY09-13E to 11.3 MMTPA on account of the increase in Dahej capacity and commissioning of the Kochi terminal. We believe that concerns on regasification charges are overdone and would not come under regulatory purview at least in the next two or three years. We believe Petronet LNG's revenues would increase at 32% CAGR over FY09-13E from Rs 8,429 crore in FY09 to Rs 25,591 crore in FY13E. The net profit will increase at 3.2% CAGR over FY09-13E from Rs 518 crore in FY09 to Rs 588 crore in FY13E.

Gas deficit to persist despite increase in domestic gas production

The demand for natural gas has continuously outpaced the supply in India. We expect the natural gas deficit in India to persist over FY09-14E despite an increase in domestic gas production from new discoveries in the KG and Mahanadi basin. The natural gas demand-supply mismatch would be met by the import of LNG in the country. Petronet LNG would benefit from the natural gas deficit in India by enhancing its LNG receiving and regasification capacity. We expect the natural gas deficit to be in the range of 37.9 mmscmd to 59.9 mmscmd over the next five years.

We expect natural gas demand to grow at 10.2% CAGR over FY09-13E from 139.1 mmscmd in FY09 to 225.9 mmscmd in FY14E. The increase in gas demand at 28.8% and 15.1% CAGR over FY09-FY14E for city gas distribution and captive power plants, respectively, will primarily lead the demand growth. We expect the demand for the power and fertiliser sector to be 83.2 mmscmd and 52.9 mmscmd, respectively, in FY14E.

Natural gas demand in India will grow at 10.2% CAGR over FY09-13E from 139.1 mmscmd in FY09 to 225.9 mmscmd in FY14E

Exhibit 4: Natural gas demand in India (mmscmd)

Demand	FY09	FY10E	FY11E	FY12E	FY13E	FY14E	CAGR
Power	61.4	72.5	75.1	75.2	81.1	83.2	**6.3%**
Fertiliser	37.0	38.6	40.1	44.3	47.2	52.9	**7.4%**
Captive Power	12.4	14.2	16.3	19.1	21.9	25.0	**15.1%**
City Gas Distribution	9.1	11.4	15.3	18.8	24.8	32.2	**28.8%**
Refinery	8.3	10.5	10.6	11.6	13.5	13.6	**10.4%**
Petrochemicals	6.7	6.7	6.7	6.7	11.3	11.3	**11.0%**
Sponge iron	4.4	5.0	6.2	7.4	7.6	7.7	**11.8%**
Total demand	**139.1**	**158.9**	**170.3**	**183.0**	**207.3**	**225.9**	**10.2%**

Source: Crisil Report, ICICIdirect.com Research

Domestic gas supply is expected to increase at 18.8% CAGR over FY09-14E from 74.3 mmscmd in FY09 to 175.7 mmscmd in FY14E

However, domestic gas supply would be unable to keep pace with increased gas demand despite an increase in domestic gas production from new discoveries in the KG and Mahanadi basin. The domestic gas supply is expected to increase at 18.8% CAGR over FY09-14E from 74.3 mmscmd in FY09 to 175.7 mmscmd in FY14E.

Exhibit 5: Domestic natural gas supply in India (mmscmd)

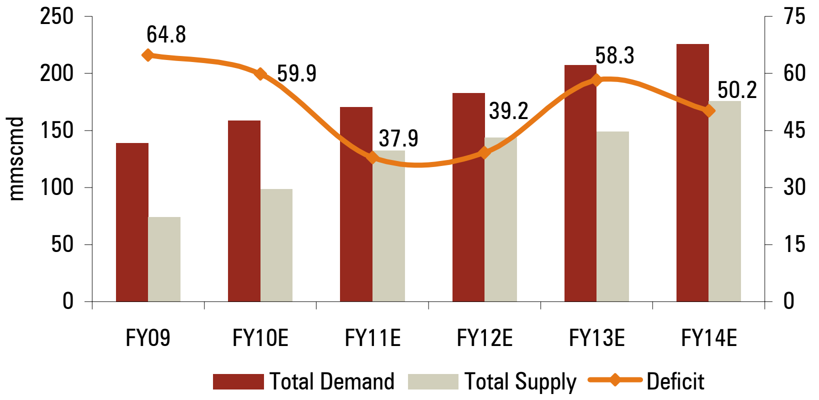
Supply	FY09	FY10E	FY11E	FY12E	FY13E	FY14E	CAGR
ONGC	51.0	44.9	38.9	37.2	37.3	41.4	-4.1%
Oil India	5.1	5.1	5.1	5.1	5.1	5.1	0.0%
PMT existing fields	13.8	14.5	14.6	14.5	14.4	14.4	0.9%
Other existing fields	4.4	4.1	3.8	3.6	3.4	3.2	-6.2%
Reliance Industries	0.0	30.4	70.0	80.0	84.0	106.0	NA
Other new fields	0.0	0.0	0.0	3.4	4.8	5.6	NA
Total Supply	**74.3**	**99.0**	**132.4**	**143.8**	**149.0**	**175.7**	**18.8%**

Source: Crisil Report, ICICIdirect.com Research

Natural gas deficit in India will persist despite an increase in domestic gas production

The natural gas deficit (in the range of 37.9 mmscmd to 59.9 mmscmd over the next five years) would be met by LNG players. Petronet LNG would benefit from the natural gas deficit in India by enhancing its LNG receiving and regasification capacity. Petronet LNG's back-to-back long-term purchase and sales agreement with LNG exporters and regasified gas offtakers, respectively, and additional demand for spot LNG from the Indian industry would ensure strong volume growth over the next few years.

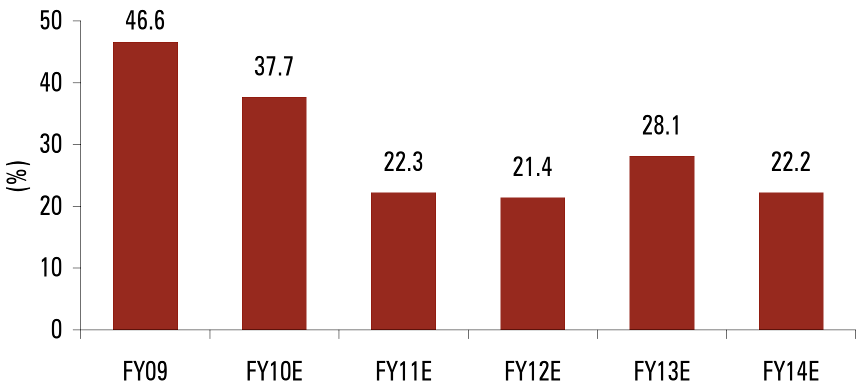
Exhibit 6: Natural gas demand-supply outlook in India



Source: Crisil Report, ICICIdirect.com Research

A widening of the natural gas demand-supply gap above our estimates may rejuvenate spot LNG demand

Exhibit 7: Natural gas deficit as a percentage of demand



Source: Crisil Report, ICICIdirect.com Research

We expect Petronet LNG to plug 42.3 mmscmd of natural gas deficit in FY13E

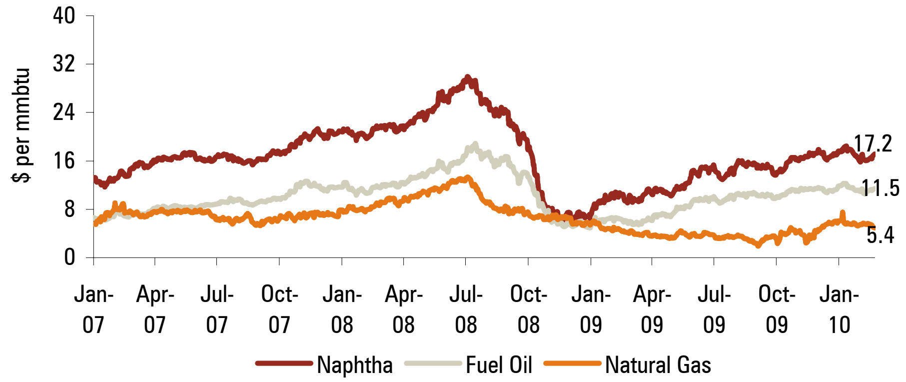
We believe LNG demand would continue to remain strong even if the natural gas deficit as a percentage of demand declines as LNG has better competitiveness vis-à-vis other competitive fuels such as naphtha and fuel oil. The current traded prices of naphtha, fuel oil and henry hub natural gas are $17.2, $11.5 and $4.9, respectively

Exhibit 8: LNG capacity available in India (mmscmd)

	FY09	FY10E	FY11E	FY12E	FY13E	FY14E
Petronet (Dahej)	24.4	37.5	37.5	37.5	37.5	37.5
Shell (Hazira)	13.5	13.5	13.5	13.5	13.5	13.5
Dabhol (Ratnagiri)	0.0	0.0	7.5	7.5	7.5	7.5
Petronet (Kochi)	0.0	0.0	0.0	0.0	9.4	9.4
Total	**37.9**	**51.0**	**58.5**	**58.5**	**67.9**	**67.9**

Source: ICICIdirect.com Research

Exhibit 9: Competitiveness of natural gas compared to other alternative fuels



Source: Bloomberg, ICICIdirect.com Research

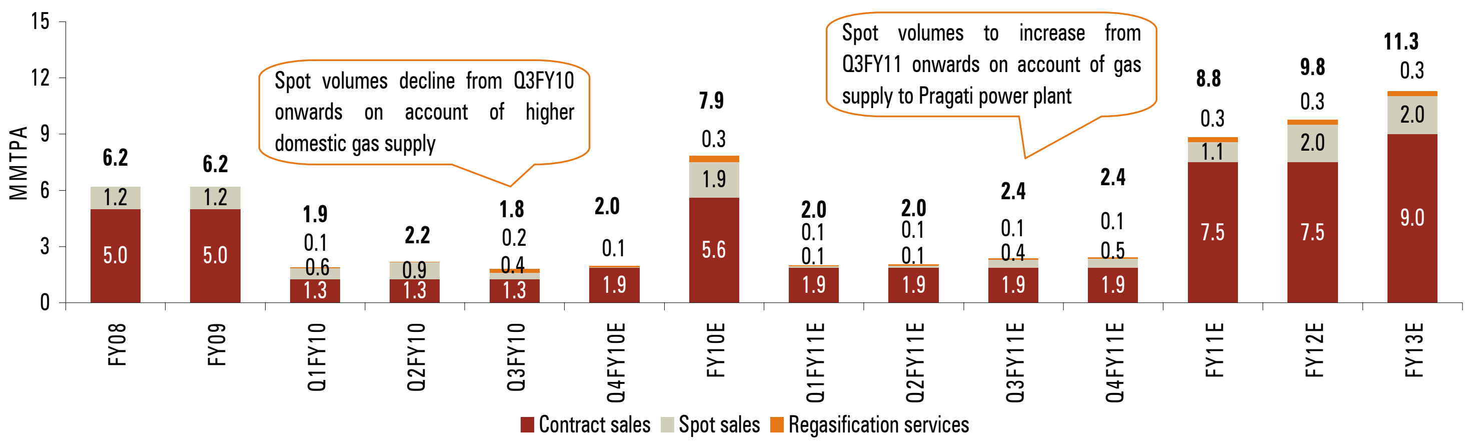
LNG regasification volume to increase at 16.2% CAGR over FY09-13E

Petronet LNG's regasification volume will increase at 16.2% CAGR over FY09-13E from 6.2 MMTPA in FY09 to 11.3 MMTPA in FY13E

The increase in Dahej regasification capacity from 5 MMTPA to 10 MMTPA in FY10 and commissioning of the new 2.5 MMTPA Kochi terminal in FY13E would increase Petronet's LNG regasification volume at 16.2% CAGR over FY09-13E.

Petronet LNG has signed a long-term contract with RasGas, Qatar for import of 7.5 MMTPA LNG for a period of 25 years. It has signed back-to-back sales agreement for this contracted volume with three offtakers i.e. GAIL, IOC and BPCL in the ratio of 60:30:10, respectively. For the new 2.5 MMTPA Kochi terminal, Petronet LNG has signed an agreement with Exxon Mobil for the supply of 1.5 MMTPA LNG from the Gorgon project of Australia over a period of 20 years. These agreements with RasGas and Exxon Mobil would increase the company's contracted volume from 5 MMTPA in FY09 to 9 MMTPA in FY13E.

Exhibit 10: Petronet's LNG regasification volume



Source: Company, ICICIdirect.com Research

Exhibit 11: Offtake of contracted volume for Dahej and Kochi terminals

Offtakers	Dahej Terminal		Kochi Terminal	
	Qty (MMTPA)	%	Qty (MMTPA)	%
GAIL	4.50	60.0	0.45	30.0
IOC	2.25	30.0	0.45	30.0
BPCL	0.75	10.0	0.60	40.0
Total	**7.50**	**100.0**	**1.50**	**100.0**

Source: Company, ICICIdirect.com Research

The increased domestic gas supply volume from the Reliance KG-D6 basin has led to a decline in Petronet's LNG spot volume to 0.4 MMTPA in Q3FY10. We expect a marginal spot volume in the next three quarters on account of the increasing domestic gas supplies. The supply of 1 MMTPA volume to the Pragati power plant from Q3FY11 onwards would mainly contribute to Petronet LNG's spot volumes, going forward. We have conservatively assumed spot volumes of 2 MMTPA in FY13E taking into account increased domestic gas supplies from new discoveries in the KG basin and Mahanadi basin. We expect Petronet's LNG regasification volume to increase from 6.2 MMTPA in FY09 to 11.3 MMTPA in FY13E.

Gross regasification margin on contracted sales will improve from Rs 29.2 per mmbtu in FY09 to Rs 36.1 per mmbtu in FY13E while margin on spot sales would remain at Rs 25 per mmbtu

Concerns on regulation of regasification charges overdone

We believe concerns on regulation of regasification charges are overdone. Our interaction with the management suggests PNGRB would not bring regasification charges under purview at least in the next two or three years. We expect the gross regasification margin on contracted sales for the Dahej terminal to increase by 5% each year till 2012 and remain flat at Rs 33.35 per mmbtu from FY13. The gross margin for the Dahej terminal would increase from Rs 30.25 per mmbtu in 2009 to Rs 33.35 per mmbtu in 2013. For the new 2.5 MMTPA Kochi terminal, we have assumed gross regasification margin of Rs 50 per mmbtu in FY13E. Overall, we expect the gross regasification margin on contracted sales to improve from Rs 29.2 per mmbtu in FY09 to Rs 36.1 per mmbtu in FY13E.

Exhibit 12: Petronet LNG's regasification margin (Rs per mmbtu)

	FY08	FY09	FY10E	FY11E	FY12E	FY13E
Gross regasification margins on contracted sales	27.8	29.2	30.8	32.2	33.3	36.1
Margins on spot sales	54.2	62.3	18.6	25.0	25.0	25.0
Margins on regasification services	NA	NA	27.8	25.0	25.0	25.0
Blended net regasification margins	30.7	32.8	25.1	27.5	27.4	29.0

Source: Company, ICICIdirect.com Research

Petronet LNG's margins on spot sales have declined to Rs 18.6 per mmbtu in 9MFY10 from Rs 62.3 per mmbtu in FY09 on account of an increase in domestic gas supply volumes. Going forward, we have conservatively modelled Petronet LNG's margins on spot sales at Rs 25 per mmbtu from FY11E. On a consolidated basis, we expect blended net regasification margins to decline from Rs 32.8 per mmbtu in FY09 to Rs 29 per mmbtu in FY13E.

Higher prices for sourcing LNG on account of linkage to JCC prices

Petronet's LNG purchase price would increase from $4.8 per mmbtu in FY09 to $9.4 per mmbtu in FY13E on account of linkage to the Japanese Cocktail Crude (JCC) prices. This would lead to an increase in sales price of regasified LNG from $5.6 per mmbtu in FY09 to $10.2 per mmbtu in FY13E assuming our blended net regasification margins are in the range of Rs 25.1 –32.8 per mmbtu over FY09-13E ($0.54 - $.71 per mmbtu).

Exhibit 13: Break-up of sourcing of LNG (MMTPA)

	FY08	FY09	FY10E	FY11E	FY12E	FY13E
Dahej contracted volume	5.0	5.0	5.6	7.5	7.5	7.5
Kochi contracted volume	0.0	0.0	0.0	0.0	0.0	1.5
Spot volume	1.2	1.4	2.0	1.2	1.2	2.2
Total	**6.2**	**6.4**	**7.6**	**8.7**	**8.7**	**11.2**

Source: Company, ICICIdirect.com Research

Exhibit 14: Petronet's purchase and sale prices ($ per mmbtu)

	FY08	FY09	FY10E	FY11E	FY12E	FY13E
Dahej contracted volume	3.0	3.1	4.5	6.0	7.7	9.5
Kochi contracted volume	NA	NA	NA	NA	NA	9.5
Spot volume	9.6	10.7	7.1	6.9	7.6	8.6
Average purchase price	**4.3**	**4.8**	**5.2**	**6.2**	**7.7**	**9.4**
Sales price	**5.1**	**5.6**	**5.8**	**6.8**	**8.4**	**10.2**

Source: Company, ICICIdirect.com Research

We expect Petronet LNG to incur capital expenditure of Rs 4,176 crore over FY10-13E for its expansion plans

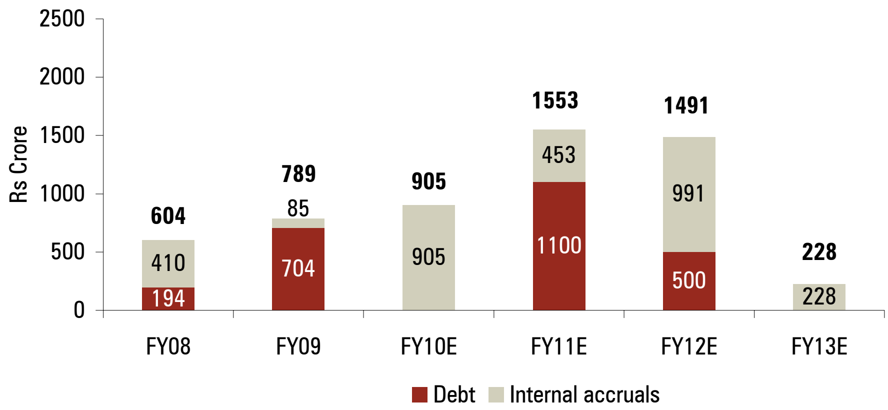
Higher capital expenditure, going forward

Petronet LNG has incurred a capital expenditure of Rs 1,600 crore for the expansion of the Dahej capacity from 5 MMTPA to 10 MMTPA, which has been commissioned in July 2009. The company has taken delivery of its third LNG vessel 'ASEEM' for transportation of an additional 2.5 MMTPA of contracted LNG from Qatar in November 2009.

Petronet LNG is also developing a second LNG jetty at the Dahej terminal for mitigating risk. This would increase its LNG handling capacity to 12.5 MMTPA. The second jetty is being set up at a cost of Rs 800 crore and would be ready for commissioning in Q4FY12. Petronet is constructing a new LNG terminal at Kochi with a capacity of 2.5 MMTPA (expandable to 5 MMTPA) at an investment of Rs 3,400 crore, expected to be commissioned by Q1FY13.

Petronet LNG's capital expenditure of Rs 4,176 crore over FY10-13E for its expansion plans would be funded through a mix of internals accruals and debt. Petronet LNG would fund its capital expenditure worth Rs 1,600 crore through loan funds while the balance Rs 2,577 crore would be funded through internal accruals over FY10-13E.

Exhibit 15: Petronet LNG's capital expenditure



Source: Company, ICICIdirect.com Research

Risks and Concerns

Domestic discoveries of natural gas

The availability of gas from new discoveries in the KG and Mahanadi basin would increase the domestic supply, which may impact the LNG sales volumes of Petronet LNG. Any further discoveries in the east coast and other parts of India would also impact the spot volumes and earnings estimates for the company.

Competitiveness of alternative fuels

LNG competes with alternative fuels like naphtha, fuel oil and coal for the supply of fuel to end-user industries like fertilisers, power, refineries, etc. A reduction in the price of alternative fuels could lead to better competitiveness of these fuels. This may have an adverse impact on the future volumes and profitability of the company.

Regulatory risk

Currently, Petronet LNG's regasification charges for the Dahej terminal are beyond the purview of the regulator. According to our interaction with the management, the Petroleum and Natural Gas Regulatory Board (PNGRB) does not intend to bring regasification charges under purview at least in the next two or three years. However, any regulatory change on regasification charges or returns front would adversely impact Petronet LNG's profitability and valuations. Petronet LNG's fair value would reduce to Rs 77 per share and Rs 82 per share if Dahej gross regasification margins are capped at Rs 30.3 per mmbtu and Rs 31.8 per mmbtu, respectively.

Petronet LNG's fair value would reduce to Rs 77 per share and Rs 82 per share if Dahej's gross regasification margins are capped at Rs 30.3 per mmbtu and Rs 31.8 per mmbtu, respectively

Exhibit 16: Sensitivity of valuation to change in Dahej gross regasification margins

Dahej gross regasification margins (Rs per mmbtu)	30.3	31.8	33.4
Target Price (Rs per share)	77.0	82.0	88.0

Source: ICICIdirect.com Research

Execution risks

Petronet LNG is setting up a 2.5 million tonne (MT) LNG terminal in Kochi at a cost of Rs 3,400 crore. The construction of the LNG terminal is expected to be complete by Q4FY12 and commissioned by Q1FY13. A delay in execution/completion and cost overruns for this project may impact the company's volumes and future profitability.

Force Majeure events

Petronet sources LNG for the Dahej terminal under long-term contract from RasGas and sells regasified LNG to three intermediate offtakers (GAIL, IOC and BPCL). Any force majeure event affecting RasGas facilities, LNG carriers, Petronet's facilities or the gas transmission network may impact the operations of the company.

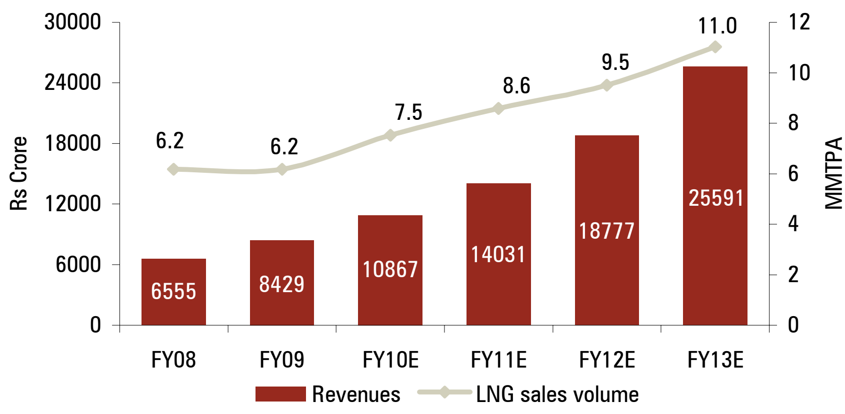
Financials

Robust revenue growth

We expect Petronet LNG to report robust revenue growth on the back of an increase in the LNG sales volume and also due to the increase in LNG sales prices. The LNG gas sales volume is expected to increase at 15.6% CAGR over FY09-13E from 6.2 MMTPA in FY09 to 11 MMTPA in FY13E on account of increase in Dahej capacity to 10 MMTPA in FY10 and commissioning of Kochi terminal in FY13E. The LNG gas sales prices are also expected to increase from $5.6 per mmbtu in FY09 to $10.2 per mmbtu in FY13E as the prices are now linked to Japanese Cocktail Crude (JCC) prices. We believe Petronet LNG's revenues would increase at 32% CAGR over FY09-13E from 8,429 crore in FY09 to Rs 25,591 crore in FY13E.

Petronet LNG's revenues would increase at 32% CAGR over FY09-13E on the back of an increase in LNG sales volume and also due to the increase in LNG sales prices

Exhibit 17: Projected revenue growth



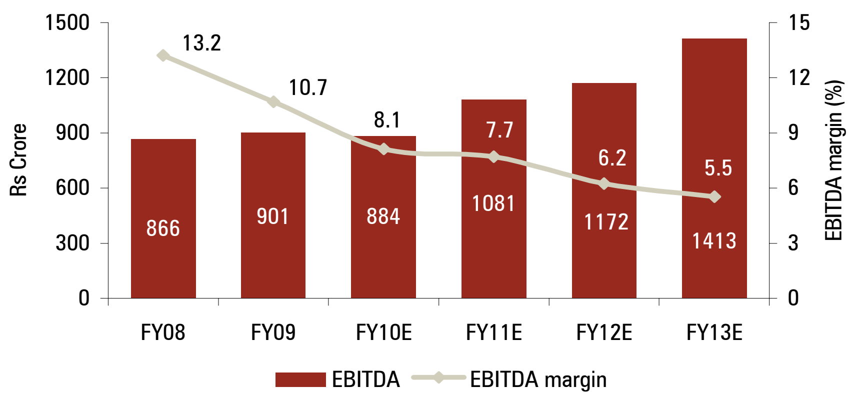
Source: Company, ICICIdirect.com Research

Steady EBITDA growth of 11.9% CAGR over FY09-13E

Petronet LNG's EBITDA is expected to increase from Rs 901 crore in FY09 to Rs 1,413 crore in FY13E at 11.9% CAGR over FY09-13E. Petronet LNG's EBITDA per mmbtu would remain stable at ~24 per mmbtu, going forward, while profitability would not be impacted despite a decline in the EBITDA margin from 10.7% in FY09 to 5.5% in FY13E.

Petronet LNG's EBITDA is expected to increase from Rs 901 crore in FY09 to Rs 1,413 crore in FY13E at 11.9% CAGR over FY09-13E

Exhibit 18: Trend in EBITDA and EBITDA margin



Source: Company, ICICIdirect.com Research

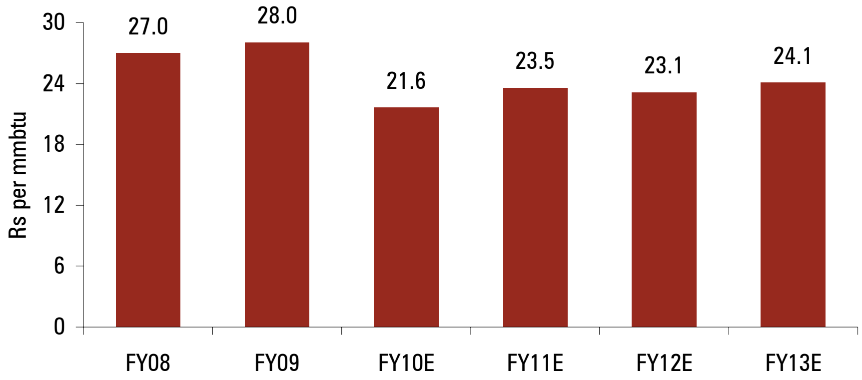
Exhibit 19: Petronet LNG's cost and profitability matrix

	FY08	FY09	FY10E	FY11E	FY12E	FY13E
Total Revenues	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
Consumption of raw materials	84.9	87.5	90.6	91.0	92.6	93.4
Employee Cost	0.3	0.2	0.2	0.2	0.1	0.1
Other Expenditure	1.6	1.6	1.1	1.2	1.1	1.0
Total Expenditure	**86.8**	**89.3**	**91.9**	**92.3**	**93.8**	**94.5**
EBITDA	**13.2**	**10.7**	**8.1**	**7.7**	**6.2**	**5.5**

Source: Company, ICICIdirect.com Research

Petronet LNG's EBITDA per mmbtu would remain stable at ~Rs 24 per mmbtu, going forward, despite a decline in the EBITDA margin

Exhibit 20: Petronet LNG's EBITDA per mmbtu



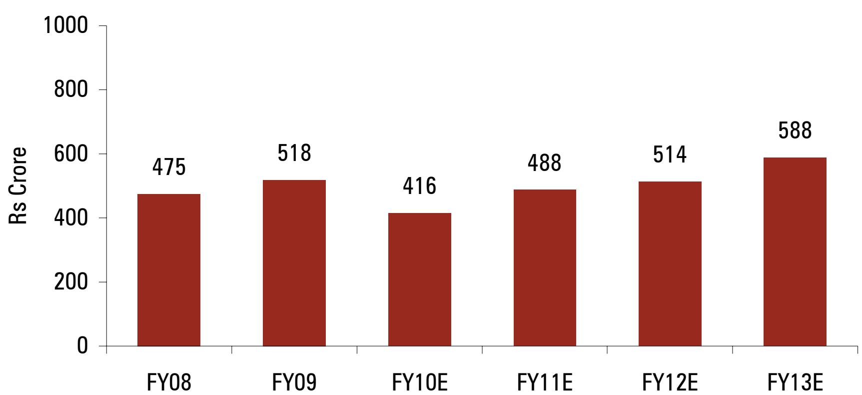
Source: Company, ICICIdirect.com Research

Net profit to increase at a slower pace

We expect Petronet's net profit to increase from Rs 518 crore in FY09 to Rs 588 crore in FY13E at 3.2% CAGR over FY09-13E. The profitability would increase at a slower pace on account of a decline in the net regasification margin and higher interest and depreciation costs. We expect that the interest costs will increase from Rs 101.2 crore in FY09 to Rs 249 crore in FY13E on higher loans while depreciation costs will increase from Rs 102.5 crore in FY09 to Rs 332.9 crore in FY13E on account of expansion of Dahej terminal and commissioning of Kochi terminal. The increase in LNG regasification volume from 6.2 MMTPA in FY09 to 11.3 MMTPA in FY13E would mainly contribute to the profitability growth, going forward.

Profitability will increase from Rs 518 crore in FY09 to Rs 588 crore in FY13E at 3.2% CAGR over FY09-13E

Exhibit 21: Trend in net profitability



Source: Company, ICICIdirect.com Research

Exhibit 22: Petronet LNG's profitability matrix

	FY08	FY09	FY10E	FY11E	FY12E	FY13E
EBITDA	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
Depreciation	11.8	11.4	18.4	17.4	18.4	23.6
EBIT	**88.2**	**88.6**	**81.6**	**82.6**	**81.6**	**76.4**
Interest	11.8	11.2	21.1	20.2	21.1	17.6
Other Income	6.2	8.5	9.4	4.1	4.1	2.9
PBT	**82.6**	**85.9**	**69.8**	**66.5**	**64.6**	**61.8**
Total Tax	27.8	28.4	22.7	21.4	20.7	20.1
PAT	**54.8**	**57.5**	**47.1**	**45.1**	**43.9**	**41.6**

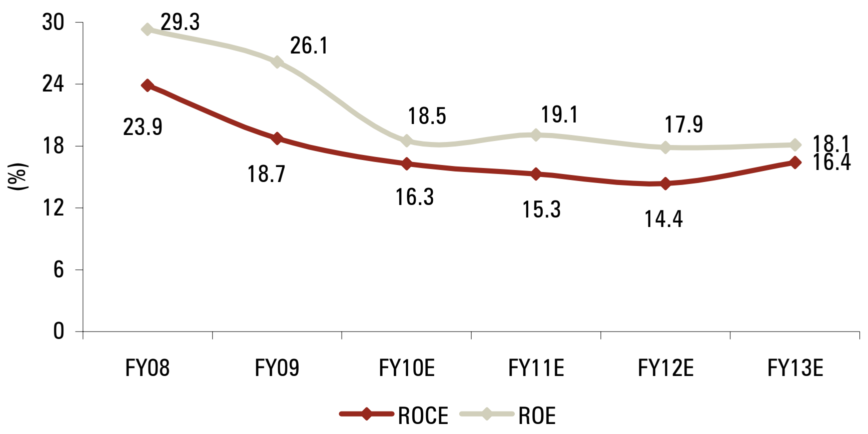
Source: Company, ICICIdirect.com Research

Return ratios to settle at lower levels

We believe the decline in the net profit margin from 6.2% in FY09 to 2.3% in FY13E would lead to lower return on equity (RoE). We expect Petronet LNG's RoE to decline from 26.1% in FY09 to 18.1% in FY13E. The return on capital employed (RoCE) is also expected to decline till FY12E on account of higher capital work in progress for the new Kochi LNG terminal. However, the RoCE is expected to improve to 16.4% in FY13E on commissioning of the Kochi terminal.

Petronet LNG would report RoCE and RoE of 16.4% and 18.1%, respectively, in FY13E

Exhibit 23: Return ratios



Source: Company, ICICIdirect.com Research

Valuations

Petronet LNG's business of receiving and regasification of LNG along with back-to-back long-term purchase and sales agreement with LNG exporters and regasified gas offtakers, respectively, offers a lot of safety for investors. We believe that concerns on regasification margins are overdone. Our interaction with the management suggests that PNGRB would not bring regasification charges under purview at least in the next two or three years. We have also conservatively assumed lower spot sales volumes for Petronet LNG, going forward, taking into account increased availability of gas from new discoveries in the KG and Mahanadi basin.

We expect Petronet's LNG regasification volume to increase from 6.2 MMTPA in FY09 to 11.3 MMTPA in FY13E on account of an increase in the Dahej capacity to 10 MMTPA in FY10 and commissioning of the new 2.5 MMTPA Kochi terminal in FY13E. We believe Petronet LNG's revenues would increase at 32% CAGR over FY09-13E from Rs 8,429 crore in FY09 to Rs 25,591 crore in FY13E. The net profit will increase at 3.2% CAGR over FY09-13E from Rs 518 crore in FY09 to Rs 588 crore in FY13E.

Petronet LNG is trading at a P/BV of 1.9x and P/E multiple of 10.4x FY12E EPS of Rs 6.9. We have valued Petronet LNG based on the DCF methodology to arrive at a price target of Rs 88 (WACC – 10.5%, terminal growth – 2%). We recommend a **STRONG BUY** rating on the stock, with a potential upside of 24%.

Exhibit 24: DCF valuation (Rs Crore)

	FY10	FY11	FY12	FY13	FY14	FY15	Terminal Cash Flows
EBITDA	883.6	1080.9	1172.0	1412.9	1525.9	1587.0	1618.7
Less: Tax paid	200.9	231.1	243.1	284.6	307.4	319.7	326.1
Cash Profit	682.7	849.9	928.9	1128.3	1218.5	1267.3	1292.6
Adjustment for working capital	158.3	-6.0	61.8	-22.9	-24.8	-25.8	-26.3
Operating Cash Flows	841.0	843.9	990.8	1105.3	1193.8	1241.5	1266.3
Less: Capex	905.2	1552.5	1491.2	227.5	50.0	50.0	50.0
Free Cash Flows	-64.2	-708.6	-500.4	877.8	1143.8	1191.5	1216.3
WACC	10.5%						
Present Value of Cash Flows till FY14E	1025.4						
Terminal Growth Rate	2.0%						
Terminal Value	14302.8						
Present Value of Terminal Cash Flows	8680.2						
Total Present Value of the Firm	9705.6						
Less: Net Debt (FY11E)	3081.7						
Total Present Value of Equity	6623.9						
Number of Outstanding shares (In Crore)	75.0						
DCF (Rs per share)	88						

Source: ICICIdirect.com Research

Exhibit 25: Sensitivity analysis of DCF valuation

		WACC				
		9.5%	10.0%	10.5%	11.0%	11.5%
Terminal	1.0%	93	84	75	67	60
	1.5%	102	91	81	73	65
Growth	2.0%	111	99	88	79	71
	2.5%	121	108	96	86	77
Rate	3.0%	134	118	105	94	84

Source: ICICIdirect.com Research

Financial Summary

P&L Statement

(Rs Crore)

	FY08	FY09	FY10E	FY11E	FY12E	FY13E
Revenue	6555.3	8428.7	10867.4	14031.0	18777.4	25591.4
Growth (%)		28.6	28.9	29.1	33.8	36.3
Op. Expenditure	5689.2	7527.4	9983.8	12950.0	17605.4	24178.5
EBITDA	866.2	901.3	883.6	1080.9	1172.0	1412.9
Growth (%)		4.1	-2.0	22.3	8.4	20.6
Depreciation	102.2	102.5	162.8	188.0	215.4	332.9
EBIT	764.0	798.7	720.8	892.9	956.6	1080.0
Interest	102.4	101.2	186.8	218.5	247.2	249.0
Other Income	53.6	76.5	82.7	44.4	47.7	41.6
PBT	715.2	774.0	616.7	718.7	757.0	872.6
Growth (%)		8.2	-20.3	16.6	5.3	15.3
Tax	240.5	255.6	200.9	231.1	243.1	284.6
Reported PAT	474.7	518.4	415.7	487.7	514.0	588.0
Growth (%)		9.2	-19.8	17.3	5.4	14.4
Adjustments	53.2	76.2	82.4	44.1	47.4	41.3
Adj. Net Profit	421.4	442.3	333.3	443.6	466.6	546.7
Growth (%)		4.9	-24.6	33.1	5.2	17.2

Key ratios (%)

	FY08	FY09	FY10E	FY11E	FY12E	FY13E
Raw material costs	84.9	87.5	90.6	91.0	92.6	93.4
Employees Cost	0.3	0.2	0.2	0.2	0.1	0.1
Other Expenditure	1.6	1.6	1.1	1.2	1.1	1.0
Average cost of debt	6.9	5.2	8.0	8.0	7.0	7.0
Effective Tax rate	33.6	33.0	32.6	32.2	32.1	32.6
Profitability ratios (%)						
EBITDA Margin	13.2	10.7	8.1	7.7	6.2	5.5
PAT Margin	7.2	6.2	3.8	3.5	2.7	2.3
Adj. PAT Margin	6.4	5.2	3.1	3.2	2.5	2.1
Per share data (Rs)						
Revenue per share	87.4	112.4	144.9	187.1	250.4	341.2
EV per share	87.3	92.7	96.2	109.7	119.0	111.6
Book Value	21.6	26.4	29.9	34.1	38.3	43.2
Cash per share	4.8	8.8	3.9	5.1	2.5	3.8
EPS	6.3	6.9	5.5	6.5	6.9	7.8
Cash EPS	7.7	8.3	7.7	9.0	9.7	12.3
DPS	1.5	1.8	1.8	2.0	2.3	2.5

Costs as % to revenue except tax rate and average cost of debt

Balance Sheet

(Rs crore)

	FY08	FY09	FY10E	FY11E	FY12E	FY13E
Equity Capital	750.0	750.0	750.0	750.0	750.0	750.0
Preference Capital	0.0	0.0	0.0	0.0	0.0	0.0
Reserves & Surplus	868.6	1233.4	1495.6	1807.8	2124.3	2492.9
Shareholder's Fund	1618.6	1983.4	2245.6	2557.8	2874.3	3242.9
Loan Funds	1577.6	2281.7	2181.7	3281.7	3781.7	3331.7
Deferred Tax Liability	269.2	272.2	372.0	372.0	472.0	572.0
Minority Interest	0.0	0.0	0.0	0.0	0.0	0.0
Source of Funds	3465.4	4537.3	4799.3	6211.5	7128.0	7146.6
Gross Block	1971.8	1974.8	3577.3	3579.8	4598.3	8025.8
Less: Acc. Depreciation	403.8	506.2	696.7	884.7	1100.2	1433.0
Net Block	1568.0	1468.6	2880.6	2695.1	3498.2	6592.8
Capital WIP	1061.4	1847.0	1177.3	2727.3	3200.0	0.0
Investments	547.3	304.3	350.0	300.0	200.0	200.0
Inventories	91.0	385.6	357.3	461.3	514.4	701.1
Debtors	333.0	671.2	565.7	730.4	926.0	1262.0
Cash	358.6	657.8	290.0	381.7	184.3	285.4
Loan & Advance, Other CA	365.1	95.2	100.0	80.0	60.0	40.0
Total Current assets	1147.6	1809.7	1313.0	1653.4	1684.8	2288.6
Current Liabilities	428.8	736.5	744.3	961.0	1234.7	1682.7
Provisions	430.1	155.7	177.2	203.3	220.3	252.0
Total CL and Provisions	858.8	892.2	921.6	1164.3	1454.9	1934.7
Net Working Capital	288.7	917.5	391.4	489.1	229.8	353.8
Miscellaneous expense	0.0	0.0	0.0	0.0	0.0	0.0
Application of Funds	3465.4	4537.3	4799.3	6211.5	7128.0	7146.6

Key ratios (%)

Return ratios	FY08	FY09	FY10E	FY11E	FY12E	FY13E
RoNW	29.3	26.1	18.5	19.1	17.9	18.1
ROCE	23.9	18.7	16.3	15.3	14.4	16.4
Financial health ratio						
Operating CF (Rs Cr)	697.2	140.9	683.1	494.2	693.8	778.6
FCF (Rs Cr)	93.0	-647.9	-222.0	-1058.3	-797.4	551.1
Cap. Emp. (Rs Cr)	3465.4	4537.3	4799.3	6211.5	7128.0	7146.6
Debt to equity (x)	1.0	1.2	1.0	1.3	1.3	1.0
Debt to cap. emp. (x)	0.5	0.5	0.5	0.5	0.5	0.5
Interest Coverage (x)	7.5	7.9	3.9	4.1	3.9	4.3
Debt to EBITDA (x)	1.8	2.5	2.5	3.0	3.2	2.4
DuPont ratio analysis						
PAT/PBT	0.7	0.7	0.7	0.7	0.7	0.7
PBT/EBIT	0.9	1.0	0.9	0.8	0.8	0.8
EBIT/Sales	0.1	0.1	0.1	0.1	0.1	0.0
Sales/ Total Asset	1.9	1.9	2.3	2.3	2.6	3.6
Total Asset/ Net Worth	2.1	2.3	2.1	2.4	2.5	2.2

Cash Flow statement

(Rs crore)

	FY08	FY09	FY10E	FY11E	FY12E	FY13E
Profit after Tax	474.7	518.4	415.7	487.7	514.0	588.0
Less: Dividend Paid	131.6	153.6	153.6	175.5	197.4	219.4
Add: Depreciation	102.2	102.5	162.8	188.0	215.4	332.9
Add: Others	22.0	3.0	99.8	0.0	100.0	100.0
Cash Profit	467.2	470.4	524.8	500.2	631.9	801.5
Increase/(Decrease) in CL	271.2	33.4	29.4	242.7	290.6	479.8
(Increase)/Decrease in CA	-41.2	-362.9	128.9	-248.7	-228.8	-502.7
CF from Operating Activities	697.2	140.9	683.1	494.2	693.8	778.6
Purchase of Assets	604.3	788.8	905.2	1552.5	1491.2	227.5
(Inc)/Dec in Investments	-269.3	243.1	-45.7	50.0	100.0	0.0
CF from Investing Activities	-873.6	-545.7	-950.9	-1502.5	-1391.2	-227.5
Inc/(Dec) in Loan Funds	194.4	704.1	-100.0	1100.0	500.0	-450.0
Inc/(Dec) in Sh. Cap. & Res.	0.0	0.0	0.0	0.0	0.0	0.0
CF from financing Activities	194.4	704.1	-100.0	1100.0	500.0	-450.0
Change in cash Eq.	18.1	299.2	-367.8	91.7	-197.4	101.1
Op. Cash and cash Eq.	340.5	358.6	657.8	290.0	381.7	184.3
Cl. Cash and cash Eq.	358.6	657.8	290.0	381.7	184.3	285.4

Working Capital Ratios

	FY08	FY09	FY10E	FY11E	FY12E	FY13E
Fixed Asset Turnover	2.5	2.5	2.7	2.6	2.8	3.9
Inventory Turnover (Days)	5.1	16.7	12.0	12.0	10.0	10.0
Debtor (Days)	18.5	29.1	19.0	19.0	18.0	18.0
Current Liabilities (Days)	23.9	31.9	25.0	25.0	24.0	24.0
Current Ratio	1.3	2.0	1.4	1.4	1.2	1.2
Quick ratio	1.2	1.6	1.0	1.0	0.8	0.8

Valuation Ratios

	FY08	FY09	FY10E	FY11E	FY12E	FY13E
Market Capitalisation	5325.0	5325.0	5325.0	5325.0	5325.0	5325.0
Enterprise Value (EV)	6544.1	6948.9	7216.7	8225.0	8922.4	8371.3
PE	11.2	10.3	12.8	10.9	10.4	9.1
Price to Book Value	3.3	2.7	2.4	2.1	1.9	1.6
Price to Cash EPS	9.2	8.6	9.2	7.9	7.3	5.8
EV/EBITDA	7.6	7.7	8.2	7.6	7.6	5.9
Market Cap/Sales	0.8	0.6	0.5	0.4	0.3	0.2
EV/Sales	1.0	0.8	0.7	0.6	0.5	0.3

Annexure

LNG regasification process

Liquefied natural gas (LNG) is natural gas (predominantly methane, CH_4) that has been converted temporarily to liquid form for ease of storage or transport. Liquefied natural gas takes up about 1/600th the volume of natural gas in the gaseous state. The reduction in volume makes it much more cost efficient to transport over long distances where pipelines do not exist. Where moving natural gas by pipelines is not possible or economical, it can be transported by specially designed cryogenic sea vessels (LNG carriers) or cryogenic road tankers.

Exhibit 26: LNG value chain

Source: Sempralng.com, ICICIdirect.com Research

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Buy: Between 10% and 20%;
Add: Up to 10%;
Reduce: Up to -10%
Sell: -10% or more;

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