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APM gas price hike to USD 4.2/mmbtu

The much awaited gas price has given a positive surprise for the upstream companies

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The government of India has approved a hike in the administered pricing mechanism (APM) gas price sold by Oil and Natural Gas Corp. Ltd (ONGC) and Oil India Ltd (OIL) from nomination blocks from Rs.3.20 per standard cu. m (scm) to Rs 6.82 per scm. Prices are now at \$4.2 per million British thermal unit (mmbtu) (pre-royalty adjusted) from \$1.9 per mmbtu earlier. After the hike, APM prices are now in line with empowered group of ministers-determined gas prices for the Krishna-Godavari (KG) D6. APM gas prices were last revised in 2005.

The move follows the finance ministry's suggestion of bringing about pricing parity between APM and KG gas in one swift move, rather than a phased increase in the APM gas prices as was proposed by the petroleum ministry. The prices will be effective until March 2014.

In a related development, the cabinet has also approved the marketing margins of \$0.112 per mmbtu (Rs200 per scm) for GAIL India Ltd on APM gas marketing volumes. Previous to this, GAIL did not receive any marketing margin on sales of APM gas.

IMPACT

Fertilizer companies cost will increase which in turn will increase the fertilizer subsidy burden.

- The gas price hike to USD 4.2/ mmbtu from current rate USD 1.79/mmbtu is a positive surprise as the expectations were an increase over few years to the benchmark level of RIL KG D 6 gas rate of USD 4.2 mmbtu. This price is valid till March, 2014 which is when the KG D-6 gas prices shall be reviewed as well.
- End users of APM gas are fertilizers, city gas distributors and power companies. There will be an increase in input cost for power and city gas distribution companies which will be passed to the customers resulting in higher power tariffs and CNG and PNG prices. Even fertilizer companies cost will increase which in turn will increase the fertilizer subsidy burden. But as the royalty on gas is increased to 10%, the GOI will be able to compensate the increase in fertilizer subsidy.
- The move is a step forward towards a uniform gas pricing policy in the country which is likely to improve the competitiveness of imported liquefied natural gas. This move could also encourage state-owned gas producers to develop marginal gas fields, which could increase domestic gas production, and benefit gas transportation companies such as GAIL and Gujarat State Petronet Ltd, apart from the producers of the gas.

Contd...

Companies to benefit

- With the increase in APM gas prices, ONGC and Oil India are the major beneficiaries. Total 55 mmscmd of APM gas is supplied by both the companies. The gas price increase will lead to increase in the earnings of both the companies. As GAIL is allowed to charge marketing margins the revenues will increase to certain extent.

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What next to follow?

After the APM gas price hike the next move by government is to come out with some positive decision on partial implementation on the Kirit Parikh Committee recommendation. The Empowered group of Ministers are likely to meet on 7th June, 2010 for the fuel price hike.

The proposal of Kirit Parekh committee are stated below –

- **Petrol:** De regulation of petrol prices.
- **Diesel:** Complete de regulation of diesel prices.
- **Kerosene :** Hike of Rs. 6/ litre
- **LPG:** Rs. 100/ cylinder hike.

OMCs loss

- **Petrol :** Rs. 5.1/ litre
- **Diesel :** Rs. 5.3/ litre
- **Kerosene :** Rs. 18.8/ litre
- **LPG :** Rs. 254.4 / cylinder

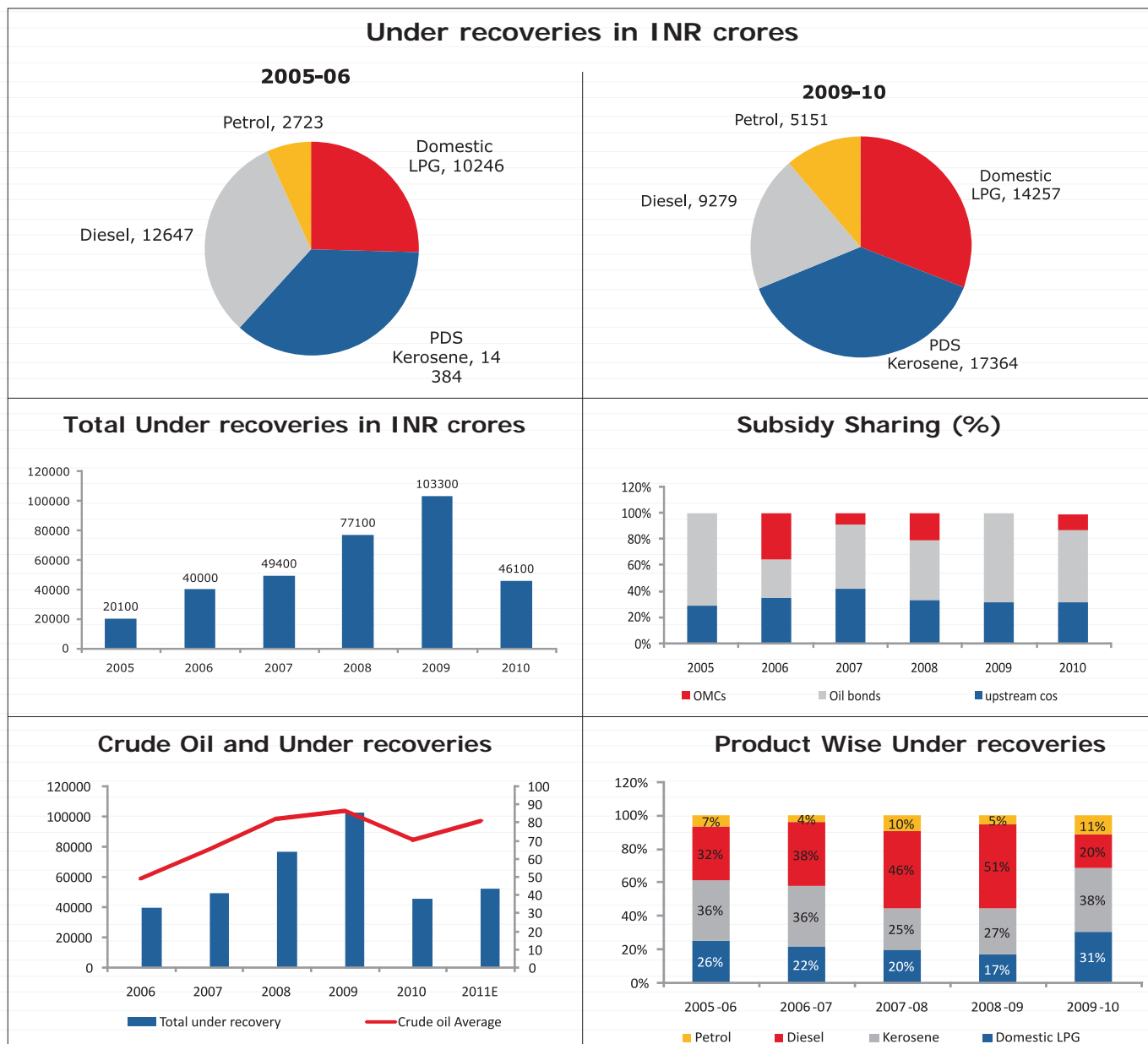
Decision Likely

EGOM may consider increase in petrol and diesel prices and may not touch LPG and kerosene. The government feels that increase in petrol and diesel prices are manageable by the consumers. LPG and kerosene are likely to be untouched as they are politically sensitive issues for the government. If both petrol and diesel are de regulated then there will be a free pricing mechanism till the crude prices increase to certain level.

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Particulars	Petrol Rs/ltr	Diesel Rs/ltr	Kerosene Rs/ltr	LPG per cylinder
Current Price	51.9	39.1	9	310
Kirit Parikh committee recommendation	5	5	6	100
Total Price	56.9	44.1	15	410
Scenario 1				
Diesel and Petrol price hike	57	44	9	310
Scenario 2				
Partial Hike in petrol and diesel prices	3	2	0	0
	54.9	41.1	9	310

(Petrol, diesel, kerosene and LPG prices are as on 1st April, 2010)



Sources:- Company, Anagram research

Impact Analysis

Particulars	80	85	90
Crude Oil Price USD/bbl			
Under recoveries in INR crores	52164	55424	58685
Scenario 1			
Kirit Parikh Recommendation			
Complete de regulation of petrol and Diesel prices and hike in kerosene and LPG			
Impact on Subsidies in INR crores	32474	35735	38995
Scenario 2			
Complete de regulation of petrol and diesel prices	50316	53576	56837
Scenario 3			
Partial deregulation of petrol and diesel prices	51329	54589	57850

(Petrol, diesel, kerosene and LPG prices are as on 1st April, 2010)

Impact on Companies

Any price hike is likely to reduce the subsidy burden on OMCs and upstream companies. We expect this move to benefit ONGC and Oil India Ltd in a big way. De regulation of petrol and diesel will reduce the burden of subsidies on OMCs.

For Further Details

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RATING INTERPRETATION :

BUY Expected to appreciate more than 20% over a 12-month period

Accumulate Expected to appreciate up to 20% over a 12-month period

Neutral Expected to remain in a narrow range

SELL Expected to depreciate more than 10% over a 12-month period

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