

November 15, 2011

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	Accumulate
Rating	
Price	Rs97
Target Price	Rs115
Implied Upside	18.6%
Sensex	17,119

(Prices as on November 14, 2011)

Trading data

Market Cap. (Rs bn)	54.4
Shares o/s (m)	562.6
3M Avg. Daily value (Rs m)	159.7

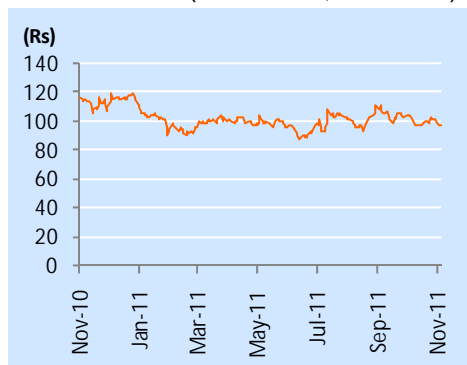
Major shareholders

Promoters	37.73%
Foreign	7.47%
Domestic Inst.	34.89%
Public & Other	19.91%

Stock Performance

(%)	1M	6M	12M
Absolute	(5.6)	(7.2)	(17.0)
Relative	(5.8)	0.5	(1.9)

Price Performance (RIC: GSPT.BO, BB: GUJS IN)



Source: Bloomberg

Gujarat State Petronet (GSPL) reported in-line operational performance for Q2FY12, with sales at Rs2.81bn against our expectation of Rs2.79bn. Transmission volumes continued to be sluggish during the quarter at 35.2mmscmd (35.3mmscmd). EBITDA, during Q2FY12 at Rs2.59bn (10.6% YoY, -0.1% QoQ), was higher than estimate of Rs2.56bn. Depreciation was 7.3% lower than estimate, while other income at Rs142.5m as against estimate of Rs70m. On account of higher-than-anticipated other income and lower-than-estimated depreciation, PBT was 2.9% higher than our estimates.

- Transmission volumes flat, Realisation increases:** In Q2FY12, GSPL recorded 10.4% YoY increase in revenues at Rs2.81bn (Rs2.55bn), which was in line with our expectation of Rs2.79bn. Transmission volumes, which were at 35.2mmscmd (35.3mmscmd), came in line with our estimate. Average transmission realization increased by 8.0% YoY to Rs833/'000scm (Rs771/'000scm), same was also slightly higher than our expectation of Rs830/'000scm.
- Depreciation declines on policy change:** GSPL has changed its pipeline depreciation rate from 8.33% SLM (based on a useful life of 12 years) to 3.71% SLM (based on a useful life of 31 years). Due to change in the depreciation policy, depreciation during the quarter was lower at Rs440m (-42.1% YoY).
- Outlook and Valuation:** GSPL's fortunes are highly linked to availability of the gas. On account of subdued domestic gas output, GSPL has not been able to deliver the volume growth over the last 7-8 quarters. We believe the domestic natural gas production outlook is unlikely to see a material uptick in the near term, resulting in lack of significant volumes growth for GSPL. We do not ascribe any value to new pipelines bagged by GSPL as there are uncertainties with regards to possible gas source over the same. On the positive we believe, impending clarity over the transmission tariffs is likely to emerge over the next six months, which is likely to provide upsides in the stock price. We recommend an '**Accumulate**' on the stock, with a target price of Rs115/share.

Key financials (Y/e March)	2010	2011	2012E	2013E
Revenues (Rs m)	9,920	10,374	11,190	11,232
Growth (%)	103.5	4.6	7.9	0.4
EBITDA (Rs m)	9,297	9,603	10,440	10,479
PAT (Rs m)	4,083	5,044	5,261	5,083
EPS (Rs)	7.3	9.0	9.4	9.0
Growth (%)	228.5	23.5	4.3	(3.4)
Net DPS (Rs)	1.0	1.5	1.6	2.1

Source: Company Data; PL Research

Profitability & Valuation	2010	2011	2012E	2013E
EBITDA margin (%)	93.7	92.6	93.3	93.3
RoE (%)	29.4	28.3	23.7	19.3
RoCE (%)	18.2	18.0	16.2	14.4
EV / sales (x)	6.6	6.4	6.0	5.9
EV / EBITDA (x)	7.0	7.0	6.4	6.3
PE (x)	13.3	10.8	10.3	10.7
P / BV (x)	3.5	2.7	2.2	1.9
Net dividend yield (%)	1.0	1.6	1.7	2.1

Source: Company Data; PL Research

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**Exhibit 1: Q2FY12 Result Overview (Rs m)**

Y/e March	Q2FY12	Q2FY11	YoY gr. (%)	Q1FY12	H1FY12	H1FY11	YoY gr. (%)
Net Sales	2,808	2,530	11.0	2,843	5,651	5,048	12.0
Expenditure							
O & M expenses	109	96	12.7	90	224	178	25.7
<i>% of net sales</i>	<i>3.9</i>	<i>3.8</i>		<i>3.2</i>	<i>4.0</i>	<i>3.5</i>	
Personnel cost	56	42	34.0	45	108	68	60.2
<i>% of net sales</i>	<i>2.0</i>	<i>1.7</i>		<i>1.6</i>	<i>1.9</i>	<i>1.3</i>	
Other expenses	59	70	(15.9)	120	116	99	16.4
<i>% of net sales</i>	<i>2.1</i>	<i>2.8</i>		<i>4.2</i>	<i>2.0</i>	<i>2.0</i>	
EBITDA	2,585	2,321	11.3	2,588	5,203	4,703	10.6
<i>Margin (%)</i>	<i>92.0</i>	<i>91.8</i>		<i>91.0</i>	<i>92.1</i>	<i>93.2</i>	
Depreciation	440	760	(42.1)	453	893	1,447	(38.3)
EBIT	2,144	1,562	37.3	2,136	4,311	3,256	32.4
Interest	337	242	39.4	324	661	466	41.8
Other Income	143	83	71.5	112	254	140	81.4
Cont. to GSEDS	-	-		-	-	-	
PBT	1,950	1,403	39.0	1,923	3,904	2,930	33.2
Total taxes	656	488	34.5	581	1,237	964	28.4
<i>ETR (%)</i>	<i>33.7</i>	<i>34.8</i>		<i>30.2</i>	<i>31.7</i>	<i>32.9</i>	
Rep. PAT	1,293	915	41.3	1,343	2,667	1,966	35.6

Source: Company Data, PL Research

Exhibit 2: Operating Metrics

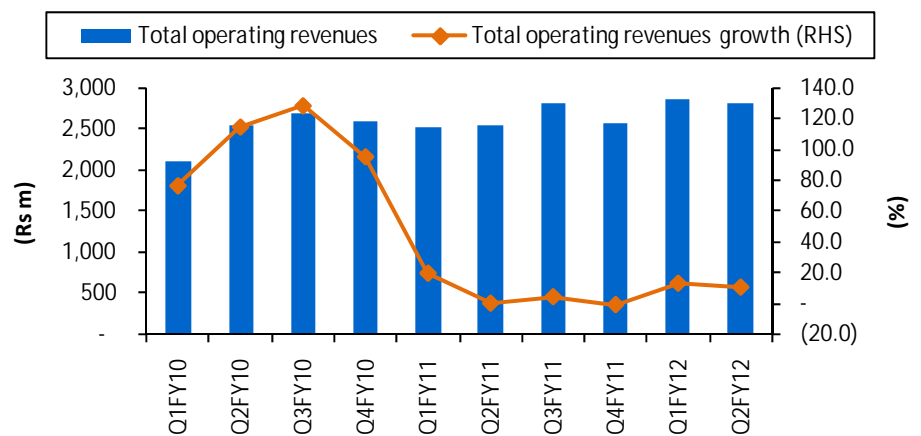
Y/e March	Q2FY12	Q2FY11	YoY gr. (%)	Q1FY12	H1FY12	H1FY11	YoY gr. (%)
Gas transmission volumes (mmscmd)	35.2	35.3	(0.3)	36.8	36.0	35.8	0.5
Avg. realisations (Rs/ '000scm)	833	771	8.0	813	823	767	7.3

Source: Company Data, PL Research

Key Result Highlights

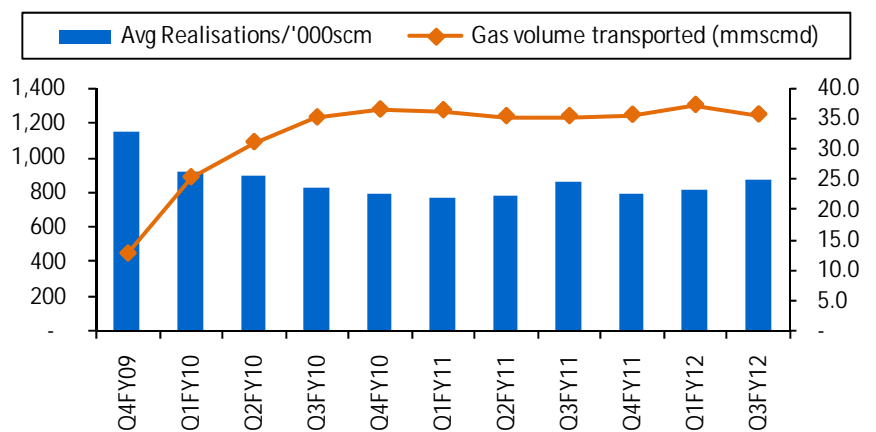
Transmission volumes flat, Realisation increases: In Q2FY12, GSPL recorded 10.4% YoY increase in revenues at Rs2.81bn (Rs2.55m), which was in line with our expectation of Rs2.79m. Transmission volumes, which were at 35.2mmscmd (35.3mmscmd), came in line with our estimates. Average transmission realization increased by 8.0% YoY to Rs833/'000scm (Rs7771/'000scm), same was also slightly higher than our expectation of Rs830/'000scm. We believe take or pay contracts, coupled with long-distance transportation of gas, must have led to higher tariffs during the quarter. Sales of electricity generated via Wind Energy during the quarter stood at Rs10.9m against Rs2.39m in the corresponding quarter previous year.

Exhibit 3: Operating revenue trend



Source: Company Data, PL Research

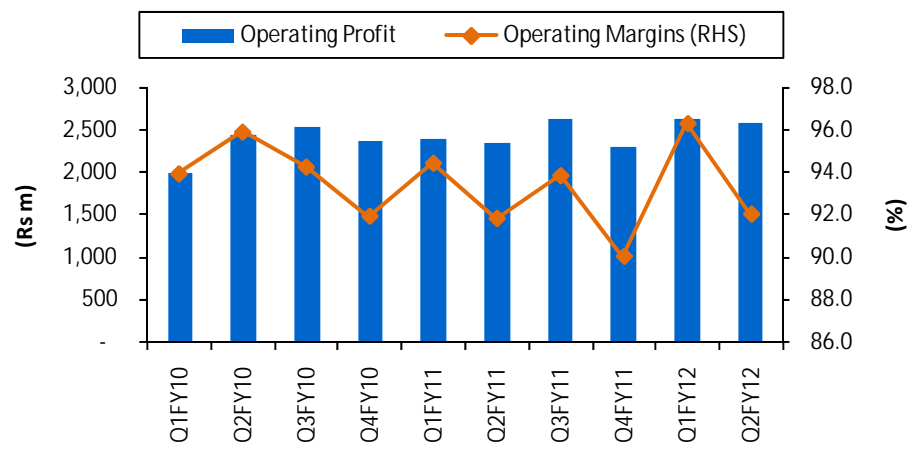
Exhibit 4: Transmission Performance



Source: Company Data, PL Research

Operating profits in with estimates: O&M expenses increased (due to higher compression cost) 12.7% YoY to Rs109m (Rs96m) and was in line with our expectation. Administrative and other charges declined by 15.9% YoY to Rs59m (Rs70m). Staff cost during the quarter was up 34% YoY to Rs59m. EBITDA registered 10.6% YoY growth to Rs2,585m (Rs2,336m) during Q2FY12. EBITDA sequentially was flat as lower revenues from sales of wind energy were compensated by higher realisations from natural gas transmission.

Exhibit 5: Operating performance

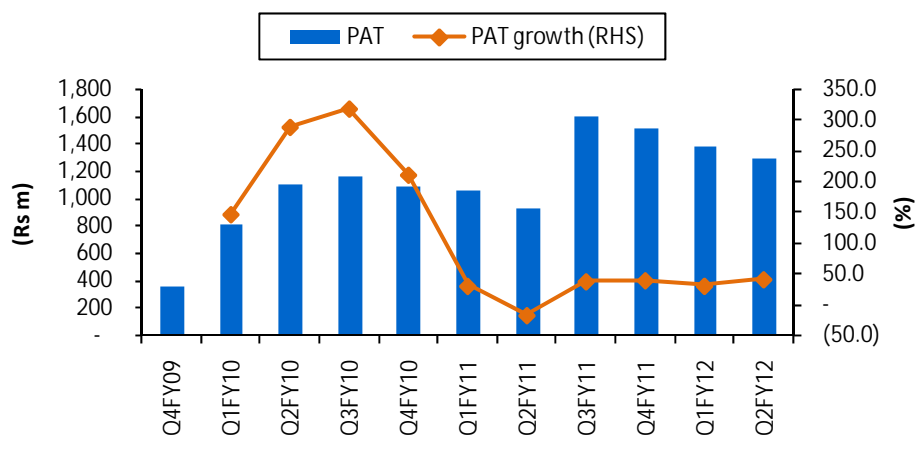


Source: Company Data, PL Research

Depreciation declines on policy change: GSPL has changed its pipeline depreciation rate from 8.33% SLM (based on a useful life of 12 years) to 3.71% SLM. On account of change in the depreciation policy, depreciation during the quarter was lower at Rs440m, registering a decline of 42.1% YoY. Depreciation during the quarter was 7.3% lower than estimate, while other income at Rs142.5m as against our estimate of Rs70m. On account of higher-than-anticipated other income and lower-than-estimated depreciation, PBT was 2.9% higher than our estimates.

PAT increases by 41.3% YoY: GSPL reported a bottom-line growth of 41.3% YoY on account of change in the depreciation policy, coupled with higher revenues from wind power and slightly higher transmission tariffs. However, due to change in depreciation policy, numbers at the bottom-line level are not comparable.

Exhibit 6: PAT growth trend



Source: Company Data, PL Research



Outlook and Valuation

GSPL's fortunes are highly linked to availability of the gas. On account of subdued domestic gas output, GSPL has not been able to deliver the volumes growth over the last 7-8 quarters. The same has resulted into subdued stock performance. We believe the domestic natural gas production outlook is unlikely to see a material change in the near term, resulting in lack of significant volumes growth for GSPL. We do not ascribe any value to new pipelines bagged by GSPL as there are uncertainties with regards to possible gas source over the same.

On the positive we believe, impending clarity over the transmission tariffs is likely to emerge over the next 6 months (PNGRB likely to notify GSPL's tariff) and is likely to create upsides in the stock price. There is limited downside to GSPL's tariffs for Gujarat network and management has also indicated the same over the various platforms in the past. Thus, the tariff notification is likely to provide some upsides to the stock price. We recommend an **'Accumulate'** on the stock, with a target price of Rs115/share.



Income Statement (Rs m)

Y/e March	2010	2011	2012E	2013E
Net Revenue	9,920	10,374	11,190	11,232
Raw Material Expenses	—	—	—	—
Gross Profit	9,920	10,374	11,190	11,232
Employee Cost	99	153	145	146
Other Expenses	523	619	604	607
EBITDA	9,297	9,603	10,440	10,479
Depr. & Amortization	2,365	1,299	1,632	1,854
Net Interest	813	673	836	924
Other Income	247	287	280	337
Profit before Tax	6,241	7,630	7,971	7,701
Total Tax	2,131	2,586	2,710	2,618
Profit after Tax	4,110	5,044	5,261	5,083
Ex-Od items / Min. Int.	(27)	—	—	—
Adj. PAT	4,083	5,044	5,261	5,083
Avg. Shares O/S (m)	562.4	562.6	562.6	562.6
EPS (Rs.)	7.3	9.0	9.4	9.0

Cash Flow Abstract (Rs m)

Y/e March	2010	2011	2012E	2013E
C/F from Operations	9,440	6,706	8,796	9,008
C/F from Investing	(8,169)	(6,720)	(6,916)	(5,413)
C/F from Financing	(504)	640	(2,100)	(2,328)
Inc. / Dec. in Cash	767	626	(220)	1,267
Opening Cash	975	1,742	2,390	2,171
Closing Cash	1,742	2,367	2,171	3,437
FCFF	(759)	(3,952)	(2,727)	(68)
FCFE	327	(1,713)	(2,727)	(68)

Key Financial Metrics

Y/e March	2010	2011	2012E	2013E
Growth				
Revenue (%)	103.5	4.6	7.9	0.4
EBITDA (%)	118.8	3.3	8.7	0.4
PAT (%)	228.7	23.5	4.3	(3.4)
EPS (%)	228.5	23.5	4.3	(3.4)
Profitability				
EBITDA Margin (%)	93.7	92.6	93.3	93.3
PAT Margin (%)	41.2	48.6	47.0	45.3
RoCE (%)	18.2	18.0	16.2	14.4
RoE (%)	29.4	28.3	23.7	19.3
Balance Sheet				
Net Debt : Equity	0.7	0.6	0.5	0.4
Net Wrkng Cap. (days)	—	—	—	—
Valuation				
PER (x)	13.3	10.8	10.3	10.7
P / B (x)	3.5	2.7	2.2	1.9
EV / EBITDA (x)	7.0	7.0	6.4	6.3
EV / Sales (x)	6.6	6.4	6.0	5.9
Earnings Quality				
Eff. Tax Rate	34.1	33.9	34.0	34.0
Other Inc / PBT	4.0	3.8	3.5	4.4
Eff. Depr. Rate (%)	7.1	3.1	3.2	3.2
FCFE / PAT	8.0	(34.0)	(51.8)	(1.3)

Source: Company Data, PL Research.

Balance Sheet Abstract (Rs m)

Y/e March	2010	2011	2012E	2013E
Shareholder's Funds	15,635	20,040	24,320	28,336
Total Debt	12,595	14,835	14,835	14,835
Other Liabilities	1,405	2,639	3,832	4,984
Total Liabilities	29,636	37,515	42,987	48,155
Net Fixed Assets	29,755	35,363	40,926	44,822
Goodwill	—	—	—	—
Investments	666	766	766	766
Net Current Assets	(785)	1,410	1,319	2,591
<i>Cash & Equivalents</i>	<i>1,742</i>	<i>2,390</i>	<i>2,171</i>	<i>3,437</i>
<i>Other Current Assets</i>	<i>5,808</i>	<i>6,607</i>	<i>6,735</i>	<i>6,740</i>
<i>Current Liabilities</i>	<i>8,334</i>	<i>7,586</i>	<i>7,586</i>	<i>7,586</i>
Other Assets	—	—	—	—
Total Assets	29,636	37,539	43,011	48,179

Quarterly Financials (Rs m)

Y/e March	Q1FY12	Q2FY11	Q3FY11	Q2FY12
Net Revenue	2,843	2,506	2,795	2,808
EBITDA	2,619	2,297	2,623	2,584
% of revenue	92.1	91.7	93.8	92.0
Depr. & Amortization	453	760	25	440
Net Interest	324	242	259	337
Other Income	112	83	50	143
Profit before Tax	1,954	1,379	2,389	1,949
Total Tax	581	488	798	656
Profit after Tax	1,374	891	1,591	1,293
Adj. PAT	1,374	891	1,591	1,293

Key Operating Metrics

Y/e March	2010	2011	2012E	2013E
Transmission volumes (mmscmd)	32	36	37	40
Avg. Transmission Tariff (Rs/000scm)	850	795	818	761
Operating expenditure (Rs/000scm)	850	795	818	761
EBDITA (Rs/000scm)	796	736	763	710
PAT (Rs/000scm)	354	386	385	344

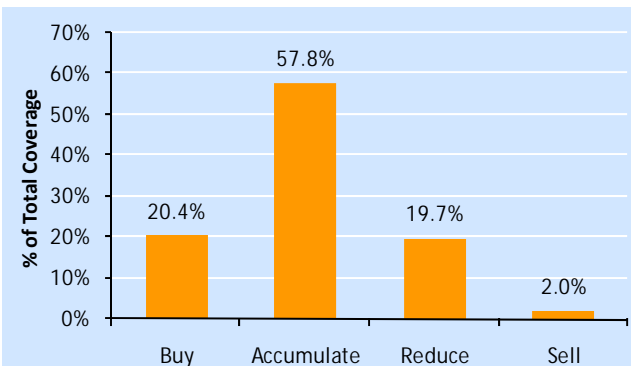
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Rating Distribution of Research Coverage



PL's Recommendation Nomenclature

BUY	: Over 15% Outperformance to Sensex over 12-months	Accumulate	: Outperformance to Sensex over 12-months
Reduce	: Underperformance to Sensex over 12-months	Sell	: Over 15% underperformance to Sensex over 12-months
Trading Buy	: Over 10% absolute upside in 1-month	Trading Sell	: Over 10% absolute decline in 1-month
Not Rated (NR)	: No specific call on the stock	Under Review (UR)	: Rating likely to change shortly

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