

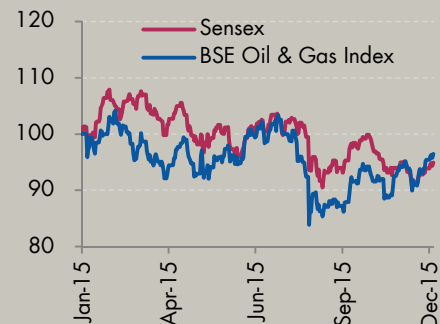
Oil & Gas: RasGas resolution priced in

India and RasGas (Qatar) have renegotiated LNG supply deal. Key highlights: (a) imported LNG prices to fall to USD 6-7/mnbtu vs. USD 12-13/mnbtu currently (FoB), (b) RasGas has agreed to waive off take-or-pay liabilities of USD 1.5 bn on PLNG/GAIL/IOC/BPCL, and (c) PLNG to import additional 1 mntpa of LNG (7.5 mntpa currently).

Positives priced in: Lower gas cost will make GAIL's petchem expansion profitable (33% YoY growth in FY17 EPS) and remove concerns of huge take-or-pay liability on PLNG. **Upgrade GAIL, PLNG to HOLD.** However, post recent run-up (up 8-10% in one month), CMP implies P/E of 13x for GAIL's core business and Kochi terminal utilization at 40% for PLNG in FY20, which we find too optimistic.

Prefer GSPL in the gas space: given short-term benefits (higher tariffs, transportation volumes) and long-term benefits from increasing gas supplies (Dahej LNG terminal expansion, Mundra/Pipapav terminals).

Relative performance



Source: Axis Capital

GAIL: Lower raw material costs for petchem, higher trading/transmission volumes

Lower gas cost will make GAIL's Pata expansion profitable vs. expected losses in FY17. Also, gas may regain its competitiveness vs. liquid fuels (fuel oil, naphtha etc), which may prop industrial demand and benefit GAIL's trading/transmission volumes. We increase our FY16-17 EPS estimates by 7-9% and TP to Rs 380 (Rs 310 earlier), and **upgrade GAIL to HOLD.** However, CMP at Rs 375 implies FY17 P/E of 13x, which is expensive given uncertain trading income and weak RoCE (6-8%). Upside to RoCE will be limited due to regulated earnings on its core pipeline business.

PLNG: No take-or-pay liability

We were negative on PLNG due to (a) possible take-or-pay liability of USD 1.5 bn due to default on RasGas contract and (b) 50% cut in regas tariffs on LNG supplied to stranded power plants. Waive-off of take-or-pay liability has reduced a huge risk on PLNG's balance sheet. We increase our TP to Rs 250 (Rs 200 earlier) and **upgrade PLNG to HOLD.** However, cut in regas tariff is still a material concern. PLNG trades at 12x FY20 EPS of Rs 32 (discounted to March '16), assuming (a) Kochi terminal utilization at 40%, (b) nil cut in regasification margin, (c) marketing margins of Rs 15/mnbtu.

City Gas Distribution: Significant cost savings

IGL and Gujarat Gas consume 0.44 and 0.9 mmscmd of RasGas' LNG respectively. Volume growth and margins were negatively impacted as they were unable to pass on higher gas costs to industrial consumers. Lower gas costs can improve EPS of IGL and Gujarat Gas by Rs 10 and Rs 17. However, we expect CGD companies to pass on part of this benefit to consumers through price cuts which may dilute EPS gains. Lower gas prices will also boost industrial demand and be accretive to profitability of CGD companies.

Exhibit 1: Valuation summary

	CMP (Rs)	TP (Rs)	Upside (%)	Rating	EPS (Rs)		PE (x)		P/BV (x)		RoCE (%)	
					FY16E	FY17E	FY16E	FY17E	FY16E	FY17E	FY16E	FY17E
GAIL	375	380	1%	HOLD	18	23	21.4	16.1	1.6	1.5	6	8
GSPL	136	160	17%	BUY	8	10	16.1	13.6	1.9	1.7	16	17
IGL	529	580	10%	HOLD	32	34	16.6	15.7	3.0	2.6	24	23
PLNG	255	250	-2%	HOLD	13	14	19.1	18.8	3.0	2.6	15	15

Source: Companies, Axis Capital CMP as on 31 Dec, 2015

Exhibit 2: GAIL: Changes in estimates

(Rs/sh)	Old		New		Change	
	FY16E	FY17E	FY16E	FY17E	FY16E	FY17E
EPS	16	21	18	23	7%	9%

Source: Axis Capital

Exhibit 3: GAIL – Implied P/E at 13x not cheap

	(Rs)
CMP	375
Less: Value of investments	67
CMP (core business)	308
EPS (FY17)	23
P/E (implied)	13x

Source: Axis Capital

Exhibit 4: Benefit to IGL and Gujarat Gas due to lower gas costs

	IGL	Gujarat Gas
Contracted Ras gas volumes	0.4	0.9
FoB gas prices		
Current Ras gas price	12.3	12.3
Ras gas price, FoB #	7.9	7.9
Landed final consumer gas price		
Current Ras gas price	16.6	15.5
Ras gas price, FoB #	11.3	10.5
Savings in gas cost	5.3	4.4
Lower cost of gas (Rs mn)	2,034	3,467
Post tax benefit(Rs mn)	1,363	2,323
Post tax benefit(Rs/sh)	9.7	16.9

Source: Company, Axis Capital; # 12.7% linkage to JCC crude oil, 3 month trailing crude price

Exhibit 5: PLNG – FY20 earnings under normal business conditions

	FY16E	FY20E
Dahej terminal		
Volumes (mntn)	11.3	15.8
- Long term & tolling	9.5	14.8
- Spot volumes	1.8	1.0
Tariffs (Rs/ mnbtu)		
- Regasification margins	41	48
- Marketing margins	(2)	15
Gross profit (Rs mn)		
- Regasification income	23,613	38,337
- Marketing income	(182)	765
- Gross profit - Dahej (A)	23,431	39,102
Kochi terminal		
Volumes (mntn)	0.1	2.0
Tariffs - total (Rs/ mnbtu)	63	80
Gross profit - Kochi (B)	324	7,074
Total gross profit, Rs mn (A+B)	23,756	46,176
Less: Internal consumption	2,554	7,525
Reported gross profit	21,202	38,652

Source: Company, Axis Capital

IGL and GGAS may have to pass on significant chunk of lower gas costs to consumers

Dahej capacity expansion and higher volumes

Kochi utilization expected at 40%

Exhibit 6: PLNG – FY20 EPS can reach Rs 32/sh

(Rs mn)	FY16E	FY20E
Gross profit	21,202	38,652
Operating expenses	4,423	8,626
EBITDA	16,779	30,026
Depreciation	3,251	4,302
Other income	1,406	9,077
EBIT	14,934	34,801
Interest	2,569	2,445
PBT	12,365	32,356
Tax	3,091	8,089
PAT	9,273	24,267
EPS (Rs/sh)	12.4	32.4

Source: Company, Axis Capital

Exhibit 7: PLNG: CMP implies optimistic assumptions

FY20E EPS	32.4
P/E (3-yr fwd)	12.0
Fair value (Mar '19)	388
Discount rate	15%
Fair value (Mar '16)	255

Source: Company, Axis Capital

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