

### Results above estimates – supported by Gas Marketing. Maintain Accumulate

GAIL Q3FY19 revenue was marginally above estimates. Profitability was better due to higher than expected performance in natural gas marketing segment. Considering the decline in crude oil, performance in gas marketing segment is commendable and made us believe that Q4FY19 performance should also be like last quarter. This has been the biggest hangover on the stock price and will continue to be. Management continues to guide that all cargoes expected in near future are completely hedged. Gas transmission volumes at 107 MMSCMD were marginally below estimates and not expected to improve significantly in the FY20. Petrochemicals business margins are impacted by higher input cost, however, moving towards higher revenue products with better margin will improve the outlook of this segment. Tariff hike for the transmission segment has been the most awaited trigger and is expected now only in second half of FY20. We believe that most of the negatives are priced in the stock. Risk to our call remains significant decline in profitability in gas marketing segment. Maintain Accumulate with a target price of ₹ 372.

### Transmission Volumes muted. Tariff hike awaited.

GAIL managed transmission volumes of 107 MMSCMD which were below by 2% on a sequential basis. We believe that with limited growth in domestic output, future increase will depend on RLNG capacity addition. Considering this, transmission volumes should not grow by more than 5% in FY20 and any significant change will happen only in FY20. PNGRB has sounded optimistic about implementing one nationalized tariff. However, delay has impacted sentiment and with central elections round the corner, we do not see this happening before H2FY20.

### Q3FY19 Result (₹ Mn)

Particulars	Q3FY19	Q3FY18	YoY (%)	Q2FY19	QoQ (%)
Revenue	1,97,890	1,44,143	37.3	1,92,753	2.7
Total Expense	1,71,155	1,24,445	37.5	1,63,478	4.7
EBITDA	26,735	19,699	35.7	29,276	(8.7)
Depreciation	3,634	3,668	(0.9)	3,506	3.7
EBIT	23,101	16,031	44.1	25,770	(10.4)
Other Income	2,201	3,027	(27.3)	3,656	(39.8)
Interest	227	479	(52.7)	455	(50.2)
EBT	25,075	18,580	44.1	28,972	(13.5)
Tax	8,262	5,957	38.7	9,342	(11.6)
RPAT	16,812	12,622	33.2	19,630	(14.4)
APAT	16,812	12,622	33.2	19,630	(14.4)
			(bps)		(bps)
Gross Margin (%)	21.2	25.2	(401)	24.5	(331)
EBITDA Margin (%)	13.5	13.7	(16)	15.2	(168)
NPM (%)	8.5	8.8	(26)	10.2	(169)
Tax Rate (%)	33.0	32.1	89	32.2	71
EBIT Margin (%)	11.7	11.1	55	13.4	(170)

CMP	₹ 332
Target / Upside	₹ 372 / 12%
BSE Sensex	36,617
NSE Nifty	10,934

### Scrip Details

Equity / FV	₹ 22,551mn / ₹ 10
Market Cap	₹ 749bn
	US\$ 10bn
52-week High/Low	₹ 399/₹ 295
Avg. Volume (no)	45,01,030
NSE Symbol	GAIL
Bloomberg Code	GAIL IN

### Shareholding Pattern Dec'18(%)

Promoters	53.1
MF/Banks/FIs	15.9
FII	19.3
Public / Others	11.7

### Valuation (x)

	FY19E	FY20E	FY21E
P/E	12.1	11.3	10.7
EV/EBITDA	7.3	6.6	5.9
ROE (%)	14.7	14.5	14.3
RoACE (%)	19.9	20.1	19.8

### Estimates (₹ mn)

	FY19E	FY20E	FY21E
Revenue	7,54,655	8,14,867	8,79,898
EBITDA	1,01,338	1,10,892	1,17,409
PAT	61,896	66,178	69,858
EPS (₹)	27.4	29.3	31.0

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### US LNG Cargoes – Uncertainty continues despite management assurances

US LNG cargoes has been a long hangover of profitability outlook and will continue to do so. During the crude upward trajectory, GAIL benefitted as these cargoes could have been sold easily in international markets through different mechanisms. However, with crude declining, this has erupted again as a big concern. Segmental profit of this segment has reduced by 35.4%. GAIL management has reassured that all cargoes for next couple of quarters have been tied and expect to keep profitability at the level witnessed in Q3FY19.

### Valuation

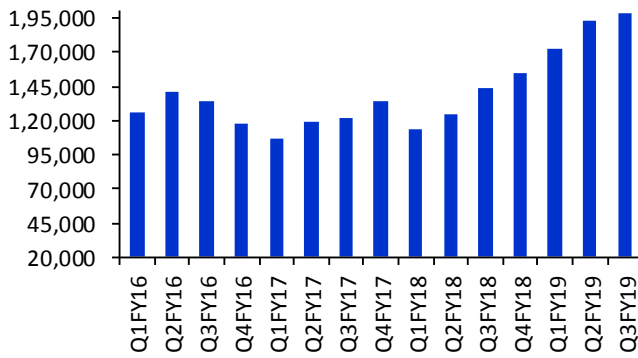
GAIL tariff hike trigger is delayed. With limited increase in volumes, tariff hike is the only resort to improve this segment. US LNG cargoes issue seems to be factored in the price, at least for the couple of quarters. Stock prices seems to be factoring in most of the negatives. We rollover valuations to FY21E. Maintain Accumulate with a target price of ₹ 372.

### Key Highlights

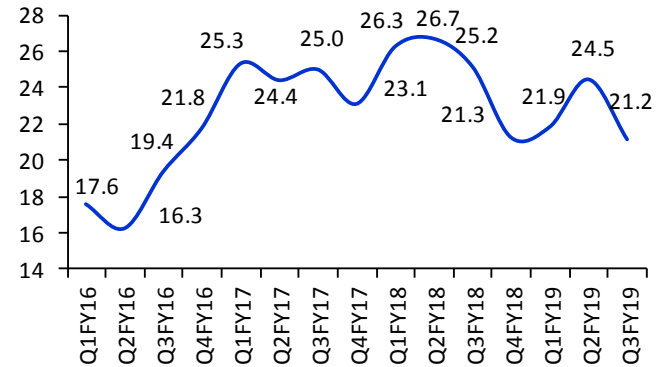
- Revenue increased by 2.7% on a sequential basis and by 37.3% on a YoY basis to ₹ 198 bn.
- Raw Material cost increased by 7.2% on a sequential basis and by 44.7% on a YoY basis to ₹ 156 bn.
- There was a de-growth in employee cost of 34.4% on a sequential basis and 4.3% on a YoY basis to ₹ 3.9 bn.
- Other expenditure decreased by 5.9% on a sequential basis and by 8.6% on a YoY basis to ₹ 11.2 bn.
- GAIL made an operating profit ₹ 26.7 bn in Q3FY19 as compared to an operating profit of ₹ 20 bn in Q3FY18.
- Depreciation increased by 3.7% on a sequential basis and was flat on a YoY basis to ₹ 3.6 bn.
- Other income decreased by 39.8% on a sequential basis and by 21.6% on a YoY basis to ₹ 2.2 bn.
- GAIL made a net profit of ₹ 16.8 bn in Q3FY18 as compared to a net profit of ₹ 12.6 bn in Q3FY18.

### Conference Call KTA's

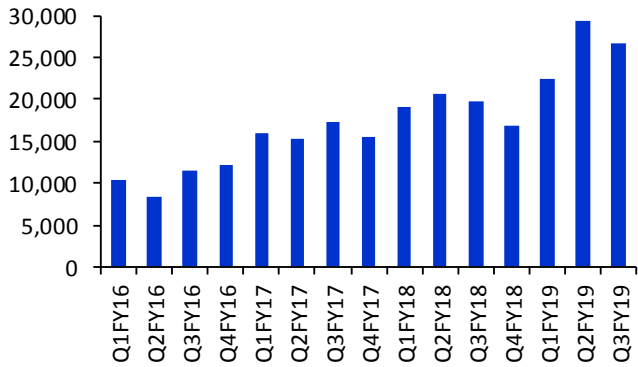
- Profitability was higher due to better performance of gas marketing and transmission segment and LHC segment.
- Transmission volumes were little lower at 107.7 mmscmd as compared to 109.2 mmscmd. Capacity utilisation of natural gas pipeline was 52-53%. Transmission volumes are expected to increase by 5-7% to 110 mmscmd.
- Petrochemicals segment growth remains robust and they are introducing a new grade from Q1FY20 known as metaculin. The plant will run a full capacity utilisation after the shutdown taken in last quarter. Almost 50,000-70,000 tonne of value added products will be produced.
- US volumes imported upto Q3FY19 was 58 LNG cargoes. Out of which 31 were sold in international market and 27 were brought to India via swap arrangement.
- Capex spent for Q3FY19 was ₹ 25,920 Mn and for FY19 is ₹ 64,000 Mn. Total Capex spent till 9MFY19 was ₹ 55,000 Mn. Planned Capex for FY20 is ₹ 70,000 Mn.
- Capital grant received in Q3FY19 was ₹ 5,780 Mn. Till date total grant received is ₹ 20,000 Mn. 405 of capital of ₹ 52,000 Mn for Jagdishpur-Haldia pipeline is received.
- The Jagdishpur-Haldia pipeline has 8 sections. It covers a total area of 3,384 kms with a capex of ₹ 1,60,000 Mn. Last month supply to Varanasi CGD started and even CNG station was set up there. This month they target to reach Patna.
- Pipeline work is as on schedule and excl. Barauni-Guwahati section; pipeline will be operational by Dec 2020. The Barauni-Guwahati will be operational by 2021.
- The Kochi-Mangalore pipeline has 2 sections of 444 kms where 87% of the work is completed. The completion of the pipeline is estimated to be by June 2019. Stage wise commissioning is starting. Total capacity of the pipeline is 16 mmscmd and volumes of less than 3 mmscmd is already tied up.
- US LNG landed price in India is \$7.5/bbl-\$8/bbl in Q3FY19 and Rasgas is \$8.5/bbl.

**Exhibit 1: Revenue (₹ Mn)**


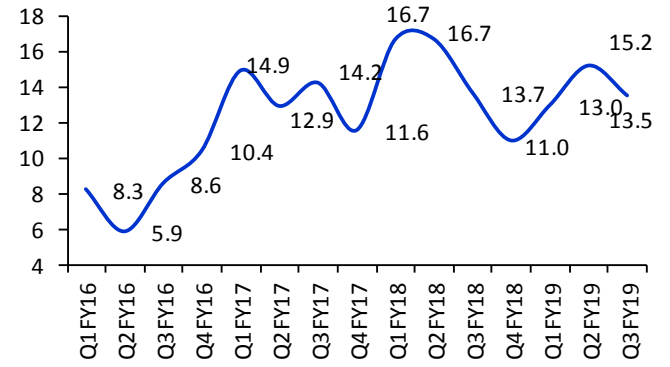
Source: Company, DART

**Exhibit 2: Gross Margin %**


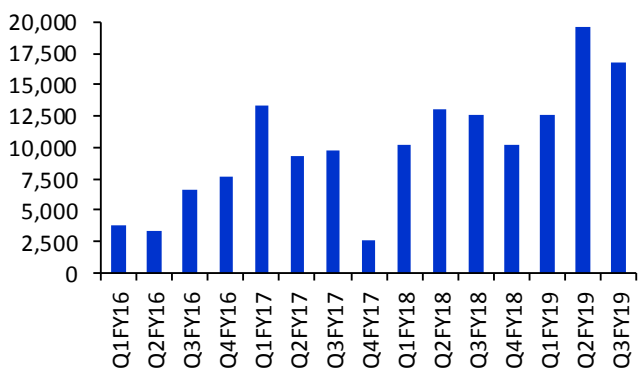
Source: Company, DART

**Exhibit 3: Operating Profit (₹ Mn)**


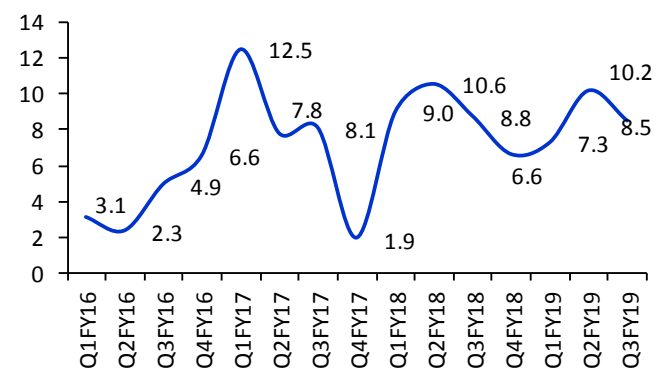
Source: Company, DART

**Exhibit 4: OPM %**


Source: Company, DART

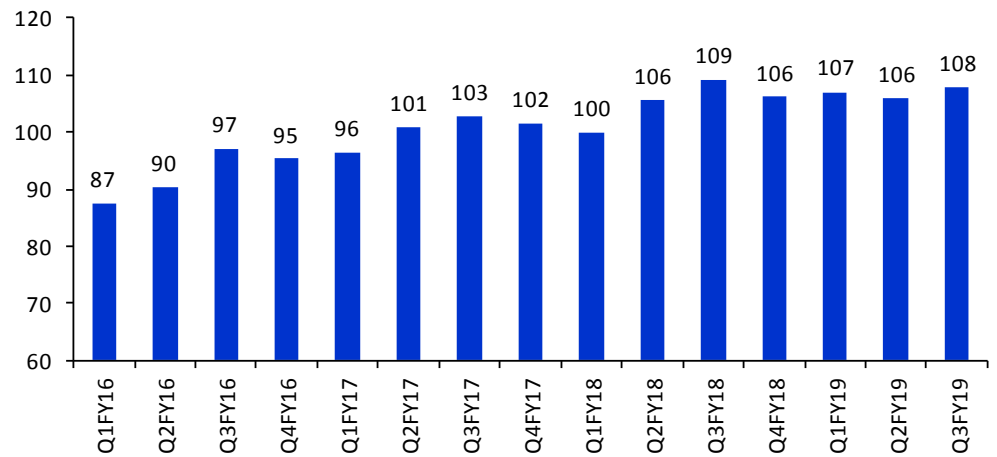
**Exhibit 5: Net Profit (₹ Mn)**


Source: Company, DART

**Exhibit 6: NPM %**


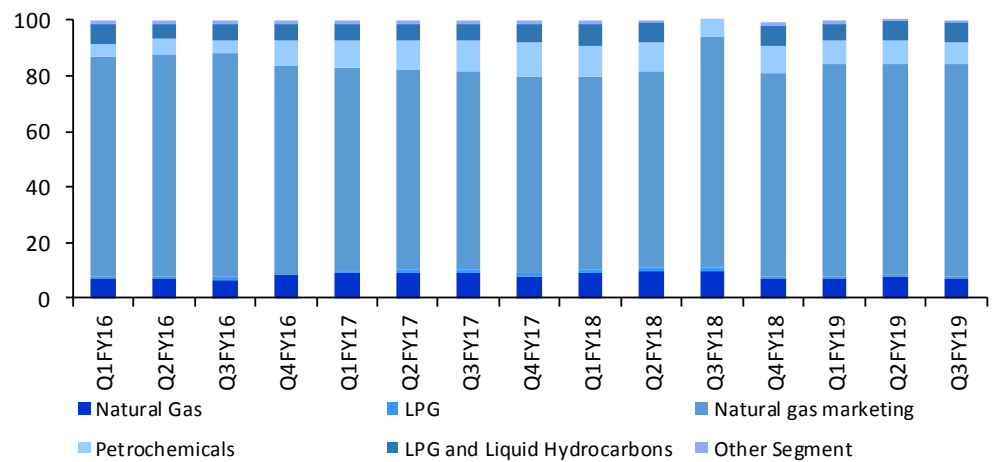
Source: Company, DART

**Exhibit 7: Natural Gas Transmission (MMSCMD)**



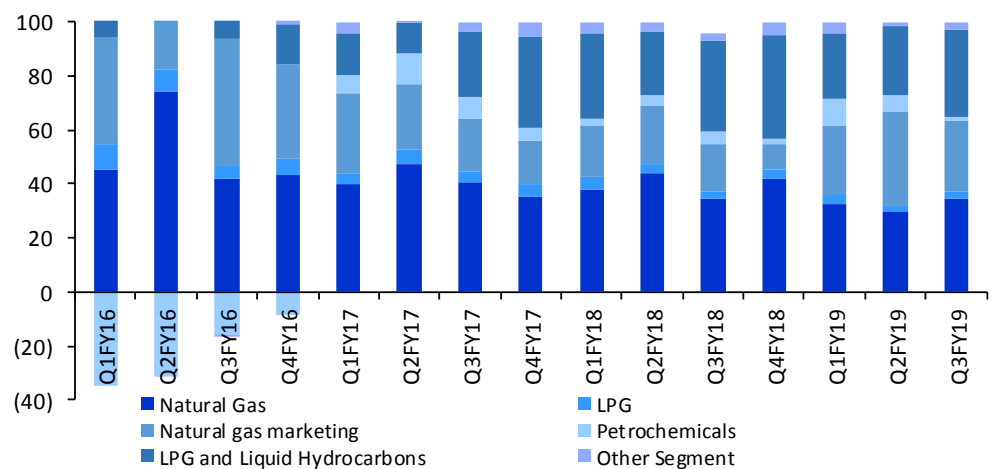
Source: Company, DART

**Exhibit 8: Segment wise % of Total revenue**



Source: Company, DART

**Exhibit 9: Segment wise % of Total Segmental Profit**



Source: Company, DART

### Profit and Loss Account

(₹ Mn)	FY18A	FY19E	FY20E	FY21E
<b>Revenue</b>	<b>5,36,616</b>	<b>7,54,655</b>	<b>8,14,867</b>	<b>8,79,898</b>
<b>Total Expense</b>	<b>4,60,277</b>	<b>6,53,317</b>	<b>7,03,976</b>	<b>7,62,488</b>
COGS	4,04,369	5,92,496	6,39,066	6,91,088
Employees Cost	13,015	14,967	16,763	18,439
Other expenses	42,893	45,854	48,147	52,961
<b>EBIDTA</b>	<b>76,339</b>	<b>1,01,338</b>	<b>1,10,892</b>	<b>1,17,409</b>
Depreciation	14,151	15,015	15,725	15,725
<b>EBIT</b>	<b>62,188</b>	<b>86,323</b>	<b>95,167</b>	<b>1,01,684</b>
Interest	2,751	1,541	1,855	2,210
Other Income	9,870	9,000	8,500	8,000
Exc. / E.O. items	277	0	0	0
<b>EBT</b>	<b>69,584</b>	<b>93,782</b>	<b>1,01,812</b>	<b>1,07,474</b>
Tax	23,400	31,886	35,634	37,616
RPAT	46,184	61,896	66,178	69,858
Minority Interest	0	0	0	0
<b>Profit/Loss share of associates</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>APAT</b>	<b>46,184</b>	<b>61,896</b>	<b>66,178</b>	<b>69,858</b>

### Balance Sheet

(₹ Mn)	FY18A	FY19E	FY20E	FY21E
<b>Sources of Funds</b>				
Equity Capital	22,551	22,551	22,551	22,551
Minority Interest	0	0	0	0
Reserves & Surplus	3,80,731	4,16,245	4,50,764	4,81,050
<b>Net Worth</b>	<b>4,03,281</b>	<b>4,38,795</b>	<b>4,73,315</b>	<b>5,03,601</b>
Total Debt	9,761	7,332	6,599	5,939
Net Deferred Tax Liability	46,309	50,940	56,034	61,638
<b>Total Capital Employed</b>	<b>4,59,352</b>	<b>4,97,068</b>	<b>5,35,948</b>	<b>5,71,178</b>

### Applications of Funds

Net Block	2,87,898	3,32,883	3,87,158	3,91,433
CWIP	55,140	52,852	27,426	32,511
Investments	99,531	95,096	90,000	85,000
<b>Current Assets, Loans &amp; Advances</b>	<b>1,38,253</b>	<b>1,55,927</b>	<b>1,82,230</b>	<b>2,25,169</b>
Inventories	19,195	24,745	24,497	26,457
Receivables	40,515	61,862	66,811	72,156
Cash and Bank Balances	25,294	9,923	25,765	55,073
Loans and Advances	49,806	55,783	61,361	67,497
Other Current Assets	3,443	3,615	3,795	3,985
<b>Less: Current Liabilities &amp; Provisions</b>	<b>1,21,470</b>	<b>1,39,691</b>	<b>1,50,866</b>	<b>1,62,935</b>
Payables	38,816	56,815	61,280	66,269
Other Current Liabilities	82,655	82,876	89,586	96,667
<b>Net Current Assets</b>	<b>16,783</b>	<b>16,237</b>	<b>31,364</b>	<b>62,234</b>
<b>Total Assets</b>	<b>4,59,352</b>	<b>4,97,068</b>	<b>5,35,948</b>	<b>5,71,178</b>

E – Estimates

### Important Ratios

Particulars	FY18A	FY19E	FY20E	FY21E
<b>(A) Margins (%)</b>				
Gross Profit Margin	24.6	21.5	21.6	21.5
EBIDTA Margin	14.2	13.4	13.6	13.3
EBIT Margin	11.6	11.4	11.7	11.6
Tax rate	33.6	34.0	35.0	35.0
Net Profit Margin	8.6	8.2	8.1	7.9
<b>(B) As Percentage of Net Sales (%)</b>				
COGS	75.4	78.5	78.4	78.5
Employee	2.4	2.0	2.1	2.1
Other	8.0	6.1	5.9	6.0
<b>(C) Measure of Financial Status</b>				
Gross Debt / Equity	0.0	0.0	0.0	0.0
Interest Coverage	31.3	71.6	64.4	56.7
Inventory days	13	12	11	11
Debtors days	28	30	30	30
Average Cost of Debt	13.8	18.0	26.6	35.3
Payable days	26	27	27	27
Working Capital days	14	6	10	20
FA T/O	1.9	2.3	2.1	2.2
<b>(D) Measures of Investment</b>				
AEPS (₹)	20.5	27.4	29.3	31.0
CEPS (₹)	26.8	34.1	36.3	38.0
DPS (₹)	7.2	10.0	12.0	15.0
Dividend Payout (%)	35.1	36.4	40.9	48.4
BVPS (₹)	178.8	194.6	209.9	223.3
RoANW (%)	11.8	14.7	14.5	14.3
RoACE (%)	15.9	19.9	20.1	19.8
RoAIC (%)	14.3	18.7	19.1	19.8
<b>(E) Valuation Ratios</b>				
CMP (₹)	332	332	332	332
P/E	16.2	12.1	11.3	10.7
Mcap (₹ Mn)	7,48,909	7,48,909	7,48,909	7,48,909
MCap/ Sales	1.4	1.0	0.9	0.9
EV	7,29,561	7,43,318	7,26,743	6,96,775
EV/Sales	1.4	1.0	0.9	0.8
EV/EBITDA	9.6	7.3	6.6	5.9
P/BV	1.9	1.7	1.6	1.5
Dividend Yield (%)	2.2	3.0	3.6	4.5
<b>(F) Growth Rate (%)</b>				
Revenue	11.4	40.6	8.0	8.0
EBITDA	19.1	32.7	9.4	5.9
EBIT	24.1	38.8	10.2	6.8
PBT	28.6	34.8	8.6	5.6
APAT	31.8	34.0	6.9	5.6
EPS	31.8	34.0	6.9	5.6

### Cash Flow

(₹ Mn)	FY18A	FY19E	FY20E	FY21E
CFO	86,626	69,877	85,672	88,885
CFI	(25,680)	(40,679)	(35,673)	(17,134)
CFF	(54,705)	(30,037)	(34,157)	(42,443)
FCFF	57,201	12,764	41,098	63,800
Opening Cash	4,519	10,761	9,923	25,765
Closing Cash	10,761	9,923	25,765	55,073

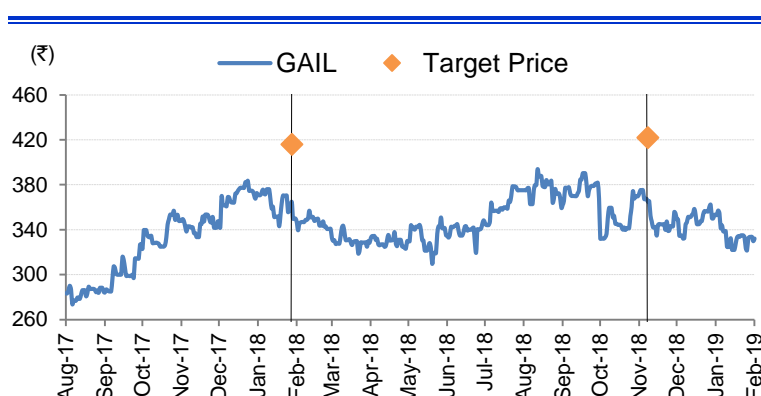
E – Estimates

### DART RATING MATRIX

Total Return Expectation (12 Months)

Buy	> 20%
Accumulate	10 to 20%
Reduce	0 to 10%
Sell	< 0%

### Rating and Target Price History



Month	Rating	TP (₹)	Price (₹)
Feb-18	Accumulate	416	365
Nov-18	Accumulate	422	365

\*Price as on recommendation date

### DART Team

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