Sharekhan
by BNP PARIBAS

Petronet LNG

Dahej utilisation continues to surprise positively

Sector: Oil & Gas
Result Update

	Change
Reco: **Buy**	↔
CMP: **Rs. 285**	
Price Target: **Rs. 330**	↑

↑ Upgrade ↔ No change ↓ Downgrade

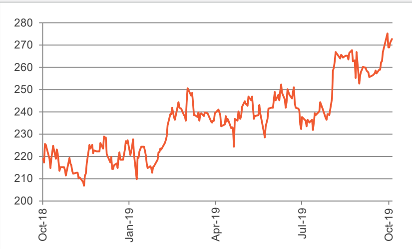
Company details

Market cap:	Rs. 42,803 cr
52-week high/low:	Rs. 302/203
NSE volume: (No of shares)	30.8 lakh
BSE code:	532522
NSE code:	PETRONET
Sharekhan code:	PETRONET
Free float: (No of shares)	75.0 cr

Shareholding (%)

Promoters	50.0
FII	27.2
DII	10.0
Others	12.8

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	7.2	20.5	18.6	33.0
Relative to Sensex	4.3	13.7	15.3	12.3

Sharekhan Research, Bloomberg

Petronet LNG (PLNG) reported a strong set of numbers in Q2FY2020 with adjusted operating profit at Rs. 1,046 crore (up 16.2% y-o-y; up 13.9% q-o-q) and adjusted PAT stood at Rs. 818 crore (up 42.5% y-o-y; up 37.6% q-o-q), above our estimates of Rs. 726 crore. The strong performance was driven by sharp jump in Dahej re-gas volumes to 240 tBtu (up 13.7% y-o-y; up 10.6% q-o-q). The Kochi terminal's utilisation rate also improved to 15.7% from 14.1% in Q1FY2020. PLNG's strong volume led earnings visibility (we expect a 16% earnings CAGR over FY19-FY21E) and superior RoE of 28-30% make it an attractive investment proposition in the domestic gas utilities space. Hence, we maintain our Buy rating on the stock with a revised price target (PT) of Rs. 330.

Key positives

- Dahej re-gas volume higher than expected, at 240 tBtu (up 10.6% q-o-q)
- Kochi terminal utilization improved to 15.7% (from 14.1% in Q1FY2020)
- Declared special dividend of Rs. 5.5/share

Key negatives

- Long-term contracted volume at Dahej terminal declined by 6% y-o-y to 109 tBtu

Our Call

Valuation - Maintain Buy with revised PT of Rs. 330: We have increased our FY2020 earnings estimates to factor in higher re-gas volumes at Dahej and a lower effective tax rate. We have also fine-tuned our FY2021 earnings estimates to reflect a marginally lower utilisation rate for the Kochi terminal (given a slight delay in construction of Kochi-Mangalore gas pipeline). We believe that PLNG is well-placed to benefit from rising gas demand, supported by its recent capacity expansion to 17.5 mmt at the Dahej terminal and plans to further expand capacity to 19.5 mmt in the next 2-3 years by setting up two storage tanks and a jetty. PLNG's strong volume-led earnings visibility (we expect a 16% earnings CAGR over FY19-FY21E) and superior RoE of 28-30% make it an attractive investment proposition in the gas utilities space. Hence, we maintain our Buy rating on the stock with a revised price target of Rs. 330 (valued at 16x FY2021E EPS of Rs. 20.5).

Key Risks

Sharp rise in LNG price could impact re-gas volumes at the Dahej terminal and continued delay in the ramp-up of utilization rate at the Kochi terminal due to pipeline connectivity issues.

Valuation (standalone) Rs cr

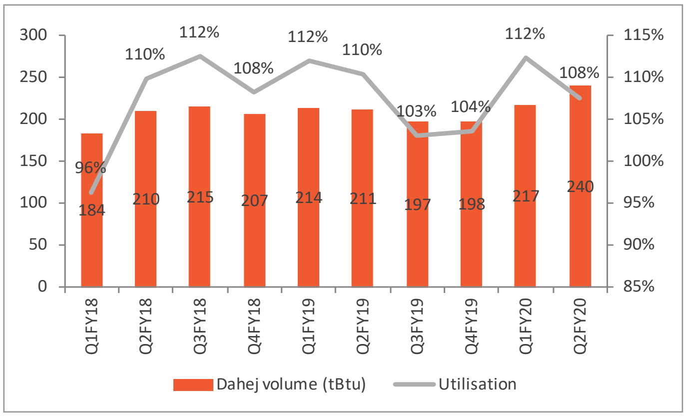
Particulars	FY17	FY18	FY19	FY20E	FY21E
Revenue	24,616	30,599	38,395	42,069	50,303
OPM (%)	10.5	10.8	8.9	9.4	8.5
Adjusted PAT	1,706	2,078	2,291	3,098	3,078
% YoY growth	86.8	21.8	10.3	35.2	-0.6
Adjusted EPS (Rs)	11.4	13.9	15.3	20.7	20.5
P/E (x)	25.1	20.6	18.7	13.8	13.9
P/B (x)	5.3	4.4	4.3	4.1	3.9
EV/EBITDA (x)	15.9	11.7	11.4	9.9	9.1
RoNW (%)	23.2	23.3	23.2	30.1	28.4
RoCE (%)	22.8	26.3	27.3	30.1	31.4

Source: Company; Sharekhan estimates

Adjusted PAT beats estimates; Robust Dahej re-gas volume of 240 tBtu (up 10.6% q-o-q)

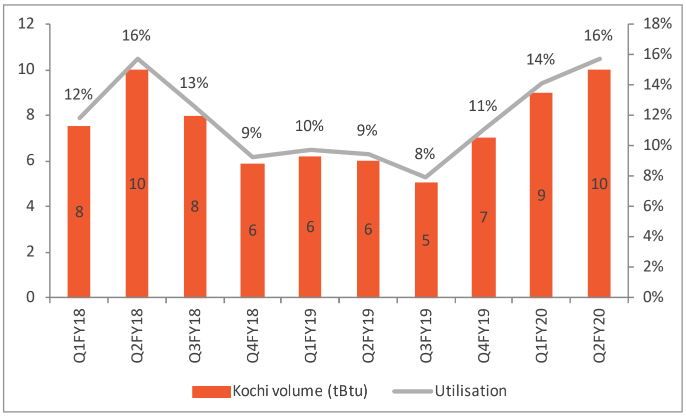
Petronet LNG's (PLNG's) Q2FY2020 reported operating profit of Rs. 1,160 crore and PAT of Rs. 1,103 crore are not comparable with previous quarters and our estimates due to implementation of the IND-AS 116 for leases and re-assessment of deferred tax liability. As a result of the switch to IND-AS 116, reported operating profit was inflated by Rs. 114 crore. Adjusting for the same, the operating profit stood at Rs. 1,046 crore (up 16.2% y-o-y; up 13.9% q-o-q), marginally below our estimate of Rs. 1,073 crore. Dahej terminal re-gas volumes stood at 240 tBtu (up 13.7% y-o-y; up 10.6% q-o-q), above our estimate of 235 tBtu. The Kochi terminal's volume stood at 10 tBtu (up 66.1% y-o-y; up 11.1% q-o-q) leading to higher utilisation rate of 15.7% versus 14.1% in Q1FY2020. As a result of implementation of IND AS 116 (negative impact of Rs137 crore) and one-time settlement for lease rent related to Kochi terminal (negative impact of Rs72 crore), reported PBT was lower by Rs209 crore. Adjusting for the same, PLNG's PBT was at Rs1,093 crore (up 23.7% y-o-y; up 22.9% q-o-q). Adjusted PAT, at Rs. 818 crore, (up 42.5% y-o-y; up 37.6% q-o-q) was higher than our estimate of Rs. 726 crore. Reported PAT stood at Rs. 1,103 crore (up 96% y-o-y; up 97% q-o-q) was supported by lower tax rate due to re-measurement of deferred tax liability pertaining to previous quarter.

Robust Dahej terminal volume and utilisation



Source: Company, Sharekhan Research

Kochi terminal volume and utilization trend



Source: Company, Sharekhan Research

Q2FY2020 results conference call highlights

- PLNG guided that the Kochi-Mangalore pipeline section would get completed by December 2019 (versus October 2019 earlier) and could also witness delay of additional 1-2 months beyond December-2019.
- Update on Tellurian Inc. deal – The company is in the process of appointing a consultant for due diligence and the deal is expected to be finalised by March 2020 with flexibility for a 1-2 month delay. The management has maintained that proposed deal with Tellurian is a non-binding memorandum of understanding (MoU) and PLNG would limit its exposure to 1-2mtpa (investment of $500million to $1billion) with back-to-back contracts for volume offtake in the absence of its affiliate companies.
- The company has guided for a capex of Rs. 450 crore for FY2020E and plans to build two storage tanks, which would require a capex of ~Rs. 1,300 crore in the next 2-3 years. The company also plans to build a jetty which would cost ~$130 million.
- The management has also highlighted that there is no reversal of the inventory loss of Rs. 119 booked in Q4FY2019.
- The delivered LNG price from Qatar and Gorgon stood at $8-9/mmBtu in Q2FY2020.
- The annual escalation clause does not have any element of revision based on the corporate tax rate.

Results Rs cr

Particulars	Q2FY20	Q2FY19	YoY %	Q1FY20	QoQ %
Net Sales	9,361	10,745	-12.9	8,613	8.7
Total Expenditure	8,201	9,862	-16.8	7,590	8.1
Reported operating profit	1,160	884	31.3	1,024	13.3
Adjusted operating profit	**1,046**	**901**	**16.2**	**919**	**13.9**
Other Income	98	111	-12.5	104	-6.6
Interest	105	25	322.4	101	4.6
Depreciation	196	104	89.0	190	3.2
PBT before one-time items	957	867	10.4	838	14.2
One-time lease settlement for Kochi terminal	72	0	NA	0	NA
Reported PBT	885	867	2.1	838	5.6
Exceptional items	-209	-17	NA	-52	NA
Adjusted PBT	1,093	884	23.7	890	22.9
Tax	-218	304	NA	278	NA
RPAT	1,103	563	96.0	560	96.9
Adjusted PAT	**818**	**574**	**42.5**	**595**	**37.6**
Equity Cap (cr)	150	150		150	
Reported EPS (Rs)	7.4	3.8	96.0	3.7	96.9
Adjusted EPS	5.5	3.8	42.5	4.0	37.6
Margins (%)			**BPS**		**BPS**
Adjusted OPM	11.2	8.4	280	10.7	51
Adjusted NPM	8.7	5.3	340	6.9	183

Source: Company; Sharekhan Research

Operating performance

Particulars	Q2FY20	Q2FY19	YoY %	Q1FY20	QoQ %
Capacity utilisation – Dahej (%)	107.6	110.4	-276	112.3	-467
Capacity utilisation – Kochi (%)	15.7	9.4	624	14.1	157
Total volume (TBTU)	**250.0**	**217.0**	**15.2**	**226.0**	**10.6**
Long term volume – Dahej	109.0	116.0	-6.0	100.0	9.0
Tolling volume – Dahej	126.0	88.0	43.2	112.0	12.5
Spot volume – Dahej	5.0	7.0	-28.6	5.0	0.0
Total Dahej volume (TBTU)	**240.0**	**211.0**	**13.7**	**217.0**	**10.6**
Long term volume – Kochi	5.0	6.0	-16.7	7.0	-28.6
Tolling volume – Kochi	3.0	0.0	NA	1.0	200.0
Spot volume – Kochi	2.0	0.0	NA	1.0	100.0
Total Kochi volume (TBTU)	**10.0**	**6.0**	**66.1**	**9.0**	**11.1**

Source: Company; Sharekhan Research

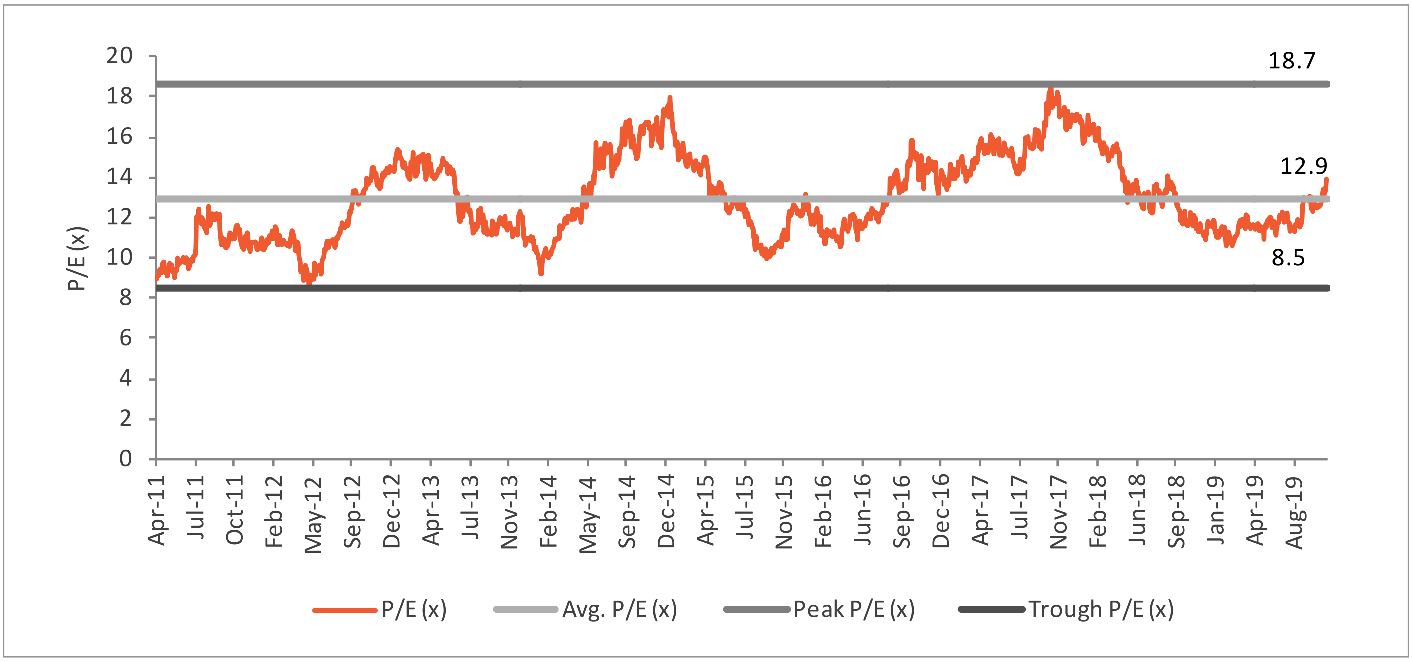
Outlook - Dahej terminal to operate above 100% utilization supported by strong LNG demand

We expect PLNG's Dahej LNG terminal to operate at near 100% utilisation in FY2020E given a strong demand outlook for imported LNG especially from city gas distribution (CGD) companies, industrial and power sectors, long-term contracted volume and limited competition from upcoming terminals. Although there is a slight delay in completion of the Kochi-Mangalore pipeline section (now expected by December 2019 versus an earlier guidance of October 2019), but after the completion of pipeline the utilization rate for Kochi terminal is expected to improve in FY2021E. Hence, we expect volume and earnings CAGR of 8% and 16% over FY2019-FY2021E.

Valuation - Maintain Buy with revised PT of Rs. 330

We have increased our FY2020 earnings estimated to factor higher re-gas volumes at Dahej and a lower effective tax rate. We have also fine-tuned our FY2021 earnings estimates to reflect a marginally lower utilisation rate for the Kochi terminal (given a slight delay in construction of Kochi-Mangalore gas pipeline). PLNG is well-placed to benefit from rising gas demand, supported by its recent capacity expansion to 17.5 mmt at the Dahej terminal and plans to further expand capacity to 19.5 mmt in the next 2-3 years by setting up two storage tanks and a jetty. PLNG's strong volume-led earnings visibility (we expect a 16% earnings CAGR over FY19-FY21E) and superior RoE of 28-30% make it an attractive investment proposition in the gas utilities space. Hence, we maintain our Buy rating on the stock with a revised price target of Rs. 330 (valued at 16x FY2021E EPS of Rs. 20.5).

One-year forward P/E (x) band



Source: Sharekhan Research

About company

PLNG was incorporated in April 1998. PLNG imports, re-gasifies and markets liquefied natural gas (LNG) in India. The company owns and operates India's largest LNG terminal with a capacity of 15 mmt at Dahej (Gujarat) and 5 mmt at Kochi (Kerala). The company has recently expanded its Dahej terminal to 17.5 mmt in June 2019 and plans to further increase the capacity to 19.5 mmt in the next 2-3 years. The company operates on a simple business model of charging re-gas margins on the LNG volume imported (both long-term and spot) through its terminals. The company earns additional marketing margins on spot volumes. The company's business is de-risked through back-to-back offtake contracts with customers.

Investment theme

PLNG's growth would be primarily driven by increase in its re-gas volumes supported by recent expansion of its Dahej terminal capacity to 17.5 mmt and improvement in utilisation rate of the Kochi terminal (currently operating at 14% utilisation). Resolution of pipeline connectivity issues in southern India is expected to improve utilisation at the Kochi terminal. Moreover, PLNG would able to take 5% re-gas tariff escalation for its Dahej terminal on a regular basis as it enjoys a competitive edge as compared to other LNG import terminals given its low re-gas tariff and long-term contracted volume with a 'use or pay' clause.

Key Risks

- Sharp rise in LNG prices could lower utilisation for the PLNG's Dahej terminal
- Delay in laying of pipeline could keep Kochi terminal's utilisation rate low for an extended period
- Non-revision of re-gas tariffs on a yearly basis.

Additional Data

Key management personnel

Prabhat Singh	Managing Director & CEO
Vinod Kumar Mishra	Director - Finance
Rajender Singh	Director - Technical

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Indian Oil Corporation Limited	12.5
2	GAIL (India) Limited	12.5
3	Bharat Petroleum Corporation Limited	12.5
4	Oil and Natural Gas Corporation Limited	12.5
5	BlackRock Inc	2.5
6	Kotak Mahindra Asset Management Company	2.3
7	FMR LLC	2.0
8	Franklin Resources Inc	1.9
9	Aditya Birla Sun Life Trustee Company Private Limited	1.4
10	Vanguard Group Inc/The	1.3

Source: Bloomberg

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