Sharekhan
by BNP PARIBAS

Petronet LNG

Strong LNG demand to aid volume growth

Sector: Oil & Gas
Company Update

	Change
Reco: **Buy**	↔
CMP: **Rs. 278**	
Price Target: **Rs. 345**	↑

↑ Upgrade ↔ No change ↓ Downgrade

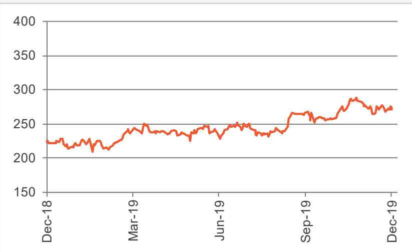
Company details

Market cap:	Rs. 41,693 cr
52-week high/low:	Rs. 302/209
NSE volume: (No of shares)	31.3 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	0.1	7.8	26.3	28.3
Relative to Sensex	-2.3	-5.0	18.3	11.3

Sharekhan Research, Bloomberg

We remain constructive on Petronet LNG (PLNG) for two reasons – First, we expect steady volume growth in the next 2-3 years, as volumes ramp up at the Kochi terminal with the nearing completion of the Kochi-Mangaluru pipeline and gradual volume growth at Dahej terminal. Second, we expect PLNG to continue to take the annual 5% re-gas tariff hike at the Dahej terminal given its competitive edge of lowest tariff in the industry. Hence, we expect PLNG to deliver a strong EBITDA/PAT CAGR of 12%/8% over FY2020E-FY2022E and a robust RoE of ~29-30%. Strong gas demand supported by low spot LNG price and regulatory push should help drive up volumes for PLNG, given lower domestic gas output. Earnings growth visibility makes the stock's valuation attractive at 11.6x FY2022E EPS and the likelihood of a higher dividend payout in FY2020E (in the absence of any significant capex) is comforting to investors. Hence, we maintain our Buy rating on PLNG with a revised price target (PT) of Rs. 345 (roll over to FY2022E EPS).

Kochi terminal utilisation to rise as Kochi-Mangaluru pipeline nears completion; Dahej utilisation to remain above 100%: As per media reports, GAIL (India) is nearing the completion of construction work at the Kochi-Mangaluru pipeline section with ~441.5kms (out of 444kms) of work already accomplished; the pipeline is expected to commissioned by March 2020. We expect utilisation rate at PLNG's Kochi terminal to improve to 25%/38% in FY2021E/FY2022E from ~16% currently, as new consumers (largely refiners and fertiliser plants) are expected to start their LNG offtake post the completion of pipeline section. Additionally, strong gas demand especially from industrial customers (supported by low LNG prices and regulatory push to curb pollution) and a likely delay in ramp-up of domestic gas production would help PLNG sustain high utilisation rate at the Dahej terminal. The company's competitive edge (lowest tariffs in industry) would also help it to take 5% annual re-gas tariff hike.

Our Call

Valuation - Maintain Buy with revised PT of Rs. 345: We have fine-tuned our FY2020E EPS and increased FY2021E EPS to factor in 5% escalation for Dahej re-gas tariffs. We have also introduced our FY2022E EPS of Rs. 23.9. We expect PLNG to be biggest beneficiary of rising share of LNG in India's overall gas consumption mix, as a timely ramp-up of capacities (recently expanded Dahej capacity to 17.5 mmt 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) and ramp-up of volumes at Kochi terminal would ensure continued volume growth in the next 2-3 years. We thus expect an EBITDA/PAT CAGR of 12%/8% over FY2020E-FY2022E along with a robust RoE of ~29-30% for PLNG. The stock is also trading at attractive valuation of 13x FY2021E EPS and 11.6x FY2022E EPS. Hence, we maintain our Buy rating on PLNG with a revised PT of Rs. 345 as we roll over our valuation to FY2022E EPS.

Key Risks

Lower-than-expected volume at Dahej if LNG price rises sharply, continued delay in ramp-up of volumes at the Kochi terminal and non-revision of re-gas tariffs on a yearly basis.

Valuation (standalone) Rs cr

Particulars	FY18	FY19	FY20E	FY21E	FY22E
Revenue	30,599	38,395	36,394	39,685	42,742
OPM (%)	10.8	8.9	10.8	11.3	11.6
Adjusted PAT	2,078	2,291	3,099	3,210	3,581
% YoY growth	21.8	10.3	35.2	3.6	11.6
Adjusted EPS (Rs)	13.9	15.3	20.7	21.4	23.9
P/E (x)	20.1	18.2	13.5	13.0	11.6
P/B (x)	4.3	4.1	4.0	3.7	3.1
EV/EBITDA (x)	11.4	11.1	9.6	8.5	7.3
RoNW (%)	23.3	23.2	30.1	29.6	29.1
RoCE (%)	26.3	27.3	30.1	32.6	32.9

Source: Company; Sharekhan estimates

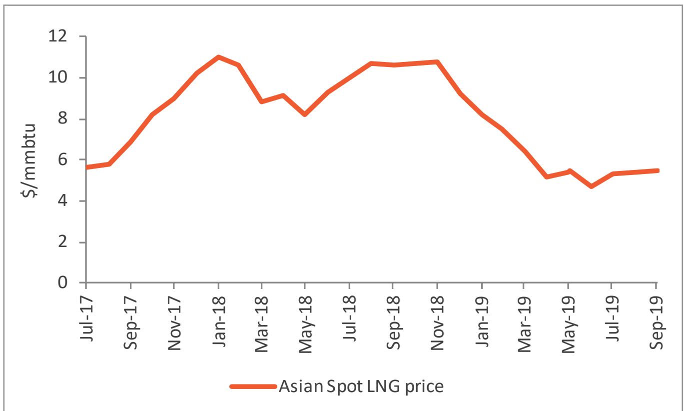
Kochi terminal - volume ramp-up expected soon as commissioning of Kochi-Mangaluru pipeline likely by Mar-2020

As per media reports, GAIL (India) has completed pipeline construction work of a ~441.5 km stretch (out of the total 444 km) for the Kochi-Mangaluru pipeline section and expects to commission the pipeline by March 2020. With the likely commissioning of this pipeline section, we expect utilisation rate for PLNG's Kochi terminal would improve to 25%/38% in FY2021E/FY2022E from low levels of ~16% in Q2FY2020. However, there is not much clarity regarding the timeline for completion of Kochi-Bengaluru section of the pipeline. Any resolution on that front could substantially improve the capacity utilisation at the Kochi terminal and drive earnings growth beyond FY2022. Every 1 mmt increase in volume at the Kochi terminal could add around Rs. 1.5/share to PLNG's earnings per share (EPS).

LNG imports increased sharply by 8.3% y-o-y during April-October 2019

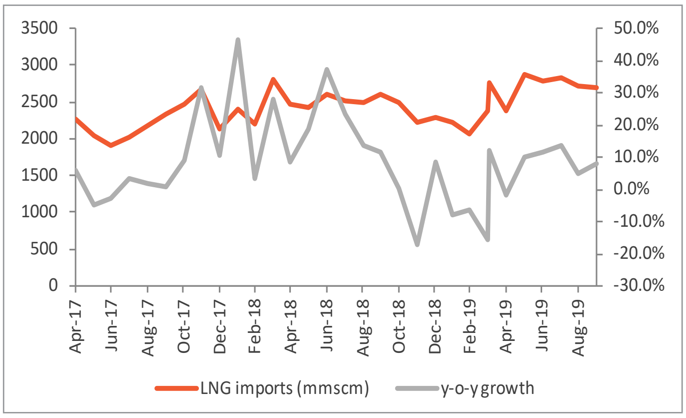
With the decline in domestic natural gas production by 2.6% y-o-y during April to October 2019, the requirement of natural gas was largely fulfilled by LNG imports, which grew sharply by ~8.3% y-o-y to 14.4 million tonne during April to October 2019. The sharp rise in the LNG imports was backed by strong demand from the power, fertiliser and city gas distribution (CGD) sectors, given low spot LNG prices of $5-5.5/mmBtu. We expect spot LNG prices to remain weak given a supply glut on the back of new LNG capacities in the US and Australia. Low LNG prices could work in favour of a revival of stranded gas-based power plants.

Spot LNG price at $5.5/mmbtu



Source: Bloomberg

India's LNG import trend



Source: Petroleum Planning and Analysis Cell

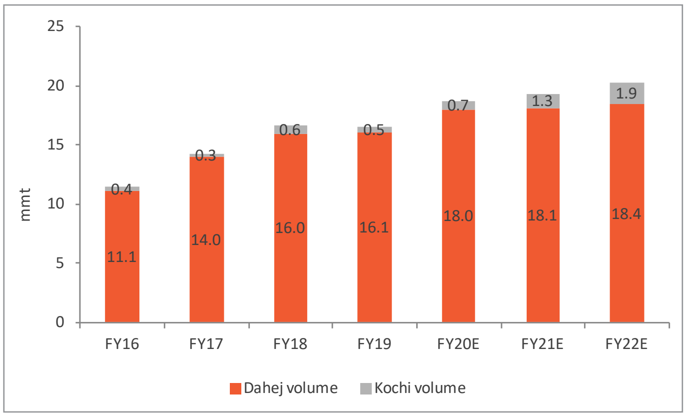
Sectoral consumption of natural Gas (October-2019) – Imported LNG share at 53%

Sectors (mmscm)	Domestic Gas	R-LNG	Total	Share of R-LNG
Fertilizer	598	750	1348	56%
CGD	490	416	906	46%
Power	657	248	905	27%
Refinery	93	581	674	86%
Petrochemical	64	238	302	79%
Others	324	290	614	47%
Total	**2,226**	**2,523**	**4,749**	**53%**

Source: Petroleum Planning and Analysis Cell

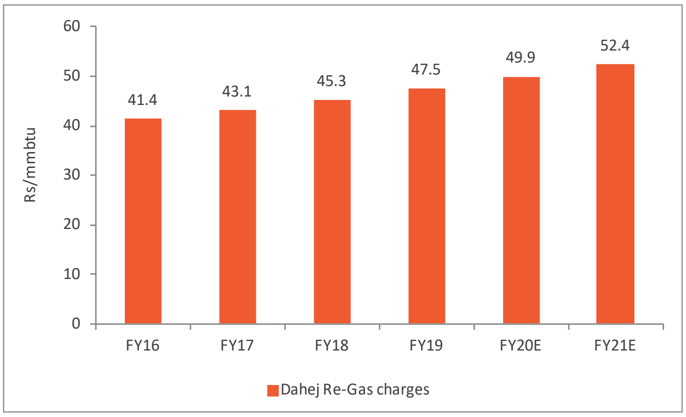
Financials in charts

Volumes growth led by capacity expansion and Kochi ramp-up



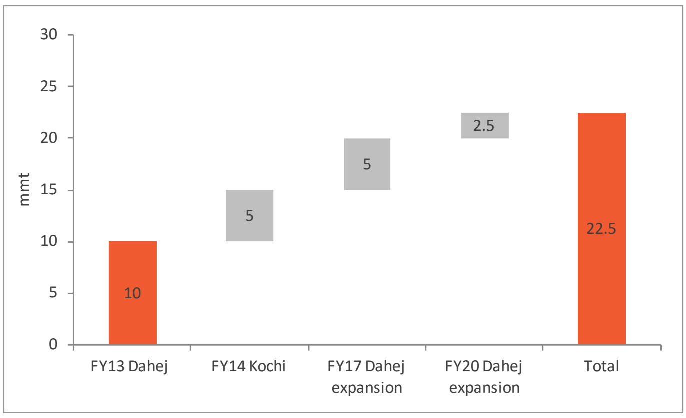
Source: Company, Sharekhan Research

Consistent hike in Dahej Re-gas charges



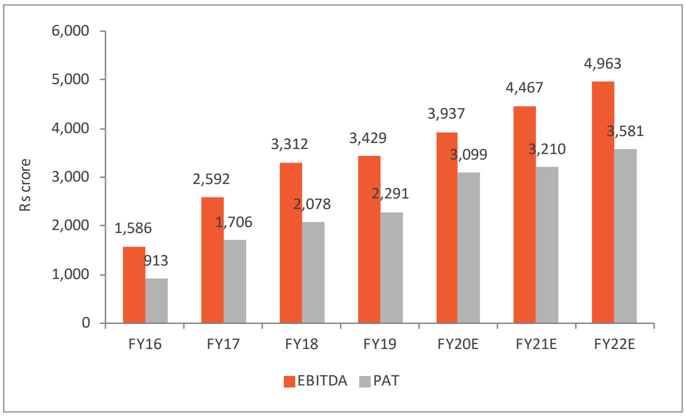
Source: Company, Sharekhan Research

PLNG capacity expansion over FY13-FY20E



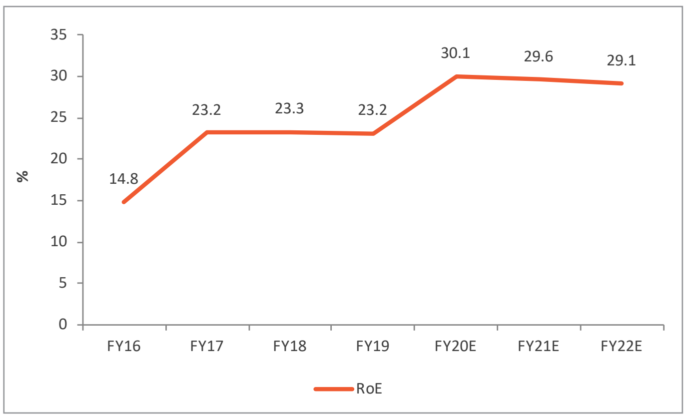
Source: Company, Sharekhan Research

EBITDA/PAT to clock 12%/8% CAGR over FY20E-FY22E



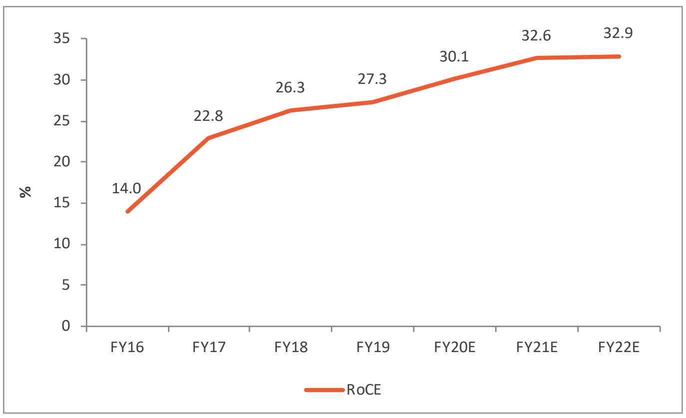
Source: Company, Sharekhan Research

Strong RoEs driven by earnings growth



Source: Company, Sharekhan Research

Consistent improvement in RoCE



Source: Company, Sharekhan Research

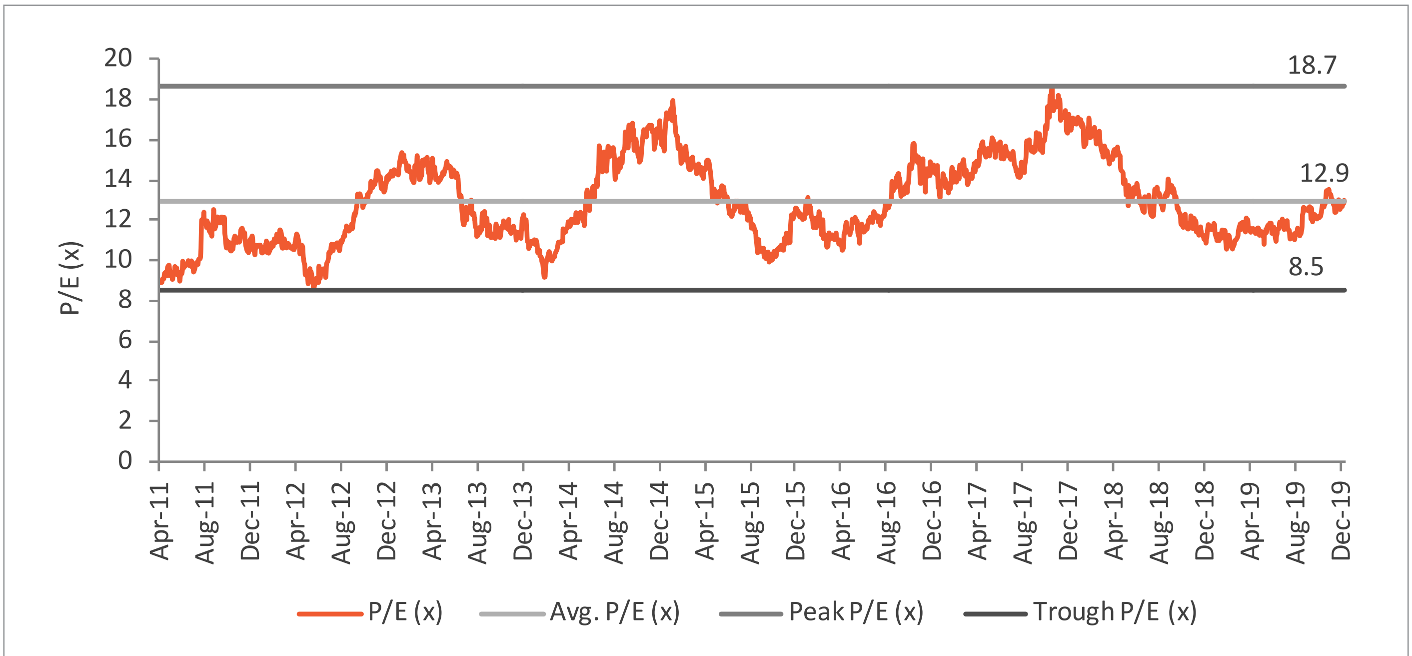
Outlook

Strong earnings visibility led by volume growth and hike in Dahej re-gas tariff: We expect PLNG's Dahej LNG terminal to operate at near 100% utilisation rate over FY2020E-FY2022E 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. We expect utilisation rate at PLNG's Kochi terminal to improve to 25%/38% in FY2021E/FY2022E from ~16% levels as new consumers (largely refiners and fertiliser plants) are likely to begin their LNG offtake post the completion of Kochi-Mangaluru pipeline section by March-2020. Volume growth coupled with hike in re-gas tariff at Dahej terminal provides strong earnings growth visibility for PLNG.

Valuation

Maintain Buy with revised PT of Rs. 345: We have fine-tuned our FY2020E EPS and increased FY2021E EPS to factor in 5% escalation for Dahej re-gas tariffs. We have also introduced our FY2022E EPS of Rs. 23.9. We expect PLNG to be biggest beneficiary of rising share of LNG in India's overall gas consumption mix, as a timely ramp-up of capacities (recently expanded Dahej capacity to 17.5 mmt 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) and ramp-up of volumes at Kochi terminal would ensure continued volume growth in the next 2-3 years. We thus expect an EBITDA/PAT CAGR of 12%/8% over FY2020E-FY2022E along with a robust RoE of ~29-30% for PLNG. The stock is also trading at attractive valuation of 13x FY2021E EPS and 11.6x FY2022E EPS. Hence, we maintain our Buy rating on PLNG with a revised PT of Rs. 345 as we roll over our valuation to FY2022E EPS.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

PLNG was incorporated in April 1998. The company 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 pipelines could keep the 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

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Oil & Natural Gas Corp Ltd	12.5
2	Bharat Petroleum Corp Ltd	12.5
3	Indian Oil Corp Ltd	12.5
4	GAIL India Ltd	12.5
5	BlackRock Inc	2.51
6	Kotak Mahindra Asset Management Co	2.49
7	FMR LLC	1.95
8	Franklin Resources Inc	1.94
9	Aditya Birla Sun Life Trustee Co P	1.37
10	Vanguard Group Inc/The	1.29

Source: Bloomberg

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