HOLD (Maintained)

CMP: **INR 202** Target Price: **INR 210 (INR 235)** ▲ 4%

ICICI Securities

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31 October 2023

India | Equity Research | Q2FY24 result review

Petronet LNG

Oil & Gas

Aggressive expansion plans risks returns dilution

Petronet LNG (PLNG) reported a 4% YoY improvement in EBITDA to INR 12.1bn and a 10% YoY rise in PAT to INR 8.2bn, up 3/4% QoQ. Management has raised the estimated investment on the PDHPP plant (nameplate capacity of ~0.75mtpa of PDH, split into 0.25kt of Propylene, 0.5mt of Polypropylene) at an investment of INR 210bn. This is way higher than the earlier indicative investment of INR 140bn (attributed to ethane handling facility and some costs not disclosed earlier). We confess that we struggle to understand the basis for management assertion that this is a 20% IRR project – our assessment of rough cut numbers indicates a much lower return profile for the project, underpinning our reiteration of **HOLD** despite low valuations, recent underperformance, steady EPS growth and high dividend yields.

Volumes strong YoY, dip QoQ due to lower re-gas volumes

Dahej's long-term volume was up 13% QoQ (down 1% YoY) to 102tbtu while service volume at 102btu was up sharply by 32% YoY but down 17% QoQ. Spot cargoes were at 6tbtu. While Kochi's volumes of 13tbtu remained modest, the imminent completion of the second leg of the Kochi-Mangalore-Bengaluru pipeline and softer LNG prices should drive volumes higher over the next 12–18 months. Overall, a strong recovery is in prospect over FY24E–FY26E for PLNG volumes, particularly if the recent moderation in spot LNG prices sustains over the next 6– 12 months.

Volume recovery to sustain over FY24–26E

PLNG expects the global supply situation to be better, with improvement in Mozambique's security situation, US FIDs and Qatar's additional capacity to help ease the global supply balance (as per IGU: against just 19.9mtpa of global export capacity addition in CY22, CY23-CY27 period may see an aggregate 178.4mtpa of projects in construction or development as of Apr'23; refer here). This coincides with the completion of the 5mtpa of additional capacity at Dahej and the completion of the Kochi-Bengaluru leg of Kochi offtake pipelines. As long as disruptions to Russian supply remain contained at current levels, additional LNG supplies may ease pricing pressures in the medium term.

Financial Summary

Y/E March (INR mn)	FY23A	FY24E	FY25E	FY26E
Net Revenue	5,98,994	7,51,920	8,57,385	10,05,757
EBITDA	48,540	52,846	56,275	60,276
EBITDA %	8.1	7.0	6.6	6.0
Net Profit	33,258	35,428	37,227	39,333
EPS (INR)	22.2	23.6	24.8	26.2
EPS % Chg YoY	(3.3)	6.5	5.1	5.7
P/E (x)	9.1	8.5	8.1	7.7
EV/EBITDA (x)	5.6	5.1	4.8	4.5
RoCE (Pre-tax) (%)	22.9	23.0	22.7	22.4
RoE (%)	23.0	22.2	21.4	20.7

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Market Data

Market Cap (INR)	303bn
Market Cap (USD)	3,634mn
Bloomberg Code	PLNG IN
Reuters Code	PLNG.BO
52-week Range (INR)	254 /197
Free Float (%)	50.0
ADTV-3M (mn) (USD)	8.0

Price Performance (%)	3m	6m	12m
Absolute	(10.8)	(13.7)	1.1
Relative to Sensex	(8.0)	(19.7)	(7.2)

ESG Disclosure	2021	2022	Change
ESG score	34.5	45.3	10.8
Environment	3.3	30.8	27.5
Social	21.4	21.4	-
Governance	78.6	83.6	5.0

Note - Score ranges from 0 - 100 with a higher score indicating higher ESG disclosures.

Source: Bloomberg, I-sec research

Earnings Revisions (%)	FY24E	FY25E
Revenue	(1.4)	(1.4)
EBITDA	(1.6)	(2.0)
EPS	(1.3)	(1.8)

Previous Reports

01-08-2023: Q1FY24 results review

04-05-2023: Q4FY23 results review

Petchem investment needs very high margins to meet management targets of profitability

Management disclosed the formal approval by the company's Board of the proposed 0.75mt capacity Propane Dehydrogenation project to produce Polyproylene, Ethane and Hydrogen (PDHPP). Total investment in the project has been raised to INR 206.9bn, out of which soft project cost is INR 167bn and other costs including contingency costs, margin money etc. form another ~INR 40bn. The initial project cost was estimated at INR 140bn, which did not include ethane handling capacity, contingency, escalation, etc.

At these costs, management has stated that at a basic assumption of Propane-Propylene margin of USD 200/t and USD 600/t margin of Propylene-Propane, the project can deliver an IRR of 20% and equity IRR of 30% (assuming a 30:70 DER). They also mention an expected EBITDA of INR 40bn from the project at a steady state. To achieve this EBITDA, however, our rough cut estimates suggest that the project needs to earn EBITDA/t of USD 800+ (Exhibit 12), which seems like a tall ask, given that even for integrated players (read RELIANCE) EBITDA/t has languished at <USD 300/t levels for the last 2-3 years. Add to that, significant capacity being added by BPCL and other players in India – we see material challenges to achieving this level of margin for PLNG.

On balance, PLNG is looking at a steady state growth of 5.8% (EPS CAGR FY23-26E), strong cash flows (aggregate OpCF of INR 136bn over FY23-26E), attractive valuations (8.1 FY25E PER/ 4.7 FY25E EV/EBITDA) and high dividend yield (estimated at 7.1–7.4% over FY24-25E). All of this, however, gets counterbalanced by what looks to us as a risky bet on diversification at a scale at which PLNG has not operated before. Reiterate **HOLD** with a revised TP of INR 210/share.

Key risks

Upside risks: Stronger utilisation, sharp reduction in LNG prices, favourable extension of the RasGas contract.

Downside risks: Higher disruption in Russian supplies, slower execution of expansion plans.

Conference call takeaways

- The board has approved petrochemical (petchem) project for setting up 750KTPA of PDH and 500KTPA of PP plant including propane and ethane handing facility at Dahej. Total estimated project cost is INR 206.9bn out of which soft project cost is INR 167bn, other costs at ~Rs40bn. The initial project cost was estimated at INR 140bn, which does not include ethane capacity, contingency, escalation, etc.
- The company has already signed term sheet with Deepak Phenolics Limited for offtake of 250KTPA of propylene and 11KTPA of Hydrogen. The balance 500KTPA will be converted to polypropylene to be sold in open market.
- As per management, the project is estimated to generate IRR of 20% and equity IRR of 30%. The project is proposed to be funded by 30:70 Equity:Debt. Spreads for Propane-Propylene and Propane-Polypropylene is estimated at USD 200/t and 600/t respectively considering 7 year averages.
- The project is likely to commission by FY28 and is estimated to generate EBITDA of INR 40bn. 50% of profitability is assured due to Ethane handling and offtake arrangements signed already.

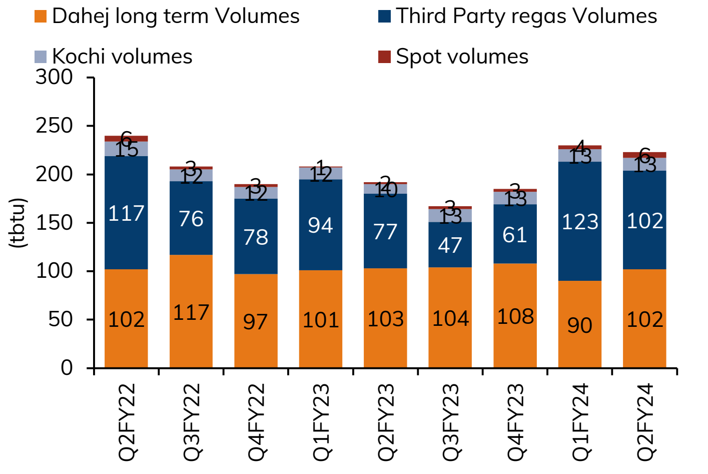
- This petchem will have advantages of: 1) Common jetty, which is already being approved. 2) Cold energy wasted at LNG plant can be used by the petchem plant and could save ~INR 1–1.2bn on power cost.
- The expansion of regasification terminal from 17.5mt to 20mt and thereafter 20 to 22.5mt, will be commissioned by March'25. Work on storage tank at Dahej is on in full swing – expected to complete by June'24
- Gopalpur project is pending for Board approval. Lease agreements with port – a prerequisite for the project for FSRU.
- No progress on realising the pending user take or pay charges during the quarter.
- On renewal of LNG contract with Qatar, the company is confident of closing it by Dec'23.
- The company's re-gas tariff is at Dahej terminal is INR 59.1/mmbtu and INR 85.09/mmbtu at Kochi Terminal. Current LNG prices is at USD15/mmbtu and as per company should be <USD 18/MMBtu in near term with Europe already at > 95% of storage capacity.
- Dhamra terminal tariff is >INR 60/MMBtu, which is higher than PLNG Dahej terminal.
- The Board approved special dividend of INR 7/share and guided that 100% dividend rate should continue for the medium term.
- We note that management is planning a separate interaction to discuss the Petrochemical project in detail – we will update details of the same as and when it happens.

Exhibit 1: Q2FY24 result snapshot

INR mn	Q2FY24	Q2FY23	YoY (%)	Q1FY24	QoQ (%)	H1FY24	H1FY23
Net Sales	**1,25,320**	**1,59,857**	**(21.6)**	**1,16,561**	**7.5**	**2,41,881**	**3,02,496**
EBITDA	12,147	11,730	3.6	11,818	2.8	23,965	22,373
EBITDA (INR/mmbtu)	54.5	61.1	(10.8)	51.4	6.0	52.9	55.9
Reported PAT	8,181	7,443	9.9	7,899	3.6	16,080	14,452
Adjusted PAT	**8,181**	**7,443**	**9.9**	**7,899**	**3.6**	**16,080**	**14,452**
EPS (INR)	5.5	5.0	9.9	5.3	3.6	10.72	9.63
Dahej Sales (tbtus)	210	182	15.4	217	(3.2)	427	378
Other income	1,567	942	66.3	1,467	6.8	3,035	2,360
Depreciation	1,948	1,922	1.4	1,919	1.5	3,867	3,835
Interest paid	747	811	(7.9)	746	0.2	1,493	1,590
Gross margins (INR/mmbtu)	68.4	86.1	(20.6)	59.6	14.6	64.3	79.3
Kochi (tbtu)	13.0	10.0	30.0	13.0	0.0	26.0	22.0
Total volume (tbtu)	**223.0**	**192.0**	**16.1**	**230.0**	**(3.0)**	**453.0**	**400.0**
Gross margins mns	8,271	9,898	(16.4)	6,382	29.6	14,653	18,160

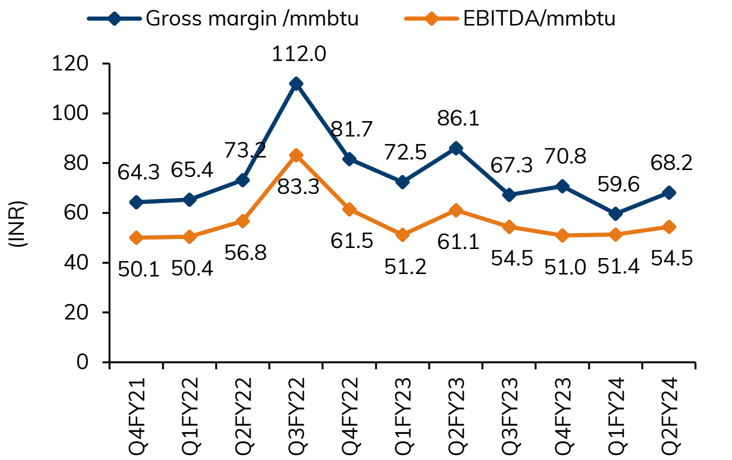
Source: Company data, I-Sec research

Exhibit 2: Overall Q2FY24 volumes remain muted QoQ



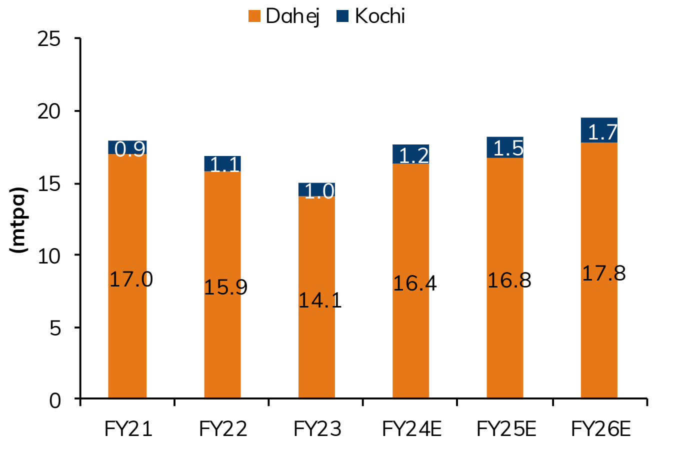
Source: Company data, I-Sec research

Exhibit 3: Tariffs – gross margin rises in Q2FY24



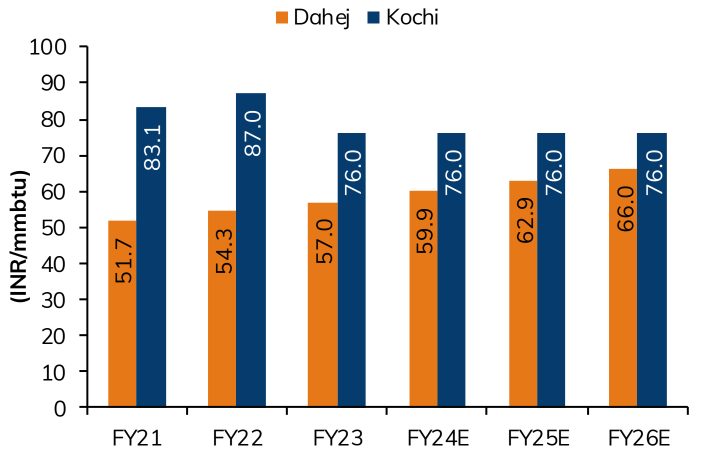
Source: Company data, I-Sec research

Exhibit 4: Volumes likely to improve over FY24E-FY26E



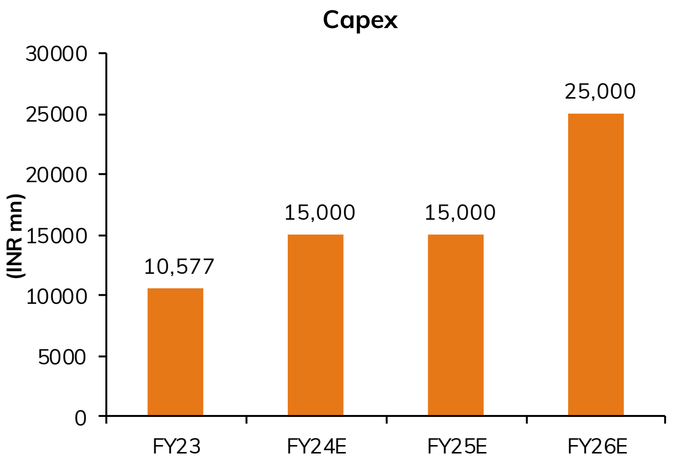
Source: Company data, I-Sec research

Exhibit 5: Blended tariffs expected to remain muted



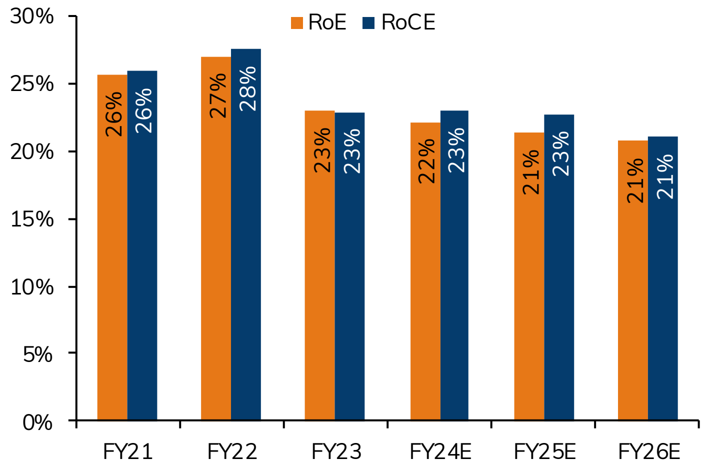
Source: Company data, I-Sec research

Exhibit 6: FY24E-FY26E capex likely to grow materially



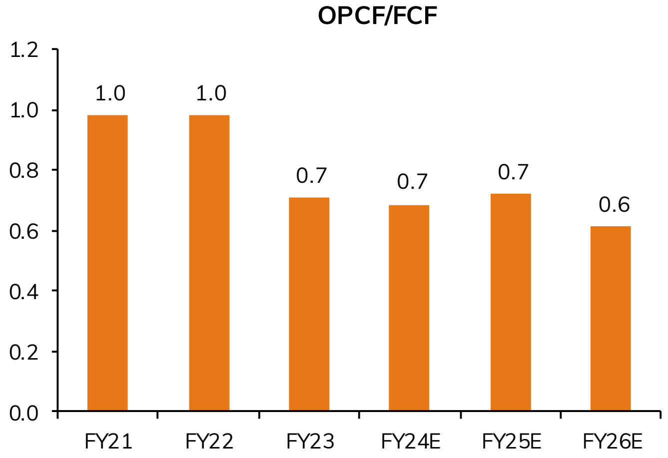
Source: Company data, I-Sec research

Exhibit 7: Return ratios may remain healthy



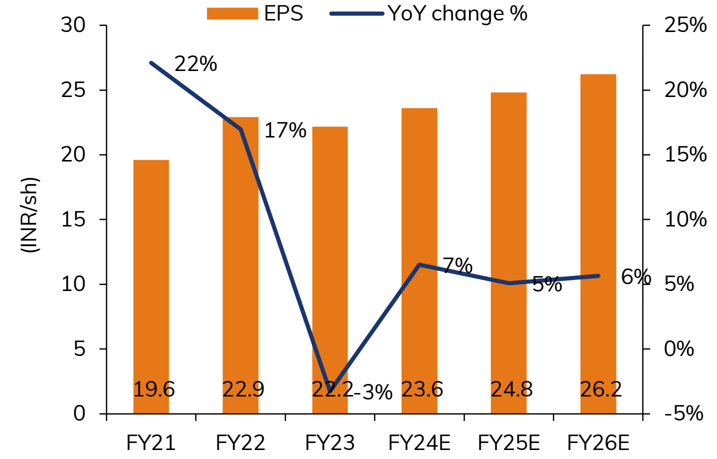
Source: Company data, I-Sec research

Exhibit 8: OpCF/FCF to remain at comfortable levels



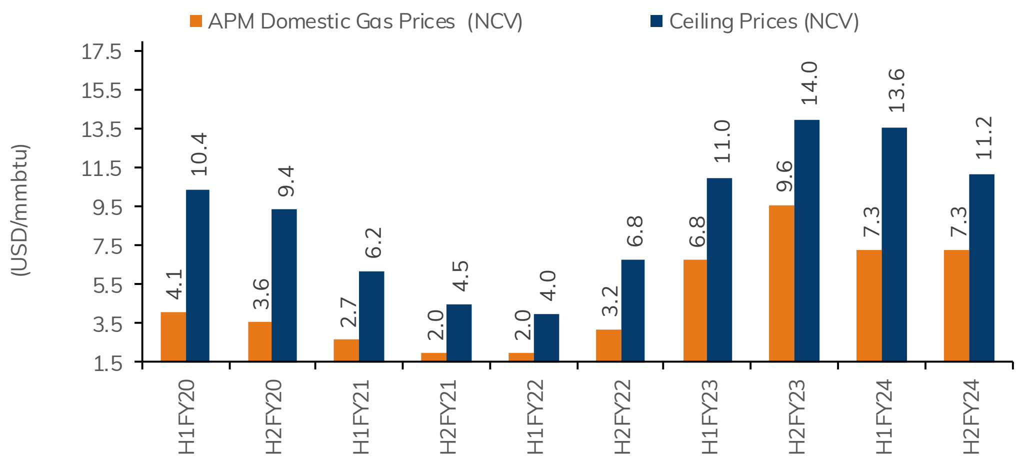
Source: Company data, I-Sec research

Exhibit 9: Earnings growth likely to moderate



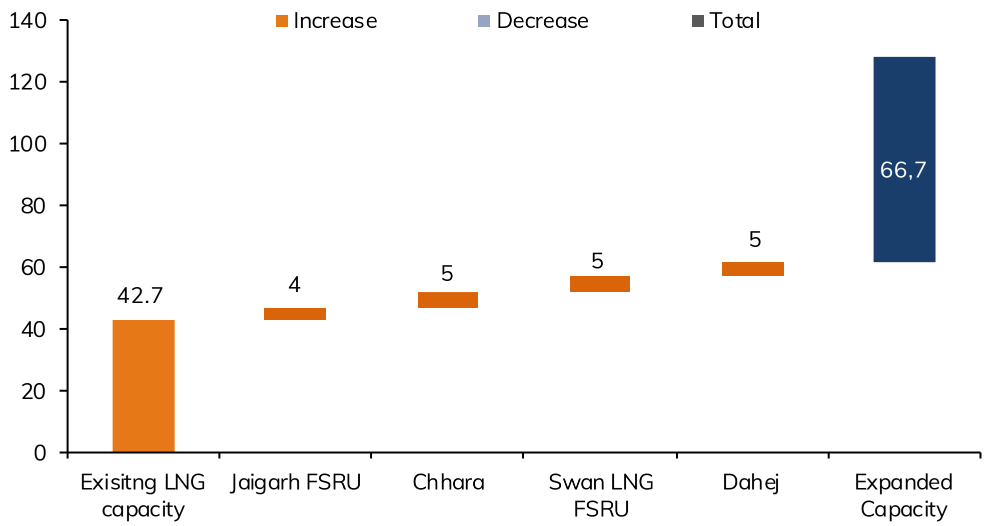
Source: Company data, I-Sec research

Exhibit 10: APM gas price capped at USD 6.5/mmbtu and HPHT gas price reduced by 18% in H2FY24 vs. H1FY24



Source: Company data, I-Sec research

Exhibit 11: LNG capacity envisaged to reach 66.7mtpa by FY26E



Source: PPAC , Company data , I-Sec research

Exhibit 12: Petchem expansion estimates – very aggressive assumptions feeding into PLNG targeted EBITDA from this project

Particulars	Units	
Investment	INR mn	2,06,850
Capacity	mt	0.75
EBITDA (RIL estimated Petchem EBITDA at ~USD 250-270/t)	USD/t	400
EBITDA	USD mn	300
EBITDA	INR mn	25,050
Depreciation (5%)	INR mn	10,343
EBIT	INR mn	14,708
ROCE (Pre-Tax)	INR mn	7.1%
For ROCE (Pre-Tax) of 20%	20%	
EBITDA has to be	USD/t	826
EBITDA targeted by PLNG	INR mn	41,370

Source: Bloomberg, I-Sec research

Valuation: **HOLD**; target price of INR 210

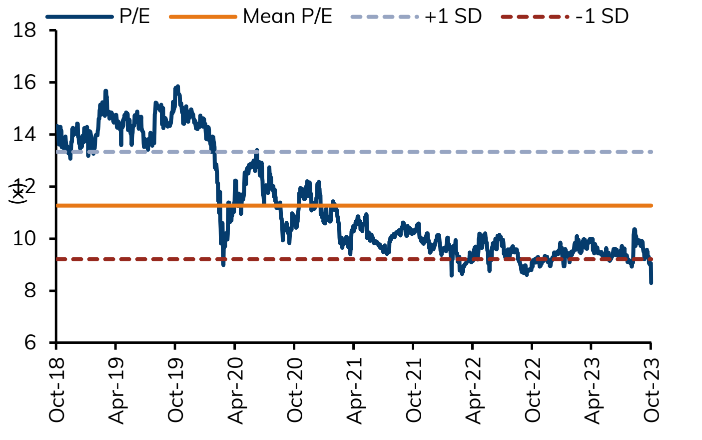
We value PLNG as per the DCF methodology, using a WACC of 12%, DER of 15%, long-term Dahej utilisation assumption of 100% and terminal growth rate of 3.0%. This leads to our target price of INR210/sh, ~4% upside from CMP.

Exhibit 13: Valuation summary

	Assumption
Cost of equity	13%
Cost of Debt	9%
WACC	12%
Terminal Growth Rate	3%
Average NPV potential (Rs mn)	3,15,211
Target Price (Rs)	210
CMP	202
Upside/(Downside)	4%

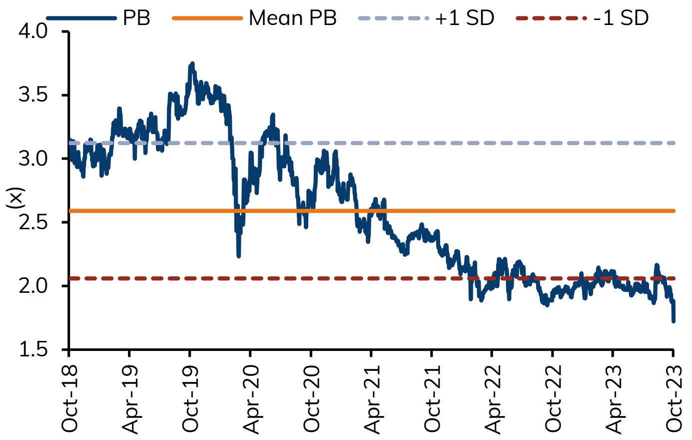
Source: Bloomberg, Company data

Exhibit 14: PLNG's P/E trading band below 5-year mean



Source: Company data, I-Sec research

Exhibit 15: PLNG's P/B trading band below 5-year mean



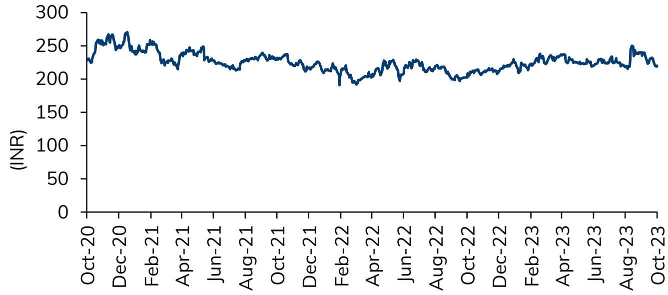
Source: Company data, I-Sec research

Exhibit 16: Shareholding pattern

%	Mar'23	Jun'23	Sep'23
Promoters	50.0	50.0	50.0
Institutional investors	39.4	39.2	39.2
MFs and other	3.0	3.4	4.8
FIs/ Banks	1.6	1.8	1.9
Insurance Cos.	0.0	0.0	0.0
FIIs	34.8	34.0	32.5
Others	10.6	10.8	10.8

Source: Bloomberg, I-Sec research

Exhibit 17: Price chart



Source: Bloomberg, I-Sec research

Financial Summary

Exhibit 18: Profit & Loss

(INR mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
Net Sales	**5,98,994**	**7,51,920**	**8,57,385**	**10,05,757**
EBITDA	**48,540**	**52,846**	**56,275**	**60,276**
EBITDA Margin (%)	8.1	7.0	6.6	6.0
Depreciation & Amortization	7,643	8,545	9,409	10,849
EBIT	40,896	44,301	46,866	49,427
Interest expenditure	-	-	-	-
Other Non-operating Income	5,231	4,405	4,154	4,319
PBT	**42,822**	**45,741**	**48,144**	**-**
Profit / (Loss) from Associates	**1,380**	**1,200**	**1,200**	**1,200**
Less: Taxes	10,944	11,513	12,118	12,827
PAT	31,878	34,228	36,027	38,133
Less: Minority Interest	-	-	-	-
Net Income (Reported)	**33,258**	**35,428**	**37,227**	**-**
Extraordinaries (Net)	-	-	-	-
Recurring Net Income	**33,258**	**35,428**	**37,227**	**39,333**

Source Company data, I-Sec research

Exhibit 19: Balance sheet

(INR mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
Total Current Assets	1,09,773	1,20,953	1,32,325	1,37,245
of which cash & bank	56,858	55,092	57,536	49,890
Total Current Liabilities & Provisions	26,259	30,797	33,944	38,357
Net Current Assets	**83,514**	**90,156**	**98,381**	**98,888**
Other Non Current Assets	4,907	4,925	4,944	-
Net Fixed Assets	87,903	94,358	99,950	1,14,101
Other Fixed Assets	-	-	-	-
Capital Work in Progress	11,259	11,259	11,259	11,259
Non Investment	4,986	5,036	5,087	5,137
Current Investment	8,697	8,784	8,872	8,961
Deferred Tax assets	-	-	-	-
Total Assets	**2,01,266**	**2,14,519**	**2,28,492**	**2,43,308**
Liabilities				
Borrowings	**33,450**	**32,450**	**31,450**	**30,450**
Deferred Tax Liability	**7,026**	**7,026**	**7,026**	**7,026**
Lease Liability	33,450	32,450	31,450	30,450
Other Liabilities	8,145	8,226	8,308	-
Equity Share Capital	15,000	15,000	15,000	15,000
Reserves & Surplus	1,37,646	1,51,817	1,66,707	1,82,441
Total Net Worth	**1,52,646**	**1,66,817**	**1,81,707**	**1,97,441**
Minority Interest	-	-	-	-
Total Liabilities	**2,01,266**	**2,14,519**	**2,28,492**	**2,43,308**

Source Company data, I-Sec research

Exhibit 20: Quarterly trend

(INR mn, year ending March)

	Dec-22	Mar-23	Jun-23	Sep-23
Net Sales	1,50,102	1,38,739	1,16,561	1,25,320
% growth (YOY)	-6.1%	-7.6%	-16.0%	7.5%
EBITDA	9,097	9,431	11,818	12,147
Margin %	6.1%	6.8%	10.1%	9.7%
Other Income	1,839	1,538	1,467	1,567
Extraordinaries	7,657			
Adjusted Net Profit	4,149	6,142	7,899	8,181

Source Company data, I-Sec research

Exhibit 21: Cashflow statement

(INR mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
Cash Flow from operation before working Capital	**54,012**	**52,846**	**56,275**	**60,276**
Working Capital Changes	(15,941)	(8,345)	(5,717)	(8,088)
Tax	(12,380)	(11,513)	(12,118)	(12,827)
Operating Cashflow	**25,690**	**32,988**	**38,440**	**39,361**
Capital Commitments	(10,577)	(15,000)	(15,000)	(25,000)
Free Cashflow	**15,113**	**17,988**	**23,440**	**14,361**
Others CFI	22,163	5,468	5,215	5,379
Cashflow from Investing Activities	**11,586**	**(9,532)**	**(9,785)**	**(19,621)**
Inc (Dec) in Borrowings	(6,177)	(1,000)	(1,000)	(1,000)
Interest Cost	(253)	(2,966)	(2,876)	(2,786)
Others	(17,250)	(21,257)	(22,336)	-
Cash flow from Financing Activities	**(23,681)**	**(25,222)**	**(26,211)**	**(27,385)**
Chg. in Cash & Bank balance	**13,595**	**(1,766)**	**2,444**	**(7,646)**
Closing cash & balance	56,858	55,092	57,536	49,890

Source Company data, I-Sec research

Exhibit 22: Key ratios

(Year ending March)

	FY23A	FY24E	FY25E	FY26E
Per Share Data (INR)				
Recurring EPS	22.2	23.6	24.8	26.2
Diluted EPS	22.2	23.6	24.8	26.2
Recurring Cash EPS	27.3	29.3	31.1	33.5
Dividend per share (DPS)	10.0	14.2	14.9	15.7
Book Value per share (BV)	101.8	111.2	121.1	131.6
Dividend Payout (%)	45.1	60.0	60.0	60.0
Growth (%)				
Net Sales	38.8	25.5	14.0	17.3
EBITDA	(7.5)	8.9	6.5	7.1
EPS	(3.3)	6.5	5.1	5.7
Valuation Ratios (x)				
P/E	9.1	8.5	8.1	7.7
P/CEPS	7.4	6.9	6.5	6.0
P/BV	2.0	1.8	1.7	1.5
EV / EBITDA	5.6	5.1	4.8	4.5
EV / Operating Income	5.9	5.6	5.2	-
Dividend Yield (%)	5.0	7.0	7.4	7.8
Operating Ratios				
EBITDA Margins (%)	8.1	7.0	6.6	6.0
Effective Tax Rate (%)	25.6	25.2	25.2	25.2
Net Profit Margins (%)	5.6	4.7	4.3	3.9
NWC / Total Assets (%)	41.5	42.0	43.1	40.6
Fixed Asset Turnover (x)	4.5	5.3	5.5	5.7
Working Capital Days	23.3	22.4	21.5	21.7
Net Debt / Equity %	(21.0)	(18.8)	(19.2)	(14.4)
Profitability Ratios				
RoCE (%)	17.0	17.2	17.0	16.8
RoCE (Pre-tax) (%)	22.9	23.0	22.7	22.4
RoE (%)	23.0	22.2	21.4	20.7

Source Company data, I-Sec research

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