

**BUY**

TP: Rs 350 | ▲ 60%

**GUJARAT STATE  
PETRONET**

Oil &amp; Gas

31 December 2019

**Power demand could be a dark horse**

**Our interaction with the Gujarat State Petronet (GSPL) management reinforces our core investment thesis. Key takeaways: a) Power demand could pick up substantially (from FY21) on improved power demand outlook, coupled with low LNG prices; b) RIL offtake could still average at ~6 mmscmd in the worst case (on start-up of petcoke gasifiers); and c) improved gas supply options from upcoming LNG terminals at Mundra and Pipavav. We raise TP to Rs350 on roll over to Mar'21, and higher value for GUJGA investment.**

Rohit Ahuja | Harleen Manglani

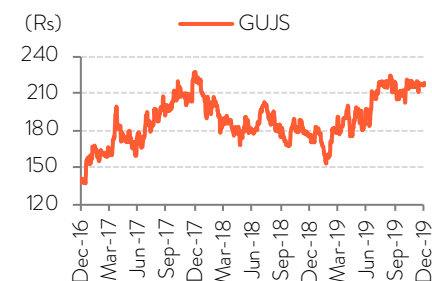
research@bobcaps.in

**Improving volume outlook:** As per GUJS management, concerns on decline in RIL's offtake seems unrealistic as it would still continue to offtake at least 6 mmscmd of gas (if all the petcoke gasifiers operate at full capacity). However, GSPL recently lost some volumes (~2 mmscmd) to GAIL as the latter's tariffs on HVJ pipeline were set lower. Management is strongly rooting for power demand to pick up for its volume growth story to play out in the long run, supported by expectations of lower spot LNG prices in CY20.

Ticker/Price	GUJS IN/Rs 219
Market cap	US\$ 1.7bn
Shares o/s	564mn
3M ADV	US\$ 1.8mn
52wk high/low	Rs 230/Rs 149
Promoter/FPI/DII	38%/16%/47%

Source: NSE

**More LNG supply options are needed for supporting power demand:** Gas demand from power sectors is usually sporadic, and requires continuous availability of spare LNG capacity. Start-up of LNG terminals at Mundra (from Feb'2020) and Pipavav (from FY22), coupled with incremental domestic gas production from ONGC/RIL, would aid power sector consumption by 15-20 mmscmd (subject to spot LNG prices remaining <US\$5/mmbtu).

**STOCK PERFORMANCE**

Source: NSE

**GST for natural gas – neutral for gas demand in Gujarat:** As industrial customers in Gujarat pay 6% VAT, impact on demand from inclusion of natural gas in GST would more or less be neutral for the state. However, it would make a huge difference for LNG volumes (imported at Dahej and Hazira) being sold outside Gujarat, as it currently attracts ~30% indirect tax.

**KEY FINANCIALS**

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	13,317	18,773	22,760	22,779	26,241
EBITDA (Rs mn)	11,478	15,426	17,073	16,770	19,090
Adj. net profit (Rs mn)	6,684	7,947	10,395	10,165	11,912
Adj. EPS (Rs)	11.9	14.1	18.4	18.0	21.1
Adj. EPS growth (%)	34.5	18.9	30.8	(2.2)	17.2
Adj. ROAE (%)	14.2	15.2	17.3	14.8	15.5
Adj. P/E (x)	18.4	15.5	11.9	12.1	10.4
EV/EBITDA (x)	10.9	8.9	8.8	8.6	7.4

Source: Company, BOBCAPS Research

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## Valuation methodology

GUJS has healthy volumes levers in place – (a) planned connectivity to all the five LNG regasification terminals in Gujarat, and (b) an improving demand outlook from CGD and power. At 10x FY22E EPS, valuations look attractive considering improving volume visibility. We raise TP to Rs350 on roll over to Mar'21, and higher value for GUJGA investment.

Key assumptions for our DCF-based fair value are as under:

- cost of equity of 9.9% (from 9.74%),
- terminal growth of 6%, and
- long-term tariffs at ~Rs 1.55/scm

### FIG 1 – VALUATION SUMMARY

Valuation type	Value (Rs mn)
PV of FCFE	20,563
PV of terminal value	1,26,077
Less: Net debt*	(14,645)
Investment values	35,751
Equity value	197,037
<b>Equity value (Rs/share)</b>	<b>350</b>

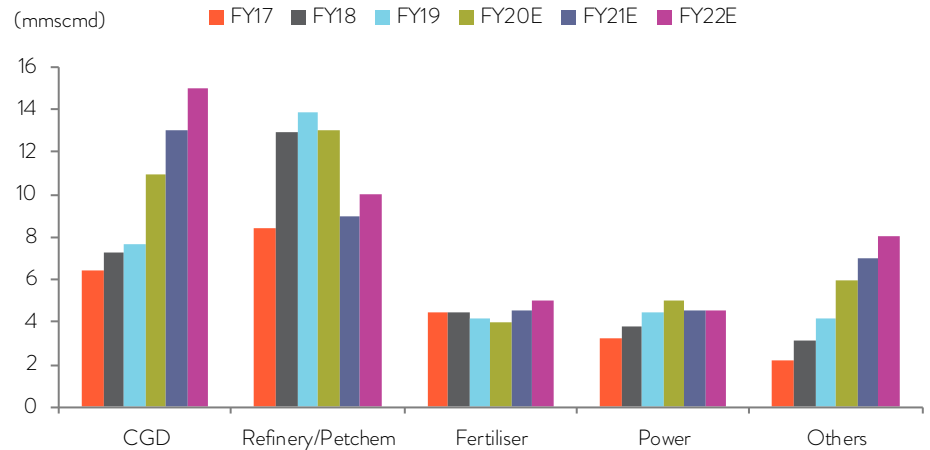
Source: BOBCAPS Research | \*Adjusted for acquisition value of equity in Gujarat Gas

### FIG 2 – FAIR VALUE SENSITIVITY TO TERMINAL GROWTH & COST OF EQUITY

		Cost of Equity (%)				
		(Rs)	8.5	9.0	9.7	10.7
Terminal growth (%)	5.0	457	360	302	265	238
	5.5	527	395	323	278	247
	<b>6.0</b>	633	443	<b>350</b>	295	258
	6.5	814	510	384	315	271
	7.0	1,192	612	429	340	287

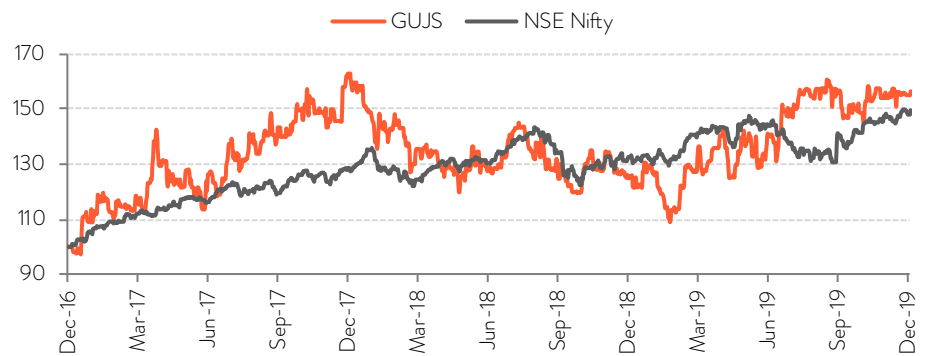
Source: BOBCAPS Research

**FIG 3 – VOLUME BREAK-UP**



Source: BOBCAPS Research, Company

**FIG 4 – RELATIVE STOCK PERFORMANCE**



Source: NSE

**Key risks**

- **Regulations:** GUJS’s pipeline tariffs are regulated by PNGRB. Any reduction in tariffs on account of a change in guidelines could severely hit earnings. There is a possibility of reduction in tariffs by ~8%, to factor in the adoption of lower tax rate (25% rate) adopted by GUJS. However, this may take longer to fructify as GAIL has not yet opted for the new tax regime.
- **Below-expected volume growth:** It can take longer than expected for GUJS to make up for the loss of 4-6mmscmd of volumes from RIL (post commissioning of the latter’s petcoke gasification plant), which could affect near-term earnings.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Total revenue</b>	<b>13,317</b>	<b>18,773</b>	<b>22,760</b>	<b>22,779</b>	<b>26,241</b>
EBITDA	11,478	15,426	17,073	16,770	19,090
Depreciation	(1,750)	(1,800)	(2,003)	(2,182)	(2,397)
EBIT	9,728	13,626	15,070	14,588	16,693
Net interest income/(expenses)	(354)	(2,192)	(1,929)	(1,682)	(1,467)
Other income/(expenses)	735	594	673	684	700
EBT	10,108	12,028	13,814	13,590	15,925
Income taxes	(3,424)	(4,081)	(2,072)	(3,425)	(4,013)
<b>Reported net profit</b>	<b>6,684</b>	<b>7,947</b>	<b>10,395</b>	<b>10,165</b>	<b>11,912</b>
<b>Adjusted net profit</b>	<b>6,684</b>	<b>7,947</b>	<b>10,395</b>	<b>10,165</b>	<b>11,912</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Accounts payables	185	238	317	317	365
Other current liabilities	1,455	533	533	533	533
Provisions	138	216	216	216	216
Debt funds	32,189	25,846	22,372	19,674	17,013
Other liabilities	5,133	5,492	5,793	6,090	6,437
Equity capital	5,638	5,638	5,638	5,638	5,638
Reserves & surplus	43,723	49,762	59,049	66,828	75,943
Shareholders' fund	49,362	55,401	64,687	72,466	81,582
<b>Total liabilities and equities</b>	<b>88,462</b>	<b>87,726</b>	<b>93,919</b>	<b>99,296</b>	<b>106,146</b>
Cash and cash eq.	3,645	1,583	3,278	3,859	5,396
Accounts receivables	1,235	2,081	2,104	2,106	2,426
Inventories	1,235	1,279	2,104	2,105	2,425
Other current assets	143	172	278	278	278
Investments	42,054	42,772	42,036	42,036	42,036
Net fixed assets	31,142	35,524	38,257	42,521	47,156
CWIP	8,959	4,194	5,861	6,390	6,428
<b>Total assets</b>	<b>88,413</b>	<b>87,605</b>	<b>93,919</b>	<b>99,296</b>	<b>106,146</b>

Source: Company, BOBCAPS Research

**Cash Flows**

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Net income + Depreciation	8,434	9,746	12,398	12,347	14,309
Changes in working capital	1,100	(1,599)	(769)	(3)	(592)
Other operating cash flows	(469)	(352)	(371)	(388)	(353)
<b>Cash flow from operations</b>	<b>9,064</b>	<b>7,796</b>	<b>11,257</b>	<b>11,956</b>	<b>13,365</b>
Capital expenditures	(3,330)	(1,417)	(6,403)	(6,974)	(7,071)
Change in investments	(34,399)	(718)	735	0	0
Other investing cash flows	703	522	673	684	700
<b>Cash flow from investing</b>	<b>(37,026)</b>	<b>(1,613)</b>	<b>(4,995)</b>	<b>(6,290)</b>	<b>(6,371)</b>
Equities issued/Others	2	0	0	0	0
Debt raised/repaid	25,883	(6,343)	(3,474)	(2,698)	(2,661)
Dividends paid	(1,128)	(1,319)	(2,440)	(2,386)	(2,797)
Other financing cash flows	(1,177)	0	0	0	0
<b>Cash flow from financing</b>	<b>23,581</b>	<b>(7,662)</b>	<b>(5,914)</b>	<b>(5,085)</b>	<b>(5,458)</b>
<b>Changes in cash and cash eq.</b>	<b>(4,381)</b>	<b>(1,480)</b>	<b>348</b>	<b>581</b>	<b>1,536</b>
<b>Closing cash and cash eq.</b>	<b>3,646</b>	<b>2,166</b>	<b>1,931</b>	<b>3,859</b>	<b>5,396</b>

**Per Share**

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20E	FY21E	FY22E
Reported EPS	11.9	14.1	18.4	18.0	21.1
Adjusted EPS	11.9	14.1	18.4	18.0	21.1
Dividend per share	1.8	2.0	3.7	3.6	4.2
Book value per share	87.5	98.3	114.7	128.5	144.7

**Valuations Ratios**

Y/E 31 Mar (x)	FY18A	FY19A	FY20E	FY21E	FY22E
EV/Sales	9.4	7.3	6.6	6.4	5.4
EV/EBITDA	10.9	8.9	8.8	8.6	7.4
Adjusted P/E	18.4	15.5	11.9	12.1	10.4
P/BV	2.5	2.2	1.9	1.7	1.5

**DuPont Analysis**

Y/E 31 Mar (%)	FY18A	FY19A	FY20E	FY21E	FY22E
Tax burden (Net profit/PBT)	66.1	66.1	75.2	74.8	74.8
Interest burden (PBT/EBIT)	103.9	88.3	91.7	93.2	95.4
EBIT margin (EBIT/Revenue)	73.0	72.6	66.2	64.0	63.6
Asset turnover (Revenue/Avg TA)	18.2	21.3	25.1	23.6	25.5
Leverage (Avg TA/Avg Equity)	1.6	1.7	1.5	1.4	1.3
Adjusted ROAE	14.2	15.2	17.3	14.8	15.5

Source: Company, BOBCAPS Research | Note: TA = Total Assets

**Ratio Analysis**

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
<b>YoY growth (%)</b>					
Revenue	29.6	41.0	21.2	0.1	15.2
EBITDA	29.2	34.4	10.7	(1.8)	13.8
Adjusted EPS	34.5	18.9	30.8	(2.2)	17.2
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	86.2	82.2	75.0	73.6	72.7
EBIT margin	73.0	72.6	66.2	64.0	63.6
Adjusted profit margin	50.2	42.3	45.7	44.6	45.4
Adjusted ROAE	14.2	15.2	17.3	14.8	15.5
ROCE	9.7	11.1	15.2	12.2	13.1
<b>Working capital days (days)</b>					
Receivables	34	32	34	34	32
Inventory	306	170	124	146	130
Payables	32	23	18	19	17
<b>Ratios (x)</b>					
Gross asset turnover	0.2	0.3	0.4	0.3	0.4
Current ratio	0.4	0.4	7.3	7.8	9.4
Net interest coverage ratio	27.5	6.2	7.8	8.7	11.4
Adjusted debt/equity	0.6	0.4	0.3	0.2	0.1

Source: Company, BOBCAPS Research

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### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

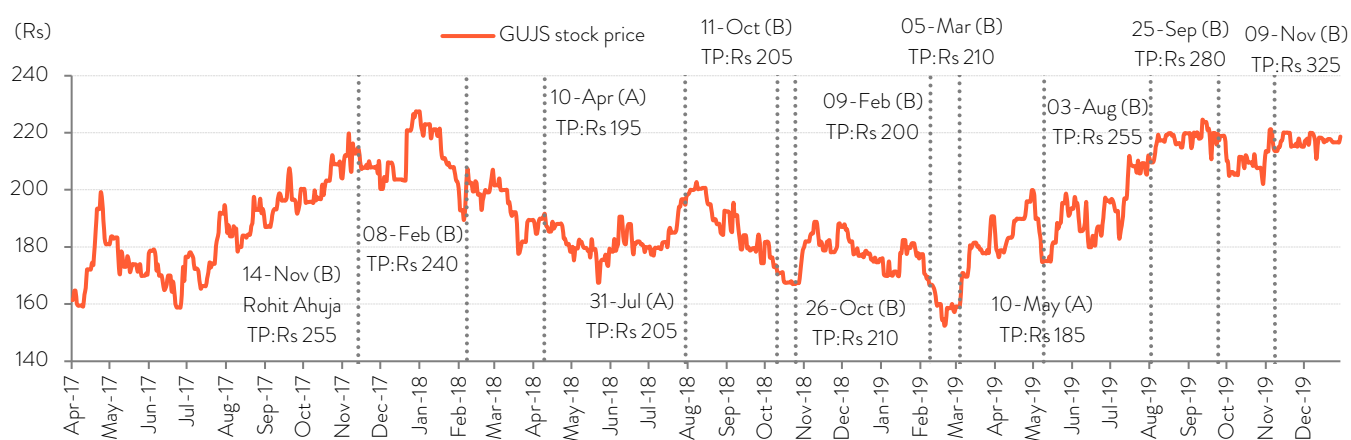
**ADD** – Expected return from >+5% to +15%

**REDUCE** – Expected return from -5% to +5%

**SELL** – Expected return <-5%

**Note:** Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

### HISTORICAL RATINGS AND TARGET PRICE: GUJARAT STATE PETRONET (GUJS IN)



B – Buy, A – Add, R – Reduce, S – Sell

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