

India

Overweight (no change)

Highlighted Companies

GAIL India

ADD, TP Rs180, Rs145 close

We value GAIL at Rs180, 1.3x Mar 23F P/BV, 13.7% ROE in FY23F. We see potential for positive earnings surprise as global oil/gas prices have been trending above our estimates.

Petronet LNG

HOLD, TP Rs240, Rs227 close

We value PLNG at Rs240, 2.4x Mar 23F P/BV, 22.4% ROE in FY23F. Medium-term growth prospects are limited due to a sharp increase in domestic gas production and rise in regas terminal capacity.

Summary Valuation Metrics

P/E (x)	Mar21-F	Mar22-F	Mar23-F
GAIL India	10.65	7.29	8.09
Petronet LNG	11.59	11.68	10.81
P/BV (x)	Mar21-F	Mar22-F	Mar23-F
GAIL India	1.26	1.14	1.07
Petronet LNG	2.89	2.56	2.29
Dividend Yield	Mar21-F	Mar22-F	Mar23-F
GAIL India	3.45%	5.17%	4.48%
Petronet LNG	6.6%	4.18%	4.67%

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Gas Transmission & Dist

Red hot gas markets offer opportunity

- Global gas prices have been breaking new records and should offer opportunities for GAIL to make some exceptional trading gains.
- LNG imports will remain muted in near to medium term due to high spot prices and rising domestic gas production (absorbed by refining, petchem and steel).
- Reiterate Add on GAIL (TP Rs180) and Hold on Petronet LNG (TP Rs240).

Global gas prices have been rocketing

Gas prices across the globe have been rising sharply (a complete contrast to the lows seen just 12 months ago) on the back of supply constraints mainly in Europe due to lower Gazprom supplies. An increase in demand has not been met by additional Gazprom supply (given its reluctance to transit more gas via Ukraine) and all hopes now rest with the start of the new Nord Stream 2 gas pipeline. Asian spot prices climbed over US\$18/mmbtu recently with oil slopes averaging 16-20% in recent months. This compares to long-term (Ras Gas) price of US\$9.6/mmbtu and Henry Hub at US\$4/mmbtu. Even the futures curve for most markets indicates that while prices will moderate from current highs, they will remain elevated in the medium term (relative to historical levels). We believe this offers GAIL an opportunity to make some exceptional trading gains on its US LNG volumes (of which more than 50% are sold outside India currently).

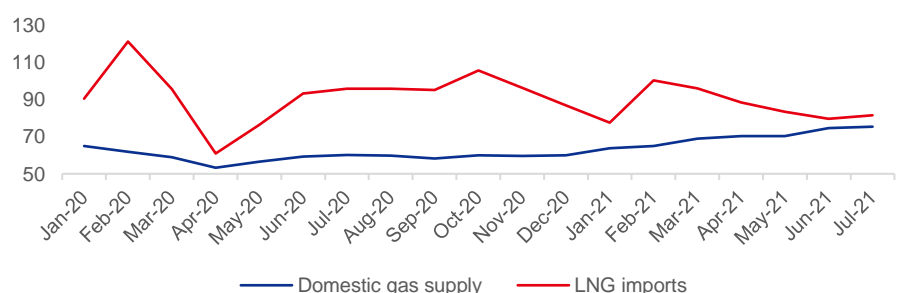
Rising domestic gas production a headwind for India LNG imports

Indian LNG imports have moderated in recent months. While the recent sharp rise in spot LNG prices will curb demand, the main headwind (which will last at least for 1-2 years) will be rising domestic gas production. Reliance Industries' KG-D6 block started production from Dec 2020 and is now producing around 18mmscmd. Government data places this entire production in "others" category, but our analysis indicates that most of this gas is consumed by sectors like refining, petchem and steel (potentially large buyers of LNG) rather than traditional sectors like fertilizer, power or city gas. Six new fertilizer plants will start operations in the next 12 months (additional demand of 10-12mmscm) and GAIL has already contracted to supply them LNG from its US contract volumes.

We retain Add on GAIL and Hold on PLNG

Global oil and gas prices rallied sharply in the last 12 months. While they could possibly moderate from current levels, the sharply lower levels seen in FY21 now seem unlikely to repeat, in our opinion. So we believe that GAIL's profitability from its US LNG contracts could offer significant upside in the near term and will likely remain elevated in the medium term, which is yet to be reflected in its stock price, in our view. A sharp drop in global oil/gas prices is the main risk. Our Hold rating on PLNG reflects lack of growth on LNG imports due to high spot gas prices (short term) and rising domestic gas production (medium term). Upside could come from any drop in domestic gas production while recent disputes on tariff and take-or-pay dues working against PLNG would be the main risks.

Figure 1: India monthly domestic gas supply and LNG imports (mmscmd)

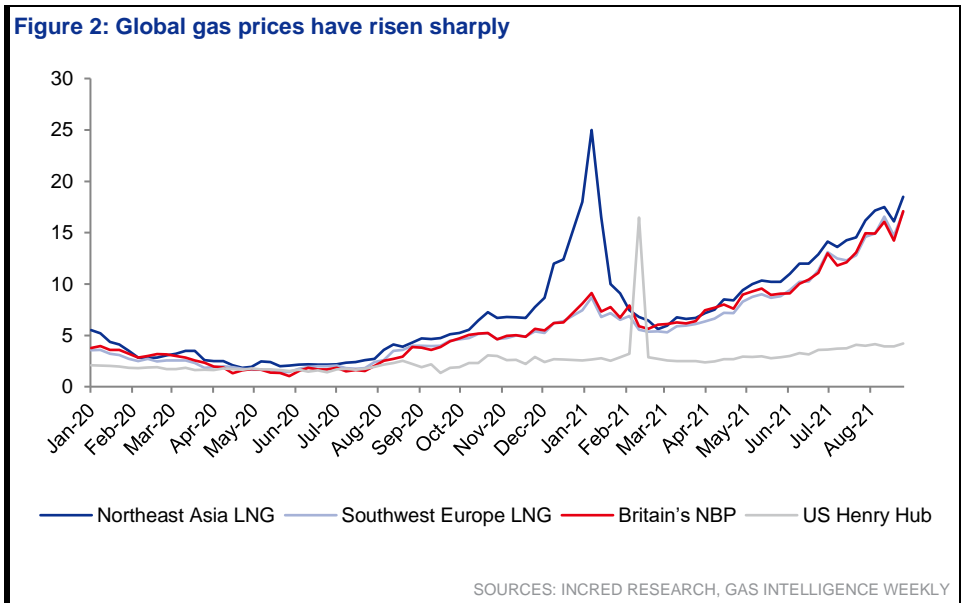


SOURCES: INCRED RESEARCH, PETROLEUM PLANNING & ANALYSIS CELL

Red hot gas markets offer opportunity

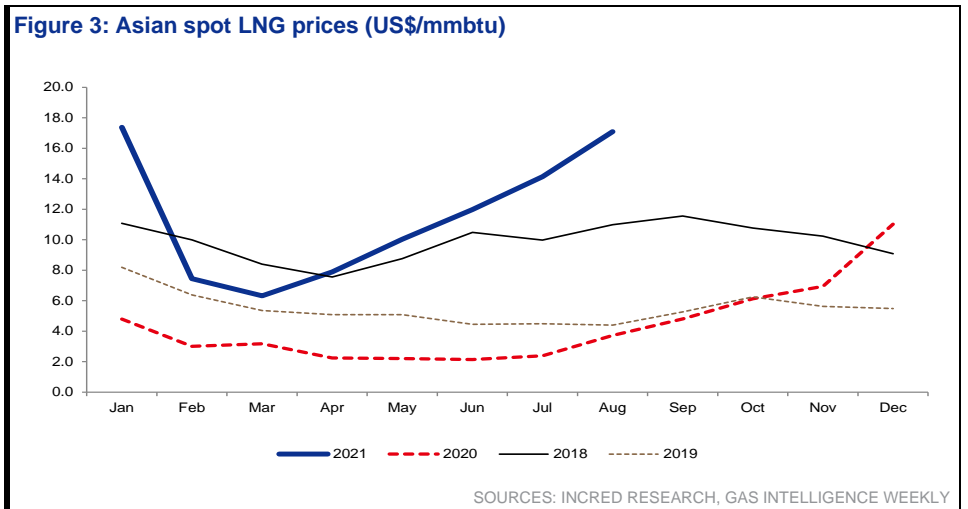
Global gas prices have all moved up in tandem, with even US Henry Hub prices touching new highs (relative to recent history). In our view, most of the tightness in the global gas market can be traced to Europe where Gazprom supplies have not matched demand, thereby pulling LNG cargoes across the world and resulting in rising prices across all markets. The futures market is indicating price moderation going ahead but prices are now unlikely to drop to the low levels seen in CY20.

Figure 2: Global gas prices have risen sharply



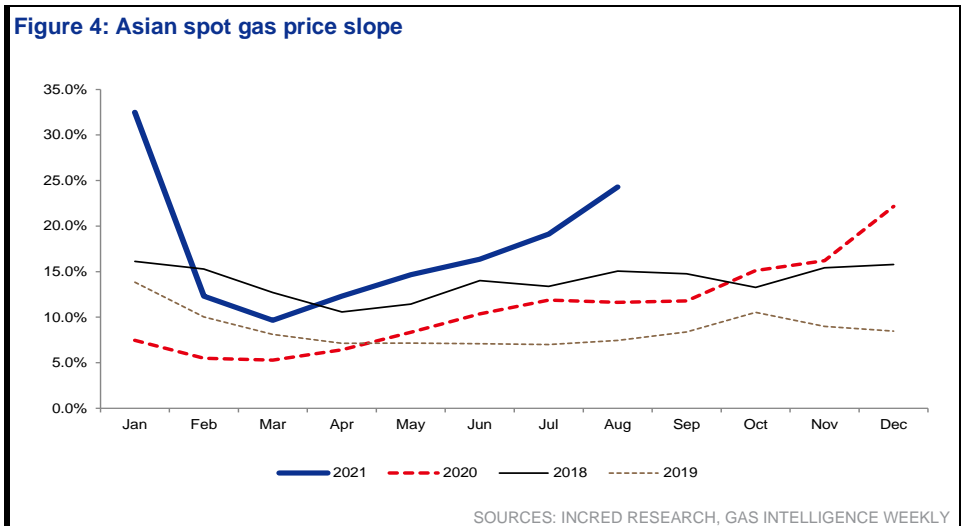
The monthly average Asian spot price averaged US\$17/mmbtu in Aug 2020 which was a seasonal high (normally these levels of prices are reached in the winter months due to seasonally high demand). This rise in price has been driven by higher oil price (which influence pricing of long-term gas contracts) as well as sharp rise in gas prices in other markets (US/Europe).

Figure 3: Asian spot LNG prices (US\$/mmbtu)

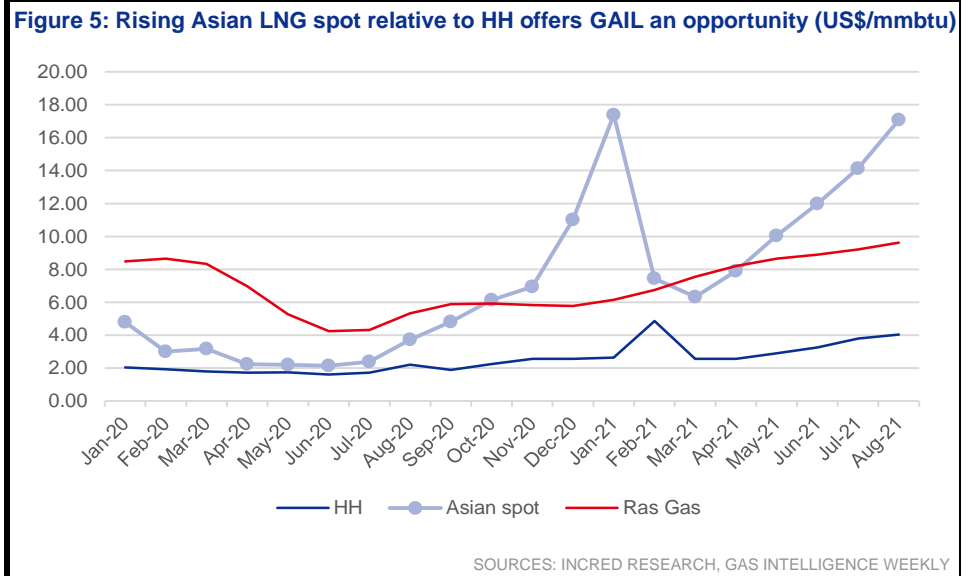


Gas price as a percentage of the oil price (termed as gas price slope) provides a better measure of gas price competitiveness vis-à-vis long-term gas which is priced at 10-14% slope. The high slope of 16-20% in recent months is reflected in the spot price at US\$17/mmbtu vs long-term (Ras Gas) price of US\$9.6/mmbtu.

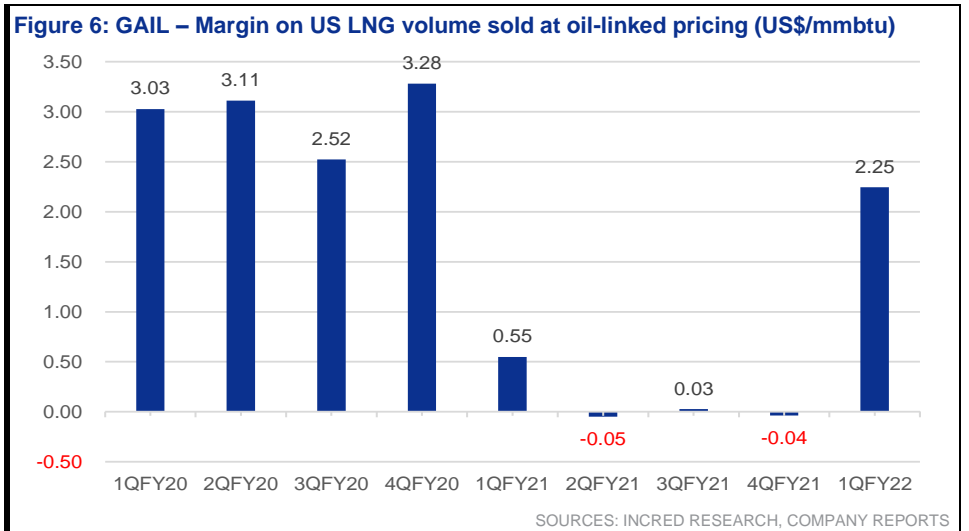
Figure 4: Asian spot gas price slope



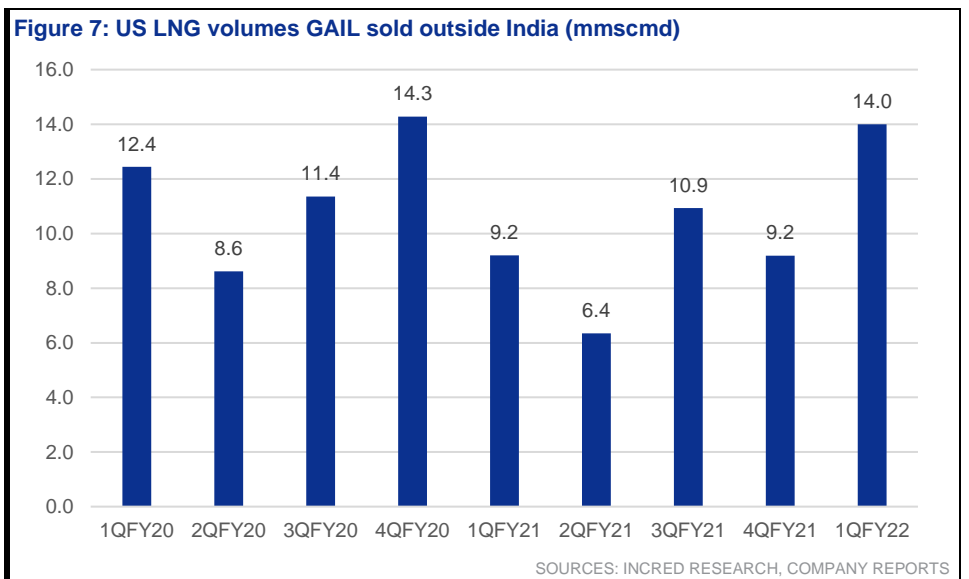
GAIL has annual contracts to buy 5.8mt of LNG from the US at 115% of the Henry Hub price plus fixed liquefaction fee of US\$3/mmbtu. This volume can then be sold to Indian customers at oil-linked (Ras Gas) pricing. Volumes that cannot be sold within India can be sold in other global markets with Asian spot prices providing a proxy of possible price that could be realized.



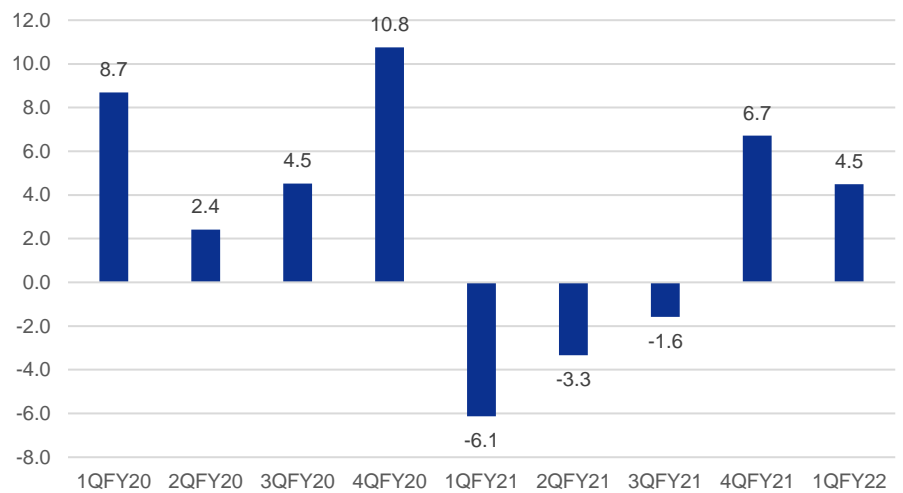
The Ras Gas price is based on 12.87% of the average Brent price over the preceding three months. Hence the impact of higher oil prices is reflected in Ras Gas price with a lag. In FY21, the collapse of the oil price wiped out any margin on the sale of US LNG in India at Ras Gas prices. With the recovery of the oil price, this margin recovered sharply in 1QFY22. With oil prices remaining high, this margin has been maintained despite the sharp rally in the Henry Hub gas price.



GAIL has broadly been selling around 10mmscmd of gas outside India out of its total US contract volume of 5.8mt (22mmscmd). GAIL hopes to ultimately sell this volume in India as new demand from fertilizer and other sectors materialize. The current level of high volumes sold outside India offers potential for GAIL to optimize its marketing operations to benefit from the elevated levels of spot gas pricing prevalent across the globe, especially in Asia.

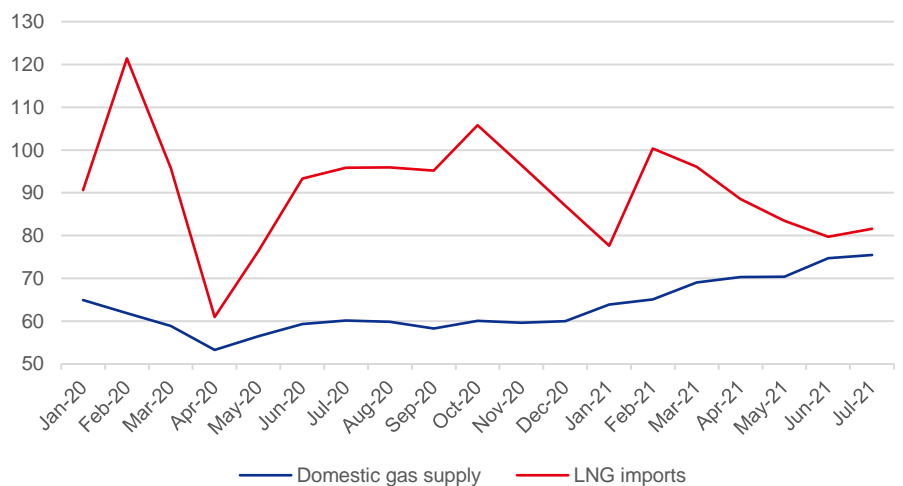


GAIL trading profits turned into losses in the first three quarters of FY21 as margins on US LNG contract crashed. This recovered in the last two quarters. Note that regas income from Konkan Gas is included in trading profits and this income comes only in 1Q and 4Q (the regas terminal is shut during the monsoon months). Given current market conditions, we believe it highly likely that GAIL could report record profits on trading in subsequent quarters.

Figure 8: GAIL consolidated trading profits (Rs bn)


SOURCES: INCRED RESEARCH, COMPANY REPORTS

RIL commenced gas production from its KGD6 block in Dec 2020 and is currently operating at 18mmscmd. Domestic gas supply has accordingly increased which would have caused moderation in LNG imports. The sharp spurt in global gas prices would also be a major headwind for LNG imports.

Figure 9: India monthly domestic gas supply and LNG imports (mmscmd)


SOURCES: PETROLEUM PLANNING & ANALYSIS CELL, INCRED RESEARCH

Historically, fertilizer and power were the largest gas consumers in India. Their dominance has reduced as fertilizer production has been stagnant while gas-based power has become uneconomic.

Figure 10: India annual gas consumption (mmscmd)

Y/E 31 Mar	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Fertiliser	38.4	40.4	43.5	41.6	44.2	42.3	40.2	41.1	44.2	48.5
Power	62.0	44.0	30.9	29.4	29.8	31.8	33.0	32.9	30.2	29.7
City gas	15.3	15.8	16.0	14.8	15.0	20.1	23.5	25.2	29.8	24.8
Refineries	11.7	10.7	10.9	12.5	13.9	14.7	17.9	19.3	21.3	21.7
Petrochemicals	5.1	6.8	6.6	7.9	10.2	11.4	11.0	9.3	9.8	8.5
Others	33.8	30.0	26.4	22.4	18.0	18.7	19.1	19.8	19.3	20.3
Total	166.3	147.7	134.2	128.6	131.1	139.1	144.7	147.5	154.6	153.6

SOURCES: PETROLEUM PLANNING & ANALYSIS CELL, INCRED RESEARCH

Petroleum Planning & Analysis Cell, a government agency, provides monthly data on segment-wise consumption. We believe that RIL's additional production of 18mmscmd has been classified as others, whereas actual segment can be inferred based on knowing the identity of the buyer (see Figure 12)

Figure 11: India gas consumption in 1QFY22 (mmscmd)

	Domestic gas	LNG	Total
Fertiliser	17.6	30.1	47.6
Power	18.7	9.1	27.8
City gas	15.1	13.1	28.2
Refineries	2.4	15.3	17.7
Petrochemicals	0.8	6.3	7.1
Others	22.4	9.9	32.3
Total	76.9	83.7	160.7

SOURCES: PETROLEUM PLANNING & ANALYSIS CELL, INCRED RESEARCH

RIL has sold its total gas production of 18mmscmd through 3 bidding rounds. RIL, through its O2C subsidiary and JV with BP (IGS), has itself got 52% of total volumes. But most of the volumes have gone to sectors like refining, petchem and steel rather than the historically large consumers like fertilizer or power.

Figure 12: Customers for RIL KG-D6 gas (mmscmd)

	Bid 1	Bid 2	Bid 3	Total	%
RIL O2C		4.80	3.20	8.00	44%
IGS (RIL/BP)		0.35	1.00	1.35	8%
Essar Steel	2.25			2.25	13%
GSPC	1.20			1.20	7%
Indian Oil			1.00	1.00	6%
GAIL	0.30	0.85	0.03	1.18	7%
Shell Energy		0.68		0.68	4%
HPCL	0.35	0.23		0.58	3%
Adani Gas	0.30	0.09	0.15	0.54	3%
Rest (< 0.5mmscmd each)	0.60	0.50	0.12	1.22	7%
Total	5.00	7.50	5.50	18.00	100%

SOURCES: PETROLEUM PLANNING & ANALYSIS CELL, INCRED RESEARCH

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Score Range:	90 - 100	80 – 89	70 - 79	Below 70	No Survey Result
Description:	Excellent	Very Good	Good	N/A	N/A

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Corporate Governance Report of Thai Listed Companies (CGR). CG Rating by the Thai Institute of Directors Association (Thai IOD) in 2020, Anti-Corruption 2020

ADVANC – Excellent, Certified, **AMATA** – Excellent, Certified, **ANAN** – Excellent, n/a, **AOT** – Excellent, n/a, **AP** – Excellent, Certified, **ASP** – Excellent, n/a, **AU** – Good, n/a, **BAM** – Very Good, Certified, **BAY** – Excellent, Certified, **BBL** – Very Good, Certified, **BCH** – Good, Certified, **BCP** – Excellent, Certified, **BCPG** – Excellent, Certified, **BDMS** – Excellent, n/a, **BEAUTY** – Good, n/a, **BH** – Good, n/a, **BJC** – Very Good, n/a, **BLA** – Excellent, Certified, **BTS** – Excellent, Certified, **CBG** – Very Good, n/a, **CCET** – n/a, n/a, **CENTEL** – Excellent, Certified, **CHAYO** – Very Good, n/a, **CHG** – Very Good, n/a, **CK** – Excellent, n/a, **COM7** – Very Good, Certified, **CPALL** – Excellent, Certified, **CPF** – Excellent, Certified, **CPN** – Excellent, Certified, **CPNREIT** – n/a, n/a, **CRC** – Very Good, n/a, **DELTA** – Excellent, Certified, **DDD** – Very Good, n/a, **DIF** – n/a, n/a, **DOHOME** – Very Good, n/a, **DREIT** – n/a, n/a, **DTAC** – Excellent, Certified, **ECL** – Excellent, Certified, **EGCO** – Excellent, Certified, **EPG** – Excellent, Certified, **ERW** – Very Good, Certified, **GFPT** – Excellent, Certified, **GGC** – Excellent, Certified, **GLOBAL** – Very Good, n/a, **HANA** – Excellent, Certified, **HMPRO** – Excellent, Certified, **HUMAN** – Good, n/a, **ICHI** – Excellent, Certified, **III** – Excellent, n/a, **INTUCH** – Excellent, Certified, **IRPC** – Excellent, Certified, **ITD** – Very Good, n/a, **IVL** – Excellent, Certified, **JASIF** – n/a, n/a, **JKN** – Excellent, Declared, **JMT** – Very Good, Declared, **KBANK** – Excellent, Certified, **KCE** – Excellent, Certified, **KEX** – n/a, n/a, **KKP** – Excellent, Certified, **KSL** – Excellent, Certified, **KTB** – Excellent, Certified, **KTC** – Excellent, Certified, **LH** – Excellent, n/a, **LPN** – Excellent, Certified, **M** – Very Good, Certified, **MAKRO** – Excellent, Certified, **MC** – Excellent, Certified, **MEGA** – Very Good, n/a, **MINT** – Excellent, Certified, **MTC** – Excellent, Certified, **NETBAY** – Very Good, n/a, **NRF** – n/a, n/a, **OR** – n/a, n/a, **ORI** – Excellent, Certified, **OSP** – Very Good, n/a, **PLANB** – Excellent, Certified, **PRINC** – Very Good, Certified, **PR9** – Excellent, n/a, **PSH** – Excellent, Certified, **PTT** – Excellent, Certified, **PTTEP** – Excellent, Certified, **PTTGC** – Excellent, Certified, **QH** – Excellent, Certified, **RBF** – Good, n/a, **RS** – Excellent, n/a, **RSP** – Good, n/a, **S** – Excellent, n/a, **SAK** – n/a, n/a, **SAPPE** – Very Good, Certified, **SAWAD** – Very Good, n/a, **SCB** – Excellent, Certified, **SCC** – Excellent, Certified, **SCGP** – n/a, n/a, **SHR** – Very Good, n/a, **SIRI** – Excellent, Certified, **SPA** – Very Good, n/a, **SPALI** – Excellent, Declared, **SPRC** – Excellent, Certified, **SSP** – Good, Declared, **STEC** – n/a, n/a, **SVI** – Excellent, Certified, **SYNEX** – Very Good, n/a, **TCAP** – Excellent, Certified, **THANI** – Excellent, Certified, **TIDLOR** – n/a, n/a, **TISCO** – Excellent, Certified, **TKN** – Very Good, n/a, **TMB** – Excellent, Certified, **TOP** – Excellent, Certified, **TRUE** – Excellent, Certified, **TU** – Excellent, Certified, **TVO** – Excellent, Certified, **VGI** – Excellent, Certified, **WHA** – Excellent, Certified, **WHART** – n/a, n/a, **WICE** – Excellent, Certified, **WORK** – Good, n/a.

- CG Score 2020 from Thai Institute of Directors Association (IOD)

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Stock Ratings

Definition:

Add	The stock's total return is expected to exceed 10% over the next 12 months.
Hold	The stock's total return is expected to be between 0% and positive 10% over the next 12 months.
Reduce	The stock's total return is expected to fall below 0% or more over the next 12 months.

The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

Sector Ratings

Definition:

Overweight	An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
Neutral	A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
Underweight	An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

Country Ratings

Definition:

Overweight	An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
Neutral	A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
Underweight	An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.