Morning Insight

MARCH 11, 2019

		% Chg		
	8-Mar	1 Day	1 Mth	3 Mths
Indian Indices				
SENSEX Index	36,671	(0.1)	0.3	2.8
NIFTY Index	11,035	(0.2)	0.8	3.2
NSEBANK Index	27,762	(0.0)	1.7	4.4
NIFTY 500 Index	9,211	(0.2)	1.9	3.0
CNXMcap Index	17,379	(0.2)	4.7	1.9
BSESMCAP Index	14,529	(0.1)	6.4	3.0
World Indices				
Dow Jones	25,450	(0.1)	1.6	4.4
Nasdaq	7,408	(0.2)	1.4	5.4
FTSE	7,104	(0.7)	(0.3)	4.4
NIKKEI	21,026	(2.0)	3.6	(0.4)
Hangseng	21,026	(2.0)	3.6	(0.4)
Shanghai	28,228	(1.9)	0.6	9.9

Value traded (Rs cr)	8-Mar	% Chg Day
Cash BSE	3,932	47.7
Cash NSE	29,136	(11.3)
Derivatives	539,931	(68.3)

Net inflows (Rs cr)	7-Mar	MTD	YTD
FII	1,074	4,757	21,139
Mutual Fund	(483)	(842)	8,492

Nifty Gainers & Losers	Price	Chg	Vol
8-Mar	(Rs)	(%)	(mn)
Gainers			
NTPC Ltd	152	4.1	28.9
Eicher Motor	21,871	1.6	0.2
Gail India Ltd	350	1.6	2.7
Losers			
Zee Entertainment	471	(2.8)	6.6
Tata Motors	189	(2.7)	22.5
Axis Bank	721	(1.6)	10.5

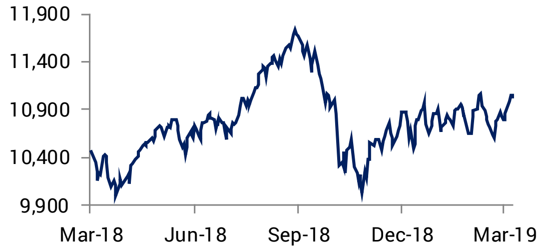
Advances / Declines (BSE)

8-Mar	A	B	T	Total	% total
Advances	191	391	74	656	100
Declines	268	585	36	889	136
Unchanged	2	23	11	36	5

Commodity		% Chg		
	8-Mar	1 Day	1 Mth	3 Mths
Crude (US$/BBL)	66.0	0.4	7.3	9.7
Gold (US$/OZ)	1,298.4	1.0	(0.9)	4.3
Silver (US$/OZ)	15.3	2.1	(2.6)	5.1

Debt / forex market	8-Mar	1 Day	1 Mth	3 Mths
10 yr G-Sec yield %	7.4	7.4	7.3	7.5
Re/US$	70.2	70.0	71.3	71.3

Nifty



Source: Bloomberg

News Highlights

- The Centre has marginally lowered the maximum sale price of Bt cotton seeds (BG-II) for a 450-gram packet to Rs 730 for the 2019-20 season. The licence, or trait fee, charged by companies has also been slashed by almost 49 per cent to Rs 20. (BS)
- The Reserve Bank of India may disallow credit rating agencies from the dual role of being advisor-cum-rating agencies for companies. (ET)
- In a relief for the automobile sector, the government has clarified that no goods and services tax needs to be paid on tax collected at source (TCS) under the Income Tax Act. (ET)
- **Reliance Capital** has begun talks with global investors to sell its 42.88 per cent stake in Reliance Nippon Life Asset Management (RNAM), which manages the mutual fund (MF) business. The investors it is talking to include the Abu Dhabi Investment Authority (ADIA), Mubadala, Singapore-based Temasek, the Ontario Teachers' Pension Plan, and private equity funds Blackstone and The Carlyle Group. (BS)
- **IDBI Bank Ltd**, the lender with India's worst-bad loan ratio, is seeking to curtail its soured debt by selling Rs 100 billion ($1.4 billion) of stressed assets and stepping up efforts to recover dues from delinquent borrowers. (BS)
- Piramal Capital will seek to bring down single borrower exposure. Piramal Capital & Housing Finance, the finance arm of **Piramal Enterprises**, has been reducing exposure to real estate developers and increasing the share of housing finance in its books to de-risk its portfolio. (BS)
- **Apollo Health & Lifestyle (AHLL),** a subsidiary of Apollo Hospitals Enterprise (AHEL) and one of the largest players in the retail health care segment in India, is expected to reach break-even on earnings before interest, tax, depreciation and amortisation (Ebitda) next financial year. (BS)
- **Life Insurance Corp. of India and IDBI Bank Ltd**. set up a task force to implement synergies, about four months after India's biggest insurer agreed to put more than 200 billion rupees ($2.9 billion) into the troubled lender. Sales of insurance policies through bank branches are among immediate areas where gains can be made. (BQ)
- The Ahmedabad bench of the National Company Law Tribunal approved ArcelorMittal's bid to take over insolvent **Essar Steel Ltd.** ArcelorMittal will pay Rs 420bn against financial creditors' claims of more than Rs 490bn. That translates into a haircut of about 14 percent for the lenders. (BQ)
- **State Bank of India (SBI)** will use the Reserve Bank of India's (RBI's) policy repo rate as a benchmark to set the savings deposit rates and those for short-term loans from May 1 this year. (BS)
- **DLF** plans to raise an estimated Rs 30bn through the sale of equity shares to qualified institutional investors. (ET)
- **IDBI Bank** is considering current MD Rakesh Sharma, for appointment for a further period of three years as its MD and Chief Execuitve, besides broadbasing the board to induct professionals and two deputy MDs.(ET)

What's Inside

- **Initiating Coverage**: Gujarat Gas Ltd

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, IE = Indian Express, BL = Business Line, BQ = BloombergQuint, ToI: Times of India, BSE = Bombay Stock Exchange, MC = Moneycontrol

Initiating Coverage

Stock Details

Market cap (Rs mn)	:	93415
52-wk Hi/Lo (Rs)	:	183 / 115
Face Value (Rs)	:	2
3M Avg. daily vol (Nos)	:	422,073
Shares o/s (m)	:	688

Source: Bloomberg

Financial Summary

Y/E Mar (Rs mn)	FY19E	FY20E	FY21E
Revenue	79,398	87,811	99,386
Growth (%)	28.6	10.6	13.2
EBITDA	9,753	10,819	12,573
EBITDA margin (%)	12.3	12.3	12.7
PAT	3,976	4,390	5,404
EPS	5.8	6.4	7.9
EPS Growth (%)	36.5	10.4	23.1
BV (Rs/share)	32	37	44
Dividend/share (Rs)	0.8	0.9	1.1
ROE (%)	16.7	18.6	19.5
ROCE (%)	14.3	14.2	15.7
P/E (x)	23.4	21.2	17.2
EV/EBITDA (x)	11.5	10.0	8.3
P/BV (x)	4.3	3.7	3.1

Source: Company, Kotak Securities - PCG

Shareholding Pattern (%)

(%)	Dec-18	Jun-18	Mar-18
Promoters	60.9	60.9	60.9
FII	13.9	14.0	13.4
DII	3.4	3.4	3.3
Others	21.8	21.6	22.4

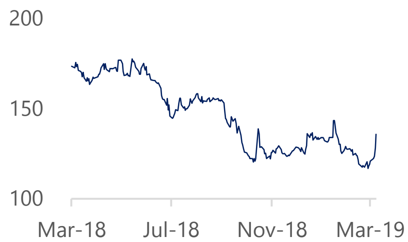
Source: Bloomberg, BSE

Price Performance (%)

(%)	1M	3M	6M
Gujarat Gas Ltd	9.3	5.8	(4.6)
Nifty	0.8	3.2	(4.8)

Source: Bloomberg

Price chart (Rs)



Source: Bloomberg

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GUJARAT GAS COMPANY LTD (GGCL)

PRICE RS.135 **TARGET RS.157** **BUY**

Gujarat Gas Company Limited (GGCL) is one of the largest gas distribution companies in India, with operations in Gujarat. We expect GGCL to report strong earnings growth in medium to long term led by strong volume growth which includes expansion in existing & new areas (Amritsar, Bathinda, and Ahmedabad), ramp up in retail gas consumption and rebound in industrial gas demand. Additionally, rebound in the industrial segment coupled with retail business expansion should help in margin improvement.

We estimate Revenue, EBITDA and EPS to grow at a CAGR of 17%, 12% and 23%, respectively over FY18-21E. We initiate coverage on GGCL with a BUY rating and a multiple based price target of Rs.157/share. Margin improvement and strong revenue visibility makes us positive on its growth prospects. Additionally, strong free cash flow and healthy return ratios also provide high comfort. We value GGCL at 20x PE based on EPS of Rs.7.9 for FY21E.

Key Investment Rationale

Strong earnings visibility:

- GGCL's earnings growth will be supported by strong gas sales volume growth and steady margin improvement in the medium to long term.
- Higher gas volumes will be led by 1). Expansion in new markets such as Dahej, Silvassa, Thane extension and Panchmahal, 2). Commencement of operations in newer areas, 3). Pick-up in industrial demand, 4). Retail expansion and 5). Regulatory support. This will support ~9.4% CAGR volume growth through FY18-FY21E, we opine.
- Some of the geographical areas have already started contributing, but majority of the volume growth would be back-ended in nature and any meaningful volume addition would require 2-3 years' time frame.
- Except incremental volume potential of 5-6 mmscmd during the next 4-5 years.

Strong volume growth outlook and pricing power will expand margins:

- A rebound in the industrial segment along with retail business expansion should help in per unit margin improvement. Conservatively, we expect EBITDA margin per unit to improve to Rs. 4.1/scm by FY2020E and Rs. 4.23/scm by FY2021E. Improvement in EBITDA/scm indicates pricing power and proactive pricing. GGCL is targeting to achieve an operating margin of Rs.4.5/scm.

Environmental issues - Regulatory support:

- Morbi-Wankaner cluster getting highly polluted due to usage of coal gasifiers. Recently, the National Green Tribunal has ordered a shutdown of all ceramic units at Morbi and Wankaner (India's largest ceramic cluster) that run on type B coal gasifier.
- We expect ceramic players to switch to natural gas as a fuel instead of closing down the unit or shifting to a new location.

- We would like to highlight, GGCL is the sole supplier of gas in that region. Currently, the ceramic manufacturing units at Morbi consume 2.5-2.6 mmscmd of gas (~50% of total units operate on gas). Earlier, Morbi units use to consume ~4 mmscmd, but this was reduced as companies switched to low-cost coal gasifiers.
- We expect Morbi to have a potential of 5-6 mmscmd gas demand as against current gas sales of ~2.5 mmscmd, suggesting the high growth prospects.

CNG/PNG versus alternative fuels- Competitive economics

- The economics of CNG is quite favorable as compared to alternative liquid fuels such as diesel and gasoline, primarily due to (1) allocation of cheaper domestic produced gas and (2) favorable taxation structure by central government as well as the state governments.
- CNG is 44% cheaper than Petrol and 34% cheaper than Diesel. The payback period for CNG kit is fairly attractive for vehicles across segments. The pay-back period for a Diesel run vehicle converting to CNG run vehicle by investing in conversion kit is 18 months and 11 months for a Petrol run vehicle converting to CNG run vehicle.

Low penetration in PNG-D and CNG offers strong growth opportunity:

- GGCL's long-term growth opportunity looks attractive with just ~18% penetration in the PNG-domestic and ~15% penetration in the CNG segment, coupled with possible regulatory push.
- A moderate uptick in GGCL's total gas volume on account of entry into new districts and favourable government policies for expansion of CGD services.

Healthy Financials:

- GGCL is likely to witness a meaningful improvement in its financial performance over FY19-21E driven by higher sales volume from both PNG and CNG segment.
- We estimated Revenue, EBIDTA and EPS to grow at a CAGR of 17%, 12% and 23%, respectively over FY18-21E.
- The company is expected to take sharp increases in realization to offset higher RLNG, domestic gas price increase and rupee depreciation, in our view.
- Higher CNG volume can quickly improve margins. With the addition of 46 CNG stations in FY18, the total number CNG dispensing stations stood at 294. CNG is a strong profitable segment given uninterrupted supply of cheap domestic gas as a result the management plans to add 60 CNG stations in FY19.
- The company has guided for annual capex run rate of Rs.5 bn (excluding acquisition) and the same will be funded internally. If any acquisition done then it may raise debt for the same.
- ROE is expected to improve with better capacity utilization, higher volumes, margin improvement, etc. In FY19E, we expect ROE of 16.7%, 18.6% for FY20E, and 19.5% for FY21E as against 16.7% for FY18.

Financials: Standalone

Profit and Loss Statement (Rs mn)

(Year-end March)	FY18	FY19E	FY20E	FY21E
Revenues	**61,743**	**79,398**	**87,811**	**99,386**
% change YoY	21.2	28.6	10.6	13.2
EBITDA	**9,029**	**9,753**	**10,819**	**12,573**
% change YoY	19.9	8.0	10.9	16.2
Other Income	279	914	300	300
Depreciation	2,718	2,880	2,996	3,506
EBIT	**6,589**	**7,787**	**8,123**	**9,367**
% change YoY	28.6	18.2	4.3	15.3
Net interest	1,961	1,921	1,571	1,265
Profit before tax	**4,628**	**5,866**	**6,552**	**8,102**
% change YoY	52.6	26.7	11.7	23.7
Tax	1,715	1,890	2,162	2,698
as % of PBT	37.0	32.2	33.0	33.3
Profit after tax	2,914	3,976	4,390	5,404
Net income	**2,914**	**3,976**	**4,390**	**5,404**
% change YoY	32.7	36.5	10.4	23.1
Shares outstanding (m)	688	688	688	688
EPS (reported) (Rs)	4.2	5.8	6.4	7.9
CEPS (Rs)	8.9	10.0	10.7	12.9
DPS (Rs)	0.8	0.8	0.9	1.1

Source: Company, Kotak Securities – Private Client Research

Balance sheet (Rs mn)

(Year-end March)	FY18	FY19E	FY20E	FY21E
Cash and cash equivalents	1,363	1,230	1,360	1,533
Accounts receivable	3,917	4,786	5,293	5,990
Inventories	568	640	741	844
Loans and Adv & Others	4,601	4,601	4,601	4,601
Current assets	10,449	11,257	11,995	12,969
Misc exp.	0	0	0	0
LT investments	174	174	174	174
Net fixed assets	55,710	58,410	60,400	62,390
Total assets	**66,333**	**69,841**	**72,569**	**75,533**
Payables	2,931	3,637	4,325	4,875
Others	11,957	13,528	14,962	16,934
Current liabilities	14,888	17,166	19,286	21,808
Provisions	383	406	444	496
LT debt	22,143	20,040	16,929	12,826
Others	10,455	10,455	10,455	10,455
Equity	1,377	1,377	1,377	1,377
Reserves	17,087	20,397	24,078	28,571
Total liabilities	**66,333**	**69,841**	**72,569**	**75,533**
BVPS (Rs)	27	32	37	44

Source: Company, Kotak Securities – Private Client Research

Cash Flow Statement (Rs mn)

(Year-end March)	FY18	FY19E	FY20E	FY21E
EBIT	6,589	7,787	8,123	9,367
Add: Depreciation	2,718	2,880	2,996	3,506
Change in working capital	(698)	(1,360)	(1,550)	(1,774)
Chgs in other net current assets	0	0	0	0
Operating cash flow	10,006	12,027	12,669	14,646
Less: Interest	(1,961)	(1,921)	(1,571)	(1,265)
Less: Tax	(1,715)	(1,890)	(2,162)	(2,698)
Cash flow from operations	**6,330**	**8,215**	**8,936**	**10,684**
Less: Capex	(4,354)	(5,580)	(4,986)	(5,496)
(Inc)/dec in investments	522	-	-	-
Cash flow from investments	**(3,833)**	**(5,580)**	**(4,986)**	**(5,496)**
Others	(234)	0	-	-
Increase/(decrease) in debt	(844)	(2,102)	(3,111)	(4,103)
Proceeds from share premium	-	-	-	-
Dividends	(664)	(666)	(709)	(911)
Cash flow from financing	**(1,743)**	**(2,768)**	**(3,821)**	**(5,015)**
Opening cash	608	1,363	1,230	1,360
Closing cash	1,363	1,230	1,360	1,533

Source: Company, Kotak Securities – Private Client Research

Ratio Analysis

(Year-end March)	FY18	FY19E	FY20E	FY21E
EBITDA margin (%)	14.6	12.3	12.3	12.7
EBIT margin (%)	10.7	9.8	9.3	9.4
Net profit margin (%)	4.7	5.0	5.0	5.4
Receivables (days)	23.2	22.0	22.0	22.0
Inventory (days)	3.4	2.9	3.1	3.1
Sales/gross assets(x)	1.5	1.9	2.1	2.3
Interest coverage (x)	3.2	3.6	5.0	7.2
Debt/equity ratio(x)	1.2	0.9	0.7	0.4
ROE (%)	16.7	16.7	18.6	19.5
ROCE (%)	12.2	14.3	14.2	15.7
EV/ Sales	1.8	1.4	1.2	1.0
EV/EBITDA	12.6	11.5	10.0	8.3
Price to earnings (P/E)	31.9	23.4	21.2	17.2
Price to book value (P/B)	5.0	4.3	3.7	3.1

Source: Company, Kotak Securities – Private Client Research

RATING SCALE

Definitions of ratings

BUY	–	We expect the stock to deliver more than 15% returns over the next 12 months
ADD	–	We expect the stock to deliver 5% - 15% returns over the next 12 months
REDUCE	–	We expect the stock to deliver -5% - +5% returns over the next 12 months
SELL	–	We expect the stock to deliver < -5% returns over the next 12 months
NR	–	**Not Rated.** Kotak Securities is not assigning any rating or price target to the stock. The report has been prepared for information purposes only.
SUBSCRIBE	–	We advise investor to subscribe to the IPO.
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NA	–	**Not Available or Not Applicable.** The information is not available for display or is not applicable
NM	–	**Not Meaningful.** The information is not meaningful and is therefore excluded.
NOTE	–	Our target prices are with a 12-month perspective. Returns stated in the rating scale are our internal benchmark.

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