

Pick of the week



GAIL INDIA LTD

Recommendation

Buy

Time Period

12 Months

Current Price

₹ 81

Target Price

₹ 150

Potential Upside

85.18%

Investment Argument

- Gail has indicated that it has already placed ~90% of the US LNG volumes for CY20 as well through adequately priced or hedged contracts. The company has managed the risk well over the past seven quarters post commencement of the US LNG supplies despite volatility in crude/spot LNG prices.
- KIE's bear-case scenario for the US LNG portfolio indicates that the gas marketing segment may break-even for a year or two, until fertilizer plants ramp up off-take.
- KIE's reverse valuation exercise suggests that GAIL is pricing in a scenario of significant gas marketing losses of over Rs20 bn in perpetuity, ignoring near-term nature of risk and GAIL's ability to manage it.
- KIE has ascribed lower EV/EBITDA multiple of 5-6x for GAIL's gas transmission & commodity segments and assumed 30% holding company discount to MTM value of investments to arrive at an implied negative value of Rs. 122 bn for gas marketing segment - at a reasonable 6x EV/EBITDA multiple, it builds in a large EBITDA loss of ~Rs. 20 bn in perpetuity.
- KIE has cut EPS estimates to Rs.11.5 (-6%) in FY20, Rs.9.8 (-29%) in FY21 and Rs.11.4 (-23%) in FY22. KIE finds the concerns overdone and reiterates BUY on GAIL with a FV of Rs. 150. We see GAIL as the top pick among energy PSUs given its structural growth prospects and play on oil price recovery.