

January 24, 2012

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Rating	Accumulate
Price	Rs337
Target Price	Rs392
Implied Upside	16.3%
Sensex	16,996
Nifty	5,127

(Prices as on January 24, 2012)

#### Trading data

Market Cap. (Rs bn)	47.2
Shares o/s (m)	140.0
3M Avg. Daily value (Rs m)	133.2

#### Major shareholders

Promoters	45.00%
Foreign	19.85%
Domestic Inst.	23.79%
Public & Other	11.36%

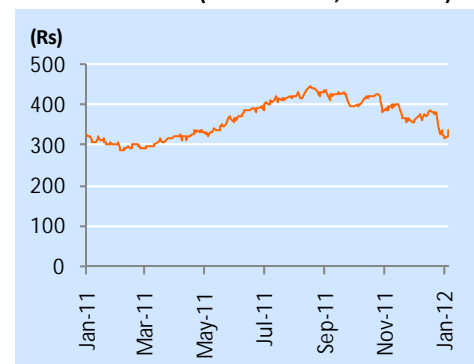
#### Stock Performance

(%)	1M	6M	12M
Absolute	(8.7)	(17.4)	3.6
Relative	(16.7)	(8.2)	14.9

#### How we differ from Consensus

EPS (Rs)	PL	Cons.	% Diff.
2013	23.0	25.4	-9.1
2014	25.0	28.1	-10.7

#### Price Performance (RIC: IGAS.BO, BB: IGL IN)



Source: Bloomberg

■ **Result Highlights:** Indraprastha Gas' (IGL's) Q3FY12 results were ahead of our expectation on the EBITDA front as well on the bottom-line front, largely on back of lower-than-anticipated LNG procurement cost. Top-line registered a growth of 45.1% YoY to Rs6,631m (Rs4,571m) as against our expectation of Rs6,769m. CNG volumes increased by 16.1% YoY to 179.8m/kg (154.8m/kg), in line with our expectation of 180.9m/kg. Growth in PNG volumes was in line with expectation at 78.0% YoY to 77.1mmscm (43.3mmscm). EBITDA during the quarter at Rs1,504m against an expectation of 1,456 was slightly higher on account of lower-than-anticipated gas cost. Bottom-line during the quarter stood at Rs692m (Rs672m), registering an increase of 2.9% YoY slightly ahead our expectation of Rs639m during the quarter.

■ **Outlook & Valuation:** IGL stock price has corrected by ~15.0% over the last one quarter, grossly underperforming the benchmark indices. Concerns were first levied on account of depreciating rupee and pass through capacity due to increasing gas prices. The concerns were further accentuated with potential the regulation of the marketing margins of the city gas distribution companies. , despite our belief that margins are unlikely to be regulated, the concern of potential regulation is likely to act as an overhang on the stock. To factor the same, we increase our discount rate from 12.0% to 12.75%, consequently leading to reduction in our target price to Rs399/share. The stock is currently available at 14.6x FY13E EPS of Rs23.0 and 3.3x P/BV. Our DCF based target price Rs392 provides an upside of 16.3% from the current levels. We recommend an **'Accumulate'** rating on the stock.

#### Key financials (Y/e March)

	2011	2012E	2013E	2014E
Revenues (Rs m)	17,441	31,149	43,121	52,927
Growth (%)	61.8	78.6	38.4	22.7
EBITDA (Rs m)	4,923	6,437	7,252	8,539
PAT (Rs m)	2,598	3,049	3,227	3,506
EPS (Rs)	18.6	21.8	23.0	25.0
Growth (%)	20.5	17.4	5.8	8.7
Net DPS (Rs)	5.0	6.0	6.3	7.5

#### Profitability & Valuation

	2011	2012E	2013E	2014E
EBITDA margin (%)	28.2	20.7	16.8	16.1
RoE (%)	28.4	27.5	24.4	22.7
RoCE (%)	22.9	19.1	15.8	14.8
EV / sales (x)	2.9	1.7	1.3	1.1
EV / EBITDA (x)	10.2	8.2	7.6	6.8
PE (x)	18.2	15.5	14.6	13.4
P / BV (x)	4.7	3.9	3.3	2.8
Net dividend yield (%)	1.5	1.8	1.9	2.2

Source: Company Data; PL Research

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**Exhibit 1: Q2FY12 Result Overview (Rs m)**

Y/e March	Q3FY12	Q3FY11	YoY gr. (%)	Q2FY12	9MFY12	9MFY11	YoY gr. (%)
<b>Operating income</b>	<b>6,631</b>	<b>4,571</b>	<b>45.1</b>	<b>5,975</b>	<b>17,980</b>	<b>12,397</b>	<b>45.0</b>
<b>Expenditure</b>							
Raw material	4,230	2,598	62.8	3,581	10,815	6,812	58.8
<i>% of net sales</i>	<i>63.8</i>	<i>56.8</i>		<i>59.9</i>	<i>60.1</i>	<i>54.9</i>	
Personnel cost	107	99	7.9	100	306	289	5.8
<i>% of net sales</i>	<i>1.6</i>	<i>2.2</i>		<i>1.7</i>	<i>1.7</i>	<i>2.3</i>	
Other operating expenses	791	581	36.0	715	2,192	1,681	30.4
<i>% of net sales</i>	<i>11.9</i>	<i>12.7</i>		<i>12.0</i>	<i>12.2</i>	<i>13.6</i>	
<b>EBITDA</b>	<b>1,504</b>	<b>1,293</b>	<b>16.4</b>	<b>1,579</b>	<b>4,667</b>	<b>3,615</b>	<b>29.1</b>
<i>Margin (%)</i>	<i>22.7</i>	<i>28.3</i>		<i>26.4</i>	<i>26.0</i>	<i>29.2</i>	
Depreciation	368	262	40.7	344	1,034	731	41.4
<b>EBIT</b>	<b>1,136</b>	<b>1,031</b>	<b>10.2</b>	<b>1,235</b>	<b>3,633</b>	<b>2,883</b>	<b>26.0</b>
Interest	135	41		118	343	61	
Other Income	15	7	120.6	15	43	23	88.1
<b>PBT</b>	<b>1,016</b>	<b>997</b>	<b>1.9</b>	<b>1,132</b>	<b>3,333</b>	<b>2,845</b>	<b>17.2</b>
Total taxes	324	325	(0.1)	360	1,069	939	13.8
<i>ETR (%)</i>	<i>31.9</i>	<i>32.6</i>		<i>31.8</i>	<i>32.1</i>	<i>33.0</i>	
<b>PAT</b>	<b>692</b>	<b>672</b>	<b>2.9</b>	<b>772</b>	<b>2,264</b>	<b>1,906</b>	<b>18.8</b>

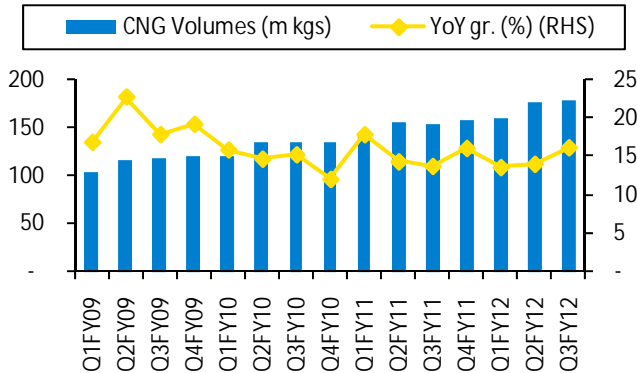
Source: Company Data, PL Research

**Exhibit 2: Segmental Breakup**

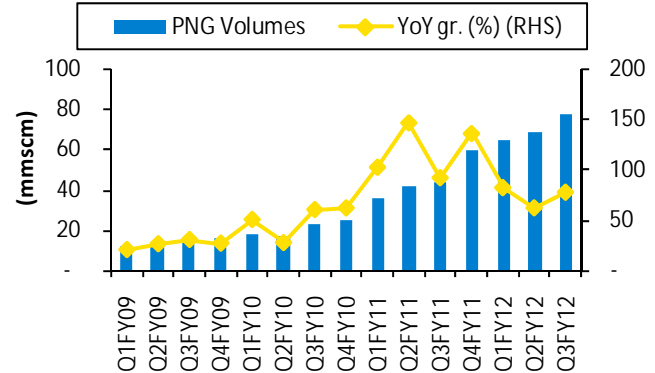
Y/E Mar	Q3FY12	Q3FY11	YoY gr. (%)	Q2FY12	9MFY12	9MFY11	YoY gr. (%)
CNG	5,700	4,248	34.2	5,248	15,636	11,665	34.0
PNG	1,636	840	94.8	1,384	4,289	2,186	96.2
<b>Gross Sales</b>	<b>7,336</b>	<b>5,088</b>	<b>44.2</b>	<b>6,632</b>	<b>19,925</b>	<b>13,851</b>	<b>43.9</b>
<b>Volumes</b>							
CNG (mn kgs)	180	155	16.1	177	519	452	14.6
PNG (mmscm)	77	43	78.0	68	210	121	73.9
<b>Realisations</b>							
CNG (Rs/ kg)	31.7	27.4	15.5	29.6	30.2	25.8	17.0
PNG (Rs/ scm)	21.2	19.4	9.4	20.3	20.4	18.1	12.8

Source: Company Data, PL Research

## Quarterly Highlights

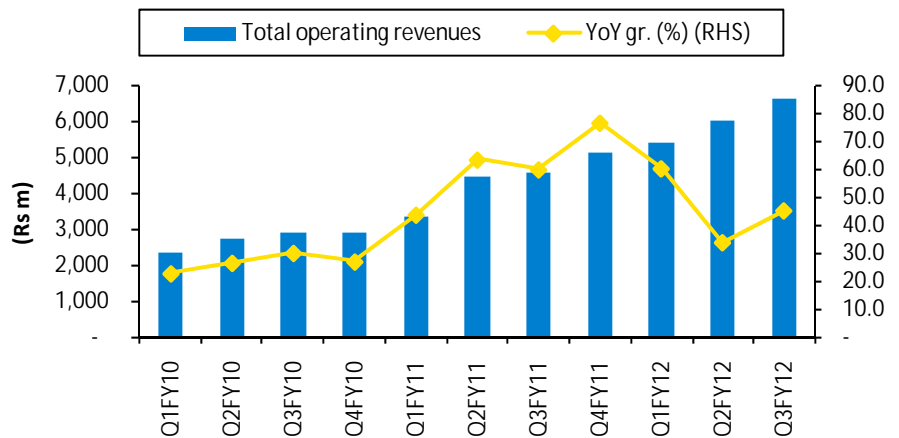
**Exhibit 1: CNG Volumes**


Source: Company Data, PL Research

**Exhibit 2: PNG Volumes**


Source: Company Data, PL Research

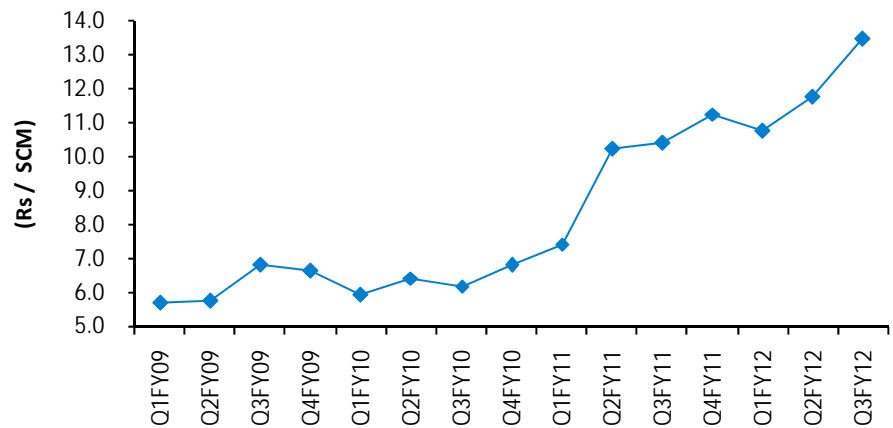
**Operating revenue in line with expectation:** For Q3FY12, IGL reported a 45.1% YoY increase in its operating income to Rs6,631m (Rs4,571m), as against our expectation of Rs6,769m CNG volumes increased by 16.1% YoY to 179.8.4m/kg (154.8m/kg), in line with our expectation of 180.9m/kg. Growth in PNG volumes was in line with expectation at 78.0% YoY to 77.1mmscm (43.3mmscm). This led to total volumes increasing by 25.9% YoY to 3.45mmscmd (2.71mmscmd). Average gross CNG realisations were higher on a YoY basis at Rs31.7/kg (Rs27.4/kg) due to the CNG price hike effective over the trailing one year. Average PNG realisations stood at Rs21.2/scm (Rs19.4/scm).

**Exhibit 3: Operating Revenue**


Source: Company Data, PL Research

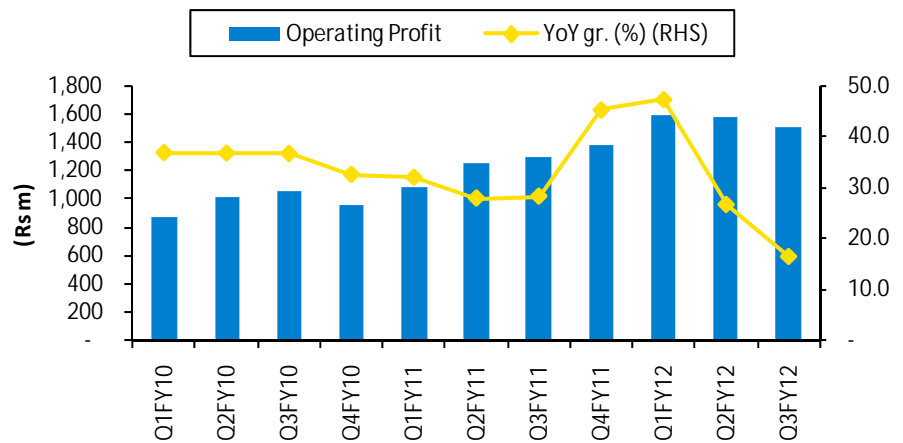
**OPM contracts by 560bps YoY to 22.7%:** Gas sourcing cost increased by 62.8% YoY to Rs4,230m (Rs2,598m). Raw material cost, during the quarter, stood at Rs13.5/scm. Gross gas spreads, during the quarter, on a YoY basis, stood higher at Rs7.7/scm (Rs7.9/scm). The same also witnessed moderation on a QoQ basis (Rs7.9/scm in Q2FY12). Staff cost increased 7.9% YoY to Rs107m (Rs99m), whereas other operating expenditure moved up 36.0% YoY to Rs791m (Rs581m). OPMs, during the quarter, contracted 560bps YoY to 22.7% (28.3%) on account of an increase in gas prices and operating expenditure. Operating profits grew by 16.4% YoY on account of volume growth.

**Exhibit 4: Gas Cost**



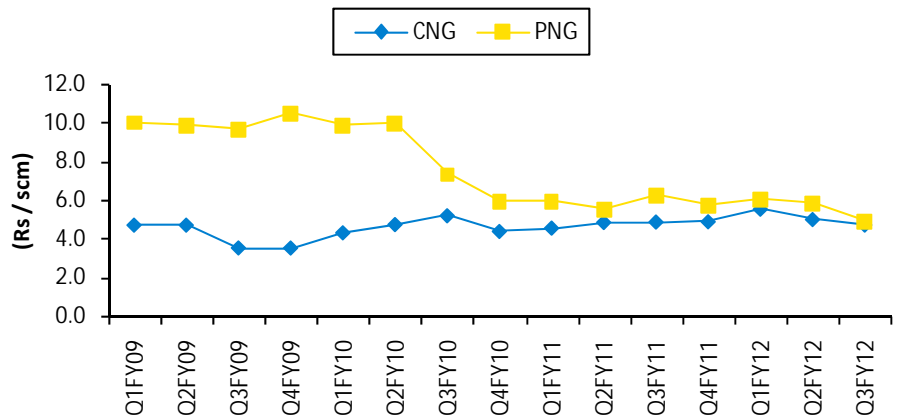
Source: Company Data, PL Research

**Exhibit 5: Operating Profits**



Source: Company Data, PL Research

**Exhibit 6: EBITDA Margins**

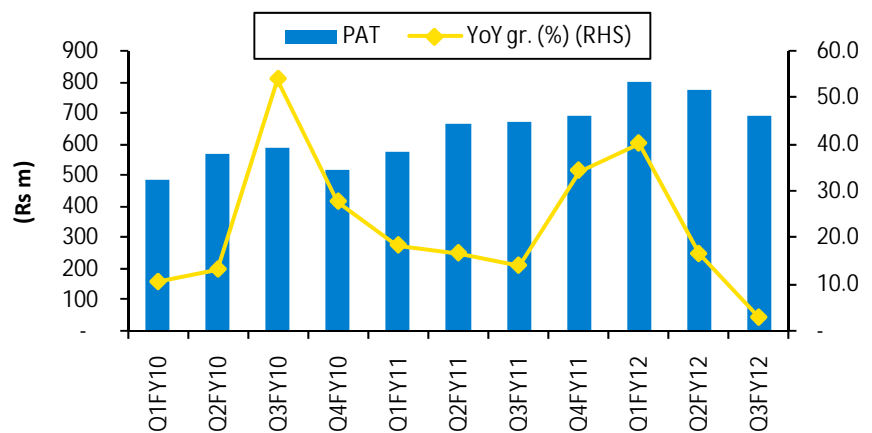


Source: Company Data, PL Research

**Depreciation increases on capitalization of assets:** Depreciation, during Q3FY12, increased by 40.7% YoY to Rs368m (Rs262m) and 6.8% QoQ. However, the same was lower due to change in the depreciation policy for the few assets from the beginning of the fiscal, which in turn, resulted in lower depreciation to the tune of Rs35.5m for the quarter.

**PAT up 2.9%, slightly ahead of our expectation:** Higher EBITDA growth resulted in bottom-line growing by 2.9% YoY to Rs692m (Rs672m), which was ahead of our expectation of Rs639m.

**Exhibit 7: Profit after tax**



Source: Company Data, PL Research

## Valuation

IGL stock price has corrected by ~15.0% over the last one quarter, grossly underperforming the benchmark indices. Concerns were first levied on account of depreciating rupee and pass through capacity due to increasing gas prices. The concerns were further accentuated with potential the regulation of the marketing margins of the city gas distribution companies.

Our understanding on the regulation of marketing margins of CGD companies is as follows:

- Our interactions with the companies involved suggest that potential regulation of the city gas distribution (CGD) companies is unlikely to happen.
- Any review of the marketing margins of the CGD companies it is likely to be a cumbersome process with amendment of Act being a difficult task. The precedent in this case can be seen from the fact that notification of the section 16 of PNRB Act took significant time.
- Moreover, any action will not be unilateral on part of PNGRB and is likely to involve the companies as well, which are likely to oppose any moves of the regulating of the margins.
- Moreover, the government's intent of extending the reach of city gas beyond the few cities will get a major jolt with regulation making a mockery of the bidding process in place.
- The potential regulation if any will also put in question the concept of marketing exclusivity to the incumbent players.
- Companies believe that given the prices of petrol, diesel, fuel oil and domestic LNG are regulated there is already an indirect regulation of the natural gas price charged by CGD companies. The key example of the same being that operation in the domestic LPG segment is not much remunerative for the city gas distribution companies.
- The tariff filing by IGL and MGL to PNGRB seems to suggest low component of marketing margins. We believe market concerns over reduction in the margins on account of high returns ratios seem exaggerated.

However, despite our belief that margins are unlikely to be regulated, the concern of potential regulation is likely to act as an overhang on the stock. To factor the same, we increase our discount rate from 12.0% to 12.75%, consequently leading to reduction in our target price to Rs399/share. The stock is currently available at 14.6x FY13E EPS of Rs23.0 and 3.3x P/BV. Our DCF based target price Rs392 provides an upside of 16.3% from the current levels.

**Exhibit 8: Key Assumptions**

<b>Y/e March</b>	<b>FY11</b>	<b>FY12E</b>	<b>FY13E</b>	<b>FY14E</b>
APM gas allocation(mmscmd)	2.2	1.9	1.7	1.5
APM gas cost (Rs/scm)	8.5	9.5	9.7	10.1
RIL gas allocation(mmscmd)	0.2	0.1	-	-
RIL gas cost (Rs/scm)	12.1	11.8	12.0	12.4
Total domestic gas(mmscmd)	2.4	2.0	1.7	1.5
Delivered price to IGL (RS) scm	12.9	26.9	29.5	28.2
Avg cost of gas sold (Rs/scm)	9.9	16.7	20.7	21.9
Gross margins (Rs./mmscm)	7.6	7.9	7.7	7.9
EBDITA (Rs./mmscm)	4.9	5.1	4.8	4.8
PAT (Rs./mmscm)	2.6	2.4	2.1	2.0

*Source: Company Data, PL Research*

**Income Statement (Rs m)**

Y/e March	2011	2012E	2013E	2014E
<b>Net Revenue</b>	<b>17,441</b>	<b>31,149</b>	<b>43,121</b>	<b>52,927</b>
Raw Material Expenses	9,835	21,146	31,394	38,937
Gross Profit	7,605	10,003	11,727	13,990
Employee Cost	379	504	636	781
Other Expenses	2,304	3,062	3,839	4,670
<b>EBITDA</b>	<b>4,923</b>	<b>6,437</b>	<b>7,252</b>	<b>8,539</b>
Depr. & Amortization	1,029	1,455	1,849	2,208
Net Interest	132	451	624	1,110
Other Income	95	70	90	70
<b>Profit before Tax</b>	<b>3,857</b>	<b>4,601</b>	<b>4,869</b>	<b>5,290</b>
Total Tax	1,259	1,551	1,642	1,784
<b>Profit after Tax</b>	<b>2,598</b>	<b>3,049</b>	<b>3,227</b>	<b>3,506</b>
Ex-Od items / Min. Int.	—	—	—	—
<b>Adj. PAT</b>	<b>2,598</b>	<b>3,049</b>	<b>3,227</b>	<b>3,506</b>
<b>Avg. Shares O/S (m)</b>	<b>140.0</b>	<b>140.0</b>	<b>140.0</b>	<b>140.0</b>
<b>EPS (Rs.)</b>	<b>18.6</b>	<b>21.8</b>	<b>23.0</b>	<b>25.0</b>

**Cash Flow Abstract (Rs m)**

Y/e March	2011	2012E	2013E	2014E
C/F from Operations	6,172	8,538	10,009	12,535
C/F from Investing	(7,856)	(5,930)	(5,910)	(5,430)
C/F from Financing	4,410	4,461	4,156	5,333
Inc. / Dec. in Cash	2,727	7,068	8,255	12,437
Opening Cash	1,213	165	813	858
Closing Cash	165	813	858	1,254
FCFF	(2,631)	(2,160)	(2,340)	(2,247)
FCFE	834	875	160	753

**Key Financial Metrics**

Y/e March	2011	2012E	2013E	2014E
<b>Growth</b>				
Revenue (%)	61.8	78.6	38.4	22.7
EBITDA (%)	29.3	30.8	12.7	17.7
PAT (%)	20.5	17.4	5.8	8.7
EPS (%)	20.5	17.4	5.8	8.7
<b>Profitability</b>				
EBITDA Margin (%)	28.2	20.7	16.8	16.1
PAT Margin (%)	14.9	9.8	7.5	6.6
RoCE (%)	22.9	19.1	15.8	14.8
RoE (%)	28.4	27.5	24.4	22.7
<b>Balance Sheet</b>				
Net Debt : Equity	0.3	0.5	0.6	0.6
Net Wrkng Cap. (days)	(33)	(14)	(5)	10
<b>Valuation</b>				
PER (x)	18.2	15.5	14.6	13.4
P / B (x)	4.7	3.9	3.3	2.8
EV / EBITDA (x)	10.2	8.2	7.6	6.8
EV / Sales (x)	2.9	1.7	1.3	1.1
<b>Earnings Quality</b>				
Eff. Tax Rate	32.7	33.7	33.7	33.7
Other Inc / PBT	2.5	1.5	1.8	1.3
Eff. Depr. Rate (%)	6.0	6.3	6.3	6.3
FCFE / PAT	32.1	28.7	5.0	21.5

Source: Company Data, PL Research.

**Balance Sheet Abstract (Rs m)**

Y/e March	2011	2012E	2013E	2014E
Shareholder's Funds	10,039	12,113	14,309	16,593
Total Debt	3,465	6,500	9,000	12,000
Other Liabilities	1,576	2,192	2,808	3,425
<b>Total Liabilities</b>	<b>15,079</b>	<b>20,805</b>	<b>26,117</b>	<b>32,018</b>
Net Fixed Assets	15,018	19,562	23,713	27,005
Goodwill	—	—	—	—
Investments	416	416	416	416
Net Current Assets	(355)	827	1,987	4,596
<i>Cash &amp; Equivalents</i>	<i>173</i>	<i>813</i>	<i>858</i>	<i>1,254</i>
<i>Other Current Assets</i>	<i>2,060</i>	<i>3,534</i>	<i>5,483</i>	<i>7,455</i>
<i>Current Liabilities</i>	<i>2,587</i>	<i>3,520</i>	<i>4,354</i>	<i>4,114</i>
Other Assets	—	—	—	—
<b>Total Assets</b>	<b>15,079</b>	<b>20,805</b>	<b>26,117</b>	<b>32,018</b>

**Quarterly Financials (Rs m)**

Y/e March	Q4FY11	Q1FY12	Q2FY12	Q3FY12
<b>Net Revenue</b>	<b>5,108</b>	<b>5,374</b>	<b>5,975</b>	<b>6,631</b>
<b>EBITDA</b>	<b>1,372</b>	<b>1,583</b>	<b>1,579</b>	<b>1,504</b>
<i>% of revenue</i>	<i>26.9</i>	<i>29.5</i>	<i>26.4</i>	<i>22.7</i>
Depr. & Amortization	297	322	344	368
Net Interest	70	90	118	135
Other Income	8	13	15	15
<b>Profit before Tax</b>	<b>1,012</b>	<b>1,185</b>	<b>1,132</b>	<b>1,016</b>
Total Tax	320	384	360	324
<b>Profit after Tax</b>	<b>692</b>	<b>801</b>	<b>772</b>	<b>692</b>
<b>Adj. PAT</b>	<b>692</b>	<b>801</b>	<b>772</b>	<b>692</b>

**Key Operating Metrics**

Y/e March	2011	2012E	2013E	2014E
CNG (mn kgs)	609.9	703.9	799.0	901.5
PNG (mmscm)	179.9	320.0	446.4	567.1
CNG (Rs/ kg)	26.5	38.4	45.4	48.0
PNG (Rs/ scm)	18.6	24.4	26.4	27.4

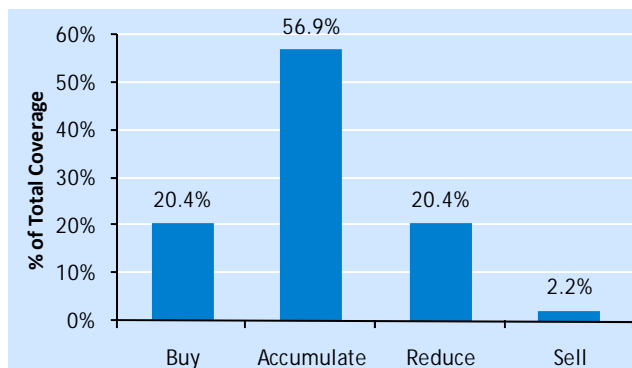
Source: Company Data, PL Research.

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#### Rating Distribution of Research Coverage



#### PL's Recommendation Nomenclature

<b>BUY</b>	: Over 15% Outperformance to Sensex over 12-months	<b>Accumulate</b>	: Outperformance to Sensex over 12-months
<b>Reduce</b>	: Underperformance to Sensex over 12-months	<b>Sell</b>	: Over 15% underperformance to Sensex over 12-months
<b>Trading Buy</b>	: Over 10% absolute upside in 1-month	<b>Trading Sell</b>	: Over 10% absolute decline in 1-month
<b>Not Rated (NR)</b>	: No specific call on the stock	<b>Under Review (UR)</b>	: Rating likely to change shortly

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