

September 28, 2022

Gas prices set to get revised while oil prices decline...

As per media sources, prices of domestically produced natural gas are expected to increase to US\$9/mmbtu for nominated fields (from US\$6.1/mmbtu) and US\$12/mmbtu (from US\$9.92/mmbtu) for HPHT fields from October 1, based on the formula determined by the government. During our Q1FY23 update, we had already factored in higher gas prices in H2 and a further gradual decline in FY24E thereafter. However, on the other hand, we now expect falling crude oil prices to impact long term gas contracts (most are crude oil linked) in the medium to long term (FY24E) whereas spot prices continue to stay elevated in the near to medium term. Hence, due to this combination of falling crude oil prices and higher domestic gas prices, we expect a decline in FY24 EPS by around 0.3% to 2.3% for our upstream companies like ONGC and Reliance Industries. Similarly, for our downstream companies in gas sector, a combination of higher domestic gas prices (already factored in during Q1 update), expected softening of long term gas prices and higher spot gas prices, would yield a variable impact on our CGD companies i.e. for MGL (up 1.9% in FY24 EPS), for IGL (down 3.3% in FY24 EPS) and GGL (down 4.6% in FY24 EPS). For mid-stream companies such as Gail, increase in gas prices and decline in crude oil prices would reduce the FY24EPS by ~11.8%. Similarly, for Petronet LNG, the above scenario of higher spot gas prices and falling crude prices would lead to a decline in FY24EPS by 9.4%.

Domestic and spot gas prices to rise but crude prices fall

- Domestic gas prices are revised every six months. Earlier, gas prices for October 1, 2021 to March 31, 2022 were US\$2.9/mmbtu and US\$6.13/mmbtu (ceiling for deepwater fields). These prices were revised to US\$6.1/mmbtu and US\$9.92/mmbtu, respectively, from April 1, 2022 onwards. Gas prices are expected to rise to US\$9/mmbtu and \$12/mmbtu from October 1 as global benchmarks are also trading at elevated levels. Upwards revision in domestic gas prices will benefit upstream companies like ONGC and RIL. Higher spot gas prices would lead to a decline in the petchem volumes and increase the LPG volumes of Gail. Regasification volumes of Petronet LNG would also be impacted. Margins of CGDs like IGL, MGL and Gujarat Gas would decline as their gas sourcing costs would increase
- Revision in gas prices comes at a time when crude oil prices have fallen to ~US\$84/bbl on account of a possible recessionary scenario in the west. Decline in crude oil prices would reduce the net oil realisation of upstream companies. However, RLNG prices, which are Brent linked, would also decline. This would reduce the long term gas cost for IGL, MGL and GGL. Hence, the long term volumes of Petronet are expected to increase
- We have already factored in the possible increase in domestic gas prices and its impact on the above companies in our previous estimates. However, the sharp fall in crude oil prices and elevated spot LNG prices, which would negate the impact of increase in domestic gas prices, have now been taken into account

Valuation and Outlook

We maintain **HOLD** rating on ONGC with a target price of ₹ 135/share. For Reliance Industries we maintain **HOLD** rating with a target price of ₹ 2685/share. We maintain **HOLD** rating on IGL, with a target price of ₹ 420/share. For MGL, we maintain **HOLD** rating with a target price of ₹ 850/share while for GGL also we maintain **HOLD** rating with a target price of ₹ 480/share. For Gail, we maintain our **BUY** rating with a target price of ₹ 100/share. For Petronet LNG, we maintain **HOLD** rating with a target price of ₹ 210/share.

Recent highlights & Key Risks

Key Risk: (i) Higher than estimated spot gas price (ii) Slowdown in domestic demand

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Exhibit 1: Rating matrix

Company	Rationale	CMP	Target Price	Upside	Rating
ONGC	We had already factored in the increase in gas prices in our previous estimates; however the sharp fall in crude oil prices has now been taken into account	124	135	9%	HOLD
Reliance Industries	In our previous update, we had already considered the possible increase in domestic gas prices. Decline in crude prices has now been factored in	2,394	2,685	12%	HOLD
IGL	Although domestic gas sourcing cost would increase and spot gas prices are trading at elevated levels, decline in crude oil prices will reduce the long term gas sourcing	423	420	-1%	HOLD
MGL	Decline in crude prices will negate the higher gas sourcing costs, which were factored in our Q1FY23 update	857	850	-1%	HOLD
Gujarat Gas	Higher domestic gas and spot LNG prices would increase the sourcing cost but falling crude prices will reduce the long term gas sourcing	500	480	-4%	HOLD
Gail	Increase in domestic gas prices had already been considered, whereas higher spot prices, which would reduce the petchem segment volumes and increase the LPG volumes have now been taken into account	86	100	16%	BUY
Petronet LNG	Decline in crude prices and elevated spot LNG prices, which would affect the regasification volume, have now been taken into account in our estimates	200	210	5%	HOLD

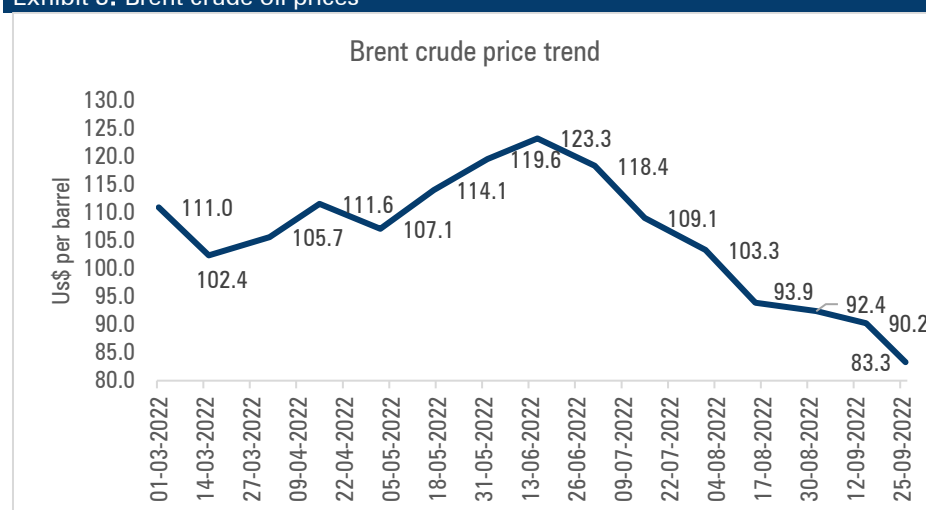
Source: Company, ICICI Direct Research

Exhibit 2: New vs. Old EPS

	ONGC	RIL	IGL	MGL	Gujarat Gas	GAIL	Petronet LNG
Prev FY24 EPS	42.80	121.80	21.00	83.60	21.90	10.10	21.20
New FY24 EPS	41.80	121.40	20.30	85.20	20.90	8.90	19.20

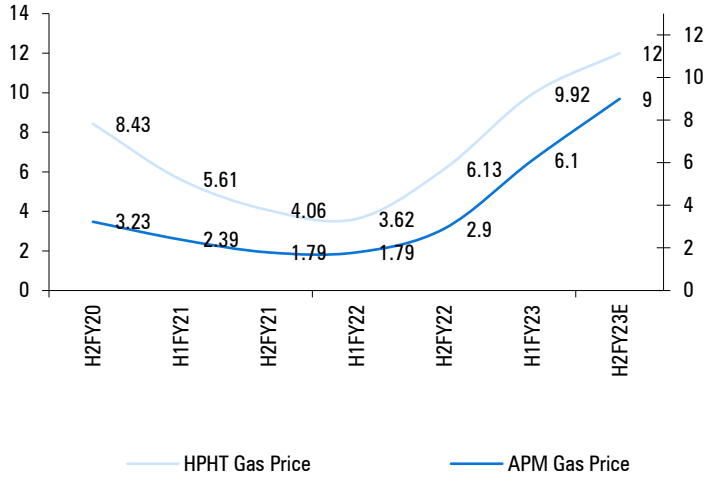
Source: Company, ICICI Direct Research

Exhibit 3: Brent crude oil prices



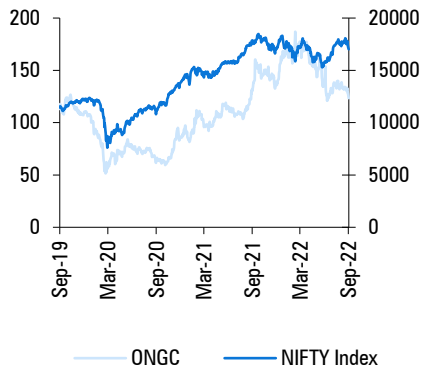
Source: Bloomberg, ICICI Direct Research

Exhibit 4: Domestic gas prices

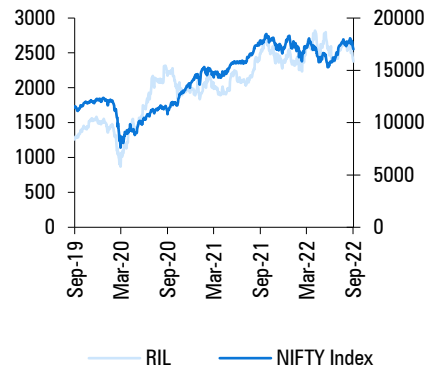


Source: Company, ICICI Direct Research

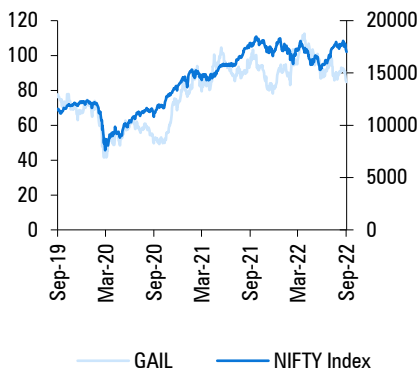
Price Chart (ONGC)



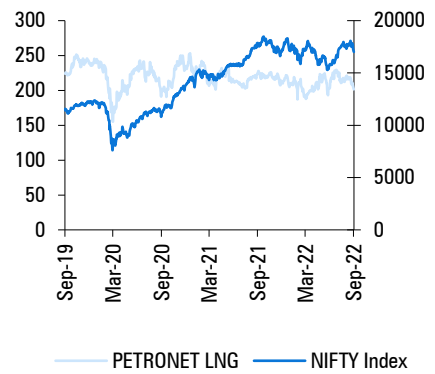
Price Chart (Reliance Industries)



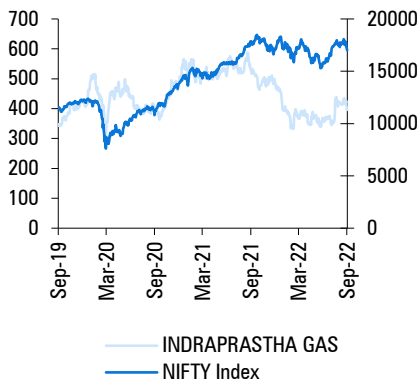
Price Chart (Gail)



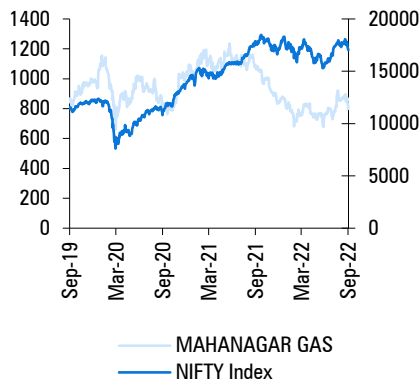
Price Chart (Petronet LNG)



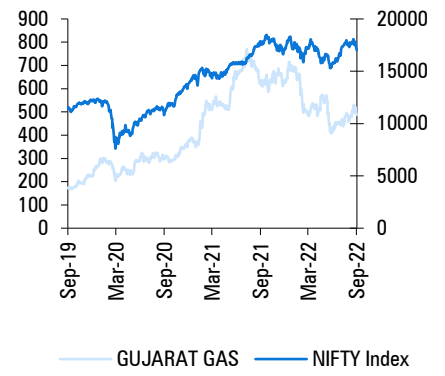
Price Chart (IGL)



Price Chart (MGL)



Price Chart (Gujarat Gas)



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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: < -15%



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