

21 March 2024

India | Equity Research | Company Update

## Mahanagar Gas

Oil &amp; Gas

### Management meeting – no red flags

We met with senior management of Mahanagar Gas (MGL) to get a sense of recent developments and the outlook ahead. Key messages from the conversation: 1) Price cut of INR 2.5/kg effected in CNG was not impacted by recent comments by the regulator/ministry and was to pass through the lower LNG price benefits and protect volumes. 2) Given that petrol/diesel prices have also been reduced, the price cut will help maintain competitiveness. 3) Margins while being lower in Q4FY24 vs. 9M average of INR 14.8/scm remain resilient, with MGL's CNG and domestic PNG prices still the lowest among peers. 4) Guidance of 6-7% volume growth for FY25, with Unison's potential volumes in 4-5 years at a material 1.3mmscmd (total volumes of MGL today at 3.6/scm). Reiterate BUY.

### Margins resilient – we do not see material downside risk

MGL and IGL announced price cuts of INR 2.5/kg each (6-7<sup>th</sup> Mar'24) based on the recent softening of LNG prices – trading below USD 9/MMBtu (Q4FY24TD average of 9.2/MMBtu) vs. average of ~USD 15.2/MMBtu in Q3FY24. We believe these cuts are in line with the recent ebb in spot LNG prices and would hardly pinch margins/profitability for these CGDs. Management has stated that the shrinking APM allocation is a concern and will imply higher HP/HT gas procurement going ahead, but margins will still sustain at levels of INR 12/scm over the medium term – this is well above FY19-24 average of INR 10.4/scm, but below the estimated INR 14.3-14.5/scm in FY24E.

### Volume growth to pick up in FY25

FY24 is likely to end up at a run rate of ~4-5%, as per management (9M growth at 3.3%); but management is a lot more bullish on FY25E's growth prospects, pegging estimates at 6-7%, on the back of: 1) steady penetration across vehicle segments; 2) growing bus population by MSRTC; 3) aggressive growth in the industrial/commercial (I/C) segments, especially in GA-2 (Thane) and GA-3 (Raigadh); and 4) growing volumes from the LCV segment owing to contiguous development of CNG network in and around MMR and the introduction of new CNG vehicles by the OEMs. Our base case estimates continue to be at ~6% for FY25-FY26E

### Financial Summary

Y/E March (INR mn)	FY23A	FY24E	FY25E	FY26E
Net Revenue	62,773	61,904	66,338	72,084
EBITDA	11,842	19,154	18,520	18,709
EBITDA %	18.9	30.9	27.9	26.0
Net Profit	7,901	13,343	12,828	13,025
EPS (INR)	80.0	135.1	129.9	131.9
EPS % Chg YoY	32.4	68.9	(3.9)	1.5
P/E (x)	16.1	9.5	9.9	9.7
EV/EBITDA (x)	9.4	5.3	5.1	4.6
RoCE (Pre-tax) (%)	24.7	35.5	28.0	23.9
RoE (%)	20.4	29.2	23.7	20.8

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#### Market Data

Market Cap (INR)	127bn
Market Cap (USD)	1,526mn
Bloomberg Code	MAHGL IN
Reuters Code	MGAS BO
52-week Range (INR)	1,580 /909
Free Float (%)	57.0
ADTV-3M (mn) (USD)	12.0

Price Performance (%)	3m	6m	12m
Absolute	11.2	23.7	32.5
Relative to Sensex	8.9	15.7	7.3

#### Earnings Revisions (%)

	FY24E	FY25E	FY26E
Revenue	0.0	0.0	0.0
EBITDA	0.0	(1.9)	(2.9)
EPS	0.0	(2.1)	(3.2)

#### Previous Reports

25-01-2024: [Q3FY24 results review](#)

28-10-2023: [Q2FY24 result review](#)

### **Unison and Raigadh can collectively add incremental 1.7-1.8mmscmd of volumes by FY28-29E**

With the formalities of the Unison Infra acquisition completed in FY24, MGL is looking to aggressively expand the CNG network in the 3 GAs operated by Unison, namely: 1) Ratnagiri; 2) Chitradurga and Devangere; and 3) Latur and Osmanabad Districts, with guidance to spend INR 4-5bn in these areas over the next three years. Management guidance is for a potential 1.2-1.3mmscmd from these areas in aggregate in the next 4-5 years (current volumes ~0.13mmscmd)

Similarly, MGL is gradually ramping up operations in the GA-3 (Raigadh) area and volumes are expected to grow from the current 0.14mmscmd to 0.7-0.75mmscmd over the next few years from this area as well by FY28-29. Given the current base of 3.6-3.7mmscmd for MGL, the incremental 1.7-1.8mmscmd from these new areas provides substantial comfort on growth over the next 6-7 years for MGL.

### **APM allocation reduces further, HPHT contracts; moderate LNG prices to offset the impact somewhat**

APM allocation to the priority sector has reduced to ~75% levels in Q4 vs. 78% in Q3. Additionally, with the rising demand from newer CGDs and stagnating volumes from the legacy fields of ONGC, the guidance is for this percentage to steadily decline over the next few years. Having said that, the 0.51mmscmd of HPHT gas contracts and the moderating Spot LNG prices should help offset the impact to a degree. Nevertheless, to factor in the weaker gas allocation, we have reduced our gas allocation expectations from APM to 73/71% over FY25/26E – this reduces margins for FY25E/26E by INR 0.3/0.4 per scm vs. the earlier estimates and EPS by 2.1/3.2%.

### **LNG retail, a material opportunity, but returns/timelines unclear**

MGL has entered into a JV with Baidyanath LNG to develop its LNG retail business. It plans to set up five–six stations initially, at a combined investment of ~INR 300mn – LNG for long haul trucks can become a substantial business opportunity, with even a 1% conversion delivering 1-2mtpa of additional LNG demand. However, with an additional cost of INR 0.8-1mn required to modify the trucks and the technology, along with the use cases still evolving, it will take time for the potential to become more apparent in this space.

### **CBG plant visibility improves**

MGL has finalised the initial plans for setting up the CBG plant in MMR in collaboration with BMC. The initial plan envisages 1,000t/d of CBG capacity in two locations with 500t/d each at an aggregate investment of INR 6bn. Waste segregation and land allocation will be handled by the BMC and availability of raw material is not a constraint. MMR generates 7,000t/d of waste, of which 3,500t/d is suitable for CBG use. The CBG offtake is proposed at a 20% discount to CNG and 1% blending will be possible in the next two–three years for MGL.

### **Valuations and view – remain positive**

Maharashtra State Road Transport's (MSRTC) plan to add ~800 new buses, higher conversion run rates of CNG and stronger price competitiveness vs. alternate fuels should drive stronger volume growth going forward. We factor in 5–6% volume growth for MGL over the medium term. We see some moderation in margins over the next two–three years, and estimate EBITDA/scm of INR 14.7/13.4/12.7 for FY24/25/26.

At its current market price, MGL trades at 9.9x FY25E and 9.7x FY26E EPS, which is at a steep discount to peers. The current correction provides an attractive opportunity to enter the stock, with our TP of INR 1,545, implying an 17% upside.

**Exhibit 1: Sensitivity on margins due to increase in Spot LNG prices**

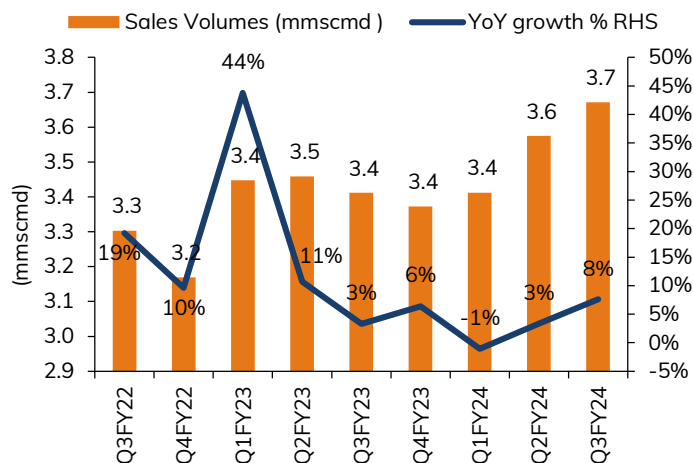
				Q1FY25e	Q1FY25e	Q1FY25e
MGL		Q3FY23	FY25E Base case	Scenario 1	Scenario 2	Scenario 3
Spot LNG	USD/mmbtu	16.2	16.6	10.0	10.5	11.0
Volume	mmscmd	2.6	2.7	2.7	2.7	2.7
CNG Realisation	INR/kg	76.0	79.3	73.5	73.5	73.5
Net CNG Realisation	INR/scm	45.8	47.8	43.6	43.6	43.6
Gas Cost	INR/scm	23.3	25.3	23.1	23.5	23.9
Gross margin	INR/scm	22.5	22.5	20.5	20.1	19.7
Gross margin	INR mn	5,390.4	22,347.1	4,955.7	4,854.0	4,766.8
Volume	mmscmd	0.5	0.5	0.5	0.5	0.5
PNG Realisation	INR/scm	47.0	47.0	47.0	47.0	47.0
Gas Cost	INR/scm	23.3	25.3	23.1	23.5	23.9
Gross margin	INR/scm	23.7	21.7	23.9	23.5	23.1
Gross margin	INR mn	1,143.2	4,329.2	1,175.1	1,154.4	1,136.6
Total Gross Margin	INR mn	6,495.2	26,215.5	6,371.7	6,220.2	6,090.3
Gross Margin	INR/scm	19.4	18.9	18.9	18.4	18.0

Source: Company data, I-Sec research

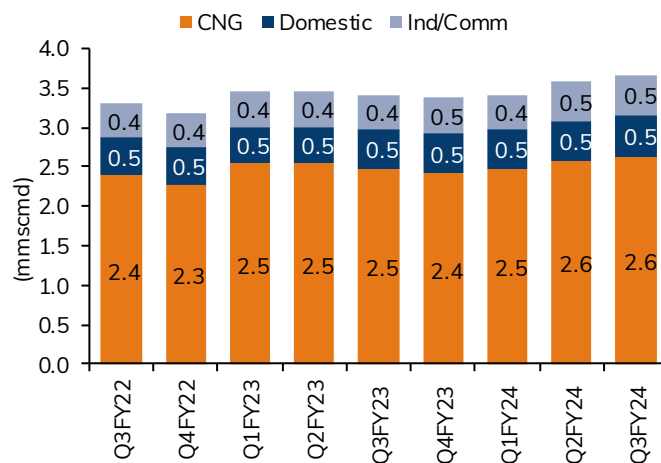
**Exhibit 2: Quarterly snapshot**

INR mn	Q3FY24	Q3FY23	YoY (%)	Q2FY24	QoQ %	9MFY24	9MFY23	YoY (%)
Sales	15,632	16,658	(6.2)	15,651	(0.1)	46,616	46,741	(0.3)
EBITDA	4,487	2,561	75.2	4,789	(6.3)	14,488	7,945	82.4
Adj. PAT	3,172	1,721	84.3	3,385	(6.3)	10,241	5,212	96.5
EPS (INR)	32.1	17.4	84.3	34.3	(6.3)	103.7	52.8	96.5
Depreciation	683	585	16.7	658	3.8	1,961	1,673	17.2
Sales (mmscm)	338	314	7.6	329	2.7	977	946	3.3
Sales (mmscmd)	3.7	3.4	7.6	3.6	2.7	3.6	3.4	3.3
CNG sales (mmscm)	242	228	6.4	238	1.9	706	693	1.9
PNG sales (mmscm)	96	86	10.8	91	4.7	271	253	7.2
Gross margin (INR/scm)	19.0	13.5	40.0	20.2	(6.4)	20.4	13.6	50.6
EBITDA margin (INR/scm)	13.3	8.2	62.8	14.6	(8.8)	14.8	8.4	76.5
EBITDA Margin (%)	28.7%	15.4%		30.6%		31.1%	17.0%	82.9
CNG sales (INR mn)	11,065	11,809	(6.3)	11,277	(1.9)	33,422	32,524	2.8
CNG realisations (INR/scm)	45.7	51.9	(11.9)	47.5	(3.7)	47.4	47.0	0.9
PNG sales (INR mn)	4,568	4,849	(5.8)	4,375	4.4	13,194	14,218	(7.2)
PNG realisations (INR/scm)	47.8	56.2	(15.0)	47.9	(0.3)	48.6	56.1	(13.4)
Gross margin (INR Mn)	6,402	4,251	50.6	6,659	(3.9)	19,952	12,820	55.6

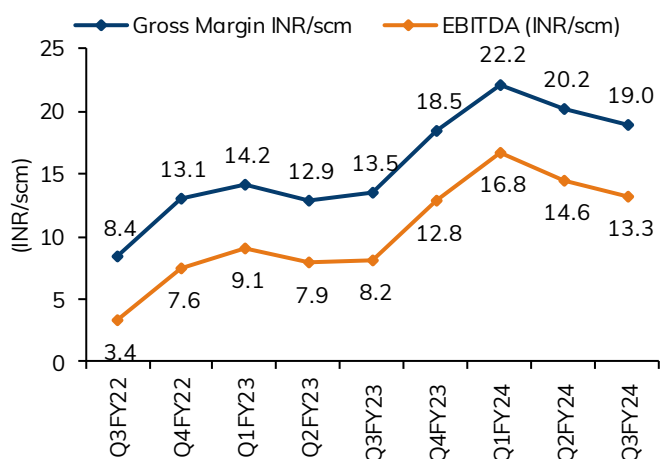
Source: Company data, I-Sec research

**Exhibit 3: Strong volume growth YoY**

Source: Company data, I-Sec research

**Exhibit 4: Segment-wise volume trends**

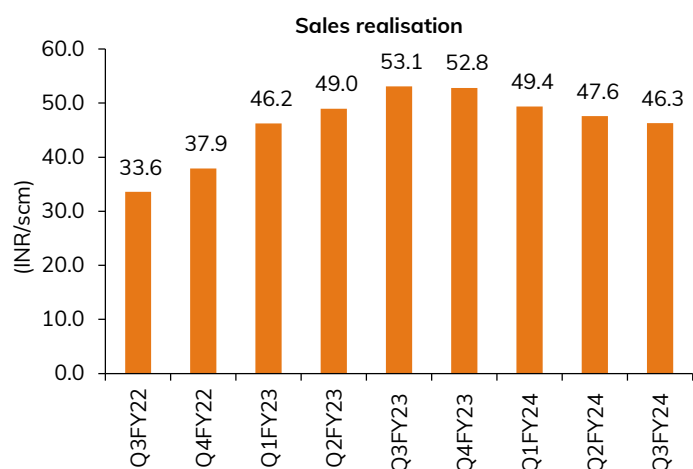
Source: Company data, I-Sec research

**Exhibit 5: Margins remain strong**

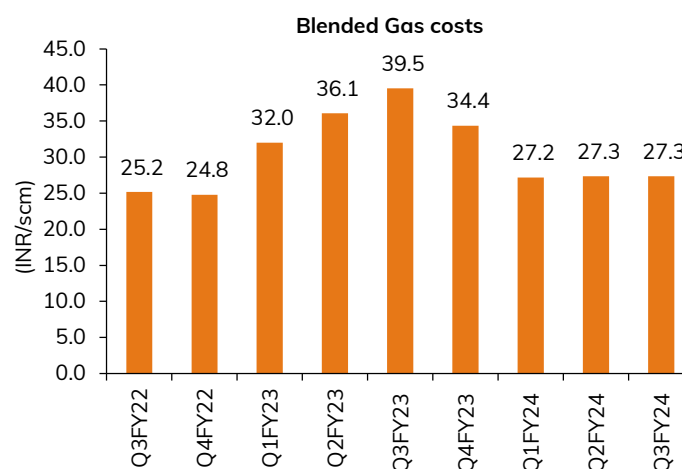
Source: Company data, I-Sec research

**Exhibit 6: Opex/scm remains muted QoQ**

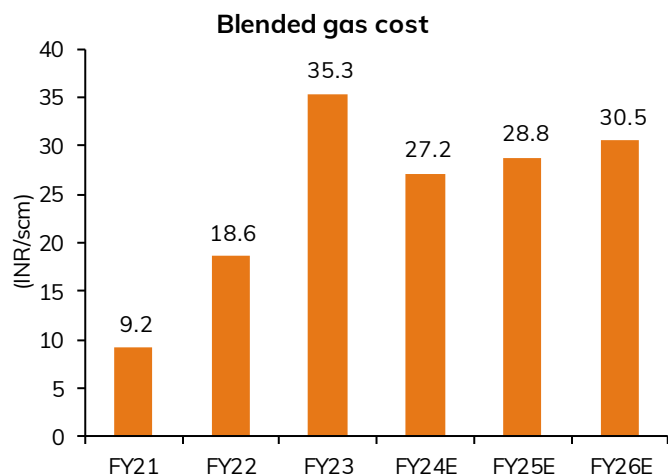
Source: Company data, I-Sec research

**Exhibit 7: Sales realisation has decreased QoQ...**

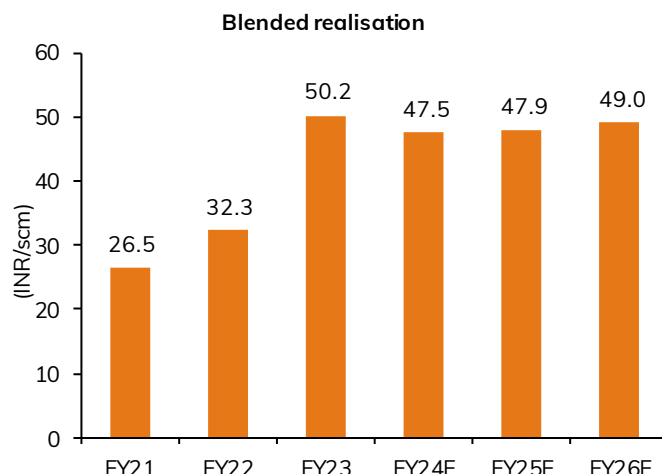
Source: Company data, I-Sec research

**Exhibit 8: ...but gas cost was flattish QoQ**

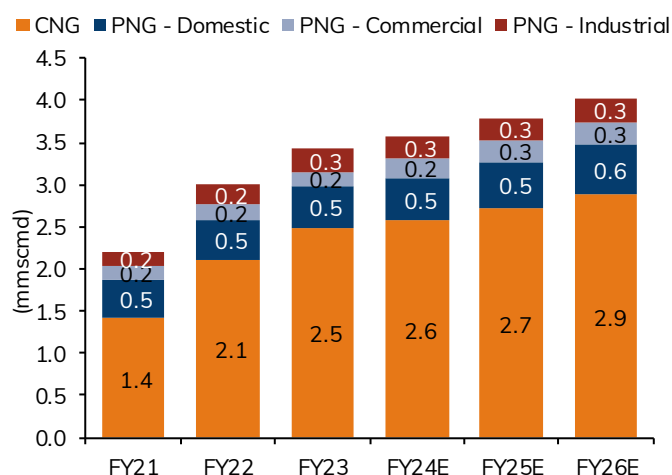
Source: Company data, I-Sec research

**Exhibit 9: MGL's gas cost may slip sharply in FY24E**

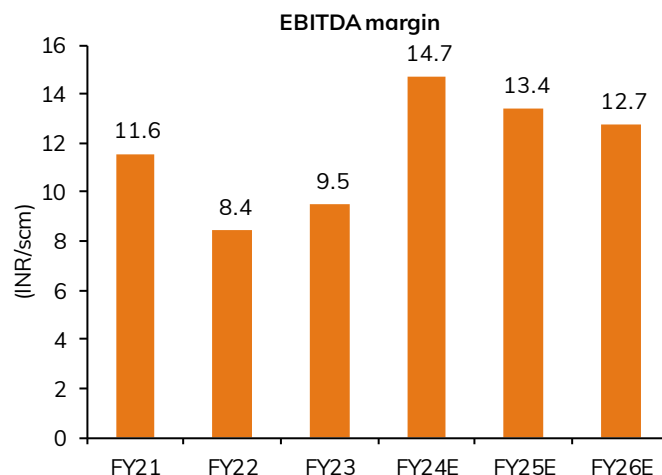
Source: Company data, I-Sec research

**Exhibit 10: Blended realisation to keep pace**

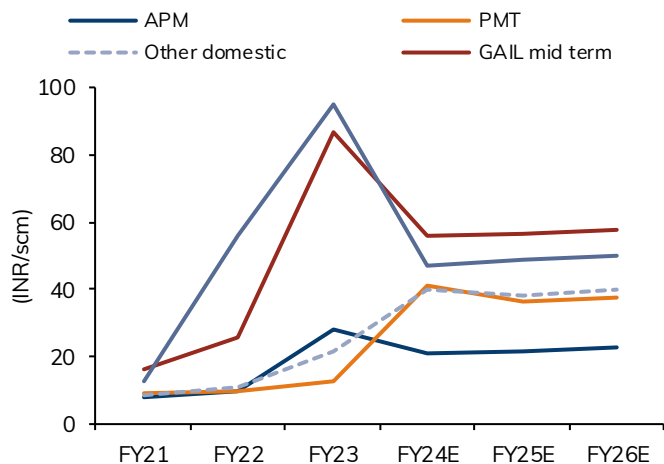
Source: Company data, I-Sec research

**Exhibit 11: Volume growth to be subject to pricing balance**

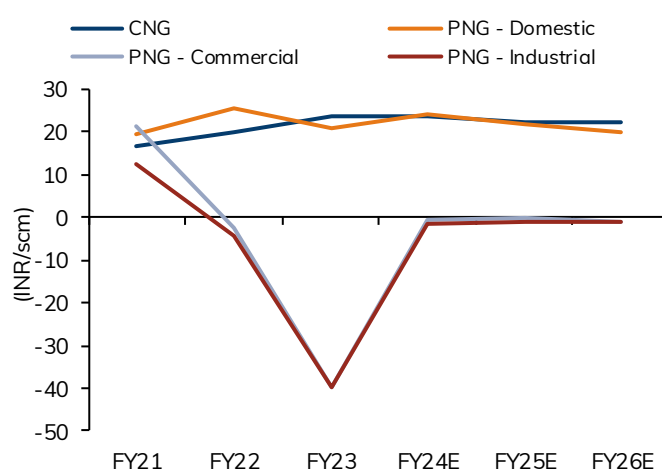
Source: Company data, I-Sec research

**Exhibit 12: Margin to moderate over FY24-FY26E**

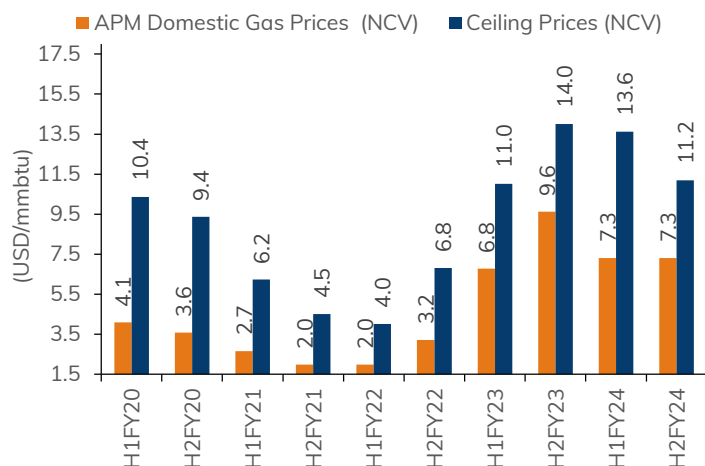
Source: Company data, I-Sec research

**Exhibit 13: Sourcing costs may decline in FY24-FY26E**

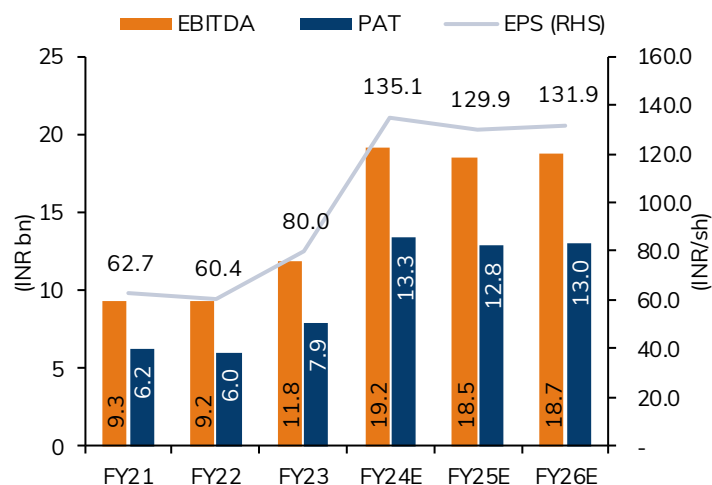
Source: Company data, I-Sec research

**Exhibit 14: Segment-wise margins to see divergence**

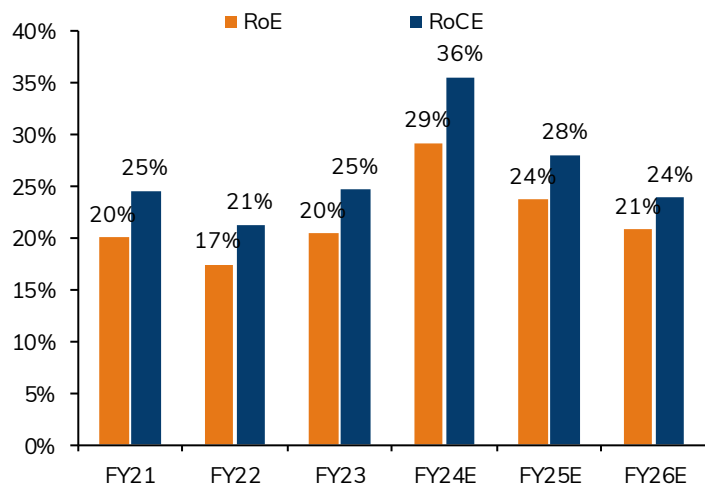
Source: Company data, I-Sec research

**Exhibit 15: APM gas prices capped with revised gas pricing policy and HPHT reduced by 18% vs H1FY24**


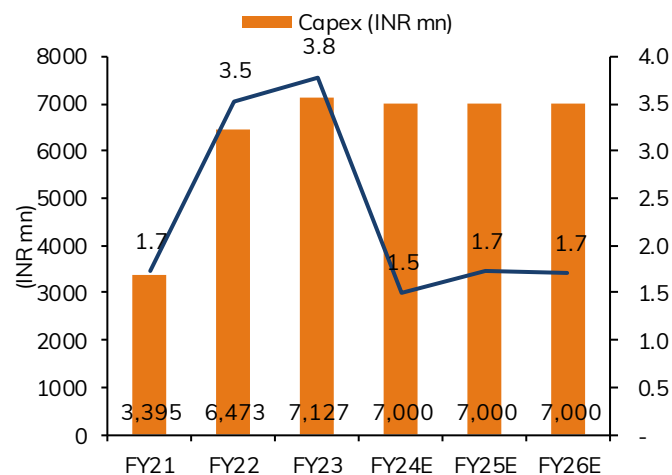
Source: Company data, I-Sec research

**Exhibit 16: EBITDA and EPS to remain muted over FY24-FY26E**


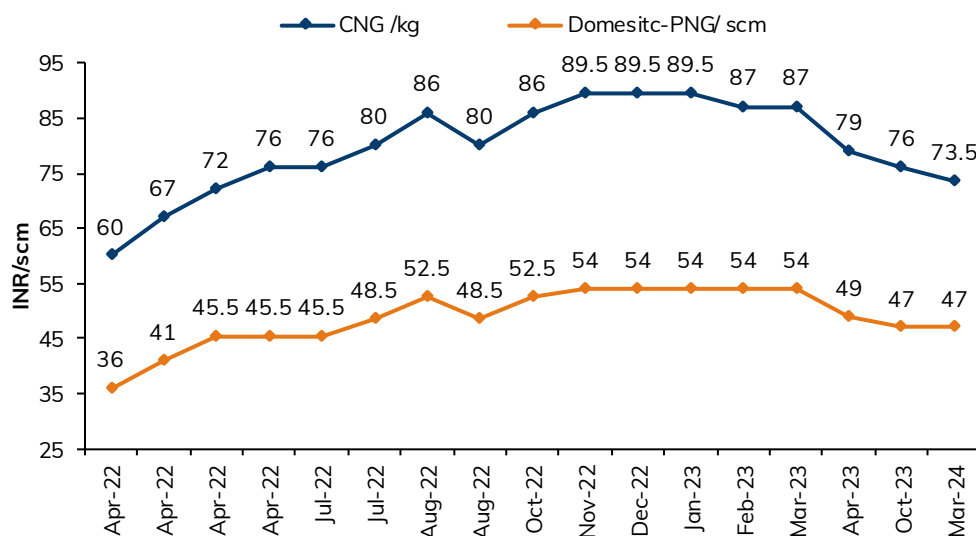
Source: Company data, I-Sec research

**Exhibit 17: Return ratios to moderate over FY24-FY26E**


Source: Company data, I-Sec research

**Exhibit 18: Capex of INR 21bn estimated over FY24-FY26E**


Source: Company data, I-Sec research

**Exhibit 19: MGL's price trends for CNG and domestic PNG**


Source: Company data, I-Sec research

## Valuation: Target price of INR 1,545 implies ~17% upside

We value MGL on DCF methodology, using a WACC of 10.9%, DER of 35%, long-term EBITDA assumption of INR 12.4/scm and terminal growth rate of 3.1%. In the long term, we build in muted volume growth beyond FY26E as well as flattish margins, given our caution around longer-term growth expectations. Our DCF value delivers a target price of INR 1,545, ~17% upside from CMP. The stock trades well below its 5-year trading band and at a steep discount to peers despite materially improved prospects over the next 2-3 years, underpinning our positive stance. Maintain **BUY**.

### Exhibit 20: Valuation summary

	Assumption
Cost of Equity	13.0%
Cost of Debt	7.3%
Post tax cost of debt	4.8%
Average D/E ratio	35.0%
WACC	10.9%
Terminal Growth rate	3.1%
Total NPV potential INR mn	1,44,507
TP MGL Standalone (INR.sh)	1,463
UEPL (INR.sh)	83
TP (INR.sh)	1,545
CMP (INR.sh)	1,320
Upside/(downside)	17%

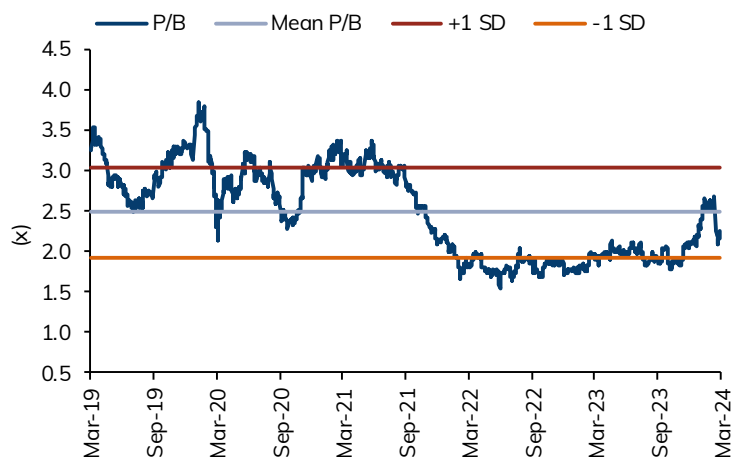
Source: Company data, I-Sec research

### Exhibit 21: MGL's P/E trading well below 5-year band



Source: Company data, I-Sec research

### Exhibit 22: MGL's P/B trading well below 5-year band



Source: Company data, I-Sec research

### Exhibit 23: Shareholding pattern

%	Jun'23	Sep'23	Dec'23
Promoters	32.5	32.5	32.5
Institutional investors	47.5	46.6	48.1
MFs and other	2.2	1.7	4.0
FIs/ Banks	-	-	-
Insurance Cos.	12.5	13.8	12.7
FIIIs	32.8	31.1	31.4
Others	20.0	20.9	19.4

Source: Bloomberg, I-Sec research

### Exhibit 24: Price chart



Source: Bloomberg, I-Sec research



## Financial Summary

### Exhibit 25: Profit & Loss

(INR Mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
<b>Net Sales</b>	<b>62,773</b>	<b>61,904</b>	<b>66,338</b>	<b>72,084</b>
<b>EBITDA</b>	<b>11,842</b>	<b>19,154</b>	<b>18,520</b>	<b>18,709</b>
EBITDA Margin (%)	18.9	30.9	27.9	26.0
Depreciation & Amortization	2,311	2,930	3,350	3,770
EBIT	9,531	16,224	15,170	14,939
Interest expenditure	94	50	50	50
Other Non-operating Income	1,119	1,653	2,019	2,513
<b>PBT</b>	<b>10,556</b>	<b>17,827</b>	<b>17,139</b>	<b>17,402</b>
<b>Profit / (Loss) from Associates</b>	-	-	-	-
Less: Taxes	2,655	4,484	4,311	4,377
PAT	7,901	13,343	12,828	13,025
Less: Minority Interest	-	-	-	-
<b>Net Income (Reported)</b>	<b>7,901</b>	<b>13,343</b>	<b>12,828</b>	<b>13,025</b>
Extraordinaries (Net)	-	-	-	-
<b>Recurring Net Income</b>	<b>7,901</b>	<b>13,343</b>	<b>12,828</b>	<b>13,025</b>

Source Company data, I-Sec research

### Exhibit 26: Balance sheet

(INR Mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
<b>Total Current Assets</b>	<b>6,964</b>	<b>15,317</b>	<b>21,140</b>	<b>27,622</b>
of which cash & bank	2,279	11,726	17,367	23,624
<b>Total Current Liabilities &amp; Provisions</b>	<b>15,612</b>	<b>20,671</b>	<b>23,247</b>	<b>26,078</b>
<b>Net Current Assets</b>	<b>(8,648)</b>	<b>(5,354)</b>	<b>(2,107)</b>	<b>1,545</b>
Other Non Current Assets	2,918	2,918	2,918	2,918
<b>Net Fixed Assets</b>	<b>30,257</b>	<b>34,327</b>	<b>37,977</b>	<b>41,207</b>
Other Fixed Assets	-	-	-	-
Capital Work in Progress	7,086	7,086	7,086	7,086
Non Investment	-	-	-	-
Current Investment	13,098	14,408	15,849	17,434
Deferred Tax Assets	-	-	-	-
<b>Total Assets</b>	<b>44,711</b>	<b>53,384</b>	<b>61,723</b>	<b>70,189</b>
<b>Liabilities</b>				
<b>Borrowings</b>	-	-	-	-
<b>Deferred Tax Liability</b>	<b>2,086</b>	<b>2,086</b>	<b>2,086</b>	<b>2,086</b>
Lease Liability	-	-	-	-
Other Liabilities	1,283	1,283	1,283	1,283
Equity Share Capital	988	988	988	988
Reserves & Surplus*	40,354	49,027	57,366	65,832
<b>Total Net Worth</b>	<b>41,342</b>	<b>50,015</b>	<b>58,353</b>	<b>66,820</b>
Minority Interest	-	-	-	-
<b>Total Liabilities</b>	<b>44,711</b>	<b>53,384</b>	<b>61,723</b>	<b>70,189</b>

Source Company data, I-Sec research

### Exhibit 27: Quarterly trend

(INR mn, year ending March)

	Mar-23	Jun-23	Sep-23	Dec-23
<b>Net Sales</b>	<b>16,031</b>	<b>15,332</b>	<b>15,651</b>	<b>15,632</b>
% growth (YOY)	-3.8%	-4.4%	2.1%	-0.1%
<b>EBITDA</b>	<b>3,897</b>	<b>5,213</b>	<b>4,789</b>	<b>4,487</b>
Margin %	24.3%	34.0%	30.6%	28.7%
Other Income	336	390	437	481
Extraordinaries	-	-	-	-
<b>Adjusted Net Profit</b>	<b>2,688</b>	<b>3,684</b>	<b>3,385</b>	<b>3,172</b>

Source Company data, I-Sec research

### Exhibit 28: Cashflow statement

(INR Mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
<b>Cash Flow from operation before working Capital</b>	<b>12,197</b>	<b>19,154</b>	<b>18,520</b>	<b>18,709</b>
Working Capital Changes	134	6,154	2,394	2,605
Tax	(2,638)	(4,484)	(4,311)	(4,377)
<b>Operating Cashflow</b>	<b>9,693</b>	<b>20,824</b>	<b>16,603</b>	<b>16,938</b>
Capital Commitments	(7,127)	(7,000)	(7,000)	(7,000)
<b>Free Cashflow</b>	<b>2,566</b>	<b>13,824</b>	<b>9,603</b>	<b>9,938</b>
Others CFI	(2,092)	343	578	928
<b>Cashflow from Investing Activities</b>	<b>(9,218)</b>	<b>(6,657)</b>	<b>(6,422)</b>	<b>(6,072)</b>
Inc (Dec) in Borrowings	-	-	-	-
Interest Cost	-	(50)	(50)	(50)
Others	(2,848)	(4,670)	(4,490)	(4,559)
<b>Cash flow from Financing Activities</b>	<b>(2,848)</b>	<b>(4,720)</b>	<b>(4,540)</b>	<b>(4,609)</b>
<b>Chg. in Cash &amp; Bank balance</b>	<b>(2,373)</b>	<b>9,447</b>	<b>5,641</b>	<b>6,257</b>
Closing cash & balance	2,279	11,726	17,367	23,624

Source Company data, I-Sec research

### Exhibit 29: Key ratios

(Year ending March)

	FY23A	FY24E	FY25E	FY26E
<b>Per Share Data (INR)</b>				
Recurring EPS	80.0	135.1	129.9	131.9
Diluted EPS	80.0	135.1	129.9	131.9
Recurring Cash EPS	103.4	164.7	163.8	170.0
Dividend per share (DPS)	26.0	47.3	45.5	46.2
Book Value per share (BV)	418.5	506.3	590.7	676.5
Dividend Payout (%)	32.5	35.0	35.0	35.0
<b>Growth (%)</b>				
Net Sales	77.5	(1.4)	7.2	8.7
EBITDA	28.1	61.7	(3.3)	1.0
EPS	32.4	68.9	(3.9)	1.5
<b>Valuation Ratios (x)</b>				
P/E	16.1	9.5	9.9	9.7
P/CEPS	12.4	7.8	7.8	7.6
P/BV	3.1	2.5	2.2	1.9
EV / EBITDA	9.4	5.3	5.1	4.6
EV / Operating Income	10.5	5.6	5.5	4.9
Dividend Yield (%)	2.0	3.7	3.5	3.6
<b>Operating Ratios</b>				
EBITDA Margins (%)	18.9	30.9	27.9	26.0
Effective Tax Rate (%)	25.2	25.2	25.2	25.2
Net Profit Margins (%)	12.6	21.6	19.3	18.1
NWC / Total Assets (%)	(19.3)	(10.0)	(3.4)	2.2
Fixed Asset Turnover (x)	1.6	1.4	1.3	1.2
Working Capital Days	(0.6)	(11.3)	(48.4)	(57.1)
Net Debt / Equity %	(37.2)	(52.3)	(56.9)	(61.4)
<b>Profitability Ratios</b>				
RoCE (%)	18.5	26.6	21.0	17.9
RoCE (Pre-tax) (%)	24.7	35.5	28.0	23.9
RoE (%)	20.4	29.2	23.7	20.8

Source Company data, I-Sec research



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