

Mahanagar Gas (MAHGAS)

₹ 986

Higher margins offset lower volumes...

- In Q1FY18, Mahanagar Gas (MGL) reported a mixed set of numbers with higher profitability but a disappointing volume performance. The topline increased 9.1% YoY to ₹ 582.9 crore in line with our estimates. Volumes increased 2.7% YoY to 2.6 mmscmd and came in below our estimate of 2.7 mmscmd. CNG volumes grew a mere 1.4% YoY and were at 1.88 mmscmd (our estimate: 1.98 mmscmd) whereas PNG volumes grew 6.7% YoY and were at 0.68 mmscmd (our estimate: 0.7 mmscmd)
- Gross margins were at ₹ 15.1/scm above our estimate of ₹ 13.7/scm on account of lower raw material costs (mainly due to lower spot gas prices and favourable exchange rate). Subsequently, EBITDA at ₹ 203.3 crore came in above our estimates of ₹ 174.1 crore
- Resultant PAT increased 34.1% YoY during the quarter to ₹ 124.3 crore, above our estimates of ₹ 107.4 crore

Strong margins, going forward

The quarter benefited from a strong rupee and lower spot LNG prices, which led to higher-than-expected gross margins at ₹ 15.1/scm vs. ₹ 12.7/scm in Q1FY17 (our estimate: ₹ 13.7/scm). On account of the same, EBITDA/scm came in above our estimates at ₹ 8.7/scm (our estimate: ₹ 7.1/scm). Going forward, we expect margins to remain strong due to the stronger rupee and lower gas prices adding to the competitiveness of CNG and domestic PNG over other liquid fuels. MGL's pricing power will enable it to pass on the increase in gas costs, if any, to customers, thus, maintaining margins. Hence, we expect gross margins at ₹ 15.1/scm in FY18E and FY19E, and, EBITDA per scm at ₹ 8.4/scm and ₹ 8.3/scm in FY18E and FY19E, respectively.

Seasonality adversely impacts CNG volume growth

During the quarter, CNG volumes were at 1.88 mmscmd, up 1.4% YoY (in kg, volume was up 4.4% YoY) and below our estimate due to lower consumption that was impacted by the vacation season. Volume growth, going ahead, may be better given steady conversion rate of vehicles to CNG and MGL's plans to aggressively set up CNG stations with 20-25 additions in FY18E. On PNG front, volumes increased 6.7% YoY to 0.68 mmscmd largely in line with our estimates on account of growth in domestic and commercial sales volumes. It plans to add 1.4 lakh households in FY18E. MGL currently has 9.8 lakh domestic PNG, ~3100 commercial customers and ~70 industrial customers. Going forward, we estimate sales volumes at 2.7 mmscmd and 2.8 mmscmd in FY18E and FY19E, respectively.

Favourable pricing, under-penetrated market to create value

The CGD sector has benefited in a significant manner from the government's decision to prioritise the allocation of domestic natural gas for CNG and domestic PNG customers. This has enabled MGL to access cheaper gas for CNG and domestic business segments, constituting ~86% of total sales volume. MGL's strong gas pipeline infrastructure and expanding operations in Mumbai, its adjoining areas and Raigad district will enable the company to capture the benefits of the large and growing market given the low penetration. The ongoing and upcoming bidding for new CGD areas also presents MGL with the scope to expand its business further. We value the stock at 22.5x FY19E EPS of ₹ 53.8 to arrive at a target price of ₹ 1210 with a **BUY** recommendation.

Rating matrix	
Rating	: Buy
Target	: ₹ 1210
Target Period	: 12 months
Potential Upside	: 23%

What's changed?	
Target	Changed from ₹ 1085 to ₹ 1210
EPS FY18E	Changed from ₹ 45.3 to ₹ 51.3
EPS FY19E	Changed from ₹ 48.2 to ₹ 53.8
Rating	Unchanged

Quarterly performance					
	Q1FY18	Q1FY17	YoY (%)	Q4FY17	QoQ (%)
Revenue	582.9	534.1	9.1	576.4	1.1
EBITDA	203.3	152.4	33.4	163.1	24.6
EBITDA (%)	34.9	28.5	635 bps	28.3	657 bps
PAT	124.3	92.7	34.1	99.5	25.0

Key financials				
₹ Crore	FY16	FY17	FY18E	FY19E
Revenues	2,285.8	2,239.1	2,521.1	2,731.4
EBITDA	513.0	644.2	825.9	864.0
Net Profit	308.7	393.4	506.3	531.4
EPS (₹)	34.6	39.8	51.3	53.8

Valuation summary				
	FY16	FY17	FY18E	FY19E
P/E	28.5	24.8	19.2	18.3
Target P/E	35.0	30.4	23.6	22.5
EV / EBITDA	16.9	14.8	11.4	10.8
P/BV	5.8	5.7	5.0	4.4
RoNW (%)	20.2	23.1	25.9	24.0
RoCE (%)	27.8	32.3	36.9	33.7

Stock data	
Particular	Amount
Market Capitalization (₹ Crore)	9,739.7
Total Debt (FY17) (₹ Crore)	2.4
Cash and Investments (FY17) (₹ Crore)	215.2
EV (₹ Crore)	9,952.5
52 week H/L	1086/528
Equity capital (₹ Crore)	98.8
Face value (₹)	10

Price performance				
Return %	1M	3M	6M	12M
IGL	14.2	20.8	20.8	78.1
Gujarat Gas	2.3	(2.3)	25.9	22.6
Mahanagar Gas	8.9	6.8	15.3	102.7

Research Analyst	
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Variance analysis

	Q1FY18	Q1FY18E	Q1FY17	YoY (%)	Q4FY17	QoQ (%)	Comments
Total Revenues	582.9	586.4	534.1	9.1	576.4	1.1	
Raw materials costs	231.2	253.0	245.5	-5.8	260.8	-11.3	
Employees Cost	17.5	16.5	14.6	19.5	16.0	8.9	
Other Expenses	130.9	142.2	121.7	7.6	136.5	-4.1	
Total Expenditure	379.6	411.7	381.8	-0.6	413.3	-8.2	
EBITDA	203.3	174.7	152.4	33.4	163.1	24.6	Higher-than-estimated EBITDA on account of higher gross margins due to benefits of lower spot LNG prices and rupee appreciation
EBITDA margins (%)	34.9	29.8	28.5	635 bps	28.3	657 bps	
Depreciation	24.6	25.7	21.6	14.0	25.7	-4.1	
EBIT	178.6	149.0	130.7	36.6	137.5	30.0	
Interest	0.2	0.3	0.5	-62.3	-0.1	-385.7	
Other Income	12.0	14.0	12.3	-2.6	13.0	-7.3	
Extra Ordinary Item	0.0	0.0	0.0	NA	0.0	NA	
PBT	190.4	162.7	142.5	33.6	150.5	26.6	
Total Tax	66.1	55.3	49.8	32.7	51.0	29.6	
PAT	124.3	107.4	92.7	34.1	99.5	25.0	Higher-than-estimated PAT mainly on account of higher gross margins

Key Metrics

Sales Volumes (mmscmd)	2.6	2.7	2.5	2.7	2.6	-2.1	CNG volumes were at 1.88 mmscmd (our estimate: 1.98 mmscmd) whereas PNG volumes were at 0.68 mmscmd (our estimate: 0.7 mmscmd)
Realisation (₹/scm)	25.0	24.1	23.3	6.9	24.4	2.2	Changes in the sales mix of CNG led to higher than estimated realisations despite nil price hikes during the quarter
Gross Margin (₹/scm)	15.1	13.7	12.7	18.6	13.4	12.5	Lower spot LNG prices and rupee appreciation led to higher gross margins

Source: Company, ICICIdirect.com Research

Change in estimates

(₹ Crore)	FY18E			FY19E			Comments
	Old	New	% Change	Old	New	% Change	
Revenue	2,468.8	2,521.1	2.1	2,685.0	2,731.4	1.7	
EBITDA	726.4	825.9	13.7	761.7	864.0	13.4	Upward revision in gross margin estimates led to revised EBITDA estimates
EBITDA Margin (%)	29.4	32.8	336 bps	28.4	31.6	326 bps	
PAT	447.6	506.3	13.1	475.7	531.4	11.7	
EPS (₹)	45.3	51.3	13.2	48.2	53.8	11.7	

Source: Company, ICICIdirect.com Research

Assumptions

	FY18E		Current		Earlier		Comments
	FY16	FY17	FY18E	FY19E	FY18E	FY19E	
Sales Volumes (mmscmd)	2.4	2.6	2.7	2.8	2.7	2.9	Volume growth of 6.5% YoY revised downward to 6% YoY for coming quarters
Realisation (₹/scm)	25.5	23.8	25.7	26.3	24.7	25.2	
Gross Margin (₹/scm)	11.9	13.0	15.1	15.1	15.0	13.7	Strong rupee and lower spot LNG prices led to increase in gross margin estimates

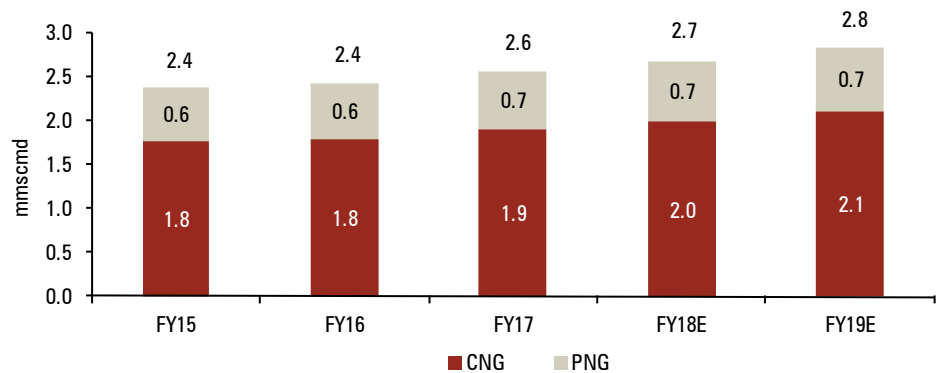
Source: Company, ICICIdirect.com Research

Company Analysis

Seasonality adversely impacts CNG volume growth

During the quarter, CNG volumes were at 1.88 mmscmd, up 1.4% YoY (in kg, volume was up 4.4% YoY) and below our estimate due to lower consumption that was impacted by the vacation season. Volume growth, going ahead, may be better given steady conversion rate of vehicles to CNG and MGL's plans to aggressively set up CNG stations with 20-25 additions in FY18E. On PNG front, volumes increased 6.7% YoY to 0.68 mmscmd largely in line with our estimates on account of growth in domestic and commercial sales volumes. It plans to add 1.4 lakh households in FY18E. MGL currently has 9.8 lakh domestic PNG, ~3100 commercial customers and ~70 industrial customers. Going forward, we estimate sales volumes at 2.7 mmscmd and 2.8 mmscmd in FY18E and FY19E, respectively.

Exhibit 1: Volume estimates

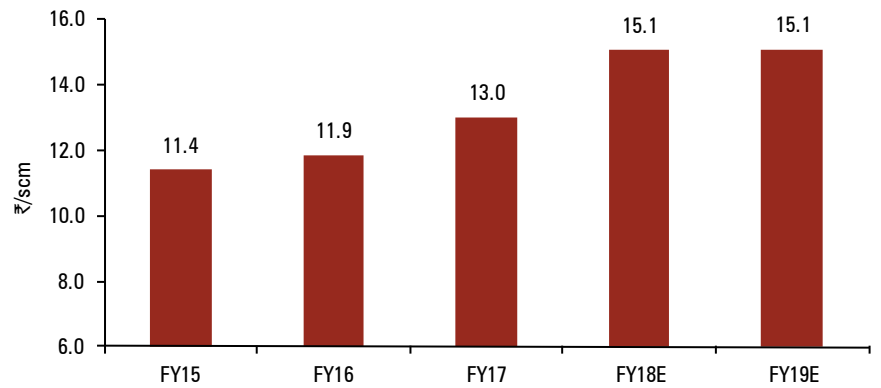


Source: Company, ICICIdirect.com Research

Strong margins, going forward

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Exhibit 2: Gross margins estimate

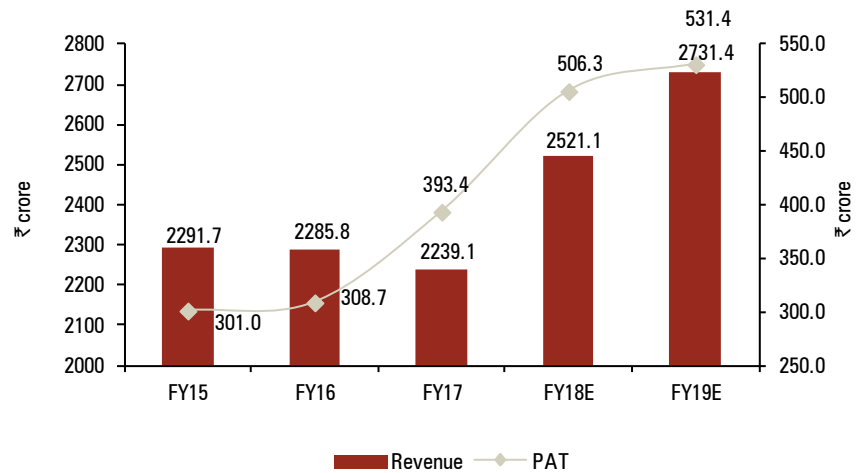


Source: Company, ICICIdirect.com Research

Robust profit growth for next two years

The revenue is expected to increase from ₹ 2239 crore in FY17 to ₹ 2731.4 crore in FY19E. PAT is expected to increase from ₹ 393.4 crore in FY17 to ₹ 531.4 crore in FY19E on account of strong margins.

Exhibit 3: Revenue and PAT trend



Source: Company, ICICIdirect.com Research

Outlook & Valuation

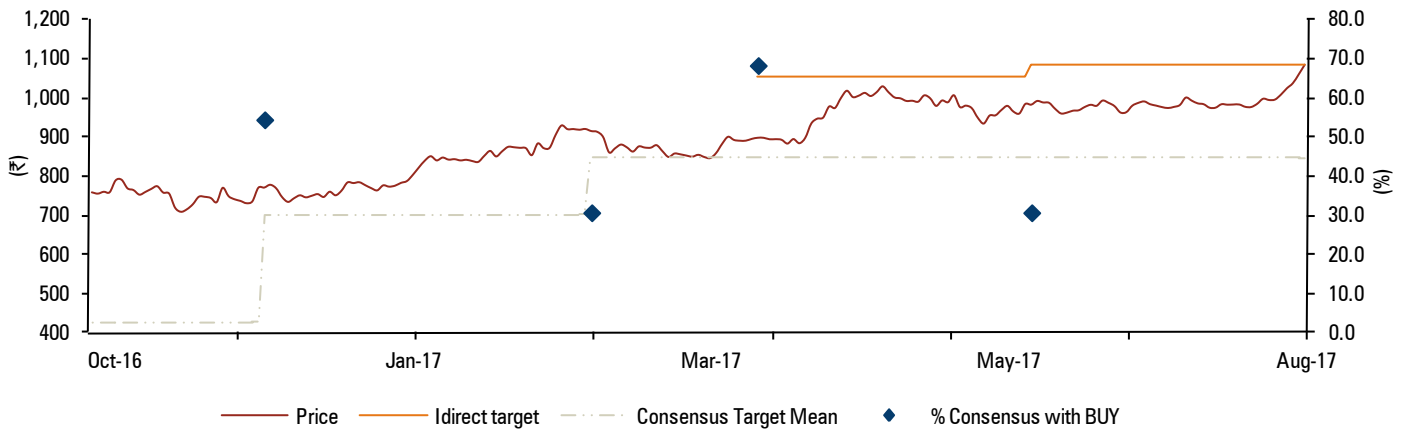
The CGD sector has benefited in a significant manner from the government's decision to prioritise the allocation of domestic natural gas for CNG and domestic PNG customers. This has enabled MGL to access cheaper gas for CNG and domestic business segments, constituting ~86% of total sales volume. MGL's strong gas pipeline infrastructure and expanding operations in Mumbai, its adjoining areas and Raigad district will enable MGL to capture the benefits of the large and growing market given the low penetration. The ongoing and upcoming bidding for new CGD areas also presents MGL with the scope to expand its business further. We value MGL at 22.5x FY19E EPS of ₹ 53.8 to arrive at a target price of ₹ 1210 with a **BUY** recommendation.

Exhibit 4: Valuations

Year	Sales (₹ Crore)	Sales Gr. (%)	EPS (₹)	EPS Gr. (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY16	2285.8	-0.3	34.6	2.6	28.5	16.9	20.2	27.8
FY17	2239.1	-2.0	39.8	15.3	24.8	14.8	23.1	32.3
FY18E	2521.1	12.6	51.3	28.7	19.2	11.4	25.9	36.9
FY19E	2731.4	8.3	53.8	5.0	18.3	10.8	24.0	33.7

Source: Company, ICICIdirect.com Research

Recommendation history vs. consensus estimate



Source: Bloomberg, Company, ICICIdirect.com Research

Key events

Date	Event
Jul-16	Mahanagar Gas Ltd (MGL) gets listed on BSE and NSE
Oct-16	Domestic Natural Gas Prices decline to US\$ 2.8/mmbtu from US\$ 3.4/mmbtu based on GCV
Oct-16	MGL reduces CNG and PNG prices due to reduction in domestic gas prices
Dec-16	MGL hikes CNG and PNG prices due to increase in input tax
Jan-17	MGL launches 100 scooters fuelled by CNG
Feb-17	MGL declares interim dividend of ₹ 8/share

Source: Company, ICICIdirect.com Research

Top 10 Shareholders

Rank	Investor Name	Latest Filing Date	% O/S	Position	Change (m)
1	Birla Sun Life Asset Management Company Ltd.	30-Jun-17	1.9	1.9	0.0
2	Goldman Sachs Asset Management International	30/Apr/17	1.2	1.2	0.0
3	Franklin Templeton Asset Management (India) Pvt. Ltd.	30-Jun-17	1.1	1.1	0.0
4	UTI Asset Management Co. Ltd.	30/Apr/17	1.0	1.0	0.0
5	Schroder Investment Management (Hong Kong) Ltd.	31-Mar-17	0.8	0.8	0.0
6	Amundi Hong Kong Limited	30/Apr/17	0.5	0.5	0.0
7	William Blair & Company, L.L.C.	28-Feb-17	0.5	0.5	0.2
8	Canara Robeco Asset Management Company Ltd.	31/May/17	0.4	0.4	0.0
9	Russell Investments Limited	31-Mar-17	0.4	0.3	0.0
10	Templeton Asset Management Ltd.	31/Mar/17	0.3	0.2	0.0

Source: Reuters, ICICIdirect.com Research

Shareholding Pattern

(in %)	Sep-16	Dec-16	Mar-17	Jun-17
Promoter	65.0	65.0	65.0	65.0
FII	9.8	11.3	9.8	9.9
DII	5.4	7.6	8.0	7.3
Others	19.8	16.1	17.2	17.8

Recent Activity

Investor name	Value (m)	Shares (m)	Investor name	Value (m)	Shares (m)
Första AP-Fonden	2.62	0.23	Mirae Asset Global Investments (India) Pvt. Ltd.	-6.88	-0.53
William Blair & Company, L.L.C.	2.83	0.22	Driehaus Capital Management, LLC	-3.07	-0.23
Pzena Investment Management, LLC	1.46	0.13	First State Investments (Singapore)	-1.09	-0.09
Canara Robeco Asset Management Company Ltd.	0.56	0.04	Sundaram Asset Management Company Limited	-1.04	-0.08
Mirae Asset Global Investments Co., Ltd.	0.38	0.03	CIBC Asset Management Inc.	-0.91	-0.07

Source: Reuters, ICICIdirect.com Research

Financial summary

Profit and loss statement		₹ Crore			
(Year-end March)	FY16	FY17	FY18E	FY19E	
Revenue	2,285.8	2,239.1	2,521.1	2,731.4	
Growth (%)	-0.3	-2.0	12.6	8.3	
Raw material Costs	1229.7	1018.4	1042.0	1159.7	
Employee Costs	53.7	60.0	72.5	79.7	
Other Expenditure	282.6	311.4	351.3	377.6	
Op. Expenditure	1772.8	1594.9	1695.2	1867.3	
EBITDA	513.0	644.2	825.9	864.0	
Growth (%)	4.7	25.6	28.2	4.6	
Depreciation	84.1	95.1	106.3	116.7	
EBIT	428.9	549.0	719.6	747.3	
Interest	3.0	1.0	1.1	0.0	
Other Income	42.7	52.7	55.0	64.0	
PBT	468.6	600.7	773.5	811.3	
Growth (%)	4.3	28.2	28.8	4.9	
Tax	160.0	207.2	267.3	279.9	
Reported PAT	308.7	393.4	506.3	531.4	
Growth (%)	2.6	27.5	28.7	5.0	
EPS	34.6	39.8	51.3	53.8	

Source: Company, ICICIdirect.com Research

Cash flow statement		₹ Crore			
(Year-end March)	FY16	FY17	FY18E	FY19E	
Profit after Tax	308.7	393.4	506.3	531.4	
Add: Depreciation	84.1	95.1	106.3	116.7	
Add: Others	15.4	15.0	15.0	15.0	
Cash Profit	408.2	503.6	627.6	663.1	
Increase/(Decrease) in CL	56.6	57.4	111.7	60.6	
(Increase)/Decrease in CA	-2.0	-9.5	-25.1	-19.1	
CF from Operating Activities	462.8	551.4	714.2	704.6	
Purchase of Fixed Assets	228.9	235.1	298.7	296.0	
(Inc)/Dec in Investments	-16.7	-40.0	-40.0	-40.0	
Others	0.0	0.0	0.0	0.0	
CF from Investing Activities	-245.7	-275.1	-338.7	-336.0	
Inc/(Dec) in Loan Funds	-1.8	-11.4	-2.4	0.0	
Inc/(Dec) in Sh. Cap. & Res.	0.0	9.4	0.0	0.0	
Less: Dividend Paid	188.2	231.1	254.3	265.8	
Others	0.0	0.0	0.0	0.0	
CF from financing activities	-189.9	-233.1	-256.6	-265.8	
Change in cash Eq.	27.2	43.1	118.8	102.8	
Op. Cash and cash Eq.	144.9	172.1	215.2	334.1	
Cl. Cash and cash Eq.	172.1	215.2	334.1	436.9	

Source: Company, ICICIdirect.com Research

Balance sheet		₹ Crore			
(Year-end March)	FY16	FY17	FY18E	FY19E	
Source of Funds					
Equity Capital	89.3	98.8	98.8	98.8	
Preference capital	0.0	0.0	0.0	0.0	
Reserves & Surplus	1,438.6	1,600.9	1,852.9	2,118.5	
Shareholder's Fund	1,528.0	1,699.7	1,951.7	2,217.3	
Loan Funds	13.8	2.4	0.0	0.0	
Deferred Tax Liability	118.1	133.1	148.1	163.1	
Minority Interest	1.0	2.0	2.0	2.0	
Source of Funds	1,659.9	1,835.2	2,099.8	2,380.4	
Application of Funds					
Gross Block	1,845.0	2,095.0	2,370.0	2,645.0	
Less: Acc. Depreciation	685.4	780.4	887.9	1,008.7	
Net Block	1,159.6	1,314.6	1,482.1	1,636.3	
Capital WIP	428.9	413.9	438.9	463.9	
Total Fixed Assets	1,588.5	1,728.5	1,920.9	2,100.2	
Investments	388.2	428.2	468.2	508.2	
Inventories	18.0	18.4	20.7	22.4	
Debtor	89.3	98.2	110.5	119.7	
Cash	172.1	215.2	334.1	436.9	
Loan & Advance, Other CA	100.3	100.5	110.9	119.0	
Total Current assets	379.6	432.3	576.2	698.1	
Current Liabilities	492.8	490.8	552.6	598.7	
Provisions	203.6	263.0	312.9	327.4	
Total CL and Provisions	696.4	753.8	865.5	926.1	
Net Working Capital	-316.8	-321.5	-289.3	-228.0	
Miscellaneous expense	0.0	0.0	0.0	0.0	
Application of Funds	1,659.9	1,835.2	2,099.8	2,380.4	

Source: Company, ICICIdirect.com Research

Key ratios					
(Year-end March)	FY16	FY17	FY18E	FY19E	
Per share data (₹)					
Book Value	171.0	172.1	197.6	224.5	
Cash per share	62.7	65.1	81.2	95.7	
EPS	34.6	39.8	51.3	53.8	
Cash EPS	44.0	49.5	62.0	65.6	
DPS	17.5	20.0	22.0	23.0	
Profitability & Operating Ratios					
EBITDA Margin (%)	22.4	28.8	32.8	31.6	
PAT Margin (%)	13.5	17.6	20.1	19.5	
Fixed Asset Turnover (x)	1.4	1.3	1.3	1.3	
Inventory Turnover (Days)	2.9	3.0	3.0	3.0	
Debtor (Days)	14.3	16.0	16.0	16.0	
Current Liabilities (Days)	78.7	80.0	80.0	80.0	
Return Ratios (%)					
RoE	20.2	23.1	25.9	24.0	
RoCE	27.8	32.3	36.9	33.7	
RoIC	43.7	51.9	62.6	58.7	
Valuation Ratios (x)					
PE	28.5	24.8	19.2	18.3	
Price to Book Value	5.8	5.7	5.0	4.4	
EV/EBITDA	16.9	14.8	11.4	10.8	
EV/Sales	3.8	4.3	3.7	3.4	
Leverage & Solvency Ratios					
Debt to equity (x)	0.0	0.0	0.0	0.0	
Interest Coverage (x)	145.4	533.0	658.7	NA	
Debt to EBITDA (x)	0.0	0.0	0.0	0.0	
Current Ratio	0.5	0.6	0.7	0.8	
Quick ratio	0.5	0.5	0.6	0.7	

Source: Company, ICICIdirect.com Research

ICICIdirect.com coverage universe (Oil & Gas)

Sector / Company	CMP			M Cap (₹ Cr)	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
	(₹)	TP(₹)	Rating		FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E
Bharat Petroleum (BHAPET)	466	473	Hold	50,543	37.1	34.2	39.2	12.6	13.6	11.9	10.4	9.4	8.2	20.3	20.9	21.3	28.1	24.9	26.9
Castrol India (CASIND)	394	475	Buy	23,492	13.6	14.1	14.4	28.9	28.0	27.4	18.6	18.4	18.0	161.1	183.5	182.1	113.3	130.9	129.7
GAIL (India) (GAIL)	377	460	Buy	63,761	20.7	26.7	28.7	19.5	14.1	13.1	11.0	9.4	9.1	13.8	15.3	14.7	10.6	12.5	12.4
Gujarat Gas (GUJGAS)	750	805	Hold	10,326	16.2	36.3	44.8	46.3	20.7	16.7	16.9	11.0	9.2	10.5	17.2	19.3	9.8	18.7	19.6
Gujarat State Petronet (GSPL)	180	175	Hold	10,140	8.8	11.2	12.6	20.4	16.0	14.3	12.3	9.8	8.8	13.7	16.7	17.5	11.4	13.1	13.2
Gulf Oil Lubricants (GULO)	816	827	Hold	4,045	24.4	26.3	29.5	33.4	31.0	27.7	21.9	20.3	17.5	32.5	32.5	33.9	34.2	30.4	28.4
Hindustan Petroleum (HINPET)	432	425	Hold	65,904	13.6	11.3	12.4	10.6	12.8	11.7	7.8	9.2	8.4	20.9	14.7	15.7	32.6	24.0	23.5
Indraprastha Gas (INDGAS)	1,215	1,140	Buy	17,010	40.8	43.8	45.5	29.8	27.7	26.7	16.7	14.8	13.8	27.7	25.4	22.7	19.9	18.3	16.6
Mahanagar Gas Ltd (MAHGAS)	986	1,210	Buy	9,740	39.8	51.3	53.8	24.8	19.2	18.3	14.8	11.4	10.8	32.3	36.9	33.7	23.1	25.9	24.0
Mangalore Refinery (MRPL)	130	150	Buy	22,785	20.8	11.0	14.3	6.3	11.8	9.1	4.2	3.6	3.2	26.0	18.8	23.7	41.2	19.4	21.7
Petronet LNG (PETLNG)	206	240	Buy	30,450	6.1	11.4	14.8	17.9	15.8	13.7	NA	NA	NA	23.7	29.4	34.8	24.3	25.3	26.5

Source: Company, ICICIdirect.com Research

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