

28 October 2023

India | Equity Research | Q2FY24 result review

## Mahanagar Gas

Oil &amp; Gas

### Margins hit new highs; volume ramp-up to strengthen earnings

Mahanagar Gas (MGL)'s Q2FY24 EBITDA/PAT at INR 4.8/3.4bn missed our estimates of INR 5bn/3.5bn, but the company delivered a second successive quarter of strong YoY growth with EBITDA/PAT up 89/106% YoY. Volume growth of just 3.4% was muted, but INR 6.6/scm jump YoY in EBITDA/scm was enough to drive the earnings strength in the quarter. Margins have jumped due to a combination of lower gas costs (down INR 8.7/scm YoY) and a relatively lower dip in realisations (down INR 1.4/scm YoY). We see further improvement in volume and margin in FY24E with the acquisition of Unison comprising 3GAs (Ratnagiri, Chitradurga & Devangere, and Latur & Osmanabad districts), new pricing policy and a moderate gas price environment. FY24/25E EPS estimates see a second successive upgrade post-Q1 upgrades (albeit smaller), due to stronger margin assumptions. Reiterate **BUY**.

### Volume growth slows; margins accelerate sharply

Volumes of 3.57mmcmd (vs. l-sec 3.55mmcmd) were up 3.4% YoY/~4.8% QoQ post a muted 1% YoY decline seen in Q1FY24. CNG volumes of 2.6mmcmd (up 1.6%/4% YoY/QoQ), domestic volumes of 0.5mmcmd (+4.3% YoY/-1% QoQ) and I/C volumes of 0.5mms cmd (+12/15% YoY/QoQ) were in line to our estimates. The plan of Maharashtra State Transport (MSRTC) to add ~800 new buses, higher conversion run rates of CNG and stronger price competitiveness versus alternate fuels should drive stronger volume growth going forward. We continue to factor in 5–6% volume growth for MGL over the medium term, and marginally raise FY24E volume to factor in the small beat versus Q2 estimates.

### Margin strength continues unabated

Post the lows seen in Q3FY22 of gross margins of INR 8.4/scm and EBITDA/scm of INR 3.4, MGL has been gradually improving its margins and maintaining its peer-leading status. Q2 has seen gross margins and EBITDA/scm moderate from the record levels seen in Q1 but gross margins of INR 20.2/scm and EBITDA/scm of INR 14.6/scm have remained well above historical averages and also Q2FY23 levels. We expect some moderation in margins for the rest of FY24E, given our assumptions of USD 2–3/MMbtu increase in spot LNG prices and higher proportion needed to fill additional demand, but annualised margins are still likely to touch all-time highs, supporting earnings.

### Financial Summary

Y/E March (INR Mn)	FY23A	FY24E	FY25E	FY26E
Net Revenue	62,773	61,073	63,840	68,764
EBITDA	11,842	18,211	18,696	19,540
EBITDA %	18.9	29.8	29.3	28.4
Net Profit	7,901	12,626	12,920	13,568
EPS (INR)	80.0	127.8	130.8	137.4
EPS % Chg YoY	32.4	59.8	2.3	5.0
P/E (x)	12.4	7.7	7.6	7.2
EV/EBITDA (x)	6.9	4.0	3.6	3.1
RoCE (Pre-tax) (%)	24.7	33.9	29.1	26.0
RoE (%)	20.4	28.0	24.5	22.3

#### Probal Sen

probal.sen@icicisecurities.com  
+91 22 6807 7274

#### Hardik Solanki

solanki.hardik@icicisecurities.com

#### Market Data

Market Cap (INR)	98bn
Market Cap (USD)	1,173mn
Bloomberg Code	MAHGL IN
Reuters Code	MGAS BO
52-week Range (INR)	1,152 /811
Free Float (%)	58.0
ADTV-3M (mn) (USD)	8.6

Price Performance (%)	3m	6m	12m
Absolute	(7.9)	(0.2)	16.9
Relative to Sensex	(4.4)	(6.5)	8.7

ESG Disclosure	2021	2022	Change
ESG score	-	32.3	-
Environment	-	13.7	-
Social	-	19.5	-
Governance	-	63.6	-

Note - Score ranges from 0 - 100 with a higher score indicating higher ESG disclosures.

Source: Bloomberg, l-sec research

Earnings Revisions (%)	FY24E	FY25E
Revenue	(1.4)	2.6
EBITDA	4.6	1.3
EPS	4.7	1.9

#### Previous Reports

05-08-2023: [Q1FY24 result review](#)

29-06-2023: [Company update](#)

### Small upgrade in earnings; reiterate BUY

We have adjusted our estimates of volumes and margins to take cognisance of the H1FY24 performance and also to factor in the sustained softness in spot LNG prices as well as the strength seen in sales realisation. Despite our assumptions of a lower margin trajectory for H2FY24, average gross margin of INR 19.3/scm is expected to be the highest the company has achieved and so will EBITDA/scm levels of INR 13.9/scm. Led by the tweaks to volumes (revised up by 0.1-0.13bps for both years) and higher margins (raised by INR 0.5/scm for FY24E), FY24/25E EPS has been revised up by ~4.7/2% respectively. TP raised marginally to INR 1,350 (from INR 1345), with higher earnings growth offset by a lower terminal growth rate assumption to factor in the imminent EV threat. Reiterate BUY.

**Key downside risks:** i) Higher gas prices. ii) Inability to pass on gas cost increases. iii) Sharper fall in alternate fuel prices for CNG (petrol/diesel).

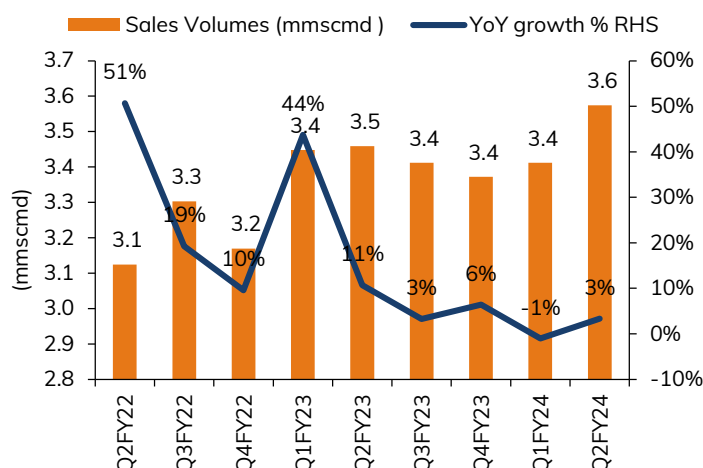
**Key upside risks:** i) Softer LNG prices. ii) Faster execution of new area development. iii) Aggressive regulatory support in the MMR region.

### Exhibit 1: Q2FY24 result snapshot

INR mn	Q2FY24	Q2FY23	YoY (%)	Q1FY24	qoq %	H1FY24	H2FY23	yoy (%)
Sales	15,651	15,581	0.4	15,332	2.1	30,984	30,083	3.0
EBITDA	4,789	2,528	89.4	5,213	(8.1)	10,002	5,384	85.8
Adj. PAT	3,385	1,640	106.4	3,684	(8.1)	7,069	3,492	102.5
EPS (INR)	34.3	16.6	106.4	37.3	(8.1)	71.6	35.3	102.5
Depreciation	658	551	19.4	620	6.0	1,278	1,088	17.5
Sales (mmscm)	329	318	3.4	310	5.9	639	632	1.2
Sales (mmscmd)	3.6	3.5	3.4	3.4	4.8	3.5	3.5	1.2
CNG sales (mmscm)	238	234	1.6	226	5.2	463	465	(0.3)
PNG sales (mmscm)	91	84	8.1	85	7.8	176	167	5.3
Gross margin (INR/scm)	20.2	12.9	56.9	22.2	(8.8)	21.2	13.6	56.3
EBITDA margin (INR/scm)	14.6	7.9	83.2	16.8	(13.3)	15.6	8.5	83.6
EBITDA Margin (%)	30.6%	16.2%		34.0%		32.3%	17.9%	80.4
CNG sales (INR mn)	11,277	10,941	3.1	11,080	1.8	22,357	20,715	7.9
CNG realisations (INR/scm)	47.5	46.8	1.4	49.1	(3.3)	48.2	44.6	8.3
PNG sales (INR mn)	4,375	4,640	(5.7)	4,252	2.9	8,627	9,369	(7.9)
PNG realisations (INR/scm)	47.9	55.0	(12.8)	50.2	(4.5)	49.0	56.1	(12.6)
Gross margin (INR Mn)	6,659	4,106	62.2	6,891	(3.4)	13,550	8,569	58.1

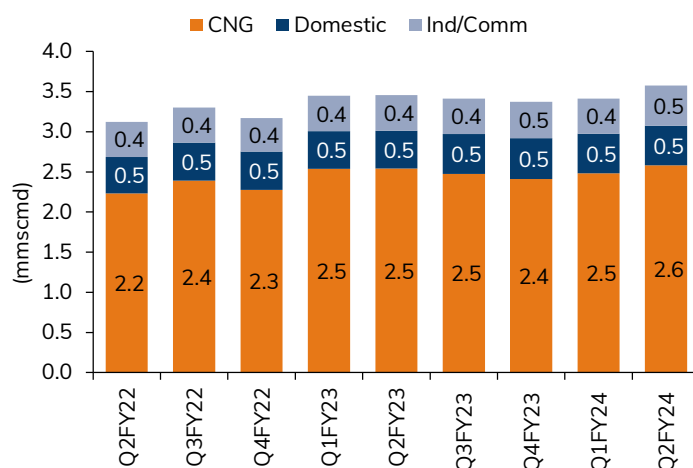
Source: Company data, I-Sec research

### Exhibit 2: Volume growth remains muted YoY

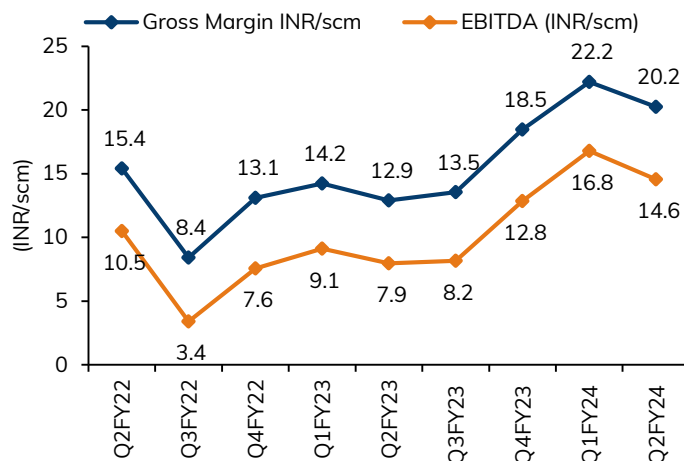


Source: Company data, I-Sec research

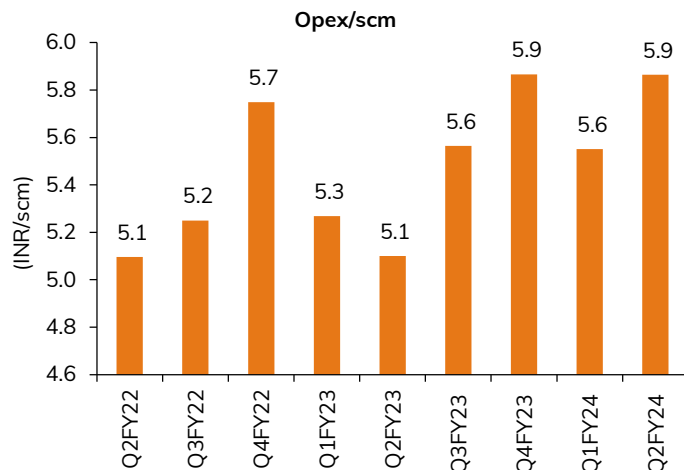
### Exhibit 3: Segment-wise volume trends



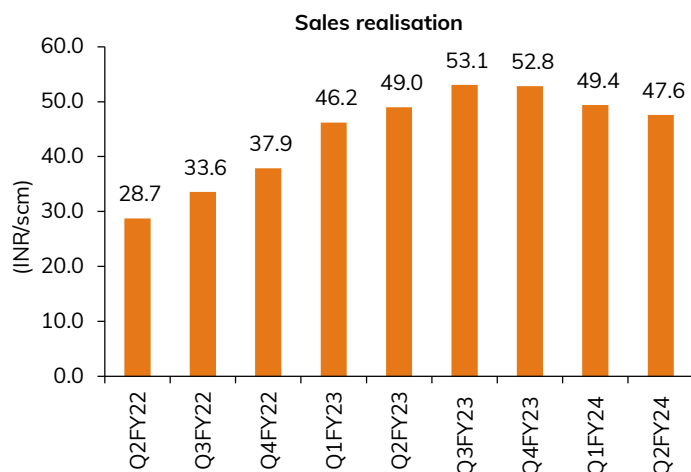
Source: Company data, I-Sec research

**Exhibit 4: Margins remain strong in Q2FY24**

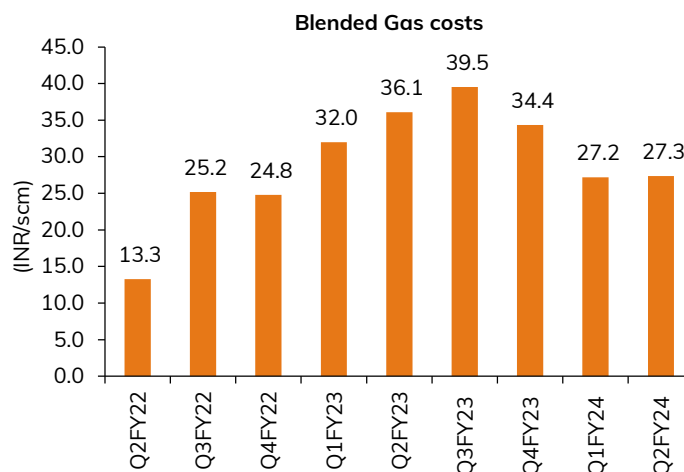
Source: Company data, I-Sec research

**Exhibit 5: Opex/scm increased sharply QoQ and YoY**

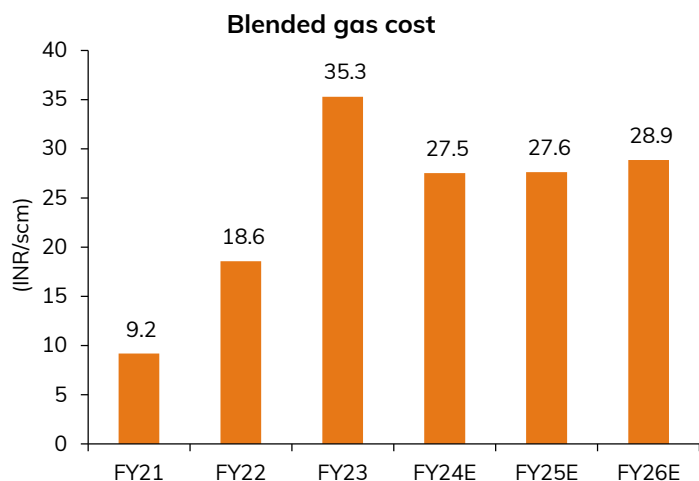
Source: Company data, I-Sec research

**Exhibit 6: Sales realisations have decreased QoQ...**

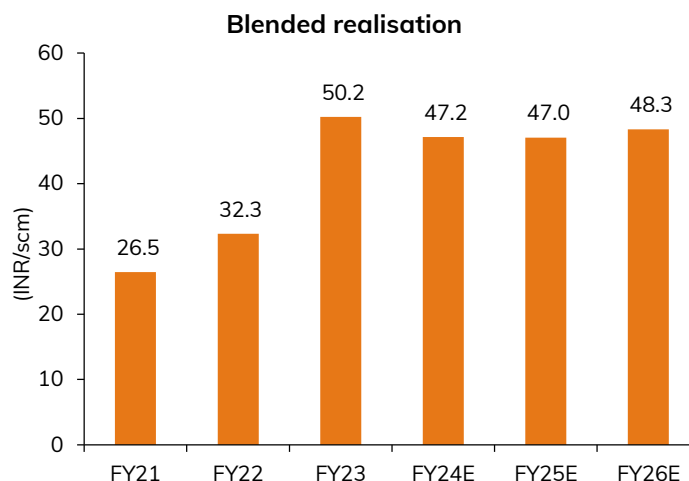
Source: Company data, I-Sec research

**Exhibit 7: ...but, gas costs was flattish QoQ**

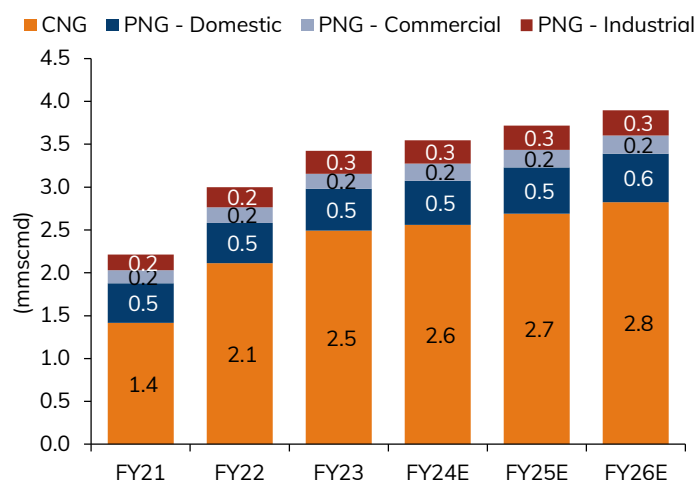
Source: Company data, I-Sec research

**Exhibit 8: MGL's gas cost likely to slip sharply in FY24**

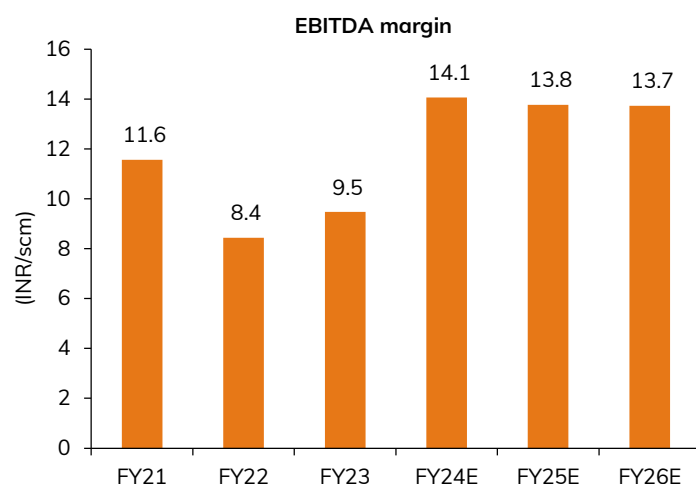
Source: Company data, I-Sec research

**Exhibit 9: Blended realisation to keep pace**

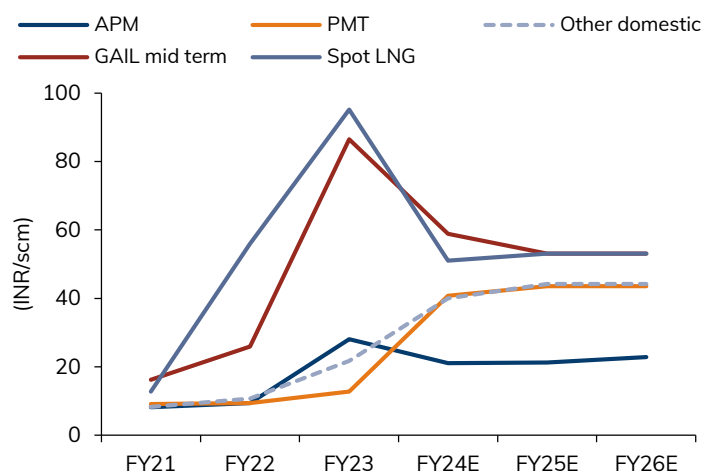
Source: Company data, I-Sec research

**Exhibit 10: Volume growth to be subject to pricing balance**

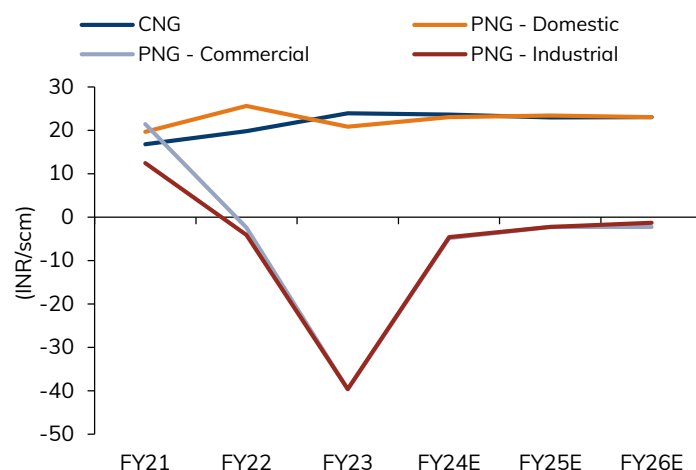
Source: Company data, I-Sec research

**Exhibit 11: Margin strength to improve in FY23-FY26E**

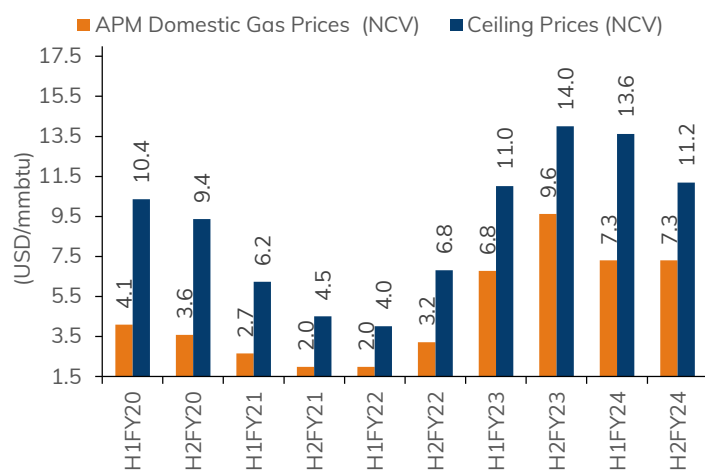
Source: Company data, I-Sec research

**Exhibit 12: Sourcing costs likely to decline in FY24-FY26E**

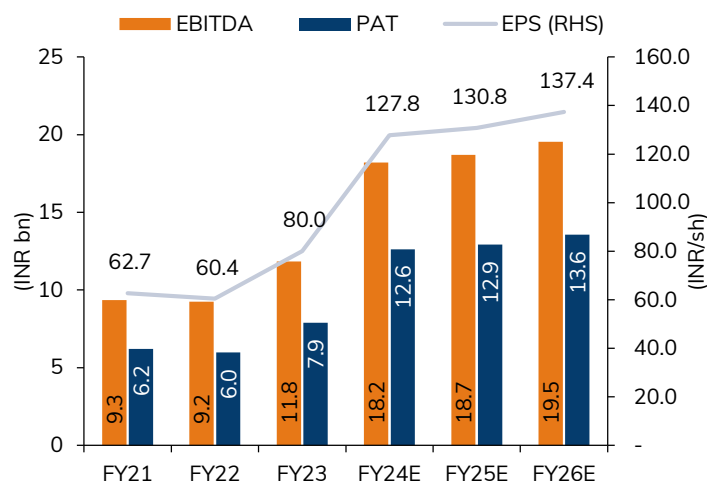
Source: Company data, I-Sec research

**Exhibit 13: Segment-wise margins to see divergence**

Source: Company data, I-Sec research

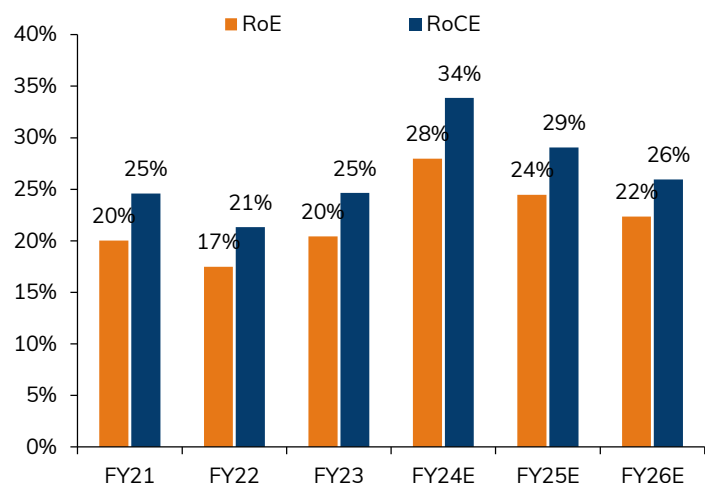
**Exhibit 14: APM gas prices capped with revised gas pricing policy and HPHT reduced by 18% vs. H1FY24**

Source: Company data, I-Sec research

**Exhibit 15: EBITDA and EPS CAGRs at 18-20% over FY23-FY26E**

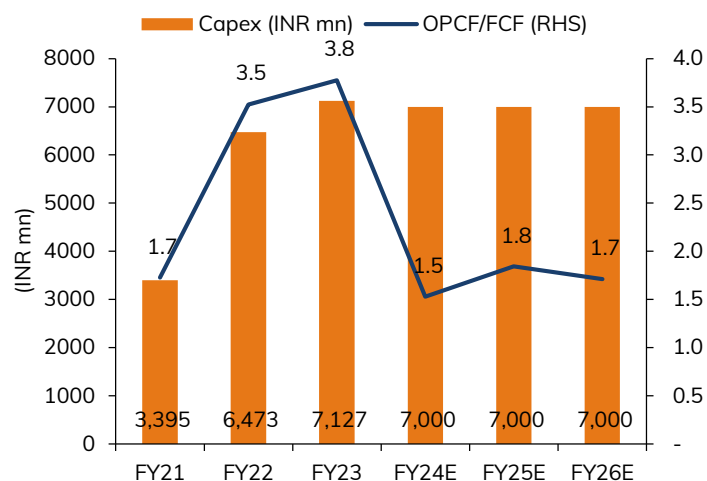
Source: Company data, I-Sec research

Exhibit 16: Return ratios to remain stable



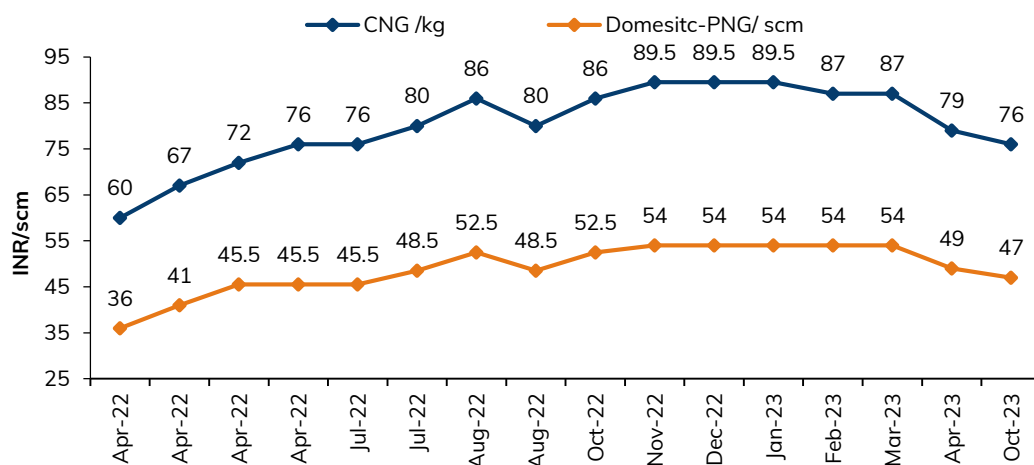
Source: Company data, I-Sec research

Exhibit 17: Capex of INR 21bn estimated over FY24-FY26E



Source: Company data, I-Sec research

Exhibit 18: MGL's price trends for CNG and domestic PNG



Source: Company data, I-Sec research

## Valuations: Target price of INR 1,350 implies ~37% upside

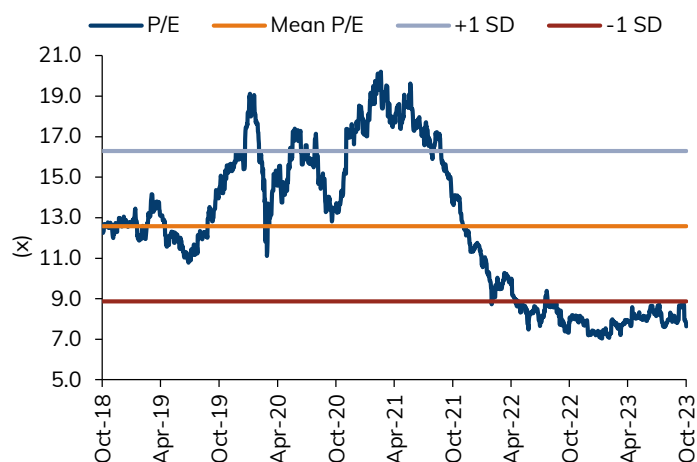
We value MGL on DCF methodology, using a WACC of 10.9%, DER of 35%, long-term EBITDA assumption of INR 12/scm and terminal growth rate of 1.6%. In the long term, we build in muted volume growth beyond FY26E as well as flattish margins, given our caution around longer-term growth expectations. Our DCF value delivers a target price of INR 1,350, ~37% upside from CMP. Maintain **BUY**.

### Exhibit 19: 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	1.6%
Total NPV potential INR mn	1,26,730
TP MGLStandalone (INR.sh)	1,283
UEPL (INR.sh)	67
TP (INR.sh)	1,350
CMP (INR.sh)	988
Upside/(downside)	37%

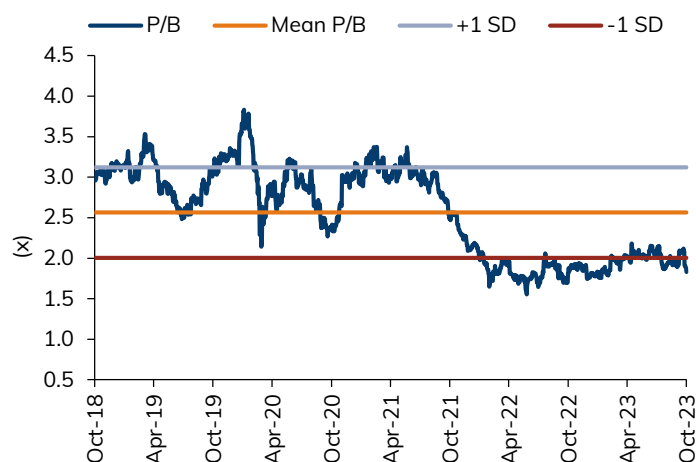
Source: Company data, I-Sec research

### Exhibit 20: MGL's P/E trading well below 5-year bands



Source: Company data, I-Sec research

### Exhibit 21: MGL's P/B trading well below 5-year bands



Source: Company data, I-Sec research

### Exhibit 22: Shareholding pattern

%	Mar'23	Jun'23	Sep'23
Promoters	32.5	32.5	32.5
Institutional investors	45.9	47.5	46.6
MFs and other	1.8	2.2	1.7
FIs/ Banks	-	-	-
Insurance Cos.	13.1	12.5	13.8
FII	31.0	32.8	31.1
Others	21.6	20.0	20.9

Source: Bloomberg, I-Sec research

### Exhibit 23: Price chart



Source: Bloomberg, I-Sec research

## Financial Summary

### Exhibit 24: Profit & Loss

(INR Mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
<b>Net Sales</b>	<b>62,773</b>	<b>61,073</b>	<b>63,840</b>	<b>68,764</b>
<b>EBITDA</b>	<b>11,842</b>	<b>18,211</b>	<b>18,696</b>	<b>19,540</b>
EBITDA Margin (%)	18.9	29.8	29.3	28.4
Depreciation & Amortization	2,311	2,930	3,350	3,770
EBIT	9,531	15,281	15,346	15,770
Interest expenditure	94	50	50	50
Other Non-operating Income	1,119	1,637	1,965	2,407
<b>PBT</b>	<b>10,556</b>	<b>16,868</b>	<b>17,261</b>	<b>18,127</b>
<b>Profit / (Loss) from Associates</b>	-	-	-	-
Less: Taxes	2,655	4,243	4,341	4,559
PAT	7,901	12,626	12,920	13,568
Less: Minority Interest	-	-	-	-
<b>Net Income (Reported)</b>	<b>7,901</b>	<b>12,626</b>	<b>12,920</b>	<b>13,568</b>
Extraordinaries (Net)	-	-	-	-
<b>Recurring Net Income</b>	<b>7,901</b>	<b>12,626</b>	<b>12,920</b>	<b>13,568</b>

Source Company data, I-Sec research

### Exhibit 25: Balance sheet

(INR Mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
Total Current Assets	6,964	14,346	18,057	23,451
of which cash & bank	2,279	10,775	14,385	19,595
Total Current Liabilities & Provisions	15,612	20,798	21,848	23,916
<b>Net Current Assets</b>	<b>(8,648)</b>	<b>(6,452)</b>	<b>(3,791)</b>	<b>(465)</b>
Other Non Current Assets	2,918	2,918	2,918	2,918
Net Fixed Assets	30,257	34,327	37,977	41,207
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>52,287</b>	<b>60,039</b>	<b>68,179</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	47,930	55,682	63,822
<b>Total Net Worth</b>	<b>41,342</b>	<b>48,918</b>	<b>56,669</b>	<b>64,810</b>
Minority Interest	-	-	-	-
<b>Total Liabilities</b>	<b>44,711</b>	<b>52,287</b>	<b>60,039</b>	<b>68,179</b>

Source Company data, I-Sec research

### Exhibit 26: Quarterly trend

(INR mn, year ending March)

	Dec-22	Mar-23	Jun-23	Sept-23
Net Sales	16,658	16,031	15,332	15,651
% growth (YOY)	6.9%	-3.8%	-4.4%	2.1%
EBITDA	2,561	3,897	5,213	4,789
Margin %	15.4%	24.3%	34.0%	30.6%
Other Income	323	336	390	437
Extraordinaries	-	-	-	-
<b>Adjusted Net Profit</b>	<b>1,721</b>	<b>2,688</b>	<b>3,684</b>	<b>3,385</b>

Source Company data, I-Sec research

### Exhibit 27: 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>18,211</b>	<b>18,696</b>	<b>19,540</b>
Working Capital Changes	134	6,300	950	1,884
Tax	(2,638)	(4,243)	(4,341)	(4,559)
<b>Operating Cashflow</b>	<b>9,693</b>	<b>20,269</b>	<b>15,304</b>	<b>16,864</b>
Capital Commitments	(7,127)	(7,000)	(7,000)	(7,000)
<b>Free Cashflow</b>	<b>2,566</b>	<b>13,269</b>	<b>8,304</b>	<b>9,864</b>
Others CFI	(2,092)	327	524	822
<b>Cashflow from Investing Activities</b>	<b>(9,218)</b>	<b>(6,673)</b>	<b>(6,476)</b>	<b>(6,178)</b>
Inc (Dec) in Borrowings	-	-	-	-
Interest Cost	-	(50)	(50)	(50)
Others	(2,848)	(5,050)	(5,168)	(5,427)
<b>Cash flow from Financing Activities</b>	<b>(2,848)</b>	<b>(5,100)</b>	<b>(5,218)</b>	<b>(5,477)</b>
<b>Chg. in Cash &amp; Bank balance</b>	<b>(2,373)</b>	<b>8,496</b>	<b>3,611</b>	<b>5,209</b>
Closing cash & balance	2,279	10,775	14,385	19,595

Source Company data, I-Sec research

### Exhibit 28: Key ratios

(Year ending March)

	FY23A	FY24E	FY25E	FY26E
<b>Per Share Data (INR)</b>				
Recurring EPS	80.0	127.8	130.8	137.4
Diluted EPS	80.0	127.8	130.8	137.4
Recurring Cash EPS	103.4	157.5	164.7	175.5
Dividend per share (DPS)	26.0	51.1	52.3	54.9
Book Value per share (BV)	418.5	495.2	573.7	656.1
Dividend Payout (%)	32.5	40.0	40.0	40.0
<b>Growth (%)</b>				
Net Sales	77.5	(2.7)	4.5	7.7
EBITDA	28.1	53.8	2.7	4.5
EPS	32.4	59.8	2.3	5.0
<b>Valuation Ratios (x)</b>				
P/E	12.4	7.7	7.6	7.2
P/CEPS	9.6	6.3	6.0	5.6
P/BV	2.4	2.0	1.7	1.5
EV / EBITDA	6.9	4.0	3.6	3.1
EV / Operating Income	7.7	4.3	3.9	3.3
Dividend Yield (%)	2.6	5.2	5.3	5.6
<b>Operating Ratios</b>				
EBITDA Margins (%)	18.9	29.8	29.3	28.4
Effective Tax Rate (%)	25.2	25.2	25.2	25.2
Net Profit Margins (%)	12.6	20.7	20.2	19.7
NWC / Total Assets (%)	(19.3)	(12.3)	(6.3)	(0.7)
Fixed Asset Turnover (x)	1.6	1.4	1.2	1.2
Working Capital Days	(0.6)	(11.3)	(51.6)	(51.7)
Net Debt / Equity %	(37.2)	(51.5)	(53.4)	(57.1)
<b>Profitability Ratios</b>				
RoCE (%)	18.5	25.3	21.8	19.4
RoCE (Pre-tax) (%)	24.7	33.9	29.1	26.0
RoE (%)	20.4	28.0	24.5	22.3

Source Company data, I-Sec research



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Name of the Compliance officer (Research Analyst): Mr. Atul Agrawal, Contact number: 022-40701000, **E-mail Address** : [complianceofficer@icicisecurities.com](mailto:complianceofficer@icicisecurities.com)

For any queries or grievances: [Mr. Prabodh Avadhoot](#) Email address: [headservicequality@icicidirect.com](mailto:headservicequality@icicidirect.com) Contact Number: 18601231122

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