

MGL is one the largest city gas distribution ("CGD") companies in India. It has more than 20 years of experience in supplying natural gas in Mumbai and are presently the sole authorized distributor of compressed natural gas ("CNG") and piped natural gas ("PNG") in Mumbai; its adjoining areas and the Raigad district in the state of Maharashtra, India. MGL is promoted by GAIL and BGAPH (now Royal Dutch Shell plc), each of who holds 45% of its equity shares.

Investment Rationale and Recommendation

At the upper end of the price band of Rs. 421, the IPO is valued at 13.4x at FY16 Post issue P/E which is at a significant discount to its immediate peers. With due consideration to factors like a) monopoly status in CGD business in Mumbai, b) significant entry barriers for competitors to enter into MGL area of operation, such as its infrastructure exclusivity, the requirement of large investments to establish a natural gas distribution network, lead time in the allocation of domestic natural gas and obtaining the required regulatory approvals, c) infrastructure exclusivity and established infrastructure network; d) cost effective availability of domestic natural gas, e) MGL being closer to the source of production of natural gas in the Mumbai offshore basin, as well as to the import terminals, Dahej, Hazira and Dabhol offers it a distinct price advantage and lower transportation tariff compared to other CGD companies, f) with rising crude oil prices, CNG's cost effectiveness versus competing fuels like Petrol and Diesel has improved, g) debt free balance sheet, h) strong execution track record, i) positive operating cashflows, j) decent RoE, k) cheaply valued against peers like Indraprastha Gas (P/E - 17x) and Gujarat Gas (P/E - 45x), we recommend investors to "SUBSCRIBE the issue for listing gains".

Company Background

MGL distributes CNG for use in motor vehicles and PNG for domestic household use as well as for commercial and industrial use. As at March 31, 2016, MGL supplied CNG to over 0.47 mn vehicles through its network of 188 CNG filling stations and provided PNG connection to ~0.86 mn domestic households, over 2,866 commercial and 60 industrial consumers in Mumbai and its Adjoining areas.

For Fiscal 2016, MGL's CNG and PNG businesses accounted for 74.21% and 25.79%, respectively, of the total volume of natural gas sold, and 71.05% and 28.95%, respectively, of its total gas sales revenue. MGL operates in Mumbai, the second largest city in India and one of the most populous cities in the world. There were ~6.7 mn motor vehicles in Mumbai, Thane region and Panvel region and has grown at a CAGR of 13.75% in Mar 2016 from Mar 2009. As per the MoPNG Guidelines, MGL has access to cost effective domestic natural gas equal to 110% of its CNG and domestic PNG requirements (such customers are classified under the "Priority Sector". This domestic natural gas is sold to MGL at US\$3.06/MMBTU (GCV), which is significant lower than the current market price of imported natural gas, for supply exclusively to the Priority sector. MGL's priority sector sales accounted for 84.14%, 85.03% and 85.58% of its total sales volume in Fiscal 2014, 2015 and 2016 respectively. The company's volumes witnessed a CAGR of 6.7% over FY11-16. Revenues and PAT have registered at a CAGR of 14.4% and 6.5%, respectively, in FY11-16. For its industrial and commercial PNG consumers, MGL sources regasified liquefied natural gas ("RLNG") from a number of sources, both on term and spot basis. The price at which MGL sells natural gas to its customers is not regulated and it is generally able to

Issue date	June 21 - June 23, 2016
Issue size	Rs. 10,394.4 mn. at upper end of the price band
Type of issue	Offer for sale: 24,694,500 Equity Shares by the Selling Shareholders
Face Value	Rs. 10
Price Band	Rs. 380 – 421 per share
Lot size	35 equity Shares & multiple of 35 equity shares thereafter
Issue structure	QIB: 50%, Retail: 35% Non – Institutional: 15%
Post issue market cap	Rs. 37.6 bn at upper price band
Book Running Lead Managers	Kotak, Citigroup Global Markets
Registrar to the issue	Karvy Computershare Pvt. Ltd.

Y/e 31 Mar (Rs. mn)	FY16	FY15	FY14	FY13
Net Sales	20,789	20,949	18,852	15144
EBITDA	5,130	4,897	4,882	4,827
OPM (%)	24.6	23.4	25.9	31.9
PAT	3,088	3,010	2,972	2,985
PAT (%)	14.8	14.4	15.8	19.7
Equity Capital	893.42	893.42	893.42	893.4
Diluted EPS (Rs.)	31.36	30.54	30.15	30.28
Networth (Rs. mn)	15,280	14,075	12,970	11826
Book Value (Rs.)	171	158	145	132
P/E (x)	13	14	13.9	13.9
P/BV(x)	2.5	1.7	2.9	3.2
RoE (%)	20.2	21.4	22.9	25.2

Source: RHP, Ajcon Research

pass on an increase in the cost of natural gas to its customers. MGL distributes natural gas through an extensive CGD network of pipelines, for which it has the exclusive authorisation to lay, build, expand and operate the CGD network in accordance with the Petroleum and Natural Gas Regulatory Board (Exclusivity for City or Local Natural Gas Distribution Network) Regulations, 2008 (the "PNGRB Regulations") in Mumbai until 2020, its Adjoining Areas until 2030 and the Raigad district until 2040. As on Mar 31, 2016, MGL had a supply network of over 4,646 kms of pipelines, including approximately 4,231 kms of polyethylene pipeline and 415 kms of steel pipeline, and 180 CNG filling stations.



Objects of the issue

Offer for sale – Upto Equity shares

Offer for sale by	Shares upto
GAIL (India) Ltd.	12,347,250
BG Asia Pacific Holdings PTE Ltd. (now acquired by Royal Dutch Shell plc)	12,347,250

Source: RHP

Concerns

- 1) A large part of CNG sold by MGL is on the network of oil marketing companies. MGL currently pays Rs 2.74 per kg to the latter for using their CNG filling stations. In case its exclusivity period ends, MGL could face competition and might have to make higher payments to these companies which are not the case with its peers.
- 2) The Company's plans to venture and scale up operations in other cities will affect ROEs to some extent as cashflows would be used to fund capital expenditure



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