

**BUY**

TP: Rs 335 | ▲ 17%

**GUJARAT GAS**

| Oil &amp; Gas

| 05 June 2020

## Robust margin outlook

**Gujarat Gas' (GUJGA) Q4FY20 earnings beat estimates, surging 115% YoY to Rs 2.5bn. Key highlights: (a) volumes came in well above expectations at 10.1mmscmd (+55% YoY), and (b) EBITDA margins outperformed at Rs 4.7/scm (+8.5% YoY). We raise FY21/FY22 earnings estimates by 5%/9% on a better operating margin outlook. Our Mar'21 TP rises to Rs 335 (from Rs 265) on higher earnings, an improved volume outlook and lower cost of equity assumptions. Sustained low LNG prices augur well for margins.**

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**Improved long-term volume prospects:** Ceramic units in Morbi (Gujarat) were absorbing >6mmscmd of GUJGA's volumes until Mar'20, resulting in a volume beat at 10mmscmd in Q4. Industrial volumes grew 3.5mmscmd YoY to 7.8mmscmd in Q4, with a bulk of the growth driven by Morbi. These are expected to average ~50% lower in Q1FY21 due to the economic lockdown, but may retrace to >7mmscmd levels within a month of restrictions being lifted. CNG volumes (1.5mmscmd in Q4, +1% YoY) may take longer to recover from the >70% slump post-lockdown; domestic PNG could recover faster.

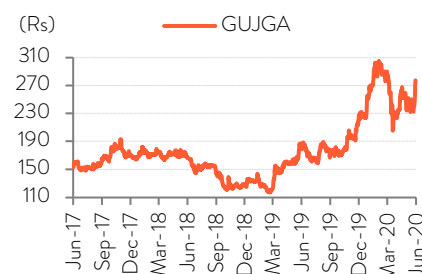
**Volume potential from new areas to fructify from FY21:** GUJGA's expansion plans are unlikely to be affected by the lockdown as a bulk of its capex usually occurs in H2 each year. The company plans to continue entering newer areas and has maintained capex guidance at Rs 6bn-7bn p.a. The initial strategy is to tap potential from existing networks (Rajasthan to rural Thane near Mumbai). It would simultaneously tap volumes from new areas such as Dahej, Punjab (licenced for six areas) and Rajasthan, that offer 4-5mmscmd potential.

**Undemanding valuations:** At 14.3x FY22E EPS, GUJGA's valuations remain attractive vs. CGD peers (17-20x for IGL/MAHGL). Expected volume and margin stability could narrow this gap.

Ticker/Price	GUJGA IN/Rs 286
Market cap	US\$ 2.6bn
Shares o/s	688mn
3M ADV	US\$ 3.1mn
52wk high/low	Rs 314/Rs 155
Promoter/FPI/DII	61%/10%/29%

Source: NSE

## STOCK PERFORMANCE



Source: NSE

## KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20P	FY21E	FY22E
Total revenue (Rs mn)	61,743	77,544	103,003	78,161	95,511
EBITDA (Rs mn)	8,951	9,836	16,344	17,201	21,232
Adj. net profit (Rs mn)	2,914	4,159	9,061	10,479	13,728
Adj. EPS (Rs)	4.2	6.0	13.2	15.2	19.9
Adj. EPS growth (%)	32.7	42.7	117.9	15.6	31.0
Adj. ROAE (%)	16.7	20.6	32.9	27.4	29.3
Adj. P/E (x)	67.5	47.3	21.7	18.8	14.3
EV/EBITDA (x)	24.1	22.2	13.2	12.3	9.7

Source: Company, BOBCAPS Research

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**FIG 1 – QUARTERLY PERFORMANCE**

(Rs mn)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19	YoY (%)
<b>Net sales</b>	<b>26,666</b>	<b>19,076</b>	<b>39.8</b>	<b>25,062</b>	<b>6.4</b>	<b>103,003</b>	<b>77,544</b>	<b>32.8</b>
Gas Purchased	20,264	14,638	38.4	19,482	4.0	78,818	60,830	29.6
% of sales	76.0	76.7	-	77.7	-	76.5	78.4	-
Other expenditure	2,135	1,896	12.6	1,875	13.9	7,843	6,868	14.2
% of sales	8.0	9.9	-	7.5	-	7.6	8.9	-
<b>EBITDA</b>	<b>4,267</b>	<b>2,541</b>	<b>67.9</b>	<b>3,705</b>	<b>15.2</b>	<b>16,343</b>	<b>9,846</b>	<b>66.0</b>
<b>EBITDA (Rs/scm)</b>	<b>4.7</b>	<b>4.3</b>	<b>8.5</b>	<b>4.3</b>	<b>9.0</b>	<b>4.7</b>	<b>4.1</b>	<b>15.1</b>
<b>EBITDA margin (%)</b>	<b>16.0</b>	<b>13.3</b>	<b>-</b>	<b>14.8</b>	<b>-</b>	<b>15.9</b>	<b>12.7</b>	<b>-</b>
Depreciation and amortisation	805	722	11.4	795	1.3	3,180	2,880	10.4
Interest	420	497	(15.5)	465	(9.6)	1,922	1,962	(2.0)
Other income	189	187	1.4	187	1.4	839	1,113	(24.6)
<b>PBT</b>	<b>3,231</b>	<b>1,508</b>	<b>114.2</b>	<b>2,633</b>	<b>22.7</b>	<b>12,080</b>	<b>6,117</b>	<b>97.5</b>
Exceptional item (as reported)	-	-	-	-	-	0	-	-
Provision for tax	717	343	108.9	668	7.2	92	1,768	(94.8)
<b>PAT (reported)</b>	<b>2,514</b>	<b>1,165</b>	<b>115.7</b>	<b>1,964</b>	<b>28.0</b>	<b>11,989</b>	<b>4,349</b>	<b>175.7</b>
<b>PAT (adjusted)</b>	<b>2,514</b>	<b>1,165</b>	<b>115.7</b>	<b>1,964</b>	<b>28.0</b>	<b>9,060</b>	<b>4,349</b>	<b>108.3</b>
<b>NPM (%)</b>	<b>9.4</b>	<b>6.1</b>	<b>-</b>	<b>7.8</b>	<b>-</b>	<b>11.6</b>	<b>5.6</b>	<b>-</b>
<b>EPS adj. (Rs)</b>	<b>3.7</b>	<b>1.7</b>	<b>115.7</b>	<b>2.9</b>	<b>28.0</b>	<b>13.2</b>	<b>6.3</b>	<b>108.3</b>

Source: Company, BOBCAPS Research

**FIG 2 – SEGMENTAL VOLUME BREAKUP**

Volumes (mmscmd)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19	YoY (%)
CNG Volume (mmscm)	134	133	0.8	139	(3.6)	543	520	4.4
PNG Volume (mmscm)	771	452	70.6	718	7.4	2,911	1,867	55.9
Domestic	60	57	5.3	53	13.2	208	195	6.7
Industrial	700	384	82.3	654	7.0	2,662	1,631	63.2
Commercial	11	11	-	11	-	41	41	-
<b>Total Volume (mmscm)</b>	<b>905</b>	<b>585</b>	<b>54.7</b>	<b>857</b>	<b>5.6</b>	<b>3,454</b>	<b>2,387</b>	<b>44.7</b>
<b>Total Volume (mmscmd)</b>	<b>10.1</b>	<b>6.5</b>	<b>54.7</b>	<b>9.3</b>	<b>7.9</b>	<b>9.5</b>	<b>6.6</b>	<b>44.2</b>

Source: Company, BOBCAPS Research

## Valuation methodology

GUJGA's unique positioning in the city gas distribution space makes it one of the best plays on gas volume growth potential, based on (a) its access to over 80% of CGD potential in Gujarat, and (b) strategic expansion into new areas (such as Dahej in Gujarat, Rajasthan, Western Maharashtra and Punjab) that are contiguous to its parent Gujarat State Petronet's pipeline networks.

We raise FY21/FY22 earnings expectations by 5%/9% on a better operating margin outlook. Our Mar'21 target price rises to Rs 335 (from Rs 265) on higher earnings, a better volume outlook and lower cost of equity assumptions. Sustained low LNG prices augur well for margins.

### FIG 3 – REVISED ESTIMATES

(Rs mn)	FY21E			FY22E		
	Old	New	Var (%)	Old	New	Var (%)
Gross Revenue	78,379	80,102	2.2	91,749	97,789	6.6
EBITDA	16,924	17,201	1.6	20,001	21,232	6.2
EBITDA margin (%)	21.6	21.5	-	21.8	21.7	-
PAT	9,993	10,479	4.9	12,602	13,728	8.9
PAT margin (%)	12.7	13.1	-	13.7	14.0	-
EPS (Rs)	14.5	15.2	5.0	18.3	19.9	9.0

Source: Company, BOBCAPS Research

At 14.3x FY22E EPS, GUJGA's valuations remain attractive vs. CGD peers (17-20x for IGL/MAHGL). Expected volume and margin stability could narrow this gap. Maintain BUY with a Mar'21 TP of Rs 335.

Key assumptions for our DCF-based fair value are as under:

- cost of equity of 11.8% (from 12.5% earlier) and terminal growth of 5%
- long-term average EBITDA margins of Rs 5.2/scm (revised from Rs 5/scm earlier)

### FIG 4 – VALUATION SUMMARY

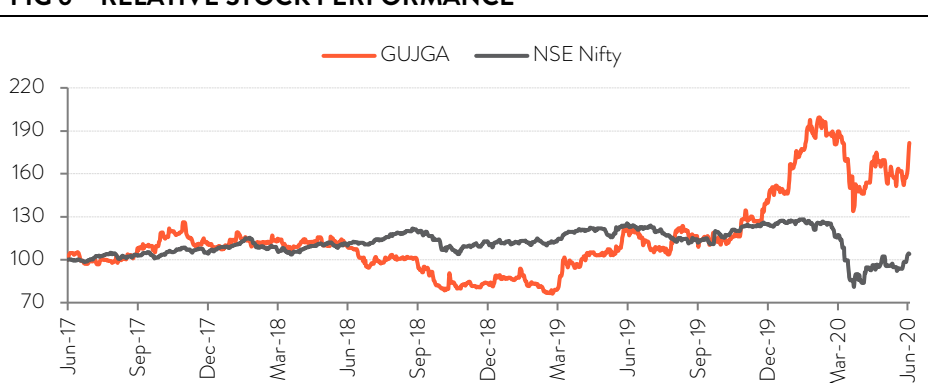
Valuation type	Value (Rs mn)
PV of FCFE	93,235
PV of terminal value	148,269
Less: Net Debt (FY19)	(11,410)
Equity value	223,881
<b>Equity value (Rs/share)</b>	<b>335</b>

Source: BOBCAPS Research

**FIG 5 – FAIR VALUE SENSITIVITY TO TERMINAL GROWTH & COST OF EQUITY**

		Cost of Equity (%)				
Terminal growth (%)	(Rs)	9.8	10.8	11.8	12.8	13.8
	3	371	318	276	243	216
	4	414	347	298	259	228
	<b>5</b>	475	387	<b>335</b>	279	243
	6	568	444	362	305	262
	7	727	530	415	339	286

Source: BOBCAPS Research

**FIG 6 – RELATIVE STOCK PERFORMANCE**

Source: NSE

### Key risks

- Lower-than-expected margins over FY21-FY22 could change our valuation outlook for GUJGA.
- Below-expected volume growth is a key risk.
- Change in PNGRB regulations or an unfavourable court ruling (against the NGT order for ceramic units) could alter our volume growth outlook.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
<b>Total revenue</b>	<b>61,743</b>	<b>77,544</b>	<b>103,003</b>	<b>78,161</b>	<b>95,511</b>
EBITDA	8,951	9,836	16,344	17,201	21,232
Depreciation	(2,718)	(2,880)	(3,180)	(3,229)	(3,499)
EBIT	6,232	6,956	13,165	13,972	17,733
Net interest income/(expenses)	(1,961)	(1,962)	(1,922)	(1,262)	(1,113)
Other income/(expenses)	357	1,116	839	1,299	1,732
Exceptional items	0	(179)	0	0	0
EBT	4,628	6,110	12,082	14,009	18,353
Income taxes	(1,715)	(1,772)	(92)	(3,530)	(4,625)
<b>Reported net profit</b>	<b>2,914</b>	<b>4,159</b>	<b>11,990</b>	<b>10,479</b>	<b>13,728</b>
Adjustments	0	0	(2,929)	0	0
<b>Adjusted net profit</b>	<b>2,914</b>	<b>4,159</b>	<b>9,061</b>	<b>10,479</b>	<b>13,728</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Accounts payables	2,931	3,523	3,804	2,397	2,953
Other current liabilities	11,957	13,129	14,259	7,325	9,022
Provisions	49	83	130	130	130
Debt funds	22,143	20,892	18,794	16,696	14,598
Other liabilities	10,789	11,808	9,094	10,495	12,330
Equity capital	1,377	1,377	1,377	1,377	1,377
Reserves & surplus	17,087	20,463	31,797	41,912	48,911
Shareholders' fund	18,464	21,840	33,174	43,289	50,288
<b>Total liabilities and equities</b>	<b>66,333</b>	<b>71,275</b>	<b>79,254</b>	<b>80,332</b>	<b>89,322</b>
Cash and cash eq.	1,363	3,092	6,941	9,468	12,678
Accounts receivables	3,917	5,103	5,101	3,872	4,731
Inventories	568	694	463	439	536
Other current assets	3,906	3,742	4,148	4,147	4,148
Investments	161	177	446	466	486
Net fixed assets	50,940	53,347	55,467	56,538	61,339
CWIP	4,783	4,885	5,686	4,783	4,783
Intangible assets	0	4	9	9	9
Other assets	695	678	610	610	610
<b>Total assets</b>	<b>66,333</b>	<b>71,722</b>	<b>78,870</b>	<b>80,332</b>	<b>89,322</b>

Source: Company, BOBCAPS Research

**Cash Flows**

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Net income + Depreciation	5,632	7,039	15,170	13,708	17,227
Changes in working capital	66	1,262	1,394	(7,086)	1,294
Other operating cash flows	249	(755)	(3,650)	102	103
<b>Cash flow from operations</b>	<b>5,947</b>	<b>7,546</b>	<b>12,914</b>	<b>6,724</b>	<b>18,623</b>
Capital expenditures	(3,665)	(5,409)	(6,376)	(3,418)	(8,320)
Other investing cash flows	357	1,116	839	1,299	1,732
<b>Cash flow from investing</b>	<b>(3,308)</b>	<b>(4,293)</b>	<b>(5,537)</b>	<b>(2,118)</b>	<b>(6,588)</b>
Debt raised/repaid	(844)	(1,251)	(2,098)	(2,098)	(2,098)
Dividends paid	(664)	(806)	(3,182)	(3,680)	(4,821)
Other financing cash flows	(376)	532	1,751	3,700	(1,908)
<b>Cash flow from financing</b>	<b>(1,884)</b>	<b>(1,525)</b>	<b>(3,529)</b>	<b>(2,077)</b>	<b>(8,826)</b>
<b>Changes in cash and cash eq.</b>	<b>755</b>	<b>1,728</b>	<b>3,849</b>	<b>2,528</b>	<b>3,210</b>
<b>Closing cash and cash eq.</b>	<b>1,363</b>	<b>3,091</b>	<b>6,941</b>	<b>9,469</b>	<b>12,678</b>

**Per Share**

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20P	FY21E	FY22E
Reported EPS	4.2	6.0	17.4	15.2	19.9
Adjusted EPS	4.2	6.0	13.2	15.2	19.9
Dividend per share	0.8	1.0	3.9	4.6	6.0
Book value per share	26.8	31.7	48.2	62.9	73.1

**Valuations Ratios**

Y/E 31 Mar (x)	FY18A	FY19A	FY20P	FY21E	FY22E
EV/Sales	3.5	2.8	2.1	2.7	2.2
EV/EBITDA	24.1	22.2	13.2	12.3	9.7
Adjusted P/E	67.5	47.3	21.7	18.8	14.3
P/BV	10.6	9.0	5.9	4.5	3.9

**DuPont Analysis**

Y/E 31 Mar (%)	FY18A	FY19A	FY20P	FY21E	FY22E
Tax burden (Net profit/PBT)	63.0	70.1	75.0	74.8	74.8
Interest burden (PBT/EBIT)	74.3	85.3	91.8	100.3	103.5
EBIT margin (EBIT/Revenue)	10.1	9.0	12.8	17.9	18.6
Asset turnover (Revenue/Avg TA)	95.1	112.3	136.8	98.2	112.6
Leverage (Avg TA/Avg Equity)	3.7	3.4	2.7	2.1	1.8
Adjusted ROAE	16.7	20.6	32.9	27.4	29.3

Source: Company, BOBCAPS Research | Note: TA = Total Assets

**Ratio Analysis**

Y/E 31 Mar	FY18A	FY19A	FY20P	FY21E	FY22E
<b>YoY growth (%)</b>					
Revenue	21.2	25.6	32.8	(24.1)	22.2
EBITDA	20.4	9.9	66.2	5.2	23.4
Adjusted EPS	32.7	42.7	117.9	15.6	31.0
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	14.5	12.7	15.9	22.0	22.2
EBIT margin	10.1	9.0	12.8	17.9	18.6
Adjusted profit margin	4.7	5.4	8.8	13.4	14.4
Adjusted ROAE	16.7	20.6	32.9	27.4	29.3
ROCE	9.8	11.7	27.6	18.7	21.2
<b>Working capital days (days)</b>					
Receivables	22	21	18	21	16
Inventory	4	4	3	3	3
Payables	21	17	15	19	13
<b>Ratios (x)</b>					
Gross asset turnover	1.0	1.2	1.4	1.0	1.2
Current ratio	0.7	0.8	0.9	1.8	1.8
Net interest coverage ratio	3.2	3.5	6.9	11.1	15.9
Adjusted debt/equity	1.1	0.8	0.4	0.2	0.0

Source: Company, BOBCAPS Research

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### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

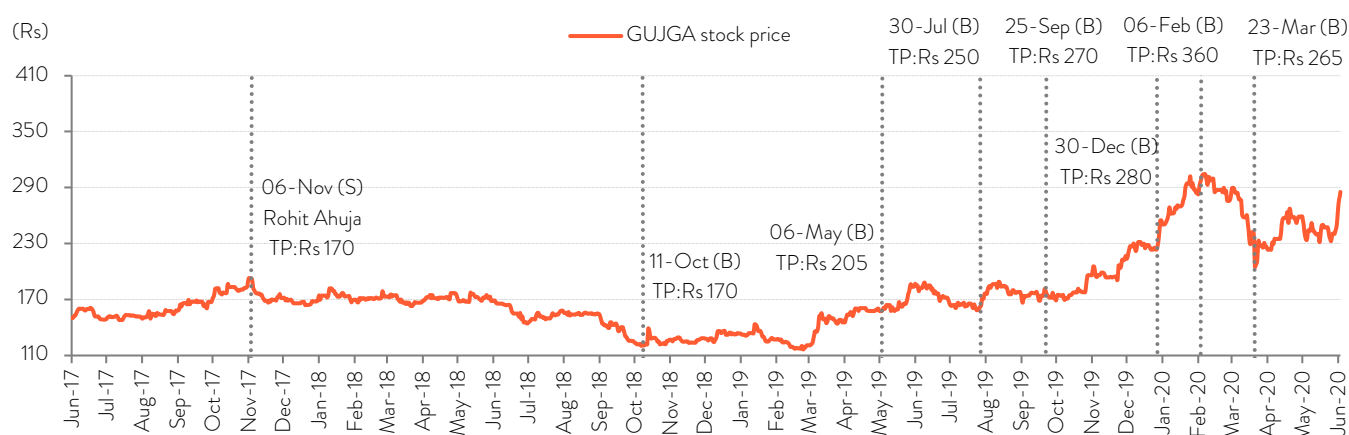
**ADD** – Expected return from >+5% to +15%

**REDUCE** – Expected return from -5% to +5%

**SELL** – Expected return <-5%

**Note:** Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

### HISTORICAL RATINGS AND TARGET PRICE: GUJARAT GAS (GUJGA IN)



B – Buy, A – Add, R – Reduce, S – Sell

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