

Retail Research	IPO Note
Sector: Natural Gas	Price Band (Rs): 480 - 505
18th October 2023	Recommendation: Subscribe for long term Horizon

IRM Energy Limited

Company Overview:

IRM Energy is a city gas distribution (CGD) company in India, with operations at Banaskantha (Gujarat), Fatehgarh Sahib (Punjab), Diu & Gir Somnath (Union Territory of Daman and Diu/Gujarat), and Namakkal & Tiruchirappalli (Tamil Nadu), engaged in the business of laying, building, operating and expanding the city or local natural gas distribution network. The company develops natural gas distribution projects in the geographical areas (GAs) allotted to the company for industrial, commercial, domestic, and automobile customers.

Key Highlights:

Customer segments:

CNG (Compressed Natural Gas): The company's customers include operators of public transport vehicles such as taxis, auto-rickshaws, and private vehicles such as cars, buses, light goods vehicles and heavy goods vehicles.

PNG (Piped Natural Gas): The company PNG customers are broadly classified into three segments, which are, industrial PNG (small, medium and large-sized enterprises), commercial PNG (such as hotels, restaurants, bakeries, hostels and community halls) and domestic PNG (predominantly using PNG as cooking gas). The company customer base includes 184/269/52,454 Industrial/Commercial/Domestic Customer.

Distribution Network: The company has 66 CNG filling stations spread across 3 geographical areas' i.e. Banaskantha, Diu and Gir Somnath, Fatehgarh Sahib connecting in total with 3,898 inch-kms pipeline. Out of 66 CNG stations, 2 stations are company-owned and company operated (COCO), 36 station are dealer-owned and dealer-operated (DODO), and 28 stations are operated by Oil Marketing Companies (OMC).

Increasing Demand in CGD Sector: Natural gas demand from the CGD sector to log at 19-20% CAGR between FY22 and FY30, growing to 117-120 Million Metric Standard Cubic Meter Per Day (MMSCMD). Demand from each sub-segment, including compressed and piped natural gas (domestic and industrial), is likely to grow at a healthy pace over the forecast period, with the expansion in the gas network to more cities. Increase in penetration is expected to be a key demand driver for the PNG and CNG segment. The government has the target to raise natural gas share in the energy mix to 15% by 2030.

Pricing: The price at which the company sells natural gas to the customers is not regulated by any authority and the company has control over the price at which the company sells natural gas. Considering natural gas is not a notified product, the pricing of natural gas is beyond the purview of PNGRB or any other regulator. In order to maintain the competitive advantage, the company periodically reviews the price at which the company sells natural gas including CNG and PNG, which is benchmarked against the prices of alternative fuels available to the customers.

Valuation: The company is valued at FY23 PE multiple of 32.8x and EV/EBITDA of 20.3x, at the upper price band on post-issue capital. Demand for natural gas in the CGD sector is expected to grow at a CAGR of 19-20% over FY23-FY27P which seems very supportive for the company's growth outlook. We recommend investors to subscribe the issue for long-term growth perspective.

Issue Details	
Date of Opening	18 th October 23
Date of Closing	20 th October 23
Price Band (Rs)	480 – 505
Issue Size (Rs cr)	518 - 545
No. of shares	1,08,00,000
Face Value (Rs)	10
Post Issue Market Cap (Rs cr)	1,970 – 2,074
BRLMs	HDFC Bank Limited, BOB Capital Markets Limited
Registrar	Link Intime India Private Limited
Bid Lot	29 shares and in multiple thereof
QIB shares	50%
Retail shares	35%
NIB (HNI) shares	15%

Objects of Issue		(Rs Cr.)*
Capex for city gas distribution network in the geographical areas of Namakkal and Tiruchirappalli		307.3
Prepayment or repayment of all or a portion of certain outstanding borrowings availed by the company		135.0
General Corporate Purpose**		-

*To be finalized upon determination of the Issue Price and updated in the Prospectus prior to filing with the RoC.

**The amount utilized for general corporate purpose shall not exceed 25% of the Net Proceeds of the Issue.

Shareholding Pattern		
Pre-Issue	No. of Shares	%
Promoter & Promoter Group	2,05,58,773	67.9
Public & Others	97,00,904	32.1
Total	3,02,59,677	100.0

Post Issue @Lower Price Band	No. of Shares	%
Promoter & Promoter Group	2,05,58,773	50.1
Public & Others	2,05,00,904	49.9
Total	4,10,59,677	100.0

Post Issue @Upper Price Band	No. of Shares	%
Promoter & Promoter Group	2,05,58,773	50.1
Public & Others	2,05,00,904	49.9
Total	4,10,59,677	100.0

Source: RHP, SSL Research

Key Performance Indicators

Particulars	FY21	FY22	FY23	3MFY23	3MFY24
CNG (MMSCM)	43.1	72.5	83.7	22.2	22.6
PNG (MMSCM)	19.9	78.5	112.7	24.8	23.1
Total (MMSCM)	63.0	151.2	196.4	46.9	45.7
Volume growth (%)	39.2	139.8	30.0	84.2	-2.7
Net Revenue from Operations (Net of Excise Duty) (Rs cr)	189.6	507.1	980.1	214.7	230.0
Gas Cost (Rs cr)	77.1	248.2	779.8	160.5	167.7
Gross Margin (Rs cr)	112.5	258.9	200.3	54.2	62.3
EBITDA (Consolidated) (Rs cr)	73.0	200.9	118.9	34.7	41.1
EBITDA (%)	38.5	39.6	12.1	16.2	17.9
PAT (Consolidated) (Rs cr)	34.9	128.0	63.1	20.5	26.9
EPS (Consolidated) (Rs)	12.4	43.9	20.9	7.0*	8.9*
PE (x)**	40.8	11.5	24.1	72.1*	56.8*
P/BV (x)***	12.5	6.1	4.4	5.6	4.1
ROE (Consolidated) (%)	29.7	52.5	18.2	7.7*	7.2*
ROCE (Consolidated) (%)	20.0	39.0	14.2	6.0*	4.9*

*Not Annualized

** PE(x) is calculated on upper price band

*** P/BV (x) is calculated on upper price band

Source: RHP, SSL Research

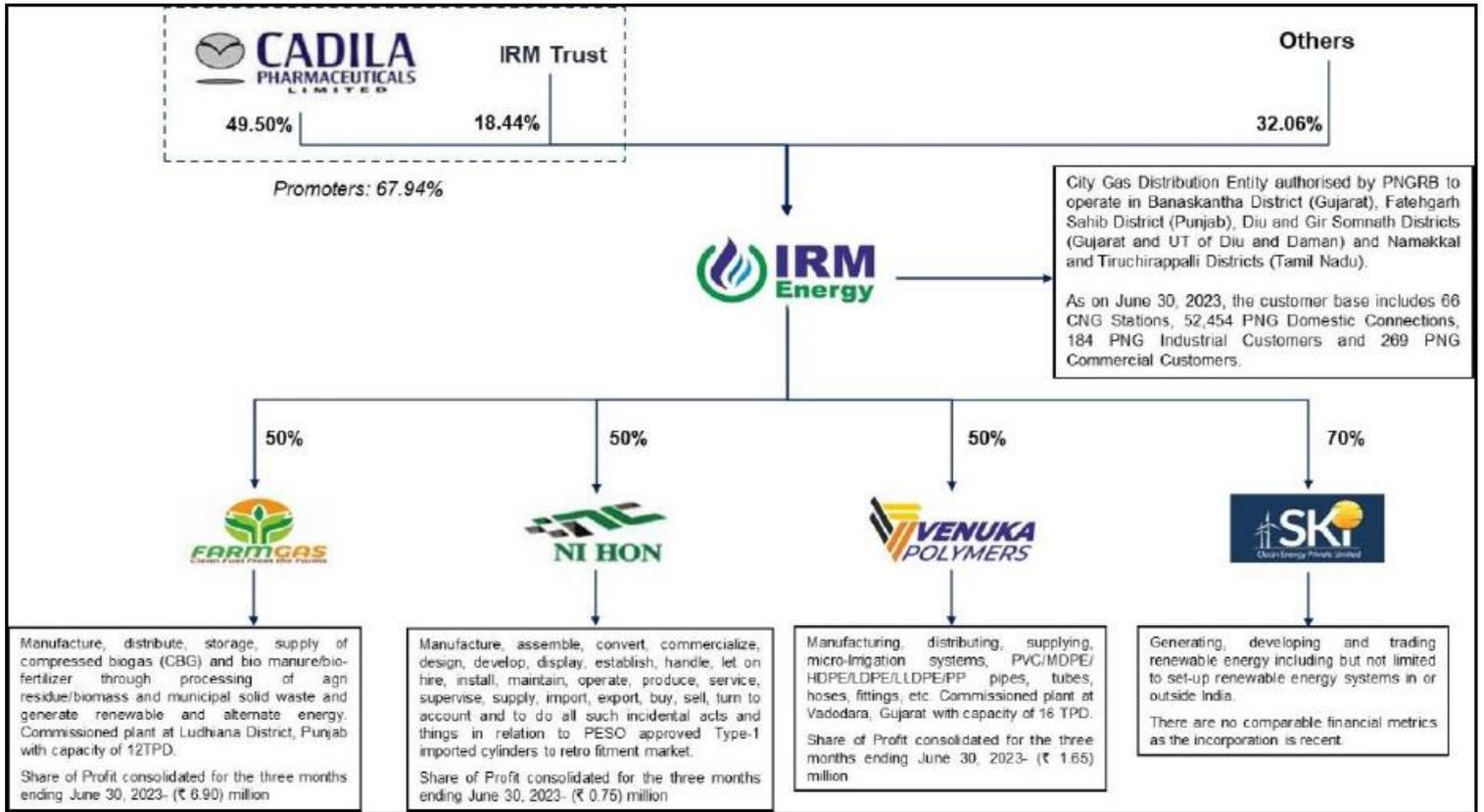
Risk Factors

- **Third party:** The company is dependent on third parties for sourcing and transportation of natural gas.
- **Transportation:** Transporting natural gas is hazardous and could result in accidents, which could adversely affect the reputation, business, financial condition, results of operations, and cash flows.
- **Operational volume:** The company's CNG and industrial PNG supply operations account for 49.4 % and 46.9 % of the total operations volume for the 3MFY24. The company is heavily reliant on the CNG and industrial PNG supply operations and any decrease in the sales, may have an adverse effect on the business, operation, financial condition and cash flows of the company.
- **Licensing:** The company requires various licenses and approvals for undertaking the businesses and the failure to obtain or retain such licenses or approvals in a timely manner, or at all, may adversely affect the operations.
- **New GAs:** The company typically requires 15-18 months to generate revenue in the new GAs. Any further delay in realizing revenue may affect our projections, results of operations, and cash flows.

Growth Strategy

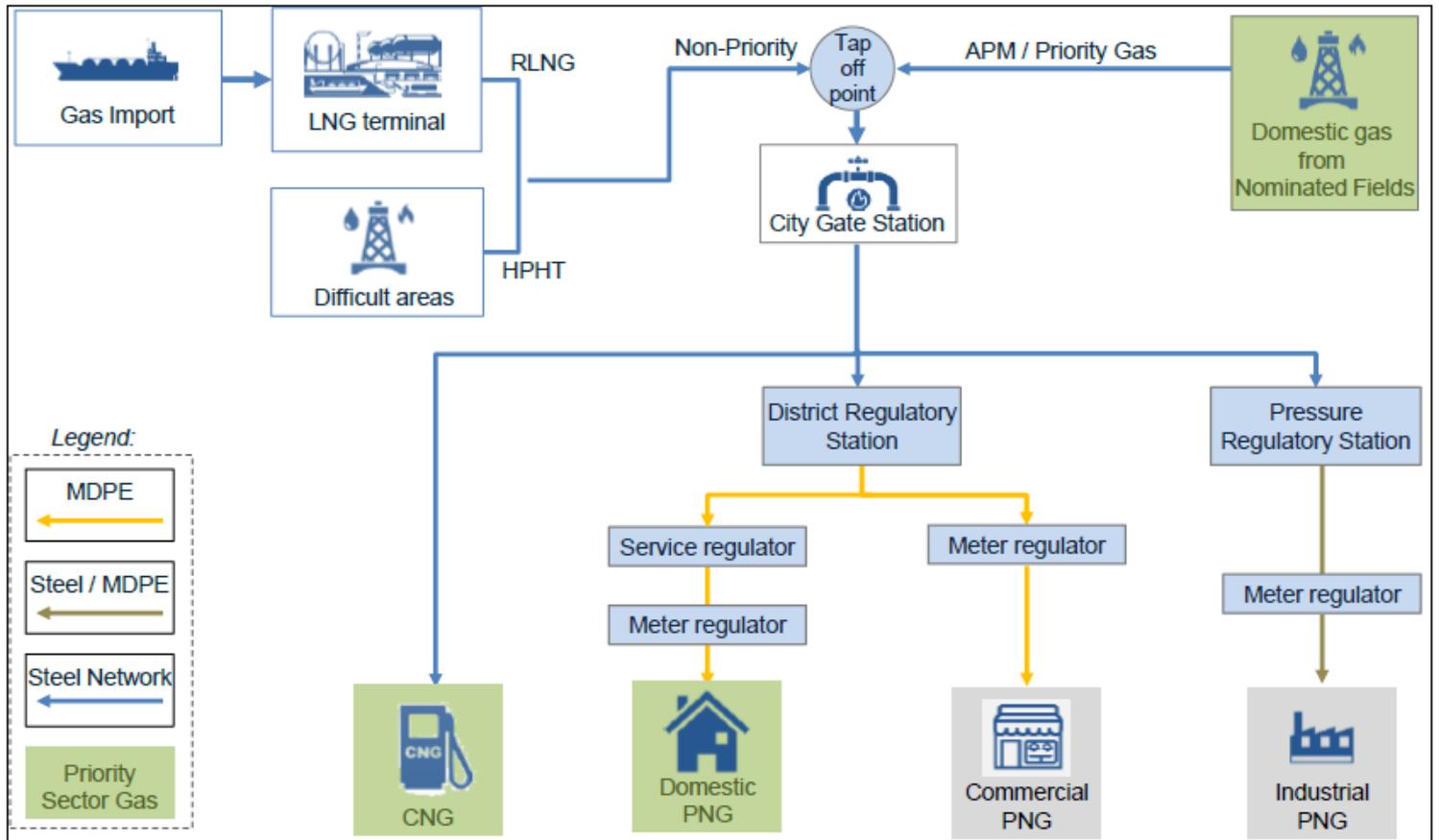
- **Expansion:** Expanding the presence in existing and newer GAs through an improved captive distribution channel.
- **New GAs:** Infrastructure roll-out for development and operation of the new licensed GA of Namakkal & Tiruchirappalli, Tamil Nadu.
- **Optimize opex:** Technology adoption to increase operational efficiency and enhance customer value.
- **Business integration:** Business integration for transition into a complete energy solution provider.
- **Cost effective:** Continue to focus on sourcing reliable and cost-effective gas from leading gas suppliers.

Corporate Structure



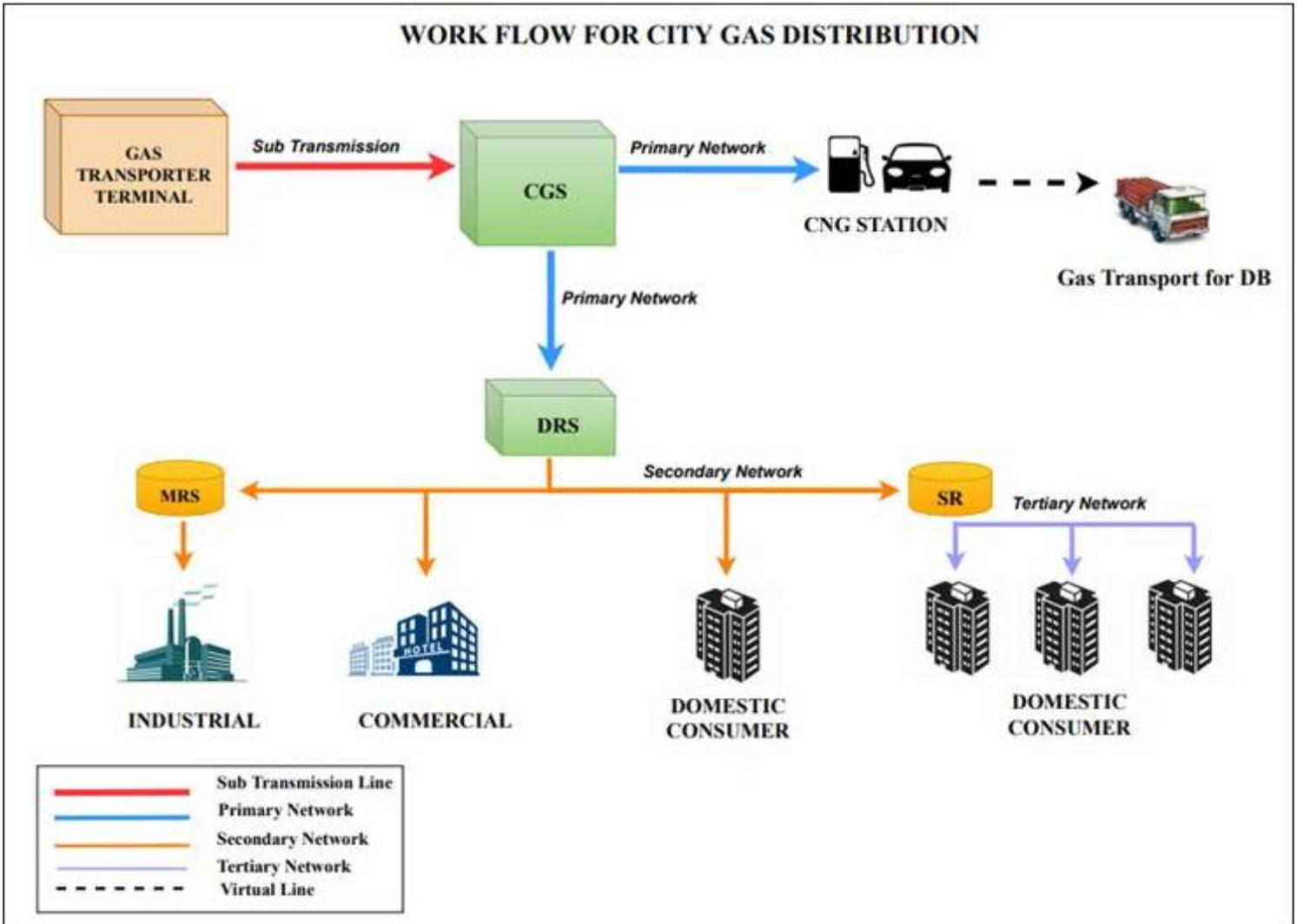
Source: RHP, SSL Research

Indicative CGD Network Structure



Source: RHP, SSL Research

Company's Distribution Network

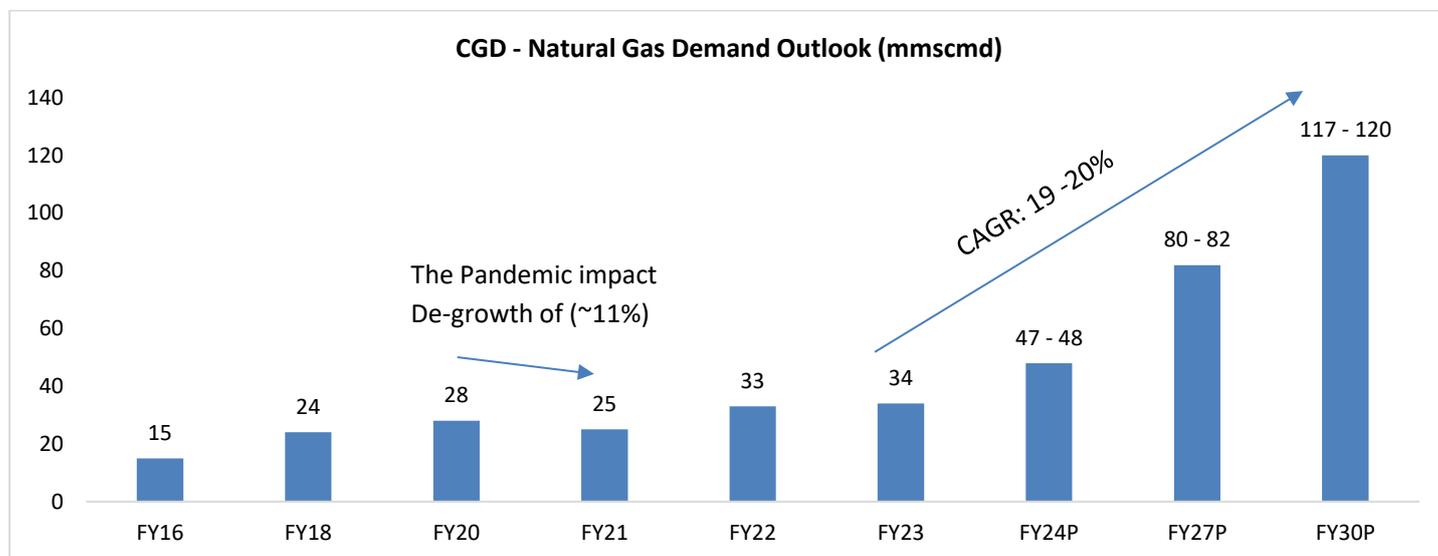


Source: RHP, SSL Research

Industry Overview

CGD - Natural Gas Demand Outlook

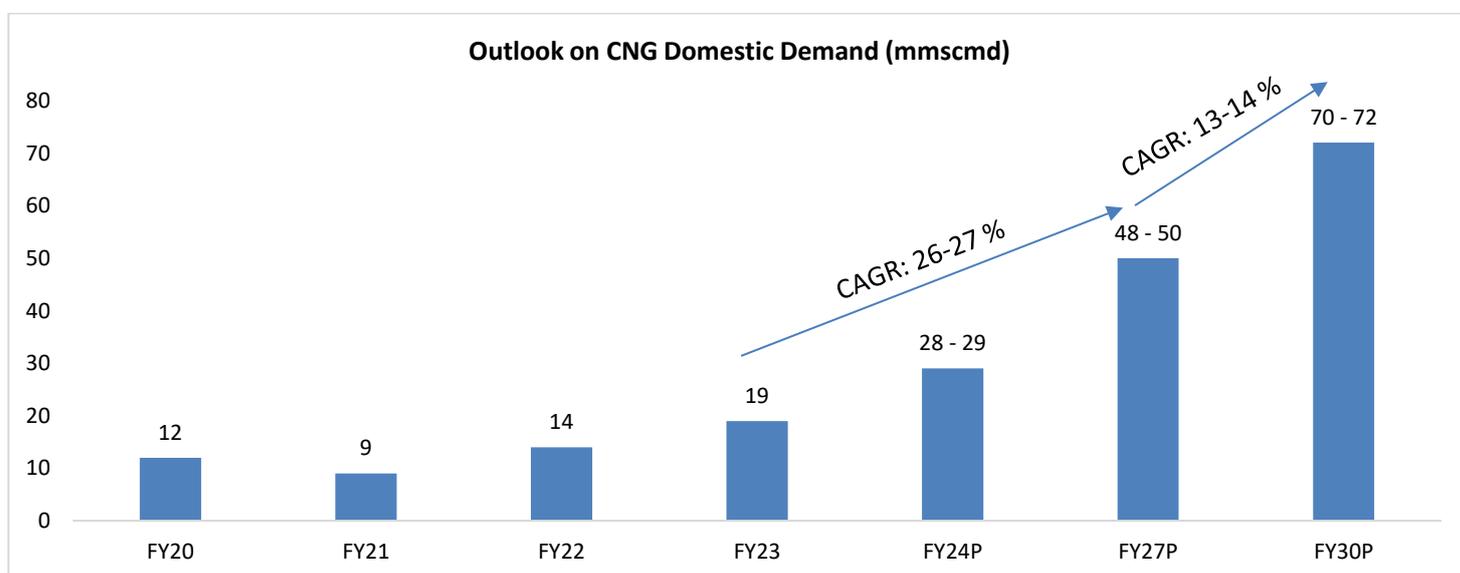
CGD delivered muted demand increase ~1-3% in FY23. As per CRISIL, MI&A consulting expects natural gas demand from the CGD sector to log 19-20% CAGR between FY23 and FY30, growing to 117-120 mmscmd. Demand from each sub-segment, including CNG and PNG (domestic and industrial), is likely to grow at a healthy pace over the forecast period, with the addition of new cities in the gas network. Increase in penetration is expected to be a key demand driver for the PNG segment. Further, the pace of development of the CGD network would be another key determinant of growth, going forward.



Source: RHP, SSL Research

Outlook on CNG Domestic Demand

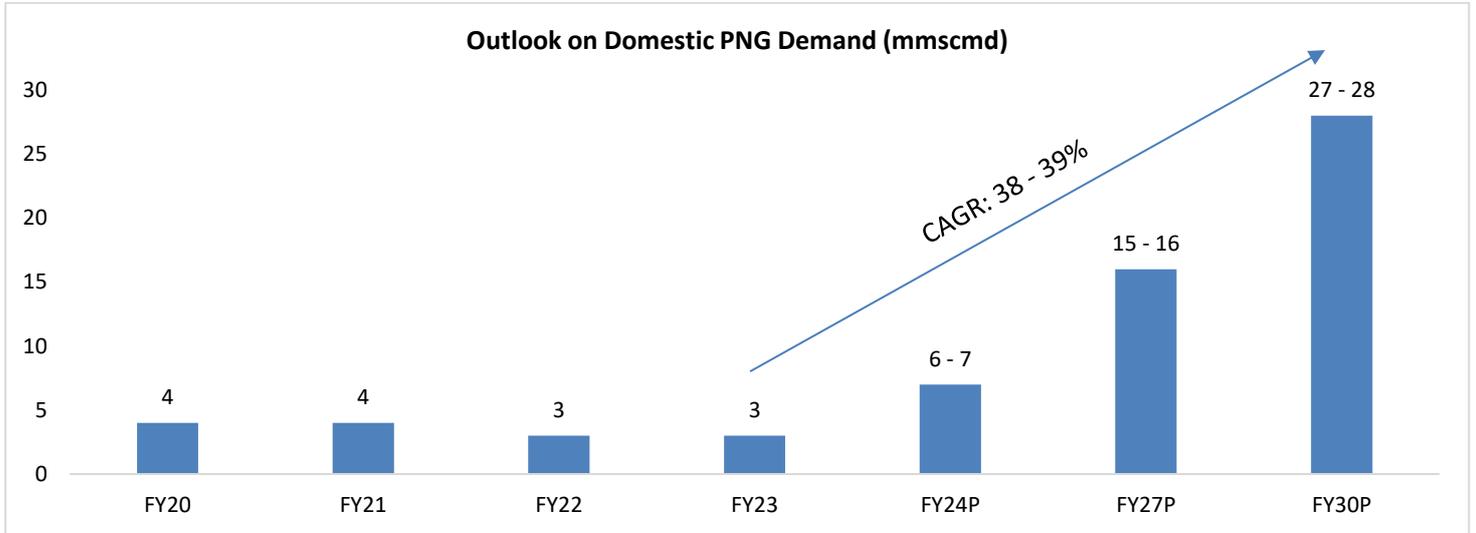
The CNG segment is expected to register a healthy CAGR of 26-27% between FY23 and FY27, driven by cost competitiveness of CNG vis-à-vis petrol. As CNG directly competes with petrol in the vehicle segment, conversion from petrol to CNG would continue during the forecast period, given the cost advantage. CNG stations has increased at a healthy YoY growth of 32% between FY22 and FY23, supporting faster adoption of CNG vehicles across various segments with OEM’s launching CNG vehicles to address the demand. CNG adoption in three-wheelers surged from 26% in FY22 to 29% in FY23. CNG adoption in light commercial vehicles (LCVs) is increased by 14% in FY23 from 5% in FY21.



Source: RHP, SSL Research

Outlook on Domestic PNG Demand

Total household PNG connections are expected to surge from ~78.2 lakh as of FY21 to 190-200 lakh by FY26 due to increasing CGD penetration in newer areas and the government’s push to increase gas consumption. This number will further multiply with the CGD network covering Andhra Pradesh, Tamil Nadu, Telangana, West Bengal, etc, between FY25 and FY30. Moreover, consumption per connection should increase due to rising disposable income and economic growth. Consequently, demand from the domestic segment is projected to log a 38-39% CAGR between FY23 and FY30.



Source: RHP, SSL Research

Financial Snapshot

INCOME STATEMENT			
(Rs cr)	FY21	FY22	FY23
Revenue from Operations	190	507	980
YoY growth (%)	-	167.5	93.3
Cost Of Revenues (incl Stock Adj)	77	248	780
Gross Profit	112	259	200
Gross margins (%)	59.3	51.1	20.4
Employee Cost	4	7	9
Other Operating Expenses	35	65	79
EBITDA	73	186	112
EBITDA margins (%)	38.6	36.8	11.5
Other Income	1	3	6
Net Interest Exp.	16	22	23
Depreciation	12	15	21
PBT	46	152	74
Tax	11	39	18
Adj PAT	35	128	63
PAT margin (%)	18.4	25.2	6.4
Adj. EPS	12.0	43.6	20.9

BALANCE SHEET			
(Rs cr)	FY21	FY22	FY23
Assets			
Net Block	238	298	377
Capital WIP	20	52	91
Intangible Assets under development	3	3	3
Other Non current Assets	20	61	96
Current Assets			
Current Investment	1	10	54
Inventories	1	2	2
Trade receivables	11	23	39
Cash and Bank Balances	41	100	98
Other Current Assets	3	7	32
Total Current Assets	58	141	226
Current Liabilities & Provisions			
Trade payables	10	25	31
Other current liabilities	17	36	48
Short-term provisions	1	1	1
Total Current Liabilities	28	63	80
Net Current Assets	30	79	145
Total Assets	310	492	713
Liabilities			
Share Capital	29	29	30
Reserves and Surplus	89	214	316
Total Shareholders Funds	118	244	346
Total Debt	163	203	304
Long Term Provisions	1	1	1
Other Long-Term Liabilities	14	26	34
Net Deffered Tax Liability	14	20	27
Total Liabilities	310	492	713

CASH FLOW (Rs cr)	FY21	FY22	FY23
Cash flow from Operating Activities	45.4	128.6	46.7
Cash flow from Investing Activities	-42.0	-110.3	-201.6
Cash flow from Financing Activities	10.3	15.1	117.7
Free Cash Flow	10.3	38.2	-115.8

RATIOS			
	FY21	FY22	FY23
Profitability			
Return on Assets (%)	10.3	23.1	8.0
Return on Capital (%)	22.0	39.1	15.0
Return on Equity (%)	29.7	52.5	18.2
Margin Analysis			
Gross Margin (%)	59.3	51.1	20.4
EBITDA Margin (%)	38.6	36.8	11.5
Net Income Margin (%)	18.4	25.2	6.4
Short-Term Liquidity			
Current Ratio (x)	1.7	1.8	2.2
Quick Ratio (x)	1.7	1.8	2.2
Avg. Days Sales Outstanding	22	16	14
Avg. Days Inventory Outstanding	2	1	1
Avg. Days Payables	19	18	12
Fixed asset turnover (x)	0.8	1.7	2.6
Debt-service coverage (x)	0.4	0.8	0.3
Long-Term Solvency			
Total Debt / Equity (x)	1.4	0.8	0.9
EBITDA / Interest Expense (x)	3.9	7.9	4.2
Valuation Ratios			
EV/EBITDA (x)	21.7	8.5	15.0
PE (x)	42.0	11.6	24.2
P/BV (x)	12.5	6.1	4.4

Source: RHP, SSL Research

Peer Comparison

	IRM Energy Limited	Gujarat Gas Limited	Indraprastha Gas Limited
CMP	505.0	427.0	487.0
Sales (Rs cr)	189.6	16,759.0	14,146.0
EBITDA (Rs cr)	73.0	2,422.0	2,058.0
Net Profit (Rs cr)	34.9	1,528.0	1,445.0
M.Cap (Rs cr)	2,073.5	29,394.0	34,094.0
Enterprise Vaue (Rs cr)	2,278.9	28,866.0	31,543.0
EBITDA Margin (%)	38.5	14.5	14.5
Net Margin (%)	18.4	9.1	10.2
PE(x)	32.8	21.6	23.3
EV/EBITDA (x)	20.3	11.9	15.3
RoE (%)	29.7	24.2	20.0
RoCE (%)	20.0	31.2	26.7

(Source: RHP, SSL Research)

The data is based on FY23 financial data, For IRM Energy Limited the Market cap, PE(x), and EV/EBITDA are calculated on post-issue equity share capital based on the upper price band.

CMP as on 17th October'23.

SBICAP Securities Limited

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SEBI Registration No.: Stock Broker: INZ000200032 | CDSL: IN-DP-314-2017 | NSDL: IN-DP-NSDL-369-2014 | Research Analyst: INH000000602

Portfolio Manager: INP000004912 | IRDA/RW/IR2/2015/081 | IRDA/RW/IR1/2016/041 | IRDA: CA0103

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