

Gati

Rs96
OUTPERFORMER

RESULT NOTE

Mkt Cap: Rs6.7bn; US\$164m

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Result: Q3FY07

Comment: In line with estimates; strong growth in express cargo division to drive 31% earnings CAGR over FY06-08

Last report: 22 January 2007 (Price Rs96; Recommendation: Outperformer)

Key valuation metrics

Year to June (Rs mn)	Sales	yoy chg (%)	Net Profit	EPS (Rs)	yoy chg (%)	PER (x)
2005	3,592	17.3	104	2.5	86.7	37.4
2006	4,561	27.0	201	3.2	31.0	28.5
2007E	5,515	20.9	266	3.7	13.1	25.2
2008E	7,449	35.1	436	5.6	51.6	16.6
2009E	9,671	29.8	581	6.2	11.5	14.9

Gati's 3QFY07 results were in line with our estimates at Rs68mn (+31% yoy growth). Revenues grew by 18% yoy to Rs1.4bn during the quarter led by strong growth in coast to coast and express cargo distribution divisions. Operating margins improved by 30bps to 9% led by 40bps improvement in express cargo distribution business as fuel expenses fell during the quarter. Going forward, Gati's expansion of its warehouses and investments in IT systems are likely to further strengthen its competitive position, and thereby driving its earnings at an estimated 31% CAGR over FY06-08. The stock currently trades at 16.6x FY08E earnings. We believe valuations are attractive considering its leadership position in express cargo business coupled with the strong earnings growth momentum and high earnings visibility. We maintain Outperformer rating on the stock.

RESULT HIGHLIGHTS

- Revenues grew by 18% yoy in 3QFY07 to Rs1.38bn mainly driven by strong growth in both coast-to-coast (shipping) as well as express distribution divisions.
- Operating margins improved by 30bps to 9% during the quarter primarily due to improvement in margins of the express distribution business. However, the fall in the coast to coast division margins muted the overall improvement in margins.
- Depreciation increased by 23% yoy to Rs27mn as Gati invested significantly in warehousing facilities as well as upgradation of IT systems.
- Other income jumped by 98% yoy to Rs8mn led by surplus cash on books. Accordingly, interest expense remained flat at Rs12mn.
- Gati has provided tax at 27% for the quarter after considering tonnage tax on its profits from coast-to-coast division.
- Overall, net profit grew by 31% to Rs68mn during the quarter.

❑ Express distribution cargo division – margin expansion

- Express cargo distribution division witnessed a strong revenue growth of 16.7% yoy to Rs992mn during the quarter led by growth in trade activity and increased trend of outsourcing of logistics solutions by corporates.
- EBIT margins have improved by 330bps to 12.1% during the quarter led by higher utilization of the trucking fleet and warehousing facilities. Moreover, the fall in fuel cost during the quarter further improved margins during the quarter.

❑ Coast-to-coast (shipping) division – margin fell due to dry docking of one ship

- Coast-to-coast division witnessed a strong revenue growth of 31.6% yoy during the quarter led by re-commissioning of one ship after dry docking.
- However, EBIT margins have fallen by 430bps to 15.9% during the quarter as one of the ships from Gati's fleet was under maintenance. Consequently, the ship did not generate any revenues, but Gati had to incur fixed costs for the ship, which impacted the margins for the division.

❑ Fuel stations – robust volume growth

- The fuel stations witnessed a revenue growth of 17.7% yoy to Rs232mn during the quarter led by growth in traded volumes.
- EBIT margins have improved marginally by 20bps during the quarter to 1.2%.
- The fuel business is not a core operation of Gati's logistics business. As a result, Gati is transferring the fuel division to a 100% subsidiary. Gati is awaiting the approval for the hive off from the High Court. The hive off will be effective 1st July 2006.

Segmental data

(Rs mn)	1Q06	2Q06	3Q06	4Q06	FY06	1Q07	2Q07	3Q07
Revenues								
Express Distribution & Supply Chain	704	830	850	873	3,256	913	990	992
Coast to Coast (Shipping)	114	124	122	132	494	158	143	161
Fuel Stations	183	197	197	238	815	262	257	232
Total	1,001	1,151	1,169	1,242	4,565	1,332	1,390	1,384
% yoy growth, Sales								
Express Distribution & Supply Chain	19.7	25.9	26.8	29.5	25.6	29.7	19.3	16.7
Coast to Coast (Shipping)	174.3	107.9	58.0	42.3	80.3	37.7	15.7	31.6
Fuel Stations	0.1	(5.8)	16.2	41.9	11.7	43.1	30.3	17.7
EBIT								
Express Distribution & Supply Chain	74	88	75	81	317	87	109	120
Coast to Coast (Shipping)	21	29	25	20	94	25	24	26
Fuel Stations	2	2	2	2	8	3	3	3
Total	97	119	102	102	419	115	136	148
EBIT margins (%)								
Express Distribution & Supply Chain	10.5	10.6	8.8	9.3	9.7	9.6	11.0	12.1
Coast to Coast (Shipping)	18.2	23.4	20.2	14.8	19.0	16.1	17.1	15.9
Fuel Stations	1.2	1.0	1.0	0.7	0.9	1.0	1.2	1.2
Total	9.7	10.3	8.7	8.2	9.2	8.7	9.8	10.7

□ Earnings CAGR of 31% over FY06-08 – Maintain Outperformer

We are not changing our earnings estimates for FY07 and FY08. Gati, with its strong infrastructure in terms of distribution network, IT systems, warehouses and value added services, is well positioned to capitalize on the boom of the fast growing express cargo distribution business. As a result, we expect Gati's revenues to grow at 23% CAGR in revenues over FY06-08 and a robust earnings growth of 31% CAGR over FY06-08. The stock currently trades at 16.6x FY08E earnings. We believe valuations are attractive in view of the strong earnings growth momentum and high earnings visibility. We maintain Outperformer rating on the stock with a target price of Rs119/share.

Quarterly results

Year end June (Rs mn)	1Q06	2Q06	3Q06	4Q06	FY06	1Q07	2Q07	3Q07	FY07E
Net Sales	1,001	1,151	1,169	1,241	4,561	1,332	1,390	1,383	5,515
Expenditure	913	1,047	1,066	1,148	4,174	1,216	1,264	1,259	5,024
Operating Profit	89	104	102	93	387	115	126	124	490
OPM (%)	8.8	9.0	8.7	7.5	8.5	8.7	9.1	9.0	8.9
Interest	13	9	11	9	42	13	18	12	55
Depreciation	19	19	22	26	87	25	27	27	112
Other Income	2	0	4	9	16	4	5	8	30
Profit before Tax	59	76	72	68	275	81	85	93	354
Deferred Tax	16	18	3	19	56	-1	3	29	7
Current Tax	(1)	1	18	1	18	22	13	(4)	81
Tax rate (%)	25.6	24.3	28.5	29.4	26.9	26.8	18.9	27.1	25.0
Profit after Tax	44	57	52	48	201	59	69	68	266
Extraordinary Items	0	0	0	0	0	(3)	(27)	0	(30)
Net Profit	44	57	52	48	201	56	43	68	236
OPM (%)	8.8	9.0	8.7	7.5	8.5	8.7	9.1	9.0	8.9
NPM (%)	4.4	5.0	4.4	3.9	4.4	4.5	5.0	4.9	4.8
Shares (m)	70.8	70.8	70.8	70.8	70.8	70.8	70.9	72.4	72.4
EPS (Rs)	0.6	0.8	0.7	0.7	2.8	0.8	0.6	0.9	3.3
PER (x)	37.5	28.6	31.7	34.2	32.7	29.2	38.5	24.6	28.4
Growth (yoy, %)									
Net Sales	23	24	27	33	27	33	21	18	21
EBITDA	68	57	40	44	51	30	21	22	27
Other Income	21	(89)	(7)	(16)	(23)	61	1,175	98	46
Interest	2	(11)	(9)	(30)	(11)	(3)	98	1	16
Depreciation	(1)	8	21	48	18	31	43	23	29
PBT	160	83	57	48	76	38	13	29	29
PAT	203	120	65	50	93	36	21	31	32
Reported PAT	203	120	65	(34)	38	29	(26)	31	18

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2. Neutral: Within 0-10% to Index
3. Underperformer: Less than 10% to Index

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