INDIA RESEARCH | LOGISTICS | BSE SENSEX: 17879 | MARCH 18, 2011

NEUTRAL

Container Corporation of India

Management Meeting

Rs1187

Mkt Cap: Rs154bn; US$3.4bn

We recently had a discussion with the management of Container Corporation of India (Concor) for an update on the business. The management indicated that while the port volumes are showing traction over the past 2-3 months, Concor is not witnessing the same in its exim volumes. JNPT port, which accounts for almost 50-60% of Concor's volumes is registering flat volumes, while volumes are muted from Mundra and Pipavav ports due to limited rail line capacity. Further, the recent '*jat*' agitation has hampered the rail cargo movement from certain northern ICD's further impacting movement of exim and domestic cargo. On the other hand, Concor is losing volumes in the domestic segment due to the steep hike by Indian Railways in December 2010 on certain commodities. Accordingly, we believe Concor is likely to witness muted volume growth of 4.8% yoy in 4QFY11. While the volume growth is likely to be muted, we believe the control on empty running costs is likely to drive improved margins (350bps yoy). We have downgraded our FY11E and FY12E earnings estimates by 1% and 4% respectively to account for the lower volumes. Concor has largely remained insulated by the entry of private players in the medium term considering its strong competitive edge in the form of its infrastructure (large wagon fleet, pan India network of ICD and CFS's) as well as its strategic alliances to garner volumes and offer end to end logistics solutions to clients. However, the near term issues on volume growth in JNPT and frequent haulage rate hikes by Indian Railways is likely to impact earnings in near term. Consequently, we believe valuations at 16.6x FY12 earnings adequately capture its strong competitive edge as also the cash on books. Maintain Neutral on the stock with a target price of Rs1215/share.

Key financials

As on 31 March	FY08	FY09	FY10	FY11E	FY12E	FY13E
Net sales (Rs m)	33,473	34,172	37,057	38,629	43,079	48,740
% growth	*10.2*	*2.1*	*8.4*	*4.2*	*11.5*	*13.1*
Adj. net profit (Rs m)	7,505	7,915	7,867	8,360	9,299	10,412
Shares in issue (m)	130	130	130	130	130	130
Adj. EPS (Rs)	57.7	60.9	60.5	64.3	71.5	80.1
% growth	*7.8*	*5.5*	*(0.6)*	*6.3*	*11.2*	*12.0*
PER (x)	20.6	19.5	19.6	18.5	16.6	14.8
Price/Book (x)	4.8	4.1	3.6	3.1	2.7	2.5
EV/EBITDA (x)	15.5	14.5	13.7	12.4	10.7	9.2
RoE (%)	25.8	22.8	19.4	18.0	17.5	17.5
RoCE (%)	25.5	22.3	19.4	18.5	18.2	18.2

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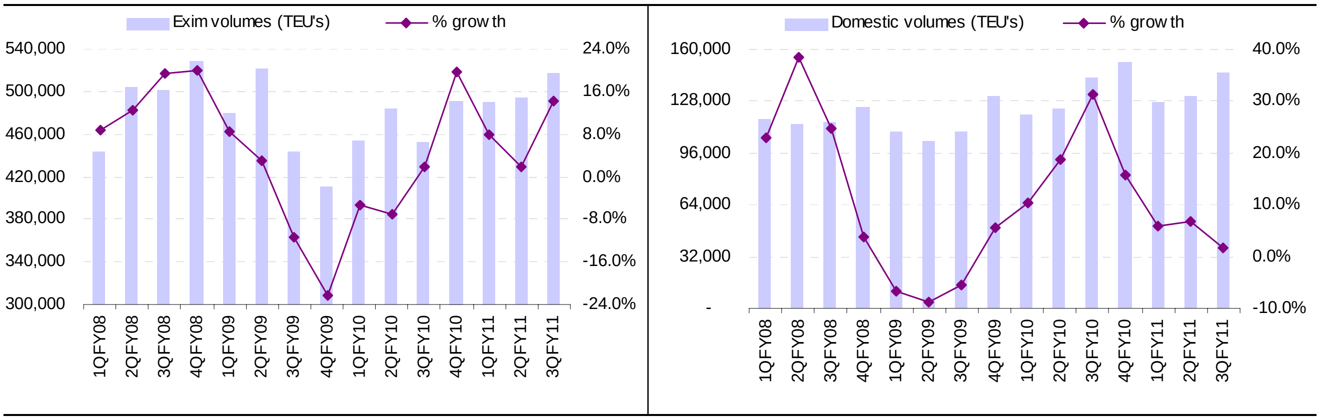
The key takeaways of our interaction with the management are:

❑ Volume growth liekly to be muted in 4QFY11

Concor had witnessed an 11% yoy volume growth (14% yoy in exim and 2% yoy in domestic) in 3QFY11 led by pick up in port volumes. While the port volume growth has continued into 4QFY11 as well, Concor has not witnessed the same growth in its exim volumes. Some of the key reasons are:

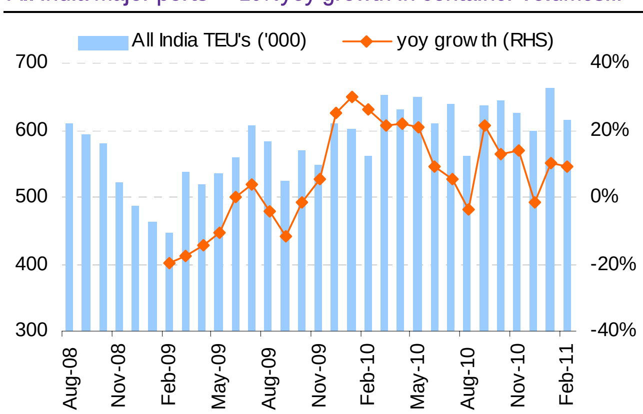
Trend in Concor's volume growth over the past few quarters



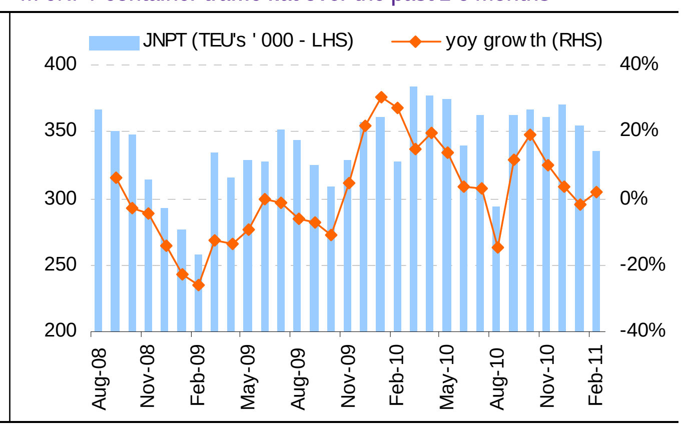
Source: Company; IDFC Research

JNPT port volumes flat: The JNPT port, which is Concor's key port for exim volumes, has witnessed flattish volume growth over the past 2 months (January 2011: -1.7% yoy; February 2011: +2.1% yoy) as the port is running at 100% capacity utilization. Accordingly, volumes for Concor have not grown from JNPT port which accounts for almost 50-60% of Concor's volumes.

All India major ports - ~10%yoy growth in container volumes...



... JNPT container traffic flat over the past 2-3 months



Source: IPA; IDFC Research

Mundra rail connectivity - an issue: The volumes at the Mundra port have been growing at a strong pace, however the container rail operators are not able to capitalize on the growth. The rail line connecting Mundra port to the NCR region is a single line, which limits the cargo movement between the port and the hinterland. Indian Railways (IR) has been focusing on the movement of bulk cargo from the port, which has resulted in slow movement of container rakes from and to the port. However, the management believes this is likely to be a temporary problem as the line is being expanded to accommodate double stacking, which will double the capacity for container rake movement. The double stacking is likely to be operational from May - June 2011 onwards.

'Jat' agitation impacts rail movement: The *'jat'* agitation in northern India has restricted the movement of rail traffic in certain northern ICDs such as Moradabad, Kanpur, etc. Accordingly, some export volumes and domestic volumes have been impacted by the slowdown as Indian Railways is moving passenger trains on these routes.

Hike in freight rates for domestic business: The steep hike in domestic freight rates of 50-200% from December 2010 onwards on select commodities has resulted in some clients shifting to road. Accordingly, Concor has witnessing a muted growth in domestic volumes.

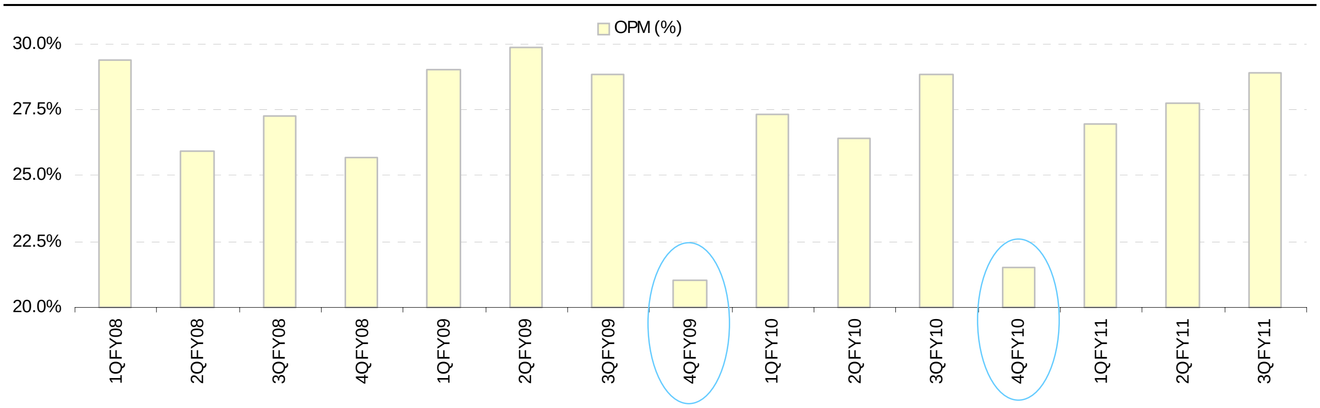
❑ Empty running in control relative to last year

In FY10, export import imbalance had resulted in severe empty running of almost 15-18%. The management mentioned that while the overall export-import trade has been largely balanced in FY11 in comparison to FY10, the imbalance at ports is yet continuing. Concor is witnessing higher exports from Mundra and higher imports from JNPT. Accordingly, it has to sometimes run empty rakes between Mundra and JNPT to balance out movement of containers.

❑ 4Q – typically a lean quarter due to volume based discount to clients

Concor had begun giving rebates and discounts to shipping lines based on the volumes handled through Concor in a year, which it gives to the shipping line in the 3rd quarter and the 4th quarter. Accordingly, the operating margins of the company are steeply lower in 4Q in comparison to the 9M period. While the trend would continue in 4QFY11, we expect the margins to expand on a yoy basis due to lower empty running and improved revenue mix in favor of exim volumes.

Operating margins fall sharply in 4Q due to volume discounts offered to clients



Source: Company; IDFC Research

❑ Capex focus maintained

Concor is likely to incur capital expenditure of Rs4.5-5bn in FY11 on additional wagons, ICD/CFS and other handling equipment at various facilities. The large investments into wagons is being undertaken to continue its dominant position and attract higher volumes. The capex will be funded through internal accruals. Concor has Rs21bn cash on hands.

❑ Maintain Neutral

We have downgraded our FY11E and FY12E estimates by 1% and 4% to an EPS of Rs64.3 and Rs71.5 respectively to factor in the slower volume growth. Concor has largely remained insulated by the entry of private players in the medium term considering its strong competitive edge in the form of its infrastructure (large wagon fleet, pan India network of ICD and CFS's) as well as its strategic alliances to garner volumes and offer end to end logistics solutions to clients. However, the near term issues on volume growth in JNPT and frequent haulage rate hikes by Indian Railways is likely to impact volumes and thereby mute earnings growth in near term. Consequently, we believe valuations at 16.6x FY12 earnings adequately capture its strong competitive edge as also the cash on books. Maintain Neutral on the stock with a target price of Rs1215/share.

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Explanation of Ratings:

1. Outperformer: More than 5% upside to Index
2. Neutral: Within 0-5% to Index (upside or downside)
3. Underperformer: More than 5% downside to Index

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