Company Flash

27 March 2007 | 6 pages

Gateway Distriparks (GATE.BO)

Buy: Rail Initiatives Continue to Gather Momentum

- What's new — GATE [through its subsidiary (GatewayRail)] and Concor are to form a 51-49 JV, which replaces the prior restrictive agreement between Concor and GATE that prohibited the latter from running its own trains until Oct/Nov08. Total outlay envisaged is Rs700m, albeit phase 1 capex will be around Rs210m (which GATE and Concor will fund through equity infusions).
- What's next — GATE's current business at the Garhi ICD will be transferred to the JV. GATE will earn lease rentals (as yet undecided) for use of its ICD. The JV will earn handling charges and ground rentals on the traffic through the Garhi ICD. The current capacity of the Garhi ICD is 60,000 TEUs pa, which should be sufficient to meet throughput generated in phase 1 of the train operation.
- Revenue and profitability — Whilst handling and other charges will be earned by the JV, haulage revenues and attendant expenses will be booked in GatewayRail. GATE's management forecasts it will earn EBITDA of cRs4-4500 / TEU on haulage operations – around Rs100m pa. Handling charges are estimated to add an additional c.Rs40m pa EBITDA (GATE's share in the JV).
- Margins at Mumbai to remain constrained — We expect margins at GATE's JNPT facility to remain depressed over the next 6 months due to increased competition. This remains an area of concern. However, we are satisfied with the trajectory of the train operations, and believe that GATE is taking the right steps to develop an integrated logistics business model.

Buy/Medium Risk	1M
Price (26 Mar 07)	Rs162.10
Target price	Rs216.00
Expected share price return	33.3%
Expected dividend yield	2.5%
Expected total return	35.7%
Market Cap	Rs14,973M
	US$347M

Statistical Abstract

Year to 31 Mar	Net Profit (RsM)	Diluted EPS (Rs)	EPS growth (%)	P/E (x)	P/B (x)	ROE (%)	Yield (%)
2005A	346	4.61	54.2	35.2	7.3	28.0	1.2
2006A	723	7.84	70.0	20.7	2.6	19.5	1.9
2007E	860	9.33	19.0	17.4	2.4	14.4	2.5
2008E	1,044	11.32	21.4	14.3	2.2	16.1	3.1
2009E	1,262	13.68	20.9	11.8	2.0	17.7	3.1

Source: Powered by dataCentral

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See Appendix A-1 for Analyst Certification and important disclosures.

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Gateway Distriparks

Company description

Incorporated in 1994, GDL offers logistics support services to export-import containerized cargo traffic in India. After commencing operations in 1998 with a single container freight station (CFS) at Mumbai, the company has acquired CFS facilities at Chennai and an inland container depot (ICD) at Garhi Harsaru (near Delhi). It is also developing a CFS at Vizag. The company has emerged as the largest private-sector player in the segment and has a presence on the east and west coasts of India, as well as the Delhi–Gurgaon–Manesar industrial belt.

Investment thesis

We have a Buy/Medium Risk (1M) rating on GDL, with a target price of Rs216. We estimate that India's containerized traffic will post a 14-15% CAGR over the next decade, benefiting from a low base as well as increased investment in the country's container handling terminals. Containerized traffic typically grows at 2-2.5x economic growth. Assuming base-case GDP growth of 6%, containerized traffic should grow at a rate of 15% in the long term. With facilities at key ports such as JNPT and Chennai, GDL looks well positioned to benefit from growth in container traffic and port-based logistics. The company has a head start over other private-sector entities, and has managed to garner around 20% market share of CFS addressable throughput at JNPT. We are positive on the train business. Although its margins are lower than at the CFS business, we believe GDL's business model is becoming more robust as its operations extend vertically through the logistics chain.

Valuation

Our 12-month target price of Rs216 is based on (1) the average of 13.3x FY08E EV/EBIT, or Rs173, and a DCF-based fair value of Rs251, and (2) Rs4 for the Punjab Conware facility. Considering GDL's strong growth prospects, but adjusting for its inherently riskier business model, we assign a 10% premium to the CY07E peer group multiple to arrive at 13.3x EV/EBIT for FY08E. We employ the EV/EBIT methodology because it reflects the depreciation costs associated with GDL's large capex program. At this multiple, we arrive at a valuation of Rs173 for GDL. We also utilize a DCF methodology because it captures growth in earnings and cash flows for GDL's train project, whose roll-out we view as crucial for the long-term growth prospects of the company. Our DCF-based target price of Rs251 is much higher than the EV/EBIT-based fair value. The EV/EBIT methodology does not fully capture the growth potential of the train business, which is a long-term story given that the near-term valuations are depressed due to high capex. At our target price of Rs216, the stock would trade at 18.7x FY08E P/E, which is at a premium to the 16.5x P/E of the peer group given GDL's higher growth potential.

Risks

We continue to rate GDL as Medium Risk, deviating from the High Risk rating assigned by our quantitative model, which tracks 260-day share price volatility. We rate the stock Medium Risk because of the following: (1) Strong secular growth prospects for the ports-related logistics business in India with low containerized traffic penetration levels should drive long-term growth; and (2) Increasing momentum of investment in ports and container terminals is driving development of CFSs and ICDs, which should support growth in container traffic. The key downside risks to our target price include: (1) GDL's business model is undergoing transition. The entry into rail-based logistics should strengthen GDL's business model in the long term, but near-term profitability could suffer; (2) Execution risks with the rail-logistics business will persist; (3) Relatively low entry barriers into the industry, suggesting intensifying competition. We believe this could impact profitability of the incumbents, as pricing/TEU remains static or even declines in the face of competition.

Appendix A-1

Analyst Certification

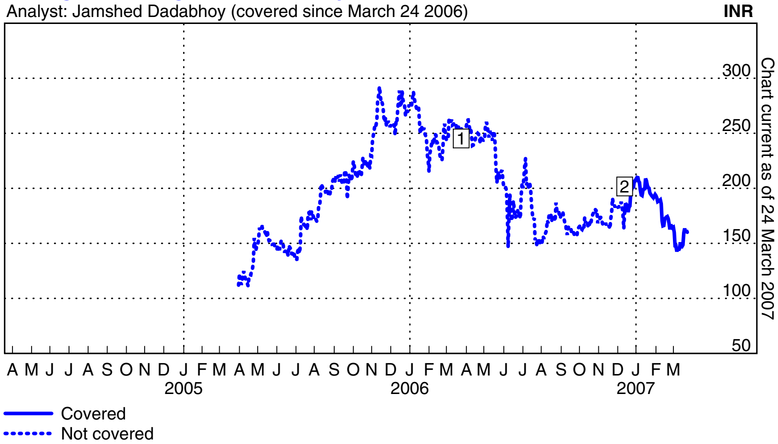
I, Jamshed Dadabhoy, research analyst and the author of this report, hereby certify that all of the views expressed in this research report accurately reflect my personal views about any and all of the subject issuer(s) or securities. I also certify that no part of my compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

IMPORTANT DISCLOSURES

Gateway Distriparks (GATE.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Jamshed Dadabhoy (covered since March 24 2006)



#	Date	Rating	Target Price	Closing Price
1:	24 Mar 06		-	255.80
2:	13 Dec 06	*1M	*216.00	179.20

*Indicates change.

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