ICICI direct.com
On-line Share Trading

Initiating Coverage

Great Eastern Shipping (GESHIP)

Current price Rs 355	Target price Rs 505
Potential upside 42%	Time Frame 12-15 months

OUTPERFORMER

Analyst's Name
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Great sailing…

Great Eastern Shipping Corporation (GESCO), India's largest private sector shipping company, is poised to witness steady growth in revenue and earnings. Consistent growth in its shipping business and an exponential increase in the nascent offshore business (184% CAGR in revenue over FY07-10E), backed by its aggressive fleet expansion over the next two years with sustainable day rates would enable it to report a 13.7% CAGR in earnings.

- **Diversified business model**

GESCO's has a fleet with equitable presence in the crude, product and dry bulk segments. Its presence in the lucrative offshore segment is also increasing. This diversification enables the company maintain steady and consistent growth in revenues and tide over volatility in any specific segment.

- **Ability to manage business cycles**

The company has displayed exceptional ability in managing the cyclical business risks. Well-timed fleet purchases during downturns, and selling old vessels during a phase of rising asset prices have enabled it ride the volatility in shipping cycle and maintain steady earnings growth. We expect a 13.7% CAGR in net profit over FY07-10E.

- **Expansion of offshore fleet to boost revenues**

GESCO, through its subsidiary, Greatship India, is aggressively scaling up its offshore fleet. It plans to expand its fleet size from 3 vessels in FY07 to 20 by FY10E. We expect contribution from offshore revenues to increase from 1% in FY07 to 15.5% in FY10E.

Valuation

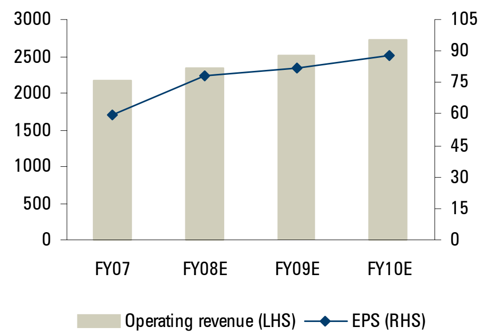
GESCO is on par with its global peers, or even better on various financial parameters. Its financials are on a sound footing with steady revenue growth, operating margin in excess of 50%, cash-to-total assets ratio of 24%, and low debt to equity ratio of 0.7x. However, we believe these positives have not been factored into the stock price, which we feel is undervalued compared to its peers. We have considered different valuation tools to arrive at a target price of Rs 505.

Exhibit 1: Key Financials

Year to March 31	FY07	FY08E	FY09E	FY10E
Operating revenue (Rs crore)	2165.96	2343.90	2505.16	2723.89
Net Profit (Rs crore)	907.37	1186.99	1247.96	1335.40
Shares in issue (in crore)	152.27	152.27	152.27	152.27
EPS (Rs)	59.59	77.95	81.96	87.70
% Growth	6.0%	30.8%	5.1%	7.0%
PER (x)	6.0	4.6	4.3	4.1
Price / Book (x)	1.73	1.33	1.06	0.87
EV/EBIDTA (x)	6.08	5.94	5.55	5.10
RoNW (%)	29.03%	29.17%	24.52%	21.61%
RoCE (%)	19.84%	15.72%	14.54%	13.45%

Source: ICICIdirect Research

Sales & EPS trend



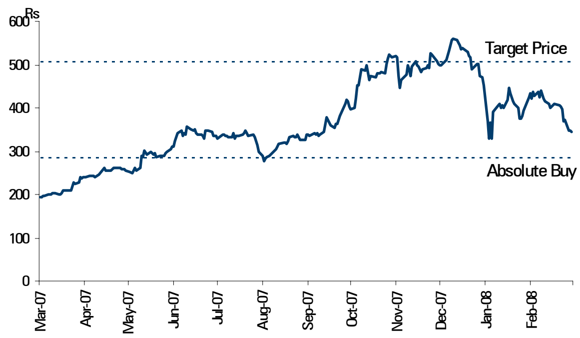
Stock Metrics

Bloomberg code	GESCO IN
Reuters code	GESC.BO
Face Value (Rs)	10
Promoters holding	29.38%
Market Cap	Rs 5025 crore
52 Week H/L	185 / 626
Sensex	16086
Average volume	102985

Comparative return metrics

Stock return	3 M	6M	12M
SCI	-24%	-8%	12%
Mercator Lines	-52%	-15%	81%
Great Offshore	-32%	-28%	4%
GE Shipping	-35%	-3%	68%

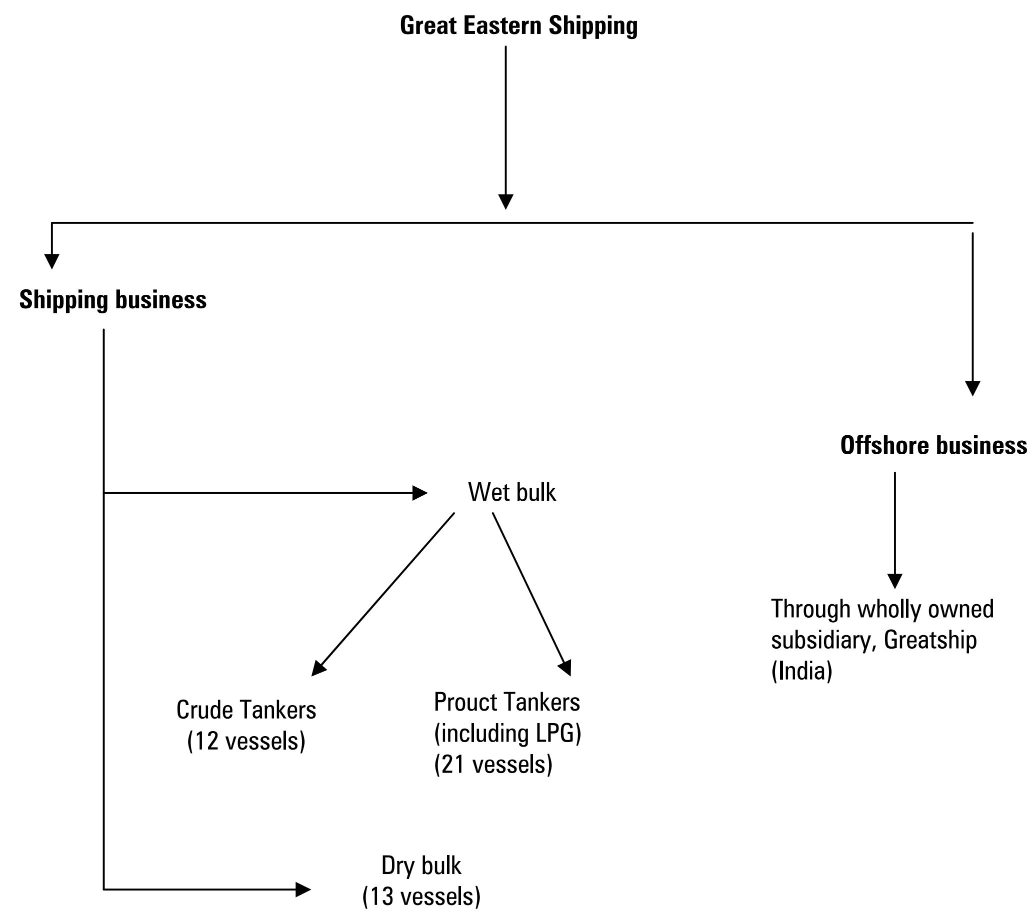
Price trend



Company Background

GESCO is India largest private sector shipping company. It is promoted by Sheths' and Biwandiwala's. GESCO operates a fleet of 46 vessels (33 tankers and 13 dry bulk carriers) and has a presence in the crude, product and dry bulk segments. It has also forayed into the lucrative offshore vessels segment through its wholly-owned subsidiary, Greatship (India) Ltd. The company with its diverse asset base and global operations has been able to ride the volatility in the shipping industry and has been able to maintain a 25 years of uninterrupted dividend payment track record.

Exhibit 2: Business segments



Source: Company, ICICIdirect Research

GESCO currently has a shipping fleet of 46 vessels. It is scaling up operations by adding 8 vessels by Q1FY12. The company is also aggressively expanding its offshore fleet through its subsidiary Greatship (India) Ltd. Greatship would add 17 vessels by the end of Q4FY10.

Share holding pattern

Shareholder	% holding
Promoters	29.38
Institutional investors	34.82
Other investors	44.55
General public	7.93

Promoter and Institutional holding trend

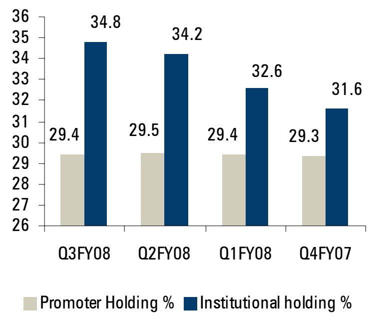


Exhibit 3: Existing fleet size

Vessel type	Number	Average age (years)
Crude oil carriers	12	7.5
Product carriers	19	13.3
LPG carriers	2	24
Dry bulk carriers	13	13.5

Source: Company, ICICIdirect Research

Committed capex of Rs 1560 crore for expansion of fleet size

Exhibit 4: Capacity additions

Vessel type	Number	Expected delivery
Product carriers	2	Q2FY09
Product carriers	2	Q3FY10
Dry bulk carriers	2	Q4FY10
Dry bulk carriers	1	Q4FY11
Dry bulk carriers	1	Q1FY12

Source: Company, ICICIdirect Research

Rs 2490 crore capex to expand offshore fleet capacity

Exhibit 5: Offshore fleet profile

Vessel type	Number	Expected delivery
PSVs	4	Existing
80T AHTS	1	Q4FY08
PSV	2	Q2FY09, Q3FY09
80T AHTS	2	Q4FY09
80T AHTS	1	Q4FY09
80T AHTS	2	Q1FY10
80T AHTS	1	Q2FY10
Multipurpose support vessel	4	Q2FY10, Q4FY10
MSV	2	Q3FY10, Q4FY10
350 feet jack up rig	1	Q3FY10

Source: Company, ICICIdirect Research

INVESTMENT RATIONALE

- **Diversified business model**

GESCO has one of the most robust and diversified business models among shipping companies with a presence across all vessel categories. Over the years, it has been able to attain a critical mass in each of the vessel category it operates in. A spreadout presence across different vessel categories is paramount for a shipping company as the sector is affected by business cycles and economic growth across the globe. GESCO has an equitable presence in crude carriers, product carriers and dry bulk carriers. The growth in these segments is driven by varied factors. For example, crude demand impacts demand for drude carriers. Demand for crude itself is impacted by factors such as crude production and seasonal variance in demand like severe or normal winters, etc.

On the other hand, demand for dry bulk carriers depends on global trade in commodities like steel and coal. Having a equitable presence across these vessel categories insulates GESCO from the vagaries of a downturn in any particular segment. Further, the company is aggressively expanding its presence in offshore vessels shipping segment. This would further diversify its operations and de-risk revenue and earnings. We believe this robust and diversified business model would enable GESCO sustain its revenues and grow at a steady pace over the longer term.

GESCO's presence across different vessel categories insulates it from the vagaries of downturn in any specific business segment

Exhibit 6: Revenue break-down by category (%)

Revenue category	FY06	FY07	FY08E	FY09E	FY10E
Crude carriers	33.8	36.7	25.7	24.6	21.7
Product carriers	38.0	35.7	30.1	30.5	27.8
LPG carriers	3.4	3.1	2.6	2.6	2.3
Dry bulk carriers	19.1	16.7	32.3	28.1	23.7
Offshore	0.0	0.9	2.6	5.7	15.5
Others	5.7	6.9	6.7	8.5	9.0

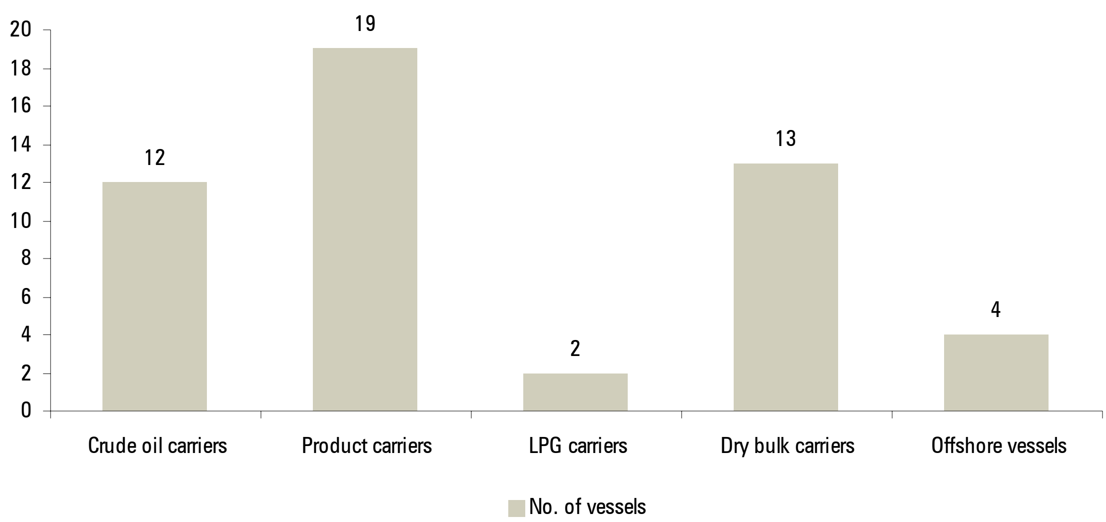
Source: Company, ICICIdirect Research

Exhibit 7: Capacity by vessel category

Vessel type	Capacity (million dwt)
Crude carriers	1.54
Product carriers	0.77
LPG carriers	0.05
Dry bulk carriers	0.72

Source: Company, ICICIdirect Research

Exhibit 8: Number of vessels by category

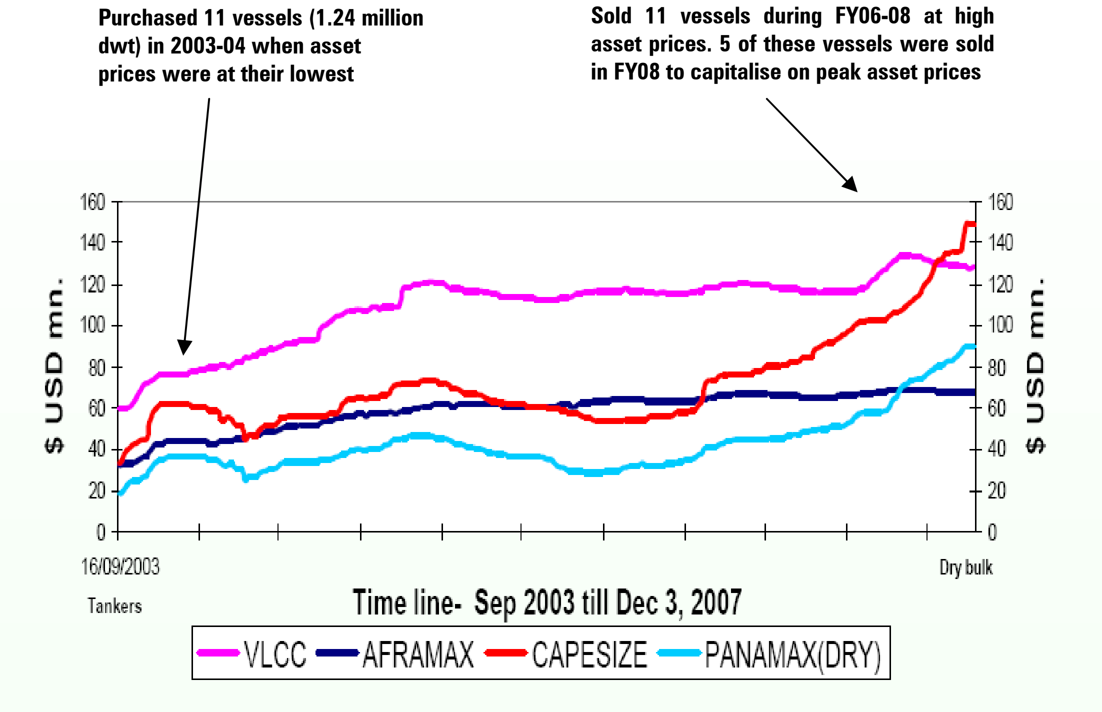


Source: Company, ICICIdirect Research

- **Ability to mange business cycles**

The management has displayed exceptional ability in managing the cyclical business risks associated with the shipping sectot. It has timed fleet purchases during phases of downturn and sold old vessels when asset prices were rising. Over the years, the company has maintained a spot and time charter mix ratio of 45:55. The balanced mix of spot and time charters has enabled the company capitalise on higher rates in the spot market, and also have stability of revenues by having more than half its fleet on time charter.

Exhibit 9: Vessel sales and purchases timed according to business cycle



Source: Company, ICICIdirect Research

Exhibit 10: Profit on sale of vessels trend (Rs crore)

	FY04	FY05	FY06	FY07	9MFY08	FY09E	FY10E
Operating revenues	1390.47	2132.37	2036.06	2166	1843	2505.16	2723.89
Profit on sale of vessels	10.33	33.64	346.58	136.31	243.74	325.00	250.00
Net profit margin (%)	31.4%	39.7%	42.0%	41.9%	57.4%	49.82%	49.03%
Net profit	437.01	845.81	856.16	907.36	1057.4	1247.96	1335.40
Profit on sale of vessels (% to net profit)	2.4%	4.0%	40.5%	15.0%	23.1%	26.0%	18.7%

Source: Capitaline, ICICIdirect Research

GESCO has effectively countered the slowdown in operating revenues by timing the sale of its vessels and maintain a healthy net profit margin

We believe that management has a good understanding of the shipping business cycle. GESCO is likely to sell some of its old vessels to take advantage of the firm asset prices prevailing at present. We expect contribution from other income to be 26% of net profit in FY09 and 18.7% in FY10.

Offshore fleet expansion to boost revenues

GESCO has promoted a wholly-owned subsidiary, Greatship India, to capitalise on increasing opportunities in the lucrative offshore segment. Though the offshore foray is still at a nascent stage, we believe that it holds significant potential and would be the trigger for revenue growth in next 2-3 years. GESCO is aggressively expanding its offshore fleet size from 3 vessels at present to 20 by Q4FY10. It has committed a capex of Rs 2,490 crore for this expansion. The increase in E&P (exploration & processing) activities from the current US$55 billion to US$65 billion by 2011 is expected to give a tremendous boost to offshore services. We expect the contribution from offshore revenues to increase from 1% in FY07 to 15.5% in FY10.

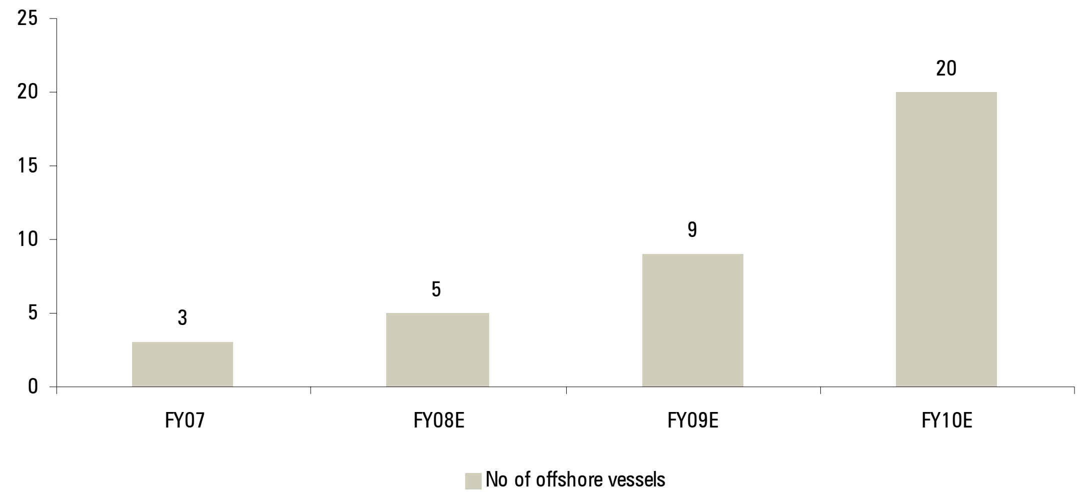
Exhibit 11: Offshore fleet profile

	Number	New/Secondhand
Anchor Handling Tug Support Vessels	8	New
Platform Supply Vessels	5	New
Multi Purpose Supply & Support vessels	3	New
Multi Support Vessels	2	New
Platform / ROV Support Vessels	2	New

Source: Company, ICICIdirect Research

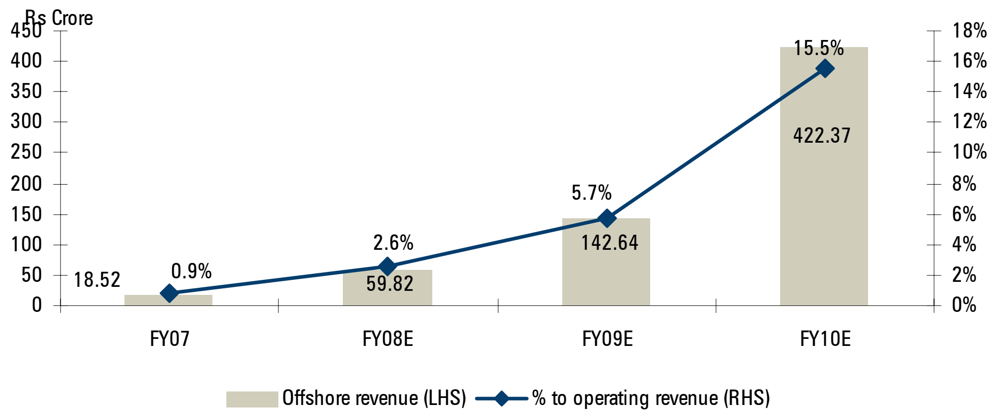
Expansion of ofshore fleet size would result in a 184% CAGR in revenue from offshore services over FY07-10E. Further, the contribution from this segment would increase from 0.9% in FY07 to 15.5% in FY10E

Exhibit 12: Scaling up offshore fleet size



Source: Company, ICICIdirect Research

Exhibit 13: Increasing contribution of revenues from offshore services



Source: ICICIdirect Research

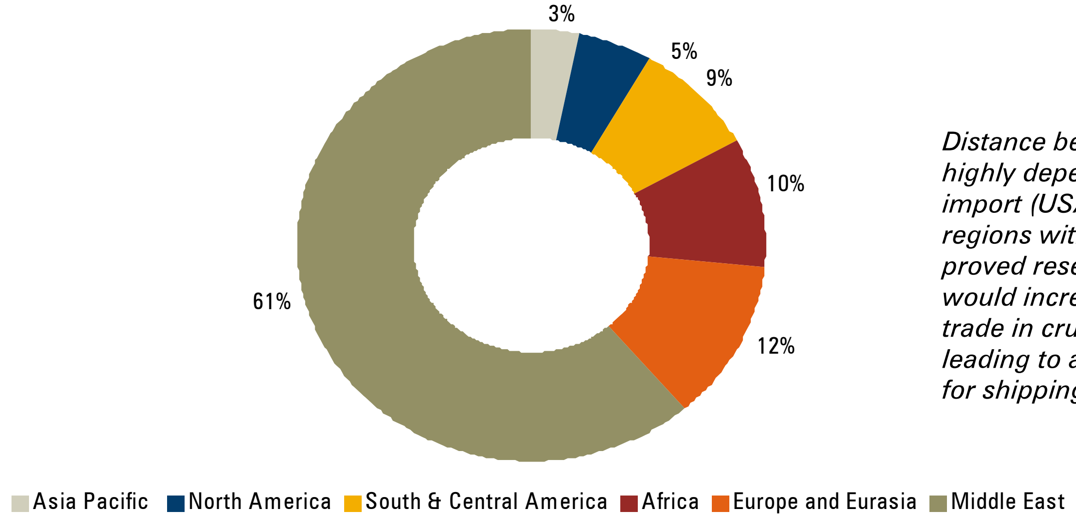
INDUSTRY OVERVIEW

- **Shipping sector to remain buoyant**

The shipping industry is the primary mean of international transportation of various essential commodities. The global shipping industry is broadly classified into wet bulk, dry bulk and liners. Demand for shipping is mainly driven by the strength of the global economy and global trade. Demand for tankers is driven by the oil demand, while dry bulk segment is influenced by demand for commodities, primarily iron ore and coal.

According to Lloyds Register/Fairplay World Fleet Statistics-January 2006, the world's cargo carrying fleet is 50,214 ships of 101.45 crore GT with an average age of 20 years. Oil tankers and dry bulk carrier tonnage constitute more than 60% of the world fleet. The increasing demand for oil and commodities like iron ore and coal is likely to keep the tonne-mile demand for shipping buoyant on account of geographical distance between the place of production and consumption of oil and commodities.

Exhibit 15: Distribution of proved reserves of crude oil in 2006 (%)



Distance between regions highly dependant on crude oil import (USA & Europe) and regions with concentration of proved reserves (Middle East), would increase the Sea borne trade in crude oil, thereby leading to a buoyant demand for shipping

Source: BP statistical review of world energy June 2007, ICICIdirect Research

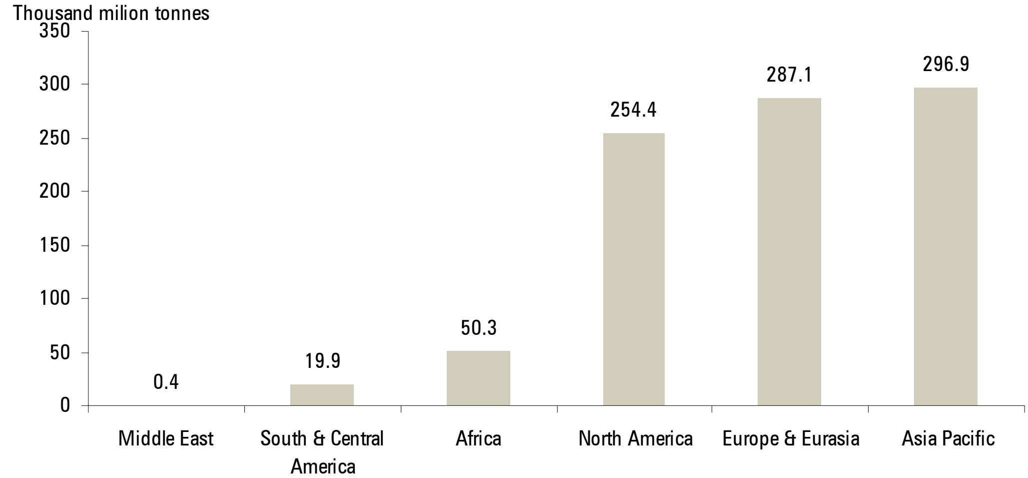
Exhibit 16: Crude oil - trade movement

Thousand barrels daily	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	Change 2006 over 2005	2006 share of total
Imports													
USA	9400	9907	10382	10550	11092	11618	11357	12254	12898	13525	13612	0.6%	25.9%
Europe	10472	10421	11017	10670	11070	11531	11895	11993	12538	13261	13461	1.5%	25.6%
Japan	5685	5735	5259	5346	5329	5202	5070	5314	5203	5225	5201	–0.5%	9.9%
Rest of World*	13835	14827	14438	15050	15880	16436	16291	17191	18651	19172	20287	5.8%	38.6%
Exports													
USA	978	976	1011	956	890	910	904	921	991	1129	1317	16.6%	2.5%
Canada	1484	1492	1603	1520	1703	1804	1959	2096	2148	2201	2330	5.8%	4.4%
Mexico	1656	1767	1770	1739	1814	1882	1966	2115	2070	2065	2102	1.8%	4.0%
S. & Cent. America	3011	3219	3240	3145	3079	3143	2965	2942	3233	3528	3681	4.3%	7.0%
Europe	1540	1463	1344	1851	1967	1947	2234	2066	1993	2149	2173	1.1%	4.1%
Former Soviet Union	3239	3413	3569	4019	4273	4679	5370	6003	6440	7076	7155	1.1%	13.6%
Middle East	17170	18184	18702	18341	18944	19098	18062	18943	19630	19821	20204	1.9%	38.4%
North Africa	2756	2743	2712	2726	2732	2724	2620	2715	2917	3070	3225	5.1%	6.1%
West Africa	2916	3102	3094	2985	3293	3182	3134	3612	4048	4358	4704	7.9%	8.9%
Asia Pacific†	3861	3841	3496	3543	3736	3914	3848	3978	4189	4243	4312	1.6%	8.2%
Rest of World*	780	690	556	791	940	1506	1551	1361	1631	1542	1359	–11.8%	2.6%

Source: BP statistical review of world energy June 2007, ICICIdirect Research

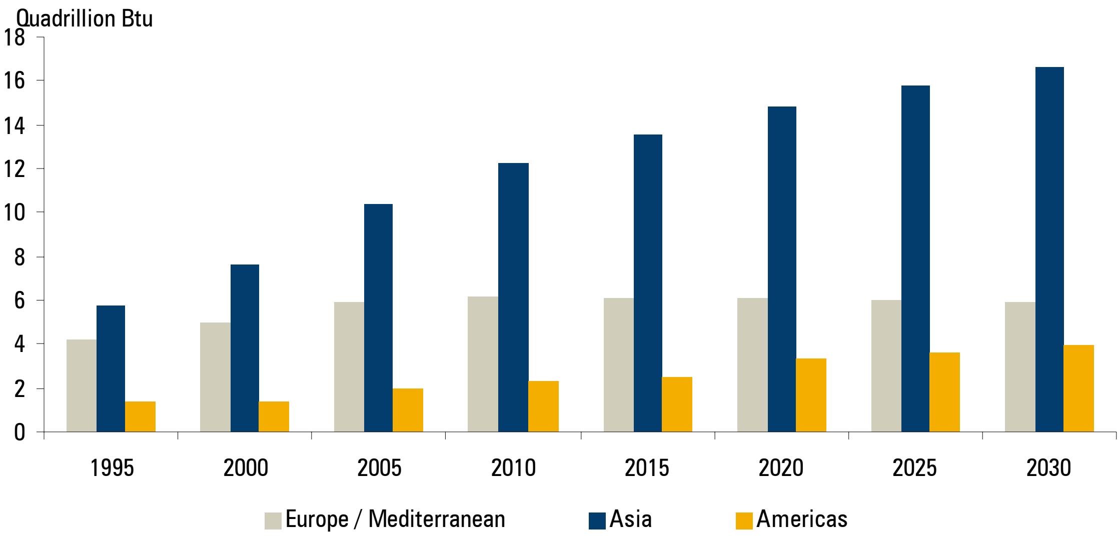
Increasing demand for energy is driving demand for fuel like coal, the proven reserves of which are spread out globally. World coal trade is projected to grow at an annual rate of 1.5% from 18.4 quadrillion BTU in 2005 to 26.5 quadrillion BTU in 2030. Australia is the largest exporter of high quality coal, while China is both an exporter and importer of coal. China bears a huge significance on global coal trade. Demand for energy in China is growing at a rapid pace along with its economic growth. China is expected to satisfy its requirement of coal from its own mines and may curtail its exports to other countries like Japan. These countries would have to source their coal requirement from other coal exporting countries like Australia, Indonesia, Vietnam and Russia resulting in higher tonne-mile demand for shipping due to the increased distance between the producing region and the consuming region.

Exhibit 17: Coal reserves (2006)



Source: BP statistical review of world energy June 2007, ICICIdirect Research

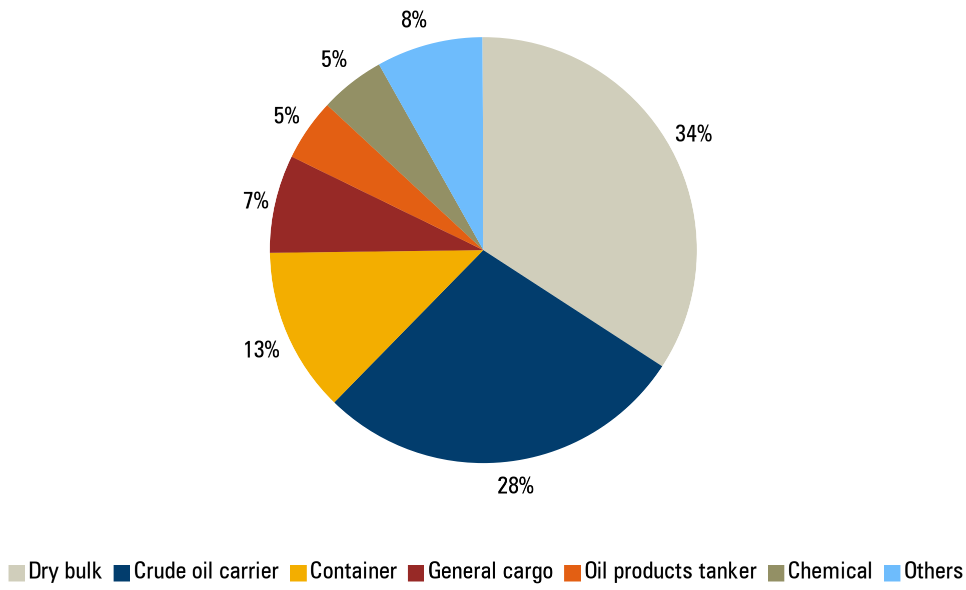
Exhibit 18: Coal imports by major importing regions (1995-2030)



Growth in global coal trade to increase tonne-mile demand for shipping

Source: IEA, ICICIdirect Research

Exhibit 19: Category wise world shipping gross tonnage (%)



Source: Lloyds Register/Fairplay World Fleet Statistics-January 2006, ICICIdirect Research

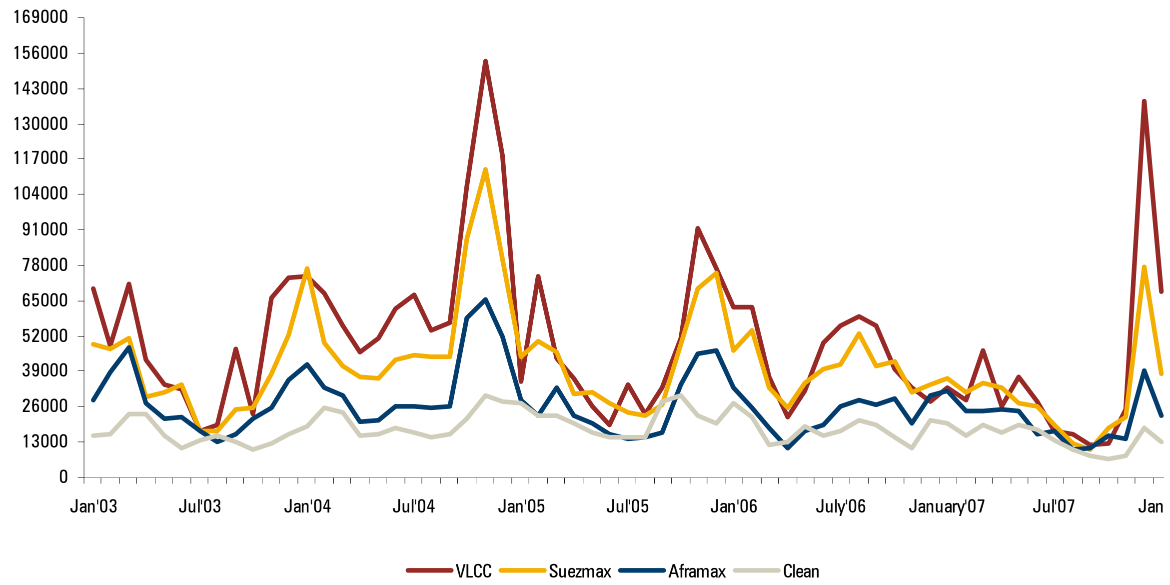
Tanker market

Tanker companies transport crude oil from ports near production fields to ports near major refineries. Crude oil tankers are used to transport crude oil from fields in the Middle East, North Sea, Africa and Latin America to refineries around the world. Product tankers carry refined products from refineries to terminals at demand centres. Crude oil is the single largest commodity in international trade. This makes crude tankers an important segment. An International Energy Agency (IEA) study has highlighted that even in 2030, crude would remain a dominant segment for energy generation at 34 per cent of total requirements. Besides, the concentration of production and consumption clusters in different geographies makes crude tanker trade a more sustainable business opportunity.

Tanker rates are very competitive and are based on two main factors —demand for petroleum shipments and the capacity of the industry to accommodate those shipments (tanker supply). The tanker demand is measured in tonmiles, and prices depend on the locations of the production and refining destinations, geopolitical events that may alter shipping routes, energy demand and inter-regional supply imbalances (the tanker capacity can sometimes be available, but not in the right part of the world).

Tanker rates have been very volatile over the years and had touched astronomical levels in November 2004 on account of surge in crude oil demand and the limited availability of tankers. The present tanker rates are down significantly from earlier high levels and we expect the rates to rebound from hereon owing to increasing movement of crude and limited availability of tankers due to scrapping of old tankers with age more than 20 years. Overall more than 40% of the tankers, representing 14% of total tonnage are above the age of 20 years.

Exhibit 20: Tanker rate movement (US$/day)



Source: Company, ICICIdirect Research

Freight rates of crude carriers to move in narrow band, while product carrier freight rates to remain soft on account of higher fleet addition

Exhibit 21: International tanker fleet

	2002		2006		Average growth rate	
Ship type	**Number**	**DWT**	**Number**	**DWT**	**Number**	**DWT**
Crude oil tankers	3672	232.9	3556	257.1	-0.8	2.5
Product tankers	2302	47.6	2467	58.8	1.7	5.4
Oil/Chemical tankers	1337	22.7	1840	37.6	8.3	13.4
Chemical tankers	1291	8.5	1354	9.9	1.2	3.9
liquid gas tankers	1114	19.0	1184	24.2	1.5	6.2
Total	**9716**	**330.7**	**10401**	**387.6**	**1.7**	**4.0**

Ships of 300gt and over, tonnage in million
Source: ISL, ICICIdirect Research

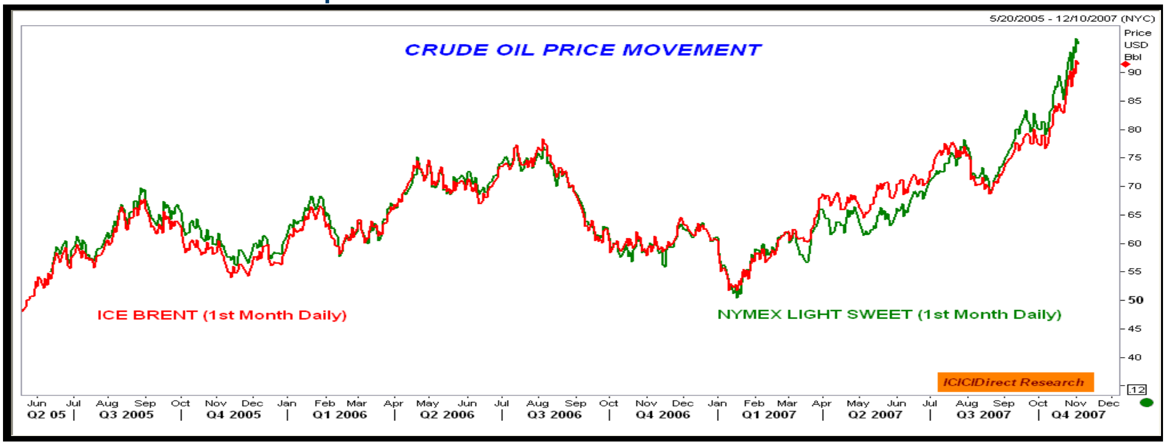
Exhibit 22: World Fleet addition

	2007	2008	2009	2010
Crude Oil tankers	6.7%	7.7%	13.8%	10.7%
Product Tankers	12.0%	9.9%	8.8%	4.3%

Source: Company, ICICIdirect Research

The crude oil carrier market is driven by world energy demand and supply patterns. Crude carrier freight rates depend on the location of refineries and the presence of pipelines on the trade route. With crude trading at all time peak, the level of E&P activities would increase and result in higher demand for crude shipping. The freight rates for crude carriers are likely to move in a narrow band.

Exhibit 23: International crude prices



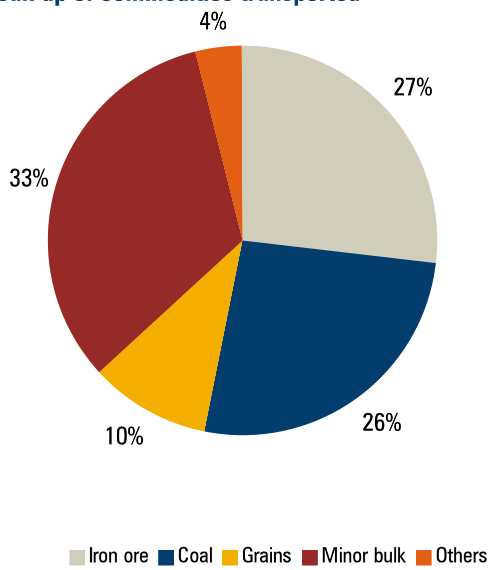
Source: Bloomberg, ICICIdirect Research

The product carrier freight rates are likely to remain soft on account of higher fleet addition between FY07-09.

Dry bulk segment

Dry bulk refers to those commodities, which are amenable to shipment loose and in bulk as full loads of homogenous cargo. Majority of the trade in the dry bulk segment is dominated by iron ore, coal, grain, bauxite/alumina, which constitute more than 60% of the dry bulk trade.

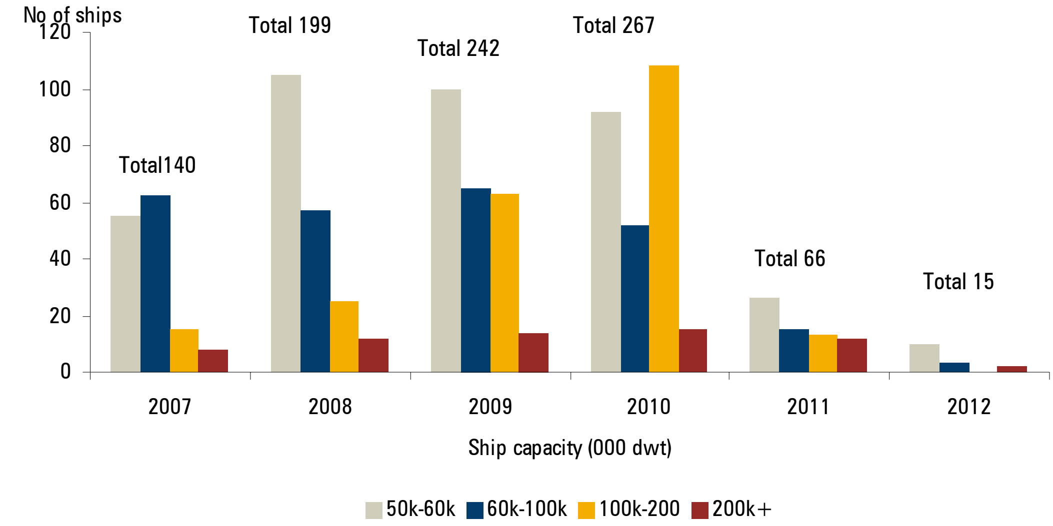
Exhibit 24: Break-up of commodities transported



Source: Company, ICICIdirect Research

The demand growth in the dry bulk segment has been driven by the booming steel industry and high demand for coal in Asia. The growth of the Chinese economy and its booming steel industry has clearly been the most important factor behind the surge. It is estimated that the Chinese and the Indian economies are responsible for more than half the demand growth seen in the last few years.

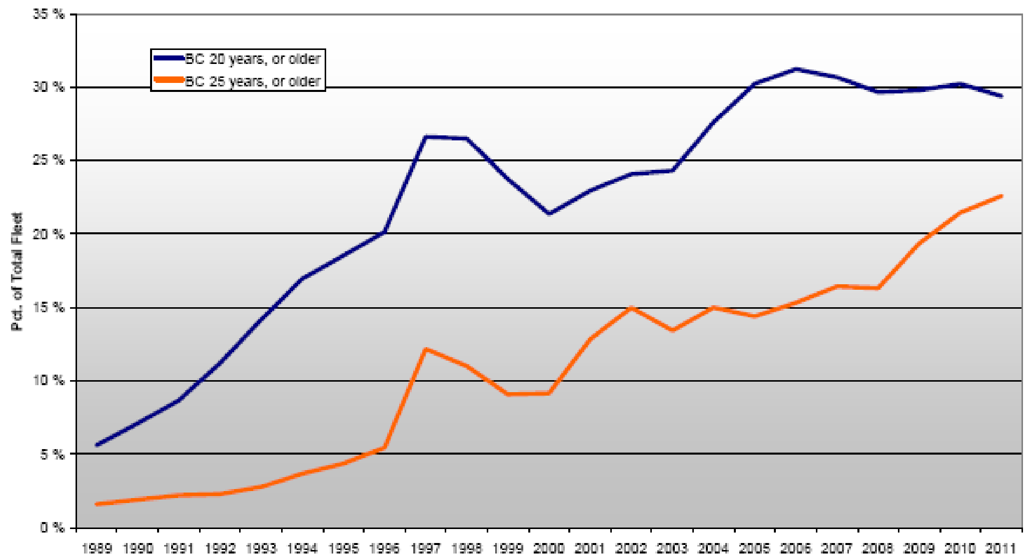
Exhibit 25: Dry bulk fleet addition



Source: Fearnley Consultations, ICICIdirect Research

Exhibit 26: Dry bulk fleet ageing trend

32% of the fleet is above 20 years age & 17% is above 25 years

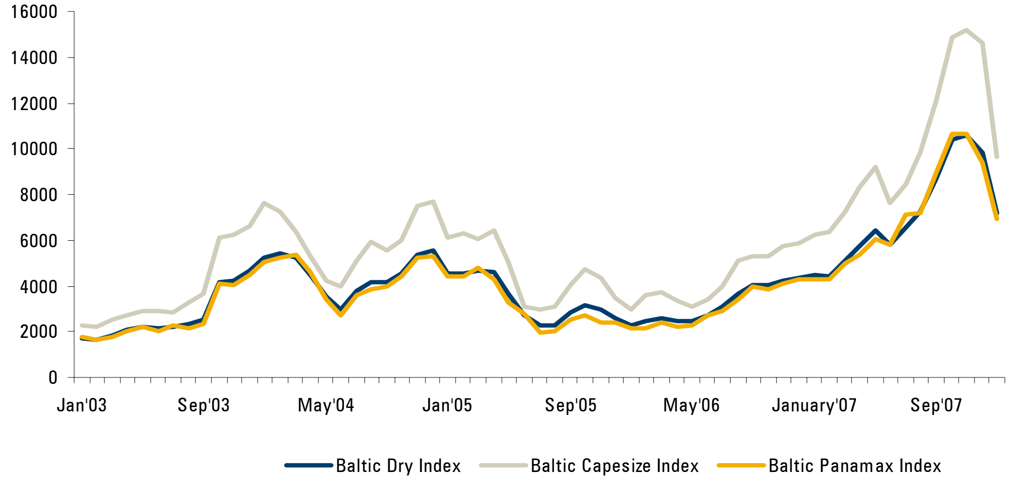


Strong commodity transportation demand and an ageing fleet with limited immediate additions to the fleet likely to keep the day rates firm

Source: Fearnley Consultants, ICICIdirect Research

The dry bulk vessels order book has increased by 47% in 2007. The dry bulk indices had touched historical high in 2007 and have touched a all time peak in November 2007. During the last 3 months the dry bulk indices have corrected significantly and have come down by more than 40%. We expect the rates to remain stable with a positive bias as the immediate addition to the fleet is not huge and the more than 45% of the fleet is over 20 years of age and would require to be replaced in the next five years.

Exhibit 27: Dry bulk indices movement



Source: Company, ICICIdirect Research

Offshore supply vessels

Exploration activities are sensitive to the price of crude and tend to increase and decrease with the movement in the price of crude. Crude prices have risen by more than 50% from their January2007 level and are at an all time high. India's oil demand is expected to grow at 6%-8% per annum, which is likely to fuel further increase in the E&P activities. The growth in E&P activities will be mainly driven by offshore exploration as 67% of India's expected prognostic hydrocarbon resources are located offshore. Further, out of the NELP blocks, 58.8% are offshore blocks. Heightened offshore E&P activities would drive demand for offshore vessels, as vessels required to support offshore activities will increase significantly. Drilling activity is moving deeper into the sea resulting in increased demand for high-powered and technically superior OSVs. OSVs are likely to earn higher day rates owing to the strong demand scenario and a premium owing to better technology.

Increasing investments in the E&P segment would increase the demand for OSVs and with 65% of the fleet over 20 years of age and new deliveries not sufficient to meet demand, vessel utilization levels are expected to increase leading to higher day rates for OSVs

Exhibit 28: Hydrocarbon prognostic resources

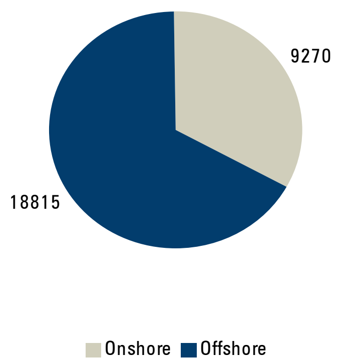
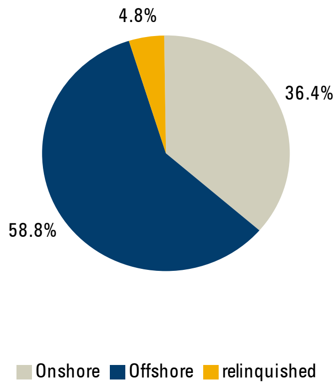


Exhibit 29: NELP block classification



Source: Industry, ICICIdirect Research

Exhibit 30: Global offshore vessels fleet summary

	Current Fleet	On order	% of order book to current fleet
AHTSV	2085	493	23.60
PSV	1517	241	15.90
Others	1578	172	10.90

Source: Industry, ICICIdirect Research

RISKS & CONCERNS

- **Cyclical nature of shipping industry**

Revenues of shipping companies are exposed to the volatility and cyclical nature of the industry.

- **Decline in freight rates**

Any substantial downward movement in global freight rates could impact the revenues of the company.

- **Regulatory risk**

Phasing out of single-hull vessels has been brought forward to 2010 from 2015. Any further change in the regulation requiring phasing out of such vessels earlier than 2010 would impact the company's business and financials.

- **Vulnerability to exchange rate fluctuations**

A significant portion of the company's revenues are denominated in US dollars and other foreign currencies. Any significant appreciation of the Indian rupee against these currencies can impact the revenue and profitability of the company.

- **Delay in delivery of new vessels**

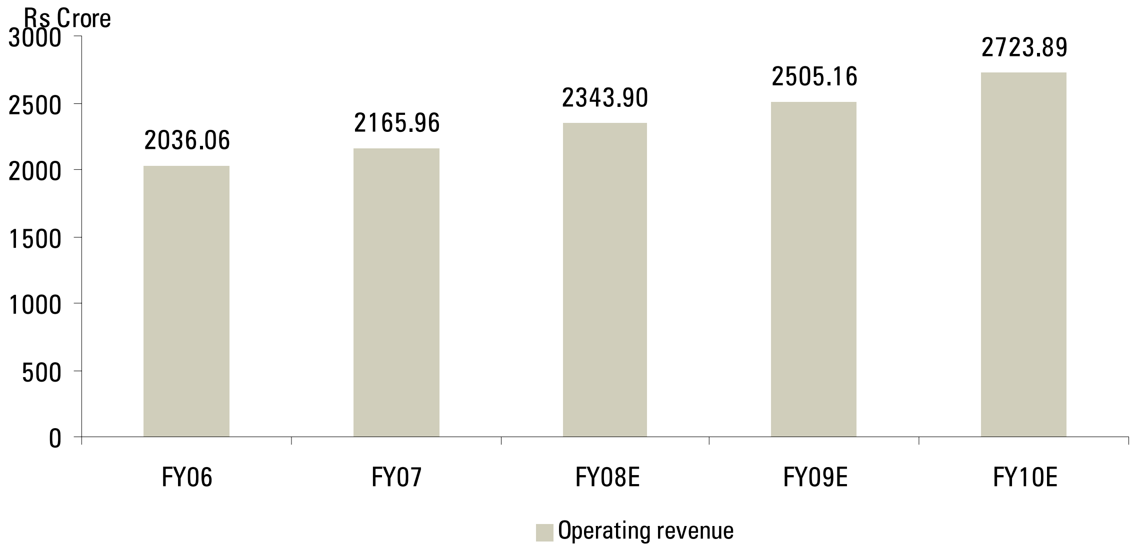
Any significant delay in receiving delivery of new vessels would impact the revenue and earnings negatively.

FINANCIALS

- **Steady revenue growth**

GESCO has been able to maintain steady growth in its operating revenues over the years. Historically, the company has maintained a time-to-spot charter ratio of 45:55. This has enabled it to achieve stable growth in revenues, despite the high volatility in freight rates. The company is expanding its asset base, both in the shipping and offshore segments. This would lead to higher operating days and with the day rates in most asset categories likely to remain stable to firm, the company will be able to achieve a steady growth in operating revenues. We expect the company to report a 7.9% CAGR in operating revenues over FY07-10E.

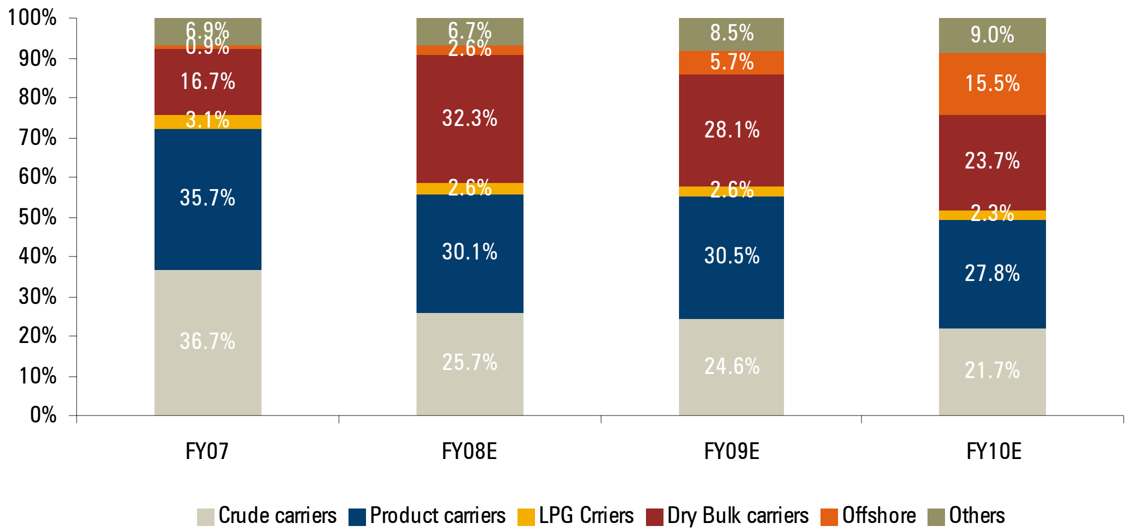
Exhibit 31: Operating revenues to grow at steady clip



Source: ICICIdirect Research

GESCO's expansion of its offshore fleet would result in de-risking and balancing the revenue mix. We expect the contribution from the offshore segment to grow at a rapid pace from 0.9% in FY07 to 15.5% in FY10E.

Exhibit 32: Contribution from offshore segment to increase

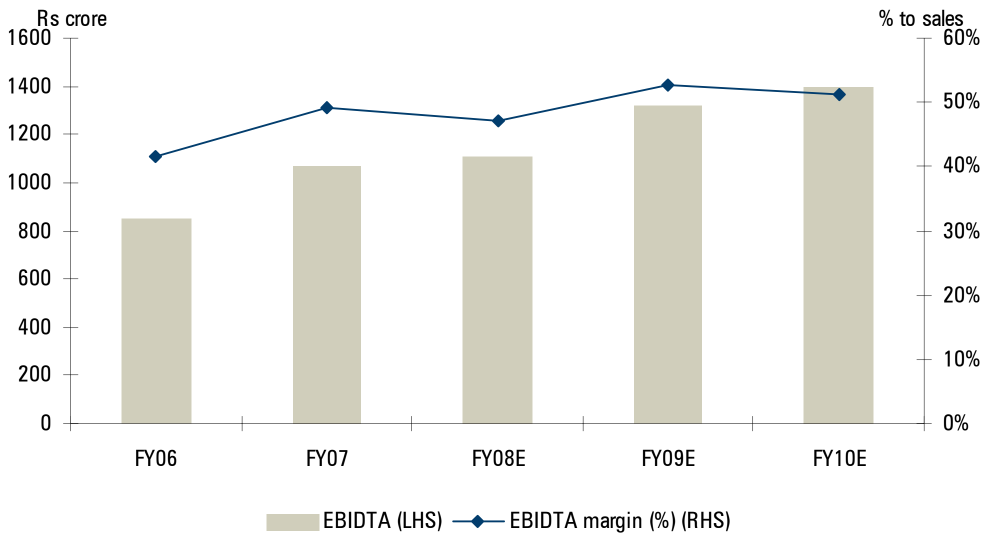


Source: ICICIdirect Research

- **Operating margin to improve**

High day rates in the offshore and dry bulk segment would enable GESCO improve its operating margin. We expect operating margin to improve from 49.3% in FY07 to 51.2% in FY10E. Easing of tanker day rates in Q1 and Q2 of FY08E would result in operating margin declining /in FY08E. We expect margins to bounce back in FY09E and FY10E on the back of increased contribution from the buoyant offshore segment.

Exhibit 33: EBIDTA margin to improve

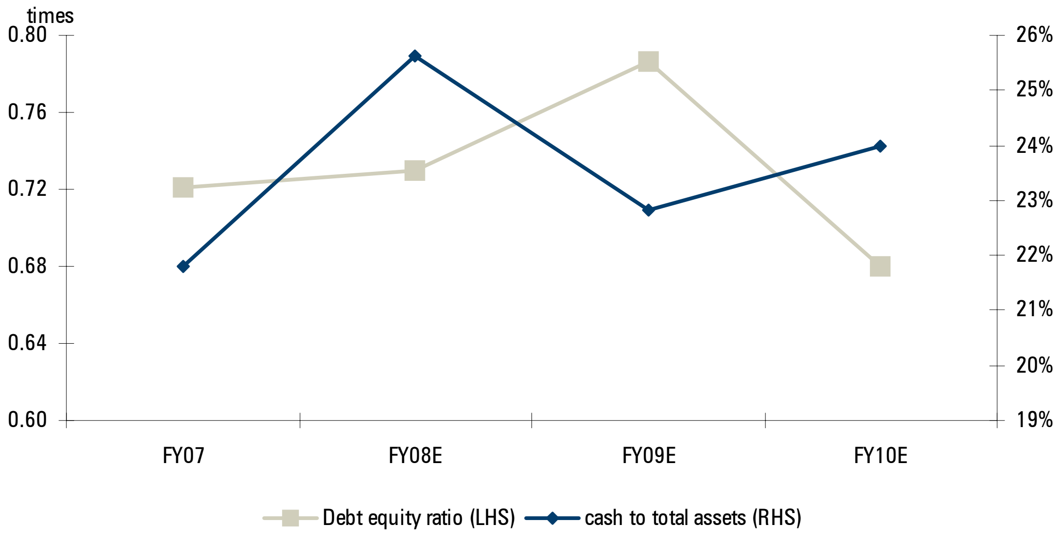


Source: ICICIdirect Research

- **Comfortable debt to equity ratio and strong cash position**

GESCO has maintained a conservative funding pattern. The company's debt to equity ratio has been in the range of 0.7x to 0.8x over the last decade. It has a high cash-to-total assets ratio of 24%. We believe that with the current debt-equity ratio and strong cash to total assets position, the company is well placed to capitalise on the opportunities in the sector.

Exhibit 34: Debt-equity, cash-to-total assets (FY07-10E)



Source: ICICIdirect Research

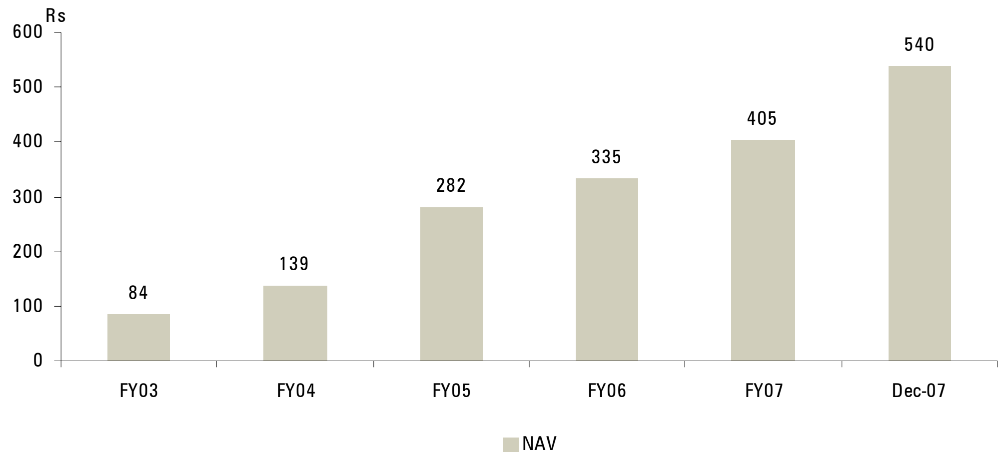
VALUATIONS

GESCO is the largest private sector shipping company in India. Its operations are in line with globals peers in terms of cargo carried and the geographies it operates in. On most parameters, GESCO is on par with its global peers, or even better. Its financials are on a sound footing with steady revenue growth, operating margin in excess of 50%, cash-to-total assets ratio of 24%, and low debt-equity ratio of 0.7x. However, we believe that these positives have not been factored in the price of GESCO. We believe the stock is undervalued compared to its peers. We have considered different valuation tools to arrive at a average target price of Rs 505.

- **Net asset value (NAV)**

GESCO's NAV has grown consistently over the years from Rs 84 in FY03 to Rs 540 in December 2007. It is currently trading at a 33% discount to its NAV. Globally, shipping companies trade at a premium to their NAVs. Tanker companies trade at 1.2x to 1.3x their NAV. Considering that major portion of GESCO is derived from the tanker segment, it should be valued at least at 1x its current NAV of Rs 540.

Exhibit 35: Consistent growth in NAV



Source: Company, ICICIdirect Research

- **Price to Book Value (P/B)**

GESCO is undervalued compared to its global peers on the price-to-book value parameter. Global peers trade at an average P/B of 3.57, while GESCO is trading at a 0.87x its book value. We value GESCO at 1.2x its book value, with a target price of Rs 487, which is at a significant discount to the multiples stocks of global shipping company's trade.

- **Market capitalisation-to-operating revenue**

The global average multiple for shipping companies for market cap/revenues is 3.1x, whereas, GESCO trades at a multiple of 1.98x. We value GESCO at a market cap/ revenue multiple of 2.6x, with a target price of Rs 465.

- **Price earning ratio**

Globally, shipping companies enjoy much better multiples compared to their Indian peers. The average PE ratio for global shipping companies is 13.3x. GESCO is significantly undervalued on this parameter and is trading at a multiple of 4.1x. We expect the stock to trade a higher multiple due to its strong operating margins and a diversified and de-risked business model. We value it at a P/E multiple of 6x, with a target price of Rs 526.

Exhibit 36: Peer comparison

	Teekay Corp CY09E	Frontline Ltd CY09E	Danaos Corp CY09E	Overseas Shipholding CY09E	Eagle Bulk Shipping CY09E	Tsakos Energy CY09E	Average	G E Shipping FY10E
Currency	US$	US$	US$	US$	US$	US$		US$
Revenues	240.47	84.34	35.16	123.01	23.99	44.31		69.13
CMP	43.42	44.86	25.16	68.22	24.94	30		9.01
EPS	3.30	2.99	1.97	3.70	2.76	2.67		2.23
PE (x)	**13.16**	**15.00**	**12.77**	**18.44**	**9.04**	**11.24**	**13.27**	**4.05**
Mcap	316.09	335.67	137.27	212.78	116.61	114.3		137.21
Mcap/Revenues (x)	**1.31**	**3.98**	**3.90**	**1.73**	**4.86**	**2.58**	**3.06**	**1.98**
EV/EBIDTA	9.55	10.51	9.13	8.40	8.62	8.96		5.10
EBIDTA margin	39.23%	72.09%	68.03%	32.16%	77.87%	59.31%		51.24%
P/BV	1.08	12.60	0.00	1.05	1.95	1.16	**3.57**	0.87

Source: Reuters, ICICIdirect Research

Exhibit 37: Average target price

Valuation based on	Target price
Global NAV average	540
Global price to book value average	487
Global Mcap/revenues average	465
Global PE multiple	526
Average target price	**505**
Current market price	355.00
Upside	42%

Source: ICICIdirect Research

FINANCIAL SUMMARY

Exhibit 38: Revenue model assumptions

Average rate per day (US$)	FY06	FY07	FY08E	FY09E	FY10E
Crude Carriers	36500	36857	36500	37000	36800
Product Carriers	27359	27877	27000	27250	27550
LPG Carriers	21908	21908	22000	23000	22750
Dry bulk carriers	20600	19624	42400	39000	37500
Anchor Handling Tug cum Supply Vessel			15000	15000	15000
Platform Supply Vessels			18500	18500	18500
Multipurpose Support Vessel			30000	30000	30000
Jack up rig					150000

Source: ICICIdirect Research

Profit & Loss (Rs crore)

Y/E March	FY06	FY07	FY08E	FY09E	FY10E
Net Sales	**2036.06**	**2165.96**	**2343.90**	**2505.16**	**2723.89**
% Growth	700.50%	6.38%	8.22%	6.88%	8.73%
Operating expenses	892.87	872.98	954.28	880.22	986.80
Employee Expenses	160.59	184.33	235.79	252.88	281.57
Sell. & Admin. Expenses	1027.42	41.16	46.88	50.10	59.93
Total Exp.	**1188.01**	**1098.47**	**1236.95**	**1183.20**	**1328.30**
% Growth	431.29%	-7.54%	12.61%	-4.35%	12.26%
Operating Profit	848.05	1067.49	1106.95	1321.96	1395.60
Depreciation	283.05	268.36	346.06	360.00	385.20
Interest expense	97.58	111.00	142.00	160.00	180.00
Other Income	423.35	251.78	627.40	505.00	570.00
PBT	890.77	939.91	1246.29	1306.96	1400.40
Tax	34.61	32.54	59.30	59.00	65.00
Net Profit	**856.16**	**907.37**	**1186.99**	**1247.96**	**1335.40**
% Growth	9855.38%	5.98%	30.82%	5.14%	7.01%
Equity	152.27	152.27	152.27	152.27	152.27
Dividend %	112%	115%	125%	130%	140%
EPS	**56.23**	**59.59**	**77.95**	**81.96**	**87.70**

7.9% CAGR in operating revenue over FY07-10E

13.7% CAGR in net profit over FY07-10E

Balance Sheet (Rs crore)

Y/E March	FY06	FY07	FY08E	FY09E	FY10E
Share Capital	152.27	152.27	152.27	152.27	152.27
Preference Share Capital	0.00	0.00	0.00	0.00	0.00
Reserves & Surplus.	2268.11	2973.72	3917.44	4937.21	6026.89
Secured Loans	1876.69	2253.86	2970.00	4000.00	4200.00
Deferred Tax	0.15	0.00	0.00	0.00	0.00
Total liabilities	**4298.41**	**5379.85**	**7039.71**	**9089.48**	**10379.16**
Net Block	2865.63	4038.70	5208.48	6848.69	7669.84
Investments	167.43	159.47	159.47	159.47	159.47
Inventories	36.78	37.01	38.53	48.04	59.70
Sundry Debtors	88.32	176.61	160.54	185.31	223.88
Cash & Bank	1417.91	1173.62	1804.29	2075.15	2488.98
Loans & Adv.	81.52	145.33	245.00	400.00	450.00
Current Assets	1624.53	1532.57	2248.36	2708.51	3222.56
CL & Prov.	359.33	350.89	576.60	627.19	672.71
Net Current Assets	1265.20	1181.68	1671.76	2081.32	2549.85
Total Assets	**4298.41**	**5379.85**	**7039.71**	**9089.48**	**10379.16**

Increase In net block on account of acquisition of new vessels

Cash flow statement (Rs crore)

Y/E March	FY06	FY07	FY08E	FY09E	FY10E
Opening Cash	**1048.20**	**1417.91**	**1173.63**	**1804.29**	**2075.15**
Profit after Tax	856.16	907.37	1186.99	1247.96	1335.40
Dividend Paid	194.85	201.71	218.27	228.19	245.71
Depreciation	283.05	268.36	346.06	360.00	385.20
Cash Profit	948.50	974.02	1314.78	1379.77	1474.88
Changes In working Capital					
Net Increase in CL	20.29	-8.44	225.71	50.59	45.52
Net Increase in CA	197.85	152.33	102.73	189.29	100.23
CF after changes in Working Capital	788.58	836.76	1430.36	1241.07	1420.18
Cash Flow from Investing Activities					
Purchase of FA	217.41	1441.43	1515.84	2000.21	1206.35
Cash from Financing Activities					
Increase /(Decrease) in Loan Funds	-231.91	377.17	716.14	1030.00	200.00
Closing Cash	**1417.91**	**1173.63**	**1804.29**	**2075.15**	**2488.98**

Ratios

Y/E March	FY06	FY07	FY08E	FY09E	FY10E
EPS (Rs)	56.23	**59.59**	**77.95**	**81.96**	**87.70**
Book Value (Rs)	158.95	205.29	267.27	334.24	405.80
Operating Margin	41.65%	49.28%	47.23%	52.77%	51.24%
Net Profit Margin	42.05%	41.89%	50.64%	49.82%	49.03%
RONW	35.37%	29.03%	29.17%	24.52%	21.61%
ROCE	19.73%	19.84%	15.72%	14.54%	13.45%
Debt/Equity(x)	0.78	0.72	0.73	0.79	0.68
FA Turnover Ratio	0.74	0.58	0.46	0.37	0.36
Enterprise Value (Rs cr)	5864.37	6485.83	6571.30	7330.44	7116.61
EV/EBIDTA(x)	6.92	6.08	5.94	5.55	5.10
Sales to Equity(x)	13.37	14.22	15.39	16.45	17.89
Market Cap to Sales(x)	2.65	2.50	2.31	2.16	1.98
Price to Book Value(x)	2.23	1.73	1.33	1.06	0.87
cash to total assets	**33.0%**	**21.8%**	**25.6%**	**22.8%**	**24.0%**

EPS CAGR of 13.7% over FY07-10E

Strong cash to total assets ratio enables the company to capitalize on opportunities in the sector by timing vessel acquisitions during softness in asset prices.

RATING RATIONALE

ICICIdirect endeavours to provide objective opinions and recommendations. ICICIdirect assigns ratings to its stocks according to their notional target price vs current market price and then categorizes them as Outperformer, Performer, Hold, and Underperformer. The performance horizon is 2 years unless specified and the notional target price is defined as the analysts' valuation for a stock.

Outperformer: 20% or more;
Performer: Between 10% and 20%;
Hold: ±10% return;
Underperformer: -10% or more.

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