investor's eye

Index

Take Five

Scrip	Reco Date	Reco Price	CMP	Target
Aban Offshore	03-Mar-05	330	**1,201**	1,760
HLL	24-Nov-05	172	**250**	300
ICICI Bank	23-Dec-03	284	**651**	770
Orient Paper	30-Aug-05	214	**605**	800
UltraTech	10-Aug-05	384	**828**	1,000

Gateway Distriparks

Cannonball

Stock Update

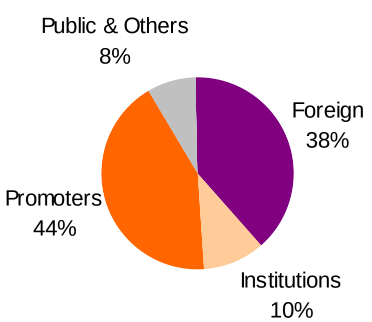
Financials continue to impress

Buy; CMP: Rs159

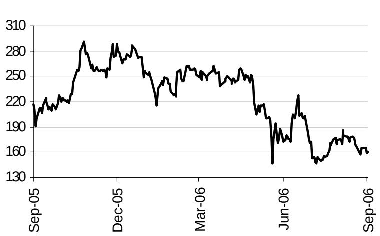
Company details

Price target:	Rs250
Market cap:	Rs1,466 cr
52 week high/low:	Rs301/144
NSE volume: (No of shares)	2.5 lakh
BSE code:	532622
NSE code:	GDL
Sharekhan code:	GATEWAY
Free float: (No of shares)	5.2 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-8.6	-12.1	-36.6	-25.3
Relative to Sensex	-12.5	-27.1	-43.2	-48.0

We recently studied the annual report of Gateway Distriparks Ltd (GDL) and presented below are the highlights of the same.

Key points

- During FY2006 GDL registered a 45% growth in its revenues on the back of a 14% rise in the throughput handled and a 30% increase in the realisation per twenty-foot equivalent units (TEUs).
- The growth in the volume and the realisation improved GDL's operating profit margin (OPM) by 540 basis points from 55.1% to 60.4%. Consequently the operating profit jumped by 59.1% to Rs83.8 crore.
- Towards the end of FY2006, GDL had come out with a USD85-million global depository receipt (GDR) issue and garnered around Rs375 crore. As the majority of the funds had not been utilised, the same had been deposited in banks. The cash that GDL had on its books was utilised to pay off its debts worth Rs50 crore. Hence we saw a very significant nine-fold jump in its other income and a 45% decline in its interest charge in FY2006.
- Although with the repayment of the debts GDL's debt/equity ratio has come down to 0.06, yet the excess un-utilised capital is hurting its return ratios. Its return on capital employed (RoCE) has come down from 27% to 20% and its return on net worth (RoNW) has fallen from 21% to 12.7%.
- In 2006 GDL commenced its rail container freight (RCF) service. It is now setting up its second rail linked inland container depot (ICD), which will ply on electric route connecting the Jawaharlal Nehru Port Trust (JNPT) to northern India.
- GDL has expanded the capacity of its container freight station (CFS) at JNPT by 36,000 TEUs to 216,000TEUs. Further with huge cash of Rs352 crore on its books, GDL is now actively looking to acquire an existing CFS at Nava Sheva.
- JNPT is all set to commission its third container terminal at Nava Sheva, taking its container handling capacity from 2.4 million TEUs currently to 3.6 million TEUs. Hence GDL's move to expand its Nava Sheva facility augurs well for its profitability.

Key financials

Particulars	FY2004	FY2005	FY2006E	FY2007E	FY2008E
Net profit (Rs cr)	19.1	34.9	73.0	89.6	127.6
Shares in issue (cr)	6.4	7.5	9.2	9.2	9.2
EPS (Rs)	3.0	4.7	7.9	9.7	13.8
% y-o-y growth	*27.3*	*82.7*	*109.2*	*22.8*	*42.3*
PER (x)	53.3	34.2	20.1	16.4	11.5
P/BV (Rs)	12.5	7.2	2.5	2.2	1.8
EV/EBIDTA (x)	37.7	22.4	13.7	12.2	8.0
RoCE (%)	24.4	27.1	20.0	16.0	19.6
RoNW (%)	23.5	21.1	12.7	13.5	16.1

The latest annual report of the company focuses on three different aspects of the company:

- its continued impressive financial performance,
- the commencement of its containerised rail operation, and
- the outlook for its business.

Impressive financial performance continues

During FY2006 GDL registered a 45% growth in its revenues. The growth was achieved on the back of a 14% growth in the throughput handled (203,000TEUs handled during FY2006) and a 30% growth in the realisation per TEU (Rs6,825 per TEU).

Particulars	2006	2005	2004	2003	2002
TEUs handled	203000	178604	130345	92885	80107
% y-o-y chg	*14*	*37*	*40*	*16*	
Realisation	6825	5250	4538	4919	4745
% y-o-y chg	*30*	*16*	*-8*	*4*	

The growth in the volume and realisation improved GDL's OPM by 540 basis points from 55.1% to 60.4%. Consequently the operating profit jumped by 59.1% to Rs83.8 crore. The cost per TEU rose by 7.4% primarily because of an increase in the other costs. However the transportation cost declined by Rs60 per TEU mainly because last year GDL bought handling equipment like trailers, which were earlier taken on a charter basis. Similarly the labour cost per TEU has remained flat as GDL entered into long-term contracts with workers.

Operating cost per TEU

Rs per TEU	2006	2005	2004	2003	2002
Operating cost/TEU	1943	1808	1884	1883	1655
Transportation cost/TEU	690	749	980	878	878
Labour cost/TEU	243	247	280	270	270
Other cost/TEU	1010	813	624	735	507
EBIDTA/TEU	4126	2947	2099	2385	2432

Sharp reduction in working capital cycle

GDL's working capital cycle has improved considerably with debtor days reducing by 14 days and creditor days reducing by 20 days. This led to a 68% growth in the cash from operation to Rs86.8 crore (adjusting for the Rs50 crore of licence fee paid to Indian Railways, shown in "Loan and advances"). The reported cash flow from the operation has shown a decline of 29%.

Particulars	2006	2005	2004	2003	2002
Debtor days	18.4	32.3	33.0	24.9	16.0
Creditors	28.4	48.7	51.4	50.4	58.1

Note: The Rs50 crore of licence fee (which GDL paid to Indian Railways) that is shown in "Loan and advances" will be included in the gross block and capitalised, once GDL signs an agreement with Indian Railways. Hence we have taken the same in the gross block and adjusted the cash flow from operation.

Rs352 crore cash on balance sheet

During the end of FY2006 GDL had come out with USD85-million GDR issue through which it had garnered around Rs375 crore. These funds were mobilised to finance the expansion of its CFSs, especially the JNPT one, and the launch of its RCF services. However other than spending Rs50 crore to start the RCF service business and carry out minor expansions at Navi Mumbai, GDL has not made any significant progress in the expansion project that seeks to set up a greenfield CFS at JNPT.

Hence with the bulk of the GDR issue proceeds lying unutilised, the company has deposited the same in banks. Also the cash that GDL had on its books was utilised to pay off debt to the tune of Rs50 crore. Hence we have seen a very significant nine-fold jump in its other income and a 45% decline in its interest charge.

Excess un-utilised capital hurting return ratios

Even though with the repayment of debt, GDL's debt/equity ratio has come down to 0.06, the excess un-utilised capital on the balance sheet is hurting the return ratios. For example, GDL's RoCE has come down from 27% to 20% and its RoNW has come down from 21% to 12.7%. In the absence of the excess capital, as represented by Rs352 crore cash on book, the RoNW would have been a very impressive 32.4%.

Key ratios	2006	2005	2004	2003	2002
RoCE (%)	20.0	27.1	24.4	22.1	21.1
RoNW (%)	12.7	21.1	23.5	19.6	16.4
Debt/Equity	0.06	0.48	0.23	0.25	0.31

RCF venture commences operation

On May 3, 2006 GDL commenced its RCF service. The company started with a single rake and is currently operating with six rakes and that too at full utilisation. GDL has signed an agreement with Container Corporation of India (Concor) to work jointly towards business development. As part of the agreement, Concor will provide GDL with its wagon and ICDs. In the annual report, the management has spoken about scaling up the RCF business. It has said that GDL has recently acquired a 50-acre land through its 100% subsidiary, Gateway Rail Freight Pvt Ltd (GRFPL). Through GRFPL, GDL is setting up its second rail linked ICD, which will be on electric route connecting JNPT to northern India. The company already has one ICD at Garhi, near Gurgaon; from this ICD it operates container rakes to JNPT. The management has further said that for the RCF services GDL is currently evaluating quotations to procure container wagons. As of now, the company has a tie-up with Concor to source container rakes from the latter. The company expects to place the order for wagons in the next 8-12 months after carefully evaluating the quotations.

Outlook remains bright

Meanwhile two positive developments are taking place within GDL. One, the company has expanded the capacity of its existing CFS at JNPT by 36,000TEUs to 216,000TEUs. Two, with huge cash of Rs352 crore on its books, GDL is now actively looking to acquire an existing CFS at Nava Sheva. The company has started negotiations with some of the players already.

With a buoyant economy and booming export-import trade, the under-penetrated container market in India is all set to witness a significant growth. This would necessitate a higher number of container terminals at all ports in the country. JNPT is all set to commission its third container terminal at Nava Sheva. This will take JNPT's container handling capacity from current 2.4 million TEUs to 3.6 million TEUs. According to the management, this additional capacity would present every CFS at Nava Sheva an opportunity to service additional 35,000TEUs in FY2007. However out of the nine odd CFSs at Nava Sheva, not all have the capacity and support infrastructure to service this additional volume. With the opportune expansion at GDL's Nava Sheva facility, the company expects to easily handle a lot more than the 35,000 incremental TEUs. Hence with the additional volume coming from the high-margin Mumbai CFS, where the realisation is as high as Rs7,000 per TEU, we expect GDL's profitability to improve from Q3FY2007.

Valuation and view

By commissioning its third container terminal JNPT is all set to gain the "first mover advantage". Being the leading logistic player at JNPT, GDL will benefit the most from the additional container handling capacity coming up at JNPT, thanks to the expanded capacity at its Mumbai CFS. Further, with its entry into the RCF service space, the expansion of the capacity at the Garhi ICD (near Delhi) and the construction of the second ICS at Faridabad, GDL is all set to offer the complete range of port-related container logistic services. We expect GDL's earnings to grow at a compounded annual growth rate (CAGR) of 33% over FY2006-08. At the current market price of Rs159, the stock is trading at 11.5x its FY2008 earnings and the valuation is attractive, considering the strong compounded annual growth in the earnings and the substantial earnings that would accrue once GDL acquires a significant scale in the RCF business. We remain positive on the company and maintain our Buy recommendation with a price target of Rs250.

The author doesn't hold any investment in any of the companies mentioned in the article.

Pharma

Sector Update

Data protection cheers MNC pharma!!

Key points

- The Government of India is on the verge of allowing 5-year data protection.
- Data protection implies the safety of the clinical trial and test data provided to the regulatory authorities by innovator drug companies. This means that other companies cannot make use of the innovator's data to obtain marketing authorisations for drugs.
- The implementation of data protection would enhance the confidence among the MNC associates to launch innovative products in the domestic market. Indian subsidiaries have been traditionally restricted from launching new products from their parent's portfolio due to lack of data protection.
- The regulation is likely to benefit Indian companies, which have shifted their focus from being pure generic players to innovative players, as it would protect their research data from being copied in the future.
- The increasing launch of new products by MNCs would increase the pressure on domestic companies to reduce drug development costs. This would provide a boost to players in the contract research and clinical data management space.

Event

The Government of India, after long political deliberation, is on the verge of giving 5-year data protection. That means protection of data submitted by an innovator company to the Drug Controller General of India (DCGI).

The following are the clauses of the data protection proposal.

- The data protection will be provided to any drug that is being introduced in India for the first time.
- The period of protection will begin on the first date of the publication of the data worldwide.
- Only drugs that have been introduced after 1995 will be eligible for data exclusivity.

In order to protect the interests of the Indian pharmaceutical companies, the government has also thrown in the following riders into the proposal.

- There will be price checks imposed on the new products introduced into the Indian market, which enjoy data exclusivity.
- Generic applicants will be allowed to put in bioequivalence data with the DCGI two years before the expiry of the exclusivity.

What is data protection?

Data protection is the protection of the clinical trial and test data provided to the regulatory authorities by the innovator drug companies. Basically, the implementation of data protection provides for a period of protection during which the test and clinical trial data of an innovator company may not be relied upon by another company to obtain a marketing authorisation of the same drug.

When manufacturers of generics apply for approval for their drug, they claim bioequivalence, or having a similar molecular structure, to the originator's product. Instead of conducting tests themselves, they make a reference to the latter's submitted data for approval. Data protection would ensure that such data might not be referred to for the marketing approval for a given number of years. This enables the originator to get market exclusivity for the given period, indirectly providing a healthy platform to encourage investments in research and development (R&D) and innovation for new drugs for social benefit. In its simplest form, the drug controller will not accept mere bioequivalence data from subsequent applicants (generic producers) for approval of their products. The subsequent applicants would have to generate data from scratch, involving considerable cost and money.

What does this mean for Indian subsidiaries of multinational pharmaceutical companies?

Historically, Indian subsidiaries of multinational pharmaceutical companies have restricted the launch of products from their parent's global portfolio in the Indian market due to lack of data protection. If the Government of India implements 5-year data protection, which safeguards the data submitted by innovators, it would provide a great deal of respite to the innovator companies from the threat of low-cost copy cat versions of their new products. This would enhance the confidence among the MNC associates to launch innovative products in the domestic market. Incidentally, the MNC peers have a rich R&D pipeline with GlaxoSmithkline having 146 products in various stages of clinical developments, Novartis having a pipeline of 75 products and Wyeth having a basket of 36 products. More product introductions, research and development and clinical trials business will come to the country only if data exclusivity is in place.

How will the implementation of data exclusivity impact the Indian pharmaceutical companies?

The Indian pharma players are likely to be impacted in two ways.

- The regulation is likely to benefit the Indian companies, which have shifted their focus from being pure generic players to innovative players. In recent times, majority of Indian companies have enhanced their R&D spending from 2-4% of sales to over 10% of sales, in order to increase their focus on innovation. The regulation will be beneficial to such companies engaged in innovative research, as it will provide protection for their data in the future.

- With MNC data not being available, Indian companies would have to resort to conducting their own clinical trials and research in order to introduce generic products in the Indian market place. The Indian domestic companies would also be under pressure to reduce drug development costs with the MNCs increasing their pace of new launches. This would increase the business for players in the contract research and clinical data management. As of now, this segment is at a very nascent stage in India.

View

If the proposal of data protection is cleared and implemented, the MNC pharma players would the major beneficiaries. Specifically players like GlaxoSmithKline Pharma India would be one of the primary beneficiaries, as it has already started conducting clinical trials in India in association with its parent for the parent's new drugs. With such participation, Glaxo India can launch new and innovative drugs within a few months of the launch in the regulated markets like the USA, the EU etc. On similar lines, other players like Pfizer and AstraZeneca have also started conducting trials in India. Further, MNCs like Novartis, Aventis and Wyeth would be enthused to launch new products from their parent's global portfolios in India.

However, on the flipside, the MNCs may not get the data protection for their products which have already been launched, as the proposal entails that the period of 5-year protection will begin on the first date of the publication of the data worldwide and only drugs that have been introduced after 1995 will be eligible.

Moreover, the implementation of data protection would provide a boost to the domestic contract research and clinical data management business. Hence, players like Biocon, Dishman Pharma, Jubilant Organosys, Vimta Lab etc are likely to be benefited by this development.

The author doesn't hold any investment in any of the companies mentioned in the article.

Monsanto India

Viewpoint

Sowing seeds of growth

CMP: Rs1,485

We recently attended the annual general meeting of Monsanto India Ltd (MIL). The company is a 72% subsidiary of Monsanto Co., USA and is in the business of manufacturing and selling herbicides (used for controlling weeds) and seeds (corn and sunflower). The company is not to be confused with Mahyco Monsanto, another joint venture of Monsanto that sells the controversial BT cotton seeds.

As the herbicide and agrochemical market has become increasingly generic and competitive, MIL's focus has shifted towards the higher margin seeds business. The contribution of the seeds business has jumped from 21% of revenues in FY2001 to 53% in FY2006. As part of this portfolio restructuring, MIL has sold one of its herbicide products, Leader, to Sumitomo Chemicals recently.

Revenue mix	1995-96	2000-01	2005-06
Herbicides (%)	100	79	47
Seeds (%)	0	21	53
Total (%)	100	100	100

MIL sees huge potential in the corn seeds business where almost 70% of seeds used are non-hybrid seeds and give poor yields. Given the strong and rising demand for corn (used for human food, animal and poultry feed, in breweries and to make starch) and the poor yields in India, MIL expects the potential of the seeds business to remain upbeat.

MIL is now going in for significant capital expenditure (capex) to expand the seeds business by spending Rs48 crore. This is a huge capex considering that the current gross block (including both seeds and herbicides) is Rs101 crore, ie almost a 50% increase in the gross block. According to the management, this will lead to not only a significant expansion of the seeds capacity but also a technological improvement. This enhanced capacity will become available during Q1CY2007.

Outlook

MIL feels it is strongly positioned in the seeds business as it has all the key requirements: Seeds manufacturing/drying capacity, strong brands, sales infrastructure, a rich product pipeline and technology. In 2005, MIL launched three new corn seed hybrid varieties. Apart from hybrid seeds, MIL has also sought government approval for a genetically modified insect resistant BT corn seed. However, given the time it takes to get approval for GM seeds, MIL does not expect the approval for this product before 2010.

In FY2006 sales were affected by three factors: (1) MIL discontinued distributing BT cotton seeds; (2) pricing pressure in herbicides especially Leader, which has now been sold off; and (3) bird flu concerns across Asia which affected exports of corn seeds. While bird flu is a potential recurring concern, the other two factors are one-off. The Q1FY2007 performance has been exceptionally strong and given the product pipeline and capacity expansion, the management is confident of sustaining growth in future as well.

Result table Rs (cr)

Particulars	Q1FY07	Q1FY06	% yoy chg
Net revenues	159.9	150.7	6.1
Total expenditure	107.2	113.9	-
Operating profits	52.7	36.8	43.1
Other income	4.2	3.7	14.0
EBITDA	56.8	40.4	40.5
Interest	0.1	0.1	16.7
Depreciation	2.0	2.0	1.0
Profit before tax	54.8	38.4	42.6
Tax	2.6	5.1	-
Profit after tax	52.2	33.4	56.4
Equity capital	8.6	8.6	0.0
EPS (Rs)	60.4	38.6	56.4

At the current market price of Rs1,485, MIL is trading at 17.6x FY2006 earnings and 14.5x FY2006 enterprise value/earnings before interest, tax, depreciation and amortisation. Considering the robust demand scenario for the seeds business and the fact that the additional seeds capacity shall become operational by Q1CY2007, MIL's valuations at current levels appear attractive.

Financials

Profit & loss Rs (cr)

Particulars	FY2004	FY2005	FY2006
Net revenues	333.3	377.6	331.6
Total expenditure	251.3	292.5	262.4
Operating profits	82.0	85.0	69.2
Other income	9.9	12.5	14.6
EBITDA	92.0	97.5	83.8
Interest	0.2	0.2	0.2
Depreciation	8.4	7.9	7.8
Profit before tax	83.3	89.4	75.8
Tax	14.0	12.6	3.0
Profit after tax	69.3	76.8	72.8

Key financials

Particulars	FY2004	FY2005	FY2006
Net profit (Rs cr)	69.3	76.8	72.8
Shares in issue (in cr)	0.9	0.9	0.9
EPS (Rs)	80.3	89.0	84.3
% y-o-y chg		*11.0*	*-5.0*
P/E (x)	18.5	16.7	17.6
BV (Rs)	378.6	441.4	377.5
P/BV	3.9	3.4	3.9
EV/EBITDA	12.1	10.3	14.5

The author doesn't hold any investment in any of the companies mentioned in the article.

Sharekhan Stock Ideas

Evergreen

HDFC Bank
Infosys Technologies
Reliance Industries
Tata Consultancy Services

Apple Green

Aditya Birla Nuvo
Associated Cement Companies
Bajaj Auto
Balrampur Chini Mills
Bank of Baroda
Bank of India
BASF India
Bharat Bijlee
Bharat Heavy Electricals
Canara Bank
Corporation Bank
Crompton Greaves
Elder Pharmaceuticals
Godrej Consumer Products
Grasim Industries
Hindustan Lever
Hyderabad Industries
ICICI Bank
Indian Hotels Company
ITC
Mahindra & Mahindra
Marico Industries
Maruti Udyog
Lupin
Nicholas Piramal India
Omax Auto
Ranbaxy Laboratories
Satyam Computer Services
SKF India
State Bank of India
Sundaram Clayton
Tata Motors
Tata Tea
Unichem Laboratories
Wipro

Cannonball

Allahabad Bank
Andhra Bank
Cipla
Gateway Distriparks
International Combustion (India)
JK Cement
Madras Cement
Shree Cement
Transport Corporation of India

Emerging Star

3i Infotech
Aban Offshore
Cadila Healthcare
KSB Pumps
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Navneet Publications (India)
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Orchid Chemicals & Pharmaceuticals
ORG Informatics
Solectron Centum Electronics
Television Eighteen India
Thermax
TVS Motor Company
UTI Bank
Welspun Gujarat Stahl Rohren

Ugly Duckling

Ashok Leyland
Deepak Fertilisers & Petrochemicals Corporation
Genus Overseas Electronics
HCL Technologies
ICI India
Jaiprakash Associates
JM Financial
KEI Industries
NIIT Technologies
Punjab National Bank
Ratnamani Metals and Tubes
Sanghvi Movers
Saregama India
Selan Exploration Technology
Subros
Sun Pharmaceutical Industries
Surya Pharmaceuticals
UltraTech Cement
Union Bank of India
Universal Cables
Wockhardt

Vulture's Pick

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