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Logistics

Transformation underway

March 2019

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LOGISTICS

14 March 2019

Transformation underway

India's US\$ 160bn logistics industry is amidst a much-needed transformation led by (1) structural reforms (GST, e-way bill) and the government's infrastructure thrust (DFC, Sagarmala), (2) the emergence of new-age, service-oriented businesses versus asset-heavy models, and (3) growing formalisation of the sector, propelling organised players to the fore. We prefer the emerging 3PL and express segments for long-term value creation. Among stocks, MLL, FSCSL, and TCIEXP are our top fundamental picks, while TRPC offers compelling valuations.

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Easing impediments: Major bottlenecks – a suboptimal modal mix, inadequate infrastructure and a lack of formalisation – have traditionally plagued the logistics industry. However, we see these impediments easing led by the implementation of structural reforms (GST, e-way bill, infrastructure status to logistics) and progress on marquee infrastructure projects such as the dedicated freight corridor (DFC). These structural drivers are expected to fuel a 9-10% CAGR in the industry over the next 3-4 years, giving rise to a US\$ 200bn+ opportunity.

Emergence of new business models: Evolving supply chain needs are fostering businesses that offer integrated, value-added services and leverage technology for efficiency gains. These models are in stark contrast to the traditional asset-intensive ones that focused solely on transportation and/or warehousing of cargo. The emerging third-party (3PL) logistics and express segments are prime examples.

Prefer 3PL and express: We like the 3PL and express distribution segments as they offer the rare trinity of structural, above-industry growth potential, sustainable moats (high customer lock-in, scalability) and sturdy return ratios (ROE of 25-30%+). Realignment of supply chains post GST rollout in 2017 and increasing logistics outsourcing trends are expected to catalyse growth in these industries – we forecast an ~18%/15% CAGR for 3PL/express over FY19-FY21.

Top picks – MLL, FSCSL, TCIEXP, TRPC: Our stock preferences are aligned with our industry theme of 3PL/express growing faster. Mahindra Logistics (MLL), Future Supply (FSCSL), and TCI Express (TCIEXP) are our top fundamental picks for their strong earnings (28%/27%/25% CAGR) and ROIC (43%/23%/44% on average) profiles over FY19-FY21. Transport Corp (TRPC) is our value pick as it is trading at an attractive 11x one-year forward P/E. We also initiate coverage on Allcargo Logistics (AGLL, BUY) and Concor (CCRI, REDUCE).

KEY RECOMMENDATIONS

Ticker	Price*	Target	Rating
MAHLOG IN	499	625	BUY
FSCSL IN	633	780	BUY
TCIEXP IN	744	880	BUY
TRPC IN	291	365	BUY
AGLL IN	112	130	BUY
CCRI IN	523	530	REDUCE

Price & Target in Rupees | MAHLOG = MLL

*All closing prices as of 13 Mar 2019



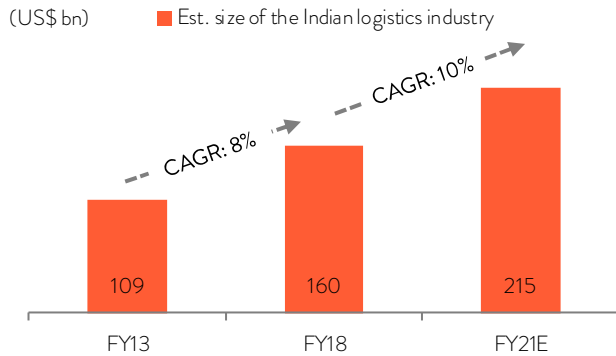
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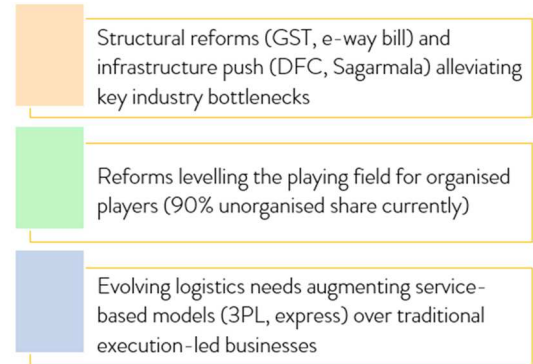
Executive summary

India's US\$ 160bn logistics industry in the midst of transformation

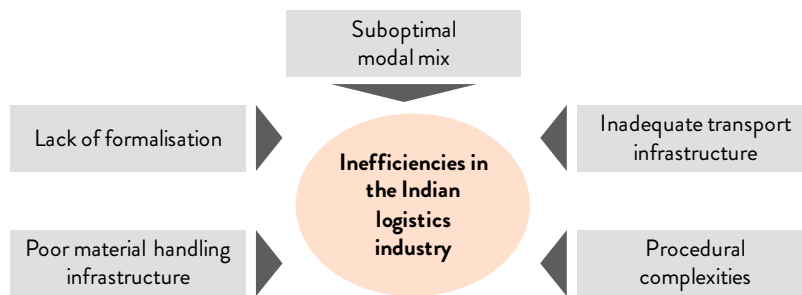
A burgeoning opportunity...



...underpinned by key structural drivers

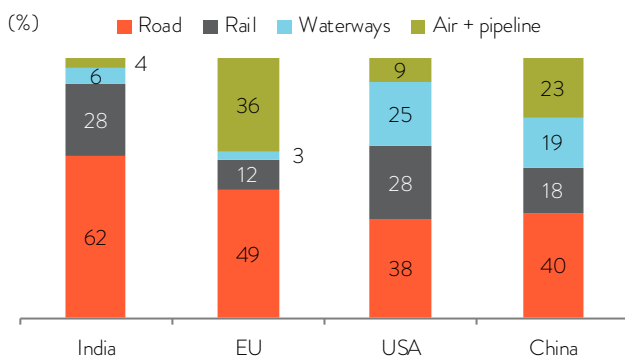


Industry traditionally plagued by acute inefficiencies

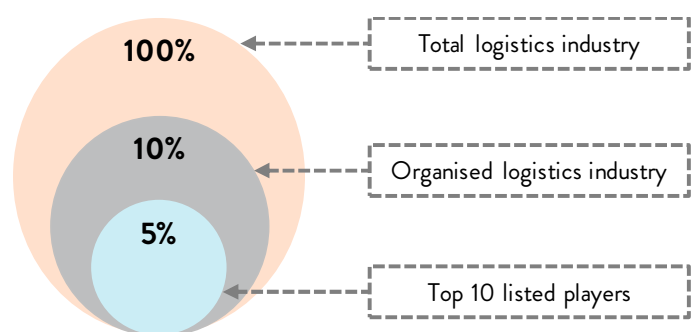


- India ranks 44th on World Bank's logistics performance index, lower than some developing nations (China, South Africa)
- At 13-14%, logistics cost as a percentage of GDP is higher than global standards and most nations

Inefficient road transport dominates the modal mix – dedicated freight corridor could revolutionise rail segment



Large unorganised sector represents opportunity for organised players



Source: Industry, BOBCAPS Research

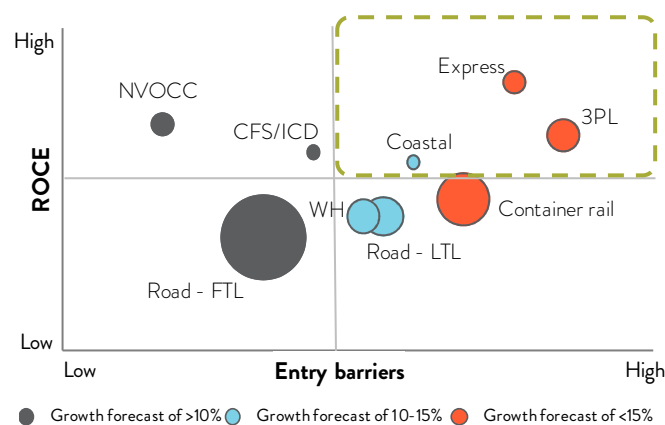
Recent reforms easing major bottlenecks and rejuvenating industry prospects

Challenges	Suboptimal modal mix	Lack of formalisation	Inadequate transport infrastructure	Underdeveloped material handling infrastructure	Procedural complexities
Beneficial Reforms	<ul style="list-style-type: none"> Dedicated freight corridor Improved rail connectivity to ports Sagarmala 	<ul style="list-style-type: none"> Goods and services tax E-way bill implementation 	<ul style="list-style-type: none"> Dedicated freight corridor Sagarmala Bharatmala Industrial corridors 	<ul style="list-style-type: none"> Multi-modal logistics parks Grade-A warehouses 	<ul style="list-style-type: none"> Goods and services tax E-way bill implementation Direct port delivery

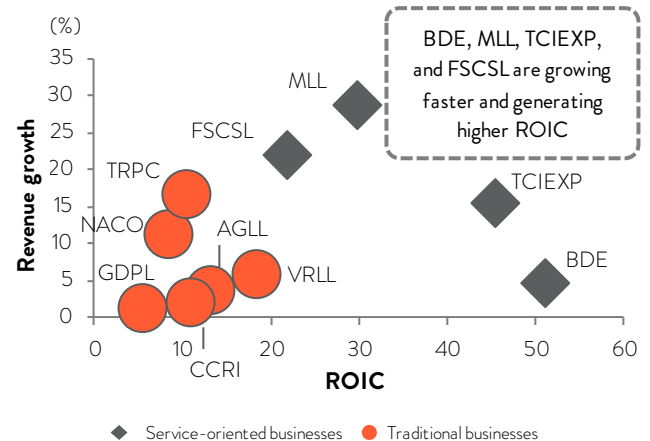
Prefer service-focused business models over traditional execution-led businesses

New-age (service-led, tech-focused) models such as 3PL & express attractive on key fundamentals: moats, growth, ROCE

Companies operating in 3PL and express leagues ahead in growth and return ratios...

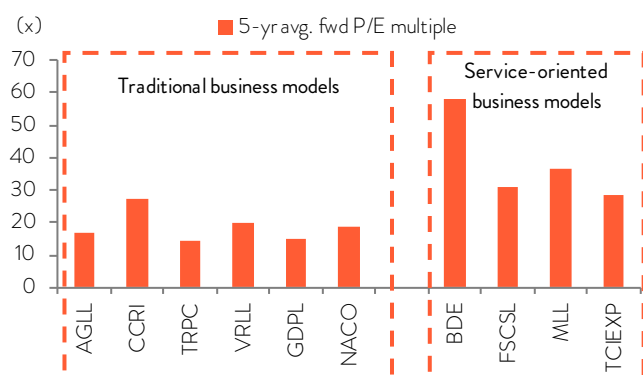


Source: FSCSL Prospectus (Alvarez & Marshall), BOBCAPS Research



Source: Company, BOBCAPS Research

...and hence command higher valuation multiples



Source: Bloomberg, BOBCAPS Research

Our top picks – MLL, FSCSL, TCIEXP, TRPC

Fundamental picks

- **MLL, FSCSL, and TCIEXP** – as these companies enjoy structural industry tailwinds, sustainable competitive advantages, robust long-term growth prospects, and strong financials

Valuation picks

- **TRPC** – which is trading at 11x FY21 EPS, a ~30% discount to its historic average of 14x, despite decent fundamentals and a healthy earnings cycle

Attractiveness matrix for logistics segments – prefer 3PL and express

Industry	Est. market size (Rs bn)	Past 5-yr CAGR (%)	Future growth expectations (%)	Entry barriers	Customer stickiness	Capital intensity	Ability to fend off external risks	Premiumisation	ROCE	Overall industry attractiveness
Road – FTL	6,300-6,500	10-12	5-8							Low
Road – LTL	700-750	12-15	10-12							Moderate
Container rail	80-85	6	12-15							Moderate
Coastal shipping/inland waterways	45-50	10-12	12-14							Moderate
Express	250	~18-20	15-17							High
CFS/ICD	50-55	4-5	2-3							Low
3PL	450-500	18-20	17-18							High
NVOCC	250-300	7-8	5-6							Moderate

Source: FSCSL Prospectus (Alvarez & Marshall), MLL Prospectus (CRISIL Research), Industry, BOBCAPS Research

Very high
 High
 Moderate
 Low
 Very low

Attractiveness matrix for our coverage universe

Company	Industry tailwinds	Competitive moat	Growth prospects	Financial strength	Overall fundamentals
AGLL					
CCRI					
FSCSL					
MLL					
TCIEXP					
TRPC					

Source: BOBCAPS Research | Note: For companies with multiple businesses, we have assigned weightages to each business according to their EBITDA share

Investment thesis for our coverage universe

Companies	Investment thesis
Mahindra Logistics (MLL) BUY TP: Rs 625 ▲25%	<ul style="list-style-type: none"> Discernible competitive advantages – unparalleled scale, asset-light model, and an established anchor client in Mahindra & Mahindra (MM) Diversified, sticky non-anchor client base (~40% of revenue) – marquee names (L'Oreal, BMW India, HUL) present in fast-growing verticals (consumer, auto); several new clients added in 9MFY19 EBITDA margin expansion driven by rising share of lucrative warehousing business Premium valuations sustainable considering strong earnings growth forecast, expanding return ratios
Future Supply Chain Solutions (FSCSL) BUY TP: Rs 780 ▲23%	<ul style="list-style-type: none"> Fast-growing anchor clients in Future Group entities – consensus estimates peg anchor clients' growth at 18% CAGR over FY19-FY21. Current penetration of 33% of anchor logistics spend leaves room for rise in wallet share Strong presence in fast-growing 3PL verticals – consumer and organised retail (~90% of revenue) Robust revenue/earnings growth forecast of 28%/27% CAGR (standalone) over FY19-FY21
TCI Express (TCIEXP) BUY TP: Rs 880 ▲18%	<ul style="list-style-type: none"> Apt positioning, marked by focus on faster growing surface express and lucrative B2B segments, to help capitalise on strong prospects of the express industry Large clientele (200,000+) comprising both corporate majors and SMEs, diversified presence across industries (auto/pharma/retail), and wide branch network forecast to catalyse strong 17%/25% revenue/earnings CAGR over FY19-FY21 Strong expected return ratios (ROE/ROCE of 30%/42%) and earnings growth to help expand P/E multiples
Transport Corporation of India (TRPC) BUY TP: Rs 365 ▲26%	<ul style="list-style-type: none"> Higher share of supply chain/3PL, LTL and seaways businesses fuelling sustained uptrend in margins and ROCE Conducive industry dynamics expected to propel strong growth in supply chain (15%/20% revenue/EBITDA CAGR over FY19-FY21) and freight (13%/16%) businesses Cheap valuation (11x one-year fwd P/E) despite healthy earnings cycle indicates room for multiple re-rating
Allcargo Logistics (AGLL) BUY TP: Rs 130 ▲16%	<ul style="list-style-type: none"> Established positioning in global LCL industry with vast network across major trade lanes; increasing FCL volumes to help tide over global trade uncertainties CFS business gradually turning around after DPD setback (13% volume growth in 9MFY19); commissioning of Kolkata CFS augmenting volumes Attractive valuations – trading at 9.9x one-year fwd P/E
Container Corp of India (CCRI) REDUCE TP: Rs 530 ▲1%	<ul style="list-style-type: none"> Commissioning of DFC likely to ease externalities that have plagued core operating performance over past decade Widest terminal network, largest rolling stock and unparalleled execution track record put CCRI leagues apart from other CTOs; best placed to capitalise on DFC-related opportunities Current valuations (~25x one-year fwd P/E) capture potential volume/earnings uptick

Source: BOBCAPS Research

Valuation snapshot

Company	Ticker	Price*	Mcap (Rs mn)	Rating	Target price (Rs)	Upside / downside (%)	EBITDA CAGR (FY19E- 21E)	Adj. PAT CAGR (FY19E- 21E)	EPS (Rs)			P/E (x)			EV/EBITDA (x)			ROE (%)		
									FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Our Coverage Universe																				
Allcargo Logistics	AGLL	112	27,592	BUY	130	15.8	16.3	15.5	8.5	9.9	11.4	13.2	11.3	9.9	6.5	5.9	5.0	10.3	11.1	11.7
Container Corp of India	CCRI	523	318,387	REDUCE	530	1.4	17.4	4.5	19.0	21.0	20.8	27.5	24.9	25.2	20.6	18.1	15.0	11.9	12.1	11.0
Future Supply Chain Solutions	FSCS	633	25,350	BUY	780	23.3	31.1	27.4	19.2	22.5	31.2	32.9	28.2	20.3	17.5	14.2	10.6	17.0	17.1	20.4
Mahindra Logistics	MLL	499	35,645	BUY	625	25.3	25.3	27.7	12.8	16.7	20.8	39.0	29.8	23.9	21.8	17.1	13.7	20.2	23.1	25.3
TCI Express	TRPC	744	28,488	BUY	880	18.3	23.6	24.7	18.9	23.5	29.4	39.3	31.6	25.3	23.8	19.5	15.7	30.9	30.3	30.1
Transport Corp of India	TCIEXP	291	22,274	BUY	365	25.6	16.8	15.8	19.5	22.9	26.1	14.9	12.7	11.1	11.3	9.4	8.1	18.0	18.2	17.9
Other Indian Companies																				
VRL Logistics	VRLL	283	25,527	NOT RATED			17.1	23.8	10.7	13.5	16.4	26.3	20.9	17.2	10.5	8.9	7.7	15.4	17.4	19.1
Blue Dart Express	BDE	3,212	76,216	NOT RATED			31.2	39.4	46.6	70.3	90.6	68.9	45.7	35.5	27.4	20.3	15.9	17.7	24.5	27.7
Gateway Distriparks	GDPL	125	13,558	NOT RATED			22.4	11.0	8.1	7.6	9.9	15.5	16.3	12.6	9.7	7.2	6.5	9.7	3.5	11.8
Navkar Corp	NACO	45	6,781	NOT RATED			20.4	43.9	3.9	5.8	8.1	8.0	8.0	5.7	6.6	5.4	4.6	3.4	4.7	5.7

Source: Bloomberg, BOBCAPS Research | *All closing prices as of 13 Mar 2019

Picking the winners

MLL, FSCSL and TCIEXP
long-term compounding
stories; TRPC available at
most attractive valuations

In this section, we set out to identify the companies that are best suited to capitalise on the vibrant prospects of India's logistics industry and to create long-term value for investors. In our view, the future winners should ideally have one or more sustainable moats, structural tailwinds, and strong financials. Based on these criteria, **our top fundamental picks are MLL (TP: Rs 625, BUY), FSCSL (TP: Rs 780, BUY), and TCIEXP (TP: Rs 880, BUY).** We also like **TRPC for its attractive valuation** (11x one-year forward P/E vs. a historical trading multiple of 14x) and healthy fundamentals.

Comparing moats





































Sustainable competitive
advantage is the most desired
fundamental trait in our view

Finding sustainable competitive advantages in a largely commoditised industry is a challenge. In fact, among the traditional logistics business models such as road transport, railways and traditional warehousing, we see very few companies with a discernible competitive edge. However, the emergence of newer, service-based business models has changed the industry landscape, introducing companies with key competitive moats over peers.

We have compared the companies in our coverage universe on the following parameters to assess their overall moats.

- **Intangible factors:** Brand strength; perceived difference in quality of product or service
- **Scalability:** Ability to add customers at negligible incremental capital costs; large growth potential in a growing industry
- **Customer lock-in:** High switching costs for customers
- **Reach & network:** Wide distribution reach/geographical presence; expansive infrastructure network versus competitors
- **Cost advantages:** Access to unique resources (raw material, government resources); lower incremental cost for marginal revenue

FIG 1 – COMPARISON OF COVERAGE UNIVERSE ON KEY QUALITATIVE PARAMETERS

	Intangible factors	Scalability	Customer lock-in	Reach & network	Cost advantages	Overall moat
AGLL						
CCRI						
FSCSL						
MLL						
TCIEXP						
TRPC						

Source: BOBCAPS Research | Note: For companies with multiple businesses, we have assigned weightages to each business according to their EBITDA share

 Very Strong
  Strong
  Moderate
  Weak
  Very weak

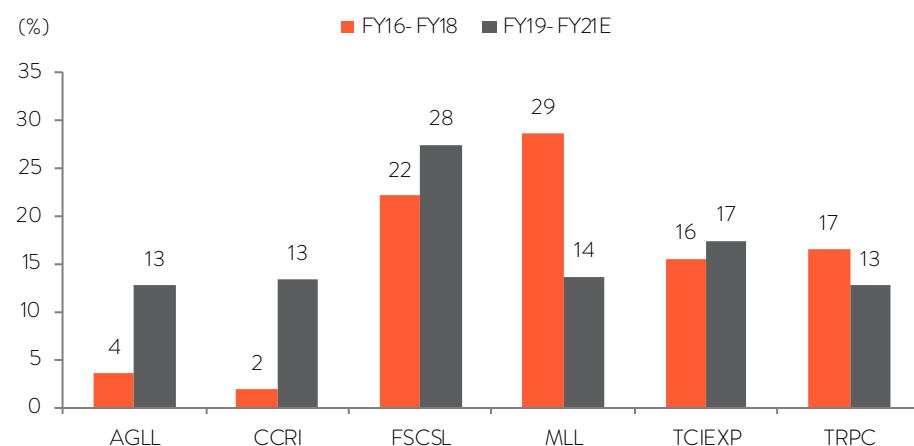
Comparing financial strength

We assess our coverage companies on the following financial parameters – revenue growth, EBITDA margin, earnings growth, balance sheet quality, return ratios, and cash flow generation. We have considered past as well as projected financials for our comparison.

Revenue growth – FSCSL, TCIEXP to outpace the industry

We expect aggregate revenue for our coverage universe to log a 14.1% CAGR over FY19-FY21, faster than the 9% growth posted over FY16-FY18. Among companies, FSCSL is forecast to surpass peers at 28% driven by fast-growing anchor customers, while TCIEXP would also outpace the industry. MLL has been the fastest growing company in the previous two-year period, but we expect a tapering down owing to the high base effect and slower anchor customer growth.

FIG 2 – REVENUE GROWTH EXPECTED TO BE HEALTHY



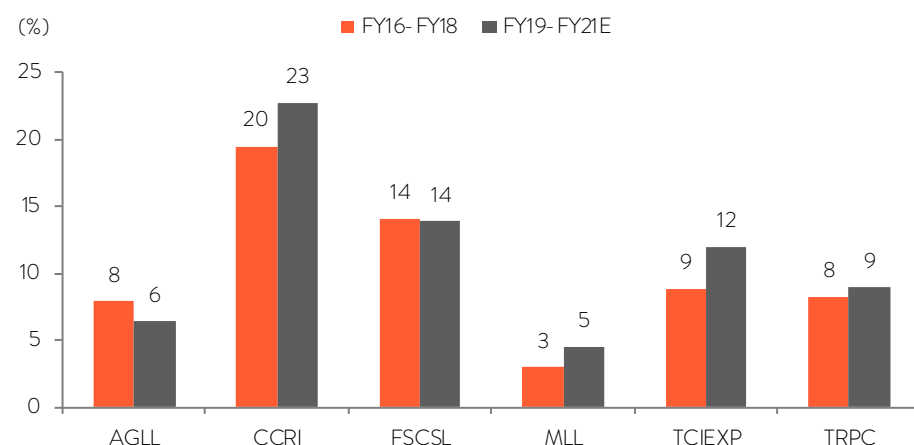
Source: Company, BOBCAPS Research | *CCRI's revenue excludes SEIS income

EBITDA margin – MLL, TCIEXP, CCRI to witness steep expansion

We expect MLL to witness operating margin expansion of 80bps over FY19-FY21 aided by a better revenue mix and TCIEXP's margins to expand 120bps backed by operational efficiencies. DFC-related benefits are likely to drive CCRI's EBITDA margin up 160bps.

FSCSL/TCIEXP to log industry-leading revenue CAGR of 28%/17% over FY19-FY21

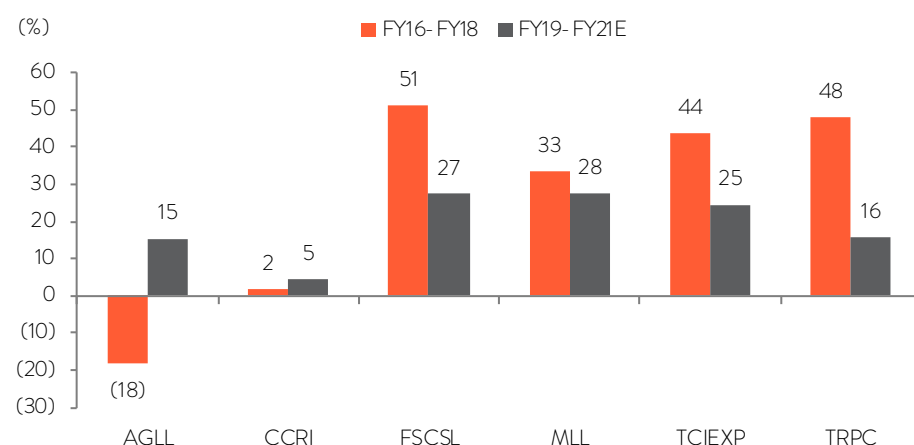
Forecast 80bps/120bps expansion in MLL/TCIEXP's EBITDA margins

FIG 3 – AVERAGE EBITDA MARGIN TO EXPAND FOR MOST COMPANIES

Source: Company, BOBCAPS Research

Adjusted PAT growth – MLL, FSCSL, TCIEXP stand out

Healthy revenue and EBITDA growth is likely to augment PAT growth for our coverage universe, where we forecast a sharp recovery to 10.1% CAGR over FY19-FY21 from 4% over FY16-FY18. MLL, FSCSL, and TCIEXP are once again likely to grow much faster than the industry. Despite healthy revenue and EBITDA growth, CCRI's adjusted PAT is forecast to grow at a sedate 5% as we have not factored in SEIS income in FY21 (included in other income; Rs 2.8bn in FY18).

FIG 4 – PAT GROWTH TREND

Source: Company, BOBCAPS Research

Lean balance sheets all around

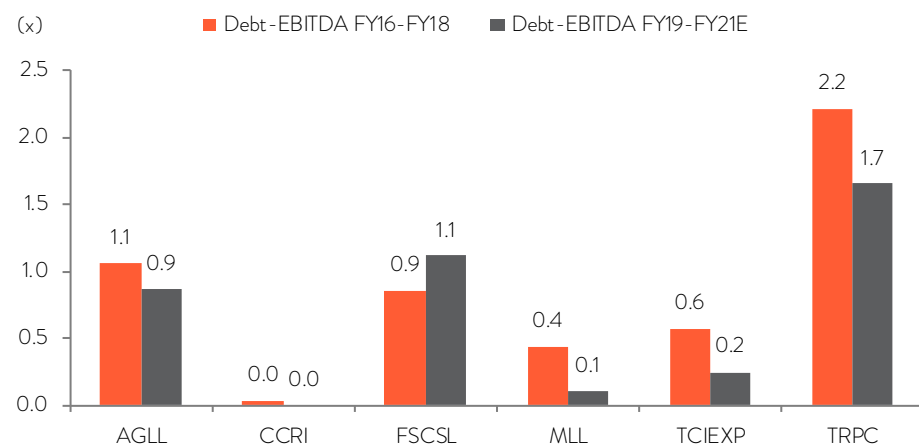
One of the major positives for the Indian logistics industry is that most companies have lean balance sheets. Despite varying capital intensity, all the companies in our coverage universe have fairly strong balance sheets, with TRPC's high debt/EBITDA ratio of 2.2x over FY16-FY18 (although its projected to reduce to 1.7x over FY19-FY21). In our opinion, this stems from lean working capital cycles,

MLL/FSCSL/TCIEXP's earnings projected to grow at 28%/27%/25% CAGR

Low debt levels a common feature for our coverage universe companies

which helps fund requisite capex through internal accrual. Strong balance sheets are likely to help companies withstand any potential industry downturn and support growth.

FIG 5 – BALANCE SHEET HEALTH SOUND FOR MOST PLAYERS

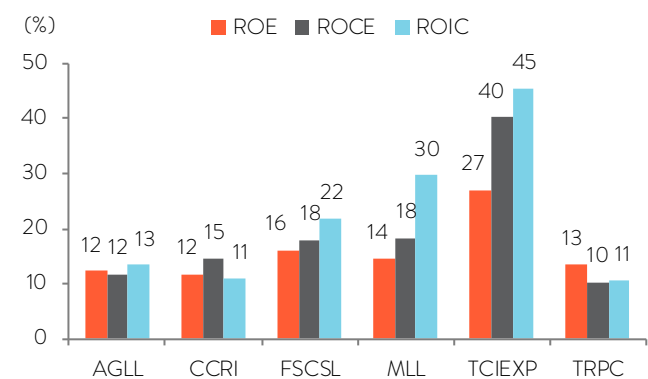


Source: Company, BOBCAPS Research

Return ratios – MLL, TCIEXP way ahead of the pack again

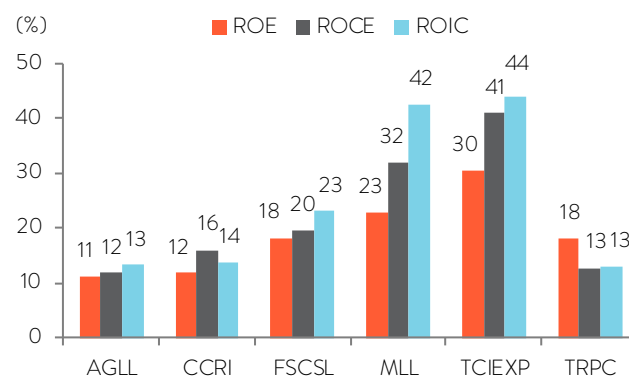
MLL and TCIEXP score ahead of peers on return ratios as well. Going forward, we believe both players will have the best ROE, ROCE and ROIC in the sector. We expect MLL's return ratios to be augmented by margin expansion and higher expected dividend payments, while TCIEXP should have comparable ratios. FSCSL and TRPC are also expected to witness improvement on this front.

FIG 6 – TCIEXP AND MLL HAVE GENERATED THE BEST ROCE/ROIC IN THE SECTOR (FY16-FY18) ...



Source: Company, BOBCAPS Research

FIG 7 – ...AND ARE EXPECTED TO CONTINUE THE TREND (FY19-FY21E)



Source: Company, BOBCAPS Research

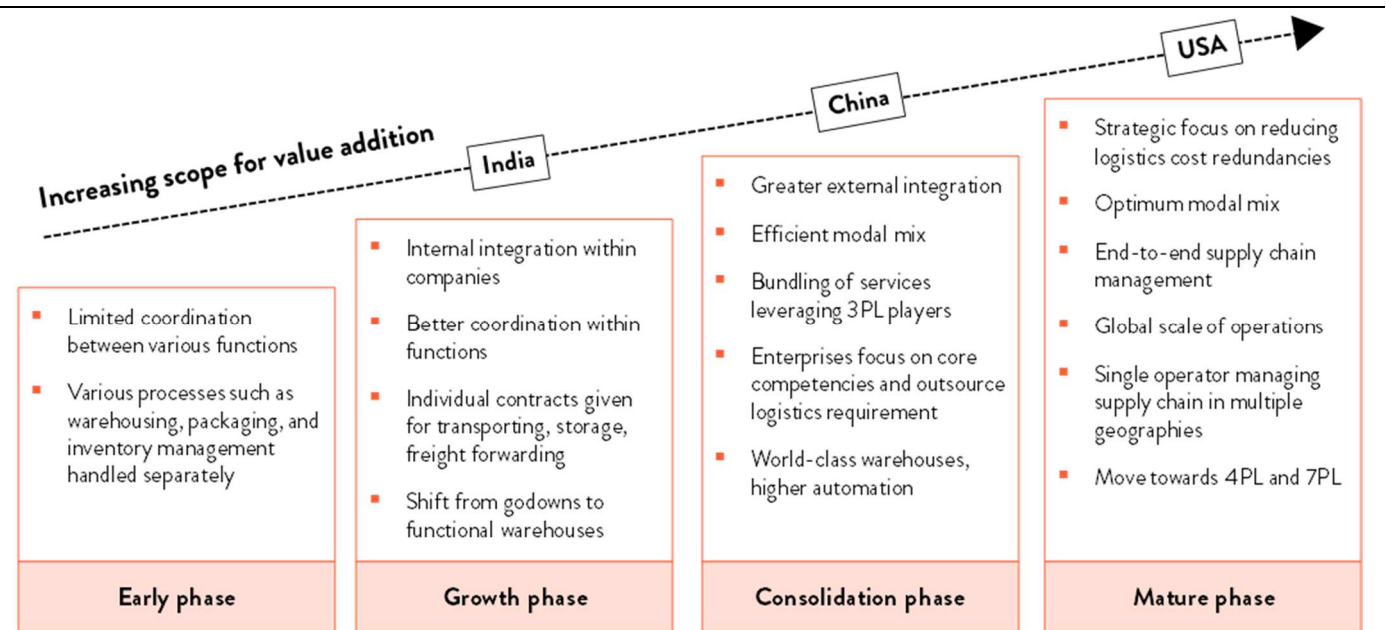
Indian logistics industry – evolving rapidly

Structural trends, reforms transforming India's ~US\$ 160bn logistics industry

India's ~US\$ 160bn logistics industry is undergoing a rapid transformation phase. The industry has historically been fraught with inefficiencies, leading to a suboptimal modal mix, inadequate supply chain networks and the dominance of unorganised players. However, recent structural reforms (GST, e-way bill) and infrastructure push (dedicated freight corridor, multi-modal logistics parks, push for inland waterway development) are addressing these inefficiencies and creating a level playing field for organised players, ushering in a new era for the sector.

Riding on these transformational developments, we expect logistics companies in India to provide multiple value creation opportunities to investors over the next few years. Growth will be led by following key themes that we forecast will play out over the medium-to-long term – (1) industry consolidation in favour of organised players; (2) rise in demand for value-added and integrated logistics services, over traditional execution focused transportation and warehousing; and (3) opportunities arising out of ebbing inefficiencies.

FIG 8 – INDIA'S LOGISTICS INDUSTRY DEVELOPING APACE



Source: Knight Frank, BOBCAPS Research

A fragmented industry...

India's logistics industry is a combination of various heterogeneous segments. Companies operate in one or more diverse segments of the industry, viz. road transportation, container rail, warehousing, 3PL, express distribution, NVOCC and CFS/ICD; adopt various business models such as asset light vs. asset heavy/B2B vs. B2C; and are present in different geographies – global, pan-India and regional.

**Unorganised segment
accounts for ~90% of industry**

The industry is also highly fragmented, characterised by the presence of numerous unorganised or regional players, which accounts for ~90% of the industry. These players dominate specific segments, primarily road transportation and warehousing.

FIG 9 – BUSINESS LANDSCAPE OF KEY LOGISTICS PLAYERS IN INDIA

Companies	Transportation					Storage			Aggregators/Service providers	
	Road (FTL & LTL)	Container rail	Coastal/ Inland	Surface express	Air express	Warehousing	CFS/ICD	Cold chain	3PL/Contract logistics	NVOCC/Freight forwarding
AGLL						✓	✓		✓	✓
BDE				✓	✓					
CCRI		✓	✓				✓			
FSCS				✓				✓	✓	
GDPL		✓					✓			
MLL									✓	✓
NACO							✓			
SNLL								✓		
TCIEXP				✓	✓					
TRPC	✓		✓						✓	
VRLL	✓									

Source: Company, BOBCAPS Research | Note: Highlighted cells indicate the company's presence in a segment | BDE: Blue Dart Express, GDPL: Gateway Distriparks; NACO: Navkar Corporation; SNLL: Snowman Logistics; VRLL: VRL Logistics

...fraught with structural constraints

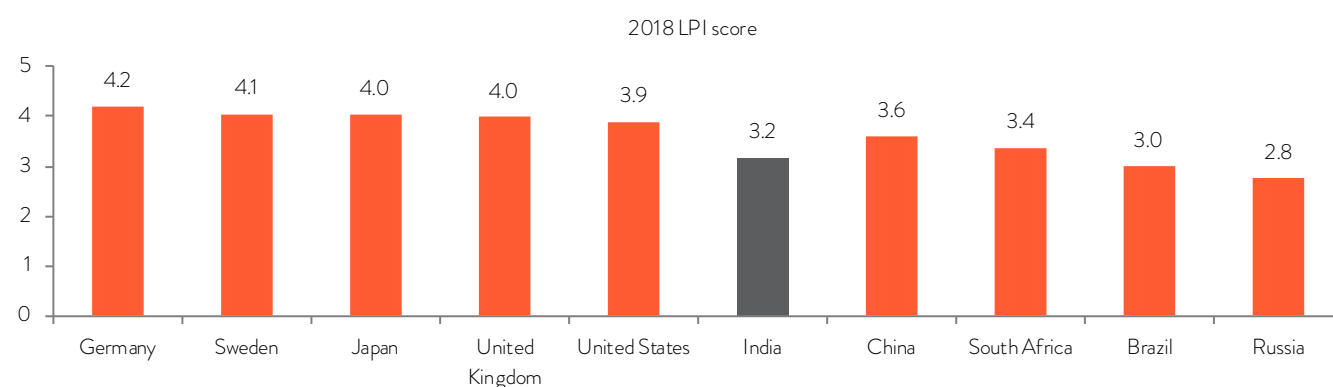
**Several key constraints lead to
inefficiencies in the Indian
logistics industry**

Traditionally, the Indian logistics industry has been plagued by several inefficiencies which have prevented it from achieving its full potential. A subpar modal mix, lack of formalisation and other infrastructural shortcomings exert pressure on overall logistics cost and impede efficiency gains. Consequently, India's rank in the World Bank's logistics performance index is also lower than comparable nations. The key inefficiencies can be classified into five broad categories, as depicted below.

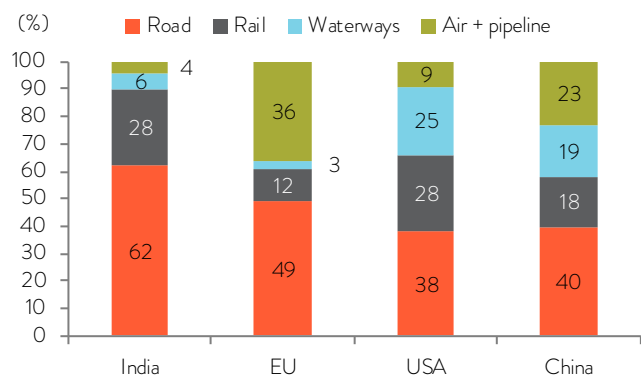
FIG 10 – KEY CONSTRAINTS IMPEDING INDIA'S LOGISTICS SECTOR PERFORMANCE

Factors	Issues and their impact
Suboptimal modal mix	<ul style="list-style-type: none"> Road transport has higher per-tonne-km (tkm) costs (~Rs 1.5) than the rail (Rs 1) and coastal (Rs 0.25) modes, while carbon emissions are also higher Inadequate rail infrastructure and underdeveloped coastal transport in India tilt the balance towards the less efficient road transport segment, leading to higher logistics costs and lower fuel efficiency.
Lack of formalisation/higher share of unorganised sector	<ul style="list-style-type: none"> The unorganised sector comprises ~90% of the logistics industry, especially in road transportation. This leads to an inefficient fleet mix, impedes adoption of global best practices and hinders technology investments.
Inadequate transport infrastructure	<ul style="list-style-type: none"> India's road as well as rail infrastructure remains substantially below global standards. Freight carriageway (four-lanes+) density is low for road transport, while high traffic density hinders rail speeds. For example, the average distance covered by a truck in India is 250-300km a day, 50-60% below global standards. Average rail speed is also much lower (~25km/hour while the global average is 2-3x higher). Inadequate infrastructure also creates challenges for last-mile and hinterland transportation.
Underdeveloped material handling infrastructure	<ul style="list-style-type: none"> India has unorganised logistics parks with limited technology deployment and immature infrastructure. Lack of mechanised material handling capacity hinders container movement and restricts efficient inter-modal transportation.
Procedural complexities	<ul style="list-style-type: none"> Complex documentation and procedures required for inter-state transport serve to delay customs clearance at ports.

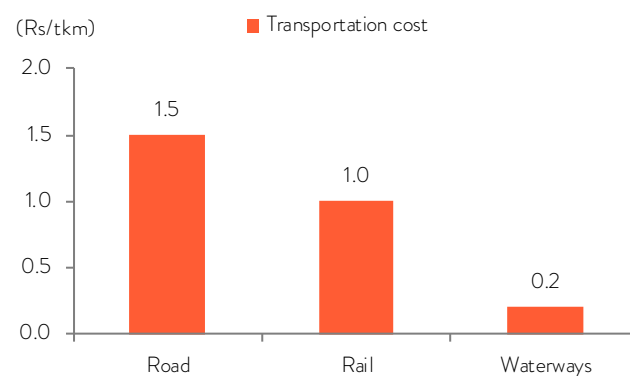
Source: Government Documents, Industry interactions, BOBCAPS Research

FIG 11 – INDIA'S LOGISTICS PERFORMANCE INDEX (LPI) SCORE IS LOWER THAN DEVELOPED AS WELL AS SOME DEVELOPING NATIONS

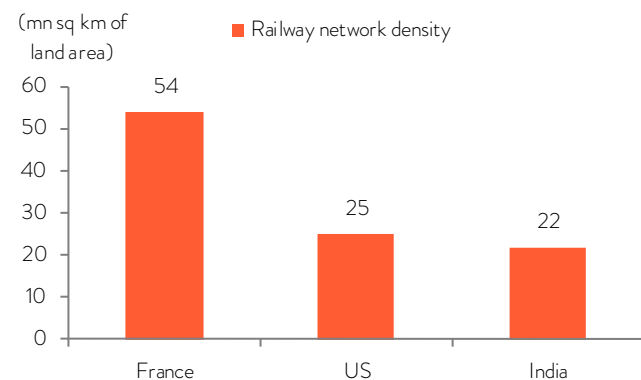
Source: World Bank, BOBCAPS Research

FIG 12 – INDIA’S TRANSPORT MODAL MIX IS SKEWED TOWARDS ROADS...


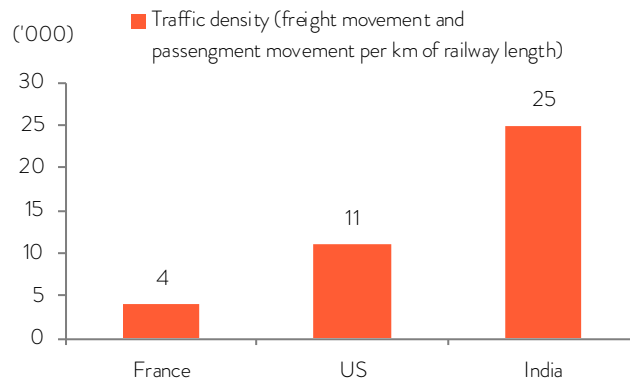
Source: Industry, BOBCAPS Research

FIG 13 – ...ALTHOUGH THIS MODE IS LESS EFFICIENT THAN RAIL AND WATERWAYS MOVEMENT


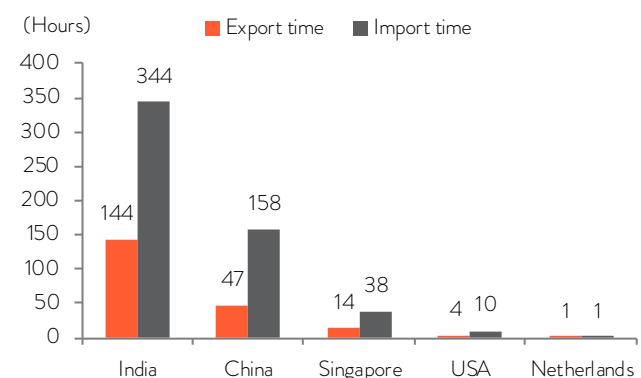
Source: Industry, Indian Railways & Shipping Ministry estimates, BOBCAPS Research

FIG 14 – RAILWAY NETWORK DENSITY LOWER THAN GLOBAL STANDARDS


Source: Indian Railways, Industry, BOBCAPS Research

FIG 15 – HIGH TRAFFIC DENSITY LEADS TO LOWER RAIL SPEED


Source: Indian Railways, Industry, BOBCAPS Research

FIG 16 – EXIM LEAD TIME SIGNIFICANTLY HIGHER THAN MOST COUNTRIES


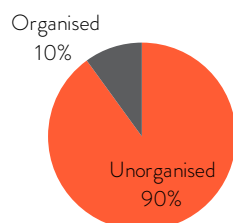
Source: Industry, BOBCAPS Research

FIG 17 – ROAD INFRASTRUCTURE ALSO SUBOPTIMAL VIS-À-VIS GLOBAL STANDARDS

Parameter	India	Global
Avg. truck speed (kmph)	30-40	60-80
Four land road length (kms)	7,000	34,000 (China)
National highway length (in kms)	~80,000	~1,900,000
Avg. distance travelled by a truck per day (km)	200-250 (pre-GST)	400

Source: Cygnus Business Consulting & Research, KPMG BOBCAPS Research

Unorganised players dominate India's logistics industry



Source: CARE, BOBCAPS Research

Large-scale reforms to have profound impact on the industry

Inefficiencies have helped unorganised players proliferate

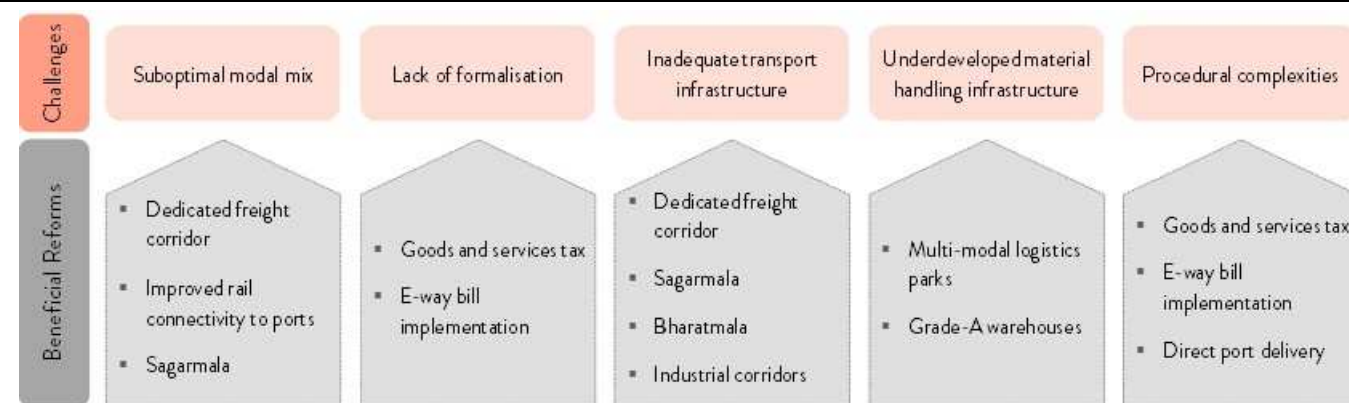
The sub-optimal industry structure has helped unorganised players thrive and prevented large-scale formalisation of the sector. According to industry sources, ~90% of traditional industry segments such as warehousing and road transport are unorganised. Consequently, the top 10 listed logistics players in the country cumulatively account for ~5% of the total industry share.

However, we note that logistics in India is in the midst of a paradigm shift, as structural reforms and evolving supply-chain requirements fast pave the way for formalisation of the sector – this in turn will open up tremendous business opportunities for organised players, in our view.

Structural reforms to ease impediments to growth

We outline below a host of ongoing government reforms and infrastructure developments that are likely to resolve most of the inefficiencies plaguing the logistics industry. Industry estimates peg the total government-led investment earmarked for infrastructure development which supports logistics industry – road and rail networks, ports, airports, logistics parks and freight stations – at US\$ 700bn over CY18-CY22, which should ease infrastructure bottlenecks. Other recent reforms – GST, e-way bill and infrastructure status for the sector – should resolve procedural aspects.

FIG 18 – STRUCTURAL REFORMS TO EASE BOTTLENECKS



Source: Industry, BOBCAPS Research

- GST implementation:** Implementation of the Goods and Services Tax (GST) in FY18 is having a multi-faceted impact on the logistics industry. The transportation segment is witnessing lower turnaround time (20-25% reduction) after abolishment of check-posts, higher productivity, increased demand for grade-A warehouses with realignment of the supply chain network, and a surge in demand for value-added services.

Organised players are expected to get a further boost as the transformational changes wrought by the GST regime gather pace, wherein companies move past the planning phase and start realigning their supply chains to maximise cost benefits.

FIG 19 – OPPORTUNITIES ARISING OUT OF GST

Industry segment	Evolved logistics requirements	Opportunities for organised players
Transportation	<ul style="list-style-type: none"> Higher capacity of vehicles for hub-to-hub transportation Change in vehicle mix for hub-to-spoke/secondary transportation 	<ul style="list-style-type: none"> Offer higher capacity vehicles required for primary transportation Attain the right mix of vehicles for secondary transportation, offering optimum service for clients
Warehousing	<ul style="list-style-type: none"> Higher demand for larger, grade-A warehouses at hubs Demand for reduced inventory and warehousing costs for transportation 	<ul style="list-style-type: none"> Make higher investments in technology-enabled, grade-A facilities Opportunity for pan-India players capable of delivering multi-location, multi-service capabilities to increase market share
Value-added services	<ul style="list-style-type: none"> Integration of logistics services Higher need for outsourcing 	<ul style="list-style-type: none"> Opportunity to provide integrated logistics services Offer efficient value-added services to clients and help them achieve strategic objectives

Source: FSCSL Prospectus (Alvarez & Marshall), BOBCAPS Research

- E-way bill:** Stricter implementation of the e-way bill is likely to tilt the balance towards organised players. Required for all consignments worth over Rs 50,000, e-way bills have enhanced the compliance burden for the unorganised sector. Since these players do not have the wherewithal to adequately invest in the compliance and technology systems required under the new regime, demand is likely to shift towards the organised sector. While penal action against non-compliance has not been stringent so far, industry participants expect stricter implementation post the general elections.
- Dedicated freight corridor (DFC):** The long-awaited DFC is closer to reality with the first stretch scheduled to be commissioned by Sep'19. Significant improvement in rail infrastructure post DFC commissioning is expected to propel a shift in freight volumes from the less efficient road transport segment (owing to higher per tonne-kilometre cost and higher carbon emissions) to rail, enabling the sector to move closer to an optimal modal mix.
- Rail connectivity to ports:** To enhance the share of railways in export-import (EXIM) movement, the government is aiming to increase the rail connectivity between ports and hinterlands. Apart from DFC, a total of 86 rail connectivity projects have been identified under the Sagarmala initiative, spanning 6,934km, with US\$ 10.2bn of investments envisaged over the next 15 years.

First stage of DFC scheduled to be commissioned by Sep'19

Sagarmala aims to improve port and related infrastructure; augurs well for coastal movement of cargo

- **Sagarmala:** The Indian government embarked on the ambitious Sagarmala programme in 2015 with a view to improve the modal mix for domestic and EXIM cargo transport by boosting coastal transportation, lower logistics cost of bulk commodities, and improve export competitiveness by developing port infrastructure. About 600 projects have been identified with an estimated investment of US\$ 120bn, to be completed over 2015-35. This initiative is expected to bolster coastal transport and improve the modal mix.
- **Bharatmala:** Under the Bharatmala Pariyojana programme Phase -I, the government plans to develop 34,800km of road infrastructure at an outlay of US\$ 76bn over 2018-22. Initiatives such as these to improve road infrastructure bode well for last-mile transportation and hinterland connectivity, besides improving average truck speed.
- **Multi-modal logistics parks (MMLP):** Development of MMLPs in critical hub locations is expected to shore up the inadequate material handling infrastructure in India and boost inter-modal transportation. Several MMLPs are being developed along the DFC – CCRI alone has invested in ~15 parks – while the government envisages the development of 35 more MMLPs in key locations under the Bharatmala Pariyojana.
- **Infrastructure status and separate ministry:** The government recently granted infrastructure status to the logistics industry and also created a separate division for it within the Ministry of Commerce. This is expected to ease access to financing for logistics companies.

Diverse models in play – traditional execution-focused vs. new-age service-oriented; asset-light vs. asset-heavy

Interesting interplay of diverse business models

India's logistics industry is a culmination of diverse business models. Traditional models such as road transportation, container rail and CFS/ICD are execution-focused and asset-heavy, whereas relatively newer-age businesses such as 3PL and express delivery are service-oriented, focused on value-addition and are typically asset-light. A company may follow an asset-light strategy for one business segment and an asset-intensive structure for another. Even within the same industry segment, asset ownership – and therefore margins and ROCE – can vary depending on the modal and business mix.

For example, within 3PL, MLL generates much higher gross asset turnover vis-à-vis FSCSL and TRPC (supply chain business) owing to its asset-light model, while FSCSL and TRPC enjoy far better operating margins owing to a higher share of warehousing/asset ownership. Further, a divergent business mix (between LTL and FTL) and asset ownership strategy leads to different margin and ROCE profiles for VRLL and TRPC's freight business. The diversity of logistics business structures and their accompanying nuances create unique investment themes for investors.

Evolving logistics needs fostering new-age business models

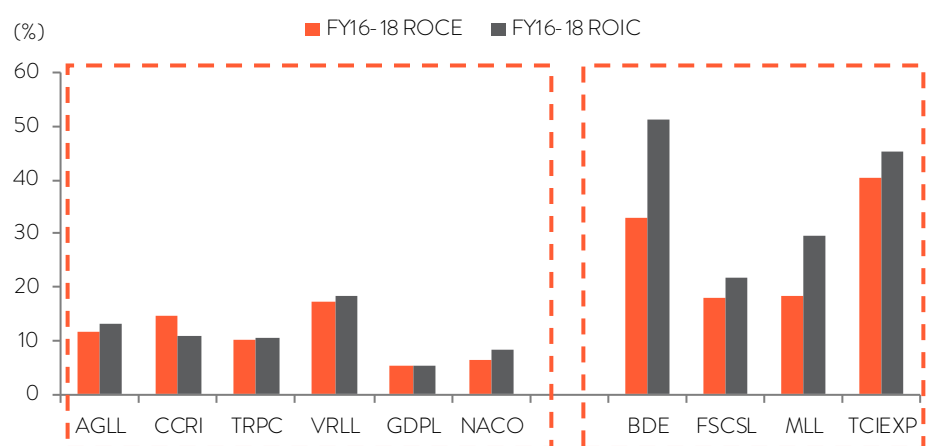
With logistics gaining strategic importance, the supply chain requirements of manufacturers have also evolved. While the focus was traditionally on execution (plain-vanilla transportation and warehousing of cargo), value-added services have gradually gained prominence, facilitating the emergence of new-age business models.

Consequently, over the past decade, service-oriented segments such as express and 3PL have mushroomed. These segments offer value-addition beyond the traditional transportation and storage services, leverage technology for efficiency gains, and offer integrated logistics solutions. Moreover, several new start-ups such as Delhivery and Rivigo have emerged which rely on innovative methods to rise above the existing inefficiencies. The advent of these next-gen businesses is playing a pivotal role in transforming the logistics industry.

Service-focused models generate higher return ratios

As depicted in the chart below, service-oriented businesses typically generate higher return ratios than traditional businesses, as the former often focus on offering value-added services following an asset-light model, in contrast with the latter's asset-intensive model. Owing to their integration with client supply chain ecosystems, service-focused businesses also have higher client switching costs and pricing power. Lastly, owing to the low penetration of these businesses currently, they also offers a multi-year, structural growth opportunity.

FIG 20 – LOWER ASSET INTENSITY HELPS SERVICE-LED MODELS GENERATE BETTER RETURN RATIOS



Source: Company, BOBCAPS Research

Contemporary, service-led businesses have better fundamentals vs. traditional, execution-led ones

















































New-age businesses better placed than traditional ones

The new-age businesses are typically less asset-intensive and are thus capable of generating higher ROCE/ROE, higher free cash flow, and have better balance sheets. These segments are also in the early growth phase and offer large, multi-year scalable growth opportunities. While we are cognizant of the company-specific nuances, we largely prefer the newer business models over the traditional ones as investment themes.

3PL, express, container rail segments most attractive

For long-term investment ideas, we prefer companies operating in the 3PL and express industries as these segments exhibit scalable growth potential, moderate asset intensity and high entry barriers. Among traditional sectors, container rail has structural tailwinds which makes it our next preference. The following table depicts the fundamental strengths of different industry segments within logistics, along with our industry attractiveness score.

Attractiveness matrix for logistics segments – prefer 3PL and express

Industry	Est. market size (Rs bn)	Past 5-yr CAGR (%)	Future growth expectations (%)	Entry barriers	Customer stickiness	Capital intensity	Ability to fend off systemic risks	Premiumisation	ROCE	Overall industry attractiveness
Road – FTL	6,300-6,500	10-12	5-8							Low
Road – LTL	700-750	12-15	10-12							Moderate
Container rail	80-85	6	12-15							Moderate
Coastal shipping/inland waterways	45-50	10-12	12-14							Moderate
Express	250	~18-20	15-17							High
CFS/ICD	50-55	4-5	2-3							Low
3PL	450-480	18-20	17-18							High
NVOCC	250-300	7-8	5-6							Moderate

Source: FSCSL Prospectus (Alvarez & Marshall), MLL Prospectus (CRISIL Research), Industry, BOBCAPS Research

 Very high
  High
  Moderate
  Low
  Very low

3PL – best long-term play in the sector

Scalable growth potential, strong moats, and low asset intensity make 3PL our most preferred segment

From amongst the various segments of India's logistics sector, third-party logistics or 3PL is our most preferred as it offers the rare trinity of (1) scalable growth potential aided by structural tailwinds (we forecast a robust 17-18% CAGR for the industry over the next few years), (2) low asset intensity, and (3) scope to develop sustainable competitive advantages. These attributes make 3PL one of the highest ROCE generators in the logistics industry.

Among the 3PL players operating in India, we believe MLL checks all the right boxes for growth (countrywide presence, well-rounded logistics footprint, asset-light business, strong clientele), followed by FSCSL (dominance in fast-growing consumer verticals, growing anchor clients) and TRPC (attractive valuations).

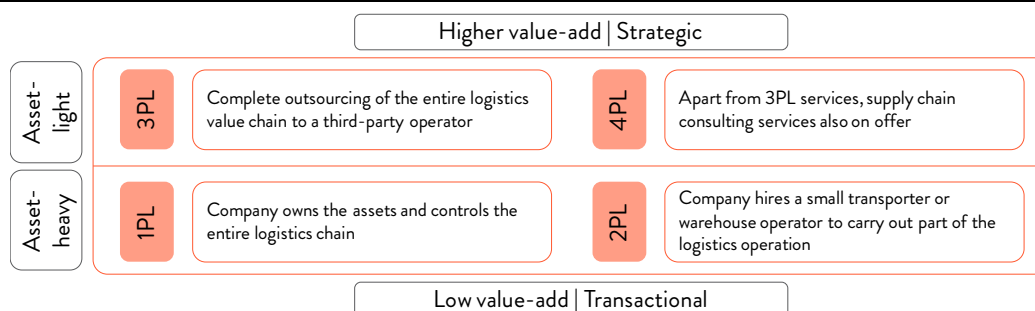
Critical cog in client operational ecosystems

Traditionally, logistics activities – transportation and warehousing – were supportive functions for end-user companies, with limited strategic importance. Two dominant models existed – one where the company owned the assets (vehicles for transportation and warehouses for storage), called the 1PL model, and another where it would hire small transporters or warehouse operators to carry out a part of the logistics function (the 2PL model).

As the economy matured and companies gained scale, they shifted their focus to optimising core operations, while control of the entire logistics function – from inbound logistics and warehousing to outbound logistics – was outsourced to third-party players, thus giving rise to 3PL logistics. Typically, these players follow an asset-light model, meeting vehicle and warehouse requirements through lease.

As procurement and distribution gradually became differentiating factors for manufacturers, 3PL players assumed a more strategic role, integrating themselves into the operational ecosystem of client companies. Today, apart from carrying out logistics operations effectively, 3PL providers also focus on efficiency gains by deploying technology and optimising costs for clients.

FIG 21 – 3PL AND 4PL OFFER HIGHER VALUE-ADD WHILE NEEDING LOW INVESTMENTS IN ASSETS



Source: Company, BOBCAPS Research

A potentially large, scalable opportunity

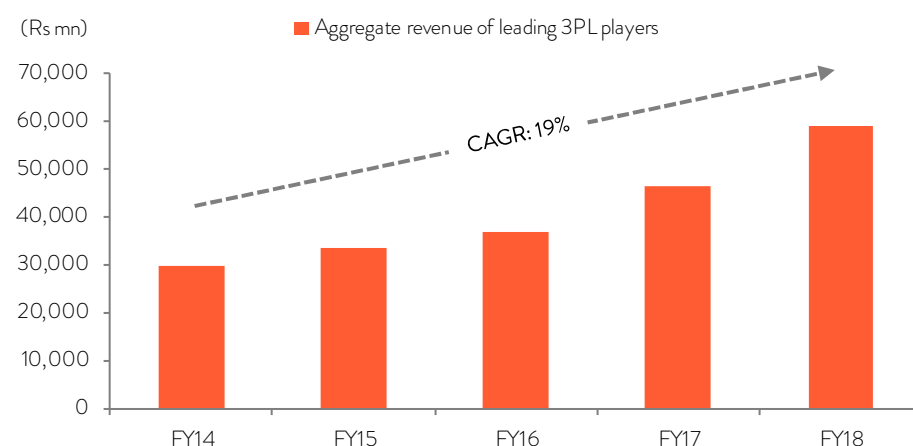
India's 3PL industry, currently estimated at Rs 450bn-480bn, provides a long-term scalable opportunity. Rising adoption of 3PL services by Indian manufacturers has propelled growth of the segment in the past few years. Despite this, penetration of 3PL in India remains well below global standards. Growing demand traction for third-party services coupled with favourable regulations (GST, e-way bill) is expected to pave the way for another strong phase of growth.

3PL segment witnessing sturdy growth

Over FY14-FY18, aggregate revenue of the leading 3PL players – MLL, FSCSL, TRPC (supply chain solutions segment), and TVS Logistics Services (TVSLSL; standalone business) – has grown at a strong 19% CAGR. Growth in key user industries such as automobiles, retail and consumer together with an increasing focus on outsourcing of non-core activities has catalysed this growth.

Aggregate revenue of leading 3PL players grew at 19% CAGR over FY14-FY18

FIG 22 – AGGREGATE REVENUE OF LEADING 3PL COMPANIES EXHIBITED STRONG GROWTH IN RECENT YEARS



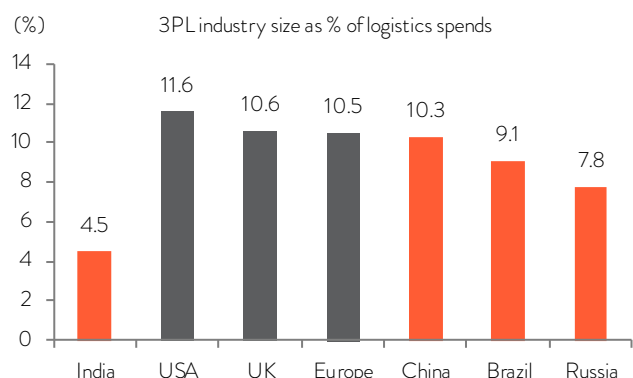
Source: Company, BOBCAPS Research

Under-penetration provides ample headroom for growth

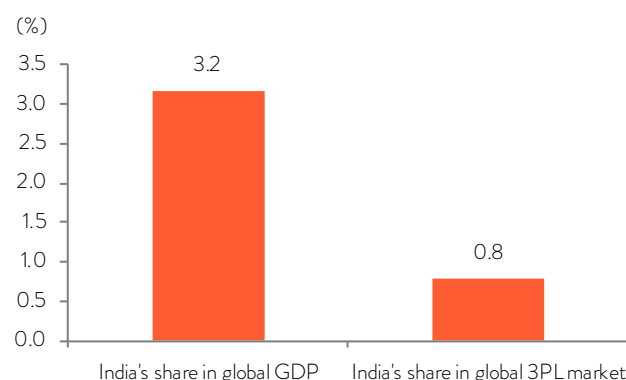
Despite the recent run-up, the Indian 3PL industry remains at an early stage of adoption. India's 3PL industry as % of total logistics spend is much below global standards, as the industry is still at a nascent stage and clients are yet to fully embrace the concept. Moreover, despite contributing ~3% of global GDP, India contributes less than 1% of the global 3PL market.

This gap indicates tremendous headroom for future growth – even assuming no growth in the total logistics spend, 1% incremental penetration is likely to lead to 20-25% growth every year in the 3PL segment.

India's 3PL industry as % of total logistics spend is lower than developed and some developing countries

FIG 23 – 3PL SHARE IN INDIA LOWER THAN MOST OTHER COUNTRIES


Source: Armstrong & Associates, BOBCAPS Research | Note: India's share is as per our estimate of 3PL segment and total logistics industry size

FIG 24 – INDIA'S CONTRIBUTION TO GLOBAL 3PL INDUSTRY STANDS AT A PALTRY 0.8%


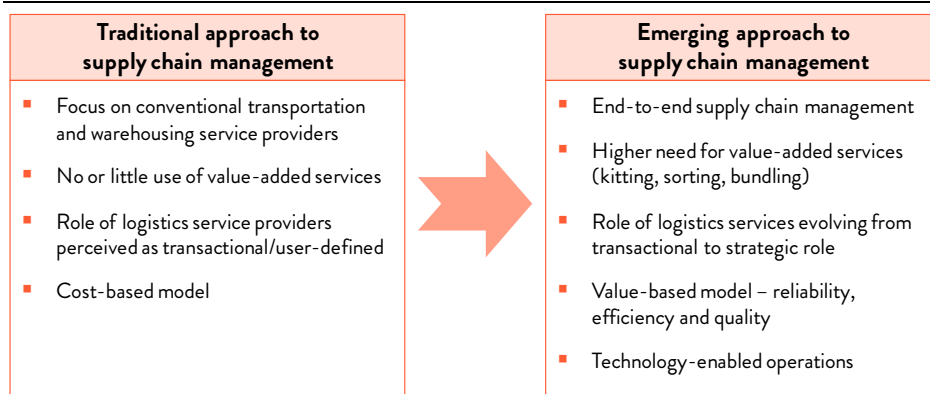
Source: IMF, Corn Ferry Annual 3PL Study, BOBCAPS Research

Confluence of structural tailwinds to hasten 3PL growth

We expect a confluence of growth enablers to propel the segment forward. Most of these factors are structural in nature – evolving supply chain practices, growing trend of outsourcing non-core activities, implementation of GST – and hence should translate into multi-year growth opportunities. We elaborate on the key factors below.

Evolving supply chain practices

With a rising scale of operations and growing complexity of business, the supply chain management needs of Indian companies are evolving. From the traditional focus on merely carrying out transportation and warehousing activities at the lowest cost possible, the emphasis is gradually shifting to end-to-end efficient supply chain management. Moreover, companies are looking at a single partner to manage all logistics-related activities instead of multiple vendors.

FIG 25 – INDIAN SUPPLY CHAIN PRACTICES IN A TRANSFORMATIVE PHASE


Source: FSCSL Investor Presentation, BOBCAPS Research

We believe 3PL players are in an advantageous position to meet the emerging supply chain needs of clients compared with C&F agents and 2PL service providers/asset owners given their ability to (1) offer efficient and reliable services, (2) leverage on technology, (3) manage large-scale operations (large warehouses, multi-user facilities, hub-and spoke transportation across the country), and (4) provide value-added, customised solutions.

Trend of outsourcing non-core activities

The growing focus on core competencies and hence outsourcing of non-core yet crucial activities by enterprises is likely to facilitate growth of the 3PL industry. Competitive pressure and the need for efficiency gains are compelling companies to run leaner operations, necessitating outsourcing. Outsourcing can also reduce capital investments by eliminating the need to own assets such as warehouses, technology platforms and vehicles, as these are managed by 3PL service providers.

GST rollout fuelling 3PL adoption

Post GST implementation across India in FY18, supply chain networks in many industry verticals are undergoing a revamp. Realignment of supply chains, as outlined below, has wide-arching implications for the logistics industry in general and 3PL players in particular –

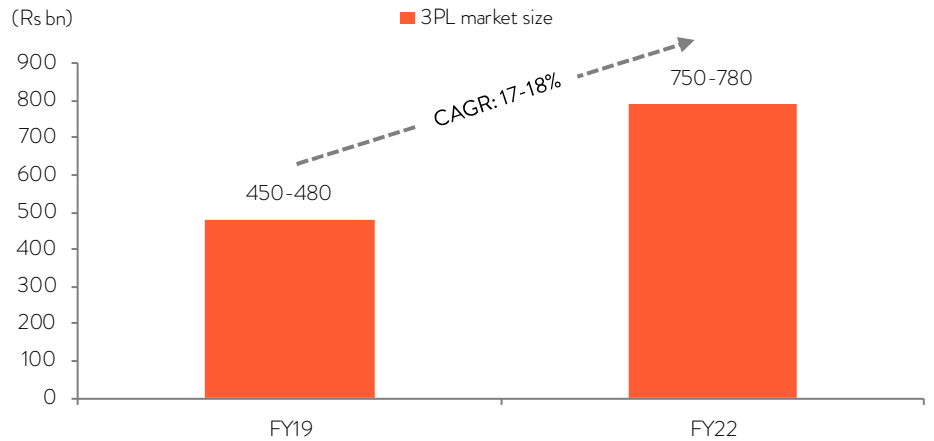
- Consolidation of warehouses as client focus shifts to efficiency gains from tax planning, giving rise to larger, grade-A warehouses – while companies have been slow to rejig their supply chain networks, industry sources indicate that this process is gradually picking up pace.
- Advent of centralised warehouses, translating into proliferation of the hub-and spoke model – this will, in turn, necessitate larger truck sizes for hub-to-hub transportation and reduce average handling costs.
- Higher need for technology-enabled solutions and inventory management

Expect 3PL segment to grow at strong ~18% CAGR

Driven by the factors mentioned above, we expect the 3PL industry to register a strong 17-18% CAGR to Rs 750bn-780bn by FY21, one of the fastest growth rates among logistics segments. This growth is likely to be helmed by the consumer-centric and auto verticals. Further, we expect the larger 3PL players to grow faster than the industry and expand market share. At the same time, any slowdown in key industry verticals, such as auto, may create challenges for growth.

Industry sources indicate supply chain consolidation gathering pace under GST

Demand for grade-A warehousing also rising

FIG 26 – 3PL INDUSTRY EXPECTED TO POST STRONG GROWTH

Source: Company, BOBCAPS Research

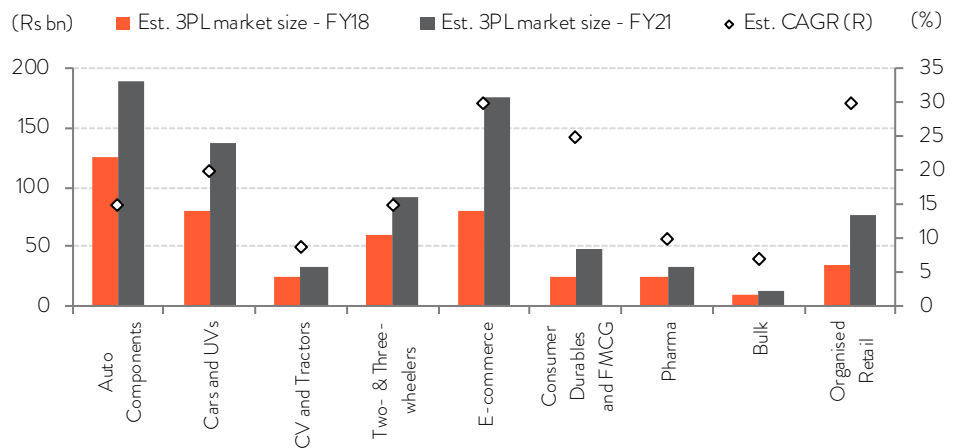
Key 3PL market trends

Based on our analysis and industry interactions, we have identified three broad trends playing out in the 3PL industry – (1) demand from consumer-focused and auto industries is growing at a faster pace, (2) asset-light players are outperforming peers, and (2) larger 3PL players are steadily gaining market share,

Consumer, auto verticals offer best opportunities

We expect consumer-oriented verticals such as durables, FMCG, organised retail, along with automobiles and engineering, to offer the best growth potential for 3PL players going ahead. Demand from consumer-centric verticals is projected to grow at a 25-30% CAGR over the next few years driven by increasing penetration and end-market growth, outpacing overall 3PL industry growth of 17-18%. We expect 3PL business from the auto and engineering verticals to grow in line with the industry despite their relatively high penetration currently.

Growth in end-user markets, rising adoption to drive consumer-oriented 3PL growth

FIG 27 – VERTICAL-WISE 3PL OPPORTUNITY

Source: Company, BOBCAPS Research

Asset-light the way forward

Although globally 3PL players typically have an asset-light business model, in the Indian context, we additionally see a hybrid of asset-intensive/light structures. In the latter, the logistics company may own a part or all of the warehouses it operates, and/or the vehicles it needs for transportation. We prefer the pure-play asset-light model wherein the assets involved are completely leased, as this offers higher scalability and flexibility with minimum capital investments.

Large 3PL players to consolidate their market position

As mentioned, the Indian 3PL market remains fragmented, with a number of players offering either integrated or select services. We believe larger 3PL players (MLL, FSCSL and TRPC) are better positioned for growth and market share gains than smaller players as the former enjoy distinct advantages, such as (1) a pan-India presence, (2) more cost-effective solutions owing to their larger scale of operations, (3) an ability to invest in technology, (4) greater flexibility and reliability of services, and (5) ability to offer customised solutions to customers.

Scope to erect strong entry barriers

One of the key reasons for our preference of 3PL over other verticals of the logistics industry is that players can create sustainable moats that are hard for competitors to emulate. These include –

- **Large scale:** Our interactions with industry participants indicate that scale acts as a critical moat for the 3PL industry as it enables (1) higher utilisation of warehouses and vehicles, (2) higher load per trip, and (3) pan-India management of warehouses and transportation.
- **Sticky clientele:** 3PL services are deeply ingrained in the operational ecosystems of clients. Client engagement typically starts at the CXO level, which translates into deep relationships. Some 3PL players also have their own employees present in various client manufacturing plants to understand respective manufacturing processes.

This relationship translates into high switching costs for customers and hence client stickiness – historically, client retention for large 3PL players has been very high, at ~96% for MLL and ~100% for FSCSL.

- **Multi-industry exposure:** Experience of working with clients across multiple industries is also a critical success factor. Multi-industry exposure helps logistics providers better understand industry-specific nuances, which in turn hastens client addition in these industries. Hence, 3PL companies with clientele across industries are better placed to generate new business from these industries.






















High client retention rates – ~96% for MLL/~100% for FSCSL – reflect high switching cost for customers

- **Large anchor customers:** The presence of one or more anchor customers, preferably well established in their respective industries, also acts as a strong moat. Anchor customers provide stability to the revenue base and ensure optimum utilisation of warehouses and vehicles.

MLL, FSCSL our preferred picks in the 3PL segment

Among the 3PL players operating in India, we prefer MLL, followed by FSCSL and TRPC. While we are positive on the prospects of each of these companies, we believe MLL is ahead of the pack as it ticks all the requisite boxes for accelerated growth, while FSCSL comes a close second. TRPC, on the other hand, offers the most attractive valuations of the three (adjusted for its other divisions).

FIG 28 – COMPETITIVE POSITIONING OF 3PL PLAYERS

Parameter	MLL	FSCSL	TRPC (Supply chain solutions segment)
Positioning on key parameters			
Scale of operations			
Capital allocation/asset ownership			
Presence in growing verticals			
Market position of anchor customers			
Growth prospects of anchor customers			
Non-anchor client portfolio			
Scope for improvement in business mix			
Financial parameters (FY16-FY18) (%)			
Revenue CAGR	28.7	22.1	20.3
Avg. EBITDA margin	3.0	14.1	10.5
PAT CAGR	33.3	51.3	NA
Gross asset turnover (x)	33.0	3.1	2.3
Avg. ROCE	21.2	18.0	18.1
Avg. ROE	14.5	16.2	NA
Debt/EBITDA (x)	0.4	0.9	2.2*

Source: Company, Industry, BOBCAPS Research | *For the consolidated entity

 Very Strong
  Strong
  Moderate
  Weak
  Very weak

- MLL has larger scale with the highest revenue and warehousing space
- Better capital allocation is reflected in better asset turn
- FSCSL's presence in the faster growing consumer verticals is higher
- TRPC's supply chain segment does not have an anchor client
- MLL has a larger non-anchor client portfolio
- MLL and TRPC have scope to improve the share of high-margin warehousing segment
- Avg. EBITDA margin for FSCSL is high owing to higher warehousing share

Express distribution – accelerating ahead

The Indian express industry has evolved rapidly in recent years. Focused predominantly on the delivery of documents till the early 2000s, the industry has since been revolutionised by rising B2B demand, growing demand from SMEs and the advent of e-commerce.

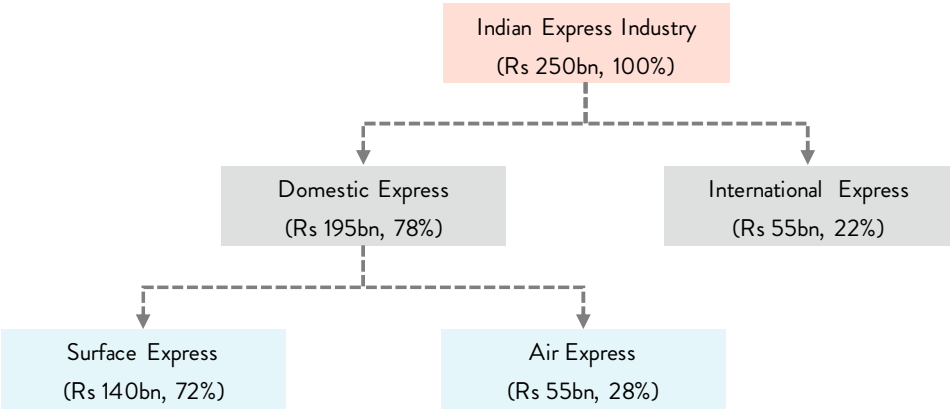
TCIEXP best placed in the fast-growing express industry

We expect the express distribution industry to grow at a brisk ~15% CAGR over the next five years, fuelled by rising demand for time-sensitive delivery from the manufacturing, SME and burgeoning e-retail segments. Surface express is projected to grow at a faster clip of 18-20%, while large players is likely to outpace industry growth. In our view, TCIEXP looks best positioned to ride the industry tailwinds on the strength of its wide surface express footprint and focus on the fast-growing B2B segment.

Domestic express industry has made rapid strides

India’s express industry is classified into the domestic and international express categories. Based on the mode of transport, the domestic business is further bifurcated into surface express (road and rail), while international express delivery is done entirely by air.

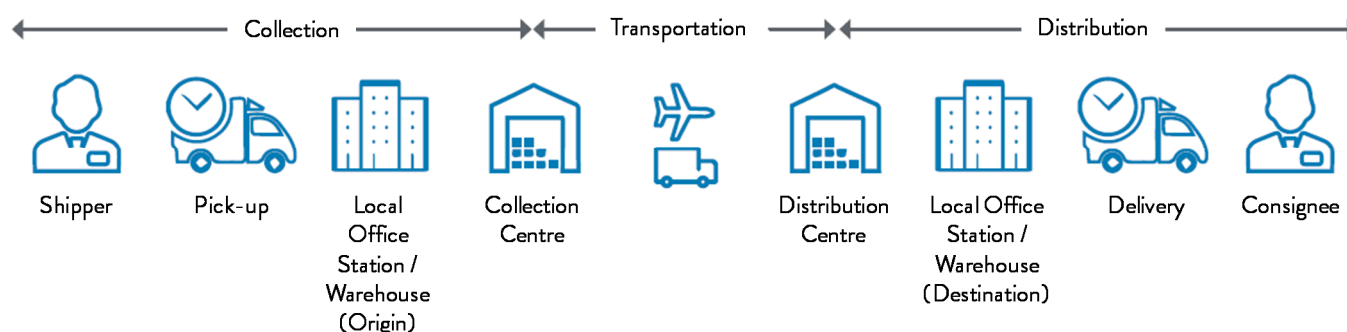
FIG 29 – INDIAN EXPRESS INDUSTRY CLASSIFICATION



Source: Deloitte, Industry Interactions, BOBCAPS Research

Time-bound, door-to-door delivery defines express

The key value proposition of express delivery service is door-to-door delivery of shipments (typically LTL) in a time-sensitive manner, with real-time shipment tracking facilities. Although the shipment may entail multiple legs of transport through different modes, the customer generally has to deal with only one touchpoint for the entire lifecycle of the delivery. The indicative value chain of express delivery is highlighted below.

FIG 30 – VALUE CHAIN OF EXPRESS DELIVERY**Flow of shipments in the express industry**

Source: Deloitte, Industry Interactions, BOBCAPS Research

Conducive climate for surface express, pan-India players

Two overarching themes –
(1) surface express to grow
faster than air, (2) players
with wide reach to thrive

Our analysis of the express industry suggests two key emerging themes – (1) surface express players will continue to outpace air express players, and (2) players with a national reach will continue to garner market share. An aggregation of these two themes should enable pan-India, surface express-focused players to outperform competitors. We analyse each of these themes in detail below.

Surface express to continue garnering share from air

Going ahead, we expect surface express (primarily road) growth to be substantially higher than the air express industry, at 18-20% over the next five years vis-à-vis low single-digit growth for the latter, driven by a shift in customer preference. The following factors are expected to underpin this shift –

Air express shipments costs
4-5x more than surface
express

- **Steep cost divergence:** Divergence in the cost of booking an express shipment through air and surface transport has always been steep (air being 4-5x more expensive). However, air was still preferred by certain industries with highly time-sensitive cargo, such as pharmaceuticals, electronics, auto components, and e-commerce, owing to its lower transit time.

Two developments in recent times have led to a massive shift in customer preference towards the less expensive surface transport mode – (1) rising cost pressure on manufacturers which is compelling them to look for low-cost alternatives, and (2) adoption of technology (such as mobility-based tools, network optimisation software and fuel sensors) by surface express players which is enabling them to shorten transit time. E-commerce is a clear example of this trend, where air express had ~80% share in 2014 which has since nosedived to ~20% by 2018, as per industry estimates.

FIG 31 – AIR EXPRESS COST ~4X THAT OF SURFACE EXPRESS ON AVERAGE

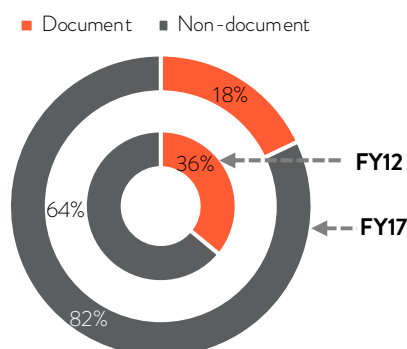
Mode (Rs/10kg non-document parcel)	Delhi-Mumbai	Delhi-Bengaluru	Delhi-Kolkata	Mumbai-Chennai
Air express	3,939	4,168	3,939	3,850
Surface express	1,000	1,038	1,558	912
Cost difference (air/surface) (x)	3.9	4.0	3.7	4.2

Source: BlueDart Express, BOBCAPS Research

Increasing B2B share to continue to translate into higher weight for shipments

- **Increase in average weight of shipments:** Rising digitisation of communication and the advent of e-banking have led to a decline in B2C express document transportation. On the other hand, various time-sensitive non-document cargoes are being shipped through the express route. With the increase in non-document express shipments, the average weight of cargo is also on the rise – currently, cargo higher than 5kg accounts for 20%+ of total volumes.

The incremental cost for bulkier shipments is higher for air versus surface transport, as highlighted in the table below. Hence, surface distribution is expected to be incrementally preferred for heavy shipments.

FIG 32 – SHARE OF NON-DOCUMENTS IN EXPRESS SHIPMENTS RISING STEADILY

Source: Deloitte, CRISIL Research, BOBCAPS Research

FIG 33 – COST OF AIR EXPRESS RISES MORE THAN SURFACE FOR HIGHER WEIGHT SHIPMENTS

(Rs)	Delhi-Mumbai			
	10kg	15kg	20kg	25kg
Air express	3,939	5,038	6,137	7,236
Surface express	1,000	1,220	1,440	1,660
Cost difference (air/surface) (x)	3.9	4.1	4.3	4.4

Source: Blue Dart Express, BOBCAPS Research

- **Improved road infrastructure:** Robust investments by central and state governments to upgrade road networks (such as the Bharatmala programme) are expected to improve India's road infrastructure. This should help surface express players by reducing turnaround time and optimising costs.
- **Onset of GST:** Abolition of inter-state check-posts under the GST regime has already improved average truck speed, with scope for further improvement, as indicated by industry sources. This should help further lower the turnaround time for surface express players.

Global express industry fairly consolidated with FedEx, UPS dominating US, and DHL, TNT driving Europe

Advantage large players with a national presence

In our view, express players with a wide network will gain prominence over regional players as the industry matures and moves towards a more oligopolistic structure from being somewhat fragmented at present. Our hypothesis is also corroborated by the structure of the global express industry, where four players – FedEx and UPS based in the US, and DHL and TNT in Europe – dominate the industry.

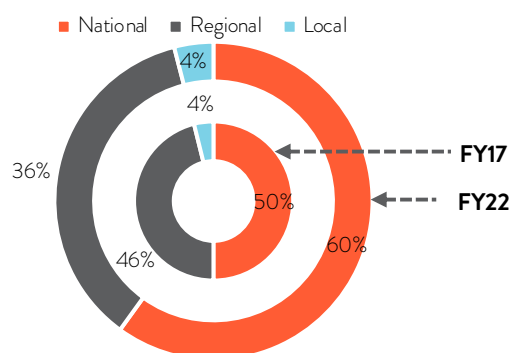
We believe the following factors will hasten the shift in customer preference towards large, national players –

- **Wider network:** Coverage of a wide number of pin codes is critical for express players as it enables them to service various customer requirements. Large players have pan-India networks of sorting centres and branches which serves as a key advantage over regional players.
- **Better infrastructure:** With deeper pockets, large players are able to invest more on technology and other network infrastructure vis-à-vis smaller players, enabling them to provide an array of value-added services to customers – these include flexible billing, storage facilities and non-standard item shipment.
- **Higher reliability:** A large scale of operations supported by technology enables national players to provide reliable services to customers. While these players are already preferred by large customers with established operations, SMEs are also increasingly choosing their services over smaller express players, as per industry sources.

Expect share of national players to grow to 60% from 50% currently

Owing to these advantages, we foresee some degree of consolidation in the express industry which would see large players growing larger and outpacing overall surface industry growth of 18-20%. Our interactions with industry participants suggest that the share of national players could rise to ~60% over the next few years, from ~50% currently.

FIG 34 – NATIONAL PLAYERS TO GARNER FURTHER MARKET SHARE IN EXPRESS INDUSTRY



Source: FSCSL DRHP, Industry, BOBCAPS Research

Poised for accelerated growth

Aided by structural tailwinds, we expect the express industry to grow at a robust CAGR of ~15% over the next five years, with surface express projected to grow at a faster 18-20% CAGR. The following factors are likely to catalyse this growth –

Expanding basket of products requiring express delivery

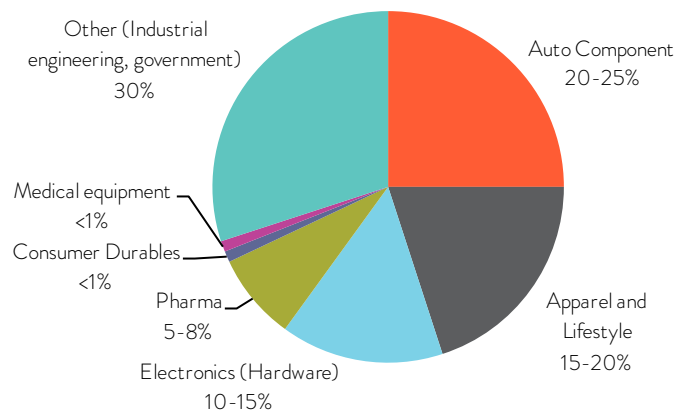
As mentioned, the express industry has witnessed a paradigm shift in terms of the nature of shipments transported over the past 15 years. The rise of digital communication has lowered the need for document delivery, while newer product categories have emerged owing to a focus on inventory management by manufacturers and their quest for lower lead times to ensure product availability.

Pharma and auto verticals to grow at 15-18% CAGR

Consequently, a wide array of industries uses express delivery services today – these include auto components, consumer durables, apparel and lifestyles, engineering, medical equipment, pharmaceuticals and electronics. Of these, the consumer and apparel industries are well penetrated, and hence expected to grow at a relatively slower pace of 10-12%; pharma and auto are pegged to grow at 15-18% CAGR over the next five years.

FIG 35 – AUTO, LIFESTYLE PRODUCTS, ELECTRONICS MAJOR CATEGORIES

Customer-wise segmentation of domestic B2B express industry



Source: Deloitte, Industry, BOBCAPS Research

FIG 36 – EXPRESS SERVICE USED FOR CRUCIAL BUSINESS CASES

Industry	Products requiring express service
Auto Components	Delivery of spare parts to remote locations and/or on an urgent basis; safe transport of products such as batteries and lubricants which require special handling due to their inflammable nature
Apparel and Lifestyle	Shipment of products from warehouse to distributors; large players use express services to meet the surge in demand during festive seasons, while smaller players use it for almost all long-haul transport
Electronics	Delivery of spare parts required for aftersales service of PCs, laptops, mobiles and printers
Medical Equipment	Urgent shipment of critical medical equipment at hospitals and nursing centres
Pharmaceuticals	Shipment of critical clinical-trial products and time- & temperature-sensitive medication requiring safe handling; also to meet seasonal demand surges

Source: Deloitte, Industry, BOBCAPS Research

SMEs entering the fray

While large players were always the mainstay of the express industry, small and medium enterprises are now increasingly opting for express services. Steady demand traction expected from the SME sector augurs well for the express business.

Boom in e-retail business
















Rapid growth in the e-retail industry with the advent of players such as Flipkart, Amazon has boosted the B2C express delivery industry in India over the past few years. Time-sensitive order delivery is a key success factor for this industry, which necessitates express distribution services. Going forward, the industry is expected to continue its growth trajectory, leapfrogging at a 25-30% CAGR (as per industry estimates), propelling growth for the B2C express business.

Prefer TCIEXP in the express space

We analyse the relative positioning and financial performance of three leading listed players in India's express segment – Blue Dart Express (BDE), TCI Express (TCIEXP), and Gati Kintetsu Express (Gati-KWE).

- BDE's market positioning score is higher as it has higher market share and vintage
- Reach is comparable due to similar pin-code coverage
- TCIEXP has higher focus on B2B and surface express than peers
- BDE and TCIEXP are better proponents of asset-light models

FIG 37 – COMPETITIVE POSITIONING OF SURFACE EXPRESS PLAYERS

Parameter	BDE	TCIEXP	Gati KWE
Positioning on parameters			
Market position			
Network & reach			
Focus on surface express			
Focus on B2B			
Focus on asset-light model			
Financial parameters (FY16-FY18) (%)			
Revenue CAGR	4.6	15.5	1.2
Avg. EBITDA margin	13.8	9.0	7.0
PAT CAGR	(14.3)	43.2	(16.3)
Gross asset turnover (x)	5.3	7.5	2.9
Avg. ROCE	33.1	36.3	12.7
Avg. ROE	40.6	27.1	10.2

Source: Company, Industry, BOBCAPS Research

 Very Strong
  Strong
  Moderate
  Weak
  Very weak

In our view, TCIEXP is the best positioned among these leading players to ride the industry tailwinds. Our argument is based on (1) TCIEXP's strong positioning in the surface express industry, which is benefitting from a shift away from air express, and (2) its focus on the B2B segment, where we project a growth uptick. The company has an infrastructure network comparable with other players, but a better financial performance marked by higher revenue and PAT growth over the past two years.

Although margins remain on the lower side, this is due to its asset-light strategy, and the impact on return ratios is negated by a higher asset turnover. We expect TCIEXP to grow much faster than the overall industry and to augment market share.

DFC is a potential game changer for the Indian container rail industry

Container rail – the time is ripe

Container rail, the perennial laggard of the Indian logistics industry, appears to be finally entering into a sustained upturn. After being beset by external challenges over the past few decades, we foresee substantial market share gains for rail over road as large swathes of the >3,000km high-speed, high-capacity dedicated freight corridor (DFC) come online over the next few years.

With the DFC expected to augment rail economics and enable time-sensitive cargo delivery, we estimate that EXIM container volumes for the Indian Railways (IR) can gallop ahead at an 18-20% CAGR (tonne-km terms) for the first 2-3 years post DFC-commissioning. Nearer-term, we expect the Rewari (Haryana)-Palanpur (Gujarat) stretch to be completed on schedule in Sep'19, connecting Gujarat ports Mundra and Pipavav to the freight corridor, in turn boosting the rail coefficient at these ports. With unmatched terminal network and a vast rolling stock, we expect CCRI to be the prime beneficiary of this new era for container rail industry.

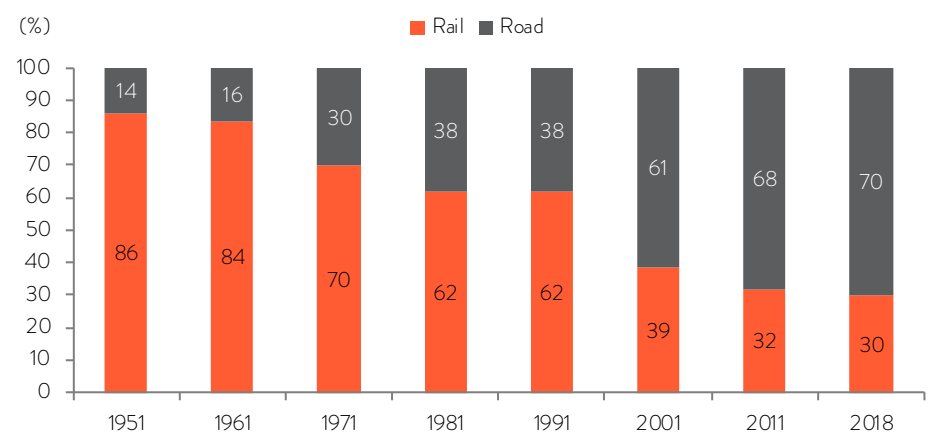
A tale of missed opportunities

IR's share in freight transport has nosedived to ~30% in 2018, from 90%+ in 1951

IR has been largely unable to capitalise on India's growth story so far. The premier mode for freight and passenger transport in the 1950s, IR has persistently lost market share to road – IR's freight share has plunged from 90%+ in 1951 to ~30% in 2018. Despite favourable economics comprising lower cost per tkm and less carbon emissions, rail transport has lost favour with customers due myriad factors.

Some of these are (1) an inability to provide transit-time guarantees, (2) inadequate infrastructure, (3) capacity constraints – both terminal and wagon, (4) cross subsidisation of passenger fare by freight, and (5) lack of flexible pricing. Market share loss to roads is even more unfortunate considering that a large part of the cargo carried in India is bulk in nature and transported over a long haul – factors which ought to favour rail over road.

FIG 38 – RAIL'S MARKET SHARE HAS SHRUNK TO ~30%



Source: Government publications, Indian Railways, BOBCAPS Research

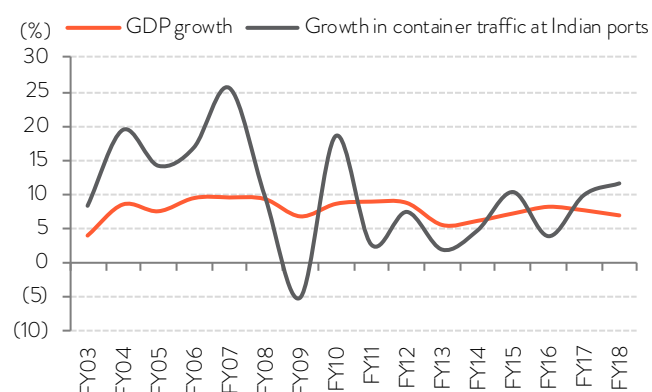
Slower growth in container traffic impacted the segment

India's container growth to GDP ratio fell to <1x over FY08-FY16 from 2.2x over FY03-FY07

Growth in container traffic in India, measured as the total container traffic handled by gateway ports (major plus non-major), has tapered off since the global economic recession in FY09. The container traffic-to-GDP growth ratio has moderated from 2.2x over FY03-FY07 to a mere 0.7x over FY08-FY16.

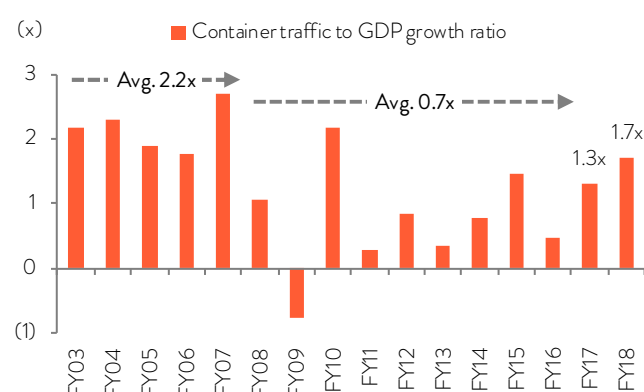
Multiple factors contributed to this including slower global trade, sluggish domestic industrial activity, and a higher base of container traffic. Given that EXIM movement is key for container train operators (CTO), this slowdown has restricted growth in the industry. While we note that the ratio has improved to 1.3x/1.7x in FY17/FY18, a tough global trade environment may pose growth challenges.

FIG 39 – CONTAINER TRAFFIC MOVES IN TANDEM WITH GDP...



Source: Central Statistics Organisation, Drewry Maritime Research, BOBCAPS Research

FIG 40 – ...BUT CONTAINER TRAFFIC-TO-GDP RATIO HAS MODERATED IN RECENT YEARS

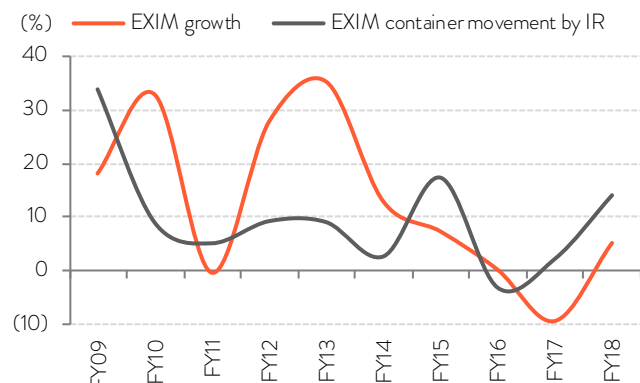


Source: Central Statistics Organisation, Drewry Maritime Research, BOBCAPS Research

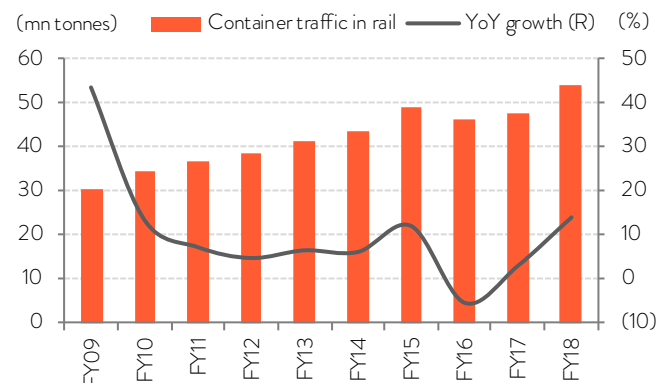
EXIM accounts for ~80% of total container volumes in India

EXIM growth dictates container rail growth

Vibrant export-import trade is vital to rail container traffic growth as EXIM movement forms ~80% of the total volumes for IR and CTOs. Past trends exhibit a healthy correlation between the two, while the intermittent divergences stem from market share gains/losses to road. Going ahead, we expect EXIM growth to continue to catalyse the growth in container rail.

FIG 41 – EXIM AND RAIL CONTAINER TRAFFIC HAVE A HEALTHY CORRELATION


Source: Indian Railways, Ministry of Commerce, BOBCAPS Research

FIG 42 – CONTAINER TRAFFIC IN RAIL HAS GROWN AT 6.7% CAGR


Source: Indian Railways, BOBCAPS Research

DFC mainly aimed at easing capacity constraints at major freight routes

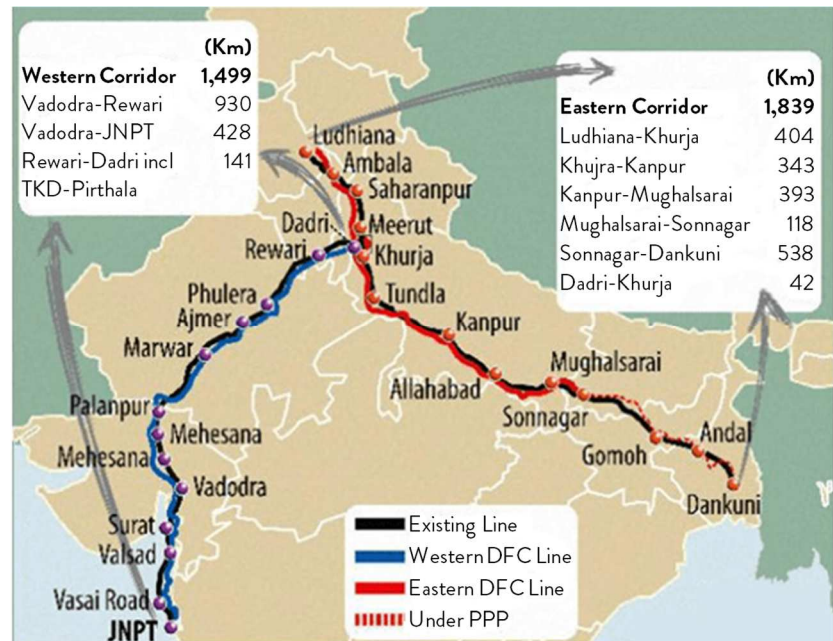
DFC – panacea to many ailments

After grappling with creaking, inadequate infrastructure for many years, IR embarked on a high-speed, high-capacity DFC linking the Golden Quadrilateral (four key metros of Delhi, Mumbai, Chennai and Kolkata) and its two diagonal routes – Mumbai-Kolkata and Delhi-Chennai, by setting up the Dedicated Freight Corridor Corporation of India Ltd in 2006.

These routes form the backbone of the railways – the 10,122km of land area that stretches between these cities accounts for 60% of total freight rail traffic and 50%+ of total passenger rail traffic. Due to high traffic density, IR has been operating at capacity utilisation rates of 100-115% on these routes. The DFC, therefore, is aimed at resolving infrastructure bottlenecks.

WDFC to drive container traffic growth; EDFC to cater to bulk movement

In the first phase, two stretches of the DFC have been envisaged – (1) the Western DFC (WDFC) comprising ~1,500km of double-line, electrified track between Dadri in Uttar Pradesh and JNPT in Mumbai, via Vadodara-Sanand-Palanpur-Phulera-Rewari; and (2) the Eastern DFC (EDFC) comprising ~1,840km between Ludhiana in Punjab and Dankuni in West Bengal. A bulk of the WDFC traffic is expected to comprise containers from manufacturing centres to the western ports, while EDFC is likely to cater largely to bulk commodities.

FIG 43 – WDFC AND EDFC SNAPSHOT

Source: DFCCIL, BOBCAPS Research

WDFC – closer to reality

**Rewari-Palanpur stretch
scheduled to be commissioned
by H2FY20**

After several time overruns, commissioning of the WDFC is finally on the horizon. Two intermediate stretches, viz. Ateli-Phulera and Rewari-Ateli, totaling ~300km have been commissioned in recent months. Execution has picked up pace as project award on the WDFC is largely complete and construction appears to be on track along most stretches, apart from JNPT to Palanpur.

Based on the current progress, we expect the Rewari-Palanpur stretch to be completed by the scheduled Sep'19 date, enabling Gujarat ports Mundra and Pipavav to be connected to the WDFC at Palanpur and Mehsana. This will translate into a higher rail coefficient at these ports (currently at ~25%/~68% of container traffic for Mundra/Pipavav), benefitting container volumes.

However, the stretch between Palanpur and Vadodara is still only a third of the way complete, while progress on Vadodara to JNPT is even lower. We thus anticipate significant delays in full commissioning of the WDFC (Dadri to JNPT) and expect benefits to flow only from FY21-FY23.

FIG 44 – TIMELINE AND STATUS OF THE WDFC

Stretch	Length (km)	Status of land acquisition (%)	Physical progress (%)	Financial progress (%)	Targeted commissioning date	Status
Ateli-Phulera	190	100.0	100	100.0	Aug-18	Commissioned
Rewari-Marwar	432	99.9	Civil – 83 System – 47	74.5	Dec-18	Trial runs completed
Marwar-Palanpur	207				Sep-18	On track
Palanpur-Vadodara	308	99.0	34	23.0	2020	Unlikely to be commissioned before FY22
Vadodara-Sachin	313	99.5	Civil – 27 System – 19	17.3	2020	Unlikely to be commissioned before FY22
Sachin-Vaitarna		92.8	23	11.0		
Vaitarna-JNPT	117	89.2	11	6.0	Jan-21	Unlikely to be commissioned before H2FY22

Source: DFCCIL, BOBCAPS Research

Multi-fold benefits beckon

DFC commissioning is likely to benefit CTOs in four key ways, in our view –

- **Substantial market share gains** – Owing to dedicated lines for freight rails (allowing for transit time guarantees) and better economics, rail is slated to gain share from road. We discuss this in greater detail below.
- **Higher cargo double-stacking** – Better line infrastructure will enable movement of rakes with higher load-carrying capacity (of 13,000tonnes from 5,000tonnes currently) on the DFC. This will facilitate double-stacking of cargo on the entire DFC route, which is currently possible only for select routes, translating into better operating margins for CTOs.
- **Stable lead distances:** IR's lead distances have been falling for the past few years due to the proliferation of consumption centres and market share gains by Mundra port from JNPT. Total lead distance has fallen to 879km in 11MFY19 from 1,119km in FY14. With WDFC aiding hinterland connectivity with JNPT by rail, lead distances are expected to stabilise post DFC-commissioning.
- **Efficiency gains:** Additional efficiency gains are likely to include faster speeds (average speed to be 2-3x of the current ~25km/hour; station spacing to be ~40km from ~7km now) and better service quality to clients.

Rail's competitiveness vs. road to improve drastically

Better competitiveness to fuel 18-20% CAGR in container rail traffic during initial years of DFC commissioning

In the past, rail transporters have lost volumes to road operators even for high lead distances of ~700km+ despite having better economics (lower cost per tonne-km), as they could not guarantee timely delivery of goods. We expect the DFC to bolster rail's competitive positioning vis-à-vis road as (1) efficiency gains enhance rail economics and lower the viable distance from ~700km at present, expanding the product basket for rail; and (2) dedicated lines for freight rails would enable CTOs to offer transit time assurance to customers.

As a result, we expect a large shift in container traffic from road to rail. The quantum of the volume shift, however, is hard to assess. Some estimates peg an increase in rail's share to ~40% of total freight from 28-30% at present, while others expect an incremental 100mn tonnes to be carried by rail. Dedicated Freight Corridor Corp's (DFCCIL) business plan envisages an increase in rail's share in port-bound container traffic to 35-40% within a few years from 20%-odd at present. We believe that for the first 2-3 years, EXIM container volumes for IR can gallop at 18-20% CAGR, in tonne-kilometre terms.

FIG 45 – DFC WILL ENHANCE RAIL'S COMPETITIVENESS VS. ROAD ON MOST FACTORS

Issues that weaken rail's competitiveness vs. road	DFC's expected impact	Our rationale
Unpredictability of rail schedule	Positive	<ul style="list-style-type: none"> Historically, freight trains in India share the track with passenger trains. With a higher focus placed on service quality of the latter, there are often delays in freight train schedules. Hence, CTOs today are unable to provide transit time assurances to customers. With an exclusive rail track for freight trains under the DFC regime, schedules for container rails will be far more reliable. This should enable CTOs to provide transit time assurances.
Unfavourable economics for short/medium-haul	Positive	<ul style="list-style-type: none"> Rail has lost market share to road for short-/medium-haul distances as the latter's per-tonne-km economics is better than rail. This can be attributed to non-linear haulage charge hikes in rail to compensate for lower passenger rates. With DFC bringing in efficiencies and increasing axle load by ~50%, rail economics are expected to improve even for medium-haul distances, making rail a viable option for more product baskets.
Higher transit time	Positive	<ul style="list-style-type: none"> Slow speed of freight trains results in higher transit time, shifting cargoes to road. Average speed of trains is expected to increase by 2-3x to ~75kmph from ~25kmph at present, leading to lower transit times.
Inadequate terminal infrastructure	Positive	<ul style="list-style-type: none"> Lack of proper infrastructure at freight terminals has hindered effective loading/unloading of cargo in the past. DFC entails significant investments in rail ICDs/terminals. CCRI has been at the forefront of setting up these terminals. This is likely to address the infrastructure constraints.
Capacity constraints	Positive	<ul style="list-style-type: none"> In the past, rail freight has been impacted by capacity constraints – e.g. lack of adequate rakes during peak time and a congested network.

Issues that weaken rail's competitiveness vs. road	DFC's expected impact	Our rationale
		<ul style="list-style-type: none"> CCRI is investing heavily on DFC-compliant rolling stock, including several new rakes which should allay the capacity concerns for container freight. Congestion is also unlikely to be an issue under DFC.
Lack of first-/last-mile connectivity	No impact	<ul style="list-style-type: none"> Rail does not provide first-/last-mile connectivity which will remain a disadvantage vs. road transport. Although IR has recently tested the idea of using RoadRailers (wagons with wheels enabling them to run on roads), large-scale adoption is still some time away.
No flexible pricing	No impact	<ul style="list-style-type: none"> Unlike road operators, rail does not provide flexible pricing to customers. This is likely to remain a disadvantage vs. roads.

Source: Industry sources, BOBCAPS Research

Valuation methodology

We have valued the logistics companies in our coverage universe using the relative valuation method (forward P/E and forward EV/EBITDA). Our target multiples are arrived at based on (1) fundamental prospects of the companies, including growth prospects, sustainable competitive advantages, return ratios, and balance sheet strength; (2) historic trading multiples; and (3) relevant peer multiples.

Aligning with our sector and company preference themes, we have assigned premium multiples (25-30x) to 3PL and express companies – MLL, FSCSL and TCIEXP – vis-à-vis cyclical companies (TRPC, AGLL) owing to better earnings growth and return ratio expectations for the former. Despite being a cyclical company, we have assigned a premium multiple of 25x to CCRI, factoring in the option valuation emanating from the DFC.

To capture the long-term growth prospects of fast-growing companies – MLL, FSCSL, TCIEXP – we have also undertaken discounted cash flow (DCF) valuations, which support the target multiples assigned to them.

FIG 46 – OUR TARGET MULTIPLES FACTOR IN FUTURE PROSPECTS

FY19-FY21E	Revenue CAGR (%)	EBITDA CAGR (%)	Earnings CAGR (%)	Avg. ROE (%)	Avg. ROIC (%)	Avg. debt-EBITDA (x)	Target P/E multiple (x)	Upside (%)
AGLL	12.8	16.3	15.5	11.0	13.2	0.9	11.0	15.8
CCRI	13.4	17.4	4.5	11.7	13.6	-	25.0	1.1
FSCSL	27.5	31.1	27.4	18.2	23.0	1.1	25.0	23.3
MLL	13.7	25.3	27.7	22.9	42.5	0.1	30.0	25.4
TCIEXP	17.4	23.6	24.7	30.4	43.8	0.2	30.0	18.3
TRPC	12.8	16.8	15.8	18.0	12.8	1.7	14.0*	25.6

Source: BOBCAPS Research | *Implied multiple; valued on EV/EBITDA

Glossary of abbreviations

3PL: Third-Party Logistics	IR: Indian Railways
AGLL: Allcargo Logistics	LTL: Less-than-Truck Load
CCRI: Container Corporation of India	MLL/MAHLOG: Mahindra Logistics
CFS: Container Freight Station	MMLP: Multi-Modal Logistics Park
DFC: Dedicated Freight Corridor	MTO: Multi-modal Transport Operations
FSCSL: Future Supply Chain Solutions	NVOCC: Non-Vessel Operating Common Carrier
FTL: Full Truck Load	TCIEXP: TCI Express
GST: Goods and Services Tax	TEU: Twenty Foot Equivalent
ICD: Inland Container Depot	TRPC: Transport Corporation of India



Companies

BUY

TP: Rs 625 | ▲ 25%

MAHINDRA LOGISTICS

Logistics

14 March 2019

One for the long haul – initiate with BUY

Discernible competitive advantages and conducive industry dynamics provide an apt backdrop for Mahindra Logistics (MLL) to consolidate its apex positioning in the Indian 3PL space. Sticky clientele, large anchor customers, and a focus on fast-growing industry segments should usher in a multi-year growth phase, while rising warehousing share is likely to drive a structural uptrend in margins. We initiate coverage with BUY and a Mar'20 target price of Rs 625 based on a 30x one-year forward P/E multiple, implying 25% upside from CMP.

Sayan Das Sharma | Rohan Korde

research@bobcaps.in

Key competitive edge: Unparalleled scale (350+ operating locations, 20+ hubs, 15msf of warehousing, 1,500 business associates), a hard-to-emulate asset-light model, and marquee clients (MM, BMW India, L'Oreal) act as strong moats for MLL, translating into best-in-class ROIC. These attributes place the company well to consolidate its pole positioning and capitalise on the robust long-term growth prospects (17-18%) of the third-party logistics (3PL) industry.

Diversifying presence: Apart from MM, the anchor customer with ~60% of the supply chain segment's (SCM) revenue, MLL has also built a sticky non-anchor customer base with marquee names across auto and fast-growing non-auto verticals (consumer, e-commerce). We expect repeat business and new client wins to drive a steady 14% CAGR in the SCM business over FY19-FY21.

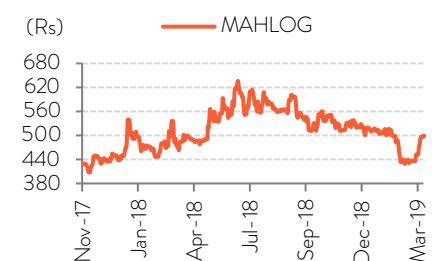
Sustainable margin expansion: An increasing contribution from high-margin warehousing together with cost rationalisation measures is expected to support a structural uptrend in margins. We forecast 80bps EBITDA margin expansion to 4.9% over FY19-FY21, driving a robust 28% CAGR in earnings.

Initiate with BUY: We value MLL at 30x FY21E EPS, yielding a Mar'20 target price of Rs 625 (25% upside). BUY.

Ticker/Price	MAHLOG IN/Rs 499
Market cap	US\$ 510.6mn
Shares o/s	71mn
3M ADV	US\$ 0.2mn
52wk high/low	Rs 544/Rs 418
Promoter/FPI/DII	59%/10%/10%

Source: NSE

STOCK PERFORMANCE



Source: NSE

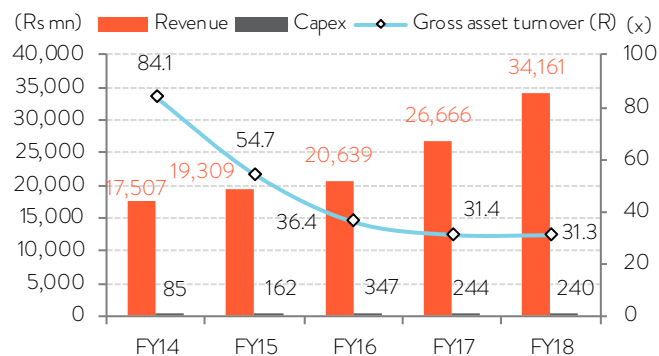
KEY FINANCIALS

Y/E 31 Mar	FY17A	FY18A	FY19E	FY20E	FY21E
Adj. net profit (Rs mn)	456	640	910	1,190	1,483
Adj. EPS (Rs)	6.7	9.0	12.8	16.7	20.8
Adj. EPS growth (%)	11.6	34.1	42.1	30.8	24.7
Adj. ROAE (%)	14.0	16.7	20.2	23.1	25.3
Adj. P/E (x)	74.4	55.4	39.0	29.8	23.9
EV/EBITDA (x)	44.9	29.0	22.1	17.1	13.8

Source: Company, BOBCAPS Research

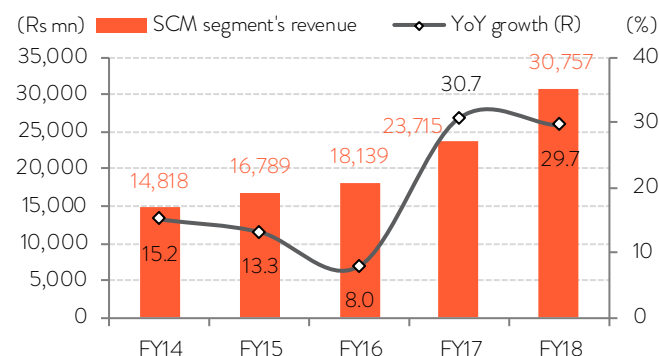
In a nutshell

FIG 1 – MLL HAS SUCCESSFULLY LEVERAGED ASSET-LIGHT MODEL TO ATTAIN SCALE



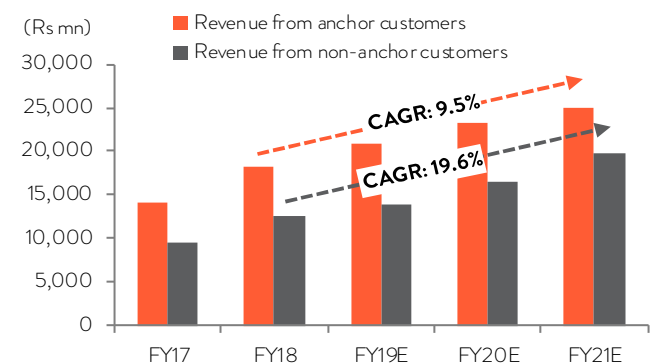
Source: Company, BOBCAPS Research

FIG 2 – NEW CLIENT ADDITION DROVE HEALTHY 20% CAGR IN SCM BUSINESS OVER FY14-FY18



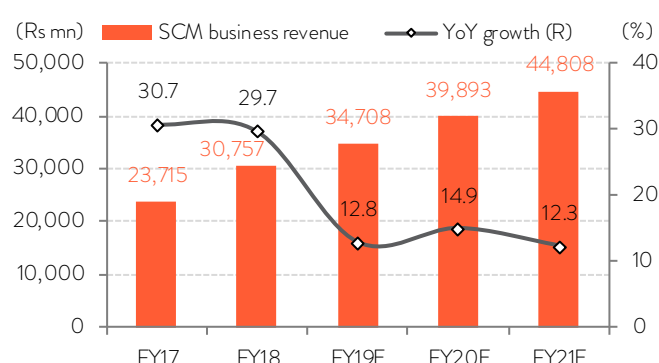
Source: Company, BOBCAPS Research

FIG 3 – NON-ANCHOR CLIENT SEGMENT TO GROW FASTER THAN ANCHOR CUSTOMER...



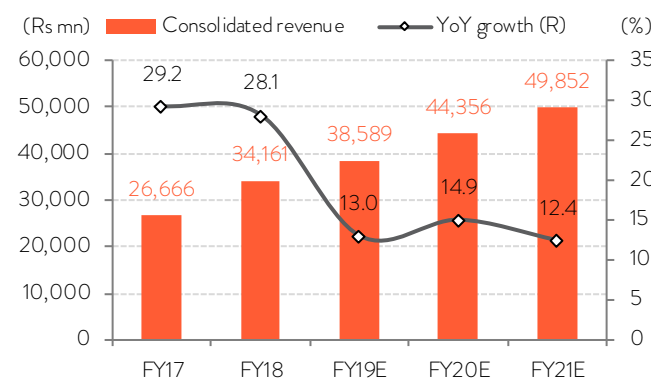
Source: Company, BOBCAPS Research

FIG 4 – ...DRIVING SCM BUSINESS GROWTH AT 13.6% CAGR OVER FY19E-FY21E



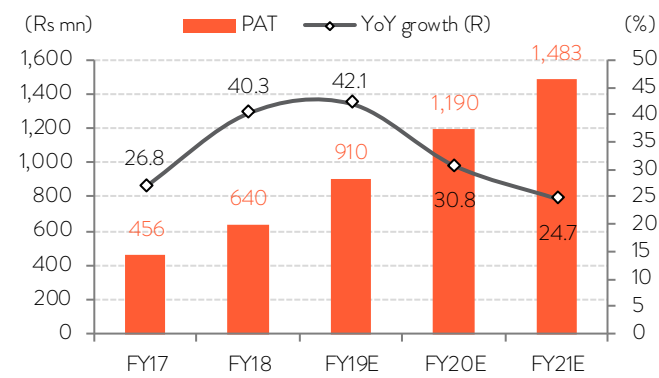
Source: Company, BOBCAPS Research

FIG 5 – CONSOLIDATED REVENUE TO GROW AT 13.7% OVER FY19-FY21



Source: Company, BOBCAPS Research

FIG 6 – PAT PROJECTED TO GROW AT A STRONG 28% CAGR OVER FY19-FY21E



Source: Company, BOBCAPS Research

Investment rationale

Asset-light model drives operational scale

Asset-light focus – vehicles and warehouses leased from network of business partners – helps ramp up scale

Judicious execution of an asset-light business model has enabled MLL to increase its topline with minimal investment in fixed assets. Instead of investing in a fleet of vehicles, the company leverages its wide network of business associates (mostly medium and small fleet operators) to meet vehicle requirements for both its supply chain management (SCM; 90% of FY18 revenue) and people transportation solution (PTS; 10%) businesses. It also hires warehouses on long-term leases rather than purchasing them outright.

We note that MLL has been the one of the best proponents of an asset-light strategy among listed logistics players in India, enabling it to attain a critical scale of operations with limited capital investment and deliver industry-leading gross asset turnover accompanied by best-in-class ROIC.

Large scale of operations acts as competitive moat

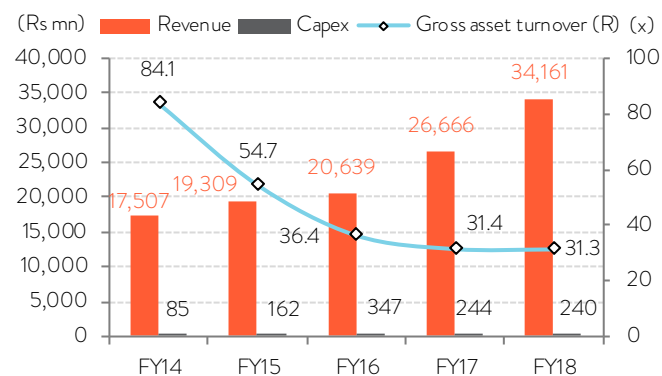
Our industry interactions indicate scale to be a key success factor for 3PL players

Our interactions with market participants indicate that scale is a key success factor for the third-party logistics (3PL) industry in India as it helps drive (1) multi-industry exposure, a prerequisite for garnering expertise in industry-specific supply chain nuances, (2) higher utilisation of warehouses and distribution centres, and (3) higher load per trip for business associates.

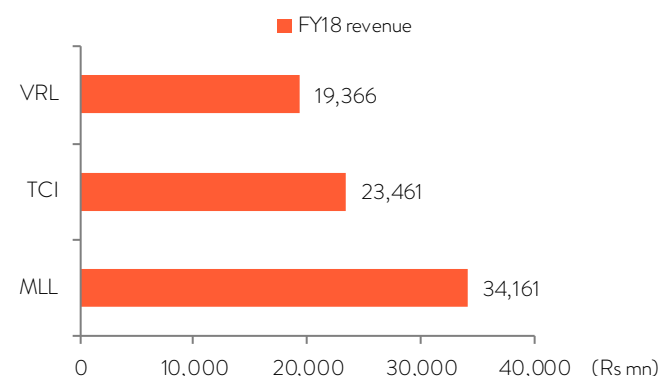
Despite only a decade of existence, MLL has established a vast network comprising 350+ operating locations, 20+ hub locations, 15mn sq ft (msf) of warehousing space, and 1,500 business associates. Leveraging this wide network, the company has been able to organically grow its SCM revenue at a strong 19% CAGR over FY13-FY18. This growth was also augmented by the large operations of its anchor customer – parent company Mahindra & Mahindra (MM).

MLL has larger scale than longstanding incumbents

Notably, within a short time MLL has attained higher scale than two leading road freight players of a much older vintage – its FY18 consolidated revenue of Rs 34.2bn was 1.5x that of Transport Corporation of India and 1.8x that of VRL Logistics. Moreover, it has established a large non-anchor customer base, yielding revenue of Rs 12.6bn in FY18 vs. Rs 2.4bn for Future Supply Chain Solutions (FSCSL), another leading 3PL player. We believe new entrants as well as industry incumbents will find it difficult to replicate this large scale of operations, which thus forms a key competitive moat for MLL.

FIG 7 – ASSET-LIGHT MODEL ENABLED REVENUE GROWTH WITH LIMITED CAPITAL INVESTMENTS


Source: Company, BOBCAPS Research

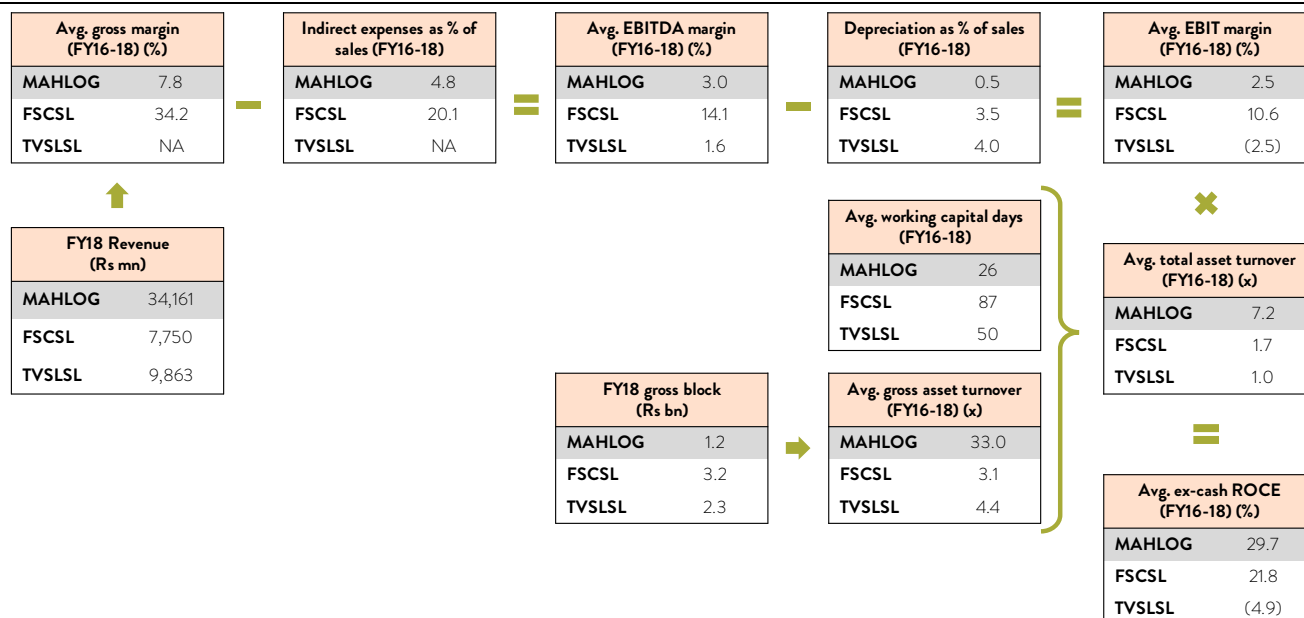
FIG 8 – MLL HAS ACHIEVED LARGER SCALE THAN MORE SEASONED ROAD FREIGHT TRANSPORTERS


Source: Company, BOBCAPS Research

Best-in-class ROIC testament to successful asset-light strategy

Average ROCE of 29.7% over FY16-FY18; higher than peers

MLL has the highest ROIC among the leading 3PL players in India, at 29.7% on average over FY16-FY18 vs. 21.8% for FSCSL. Owing to its asset-light model, MLL's average margin profile has been lower vis-à-vis its peers – FSCSL and TVSLSL, which is more than compensated for by the higher fixed asset and working capital turnovers. The below diagram displays the source of ROIC divergence for the three leading 3PL companies.

FIG 9 – BEST-IN-CLASS ASSET EFFICIENCY TRANSLATES INTO SUPERIOR ROIC FOR MLL


Source: Company, BOBCAPS Research; FY15-FY17 standalone financials for TVSLSL

Integrated offerings address end-to-end supply chain requirements of clients

Offers integrated transport, warehousing, value-added solutions in SCM business; people transportation in PTS

MLL offers end-to-end, customised supply chain solutions to customers. Its SCM business encompasses primary and secondary transportation, warehousing & value-added services, and in-factory logistics. The PTS business offers shared mobility services to companies. A wide service basket provides cross-selling opportunities and helps the company capture incremental wallet share in key customer accounts. Focused investments in technology further complement MLL's core offerings.

FIG 10 – MLL'S INTEGRATED SERVICE OFFERINGS ENCOMPASS THE ENTIRE SUPPLY CHAIN



Source: Company

Technology complements core offerings

Strong transport management systems in place

MLL has developed two transport management systems (TMS): (1) Mahindra Integrated Logistics Execution System (MILES) – used for transportation of automobiles, and (2) Mycargo – a multi-industry technology solution. For its PTS business, MLL has a multi-purpose system, used for automating route planning and allocation, tracking of trips, safety and billing & collection.

According to management, leveraging technology has enabled it to lower transit time and provide customised solutions. To fortify its technological capabilities, the company acquired a strategic stake in Transtech Technologies (also known as ShipX), a technology solution provider for the transportation industry, in Q3FY19.

Diversified, sticky non-anchor client base

Diversified client base; strong credentials pave way for future client wins

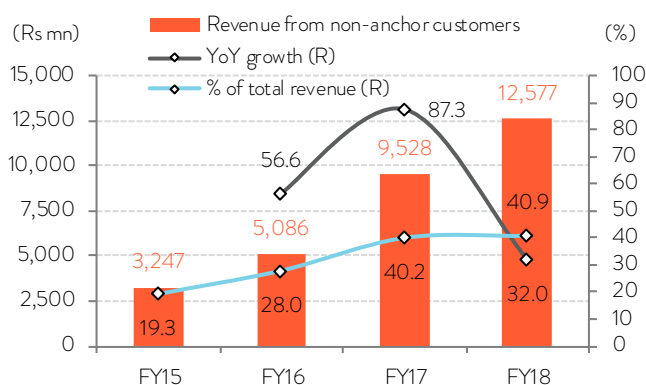
Non-anchor customers accounted for 41% of SCM revenue in FY18

MLL has successfully expanded its non-anchor customer base over the past few years, reducing its dependence on anchor customer MM. Driven by new client additions, its non-anchor customer segment has clocked a strong 57% CAGR over FY15-FY18 vs. 10% CAGR for the anchor business, increasing its share in SCM revenue to 41% from 19%.

475+ clients include marquee names across auto, engineering, consumer goods, bulk, and e-commerce

As of 9MFY19, MLL has 475+ non-anchor clients, including marquee names in its focus verticals – Mercedes-Benz India, BMW India, Volkswagen, Ashok Leyland, and Bosch in automotive (a noteworthy feat given that some of these are competitors of its parent); 3M, Thermax and Siemens in capital goods/engineering; HUL and L'Oréal in consumer goods; JSW Group in bulk transport; and Amazon and Flipkart in e-commerce. A strong track record of servicing established players across vertical would pave the way for more client wins ahead, in our view.

FIG 11 – NON-ANCHOR CUSTOMER SEGMENT HAS GROWN AT A ROBUST PACE



Source: Company, BOBCAPS Research

FIG 12 – CLIENTELE INCLUDES MARQUEE NAMES ACROSS INDUSTRIES



Source: Company, BOBCAPS Research

Integration with client operations leads to high switching costs – reflected in only 4% churn rate

Deep-seated relationship with clients ensures repeat business

MLL's services are deeply ingrained in its clients' operational ecosystems. Its engagement typically starts at the CXO level, which translates into deep relationships. The company also has its own employees present in various client manufacturing plants who are well-versed with the respective manufacturing processes. This relationship translates into high switching costs for customers, reflected in low churn (~4% attrition in non-anchor customer base in FY18).

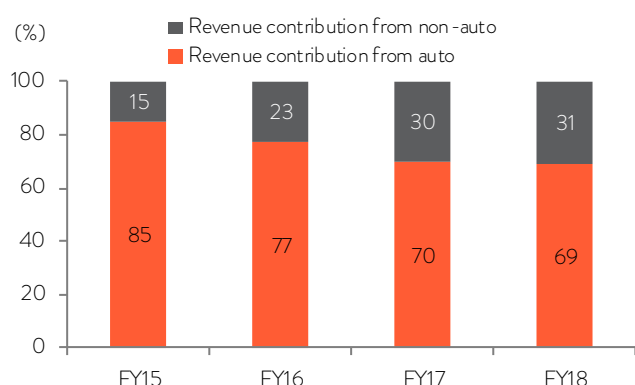
MLL thus receives repeat business from customers; and also increases its wallet share in key client accounts – the top 20 customers accounted for 66% of the non-Mahindra SCM segment, up from 56.5% in FY15.

Increasing presence in fast-growing industry verticals

Fast growth in non-auto vertical has reduced share of auto to 69% in FY18 from 85% in FY15

Over the past few years, MLL has stepped up its focus on non-auto verticals such as consumer, e-commerce and pharma, acquiring a sizeable client base. These industries have low 3PL penetration, indicating abundant growth potential. Client diversification has also enabled the company to reduce its exposure to the cyclical auto industry to 69% of total SCM revenues in FY18 from 85% in FY15. Established credentials in these fast-growing industry verticals place the company favourably to capitalise on the market potential.

FIG 13 – RAMP-UP IN NON-AUTO VERTICALS HAS REDUCED INDUSTRY CONCENTRATION RISK



Source: Company, BOBCAPS Research

FIG 14 – 3PL MARKET IN NON-AUTO VERTICALS TO GROW AT A FASTER PACE

(Rs bn)	3PL market size		CAGR (%)
	FY18	FY21E	
Auto & auto comps	290-300	450-470	15-16
E-commerce	80-85	180-185	30-35
Consumer durables and FMCG	25-27	50-52	20-25
Organised retail	35-40	75-80	25-30

Source: Company, BOBCAPS Research, CRISIL Research

After 3.8% CAGR in H1FY19, non-anchor client growth has risen to 15.5% in Q3FY19

Non-anchor SCM segment to rebound in driven by client adds

Following a stellar run over FY15-FY18, non-anchor customers in the SCM segment slowed to 3.8% YoY in H1FY19. This is attributable to (1) lower transportation spend by a large customer owing to a change in its business mix, (2) discontinuation of some low-profit transportation routes, and (3) a trucker strike in July leading to lower manufacturing days for the in-factory logistics business. Additionally, new customer addition was muted in Q1FY19 as companies were cautious after the implementation of GST.

However, with new client accounts stabilising, growth improved to 15.5% in Q3FY19. We expect growth trajectory to pick up in coming quarters, driven by addition of new marquee names in clientele.

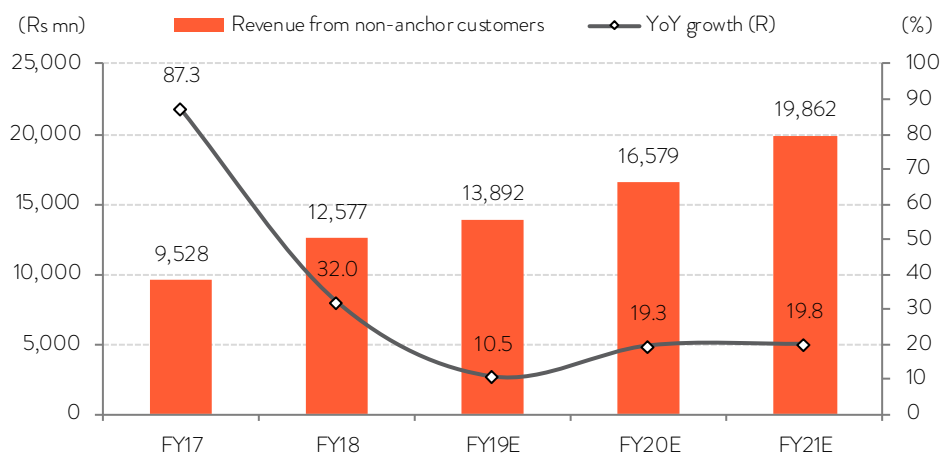
FIG 15 – CLIENT ADDITIONS IN 9MFY19

Client	
▪ Aftermarket distribution for MNC OEM	▪ Warehousing and sorting centre for a large B2C e-commerce company
▪ Leading Indian non-ferrous metal company	▪ Leading lubricant and marketing player
▪ Indian textile company	▪ Prominent engineering and industrial MNC
▪ Large MNC luxury passenger vehicle OEM	▪ Global construction equipment manufacturer
▪ European MNC engaged in power, heavy electricals, and automation	▪ Global telecom equipment manufacturer
▪ Global aviation component manufacturer	▪ Leading lubricant manufacturer and marketing company in India
▪ Diversified conglomerate manufacturing aviation and locomotive components	▪ Multi-national beverage group

Source: Company, BOBCAPS Research

Expect 20% CAGR in non-anchor client segment over FY19-FY21

Beyond FY19, the non-anchor customer segment's growth is also expected to be bolstered by (1) an increase in wallet share of existing customers, (2) new client addition hastened by GST, and (3) a focus on non-auto verticals with high growth potential. We factor in a healthy 20% CAGR in this segment over FY19-FY21.

FIG 16 – NON-ANCHOR CUSTOMER SEGMENT EXPECTED TO GROW AT A HEALTHY 20% CAGR OVER FY19-FY21


Source: Company, BOBCAPS Research

Anchor business growth to largely depend on MM

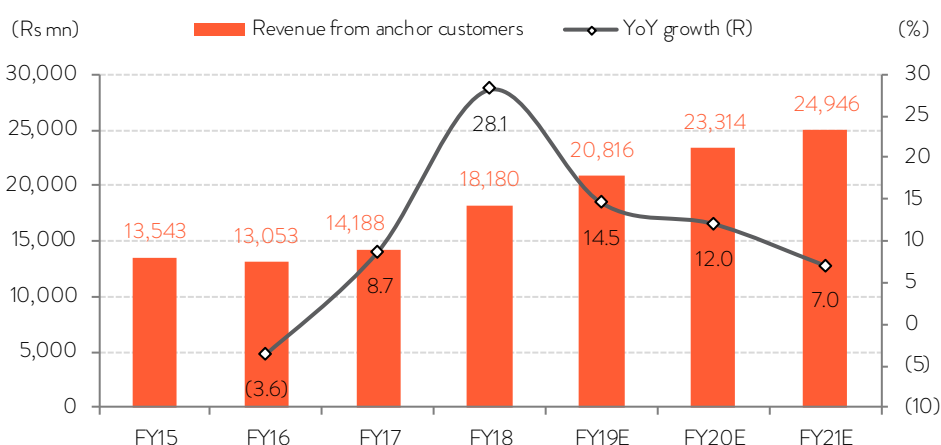
MLL's anchor business primarily comprises the automotive and farm equipment divisions of MM, with some other Mahindra Group entities forming a small portion of revenues. Although the non-anchor customer segment has grown at a faster pace over the past few years, MM remains the mainstay for the company with a 59% contribution to SCM revenue.

Currently, MLL's share in MM's total logistics spend stands at 90%+ (of auto and farm equipment division), indicating limited headroom for further penetration. Hence, we expect this segment to grow largely in line with MM's automotive and farm equipment business. The company also has the potential to extend its services to other Mahindra Group entities, which can add to this growth.

We expect MM's standalone revenues/volumes to clock an 7%/6% CAGR over FY19-FY21. MLL's SCM anchor customer segment growth is accordingly forecast to post a slightly higher 9.5% CAGR during the same period.

Project 9.5% CAGR in anchor customer revenue over FY19-FY21

FIG 17 – ANCHOR CUSTOMER SEGMENT EXPECTED TO POST 9.5% CAGR OVER FY19-FY21



Source: Company, BOBCAPS Research

Focus on warehousing, value-added services to propel margins

Warehousing has 15-20% gross margin vs. 6-8% in transportation

Management's focus on the high-margin warehousing and value-added services (kitting, bundling, packaging) segment is expected to catalyse margin expansion. As of 9MFY19, warehousing accounts for 26% of MLL's non-anchor SCM customer revenue and 13% to its total SCM revenue. MLL is increasingly focusing on this segment considering higher margins (15-20% gross margin vs. 6-8% for transportation, as per our industry interactions) and GST-led growth opportunities for the industry. Incremental client addition is also focused on warehousing - majority of the new client contracts have a warehousing component, as per the management - which indicates progress on this plan.

Expect 32% CAGR in warehousing revenue over FY19-FY21

Concurrently, we expect revenue contribution from warehousing and value-added segment to gradually ramp up. We expect warehousing segment to grow at ~32% CAGR over FY19-FY21. Increasing share of this high-margin segment is expected to provide a fillip to EBITDA margins as well.

Has 120+ clients across 12 cities in the PTS division

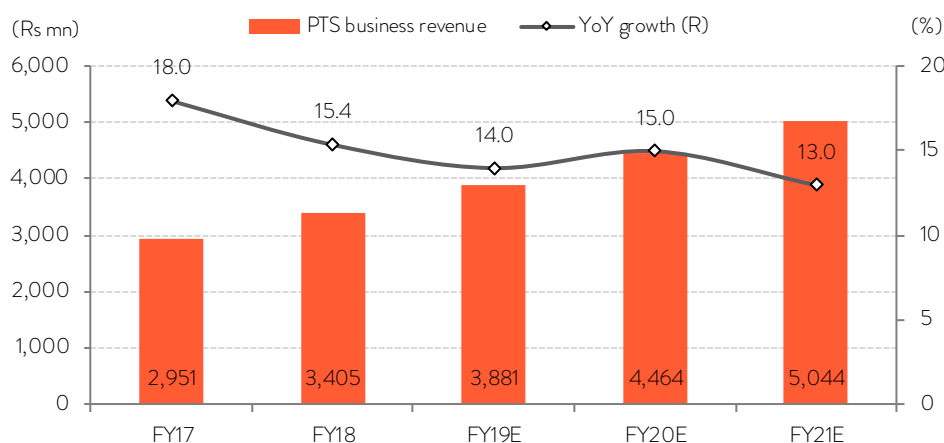
Expect PTS segment to grow faster than industry growth of 9-10%

PTS business – expect 14% CAGR over FY19-FY21

MLL offers shared mobility services to corporates through a fleet of hired vehicles. As of 9MFY19, it caters to 120+ clients in 12 cities across various industries such as IT, ITeS, BPO, financial services, consulting, and manufacturing. The company follows an asset-light model for this business as well, where it leases the required fleet from a pool of business associates. MLL leverages technology to optimise route planning, ensure safety and security measures, and achieve optimum vehicle utilisation.

Industry participants expect the PTS industry to register a 9-10% CAGR over FY19-FY21. Given the highly unorganised, fragmented nature of the industry and MLL's endeavour to provide reliable services to client at competitive pricing, we expect the company's PTS business to grow faster than the industry, at a 14% CAGR over this period.

FIG 18 – PTS BUSINESS TO GROW AT 14% CAGR OVER FY19-FY21



Source: Company, BOBCAPS Research

Foray into freight forwarding can open up growth avenues

As a natural extension of its core offerings, MLL forayed into the freight forwarding business (mostly LCL or less-than-container load consolidation) by acquiring a majority stake in Lords Freight (India) Pvt Ltd in FY15. The segment accounted for 5% of total consolidated revenue in FY18. The company plans to aggressively scale up this business to 10-15% of revenues, bringing its mix closer to that of large global 3PL players (20-25% of total revenues).

To this end, MLL is eyeing acquisition opportunities in the global freight forwarding space. Given the large and fragmented nature of the LCL consolidation industry, the company can potentially gain incremental market share here, opening up newer growth avenues.

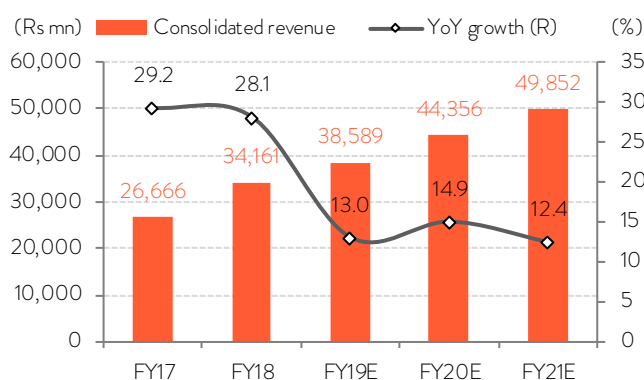
Financial review

Revenue projected to grow at 13.7% CAGR over FY19-FY21

Expect faster growth in non-anchor customer segment (20% CAGR) than anchor customer (9.5% CAGR)

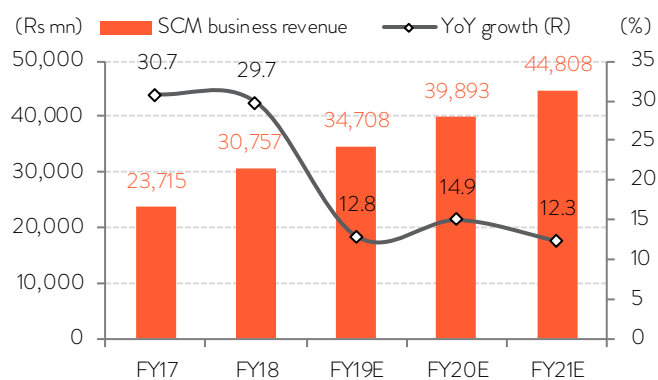
We expect MLL's consolidated revenue to grow at a 13.7% CAGR over FY19-FY21 to Rs 49.9bn. This is lower than the 28.7% CAGR posted by the company over FY16-FY18, as we foresee headwinds to anchor customer MM's volumes in FY21 owing to a potential slowdown in the automotive industry. Among segments, SCM is projected to grow at a 13.6% CAGR, while PTS is expected to record a 14.0% CAGR. Within SCM, the non-Mahindra customer segment is likely to outperform at 20% CAGR vs. 9.5% for the anchor customer segment.

FIG 19 – CONSOL. REVENUE TO LOG 13.7% CAGR



Source: Company, BOBCAPS Research

FIG 20 – SCM SEGMENT TO GROW AT SIMILAR PACE



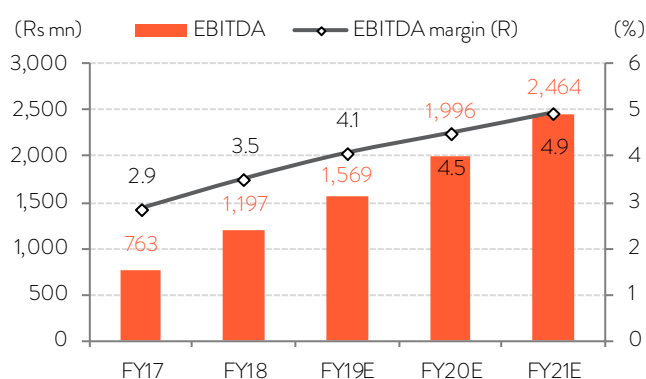
Source: Company, BOBCAPS Research

Improving business mix to fuel margin expansion

Expect 80bps margin expansion over FY19-FY21

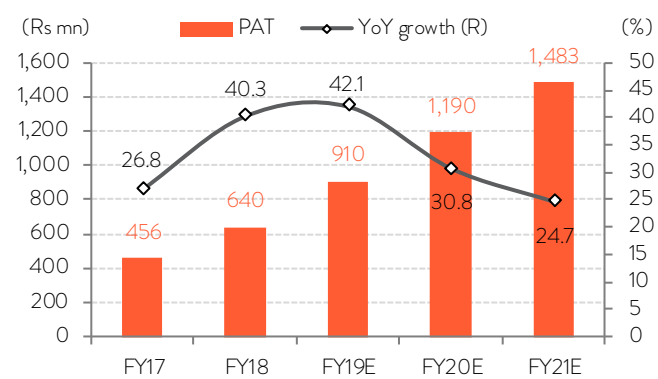
A rising share of warehousing and value-added services along with cost optimisation measures undertaken by the company are likely to augment margin expansion. We expect MLL's EBITDA margin to expand 80bps over FY19-FY21 to 4.9%. Healthy margin expansion is likely to drive sturdy earnings growth. During FY19-FY21, we expect PAT to grow at a 28% CAGR to Rs 1.5bn from Rs 910mn.

FIG 21 – EBITDA MARGIN POISED TO EXPAND



Source: Company, BOBCAPS Research

FIG 22 – 28% PAT CAGR EXPECTED OVER FY19-FY21



Source: Company, BOBCAPS Research

Strong return ratios, FCFF generation on the cards

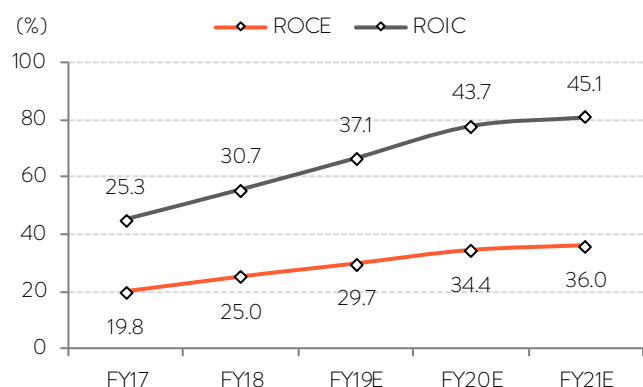
Aided by margin expansion and benefits from its asset-light model, MLL is likely to further strengthen its already impressive pre-tax ROCE/ROIC profile. We expect ROCE/ROIC to improve to 36%/45% in FY21 from 30%/37% in FY19.

Free cash flow generation has been adversely impacted over the past two years by a delay in income tax refund from the income tax authorities. Net income tax assets increased to Rs 868 mn in FY18 from Rs 276 mn in FY16, which led to negative FCF of Rs 463 mn in FY17 and a meagre FCF of Rs 13 mn in FY18.

Lower applicable TDS rates, income tax refund to drive healthy cash flows

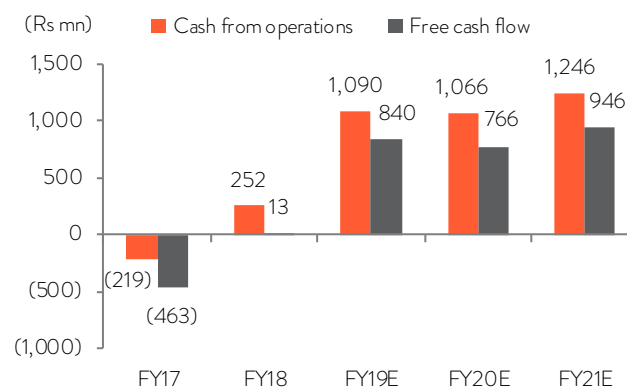
Two positive developments have occurred in YTD FY19 on this front – 1) MLL filed an application with Income Tax authorities and was able to reduce the tax deducted at source (TDS) incidence applicable to its businesses – to 1.0% from 2% in transportation, and to 2.5% from 10% in warehousing, rental, and interest income; and 2) received refund of Rs 177 mn along with interest of Rs 19 mn. Management expects further recovery in the coming quarters. Based on this, we expect income tax assets to reduce from FY19 onwards. This, coupled with stable working capital cycle and absence of any major capex, should translate into healthy FCFF generation. We estimate Rs 2.5 bn of FCFF to be generated over FY19-21, ~70% of aggregate PAT, creating room for increased dividend pay-outs.

FIG 23 – ROCE AND ROIC TO IMPROVE FURTHER



Source: Company, BOBCAPS Research

FIG 24 – STRONG FCF GENERATION LIKELY



Source: Company, BOBCAPS Research

Valuation methodology

**Initiate coverage with BUY
and a Mar'20 TP of Rs 625**

Since its public listing in Q3FY17, MLL has traded at ~35x one-year forward P/E multiple. Prima-facie, this multiple may appear high, especially compared with median one-year forward trading multiple of ~18-20x for the sector. We believe MLL merits this premium valuation owing to (1) its apex positioning in India's 3PL industry, (2) robust long-term sector prospects, (3) well-established anchor customer and sticky non-anchor clientele, and (4) superior return ratios. Further, we expect the company to continue to command premium multiples, as the company's earnings trajectory is expected to remain strong at 28% CAGR during FY19-FY21.

**We assign a target multiple of
30x to FY21E EPS**

We have valued the company using the P/E methodology, assigning a multiple of 30x on the FY21E EPS of Rs 20.8 to arrive at a Mar'20 target price of Rs 625. Initiate with BUY.

FIG 25 – KEY VALUATION ASSUMPTIONS

Rs per share	
FY21E EPS	20.8
P/E multiple applied (x)	30
Target price	625
Upside from CMP (%)	25.1

Source: BOBCAPS Research

To substantiate the multiple assigned to the company, we have also done a discounted cash flow valuation. Our DCF factors in cash flow projections till FY30, well beyond the explicit projection period of FY21.

We expect MLL to capitalise on the large market opportunity and maintain a strong growth trajectory over the next 5-6 years. Thus, we have factored in a healthy sales/EBITDA/earnings CAGR of 14%/24%/26% over FY19-FY24. With industry growth maturing gradually, we expect the sales/EBITDA/earnings CAGR to moderate to 9%/13%/14% over FY24-FY30. We have discounted the cash flows over FY21-FY30 with a 12.4% weighted average cost of capital, and assumed a 6% terminal growth rate to arrive at a DCF based valuation of Rs 652 per share. This implies a one-year forward P/E multiple of 31x.

FIG 26 – KEY DCF ASSUMPTIONS
Growth assumptions during the projection period – FY19-FY30E (%)

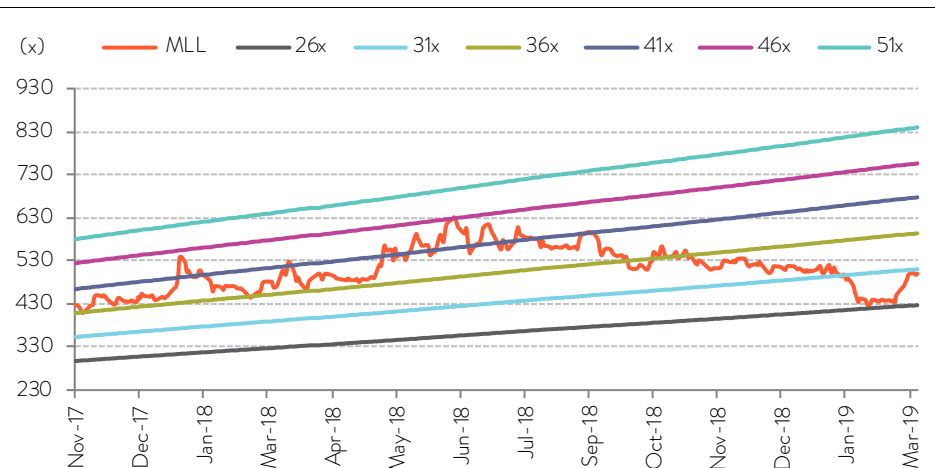
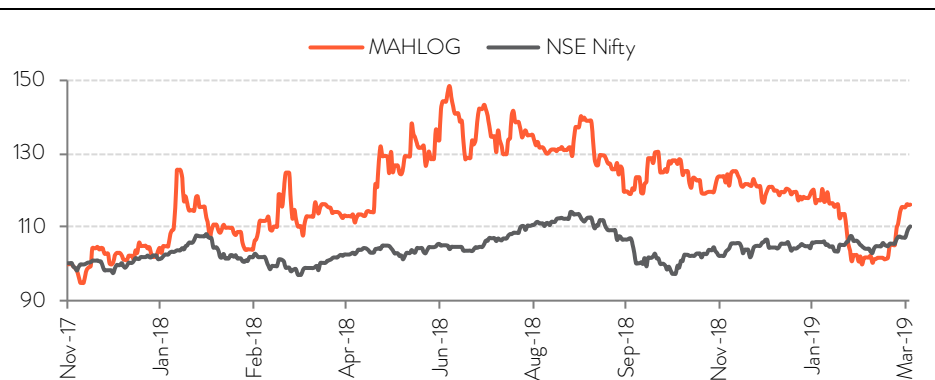
Sales CAGR	11.6
EBITDA CAGR	17.7
Earnings CAGR	19.3

Other assumptions (%)

First year of discounting	FY21
Cost of equity	12.5
WACC	12.4
Terminal growth rate	6.0
Terminal value contribution	62.0

Fair value per share (Rs)	652
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Source: Company, BOBCAPS Research

FIG 27 – ONE-YEAR FORWARD P/E BAND

FIG 28 – RELATIVE STOCK PERFORMANCE


Key risks

- **Slowdown in anchor customer's business:** As MLL continues to derive a majority of its revenue from parent company MM, any slowdown in the latter's operations can be detrimental to revenues and profitability.
- **High client attrition:** While we note that customer churn rates have been low in the past, retention of key client accounts remains critical for sustainability of the business.
- **Prolonged downturn in auto industry:** Despite diversifying its revenue mix to include non-auto industries, auto remains the mainstay for MLL owing to its large anchor customer. This exposes the company's operations to inherent cyclicity of the automotive industry. Any prolonged downturn in the auto industry can thus pose a threat to our estimates.
- **Shortage of vehicle:** MLL meets its vehicle requirements through a network of ~1,500 business associates. While we note that it has not faced any shortage in vehicle availability in the past, any deterioration in relation with/attrition of business associates may lead to a vehicle shortage, impacting operating performance.

Management overview

FIG 29 – KEY MANAGEMENT PERSONNEL

Name	Brief profile
Mr. Pirojshaw Sarkari Chief Executive Officer	Mr. Pirojshaw Sarkari is the Chief Executive Officer of MLL. He graduated from the University of Mumbai in 1987 with a Bachelor's Degree in Commerce and he is a qualified Chartered Accountant. Prior to joining MLL, he has served as a managing director in UPS Jetair Express Private Limited and UPS International Incorporated, Philippines. He joined MLL on April 1, 2010.
Mr. Sushil Rathi Chief Operating Officer	Mr. Sushil Rathi is the Chief Operating Officer MLL, currently managing the SCM business. He graduated in 1983 with a Bachelor's degree in Mechanical Engineering from Maulana Azad College of Technology, Bhopal University and a Post-Graduate Diploma in Industrial Engineering from National Institute for Training Industrial Engineering. Prior to joining MLL, he has worked with Anantara Solutions Private Limited, the Premier Automobiles Limited and Satyam Computer Services Limited. He joined MLL on March 21, 2011.
Mr. Yogesh Patel Chief Financial Officer	Mr. Yogesh Patel has over 20 years of experience across the Finance function. A Chartered Accountant and a Bachelor in Commerce from Kolkata University, Yogesh was associated with HCG as CFO, E&Y - as a Director-Finance; Wipro as Vice President – Finance and with IBM as Country Finance Planning Manager, amongst others. He joined MLL on 20 August 2018.
Ms. Rama Malik Vice President, PTS Business	Ms. Rama Malik, is the Vice President – People Transport Solutions of MLL. She holds a Bachelor's degree in Arts from University of Mumbai. She graduated from University of Pune in 1994 with a Master's degree in Business Administration. She has previously worked with Hindustan Unilever (formerly known as International Bestfoods), Kodak India Limited and Writer Relocations, India. She joined MLL on November 2, 2015.
Mr. Kamal Kapoor Vice President Transportation	Mr. Kamal Kapoor, 55 years, is the Vice President - Transportation of MLL. He graduated University of Mumbai in 1986 with a Bachelor's degree in Commerce. He has previously worked with Dangote Industries Limited, Indian Roadways Corporation, Hindustan Zinc Limited, Saurashtra Clearing Agency, Sterlite Industries (India) Limited, VSK Logistics Private Limited and Reliance Industries Limited. He joined MLL on March 1, 2016.
Mr. Prasanna Pahade Chief Strategy Officer	Mr. Prasanna Pahade, 43, is the Chief Strategy Officer at MLL and is responsible for strategy, marketing and communications. He graduated from College of Engineering, Pune in 1996 with a Bachelor's Degree in Mechanical Engineering and has a PGDM in Finance and Strategy from IIM Calcutta. Prior to joining MLL he has worked with Tata Strategic Management Group, Voltas Ltd and has co-founded a start-up "Making Champs". He joined MLL on 3rd October 2017.

Source: Company, BOBCAPS Research

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Total revenue	26,666	34,161	38,589	44,356	49,852
EBITDA	763	1,197	1,569	1,996	2,464
EBIT	617	1,000	1,356	1,738	2,158
Net interest income/(expenses)	(35)	(38)	(34)	(26)	(14)
Other income/(expenses)	97	59	81	112	138
Exceptional items	0	0	0	0	0
EBT	678	1,021	1,403	1,824	2,282
Income taxes	(217)	(368)	(484)	(620)	(776)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	(5)	(13)	(9)	(14)	(23)
Reported net profit	456	640	910	1,190	1,483
Adjustments	0	0	0	0	0
Adjusted net profit	456	640	910	1,190	1,483

Balance Sheet

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Accounts payables	3,993	4,863	5,815	6,684	7,512
Other current liabilities	144	205	231	266	299
Provisions	164	180	204	234	263
Debt funds	343	346	296	196	66
Other liabilities	0	0	0	0	0
Equity capital	680	711	711	711	711
Reserves & surplus	2,845	3,554	4,180	4,797	5,564
Shareholders' fund	3,525	4,266	4,892	5,508	6,276
Total liabilities and equities	8,168	9,860	11,438	12,888	14,415
Cash and cash eq.	1,082	1,161	1,599	1,620	1,707
Accounts receivables	4,121	5,200	6,132	7,534	8,878
Inventories	0	0	0	0	0
Other current assets	1,477	1,461	1,651	1,897	2,132
Investments	0	0	0	0	0
Net fixed assets	572	616	658	700	693
CWIP	7	6	0	0	0
Intangible assets	43	43	43	43	43
Deferred tax assets, net	132	141	141	141	141
Other assets	735	1,232	1,214	952	821
Total assets	8,168	9,860	11,438	12,888	14,415

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Net income + Depreciation	602	837	1,123	1,448	1,789
Interest expenses	35	38	34	26	14
Non-cash adjustments	(44)	(9)	0	0	0
Changes in working capital	(812)	(614)	(102)	(453)	(557)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	(219)	252	1,056	1,021	1,246
Capital expenditures	(244)	(240)	(250)	(300)	(300)
Change in investments	0	0	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(244)	(240)	(250)	(300)	(300)
Equities issued/Others	82	31	0	0	0
Debt raised/repaid	42	3	(50)	(100)	(131)
Interest expenses	(35)	(38)	(34)	(26)	(14)
Dividends paid	0	(129)	(274)	(574)	(715)
Other financing cash flows	(60)	197	(9)	0	0
Cash flow from financing	28	66	(367)	(700)	(860)
Changes in cash and cash eq.	(435)	78	438	21	86
Closing cash and cash eq.	1,082	1,161	1,599	1,620	1,707

Per Share

Y/E 31 Mar (Rs)	FY17A	FY18A	FY19E	FY20E	FY21E
Reported EPS	6.7	9.0	12.8	16.7	20.8
Adjusted EPS	6.7	9.0	12.8	16.7	20.8
Dividend per share	0.0	1.5	3.2	6.7	8.3
Book value per share	51.1	59.0	67.9	76.8	87.9

Valuations Ratios

Y/E 31 Mar (x)	FY17A	FY18A	FY19E	FY20E	FY21E
EV/Sales	1.3	1.0	0.9	0.8	0.7
EV/EBITDA	44.9	29.0	22.1	17.1	13.8
Adjusted P/E	74.4	55.4	39.0	29.8	23.9
P/BV	9.8	8.5	7.3	6.5	5.7

DuPont Analysis

Y/E 31 Mar (%)	FY17A	FY18A	FY19E	FY20E	FY21E
Tax burden (Net profit/PBT)	67.3	62.7	64.8	65.2	65.0
Interest burden (PBT/EBIT)	110.0	102.1	103.5	105.0	105.7
EBIT margin (EBIT/Revenue)	2.3	2.9	3.5	3.9	4.3
Asset turnover (Revenue/Avg TA)	7.1	7.8	7.6	7.9	8.0
Leverage (Avg TA/Avg Equity)	1.1	1.1	1.1	1.1	1.1
Adjusted ROAE	14.0	16.7	20.2	23.1	25.3

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY17A	FY18A	FY19E	FY20E	FY21E
YoY growth (%)					
Revenue	29.2	28.1	13.0	14.9	12.4
EBITDA	45.7	57.0	31.1	27.2	23.5
Adjusted EPS	11.6	34.1	42.1	30.8	24.7
Profitability & Return ratios (%)					
EBITDA margin	2.9	3.5	4.1	4.5	4.9
EBIT margin	2.3	2.9	3.5	3.9	4.3
Adjusted profit margin	1.7	1.9	2.4	2.7	3.0
Adjusted ROAE	14.0	16.7	20.2	23.1	25.3
ROCE	17.1	23.6	27.7	31.9	35.8
Working capital days (days)					
Receivables	56	56	58	62	65
Inventory	0	0	0	0	0
Payables	56	54	57	58	58
Ratios (x)					
Gross asset turnover	31.4	31.3	28.9	27.5	26.1
Current ratio	1.6	1.5	1.5	1.6	1.6
Net interest coverage ratio	17.7	26.5	40.2	67.2	157.0
Adjusted debt/equity	(0.2)	(0.2)	(0.3)	(0.3)	(0.3)

Source: Company, BOBCAPS Research

BUY

TP: Rs 780 | ▲ 23%

**FUTURE SUPPLY CHAIN
SOLUTIONS**

| Logistics

| 14 March 2019

Promising future – initiate with BUY

Future Supply Chain Solutions (FSCSL) is among the leading players in India's contract logistics space, where its deep expertise in consumer-oriented supply chain management paired with astute technology investments equips it well to capitalise on the robust 3PL industry prospects (17-18% CAGR). We expect rapidly growing anchor customers (Future Group entities) and a diversified non-anchor clientele to catalyse a strong revenue/earnings CAGR of 28%/27% over FY19-FY21 – initiate coverage with BUY and a Mar'20 target price of Rs 780.

Sayan Das Sharma | Rohan Korde

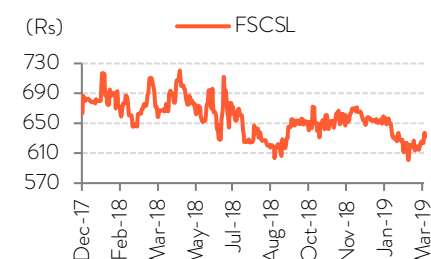
research@bobcaps.in

Differentiated player with a niche focus: Established as a captive supply chain management arm for the Future Group's retail business in 2006, FSCSL has emerged as one of the leading contract logistics players in India with niche expertise in consumer supply chains (90%+ of revenue) – a key competitive moat considering that consumer verticals (durables, retail, fashion) have complex logistic needs and also offer the best growth opportunities in the 3PL space.

Ticker/Price	FSCSL IN/Rs 633
Market cap	US\$ 364.2mn
Shares o/s	40mn
3M ADV	US\$ 0.1mn
52wk high/low	Rs 699/Rs 600
Promoter/FPI/DII	52%/5%/19%

Source: NSE

Rapidly growing anchor clients: Consensus estimates peg revenue growth for FSCSL's three key anchor customers (FRETAIL, FLFL, FCON) at 18% over FY19-FY21. FSCSL is more than doubling warehouse space to 10mn sq ft by FY20 over FY18 to cater to its fast-growing anchor customers (62% of revenue, >40% growth over FY15-FY18) and expanding non-anchor base.

STOCK PERFORMANCE

Source: NSE

Strong growth ahead: Established credentials, a robust client base, technology investments and conducive industry dynamics are forecast to drive a 30%/17% CAGR in FSCSL's contract logistics/express businesses for FY19-FY21. Standalone revenue/EBITDA/earnings are forecast to log a robust 28%/31%/27% CAGR.

Initiate with BUY: We value FSCSL at 25x FY21E P/E, a 20% discount to Mahindra Logistics' 30x P/E multiple, yielding a Mar'20 TP of Rs 780.

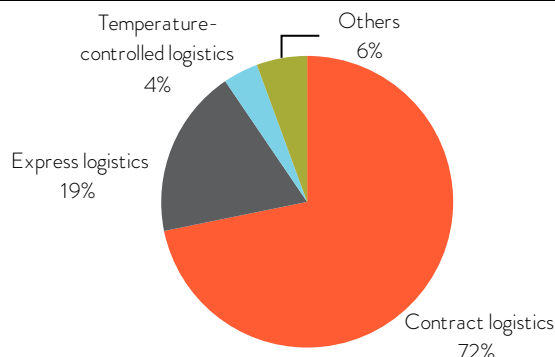
KEY FINANCIALS

Y/E 31 Mar	FY17A	FY18A	FY19E	FY20E	FY21E
Adj. net profit (Rs mn)	458	673	770	900	1,250
Adj. EPS (Rs)	11.7	16.8	19.2	22.5	31.2
Adj. EPS growth (%)	55.6	43.8	14.3	17.0	38.8
Adj. ROAE (%)	16.9	19.0	17.0	17.1	20.4
Adj. P/E (x)	54.1	37.6	32.9	28.2	20.3
EV/EBITDA (x)	35.1	21.2	16.8	13.8	10.5

Source: Company, BOBCAPS Research

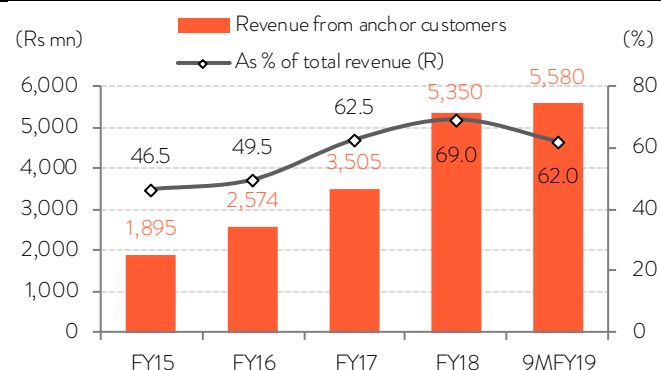
In a nutshell

FIG 1 – CONTRACT LOGISTICS ACCOUNT FOR MAJORITY OF REVENUE, FY18



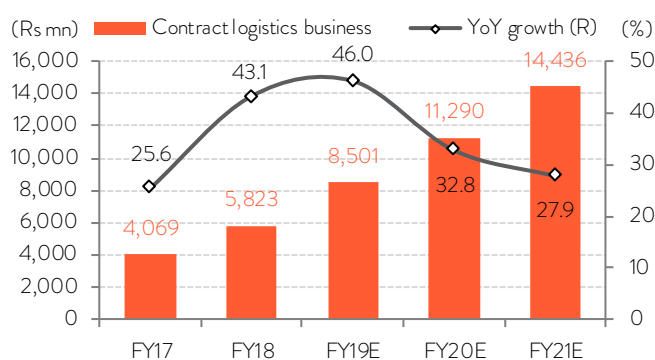
Source: Company, BOBCAPS Research

FIG 2 – FAST GROWING ANCHOR CUSTOMERS HAVE HELPED FSCSL TO SCALE UP



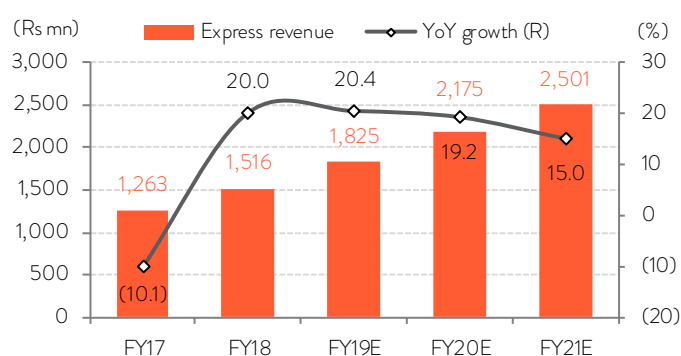
Source: Company, BOBCAPS Research

FIG 3 – CONTRACT LOGISTICS POISED FOR STRONG GROWTH



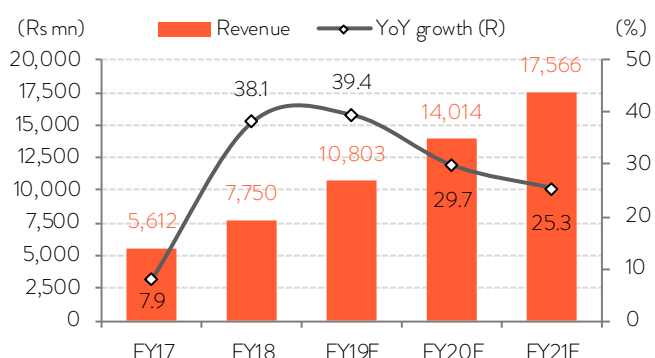
Source: Company, BOBCAPS Research

FIG 4 – EXPRESS SEGMENT TO RIDE ON THE INDUSTRY GROWTH WAVE



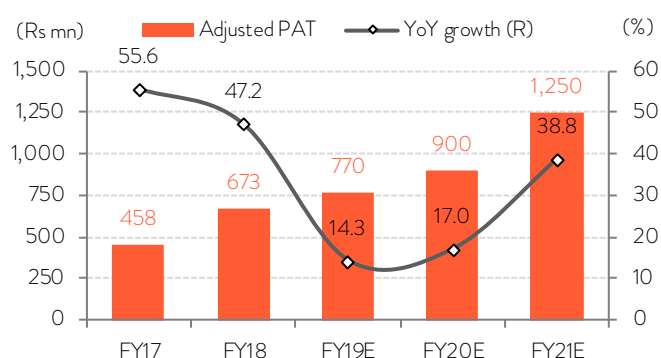
Source: Company, BOBCAPS Research

FIG 5 – STANDALONE REVENUE CAGR OF 28% FORECAST OVER FY19-FY21



Source: Company, BOBCAPS Research

FIG 6 – ADJ. PAT EXPECTED TO GROW AT 27.4% CAGR



Source: Company, BOBCAPS Research

Investment thesis

Differentiated, niche contract logistics player

Established as a captive supply chain management arm for the Future Group in 2006, FSCSL has emerged as one of the leading contract logistics players in India. While retail-focused Future Group entities - Future Retail (FRETAIL), Future Lifestyle (FLFL) and Future Consumer (FCON) - remain the mainstay anchor customers, the company has broadened its client base such that non-anchor customers formed 38% of revenue in 9MFY19. It has also added several value-added services to its repertoire. Deep expertise derived from servicing its anchor clients complemented by astute investments in technology have enabled FSCSL to carve a niche for itself in consumer-oriented supply chain management.

Well-rounded presence across complementary businesses

Contract logistics the largest segment with 69.5% revenue contribution, followed by express (15%) and LMD (12%)

Contract logistics is FSCSL's core business (69.5% of consolidated revenue, including last-mile delivery segment, in 9MFY19), through which it offers warehousing, transportation and value-added services to customers. To cater to the evolving supply chain needs of customers, the company has ventured into complementary businesses – express logistics, where it provides time-definite transportation solutions, and temperature-controlled logistics largely via cold-chain warehousing.

Together the three businesses have internal synergies in the form of: (1) cross-selling to customers which enables it to garner higher wallet share, and (2) similarity in operating models (e.g. warehouses under contract logistics can have cold-chains; express logistics has similarities with the transportation aspect of contract logistics). To further strengthen its delivery solutions, the company acquired Vulcan Express, the last-mile delivery (LMD) arm of Snapdeal, in Feb'18.

FIG 7 – FSCSL BUSINESS SNAPSHOT

Business segment	Services provided	Network/Assets (as of 9MFY19)	% of consolidated revenues (9MFY19)	Gross margin (%)
Contract logistics	<ul style="list-style-type: none"> Integrated warehousing incl. inventory management Transportation & distribution Value-added services (kitting, bundling, promotional packaging, reverse logistics, consolidation) 	<ul style="list-style-type: none"> 91 distribution centres 7.3sq ft of warehousing space 	69.5	34.3
Express logistics	<ul style="list-style-type: none"> Point-to-point transportation Full and part truck-load Time-defined transportation 	<ul style="list-style-type: none"> 11,746 pin codes covered 	14.9	22.1
Last-mile delivery (LMD) and agility solutions	<ul style="list-style-type: none"> Last-mile delivery Value-added services for the e-commerce sector Transportation and warehousing 	<ul style="list-style-type: none"> 0.53mn sq ft 2,200 pin codes covered 	12.3	4.7
Temperature-controlled logistics	<ul style="list-style-type: none"> Cold-chain warehousing Transportation of perishable products 	<ul style="list-style-type: none"> 5 temperature-controlled distribution centres 10,816 pallets 116 owned reefer trucks 	2.8	4.4

Source: Company, BOBCAPS Research

Credible track record in managing consumer-oriented supply chain – a key competitive advantage

Experience working with retail-focused anchor clients lends innate understanding of B2C supply chains

Consumer-oriented businesses have a distinct set of supply chain needs, characterised by a greater importance attached to efficient outbound delivery to various stores, handling of a large number of SKUs, high replenishment cycles, and the need for pilferage management. With over a decade's experience in managing the distribution and warehousing requirements for its anchor customers engaged in the retail and fashion-related businesses, FSCSL has garnered the requisite skills for managing complex consumer-oriented B2C supply chains.

This in turn has enabled it to add various consumer companies to its clientele – consumer-centric industries account for ~90% of current revenue. We believe this acts as a competitive moat for the company and will enable it to capitalise on the robust growth opportunities offered by consumer-focused 3PL verticals.

FIG 8 – FSCSL'S CLIENTELE INCLUDES MARQUEE CONSUMER NAMES

Anchor customers	Non-anchor customer
	

Source: Company, BOBCAPS Research

Case in point: FSCSL helped Future Group entities gain efficiency by revamping distribution model and adopting automation

At the turn of the decade, the Future Group – with ~12 mn sq ft of retail area – was faced with the daunting task of managing a vast pan-India supply chain. Initially, regional warehouses were set up in large consumption hubs – Mumbai, Delhi, Kolkata, Bengaluru – with each serving stores in the vicinity. The warehouses lacked adequate technological support and were controlled locally, with limited integration to the overall supply chain. This led to high inventory holding costs, frequent stock-out at stores, longer transit time and high pilferage costs.

In a quest for greater efficiency, FSCSL revamped the supply chain by setting up a mother distribution hub at Nagpur – a central location with equal proximity to major consumption hubs in India. Vendors from across the country would supply products to the Nagpur warehouse, where it would be stored, consolidated and distributed to retail outlets.

A two-pronged distribution strategy was adopted – (1) ~50 large outlets which accounted for a majority of the Group's business were catered to directly via FTL consignments through the Nagpur distribution centres, and (2) smaller outlets, which required LTL consignments, were divided into clusters. The clusters were served by the Nagpur centre, which in turn, catered to the smaller outlets.

This brought in significant supply chain efficiencies through lower inventory holding cost, lower distribution expenses owing to a higher number of FTL consignments, reduced employee requirement and lower rental expenses. Additionally, by use of warehouse management systems and SAP, the overall supply chain was integrated, enabling less frequent stock-out at stores and lower pilferage.

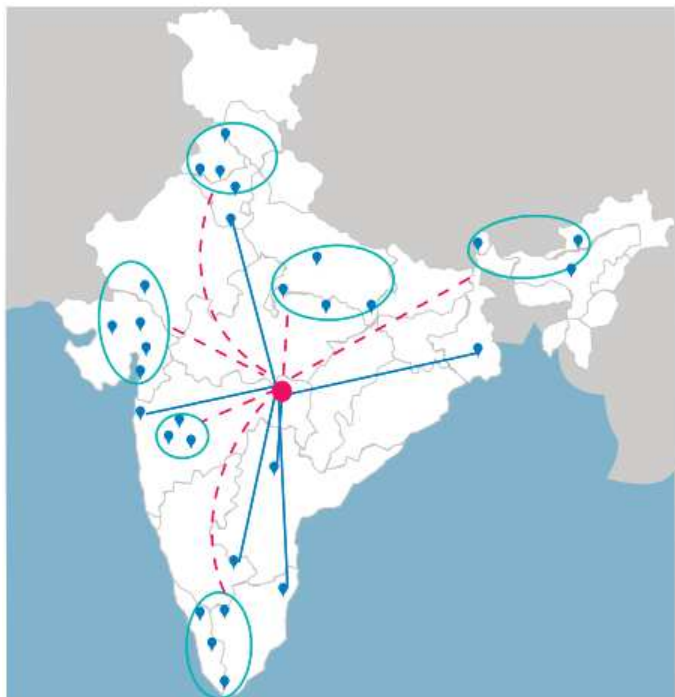
Successful reorganisation of the complex supply chain operations of the Group underpins FSCSL's domain expertise.

FIG 9 – TRADITIONAL DISTRIBUTION MODEL FOLLOWED BY FUTURE GROUP ENTITIES



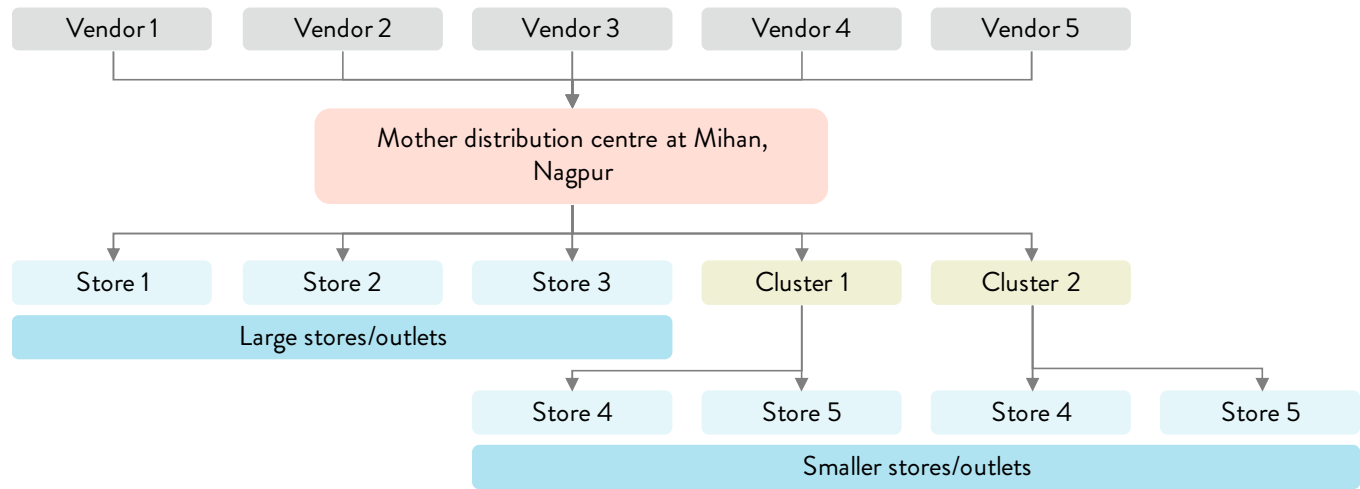
Source: Company, Knight Frank, BOBCAPS Research

FIG 10 – EVOLVED MODEL POST SETTING UP OF NAGPUR DISTRIBUTION CENTRE



Source: Company, Knight Frank, BOBCAPS Research

FIG 11 – NAGPUR CENTRE FOLLOWS A TWO-PRONGED DISTRIBUTION STRATEGY



Source: Company, BOBCAPS Research

Mihan facility boasts a cutting-edge sorting system aimed at efficiency gains

Astute technology investments aid efficiency gains

FSCSL has been one of the early adopters of cutting-edge technology in the 3PL space. We note that technology is a critical cog of consumer-oriented supply chains due to the higher SKU handling, sorting and distribution requirements. FSCSL has maintained steady investments in technology to match its growing scale of operations. This has also enabled the company to provide differentiated services to its customers. Some of its key technological initiatives include –

- **High-speed cross-belt sorter system:** Enables faster sorting (~2,000 cases per hour), translating into higher material handling capacity without additional space addition
- **‘Dynamic put-to-light’ sortation system:** Light-directed sorting system which enables faster sorting speed and inventory throughput
- **Warehouse management system:** Inventory management tool integrated directly with customer’s ERP system, providing visibility on inventory
- **Transport management system:** Provides customers with real-time visibility of the distribution chain through an online portal
- **Vehicle tracking system:** GPS-enabled vehicles allow for real-time tracking of customer goods

Revenue from anchor customers has grown at 41% CAGR over FY15-FY18

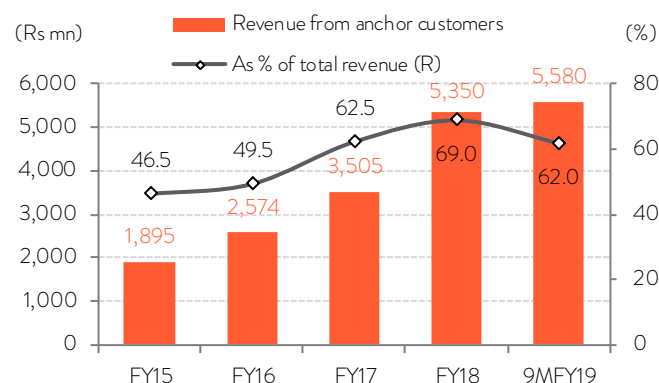
Entrenched presence with rapidly growing anchor customers

FSCSL’s anchor customers – FRETAIL, FCON and FLFL – have aggressively expanded their retail presence over FY15- FY18 through a series of acquisitions and organic expansion programmes (20mn sq ft of retail area vs. ~12 mn sq ft in FY15), translating into a ~60% CAGR in their combined revenue over FY15- FY18 (including inorganic growth). Leveraging on this, FSCSL has increased its presence among anchor customers and posted a robust 41% CAGR in revenue from this client segment. This ramp-up compensated for tepid growth (3% CAGR) witnessed in the non-anchor segment over FY15- FY18.

Anchor customers’ total revenue forecast to grow at 18% CAGR over FY19-FY21, as per consensus estimates

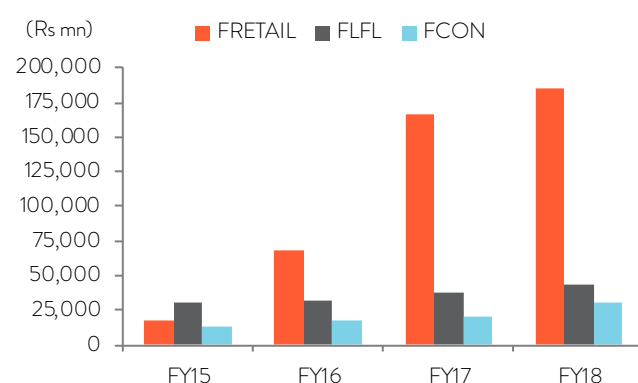
The anchor customers have lofty expansion plans going forward as well, with consensus estimates pegging their aggregate revenue growth at 18% CAGR over FY19- FY21. We view this robust growth potential as a major positive for FSCSL. As per management, FSCSL’s current share in the total logistics spend of Future Group entities stands at ~35-40%, indicating ample headroom for further penetration. We thus expect the anchor customer segment to remain a key growth driver going ahead.

FIG 12 – ANCHOR CUSTOMER SEGMENT HAS POSTED STRONG GROWTH



Source: Company, BOBCAPS Research

FIG 13 – ...DRIVEN BY RAPID GROWTH IN FUTURE GROUP ENTITIES



Source: Company, BOBCAPS Research

Revival in non-anchor client addition

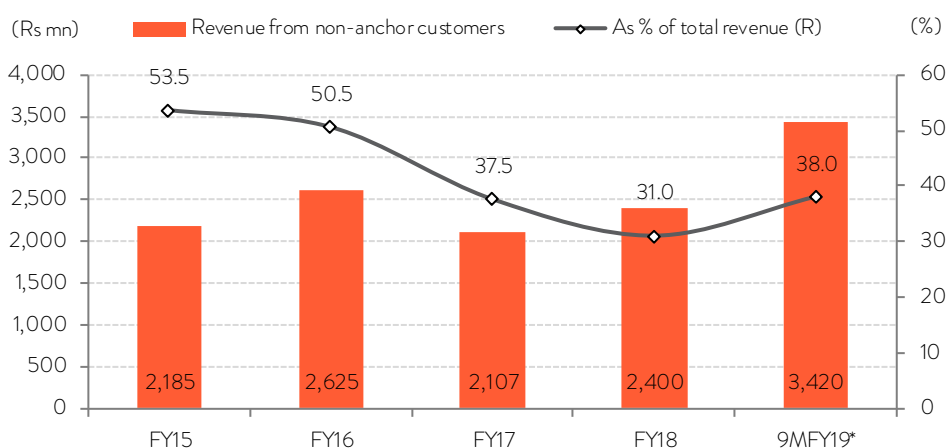
After pruning non-profitable customers over FY16-FY18, FSCSL has added several marquee non-anchor clients to its roster this year, mostly from consumer and related industries. Considering that consumer verticals (durables, retail, fashion) offer the best opportunities in the 3PL space, this traction in non-anchor customer addition augurs well for the company.

Consolidation phase ends; prominent new clients added in FY19

Since starting to focus on non-anchor customers in FY11, FSCSL was able to rapidly ramp up revenue from the segment to Rs 2.6bn in FY16 (50.5% of total). However, owing to payment delays from some customers, receivable days spiked to 155 that year. To improve the cash conversion cycle, FSCSL consciously consolidated its non-anchor customer portfolio and focused on the fast-growing anchor business; which led to a decline in segmental revenue to Rs 2.4bn by FY18. Concurrently, receivable days also moderated to 97 in 9MFY19.

Consciously pruned exposure to non-anchor clients, leading to improved receivable days

FIG 14 – NON-ANCHOR CUSTOMER SEGMENT DECLINED OVER FY16-FY18



Source: Company, BOBCAPS Research

Implementation of GST in Jul'17 has boosted demand for 3PL services. Consequently, FSCSL has been witnessing healthy traction in new client addition in recent quarters. In 9MFY19, the company added prominent names, including Haldirams, Crompton Greaves, Myntra, Voltbek Home Appliances (a Voltas JV), and Helene Curtis (part of Raymond Group), besides a large global fashion brand and a reputed men's casual wear brand.

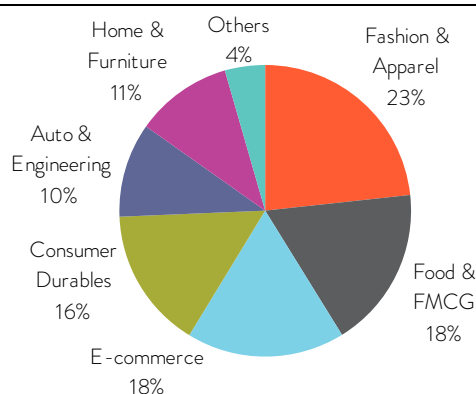
According to the company, the new client additions in 9MFY19 have incremental sales potential of Rs 1.25bn, while the 12-month sales pipeline (potential clients at different stages of negotiation) is pegged at Rs 4bn-5bn. Given the large growth potential of consumer-focused 3PL verticals, we expect the client addition momentum witnessed in 9MFY19 to continue.

Diversified presence across fast-growing consumer space

Consumption-oriented industries account for ~90% of revenue

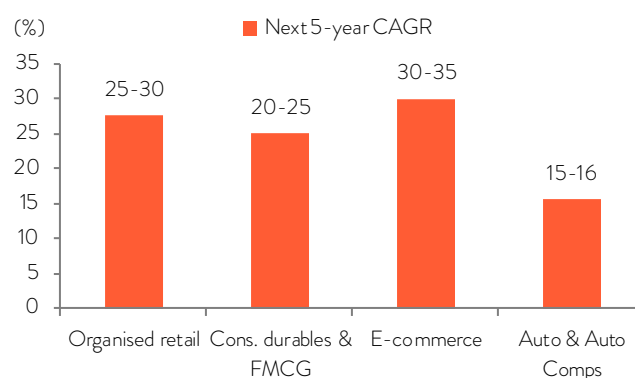
In its non-anchor customer segment, FSCSL has clientele spread across diverse industries such as fashion, food & FMCG, e-commerce, consumer durables and automobiles. We view this multi-industry exposure as a key positive as (1) it imparts industry-specific supply chain management skills to FSCSL, (2) lowers the concentration risk emanating from reliance on anchor customers, and (3) positions the company well to gain further ground in these growing consumer industry verticals.

FIG 15 – FOOTPRINT ACROSS CONSUMER-ORIENTED INDUSTRIES... (H1FY19; NON-ANCHOR SEGMENT)



Source: Company, BOBCAPS Research

FIG 16 – ...WHICH WE ALSO EXPECT WILL BE AMONG THE FASTEST GROWING 3PL VERTICALS



Source: Industry, BOBCAPS Research

GST-led changes, outsourcing trends driving demand for 3PL/contract logistics services

Evolving supply chain needs to fuel next leg of growth

Post GST implementation, the evolving supply chain needs of customers is heralding a new era for 3PL/contract logistics players in India. A shift in focus to efficiency from tax considerations is leading to (1) larger, centralised warehouses, (2) proliferation of hub-and-spoke distribution models, and (3) focus on tech-enabled solutions and inventory management. Manufacturers are expected to increasingly outsource their supply chain requirement and focus on core activities. With expertise

in providing end-to-end supply chain services, including transportation, warehousing, and value-added services, organised 3PL/contract logistics players such as FSCSL stand to gain from these trends.

Resurgent demand in contract logistics space

Over the past few quarters, FSCSL has been witnessing strong traction from clients – it has signed contracts to develop 3.2mn sq ft of built-to-suit warehousing space, expected to be completed by FY20, besides adding multiple clients to its portfolio. To capitalise on the industry opportunities, the management is also meeting with prospective clients to create awareness regarding the benefits of FSCSL's services.

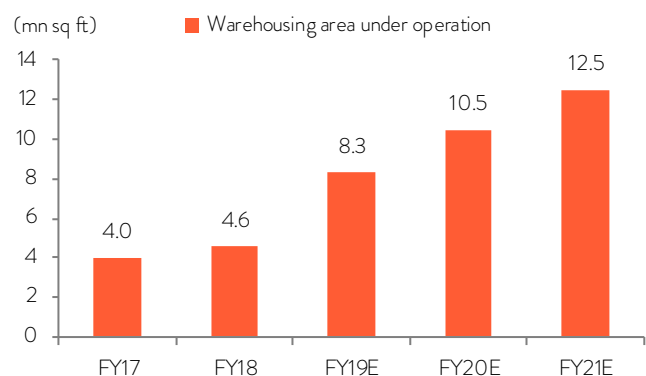
Plans to add ~6mn sq ft of warehousing space in FY19-FY20

Strong client traction for the contract logistics business is also reflected in FSCSL's warehouse expansion plans. The company plans to add 6mn sq ft over FY19-FY20 taking total area under operation to 10.6mn sq ft, more than doubling its capacity from 4.6mn sq ft in FY18. In 9MFY19, it added ~3mn sq ft – including 0.23mn sq ft of Vulcan Express integrated and 0.29mn sq ft managed by FSCSL for a customer – vis-à-vis 0.6mn sq ft added over all of FY18. It plans to roll out a further 3mn sq ft in FY20 (we estimate 2.2mn sq ft to be added). We believe this aggressive warehousing expansion plan will enable the company to cater to the growing demand.

Contract logistics estimated to log strong 30% CAGR over FY19-FY21

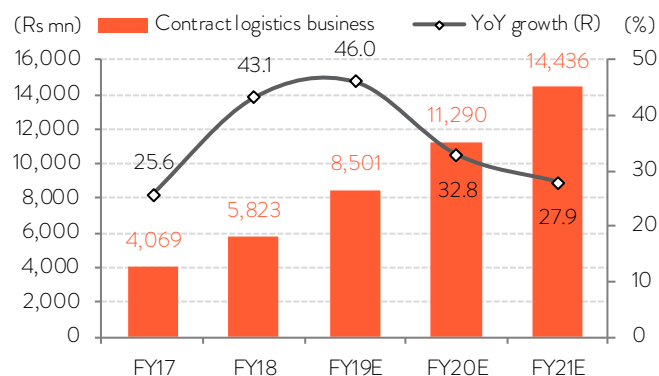
We expect FSCSL's contract logistics business to benefit from (1) strong demand from anchor customers, (2) healthy industry prospects translating into traction in non-anchor client addition, and (3) expertise in handling complex consumer-oriented supply chains. Led by these drivers, the contract logistics business is forecast to grow at a strong 30% CAGR over FY19-FY21, to Rs 14.4bn.

FIG 17 – WAREHOUSING SPACE TO REACH 10MN SQ FT BY FY20E



Source: Company, BOBCAPS Research

FIG 18 – CONTRACT LOGISTICS BUSINESS FORECAST TO GROW AT A STRONG 30% CAGR



Source: Company, BOBCAPS Research

Express segment to ride on industry prospects

**Express reach extends to
~60% of all pin codes in India**

In its express segment, FSCSL provides point-to-point transportation of LTL and FTL cargo in a time-definite manner. It delivers to 11,746 pin codes, ~60% of the total in India, through a fleet of containerised vehicles procured from external vendors. This business caters to both anchor and non-anchor customers. After a sluggish period over FY15-FY17, where revenue growth dropped ~10% each year, growth has rebounded to 20% in FY18 and 22% in 9MFY19.

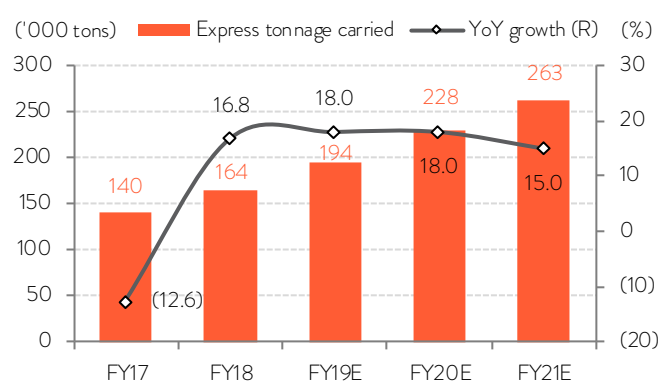
Surface express to lead the way

**We expect surface express to
grow faster than express
industry; large players to gain
market share**

Our analysis of the express industry suggests two key themes playing out over the medium term – (1) surface express will continue outpacing the air express segment, and (2) players with a pan-India reach will continue to garner market share. An aggregation of these two themes should enable pan-India, surface express-focused players to outpace industry growth, which is estimated to clock a ~15% CAGR over the next five years.

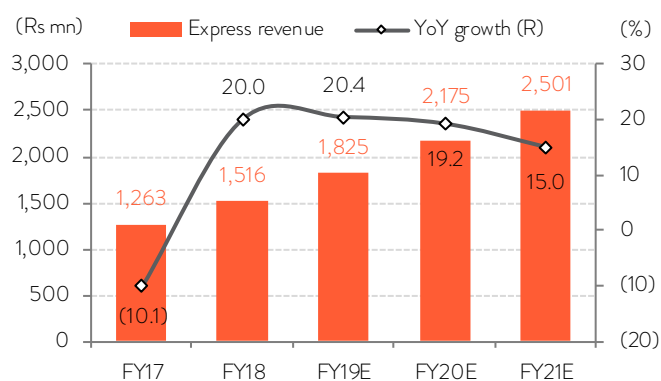
FSCSL ticks both boxes – it is present in surface express and has a reach across multiple states – which should fuel growth going ahead. Accordingly, we expect revenue from the segment to grow at a 17% CAGR over FY19-FY21, largely in line with the surface express industry.

FIG 19 – VOLUME GROWTH EXPECTED TO GROW AT A HEALTHY 16.5% CAGR...



Source: Company, BOBCAPS Research

FIG 20 – ...DRIVING 17% CAGR IN EXPRESS SEGMENT REVENUE



Source: Company, BOBCAPS Research

Synergistic benefits of Vulcan acquisition remain elusive

Vulcan Express – turnaround unlikely in near term

To augment its delivery offerings, FSCSL acquired Vulcan Express – the last-mile delivery arm of Snapdeal – in Feb'18, for a consideration of Rs 350mn. At the time of acquisition, Vulcan had 0.9mn sq ft of space across 15 warehouses, with a reach of >2,000 pin codes, and a focus on the e-commerce segment. As per the company, the acquisition was to bring in several synergies –

- Enable foray into last-mile delivery segment
- Give access to >2,000 pin codes across India
- Allow entry into new services, deriving from the capabilities of Vulcan, such as cash-on-delivery
- Deliver cost and operational efficiencies through integration of Vulcan's warehouses and other operational aspects with FSCSL

The acquisition has not delivered the expected benefits so far. Based on FSCSL's reported numbers, we estimate that Vulcan's operating loss stands at Rs 175mn in H1FY19. While management is confident of achieving operational breakeven in the next few quarters driven by its focus on enhancing efficiencies, we are cautious about the near-term turnaround prospects of the business.

Restructuring process underway

In Q3FY19, FSCSL merged Vulcan with the standalone entity. The new business is called the last-mile delivery and agility solution segment (LMD). Accordingly, the company reported Q3 and 9MFY19 financials inclusive of Vulcan. Since the effective date of the merger was Oct. 2016, it also restated the previous quarters' and FY18 financials.

As per the company's exchange filing and our subsequent discussion with the management, we understand that it is now looking to transfer the last-mile delivery business (Vulcan) on a slump-sale basis to Leanbox Logistics Solutions Pvt Ltd (a company in which FSCSL has 50% shareholding currently) against allotment of shares.

As a result, Leanbox including Vulcan would become a subsidiary (77% stake post transfer) of FSCSL, while the standalone numbers reported will comprise the contract logistics, express and temperature-controlled business segments, and would be comparable with the standalone numbers published in the FY18 annual report. We have calculated the financials of Vulcan based on the restated and previous financials, as provided below.

FIG 21 – DERIVED FINANCIALS FOR VULCAN –PRESSURE ON PROFITABILITY CONTINUES

(Rs mn)	Reported standalone financials (excluding Vulcan)			Reported financials including Vulcan			Vulcan Express – Derived financials		
	H1FY18	H1FY19	FY18	H1FY18	H1FY19	FY18	H1FY18	H1FY19	FY18
Revenue	3,574	5,041	7,750	4,462	5,674	9,299	888	633	1,549
Gross profit	1,203	1,573	2,677	1,400	1,613	2,931	197	40	254
Gross margin (%)	33.6	31.2	34.5	31.4	28.4	31.5	22.2	6.3	16.4
EBITDA	562	709	1,212	422	534	815	(140)	(175)	(397)
EBITDA margin (%)	15.7	14.1	15.6	9.5	9.4	8.8	(15.8)	(27.6)	(25.6)
EBIT	460	556	980	247	320	322	(213)	(236)	(658)
PBT	494	532	987	224	294	306	(270)	(238)	(681)
PAT	333	392	673	224	294	306	(109)	(98)	(367)

Source: Company, BOBCAPS Research | Note: 9MFY19 financials excluding Vulcan aren't available

Operational breakeven unlikely in near term

Our industry interactions suggest that e-commerce last-mile delivery remains a highly competitive industry, with players facing acute margin pressure.

Considering this factor and the company's relatively small size, we are cautious about the turnaround prospects of the LMD segment at the EBITDA level, at least during our explicit projection period up to FY21, although we note that management remains confident of a turnaround. We thus have not assigned any value to the first- and last-mile business of FSCSL (erstwhile Vulcan and Leanbox), as against an investment of Rs 631mn in the two entities.

Financial review

We have projected the standalone financials of FSCSL comprising three businesses – contract logistics, express, and temperature-controlled logistics, while excluding the LMD segment's financials. In our view, this better represents the company's core operational performance. Although the reported 9MFY19 numbers are inclusive of the Vulcan/LMD segment, from Q4FY19 onwards the quarterly financials are expected to have standalone financial disclosures as well.

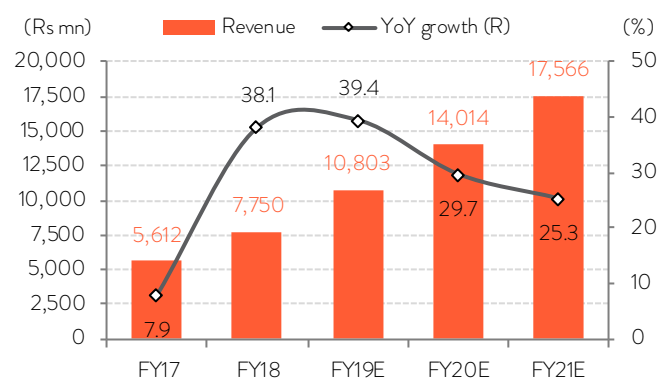
Contract logistics to drive strong 28% revenue CAGR

Contract logistics expected to grow at 30% CAGR over FY19-FY21

We expect a 28% CAGR in standalone revenue over FY19-FY21, driven by 30% growth in contract logistics while the express and temperature-controlled logistics segments grow at 17% and 10% respectively. Consequently, the share of contract logistics is projected to rise to 82% in FY21 from 79% currently.

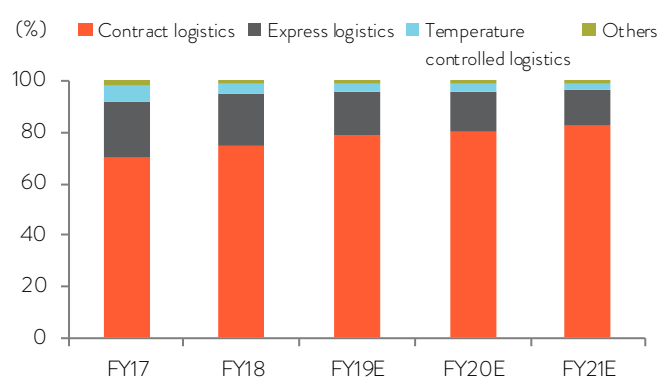
Consensus estimates peg revenue growth of anchor customers FRETAIL/FLFL/FCON at a 15%/20%/33% CAGR over FY19-FY21 – strong growth in anchor clients is expected to be a major driver for the company. Recent traction in new non-anchor client addition also bodes well. To capitalise on these opportunities, FSCSL is adding ~8mn sq ft of warehousing area over FY19-FY21, which should act as a key growth enabler.

FIG 22 – REVENUE TO GROW AT A STRONG 28% CAGR



Source: Company, BOBCAPS Research

FIG 23 – CONTRACT LOGISTICS' SHARE TO INCREASE



Source: Company, BOBCAPS Research

EBITDA margin to expand in FY21

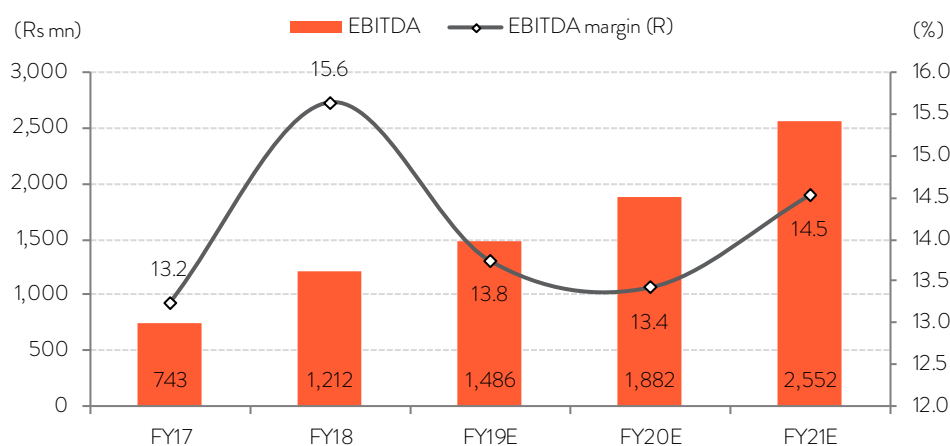
Below-optimum utilisation of new warehousing space dented margins in H1FY19

In H1FY19, FSCSL's standalone EBITDA margin contracted 160bps YoY to 14.1% as the utilisation of new warehousing space was yet to ramp up. The company added ~2.7mn sq ft of space in 9MFY19, much above the 0.6mn sq ft added in whole FY18. As per management, newly commissioned warehousing space typically takes 6-8 quarters before it reaches peak utilisation.

Going ahead, we expect margins to contract further by 40bps in FY20 given (1) the addition of another ~3mn sq ft of space, which is expected to remain below optimum utilisation, and (2) a higher share of the food vertical, which generates lower margins. We thereafter expect operating margins to expand 110bps YoY to 14.5% in FY21, as the utilisation of new space gradually ramps up and operating leverage benefits from higher revenue kick in.

Gradual improvement in utilisation to aid 110bps margin expansion in FY21

FIG 24 – EBITDA MARGIN EXPECTED TO INCREASE IN FY21

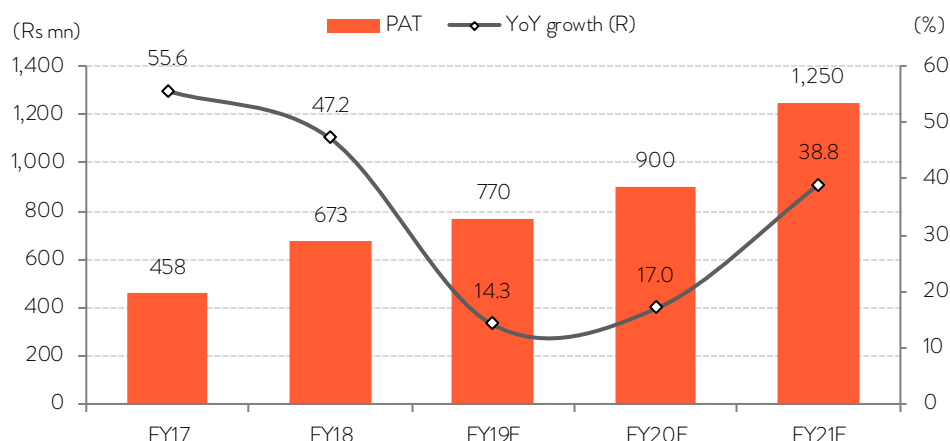


Source: Company, BOBCAPS Research

PAT slated to post strong growth

Margin expansion in FY21 to help drive PAT growth of 27% CAGR

After a growing at a strong 44% CAGR over FY15-FY18, standalone PAT grew at a relatively sedate 17.7% CAGR in H1FY19. Apart from lower EBITDA margins, depreciation increased as the company incurred capex to expand warehousing space; other income also dipped, contributing to the growth moderation. We expect PAT to clock a 27% CAGR over FY19-FY21, with growth rising from 17% in FY20E to 39% in FY21E as margins expand.

FIG 25 – PAT GROWTH TREND

Source: Company, BOBCAPS Research

Capex to affect FCF generation

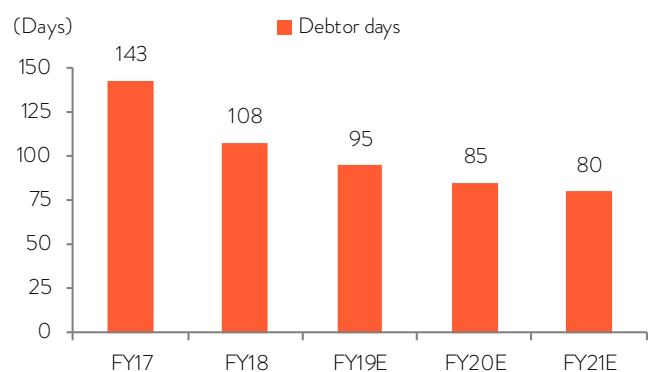
Despite an improvement in operating cash flow (OCF) on account of lower debtor days, free cash flow (FCF) is likely to be affected due to capex outgo over FY19-FY21.

Pruning of customers with payment delays helped improve receivable days

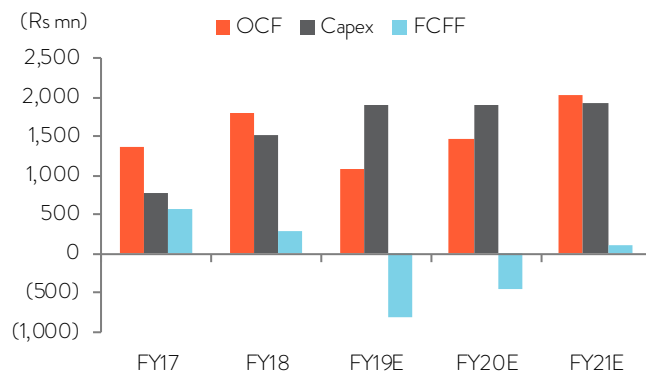
FSCSL's debtor days were at elevated levels - 155 days - in FY16. To lower this untenable receivable cycle, the company decided to discontinue working with some non-anchor customers, across its contract logistics and express segments. This, coupled with a rising share of anchor customers, led to a substantial moderation in receivable days - from 155 in FY16 to 97 days in H1FY19. We expect this trend to continue and forecast a decline to 80 days by FY21, thereby lowering the cash conversion cycle.

FCF to be negative in FY19-FY20 and turn marginally positive in FY21

However, this improvement in working capital cycle is unlikely to percolate to FCF due to high capex. In line with the company's warehousing addition plans, we have pegged capex at ~Rs 1.9bn each year over FY19-FY21. Consequently, we expect FCF to be negative in FY19 and FY20 and turn marginally positive in FY21.

FIG 26 – DEBTOR DAYS TO IMPROVE

Source: Company, BOBCAPS Research

FIG 27 – FCF TO BE MUTED DUE TO HIGH CAPEX

Source: Company, BOBCAPS Research

Valuation methodology

**Initiate coverage with BUY
and a Mar'20 TP of Rs 780**

We value FSCSL using the P/E methodology, assigning a multiple of 25x on FY21E EPS to arrive at a Mar'20 target price of Rs 780 – a 23% upside from current levels. Initiate coverage with BUY.

Since listing on the exchanges in Dec'17, the stock has traded at a median one-year forward P/E multiple of 30x. Our assigned multiple is lower to factor in slower earnings growth – at a 27% CAGR expected over FY19-FY21 vis-à-vis 50% over FY16-FY18 – and lower anticipated FCF generation owing to higher capex outgo.

FIG 28 – KEY VALUATION ASSUMPTIONS

Rs per share	
FY21E EPS	31.2
P/E multiple applied (x)	25
Target price	780
Upside from CMP (%)	23..3

Source: BOBCAPS Research

**DCF method yields a fair
value of Rs 814**

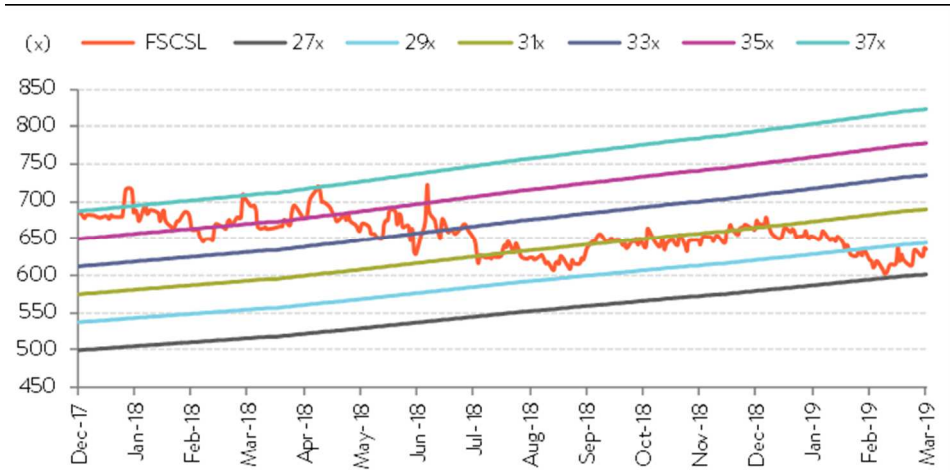
To capture FSCSL's long-term earnings growth potential, we have also done a DCF valuation. We expect the company to maintain a strong growth trajectory over the next 5-6 years, leveraging on industry prospects. Thus, we have factored in a healthy sales/EBITDA/earnings CAGR of 24%/30%/30% over FY18-FY24; our steady-state forecast over FY24-FY30 is 9%/8%/12%. We have discounted the cash flows over FY21-FY30 with a 13.5% weighted average cost of capital and assumed a 6% terminal growth rate, leading to a DCF-based fair value of Rs 814.

FIG 29 – KEY DCF ASSUMPTIONS

Growth assumptions during the projection period – FY19-FY30E (%)	
Revenue CAGR	15.3
EBITDA CAGR	17.6
Earnings CAGR	19.9
Other assumptions (%)	
First year of discounting	FY21
Cost of equity	15.5
WACC	13.5
Terminal growth rate	6.0
Terminal value contribution	61
Target price per share (Rs)	814

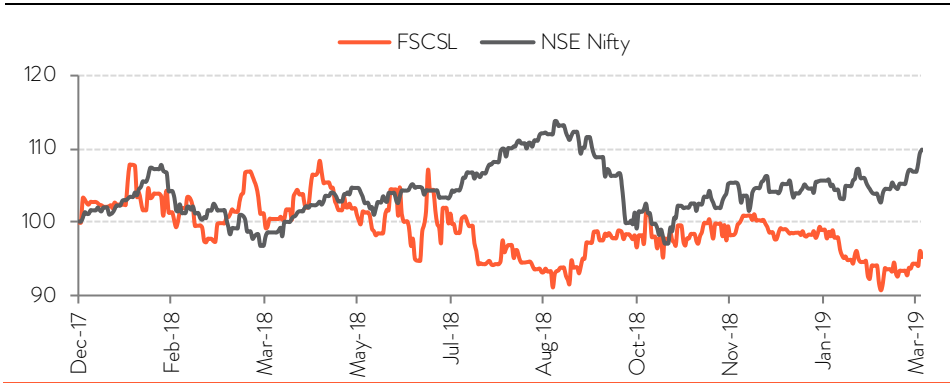
Source: BOBCAPS Research

FIG 30 – ONE-YEAR FORWARD P/E BAND



Source: Bloomberg, BOBCAPS Research

FIG 31 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- **Slowdown in anchor customer business:** Future Group entities continue to form the majority of FSCSL's revenue at ~62%. These anchor customers are also expected to be a major growth driver for the company ahead. Any slowdown in their expansion plans is likely to hurt FSCSL's growth prospects.
- **Optimal utilisation of new warehousing space:** The company plans to add 6mn sq ft over FY19-FY20, more than doubling its total warehousing space of 4.6mn sq ft in FY18. Owing to the resultant higher fixed costs, in case the company is unable to ensure higher utilisation, its EBITDA margin and earnings are likely to be adversely impacted.
- **Shortage of vehicles:** FSCSL outsources its transportation vehicle requirement to third-party vendors. While we note that it has not faced any shortage in vehicle availability in the past, any deterioration in vendor relations or attrition of vendors may lead to a vehicle shortage, impacting operating performance.
- **Slowdown in consumption spends:** About 90% of FSCSL's revenue comes from consumer-oriented industry verticals. In case of a prolonged slowdown in consumption spends in the country, demand for the company's services may decline, weakening operating performance.

Management overview

FIG 32 – KEY MANAGEMENT PERSONNEL

Name	Brief profile
Mayur Toshniwal Managing Director	<p>Mr. Toshniwal has around 25 years of experience across paints, fast moving consumer goods and retail industries, including five years of experience as an entrepreneur. Previously, he has worked with Asian Paints, Coca Cola, Future Group and Allgreen Ecotech solutions which was an entrepreneurial venture. He holds post graduate diploma in management from the Indian Institute of Management, Ahmedabad and a bachelor's degree in technology in Mechanical Engineering from the Indian Institute of Technology, Banaras Hindu University, Varanasi. He has been a Director on the Board of the Company since August 5, 2017.</p>
P V Sheshadri Chief Executive Officer	<p>Mr. Sheshadri has 26 years of experience in the supply chain solution function in the field of warehousing, transportation, project procurement and vendor development/management. He holds a Bachelor's degree in Science from Bangalore University. Previously, he has worked with Llyods Steel, Grasim Industries, Bomabay Dyeing, Pantaloons Retail and Welspun Retail.</p>
Samir Kedia Chief Financial Officer	<p>Mr. Kedia has 16 years of experience primarily in commercial, financial and accounting affairs besides corporate secretarial and compliance functions. He is a qualified chartered accountant; and has been part of the Future Group for more than 12 years, most recently associated with Future Consumers Ltd. as Financial Controller. He has also worked with H&R Johnson (India) Ltd.</p>

Source: Company, BOBCAPS Research

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Total revenue	5,612	7,750	10,803	14,014	17,566
EBITDA	743	1,212	1,486	1,882	2,552
EBIT	552	980	1,131	1,333	1,831
Net interest income/(expenses)	(128)	(87)	(159)	(145)	(145)
Other income/(expenses)	158	94	68	97	98
Exceptional items	0	0	0	0	0
EBT	582	987	1,040	1,286	1,785
Income taxes	(125)	(313)	(270)	(386)	(536)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	458	673	770	900	1,250
Adjustments	0	0	0	0	0
Adjusted net profit	458	673	770	900	1,250

Balance Sheet

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Accounts payables	978	1,384	1,647	2,281	2,819
Other current liabilities	234	683	989	869	1,064
Provisions	28	59	83	107	134
Debt funds	827	347	2,241	1,990	1,990
Other liabilities	0	0	0	0	0
Equity capital	391	401	401	401	401
Reserves & surplus	2,537	3,769	4,484	5,221	6,245
Shareholders' fund	2,928	4,170	4,884	5,622	6,645
Total liabilities and equities	4,994	6,642	9,844	10,869	12,652
Cash and cash eq.	470	757	1,621	615	360
Accounts receivables	2,198	2,289	2,812	3,264	3,850
Inventories	0	0	0	0	0
Other current assets	196	156	312	405	507
Investments	0	631	631	631	631
Net fixed assets	1,288	2,608	4,178	5,537	6,743
CWIP	698	26	0	0	0
Intangible assets	10	13	13	13	13
Deferred tax assets, net	(101)	(155)	(155)	(155)	(155)
Other assets	236	318	432	561	703
Total assets	4,994	6,642	9,844	10,869	12,652

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Net income + Depreciation	649	906	1,125	1,449	1,971
Interest expenses	128	87	159	145	145
Non-cash adjustments	(11)	54	0	0	0
Changes in working capital	595	752	(200)	(134)	(72)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	1,361	1,799	1,084	1,459	2,043
Capital expenditures	(784)	(883)	(1,900)	(1,907)	(1,927)
Change in investments	0	(631)	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(784)	(1,514)	(1,900)	(1,907)	(1,927)
Equities issued/Others	0	9	0	0	0
Debt raised/repaid	4	(480)	1,895	(251)	0
Interest expenses	(128)	(87)	(159)	(145)	(145)
Dividends paid	0	(48)	(55)	(163)	(226)
Other financing cash flows	(2)	608	0	0	0
Cash flow from financing	(125)	1	1,680	(558)	(371)
Changes in cash and cash eq.	451	286	864	(1,006)	(255)
Closing cash and cash eq.	470	757	1,621	615	360

Per Share

Y/E 31 Mar (Rs)	FY17A	FY18A	FY19E	FY20E	FY21E
Reported EPS	11.7	16.8	19.2	22.5	31.2
Adjusted EPS	11.7	16.8	19.2	22.5	31.2
Dividend per share	0.0	1.0	1.1	3.4	4.7
Book value per share	74.8	104.1	121.9	140.3	165.9

Valuations Ratios

Y/E 31 Mar (x)	FY17A	FY18A	FY19E	FY20E	FY21E
EV/Sales	4.7	3.3	2.3	1.9	1.5
EV/EBITDA	35.1	21.2	16.8	13.8	10.5
Adjusted P/E	54.1	37.6	32.9	28.2	20.3
P/BV	8.5	6.1	5.2	4.5	3.8

DuPont Analysis

Y/E 31 Mar (%)	FY17A	FY18A	FY19E	FY20E	FY21E
Tax burden (Net profit/PBT)	78.6	68.2	74.0	70.0	70.0
Interest burden (PBT/EBIT)	105.5	100.7	92.0	96.5	97.5
EBIT margin (EBIT/Revenue)	9.8	12.6	10.5	9.5	10.4
Asset turnover (Revenue/Avg TA)	1.5	1.8	1.8	1.9	2.1
Leverage (Avg TA/Avg Equity)	1.8	1.6	1.8	2.0	1.9
Adjusted ROAE	16.9	19.0	17.0	17.1	20.4

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY17A	FY18A	FY19E	FY20E	FY21E
YoY growth (%)					
Revenue	7.9	38.1	39.4	29.7	25.3
EBITDA	6.3	63.1	22.6	26.6	35.6
Adjusted EPS	55.6	43.8	14.3	17.0	38.8
Profitability & Return ratios (%)					
EBITDA margin	13.2	15.6	13.8	13.4	14.5
EBIT margin	9.8	12.6	10.5	9.5	10.4
Adjusted profit margin	8.2	8.7	7.1	6.4	7.1
Adjusted ROAE	16.9	19.0	17.0	17.1	20.4
ROCE	15.2	23.0	18.9	17.7	22.1
Working capital days (days)					
Receivables	143	108	95	85	80
Inventory	0	0	0	0	0
Payables	73	77	65	69	69
Ratios (x)					
Gross asset turnover	3.5	3.2	2.6	2.3	2.2
Current ratio	2.4	1.5	1.8	1.3	1.2
Net interest coverage ratio	4.3	11.2	7.1	9.2	12.7
Adjusted debt/equity	0.1	(0.1)	0.1	0.2	0.2

Source: Company, BOBCAPS Research

BUY

TP: Rs 880 | ▲ 18%

TCI EXPRESS

Logistics

14 March 2019

Best play in the express industry – initiate with BUY

TCI Express (TCIEXP), with its established footprint in India's fast-growing surface express distribution industry and extensive network reach, is on track for a robust 17% revenue CAGR over FY19-FY21E. Efficiency gains and operating leverage benefits are likely to bolster EBITDA margins, aiding a strong 25% earnings CAGR. We expect return ratios to remain healthy (FY21 ROE/ROCE of 30%/42%) thanks to judicious capital allocation. Our Mar'20 target price of Rs 880 is set at 30x FY21E P/E – initiate with BUY.

Sayan Das Sharma | Rohan Korde

research@bobcaps.in

In a sweet spot: We expect two themes to continue dominating the Indian express industry over the next five years – (1) surface express segment to grow ahead of industry (at 18-20% vs. 15% industry CAGR), and (2) national players to gain market share (to ~60% from 50% currently). Among listed players, TCIEXP is in a sweet spot owing to its higher focus on surface express operations (86% of revenue) and pan-India reach (~95% of all pin codes).

Key growth catalysts: TCIEXP's operations are underpinned by a large client base (200,000+) comprising corporate majors and SMEs, a diversified presence across industries (auto/pharma/retail), wide branch network (680), and proven asset-light model. Incremental capex to enhance capacity and expand the branch network in tier-II and III cities should complement growth.

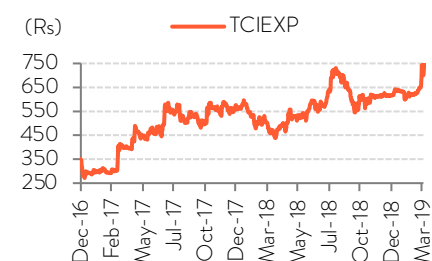
Robust earnings profile: After clocking a 44% CAGR over FY16-FY18, we expect earnings growth to remain healthy at a 25% CAGR over FY19-FY21. A volume/revenue CAGR of 14%/17% and 120bps EBITDA margin expansion backed by efficiency gains during this period are expected to catalyse growth.

Initiate with BUY: We have a Mar'20 TP of Rs 880 for the stock based on a one-year forward P/E multiple of 30x, implying upside of 18%.

Ticker/Price	TCIEXP IN/Rs 744
Market cap	US\$ 409.6mn
Shares o/s	38mn
3M ADV	US\$ 0.1mn
52wk high/low	Rs 768/Rs 584
Promoter/FPI/DII	67%/4%/7%

Source: NSE

STOCK PERFORMANCE



Source: NSE

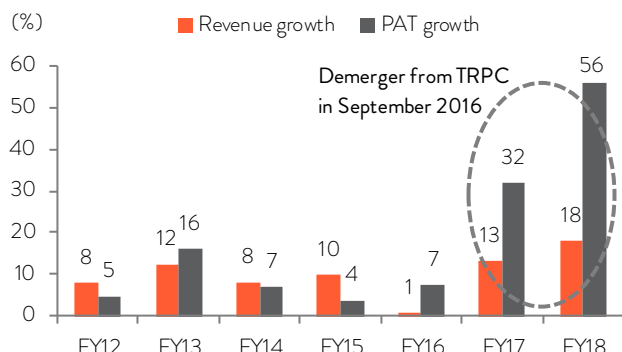
KEY FINANCIALS

Y/E 31 Mar	FY17A	FY18A	FY19E	FY20E	FY21E
Adj. net profit (Rs mn)	375	584	724	900	1,125
Adj. EPS (Rs)	9.8	15.3	18.9	23.5	29.4
Adj. EPS growth (%)	32.7	55.8	24.0	24.3	25.0
Adj. ROAE (%)	26.4	31.8	30.9	30.3	30.1
Adj. P/E (x)	76.0	48.8	39.3	31.6	25.3
EV/EBITDA (x)	46.5	31.7	24.0	19.4	15.7

Source: Company, BOBCAPS Research

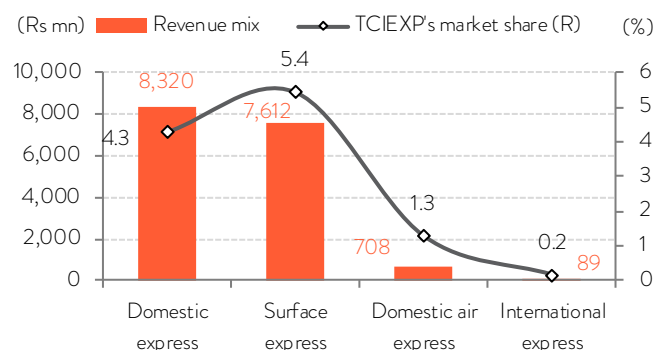
In a nutshell

FIG 1 – UPTICK IN REVENUE AND PAT GROWTH POST DEMERGER FROM TRANSPORT CORP



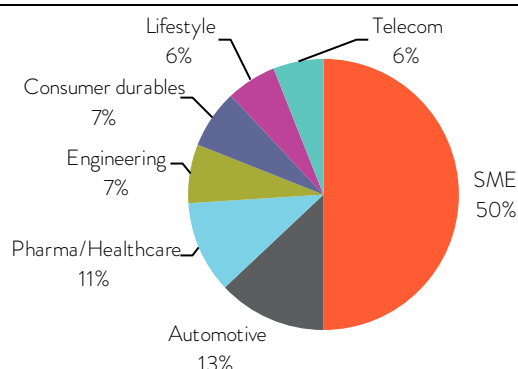
Source: Company, BOBCAPS Research

FIG 2 – SIZEABLE PLAYER IN DOMESTIC SURFACE EXPRESS SEGMENT, FY18



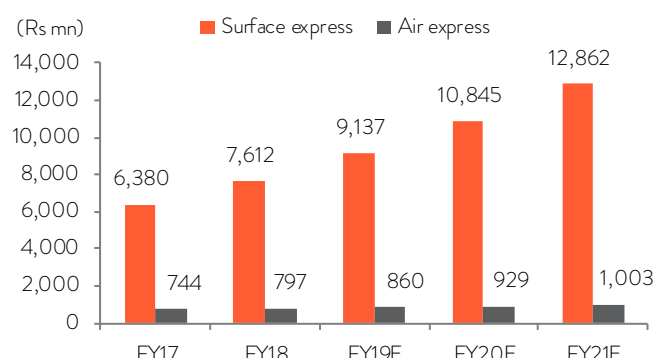
Source: Company, BOBCAPS Research

FIG 3 – CLIENT MIX FAIRLY DIVERSIFIED ACROSS INDUSTRIES



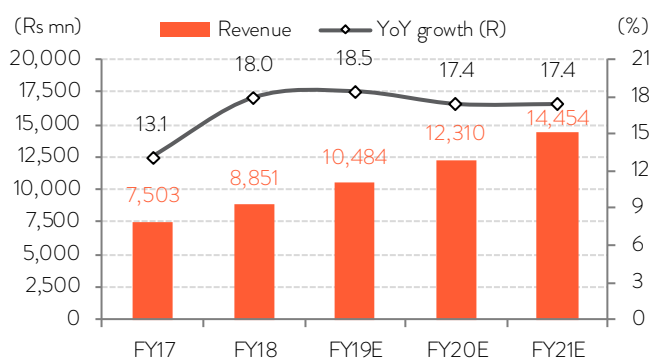
Source: Company, BOBCAPS Research

FIG 4 – TCIEXP'S SURFACE EXPRESS REVENUE EXPECTED TO GROW FASTER THAN AIR EXPRESS



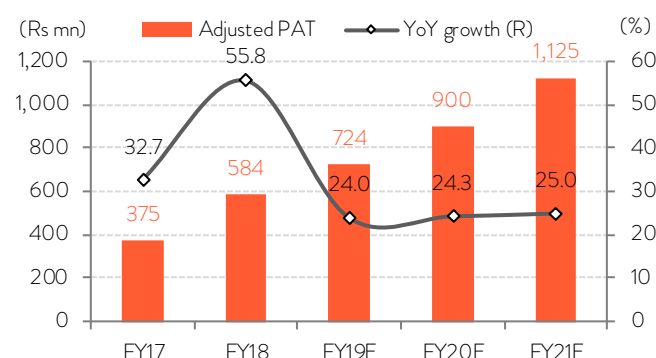
Source: Company, BOBCAPS Research

FIG 5 – ESTIMATE 17% REVENUE CAGR LED BY HIGHER VOLUMES



Source: Company, BOBCAPS Research

FIG 6 – ADJ. PAT PROJECTED TO GROW AT STRONG 25% CAGR OVER FY19-FY21



Source: Company, BOBCAPS Research

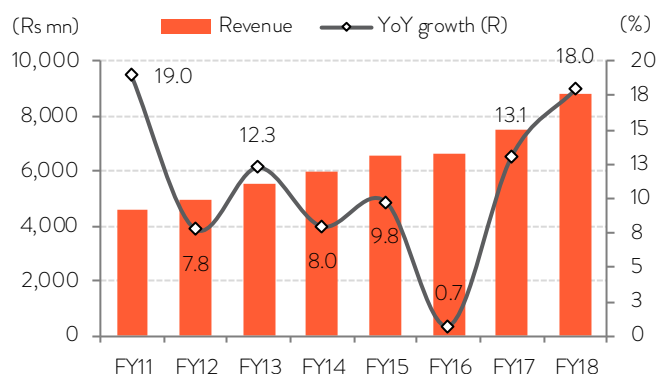
Investment rationale

Strong uptick in growth post demerger

Demerger from the parent company in 2016 has ushered in a new growth phase for TCIEXP. Erstwhile a business division of Transport Corporation of India (TRPC), TCIEXP was demerged into a new entity in 2016, as the distinct characteristics of the business required dedicated management attention.

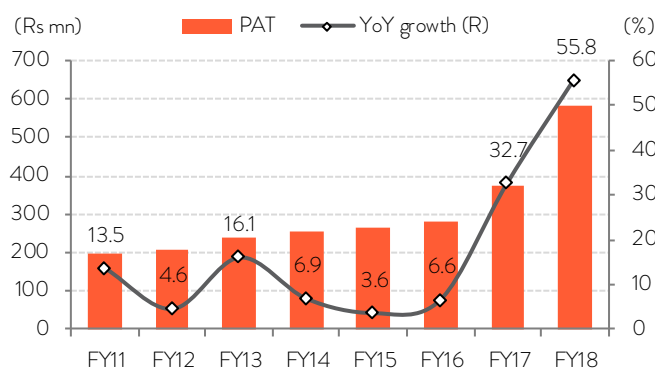
Enhanced management focus backed by adequate investments have since rejuvenated growth – revenue/PAT have increased at 13%/33% in FY17 and 18%/56% in FY18, substantially higher than the 7.6%/7.5% CAGR over FY11-FY16. The demerger has also unlocked value for investors, enabling them to play on the growing express industry story as a separate investment theme.

FIG 7 – REVENUE GROWTH REBOUNDED POST DEMERGER...



Source: Company, BOBCAPS Research | Note: Appointed date of demerger was 31 Mar 2016

FIG 8 – ...DRIVING STURDY GROWTH IN TCIEXP's PROFITABILITY



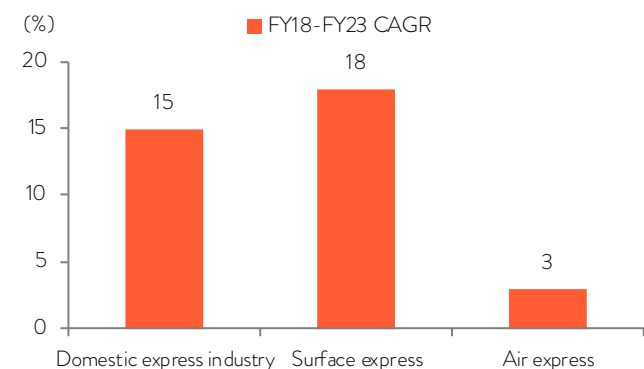
Source: Company, BOBCAPS Research

Surface express segment in India to grow faster at ~18% vs. single-digit growth for air express over next five years

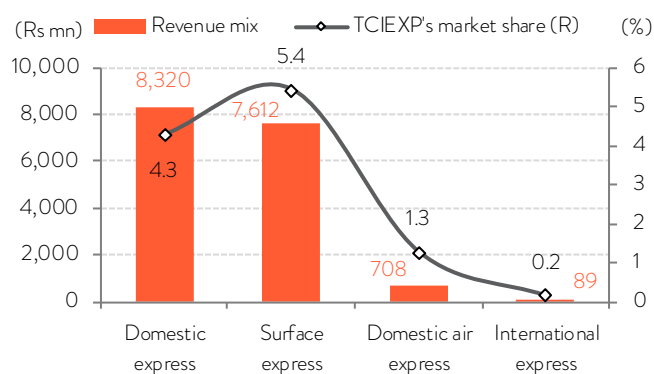
In a sweet spot to benefit from industry tailwinds

Our analysis of the express distribution industry suggests two key themes playing out over the medium-long term – (1) surface express distribution continuing to outpace the air express segment, and (2) players with a pan-India reach continuing to garner market share. These structural tailwinds should enable pan-India surface express players to outperform expected industry growth of ~15% over the next five years.

In our view, TCIEXP is aptly positioned, being one of the country's premier surface express industry players (~5% share) with a national footprint reaching ~95% of India's 19,000+ pin codes, a well-balanced client mix, and a majority (95%) of its revenue derived from the lucrative B2B division.

FIG 9 – SURFACE EXPRESS SEGMENT EXPECTED TO GROW FASTER THAN THE EXPRESS INDUSTRY


Source: Company, Deloitte, BOBCAPS Research

FIG 10 – TCIEXP HAS SIZABLE MARKET SHARE IN DOMESTIC SURFACE EXPRESS DISTRIBUTION, FY18


Source: Company, Deloitte, BOBCAPS Research

A leading express service provider

TCIEXP is the third largest express service provider in India, after Blue Dart Express (BDE) and Gati Kintetsu Express (Gati KWE; subsidiary of the publicly listed GTIC), in terms of revenue. We believe TCIEXP compares favourably with these players on most parameters, which underpins its strong market positioning.

FIG 11 – TCIEXP: COMPETITIVE POSITIONING

Parameter	BDE	TCIEXP	Gati KWE
Market position	The leading air express operator with ~50% market share; sizable player in surface express delivery	One of the leading surface express players, also present in air express	Among the leaders in surface express and e-retail logistics; also present in air express
Network & reach	Serves ~17,700 pin codes across India through a vast network of 600+ branches and 100+ hubs	Caters to 18,000+ pin codes through a wide network of 28 sorting centres, 680 branch offices, and 2,500 feeder routes	Present across ~5,400 direct and ~14,500 remote pin codes
Focus (mode, industry segment)	Air express; both B2B and B2C	Surface express (86% revenue share); primarily B2B (95%)	Primarily surface (75-80% revenue share)
Fleet available (FY18)	11,122 vehicles; 6 aircraft	5,000 containerised vehicles	5,000 vehicles
Asset ownership	Asset-light in surface; owns aircraft	Asset-light; owns 10 sorting centres	Mix of asset-light and asset-heavy
Market share (domestic express segment, %)	~14	~4	~6
FY18 revenue (Rs mn)	27,906	8,872	11,663

Source: Company, Industry, BOBCAPS

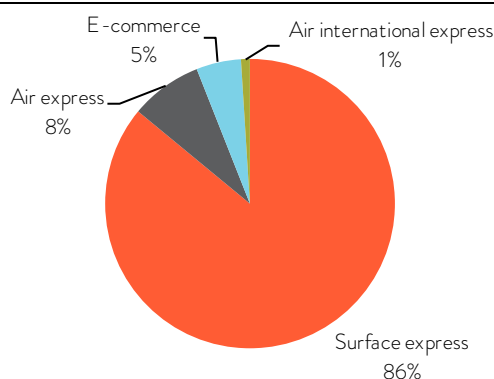
Surface express, B2B key focus areas

Surface mode dominates with 86% of revenue share; B2B clients account for 95%

TCIEXP provides various services to customers – surface express (86% of revenue), domestic air express (8%), international air express (1%), e-commerce logistics (5%), and reverse logistics. Surface express will remain the dominant mode going forward owing to higher management focus.

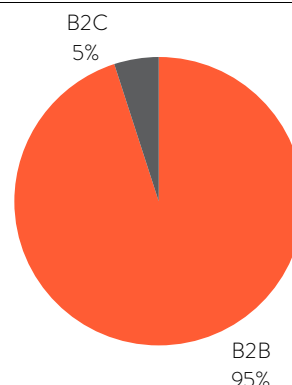
Among customer segments, B2B remains the core with 95% revenue contribution. Despite B2C being the faster growing segment, the company focuses on the B2B segment as it generates better margins and is comparatively less competitive. In B2C, it works largely with smaller e-commerce companies – such as Naaptol, Shopclues and Infibeam – in tier-II and tier-III cities, owing to the lower competition – leveraging on its expansive branch network.

FIG 12 – SURFACE EXPRESS CONTRIBUTES 86% OF REVENUE



Source: Company, BOBCAPS Research

FIG 13 – B2B CUSTOMER SEGMENT A PRIMARY FOCUS AREA



Source: Company, Deloitte, BOBCAPS Research

Network of 680 branches and 500 express routes enables pan-India coverage

Robust network infrastructure enables national reach

TCIEXP has a robust network spanning the entire country. It caters to ~95% of all pincodes in India through its network of 28 sorting centres, 500 express routes, 2,500 feeder routes, and 680 branch offices. Access to ~5,000 vehicles supports this network infrastructure. The company has further strengthened its network across the country post the demerger – branch office network increased to 680 in 9MFY19, from 550 in FY17. Going forward, it plans to expand some of the existing sorting centres, add new centres, and increase the branch office network to ~1,000 within the next two years.

A pan-India network results in a balanced geographic mix for the company. The North zone contributes 29% of revenue, followed by the West and South zones (28% each), and East and special zones (15%). In our view, this wide presence provides TCIEXP with a distinct edge over regional and local players that only cater to a particular region.

Well-rounded client mix lays a strong foundation for growth

TCIEXP has developed a strong clientele comprising marquee names across industries, complemented by a diverse SME client base. As per management, the company has ~200,000 clients as of 9MFY19. Currently, large corporate clients account for ~50% of total revenue, while SMEs contribute the rest.

Large corporates and SMEs account for 50% of revenue each

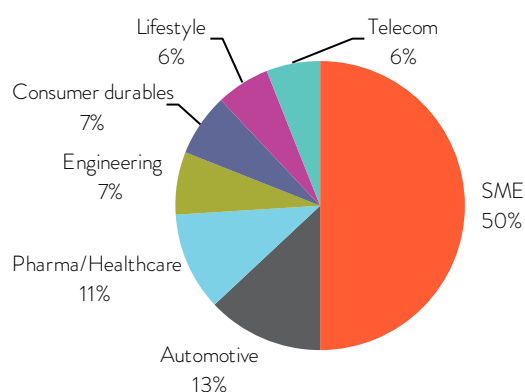
The company's client roster features prominent names across an array of industries – automobiles, pharmaceuticals, electrical goods and energy, retail and textile, telecom and e-commerce. It typically acquires large institutional customer accounts by participating in their tendering process. Contracts with such customers are for a minimum of one year, after which the tendering process is repeated. These customers look for reliable service along with competitive pricing, which TCIEXP has been providing successfully, ensuring repeat business. Large corporates provide revenue visibility and meet payment commitments, albeit at a lower margin profile.

The company has also established a large SME clientele, leveraging on the growing demand from SMEs for organised express players capable of providing reliable services. These contracts are shorter-term in nature, but owing to the company's better bargaining power (in many cases it is the sole express vendor to these SMEs) usually generate better margin.

Low concentration risk – top 25 clients account for 10-11% of revenue

In our view, this healthy mix of large and small customers lays a strong base for future growth. A diversified clientele also lowers concentration risk – as per the company, the top 25 clients together contribute only 10-11% of total revenue.

FIG 16 – DIVERSIFIED PRESENCE ACROSS SEVERAL INDUSTRIES



Source: Company, BOBCAPS Research

FIG 17 – CLIENT ROSTER INCLUDES MARQUEE NAMES ACROSS INDUSTRY SEGMENTS

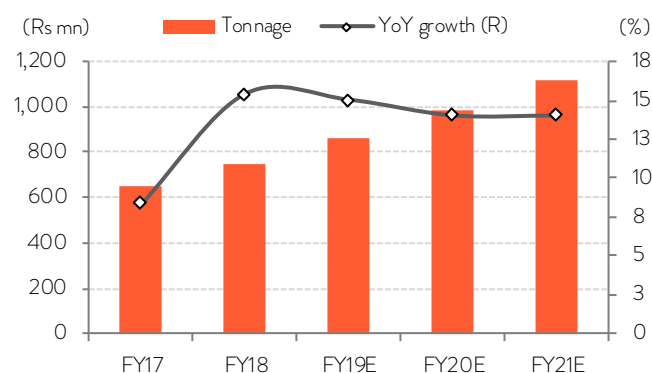
Auto	Pharma	Electrical goods	Retail	Telecom	E-commerce
Hero MotoCorp	Dr Reddy's	BHEL	Page Industries	Nokia	Flipkart
Tata Motors	Micro Labs	Havells	ITC	Xiaomi	Shopclues
Maruti Suzuki	Cipla	Cummins	Adidas	Siemens	Home Shoppe
Toyota	Intas	Panasonic	Reebok	NRB	Naaptol
Eicher Motors	Neon	L&T	Arvind	Spirax	Oyo
Force Motors	Allergan	Yokogawa	Raymond	Meritor	ShopCJ
Ford	Abbott	ABB	Lifestyle	ISGES	Entex
TVS	Zydus Cadila	Epitome	Siyaram's	TE	Infibeam

Source: Company, BOBCAPS Research

Expect TCIEXP's volumes to grow at 14% CAGR

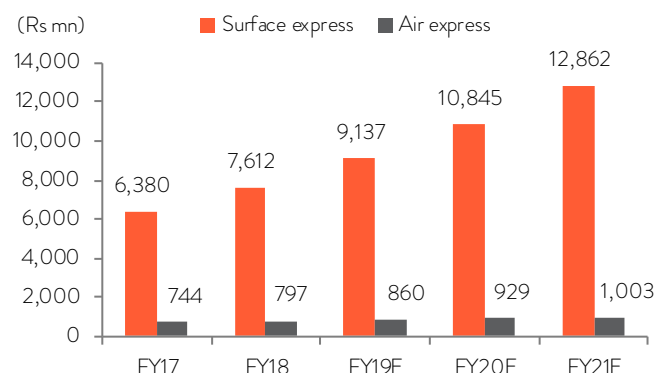
TCIEXP's well-entrenched market positioning would help the company leverage on the robust prospects of India's express industry. We expect tonnage carried to log a 14% CAGR over FY19-FY21. Surface express is projected to grow at 19% vs. an 8% CAGR for air express over FY19-FY21. We model for a ~3% CAGR in realisations during the same period, culminating in a 17.4% CAGR in revenue.

FIG 18 – TONNAGE GROWTH PEGGED AT 14% CAGR OVER FY19-FY21E



Source: Company, BOBCAPS Research

FIG 19 – SURFACE EXPRESS REVENUES TO CONTINUE TO OUTPACE AIR EXPRESS



Source: Company, BOBCAPS Research

Asset-light on vehicles; owns ~30% of total sorting centres at key locations

Striking the right balance of asset-light vs. ownership model

TCIEXP follows a blend of an asset-light and asset-ownership model. A majority of its gross block is deployed toward network infrastructure, mainly sorting centres in key locations, which are critical to its operations – out of its 28 sorting centres, it owns 10 in key locations. The company does not own any vehicles and meets its fleet requirement entirely through a network of vendors. We believe that TCIEXP has struck the right balance with its business model – outsourced vehicles enable it attain scale with limited capital, while owning key assets helps it ensure operational control.

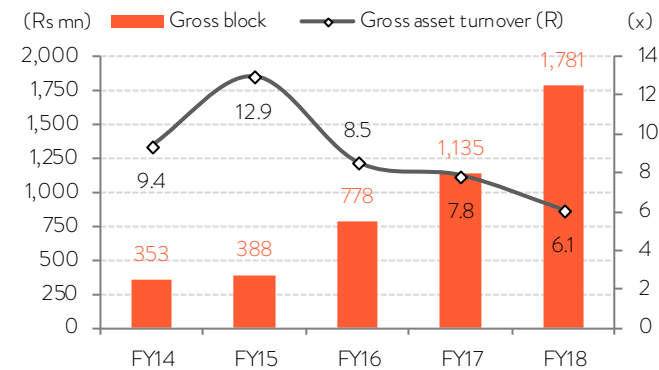
5,000 vehicles sourced from 1,500 vendors to de-risk the business model

De-risked asset-light model fulfils fleet requirement

Instead of investing in a fleet, TCIEXP leverages on the fragmented fleet ownership industry to meet its vehicle requirements. It has access to 5,000 vehicles through a network of 1,500 vendors and has taken several measures to de-risk its business model – (1) no more than 3-4 vehicles sourced from the same vendor; (2) payment made on kilometre-run basis to vendors, without any linkage to utilisation levels/tonnage carried; (3) vehicles replaced every 6-7 years; and (4) thorough diligence conducted of fleet owner's financial standing and security deposit taken before enlisting the operator.

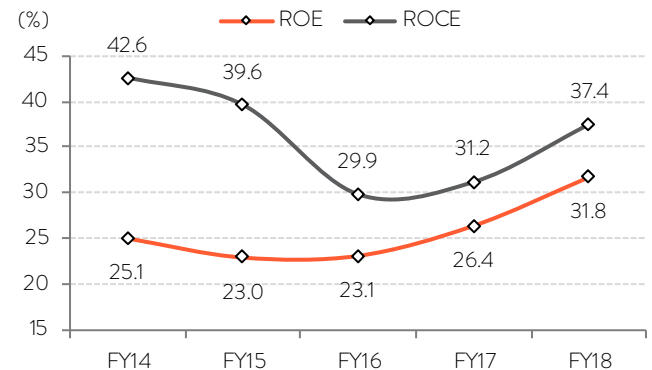
For air express as well, the company does not own the aircraft and partners with commercial aircraft to carry its cargo. This prudent strategy helps it optimise carrier utilisation, boosting operating margins.

FIG 20 – ASSET-LIGHT STRATEGY DRIVES HIGHER ASSET TURNS...



Source: Company, BOBCAPS Research

FIG 21 – ...THEREBY BOOSTING RETURN RATIOS



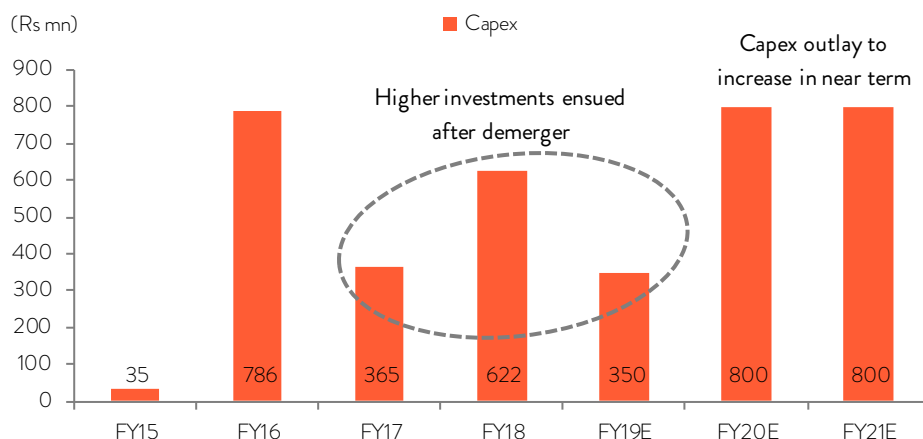
Source: Company, BOBCAPS Research

Plans to spend Rs 4bn to expand handling capacity and branch network

Capex plan envisages addition of more owned sorting centres

After demerger from the erstwhile parent company, TCIEXP has stepped up its capex plan to support growth. To further expand its network infrastructure, the company has earmarked capex of Rs 4bn to be spent over five years starting from FY19 – this comprises Rs 3.5bn towards increasing handling capacity of the sorting centres and branch network, and Rs 0.5bn towards information technology (IT) infrastructure. While capex has been on the lower side in FY19 (~Rs 200mn in 9MFY19), FY20-FY21 outlay is expected to rise to Rs 800mn each.

TCIEXP currently owns ~30% of its 2.2mn sq ft of sorting area (10 out of 28 sorting centres), while ~70% are leased. Going forward, it plans to own most of the incremental sorting centres, especially in key locations, as this provides better operational control and eliminates renewal/lease rental risk. As per management, the company has already acquired land in key cities such as Delhi, Pune, Kolkata and Indore, and is currently seeking requisite approvals.

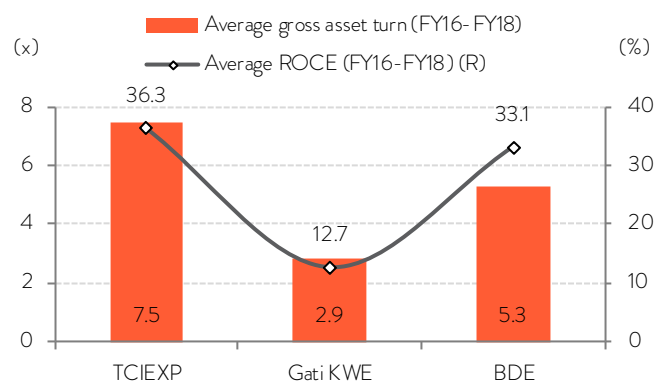
FIG 22 – CAPEX OUTLAY TO INCREASE OVER FY20-FY21E

Source: Company, BOBCAPS Research

Superior asset-light model vis-à-vis peers

Better ROCE and asset turn than peers a testament to effective capital allocation

TCIEXP has been a better proponent of the asset-light strategy than other express players, in our view. This is reflected in its higher gross asset turnover and superior pre-tax ROCE. The company's capital deployment strategy has also been starkly different from peers – TCIEXP has ~80% of its FY18 gross block geared towards land and buildings, with only ~10% towards vehicles and plant & machinery as it outsources its vehicle requirement. In contrast, Gati KWE has ~25% of its gross block deployed towards vehicles and plant & machinery owing to higher vehicle ownership, while BDE has ~62% towards aircraft components and overhaul, machinery and equipment as it owns some aircraft.

FIG 23 – HIGHER ASSET TURN AND ROCE INDICATE BETTER EXECUTION OF ASSET-LIGHT MODEL

Source: Company, BOBCAPS Research

FIG 24 – LOWER GROSS BLOCK DEPLOYED TOWARDS VEHICLES AND PLANT & MACHINERY THAN PEERS

% of total gross block	TCIEXP	Gati KWE	BDE
Land	36	31	11
Building	43	16	2
Plant and machinery	6	12	17
Vehicles (includes aircraft components for BDE)	3	12	45
Furnitures and fixtures	4	9	10
Others	7	19	15
Total	100	100	100

Source: Company, BOBCAPS Research

Outperforms peers on most financial parameters

We have benchmarked the financial performance of the three leading express players in India. Since the demerger, TCIEXP's financial performance has improved, which has helped it outstrip peers on most key parameters, as illustrated in Fig 25.

FIG 25 – TCIEXP VS. PEERS ON KEY RATIOS

Parameter	TCIEXP				Gati KWE				BDE			
	FY16	FY17	FY18	Average	FY16	FY17	FY18	Average	FY16	FY17	FY18	Average
Revenue growth (%)	0.7	13.1	18.0	15.5	0.1	(2.6)	5.0	1.2	12.4	4.9	4.2	4.6
ROE (%)	23.1	26.4	31.8	27.1	12.9	9.0	8.6	10.2	57.1	34.5	30.1	40.6
ROCE (%)	40.4	31.2	37.4	36.3	15.9	11.2	11.1	12.7	43.5	29.2	26.6	33.1
Debtor days	58	55	64	59	46	37	47	43	42	49	55	49
Payable days	14	20	30	21	25	17	30	24	86	88	66	80
Gross asset turnover (x)	8.5	7.8	6.1	7.5	3.0	2.8	2.8	2.9	6.5	5.0	4.4	5.3
Total asset turnover (x)	8.0	4.1	4.0	5.4	1.9	1.9	1.8	1.9	2.3	2.0	1.9	2.1
Debt/EBITDA (x)	0.8	0.5	0.4	0.6	1.5	1.9	1.7	1.7	1.2	1.4	1.2	1.3

Source: Company, BOBCAPS Research

We have compared the common size P&L for the three players to display the relative difference in business models

FIG 26 – COMMON SIZE P&L FOR EXPRESS PLAYERS

(%)	TCIEXP	Gati KWE	BDE
FY18 Revenue – absolute (Rs mn)	8,851	11,663	27,906
Revenue	100.0	100.0	100.0
Operating expenses	75.1	69.1	52.8
Gross profit	24.9	30.9	47.2
Employee costs	8.2	13.2	20.9
Other expenses	6.5	11.7	13.7
EBITDA	10.2	6.1	12.5
Depreciation	0.6	1.5	4.1
EBIT	9.7	4.6	8.5
Other income	0.2	0.3	0.7
Interest expenses	0.4	1.5	1.4
PBT	9.5	3.4	7.8
Tax	2.9	0.8	2.6
PAT	6.6	2.7	5.2

Source: Company, BOBCAPS Research

- TCIEXP has the lowest gross margin among peers as it outsources its vehicle requirement to vendors. BDE's gross margin is the highest, benefitting from higher contribution of the air express segment which generates higher margins.

- Employee cost as a percentage of sales is the lowest for TCIEXP as it needs fewer vehicle drivers, implying lower manpower and allied costs, owing to its outsourcing strategy. Lower other expenses stem from divergence in rent expenses as a percentage of sales vs. peers.
- A higher share of air express revenue helps BDE post higher EBITDA margins than peers.
- The benefit of TCIEXP's asset-light model is visible in lower depreciation and interest expenses, enabling it to generate higher PBT and PAT margins than peers.

Financial review

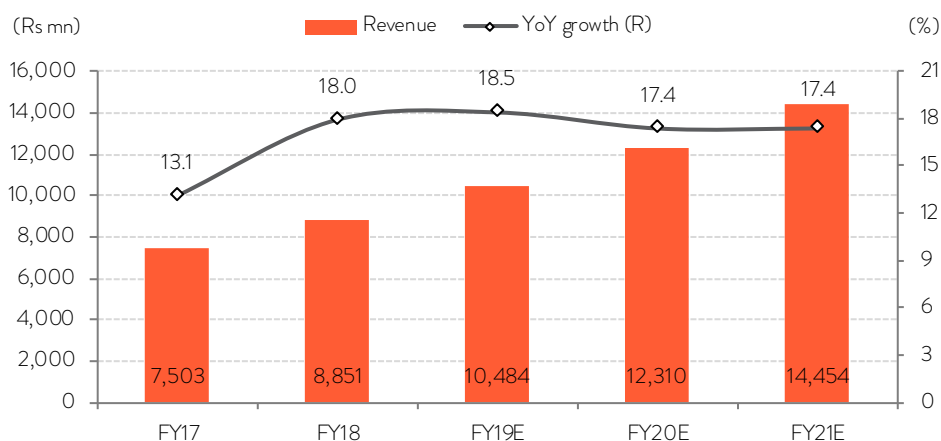
Volume growth to drive 17% revenue CAGR

**Expect volume growth of 14%;
realisation growth of 3% over
FY19-FY21**

Driven by sturdy volume growth, we expect TCIEXP's revenue to grow at a 17% CAGR over FY19-FY21, largely in line with the express industry. Total tonnage is projected to increase at a 14% CAGR, aided by client additions, demand from the SME segment and branch network expansion. A presence in high-growth industry verticals such as pharma, auto and retail is expected to provide added impetus. The company has announced that it will declare higher rates for FY20 in Apr'19, which should aid realisations – we expect a 3% CAGR in realisations over FY19-FY21.

Capacity utilisation levels remain elevated at 86% currently, with optimum utilisation at 90-92% as per management. To ensure adequate capacity, the company is expanding its sorting centres, which should be a growth enabler.

FIG 27 – REVENUE EXPECTED TO GROW AT 17% CAGR TO RS 14.5BN BY FY21



Source: Company, BOBCAPS Research

Operating efficiency to drive margin expansion

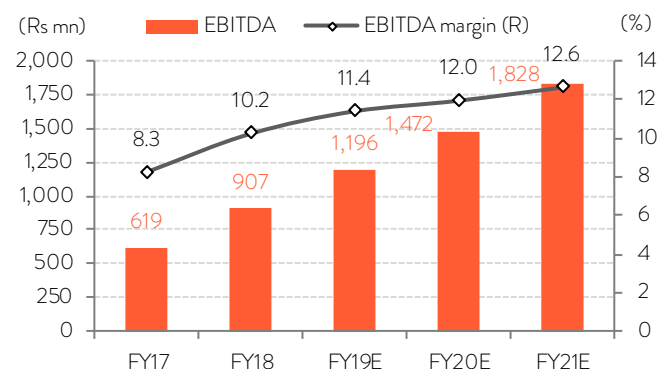
**Estimate a 24%/25% CAGR
in EBITDA/PAT over FY19-
FY21**

We expect TCIEXP's EBITDA margin to expand by 120bps to 12.6% over FY19-FY21 as (1) healthy volume growth drives operating leverage benefits; (2) a higher share of owned sorting centres lowers rental expenses; and (3) increased automation fuels efficiency gains. Consequently, EBITDA is estimated to grow at a 24% CAGR during the same period.

We note that our margin estimates are below management's guidance for 14%+ margins by FY21 as we are cautious on the potential impact of competition from the unorganised segment on pricing and hence on margins. Any sharp increase in diesel prices can also have a transitory impact, as the increase is often passed on with a lag, at least for contractual customers. Our margin assumptions thus carry an upside risk, if management meets margin guidance. Consequent to healthy

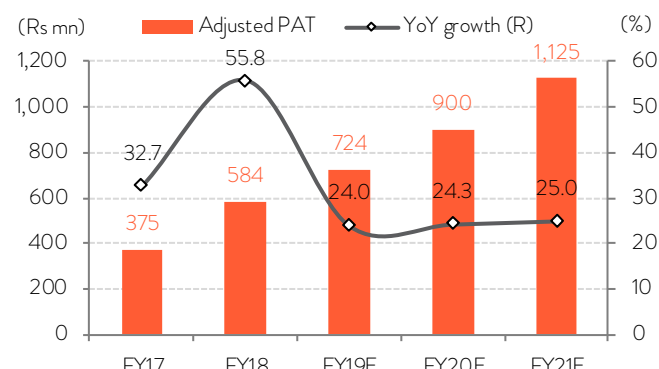
EBITDA growth, adj. PAT is also expected to log a strong 25% CAGR over FY19-FY21 to Rs 1.1bn.

FIG 28 – HEALTHY EBITDA MARGIN EXPANSION OF 120BPS...



Source: Company, BOBCAPS Research

FIG 29 – ...EXPECTED TO DRIVE A ROBUST 25% CAGR IN ADJ. PAT



Source: Company, BOBCAPS Research

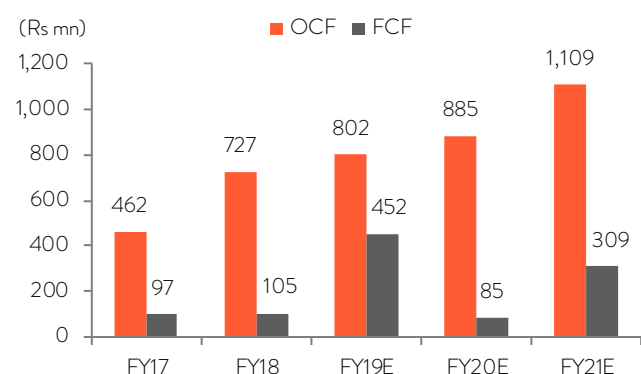
Capex plan to cap FCF, return ratios healthy

Rs 4bn of capex to result in lower FCF in FY20

TCIEXP plans to spend Rs 4bn over five years (FY19-FY23) towards expanding its handling capacities at existing sorting centres, adding more sorting centres, and branch network expansion. Accordingly, we have factored in Rs 800mn of capex each in FY20 and FY21. While we expect the company to generate adequate operating cash flow to fund this capex, FCF generation is likely to be lower, especially in FY20.

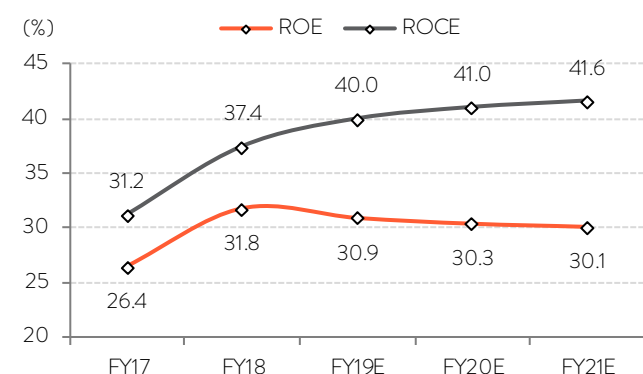
A higher share of company-owned sorting centres is likely to reduce the asset turnover ratio. Despite that, ROCE is projected to increase to 41.6% in FY21 from 37.4% in FY18, owing to higher operating margins. ROE, however, is estimated to be lower as we factor in debt repayment, leading to lower leverage.

FIG 30 – FCF GENERATION TO BE MUTED IN FY20



Source: Company, BOBCAPS Research

FIG 31 – ROCE EXPECTED TO IMPROVE



Source: Company, BOBCAPS Research

Valuation methodology

**Initiate coverage with BUY
and a Mar'20 TP of Rs 880
based on 30x forward P/E**

We value TCIEXP using the P/E methodology, assigning a multiple of 30x to FY21E EPS to arrive at our Mar'20 target price of Rs 880 (18% upside). Our multiple is at a discount to the one-year forward P/E multiple of 35x at which BDE currently trades. Initiate with BUY.

FIG 32 – KEY VALUATION ASSUMPTIONS

Rs per share	
FY21E EPS	29.4
P/E multiple applied (x)	30
Target price	880
Upside from CMP (%)	18.3

Source: BOBCAPS Research

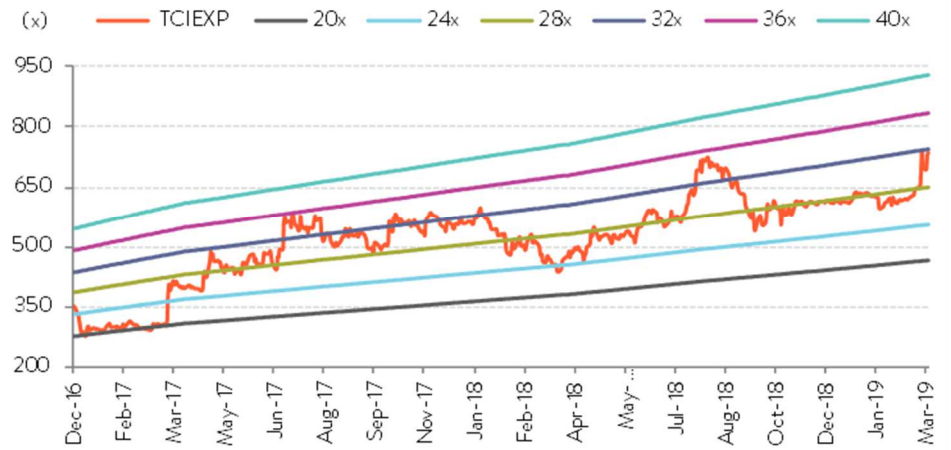
To capture the company's long-term earnings growth story, we have also done a DCF valuation by projecting FCF till FY30 and using a WACC of 12.5% to discount the cash flows generated over the forecast period. We arrive at a fair value of Rs 913 based on the DCF valuation method. Our key valuation assumptions are outlined below.

FIG 33 – KEY DCF ASSUMPTIONS

Assumptions	
Growth assumptions – FY19-FY30E (%)	
Revenue CAGR	13.8
EBITDA CAGR	18.6
Earnings CAGR	20.3
Other assumptions (%)	
First year of discounting	FY21
Cost of equity	12.5
WACC	12.8
Terminal growth rate	6.0
Terminal value contribution	67.0
Target price per share (Rs)	913

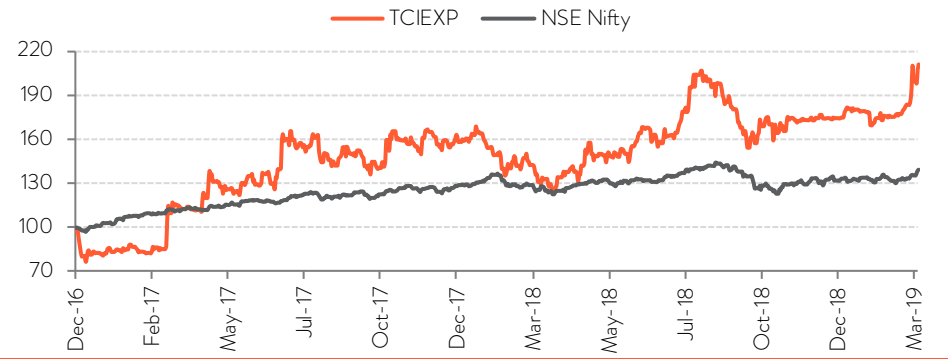
Source: BOBCAPS Research

FIG 34 – ONE-YEAR FORWARD P/E BAND CHART



Source: Bloomberg, BOBCAPS Research

FIG 35 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- **Lower capacity utilisation:** Deviating slightly from its erstwhile asset-light strategy, TCIEXP plans to own a majority of the sorting centres planned over the next few years. If the company is unable to ramp up utilisation at these new facilities to the desired 70-80% levels, it would impact revenue growth and operating margins (due to higher operating leverage in owned assets), leading to a shortfall in our estimates.
- **Prolonged economic slowdown:** The express industry's fortunes are closely linked with economic and industrial activity. Any prolonged economic slowdown would therefore affect the company's growth prospects.
- **Acute price competition:** Cost effectiveness remains a key decision-making parameter for some institutional customers, along with reliability of services. In case any leading industry incumbent or new entrant capable of delivering reliable services decides to cut pricing, it may drive down industry-wide pricing, impacting the company's operating performance.
- **Downturn in key industry verticals:** Any downturn in TCIEXP's key verticals – automobiles and pharmaceuticals, together ~25% of revenue – is likely to have a substantial impact on its operating performance, and therefore poses a risk to our estimates.
- **Increase in competitive intensity:** The company faces competition from large national players, Indian entities of large international players, and smaller regional players. Moreover, the entry of new-age players aiming to disrupt the logistics industry based on technology also poses a threat. Any increase in competitive intensity can draw market share away from the company, posing a downside risk to our estimates.

Management overview

FIG 36 – KEY MANAGEMENT PERSONNEL

Name	Brief profile
Mr. D. P. Agarwal Chairman and Director	Mr. D. P. Agarwal is the Chairman and Director of TCIEXP and also the Chairman and Managing Director of TRPC. Mr. Agarwal has been associated with the transport industry for more than 50 years. He is also a part of various associations including CII, FICCI and PHDCCI.
Mr. Chander Agarwal Managing Director	Mr. Chander Agarwal is the Managing Director of TCIEXP and a Director of TRPC. He holds a Bachelor of Science degree in Business Administration from Bryant College, Smithfield, USA. He has worked with Transfreight USA, a 3PL specialising in 'lean logistics' for Toyota Motor Vehicles, USA.
Mr. P. C. Sharma Chief Executive Officer and Whole Time Director	Mr. PC Sharma has been associated with the TCI Group since 1982. He started his career in TRPC as a trainee and currently heads TCIEXP. He holds a B. Com degree and has undergone executive training programs from IIM-A, Indian School of Business (ISB), XLRI Jamshedpur and is also an alumnus of Harvard Business School and National University of Singapore.
Mr. Mukti Agarwal Chief Financial Officer	Mr. Mukti Agarwal is the Chief Financial Officer of TCIEXP. He is a qualified Chartered Accountant and has been associated with TRPC in various capacities for the last 13 years. Pre-demerger, he was CFO-XPS at TRPC.
Mr. Manish Jain Sales, Marketing & Corporate Communication	Mr. Manish Jain is a management graduate with 20 years of logistics/express industry expertise. He currently heads the sales and marketing division for TCIEXP.

Source: Company, BOBCAPS Research

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Total revenue	7,503	8,851	10,484	12,310	14,454
EBITDA	619	907	1,196	1,472	1,828
EBIT	576	854	1,131	1,387	1,716
Net interest income/(expenses)	(24)	(38)	(44)	(40)	(37)
Other income/(expenses)	14	21	27	38	39
Exceptional items	0	0	0	0	0
EBT	565	838	1,114	1,385	1,718
Income taxes	190	254	390	485	593
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	375	584	724	900	1,125
Adjustments	0	0	0	0	0
Adjusted net profit	375	584	724	900	1,125

Balance Sheet

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Accounts payables	372	646	862	1,012	1,188
Other current liabilities	91	240	284	334	392
Provisions	24	35	41	49	57
Debt funds	316	407	390	340	340
Other liabilities	0	0	0	0	0
Equity capital	77	77	77	77	77
Reserves & surplus	1,531	1,992	2,546	3,236	4,098
Shareholders' fund	1,608	2,068	2,623	3,313	4,175
Total liabilities and equities	2,411	3,395	4,200	5,047	6,152
Cash and cash eq.	88	122	344	128	137
Accounts receivables	1,131	1,544	1,829	2,147	2,521
Inventories	0	0	0	0	0
Other current assets	126	101	105	123	145
Investments	0	0	0	0	0
Net fixed assets	955	1,602	1,887	2,602	3,291
CWIP	79	0	0	0	0
Intangible assets	16	18	18	18	18
Deferred tax assets, net	(34)	(43)	(43)	(43)	(43)
Other assets	50	52	61	72	84
Total assets	2,411	3,395	4,200	5,047	6,152

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Net income + Depreciation	418	636	790	985	1,237
Interest expenses	24	38	44	40	37
Non-cash adjustments	10	9	0	0	0
Changes in working capital	9	44	(31)	(141)	(165)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	462	727	802	885	1,109
Capital expenditures	(365)	(622)	(350)	(800)	(800)
Change in investments	0	0	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(365)	(622)	(350)	(800)	(800)
Equities issued/Others	1	0	0	0	0
Debt raised/repaid	(97)	90	(17)	(50)	0
Interest expenses	(24)	(38)	(44)	(40)	(37)
Dividends paid	(37)	(129)	(169)	(211)	(263)
Other financing cash flows	39	5	0	0	0
Cash flow from financing	(118)	(71)	(230)	(301)	(301)
Changes in cash and cash eq.	(21)	34	222	(216)	9
Closing cash and cash eq.	88	122	344	128	137

Per Share

Y/E 31 Mar (Rs)	FY17A	FY18A	FY19E	FY20E	FY21E
Reported EPS	9.8	15.3	18.9	23.5	29.4
Adjusted EPS	9.8	15.3	18.9	23.5	29.4
Dividend per share	0.8	2.8	3.8	4.7	5.9
Book value per share	42.0	54.0	68.5	86.5	109.0

Valuations Ratios

Y/E 31 Mar (x)	FY17A	FY18A	FY19E	FY20E	FY21E
EV/Sales	3.8	3.2	2.7	2.3	2.0
EV/EBITDA	46.5	31.7	24.0	19.4	15.7
Adjusted P/E	76.0	48.8	39.3	31.6	25.3
P/BV	17.7	13.8	10.9	8.6	6.8

DuPont Analysis

Y/E 31 Mar (%)	FY17A	FY18A	FY19E	FY20E	FY21E
Tax burden (Net profit/PBT)	66.3	69.7	65.0	65.0	65.5
Interest burden (PBT/EBIT)	98.1	98.0	98.6	99.9	100.1
EBIT margin (EBIT/Revenue)	7.7	9.7	10.8	11.3	11.9
Asset turnover (Revenue/Avg TA)	4.1	4.0	3.8	3.6	3.5
Leverage (Avg TA/Avg Equity)	1.3	1.2	1.2	1.1	1.1
Adjusted ROAE	26.4	31.8	30.9	30.3	30.1

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY17A	FY18A	FY19E	FY20E	FY21E
YoY growth (%)					
Revenue	13.1	18.0	18.5	17.4	17.4
EBITDA	13.8	46.5	31.9	23.1	24.2
Adjusted EPS	32.7	55.8	24.0	24.3	25.0
Profitability & Return ratios (%)					
EBITDA margin	8.3	10.2	11.4	12.0	12.6
EBIT margin	7.7	9.7	10.8	11.3	11.9
Adjusted profit margin	5.0	6.6	6.9	7.3	7.8
Adjusted ROAE	26.4	31.8	30.9	30.3	30.1
ROCE	31.2	37.4	40.0	41.0	41.6
Working capital days (days)					
Receivables	55	64	64	64	64
Inventory	0	0	0	0	0
Payables	20	30	34	34	34
Ratios (x)					
Gross asset turnover	7.8	6.1	5.4	4.9	4.3
Current ratio	2.8	1.9	1.9	1.7	1.7
Net interest coverage ratio	23.6	22.7	25.8	34.5	45.9
Adjusted debt/equity	0.1	0.1	0.0	0.1	0.0

Source: Company, BOBCAPS Research

BUY

TP: Rs 365 | ▲ 26%

**TRANSPORT CORP OF
INDIA**

| Logistics

| 14 March 2019

Scaling up the value chain – initiate with BUY

Transport Corporation of India (TRPC), a leading multi-modal logistics company, is witnessing secular growth across segments and improvement in business mix with a rising share of the high-margin supply chain, seaways and LTL businesses. This has driven a strong EBITDA/EPS CAGR of 28%/48% over FY16-FY18; the outlook over FY19-FY21 remains healthy at 17%/16% CAGR as we expect these trends to sustain. We initiate coverage with BUY and a Mar'20 SOTP-based target price of Rs 365, implying 26% upside.

Sayan Das Sharma | Rohan Korde

research@bobcaps.in

Moving up the value chain: A growing revenue share of higher margin segments – supply chain (+200bps), seaways (+300bps) and LTL in freight – has helped TRPC move up the logistics value chain, translating into 160bps EBITDA margin expansion over FY16-FY18. We expect the business mix to improve further driven by the supply chain and LTL businesses, catalysing a sustained uptrend in EBITDA margin/ROCE profile (+60bps/130bps over FY19-FY21).

Industry tailwinds to boost supply chain/3PL segment: Leveraging its early-mover advantage, TRPC has established strong credentials in the domestic 3PL industry, especially in the auto vertical. Robust long-term industry prospects (17-18% CAGR) coupled with established positioning bodes well for the company – we build in a 15%/20% CAGR in segmental revenue/EBITDA over FY19-FY21.

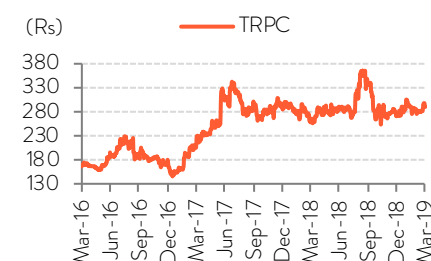
LTL uptick positive for freight segment: The rising LTL share is a major positive due to its >2x margin advantage over FTL and lower receivable days. We expect this to steer a 13%/16% revenue/EBITDA CAGR in freight over FY19-FY21.

Initiate with BUY: Our SOTP valuation comprises target FY21E EV/EBITDA multiples of 6x/10x/7x for the freight/supply chain/seaways businesses, yielding a Mar'20 TP of Rs 365 – an implied one-year forward P/E of 14x.

Ticker/Price	TRPC IN/Rs 291
Market cap	US\$ 320.1mn
Shares o/s	77mn
3M ADV	US\$ 0.1mn
52wk high/low	Rs 330/Rs 260
Promoter/FPI/DII	67%/4%/8%

Source: NSE

STOCK PERFORMANCE



Source: NSE

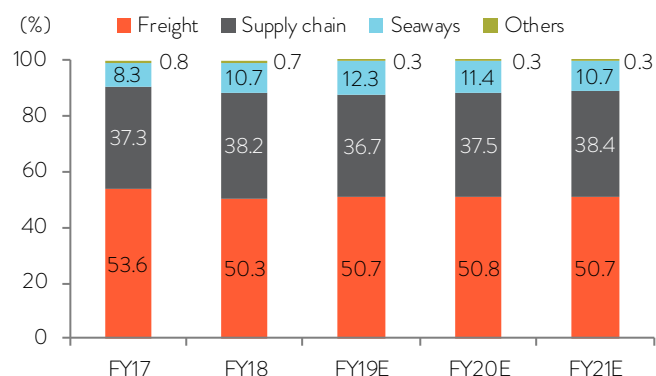
KEY FINANCIALS

Y/E 31 Mar	FY17A	FY18A	FY19E	FY20E	FY21E
Adj. net profit (Rs mn)	813	1,238	1,491	1,752	1,999
Adj. EPS (Rs)	10.6	16.2	19.5	22.9	26.1
Adj. EPS growth (%)	42.8	52.4	20.4	17.5	14.1
Adj. ROAE (%)	13.3	17.6	18.0	18.2	17.9
Adj. P/E (x)	27.4	18.0	14.9	12.7	11.1
EV/EBITDA (x)	15.6	12.2	11.0	9.5	8.2

Source: Company, BOBCAPS Research

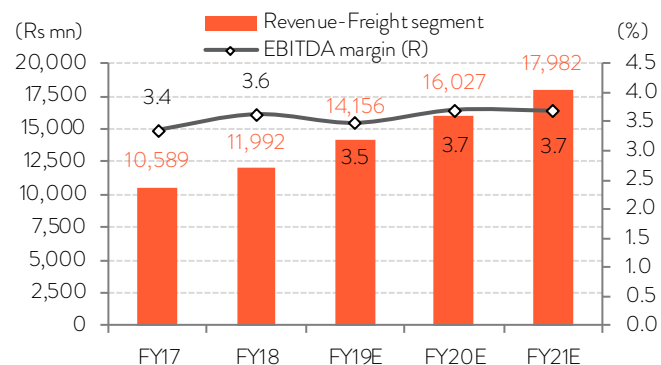
In a nutshell

FIG 1 – SHARE OF VALUE-ADDED SEGMENTS ON THE RISE



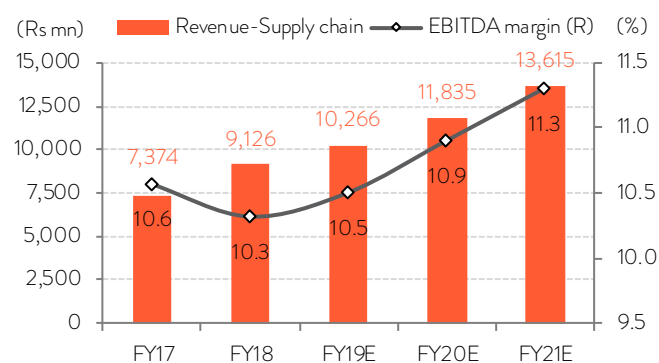
Source: Company, BOBCAPS Research

FIG 2 – RISING SHARE OF LTL EXPECTED TO DRIVE MARGIN EXPANSION IN FREIGHT SEGMENT



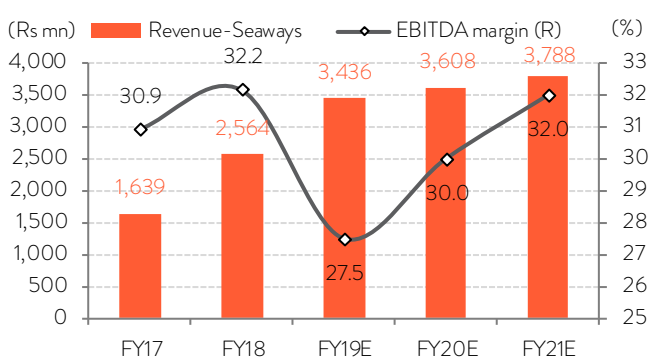
Source: Company, BOBCAPS Research

FIG 3 – SUPPLY CHAIN BUSINESS EXPECTED TO GROW AT 15% CAGR OVER FY19-FY21



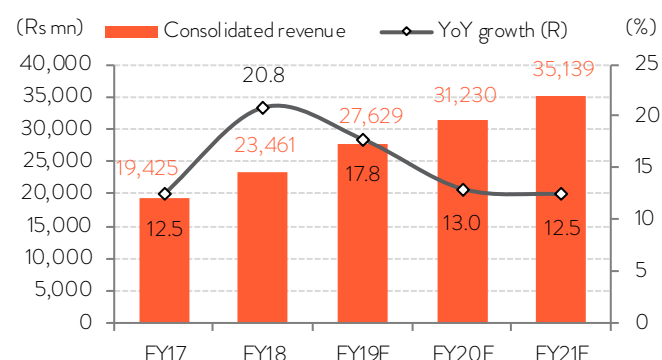
Source: Company, BOBCAPS Research

FIG 4 – SEAWAYS BUSINESS GROWTH TO REMAIN MUTED BUT MARGINS LIKELY TO EXPAND



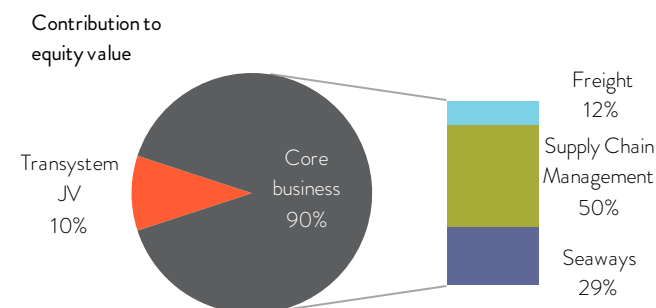
Source: Company, BOBCAPS Research

FIG 5 – CONSOLIDATED REVENUES FORECAST TO GROW AT 12.9% CAGR OVER FY19-FY21



Source: Company, BOBCAPS Research

FIG 6 – SUPPLY CHAIN DIVISION TO BE THE KEY VALUATION DRIVER



Source: Company, BOBCAPS Research

Investment rationale

Scaling up the logistics value chain

Over the past few years, TRPC has been steadily moving up the logistics value chain with a focus on the supply chain and seaways segments, which have higher scope for value-addition than road freight transportation (mainly FTL). A higher revenue share from these businesses – supply chain (36% to 38%) and seaways (8% to 11%) along with LTL over FTL in freight – has helped TRPC clock 160bps EBITDA margin expansion over FY16-FY18, with scope for further gains ahead.

Rising contribution from high-value segments

EBITDA margin/ROCE rose 160bps/450bps over FY16-FY18 on higher supply chain, LTL and seaways contribution

Over FY16-FY18, TRPC's supply chain and seaways segments have posted a 20% and 35% revenue CAGR respectively, while the lower-margin freight segment has registered an 11% CAGR. Benefits of this enhanced business mix are visible from the company's margin and ROCE profile – EBITDA margins have expanded to 9.1% in FY18 from 7.5% in FY16, while ROCE has risen to 12.6% from 8.1%.

Additionally, within the freight segment, the share of high-margin LTL business (8-11% operating margin, vs. 2-4% in FTL) is on the rise, as claimed by the management (the company does not share absolute contribution of LTL in freight division). Consequently, EBITDA margins of the freight business have also expanded to 3.6% from 2.9% in FY16.

The following table depicts that supply chain, coastal shipping, and LTL industry segments typically generates higher EBITDA margin and ROCE than FTL.

FIG 7 – SUPPLY CHAIN, COASTAL SHIPPING, LTL INDUSTRIES ARE MORE PREMIUM THAN FTL

	Full-truck-load (FTL)	Less-than-truck-load (LTL)	Supply Chain Solutions	Coastal Shipping
Est. market size (Rs bn)	6,300	700	450-500	45-50
Industry structure	Fragmented; highly unorganised	Relatively less fragmented	Organised	Organised
Entry barriers	Low	High	Very High	High
Scope for value addition	Low	High	Very High	Moderate
Expected 5-yr CAGR	~5-8%	~10-12%	17-18%	12-14%
Avg. EBITDA margin	2-4%	8-11%	5-15%	25-35%
Avg. ROCE	8-10%	15-16%	25-30%	20-22%
TRPC's revenue contribution (FY16/FY18)	55%/50%		36%/38%	8/11%

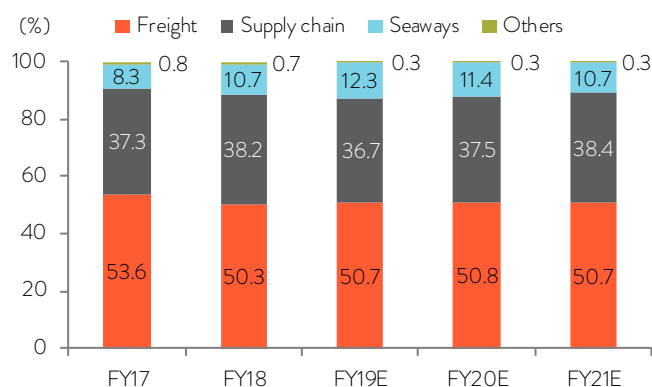
Source: Company, Industry, BOBCAPS Research

Expect sustained margin and ROCE gains ahead

Going forward, we expect similar trends – faster growth in supply chain and rising share of LTL in the freight business – to continue, propelling further improvement in margin and ROCE profile. The supply chain business is forecast to grow at 15.2% CAGR over FY19-FY21, ahead of freight (12.7% CAGR).

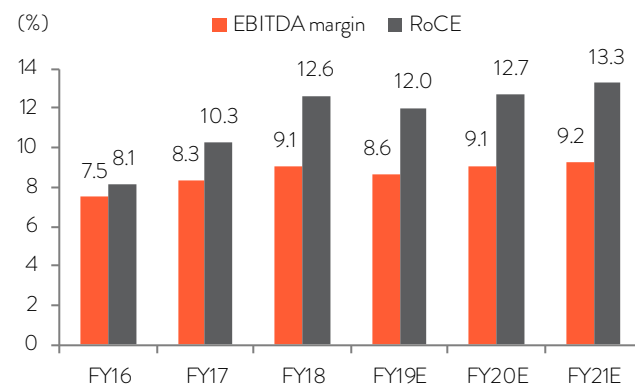
We expect both segments to see EBITDA margin expansion – 80bps to 11.3% for supply chain solutions over FY19-FY21 as new client accounts stabilise, and 20bps to 3.7% for the freight business owing to higher LTL contribution. Although seaways business growth is likely to be tepid at a 5% CAGR, we forecast stronger margins of 32% in FY21 from 27.5% in FY19. Buoyed by these factors, we expect TRPC's consolidated EBITDA margin/ROCE to increase 70bps/100bps over FY19-FY21.

FIG 8 – SHARE OF VALUE-ADDED BUSINESSES GOING UP STEADILY...



Source: Company, BOBCAPS Research

FIG 9 – ...DRIVING SUSTAINED UPTREND IN MARGINS AND ROCE



Source: Company, BOBCAPS Research

Integrated, multi-modal transport solution provider

With a presence across road freight, coastal shipping and rail, TRPC is one of the few players in India with end-to-end multi-modal transport capabilities and a pan-India reach. This enables the company to offer seamless and efficient movement of goods along with a wide breadth of logistics services.

Flexible multi-modal offerings...

In the road freight segment, TRPC has access to 3,500 trucks and trailers, 700 branches and 25 hubs; in seaways, it has 6 cargo ships with ~64,000dwt (deadweight tonnage) capacity; and also, container rail connectivity through a joint venture with Container Corporation of India (CCRI)– TCI Concor Multimodal Solutions Pvt. Ltd. (subsidiary of TRPC). Multi-modal capabilities along with a wide reach enable the company to offer flexible and optimum transport solutions to clients.

FIG 10 – MULTI-MODAL CAPABILITIES


Source: Company, BOBCAPS Research

...complemented by diversified service solutions

Through its three operating divisions – road freight, supply chain solutions and seaways – TRPC offers a whole gamut of logistics services to customers. This includes (1) FTL, LTL and over-dimensional cargo transportation in the freight business, (2) 3PL services through supply chain division, and (3) coastal shipping, freight forwarding (NVOCC) and project cargo in seaways. This diversified service offering complements its multi-modal capabilities and also places the company favourably to capitalise on opportunities arising in various segments of the Indian logistics industry.

FIG 11 – TRPC BUSINESS SNAPSHOT

(Rs mn)	Services offered	FY18 revenue (share in total)	FY18 EBIT (share in total)	EBIT margin (%)	ROCE (%)
Freight	Full truck load (FTL); less-than truck load (LTL); over-dimensional cargo transport	11,992 (50%)	336 (21%)	2.8	13.6
Supply Chain	Contract logistics/third-party logistics (3PL) services including warehousing, transportation and distribution, value-added services	9,126 (38%)	605 (38%)	6.6	21.6
Seaways	Coastal shipping, non-vessel owned common carrier (NVOCC), and project cargo	2,564 (11%)	591 (37%)	23.1	19.6
Energy & un-allocable	-	179 (1%)	79 (5%)	NM	1.9
Total	-	23,861*	1,611	6.9	14.2

Source: Company, BOBCAPS Research | *Consolidated revenue before inter-segment revenue adjustments; segmental revenue and EBIT include other income

Freight: Growing LTL business augurs well

With a wide fleet and office network, TRPC is one of the largest organised road freight transporters in India. The company's LTL segment has been growing faster than the FTL segment over the past two years, a major positive due to its >2x margins over FTL and lower receivable days. We expect a growing LTL share in the revenue mix to drive a 16% EBITDA CAGR in the freight business over FY19-FY21.

LTL a key margin driver

Traditionally a strong player in the FTL segment, TRPC has focused on enhancing the share of LTL by tapping a higher number of SME customers, in recent years. According to the company, this strategy has led to faster growth in LTL over FTL segment over the past two years (albeit it does not yet share specific information pertaining to LTL's contribution to the freight segment). This has translated into a healthy revenue/EBITDA CAGR of 11.1%/23.7% for the freight division over FY16-FY18. This momentum sustained in 9MFY19 as well, with 20.5% YoY revenue growth while EBIT margins expanded by 10bps.

We view the growing mix of LTL business as a key positive given that (1) organised players have a natural advantage in LTL as it requires the presence of distribution hubs and a wider geographic footprint, (2) margins are higher than FTL (8-11% vs. 2-4%), and (3) a more fragmented, smaller clientele leads to lower receivable days than FTL.

Margin and ROCE gap versus peers to narrow

A comparison of EBITDA margins for the three leading road freight operators shows that VRL Logistics (VRL) scores far above peers with margins ~3x that of DARCL Logistics and ~5x that of TRPC, due to a higher LTL share (~90% of revenue) and majority owned fleet. The difference in margins between DARCL and TRPC can be attributed largely to the owned vs. hired vehicle mix.

Owing to lower margins, TRPC's ROCE is much lower than peers despite a higher asset turn that stems from an asset-light model (however, we note EBITDA margins/ROCE have improved to 3.6%/13.6% in FY18). With TRPC's LTL share rising faster, as reflected in faster revenue/EBITDA growth than peers, the margin and ROCE gap should narrow.

LTL has 2-3x higher operating margins and lower receivable days vs. FTL

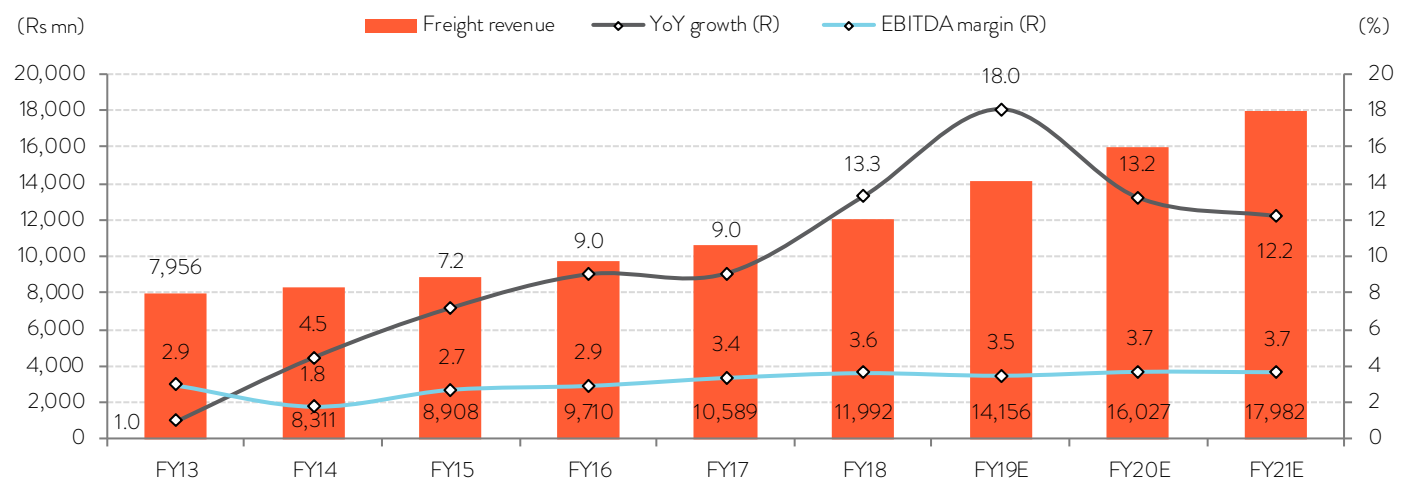
FIG 12 – COMPETITIVE LANDSCAPE OF TRPC'S ROAD FREIGHT* SEGMENT

(Rs mn)	TRPC	VRLL	DARCL (unlisted)
Business focus	Higher share of FTL, but share of LTL is increasing steadily	LTL accounts for ~90% of total revenue	Primarily FTL
Fleet details	3,500 vehicles, of which 120 are owned	~4,000 owned vehicles	700 owned, ~10,000 associated vehicles**
Geographic presence	700 offices and 25 strategic hubs across India	950+ branch and franchise offices across India; especially strong presence in West and South India	~200 offices
Revenue CAGR (FY15- FY18) (%)	10.4	5.5	2.7
EBITDA CAGR (FY15- FY18) (%)	21.8	(3.7)	(7.3)
Average EBITDA margin (FY15- FY18) (%)	3.2	13.8	5.1
Average asset turn (FY15- FY18) (x)	4.1	2.8	3.6
Average ROCE (FY15- FY18) (%)	9.8	32.7	15.5

Source: Company, BOBCAPS Research | *Freight business details for TRPC; goods transport business details for VRL, and standalone road freight business for DARCL | **Fleet under operations would be lower

Freight segment expected to grow at 12.7% CAGR

Rising share of LTL and established market positioning should continue to aid growth of the freight segment going ahead. We forecast 12.7%/15.9% CAGR in revenue/EBITDA over FY19- FY21.

FIG 13 – FREIGHT REVENUE AND MARGIN MOMENTUM TO SUSTAIN OVER FY19-FY21


Source: Company, BOBCAPS Research

Supply chain business: Riding on the industry wave

Leveraging its early-mover advantage, TRPC has established strong credentials in the domestic 3PL industry, especially auto. Robust long-term industry prospects (17-18% CAGR) coupled with established positioning are expected to support a 15%/20% CAGR in revenue/EBITDA for the supply chain business over FY19- FY21.

Strong positioning in 3PL industry

Auto the mainstay (~70% revenue contribution); also caters to retail, consumer, chemicals, and e-commerce

As one of the earliest incumbents of the Indian 3PL industry, TRPC has carved a niche for itself over the past two decades. Leveraging its first-mover advantage, it has developed a strong clientele and wide service suite, especially in the auto sector which is the mainstay of the business (~70% contribution to segment revenue). Apart from auto, TRPC also caters to the retail and consumer products, chemicals, and e-commerce industries.

The company currently manages 12mn sq ft of warehousing space spanning the country and has a fleet of 4,000 trucks (1,350 owned). TRPC's strong market positioning is even more impressive considering that it was achieved without any anchor customers, unlike most other companies operating in this space.

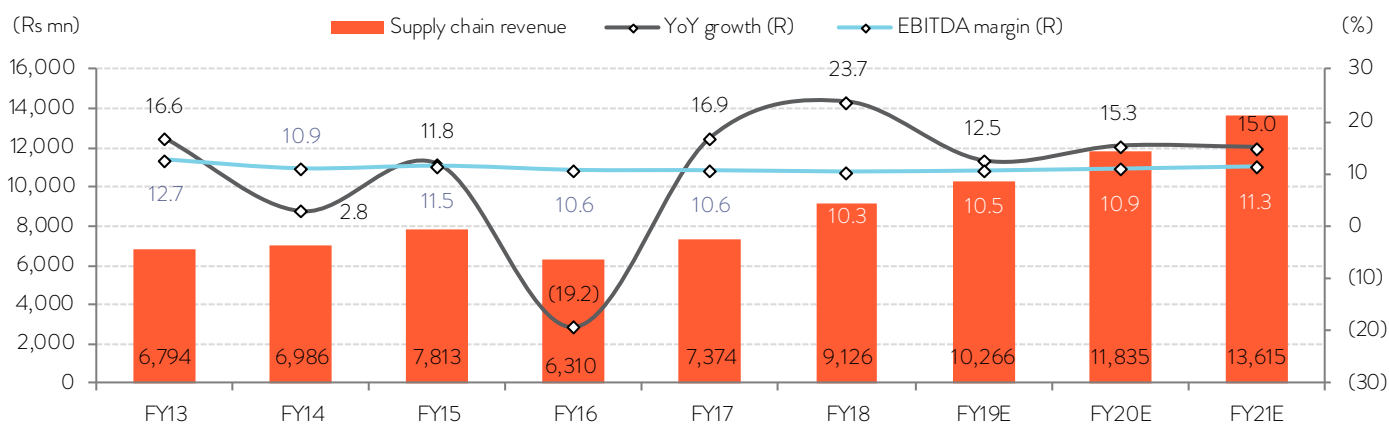
Expect healthy revenue and EBITDA growth ahead

The company's supply chain segment grew at a relatively tepid 6% CAGR over FY11-FY16. However, growth bounced back to a strong 20% CAGR over FY16-FY18 aided by client wins and an increasing trend of outsourcing logistics activities. In 9MFY19, growth moderated slightly to 12.7% YoY, owing to delayed onset of festival seasons and Kerala floods. According to management, the contract pipeline is strong, especially in the FMCG, e-commerce fulfilment and auto space, which should augment volume growth.

Supply chain revenue/ EBITDA projected to grow at 15%/20% over FY19-FY21

We expect TRPC to be a key beneficiary of the expected 3PL industry growth in India (17-18% CAGR; detailed outlook in our industry chapter), owing to its (1) established execution track record in complex supply chain management for auto OEMs; (2) two decades of expertise in the supply chain industry; and (3) pan-India presence. We build in a CAGR of 15% over FY19-FY21 for the segment, lower than the previous two-year period, factoring in some impact from slowdown in the automotive industry. Consequently, we expect segmental EBITDA to grow at 20% CAGR during the same period.

FIG 14 – SUPPLY CHAIN SEGMENT EXPECTED TO GROW AT A 15% CAGR OVER FY19-FY21



Source: Company, BOBCAPS Research

FIG 15 – VERTICAL WISE OPPORTUNITY IN THE 3PL SPACE

Verticals	Est. 3PL market size (Rs bn)		CAGR (%)
	FY18	FY21E	
Auto & auto comps	290-300	450-470	15-16
E-commerce	80-85	180-185	30-31
Consumer durables and FMCG	25-27	50-52	25
Organised retail	35-40	75-80	25-30

Source: CRISIL Research, BOBCAPS Research

Seaways: Right place, right time

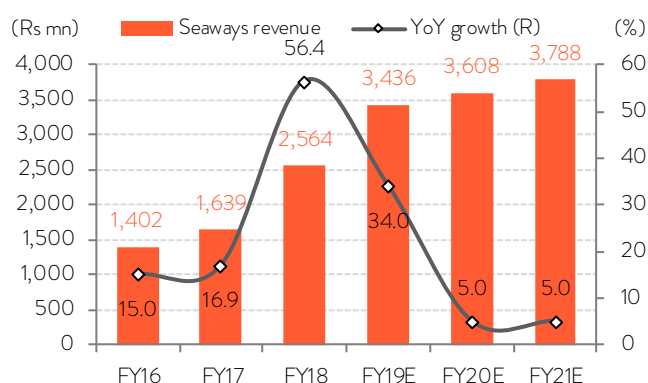
With a fleet of six ships – three each operating on the western and eastern coasts – aggregating ~64,000dwt of capacity, TRPC is a prominent player in the Indian coastal shipping industry. It mainly carries container cargo along the western coast between Mundra and Kochi, and bulk cargo on the eastern coast to Port Blair in the Andaman and Nicobar Islands. In our view, TRPC is well placed to be a prime beneficiary of healthy activity in the Indian coastal shipping and inland waterways sector.

Increasing utilisation to boost margins

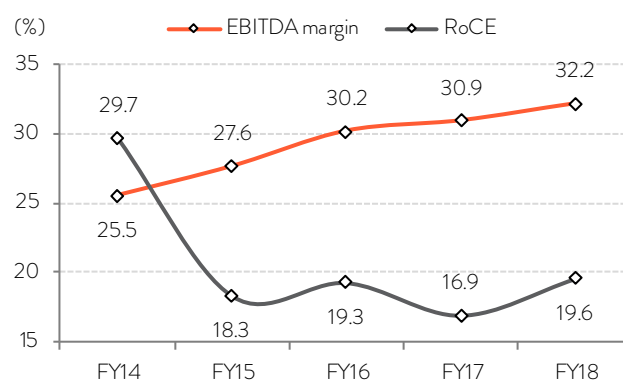
Addition of ships drove sturdy revenue/EBITDA CAGR of 35%/40% over FY16-FY18

The seaways segment has posted a healthy revenue/EBITDA CAGR of 35%/40% over FY16-FY18 driven by the addition of one ship which started operating in FY18. Revenue growth in 9MFY19 has also remained strong at 38%, aided by the addition of one ship in Q2FY19 and higher utilisation of the existing fleet (container utilisation stands at 55-60% at present).

Going ahead, the company plans to add one more ship if internal EBITDA and ROCE targets are met. However, we have not factored in the same and hence expect a relatively sedate CAGR of 5% over FY19-FY21, driven mostly by higher utilisation. We expect EBITDA margins to remain strong at 30-32% aided by operating leverage benefits.

FIG 16 – SEAWAYS REVENUE HAS GROWN SHARPLY AIDED BY SHIP ADDITION

Source: Company, BOBCAPS Research

FIG 17 – HAS GENERATED ROBUST EBITDA MARGIN AND ROCE

Source: Company, BOBCAPS Research

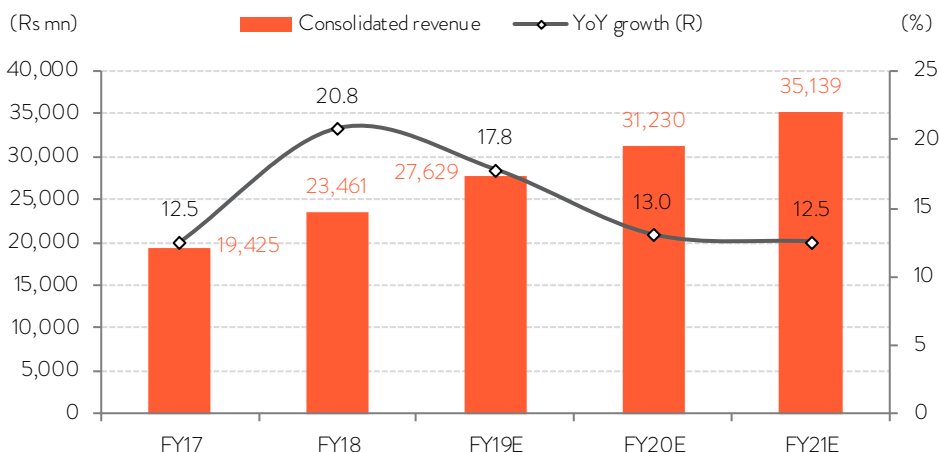
Financial review

Revenue CAGR of 12.8% forecast over FY19-FY21

Supply chain (15.2% CAGR) and freight (12.7% CAGR) to drive consolidated revenue

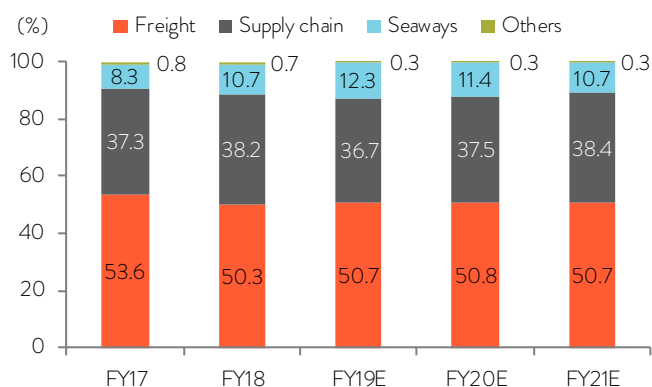
We expect TRPC to log a consolidated revenue CAGR of 12.8% over FY19-FY21, driven by the freight (12.7% CAGR) and supply chain (15.2%) segments, while seaways (5%) grows at a slower pace, assuming no fleet additions. Consequently, the supply chain business is expected to increase its share by 170bps to 38.4%, while freight rises remains flat at 50.7%. Although revenue share of the seaways business is likely to come down, its EBITDA contribution is expected to remain substantial at 37%.

FIG 18 – REVENUE TO GROW AT 12.8% CAGR OVER FY19-FY21E



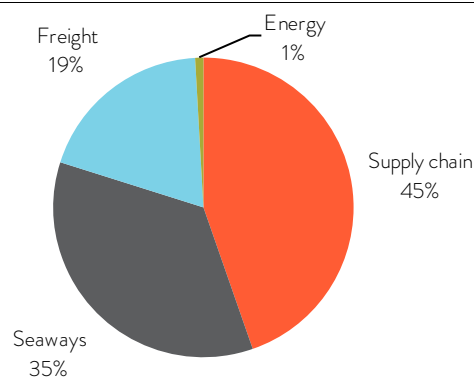
Source: Company, BOBCAPS Research

FIG 19 – REVENUE SHARE OF SUPPLY CHAIN BUSINESSES TO INCREASE



Source: Company, BOBCAPS Research

FIG 20 – SEAWAYS, SUPPLY CHAIN SEGMENTS TO CONTINUE TO ACCOUNT FOR MAJORITY OF EBITDA



Source: Company, BOBCAPS Research

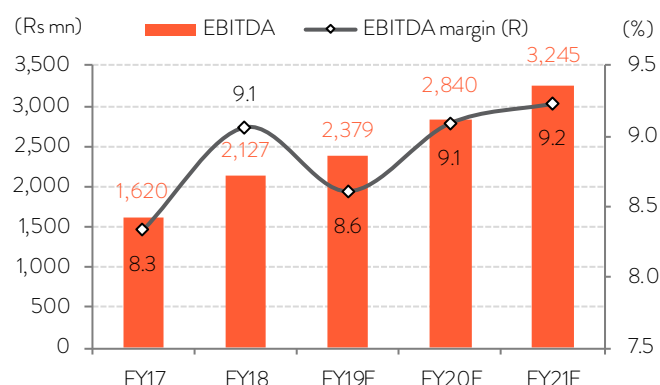
EBITDA margins to expand steadily

Project EBITDA margin expansion of 60bps over FY19-FY21

A temporary blip in FY19 notwithstanding, we expect TRPC's EBITDA margin to expand 60bps over FY19-FY21 to 9.2%. Margin expansion is expected across segments – a rising LTL share is projected to aid higher freight margins of 3.7% in FY21 from 3.5% in FY19, while supply chain solutions and seaways are likely to witness 80bps and 250bps expansion respectively. Accordingly, we project a 16.8% EBITDA CAGR for the company over FY19-FY21. PAT is expected to grow at a slightly lower CAGR of 15.8%.

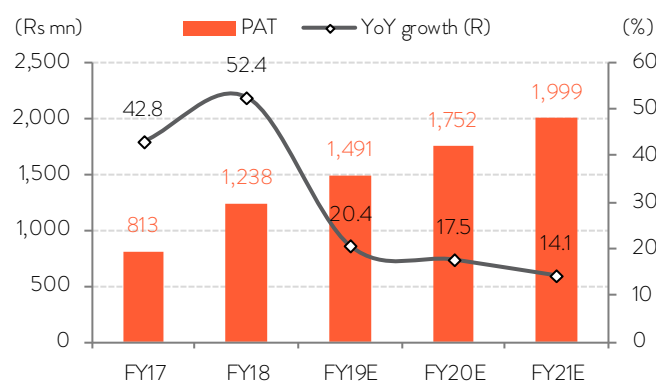
Relatively lower growth in PAT over EBITDA is attributed to slower growth expected in TRPC's joint venture – Transystem Logistics International – with Mitsui of Japan. This JV provides end-to-end logistics services to Toyota Kirloskar Motors (recently started providing services to other Japanese auto OEMs); we forecast in a 7% earnings CAGR over FY19-FY21, factoring in a potential demand slowdown for passenger vehicles.

FIG 21 – EBITDA MARGIN TO EXPAND 60BPS OVER FY19-FY21E



Source: Company, BOBCAPS Research

FIG 22 – PAT ESTIMATED TO GROW AT 15.8% CAGR



Source: Company, BOBCAPS Research

FCFF generation and return ratios to remain healthy

TRPC has generated positive FCFF in six of the seven preceding financial years, owing to healthy operating cash generation and moderate capex. EBITDA margin expansion of 160bps, coupled with higher gross asset turnover (3.4x from 2.5x) has translated into better return ratios over FY16-18 – ROE/ROCE have improved to 17.6%/12.6% in FY18 from 9.5%/8.1% in FY16.

We forecast healthy FCFF generation over FY20-FY21 led by higher EBITDA and a steady working capital cycle. ROCE is also expected to improve to 13.3% in FY21 from 12% in FY19, driven by higher EBIT margins (6.1% from 5.7%).

Valuation methodology

**Initiate coverage with BUY
and an SOTP-based Mar'20
TP of Rs 365**

We have a Mar'20 target price of Rs 365 for TRPC arrived at using the sum-of-the-parts (SOTP) methodology, as follows:

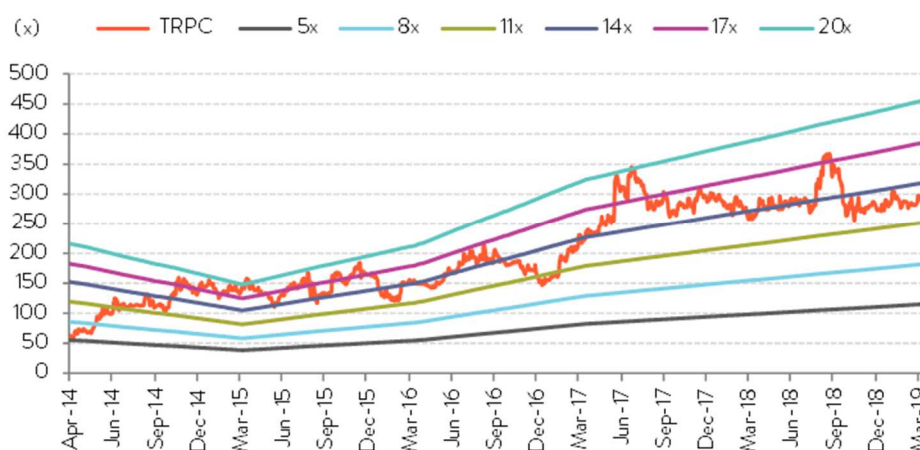
- Freight business valued at 6x FY21E EV/EBITDA, a ~25% discount to VRL Logistics, factoring in a lower margin and ROCE profile;
- Supply chain solutions business valued at 10x FY21E EV/EBITDA, a discount to our implied multiple assigned to Mahindra Logistics (17x) and Future Supply (13x), due to the absence of an anchor customer and a slower track record of growth;
- Seaways segment valued at 7x FY21E EV/EBITDA, based on its margin and ROCE profile; and
- Transystem JV valued at 10x FY21E EPS, a significant discount to other auto-focused 3PL players owing to its privately held status, customer concentration risk and comparatively weak financial performance.

Our target price of Rs 365 carries 26% upside and implies a P/E multiple of 16x/14x on FY20E/FY21E EPS. Initiate with BUY.

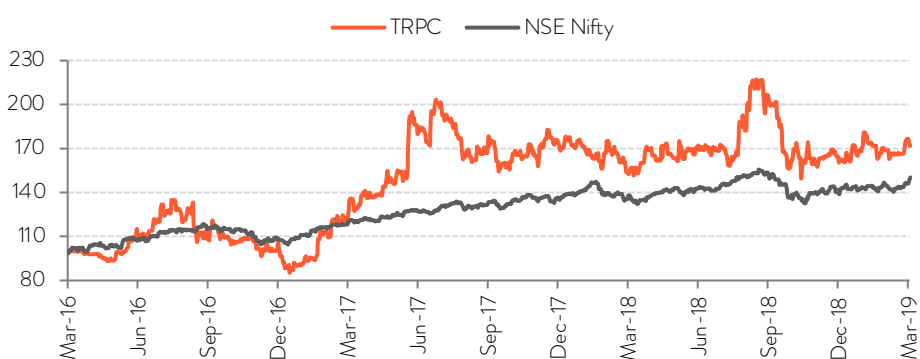
FIG 23 – KEY VALUATION ASSUMPTIONS

Segment-wise valuation	(Rs mn)
Freight segment	
FY21E EBITDA	662
EV/EBITDA multiple applied (x)	6.0
Total EV for the segment	3,971
Supply chain segment	
FY21E EBITDA	1,538
EV/EBITDA multiple applied (x)	10.0
Total EV for the segment	15,385
Seaways segment	
FY21E EBITDA	1,212
EV/EBITDA multiple applied (x)	7.0
Total EV for the segment	8,486
Total EV of the consolidated business (ex. JV)	27,841
FY20E net debt	3,295
Equity value of the consolidated business (ex. JV)	24,546
FY21E EPS of Transystem Logistics	661
P/E multiple applied (x)	10.0
Fair value of Transystem Logistics	6,610
Share of TRPC (%)	49
Valuation attributed to TRPC	3,239
Total equity value including JV	27,785
No. of shares	76.6
Target price	365

Source: Company, BOBCAPS Research

FIG 24 – ONE-YEAR FORWARD P/E BAND

Source: Bloomberg, BOBCAPS Research

FIG 25 – RELATIVE STOCK PERFORMANCE

Source: NSE

Key risks

- **Sharp rise in crude oil prices:** Given the time lag between fuel price increases and pass-along of the burden to customers, a sharp rally in crude price may intermittently affect margins.
- **Prolonged downturn in auto industry:** Auto OEMs remain the mainstay for the supply chain business with ~70% revenue contribution. This exposes the company's operations to inherent cyclicality of the automotive industry. Owing to a diverse client base – two-wheelers, passenger vehicles, commercial vehicles, tractors and construction equipment; as well as export and aftermarket – TRPC is well poised to combat sectoral headwinds. However, a prolonged downturn in the auto industry can adversely affect operating performance.
- **High client attrition:** While we note that customer churn rates have been low in the past, retention of key client accounts remains critical for sustainability of the supply chain business.

Management overview

FIG 26 – KEY MANAGEMENT PERSONNEL

Name	Brief profile
Mr. D. P. Agarwal Vice Chairman and Managing Director	Mr. D P Agarwal is the Vice-Chairman and Managing Director of TRPC. Mr. Agarwal has been associated with the transport industry for more than 50 years. Mr. Agarwal is also associated with various Chambers of Commerce including CII, FICCI & PHDCCI.
Mr. Vineet Agarwal Managing Director	Mr. Vineet Agarwal is the Managing Director of TRPC. Mr. Agarwal joined TCI in 1996 as the Executive Director after completing his Bachelor of Science in Economics and Industrial Management from Carnegie Mellon University, USA & has held various finance and management roles within the company. Mr Agarwal initiated Transystem Logistics International, a JV between TI and Mitsui & Co, Japan for the complete logistics management of Toyota Kirloskar Motors in India. He has played a key role in orienting the organization to move from being a mere trucking company to evolve as one of Asia's foremost integrated supply chain solutions provider.
Mr. Chander Agarwal Director	Mr. Chander Agarwal is the Director of TRPC. A Bachelor of Science in Business Administration from 1996 to 2001 from Bryant College, Smithfield, RI, Mr. Agarwal joined TRPC as Summer Intern and worked in various departments including operations, Logistics and Marketing etc. Currently he is spearheading Group TRPC's international expansion across Asia, Latin America & Africa. He is also the Managing Director of TCIEXP.
Mr. Ashish Tiwari Group CFO	Mr. Tiwari is the Group CFO of TRPC
Mr. Jasjit Sethi President and CEO – SCS	Mr. Sethi is the President and Chief Executive Officer of TRPC's Supply Chain Solutions division
Mr. IS Sigar CEO – Freight	Mr. Sigar is the Chief Executive Officer of TRPC's Freight division
Mr. R.U. Singh President and CEO – Seaways	Mr. Singh is the President and Chief Executive Officer of TCI Seaways division

Source: Company, BOBCAPS Research

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Total revenue	19,425	23,461	27,629	31,230	35,139
EBITDA	1,620	2,127	2,379	2,840	3,245
EBIT	1,028	1,441	1,580	1,878	2,141
Net interest income/(expenses)	(301)	(322)	(362)	(386)	(370)
Other income/(expenses)	122	182	310	332	349
Exceptional items	0	0	0	0	0
EBT	849	1,301	1,529	1,823	2,120
Income taxes	(191)	(287)	(321)	(383)	(445)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	155	224	283	312	324
Reported net profit	813	1,238	1,491	1,752	1,999
Adjustments	0	0	0	0	0
Adjusted net profit	813	1,238	1,491	1,752	1,999

Balance Sheet

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Accounts payables	357	597	725	815	916
Other current liabilities	1,165	1,245	1,514	1,711	1,925
Provisions	53	55	65	74	83
Debt funds	3,815	3,971	4,771	4,571	4,371
Other liabilities	0	0	0	0	0
Equity capital	153	153	153	153	153
Reserves & surplus	6,355	7,511	8,823	10,258	11,896
Shareholders' fund	6,508	7,664	8,976	10,411	12,049
Total liabilities and equities	11,900	13,533	16,051	17,582	19,344
Cash and cash eq.	187	142	124	232	379
Accounts receivables	3,584	4,249	5,601	5,989	6,739
Inventories	25	33	39	44	50
Other current assets	953	1,198	1,411	1,595	1,794
Investments	866	1,044	1,044	1,044	1,044
Net fixed assets	5,410	6,252	7,817	8,604	9,251
CWIP	568	563	0	0	0
Intangible assets	7	6	6	6	6
Deferred tax assets, net	(395)	(445)	(445)	(445)	(445)
Other assets	694	491	454	513	527
Total assets	11,900	13,533	16,051	17,582	19,344

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Net income + Depreciation	1,405	1,925	2,290	2,715	3,103
Interest expenses	301	322	362	386	370
Non-cash adjustments	72	50	0	0	0
Changes in working capital	(735)	(392)	(1,128)	(340)	(645)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	1,042	1,905	1,524	2,761	2,828
Capital expenditures	(1,130)	(1,523)	(1,800)	(1,750)	(1,750)
Change in investments	(106)	(177)	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(1,236)	(1,700)	(1,800)	(1,750)	(1,750)
Equities issued/Others	1	0	0	0	0
Debt raised/repaid	669	155	800	(200)	(200)
Interest expenses	(301)	(322)	(362)	(386)	(370)
Dividends paid	(84)	(123)	(180)	(317)	(361)
Other financing cash flows	(9)	40	0	0	0
Cash flow from financing	276	(249)	259	(903)	(931)
Changes in cash and cash eq.	81	(44)	(18)	108	146
Closing cash and cash eq.	187	142	124	232	379

Per Share

Y/E 31 Mar (Rs)	FY17A	FY18A	FY19E	FY20E	FY21E
Reported EPS	10.6	16.2	19.5	22.9	26.1
Adjusted EPS	10.6	16.2	19.5	22.9	26.1
Dividend per share	1.1	1.6	1.9	3.4	3.9
Book value per share	84.4	99.5	116.6	135.4	156.7

Valuations Ratios

Y/E 31 Mar (x)	FY17A	FY18A	FY19E	FY20E	FY21E
EV/Sales	1.3	1.1	0.9	0.9	0.8
EV/EBITDA	15.6	12.2	11.0	9.5	8.2
Adjusted P/E	27.4	18.0	14.9	12.7	11.1
P/BV	3.4	2.9	2.5	2.1	1.9

DuPont Analysis

Y/E 31 Mar (%)	FY17A	FY18A	FY19E	FY20E	FY21E
Tax burden (Net profit/PBT)	95.7	95.2	97.5	96.1	94.3
Interest burden (PBT/EBIT)	82.6	90.3	96.8	97.1	99.0
EBIT margin (EBIT/Revenue)	5.3	6.1	5.7	6.0	6.1
Asset turnover (Revenue/Avg TA)	1.9	2.1	2.1	2.1	2.2
Leverage (Avg TA/Avg Equity)	1.6	1.6	1.6	1.5	1.4
Adjusted ROAE	13.3	17.6	18.0	18.2	17.9

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY17A	FY18A	FY19E	FY20E	FY21E
YoY growth (%)					
Revenue	12.5	20.8	17.8	13.0	12.5
EBITDA	25.2	31.3	11.9	19.3	14.3
Adjusted EPS	42.8	52.4	20.4	17.5	14.1
Profitability & Return ratios (%)					
EBITDA margin	8.3	9.1	8.6	9.1	9.2
EBIT margin	5.3	6.1	5.7	6.0	6.1
Adjusted profit margin	4.2	5.3	5.4	5.6	5.7
Adjusted ROAE	13.3	17.6	18.0	18.2	17.9
ROCE	10.3	12.6	12.0	12.7	13.3
Working capital days (days)					
Receivables	69	67	66	74	70
Inventory	0	1	1	1	1
Payables	7	10	10	10	10
Ratios (x)					
Gross asset turnover	3.2	3.4	3.1	2.9	2.8
Current ratio	3.0	3.0	3.1	3.0	3.1
Net interest coverage ratio	3.4	4.5	4.4	4.9	5.8
Adjusted debt/equity	0.6	0.5	0.5	0.4	0.3

Source: Company, BOBCAPS Research

BUY

TP: Rs 130 | ▲ 16%

ALLCARGO LOGISTICS

Logistics

14 March 2019

Worst is behind – initiate with BUY

While a convergence of industry headwinds marred Allcargo Logistics' (AGLL) FY18 performance, the worst looks to be over as reflected in a growth rebound in 9MFY19 (+15% YoY). Market leadership and a diversified presence have helped the MTO business weather trade volatility, while the CFS segment is recovering after Kolkata facility launch and an ebbing impact of direct port delivery (DPD). We expect AGLL to post a healthy 13%/16% revenue/earnings CAGR over FY19-FY21 and initiate coverage with BUY for a Mar'20 target price of Rs 130.

Sayan Das Sharma | Rohan Korde

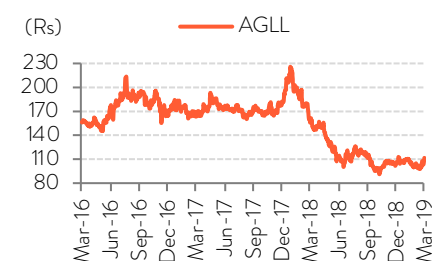
research@bobcaps.in

MTO – riding the storm: Escalating global trade tensions have cast a shadow over container trade, but we believe AGLL's multi-modal transport operations (MTO) business is well equipped to outpace global container trade (at 14.5% volume CAGR vs. ~4% CAGR over FY19-FY21E) due to (1) its leadership in the growing LCL segment, (2) presence across major trade lanes, and (3) strong FCL volumes. However, muted realisations are likely to cap revenue growth at 12.8% CAGR.

Ticker/Price	AGLL IN/Rs 112
Market cap	US\$ 397.0mn
Shares o/s	246mn
3M ADV	US\$ 0.2mn
52wk high/low	Rs 115/Rs 98
Promoter/FPI/DII	70%/4%/13%

Source: NSE

CFS – turning around: After a tumultuous phase, AGLL's container freight (CFS) segment has rebounded in 9MFY19 led by volume ramp-up in the Kolkata CFS (40% utilisation within a year of commission) and a plateauing share of DPD at JNPT. We expect the segment to grow in line with container traffic at major ports and forecast a volume/revenue CAGR of 11%/15% over FY19-FY21.

STOCK PERFORMANCE

Source: NSE

P&E – still a drag: Low returns from the asset-intensive project & engineering (P&E) segment, accentuated by cyclical downturn in end-user industries, is a major drag on consolidated ROCE. Demand revival from key end-user industries (we cautiously build in an 8% CAGR to FY21) could ease the pain.

Initiate with BUY: We initiate coverage on AGLL with BUY and a Mar'20 TP of Rs 130, valuing the core business at 11x one-year forward P/E (16% upside).

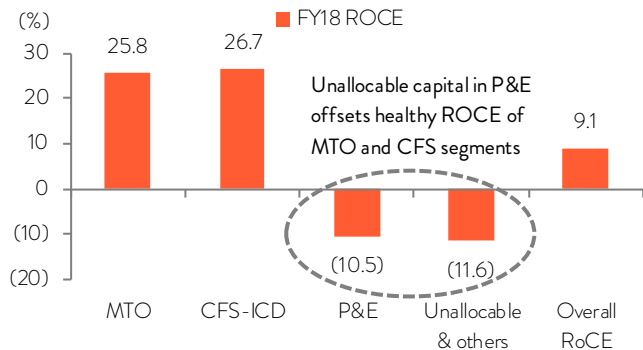
KEY FINANCIALS

Y/E 31 Mar	FY17A	FY18A	FY19E	FY20E	FY21E
Adj. net profit (Rs mn)	2,378	1,808	2,096	2,435	2,794
Adj. EPS (Rs)	9.7	7.4	8.5	9.9	11.4
Adj. EPS growth (%)	(1.5)	(24.0)	15.9	16.2	14.8
Adj. ROAE (%)	13.5	9.6	10.3	11.1	11.7
Adj. P/E (x)	11.6	15.3	13.2	11.3	9.9
EV/EBITDA (x)	6.0	8.1	6.7	5.6	5.1

Source: Company, BOBCAPS Research

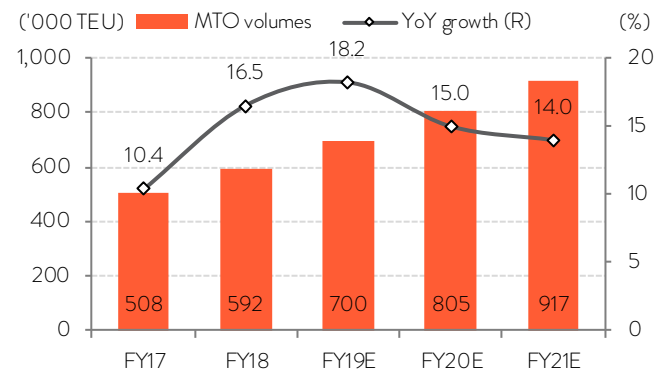
In a nutshell

FIG 1 – MTO AND CFS GENERATE HEALTHY ROCE; P&E, UNALLOCATED CAPITAL EXERT MAJOR DRAG



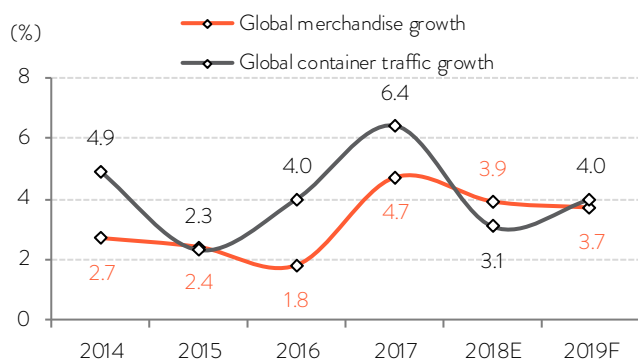
Source: Company, BOBCAPS Research

FIG 2 – MTO VOLUME GROWTH TO REMAIN HEALTHY OVER FY19-FY21E...



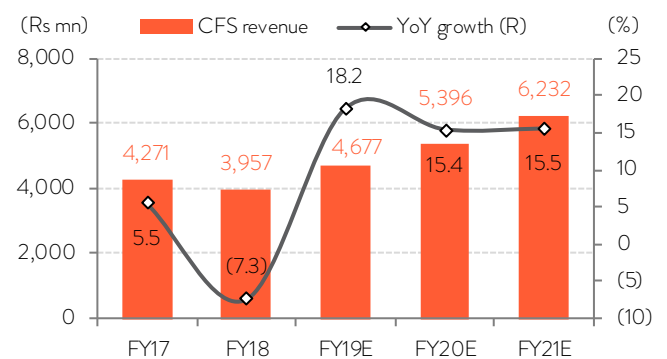
Source: Company, BOBCAPS Research

FIG 3 – ...DESPITE SOFT GLOBAL MERCHANDISE TRADE AND CONTAINER TRAFFIC GROWTH



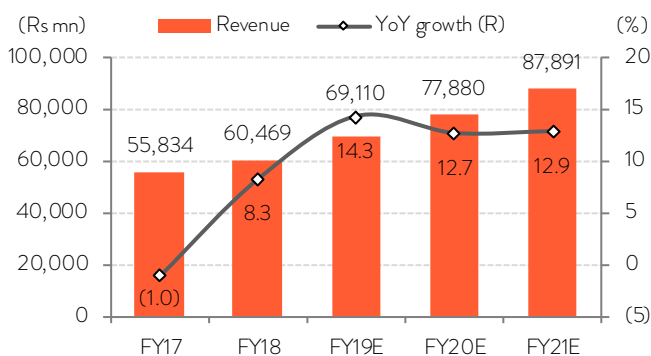
Source: WTO, World Bank, United Nations Conference on Trade and Development

FIG 4 – CFS SEGMENT RECOVERING FROM THE IMPACT OF DPD



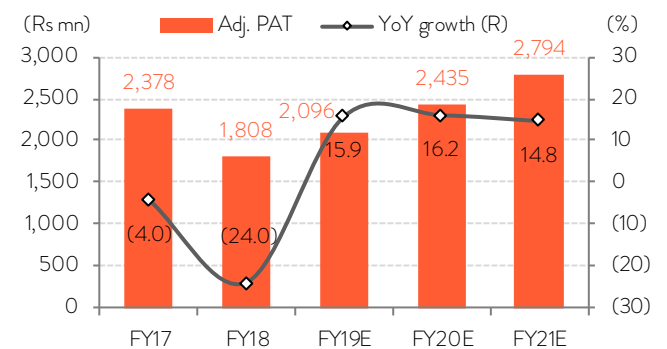
Source: Company, BOBCAPS Research

FIG 5 – REVENUE EXPECTED TO GROW AT 13% CAGR; MARGINS TO EXPAND 40BPS OVER FY19-FY21E



Source: Company, BOBCAPS Research

FIG 6 – ADJ. PAT PROJECTED TO GROW AT 15.5% CAGR



Source: Company, BOBCAPS Research

Investment rationale

Well placed for growth amid receding industry headwinds

After growing at a meagre 2.4% CAGR over FY15-FY18; we expect revenue growth to improve to 12.8% CAGR over FY19-FY21

FY15-FY18 was a tumultuous period for AGLL as industry-wide headwinds restricted consolidated revenue growth to a meagre 2.4% CAGR, with PAT declining to Rs 1.7bn from Rs 2.4bn in FY15. We see some of these headwinds receding, especially in the CFS and P&E segments. This coupled with AGLL's leadership in the LCL space should drive a healthy 12.8%/15.5% revenue/earnings CAGR for the company over FY19-FY21, in our view.

Established market standing

Three business segment – MTO (89% of FY18 revenue, 61% of EBITDA), CFS (7% of revenue, 31% of EBITDA), and P&E (4% of revenue, 8% of EBITDA)

AGLL operates in three business segments – multi-modal transport operations (MTO: 89% of FY18 revenue, 61% of EBITDA), container freight stations (CFS: 7% of revenue, 31% of EBITDA), and project & engineering (P&E: 4% of revenue, 8% of EBITDA).

In the MTO business, AGLL operates as an NVOCC (non-vessel operating common carrier) globally, with a presence in the less-than-container load (LCL) consolidation and full-cargo-load (FCL) forwarding businesses. It operates four CFSs in major container ports in India – JNPT, Mundra, Chennai and Kolkata – with annual capacity of ~0.5mn TEU, and one inland container depot (ICD) at Dadri. In the P&E segment, it is engaged in the equipment leasing and project logistics business to various end-user industries.

The company enjoys established market positioning, particularly in MTO and CFS. AGLL is currently among the top three LCL players worldwide and has 10-12% share of the global market, underpinned by an extensive global transport network.

Headwinds ebbing across segments

Revenue and EBITDA growth was muted for all segments over FY15-FY18

While MTO segment posted healthy volume growth of 12% CAGR over FY15-FY18, revenue growth was moderate at 4% as realisations declined at ~7% CAGR. EBITDA grew at 7% CAGR. Muted revenue growth is attributable to subdued shipping freight rates amidst escalating trade uncertainties and a demand-supply imbalance in the global shipping market.

AGLL's CFS segment posted revenue/EBITDA growth of 1% each during the period, as the impact of direct port delivery (DPD), which aimed to cut dwell time by bypassing freight stations, set in from FY17 onwards. Performance of the P&E segment was the worst – revenue declined at a 16% CAGR, culminating in a plunge in EBITDA to Rs 343mn in FY18 from Rs 1,692mn in FY15, as a cyclical demand downturn in key end-user industries took a toll.

MTO/CFS volumes increased 21%/13% YoY in 9MFY19, signalling ebbing headwinds

We are seeing signs that some of these headwinds are receding. While trade uncertainties remain, MTO volume growth improved to 21% YoY in 9MFY19. In CFS, volume ramp-up along with a plateauing of DPD share in JNPT at 40-45% aided volume growth of 13.4% YoY; EBIT/TEU also improved by 6% YoY. In the P&E segment, although revenue growth remains muted (2.5%), demand from key end-user industries is gradually improving, as per management, which bodes well for future order flow.

MTO business – undisputed leadership in a promising market

Strong market positioning to help MTO volumes outpace global container trade growth – 14.5% CAGR vs. 4% over FY19-FY21

Despite the shadow cast by escalating trade war tensions, we believe AGLL's MTO business is well equipped to outpace global container trade volumes (at 14.5% CAGR vs. 4% CAGR over FY19-FY21) due to (1) its leadership in the global LCL segment post a slew of astute acquisitions, (2) presence across key trade lanes (transatlantic, transpacific, intra-Asia, and Asia-Europe), and (3) growing FCL volumes (~30% CAGR in three years). Despite a muted outlook on realisations, we estimate a healthy 13% revenue CAGR for the business through to FY21.

Series of acquisitions helped fortify LCL leadership position

Acquisition of ECU Worldwide propelled AGLL as one of the market leaders in the global LCL space

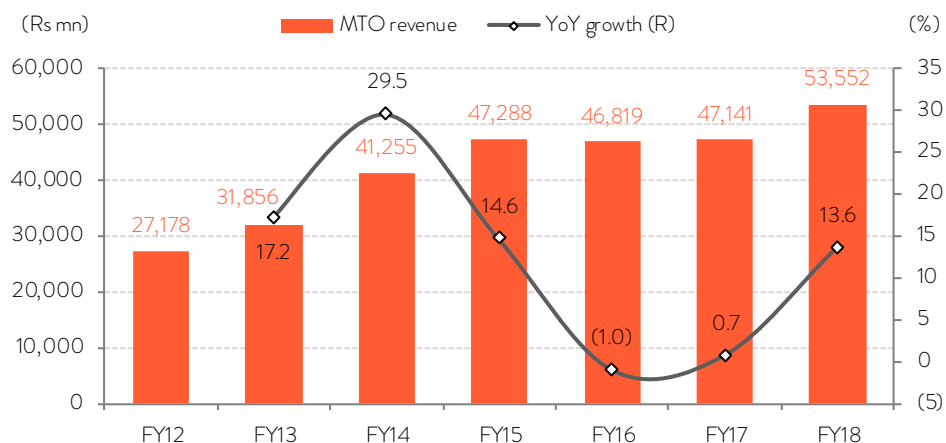
A series of astute acquisitions has helped AGLL emerge as one of the top players in the global LCL consolidation market. In FY06, it acquired Belgium-based ECU Worldwide (erstwhile ECU-Line), which had 4.3x AGLL's revenue at the time – this move propelled it into a prominent player in the global LCL landscape. The company further expanded its reach through several bolt-on acquisitions over the past decade, which have helped consolidate its position in a fragmented LCL market and expand its geographic presence.

Currently, AGLL is among the top three LCL players, along with Vanguard Logistics and Shipco Transports, and has 10-12% share of the global market

FIG 7 – NOTABLE ACQUISITIONS BY AGLL

Year	Company	Geography	Deal value (US\$ mn)	Comments
2005-06	ECU Worldwide	Belgium	60	One of the leading LCL players globally with 4.3x revenue and 10x office network of AGLL; originally a customer of AGLL's services
2007	Hindustan Cargo	India	NA	Air-freight and logistics arm of Thomas Cook India
2005	Econocaribe	USA	50	A leading LCL players in the US with a presence across the world; also provided FCL services. Fortified AGLL's position in the US market
2010	China Consolidation Shipping; Ningbo Star Express	Hong Kong/ PRC	NA	Strengthened presence in China and Eastern region
2013	FCL Marine	Netherlands	NA	Leading NVOCC service provider in the FCL segment operating in Europe, US and Canada. Helped AGLL enter the FCL segment

Source: BOBCAPS Research, Company

FIG 8 – INORGANIC EXPANSION ENABLED MTO BUSINESS SCALE-UP

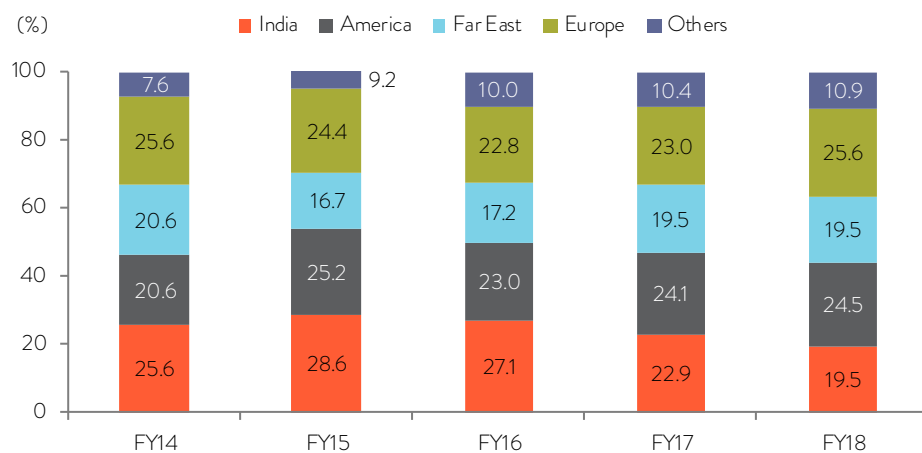
Source: Company, BOBCAPS Research

Diversified footprint across all major trade lanes

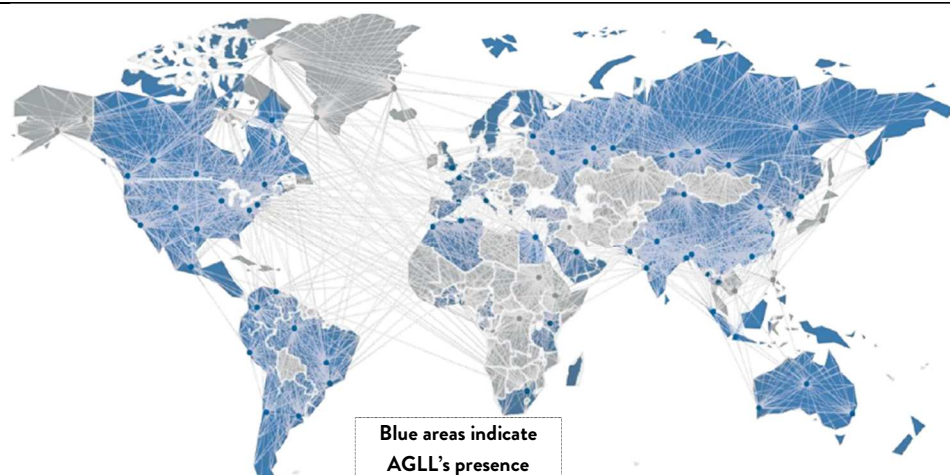
Vast network - 300 offices spread over 160 countries; connects 4,000 port pairs

With 300 offices spread over 160 countries, AGLL boasts one of the widest networks among LCL players globally. It has a presence across all major trade routes – transatlantic, transpacific, intra-Asia, and Asia-Europe – connecting ~4,000 port pairs. Concurrently, its geographic dispersion of revenue is also fairly uniform – Europe 25.6% (of FY18 revenue), America 24.5%, India 19.5%, Far East 19.5%, and others 10.9% – with little reliance on any single trade lane or country.

Global scale and a vast network help the company combat trade slowdown in a particular route and effectively negotiate with shipping lines and airlines on freight rates. Leading global freight forwarders such as DHL, Kuehne Nagel, FedEx, DB Schenker, Ceva Logistics and Panalpina figure among AGLL's clientele, which provides business stability.

FIG 9 – REVENUE BASE WELL DIVERSIFIED ACROSS GEOGRAPHIES

Source: Company, BOBCAPS Research

FIG 10 – AGLL HAS A PRESENCE IN MOST MAJOR COUNTRIES ACROSS THE GLOBE

Source: Company, BOBCAPS Research

Global LCL demand to sustain growth momentum

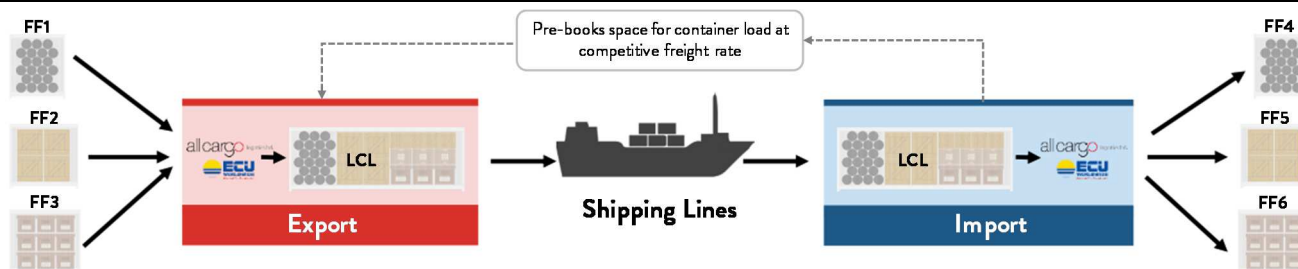
As per industry estimates, the global LCL segment has grown at double digits in recent years, much faster than the average 3-4% growth in global container trade. This uptrend has been led by evolving trade patterns in the form of (1) smaller, specific consignments, (2) focus on just-in-time manufacturing, (3) advent of e-commerce, and (4) availability of supply chain data enabling optimisation of cargo flow. Global LCL demand is expected to maintain this strong growth trajectory going forward. Being a market leader, AGLL should benefit from the uptrend.

LCL: Industry dynamics

Globally, manufacturers have two options for shipping their cargo: (1) contact the shipping lines directly, or (2) engage with freight forwarders/NVOCCs who can facilitate the transportation and related activities more efficiently. Freight forwarders are further classified into FCL forwarders and LCL consolidators.

Less-than-container load or LCL consolidation facilitates the transportation of small freight shipments which do not require the entire capacity of a container. LCL consolidators, such as AGLL, create a full container load (FCL) shipment by combining multiple LCL shipments from various clients. LCL consolidators pre-book inventory from shipping lines for full container load and utilise it by loading the assorted container. For their services, consolidators charge a premium over the prevailing shipping freight rate to clients.

As per industry estimates, freight forwarders handle 40-50% of overall container trade volumes, of which a majority pertains to FCL. LCL accounts for ~4-5% of global container trade, putting the market size at ~6mn TEU as of 2017. The market is fragmented with the top three players accounting for 35-40% of total volumes.

FIG 11 – LCL CONSOLIDATION PROCESS

Source: Company, BOBCAPS Research; FF stands for freight forwarders

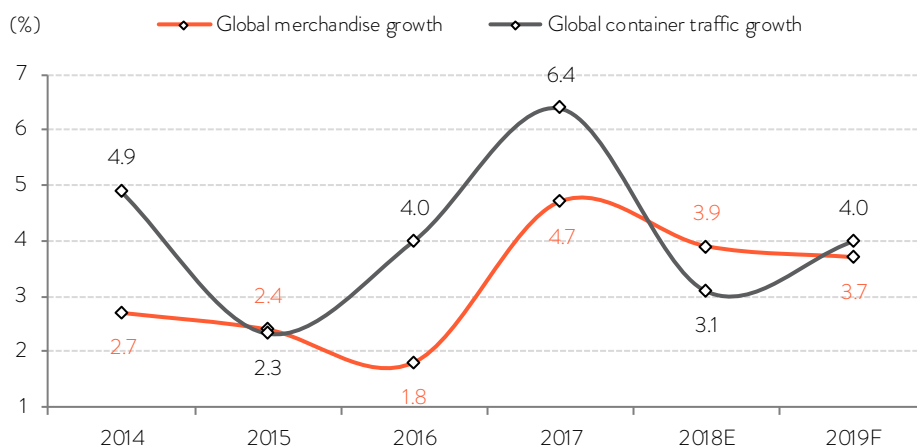
WTO forecasts 3.7% growth in global merchandise trade in 2019; container trade growth pegged at ~4% over the next few years

Medium-term outlook for global trade remains gloomy...

The world merchandise trade outlook remains gloomy for 2019, according to WTO. In its Sep'18 publication, WTO lowered its global merchandise trade forecast for 2018 to 3.9% from 4.4% earlier and anticipated a moderation in growth for 2019 to 3.7%, with risks heavily weighted to the downside.

The projected trade growth slowdown can be attributed to a convergence of headwinds – (1) protectionist trade policy measures by large economies such as the US and China, (2) volatility in exchange rates stemming from monetary policy tightening in developed economies, (3) possible capital outflow from emerging and developing economies owing to higher interest rates in developed nations, and (4) structural factors such as rebalancing of the Chinese economy away from investments and toward consumption.

Consequently, container trade is also expected to grow at a modest ~4% CAGR over the next few years. Shipping freight rates are likely to be benign as supply remains higher than demand.

FIG 12 – GLOBAL MERCHANDISE GROWTH AND CONTAINER TRADE GROWTH LIKELY TO REMAIN MUTED IN 2019

Source: WTO, World Bank, United Nations Conference on Trade and Development, BOBCAPS Research

...but AGLL on a firm footing

Despite industry headwinds, we expect AGLL's MTO volumes to post double-digit growth rates over FY19-FY21. The following factors work in the company's favour, in our view –

- Continued growth in the LCL consolidation segment at a pace outstripping that of global container trade;
- Presence across trade lanes, which mitigates the negative impact from a slowdown in a particular area – for example, any potential disruption in the transpacific route (Asia-North America) can be compensated for by higher volumes in the intra-Asia route;
- Large scale of operations, a critical factor for the LCL business, which helps in negotiating for preferential freight rates from shipping lines and in ensuring smooth services to customers; and
- Incremental market share gains in the FCL business.

Foray into FCL forwarding business incrementally positive

As a natural extension of its LCL consolidation business, AGLL forayed into the FCL forwarding space with the acquisition of FCL Marine in 2013. The two businesses have several synergies – overlapping clientele, same network and negotiations with the same shipping lines. Over the past three years, its FCL volumes has grown at a sturdy ~30% CAGR and has been a key driver of AGLL's MTO business.

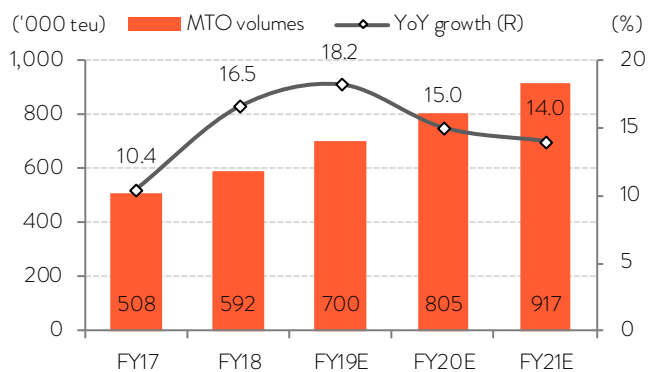
The addressable market in FCL forwarding is 10-12x larger than the LCL market, and although several large logistics players such as DHL, Kuehne Nagel, FedEx, DB Schenker and Panalpina are present in the industry, it is still fragmented in nature. Such an industry landscape provides ample opportunity for AGLL to gain incremental market share in the FCL business, leveraging its vast LCL network.

Factor in a 14.5% volume CAGR for the segment

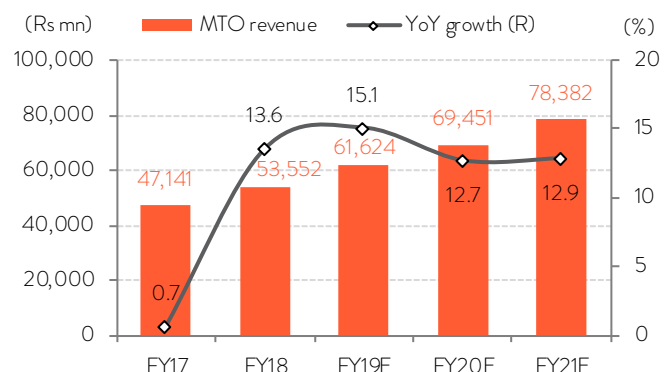
We model for a 14.5% volume CAGR for AGLL's MTO segment over FY19-FY21. However, we expect realisations to remain under pressure due to tepid shipping rates and a rising share of FCL. Therefore, we forecast a lower revenue CAGR of 12.8% for the segment (in rupee terms) over the same time period.

FCL volumes growing at a sharp click; large addressable market provide opportunity

Forecast 14.5% CAGR in MTO segment's volumes over FY19-FY21

FIG 13 – EXPECT A 14.5% CAGR IN MTO VOLUMES

Source: Company, BOBCAPS Research

FIG 14 – REVENUE GROWTH PEGGED AT 12.8% CAGR

Source: Company, BOBCAPS Research

CFS-ICD – worst phase of DPD is behind

After a challenging phase due to the implementation of DPD last year, the CFS segment has rebounded in 9MFY19 led by volume ramp-up in the Kolkata CFS (40% utilisation within a year of commission), growth in Chennai CFS and a plateauing share of DPD at JNPT (at 42-43%). With a diversified presence across major ports – JNPT, Mundra, Chennai and Kolkata, we expect AGLL to grow in line with container traffic and forecast a volume/revenue CAGR of 11%/15% over FY19-FY21.

DPD volumes likely to remain rangebound

The DPD or direct port delivery scheme was introduced by the government last year at JNPT as a panacea to cut cargo dwell time and costs. DPD essentially means import containers are delivered directly to pre-approved clients at the port itself instead of waiting in a CFS located outside for clearance.

While this system has hurt the business of CFSs servicing the port, we believe the worst is over for the CFS industry, with DPD share of road bound import cargo stagnating at 40-50% (50,000-60,000TEUs) over the past few months. Though the government aims to take DPD share to 70%, infrastructure bottlenecks – such as approach road infrastructure – are hindering further progress. Much of the DPD cargoes (70-75%) are also being diverted to freight stations for warehousing as importers face storage issues at their end, which has breathed life into many CFS operators.

Our channel checks indicate that DPD volumes are likely to remain rangebound until infrastructure issues at JNPT are resolved. Concurrently, we expect CFS volumes (including DPD cargo handling) to grow largely in line with container traffic growth at ports.

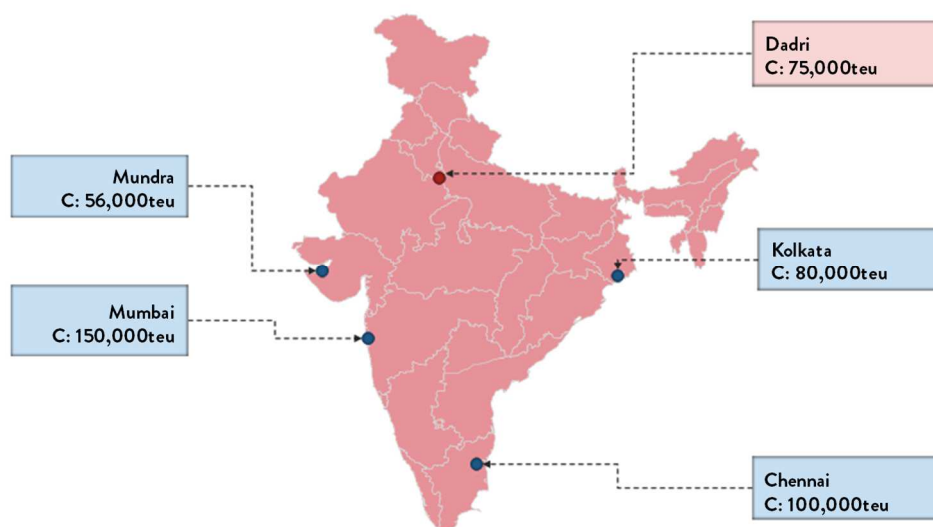
DPD laden containers at JNPT have stagnated between 50,000-60,000 over the past few months

Present in four key container ports – JNPT, Mundra, Chennai, and Kolkata – accounting for ~80% of total container volumes in India

Diversified geographic presence a major advantage

AGLL has a presence across the top container ports in India – JNPT, Mundra, Chennai and Kolkata – which together account for ~80% of India's container volumes. This diversified geographic footprint cushioned the impact of DPD on volumes – CFS operators with higher dependence on JNPT were affected more than AGLL. A presence across major ports also positions the company well to benefit from the growing container traffic in India.

FIG 15 – AGLL HAS CFS ACROSS KEY CONTAINER PORTS IN INDIA



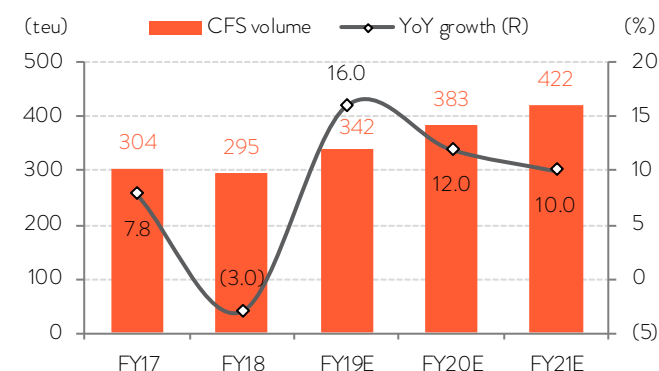
Source: Company, BOBCAPS Research

Ramp-up in the newly-commissioned Kolkata CFS, higher DPD-CFS cargo to drive volume growth for the segment

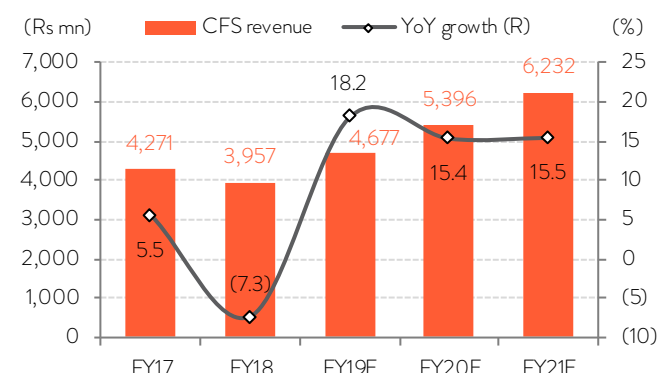
Expect volume growth to rebound to 11% CAGR over FY19-FY21

After a muted performance in FY18, the CFS-ICD segment posted consecutive quarters of healthy volume growth, at 22%/15% YoY in Q2/Q3FY19, led by utilisation ramp-up of the newly commissioned Kolkata CFS, growth in Chennai CFS, and higher DPD-CFS cargo (DPD cargo which is routed through a CFS) handled at JNPT. Within a year of commissioning, the Kolkata CFS has ramped up utilisation to ~40%, which is encouraging.

Going forward, we expect the segment to continue to register double-digit volume growth. Following stabilisation in DPD share, non-DPD cargo is expected to grow in line with container traffic at these ports, at 9-10% over the next five years. We forecast a 11% volume CAGR for AGLL's CFS segment over FY19-FY21, slightly higher than container traffic growth. Factoring in a 4% CAGR in realisation, we forecast a 15% revenue CAGR for the segment. Any increase in DPD volumes and/or decrease in non-DPD cargo in JNPT is a material risk to our projection.

FIG 16 – CFS VOLUMES TO GROW AT 11% CAGR OVER FY19-FY21E


Source: Company, BOBCAPS Research

FIG 17 – CFS REVENUE TO GROW AT 15% CAGR OVER FY19-FY21E


Source: Company, BOBCAPS Research

P&E – Remain cautious on long-term prospects

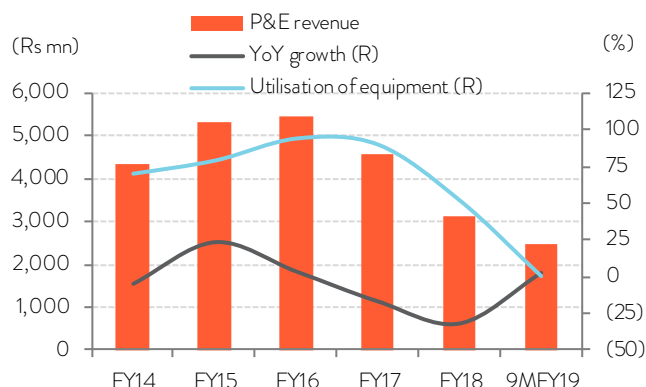
Low returns from the asset-intensive P&E segment, accentuated by a cyclical downturn in key end-user industries, has been a major drag on consolidated ROCE (at 9% in FY18 despite >25% ROCE in MTO/CFS). While AGLL expects demand revival from some industries, we cautiously build in 8% revenue growth over FY19-FY21.

Losses curtailed but revival awaited

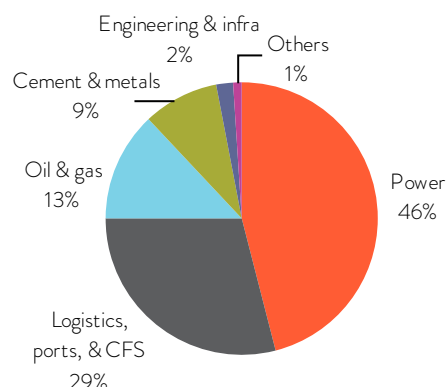
In the P&E business, AGLL engages in project logistics, equipment rental and other related activities. It caters to various end-industries such as power (thermal and wind); oil & gas; logistics, ports and CFSs; cement and metals; and engineering and infrastructure. Subdued demand from these industries has eroded utilisation levels over the past couple of years, to 52% in FY18 from 94% in FY16, culminating in an EBIT loss of Rs 516mn. This has exerted a major drag on AGLL's consolidated profitability and return ratios.

To combat the slowdown, management has liquidated some equipment, which helped curtail losses in 9MFY19 – segment EBIT loss has reduced to Rs 38mn in 9MFY19 vs. Rs 150mn in 9MFY18 – but a growth revival is yet to take place.

Slowdown in demand from key end-user industries have led to a decline in utilisation – to 52% in FY18, from 94% in FY16

FIG 18 – P&E REVENUE AND UTILISATION HAS COME DOWN SHARPLY IN RECENT YEARS...


Source: Company, BOBCAPS Research

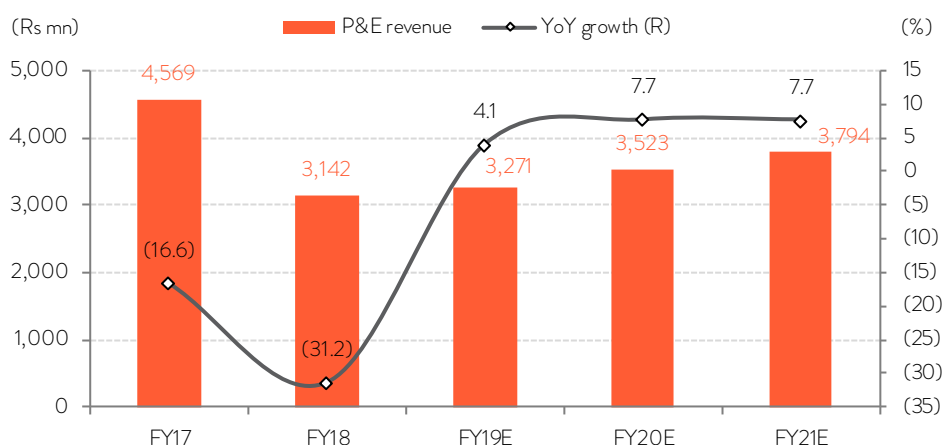
FIG 19 – ...OWING TO SUBDUED DEMAND FROM KEY INDUSTRIES (FY18 REVENUE SHARE)


Source: Company, BOBCAPS Research

Expect revival of demand from wind, oil & gas sectors to augment growth for the segment

Expect steady-state revenue growth at 7.7% CAGR

We expect P&E revenue to grow at a 7.7% CAGR over FY19-FY21. As of 9MFY19, the company has an executable order book of Rs 1.9bn, which provides revenue visibility for the next couple of quarters. Management is seeing early signs of demand revival from some end-user industries, such as wind, oil & gas and power, which should boost order flow. However, we are cautious about the segment's future prospects due to the cyclical nature of demand, excess capacity in the equipment leasing industry and weak past performance – we therefore build in single-digit growth.

FIG 20 – EXPECT P&E REVENUES TO GROW AT 7.7% CAGR


Source: Company, BOBCAPS Research

Financial review

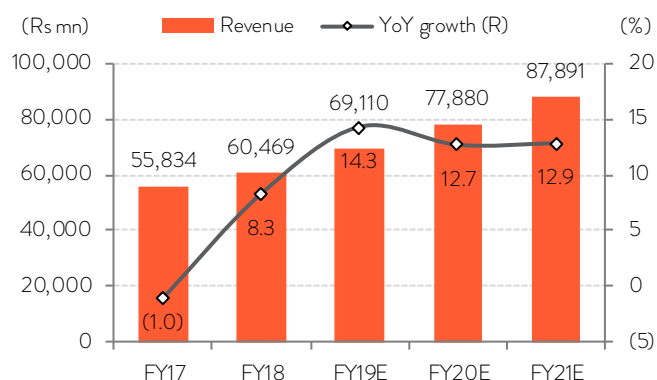
Expect revenue CAGR of 13% over FY19-FY21

Double-digit growth in MTO and CFS volumes to drive consolidated revenue growth

After a subdued 2.4% CAGR over FY15-FY18, AGLL's consolidated revenue growth rebounded in 9MFY19 to 14.5% YoY (FY19 estimate of 14.3%). The MTO and CFS segments witnessed double-digit volume growth as headwinds abated partially. We forecast a 13% revenue CAGR for AGLL over FY19-FY21, with the MTO/CFS segments estimated to grow at 13%/15% and the P&E business at a lower 7.7% CAGR.

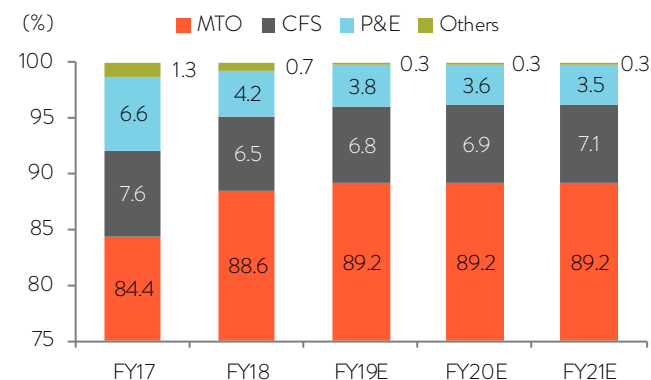
The MTO business is expected to be driven by volume growth (14.5% CAGR), though the rising FCL share in revenue mix is likely to keep realisations muted. The CFS segment is likely to witness both volume and realisation growth fuelled by ramp-up in Kolkata CFS utilisation and gradual improvement in volumes and realisations at JNPT post stabilisation of DPD.

FIG 21 – CONSOLIDATED REVENUE TO GROW AT 13% CAGR OVER FY19-FY21



Source: Company, BOBCAPS Research

FIG 22 – SHARE OF CFS SEGMENT IN OVERALL REVENUE TO IMPROVE SLIGHTLY



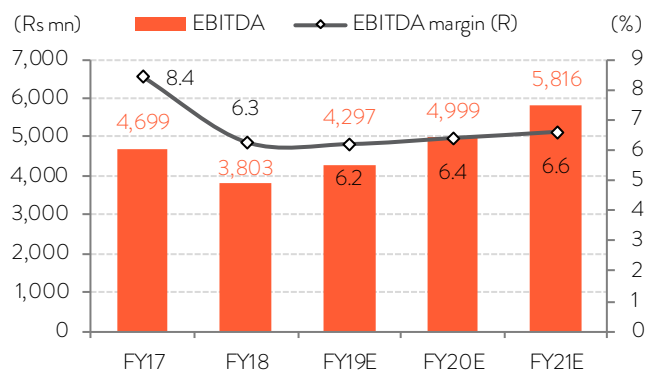
Source: Company, BOBCAPS Research

EBITDA margin to expand

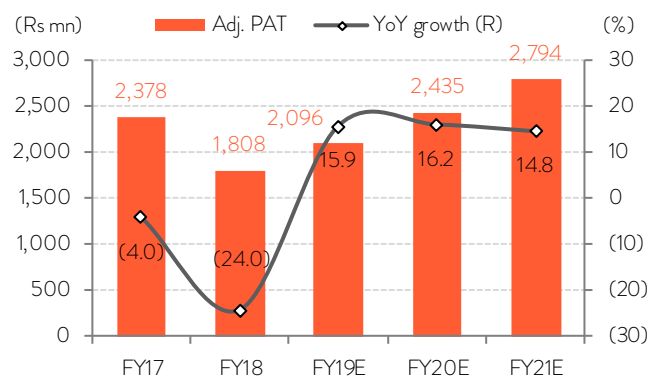
Project a 40bps margin expansion over FY19-FY21

AGLL's consolidated EBITDA margin is projected to improve by 40bps to 6.6% in FY21 from 6.2% in FY19, catalysed by the CFS and P&E segments, while MTO segment's margin is expected to be flat. We expect CFS margins to be boosted by operating leverage benefits stemming from higher volumes, while a stable share of DPD cargo in total volumes should provide support. Similarly, higher utilisation in the P&E segment should augment margin expansion. In MTO, the increasing share of FCL in total revenue is likely to keep EBITDA margins subdued.

Consequent to the revenue growth and margin expansion, we model for an adj. PAT CAGR of 15.5% for AGLL over FY19-FY21.

FIG 23 – EBITDA MARGIN TO EXPAND BY 40BPS OVER FY19-FY21E


Source: Company, BOBCAPS Research

FIG 24 – ADJ. PAT ESTIMATED TO GROW AT 15.5% CAGR


Source: Company, BOBCAPS Research

Valuation methodology

Initiate coverage with BUY and a Mar'20 TP of Rs 130, based on SOTP method

We have valued AGLL using the sum-of-the-parts (SOTP) method. For the core business, we assign a P/E multiple of 11x on FY21E EPS of Rs 11 (excludes share of profit from associates), which translates to Rs 121/sh.

The stock is currently trading at a P/E of 10.2x on FY21E EPS, below its past five-year average one-year forward P/E of 17x. Our assigned target multiple is ~50% lower than the historical average, as we expect global trade uncertainties, lingering impact of DPD, and weak end-industry demand for the P&E business to weigh on the stock price. While we believe the worst is over, the overhang on the multiple may continue for some time.

Apply a 11x 1-yr forward P/E multiple for the core business; 15x for ACCI, the contract logistics business

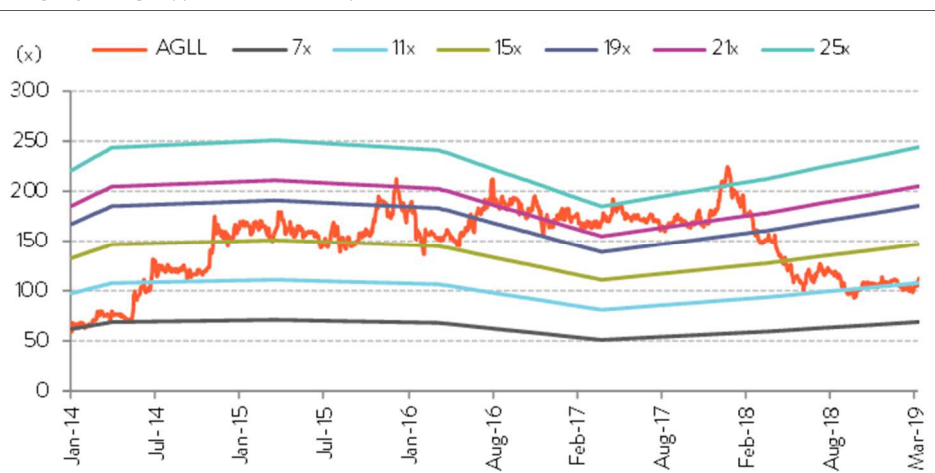
We value AGLL's 61.1% stake in contract logistics arm ACCI at a P/E multiple of 15x on the latter's FY21E earnings, translating to a value of Rs 9/sh. This leads to a Mar'20 target price of Rs 130, implying 16% upside from CMP. Initiate with BUY.

FIG 25 – KEY VALUATION ASSUMPTIONS

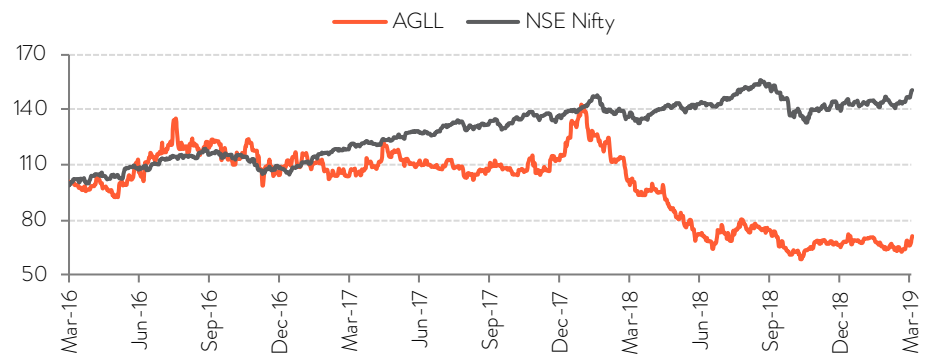
AGLL – core business	
FY21E EPS (Rs) – before share of profit from associates	11.0
P/E multiple applied (x)	11
Value of core business (Rs per share)	121
Value of stake in ACCI	
ACCI's PAT in FY21E (Rs mn)	279
P/E multiple (x)	15
Total equity value	4,179
AGLL's stake in ACCI (%)	61.1
Value of AGLL's stake (Rs per share)	9
Target price per share (Rs)	130

Source: Company, BOBCAPS Research

FIG 26 – FORWARD P/E BAND



Source: Bloomberg, BOBCAPS Research

FIG 27 – RELATIVE STOCK PERFORMANCE

Source: NSE

Key risks

- **Jump in DPD volume:** We expect the DPD share in total laden container imports at JNPT to remain largely stable, in the region of 40-45%, as infrastructure bottlenecks are likely to prevent a further uptrend, as per our channel checks. However, any sharp increase in DPD volumes at JNPT beyond our estimates is likely to be acutely negative for AGLL's CFS segment.
- **Inefficient capital allocation:** Allocation of capital to low-yielding assets and/or costly acquisitions would exert pressure on AGLL's return ratios. In the past, much of the company's growth has been driven by inorganic growth, and strategic acquisitions remain high on the management's agenda. While we note that the company has a track record of successful acquisitions, costly acquisitions in future remain a risk. In the past, AGLL has invested in low-yielding assets, such as the P&E segment. Substantial capital allocation to such assets is likely to be a drag on return ratios.
- **Sharp downturn in global trade:** Fortunes of the MTO business hinge on global trade momentum. Protectionist trade measures by large economies or a downturn in the global economy can potentially lead to lower global trade, thereby adversely affecting the company's MTO business.
- **Technology disruptions:** The freight forwarding business is facing a wave of technology-related shifts. Any structural change emanating from technological disruptions can have a long-lasting effect on freight forwarders.

Management overview

FIG 28 – KEY MANAGEMENT PERSONNEL

Name	Brief profile
Mr. Shashi Kiran Shetty Chairman	Mr. Shetty has experience of over three decades in the Indian logistics industry. He was the founder of AGLL. Mr. Shetty is leading several internal change management campaigns.
Mr. Adarsh Hedge Joint Managing Director	Mr. Hegde has been associated with Allcargo Logistics since its inception. Under his leadership, AGLL established multiple CFS & ICD facilities along with the P&E division. He has helped foster relationships with major liners and other global partners.
Mr. Suryanarayanan S Group Chief Strategy and Financial Officer	A Chartered Accountant, Mr. Suryanarayanan is the Group Chief Strategy and Financial Officer. He has close to 35 years of work experience in diversified businesses like engineering, petrochemical, shipping and logistics. He has led company through a series of project implementation and M&As.
Mr. Prakash Tulsiani Executive Director and Chief Executive Officer – CFS-ICD	Mr. Tulsiani has over two decades of experience in the business of shipping and ports, both in India and overseas. He is a qualified Chartered Accountant and Company Secretary.
Mr. Sandeep Anand Chief Executive Officer, Projects and Engineering Solutions	Mr. Anand has 22 years of sea service including 8 years of command experience. Over 10 years of industry experience in the field of cranes, over dimensional cargo, heavy lift and transport solutions for all types of project cargo.

Source: Company, BOBCAPS Research

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Total revenue	55,834	60,469	69,110	77,880	87,891
EBITDA	4,699	3,803	4,297	4,999	5,816
EBIT	3,037	2,212	2,702	3,118	3,588
Net interest income/(expenses)	(374)	(353)	(310)	(318)	(328)
Other income/(expenses)	453	414	355	385	385
Exceptional items	0	0	0	0	0
EBT	3,116	2,273	2,747	3,184	3,645
Income taxes	(776)	(513)	(736)	(855)	(982)
Extraordinary items	0	(69)	0	0	0
Min. int./Inc. from associates	38	48	85	106	131
Reported net profit	2,378	1,740	2,096	2,435	2,794
Adjustments	0	69	0	0	0
Adjusted net profit	2,378	1,808	2,096	2,435	2,794

Balance Sheet

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Accounts payables	6,232	6,902	8,013	9,032	10,199
Other current liabilities	1,212	1,642	1,876	2,115	2,386
Provisions	1,007	894	1,022	1,151	1,299
Debt funds	5,941	4,796	4,121	4,371	4,371
Other liabilities	0	0	0	0	0
Equity capital	491	491	491	491	491
Reserves & surplus	17,638	19,324	20,873	22,680	24,763
Shareholders' fund	18,129	19,816	21,364	23,171	25,254
Total liabilities and equities	32,522	34,049	36,396	39,840	43,510
Cash and cash eq.	2,725	3,553	3,851	2,404	2,779
Accounts receivables	7,522	8,386	10,414	11,735	13,244
Inventories	101	96	109	123	139
Other current assets	1,980	2,073	2,108	2,376	2,681
Investments	2,057	2,143	2,143	2,143	2,143
Net fixed assets	11,975	11,333	11,238	14,357	15,630
CWIP	753	100	0	0	0
Intangible assets	3,420	4,271	4,271	4,271	4,271
Deferred tax assets, net	721	931	931	931	931
Other assets	1,267	1,164	1,330	1,499	1,692
Total assets	32,522	34,049	36,396	39,840	43,510

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Net income + Depreciation	4,040	3,399	3,690	4,316	5,022
Interest expenses	374	353	310	318	328
Non-cash adjustments	123	(210)	0	0	0
Changes in working capital	(2,099)	138	(770)	(385)	(435)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	2,437	3,680	3,230	4,249	4,914
Capital expenditures	(974)	(1,145)	(1,400)	(5,000)	(3,500)
Change in investments	(1,755)	(86)	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(2,729)	(1,231)	(1,400)	(5,000)	(3,500)
Equities issued/Others	(13)	0	0	0	0
Debt raised/repaid	2,589	(1,145)	(675)	250	0
Interest expenses	(374)	(353)	(310)	(318)	(328)
Dividends paid	(491)	(491)	(632)	(734)	(842)
Other financing cash flows	(1,278)	453	85	106	131
Cash flow from financing	433	(1,537)	(1,532)	(696)	(1,039)
Changes in cash and cash eq.	142	912	298	(1,447)	375
Closing cash and cash eq.	2,725	3,553	3,851	2,404	2,779

Per Share

Y/E 31 Mar (Rs)	FY17A	FY18A	FY19E	FY20E	FY21E
Reported EPS	9.7	7.4	8.5	9.9	11.4
Adjusted EPS	9.7	7.4	8.5	9.9	11.4
Dividend per share	2.0	2.0	2.1	2.5	2.8
Book value per share	72.9	80.0	85.9	92.8	100.8

Valuations Ratios

Y/E 31 Mar (x)	FY17A	FY18A	FY19E	FY20E	FY21E
EV/Sales	0.5	0.5	0.4	0.4	0.3
EV/EBITDA	6.0	8.1	6.7	5.6	5.1
Adjusted P/E	11.6	15.3	13.2	11.3	9.9
P/BV	1.5	1.4	1.3	1.2	1.1

DuPont Analysis

Y/E 31 Mar (%)	FY17A	FY18A	FY19E	FY20E	FY21E
Tax burden (Net profit/PBT)	76.3	79.6	76.3	76.5	76.7
Interest burden (PBT/EBIT)	102.6	102.7	101.7	102.1	101.6
EBIT margin (EBIT/Revenue)	5.4	3.7	3.9	4.0	4.1
Asset turnover (Revenue/Avg TA)	2.5	2.5	2.8	2.9	3.1
Leverage (Avg TA/Avg Equity)	1.3	1.3	1.2	1.2	1.2
Adjusted ROAE	13.5	9.6	10.3	11.1	11.7

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY17A	FY18A	FY19E	FY20E	FY21E
YoY growth (%)					
Revenue	(1.0)	8.3	14.3	12.7	12.9
EBITDA	(7.7)	(19.1)	13.0	16.3	16.3
Adjusted EPS	(1.5)	(24.0)	15.9	16.2	14.8
Profitability & Return ratios (%)					
EBITDA margin	8.4	6.3	6.2	6.4	6.6
EBIT margin	5.4	3.7	3.9	4.0	4.1
Adjusted profit margin	4.3	3.0	3.0	3.1	3.2
Adjusted ROAE	13.5	9.6	10.3	11.1	11.7
ROCE	13.5	9.1	10.8	11.7	12.5
Working capital days (days)					
Receivables	49	51	55	55	55
Inventory	1	1	1	1	1
Payables	44	44	45	45	45
Ratios (x)					
Gross asset turnover	3.9	4.1	4.3	4.1	3.7
Current ratio	1.5	1.5	1.5	1.4	1.4
Net interest coverage ratio	8.1	6.3	8.7	9.8	10.9
Adjusted debt/equity	0.2	0.1	0.0	0.1	0.1

Source: Company, BOBCAPS Research

REDUCE

TP: Rs 530 | ▲ 1%

**CONTAINER CORP OF
INDIA**

| Logistics

| 14 March 2019

Lofty valuations factor in upside – initiate with REDUCE

Container Corporation of India's (CCRI) fortunes are inherently linked with cyclical systemic factors of India's export-import trade and industrial activity. Despite this, it has commanded steep valuations, trading at an average one-year forward P/E of 25x over the past five years, as the Dedicated Freight Corridor (DFC) came closer to reality. While we expect the DFC to bring in transformational changes, the positives appear priced in – we thus initiate coverage with REDUCE; our Mar'20 TP of Rs 530 is set at 25x FY21E EPS.

Sayan Das Sharma | Rohan Korde

research@bobcaps.in

Undisputed leader among CTOs: CCRI is the undisputed leader in India's container rail terminal operator (CTO) industry with ~70% market share. Armed with an unmatched terminal network (81 vs. 5 for its closest competitor), vast rolling stock (25k containers, 13k high-speed wagons), and >50% share in major container ports, CCRI comfortably fends off competition from private CTOs.

Dedicated Freight Corridor – a panacea for industry ills: External challenges – softening container traffic, road competition, adverse regulations – have assailed CCRI's operating performance in recent years. Commissioning of the DFC should come as a much-needed panacea, augmenting market share gains, steering efficiency benefits (higher double-stacking, faster turnaround), and stabilising lead distances. While full benefits of the DFC would accrue only from FY23, the transport corridor is likely to support stock performance in the interim.

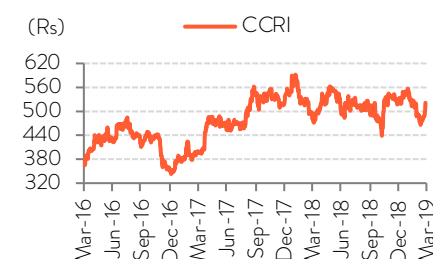
Healthy topline growth: A robust volume CAGR of 13% over FY19-FY21E is likely to fuel a similar revenue CAGR; EBITDA margins are forecast to expand 160bps. Expiry of SEIS export incentive income in FY20 could limit PAT growth to 4.5%.

Initiate with REDUCE: We value CCRI at 25x FY21E EPS, in line with the 5Y average, yielding a Mar'20 TP of Rs 530. Initiate with REDUCE on limited upside.

Ticker/Price	CCRI IN/Rs 523
Market cap	US\$ 4.6bn
Shares o/s	609mn
3M ADV	US\$ 8.8mn
52wk high/low	Rs 705/Rs 461
Promoter/FPI/DII	55%/28%/13%

Source: NSE

STOCK PERFORMANCE



Source: NSE

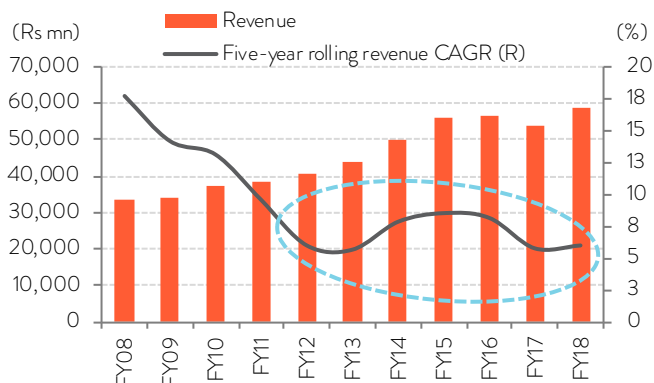
KEY FINANCIALS

Y/E 31 Mar	FY17A	FY18A	FY19E	FY20E	FY21E
Adj. net profit (Rs mn)	9,445	10,619	11,581	12,810	12,648
Adj. EPS (Rs)	15.5	17.4	19.0	21.0	20.8
Adj. EPS growth (%)	(7.7)	12.4	9.1	10.6	(1.3)
Adj. ROAE (%)	11.0	11.6	11.9	12.1	11.0
Adj. P/E (x)	33.7	30.0	27.5	24.9	25.2
EV/EBITDA (x)	29.0	25.0	20.5	18.1	14.9

Source: Company, BOBCAPS Research

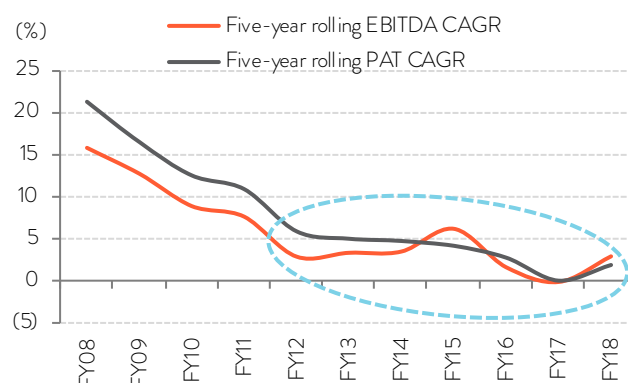
In a nutshell

FIG 1 – CHALLENGING EXTERNALITIES HAVE LED TO MODERATION IN REVENUE...



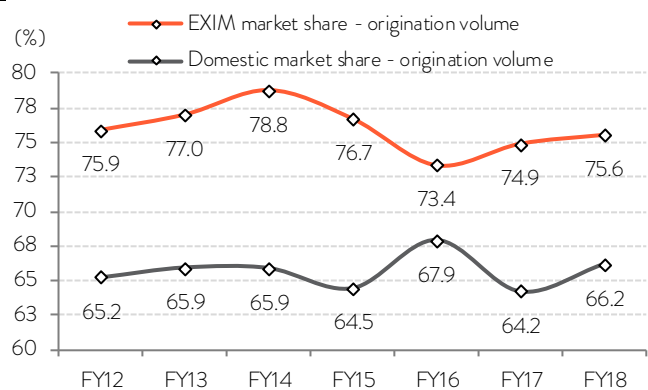
Source: Company, BOBCAPS Research

FIG 2 – ...AS WELL AS PROFITABILITY OVER THE PAST FEW YEARS



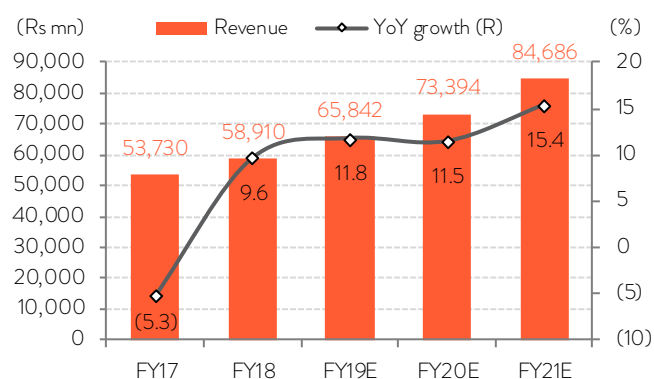
Source: Company, BOBCAPS Research

FIG 3 – MAINTAINED MARKET SHARE DESPITE ADVERSITIES



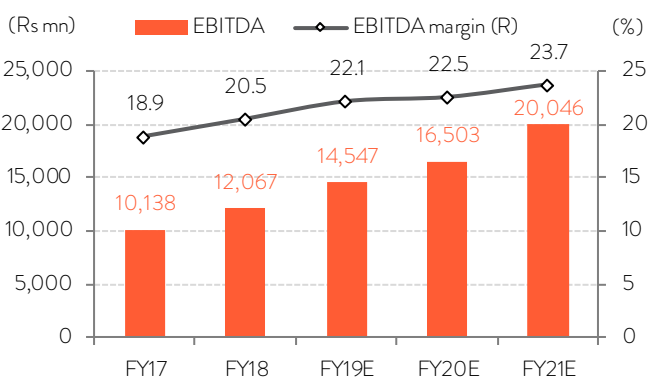
Source: Company, BOBCAPS Research

FIG 4 – FORECAST 13% REVENUE CAGR DRIVEN BY HIGHER VOLUMES



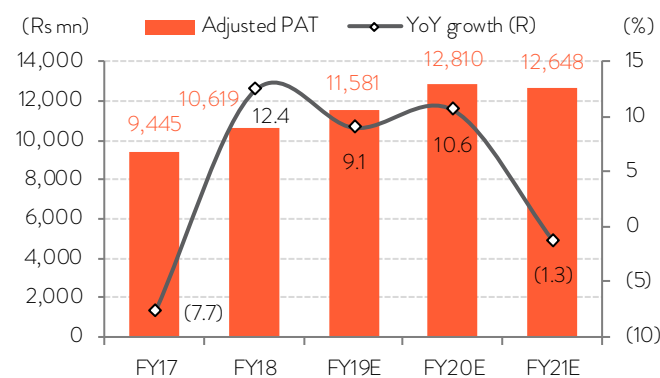
Source: Company, BOBCAPS Research

FIG 5 – EXPECT EBITDA GROWTH TO BE HEALTHY AT 17% CAGR OVER FY19-FY21



Source: Company, BOBCAPS Research

FIG 6 – BUT ABSENCE OF SEIS INCOME IN FY21 TO KEEP PAT GROWTH MUTED AT 4.5% CAGR



Source: Company, BOBCAPS Research

Investment rationale

Core performance volatile...

CCRI, the largest container rail operator in India, is standing at an interesting crossroads in its journey. The CTO business remains exposed to challenging externalities, such as softening container traffic growth, competition from road transport operators and adverse regulations, which keep operating performance volatile. However, DFC commissioning is expected to transform the industry in many ways. We note that even a decade after opening up of the CTO industry, CCRI maintains its competitive edge over private CTOs and hence is best positioned to capitalise on DFC-related opportunities.

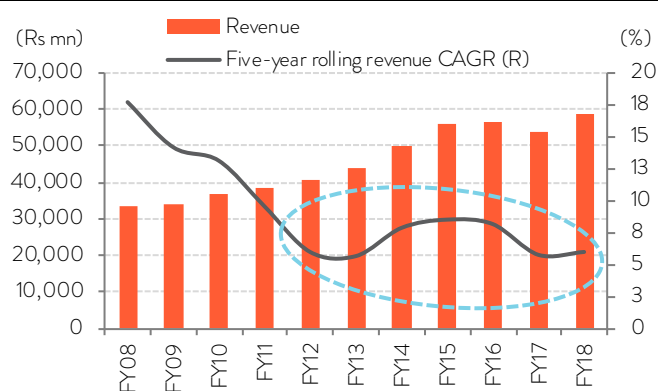
Prolonged period of operational weakness

Revenue/PAT growth has slackened since FY11, vs. growth in the previous period

CCRI's operating performance on several key metrics was suppressed for the better part of the past decade, largely owing to systemic factors. A study of five-year rolling CAGRs from FY05 onwards clearly demonstrates a declining trend in revenue and profitability since FY11 – revenue CAGR has moderated to 7% on average over FY11-FY18 compared to a sturdy 16.8% average over FY05-FY10, whereas PAT CAGR has nosedived to 4.3% vs. 18.7% on average.

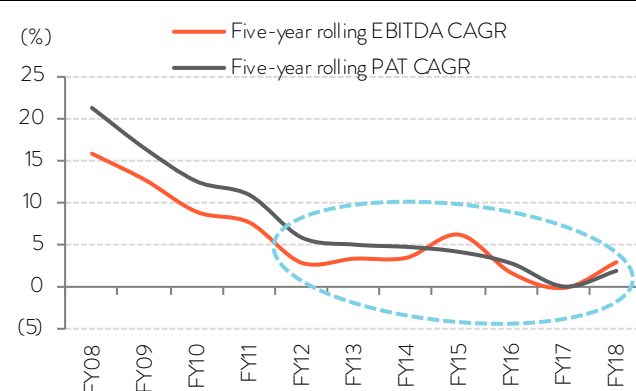
In our view, this relatively sedate performance can be attributed to a moderation in container traffic growth, higher competitive intensity from private CTOs and road freight operators, and a challenging regulatory environment.

FIG 7 – REVENUE GROWTH HAS MODERATED OVER THE PAST FEW YEARS



Source: Company, BOBCAPS Research

FIG 8 – EBITDA AND PAT HAVE POSTED SINGLE-DIGIT ROLLING CAGR OVER FY11-FY18



Source: Company, BOBCAPS Research

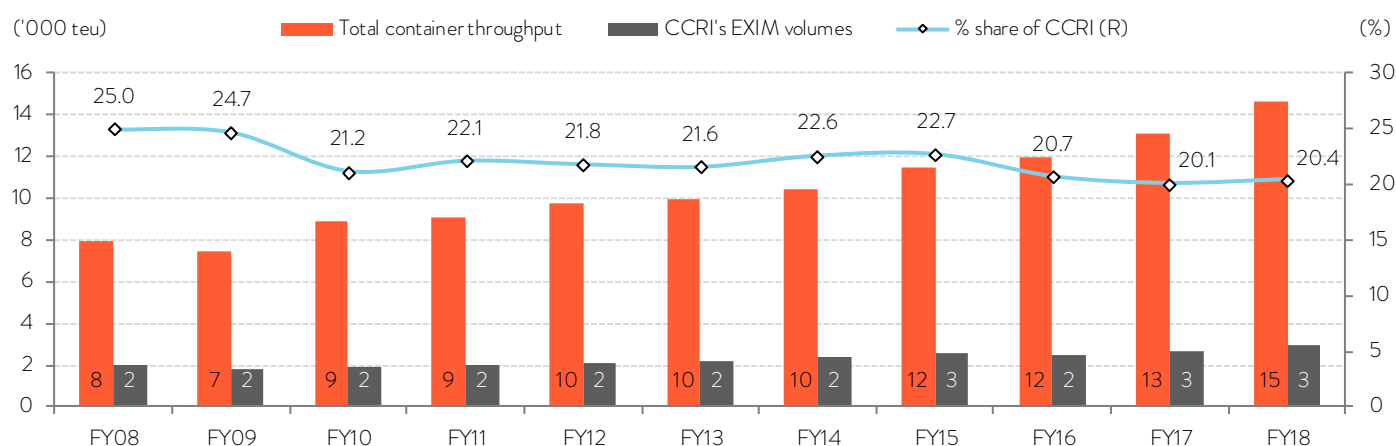
Slowing container traffic growth, policy headwinds were major dampeners

Container traffic growth in India has moderated during the decade - 6-7% over FY11-FY18 vs. ~15% over FY05-FY10

CCRI's aggregate volume growth also tapered off from a 10.2% average five-year rolling CAGR over FY05-FY10 to 4.2% over FY11-FY18, which can be attributed to lower container throughput growth in India (6-7% over FY11-FY18 vs. ~15% over FY05-FY10) and moderation in economic growth over the previous decade. As container traffic is contingent on both global trade growth and domestic economic buoyancy, CCRI's volumes are exposed to cyclical in these factors.

Stiff competitive intensity from road transporters and private CTOs have also capped volume growth. During FY09-FY10, CCRI lost market share as the container freight segment was opened up to private terminal operators. While the company has largely held its ground since then, there have been intermittent aberrations in market share, such as in FY14/FY16 when diesel prices moved +17%/-13% YoY, owing to divergence between road and rail freight upon sharp movement in crude prices.

FIG 9 – SOFTENING CONTAINER THROUGHPUT GROWTH EXPLAINS CCRI'S EXIM GROWTH MODERATION



Source: Company, Drewry Maritime Advisors, BOBCAPS Research

Adverse policy measures have taken a toll on CTO's performance

Some policy measures by the Indian Railways (IR) have also taken their toll on CCRI's operating performance. The most prominent was the opening up of the sector to allow private players into the container freight segment, after issuance of licences in FY07-FY08, leading to erosion of market share for CCRI. Further policy actions by the IR have also created impediments for the company, such as multiple hikes in haulage/terminal access charges in quick succession, stiff charges for empty container and wagon movement, and levy of other surcharges (development surcharge, parking fee).

IR has taken prudent pricing measures in recent years

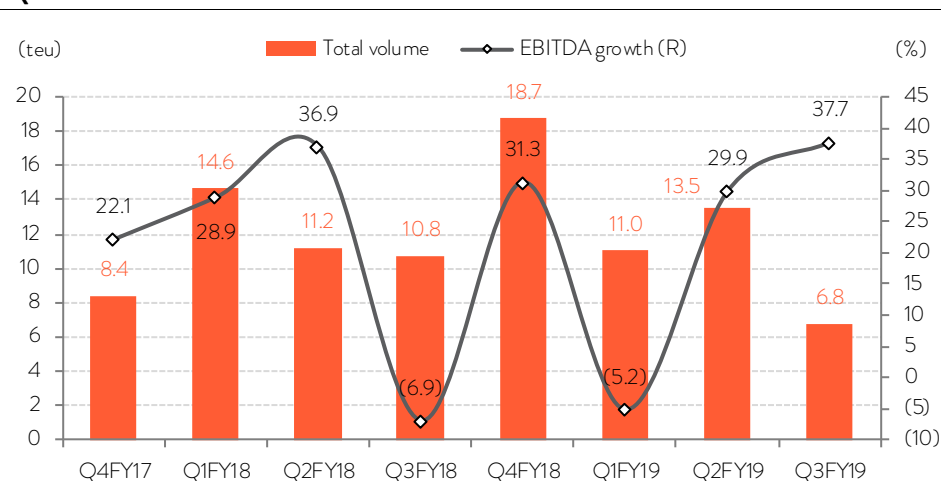
While regulatory concerns have abated somewhat owing to prudent pricing measures by IR in recent years (only one haulage charge increase in past four years, recent discount on empty running charges), the possibility of adverse pricing action cannot be ruled out and hence remains an overhang.

FIG 10 – HAULAGE RATE HIKES FOR CONTAINER MOVEMENT BY IR

Date	Range of increase	Haulage rate hike
Dec 2012	Up to 22%	0-22% increase on all lightweight and empty containers
Feb 2013	Up to 7.2%	Increased for long-haul distances (500km+)
Dec 2014	Up to 18%	18% hike for all categories; ~3% for empties
Mar 2015	Up to 18%	7.7% hike for majority of the categories; ~10% for 31tonne+ category
Nov 2018	5%	5% hike for all container movement effective Nov'18; subsequently provided 25% discount on empty flat and empty wagon running charges from Jan'19

Source: Indian Railways, BOBCAPS Research

Over Q4FY17-9MFY19, volume growth improved steadily, driven by growth in both EXIM and domestic segments, as container traffic improved. Double-stacking benefits and price hikes in 9MFY19 also helped lift EBITDA growth during the period.

FIG 11 – OPERATING PERFORMANCE HAS IMPROVED IN PAST FEW QUARTERS

Source: Company, BOBCAPS Research

EBITDA per TEU nosedived 11% CAGR over FY15-FY17 due to plunging lead distances, before growing 5% in FY18

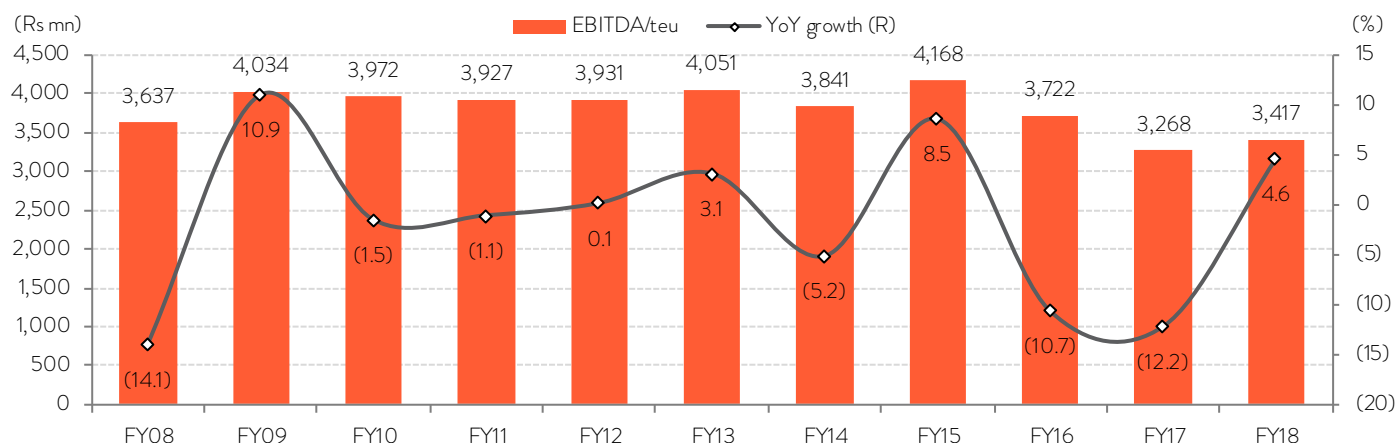
Per-unit profitability rangebound for a long period

CCRI's EBITDA per TEU, a measure of per-unit profitability, has remained flat over the past decade. After growing at a sedate 2% CAGR over FY08-FY15, when several pricing and other regulatory actions kept profitability suppressed, EBITDA/TEU plummeted in FY16-FY17, consequent to a plunge in lead distances. In FY18, it increased by 5%, driven by higher double stacking. Over FY15-FY18, CCRI's overall lead distance fell to 858km from 1,032km. This fall was more pronounced in EXIM (down 177km) than domestic (down 134km) trade, leading to lower realisations and per unit profitability.

Drop in EBITDA/TEU/km was less pronounced

Notably, EBITDA/TEU/km (the metric for per-unit profitability adjusted for lead distances) also decreased over FY15-FY18, although the decline was less pronounced, indicating possibly that the price hikes taken were not commensurate with the increase in haulage charges in the previous year (H2FY15). Improvement in FY18 can be attributed to higher double-stacking (total 2,297 double-stacked trains during the year vs. 1,160 in FY17).

FIG 12 – EBITDA/TEU HAS REMAINED FLAT OVER THE PAST DECADE



Source: Company, Indian Railways, BOBCAPS Research

70% share in a market with 17-18 private CTOs indicate CCRI's dominance

...but CCRI still a cut above peers; aptly placed to leverage DFC

CCRI remains the undisputed leader among CTOs with ~70% market share in the rail segment. Although the entry of private players since FY08 had weakened its operating performance, the company continues to dwarf its peers in scale and volumes – it enjoys far higher economies of scale, a superior infrastructure and terminal network, besides stronger connections between all major west-coast container ports and consumption centres. Competition from private CTOs notwithstanding, CCRI has been able to maintain its volume market share in both the EXIM and domestic segments, which is a testimony to its apex positioning.

Network infrastructure dwarves that of peers

Vast network of 81 terminals, 25,000 containers, 15,000 wagons dwarf that of peers

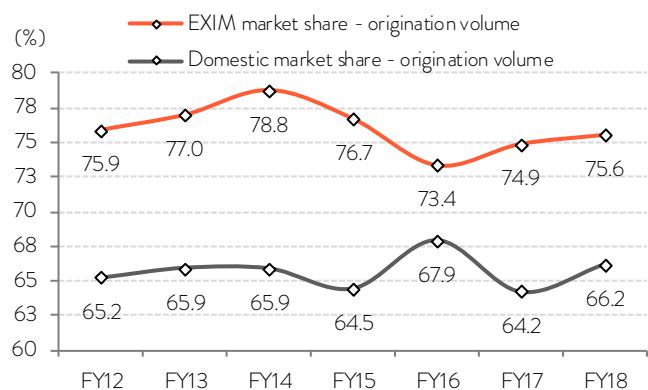
CCRI boasts an unparalleled network of 81 ICDs (73 owned terminals, 8 strategic tie-ups) across the country and a vast rolling stock of ~25,000 containers and ~15,000 wagons (including 13,000 high-speed wagons), 16 gantry cranes, and 70 reach stackers. In comparison, the second largest CTO, Gateway Distriparks, has only 5 terminals (3 in the North, 2 in the West) and 10 reach stackers. Moreover, CCRI has a strong presence in major container ports on the west coast, with ~80% volume share in JNPT and 50-55% in Mundra and Pipavav.

Steady market share in IR container traffic

Has maintained ~75% share in EXIM originating volumes; gained marginally in domestic

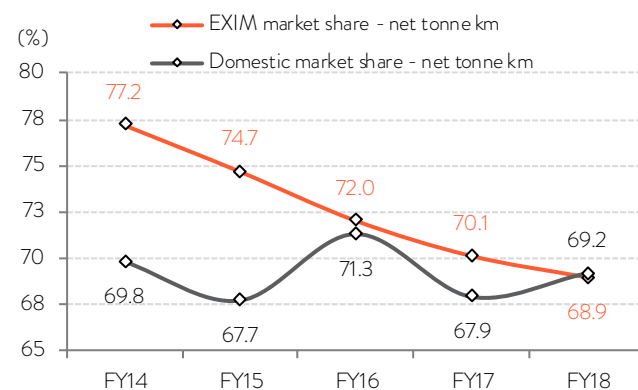
In terms of origination volumes (in million tonnes), CCRI has maintained its market share in the EXIM volume carried by the IR at ~75% over FY12-FY18, while gaining some share in the domestic segment. This reflects its competitive edge vis-à-vis private CTOs. In net tonne-kilometre (tkm) terms, while CCRI has lost share in the EXIM segment (attributable to a sharper drop in EXIM lead distance relative to IR), it has largely maintained market share in the domestic segment. CCRI's EXIM lead has fallen 240km over FY14-FY18 (to 740km) vs. a 190km drop in IR container traffic (to 810km).

FIG 13 – CCRI MAINTAINED MARKET SHARE IN ORIGINATION TERMS...



Source: Company, BOBCAPS Research

FIG 14 – ...BUT STEEPER DECLINE IN LEAD DISTANCE LED TO EROSION ON NTKM BASIS



Source: Company, BOBCAPS Research

Private CTOs pose limited threat

We do not foresee any major threat from private CTOs to CCRI. Industry headwinds have had a far worse impact on private operators than CCRI, and hence most have a weak balance sheet at present. Most of them have also under-invested in new terminal networks and high-speed wagons, while CCRI has been at the forefront. Hence, we believe the company will be aptly placed to exploit the large opportunities that will emerge post DFC commissioning.

Dedicated Freight Corridor – a potential panacea

DFC is closer to reality with the Rewari-Palanpur slated to start operations by H2FY20; should connect Gujarat ports

We expect commissioning of the DFC to be a game-changer for CCRI as it will alleviate several of the constraints that have prevented CTOs (including CCRI) from achieving their full potential, bringing structural stability to an otherwise cyclical industry. Benefits of a dedicated transport corridor are likely to be four-pronged for CCRI – (1) substantial market share gains away from road transport, leading to a jump in volumes, (2) higher load carrying capacity due to increased double-stacking, (3) greater stability in lead distances, and (4) efficiency gains.

DFC should improve competitiveness with road on various fronts

Set to regain substantial market share from road transport

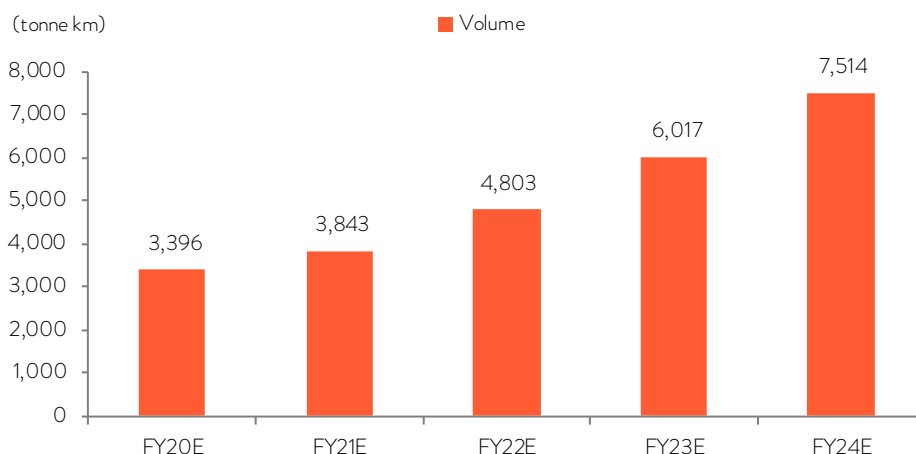
We expect CCRI's volumes to soar post DFC commissioning. In the past, rail transporters have lost volumes to road operators even for lead distances of ~700km+ despite having better economics (lower cost per tonne-km), as they could not guarantee timely delivery of goods. DFC is likely to improve the competitiveness of rail vs. road as (1) efficiency gains enhance rail economics and lower the viable distance from ~700km at present, thus expanding the product basket for rail; and (2) dedicated lines for freight rails would enable CCRI to offer transit time assurance to customers (Fig 9).

As a result, we expect a large shift in container traffic from road to rail. With its advantageous positioning over other CTOs, CCRI is likely to be the largest beneficiary of this shift. The quantum of the volume shift from road to rail is, however, hard to assess. Some estimates peg an increase in rail's share to ~40% of total freight from 28-30% at present, while others expect an incremental 100mn tonnes to be carried by rail. Dedicated Freight Corridor Corp's (DFCCIL) business plan envisages an increase in rail's share in port-bound container traffic to 35-40% within a few years from 20%-odd at present.

Expect 18-20% CAGR in EXIM container volume, in tkm terms

We believe that for the first 2-3 years, EXIM container volumes for IR can gallop at 18-20% CAGR, in tonne-km terms. CCRI is expected to grow at a faster clip of ~22% over FY20-FY24 (with DFC benefits likely to trickle in from FY21, with full benefits expected from FY23), increasing its market share in tonne-km terms to ~79% in FY24 from ~69% currently.

FIG 15 – CCRI TO GAIN VOLUMES POST DFC COMPLETION



Source: Company, BOBCAPS Research

Efficiency gains – higher double-stacking, steady lead distances

Apart from volume gains, CCRI is also expected to witness several efficiency gains. Rakes with higher load carrying capacity will lead to higher throughput per

train and enable increased double-stacking of cargo, translating to margin improvement. Other efficiency gains include faster transit time and better service quality to clients.

A key development would be the increased stability in lead distances. Once JNPT is connected to the freight corridor, its connectivity to the hinterlands via rail is expected to improve. This should raise the rail coefficient for JNPT (currently 15-20% of total container traffic) and consequently stabilise lead distances.

FIG 16 – DFC WILL ENHANCE RAIL'S COMPETITIVENESS VS. ROAD ON MOST FACTORS

Issues that weaken rail's competitiveness vs. road	DFC's expected impact	Our rationale
Unpredictability of rail schedule	Positive	<ul style="list-style-type: none"> Historically, freight trains in India share the track with passenger trains. With a higher focus placed on service quality of the latter, there are often delays in freight train schedules. Hence, CTOs today are unable to provide transit time assurances to customers. With an exclusive rail track for freight trains under the DFC regime, schedules for container rails will be far more reliable. This should enable CTOs to provide transit time assurances.
Unfavourable economics for short/medium-haul	Positive	<ul style="list-style-type: none"> Rail has lost market share to road for short-/medium-haul distances as the latter's per-tonne-km economics is better than rail. This can be attributed to non-linear haulage charge hikes in rail to compensate for lower passenger rates. With DFC bringing in efficiencies and increasing axle load by ~50%, rail economics are expected to improve even for medium-haul distances, making rail a viable option for more product baskets.
Higher transit time	Positive	<ul style="list-style-type: none"> Slow speed of freight trains results in higher transit time, shifting cargoes to road. Average speed of trains is expected to increase by 2.5-3x to ~75kmph from ~23kmph at present, leading to lower transit times.
Inadequate terminal infrastructure	Positive	<ul style="list-style-type: none"> Lack of proper infrastructure at freight terminals has hindered effective loading/unloading of cargo in the past. DFC entails significant investments in rail ICDs/terminals. CCRI has been at the forefront of setting up these terminals. This is likely to address the infrastructure constraints.
Capacity constraints	Positive	<ul style="list-style-type: none"> In the past, rail freight has been impacted by capacity constraints – e.g. lack of adequate rakes during peak time and a congested network. CCRI is investing heavily on DFC-compliant rolling stock, including several new rakes which should allay the capacity concerns for container freight. Congestion is also unlikely to be an issue under DFC.
Lack of first-/last-mile connectivity	No impact	<ul style="list-style-type: none"> Rail does not provide first-/last-mile connectivity which will remain a disadvantage vs. road transport. Although IR has recently tested the idea of using RoadRailers (wagons with wheels enabling them to run on roads), large-scale adoption is still some time away.
No flexible pricing	No impact	<ul style="list-style-type: none"> Unlike road operators, rail does not provide flexible pricing to customers. This is likely to remain a disadvantage vs. roads.

Source: Industry sources, BOBCAPS Research

Management initiatives to bolster integrated offerings

CCRI has entered related businesses – coastal shipping, distribution logistics – to offer integrated solutions to clients

CCRI continues to focus on bolstering its multi-modal positioning by entering newer business areas and providing integrated logistics offerings to customers. The company started coastal shipping operations in Q4FY19 and is setting up distribution centres to offer distribution logistics. While these steps may not contribute materially to revenue in the foreseeable future, they can help diversify the company's revenue base over the longer term.

New offerings to round off service basket

- **Coastal shipping:** CCRI started its coastal shipping operations in Jan'19, partnering with a private shipping company, by deploying two dedicated vessels with 700TEU capacity each. CCRI provides end-to-end services including first- and last-mile connectivity, port handling and coastal transportation between Kandla and Tuticorin Port, via the Mangalore and Cochin ports. Given the vast potential for the coastal shipping/inland water movement industry, management believes that this business can attain sizable scale in coming years.
- **Distribution logistics:** Considering the vast 3PL potential in the post GST era, CCRI plans to open up ~20 distribution centres across the country and has floated tenders for two distribution warehouses in Chennai and Tripura.
- **International ventures:** The company is in the early stages of two of its international forays – (1) it is the leader of one of three consortiums competing for a dry port/ICD in Cairo, Egypt; and (2) it has signed an MoU with JSC RZD Logistics of Russia to explore opportunities in international logistics.

International ventures are at early stages

Management taking agile steps to stay ahead of the curve

Proactive management with deep industry expertise provides an edge

In a difficult business environment, CCRI's management has taken several proactive decisions to stay ahead of competition. Apart from the long-term initiatives mentioned above, some other notable steps taken in FY19 YTD are –

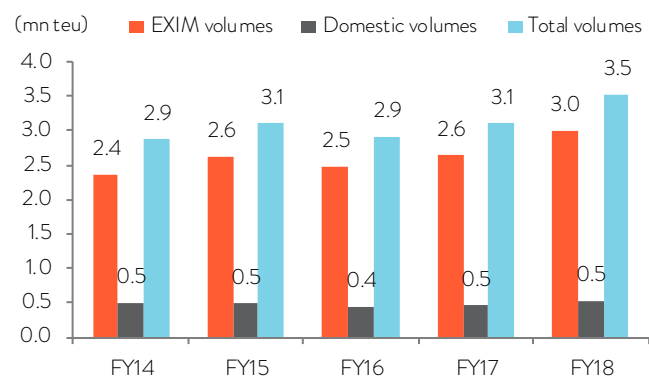
- 45 days of free storage launched at its EXIM terminals to attract volumes;
- freight rates proactively increased by Rs 1,000/TEU in May'18 and service charges hiked by Rs 1,500/TEU in Aug'18, which helped offset IR's haulage charge increase (~Rs 500/TEU);
- double-stacking volumes gradually increased over the past three years to ~2,300 trains in 9MFY19 from ~350 trains in FY16; and
- several terminals established around the upcoming DFC corridor.

Financial review

Revenue grew a modest 4% over FY14-FY18

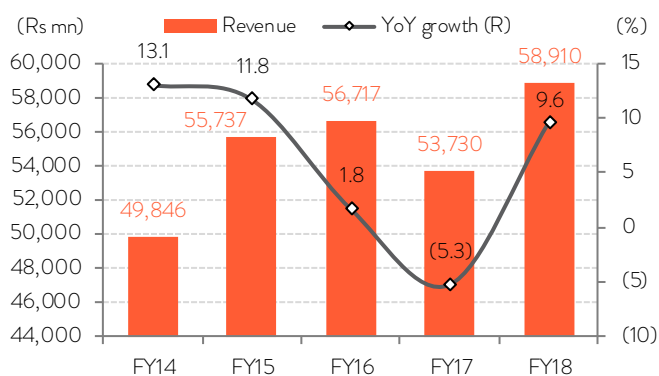
Over FY14-FY18, CCRI's standalone revenue clocked a CAGR of 4.3%. While volumes posted a 5.3% CAGR (6.2% in EXIM, 1.1% in domestic), falling lead distances meant realisation/TEU declined at a 1% CAGR. But realisation/TEU/km, which does not include distance, grew at a steady 4.7%. Note that we have classified export incentives received from the government under the Service Exports from India Scheme (SEIS) as part of other income and not revenue.

FIG 17 – VOLUMES GREW AT A STABLE 5.3% CAGR...



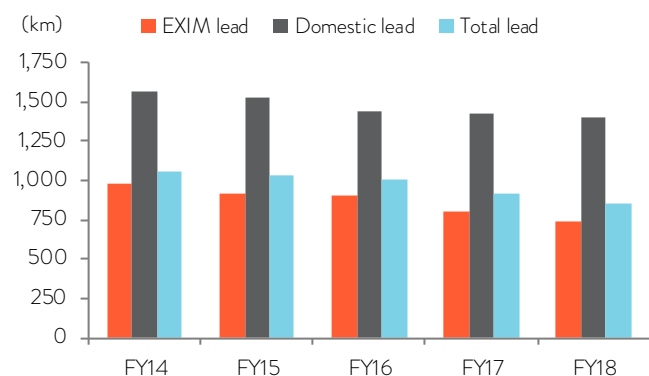
Source: Company, BOBCAPS Research

FIG 18 – ...BUT REVENUE GREW SLOWER AT 4.3% CAGR OVER FY14-FY18



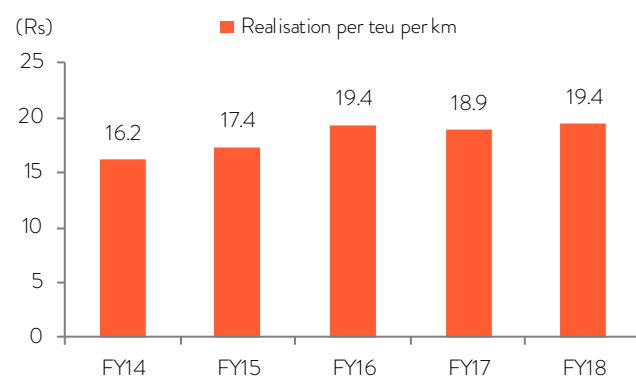
Source: Company, BOBCAPS Research

FIG 19 – LEAD DISTANCE DECLINED SHARPLY FOR BOTH EXIM AND DOMESTIC SEGMENTS



Source: Company, BOBCAPS Research

FIG 20 – REALISATION PER TEU KM EXHIBITED A BETTER TREND



Source: Company, BOBCAPS Research

DFC to boost volume and revenue growth in FY21

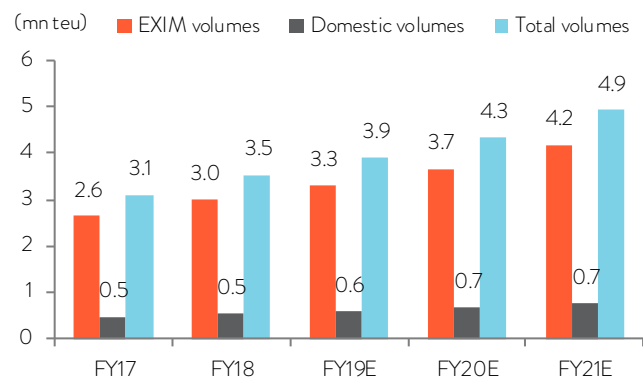
Expect a revenue CAGR of 13% over FY19-FY21

We expect the rollout of DFC to usher in a new growth era for CCRI. Industry sources expect the first leg of the western corridor (WDFC) from Rewari to Palanpur to be completed by Sep'19, which would connect to the Gujarat ports. While substantial progress indicates likelihood of timely commissioning, we have cautiously factored in DFC related benefits from FY21 only.

We expect WDFC commissioning to fuel some shift in container traffic from road to rail, though full benefits will only be visible once the stretch up to JNPT is completed. As CCRI is most suited to gain from the shift, we have factored in some benefits from DFC in FY21. Accordingly, we forecast a healthy 12.5% volume CAGR for the company over FY19-FY21.

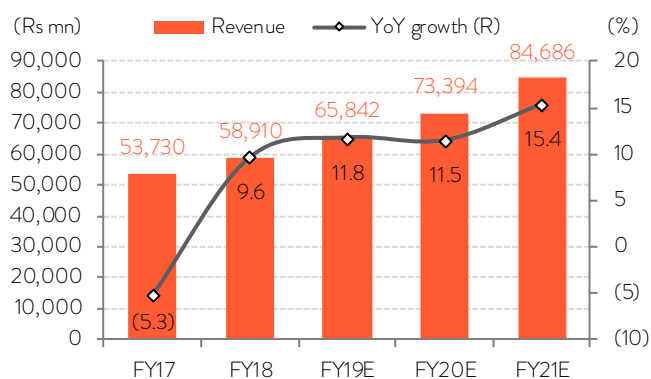
WDFC is also expected to improve hinterland connectivity with JNPT by rail, which coupled with ramp-up in the recently commissioned Bharat Mumbai Container Terminal (BMCT) at JNPT should help stem the decline in EXIM lead distance. We expect CCRI's EXIM lead to stabilise at ~680km by FY21 from 740km in FY18, while domestic lead distance is expected to settle at ~1,400km, similar to current levels. Realisation/TEU/km is forecast to increase at a ~1% CAGR over FY19-FY21, aiding a revenue CAGR of 13% to Rs 87.4bn.

FIG 21 – EXPECT STRONG VOLUME CAGR OF 12.5% OVER FY19-FY21



Source: Company, BOBCAPS Research

FIG 22 – REVENUE FORECAST TO GROW AT 13% CAGR OVER FY19-FY21



Source: Company, BOBCAPS Research

Forecast sturdy 17% CAGR in EBITDA; 160 bps margin expansion over FY19-FY21

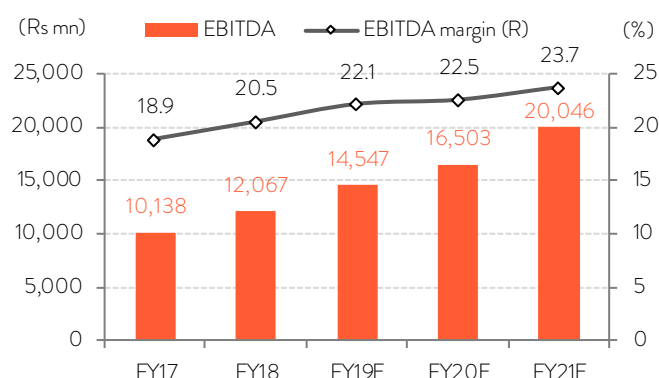
Double-stacking, efficiency gains to drive margins

Apart from aiding a shift from road to rail, we expect the DFC to fuel margin improvement for CCRI by enabling higher double-stack running and also efficiency gains from lower turnaround time. As mentioned, we expect a part of the DFC to start operating from FY21 onwards, leading to margin gains. Additionally, operating leverage benefits are also likely to trickle in, stemming from higher volumes. Consequently, we model for 160bps expansion in CCRI's

EBITDA margin over FY19-FY21 to 23.7%. This implies a sturdy 17.4% CAGR in EBITDA during the same period.

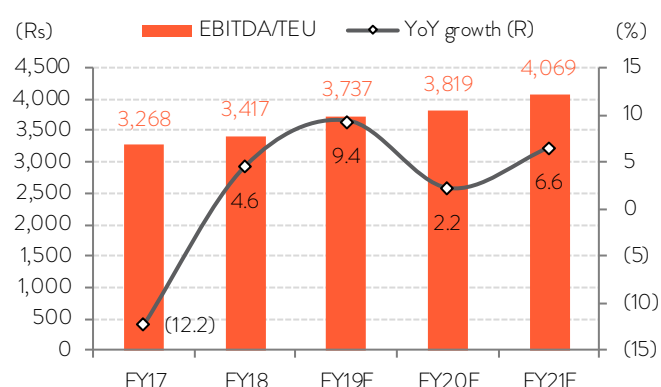
Our EBITDA forecast does not factor in, and is therefore exposed to, two downside risks – further delay in commissioning of the Rewari-Palanpur DFC stretch and a sharp increase in haulage charges by the IR.

FIG 23 – EBITDA MARGIN FORECAST TO IMPROVE 160BPS OVER FY19-FY21



Source: Company, BOBCAPS Research

FIG 24 – EBITDA PER TEU TO TREND UPWARDS LED BY EFFICIENCY GAINS

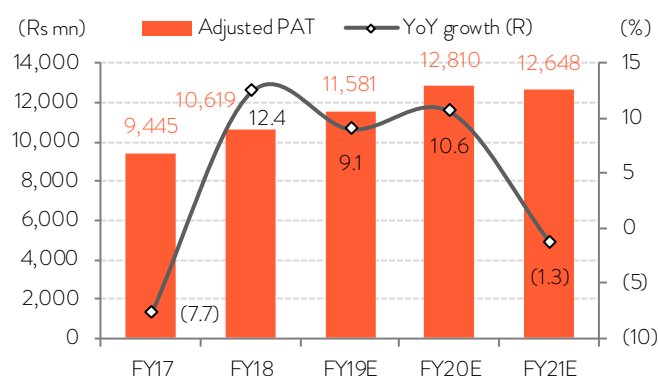


Source: Company, BOBCAPS Research

Sedate PAT growth as SEIS income expires in FY20

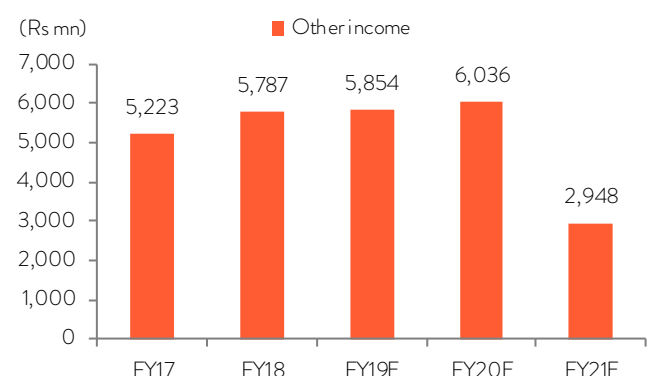
Despite strong operating profit, adj. PAT is expected to grow at a subdued 4.5% CAGR over FY19-FY21, owing to a fall in other income in FY21. We have not factored in any income from SEIS (assumed to be part of other income in FY19-20) in FY21, as the government notification stipulates the benefit only for FY15-FY20. As a result, other income is projected to drop to Rs 2.9bn in FY21 from Rs 6bn in FY20 (which includes Rs 3.3bn of SEIS income). In case the SEIS income is extended for FY21, it will be an upside to our estimates.

FIG 25 – ADJ. PAT TO GROW AT A SUBDUED 4.5% CAGR...



Source: Company, BOBCAPS Research

FIG 26 – ...AS SEIS INCOME EXPIRES IN FY20, LEADING TO LOWER OTHER INCOME



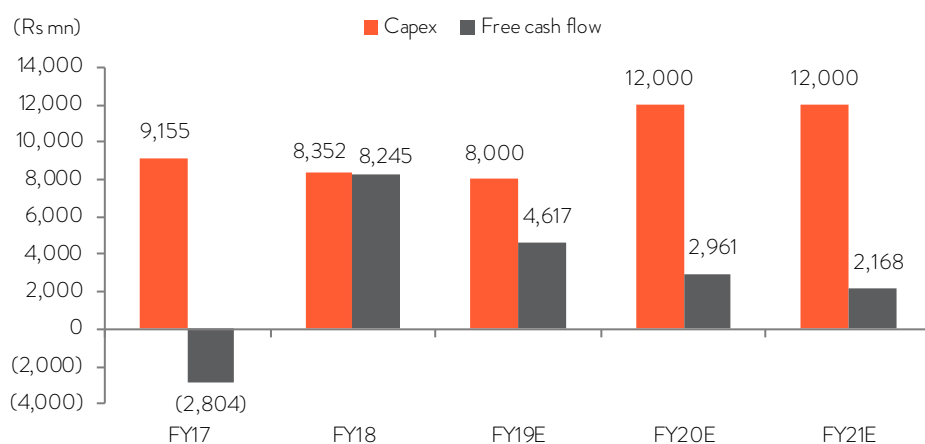
Source: Company, BOBCAPS Research

Elevated capex of Rs 60-80 bn over the next five years to keep FCF generation moderate

Moderate FCF generation owing to elevated capex

To prepare for the DFC, CCRI has embarked on a Rs 60bn-80bn capex plan over FY17-FY22. This will include capex outgo towards new high-speed rakes (270 rakes to be added for ~Rs 4.5bn from H2FY20 onwards), high-speed wagons, and investments in terminal infrastructure/multi-modal logistics parks (MMLP). We build in capex of Rs 12bn each in FY20-FY21. Accordingly, free cash flow (FCF) generation is likely to be moderate over these two years vis-à-vis the historic run-rate.

FIG 27 – FCF GENERATION TO BE SUPPRESSED DUE TO HIGHER CAPEX



Source: Company, BOBCAPS Research

Valuation methodology

**Initiate coverage with
REDUCE and Mar'20 TP of
Rs 530**

We value CCRI using the P/E methodology. Factoring in the anticipated boost from the upcoming freight corridor, we have assigned a multiple of 25x to standalone FY21E EPS, yielding a Mar'20 target price of Rs 530. Our target P/E is at a ~25% premium to the stock's average one-year forward multiple for the last ten years (20x) and is in line with the past five-year average (25x). We value the investments in JVs and subsidiaries at 0.8x FY21E P/B (Rs 10/sh). The current share price of Rs 523 factors in most of the positives and hence we initiate coverage with REDUCE.

**Our 25x 1-yr fwd P/E
multiple is in line with 5-yr
avg. trading P/E**

We note that expectations of DFC benefits have seen the stock trade at premium valuations over the past five years (25x vs. 14x during the previous five years), despite moderate operational performance. In our opinion, the steady-state business ex-DFC merits a 17-18x one-year forward P/E multiple at most, which implies that DFC benefits account for ~40% of the current valuation. Hence, even with commissioning of the freight corridor, we see limited scope for a material P/E re-rating.

FIG 28 – KEY VALUATION ASSUMPTIONS

Rs per share	
FY21E EPS	20.8
P/E multiple applied (x)	25
Value of the core business	520
Value of investments in JVs and subsidiaries	10
Total target price	530

Source: BOBCAPS Research

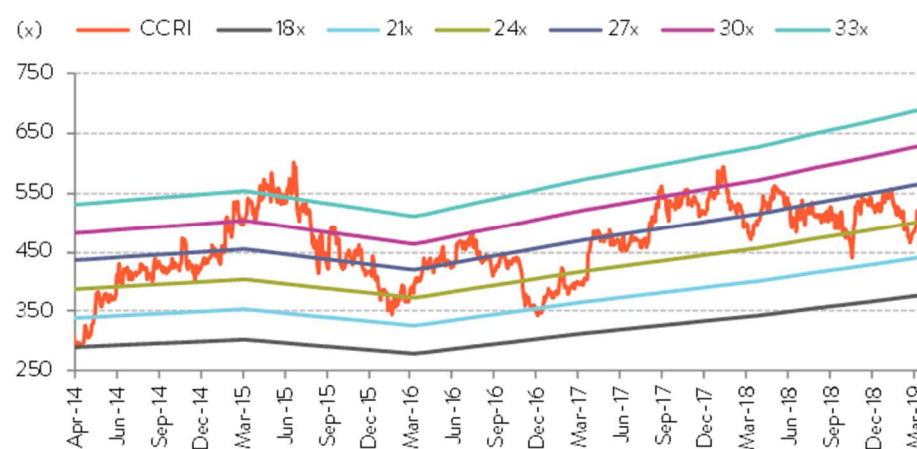
To corroborate our valuation using the multiple method, we have also conducted a DCF valuation. Despite factoring in the benefits stemming from the freight corridor, our DCF valuation converges with our P/E-based valuation, indicating limited upside from current levels.

We have projected CCRI's FCF till FY30, beyond our explicit projection period of FY19-FY21. We have assumed a volume/revenue CAGR of 20%/22% over FY19-FY25 (with FY22-FY25 expected to be the high growth phase post DFC commissioning) and 15%/17% over FY19-FY30. Building in margin improvement, we forecast EBITDA growth of 31% and 20% over FY19-FY25 and FY19-FY30 respectively. We have used a 14% weighted average cost of capital to discount the FCF generated over FY21-FY30 and assumed a terminal growth rate of 3%. Based on these assumptions, we arrive at a target price of Rs 534, similar to our multiple-based valuation.

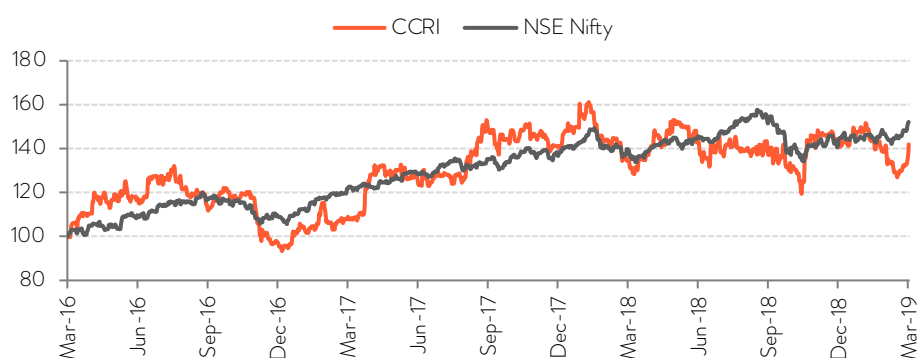
FIG 29 – KEY DCF ASSUMPTIONS

(%)	FY19-FY25	FY19-FY30
Volume CAGR	20.0	15.0
Revenue CAGR	21.8	16.5
EBITDA CAGR	30.8	20.2
PAT CAGR	25.8	18.4
Cost of capital	14	
Terminal growth rate	3	
Target price (Rs/share)	534	

Source: BOBCAPS Research

FIG 30 – ONE-YEAR FORWARD P/E BAND

Source: Bloomberg, BOBCAPS Research

FIG 31 – RELATIVE STOCK PERFORMANCE

Source: NSE

Key risks

- **Sharp increase in haulage charges:** As witnessed in the past, a sharp increase in haulage charge can adversely affect CCRI's volumes/EBITDA margin. There is a possibility of haulage charge escalation after DFC commissioning. While CCRI can pass on the hike to customers to a certain extent, a sharp rise in haulage charges is likely to deplete margins.
- **Execution delays in DFC:** While we have factored in some delays beyond the scheduled H2FY20 commissioning of DFC phase-one (Dadri to Palanpur), any further unforeseen delays in execution will pose a downside risk to our estimates.
- **Prolonged trade slowdown:** Given CCRI's reliance on India EXIM trade, any prolonged slowdown in India's foreign trade is likely to adversely impact volumes. Moreover, a rise in the imbalance between imports and exports can lead to higher empty running charges, thereby affecting margins.
- **Steep decline in fuel price:** In the past, a sharp decline in diesel price has led to an increase in freight rate divergence between rail and road, hurting CCRI's volumes. Any such decline in future can intermittently lower the company's market share vis-à-vis road and affect volumes.

Management overview

FIG 32 – KEY MANAGEMENT PERSONNEL

Name	Brief profile
Mr. V. Kalyana Rama Chairman and Managing Director	Mr. V Kalyana Rama is a Mechanical Engineer with ICFAI. He is an Indian Railway Traffic Service (IRTS) officer of 1987 batch. He had worked in BHPV & BHEL before joining Indian Railways. Prior to joining Board of Directors of CCRI as Director (Projects & Services), he held various assignments such as Executive Director, Chief General Manager in CCRI.
Mr. Pradip Kumar Agrawal Director (Domestic)	Mr. Pradip Kumar Agrawal has taken over the charge of Director (Domestic Division) from 1st July, 2016. He belongs to Indian Railway Traffic Service. He has worked for Indian Railways for more than 17 years on various assignments, both at Divisional and Zonal Headquarter level covering operations, commercial, marketing and safety of Indian Railways. He joined CCRI in the year 2006 as GGM (Ops)/Western Region, thereafter, worked as Chief General Manager, Western Region for four years.
Mr. Sanjay Swarup Director (International Marketing & Operations)	Mr. Sanjay Swarup has done his B.E. (Hons.)- Electronics and Communication Engineering from IIT Roorkee and PGDM from IIM Bangalore. He belongs to 1990 Batch of Indian Railway Traffic Service. His 31-year career spans a range of assignments in Public Sector and Government. He started his career in Bharat Heavy Electricals Ltd. and followed by various assignment with the Indian Railways in various capacities.
Mr. Rahul Mithal Director (Projects and Services)	Mr. Rahul Mithal is from the Indian Railways Service of Mechanical Engineers (SCRA 1985 Batch). He has had a long stint of more than 20 years in various key positions in Indian Railways. In the last 6 years in CCRI, he has been closely associated with various mega Projects and has played a key role in drafting the Strategic Plan : Vision 2020 of the Company.
Manoj Kumar Dubey Director (Finance)	Mr. Manoj K. Dubey did his under graduation and post-graduation from the Hindu College of the University of Delhi. Before clearing Civil Service and joining IRAS of 1993 batch, he worked with UTI for two years. He did his MBA at Department of Management Studies of Indian School of Mines, Dhanbad and with specialization in Finance and Human Resources.
Mr. Sanjay Bajpai ED/Traffic (Co-ordination)/ Railway Board Part-Time Government Director	Mr. Sanjay Bajpai, Executive Director/Traffic (Co-ordination), Railway Board, an officer of the Indian Railway Traffic Service 1991 batch, joined Indian Railways in 1992. He is a Post-Graduate in Economics from Allahabad University. He has had vast and varied experience in railway operations, commercial working, general administration.
Mr. Manoj Kumar Srivastava ED/Traffic Transportation (Freight)/ Railway Board Government Director	Mr. Manoj Kumar Srivastava, is an officer of the Indian Railway Traffic Service of 1988 batch. He is a Post-Graduate in Geology and has vast experience in railway operations, commercial working and general administration.

Source: Company, BOBCAPS Research

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Total revenue	53,730	58,910	65,842	73,394	84,686
EBITDA	10,138	12,067	14,547	16,503	20,046
EBIT	6,619	8,141	10,298	11,755	14,618
Net interest income/(expenses)	(37)	(1)	(1)	0	0
Other income/(expenses)	5,223	5,787	5,854	6,036	2,948
Exceptional items	0	0	0	0	0
EBT	11,806	13,926	16,152	17,792	17,566
Income taxes	(2,361)	(3,307)	(4,571)	(4,982)	(4,919)
Extraordinary items	(865)	(129)	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	8,580	10,490	11,581	12,810	12,648
Adjustments	865	129	0	0	0
Adjusted net profit	9,445	10,619	11,581	12,810	12,648

Balance Sheet

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Accounts payables	2,415	2,542	2,790	3,097	3,532
Other current liabilities	5,069	7,010	7,216	8,043	9,281
Provisions	686	704	692	771	890
Debt funds	373	334	0	0	0
Other liabilities	0	0	0	0	0
Equity capital	1,950	2,437	3,046	3,046	3,046
Reserves & surplus	86,512	91,574	97,659	1,07,380	1,16,978
Shareholders' fund	88,462	94,011	1,00,705	1,10,426	1,20,025
Total liabilities and equities	97,004	1,04,601	1,11,403	1,22,338	1,33,728
Cash and cash eq.	16,835	19,817	19,212	19,084	18,203
Accounts receivables	425	604	675	753	868
Inventories	225	274	306	341	394
Other current assets	8,715	10,838	11,972	13,346	15,399
Investments	13,737	13,890	13,890	13,890	13,890
Net fixed assets	33,594	36,384	46,846	54,098	60,670
CWIP	5,071	6,710	0	0	0
Intangible assets	104	100	100	100	100
Deferred tax assets, net	(2,402)	(1,877)	(1,877)	(1,877)	(1,877)
Other assets	20,700	17,861	20,278	22,604	26,081
Total assets	97,004	1,04,601	1,11,403	1,22,338	1,33,728

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Net income + Depreciation	12,964	14,546	15,829	17,558	18,076
Interest expenses	37	1	1	0	0
Non-cash adjustments	(862)	(525)	0	0	0
Changes in working capital	(5,787)	2,575	(3,213)	(2,597)	(3,908)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	6,351	16,597	12,617	14,961	14,168
Capital expenditures	(9,155)	(8,352)	(8,000)	(12,000)	(12,000)
Change in investments	(161)	(153)	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(9,316)	(8,505)	(8,000)	(12,000)	(12,000)
Equities issued/Others	0	488	609	0	0
Debt raised/repaid	(95)	(39)	(334)	0	0
Interest expenses	(37)	(1)	(1)	0	0
Dividends paid	(3,700)	(4,168)	(4,887)	(3,089)	(3,050)
Other financing cash flows	(740)	(1,390)	(609)	0	0
Cash flow from financing	(4,571)	(5,110)	(5,221)	(3,089)	(3,050)
Changes in cash and cash eq.	(7,536)	2,982	(605)	(128)	(882)
Closing cash and cash eq.	16,835	19,817	19,212	19,084	18,203

Per Share

Y/E 31 Mar (Rs)	FY17A	FY18A	FY19E	FY20E	FY21E
Reported EPS	14.1	17.2	19.0	21.0	20.8
Adjusted EPS	15.5	17.4	19.0	21.0	20.8
Dividend per share	6.1	6.8	8.0	5.1	5.0
Book value per share	145.2	154.3	165.3	181.2	197.0

Valuations Ratios

Y/E 31 Mar (x)	FY17A	FY18A	FY19E	FY20E	FY21E
EV/Sales	5.5	5.1	4.5	4.1	3.5
EV/EBITDA	29.0	25.0	20.5	18.1	14.9
Adjusted P/E	33.7	30.0	27.5	24.9	25.2
P/BV	3.6	3.4	3.2	2.9	2.7

DuPont Analysis

Y/E 31 Mar (%)	FY17A	FY18A	FY19E	FY20E	FY21E
Tax burden (Net profit/PBT)	80.0	76.3	71.7	72.0	72.0
Interest burden (PBT/EBIT)	178.4	171.1	156.8	151.3	120.2
EBIT margin (EBIT/Revenue)	12.3	13.8	15.6	16.0	17.3
Asset turnover (Revenue/Avg TA)	0.6	0.6	0.7	0.7	0.7
Leverage (Avg TA/Avg Equity)	1.0	1.0	1.0	1.0	1.0
Adjusted ROAE	11.0	11.6	11.9	12.1	11.0

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY17A	FY18A	FY19E	FY20E	FY21E
YoY growth (%)					
Revenue	(5.3)	9.6	11.8	11.5	15.4
EBITDA	(6.9)	19.0	20.5	13.4	21.5
Adjusted EPS	(7.7)	12.4	9.1	10.6	(1.3)
Profitability & Return ratios (%)					
EBITDA margin	18.9	20.5	22.1	22.5	23.7
EBIT margin	12.3	13.8	15.6	16.0	17.3
Adjusted profit margin	17.6	18.0	17.6	17.5	14.9
Adjusted ROAE	11.0	11.6	11.9	12.1	11.0
ROCE	7.4	8.7	10.4	10.9	12.5
Working capital days (days)					
Receivables	3	4	4	4	4
Inventory	2	2	2	2	2
Payables	20	20	20	20	20
Ratios (x)					
Gross asset turnover	1.5	1.3	1.2	1.1	1.1
Current ratio	3.4	3.2	3.2	3.0	2.7
Net interest coverage ratio	NM	NM	NM	NM	NM
Adjusted debt/equity	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)

Source: Company, BOBCAPS Research

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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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