# Container Corporation of India

## Volume growth elusive; street optimism misplaced

**Equities**

India
Transportation Services

| | |
|---|---|
| **12-month rating** | **Sell** |
| **12m price target** | **Rs1,050.00** |
| | *Prior: Rs1,380.00* |
| **Price** | **Rs1,176.20** |

**RIC:** CCRI.BO **BBG:** CCRI IB

**Trading data and key metrics**

| | |
|---|---|
| **52-wk range** | Rs1,880.95-1,082.70 |
| **Market cap.** | Rs229bn/US$3.35bn |
| **Shares o/s** | 195m (ORD) |
| **Free float** | 37% |
| **Avg. daily volume ('000)** | 306 |
| **Avg. daily value (m)** | Rs385.0 |
| **Common s/h equity (03/16E)** | Rs81.4bn |
| **P/BV (03/16E)** | 2.8x |
| **Net debt / EBITDA (03/16E)** | NM |

**EPS (UBS, diluted) (Rs)**

| | From | To | % ch | Cons. |
|---|---|---|---|---|
| **03/16E** | 48.44 | 45.04 | -7 | 48.04 |
| **03/17E** | 53.22 | 48.90 | -8 | 54.48 |
| **03/18E** | 63.48 | 54.67 | -14 | 61.18 |

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### Weak EXIM volumes and impact of rail freight charges continue to hurt

We believe consensus expectations of 9-10% volume growth in FY17/18 (assuming 3-4% realization improvement) are optimistic compared with our volume growth estimates of 5.0%/7.2%. In our view, strong macro headwinds in export-import (EXIM) trade and a weak domestic market will likely result in elusive volume growth for Container Corp. (Concor). We believe container train operators (CTOs) are seeing traffic shift from rail to road as the latter offers better pricing backed by lower fuel costs and overcapacity. We cut our FY16/17/18 earnings estimates by 7%/8%/14% as we expect: 1) lower volume growth; and 2) management is unlikely to increase realization rates meaningfully in a weak demand environment. In the past six to seven months, the share price has corrected by 40% and based on consensus estimates, it is trading at 21.8x FY17F PE; still higher than its five-year average (19.0x). We think a rerating will be difficult given impending earnings cuts and the likely weak macro environment. We maintain our Sell rating.

### Missing levers for operating margin expansion through cost cutting

Empty haulage charges, rebates and a higher proportion of rail freight charges as a percentage of operating costs leaves limited leeway for management to drive an operating margin expansion. We believe erratic movement in the trade imbalance (export-import gap) will remain an area of concern as it leads to higher empty haulage charges. Management's earlier strategy of using rebates (especially for export cargo) for volume gain will continue to impact margins, whereas reducing the use of rebates could lead to volume loss. We see limited scope for operating margin expansion in our base-case scenario.

### Uncertainties around the quantum of Dedicated Freight Corridor (DFC) benefits

We think the DFC is going to be big driver for container train volumes but uncertainty looms around DFC's track access charges, which will govern operating costs for CTOs. Subsequent increases in rail freight charges for DFC usage could offset CTOs' financial gains, in our view. Further, our on-the-ground checks suggest DFC commencement is not due before FY20, while part of it may be available for use by FY18/19.

### Valuation: maintain Sell rating; cut price target to Rs1,050.00 (from Rs1,380.00)

We value the stock using a DCF methodology (assuming a WACC of 11.3% and terminal growth of 4% in FY25). At our price target, the stock would trade at 21.4x FY17E PE and 13.3x EV/EBITDA.

| Highlights (Rsm) | 03/13 | 03/14 | 03/15 | 03/16E | 03/17E | 03/18E | 03/19E | 03/20E |
|---|---|---|---|---|---|---|---|---|
| **Revenues** | 44,450 | 53,167 | 61,493 | 58,978 | 63,765 | 70,497 | 80,721 | 94,661 |
| **EBIT (UBS)** | 8,732 | 9,166 | 9,912 | 8,449 | 9,600 | 11,131 | 13,740 | 17,479 |
| **Net earnings (UBS)** | 9,306 | 9,450 | 10,540 | 8,782 | 9,534 | 10,659 | 12,728 | 15,830 |
| **EPS (UBS, diluted) (Rs)** | 47.73 | 48.47 | 54.06 | 45.04 | 48.90 | 54.67 | 65.28 | 81.19 |
| **DPS (Rs)** | 11.67 | 12.30 | 14.00 | 15.00 | 16.50 | 19.00 | 23.00 | 28.00 |
| **Net (debt) / cash** | 28,974 | 26,371 | 27,975 | 25,497 | 24,271 | 23,945 | 26,068 | 30,363 |
| **Profitability/valuation** | **03/13** | **03/14** | **03/15** | **03/16E** | **03/17E** | **03/18E** | **03/19E** | **03/20E** |
| **EBIT margin %** | 19.6 | 17.2 | 16.1 | 14.3 | 15.1 | 15.8 | 17.0 | 18.5 |
| **ROIC (EBIT) %** | 31.2 | 27.3 | 24.5 | 17.9 | 17.6 | 18.1 | 20.4 | 24.1 |
| **EV/EBITDA (core) x** | 8.7 | 9.7 | 15.8 | 16.5 | 14.8 | 13.0 | 10.9 | 8.9 |
| **P/E (UBS, diluted) x** | 13.2 | 15.2 | 24.0 | 26.1 | 24.1 | 21.5 | 18.0 | 14.5 |
| **Equity FCF (UBS) yield %** | 2.6 | 4.2 | 2.0 | 0.9 | 1.6 | 2.3 | 3.9 | 5.4 |
| **Net dividend yield %** | 1.9 | 1.7 | 1.1 | 1.3 | 1.4 | 1.6 | 2.0 | 2.4 |

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of Rs1,176.20 on 17 Feb 2016 22:36 HKT

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**UBS Research THESIS MAP** a guide to our thinking and what's where in this report

OUR THESIS IN PICTURES →

PIVOTAL QUESTIONS

**Q: Can Concor grow volumes by 9-10% in the next two years?**

Less likely. Concor's volume growth is highly geared to 1) growth in EXIM containers volume, 2) intensity of competition from other private players, and 3) the road sector. We expect all three drivers to be unfavourable for Concor in the next two years.

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**Q: Can EBITDA margins expand via cost cutting, against a low-volume growth backdrop?**

Limited likelihood. We think a low-volume growth environment provides limited room for Concor to pass on rail freight charge increases, lower rebates and other cost items to drive operating margin expansion.

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**Q: Will Concor's operating costs drop by 20-30% on commencement of Dedicated Freight Corri dor (DFC), driving a near doubling of its volume over the subsequent two to three years post DFC?**

Unclear. The DFC will likely lower operating costs but there is uncertainty whether these savings will be retained by Indian Railways (IR) or passed on to container train operators.

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UBS VIEW

Sell. Concor is facing strong macro headwinds of weak EXIM container growth and the impact of high rail freight charges resulting in potential market share loss. Consensus earnings forecasts have been revised lower on the back of weak growth guidance but we see further earnings cuts over the next two to three quarters. We think the markets may be overly optimistic about the likely benefits of DFC.

EVIDENCE

**Weak macro and increase in rail freight charges is a double whammy:** The increase in rail freight charges in a weak macro environment has led Concor to lose market share, resulting in a decline in operating margins inr 9MFY16. Negative volume growth of 6.8% YoY in 9MFY16 is the lowest after FY09 and is indicative of the company's vulnerability to these external events.

WHAT'S PRICED IN?

Our residual income methodology indicates that a significant proportion (c61%) of Concor's current share price is explained by long-term growth expectations. This is much higher than the period prior to 2014 (Figure 10) and implies a structural shift in market expectations on Concor's long-term outlook; we think this is in anticipation of the DFC's benefits, which are not yet clear.

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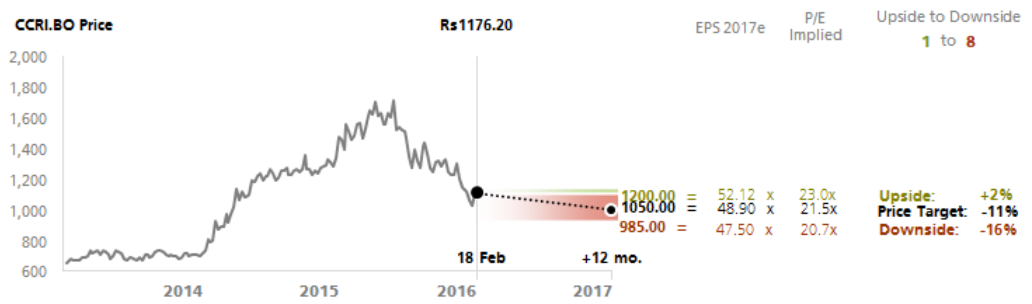
UPSIDE / DOWNSIDE SPECTRUM




| Value drivers | Volume growth | Realization growth | Terminal charges as % of revenue | EBITDA margin |
|---|---|---|---|---|
| Rs1,200 upside | 6.4% | 3.4% | 70.0% | 22.1% |
| Rs1,050 target | 5.0% | 2.9% | 70.5% | 21.1% |
| Rs985 downside | 3.5% | 1.9% | 71.5% | 20.0% |

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COMPANY DESCRIPTION

Container Concor is a leading container train operator and complements its service through 63 CFS and ICD facilities, largely in cargo hubs across India. Of these, 13 are for international cargo and 15 for domestic cargo, with the remainder handling both. Concor has a market share of 74% of rail container

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## OUR THESIS IN PICTURES

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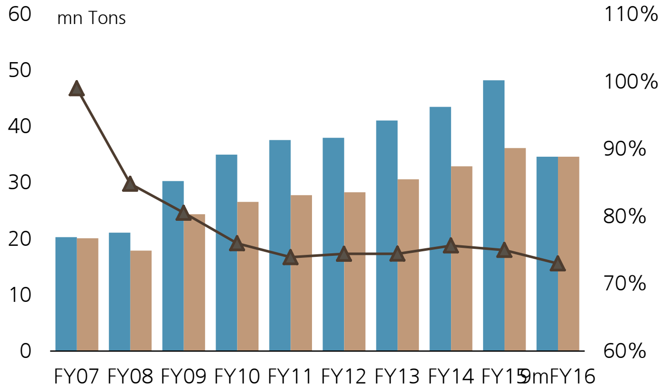
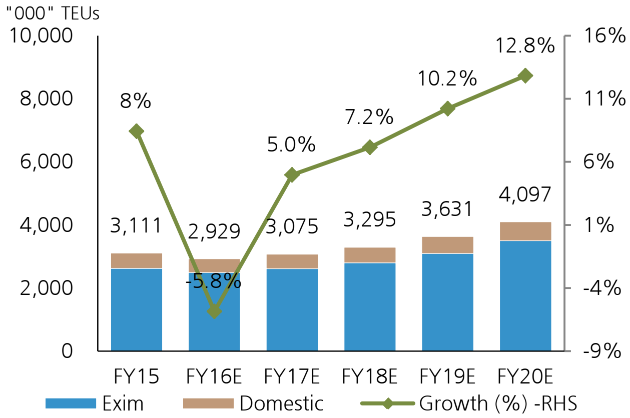
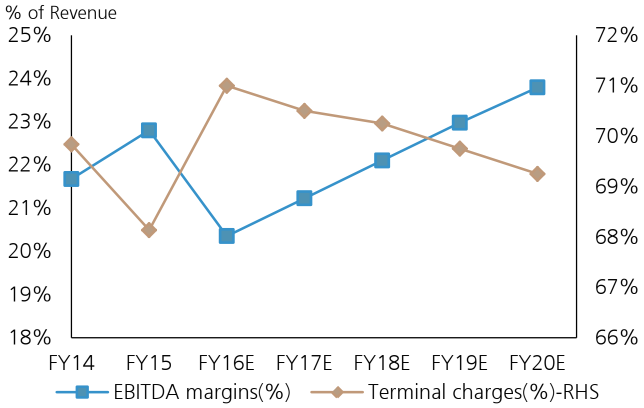


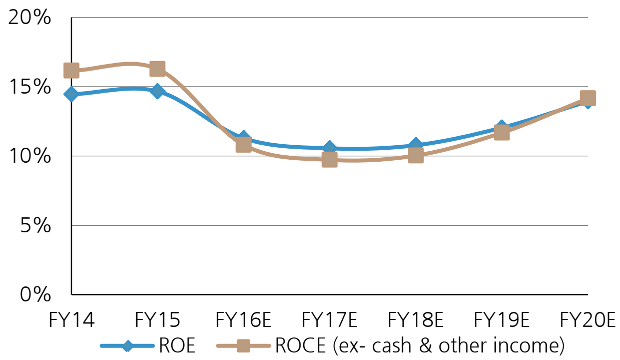

**Concor remains the market leader but has lost market share from 74.3% in 9MFY15 to 72.8%in 9MFY16**




**We expect a volume growth revival from -5.8% in FY16 to 5.0% in FY17**




**Increased terminal charges passed on to customers gradually may lead to some EBITDA margin improvement**




**Long-term case for improvement in ROE/ROCE on the back of margin expansion and higher capacity utilization**

# OUR THESIS IN PICTURES

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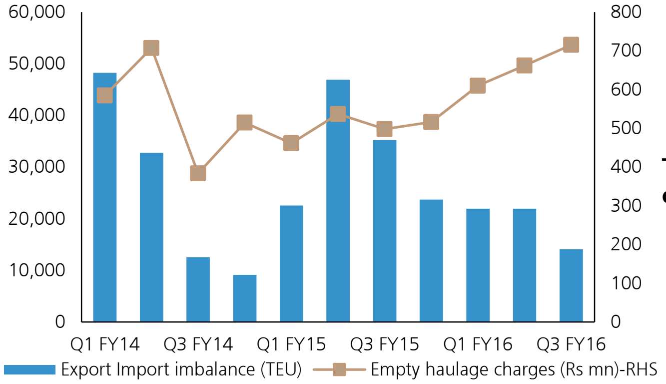
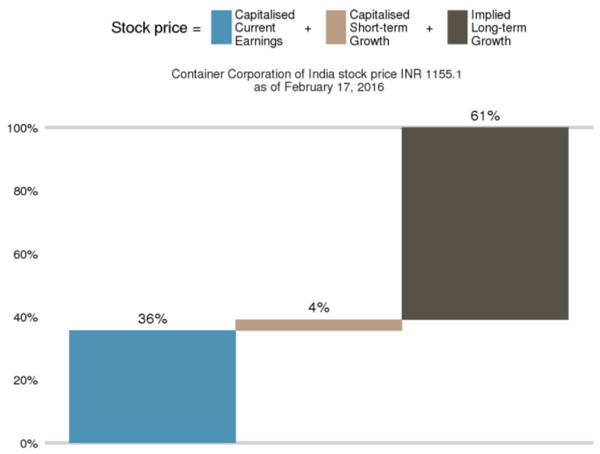
Export-import gap (TEU)



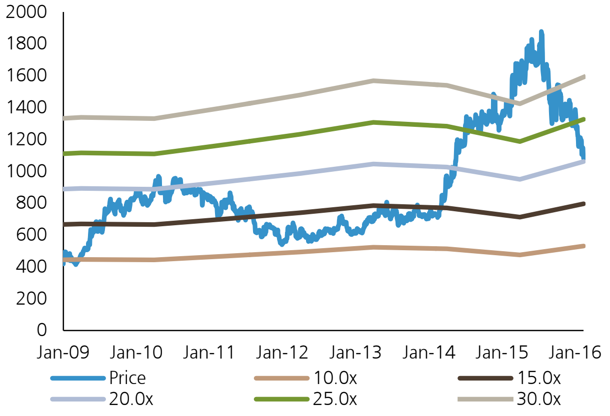

**Trade imbalance may lead to higher empty haulage charges**

Residual income model




**A significant proportion (c61%) of Concor's current share price is explained by long-term growth expectations**

PE bands




**The stock is trading at a one-year fwd PE multiple of 21.8x, based on consensus earnings estimates, which is higher than its five-year average (19.0x). We think a rerating will be difficult, given impending earnings cuts and a likely weak macro environment**

Sources for exhibits above: Company data, UBS Research



Sources for exhibits above: Company data, UBS Research

PIVOTAL QUESTIONS

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# Q: Can Concor grow volumes by 9-10% in the next two years?

### UBS VIEW

Less likely. Concor volume growth is highly geared to 1) growth in EXIM containers volumes, 2) intensity of competition from other private players, and 3) the road sector. We expect all three drivers to be unfavourable for Concor in the next two years. We do not expect a strong revival in EXIM volumes and expect Concor to remain vulnerable to external events, resulting in potential market share loss. The increase in rail freight charges, decrease in diesel fuel prices and overcapacity in the road transport sector have shifted container cargo from rail to road, and we expect rail operators to have limited scope to recover volumes.

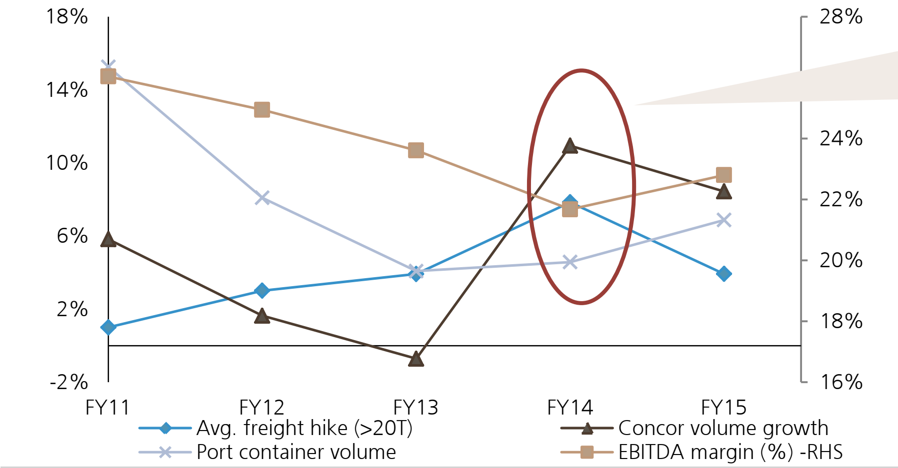
### EVIDENCE

Historically, Concor's volume growth has been dependent on EXIM container volume growth at ports and increases in rail freight charges. In a strong macro environment, volume growth for CTOs is less elastic with respect to rail freight charges, whereas elasticity increases in a weaker environment. The increase in rail freight charges by Indian Railways in FY16 is the highest in the recent past, and we expect CTOs to experience weak volume growth as a result of this.

## Volume growth in relation to EXIM growth and rail freight charges

Concor's volume growth is geared to Indian ports' container volume growth and management's ability to pass on any increase in rail freight costs. Historically, management has been able to gain volume by offering rebates amid a weak macro environment, which has then led to lower operating margins. We believe rail freight increases of ~25-30% in FY16 have left limited leeway for management to offer rebates. According to industry sources, 9MFY16 port volume growth is estimated at 2-3% compared with Concor's negative growth of 6.8%, indicating a loss of market share.

**Figure 1: Concor volume growth in relation to freight hikes (%)**



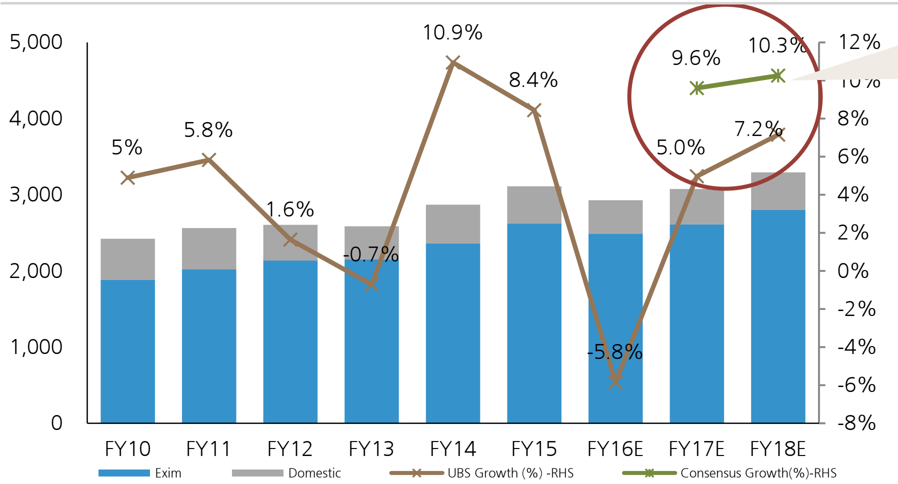

Source: Reuters, company data

Higher volume growth in FY14 as Concor gained market share by offering higher rebates and compromising on EBITDA margins

## Our volume growth estimates are lower than consensus

Consensus (Bloomberg) volume growth forecasts of 9-10% in FY17 and 10-11% in FY18 (assuming a 3-4% realization improvement), with respective margin expansion of 70bp and 90bp, are optimistic, in our view. Although FY16 is going to be a significantly low volume base year, we believe achieving ~10% volume growth in a weak macro environment is still going to be difficult, as evidenced by the historical data. Concor generated a volume CAGR of 5.1% during FY09-15, and it has achieved c10% growth only once in the past seven years.

**Figure 2: We think consensus volume growth forecasts are too optimistic**




Source: Bloomberg, Company data, UBS estimates

We think consensus volume growth forecasts of 9-10% for FY17 and FY18 are on the high side, given the weak macro environment and historical evidence

## Continuing competition from the road sector

Container train operators compete with road transporters for containers, specifically in the domestic segment and for the light-cargo part of the EXIM segment. There is a shift in container cargo from rail to road as: 1) road transporters are able to offer better pricing backed by lower diesel prices (which have declined by c10-14% YoY); and 2) overcapacity is evident in road transportation due to weak demand in the steel and commodity industries. Anecdotally, rail's share of container cargo from JNPT port has declined from c32-33% to c25-26% in the past year, as per industry experts. We do not expect competition from road transporters to weaken anytime soon, making it difficult for container train operators to recover lost volumes.

## PIVOTAL QUESTIONS

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# Q: Can EBITDA margins expand via cost cutting, against a low-volume growth backdrop?

### UBS VIEW

Limited likelihood. We think a low-volume growth environment provides limited room for Concor to: 1) pass on increases in rail freight charges, 2) lower rebates, and 3) reduce other cost items, in order to drive operating margin expansion. Managing empty haulage charges and rebates will be tricky because excessive curbing of these costs can lead to volume loss. Rail freight charges form c70% of operating charges on average, which leaves limited room to optimize other operating costs.

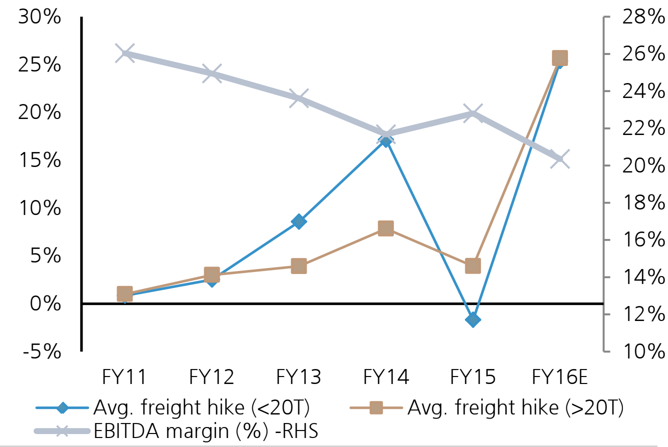
### EVIDENCE

Concor's EBITDA margin declined from 24% in 9MFY15 to 20.4% in 9MFY16 as management has been unable to pass on the higher rail freight charges applicable in FY16. The historical precedent also indicates only a gradual improvement in operating margins post previous freight hikes by Indian Railways. Historically, management has also used rebates/discounts as a tool to gain volume in a weak macro environment, while compromising on margins. We believe there is limited scope to reduce rebates in the current scenario.

## Margin dependency on rail freight charges leaves limited room for operating margin expansion

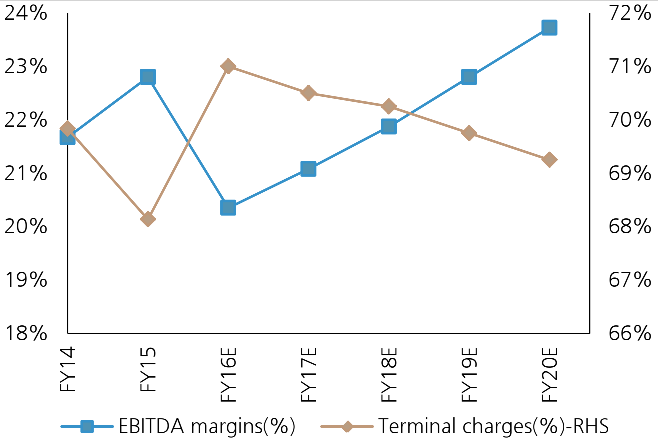
Rail freight charges are a key operating cost for container train operators and form c70% of Concor’s total operating costs. Historically, increases in rail freight charges have adversely impacted Concor’s EBITDA margin. We expect management to pass on only part of the freight charge increase to clients and will do so differently for EXIM and domestic cargo. We expect operating margin expansion to be driven by other cost items such as staff costs, rebates and discounts, repairs and other charges. However, there is limited scope for margin improvement as other cost items are relatively small.

**Figure 3: Adjusted rail freight hikes versus EBITDA (%)**




Source: Indian Railways, company data, UBS estimates

**Figure 4: Scope for gradual improvement in EBITDA (%)**

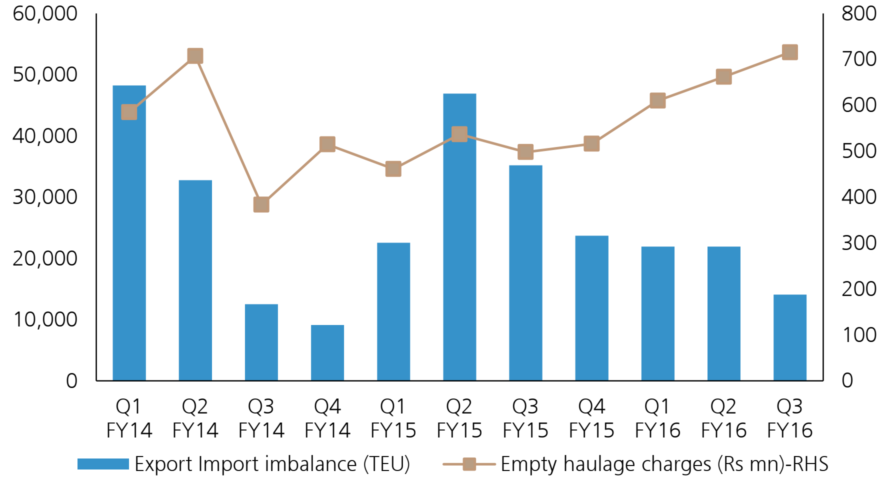



Source: Company data, UBS estimates

## Trade imbalance can be a party spoiler

Concor's empty haulage charges as a percentage of total operating costs increased significantly from 4.8% in 9MFY15 to 5.8% in 9MFY16, although the export-import (EXIM) imbalance has declined over the same period. This increase in empty haulage charges is driven by volatility and unpredictability of EXIM at various ports, which has led to higher empty haulage charges. We believe that managing empty container movement is going to be incrementally difficult and the associated costs can increase with imbalance.

**Figure 5: Export-import difference and empty haulage charges**




Source: Company data

## Change in our earnings expectations

Management has guided for a weak Q4FY16 and expects c6-7% volume growth in H1FY17. Although management is hopeful of a recovery in H2FY17, we have not found any strong evidence to support this expectation; moreover, management has missed its FY16 guidance (7-8% volume growth in 9MFY16 compared to the actual 5.8% decline during that period) by a large margin. We have cut our earnings expectations on the back of our lower volume growth estimates and management's perceived inability to pass on higher rail freight charges, in the current environment.

**Figure 6: Changes in our estimates**

| | New | | | Old | | | New versus old | | |
|---|---|---|---|---|---|---|---|---|---|
| (Rs m) | FY16E | FY17E | FY18E | FY16E | FY17E | FY18E | FY16E | FY17E | FY18E |
| Volume growth | -5.8% | 5.0% | 7.2% | 1.5% | 8.0% | 9.7% | | | |
| Revenue | 58,978 | 63,765 | 70,497 | 63,446 | 70,970 | 81,493 | -7.0% | -10.2% | -13.5% |
| EBITDA | 12,003 | 13,442 | 15,419 | 12,890 | 14,663 | 17,544 | -6.9% | -8.3% | -12.1% |
| EBITDA margin | 20.4% | 21.1% | 21.9% | 20.3% | 20.7% | 21.5% | | | |
| Adjusted net profit | 8,782 | 9,534 | 10,659 | 9,445 | 10,376 | 12,377 | -7.0% | -8.1% | -13.9% |

Source: UBS estimates

PIVOTAL QUESTIONS

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# Q: Will Concor's operating costs drop by 20-30% on commencement of Dedicated Freight Corridor (DFC), driving a near doubling of its volume over the subsequent two to three years post DFC?

UBS VIEW

Unclear. The DFC will likely lower operating costs but there is uncertainty whether these savings will be retained by Indian Railways (IR) or passed on to container train operators. Even higher traffic growth for CTOs post DFC's commencement may not translate into higher earnings growth if IR significantly increases rail freight charges.

EVIDENCE

In 9MFY16, as per container train operators, container traffic has shifted from rail to road due to increased rail freight charges levied by IR. The shift in container cargo volumes from road to rail, or otherwise, is highly elastic relative to transportation charges, in our view. Further, multi-modal transport for short-distance container transport by rail may still be expensive following the introduction of the DFC due to handling charges.

## Market forces to play a role – potential risk of higher rail freight charges for DFC users?

We expect Concor to be one of the biggest beneficiaries of the DFC as container cargo potentially shifts from road to rail. The DFC will ease traffic congestion and improve the efficiency of CTOs. However, there is lack of clarity on the track access charges that the DFC committee will levy upon Indian Railways and the associated impact on CTOs operating costs, which consensus may not be completely pricing in. In high-usage charge scenario, higher traffic growth for CTOs post the DFC's introduction may not translate into higher earnings growth.

Our interaction with industry participants suggested that IR plans to prioritise the optimal utilization of DFC tracks and any increase in rail freight charges will likely be governed by that goal. Track access charges that the DFC committee will levy on IR are yet to be confirmed. We believe that part of the CTOs' potential financial gains – to be achieved via improved asset utilization, and the post-DFC shift in container traffic from road to rail – will likely be offset by IR's higher rail freight charges.

## Possible delay in DFC commissioning

Our on-the-ground checks suggest DFC commencement is not due before FY20. However, a portion of the track (~640km) on the western corridor may be available for use by FY18, owing to a change in land acquisition status from c91% acquired land in 2014, to c81% land currently (updated around September 2015) (see Figure 7). The key reason for the increase in land required is due to the realignment of tracks as a result of detours. Major detours have been necessary primarily in regions where Indian Railway tracks are passing through cities and the surrounding areas are densely populated.

**Figure 7: Change in land acquisition status**

| Project description | State | Total Scope Area (Ha) | 20F (Acquired) Area (Ha) | Completion (%) | Total Scope Area (Ha) | 20F (Acquired) Area (Ha) | Completion (%) | Change in Total Scope Area (Ha) |
|---|---|---|---|---|---|---|---|---|
| Western Corridor | | 2014 | 2014 | | Current (Sep'15) | Current (Sep'15) | | |
| Phase-I | Haryana | 234 | 234 | 100% | 253 | 253 | 100% | 19 |
| (Rewari- Vadodara) | Rajasthan | 1,829 | 1,829 | 100% | 1,774 | 1,774 | 100% | (55) |
| | Gujarat | 1,545 | 1,442 | 93% | 1,695 | 1,442 | 85% | 150 |
| Total | | 3,608 | 3,504 | 97% | 3,722 | 3,449 | 93% | 114 |
| Phase-II | Gujarat | 868 | 817 | 94% | 977 | 633 | 65% | 109 |
| (Vadodara-JNPT & Rewari-Dadri) | Maharashtra | 442 | 438 | 99% | 461 | 442 | 96% | 19 |
| | Haryana | 745 | 650 | 87% | 744 | 651 | 88% | (1) |
| | Rajasthan | 95 | 90 | 95% | 128 | 81 | 63% | 33 |
| | Uttar Pradesh | 102 | 102 | 100% | 172 | 104 | 60% | 70 |
| Total | | 2,252 | 2,107 | 94% | 2,480 | 1,912 | 77% | 228 |
| **Total of WDFC** | | **5,860** | **5,612** | **96%** | **6,203** | **5,361** | **86%** | **343** |
| Eastern Corridor | | | | | | | | |
| APL- 1 (Khurja - Bhaupur) | Uttar Pradesh | 1,320 | 1,315 | 100% | 1,410 | 1,351 | 96% | 90 |
| APL- 2 (Bhaupur - Mughalsarai) | Uttar Pradesh | 1,400 | 1,373 | 98% | 1,475 | 1,407 | 95% | 75 |
| APL- 3 (Ludhiana - Khurja) | Punjab | 251 | 251 | 100% | 263 | 263 | 100% | 12 |
| | Haryana | 78 | 78 | 100% | 76 | 52 | 68% | (2) |
| | Uttar Pradesh | 436 | 338 | 78% | 992 | 253 | 26% | 556 |
| Total | | 766 | 667 | 87% | 1,331 | 567 | 43% | 565 |
| Railway Funded | Uttar Pradesh | 51 | 42 | 82% | 55 | 49 | 89% | 4 |
| (Mughalsarai - Sonnagar) | Bihar | 268 | 259 | 97% | 226 | 179 | 79% | (42) |
| Total | | 319 | 301 | 94% | 282 | 228 | 81% | (37) |
| (Sonnagar- Dhankuni) | Bihar | 202 | 121 | 60% | 202 | 121 | 60% | 0 |
| | Jharkhand | 373 | 138 | 37% | 368 | 133 | 36% | (5) |
| | West Bengal | 427 | 127 | 30% | 427 | 169 | 40% | 0 |
| Total | | 1,002 | 386 | 39% | 997 | 423 | 42% | (5) |
| **Total of EDFC** | | **4,807** | **4,041** | **84%** | **5,494** | **3,975** | **72%** | **687** |
| Total of WDFC+EDFC | | 10,667 | 9,653 | 91% | 11,697 | 9,336 | 80% | 1,030 |

Source: Dedicated Freight Corridor Committee

# WHAT'S PRICED IN?

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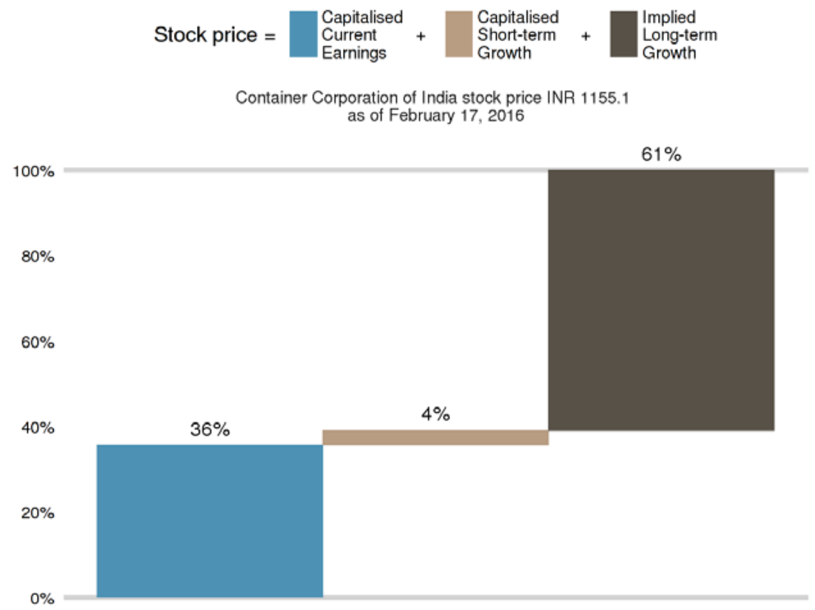
**Even after the stock price's 40% correction, we calculate the market is ascribing 61% of its valuation to implied long-term growth**

**Figure 8: What's priced in?**

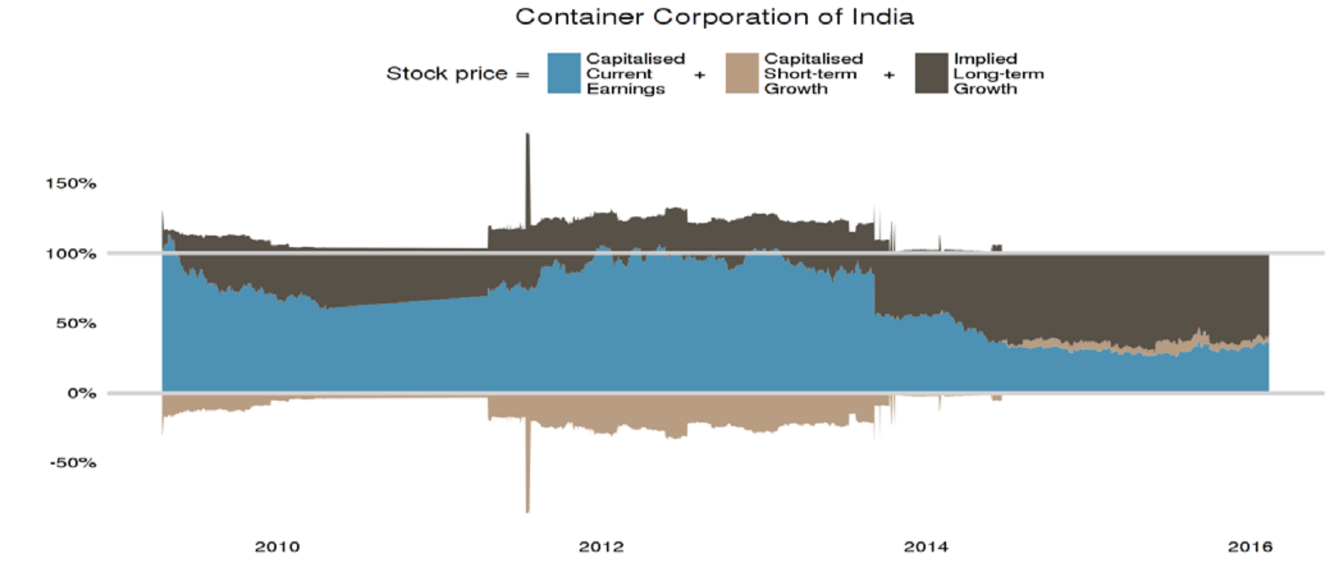



Source: UBS estimates

### Market still assigns substantial value to long-term growth expectations

Our residual income methodology indicates that a significant proportion (c61%) of Concor's current share price is explained by long-term growth expectations. This is much higher than the period prior to 2014 (Figure 10) and implies a structural shift in market expectations of Concor's long-term outlook. We believe this is driven by anticipation of large benefits arising from the DFC, which are not yet clear.

**Figure 9: Concor – historical residual income comparison**

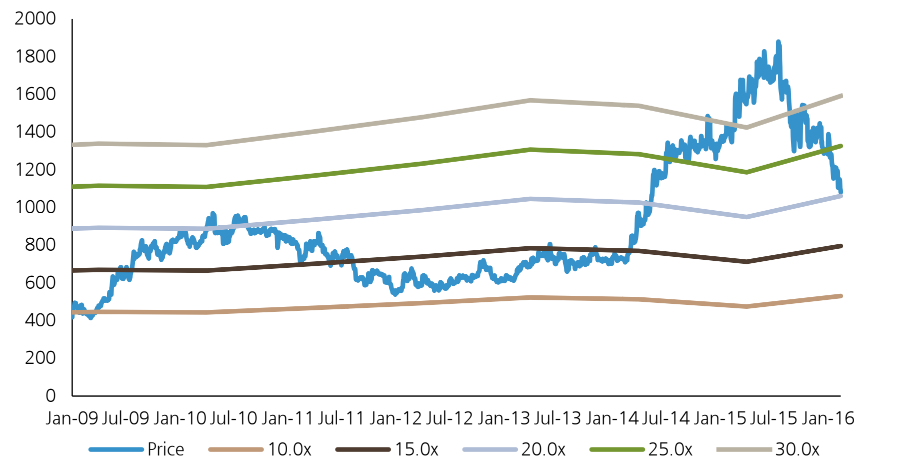



Source: Reuters, UBS

## On a 1-yr fwd PE multiple, the stock is trading above its 5-yr average

Concor's stock price has corrected by 40% in the past six months. Although it is currently trading at 21.8x on a one-year forward PE, based on consensus earnings forecasts, this is higher than its five-year average (19.0x). We do not expect the stock to rerate from current multiple levels in the near term, given the weak macro environment. Moreover, we expect consensus earnings forecasts could be downgraded.

**Figure 10: Concor – one-year forward PE bands**




Source: Datastream

## Expensive relative to peers

Concor is trading at a premium to Gateway and other the global rail operators based on FY17E PE. We estimate FY16-18 earnings CAGRs of 10% for Concor compared 35% for Gateway and to an average of 5% for global peers (2015-17E). We believe Concor's premium valuation is not justifiable, even with the expected improvement in the economic environment and growth.

**Figure 11: Valuation comparison for rail operators**

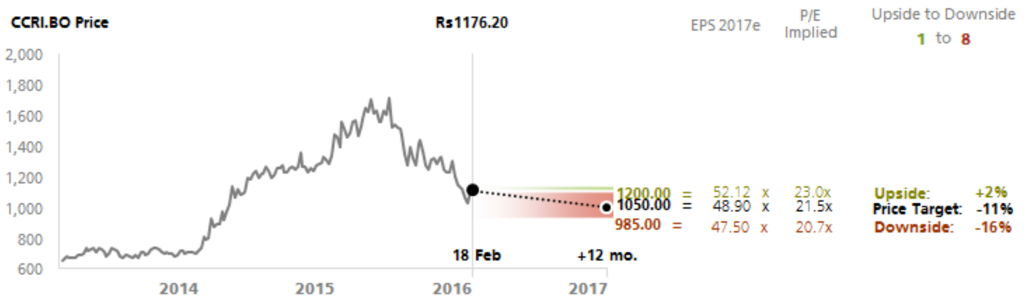
| | | | | EV/EBITDA (x) | | EBITDA CAGR | PE (x) | | EPS CAGR | ROE | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Company | Country | Share Price (LC) | Mkt cap US$ m | CY15E/ FY16E | CY16E/ FY17E | CY15-17E/ FY16-18E | CY15E/ FY16E | CY16E/ FY17E | CY15-17E/ FY16-18E | CY15E/ FY16E | CY16E/ FY17E |
| Concor | India | 1,176.20 | 3,348 | 16.5 | 14.8 | 13% | 26.1 | 24.1 | 10% | 11.2 | 11.3 |
| Gateway | India | 216.30 | 346 | 12.1 | 10.6 | 16% | 27.9 | 19.1 | 35% | 9.2 | 13.2 |
| Guangshen Railway | China | 3.99 | 4,104 | 7.1 | 6.9 | 5% | 20.7 | 19.1 | 7% | 5.0 | 5.3 |
| MTRCL | Hong Kong | 35.50 | 26,098 | 11.3 | 11.8 | 5% | 18.7 | 21.1 | 0% | 6.7 | 6.0 |
| Union Pacific | United States | 79.96 | 71,759 | 8.1 | 8.7 | 1% | 14.6 | 15.4 | 4% | 22.6 | 21.2 |
| Norfolk Southern | United States | 75.77 | 23,406 | 7.5 | 7.7 | 4% | 14.4 | 14.2 | 8% | 12.6 | 12.5 |
| Kansas City Southern | United States | 82.67 | 9,122 | 10.7 | 10.6 | 6% | 17.9 | 18.1 | 7% | 12.9 | 12.0 |

Note: Above data as of 17 February 2016.
Source: Reuters, UBS estimates

## UPSIDE / DOWNSIDE SPECTRUM

return ↑

Concor is trading at Rs1,176.20 (as of 17 February)




| Value drivers | Volume growth | Realization growth | Terminal charges as % of revenue | EBITDA margin |
|---|---|---|---|---|
| Rs1,200 upside | 6.4% | 3.4% | 70.0% | 21.2% |
| Rs1,050 target | 5.0% | 2.9% | 70.5% | 20.7% |
| Rs985 downside | 3.5% | 1.9% | 71.5% | 20.0% |

Source: UBS estimates

### Risk to the current share price is skewed to the downside (1:8).

Concor is trading at **Rs1,176.20** (as of 17 February).

**Upside (Rs1,200):** Our upside scenario assumes a higher uptick in container volume growth and management's ability to increase realization as it passes on freight charges to customers. Our upside scenario takes into account an early commencement of the DFC from FY18. We have further considered an improvement in the import-export balance leading to lower empty haulage charges. We estimate a valuation of Rs1,200 in this scenario.

**Base (Rs1,050):** We expect strong macro headwinds and the impact of higher rail freight charges could impede any strong volume uptick. We more conservative than consensus and believe that consensus is building an optimistic case with respect to growth revival, DFC benefits, and margin expansions. We value Concor at a price target of Rs1,050 using a DCF methodology (assuming a WACC of 11.3% and terminal growth of 4% in FY25E). At our price target, the stock would trade at 19.5x FY17E PE, based on consensus estimates, and at 21.4x FY17E based on our estimates. The five-year average of Concor's one-year forward PE multiple, based on consensus forecasts, is 19.0x.

**Downside (Rs985):** Our downside scenario assumes muted growth in international cargo and a steep decline in domestic cargo as traffic shifts to road transporters. We assume a higher trade deficit leading to an increasing imbalance of import-export cargo and higher empty running charges. We further assume DFC benefits only commence from FY20 due to execution delay risk. We estimate a valuation of Rs985 in this scenario.

## COMPANY DESCRIPTION

return ↑

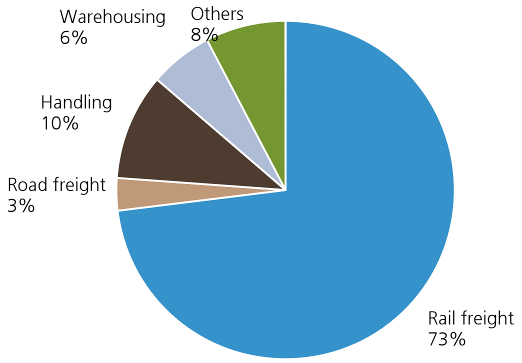
| | |
|---|---|
| **Market Cap** | US$3.3bn |
| **Shares Outstanding** | 195m (COM) |
| **Industry and outlook** | Transportation |
| **Region** | Asia |
| **Website** | www.concorindia.com |

Container Corporation of India is the largest container train operator in India, with a 76% market share in FY14. It began operations in 1989 by acquiring seven inland container depots (ICDs) from Indian Railways. It now operates a network of 63 ICDs and container freight stations, and has 11,770 wagons (including 10,413 high-speed wagons). It owned or leased 18,680 containers in FY13. It is evolving into a more integrated logistics company and increasing its emphasis on value-added services such cargo managment, cold chain and air cargo clearance. The government of India has a 63.1% stake in the company.

### Industry outlook

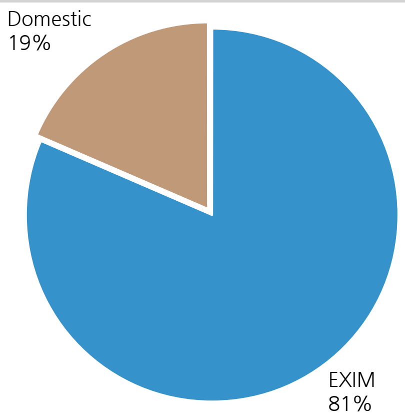
Container train operators are an essential part of India's logistics chain and key beneficiaries of upticks in economic activity leading to higher trade volume. The sector is plagued by inadequate rail infrastructure that leads to longer delivery times and higher freight charges to subsidise passenger trains. Government initiatives, including the development of the DFC and allowing the private sector to set up warehousing and cargo handling facilities under the Private Freight Station Act are likely to be growth catalysts. These initiatives should enable higher growth and improve margins for container train operators in the long term.

**Revenue by segment (FY15)**




Source: Company data

**Revenue by freight type (FY15)**




Source: Company data

## Container Corporation of India (CCRI.BO)

| Income statement (Rsm) | 03/13 | 03/14 | 03/15 | 03/16E | % ch | 03/17E | % ch | 03/18E | 03/19E | 03/20E |
|---|---|---|---|---|---|---|---|---|---|---|
| **Revenues** | **44,450** | **53,167** | **61,493** | **58,978** | *-4.1* | **63,765** | *8.1* | **70,497** | **80,721** | **94,661** |
| Gross profit | 13,559 | 16,037 | 19,594 | 17,104 | *-12.7* | 18,811 | *10.0* | 20,973 | 24,418 | 29,108 |
| **EBITDA (UBS)** | **10,495** | **11,523** | **14,020** | **12,003** | *-14.4* | **13,442** | *12.0* | **15,419** | **18,405** | **22,457** |
| Depreciation & amortisation | (1,763) | (2,356) | (4,108) | (3,554) | *-13.5* | (3,842) | *8.1* | (4,287) | (4,664) | (4,978) |
| **EBIT (UBS)** | **8,732** | **9,166** | **9,912** | **8,449** | *-14.8* | **9,600** | *13.6* | **11,131** | **13,740** | **17,479** |
| Associates & investment income | 402 | 540 | 413 | 454 | *10.0* | 499 | *10.0* | 549 | 604 | 664 |
| Other non-operating income | 0 | 0 | 0 | 0 | - | 0 | - | 0 | 0 | 0 |
| Net interest | 2,893 | 2,815 | 2,854 | 2,807 | *-1.6* | 2,613 | *-6.9* | 2,531 | 2,626 | 2,963 |
| Exceptionals (incl goodwill) | 0 | 0 | 0 | 0 | - | 0 | - | 0 | 0 | 0 |
| **Profit before tax** | **12,027** | **12,522** | **13,178** | **11,710** | *-11.1* | **12,712** | *8.6* | **14,212** | **16,970** | **21,106** |
| Tax | (2,721) | (3,072) | (2,638) | (2,927) | *-11.0* | (3,178) | *-8.6* | (3,553) | (4,243) | (5,277) |
| **Profit after tax** | **9,306** | **9,450** | **10,540** | **8,782** | *-16.7* | **9,534** | *8.6* | **10,659** | **12,728** | **15,830** |
| Preference dividends | 0 | 0 | 0 | 0 | - | 0 | - | 0 | 0 | 0 |
| Minorities | 0 | 0 | 0 | 0 | - | 0 | - | 0 | 0 | 0 |
| Extraordinary items | 0 | 0 | 0 | 0 | - | 0 | - | 0 | 1 | 2 |
| **Net earnings (local GAAP)** | **9,306** | **9,450** | **10,540** | **8,782** | *-16.7* | **9,534** | *8.6* | **10,659** | **12,729** | **15,832** |
| **Net earnings (UBS)** | **9,306** | **9,450** | **10,540** | **8,782** | *-16.7* | **9,534** | *8.6* | **10,659** | **12,728** | **15,830** |
| Tax rate (%) | 22.6 | 24.5 | 20.0 | 25.0 | *24.9* | 25.0 | *0.0* | 25.0 | 25.0 | 25.0 |

| Per share (Rs) | 03/13 | 03/14 | 03/15 | 03/16E | % ch | 03/17E | % ch | 03/18E | 03/19E | 03/20E |
|---|---|---|---|---|---|---|---|---|---|---|
| EPS (UBS, diluted) | 47.73 | 48.47 | 54.06 | 45.04 | *-16.7* | 48.90 | *8.6* | 54.67 | 65.28 | 81.19 |
| EPS (local GAAP, diluted) | 47.73 | 48.47 | 54.06 | 45.04 | *-16.7* | 48.90 | *8.6* | 54.67 | 65.28 | 81.20 |
| EPS (UBS, basic) | 47.73 | 48.47 | 54.06 | 45.04 | *-16.7* | 48.90 | *8.6* | 54.67 | 65.28 | 81.19 |
| Net DPS (Rs) | 11.67 | 12.30 | 14.00 | 15.00 | *7.1* | 16.50 | *10.0* | 19.00 | 23.00 | 28.00 |
| Cash EPS (UBS, diluted)[1] | 56.77 | 60.55 | 75.13 | 63.27 | *-15.8* | 68.61 | *8.4* | 76.66 | 89.20 | 106.72 |
| Book value per share | 319.05 | 353.15 | 390.21 | 417.70 | *7.0* | 447.29 | *7.1* | 479.73 | 518.10 | 566.53 |
| Average shares (diluted) | 194.97 | 194.97 | 194.97 | 194.97 | *0.0* | 194.97 | *0.0* | 194.97 | 194.97 | 194.97 |

| Balance sheet (Rsm) | 03/13 | 03/14 | 03/15 | 03/16E | % ch | 03/17E | % ch | 03/18E | 03/19E | 03/20E |
|---|---|---|---|---|---|---|---|---|---|---|
| Cash and equivalents | 29,460 | 27,742 | 29,492 | 27,014 | *-8.4* | 25,788 | *-4.5* | 25,462 | 27,585 | 31,880 |
| Other current assets | 5,645 | 6,301 | 7,702 | 8,174 | *6.1* | 8,973 | *9.8* | 9,876 | 10,915 | 12,103 |
| **Total current assets** | **35,104** | **34,043** | **37,193** | **35,188** | *-5.4* | **34,760** | *-1.2* | **35,337** | **38,501** | **43,984** |
| Net tangible fixed assets | 29,227 | 35,577 | 40,187 | 47,633 | *18.5* | 53,791 | *12.9* | 59,503 | 63,839 | 67,861 |
| Net intangible fixed assets | 490 | 519 | 519 | 519 | *0.0* | 519 | *0.0* | 519 | 519 | 519 |
| Investments / other assets | 7,511 | 12,544 | 12,052 | 13,084 | *8.6* | 14,270 | *9.1* | 15,634 | 17,203 | 19,006 |
| **Total assets** | **72,332** | **82,683** | **89,952** | **96,424** | *7.2* | **103,340** | *7.2* | **110,993** | **120,061** | **131,370** |
| Trade payables & other ST liabilities | 6,491 | 8,397 | 9,364 | 10,338 | *10.4* | 11,326 | *9.6* | 12,473 | 13,851 | 15,477 |
| Short term debt | 486 | 211 | 209 | 209 | *0.00* | 209 | *0.00* | 209 | 209 | 209 |
| **Total current liabilities** | **6,977** | **8,608** | **9,573** | **10,547** | *10.2* | **11,535** | *9.4* | **12,682** | **14,060** | **15,686** |
| Long term debt | 0 | 1,160 | 1,308 | 1,308 | *0.0* | 1,308 | *0.0* | 1,308 | 1,308 | 1,308 |
| Other long term liabilities | 3,151 | 4,062 | 2,991 | 3,128 | *4.6* | 3,286 | *5.1* | 3,468 | 3,677 | 3,917 |
| Preferred shares | 0 | 0 | 0 | 0 | - | 0 | - | 0 | 0 | 0 |
| **Total liabilities (incl pref shares)** | **10,128** | **13,830** | **13,872** | **14,983** | *8.0* | **16,129** | *7.6* | **17,458** | **19,045** | **20,911** |
| Common s/h equity | 62,205 | 68,853 | 76,080 | 81,441 | *7.0* | 87,211 | *7.1* | 93,535 | 101,016 | 110,459 |
| Minority interests | 0 | 0 | 0 | 0 | - | 0 | - | 0 | 0 | 0 |
| **Total liabilities & equity** | **72,332** | **82,683** | **89,952** | **96,424** | *7.2* | **103,340** | *7.2* | **110,993** | **120,061** | **131,370** |

| Cash flow (Rsm) | 03/13 | 03/14 | 03/15 | 03/16E | % ch | 03/17E | % ch | 03/18E | 03/19E | 03/20E |
|---|---|---|---|---|---|---|---|---|---|---|
| Net income (before pref divs) | 9,306 | 9,450 | 10,540 | 8,782 | *-16.7* | 9,534 | *8.6* | 10,659 | 12,729 | 15,832 |
| Depreciation & amortisation | 1,763 | 2,357 | 4,108 | 3,554 | *-13.5* | 3,842 | *8.1* | 4,287 | 4,664 | 4,978 |
| Net change in working capital | 425 | 1,249 | (433) | 502 | - | 189 | *-62.4* | 244 | 338 | 439 |
| Other operating | (2,390) | 1,186 | (436) | 137 | - | 158 | *15.0* | 182 | 208 | 238 |
| **Operating cash flow** | **9,104** | **14,241** | **13,779** | **12,976** | *-5.8* | **13,723** | *5.8* | **15,372** | **17,939** | **21,486** |
| Tangible capital expenditure | (5,874) | (8,184) | (8,719) | (11,000) | *-26.2* | (10,000) | *9.1* | (10,000) | (9,000) | (9,000) |
| Intangible capital expenditure | 0 | 0 | 0 | 0 | - | 0 | - | 0 | 0 | 0 |
| Net (acquisitions) / disposals | 0 | 0 | 0 | 0 | - | 0 | - | 0 | 0 | 0 |
| Other investing | 1,452 | (5,061) | 492 | (1,031) | - | (1,186) | - | (1,364) | (1,569) | (1,804) |
| **Investing cash flow** | **(4,422)** | **(13,246)** | **(8,227)** | **(12,031)** | *-46.2* | **(11,186)** | *7.0* | **(11,364)** | **(10,569)** | **(10,804)** |
| Equity dividends paid | (2,568) | (2,806) | (3,194) | (3,422) | *-7.1* | (3,764) | *-10.0* | (4,334) | (5,247) | (6,387) |
| Share issues / (buybacks) | 0 | 0 | 0 | 0 | - | 0 | - | 0 | 0 | 0 |
| Other financing | (33) | 0 | 0 | 0 | - | 0 | - | 0 | 0 | 0 |
| Change in debt & pref shares | (196) | 885 | 146 | 0 | - | 0 | - | 0 | 0 | 0 |
| **Financing cash flow** | **(2,798)** | **(1,920)** | **(3,048)** | **(3,422)** | *-12.3* | **(3,764)** | *-10.0* | **(4,334)** | **(5,247)** | **(6,387)** |
| **Cash flow inc/(dec) in cash** | **1,884** | **(925)** | **2,504** | **(2,477)** | - | **(1,227)** | *50.5* | **(326)** | **2,124** | **4,295** |
| FX / non cash items | 0 | (792) | (755) | 0 | - | 0 | - | 0 | 0 | 0 |
| **Balance sheet inc/(dec) in cash** | **1,884** | **(1,717)** | **1,749** | **(2,477)** | - | **(1,227)** | *50.5* | **(326)** | **2,124** | **4,295** |

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.[1]Cash EPS (UBS, diluted) is calculated using UBS net income adding back depreciation and amortization.

## Container Corporation of India (CCRI.BO)

| Valuation (x) | 03/13 | 03/14 | 03/15 | 03/16E | 03/17E | 03/18E | 03/19E | 03/20E |
|---|---|---|---|---|---|---|---|---|
| P/E (local GAAP, diluted) | 13.2 | 15.2 | 24.0 | 26.1 | 24.1 | 21.5 | 18.0 | 14.5 |
| P/E (UBS, diluted) | 13.2 | 15.2 | 24.0 | 26.1 | 24.1 | 21.5 | 18.0 | 14.5 |
| P/CEPS | 11.1 | 12.2 | 17.3 | 18.6 | 17.1 | 15.3 | 13.2 | 11.0 |
| Equity FCF (UBS) yield % | 2.6 | 4.2 | 2.0 | 0.9 | 1.6 | 2.3 | 3.9 | 5.4 |
| Net dividend yield (%) | 1.9 | 1.7 | 1.1 | 1.3 | 1.4 | 1.6 | 2.0 | 2.4 |
| P/BV x | 2.0 | 2.1 | 3.3 | 2.8 | 2.6 | 2.5 | 2.3 | 2.1 |
| EV/revenues (core) | 2.1 | 2.1 | 3.6 | 3.4 | 3.1 | 2.8 | 2.5 | 2.1 |
| EV/EBITDA (core) | 8.7 | 9.7 | 15.8 | 16.5 | 14.8 | 13.0 | 10.9 | 8.9 |
| EV/EBIT (core) | 10.4 | 12.2 | 22.3 | 23.4 | 20.8 | 18.0 | 14.6 | 11.5 |
| EV/OpFCF (core) | 18.1 | 24.3 | NM | NM | NM | NM | 20.6 | 14.4 |
| EV/op. invested capital | 3.3 | 3.3 | 5.5 | 4.2 | 3.7 | 3.3 | 3.0 | 2.8 |

| Enterprise value (Rsm) | 03/13 | 03/14 | 03/15 | 03/16E | 03/17E | 03/18E | 03/19E | 03/20E |
|---|---|---|---|---|---|---|---|---|
| Market cap. | 122,725 | 143,960 | 253,322 | 229,324 | 229,324 | 229,324 | 229,324 | 229,324 |
| Net debt (cash) | (27,815) | (27,672) | (27,173) | (26,736) | (24,884) | (24,108) | (24,108) | (24,108) |
| Buy out of minorities | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Pension provisions/other | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| **Total enterprise value** | **94,911** | **116,287** | **226,149** | **202,588** | **204,440** | **205,216** | **205,216** | **205,216** |
| Non core assets | (3,690) | (4,836) | (4,882) | (4,882) | (4,882) | (4,882) | (4,882) | (4,882) |
| **Core enterprise value** | **91,221** | **111,451** | **221,267** | **197,706** | **199,558** | **200,334** | **200,334** | **200,334** |

| Growth (%) | 03/13 | 03/14 | 03/15 | 03/16E | 03/17E | 03/18E | 03/19E | 03/20E |
|---|---|---|---|---|---|---|---|---|
| Revenue | 8.4 | 19.6 | 15.7 | -4.1 | 8.1 | 10.6 | 14.5 | 17.3 |
| EBITDA (UBS) | 2.6 | 9.8 | 21.7 | -14.4 | 12.0 | 14.7 | 19.4 | 22.0 |
| EBIT (UBS) | 1.4 | 5.0 | 8.1 | -14.8 | 13.6 | 16.0 | 23.4 | 27.2 |
| EPS (UBS, diluted) | 7.5 | 1.5 | 11.5 | -16.7 | 8.6 | 11.8 | 19.4 | 24.4 |
| Net DPS | 6.1 | 5.4 | 13.8 | 7.1 | 10.0 | 15.2 | 21.1 | 21.7 |

| Margins & Profitability (%) | 03/13 | 03/14 | 03/15 | 03/16E | 03/17E | 03/18E | 03/19E | 03/20E |
|---|---|---|---|---|---|---|---|---|
| Gross profit margin | 30.5 | 30.2 | 31.9 | 29.0 | 29.5 | 29.8 | 30.3 | 30.8 |
| EBITDA margin | 23.6 | 21.7 | 22.8 | 20.4 | 21.1 | 21.9 | 22.8 | 23.7 |
| EBIT margin | 19.6 | 17.2 | 16.1 | 14.3 | 15.1 | 15.8 | 17.0 | 18.5 |
| Net earnings (UBS) margin | 20.9 | 17.8 | 17.1 | 14.9 | 15.0 | 15.1 | 15.8 | 16.7 |
| ROIC (EBIT) | 31.2 | 27.3 | 24.5 | 17.9 | 17.6 | 18.1 | 20.4 | 24.1 |
| ROIC post tax | 24.1 | 20.6 | 19.6 | 13.4 | 13.2 | 13.6 | 15.3 | 18.0 |
| ROE (UBS) | 15.8 | 14.4 | 14.5 | 11.2 | 11.3 | 11.8 | 13.1 | 15.0 |

| Capital structure & Coverage (x) | 03/13 | 03/14 | 03/15 | 03/16E | 03/17E | 03/18E | 03/19E | 03/20E |
|---|---|---|---|---|---|---|---|---|
| Net debt / EBITDA | (2.8) | (2.3) | (2.0) | (2.1) | (1.8) | (1.6) | (1.4) | (1.4) |
| Net debt / total equity % | (46.6) | (38.3) | (36.8) | (31.3) | (27.8) | (25.6) | (25.8) | (27.5) |
| Net debt / (net debt + total equity) % | (87.2) | (62.1) | (58.2) | (45.6) | (38.6) | (34.4) | (34.8) | (37.9) |
| Net debt/EV % | (31.8) | (23.7) | (12.6) | (12.9) | (12.2) | (12.0) | (13.0) | (15.2) |
| Capex / depreciation % | NM | NM | NM | NM | NM | NM | 193.0 | 180.8 |
| Capex / revenue % | 13.2 | 15.4 | 14.2 | 18.7 | 15.7 | 14.2 | 11.1 | 9.5 |
| EBIT / net interest | NM | NM | NM | NM | NM | NM | NM | NM |
| Dividend cover (UBS) | 4.1 | 3.9 | 3.9 | 3.0 | 3.0 | 2.9 | 2.8 | 2.9 |
| Div. payout ratio (UBS) % | 24.4 | 25.4 | 25.9 | 33.3 | 33.7 | 34.8 | 35.2 | 34.5 |

| Revenues by division (Rsm) | 03/13 | 03/14 | 03/15 | 03/16E | 03/17E | 03/18E | 03/19E | 03/20E |
|---|---|---|---|---|---|---|---|---|
| Others | 44,450 | 53,167 | 61,493 | 58,978 | 63,765 | 70,497 | 80,721 | 94,661 |
| **Total** | **44,450** | **53,167** | **61,493** | **58,978** | **63,765** | **70,497** | **80,721** | **94,661** |

| EBIT (UBS) by division (Rsm) | 03/13 | 03/14 | 03/15 | 03/16E | 03/17E | 03/18E | 03/19E | 03/20E |
|---|---|---|---|---|---|---|---|---|
| Others | 8,732 | 9,166 | 9,912 | 8,449 | 9,600 | 11,131 | 13,740 | 17,479 |
| **Total** | **8,732** | **9,166** | **9,912** | **8,449** | **9,600** | **11,131** | **13,740** | **17,479** |

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.

**Forecast returns**

| | |
|---|---|
| Forecast price appreciation | -10.7% |
| Forecast dividend yield | 1.5% |
| Forecast stock return | -9.2% |
| Market return assumption | 12.7% |
| Forecast excess return | -21.9% |

**Valuation Method and Risk Statement**

We derive our price target from a DCF-based methodology and explicitly forecast a long-term valuation.

We believe the risks to our long-term estimates and investment thesis are an economic slowdown, any increase in rail freight charges, delays in Dedicated Freight Corridor commissioning, and other government policy changes.

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| 12-Month Rating | Definition | Coverage[1] | IB Services[2] |
|---|---|---|---|
| **Buy** | FSR is > 6% above the MRA. | 48% | 36% |
| **Neutral** | FSR is between -6% and 6% of the MRA. | 39% | 28% |
| **Sell** | FSR is > 6% below the MRA. | 12% | 22% |
| **Short-Term Rating** | **Definition** | **Coverage[3]** | **IB Services[4]** |
| **Buy** | Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event. | <1% | <1% |
| **Sell** | Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event. | <1% | <1% |

Source: UBS. Rating allocations are as of 31 December 2015.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
3:Percentage of companies under coverage globally within the Short-Term rating category.
4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

**KEY DEFINITIONS: Forecast Stock Return (FSR)** is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months. **Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (a proxy for, and not a forecast of, the equity risk premium). **Under Review (UR)** Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation. **Short-Term Ratings** reflect the expected near-term (up to three months) performance of the stock and do not reflect any change in the fundamental view or investment case. **Equity Price Targets** have an investment horizon of 12 months.

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**UBS Securities India Private Ltd:** Shaleen Kumar; Gautam Chhaochharia.

**Company Disclosures**

| Company Name | Reuters | 12-month rating | Short-term rating | Price | Price date |
|---|---|---|---|---|---|
| **Container Corporation of India** | CCRI.BO | Suspended | N/A | Rs1,176.20 | 17 Feb 2016 |

Source: UBS. All prices as of local market close.
Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date

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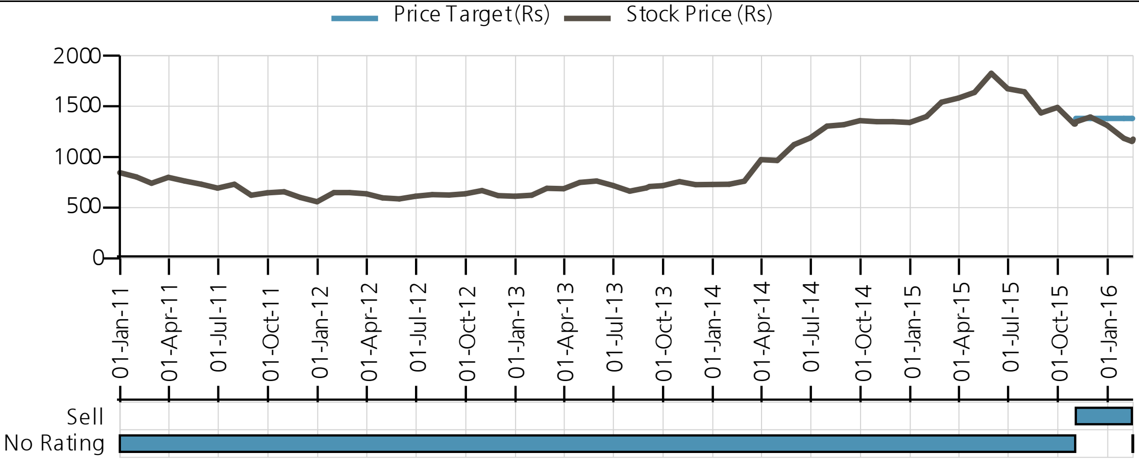
**Container Corporation of India (Rs)**




Source: UBS; as of 17 Feb 2016

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