

# ADANI PORTS AND SEZ

## Forex risk: Vulnerable but manageable

India Equity Research | Infrastructure - Ports

Given its USD1.9bn unhedged foreign currency exposure, Adani Ports SEZ (APSEZ) is caught in the recent USD/INR crossfire. We observe that every 10% depreciation of USD/INR: 1) impacts the company's P&L to the tune of USD105–110mn given positive adjustment of USD40mn on revenue and negative USD150mn on the principal and interest components; 2) raises gearing to 1.13x from 1.08x currently; and 3) does not impact cash flow (first tranche of bond repayment due in June 2020). APSEZ remains vulnerable to forex risk and up-fronting of losses would hit P&L in the near term, but the exposure is positive up to 100USD/INR considering cost savings in absence of hedging, making forex risk manageable. However, the cost of debt (currently 3.8%) would eventually rise (beyond FY20) given hardening US bond yields. That said, volume growth momentum is strong with major ports logging 6% volume growth in July/August, which bodes well for APSEZ. All in all, maintain 'BUY/SO'.

### Unhedged foreign currency exposure – coming full circle?

APSEZ's unhedged USD borrowing is largely USD1.65bn foreign currency borrowings (FCB) payable in three tranches (first one worth USD650mn falls due June 2020). Since hedging involved additional cost of 5–5.5%, APSEZ had kept open the FCBs, thereby saving about USD100mn per year. Our analysis suggests USD/INR depreciation up to 100 is P&L-positive over a five-year period (refer to table1) factoring in cost savings in absence of hedging. The INR's sharp depreciation against the greenback (USD/INR at 72) would hit P&L by a notional loss of INR8–9bn (INR3.8bn recognised in Q1).

### Volume momentum going strong; 200MT guidance comfortable

Looking at major ports' growth for July and August, APSEZ is likely to report another strong quarter with volume growth of 10%-plus. Growth in cargo is led by substantial growth in coal imports (up 34% YoY). Container volume growth has averaged about 6.5%. We believe APSEZ is on track to meet its FY19 guidance of 200MT cargo and has a cushion of 4–5MT since the resumption of operations at Adani Mundra power plant.

### Outlook and valuations: Outperformance to sustain; maintain 'BUY'

We are optimistic on APSEZ's long-term prospects given its strong positioning among shipping lines and focus on sweating out assets. We maintain 'BUY/SO' with a target price of INR451 (20% upside), implying an exit P/E of 19x and EV/EBITDA of 13x.

#### Financials (Consolidated)

Year to March	FY17	FY18	FY19E	FY20E
Revenues (INR mn)	84,394	113,230	113,045	135,099
EBITDA (INR mn)	56,921	70,621	72,591	86,250
Adjusted Profit (INR mn)	39,115	35,184	40,634	49,510
Adjusted Diluted EPS (INR)	18.9	17.0	19.6	23.9
EV/EBITDA (x)	17.3	13.8	13.2	10.9
P/B (x)	4.4	3.7	3.2	2.7
ROAE (%)	24.9	18.2	17.9	18.8

EDELWEISS 4D RATINGS	
Absolute Rating	BUY
Rating Relative to Sector	Outperform
Risk Rating Relative to Sector	Low
Sector Relative to Market	Overweight

#### MARKET DATA (R: APSE.BO, B: ADSEZ IN)

CMP	: INR 381
Target Price	: INR 451
52-week range (INR)	: 452 / 347
Share in issue (mn)	: 2,071.0
M cap (INR bn/USD mn)	: 789 / 10,879
Avg. Daily Vol.BSE/NSE('000)	: 4,047.5

#### SHARE HOLDING PATTERN (%)

	Current	Q4FY18	Q3FY18
Promoters *	62.3	66.3	65.8
MF's, FI's & BK's	12.0	12.0	11.9
FII's	18.3	18.3	18.3
Others	3.5	3.5	4.0
* Promoters pledged shares (% of share in issue)	:	NIL	

#### PRICE PERFORMANCE (%)

	Stock	Nifty	EW Power Index
1 month	1.8	(0.8)	6.8
3 months	2.1	5.2	4.7
12 months	(6.0)	12.8	(7.8)

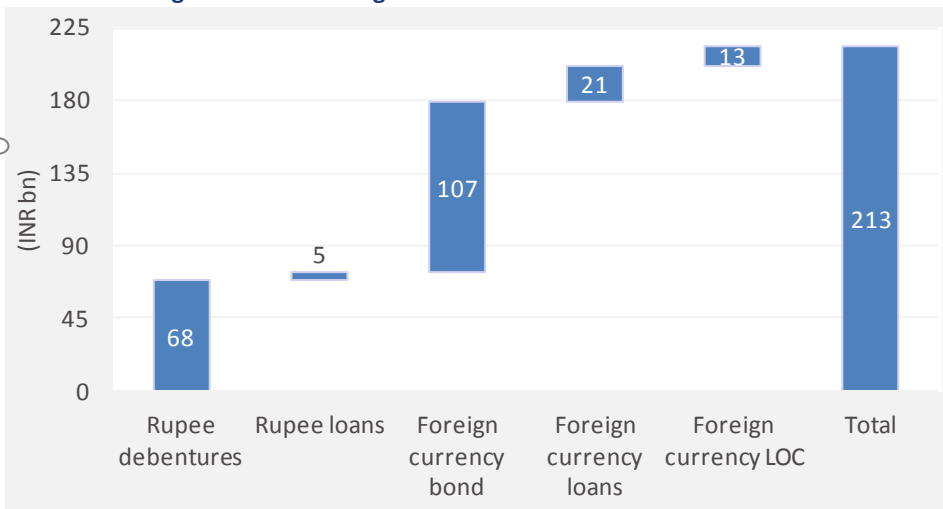
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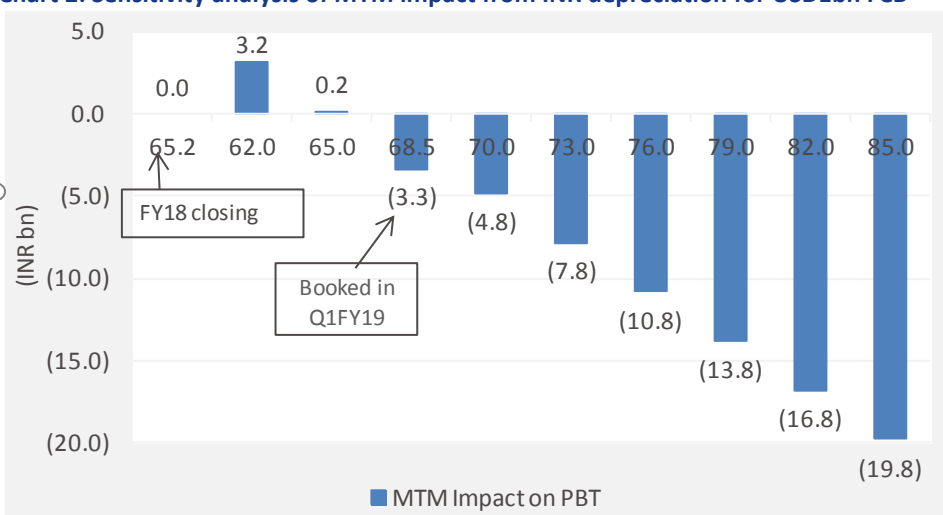
APSEZ's unhedged USD borrowing is largely USD1.65bn FCB payable in three tranches

INR 3.3bn MTM loss booked in Q1FY19 on account of USD 1bn FCB issued post IND-AS adoption

**Chart 1: Unhedged USD borrowing of USD1.9bn at FY18-end**



**Chart 2: Sensitivity analysis of MTM impact from INR depreciation for USD1bn FCB**



**Table 1: Our sensitivity analysis suggests that unhedged position is P&L-positive till 60% INR depreciation over five-year period**

Line Item	Description	Impact on P&L	Frequency	USD Exposure (mn)	5 Year Impact from INR depreciation				
					10% (USD mn)	20% (USD mn)	30% (USD mn)	40% (USD mn)	50% (USD mn)
Revenue	Revenue from Marine business+Royalty+CT2+port development	Positive	Recurring	400	123	253	390	534	686
Interest Outgo	USD 1.9bn unhedged borrowing at ~4% cost of debt	Negative	Recurring	72	(22)	(46)	(70)	(96)	(124)
Principal Outgo	USD 1.9bn	Negative	One-Time	1,897	(190)	(379)	(569)	(759)	(948)
Interest cost savings in absence of hedging	5% cost of hedging on USD 1.9bn exposure	Positive	Recurring	95	474	474	474	474	474
<b>Net Impact</b>					<b>386</b>	<b>302</b>	<b>225</b>	<b>154</b>	<b>89</b>

Note: 1) Revenue and debt is at the end of March 2018; 2) Impact on revenue and interest outgo is calculated assuming straight-line depreciation over five years; 3) We have not factored growth in USD denominated revenues and higher cost of debt on USD650mn which is likely to be refinanced in June 2020

Source: Company, Edelweiss research

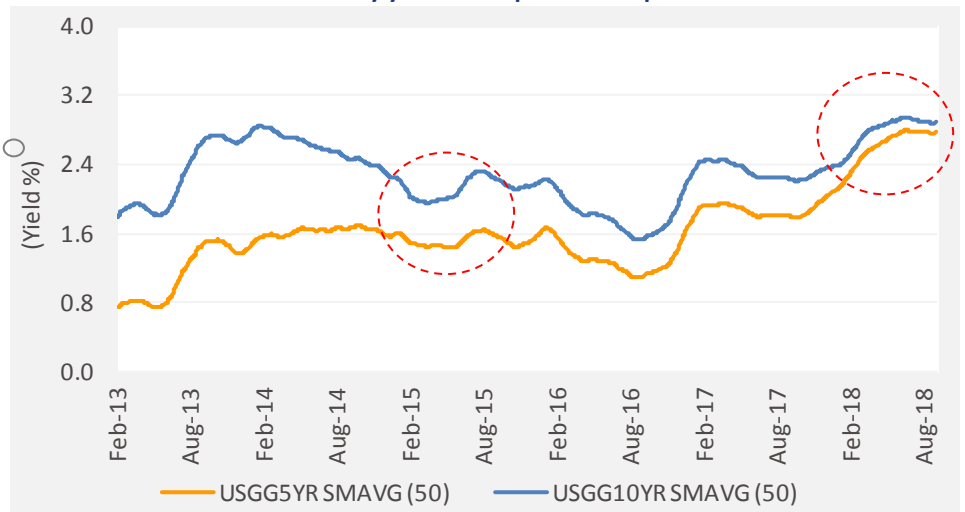
**Table 2: APSEZ is likely to refinance USD650mn FCB due in 2020...**

Loan Type	Outstanding Amount FY18 (INR bn)	USD Exposure (mn)	Interest Rate	Maturity	Hedging Status	Bond Pricing
5 years foreign currency bond	42.4	650	3.50% p.a	Bullet repayment in the year 2020	Unhedged	195 basis points over the 5 years US Treasury Note
5 years foreign currency bond	32.3	500	3.95% p.a	Bullet repayment in the year 2022	Unhedged	189 basis points over the 5 years US Treasury Note
10 years foreign currency bond	32.0	500	4.00% p.a	Bullet repayment in the year 2027	Unhedged	195 basis points over the 10 years US Treasury Note

Source: Company, Edelweiss research

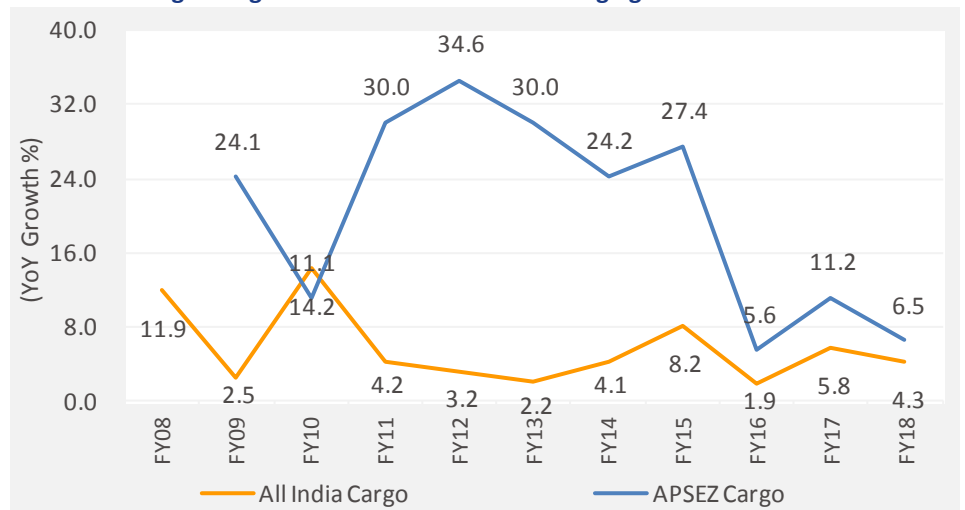
Cost of debt likely to increase for APSEZ

**Chart 3: ...however US 5Y treasury yields are up 110–120bps since 2015**



Source: Bloomberg, Edelweiss research

**Chart 4: APSEZ growing much faster than All India Cargo growth...**



Source: Company, IPA, Edelweiss research

Chart 5: ...thereby gaining market share from competitors...

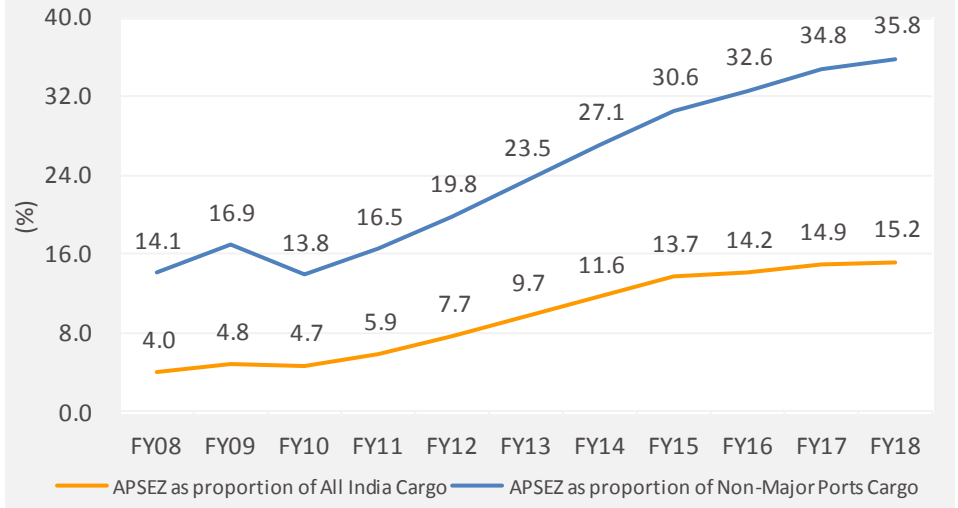


Chart 6: ...with container being a major growth driver

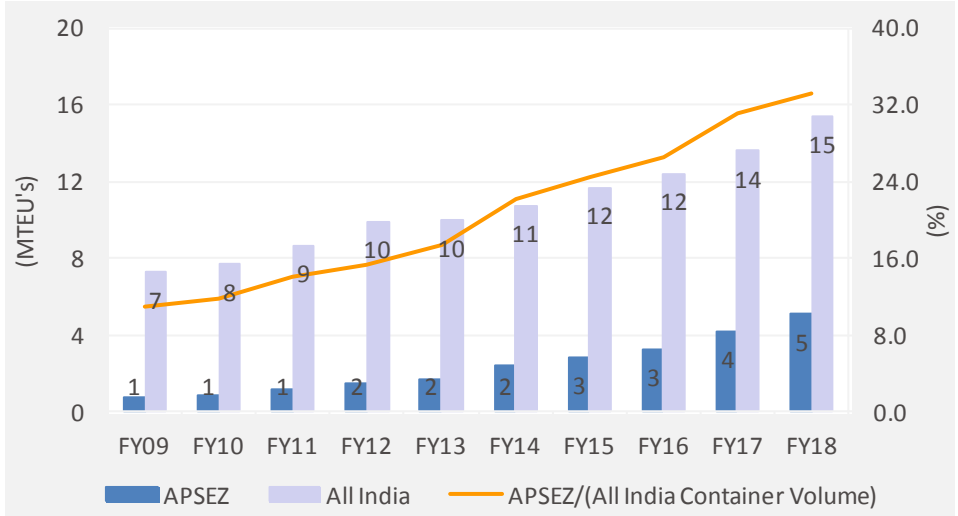
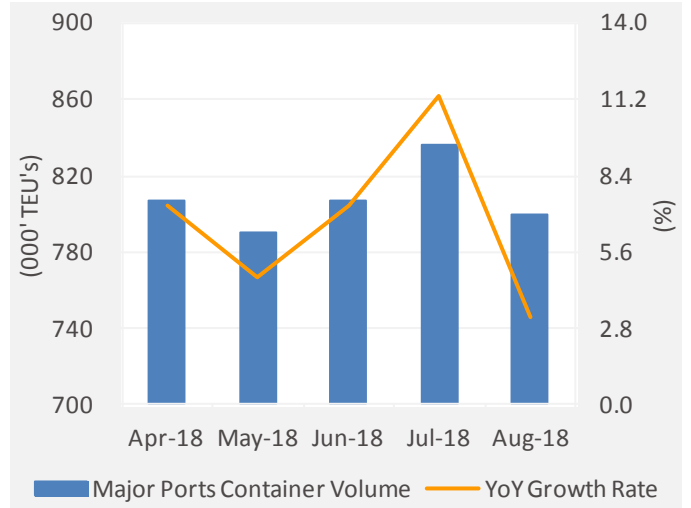
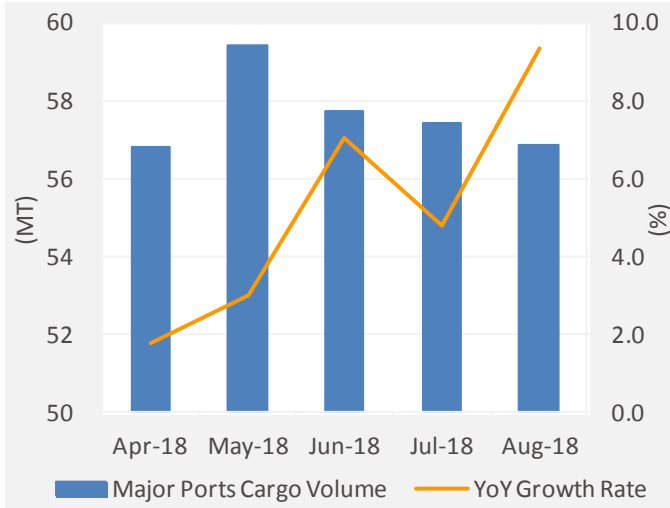


Chart 7: APSEZ typically grows 1.5x major ports' cargo growth and 2x major ports' container growth



Source: Company, IPA, Edelweiss research

Table 3: SOTP-based valuation

	Method	CoE (%)	Value (INR mn)	Stake (%)	Value of stake (INR mn)	Price per share (INR)	% age of SOTP (%)
Mundra Port	DCF	11.6	284,394	100.0	284,394	137	30.5
CT3/4/5....	DCF	11.6	96,600	50.0	48,300	23	5.2
SEZ	DCF	11.8	102,718	100.0	102,718	50	11.0
Dahej Port	DCF	11.8	32,324	74.0	23,920	12	2.6
Mormugao Terminal	DCF	12.1	3,298	74.0	2,441	1	0.3
Hazira Port	DCF	11.8	84,205	100.0	84,205	41	9.0
Ennore Cont. Terminal	DCF	12.1	(2,910)	100.0	(2,910)	(1)	(0.3)
Kandla Bulk Terminal	DCF	12.1	4,798	74.0	3,550	2	0.4
Dhamra Port	DCF	11.8	83,426	100.0	83,426	40	8.9
Katupalli Port	DCF	11.8	24,521	100.0	24,521	12	2.6
ALL	P/E	20x	20,790	100.0	20,790	10	2.2
Vizhinjam port	2x Equity		18,750	100.0	18,750	9	2.0
Harbour busniess	DCF	0.1	209,987	100.0	209,987	101	22.5
Cash & Investments	BV	FY18	29,676	100.0	29,676	14	3.2
Total			992,577		933,768	451	100.0

Source: Company, Edelweiss research

### Company Description

APSEZ is the seamless integration of 3 verticals consisting of Ports, Logistics and Special Economic Zone. The company has pan India presence in ten locations (nine are operational) with the flagship Mundra port in the Gulf of Kachchh, also India's largest commercial port.. APSEZ has both the capacity and ability to handle multiple cargo at its ports. APSEZ has a large land bank of 8,481 hectares of contiguous land at Mundra, with requisite approvals and clearances in place and provides a diversified revenue stream. APSEZ has been investing in tightly integrated assets, with an objective of reducing bottlenecks in the overall logistics value chain - saving time and cost for its customer.

### Investment Theme

Sound business fundamentals: We expect sustainable volumes on back of pick up in import/export trade & port of calls along with new handling facilities. Moreover, continuous expansion of LPG, LNG terminals and upcoming Vizhinham port is likely to keep volume growth ticking in double digits for the next 3-4 years.

APSEZ to benefit from consolidation of volumes: As shipping lines deploy larger vessels and consolidate routes, the focus will move to ports with O&D demand over transshipment. Thus, this consolidation will help APSEZ given its scale, pan India presence and existing strong relationships with container liner companies.

Corporate governance issues waning: Management is committed to stay away from related party transactions as it has recovered

### Key Risks

Uncertainty in traffic at ports: Since cargo at ports is contingent on international trade, any slowdown in it could affect Mundra Port as well.

Regulatory changes regarding SEZs: The existing SEZ policies and benefits outlined by the government to promote exports are relatively new and are being continuously reviewed. Any changes in the form of reversal of current tax benefits to units under the SEZ umbrella will significantly undermine incentives for industries to setup units in the SEZ, hampering current plans of land sale. Land parcel sale at the SEZ is yet to pick up.

Currency Fluctuation: APSEZ having exposure to dollar denominated foreign currency loans and revenues faces forex risk as it does not undertake any major hedge to currency movements.

## Financial Statements

## Key Assumptions

Year to March	FY17	FY18	FY19E	FY20E
<b>Macro</b>				
GDP(Y-o-Y %)	7.1	6.7	7.3	7.6
Inflation (Avg)	4.5	3.6	4.5	4.5
Repo rate (exit rate)	6.3	6.0	6.8	6.8
USD/INR (Avg)	67.1	64.5	70.0	72.0
<b>Company</b>				
Mundra cargo (MT)	114.2	121.6	129.9	142.2
Avg. realisation (INR/t)	386	333	341	363
EBITDA margin (%)	64.3	67.4	62.4	64.2
SEZ land sold (Acre)	107	83	100	100

## Income statement

(INR mn)

Year to March	FY17	FY18	FY19E	FY20E
Net revenue	84,394	113,230	113,045	135,099
Cost of Operations	18,905	33,151	31,882	39,374
Other operating expenses	4,736	4,984	4,885	5,436
Employee costs	3,831	4,473	3,687	4,039
Total operating expenses	27,472	42,608	40,454	48,849
EBITDA	56,921	70,621	72,591	86,250
Depreciation	11,602	11,884	13,141	14,299
EBIT	45,319	58,738	59,450	71,951
Less: Interest Expense	13,932	14,954	13,799	13,724
Add: Other income	10,401.1	10,109.29	10,436.08	10,336.2
Profit Before Tax	41,789	52,341	56,087	68,564
Less: Provision for Tax	2,866	15,442	15,144	18,512
Less: Minority Interest	(100)	163	310	542
Add: Exceptional items	-	(1,552)	-	-
Associate profit share	93	-	-	-
Reported Profit	39,115	36,736	40,634	49,510
Exceptional Items	-	1,552	-	-
Adjusted Profit	39,115	35,184	40,634	49,510
Shares o/s (mn)	2,070	2,070	2,070	2,071
Adjusted Basic EPS	18.9	17.0	19.6	23.9
Diluted shares o/s (mn)	2,070	2,070	2,070	2,071
Adjusted Diluted EPS	18.9	17.0	19.6	23.9
Adjusted Cash EPS	24.5	22.7	26.0	30.8
Dividend per share (DPS)	1.3	2.0	2.9	3.6
Dividend Payout Ratio(%)	8.3	13.5	18.0	18.0

## Common size metrics

Year to March	FY17	FY18	FY19E	FY20E
Operating expenses	32.6	37.6	35.8	36.2
Depreciation	13.7	10.5	11.6	10.6
Interest Expense	16.5	13.2	12.2	10.2
EBITDA margins	67.4	62.4	64.2	63.8
Net Profit margins	46.2	31.2	36.2	37.0

## Growth ratios (%)

Year to March	FY17	FY18	FY19E	FY20E
Revenues	18.7	34.2	(0.2)	19.5
EBITDA	24.4	24.1	2.8	18.8
PBT	34.0	25.3	7.2	22.2
Adjusted Profit	35.0	(10.0)	15.5	21.8
EPS	35.0	(10.0)	15.5	21.8

## Infrastructure - Ports

Balance sheet		(INR mn)			
As on 31st March	FY17	FY18	FY19E	FY20E	
Share capital	4,142	4,142	4,142	4,142	
Reserves & Surplus	171,118	206,546	239,866	280,464	
Shareholders' funds	175,260	210,688	244,008	284,606	
Minority Interest	1,392	1,496	1,806	2,348	
Long term borrowings	180,863	207,380	181,295	161,748	
Short term borrowings	45,316	20,950	20,950	20,950	
Total Borrowings	226,178	228,330	202,244	182,698	
Long Term Liabilities	10,620	12,320	12,320	12,320	
Def. Tax Liability (net)	(17,759)	(11,681)	(11,681)	(11,681)	
<b>Sources of funds</b>	<b>395,692</b>	<b>441,152</b>	<b>448,696</b>	<b>470,289</b>	
Gross Block	188,486	217,398	282,132	303,916	
Net Block	166,628	184,441	236,034	243,519	
Capital work in progress	45,140	45,455	2,482	2,680	
Intangible Assets	43,907	42,260	42,260	42,260	
Total Fixed Assets	255,675	272,155	280,775	288,458	
Non current investments	2,523	5,591	5,591	5,591	
Cash and Equivalents	19,768	29,676	24,976	24,111	
Inventories	6,571	5,203	5,004	6,180	
Sundry Debtors	19,784	35,401	29,661	36,985	
Loans & Advances	41,110	49,276	52,878	59,279	
Other Current Assets	70,505	63,345	69,329	70,447	
Current Assets (ex cash)	137,969	153,224	156,872	172,890	
Trade payable	4,937	4,897	4,650	5,615	
Other Current Liab	15,306	14,597	14,869	15,147	
Total Current Liab	20,244	19,494	19,519	20,761	
Net Curr Assets-ex cash	117,726	133,730	137,354	152,129	
<b>Uses of funds</b>	<b>395,692</b>	<b>441,152</b>	<b>448,696</b>	<b>470,289</b>	
BVPS (INR)	84.7	101.8	117.9	137.4	

Free cash flow		(INR mn)			
Year to March	FY17	FY18	FY19E	FY20E	
Reported Profit	39,115	36,736	40,634	49,510	
Add: Depreciation	11,602	11,884	13,141	14,299	
Interest (Net of Tax)	12,976	10,542	10,073	10,018	
Others	(10,805)	3,990	(6,400)	(6,089)	
Less: Changes in WC	(12,263)	(7,071)	(3,623)	(14,775)	
Operating cash flow	40,626	56,081	53,824	52,962	
Less: Capex	32,504	29,250	21,761	21,982	
<b>Free Cash Flow</b>	<b>8,121</b>	<b>26,832</b>	<b>32,063</b>	<b>30,980</b>	

Cash flow metrics				
Year to March	FY17	FY18	FY19E	FY20E
Operating cash flow	40,626	56,081	53,824	52,962
Financing cash flow	(13,247)	(18,890)	(47,198)	(42,182)
Investing cash flow	(26,394)	(38,458)	(11,325)	(11,646)
Net cash Flow	985	(1,267)	(4,699)	(866)
Capex	(32,504)	(23,104)	(21,761)	(21,982)
Dividend paid	(7)	(3,240)	(7,314)	(8,912)

Profitability and efficiency ratios				
Year to March	FY17	FY18	FY19E	FY20E
ROAE (%)	24.9	18.2	17.9	18.8
ROACE (%)	14.6	16.3	15.7	17.9
Inventory Days	84	65	58	52
Debtors Days	85	89	105	90
Payable Days	87	54	55	48
Cash Conversion Cycle	82	100	109	94
Current Ratio	7.8	9.4	9.3	9.5
Gross Debt/EBITDA	4.0	3.2	2.8	2.1
Gross Debt/Equity	1.3	1.1	0.8	0.6
Adjusted Debt/Equity	1.3	1.1	0.8	0.6
Interest Coverage Ratio	3.3	3.9	4.3	5.2

Operating ratios				
Year to March	FY17	FY18	FY19E	FY20E
Total Asset Turnover	0.2	0.3	0.3	0.3
Fixed Asset Turnover	0.4	0.5	0.4	0.5
Equity Turnover	0.5	0.6	0.5	0.5

Valuation parameters				
Year to March	FY17	FY18	FY19E	FY20E
Adj. Diluted EPS (INR)	18.9	17.0	19.6	23.9
Y-o-Y growth (%)	35.0	(10.0)	15.5	21.8
Adjusted Cash EPS (INR)	24.5	22.7	26.0	30.8
Diluted P/E (x)	20.2	22.4	19.4	15.9
P/B (x)	4.5	3.7	3.2	2.8
EV / Sales (x)	11.7	8.6	8.5	6.9
EV / EBITDA (x)	17.5	14.0	13.3	11.0
Dividend Yield (%)	0.3	0.5	0.8	0.9

### Peer comparison valuation

Name	Market cap (USD mn)	EV / EBITDA (X)		P/B (X)		ROAE (%)	
		FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
Adani Ports and Special Economic Zone	10,879	13.3	11.0	3.2	2.8	17.9	18.8
Gujarat Pipavav Port	716	11.0	8.8	2.5	2.5	12.2	15.6
Median	-	12.1	9.9	2.9	2.6	15.0	17.2
AVERAGE	-	12.1	9.9	2.9	2.6	15.0	17.2

Source: Edelweiss research



## Additional Data

### Directors Data

Mr. Gautam S. Adani	CMD, Promoter & Executive Director	Mr. Rajesh S. Adani	Promoter & Non-Independent Director
Dr. Malay Mahadevia	Executive Director	Prof. G. Raghuram	Independent & Non Executive Director
Mr. G.K. Pillai	Independent & Non Executive Director	Mr. Sanjay Lalbhai	Independent & Non Executive Director
Mr. A. K. Rakesh	GMB Nominee	Ms. Radhika Haribhakti	Independent & Non Executive Director

Auditors - M/s. S. R. Batliboi & Associates

*\*as per last annual report*

### Holding – Top10

	Perc. Holding		Perc. Holding
Adani gautam s	39.25	Life insurance corp	7.59
Adani tradeline	6.78	Afro asia trade & in	4.42
Emerging market inv	4.13	Universal trading co	3.9
Worldwide emerge mkt	3.82	Fmr llc	1.64
Elara india opportun	1.29	Vanguard group	1.19

*\*in last one year*

### Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
29 Jun 2018	CAMAS INVESTMENTS PTE LTD	BUY	13526309	369.65
29 Jun 2018	CAMAS INVESTMENTS PTE LIMITED	BUY	13526309	369.65
29 Jun 2018	S B ADANI FAMILY TRUST	SELL	27052618	369.65
21 Jun 2018	AAFTS2164Q	SELL	37500000	369.65
21 Jun 2018	EUROPACIFIC GROWTH FUND	BUY	38150865	369.65
21 Jun 2018	GAUTAM S ADANI FAMILY TRUST	SELL	12480142	369.65

*\*in last one year*

### Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
25 Jun 2018	Pan Asia Trade & Investment Pvt Ltd	Sell	5208562.00
25 Jun 2018	Gautam S. Adani & Rajesh S Adani (On Behalf Of S. B. Adani Family Trust)	Sell	37500000.00
25 Jun 2018	Gautam S. Adani & Priti G. Adani (On Behalf Of Gautam S. Adani Family Trust)	Sell	12480142.00
05 Feb 2018	Emerging Market Investment DMCC	Buy	150000.00
29 Jan 2018	Emerging Market Investment DMCC	Buy	8250000.00

*\*in last one year*

Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
Adani Ports and Special Economic Zone	BUY	SO	L	Gujarat Pipavav Port	BUY	None	None

## ABSOLUTE RATING

Ratings	Expected absolute returns over 12 months
Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

## RELATIVE RETURNS RATING

Ratings	Criteria
Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
	Stock return < 1.25 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

## RELATIVE RISK RATING

Ratings	Criteria
Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

## SECTOR RATING

Ratings	Criteria
Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
	Sector return < 1.25 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return

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## Coverage group(s) of stocks by primary analyst(s): Infrastructure - Ports

Adani Ports and Special Economic Zone, Gujarat Pipavav Port

### Recent Research

Date	Company	Title	Price (INR)	Recos
09-Aug-18	Gujarat Pipavav Port	Altered cargo mix trips margin; Result Update	115	Buy
06-Aug-18	Adani Ports and SEZ	In for long haul — volume uptick sustains; Result Update	397	Buy
17-May-18	Gujarat Pipavav Port	Volume picks up; realisation pressure to persist; Result Update	134	Buy

### Distribution of Ratings / Market Cap

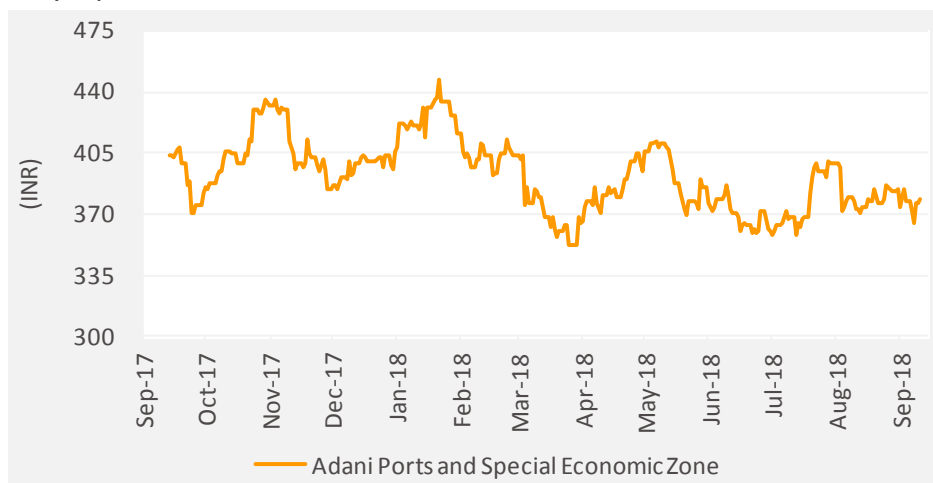
#### Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

### Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

### One year price chart



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