Adani Ports and Special Economic Zone Ltd.

August 29th , 2014

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Adani Ports and Special Economic Zone Ltd (APSEZ), established in 1998, is Adani Group's crown jewel and the largest port in India. Previously known as Mundra Port & Special Economic Zone Ltd, the company changed its name on January 6, 2012. The company is engaged in the business of developing, operating and maintaining the Mundra Port and Port based related infrastructure facilities, including Multi product Special Economic Zone. With presence across six ports in India, namely, Mundra Ports, Adani Hazira Port Pvt Ltd, Adani Petronet (Dahej) Port Pvt Ltd, Adani Mormugao Port Pvt Ltd, Adani Vizag Coal Terminal Pvt. Ltd and Adani Kandla Bulk Terminal Pvt Ltd, the company also operates internationally. With an annual cargo handling capacity of 112.8 MMT, as of 2014, APSEZ is the country's first multi-product port-based special economic zone.

Investor's Rationale

Acquisition of Dhamra port - a strategic fit for the company: Dhamra port's strategic location allows APSEZ to tap a larger market, the most prominent of which is the Chota Nagpur plateau. This region is a store house of minerals like mica, bauxite, copper, limestone, iron ore and coal. The Damodar valley, around the Bengal-Bihar border is rich in coal and it is considered as the prime center of coking coal in the country. Massive coal deposits are found in the central basin spreading over 2,883 sq.km. Coal deposits are also spread over central parts of Orissa and northern Chhattisgarh. Dhamra Port is well located to serve for domestic movement of coal from this region. With the recent acquisition of Dhamra Port, the company further enhanced its portfolio and is now forayed into Eastern Coast of India.

Strong projects pipeline, expansion on track: APSEZ has a strong portfolio of projects on the Indian west coast other than the flagship Mundra port. These projects are comprised of brown-field port development i.e. currently at Dahej & Hazira and as terminal operator at the major ports i.e. coal terminal under development at the Murmagao port. Such projects would help APSEZ to gain market share and expand its footprint with a target to achieve 200 MMT capacity by 2020.

Container volumes to drive sales: Mundra's container volumes have grown significantly at a CAGR of 24.9% from 1.29 mn TEU in FY11 to 2.39 mn TEU in FY14. We believe the container traffic on the western coast would be driven by improvement in the overall export-import (exim) cycle, led by improvement in engineering goods imports and textile exports.

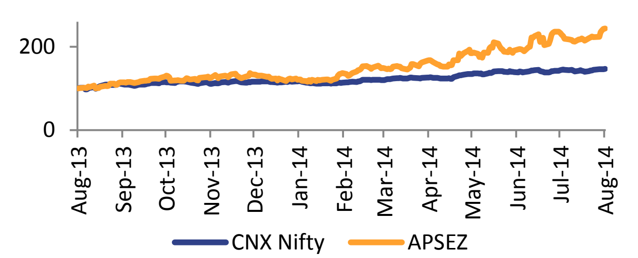
Market Data

Rating	BUY
CMP (₹)	282.9
Target (₹)	330
Potential Upside	~16.6%
Duration	Long Term
Face Value (₹)	2.0
52 week H/L (₹)	302.7/118.7
Adj. all time High (₹)	297.5
Decline from 52WH (%)	6.6
Rise from 52WL (%)	138.3
Beta	2.2
Mkt. Cap (₹bn)	585.6
Enterprise Value (₹bn)	698.9

Fiscal Year Ended

Y/E	FY13A	FY14A	FY15E	FY16E
Revenue (₹bn)	35.8	48.2	62.6	79.7
EBITDA (₹bn)	23.8	29.2	38.7	49.8
Net Profit (₹bn)	16.2	17.4	21.4	27.5
EPS (₹)	8.1	8.5	10.4	13.4
P/E (x)	34.9	33.5	27.2	21.2
P/BV (x)	8.9	6.6	5.5	4.4
EV/EBITDA (x)	28.7	23.8	17.9	13.8
ROCE (%)	12.3	13.4	14.4	16.3
ROE (%)	25.4	19.8	20.1	20.9

One year Price Chart



Shareholding Pattern	Jun'14	Mar'14	Diff.
Promoters	75.0	75.0	-
FII	18.1	17.5	0.6
DII	2.5	3.2	(0.7)
Others	4.4	4.3	0.1

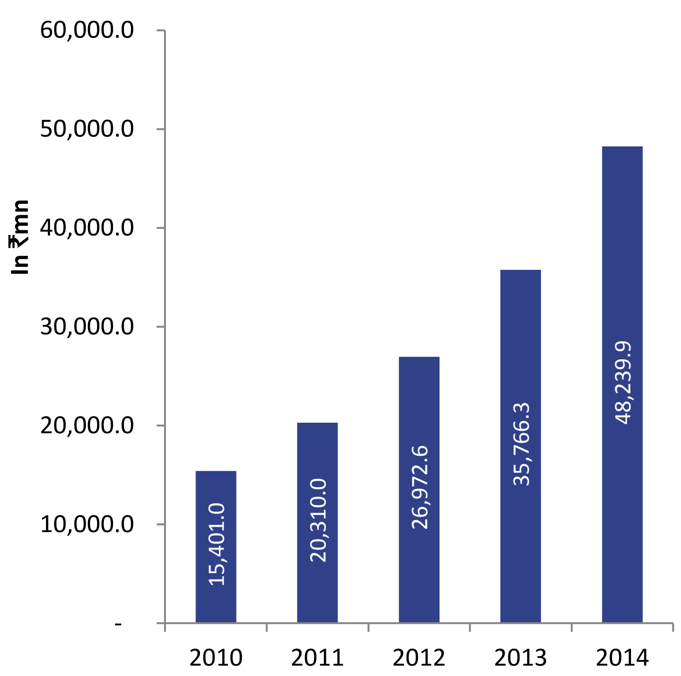
Adani ports and SEZ Ltd.- India's largest multi-port operator

APSEZ is engaged in the business of developing, operating and maintaining the port and port based related infrastructure facilities, including Multi-product special economic zone.

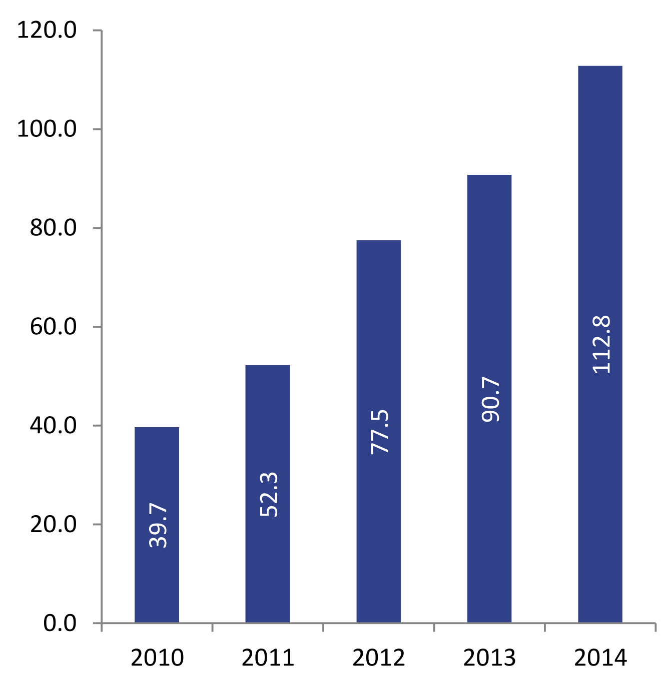
Adani Port and SEZ Ltd (APSEZ) is a part of India's leading infrastructure conglomerate, the Adani Group. Established in 1998, the company holds country's largest private port and special economic zone. The company is engaged in the business of developing, operating and maintaining the port and port based related infrastructure facilities, including Multi-product special economic zone. APSEZ's port services include marine, handing intra-port transport, storage, other value-added and evacuation services for a diverse range of customers, primarily terminal operators, shipping lines and agents, exporters, importers and other port users. This helps the company to diversify its income sources, reduce its financial risk and compete more effectively. APSEZ is the only private sector port operator with presence across six ports in India. APSEZ's aim is to increase annual cargo handling capacity from 112.8 MMT (million metric tons) in 2014 to 200 MMT by 2020.

APSEZ's three operational facilities on the west coast of India are capable of handling cape size bulk cargo vessels and more than 16,000 TEUs (TEU: 20 foot equivalent units) container vessels. The company also provides other services, which includes infrastructure leasing and logistics services at the Mundra Port through its surrounding infrastructure, including the Mundra SEZ, which the company has developed and operates. Mundra SEZ is one of the largest operating port-based multi-product special economic zones in India. The company has developed and operates 10 terminals having 28 berths to handle bulk and container cargo; and 2 single point mooring facilities at the ports of Mundra, Dahej and Hazira. The port of Mundra, which is considered as the group's crown jewel and the largest port in India has 4 bulk terminals having 15 berths to handle dry as well as liquid bulk cargo, 3 container terminals having 6 berths and 2 offshore single point mooring facilities for handling crude cargo. At the port of Dahej, the company has developed and operates a dry bulk cargo terminal having 2 berths. The company has also developed and operates 1 bulk terminal having 3 berths to handle dry as well as liquid bulk cargo and 1 container terminal having 2 berths to handle container cargo at the port of Hazira.

Total consolidated income trend



Consolidated cargo volumes trend (MMT)



Strong growth in cargo volumes triggered 36% YoY rise in Q1FY15 net profit

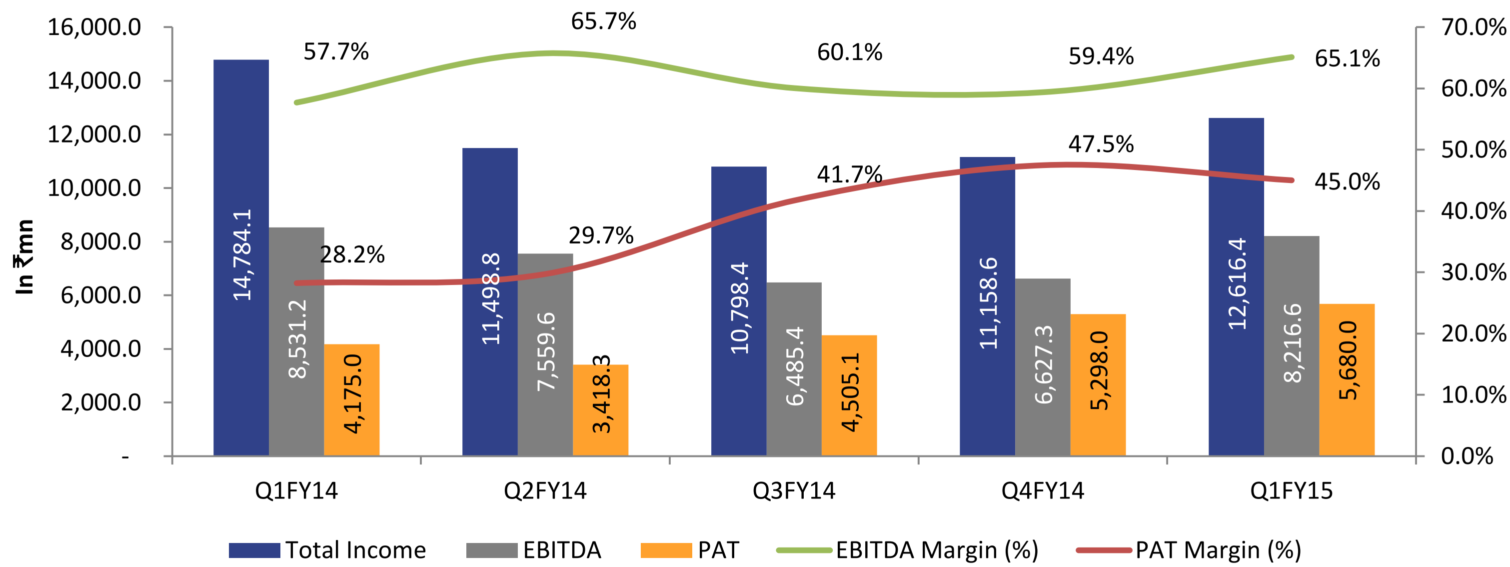
APSEZ reported a healthy performance in Q1FY15 with 36.0% YoY growth in net profit at ₹5,680.0 mn as against ₹4,175.0 mn.

During Q1FY15, the company handled 33.83 MMT of cargo on consolidated basis, up 27% from the corresponding quarter of last fiscal.

APSEZ managed to report a robust growth of 36.0% YoY in its consolidated net profit in Q1FY15 at ₹5,680.0 mn as against ₹4,175.0 mn in Q1FY14 helped by higher other income and sales volume growth; however the higher depreciation cost on account of commissioning of assets like Dahej and Hazira capped some of the profitability. Other income grew sharply by 88.4% to ₹1,687.4 mn in Q1FY15 as against ₹895.6 mn in Q1FY14. While the depreciation expense grew by 18.8% YoY to ₹1,758.7 mn in Q1FY15. During Q1FY15, the company handled 33.83 MMT of cargo on consolidated basis, up 27% from the corresponding quarter of last fiscal. The company's port at Mundra in Kutch district of Gujarat alone handled 28.86 MMT of cargo in Q1FY15, a 22% growth over the year-ago period. During the said period, Dhamra port has contributed another 4.2 MMT to the total cargo. On the margins front, the company managed to improve its EBITDA margins to 65.1% in Q1FY15 as against 57.7% in Q1FY14 on account of improved operational performance.

However, the consolidated total income declined by 14.7% YoY to ₹12,616.4 mn in Q1FY15 as against ₹14,784.1 mn in Q1FY14. This decline in total income on yearly basis came as the company included a consideration of ₹700.1 mn in Q1FY14 received towards transfer of container terminal (CT3) operated by APSEZ to a 50:50 JV with MSC. While on sequentially basis, the consolidated total income grew by 13.1% driven by healthy growth in its volumes with meaningful contributions coming from Dahej and Hazira ports.

Quarterly performance trend



Out of total cargo handled of 112.8 MMT, Mundra Port alone contributed nearly 101.1 MMT cargos in FY14 and is now the only commercial port in India to achieve this milestone and holds the No. 1 position amongst all commercial ports in terms of cargo handling.

During FY14, APSEZ has reported a strong set of numbers, with the total income grew sharply by 34.9% YoY to ₹48,239.9 mn in FY14 as against ₹35,766.3 mn in FY13 supported by strong growth in cargo volumes. Consolidated cargo volume in FY14 increased sharply by 24.3% YoY to 112.8 MMT as against 90.7 MMT in FY13. Out of total cargo handled of 112.8 MMT, Mundra Port alone contributed nearly 101.1 MMT cargos in FY14 and is now the only commercial port in India to achieve this milestone and holds the No. 1 position amongst all commercial ports in terms of cargo handling. In line with this, consolidated EBIDTA increased sharply by 22.9% YoY to ₹29,203.5 mn in FY14 as compared to ₹23,759.8 mn in FY13. Further, the other income grew sharply by 158.5% YoY to ₹6,836.3 mn in FY14 as against ₹2,644.4 mn in FY13. Though other income was higher, the growth in the consolidated PAT (without considering Abbot Point, which had been divested last year) increased merely by 7.2% YoY to ₹17,396.4 mn in FY14 as compared to ₹16,232.2 mn in the last year, due to higher interest and depreciation charges. Interest and depreciation expenses grew sharply by 53.9% YoY and 80.3% YoY to ₹6,494.8 mn and ₹9,767.6 mn respectively.

The Dhamra port acquisition gives the company an opportunity to replicate its development and phenomenal growth of the Mundra port on the eastern coast of India.

APSEZ completed the acquisition of 100% stake in the Dhamra Port Company Limited (DPCL)

APSEZ recently has completed the acquisition of 100% stake in the Dhamra Port Company Limited (DPCL) from L&T Infrastructure Development Projects (L&T IDPL) and Tata Steel. The Dhamra port acquisition now gives the company an opportunity to replicate its development and phenomenal growth of the Mundra port on the eastern coast of India. The Dhamra port has a capacity to handle 25 MMT (Phase-1) of cargo and it handled 14.3 MMT of cargo in FY14. The company expects that the second phase of development (75 MMT capacity) will be initiated in coming months at a cost of ₹80 bn and company aims to complete this expansion in the next 30 months. The expansion will allow the Dhamra port to reach 100 MMT of cargo capacity by 2020 and therefore will allow Adani Ports to fulfill its stated vision of becoming a 200 MMT ports business well before the year 2020.

Addition of Dhamra port – a strategic fit for the company

Particulars	Dhamra port
Capacity (Phase -1)	*25 MMT*
Storage	2.2 MMT
Draft	*17.5 MMT*
Phase-2 expansion plan	Addition of another 75 MMT capacity with an investment of ₹80 bn.

During FY14, the company's Mundra port handled highest ever coal volume of 36.2 MMT surpassing Paradip Port coal volumes of 32.1 MMT.

Volume growth at the Mundra port continues to remain strong

Mundra port alone has achieved a milestone in cargo handling that has crossed 100 MMT mark by handling 101.1 MMT of cargo in FY14 and is now the only commercial port in India to achieve this milestone amongst all commercial ports in terms of cargo handling. It registered a 23.1% growth in FY14 as compared to average 1.8% growth in cargo achieved by the rest all major ports during the said period. During FY14, the company's Mundra port handled highest ever coal volume of 36.2 MMT surpassing Paradip Port coal volumes of 32.1 MMT. In case of containers, the company handled 2.4 mn TEUs registering a growth of 38.0%. While, container volume handling at the rest all major ports witnessed a de-growth of 3% in during the same period. Even Dahej have started showing signs of scaling up. The port at Dahej continues to perform very well. It handled cargo of 7.9 MMT in FY14, a rise of 4% as compared to 7.6 MMT in corresponding period previous year. During FY14, the company's Adani Hazira Port, which operates all non-LNG facilities in Hazira Port, successfully handled its first liquid bulk vessel M.T. JBU OPAL. The vessel discharged 4,699 metric tons of Vinyl Acetate Monomer (VAM) at a record discharge rate of 350 metric tons per hour.

With the new and the strong government at center, the investor and business sentiment has shown some sign of revival. Also, as per the latest economic data, we expect that the economy has bottomed out and has already shown initial sign of revival. With the expected revival in the economy, import and export activity is likely to pick up in the coming quarters and hence will increase the cargo volume. APSEZ, being the largest port player (in terms of cargo handling capacity of 112.8 MMT in 2014) will benefit the most with this revival.

Cargo growth trend across major ports

Major Ports	FY11	FY12	FY13	FY14	CAGR(FY11-14)
KANDLA	*81.9*	*82.5*	*93.6*	*87.0*	*2.0%*
PARADIP	*68.0*	*67.4*	*56.6*	*68.0*	*0.0%*
JNPT	*64.3*	*65.8*	*64.5*	*62.4*	*(1.0)%*
MUMBAI	*54.6*	*56.2*	*58.0*	*59.2*	*2.7%*
VISAKHAPATNAM	*61.5*	*55.7*	*59.0*	*58.5*	*(1.6)%*
CHENNAI	*56.0*	*54.3*	*53.4*	*51.1*	*(3.0)%*
NEW MANGALORE	*31.6*	*32.9*	*37.0*	*39.4*	*7.7%*
V.O. CHIDAMBARANAR	*35.0*	*31.0*	*28.3*	*28.6*	*(6.5)%*
Haldia Dock Complex	*25.7*	*28.1*	*28.1*	*28.5*	*3.5%*
KAMARAJAR (ENNORE)	*17.9*	*20.1*	*17.9*	*27.3*	*15.2%*
COCHIN	*11.0*	*15.0*	*19.9*	*20.9*	*23.8%*
Kolkata Dock System	*12.5*	*12.2*	*11.8*	*12.9*	*0.9%*
MORMUGAO	*50.0*	*39.0*	*17.7*	*11.7*	*(38.3)%*
Total	***570.0***	***560.2***	***545.8***	***555.5***	***(0.9)%***
APSEZ Mundra	***51.7***	***64.0***	***82.1***	***101.1***	***25.1%***

Agreement with CMA CGM for setting up 4th container terminal complements its existing portfolio of services

This new container terminal will make Mundra the largest container port in the country and this project is expected to be completed in the next 24 months and take Mundra's total container handling capacity to 5.5 mn TEUs.

APSEZ has signed an agreement (50:50 JV) with France's CMA CGM Group (the world's third largest container shipping company) to develop a new "common user" Container Terminal at an estimated cost of ₹21,000 mn at Mundra port in Gujarat. This will be the fourth container terminal at Mundra. The project comprises design and construction of 650 meters jetty, with a water depth of 16.5 meters. It will also have an area of 27 hectare that will be capable of handling 1.3 mn TEUs (20-ft equivalent units) annually. The terminal will initially have four units of 65 tons capacity of Rail Mounted Quay Cranes, capable of handling 1,800 TEU vessels and Super Post and Ultra Large Container Vessels. These cranes will be the largest and first of its kind in India and this 50:50 JV partnership will help Adani Ports to expand its container terminals footprint across India's coastline and further augment its existing two container handling locations at Mundra and Hazira. The company has already announced two container terminals to be constructed at Ennore in Chennai and Dhamra in Odisha. It will allow Adani Ports to fulfill its stated vision of handling 200 MMT of cargo well before the year 2020.

According to the company, this new container terminal will make Mundra the largest container port in the country and this project is expected to be completed in the next 24 months and take Mundra's total container handling capacity to 5.5 mn TEUs.

The company has received a LoI by the Kandla Port Trust to develop a 20 MMT dry bulk terminal at investment of ₹10 bn on BOOT basis for 30 years.

Strong project pipeline to support growth

APSEZ was recently issued LoI (letter of intent) by the Kandla Port Trust to develop a 20 MMT dry bulk terminal at an investment of ₹10 bn on BOOT basis for 30 years. The dry bulk terminal that will be designed to have four berths will come up at Tekra near Tuna off 20 Km from the existing Kandla port with a draft of 16.5 meter which will enable larger vessels calling the port. The construction of the new bulk terminal will begin after signing of the concession agreement with the Kandla Port Trust which is expected shortly. Further, the company is also scaling up capacity at its flagship port, Mundra buoyed by higher demand for coal imports. The company also plans to add another 5 berths (ranking 9-12) multipurpose berths at a cost of ₹7.3 bn which would add a capacity of 15 MMT to the existing 30 MMT. While, the berths 9 and 10 are ready, the next two would be ready in the coming quarters.

The government of India's announcement to incentivize the companies investing in port infrastructure with 100% tax exemption and a 10 year tax holiday augurs well for APSEZ.

Government patronage augurs well for expansion plans

Government of India has incentivized the companies investing in port infrastructure with 100% tax exemption and a 10 year tax holiday. It allows 100% FDI investment in the port infrastructure space and is now focusing on build-own-operate-transfer (BOOT) mechanism (which acts as a risk cover) to encourage investments by companies eyeing expansion. Moreover, the private ports enjoy price flexibility, as the government allows non-major ports to determine their own tariffs in consultation with the State Maritime Boards. This scenario is lucrative for foreign investments and will aid in catalysing the asset ramp up at APSEZ.

We expect company's total income and net profit to grow at a CAGR of 28.5% and 25.7% respectively during FY14-16E.

Term contracts ensures long term earning visibility

APSEZ has entered into long-term contracts with take-or-pay provisions (in most cases) with large customers, such as Tata Power (for coal imports for 4GW Mundra UMPP), Adani Power (coal imports for 4.62GW Mundra power project and other power projects), IOC (crude oil import for 15 MTPA Panipat refinery) and HPCL Mittal Energy (crude oil import for 9 MTPA Bhatinda refinery). Mundra port has two single-point moorings (SPMs) of 25 MTPA each for IOCL Panipat and HMEL Bhatinda, respectively. These long term contracts ensure APSEZ long term earning visibility. We expect company's total income and net profit to grow at a CAGR of 28.5% and 25.7% respectively during FY14-16E.

Key Risks

- ✓ **Any unexpected decline in traffic at ports:** Since cargo at ports is contingent on international trade (Imports & Exports), any slowdown in it could affect Mundra Port as well.

- ✓ **Lower cargo volume growth:** Slower-than-expected volume growth, either due to lower coal imports, if domestic coal production ramps up faster than expected, or container cargo growth disappoints due to a slowdown in the economic activity, could hamper sales and profitability.

- ✓ **Regulatory risk regarding SEZs:** The existing SEZ policies and benefits outlined by the government that aims to promote exports are being continuously reviewed. Any changes in the form of reversal of current tax benefits to units under the SEZ territory will significantly undermine the incentives for industries to setup units in the SEZ.

Balance Sheet (Consolidated)

Y/E (₹mn)	FY13A	FY14A	FY15E	FY16E
Share Capital	4,035	4,168	4,168	4,168
Reserve and surplus	59,928	83,513	102,530	127,602
Minority Interest	1,423	1,437	1,465	1,495
Loans	106,622	116,940	130,142	134,132
Other long term liabilities	5,939	7,336	8,069	8,876
Deferred tax Liability	5,530	6,745	6,745	6,745
Provisions	4,043	6,943	8,501	9,991
Current Liabilities	23,077	19,690	22,776	26,352
Capital Employed	**210,596**	**246,771**	**284,397**	**319,360**
Fixed assets	142,933	151,475	160,563	170,197
Goodwill on consolidation	404	404	404	404
Long term loans & advances	11,511	30,928	32,165	34,095
Non-current Investments	771	575	575	575
Deferred tax Assets	244	0	0	0
Current Assets	50,235	54,440	80,087	102,113
Other non-current assets	4,499	8,950	10,604	11,977
Capital Deployed	**210,596**	**246,771**	**284,397**	**319,360**

Profit & Loss Account (Consolidated)

Y/E (₹mn)	FY13A	FY14A	FY15E	FY16E
Total Income	**35,766**	**48,240**	**62,619**	**79,652**
Operating Expenses	12,007	19,036	23,921	29,869
EBITDA	**23,760**	**29,204**	**38,699**	**49,782**
Other Income	2,644	6,836	5,736	5,966
Depreciation	4,220	6,495	7,794	9,353
EBIT	**22,185**	**29,545**	**36,641**	**46,396**
Interest	5,418	9,768	11,721	14,065
PBT	**16,766**	**19,777**	**24,920**	**32,330**
Tax	1,231	2,367	3,468	4,821
Loss/gain on account of discontinued operations	853	0	0	0
PAT	**16,388**	**17,410**	**21,453**	**27,509**
Minority Interest	156	14	14	15
Net Profit	**16,232**	**17,396**	**21,439**	**27,494**

Key Ratios (Consolidated)

Y/E	FY13A	FY14A	FY15E	FY16E
EBITDA Margin (%)	66.4	60.5	61.8	62.5
EBIT Margin (%)	62.0	61.2	58.5	58.2
NPM (%)	45.4	36.1	34.2	34.5
ROCE (%)	12.3	13.4	14.4	16.3
ROE (%)	25.4	19.8	20.1	20.9
EPS (₹)	8.1	8.5	10.4	13.4
P/E (x)	34.9	33.5	27.2	21.2
BVPS(₹)	31.9	42.6	51.8	64.0
P/BVPS (x)	8.9	6.6	5.5	4.4
EV/Operating Income (x)	19.1	14.4	11.1	8.6
EV/EBITDA (x)	28.7	23.8	17.9	13.8

Valuation and view

We believe APSEZ will sustain its growth momentum backed by strong fundamentals, unique asset profile, robust cargo volume growth, strategic customer relations and increasing traction in the domestic market. On the economic front, the increase in container traffic and government initiatives will act as growth drivers. With the global economic pressures phasing out, the company expects to witness a strong revival in demand. Addition of Dhamra port into the company's portfolio likely to aid volume and profitability going ahead. Moreover acquisition of Dhamra port will allow APSEZ to cater to companies situated near eastern coast of India and will further boost its market share (in terms of cargo handled).

At a current market price (CMP) of ₹282.9, the stock trades at an EV/EBITDA of 17.9x FY15E and 13.8x FY16E. We recommend 'BUY' with a target price of ₹330, which implies potential upside of ~16.6% to the CMP from long term perspective.

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