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MUNDRA PORT AND SPECIAL ECONOMIC ZONE LTD.

December 23, 2011

BSE Code:	532921	NSE Code:	MUNDRAPORT	Reuters Code:	MPSE.NS	Bloomberg Code:	MSEZ:IN

Mundra Port and Special Economic Zone Ltd (MPSEZ) is engaged in the business of developing and operating the largest private port in India, the Mundra Port. It is also engaged in developing other port based related infrastructure facilities, including multi product Special Economic Zone. With a capacity to handle million tonnes of cargoes ranging from Bulk cargo like coal, fertilizer, petroleum products to container cargo and automobiles, MPSEZ has marked a record handling of 1.23 million TEU's in FY11. The company is also is in the process of setting up coal import terminal at Vishakhapatnam.

Investor's Rationale

- During Q2FY12, MPSEZ reported an impressive revenue growth of 50% (y-o-y) at ₹6.2 billion backed by significant volume growth in dry cargo, bulk and liquid cargo. Going further, we expect MPSEZ's superior infrastructure and natural advantages to drive its rapid pace of growth with strong volumes improvement. With the overall growth in line with its plan, MPSEZ is expected to mark significant revenue growth of 25-30% in FY12E.

- MPSEZ, the operator of the fourth largest commercial port of India, has set new paradigms for the industry by setting records of handling 111,699 metric tonnes per day of steam coal and a 984,000 metric tonnes of fertilizers handling record in the second quarter of this fiscal.

- Considering the need for port capacity in India and an expected investment of $10 billion over the next five years in the sector, we see substantial business opportunities for the operator of the largest private in the country, MPSEZ. Beside, MPSEZ is also expanding its presence in the name of Adani Port at various other locations on East Coast as well as at Hazira and Dahej.

- With a superior infrastructure and support services to meet ~150mtpa traffic, MPSEZ is strategically located on the west coast spread across 36,000 acres catering to the vicinity of north and northwest India, which account for almost two-thirds of India's GDP. The ideal geographic presence of Mundra port keeps MPSEZ at a greater advantage against its peers by enhancing its potential to attract huge volumes and benefits from economies of scale and higher operational efficiency.

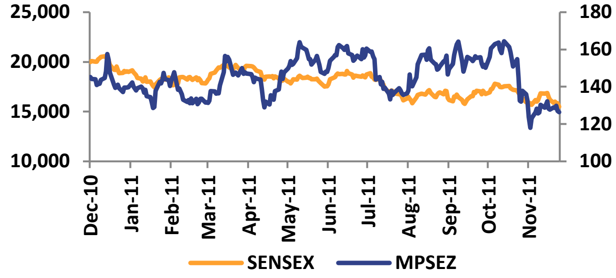
Market Data

Rating	**ACCUMULATE**
CMP (₹)	125
Target (₹)	**162**
Potential Upside	~30%
Duration	Long Term
52 week H/L (₹)	169.7/115.2
All time High (₹)	249
Decline from 52WH (%)	26.4
Rise from 52WL (%)	13.6
Beta	0.84
Mkt. Cap (₹ mn)	251,784
Enterprise Val (₹ mn)	287,347

Fiscal Year Ended

	FY10A	FY11A	FY12E	FY13E
Revenue (₹mn)	14,955	20,001	26,001	35,101
Net Profit(₹mn)	6,671	8,930	11,316	15,793
Share Capital	4,035	4,035	4,035	4,035
EPS (₹)	3.3	4.4	5.6	7.8
PE (x)	37.7	28.2	22.2	15.9
P/BV (x)	7.3	6.0	4.9	3.9
EV/EBITDA (x)	29.2	22.1	17.1	12.7
ROE (%)	19.3	21.3	22.1	24.3
ROCE (%)	9.5	11.9	13.7	16.0

One year Price Chart

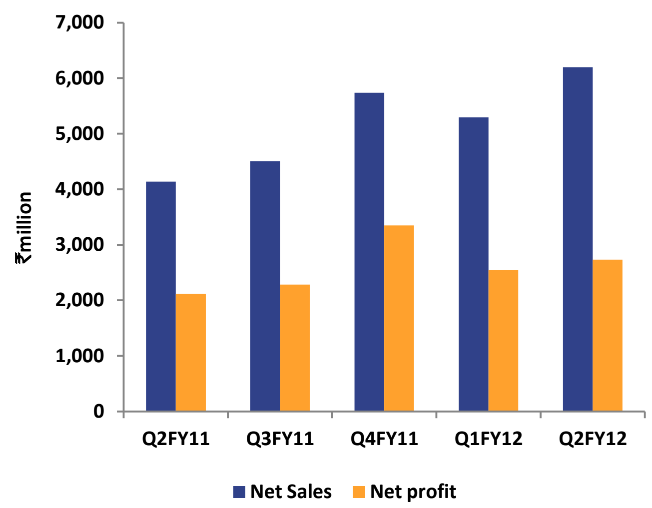


Shareholding Pattern	Sep'11	Jun'11	Diff.
Promoters	77.5%	77.5%	-
Institutional	15.7%	15.4%	0.29
General Public	0.3%	0.0%	0.29
Others	6.6%	7.1%	(0.58)

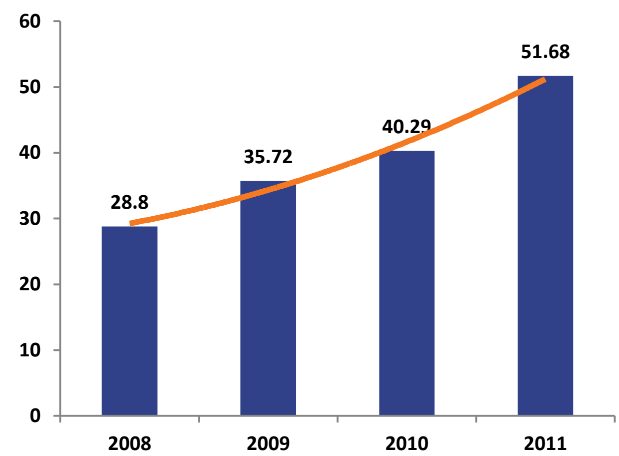
Better operational performance; volumes up 34% yoy

MPSEZ reported an impressive Q2FY12 result, with cargo volume growth of 34% YoY, led by an overall growth in dry cargo, bulk and liquid cargo at 46%, 41% and 33% respectively during the quarter. Container cargo witnessed a lower growth of 16% at 4.4 MMT. It handled 16.8 million tonnes of total cargo in Q2FY12, leading to revenues of ₹6.2 billion (up 50% yoy). EBIDTA for the quarter stood at ₹4.1 billion, reflecting a growth of 47% on y-o-y basis. Backed by increased total Income, the EBIDTA margins remained robust at 68%. The surge in topline also helped the company report a PAT of ₹2.7 billion, reflecting an increase of 29% yoy with net profit margin at 46%. MPSEZ outperformed other Indian ports during the first half of the fiscal by growing 27% in cargo and 20% in container business. With the overall growth in line with its plan, MPSEZ is expected to mark significant revenue growth of 25-30% in FY12E. MPSEZ's superior infrastructure and natural advantages is expected to drive its rapid pace of growth with strong volumes growth in dry, bulk and container.

Volume growth fuels up sales



Cargo volume trend (MTPA)



Commissioning of new coal terminal to augment growth

MPSEZ has started handling coal for Tata power UMPP in Q2FY12, which led to more than 60% YoY surge in coal volumes at 5.13 million tonnes. It has also entered into port service agreements with Adani Power (for 4620 MW) and Tata Power (for 4,000 MW), for transporting imported coal from Indonesia/Australia to their respective power plants. These power plants, when fully operational, would require about ~30 MTPA of coal cargo to be handled at Mundra port. The company is expected to handle ~11 MTPA of coal in FY12E at the new coal terminal for both Adani Power and Tata Power.

MPSEZ sets industry paradigms

MPSEZ, the operator of the fourth largest commercial port of India, has set new records by handling a record 111,699 metric tonnes per day of steam coal to Adani Power's power plant located adjacent to the port followed by a 984,000 metric tonnes of fertilizers handling record in the second quarter of this fiscal.

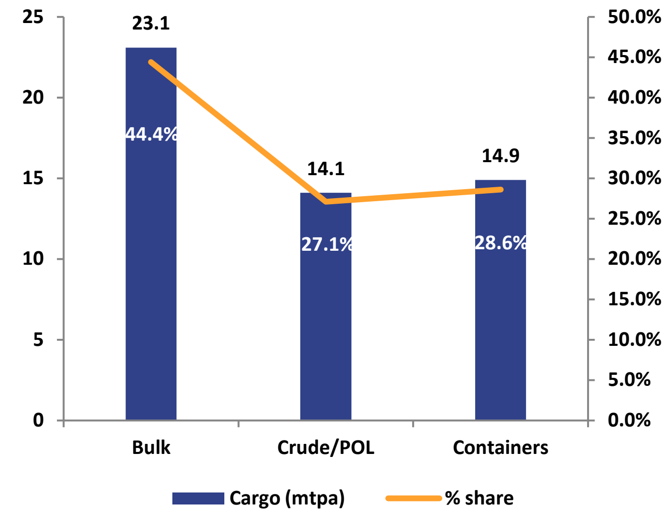
The large tranche of coal delivered by MPSEZ through a world class high speed conveyor belt at a speed of 6,000 metric tonnes per hour stands out to the best coal discharge performance in the country till date. Further, MPSEZ is expanding the West Basin terminal and constructing fourth berth, which is expected to be completed in 2nd quarter of FY13. The company is also investing heavily in augmentation of the material handling system to cater to additional volumes of imported coal for power plants in the vast North West Indian hinterland.

Meanwhile, MPSEZ is also well equipped to handle around 20% share of India's annual fertilizer imports that stand at 22 million tonnes currently backed by its dedicated and fully mechanized fertilizer cargo complex with a total capacity of 500,000 metric tonnes. With India's fertilizer imports slated to rise, MPSEZ intends to capture a higher share of the imported fertilizer cargo in next few years.

Diversified business portfolio; curtails risk

Beyond Mundra, the company holds 74% stake in Adani Petronet Port Pvt (APPL) at Dahej, a JV company with Petronet LNG (PLL) for a solid cargo port terminal at Dahej with a capacity of 15 MTPA. It has won a BOT for a 10 MTPA coal terminal at Mormugoa for a period of 30 years and has been awarded the LOI for construction and operation of 13 berths (bulk, break bulk, liquid cargo, and containers) at the Hazira Port (a 74:26 JV between Shell Gas and Total Gaz of France). Moreover, it has acquired Abbot Point coal terminal, Australia, which has a current capacity of 50 mtpa, which can be extended up to 80 mtpa by FY16E. The terminal has 'take or pay' agreements with nine mining companies including Rio Tinto, Xstrata and BHP. This, put together would give MPSEZ, an additional volume of more than 92 mtpa by FY16E.

Cargo profile of Mundra for FY11



SEZ with distinct advantages; compliments MPSEZ's Port business

Mundra has 26,000 acres of land, of which 16,000 acres have been notified as SEZ by the government. The port and the SEZ complement each other in business as the vast SEZ provides captive cargo to the port and the port provides smooth transport of goods produced in SEZ. Though, so far, Mundra has just leased out a meager ~1800 acres of land, the complementary nature of business provides for significant pickup in land volumes at the SEZ, which is likely to benefit MPSEZ in the coming years.

Hunting new locations for next level of growth

The company is expanding its presence in the name of Adani Port at various other locations on East Coast as well as at Hazira and Dahej. Brand Adani Port will portray larger canvas as they are going even international with recently acquire port in Australia. Currently, the East Coast is being serviced by seven major ports, where Government ports handled 275 million tonnes of cargo in FY11. Over the past five years, cargo traffic has grown at an 11.3% CAGR for west coast ports against 5.2% growth witnessed in the eastern coast of the country.

Strategic location & well-built infrastructure – attracts volumes

Mundra port is strategically located on the west coast spread across 36,000 acres catering to the vicinity of north and northwest India. The port has superior infrastructure and support services to meet ~150mtpa traffic presently and would ramp it up to 225 mtpa by FY'15E. The port has one of the deepest drafts, which range from approx 15 to 32 meters, capable to handle ultra large vessels. As a result, it is able to attract huge volumes and benefits from economies of scale and higher operational efficiency.

Mundra Port is ideally situated to service the huge hinterland of northern and northwest India, which account for almost two-thirds of India's GDP. It has significant distance advantage over other ports to most destinations in Rajasthan, Haryana, Punjab, Delhi – NCR, Uttar Pradesh, Madhya Pradesh, Himachal Pradesh, Uttarakhand and Jammu & Kashmir. Any economic development, taking place in these hinterland states has a direct impact on Gujarat ports. MPSEZ further derives significant advantages from the favourable and proactive government policies and promising governance strategies in Gujarat.

Mundra Port's location provides a natural protection which enables the company to handle cargo throughout the year in all weather conditions, including during severe weather of the monsoon season characterised by high rains, winds and waves, with minimal costs, delays and damages that often impact other more exposed ports.

Long term contracts ~ hedged cargo uncertainty risk

MPSEZ currently derives ~ 50% of its total cargo volumes from long-term contracts with big industrial players. It has inked strategic long-term contracts with several companies including HPCL, IOC, Tata Power and Maruti Suzuki, which provide guaranteed cargo volumes and income from operations at Mundra Port. Such arrangements not only provide stable cash flows to the company, but also give headroom to increase range of operations.

India port capacity, demand-supply mismatch to aggravate

Investments in the port sector of India have lagged targets so far, as private-sector participation has been well below expectations. The economic crisis, a slowdown in export-import (EXIM) traffic, and regulatory flip-flops have further hurt the expected revival in investment in ports over the past three years. However, given a sustained need for port capacity and an expected investment of $10 billion over the next five years, we see substantial business opportunities for MPSEZ.

Key Risk

Uncertainty in traffic at ports

Since cargo at ports is contingent on international trade, any slowdown in it could affect Mundra Port as well. MPSEZ is hedged to some extent from the traffic risk because of the take-or-pay agreements which constitute about 45% of the cargo going ahead.

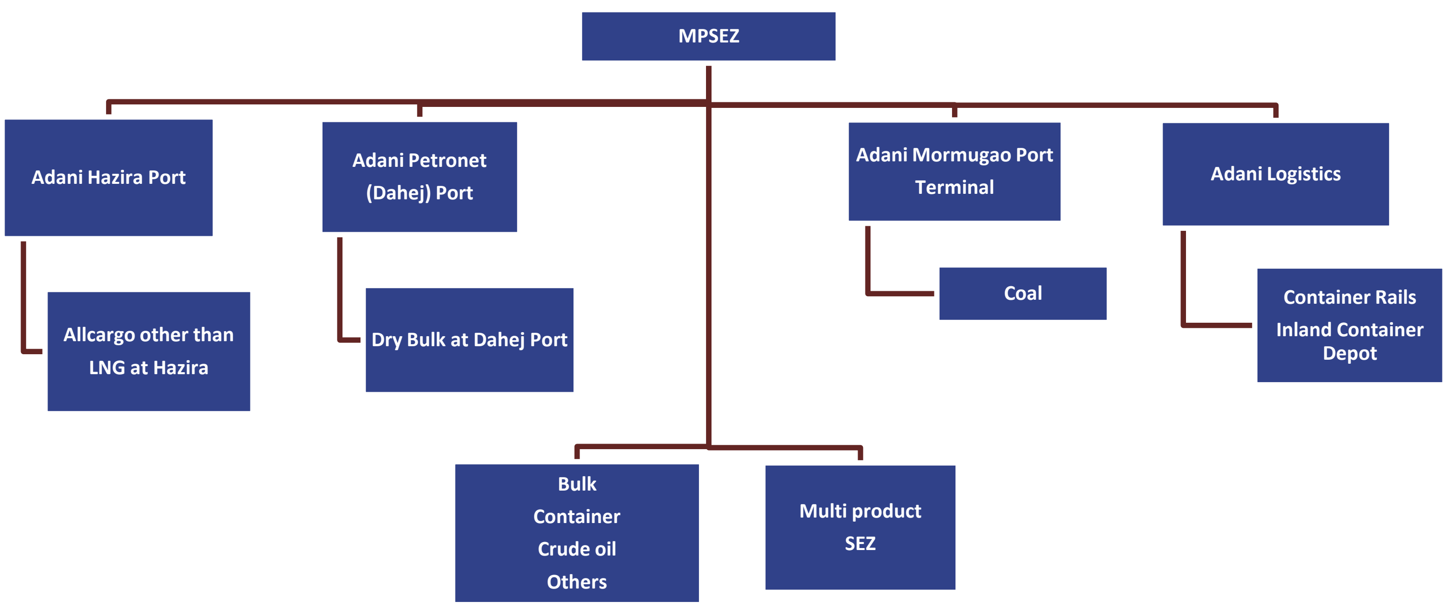
Regulatory changes regarding SEZs

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.

Execution risk in international projects

Although the company has been successful in port projects implemented in India (largely Gujarat), we need to watch out for the execution and the profitability in its international ventures as well the East coast of India. MPSEZ is planning to leverage its captive group business—Adani Enterprises' mining operations and Adani Power's coal imports—to provide assured cargo visibility and thereby minimize the risks associated with a greenfield venture.

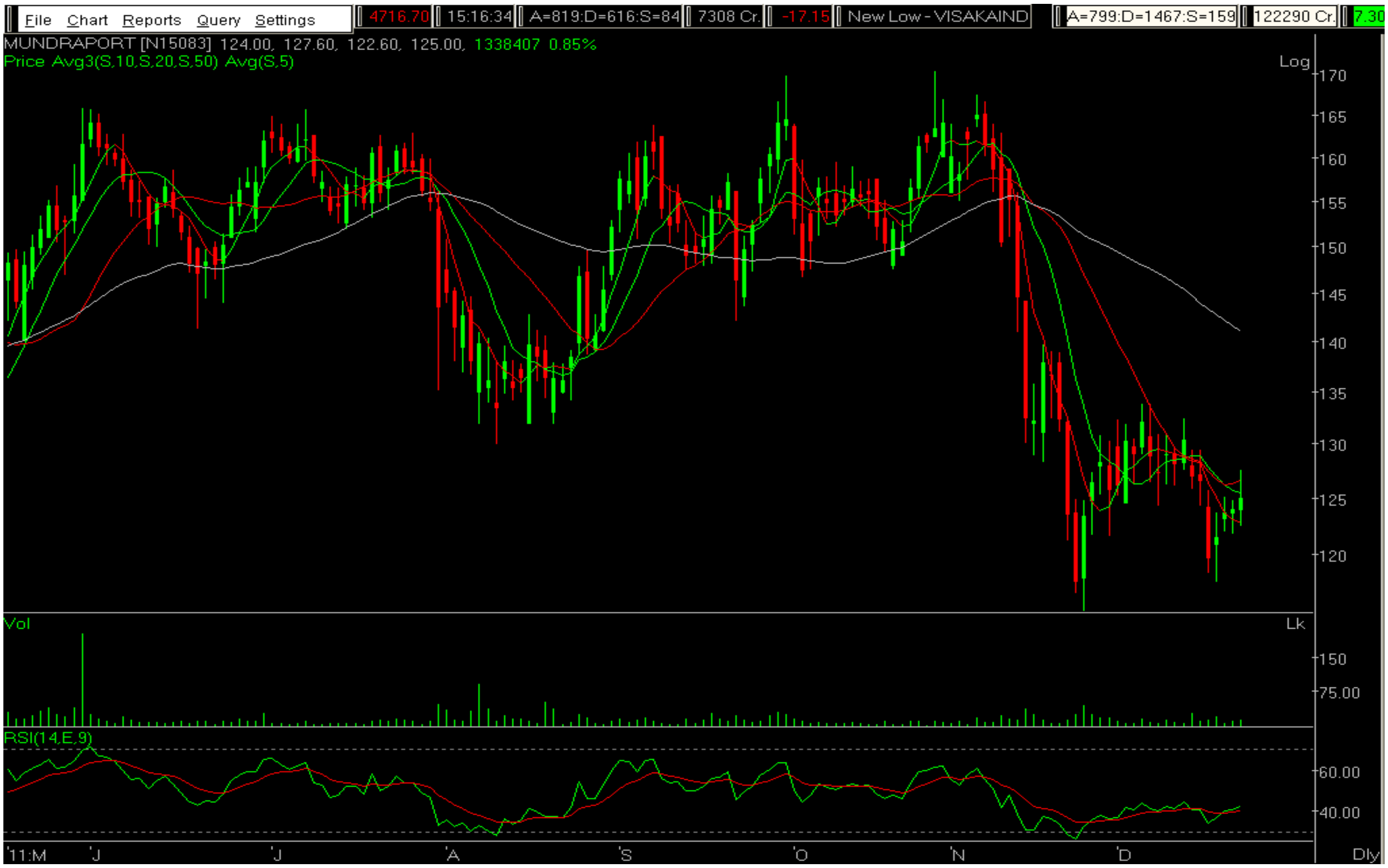
Business Overview



Unlikely to get hit from global macro concerns

Around ~ 90% of MSEZ's estimated traffic comprises coal, crude oil, and container. Of this, coal and crude oil are unlikely to see any impact from global macro concerns, while container traffic should continue to benefit from a shortage of capacity on India's west coast. The slowdown in global trade has already hit container traffic throughput at ports sharply. With the expected rebound in the EXIM container traffic across all ports of India and limited port access in the India's western coast, we expect container traffic at Mundra to grow at a CAGR of 25% over the next 2-3 years.

Technical View



MPSEZ after falling from levels of ₹165 to ₹115 and is consolidating in the range of ₹130-120 for the past one month. The current low is higher is than the previous lows with mild increase in volume suggesting that, the investors are not comfortable in selling this counter any more. Averages are also getting intermingled depicting short term traders are covering their position, 14 Day RSI has also given a positive break out and if MPSEZ breaks out of ₹130 than it can easily go up to ₹150-₹165 levels. We recommend to **"BUY"** the stock on every decline, with the 1 years price objective of ₹162.

Indian Port Industry

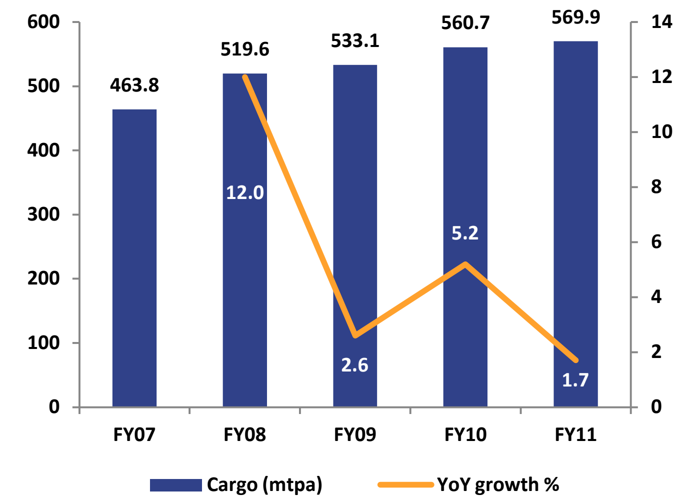
Indian Scenario of Ports

Growth in port industry of a country is linked to location dynamics of key sources of cargo traffic and GDP growth of that country. With expectations of India's GDP growth for FY12E at 7.5% during FY12E, the country's port industry should grow at ~10-11% YoY. The Government of India (GoI) encouraged private investment in the sector by undertaking several favourable policy measures. The GoI has allowed FDI of up to 100% under the automatic route for the construction and maintenance of ports and harbours. It also offers a 10-year tax holiday to enterprises engaged in the business of developing, maintaining and operating ports, inland waterways and inland ports.

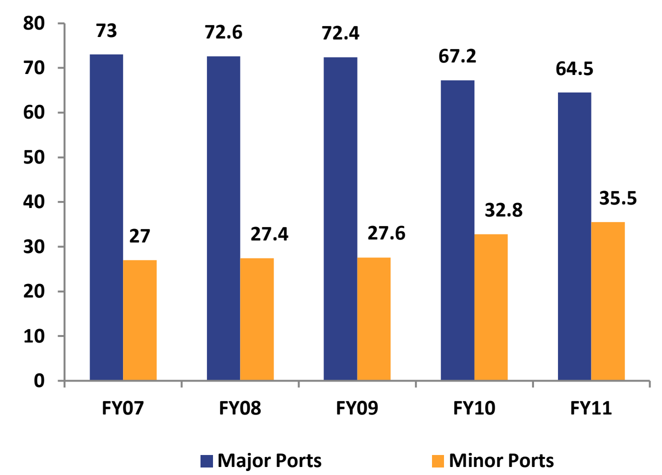
India's 95% external trade by volume and 70% by value moves by sea. Cargo handling volume in 12 Major Ports in India was at 569 mtpa in 2010-11 compared to 561 mtpa in 2009-10, a growth of 1.57%. According to GMB figures, the non-Major Ports in Gujarat have registered a traffic growth of 12.34% over last year with cargo handling rising from 206 mtpa in 2009-10 to 231 mtpa in 2010-11. Meanwhile, the total port capacity of the Gujarat's non-Major Ports grew by 16% this year, reaching 284 mtpa compared 244 mtpa last year.

The cargo traffic is expected to primarily be driven by coal, crude and containers, which contribute about 80% of the total traffic at Indian Ports. Moreover, implementation of the high growth plans for development of northern India through the Delhi-Mumbai Industrial Corridor (involving anticipated investments of ₹225bn) will also drive growth.

Total cargo growth trend for 12 major ports



Trend for Market share of Ports (in %)



Infrastructure and performance of major ports

The 12 major ports in the country are suffering from limited water depths, old infrastructure, inefficient handling systems, poor hinterland connectivity, overstaffing and poor quality of services. The traffic at major ports is growing at a slow rate. This has led to steady decline in market share of the major ports over the last 10 years in the face of growing competition from the rapidly developing non-major ports (intermediate ports developed under public-private partnerships and private ports) like MPSEZ.

Outlook

Investments in the port sector have lagged targets so far, as private-sector participation has been well below expectations. The economic crisis, a slowdown in export-import (EXIM) traffic, and regulatory flip-flops have further hurt the expected revival in investment in ports over the past three years. However, given a sustained need for port capacity on the back of rising trade, we expect a pick-up in investments, and believe the sector presents an investment opportunity of USD10bn over the next five years.

Balance Sheet (Consolidated)

(₹million)	FY10A	FY11A	FY12E	FY13E
Share Capital	4,035.0	4,035.0	4035.0	4035.0
Reserve and surplus	30,504.0	37,864.0	47,162.8	60,938.1
Net Worth	34,539.0	41,899.0	51,197.8	64,973.1
Loan funds	37,668.8	35,924.9	38,124.0	43,824.0
Other Liabilities	6,290.7	6,121.2	6,142.8	6,224.2
Deferred Tax Liability	2,816.8	3,501.5	4,024.2	4,625.4
Minority Interest	822.0	987	1,270.0	1,650.0
Capital Employed	**82,137.3**	**88,433.60**	**100,758.8**	**121,296.7**
Net Block	48,529.1	63,912.0	73,169.0	86,822.4
Capital Work in Progress	19,182.5	21,174.4	19,174.4	18,950.1
Net Fixed Assets	67,711.6	85,086.4	92,343.4	105,772.5
Investments	2,219.3	666.2	666.2	666.2
Net Current Assets	12,206.4	2,681.0	7,749.2	14,858.0
Capital Deployed	**82,137.3**	**88,433.6**	**100,758.8**	**121,296.7**

Profit & Loss Account (Consolidated)

(₹million)	FY10A	FY11A	FY12E	FY13E
Net Sales	**14,955.0**	**20,001.0**	**26,001.3**	**35,101.8**
Total Expenditure	5,293.0	7,007.0	9,184.0	12,284.0
EBIDTA	**9,662.0**	**12,994.0**	**16,817.3**	**22,817.8**
EBITDA Margin %	64.6	65.0	64.7	65.0
Depreciation	1,852.0	2,444.0	2,988.0	3,428.0
EBIT	**7,810.0**	**10,550.0**	**13,829.3**	**19,389.8**
Other Income	1,640.0	1,101.0	1,101.0	1,101.0
Interest	2,177.0	1,671.0	2,320.0	2,724.0
Profit Before Tax	**7,273.0**	**9,980.0**	**12,610.3**	**17,766.8**
Tax	601.0	874.0	1,044.0	1,624.0
Profit After Tax	**2,124.0**	**1,662.0**	**1,030.4**	**1,121.4**
Minority Interest	-1.0	-176.0	-250.0	-350.0
Net Profit	**6,671.0**	**8,930.0**	**11,316.3**	**15,792.8**
NPM%	44.6	44.6	43.5	45.0

Key Ratios

	FY10A	FY11A	FY12E	FY13E
EBITDA Margin (%)	64.6	65.0	64.7	65.0
EBIT Margin (%)	52.2	52.7	53.2	55.2
NPM (%)	44.6	44.6	43.5	45.0
ROCE (%)	9.5	11.9	13.7	16.0
ROE (%)	19.3	21.3	22.1	24.3
EPS (₹)	3.3	4.4	5.6	7.8
P/E (x)	37.7	28.2	22.2	15.9
BVPS (₹)	17.1	20.8	25.4	32.2
P/BVPS (x)	7.3	6.0	4.9	3.9
EV/Operating Income (x)	18.8	14.4	11.1	8.3
EV/EBITDA (x)	29.2	22.1	17.1	12.7

Valuation & View

While the growth momentum at Mundra port would persist, performance of other domestic and global projects - which it has acquired through bidding - will be key monitoring factors going forward. The high visibility and scale up of cargo along with the de-risked revenue model should aid valuations.

MPSEZ is attractively placed at P/E of ~ 15.9x FY13E. Considering the above aspects, we rate the stock as 'BUY' at the current market price of ₹125; the stock is expected to attract 'Premium' over other players.

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