IDFC SECURITIES

MEP Infrastructure Developers

Differentiated play on the highways opportunity

UNRATED

MANAGEMENT SPEAK

25 January 2016

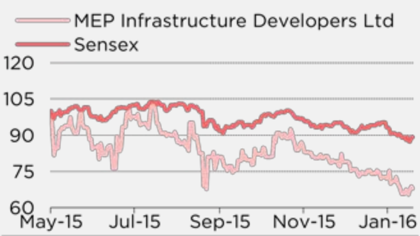
BSE Sensex: 24486

Sector: Infra Developers

Stock data

CMP (Rs)	43
Mkt Cap (Rs bn/USD m)	7.0 /103
Target Price (Rs)	-
Potential from CMP (%)	-
Earnings change (%)	
FY16E	⇔
FY17E	⇔
FY18E	⇔
Bloomberg code	MIDL IN
1-yr high/low (Rs)	67/36
6-mth avg. daily volumes (m)	1.2
6-mth avg. daily traded value	
(Rsm/USDm)	61.8/0.9
Shares outstanding (m)	162.6
Free float (%)	32.8
Promoter holding (%)	67.2

Price performance – relative & absolute



(%)	3-mth	6-mth	1-yr
MIDL	(23.5)	(25.3)	-
BSE Sensex	(10.9)	(12.9)	(16.4)

We met the management of MEP Infrastructure Developers (MEP) and following are the key takeaways:

Market leader with increasing focus on long-term projects: MEP is a leading toll operator in India with an overall experience of 13+ years. It has completed 86 projects, with an aggregate of 148 toll plazas and 953 lanes in India. Currently, MEP is present in 10 states with 23 operational projects. Its focus on increasing the share of long-term projects has led to a rise in share of revenues from such projects to 70% in H1FY16 (39% in FY12). Mumbai Entry Point (MIPL), a key long-term revenue generating project, contributed 21% to MEP's consolidated revenues in H1FY16.

Opportunity pool for tolling projects to grow rapidly: Currently, 104 projects are tolled by the NHAI under short-term tolling. This opportunity pool is likely to expand as NHAI has 6,601km of stretches under various stages of construction as on Dec-15. Once completed, most of these projects will come up for tolling. The Ministry of Road Transport & Highways (MORTH) has introduced the Toll-Operate-Transfer (TOT) model for securitising existing toll roads over 20-25 years. As a result, we expect sustained growth opportunities for tolling players.

Turnaround in PAT led by improving revenues and reduction in debt: MEP's consolidated revenues grew at a CAGR of 22.5% to Rs19.8bn over FY12-15, led by addition of new projects and rise in traffic/toll rates in existing projects. With increase in toll collections in MIPL and repayment of Rs2.6bn debt (Sept 2015: Rs30.9bn), profitability has improved. Also, with NHAI payments being partly deferred in the Chennai bypass project, losses have reduced. Consequently, MEP reported a PAT of Rs110m in H1FY16 as against a net loss of Rs1.2bn in FY15.

MEP, an early mover in the tolling/OMT space, has gained valuable experience in handling projects through their complete life cycle. MEPs diverse geographic presence and asset light model makes it an ideal play on recovery in traffic growth as and when economic recovery gains momentum. MEP's ability to manage multiple projects across different geographies gives it a significant advantage to efficiently manage its growth and expansion. With renewed government focus on building roads through the EPC mode, we see strong growth opportunities for tolling/OMT players like MEP. The stock trades at EV/EBITDA of 8.9x on FY15 basis. Key risk is any adverse impact on profits if toll exemptions are given in the MIPL project and compensation is inadequate.

Key valuation metrics

Year to 31 Mar	FY11	FY12	FY13	FY14	FY15
Net sales (Rs m)	4,494	10,801	12,800	11,979	19,843
Adj. net profit (Rs m)	(762)	(477)	(929)	(1,292)	(1,153)
Shares in issue (m)	109	109	109	109	111
Adj. EPS (Rs)	(7.0)	(4.4)	(8.5)	(11.8)	(10.4)
% change	NM	NM	NM	NM	NM
PE (x)	NM	NM	NM	NM	NM
Price/ Book (x)	22.3	4.4	32.3	(5.3)	(2.1)
EV/ EBITDA (x)	47.7	10.1	9.3	11.4	8.9
RoE (%)	NM	NM	NM	NM	NM
RoCE (%)	2.2	7.7	8.1	5.4	6.9

Source: Company, IDFC Securities Research

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Leading player in tolling and OMT market

MEP is an established pan-India player in the tolling and Operate, Maintain and Transfer (OMT) market, with presence in 10 states. The company has so far executed over 100 projects and currently has a portfolio of 23 operational projects. Its current portfolio has a healthy mix of long-term and short-term contracts, with the share of long-term contracts being on the rise. More long-term projects enhance revenue visibility and provide scope for value addition through improved collection efficiencies. Since tolling/OMT contracts typically do not involve large capital commitments, MEP has an asset light business model.

❑ Leading player in the pure tolling and OMT business

MEP is an established and leading player in tolling operations in the road infrastructure sector, with presence in 10 states. The company focuses on pure toll collection and OMT projects, which involve maintenance obligations in addition to toll collection on operational roads constructed by third parties. MEP commenced operations in 2002 for toll collection at the five Mumbai Entry Points for eight years. MEP, so far, has executed over 100 projects and completed 86 projects, including 148 toll plazas and 953 lanes. As on 30 November 2015, the company had 23 operational projects, 3,249 employees in tolling and maintenance activities and 1,077 contract workforce. MEP is pre-qualified by the NHAI and various statutory corporations and government companies for bidding in tolling and OMT space.

❑ Asset-light business model

MEP focuses on pure toll collection contracts as well as OMT projects, which involve maintenance obligations in addition to toll collection on operating roads (including highways) constructed by third parties. These projects are awarded to the company by statutory corporations or government companies, mainly NHAI (National Highway Authority of India), MSRDC (Maharashtra State Road Development Corporation), RIDCOR (Road Infrastructure Development Company of Rajasthan), MJPRCL (Mumbai JNPT Port Road Corporation Limited) and HRBC (Hooghly River Bridge Commissioners). While a BOT road developer undertakes both the construction and traffic risk, an OMT player like MEP takes only the traffic risk. This model substantially reduces capital intensity in the business.

- For short-term toll collection contracts, MEP does not have to incur any capex.
- For NHAI OMT contracts (typically nine years), MEP has to incur a small upfront capex (typically Rs300-350m) and pre-specified maintenance expenditure during the concession period.
- For OMT projects awarded by state governments, usually an upfront amount is payable.

❑ Well balanced business mix

MEP has a balanced business model with a mix of OMT and toll collection projects. As on 30 November 2015, the company had 23 operational projects comprising 11 short-term tolling projects in the states of Uttar Pradesh (3); West Bengal (2); Rajasthan (2); Tamil Nadu (1); Telangana (1); Karnataka (1) and Gujarat (1), 6 long-term tolling projects located in the states of Maharashtra (3); Delhi (1); West Bengal (1) and Tami Nadu (1), 5 OMT projects located in the states of Maharashtra (2); Tamil Nadu (2) and Andhra Pradesh (1) and 1 BOT project in Maharashtra. Recently, MEP's long-term toll collection project of Delhi entry point (25% stake) was terminated on amicable grounds. MEP is planning to rebid for this project. The various operating models are described as under:

A) Toll collection contracts

Under this type of contract, a private player is given the opportunity to toll highways wherein the construction work has already been completed. As part of this agreement, maintenance of the highway does not come under the purview of the concessionaire. The scope of work includes:

- Right to collect toll on the respective stretch of road.
- To upgrade/provide necessary facilities required to facilitate toll collection (such as making necessary arrangements for power to ensure the proper functioning of the toll plaza, including office equipment installation, maintenance and running all electric equipment, generator and bearing all the expenses during the entire period of the contract).

Concession period

Toll collection contract is typically of a short duration, which in case of NHAI, ranges from 3-12 months for roads constructed under the EPC model and 24 months for roads constructed under the BOT annuity model. In case of state authorities, the concession period typically extends from 12-36 months.

Risk under toll collection contract

Low traffic can deter the revenues.

Salient features

The model provides certain advantages, mentioned below:

- Toll management companies with expertise in this segment can leverage on their experience and operational efficiency to maximise revenues through better traffic management and plugging leakages.
- Low capital intensity as it involves minimal to negligible construction work.
- Payments to authority are monthly, to be paid out of toll collections. Operator has to provide funded bank guarantee equivalent to one month's toll collection and a non-funded bank guarantee of one month's toll collection

B) OMT contracts

This model was introduced by the NHAI in 2009 for select existing and near completion four-lane national highways. Under this model, the concessionaire has to collect the toll and maintain the road asset and properties attached to the asset. The scope of work includes:

- Operation and maintenance of the project section.
- Toll collection.
- Construction of project facilities such as toll plaza, street lighting etc.
- Any major maintenance works (as may be necessary in some cases).

Concession period

The concession period is identified on project specific basis, but typically, for NHAI projects, it is nine years, after which the concessionaire has to transfer the project stretch back to the government authority.

Risk under OMT contract

The concessionaire has to assume the traffic risk, toll collection risk and the financing risk, while the construction risk is relatively lower as compared to EPC/BOT projects.

Salient features

The model provides certain advantages, mentioned below:

- The efficiency of the private sector in toll collection and O&M is leveraged. This typically leads to a decrease in costs as well as increase in revenues – owing to a reduction in traffic leakage.
- A concessionaire is awarded O&M and tolling of a project stretch, for a typical duration of nine years. This significantly reduces the administrative efforts of the awarding agency.
- All OMT projects awarded till date have resulted in the premium (concession fee) being shared by the concessionaire with the awarding authority (NHAI/state authority). Revenue generated through premium sharing can be used for development of other road corridors.

Balanced portfolio mix

MEP has executed more than 100 projects and has completed 86 projects, including 148 toll plazas and 953 lanes. As on 30 November 2015, the company had 23 operational projects as listed below:

- Sixteen long-term and short-term toll collection projects (28 toll plazas) in 10 states;
- One long-term toll collection project of Delhi Entry Points with 124 toll plazas (MEP's share being 25% – recently, the project was amicably terminated and will be rebid for shortly);
- Five long-term OMT projects (covering 2,530 lane kms and 15 toll plazas) and
- One long-term BOT project (covering 2 lane kms and five toll plazas).

Exhibit 1: List of operational short-term toll collection projects*

Toll Name	State	Client	Contract start date	Contract end date	No. of days	Payment to authority (Rs m)
Surajbari Toll Plaza	Gujarat	NHAI	30-Sep-15	29-Sep-16	365	741
Bankapur Toll Plaza	Karnataka	NHAI	03-Jan-15	02-Jan-16	364	441
Manohrabad Toll Plaza	Telangana	NHAI	17-Feb-15	16-Feb-16	364	491
Athur Toll Plaza	Tamil Nadu	NHAI	26-Mar-15	25-Mar-16	365	628
Palsit Toll Plaza	West Bengal	NHAI	26-Mar-15	25-Mar-16	365	950
Paduna Toll Plaza	Rajasthan	NHAI	12-May-15	11-May-16	365	1,001
Garau Toll Plaza	Uttar Pradesh	NHAI	22-Jul-15	22-Jul-16	366	628
Phalodi Ramji Toll Plaza	Rajasthan	RIDCOR	17-Sep-15	31-Mar-16	196	950
Semri Toll Plaza	Uttar Pradesh	NHAI	28-Sep-15	27-Sep-16	365	1,001
Dasna Toll Plaza	Uttar Pradesh	NHAI	27-Nov-15	27-Nov-16	366	281
Surjapur Toll Plaza	West Bengal	NHAI	27-Nov-15	27-Nov-16	366	420

*Source: Company, IDFC Securities Research, *as on 30 November 2015*

Exhibit 2: Operational BOT project*

Name of the Project/State	Concession Operator/Stake	Concession start date	Number of Toll Plazas	Client/Tenure	Payment to Authority	Description of the project
Baramati Project, Maharashtra	Baramati Tollways Private Limited (BTPL), 100%	25-Oct-10	5	MSRC/19 years	Upfront payment of Rs650mn	Construction of the four lane Sakhali bridge on Karha River in Baramati and operation and maintenance of, and collection of toll for the Ring Road and the bridges in Baramati

*Source: Company, IDFC Securities Research, *as on 30 November 2015*

Exhibit 3: List of operational OMT projects*

Name of the project/ State	Name of concession operator/ stake	Concession start date	Number of toll plazas	Client/ Tenure	Payment to authority	Description of the project
Mumbai Entry Points Project, Maharashtra	MEP Infrastructure Private Limited (MIPL)/ 100%	20-Nov-10	5	MSRDC /16 years	Upfront payment of Rs21,000m	Operation and maintenance of and collection of toll at, the five Mumbai Entry Points along with 27 flyovers and certain allied structures on the Sion–Panvel Highway, the Western Express Highway corridor, the Eastern Express Highway corridor, the Lal Bahadur Shashtri Marg corridor and the Airoli Bridge corridor.
Madurai-Kanyakumari Project, Tamil Nadu	Raima Toll Road Private Limited (RTRPL)/ 100%	22-Sep-13	4	NHAI/9 years	Rs1,109m for the first year of the concession period to be paid in 12 equal monthly instalments. The annual payment amount will be increased at the rate of 10% every year as compared to the preceding year	Operation and maintenance of and collection of toll at, the Madurai-Tirunelveli-Panagudi-Kanyakumari section of the National Highway No 7. The Madurai–Kanyakumari section of the National Highway No. 7 is a 243km long, four-lane carriageway in Tamil Nadu.
Hyderabad-Bangalore Project, Andhra Pradesh	MEP Hyderabad Bangalore Toll Road Private Limited (MEP HB)/ 100%	16-May-13	2	NHAI/9 years	Rs1,059m for the first year of the concession period to be paid in 12 equal monthly instalments. The annual payment amount will be increased at the rate of 10% each year as compared to the preceding year	Operation and maintenance of, and collection of toll at, the Hyderabad–Bangalore section of the National Highway No. 7. The Hyderabad–Bangalore section of the National Highway No. 7 is a 251.16 km long four-lane carriageway in Andhra Pradesh.
Chennai Bypass Project, Tamil Nadu	MEP Chennai Bypass Toll Road Private Limited (MEP CB)/ 100%	14-May-13	2	NHAI/9 years	Rs1,530m for the first year of the concession period to be paid in 12 equal monthly instalments. The annual payment amount will be increased at the rate of 10% every year as compared to the preceding year	Operation and maintenance of, and collection of toll for the Chennai bypass section. The Chennai bypass section is a 32.60 km long, six-lane carriageway in Tamil Nadu.
RGSL Project, Maharashtra	MEP RGSL Toll Bridge Private Limited (MEP RGSL)/ 100%	06-Feb-14	1	MSRDC /3 years	Rs690m for the first year of the contract to be paid in 12 equal instalments along with an additional one-time payment of Rs5m. The annual payment is subject to escalation by 10% for the second year and 20% for the third year of the project, to be paid in 12 equal monthly instalments for each year.	The Rajiv Gandhi Sea Link is a 5km long, eight-laned carriageway in Mumbai in Maharashtra

*Source: IDFC Securities Research, Company, *as on 30 November 2015*

Exhibit 4: List of operational long-term toll collection projects**

Name of the project/state	Name of concession operator/stake	Concession start date	Number of toll plazas	Client/ Tenure	Payment to authority	Description of the project
IRDP Solapur Project, Maharashtra	MEP IRDP Solapur Toll Road Private Limited/100%	02-Jan-13	4	MSRDC /156 weeks	Rs208m be paid in three equal annual instalments	Toll collection activities together with maintenance of toll plazas and maintenance of property and equipment provided by MSRDC. The project is located in Solapur
Vidyasagar Setu Project, West Bengal	Rideema Toll Bridge Private Limited/100%	01-Sep-13	1	HRBC/ 5 years	Rs2,610m in five equal annual instalments consisting of an upfront payment of Rs522m and payment of remaining amount in four equal instalments annually in advance	Toll collection activities. 18 lane toll plaza at Vidyasagar Setu, links Howrah to Kolkata
Rajiv Gandhi Salai Project, Tamil Nadu*	Company	08-Mar-14	5	ITEL/3 years	Rs14.6m for the first year, subject to escalation at the rate of 5% p.a. during each subsequent year, for a period of two years	Toll collection service. Previously known as the IT corridor
Kini Tasawade Project, Maharashtra	Raima Toll & Infrastructure Private Limited/100%	29-May-14	2	MSRDC /104 weeks	Rs2,271m to be paid in upfront monthly instalments	Toll collection activities. Located on Satara-Kolhapur section of NH-4
Kalyan Shilphata Project, Maharashtra*	Company	27-Sep-13	2	MSRDC /156 weeks	Rs634m to be paid in upfront monthly instalments	Toll collection service. Connecting Mumbai-Pune highway (NH-4) at Shilphata and Mumbai-Nasik highway (NH-3) at Bhiwandi
Delhi Entry Point, New Delhi	SMYR Consortium/25%	16-May-15	22 entry points	SDMC/ 3 years	Rs106m to be paid on weekly basis	Toll collection activities. 124 entry points of Delhi of which 22 entry points being toll by the company

*Source: Company, IDFC Securities Research, *the company is paid by the respective authority for providing manpower services, **as on 30 November 2015*

Exhibit 5: Revenue from key long-term tolling/OMT projects

Key long term projects	Type	FY14 Revenues (Rs m)	No. of months operational	FY15 Revenues (Rs m)	No. of months operational	H1FY16 Revenues (Rs m)	No. of months operational
Mumbai Entry Point	OMT	3,345	12	3,798	12	2,013	6
Madurai – Kanyakumari	OMT	593	6	1,591	12	805	6
Kini Tasawade	Toll Collection	-	-	1,226	10	782	6
Hyderabad – Bangalore	OMT	1,018	11	1,298	12	677	6
Delhi Entry Point (SMYR)**	Toll Collection	-	-	-	-	534	4.5
Rajiv Gandhi Sea link	OMT	132	2	897	12	548	6
Chennai Bypass	OMT	933	11	1,041	12	482	6
Phalodi Ramji (RIDCOR)	Toll Collection	568	12	677	12	373	6
Vidyasagar Setu	Toll Collection	366	7	647	12	321	6
Kalyan Shilphata*	Toll Collection	-	-	370	12	132	6
IRDP Solapur	Toll Collection	92	12	103	12	63	6
BTPL	BOT	68	12	59	12	32	6
Nagzari	Toll Collection	-	-	38	-	-	-
Total		**7,115**		**11,746**		**6,762**	

*Source: Company, IDFC Securities Research, *the revenue has reduced on account of exemption to cars for which the compensation to the tune of Rs38m has been set off against concession fees to the authority, **Supreme Court allowed SMYR consortium which collects toll at various entry points of Delhi, to exit the contract by 31st January 2016.*

Strong growth opportunities

The tolling market offers sustained growth opportunities due to a revival in the EPC mode of development within the MORTH, NHAI and various state road development corporations. These projects (especially four-laned projects) once completed will need to be tolled and will add to the current opportunity pool for toll operators. Further, there is also an increasing preference for long term/OMT projects amongst various authorities. Projects awarded on long-term basis lend visibility and stability to OMT/tolling business model. Lastly, the government's plans of securitising part of its pool of short-term tolling projects on Toll-Operate-Transfer (TOT) basis for 20-25 years will reduce competition from smaller regional players and provide good growth opportunities for serious long-term players.

❑ Opportunity pool for tolling projects to grow rapidly

Currently, 104 projects are tolled by the NHAI under short-term tolling basis. This opportunity pool is likely to expand as NHAI has ~80 EPC projects (4,723km) under various stages of construction (as on March 2015). Once completed, these projects will come up for tolling over the next 2-3 years. Further, during 9MFY16, NHAI has awarded 36 (1,878km) projects on EPC mode, which too will come up for tolling once completed. In FY17, MORTH is planning to award 15,000km projects, of which 30% will be on PPP mode and balance 70% on EPC basis. As a result, we expect consistent growth in the opportunity pool for tolling projects over the next five years.

Exhibit 6: NHAI project pipeline*

Mode	Km	Cost (Rs bn)
EPC	558	85
BOT (Toll)	785	85
Hybrid Annuity	1,215	139
Total	**2,558**	**309**

*Source: NHAI, IDFC Securities Research,*as on 18 Jan 2016*

Exhibit 7: NHAI awards (Apr-Dec 2015*)

Mode	km	Cost (Rs bn)
BOT	803	98
EPC	1,878	226
Hybrid Annuity	31	19
Total	**2,712**	**343**

*Source: NHAI, IDFC Securities Research, *Provisional data*

❑ Increasing preference for OMT projects

The market for OMT projects is likely to expand due to rising preference amongst government authorities for awarding projects on long term basis. The OMT market is primarily driven by:

- After completion of the defect liability period of 2-3 years for roads constructed on EPC basis, these projects would move from tolling on short term basis to tolling on OMT basis.
- Increasing number of BOT players exiting their operational projects, creating an opportunity to contract these projects on OMT basis.
- Rise in penetration of OMT stretches in state highways, especially in major states such as Karnataka, Bihar and Madhya Pradesh.
    - Karnataka: KRDCL (Karnataka Road Development Corporation Limited) has identified eight OMT projects worth Rs6bn.
    - Bihar: BSRDC (Bihar State Road Development Corporation) has identified OMT contracts to cover 1,800km of state highways, 4,000km of major district roads and 675km of state roads.
    - Madhya Pradesh: MPRDC (Madhya Pradesh Road Development Corporation) has identified 12 projects worth Rs450m.

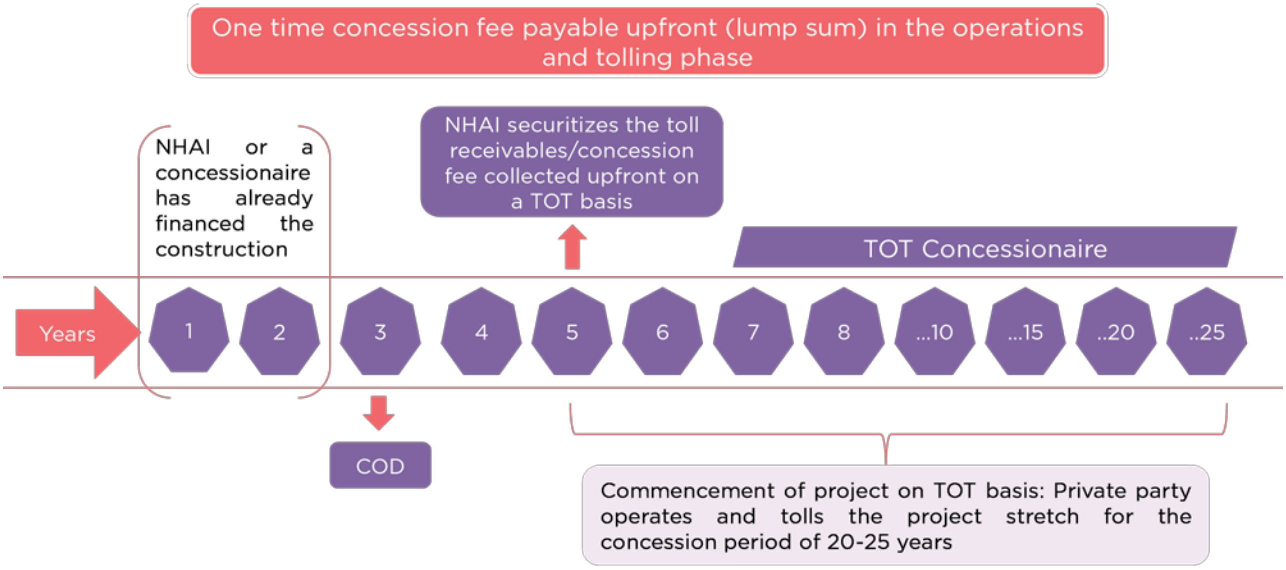
❑ TOT model – Opportunity for long-term players

MORTH has introduced a new operating model of tolling called TOT for efficient monetisation of existing toll roads. Under this model, the authority plans to securitise existing toll roads to private operators for operation and maintenance over a fixed long-term period (20-25 years). The government plans to initially raise ~Rs600bn through this model. The key benefits of TOT model are:

- Improvement in operation and maintenance activities; resulting in its efficient management;
- Efficient control on toll pilferage;
- Support the government in fresh capital inflows which can be reinvested in new road projects;
- This will create an opportunity for a private entity to invest in a low risk asset.

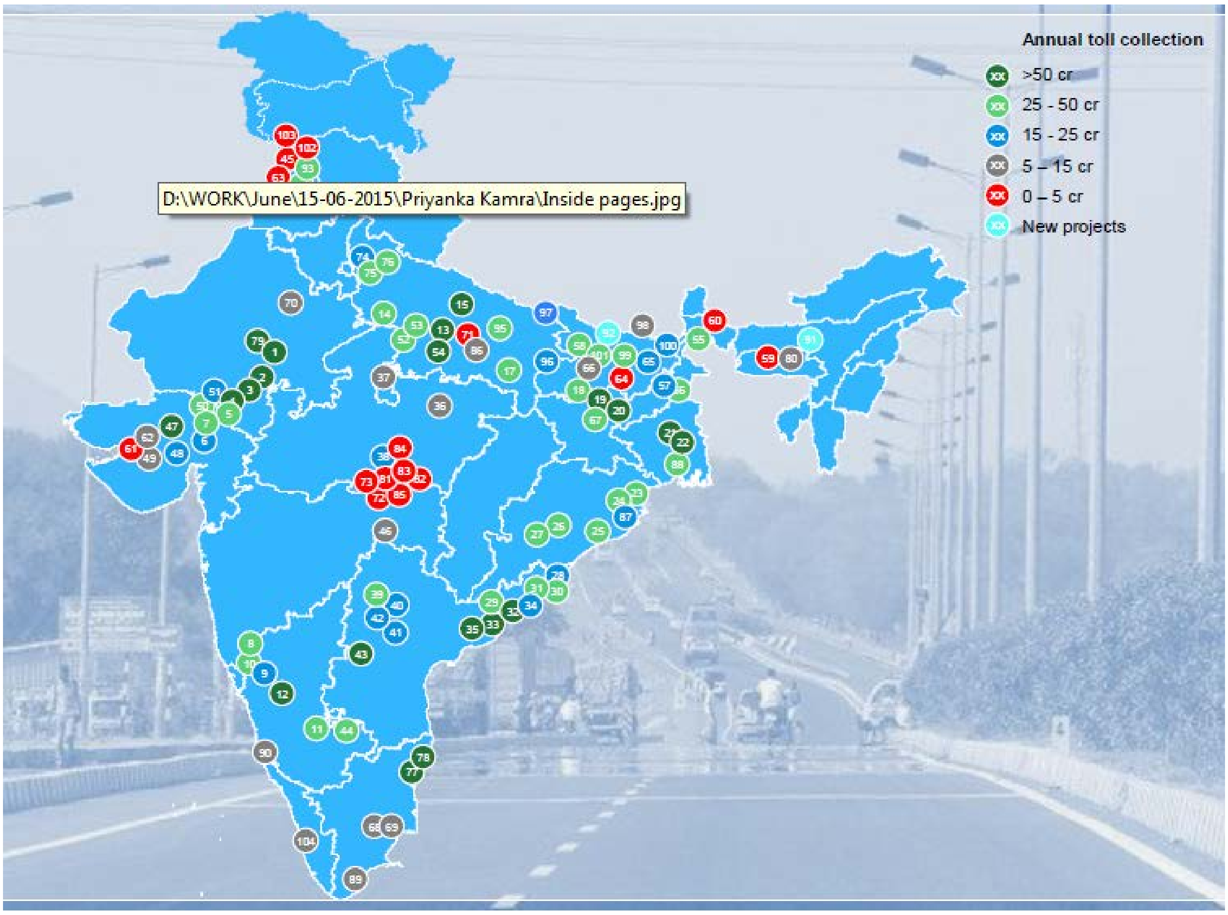
There are 104 road projects across India, which are funded by the government and are currently tolled on short-term basis by private toll operators. As of July 2015, 42% of these projects are generating annual toll revenues that are higher than 10% of their project cost. These projects have higher traffic potential since they are located in key mining and industrial corridors. It is likely that the government will initially securitise only these high potential projects under the TOT model.

Exhibit 8: How the TOT model works



Source: MORTH, IDFC Securities Research

Exhibit 9: Geographical spread of the pool of 104 projects that are currently tolled on short-term basis



Source: Ministry of Road Transport & Highways, IDFC Securities Research

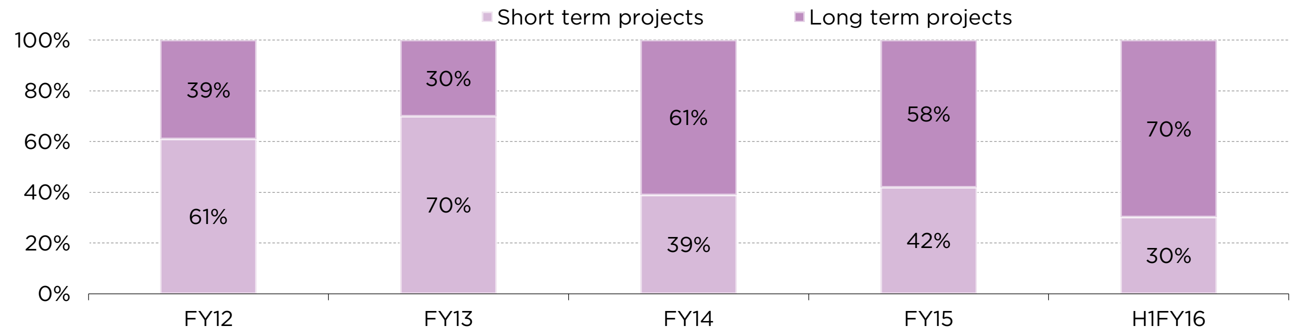
BUSINESS STRATEGY

MEP plans to continue focussing on increasing the share of long term projects in its portfolio. It is also enhancing its in-house maintenance capabilities to minimise dependence on sub-contractors and improve margins. MEP is also increasingly adopting technological solutions such as electronic tolling to improve tolling efficiency. The government plans to monetise part of its operational toll projects portfolio under the TOT model and MEP is exploring strategic tie-ups to participate in this opportunity. MEP is also selectively looking at acquiring operational toll projects as also provide OMT services to projects of third parties.

❑ Increasing its share of long-term projects in the portfolio

MEP has a portfolio of 11 short-term projects, six long-term projects, one BOT project and five OMT projects awarded by various government run authorities. MEP has been focussing on increasing the share of long-term projects, leading to an increase in the share of revenues from such projects to 70% in H1FY16 as against 39% in FY12. Long-term projects provide with steady and predictable revenue stream as compared to short-term projects. They also provide scope for maximising revenues through operational efficiencies and plugging of traffic leakages. While MEP will continue bidding for short-term projects, long-term projects will clearly be the growth driver going forward.

Exhibit 10: Increasing share of revenues from long-term projects



Source: Company, IDFC Securities Research

❑ Developing in-house capabilities in maintenance of road infrastructure

MEP is developing in-house capabilities in maintenance activities for road infrastructure. Such specialised in-house experience in maintenance activities would prove to be advantageous while bidding for and executing OMT contracts. The company has a subsidiary, MEP Highway Solutions Private Limited to focus on maintenance activities for roads, and intends to undertake maintenance activities for the OMT projects through this subsidiary. This would eventually reduce dependence on sub-contractors, thereby avoiding risks and minimising costs associated with sub-contracting which shall lead to margin improvement.

❑ Enhancing usage of technology to improve operational efficiency and boost revenues

MEP is exploring options to reduce dependence on manpower in tolling operations, specially through use of technologies at toll booths such as RFID (at certain toll booths), video/image capturing equipment, automatic vehicle identification based on in-road/infrared sensors and weigh-in-motion technology where weight-based toll collection is mandated. For instance, the company has implemented the RFID based electronic toll collection (ETC) system at the toll plaza for the RGSL project in Mumbai and at four toll plazas forming part of the Mumbai Entry Points project. Further, NHAI has recently promoted Indian Highways Management Company Limited (IHMCL), which proposes to establish nationwide RFID based ETC system together with central clearing house services, under which all toll plazas in India those are under NHAI's jurisdiction would have dedicated RFID-based ETC lanes, under a centralised toll collection system. Pursuant to this, the company is required to establish RFID-based ETC system at the toll plazas for projects awarded by NHAI. ETC systems reduce cash management, thereby minimising revenue leakage and improving transparency in the amount of toll collected. ETC systems also help in reducing the clearing time for vehicles at the toll stations, thereby improving operational efficiency. The company is planning to expand the usage of information technology to toll plazas that are currently being operated manually to improve operational efficiency and ensure better transparency in the process of toll collection.

❑ Foray into TOT model

MORTH has introduced a new operating model of tolling called TOT for efficient monetisation of existing toll roads. Under this model, the authority plans to securitise existing toll roads to private operators for efficient operation and maintenance over a fixed long-term period (20-25 years). NHAI, currently, has a portfolio of 104 such projects, which are being tolled on short-term basis. Of this pool, ~40% of the projects generate toll revenues in excess of 10% of the project cost and hence, are likely to be attractive for private operators. NHAI now plans to award these viable projects on TOT. MEP is targeting to bid for these TOT projects and may enter into a strategic JV for the same.

❑ Acquire operational roads constructed by third parties

MEP intends to acquire, on an opportunistic basis, the OMT and/or toll collection rights from third parties for the roads constructed by them, which are fully operationalised with well-established traffic. The company intends to acquire such maintenance and/or toll collection rights either individually or jointly with other parties, subject to availability of projects on terms that are favourable. Through such acquisitions, the company intends to become a concessionaire without undertaking construction of such projects. In addition, MEP has recently incorporated a subsidiary, MEP Tormato Private Limited, to provide specialised OMT services for projects of third parties.

FINANCIAL OVERVIEW

MEP has witnessed strong 22.5% revenue CAGR over FY12-15, led by robust revenue growth from long-term tolling/OMT projects. The share of revenues from long-term projects has increased from 39% in FY12 to 70% in H1FY16. EBITDA margins have remained in the range of 25-30% over the past 3-4 years and have improved in the last six months due to an improved revenue mix. MEP's consolidated debt stood at Rs30.9bn as on September 2015, comprising Rs24.5bn debt in its MIPL project. While MEP had incurred net losses over FY12-15, it reported a PAT of Rs110m in H1FY16 due to improved revenue mix and change in accounting treatment for premium paid to authority in the Chennai bypass project.

❑ Revenue CAGR at 22.5% through FY12-15

MEP's consolidated revenue went up from Rs10.8bn in FY12 to Rs19.8bn in FY15, a CAGR of 22.5%. The main reason for this growth was higher revenue contribution from long-term tolling/OMT projects. Share of revenues from long-term projects has gone up from 39% in FY12 to 58% in FY15 and further improved to 70% in H1FY16. The company has a proven track record of successfully converting a few of its short-term projects into long-term projects, resulting in consistent revenue growth. Revenue growth was aided by increase in traffic and toll rates in its projects, especially Mumbai Entry Point (MIPL).

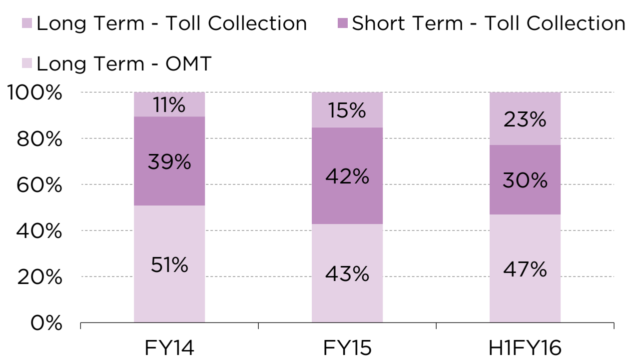
❑ EBITDA CAGR of 10.9% through FY12-15

MEP's consolidated EBITDA increased from Rs3.5bn in FY12 to Rs4.8bn in FY15, a CAGR of 10.9%, led by addition of new projects and increase in traffic/toll rates in existing projects. EBITDA margins have remained in the range of 25-30% over the last 3-4 years. In FY14/15, MEP's margins were impacted due to lower-than-expected toll collection in the Chennai bypass project as also a few of its short-term tolling projects. In short-term projects, operators typically commit to share a fixed amount with the awarding authority and any shortfall in toll collections vis-à-vis estimates directly impacts margins.

❑ Consolidated debt of Rs30.9bn; attributable largely to MIPL upfront payment

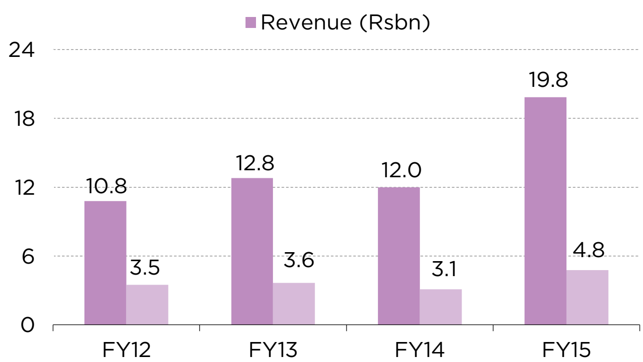
MEP had a debt of Rs33.4bn as on March 2015, which came down to Rs30.9bn as on September 2015. The reduction in debt was mainly due to use of net proceeds of Rs3bn from the IPO money to pay off the debt of Rs2.6bn in the books of its subsidiary, MIPL (Mumbai Entry Point SPV). Of the total debt, MIPL has debt of ~Rs24.5bn taken largely to fund the upfront payment of Rs21bn to MSRDC. Apart from this, the company is also required to provide certain guarantees to the awarding authorities for its projects. For short term tolling contracts, MEP has to provide a funded guarantee equivalent to one month's toll collection and a non-funded bank guarantee of one month's toll collection. In case of OMT projects, MEP has to maintain a bank guarantee equivalent to three months' payment to the authorities. Due to reduction in debt levels in H1FY16, interest costs have reduced from Rs4bn in FY15 to Rs1.9bn in H1FY16 (implying ~Rs200m reduction in annualised interest costs).

Exhibit 11: Increase in revenues from long-term projects



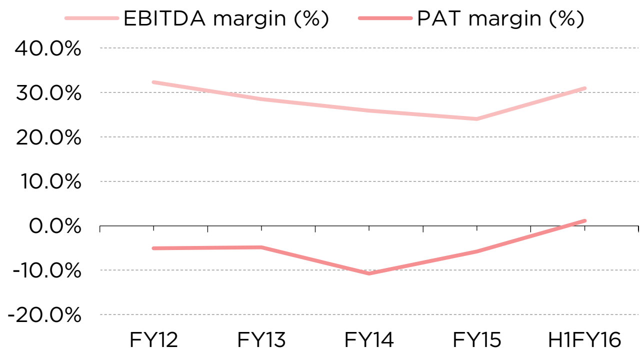
Source: Company, IDFC Securities Research

Exhibit 12: Significant jump in revenue/EBITDA in FY15



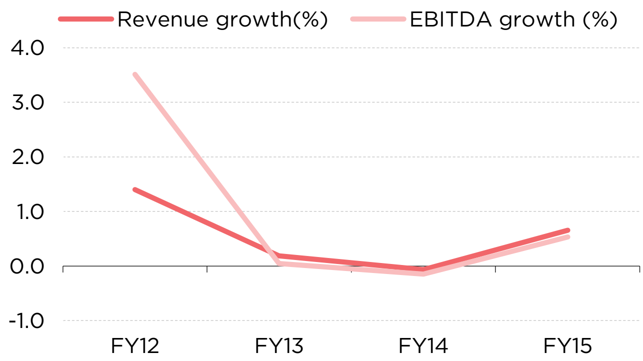
Source: Company, IDFC Securities Research

Exhibit 13: Changing revenue mix; rise in margins



Source: Company, IDFC Securities Research

Exhibit 14: FY12-15 revenue/EBITDA CAGR at 22%/11%



Source: Company, IDFC Securities Research

❑ Improved PAT led by traffic/toll growth and premium deferments in Chennai bypass

MEP had incurred net loss over FY12-15, largely due to higher interest costs in MIPL and revenue shortfall in the Chennai bypass project. In case of the Chennai bypass project, the 3CGM committee of NHAI has accepted MEP's stand of loss of revenues due to NHAI event of default. As a result, starting November 2014, MEP is recognising in the P&L only the actual cash amounts of premium being paid to NHAI (the difference between premium due and actually paid is recognised as deferred payments). Due to this, the project is no longer reporting losses. Also, increase in toll collections in MIPL and repayment of Rs2.6bn debt from IPO proceeds have improved profitability/reduced interest costs. As a result, MEP reported a PAT of Rs110m in H1FY16 as against a net loss of Rs1.2bn in FY15.

Explanation of accounting treatment of Chennai bypass project

In the Chennai bypass project, toll collections are significantly below the annual premium payments committed to NHAI, leading to significant losses. The revenues were falling short of projections due to traffic diversion to alternate routes in the absence of state support agreement. Till October 2014, the company was recognising the actual premium liability to be paid to NHAI in the P&L. This led to huge accounting losses in the previous periods. In cash terms, the company was not paying premium to NHAI to the extent of its estimated loss of revenues due to traffic diversion. The difference between the premium recognized in P&L and the cash premium actually paid was being carried as premium payable in the balance sheet.

From November 2014, the company is recognizing in the P&L only the actual cash amounts of premium being paid to NHAI as the 3CGM committee of NHAI has accepted its stand of loss of revenues due to NHAI event of default. The premium not recognized in P&L in H1FY16 was Rs609m and during November 2014-March 2015 was Rs385m. To that extent there has been a positive impact in its reported profits.

MEP has lodged its claims with the NHAI and the independent engineer (IE) appointed by the NHAI is in the process of quantifying these claims. The NHAI and MEP have agreed to resolve this issue amicably, wherein if the claim amount as quantified by the IE is more than the outstanding premium payable by MEP to NHAI, MEP will forego the difference. Once this issue is settled, the concession is likely to be terminated.

Exhibit 15: Consolidated Balance Sheet

In Rsm	Sept-15	Mar-15
Share Capital	1,626	1,115
Reserves & Surplus	(727)	(3,379)
Total Shareholder's Funds	899	(2,264)
Long-term Borrowings	27,478	29,568
Other Long-term Liabilities	1,044	1,044
Long-term Provisions	27	23
Short-term Borrowings	1,960	2,072
Trade Payables	2,850	2,663
Other Current Liabilities	2,502	3,247
Short-term Provisions	5	5
Total Equity & Liabilities	**36,765**	**36,358**
Fixed Assets	20,964	21,723
Non-Current Investments	216	216
Deferred Tax Assets (net)	1,069	942
Long-term Loans & Advances	9,781	8,934
Other Non-Current Assets	412	387
Current Investments	-	106
Trade Receivables	215	258
Cash & Bank Balance	1,392	1,348
Short-term Loans & Advances	1,962	1,812
Other Current Assets	754	632
Total Assets	**36,765**	**36,358**

Source: Company, IDFC Securities Research

Exhibit 16: Consolidated Income Statement

In Rsm	H1FY16	FY15
Revenue	**9,682**	**20,088**
Operating and Maintaining Expenses	6,344	14,570
Employee Expenses	350	716
Other Expenses	179	366
Total operating expenses	**6,873**	**15,652**
EBITDA	**2,809**	**4,436**
EBITDA Margin (%)	29.0	22.1
Other Income	189	325
Depreciation	865	1,799
Finance Costs	1,914	4,036
PBT	219	(1,075)
Taxes	109	79
PAT before Minority Interest	110	(1,153)
Minority Interest	-	-
PAT	**110**	**(1,153)**
PAT Margin (%)	1.1	(5.7)

Source: Company, IDFC Securities Research

KEY CONCERNS

❑ Concentration risk – Bulk of revenues and value derived from a single asset

MEP derives a substantial portion of its revenue from the Mumbai Entry Points project. Termination of, or reduction in revenues from this project could materially affect business, results of operation and financial condition.

❑ Risk of shortfall in traffic projections

If the traffic volume is less than forecasted, revenues from such toll collection or OMT project may be lower than expected and may lead to losses or lower-than-estimated profits on such contract. The authority payments are usually fixed amounts and hence, any shortfall in toll collections will directly dent MEP's profitability.

❑ Local opposition and political risks

MEP's projects may face local opposition or politically supported protests against collection of tolls, which may have an adverse impact on business, cash flows and results of operations. Effective June 2015, the Maharashtra government exempted cars/SUVs from paying tolls on 53 toll plazas and also shut down 12 toll plazas. Three of MEP's toll plazas have been included in the list of 53, wherein cars/SUVs have been exempted. The impact of these exemptions on MEP is ~Rs120-Rs140m of annual toll revenues, ~2.5% of its total revenues. Apart from this, the government has also set up a committee to evaluate if exemptions can be given for Mumbai Entry Point. The committee, which was set up to give its recommendations on future tolling options at the five entry points of Mumbai (MIPL), has submitted its final recommendations to the government and its decision on the same is awaited. The government will compensate the project operators for the resulting loss of revenues out of its budgetary provisions. However, there is a risk that the compensation amount may be inadequate.

❑ Loans given to promoter group company – Recovery is a key monitorable

MIPL (SPV of MEP), which operates Mumbai Entry Point, had given a loan of Rs3.75bn to Ideal Toll and Infrastructure Private Limited (ITIPL), a promoter-group company. ITIPL, in turn, has used this to fund its equity investment of Rs6.4bn in the 2x270MW Ideal Energy Power Plant, owned by the promoters. The promoters had signed an agreement to sell this plant to Tata Power but the deal has recently been called off as certain conditions precedents could not be fulfilled. The key reason for deal cancellation appears to be a reduction in the off-take approved by the MERC (Maharashtra Electricity Regulatory Commission) from this plant by Tata Power for the Mumbai Distribution circle. As against the originally envisaged off-take of 270MW at Rs4.06/unit, MERC approved only 170MW at Rs3.9/unit. We believe this would have led to difficulties in securing the approval of the lenders for completing the deal. The promoter company, ITIPL has an agreement with MIPL to repay this loan (balance amount Rs3.6bn) with interest over 10 years (ballooning repayments). Recovery of this loan is a key monitorable.

❑ Investment recovery in Baramati project contingent on receipt of termination payment

Under the Baramati project, MEP undertakes maintenance and toll collection for Ring Road and bridges in Baramati on BOT basis. MEP has also constructed a 4-lane Sakhali bridge on Karha river as part of this project. The concession period is 19 years and 4 months starting 25 October 2010 and ending on 24 February 2030. As part of the project terms, MEP has the right to develop 21 acres of land on mixed use basis for 93 years. However, MSRDC, the awarding authority, has not yet handed over this land to MEP, due to which MEP has issued a notice to terminate the concession agreement. This termination has not yet been accepted by MSRDC and MEP continues to operate the project. The total capital invested in this project is ~Rs750m which includes an upfront payment of Rs650m to MSRDC. The outstanding debt on this project is Rs540m. The termination payment under the concession terms is 150% of equity invested and takeover of outstanding debt. The acceptance of the termination and payment of compensation are key to MEP recovering its investments in the project.

Income statement

Year to 31 Mar (Rs m)	FY11	FY12	FY13	FY14	FY15
Net sales	4,494	10,801	12,800	11,979	19,843
% growth	36.9	140.4	18.5	(6.4)	65.6
Operating expenses	3,720	7,311	9,151	8,874	15,652
EBITDA	774	3,490	3,650	3,105	4,191
% change	1,314.6	351.0	4.6	(14.9)	34.9
Other income	142	565	220	433	570
Net interest	(1,299)	(3,766)	(3,765)	(3,797)	(4,036)
Depreciation	387	947	990	1,303	1,799
Pre-tax profit	(769)	(658)	(885)	(1,519)	(1,075)
Deferred tax	(40)	(245)	(63)	(264)	(186)
Current tax	86	119	107	28	265
Profit after tax	(815)	(531)	(929)	(1,283)	(1,153)
Preference dividend	0	0	0	0	0
Minorities	53	54	0	(9)	0
Adjusted net profit	(762)	(477)	(929)	(1,292)	(1,153)
Non-recurring items	0	0	0	0	0
Reported net profit	(762)	(477)	(929)	(1,292)	(1,153)
% change	NM	NM	NM	NM	NM

Balance sheet

As on 31 Mar (Rs m)	FY11	FY12	FY13	FY14	FY15
Paid-up capital	113	1,453	1,453	1,000	1,115
Preference capital	0	0	0	0	0
Reserves & surplus	98	(379)	(1,308)	(1,878)	(3,379)
Shareholders' equity	264	1,074	145	(870)	(2,265)
Total current liabilities	510	725	1,691	2,427	3,663
Total debt	32,754	31,503	30,890	32,201	33,886
Deferred tax liabilities	99	336	1,620	734	3,065
Other non-current liabilities	7	10	16	1,584	1,072
Total liabilities	33,370	32,575	34,217	36,946	41,686
Total equity & liabilities	33,635	33,649	34,362	36,076	39,422
Net fixed assets	22,543	22,074	21,513	23,695	21,722
Investments	944	28	30	6	323
Cash	608	824	1,539	1,623	1,348
Other current assets	9,400	10,101	9,311	9,263	12,022
Deferred tax assets	140	623	1,969	1,490	4,007
Other non-current assets	0	0	0	0	0
Net working capital	9,497	10,199	9,159	8,459	9,707
Total assets	33,635	33,649	34,362	36,076	39,422

Cash flow

Year to 31 Mar (Rs m)	FY11	FY12	FY13	FY14	FY15
Pre-tax profit	(769)	(658)	(885)	(1,519)	(1,075)
Depreciation	(387)	(947)	(990)	(1,303)	(1,799)
Chg in Working capital	(6,855)	(486)	1,756	784	(1,523)
Total tax paid	(86)	(119)	(107)	(28)	(265)
Interest Received	0	0	0	0	0
Ext ord. Items	0	0	0	0	0
Operating cash flow	(6,022)	3,454	5,524	5,905	2,461
Capital expenditure	(22,913)	(477)	(429)	(3,485)	173
Free cash flow (a+b)	(30,233)	(789)	1,330	(1,378)	(1,402)
Chg in investments	(942)	916	(2)	24	(316)
Debt raised/(repaid)	31,473	(1,252)	(613)	1,311	1,685
Interest Paid	(1,299)	(3,766)	(3,765)	(3,797)	(4,036)
Capital raised/(repaid)	0	1,341	0	(453)	115
Dividend (incl. tax)	0	0	0	0	0
Other items	0	0	0	536	(348)
Net chg in cash	405	216	715	84	(274)

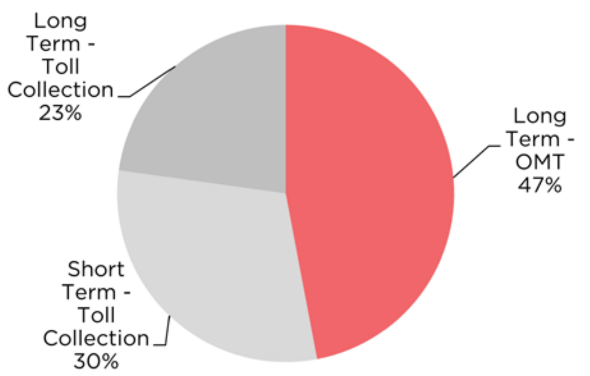
Key ratios

Year to 31 Mar	FY11	FY12	FY13	FY14	FY15
EBITDA margin (%)	17.2	32.3	28.5	25.9	21.1
EBIT margin (%)	8.6	23.5	20.8	15.0	12.1
PAT margin (%)	(17.0)	(4.4)	(7.3)	(10.8)	(5.8)
RoE (%)	(128.8)	(74.3)	(152.4)	NM	NM
RoCE (%)	2.2	7.7	8.1	5.4	6.9
Gearing (x)	121.6	28.6	202.3	NM	NM)
Net debt/ EBITDA (x)	41.5	8.8	8.0	9.8	7.8
FCF yield (%)	(644.6)	(16.8)	28.4	(29.4)	(29.6)
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0

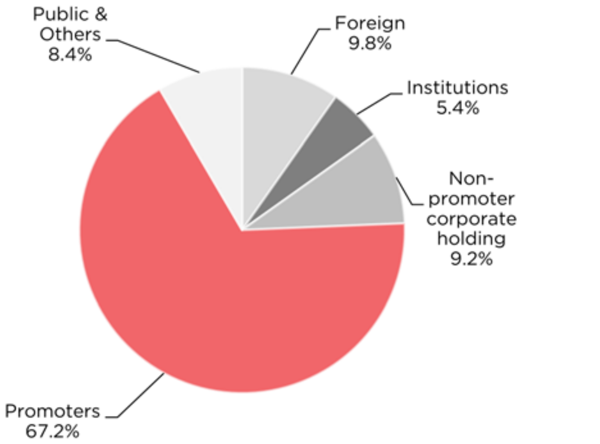
Valuations

Year to 31 Mar	FY11	FY12	FY13	FY14	FY15
Reported EPS (Rs)	(7.0)	(4.4)	(8.5)	(11.8)	(10.4)
Adj. EPS (Rs)	(7.0)	(4.4)	(8.5)	(11.8)	(10.4)
PE (x)	NM	NM	NM	NM	NM
Price/ Book (x)	22.3	4.4	32.3	(5.3)	(2.1)
EV/ Net sales (x)	8.2	3.3	2.7	2.9	1.9
EV/ EBITDA (x)	47.7	10.1	9.3	11.4	8.9
EV/ CE (x)	1.1	1.1	1.0	1.0	1.0

H1FY16 revenue mix



Shareholding pattern



As of Sep 15

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