

# TransContainer

Q3 results

## Record EBITDA margins in Q317

TransContainer announced its third quarter IFRS results on 28 November, revealing continued growth in net income and EBITDA, driven by increased container traffic (y-o-y and q-o-q) and falling empty run ratios. Net income grew by 33% from second quarter levels and was more than double that seen in the same period last year. EBITDA margins increased to record levels of 50.3%. We expect margins to return to more normal levels, but remain strong (c 40%) in the long term aided by continued market growth. The company continues to trade well below global peers on EV metrics and our valuation of RUB5,100/share (derived from a mix of EV/EBITDA and DCF methodologies) indicates around 15% upside in the shares.

Year end	Adjusted revenue (RUBm)	PBT* (RUBm)	EPS* (RUB)	P/E (x)	EV/EBITDA (x)
12/15	20,311	3,530	139	31.4	11.0
12/16	21,988	4,302	202	21.5	10.1
12/17e	26,401	7,859	454	9.6	6.4
12/18e	27,970	7,903	457	9.5	6.1

Note: \*PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

## Strong operational performance in Q317

CAGR growth over the last three years has averaged 7% in rail container transportation with import and domestic routes the main drivers over that period. However, absolute growth over the last 12 months has come from export, import and transit routes indicating growth across the company's markets. Meanwhile, margins have been increased by better performance in empty runs, where Q317 performance fell to 16.7% (from 22.1%).

## Forecasts nudged up again

The company continues to beat our expectations and we upgrade our 2017 forecasts again. We note that record margins in Q317 are unlikely to continue into Q417, as seasonal costs increase while volumes dip in Q118. However, the tight cost control and continued growth in volumes continue to give us confidence in a 40% EBITDA margin in the longer term.

## Valuation: Increases to c RUB5,100/share

We have increased our 2017 and 2018 expectations following the very strong results seen in Q317. This increases our valuation from RUB4,900/share to c RUB5,100/share, based on a mix of EV/EBITDA and DCF methodologies, despite a slight increase in our applied WACC. Based on our 2018 EBITDA expectations, the company continues to trade at a discount to its global peers (6.2x vs peers at 9.0x) given political and market risk.

## Industrial support services

6 December 2017

**Price** RUB4,350

**Market cap** RUB60bn

RUB58.3/US\$

Net debt (RUBm) at 30 September 2017 1,217

Shares in issue 13.8m

Free float 50%

Code TRCN

Primary exchange MICEX

Secondary exchange LSE

## Share price performance



% 1m 3m 12m

Abs (1.6) 28.5 18.5

Rel (local) (3.1) 21.8 21.0

52-week high/low RUB4,750 RUB2,940

## Business description

TransContainer owns and operates rail freight assets across Russia. Its assets comprise rail flatcars, handling terminals and trucks, through which it provides integrated end-to-end freight forwarding services to its customers.

## Next events

Full year results February 2018

## Analyst

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## Results and operational summary

Third quarter results produced the highest EBITDA margin (company definition) in TransContainer's history at over 50%. This was driven by improved operational metrics, with 16% y-o-y growth of rail transportation in TEU (20ft equivalent units) and continued cost control. While adjusted revenues have increased by 30% (Q316-Q317), costs per quarter have increased by only 2%. Part of this is reduced waste (of empty runs), but the company also points to keeping a tight handle on general and administrative costs.

**Exhibit 1: Summary of key financial metrics**

RUBm	Q317	Q217	Q316	Q-o-q	Y-o-y
Net income	2,350	1,770	1,159	33%	103%
<b>Net income margin</b>	<b>31.6%</b>	<b>25.4%</b>	<b>20.2%</b>	<b>6%</b>	<b>11%</b>
Revenue	17,569	16,611	13,357	6%	32%
Adjusted revenue (net of subcontractors charges)	7,442	6,969	5,738	7%	30%
Adjusted EBITDA (company definition)	3,744	3,050	2,106	23%	78%
<b>EBITDA margin</b>	<b>50%</b>	<b>44%</b>	<b>37%</b>	<b>7%</b>	<b>14%</b>
Assets	54,789	54,330	55,415	1%	-1%
Total debt	6,267	7,703	8,938	-19%	-30%
Net debt	1,217	1,292	(310)	-6%	#N/A

Source: TransContainer Note: company EBITDA is defined as profit before income tax + interest expense + depreciation and amortisation.

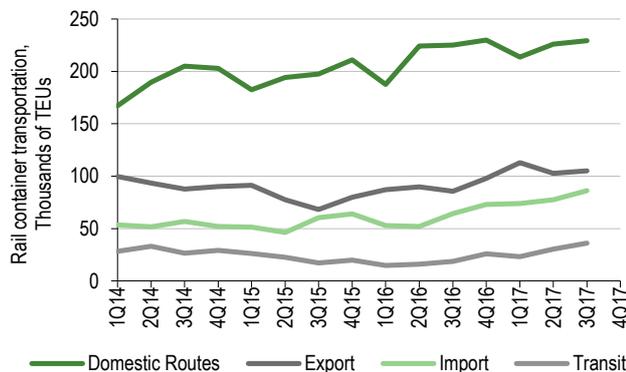
Operational measures improved with 16% growth across the portfolio and strong performance from export, import and transit divisions. Implied cost of empty runs continues to fall.

**Exhibit 2: Rail container performance, TEU000s**

	Q317	Q217	Q316	Relative move		Absolute move (TEU 000s)	
				Q-o-q	Y-o-y	Q-o-q	Y-o-y
Domestic routes	229.3	226	225	1%	2%	3.3	4.3
Export	105.2	102.8	85.7	2%	23%	2.4	19.5
Import	86.2	77.4	64.3	11%	34%	8.8	21.9
Transit	36	30.3	18.7	19%	93%	5.7	17.3
All routes	456.7	436.4	393.8	5%	16%	20.3	62.9

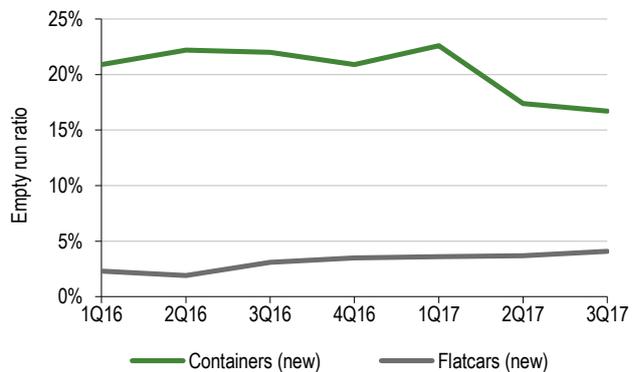
Source: TransContainer

**Exhibit 3: Rail container transportation indicates continuing (if seasonal) growth**



Source: TransContainer

**Exhibit 4: Empty run ratio on containers continues to fall**



Source: TransContainer

## Valuation

We continue to employ a combination of DCF and EV/EBITDA multiples to estimate value for TransContainer. We apply a 7x EV/EBITDA multiple, acknowledging that investors apply a discount

to developed market peers and the investment that the company will be making in the coming years to grow the business. As the company continues to successfully retain EBITDA margins of 40% and above (management's long-term target is 40-50%) and significant investments in 2017/18 bear fruit, we would expect this multiple to strengthen.

In our DCF, we apply a 10% WACC to our five-year forecasts, with a 3% terminal growth rate thereafter. This results in a value estimate of RUB5,107/share, suggesting 14% upside. Again, as the premium demanded for Russia/developing markets fall, we may expect the WACC to fall. We note the CAPM-derived WACC (from Bloomberg) for developed markets is around 8.2% (see peer comparison table below), compared to the 10.6% for TransContainer (we round this down to 10% in our valuation for simplicity).

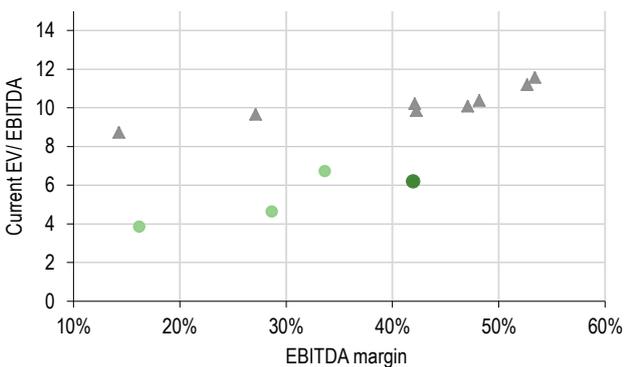
Our fair value estimate (using an average of the two approaches) therefore moves slightly from RUB4,900/share to RUB5,121/share, implying around 16% upside in the shares.

Exhibit 5: EV/EBITDA valuation outline		
2018		RUBm
FY18e EBITDA	2018e	11,734
Multiple		7.0x
EV		82,138
Net debt (FY estimate)	2017e	11,374
Pension liability	2018e	1,097
Equity value		69,667
Number of shares (m)		13.8
<b>Implied equity value per share</b>		<b>5,040</b>
Current share price (RUB)		4,415
Current market cap		61,022
Upside/downside (%)		14%

Source: Edison Investment Research

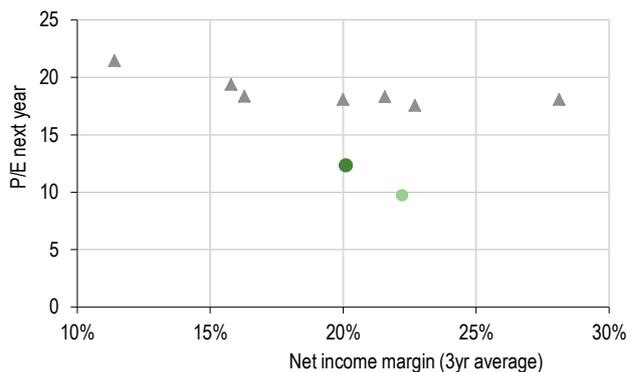
Based on our estimates, the shares continue to trade at a notable discount to TransContainer's global peers (6.2x vs 9.0x based on 2018 metrics). While a discount to developed markets peers can be expected given caution over investing in Russia and developing markets, investors may see the discount as too wide given the steady growth in the market.

**Exhibit 6: TransContainer continues to trade at a discount to developed market peers on EV/EBITDA (x)**



Source: Bloomberg, Edison Investment Research. Note: Dark green dot is TransContainer, light green dots are developing markets peers, grey triangles are developed market peers.

**Exhibit 7: TransContainer continues to trade at a discount to developed market peers on P/E (x)**



Source: Bloomberg, Edison Investment Research. Note: Dark green dot is TransContainer, light green dots are developing markets peers, grey triangles are developed market peers.

**Exhibit 8: Peer comparables table**

		Market Cap (USD m)	Current EV/ EBITDA	Next EV/ EBITDA	Current P/E	Next P/E	WACC
<b>European Transport</b>							
Globaltrans Investment PLC	Cyprus	1,618	4.8x	4.6x	9.5x	9.1x	12.1%
PKP Cargo SA	Poland	722	4.8x	3.8x	49.5x	13.1x	8.9%
VTG AG	Germany	1,521	8.7x	6.7x	26.0x	18.7x	3.6%
Average			6.1x	5.1x	28.3x	13.6x	8.2%
<b>Emerging Markets Transport</b>							
China Railway Tielong Container Logistics	China	2,012	21.4x	20.6x	39.0x	35.2x	13.6%
Daqin Railway Co Ltd	China	20,009	6.3x	6.0x	9.8x	9.7x	11.1%
Guangshen Railway Co Ltd	China	5,113	10.5x	9.5x	34.5x	26.7x	8.6%
Average			12.7x	12.0x	27.8x	23.9x	11.1%
<b>Developed Market Transport</b>							
Canadian Pacific Railway Ltd	Canada	25,399	11.9x	11.2x	19.5x	17.6x	9.9%
Kansas City Southern	United States	11,066	11.2x	10.4x	20.4x	18.1x	6.8%
Union Pacific Corp	United States	93,516	10.8x	10.1x	20.5x	18.3x	7.4%
Norfolk Southern Corp	United States	37,242	10.4x	9.8x	20.1x	18.3x	8.7%
Canadian National Railway Co	Canada	58,342	12.2x	11.6x	19.8x	18.1x	8.8%
Genesee & Wyoming Inc	United States	4,686	10.9x	9.7x	25.9x	21.4x	9.4%
CSX Corp	United States	46,590	11.5x	10.2x	23.6x	19.4x	8.5%
Aurizon Holdings Ltd	Australia	7,937	9.1x	8.7x	19.6x	17.7x	7.1%
Average			11.0x	10.2x	21.2x	18.6x	8.3%
<b>Overall Transport Average</b>			<b>10.3x</b>	<b>9.5x</b>	<b>24.1x</b>	<b>18.7x</b>	<b>8.9%</b>
TransContainer	Russia	1,064	6.4x	6.2x	9.7x	9.8x	10.6%

Source: Bloomberg, Edison Investment Research. Note: The WACC is based on CAPM from Bloomberg. Prices as at 29 November 2017

## Valuation sensitivities

Evaluating the DCF approach, we apply a 10% discount rate, but are aware that others may want to use a different rate. More bullish investors may look for a fall in the discount rate towards the developed markets average of just over 8%, while some may see our 10% value as too low given the debt costs of over 8%.

The effect of a 1% increase in discount rate to 11% would see the valuation fall by 16%, while if we applied a 9% discount rate our value would be 22% higher. Similar movements would follow from a 1% reduction/increase in terminal growth rates.

**Exhibit 9: Effect of WACC and terminal growth rate on DCF valuation**

5,107	8.0%	9.00%	10.00%	11.00%	12.00%
1.0%	5,375	4,501	3,821	3,276	2,830
2.0%	6,386	5,246	4,390	3,723	3,189
3.0%	7,802	6,239	5,121	4,282	3,628
4.0%	9,926	7,629	6,096	5,000	4,177
5.0%	13,466	9,714	7,461	5,957	4,882

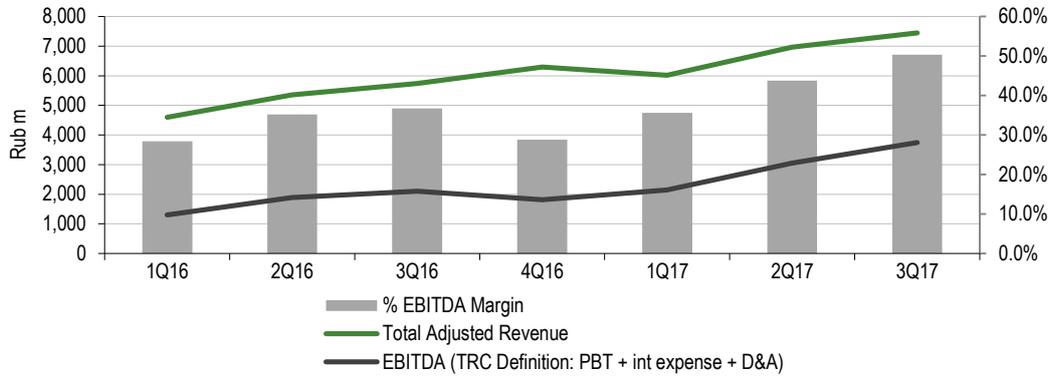
Source: Edison Investment Research

## Financials

The record results seen in Q317 are very encouraging for the company's development, but we do not expect the margins to be sustained into Q417 as higher seasonal costs affect margin capture. Additionally, capex so far this year has been light, but will increase before year end as the company invests in more fixed assets to grow the business – we continue to forecast capex in 2017 of

around RUB8bn, which will increase in 2018. This will require the company to increase its borrowings (currently at very low levels) and tap the bond market in 2017-19.

**Exhibit 10: Revenue, EBITDA and margin progression**



Source: TransContainer

**Exhibit 11: Financial summary**

	RUBm	2014	2015	2016	2017e	2018e	2019e	2020e
31-December		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
<b>PROFIT &amp; LOSS</b>								
Revenue		20,538	20,311	21,988	26,401	27,970	29,696	31,340
EBITDA (company definition)		7,816	6,526	7,099	11,253	11,734	12,391	13,224
EBITDA		1,622	804	1,321	4,806	4,527	3,122	2,991
Operating Profit (before amort. and except.)		4,083	3,274	3,849	7,464	7,576	7,366	7,661
Intangible Amortisation		0	0	0	0	0	0	0
Exceptionals		0	0	0	0	0	0	0
Other		0	0	0	0	0	0	0
Operating Profit		4,083	3,274	3,849	7,464	7,576	7,366	7,661
Net Interest		(497)	(356)	(216)	(287)	(390)	(1,324)	(1,550)
Share of assocs/jvs gains/(losses)		165	612	669	682	716	788	867
Forex gains/(losses)		938	0	(223)	65	0	0	0
Other		18	18	0	41	50	0	0
Profit Before Tax (norm)		3,751	3,530	4,302	7,859	7,903	6,830	6,977
Profit Before Tax (FRS 3)		4,707	3,548	4,079	7,965	7,953	6,830	6,977
Tax		(1,049)	(717)	(835)	(1,581)	(1,591)	(1,366)	(1,395)
Profit After Tax (norm)		2,702	2,813	3,467	6,277	6,312	5,464	5,582
Profit After Tax (FRS 3)		3,658	2,831	3,244	6,383	6,362	5,464	5,582
Average Number of Shares Outstanding (m)		13.7	13.7	13.8	13.8	13.8	13.8	13.8
EPS - normalised (RUB)		286.0	138.7	202.4	454.2	456.7	395.3	403.8
EPS - normalised fully diluted (RUB)		286.0	138.7	202.4	454.2	456.7	395.3	403.8
EPS - (IFRS) (RUB)		267.1	206.7	234.7	461.8	460.3	395.3	403.8
Dividend per share (RUB)		71.0	251.8	394.4	184.7	184.1	158.1	161.5
EBITDA Margin (%)		7.9	4.0	6.0	18.2	16.2	10.5	9.5
Operating Margin (before GW and except.) (%)		19.9	16.1	17.5	28.3	27.1	24.8	24.4
<b>BALANCE SHEET</b>								
Fixed Assets		42,012	41,739	40,822	49,459	61,010	66,767	70,097
Intangible Assets		210	246	290	333	333	333	333
Tangible Assets		37,900	37,827	37,485	45,905	57,456	63,213	66,543
Investments		3,343	3,023	2,685	3,141	3,141	3,141	3,141
Other		559	643	362	80	80	80	80
Current Assets		6,965	7,435	11,006	6,738	7,279	7,653	7,853
Stocks		340	315	209	246	246	246	246
Debtors		1,542	1,392	1,605	2,113	2,113	2,113	2,113
Cash		1,904	2,110	5,525	(107)	434	808	1,008
Other		3,179	3,618	3,667	4,486	4,486	4,486	4,486
Current Liabilities		(5,581)	(6,747)	(8,372)	(8,088)	(8,088)	(8,088)	(8,088)
Creditors		(3,084)	(3,405)	(4,279)	(5,758)	(5,758)	(5,758)	(5,758)
Short term borrowings		(919)	(1,893)	(2,762)	(1,280)	(1,280)	(1,280)	(1,280)
Other		(1,578)	(1,449)	(1,331)	(1,050)	(1,050)	(1,050)	(1,050)
Long Term Liabilities		(8,151)	(6,240)	(8,947)	(12,873)	(21,873)	(25,873)	(26,873)
Long term borrowings		(5,458)	(3,744)	(6,236)	(9,987)	(18,987)	(22,987)	(23,987)
Other long term liabilities		(2,693)	(2,496)	(2,711)	(2,886)	(2,886)	(2,886)	(2,886)
Net Assets		62,709	62,161	69,147	77,158	98,250	108,381	112,910
<b>CASH FLOW</b>								
Operating Cash Flow		7,617	5,437	7,421	9,723	10,675	11,609	12,330
Net Interest		(557)	(394)	(165)	(398)	(390)	(1,324)	(1,550)
Tax		(964)	(727)	(781)	(1,581)	(1,591)	(1,366)	(1,395)
Capex		(4,136)	(2,400)	(2,192)	(8,268)	(12,300)	(10,000)	(8,000)
Acquisitions/disposals		(75)	(12)	(128)	(2,399)	(2,300)	0	0
Financing		199	0	517	14	0	0	0
Dividends		(1,117)	(974)	(4,830)	(5,250)	(2,553)	(2,545)	(2,185)
Other		199	0	517	14	0	0	0
Net Cash Flow		967	930	(158)	(8,159)	(8,459)	(3,626)	(801)
Opening net debt/(cash)		6,004	4,473	3,527	3,473	11,374	19,833	23,459
HP finance leases initiated		0	0	0	0	0	0	0
Other		564	16	212	258	0	0	0
Closing net debt/(cash)		4,473	3,527	3,473	11,374	19,833	23,459	24,260

Source: Edison Investment Research, company accounts Note: For illustrative purposes we assume any capital required for investment purposes in 2017-19 is raised in debt.

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