

BSE SENSEX	S&P CNX
34,844	10,742
Bloomberg	MCX IN
Equity Shares (m)	51
M.Cap.(INRb)/(USDb)	47.5 / 0.7
52-Week Range (INR)	1,258 / 897
1, 6, 12 Rel. Per (%)	-12/-28/-52
Avg Val, INRm	413
Free float (%)	100.0

Financials & Valuations (INR b)

Y/E Mar	2018E	2019E	2020E
Net Sales	2.5	3.0	3.4
EBITDA	0.7	1.1	1.5
PAT	1.1	1.5	1.8
EPS (INR)	20.8	29.4	34.9
Gr. (%)	-16.0	41.1	18.5
BV/Sh (INR)	259.2	274.1	329.2
RoE (%)	7.9	11.0	11.6
RoCE (%)	7.7	10.7	11.2
P/E (x)	44.7	31.6	26.7
P/BV (x)	3.6	3.4	2.8

Estimate change



TP change



Rating change


CMP: INR931 TP: INR1,100(+18%)
Buy

Disappointment led by one-offs and other income...

...but volume triggers well in place

- **Yield-led PAT miss:** MCX's 3QFY18 revenue came in at INR610m, 2% below our estimate of INR621m, led by a slight decline in realization. Operating expenses stood at INR475m, exceeding our estimate of INR453m by 5% due to one-off expense (INR20m) toward events hosted by MCX in 3Q – excluding which operational results were in line. PAT of INR188m (below our estimate of INR283m) was dragged lower, as other income of INR156m missed our estimate by 39% due to MTM losses on fixed income instruments.
- **Base for volumes to normalize in 4Q:** The bullion-led volume decline at MCX commenced in Dec'16 – the month post demonetization. In the subsequent 12 months (Dec'16 to Nov'17), gold/silver volumes declined 47/31% YoY, leading to an overall volume decline of 17% YoY. However, with the quantum of decline reducing dramatically and the sharp uptick seen in base metal volumes (19% YoY), growth can be expected to return in the next quarter.
- **Regulatory action striding well:** Over the past nine months, several regulatory steps have supported a case for volumes uptick on the retail (allowing distribution by bank subsidiaries) and institutional (allowing Category-III AIFs to take commodity exposure) fronts. Approval of the proposal to allow MFs/PMS players in commodity derivatives would further boost participation. With reforms underway, we see scope for significant volumes recovery, from new products and participants.
- **Valuation view:** MCX retained its market leadership with a share of 80-90% over FY09-17, even in the most turbulent of months of FY13-15, when the parent's existence was in deep waters on issues of fraud around NSEL. While universal licenses would open the doors for competition, we believe established liquidity and already existing fungibility of margins should play a larger role in determining the leader board compared to predatory pricing. We expect earnings CAGR of 29% over FY18-20. Our TP of INR1,100 discounts forward earnings by 30x. **Buy.**

Quarterly Performance (Consolidated)

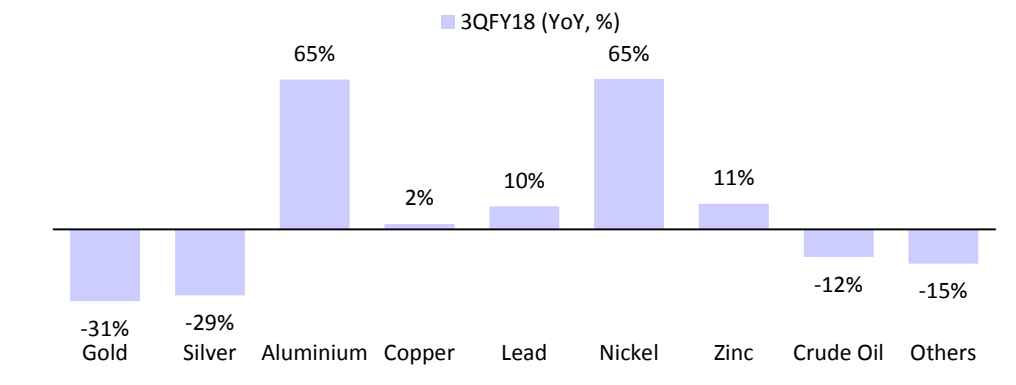
	FY17				FY18				FY17	FY18E	Est.	Var.
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q			3Q	(%/bp)
Sales	676	652	686	626	592	673	610	659	2,641	2,533	621	(1.8)
Q-o-Q Gr. (%)	18.7	7.8	5.1	-8.7	-5.5	13.6	-9.4	8.0	12.4	-4.1	-7.7	-166bp
Staff Costs	143	144	198	160	178	178	169	169	644	693	178	(5.4)
Other expenses	265	257	296	335	282	288	306	278	1,116	1,152	274	11.5
Depreciation	49	42	45	49	48	48	35	40	186	171	48	(27.5)
EBIT	219	209	148	82	84	158	101	171	695	516	120	(16.4)
Margins (%)	32.4	32.1	21.5	13.1	14.2	23.6	16.5	26.0	26.3	20.4	19.4	-289bp
Other Income	308	302	312	243	277	243	156	257	1,164	932	257	(39.4)
PBT bef. Exceptional items	527	511	459	325	361	401	256	428	1,857	1,448	377	(32.1)
Tax	152	134	119	106	98	110	68	107	512	383	94	(27.3)
Rate (%)	28.9	26.3	26.0	32.6	27.2	27.3	26.7	25.0	27.5	26.5	25.0	174bp
PAT	375	376	339	219	263	292	188	321	1,346	1,065	283	(33.6)
Q-o-Q Gr. (%)	30.3	0.5	-9.9	-35.5	20.0	11.0	-35.6	71.1	221.7	-18.7	-3.0	
EPS (INR)	6.5	7.4	6.7	4.3	5.1	5.7	3.7	6.3	26.4	20.9	5.5	(33.6)
Total volumes (INR t)	16.0	16.4	13.9	12.4	12.0	14.1	12.8	13.8	58.7	52.6	12.8	
Q-o-Q Gr. (%)	7.3	2.3	-15.2	-10.3	-3.4	17.0	-8.8	7.3			-8.8	
Y-o-Y Gr. (%)	17.7	10.3	6.4	-16.5	-24.8	-14.0	-7.6	10.5	4.1	-10.2	-7.6	

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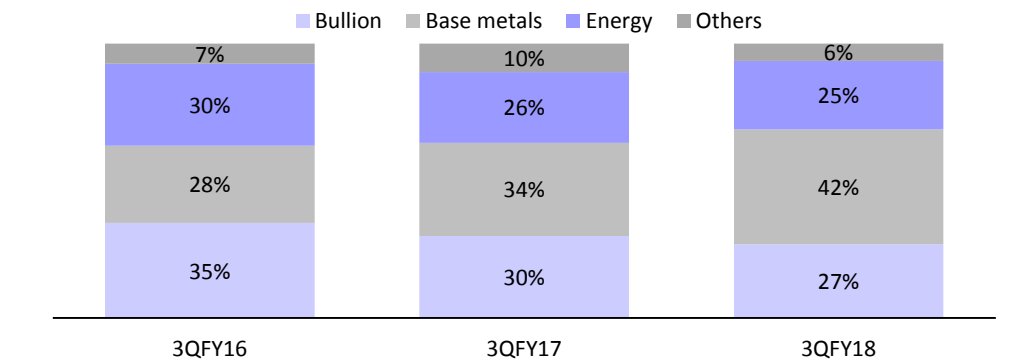
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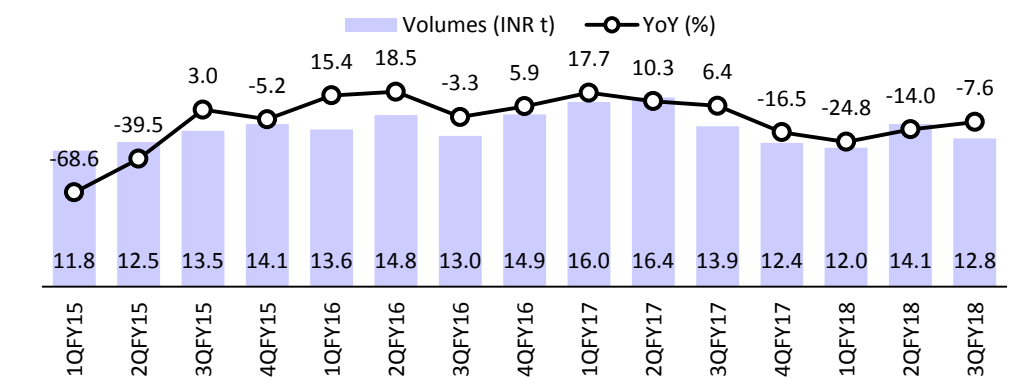
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Exhibit 1: Bullion-led volume pressures partly offset by strength in Base Metals

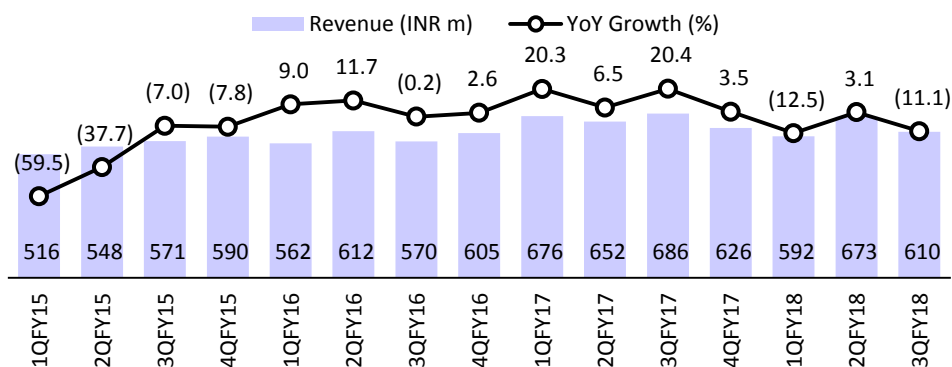
Source: Company, MOSL

Exhibit 2: Bullion composition down to 27% in 3QFY18 (from 35% in 3QFY16) and Base Metals up to 42% (from 28%)

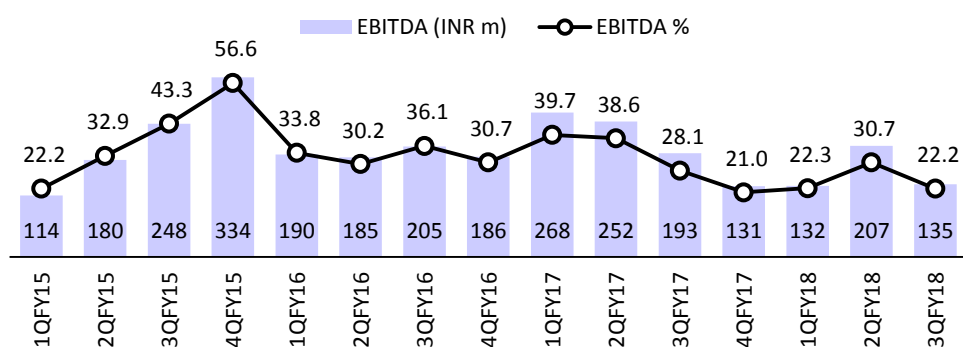
Source: Company, MOSL

Exhibit 3: Overall volume has fallen dramatically over the last four quarters (now in the base)...

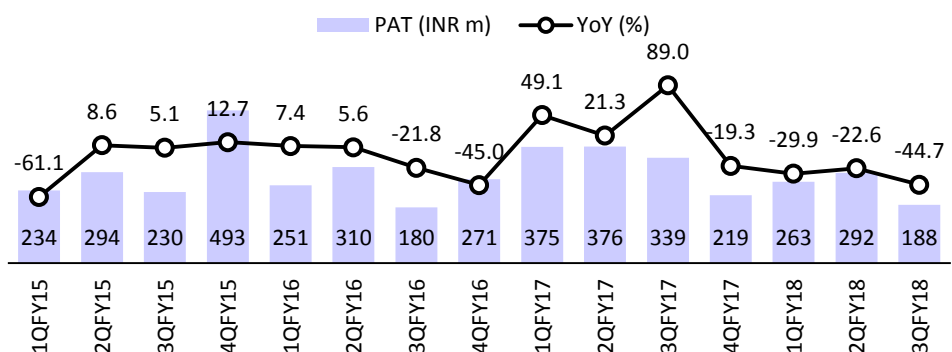
Source: Company, MOSL

Exhibit 4: ...Leading to subdued revenue growth trends

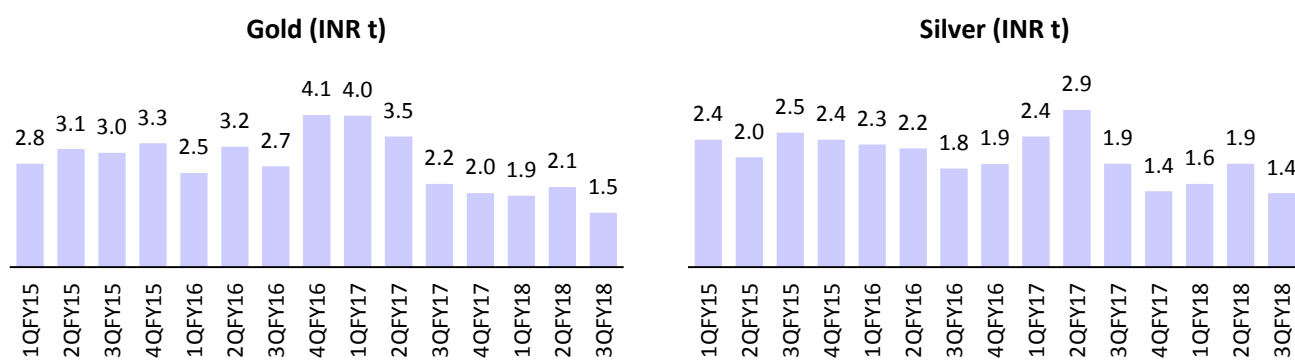
Source: Company, MOSL

Exhibit 5: Stable cost structure over the last couple of quarters (minus 3Q one-offs)

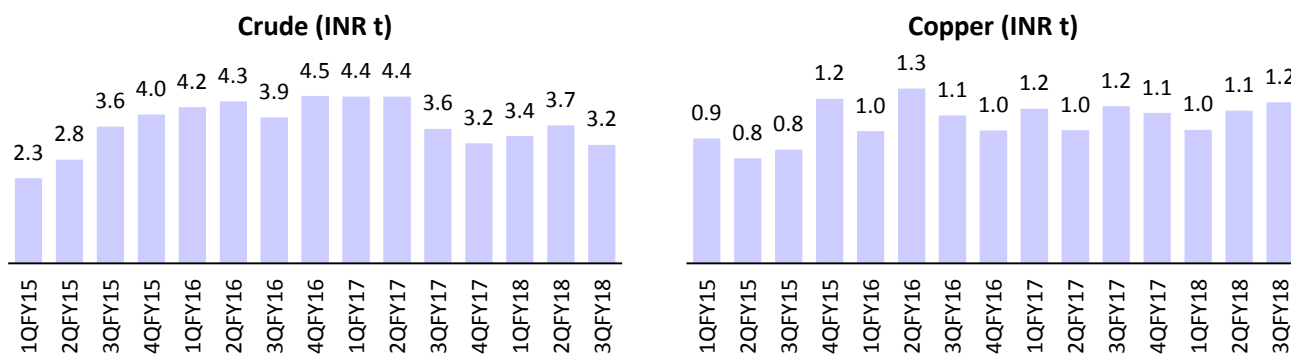
Source: Company, MOSL

Exhibit 6: Lower yield on cash aggravated the one-off expenses

Source: Company, MOSL

Exhibit 7: Bullion volumes were severely impacted by demonetization and GST

Source: Company, MOSL

Exhibit 8: Crude volumes declined by 12% YoY, while Copper volumes grew by 2% YoY

Source: Company, MOSL



Takeaways from Management Commentary

- **Volume pick-up from next quarter:** Volumes have been subdued post demonetization and GST in bullion, but significant upside can be seen in coming quarters based on volumes in January so far, which are up by 10%. Volume barring bullion has anyway been showing strength, as evident from the increase seen in base metals.
- **Further boost expected from increased distribution:** There could be significant volume increase as bank subsidiaries have been approved to become members of MCX. Axis Securities has already come on board, and MCX expects all major bank subsidiaries to come on board in next quarter.
- **Positive on the contribution of Options:** While only one contract is introduced on Options i.e. gold, roughly nine contracts would be traded next year. MCX expects 20-25% of total volume to be added by the full-fledged launch of Options in a span of 2-3 years. It has already given SEBI feedback on the first few expiries and has made applications for the launch of the other four commodities allowed under the guidelines.
- **Launching new futures contracts:** MCX has received approval from SEBI to launch Brass contracts and will look at 5 to 6 more launches in next six months.
- **Impact of universal license:** Now that SEBI has given a go-ahead for exchanges to trade multiple asset classes, competitive dynamics are likely to change. If competition plays predatory on pricing, MCX may be forced to give some discounts. However, volumes might not be affected due to an increase in the size of the overall market.
- **Keen on currencies:** Once exchanges are allowed to trade other asset classes, MCX would be keen on making an entry into currencies. It may also look at other segments, but will take that call only once an announcement comes from SEBI.
- **One-off cost items:** There was an aberration in the quarter's costs because of marketing events. Apart from costs that are linked to volumes, other costs are likely to remain stable to lower in FY18 versus the previous year.

Valuation and view

- **Market leadership in winner-takes-all business:** MCX has retained its market leadership position, with a share of 80-90% over FY09-16. Even in the most turbulent of months during FY13-14, when the parent's existence was in deep waters on issues of fraud around National Spot Exchange (NSE), the exchange managed to retain its share. Additionally, it has remained without a fulltime MD & CEO since May 2014 when Mr Manoj Vaish resigned after just three months. This is a reflection of the winner-takes-all nature of the business model.
- **Monopoly share in multiple commodities takes care of concentration risk:** MCX's golden run in terms of volumes came at the time of significant run-up in gold and silver prices in FY12 and FY13. That was also perceived to be a risk, given that the share of volumes from these two commodities had exceeded 70%. However, presence in multiple commodities helps avert the concentration risk, and this was evidenced in FY15, when action in oil prices drove energy to exceed gold as the largest traded commodity at MCX by value.
- **All eyes on reforms, as SEBI-FMC merger is complete:** SEBI's merger with FMC is now complete, paving the way for much awaited reforms in the ecosystem. The upside for MCX may yet be partly a function of reports around approvals to competition and entry of a credible global exchange materializing. We don't expect these at one-go or immediately, but rather in a gradual, phased manner over the course of the next calendar year. SEBI already has the ball rolling in terms of reform and expects universal licenses to be active through the course of the year. MCX could, in the meanwhile: [1] get a head start, and [2] strengthen itself with investment from CME.
- **Volume reversal to pre-CTT levels is our base case:** Our base case assumes gradual recovery in volumes to INR240b-270b in FY19E and INR280-310b in FY20E, yet lower than pre-commodities transaction tax (CTT) average daily turnover of INR450b-500b. This compares with current ADT of INR200b-225b.
- **Volumes have taken a temporary hit:** Volumes suffered 2HFY17 onwards on account of demonetization's impact on gold volumes. Post this, a failure in pick-up has resulted out of tepid activity in the physical market. This time, it is compounded by uncertainty posed by GST. That said, December 2017 marks one year from the commencement of problems, and the base would hence normalize 4QFY18 onwards. While bullion remains lower than pre-demonetization levels, a good contribution has been made by a rally in base metals. Options are on the verge of being launched, and will result in a further volume boost once they start trading.
- **Multiplier effect on operational earnings from operating leverage, Buy:** From 4QFY18, Options on all commodities will also be launched, a key trigger for volumes. This should kick start the recovery in volumes, that should continue with the entry of new participants such as FIs and new products such as indices. This drives our expectation of healthier revenue growth over FY18-20 (16%) and consequently driving earnings growth (29%). Our price target of INR1,100 discounts forward earnings by 30x, implying 18% upside. **Buy.**

Key triggers

- Pick-up in volume led by the introduction of new products like Options / Indices
- Introduction of new participants like Banks / FIs
- High volatility in key commodities like Bullion / Crude

Key risk – increased competition from equity exchanges

One of the implications of FMC's merger with SEBI is that stock exchanges will be able to become universal exchanges, where equities, debt instruments and currencies are traded under the same roof as commodity derivatives. Stock exchanges already have depositories and clearing corporations that will cater to the needs of commodity traders as well. If NSE enters the commodities segment, MCX could see stiff competition, which may impair both market share and profit margins.

Financials and Valuations

Income Statement						(INR Million)		
Y/E Mar	2013	2014	2015	2016	2017	2018E	2019E	2020E
Net Sales	5,160	3,407	2,225	2,349	2,641	2,533	2,955	3,407
Change (%)	-1.9	-34.0	-34.7	5.6	12.4	-4.1	16.7	15.3
EBITDA	3,276	1,457	876	766	844	685	1,094	1,459
EBITDA Margin (%)	63.5	42.8	39.4	32.6	32.0	27.1	37.0	42.8
Depreciation	307	343	259	246	186	171	163	166
EBIT	2,969	1,114	616	521	658	515	932	1,293
Interest	0	11	14	0	2	0	0	0
Other Income	1,259	993	1,098	977	1,164	932	1,068	1,078
Extraordinary items	0	0	0	-667	0	0	0	0
PBT	4,227	2,097	1,701	831	1,821	1,446	2,000	2,371
Tax	1,065	569	450	413	512	383	500	593
Tax Rate (%)	25.2	27.1	26.5	49.7	28.1	26.5	25.0	25.0
Min. Int. & Assoc. Share	0	0	0	0	0	0	0	0
Reported PAT	3,162	1,528	1,251	418	1,309	1,063	1,500	1,778
Adjusted PAT	3,162	1,528	1,251	418	1,309	1,063	1,500	1,778
Change (%)	10.5	-51.7	-18.1	-66.6	213.0	-18.8	41.1	18.5
Balance Sheet						(INR Million)		
Y/E Mar	2013	2014	2015	2016	2017	2018E	2019E	2020E
Share Capital	510	510	510	510	510	510	510	510
Reserves	11,058	10,931	11,512	11,529	13,078	12,707	13,470	16,277
Net Worth	11,567	11,441	12,022	12,039	13,588	13,217	13,980	16,787
Debt	569	2,169	2,214	2,162	2,125	2,183	2,183	2,125
SGF	0	1,720	1,871	1,879	1,705	1,731	1,731	1,705
Total Capital Employed	12,136	13,610	14,236	14,201	15,713	15,400	16,163	18,912
Net Fixed Assets	2,044	1,735	1,553	1,430	1,633	1,768	1,866	1,766
Capital WIP	0	0	0	0	0	0	0	0
Investments	10,682	10,898	12,927	10,741	11,948	13,296	13,296	11,972
Current Assets	5,131	4,782	3,764	5,997	5,077	4,033	4,314	9,128
Debtors	69	90	107	42	28	72	86	114
Cash & Bank	3,475	3,417	2,655	5,003	3,890	2,795	2,893	7,133
Loans & Adv, Others	1,587	1,275	1,002	952	1,159	1,166	1,335	1,881
Curr Liabs & Provns	5,721	3,805	4,007	3,967	2,945	3,698	3,313	3,954
Net Current Assets	-590	977	-243	2,030	2,132	336	1,000	5,174
Total Assets	12,136	13,610	14,236	14,201	15,713	15,400	16,163	18,912

Financials and Valuations

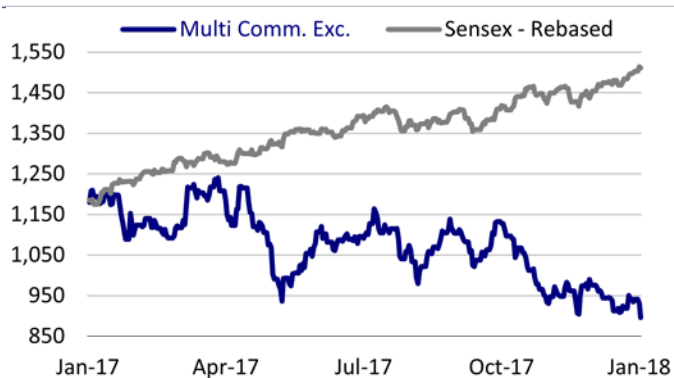
Ratios								
Y/E Mar	2013	2014	2015	2016	2017	2018E	2019E	2020E
Basic (INR)								
EPS	58.6	30.0	24.6	23.4	24.8	20.8	29.4	34.9
Cash EPS	68.0	36.9	29.6	13.0	29.3	24.2	32.6	38.1
Book Value	226.8	225.4	235.8	236.1	266.4	259.2	274.1	329.2
DPS	0.5	10.2	10.2	0.0	15.3	20.4	20.4	20.4
Payout (incl. Div. Tax.)	0.9	39.0	48.5	0.0	70.7	116.0	82.2	69.4
Valuation(x)								
P/E				39.8	37.5	44.7	31.6	26.7
Cash P/E				71.5	31.8	38.5	28.5	24.4
Price / Book Value				3.9	3.5	3.6	3.4	2.8
EV/Sales				14.6	13.8	14.3	12.2	10.6
EV/EBITDA				44.6	43.1	52.7	32.9	24.7
Dividend Yield (%)				0.0	1.9	2.6	2.6	2.6
Profitability Ratios (%)								
RoE	29.4	13.3	10.7	3.5	10.2	7.9	11.0	11.6
RoCE	28.1	12.8	10.4	8.8	10.0	7.7	10.7	11.2
RoIC	0	0	0	0	0	0	0	0
Turnover Ratios (%)								
Fixed Asset Turnover (x)	28.2	19.3	12.5	12.9	14.3	13.4	15.3	16.1
Debtors (No. of Days)	5	10	17	7	4	10	11	10
Leverage Ratios (%)								
Net Debt/Equity (x)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Cash Flow Statement								
	(INR Million)							
Y/E Mar	2013	2014	2015	2016	2017	2018E	2019E	2020E
Adjusted EBITDA	3,276	1,457	876	766	844	685	1,094	1,459
Non cash opr. exp (inc)	-25	876	0	0	0	0	0	0
(Inc)/Dec in Wkg. Cap.	-1,941	-1,565	503	22	-1,251	759	-567	-775
Tax Paid	-782	-384	-259	-62	-197	-120	-221	-313
Other operating activities	0	0	0	0	0	0	0	0
CF from Op. Activity	529	385	1,120	727	-604	1,325	307	371
(Inc)/Dec in FA & CWIP	-462	-59	-9	-200	-345	-237	-261	-287
Free cash flows	68	325	1,111	527	-950	1,088	46	84
(Pur)/Sale of Invt	1,910	586	-1,214	5,174	1,810	-656	790	799
Others	0	0	0	0	0	0	0	0
CF from Inv. Activity	1,448	527	-1,222	4,974	1,464	-894	529	512
Inc/(Dec) in Net Worth	0	0	0	0	0	0	0	0
Inc / (Dec) in Debt	0	0	0	0	0	0	0	0
Interest Paid	0	0	0	-14	0	-2	0	0
Divd Paid (incl Tax) & Others	-2,134	-1,133	0	0	-925	-522	-737	-874
CF from Fin. Activity	-2,134	-1,133	0	-14	-925	-524	-737	-874
Inc/(Dec) in Cash	-156	-221	-103	5,687	-65	-93	98	9
Add: Opening Balance	3,124	3,475	3,417	2,655	5,003	3,890	2,795	2,893
Closing Balance	2,968	3,254	3,315	8,342	4,937	3,797	2,893	2,902

Corporate profile

Company description

MCX, India's largest and only listed exchange, commenced operations on 10 November 2003. It is an electronic commodity futures exchange, with a scalable technology framework and disaster recovery site (DRS) for end-to-end functioning of systems and network. MCX had 84% market share in terms of the value of commodities traded in the futures market in FY15. MCX has a pan India presence, with over 2,000 members, and operations through 486,700+ terminals, across 1,879 cities and towns.

Exhibit 1: Sensex rebased



Source: MOSL/Bloomberg

Exhibit 2: Shareholding pattern (%)

	Dec-17	Sep-17	Dec-16
Promoter	0.0	0.0	0.0
DII	35.5	33.6	37.5
FII	29.0	30.9	24.0
Others	35.5	35.5	38.5

Note: FII Includes depository receipts

Source: Capitaline

Exhibit 3: Top holders

Holder Name	% Holding
KOTAK MAHINDRA BANK LIMITED	15.0
JHUNJHUNWALA RAKESH RADHESHYAM	3.9
AXIS MUTUAL FUND (HOLDING UNDER VARIOUS SCHEMES)	3.0
RELIANCE MUTUAL FUND (HOLDING UNDER VARIOUS SCHEMES)	2.4
IDFC PREMIER EQUITY FUND	2.0

Source: Capitaline

Exhibit 4: Top management

Name	Designation
Saurabh Chandra	Chairman
Mrugank Paranjape	Managing Director & CEO
Ashwin Patel	Company Secretary
Parveen Kumar Singhal	President & Whole-time Dir.

Source: Capitaline

Exhibit 5: Directors

Name	Name
Arun Bhargava	Prithvi Haldea
Ajay Kumar	Amit Goela
Chengalath Jayaram	Hemang Raja
M A K Prabhu	Madhu Jayakumar
Padma Raghunathan	Arun Nanda
Govinda Rao Marapalli	PRAVIN TRIPATHI
S K Mitra	

*Independent

Exhibit 6: Auditors

Name	Type
Rathi & Associates	Secretarial Audit
Shah Gupta & Co	Statutory

Source: Capitaline

Exhibit 7: MOSL forecast v/s consensus

EPS (INR)	MOSL forecast	Consensus forecast	Variation (%)
FY18	20.8	26.3	-21.0
FY19	29.4	40.2	-26.8
FY20	34.9	49.0	-28.8

Source: Bloomberg

Disclosures:

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Pending Regulatory Enquiries against Motilal Oswal Securities Limited by SEBI:

SEBI pursuant to a complaint from client Shri C.R. Mohanraj alleging unauthorized trading, issued a letter dated 29th April 2014 to MOSL notifying appointment of an Adjudicating Officer as per SEBI regulations to hold inquiry and adjudge violation of SEBI Regulations; MOSL requested SEBI to provide all documents, records, investigation report relied upon by SEBI which were referred in Show Cause Notice. The matter is currently pending.

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