

POWER GRID CORP OF INDIA

Earnings looking up

India Equity Research | Power



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Power Grid Corporation of India's (PGCIL) Q2FY13 Adj. PAT came in at INR9.5bn against our estimate of INR9.2bn largely due to lower employee costs and better returns from the ancillary business. Given the H1 capex/commissioning run-rate of INR70bn, FY13 capex target of INR200bn and current investment approvals for INR880bn of projects, we believe commissioning is key for both earnings growth and avoiding an equity dilution in FY14/FY15. Maintain 'BUY' with TP of INR122/share.

PAT beats estimates; execution momentum maintained

Adjusting for INR1.05bn of FERV gain, INR140mn of prior period sales and INR800mn of higher dividend income, PAT at INR9.5bn was higher than our estimate of INR9.2bn. PGCIL commissioned INR26.6bn worth projects in Q2FY13 (H1 INR67.6bn) and incurred a capex of INR41.7bn (H1 INR71.8bn). Management continues to guide for a full year capex target of INR200bn and hopes to commission INR160bn. Given that Q2 is a slow quarter due to monsoons and also that H2 is strong on execution (~60% of full year execution with Q4 especially being substantial), we do not expect slippage beyond 5% - 7% to our FY13 commissioning estimate of INR170bn.

Confident of achieving INR1tn capex in XIIth Plan

The company has chalked out a capex of INR1tn for the XIIth Plan and is confident of funding it with 28%-30% equity. Apart from the robust commissioning, we believe a combination of short term funding, recovery of deferred tax and surplus of depreciation (over debt repayment obligation) would be for internal accruals. It has received investment approvals for contracts worth INR880bn, of which, INR730bn has already been awarded. While regulated tariff based projects are approved by CERC, there are multiple payment security levels for IPP projects due to which the management is confident that internal accruals would be enough to fund the equity portion of capex.

Outlook and valuations: Earnings looking up; maintain 'BUY'

Given the yearly capex run-rate of INR200bn and current investment approvals for INR880bn, the pace of commissioning needs to pick up for both earnings uptick and avoiding equity dilution. At CMP of INR 120/share, the stock is trading at P/BV of 2.1x FY13E and 1.9x FY14E. Maintain 'BUY/SO' with SOTP based TP of INR122/share.

EDELWEISS 4D RATINGS

Absolute Rating	BUY
Rating Relative to Sector	Outperformer
Risk Rating Relative to Sector	Low
Sector Relative to Market	Equalweight

MARKET DATA (R: PGRD.BO, B: PWGR IN)

CMP	: INR 120
Target Price	: INR 122
52-week range (INR)	: 125 / 94
Share in issue (mn)	: 4,629.7
M cap (INR bn/USD mn)	: 554/ 10,178
Avg. Daily Vol.BSE/NSE('000)	: 3,407.5

SHARE HOLDING PATTERN (%)

	Current	Q1FY13	Q4FY12
Promoters*	69.4	69.4	69.4
MF's, FI's & BK's	7.5	7.8	8.0
FII's	13.8	13.1	12.9
Others	9.3	9.7	9.6
* Promoters pledged shares (% of share in issue)	:		NIL

PRICE PERFORMANCE (%)

	Stock	Nifty	EW Power Index
1 month	1.2	(0.4)	3.7
3 months	(0.7)	8.4	2.8
12 months	15.2	8.3	(7.6)

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Financials (Standalone)

(INR mn)

Year to March	Q2FY13	Q2FY12	% Change	Q1FY13	% Change	FY12	FY13E	FY14E
Revenues	30,858	22,644	36.3	28,883	6.8	100,353	123,555	147,056
EBITDA	26,693	18,978	40.6	24,646	8.3	83,824	104,157	124,200
Adj. net profit	9,459	7,355	28.6	8,701	8.7	30,638	36,513	42,575
Diluted EPS (INR)						6.6	7.9	9.2
P/BV						2.4	2.1	1.9
ROAE (%)						14.5	14.7	15.5

Table 1: SOTP valuations

	Value	Comments	Multiple	Comments	Value	Per share
Regulated equity	239,082	FY14 req equity	1.88	(RoE-g)/(CoE-g)	448,278.8	96.8
CWIP	65,459	PV of FY14E CWIP	1.00	Equity value	65,458.9	14.1
Cash and investments	10,983	FY13E Cash + Invst	1.00	At book value	10,982.5	2.4
Value of telecom business	8,000	Current equity	2.00	2x P/BV	16,000.0	3.5
Value of consultancy business	1,928	FY13E earnings	12.0	12x P/E	23,137.3	5.0
Total					563,857	122

Source: Edelweiss research

Financial snapshot

(INR mn)

Year to March	Q2FY13	Q2FY12	% Change	Q1FY13	% Change	FY12	FY13E	FY14E
Total operating income	30,858	22,644	36.3	28,883	6.8	100,353	123,555	147,056
Transmission expense	1,998	1,743	14.6	2,000	(0.1)	8,100	10,125	12,656
Gross profit	28,860	20,900	38.1	26,883	7.4	92,254	113,430	134,400
Salaries,wages, other payments	2,168	1,922	12.8	2,237	(3.1)	8,430	9,273	10,200
Total expenditure	4,165	3,665	13.6	4,236	(1.7)	16,530	19,397	22,856
EBITDA	26,693	18,978	40.6	24,646	8.3	83,824	104,157	124,200
Other income	1,570	1,942	(19.2)	920	70.6	7,497	5,582	4,867
PBDIT	28,262	20,920	35.1	25,567	10.5	91,321	109,739	129,067
Depreciation	8,252	5,966	38.3	7,565	9.1	25,725	36,163	42,913
Interest	6,343	5,556	14.2	6,461	(1.8)	19,433	27,935	32,935
Profit before tax	14,715	9,398	56.6	11,540	27.5	46,163	45,642	53,219
Tax	3,597	2,331	54.3	2,836	26.8	13,427	9,128	10,644
Core profit	11,259	7,087	58.9	8,701	29.4	32,550	36,513	42,575
Prev yr sales/write back	(112)	(350)	NA			(967)		
Forex (gains)/loss	(1,048)	638	NA	-		840	-	-
Prior period items	-	(21)	(100.0)	-		10	-	-
Tax adjustments						(1,794)		
Net profit	9,459	7,355	28.6	8,701	8.7	30,638	36,513	42,575
No. of shares (mn)	4,630	4,630		4,630		4,630	4,630	4,630
Diluted EPS (INR)	2.0	1.6	28.6	1.9	8.7	6.6	7.9	9.2

As % of net revenues

COGS	6.5	7.7		6.9		8.1	8.2	8.6
Gross profit	93.5	92.3		93.1		91.9	91.8	91.4
Other expenses	7.0	8.5		7.7		8.4	7.5	6.9
Total expenses	13.5	16.2		14.7		16.5	15.7	15.5
EBITDA	86.5	83.8		85.3		83.5	84.3	84.5
Adjusted net profit	30.7	32.5		30.1		30.5	29.6	29.0
Tax rate	24.4	24.8		24.6		29.1	20.0	20.0

Change in estimates

	FY13E			FY14E			Comments
	New	Old	% change	New	Old	% change	
Net revenue	123,555	126,886	(2.6)	147,056	152,415	(3.5)	
EBITDA	104,157	107,489	(3.1)	124,200	129,559	(4.1)	
EBITDA margin	84.3	84.7		84.5	85.0		
Core profit	36,513	36,766	(0.7)	42,575	45,789	(7.0)	Revising commissioning for FY13 and lowering other income in FY14
PAT margin	29.6	29.0		29.0	30.0		
Capex	160,000	160,000	0.0	160,000	160,000	0.0	

Company Description

PGCIL commenced operations in 1992 by consolidating transmission assets of NTPC, NHPC, NEEPC, NPCIL, Tehri Hydro Development Corporation, and Neyveli Lignite. In 1994, the assets and communication systems of regional load dispatch centre (RLDC) were also transferred to the company with an objective to enhance grid management. Due to the central transmission utility status, PGCIL is mandated to undertake and operate inter-state transmission systems efficiently, provide for open access, and undertake various functions of RLDC. Recently, under the Rajiv Gandhi Grameen Vidyutikaran Yojana, PGCIL is mandated to implement the electrification of rural households in association with the Rural Electrification Corporation, SEBs, and the respective state governments.

Investment Theme

Growth visibility: The company has met its Eleventh Five Year capex Plan of INR 550 bn for its various transmission projects. Of these close to 60% are for strengthening the overall grid capacity and the balance 40% is generation linked. The 12th Plan target for capex is touted to be INR 1 tn. Hence, there is a certain visibility on the capex program and in turn earnings growth. The company has been consistently delivering 20-25% profit growth every quarter driven by its capex.

Reversal in the current trend of capex and telecom earnings: If the company is able to scale up internal accruals through superior earnings from telecom which would in turn invested in power business then the overall earnings growth could be significant.

Key Risks

Telecom scale up: The company's strategy of leveraging its transmission towers also as telecom towers has not scaled up so far.

Funding issues: PGCIL is constrained by its limited retained earnings in undertaking significant capex programme under the 70:30 debt/equity norm. While the company could raise the threshold to 75% debt and 25% equity to meet its XII Plan target but earnings will continue to be on the actual equity deployed.

Slow pace of capex – dependant on generation capacity growth: Power Grid capex is dependant heavily (40-50% of total capex) on the capacity addition of its associated generation projects. Any delay in these generation assets will cascade to a delay in PGCIL's project execution slowing its pace of growth. Escalation in project costs, delay in commissioning of generation projects, and long gestation periods could impact profitability, if delays are not compensated through tariffs.

Financial Statements

Key Assumptions

Year to March		FY10	FY11	FY12	FY13E	FY14E
Macro -	GDP(Y-o-Y %)	8.4	8.4	6.5	5.8	6.5
	Inflation (Avg)	3.6	9.9	8.8	7.8	6.0
	Repo rate (exit rate)	5.0	6.8	8.5	7.5	6.8
	USD/INR (Avg)	47.4	45.6	47.9	53.5	52.0
Company -	Capex (INR mn)	106,170	120,770	178,140	160,000	160,000
	Commissioning (INR mn)	31,534	73,130	138,300	170,000	170,000
	Closing Regulated Equity (INR)	115,000	136,939	165,982	199,982	234,482
	RoE on Regulated Equity (%)	15	17	17	17	17

Income statement

Year to March		FY10	FY11	FY12	FY13E	FY14E
(INR mn)						
Income from operations		71,275	83,887	100,353	123,555	147,056
Direct costs		5,074	5,857	8,100	10,125	12,656
Employee costs		7,267	7,459	8,430	9,273	10,200
Total operating expenses		12,341	13,315	16,530	19,397	22,856
EBITDA		58,933	70,572	83,824	104,157	124,200
Depreciation & Amortization		19,797	21,994	25,725	36,163	42,913
EBIT		39,136	48,578	58,098	67,994	81,287
Other income		3,759	6,709	7,497	5,582	4,867
Interest expenses		15,432	17,339	19,433	27,935	32,935
Income from Provisions written back		963	(359)	187	-	-
Expenditure from provisions		(237)	(58)	-	-	-
Profit before tax		26,263	38,247	45,976	45,642	53,219
Provision for tax		5,854	11,278	13,427	9,128	10,644
Net profit		20,409	26,969	32,550	36,513	42,575
Extraordinary income/ (loss)		725	(2,303)	(1,911)	-	-
Profit After Tax		21,135	24,666	30,638	36,513	42,575
Diluted EPS (INR)		5.0	5.3	6.6	7.9	9.2
Dividend per share (INR)		1.5	1.5	2.1	2.0	2.4
Dividend payout (%)		36.1	30.0	34.5	30.0	30.0

Common size metrics - as % of net revenues

Year to March	FY10	FY11	FY12	FY13E	FY14E
Operating expenses	17.3	15.9	16.5	15.7	15.5
EBITDA margins	82.7	84.1	83.5	84.3	84.5
Net profit margins	28.6	32.1	32.4	29.6	29.0

Growth ratios (%)

Year to March	FY10	FY11	FY12	FY13E	FY14E
Rev. growth (%)	8.3	17.7	19.6	23.1	19.0
EBITDA	7.6	19.7	18.8	24.3	19.2
Net profit	20.7	32.1	20.7	12.2	16.6
EPS growth (%)	23.3	6.1	24.2	19.2	16.6

Balance sheet					
(INR mn)					
As on 31st March	FY10	FY11	FY12	FY13E	FY14E
Equity capital	42,088	46,297	46,297	46,297	46,297
Reserves & surplus	117,331	167,373	188,581	214,140	243,942
Shareholders funds	159,419	213,670	234,878	260,437	290,240
Secured loans	313,458	363,251	491,192	593,192	691,192
Unsecured loans	30,710	45,577	16,500	16,500	16,500
Borrowings	344,168	408,828	507,692	609,692	707,692
Deferred revenue	-	23,474	22,831	22,831	22,831
Others	31,160	11,467	16,009	16,009	16,009
Sources of funds	534,747	657,439	781,410	908,969	1,036,772
Gross block	434,727	503,518	633,626	803,626	953,626
Depreciation	114,114	131,278	157,003	193,167	236,080
Net block	320,613	372,240	476,623	610,460	717,547
Capital work in progress	204,222	266,246	281,835	271,835	281,835
Total fixed assets	524,835	638,486	758,458	882,295	999,382
Investments	14,532	13,651	12,845	10,983	9,121
Inventories	3,449	3,815	4,403	6,093	7,252
Sundry debtors	22,149	31,621	23,154	28,507	33,929
Cash and equivalents	32,776	36,801	23,369	21,295	14,213
Loans and advances	37,935	32,935	99,932	104,429	108,983
Total current assets	96,309	105,171	150,858	160,323	164,377
Sundry creditors and others	76,346	71,138	105,892	106,287	93,928
Provisions	24,584	28,755	34,859	38,345	42,179
Total current liabilities & provisions	100,930	99,893	140,751	144,632	136,108
Net current assets	(4,621)	5,279	10,107	15,691	28,269
Others	-	24	-	-	-
Uses of funds	534,747	657,439	781,410	908,969	1,036,772
Book value per share (INR)	37.9	46.1	50.7	56.3	62.7

Free cash flow					
(INR mn)					
Year to March	FY10	FY11	FY12	FY13E	FY14E
Net profit	21,135	24,666	30,638	36,513	42,575
Depreciation	19,797	21,994	25,725	36,163	42,913
Others	(3,233)	(503)	7,333	-	-
Gross cash flow	37,699	46,157	63,697	72,676	85,488
Less: Changes in WC	(13,106)	5,875	18,260	7,659	19,660
Operating cash flow	50,805	40,282	45,437	65,018	65,828
Less: Capex	102,896	130,815	145,698	160,000	160,000
Free cash flow	(52,091)	(90,533)	(100,261)	(94,982)	(94,172)

Cash flow metrics					
Year to March	FY10	FY11	FY12	FY13E	FY14E
Operating cash flow	50,805	40,282	45,437	65,018	65,828
Investing cash flow	(96,609)	(133,310)	(158,343)	(158,138)	(158,138)
Financing cash flow	38,906	94,968	95,936	91,046	85,228
Net cash flow	(6,898)	1,940	(16,971)	(2,074)	(7,082)
Capex	(102,896)	(130,815)	(145,698)	(160,000)	(160,000)
Dividends paid	(6,313)	(6,925)	(9,769)	(9,362)	(10,917)

Profitability & efficiency ratios

Year to March	FY10	FY11	FY12	FY13E	FY14E
ROAE (%)	13.4	14.5	14.5	14.7	15.5
ROACE (%)	8.1	8.3	8.2	8.2	8.4
Debtors days	92	117	100	76	77
Current ratio	1.0	1.1	1.1	1.1	1.2
Debt/EBITDA	5.8	5.8	6.1	5.9	5.7
Fixed asset turnover (x)	0.2	0.2	0.2	0.2	0.2
Average working capital turnover	(30.8)	255.0	13.0	9.6	6.7
Average capital employed turnover (x)	0.1	0.1	0.1	0.1	0.2
Debt/Equity	2.2	1.9	2.2	2.3	2.4
Adjusted debt/equity	2.3	1.9	2.2	2.3	2.4

Operating ratios

Year to March	FY10	FY11	FY12	FY13E	FY14E
Total asset turnover	0.1	0.1	0.1	0.1	0.2
Fixed asset turnover	0.2	0.2	0.2	0.2	0.2
Equity turnover	0.5	0.4	0.4	0.5	0.5

Valuation parameters

Year to March	FY10	FY11	FY12	FY13E	FY14E
Diluted EPS (INR)	5.0	5.3	6.6	7.9	9.2
Y-o-Y growth (%)	23.3	6.1	24.2	19.2	16.6
CEPS (INR)	9.6	10.6	12.6	15.7	18.5
Diluted PE (x)	23.8	22.5	18.1	15.2	13.0
Price/BV (x)	3.2	2.6	2.4	2.1	1.9
EV/Sales (x)	11.2	10.9	10.2	9.2	8.4
EV/EBITDA (x)	13.6	12.9	12.2	10.9	10.0
Dividend yield (%)	1.3	1.3	1.8	1.7	2.0

Peer comparison valuation

	Price	Market cap (INR mn)	P/BV(x)		EV/EBITDA(x)		RoE (%)	
			2013E	2014E	2013E	2014E	2013E	2014E
CESC	280	34,988	0.7	0.6	5.0	4.8	8.9	8.5
NTPC	169	1,390,598	1.8	1.7	10.9	9.6	11.9	12.6
Tata Power Co	106	252,614	1.9	1.7	8.7	6.4	8.7	13.3
Average			1.6	1.5	8.9	7.7	11.1	12.5
Power Grid Corp of India	120	553,947	2.1	1.9	10.9	10.0	14.7	15.5

Source: Edelweiss research

Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
Adani Enterprises	BUY	SP	M	Adani Ports and Special Economic Zone	BUY	SO	M
Adani Power	REDUCE	SU	M	CESC	HOLD	SU	H
Essar Ports	BUY	None	None	GMR Infrastructure	BUY	SO	H
Gujarat Pipavav Port	REDUCE	None	None	GVK Power and Infra	HOLD	SU	H
JSW Energy	HOLD	SP	H	Lanco Infratech	BUY	SU	H
Marg	BUY	None	None	Navabharat Ventures	BUY	None	None
NTPC	HOLD	SU	L	Power Grid Corp of India	BUY	SO	L
PTC India	BUY	None	None	Reliance Infrastructure	BUY	SO	M
Tata Power Co	BUY	SO	L				

ABSOLUTE RATING

Ratings	Expected absolute returns over 12 months
Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

RELATIVE RETURNS RATING

Ratings	Criteria
Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
	Stock return < 1.25 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

RELATIVE RISK RATING

Ratings	Criteria
Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

SECTOR RATING

Ratings	Criteria
Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
	Sector return < 1.25 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return



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Coverage group(s) of stocks by primary analyst(s):

Adani Power, Adani Enterprises, Adani Ports and Special Economic Zone, CESC, Essar Ports, GMR Infrastructure, Gujarat Pipavav Port, GVK Power and Infra, JSW Energy, Lanco Infratech, Marg, Navabharat Ventures, NTPC, PTC India, Power Grid Corp of India, Reliance Infrastructure, Tata Power Co

Recent Research

Date	Company	Title	Price (INR)	Recos
02-Nov-12	JSW Energy	Operationally sound, but open to market vagaries; <i>Result Update</i>	63	Hold
31-Oct-12	Gujarat Pipavav Port	Negative surprise continues; <i>Result Update</i>	48	Reduce
26-Oct-12	NTPC	Nothing to cheer; <i>Result Update</i>	169	Hold

Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	113	53	19	186
* 1 stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	114	58	14	

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

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