

## Power Finance Corporation

### Power-packed quarter

Power Finance Corporation's (PFC) Q3FY10 results were largely in line with our estimates. NII increased by 33% YoY to Rs 7.5bn driven by a 20% growth in loan book and a 42bps YoY improvement in net interest margin. Reported PAT swelled 66% YoY to Rs 5.6bn due to notional MTM profits of Rs 290mn (versus a Rs 580mn loss in Q3FY09) on unhedged foreign currency borrowings and a lower effective tax rate (26% as against ~32% in Q3FY09). Adjusting for these two items, net profit increased 33% YoY.

**Strong recovery in disbursements:** After two quarters of muted growth, loan disbursements witnessed a strong uptick in Q3FY10. Total disbursements grew by 52% YoY to Rs 65bn. In 9MFY10, disbursements increased 9% YoY to Rs 154bn. With the revival in growth, the management is confident of achieving its guidance of Rs 230bn in disbursements for FY10. The company currently has an outstanding sanctions book of Rs 1.25trillion which provides high visibility to loan growth for the next few years. We are currently factoring in loan growth of 19% (CAGR) over FY09-FY12.

**Slowdown in sanctions to state utilities:** Loan sanctions were muted at Rs 42bn in Q3FY10 (as against an average of Rs 154bn in the last six quarters), as PFC held back loans of Rs 110bn to state power utilities (SPU). The RBI recently raised concerns over the company's exposure norms to SPUs, leading to a voluntary slowdown of sanctions by the management. Being a government-owned NBFC, RBI exposure norms are not applicable to PFC; hence the management is confident of securing the central bank's permission to maintain its current exposure levels.

**NIMs largely stable:** Reported yield on assets declined by 21bps QoQ to 11.1% as the company gradually reduced its lending rates by 50bps over the last six months. However, the cost of funds also declined by 26bps QoQ to 8.6% and consequently, NIMs remained largely stable at 4.2%. With a hardening of interest rates, we expect NIMs to decline by ~10bps in FY11.

**Maintain Hold:** We like PFC due to its superior domain expertise and robust business outlook driven by strong demand in the power sector. For 9MFY10, the company has reported a sharp 54% YoY increase in PAT (excluding extraordinary) on strong loan growth, expansion in margins, and a lower tax rate. While we expect business growth to remain strong, momentum in PAT may slow down to 16-18% in FY11 and FY12 due to a marginal drop in NIMs and a stable tax rate in these two years (vis-à-vis FY10). At current valuations of 1.8x FY11E BV and 1.6x FY12E BV, the stock is trading at a significant premium to PSU banks. We maintain a Hold on PFC with a target price of Rs 270 (2.1x FY11E ABV).

#### Financial highlights

(Rs mn)	FY09	FY10E	FY11E	FY12E
NII	22,140	28,547	33,445	39,192
Growth (%)	25.2	28.9	17.2	17.2
PPP	22,466	29,691	34,852	40,793
Growth (%)	25.4	32.2	17.4	17.0
FDEPS (Rs)	17.2	19.6	22.4	26.2
Growth (%)	63.2	14.4	14.0	17.1

#### Profitability and return ratios

(%)	FY09	FY10E	FY11E	FY12E
Net interest margin	3.8	4.0	3.9	3.9
Non-int inc/Total inc	5.3	6.5	6.7	6.5
Cost/Inc ratio	4.0	3.1	3.1	3.0
RONW	18.9	18.3	18.2	18.6
ROA	3.4	3.2	3.0	3.0
Net NPA	0.0	0.0	0.0	0.0

#### What's New? Target Rating Estimates

CMP	TARGET	RATING	RISK
Rs 242	Rs 270	HOLD	LOW

BSE	NSE	BLOOMBERG
532810	PFC	POWF IN

#### Company data

Market cap (Rs bn / US\$ mn)	276.9 / 5,955
Outstanding equity shares (mn)	1,148
Free float (%)	10.2
Dividend yield (%)	1.7
52-week high/low (Rs)	285 / 125
3-month average daily volume	866,368

#### Stock performance

Returns (%)	CMP	1-mth	3-mth	6-mth
PFC	242	(4.8)	9.1	5.1
Sensex	16,358	(6.3)	2.9	4.4

#### Valuation matrix

(x)	FY09	FY10E	FY11E	FY12E
P/BV @ CMP	2.4	2.1	1.8	1.6
P/BV @ Target	2.7	2.4	2.1	1.8
P/E @ CMP	14.1	12.3	10.8	9.2





## Result highlights

Fig 1 - Actual vs estimated performance

(Rs mn)	Actual	Estimate	% Variance
NII	7,470	7,215	3.5
PPP	7,350	7,095	3.6
PAT	5,640	5,447	3.5
FDEPS (Rs)	4.9	4.7	3.5

Source: Company, RHH

Fig 2 - Quarterly performance

(Rs mn)	Q3FY10	Q3FY09	% Chg YoY	Q2FY10	% Chg QoQ
Interest income	19,850	16,810	18.1	19,350	2.6
Interest expenses	12,380	11,200	10.5	12,150	1.9
Net interest income	7,470	5,610	33.2	7,200	3.8
Other income	130	110	18.2	810	(84.0)
Total income	7,600	5,720	32.9	8,010	(5.1)
Operating costs	250	230	8.8	240	4.2
PPOP	7,350	5,490	33.9	7,770	(5.4)
Provisions	10	(90)		1	
PBT	7,340	5,580	31.5	7,769	(5.5)
Tax	1,912	1,800	6.2	1,299	47.2
PAT	5,428	3,781	43.6	6,470	(16.1)
Extraordinary income (net of tax)	212	(382)		(96)	
Reported PAT	5,640	3,399	65.9	6,374	(11.5)
EPS (incl extraordinary) (Rs)	4.9	3.0	65.9	5.6	(11.5)
EPS (excl extraordinary) (Rs)	4.7	3.3	43.6	5.6	(16.1)
Tax rate (%)	26.0	32.2		16.7	
Cost/income (%)	3.3	4.0		3.0	
NIMs (%)	4.2	3.8		4.2	
Loan book (Rs bn)	724	604	19.9	687	5.5
Disbursements (Rs bn)	65	43	51.8	45	43.7
Sanctions (Rs bn)	42	138	(69.3)	162	(73.7)
Gross NPA (Rs mn)	130	130		130	
Net NPA (Rs mn)	60	60		60	

Source: Company, RHH

Results largely in line with our estimates

NII up 33% YoY on 20% growth in loan book and 42bps margin expansion

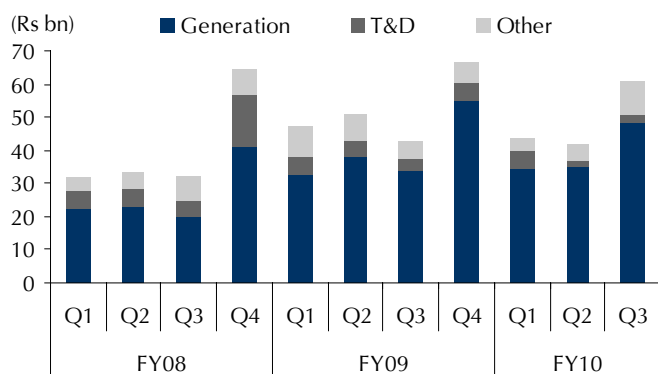
Reported MTM profit of Rs 212mn (net of tax) on unhedged external borrowings

NIMs remained largely stable QoQ

Disbursals strong during the quarter after muted growth in H1FY10

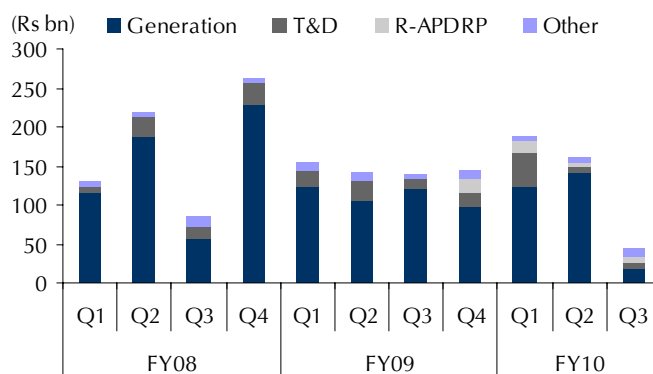


**Fig 3 - Disburseals picked up in Q3FY10**



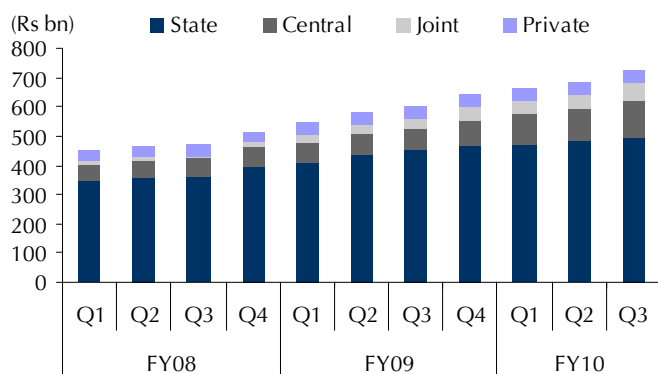
Source: RHH, Company

**Fig 4 - Sanctions dropped due to delay in loan release to SPUs**



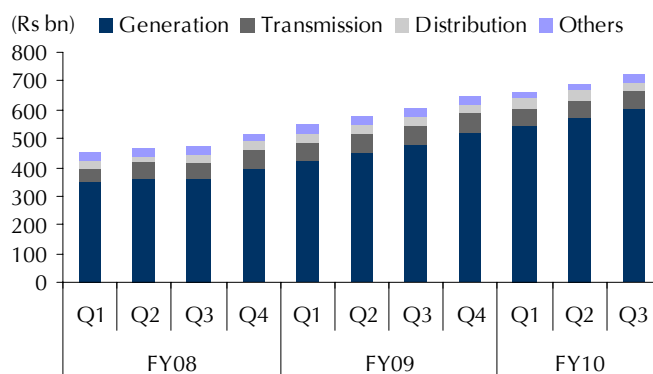
Source: RHH, Company

**Fig 5 - Borrower-wise loan composition**



Source: RHH, Company

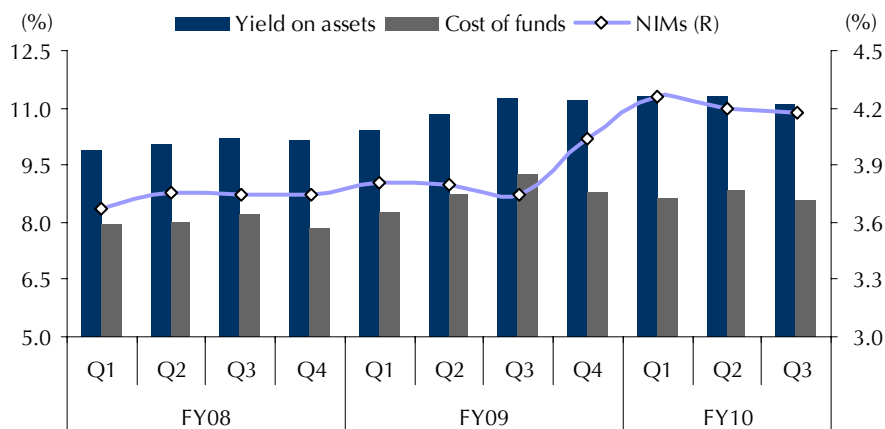
**Fig 6 - Generation constitutes 84% of total loan book**



Source: RHH, Company

**Fig 7 - NIM remained stable**

**NIMs (reported) remained stable QoQ**



Source: Company

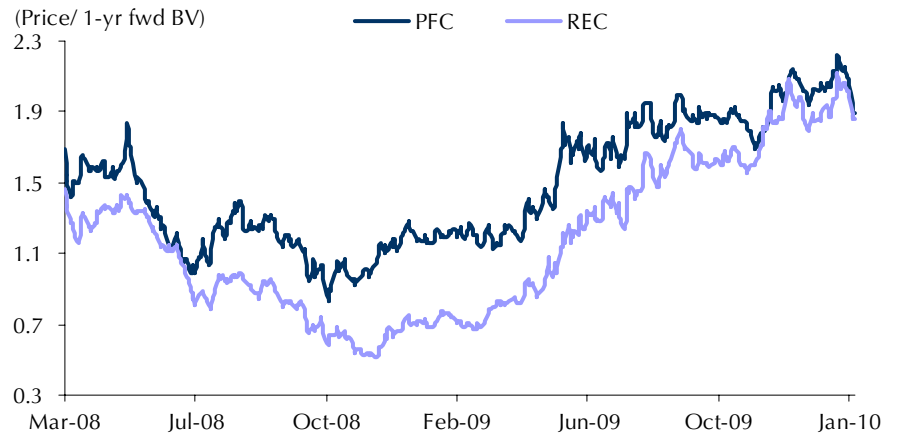


Fig 8 - Comparative valuation – PFC and REC

Company	Price	MCap	P/BV (x)		ROE (%)	
	(Rs)	(Rs bn)	FY10E	FY11E	FY10E	FY11E
PFC	242	278	2.1	1.8	18.3	18.2
REC*	240	206	2.1	1.8	21.6	18.3

Source: RHH, Company \* Adding reserves created for deferred tax liability in net worth

Fig 9 - Valuations – PFC vs REC



Valuation discount of REC has reduced in the last nine months due to its capital raising plans



## Standalone financials

### Profit and Loss statement

Y/E March (Rs mn)	FY09	FY10E	FY11E	FY12E
Interest earned	64,601	79,421	95,740	1,13,196
Interest expended	42,461	50,874	62,295	74,004
<b>Net interest income</b>	<b>22,140</b>	<b>28,547</b>	<b>33,445</b>	<b>39,192</b>
Non-interest income	1,234	1,975	2,389	2,718
Operating expenses	908	831	982	1,117
Pre-provisioning profits	22,466	29,691	34,852	40,793
Provisions	37	115	140	140
PBT	22,430	29,577	34,712	40,653
Tax	5,871	7,038	9,025	10,570
Net profit	16,559	22,539	25,687	30,083
Extraordinaries (net of tax)	3,141	-	-	-
<b>Reported PAT</b>	<b>19,700</b>	<b>22,539</b>	<b>25,687</b>	<b>30,083</b>

### Balance sheet

Y/E March (Rs mn)	FY09	FY10E	FY11E	FY12E
Cash and Bank balances	3,922	3,263	3,389	2,869
Loans and Advances	19,358	21,511	25,173	25,173
Other current assets	13,406	17,498	21,099	24,956
Investments	359	636	636	636
Advances	6,44,290	7,72,417	9,21,093	10,82,192
Net Block (inc CWIP)	751	761	801	839
<b>Total assets</b>	<b>6,82,085</b>	<b>8,16,085</b>	<b>9,72,192</b>	<b>11,36,664</b>
Share Capital	11,478	11,478	11,478	11,478
Reserves & surplus	1,03,600	1,20,096	1,39,068	1,61,094
Net Worth	1,15,078	1,31,574	1,50,546	1,72,572
Unsecured Loans	5,21,602	6,34,465	7,65,496	9,01,012
Current Liabilities	18,606	21,980	26,178	30,519
Provisions	17,156	19,423	22,328	25,917
Deferred Tax liability	555	555	555	555
Interest subsidy fund from Govt	9,089	8,089	7,089	6,089
<b>Total liabilities</b>	<b>6,82,085</b>	<b>8,16,085</b>	<b>9,72,192</b>	<b>11,36,664</b>

Y/E March (Rs mn)	FY09	FY10E	FY11E	FY12E
Sanctions	5,70,300	6,61,548	7,27,703	8,00,473
Growth (%)	(17.9)	16.0	10.0	10.0
Disbursements (Excl. RGGVY)	2,10,540	2,31,213	2,64,539	2,99,262
Growth (%)	29.9	9.8	14.4	13.1

### Per share data

Y/E March	FY09	FY10E	FY11E	FY12E
Shares outstanding (mn)	1,147.8	1,147.8	1,147.8	1,147.8
FDEPS (Rs)	17.2	19.6	22.4	26.2
DPS (Rs)	4.0	4.5	5.0	6.0
Book value (Rs)	100.3	114.6	131.2	150.4

### Key ratios

Y/E March (Rs mn)	FY09	FY10E	FY11E	FY12E
<b>Valuation ratios (x)</b>				
P/E	14.1	12.3	10.8	9.2
P/BV	2.4	2.1	1.8	1.6
P/ABV	2.4	2.1	1.8	1.6
<b>Return ratios (%)</b>				
Interest spread	2.4	2.8	2.8	2.8
Net interest margin	3.8	4.0	3.9	3.9
Yield on assets	10.9	11.2	11.3	11.3
Cost of funds	8.7	8.4	8.5	8.5
Non-int Inc/ Total income	5.3	6.5	6.7	6.5
Opex cost/ Total income	<b>4.0</b>	<b>3.1</b>	<b>3.1</b>	<b>3.0</b>
<b>ROE calculation (%)</b>				
Net interest income/assets	3.8	4.0	3.9	3.9
Non interest income/assets	0.2	0.3	0.3	0.3
Net revenues/Assets	4.0	4.3	4.2	4.2
Operating expense/Assets	0.2	0.1	0.1	0.1
Taxes/Assets	1.0	1.0	1.1	1.1
Extraordinaries/Assets	0.5	-	-	-
ROA	3.4	3.2	3.0	3.0
Equity/Assets	17.8	17.4	16.6	16.1
ROAE	18.9	18.3	18.2	18.6
<b>Growth ratios (%)</b>				
Net interest income	25.2	28.9	17.2	17.2
Non-interest Income	13.2	60.0	20.9	13.8
Total income	24.5	30.6	17.4	17.0
Pre-provisioning profit	25.4	32.2	17.4	17.0
Net profit	36.1	36.1	14.0	17.1
Reported profit	63.2	14.4	14.0	17.1
EPS	63.2	14.4	14.0	17.1
Book value	23.3	14.3	14.4	14.6
<b>Asset quality (%)</b>				
Gross NPA	0.02	0.02	0.02	0.02
Net NPA	0.01	0.01	0.01	0.01



### Quarterly trend

Particulars	Q3FY09	Q4FY09	Q1FY10	Q2FY10	Q3FY10
NII (Rs mn)	5,610	6,370	7,000	7,200	7,470
YoY growth (%)	20.9	32.2	36.2	32.8	33.2
QoQ growth (%)	3.5	13.5	9.9	2.9	3.8
Total income (Rs mn)	5,720	6,610	7,060	8,010	7,600
YoY growth (%)	20.2	28.3	35.2	41.5	32.9
QoQ growth (%)	1.1	15.6	6.8	13.5	(5.1)
PPP (Rs mn)	5,490	6,334	6,880	7,770	7,350
YoY growth (%)	20.9	32.1	36.3	43.1	33.9
QoQ growth (%)	1.1	15.4	8.6	12.9	(5.4)
Adj net profit (Rs mn)	3,781	4,173	5,082	6,470	5,428
YoY growth (%)	18.6	30.6	50.9	67.6	43.6
QoQ growth (%)	(2.1)	10.4	21.8	27.3	(16.1)

### Company profile

Power Finance Corporation (PFC) is a leading public institution primarily involved in the financing of power projects across India. The company provides long-term, short-term and working capital loans to power utilities (state, central and private sector) and power equipment manufacturers. PFC is promoted by the government of India (which holds an 89.8% stake) and plays a strategic role in the government's plan to develop the country's power sector.

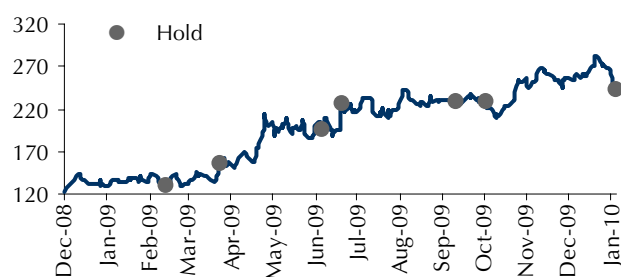
### Shareholding pattern

(%)	Jun-09	Sept-09	Dec-09
Promoters	89.8	89.8	89.8
FIs	5.5	4.2	3.8
Banks & FIs	1.7	3.2	3.3
Public	3.0	2.8	3.1

### Recommendation history

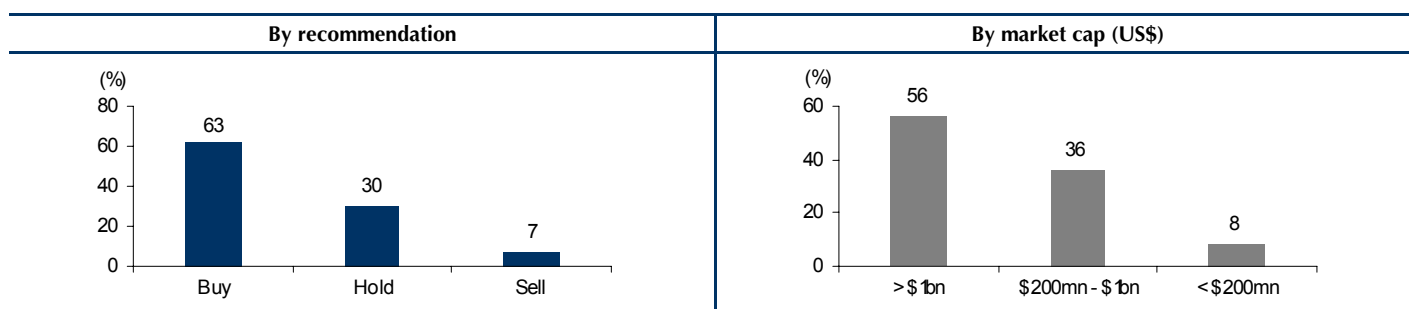
Date	Event	Reco price	Tgt price	Reco
12-Mar-09	Initiating Coverage	129	145	Hold
20-Apr-09	Results Review	154	149	Hold
2-Jul-09	Quarterly Preview	195	185	Hold
15-Jul-09	Results Review	225	219	Hold
6-Oct-09	Quarterly Preview	228	245	Hold
27-Oct-09	Results Review	227	245	Hold
1-Feb-10	Results Review	242	270	Hold

### Stock performance





### Coverage Profile



### Recommendation interpretation

Recommendation	Expected absolute returns (%) over 12 months
Buy	More than 15%
Hold	Between 15% and -5%
Sell	Less than -5%

Recommendation structure changed with effect from March 1, 2009

Expected absolute returns are based on share price at market close unless otherwise stated. Stock recommendations are based on absolute upside (downside) and have a 12-month horizon. Our target price represents the fair value of the stock based upon the analyst's discretion. We note that future price fluctuations could lead to a temporary mismatch between upside/downside for a stock and our recommendation.

### Religare Capital Markets Ltd

4<sup>th</sup> Floor, GYS Infinity, Paranjpe 'B' Scheme, Subhash Road, Vile Parle (E), Mumbai 400 057.

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