

## Reliance Infra – REDUCE

18 May 2010

## Timely completion of projects holds the key

**RELI's 4QFY10 adjusted (standalone) profit growth of 20% YoY came in-line. While disclosing FY10 consolidated profit (up 12% YoY), it disclosed revenues from road projects. At its analyst meet, the management said it would commercialise 13 projects in FY11 (metros, roads). The stock in our view is unlikely to see a re-rating, unless RELI completes these projects on time and reduces the ICD (Rs25bn as of FY09), which have been key concerns for investors.**

**Adjusted profit growth in-line:** RELI's EPC business revenues were up 43% YoY, which offset the 10% YoY fall in power revenues and led to 9% YoY growth in sales. The 4QFY10 adjusted profit growth of 20% YoY was more driven by power business (EBIT up 72% YoY), as the EPC business reported moderate 20% YoY growth in EBIT. FY10 consolidated profit was up 12% YoY, including revenues from the road business. Continuation of such disclosures would help better estimate RELI's earnings trajectory.

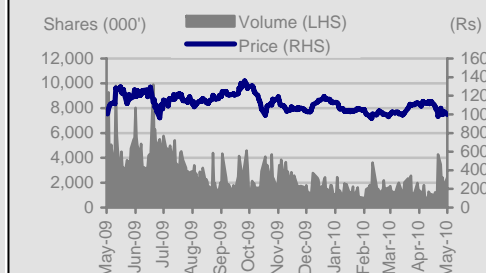
**Recovery of regulatory assets critical going ahead:** RELI's unbilled power revenues during the year were Rs6bn (Rs16bn including for FY09). Recovery of regulatory assets is critical for RELI earning entitled 15% assured RoE for its distribution business. During the analyst meet, management said it was confident it would recover such unbilled revenues in subsequent years. Our forecasts do not build in any under-recoveries in FY11 as well as FY12.

**EPC business growth linked to R-Power's project completion:** As of FY10, RELI's EPC order book was US\$4.3bn. To achieve ~40-50% YoY revenue growth (management guidance), milestone achievement in R-Power's projects holds the key, which account for the bulk of the order book. Our FY11 forecasts build in ~50% YoY growth in revenues, with EBITDA margin of 8.5% (almost flat YoY).

**Timely completion of projects key for stock's outperformance:** The stock in our view is unlikely to trade substantially below its FY11 consolidated BV (estimated at Rs885/share, assuming promoters convert the outstanding 23m warrants). However, for a re-rating thereon, RELI would have to execute projects on time and reduce inter-corporate deposits (Rs25bn as of FY09).

<b>CMP</b>	<b>Rs998</b>
<b>Market cap (US\$ m)</b>	<b>4997</b>
<b>Bloomberg</b>	<b>RELI IN</b>
52Wk High/Low (Rs)	1405/889
Diluted o/s shares (m)	225
Daily volume (US\$ m)	36
Dividend yield FY10ii (%)	2.0
Free float (%)	62.3
<b>Shareholding pattern (%)</b>	
Promoters	37.8
FII's	16.4
Domestic MFs	27.6
Others	18.2

<b>Price performance (%)</b>			
	<b>1M</b>	<b>3M</b>	<b>1Y</b>
Reliance Infra	-10.7	-5.1	21.6
Rel. to Sensex	-6.4	-7.6	-16.7
NTPC	-1.7	1.1	8.8
TPWR	-0.4	4.5	45.2
CESC	-0.2	1.5	55.4

**Stock Performance****Financial Summary (standalone)**

<b>Y/e 31 Dec</b>	<b>FY08A</b>	<b>FY09ii</b>	<b>FY10</b>	<b>FY11ii</b>	<b>FY12ii</b>
Revenues (Rs m)	63,642	96,965	96,285	127,693	156,250
EBITDA Margins (%)	13%	7%	12%	11%	12%
Pre-Exceptional PAT (Rs m)	7,157	4,389	11,517	13,850	16,566
Reported PAT (Rs m)	10,846	10,461	11,517	13,850	16,566
EPS (Rs)	30.4	19.4	47.0	51.6	61.8
Growth (%)	-7.5	-36.1	142.2	9.8	19.6
<b>PER (x)</b>	32.9	51.4	21.2	19.3	16.2
ROE (%)	9.6	8.6	9.0	8.8	9.9
Debt/Equity (x)	0.4	0.6	0.5	0.3	0.3
<b>EV/EBITDA (x)</b>	33.5	43.0	27.8	22.2	17.3
Price/Book (x)	2.1	1.9	1.9	1.7	1.6

Source: IIFL Research, Priced as on 17 May 2010

**Figure 1: RELI's 4QFY10 adjusted profits were up 20% YoY**

(Rs m)	4QFY09	3QFY10	4QFY10	% YoY	% QoQ
Generation (MU)	1,480	1,659	1,428	-4%	-14%
Units sold (MU)	2,224	2,459	2,459	11%	0%
Realisation Rs/unit)	6.62	6.60	5.39	-19%	-18%
<b>Net Sales</b>	<b>23,397</b>	<b>22,351</b>	<b>25,531</b>	<b>9%</b>	<b>14%</b>
Material costs	17,503	17,016	20,475	17%	20%
Personnel Costs	1,313	1,722	1,647	25%	-4%
Other overheads	3,499	1,784	1,603	-54%	-10%
<b>EBIDTA</b>	<b>1,081</b>	<b>1,830</b>	<b>1,806</b>	<b>67%</b>	<b>-1%</b>
<b>EBIDTA Margin</b>	<b>5%</b>	<b>8%</b>	<b>7%</b>		
Depreciation	627	830	581	-7%	-30%
Interest	1,013	565	907	-10%	60%
Other income	3,302	2,679	2,576	-22%	-4%
<b>PBT</b>	<b>2,743</b>	<b>3,114</b>	<b>2,895</b>	<b>6%</b>	<b>-7%</b>
Tax	649	395	384	-41%	-3%
<b>Adjusted PAT</b>	<b>2,094</b>	<b>2,719</b>	<b>2,511</b>	<b>20%</b>	<b>-8%</b>
<b>Adj. PAT Margin</b>	<b>9%</b>	<b>12%</b>	<b>10%</b>		
Extra ordinary (expense)/income	1,367	52	-		
<b>Reported PAT</b>	<b>3,461</b>	<b>2,771</b>	<b>2,511</b>	<b>-27%</b>	<b>-9%</b>

Source: IIFL Research

**Figure 2: Sharp jump in EPC revenues driving the sales growth**

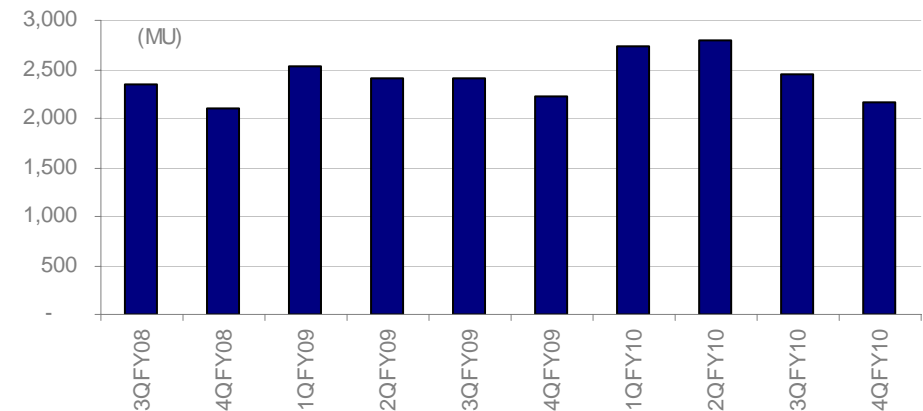
(Rs m)	4QFY09	3QFY10	4QFY10	% YoY	% QoQ
Sale of Electricity Energy	14,721	16,237	13,258	-10%	-18%
EPC and Contracts	9,249	6,638	13,181	43%	99%
<b>Gross Turnover</b>	<b>23,971</b>	<b>22,875</b>	<b>26,439</b>	<b>10%</b>	<b>16%</b>

Source: IIFL Research

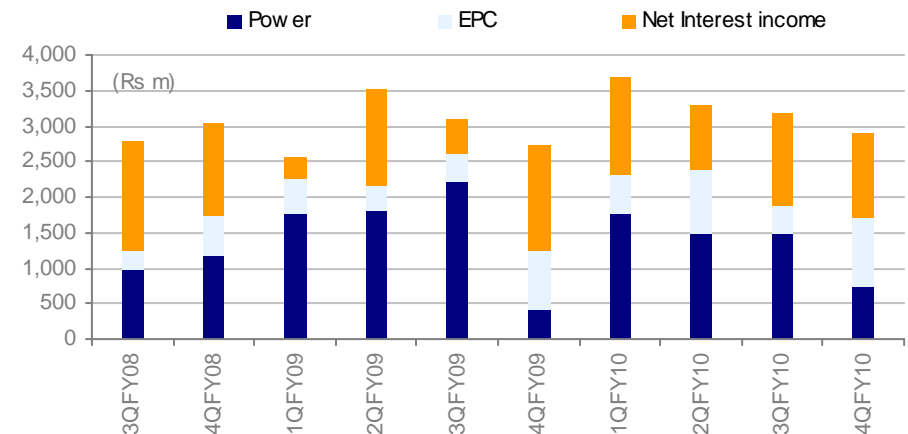
**Figure 3: 38% YoY growth in EBIT was driven however by power business**

(Rs m)	4QFY09	3QFY10	4QFY10	% YoY	% QoQ
Sale of Electricity Energy	431	1,492	742	72%	-50%
EPC and Contracts	818	398	981	20%	147%
Other Operations	0	-	-	-100%	-
<b>Total EBIT</b>	<b>1,250</b>	<b>1,890</b>	<b>1,723</b>	<b>38%</b>	<b>-9%</b>

Source: IIFL Research

**Figure 4: RELI in 4QFY10 sold 2.2BU, flat YoY**


Source: IIFL Research

**Figure 5: Share of treasury income down to 40% from 54% YoY**


Source: IIFL Research

**Figure 6: RELI's consolidated profits up 12% YoY**

(Rs m)	FY10	FY09	% YoY
Sales	144,960	125,013	16.0%
EBITDA	15,203	14,095	7.9%
PAT (pre consol profits of RPWR)	11,978	12,591	-4.9%
PAT (Post consol profits of RPWR)	15,194	13,532	12.3%

Source: IIFL Research

**Figure 7: Disclosed road revenue for the first time**

(Rs m)	FY10	FY09	% YoY
Sale of Electricity Energy	115,345	103,188	11.8%
EPC and Contracts	33,048	25,259	30.8%
Roads	253	-	NA
Others	2	-	NA

Source: IIFL Research

**Figure 8: EPC EBIT up 30% YoY**

(Rs m)	FY10	FY09	% YoY
Sale of Electricity Energy	8,286	7,219	14.8%
EPC and Contracts	2,410	1,855	29.9%
Roads	155	-	NA
Others	(23)	(30)	NA

Source: IIFL Research

**Figure 9: EBIT margins in roads below management's guidance of ~75-80%**

%	FY10	FY09	% YoY
Sale of Electricity Energy	7.2%	7.0%	19bps
EPC and Contracts	7.3%	7.3%	-5bps
Roads	61.2%	0%	NA

Source: IIFL Research

**Figure 10: Key projects being implemented by RELI's EPC division**

Project	Comment
1,200 MW Rajiv Gandhi thermal power project, Hisar	First 600MW unit synchronized. Commissioning of Chinese equipment carried out by in-house team
1,200MW Raghunathpur thermal power station, West Bengal	Owned by Damodar Valley Corp Steam-drum lifting completed
500MW Parichha thermal power station, UP	BOP project
300MW Butibori thermal power station, UP	Owned by Reliance Power
Western region system strengthening	Projects under implementation on BOO basis Erection of towers completed Expect completion by 1QFY11
Mumbai transmission network strengthening	All regulatory approvals in place Expected completion by 4QFY12
Parbati Koldam transmission lines (JV with PGCIL)	Stage-I forest clearance for Parbati-Koldam section received Expect completion by Dec-2012

Source: Company, IIFL Research

**Figure 11: Key infrastructure projects under various stages of development**

Project	Comment
NK Toll Project	Already operational
DS Toll Project	Already operational
TK Toll Project	Commercial operations expected in FY11
TD Toll Project	Commercial operations expected in FY11
SU Toll Project	Commercial operations expected in FY11
Road between Gurgaon and Faridabad	4-laning of Gurgaon-Faridabad corridor of 24km and reconstruction of Ballabgarh-Sohna road link 17-year concession period. Commercial operations expected by end-FY11
Pune Satara Toll project	4/6-laning of 53km road connecting Jaipur and Bikaner via Sikar 18-year concession period; Commercial operations expected by end of Apr-2010
Jaipur Reengus Toll project	4/6-laning of road connecting Pune and Satara; Commercial operations expected by end of Apr-2010
Mumbai Metro I	65-75% civil work completed; Received Rs2bn viability gap funding from MMRDA; Commercial operations expected by end CY10
Airport Metro Express Line - Delhi	Financial closure for complete debt of Rs20bn achieved in Feb-09 First train expected in April; Commercial operations before Sept-2010

Source: Company, IIFL Research

## Key takeaways from the analyst meet:

- Revenue contribution from 13 projects expected in FY11:** RELI indicated that it expects 13 assets in its portfolio worth Rs213bn to start contributing revenues in FY11. These include nine road projects, Delhi and Mumbai Phase I metros, Western region strengthening scheme, and Bandra-Worli Sea Link.
- Quarterly disclosure of consolidated results going forward:** RELI highlighted that given its large asset portfolio spread across various SPVs, standalone results (comprising distribution, EPC and R-Power businesses) would be an inaccurate representation of the company's performance. Hence, going forward, it would start quarterly disclosures of its consolidated results. It also intends to provide a segmental break-up highlighting performance across its distribution, EPC, roads and metros divisions. Such disclosures would help track performance of each asset class on a quarterly basis.
- Regulatory assets of Rs16bn not threatened by upcoming license renewal:** RELI has recognised Rs16bn regulatory assets during the year in its Mumbai distribution business, on account of its cost under-recoveries incurred due to the stay on its proposed tariff hike. It was feared that as a part of the distribution licence renewal process, these regulatory assets could be cancelled. Management indicated that these regulatory assets would not be affected by the licence renewal. It also highlighted that any cost savings over and above an approved costs, would be used to extinguish these regulatory assets before being passed on to the consumers. RELI does not expect the new tariff to result in cost under-recoveries going forward.
- Delhi distribution expected to remain in the incentive zone in FY11:** The Delhi distribution business continued its strong performance; we expect it to earn an incentive of Rs1.4bn in FY10, as it continues to surpass the AT&C loss reduction targets. RELI expects the Delhi business to remain in the incentive zone over FY11, and maintain its current rate of profit growth.

Figure 12: Delhi discoms expected to earn Rs1.4bn in incentives over FY10

Discom	Target AT&C losses	Actual AT&C loss
BRPL	20.2%	18.9%
BYPL	26.2%	22.9%

Source: IIFL Research

- Net cash and cash equivalent of Rs47bn:** As of 31-March 2010, RELI has cash and cash equivalents of Rs88bn, and an outstanding debt of Rs41bn. There have been concerns that the ICDs on books have increased in FY10. Management did disclose the exact break-up of cash and cash equivalents, but it did say that the ICDs have remained flat over FY10. As of FY09, ICDs on books stood at Rs25bn.

**Key to our recommendation structure**

**BUY** - Absolute - Stock expected to give a positive return of over 20% over a 1-year horizon.

**SELL** - Absolute - Stock expected to fall by more than 10% over a 1-year horizon.

In addition, **Add** and **Reduce** recommendations are based on expected returns relative to a hurdle rate. Investment horizon for **Add** and **Reduce** recommendations is up to a year. We assume the current hurdle rate at 10%, this being the average return on a debt instrument available for investment.

**Add** - Stock expected to give a return of 0-10% over the hurdle rate, ie a positive return of 10%+.

**Reduce** - Stock expected to return less than the hurdle rate, ie return of less than 10%.

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