

Rural Electrification Corporation
Maintain - Sell
Good Company - Price Not Justified



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Good Company - - Priced In

REC Q2FY10 is better than our expectation where in for the quarter PAT has grown up by 60% YoY & 5% QoQ, on account of robust loan book growth of 32% YoY, with stable interest spread of 3.35% as compare to 3.36% in Q2FY09. Assets quality remained healthy with gross NPA at 0.04%.

Particular (Rsmn)	Q2FY10	Q2FY09	Q1FY10	YoY%	QoQ%
Interest Earned	15,836	11,180	14,609	42%	8%
Interest Expended	9,413	6,692	8,735	41%	8%
NII	6,423	4,488	5,874	43%	9%
Other Income	393	556	480	-29%	-18%
Total Income	6,816	5,043	6,354	35%	7%
Operating Expenses	351	393	300	-11%	17%
PPP	6,466	4,651	6,054	39%	7%
Provisions & Contingencies	1	-	1		-31%
Provision for Taxes	1,521	1,563	1,335	-3%	14%
Net Profit	4,944	3,088	4,718	60%	5%

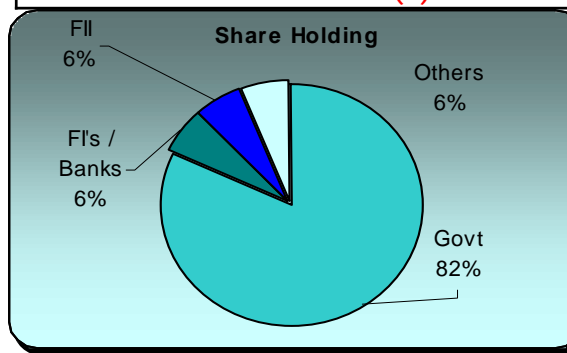
Sensex	16052
Nifty	4750

Stock Data

BSE Code	532955
NSE Code	RECLTD
Bloomberg	RECL IN
Reuters	RURL.BO
Shares Issued (mn)	858.66
Market Cap (Rs mn)	1,69,413
52 Wk H/L (Rs)	225/54
Face Value (Rs)	10
Avg. daily vol. (12m)	3,81,041

Absolute Return (%)

	1m	3m	12m
Absolute	(2)	5	202
Rel. to Sensex	3	(1)	125



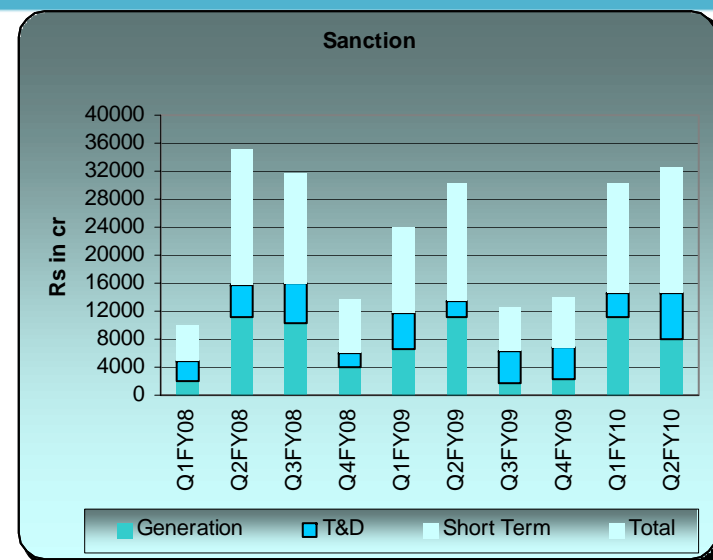
Result Highlights

Outstanding Sanction of 0.8trn provide strong visibility on loan growth: Loan disbursal for the quarter grew YoY by 16% at Rs 55bn, however sanction for the quarter grew by 8% YoY at Rs 163bn out of which transmission & distribution activity led the race with a sanction of Rs 67bn .We remain status quo on our loan growth estimate of 27% CAGR for FY09-11E as compare to aggressive credit growth guidance by the management

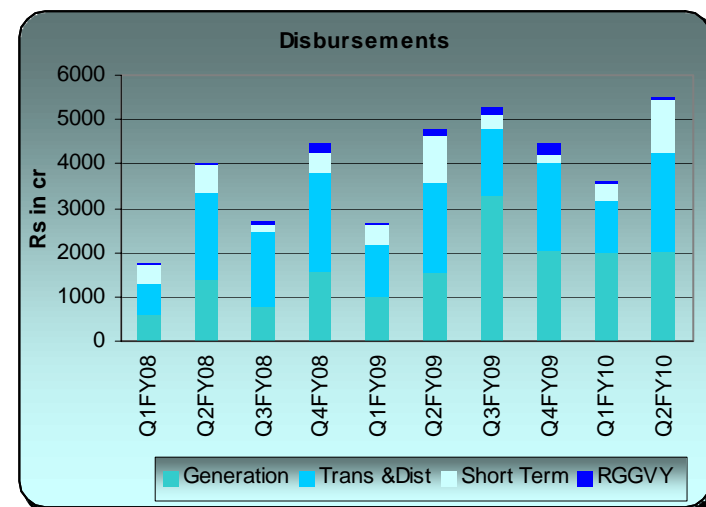
Margin still above 3%: Reported Yield on assets reduces marginally by 12bps QoQ to 11% incremental loan at lower rate. Due to replacement of low rate capital bond with high cost fund led to an increase in cost of fund by 5bps QoQ. Which in total resulted to a reduction of 17 bps QoQ in interest spread to 3.35%. We expect that the NIM to remain above 3% in FY10E-11E due to pricing & reprising of loan book at a higher rate.

Asset Quality: Gross NPA in quarter at Rs 210mn as compare to Rs 320mn in Q1FY10 resulted to a GNPA of 0.04% & Net NPA still stood at Zero of loan outstanding. We expect that with the majority of lending is to the government backed projects so the NPL level to remain below 1%.

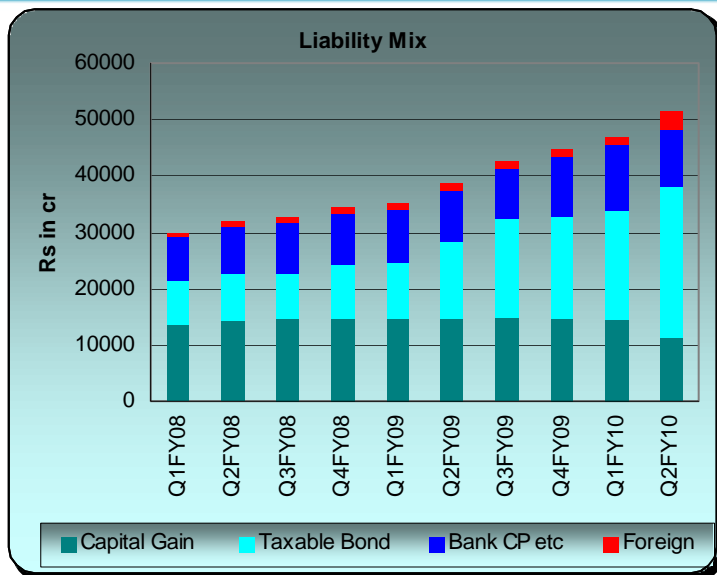
Government approves capital raising plan: REC got a nod from GOI to raise fresh equity to the tune of 15% of current equity and government will divest 5%. We have factor equity issuance at a price of Rs195/- in our calculation. Management indicate that REC will rollout FPO in Q4FY10E



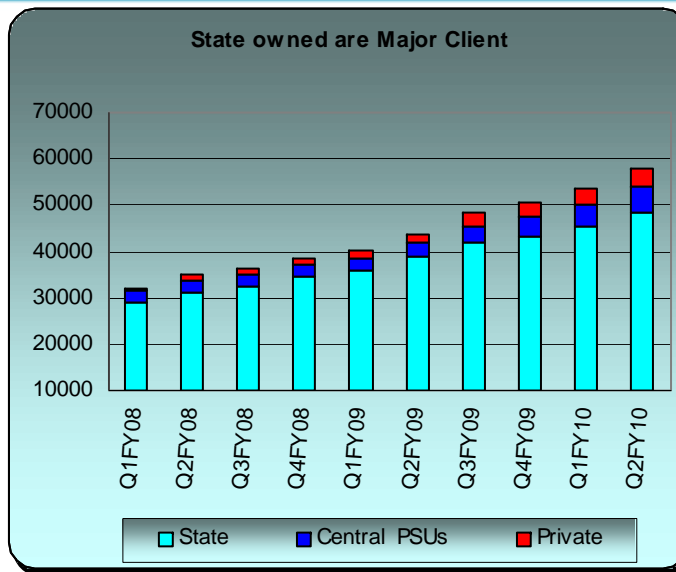
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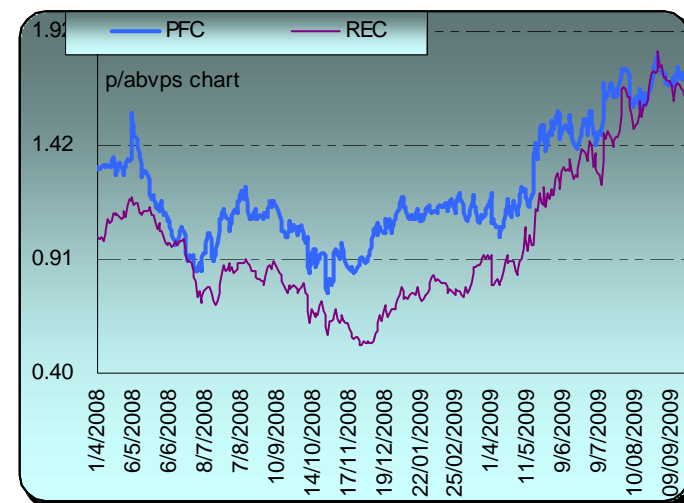
Source: MF Global PCG, Company



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Valuation: At CMP of Rs.199 REC is currently trading at 1.9x & 1.6x of its ABV of FY10E & 11E respectively. With the thrust of government for rural electrification & there plan on it led funding requirement for transmission & distribution around Rs 3.5tn, which we expect give ample visibility for REC to grow, still the current sanction limit gives robust visibility. We maintain our RONW of REC in range of 16-18% and ROAA estimate of 2.2-2.6%. With a robust visibility & thrust on power sector we had expected the rerating in power & Infrastructure finance companies but as the Stock has rallied by 150% from our recommended price of Rs 80 (Jan09) in eight month so we **have downgraded the stock to Sell**. With approval from government for a FPO we expect some speculation in price as a possibility

Concern: We expect that current price is factoring the FPO pricing to be in range of Rs180-200, any upward pricing will only give visibility for further upside from current levels.



Financials

Income Statement (Rs mn)					Balance Sheet (Rs mn)				
Year ended	FY08	FY09	FY10E	FY11E	Year ended	FY08	FY09	FY10E	FY11E
Interest income	33,610	46,650	55,631	69,834	Owned Fund	53,678	62,179	102,383	121,597
Interest expenses	20,624	28,970	33,089	42,857	Borrowed Fund	342,820	448,512	569,610	729,101
Net Interest Income	12,986	17,680	22,542	26,977	Total equity & liabilities	396,498	510,691	671,994	850,698
Non Interest income	1,768	2,680	2,254	2,698	YOY Growth %		29%	32%	27%
Operating income	14,754	20,360	24,796	29,675	Cash & Bank Balance	12,530	16,763	28,481	36,455
Operating expenses	1,628	1,127	1,179	1,233	Investment	11,474	10,074	10,175	10,276
Pre-provisions profit	13,126	19,233	23,617	28,442	Advances	393,165	513,810	637,124	828,262
Provisions & Contingencies	-	24	183	994	Fixed Assets	772	785	903	1,038
Tax	452	6,488	6,093	8,234	Other Net Assets	(21,444)	(30,741)	(4,689)	(25,333)
Net Profit	12,673	12,721	17,341	19,213	Total assets	396,497	510,691	671,994	850,698
EPS	10	15	18	19	Abvps	60	72	104	121

Ratios

Profitability Ratio	FY08	FY09	FY10E	FY11E	Du Pond Analysis	FY08	FY09	FY10E	FY11E
NIM Computed	3.1%	3.3%	3.3%	3.1%	NII/Avg.total assets	3.0%	3.2%	3.7%	3.5%
Operating Exp/Net Income	12.5%	6.4%	5.2%	4.6%	Non-Interest Income/ Avg.total assets	0.4%	0.5%	0.4%	0.3%
RoNW	16.0%	20.5%	16.9%	15.8%	Operating expenses/Avg.total assets	0.4%	0.2%	0.2%	0.2%
ROAA	2.0%	2.3%	2.6%	2.2%	Provisions/Avg.total assets	0.0%	0.0%	0.0%	0.1%
Equity/ Total Assets	12.5%	11.1%	15.1%	13.9%	Tax/Avg.total assets	1.1%	1.2%	1.0%	1.1%
					Avg Asset / Avg Eq	8.0	9.0	6.0	6.4
Growth	FY08	FY09	FY10E	FY11E	Asset Quality	FY08	FY09	FY10E	FY11E
Credit	23.9%	31.0%	24.0%	30.0%	Gross NPA Absolute (Rs in mn)	3220.0	690.0	828.3	3313.0
Borrowing	13.2%	31.0%	27.0%	28.0%	Net NPA Absolute (Rs in mn)	2400.0	210.0	165.7	1656.5
Balance Sheet	0.0%	30.1%	21.2%	29.5%	Gross NPA %	0.8%	0.1%	0.1%	0.4%
Net Profit	0.0%	47.9%	36.3%	10.8%	Net NPA %	0.6%	0.0%	0.0%	0.2%
Book value	0.0%	15.8%	43.2%	18.8%	Provision Coverage	25.5%	69.6%	80.0%	50.0%

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