

Company Results Review

31 January 2007 | 9 pages

National Thermal Power (NTPC.BO)

Buy: Another Quarter of Steady Profit Growth

- Another quarter of strong growth** — After growing 19% YoY in 1HFY07, NTPC once again grew Recurring PAT 20% in 3QFY07 to Rs19.5bn, 5% ahead of CIR estimates of Rs18.6bn and 7% ahead of consensus estimates of Rs18.2bn on account of higher than expected generation and incentives.
- Generation grew 13.3%** — According to the CEA's monthly generation report, NTPC generated 49.3 billion units (bu) in 3QFY07 up 13% YoY partially aided by the asset takeover of the 720MW Badarpur Power Plant.
- Capacity addition of 3210MW in FY07E** — To date in FY07E NTPC has commissioned a 210MW unit in Unchahar and a 500MW unit in Vindhyachal. Due to a bunching up of projects 2500MW is expected to be synchronized in the last 2 months of the financial years. A 500MW unit in Sipat might slip over to June 07.
- Capacity increasing 2x in 5 years and 3x in 10 years** — NTPC aims to double its capacity to 48GW and effectively control 51GW by FY12E. The company has plans to triple capacity to 76GW by FY17E. Its capex is well funded with low current gearing of 0.45x, high current cash levels of Rs84.7bn, a strong credit rating and a high annual cash flow from operations of Rs175bn for FY07E-15E.
- Our top pick among the Indian electric utilities** — NTPC is our top pick in the Indian Electric Utility space for its defensiveness (particularly for investors who are benchmarked against broad market indices), large market capitalization, regulated earnings stream and secular growth.

Buy/Low Risk	1L
Price (31 Jan 07)	Rs141.95
Target price	Rs181.00
Expected share price return	27.5%
Expected dividend yield	2.3%
Expected total return	29.8%
Market Cap	Rs1,170,444M US\$26,571M

Price Performance (RIC: NTPC.BO, BB: NATP IN)



Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
31 Mar	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2005A	49,271	6.14	20.2	23.1	2.8	12.7	1.7
2006A	55,714	6.76	10.1	21.0	2.6	12.8	2.0
2007E	69,280	8.40	24.4	16.9	2.4	14.8	2.3
2008E	78,432	9.51	13.2	14.9	2.2	15.3	2.5
2009E	83,201	10.09	6.1	14.1	2.0	15.0	2.8

Source: Powered by dataCentral

See page 7 for Analyst Certification and important disclosures.

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¹Citigroup Global Market India Private Limited

Fiscal year end 31-Mar	2005	2006	2007E	2008E	2009E
Valuation Ratios					
P/E adjusted (x)	23.1	21.0	16.9	14.9	14.1
EV/EBITDA adjusted (x)	18.9	17.5	13.0	11.6	10.6
P/BV (x)	2.8	2.6	2.4	2.2	2.0
Dividend yield (%)	1.7	2.0	2.3	2.5	2.8
Per Share Data (Rs)					
EPS adjusted	6.14	6.76	8.40	9.51	10.09
EPS reported	7.23	7.06	8.40	9.51	10.09
BVPS	50.67	54.53	59.28	64.69	70.22
DPS	2.40	2.80	3.20	3.60	4.00
Profit & Loss (RsM)					
Net sales	222,252	256,761	305,828	354,684	401,991
Operating expenses	-184,638	-215,233	-247,771	-284,666	-322,814
EBIT	37,614	41,528	58,057	70,018	79,177
Net interest expense	-9,231	-9,585	-11,686	-14,393	-17,584
Non-operating/exceptionals	23,600	26,078	26,452	26,608	25,215
Pre-tax profit	51,983	58,021	72,823	82,232	86,808
Tax	-2,712	-2,307	-3,543	-3,800	-3,607
Extraord./Min.Int./Pref.div.	8,799	2,488	0	0	0
Reported net income	58,070	58,202	69,280	78,432	83,201
Adjusted earnings	49,271	55,714	69,280	78,432	83,201
Adjusted EBITDA	57,198	62,005	86,416	101,763	119,395
Growth Rates (%)					
Sales	9.7	15.5	19.1	16.0	13.3
EBIT adjusted	57.0	10.4	39.8	20.6	13.1
EBITDA adjusted	29.4	8.4	39.4	17.8	17.3
EPS adjusted	20.2	10.1	24.4	13.2	6.1
Cash Flow (RsM)					
Operating cash flow	65,007	68,373	96,021	98,078	102,292
Depreciation/amortization	19,584	20,477	28,359	31,745	40,218
Net working capital	-12,647	-10,306	-1,618	-12,100	-21,126
Investing cash flow	-91,106	-49,159	-121,232	-107,164	-169,537
Capital expenditure	-54,508	-65,279	-128,393	-113,097	-175,529
Acquisitions/disposals	0	0	0	0	1
Financing cash flow	20,531	4,717	33,417	10,956	45,240
Borrowings	16,350	31,095	63,497	44,795	82,839
Dividends paid	-22,470	-26,325	-30,080	-33,840	-37,599
Change in cash	-5,568	23,931	8,207	1,869	-22,004
Balance Sheet (RsM)					
Total assets	659,483	717,371	828,937	920,744	1,048,584
Cash & cash equivalent	60,783	84,714	92,921	94,790	72,783
Accounts receivable	13,747	8,678	11,712	18,172	30,895
Net fixed assets	322,433	367,235	467,270	548,621	683,932
Total liabilities	241,720	267,784	340,150	387,364	469,602
Accounts payable	67,467	61,402	70,271	72,690	72,089
Total Debt	170,878	201,973	265,470	310,265	393,104
Shareholders' funds	417,763	449,587	488,788	533,380	578,980
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	25.7	24.1	28.3	28.7	29.7
ROE adjusted	12.7	12.8	14.8	15.3	15.0
ROIC adjusted	11.7	11.2	12.7	12.6	11.6
Net debt to equity	26.4	26.1	35.3	40.4	55.3
Total debt to capital	29.0	31.0	35.2	36.8	40.4

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Figure 1. NTPC 3QFY07 Results

Year End March 31 (Rs million)	3QFY06	3QFY07	% change	3QFY07E
Net Sales	68689	81468	19%	79936
Fuel Cost	(41886)	(52314)	25%	(50839)
<i>% of net sales</i>	<i>61.0%</i>	<i>64.2%</i>		<i>63.6%</i>
Employee Cost	(2478)	(2805)	13%	(2700)
<i>% of net sales</i>	<i>3.6%</i>	<i>3.4%</i>		<i>3.4%</i>
Others	(3393)	(3754)	11%	(4237)
<i>% of net sales</i>	<i>4.9%</i>	<i>4.6%</i>		<i>5.3%</i>
Rebate under one time settlement	(1612)	0	-100%	0
EBITDA	19320	22595	17%	22160
% Margin	28%	28%	(39)	28%
Depreciation	(5063)	(5138)	1%	(4800)
EBIT	14257	17457	22%	17360
% Margin	21%	21%	67	22%
Interest	(2829)	(4374)	55%	(4850)
Other Income: Recurring	5260	7752	47%	6700
PBT	16688	20835	25%	19210
Provision for tax	(516)	(1369)	165%	(600)
Effective tax rate	3.1%	6.6%		3.1%
Recurring PAT	16172	19466	20%	18610
Prior Period/Extra-ordinary	1645	1567		
Reported PAT	17817	21033	18%	18610

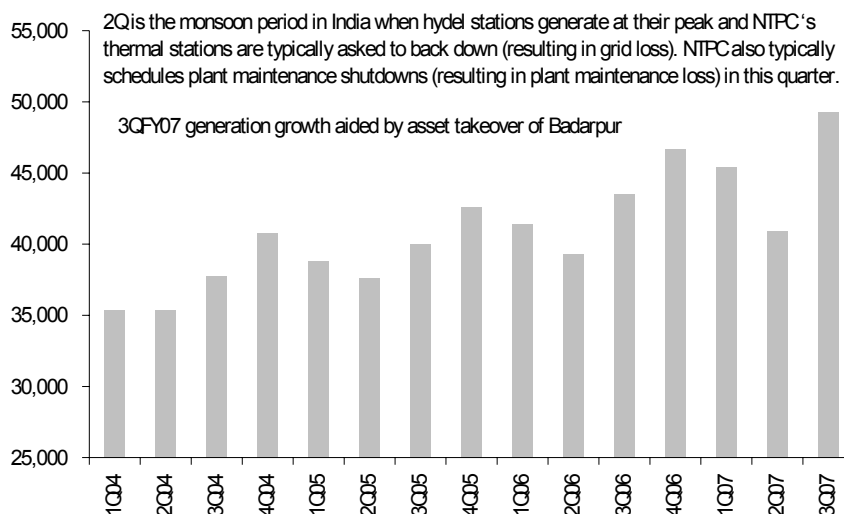
Source: NTPC and Citigroup Investment Research

Figure 2. NTPC Capacity Addition Schedule in FY07E

	FY07E	Schedule	Contractors
Vindhyachal	1000	1- Jul 06, 2 - Mar07	BHEL
Kahalgaon II	1500	1- Feb 07, 2- Mar 07, 3 - Mar 07	BHEL
Unchahar	210	Sep 06	BHEL
Sipat II	500	1 - Mar07, 2 - Jun 07	BHEL
Total	3210		

Source: Citigroup Investment Research

Figure 3. NTPC Quarterly Gross Generation



Source: CEA and Citigroup Investment Research

National Thermal Power

Company description

NTPC is India's largest power generator with 25GW of capacity (22% of India's installed capacity) and generates 170bu (29% of India's generation). Its capacity is spread across 21 locations with coal-based units (20.69GW), gas-based units (3.96GW) and three JV projects (314MW). NTPC's output is contracted through long-term PPAs (25 years for coal-based and 15 years for gas-based) with its customers (SEBs 99% of its sales). Currently, the entire billing to the SEBs is secured through letters of credit. NTPC plans to double capacity by FY12E and triple capacity by FY17E. The company's strong finances and project implementation record leave us optimistic about it achieving its targeted growth.

Investment thesis

We rate NTPC as Buy/Low Risk (1L) with a target price of Rs181. At current levels, we view NTPC as a defensive option, particularly for investors benchmarked against broad market indices, and like it for its large market capitalization, regulated earnings stream and secular growth. NTPC's market leadership (29% share of the country's power generation), competitive cost structure (average tariffs of Rs1.20 to 1.90/ unit – the lowest in the country), strong project-implementation skills and robust finances (gearing of 0.45x and cash/share of Rs10.3) puts the company in a strong position to expand capacity (12% CAGR targeted for FY06-12E), in our view. We expect volatility in earnings (FY05-09E) to be minimal – under current regulations, key costs are a pass-through, allowing for post tax ROE of 14% vs. the current 10-year GOI bond yield of 7.5%.

The tripartite agreement signed among the Central Power Sector Utilities (including NTPC), the Reserve Bank of India and the state governments to ensure a payment guarantee mechanism to the central utilities appears to be working well. This has resulted in a significant improvement in the cash flows of NTPC, and hence its ability to invest in new generation projects.

Valuation

Our valuation methodology for NTPC involves setting a floor price for the stock and then valuing the value of growth opportunity (VGO) captured by our DCF calculation. We set a floor price of Rs141 for the NTPC stock using Replacement Cost of Assets methodology and adding the value of power bonds and cash and investment holdings.

However, we believe the Replacement Cost of Methods does not fully capture the upside inherent in NTPC's unprecedented capacity addition plan against a backdrop of persistent peak and base load deficits that is further exacerbated by rapid economic growth. To capture this value we use DCF methodology and set a target price of Rs181.

Risk

We rate NTPC as Low Risk according to our quantitative risk-rating system, which tracks 260-day historical share price volatility. We also consider the following factors: v Stable and regulated earnings and cash flows from operations, with fuel costs being a pass-through.

- Secular growth prospects for the power sector in India, given current shortages and low usage and penetration levels.
- Competitiveness, reflected in dominant market share and strong technical and operating performance.

Key risks to NTPC's operations and our earnings forecasts could emanate from the following:

- NTPC's operations depend on timely availability of fuel. NTPC's gas-based plants have been hampered by poor fuel supply, resulting in sub-optimal capacity utilization.
- NTPC is implementing larger modules and newer technologies such as 660MW and 800MW super critical technology and alternative fuels such as gas and hydro more aggressively. These initiatives could place demands on the company's project management and technology absorption skills.
- NTPC's regulated rate of return for the period FY05-09 was reduced from 16% to 14% (post tax ROE) due to falling interest rates and the presence of a payment security mechanism. Any further reduction post-Y09 would affect earnings and profitability.
- UI rates are very high compared with normal tariff rates and there could be pressure from the SEBs to reduce this spot market premium.
- There could be future payment risk due to resurfacing of free power supply to agricultural customers as a populist measure by a few states.

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- NTPC has entered into a JV with GasPatrol – France, and Canoro Resources – Canada and has bid for an oil & gas exploration block in northeast India. This raises the risk of non-discovery, like for any exploration & production (E&P) venture.

Analyst Certification Appendix A-1

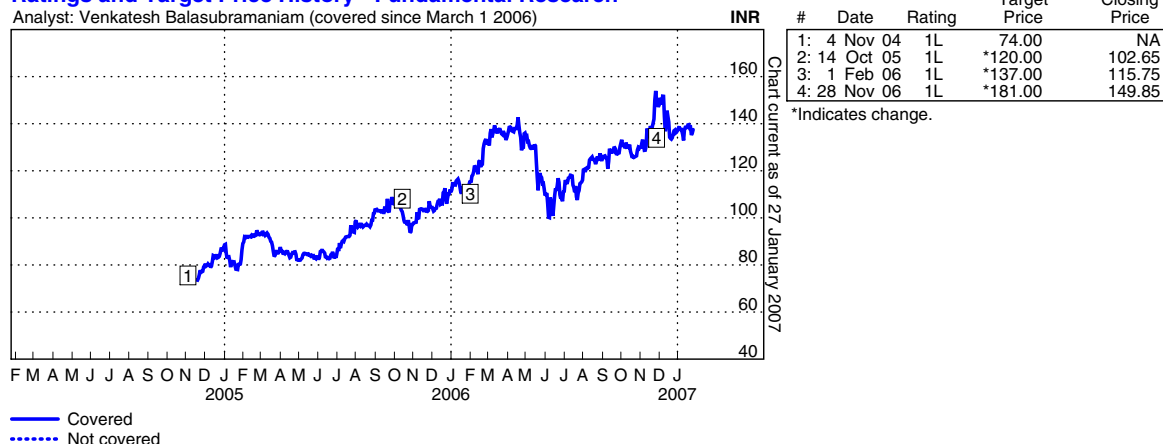
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Ratings and Target Price History - Fundamental Research

Analyst: Venkatesh Balasubramaniam (covered since March 1 2006)



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