

MAT grossing to hit ROE by 4%; Downgrade to Hold

October 27, 2010

Reco	Previous Reco
Hold	Accumulate
CMP	Target Price
Rs 198	Rs 190
EPS change FY11E/12E (%)	-11/ -13
Target Price change (%)	-14
Nifty	6,013
Sensex	20,005

Price Performance

(%)	1M	3M	6M	12M
Absolute	(7)	(1)	(3)	(9)
Rel. to Nifty	(7)	(11)	(16)	(26)

Source: Bloomberg

Relative Price Chart



Source: Bloomberg

Stock Details

Sector	Power
Bloomberg	NATP@IN
Equity Capital (Rs mn)	82455
Face Value(Rs)	10
No of shares o/s (mn)	8245
52 Week H/L	242/190
Market Cap (Rs bn/USD mn)	1639/36846
Daily Avg Volume (No of sh)	2989360
Daily Avg Turnover (US\$m)	13.9

Shareholding Pattern (%)

	S'10	J'10	M'10
Promoters	84.5	84.5	84.5
FII/NRI	2.9	2.6	2.6
Institutions	8.8	9.1	9.1
Private Corp	1.6	1.5	1.5
Public	2.2	2.3	2.3

Source: Capitaline

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- **Results disappoint (APAT down 2%) due to (1) grossing up ROE at MAT, (2) Kahalgaon/Farakka continue to report lower PAF (70%) on fuel constraints & (3) lower interest income**
- **Changed the grossing up to MAT rate frm earlier full tax rate; to hit profits by Rs10bn or 4% of core ROE from 28% to 24%**
- **Reduce earnings by 11-13% in FY11E/12E**
- **Valuations at 2.3x FY12E Book value, not attractive on core ROE of 24% (Earlier 28%); Lower target price to Rs190/Share; Downgrade to 'Hold'**

Results disappoint mainly due to grossing up at MAT rate

NTPC reported PAT of Rs21.1bn (down 2% yoy), below expectations of Rs21.5bn. After adjusting for one time items (depreciation write back, previous year sales and provisions), APAT stood at Rs18.4bn (down 2% yoy). This is despite company commercializing 1,480MW of capacity after Q2FY10. The lower than expected PAT is attributed to (1) grossing up of ROE by MAT rate (hit of Rs2.2bn in Q2FY10), (2) lower PAF at Kahalgaon and Farakka (hit of Rs0.9bn) and lower other income (Rs0.3bn). We understand that Kahalgaon STPS with a capacity of 2340MW or 7% of overall capacity, operated at 67% PLF and Farakka STPS with a capacity of 1600MW or 5% of overall capacity operated at 71% PLF. This is due to forced outages related to fuel constraints. Therefore, NTPC could not recover full capacity charges (approx. Rs6.5bn for both the plants put together). We estimate the loss in the range of Rs0.8-1.0bn. Though this looks to be a non recurring problem and should be resolved in near future. But the key issue is grossing up its ROE with MAT rate as against grossing up by full tax rate earlier. This we believe is significant negative as its going to impact its core ROE by 4%. The management guided for grossing up at MAT rate in foreseeable future.

Reduce earnings by 11-13% in FY11E/12E driven by MAT grossing up

We are reducing our earnings by 11% and 13% for FY11E and FY12E respectively driven by lower core ROE of 24% instead of 28% earlier. This is driven by grossing up at MAT rate (19%) instead of full tax rate earlier (33%). This has resulted in a hit of Rs10bn and Rs14bn to our FY11E and FY1 earnings post analyst meet. Our current earnings stand at Rs10/Share in FY11E and Rs11.1/Share in FY12E. We continue to build in capacity addition of 7040MW in FY10-FY12E. We have not factored merchant sale out of Korba and Farakka plants in FY11E and FY12E.

Core ROE of 24%; Valuations unattractive; downgrade to 'Hold'

The earnings cut have hit the FY12E Book by 2% to Rs87/Share. At CMP of Rs198, the stock is trading at 2.3x FY12E Book Value and 17.8x FY12E earnings. The valuations are not attractive now at 2.3x FY12E Book considering core ROE of 24% only. We downgrade the stock to 'Hold' rating. We have reduced our target price to Rs190/Share from Rs220/Share earlier. Based on its core ROE of 24% in FY12E, we have assigned multiple of 2.4x (cost of equity of 10%) to its core book of Rs602bn and multiple of 1x to its equity financed cash and equivalents of Rs133bn

Financial Snapshot

Rs Mn

YE-	Net	EBITDA	EPS	EPS	RoE	EV/				
Mar	Sales	(Core)	(%)	APAT	(Rs)	% chg	(%)	P/E	EBITDA	P/BV
FY09	412,169	98,239	23.8	82,742	10.0	6.8	14.7	20.3	18.5	2.9
FY10	470,426	131,404	27.9	84,806	10.3	2.5	14.8	18.5	14.2	2.6
FY11E	523,767	132,964	25.4	82,209	10.0	(3.1)	12.7	19.9	15.4	2.4
FY12E	602,985	163,178	27.1	91,852	11.1	11.7	13.2	17.8	14.0	2.3

Quarterly Results

Rs mn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)	YTD'09	YTD'10	YoY (%)
Revenue	105,087	111,837	123,534	129,445	129,893	23.6	0.3	225,114	259,338	15.2
Expenditure	-76,519	-78,184	-96,877	-99,579	-99,792	30.4	0.2	-164,789	-199,371	21.0
<i>as % of sales</i>	<i>-72.8%</i>	<i>-69.9%</i>	<i>-78.4%</i>	<i>-76.9%</i>	<i>-76.8%</i>			<i>-73.2%</i>	<i>-76.9%</i>	
Consumption of RM	-66,068	-67,672	-83,460	-87,023	-86,073	30.3	-1.1	-143,495	-173,096	20.6
<i>as % of sales</i>	<i>-62.9%</i>	<i>-60.5%</i>	<i>-67.6%</i>	<i>-67.2%</i>	<i>-66.3%</i>			<i>-63.7%</i>	<i>-66.7%</i>	
Power and Fuel	0	0	0	0	0			0	0	
<i>as % of sales</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>			<i>0</i>	<i>0</i>	
Other Mfg Expenses	0	0	0	0	0			0	0	
<i>as % of sales</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>			<i>0</i>	<i>0</i>	
Employee Cost	-5040	-5723	-7456	-6838	-7092	40.7	3.7	-10,944	-13,930	27.3
<i>as % of sales</i>	<i>-4.8%</i>	<i>-5.1%</i>	<i>-6.0%</i>	<i>-5.3%</i>	<i>-5.5%</i>			<i>-4.9%</i>	<i>-5.4%</i>	
Other expenditure	-5411	-4789	-5961	-5718	-6628	22.5	15.9	-10,350	-12,346	19.3
<i>as % of sales</i>	<i>-5.1%</i>	<i>-4.3%</i>	<i>-4.8%</i>	<i>-4.4%</i>	<i>-5.1%</i>			<i>-4.6%</i>	<i>-4.8%</i>	
EBITDA	28,568	33,653	26,657	29,866	30,101	5.4	0.8	60,325	59,967	-0.6
Depreciation	-6438	-6614	-7322	-6827	-5063	-21.4	-25.8	-12,566	-11,890	-5.4
EBIT	22,131	27,039	19,335	23,039	25,038	13.1	8.7	47,759	48,077	0.7
Other Income	7410	7792	6277	5850	6147	-17.0	5.1	15,173	11,997	-20.9
Interest	-5407	-3418	-4818	-5357	-5902	9.2	10.2	-9,854	-11,259	14.3
PBT	24,134	31,413	20,794	23,532	25,283	4.8	7.4	53,078	48,815	-8.0
Total Tax	-5378	-7763	-618	-5113	-6898	28.3	34.9	-12,387	-12,011	-3.0
Adjusted PAT	18755	23650	20176	18419	18385	-2.0	-0.2	40691	36804	-9.6
Extra ordinary items	2774	0	0	0	2688			2,774	2,688	
Reported PAT	21529	23650	20176	18419	21073	-2.1	14.4	43465	39492	-9.1
(Profit)/loss from JV's/Ass/MI	0	0	0	0	0			0	0	
PAT after MI	21529	23650	20176	18419	21073	-2.1	14.4	43465	39492	-9.1
Reported EPS	2.6	2.9	2.4	2.2	2.6	-2.1	14.4	5.3	4.8	-9.1

Margins (%)						(bps)	(bps)			(bps)
EBIDTA	27.2	30.1	21.6	23.1	23.2	-401	10	26.8	23.1	367
EBIT	21.1	24.2	15.7	17.8	19.3	-178	148	21.2	18.5	268
EBT	26.4	28.1	16.8	18.2	23.3	-304	514	23.6	18.8	476
PAT	17.8	21.1	16.3	14.2	14.2	-369	-8	18.1	14.2	388
Effective Tax rate	22.3	24.7	3.0	21.7	30.4	814	870	23.3	24.6	-127

Financials

Income Statement

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
Net Sales	412,169	470,426	523,767	602,985
<i>Growth (%)</i>	18.4	14.1	11.3	15.1
Expenditure	313,930	339,022	390,803	439,807
Raw Materials	271,106	294,627	340,035	378,334
Construction Exp	0	0	0	0
Employee Cost	24,631	24,124	26,975	31,414
Other Exp	18,192	20,271	23,794	30,058
EBITDA	98,239	131,404	132,964	163,178
<i>Growth (%)</i>	6.0	33.8	1.2	22.7
EBITDA margin (%)	23.8	27.9	25.4	27.1
Depreciation	23,645	26,501	26,299	35,077
EBIT	74,595	104,903	106,665	128,101
EBIT margin (%)	18.1	22.3	20.4	21.2
Other Income	30,510	25,671	22,583	19,253
Interest expenses	17,274	18,089	23,130	30,278
PBT	87,830	112,485	106,118	117,077
Tax	4,002	28,772	25,275	27,805
<i>Effective tax rate (%)</i>	4.7	24.6	23.5	23.2
Adjusted PAT	83,829	83,713	80,843	89,272
(Profit)/loss from JV's/Ass/MI	-1,087	1,093	1,367	2,580
Adjusted PAT after MI	82,742	84,806	82,209	91,852
<i>Growth (%)</i>	6.8	2.5	-3.1	11.7
Net Margin (%)	20.1	18.0	15.7	15.2
E/O items	-1,818	3,569	0	0
Reported PAT	80,924	88,375	82,209	91,852
<i>Growth (%)</i>	8.3	9.2	-7.0	11.7

Cash Flow

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
PBT (Ex-Other income)	54,416	91,476	84,902	100,404
Depreciation	23,645	26,501	26,299	35,077
Interest Provided	17,274	18,089	23,130	30,278
Other Non-Cash items	0	0	0	0
Chg in working cap	-12,794	-16,330	-6,348	-9,427
Tax paid	-9,668	-28,902	-25,275	-27,805
Operating Cashflow	72,873	90,834	102,708	128,526
Capital expenditure	-131,351	-101,731	-224,000	-302,355
Free Cash Flow	-58,478	-10,897	-121,292	-173,829
Other income	30,510	25,671	22,583	19,253
Investments	11,335	-9,251	-9,695	-17,516
Investing Cashflow	-89,506	-85,311	-211,112	-300,618
Equity Capital Raised	5,626	-3,253	0	0
Loans Taken / (Repaid)	73,772	32,292	129,920	190,484
Interest Paid	-17,274	-18,089	-23,130	-30,278
Dividend paid (incl tax)	-29,683	-31,268	-29,912	-33,031
Income from investments	-2,839	-5,434	-8,440	-11,656
Others	0	0	622	880
Financing Cashflow	29,602	-25,752	69,060	116,399
Net chg in cash	12,969	-20,229	-39,344	-55,692
Opening cash position	151,855	164,824	144,595	105,251
Closing cash position	164,824	144,595	105,251	49,559

Balance Sheet

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
Equity share capital	82,455	82,455	82,455	82,455
Reserves & surplus	510,606	558,028	603,874	654,500
Net worth	593,061	640,483	686,329	736,955
Minority Interest	0	0	0	0
Secured Loans	345,678	377,970	507,890	698,374
Unsecured Loans	0	0	0	0
Loan Funds	345,678	377,970	507,890	698,374
Net deferred tax liability	0	2,093	2,093	2,093
Total Liabilities	938,739	1,020,546	1,196,312	1,437,422
Gross Block	623,530	709,310	781,038	954,586
Less: Depreciation	294,153	320,654	346,953	382,029
Net block	329,377	388,656	434,085	572,556
Capital work in progress	264,049	280,000	432,272	561,079
Investment	137,727	148,071	159,132	179,228
Current Assets	311,361	308,158	287,360	259,212
Inventories	32,434	33,477	37,273	42,910
Sundry debtors	35,842	66,515	74,057	85,258
Cash & bank balance	164,824	144,595	105,251	49,559
Loans & advances	78,261	63,571	70,779	81,484
Other current assets	0	0	0	0
Current lia & Prov	106,886	107,582	119,780	137,897
Current liabilities	106,886	107,582	119,780	137,897
Provisions	0	0	0	0
Net current assets	204,475	200,576	167,579	121,315
Misc. exp & Def. Assets	3,111	3,243	3,243	3,243
Total Assets	938,739	1,020,546	1,196,312	1,437,422

Key Ratios

Y/E, Mar	FY09	FY10	FY11E	FY12E
Profitability (%)				
EBITDA Margin	23.8	27.9	25.4	27.1
Net Margin	20.1	18.0	15.7	15.2
ROCE	8.5	10.7	9.6	9.8
ROE	14.7	14.8	12.7	13.2
RoIC	21.3	24.0	20.7	19.9
Per Share Data (Rs)				
EPS	10.0	10.3	10.0	11.1
CEPS	12.8	12.8	12.4	14.4
BVPS	69.6	75.7	81.3	87.4
DPS	3.6	3.8	3.6	4.0
Valuations (x)				
PER	20.3	18.5	19.9	17.8
P/CEPS	15.6	15.5	16.0	13.8
P/BV	2.9	2.6	2.4	2.3
EV / Sales	4.4	4.0	3.9	3.8
EV / EBITDA	18.5	14.2	15.4	14.0
Dividend Yield (%)	1.8	1.9	1.8	2.0
Gearing Ratio (x)				
Net Debt/ Equity	0.3	0.4	0.6	0.9
Net Debt/EBITDA	1.9	1.8	3.0	3.9
Working Cap Cycle (days)	35	43	43	43

Recommendation History: NTPC – NATP IN

Date	Reports	Reco	CMP	Target
26/11/2010	NTPC Q1FY11 Result Update	Accumulate	202	220
02/06/2010	NTPC Q4FY10 Result Update	Accumulate	197	220
02/02/2010	NTPC Q3FY10 Result Update	Hold	208	204
26/10/2009	NTPC Q2FY10 Result Update	Reduce	215	204

Recent Research Reports

Date	Reports	Reco	CMP	Target
26/10/2010	Emco Q2FY11 Result Update	Reduce	64	60
20/10/2010	TRIL Q2FY11 Result Update	Accumulate	380	448
12/10/2010	Sintex Industries Q2FY11 Result Update	Hold	430	325
10/08/2010	HBL Power System Q1FY11 Result Update	Buy	31	43

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