

C O M P A N Y R E P O R T

JSW ENERGY LTD

Company Profile

JSW Energy Ltd (JSWEL) is a fast growing power services company that is part of the prestigious, \$4 Billion valued Jindal South West (JSW) group. The group has diversified interests in areas ranging from steel, energy, minerals and mining, aluminum, infrastructure and logistics, cement and information technology. Formed in the year 1994, as a joint venture between the JSW group and Tractebel S.A. of Belgium, JSW Energy commenced operations in the year 2000 as an Independent Power Producer (IPP), setting up a 260 MW power generating unit. The company was initially called 'Jindal Tractebel Power Company Ltd.', but after Tractebel S.A. sold their stake in 2001, the company was renamed as 'Jindal Thermal Power Company Limited'. The company secured its current name



'JSW Energy' once the JSW group secured a 100% stake in the company. The company has the distinction of being the first Independent Power Producer (IPP) to set up operations in the state of Karnataka, initially installing 2 units of 130 MW each, with both units generating power using corex gas and coal. In addition to power generation, the firm is also involved in power trading (playing the role of a power supplier to JSW Steel Ltd. and other Power Trading Corporations), power distribution, providing operation and maintenance services, mining and the manufacturing of super critical boilers. The company follows very strict environmental standards and its Environmental Management system (EMS) has been certified as ISO 14001 compliant by BVQI. JSW Energy is also an ISO 9001-2000 and ISO 18001 certified company.

BUY ON DIPS**CMP: Rs. 121.8** (closing price as on 13/05/2010)**Target: Rs 194 and Rs 219**

Business

Being a power services company, the main source of revenue for JSW Energy arises from power generation and power trading. However the firm is also involved in other services, primarily, the rendering of operation and maintenance services. In addition to those services, the company is also involved in a diversified range of joint venture agreements that focus on areas such as mining, manufacturing of equipment and power transmission.

Power Generation: The power generation business is without doubt the métier of JSW Energy, averaging around 83% of the total sales for the last 5 years (from FY06-FY10). The company has a rather strong expertise in this area, having been involved in the business since 2000. For a considerable period of time (till FY09), the company's source of power generation was limited to its 260 MW (2 X 135 MW) unit in Vijaynagar, Karnataka (JSWEL SBU 1). Through this plant alone, the firm was able to generate income to the tune of Rs. 1240 crores (in FY09). Chief among various reasons for this impressive performance is the exceptionally high PLF (Plant Load Factor) of the plant. The Plant Load Factor is the ratio of actual units of power generated by a plant, to the maximum power that could theoretically be generated by the power plant during any contract period. The 260 mw dual fuel (coal and gas) power plant's plant load factor has averaged 93.44% since its inception. This plant had also proved to be a financially beneficial enterprise as it has been exempt from income tax until 2013. In July 2009, the company added to its power generation portfolio by commencing the first of its 600 mw (1 X 300 MW) coal plant (JSWEL SBU II). This plant too is located in Vijaynagar. The second unit (2 X 300 MW) was operationalized in September 2009. In November 2009, the firm also started operations of the first unit of its 1080 MW (RWPL 1 X 135 MW) lignite power plant in Barmer,

Rajasthan, taking the total capacity to 995 mw (260 mw + 600 mw + 135 mw) by the end of fiscal year 2010. The company intends to add a further 2010 MW in fiscal year 2011, taking its total capacity to 3005 mw by the end of the year. JSWEL's big aim is to reach a target capacity of 11390 MW by 2015.

As far as its sales are concerned, the company secures its power generation revenues through a combination of long term PPAs (Power Purchase Agreements) and short term merchant power sales with various state-owned utilities, power trading companies and industrial consumers. The SBU 1 (260 MW) in Vijaynagar generates sales on a 10:90 long term PPAs to short term merchant power ratio. The SBU II (600 MW) in Vijaynagar, generates sales through an optimum combination of long term PPAs to short term trading while the first unit of the Barmer plant (1 X 135 MW) generates sales exclusively through long term contracts with the Rajasthan State Distribution Utilities.

Power Trading: The company has been in the power trading business since 2006 and it is carried out by its subsidiary-JSWPTC (JSW Power Trading Corporation). The Central Electricity Regulatory Commission (CERC) has granted the company with an 'F' category license, the highest license in India, for power trading. JSWPTC sells power of not only the JSWEL but from external power supplies as well. The power is sold to state utility boards through short-term power off-take arrangements, where the price is subject to rapid market demand fluctuations. The time period of these short-term arrangements range from several hours to upto 11 months.

Power Transmission: Power transmission is another power-related area that the firm has been involved in, rendered through yet another subsidiary JSWPTL (JSW Power Transco Limited). The other partner in the venture is the government unit-MSETCL (Maharashtra State Electricity Transmission Company Limited). Through its transmission lines the company transmits power from power generation units to

state and national grids. The company is currently in the process of constructing two 400 kV double circuit quad moose transmission lines in the state of Maharashtra (transmission line from Jaigad to New Koyna). The company is very upbeat about this sector and has bid for transmission projects in West Bengal, Jharkhand and Orissa.

Operation and Maintenance services: JSWEL also performs specialized operation and maintenance services, for its group company- JSWSL (JSW Steel Limited). The contract for the operation and maintenance services with JSWSL's 230 MW captive power plant is until March 2011 where JSWEL seeks to maximize operational performance and the availability of generation assets.

Equipment manufacture and Mining: Equipment manufacture and mining activities make up the remaining part of the company's business. Both these activities are conducted through joint ventures. In 2008, JSWEL signed a deal with Japanese conglomerate- Toshiba Corporation, for the design, engineering, manufacturing, assembling and sale of sub-critical and super-critical steam turbines and generators with capacities ranging from 500MW to 1000MW. However JSWEL's stake in the venture is only 20% so it is not expected to contribute much in terms of cost nor will it benefit much in terms of revenue. Production under Phase I would commence in January 2011 and initially, the unit would produce steam turbine and generator (STG) parts. By 2012, it would start manufacturing STG sets with a target production capacity of 3000 mega watt per annum by 2014. The JV is targeting sales of \$400 million (around Rs 1,840 crore) only by the end of 2015 fiscal. The company's mining activities are conducted in the state of Maharashtra and Orissa. The Maharashtra mining activity is carried out for the purpose of securing lignite for the (8X 135 MW) 1080 mw lignite plant in Ratnagiri, Maharashtra.

Sale of CERs: Occasionally the company is also able to secure revenue through the sale of carbon credits or CERs (Certified Emission Rights). In fiscal year 2008 it proved to be a considerable source of revenue with the firm garnering around Rs.328 crore. But revenue from this source is not of a recurring nature and the company's next opportunity through the CER option is likely to come from its Kutehr plant in Himachal Pradesh, which is only due to commence operations in fiscal year 2016.

Management: The Chairman and MD of JSW Energy is Mr. Sajjan Jindal while the joint MD and CEO is Mr. S.S. Rao. The management team of JSW Energy possesses extensive industrial experience, project management experience, and strong negotiation skills in PPA and fuel supply projects. This team has already overseen a number of projects since the company's inception in 2000 and this will aid them in their future dealings. However reports have suggested that there could be a change at the top of the organizational hierarchy with Mr. S.S. Rao, likely to retire in three months. It was reported that the company is in the process of looking for suitable replacements both within and outside the

organization. It remains to be seen if a change in the top management will have a significant impact on the long-term direction of the company. The company also has adequate internal controls and risk management protocols to ensure their competitive advantage in the industry. The company has complied with the corporate governance requirements of SEBI with regard to minimum number of independent directors (5 out of 9) and the presence of various committees.

Corporate Social Responsibilities: The company participates in a range of CSR activities as part of the JSW group. These activities are essentially carried out by 3 charitable trusts and the JSW foundation (the CSR wing of the JSW group) established by the JSW group. As part of its CSR activities JSW Energy also indulged in resources conservation, environment protection and enrichment and the development of local communities in areas in which the company is in operation.

Segment

While India possesses a range of admirable and distinct characteristics over other major developing nations, it definitely falls short on the power front. The Indian continent is characterized by intermittent power shortages that are threatening to make a severe dent on the industrial, infrastructure and economic progress of the country. India's power deficit currently stands at 10.2% (as at December 2009) and the limited participation of private players is another reason attributed to the inefficiencies in the power sector. Currently the Centre and State government together own and operate over 85% of the installed power capacity in India (State Electricity Boards account for 51% while Central Public Sector Units account for 32.6% and the remaining 16.6% is made up by the private sector). However the winds of change seemed to be blowing through the power sector, with the Government of India implementing a number of changes, such as encouraging more private participation, increasing competition in the sector and reducing aggregate technical and commercial losses. As per the projections of investment in infrastructure during the 11th Plan, the power sector is expected to attract 30.4% of the total \$581.68 billion projected investment in infrastructure during the 11th Plan. Meanwhile as part of its 'Power for All by 2012 project' the government has set a target of reaching a power generation capacity of 200,000 mw by 2012 from its present level of 143,000 mw. According to the 17th Electric power survey, May 2007 (EPS), India's peak demand is expected to grow at a CAGR of 7.6% over a period of 10 years (2007-2017) and would require a generating capacity of 300,000 mw by 2017 to cater to this demand, compared to an installed capacity of 132329 mw as on March 31 2007.

Power generating capacity in India is expected to move at a greater pace (7.2% for FY11E against 5.3% in FY10), with the figure expected to increase by 21355 mw in 2010-11. An increase in power generation and better realizations will see

the sales of power services entities increase. However many firms are resorting to capacity additions and have done so, using substantial debt. This will result in an increase in the depreciation and interest charge, and consequently cause some strain on the bottomline.

All in all the power sector is considered to be a rather lucrative sector with great prospects, mainly due to the prevalence of considerable and intermittent power supply deficits (thereby opening up greater servicing opportunities), a conducive government policy and superior growth potential.

Outlook and Scope

It would not be inappropriate to say that JSWEL is on the verge of embarking on, perhaps, the most exciting journey since its inception, as it increases its power generation capacity by three times in FY11, before crossing the 10000 mw level by 2014-2015 (11390 mw by 2015). All the while, from the year 2000, to the first half of 2009, it has had to rely on the power generating capacity of its highly efficient 260 mw dual fuel plant in Vijaynagar, Karnataka. However, in FY10 it was able to see the benefits of its second SBU (Strategic Business Unit) in Vijaynagar and a further 135mw from its Barmer unit, taking its total power generation capacity to 995 mw. FY11 could prove to be a massive year for the firm as it completes its 1200 mw Ratnagiri project in Maharashtra along with the operationalization of 7 of the 8 units of its 1080 MW lignite plant in Barmer. If the firm is able to implement all its projects on time, it should have a power generation capacity of over 3000mw by the end of FY11. While the following two years will see the company consolidate its status and improve the efficiencies of its new plants, FY15-FY16 in turn, has the potential to be another fruitful period, with a number of impressive and area-diverse projects, due to commence operations. The company intends to expand its units in Barmer and Ratnagiri, in addition to a hydroelectric 240 mw power project in Himachal Pradesh, a 1320 mw coal based project in Chhattisgarh, a 1600 mw coal based project in West Bengal and a 1620 mw coal based project in Jharkhand. The company is hoping to secure carbon credit benefits through its hydroelectric plant in Himachal Pradesh (Kutehr). The company has applied for 'mega power status' for its 1200 mw power project in Ratnagiri which will enable it to receive excise and custom duty requirements. However if their application is not successful and they don't receive 'mega power status' then they will incur additional expenditure to the tune of Rs.45000 million. So there is a potentially interesting trade-off lying at the heart of that project.

The management has stated that they will be investing Rs. 4000 crore for expanding its power generating capacity in FY11, out of which Rs.3000 crore will be funded by debt. The company has so far completed funding for 3200 MW and is looking for financial closure of its power projects in West Bengal and Chhattisgarh by October 2010.

Historically the firm has faced some difficulties in securing coal (which is the key raw material). Despite being involved in long term coal supply deals with Indonesian coal major- P T Sungai Belati, the company does not possess an efficient coal linkage facility unlike some of its other counterparts such as Tata Power and NTPC (National Thermal Power Corporation). However the situation is likely to change, as the firm recently acquired a 49.8% stake in Royal Bafokeng Capital (Proprietary) - a company that owns a stake in the South African Coal Mining Holding. This will most certainly enable it to secure coal on a more efficient basis consequently enabling the firm to ease the strain on its cost of production.

Lately the company has been striving to increase its presence in the power trading and power transmission sectors. As far as power trading is concerned, the company is at the mercy of fluctuating prices, where prices soar to around Rs.14 per unit during the summer, all the way up til June, before they ease off and decline to as low as Rs.2 per unit by December. Power transmission is not an area of strength for JSWEL, but it is striving to make an impression in the sector. Power Grid Corporation is the big player in this business and JSWEL has a long way to go before it can compete with the latter. November 2010 will see the company commission a 400 kV transmission line in Maharashtra while it also has transmission projects in Orissa, Jharkhand and West Bengal lined up for the long-term future.

To complete its status as a comprehensive power services provider, the firm now wants to get into the power distribution business, particularly in the Western region of India as it has power plants in that area.

Financials

(In crores)	FY10	FY11E	FY12E	FY13E
Sales	2336.40	6106.78	8002.35	10672.70
PAT	745.59	1799.97	2309.37	3004.29
EPS	4.54	10.97	14.08	18.31
P/E	26.79	11.09	8.64	6.64

Concerns

JSWEL's high debt equity ratio of close to 4 is a matter of concern as it means severe pressure on the bottomline. The firm employs a trademark 75:25 debt to equity funding for most of its projects and this is likely to continue all the way up to 2015, as the company has set a target of reaching a 11390 MW capacity by that year. Nevertheless the high debt levels are somewhat justifiable as the power business is a capital intensive business and superior revenues in the future should more than compensate for the strain caused by the interest payments. Besides the company also face some legal issues

with regard to its Ratnagiri plant in Maharashtra and that has been lingering for quite some time now.

Valuation

JSW Energy is considered to be one of the fastest growing power sector companies and its historical sales and profit growth rates provide ample proof of this fact. From FY06-FY10 the sales of the company grew at an impressive CAGR (Cumulative Annual Growth Rate) of 44% even as its profits grew at a much superior 58%. Going forward, these growth rates are likely to improve with greater capacity additions, however the profits (unlike the historical trend) are likely to grow at a rate lower than the sales growth rate. From FY10-FY13 the sales have been forecasted to increase by 65% (CAGR), as the company increases its power generation capacity from 995 MW to 3140MW. By FY11-FY12, The company's new 400 Kv transmission line in Jaigad, Maharashtra will also start contributing to the top line. JSWEL currently provides operation and maintenance services to JSW Steel where it receives income to the tune of around Rs.17.5 crores on a yearly basis. However this contract is due to expire by the end of 2011 and it remains to be seen if it will be renewed. If not, revenues may not increase as much as initially forecasted for FY12 and FY13. Notwithstanding the renewal of the operation and maintenance service agreement with JSW Steel, revenues from FY12 and FY13 are not expected to increase manifold, as there are no major capacity additions forecasted for those years (sales growth rate of 31% and 33% for FY12 and FY13 respectively) and sales will increase mainly on account of an improving PLF figure and revenue from its power trading and power transmission business. The big year will be FY11, where the company increases its capacity three-fold, consequently resulting in a 161% increase in the top line. Profits for that year will grow at a slightly lower 141%, easing off in FY12 and FY13 with profit growth rates of 28% and 30% respectively. As mentioned before, traditionally, the profits have grown at a much superior rate to its sales. This was mainly due to the fact that there were no major capacity additions, (resulting in a moderately low depreciation figure) along with an optimal debt position (resulting in low interest payments). However, this trend is likely to change as the company goes on a capacity addition spree. Greater capacity additions from 995 mw to 3140 mw will result in a superior depreciation figure. Besides all of JSWEL's projects have been funded (and will be funded) using a debt equity ratio of 75:25 resulting in exorbitant interest payments up till 2015. Both these factors will see, the profits growing at a rate lower than the sales. The profit margin which stood at 32% at the end of FY10 will decrease to 29.4% in FY11, 28.8% in FY12 and 28% in FY13. **At a CMP of Rs.121.8, the stock is trading at 11 times its FY11E earnings, 8.6 times its FY12E earnings and 6.6 times its FY13E earnings.**

Investment Rationale

What's interesting about JSW Energy's journey so far, is that despite being involved in the power generation business since 2000, it did not increase its capacity until 2009. From 2000 to 2009, its sales from power generation emanated from its 260 mw dual gas plant in Vijaynagar. While the company's decision not to increase its capacity until 2009 remains a matter of conjecture, one would like to believe that the company was only laying the groundwork for its future projects, even as it developed a rigorous and informed impression on the power sector in India. In FY09, the 260 mw power plant (with a superior PLF of 97.3%) was able to generate sales to the tune of Rs.1240 crore. Since then, the company has added a further 735 mw in FY10 and is due to take this capacity further by adding 3005 mw in FY11 before touching 11390 mw by 2015. So if a 260 mw plant is capable of generating sales worth Rs.1200 crore, one can only imagine what the sales figure with a 3005 mw capacity and a 11390 mw capacity will be. Besides the JSW Energy team is known to be extremely efficient in the operation of their plants, generating a 10 year average PLF of 93.44% for its 260 mw Vijaynagar plant (In FY10, its 260 mw Vijaynagar plant had a PLF of 100% while its 600 mw Vijaynagar plant had a PLF of 93.8%). Enormous capacity additions coupled with superior executing skills should see the revenues of the firm shoot up (forecasted to grow by 65% over the next three years, with a sales growth rate of 161% from FY10-FY11). Moreover, strategically, all its power units are located in areas where there is ample power shortage and fuel linkage is easier. Previously the firm along with its group company-JSW Steel, did face some difficulties in the procurement of coal, as a considerable proportion of its coal supply comes from an Indonesian coal entity (PT Sungai Belati). However in April, JSWEL secured a 59.8% stake in a South African coal mining entity, and this will definitely ease the pressure that the company had previously faced in the procurement of coal. Ease of access to coal will most certainly reflect favorably on the cost of production.

While power generation continues to be its forte, the firm is making conscious efforts to strengthen its profile as a comprehensive power services organization, by developing its power transmission business and stating its intention to tap the Western region of India for power distribution purposes. The company is also looking to delve deep into the power trading business but revenues from this source are subject to volatility throughout the year as sales are made on a short term merchant trading basis.

The company is also involved in a number of joint venture agreements particularly for its mining business and the manufacturing of equipment. Despite only having a 20% stake in the turbine manufacture joint venture with Toshiba, JSWEL should benefit through the former's Japanese expertise.

Perhaps one of the most reassuring facts of JSW Energy is that it is backed by a very prestigious and diversified group. Being part of such a diversified and established business conglomerate not only provides a degree of insurance to JSWEL, but also enables it to be less risk averse and engage in projects that smaller players in the energy and power sector cannot pursue. Moreover it receives synergy benefits from other entities that are a part of the group particularly JSW

Steel for which it supplies power and receives among other things, fuel, power evacuation and off-take arrangements.

Considering that the stock has multi-bagger properties, it should serve as a good source of investment over the next 5 years. However based on the FY11E earnings, FY12E earnings and FY13E earnings we recommend accumulation of the stock with 1-2 year targets of Rs.194 and Rs.219.

R E F E R E N C E

Power generation projects of JSW ENERGY LIMITED

PLANT	LOCATION	UNITS & CAPACITY	FUEL	STATUS	PERIOD OF COMMENCEMENT
JSWEL SBU1*	Vijaynagar, Karnataka	260 MW (2 x 135 MW)	Dual (Coal & Gas)	Under operation	2000
JSWEL SBU 2, Unit 1 & 2	Vijaynagar, Karnataka	600 MW (2 x 300 MW)	Imported coal	Under operation	Unit 1- July 2009 & Unit 2- September 2009
RWPL Unit 1** Phase 1	Barmer, Rajasthan	1 x 135 MW	Lignite	Under operation	November 2009
RWPL Unit 2- 8 Phase 1	Barmer, Rajasthan	945 MW (7 x 135 MW)	Lignite	Under construction	Between May 2010 to February 2011
JSWERL*** SBU1	Ratnagiri, Maharashtra	1200 MW (4 x 300 MW)	Imported coal	Under construction	Between May 2010 to December 2010
JSWEL Kutehr	Kutehr, Himachal Pradesh	240 MW (3x 80 MW)	Hydroelectric	Under implementation	January 2013 to December 2015
RWPL Phase 2	Barmer, Rajasthan	270 MW (2 x 135 MW)	Lignite	Under implementation	January 2013 to December 2015
JSWERL SBU2	Ratnagiri, Maharashtra	3200 MW (4 x 800 MW)	Imported coal	Under implementation	August 2014 to August 2015
JSWEL Chhattisgarh	Raipur, Chhattisgarh	1320 MW (2 x 660 MW)	Domestic coal	Under development	August 2014 to August 2015
JSWEL West Bengal	Salboni, West Bengal	1600 MW (2 x 800MW)	Domestic coal	Under development	August 2014 to August 2015
JSWEL Jharkhand	Ranchi, Jharkhand	1620 MW (2 x 660 MW, 1 x 300 MW)	Domestic coal	Under development	August 2015

* JSWEL SBU1: JSW Energy Limited, Strategic Business Unit 1

** RWPL Unit 1: Raj West Power Limited 1

*** JSWERL : JSW Energy (Ratnagiri) Limited

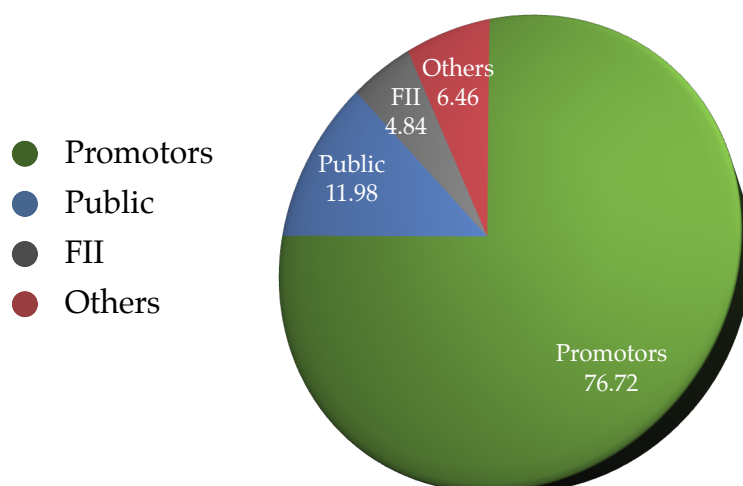
Major Investors

Life Insurance Corporation of India (LIC), ICICI Bank, Indus Capital Group Ltd., Steel Traders Limited, Eton Park International Up, Credit Suisse Singapore, Deutsche Securities Mauritius, Reliance Capital Trustee Limited.

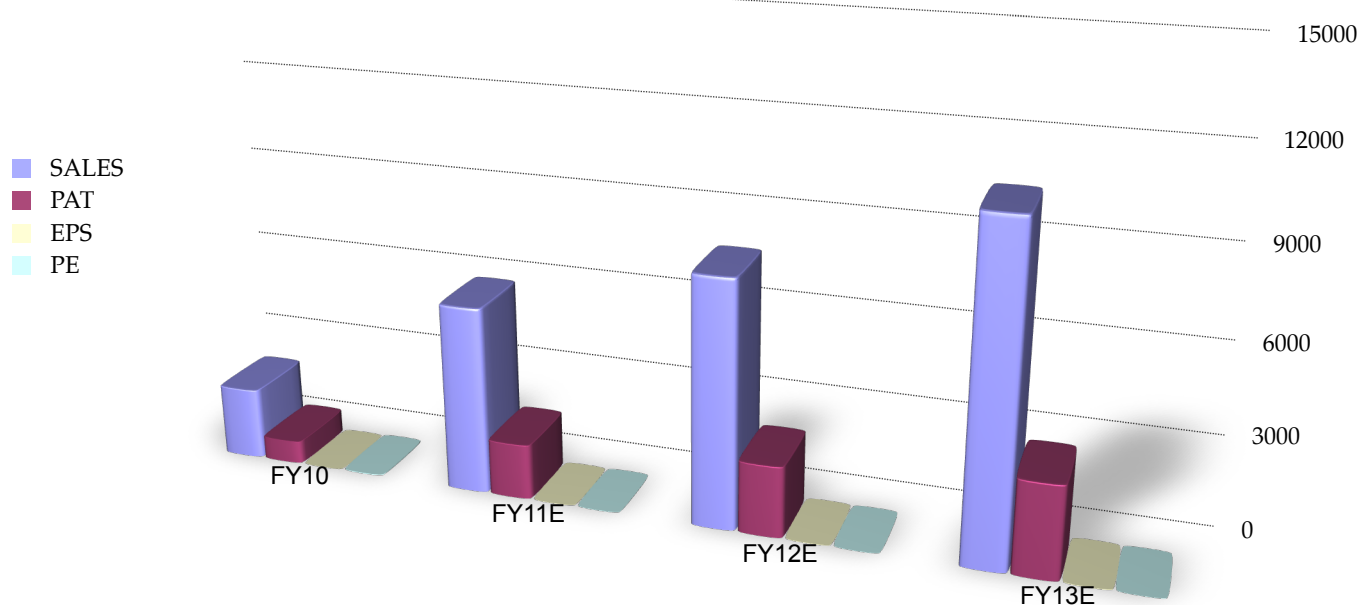
Key Indicators			
EPS (TTM)	5.16	Face Value	Rs.10
P/E (with TTM – EPS)	23.46	Equity Capital	Rs.1640.06 Cr
Industry P/E	26.23	Management	PRIVATE (INDIAN)
Book Value	Rs. 32.72	NSE Code	JSWENERGY
P/B	3.72	BSE Code	533148
Beta	1.09	ISIN Code	INE121E01018
Debt -Equity	3.96		

Share Holding Pattern (Dec 2009)	
Promoters	76.72%
Public	11.98%
FII	4.84%
Others	6.46%
Total	100.00

Share holding pattern



Sales, PAT, EPS & PE



JSW vs Nifty



By Krishnan Thampi K and Amar Chandramohan, Hedge Equities Ltd

Hedge Equities Ltd
12th Floor, M.M. Tech Towers,
Kaloor, Kochi 682 017

Tel: 0484 3040400 to 429

Fax: 0484 3040404

info@hedgeequities.com

www.hedgeequities.com



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