

Reimbursement of water-cess aids a seasonally good quarter; project execution lags

- **NHPC reported a better than estimated 2QFY12 numbers with revenues of Rs. 19.8bn and a PAT of Rs. 9.67bn**, a substantial increase both on a qoq basis as well as on a yoy basis.
- The Company booked a Rs. 4,637mn revenues as CERC allowed reimbursement of the water-cess being paid to J&K for the Salal (690MW) and Uri I (480MW) projects, though this amount has not been billed and collected from the beneficiary states (J&K, UP, Punjab, Haryana, Himachal Pradesh, Chandigarh, New Delhi and Rajasthan). The Company has paid a total of Rs. 5,466mn as water-cess so far.
- As the Company has contested this new water-cess in J&K's High Court it is unclear whether the amount will be recovered from the beneficiary states. Also, if the concerned EBs do not accept the higher tariffs it is likely that the additional revenues booked and the corresponding profits are at risk. Thus, if NHPC loses the case against J&K and is unable to recover the cost from beneficiary states it faces the double-whammy of higher costs with no pass-through.
- There was also a Rs. 1,231mn booked towards interest income from state EBs for tariff arrears. Adjusted for these non-recurring items the quarter's revenues comes to Rs. 13.95bn which is a ~9% yoy growth
- Generation was high during the quarter due to the monsoon months of 2QFY12 generating 7,086mn units (vs. 7,167mn in 2QFY11 and 6,284mn in 1QFY12). Adjusted EBITDA margin remained low at 74% vs. 82% in 2QFY11 primarily because of the water-cess being paid to the J&K government. Consequently the other expenditure was high yoy (Rs. 3,256mn vs. Rs. 899mn in 2QFY11); consequently adjusted PAT coming-in at Rs. 5,874mn, a 15% yoy drop.
- Execution for the ~1,300MW of plants under construction has lagged with the expected CoD timelines now stretching beyond FY12E. Only Chutak (44MW) expected to be commissioned in 3QFY12, Uri II (240MW) in 3QFY12 and Chamera III (231MW) in 4QFY12 will be likely be commissioned in FY12. While Nimmo-Bazgo, Parbati III and Teesta Low Dam III stand postponed to FY13. We view such persistent delays a key downside risk for the company.

Though we like NHPC's high quality balance sheet and the strong ability to fund growth aspirations from accruals, constant delays in project execution imply that the quantum improvement in RoE (>11%) is possible only after FY13E. Also an unfavorable outcome in the dispute with J&K government can likely dent margins going forward, which make us maintain our negative stance on the stock. We value it at 1.0x FY13E P/ABV (45% discount to NTPC), yielding a target price of Rs. 25/ share (earlier Rs. 28). **Retain Add / Underperform.**

Financial summary - Consolidated

| Year | Revenues (Rs. mn) | EBITDA (Rs. mn) | PAT (Rs. mn) | BV (Rs.) | P/BV(x) |
|-------|-------------------|-----------------|--------------|----------|---------|
| FY11 | 51,437 | 42,876 | 23,162 | 21.3 | 1.2 |
| FY12E | 59,502 | 42,702 | 23,500 | 23.2 | 1.1 |
| FY13E | 63,275 | 45,686 | 25,839 | 25.2 | 1.0 |

2QFY12 Update

| Date | Nov 1, 2011 |
|------|-------------|
|------|-------------|

Market Data

| | |
|-------------------|-----------|
| SENSEX | 17447 |
| Nifty | 5246 |
| Bloomberg | NHPC IN |
| Shares o/s | 12,301mn |
| Market Cap | Rs. 301bn |
| 52-wk High-Low | 32-22 |
| 3m Avg. Daily Vol | Rs. 97mn |
| Index member | BSE100 |

Latest shareholding (%)

| | |
|--------------|------|
| Promoters | 86.4 |
| Institutions | 4.8 |
| Public | 8.8 |

Stock performance (%)

| | 1m | 3m | 12m |
|--------|----|-----|------|
| NHPC | 4% | -2% | -22% |
| Sensex | 6% | -4% | -15% |
| BSE100 | 5% | -4% | -17% |

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| | | | |
|---------------|---------------|-----------------|---------------------|
| CMP | Rs. 25 | Absolute | Add |
| Target | Rs. 25 | Relative | Underperform |

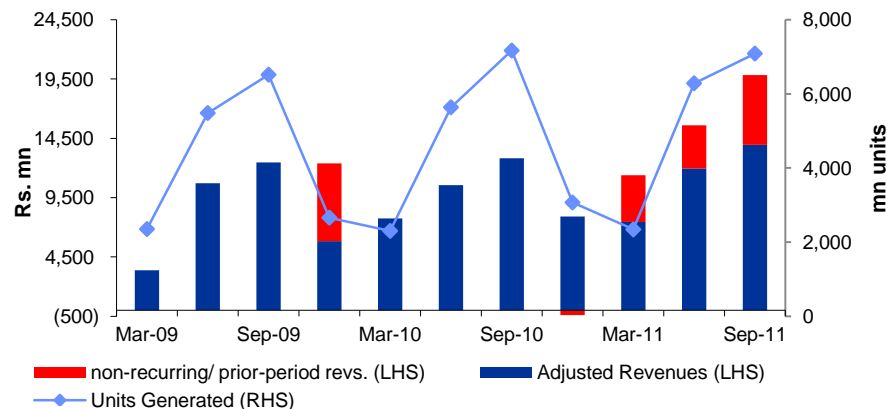
| Quarterly Financial Results | | | | | | | | |
|----------------------------------|---------------|---------------|------------|---------------|------------|---------------|---------------|---------------|
| Rs. mn \ Period | 30-Sep-11 | 30-Sep-10 | YoY Growth | 30-Jun-11 | QoQ Growth | FY11 | FY12E | Annual Growth |
| Net Sales from generation | 18,307 | 12,404 | 48% | 14,314 | 28% | 49,650 | 56,718 | 14% |
| Other Operating Income | 1,509 | 409 | 269% | 1,291 | 17% | 1,787 | 2,784 | 56% |
| Employee Cost | 2,046 | 1,321 | 55% | 2,058 | -1% | 7,697 | 7,850 | 2% |
| Other Expenses | 3,256 | 899 | 262% | 3,165 | 3% | 7,429 | 7,949 | 7% |
| Prior Period Adjustments | 352 | 0 | | (80) | -541% | (6,565) | 1,000 | |
| Total Expenditures | 5,654 | 2,220 | 155% | 5,143 | 10% | 8,561 | 16,800 | 96% |
| EBITDA | 14,161 | 10,593 | 34% | 10,463 | 35% | 42,876 | 42,702 | 0% |
| Other income | 1,812 | 1,711 | 6% | 2,379 | -24% | 8,071 | 8,475 | 5% |
| Depreciation | 2,234 | 2,677 | -17% | 2,258 | -1% | 11,666 | 9,667 | -17% |
| Interest & Finance Charges | 883 | 1,091 | -19% | 865 | 2% | 6,709 | 8,528 | 27% |
| PBT | 12,856 | 8,537 | 51% | 9,718 | 32% | 32,572 | 32,982 | 1% |
| Taxes | 3,191 | 1,635 | 95% | 1,808 | 77% | 7,945 | 8,246 | 4% |
| PAT | 9,665 | 6,902 | 40% | 7,911 | 22% | 23,162 | 23,500 | 1% |
| EPS (in Rs.) | 0.79 | 0.56 | 40% | 0.64 | 22% | 1.88 | 1.91 | 1% |

NHPC

Quarterly Performance

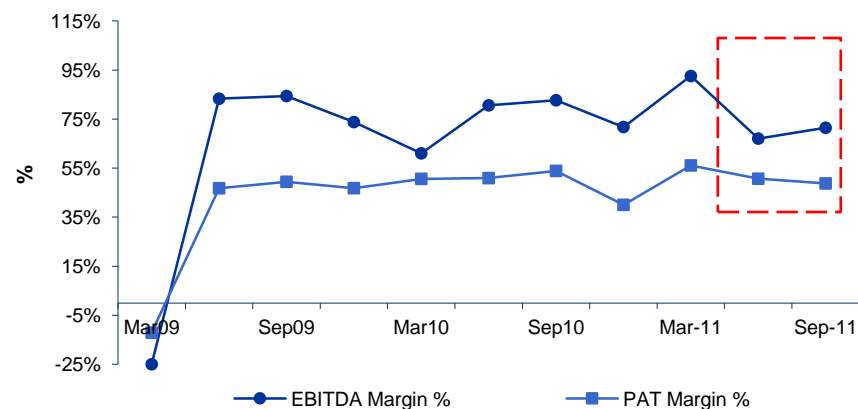
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|---------------|---------------|-----------------|---------------------|
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Seasonal higher generation & prior period items increase revenues



Source: Company, Spark Capital Research

EBITDA margins fall due to the water-cess expense



Source: Company

Adjustments for prior-period/ non-recurring items

| Rs. mn | 2QFY12 |
|--|---------------|
| Reported Sales | 19,817 |
| Less: Revenues recognized for payment of water-cess in prior periods | 4,637 |
| Less: Interest income on Tariff arrears | 1,231 |
| Adjusted Sales | 13,949 |
| Reported Total Expenses | 5,654 |
| Less: Cost associated with the water cess revenues for prior periods | 2,055 |
| Adjusted Expenses | 3,599 |
| Adjusted EBITDA | 10,351 |
| Reported Other Income | 1,812 |
| Reported Depreciation | 2,234 |
| Reported Interest Cost | 863 |
| Adjusted PBT | 9,065 |
| Reported Taxes | 3,191 |
| Adjusted PAT | 5,874 |

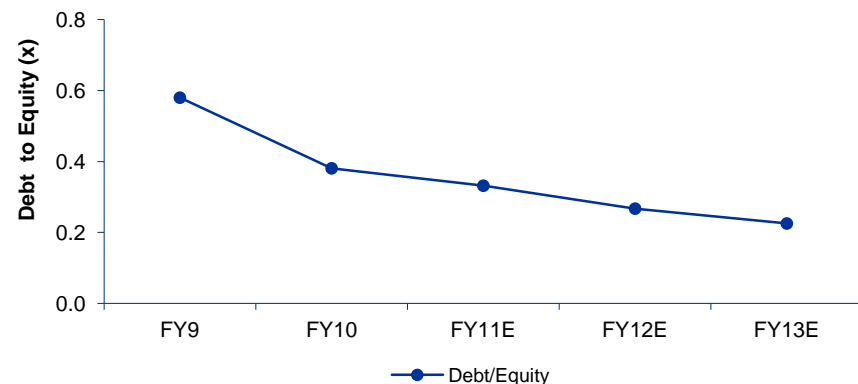
Actual vs. Estimates (Standalone)

| 2QFY12 | Actual (adjusted) | Spark Estimate | Delta |
|--------------|-------------------|----------------|---------|
| Adj. Revenue | 13,949 | 13,829 | 0.87% |
| Adj. EBITDA | 10,351 | 9,265 | 11.71% |
| Margin (%) | 74.2% | 67.0% | 720bps |
| Adj. PAT | 5,874 | 5,917 | -0.73% |
| Margin (%) | 42.1% | 42.8% | (68bps) |
| EPS | 0.48 | 0.48 | -0.73% |

All figures in Rs. mn, except EPS, which is in Rs.

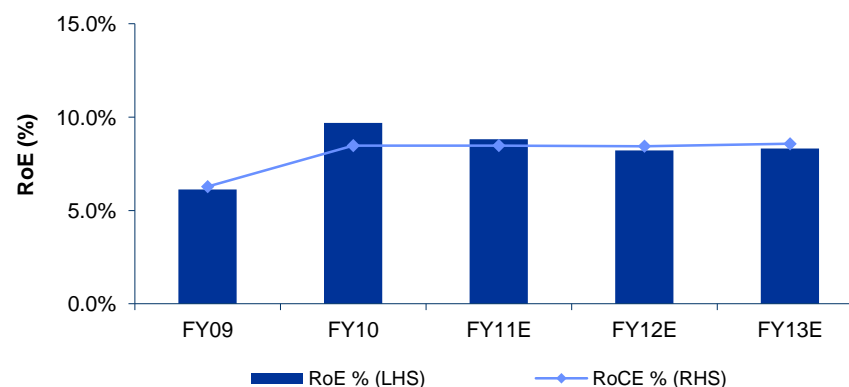
| | | | |
|---------------|---------------|-----------------|---------------------|
| CMP | Rs. 25 | Absolute | Add |
| Target | Rs. 25 | Relative | Underperform |

Debt-equity ratio is at a comfortable level



Source: Company, Spark Capital Research

Capital efficiencies to remain flat



Source: Company, Spark Capital Research

Key estimate revision (Consolidated)

| | FY12E | | | FY13E | | |
|------------|--------|--------|--------|--------|--------|--------|
| | Old | New | Change | Old | New | Change |
| Revenue | 59,502 | 59,502 | 0% | 63,275 | 63,275 | 0% |
| EBITDA | 42,702 | 42,702 | 0% | 45,686 | 45,686 | 0% |
| Margin (%) | 71.77% | 71.77% | | 72.20% | 72.20% | |
| PAT | 23,500 | 23,500 | 0% | 25,839 | 25,839 | 0% |
| Margin (%) | 39.49% | 39.49% | | 40.84% | 40.84% | |
| EPS | 1.9 | 1.9 | 0% | 2.1 | 2.1 | 0% |

All figures in Rs. mn, except EPS, which is in Rs.

1 year forward P/BV



Source: Bloomberg, Spark Capital Research

NHPC

Financial Summary

CMP

Rs. 25

Absolute

Add

Target

Rs. 25

Relative

Underperform

| Abridged Financial Statements (Consolidated) | | | | |
|--|----------------|----------------|----------------|----------------|
| Rs. mn | FY10 | FY11E | FY12E | FY13E |
| Profit & Loss | | | | |
| Revenues | 52,273 | 51,437 | 59,502 | 63,275 |
| EBITDA | 41,291 | 42,876 | 42,702 | 45,686 |
| Other Income | 6,473 | 8,071 | 8,475 | 8,354 |
| Depreciation | 12,827 | 11,666 | 9,667 | 9,500 |
| EBIT | 34,936 | 39,281 | 41,510 | 44,540 |
| PBT | 27,543 | 32,572 | 32,982 | 35,888 |
| PAT after MI | 21,757 | 23,162 | 23,500 | 25,839 |
| Balance Sheet | | | | |
| Net Worth + MI | 266,968 | 291,595 | 316,332 | 343,248 |
| Total debt and grants | 163,515 | 168,901 | 170,878 | 173,371 |
| Income from Advance Against Dep. | 15,398 | 15,076 | 15,076 | 15,076 |
| Deferred Tax | 2,521 | 2,774 | 2,774 | 2,774 |
| Total Networth & Liabilities | 448,402 | 478,345 | 505,059 | 534,468 |
| Gross Fixed assets | 280,120 | 286,775 | 371,750 | 371,750 |
| Net fixed assets | 223,020 | 218,009 | 293,317 | 283,818 |
| CWIP | 140,620 | 155,310 | 96,208 | 123,901 |
| Investments | 33,455 | 43,194 | 43,194 | 43,194 |
| Inventories | 2,278 | 2,170 | 2,189 | 2,320 |
| Sundry Debtors | 15,338 | 22,166 | 13,985 | 14,875 |
| Cash and bank balances | 61,895 | 72,201 | 86,385 | 96,039 |
| Loans & Advances | 18,847 | 19,760 | 19,333 | 20,560 |
| Current liabilities | 47,047 | 54,465 | 49,553 | 50,239 |
| Net current assets | 51,311 | 61,832 | 72,340 | 83,555 |
| Miscellaneous Exp. Not written off | (4) | 0 | 0 | 0 |
| Total Assets | 448,402 | 478,345 | 505,059 | 534,468 |
| Cash Flows | | | | |
| Cash flows from Operations | 42,389 | 43,039 | 46,608 | 43,507 |
| Cash flows from Investing | (34,220) | (31,084) | (25,873) | (27,694) |
| Cash flows from Financing | 156,121 | (1,650) | (6,551) | (6,159) |

| Key metrics | | | | |
|-----------------------------------|---------|--------|--------|--------|
| | FY10 | FY11E | FY12E | FY13E |
| Growth ratios | | | | |
| Sales | 50.4% | -1.6% | 15.7% | 6.3% |
| EBITDA | 78.7% | 3.8% | -0.4% | 7.0% |
| PAT | 83.6% | 6.5% | 1.5% | 10.0% |
| Margin ratios | | | | |
| EBITDA | 79.0% | 83.4% | 71.8% | 72.2% |
| PAT | 41.6% | 45.0% | 39.5% | 40.8% |
| Performance ratios | | | | |
| RoA | 5.3% | 5.0% | 4.8% | 5.0% |
| RoE | 9.7% | 8.8% | 8.2% | 8.3% |
| RoCE | 8.5% | 8.5% | 8.4% | 8.6% |
| Total Assets Turnover (x) | 0.12 | 0.11 | 0.12 | 0.12 |
| Fixed Assets Turnover (x) | 0.23 | 0.24 | 0.20 | 0.22 |
| Working capital Turnover (x) | 1.02 | 0.83 | 0.82 | 0.76 |
| Financial stability ratios | | | | |
| Net Debt to Equity (x) | 0.38 | 0.33 | 0.27 | 0.23 |
| Current ratio (x) | 2.09 | 2.14 | 2.46 | 2.66 |
| Working capital days | 358 | 439 | 444 | 482 |
| Inventory & Debtor days | 121 | 170 | 98 | 98 |
| Creditor days | 324 | 381 | 300 | 286 |
| Interest cover (x) | 4.7 | 5.9 | 4.9 | 5.1 |
| Valuation metrics | | | | |
| Fully Diluted shares (mn) | 12,301 | 12,301 | 12,301 | 12,301 |
| Fully diluted M. Cap (Rs.mn) | 306,288 | | | |
| Fully Diluted EPS (Rs.) | 1.77 | 1.88 | 1.91 | 2.10 |
| P/E (x) | 14.1 | 13.2 | 13.0 | 11.9 |
| EV (Rs.mn) | 429,537 | | | |
| EV/ EBITDA (x) | 10.4 | 10.0 | 10.1 | 9.4 |
| BV/ share (Rs.) | 18.2 | 21.3 | 23.2 | 25.2 |
| Price to BV (x) | 1.4 | 1.2 | 1.1 | 1.0 |

| | | | |
|---------------|---------------|-----------------|---------------------|
| CMP | Rs. 25 | Absolute | Add |
| Target | Rs. 25 | Relative | Underperform |

Absolute Rating Interpretation

| | |
|---------------|---|
| BUY | Stock expected to provide positive returns of > 15% over a 1-year horizon |
| ADD | Stock expected to provide positive returns of <=15% over a 1-year horizon |
| REDUCE | Stock expected to fall <=15% over a 1-year horizon |
| SELL | Stock expected to fall >15% over a 1-year horizon |

Relative Rating Interpretation

| | |
|---------------------|--|
| OUTPERFORM | Stock expected to outperform sector index /sector peers in our coverage |
| UNDERPERFORM | Stock expected to underperform sector index/ sector peers in our coverage |

Recommendation History

| Date | CMP | Target price | Absolute Rating | Relative Rating |
|-----------|-----|--------------|-----------------|-----------------|
| 10-Aug-11 | 25 | 28 | ADD | UPF |
| 01-Jun-11 | 25 | 28 | ADD | UPF |
| 21-Feb-11 | 25 | 29 | BUY | OPF |
| 10-Jan-11 | 28 | 38 | BUY | OPF |
| 02-Nov-10 | 31 | 38 | | OPF |

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