Company

4 August 2010 | 9 pages

Adani Power (ADAN.BO)

Equity

1QFY11: Operationally Weak Quarter

- **1QFY11 PAT grew 16% QoQ** — Adani Power's 1QFY11 PAT at Rs1.15bn grew 16% QoQ driven primarily by Mundra Unit 2 (330 MW) being operational for full quarter. Unit 2 was only partially operational in 4QFY10. 1QFY11 results also benefited from seasonally high merchant power prices (~Rs6.75/kwh) which led to higher ASP of Rs3.43/kwh v/s Rs3.27/kwh in 4QFY10.
- **Operationally lower than expected** — Mundra Unit 1&2 achieved average PLF of 80% during 1QFY11 which was below CIRA estimate of 90% PLF for FY11.
- **Mundra Unit 3 (330MW) synchronized** — Adani Power has synchronized Mundra Unit 3 (330MW) on July 30, 2010 v/s CIRA estimate of April 30, 2010. Unit 4 (330MW) is now expected to be synchronized by October 2010 v/s CIRA estimate of June 30, 2010.
- **Fuel and O&M costs** — 1QFY11 fuel cost at Rs0.95/kwh has declined from Rs1.05/kwh in 4QFY10 and Rs1.45/kwh in 3QFY10. 1QFY11 O&M cost at Rs0.29 /kwh has increased from Rs0.23/kwh in 4QFY10 and Rs0.16/kwh in 3QFY10.
- **Maintain Sell** — Our Rs106 target price values 9,240MW of capacity. We maintain sell given downside to current market price.

Sell/Medium Risk	3M
Price (04 Aug 10)	Rs137.00
Target price	Rs106.00
Expected share price return	-22.6%
Expected dividend yield	0.0%
Expected total return	**-22.6%**
Market Cap	Rs298,665M
	US$6,470M

Price Performance (RIC: ADAN.BO, BB: ADANI IN)

Statistical Abstract

Year to 31 Mar	Net Profit (RsM)	Diluted EPS (Rs)	EPS growth (%)	P/E (x)	P/B (x)	ROE (%)	Yield (%)
2008A	-72	-0.13	na	nm	5.9	na	0.0
2009A	-26	-0.01	89.3	nm	11.1	-0.1	0.0
2010E	1,454	0.67	na	nm	5.5	3.8	0.0
2011E	9,139	4.19	528.3	32.7	4.7	15.5	0.0
2012E	46,768	21.45	411.8	6.4	2.7	53.8	0.0

Source: Powered by dataCentral

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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

Fiscal year end 31-Mar	2008	2009	2010E	2011E	2012E
Valuation Ratios					
P/E adjusted (x)	nm	nm	nm	32.7	6.4
EV/EBITDA adjusted (x)	na	nm	145.0	25.3	6.4
P/BV (x)	5.9	11.1	5.5	4.7	2.7
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Per Share Data (Rs)					
EPS adjusted	-0.13	-0.01	0.67	4.19	21.45
EPS reported	-0.13	-0.01	0.67	4.19	21.45
BVPS	23.26	12.35	24.98	29.17	50.63
DPS	0.00	0.00	0.00	0.00	0.00
Profit & Loss (RsM)					
Net sales	0	0	4,664	32,483	119,226
Operating expenses	-72	-28	-2,476	-16,842	-45,289
EBIT	**-72**	**-28**	**2,189**	**15,641**	**73,937**
Net interest expense	0	0	-347	-4,631	-14,305
Non-operating/exceptionals	0	0	0	0	0
Pre-tax profit	**-72**	**-28**	**1,842**	**11,010**	**59,632**
Tax	0	0	-388	-1,872	-10,135
Extraord./Min.Int./Pref.div.	0	2	0	0	-2,729
Reported net income	**-72**	**-26**	**1,454**	**9,139**	**46,768**
Adjusted earnings	-72	-26	1,454	9,139	46,768
Adjusted EBITDA	-72	-28	2,565	17,559	80,048
Growth Rates (%)					
Sales	na	na	na	596.4	267.0
EBIT adjusted	na	61.3	nm	614.7	372.7
EBITDA adjusted	na	61.3	nm	584.6	355.9
EPS adjusted	na	89.3	nm	528.3	411.8
Cash Flow (RsM)					
Operating cash flow	**-72**	**-1,170**	**140**	**11,921**	**59,603**
Depreciation/amortization	0	0	376	1,918	6,110
Net working capital	0	-1,142	-1,964	-2,979	-7,878
Investing cash flow	**-1**	**-44,085**	**-86,850**	**-94,168**	**-101,150**
Capital expenditure	-1	-44,618	-86,850	-94,168	-101,150
Acquisitions/disposals	0	0	0	0	0
Financing cash flow	**0**	**48,215**	**83,314**	**81,032**	**59,407**
Borrowings	0	39,785	53,322	84,875	71,281
Dividends paid	0	0	0	0	0
Change in cash	**-73**	**2,960**	**-3,396**	**-1,216**	**17,860**
Balance Sheet (RsM)					
Total assets	**28,811**	**78,962**	**158,629**	**253,123**	**374,626**
Cash & cash equivalent	1,921	5,585	2,189	973	18,834
Accounts receivable	0	0	301	1,531	5,201
Net fixed assets	24,595	69,213	155,687	247,937	342,977
Total liabilities	**14,472**	**55,516**	**103,464**	**188,820**	**260,825**
Accounts payable	4,361	5,620	245	725	1,449
Total Debt	10,112	49,897	103,219	188,094	259,375
Shareholders' funds	**14,339**	**23,446**	**55,165**	**64,304**	**113,801**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	na	na	55.0	54.1	67.1
ROE adjusted	na	-0.1	3.8	15.5	53.8
ROIC adjusted	na	-0.1	1.6	6.8	21.1
Net debt to equity	57.1	189.0	183.1	291.0	211.4
Total debt to capital	41.4	68.0	65.2	74.5	69.5

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Powered by: dataCentral

Figure 1. Adani Power – 1QFY11 Results

Rsmn	3QFY10	4QFY10	FY10	1QFY11
Generation (mu)	670	664	1,335	1,153
Sales (mu)	606	615	1,221	1,030
Auxiliary Consumption	9.7%	7.4%	8.5%	10.7%
Net Sales	**2,336**	**2,013**	**4,349**	**3,531**
Rs/kWh per unit sold	3.86	3.27	3.56	3.43
Total	**2,336**	**2,013**	**4,349**	**3,531**
Consumption of RM	(970)	(697)	(1,667)	(1,098)
Rs/kWh per unit generated	1.45	1.05	1.25	0.95
O&M Cost	(94)	(142)	(236)	(301)
Rs/kWh per unit sold	0.16	0.23	0.19	0.29
Total Expenses	**(1,064)**	**(839)**	**(1,903)**	**(1,399)**
EBITDA	**1,272**	**1,174**	**2,446**	**2,132**
EBITDA margin	**54.5%**	**58.3%**	**56.2%**	**60.4%**
Rs/kWh per unit sold	**2.10**	**1.91**	**2.00**	**2.07**
Depreciation	(176)	(177)	(353)	(279)
Rs/kWh per unit sold	0.29	0.29	0.29	0.27
EBIT	**1,096**	**997**	**2,092**	**1,852**
EBIT margin	**47%**	**50%**	**48%**	**52%**
EBIT per unit sold	**1.81**	**1.62**	**1.71**	**1.80**
Interest	(167)	(210)	(377)	(433)
Other income	0	319	319	79
Other operating income	0	0		1
PBT	**929**	**1,106**	**2,035**	**1,499**
PBT per unit sold	**1.53**	**1.80**	**1.67**	**1.46**
Tax	(204)	(123)	(327)	(354)
Rate%	22.0%	11.1%	16.1%	23.6%
PAT	**725**	**983**	**1,708**	**1,145**
PAT margin	**31.0%**	**48.8%**	**39.3%**	**32.4%**

Source: Citi Investment Research and Analysis

Adani Power

Company description

Adani Power Limited (APL) has five thermal power projects in various stages of development, with combined capacity of 12,540 MW, namely: (i) Mundra Power Project with 4,620MW (ii) Tiroda Power Project with 3,300MW (iii) Kawai Power Project with 1,320MW (iv) Dahej Power Project with a capacity of 1,980MW and (v) Chhindwara Power Project with a capacity of 1320MW.

Investment strategy

Adani Power is an interesting case of private sector entrepreneurship at its best, capitalizing on persistent power deficits and exploiting high medium term merchant tariffs before the start of long term PPAs to reduce project payback, using faster-than-BHEL execution time cycles of Chinese equipment suppliers. Impressive progress on 4620MW of capacity at Mundra and the Adani Group's experience in executing mega projects like the Mundra Ports and SEZ project bolsters the investment case. However, we see a few loose ends that need tying: 1) insufficient coal for 25 years, 2) coal mining license risk, 3) fuel pricing for Indonesian coal from AEL, and 4) dependence on reasonable merchant rates to extract higher than regulated peer value. We believe some will be tied up in time. We give APL the benefit of the doubt and model in flawless execution of 9240MW and arrive at a fair value of Rs106/share. Despite this the current stock price does not leave much on the table for investors who are prepared to back the Adani Group's entrepreneurial ability. We rate APL Sell/ Medium (3M) risk.

Valuation

Traditional valuation methodologies like P/E and EV/EBITDA multiples can be misleading if used to value pure infrastructure asset holders, as profitability of the projects can be lumpy, primarily on the basis of year of commissioning and the life of the asset. In some years, when projects are commissioned, the company may look attractive on a PE multiple basis, while in another year, when the asset life ends, the stock may appear relatively expensive. Infrastructure assets and more specifically Electric Utilities generate regular and largely predictable cash flow streams for a fixed time period. Therefore, discounted cash flow (DCF) is best-suited to value BOT projects. While applying DCF one can choose free cash flow to the firm (FCF) or free cash flow to equity (FCFE). We prefer FCFE as individual projects are highly geared and gearing changes as debt is rapidly paid off. If we assume APL executes all its projects flawlessly in line with our assumptions we would arrive at a value of Rs106 for the stock.

Risks

Our quantitative risk-rating system, which tracks 260-day historical share price volatility, assigns a Speculative Risk rating to Adani Power given the relatively short trading history of the stock. However, we believe a Medium Risk rating is more appropriate based on a number of factors, namely industry-specific risks, financial risk and management risks. Downside risks include: 1) Insufficient quantity of coal in Bunyu to fire the Mundra project; 2) The total reserves of 150mn tonnes have three licenses.

While the counterparties of 2 of the 3 mines have procured long-term exploitation licenses the third license has not yet been granted to the counterparty; 3) Regulatory risk in Indonesia; 4) Fuel supply to Mundra Phase IV and Tiroda is contingent on AEL achieving certain milestones and finalizing the coal supply agreements and timely mining; 5) Fuel pricing risk for the Indonesian coal; 6) Merchant tariff risks; 7) Execution risks; 8) Chinese equipment quality risks; and 8) Interest rate risk. Upside risks include: 1) Better than expected operating parameters; 2) Faster than expected execution; 3) Higher than expected merchant tariffs; and 4) Significant progress on 3300MW of projects now in planning stages.

Appendix A-1

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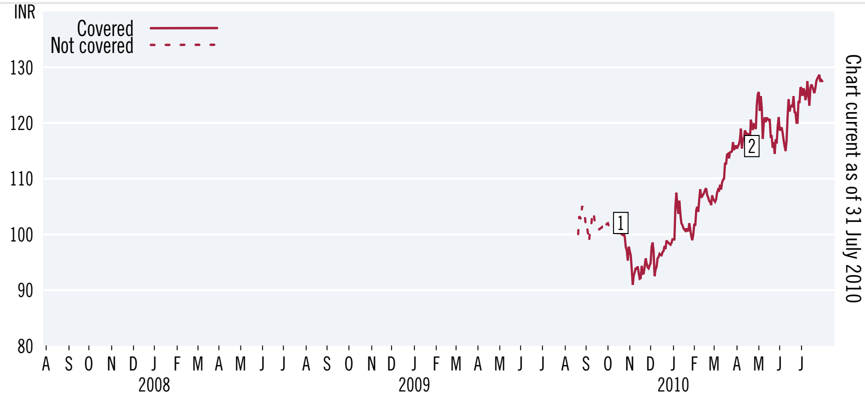
Adani Power (ADAN.BO)

Ratings and Target Price History
Fundamental Research

Analyst: Venkatesh Balasubramaniam
Covered since October 20 2009



	Date	Rating	Target Price	Closing Price
1	20-Oct-09	*3M	*88.00	100.15
2	22-Apr-10	3M	*106.00	119.50

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

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