Company

3 August 2010 | 7 pages

NTPC (NTPC.BO)

Equity

Buy: Analyst Meet Takeaways – Preparing for Regulatory Changes

- We attended NTPC's annual analyst meet. Following are key takeaways.
- **Preparing for changes in regulatory regime** — National Tariff Policy of Government of India mandates that all purchases of power will have to be done on competitive bidding basis from January 2011 onwards. NTPC management appeared confident of winning projects on competitive bidding basis.
- **Plans to tie up most of 75GW capacity under regulated RoE PPAs —** Management mentioned that company will be able to tie up most of 75GW capacity planed till 2017 under current regime of regulated RoEs by January 2011. This includes – 32.2GW (operational), 17.3 GW (under construction), 14GW (660MW and 800MW bulk tenders projects) and 6 GW (planned gas based expansion).
- **Long term capacity addition plan unveiled** — NTPC has unveiled long term plan of achieving 128GW capacity by 2032. Management reiterated commitment to previously outlined plan of achieving 75GW by 2017. NTPC currently has 32.2GW operational, 17.3GW under construction and 7.1GW under bidding. Feasibility reports have been approved for 8.5GW and are under preparation for10GW more.
- **Increasing focus on execution** — Company is trying to reduce execution time for projects by using IT based real time monitoring of projects. NTPC has now decided to issue limited notice to proceed to its vendors to enable start of engineering activities before award of main plant equipment. This is expected to reduce execution time of projects by 5-6 months.
- **FY11 capacity addition and capex** — NTPC plans to add 4,150MW (990MW in 2Q11, 1160MW in 3Q11 and 2000MW in 4Q11) capacity in FY11. Company has commercialized 1490MW during FY10. Company plans to do capex of Rs224bn in FY11 of which Rs128bn will be funded through debt.
- **1QFY11 PAT fell 16% YoY** — Reasons for the fall in PAT are (1) Company pre-poned outages planned for 2QFY11 to 1QFY11 due to common wealth games. As a result generation growth was muted and company could not earn availability incentives. So far in 2QFY11, generation has grown 7% YoY. (2) Interest on cash balance reduced to 6% in 1QFY11 from 8.65% in 1QFY10 leading to ~Rs2bn decline in other income.
- **Fuel supply situation remains satisfactory** — NTPC is receiving required quantity of coal on all its plants except Kahalgaon and Farakka. At these two stations, NTPC has planned to increase blending of imported coal to 50% to make up for the shortfall. Gas is now available and gas stations are operating at ~80% PLFs.

Buy/Low Risk	**1L**
Price (02 Aug 10)	Rs198.00
Target price	Rs229.00
Expected share price return	15.7%
Expected dividend yield	1.9%
Expected total return	**17.6%**
Market Cap	Rs1,632,602M
	US$35,303M

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

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Fiscal year end 31-Mar	2008	2009	2010E	2011E	2012E
Valuation Ratios					
P/E adjusted (x)	20.3	21.3	18.4	15.5	14.0
EV/EBITDA adjusted (x)	14.9	16.8	12.6	10.5	9.5
P/BV (x)	3.1	2.8	2.6	2.4	2.1
Dividend yield (%)	1.8	1.8	1.9	2.0	2.1
Per Share Data (Rs)					
EPS adjusted	9.77	9.29	10.74	12.80	14.13
EPS reported	8.99	9.95	10.74	12.80	14.13
BVPS	63.84	69.58	75.87	83.99	93.21
DPS	3.50	3.60	3.80	4.00	4.20
Profit & Loss (RsM)					
Net sales	370,974	419,922	480,963	554,773	622,767
Operating expenses	-284,105	-344,521	-371,079	-417,685	-467,798
EBIT	**86,869**	**75,401**	**109,884**	**137,088**	**154,970**
Net interest expense	-10,778	-13,529	-16,702	-19,540	-22,945
Non-operating/exceptionals	29,203	32,806	29,372	30,980	32,806
Pre-tax profit	**105,294**	**94,678**	**122,554**	**148,529**	**164,831**
Tax	-24,766	-18,110	-34,027	-43,006	-48,287
Extraord./Min.Int./Pref.div.	-6,380	5,445	0	0	0
Reported net income	**74,148**	**82,013**	**88,527**	**105,522**	**116,544**
Adjusted earnings	80,528	76,568	88,527	105,522	116,544
Adjusted EBITDA	108,254	99,046	136,789	168,116	191,300
Growth Rates (%)					
Sales	13.7	13.2	14.5	15.3	12.3
EBIT adjusted	21.1	-13.2	45.7	24.8	13.0
EBITDA adjusted	17.0	-8.5	38.1	22.9	13.8
EPS adjusted	11.7	-4.9	15.6	19.2	10.4
Cash Flow (RsM)					
Operating cash flow	**89,648**	**90,855**	**113,918**	**136,361**	**152,428**
Depreciation/amortization	21,385	23,645	26,906	31,029	36,330
Net working capital	-8,439	-12,794	-1,515	-190	-445
Investing cash flow	**-66,794**	**-116,545**	**-103,029**	**-144,222**	**-159,486**
Capital expenditure	-82,232	-131,351	-113,920	-154,648	-164,944
Acquisitions/disposals	0	0	0	0	0
Financing cash flow	**-6,668**	**39,074**	**14,279**	**36,615**	**35,626**
Borrowings	27,062	73,772	50,937	75,203	76,143
Dividends paid	-33,764	-34,700	-36,659	-38,588	-40,517
Change in cash	**16,186**	**13,384**	**25,167**	**28,754**	**28,567**
Balance Sheet (RsM)					
Total assets	**893,880**	**1,052,248**	**1,162,293**	**1,316,112**	**1,480,589**
Cash & cash equivalent	149,332	162,716	187,883	216,637	245,204
Accounts receivable	29,827	35,842	39,462	44,695	50,366
Net fixed assets	485,720	593,426	680,440	804,060	932,675
Total liabilities	**367,494**	**478,547**	**536,723**	**623,608**	**712,059**
Accounts payable	48,263	64,469	69,551	78,788	88,496
Total Debt	271,906	345,678	396,615	471,818	547,961
Shareholders' funds	**526,386**	**573,701**	**625,570**	**692,504**	**768,530**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	29.2	23.6	28.4	30.3	30.7
ROE adjusted	15.9	13.9	14.8	16.0	16.0
ROIC adjusted	12.5	9.5	10.7	11.5	11.3
Net debt to equity	23.3	31.9	33.4	36.8	39.4
Total debt to capital	34.1	37.6	38.8	40.5	41.6

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NTPC

Company description

NTPC is India's largest power generator with 31GW of capacity (19% of installed capacity) and generates 207bu (31% of generation). Capacity is spread across coal-based units (24.4GW), gas-based units (3.9GW) and JV projects (2.3GW). NTPC's output is contracted through long-term PPAs (25 years for coal-based and 15 years for gas-based) with customers (SEBs 99% of its sales). All billing to SEBs is secured through letters of credit. It plans to be a 75GW company by FY17E.

Investment strategy

We rate NTPC Buy/Low Risk (1L). The Indian regulatory system of cost pass-throughs works well and provides a defensive characteristic to NTPC's financials, unlike other Asian generators. Capex is well-funded with low gearing (0.63x), high cash balance of Rs188bn, strong credit rating and high annual CFO. NTPC's market leadership (31% share of the country's power generation), competitive cost structure, strong project-implementation skills and robust finances put the company in a strong position to target a capacity of 75GW by FY17E. Volatility in earnings would also be minimal - under current regulations, key costs are a pass-through, allowing for post-tax ROE of 15.5% v/s the current 10-year GOI bond yield of 7.85%.

Valuation

Our target price for NTPC of Rs229 is based on a DCF model that uses a WACC of 9.7% and a terminal growth rate of 3%. Our assumptions are a risk-free rate of 8.5%, a market risk premium of 6% and beta of 0.9. We believe DCF is the best way to capture the value inherent in NTPC's unprecedented capacity addition plan against a backdrop of persistent peak and base load deficits. Further, at our Rs229 target price NTPC would trade at a P/BV of 2.7x FY11E. We see this as reasonable given the Indian regulatory system of cost pass-throughs works well and provides a defensive characteristic to NTPC's financials, unlike other Asian generators.

Risks

We rate NTPC Low Risk according to our quantitative risk-rating system, which tracks 260-day historical share price volatility. Key downside risks to our target price are: 1) NTPC's operations depend on timely availability of fuel. NTPC's gas-based plants were hampered by poor fuel supply, resulting in sub-optimal capacity utilization. 2) 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, which could place demands on its project management and technology absorption skills. 3) UI rates are very high compared with normal tariff rates, creating pressure from the SEBs to reduce this spot market premium. 4) Future payment risk due to resurfacing of free power supply to agricultural customers as a populist measure by a few states. 5) NTPC has entered 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, as with any exploration & production (E&P) venture.

Appendix A-1

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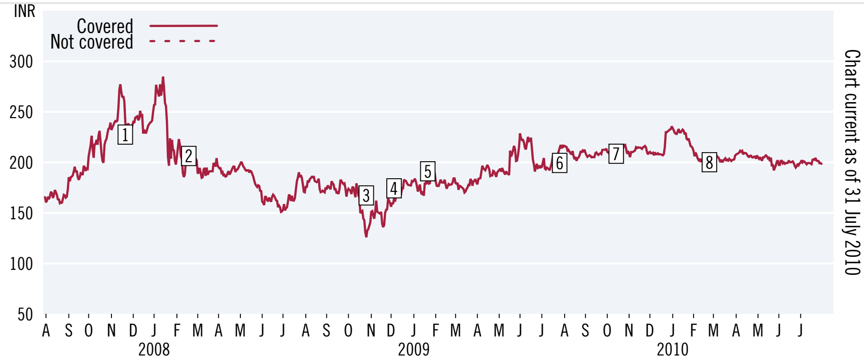
NTPC (NTPC.BO)

Ratings and Target Price History
Fundamental Research

Analyst: Venkatesh Balasubramaniam



	Date	Rating	Target Price	Closing Price
1	21-Nov-07	*3L	*231.00	239.50
2	19-Feb-08	*1L	*235.00	204.60
3	27-Oct-08	1L	*152.00	125.95
4	4-Dec-08	*3L	*149.00	164.55
5	21-Jan-09	*2L	*195.00	179.65
6	27-Jul-09	2L	*224.00	214.45
7	14-Oct-09	2L	*220.00	214.20
8	23-Feb-10	*1L	*229.00	201.60

* Indicates change

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