CESC Ltd.

Sensex: 15,727.85 CMP: INR 195 Target: INR 346

THE FINANCIAL ADVISORS

Power

CESC Ltd. is a fully integrated power utility engaged in the generation and distribution of electricity across 567 square kms of licensed area in Kolkata and Howrah in West Bengal. CESC is also operating a retail chain of 208 stores through its subsidiary Spencer's Retail (SRL). SRL has been incurring losses for the past five years and has dented CESC's core profitability by ~42% in FY11. However the retail business has already started earning at store level and we expect it to breakeven at corporate level by FY14E.

Capacity to double by FY15

CESC has increased its generation capacity by over 25% within a year to 1225 MW in FY11. The company is expected to double its generation capacity to 2425MW by FY15 through addition of 600MW in Chandrapur and 600MW in Haldia, scheduled to commission by May 2013 and Sept 2014 respectively. In addition to this, 3240 MW of thermal capacities are under development.

Integrated Power Utility

In India where most of the power generating companies sells power to distribution companies, CESC is in an advantageous position as it has its own distribution arm in Kolkata area which secures company from delayed payments and longer debtor days. Besides, for securing its coal requirement, CESC has also acquired 26% stake in its group company ICML which meets ~50% of the company's coal needs.

Stable and Regulated business with fixed ROE

CESC's current power capacity earns fixed post tax ROE of 14% on generation and 15% on distribution. The combined regulated equity for this business stands at INR 22.8 bn. We expect the company to invest INR 5 bn every year in distribution segment. This translates into a growth of combined regulated equity by INR 1.5 bn (6%-7%) every year.

Secured Coal Linkages

CESC's current capacity requires 6mmtpa of coal and it depends on domestic coal for most of its fuel requirements. About 50-55% of its coal requirements are met through ICML, 40% from Coal India linkage and the balance 5-10% is imported from Indonesia. Additionally CESC has invested 10% in Resource Gen which is developing mines in South Africa and would potentially provide access to 3.6 mmtpa of coal.

Spencer's to breakeven by FY15E

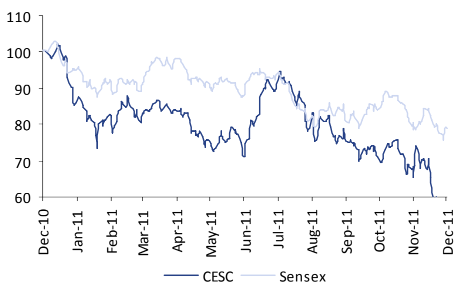
Spencer's Retail has already started earning at store level and we expect it to breakeven at corporate level by FY15E. Overall the retail business is expected to recover from the loss of INR 1.6bn in FY11 to INR 152 mn in FY14E and is estimated to breakeven in FY15E. This would be driven by closing of unviable stores, increasing the number of same stores (stores that have been open for a year or more) and changing the product mix to higher margin segment.

Outlook & Valuation

CESC is one of the cheapest utility stocks available in the Indian equity market. One of the key reasons for the lower valuation is the concern related to loss in its retail business. CESC's core regulated business is fully secured in the terms of fixed ROE, secured fuel availability and power offtaking agreements. We believe future growth would come from capacity expansion through SPVs, expected turnaround in retail business and commissioning of premium mall within a year. The company is expected to deliver CAGR of 14% and 31% in consolidated revenues and profitability over FY11-FY13E. We recommend BUY on CESC with a target price of INR 346 based on SOTP Valuation approach. At CMP the stock is trading at P/E of 5.1x FY13E EPS and P/BV of 0.44x its FY13E book value on consolidated basis.

Shareholding (%)	Sep-11
Promoters	52.48
FIIs	18.37
DIIS	16.99
Others	12.16

Relative Price Performance



Key Data	
BSE Code	500084
NSE Code	CESC
Bloomberg Code	CESC IN
Reuters Code	CESC.BO
Shares Outstanding (mn)	124.94
Face Value	10
Mcap (INR bn)	24
52 Week H/L	384.90/192.50
2W Avg. Qty, NSE	299,645
Free Float (INR bn)	13
Beta	0.93

Y/E March (INR mn)	FY10	FY11	FY12E	FY13E
Net Sales	42042	49425	59247	63687
Growth (%)	3.77%	17.56%	19.87%	7.49%
EBIDTAM (%)	10.86%	15.23%	16.88%	17.49%
Adj. PAT	1572	2784	4028	4757
Growth (%)	102.90%	77.03%	44.86%	18.13%
Adj. EPS (INR)	12.59	22.28	32.24	38.07
P/E (x)	30.38	13.96	6.06	5.13
EV/EBIDTA (x)	18.55	10.94	8.12	9.04
Net Debt/Equity (x)	0.81	0.92	1.11	1.37
RoACE (%)	4.48%	6.33%	6.96%	6.51%
RoAE (%)	3.46%	5.92%	7.89%	8.53%

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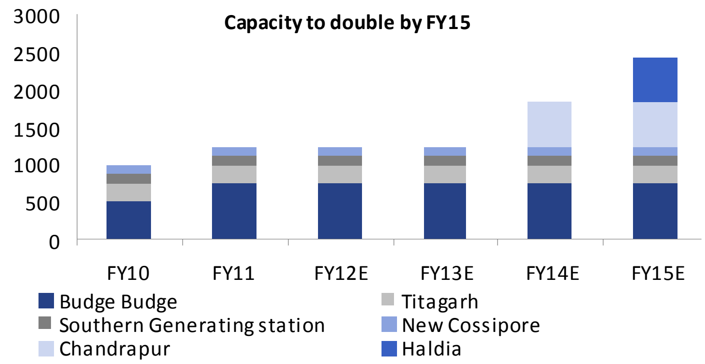
Investment Rationale

Capacity to double by FY15

CESC has increased its generation capacity by over 25% within a year to 1225 MW in FY11. The company is expected to double its generation capacity to 2425MW by FY15 through addition of 600MW in Chandrapur and 600MW in Haldia. For this, the company has already secured environmental and other clearances. The coal linkages have also been obtained and hence the projects are on schedule to be commissioned by May 2013 (Chandrapur) and Sept 2014(Haldia).

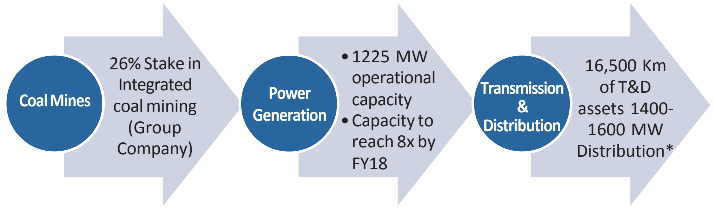


Source: Company, Research

In addition to Chandrapur and Haldia, 3240 MW of thermal capacities are under development. This includes 1320 MW facility in Orissa, 600MW facility in Jharkhand and 1,320MW facility in Balagarh. We have not included these projects in our valuation as these are in the very early stages of development and coal linkages have not been obtained for the same.

Integrated Power Utility

The state electricity boards (SEBs) are grappling with huge financial losses due to irrational power tariffs, insufficient infrastructure and T& D losses, with the figure pegged at INR 680 bn for FY11. The Finance Commission has estimated that the net annual losses of the state T&D utilities could be as high as INR 1000 bn by 2014-15 if the business-as-usual approach continues. In India where most of the power generating companies sells power to distribution companies (DISCOMs), CESC is in an advantageous position as it has its own distribution arm in Kolkata area which secures company from delayed payments and longer debtor days. Besides, for securing its coal requirement, CESC also acquired 26% stake in its group company ICML which meets ~50% of its coal needs.



**CESC buys ~200-400MW from WBSEB and other sources*

Source: Company, Research

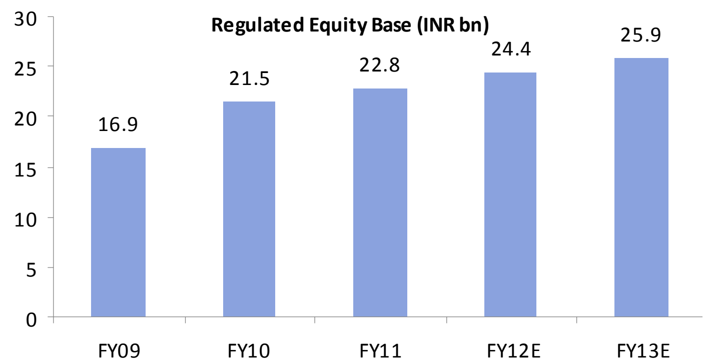
Projects in pipeline

Thermal Power Plants	Capacity	Commissioning	Total Investment (INR bn)	D/E	PPA: Merchant	Status
Project Under Construction						
Chandrapur, Maharashtra	600 MW	May-13	28.5	75:25	50:50	Fully under implementation, south eastern coalfields
Haldia Phase I, West Bengal	600 MW	Sep-14	33	75:25	75:25	Land in possession. Final Regulatory approval expected soon. All other approvals in place. ICB process completed. Domestic linkage from Mahanadi Coalfields (MCL) already established.
Project under Development						
Dhenkanal, Orissa	1000 MW	2015	65	75:25	60:40	Land in possession. Awaiting Long Term Coal linkage, Environmental TOR received & EIA completed.
Dumka, Jharkahand	600 MW	2016	35	75:25	60:40	Environmental TOR in place. Captive mine allocated. Land being acquired
Balagarh, West Bengal	1320 MW	2016	N.A	75:25	N.A	Land in hand, Environmental TOR in place. Linkage pending.
3rd unit on Haldia	300 MW	2018	N.A	N.A	N.A	Land in hand
OrissaPhase 2	1320 MW	2018	N.A	N.A	N.A	Land in hand; Environment & coal linkage pending
Pirpainti, Bihar	2000 MW	2018	N.A.	75:25	N.A	Environmental TOR in place. Land acquisition & coal linkage pending

Source: Company, SPA Research

Stable and Regulated business with fixed ROE

CESC's current capacity earns fixed post tax ROE of 14% on generation and 15% on distribution. The combined regulated equity for this business stands at INR 22.8 bn. We expect the company to invest INR 5 bn every year in distribution segment. The investment would be financed in D:E ratio of 70:30. This translates into growth of combined regulated equity by INR 1.5 bn (6%-7%) every year.



Source: Company, Research

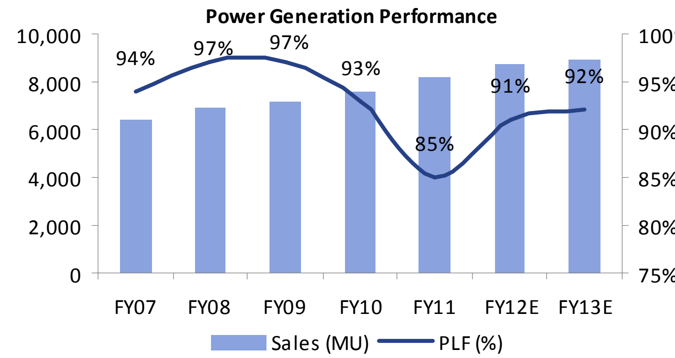
Secured Coal Linkages

CESC's current capacity requires 6 mmtpa of coal and it depends on domestic coal for most of its fuel requirements. About 50-55% of its coal requirements are met through Integrated Coal Mining (a group company), while 40% is linkage from Eastern Coalfields & Bharat Coking Coal (Coal India arms) and the balance 5-10% is imported from Indonesia.

Coal shortage is one of the key challenges for Indian power generating companies. Although CESC has obtained coal linkages for the under construction power projects, the company has raised stake in Resource Generation from 4.8% to 11.6%. This will entitle the company to offtake 139 mmt of coal for 38 years from the Australian company's Boikarabelo mines in South Africa. The mine is expected to be operational by FY13. The company is also looking forward for acquiring mines in Indonesia to further secure its fuel requirement.

Consistent improvement in operational efficiency

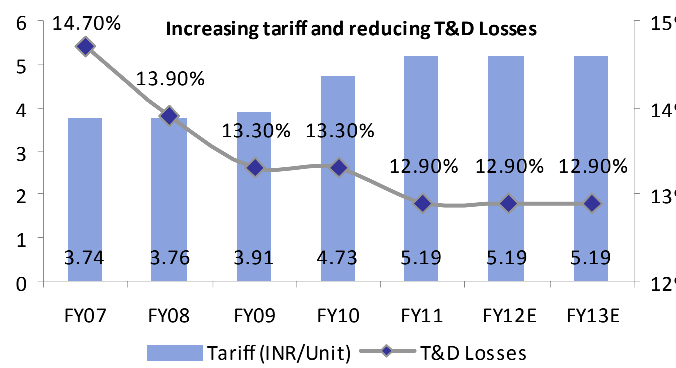
CESC has been able to consistently maintain more than 90% of PLF over the last few years which is above the industry average of 77-80%. The company registered a PLF of 85% in FY11 as 250 MW Budge Budge Unit was fully added in Q4FY11. Going forward we believe PLF to remain in the range of 91-92%. We expect CESC's sales volume to increase at a CAGR of 5% over FY11-13E to 8885 MUs.



Source: Company, SPA Research

T&D losses reducing consistently

With 2.3mn customers, 16,500km of the T&D network over 567sq km, the Kolkata T&D network is one of the most efficient operating distribution assets in the country, consistently beating the regulated T&D loss target. The company has been able to maintain its tariff in distribution area, while T&D losses have been brought down from 17.3% in FY04 to 13.3% in FY11, (~10% is expected to be technical loss at perfect efficiency). CESC's power regulator West Bengal Electricity Regulatory Commission (WBERC) is expected to approve tariff petition for three years from FY12-14E within couple of months. On a conservative basis we have assumed no hike in tariff as the regulator has already allowed hiking tariff by INR 0.46/unit due to the increased cost of fuel.



Source: Company, SPA Research

Core regulated business valued at INR 266

We expect CESC's standalone revenue and profitability to increase at CAGR of 7% and 6% respectively over FY11-13E. We have assumed Coal India Transfer price for domestic coal linkages and USD 110/ tonne for 5-10% of coal requirement to be imported. However, the company is less affected by increase in coal prices due to the provision of passing on the increased cost to the consumers.

Incentives for FY12E and FY13E are expected at INR 313 mn and INR 368 mn assuming 12% and 1.85% spread between actual and regulated norms for PLF and T&D losses respectively. We have valued CESC's regulated business at INR 266 per share by assigning P/E multiple of 6x to its FY13E EPS of INR 44.

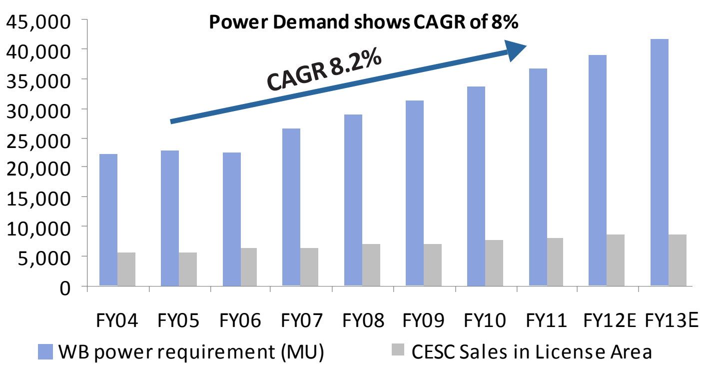
Standalone Regulated Business Financials

INR Mn	FY10	FY11	FY12E	FY13E
Installed Capacity (MW)	975	1,225	1,225	1,225
Commercial generation (MU)	7,595	8,135	8,789	8,885
Net Sales	33,549	40,111	45,927	46,482
Cost of Fuel / Coal Consumed	9319	12374	14,102	14,211
Electricity Purchased	6370	6654	6,787	6,923
Others	9789	10473	13951	13568
Total Expenditure	25478	29502	34840	34702
EBIDTA	8071	10609	11087	11780
Depreciation	2,056	2,674	2,694	2,754
interest	2,356	3,317	3,657	3,954
Other Income	1,562	1,524	1,677	1,845
Tax	888	1,259	1,283	1,383
Adj PAT	4,325	4,889	5,131	5,533
EPS	34.62	39.13	41.07	44.29

Source: Company, SPA Research

Power demand Supply scenario in licensed area

Demand for power across the licensed area is quite variable depending upon time of the day, with peak period demand higher than 1600 MW and lean period demand as low as 550 MW. During peak period CESC is able to fulfill only 70% of the demand in licensed area and thus it has to purchase power from the state and national power grids. Conversely during the lean period, CESC exports surplus power production, when possible, to maintain its PLF at higher level. The peak demand is expected to increase @ 5-6% p.a. going forward based on historical trend. However, overall power demand in West Bengal increased at a CAGR of 8% over FY05-11.



Source: Company, SPA Research

Chandrapur Power plant U/C valued at INR 40

CESC, through its wholly owned subsidiary, Dhariwal Infrastructure Pvt. Ltd., is setting up 600 MW power plant at Chandrapur in Maharashtra for INR 28.5 bn. It plans to fund this project through debt-equity mix of 75:25. CESC has already invested INR 10bn as equity. The plant is likely to commission from May 2013. The company has acquired land and established fuel linkages from South Eastern Coalfields Ltd (SECL). Keeping in view the current coal scenario, we have assumed that only 50% of the linkage coal will materialize and rest would be imported. The BTG and BoP orders have been placed with Shanghai Electric and Punj Lloyd respectively. We expect company to sell 50% of power from the project on long term basis to Maharashtra State Electricity Board at regulated rates and balance in short term market at merchant rates. We have assumed merchant rates at INR 3.5/unit and long term average PPA rate at INR 3/unit. We have valued this project at INR 40 per share on DCF basis discounting its free cash flow by 14% cost of equity (COE).

Financials & Valuation of Chandrapura Power Plant (600 MW)

INR Mn	FY14E	FY15E	FY16E	FY17E	FY18E	FY19E	FY20E
Installed Capacity (MW)	600	600	600	600	600	600	600
Sales Volume (MU)	1076	3348	3826	3826	4066	4066	4066
Total Revenue	3605	11049	12531	12436	13213	13213	13213
EBIDTA	1247	3979	5059	5238	6103	6103	6073
Depreciation	1187	1583	1583	1583	1583	1583	1583
Interest	1630	2173	1956	1738	1521	1304	1086
PBT	-1569	223	1521	1917	2999	3217	3404
PAT	-1569	179	1217	1534	2400	2573	2723
FCFE	-454	1541	135	453	1304	1478	1628
NPV (Explicit period FY12-FY37E)	5025						
Value per share (INR)	40						

Source: Company, SPA Research

Haldia Power Plant U/C valued at INR 5

Haldia Energy, a subsidiary of CESC, is setting up 600 MW greenfield Haldia Thermal Power Plant at a cost of INR 33 bn. CESC has already secured environmental and other clearances including water consumption for the project, while the coal linkage has also been obtained. Here too we have assumed that only 50% of the linkage coal will materialize and the rest would be imported. The project will be funded by debt-equity mix of 75:25. As per the Management guidance, we expect 75% (450 MW) of power from the project would be supplied to CESC distribution business at long term PPA rate and the balance 25% (150 MW) would be sold in short term market at merchant rates. We have assumed long term average merchant rate and PPA rate at INR 3.5/unit and INR 3/unit respectively. We have valued this project at INR 4.60 per share on DCF basis discounting its free cash flow by 14% COE.

Fiancials & Valuation of Haldia Power Plant (600 MW)

INR Mn	FY15E	FY16E	FY17E	FY18E	FY19E	FY20E
Installed Capacity (MW)	600	600	600	600	600	600
Sales Volume (MU)	1435	3348	3826	3826	4066	4066
Total Revenue	4699	10714	12101	11957	12705	12705
EBIDTA	1344	2983	3414	3545	4562	5170
Depreciation	1742	1742	1742	1742	1742	1742
Interest	2228	2228	2005	1782	1559	1337
PBT	-2626	-987	-333	20	1261	2091
PAT	-2626	-987	-333	16	1009	1673
FCFE	(977)	(1,934)	(1,308)	(955)	22	686
NPV (Explicit period FY12-FY40E)	581					
Value per share (INR)	4.65					

Source: Company, SPA Research

First Exposure to merchant rates

Although CESC sells surplus power from its Kolkata business in the open market at night, it will have its first full fledged merchant exposure of 300MW (Chandrapur power plant) in FY14 and another 150 MW (Haldia power plant) in FY15E. This will take its merchant exposure to 18.6% of its total capacity in FY15E. The merchant power rates in India have gone up from INR 3/unit in FY06 to INR 6/unit in FY10 due to increased power deficit. With new capacities (44% of the upcoming capacity is merchant based) getting operational, the merchant rates have fallen to INR 3 per unit. In our view, if the financial health of the SEBs does not improve, it would prevent them from purchasing power at competitive rates, which could cap the merchant power rates and affect the merchant power players negatively. However, we do not expect further decline in merchant rates as some of the planned capacities are not coming up due to fuel shortages. Hence we expect merchant power rates to remain at around INR 3.5/ kwh in the longer term.

Constructing a luxury mall in Kolkata

CESC Properties, a 100% subsidiary, is constructing a luxury mall in Central Kolkata on about 3 acre land with retail area of 0.4mn sq.ft and parking area of 0.3mn sq.ft. The mall is expected to start operations from FY13E at a cost of INR 2 bn with a D:E ratio of 60:40. We expect lease rentals of INR 90/sqft/mth for first three years starting from FY13E and then the company increase its rentals every three years by 15%. We have assumed occupancy rate of 50% in FY13E, 70% in FY14E and 90% thereafter. We have valued this business at INR 4.83 per share on DCF basis discounting its free cash flow by 14% COE.

Financials & Valuation of Mall in Central Kolkata

INR Mn	FY13E	FY14E	FY15E	FY16E	FY17E	FY18E	FY19E	FY20E	FY21E	FY22E	FY23E
Area under Mall (mn sq ft)	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40
Rentals (INR/sqft/Mth)	90	90	90	104	104	104	119	119	119	137	137
Rental income	108	302	367	422	422	422	486	486	486	605	652
EBIT	106	296	360	414	414	414	476	476	476	593	639
PAT	(26)	115	159	197	209	220	275	291	306	403	447
FCFE	(26)	115	159	47	59	70	75	91	106	253	447
PV of cash flows (Explicit period FY13-23E)	369										
PV of terminal value	234										
NPV of mall	603										
Value per share	4.83										

Source: Company, SPA Research

CESC Mulajore land - not included in valuation

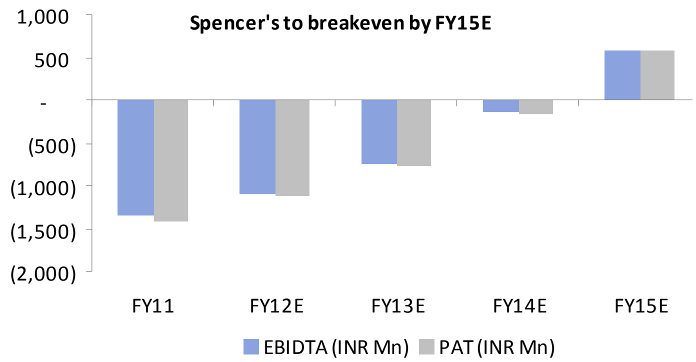
CESC Properties has 45 acres land which is idle due to closure of its oldest power station at Mulajore in 2003. The company has got the approval from West Bengal govt. to redevelop the land. CESC may look for gas-based power station at Mulajore as the site has become unsuitable for a coal-field thermal power plant, seeing that, densely populated residential areas has grown up around it. However the company has not finalized anything and has no plans to redevelop it at least for the next 2-3 years. Hence we have not included value of this land in our valuation.

Spencer's Retail

Spencer's to breakeven by FY15E

CESC forayed into retail business by acquiring 94.7% stake in Spencer's Retail Ltd. in 2007. CESC's retail business has been incurring losses for the past five years which peaked at INR 2.5 bn in FY10 and dented ~60% of CESC's core profitability. However, in FY11 its loss contribution to CESC's core profitability reduced to ~42% due to various strategies adopted by the company to recover losses. CESC closed more than 100 stores which were unprofitable and increased the number of same stores (stores that have been open for a year or more) which currently contributes ~80% of total number of stores. The same store sales increased by 14% p.a. in FY11. Currently SRL operates 208 stores with total area of 9.5 lakh sqft.

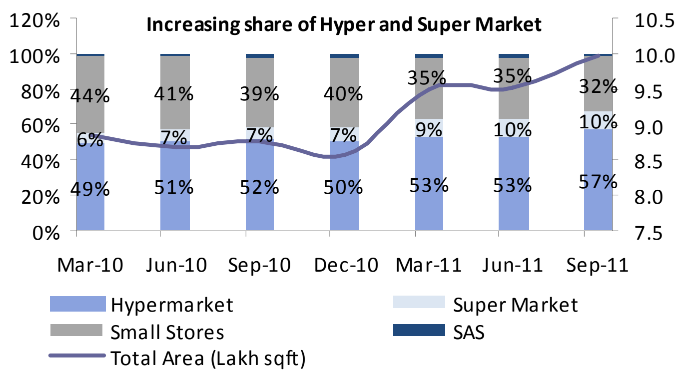
Although Management believes SRL to breakeven by FY14E, we expect SRL to breakeven only by FY15E. Overall the retail business is expected to recover from the loss of INR 1.6bn in FY11 to INR 760 mn in FY13E, INR 152 mn in FY14E and is estimated to breakeven in FY15E. This would be driven by closing of unviable stores, increasing the number of same stores and changing the product mix to higher margin segment.



Source: Company, SPA Research

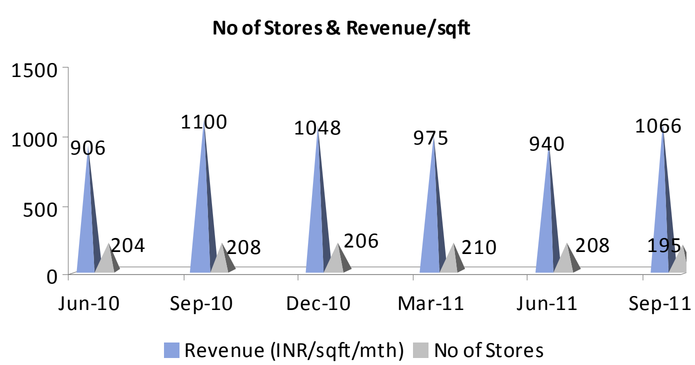
Same stores and revenue/sqft to gain momentum

We expect SRL to add 1 lakh sqft in FY12E, 1.75 lakh sqft in FY13E and further an addition of 15% p.a. going forward. The company is likely to invest INR 400-500 mn every year.



Source: Company, SPA Research

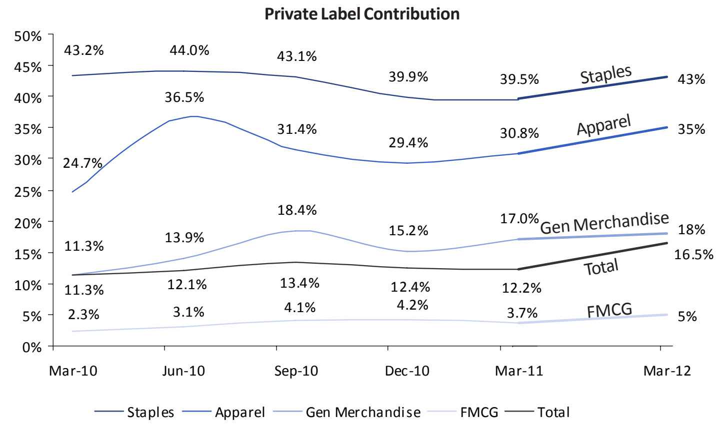
We anticipate SRL to add 9 stores every year from FY12-14E mainly in Hyper and Super market. The revenue per sq.ft is expected to increase at a CAGR of 10% from INR 962/sqft/mth in FY11 to INR 1164/ sqft/mth in FY13E.



Source: Company, SPA Research

Changing product mix to higher margin segment

The Company is changing its product mix by shifting from lower margin segment to higher margin food segment. The contribution of private label is expected to increase from 15% to 25% within two years. Retail Gross Margin (RGM) is expected to increase from 19% in FY11 to 22% by FY15E.



Source: Company, SPA Research

SRL Valuation

SRL's revenue is expected to increase at a CAGR of 10% over FY11-15E to INR 27 bn. We have calculated SRL's fair value at INR 24 per share on the basis of 0.8x EV/Sales. However we have not incorporated the same in our valuation as the company is not expected to turn profitable before FY15E.

SRL Valuation

	INR mn
FY13E Sales	17,097
EV/Sales	0.8x
EV	13,678
Amt invested by CESC till date	9,603
Capex for FY12-13	900
Fair Value of Company	3,175
CESC's Stake	94%
Value for CESC's stake	2,984
Value per share	23.89

Source: SPA Research

FDI in Retail

The Government is mulling a proposal to allow Foreign Direct Investment (FDI) in multi-brand retail. In case the Government allows FDI in multi-brand retail and any strategic partner picks up stake in CESC's retailing business, it would be a big positive trigger for CESC.

Spencer's Retail Ltd. - Financials

INR Mn	FY11	FY12E	FY13E	FY14E	FY15E
Total Area (Mn sq ft)	0.882	1.049	1.224	1.408	1.619
Retail Revenue	10177	13321	17097	21628	27359
Gross Profit	1,944	2,664	3,505	4,650	6,019
Retail Gross Margin (%)	19.10%	20.00%	20.50%	21.50%	22.00%
Store EBIDTA	183	537	953	1,630	2,442
Corp EBIDTA	(1,342)	(1,086)	(747)	(151)	576
Depreciation	508	492	516	538	562
Interest	327	272	271	270	269
Tax	(752)	(739)	(775)	(807)	(843)
Extra ordinary item	(211)	-	-	-	-
APAT	(1,636)	(1,112)	(760)	(152)	589

Source: Company, SPA Research

Well placed to fund future growth plans

CESC is likely to invest NR 84 bn in power and retail business over FY12-15E. We expect the company would take debt to the tune of INR 60 bn and rest INR 24 bn would be financed through internal accruals. The regulated business of the company generates steady operating cash flows (INR 10 bn in FY11) which would fund the equity requirement for upcoming power projects as well as cash losses in Spencer's.

Outlook & Valuation

CESC is one of the cheapest utility stocks available in the Indian equity market. One of the key reasons for the lower valuation is the concern related to loss in retail business. CESC's core regulated business is fully secured in the terms of fixed ROE, secured fuel availability and power offtaking agreements. We believe future growth would come from capacity expansion through SPVs, expected turnaround in retail business and commissioning of premium mall within a year.

We expect CESC's standalone net profit to increase at a CAGR of 6% respectively over FY11-13E to INR 5.5 bn. On consolidated basis, we expect the company to deliver CAGR of 14% and 31% in revenues and profitability respectively over FY11-FY13E.

We recommend BUY on CESC with a target price of INR 346. Our target price shows potential upside of 75% from the CMP. The assigned multiples to arrive at our target price are within the historical long-term range of the respective multiples. At CMP the stock is trading at P/E of 5.1x FY13E EPS and P/BV of 0.44x its FY13E book value on a consolidated basis.

We have valued CESC on Sum of the Parts Valuation Approach. Power business is valued at INR 266 based on 6x FY13E earnings. Upcoming Chandrapur and Haldia power projects are valued on FCFE basis at INR 40 and INR 5 per share respectively. Real Estate mall is valued at INR 5 per share discounting its free cash flow for equity. We have arrived at 14% cost of equity by assuming risk free rate of 8%, risk premium of 7% and beta of 0.87. We have not included SRL's value to arrive at our target price as it is not expected to turn profitable before FY15E.

SOTP Valuation

Business Segment	Activities	Valuation Methodology	Value (INR Mn)	Value (INR/Share)
Regulated Business	Power Generation & Distribution	P/E of 6x FY13E earnings	33199	265.72
CESC Properties	Real Estate	DCF, COE - 14%, Terminal Growth - 3%	603	4.83
Chandrapur 600MW	Power Generation	DCF, COE - 14%	5025	40.22
Haldia 600MW	Power Generation	DCF, COE - 14%	581	4.65
Liquid Investments		1x book value	3814	30.52
Equity Value/ Per share Value			43,221	345.93

Source: Company, SPA Research

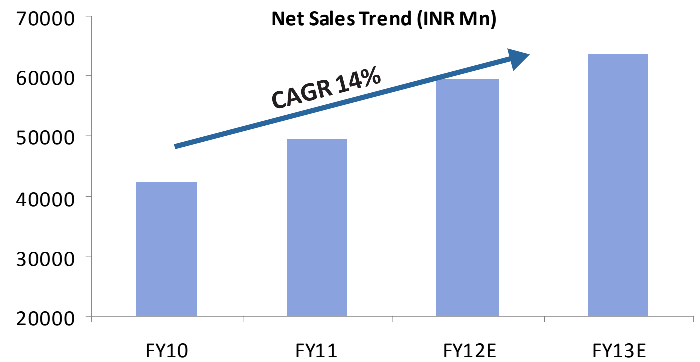
Risk and Concerns

- Delay in project execution under construction or development
- Limited domestic coal supply for its expansion would result in procuring coal either through E-auction or import at higher prices.
- Sharp increase in coal prices would result in importing coal at higher prices as well as would limit hike in tariff for regulated business
- Sharp decline in merchant rates
- Delays in commissioning the Boikarabelo mine in South Africa
- Higher than expected loss in retail business

Financial Analysis

Revenue to increase at a CAGR of 14%

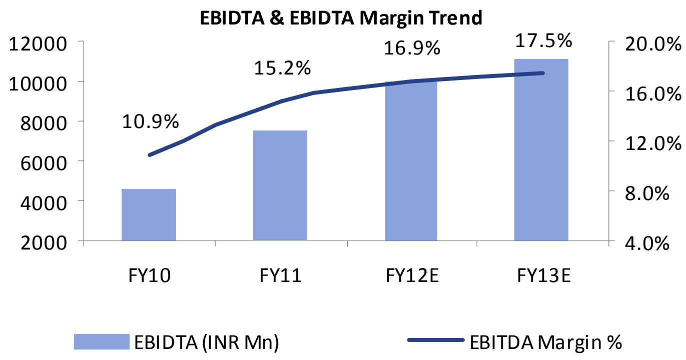
We expect CESC's consolidated revenue to increase at a CAGR of 14% over FY11-13E to INR 63 bn. This is mainly on the back of full operation of Budge Budge 3rd unit of 250 MW and 30% CAGR in SRL's revenue over FY11-13E.



Source: Company, SPA Research

Operating performance to improve

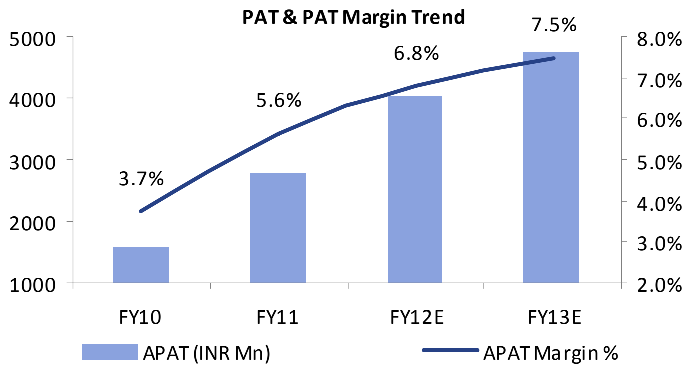
We estimate CESC's consolidated EBIDTA to register a growth of 22% as the company would be able to pass on higher cost and SRL's operating loss is expected to reduce by 44% from INR 1342 mn in FY11 to INR 747 mn by FY13E. EBIDTA margin is likely to improve from 15.3% in FY11 to 17.5% in FY13E.



Source: Company, SPA Research

PAT to increase at a CAGR of 31%

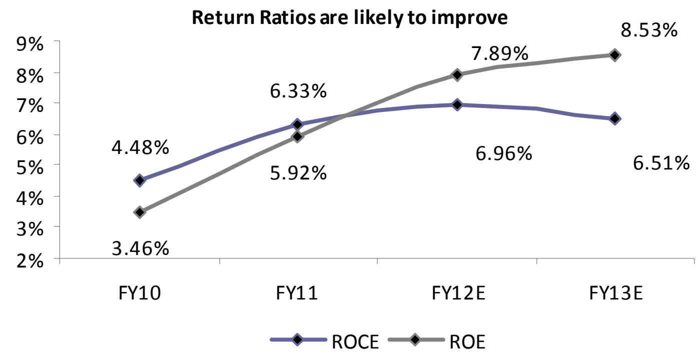
CESC 's consolidated net profit is expected to increase at a CAGR of 31% mainly due to sharp 55% decline in SRL's net loss from INR 1636 mn in FY11 to INR 760 mn in FY13E and 6% CAGR in CESC's regulated power business. PAT margin is expected to improve by 117 bps in FY12E and 67 bps in FY13E to 7.5%.



Source: Company, SPA Research

Return ratios to improve

We estimate ROCE to remain in the range of 6.5-7% over FY12E-FY13E and ROE to improve from 6.33% in FY11 to 8.53% by FY13E. We believe any further improvement in profitability due to faster turnaround in retail segment can improve the return ratios.



Source: Company, SPA Research

Quarterly Highlights

- In H1FY12, on a standalone basis, the total operating income stood at INR 24bn representing a growth of 10% over 1HFY11 aided by 9% increase in average realisation to INR 5.2/kwh and 1% increase in sales volume.
- In Q2FY12 CESC has recorded PLF of about 91.8% vs 90.2% in Q2FY11, excluding new Cossipore generating station. PLF showed an increase of about 1.6% YoY in Q2FY12. The T&D losses during Q2FY12 was at 12.8% vs 13.6% in Q2FY11 registering a decline of 80bps.
- CESC retail business' (Spencer's) half yearly average sales increased from INR 940/sqft/mth in H1FY11 to INR1066/sqft / mth in H1FY12. Same Stores Sales (SSS) increased from INR 981/sqft in H1FY11 to INR 1146/sqft/mth in H1FY12 registering a growth of 18.8%. Spencer's has made a store level EBIDTA of INR 31/sqft per month in H1FY12.

Quarterly Analysis

Standalone Quarterly Income Statement

INR Mn	Q2FY12	Q1FY12	QoQ Chg	Q2FY11	YoY Chg	1HFY12	1HFY11	Chg
Net Sales	12230	11690	4.62%	10900	12.20%	23920	21720	10.13%
Other Operating Income	180	140	28.57%	150	20.00%	320	290	10.34%
Total Income	12410	11830	4.90%	11050	12.31%	24240	22010	10.13%
Total Expenditure	9810	9160	7.10%	7870	24.65%	18970	16270	16.59%
EBIDT	2600	2670	-2.62%	3180	-18.24%	5270	5740	-8.19%
EBIDTM	20.95%	22.57%	(2257bps)	28.78%	(783 bps)	21.74%	26.08%	(433 bps)
Interest	750	700	7.14%	770	-2.60%	1450	1440	0.69%
Other Income	290	130	123.08%	170	70.59%	420	320	31.25%
PBDT	2140	2100	1.90%	2580	-17.05%	4240	4620	-8.23%
Depreciation	720	710	1.41%	640	12.50%	1430	1310	9.16%
PBT	1420	1390	2.16%	1940	-26.80%	2810	3310	-15.11%
Tax	280	280	0.00%	390	-28.21%	560	660	-15.15%
Net Profit	1140	1110	2.70%	1550	-26.45%	2250	2650	-15.09%
PATM	9.19%	9.38%	(938 bps)	14.03%	(484 bps)	9.28%	12.04%	(275 bps)
EPS (INR)	9.13	8.91	2.47%	12.41	-26.43%	18.04	21.21	-14.95%

Source: Company, SPA Research

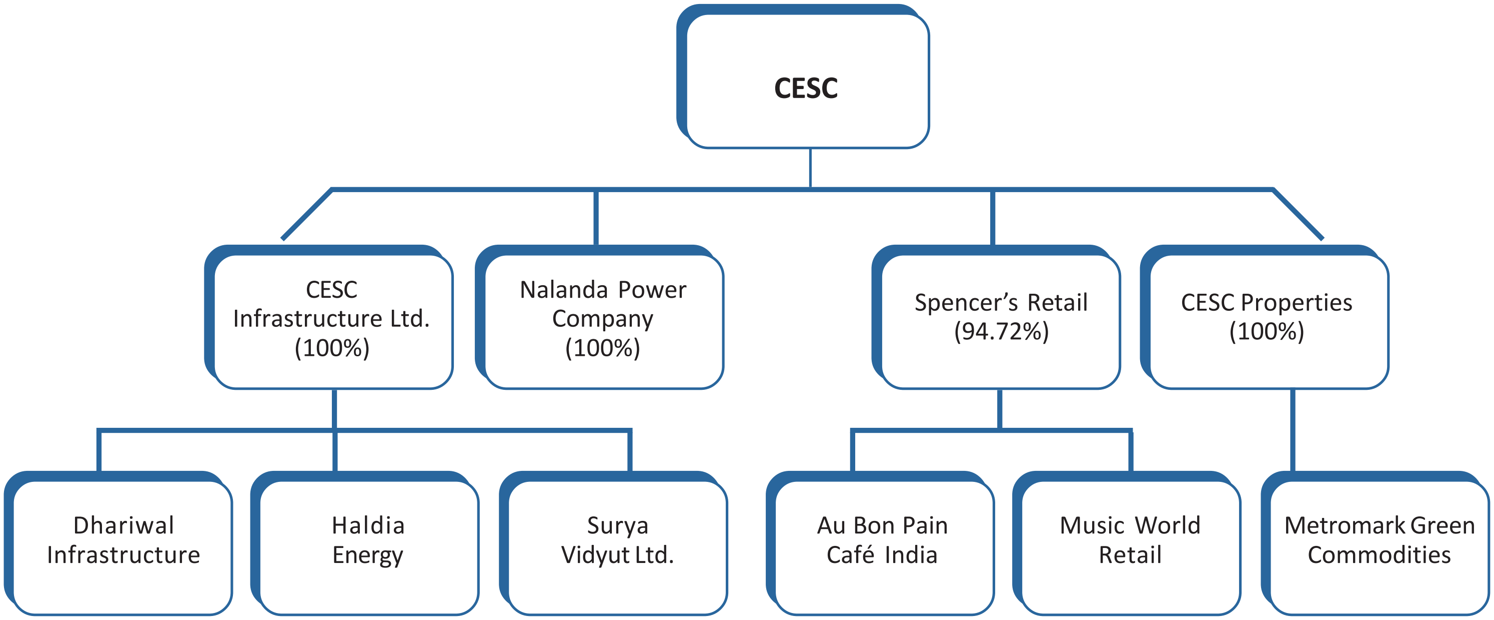
Company Background

CESC, a flagship company of RPG enterprise, is a fully integrated power utility with its operation spanning from generating power to distribution of power. It is the sole distributor of electricity within an area of 567 square kms of Kolkata & Howrah serving 2.4mn consumers, which includes domestic, industrial and commercial users.

CESC owns and operates four thermal power plants generating 1,225MW power. These are Budge Budge Generating Station (750MW), Southern Generating Station (135MW), Titagarh Generating Station (240MW) and New Cossipore Generating Station (100MW). More than 50% of its coal requirement is sourced from captive mines.

CESC owns and operates the T&D system comprises of 474 kms circuit of transmission, and 85 distribution stations, 3,837 kms circuit of HT lines linking distribution stations with LT substations, large industrial consumers and 9,867 kms circuit of LT lines connecting the LT substations to LT consumers. The company owns two subsidiaries namely CESC Properties Ltd. which is running real estate business and Spencer's Retail (SRL), which is engaged in running retail stores. CESC has ten subsidiaries - four direct and six indirect.

Organisation Structure



Financials - Consolidated

Income statement

Y/E March (INR mn)	FY10	FY11	FY12E	FY13E
Net Sales	42,042	49,425	59,247	63,687
% Growth	*3.77%*	*17.56%*	*19.87%*	*7.49%*
Cost of Energy Purchase	6,370	6,654	6,787	6,923
Cost of fuel for power	10,771	14,283	18,178	17,785
COGS for Retail business	7,959	8,658	10,656	13,592
Other Expenditure	12,376	12,305	13,625	14,248
Total Expenditure	37,475	41,900	49,247	52,548
EBIDTA (excl OI)	4,566	7,525	10,001	11,139
% Growth	*56.38%*	*64.81%*	*32.89%*	*11.38%*
EBITDA Margin %	*10.86%*	*15.23%*	*16.88%*	*17.49%*
Dep./Amortization	2,514	3,165	3,186	3,271
EBIT	2,053	4,360	6,815	7,868
EBIT Margin %	*4.88%*	*8.82%*	*11.50%*	*12.35%*
Interest Expense	2,040	2,988	3,929	4,357
Other Income	2,158	2,143	1,677	1,845
Exceptionals	(432)	(212)	-	-
EBT	1,739	3,304	4,562	5,355
Tax Expenses	175	530	544	609
PAT	1,563	2,774	4,018	4,747
Extra ordinary item	-	(752)	(739)	(775)
Minority Interest	9	10	10	10
APAT	1,572	2,784	4,028	4,757
% Growth	*102.90%*	*77.03%*	*44.86%*	*18.13%*
APAT Margin %	*3.74%*	*5.63%*	*6.80%*	*7.47%*

Balance Sheet

Y/E March (INR mn)	FY10	FY11	FY12E	FY13E
Share Capital	1,256	1,256	1,256	1,256
Reserves and Surplus	44,137	45,752	49,780	54,537
Total Networth	45,393	47,008	51,036	55,793
Minority Interest	9	21	31	41
Secured	28,062	33,008	41,974	55,238
Unsecured	20,553	22,762	28,945	38,091
Total Debt	48,615	55,769	70,919	93,329
Source of Funds	**94,017**	**102,798**	**121,986**	**149,163**
Net Block	78,450	80,618	90,092	105,301
CWIP	4,422	8,801	13,865	21,257
Investments	4,374	4,174	4,215	4,258
Current Assets	23,566	25,237	31,043	34,617
Current Liabilities	19,329	19,312	21,241	21,049
Net Current Assets	4,237	5,925	9,802	13,568
Misc. Expenditure	71	64	57	50
Deferred Tax Assets	2,463	3,215	3,954	4,729
Application of Funds	**94,017**	**102,798**	**121,986**	**149,163**

Key Ratios

Y/E March	FY10	FY11	FY12E	FY13E
Per Share Data (INR)				
Reported EPS	12.59	22.28	32.24	38.07
Adj. EPS	12.59	22.28	32.24	38.07
Growth (%)	102.90%	77.03%	44.71%	18.08%
CEPS	32.70	47.61	57.74	64.25
DPS	4.00	4.00	4.00	4.00
Adj BVPS	363.32	376.24	408.48	446.56
Return Ratios (%)				
RoACE	4.48%	6.33%	6.96%	6.51%
RoANW	3.46%	5.92%	7.89%	8.53%
Liquidity Ratios (x)				
Net Debt/Equity	0.81	0.92	1.11	1.37
Interest Coverage Ratio	2.06	2.18	2.16	2.23
Current Ratio	1.22	1.31	1.46	1.64
Quick Ratio	0.61	0.67	0.80	0.83
Efficiency Ratios				
Asset Turnover Ratio	0.45	0.48	0.49	0.43
Inventory Days	32	30	31	30
Debtor Days	45	43	45	43
Creditor Days	44	44	44	44
Valuation Ratios				
P/E (x)	30.38	13.96	6.06	5.13
P/BV (x)	1.05	0.83	0.48	0.44
P/CEPS (x)	11.69	6.53	3.38	3.04
Dividend Yield (%)	1.05	1.29	2.05	2.05
EV/Net Sales (x)	2.01	1.67	1.37	1.58
EV/EBIDTA (x)	18.55	10.94	8.12	9.04

Cash Flow

Y/E March (INR mn)	FY10	FY11	FY12E	FY13E
EBT	1,739	3,304	4,562	5,355
Less: Other Income/Exceptionals	1,268	1,616	(1,677)	(1,845)
Add:Depreciation	2,514	3,165	3,186	3,271
Add: Interest paid	2,040	2,988	3,929	4,357
Direct taxes paid	(888)	(1,259)	(1,283)	(1,383)
Change in Working Capital	818	(1,128)	(1,427)	(208)
Cash Flow from operations (a)	**7,491**	**8,685**	**7,291**	**9,548**
Change in Fixed Assets	(7,390)	(6,166)	(12,660)	(18,480)
Change in CWIP	(6,396)	(4,380)	(5,064)	(7,392)
Change in Investments	956	200	(42)	(42)
Others	(345)	(917)	1,677	1,845
Cash Flow from Investing (b)	**(13,175)**	**(11,263)**	**(16,089)**	**(24,070)**
Change in Equity	20	10	-	-
Debt Raised/(Repaid)	9,051	7,154	15,149	22,410
Dividend paid	(583)	(585)	(585)	(585)
Interest paid	(2,040)	(2,988)	(3,929)	(4,357)
Others	(2,241)	(403)	-	-
Cash Flow from Financing (c)	**4,208**	**3,189**	**10,636**	**17,468**
Net Change in Cash (a+b+c)	**(1,477)**	**611**	**1,837**	**2,946**
Opening Cash	13,157	11,680	12,291	14,129
Closing Cash	**11,680**	**12,291**	**14,129**	**17,075**

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Disclosure of Interest Statement

1. Analyst ownership of the stock - No
2. Group/Directors ownership of the stock - No
3. Broking relationship with company covered - No

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