

INDIA

# GVK Power and Infra

3 February 2009

**GVKP IN** **Outperform**

|                             |    |       |
|-----------------------------|----|-------|
| Stock price as of 30 Jan 09 | Rs | 18.80 |
| 12-month target             | Rs | 27.00 |
| Upside/downside             | %  | +43.6 |
| Valuation                   | Rs | 27.00 |
| - Sum of Parts              |    |       |

|                        |       |           |
|------------------------|-------|-----------|
| GICS sector            |       | utilities |
| Market cap             | Rs m  | 26,430    |
| 30-day avg turnover    | US\$m | 13.1      |
| Market cap             | US\$m | 541       |
| Number shares on issue | m     | 1,406     |

## Investment fundamentals

| Year end 31 Mar |    | 2008A | 2009E | 2010E  | 2011E  |
|-----------------|----|-------|-------|--------|--------|
| Total revenue   | m  | 4,700 | 4,692 | 12,994 | 21,815 |
| EBITDA          | m  | 2,477 | 2,066 | 4,091  | 6,835  |
| EBITDA growth   | %  | 9.9   | -16.6 | 98.0   | 67.1   |
| Adjusted profit | m  | 1,355 | 1,131 | 1,388  | 2,924  |
| EPS adj         | Rs | 1.04  | 0.80  | 0.99   | 2.08   |
| EPS adj growth  | %  | 68.0  | -22.6 | 22.7   | 110.6  |
| PE adj          | x  | 18.1  | 23.4  | 19.1   | 9.1    |
| Total DPS       | Rs | 0.00  | 0.00  | 0.00   | 0.00   |
| Total div yield | %  | 0.0   | 0.0   | 0.0    | 0.0    |
| ROA             | %  | 5.2   | 3.3   | 5.8    | 8.4    |
| ROE             | %  | 8.6   | 4.7   | 5.5    | 10.6   |
| EV/EBITDA       | x  | 10.4  | 18.8  | 9.5    | 5.7    |
| Net debt/equity | %  | 47.7  | 54.9  | 92.0   | 122.1  |
| Price/book      | x  | 0.6   | 1.1   | 1.0    | 0.9    |

## GVKP IN rel SENSEX performance, & rec history



Source: Datastream, Macquarie Research, February 2009 (all figures in INR unless noted)

## Analyst

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## Incremental clarity on gas emerging

### Event

- GVK reported results in line with expectations, with clarity emerging on gas.

### Impact

- Results in line with expectations:** GVK reported 1% revenue growth and a PAT decline in its 3Q FY3/09 results, in line with our expectations. Weak revenue bookings were a result of non-availability of gas in its power plants, with Jegrupada-I running at only a 63% Plant Load Factor (PLF), much below the threshold requirement. The PAT decline was accentuated due to lower other income and a one-time hit of Rs128m from payment of arrears to Airport Authority of India (AAI) employees on account of the 6<sup>th</sup> pay commission pay revisions. These employees are on the payroll until May 2009, post which GVK would not have to take the extra hit, which should help boost margins.
- Significant upside from early availability of gas:** Incremental clarity is emerging on gas availability, with the Bombay High Court modifying its earlier interim order, now allowing Reliance (RIL IN, OP, Rs1,280, TP: Rs1,700) to sell gas from KG-D6 to third parties as soon as production starts, with a final judgement expected by 15 March 2009. However, we are still building in gas availability from September 2009. Our sensitivity analysis suggests a 4% increase in the target price if gas is made available even by June 2009.
- Two upcoming power projects could benefit from recent CERC ruling:** Two of GVK's upcoming power plants – Alaknanda and Govindwahil Sahib – could benefit from the recent Central Electricity Regulatory Commission's (CERC) ruling that ROEs would be increased to 15.5% from 14%. However, management said that clarity is yet to emerge on the guidelines.

### Earnings revision

- We have increased our FY09E earnings by 22% and FY10E earnings by 8% to incorporate better margins.

### Price catalyst

- 12-month price target: Rs27.00 based on a Sum of Parts methodology.
- Catalyst: Availability of gas as early as March 2009

### Action and recommendation

- GVK remains our preferred pick in the developer space. The stock has excellent growth prospects, with gas availability coming up, stable road projects and a financially closed Mumbai airport project. The stock is currently available at attractive valuations of 0.9x FY10E P/BV.

**GVK Power and Infrastructure Ltd (GVKP IN, Outperform, Target price: Rs27.00)**

| Quarterly Results                 |        |        |        |        | Profit & Loss             |                                   |        |         |         |         |         |
|-----------------------------------|--------|--------|--------|--------|---------------------------|-----------------------------------|--------|---------|---------|---------|---------|
|                                   | 2Q/09A | 3Q/09E | 4Q/09E | 1Q/10E |                           | 2008A                             | 2009E  | 2010E   | 2011E   |         |         |
| <b>Revenue</b>                    | m      | 938    | 1,173  | 1,642  | 2,599                     | <b>Revenue</b>                    | m      | 4,700   | 4,692   | 12,994  | 21,815  |
| <b>Gross Profit</b>               | m      | 508    | 636    | 890    | 959                       | <b>Gross Profit</b>               | m      | 2,964   | 2,542   | 4,797   | 7,599   |
| Cost of Goods Sold                | m      | 430    | 538    | 753    | 1,640                     | Cost of Goods Sold                | m      | 1,736   | 2,150   | 8,198   | 14,216  |
| <b>EBITDA</b>                     | m      | 378    | 517    | 793    | 769                       | <b>EBITDA</b>                     | m      | 2,477   | 2,066   | 4,091   | 6,835   |
| Depreciation                      | m      | 194    | 194    | 194    | 345                       | Depreciation                      | m      | 776     | 776     | 1,381   | 1,701   |
| Amortisation of Goodwill          | m      | 0      | 0      | 0      | 0                         | Amortisation of Goodwill          | m      | 0       | 0       | 0       | 0       |
| Other Amortisation                | m      | 0      | 0      | 0      | 0                         | Other Amortisation                | m      | 0       | 0       | 0       | 0       |
| <b>EBIT</b>                       | m      | 184    | 323    | 599    | 424                       | <b>EBIT</b>                       | m      | 1,701   | 1,291   | 2,710   | 5,134   |
| Net Interest Income               | m      | -80    | -80    | -80    | -410                      | Net Interest Income               | m      | -414    | -320    | -1,639  | -1,800  |
| Associates                        | m      | 0      | 0      | 0      | 0                         | Associates                        | m      | 0       | 0       | 0       | 0       |
| Exceptionals                      | m      | 0      | 0      | 0      | 0                         | Exceptionals                      | m      | 0       | 0       | 0       | 0       |
| Forex Gains / Losses              | m      | 0      | 0      | 0      | 0                         | Forex Gains / Losses              | m      | 0       | 0       | 0       | 0       |
| Other Pre-Tax Income              | m      | 0      | 0      | 0      | 0                         | Other Pre-Tax Income              | m      | 0       | 0       | 0       | 0       |
| <b>Pre-Tax Profit</b>             | m      | 104    | 243    | 519    | 14                        | <b>Pre-Tax Profit</b>             | m      | 1,287   | 971     | 1,071   | 3,334   |
| Tax Expense                       | m      | -36    | -45    | -63    | -40                       | Tax Expense                       | m      | -239    | -180    | -198    | -618    |
| <b>Net Profit</b>                 | m      | 68     | 198    | 456    | -25                       | <b>Net Profit</b>                 | m      | 1,049   | 791     | 873     | 2,716   |
| Minority Interests                | m      | 85     | 85     | 85     | 129                       | Minority Interests                | m      | 306     | 340     | 515     | 208     |
| <b>Reported Earnings</b>          | m      | 153    | 283    | 541    | 103                       | <b>Reported Earnings</b>          | m      | 1,355   | 1,131   | 1,388   | 2,924   |
| <b>Adjusted Earnings</b>          | m      | 153    | 283    | 541    | 103                       | <b>Adjusted Earnings</b>          | m      | 1,355   | 1,131   | 1,388   | 2,924   |
| EPS (rep)                         |        | 0.11   | 0.20   | 0.38   | 0.07                      | EPS (rep)                         |        | 0.24    | 0.80    | 0.99    | 2.08    |
| EPS (adj)                         |        | 0.11   | 0.20   | 0.38   | 0.07                      | EPS (adj)                         |        | 1.04    | 0.80    | 0.99    | 2.08    |
| EPS Growth yoy (adj)              | %      | 354.3  | 323.6  | -59.2  | -32.6                     | EPS Growth (adj)                  | %      | 68.0    | -22.6   | 22.7    | 110.6   |
|                                   |        |        |        |        |                           | PE (rep)                          | x      | 76.9    | 23.4    | 19.1    | 9.1     |
|                                   |        |        |        |        |                           | PE (adj)                          | x      | 18.1    | 23.4    | 19.1    | 9.1     |
| EBITDA Margin                     | %      | 40.3   | 44.0   | 48.3   | 29.6                      | Total DPS                         |        | 0.00    | 0.00    | 0.00    | 0.00    |
| EBIT Margin                       | %      | 19.6   | 27.5   | 36.5   | 16.3                      | Total Div Yield                   | %      | 0.0     | 0.0     | 0.0     | 0.0     |
| Earnings Split                    | %      | 13.6   | 25.0   | 47.9   | 7.4                       | Weighted Average Shares           | m      | 5,539   | 1,409   | 1,409   | 1,409   |
| Revenue Growth                    | %      | -0.2   | -0.2   | -0.2   | 176.9                     | Period End Shares                 | m      | 715     | 1,409   | 1,409   | 1,409   |
| EBIT Growth                       | %      | -25.1  | -24.1  | -23.5  | 130.0                     |                                   |        |         |         |         |         |
| Profit and Loss Ratios            |        |        |        |        | Cashflow Analysis         |                                   |        |         |         |         |         |
|                                   | 2008A  | 2009E  | 2010E  | 2011E  |                           | 2008A                             | 2009E  | 2010E   | 2011E   |         |         |
| Revenue Growth                    | %      | 17.9   | -0.2   | 176.9  | 67.9                      | <b>EBITDA</b>                     | m      | 2,477   | 2,066   | 4,091   | 6,835   |
| EBITDA Growth                     | %      | 9.9    | -16.6  | 98.0   | 67.1                      | Tax Paid                          | m      | -239    | -180    | -198    | -618    |
| EBIT Growth                       | %      | 17.5   | -24.1  | 110.0  | 89.4                      | Chgs in Working Cap               | m      | -4,969  | 2,616   | -1,457  | -2,139  |
| Gross Profit Margin               | %      | 63.1   | 54.2   | 36.9   | 34.8                      | Net Interest Paid                 | m      | -414    | -320    | -1,639  | -1,800  |
| EBITDA Margin                     | %      | 52.7   | 44.0   | 31.5   | 31.3                      | Other                             | m      | 0       | 0       | 0       | 0       |
| EBIT Margin                       | %      | 36.2   | 27.5   | 20.9   | 23.5                      | <b>Operating Cashflow</b>         | m      | -3,144  | 4,183   | 796     | 2,278   |
| Net Profit Margin                 | %      | 22.3   | 16.9   | 6.7    | 12.5                      | Acquisitions                      | m      | 0       | 0       | 0       | 0       |
| Payout Ratio                      | %      | 0.0    | 0.0    | 0.0    | 0.0                       | Capex                             | m      | -35     | -6,862  | -11,813 | -14,813 |
| EV/EBITDA                         | x      | 10.4   | 18.8   | 9.5    | 5.7                       | Asset Sales                       | m      | 0       | 0       | 0       | 0       |
| EV/EBIT                           | x      | 15.2   | 30.1   | 14.4   | 7.6                       | Other                             | m      | -5,294  | 0       | 0       | 0       |
| <b>Balance Sheet Ratios</b>       |        |        |        |        | <b>Investing Cashflow</b> | m                                 | -5,329 | -6,862  | -11,813 | -14,813 |         |
| ROE                               | %      | 8.6    | 4.7    | 5.5    | 10.6                      | Dividend (Ordinary)               | m      | 0       | 0       | 0       | 0       |
| ROA                               | %      | 5.2    | 3.3    | 5.8    | 8.4                       | Equity Raised                     | m      | 323     | 0       | 0       | 0       |
| ROIC                              | %      | 5.5    | 3.0    | 5.8    | 8.3                       | Debt Movements                    | m      | -2,536  | 1,357   | 11,535  | 11,494  |
| Net Debt/Equity                   | %      | 47.7   | 54.9   | 92.0   | 122.1                     | Other                             | m      | 0       | 0       | 0       | 0       |
| Interest Cover                    | x      | 4.1    | 4.0    | 1.7    | 2.9                       | <b>Financing Cashflow</b>         | m      | -2,213  | 1,357   | 11,535  | 11,494  |
| Price/Book                        | x      | 0.6    | 1.1    | 1.0    | 0.9                       | <b>Net Chg in Cash/Debt</b>       | m      | -10,685 | -1,322  | 519     | -1,042  |
| Book Value per Share              |        | 33.1   | 17.6   | 18.6   | 20.6                      |                                   |        |         |         |         |         |
|                                   |        |        |        |        | Balance Sheet             |                                   |        |         |         |         |         |
|                                   | 2008A  | 2009E  | 2010E  | 2011E  |                           | 2008A                             | 2009E  | 2010E   | 2011E   |         |         |
| Cash                              | m      | 1,643  | 661    | 1,726  | 1,278                     | Cash                              | m      | 1,643   | 661     | 1,726   | 1,278   |
| Receivables                       | m      | 652    | 651    | 1,068  | 1,494                     | Receivables                       | m      | 652     | 651     | 1,068   | 1,494   |
| Inventories                       | m      | 227    | 281    | 674    | 974                       | Inventories                       | m      | 227     | 281     | 674     | 974     |
| Investments                       | m      | 7,068  | 4,461  | 5,219  | 5,929                     | Investments                       | m      | 7,068   | 4,461   | 5,219   | 5,929   |
| Fixed Assets                      | m      | 12,275 | 18,361 | 28,794 | 41,906                    | Fixed Assets                      | m      | 12,275  | 18,361  | 28,794  | 41,906  |
| Intangibles                       | m      | 0      | 0      | 0      | 0                         | Intangibles                       | m      | 0       | 0       | 0       | 0       |
| Other Assets                      | m      | 15,862 | 15,800 | 16,166 | 17,374                    | Other Assets                      | m      | 15,862  | 15,800  | 16,166  | 17,374  |
| <b>Total Assets</b>               | m      | 37,728 | 40,216 | 53,647 | 68,955                    | <b>Total Assets</b>               | m      | 37,728  | 40,216  | 53,647  | 68,955  |
| Payables                          | m      | 269    | 269    | 745    | 1,251                     | Payables                          | m      | 269     | 269     | 745     | 1,251   |
| Short Term Debt                   | m      | 0      | 0      | 0      | 0                         | Short Term Debt                   | m      | 0       | 0       | 0       | 0       |
| Long Term Debt                    | m      | 12,910 | 14,267 | 25,803 | 37,296                    | Long Term Debt                    | m      | 12,910  | 14,267  | 25,803  | 37,296  |
| Provisions                        | m      | 28     | 28     | 28     | 28                        | Provisions                        | m      | 28      | 28      | 28      | 28      |
| Other Liabilities                 | m      | 891    | 891    | 891    | 891                       | Other Liabilities                 | m      | 891     | 891     | 891     | 891     |
| <b>Total Liabilities</b>          | m      | 14,098 | 15,455 | 27,467 | 39,466                    | <b>Total Liabilities</b>          | m      | 14,098  | 15,455  | 27,467  | 39,466  |
| Shareholders' Funds               | m      | 23,624 | 24,755 | 26,143 | 29,067                    | Shareholders' Funds               | m      | 23,624  | 24,755  | 26,143  | 29,067  |
| Minority Interests                | m      | 6      | 6      | 37     | 422                       | Minority Interests                | m      | 6       | 6       | 37      | 422     |
| Other                             | m      | 0      | 0      | 0      | 0                         | Other                             | m      | 0       | 0       | 0       | 0       |
| <b>Total S/H Equity</b>           | m      | 23,630 | 24,761 | 26,180 | 29,490                    | <b>Total S/H Equity</b>           | m      | 23,630  | 24,761  | 26,180  | 29,490  |
| <b>Total Liab &amp; S/H Funds</b> | m      | 37,728 | 40,216 | 53,647 | 68,955                    | <b>Total Liab &amp; S/H Funds</b> | m      | 37,728  | 40,216  | 53,647  | 68,955  |

All figures in INR unless noted.

Source: Macquarie Research, February 2009

## Important disclosures:

| <p><b>Recommendation definitions</b></p> <p><b>Macquarie - Australia/New Zealand</b><br/> Outperform – return &gt;5% in excess of benchmark return<br/> Neutral – return within 5% of benchmark return<br/> Underperform – return &gt;5% below benchmark return</p> <p><b>Macquarie – Asia/Europe</b><br/> Outperform – expected return &gt;+10%<br/> Neutral – expected return from -10% to +10%<br/> Underperform – expected return &lt;-10%</p> <p><b>Macquarie First South - South Africa</b><br/> Outperform – expected return &gt;+10%<br/> Neutral – expected return from -10% to +10%<br/> Underperform – expected return &lt;-10%</p> <p><b>Macquarie - Canada</b><br/> Outperform – return &gt;5% in excess of benchmark return<br/> Neutral – return within 5% of benchmark return<br/> Underperform – return &gt;5% below benchmark return</p> <p><b>Macquarie - USA</b><br/> Outperform (Buy) – return &gt;5% in excess of benchmark return<br/> Neutral (Hold) – return within 5% of benchmark return<br/> Underperform (Sell) – return &gt;5% below benchmark return</p> <p><b>Recommendations – 12 months</b></p> <p><b>Note:</b> Quant recommendations may differ from Fundamental Analyst recommendations</p> | <p><b>Volatility index definition*</b></p> <p>This is calculated from the volatility of historical price movements.</p> <p><b>Very high–highest risk</b> – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.</p> <p><b>High</b> – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.</p> <p><b>Medium</b> – stock should be expected to move up or down at least 30–40% in a year.</p> <p><b>Low–medium</b> – stock should be expected to move up or down at least 25–30% in a year.</p> <p><b>Low</b> – stock should be expected to move up or down at least 15–25% in a year.</p> <p>* Applicable to Australian/NZ/Canada stocks only</p> | <p><b>Financial definitions</b></p> <p>All "Adjusted" data items have had the following adjustments made:<br/> Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives &amp; hedging, IFRS impairments &amp; IFRS interest expense<br/> Excluded: non recurring items, asset revals, property revals, appraisal value uplift, preference dividends &amp; minority interests</p> <p><b>EPS</b> = adjusted net profit / efpowa*<br/> <b>ROA</b> = adjusted ebit / average total assets<br/> <b>ROA Banks/Insurance</b> = adjusted net profit / average total assets<br/> <b>ROE</b> = adjusted net profit / average shareholders funds<br/> <b>Gross cashflow</b> = adjusted net profit + depreciation<br/> *equivalent fully paid ordinary weighted average number of shares</p> <p>All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).</p> |        |        |        |        |     |    |     |            |        |        |        |        |        |        |         |        |        |        |        |        |        |              |        |        |       |       |       |       |
|---|---|--|--------|--------|--------|--------|-----|----|-----|------------|--------|--------|--------|--------|--------|--------|---------|--------|--------|--------|--------|--------|--------|--------------|--------|--------|-------|-------|-------|-------|
| <p><b>Recommendation proportions – For quarter ending 31 December 2008</b></p> <table border="1"> <thead> <tr> <th></th> <th>AU/NZ</th> <th>Asia</th> <th>RSA</th> <th>USA</th> <th>CA</th> <th>EUR</th> </tr> </thead> <tbody> <tr> <td>Outperform</td> <td>38.55%</td> <td>50.61%</td> <td>64.52%</td> <td>53.13%</td> <td>65.55%</td> <td>43.00%</td> </tr> <tr> <td>Neutral</td> <td>41.82%</td> <td>15.92%</td> <td>25.81%</td> <td>40.63%</td> <td>27.73%</td> <td>48.00%</td> </tr> <tr> <td>Underperform</td> <td>19.64%</td> <td>33.47%</td> <td>9.68%</td> <td>6.25%</td> <td>6.72%</td> <td>9.00%</td> </tr> </tbody> </table>   |   |  |        | AU/NZ  | Asia   | RSA    | USA | CA | EUR | Outperform | 38.55% | 50.61% | 64.52% | 53.13% | 65.55% | 43.00% | Neutral | 41.82% | 15.92% | 25.81% | 40.63% | 27.73% | 48.00% | Underperform | 19.64% | 33.47% | 9.68% | 6.25% | 6.72% | 9.00% |
|   | AU/NZ   | Asia   | RSA    | USA    | CA     | EUR    |     |    |     |            |        |        |        |        |        |        |         |        |        |        |        |        |        |              |        |        |       |       |       |       |
| Outperform  | 38.55%  | 50.61%   | 64.52% | 53.13% | 65.55% | 43.00% |     |    |     |            |        |        |        |        |        |        |         |        |        |        |        |        |        |              |        |        |       |       |       |       |
| Neutral   | 41.82%  | 15.92%   | 25.81% | 40.63% | 27.73% | 48.00% |     |    |     |            |        |        |        |        |        |        |         |        |        |        |        |        |        |              |        |        |       |       |       |       |
| Underperform  | 19.64%  | 33.47%   | 9.68%  | 6.25%  | 6.72%  | 9.00%  |     |    |     |            |        |        |        |        |        |        |         |        |        |        |        |        |        |              |        |        |       |       |       |       |

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