

Reliance Power

Neutral

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Issue Open: 15 January 2008

Issue Close: 18 January 2008

Issue Details

Face Value: Rs10

Present Equity Capital: Rs2,000cr

Post Issue Equity Capital: Rs2,260cr

Total Issue size (shares): 26cr

Issue size (amt): Rs10,374cr – 11,544cr
(Including promoters contribution of 3.2cr shares)

Issue Price : Price Band of Rs405-450

Promoters holding pre-issue: 100%

Promoters holding post-issue: 89.9%

Book Building of the Net Issue

| | |
|-------------------|--------------|
| QIBs | Up to 60% |
| Non-Institutional | At least 10% |
| Retail* | At least 30% |
| Mutual Funds | 5% of QIB |

*Retail participants will get a discount of Rs20 from issue price

Post Issue Shareholding Pattern

| | |
|-------------------------------------|-------|
| Promoters Group | 89.9% |
| MF/Banks/Indian FIs/Public & Others | 10.1% |

Rationale for our Neutral view

Reliance Power's projects to be one of the largest in India: The upcoming 13 power projects by Reliance Power (RPL) are expected to have a combined planned installed capacity of 28,200MW, which will be one of the largest power generation portfolios under development in India.

Pan-India presence

RPL plans to develop 28,200MW of power projects on a pan-India scale. Highest contribution of power will be in West India (12,220MW) followed by North India (9,080MW), South India (4,000MW) and the North-Eastern states (2,900MW).

Strategic location of the projects: Majority of RPL's projects are located in the North, West and North-Eastern regions of India. These are expected to cater to the significant unmet demand for power in these regions. The power projects are also located either close to its fuel source or load center, which will help enhance RPL's efficiency.

Execution risks: RPL's projects under development have a long gestation period. Most of the projects are expected to be commissioned in or after FY2010. Projects could get delayed due to unforeseen engineering problems, unanticipated cost increase, delay in obtaining property rights, fuel supply, government approvals or termination of a project's development. Considering all this, we believe that execution risks cannot be ruled out.

We have a Neutral view on the Issue. We believe that the pricing of the Issue is a bit aggressive even though the business prospects are expected to be robust over the next several years for RPL, with an expected generation capacity of 5,500MW by 2012 and 28,200MW by 2016. Further, valuations should be seen considering the fact that currently RPL hardly has any capacity which is operating. The company's first power plant will get operational only by March 2010. This is assuming there are no execution delays.

As for relative valuations, RPL is being priced at a 'considerable' premium to NTPC, which already has an installed capacity of 27,000MW, good execution capabilities and a proven track record. Our calculations indicate that by FY2012, four of RPL's announced projects would be fully operational with a capacity of 5,500MW. Assuming an optimistic PLF of 80%, potential revenues could be in the vicinity of Rs8,500cr, which could help the company report an EPS of Rs6-7. Also, the Book Value in FY2012 (*sans* dilutions) would be Rs60-65 per share, which implies that the P/BV at the upper end of the price band would be 7-7.5x.

Nonetheless, considering the buoyancy in the capital markets, especially the primary market, we expect the IPO to receive good investor response along with follow-up appetite for the Issue on listing. Also, while further dilutions by the promoters in the future is a very high probability, which over a period of time would lead to significant Book Value accretion, we believe the same is already priced in.

Company overview

Reliance Power (RPL) is part of the Reliance ADA Group and was established to develop, construct and operate power projects in India and abroad. RPL is in the process of developing 13 medium and large sized power projects, which will create a combined planned installed capacity of 28,200MW and will be one of the largest portfolios of power generation assets under development in India. The upcoming 13 power projects will be diverse in terms of geographical location, fuel type and source, and off-take. RPL's installed capacities will be spread across the states in India with capacity of 12,220MW in West India, 9,080MW in North India, 2,900MW in North-East India and 4,000MW in the South. These include seven coal-fired projects of around 14,620MW, which will be fueled by reserves from the captive mines and supplies from India and abroad. Out of the total 13 projects, RPL has placed orders for two gas-fired projects of 10,280MW capacity, which is expected to be fueled from reserves from the Krishna-Godavari basin (KG Basin), and four hydroelectric projects of 3,300MW capacity. The power generated by these projects would be sold under a combination of long and short-term power purchase agreements (PPAs) to state-owned, private distribution companies and industrial consumers.

Exhibit 1: Objects of the Issue

| Objects | Amount (Rs cr) |
|------------------------------------------------------------------|----------------|
| Part finance construction and development of new projects | 8,642 |
| 600MW Rosa Phase I | 393.2 |
| 600MW Rosa Phase II | 615.0 |
| 300MW Butibori | 411.5 |
| 3,960MW Sasan | 5,461.4 |
| 1,200MW Shahapur Coal | 1,145.8 |
| 400MW Urthing Sobla | 615.8 |
| General Corporate Expenses | {-} |
| Issue Expenses | {-} |
| Total Proceeds | {-} |

Source: RHP

RPL is raising funds to develop 13 power generation projects that are currently under various stages of development. The company has already commenced construction of the Rosa Phase I.

Exhibit 2: Projects at a glance

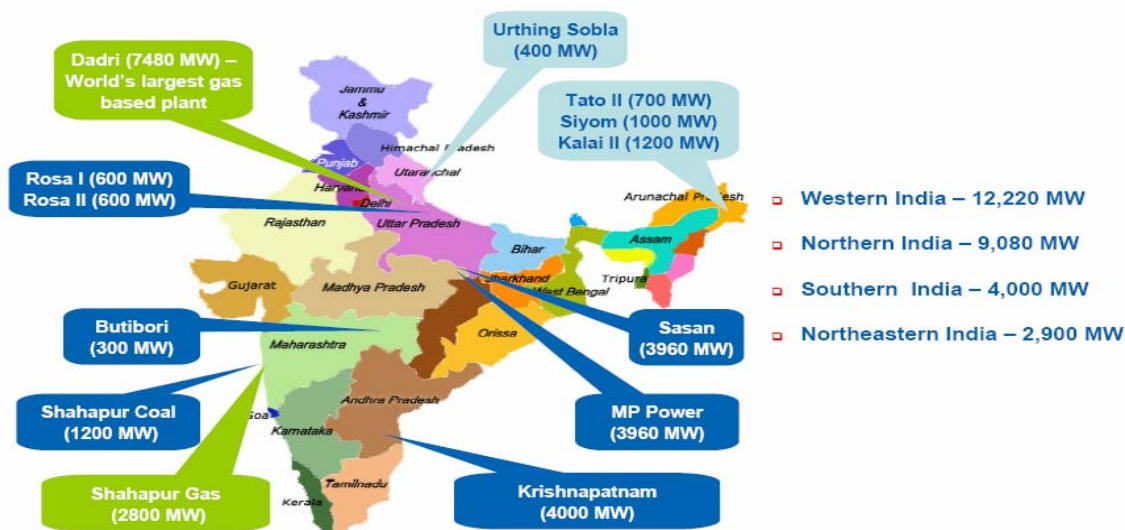
| Project break-up | Capacity (MW) | Type | Location | Commission |
|------------------|---------------|---------------------------------------------|----------------|------------------------|
| Rosa Phase I | 600 | Coal-fired | Uttar Pradesh | March 2010 |
| Rosa Phase II | 600 | Coal-fired | Uttar Pradesh | Sept 2010 |
| Butibori | 300 | Coal-fired | Maharashtra | June 2010 |
| Sasan | 3,960 | UMPP, coal-fired | | April 2016 |
| Shahapur | 4,000 | Coal-fired (1,200MW) Gas-fired (2,800MW) | Maharashtra | Dec 2011 March 2011 |
| Urthing Sobla | 400 | Hydroelectric | Uttarakhand | March 2014 |
| Dadri | 7,480 | Gas-fired | Uttar Pradesh | Under Dev. |
| MP Power | 3,960 | Coal-fired | | Under Dev. |
| Krishnapatnam | 4,000 | UMPP, Coal-fired | Andhra Pradesh | Under Dev. |
| Siyom | 1,000 | Hydroelectric | | Under Dev. |
| Tato II | 700 | Hydroelectric | | Under Dev. |
| Kalai II | 1,200 | Hydroelectric | | Under Dev. |

Source: RHP

Competitive strengths

RPL's power projects to be one of the largest in India: The upcoming 13 power projects would have a combined planned installed capacity of 28,200MW and will be one of the largest power generation portfolios under development in India. This upcoming portfolio of 13 power projects includes:

Exhibit 3: Pan India presence



Source: Company

RPL plans to develop 28,200MW of power projects on a pan-India basis. Highest contribution of power will lie in West India (12,220MW) followed by North India (9,080MW), South India (4,000MW) and North-East India (2,900MW).

Strategic location of projects: Majority of RPL's projects are located in the North, West and North-East parts of India. These are expected to cater to the significant un-met demand for power in these regions. Further, the proposed power projects are located either close to their fuel source or load center, which is expected to improve RPL's efficiency.

Diversified portfolio of power projects: The upcoming power projects are diverse in terms of geographic location, off-take, fuel type and source. These include seven coal-fired projects (14,620MW), two gas-fired projects (10,280MW) and four run-of-the-river hydroelectric projects (3,300MW). RPL plans to source coal from captive mines and supplies from India and abroad. The company also plans to source gas from the KG Basin through RNRL and others. The hydroelectric projects will be run-of-the-river projects, out of which three will be located in Arunachal Pradesh and one will be in Uttarakhand. With this diverse portfolio of power projects, RPL seeks to de-risk its business model. RPL will sell its power to state-owned and private distribution companies and industrial consumers.

Concerns

Execution risk: RPL's projects under development have a long gestation period. Most of the projects are expected to be commissioned in or after FY2010. Projects could get delayed due to unforeseen engineering problems, unanticipated cost increase, delay in obtaining property rights, fuel supply, government approvals or termination of a project's development. Considering all of this, we believe that execution risks cannot be ruled out.

Business is subject to government regulation: RPL's business is subject to government norms and regulations and any changes in these could disrupt/delay the company's plans and impact its business performance. In order to conduct its business, RPL will have to obtain various licenses, permits and approvals, indicating a pipeline of government clearances that could potentially delay procedures.

Industry overview

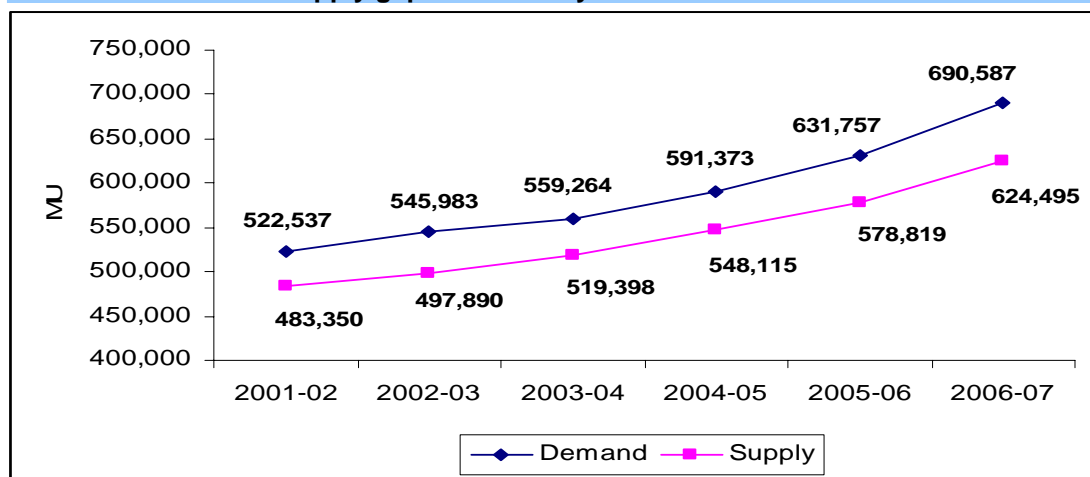
India is currently facing a demand-supply gap in power. This gap has been increasing, leading to increased power shortages.

Exhibit 4: Power – Demand-Supply Scenario in India

| Fiscal | Peak Deficit (MW) |
|----------------------|-------------------|
| 2001-02 | 10,293 |
| 2002-03 | 9,945 |
| 2003-04 | 9,508 |
| 2004-05 | 10,254 |
| 2005-06 | 11,463 |
| 2006-07 | 13,897 |
| April-September 2007 | 12,409 |

Source: CEA, Power Scenario at a glance, October 2007

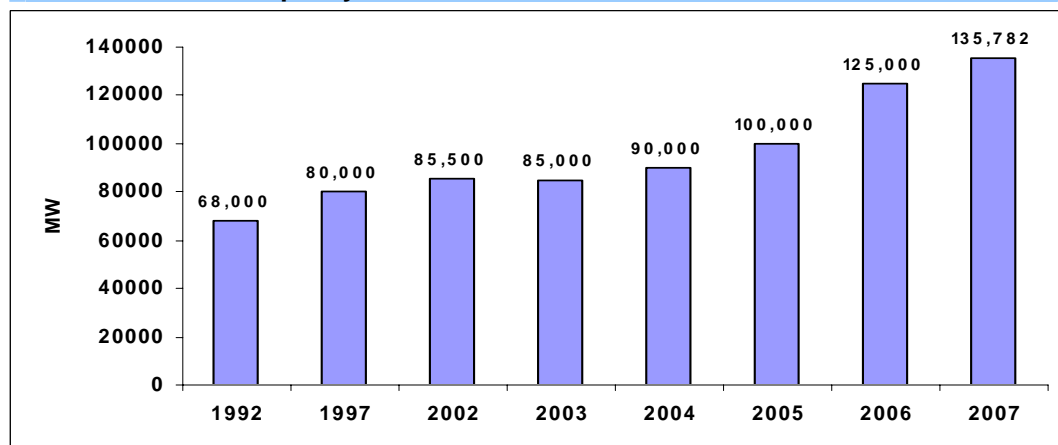
Peak demand deficit between April - September 2007 stood at 12,409MW. Peak deficit varies across India ranging from 5.8% of peak demand requirements in the South to 26.5% of peak demand requirement in the West.

Exhibit 5: Demand - Supply gap of Electricity in India


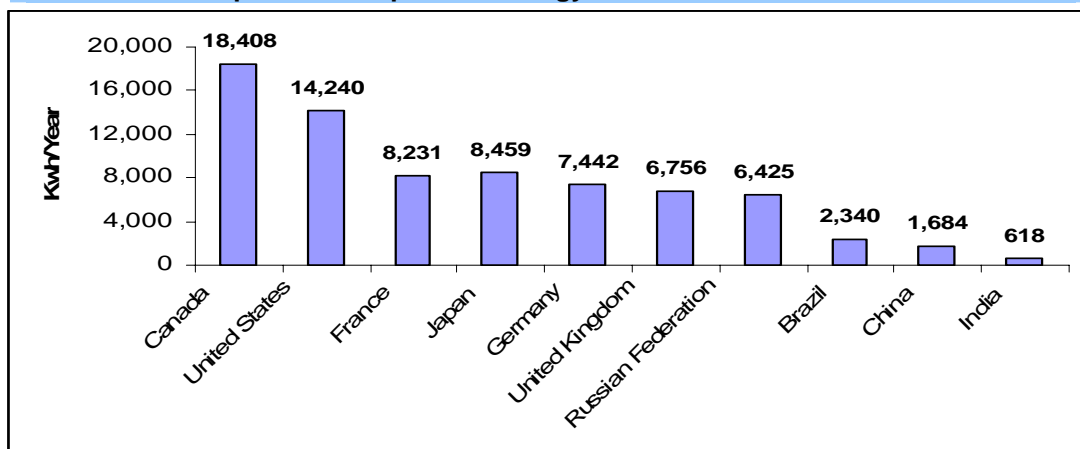
Source: CEA, Power Scenario at a glance, October 2007

Installed generation capacity

According to the Ministry of Power, India has an installed generation capacity of about 1,35,782MW as of September 30, 2007. Despite the economic liberalisation policies that have been in existence since 1992 and focused on the Power sector, the Indian Power sector has failed to grow at the required pace to meet the shortage of power in the country..

Exhibit 6: Overall capacity


Source: Ministry of Power

Exhibit 7: Per capita consumption of Energy


Source: *Company, World Energy Outlook, 2006; Human Development Report 2007-08*

Per capita consumption of energy in India is only 618Kwh/year, which indicates low penetration and provides significant opportunities for future growth. Currently, over 400 million in India do not have access to electricity. This provides immense scope for growth for the Power sector in India. The Government of India has set a target to achieve per capita electricity consumption of 1,000Kwh/year by 2012. To achieve this target large investments are required to flow into the sector.

Outlook and Valuation

We have a Neutral view on the issue. This is in keeping with the view that while RPL's business growth prospects remain robust for the next several years with expected generation capacity of 5,500MW by 2012 and 28,200MW by 2016, pricing of the Issue is a bit aggressive. Moreover, valuations must be seen in conjunction with the fact that currently, RPL has hardly any capacity which is operating. RPL's first power plant would be getting operational only by March 2010 assuming there are no execution delays.

On the relative valuations front, RPL is being priced at a 'considerable' premium to NTPC, while the latter already has an installed capacity of 27,000MW and with good execution capabilities and proven track record. Our calculations indicate that by FY2012, four of the announced projects would be fully operational with a capacity of 5,500MW. Assuming an optimistic PLF of 80% the company's potential revenues could be in the vicinity of Rs8,500cr, which could help the company report an EPS of Rs6-7. Also, the Book Value in FY2012 (*sans* dilutions) would be Rs60-65 per share, which implies that the P/BV at the upper end of the price band would be 7-7.5x.

Nonetheless, considering the buoyancy in the market, especially the primary market, we expect the IPO to receive good investor response along with follow-up appetite for the Issue on listing. Also, while further dilutions by the promoters in the future is a very high probability, which over a period of time would lead to significant Book Value accretion, we believe the same is already priced in.

| Exhibit 8 : Profit and Loss (Stand-alone) | | | | |
|--------------------------------------------------|---------------|---------------|---------------|-----------------|
| Y/E March | FY2005 | FY2006 | FY2007 | 1HFY2008 |
| Income | | | | |
| Income from contractual services | 0.00 | 0.00 | 2.25 | 0.00 |
| Profit on redemption of Mutual Fund | 0.00 | 0.00 | 0.00 | 3.21 |
| Miscellaneous Income | 0.00 | 0.00 | 0.00 | 0.02 |
| Net Sales | 0.00 | 0.00 | 2.25 | 3.23 |
| Net sales growth | | | | |
| Expenditure break-up | | | | |
| Employee cost | 0.00 | 0.00 | 0.25 | 0.00 |
| Admin. and general exp. | 0.01 | 0.11 | 0.64 | 1.45 |
| Bank/Corporate guarantee charges | 0.00 | 0.00 | 0.82 | 0.00 |
| Depreciation | 0.00 | 0.00 | 0.00 | 0.00 |
| Total expenditure | 0.01 | 0.11 | 1.71 | 1.45 |
| | | | | |
| PBT | (0.01) | (0.11) | 0.54 | 1.78 |
| | | | | |
| Provision for Tax | 0.00 | 0.02 | 0.38 | 0.60 |
| Current Tax (Includes FBT) | 0.00 | 0.02 | 0.38 | 0.60 |
| Deferred Tax | 0.00 | | | |
| | | | | |
| PAT | (0.01) | (0.13) | 0.16 | 1.18 |
| | | | | |
| Adj. due to change in accounting policy | | | | |
| Profit on redemption of MF | 0.00 | 0.00 | 1.68 | 0.00 |
| Total Adjustments | 0.00 | 0.00 | 1.68 | 0.00 |
| Tax impact of adjustments | 0.00 | 0.00 | 0.57 | 0.00 |
| Total adjustment after Tax impact | 0.00 | 0.00 | 1.11 | 0.00 |
| Net Profit | (0.01) | (0.13) | 1.27 | 1.18 |
| | | | | |
| P&L at the start of the year | (0.01) | (0.02) | (0.15) | 1.12 |
| Profit/(Loss) available for appropriation | (0.02) | (0.15) | 1.12 | 2.30 |
| Balance c/f | (0.02) | (0.15) | 1.12 | 2.30 |

Source: RHP

Exhibit 9: Balance Sheet (Stand-alone)

| Y/E March | FY2005 | FY2006 | FY2007 | 1HFY2008 |
|--------------------------------------------------|---------------|---------------|---------------|-----------------|
| Assets | | | | |
| Gross Fixed Assets | 0.30 | 66.77 | 67.27 | 67.29 |
| Less: Acc. Depreciation | 0.19 | 0.76 | 1.00 | 1.04 |
| Net Fixed Assets | 0.11 | 66.01 | 66.27 | 66.25 |
| Capital work in progress | 84.20 | 28.21 | 35.97 | 36.92 |
| | 84.31 | 94.22 | 102.24 | 103.17 |
| Incidental Exp Pending Allocation/Capitalisation | 3.88 | 7.79 | 16.96 | 20.83 |
| Investments | 0.02 | 0.01 | 41.28 | 1772.77 |
| Current Assets | | | | |
| Cash and Bank | 0.78 | 0.94 | 45.05 | 110.78 |
| Sundry Debtors | 0.70 | 0.59 | 0.78 | 0.52 |
| Loans and Advances | 0.00 | 0.00 | 2.25 | 0.00 |
| | 0.08 | 0.35 | 42.02 | 110.26 |
| Liabilities and Provisions | | | | |
| Secured Loans | 88.96 | 103.06 | 4.37 | 0.64 |
| Unsecured Loans | 0.00 | 0.00 | 0.00 | 0.00 |
| Share Application Money | 0.00 | 0.00 | 0.00 | 0.00 |
| Current Liabilities and Provisions | 88.36 | 102.36 | 0.00 | 0.00 |
| | 0.60 | 0.70 | 4.37 | 0.64 |
| Networth | 0.03 | (0.10) | 201.16 | 2006.91 |
| Share Capital | 0.05 | 0.05 | 200.04 | 2000.00 |
| Reserves and Surplus | (0.02) | (0.15) | 1.12 | 6.91 |
| Networth | 0.03 | (0.10) | 201.16 | 2006.91 |

Source: RHP

Exhibit 10: Cash Flow (Stand-alone)

| Y/E March | FY2005 | FY2006 | FY2007 | 1HFY2008 |
|--------------------------------------------------------|----------------|----------------|----------------|-----------------|
| Cash flow from operating activities | | | | |
| Net Profit/(Loss) before tax | (0.01) | (0.11) | 2.22 | 1.78 |
| Depreciation | 0.00 | 0.00 | 0.00 | 0.00 |
| Operating profit before working capital changes | (0.01) | (0.11) | 2.22 | 1.78 |
| Changes in trade and other receivables | (0.08) | (0.25) | (3.82) | 2.61 |
| Changes in trade and other payables | 0.46 | 0.07 | 2.72 | (4.32) |
| Cash from/(used) in operations | 0.37 | (0.29) | 1.12 | 0.07 |
| Income tax paid | 0.00 | (0.02) | (0.38) | (0.51) |
| Net cash from/(used) in operating activities | 0.37 | (0.31) | 0.74 | (0.44) |
| Cash flow from investing activities | | | | |
| Purchase of Fixed Assets | (72.05) | (13.81) | (17.19) | (4.80) |
| Loans and advances to subsidiaries | 0.00 | 0.00 | (39.72) | (68.09) |
| Purchase of investments | 0.00 | 0.00 | (96.72) | (823.76) |
| Sale of investments | 0.00 | 0.01 | 55.45 | 96.84 |
| Net cash from/(used) in investing activities | (72.05) | (13.80) | (98.18) | (799.81) |
| Cash flow from financing activities | | | | |
| Share application money/(adjusted) | 72.36 | 14.00 | 102.36 | 0.00 |
| Proceeds from share capital | 0.00 | 0.00 | 199.99 | 799.96 |
| Increase/(Decrease) in Unsecured Loans | (0.02) | 0.00 | 0.00 | 0.00 |
| Net cash from financing activities | 72.34 | 14.00 | 97.63 | 799.96 |
| Net (Decrease)/ Increase in cash | 0.66 | (0.11) | 0.19 | (0.29) |
| Cash and cash equivalents at the start of the year | 0.04 | 0.70 | 0.59 | 0.78 |
| Add: Cash received on amalgamation | 0.00 | 0.00 | 0.00 | 0.03 |
| Cash and cash equivalents at the end of the year | 0.70 | 0.59 | 0.78 | 0.52 |
| Net (Decrease)/ Increase as above | 0.66 | (0.11) | 0.19 | (0.29) |

Source: RHP



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