

Company Focus

30 January 2008 | 12 pages

Tata Power (TTPW.BO)

 Target price change

Buy: Strong Quarter of Growth

- Raising our target price** — We are raising our target price to Rs1,494 from Rs1,078 earlier on the back of: 1) rolling forward DCF value of core business to Dec 2008E (from Sep 08 earlier), 2) rollover of DCF value of Mundra UMPP and Maithon projects to Dec 2008E (from Mar 08), and (3) inclusion of a 1.6% stake value in TCS in our sum of the parts.
- Maintain Buy/Low Risk (1L)** — Tata Power is embarking on an ambitious, but measured plan of multiplying generation capacity six fold to 13GW in the next six years. Given the new aggressive management and a very good execution track record evident in its reduction of AT&C losses to 23% in five years in NDPL, we believe it has a very realistic chance of achieving these targets.
- 3QFY08 recurring PAT up 64% YoY** — Tata Power's 3QFY08 recurring PAT of Rs1.97bn (+64% YoY) was 8% ahead of our estimates of Rs1.82bn on the back of lower-than-expected tax. Reported PAT declined 30% YoY on the back of exceptional higher reversal of tax provisions in 3QFY07 arising out of favourable orders pertaining to the Mumbai licence area operations.
- Coal block allocation** — Tata Power has been allotted two coal mines (in Orissa and Jharkand) in which Tata Power's total share of indicated coal reserves is ~140mt, which is sufficient to support ~1,000MW new generation capacity. This could be a significant positive under the scenario of rising global coal prices.

Buy/Low Risk	1L
Price (30 Jan 08)	Rs1,287.10
Target price	Rs1,494.00
	<i>from Rs1,078.00</i>
Expected share price return	16.1%
Expected dividend yield	0.8%
Expected total return	16.9%
Market Cap	Rs268,484M
	US\$6,832M

Price Performance (RIC: TTPW.BO, BB: TPWR IN)


Figure 1. Statistical Abstract

Year to	Net Profit	EPS	EPS Growth	P/E	P / Book	ROE	Div. Yield	# Adj P/E	# Adj P/BV
31-Mar	(Rsmn)	(Rs)	(%)	(x)	(x)	(%)	(%)	(x)	(x)
FY2005A	3,894	19.7	-18.7%	65.4	5.6	8.6%	0.6%	15.3	1.3
FY2006A	4,371	20.6	4.5%	62.6	5.1	9.2%	0.7%	14.6	1.2
FY2007A	4,962	23.3	13.5%	55.1	4.7	9.5%	0.7%	12.9	1.1
FY2008E	5,752	24.7	5.8%	52.1	4.2	9.7%	0.8%	12.2	1.0
FY2009E	6,706	28.8	16.6%	44.7	3.8	9.8%	0.9%	10.4	0.9
FY2010E	8,048	34.6	20.0%	37.2	3.6	10.6%	1.0%	8.7	0.8

Source: Citi Investment Research estimates # Adjusted for the value of non parent business

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See Appendix A-1 for Analyst Certification and important disclosures.

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¹Citigroup Global Markets India Private Limited

Fiscal year end 31-Mar	2006	2007	2008E	2009E	2010E
Valuation Ratios					
P/E adjusted (x)	62.6	55.1	52.1	44.7	37.2
EV/EBITDA adjusted (x)	32.4	38.8	32.1	27.7	23.4
P/BV (x)	5.1	4.7	4.2	3.8	3.6
Dividend yield (%)	0.7	0.7	0.8	0.9	1.0
Per Share Data (Rs)					
EPS adjusted	20.56	23.34	24.70	28.80	34.57
EPS reported	27.44	32.77	24.70	28.80	34.57
BVPS	251.63	275.73	305.78	336.31	358.88
DPS	8.51	9.51	10.50	11.50	12.50
Profit & Loss (RsM)					
Net sales	45,203	46,590	54,498	60,698	66,260
Operating expenses	-40,027	-42,812	-49,518	-55,015	-59,474
EBIT	5,175	3,779	4,980	5,683	6,786
Net interest expense	-1,653	-1,895	-2,180	-2,321	-2,412
Non-operating/exceptionals	1,824	3,573	4,048	4,719	5,443
Pre-tax profit	5,347	5,457	6,848	8,081	9,817
Tax	-1,303	-694	-1,096	-1,374	-1,767
Extraord./Min.Int./Pref.div.	1,791	2,206	0	0	0
Reported net income	5,835	6,968	5,752	6,707	8,050
Adjusted earnings	4,371	4,962	5,752	6,707	8,050
Adjusted EBITDA	7,959	6,698	8,203	9,407	10,805
Growth Rates (%)					
Sales	16.3	3.1	17.0	11.4	9.2
EBIT adjusted	-6.0	-27.0	31.8	14.1	19.4
EBITDA adjusted	-12.5	-15.8	22.5	14.7	14.9
EPS adjusted	4.5	13.5	5.8	16.6	20.0
Cash Flow (RsM)					
Operating cash flow	4,287	7,553	5,908	8,737	10,426
Depreciation/amortization	2,783	2,919	3,223	3,724	4,018
Net working capital	-4,056	-2,553	-3,067	-1,694	-1,643
Investing cash flow	-1,558	-10,464	-20,035	-4,510	-5,154
Capital expenditure	-2,465	-8,885	-12,259	-2,357	-1,000
Acquisitions/disposals	908	-1,580	-7,776	-2,153	-4,154
Financing cash flow	-2,620	6,683	3,220	1,884	-4,370
Borrowings	-1,050	8,784	0	-1,247	-1,247
Dividends paid	-1,919	-2,202	-2,498	-2,873	-3,123
Change in cash	109	3,772	-10,906	6,112	901
Balance Sheet (RsM)					
Total assets	96,155	114,295	124,007	133,924	138,622
Cash & cash equivalent	9,906	13,677	2,771	8,882	9,781
Accounts receivable	10,582	14,782	17,407	19,462	21,220
Net fixed assets	32,148	38,114	47,149	45,782	42,764
Total liabilities	46,353	59,721	60,462	60,540	60,313
Accounts payable	5,489	8,934	9,473	10,403	11,152
Total Debt	27,550	36,334	36,334	35,086	33,839
Shareholders' funds	49,802	54,573	63,546	73,384	78,309
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	17.6	14.4	15.1	15.5	16.3
ROE adjusted	9.2	9.5	9.7	9.8	10.6
ROIC adjusted	9.0	6.3	6.5	6.5	7.6
Net debt to equity	35.4	41.5	52.8	35.7	30.7
Total debt to capital	35.6	40.0	36.4	32.3	30.2

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Maintain Buy, Target Price Rs1,494

We are raising our target price to Rs1,494 from Rs1,078 on the back of:

- Rolling forward our DCF to Dec 08E (from Sep08). We use a WACC of 10.3% (Rm-Rf = 6%, Rf = 8%, Beta = 0.85, after tax cost of debt = 6%, debt/capital = 40% and equity/capital = 60%).
- Rolling forward Mundra and Maithon DCF to Dec 08E (from Mar08).
- We also now include the value of the 1.6% stake in TCS in our SOTP.

In what we see as a measured plan, Tata Power is embarking on an ambitious multiplication of generation capacity by four-fold to 10GW in the next five years, and six-fold to 13GW in the next seven years. Given the new aggressive management and a good execution record evident when it cut AT&C losses from 53% before privatization to 23% in five years in NDPL, we believe Tata Power has a realistic chance of achieving these targets. As a consequence, we maintain our Buy/Low (1L) risk rating.

Figure 2. Tata Power – Sum of the Parts

Part	Remarks	Value
Power Business (ex Delhi and Powerlinks)	DCF Value as of Dec 2008	507
NDPL (49% Stake)	3.0x FY07 Book Value	42
Power Links	2.0x FY07 P/Equity Investment	20
Value of Power Generation, Transmission and Distribution Business		570
Tata Teleservices (Maharashtra)	20% Discount to Current MV	27
Tata Teleservices	75% Premium to private Equity Value	113
Panatone Finvest (VSNL)	20% Discount to Current MV	87
Value of Telecom Investments		227
Mundra UMPP	DCF Value as of Dec 2008	223
Maithon Project	DCF Value as of Dec 2008	50
Bumi Resources (30% Stake)	20% discount to mkt cap - Acquisition amount	344
Tata BP Solar (49% Stake)	30x FY07 PAT	26
NELCO (Direct and Indirect Stake 50%)	20% Discount to Current MV	7
TCS (Indirect 1.6% stake)	20% Discount to Current MV	46
Total Value/Share		1,494

Source: Citi Investment Research estimates

Figure 3. India – Electric Utilities Comparables

	Rating	RIC Code	Price (Rs) 28/1/08	MCap (\$mn)	EPS 08E-10E	P/E			P/B			# Adj P/E			# Adj P/B		
						FY08E	FY09E	FY10E	FY08E	FY09E	FY10E	FY08E	FY09E	FY10E	FY08E	FY09E	FY10E
NTPC	3L	NTPC.BO	206	42,464	11%	21.1	18.9	17.1	3.2	2.9	2.6	20.4	18.3	16.5	3.1	2.8	2.6
TPWR	1L	TTPW.BO	1,287	6,832	18%	52.1	44.7	37.2	4.2	3.8	3.6	12.2	10.4	8.7	1.0	0.9	0.8
CESC	1L	CESC.BO	495	1,546	14%	18.7	16.0	14.3	1.7	1.6	1.4	11.2	9.6	8.5	1.0	0.9	0.9

Source: Citi Investment Research estimates; # Adjusted for non parent value

3QFY08 recurring PAT up 64% YoY

- Tata Power's 3QFY08 recurring PAT of Rs1.97bn (+64% YoY) was 8% ahead of our estimates of Rs1.82bn on the back of lower-than-expected tax. Reported PAT declined 30% YoY on the back of exceptional higher reversal

of tax provisions in 3QFY07 arising out of favourable orders pertaining to the Mumbai licence area operations.

Figure 4. Tata Power – 3QFY08 Results

	3QFY07	3QFY08	% Chg	3QFY08E	% Chg
Generation (MU)	3587	3672	2.4%	3700	3.2%
Sales (MU)	3655	3614	-1.1%	3900	6.7%
Power Sales	11,831	14,194	20.0%	13,706	15.8%
Realization (Rs/kwh)	3.24	3.93		3.51	
Contract Services	174	-	-100.0%	90	-48.3%
Sales	12,005	14,194	18.2%	13,796	14.9%
Staff Cost	551	370	-32.9%	790	43.4%
% of sales	4.6%	2.6%			
Cost of Power Purchased	1,202	506	-57.9%	1,371	14.0%
% of power sales	10.2%	3.6%		10.0%	
Cost of Fuel	7,140	9,642	35.0%	7,955	11.4%
Cost/Unit Generated	1.99	2.63		2.15	
% of power sales	60.3%	67.9%		58.0%	
Other Exp	1,005	1,042	3.6%	930	-7.5%
% of sales	8.4%	7.3%		6.7%	
Total Exp	9,898	11,559	16.8%	11,046	11.6%
EBITDA	2,108	2,635	25.0%	2,750	30.5%
% margin	17.6%	18.6%		19.9%	
Interest	(510)	(386)	-24.5%	(430)	-15.7%
Depreciation	(735)	(705)	-4.1%	(710)	-3.4%
Other Income	460	414	-9.9%	465	1.1%
PBT	1,322	1,960	48.2%	2,075	56.9%
Taxation	(117)	13	-111.2%	(249)	112.6%
Effective Tax Rate	8.9%	-0.7%		12.0%	
Recurring PAT	1,205	1,973	63.7%	1,826	51.5%
Contingency Provision	0	0		0	
Exceptional	1,594	0		0	
Reported PAT	2,799	1,973	-29.5%	1,826	-34.8%

Source: Company reports, Citi Investment Research estimates

Captive coal block allocation

- **Tubed coal block in Jharkhand:** Tata Power has a 40% share in the 140mn tonne Auranga coalfield in the Lathehar district of Jharkhand. It has entered a JV with Hindalco and Tubed Coal Mining Limited.
- **Mandakini coal block in Orissa:** The screening committee of the Ministry of Coal has allotted Mandakini Coal Block in Orissa, with proven reserves of 291mn tonnes, jointly to Tata Power, Jindal Photo and Monnet Ispat.

Update on capacity expansion

- **250MW Trombay unit 8:** Progressing as per schedule and will be commissioned by October 2008.
- **4,000MW, Mundra UMPP:** Progressing as per schedule. Orders for the main equipments have been placed and site preparatory works are in progress.

- **1,050MW Maithon power project:** Progressing as per schedule. Orders for the main equipment are placed and site preparatory works are underway.
- **Wind Farm Projects:** 50.4MW Khandke project was completed. Two additional wind projects of 50.4MW each are being developed in Jamnagar district, Gujarat and Gadag district. Orders have been placed with Enercon.
- **120MW Power Project at Haldia:** Progressing as per schedule, set for commissioning in 2008.
- **Captive power projects for Tata Steel:** The 120MW Power House #6 at Tata Steel Works, Jamshedpur and 120MW Unit # 5 at Jojobera are also progressing as per schedule and should be commissioned in FY09.

Figure 5. Tata Power – Projects Under Implementation

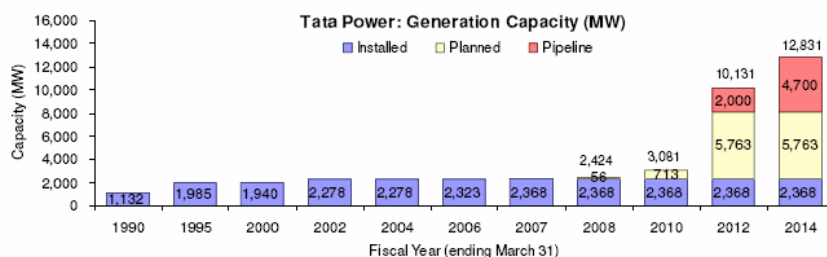
Project	Capacity (MW)	Fuel	Project Cost (Rsmn)	Project Cost (US\$m)	Per MW	Stake	Balance Stake	Commissioning - Status	
Capacity Being Added Through Parent									
Trombay Expansion	250	Imported Coal	9900	247.5	39.6	100%	NA	Oct 2008 - Main and BOP Order To BHEL - Boiler Drum Lifting Completed - Boiler Hydro in Feb 2008	
DG Sets	100	Diesel	3500	87.5	35.0	100%	NA	Early 2008	
Haldia Power Plant	90	Hot Flue Gases	4100	102.5	45.6	100%	NA	2008 - Waste heat recovery plant - 6MW to fuel supplier	
Haldia Power Plant	30	Hot Flue Gases	1367	34.2	45.6	100%	NA	2H 2008 - Boiler - Thermax, - Turbine – BHEL - BOP - Tata Projects	
Wind Capacity	137	Wind	6760	169	49.3	100%	NA	1H 2008 - 2H 2008 - Orders placed with Suzlon and Enercon - 50.4MW Khandke project commissioned	
Total	607		25627	641	42.2				
Capacity Being Added Through Subsidiaries									
Mundra	4000	Imported Coal	170000	4250	42.5	100%	NA	1H FY13 - 1H FY15 - Land Acquired - Coal from Bumi Resources - 10 MMTPA (+/- 20%) - BTG orders placed	
Maithon	1050	Domestic Coal	44,000	1100	41.9	74%	DVC	2H 2011 - 1120 acres (80% of land acquired) - BHEL for BTG/Long term coal linkage of 4.86MMTPA from BCCL - PPA for 300MW with DVC, MoU with TPTCL for 750MW	
IEL									
- Jamshedpur	120	Waste Gases	4,900	122.5	40.8	74%	Tata Steel	FY09 - Order placed with BHEL and Alstom	
- Jojobera	120	Domestic Coal	6,200	155.0	51.7	74%	Tata Steel	FY09 - Order placed with various vendors	
Total	5290		225100	5628	42.6				

Source: Tata Power, Citi Investment Research

Six-fold generation capacity growth in seven years

Tata Power has ambitious expansion plans to increase generation capacity four-fold to 10GW in the next five years and six-fold to 13GW in the next seven years

Figure 6. Perspective Plan Till FY14



Source: Tata Power, Citi Investment Research

Tata Power

Company description

Tata Power is one of the leading Indian power companies with interests in: generation (2,368MW of capacity), distribution (Delhi license area), transmission (Tala transmission project) and trading (Tata Power Trading).

Investment strategy

Tata Power has historically has been slightly conservative in its plans. The company's approach to growth has, however, undergone a sea change with the appointment of Prasad Menon as the MD and Gerald Grove-White as the COO prior to the bidding of the Sasan and Mundra UMPPs. With these appointments the company has started taking what we believe are measured risks. The key element of the Mundra bid was the management of imported coal prices. With the acquisition of the two coal mines of Bumi Resources, Tata Power has not only secured fuel supply for Mundra, but also acquired world class assets (evident from the Bumi Resources stock moving up 70%+ post the acquisition). We rate Tata Power Buy/ Low Risk (1L).

Valuation

Our Rs1,494 target price is based on sum-of-the-parts (SOTP) comprising:

- Parent business using DCF as of Dec 2008. We have used a WACC of 10.3% (Rm-Rf = 6%, Rf = 8%, Beta = 0.85, After Tax Cost of Debt = 6%, Debt/Capital = 40% and Equity/Capital = 60%).
- Tata Power's 49% stake in NDPL at 3.0x FY07 P/BV
- Tata Power's stake in Powerlinks is valued at 2.0x FY07 P/BV.
- Direct holdings in Tata Teleservices (Maharashtra) and direct/ indirect holdings in VSNL at 20% discount to market value.

- Stake in Tata Teleservices at a 75% premium to last transacted private equity value
- Mundra UMPP using a FCFE and Cost of Equity = 12% ($R_m - R_f = 6%$, $R_f = 8%$ and $Beta = 0.75$).
- The Maithon project in a similar manner as Mundra UMPP
- Valuing its 30% stake in Bumi's coal mines at a 30% discount to market value, less the acquisition cost
- Direct/indirect stake in NELCO is valued at a 20% discount to market value.
- The 49% stake in Tata BP Solar at 30x FY07 PAT.
- Indirect 1.6% stake in TCS at a 20% discount to market value.

Risks

We rate Tata Power shares Low Risk based on our quantitative risk-rating system, which tracks 260-day historical share price volatility. Key downside risks that could prevent the shares from reaching our target price are: 1) An unfavorable judgement in the MERC order petition and the standby charges case vs. Reliance Energy could negatively impact Tata Power. 2) The power sector is gradually liberalizing, but the regulatory and tariff structures are still evolving. Companies in the sector are vulnerable to delays, mid-term corrections and dramatic policy changes; under the existing system, litigation following any discord may be time consuming, and the lack of precedents adds uncertainty. 3) Delays and cost escalation in its capacity expansion and an unfavorable interest rate environment. The key upside risks which could drive the shares above our target price are: 1) Positive judgment on the MERC order and standby charges case vs. Reliance Energy could positively impact investor sentiment, even though it would not have any positive bearing on Tata Power's financials, by our estimates. 2) Tata Power exiting its telecom holdings at a significant premium to current market value. 3) Tata Power winning another UMPP at a reasonable tariff bid.

NTPC

Valuation

Our valuation methodology for NTPC involves setting a floor price for the stock and then valuing the value of growth opportunity (VGO) captured by our DCF calculation. We set a floor price of Rs168 for the NTPC stock using replacement cost of assets methodology and adding the value of power bonds and coal mining. However, we believe the replacement cost of method does not fully capture the upside inherent in NTPC's unprecedented capacity addition plan against a backdrop of persistent peak and base load deficits that is further exacerbated by rapid economic growth. To capture this value we use DCF methodology and set a target price of Rs231.

Risks

We rate NTPC as Low Risk according to our quantitative risk-rating system, which tracks 260-day historical share price volatility. Key risks on the upside include: 1) NTPC increasing its capacity additions plans for the XIth plan; 2) Faster-than-expected ramp up of capacity; 3) Positive change in the regulatory structure in terms of returns and incentives; 4) Any significant drop in interest rates leading to a fall in the cost of capital; and 5) Additional allocation of coal mines by the Ministry of Coal.

CESC

Valuation

Our target price to Rs777 is based on a sum of the parts. We value the power business using a DCF at Rs578. We also value the Haldia power project at a P/BV of 1.2x. We have valued CESC Plaza at Rs10 using a DCF and value the 35 acres of the Mulajore plant area at Rs20mn/acre. We also value CESC's 94% stake in Spencer's Retail at a 25% premium to the merger valuation giving us a value of Rs109/share. Further upside from target price would be possible once CESC takes a firm call on shutting down New Cossipore and decides to monetize the retail estate that would be freed up.

Risks

We rate CESC Low Risk, which differs from the Medium Risk rating assigned by our quantitative risk-rating system that tracks 260-day historical share price volatility. Key risks to CESC's operations and our earnings forecasts could emanate from: 1) the State Electricity Boards (SEBs) are still loss-making and trifurcation-corporatization-privatization process has yet to be completed; 2) given that India has a significant deficit of power, the big question for the sector remains whether private generating companies can earn the expected returns with adequate payment security; 3) following passage of the Electricity Act, a number of High Tension (HT) industrial consumers have set up captive capacity and are not purchasing power from the grid. CESC has faced similar problems in its license area. If the speed of switching to captive power increases beyond our expectation, CESC's operations could be negatively affected; 4) despite CESC having access to substantial coal for its operations, future growth beyond the Budge Budge operations will depend on its ability to secure captive mining blocks in Orissa and Jharkand; 5) free power has been a bane for the Indian electric utilities sector in the past. Although CESC's license area is unlikely to face such problems, this remains an area of risk; and 6) CESC's future capacity expansion depends on various regulatory authorities' clearances for land, water, fuel and project plans.

Appendix A-1

Analyst Certification

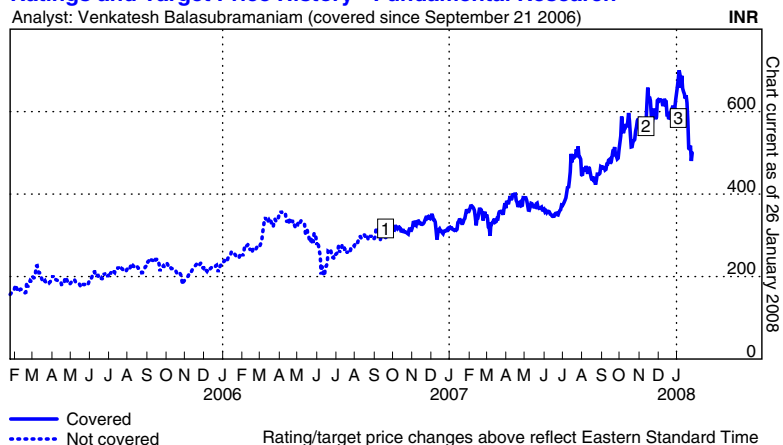
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IMPORTANT DISCLOSURES

CESC (CESC.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Venkatesh Balasubramaniam (covered since September 21 2006)



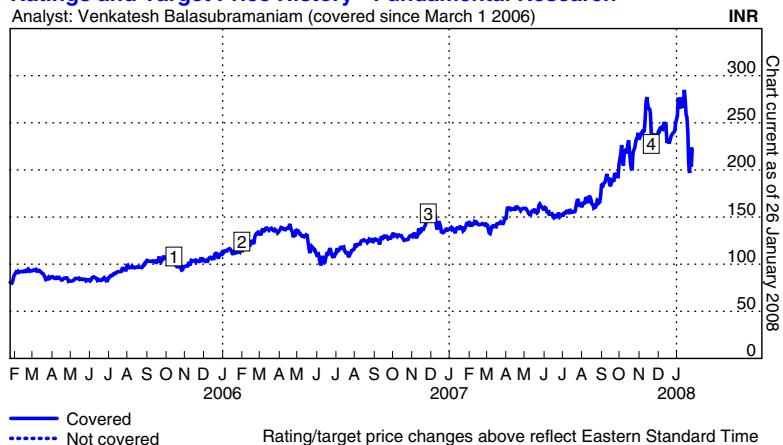
#	Date	Rating	Target Price	Closing Price
1:	20 Sep 06	1L	359.00	294.35
2:	13 Nov 07	1L	*650.00	571.00
3:	3 Jan 08	1L	*777.00	679.20

*Indicates change.

NTPC (NTPC.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Venkatesh Balasubramaniam (covered since March 1 2006)

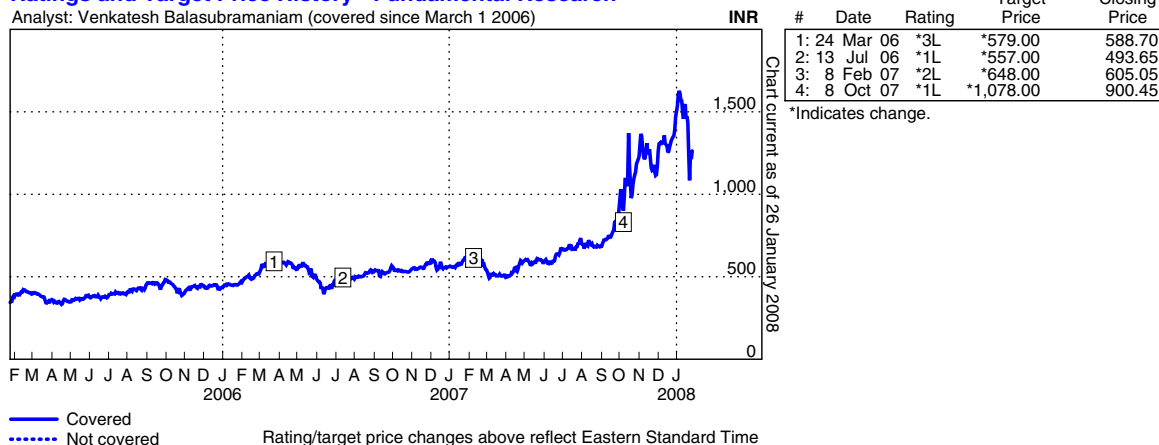


#	Date	Rating	Target Price	Closing Price
1:	14 Oct 05	1L	*120.00	102.65
2:	1 Feb 06	1L	*137.00	115.75
3:	28 Nov 06	1L	*181.00	149.85
4:	21 Nov 07	*3L	*231.00	239.50

*Indicates change.

Tata Power (TTPW.BO)
Ratings and Target Price History - Fundamental Research

Analyst: Venkatesh Balasubramaniam (covered since March 1 2006)



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Citigroup Global Markets Inc. or its affiliates expects to receive or intends to seek, within the next three months, compensation for investment banking services from NTPC.

Citigroup Global Markets Inc. or an affiliate received compensation for products and services other than investment banking services from CESC, NTPC and Tata Power in the past 12 months.

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