

# TATA POWER

## On the right path

India Equity Research | Power



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Tata Power (TPC) posted Q1FY13 adjusted PAT of ~INR4.7bn (our/consensus profit estimates INR5.2bn/INR4.3bn) largely on account of ~INR1bn of front-ended costs at Mundra UMPP as well as in coal companies ~INR1bn, forex loss of INR452mn and INR1.2bn reversal of tariffs in Mumbai licence area. Management expects benefits on higher blending and cost rationalisation at Mundra and Maithon (once fully operational) and scale up at coal mines to improve profitability. Maintain 'BUY' with TP of INR120/share.

### Earnings lower on front ending of costs, Mumbai tariff reversal

TPC's standalone Q1FY13 PAT of INR3.1bn was higher on account of higher treasury income and dividend from coal subsidiaries offset by INR1.6bn of revenue reversal on recent MERC regulations; adjusting for which, PAT at INR2.4bn was in line. However consolidated PAT at INR1.5bn was lower largely on account of higher-than-expected losses at Mundra UMPP (due to higher stabilisation/front ending of costs, fixed take-or-pay costs for port/ships). Lower realisation of USD84/t (USD94/t in Q1FY12), higher cash cost of USD48.9/t (USD40.2/t Q1FY12) due to upfront leasing /demurrage charges and higher amortisation of deferred costs capitalised at KPC/Arutmin mines dented profits of coal companies. Further, Maithon (1,050MW operational now) posted a loss of INR178mn as unit 1 boiler faced some problems during the quarter.

### Outlook and valuations: Positive; maintain 'BUY'

Management has been largely successful in restricting losses at Mundra's first unit to ~INR700mn in Q1FY13 through 70% ecocoal blending, leading to only INR5bn of annual loss in FY13. Earnings from Maithon project and volume scale up at coal mines are expected to improve earnings going ahead. TPC is working on ~6GW pipeline projects, of which ~10% are expected by FY15 at Kalinganagar. We have cut our FY13 earnings by 39% to factor in higher cash cost/upfront leasing costs in coal companies and front-ending of costs in Mundra UMPP. At CMP of INR101/share, the stock is trading at 1.8x and 1.6x FY13E and FY14E consolidated BV, respectively. Maintain 'BUY/SO' rating with SOTP based TP of INR120/share.

#### Financials (Consolidated)

(INR mn)

Year to March	Q1FY13	Q1FY12	% Change	Q4FY12	% Change	FY12	FY13E	FY14E
Revenues	72,539	58,245	24.5	72,348	0.3	260,014	263,636	317,686
EBITDA	14,129	14,234	(0.7)	14,601	(3.2)	53,253	61,589	82,409
Rep. net profit	1,459	4,304	(66.1)	(6,288)	(123.2)	(10,877)	10,936	18,250
Adj. net profit	4,752	5,542	(14.2)	5,308	(10.5)	15,001	10,936	18,250
Adj EPS (INR)						6.1	4.4	7.4
Price/BV(x)						2.0	1.8	1.6
ROAE (%)						11.7	8.7	13.3

#### EDELWEISS 4D RATINGS

Absolute Rating	BUY
Rating Relative to Sector	Outperformer
Risk Rating Relative to Sector	Low
Sector Relative to Market	Underweight

#### MARKET DATA (R: TTPW.BO, B: TPWR IN)

CMP	: INR 101
Target Price	: INR 120
52-week range (INR)	: 123 / 80
Share in issue (mn)	: 2,373.1
M cap (INR bn/USD mn)	: 239/ 4,309
Avg. Daily Vol.BSE/NSE('000)	: 4,232.5

#### SHARE HOLDING PATTERN (%)

	Current	Q4FY12	Q3FY12
Promoters %	31.8	31.8	31.8
MF's, FI's & BK's	25.6	26.6	28.6
FII's	23.0	21.9	20.0
others	19.6	19.8	19.5
* Promoters pledged shares (% of share in issue)	:		2.2

#### PRICE PERFORMANCE (%)

	Stock	Nifty	EW Power Index
1 month	(3.0)	0.9	(1.3)
3 months	1.3	7.0	1.5
12 months	(16.6)	4.9	(16.7)

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## Key concall takeaways

### Mundra UMPP

- First unit of 800MW commercialised in Q4FY12, operated at PLF of ~73% (PAF of 82%) generating total of 1.3bn units.
- CGPL, the subsidiary implementing UMPP, reported loss of INR1.65bn on revenue of INR2.85 (implied average realisation of INR2.4/unit for ~ 1.2bn units of sale). Higher fixed costs (loading of BoP cost on unit 1 and initial stabilisation costs) and higher fuel cost of INR2.5bn (INR400mn due to fixed take-or-pay contracts with port/ships) aggravated losses. Management has clarified that costs for the quarter are not indicative and the monthly rate would be ~ INR400mn of loss going ahead. EBITDA contribution has been positive from June.
- While blending in Q1FY12 was 40:60, from Q2FY12 70:30 (Ecocoal : high grade coal) blending has resulted in higher heat rate and aux consumption, but helped reduce fuel cost ~ 15 paisa/unit. Given the cost benefit, blending in this proportion is expected to continue.
- On tariff revision for the PPA, the company is still in negotiations with state discoms and only if these fail will it have to take up the issue with CERC. TPC in its petition has asked for complete fuel cost escalation in tariff. Management indicated a hike of ~INR0.40 paisa/unit for breakeven and ~INR0.65 paisa/unit to make reasonable returns in FY13.

### Maithon

- Both the units (2x525) are operational (second unit commercialised in July). However, for the quarter, TPC reported loss of INR180mn as unit 1 boiler faced some problems.
- Fuel has been tied up with CIL (with back up also in place) which will help in showing required availability to recover complete fixed cost on 75% of the capacity which is on regulated basis. Balance capacity is expected to be sold on merchant basis in FY13.

### Coal SPVs

- Production during Q1FY13 was 16.4 MT (15.54 MT in Q1FY12) and sale of 16.35 MT @ USD 84/t (USD94/t in Q1FY12). Cash cost shot up to USD48.92/t (40.5/t in Q1FY12) due to heavy rains leading to demurrage charges. Further, pre commission costs at KPC/Artmin mines and additional amortisation of the deferred capitalised cost have shot up coal processing costs (~USD8/tonne) during the quarter. TPC expects the full year target of 75MT sale to be back ended.

## SOTP valuations

Business segment	Methodology	Multiple	INR per share
Regulated power	P/BV	1.9	56
Mundra UMPP	NPV		(5)
BUMI	NPV		57
Cash & Investments	At par, Listed equities 25% disc, TTSL - 7x EV/Ebitda		12
<b>Total</b>			<b>120</b>

Source: Edelweiss research

**Financial snapshot**
**(INR mn)**

Year to March	Q1FY13	Q1FY12	% Change	Q4FY12	% Change	FY12	FY13E	FY14E
Sale of Electricity	71,976	58,048	24.0	71,699	0.4	260,014	263,636	317,686
Other operating income	563	197	186.0	649	(13.2)	-	-	-
Total operating income	72,539	58,245	24.5	72,348	0.3	260,014	263,636	317,686
Cost of goods sold	47,228	34,768	35.8	47,808	(1.2)	166,210	160,930	185,732
Fuel cost	29,784	19,605	51.9	27,770	7.3	100,808	77,606	85,324
Power purchase	16,606	14,477	14.7	17,131	(3.1)	61,226	79,091	95,306
Material and Component	838	687	21.9	2,907	(71.2)	4,176	4,234	5,102
Gross profit	25,311	23,477	7.8	24,540	3.1	93,804	102,705	131,954
Salaries,wages, other payments	3,098	2,432	27.4	2,901	6.8	11,463	11,622	14,005
Other expenses	8,084	6,811	18.7	7,038	14.9	29,089	29,494	35,540
Total expenditure	58,410	44,011	32.7	57,747	1.1	206,761	202,046	235,277
EBITDA	14,129	14,234	(0.7)	14,601	(3.2)	53,253	61,589	82,409
Other income	626	1,243	(49.7)	(1,071)	(158.4)	(1,563)	3,074	3,060
PBDIT	14,755	15,477	(4.7)	13,530	9.1	51,690	64,663	85,468
Depreciation	5,060	2,719	86.1	4,093	23.6	13,346	19,108	21,156
Interest	5,481	2,630	108.4	4,566	20.1	15,271	19,027	24,156
Profit before tax	4,214	10,129	(58.4)	4,871	(13.5)	23,073	26,527	40,157
Tax	2,263	5,089	(55.5)	2,796	(19.1)	14,755	14,113	19,954
Core profit	1,459	4,304	(66.1)	(6,288)	(123.2)	(10,877)	10,936	18,250
Adj. Net profit	4,752	5,542	(14.2)	5,308	(10.5)	15,001	10,936	18,250
No. of shares (mn)	2,373	2,373		2,373		2,459	2,459	2,459
Diluted EPS (INR)	2.0	2.3	(14.2)	2.2	(10.5)	6.1	4.4	7.4

**As % of net revenues**

COGS	65.1	59.7		66.1		63.9	61.0	58.5
Gross profit	34.9	40.3		33.9		36.1	39.0	41.5
Other expenses	15.4	15.9		13.7		15.6	15.6	15.6
Total expenses	80.5	75.6		79.8		79.5	76.6	74.1
EBITDA	19.5	24.4		20.2		20.5	23.4	25.9
Adjusted net profit	6.6	9.5		7.3		5.8	4.1	5.7
Tax rate	53.7	50.2		57.4		64.0	53.2	49.7

**Change in Estimates**

	FY13E			FY14E			Comments
	New	Old	% change	New	Old	% change	
Net Revenue	263,636	261,894	0.7	317,686	312,618	1.6	
EBITDA	61,589	69,006	(10.7)	82,409	83,484	(1.3)	Higher cash cost and depreciation assumed at KPC/Arutmin for FY13/FY14
EBITDA Margin	23.4	26.3		25.9	26.7		
Core profit	12,414	20,332	(38.9)	20,203	18,689	8.1	Loading higher interest/depreciation cost (of BoP) at Mundra UMPP , lower profits from Maithon in FY13. Proportionate interest/depreciation in FY14 for UMPP improves profits
PAT Margin	4.7	7.8		6.4	6.0		
Capex	41,848	41,848	0.0	8,650	8,650	0.0	

### Company Description

TPC is a pioneer in India's power sector, with a presence in all spheres of the power industry, encompassing generation, transmission, trading, and distribution. It has demonstrated exceptional performance in its transmission and distribution JVs. The company was also awarded the first UMPP at Mundra (Gujarat) due to its lowest levelised tariff bid at INR 2.26 per unit.

### Investment Theme

We believe TPC is poised to play an important role in the Indian power sector. All its plants under construction are on schedule, which exhibits the company's expertise in project execution. We expect the company to have an installed capacity of ~7,900 MW by FY13E. The company has 30% stake in two coal mines of Bumi Resources with proven reserves of ~1.9 bn tonnes. With rising coal prices, we believe, Tata Power will have significant profits from these assets.

### Key Risks

TPC is at an advanced stage of commissioning 3,200 MW of projects (one unit each of Mundra—4,000 MW and Maithon—1,050 MW already commercially operational). The dynamics of Indian electricity market has undergone a sea change due to higher imported coal prices, weak customer finances, changing fiscal norms at coal exporting countries and now a depreciating rupee. Hence, balancing between contractual supplies (both vols and price) and maximizing earnings has become a key determinant/risk.

The company had restated stripping costs by ~15% to 11.5 in 2010 which should have lead to upward restatement of reserves from 2.1 bn tonnes. However, recently the restatement was only to the extent of 20 mn tonnes. Unless another round of restatement is done or costs are brought down the value of coal mines could be suppressed.

## Financial Statements

### Key Assumptions

Year to March		FY10	FY11	FY12	FY13E	FY14E
<b>Macro -</b>	GDP(Y-o-Y %)	8.4	8.4	6.5	6.4	7.0
	Inflation (Avg)	3.6	9.9	8.8	7.0	6.0
	Repo rate (exit rate)	5.0	6.8	8.5	7.3	6.8
	USD/INR (Avg)	47.4	45.6	47.9	53.5	50.0
<b>Sector -</b>	Merchant prices (INR/kWh)	5.0	4.5	4.0	4.0	4.0
	New Castle 6700 Kcal (USD/t)	78	108	117	105	113
	Melawan 5400 Kcal (USD/t FoB)	56	77	89	74	79
<b>Company -</b>	Consol Reg Equity (INR mn)	44,875	54,599	71,136	76,375	81,664
	BUMI coal sales (MT)	58.0	61.0	65.0	70.0	75.0
	BUMI avg realisation (USD/t)	63.2	71.6	92.5	84.0	90.4
	BUMI PAT/t (USD)	4.7	7.3	18.4	9.9	14.4

### Income statement

(INR mn)

Year to March	FY10	FY11	FY12	FY13E	FY14E
Income from operations	189,858	193,482	260,014	263,636	317,686
Direct costs	116,764	117,786	162,035	156,696	180,630
Employee costs	8,060	8,259	11,463	11,622	14,005
Other Expenses	26,655	22,605	33,264	33,728	40,642
Total operating expenses	151,479	148,650	206,761	202,046	235,277
EBITDA	38,379	44,832	53,253	61,589	82,409
Depreciation & Amortization	8,777	9,802	13,346	19,108	21,156
EBIT	29,602	35,030	39,906	42,481	61,253
Other income	5,889	4,647	(1,563)	3,074	3,060
Interest expenses	7,818	8,102	15,271	19,027	24,156
Expenditure from provisions	-	-	18,000	-	-
Profit before tax	27,673	31,575	5,073	26,527	40,157
Provision for tax	6,287	9,756	14,755	14,113	19,954
Net profit	21,386	21,819	(9,683)	12,414	20,203
Extraordinary income/ (loss)	(1,916)	(565)	25,877	-	-
Profit after minority interest	17,753	20,031	15,001	10,936	18,250
Shares outstanding (mn)	2,443	2,443	2,459	2,459	2,459
Diluted EPS (INR)	8.1	8.4	(4.4)	4.4	7.4
Dividend per share (INR)	1.2	1.3	1.3	0.7	1.1
Dividend payout (%)	14.5	14.8	19.8	14.8	14.8

### Common size metrics - as % of net revenues

Year to March	FY10	FY11	FY12	FY13E	FY14E
Operating expenses	79.8	76.8	79.5	76.6	74.1
EBITDA margins	20.2	23.2	20.5	23.4	25.9
Net profit margins	11.3	11.3	(3.7)	4.7	6.4

### Growth ratios (%)

Year to March	FY10	FY11	FY12	FY13E	FY14E
Rev. growth (%)	8.0	1.9	34.4	1.4	20.5
EBITDA	13.9	16.8	18.8	15.7	33.8
Net profit	45.7	12.8	(25.1)	(27.1)	66.9
EPS growth (%)	46.2	4.7	(152.5)	(200.5)	66.9

Balance sheet					(INR mn)
As on 31st March	FY10	FY11	FY12E	FY13E	FY14E
Equity capital	2,373	2,373	2,373	2,373	2,373
Reserves & surplus	115,370	132,569	118,310	127,398	142,564
Shareholders funds	117,743	134,942	120,683	129,771	144,937
Minority interest (BS)	12,097	14,143	15,337	16,814	18,767
Secured loans	147,001	195,507	242,102	257,850	256,681
Unsecured loans	37,468	52,117	52,117	52,117	52,117
Borrowings	184,469	247,624	294,219	309,967	308,798
Others	10,660	11,144	11,144	11,144	11,144
<b>Sources of funds</b>	<b>324,970</b>	<b>407,853</b>	<b>441,383</b>	<b>467,696</b>	<b>483,646</b>
Gross block	182,280	201,388	261,942	364,602	441,102
Depreciation	74,549	83,295	96,642	115,750	136,906
Net block	107,731	118,093	165,301	248,852	304,196
Capital work in progress	116,927	195,751	174,171	113,359	45,509
Total fixed assets	224,658	313,844	339,471	362,211	349,705
Investments	30,823	28,410	28,410	28,410	28,410
Inventories	9,539	11,333	15,142	14,751	17,126
Sundry debtors	39,845	47,879	64,343	65,239	78,614
Cash and equivalents	23,108	22,066	9,695	12,764	25,469
Loans and advances	24,410	29,651	29,651	29,651	29,651
Total current assets	96,901	110,928	118,830	122,404	150,860
Sundry creditors and others	29,604	39,812	39,812	39,812	39,812
Provisions	44,477	55,274	55,274	55,274	55,274
Total current liabilities & provisions	74,081	95,087	95,087	95,087	95,087
Net current assets	22,821	15,842	23,744	27,318	55,773
Others	46,669	49,758	49,758	49,758	49,758
<b>Uses of funds</b>	<b>324,970</b>	<b>407,853</b>	<b>441,383</b>	<b>467,696</b>	<b>483,646</b>
Book value per share (INR)	49.6	56.9	50.9	54.7	61.1

Free cash flow					(INR mn)
Year to March	FY10	FY11	FY12E	FY13E	FY14E
Net profit	17,753	20,031	15,001	10,936	18,250
Depreciation	8,777	9,802	13,346	19,108	21,156
Others	2,739	(907)	(8,266)	17,204	22,669
Gross cash flow	29,268	28,927	20,081	47,249	62,075
Less: Changes in WC	4,839	(5,937)	20,273	505	15,750
Operating cash flow	24,430	34,864	(191)	46,743	46,325
Less: Capex	73,664	97,932	38,974	41,848	8,650
<b>Free cash flow</b>	<b>(49,234)</b>	<b>(63,068)</b>	<b>(39,165)</b>	<b>4,895</b>	<b>37,675</b>

Cash flow metrics					
Year to March	FY10	FY11	FY12E	FY13E	FY14E
Operating cash flow	24,430	34,864	(191)	46,743	46,325
Investing cash flow	(67,737)	(90,309)	(40,537)	(38,774)	(5,590)
Financing cash flow	55,953	54,142	28,358	(4,900)	(28,029)
Net cash flow	12,645	(1,302)	(12,371)	3,069	12,705
Capex	(73,664)	(97,932)	(38,974)	(41,848)	(8,650)
Dividends paid	(2,900)	(3,395)	(3,382)	(1,848)	(3,085)
Share issuance/(buyback)	2,712	923	-	-	-

**Profitability & efficiency ratios**

Year to March	FY10	FY11	FY12E	FY13E	FY14E
ROAE (%)	17.2	15.9	11.7	8.7	13.3
ROACE (%)	11.6	10.4	10.1	10.0	13.7
Debtors days	67	83	79	90	83
Current ratio	1.3	1.2	1.2	1.3	1.6
Debt/EBITDA	4.8	5.5	5.5	5.0	3.7
Average working capital turnover	7.4	9.1	9.6	7.6	6.3
Average capital employed turnover (x)	0.7	0.5	0.6	0.6	0.7
Debt/Equity	1.6	1.8	2.4	2.4	2.1
Adjusted debt/equity	1.6	1.8	2.4	2.4	2.1

**Operating ratios**

Year to March	FY10	FY11	FY12E	FY13E	FY14E
Total asset turnover	0.7	0.5	0.6	0.6	0.7
Fixed asset turnover	1.9	1.7	1.8	1.3	1.1
Equity turnover	1.8	1.5	2.0	2.1	2.3

**Valuation parameters**

Year to March	FY10	FY11	FY12E	FY13E	FY14E
Diluted EPS (INR)	8.1	8.4	(4.4)	4.4	7.4
Y-o-Y growth (%)	46.2	4.7	(152.5)	(200.5)	66.9
CEPS (INR)	140.2	144.7	26.4	139.1	182.5
Diluted PE (x)	12.5	11.9	(22.7)	22.6	13.5
Price/BV (x)	2.0	1.8	2.0	1.8	1.6
EV/Sales (x)	2.0	2.3	2.0	2.0	1.6
EV/EBITDA (x)	9.9	10.0	9.6	8.5	6.2
Dividend yield (%)	1.2	1.2	1.2	0.7	1.1

**Peer comparison valuation**

	Price	Market cap (INR mn)	P/BV(x)		EV/EBITDA(x)		RoE (%)	
			2013E	2014E	2013E	2014E	2013E	2014E
Adani Power	42	91,125	1.6	1.3	18.5	6.7	(5.6)	22.2
CESC	303	37,868	0.7	0.7	5.2	5.0	8.9	8.5
JSW Energy	52	85,775	1.4	1.2	6.5	5.1	11.2	13.6
NTPC	170	1,401,317	1.8	1.7	10.9	9.6	11.9	12.5
Power Grid Corp of India	119	551,169	2.1	1.9	10.7	9.4	14.8	16.6
<b>Average</b>			<b>1.6</b>	<b>1.4</b>	<b>10.1</b>	<b>7.0</b>	<b>8.3</b>	<b>14.4</b>
<b>Tata Power Co</b>	<b>101</b>	<b>238,635</b>	<b>1.8</b>	<b>1.6</b>	<b>8.5</b>	<b>6.2</b>	<b>8.7</b>	<b>13.3</b>

Source: Edelweiss research

Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
Adani Enterprises	BUY	SP	M	Adani Ports and Special Economic Zone	BUY	SO	M
Adani Power	REDUCE	SU	M	CESC	BUY	SU	H
GMR Infrastructure	BUY	SO	H	GVK Power and Infra	HOLD	SU	H
JSW Energy	HOLD	SP	H	Lanco Infratech	BUY	SU	H
Marg	BUY	None	None	Navabharat Ventures	BUY	None	None
NTPC	HOLD	SU	L	Power Grid Corp of India	BUY	SO	L
PTC India	BUY	None	None	Reliance Infrastructure	BUY	SO	M
Tata Power Co	BUY	SO	L				

## ABSOLUTE RATING

Ratings	Expected absolute returns over 12 months
Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

## RELATIVE RETURNS RATING

Ratings	Criteria
Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
	Stock return < 1.25 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

## RELATIVE RISK RATING

Ratings	Criteria
Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

## SECTOR RATING

Ratings	Criteria
Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
	Sector return < 1.25 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return



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**Coverage group(s) of stocks by primary analyst(s): Power**

Adani Power, Adani Enterprises, Adani Ports and Special Economic Zone, CESC, GMR Infrastructure, GVK Power and Infra, JSW Energy, Lanco Infratech, Marg, Navabharat Ventures, NTPC, PTC India, Power Grid Corp of India, Reliance Infrastructure, Tata Power Co

**Recent Research**

Date	Company	Title	Price (INR)	Recos
08-Aug-12	<b>GVK Power &amp; Infra.</b>	Balance sheet concerns come to fore; <i>Result Update</i>	13	Hold
06-Aug-12	<b>Adani Power</b>	Triad of issues impacts earnings; <i>Result Update</i>	43	Reduce
02-Aug-12	<b>NTPC</b>	Superior coal supplies boost profit; <i>Result Update</i>	158	Hold

**Distribution of Ratings / Market Cap**

Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	104	60	18	183
* 1 stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	114	58	11	

**Rating Interpretation**

Rating	Expected to
<b>Buy</b>	appreciate more than 15% over a 12-month period
<b>Hold</b>	appreciate up to 15% over a 12-month period
<b>Reduce</b>	depreciate more than 5% over a 12-month period

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