

NTPC | BUY

Adj. Profit growth begins to reflect capacity addition benefits

NTPC's 1QFY19 adjusted net profit stood at INR 25bn, +11% YoY vs. 5-6% growth trend of past quarters. This compares with 16%YoY growth in regulated equity as the benefit of capex is now beginning to reflect in earnings growth. During the quarter NTPC witnessed a) reduction in coal under-recovery from c. INR 3.5bn in 3QFY18 to INR 1.3bn as Mauda was the only impacted project, b) fixed cost under recoveries of INR 1.6bn in Unchahar and Badarpur which will discontinue by 2H FY19 and c) INR 2bn fixed cost under recovery from annual maintenance shutdowns which got advanced to 1Q in FY19 vs. 2Q in FY18. Without the shutdown related under-recoveries, we estimate profit growth to have been c.15%. Hence we expect strong growth in 2Q and 3Q FY19 given that the O&M related shutdowns have been completed in advance for many projects in FY19. As highlighted in our earlier reports, the issues related to coal shortages in newly-commissioned plants has been arrested as reflected in Mar-April'18 plant availability (PAF). We expect the coal situation to improve by 1HFY19 given efforts by NTPC and measures taken by Power, Coal and Railway Ministries (detailed report). The current scenario of stable power demand growth strengthens our long-term thesis of NTPC benefitting from capacity additions and improving PLFs. We expect NTPC to add 4-5GW annually in FY19 and FY20 resulting in >12% earnings CAGR despite, assuming 18% core RoE (vs. a run rate of 20%). With inexpensive valuations of c.1x FY20 BV, we reiterate our BUY rating with a TP of INR 215.

- **1QFY19 adj. profit +11% YoY; Core RoE at 21%:** NTPC's 1QFY19 adjusted net profit stood at INR 25bn +11% YoY vs. previous run rate of 5-6% growth. During the quarter NTPC witnessed a) reduction in coal under-recovery from c INR 3.5bn in 3QFY18 to INR 1.3bn in 1QFY19, with Mauda being the only impacted project, b) fixed cost under recoveries of INR 1.3bn in Unchahar which will stop as the plant restarts in 3QFY18, c) INR 300mn fixed cost under-recovery in Badarpur to be recovered post CERC order and d) INR 2bn under recoveries on account of annual maintenance shutdowns, which got scheduled in 1Q in FY19 vs. 2Q in FY18 (Exhibit 2). Without the shutdown related under-recoveries, we estimate profit growth to have been c.15%. Hence we expect strong growth in 2Q and 3Q FY19 given that the O&M related shutdowns have been completed in advanced for many projects in FY19. The coal related issues at Mauda are also expected to phase out over the year as PAFs continue to show improvement (Exhibit 2).
- **Falling all-India capex to improve PLFs / CERC approach paper:** With slower investments in thermal power by private sector and shutdown of older capacities, SEB continue to prefer purchasing from capacities signed PPAs and low costs. In a rising power demand scenario we find NTPC benefitting as its PLFs rise over a period of time. The CERC approach paper outlines some positives like grandfathering of RoE revision (see report) along with tightening of norms, new tariff model etc. Even considering the bear case where all the stringent norms and new 3-part tariff model get accepted (unlikely in our view), we find no downside for NTPC as the CMP implies only 14% RoE vs. 20% historical run rate. **Risk to our call:** Delayed capacity addition and higher impact from adverse CERC norms.



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Recommendation and Price Target

Current Reco.	BUY
Previous Reco.	BUY
Current Price Target (12M)	215
Upside/(Downside)	38.8%
Previous Price Target	220
Change	-2.3%

Key Data – NTPC IN

Current Market Price	INR155
Market cap (bn)	INR1,277.6/US\$18.6
Free Float	25%
Shares in issue (mn)	8,245.5
Diluted share (mn)	8,245.5
3-mon avg daily val (mn)	INR967.4/US\$14.1
52-week range	188/149
Sensex/Nifty	37,337/11,278
INR/US\$	68.7

Price Performance

%	1M	6M	12M
Absolute	0.7	-9.9	-6.3
Relative*	-5.0	-13.0	-18.7

* To the BSE Sensex

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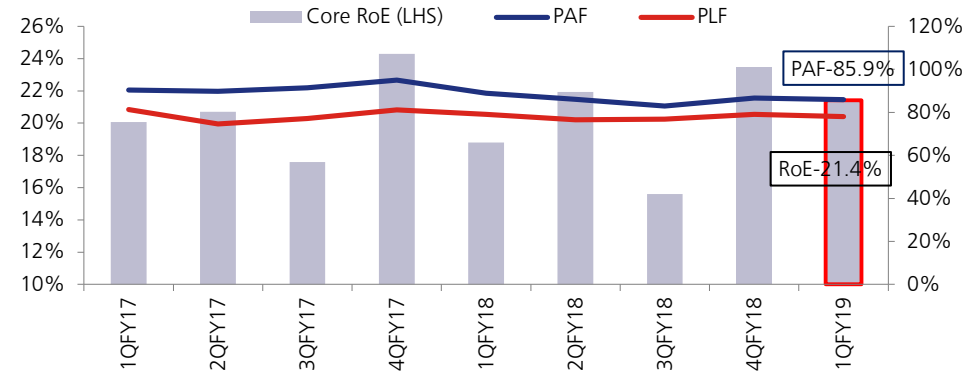
Financial Summary	(INR mn)				
Y/E March	FY16A	FY17A	FY18A	FY19E	FY20E
Net Sales	7,08,438	8,20,425	8,80,833	9,77,916	10,62,173
Sales Growth (%)	-2.5	15.8	7.4	11.0	8.6
EBITDA	1,78,871	2,17,585	2,29,808	2,72,132	2,91,778
EBITDA Margin (%)	25.2	26.5	26.1	27.8	27.5
Adjusted Net Profit	91,231	1,04,902	1,08,000	1,26,659	1,32,601
Diluted EPS (INR)	11.1	12.7	13.1	15.4	16.1
Diluted EPS Growth (%)	10.3	15.0	3.0	17.3	4.7
ROIC (%)	8.6	7.0	6.4	6.9	6.9
ROE (%)	10.7	11.3	10.9	11.8	11.3
P/E (x)	14.0	12.2	11.8	10.1	9.6
P/B (x)	1.4	1.3	1.3	1.1	1.0
EV/EBITDA (x)	11.7	10.4	10.4	8.9	8.2
Dividend Yield (%)	1.6	1.6	1.6	1.6	1.6

Source: Company data, JM Financial. Note: Valuations as of 27/Jul/2018

JM Financial Research is also available on:
Bloomberg - JMFR <GO>,
Thomson Publisher & Reuters
S&P Capital IQ and FactSet

Please see Appendix I at the end of this report for Important Disclosures and Disclaimers and Research Analyst Certification.

Exhibit 1. Core RoEs improve in 1QFY19 driven by PAFs



Source: Company, JM Financial

Core RoE recovers in 1Q19 as PAFs improve on better coal sourcing

Exhibit 2. Improving trend of PAFs

Plant	Units	Capacity (MW)	Average PAF					Remarks
			1QFY18	2QFY18	3QFY18	4QFY18	1Q FY19	
Farakka	1,2,3,4,5	1,600	57.5	86.5	84.1	84.6	73.2	Annual Maintenance
Farakka	6	500	97.4	92.7	74.0	80.3	89.0	Improving trend
Kahalgaoon	1,2,3,4	840	96.9	94.0	81.5	82.7	94.0	Improving trend
Kahalgaoon	5,6,7	1,500	96.1	88.5	95.2	96.0	82.3	
Talcher New	1,2	1,000	84.0	94.6	73.3	94.1	91.1	
Barh II	1,2	1,320	100.0	70.7	87.1	98.7	90.5	
Dadri NCTPP	1,2,3,4	840	106.0	78.1	90.9	99.0	90.8	
Dadri NCTPP	5,6	980	105.4	85.6	89.4	69.5	93.1	Improving trend
Rihand	1,2	1,000	99.8	87.2	97.0	85.1	78.9	Annual Maintenance
Rihand	3,4	1,000	50.3	94.5	99.7	98.9	73.9	
Rihand	5,6	1,000	96.6	82.7	97.6	100.0	95.3	
Singrauli	All	2,000	85.0	92.5	81.1	82.5	73.8	Annual Maintenance
Unchahar	1,2	420	100.4	97.4	65.0	96.6	97.5	
Unchahar	3,4	420	105.8	97.4	86.9	99.9	99.6	
Unchahar	5	210	92.1	100.5	98.6	99.6	69.2	Annual Maintenance
Ramagundem	1,2,3,4,5,6	2,100	87.6	96.3	90.5	88.9	93.8	Improving trend
Ramagundem	7	500	101.7	90.5	100.4	99.1	94.9	
Talcher New	3,4,5,6	2,000	91.3	79.0	91.8	98.3	91.6	
Simhadri	3,4	1,000	74.1	75.3	81.5	96.9	71.2	Annual Maintenance
Korba	1,2,3,4,5,6	2,100	96.2	93.0	81.4	93.1	91.8	
Korba	7	500	100.0	71.0	94.6	97.1	93.5	
Mauda I	1,2	1,000	99.3	79.0	56.7	78.6	63.7	Annual Maintenance
Sipat	1,2	1,000	100.3	96.8	96.6	68.2	98.5	Improving trend
Sipat	3,4,5	1,980	96.5	99.8	74.9	94.7	90.6	
Vindhyachal	1,2,3,4,5,6	1,260	95.9	85.5	98.6	88.1	86.4	
Vindhyachal	7,8	1,000	98.8	94.9	97.0	97.8	89.9	
Vindhyachal	9,10	1,000	101.4	84.7	97.0	99.6	95.9	
Vindhyachal	11,12	1,000	59.9	80.6	98.3	98.5	99.6	
Vindhyachal	13	500	100.2	99.2	99.9	99.9	97.0	
Bongaigaon I	1,2	500	43.2	43.3	90.0	94.8	89.9	
Simhadri	1,2	1,000	-	63.5	79.4	90.1	101.1	
Mauda I	3,4	1,000	-	65.0	43.5	41.8	67.9	Improving trend
Kudgi I	1,2	1,600	-	80.6	87.0	87.3	104.3	
Solapur	1	600	-	24.4	40.0	60.9	82.1	Improving trend
Unchahar	6	500	-	43.2	27.7	-	-	Shutdown due to Accident, to restart in 3Q19

Source: Company, JM Financial

Exhibit 3. SOTP Valuation

	Comments	Multiple	Per share value
Regulated equity FY20E	FY20E regulated equity	2.1	166
Regulated equity in JV Co's	FY20E regulated equity	1.5	15
CWIP (Equity component)	1X FY20 BV	1.0	29
Investments & Cash	1x BV	1.0	5
			215

Source: Company, JM Financial

We find FV at 18% RoE with 4–5GW annual capacity addition, implying a 12% EPS CAGR

Exhibit 4. SOTP sensitivity

		Core RoE			
		16%	18%	19%	20%
Growth (g)	5%	176	199	211	223
	6%	185	215	225	239
	7%	196	229	245	262
	8%	214	255	276	297
	9%	244	300	328	356

Source: Company, JM Financial

We value NTPC at 18% RoE Vs. historic run-rate of 20%+ core RoEs

Exhibit 5. Quarterly Financials

Y/E March	1QFY18	1QFY19	%YoY	4QFY18	%QoQ	FY18	FY19E	%YoY
Generation (MUs)	64,411	69,212	7.5	61,452	12.6	2,58,692	2,83,746	9.7
Net Sales	1,98,793	2,28,637	15.0	2,31,003	-1.0	8,80,833	9,77,916	11.0
Expenditure	1,46,110	1,67,488	14.6	1,68,906	-0.8	6,51,025	7,05,784	8.4
EBITDA	52,684	61,149	16.1	62,097	-1.5	2,29,808	2,72,132	18.4
EBITDA (%)	26.5	26.7	0.9	26.9	-0.5	26.1	27.8	174bps
Other income	6,626	1,364	-79.4	5,176	-73.6	15,583	19,500	25.1
Depreciation	15,700	18,602	18.5	19,348	-3.9	74,599	78,228	4.9
EBIT	43,610	43,912	0.7	47,924	-8.4	1,70,792	2,13,404	24.9
Interest	8,956	12,199	36.2	11,042	10.5	44,346	45,405	2.4
PBT	34,654	31,712	-8.5	36,883	-14.0	1,26,446	1,67,999	32.9
Tax	8,472	5,831	-31.2	7,627	-23.5	25,881	41,340	59.7
Tax rate (%)	24.4	18.4	-24.8	20.7	-11.1	20.5	24.6	
PAT	26,182	25,881	-1.1	29,256	-11.5	1,00,565	1,26,659	25.9
PAT (adjusted) JMFe	22,942	25,498	11.1	33,994	-25.0	1,08,000	1,26,659	17.3
EPS (INR)	2.8	3.1	11.1	4.1	-25.0	12.2	15.4	25.9
RoE	19%	21%		23%	-9	20%	20%	

Source: Company, JM Financial

Exhibit 6. Cost Break-up

	1QFY18	1QFY19	%YoY	4QFY18	%QoQ	FY18	FY19E
Raw material Costs	1,19,401	1,37,996	15.6	1,25,697	9.8	4,89,928	5,87,001
% of sales	60	60	29bps	54	11bps	56	60
RM/MU	1.9	2.0	7.6	2.0	-2.5	1.9	2.1
Staff Costs	10,712	12,419	15.9	13,682	-9.2	47,920	50,795
% of sales	5.4	5.4	4bps	5.9	-8bps	5.4	5.2
Other Expenses	15,996	17,073	6.7	29,527	-42.2	1,13,177	67,988
% of sales	8.0	7.5	-58bps	12.8	-42bps	12.8	7.0

Source: Company, JM Financial

Company background

- NTPC is the largest power utility company in India owning and operating 40GW on assured regulated RoE-based norms. Recently, it was impacted by the tightening of CERC norms, impacting RoE by 5–6%. Capacity addition has also tapered off to 1–1.2GW annually.
- Potential triggers: a) Revival in GW addition with 25GW planned during the 13th plan period—15GW thermal + 10GW solar; b) revival in RoEs as the company adjusts to newer efficiency thresholds; and c) recovery in project CoD, as bunched under-construction capacity commissions in FY17–18 can boost growth. Current schedule points to bunched project commissioning of 6–8GW in FY17–18.

Investment rationale

- **High earning visibility:** With a capacity addition pick up expected in FY17–19, NTPC has high earnings visibility, since it earns a minimum of 15.5% RoE invested in the power business under CERC norms. The FY15/FY16 actual earnings were at 17–19% of regulated equity on incentives/cost savings. Most utilities are currently suffering from low capacity utilisation (PLF) due to low power demand, while NTPC continues to enjoy guaranteed 15.5% RoE, as long as its plants are available to produce power.
- **Large capex pipeline:** With 18GW of under-construction capacity to be commissioned by FY19–20, NTPC will add >40% of its existing 38GW commercial base, in the next 3–4 years. With all of this capacity being based on regulated RoEs, earnings growth will closely follow project capitalisation. Once executed, this can potentially add >60% to regulated equity by FY19–20. Solar capex is an additional 10GW targeted in the next seven years, of which 250MW in AP has been ordered.

Key risks

- Delayed capacity addition and lower incentive earnings, in case PLFs decline, continue to be risks.
- Any incremental hit from the new CERC norms (FY20 onwards) which can have higher than expected impact on core RoE, over and above the 2% impact already factored.

Financial Tables (Standalone)

Income Statement					(INR mn)
Y/E March	FY16A	FY17A	FY18A	FY19E	FY20E
Net Sales	7,08,438	8,20,425	8,80,833	9,77,916	10,62,173
Sales Growth	-2.5%	15.8%	7.4%	11.0%	8.6%
Other Operating Income	0	0	0	0	0
Total Revenue	7,08,438	8,20,425	8,80,833	9,77,916	10,62,173
Cost of Goods Sold/Op. Exp	55,765	79,607	1,13,177	67,988	76,392
Personnel Cost	35,817	43,755	47,920	50,795	53,843
Other Expenses	4,37,986	4,79,478	4,89,928	5,87,001	6,40,161
EBITDA	1,78,871	2,17,585	2,29,808	2,72,132	2,91,778
EBITDA Margin	25.2%	26.5%	26.1%	27.8%	27.5%
EBITDA Growth	15.7%	21.6%	5.6%	18.4%	7.2%
Depn. & Amort.	51,723	60,099	74,599	78,228	88,326
EBIT	1,27,147	1,57,486	1,55,209	1,93,904	2,03,452
Other Income	11,654	9,668	15,583	19,500	20,000
Finance Cost	32,964	36,511	44,346	45,405	47,572
PBT before Excep. & Forex	1,05,837	1,30,643	1,26,446	1,67,999	1,75,880
Excep. & Forex Inc./Loss(-)	0	0	0	0	0
PBT	1,05,837	1,30,643	1,26,446	1,67,999	1,75,880
Taxes	-1,738	29,751	25,881	41,340	43,279
Extraordinary Inc./Loss(-)	0	0	0	0	0
Assoc. Profit/Min. Int.(-)	0	0	0	0	0
Reported Net Profit	1,07,575	1,00,892	1,00,565	1,26,659	1,32,601
Adjusted Net Profit	91,231	1,04,902	1,08,000	1,26,659	1,32,601
Net Margin	12.9%	12.8%	12.3%	13.0%	12.5%
Diluted Share Cap. (mn)	8,245.5	8,245.5	8,245.5	8,245.5	8,245.5
Diluted EPS (INR)	11.1	12.7	13.1	15.4	16.1
Diluted EPS Growth	10.3%	15.0%	3.0%	17.3%	4.7%
Total Dividend + Tax	24,788	24,788	23,190	23,190	23,190
Dividend Per Share (INR)	2.5	2.5	2.5	2.5	2.5

Source: Company, JM Financial

Cash Flow Statement					(INR mn)
Y/E March	FY16A	FY17A	FY18A	FY19E	FY20E
Profit before Tax	1,05,837	1,30,643	1,26,446	1,67,999	1,75,880
Depn. & Amort.	51,723	60,099	74,599	78,228	88,326
Net Interest Exp. / Inc. (-)	32,964	36,511	44,346	45,405	47,572
Inc (-) / Dec in WCap.	-21,912	-13,649	9,998	-3,901	-6,950
Others	0	0	-7,030	0	0
Taxes Paid	-1,738	29,751	25,881	41,340	43,279
Operating Cash Flow	1,70,350	1,83,853	2,22,477	2,46,390	2,61,549
Capex	-1,00,308	-2,08,741	-3,09,558	-1,94,815	-2,54,378
Free Cash Flow	70,043	-24,888	-87,081	51,575	7,171
Inc (-) / Dec in Investments	-1,71,235	-71,201	29,539	-20,918	1,03,050
Others	0	0	0	0	0
Investing Cash Flow	-2,71,543	-2,79,942	-2,80,019	-2,15,733	-1,51,328
Inc / Dec (-) in Capital	0	43,018	-21,909	0	0
Dividend + Tax thereon	-24,788	-24,788	-23,190	-23,190	-23,190
Inc / Dec (-) in Loans	78,504	1,39,571	1,48,581	65,423	58,111
Others	-37,249	-76,471	-35,460	-45,405	-47,572
Financing Cash Flow	16,468	81,331	68,021	-3,172	-12,651
Inc / Dec (-) in Cash	-84,725	-14,759	10,479	27,485	97,570
Opening Cash Balance	1,28,788	44,064	29,305	39,784	67,268
Closing Cash Balance	44,064	29,305	39,784	67,268	1,64,838

Source: Company, JM Financial

Balance Sheet					(INR mn)
Y/E March	FY16A	FY17A	FY18A	FY19E	FY20E
Shareholders' Fund	8,87,820	9,62,312	10,17,778	11,21,246	12,30,657
Share Capital	82,455	82,455	82,455	82,455	82,455
Reserves & Surplus	8,05,365	8,79,858	9,35,323	10,38,792	11,48,202
Preference Share Capital	0	0	0	0	0
Minority Interest	0	0	0	0	0
Total Loans	8,63,828	10,03,398	11,51,979	12,17,402	12,75,513
Def. Tax Liab. / Assets (-)	11,522	14,848	24,086	24,086	24,086
Total - Equity & Liab.	17,63,170	19,80,559	21,93,843	23,62,735	25,30,256
Net Fixed Assets	15,80,635	18,01,329	19,95,786	21,50,468	22,30,646
Gross Fixed Assets	13,90,934	16,00,126	18,91,690	21,03,681	23,75,235
Intangible Assets	0	401	7,431	7,431	7,431
Less: Depn. & Amort.	5,46,469	6,06,568	6,81,168	7,59,395	8,47,721
Capital WIP	7,36,170	8,07,371	7,77,832	7,98,751	6,95,701
Investments	82,932	82,481	1,00,475	83,299	66,122
Current Assets	4,82,627	4,77,137	5,05,675	5,48,188	6,58,801
Inventories	71,925	65,048	60,574	67,250	73,044
Sundry Debtors	78,440	81,735	75,780	84,132	91,381
Cash & Bank Balances	44,064	29,305	39,784	67,268	1,64,838
Loans & Advances	1,92,295	7,675	9,359	9,359	9,359
Other Current Assets	95,903	2,93,374	3,20,179	3,20,179	3,20,179
Current Liab. & Prov.	3,83,023	3,80,388	4,08,092	4,19,220	4,25,313
Current Liabilities	74,495	70,104	77,019	88,146	94,239
Provisions & Others	3,08,528	3,10,285	3,31,074	3,31,074	3,31,074
Net Current Assets	99,604	96,749	97,583	1,28,968	2,33,488
Total - Assets	17,63,170	19,80,559	21,93,843	23,62,735	25,30,256

Source: Company, JM Financial

Dupont Analysis					
Y/E March	FY16A	FY17A	FY18A	FY19E	FY20E
Net Margin	12.9%	12.8%	12.3%	13.0%	12.5%
Asset Turnover (x)	0.3	0.4	0.4	0.4	0.4
Leverage Factor (x)	2.4	2.4	2.5	2.5	2.4
RoE	10.7%	11.3%	10.9%	11.8%	11.3%

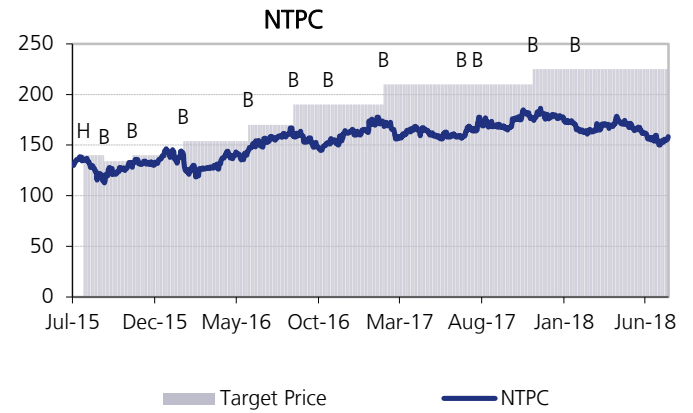
Key Ratios					
Y/E March	FY16A	FY17A	FY18A	FY19E	FY20E
BV/Share (INR)	107.7	116.7	123.4	136.0	149.3
ROIC	8.6%	7.0%	6.4%	6.9%	6.9%
ROE	10.7%	11.3%	10.9%	11.8%	11.3%
Net Debt/Equity (x)	0.9	1.0	1.1	1.0	0.9
P/E (x)	14.0	12.2	11.8	10.1	9.6
P/B (x)	1.4	1.3	1.3	1.1	1.0
EV/EBITDA (x)	11.7	10.4	10.4	8.9	8.2
EV/Sales (x)	3.0	2.7	2.7	2.5	2.2
Debtor days	40	36	31	31	31
Inventory days	37	29	25	25	25
Creditor days	38	30	31	35	35

Source: Company, JM Financial

History of Earnings Estimate and Target Price

Date	Recommendation	Target Price	% Chg.
30-Jul-15	Hold	140	
7-Sep-15	Buy	134	-4.3
29-Oct-15	Buy	140	4.5
1-Feb-16	Buy	154	10.0
1-Jun-16	Buy	170	10.4
24-Aug-16	Buy	190	11.8
28-Oct-16	Buy	190	0.0
8-Feb-17	Buy	210	10.5
3-Jul-17	Buy	210	0.0
2-Aug-17	Buy	210	0.0
13-Nov-17	Buy	225	7.1
31-Jan-18	Buy	225	0.0
29-May-18	Buy	220	-2.2

Recommendation History



APPENDIX I

JM Financial Institutional Securities Limited

(formerly known as JM Financial Securities Limited)

Corporate Identity Number: U67100MH2017PLC296081**Member of BSE Ltd., National Stock Exchange of India Ltd. and Metropolitan Stock Exchange of India Ltd.****SEBI Registration Nos.: Stock Broker - INZ000163434, Research Analyst – INH000000610****Registered Office: 7th Floor, Cnergy, Appasaheb Marathe Marg, Prabhadevi, Mumbai 400 025, India.****Board: +9122 6630 3030 | Fax: +91 22 6630 3488 | Email: jmfinancial.research@jmfl.com | www.jmfl.com****Compliance Officer: Mr. Sunny Shah | Tel: +91 22 6630 3383 | Email: sunny.shah@jmfl.com**

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Rating	Meaning
Buy	Total expected returns of more than 15%. Total expected return includes dividend yields.
Hold	Price expected to move in the range of 10% downside to 15% upside from the current market price.
Sell	Price expected to move downwards by more than 10%

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