

Sector: Power
Result Update

	Change
Reco: Buy	↔
CMP: Rs. 622	
Price Target: Rs. 825	↓
↑ Upgrade ↔ No change ↓ Downgrade	

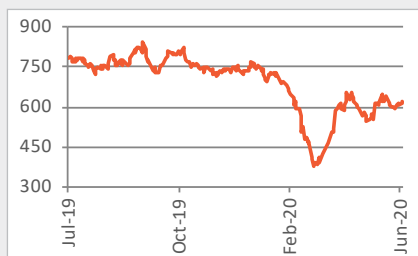
Company details

Market cap:	Rs. 7,766 cr
52-week high/low:	Rs. 855/366
NSE volume: (No of shares)	5.5 lakh
BSE code:	500084
NSE code:	CESC
Sharekhan code:	CESC
Free float: (No of shares)	6.6 cr

Shareholding (%)

Promoters	50
FII	18
DII	23
Others	9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	1	52	-16	-21
Relative to Sensex	-4	34	0	-9

Sharekhan Research, Bloomberg

CESC Limited (CESC) Q4FY2020 consolidated PAT increased by 7% y-o-y to Rs439 crore primarily led by: 1) better profitability at Dhariwal Infrastructure (PAT up 1.9x y-o-y to Rs54 crore) and 2) sharp reduction in losses at distribution franchisee (DF) to Rs. 9 crore as compared to Rs. 22 crore in Q4FY2019. Improvement in performance of Dhariwal and DF was partially offset by weak performance of Noida Power (PAT down by 61% y-o-y to Rs. 19 crore). However, standalone PAT declined by 19% y-o-y to Rs. 250 crore led by subdued power sales volume at 2,107 million units (down 8% y-o-y). Potential reduction in losses at distribution franchisee and an improvement in utilisation rate at Dhariwal (64% in FY2020 versus 61% in FY2019) coupled with steady earnings contribution from standalone business keeps us constructive on CESC. The stock is also trading at an attractive valuation of 0.7x FY2022E P/BV and 7.9x its FY2022E EPS on a standalone basis. Hence, we maintain our Buy rating on CESC with revised SoTP-based PT of Rs. 825.

Key positives

- Loss at Dhariwal Infrastructure reduced to Rs. 10 crore in FY2020 as compared to Rs. 93 crore in FY2019.
- Loss at distribution franchisee shrunk to Rs. 38 crore in FY2020 as compared to Rs. 60 crore in FY2019.
- Short-term PPA for 185 MW with Maharashtra for unit-1 of Dhariwal extended till October 2020.

Key negatives

- Standalone power sales volume declined by 8% y-o-y to 2,107 million units in Q4FY2020.

Our Call

Valuation - Maintain Buy on CESC with revised SoTP-based PT of Rs. 825: We have lowered our FY2021E EPS to factor lower incentive income and power sales volume as PLF (plant load factor) was impacted in Q1FY2021 and have fine-tuned our FY2022E EPS. CESC's consolidated financial are expected to improve with reduction in losses at Rajasthan distribution franchisee, improvement in utilisation at Dhariwal Infrastructure and stable earnings contribution from standalone business. The stock is also trading at an attractive valuation of 0.7x FY2022E P/BV and 7.9x its FY2022E EPS on standalone basis. Hence, we maintain our Buy rating on CESC with revised SoTP-based PT of Rs. 825.

Key Risks

Delay in signing of long-term PPA for the Chandrapur plant and sustained losses in the distribution franchisee for an extended period.

Valuation (Standalone)	Rs cr					
Particulars	FY17	FY18	FY19	FY20	FY21E	FY22E
Revenues	7,220	7,786	7,754	7,836	7,710	8,846
OPM (%)	22.5	21.0	17.5	18.3	18.8	18.8
PAT	861	864	937	918	828	1,048
% y-o-y growth	1.9	0.3	8.4	(2.0)	(9.8)	26.6
EPS (Rs.)	64.6	65.0	70.3	68.9	62.1	78.7
P/E (x)	9.6	9.6	8.8	9.0	10.0	7.9
Price/ Book (x)	0.6	0.9	0.8	0.8	0.8	0.7
EV/EBITDA (x)	7.4	7.3	8.8	8.5	7.7	6.2
RoCE (%)	6.6	7.2	8.3	8.0	6.9	8.5
RoE (%)	6.5	7.6	9.8	9.3	8.0	9.6

Source: Company; Sharekhan estimates

Reduced losses at subsidiaries led to 7% y-o-y rise in consolidated PAT; Standalone PAT was down 19.1% y-o-y: Consolidated PAT increased by 7% y-o-y (up 64% q-o-q) to Rs 439 crore in Q4FY2020 primarily led by: 1) better profitability at Dhariwal Infrastructure (PAT rose 1.9x y-o-y to Rs. 54 crore) and 2) sharp reduction in losses at distribution franchisee (DF) to Rs 9 crore as compared to Rs. 22 crore in Q4FY2019. Improvement in performance of Dhariwal was partially offset by weak performance of Noida Power (PAT down by 61% y-o-y to Rs19 crore).

Standalone revenues declined by 4.8% y-o-y (down 3.9% q-o-q) to Rs. 1,583 crore, below our estimate of Rs. 1701 crore due to lower-than-expected power realization at Rs 7.5/unit (down 3.4% y-o-y) as compared to our estimate of Rs. 8.1/unit. Power sales volume at 2,119 million units (down 8% y-o-y; flat q-o-q) was in-line with estimates. Operating profit increased by 67.3% y-o-y (down 9.4% q-o-q) to Rs. 251 crore, above our estimate of Rs. 390 crore on account of lower generation costs (down 13.2% y-o-y; down 6.3% q-o-q). Standalone PAT stood at Rs. 250 crore (down 19.1% y-o-y; up 42% q-o-q), which was above our estimate of Rs. 160 crore.

Key takeaways from discussion with management

- ◆ **Standalone PAT guidance** – The management has guided for 10% y-o-y decline in the standalone PAT for FY2021E due to likely lower PLF-based incentive income (stood at Rs 250 crore in FY2020). The power generation and sales volume is expected to decline by 10% y-o-y in FY2021E due to lower power demand amid COVID-19. PLF for standalone power generation plants was weak in April-May 2020 given a sharp decline in power demand but the same has improved to 85% in June 2020.
- ◆ **DF loss to reduce further in FY2021** - The management has guided that loss at distribution franchisee (DF) is expected to reduce further to Rs. 25-30 crore in FY2021E (as compared to a loss of Rs. 38 crore in FY2020) given likely reduction in transmission and distribution (T&D). We believe that the distribution franchisee would create value over next 2-3 years for CESC given its strong track record to reduce T&D losses. The loss at DF declined to Rs38 crore in FY2020 as compared to Rs. 60 crore in FY2019.
- ◆ Loss at Dhariwal Infrastructure reduced to Rs. 10 crore in FY2020 as compared to Rs. 93 crore in FY2019.
- ◆ **Dividend** – The management had said that dividend would increase by Rs1-2/share every year. The dividend per share (DPS) was at Rs. 20 in FY2020, which implies a healthy dividend yield of 3.2%.
- ◆ Power generation declined by 2.5% y-o-y to 6,137 million units in FY2020 as compared to 6,298 million units in FY2019. Total power sales stood at 10,282 million units in FY2020 as compared to 10,390 million units in FY2019.
- ◆ Transmission and distribution stood at 8.9% in FY2020 versus 9% in FY2019. Haldia and Chandrapur PLF was at 84.1% (versus 88% in FY2019) and 64.1% (versus 61.4% in FY2019) respectively in FY2020.
- ◆ The cash & bank balance stood at Rs. 1,789 crore as on March 31, 2020 as compared to Rs. 1,031 crore as on March 31, 2019.
- ◆ Consolidated gross debt was at Rs. 12,171 crore as on March 31, 2020 as against Rs. 12,612 crore as on March 31, 2019.

Results

Particulars	Rs cr				
	Q4FY20	Q4FY19	y-o-y (%)	Q3FY20	q-o-q (%)
Revenue	1,583	1,662	(4.8)	1,648	(3.9)
Gross Profit	680	669	1.6	672	1.2
EBITDA	251	150	67.3	277	(9.4)
Other Income	49	72	(31.9)	29	69.0
Depreciation	121	103	17.5	110	10.0
Finance Cost	170	109	56.0	117	45.3
PBT	306	264	15.9	214	43.0
Total Tax	56	-45	NA	38	47.4
Reported PAT	250	309	(19.1)	176	42.0
EPS (Rs.)	18.8	23.2	(19.1)	13.2	42.0
			bps		bps
Gross Margin (%)	43.0	40.3	270	40.8	218
EBITDA Margin (%)	15.9	9.0	683	16.8	-95
PAT Margin (%)	15.8	18.6	-280	10.7	511

Source: Company; Sharekhan Research

Financial performance of key subsidiaries

Particulars	Rs cr			
	Revenues		PAT	
	Q4FY20	Q4FY19	Q4FY20	Q4FY19
CESC Consolidated	2534	2417	446	419
Haldia	518	517	68	59
Dhariwal Infrastructure Ltd	383	305	54	28
Crescent Power	93	89	24	24
Noida Power	387	354	19	49
Kota/Bharatpur/Bikaner	398	289	-9	-22

Source: Company; Sharekhan Research

Outlook

Weak power demand to impact near term profitability; turnaround of subsidiaries to improve performance:

We expect near-term profitability of CESC to be impacted by weak power demand amid COVID-19. However, reduction of losses at distribution franchisee led by lower T&D losses and higher utilization at Dhariwal would improve earnings visibility. Furthermore, the short-term PPA for 185 MW with Maharashtra for unit-1 of Dhariwal was extended till October 2020. Dhariwal has tied up 287 MW under a long-term power purchase agreement (PPA) for unit-2.

Valuation

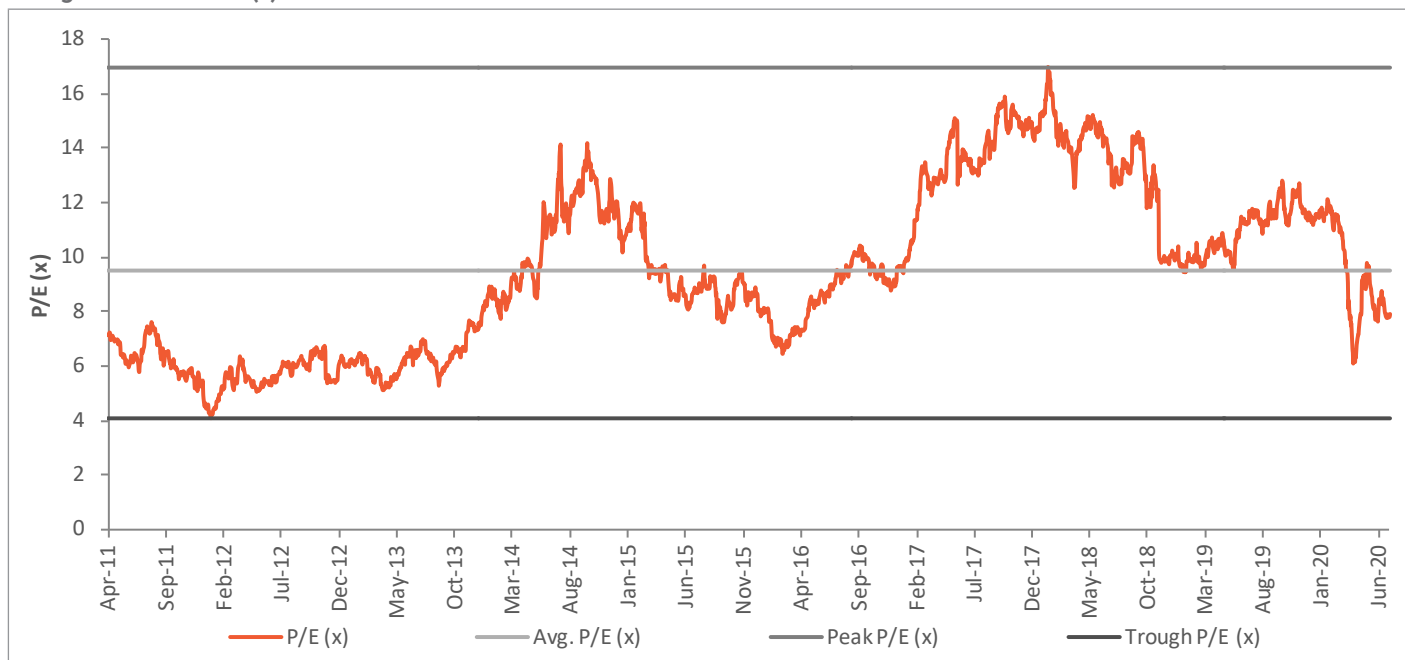
Maintain Buy on CESC with revised SoTP-based PT of Rs. 825: We have lowered our FY2021E EPS to factor lower incentive income and power sales volume as PLF (plant load factor) was impacted in Q1FY2021 and have fine-tuned our FY2022E EPS. CESC's consolidated financial are expected to improve with reduction in losses at Rajasthan distribution franchisee, improvement in utilisation at Dhariwal Infrastructure and stable earnings contribution from standalone business. The stock is also trading at an attractive valuation of 0.7x FY2022E P/BV and 7.9x its FY2022E EPS on standalone basis. Hence, we maintain our Buy rating on CESC with revised SoTP-based PT of Rs. 825.

SoTP-based PT of Rs. 825

Particulars	Value (Rs/share)	Methodology
Standalone business	550	7x FY22E EPS
Haldia	130	1.5x regulated equity of ~Rs 1150 crore
Dhariwal	75	1x regulated equity of ~Rs 1000 crore
Crescent Power	10	6.5x FY20 PAT for 67.8% stake
Noida	30	2x regulated equity of ~Rs400 crore for 49.6% stake
DF	30	1x Investments
Price target	825	

Source: Company; Sharekhan Research

One-year forward P/E (x) band



Source: Sharekhan Research

About company

CESC Limited, started operations in 1899, is a fully integrated power utility company. The company is the sole distributor of electricity within an area of 567 sq. km of Kolkata and Howrah and serves 3.3 million consumers (including domestic, industrial and commercial users). The company owns and operates three thermal power plants with generation capacity of 1,125 MW for its Kolkata distribution business. Additionally, CESC has independent power plants at Haldia (600 MW) and Chandrapur (600 MW) along with renewable energy (174 MW wind projects). CESC have distribution licensee with in an area of 335 sq. km of Noida and serves 82,000 consumers. The company also has distribution franchisee in three cities of Rajasthan (Kota, Bikaner and Bharatpur – all are operational) and one city in Maharashtra (Malegaon – operations expected to start soon).

Investment theme

CESC has stable earnings contribution from standalone operations with regulated power generation and distribution businesses getting assured RoE of 15.5% on generation assets and 16.5% for distribution assets. Reducing loss at Dhariwal Infrastructure and Rajasthan distribution franchisee makes CESC an attractive investment proposition. CESC's valuation is also attractive.

Key Risks

- ◆ Delay in signing of long-term PPA for Chandrapur plant.
- ◆ Sustained losses in distribution franchisee for an extended period.

Additional Data

Key management personnel

Sanjiv Goenka	Chairman
Rajarshi Banerjee	Chief Financial Officer
Rabi Chowdhury	Managing Director – Generation
Debasish Banerjee	Managing Director – Distribution

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	HDFC Asset Management Co Ltd	9.3
2	Sun Life Financial Inc	5.4
3	Reliance Capital Trustee Co Ltd	2.2
4	BNK Capital Markets Ltd	2.2
5	ICICI Prudential Asset Management	2.1
6	Life Insurance Corp of India	2.1
7	Franklin Resources Inc	2.0
8	Vanguard Group Inc/The	1.7
9	Emirate of Abu Dhabi United Arab	1.5
10	Aditya Birla Sun Life Trustee Co	1.2

Source: Bloomberg

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