Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Power Grid Corporation of India Limited

Strong Q2; capitalization to drive growth

Power	Sharekhan code: POWERGRID	Result Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 189**	
Price Target: **Rs. 220**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

Company details

Market cap:	Rs. 99,112 cr
52-week high/low:	Rs. 211/130
NSE volume: (No of shares)	107.4 lakh
BSE code:	532898
NSE code:	POWERGRID
Free float: (No of shares)	255 cr

Shareholding (%)

Promoters	51
FII	26
DII	16
Others	6

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	18	6	14	0
Relative to Sensex	11	-7	-22	-8

Sharekhan Research, Bloomberg

Summary

- Power Grid's Q2FY2021 PAT grew by 23.4% y-o-y to Rs. 3,117 crore, which was in-line with our estimate of Rs. 3,093 crore. Strong growth was driven by higher capitalisation at Rs. 11,877 crore in H1FY2021 (versus. Rs. 5,687 crore in H1FY20), higher other income, and lower tax rate.
- Management reiterated its asset capitalisation and capex guidance of Rs. 20,000 crore-25,000 crore and Rs. 10,500 crore, respectively, for FY2021E. Work in hands at Rs. 41,000 crore provides earnings visibility (expect an 11% PAT CAGR over FY2020-FY2023E).
- Power Grid targets to monetise 5 TBCB assets worth Rs. 7,164 crore in FY2021, which would help unlock value, while potential reduction in receivables (through power sector liquidity scheme) would improve balance sheet.
- Hence, we recommend Buy on Power Grid with a PT of Rs. 220, given earnings visibility over FY2021E-FY2023E, attractive valuation of 1.2x FY2023E P/BV (31% discount to historical P/BV), and healthy dividend yield at 4%.

Power Grid Corporation of India Limited's (Power Grid) Q2FY2021 PAT increased by 23.4% y-o-y to Rs. 3,117 crore, which was in-line with our estimate of Rs. 3093 crore. Robust growth in PAT was led by strong capitalisation of Rs. 11,877 crore in H1FY2021 (versus Rs. 5,687 crore in H1FY2020), higher other income (up 67.1% y-o-y), and lower tax rate at 17.9% (versus assumption of 25.2%). Management has maintained its FY2021E capitalisation guidance of Rs. 20,000 crore-25,000 crore (HVDC Raigarh-Pugalur project to be completed in FY2021 – total capitalisation done Rs. 9500 crore till date and remaining Rs. 10,000 crore expected in H2FY2021) and work-in-hand pipeline stands at ~Rs. 41,000 crore. Robust order pipeline offers earnings growth visibility over the next few years (we expect an 11% PAT CAGR over FY2020-FY2023E) and RoE to remain strong at 17%-19%. Moreover, Power Grid is trading at an attractive valuation of 1.2x its FY2022E P/BV (31% discount to its historical average one-year forward P/BV of 1.7x). Hence, we recommend Buy on Power Grid with a PT of Rs. 220.

Key positives

- Strong capitalisation of Rs. 10,693 crore in Q2FY2021 versus Rs. 1,184 crore in Q1FY2021 and Rs. 4,221 crore in Q2FY2020.
- Outstanding dues have reduced to Rs. 6,477 crore as compared to Rs. 8,243 crore at the end of Q1FY2021.
- Management has maintained its capex guidance of Rs. 10,500 crore and asset capitalisation guidance of Rs. 20,000 crore-25,000 crore for FY2021E.

Key negatives

- Lower surcharge income sequentially at Rs. 220 crore in Q2FY2021 as power transmission companies continue to get late payment surcharge at lower rate of 12%.

Our Call

Valuation – Recommend Buy on Power Grid with a PT of Rs. 220: We have largely maintained our FY2021-FY2023 earnings estimates. Power Grid has a robust Rs. 41,000 crore of project pipeline, which provides earnings visibility for the next 2-3 years. Thus, we expect an 11% PAT CAGR over FY2020-FY2023 along with RoE of 17%-19%. Moreover, Power Grid is hopeful to complete the monetisation of 5 TBCB assets (worth Rs. 7,164 crore) in FY2021 and the same would help in value unlocking. The balance sheet is also expected to improve with further reduction in receivables as Power Grid would receive outstanding dues from discom under the power sector liquidity infusion scheme. Power Grid's valuation of 1.2x FY2023E P/BV is also attractive given 31% discount to its average historical average one-year forward P/BV at 1.7x, and the stock offers a healthy dividend yield of 4%. Hence, we recommend Buy on Power Grid with a PT of Rs. 220.

Key risk

Slower-than-expected capitalisation of projects (due to delayed project execution amid COVID-19). Inability to win new projects under the tariff-based competitive bidding route.

Valuation (Consolidated) Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Revenue	35,059	37,744	40,763	44,839	49,099
OPM (%)	86.2	87.3	83.6	86	86
Adjusted PAT	10,034	11,059	10,529	12,492	15,003
y-o-y growth (%)	22.3	10.2	-4.8	18.6	20.1
Ajusted EPS (Rs.)	19.2	21.1	20.1	23.9	28.7
P/E (x)	9.9	9	9.4	7.9	6.6
Price/ Book (x)	1.7	1.5	1.4	1.3	1.2
EV/EBITDA (x)	7.6	7	6.7	5.8	5.2
RoCE (%)	10.1	10.4	10.4	11.8	12.7
RoE (%)	17.7	17.9	15.8	17.3	18.9

Source: Company; Sharekhan estimates

Note: We now convert Power Grid into a stock update; It was earlier a 'Viewpoint' under our coverage.

Inline PAT; strong capitalisation of Rs. 11,877 crore in H1FY2021

Q2FY2021 revenue grew by 4.3% y-o-y to Rs. 9,058 crore, below our estimate of Rs. 9,579 crore. Revenue from the transmission business was up by 6.3% y-o-y to Rs. 9,034 crore. Operating profit margin (OPM) at 88% (up 99 bps y-o-y) was marginally above our estimate of 87.5%. Consequently, operating profit at Rs. 7,971 crore (up 5.5% y-o-y; up 1.4% q-o-q) was below our estimate of Rs. 8,382 crore. PAT increased by 23.4% y-o-y to Rs. 3,117 crore, in-line with our estimate of Rs. 3,093 crore. Strong PAT growth was on the account of strong capitalisation of Rs. 11,877 crore in H1FY2021 (versus Rs. 5,687 crore in H1FY2020) and higher other income (up 67.1% y-o-y) and lower tax rate.

Q2FY2021 conference call highlights

- **Asset capitalisation and capex in Q2FY2021 –** Power Grid has capitalised its assets worth Rs. 10,693 crore in Q2FY2021 versus Rs. 1,184 crore in Q1FY2021 as compared to Rs. 4,221 crore in Q2FY2020. Q1FY2021 capex stood at Rs. 3,100 crore as compared to Rs. 1,906 crore in Q1FY2021 and Rs. 3,623 crore in Q2FY2020. The company has work-in-hand worth Rs. 41,000 crore (ongoing projects at Rs. 22,500 crore, new projects at Rs. 6,600 crore, and Rs. 12,000 crore for TBCB). Management expects upcoming opportunities worth Rs. 17900 crore (inter-state transmission works from RE at Rs. 16,000 crore and intra-state works in TBCB at Rs. 2,000 crore.

- **Capex and capitalisation guidance –** Management has maintained its capex guidance of Rs. 10,500 crore and asset capitalisation guidance of Rs. 20,000 crore-25,000 crore for FY2021E. The 800kV HVDC Raigarh-Pugalur project is expected to be completed in FY2021 and total Rs. 9,500 crore has been capitalised on the project till date and capitalisation of Rs. 10,000 crore would be done in H2FY2021.

- **Outstanding dues –** Total outstanding dues reduced to Rs. 6,477 crore as compared to Rs. 8,243 crore at the end of Q1FY2021. The company has settled Rs. 1,391 crore under the Atmanirbhar Bharat scheme till date.. Trade receivables (>45 days) also reduced to Rs. 4,502 crore versus Rs. 6,145 crore at the end of Q1FY2021. Major outstanding dues were from states of Uttar Pradesh, J&K, Karnataka, Maharashtra, and Telangana. Management targets to lower overall debtors days to 45 by March 2021 as compared to 69 days at the end of Q2FY2021 and total outstanding dues are expected to reduce to Rs. 4,500 crore.

- **Update on InvIT –** Management expects monetisation of 5 TBCB assets through InvIT, which would get completed in FY2021. The 5 TBCB assets are worth Rs. 7,164 crore (versus corresponding liabilities of Rs. 280 crore) on books and amount raised through monetisation would be utilised for new assets.

- Consolidated debt stood at Rs. 1,43,750 core as of September 2020 as compared to Rs. 1,45,998 crore as of June 2020 and Rs. 1,42,459 crore as of September 2019. Debt on standalone basis stood at Rs. 1,43,750 crore as of September 2020 versus Rs. 1,45,998 crore as of June 2020 as compared to Rs. 1,42,159 crore as of September 2019. The company has raised total debt of Rs. 3,300 crore in H1FY2021 and the average cost of debt was at 6.12% in H1FY2021 versus 6.99% in H1FY2020.

- Equity investment in operational TBCB projects stood at Rs. 2,211 crore versus Rs. 2,020 crore in Q2FY2020 and Rs. 2,205 crore in Q1FY2021.

- Surcharge income (consolidated) was at Rs. 220 crore in Q2FY2021 versus Rs. 82 crore in Q2FY2020 and Rs. 265 crore in Q1FY2021. Incentive income (consolidated) stood at Rs. 120 crore versus Rs. 110 crore in Q2FY2020 and Rs. 126 crore in Q1FY2021. Income from subsidiaries and JV was at Rs. 268 crore as compared to Rs. 238 crore in Q2FY2020 and Rs. 260 in Q1FY2021.

Results (Standalone) Rs cr

Particulars (Rs. cr)	Q2FY21	Q2FY20	YoY(%)	Q1FY21	QoQ(%)
Reported Net Sales	**9,058**	**8,685**	**4.3**	**8,989**	**0.8**
Employee Expenses	489	485	1.0	486	0.7
Other Exp	597	643	(7.2)	625	(4.5)
Total Expenditure	**1,087**	**1,128**	**(3.7)**	**1,112**	**(2.2)**
Operating profit	**7,971**	**7,557**	**5.5**	**7,877**	**1.2**
Other income	832	498	67.1	631	31.8
PBDIT	**8,803**	**8,055**	**9.3**	**8,509**	**3.5**
Depreciation	2,897	2,748	5.4	2,797	3.6
Interest	2,095	2,376	(11.8)	2,279	(8.1)
Exceptional expense/(Income)	4	0	NA	1,075	NA
Reported PBT	**3,808**	**2,931**	**29.9**	**2,358**	**61.5**
Adjusted PBT	**3,812**	**2,931**	**30.1**	**3,433**	**11.0**
Tax	682	756	(9.7)	773	(11.7)
Regulatory Deferral A/c	-8	352	NA	394	NA
Reported PAT	**3,117**	**2,527**	**23.4**	**1,979**	**57.5**
Adjusted PAT	**3,117**	**2,527**	**23.4**	**2,875**	**8.4**
Reported EPS (Rs.)	6.0	4.8	23.4	3.8	57.5
Adjusted EPS (Rs.)	6.0	4.8	23.4	5.5	8.4
Ratios (%)			**YoY (bps)**		**QoQ (bps)**
EBITDA Margin	87.6	89.7	(205.6)	83.2	445
EBITDA Margin	87.6	89.7	(205.6)	83.2	445
PAT Margin	22.0	27.6	(556.1)	32.8	-1,078

Source: Company; Sharekhan Research

Segmental performance Rs cr

Particulars	Q2FY21	Q2FY20	YoY(%)	Q1FY21	QoQ(%)
Revenue					
Transmission	9,034	8,498	6.3	9,045	(0.1)
Consultancy	108	174	(37.6)	99	10.0
Telecom	190	199	(4.3)	188	1.4
Intersegment	-18	-20	(12.8)	-17	2.4
Net Revenue	**9,315**	**8,850**	**5.3**	**9,314**	**0.0**
EBIT					
Transmission	5,221	5,191	0.6	5,767	(9.5)
Consultancy	21	96	(78.4)	16	32.4
Telecom	80	113	(28.9)	100	(19.7)
Total EBIT	**5,322**	**5,400**	**(1.4)**	**5,883**	**(9.5)**
EBIT margin (%)					
Transmission	57.8	61.1	-330	63.8	-597
Consultancy	19.2	55.6	-3,636	16.0	325
Telecom	42.2	56.8	-1,460	53.3	-1,106
Overall EBIT margin	57.1	61.0	-389	63.2	-603
Overall	**63.2**	**60.1**	**310**	**66.7**	**-356**

Source: Company; Sharekhan Research

Outlook and Valuation

■ **Sector View – Regulated tariff model provides earnings visibility; Reforms in the power sector to strengthen the balance sheet of power companies**

India's power sector is regulated by CERC with availability-based earnings model (fixed RoE on power transmission assets) and, thus, regulated tariff model provides strong earnings visibility for power transmission companies. Moreover, the government's power sector liquidity infusion package of Rs. 90,000 crore to clear dues of power generation and transmission companies by discoms would reduce receivables of the power sector and strengthen the balance sheet of companies.

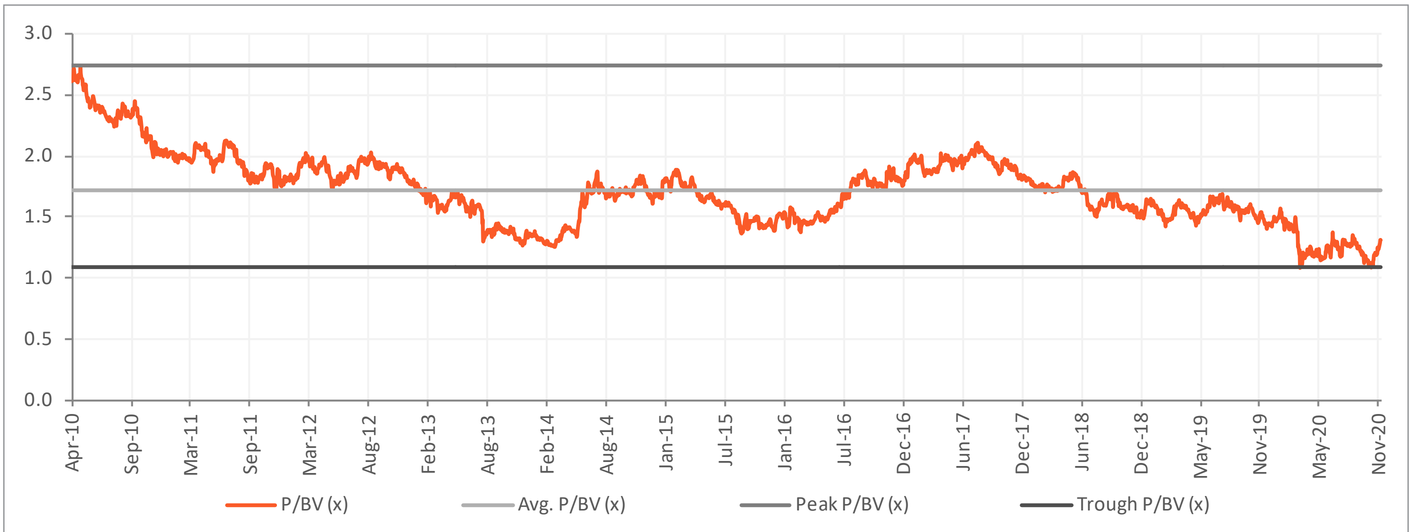
■ **Company Outlook – Order book worth ~Rs. 41,000 crore provides earnings visibility; FY2021E asset capitalisation target maintained at Rs. 20,000 crore-25,000 crore**

Strong FY2021E capitalisation guidance of Rs. 20,000 crore-25,000 crore and work-in-hand pipeline at ~Rs. 41,000 crore (which is likely to be completed over the next 3-4 years) provide healthy earnings growth visibility (we expect an 11% PAT CAGR over FY2020-FY2022E). Capex guidance has also been maintained at Rs. 10,500 crore for FY2021E.

■ **Valuation – Recommend Buy on Power Grid with a PT of Rs. 220**

We have largely maintained our FY2021-FY2023 earnings estimates. Power Grid has a robust Rs. 41,000 crore of project pipeline, which provides earnings visibility for the next 2-3 years. Thus, we expect an 11% PAT CAGR over FY2020-FY2023 along with RoE of 17%-19%. Moreover, Power Grid is hopeful to complete the monetisation of 5 TBCB assets (worth Rs. 7,164 crore) in FY2021 and the same would help in value unlocking. The balance sheet is also expected to improve with further reduction in receivables as Power Grid would receive outstanding dues from discom under the power sector liquidity infusion scheme. Power Grid's valuation of 1.2x FY2023E P/BV is also attractive given 31% discount to its average historical average one-year forward P/BV at 1.7x, and the stock offers a healthy dividend yield of 4%. Hence, we recommend Buy on Power Grid with a PT of Rs. 220.

One-year forward P/BV (x) band



Source: Sharekhan Research

About company

Power Grid is into the power transmission business with the responsibility for planning, implementation, operation, and maintenance of inter-state transmission system and operation of the National and Regional Load Dispatch Centres. The company's segments include transmission, telecom, and consultancy. The transmission segment includes extra-high voltage/high voltage (EHV/HV) networks and grid management. The company owns and operates over 1,63,695 circuit kilometers of EHV transmission lines. Power Grid has approximately 248 sub-stations. The company's Smart Grid enables real-time monitoring and control of power systems.

Investment theme

Power Grid is expected to maintain its strong growth momentum, given ~Rs. 53,000 crore (including CWIP) worth of projects pending for capitalisation, which provides healthy earnings growth visibility over the next few years. Power Grid has a healthy RoE of 18%-19% and is trading at an attractive valuation.

Key Risks

- Slower-than-expected capitalisation of projects.
- Inability to win new projects under the tariff-based competitive bidding route.

Additional Data

Key management personnel

K Sreekant	Chairman and Managing Director
M. Taj Mukarrum	Director – Finance
Abhay Choudhary	Director – Projects

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp of India	5.7
2	HDFC Asset Management Co Ltd	4.1
3	Reliance Capital Trustee Co Ltd	2.5
4	Comgest SA	2.1
5	FIL Ltd	2.0
6	Vanguard Group Inc/The	2.0
7	Republic of Singapore	1.7
8	FMR LLC	1.5
9	SBI Funds Management Pvt Ltd	1.3
10	Government Pension Fund - Global	1.1

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

Sharekhan
by BNP PARIBAS

Know more about our products and services

For Private Circulation only

Disclaimer: This document has been prepared by Sharekhan Ltd. (SHAREKHAN) and is intended for use only by the person or entity to which it is addressed to. This Document may contain confidential and/or privileged material and is not for any type of circulation and any review, retransmission, or any other use is strictly prohibited. This Document is subject to changes without prior notice. This document does not constitute an offer to sell or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. Though disseminated to all customers who are due to receive the same, not all customers may receive this report at the same time. SHAREKHAN will not treat recipients as customers by virtue of their receiving this report.

The information contained herein is obtained from publicly available data or other sources believed to be reliable and SHAREKHAN has not independently verified the accuracy and completeness of the said data and hence it should not be relied upon as such. While we would endeavour to update the information herein on reasonable basis, SHAREKHAN, its subsidiaries and associated companies, their directors and employees ("SHAREKHAN and affiliates") are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent SHAREKHAN and affiliates from doing so. This document is prepared for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Recipients of this report should also be aware that past performance is not necessarily a guide to future performance and value of investments can go down as well. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. We do not undertake to advise you as to any change of our views. Affiliates of Sharekhan may have issued other reports that are inconsistent with and reach different conclusions from the information presented in this report.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject SHAREKHAN and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

The analyst certifies that the analyst has not dealt or traded directly or indirectly in securities of the company and that all of the views expressed in this document accurately reflect his or her personal views about the subject company or companies and its or their securities and do not necessarily reflect those of SHAREKHAN. The analyst further certifies that neither he or its associates or his relatives has any direct or indirect financial interest nor have actual or beneficial ownership of 1% or more in the securities of the company at the end of the month immediately preceding the date of publication of the research report nor have any material conflict of interest nor has served as officer, director or employee or engaged in market making activity of the company. Further, the analyst has also not been a part of the team which has managed or co-managed the public offerings of the company and no part of the analyst's compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this document. Sharekhan Limited or its associates or analysts have not received any compensation for investment banking, merchant banking, brokerage services or any compensation or other benefits from the subject company or from third party in the past twelve months in connection with the research report.

Either SHAREKHAN or its affiliates or its directors or employees / representatives / clients or their relatives may have position(s), make market, act as principal or engage in transactions of purchase or sell of securities, from time to time or may be materially interested in any of the securities or related securities referred to in this report and they may have used the information set forth herein before publication. SHAREKHAN may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall SHAREKHAN, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind.

Compliance Officer: Mr. Joby John Meledan; Tel: 022-61150000; email id: compliance@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com

Registered Office: Sharekhan Limited, 10th Floor, Beta Building, Lodha iThink Techno Campus, Off. JVLR, Opp. Kanjurmarg Railway Station, Kanjurmarg (East), Mumbai – 400042, Maharashtra. Tel: 022 - 61150000. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183;