Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Tata Power Company Ltd

Integrated CGPL & coal biz. drive strong Q1

Power Utilities	Sharekhan code: TATAPOWER

Reco/View: Buy	↔	CMP: **Rs. 226**	Price Target: **Rs. 260**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

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

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING 39.77

Updated July 08, 2022

High Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

Company details

Market cap:	Rs. 72,263 cr
52-week high/low:	Rs. 298/118
NSE volume: (No of shares)	293.7 lakh
BSE code:	500400
NSE code:	TATAPOWER
Free float: (No of shares)	169.8 cr

Shareholding (%)

Promoters	46.9
FII	10.1
DII	14.7
Others	28.3

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	8.7	0.6	-6.2	86.7
Relative to Sensex	4.7	-0.1	-2.7	81.6

Sharekhan Research, Bloomberg

Summary

- Strong start to FY2023 with 47% beat in reported PAT at Rs. 795 crore (up 103% y-o-y), supported by higher integrated CGPL + coal profit, strong growth in RE generation business, and standalone profit.
- Integrated CGPL + Coal PAT of Rs. 506 crore (versus loss of Rs. 178 crore in Q4FY2022) led by higher coal realisation/volume and partial benefit of full cost pass through for Mundra UMPP. However, solar EPC performance disappointed with loss of Rs. 33 crore on weak margin of only 1%; Tata Project reported huge loss of Rs. 222 crore due to write-offs.
- Mundra UMPP is operating under Section 11 and full cost pass through is provided till October 2022 and Tata Power is working on SPPA with Gujarat. A potential favourable tariff order by CERC and long-term agreement with states could turnaround Mundra UMPP.
- We maintain Buy on Tata Power with a revised PT of Rs. 260. At the CMP, the stock trades at 2.9x/2.6x its FY2023E/FY2024E P/BV.

Tata Power Company Limited's (TPCL) Q1FY23 reported PAT of Rs. 795 crore (up 103% y-o-y) was 47% above our estimate of Rs. 540 crore, led by higher integrated CGPL + coal profit, robust growth in RE power generation PAT, and strong standalone performance partially offset by loss in solar EPC/Tata Projects. Integrated CGPL + coal profits grew strongly by 3.4x y-o-y to Rs. 506 crore, led by higher coal profits (up 2.4x q-o-q to Rs. 968 crore) and likely lower loss at CGPL, given partial benefit of full cost through at Mundra (3 units operational) as per interim tariff under section 11 with effect from May 5, 2022. Coal profits were aided by higher coal realisation of $150/tonne (up 53% q-o-q) and volume recovery to 12 million tonne (up 15% q-o-q). Thus, PAT/tonne grew by 72% q-o-q to $25/tonne. Standalone PAT increased by 19% y-o-y to Rs. 421 crore, led by higher dividend income and tax benefit with CCPL merger. Renewable energy (RE) generation (TPREL + WREL) profit was up by 49% to Rs. 228 crore, reflecting higher power generation/sales and tariff revision benefit of Rs. 28 crore for WREL. However, solar EPC business continued to disappoint with EBITDA margin of only 1% (versus 3%/2% in Q1FY2022/ Q4FY2022) and net loss of Rs. 33 crore on higher module cost and forex loss, given adverse forex movement on USD liabilities, while Tata Project also made huge loss of Rs. 222 crore due to write-offs (as accounting losses on cost of project completion basis) and commodity price inflation. All four Odisha discoms (North, West, Central, and South) reported combined PAT of Rs. 9 crore versus net loss of Rs. 19 crore in Q1FY2022; however, TP Western Odisha Distribution Limited reported higher loss of Rs. 23 crore.

Key positives

- Integrated CGPL + coal business profit was up 3.4x y-o-y to Rs. 506 crore, given benefit of better coal margin and partial benefit of Mundra coal cost pass through to customers.
- RE power generation (TPREL + WREL) profit grew strongly by 49% y-o-y to Rs. 228 crore.

Key negatives

- Tata Power Solar System reported weak EBITDA margin of only 1% and net loss of Rs. 33 crore on higher module cost and forex loss.
- Tata Projects reported net loss of Rs. 222 crore due to write-offs.

Management Commentary

- Mundra UMPP is operating under section 11 of Electricity Act and full cost pass through (fixed + variable) is provided based in interim tariff decided by MoP. The current arrangement is valid till October 2022 and could be extended. CERC is expected to soon decide on final tariff.
- Solar EPC margin is expected to recover as new orders have revised module pricing, focus on contract manufacturing, lower commodity cost, and full currency hedging.
- FY2023 capex plan of Rs. 14,000 crore, of which ~Rs. 10,000 crore (which includes proposed Rs. 3,000 crore capex for 4GW solar cell and module manufacturing plant in TN) would be spent on renewable energy.
- Odisha discoms profits are expected to improve meaningfully in FY2024, led by regulatory capex, reduction in AT&C, and billing efficiency.
- Actively participating in power transmission bidding and expects ~Rs. 42,000 crore of RE transmission projects to come-up for bidding.
- Large solar EPC order book of Rs. 15,380 crore, which includes Rs. 14,626 crore for solar utility and Rs. 754 crore for rooftop solar.
- **Other updates -** 1) Consolidated net debt increased to Rs. 42,343 crore versus Rs. 39,708 crore as of March 2022, 2) Q1FY2023 capex stood at Rs. 2,000 crore, and 3) got CCI approval for RE deal and expects to receive first tranche of Rs. 2,000 crore soon.

Revision in estimates – We have largely maintained our FY2023-FY2024 earnings estimate.

Our Call

Valuation – We maintain our Buy rating on TPCL with a revised PT of Rs. 260: TPCL's focus on business restructuring (CGPL merger) and high-growth RE business and entry in to power transmission would play a crucial role for sustained earnings growth and improved earnings quality (expect RoE to improve to 12.1% in FY2024E versus only 7.8% in FY2022). In addition, management's business restructuring plans to increase the share of high-growth RE business would drive sustained improvement in ESG scores. Hence, we maintain Buy on Tata Power with a revised price target (PT) of Rs. 260. At the CMP, the stock is trading at 2.9x/2.6x its FY2023E/FY2024E P/BV. Turnaround of Mundra UMPP and higher profitability at Odisha discoms are catalysts.

Key Risks

1) Slower-than-expected ramp-up of RE portfolio and expansion in distribution business, 2) Lower-than-expected profitability in solar EPC business, 3) Delay in plan to monetise RE asset, and 4) Volatility in international coal prices.

Valuation (Consolidated) Rs cr

Particulars	FY21	FY22E	FY23E	FY24E
Revenue	32,468	42,816	47,567	51,905
OPM (%)	21.3	17.5	23.8	24.4
Adjusted PAT	1,283	1,741	2,784	3,150
% YoY growth	6.8	35.7	59.9	13.2
Adjusted EPS (Rs.)	4.0	5.4	8.7	9.9
P/E (x)	56.3	41.5	26.0	22.9
P/B (x)	3.2	3.2	2.9	2.6
EV/EBITDA (x)	15.1	15.1	9.7	8.5
RoNW (%)	6.1	7.8	11.8	12.1
RoCE (%)	6.1	6.5	9.6	11.3

Source: Company; Sharekhan estimates

Q1 PAT beats estimate on higher coal profit, partial benefit of Mundra tariff revision and strong RE generation profit

Q1FY23 reported PAT of Rs. 795 crore (up 103% y-o-y) was 47% above our estimate of Rs. 540 crore, led by higher integrated CGPL + coal profit, robust growth in RE power generation PAT, and strong standalone performance partially offset by loss in solar EPC/Tata Projects. Integrated CGPL + coal profits grew strongly by 3.4x y-o-y to Rs. 506 crore, led by higher coal profits (up 2.4x q-o-q to Rs. 968 crore) and likely lower loss at CGPL, given partial benefit of full cost through at Mundra (3 units operational) as per interim tariff under section 11 with effect from May 5, 2022. Coal profits were aided by higher coal realisation of $150/tonne (up 53% q-o-q) and volume recovery to 12 million tonne (up 15% q-o-q). Thus, PAT/tonne grew by 72% q-o-q to $25/tonne. Standalone PAT increased by 19% y-o-y to Rs. 421 crore, led by higher dividend income and tax benefit with CCPL merger. Renewable energy (RE) generation (TPREL + WREL) profit was up by 49% to Rs. 228 crore, reflecting higher power generation/sales and tariff revision benefit of Rs. 28 crore for WREL. However, solar EPC business continued to disappoint with EBITDA margin of only 1% (versus 3%/2% in Q1FY2022/ Q4FY2022) and net loss of Rs. 33 crore on higher module cost and forex loss, given adverse forex movement on USD liabilities, while Tata Project also made huge loss of Rs. 222 crore due to write-offs (as accounting losses on cost of project completion basis) and commodity price inflation. All four Odisha discoms (North, West, Central, and South) reported combined PAT of Rs. 9 crore versus net loss of Rs. 19 crore in Q1FY2022; however, TP Western Odisha Distribution Limited reported higher loss of Rs. 23 crore.

Conference call highlights

- **Mundra cost pass through update** - Mundra UMPP is operating under section 11 of Electricity Act and full cost pass through (fixed + variable) is provided based in interim tariff decided by MoP. The current arrangement is valid till October 2022 and could be extended as power demand seems strong. Management expects CERC to soon decide on the final tariff. TPCL is working with Gujarat to implement supplementary PPAs (SPPAs) and expects to work out similar agreements with other states. Management expects tariff to be cost reflecting without any adjustment and hopefully there would not be any under-recoveries going forward.
- **Solar EPC margin to improve gradually** - Solar EPC margin is expected to recover as new orders have revised module pricing, focus on contract manufacturing, lower commodity cost, and full currency hedging. Own manufacturing of solar cells and module would further reduce margin volatility in the business.
- **Capex plan** - FY2023 capex plan of Rs. 14,000 crore, of which ~Rs. 10,000 crore (which includes proposed Rs. 3,000 crore capex for 4GW solar cell and module manufacturing plant in TN) would be spent on renewable energy. The first/second phase of 4GW plant is expected by June/November 2023.
- **Transmission is a key focus area** - Actively participating in power transmission bidding and expects ~Rs. 42,000 crore of RE transmission projects to come up for bidding.
- **Solar EPC project commissioned** - 370MW/234MW for third party/in-house projects in QFY2023. Large solar EPC order book of Rs. 15,380 crore, which includes Rs. 14,626 crore for solar utility and Rs. 754 crore for rooftop solar. The company won new solar EPC order of 1.7 GW.
- **Other updates -** 1) Consolidated net debt increased to Rs. 42,343 crore versus Rs. 39,708 crore as of March 2022, 2) Q1FY2023 capex stood at Rs. 2,000 crore, 3) got CCI approval for RE deal and expects to receive the first tranche of Rs. 2,000 crore soon, 4) receivables increased by 40-50%, and 5) RE capacity of 5.5 GW, which includes installed capacity of 3.6 GW and 1.9 GW under various stages of implementation.

Results (Consolidated) Rs cr

Particulars	Q1FY23	Q1FY22	y-o-y (%)	Q4FY22	q-o-q (%)
Revenue	**14,495**	**10,132**	**43.1**	**11,960**	**21.2**
Total Expenditure	12,812	7,787	64.5	10,091	27.0
Reported operating profit	**1,683**	**2,345**	**-28.2**	**1,869**	**-9.9**
Other Income	143	178	-19.4	259	-44.8
EBITDA	1,827	2,523	-27.6	2,128	-14.2
Interest	1,026	945	8.5	1,015	1.1
Depreciation	822	747	10.0	846	-2.8
Exceptional income/(expense)	0	0.0	NA	0	NA
Reported PBT	**-21**	**830**	**-102.6**	**268**	**-108.0**
Add: Net movement in regulatory deferral account balances (net of tax)	280	-158.0	-277.5	125	124.0
Add: Share of Profit of Associates and JV	803	366.0	119.4	296	171.3
Exceptional income/(expense)	0	0	NA	-150	NA
PBT after regulatory deferral account and share of profit from JV	**1,062**	**1,038**	**2.3**	**539**	**97.2**
Tax	179	573	-68.8	-562	-131.8
Reported PAT before MI	**884**	**466**	**89.7**	**1,100**	**-19.7**
Minority Interest	89	75	19.1	129	-31.2
Reported PAT after MI	**795**	**391**	**103.1**	**971**	**-18.2**
Add: Profit from Discontinued Operations	0	0	NA	-468	NA
Reported PAT	**795**	**391**	**103.1**	**503**	**57.9**
Adjusted PAT	**795**	**391**	**103.1**	**653**	**21.6**
No. of Equity Shares (cr)	319.6	319.6	0.0	319.6	0.0
Reported EPS (Rs.)	2.5	1.2	103.1	1.6	57.9
Adjusted EPS (Rs.)	2.5	1.2	103.1	2.0	21.6
Margins (%)			**BPS**		**BPS**
OPM	11.6	23.1	-1,153	15.6	-401
NPM	5.5	3.9	162	5.5	2
Effective tax rate	16.8	55.1	-3,833	-104.3	NA

Source: Company, Sharekhan Research

TPCL's consolidated performance for Q1FY2023 Rs cr

Particulars	Op Income		EBITDA^^		PAT	
	Q1 FY23	Q1 FY22	Q1 FY23	Q1 FY22	Q1 FY23	Q1 FY22
Consolidated before exceptional items	14,776	9,974	2,107	2,365	884	466
Standalone & Key Subsidiaries						
Tata Power (Standalone)	5,270	2,761	1,271	1,405	421	354
MPL (Maithon Power)*	755	704	188	190	80	79
TPDDL (Delhi Discom)**	3,123	2,107	341	351	121	123
TPTCL (Power Trading)	73	59	(14)	20	(12)	13
Tata Power Solar (Solar EPC)	1,353	1,949	15	74	(33)	22
TPREL Standalone (Renewable Power)	442	311	371	251	54	24
WREL (Renewable Power)	381	334	357	317	170	123
Coal SPVs (Investment Companies)	0	0	(8)	(1)	(83)	(40)
TERPL (Shipping Co)	166	154	59	40	26	10
TP Central Odisha Dist Ltd (CESU)**	1,298	1,010	67	3	7	(28)
TP Southern Odisha Dist Ltd (SOUTHCO)**	521	421	45	53	18	15
TP Western Odisha Dist Ltd (WESCO)**	1,356	995	5	24	(23)	(3)
TP Northern Odisha Dist Ltd (NESCO)**	786	596	43	28	7	(3)
TPIPL (Overseas Investment Co)	-	-	8	7	(11)	(5)
Others	270	228	51	56	0	10
Total – Before JVs & Associates	15,794	11,630	2,798	2,817	744	695
Joint Venture and Associates	-	-	-	-	803	366
Total – Before Eliminations	15,794	11,630	2,798	2,817	1,547	1,061
Eliminations#	(1,018)	(1,656)	(691)	(452)	(663)	(595)
Total	14,776	9,974	2,107	2,365	884	466

Previous year numbers are restated

*TPCL stake-74%; **TPCL stake-51%; # Eliminations include inter-company transactions; ^^ including other income

Source: Company

Share of JVs and Associates

Rs cr

Particulars	% Share	Op Income		EBITDA		PAT	
		Q1 FY23	Q1 FY22	Q1 FY23	Q1 FY22	Q1 FY23	Q1 FY22
Coal & Infra Companies (KPC, BSSR, AGM & NTP)	30% / 26%	4,859	2,599	1,437	747	968	319
Powerlinks Trans Ltd	51%	16	15	15	15	10	10
Industrial Energy Ltd	74%	65	53	46	38	31	24
Resurgent Power	26%	270	259	65	71	14	20
Tata Projects	48%	1,723	1,489	(210)	66	(222)	(13)
Others JVs		8	18	10	19	2	5
Total		**6,941**	**4,433**	**1,362**	**956**	**803**	**366**

Source: Company

Odisha Discoms performance in Q1FY2023

Rs cr

Q1 FY 23 Highlights	TPCODL	TPSODL	TPWODL	TPNODL
Purchase (Mus)	2,893	1,169	2,941	1,666
Sales (Mus)	2,201	891	2,280	1,346
Revenue per unit	5.69	5.84	5.76	5.56
Power Cost per unit	3.25	2.52	3.89	3.46
Actual Technical losses YTD (%)	23.9%	23.7%	22.5%	19.2%
Actual AT&C losses YTD (%)	35.7%	40.3%	36.4%	30.1%
Vesting order Target AT&C losses (%)	23.7%	25.8%	20.4%	19.2%
Income from Operation	1,298	521	1,356	786
EBITDA	67	45	5	43
PAT	**7**	**18**	**(23)**	**7**

Source: Company

Tata Power Solar Systems Limited –Weak Q1FY2023 margin of only 1%

Rs cr

Particulars	Q1 FY23	Q1 FY22	Qtr Var	Quarter Variance Remarks
Operating Income	1,353	1,949	(596)	Lower execution of large projects due to change in timelines
Operating expenses	1,340	1,891	551	Lower execution offset by higher commodity prices
Operating profit	**12**	**58**	**(46)**	
Other income	2	16	(14)	
EBITDA	**15**	**74**	**(59)**	
Interest cost	42	30	(12)	Higher bank guarantee and adverse forex movement on dollar liabilities
Depreciation	15	15	(1)	
PBT	**(42)**	**30**	**(72)**	
Tax	(9)	8	17	
PAT	**(33)**	**22**	**(55)**	

Source: Company

TPCL's Debt Profile

Rs cr

Source: Company

PARTICULARS	CONSOLIDATED				
	Q1 FY23			Q4 FY22	Q1 FY22
	Rupee	Forex	Total	Total	Total
Long term	29,227	787	30,014	32,730	29,226
Short term	9,644	1,363	11,007	6,975	13,433
Current Maturity of LT	6,146	2,526	8,672	7,885	5,842
Total Debt	**45,017**	**4,676**	**49,693**	**47,590**	**48,502**
Less: Cash & Cash equivalent			5,987	7,051	9,006
Less: Debt against dividend in Coal SPVs			1,363	830	598
Net External Debt			**42,343**	**39,708**	**38,898**
Equity			**27,284**	**26,028**	**24,753**
Net Debt to Equity			**1.55**	**1.53**	**1.57**

Source: Company

Outlook and Valuation

■ **Sector view - Regulated tariffs provide earnings visibility; Reforms to strengthen balance sheets of power companies**

India's power sector is regulated by the CERC with an availability-based earnings model (fixed RoE on power generation assets). Thus, the regulated tariff model provides strong earnings visibility for power-generation, transmission and distribution companies. Moreover, the government's power sector package of over Rs. 3 lakh crore announced in the Union Budget 2021 would help power discoms clear dues of power generation and transmission companies. This would reduce receivables of the power sector and strengthen balance sheets of companies.

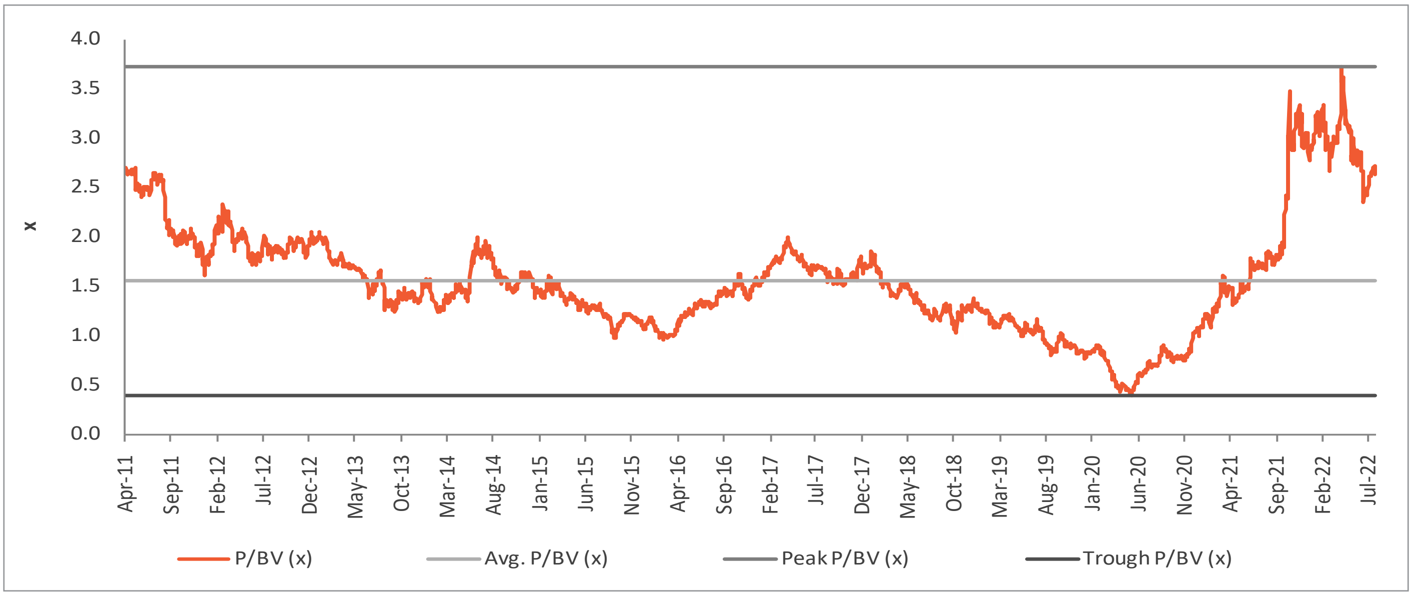
■ **Company outlook - Focus on distribution and RE business to drive robust earnings growth**

Tata Power has a well-planned strategy to shift towards clean energy and targets to treble PAT to over Rs. 3,600 crore and double RoE to 12.1% by FY2025 (versus 7.8% in FY2022). We believe growth would be driven largely by distribution and the RE business. We expect PAT to register a CAGR of 35% over FY2021-FY2024E with sharp improvement in RoE to 12.1% by FY2024E.

■ **Valuation - We maintain our Buy rating on TPCL with a revised PT of Rs. 260**

TPCL's focus on business restructuring (CGPL merger) and high-growth RE business and entry in to power transmission would play a crucial role for sustained earnings growth and improved earnings quality (expect RoE to improve to 12.1% in FY2024E versus only 7.8% in FY2022). In addition, management's business restructuring plans to increase the share of high-growth RE business would drive sustained improvement in ESG scores. Hence, we maintain Buy on Tata Power with a revised price target (PT) of Rs. 260. At the CMP, the stock is trading at 2.9x/2.6x its FY2023E/FY2024E P/BV. Turnaround of Mundra UMPP and higher profitability at Odisha discoms are catalysts.

One-year forward P/BV (x) band



Source: Sharekhan Research

About company

Tata Power is India's largest integrated private power company present in power generation (capacity of 12808 MW with 69% from thermal and 31% from renewables), transmission, distribution (largest private sector player with a customer base of 11.7 million), trading, and solar EPC (largest solar EPC player in India).

Investment theme

Tata Power's core earnings are resilient even in demand down cycle as it gets regulated returns on power generation and distribution assets. The company's focus to shift from a B2G to B2C model would drive robust earnings growth (to be driven by RE and distribution business) over the next 4-5 years and materially improve its RoE to ~9.4% by FY2024E (from just 6.1% in FY2021). Monetisation of renewable assets and potential improvement in ESG rating could re-rate the company, while focus on debt reduction would strengthen balance sheet.

Key Risks

- Slower-than-expected ramp-up of RE portfolio and expansion in distribution business.
- Lower-than-expected profitability in solar EPC business. Continued losses at Mundra UMPP in case of high imported coal prices.
- Delay in plan to monetise RE assets.
- Volatility in international coal prices.

Additional Data

Key management personnel

Mr. Natarajan Chandrasekaran	Chairman
Dr. Praveer Sinha	Managing Director and CEO
Ramesh Subramanyam	CEO and Managing Director

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corporation of India	6.75
2	Vanguard Group Inc	2.34
3	Blackrock Inc	1.36
4	HDFC Life Insurance	1.22
5	Matthews International Capital Management LLC	1.18
6	Matthews Pacific Tiger FD	1.12
7	Franklin Resources Inc	0.57
8	L&T Mutual Fund Trustee/India	0.50
9	Dimensional Fund Advisors LP	0.44
10	Kotak Mahindra Asset Management Co Ltd	0.40

Source: Bloomberg (old data)

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

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