Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

CESC Ltd

Steady Q1; valuation attractive & healthy dividend yield

Power	Sharekhan code: CESC		
Reco/View: Buy ↔	CMP: Rs. 79	Price Target: Rs. 95 ↔	

↑ 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 34.35

Updated July 08, 2022

High Risk

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

Source: Morningstar

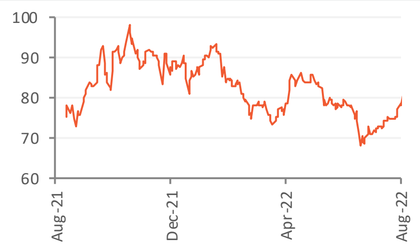
Company details

Market cap:	Rs. 9,907 cr
52-week high/low:	Rs. 102/68
NSE volume: (No of shares)	19.2 lakh
BSE code:	500084
NSE code:	CESC
Free float: (No of shares)	63.5 cr

Shareholding (%)

Promoters	52
FII	14
DII	21
Others	13

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	9.2	-0.6	-5.3	4.9
Relative to Sensex	-1.0	-12.7	-7.3	-3.2

Sharekhan Research, Bloomberg

Summary

- Q1FY23 consolidated PAT grew by 5.5% y-o-y to Rs. 286 crore led by strong profit growth of 2.8x/17% y-o-y from Dhariwal Infrastructure/Noida Power, profitable operations at RJ DF, lower tax rate which was partially offset by lower earnings from Haldia Energy/Crescent Power and a loss at Malegaon DF.
- WBERC tariff order does not provide for higher power tariffs and thus standalone PAT was flat y-o-y at Rs. 138 crore despite strong 17.5% y-o-y growth in power sales volume.
- Strong power demand and 210 MW medium-term PPA with Central Railway bodes for higher PLF for Chandrapur; thus we expect Dhariwal Infra to post strong PAT growth in FY23. Rajasthan DF to break-even in FY23 versus loss of Rs. 30 crore seen in FY22.
- We maintain a Buy on CESC with an unchanged PT of Rs. 95 crore given attractive valuation of 0.9x FY24E P/BV and dividend yield of ~6%. Turnaround of power distribution businesses could create value.

CESC reported a steady growth of 5.5% y-o-y in its consolidated PAT to Rs. 286 crore in Q1FY23 as sharp rise of 184%/17% y-o-y in earnings from Dhariwal infrastructure/ Noida Power, profitable operations at Rajasthan DF and a lower tax rate of 17.3% (versus 28.8% in Q1FY22) was partially offset by decline of 27%/43% y-o-y in profits from Haldia Energy/Crescent Power and a loss at Malegaon DF. Standalone PAT was flat y-o-y at Rs. 138 crore as there was no tariff hike in WBERC tariff order, while fuel cost surged. However, standalone power sales volumes grew strongly by 17.5% y-o-y to 3,049 million units. Dhariwal Infrastructure PAT of Rs. 71 crore (up 2.8x y-o-y) got a boost from a higher plant load factor (PLF) of 86.31% (versus 84.95% in Q1FY22) as power supply started for 210 MW medium-term PPA with Central Railways and higher power prices (benefit of Rs. 10-15 crore) on energy exchanges. Rajasthan DF's PAT stood at Rs. 6 crore (versus net loss of Rs. 11 crore) led by volume recovery across Kota/Bharatpur/Bikaner.

Key positives

- Dhariwal Infra reported robust PAT growth of 184% y-o-y led by improved PLF and a higher merchant power rate.
- Rajasthan DF was profitable with PAT of Rs. 6 crore versus loss of Rs. 11 crore in Q1FY22.

Key negatives

- Malegaon reported loss of Rs. 19 crore versus marginal profit of Rs. 2 crore in Q1FY22.
- WBERC Tariff order does not provide for higher power tariff for standalone business.

Revision in estimates – We have fine-tuned our FY23 standalone earnings estimates to factor Q1FY23 performance and maintain our FY24 earnings estimates.

Our Call

Valuation - Maintain Buy with an unchanged SoTP-based PT of Rs. 95: CESC is a play on investment and turnaround of the power distribution business, while earnings are expected to gradually improve with a further rise in in utilisation at Dhariwal Infrastructure and potential turnaround of Rajasthan/Malegaon DF in FY24E, while standalone business is largely stable given regulated RoE model. Valuation is attractive at 0.9x its FY2024E P/BV and the stock offers a healthy dividend yield of ~6%. Hence, we maintain a Buy on CESC with an unchanged SoTP-based PT of Rs. 95.

Key Risks

Sustained losses in distribution franchisee for an extended period and lower utilisation at Chandrapur plant.

Valuation (Standalone) Rs cr

Particulars	FY21	FY22	FY23E	FY24E
Revenue	6,921	7,294	8,087	8,849
OPM (%)	17.0	15.3	17.0	17.5
PAT	814	816	914	1,039
% y-o-y growth	(11.3)	0.2	12.0	13.7
EPS (Rs.)	6.1	6.2	6.9	7.8
P/E (x)	13.0	12.9	11.6	10.2
P/B (x)	1.1	1.1	1.0	0.9
EV/EBITDA (x)	13.5	15.9	11.3	9.5
RoCE (%)	6.2	6.7	6.7	7.9
RoE (%)	8.1	8.2	8.9	9.5

Source: Company; Sharekhan estimates

Steady consolidated earnings growth in Q1; Dhariwal Infra continues to report robust growth

CESC reported a steady growth of 5.5% y-o-y in its consolidated PAT to Rs. 286 crore as sharp rise of 184%/17% y-o-y in earnings from Dhariwal infrastructure/Noida Power, profitable operations at Rajasthan DF and a lower tax rate of 17.3% (versus 28.8% in Q1FY22) was partially offset by decline in of 27%/43% y-o-y in profits from Haldia Energy/Crescent Power and a loss at Malegaon. Standalone PAT was flat y-o-y at Rs. 138 crore as there was no tariff hike in WBERC tariffs, while fuel cost surged. However, standalone power sales volumes grew strongly by 17.5% y-o-y to 3,049 million units. Dhariwal Infrastructure PAT of Rs. 71 crore (up 2.8x y-o-y) got a boost from a higher plant load factor (PLF) of 86.31% (versus 84.95% in Q1FY22) as power supply started for 210 MW medium-term PPA with Central Railways and higher power prices (benefit of Rs. 10-15 crore) on energy exchanges.

Results (Standalone) Rs cr

Particulars	Q1FY23	Q1FY22	YoY(%)	Q4FY22	QoQ(%)
Revenue	**2,672**	**2,048**	**30.5**	**1,811**	**47.5**
Total expenditure	1,898	1,601	18.6	1,412	34.4
Operating profit	**774**	**447**	**73.1**	**399**	**93.9**
Other Income	20	14	42.9	81	(75.3)
Depreciation	120	118	1.7	120	0.0
Finance Cost	134	127	5.5	130	3.1
PBT	173	175	(1.1)	332	(47.9)
Tax	35	37	(5.4)	73	(52.1)
Reported PAT	**138**	**138**	**0.0**	**259**	**(46.7)**
EPS (Rs.)	10.4	10.4	0.0	19.5	(46.7)
Margin (%)			**bps**		**Bps**
OPM (%)	16.8	16.1	68	10.9	586
NPM (%)	5.9	7.1	-127	16.1	-1,021
Tax Rate (%)	20.2	21.1	-91	22.0	-176

Source: Company, Sharekhan Research

Financial performance of key subsidiaries Rs cr

Particulars	Revenue		PAT	
	Q1FY23	Q1FY22	Q1FY23	Q1FY22
Haldia Energy	477	583	66	90
Dhariwal Infrastructure	484	387	71	25
Crescent Power	30	61	4	7
Noida Power	681	455	34	29
Kota/Bharatpur/Bikaner	599	423	6	(11)
Malegaon	135	131	(19)	2

Source: Company, Sharekhan Research

Results (Consolidated) Rs cr

Particulars	Q1FY23	Q1FY22	y-o-y (%)	Q4FY22	q-o-q (%)
Revenue	**4102**	**3216**	**27.5%**	**3011**	**36.2%**
Total Expenditure	3452	2448	41.0%	2315	49.1%
Operating profit	**650**	**768**	**-15.4%**	**696**	**-6.6%**
Other income	44	26	69.2%	81	-45.7%
Depreciation	217	219	-0.9%	223	-2.7%
Interest	265	283	-6.4%	298	-11.1%
PBT	212	292	-27.4%	256	-17.2%
Regulatory income	147	101	45.5%	328	-55.2%
PBT	**359**	**393**	**-8.7%**	**584**	**-38.5%**
Tax	62	113	-45.1%	139	-55.4%
PAT before MI	**297**	**280**	**6.1%**	**445**	**-33.3%**
Minority interest (MI)	11	9	22.2%	21	-47.6%
Reported PAT	**286**	**271**	**5.5%**	**424**	**-32.5%**
EPS	2.2	2.0	5.5%	3.2	-32.5%
Margin (%)			**BPS**		**BPS**
OPM	15.8	23.9	-803	23.1	-727
NPM	7.0	8.4	-145	14.1	-711
Tax rate	17.3	28.8	-1148	23.8	-653

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector View – Regulated tariff model provides earnings visibility for power-generation companies

India's power sector is regulated by the Central Electricity Regulatory Commission (CERC) through an availability-based earnings model (fixed RoE on power-generation assets) and, thus, the regulated tariff model provides strong earnings visibility for power-generation companies such as CESC. Improved power demand (except for April-May 2021 given the lockdown, yet situation is better as compared to last year) would drive up PLFs for power-generation companies and better PLF incentive income. Additionally, receivables of power-generation companies are likely to reduce in FY2022 as an economic recovery would result in timely receipt of dues from customers.

■ Company Outlook – Steady performance by standalone biz, turnaround of subsidiaries to improve consolidated earnings

CESC is quite optimistic that FY2023 would see better earnings given recovery in power demand in the standalone business. Recovery in earnings from standalone operations, lower losses at distribution franchisees led by lower T&D losses, and higher utilisation at Dhariwal Infrastructure are expected to improve consolidated earnings of CESC over FY2023E-FY2024E.

■ Valuation – Maintain Buy with an unchanged SoTP-based PT of Rs. 95

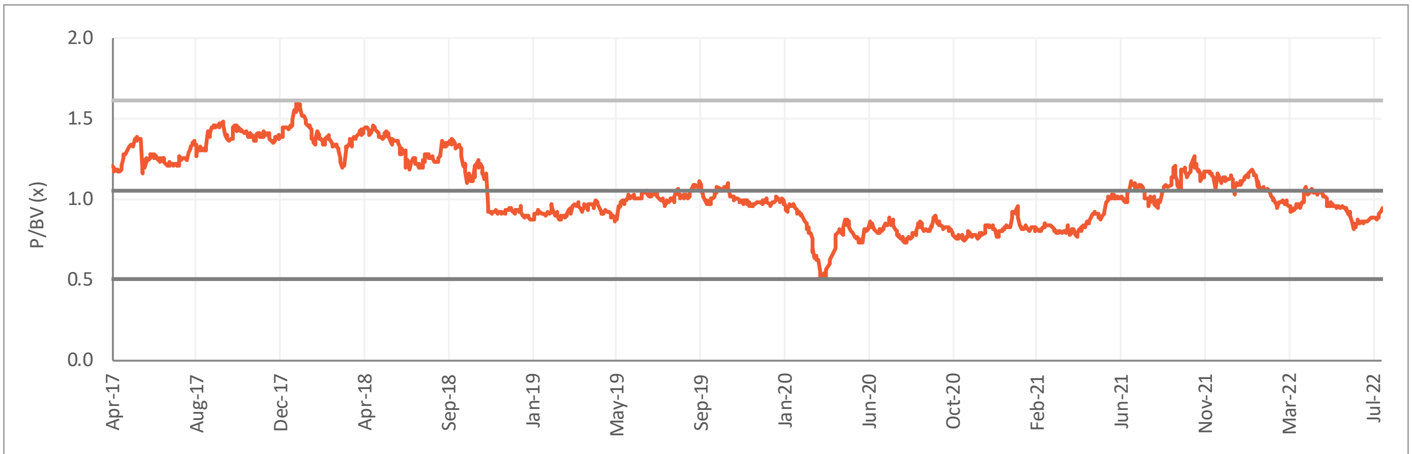
CESC is a play on investment and turnaround of the power distribution business, while earnings are expected to gradually improve with a further rise in in utilisation at Dhariwal Infrastructure and potential turnaround of Rajasthan/Malegaon DF in FY24E, while standalone business is largely stable given regulated RoE model. Valuation is attractive at 0.9x its FY2024E P/BV and the stock offers a healthy dividend yield of ~6%. Hence, we maintain a Buy on CESC with an unchanged SoTP-based PT of Rs. 95.

SoTP-based PT of Rs. 95

Particulars	Value (Rs. /share)	Methodology
Standalone business	56	8x FY23E EPS
Haldia	15	1.7x regulated equity of ~Rs. 1150 crore
Dhariwal	17	2.3x regulated equity of ~Rs. 1000 crore
Crescent Power	1	6.5x FY21 PAT for 67.8% stake
Noida	4	2x regulated equity of ~Rs. 400 crore for 72.73% stake
DF	2	0.6x Investments
Price target	**95**	

Source: Company, Sharekhan Research

One-year forward P/BV (x) band



Source: Sharekhan Research

About company

CESC started operations in 1899. The company 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 has a distribution license within 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 DF make 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 DF 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	6.68
2	ICICI Prudential India OPP	3.74
3	ICICI Prudential Asset Management Co Ltd/ India	3.04
4	Life Insurance Corp of India	3.03
5	Massachusetts Financial Services	2.34
6	UTI Asset Management Co Ltd	2.12
7	Vanguard Group Inc	1.57
8	Aditya Birla Sun Life Trustee Co Pvt Ltd	1.24
9	Aditya Birla Sun Life Asset Management Co Ltd	1.24
10	FIL Ltd	0.93

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

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