Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Power Grid Corporation of India Ltd

Steady Q3; attractive valuation & healthy dividend yield

Power	Sharekhan code: POWERGRID

Reco/View: Buy	↔	CMP: **Rs. 213**	Price Target: **Rs. 265**	↔

↑ 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 Updated Dec 08, 2022	26.33

Medium Risk

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

Source: Morningstar

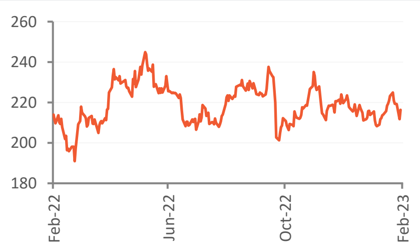
Company details

Market cap:	Rs. 1,48,438 cr
52-week high/low:	Rs. 248/186
NSE volume: (No of shares)	119.3 lakh
BSE code:	532898
NSE code:	POWERGRID
Free float: (No of shares)	339 cr

Shareholding (%)

Promoters	51.3
FII	32.8
DII	12.7
Others	3.2

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-1.3	-6.7	-4.8	-0.6
Relative to Sensex	0.9	-5.2	-7.5	-1.2

Sharekhan Research, Bloomberg

Summary

- Q3FY23 standalone PAT grew by 10.5% y-o-y to Rs. 3,702 crore (above estimate) led by higher dividend income and lower tax rate of 7.9%, which offset muted asset capitalization.
- Standalone/consolidated asset capitalisation was muted at Rs. 2,866 crore/Rs. 5,190 crore; down 78%/72% y-o-y in 9MFY23. Q4FY23 asset capitalisation is likely to be robust given full-year guidance of Rs. 10,000-12,000 crore (lower than earlier guidance of Rs. 13,000 crore). Overall receivables continue to increase and stood at Rs. 9234 crore, up 36% q-o-q.
- Management guided for FY24 capex/asset capitalisation of Rs. 8,800 crore/Rs. 10,000 crore but expects upside to these number given strong Rs. 40,000-50,000 crore of transmission bid pipeline. Asset monetisation delays are disappointing, but the management hinted at maintaining dividend payout ratio of 60%. Power Grid has projects worth Rs. 47,600 crore.
- We maintain a Buy on Power Grid with an unchanged PT of Rs. 265 as valuation of 1.6x/1.4x FY24E/FY25E P/BV seems attractive given expectation of 10% PAT CAGR over FY22-25E, RoE of 18% and a dividend yield of ~6-7%.

Power Grid Corporation of India Limited's (Power Grid) standalone Q3FY23 PAT increased by 10.5% y-o-y to Rs. 3,702 crore (7% above our estimate of Rs. 3,452 crore) led by high other income (up 14.4% y-o-y) and a sharply lower tax rate of 7.9% (versus 20.2% in Q3FY22). However, operational performance was muted with asset capitalisation of Rs. 1,189 crore (versus Rs. 3854 crore in Q3FY22) and lower incentive/surcharge income of Rs. 130 crore/Rs. 34 crore (versus Rs. 147 crore/Rs. 38 crore in Q3FY22). Dividend/interest income from subsidiaries/JVs increased to Rs. 189 crore/Rs. 289 crore (versus Rs. 143 crore/Rs. 218 crore in Q3FY22) and interest on differential tariffs at Rs. 74 crore versus Rs. 54 crore in Q3FY22.

Key positives

- Transmission bid pipeline strong at Rs. 40000-50000 crore for next 12 months.
- Declared second interim dividend of Rs. 5/share and thus taking total DPS to Rs. 10/share (implies 5% dividend yield) so far in FY23.

Key negatives

- Lowered asset capital guidance to Rs. 10,000-12,000 crore for FY23.
- Consolidated asset capitalisation was muted at Rs. 2,886 crore in 9MFY23 versus Rs. 12,992 crore in 9MFY22.
- Delay in asset monetisation.

Management Commentary

- FY24 asset capitalisation/capex guidance of Rs. 10,000 crore/Rs. 8,800 crore. However, these numbers could see upside if the company is able to win new transmission bids (bid pipeline of Rs. 40,000-50,000 crore for the next 12 months).
- TBCB project IRR under pressure given intensified competition. Power Grid focus is to gain market share.
- Asset onetization (initial target of Rs. 6,800 cr for FY23) is seeing delay as valuation getting impacted given rise in interest rate/yield expectation. Also, working on new monetisation structure as now assets must come back to owner under NMP. The company is now looking at securitization worth Rs. 3000 crore by March 2023.
- Smart metering bidding conducted for 1 crore meters for two discoms in Gujarat. Estimated capex of Rs. 5,500-6,000 crore and revenue expectation of Rs. 700 crore. Looking for opportunities in other states like Mizoram.
- Work in hand worth Rs. 47,600 crore (**Ongoing projects –** Rs. 7,600 crore, **New projects –** Rs. 27,000 crore and **TBCB projects –** Rs. 13,000 crore). Estimated ISTS investment of Rs. 2.44 lakh crore from 500 GW RE projects by FY30.

Revision in estimates – We have fine-tuned our estimate FY24-25 earnings estimates to factor 9MFY23 performance and asset monetisation guidance.

Our Call

Valuation – Maintain Buy on Power Grid with an unchanged PT of Rs. 265: Power Grid has a robust project pipeline worth Rs. 47,600 crore and has capitalised ~Rs. 20,695 crore in FY22, which provides earnings visibility for 2-3 years. We thus expect a 10% CAGR in PAT over FY2022-FY2025E along with RoE of ~18-19% in FY25E. We maintain a Buy on Power Grid with an unchanged PT of Rs. 265, as valuation of 1.6x/1.4x FY24E/FY25E P/BV seems attractive considering decent growth outlook, healthy RoE and a dividend yield of ~6-7%.

Key Risks

1) Slower-than-expected capitalisation of projects and 2) Inability to win new projects under tariff-based competitive bidding route.

Valuation (Consolidated) Rs cr

Particulars	FY22	FY23E	FY24E	FY25E
Revenue	41,616	45,570	49,899	54,390
OPM (%)	87.9	86.1	86.2	86.0
Adjusted PAT	13,504	14,776	15,563	18,153
y-o-y growth (%)	3.0	9.4	5.3	16.6
Adjusted EPS (Rs.)	19.4	21.2	22.3	26.0
P/E (x)	11.0	10.0	9.5	8.2
Price/ Book (x)	1.9	1.8	1.6	1.4
EV/EBITDA (x)	7.6	6.5	5.8	5.1
RoCE (%)	11.2	11.5	12.1	12.7
RoE (%)	18.5	18.6	17.8	18.5

Source: Company; Sharekhan estimates

Steady Q3 PAT growth on lower tax rate; asset capitalization remain muted

Standalone Q3FY23 revenues grew by 7.4% y-o-y to Rs. 10,746 crores, which was 5.7% below our estimate of Rs.11,392 crore. Revenues from the transmission business was up by 7.3% y-o-y to Rs. 10,518 crores. The operating profit margin (OPM) at 87.3% (down 40 bps y-o-y) was 317 bps above our estimate of 84.1%. Operating profit at Rs. 9,379 crore (up 7.9% y-o-y) was 2.1% below our estimate of Rs. 9,582 crores due to miss in revenue partially offset by beat in margin. PAT increased by 10.5% y-o-y to Rs. 3,702 crore (7% above our estimate of Rs. 3,452 crore) led by high other income (up 14.4% y-o-y) and sharply lower tax rate of 7.9% (versus 20.2% in Q3FY22). However, operational performance was muted with asset capitalization of Rs. 1189 crore (versus Rs. 3,854 crore in Q3FY22) and lower incentive/surcharge income of Rs. 130 crore/Rs. 34 crore (versus Rs. 147 crore/Rs. 38 crore in Q3FY22). Dividend/interest income from subsidiaries/JVs increased to Rs. 189 crore/ Rs. 289 crore (versus Rs. 143 crore/Rs. 218 crore in Q3FY22) and interest on differential tariffs at Rs. 74 crore versus Rs. 54 crore in Q3FY22.

Q3FY23 earnings conference call highlights

- **Capitalisation & capex guidance:** The management lowered its capitalisation guidance to Rs. 10,000-12,000 crore for FY23 from Rs. 13,000 crore. They have provided a capitalisation target of Rs. 10,000 crore for FY24 (large part will be TBCB) and have guided for capex of Rs. 8800 crore for FY24. The company expects to see a pick-up in transmission bidding activity to pick-up and expects upside to capex/asset capitalisation guidance.
- **Asset monetisation getting delayed:** Asset monetisation target for FY23 was initially projected at Rs. 6,800 crore but the same is seeing delay as valuation has declined as uptick in interest rate has raised yield expectation. The company is looking at securitization of cashflow for raising fund and plans to raise Rs. 3000 cr by March 2023
- **Smart meter update –** The company has conducted biding for 1 crore smart meters in Gujarat (2 discoms) and also looking for opportunities in other states like Mizoram. The management has indicated a capex of Rs.5500-6000 crore for 1 crore smart meters with a completion period of 2 years. It would be a rental model for smart meter with revenues potential of 700 crore
- **Transmission opportunities –** bidding activity to pick up: The company hinted at estimated ISTS investment of Rs. 2.44 lakh crore from 500 GW RE projects by FY30. This would require an additional 50,890 ckm of transmission lines and 433575 MVA sub-stations capacity. In next 12 months, ~Rs. 40,000-50,000 crore of new transmission projects will come under bidding and Power Grid is focused on market share. The management mentioned that intra state opportunity size is limited as states are doing projects on its own expect of few states like Rajasthan/UP.
- **Work in hand worth status:** The company has total work in hand of Rs. 47,600 crore (Ongoing projects – Rs. 7,600 crore, New projects – Rs. 27,000 crore and TBCB projects – Rs. 13,000 crore). This includes Rs. 22000 crore for Leh-Ladakh project (capex to start in FY24 and to get completed in 5 years). The company also mentioned that except for Leh-Ladakh project, rest of works in hand is expected to get completed in 2 years.
- **Other updates –** 1) Finance costs have increased due to a rise in capitalization, exchange rate variation and increase in floating rates, 2) Management indicated to maintain dividend payout at 60% and 3) Outstanding receivables increased to Rs. 9234 crore in Q3FY23 versus Rs. 6,777 crore in Q2FY23.

Results (Standalone) Rs cr

Particulars	Q3FY23	Q3FY22	YoY (%)	Q2FY23	QoQ (%)
Revenues	**10,746**	**10,002**	**7.4**	**10,656**	**0.9**
Total Expenditure	1,367	1,313	4.1	1,698	(19.5)
Operating profit	**9,379**	**8,689**	**7.9**	**8,958**	**4.7**
Other income	726	635	14.4	535	35.8
Depreciation	3,304	3,193	3.5	3,219	2.6
Interest	3,037	1,852	64.0	2,206	37.7
PBT	**3,765**	**4,279**	**(12.0)**	**4,068**	**(7.4)**
Tax	**297**	**862**	**(65.6)**	**383**	**(22.4)**
Regulatory Deferral A/c	234	-67	(447.1)	-34	(786.7)
Reported PAT	**3,702**	**3,349**	**10.5**	**3,651**	**1.4**
Reported EPS	5.3	4.8	10.5	5.2	1.4
Adjusted EPS	5.3	4.8	10.5	5.2	1.4
Margin (%)			**bps**		**bps**
OPM	87.3	86.9	40.5	84.1	321
NPM	34.4	33.5	95.8	34.3	18
Tax rate	7.9	20.2	(1,226.6)	9.4	-152

Source: Company, Sharekhan Research

Segmental performance (standalone) Rs cr

Particulars	Q3FY23	Q3FY22	YoY (%)	Q2FY23	QoQ (%)
Revenue					
Transmission	10,518	9,801	7.3	10,412	1.0
Consultancy	172	171	0.1	139	23.3
Telecom	210	185	13.2	205	2.2
Intersegment	-19	-17	6.6	-19	(2.4)
Net Revenue	**10,880**	**10,140**	**7.3**	**10,737**	**1.3**
EBIT					
Transmission	6,328	5,454	16.0	5,662	11.8
Consultancy	78	57	37.1	40	96.3
Telecom	86	69	24.0	77	11.5
Overall EBIT	**6,493**	**5,581**	**16.3**	**5,779**	**12.4**
EBIT margin (%)			**bps**		**bps**
Transmission	60.2	55.7	452	54.4	579
Consultancy	45.7	33.4	1,231	28.7	1,698
Telecom	40.9	37.4	359	37.6	339
Overall EBIT margin	**59.7**	**55.0**	**464**	**53.8**	**585**

Source: Company, Sharekhan Research

Outlook and Valuation

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

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

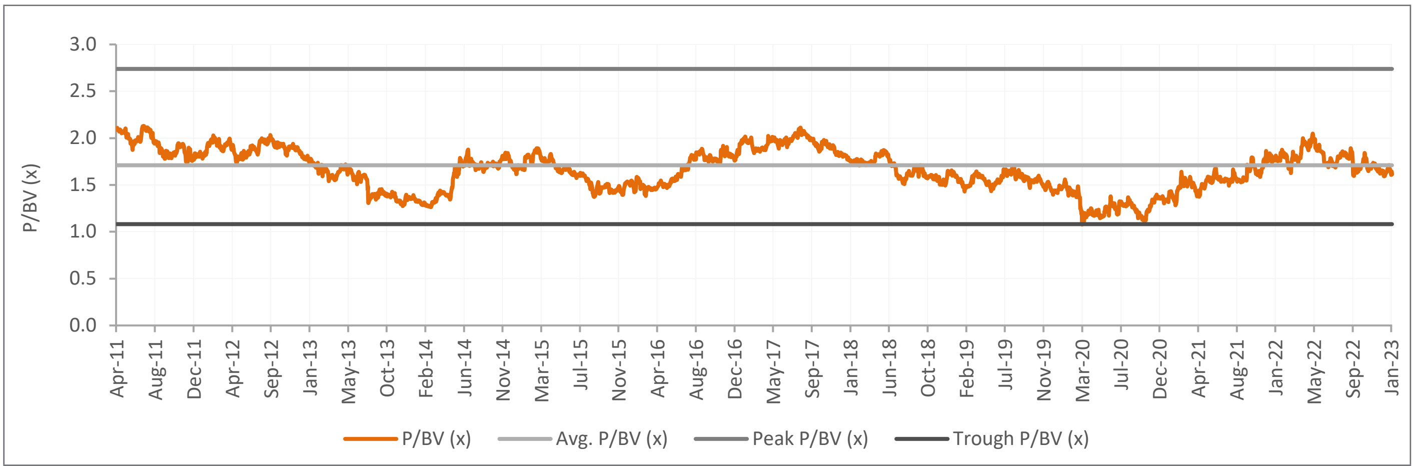
■ **Company Outlook – Earnings visibility led by robust capitalization in last one year**

Robust capitalisation in the past 12 months and work-in-hand pipeline of ~Rs. 47,600 crore provide healthy earnings growth visibility (we expect a 10% PAT CAGR over FY2022-FY2025E). Capex/capitalisation guidance of Rs. 8,800 crore/Rs. 10,000-12,000 crore each for FY2023 is lower than FY22 levels but could pick up, given strong upcoming opportunities in the TBCB segment.

■ **Valuation – Maintain Buy on Power Grid with an unchanged PT of Rs. 265**

Power Grid has a robust project pipeline worth Rs. 47,600 crore and has capitalised ~Rs. 20,695 crore in FY22, which provides earnings visibility for 2-3 years. We thus expect a 10% CAGR in PAT over FY2022-FY2025E along with RoE of ~18-19% in FY25E. We maintain a Buy on Power Grid with an unchanged PT of Rs. 265, as valuation of 1.6x/1.4x FY24E/FY25E P/BV seems attractive considering decent growth outlook, healthy RoE and a dividend yield of ~6-7%.

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 1,73,790 circuit kilometers of EHV transmission lines. Power Grid has approximately 270 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. 47,600 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 19% and is trading at an attractive valuation. Further asset monetisation over FY24E-FY25E and lower capex could result in higher dividend payout in coming years.

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
G Ravisankar	Director – Finance
Abhay Choudhary	Director – Projects

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Capital Group Cos Inc	6.6
2	Life Insurance Corp of India	5.96
3	Capital Income Builder	2.6
4	Nippon Life India Asset Management	2.57
5	Vanguard Group Inc	2.43
6	Republic of Singapore	2.43
7	SBI Funds Management	2.21
8	FMR LLC	1.67
9	Blackrock Inc	1.48
10	ABRDN PLC	1.1

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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