Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

CESC Ltd

Steady Q4 earnings; valuation attractive

Power	Sharekhan code: CESC

Reco/View: Buy	↔	CMP: Rs. 70	Price Target: Rs. 85	↓

↑ 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 33.86

Updated Mar 08, 2023

High Risk

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

Source: Morningstar

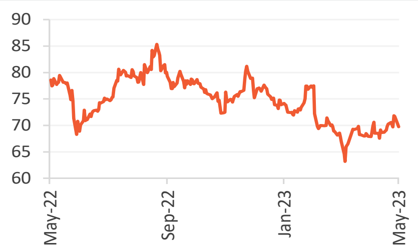
Company details

Market cap:	Rs. 8,714 cr
52-week high/low:	Rs. 87/62
NSE volume: (No of shares)	22.5 lakh
BSE code:	500084
NSE code:	CESC
Free float: (No of shares)	63.5 cr

Shareholding (%)

Promoters	52
FII	12
DII	22
Others	14

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	2.7	-3.4	-6.8	-11.3
Relative to Sensex	0.5	-7.6	-6.3	-25.9

Sharekhan Research, Bloomberg

Summary

- Q4FY23 consolidated PAT was up by 2% y-o-y to Rs. 433 crore, while FY23 consolidated PAT was flat y-o-y at Rs. 1,397 crore as modest growth in standalone earnings, higher earnings at Dhariwal gets offset by a decline in Haldia Energy's PAT and higher losses at Malegaon DF.
- Dhariwal performance improved with strong PAT growth of 79% y-o-y to Rs. 244 crore supported by higher Chandrapur PLF at 80.5% (versus 75.9% in FY22) and higher merchant power demand/prices. However, Rajasthan/Malegaon DF posted loss of Rs. 25 crore/Rs. 77 crore versus Rs. 30 crore/Rs. 57 crore in FY22.
- New tariff norms of the West Bengal Electricity Regulatory Commission is effective from April 1, 2023 and if tariff for Kolkata distribution business would remain steady than the impact of new norms will be minimal as lower incentives would get offset by under-recoveries.
- We maintain a Buy on CESC with a revised PT of Rs. 85 given an attractive valuation of 0.8x FY25E P/BV and dividend yield of ~5-6%. Turnaround of power distribution businesses could create value.

Q4FY23 consolidated revenues, operating profit and PAT stood at Rs. 3,543 crore (up 6.1% y-o-y), Rs. 954 crore (down 6.8% y-o-y) and Rs. 433 crore (up 2.1% y-o-y), respectively. For FY23, consolidated PAT at Rs. 1397 crore was flat y-o-y as steady standalone PAT of Rs. 830 crore (up 1.7% y-o-y), improved performance by Dhariwal (PAT up 79% y-o-y to Rs. 244 crore) was offset by a steep 22% y-o-y decline in Haldia Energy's PAT and wider net losses at Malegaon DF of Rs. 77 crore (versus Rs. 57 crore in FY22). Q4FY23 standalone earnings increased by 1.5% y-o-y to Rs. 263 crore reflecting a marginal improvement in power sales volume by 1.3% y-o-y to 2,155 million units and slightly better tariff of Rs. 9.2/unit (up 1.5% y-o-y). Subsidiaries performance - Dhariwal Infrastructure's PAT up by 179% y-o-y to Rs. 78 crore, Haldia Energy's PAT of Rs. 69 crore (up 15% y-o-y), Crescent Power PAT of Rs. 12 crore, surging 200% y-o-y. Rajasthan DF posted PAT of Rs. 4 crore versus loss of Rs. 11 crore in Q4FY23 and net loss in Malegaon DF reduced to Rs. 10 crore (versus Rs. 56 crore in Q4FY22).

Key positives

- Dhariwal Infrastructure PAT grew strongly by 179%/78% y-o-y to Rs. 78 crore/Rs. 244 crore in Q4FY23/FY23.
- Steady standalone earnings of Rs. 263 crore in Q4FY23.

Key negatives

- Haldia Energy PAT declined by 22% y-o-y in FY23.
- Malegaon DF's losses increased to Rs. 77 crore in FY23.

Revision in estimates: We have lowered our FY24/FY25 earnings estimate to factor higher interest cost and FY23 P&L and balance sheet numbers.

Our Call

Valuation - Maintain Buy with a revised SoTP-based PT of Rs. 85: 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 utilisation at Dhariwal Infrastructure and potential turnaround of Rajasthan/Malegaon DF over FY24-25. Valuation is attractive at 0.8x its FY2025E P/BV, and the stock offers a healthy dividend yield of ~5-6%. Hence, we maintain a Buy on CESC with a revised SoTP-based PT of Rs. 85 (the cut in PT reflects lower valuation for standalone business given lack of growth catalyst in the near term).

Key Risks

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

Valuation (Standalone) Rs cr

Particulars	FY22	FY23	FY24E	FY25E
Revenue	7,294	7,973	9,015	9,557
OPM (%)	15.3	14.8	18.0	18.5
PAT	816	830	872	983
% y-o-y growth	0.2	1.7	5.1	12.7
EPS (Rs.)	6.2	6.3	6.6	7.4
P/E (x)	11.4	11.2	10.7	9.4
P/B (x)	0.9	0.9	0.9	0.8
EV/EBITDA (x)	14.7	14.3	8.6	7.5
RoCE (%)	6.7	6.9	7.2	7.8
RoE (%)	8.2	8.3	8.5	9.0

Source: Company; Sharekhan estimates

Steady Q4 standalone earnings supported by regulated RoE

Q4FY23 consolidated revenues, operating profit and PAT stood at Rs. 3,543 crore (up 6.1% y-o-y), Rs. 954 crore (down 6.8% y-o-y) and Rs. 433 crore (up 2.1% y-o-y), respectively. For FY23, consolidated PAT at Rs. 1397 crore was flat y-o-y as steady standalone PAT of Rs. 830 crore (up 1.7% y-o-y), improved performance by Dhariwal (PAT up 79% y-o-y to Rs. 244 crore) was offset by a steep 22% y-o-y decline in Haldia Energy's PAT and wider net losses at Malegaon DF of Rs. 77 crore (versus Rs. 57 crore in FY22). Q4FY23 standalone earnings increased by 1.5% y-o-y to Rs. 263 crore reflecting a marginal improvement in power sales volume by 1.3% y-o-y to 2,155 million units and slightly better tariff of Rs. 9.2/unit (up 1.5% y-o-y). Subsidiaries performance - Dhariwal Infrastructure's PAT up by 179% y-o-y to Rs. 78 crore, Haldia Energy's PAT of Rs. 69 crore (up 15% y-o-y), Crescent Power PAT of Rs. 12 crore, surging 200% y-o-y. Rajasthan DF posted PAT of Rs. 4 crore versus loss of Rs. 11 crore in Q4FY23 and net loss in Malegaon DF reduced to Rs. 10 crore (versus Rs. 56 crore in Q4FY22).

Results (Standalone) Rs cr

Particulars	Q4FY23	Q4FY22	YoY(%)	Q3FY23	QoQ(%)
Revenue	**1,988**	**1,935**	**2.7**	**1,939**	**2.5**
Total expenditure	1,417	1,434	(1.2)	1,483	(4.5)
Operating profit	**571**	**501**	**14.0**	**456**	**25.2**
Other Income	56	81	(30.9)	56	0.0
Depreciation	122	120	1.7	119	2.5
Finance Cost	166	130	27.7	156	6.4
PBT	339	332	2.1	237	43.0
Tax	76	73	4.1	51	49.0
Reported PAT	263	259	1.5	186	41.4
EPS (Rs.)	19.8	19.5	1.5	14.0	41.4
Margin (%)			**bps**		**(bps)**
OPM (%)	28.7	25.9	283	23.5	521
NPMin (%)	15.9	16.1	-20	10.9	500
Tax Rate (%)	22.4	22.0	43	21.5	90

Source: Company, Sharekhan Research

Financial performance of key subsidiaries Rs cr

Particulars	Revenue		PAT	
	Q4FY23	Q4FY22	Q4FY23	Q4FY22
Haldia Energy	425	481	69	60
Dhariwal Infrastructure	474	534	78	28
Crescent Power	54	31	12	4
Noida Power	495	555	31	71
Kota/Bharatpur/Bikaner	342	344	4	-11
Malegaon	161	128	-10	-56

Source: Company, Sharekhan Research

Result (Consolidated) **Rs cr**

Particulars	Q4FY23	Q4FY22	y-o-y (%)	Q3FY23	q-o-q (%)
Revenue	**3,543**	**3,339**	**6.1%**	**3,460**	**2.4%**
Total Expenditure	2,589	2,315	11.8%	2,633	-1.7%
Operating profit	**954**	**1024**	**-6.8%**	**827**	**15.4%**
Other income	106	81	30.9%	95	11.6%
Depreciation	221	223	-0.9%	219	0.9%
Interest	289	298	-3.0%	289	0.0%
PBT	**550**	**584**	**-5.8%**	**414**	**32.9%**
Tax	105	139	-24.5%	78	34.6%
PAT	**445**	**445**	**0.0%**	**336**	**32.4%**
Minority interest	12	21	-42.9%	17	-29.4%
PAT post MI	433	424	2.1%	319	35.7%
EPS	3.3	3.2	2.1%	2.4	35.7%
Margin (%)			**bps**		**bps**
OPM	26.9	30.7	-374	23.9	302
NPM	12.2	12.7	-48	9.2	300
Tax rate	19.1	23.8	-471	18.8	25

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 (i.e. fixed RoE on power-generation assets). Thus, the regulated tariff model provides strong earnings visibility for power-generation companies such as CESC. Better power demand (except for April-May 2021, given the lockdown, yet the situation is better than 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 the timely receipt of dues from customers.

Company outlook - Steady performance by standalone biz, the turnaround of subsidiaries to improve consolidated earnings

Recovery in earnings from standalone operations given strong power demand, lower losses at distribution franchisees led by lower T&D losses, and higher utilisation at Dhariwal Infrastructure and potential turnaround of Rajasthan/Malegaon DF are expected to improve the consolidated earnings of CESC over FY2024E-FY2025E.

Valuation - Maintain Buy with a revised SoTP-based PT of Rs. 85

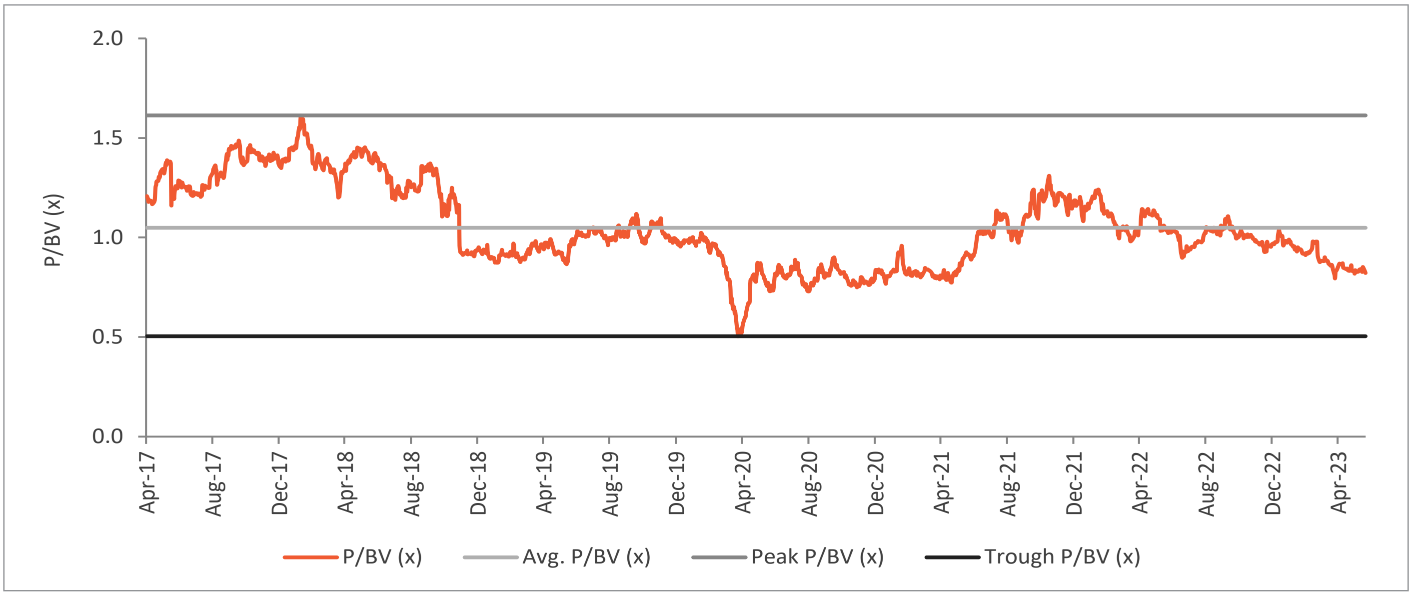
CESC is a play on investment and turnaround of the power distribution business, while earnings are expected to gradually improve with a further rise in utilisation at Dhariwal Infrastructure and potential turnaround of Rajasthan/Malegaon DF over FY24-25. Valuation is attractive at 0.8x its FY2025E P/BV, and the stock offers a healthy dividend yield of ~5-6%. Hence, we maintain a Buy on CESC with a revised SoTP-based PT of Rs. 85 (the cut in PT reflects lower valuation for standalone business given lack of growth catalyst in the near term).

SoTP-based PT of Rs. 85

Particulars	Value (Rs. / share)	Methodology
Standalone business	52	7x FY24E EPS
Haldia	12	1.4x regulated equity of ~Rs. 1150 crore
Dhariwal	15	2x regulated equity of ~Rs. 1000 crore
Crescent Power	1	6.5x FY23 PAT for 67.8% stake
Noida	3	2x regulated equity of ~Rs. 400 crore for 72.73% stake
DF	2	0.6x Investments
Price target	**85**	

Source: 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 electricity distributor 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 franchisees 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 contributions 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 appealing.

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

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	SBI Funds Management Ltd	5.44
2	HDFC Asset Management Co Ltd	5.15
3	Life Insurance Corp of India	3.21
4	ICICI Prudential Asset Management	2.41
5	UTI Asset Management Co Ltd	2.41
6	Massachusetts Financial Services C	2.34
7	ICICI PRUDENTIAL INDIA OPP	2.25
8	Sprott Resource Lending Corp	2.19
9	Vanguard Group Inc/The	1.85
10	Aditya Birla Sun Life Asset Manage	0.98

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

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