Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

CESC Ltd

Strong Q1; turnaround of Rajasthan DF key positive

Power	Sharekhan code: CESC		
Reco/View: Buy ↔	CMP: Rs. 79	Price Target: Rs. 93 ↑	

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- Q1FY24 consolidated PAT grew strongly by 21% y-o-y to Rs. 347 crore led by robust PAT growth from standalone business and strong earnings contribution from subsidiaries.
- Standalone PAT grew by 23% y-o-y led by healthy power sales volume, lower T&D loss and better tariff. Rajasthan DF posted PAT growth of 2.8x y-o-y as all three circles recorded a positive bottom line. Dhariwal/Crescent Power/Noida Power posted 11%/400%/59% y-o-y increase in PAT while Haldia PAT decline by 6% y-o-y and Malegaon DF loss increased to Rs. 33 crore.
- We view the turnaround of Rajasthan DF as a key positive and potential turnaround of Malegaon DF along with sustained strong performance from Dhariwal and standalone operations would improve consolidated earnings over the coming years.
- We maintain our positive stance on power sector and retain Buy on CESC with a revised PT of Rs. 93. Valuation of 0.9x FY25E P/BV is attractive, and stock offers healthy dividend yield of ~5-6%. Turnaround of power distribution businesses could create value.

Q1FY24 consolidated revenues, operating profit and PAT grew strongly by 8%/24%/21% y-o-y to Rs. 4,574 crore/Rs. 988 crore/Rs. 347 crore led by strong earnings from standalone and robust growth at subsidiaries (ex Haldia Energy). Standalone PAT grew by 23% y-o-y to Rs. 170 crore led by healthy power sales volume growth of 7.5% y-o-y to 3274 mn units, lower T&D loss of 7.46% (versus 8.12% in Q1FY23) and higher derived tariff of Rs. 8.4/unit (up 7.9% y-o-y). Rajasthan distribution franchisee posted robust performance with 2.8x y-o-y rise in PAT to Rs. 17 crore as all three circles (Kota/Bharatpur/Bikaner) posted positive earnings supported by lower T&D loss. Dhariwal Infrastructure also continued its resilient show which is reflected in 11% y-o-y growth in PAT to Rs. 79 crore as Chandarpur TPP PLF remained robust at 90.4% (versus 86.3% in Q1FY23) supported by rise in power demand and 210 MW medium term PPA with Central Railway for a period of 3 years. Crescent Power/Noida Power also posted 400%/59% y-o-y increase in PAT to Rs. 20 crore/Rs. 54 crore. However, Haldia Energy's PAT declined by 6% y-o-y to Rs. 62 crore and net loss in Malegaon DF increased to Rs. 33 crore (versus Rs. 19 crore in Q1FY23).

Key positives

- Strong standalone PAT growth of 23% y-o-y.
- Rajasthan DF posted robust financials with a 2.8x y-o-y increase in earnings.

Key negatives

- Malegaon DF's losses increased to Rs. 33 crore in Q1FY24.

Revision in estimates – We maintain our FY24/FY25 earnings estimates.

Our Call

Valuation – Maintain Buy with a revised SoTP-based PT of Rs. 93: CESC is a play on investment and turnaround of the power distribution business and consolidated earnings are expected to gradually improve over the coming years. Valuation is attractive at 0.9x 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. 93 (increase in PT reflects rollover of standalone valuation to FY25 earnings estimates).

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	8,087	8,684	9,120
OPM (%)	15.3	17.0	17.5	18.5
PAT	816	811	959	1,082
% y-o-y growth	0.2	(0.6)	18.3	12.8
EPS (Rs.)	6.2	6.1	7.2	8.2
P/E (x)	12.9	13.0	11.0	9.7
P/B (x)	1.1	1.0	0.9	0.9
EV/EBITDA (x)	15.8	11.4	9.8	8.4
RoCE (%)	6.7	6.7	7.8	8.3
RoE (%)	8.2	7.9	8.9	9.4

Source: Company; Sharekhan estimates

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 Jun 08, 2023	
High Risk	

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

Source: Morningstar

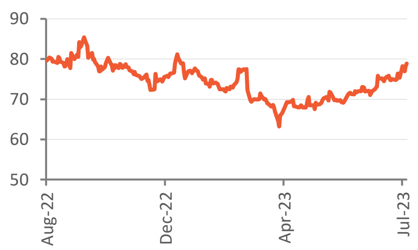
Company details

Market cap:	Rs. 10,455 cr
52-week high/low:	Rs. 87 / 62
NSE volume: (No of shares)	26.8 lakh
BSE code:	500084
NSE code:	CESC
Free float: (No of shares)	63.5 cr

Shareholding (%)

Promoters	52
FII	12
DII	21
Others	15

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	7.9	14.9	8.8	-0.9
Relative to Sensex	7.5	7.3	0.8	-13.4

Sharekhan Research, Bloomberg

Strong Q1 consolidated performance; Rajasthan turnaround a key positive

Q1FY24 consolidated revenues, operating profit and PAT grew strongly by 8%/24%/21% y-o-y to Rs. 4574 crore/Rs. 988 crore/Rs. 347 crore led strong earnings from standalone and robust growth at subsidiaries (ex Haldia Energy). Standalone PAT grew by 23% y-o-y to Rs. 170 crore led by healthy power sales volume growth of 7.5% y-o-y to 3274 mn units, lower T&D loss of 7.46% (versus 8.12% in Q1FY23) and higher derived tariff of Rs. 8.4/unit (up 7.9% y-o-y). Rajasthan distribution franchisee posted robust performance with 2.8x y-o-y rise in PAT to Rs. 17 crore as all three circles (Kota/Bharatpur/Bikaner) posted positive earnings supported by lower T&D loss. Dhariwal Infrastructure also continued its resilient show which is reflected in 11% y-o-y growth in PAT to Rs. 79 crore as Chandarpur TPP PLF remained robust at 90.4% (versus 86.3% in Q1FY23) supported by rise in power demand and 210 MW medium term PPA with Central Railway for a period of 3 years. Crescent Power/Noida Power also posted 400%/59% y-o-y increase in PAT to Rs. 20 crore/Rs. 54 crore. However, Haldia Energy's PAT declined by 6% y-o-y to Rs. 62 crore and net loss in Malegaon DF increased to Rs. 33 crore (versus Rs. 19 crore in Q1FY23).

Results (Standalone) Rs cr

Particulars	Q1FY24	Q1FY23	Y-o-Y %	Q4FY23	Q-o-Q %
Revenue	**2,735**	**2,360**	**15.9**	**1,988**	**37.6**
Total expenditure	2,181	1,953	11.7	1,417	53.9
Operating profit	**554**	**407**	**36.1**	**571**	**(3.0)**
Other Income	21	20	5.0	56	(62.5)
Depreciation	179	120	49.2	122	46.7
Finance Cost	181	134	35.1	166	9.0
PBT	215	173	24.3	339	(36.6)
Tax	45	35	28.6	76	(40.8)
Reported PAT	**170**	**138**	**23.2**	**263**	**(35.4)**
EPS (Rs.)	12.8	10.4	23.2	19.8	(35.4)
Margin (%)			**bps**		**bps**
OPM	20.3	17.2	301	28.7	-847
NPM	6.7	5.9	85	15.9	-916
Tax Rate	20.9	20.2	70	22.4	-149

Source: Company; Sharekhan Research

Financial performance of key subsidiaries Rs cr

Particulars	Revenue		PAT	
	Q1FY24	Q1FY23	Q1FY24	Q1FY23
Haldia Energy	539	477	62	66
Dhariwal Infrastructure	516	484	79	71
Crescent Power	51	30	20	4
Noida Power	636	681	54	34
Kota/Bharatpur/Bikaner	570	599	17	6
Malegaon	154	135	-33	-19

Source: Company; Sharekhan Research

Results (Consolidated) Rs cr

Particulars	Q1FY24	Q1FY23	Y-o-Y %	Q4FY23	Q-o-Q %
Revenue	**4,574**	**4,249**	**7.6%**	**3,543**	**29.1%**
Total expenditure	3,586	3,452	3.9%	2,589	38.5%
Operating profit	**988**	**797**	**24.0%**	**954**	**3.6%**
Other income	59	44	34.1%	106	-44.3%
Depreciation	300	217	38.2%	221	35.7%
Interest	308	265	16.2%	289	6.6%
PBT	**439**	**359**	**22.3%**	**550**	**-20.2%**
Tax	71	62	14.5%	105	-32.4%
PAT	**368**	**297**	**23.9%**	**445**	**-17.3%**
Minority interest	21	11	90.9%	12	75.0%
PAT post MI	**347**	**286**	**21.3%**	**433**	**-19.9%**
EPS	2.6	2.2	21.3%	3.3	-19.9%
Margin (%)			**bps**		**bps**
OPM	21.6	18.8	284	26.9	-533
NPM	7.6	6.7	86	12.2	-463
Tax rate	16.2	17.3	-110	19.1	-292

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. 93

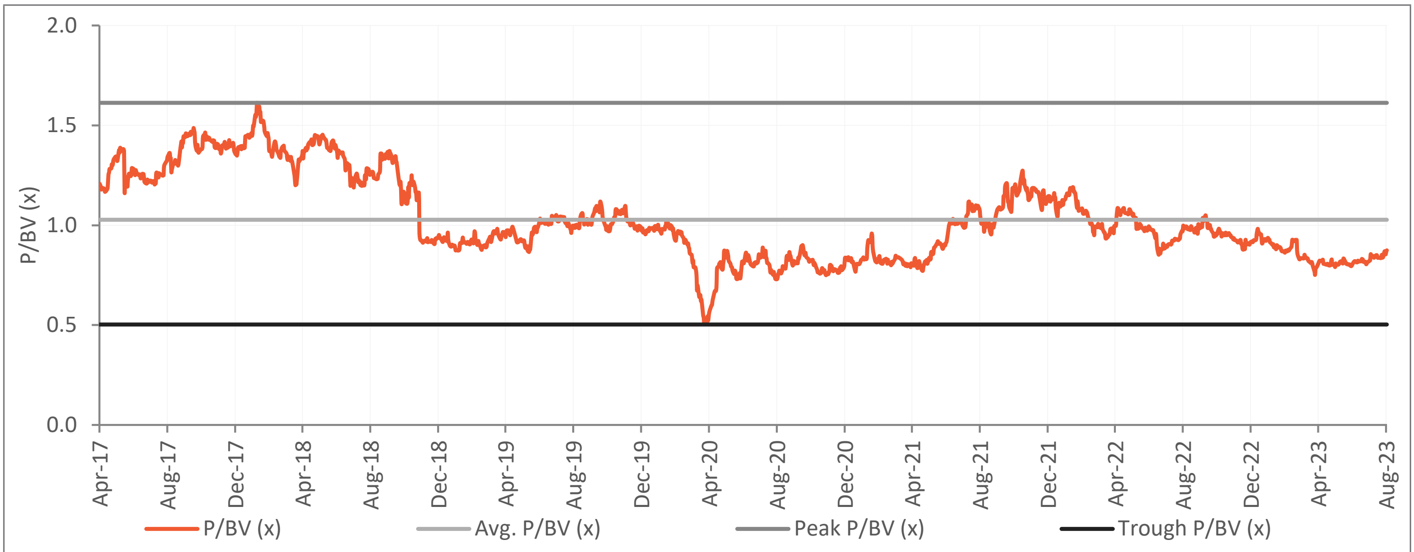
CESC is a play on investment and turnaround of the power distribution business and consolidated earnings are expected to gradually improve over the coming years. Valuation is attractive at 0.9x its FY2025E P/BV, and the stock offers a healthy dividend yield of ~5-6%. Hence, we maintain a Buy on CESC with a revised SoTP-based PT of Rs. 93 (increase in PT reflects rollover of standalone valuation to FY25 earnings estimate).

SoTP-based PT of Rs. 93

Particulars	Value (Rs. /share)	Methodology
Standalone business	57	7x FY25E 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	4	2x regulated equity of ~Rs. 400 crore for 72.73% stake
DF	4	1x Investments
Price target	**93**	

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 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 Website

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	2.62
5	Massachusetts Financial Services C	2.34
6	ICICI PRUDENTIAL INDIA OPP	2.25
7	Sprott Resource Lending Corp	2.19
8	UTI Asset Management Co Ltd	2.19
9	Vanguard Group Inc/The	1.59
10	BlackRock Inc	0.97

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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