Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

CESC Ltd

Subdued Q3; Rajasthan DF break-even key positive

Power	Sharekhan code: CESC
Reco/View: Buy ↔	CMP: **Rs. 138**
	Price Target: **Rs. 162** ↑

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- Consolidated PAT fell 12% y-o-y to Rs. 281 crore due to earnings decline from key subsidiaries/ standalone business and higher loss at Malegaon DF.
- Haldia/ Dhariwal Infra's PAT declined by 31%/18% y-o-y due to lower PLFs while Noida Power PAT declined by 13% y-o-y. Rajasthan DF turned break-even at PAT level. PLF at Haldia/ Dhariwal was hit by annual maintenance shutdown and is likely to recovery strongly in Q4FY24.
- Aggressive RE strategy with a plan of 3 GW (capex of ~Rs. 12,000-13,000 crore) in 4-5 years offers a good value proposition given lower RE cost, strong growth prospects, and likely improvement in ESG rating. CESC's subsidiary has been selected as successful bidder to set-up of 10,500 TPA green hydrogen production facility in India.
- We retain Buy on CESC with a revised PT of Rs. 162. Valuation of 1.5x FY26E P/BV is attractive, and stock offers a healthy dividend yield of ~3-4%. Turnaround of power distribution businesses could create value.

Q3FY24 consolidated revenues/operating profit grew by 10%/9.6% y-o-y to Rs. 3804 crore/Rs. 906 crore while its PAT declined by 12% y-o-y to Rs. 281 crore. Earnings fall was on the account of PAT decline from key subsidiaries (Haldia/Dhariwal were impacted by a pre-poned annual maintenance shutdown, which dragged down plant load factor, while the standalone business' PAT fell 8.6% y-o-y to Rs. 170 crore despite 8% y-o-y rise in power sales volume. Subdued performance of subsidiaries – 1) Haldia Energy's PAT declined by 31% y-o-y to Rs. 48 crore due to a lower PLF of 72.8% versus 81.3% in Q3FY23, 2) Dhariwal Infrastructure posted an 18% y-o-y PAT decline to Rs. 42 crore reflecting 20% y-o-y fell in volumes at 783 million units, 3) Noida Power PAT was also down by 13% y-o-y to Rs. 48 crore, but its power sales volume was up by 13% y-o-y to 669 million units, 4) A higher loss at the Malegaon distribution franchisee (DF) at Rs. 27 crore (versus Rs. 19 crore in Q3FY23). Rajasthan DF turned break-even at PAT level with the Bharatpur/Bikaner DF remaining PAT positive, while the Kota DF witnessed turnaround and became cash positive in Q3FY24.

Key positives

- The Rajasthan DF turned break-even at PAT level.
- It declared an interim dividend of Rs. 4.5/share, which implies yield of 3% on CMP.

Key negatives

- Haldia/Dhariwal/Noida Power PAT declined by 31%/18%/13% y-o-y.

Revision in estimates – We have lowered our FY24-26 earnings estimate to factor 9MFY24 performance.

Our Call

Valuation - Maintain Buy with a revised SoTP-based PT of Rs. 162: CESC is a play on the renewable energy (RE) capex revival and turnaround of the power distribution businesses and earnings are expected to gradually improve in the coming years. Valuation is attractive at 1.5x its FY2026E P/BV, and the stock offers a healthy dividend yield of 3-4%. Hence, we maintain a Buy on CESC with a revised SoTP-based PT of Rs. 162.

Key Risks

Sustained losses in distribution franchisees for an extended period and lower utilisation at the Chandrapur plant. Delay in implementation and execution of renewable energy projects.

Valuation (Standalone) Rs cr

Particulars	FY22	FY23	FY24E	FY25E	FY26E
Revenue	7,294	7,973	8,860	9,428	9,776
OPM (%)	15.3	14.8	17.5	18.5	18.5
PAT	816	830	850	993	1,025
% y-o-y growth	0.2	1.7	2.5	16.7	3.2
EPS (Rs.)	6.2	6.3	6.4	7.5	7.7
P/E (x)	22.5	22.2	21.6	18.5	17.9
P/B (x)	1.8	1.8	1.7	1.6	1.5
EV/EBITDA (x)	22.9	22.0	16.2	14.2	13.4
RoCE (%)	6.7	6.9	7.4	8.0	7.9
RoE (%)	8.2	8.3	8.3	9.1	8.8

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		↔	

Company details

Market cap:	Rs. 18,300 cr
52-week high/low:	Rs. 146/62
NSE volume: (No of shares)	87.6 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	13.7	53.2	84.7	86.8
Relative to Sensex	13.7	44.4	78.3	69.0

Sharekhan Research, Bloomberg

Subdued performance; RJ DF turned break-even at PAT level

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Subdued performance of subsidiaries: 1) Haldia Energy's PAT declined by 31% y-o-y to Rs. 48 crore due to a lower PLF of 72.8% versus 81.3% in Q3FY23, 2) Dhariwal Infrastructure posted an 18% y-o-y PAT decline to Rs. 42 crore reflecting 20% y-o-y fell in volumes at 783 million units, 3) Noida Power PAT was also down by 13% y-o-y to Rs. 48 crore, but its power sales volume was up by 13% y-o-y to 669 million units, 4) A higher loss at the Malegaon distribution franchisee (DF) at Rs. 27 crore (versus Rs. 19 crore in Q3FY23). Rajasthan DF turned break-even at PAT level with the Bharatpur/ Bikaner DF remaining PAT positive, while the Kota DF witnessed turnaround and became cash positive in Q3FY24.

Results (Standalone) Rs cr

Particulars	Q3FY24	Q3FY23	YoY (%)	Q2FY24	QoQ (%)
Revenue	**2,309**	**1,939**	**19.1**	**2,737**	**(15.6)**
Total expenditure	1,757	1,483	18.5	2,125	(17.3)
Operating profit	**552**	**456**	**21.1**	**612**	**(9.8)**
Other Income	22	56	(60.7)	47	(53.2)
Depreciation	180	119	51.3	178	1.1
Finance Cost	177	156	13.5	176	0.6
PBT	217	237	(8.4)	305	(28.9)
Tax	47	51	(7.8)	75	(37.3)
Reported PAT	**170**	**186**	**(8.6)**	**230**	**(26.1)**
EPS (Rs.)	12.8	14.0	(8.6)	17.3	(26.1)
Margin (%)			**bps**		**bps**
OPM (%)	23.9	23.5	39	22.4	155
NPM (%)	9.3	10.9	-154	9.4	-5
Tax Rate (%)	21.7	21.5	14	24.6	-293

Source: Company; Sharekhan Research

Financial performance of key subsidiaries Rs cr

Particulars	Revenue		PAT	
	Q3FY24	Q3FY23	Q3FY24	Q3FY23
Haldia Energy	428	509	48	70
Dhariwal Infrastructure	370	511	42	51
Crescent Power	53	54	21	7
Noida Power	557	475	48	55
Kota/Bharatpur/Bikaner	397	383	0.1	-11
Malegaon	170	164	-27	-19

Source: Company; Sharekhan Research

Results (Consolidated) Rs cr

Particulars	Q3FY24	Q3FY23	y-o-y (%)	Q2FY24	q-o-q (%)
Revenue	**3,804**	**3,460**	**9.9%**	**4,713**	**-19.3%**
Expenses	2,898	2,633	10.1%	3,706	-21.8%
Operating profit	**906**	**827**	**9.6%**	**1007**	**-10.0%**
Other income	57	95	-40.0%	62	-8.1%
Depreciation	303	219	38.4%	303	0.0%
Interest	296	289	2.4%	305	-3.0%
PBT	364	414	-12.1%	461	-21.0%
Tax	**63**	**78**	**-19.2%**	**98**	**-35.7%**
PAT	301	336	-10.4%	363	-17.1%
Minority interest	**20**	**17**	**17.6%**	**15**	**33.3%**
PAT post MI	281	319	-11.9%	348	-19.3%
EPS	**2.1**	**2.4**	**-11.9%**	**2.6**	**-19.3%**
Margin (%)			**bps**		**bps**
OPM	23.8	23.9	-8	21.4	245
NPM	7.4	9.2	-183	7.4	0
Tax rate	17.3	18.8	-153	21.3	-395

Source: Company; Sharekhan Research

Generation business – operational performance

	Capacity (MW)	Q3 FY24		Q3 FY23		9M FY24		9M FY23	
		Sent Out Units (MU)	PLF %	Sent Out Units (MU)	PLF %	Sent Out Units (MU)	PLF %	Sent Out Units (MU)	PLF %
Budge Budge Generating Station	750	1319	86.2%	1073	70.4%	4150	90.8%	3661	80.4%
Southern Generating Station	135	98	36%	34	13%	535	66.2%	523	64.2%
Haldia Energy	600	893	72.8%	996	81.3%	3189	87.2%	3076	84.5%
Dhariwal Infrastructure	600	783	63.7%	981	80%	3000	81.6%	2944	80.3%
Crescent Power	40	78	99%	79	101%	219	93.5%	217	93%
Solar (TN)	18	5	12.7%	5.7	14.3%	18.6	15.7%	19	16%

Source: Company

Distribution business – operational performance

	Q3 FY24			Q3 FY23			9M FY24			9M FY23		
	Sales (MU)	T&D Loss %	Revenue (Rs. Crs)	Sales (MU)	T&D Loss %	Revenue (Rs. Crs)	Sales (MU)	T&D Loss %	Revenue (Rs. Crs)	Sales (MU)	T&D Loss %	Revenue (Rs. Crs)
CESC Kolkata	2383	-	1841	2201	-	1764	8817	8.1%*	6882	8208	8.1%*	6442
Noida Power	669	6.56%	557	591	6.87%	475	2423	8.36%	1905	2252	8.40%	1830
Kota DF	259	15.6%	203	309	14.3%	215	1093	14.7%	832	1134	15.5%	832
Bharatpur DF	59	8.8%	46	54	9.9%	40	236	10.3%	181	227	11.8%	176
Bikaner DF	157	12.7%	148	150	12.7%	128	619	12.9%	544	599	14.1%	504
Malegaon DF	218	36.7%	170	206	38.3%	164	617	39.4%	484	577	39.4%	447

Source: Company

Outlook and Valuation

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

The Central Electricity Regulatory Commission (CERC) regulates India's power sector 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 like CESC. Better power demand (peak power demand in India likely to cross 400 GW by 2030) would drive up PLFs for power-generation companies and better PLF incentive income.

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

A recovery in earnings from standalone operations given strong power demand, lower losses at distribution franchisees (DFs) led by lower T&D losses, and higher utilisation at Dhariwal Infrastructure and potential turnaround of Rajasthan/ Malegaon DF are expected to improve CESC's consolidated earnings over FY2024E-FY2026E.

■ Valuation – Maintain Buy with a revised SoTP-based PT of Rs. 162

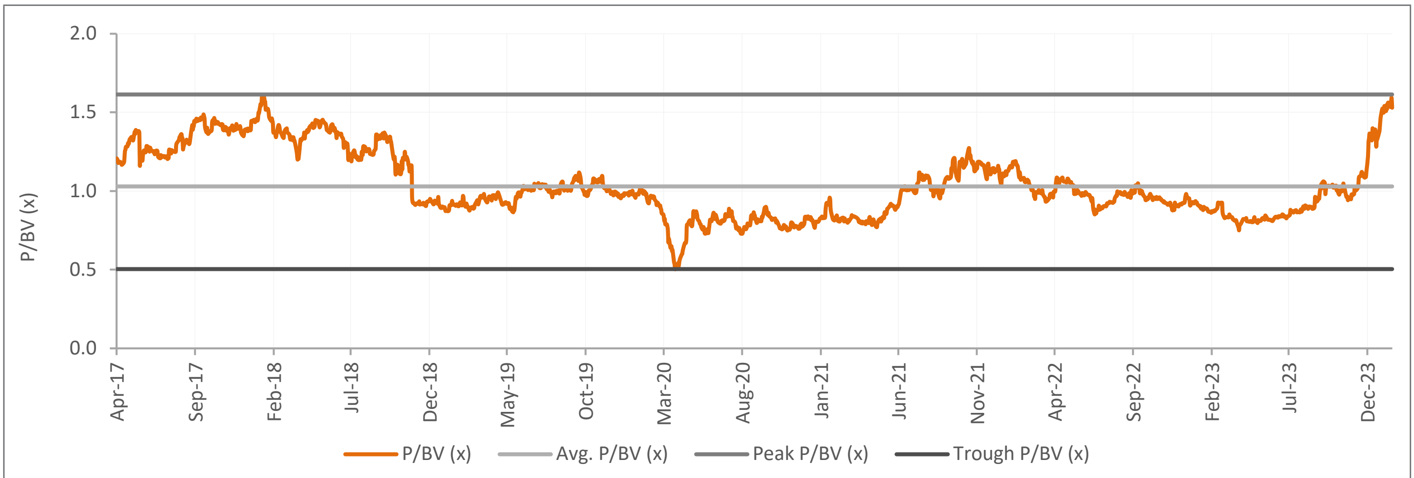
CESC is a play on the renewable energy (RE) capex revival and turnaround of the power distribution businesses and earnings are expected to gradually improve in the coming years. Valuation is attractive at 1.5x its FY2026E P/BV, and the stock offers a healthy dividend yield of 3-4%. Hence, we maintain a Buy on CESC with a revised SoTP-based PT of Rs. 162.

SoTP-based PT of Rs. 162

Particulars	Value (Rs. /share)	Methodology
Standalone business	77	10x FY26E EPS
Haldia	22	2.5x regulated equity of ~Rs. 1150 crore
Dhariwal	19	2.5x regulated equity of ~Rs. 1000 crore
Crescent Power	1	6.5x FY23 PAT for 67.8% stake
Noida	19	10x FY23 EBITDA for 72.73% stake
DF	6	2x Investments
Cash & Cash equivalent	18	
Price target	**162**	

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 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 a 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 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. Sustained strong performance at Dhariwal Infrastructure, likely turnaround of Rajasthan DF and planned investment in RE makes 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	5.8
2	HDFC Asset Management Co Ltd	4.1
3	Life Insurance Corp of India	3.4
4	ICICI Prudential Asset Management	2.8
5	Massachusetts Financial Services C	2.3
6	ICICI PRUDENTIAL INDIA OPP	2.3
7	Sprott Resource Lending Corp	2.2
8	UTI Asset Management Co Ltd	1.7
9	Vanguard Group Inc/The	1.9
10	BlackRock Inc	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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