

BUY

TP: Rs 108 | ▲ 44%

CESC

| Power

| 15 February 2023

Stable performance; DF circles disappoint

- **Stable Q3 with 4% YoY revenue growth to Rs 19bn and flattish net profit at Rs 1.9bn**
- **Distribution franchisee (DF) circles in Rajasthan and Malegaon continue to disappoint as losses widened**
- **Stock at attractive valuations of 0.8x FY25E P/BV with dividend yield at 6%; retain BUY with an unchanged TP of Rs 108**

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Flat performance: CESC's standalone Q3FY23 net revenue (including regulated income) grew 4% YoY to Rs 19bn, slightly above our estimate. Standalone EBITDA including regulatory income increased 10% YoY to Rs 4.5bn. The company posted regulatory income of only Rs 2.3bn during the quarter as against Rs 2bn in the year-ago period. Standalone net income was flat YoY at Rs 1.9bn (Rs 1.7 bn est.). On a consolidated basis, revenue grew 11% YoY to Rs 31bn, EBITDA (incl. regulatory income) was flat at Rs 8.3bn and net income was also flat at Rs 3.4bn.

Demand stable due to early winter in Kolkata circle: Power sales during Q3FY23 stood at 2,201MU, an increase of only 2.6% YoY.

Losses in DF circles widen: CESC's Rajasthan distribution franchisees (DF) continued to post losses in 9MFY23 at Rs 290mn vs. Rs 190mn in 9MFY22. Malegaon DF losses also widened to Rs 670mn from Rs 410mn.

Dhariwal performance has stabilised: PLF (plant load factor) for subsidiary Dhariwal Infrastructure stood at 80% vs. 63.4% in Q3FY22 on the back of a three-year power purchase agreement (PPA) for Unit-1. Net profit for 9MFY23 came in higher at Rs 1.7bn compared to Rs 1.1bn in the corresponding year-ago period.

Retain BUY: CESC's generation and distribution assets in Kolkata remain a cash cow for the company, producing strong cash flows and high ROE. A steady performance at Dhariwal due to the new PPA should continue to broaden earnings visibility and cash generation. This apart, CESC's dividend yield is high at 6%, and we find current valuations attractive at 0.8x FY25E P/BV. We thus maintain BUY with an unchanged SOTP-based TP of Rs 108 for 44% upside potential. Turnaround in DF circles, however, remains a key monitorable.

Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	CESC IN/Rs 75
Market cap	US\$ 1.2bn
Free float	48%
3M ADV	US\$ 1.8mn
52wk high/low	Rs 88/Rs 68
Promoter/FPI/DII	52%/13%/35%

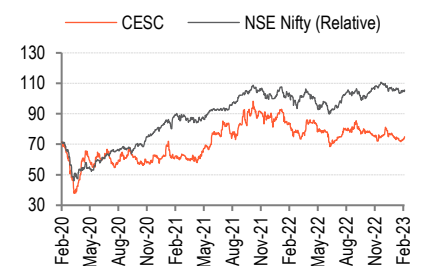
Source: NSE | Price as of 14 Feb 2023

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	1,32,810	1,42,934	1,45,859
EBITDA (Rs mn)	36,540	37,161	38,092
Adj. net profit (Rs mn)	14,026	15,829	16,783
Adj. EPS (Rs)	10.5	11.9	12.6
Consensus EPS (Rs)	10.5	11.6	12.1
Adj. ROAE (%)	13.5	14.3	14.2
Adj. P/E (x)	7.1	6.3	6.0
EV/EBITDA (x)	5.9	5.9	5.5
Adj. EPS growth (%)	2.1	12.9	5.9

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Fig 1 – Standalone quarterly performance

(Rs mn)	Q3FY23	Q3FY22	YoY (%)	Q2FY23	QoQ (%)	9MFY23	9MFY22	YoY (%)
Revenue	19,390	18,630	4.1	24,730	(21.6)	67,720	44,120	53.5
EBITDA	4,560	4,130	10.4	5,300	(14.0)	13,930	9,860	41.3
EBITDA margin (%)	23.5	22.2	135bps	21.4	209bps	20.6	22.3	(178bps)
Depreciation	1,190	1,170	1.7	1,190	0.0	3,580	2,380	50.4
Finance Cost	1,560	1,230	26.8	1,480	5.4	4,380	3,040	44.1
Other Income	560	580	(3.4)	480	16.7	1,240	1,040	19.2
PBT	2,370	2,310	2.6	3,110	(23.8)	7,210	5,480	31.6
Tax Expense	510	470	8.5	680	(25.0)	1,540	1,190	29.4
Reported PAT	1,860	1,840	1.1	2,430	(23.5)	5,670	4,290	32.2
PAT margin (%)	9.6	9.9	(28bps)	9.8	(23bps)	8.4	9.7	(135bps)
Adj. EPS (Rs)	1.4	1.4	1.1	1.8	(23.5)	4.3	3.2	32.2

Source: Company, BOBCAPS Research

Fig 2 – Q3FY23 Actual vs. Estimates

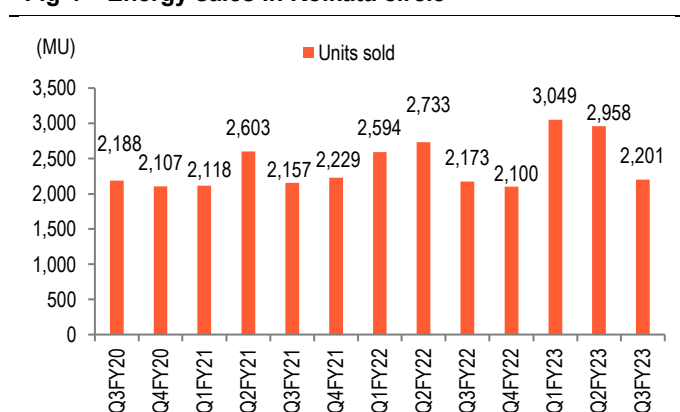
(Rs mn)	Actual	Estimate	Variance (%)	Consensus Estimate	Variance (%)
Revenue	19,390	18,573	4.4	18,221	6.4
EBITDA	4,560	4,230	7.8	3,988	14.3
EBITDA margin (%)	23.5	22.8	74bps	21.9	163bps
PAT	1,860	1,730	7.5	1810	2.8

Source: Company, BOBCAPS Research

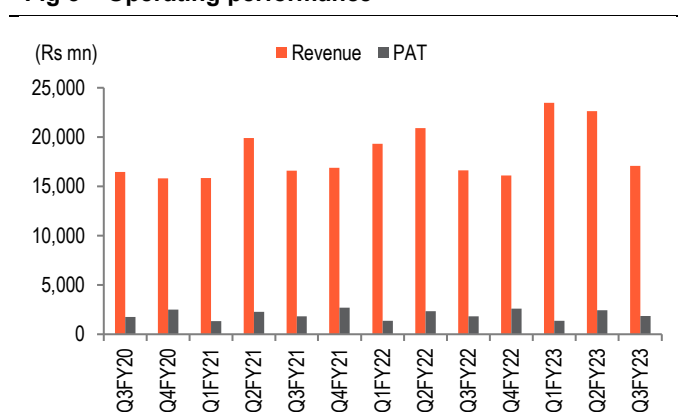
Fig 3 – Segmental performance

(Rs mn)	9MFY23		9MFY22	
	Revenue	PAT	Revenue	PAT
CESC (standalone)	67,720	5,670	44,120	4,290
Haldia Energy	15,620	1,920	17,700	2,730
Dhariwal Infrastructure	14,440	1,660	11,200	1,090
Crescent Power	1,230	210	940	110
Noida Power	18,300	1,300	15,000	790
Rajasthan DF	15,120	(290)	12,450	(190)
Malegaon	4,470	(670)	3,660	(410)

Source: Company, BOBCAPS Research

Fig 4 – Energy sales in Kolkata circle

Source: Company, BOBCAPS Research

Fig 5 – Operating performance

Source: Company, BOBCAPS Research

Valuation methodology

CESC's generation and distribution assets in Kolkata remain a cash cow for the company, with strong cash flows and high ROE. A steady performance at Dhariwal due to the new medium-term PPA should continue to broaden earnings visibility and cash generation. Further, the proposed tie-up of 250MW toward renewable purchase obligations (RPO) would boost the company's ESG score.

We believe the stock's performance will be largely tied to energy demand in the Kolkata circle and turnaround in DF circles (which is currently lagging expectations). Overall, we find the current valuation attractive at 0.8x FY25E P/BV, which is 27% below the five-year average, and note that dividend yield is as high as 6%. We maintain BUY with an unchanged SOTP-based TP of Rs 108 (44% upside), which implies an FY24E P/BV of 1.1x based on the stock's average valuation and improving ROE profile.

Fig 6 – SOTP valuation

Particulars	NPV (Rs mn)	Implied valuation (P/B)	Value (Rs m)	Value (Rs/sh)
DCF based				
Standalone Regulated Business	66,464	1.3	66,464	50
Haldia 600MW	34,208	1.0	34,208	26
Chandrapur 600MW	12,200	1.2	12,200	9
Distribution Franchisee	3,459	1.0	3,459	3
Book value based	Our assumption of Valuation Multiple	Rationale		
Noida distribution	1.2	Noida business ROE is ~30%	14,569	11
Crescent Power	0.4	Renewable business has not generated the expected return for the company	0	0
Cash + Investments + Bank Balance (FY22)	-	-	12,982	10
Equity Value per Share	-	-	-	108

Source: Company, BOBCAPS Research

Key risks

Key downside risks to our estimates:

- As the company is carrying a high level of regulated assets in its book, adverse regulatory orders/policies can negatively impact earnings.
- Delays in reducing transmission & distribution (T&D) losses in DF circles will delay earnings turnaround in this business.

Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
CESC	CESC IN	1.2	75	108	BUY
NTPC	NTPC IN	19.5	166	210	BUY
Power Grid Corp	PWGR IN	18.1	215	251	BUY
Tata Power	TPWR IN	7.8	203	271	BUY

Source: BOBCAPS Research, NSE | Price as of 14 Feb 2023

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Total revenue	1,20,630	1,32,810	1,42,934	1,45,859	1,50,589
EBITDA	36,100	36,540	37,161	38,092	41,298
Depreciation	(8,670)	(8,850)	(8,036)	(8,033)	(8,035)
EBIT	27,430	27,690	29,124	30,060	33,263
Net interest inc./(exp.)	2,350	2,760	2,887	2,898	2,915
Other inc./(exp.)	(12,260)	(11,290)	(12,660)	(12,603)	(12,656)
Exceptional items	(9)	(8)	(7)	(6)	(5)
EBT	17,511	19,152	19,344	20,349	23,516
Income taxes	(3,890)	(5,110)	(3,501)	(3,554)	(4,098)
Extraordinary items	(9)	(8)	(7)	(6)	(5)
Min. int./Inc. from assoc.	320	460	508	560	620
Reported net profit	13,612	14,034	15,836	16,789	19,414
Adjustments	(9)	(8)	(7)	(6)	(5)
Adjusted net profit	13,603	14,026	15,829	16,783	19,409

Balance Sheet

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Accounts payables	10,030	11,050	13,361	13,521	13,422
Other current liabilities	30,650	15,010	44,588	44,809	44,981
Provisions	5,680	5,600	3,805	3,814	3,835
Debt funds	1,24,650	1,49,610	1,38,493	1,36,858	1,34,890
Other liabilities	88,878	89,690	85,164	86,634	88,164
Equity capital	1,332	1,332	1,332	1,332	1,332
Reserves & surplus	97,400	1,02,638	1,09,345	1,17,003	1,27,284
Shareholders' fund	98,732	1,03,970	1,10,677	1,18,335	1,28,616
Total liab. and equities	3,58,620	3,74,930	3,96,088	4,03,971	4,13,907
Cash and cash eq.	18,580	32,500	35,956	39,249	44,199
Accounts receivables	23,150	20,950	25,699	26,553	27,114
Inventories	5,970	6,590	7,856	7,871	7,950
Other current assets	6,580	8,030	9,944	10,757	11,600
Investments	2,320	4,080	770	770	770
Net fixed assets	2,39,710	2,30,190	2,41,496	2,42,500	2,43,368
CWIP	1,340	1,030	1,483	1,483	1,148
Intangible assets	1,630	1,340	1,237	1,153	1,068
Deferred tax assets, net	0	0	0	0	0
Other assets	59,340	70,220	71,646	73,634	76,689
Total assets	3,58,620	3,74,930	3,96,088	4,03,971	4,13,907

Cash Flows

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Cash flow from operations	28,171	24,982	52,259	35,075	36,592
Capital expenditures	(6,750)	(4,650)	(19,693)	(8,952)	(8,484)
Change in investments	(5,580)	(1,300)	3,803	544	605
Other investing cash flows	(2,570)	200	(3,148)	(3,148)	(3,148)
Cash flow from investing	(14,900)	(5,750)	(19,038)	(11,556)	(11,028)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	210	11,010	(11,117)	(1,635)	(1,969)
Interest expenses	(11,780)	(11,090)	(12,660)	(12,603)	(12,656)
Dividends paid	(5,940)	(6,030)	(5,995)	(5,995)	(5,995)
Other financing cash flows	0	0	0	0	0
Cash flow from financing	(17,510)	(6,110)	(29,772)	(20,232)	(20,620)
Chg in cash & cash eq.	(4,239)	13,122	3,449	3,287	4,945
Closing cash & cash eq.	8,391	21,522	35,949	39,243	44,194

Per Share

Y/E 31 Mar (Rs)	FY21A	FY22A	FY23E	FY24E	FY25E
Reported EPS	10.2	10.5	11.9	12.6	14.6
Adjusted EPS	10.2	10.5	11.9	12.6	14.6
Dividend per share	4.5	4.5	4.5	4.5	4.5
Book value per share	74.1	78.0	83.1	88.8	96.5

Valuations Ratios

Y/E 31 Mar (x)	FY21A	FY22A	FY23E	FY24E	FY25E
EV/Sales	1.7	1.6	1.5	1.4	1.4
EV/EBITDA	5.8	5.9	5.9	5.5	5.2
Adjusted P/E	7.3	7.1	6.3	6.0	5.1
P/BV	1.0	1.0	0.9	0.8	0.8

DuPont Analysis

Y/E 31 Mar (%)	FY21A	FY22A	FY23E	FY24E	FY25E
Tax burden (Net profit/PBT)	77.7	73.3	81.9	82.5	82.6
Interest burden (PBT/EBIT)	63.9	69.2	66.4	67.7	70.7
EBIT margin (EBIT/Revenue)	22.7	20.8	20.4	20.6	22.1
Asset turnover (Rev./Avg TA)	33.6	35.4	36.1	36.1	36.4
Leverage (Avg TA/Avg Equity)	3.6	3.6	3.6	3.4	3.2
Adjusted ROAE	13.8	13.5	14.3	14.2	15.1

Ratio Analysis

Y/E 31 Mar	FY21A	FY22A	FY23E	FY24E	FY25E
YoY growth (%)					
Revenue	(4.3)	7.8	12.4	2.3	2.5
EBITDA	1.3	(8.4)	20.6	3.5	5.8
Adjusted EPS	5.1	2.1	12.9	5.9	15.8
Profitability & Return ratios (%)					
EBITDA margin	29.9	27.5	26.0	26.1	27.4
EBIT margin	22.7	20.8	20.4	20.6	22.1
Adjusted profit margin	11.3	10.6	11.1	11.5	12.9
Adjusted ROAE	13.8	13.5	14.3	14.2	15.1
ROCE	12.3	10.9	11.7	11.8	12.6
Working capital days (days)					
Receivables	69	57	65	66	65
Inventory	18	18	20	19	19
Payables	30	30	34	33	32
Ratios (x)					
Gross asset turnover	0.5	0.6	0.6	0.6	0.6
Current ratio	1.3	2.6	1.4	1.4	1.6
Net interest coverage ratio	11.7	10.0	10.1	10.4	11.4
Adjusted debt/equity	1.3	1.4	1.3	1.2	1.0

Source: Company, BOBCAPS Research | Note: TA = Total Assets

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Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

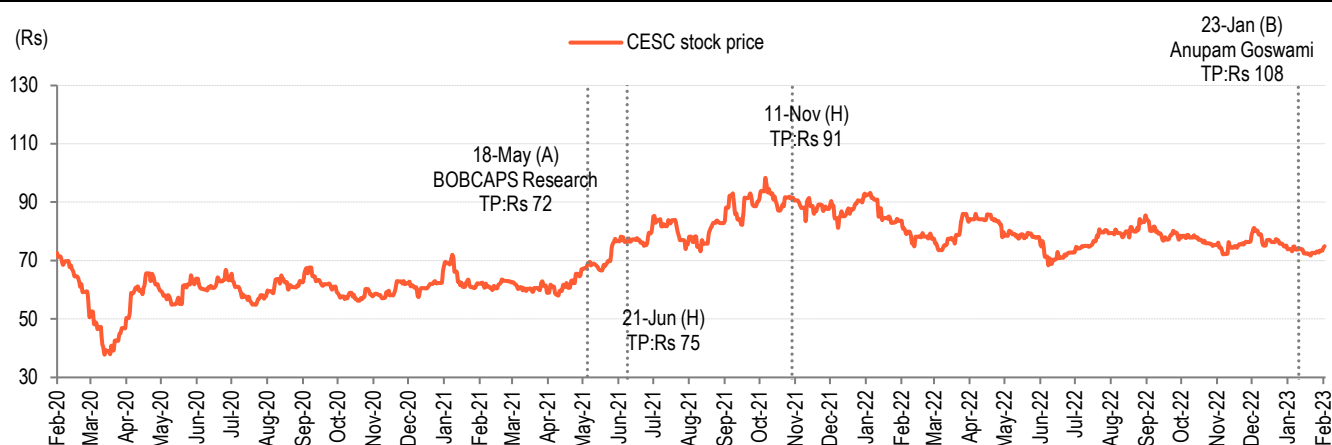
HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

Ratings and Target Price (3-year history): CESC (CESC IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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