

HOLD
 TP: Rs 201 | ▲ 9%

POWER GRID CORP

| Power

| 10 November 2021

Steady but limited growth drivers

- **Steady 1.9% YoY growth in Q2 pretax income and appreciable decline in outstanding payments**
- **Transmission pipeline weak. PWGR pursuing smart meter and distribution-related opportunities but business models yet to evolve**
- **Retain HOLD with slight change in TP from Rs 196 to Rs 201 driven by revised earnings estimates**

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Steady quarter: PWGR reported Q2FY22 PAT growth of 9% YoY driven by a drop in effective tax rate. Pretax income was up just 1.9%. Sequentially, core PAT rose 13% QoQ due to lower tax and higher other income (reported PAT fell due to a gain from InvIT sale in Q1FY22). Outstanding payments have declined 23% YoY, indicating improvement in payments from discoms.

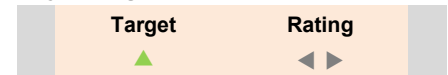
Transmission growth opportunities limited: PWGR’s management cited potential opportunities worth Rs 250bn primarily for interstate transmission services (ISTS) for the entire industry. Management expects project awards to accelerate in H2FY22 after a slow H1 that dragged the outstanding backlog down sharply to Rs 275bn. The recent policy change is also expected to accelerate the award of transmission projects.

Opportunity from smart meters and distribution network augmentation: Management sees opportunities in smart meter financing, system integration and data analysis, for which the company is in talks with six states. PWGR is also talking to five states for augmentation of their distribution network. However, it is unclear how these contract structures will evolve.

Steady earnings should continue: PWGR owns 40% of India’s transmission lines. Transmission is the least risky segment in the power sector due to a secure payment system and low scope for default given discoms’ high dependence on the transmission grid.

Valuations low but modest network scale-up a negative: We change our SOTP-based Sep’22 TP from Rs 196 to Rs 201 driven largely by a 7%/6%/9% increase in our FY22/FY23/FY24 net income estimates. We retain our HOLD rating. Key positive stock drivers are special dividends and order wins. Swift opening of the sector to private investment would act as a negative driver.

Key changes



Ticker/Price	PWGR IN/Rs 184
Market cap	US\$ 17.3bn
Free float	49%
3M ADV	US\$ 30.3mn
52wk high/low	Rs 210/Rs 134
Promoter/FPI/DII	51%/28%/8%

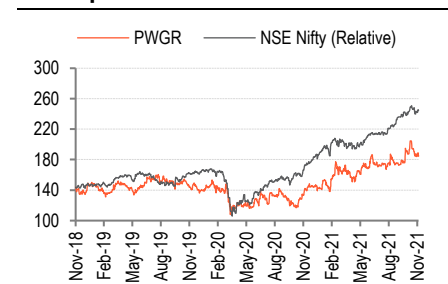
Source: NSE | Price as of 10 Nov 2021

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	3,96,398	4,01,331	4,12,780
EBITDA (Rs mn)	3,53,548	3,56,652	3,65,564
Adj. net profit (Rs mn)	1,31,141	1,31,356	1,36,330
Adj. EPS (Rs)	25.1	18.8	19.5
Consensus EPS (Rs)	25.1	19.7	21.2
Adj. ROAE (%)	19.5	17.7	16.8
Adj. P/E (x)	7.4	9.8	9.4
EV/EBITDA (x)	7.3	7.2	6.8
Adj. EPS growth (%)	5.7	(24.9)	3.8

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Fig 1 – Quarterly performance

(Rs mn)	Q2FY22	Q2FY21	YoY (%)	Q1FY22	QoQ (%)	H1FY22	H1FY21	YoY (%)
Revenue (post indirect taxes)	1,02,670	95,297	7.7	1,02,165	0.5	2,04,835	1,89,871	7.9
Cost of Revenue	0	0	-	0	-	0	0	-
Gross Profit	1,02,670	95,297	7.7	1,02,165	0.5	2,04,835	1,89,871	7.9
Gross Margin (%)	100.0	100.0	0bps	100.0	0bps	100.0	100.0	0bps
Employee Benefits Expense	(5,336)	(4,898)	8.9	(5,269)	1.3	(10,605)	(9,760)	8.6
Other Expense	(6,229)	(5,985)	4.1	(6,911)	(9.9)	(13,139)	(12,280)	7.0
Other Income	(3,394)	(82)	4,029.3	5,155	(165.8)	1,761	3,858	(54.4)
EBITDA	87,711	84,332	4.0	95,141	(7.8)	1,82,852	1,71,689	6.5
EBITDA margin (%)	85.4	88.5	(306bps)	93.1	(769.5bps)	178.6	180.9	(231bps)
Depreciation & Amortization	(31,946)	(28,948)	10.4	(31,125)	2.6	(63,071)	(58,536)	7.7
EBIT	55,766	55,384	0.7	64,016	(12.9)	1,19,781	1,13,152	5.9
EBIT margin (%)	54.3	58.1	(380bps)	62.7	(834bps)	58.5	59.6	(112bps)
Interest Income	0	0	-	0	-	0	0	-
Interest Expense	(18,845)	(20,033)	(5.9)	(22,160)	(15.0)	(41,005)	(42,060)	(2.5)
Dividend	0	0	-	0	-	0	0	-
Other Financial Items	2,478	3,013	(17.8)	1,751	41.5	4,229	6,606	(36.0)
Forex	0	0	-	0	-	0	0	-
Total Financials	(16,368)	(17,020)	(3.8)	(20,408)	(19.8)	(36,776)	(35,453)	3.7
Income after financial items	39,398	38,364	2.7	43,608	(9.7)	83,006	77,699	6.8
Margin (%)	38.4	40.3	(188bps)	42.7	(431bps)	40.5	40.9	(40bps)
Associate Income	285	565	(49.5)	173	65.3	458	1,044	(56.2)
Pretax income	39,683	38,929	1.9	43,780	(9.4)	83,463	78,743	6.0
Total Non-Recurring	0	(36)	(100.0)	30,140	(100.0)	30,140	(10,786)	(379.4)
Reported Pretax	39,683	38,893	2.0	73,920	(46.3)	1,13,603	67,956	67.2
Taxation	0	0	-	0	-	0	0	-
Total	(5,919)	(7,952)	(25.6)	(13,937)	(57.5)	(19,856)	(16,531)	20.1
% of pretax income before Associates	15	21	(27.5)	32	0.0	47	43	0.0
Net income before minorities	33,764	30,941	9.1	59,983	(43.7)	93,747	51,425	82.3
Minorities	0	0	-	0	-	0	0	-
Net income after minorities	33,764	30,941	9.1	59,983	(43.7)	93,747	51,425	82.3
Core net income	33,764	30,977	9.0	29,843	13.1	63,607	62,212	2.2
Net margin (%)	32.9	32.5	38bps	29.2	368bps	31.1	32.8	(171bps)

Source: Company, BOBCAPS Research

Fig 2 – Segmental performance

(Rs bn)	Q2FY22	Q2FY21	YoY (%)	Q1FY22	QoQ (%)	H1FY22	H1FY21	YoY (%)
Revenue								
Transmission	1,00,543	95,304	5.5	1,01,064	(0.5)	2,01,606	1,90,603	5.8
Consultancy	1,898	1,084	75.1	1,563	21.4	3,461	2,069	67.3
Telecom	1,910	1,902	0.4	1,188	60.7	3,098	3,778	(18.0)
Segment Profit								
Transmission	54,602	57,043	(4.3)	65,537	(16.7)	1,20,139	1,18,269	1.6
Consultancy	951	208	356.4	683	39.1	1,634	366	347.0
Telecom	802	803	0.0	268	199.6	1,070	1,802	(40.6)
Segment EBIT Margin (%)								
Transmission	54.3	59.9	(555bps)	64.8	(1,054bps)	59.6	62.1	(246bps)
Consultancy	50.1	19.2	3,087bps	43.7	637bps	47.2	17.7	2,955bps
Telecom	42.0	42.2	(19bps)	22.5	1,948bps	34.5	47.7	(1,315bps)

Source: Company, BOBCAPS Research

Valuation methodology

Raise PAT estimates on execution, lower interest costs

We raise our FY22-FY24 net income estimates by 6-9% largely driven by a drop in interest expenses. We are close to consensus in terms of our net income estimates.

Fig 3 – Revised estimates

(Rs bn)	New			Old			Change (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	401	413	419	400	411	411	0.3	0.4	2.1
EBITDA	357	366	370	356	364	366	0.3	0.4	1.0
EBIT	226	226	223	228	227	240	(1.2)	(0.6)	(6.9)
Pretax Income	189	165	168	149	155	163	26.8	6.1	3.0
Net Income	131	136	139	123	128	128	6.5	6.1	9.2

Source: BOBCAPS Research

Fig 4 – Estimates vs. Consensus

(Rs bn)	BOBCAPS			Consensus			BOBCAPS vs. Consensus		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	401	413	419	411	435	442	(2.3)	(5.0)	(5.1)
EBITDA	357	366	370	364	380	386	(1.9)	(3.8)	(4.1)
EBIT	226	226	223	226	234	242	(0.1)	(3.4)	(7.7)
Pretax Income	189	165	168	170	177	185	10.7	(6.8)	(9.0)
Core Net Income	131	136	139	128	138	146	2.3	(1.4)	(4.3)
EPS (Rs/sh)	18.8	19.5	20.0	19.7	21.2	20.8	(4.4)	(7.8)	(3.7)

Source: Bloomberg, BOBCAPS Research

Fig 5 – Key assumptions

Parameter	FY21	FY22E	FY23E	FY24E
RTM (Regulatory Tariff Mechanism) New Orders	20,000	1,00,000	1,00,000	1,00,000
TBCB (Tariff Based Competitive Bidding) New Orders	40,000	50,000	50,000	50,000
RTM (Regulatory Tariff Mechanism) Regulated ROE (%)	15.5	15.5	15.5	15.5

Source: Company, BOBCAPS Research

Retain HOLD, TP of Rs 201

We have a new SOTP-based Sep'22 TP of Rs 201 (Rs 196 earlier), which implies an EV/EBITDA of 7.2x on FY23E – close to the 10-year mean. Given the company's steady but unexceptional growth outlook, we believe this multiple is justified and hence retain our HOLD rating.

The change in target price factors in the higher outstanding shares post a stock dividend as well as revisions to our earnings estimates and cost of equity assumptions for valuing the company's business segments through DCF. Our cost of equity has risen to 11.0% from 10.8% due to an increase in risk-free rate (to 6.22% from 6.12% reflecting changes in the Indian Government's 10-year treasury bond yield) and change in beta to 0.70 from 0.68 based on rolling two-year weekly returns. Our cost of debt has reduced to 7.0% from 7.5%, reflecting the drop in interest costs.

Fig 6 – SOTP valuation

Business (Rs mn)	EV	Net Debt FY22E	Equity Value	Stake (%)	Value of Stake	EV/EBITDA FY22E (x)	EBITDA FY22E
Standalone	22,69,513	11,57,257	11,12,256	100	11,12,256	6.7	3,38,431
Subsidiaries	2,09,451	76,520	1,32,931	100	1,32,931	11.5	18,221
Future TBCB Projects	60,080	0	60,080	100	60,080	-	-
Elimination	0	(55,290)	55,290	100	55,290	7.0	0
Majority Owned	25,39,044	11,78,487	13,60,557	-	13,60,557	7.1	3,56,652
JVs	-	-	-	-	-	-	-
INVIT	-	-	1,10,565	26	28,747	-	-
Other JVS	-	-	-	-	12,914	-	-
Total	-	-	-	-	14,02,218	7.2	-
Number of Share	-	-	-	-	6,975	-	-
Target Price	-	-	-	-	201	-	-
Target Price (Rounded to the nearest 1)	-	-	-	-	201	-	-

Source: BOBCAPS Research

Fig 7 – Peer comparison

Company	Ticker	Rating	Target Price (Rs)	EPS CAGR FY21-24E (%)	P/E (x)		EV/EBITDA (x)		Net Debt/EBITDA FY22E (x)
					FY22E	FY23E	FY22E	FY23E	
Power Grid	PWGR IN	HOLD	201	(7.26)	9.9	9.5	7.3	6.9	3.42
NTPC	NTPC IN	HOLD	111	7.39	8.3	7.3	7.8	7.2	4.85
Torrent Power	TPW IN	HOLD	461	12.87	16.8	15.7	8.4	7.4	1.62
CESC	CESC IN	HOLD	751	1.55	0.9	0.8	3.3	3.2	3.30

Source: Company, BOBCAPS Research

Key risks

- Upside risks to our estimates include faster-than-estimated growth in new transmission orders.
- Downside risks include slow order flows and a rapid opening up of the sector to private players, leading to more projects being bid out under the TBCB model.

Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
CESC	CESC IN	0.2	91	75	HOLD
NTPC	NTPC IN	18.3	137	111	HOLD
Power Grid Corp	PWGR IN	17.3	184	201	HOLD
Torrent Power	TPW IN	3.5	539	461	HOLD

Source: BOBCAPS Research, NSE | Price as of 10 Nov 2021

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Total revenue	3,77,435	3,96,398	4,01,331	4,12,780	4,19,244
EBITDA	3,46,236	3,53,548	3,56,652	3,65,564	3,69,978
Depreciation	(1,16,070)	(1,20,392)	(1,31,082)	(1,39,646)	(1,46,774)
EBIT	2,30,166	2,33,156	2,25,570	2,25,917	2,23,204
Net interest inc./(exp.)	(95,484)	(79,187)	(79,618)	(74,299)	(67,740)
Other inc./(exp.)	9,668	9,678	9,678	9,678	9,678
Exceptional items	0	(10,786)	30,140	0	0
EBT	1,45,902	1,55,008	1,88,688	1,64,511	1,68,303
Income taxes	(35,308)	(34,653)	(27,192)	(28,182)	(28,854)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	1,551	2,147	2,918	3,215	3,162
Reported net profit	1,10,594	1,20,355	1,61,496	1,36,330	1,39,450
Adjustments	13,440	10,786	(30,140)	0	0
Adjusted net profit	1,24,034	1,31,141	1,31,356	1,36,330	1,39,450

Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Accounts payables	2,265	1,875	1,898	1,952	1,983
Other current liabilities	9,686	10,326	10,349	10,403	10,434
Provisions	0	0	0	0	0
Debt funds	13,84,211	13,09,748	12,18,620	11,37,070	10,16,234
Other liabilities	4,45,671	2,63,890	2,63,890	2,63,890	2,63,890
Equity capital	52,316	52,316	52,316	52,316	52,316
Reserves & surplus	5,94,638	6,47,045	7,30,067	7,85,649	8,56,934
Shareholders' fund	6,46,954	6,99,361	7,82,383	8,37,965	9,09,250
Total liab. and equities	27,47,652	25,57,491	25,49,409	25,23,495	24,73,975
Cash and cash eq.	54,390	53,587	40,133	41,278	41,924
Accounts receivables	50,407	36,755	49,479	50,891	51,688
Inventories	14,335	13,669	13,840	14,234	14,457
Other current assets	61,988	83,407	83,407	83,407	83,407
Investments	989	1,387	1,387	1,387	1,387
Net fixed assets	17,94,498	18,21,090	18,11,376	17,82,598	17,31,442
CWIP	19,353	0	0	0	0
Intangible assets	16,623	16,170	16,170	16,170	16,170
Deferred tax assets, net	0	0	0	0	0
Other assets	7,35,069	5,31,426	5,03,478	5,03,391	5,03,360
Total assets	27,47,652	25,57,491	25,19,269	24,93,355	24,43,835

Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Cash flow from operations	3,36,092	2,93,122	3,16,590	3,35,630	3,40,135
Capital expenditures	(1,13,671)	(93,636)	(1,21,368)	(1,10,868)	(95,618)
Change in investments	1,016	(3,414)	27,415	0	0
Other investing cash flows	(124)	5,409	0	0	0
Cash flow from investing	(1,12,780)	(91,641)	(93,953)	(1,10,868)	(95,618)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	(17,397)	(46,263)	(91,128)	(81,550)	(1,20,836)
Interest expenses	(95,090)	(91,137)	(71,869)	(66,303)	(59,780)
Dividends paid	(53,440)	(68,220)	(78,474)	(80,748)	(68,165)
Other financing cash flows	1,43,795	2,06,029	2,41,470	2,28,601	2,48,780
Cash flow from financing	(22,132)	409	0	0	0
Chg in cash & cash eq.	37,611	(1,819)	(13,454)	1,145	646
Closing cash & cash eq.	54,390	53,587	40,133	41,278	41,924

Per Share

Y/E 31 Mar (Rs)	FY20A	FY21A	FY22E	FY23E	FY24E
Reported EPS	21.1	23.0	23.2	19.5	20.0
Adjusted EPS	23.7	25.1	18.8	19.5	20.0
Dividend per share	10.0	12.0	11.6	9.8	10.0
Book value per share	123.7	133.7	112.2	120.1	130.3

Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21A	FY22E	FY23E	FY24E
EV/Sales	6.7	6.5	6.4	6.1	5.8
EV/EBITDA	7.3	7.3	7.2	6.8	6.6
Adjusted P/E	7.8	7.4	9.8	9.4	9.2
P/BV	1.5	1.4	1.6	1.5	1.4

DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21A	FY22E	FY23E	FY24E
Tax burden (Net profit/PBT)	85.0	79.1	82.8	82.9	82.9
Interest burden (PBT/EBIT)	63.4	71.1	70.3	72.8	75.4
EBIT margin (EBIT/Revenue)	61.0	58.8	56.2	54.7	53.2
Asset turnover (Rev./Avg TA)	14.0	14.9	15.8	16.5	17.0
Leverage (Avg TA/Avg Equity)	4.4	3.9	3.4	3.1	2.8
Adjusted ROAE	20.0	19.5	17.7	16.8	16.0

Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22E	FY23E	FY24E
YoY growth (%)					
Revenue	7.7	5.0	1.2	2.9	1.6
EBITDA	25.0	2.1	0.9	2.5	1.2
Adjusted EPS	23.6	5.7	(24.9)	3.8	2.3
Profitability & Return ratios (%)					
EBITDA margin	91.7	89.2	88.9	88.6	88.2
EBIT margin	61.0	58.8	56.2	54.7	53.2
Adjusted profit margin	32.9	33.1	32.7	33.0	33.3
Adjusted ROAE	20.0	19.5	17.7	16.8	16.0
ROCE	9.4	9.9	10.0	10.1	10.1
Working capital days (days)					
Receivables	49	34	45	45	45
Inventory	14	13	13	13	13
Payables	2	2	2	2	2
Ratios (x)					
Gross asset turnover	0.2	0.2	0.2	0.2	0.2
Current ratio	0.6	0.6	0.6	0.6	0.6
Net interest coverage ratio	2.4	2.9	2.8	3.0	3.3
Adjusted debt/equity	2.1	1.9	1.6	1.4	1.1

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

Disclaimer

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

BUY – Expected return >+15%

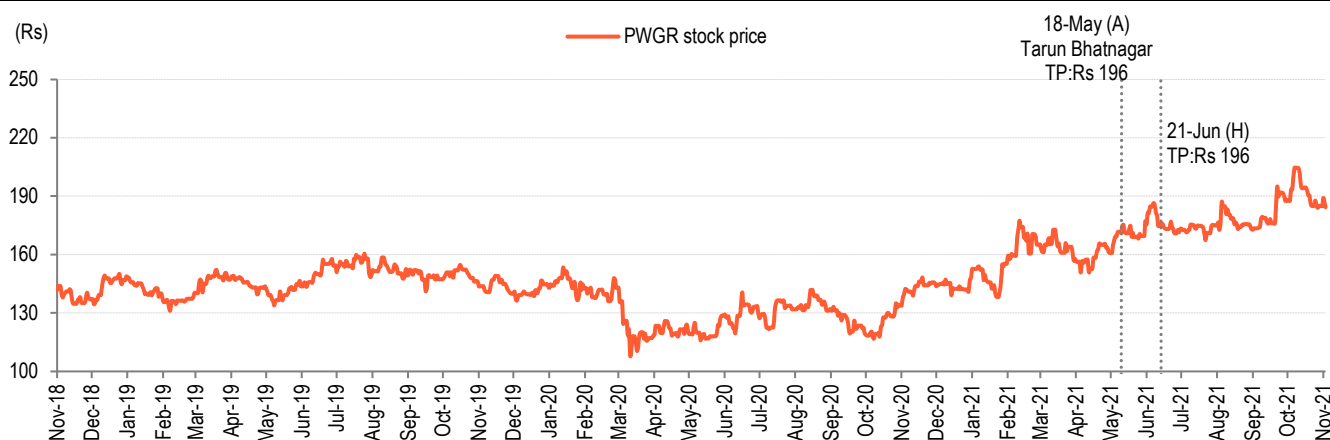
HOLD – Expected return from -6% to +15%

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): POWER GRID CORP (PWGR IN)



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

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