

NTPC | BUY

1Q18 Core RoE at 19%; High commercialisation cycle begins

NTPC's 1Q18 adjusted net profit stood at INR23bn (flat YoY) given lower PLFs YoY and some impact from coal accounting change. The key adjustment is for interest on income tax refunds, resulting in 3x increase in other income. However core RoEs (on regulated equity) remained stable at 19%, even as fuel cost/kWh increased 3% YoY due to shift to coal accounting on 'as received' vs. 'as fired' earlier. Kudgi U-1 commercialisation of 800MW on 31st July marks the beginning of high capacity addition cycle. NTPC guides for an additional 2.1GW to commercialise by 2Q18 end / early 3Q18, taking the full year target to 5.4GW (includes 1.8GW through JVs). The period of FY18–20 will witness annual addition of 4–5GW. Thus NTPC is set to add c40% of its existing base and almost double its regulated equity base in next 4–5 years. With NTPC delivering 19%–20% core RoE despite coal accounting impact, we remain confident of 14% earnings CAGR in next 3 years. With inexpensive valuations of 1.2x FY19 BV, we reiterate our BUY rating.

- **1Q18 adjusted profit flat YoY / Core RoE at 19%:** NTPC reported 1Q18 profit of INR26bn (+12% YoY) led by higher other income of Rs6.6bn (up 3x YoY). However, adjusted for interest on IT refund the adj. profit has been flat YoY even as coal plant PLFs declined to 79% (81% last year). However core RoEs remain steady at 19% in 1Q18. Better coal supply has almost fully negated imported coal use which is down to 75% YoY at 0.14mnT vs 38mnT of domestic coal consumed.
- **Commercialisation cycle begins:** Kudgi U-1 commercialisation of 800MW on 31st July marks the beginning of high capacity addition cycle. NTPC targets to commercialise 3.6GW of standalone capacity in FY18, with 2.1GW targeted in 2H18. Hence we believe NTPC is poised to deliver 14% profit CAGR growth in FY18–20 period, assuming 18% core RoE (vs. 20% in FY17).
- **Replacement of older plants:** 11GW of older plants are slotted for replacement, beginning with Patratu, Badarpur and Talcher-Thermal projects. However older plants can only be phased out once their replacement capacities are in place and PPAs for new capacities are signed with respective Discoms. We do not factor any benefit from this new replacement capacity adding to regulated equity.
- **Energy Pooling may boost PLF incentives:** NTPC has observed that some of its coal pit-head based plants (with low fuel cost) operate at sub-optimal PLFs given lower demand from regional States. On the other hand some of its high fuel cost plants in other regions operate at higher PLFs due to greater demand. Hence NTPC is proposing an arrangement whereby low fuel cost plants generate maximum power (raising PLFs), while lowering offtake from its high fuel cost plants. The power and fuel cost of all NTPC stations will be pooled across States while fixed costs are charged as per PPAs with respective Discoms. This creates a win-win, as State get cheaper electricity, while NTPC benefits from PLF incentives raising its core RoE. Discoms, MoP and CERC have all granted initial approval with granularities being worked. NTPC plans to implement this in FY19.

Financial Summary					(Rs mn)
Y/E March	FY15A	FY16A	FY17E	FY18E	FY19E
Net Sales	7,26,378	7,08,438	7,82,734	8,72,413	10,18,800
Sales Growth (%)	1.4	-2.5	10.5	11.5	16.8
EBITDA	1,54,615	1,78,871	2,12,843	2,39,477	2,81,530
EBITDA Margin (%)	21.3	25.2	27.2	27.5	27.6
Adjusted Net Profit	82,739	91,231	1,01,187	1,13,545	1,31,168
Diluted EPS (Rs.)	10.0	11.1	12.3	13.8	15.9
Diluted EPS Growth (%)	-21.7	10.3	10.9	12.2	15.5
ROIC (%)	7.7	8.6	6.9	6.8	7.0
ROE (%)	9.9	10.7	10.9	11.3	11.9
P/E (x)	17.1	15.5	14.0	12.5	10.8
P/B (x)	1.7	1.6	1.5	1.3	1.2
EV/EBITDA (x)	13.4	12.5	10.9	10.4	8.9
Dividend Yield (%)	1.5	1.5	1.5	1.5	1.5

Source: Company data, JM Financial. Note: Valuations as of 02/Aug/2017



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Recommendation and Price Target

Current Reco.	BUY
Previous Reco.	BUY
Current Price Target (12M)	210
Upside/(Downside)	22.2%
Previous Price Target	210
Change	0.0%

Key Data – NTPC IN

Current Market Price	Rs172
Market cap (bn)	Rs1,417.0/US\$22.3
Free Float	18%
Shares in issue (mn)	8,245.5
Diluted share (mn)	8,245.5
3-mon avg daily val (mn)	Rs742.8/US\$0.7
52-week range	178/143
Sensex/Nifty	32,477/10,082
Rs/US\$	63.7

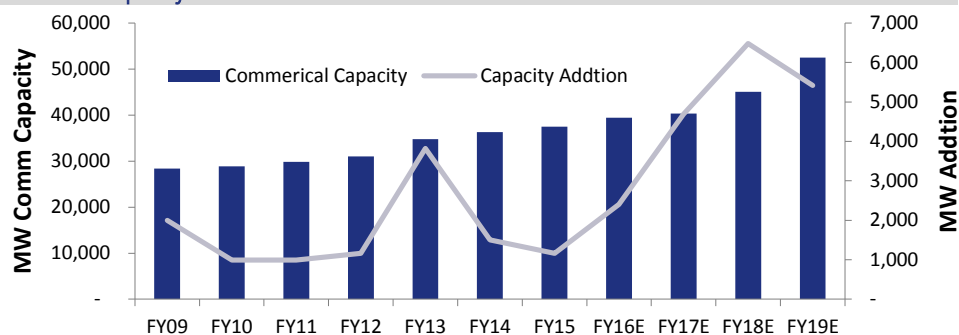
Price Performance

%	1M	6M	12M
Absolute	8.1	-0.4	7.8
Relative*	2.9	-13.4	-7.1

* To the BSE Sensex

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Please see Appendix I at the end of this report for Important Disclosures and Disclaimers and Research Analyst Certification.

Exhibit 1. Capacity Additions accelerates in FY18-19

Source: JM Financial, Company

4-5GW of annual capacity addition in FY18-20

Exhibit 2. SOTP Valuation

	Comments	Multiple	Per share value
Regulated equity FY19E	FY19E regulated equity	2.1	167
Regulated equity in JV Co's	FY19E regulated equity	1.5	15
CWIP (Equity component)	1X FY19 BV	1.0	25
Investments & Cash	1x BV	1.0	6
			212

Source: Company, JM Financial

We find FV at 18% RoE with

4-5GW annual capacity addition, implying a 14% EPS CAGR

Exhibit 3. SOTP Sensitivity

		Core RoE			
Growth (g)		16%	18%	19%	20%
	5%	174	199	212	225
	6%	183	212	227	241
	7%	194	230	247	265
	8%	213	256	278	300
	9%	244	302	332	361

Source: Company, JM Financial

We value NTPC at 18% RoE Vs. run-rate of 19-20% core RoEs

Exhibit 4. Quarterly Financials

Y/E March	1Q17	1Q18	%YoY	FY17	FY18E	%YoY
Generation (MUs)	64,555	64,411	-0.2	2,50,318	2,62,362	4.8
Net Sales	1,90,367	1,98,793	4.4	7,82,734	8,72,413	11.5
Expenditure	1,38,524	1,46,110	5.5	5,69,892	6,32,935	11.1
EBITDA	51,843	52,684	1.6	2,12,843	2,39,477	12.5
EBITDA (%)	27.2	26.5	-2.7	27.2	27.5	26bps
Other income	1,579	6,626	319.7	10,689	18,000	68.4
Depreciation	13,952	15,700	12.5	59,208	64,122	8.3
EBIT	39,470	43,610	10.5	1,64,323	1,93,355	17.7
Interest	9,004	8,956	-0.5	35,972	42,750	18.8
PBT	30,466	34,654	13.7	1,28,351	1,50,605	17.3
Tax	7,066	8,472	19.9	30,026	37,060	23.4
Tax rate (%)	23.2	24.4	5.4	23.4	24.6	
PAT	23,400	26,182	11.9	98,325	1,13,545	15.5
RoE	20%	19%		20%	13%	

Source: Company, JM Financial

Exhibit 5. Cost Break-up

	1Q17	1Q18	%YoY	FY17	FY18E
Raw material Costs	1,16,324	1,19,401	2.6	4,75,722	5,32,821
% of sales	61	60	-104bps	61	61
RM/MU	1.8	1.9	2.9	1.9	2.0
Staff Costs	9,589	10,712	11.7	43,246	40,243
% of sales	5.0	5.4	35bps	5.5	4.6
Other Expenses	12,611	15,996	26.8	50,924	59,870
% of sales	6.6	8.0	142bps	6.5	6.9

Source: Company, JM Financial

Company background

- NTPC is the largest power utility company in India owning and operating 40GW on assured regulated RoE-based norms. Recently, it was impacted by the tightening of CERC norms, impacting RoE by 5–6%. Capacity addition has also tapered off to 1–1.2GW annually.
- Potential triggers: a) Revival in GW addition with 25GW planned during the 13th plan period—15GW thermal + 10GW solar; b) revival in RoEs as the company adjusts to newer efficiency thresholds; and c) recovery in project CoD, as bunched under-construction capacity commissions in FY17–18 can boost growth. Current schedule points to bunched project commissioning of 6–8GW in FY17–18.

Investment rationale

- **High earning visibility:** With a capacity addition pick up expected in FY17–19, NTPC has high earnings visibility, since it earns a minimum of 15.5% RoE invested in the power business under CERC norms. The FY15/FY16 actual earnings were at 17–19% of regulated equity on incentives/cost savings. Most utilities are currently suffering from low capacity utilisation (PLF) due to low power demand, while NTPC continues to enjoy guaranteed 15.5% RoE, as long as its plants are available to produce power.
- **Large capex pipeline:** With 18GW of under-construction capacity to be commissioned by FY19–20, NTPC will add >40% of its existing 38GW commercial base, in the next 3–4 years. With all of this capacity being based on regulated RoEs, earnings growth will closely follow project capitalisation. Once executed, this can potentially add >60% to regulated equity by FY19–20. Solar capex is an additional 10GW targeted in the next seven years, of which 250MW in AP has been ordered.

Key risks

- Delayed capacity addition and lower incentive earnings, in case PLFs decline, continue to be risks.
- Any incremental hit from the HC's decision on the CERC policy of coal costing based on coal "as received" from CIL vis-à-vis "as fired" over and above the 2% core RoE impact already factored.

Financial Tables (Standalone)

Income Statement (Rs mn)					
Y/E March	FY15A	FY16A	FY17E	FY18E	FY19E
Net Sales	7,26,378	7,08,438	7,82,734	8,72,413	10,18,800
Sales Growth	1.4%	-2.5%	10.5%	11.5%	16.8%
Other Operating Income	0	0	0	0	0
Total Revenue	7,26,378	7,08,438	7,82,734	8,72,413	10,18,800
Cost of Goods Sold/Op. Exp	46,455	55,765	50,924	59,870	72,150
Personnel Cost	36,856	35,817	43,246	40,243	43,735
Other Expenses	4,88,452	4,37,986	4,75,722	5,32,821	6,21,384
EBITDA	1,54,615	1,78,871	2,12,843	2,39,477	2,81,530
EBITDA Margin	21.3%	25.2%	27.2%	27.5%	27.6%
EBITDA Growth	-10.9%	15.7%	19.0%	12.5%	17.6%
Depn. & Amort.	49,117	51,723	59,208	64,122	81,841
EBIT	1,05,498	1,27,147	1,53,635	1,75,355	1,99,689
Other Income	27,405	11,654	10,689	18,000	19,500
Finance Cost	27,436	32,964	35,972	42,750	45,209
PBT before Excep. & Forex	1,05,467	1,05,837	1,28,351	1,50,605	1,73,981
Excep. & Forex Inc./Loss(-)	0	0	0	0	0
PBT	1,05,467	1,05,837	1,28,351	1,50,605	1,73,981
Taxes	2,558	-1,738	30,026	37,060	42,812
Extraordinary Inc./Loss(-)	0	0	0	0	0
Assoc. Profit/Min. Int.(-)	0	0	0	0	0
Reported Net Profit	1,02,909	1,07,575	98,325	1,13,545	1,31,168
Adjusted Net Profit	82,739	91,231	1,01,187	1,13,545	1,31,168
Net Margin	11.4%	12.9%	12.9%	13.0%	12.9%
Diluted Share Cap. (mn)	8,245.5	8,245.5	8,245.5	8,245.5	8,245.5
Diluted EPS (Rs.)	10.0	11.1	12.3	13.8	15.9
Diluted EPS Growth	-21.7%	10.3%	10.9%	12.2%	15.5%
Total Dividend + Tax	24,788	24,788	24,788	23,190	23,190
Dividend Per Share (Rs)	2.5	2.5	2.5	2.5	2.5

Source: Company, JM Financial

Balance Sheet (Rs mn)					
Y/E March	FY15A	FY16A	FY17E	FY18E	FY19E
Shareholders' Fund	8,16,574	8,87,820	9,61,357	10,51,712	11,59,690
Share Capital	82,455	82,455	82,455	82,455	82,455
Reserves & Surplus	7,34,119	8,05,365	8,78,902	9,69,257	10,77,235
Preference Share Capital	0	0	0	0	0
Minority Interest	0	0	0	0	0
Total Loans	7,85,323	8,63,828	0	12,19,336	12,89,446
Def. Tax Liab. / Assets (-)	9,791	11,522	11,522	11,522	11,522
Total - Equity & Liab.	16,11,688	17,63,170	9,72,879	22,82,570	24,60,658
Net Fixed Assets	0	0	0	19,98,873	21,27,935
Gross Fixed Assets	12,83,237	13,90,934	14,41,840	17,24,359	22,00,859
Intangible Assets	0	0	0	0	0
Less: Depn. & Amort.	4,94,746	5,46,469	6,05,678	6,69,800	7,51,641
Capital WIP	5,64,935	7,36,170	9,15,656	9,44,314	6,78,716
Investments	90,321	82,932	65,755	48,579	31,403
Current Assets	5,27,100	4,82,627	6,34,338	6,30,055	7,07,385
Inventories	74,530	71,925	79,468	88,573	1,03,435
Sundry Debtors	76,044	78,440	86,666	96,596	1,12,804
Cash & Bank Balances	1,28,788	44,064	1,80,006	1,56,689	2,02,948
Loans & Advances	1,79,355	1,92,295	1,92,295	1,92,295	1,92,295
Other Current Assets	68,384	95,903	95,903	95,903	95,903
Current Liab. & Prov.	3,59,160	3,83,023	3,87,764	3,94,938	4,06,065
Current Liabilities	73,473	74,495	79,236	86,410	97,537
Provisions & Others	2,85,687	3,08,528	3,08,528	3,08,528	3,08,528
Net Current Assets	1,67,941	99,604	2,46,574	2,35,117	3,01,320
Total - Assets	-3,59,160	-3,83,023	-3,87,764	22,82,570	24,60,658

Source: Company, JM Financial

Cash Flow Statement (Rs mn)					
Y/E March	FY15A	FY16A	FY17E	FY18E	FY19E
Profit before Tax	1,05,467	1,05,837	1,28,351	1,50,605	1,73,981
Depn. & Amort.	49,117	51,723	59,208	64,122	81,841
Net Interest Exp. / Inc. (-)	27,436	32,964	35,972	42,750	45,209
Inc (-) / Dec in WCap.	82,689	-21,912	-11,028	-11,860	-19,943
Others	0	0	0	0	0
Taxes Paid	2,558	-1,738	30,026	37,060	42,812
Operating Cash Flow	2,62,150	1,70,350	1,82,477	2,08,557	2,38,275
Capex	-1,07,404	-1,00,308	-33,729	-2,65,343	-4,59,324
Free Cash Flow	1,54,745	70,043	1,48,748	-56,786	-2,21,049
Inc (-) / Dec in Investments	-1,16,068	-1,71,235	-1,79,486	-28,658	2,65,598
Others	0	861	0	0	0
Investing Cash Flow	-2,23,472	-2,70,681	-2,13,215	-2,94,002	-1,93,726
Inc / Dec (-) in Capital	0	0	0	0	0
Dividend + Tax thereon	-24,788	-24,788	-24,788	-23,190	-23,190
Inc / Dec (-) in Loans	1,13,622	78,504	2,27,440	1,28,068	70,110
Others	-1,51,837	-32,964	-35,972	-42,750	-45,209
Financing Cash Flow	-63,003	20,752	1,66,680	62,128	1,711
Inc / Dec (-) in Cash	-24,326	-79,579	1,35,942	-23,317	46,259
Opening Cash Balance	1,53,114	1,28,788	44,064	1,80,006	1,56,689
Closing Cash Balance	1,28,788	49,210	1,80,006	1,56,689	2,02,948

Source: Company, JM Financial

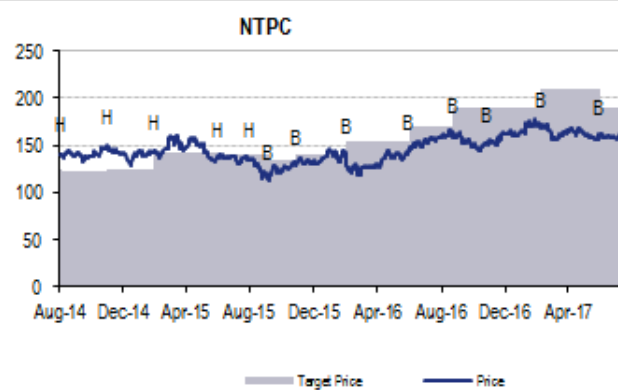
Dupont Analysis					
Y/E March	FY15A	FY16A	FY17E	FY18E	FY19E
Net Margin	11.4%	12.9%	12.9%	13.0%	12.9%
Asset Turnover (x)	0.4	0.3	0.3	0.3	0.4
Leverage Factor (x)	2.2	2.4	2.5	2.5	2.5
RoE	9.9%	10.7%	10.9%	11.3%	11.9%
Key Ratios					
Y/E March	FY15A	FY16A	FY17E	FY18E	FY19E
BV/Share (Rs.)	99.0	107.7	116.6	127.6	140.6
ROIC	7.7%	8.6%	6.9%	6.8%	7.0%
ROE	9.9%	10.7%	10.9%	11.3%	11.9%
Net Debt/Equity (x)	0.8	0.9	0.9	1.0	0.9
P/E (x)	17.1	15.5	14.0	12.5	10.8
P/B (x)	1.7	1.6	1.5	1.3	1.2
EV/EBITDA (x)	13.4	12.5	10.9	10.4	8.9
EV/Sales (x)	2.9	3.2	3.0	2.8	2.5
Debtor days	38	40	40	40	40
Inventory days	37	37	37	37	37
Creditor days	38	38	38	39	39

Source: Company, JM Financial

History of Earnings Estimate and Target Price

Date	FY17E EPS (Rs)	% Chg.	FY18E EPS (Rs)	% Chg.	Target Price	% Chg.
19-May-14					125	
4-Aug-14					122	-2.4
31-Oct-14	11.5				125	2.5
30-Jan-15	12.2	6.1			142	13.6
30-May-15	11.6	-4.9			140	-1.4
30-Jul-15	11.6	0.0			140	0.0
7-Sep-15	11.3	-2.6	14.0		134	-4.3
29-Oct-15	11.8	4.4	14.5	3.6	140	4.5
1-Feb-16	11.3	-4.2	13.9	-4.1	154	10.0
1-Jun-16	11.6	2.7	13.6	-2.2	170	10.4
24-Aug-16	11.2	-3.4	13.3	-2.2	190	11.8
28-Oct-16	12.3	9.8	13.2	-0.8	190	0.0
9-Feb-17	11.6	-5.7	13.2	0.2	210	10.5
31-May-17	11.7	0.8	12.9	-2.8	190	-9.5

Recommendation History



APPENDIX I

JM Financial Institutional Securities Limited

Corporate Identity Number: U65192MH1995PLC092522

Member of BSE Ltd. and National Stock Exchange of India Ltd. and Metropolitan Stock Exchange of India Ltd.

SEBI Registration Nos.: BSE - INZ010012532, NSE - INZ230012536 and MSEI - INZ260012539, Research Analyst – INH000000610

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Rating	Meaning
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Sell	Price expected to move downwards by more than 10%

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