CESC

BSE SENSEX	S&P CNX
54,493	16,295

Bloomberg	CESC IN
Equity Shares (m)	133
M.Cap.(INRb)/(USDb)	102.1 / 1.4
52-Week Range (INR)	871 / 553
1, 6, 12 Rel. Per (%)	0/19/-9
12M Avg Val (INR M)	375

Financials & Valuations (INR b)

Y/E MARCH	2021	2022E	2023E
Sales	116.4	118.9	122.6
EBITDA	36.1	36.1	36.8
Adj. PAT	13.3	14.2	14.8
EBITDA Margin (%)	31.0	30.4	30.0
Adj. EPS (INR)	100.1	106.4	111.4
EPS Gr. (%)	2.4	6.4	4.7
BV/Sh. (INR)	742.3	801.5	851.3
Ratios			
RoE (%)	13.7	13.8	13.5
RoCE (%)	9.2	9.5	9.5
Payout (%)	45.0	44.4	44.5
Valuations			
P/E (x)	7.7	7.2	6.9
P/BV (x)	1.0	1.0	0.9
EV/EBITDA(x)	6.3	5.9	5.6
Div. Yield (%)	5.8	6.1	6.4

Shareholding pattern (%)

As On	Jun-21	Mar-21	Jun-20
Promoter	49.9	49.9	49.9
DII	23.6	38.6	23.8
FII	13.4	0.0	17.9
Others	13.1	11.5	8.4

FII Includes depository receipts

CMP: INR771 TP: INR905 (+17%) Buy

Expanding its distribution footprint

- CESC has emerged as the highest bidder for a 100% stake in Chandigarh Distribution Company (DISCOM). The takeover would be subject to the completion of certain formalities, as per the company. The receipt of the Letter of Intent (LOI) for the same is still pending.
- The move is in line with the co.'s strategy to grow its presence within the Distribution space. With a healthy balance sheet (net debt/equity: 1.2x) and strong expertise, the company is well-placed to capitalize on privatization opportunities.
- Media articles reveal CESC bid INR8.71b for the acquisition. Based on the current regulated equity base and regulated RoEs of 15.5–16%, the bid appears to be on the higher side. Although, CESC has significant expertise in power distribution, along with the ability to generate returns higher than the regulated RoEs. We await clarity on the details of the Chandigarh circle takeover.

Steady circle, with scope to lower T&D losses

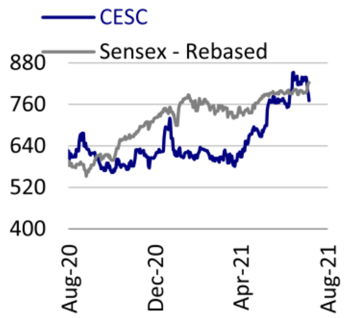
- A look into the tariff filings indicates a steady circle – nearly a 50% mix of residential consumers. Power demand / The number of consumers at the Chandigarh circle has seen a modest ~2% CAGR over FY15–20.
- Aggregate T&D losses have been in the range of ~16% over the past five years (intra-state: 12%; inter-state: 4%).
- Regulated RoEs stand at 15.5–16% (Wires business: 15.5%; Supply: 16%), with avg. gross fixed assets posting a 3% CAGR over the last five years.
- Capitalization has been at an avg. of ~INR100m in recent years. There is scope for T&D losses to decrease, with intra-state losses of 12%, and the same may necessitate higher capex/capitalization.

Await details on the takeover

- Media articles (see here) have indicated that the co. has won the stake for INR8.71b. Given a) the current regulated equity of INR1.3b for the circle, b) a growth rate of just 2%, and c) regulated RoEs of 15.5–16%, the bid appears to be high – implying a value of ~6.5x regulated equity.
- However, we await details on the takeover plan (initial regulated equity base, capitalization outlook, AT&C norms, and incentives). We note CESC has significant expertise in the Distribution space, with operations in Kolkata, Rajasthan, and Noida, along with the ability to generate returns higher than the regulated RoEs. Our interaction with the co. further indicates a longer term strategy being employed with its entry into Chandigarh – which would prepare it well for future opportunities in nearby (Haryana and Punjab) circles.

Aniket Mittal – Research Analyst (Aniket.Mittal@MotilalOswal.com)

Stock Performance (1-year)



- Accordingly, we do not bake in Chandigarh into our estimates – as the actual takeover is yet to take place. While we keep a keen eye on details and value-accretion from the circle, the turnaround story for its existing businesses of Dhariwal as well as distribution franchises (DFs) remains intact. CESC's existing Distribution business is high-RoE and delivers steady growth, with generation assets yielding healthy FCF. The stock trades attractively at ~7x FY22/23E P/E as we factor in the tightening of norms at Haldia and S/A in FY23. We value the stock at 8.5x FY22 P/E and maintain our Buy rating, with TP of INR905/sh.

Exhibit 1: Key snapshot of Chandigarh circle

		FY15	FY16	FY17	FY18	FY19	FY20	CAGR/ Annual capitalization	
Chandigarh									
No of consumers	'000	210	216	222	229	231	231	1.9	
Energy Sales	MU	1,472	1,491	1,591	1,589	1,536	1,596	1.6	*5 year CAGR*
Resident	%	41	41	45	46	44	48		
Commercial	%	29	29	31	31	30	30		
Industry	%	15	16	16	16	16	16		
Agriculture	%	0	0	0	0	0	0		
Others	%	7	7	7	6	6	6		
Power Purchase	MU	1,840	1,917	1,981	1,954	2,053	2,152	3.2	*5 year CAGR*
Cost	INR/kWh	3.8	3.6	3.4	3.5	3.7	3.6		
T&D losses (indicative)	%	17.3	17.5	18.2	12.8	16.7	15.4		
Regulated Equity	INR m	NA	1,212	1,228	1,253	1,297	1,314	2.0	*4 year CAGR*
Capitalization	INR m	166	123	56	81	149	55	105	*Avg. Annual capitalization*
Gross Fixed Assets	INR m	3,916	4,039	4,293	4,374	4,523	4,578	3.2	*5 year CAGR*

Source: JERC, MOFSL

Financials and valuations

Income Statement (INR m)

Y/E March	2017	2018	2019	2020	2021	2022E	2023E
Net Sales	**83,634**	**102,749**	**106,641**	**110,146**	**116,390**	**118,850**	**122,594**
Change (%)	-31.0	22.9	3.8	3.3	5.7	2.1	3.1
EBITDA	**27,845**	**29,991**	**33,867**	**35,355**	**36,100**	**36,128**	**36,804**
% of Net Sales	33.3	29.2	31.8	32.1	31.0	30.4	30.0
Depn. & Amortization	7,148	7,515	7,638	7,814	8,670	8,125	8,792
EBIT	**20,697**	**22,477**	**26,230**	**27,541**	**27,430**	**28,003**	**28,012**
Net Interest	13,724	13,030	13,247	13,574	12,260	12,556	11,694
Other income	2,300	2,520	2,043	2,025	2,350	2,285	2,078
EO expense	0	0	0	0	0	0	0
PBT after EO	9,273	11,967	15,025	15,992	17,520	17,732	18,397
Tax	3,210	3,562	3,737	3,627	3,890	3,269	3,239
Rate (%)	34.6	29.8	24.9	22.7	22.2	18.4	17.6
Reported PAT	**6,063**	**8,405**	**11,288**	**12,365**	**13,630**	**14,463**	**15,157**
Minority and Associates	-710	-129	552	655	-320	-305	-337
Adjusted PAT	**5,354**	**8,276**	**11,840**	**13,021**	**13,310**	**14,157**	**14,821**
Change (%)	-11.1	54.6	43.1	10.0	2.2	6.4	4.7

Balance Sheet Statement (INR m)

Y/E March	2017	2018	2019	2020	2021	2022E	2023E
Share Capital	1,332	1,332	1,332	1,332	1,330	1,330	1,330
Reserves	104,895	82,870	88,406	94,942	97,400	105,273	111,888
Net Worth	**106,227**	**84,202**	**89,738**	**96,274**	**98,730**	**106,603**	**113,218**
Minority Interest	12,101	694	821	858	3,970	4,275	4,612
Total Loans	155,994	145,778	144,721	139,909	140,119	131,785	122,204
Deferred Tax Liability	38,873	36,410	39,404	40,053	41,590	41,590	41,590
Capital Employed	**313,194**	**267,083**	**274,684**	**277,094**	**284,409**	**284,254**	**281,624**
Gross Block	267,642	268,271	276,618	286,327	301,102	308,776	316,454
Less: Accum. Deprn.	21,486	29,736	40,132	50,462	59,132	67,256	76,048
Net Fixed Assets	**246,156**	**238,535**	**236,485**	**235,866**	**241,970**	**241,520**	**240,406**
Capital WIP	3,919	2,166	1,614	1,468	1,340	1,340	1,340
Goodwill	20,106	0	0	0	0	0	0
Investments	4,224	6,673	6,724	6,703	1,400	1,400	1,400
Curr. Assets	**104,322**	**82,499**	**89,859**	**99,685**	**113,910**	**113,588**	**111,872**
Inventories	8,454	5,826	7,005	7,184	5,970	5,819	5,937
Account Receivables	15,596	15,374	17,389	18,818	23,150	18,797	16,969
Cash and Bank Balance	22,931	17,003	15,437	18,060	20,270	24,442	24,436
Others	57,340	44,296	50,029	55,623	64,520	64,531	64,531
Curr. Liability & Prov.	**65,533**	**62,791**	**60,000**	**66,627**	**74,211**	**73,594**	**73,395**
Account Payables	7,890	6,907	6,778	6,568	9,390	8,718	7,915
Provisions & Others	57,642	55,884	53,222	60,058	64,821	64,876	65,480
Net Curr. Assets	**38,789**	**19,708**	**29,860**	**33,058**	**39,699**	**39,994**	**38,478**
Appl. of Funds	**313,194**	**267,083**	**274,684**	**277,094**	**284,409**	**284,254**	**281,624**

Source: Company, MOFSL

Financials and valuations

Ratios

	2017	2018	2019	2020	2021	2022E	2023E
Basic (INR)							
EPS	**40.2**	**62.1**	**88.9**	**97.7**	**100.1**	**106.4**	**111.4**
Cash EPS	93.8	118.5	146.2	156.4	165.3	167.5	177.5
BV/Share	797.4	632.0	673.6	722.7	742.3	801.5	851.3
DPS	10.0	12.0	17.5	20.0	45.0	47.3	49.6
Payout (%)	24.9	19.3	19.7	20.5	45.0	44.4	44.5
Dividend yield (%)	1.3	1.6	2.3	2.6	5.8	6.1	6.4
Valuation (x)							
P/E	19.2	12.4	8.7	7.9	7.7	7.2	6.9
Cash P/E	8.2	6.5	5.3	4.9	4.7	4.6	4.3
P/BV	1.0	1.2	1.1	1.1	1.0	1.0	0.9
EV/EBITDA	8.9	7.7	6.9	6.4	6.3	5.9	5.6
Dividend Yield (%)	1.3	1.6	2.3	2.6	5.8	6.1	6.4
Return Ratios (%)							
RoE	5.0	8.7	13.6	14.0	13.7	13.8	13.5
RoCE (post-tax)	6.4	7.4	9.1	9.4	9.2	9.5	9.5
RoIC (post-tax)	5.2	6.3	8.0	8.5	8.3	8.8	9.0
Working Capital Ratios							
Fixed Asset Turnover (x)	0.3	0.4	0.5	0.5	0.5	0.5	0.5
Asset Turnover (x)	0.3	0.4	0.4	0.4	0.4	0.4	0.4
Debtor (Days)	68	55	60	62	73	58	51
Leverage Ratio (x)							
Net Debt/EBITDA	4.8	4.3	3.8	3.4	3.3	3.0	2.7
Debt/Equity	1.1	1.5	1.4	1.3	1.2	1.0	0.8

Source: Company, MOFSL

Cash Flow Statement (INR m)

Y/E March	2017	2018	2019	2020	2021	2022E	2023E
EBITDA	**27,845**	**29,991**	**33,867**	**35,355**	**36,100**	**36,128**	**36,804**
WC	-918	-6,336	-9,779	1,580	-2,000	3,876	1,511
Others	3,081	4,393	7,731	2,185	1,520	0	0
Direct taxes (net)	-3,457	-3,727	-3,168	-2,461	-3,200	-3,269	-3,239
CF from Op. Activity	**26,552**	**24,321**	**22,939**	**30,033**	**28,180**	**36,735**	**35,076**
Capex	-14,720	-8,944	-8,317	-7,410	-6,750	-7,674	-7,679
Interest income	375	311	340	315	340	0	0
Investments	-634	568	0	0	0	0	0
Others	1,064	-7,695	845	984	-2,050	2,285	2,078
CF from Inv. Activity	**-13,915**	**-15,760**	**-7,133**	**-6,112**	**-8,460**	**-5,390**	**-5,600**
Share capital	158	22	0	0	0	0	0
Borrowings	8,622	854	-1,246	-4,892	210	-8,334	-9,581
Finance cost	-15,036	-13,828	-13,336	-13,306	-11,780	-12,556	-11,694
Dividend	-1,599	-1,902	-2,790	-3,188	-5,940	-6,284	-6,973
Others	256	365	0	86	0	0	-1,234
CF from Fin. Activity	**-7,599**	**-14,490**	**-17,373**	**-21,299**	**-17,510**	**-27,174**	**-29,482**
(Inc)/Dec in Cash	**5,037**	**-5,928**	**-1,566**	**2,623**	**2,210**	**4,172**	**-6**
Opening balance	17,894	22,931	17,003	15,437	18,060	20,270	24,442
Closing balance	**22,931**	**17,003**	**15,437**	**18,060**	**20,270**	**24,442**	**24,436**

Source: Company, MOFSL

Explanation of Investment Rating	
Investment Rating	**Expected return (over 12-month)**
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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