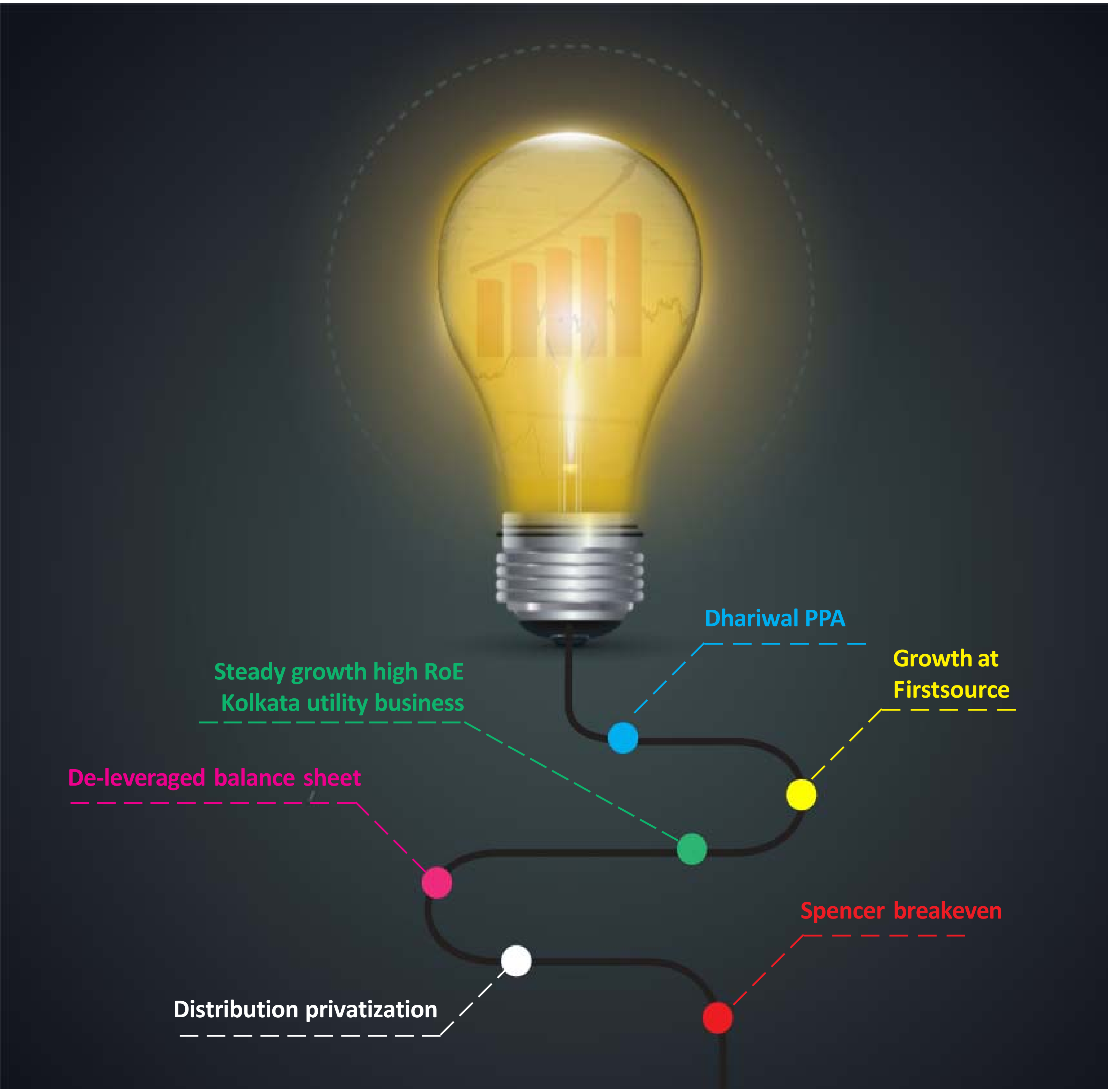
Initiating Coverage | 10 November 2016
Sector: Utilities

CESC



Best fully integrated power DISCOM

Dhruv Muchhal (Dhruv.Muchhal@MotilalOswal.com); +91 22 6129 1549
Sanjay Jain (SanjayJain@MotilalOswal.com); +91 22 6129 1523

Contents: CESC | Best fully integrated power DISCOM

CESC

BSE Sensex	S&P CNX
27,591	8,544

CMP: INR599 **TP: INR940 (+57%)** **Buy**

Stock Info

Bloomberg	CESC IN
Equity Shares (m)	133.2
52-Week Range (INR)	683 / 405
1, 6, 12 Rel. Per (%)	-3/5/6
M.Cap. (INR b)	79.8
M.Cap. (USD b)	1.2
Avg Val, INRm	238.6
Free float (%)	50.08

Financial Snapshot (INR b)

Y/E Mar	2016	2017E	2018E
Sales	119.0	135.6	147.7
EBITDA	28.5	31.6	34.6
NP	3.7	5.4	8.6
EPS (INR)	27.8	40.9	64.7
EPS Gr. (%)	86.6	47.1	58.4
BV/Sh. (INR)	470.5	431.9	484.6
RoE (%)	6.0	9.1	14.1
RoCE (%)	9.1	9.8	11.0
P/E (x)	17.0	14.6	9.2
P/BV (x)	1.0	1.4	1.2

Shareholding pattern (%)

As On	Jun-16	Mar-16	Jun-15
Promoter	49.9	49.9	49.9
DII	18.2	19.1	14.1
FII	23.5	22.6	26.6
Others	8.4	8.4	9.4

FII Includes depository receipts

CESC

Best fully integrated power DISCOM

+91 22 3027 8033
Dhruv.Muchhal@motilaloswal.com
Please click here for Video Link

Best fully integrated power DISCOM

EPS CAGR of 30%; Initiating with Buy and TP of INR940

RoEs and profits to double led by asset sweating

CESC is primarily an integrated electricity generation, transmission and distribution company. Its recent diversification into independent power generation (Dhariwal), organized retail (Spencer) and business process management (Firstsource) entailed significant investments, which compressed consolidated RoE to single-digit over FY11-16. However, the earnings outlook has improved with commissioning of generation assets, signing of PPAs, reducing losses at Spencer and growth at Firstsource (FS). We expect RoE and PAT to more than double to ~14% and INR8.6b, respectively, over FY16-18E.

High RoE in distribution business

CESC's integrated electricity distribution business in West Bengal is its key strength and major value driver. While normative returns are 15-16%, the distribution business is able to generate high RoEs of +25% via operating (attractive AT&C incentives) and capital (customer advances) efficiencies.

Distribution and Firstsource as growth drivers

New customer additions and upgradation of infrastructure are the key growth drivers of its regulated distribution business. Over FY16-20, we expect regulated equity CAGR of ~7% and Firstsource PAT CAGR of ~14%.

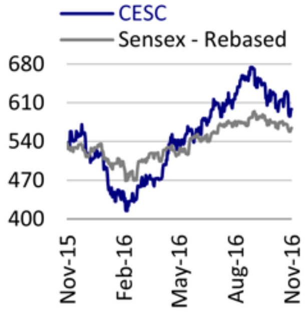
Reducing losses at Dhariwal and Spencer to boost RoE

Dhariwal's losses have started reducing with operationalization of the 100MW Tamil Nadu PPA at end-FY16. Another 187MW PPA with Noida is expected to become operational by 3QFY17. Besides this, 300MW may remain unsold for next few years until the demand-supply gap is bridged. Losses at Spencer too have started declining due to the focus on consolidation (rather than growth) and operational efficiencies. GST should also be beneficial, in our view.

Opportunity: Privatization of power distribution

The Indian power distribution system with INR3.9t of revenues is incurring heavy operating losses under state governments' control. With banks no longer funding losses, DISCOMs will have to take various measures (including partial privatization) to turn around under the 'UDAY' scheme. This is big opportunity for CESC, which is one of handful players with a proven track record. Notably, it has recently won the privatization rounds in Kota and Bharatpur.

Stock Performance (1-year)



Initiating with Buy; SOTP-based valuation at INR940

CESC is one of the few private sector power companies with strong earnings growth visibility, healthy FCF generation and strong balance sheet. Profit and RoE are expected to more than double in two years. While distribution and FS are the key business growth drivers, we believe reducing losses at Dhariwal and Spencer will boost RoE.

At current market price, the stock is trading at attractive 11% FCF yield, ~1.2x P/BV and 9.2x P/E on FY18E. Valuations are compelling in light of 30% EPS CAGR and recovery in RoE from 6% to 14% over FY16-20E.

We value the standalone regulated business at INR603/share based on 10.6x P/E, considering RoE, cost of equity and growth. Since cash flows are structured for the power generation businesses of Haldia and Dhariwal, we value them on INR164 and INR5/share based on DCF.

Spencer is a loss-making business currently, and we have thus valued it at 0.4x EV/sales or INR27/share. FS is valued at 9x P/E or INR141/share. Other businesses (comprising shopping mall, real estate, sports and renewables) are valued at EV/EBITDA of 6x. Thus, **we value the stock at INR940 on SOTP, with a Buy rating**.

CESC target price derivation

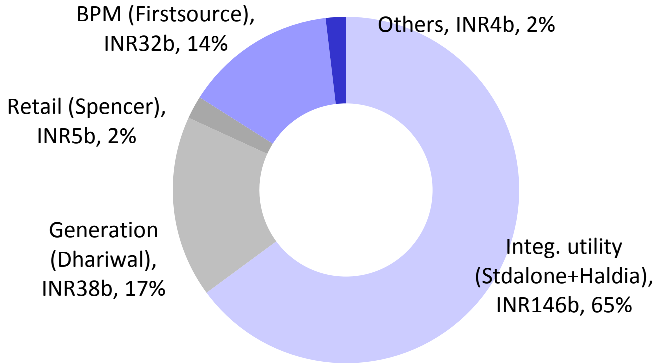
	Business	Method	CoE (%)	Sus. Gr. (%)	RoE FY17-20E (%)	Valuation Multiple (x)	Base Value	Stake %	EV INR m	Debt & Eq. cont. INR m	Value INR m	Value INR/sh.
a. Power business									**212,393**	**109,451**	**102,942**	**773**
Standalone	Gen. & distribution	PE FY18E	11.6	5.0	16.8	10.6	7,549	100.0	125,255	44,864	80,391	603
Haldia	Gen. & transmission	DCF based	11.6					100.0	50,050	28,207	21,843	164
Dhariwal	Generation	DCF based	11.6					100.0	37,089	36,380	709	5
b. Spencer	**Retailing**	**EV/sales FY18E**				**0.40**	**23,063**	**100.0**	**9,225**	**5,674**	**3,551**	**27**
c. Firstsource	**Business process o/s**	**PE FY18E**				**9.0**	**3,755**	**55.5**	**36,114**	**2,318**	**18,771**	**141**
d. Others	**Mall/renewable & others**	**EV/EBITDA FY18E**				**6.00**	**908**	**100.0**	**5,448**	**3,346**	**2,102**	**16**
Less: Cricket loss											**-1,000**	**-8**
TP		**Rounded**										**940**

Executive summary

CESC began operations as an integrated electricity utility (standalone and Haldia), and later diversified into independent generation (Dhariwal), organized retailing (Spencer), business process management solutions (Firstsource) and other businesses (malls, renewables, etc.). It holds ~55% stake in Firstsource.

~80% of CESC's capital is invested in power generation and distribution business

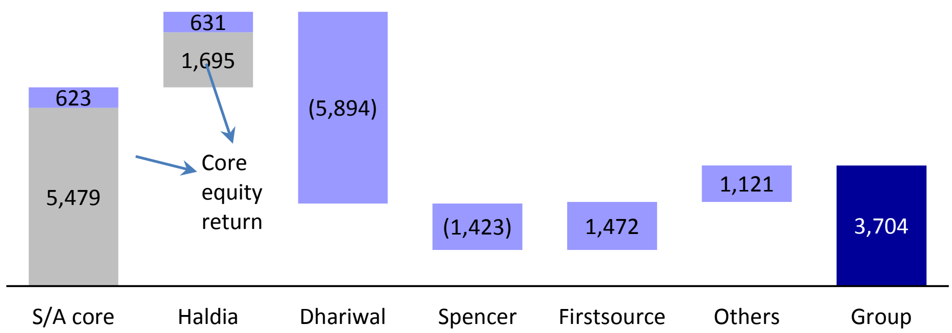
Exhibit 1: CESC's invested capital by businesses and as share of total (FY16)



Source: MOSL, Company

PAT was dragged by loss of INR5.9b at Dhariwal and INR1.4b at Spencer

Exhibit 2: CESC group FY16 PAT – INR m

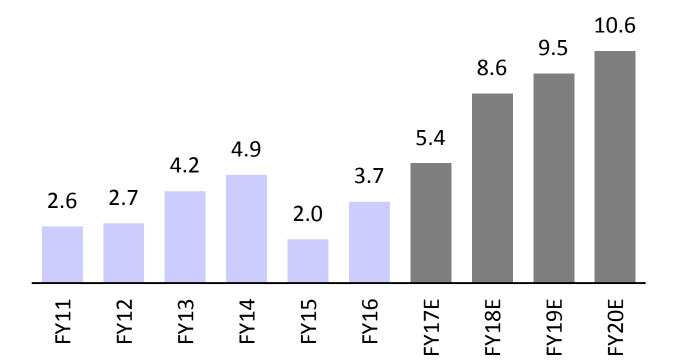


Source: MOSL, Company

We expect CESC's consolidated PAT to more than double from INR3.7b in FY16 to INR8.5b in FY18E (and to INR10.5b by FY20E), led by commencement of long-term power supplies at Dhariwal for part of capacity and growth at Firstsource. The estimated decline in losses at Spencer should also contribute, but to a certain extent. The integrated utility business is a steady 6-8% growth business.

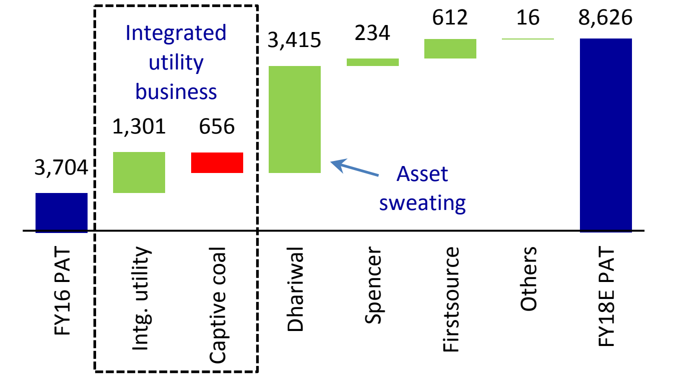
We build annual INR0.7b impact from FY17 onwards for the captive coal block, which offsets part of the growth. We believe the remaining untied capacity at Dhariwal (~300MW) is unlikely to secure long-term contracts at least until FY20E due to its exposure to the surplus Maharashtra region (we build in only 50% PLF for the plant until FY20E). Breakeven at Spencer is estimated only by FY20E.

Exhibit 3: CESC's attributable PAT to double – INR b



Source: MOSL, Company Data

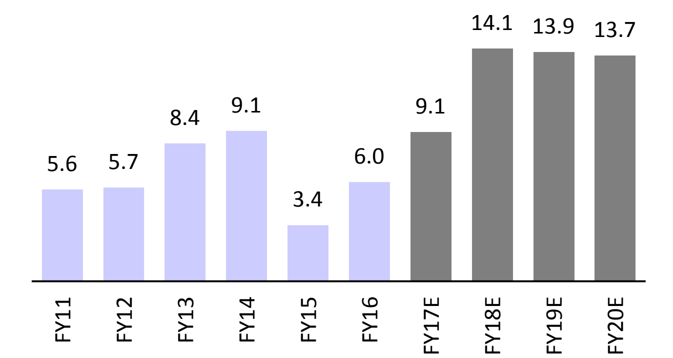
Exhibit 4: Drivers of PAT for CESC – INR m



Source: MOSL, Company Data

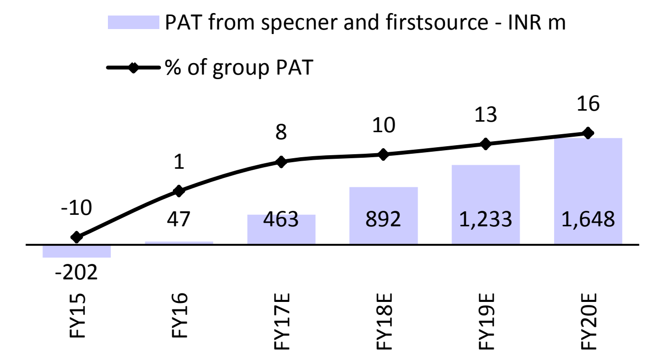
Doubling of PAT should lead to a significant increase in RoE from subpar 3-9% levels over FY11-16 to ~14% over FY17E-20E, given that it would come from sweating of assets commissioned over last few years and an increase in contribution to PAT from less capital-intensive businesses (Spencer and Firstsource) from ~1% in FY16 to ~16% in FY20E. The likely commencement of power supplies under long-term contracts for part of capacity at Dhariwal would drive better asset utilization.

Exhibit 5: CESC's RoE (%) to double



Source: MOSL, Company

Exhibit 6: Share of profit from less capital-intensive business

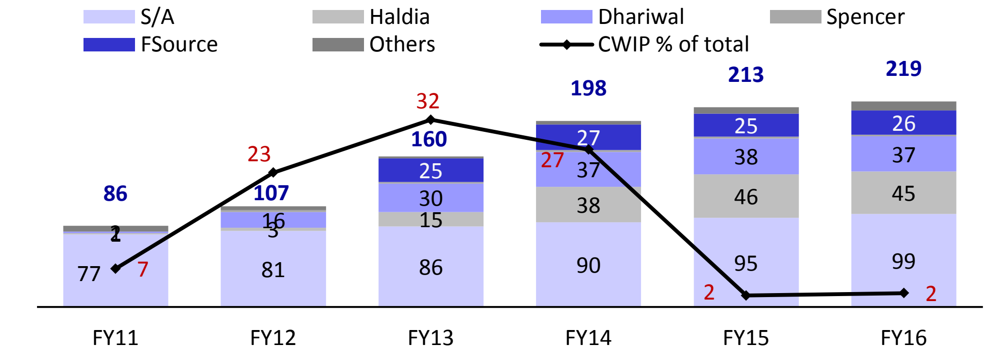


Source: MOSL, Company

CESC's subpar RoE performance in past five years was on account of the heavy investment phase, when its asset base more than doubled. Utilization of these new generation assets was low due to the oversupplied power market. In FY13, it diversified into Firstsource, an under-performing business then. Returns were also impacted by continuing losses at Spencer due to slow improvement in its operating performance.

CESC's asset base more than doubled in last five years

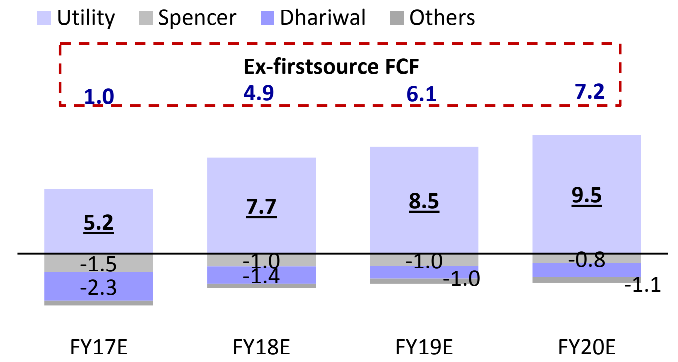
Exhibit 7: CESC's net fixed assets (incl. goodwill) and CWIP as % of total



Source: MOSL, Company

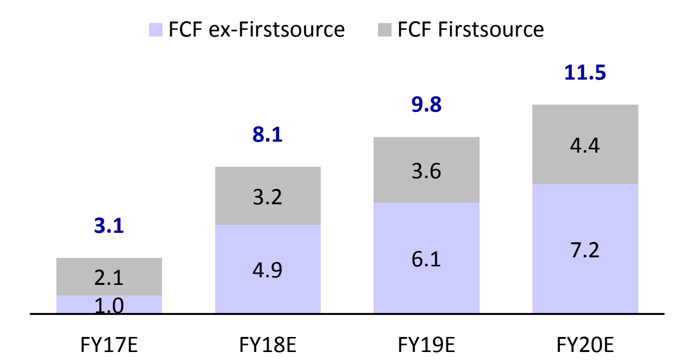
We estimate CESC to generate annual FCF of ~INR3-11b (~4-14% of current market capitalization). This is after factoring in estimated cash losses of ~INR1-2b p.a. at Dhariwal (on account of unused capacity) and ~INR1-1.5b at Spencer. Strong cash generation in the utility and Firstsource businesses provides support to these underperforming operations and should help unlock value over the long term. It allows Dhariwal to wait for lucrative deals until the electricity market improves and facilitates funding to Spencer.

Exhibit 8: Break-up of FCF ex-Firstsource – INR b



Source: MOSL, Company

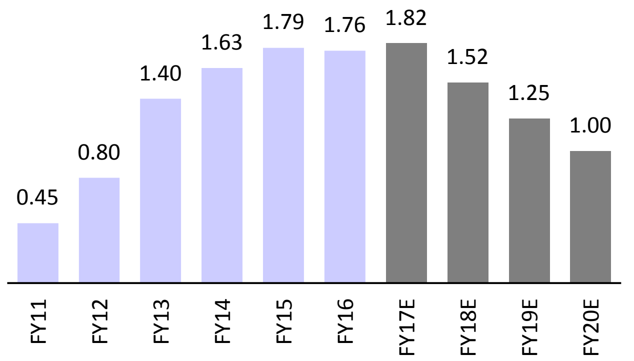
Exhibit 9: FCF from Firstsource and ex-Firstsource – INR b



Source: MOSL, Company

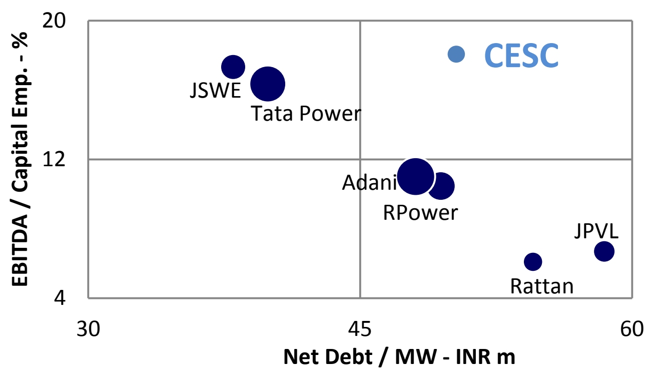
Predictability of cash flows at the utility business and growth at Firstsource also provide deleveraging visibility. We estimate net debt-to-equity to decline from an already healthy 1.8x in FY16 to 1.0x by FY20. We believe CESC is one of the few private sector utility companies with balance sheet strength to pursue inorganic growth opportunities.

Exhibit 10: Net debt-to-equity (x)



Source: MOSL, Company

Exhibit 11: CESC's has one of the best balance sheets



Source: MOSL, Company

Although CESC has grown via diversification into other businesses in the past, we see the gradual privatization of the electricity distribution sector in India as a key growth driver. The market is more than INR3.9t in size, but highly inefficient with operating losses of more than INR0.5t. CESC is one of the few players in India with experience in distribution. It recently won the bid for the privatization of Kota and Bharatpur in Rajasthan, and has started operations there from September 2016.

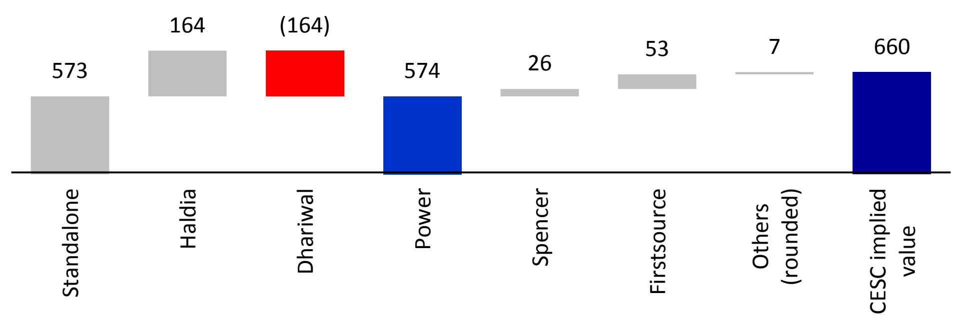
Initiating with Buy and TP of INR940

CESC's PAT/RoE is estimated to double in two-years while earnings growth would continue on steady growth in its integrated utility business. CESC's exposure to electricity distribution, being one of the few, places it favorable to other private sector companies operating in over-supplied generation sector. FCF generation is estimated to be healthy at ~INR11b p.a. over FY17-20E – an FCF yield of ~11%.

For ~14% RoE and steady growth the stock currently trades at ~1.2x FY18E. The current valuations do not factor the long-term value potential of the untied capacity at Dhariwal and potential at Spencer. At current stock price the market is probably factoring that Dhariwal would remain under-utilized (continue to operate at 50% PLFs) over its life.

At current stock price, the market is probably factoring in that Dhariwal would perpetually remain at 50% PLF

Exhibit 12: What is CESC's current stock price probably implying



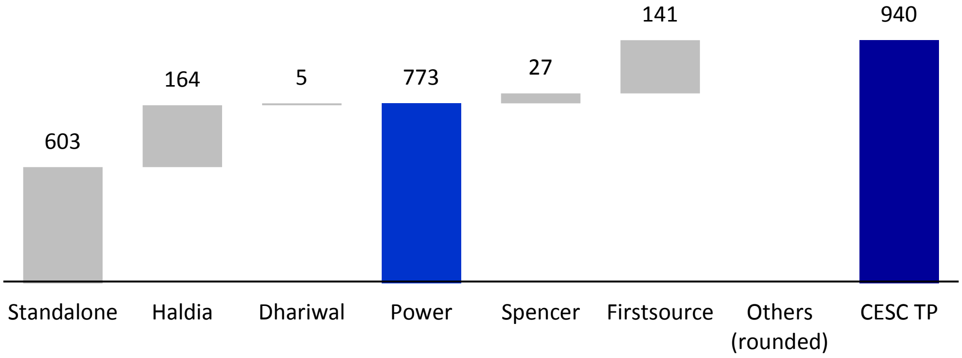
Source: MOSL, Company

While currently loss making, Dhariwal and Spencer have long-term value potential. Generation market will start to balance by FY20-21 while organized retail is maturing in India. CESC with its balance sheet strength has the ability to play the cycle. This, in our view deserves premium.

We value CESC on SOTP – mix of DCF and relative – as it best captures the long-term value potential of the various businesses. Moreover, earnings mix is expected to diversify from ~1% of consolidated PAT in FY16 coming from less capital intensive business (Spencer and Firstsource) in FY16 rising to ~16% by FY20.

Power business represents ~75% of our target value

Exhibit 13: CESC's target price build-up – INR/share



Source: MOSL, Company

While not captured in our valuation, we believe CESC also offers one of the best plays on the privatization of electricity distribution sector in India. It has more than 100 years of experience in the sector and is amongst the few players in the sector. Notably, it recent won the privatization round at Kota and Bharatpur.

Our SOTP based target price is INR940/sh. Power business represents ~80% of our target value. The implied P/BV is 1.9x FY18E. We initiate coverage on CESC with Buy rating with an upside of ~60%.

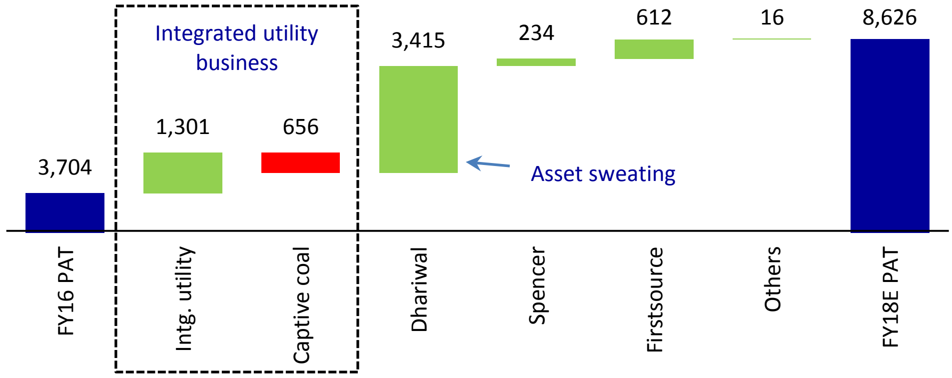
Key risk: (a) Slower-than-expected electricity demand growth in its distribution license area leading to moderation in distribution capex investment, (b) Delay in commissioning of the Noida PPA at Dhariwal and (c) Impact of 'Brexit' on Firstsource – derives ~40% of revenues from UK.

Profit to double in two years led by asset sweating

We estimate CESC's attributable PAT to double in two years, from INR3.7b in FY16 to INR8.6b in FY18, driven by the full benefit of ~300MW long-term supply contracts at Dhariwal and growth at Firstsource. Spencer's performance is also estimated to improve but remain in red. The ~INR0.7b impact from the penalty related to the captive coal block would offset part of the growth at its integrated utility business in FY17. Excluding this impact, we estimate utility business PAT to grow at a steady ~6-8%.

Sweating of assets (supply under PPAs starting) and growth at Firstsource to aid profitability

Exhibit 14: PAT doubling in two years – INR m



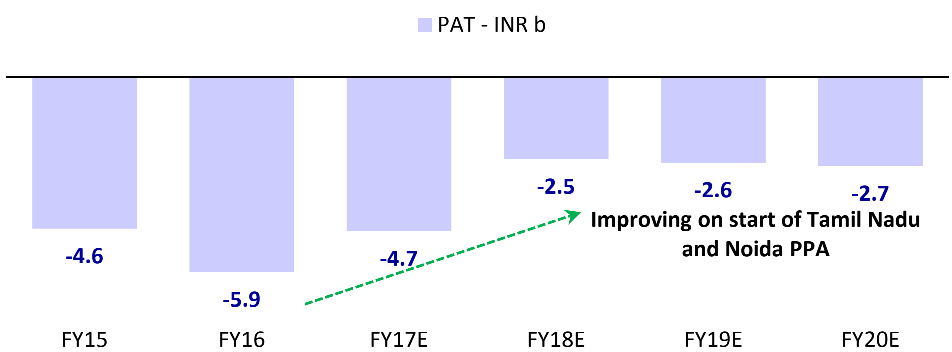
Source: MOSL, Company

Losses at Dhariwal to halve led by commencement of Noida supplies and full benefit of Tamil Nadu contract

From EBITDA loss of INR0.7b in FY16, we estimate Dhariwal to turn EBITDA positive with INR3.1b in FY18. Although the power plant was commissioned in FY15, operations were constrained due to the lack of transmission network, fuel linkage and PPAs. We expect supply of 50% of capacity under long-term contracts to commence before end-FY17, with full benefits visible from FY18E. The remaining 50% capacity is connected to the surplus state of Maharashtra, where supplies would be difficult, in our view. We estimate the plant to run at not more than 50% PLF over FY17E-20E. However, with the start of PPAs, net loss would reduce from INR5.9b in FY16 to INR2.5b in FY18E.

Dhariwal losses are estimated to more than halve on start of Noida PPA and full benefit of Tamil Nadu PPA

Exhibit 15: Dhariwal net loss – INR b



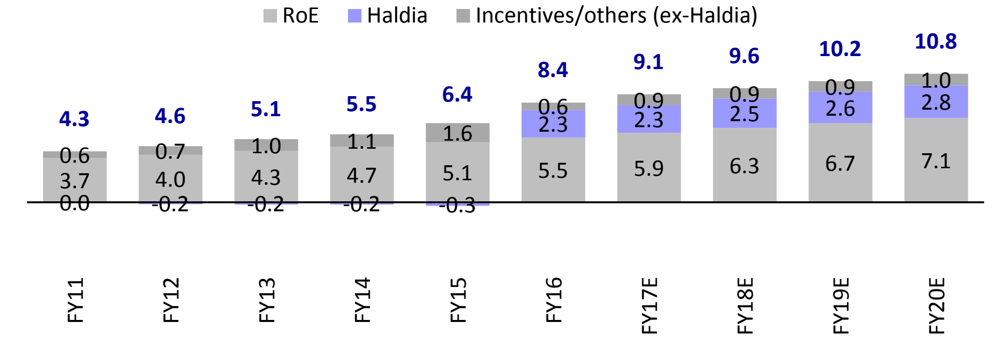
Source: MOSL, Company

Integrated electricity utility business at Kolkata to deliver steady 6-8% earnings growth

Electricity demand growth drives earnings in the integrated electricity utility business of Kolkata (including Haldia) in the form of capex and incentives/savings, which are a factor of units sold. We estimate ~3-4% growth in peak demand (v/s. 4.3% CAGR over FY10-16 and guidance of ~4.5%). Regulated equity base is estimated to grow at ~7% CAGR over FY16-20 v/s ~8% over FY10-16 on demand/customer growth led distribution capex. We estimate ~INR0.8b p.a. (pre-tax) impact from the unreasonable bid for the captive coal block. We view the Kolkata business as a stable 6-8% annual growth business. Excluding the impact of the captive coal block, we estimate PAT to grow from INR8.4b in FY16 to INR9.6b by FY18, implying annual growth of ~7%.

Integrated utility business (ex-captive coal block impact) to grow steadily by 6-8% p.a.

Exhibit 16: Integrated utility PAT (standalone + Haldia) ex-captive block impact – INR b



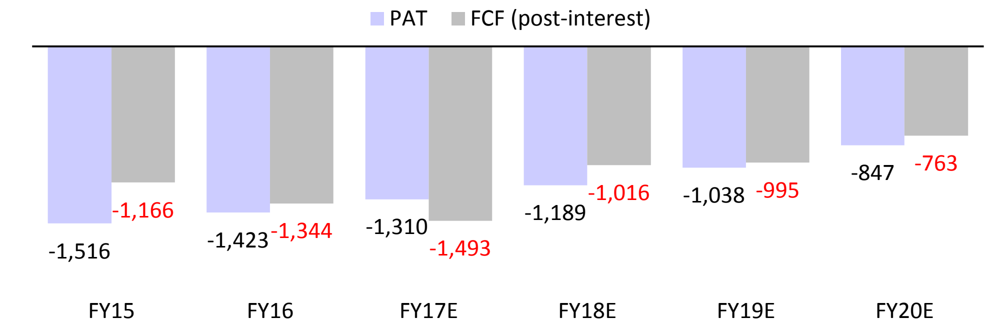
Source: MOSL, Company

Spencer to become operating breakeven by FY20

Looking at Spencer's performance v/s other organized retail players whose data are available and comparable, we find that Spencer has higher unit sales and broadly similar gross margins. However, overheads are high, which leads to EBITDA losses. Management is rightly focused on rationalizing non-profitable stores, increasing unit sales and optimizing cost. We estimate 190bp improvement in EBITDA margin to negative 1.3% by FY18, led by lower 'non-store overheads'. We expect Spencer to turn EBITDA positive by FY20E (which is conservative compared to management's guidance of FY18E). PAT loss is estimated to decline from INR1.4b in FY16 to INR1.2b in FY18E (and INR0.8b by FY20E).

Losses to decline on rationalization of non-profitable stores, increasing unit sales and cost optimization

Exhibit 17: Spencer losses – INR b

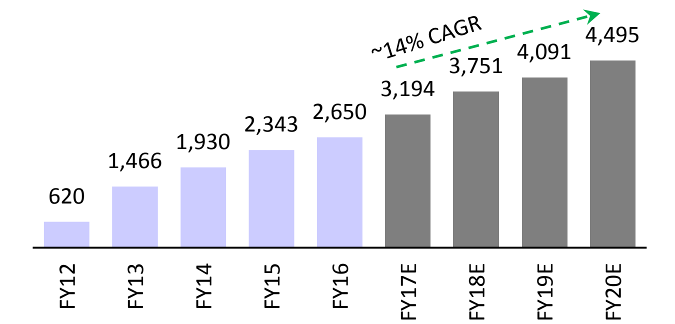


Source: MOSL, Company

Strong profit growth and FCF generation at Firstsource

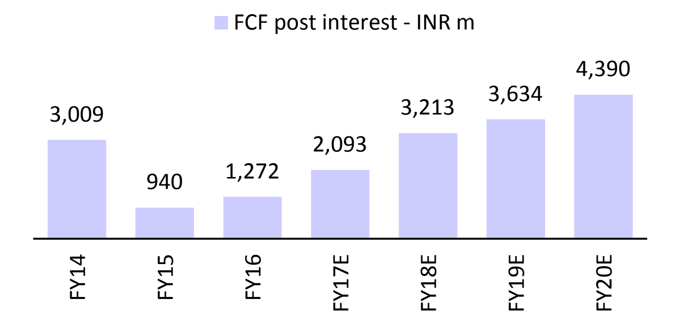
Previously an underperforming debt-laden business when acquired in FY13, Firstsource has improved considerably, with its PAT almost doubling in three years to INR2.6b in FY16 and net debt declining by ~INR4b to INR7.6b. We expect PAT growth of ~19% to INR3.7b over FY16-18E, and ~10% thereafter to INR4.5b by FY20E, led by the acquisition of ISGN, the sole partnership agreement with Sky and lower interest cost. We estimate Firstsource to generate annual FCF (post-interest) of INR2-4b over FY17E-20E, representing close to half of the group's FCF.

Exhibit 18: Firstsource PAT – INR m



Source: MOSL, Company

Exhibit 19: Firstsource FCF – INR m

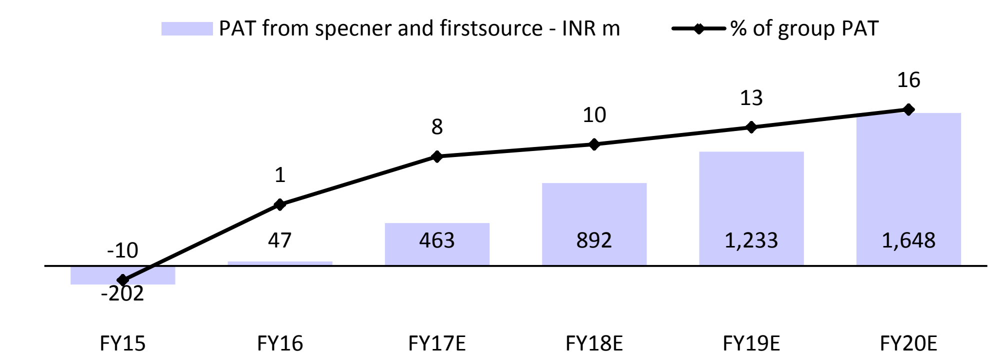


Source: MOSL, Company

Contribution from less capital-intensive businesses to improve

We estimate contribution of less capital-intensive Spencer (retail) and Firstsource (BPM) businesses to increase from ~1% of group PAT in FY16 to ~16% by FY20.

Exhibit 20: Share of group PAT from retail and IT



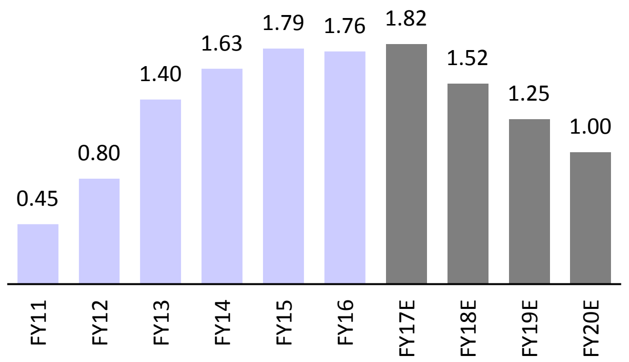
Source: MOSL, Company

Deleveraging visibility

CESC's utility business generates a predictable stream of cash flows due to its regulated nature. Firstsource FCF generation is estimated to increase led by operating profit growth and decline in interest cost. We estimate the utility business and Firstsource to generate annual FCF of ~INR5-9b and ~INR2-4b, respectively.

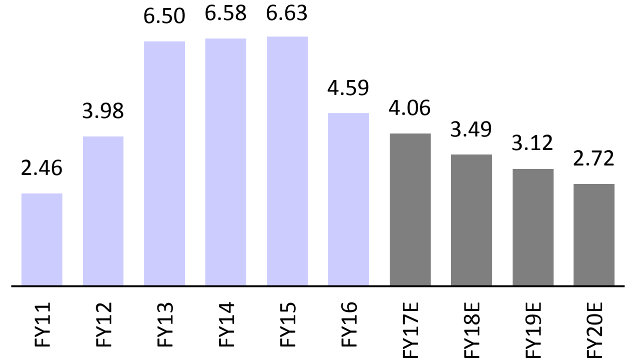
Predictability of cash flows of the utility business and growth at Firstsource provide strong visibility for balance sheet deleveraging. We expect net debt to equity to decline from an already healthy 1.8x in FY16 to 1.5x by FY18 and 1.0x by FY20. Net debt to EBITDA is estimated to improve from 4.6x in FY16 to 3.5x by FY18 and 2.7x by FY20.

Exhibit 21: Net-debt to equity (x)



Source: MOSL, Company

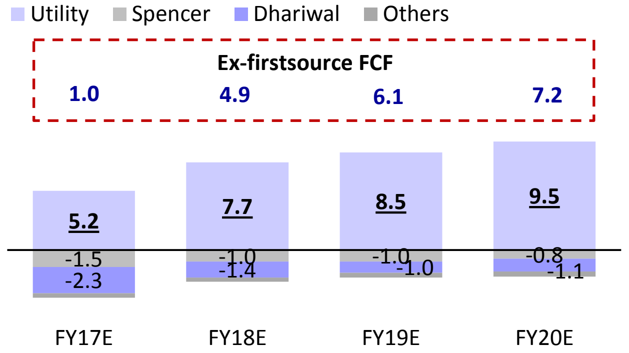
Exhibit 22: Net debt to EBITDA (x)



Source: MOSL, Company

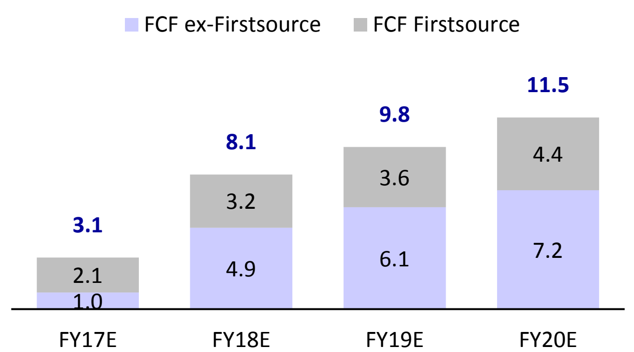
Strong cash generation in the utility business would also support Dhariwal's operations and Spencer's turnaround. We estimate Dhariwal to burn ~INR1.1-2.3b annually over FY17E-20E as the asset is likely to remain under-utilized. Spencer is estimated to burn ~INR0.8-1.5b annually until operating performance improves gradually. Balance sheet strength of the parent and healthy cash generation would help unlock value from these assets in the long term. Dhariwal will be able to wait for lucrative deals until the market balances and Spencer's turnaround can be funded due to the company's strong balance sheet positioning.

Exhibit 23: FCF ex-Firstsource – INR b



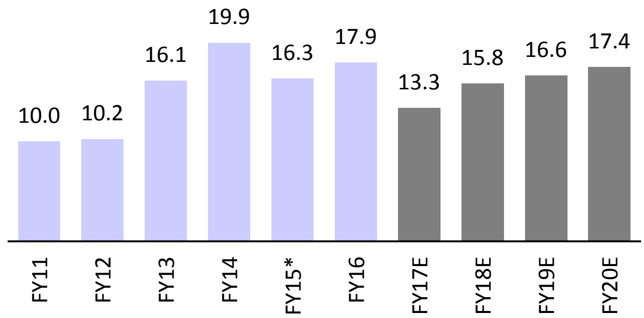
Source: MOSL, Company

Exhibit 24: FCF from Firstsource and ex-Firstsource – INR b



Source: MOSL, Company

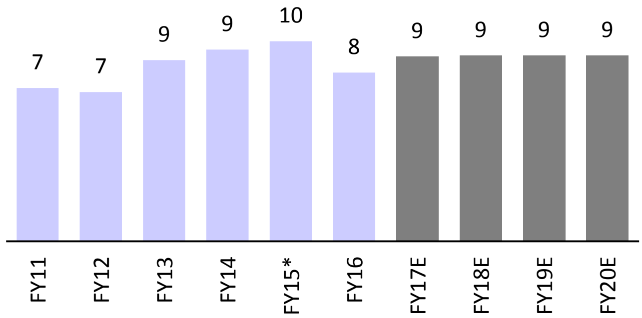
Exhibit 25: Utility business operations cash flows…



*Adj. for one-time payment of INR9b for captive

Source: MOSL, Company

Exhibit 26: …and capex – INR b

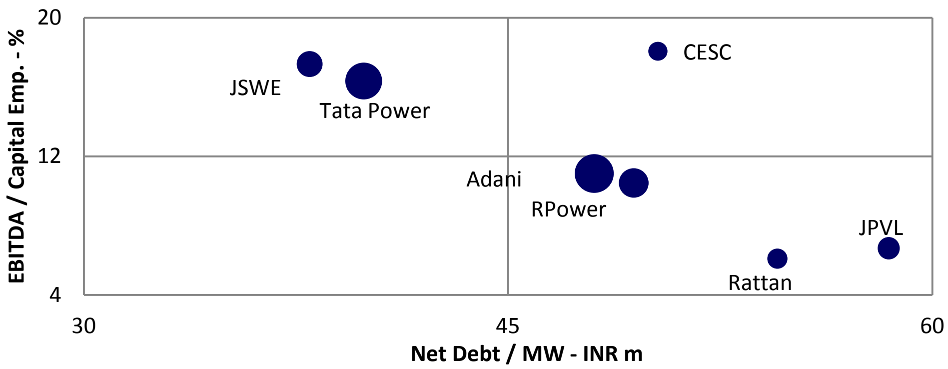


*Adj. for one-time payment of INR9b for captive

Source: MOSL, Company

We have identified CESC as one of the few private companies in the utility sector that has balance sheet strength to exploit inorganic growth opportunities.

Exhibit 27: Private sector power companies' balance sheet positioning



Source: MOSL, Company, Bloomberg

Integrated utility: Healthy cash-generating business

The integrated utility business includes Kolkata generation & distribution operations (standalone) and Haldia generation operations.

Standalone: +25% RoE business delivering steady growth

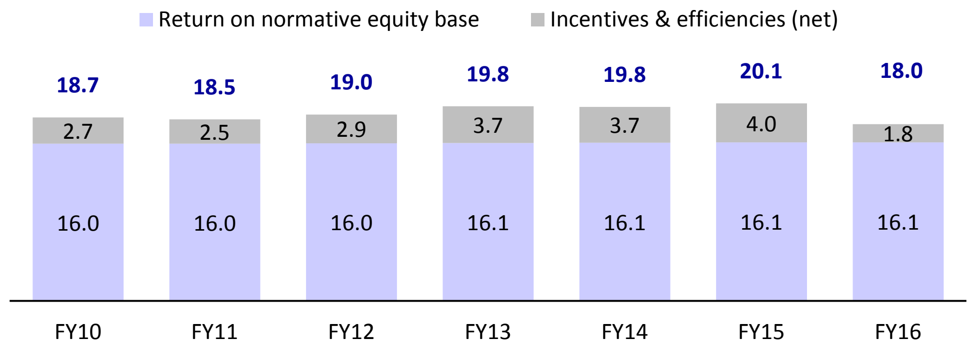
CESC has roots as an integrated electricity utility company. It is the sole distributor (although not exclusive) within a 567 sq. km area of Kolkata and Howrah in the state of West Bengal. It served ~3m customers, had a distribution network of ~21k ckm and integrated power generation capacity of 1,125MW as at end-FY16. The business works on a regulated return model. CESC's operating area is regulated by the West Bengal Electricity Regulated Commission (WBERC), which typically sets return and operating norms for a period of three years. The current block period is FY15-17.

Under the regulated return model, normative equity approved by the regulator is the key source of earnings. Normative equity (which is driven by capex), however, can be different from actual equity invested due to the nature of the business.

CESC is assured post-tax equity return of 15.5% in generation and 16.5% in distribution on normative equity. However, RoE on normative equity it generated over FY10-16 was ~18-20%. The top-up is from incentives and savings from efficient operations (performing better than the normative level set by the regulator).

Incentives and savings from efficient operations contributed ~2-4% of RoE (on normative equity base)

Exhibit 28: Standalone RoE build-up (on normative equity) – %

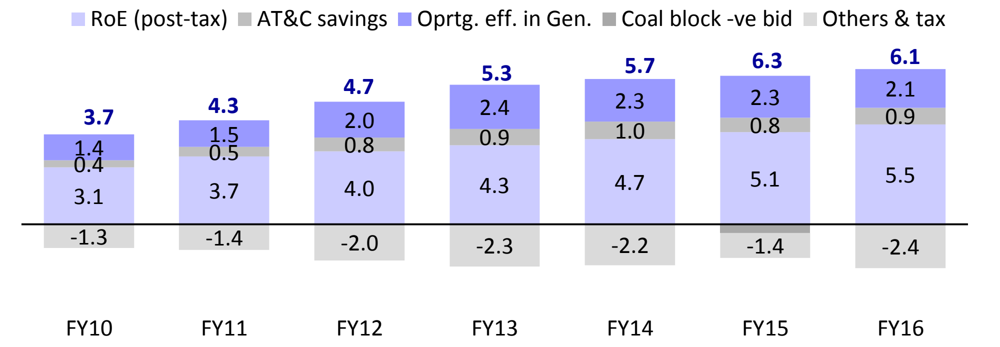


Source: MOSL, Company, Regulatory Filings

CESC's standalone core business PAT (i.e. excluding other income) grew at a CAGR of 8.9% to INR6.1b over FY10-16.

Efficient operations of generation plants and savings on AT&C losses contributed ~INR3b to core PAT of ~INR6b in FY16

Exhibit 29: Standalone – build-up of core (ex-other income) PAT – INR b



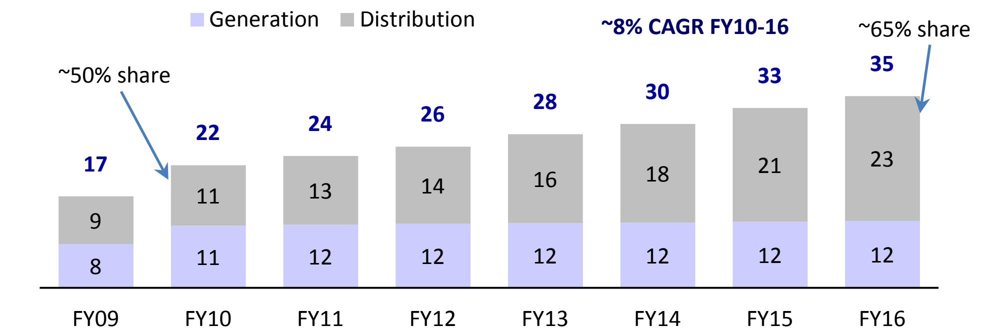
Source: MOSL, Company, Regulatory Filings

Key drivers of earnings over FY10-16 are estimated to be:

(a) Normative equity earnings (RoE earnings) CAGR of 9.8% to INR5.5b. Although normative equity recorded a lower 7.7% CAGR to ~INR35b over the period, there is an increase in the distribution business share (which earns higher RoE) in total normative equity of the standalone business from ~50% to ~65%.

Share of distribution business, which earns higher RoE of 16.5%, is estimated to have increased from 50% in FY10 to ~65% in FY16 in total normative equity of standalone business

Exhibit 30: Normative equity – INR b

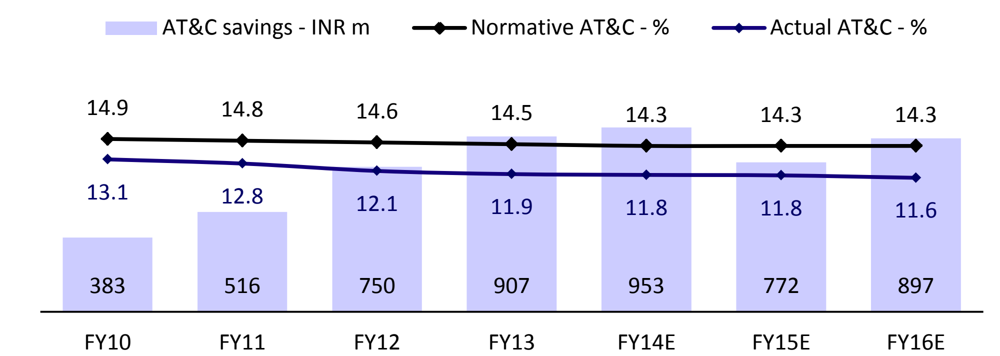


Source: MOSL, Company, Regulatory Filings

(b) Earnings from achieving lower-than-normative aggregate technical and commercial losses (AT&C) are estimated to have increased at a CAGR of ~14% to INR0.9b in FY16. Benchmark AT&C was 14.3%, while actual is estimated to be 11.6% in FY16. CESC earns cost of supply on units saved.

Earnings from AT&C efficiency are estimated to have increased at ~14% CAGR over FY10-16 to INR0.9b

Exhibit 31: Earnings from AT&C efficiency

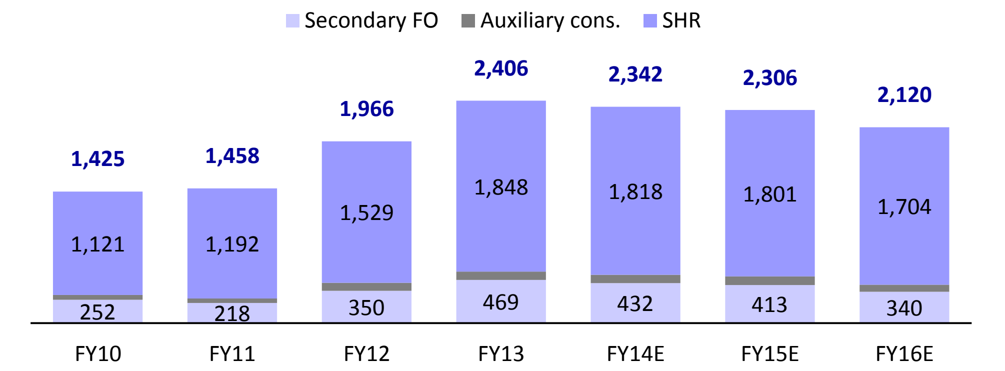


Source: MOSL, Company, Regulatory Filings

(c) Earnings from efficient operations of generation plants – better than normative level – are estimated to have increased at a CAGR of 6.4% to INR2.1b. Station heat rate (SHR) efficiency is the primary component. Fuel oil saving and lower auxiliary consumption are the other components.

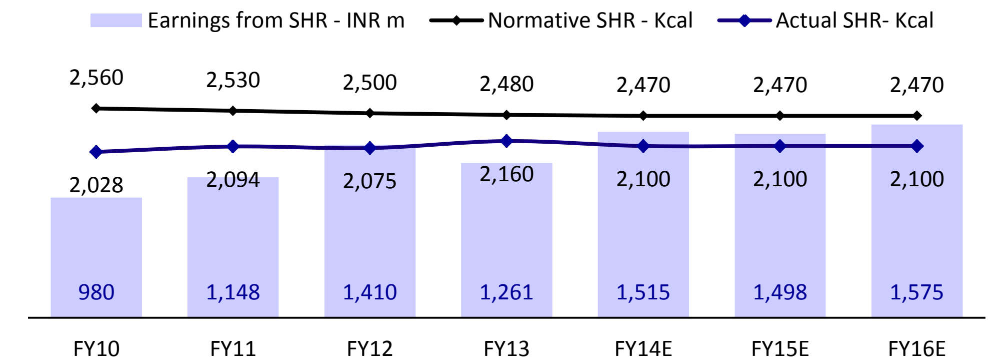
SHR is driven by Budge Budge power plant, which has SHR of ~2000-2,100kCal v/s normative of ~2,400-2,500kCal

Exhibit 32: Earnings from generating efficiencies – INR m



Source: MOSL, Company, Regulatory Filing

Exhibit 33: Budge Budge earnings from SHR (post 20% sharing in tariffs)



Source: MOSL, Company, Regulatory Filing

(d) Costs not allowed as pass-through in tariffs and certain corporate overheads offset part of growth from above components of earnings. Such costs – which increased at a CAGR of ~10% over FY10-16 – are estimated to have offset INR2.4b from core earnings in FY16.

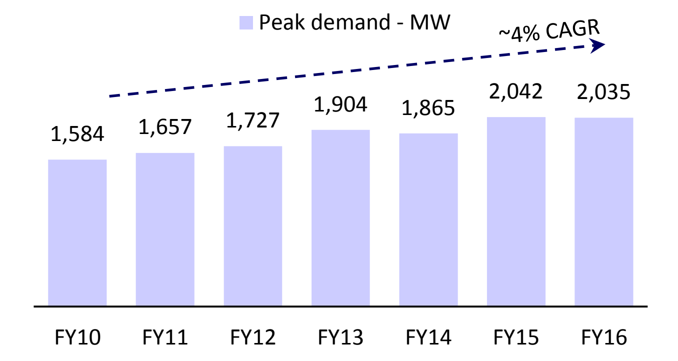
Normative equity to record ~7% CAGR over FY16-20E on demand growth

Electricity consumption growth in the company's distribution area, along with an increase in the customer base, is the key earnings driver, in our view. Demand growth drives (a) distribution capex, (b) AT&C earnings on higher volumes and (c) higher generation PLFs, which drive earnings from SHR, auxiliary and fuel oil as they are based on units generated.

Peak demand in CESC's distribution area has increased at a CAGR of 4.3% over FY10-16 to 2,035MW, and is guided to increase to 3,000MW by FY25, implying ~4.5% growth. Distribution network addition has seen a similar trend – network length has increased at ~4% CAGR and transformer capacity at ~6% CAGR over FY10-16. We estimate electricity demand in its distribution area to grow at ~3-4%. Normative equity base is estimated to grow at ~7% CAGR over FY16-20E (as against ~8% over

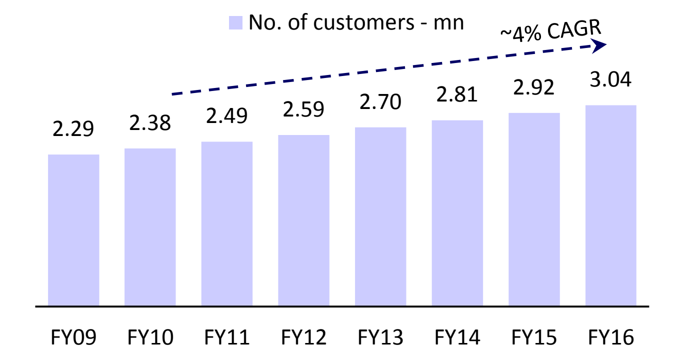
FY10-16) on demand/customer growth-led distribution investments. Normative equity from the distribution business is estimated to represent ~72% of total standalone normative equity by FY20.

Exhibit 34: Peak demand increased at ~4% CAGR…



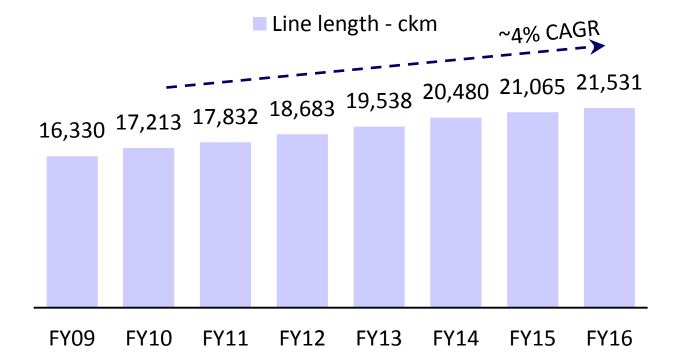
Source: MOSL, Company

Exhibit 35: …on increase in customer base



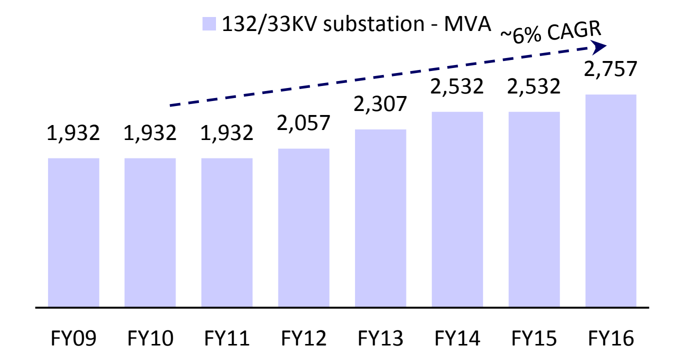
Source: MOSL, Company

Exhibit 36: …which drives investment in…



Source: MOSL, Company

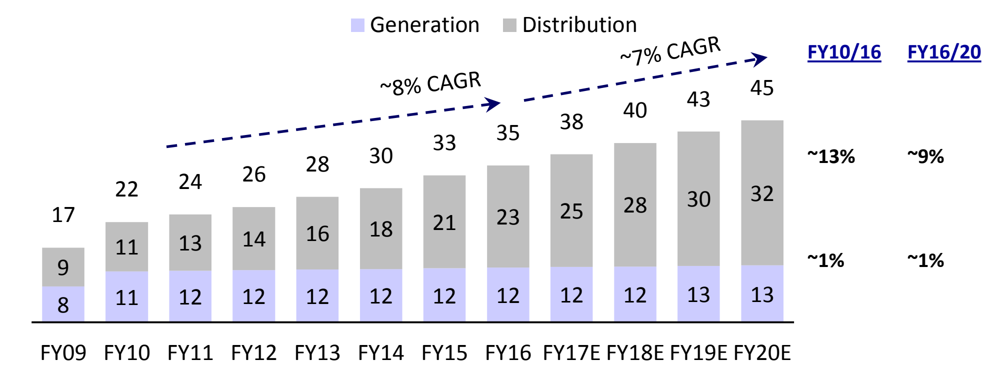
Exhibit 37: …distribution network



Source: MOSL, Company

Capex toward distribution following improving demand would drive normative equity higher

Exhibit 38: Normative equity estimated to grow at ~7% CAGR over FY16-20E



Source: MOSL, Company, Regulatory Filings

Unreasonable bid in coal block – around INR0.8b (pre-tax) annual impact

CESC bid a price of INR370/t to secure the Sarshatali captive coal block (CESC was the previous owner). The bid price (along with the mining cost) is not allowed as pass-through in tariffs leading to an annual impact of INR1.7b. CESC would be able to offset part of the impact through sale of middling (~INR0.3b) and sale of merchant power (INR0.6b). Mines won through bidding are allowed to use 15% of the coal for merchant power sales. We estimate margin of ~INR1/kWh on its merchant sales. Post-tax, we estimate the net annual impact due to the captive coal block is ~INR0.6b.

Exhibit 39: Impact (pre-tax) of negative bid in Sarshatali captive coal block

		FY17E	FY18E	FY19E	FY20E
Impact of Sarisatolli coal block	INR m	-830	-830	-830	-830
Coal production	mt	2.2	2.2	2.2	2.2
Bid price (negative bid)	INR/t	370	370	370	370
Mining cost	INR/t	400	400	400	400
Realn. From sale of midlings	INR/t	1,000	1,000	1,000	1,000
Midling volumes	mt	0.34	0.34	0.34	0.34
Merchant power sales	INR m	561	561	561	561
Gain per unit	INR/kWh	1.0	1.0	1.0	1.0

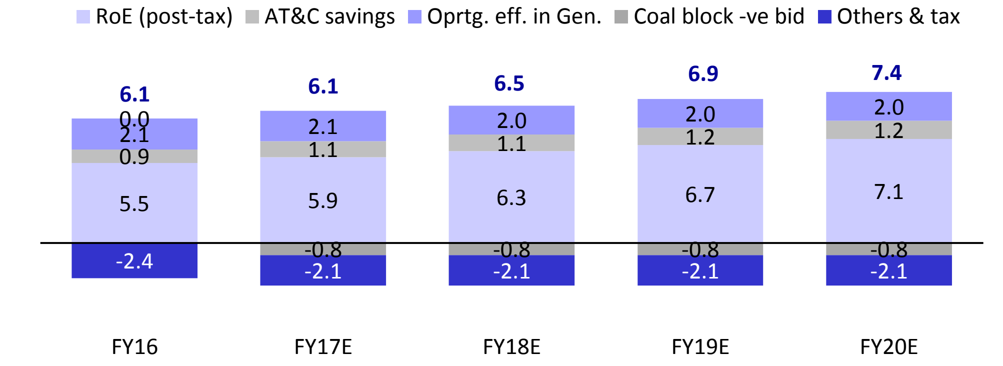
Source: MOSL, Company

Standalone core PAT to grow at 5% over FY16-20E

We estimate standalone core business PAT to grow at ~5% CAGR to INR7.4b over FY16-20E led by capex and increase in incentives, partly offset by the impact of captive coal block. Sustainable RoE on normative equity is estimated to reduce from a run-rate of 18-20% to 16-17% due to the drag from the captive coal block.

We expect ~5% CAGR growth in standalone core business PAT over FY16-20E on capex and incentive income due to higher volumes.

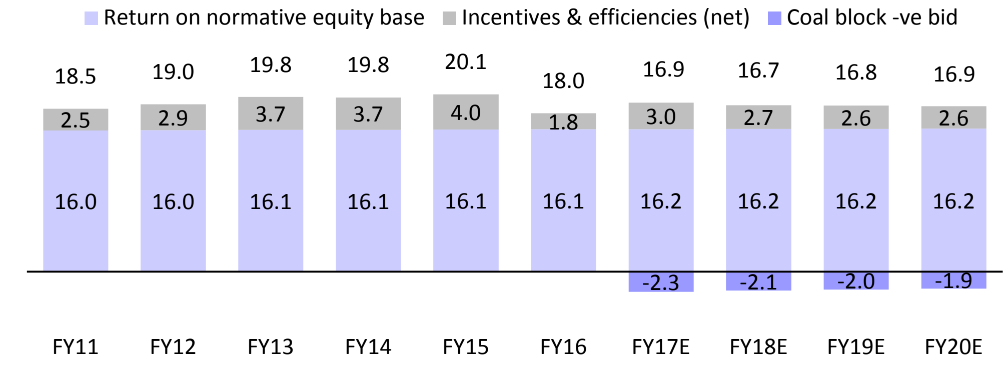
Exhibit 40: Standalone: Core PAT build-up – INR b



Source: MOSL, Company

Sustainable returns on normative equity to decline from ~18-20% to ~16-17% due to captive coal block

Exhibit 41: Standalone: Returns on normative equity – %



Source: MOSL, Company

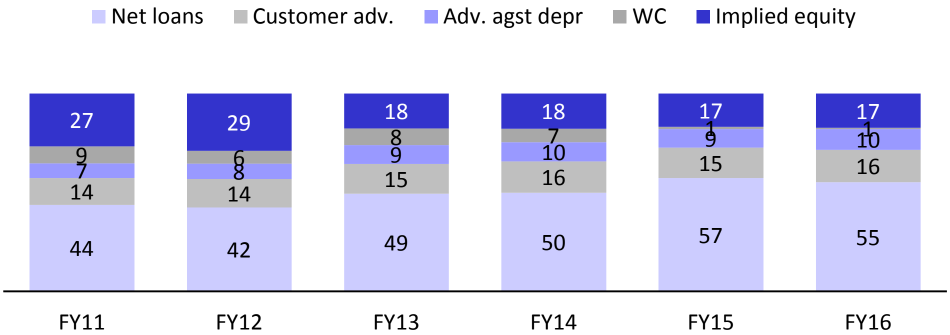
Capital structure advantage drives higher-than-normative RoEs

At standalone level, CESC operates on a regulated business model, which requires minimum 70% debt for capex. However, the nature of the distribution business (sticky customer deposits) allows the company to cheaply leverage more than the normative levels. Thus, while it earns return on normative equity, actual equity invested in business is lower. Customer deposits represented ~16% of invested capital in FY16. We expect CESC to generate RoE (on equity actually invested) of +20% (as against 16-17% calculated on normative equity) due to higher leverage.

Over last five years, deposits per customer have grown at ~6% to reach INR5,288 in FY16. We estimate ~3% annual growth over our forecast period. Incremental deposits are estimated to represent ~10-20% of its annual capex, a cheap source of leverage.

Cheap cost customer deposits represented ~16% of invested capital, allowing more than mandated leverage and earning RoEs higher than implied by normative equity

Exhibit 42: Sources of funds in standalone core business – %



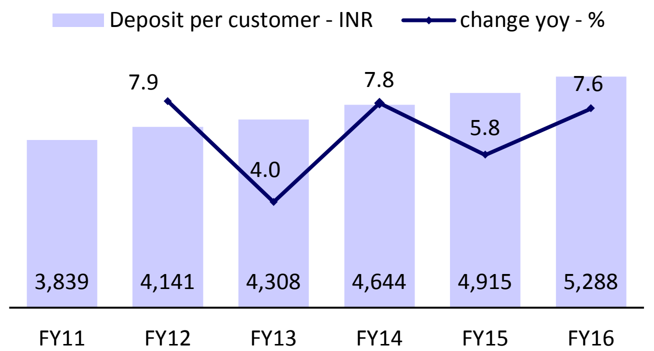
Source: MOSL, Company

Exhibit 43: Standalone core RoE (on actual equity invested) – INR m

	FY11	FY12	FY13	FY14	FY15	FY16	FY17E	FY18E	FY19E	FY20E
Standalone net worth	**55,692**	**60,118**	**64,950**	**70,386**	**80,799**	**86,356**	**82,918**	**88,868**	**95,345**	**102,362**
Adj.										
Investments	10,843	11,332	21,779	31,911	42,493	46,466	50,006	52,466	54,466	56,366
Adv. to subs/associates	9,677	10,820	11,892	11,346	12,023	12,330	12,330	12,330	12,330	12,330
Cash	8,388	8,598	7,714	2,006	7,377	8,366	6,217	7,359	9,440	12,216
Core business net worth	**26,784**	**29,368**	**23,564**	**25,124**	**18,906**	**19,194**	**14,305**	**16,714**	**19,109**	**21,450**
Core PAT	**4,295**	**4,733**	**5,332**	**5,731**	**6,307**	**6,102**	**6,126**	**6,496**	**6,949**	**7,405**
Core RoE (on actual equity) - %	**16.0**	**16.9**	**20.1**	**23.5**	**28.6**	**32.0**	**36.6**	**41.9**	**38.8**	**36.5**

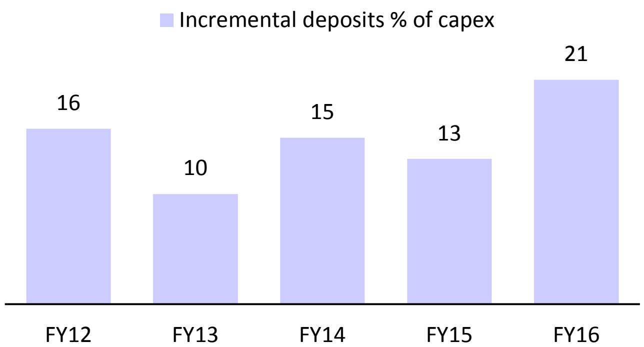
Source: MOSL, Company

Exhibit 44: Deposit per customer and growth



Source: MOSL, Company

Exhibit 45: Incremental deposits to capex – %

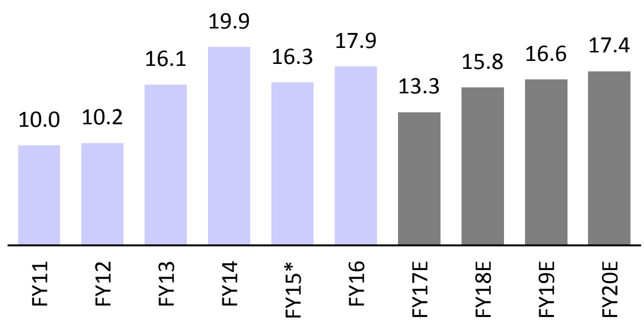


Source: MOSL, Company

Steady and predictable cash flow business

The regulated nature of the business and expectations of electricity demand growth in its operating areas make cash flows steady and predictable. We estimate operating cash flow (post tax, pre interest) of INR13-17b and capex of ~INR9b over FY17-20.

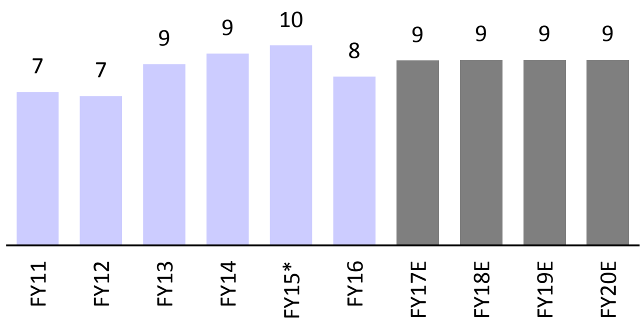
Exhibit 46: Standalone: Operating cash flow – INR b



*Adj. for one-time payment of INR9b for captive

Source: MOSL, Company

Exhibit 47: Standalone: Capex – INR b



*Adj. for one-time payment of INR9b for captive

Source: MOSL, Company

Risks

- Open-access/renewables: Increasing customer preference for open access/net-metering is likely to impact its power offtake. Although base equity return is still guaranteed, incentives and savings which are linked to energy sold would be impacted. However, industrial consumers who have the load profile to shift to open access represented less than 25% of its total supplies.
- Carriage and content: The draft Electricity Act, 2015 calls for splitting carriage and content promoting competition in the last-mile electricity supply business. Although the proposal is being opposed, it is likely to be introduced as an optional guideline rather than a mandatory one. Metros like Kolkata could be encouraged to shift first.

Haldia: INR6-9b p.a. operating cash flow visibility over next decade

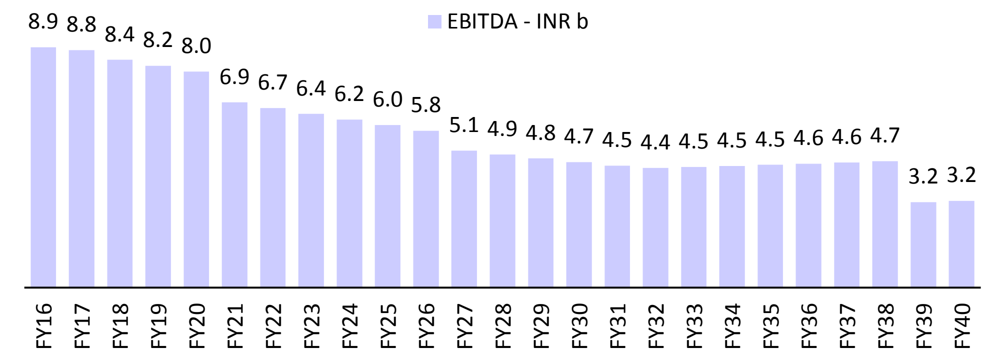
Haldia is a 600MW coal-based thermal power plant located in West Bengal. The plant was commissioned at end-FY15. It has a long-term regulated return-based arrangement with CESC's Kolkata distribution business (standalone). The project's SPV also houses the 96km transmission line under the regulated return model. Regulations and operating norms are set by the West Bengal Electricity Regulatory Commission (WBERC) typically for a block period of three years.

Key project and operating highlights

- Project cost is ~INR38b for the power plant, and ~INR5.7b for the transmission line.
- Normative equity is @ 25%, which earns post-tax return of 15.5%.
- In its first full year of operations (i.e. FY16), it earned RoE of ~20%, driven by earnings from incentives, primary related to station heat rate, in our view.
- Of its PBT of INR2.9b in FY16, we estimate ~INR0.9b was from station heat rate incentive. We conservatively estimate the regulator to squeeze the SHR norms from FY21.

- The approved station heat rate is 2,345kCal/kWh, as against our estimated actual heat rate (based on other coal plants) of 2,150kCal/kWh.

Exhibit 48: Haldia EBITDA – INR b



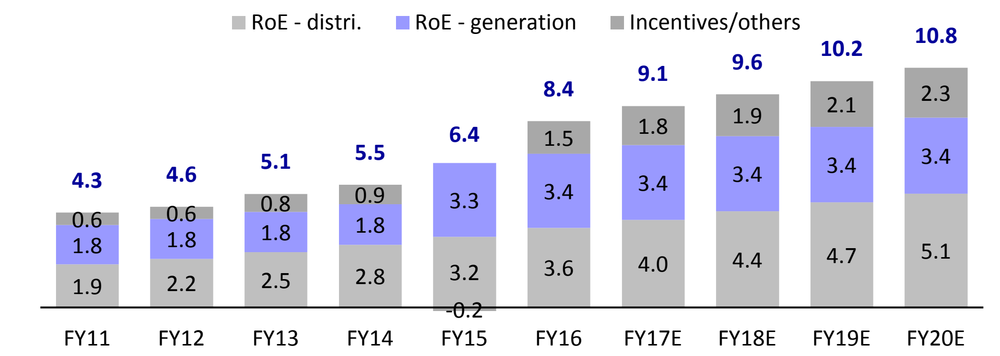
Source: MOSL, Company

Integrated electricity utility business at Kolkata to deliver steady 6-8% earnings growth

Electricity demand growth drives earnings in the integrated electricity utility business of Kolkata (including Haldia) in the form of capex and incentives/savings, which are a factor of units sold. We estimate ~3-4% growth in peak demand (v/s. 4.3% CAGR over FY10-16 and guidance of ~4.5%). Regulated equity base is estimated to grow at ~7% CAGR over FY16-20 v/s ~8% over FY10-16 on demand/customer growth led distribution capex. We estimate ~INR0.8b p.a. (pre-tax) impact from the unreasonable bid for the captive coal block, although the company considers this as pass-through in tariffs (matter with the regulator). We view the Kolkata business as a stable 6-8% annual growth business. Excluding the impact of the captive coal block, we estimate PAT to grow from INR8.4b in FY16 to INR9.6b by FY18E, implying annual growth of ~7%.

Integrated utility business (ex-captive coal block impact) to grow at steady 6-8% p.a.

Exhibit 49: Integrated utility PAT (standalone + Haldia) ex-captive block impact



Source: MOSL, Company

Dharriwal: Noida PPA likely in 3QFY17

But drag would continue

- **PAT loss is estimated to halve to INR2.5b by FY18 as supplies commence under the Noida long-term contract with the commissioning of Champa-Kurukshetra HVDC line and full benefit of Tamil Nadu contract materializes.**
- **However, with 50% of capacity connected to the surplus-Maharashtra state, we believe offtake would be difficult and thus assume PLF of just 50%.**
- **Interest and depreciation of ~INR6b would mean loss would continue unless PPAs are signed for remaining capacity.**
- **We believe strong support from the parent would help sustain operations until the generation market balances and lucrative opportunities emerge.**

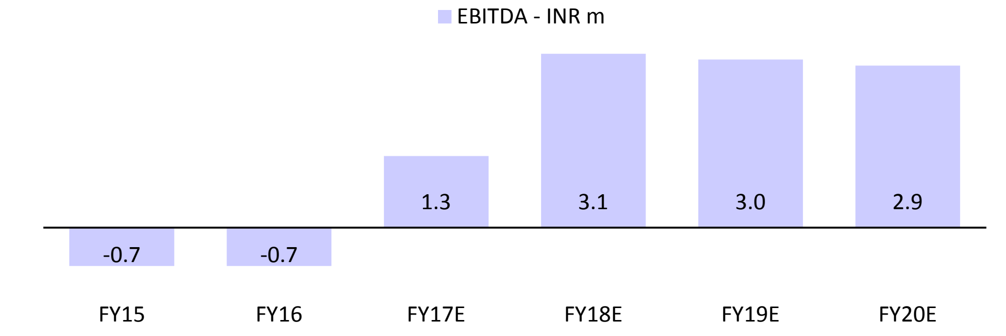
Dhariwal (Chandrapur) is a 2x300MW coal-based power plant in the state of Maharashtra. It is housed in CESC's 100% subsidiary Dhariwal Infrastructure. CESC had acquired the plant in 2009 (was under construction then) from the Manikchand Group. The plant was commissioned in phases by end-FY15. It has coal supply agreement with SECL. Furthermore, the plant has signed power purchase agreements (PPA) for (a) 100MW with Tamil Nadu, under competitive bidding and (b) 187MW with Noida, under a regulated return model. Project cost as per regulatory filings is ~INR39b.

Commissioning of Noida and Tamil supplies to provide some relief...

In its first full year of operation in FY16, Dhariwal reported EBITDA loss of INR0.7b due to the lack of PPAs, transmission capacity and coal availability issues (PLF was 7%). It reported PAT loss of INR5.9b on interest and depreciation charge. Supplies have commenced (late FY16) under the Tamil Nadu PPA, and are likely to start from 3QFY17 under the Noida PPA with the commissioning of the Champa-Kurukshetra HVDC line. We estimate EBITDA of INR1.2b in FY17 and INR3.1b in FY18 as full benefits of these PPAs get reflected.

Dhariwal to turn EBITDA positive with start of PPAs

Exhibit 50: Dhariwal EBITDA



Source: MOSL, Company

...but losses would continue due to exposure to surplus Maharashtra

Dhariwal has 300MW capacity connected to the central transmission unit (CTU), for which it has already secured long-term PPAs (TN and Noida). However, the remaining 300MW capacity is connected to the surplus state Maharashtra's transmission network. According to our estimates, Maharashtra would remain an electricity-surplus region at least until FY20E, based on our study of the state's demand-supply and tariff filings. We believe Dhariwal is unlikely to achieve more than 50% PLF over our forecast period of FY17-20E, i.e. sales would be only under PPAs.

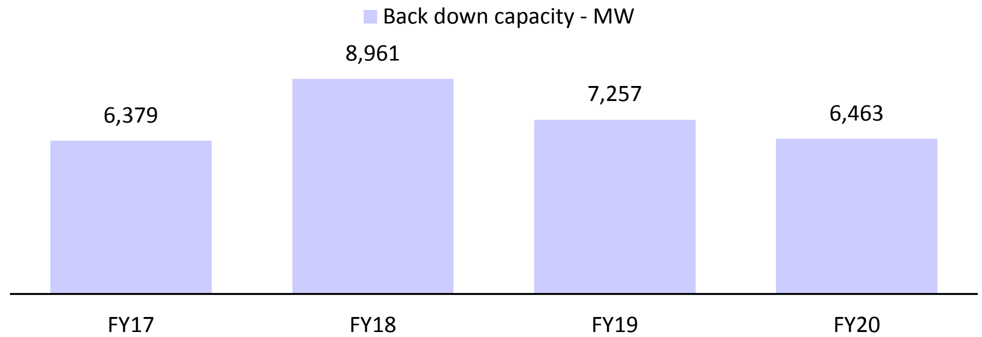
Exhibit 51: Dhariwal's cost competitiveness v/s. Maharashtra gencos thermal plants

Power plants	VC (INR/kWh)
Koradi U-8,9,10	1.25
Chandrapur U-8,9	1.26
Paras	2.16
Bhusawal (4-5)	2.18
CESC - Dhariwal	**2.43**
Khaperkheda	2.50
Parli	2.50
Chandrapur	2.56
Bhusawal	2.59
Koradi	2.97
Nasik	3.39

Source: MOSL, Regulatory Filings

As per regulatory filings, Maharashtra plans to back down ~6-8GW capacity in FY17-20E

Exhibit 52: Maharashtra's back down capacities – MW

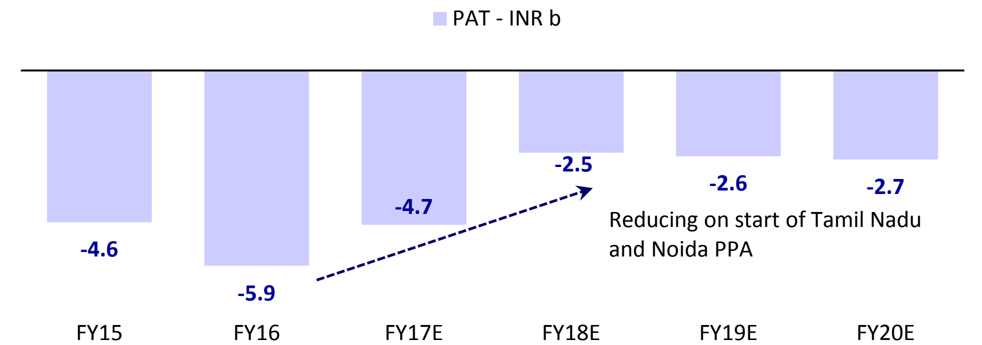


Source: MOSL, Regulatory Filings

We believe PAT loss at Dhariwal would reduce from INR5.9b in FY16 to INR4.6b in FY17E and to INR2.5b in FY18E, led by commencement of the two PPAs. However, with 50% capacity estimated to remain open at least until FY20, the ~INR6b annual burden of interest and depreciation would mean Dhariwal would remain a drag of INR2-2.4b annually until FY20E.

We estimate net loss to decline from INR5.9b in FY16 to INR2.5b in FY18E on start of PPAs

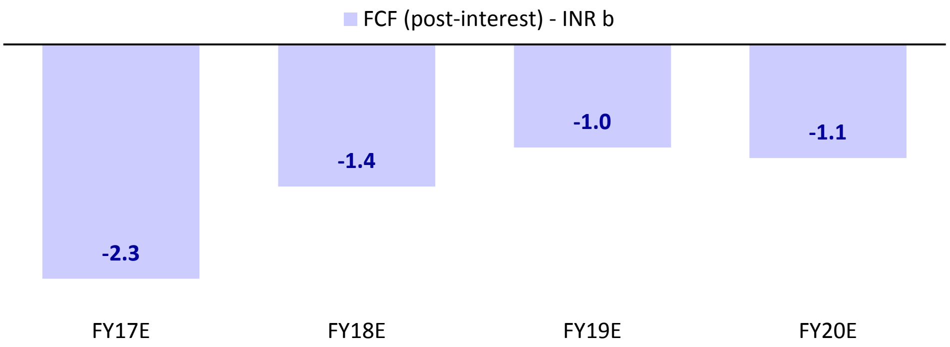
Exhibit 53: Dhariwal net loss – INR b



Source: MOSL, Company

We estimate Dhariwal would need equity support of ~INR1-2b over FY17-20

Exhibit 54: Dhariwal FCF (post-interest) – INR b



Source: MOSL, Company

Spencer: EBITDA breakeven by FY20

Losses have started reducing

- **Performance has improved with an increased focus on costs and closure of unviable stores. EBITDA margin has improved from loss of ~7% in FY13 to 3.2% in FY16.**
- **Unit sales are better than peers, while gross margins are broadly similar.**
- **Higher overheads are dampening its performance. Given management's focus on cost, we expect EBITDA to breakeven by FY20.**

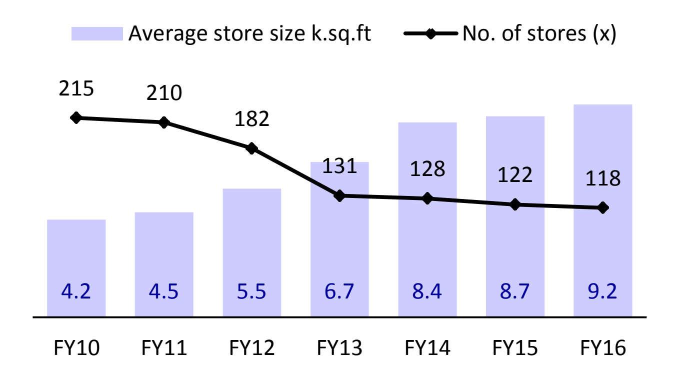
CESC operates its organized retail business under the 'Spencer' brand (part of its 100% subsidiary Spencer Retail). It acquired the business in 2007 from Pathik Retail, a promoter group company. Spencer had 118 stores with an area of 1,083k sq.ft as at end-FY16. While India's retail sector size is estimated to be more than USD600b, organized retail represents just 10% of the market. Spencer is ~10% of the size of the largest organized retail player in India in terms of store area.

Store optimization and focus on opex drive margin improvement

Spencer reported EBITDA loss of INR0.6b in FY16. Although still a drag, it has improved from loss of INR0.9b in FY13 (and INR1.7b in FY11). Spencer has been focusing on:

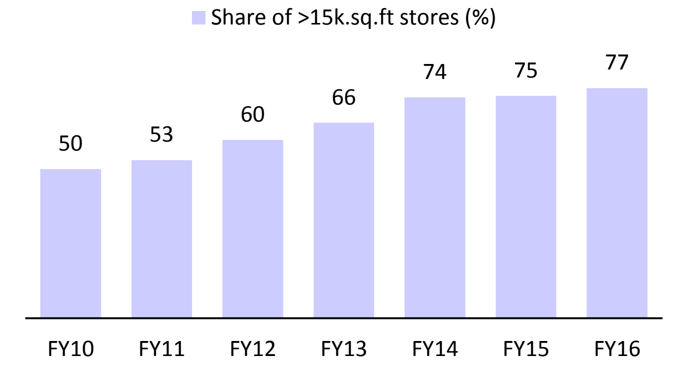
(a) Shifting to larger format stores, which according to the company are more profitable – 77% of its store area was represented by >15k sq.ft stores in FY16, as against 66% in FY13 (and 53% in FY11). The change is more an optimization rather than expansion exercise as the shift is happening primarily through closing of smaller stores (less than 3k sq.ft stores have reduced from 155 in FY11 to 92 in FY13 and to 70 in FY16).

Exhibit 55: Avg. store size and no. of stores



Source: MOSL, Company

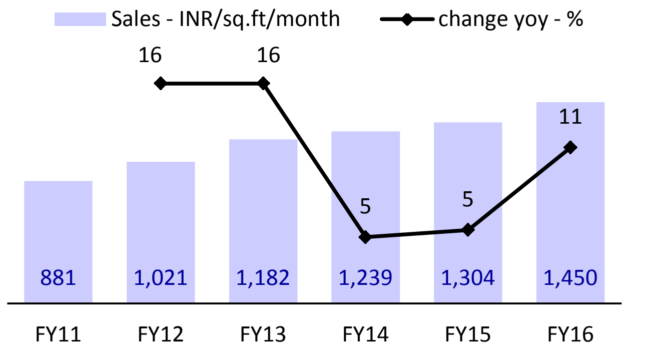
Exhibit 56: Share of >15k sq.ft stores (in area terms)



Source: MOSL, Company

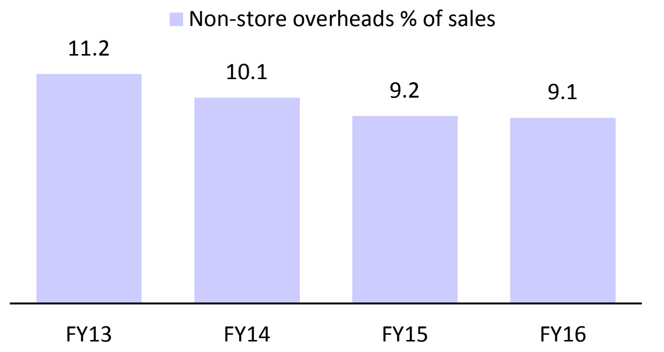
(b) Increasing unit sales and controlling non-store overheads: Same-store sales have increased at a CAGR FY13-16 of 7% to INR1,584 sq.ft/m (and at a 10% CAGR over FY11-16). Higher unit sales and better control over non-store overheads have led to a 210bp reduction in non-store expenses from 11.2% of sales in FY13 to 9.1% in FY16.

Exhibit 57: Unit sales increased at 7% CAGR over FY11-16



Source: MOSL, Company

Exhibit 58: Non-store overheads as % of sales

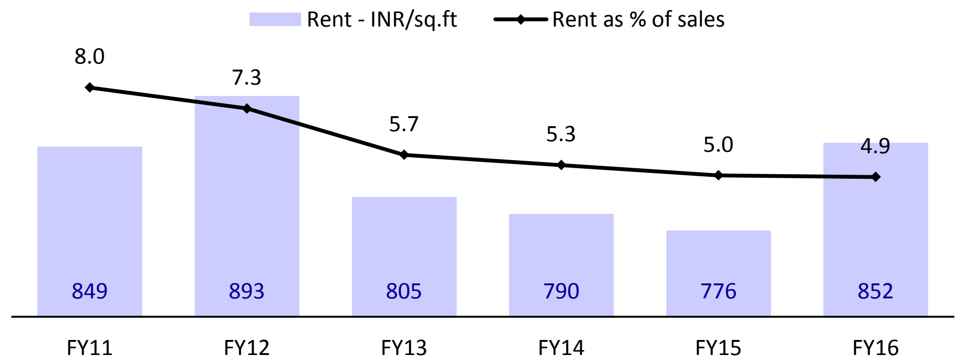


Source: MOSL, Company

(c) Rent cost – Rent per sq.ft. has increased by just 2% to INR852 over FY13-16 (and flat since FY11). Rent as a % of sales has declined ~80bp since FY13 to 4.9% in FY16 (and 310bp since FY11).

Unit rent cost has increased at just 2% over FY13-16. From 5.7% of sales in FY13, it has declined to 4.9% in FY16

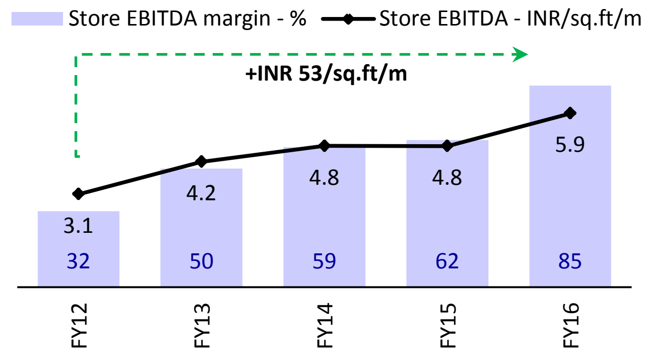
Exhibit 59: Rent per sq.ft. and % of sales



Source: MOSL, Company

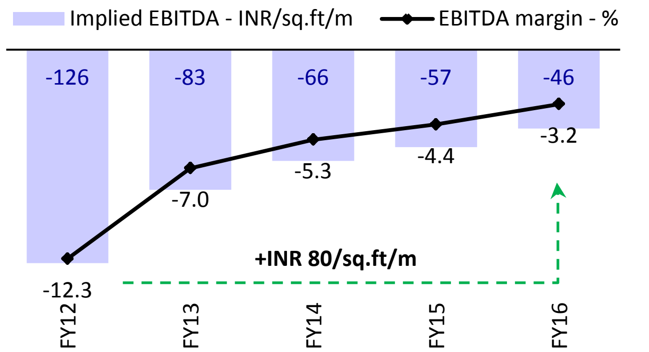
Resultantly, EBITDA margin has improved ~380bp since FY13 to negative 3.2% in FY16. Store-level EBITDA (as reported) has improved ~170bp since FY13 to 5.9% of sales in FY16. Revenues have increased at a 12% CAGR over FY13-16 to ~INR18b, led by 7% CAGR in store area.

Exhibit 60: Store EBITDA – unit and margin



Source: MOSL, Company

Exhibit 61: Implied EBITDA – unit and margin



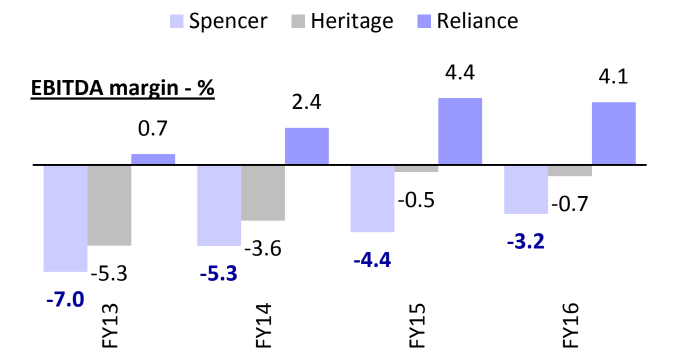
Source: MOSL, Company

Peer comparison suggests significant scope to improve margins

On comparing Spencer's performance to peers (Reliance Retail and Heritage Foods, where data are available and comparative), we understand that the company needs to focus more on reducing cost to improve profitability. Spencer is generating EBITDA loss, despite higher-than-peers unit sales and broadly similar gross margins.

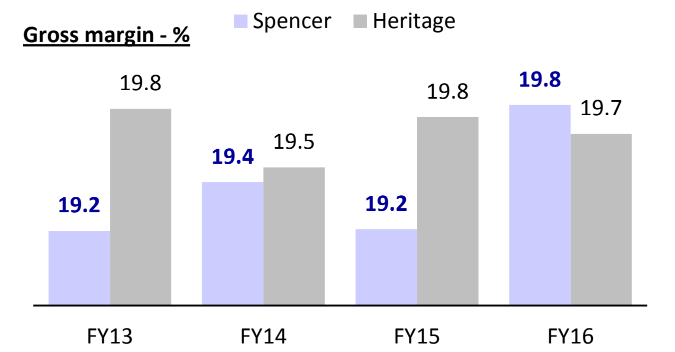
- Spencer generated revenue of INR1,450/sq.ft/month higher than Reliance Retail's ~INR1,400 and Heritage's ~INR1,250 (in FY16)..
- ..But reported higher losses. Spencer EBITDA margin was negative 3.2% v/s. Reliance Retail's +ve 3.2% and Heritage's loss of 0.7%..
- ..Even as gross margins were broadly similar at ~20%
- Spencer has higher 'non-store' cost relative to peers. At 9.1% of sales compared to Heritage's 6.9%.
- At the store level Spencer's EBITDA of ~INR85/sq.ft/month is broadly similar to Heritage's.
- We understand that Spencer needs to particularly focus on rationalizing 'non-store' expenses to improve profitability..

Exhibit 62: Spencer has been underperforming peers…



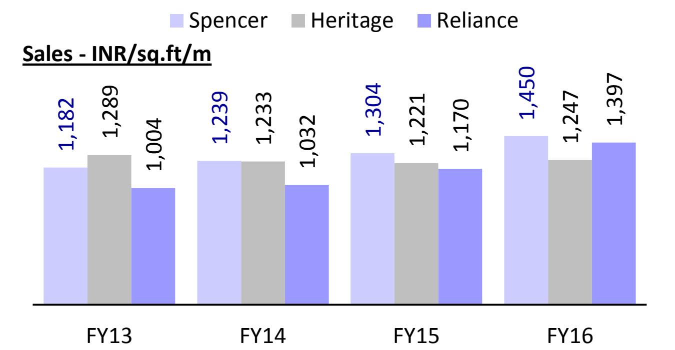
Source: MOSL, Company

Exhibit 63: …despite similar gross margins



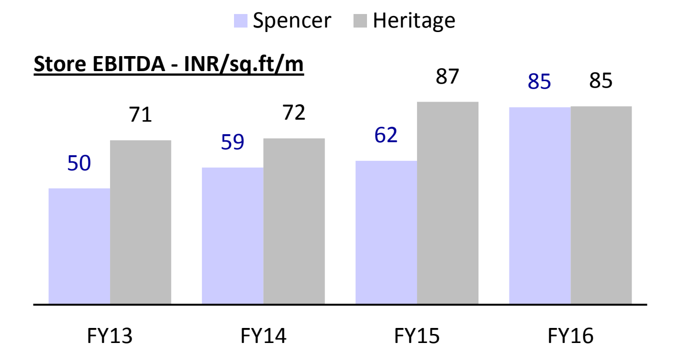
Source: MOSL, Company

Exhibit 64: ...higher unit sales



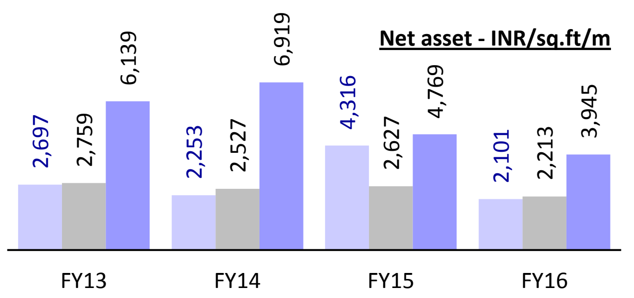
Source: MOSL, Company

Exhibit 65: ...similar unit store EBITDA



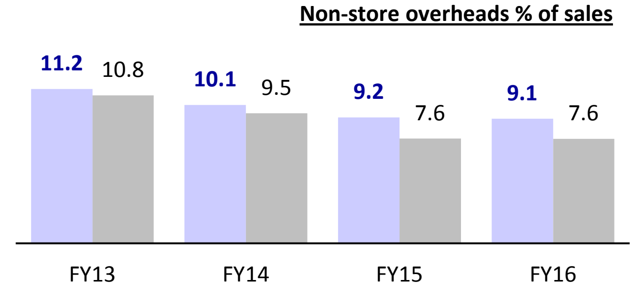
Source: MOSL, Company

Exhibit 66: …and efficient capital deployed…



Source: MOSL, Company

Exhibit 67: …due to higher non-store overheads



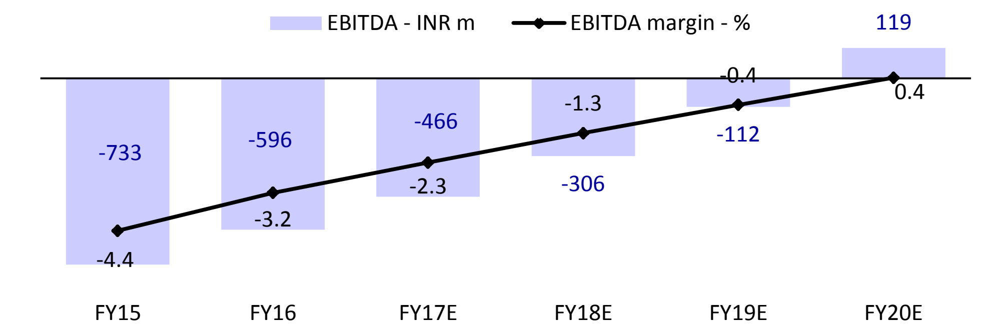
Source: MOSL, Company

Spencer to turn EBITDA positive by FY20E

We estimate Spencer would turn EBITDA positive only by FY20E from loss of INR0.6b in FY16 (or 3.2% of sales). Our estimates are conservative relative to management's guidance of EBITDA positive by FY18E. We estimate slow growth of just 3% in store area by FY20E to 1,225k sq.ft with a further shift toward larger-size stores (84% of total space). Unit sales are estimated to grow ~8% over our forecast period to ~INR1,970/sq.ft/month, broadly in line with ~8% growth in last four years to FY16. Margins improvement would be primarily driven by a decline in non-rent overhead costs from ~18% in FY16 to ~15% by FY20E due to operating leverage and cost optimization. Spencer would continue to incur PAT loss (which should reduce from INR1.4b in FY16 to INR0.8b in FY20E) on depreciation and interest cost.

We expect Spencer to turn EBITDA breakeven by FY20E on increase in unit sales and decline in non-rent overhead cost by ~300bp to ~15% by FY20E

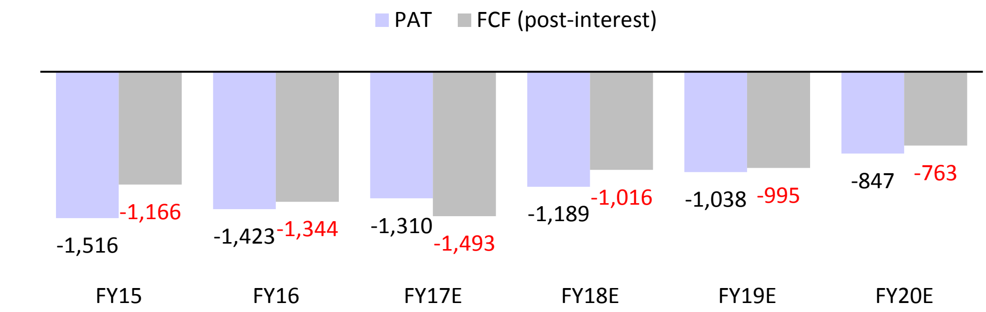
Exhibit 68: Spencer: EBITDA and margin



Source: MOSL, Company

Spencer's net loss is estimated to reduce from ~INR1.4b in FY16 to ~INR1.2b in FY18E and ~INR0.8b in FY20E. It would continue to rely on equity support from parent to a tune of ~INR1.5-0.7b over FY17E-20E

Exhibit 69: Spencer: PAT and FCF (post-interest) – INR m



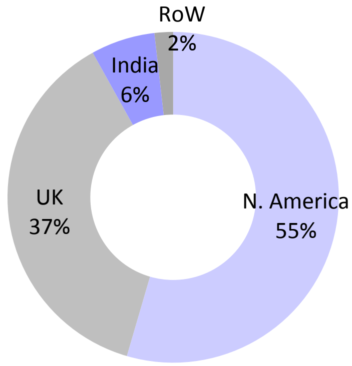
Source: MOSL, Company

Firstsource: PAT to grow at ~14% CAGR over FY16-20E

Firstsource (FS) is the most recent diversification of the CESC group. It is into Business Process Management (BPM) services. CESC acquired ~55% stake in the business in October 2012, then a struggling debt-laden company, and has since directed it on the path of revival. FS is listed on NSE/BSE under the ticker FSL/532809.

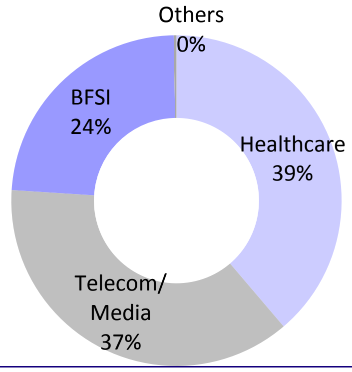
FS recorded revenues of INR32b in FY16 (or USD485m), implying modest ~4% CAGR since its acquisition in FY13. However, EBITDA has increased at ~12% CAGR over the period to ~INR4b, driven by cost optimization. It had employee strength of 23.8k, which has reduced at ~9% CAGR over FY13-16. Geographically, the US represented 55% of its revenue and 42% of EBITDA in FY16. The UK follows with a 37% revenue share, but a higher 51% EBITDA share. Healthcare and telecom/media represent the major end-use industries (~8% share of revenues each), followed by banking and financials (at 24%).

Exhibit 70: Share of revenue by region FY16 – %



Source: MOSL, Company

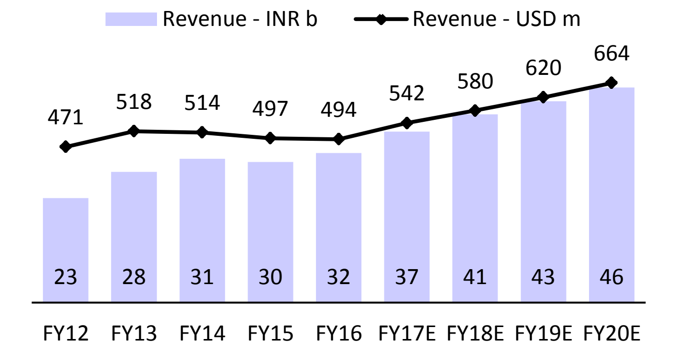
Exhibit 71: Share of revenue by sector – %



Source: MOSL, Company

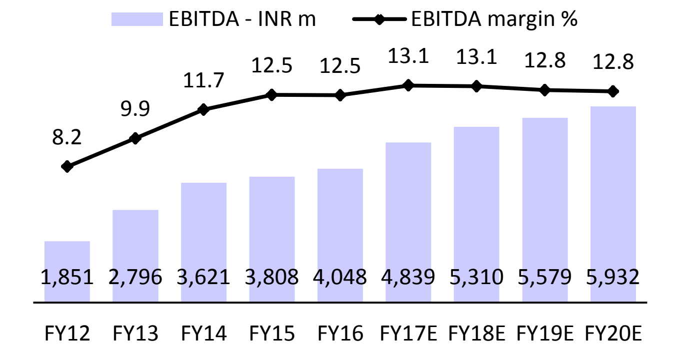
We estimate revenues to increase at ~12% CAGR over FY16-18E to INR40b (or USD580m), driven by the acquisition of ISGN and the sole partnership agreement with Sky. Thereafter, we estimate 7% growth in revenues, which is conservative v/s NASCOM's BPM market growth forecast of 8-9%. EBITDA margins are estimated at ~13% over the forecast period (FY17E-20E). We estimate PAT to increase 21% YoY to INR3.2b in FY17 and 17% YoY to INR3.7b in FY18, and grow at ~10% thereafter due to lower interest cost.

Exhibit 72: Revenue – INR m and USD m



Source: MOSL, Company

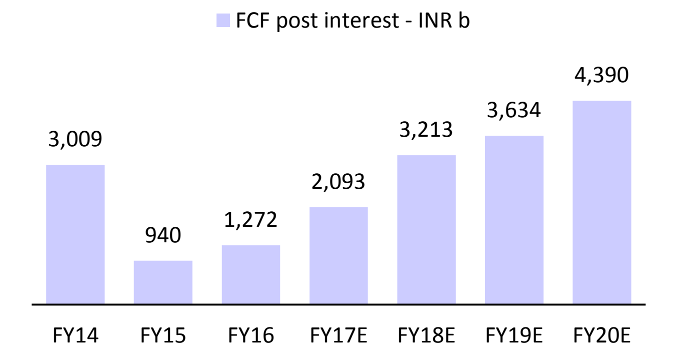
Exhibit 73: EBITDA (INR m) and margin (%)



Source: MOSL, Company

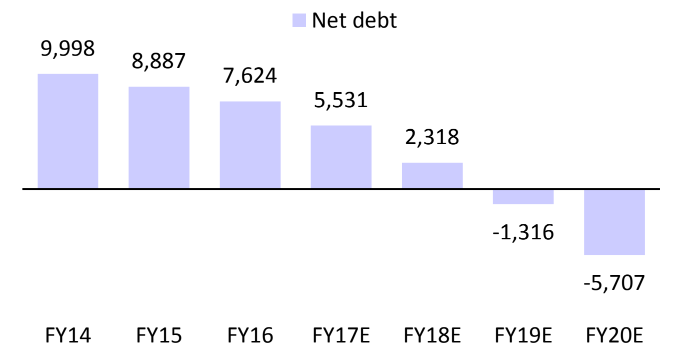
With strong free cash flow generation, FS is estimated to become a debt-free company by FY19.

Exhibit 74: Strong FCF generation at Firstsource



Source: MOSL, Company

Exhibit 75: Firstsource to be net cash company by FY19E

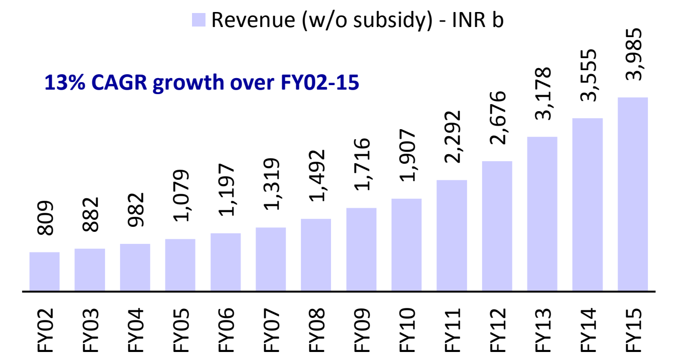


Source: MOSL, Company

Distribution sector – apt for gradual privatization

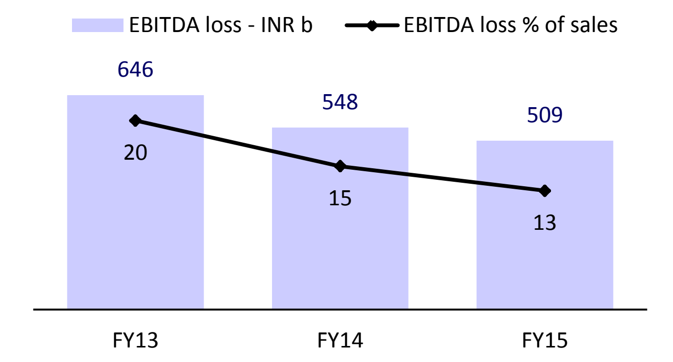
Electricity distribution sector in India is predominantly state-owned (DISCOMs). In our view, its size is more than USD3.9t. However, it terms of performance, it has been extremely weak. It recorded operating loss of more than USD0.5t in FY15 (not made profit at least for last 15 years, according to available data), has debt burden of more than INR4t and rising, and is dependent on state subsidy of ~INR0.4t (in FY15) to remain functional.

Exhibit 76: DISCOMs revenues – INR b



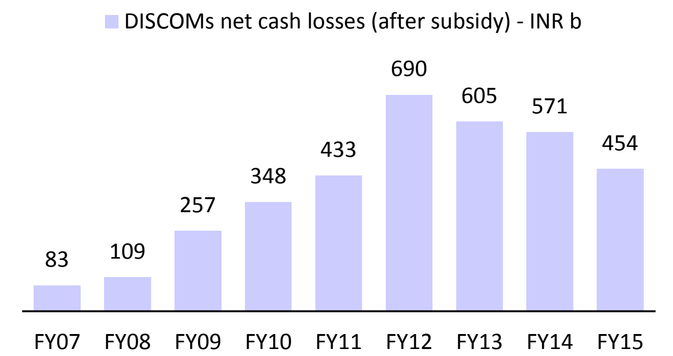
Source: MOSL, PFC

Exhibit 77: DISCOMs operating losses – INR b



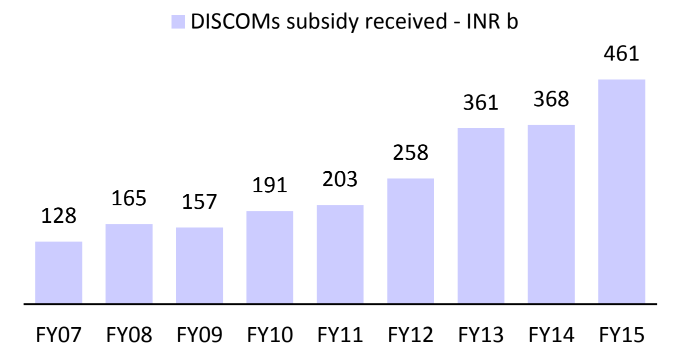
Source: MOSL, PFC

Exhibit 78: DISCOMs net cash loss (after subsidy) – INR b



Source: MOSL, PFC

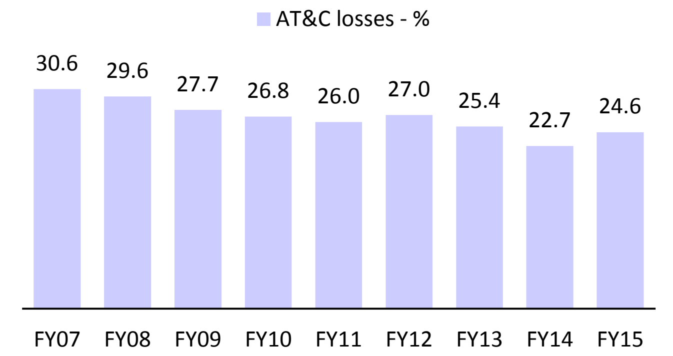
Exhibit 79: DISCOMs subsidy received – INR b



Source: MOSL, PFC

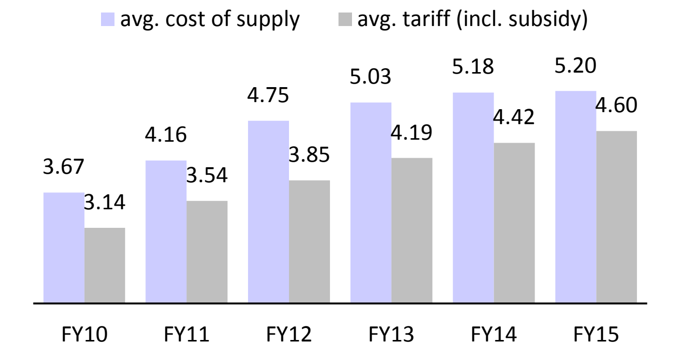
DISCOMs' poor health can be ascribed to their high AT&C losses – more than 20%. The losses are high due to less-than-adequate capital investments, malice in the system (at times political or even operational) and declining share of consumption by cross-subsidizing customers on account of high tariffs.

Exhibit 80: AT&C losses of DISCOMs – %



Source: MOSL, PFC

Exhibit 81: DISCOMs cost of supply and tariff gap – INR/kWh



Source: MOSL, PFC

The 'UDAY' scheme is helpful as it rightly shifts the past burden of DISCOMs to the respective state government (although there are some loopholes, they are not much relevant for our present discussion), lays a stern timeline for AT&C loss reduction, provides subsidy for capex and mandates quarterly tariff revisions. Even on optimistic assumptions, our all-India DISCOMs economics model suggests that DISCOMs would still be making ~INR0.3t operational losses by FY19E.

Exhibit 82: All-India DISCOM economics – INR/kWh

	FY13	FY14	FY15	FY16	FY17E	FY18E	FY19E	FY20E
Agricultural	1.46	1.76	1.93	2.04	2.14	2.26	2.37	2.50
Growth (%)	14.5	20.8	5.0	5.3	5.3	5.3	5.3	5.3
Residential	3.54	3.83	4.03	4.29	4.56	4.86	5.17	5.50
Growth (%)	10.0	8.3	5.3	6.4	6.4	6.4	6.4	6.4
Commercial	7.32	7.74	8.05	8.32	8.60	8.89	9.19	9.50
Growth (%)	13.9	5.7	4.0	3.4	3.4	3.4	3.4	3.4
Industrial	5.93	6.65	6.28	6.50	6.74	6.98	7.24	7.50
Growth (%)	3.6	12.1	-5.6	3.6	3.6	3.6	3.6	3.6
Others	5.47	5.06	6.73	7.07	7.42	7.80	8.19	8.59
Growth (%)	42.9	-7.4	5.0	5.0	5.0	5.0	5.0	5.0
Realization - on energy sold	**4.39**	**4.73**	**4.90**	**5.10**	**5.33**	**5.57**	**5.82**	**6.09**
Realization - on input energy	**3.63**	**3.96**	**4.01**	**4.16**	**4.36**	**4.63**	**4.91**	**5.28**
Growth (%)	18.2	9.0	1.5	3.7	4.8	6.1	6.1	7.4
Other income - on input energy	**0.37**	**0.31**	**0.36**	**0.37**	**0.38**	**0.40**	**0.41**	**0.42**
All-in realization - on input energy	**4.00**	**4.26**	**4.38**	**4.54**	**4.75**	**5.03**	**5.32**	**5.70**
Input cost (ex-Int/Dep)	**4.81**	**4.90**	**4.94**	**5.12**	**5.27**	**5.43**	**5.59**	**5.75**
Power purchase cost	4.02	4.22	4.34	4.46	4.59	4.72	4.86	5.00
Employee	0.42	0.43	0.45	0.46	0.47	0.48	0.49	0.50
Oth. Operating	0.37	0.24	0.15	0.20	0.21	0.23	0.24	0.25
Subsidy req. for EBITDA break-even	**0.81**	**0.63**	**0.56**	**0.58**	**0.52**	**0.40**	**0.27**	**0.05**
INR b	647	528	509	577	562	470	333	72
provided	361	368	461					

Source: MOSL, Company

Although 'UDAY' is unlikely to get DISCOMs out of red, it along with certain other developments in the sector lays the groundwork for acceleration in privatization of the distribution sector.

- **'UDAY' limits ability to park losses** as banks are no longer allowed to fund DISCOM losses. States earlier could build up on their inefficiencies by parking them on DISCOMs' balance sheets. 'UDAY' fills this loophole. This, in our view, would put pressure on state governments to make quick decisions on underperforming/socially acceptable areas that can be privatized to reduce losses.

- **Private DISCOMs have outperformed:** Although not universally, private entities have demonstrated satisfactory performances. Targets such as 'Power for All' and increasing agriculture supply in areas where electricity supply economics are unfavorable would put strain on state government balance sheets and their ability to fund capex. Privatization is a way out, in our view.

Exhibit 83: Performance of private sector companies in distribution sector

Region	State	Takeover	AT&C		Latest	Licensee	Remarks
		Date	Before	Latest	Data For		
Bhiwandi	Maharashtra	Jan-07	61.4	21.9	FY15	Torrent Power	
Nagpur	Maharashtra	May-11	30.4	15.9	FY15	Essel	
Sagar	MP	Dec-12	42.0	30.0	FY14	Essel	Operating satisfactory
Gaya	Bihar	Jan-14	58.0	45.0	FY16	India Power	
Delhi (Tata)	Delhi	Apr-04	45.0	8.8	FY16	Tata	
Agra	UP	Apr-10	42.0				Not satisfactory
Kanpur	UP	Apr-10	47.0				Cancelled
Jalgaon	Maharashtra	Nov-11	29.1	28.0	FY15	CGL	Contract terminated
Aurangabad	Maharashtra	May-11	20.2	18.8	FY15	GTL	Contract terminated
Ujjain	MP	Aug-14					Terminated
Muzaffarpur	Bihar	Jan-14	NA	NA		Essel	
Bhagalpur	Bihar	Jan-14	NA	NA		SMPL	

Source: MOSL, Regulatory filings

- **Complexity in operations** has increased with a focus on renewables, net metering and requirement for time-of-day tariffs. All these changes require data analytics and technological upgrades. Our checks with public DISCOMs suggest that this is one area where public DISCOMs have a major disadvantage (other than capital availability). Public DISCOMs often get entangled in procedural delays, scope issues and implementation with IT companies. Our interaction with private entities suggests that data analytics (something which public DISCOMs have not adopted well) is critical to understand the rationale behind losses. With increasing complexity and the lack of technological prowess among public companies, we believe the shift to privatization would only accelerate.
- **Draft Electricity Act proposal for splitting carriage and content** would encourage competition in the content business as it splits the wire and supply business. It does away with the current stringent licensing requirement in distribution and opens the sector for competition. Although the proposal is being opposed, it is likely to be introduced as an optional guideline rather than a mandatory one.
- **Various other developments** like open-access, along with price transparency through exchanges and oversupplied generation market, have made DISCOMs' operations even more transparent. Measures like 'Power for All' would gradually shift the focus from 'availability of power' to 'quality availability of power', which cannot be accomplished by DISCOMs without incurring capex.

While various models are available for privatization, the input-based distribution franchisee model has been generally preferred in all the recent bids.

Exhibit 84: Various models for privatization of DISCOMs

Franhisee models (below) Responsibilty of partner (right)	Energy Purchase	Network capex	O&M	Metering & Billing	Revenue Collection	ARR for tariff	Positives	Negatives
Collection based revenue	×	×	×	✓	✓	×	Works in areas where commercial losses are high (e.g. rural)	Loss reduction is not the objective as revenue is linked to collection
Input based revenue	✓	×	×	✓	✓	×	Partner in loss reduction	Extremely close co-ordination between the discom and partner
Input based	✓	✓	✓	✓	✓	×	Complete responsibility as earnings are linked to reducing AT&C with operating freedom	Have to depend on discom for power supplies.

Source: MOSL

The working of input-based franchisee model is:

- Franchisee bids for the price at which it would buy power from the DISCOM (called 'Bulk Supply Price'); the highest bidder is the winner.
- Franchisee raises bill at the tariff decided by the regulator and pays the DISCOM for input energy at the bid price.
- Franchisee keeps with itself the surplus revenue left after paying the DISCOM. Thus, the faster it is able to reduce losses, the more is the surplus available.
- Franchisee earnings are directly correlated to energy it bills/realizes. The more the energy quantity billed, the higher is the surplus.
- Franchisee makes the required investment in network infrastructure and maintenance. All operations of the distribution area (like new connections, billing and complaint resolution) are undertaken by the franchisee.

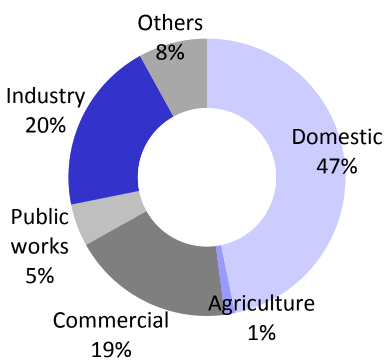
Our interactions with private companies and the past bid results suggest that companies prefer to participate in urban areas, where agriculture load is very low. Agriculture supply is generally perceived to come with political interference and is difficult to manage. As per the Planning Commission study in 2011 on privatization of DISCOMs, there are 255 cities in India where privatization can be adopted.

CESC secures Kota and Bharatpur in distribution franchisee bidding

CESC won the distribution circles of Kota and Bharatpur in Rajasthan in the recent input-based distribution franchisee bidding. Competition was limited with Tata Power being the only other eligible bidder.

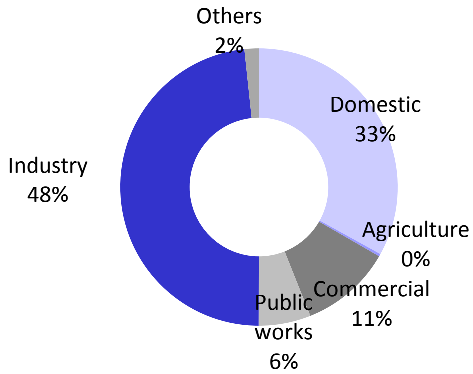
Agriculture consumption is low in both the circles. Billed tariff is above INR5/kWh, broadly similar to metro cities. AT&C losses are above 25%.

Exhibit 85: Kota consumption by category (in MUs)



Source: MOSL, Rajasthan DISCOM

Exhibit 86: Bharatpur consumption by category (in MUs)



Source: MOSL, Rajasthan DISCOM

Exhibit 87: Kota distribution area – few operating parameters

	FY11	FY12	FY13	FY14	FY15
Input Energy - MU	937	919	937	974	1,088
Unit Billed - MU	682	724	712	731	765
AT&C loss - %	26.8	28.0	29.2	26.0	29.7
T&D loss - %	22	21	24	25	30
Collection efficiency - %	94	91	93	99	100
Avg. billing rate - INR/kWh	3.69	4.29	5.24	5.52	5.62
Avg. realization - INR/kWh	2.70	3.09	3.71	4.08	4.07

Source: MOSL, Rajasthan DISCOM

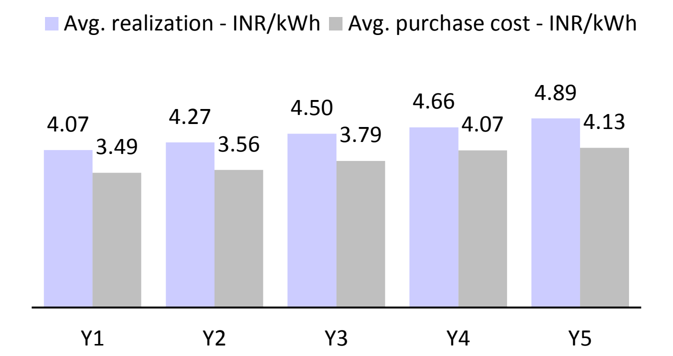
Exhibit 88: Bharatpur distribution area – few operating parameters

	FY11	FY12	FY13	FY14	FY15
Input Energy - MU	242	262	273	287	317
Unit Billed - MU	194	212	213	226	230
AT&C loss - %	22.5	21.1	23.6	27.4	27.4
T&D loss - %	20	19	22	20	27
Collection efficiency - %	97	97	98	91	100
Avg. billing rate - INR/kWh	4.00	4.63	5.47	5.81	5.93
Avg. realization - INR/kWh	3.10	3.65	4.18	4.17	4.31

Source: MOSL, Rajasthan DISCOM

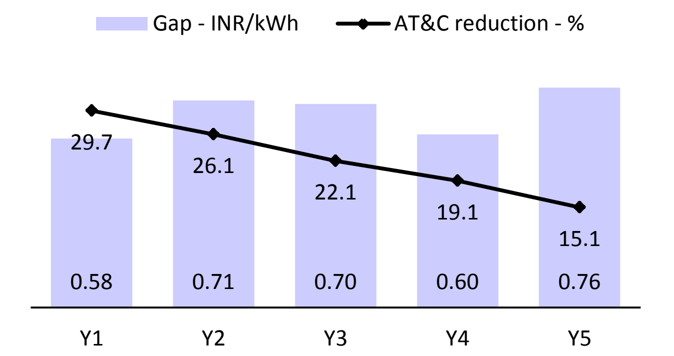
There is limited guidance on these businesses, given their relatively small size and management's wait-and-watch stance. Based on our analysis of target AT&C loss reduction to 15% in five years and input rates (Bulk Supply Price) available from the bidding document, we estimate the gap earned (i.e. realized price less input price) is likely to range between INR 0.5-0.8/kWh of input energy over the first five years in both the distribution areas. Rajasthan DISCOMs and all-India DISCOMs average power supply operating cost is ~INR 0.7-0.9/kWh. CESC believes that it can be competitive compared to public DISCOMs. We consider supply cost of INR0.5/kWh to increase ~4% annually.

Exhibit 89: Kota realization and cost at input energy



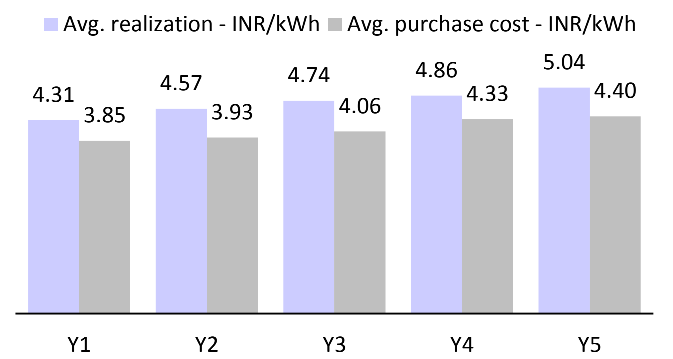
Source: MOSL, Rajasthan DISCOM

Exhibit 90: Kota gap earned and AT&C loss reduction



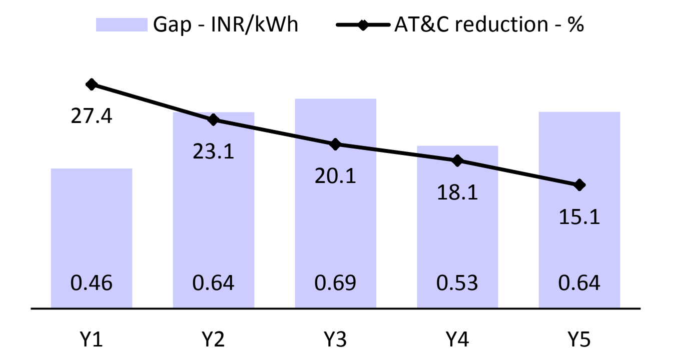
Source: MOSL, Rajasthan DISCOM

Exhibit 91: Bharatpur realization and cost at input energy



Source: MOSL, Rajasthan DISCOM

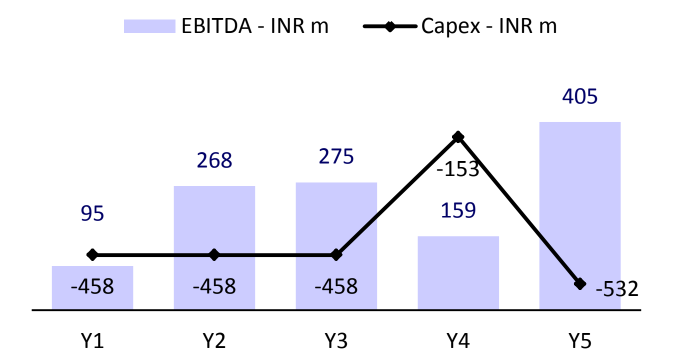
Exhibit 92: Bharatpur gap earned and AT&C loss reduction



Source: MOSL, Rajasthan DISCOM

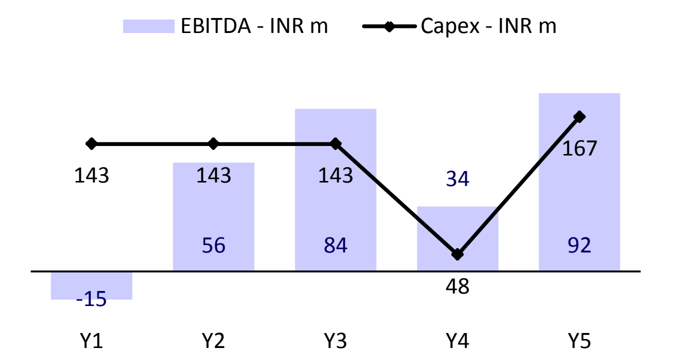
Based on our preliminary analysis, we estimate Kota to generate EBITDA of INR 95-405m annually in the first five years. Bharatpur is estimated to generate EBITDA of negative INR50–90b annually. CESC has committed capex of INR2b in these distribution circles over next five years.

Exhibit 93: Kota EBITDA and capex



Source: MOSL, Rajasthan DISCOM

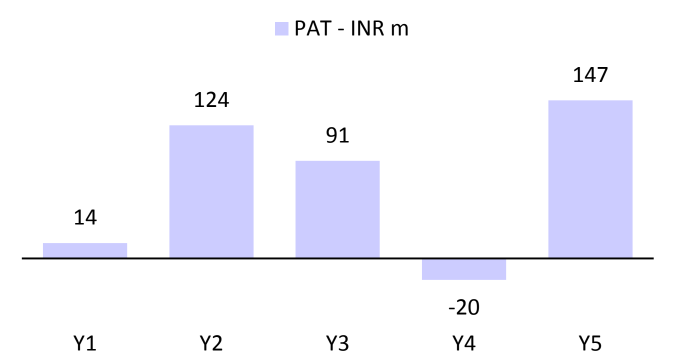
Exhibit 94: Bharatpur EBITDA and capex



Source: MOSL, Rajasthan DISCOM

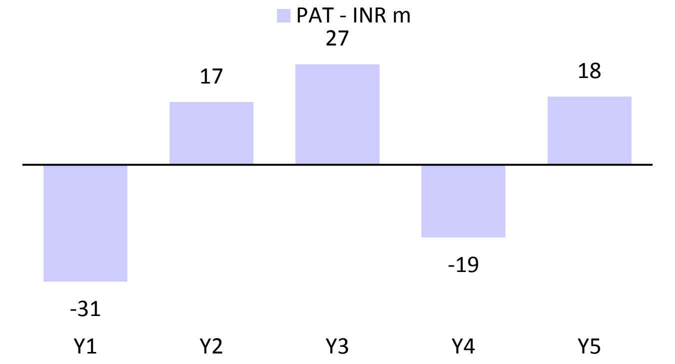
We estimate PAT of less than ~INR150m p.a. in both these circles together. Given that the quantum is insignificant and our estimates are only preliminary based on market understanding, we do not incorporate the numbers into our model.

Exhibit 95: Kota PAT



Source: MOSL, Rajasthan DISCOM

Exhibit 96: Bharatpur PAT



Source: MOSL, Rajasthan DISCOM

CESC well placed to gain from privatization of DISCOMs

CESC is among the few companies in India with experience in electricity distribution. The other notable companies are Tata Power, Torrent Power and Essel Utilities. CESC is operating the Kolkata distribution circle for the past 100+ years and has expertise in managing the unique issues related to operating in India (e.g., regulatory requirements, handling value-for-money customer class, subsidized tariff structure and unionized operating environment).

The market potential is huge, while competition is limited. Our estimates do not factor in the company's advantageous position. CESC has the balance sheet strength and considers distribution as a key growth area. Thus, we believe CESC is a well-balanced play on the opening up of the distribution sector in India.

Valuation

Initiating with Buy and TP of INR940/share

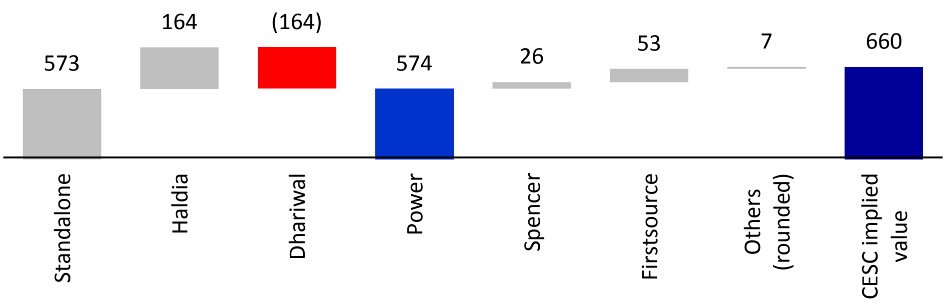
FCF of ~INR2-10b p.a. represents ~11% of market capitalization.

We expect CESC's PAT/ROE to more than double in the two years on commencement of long-term power supplies at Dhairwal and growth at Firstsource. Earnings growth would continue on back of steady growth at the integrated utility business and improvement at Spencer. CESC is of the few private power sector companies with visibility and momentum of earnings growth. FCF generation is estimated to be healthy at ~INR11b – an FCF yield of ~11%. The regulated integrated utility business generates steady cash (FCF of INR5-9b p.a.) further aided by improving performance at Firstsource (FCF of INR2-4b p.a), thus more than absorbing the temporary losses at Dhariwal and Spencer. It provides deleveraging visibility from an already healthy 1.8x net debt-to-equity in FY16 to 1.0x by FY20E.

For ~14% RoE and steady growth the stock currently trades at ~1.2x FY18E. The valuations do not factor the long-term value potential of the untied capacity at Dhariwal and potential at Spencer. At current stock price the market is probably factoring that Dhariwal would remain under-utilized (continue to operate at 50% PLFs) over its life.

At current stock price, the market is probably factoring in that Dhariwal would perpetually remain at 50% PLF

Exhibit 97: What is CESC's current stock price probably implying



Source: MOSL, Company

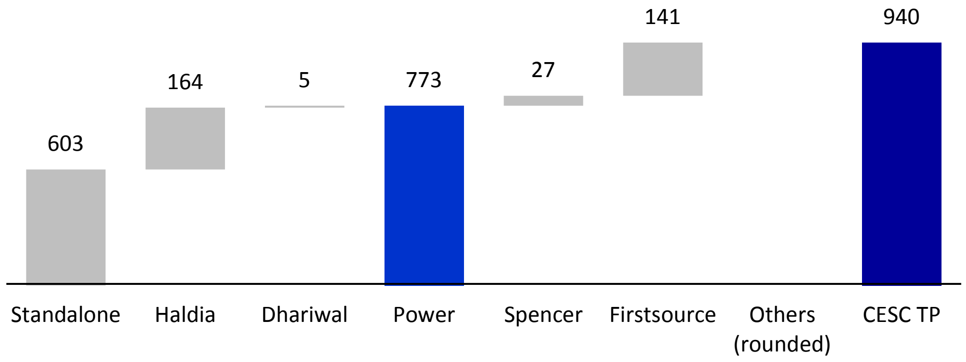
The loss making business of Dhariwal and Spencer have long-term potential and CESC has the ability to unlock value.

We believe Dhairwal remaining untied for rest of its asset life it is highly unlikely for the growth potential which Indian power market offers. While there are a number of untied power generation capacities in the system, we believe, CESC is one of the few that has the balance strength to play the cycle. It is significant better positioned to wait for lucrative deals until the electricity market balances. This, in our view deserves premium. Even the losses at Spencer are a drag on overall returns. CESC has demonstrated cost excellence in past – ~380bps margin improvement over FY13-16. We believe with continued focus on cost, optimizing stores and increasing unit sales, Spencer can turn operating break-even by FY20E. Where we to assume Dhariwal and Spencer turnaround by FY20E (refer Bull case scenario), CESC would be generating RoE of ~20% and net debt-to-equity of less than 1x.

Considering the above factors we value CESC on SOTP – mix of DCF (for power businesses) and relative (for other business) valuation. In our view SOTP best captures the long-term value potential of the businesses. Moreover, earnings mix is expected to diversify from ~1% of consolidated PAT in FY16 coming from less capital intensive business (Spencer and Firstsource) in FY16 rising to ~16% by FY20. This warrants SOTP to better capture value of different businesses, in our view.

Power business represents ~80% of our target value

Exhibit 98: CESC's target price build-up – INR/share



Source: MOSL, Company

While not captured in our valuation, we believe CESC also offers one of the best plays on the privatization of electricity distribution sector in India. It has more than 100 years of experience in the sector and is amongst the few players in the sector. Notably, it recent won the privatization round at Kota and Bharatpur.

Our SOTP based target price is INR940/sh. Power business represents ~80% of our target value. The implied P/BV is 1.9x FY18E. We initiate coverage on CESC with Buy rating with an upside of 60%.

Exhibit 99: CESC target price derivation

	Business	Method	CoE (%)	Sus. Gr. (%)	RoE FY17-20E (%)	Valuation Multiple (x)	Base Value	Stake %	EV INR m	Debt & Eq. cont. INR m	Value INR m	Value INR/sh.
a. Power business									**212,393**	**109,451**	**102,942**	**773**
Standalone	Gen. & distribution	PE FY18E	11.6	5.0	16.8	10.6	7,549	100.0	125,255	44,864	80,391	603
Haldia	Gen. & transmission	DCF based	11.6					100.0	50,050	28,207	21,843	164
Dhariwal	Generation	DCF based	11.6					100.0	37,089	36,380	709	5
b. Spencer	**Retailing**	**EV/sales FY18E**				**0.40**	**23,063**	**100.0**	**9,225**	**5,674**	**3,551**	**27**
c. Firstsource	**Business process o/s**	**PE FY18E**				**9.0**	**3,755**	**55.5**	**36,114**	**2,318**	**18,771**	**141**
d. Others	**Mall/renewable & others**	**EV/EBITDA FY18E**				**6.00**	**908**	**100.0**	**5,448**	**3,346**	**2,102**	**16**
Less: Cricket loss											**-1,000**	**-8**
TP		**Rounded**										**940**

Key risk: (a) Slower-than-expected electricity demand growth in its distribution license area leading to moderation in distribution capex investment, (b) Delay in commissioning of the Noida PPA at Dhariwal and (c) Impact of 'Brexit' on Firstsource – derives ~40% of revenues from UK.

Relative valuations

	Rating	CMP (INR)	TP (INR)	Upside %	MCAP (USD M)	EPS FY16	EPS FY17E	EPS FY18E	P/E (x) FY17E	P/E (x) FY18E	P/B(x) FY17E	P/B(x) FY18E	RoE (%) FY17E	RoE (%) FY18E
Powergrid	Buy	180	209	16	14,211	11.5	14.2	16.8	12.7	10.7	1.9	1.7	16.1	16.6
NTPC	Buy	154	199	29	19,127	12.3	11.9	14.3	13.0	10.8	1.3	1.2	10.6	11.9
JSW Energy	Buy	59	86	45	1,459	8.5	4.6	6.7	13.0	8.9	1.1	1.0	8.6	11.8
CESC	**Buy**	**599**	**940**	**57**	**1,201**	**27.8**	**40.9**	**64.7**	**14.6**	**9.3**	**1.4**	**1.2**	**9.1**	**14.1**
Coal India	Neutral	318	327	3	30,227	22.6	17.0	21.1	18.7	15.0	5.7	5.5	31.3	37.5

Bull and Bear case

Bull case

- Dhariwal PPA for remaining capacity of 300MW is secured by FY19 on higher-than-expected electricity demand growth in India.
- Spencer turns EBITDA break-even by FY18 in-line with management's guidance and generates margin of ~4% by FY20E in line with Reliance Retail.
- In the Kolkata utility business, distribution capex grows at the FY10-16 CAGR of ~13% as against ~9% growth estimated in our base case on higher-than-expected demand growth in its circle area led by improvement in standard of living.
- Long-term sustainable growth in the Kolkata utility business turns to be higher at 7% as against 5% in our base case estimate.

Bear case

- Dhariwal power plants continues to operate at 50% PLF (remaining 300MW does not secure a PPA) at least until FY25E as renewables become competitive. Moreover, the 187MW PPA with Noida that is likely to start in FY18 gets delayed to FY21E.
- Spencer losses continue at current levels facing risk from online retail and weaker than expected turnaround.
- In the Kolkata utility business, distribution capex growth tapers down to less than 3% as consumers shift to roof-top solar based power generation and battery back-up reducing the requirement for distribution network.
- Long-term sustainable growth in the Kolkata utility business turns to be at 3% as against 5% in our base case estimate.
- Firstsource revenues grow at just 3% v/s. our base case estimate of 7-10% growth.

Exhibit 100: Bull and Bear case scenario

	Base case				Bull case				Bear case			
	FY17E	FY18E	FY19E	FY20E	FY17E	FY18E	FY19E	FY20E	FY17E	FY18E	FY19E	FY20E
Revenue	136	148	156	164	136	148	164	174	133	141	146	152
EBITDA	32	35	36	37	32	35	41	44	30	28	27	26
PAT	5.4	8.6	9.5	10.6	5.7	9.1	14.7	16.7	4.6	4.6	4.5	4.4
Net debt/Equity	1.8	1.5	1.2	1.0	1.8	1.6	1.2	0.9	1.8	1.6	1.4	1.3
RoE	9.1	14.1	13.9	13.7	9.4	14.8	20.5	19.4	7.7	7.9	7.4	6.8
P/E	14.6	9.2	8.3	7.5	14.0	8.7	5.4	4.8	17.3	17.3	17.6	18.1
P/BV	1.4	1.2	1.1	1.0	1.4	1.2	1.0	0.8	1.4	1.3	1.3	1.2
SOTP	**940**				**1,140**				**670**			

Source: MOSL, Company

SWOT ANALYSIS

SWOT

ANALYSIS

STRENGTHS

- Of the few private sector players in the electricity distribution sector where it has more than 100 years of experience.
- Strong project execution capability completing power plants within reasonable cost estimates despite the regulatory logjam in the last few years.
- One of the best balance sheets in the private power sector in India.

WEAKNESS

- Regulator has to approve capital investment & operating expenses (controllable and pass-through). The expenses can be disallowed if the regulator is not convinced, impacting earnings.
- Unexpected sharp increase in uncontrollable expenses (like O&M costs) in generation and distribution can impact returns. Tariffs are set by regulator which restricts the company's ability to pass-on the cost increase on consumers.

THREATS

- Open-access and decline in electricity demand in its distribution area.
- Squeezing of incentives (like SHR efficiency, AT&C loss target, Auxiliary consumption) by regulator.
- Machine learning and artificial intelligence can impact the opportunity size of the BPM business.
- Online retail is a major threat to its organized retail business.

OPPORTUNITY

- Opening up of electricity distribution sector in India.
- Growth in electricity demand and improvement in PLFs.
- Penetration of organized retail which currently represents just 10% of the market size.

Financials and Valuations

Income Statement							(INR Million)
Y/E March	**2012**	**2013**	**2014**	**2015**	**2016**	**2017E**	**2018E**
Net Sales	**58,917**	**75,567**	**101,109**	**110,666**	**118,995**	**135,582**	**147,720**
Change (%)	13.8	28.3	33.8	9.5	7.5	13.9	9.0
Total Expenses	49,195	62,906	84,883	91,721	90,513	103,942	113,104
EBITDA	**9,722**	**12,661**	**16,226**	**18,945**	**28,483**	**31,640**	**34,616**
% of Net Sales	16.5	16.8	16.0	17.1	23.9	23.3	23.4
Depn. & Amortization	3,401	3,645	4,714	5,889	7,725	8,717	8,986
EBIT	**6,321**	**9,016**	**11,512**	**13,056**	**20,758**	**22,922**	**25,630**
Net Interest	3,451	4,304	5,660	9,565	14,856	14,699	13,995
Other income	1,323	1,437	1,734	1,490	2,191	2,163	2,445
PBT before EO	**4,193**	**6,149**	**7,585**	**4,981**	**8,092**	**10,386**	**14,079**
EO expense	257	-418	0	0	40	8,989	0
PBT after EO	3,936	6,567	7,585	4,981	8,052	1,398	14,079
Tax	1,492	1,758	1,856	1,992	3,087	3,396	3,663
Rate (%)	37.9	26.8	24.5	40.0	38.3	243.0	26.0
Reported PAT	**2,445**	**4,809**	**5,729**	**2,989**	**4,965**	**-1,999**	**10,416**
Minority and Associates	14	-215	-813	-1,004	-1,301	-1,543	-1,790
Adjusted PAT	**2,716**	**4,176**	**4,916**	**1,985**	**3,704**	**5,447**	**8,626**
Change (%)	5.6	53.8	17.7	-59.6	86.6	47.1	58.4

Balance Sheet							(INR Million)
	2012	**2013**	**2014**	**2015**	**2016**	**2017E**	**2018E**
Share Capital	1,256	1,256	1,256	1,332	1,332	1,332	1,332
Reserves	47,167	50,180	55,094	58,958	61,345	56,205	63,232
Net Worth	**48,423**	**51,436**	**56,350**	**60,290**	**62,677**	**57,537**	**64,564**
Minority Interest	27	7,425	9,079	10,004	11,497	13,040	14,830
Total Loans	52,947	96,608	119,164	142,020	149,053	148,428	145,372
Deferred Tax Liability	0	285	332	832	795	795	795
Capital Employed	**101,397**	**155,753**	**184,925**	**213,146**	**224,022**	**219,800**	**225,561**
Gross Block		146,690	185,350	258,955	270,708	279,646	289,992
Less: Accum. Deprn.		60,502	65,631	72,685	79,807	88,524	97,510
Net Fixed Assets	**82,696**	**86,189**	**119,719**	**186,270**	**190,901**	**191,123**	**192,482**
Capital WIP	24,542	51,097	53,117	4,102	5,130	5,130	5,130
Goodwill	0	22,938	25,392	22,417	22,907	24,692	24,692
Investments	914	976	737	735	801	801	801
Curr. Assets	**39,719**	**51,937**	**50,798**	**65,858**	**66,632**	**62,429**	**68,493**
Inventories	4,077	4,342	5,383	6,625	6,967	7,437	7,826
Account Receivables	9,941	16,201	15,302	17,066	14,146	16,550	17,737
Cash and Bank Balance	14,283	14,314	12,422	16,453	18,182	20,095	24,583
Others	11,418	17,081	17,692	25,714	27,336	18,348	18,348
Curr. Liability & Prov.	**46,474**	**57,383**	**64,838**	**66,235**	**62,350**	**64,376**	**66,038**
Account Payables	4,342	5,775	5,318	6,007	5,981	6,967	7,607
Provisions & Others	42,133	51,608	59,521	60,228	56,369	57,408	58,431
Net Curr. Assets	**-6,755**	**-5,446**	**-14,040**	**-377**	**4,282**	**-1,947**	**2,455**
Appl. of Funds	**101,397**	**155,753**	**184,925**	**213,146**	**224,022**	**219,800**	**225,561**

Financials and Valuations

Ratios

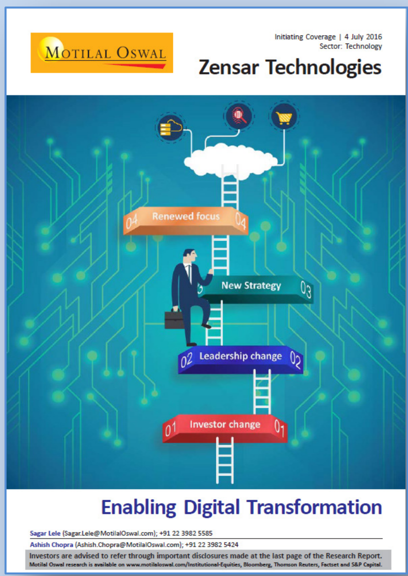
	2012	2013	2014	2015	2016	2017E	2018E
Basic (INR)							
EPS	**21.6**	**33.2**	**39.1**	**14.9**	**27.8**	**40.9**	**64.7**
Cash EPS	48.7	62.3	76.7	59.1	85.8	106.3	132.2
BV/Share	385.5	409.5	448.6	452.6	470.5	431.9	484.6
DPS	5.0	7.0	8.0	9.0	10.0	10.0	10.0
Payout (%)	23.1	21.1	20.4	60.4	36.0	24.5	15.4
Valuation (x)							
P/E				40.4	17.0	14.6	9.2
Cash P/E				10.2	5.5	5.6	4.5
P/BV				1.3	1.0	1.4	1.2
EV/EBITDA				10.9	6.8	6.6	5.8
Dividend Yield (%)				1.5	2.1	1.7	1.7
Return Ratios (%)							
RoE	5.7	8.4	9.1	3.4	6.0	9.1	14.1
RoCE (post-tax)	6.6	6.8	6.7	6.3	9.1	9.8	11.0
RoIC (post-tax)	6.3	10.3	10.9	6.0	7.4	-18.9	11.2
Working Capital Ratios							
Fixed Asset Turnover (x)	0.7	0.9	0.8	0.6	0.6	0.7	0.8
Asset Turnover (x)	0.6	0.5	0.5	0.5	0.5	0.6	0.7
Debtor (Days)	62	78	55	56	43	45	44
Inventory (Days)	25	21	19	22	21	20	19
Leverage Ratio (x)							
Net Debt/MW	15	26	34	40	29	29	28
Net Debt/EBITDA	4.0	6.5	6.6	6.6	4.6	4.1	3.5
Debt/Equity	0.8	1.4	1.6	1.8	1.8	1.8	1.5

Cash flow statement (INR Million)

	2012	2013	2014	2015	2016	2017E	2018E
EBITDA	**9,722**	**12,661**	**16,226**	**18,945**	**28,483**	**31,640**	**34,616**
WC	-272	5,406	7,301	-10,274	-4,025	7,102	-936
Others	1,102	1,968	1,125	2,729	3,132	-8,989	0
Direct taxes (net)	-1,445	-1,479	-2,141	-2,506	-3,311	-3,396	-3,663
CF from Op. Activity	**9,108**	**18,556**	**22,511**	**8,895**	**24,280**	**26,357**	**30,017**
Capex	-24,519	-36,148	-34,209	-19,509	-12,675	-10,724	-10,346
Interest income	576	770	670	550	329	0	0
Investments in subs/assoc.	-406	-5,127	0	-369	-681	0	0
Others	74	2,581	912	1,155	1,076	2,163	2,445
CF from Inv. Activity	**-24,276**	**-37,924**	**-32,627**	**-18,172**	**-11,952**	**-8,561**	**-7,902**
Share capital	20	10	37	5,021	117	0	0
Borrowings	16,434	24,494	19,282	20,980	6,420	-625	-3,057
Finance cost	-3,642	-5,465	-11,134	-11,978	-15,303	-14,699	-13,995
Dividend	-579	-726	-1,021	-1,168	-3,009	-1,599	-1,599
Others	1,126	1,085	1,061	454	1,176	1,039	1,023
CF from Fin. Activity	**13,360**	**19,399**	**8,225**	**13,309**	**-10,599**	**-15,883**	**-17,628**
(Inc)/Dec in Cash	**-1,809**	**31**	**-1,891**	**4,031**	**1,729**	**1,913**	**4,488**
Opening balance	16,091	14,283	14,314	12,422	16,453	18,182	20,095
Closing balance (as per B/S)	**14,283**	**14,314**	**12,422**	**16,453**	**18,182**	**20,095**	**24,583**

REPORT GALLERY

RECENT INITIATING COVERAGE REPORTS



Disclosures

This document has been prepared by Motilal Oswal Securities Limited (hereinafter referred to as Most) to provide information about the company (ies) and/sector(s), if any, covered in the report and may be distributed by it and/or its affiliated company(ies). This report is for personal information of the selected recipient/s and does not construe to be any investment, legal or taxation advice to you. This research report does not constitute an offer, invitation or inducement to invest in securities or other investments and Motilal Oswal Securities Limited (hereinafter referred as MOSt) is not soliciting any action based upon it. This report is not for public distribution and has been furnished to you solely for your general information and should not be reproduced or redistributed to any other person in any form. This report does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients. Before acting on any advice or recommendation in this material, investors should consider whether it is suitable for their particular circumstances and, if necessary, seek professional advice. The price and value of the investments referred to in this material and the income from them may go down as well as up, and investors may realize losses on any investments. Past performance is not a guide for future performance, future returns are not guaranteed and a loss of original capital may occur.

MOSt and its affiliates are a full-service, integrated investment banking, investment management, brokerage and financing group. We and our affiliates have investment banking and other business relationships with a some companies covered by our Research Department. Our research professionals may provide input into our investment banking and other business selection processes. Investors should assume that MOSt and/or its affiliates are seeking or will seek investment banking or other business from the company or companies that are the subject of this material and that the research professionals who were involved in preparing this material may educate investors on investments in such business . The research professionals responsible for the preparation of this document may interact with trading desk personnel, sales personnel and other parties for the purpose of gathering, applying and interpreting information. Our research professionals are paid on twin parameters of performance & profitability of MOSt.

MOSt generally prohibits its analysts, persons reporting to analysts, and members of their households from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover. Additionally, MOSt generally prohibits its analysts and persons reporting to analysts from serving as an officer, director, or advisory board member of any companies that the analysts cover. Our salespeople, traders, and other professionals or affiliates may provide oral or written market commentary or trading strategies to our clients that reflect opinions that are contrary to the opinions expressed herein, and our proprietary trading and investing businesses may make investment decisions that are inconsistent with the recommendations expressed herein. In reviewing these materials, you should be aware that any or all of the foregoing among other things, may give rise to real or potential conflicts of interest. MOSt and its affiliated company(ies), their directors and employees and their relatives may; (a) from time to time, have a long or short position in, act as principal in, and buy or sell the securities or derivatives thereof of companies mentioned herein. (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company(ies) discussed herein or act as an advisor or lender/borrower to such company(ies) or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions.; however the same shall have no bearing whatsoever on the specific recommendations made by the analyst(s), as the recommendations made by the analyst(s) are completely independent of the views of the affiliates of MOSt even though there might exist an inherent conflict of interest in some of the stocks mentioned in the research report

Reports based on technical and derivative analysis center on studying charts company's price movement, outstanding positions and trading volume, as opposed to focusing on a company's fundamentals and, as such, may not match with a report on a company's fundamental analysis. In addition MOST has different business segments / Divisions with independent research separated by Chinese walls catering to different set of customers having various objectives, risk profiles, investment horizon, etc, and therefore may at times have different contrary views on stocks sectors and markets.
Unauthorized disclosure, use, dissemination or copying (either whole or partial) of this information, is prohibited. The person accessing this information specifically agrees to exempt MOSt or any of its affiliates or employees from, any and all responsibility/liability arising from such misuse and agrees not to hold MOSt or any of its affiliates or employees responsible for any such misuse and further agrees to hold MOSt or any of its affiliates or employees free and harmless from all losses, costs, damages, expenses that may be suffered by the person accessing this information due to any errors and delays. The information contained herein is based on publicly available data or other sources believed to be reliable. Any statements contained in this report attributed to a third party represent MOSt's interpretation of the data, information and/or opinions provided by that third party either publicly or through a subscription service, and such use and interpretation have not been reviewed by the third party. This Report is not intended to be a complete statement or summary of the securities, markets or developments referred to in the document. While we would endeavor to update the information herein on reasonable basis, MOSt and/or its affiliates are under no obligation to update the information. Also there may be regulatory, compliance, or other reasons that may prevent MOSt and/or its affiliates from doing so. MOSt or any of its affiliates or employees shall not be in any way responsible and liable for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. MOSt or any of its affiliates or employees do not provide, at any time, any express or implied warranty of any kind, regarding any matter pertaining to this report, including without limitation the implied warranties of merchantability, fitness for a particular purpose, and non-infringement. The recipients of this report should rely on their own investigations.

This report is intended for distribution to institutional investors. Recipients who are not institutional investors should seek advice of their independent financial advisor prior to taking any investment decision based on this report or for any necessary explanation of its contents.

Most and it's associates may have managed or co-managed public offering of securities, may have received compensation for investment banking or merchant banking or brokerage services, may have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past 12 months.
Most and it's associates have not received any compensation or other benefits from the subject company or third party in connection with the research report.
Subject Company may have been a client of Most or its associates during twelve months preceding the date of distribution of the research report
MOSt and/or its affiliates and/or employees may have interests/positions, financial or otherwise of over 1 % at the end of the month immediately preceding the date of publication of the research in the securities mentioned in this report. To enhance transparency, MOSt has incorporated a Disclosure of Interest Statement in this document. This should, however, not be treated as endorsement of the views expressed in the report.
Motilal Oswal Securities Limited is registered as a Research Analyst under SEBI (Research Analyst) Regulations, 2014. SEBI Reg. No. INH000000412

Pending Regulatory inspections against Motilal Oswal Securities Limited:
SEBI pursuant to a complaint from client Shri C.R. Mohanraj alleging unauthorized trading, issued a letter dated 29th April 2014 to MOSL notifying appointment of an Adjudicating Officer as per SEBI regulations to hold inquiry and adjudge violation of SEBI Regulations; MOSL replied to the Show Cause Notice whereby SEBI granted us an opportunity of Inspection of Documents. Since all the documents requested by us were not covered we have requested to SEBI vide our letter dated June 23, 2015 to provide pending list of documents for inspection.
List of associate companies of Motilal Oswal Securities Limited -Click here to access detailed report

Analyst Certification

The views expressed in this research report accurately reflect the personal views of the analyst(s) about the subject securities or issues, and no part of the compensation of the research analyst(s) was, is, or will be directly or indirectly related to the specific recommendations and views expressed by research analyst(s) in this report. The research analysts, strategists, or research associates principally responsible for preparation of MOSt research receive compensation based upon various factors, including quality of research, investor client feedback, stock picking, competitive factors and firm revenues

Disclosure of Interest Statement	CESC
▪ Analyst ownership of the stock	No
▪ Served as an officer, director or employee -	No

A graph of daily closing prices of securities is available at www.nseindia.com and http://economictimes.indiatimes.com/markets/stocks/stock-quotes

Regional Disclosures (outside India)

This report is not directed or intended for distribution to or use by any person or entity resident in a state, country or any jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject MOSt & its group companies to registration or licensing requirements within such jurisdictions.
For Hong Kong: This report is distributed in Hong Kong by Motilal Oswal capital Markets (Hong Kong) Private Limited, a licensed corporation (CE AYY-301) licensed and regulated by the Hong Kong Securities and Futures Commission (SFC) pursuant to the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) "SFO". As per SEBI (Research Analyst Regulations) 2014 Motilal Oswal Securities (SEBI Reg No. INH000000412) has an agreement with Motilal Oswal capital Markets (Hong Kong) Private Limited for distribution of research report in Kong Kong. This report is intended for distribution only to "Professional Investors" as defined in Part I of Schedule 1 to SFO. Any investment or investment activity to which this document relates is only available to professional investor and will be engaged only with professional investors." Nothing here is an offer or solicitation of these securities, products and services in any jurisdiction where their offer or sale is not qualified or exempt from registration. The Indian Analyst(s) who compile this report is/are not located in Hong Kong & are not conducting Research Analysis in Hong Kong.

For U.S.

Motilal Oswal Securities Limited (MOSL) is not a registered broker - dealer under the U.S. Securities Exchange Act of 1934, as amended (the"1934 act") and under applicable state laws in the United States. In addition MOSL is not a registered investment adviser under the U.S. Investment Advisers Act of 1940, as amended (the "Advisers Act" and together with the 1934 Act, the "Acts), and under applicable state laws in the United States. Accordingly, in the absence of specific exemption under the Acts, any brokerage and investment services provided by MOSL, including the products and services described herein are not available to or intended for U.S. persons.
This report is intended for distribution only to "Major Institutional Investors" as defined by Rule 15a-6(b)(4) of the Exchange Act and interpretations thereof by SEC (henceforth referred to as "major institutional investors"). This document must not be acted on or relied on by persons who are not major institutional investors. Any investment or investment activity to which this document relates is only available to major institutional investors and will be engaged in only with major institutional investors. In reliance on the exemption from registration provided by Rule 15a-6 of the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act") and interpretations thereof by the U.S. Securities and Exchange Commission ("SEC") in order to conduct business with Institutional Investors based in the U.S., MOSL has entered into a chaperoning agreement with a U.S. registered broker-dealer, Motilal Oswal Securities International Private Limited. ("MOSIPL"). Any business interaction pursuant to this report will have to be executed within the provisions of this chaperoning agreement.
The Research Analysts contributing to the report may not be registered /qualified as research analyst with FINRA. Such research analyst may not be associated persons of the U.S. registered broker-dealer, MOSIPL, and therefore, may not be subject to NASD rule 2711 and NYSE Rule 472 restrictions on communication with a subject company, public appearances and trading securities held by a research analyst account.

For Singapore

Motilal Oswal Capital Markets Singapore Pte Limited is acting as an exempt financial advisor under section 23(1)(f) of the Financial Advisers Act(FAA) read with regulation 17(1)(d) of the Financial Advisors Regulations and is a subsidiary of Motilal Oswal Securities Limited in India. This research is distributed in Singapore by Motilal Oswal Capital Markets Singapore Pte Limited and it is only directed in Singapore to accredited investors, as defined in the Financial Advisers Regulations and the Securities and Futures Act (Chapter 289), as amended from time to time.
In respect of any matter arising from or in connection with the research you could contact the following representatives of Motilal Oswal Capital Markets Singapore Pte Limited:

Varun Kumar
Varun.kumar@motilaloswal.com
Contact : (+65) 68189232
Office Address:21 (Suite 31),16 Collyer Quay,Singapore 04931

MOTILAL OSWAL
Motilal Oswal Securities Ltd
Motilal Oswal Tower, Level 9, Sayani Road, Prabhadevi, Mumbai 400 025
Phone: +91 22 3982 5500 E-mail: reports@motilaloswal.com