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3QFY12 appears weak; await colour on tax items

First Look

January 28, 2012

Rating Remains	**Buy**
Target price Remains	INR 206
Closing price January 27, 2012	INR 174

Prima facie, 3QFY12 normalized earnings disappoint…

At Rs20.1bn, NTPC's 3QFY12 normalized net profit appears 12% below our forecast (13% below consensus); at Rs30.5bn, normalized EBITDA missed our forecast by 14%. We peg NTPC's first-cut 3QFY12 normalized net profit by adjusting the reported PAT (Rs21.3bn, 7% below our forecast) for [1] prior period sales write-back of Rs1.6bn, [2] a one-off provision of Rs0.4bn relating to an exploratory oil/gas block, and [3] prior-period tax write-back of Rs3.1bn. Notably, NTPC has recommended an interim dividend of Rs3.5/share (implying a 2% dividend yield on 27 January closing price).

…treatment of the exaggerated tax 'refund' to customers holds key to interpretation of the result

Notes to accounts presented in NTPC's 3QFY12 earnings release indicates that sales included a 'negative' Rs4.07bn tax recoverable from customers (effectively a refund via adjustment in the tariffs) as per CERC's 2004-09 tariff regulations. Although such an adjustment typically recurs in NTPC's quarterly results and we deem the same to be 'normal' as tariff orders for NTPC's stations by the Regulatory bodies (CERC, APTEL) are issued through the year, arguably, the magnitude of this line item in 3QFY12 has had an exaggerated impact on the top line (and in turn, the EBITDA and the bottom line). If we were to adjust the reported financials for this line item as well, NTPC's 3QFY12 normalized net profit would appear at Rs24.1bn, ~5% ahead of our forecast.

What if our first-cut analysis holds good?

Going by our base-case assessment of NTPC's 3QFY12 normalized financials, we note: [1] realization appears to have dropped ~4.8% QoQ to below Rs3/kWh, partially on the back of a 3.7% QoQ drop in unit fuel cost and [2] pick-up in efficiency linked incentives appears subdued, particularly considering the ~1100MW of effective capacity accretion. Accordingly, our earnings estimates for NTPC would entail a downside risk.

As usual, adjustments enunciated in earnings call remain critical

Ahead of its earnings call (scheduled at 1600hrs IST on January 30), we maintain our earnings forecast for NTPC. We particularly await clarity on [1] key operating metrics, [2] dent from Rs4.07bn tariff-orders related tax incidence on reported revenues, and [3] capacity addition and captive mining related timelines. On our estimates, the stock trades at 1.8x FY13F P/B. Maintain BUY.

Fig. 1: NTPC – 3QFY12 Actual vs. Estimates

Prima facie, normalized PAT appears 12% below our forecast

NTPC - 3QFY12 (INR m)	Actual	Nomura Estimate	Actual vs. Est.	Cons. Estimate	Actual vs. Cons.
Sales	154,888	165,600	-6.5%	160,900	-3.7%
EBITDA	30,522	35,512	-14.1%	35,061	-12.9%
Adj. Net Profit	**20,119**	**22,950**	**-12.3%**	**23,124**	**-13.0%**
Reported PAT	21,304	22,950	-7.2%	23,124	-7.9%

Note: Consensus = Bloomberg mean estimates

Source: Company data, Bloomberg, Nomura estimates

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Fig. 2: NTPC – 3QFY12 Consolidated Earnings Summary

Marginal drop in normalized PAT despite ~1100MW higher effective commercial capacity and ~25% QoQ rise in non-operating income (net) is surprising

Quarterly Results (Rs million)	3QFY11 Dec-10	4QFY11 Mar-11	1QFY12 Jun-11	2QFY12 Sep-11	3QFY12 Dec-11	qoq (%)	yoy (%)	3QFY12F Dec-11	Actual vs Estimate
Revenues	**132,615**	**146,307**	**144,120**	**146,186**	**154,888**	**6.0%**	**16.8%**	**165,600**	**-6.5%**
Fuel cost	(83,386)	(97,256)	(97,498)	(100,597)	(107,933)	7.3%	29.4%	(113,988)	-5.3%
O&M expenses	(13,247)	(15,697)	(15,554)	(16,697)	(16,433)	-1.6%	24.0%	(16,100)	2.1%
EBITDA	**35,981**	**33,354**	**31,068**	**28,892**	**30,522**	**5.6%**	**-15.2%**	**35,512**	**-14.1%**
EBITDA Margin	*27.1%*	*22.8%*	*21.6%*	*19.8%*	*19.7%*	*-0.3%*	*-27.4%*	*21.4%*	
Depreciation	(5,986)	(6,981)	(6,411)	(6,583)	(7,560)	14.8%	26.3%	(7,241)	4.4%
EBIT	**29,996**	**26,372**	**24,656**	**22,309**	**22,962**	**2.9%**	**-23.4%**	**28,271**	**-18.8%**
Interest expense	(4,575)	(5,578)	(3,744)	(5,300)	(4,496)	-15.2%	-1.7%	(5,172)	-13.1%
Non operating income	6,694	6,642	7,328	9,015	9,121	1.2%	36.3%	7,500	21.6%
Profit before tax	**32,115**	**27,436**	**28,241**	**26,024**	**27,587**	**6.0%**	**-14.1%**	**30,600**	**-9.8%**
Tax	(9,983)	(2,063)	(7,065)	(5,612)	(7,468)	33.1%	-25.2%	(7,650)	-2.4%
Current	(8,317)	(5,603)	(7,483)	(7,207)	(6,432)	-10.8%	-22.7%	-	
Deferred	(1,667)	3,540	418	1,595	(1,036)	-165.0%	-37.8%	-	
Effective tax rate	*31.1%*	*7.5%*	*25.0%*	*21.6%*	*27.1%*	*25.5%*	*-12.9%*	*25.0%*	
Net Profit (normalized)	**22,132**	**25,374**	**21,176**	**20,412**	**20,119**	**-1.4%**	**-9.1%**	**22,950**	**-12.3%**
Extraordinary items	1,583	2,445	(418)	3,829	1,185	-69.1%	-25.1%	-	
Reported PAT	**23,715**	**27,818**	**20,758**	**24,241**	**21,304**	**-12.1%**	**-10.2%**	**22,950**	**-7.2%**

Source: Company data, Nomura estimates

Appendix A-1

Analyst Certification

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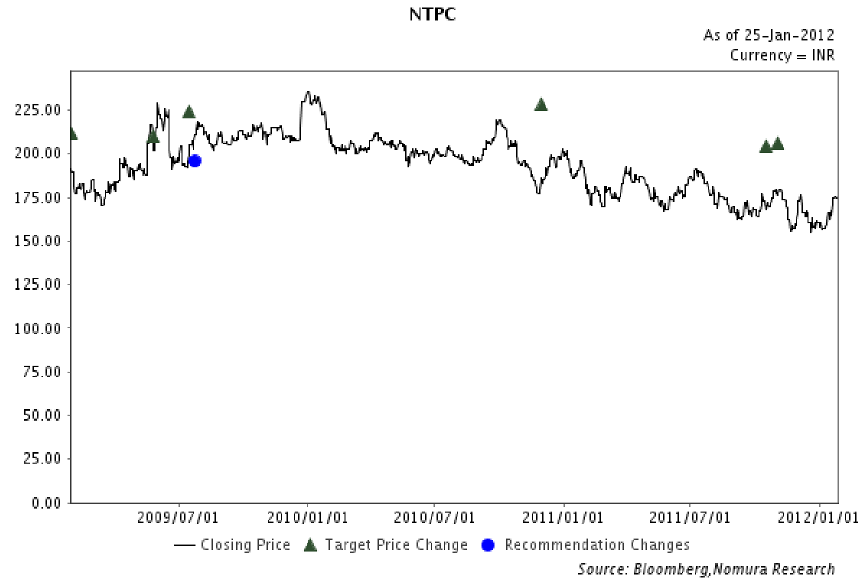
Issuer name	Ticker	Price	Price date	Stock rating	Sector rating	Disclosures
NTPC	NTPC IN	INR 174	27-Jan-2012	Buy	Not rated	

Previous Rating

Issuer name	Previous Rating	Date of change
NTPC	Neutral	15-Jul-2009

NTPC (NTPC IN) **INR 174 (27-Jan-2012)** Buy (Sector rating: Not rated)

Rating and target price chart (three year history)



Date	Rating	Target price	Closing price
03-Nov-11		206.00	178.10
17-Oct-11		204.00	168.25
01-Dec-10		228.00	186.35
15-Jul-09	Buy		199.00
15-Jul-09		224.00	199.00
26-May-09		210.00	201.60
29-Jan-09		212.00	190.25

For explanation of ratings refer to the stock rating keys located after chart(s)

Valuation Methodology Our TP of INR206 is a sum of the fair value of operating assets based on a residual income model (INR176), investment in JVs/subsidiaries (~INR10) and book value of FY12F non-operating financial assets (~INR21). Key assumptions of our model are 1) Cost of equity - 12.5%; 2) Terminal RoE - 18.5%; and 3) terminal growth rate - 2%.

Risks that may impede the achievement of the target price 1) Project execution delays; 2) lower coal supplies under already signed FSAs/LoAs; 3) reinvestment risk; and 4) adverse regulatory changes.

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