Tata Power

Jan-21

Key Assets

Asset	Regulated Equity (In Rs Mn)	RoE (FY20)	Remarks
Mumbai Operation (Generation and T&D)	39,520	Nmf*	regulated business and earns stable income
Jojobera	5,220	Nmf*	regulated business and earns stable income
Tata Power Delhi Distribution Ltd	15,410	12%	Cost-plus tariff regime with assured return
Maithon Power Ltd	14,400	16%	strong availability-based tariff structure provides regulated returns. tied up its entire capacity through long-term PPAs.
Industrial Energy Limited	7,160	18%	JV with Tata Steel. Operates coal-based plant in Jojobera and Jamshedpur
Powerlinks Transmission	4,670	13%	Assured sales under the transmission service agreement (TSA) which ensures payment of stipulated tariff subject to achievement of 98% line availability annually
	Net Assets (In Rs Mn)		
Coastal Gujarat Power Ltd (Mundra UMPP)	40,321	-20%	Since the commissioning of the plant, TPCL has infused around Rs 83 billion in the form of perpetual securities, equity, and inter-company loans. About 55% of the variable charges cannot be escalated.
Tata Power Renewable Energy Ltd	50,307	8%	Renewables asset . To be transferred to InVIT
Walwhan Renewable Energy Ltd	23,003	8%	Renewables asset . To be transferred to InVIT
Bhira Investments Ltd	20,345	47%**	Holding Company for Indonesian investments
Tata Projects	6,189	8%	Provides turnkey solutions related to urban and industrial infrastructure projects
other adjustments	-30,885	N.A	Adjustments arising out of consolidation

**Nmf- Tata standalone ROE includes other businesses and does not give clear picture of Mumbai and Jojobera Operations, **Avg ROE*

Regulated business

Regulated Book		
Total Regulated Book across distribution, generation and transmission	86,380	Rs million
- Mumbai	39,520	Rs million
- Delhi	14,400	Rs million
- Maithon	15,410	Rs million
Regulated RoE	15.5%	% of regulated equity
Additional incentives on performance and financial parameters	3-4%	% of regulated equity
Regulated tenure remaining (with possibility of renewal)		
Maithon	15	years
Distribution - Delhi	19	years
Distribution - Mumbai	9	years
Power Generation - Mumbai	4	years

At consolidated level, Tata Power's regulated equity of Rs 86,380 accounts for Rs 27 on per share basis. This book can be expected to provide steady cash generation and returns near cost of capital.

Regulated business

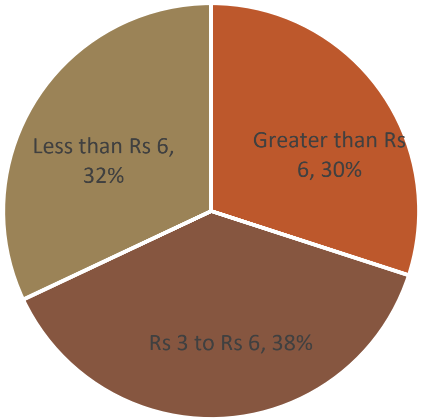
(in Rs mn)	FY16	FY17	FY18	FY19	FY20
Regulated Business EBITDA	40,662	37,886	39,600	41,933	33,229
Total EBITDA	55,090	54,755	58,164	62,169	70,415
As % of total EBITDA	**74%**	**69%**	**68%**	**67%**	**47%**

- EBITDA and EBITDA contribution from regulated business declined in FY-20 on:
  - lower generation and demand from procurers,
  - lower transmission charges as per the MERC tariff order and
  - the impact of the truing up order passed by MERC.

- According to management, FY-20 numbers are not sustainable and will recover.

- EBITDA contribution from regulated business has reverted to 61% of total EBITDA. The company has clocked Rs 13,360 mn EBITDA during H1 FY-21. While it is lower by 12% as compared to previous year, Q2 has shown signs of recovery with 9% growth.

Renewable Business



TPREL Consolidated (with WREL and SPVs

(In Rs mn)	FY17	FY18	FY19	FY20
Sales	9,854	17,453	20,458	21,768
Operating Profit	8,662	15,696	18,369	19,034
Operating margin	88%	90%	90%	87%
Interest	4,602	6,979	7,737	9,264
Interest coverage	2.0	2.3	2.43	2.31
ROE*	3.1%	5.3%	6.1%	2.8%
ROCE (%)	4.7%	8.0%	9.1%	7.7%
Total Debt/Equity(x)	1.67	1.65	1.58	1.89

*ROE calculation includes unsecured Perpetual Securities held by parent Tata Power. They are in the nature of equities.

- Tata Power's renewable operations consist of wind and solar assets across its standalone entity, Tata Power Renewable Energy Ltd (TPREL), Walwhan Renewable Energy Ltd (WREL) and Tata Power Solar Systems Ltd (Tata Power Solar).
- Tata Power's renewable capacity currently stands at 2.64 GW. With another 1.5GW of solar capacity in the pipeline. It plans to add ~2GW of incremental solar capacity every year. Along with inorganic growth, it targets of having ~15GW of renewable capacity by FY25E.
- With existing assets fetching low returns even with high per unit pricing of Rs 6.9, quality of growth may be a concern in current low per unit price scenario.
- In FY20, TPREL returns were lower due to a decline in profitability on higher interest costs and remeasurement of deferred tax in new regime. A decline in profitability was on the back of increased O&M costs, curtailment of power offtake in Andhra Pradesh, and increased finance charges due to higher borrowings.
- FY-21 onwards, tax rates are expected to be lower at 25%, helping improve profitability.

CGPL Dragging Tata Power's Performance

- Around 39% of Tata Power's total capital employed has been invested in CGPL & coal (coal subsidiaries in Indonesia which provide captive coal to CGPL). In addition to Rs 42,500 mn initial equity commitment, Tata Power has made additional investments of Rs 83,000 million till FY20 in the form of perpetual securities, equity, and inter-company loans.

- About 55% of the variable charges cannot be escalated. The high cost of imported coal and change in coal pricing regulations by the Indonesian government has contributed towards unviability of the project.

- The under recovery of fuel costs declined to Rs 0.46/kWh in FY20 compared to Rs 0.78/kWh in FY19. Cash flow is likely to remain exposed to fluctuations in coal prices, and losses, though reduced, may continue given the current unviable tariff structure.

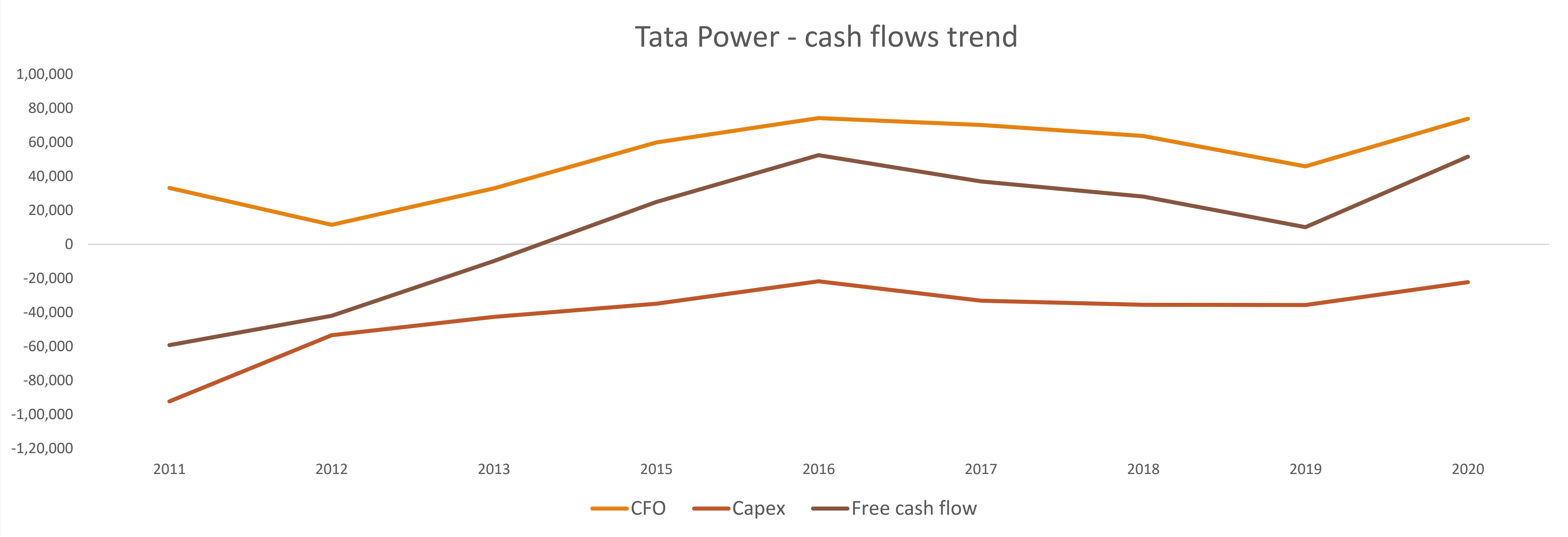
- In October 2018, the High Powered Committee (HPC) recommended sharing the losses incurred in CGPL between consumers, lenders, and developers. In January 2019, the Supreme Court also ruled that power purchase agreements (PPAs) could be amended with distribution companies subject to approval of the Central Electricity Regulatory Commission (CERC). As per the latest, the PPA is amended and approved by CERC. As per CRISIL report, if tariffs are revised inline with HPC, under-recoveries will reduce by 15-20 paise against current under-recovery of 46 paise per unit.

- In August 2020, Tata Power announced merger of CGPL with the parent entity will bring in significant tax savings and fiscal alignment through lower borrowing cost. CGPL has an accumulated loss of Rs 180,000 million which would be utilized in the merged entity to offset tax expenses.

CGPL Financials	FY17	FY18	FY19	FY20
EBITDA Margin	5.42%	-2.49%	-2.74%	11.55%
PAT Margin	-14.0%	-28.4%	-23.4%	-12.7%
ROE	-39.3%	-49.6%	-41.5%	-20.0%
ROCE	-1.21%	-6.73%	-4.75%	2.19%
Total Debt/Equity(x)	2.49	3.33	1.79	2.18
Interest Cover(x)	-0.26	-1.1	-0.63	0.24

LT EBITDA margin of NTPC = 31%

Cash flows

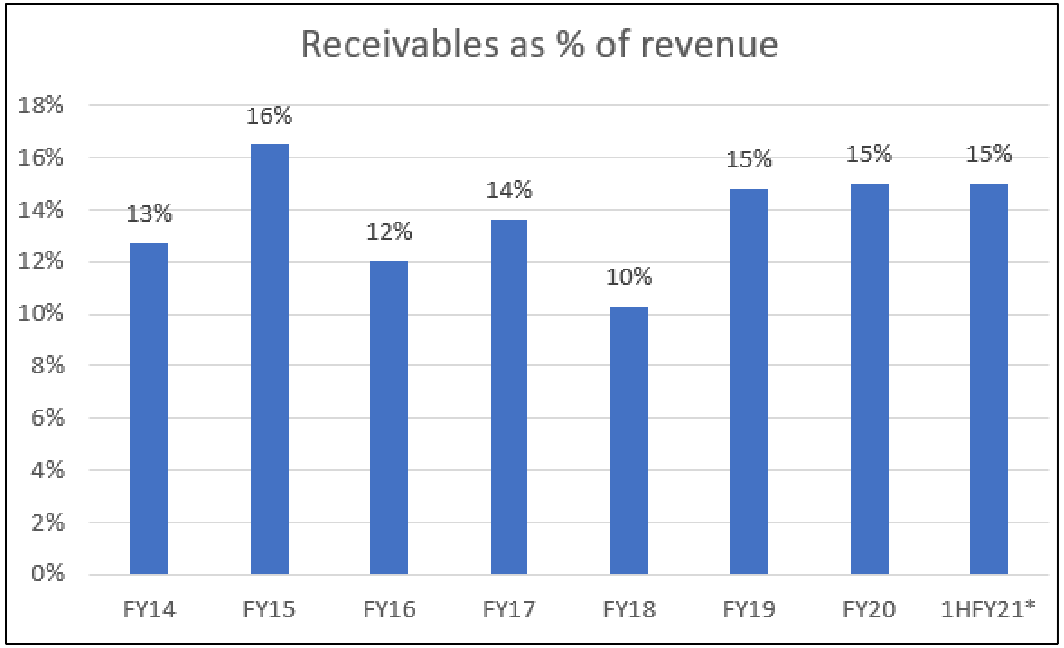


- After getting impacted between 2017 and 2019 due to lower profits from coal companies on account of lower FOB price, higher finance cost due to loss funding for CGPL (Mundra Operations). Cash flow generation appears to have improved again on the back of an improvement in performance of CGPL as losses declined from Rs 16,537 million in FY19 to Rs 8,905 million in FY20.

- Cash flows operations (CFO) from regulated business accounted for ~60% of the total CFO in FY20. In the last 4 years, CFO from regulated business remained consistent at ~62% of total.

Receivables

(In Rs mn)	FY14	FY15	FY16	FY17	FY18	FY19	FY20
Debtors more than Six months	3,216	4,140	7,182	8,249	12,919	10,516	16,441
As % of total receivables	7%	7%	20%	22%	46%	24%	37%
Reserve for doubtful debts	2,137	2,248	2,649	3,106	3,232	3,915	4,335
As a % of debtors o/s more than 6 months	66%	54%	37%	38%	25%	37%	26%



- In FY15, receivables as a % of revenue jumped to 16% from 13% in FY14. It increased mainly due to outstanding receivables from BEST (Mumbai Operations).

- Debtors outstanding more than 6 months as seen a steady increase from 7% in FY15 to ~37% in FY20. It increased sharply to 46% in FY18 from 22% in FY17 due to increased in receivables from defence business. However, over the years, receivables as % of revenue remained stable at around 15%.

- Even after Covid-19 impact in H1FY21, receivable days remained stable at 15% of sales (annualized).

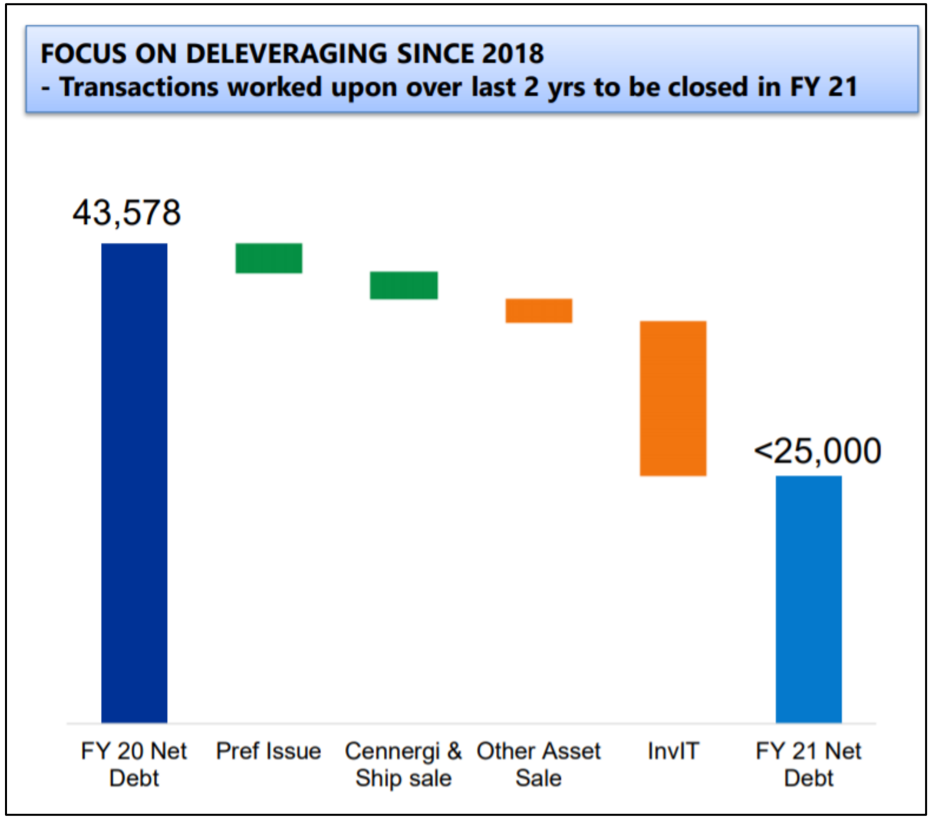
Debt/Equity

	2015	2016	2017	2018	2019	2020	1HFY21
Total Debt/Equity	3.2	3.1	4.5	2.7	2.6	2.6	1.8
Interest coverage (x)	1.4	1.4	1.1	1.3	1.5	1.2	1.5
Average Interest Cost (%)	9.5%	7.9%	7.6%	8.6%	10.1%	10.0%	10.6%*

*annualized

- The company has stepped up to reduce its leverage profile and managed to reduce Total Debt/equity from the highs of 4.5x in FY17 to 2.6x in FY20.
- In 2QFY21, the total Debt/Equity further reduced to 1.8x on the back of equity infusion, sale of non-core assets etc.
- On the back of debt reduction, Tata Power's interest coverage ratio has been improving from 1.1x in FY17 to 1.5x 1HFY21.
- The company's interest rate is increasing steadily. This, however, expected to decrease on the back of a decline in leverage, improvement in credit rating etc. CRISIL has upgraded its rating of The Tata Power Company Limited (Tata Power) to 'CRISIL AA' from 'CRISIL AA'-. This is on the back of deleveraging initiatives such as sale of non-core assets (South African wind asset and shipping business) and the preferential allotment of equity undertaken by the Company.

Deleveraging

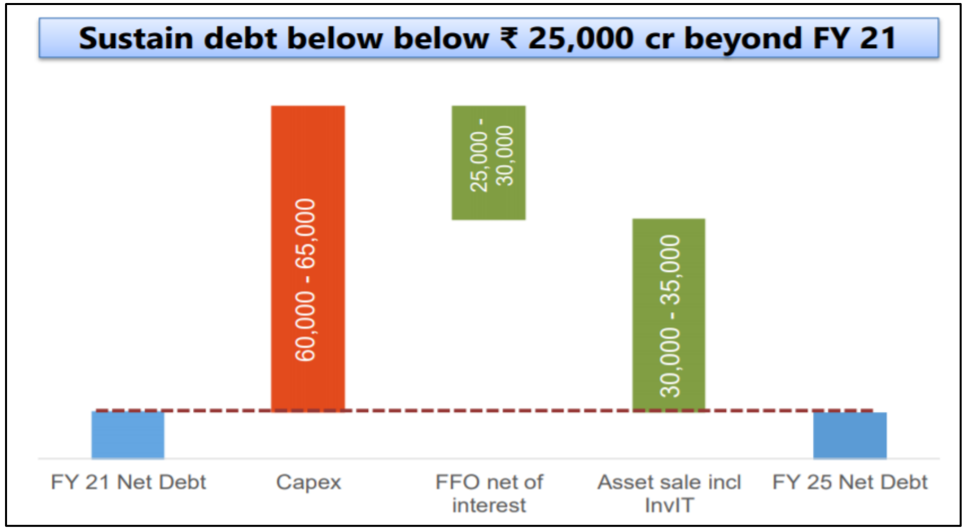


Source: Company presentation, Aug-20

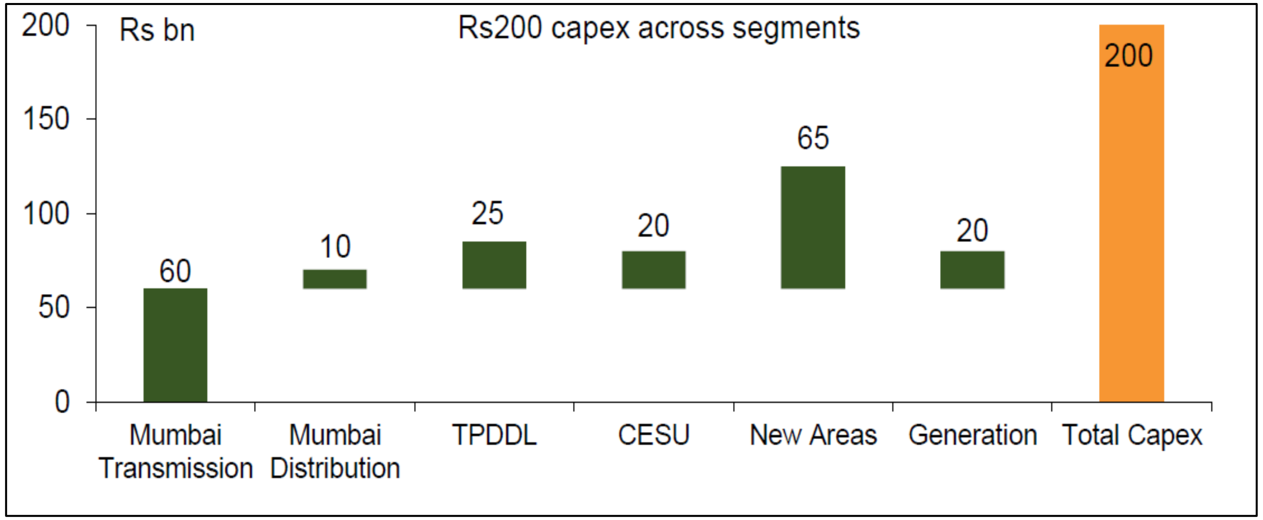
Type	Amount (in Rs Million)
Equity Infusion (Pref Issue)	26,000
Cennergi & Ship sale	23,310
Other asset sale	28,000
InVIT	1,10,000
Total	**1,87,310**

- In FY21, The company seen a meaningful reduction in the debt with the receipt of the balance consideration from ship sale, and completion of preferential equity issuance. The company also sold defense related business.
- Due to improvement in debt matrix, the Company saw an upgrade in its credit rating with CRISIL upgrading the long-term rating to AA stable, and ICRA changing the outlook to positive on its rating of AA-.
- Company is yet to execute InVIT of renewable assets though.

Capex Plan Beyond FY21



Source: Company presentation, Aug-20



Source: Emkay Report

- The company has laid out an Rs 200,000 million of capex plan across all three regulated business segments - generation, distribution and transmission - over FY21-25E with a D/E ratio of 70:30.
- As per the company presentation, the company expected to incur capex of Rs 600,000-650,000 million during the same period. This is likely capex for Tata Power and InVIT (combined). As per the broker report, going ahead, the company would be creating 100% SPVs for all the under construction and new solar projects, which would eventually be transferred to the InVIT portfolio 6-8 months after commissioning. Thus, in any given year, Tata Power consolidated company will have only 1.5-2 GW of newly commissioned capacity.
- However, there could be a challenge of matching InVIT cash flows with the company's capex needs. Huge chunk of the funding would come from asset recycling to InvIT and may carry risk of timing mismatch.

Capex Plan and Debt

If one were to assume all renewables related capex is routed outside of the company, company will still witness significant rise gross block by way of planned capex in retained businesses.

GFA Calculation	FY20	FY21	FY22	FY23	FY24	FY25
GFA	6,32,923	6,72,923	7,22,923	7,72,923	8,22,923	8,72,923
Capex		40,000	50,000	50,000	50,000	50,000

Based on consensus EBITDA estimates by brokers and the amount of OCF that company will have to forgo on transfer of renewables business to InVIT, it appears that the company's OCF will largely meet its capital expenditure targets as suggested above.

OCF Calculation		FY21	FY22	FY23
OCF as % of EBITDA		70,424	68,260	72,797
Less: OCF of renewables (TPRL Consolidated) +CSL +Indorama		13,743	15,804	18,175
OCF		**56,681**	**52,456**	**54,622**

<< Similar to capex requirements as above

There will be some additional income by way of dividends from InVIT. However, it is not expected to be large considering InVIT is expected to acquire 12GW of Tata Power's renewable assets over next 4 years.

Capex Plan and Debt

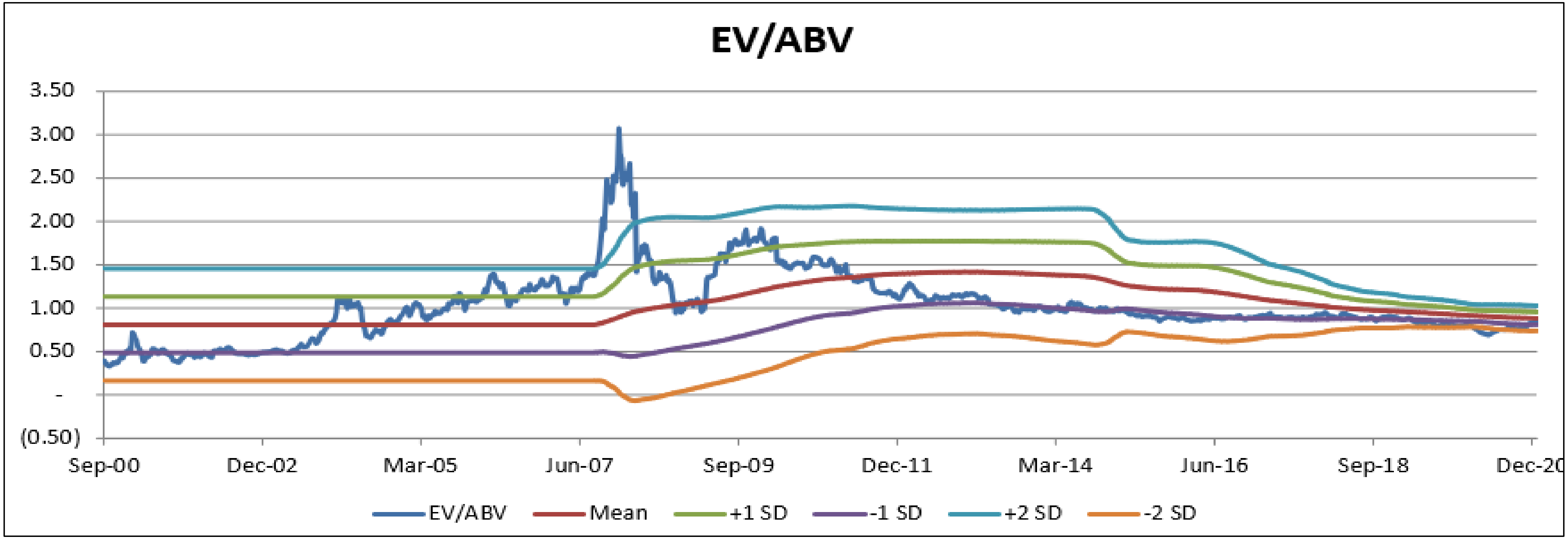
Does not include new renewable capex

Net Debt Calculation	FY20	FY21	FY22	FY23
Debt	5,35,528	2,46,812	2,67,845	2,95,257
Cash and Invt	27,269	44,407	42,415	40,410
Asset Sale				
- INVIT		99,195		
Consideration from sale of other non-core assets		59,496		
Gain - on sale of assets		19,980		
Equity Infusion		26,000		
Invit Debt Transfer		1,14,457		
Capex (70% Debt)		-28,000	-46,242	-52,500
OCF-Interest		**19,520**	**28,010**	**27,875**
OCF		56,681	52,456	54,622
Interest		-37,161	-24,446	-26,747
Dividend (Tata Power Shareholders)		-4,793	-4,793	-4,793
Net Debt	**5,08,259**	**2,02,405**	**2,25,430**	**2,54,847**

- Debt levels of the company are thus expected to remain steady and may be even rise gradually over next few years, once company hives off its renewable energy business via InVIT.
- The company may be required to carry additional investments in SPVs of renewable energies till the time they are transferred to InVIT.
- A lot of deleveraging thus depends upon company's ability to sell its renewable energy business and its ability to execute and sell its planned capex in renewable space.
- Overall, if company intends to go ahead with its planned expansion, it is likely that cash generations will remain low and debt will remain steady or rise gradually.
- The earnings growth (at higher pace) is thus likely to be a one-time bump up.

Note that this and above slides calculations and estimates are based on consensus estimates and other back of the envelope workings. They are done to get a sense of company's cash and debt direction.

Valuation - ABV



EV/ABV			
Range		-1 SD	+1 SD
		Low	High
Multiple		0.81	0.96
EV/ABV - 2021		68	116
EV/ABV - 2022		86	122

- The company had seen major “de-rating” over the years. Issues over last 2-3 years aggravated de-rating. This is due to rising debt levels, loss making operations at Mundra UMPP, etc.

ABV – Key value driver – is likely to grow at slow pace

EV/ABV Calculation	FY20	FY21	FY22	FY23
ABV - Total for firm	8,83,499	6,36,761	6,80,926	7,25,408
Net Debt	5,08,259	2,02,405	2,13,630	2,23,514
Minority Interest	23,320	23,320	23,320	23,320
ABV - Total for shareholders	3,51,920	4,11,036	4,43,976	4,78,574
Average 'Shares' Outstanding - diluted	2,706	3,195	3,195	3,195
ABV per share	**130.0**	**128.6**	**138.9**	**149.8**

Scenario 1 – The company can reduce its debt via InVIT and improve earnings sustainably, the company can return to "normal" distribution as opposed to de-rating that it saw in last few years. Valuation range can thus revert to:

EV/ABV	FY21	FY22	FY23
Low (- 1 SD)	91	99	107
High (+1 SD)	120	129	140

Scenario 2 – The company additionally can execute and start showing growth in its beyond FY-22 / FY-23.

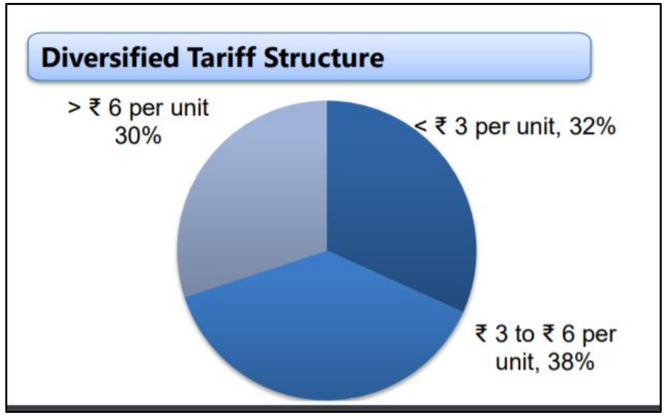
EV/ABV Range	FY21	FY22	FY23
Low (mean)	105	114	123
High (+2 SD)	134	145	156

<u>Failure to sell renewable assets via InVIT at expected valuations remains biggest immediate risk.</u>

Risks and Concerns

1. Decline in Tariff Structure-

30% of the capacity is above Rs 6 per unit. Any decline/re-negotiation in tariff would impact margins and profitability. For example, the average tariff for WREL (Renewable subsidiary) remains high at Rs 6.9/kWh. With distribution utilities trying to optimise power purchase costs, any effort for the renegotiation or termination of PPAs will be a key risk.



2. **Slow progress in resolution of tariff issue for CGPL-**

Continued delay in implementation of revised tariff for Mundra UMPP, coupled with the inability to generate dividend inflow from coal mining companies could lead to net operating losses and large support requirement. Company continues to under-recover on fuel.

3. Scale up renewable energy could be a challenge

Improvement in financials of state discoms is key to Tata Power's renewable energy portfolio scale-up plans as well as recycling assets in the InvIT. Buyer's reluctance to pay higher tariffs is a big challenge.

4. InVIT

Inability to sell renewable assets at expected valuations. Company may even have to fund initially towards the projects that will be ultimately transferred to InVIT. This can put additional pressure on balance sheet.

Technical Chart – near term momentum

Technical chart appears strong but is now near resistance zone of Rs 85-90, but no signs of weakness yet.
Chart appears to have completed its ABCD pattern (technique that we use) at these levels based on weekly prices and thus may have limited upside.
It may still have additional upside till Rs 90-91 based on daily prices.

To conclude

Regulated business – remains good quality assets. Per share value of regulated utility is ~Rs 27 per share. Bidding for similar businesses in new areas can be positive.

Mundra plant and coal blocks – things can improve on HPC recommendation implementation. However, company may not be in position to recover full losses. Cash flows remain dependent upon price of imported coal. Project remains unviable for the time being. Large portion of company's capital is thus deployed in business that requires additional cash to sustain. Merger with Tata Power (parent) can be positive to some extent as it can lower overall taxes for the company.

Renewable assets – Does not appear to generate adequate returns if we consider perpetual instruments held by Tata Power. Selling these assets to InVIT remains key to lower debt as well as interest costs of the company.

New Capex – Company has big capex plans till 2025. Execution of which is likely to require external capital.

Valuation – After witnessing de-rating, company has witnessed improvement in multiples on lower losses of Mundra plant as well as expected improvement in balance sheet and earnings on lower interest costs.

In a scenario of successful improvement in balance sheet and resultant earnings, company can be expected to revert to regular -1SD to +1SD band of Rs 99 – 129 for FY-22.

In a scenario where company is also able to provide high confidence execution on capex and assets growth beyond FY-22/23, EV/ABV can even quote between Mean and +2SD range of Rs 114 – 145 for FY-22.

In scenario where company is unable to improve its balance sheet by selling renewable assets, it can revert to -2SD valuations of Rs ~Rs 53 for FY22.

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