

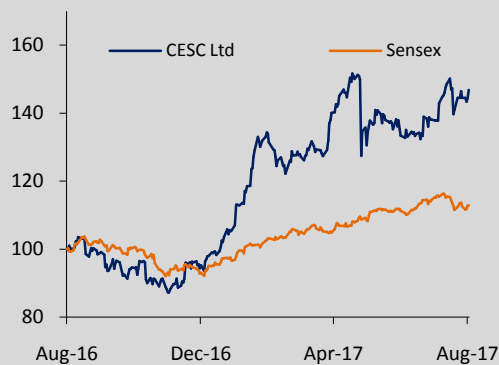
| | |
|----------------|---------------------|
| Sector | Power/Miscellaneous |
| Recommendation | BUY |
| Upside | 22.5% |

| Stock Data | |
|----------------------|-------------|
| Sensex | 31,596 |
| 52 Week h/l (Rs): | 1,002 / 539 |
| Market cap (Rs Cr) : | 12,721 |
| BSE code: | 500084 |
| NSE code: | CESC |
| FV (Rs): | 10.0 |
| Div yield (%): | 1.0 |

| Shareholding Pattern | | | |
|----------------------|--------|--------|--------|
| | Dec-16 | Mar-17 | Jun-17 |
| Promoters | 49.9 | 49.9 | 49.9 |
| DII+FII | 41.9 | 41.4 | 40.9 |
| Individuals | 8.1 | 8.7 | 9.2 |

Source: Source: www.bseindia.com

Share Price Trend



Prices as on 24/08/2017

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De-merger to streamline business segments

CESC is demerging its business segments into four separate entities: Power generation, Power distribution, Retail and CESC ventures (business process outsourcing - Firstsource Solutions, Quest mall and other businesses). Post the de-merger, CESC along with the other three entities, will be listed on the stock exchanges, with a similar shareholding pattern of CESC. The entire process is expected to be completed by October 1, 2017.

First-listed Power Distribution Company, generation business to provide consistent returns

Power contributes ~60% (FY17) to the consolidated sales of CESC. Its core business Power distribution will be the first distribution entity to be listed in India. CESC's distribution business has high RoE @15.5% and is growing at a steady rate of ~6%. We are bullish on regulated power distribution business as it is steady and attractive, requiring less capital infusion and minimal government intervention. CESC also plans to pursue asset light distribution franchise model. In FY17, it has already won franchise in few cities in Rajasthan and plans to grow in other states as well. With respect to power generation, the total capacity with PPAs is ~ 2.0 GW. The performance of Haldia plant continues to be strong with PAT of Rs 296 cr (up 27% YoY) in FY17. Also, Chandrapur plant's performance is likely to improve as the company is trying to convert short term PPA of 270MW unit with the Maharashtra government to a long term one. We expect regulated power generation business to continue to generate 16-17% RoE over the next two years.

Rebound in Retail business through expansion, bright prospects for CESC ventures

Spencer Retail reported same store sales growth of ~ 9% YoY and store EBITDA of Rs 101/sqft per month (up 19% YoY) in FY17. The company plans to open 11 new stores in FY18 and add 0.2 mn sq.ft. p.a over the next two years. Its recent entry into high margin apparel business under the brand "2Bme" will support profit growth going forward. We believe that de-leveraging, expansion and operating leverage are likely to drive 12% sales CAGR (over FY17-19E) and break even (at PAT) in FY18E in Retail.

CESC's fourth entity- CESC Ventures' growth will be driven by Quest Mall (PAT CAGR of 20% over FY17-19E) and Firstsource Solutions (sales growth @8.5% CAGR over FY17-19E through new deal wins).

Outlook & Valuation

We believe the demerger is a step in the right direction as each business has varied risk and return profile and different working capital requirements. We believe that the demerger will lead to re-rating of multiples in each of its businesses and expect investors to benefit from value unlocking. We have valued the company on SOTP basis and arrived at a Target Price of Rs 1,172. We recommend Buy on the stock.

Financial Summary

| Consolidated ₹ cr | FY16 | FY17 | FY18E | FY19E |
|-------------------|--------|--------|--------|--------|
| Revenue | 12,124 | 13,904 | 14,993 | 15,263 |
| YoY Growth % | 9.6 | 14.7 | 7.8 | 1.8 |
| EBITDA Margin % | 27.1 | 22.4 | 22.9 | 24.3 |
| PAT | 729 | 810 | 1,048 | 1,205 |
| YoY Growth % | 268.2 | 11.1 | 29.4 | 15.0 |
| EPS (₹) | 54.8 | 60.9 | 78.8 | 90.6 |
| P/E (x) | 17.5 | 15.7 | 12.1 | 10.6 |
| ROE % | 12.1 | 11.3 | 13.0 | 13.3 |

Source: Company, IIFL Research

SOTP Valuation

| Segments | Business | Valuation Method | Valuation Multiple | **Value Per Share |
|---------------------------------------|------------------------|------------------|--------------------|-------------------|
| Power Standalone* | Gen & Distribution | P/E | 9.0 | 602 |
| Haldia | Gen & Transmission | EV/EBITDA | 5.0 | 149 |
| Chandrapur | Generation | P/BV | 0.8 | 77 |
| Power | | | | 828 |
| Spencer | Retail | EV/Sales | 0.8 | 174 |
| Firstsource Solutions | IT/Business Processing | P/E | 10.0 | 101 |
| CESC Ventures-Property (Quest) | Mall | P/E | 6.0 | 70 |
| Target Price | | | | 1,172 |

*Includes Kolkata Distribution and few generation assets

**Valuation based on current O/S shares – 13.3 cr

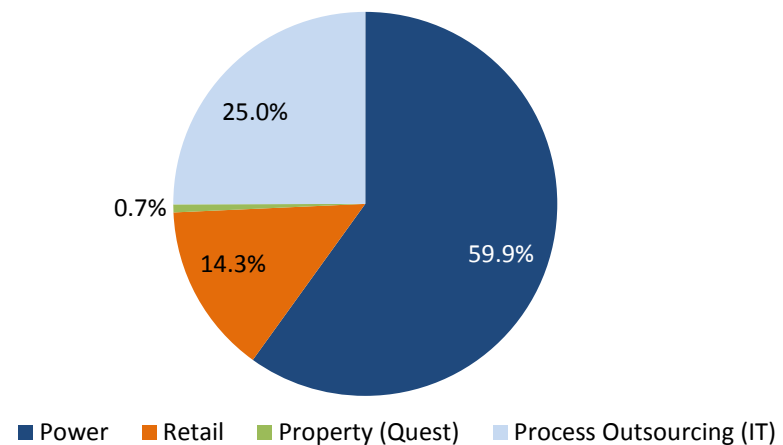
Source: Company, IIFL Research

Company Background

CESC is the flagship company of the RPG Group and is the sole power distributor in Kolkata. CESC has four main business segments: power generation and distribution, Spencer retail business, IT business and real estate. CESC's power business generates and distributes 1.8GW power annually to 3.0 mn consumers in Kolkata and Howrah; it has a generation capacity of 1125 MW (all coal based). The company's licensee area is 567 sq. km. Additionally; CESC has a 2x300 MW thermal power plant at Haldia in West Bengal operated by its subsidiary Haldia Energy Limited (HEL). The company also has a 2x300 MW thermal power plant at Chandrapur in Maharashtra, run by its step down subsidiary - Dhariwal Infrastructure Limited (DIL).

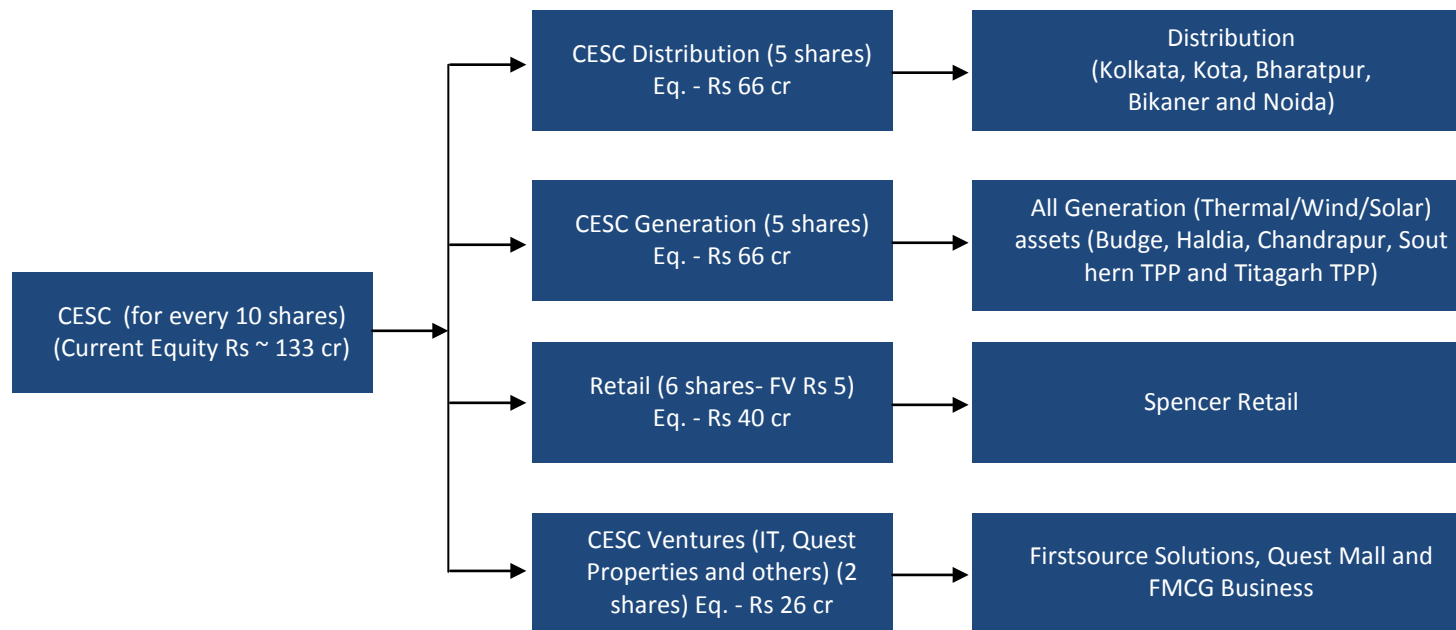
In the Retail segment, CESC operates 125 stores having a total area of 1.2m sq ft across India through its 100% subsidiary Spencer Retail. Further, it also operates Quest-a high-end luxury mall in Kolkata with retail area of 0.4m sq. ft. CESC has a controlling stake of ~55% in Firstsource Solutions Ltd. (FSL), a leading global BPO company.

Consolidated revenue break-up FY17



Source: Company, IIFL Research

De-merger Structure



Source: Company, IIFL Research

Current Equity Capital of CESC of Rs 132 cr will increase to Rs 198 cr post de-merger. Hence, shareholders will get additional ~ Rs 66 cr (cannot be termed as bonus) when they receive fresh shares of the four demerged entities.

Recommendation Parameters for Fundamental/Technical Reports:

Buy – Absolute return of over +10%

Accumulate – Absolute return between 0% to +10%

Reduce – Absolute return between 0% to -10%

Sell – Absolute return below -10%

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