



India Grid Trust Initiating Coverage

MARKET DATA - BGAL

Networth Post Money (₹Cr)	2,600
P/BV Ratio (FY17E) (x)	1.0x
EBITDA FY17 (₹Cr)	441
Market Price (₹)	96.3
Enterprise Value (₹Cr)	8.2x
Market Capitalisation (₹Cr)	2,500

AVERAGE MONTHLY VOLUME ('000)

BSE	220
NSE	452

SHAREHOLDING PATTERN POST IPO

Sponsor	Others
15%	85%

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India Grid (IndiGrid) is an infrastructure investment trust ("InvIT") established to own inter-state power transmission assets in India. IndiGrid was established on October 21, 2016 by its Sponsor, Sterlite Power Grid Ventures Limited. Its sponsor is one of the leading independent power transmission companies operating in the private sector, with extensive experience in bidding, designing, financing, constructing and maintaining power transmission projects across India.

Highly stable cash-flows with a high degree of predictability

Power transmission assets provide a predictable and stable cash flow devoid of price, off-take and execution risks. We believe these low risks warrant a low discounting rate of ~200 bps premium to G-Sec yields.

High pay-out ratios to guarantee stable yields for investors

In accordance with the InvIT Regulations, IndiGrid is required to distribute at least 90% of its net cash available for distribution to its Unit holders once at least every six months in every financial year. It believes its financial position will enable it to offer stable distributions to its Unit holders and finance its growth plans in the coming years. IndiGrid has been given a Corporate Credit Rating AAA/Stable by CRISIL, 'IND AAA'/Stable by India Ratings and "IrAAA" (pronounced as IR triple A) by ICRA.

Market seems to be mispricing risk, has higher return expectations

The IPO had a subdued listing and currently trades ~3.5% below its allotment price primarily because of higher return expectations inherent in the equity markets. However given the extremely low risk and near term projected yields of ~12% pre-tax we believe the opportunity would be attractive to fixed-income investors.

Market not pricing in any probability for sponsors future pipeline

In order to manage any potential competition and conflicts of interest that may arise between the Sponsor and IndiGrid in relation to any interests in transmission business, the Sponsor has entered into a ROFO Deed with the Trust. This deed gives a potential to acquire 8 more assets from the Sponsor in the coming years. These assets provide predictable and stable cash flows devoid of price, off-take and execution risks.

Key Risks

- The yield on India Grid Trust is irrespective of interest rates in broader economy and is extremely long dated ~FY49. A ~1% change in interest rates would inversely affect the fair value of the trust by ~16%
- The Trust assets are also exposed to low probability operational risks such as, system breakdowns, labour disturbances, equipment theft etc.

Financial Outlook & Valuation

As on March 2017, the assets to be acquired by the InvIT have a debt of Rs.36.7bn, of which ₹25.7bn was external debt, while the rest was sub debt/NCDs subscribed by the Sponsor. Post the IPO, the debt of the InvIT Trust will be ₹10bn (external). Of ₹26.7bn of debt repaid, ₹23.0bn would be through IPO Proceeds, while ₹4.2bn could be converted into units to the Sponsor. The assets are valued at an EV of ₹36.5bn-37.0bn and trade at a P/BV of ~1.0x as compared to PowerGrid which trades at a P/BV of ~2.0x accounting for future growth prospects and the ability to re-deploy capital. Power transmission assets have a life-time ROE of ~15% (ex-costs) thereby ensuring a healthy yield for trust holders with negligible risks.

We value India Grid Trust using a ~35 year DCF and value the units at INR 109 using a discount rate of 9%. At CMP the units have an underlying YTM of 10.5%

We thereby Initiate coverage on the India Grid Trust with a **buy rating** and believe the mispricing of the asset post IPO creates a highly favorable risk reward scenario for investors seeking low risk yields.



Overview

Issue proceeds will be utilized towards reduction of debt of both the projects. Both transmission assets are operational and will distribute at least 90% of net cash available for distribution to InvIT unit holders. Transmission assets, in general, have reasonably higher certainty of cash flow with assured tariffs. The cash flow will improve as and when new projects are acquired by the Trust.

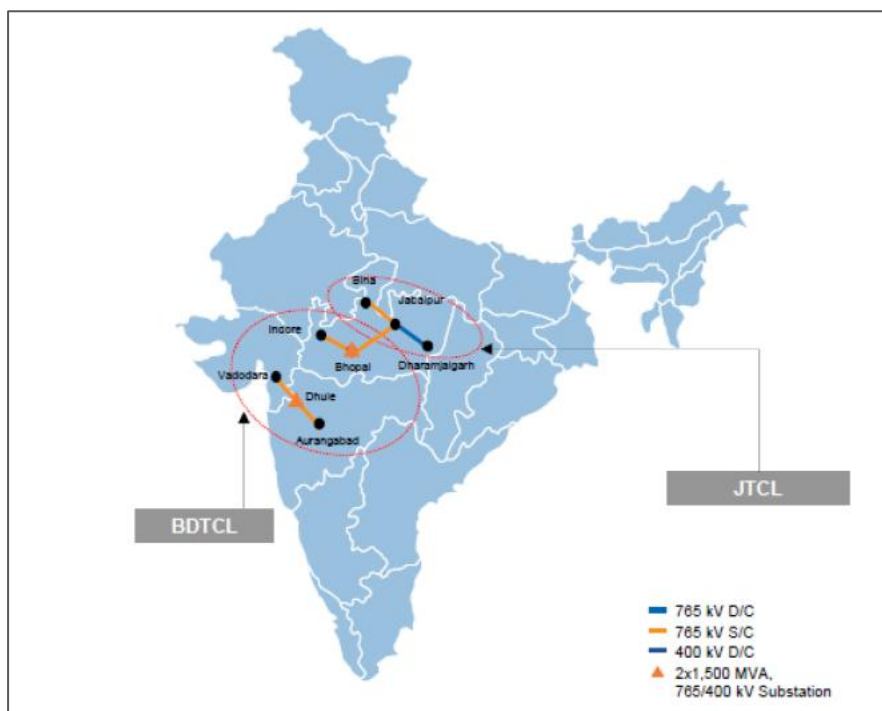
Operational Highlights

- Revenues are derived out of contracted tariffs under long term contracts (up to 35 years) from assets with relatively low operating and maintenance costs
- Inter-state power transmission projects receive tariffs for availability, irrespective of the quantity of power transmitted through the line thereby generating pre-determined returns
- Power transmission projects are characterized by low levels of operating risk. Portfolio assets are operational power transmission projects with an operating history and no construction risks or major capital expenditure requirements

Summary description of initial portfolio assets

Project Name	Transmission line/sub-station Configuration		Route Length (ckms)	Expiry of term of the TSA
Bhopal Dhule Transmission Company Limited	Bhopal-Indore	765 kV S/C transmission line	176	March 31, 2049
	Dhule-Aurangabad	765 kV S/C transmission line	192	
	Dhule-Vadodara	765 kV S/C transmission line	263	
	Bhopal-Jabalpur	765 kV S/C transmission line	260	
	Dhule-Dhule	400 kV D/C transmission line	36	
	Bhopal-Bhopal	400 kV D/C transmission line	17	
	Bhopal substation	2 x 1,500 MVA 765/400 kV	-	
	Dhule substation	2 x 1,500 MVA 765/400 kV	-	
Jabalpur Transmission Company Limited	Jabalpur-Dharamjaygarh	765 kV D/C transmission line	757	March 31, 2049
	Jabalpur-Bina	765 kV S/C transmission line	235	

Location of initial portfolio assets





Valuation

DCF Assumptions	Quantum	Rationale
Discount Rate	9%	50 bps premium to cost of debt
Estimated Annual Revenues (0% Growth)	445	ROE linked, as per CERC tariff orders
Escalation in Op-ex	5%	Inflation linked
Perpetual Debt on Balance Sheet (INR Cr)	1000	As per DRHP
Cost of Debt	8.5%	Existing cost
Pre- Tax YTM at CMP of 96.3 at a 100% pay-out	10.5%	Output
Valuation at 9% discount rate	109	Output Target Price per Unit

We value India Grid Trust using a ~35 year DCF and value the units at INR 109 using a discount rate of 9%. At CMP the units have an underlying YTM of 10.5%

Sensitivity Analysis:-

Discount Rate	Value of Unit
7.0%	134
7.5%	127
8.0%	121
8.5%	115
9.0%	109
9.5%	104
10.0%	99.7
10.5%	95.2
11.0%	91.1

Being a long dated instrument, the valuations shall be inversely co-related with interest rates in the broader economy which shall in-turn affect return expectations and capital values.

Taxation

Income Head	Tax Payable by Trust	Tax Payable by Investor
Income from core-transmission operations	Nil (No Dividend Distribution Tax Payable)	Payable as per respective tax bracket, to the extent to which income is distributed
Non-Core Interest Income	Payable by Trust	Nil
Non-Core Capital Gains/ Dividend Income/ Other Treasury Income*	Payable by Trust	Nil
Capital Gains on sale by the Unit Holder	Nil	STCG is applicable if the unit is held for a period less than 3 years

*Dividends paid out from proceeds of other income arising out of capital gains or dividends would be subject to Dividend Distribution Tax. The same would however be minimal as the trust is unlikely to have any investments as a minimum of 90% of cash generation must be paid out to unit holders.

The trust structure reduces the burden of double taxation; as there are no dividend distribution taxes or taxes paid by the trust on core operational earnings. Taxation would be in the hands of the unit holders as per their respective tax slabs.

Recommendation

We thereby Initiate coverage on the India Grid Trust with a **buy rating** and believe the mispricing of the asset post IPO creates a highly favorable risk reward scenario for investors seeking healthy yields with minimal risk.



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