

Day Break

Friday, 06 October 2017

COMPANY UPDATE

THE HUB POWER COMPANY LIMITED
 POWER GENERATION & DISTRIBUTION

Recommendation	BUY
Target Price:	136.6
Last Closing:	5-Oct-17 108.0
Upside:	26.5
Valuation Methodology:	Dividend Discount Model (DDM)

Time Horizon: Jun-18

Market Data

Bloomberg Tkr.	HUBC PA
Shares (mn)	1,157.2
Free Float Shares (mn)	752.2
Free Float Shares (%)	65.0%
Market Cap (PKRbn USDmn)	124.9 1,185.3
Exchange	KSE 100
Price Info.	90D 180D 365D
Abs. Return	(4.1) (15.7) (7.5)
Lo	110.2 110.2 103.2
Hi	125.9 136.6 145.4

Key Company Financials

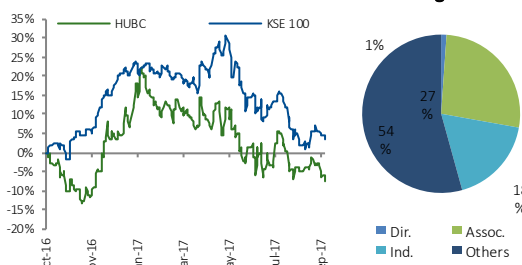
Period End: Jun

PKRbn	FY16A	FY17A	FY18E	FY19F
Total Revenue	91.6	101.2	109.2	113.9
Net Income	11.90	10.7	12.5	13.3
EPS (PKR)	10.3	9.2	10.8	11.5
DPS (PKR)	11.0	7.5	8.0	9.0
Total Assets	153.8	159.6	166.6	146.4
Total Equity	31.2	32.6	33.3	34.1

Key Financial Ratios

ROE (%)	38.1	32.8	37.6	39.1
P/E (x)	10.5	11.7	10.0	9.4
P/B (x)	4.0	3.8	3.7	3.7
DY (%)	10.2	6.9	7.4	8.3

Relative Price Performance & Shareholding



About the Company

The Company was incorporated in Pakistan on August 01, 1991 as a public limited company. Its GDR are listed on the Luxembourg Stock Exchange. The principal activities of the Company are to develop, own, operate and maintain power stations.

Source: Bloomberg, PSX & IGI Research

Abdullah Farhan

Research Analyst

Abdullah.farhan@igi.com.pk

Tel: (+92-21) 111-234-234 Ext.: 912

Power Generation & Distribution

HUBC: Estimates revised on new project details; maintain 'BUY'

- The Hub Power Company Limited's (HUBC) reported 4QFY17 consolidated earnings of PKR 3.28bn (EPS PKR 2.7) down 12%YoY, resultantly taking FY17 NPAT to PKR 11.34bn (EPS PKR 9.24), down 10%YoY. FY17 DPS came in at PKR 7.5/share.
- We have revised upwards earnings estimates for HUBC based on lower debt financing for equity stake in CPHGCL. Revealed in FY17 financials; HUBC is anticipated to reduce reliance on debt financing for 46% equity stake (Ex. 1.5% Baluchistan stake) in CPHGCL, where c.15% of US\$238mn is likely to be financed internally. While this may strain dividends over the medium-term, we raise EPS estimates by +4% to cater in lower finance expense, where early COD may further dilute impact.
- While we revise upward our EPS estimates, our TP is driven down by valuation rollover to FY18E. Thus we maintain "BUY" call on the company with our new TP of PKR 136.6/share (down by 2%), offering a potential upside of +27%. HUBC trades at an FY18E D/Y of 7.4%.

FY17 earnings drop 10%YoY to PKR 9.24/share, DPS clocks in at PKR 7.5

The Hub Power Company Limited's (HUBC) reported 4QFY17 consolidated earnings of PKR 3.28bn (EPS PKR 2.7) down 12%YoY, resultantly taking FY17 NPAT to PKR 11.34bn (EPS PKR 9.24), down 10%YoY. Results were accompanied with final cash dividend of PKR 2.5/share, taking full-year payout to PKR 7.5/share (payout ratio: 81%- lowest since FY12). Going forward, strain on dividend payout may continue as HUBC looks towards internal financing for equity stake in its associated undertakings (namely: CPHGCL).

We attribute decline in 4QFY17 earnings to planned overhaul carried out at the Narowal plant (8 out of 11 engines) which gave rise to higher stores and spares cost. This was in addition to lower dispatch (FY17: 64%) at Hub plant on load curtailment by National Power Control Centre which was partially moderated by 71%/58% utilization at Narowal and Laraib respectively. FY17 receivable position deteriorated further to PKR 85bn, levels last seen in FY12 (pre-PML-N) when circular debt ballooned to 480bn. This consequently increased reliance on working capital financing where ST Borrowings clocked in at PKR 24.8bn, up +50%YoY.

Exhibit:

Financial Highlights (Consolidated)

PKR mn	4QFY17	4QFY16	YoY	FY17	FY16	YoY
Turnover	27,049	21,843	24%	101,188	91,595	10%
Gross Profit	4,829	5,336	-10%	17,260	18,582	-7%
General & Admin expenses	385	388	-1%	1,365	1,262	8%
Financing Cost	998	986	1%	4,081	4,133	-1%
EBT	3,407	3,944	-14%	11,708	12,773	-8%
PAT	3,284	3,826	-14%	11,349	12,502	-9%
PAT - Attributable to HUBC	3,120	3,560	-12%	10,689	11,903	-10%
EPS (PKR)	2.70	3.08		9.24	10.29	
DPS (PKR)	2.50	3.00		7.50	11.00	

Source: Company Financials & IGI Research

No of Shares: 1,157.15 mn

Exhibit: Time line of Projects

Project	Financial close	Commerical Operation
CPHGC	Jun-17	Aug-19
TEL	Construction to start between Apr-Jun 2017	
SECMC	Apr-16	Jun-19

Exhibit: Segment-wise Profitability (PKR/share)

Segment	4QFY17	4QFY16	FY17	FY16
Hub Plant	1.84	2.14	7.39	8.13
Narowal Plant	0.70	0.76	1.86	2.12
Laraib	0.58	0.69	1.71	1.55
HPSL	0.07	(0.00)	0.10	0.09
Elimination/Unallocated	0.50	0.50	1.82	1.60
HUBC Earnings	2.70	3.08	9.24	10.29

Exhibit: Generation Plant-wise (Gwh)

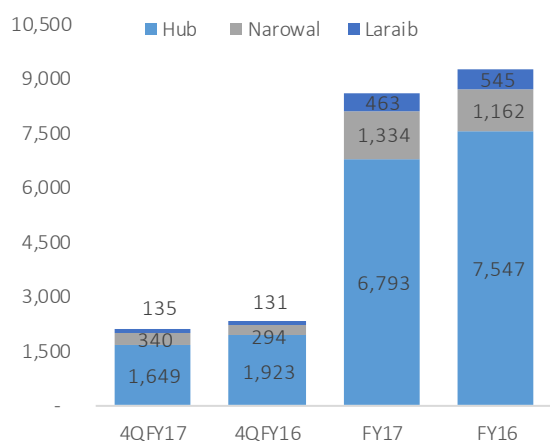
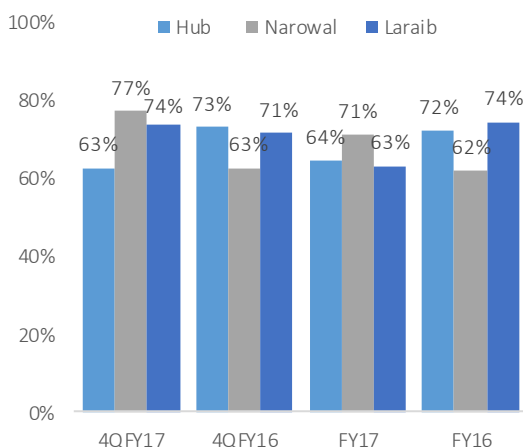


Exhibit: Load Factor - Plant-wise (%)



Lower debt financing for equity stake in CPHGCL to pull earnings up

HUB Power Holding Limited requires financing for its 46% equity stake in 1,320MW coal fired project; CPHGCL. Recall, HPHL project cost was revised down to USD 2bn (prev. US 2.5bn), where USD 500mn now accounts for equity portion. Post financial close, both HUBC and CPIH will allocate 1.5% equity portion each to the Govt. of Baluchistan, while bearing all costs to the bottom-line. Therefore, we incorporate 46% (previously: 47.5%) equity injection by HPHL which translates to about USD 238mn/PKR 21bn. As per management guidance this is to be financed c.80% by debt and remaining through internal cashflows. This is further illustrated in FY17 financials, wherein HUBC has entered into PKR 21bn loan for financing of associated undertakings (CPHGC, TEL and SECMC). Although this may strain dividend payout (~80% FY18-20F) in the medium-term, lower finance cost and upward timeline revision in cashflows from CPHGCL (COD: Aug'19) will likely dilute the impact in the long run.

TEL & SECMC projects on track

Project timelines of HUBC's other associated undertakings are on track. Thar Energy Limited (60% owned Associate) is expected to achieve commercial operations tentatively by Dec'20. Implementation Agreement has been initiated while Water-use-Agreement is underway. To recall, FFC entered TEL as 30% equity strategic partner in 3QFY17. As per management guidance, SECMC project (8% equity ownership) is 8% ahead of schedule with production commencement expected by Jun'19.

Culmination of major maintenance at Narowal on track; accounts demerged

Narowal underwent major overhaul of 8 out of 11 engines in FY17 in addition to major steam turbine overhaul. Remaining 3 engines are expected to undergo maintenance in FY18. Narowal successfully demerged its accounts in FY17, where profits from discontinued operations came in at PKR 1.34bn (EPS: PKR 1.16), down 45%YoY. All assets and liabilities of Narowal have been transferred to NEL.

Risks of PKR fluctuation to dollar hedged loans overblown- Increased WC financing may sting

Fears of earnings volatility on foreign currency loans of associated undertakings seem overblown in our view. Based on US\$2bn project financing for CPHGC, 75% debt portion translates to US\$1.5bn. With no major cashflow impact given the nature of US\$ denominated loans (pass through item), and expected curtailment of dividend to finance equity stake, we deem fears of earnings attrition as unwarranted. That said, increased reliance on working capital (ST borrowings up +50%YoY) may keep finance cost elevated in the medium-term.

Recommendation

We have revised upward our earnings estimates for HUBC on lower finance cost assumption, as reliance on debt financing for 46% equity stake in CPHGCL contracts to c.85%. While this may dampen dividend payout in the medium-term, we anticipate early COD of associated undertakings may dilute impact in the long run. We maintain our **"BUY"** call on the company as we rollover our TP to Jun-18. Our new target price of PKR 136.6/share (down by 2% from previous PKR 137/share), offers +27% upside from its last closing. The company is currently trading at a FY18/19F P/E of 10.0x/9.4x and offers a healthy dividend yield of 7.4%.

Source: Company Financials, IGI Research

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Time Horizon: Jun – 2018

Valuation Methodology: The analyst(s) has used following valuation methodology to arrive at the target price of the said security (ies):

DDM (Dividend Discount Model)

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IGI Finex Securities Limited

Research Analyst(s)

Research Identity Number: BRP009

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Contact Details

Research Team

Saad Khan	Head of Research	Tel: (+92-21) 111-234-234 Ext: 810	saad.khan@igi.com.pk
Abdullah Farhan	Senior Analyst	Tel: (+92-21) 111-234-234 Ext: 912	abdullah.farhan@igi.com.pk
Syed Daniyal Adil	Research Analyst	Tel: (+92-21) 111-234-234 Ext: 973	daniyal.adil@igi.com.pk
Suleman Ashraf	Research Analyst	Tel: (+92-21) 111-234-234 Ext: 957	suleman.ashraf@igi.com.pk
Muhammad Saad	Research Analyst	Tel: (+92-21) 111-234-234 Ext: 973	muhammad.saad@igi.com.pk
Tanweer Kabbeer	Research/Fund Select	Tel: (+92-21) 111-234-234 Ext: 966	tanweer.kabbeer@igi.com.pk
Umesh Solanki	Database Manager	Tel: (+92-21) 111-234-234 Ext: 974	umesh.solanki@igi.com.pk

Equity Sales

Faisal Jawed Khan	Head of Equities	Tel: (+92-21) 35301779	faisal.jawed@igi.com.pk
Zaeem Haider Khan	Regional Head (North)	Tel: (+92-42) 35777863-70	zaeem.haider@igi.com.pk
Muhammad Naveed	Regional Manager (Islamabad & Upper North)	Tel: (+92-51) 2604861-62	muhammad.naveed@igi.com.pk
Ejaz Rana	Regional Manager (Faisalabad)	Tel: (+92-41) 2540843-45	ejaz.rana@igi.com.pk
Asif Saleem	Branch Manager (RY Khan)	Tel: (+92-68) 5871652-56	asif.saleem@igi.com.pk
Mehtab Ali	Branch Manager (Multan)	Tel: (+92-61) 4512003	mehtab.ali@igi.com.pk
Zeeshan Kayani	Branch Manager (Abbottabad)	Tel: (+92-992) 408243-44	zeeshan.kayani@igi.com.pk
Ihsan Mohammad	Branch Manager (Peshawar)	Tel: (92-91) 5253035	ihsan.mohammad@igi.com.pk

IGI Finex Securities Limited

Trading Rights Entitlement Certificate (TREC) Holder of
Pakistan Stock Exchange Limited |
Corporate member of Pakistan Mercantile Exchange Limited

Head Office

Suite No 701-713, 7th Floor, The Forum, G-20,
Khayaban-e-Jami Block-09, Clifton, Karachi-75600
UAN: (+92-21) 111-444-001 | (+92-21) 111-234-234
Fax: (+92-21) 35309169, 35301780

Website: www.igisecurities.com.pk

Stock Exchange Office

Room # 719, 7th Floor, PSX Building, Stock Exchange Road, Karachi.
Tel: (+92-21) 32429613-4, 32462651-2, Fax: (+92-21) 32429607

Lahore Office

5-F.C.C. Ground Floor, Syed Maratib Ali Road,
Gulberg II, Lahore
Tel: (+92-42) 35777863-70, 35876075-76
Fax: (+92-42) 35763542

Faisalabad Office

Room #: 515-516, 5th Floor, State Life
Building, 2- Liaqat Road, Faisalabad
Tel: (+92-41) 2540843-45
Fax: (+92-41) 2540815

Multan Office

Mezzanine Floor, Abdali Tower,
Abdali Road, Multan
Tel: (92-992) 408243 - 44

Peshawar Office

2nd Floor, The Mall Tower,
35 The Mall Peshawar Cantt.
Tel: (92-91) 5253035, 5278448

Islamabad Office

Mezzanine Floor, Office 5, 6 & 7, Kashmir Plaza,
Block- B, Jinnah Avenue, Blue Area, Islamabad
Tel: (+92-51) 2604861-2, 2604864, 2273439
Fax: (+92-51) 2273861

Rahim Yar Khan Office

Plot # 12, Basement of Khalid Market,
Model Town, Town Hall Road, Rahim Yar Khan
Tel: (+92-68) 5871653-6, 5871652
Fax: (+92-68) 5871651

Abbottabad Office

Ground Floor, Al Fatah Shopping Center, Opp. Rad
Station, Mansehra Road, Abbottabad
Tel: (+92-99) 2408243 - 44

Sialkot Office

Suite No. 10 & 11, 1st Floor, Soni Square,
Mubarak Pura, Sialkot.
Tel: (+92-52) 3258437, 3258762