PTC INDIA FINANCIAL SERVICES LTD (PFS) IPO note –"SUBSCRIBE" 16th Mar, 2011

Issue at a Glance

Issue Summary	
Total Issue of Shares (Cr)	15.67
Fresh Issue (Cr)	12.75
Equity Shares offer for sale (Cr)	2.92
QIB Investors (Cr)	7.83
Non -Institutional Investors (Cr)	2.35
Retail Investors (Cr)	5.49
Issue opens on	16th Mar,2011
Issue closes on	18th Mar,2011
Price Band (Rs.)	26 - 28
Lot size (No. of shares) and multiple	250
Face Value (Rs)	10.00
Issue Size (Rs in Cr.)	407.42 – 438.76
Equity Shares outstanding prior to the Issue (Cr)	43.45
Equity Shares outstanding after the Issue (Cr)	56.20

*** (The retail bidders - will be entitled to a discount of Rs 1 /- on cut-off price - on allotment)*

Shareholding Pattern

	Pre-Issue (%)	Post- Issue (%)
PTC India Ltd	77.60	60.00
GS Strategic Investments Ltd	11.20	8.66
Macquarie India Holdings Limited	11.20	3.46
Public	-	27.88
Total Share Capital	100	100

CARE & ICRA GRADING 4/5 indicating "Above Average Fundamentals"
CRISIL GRADING 3/5 indicating "Average Fundamentals"

Issue Objectives

PFS is coming out with an IPO of 15.67 Cr Equity Shares. This is an offer for sale of 2.92 Cr equity shares by Macquarie India Holdings Limited as a part of the decision to divest part of its shareholding in PFS. Thus PFS will not receive any IPO proceeds from the same to the extent ~ Rs 81 Cr. The total shareholding of Promoters will reduce from 100% to 72.12% post issue.

PFS intends to utilize the proceeds from the fresh issue to augment its capital base to meet the future capital requirements arising out of growth in its business

Company Background

PFS is an Indian non-banking financial institution and subsidiary of (PTC) India Limited Incorporated in 2006. PFS is one of the few Indian financial institutions that are engaged in both equity and debt financing including short-term and long-term debt as well as structured debt financing.

They also provide fee based syndication and advisory services as well as carbon credit financing against certified emissions reduction (CER) exclusively to the power sector. The company offers an integrated suite of services including provision financing to, and make investments in, private sector Indian companies in the power sector, including for power generation, equipment supply and fuel source projects. PFS company is currently focusing on power generation projects in India

PFS is regulated by Reserve Bank of India and enjoys the dual status of NBFC (Non banking finance company) as well as IFC (Infrastructure Finance Company) in Aug 2010. The IFC status enhances PFC's ability to raise funds on a cost-competitive basis and enables them to assume higher debt exposure in infrastructure projects.

Overview of Indian Power Industry

India has continuously experienced shortages in energy and peak power requirements. The total energy deficit and peak power deficit during April 2010 to October 2010 was ~ 9.2% and 10.1%, respectively. The total installed power generation capacity in India was 167278.36 MW as of August 31, 2010.

Source: Monthly Review of the Power Section (published by the CEA in October 2010

Power Consumption

The total energy consumption in India is estimated to grow from 566 Mtoe in 2006 to 1280 Mtoe in 2030. This implies growth at a CAGR of 3.5% CAGR in India's energy requirement over the next 25-30 years and hence, there is a huge potential for investments in the energy sector in India. The GoI has set a goal of 1,000 kWh per capita by fiscal 2012 in its mission of “Power for All by 2012” under the National Electricity Policy.

Source: World Economic Outlook 2008, IEA

Power Demand-Supply Overview

The Indian power sector has historically been beset by energy shortages which have been rising over the years. In fiscal 2010, peak energy deficit was 12.7% and total energy deficit was 10.1%. The deficits in electric energy and peak power requirements vary across different regions in India. The peak deficit was 17.2% in the Western Region, followed by 18.5% in the North Eastern Region in the period from April to October 2010.

Source: Monthly Review of the Power Section ("Monthly Review") published by the CEA in October 2010

Power Generation

According to the White Paper on Strategy for XI Plan, the total capacity addition during the past 25 years between the 6th and the 10th Five-Year Plans was ~91,000 MW. A total capacity addition of 78,700 MW is planned for the XIth Five-Year Plan which should result in significant investments in the power generation sector. The installed generation capacity and the proposed capacity addition during the XIth Five- Year Plan is 167,278.36 MW and 78,700.4

Source: Monthly Review of the Power Section published by the CEA in October 2010

Planned Expansion

The aim for the 11th Plan i.e. by 2012 is a capacity addition of 15,000 MW from renewable energy. The total fund requirement for generation projects, during the XIIth Plan period is estimated at ~ Rs 4951 Bn with ~ Rs 1,266 Bn being required for the hydro sector, ~ Rs 3306 Bn being required for the thermal sector and ~ Rs 377 Bn being required for the nuclear sector.

(*Source: International Conclave on Key Inputs for Accelerated Development of Indian Power Sector for Twelfth Plan and Beyond, 18-19 August 2009, MoP and CEA*)

Investments in generation, transmission and distribution

The total fund requirement for transmission system development and related schemes during the XIIth Plan period is estimated at ~ Rs 2400Bn, with ~ Rs 1400Bn being required for the central sector and ~ Rs1,000Bn being required for the state sector.

The total fund requirement for the distribution sector, during the XIIth Plan period is estimated at ~ Rs 3,710Bn.

(*Source: International Conclave on Key Inputs for Accelerated Development of Indian Power Sector for Twelfth Plan and Beyond, 18-19 August 2009, MoP and CEA*)

Principal Investments

PFS has made strategic equity investments in companies in the energy value chain in India, including in Greenfield and Brownfield projects.

As of December 31, 2010, PFS Board has approved equity commitments for ten companies for an aggregate amount of Rs 5,641.66 million, with projects aggregating 3,221.45 MW of power generation capacity.

The company has entered into definitive agreements for investments in eight companies for an aggregate amount of Rs 4,827.67 million, with projects aggregating 2,621.45 MW of power generation capacity. All of its principal investments have been in private unlisted companies.

As of December 31, 2010, its principal investments aggregated Rs 4,186.23 million in eight companies including in Indian Energy Exchange Limited ("IEX"), India's first nationwide, automated and online electricity trading platform.

PFS current portfolio comprises of principal investments are mostly Greenfield projects, which typically involve between two and five years of development activity prior to commencement of commercial operations.

Three of its principal investment projects, with an aggregate power generation capacity of 175.60 MW, have commenced commercial operation.

In September 2010, it liquidated a portion of our investment in IEX for a gain.

PFS has approved debt commitments aggregating Rs 22,567.30 million to 31 companies, with projects aggregating 8,982.20 MW of power generation capacity.

PFS has entered into definitive agreements for financing arrangements for an aggregate amount of Rs 11,198.72 million to 17 companies, with power projects aggregating 8,283 MW of power generation capacity.

As of December 31, 2010, it had outstanding loan financing of Rs 5,951.15 million to 13 companies with projects representing 6,794 MW of aggregate power generation capacity.

PFS has **outstanding principal investments** in eight companies aggregating Rs 4186.23 million as of December 31, 2010.

As of December 31, 2010 PFS did not have any non-performing assets in its loan portfolio.

PFS's Competitive Strengths

1) **Composite financial services platform focused on all areas of the energy value chain:** PFS is a one stop solution provider offering a comprehensive range of financial products and services that add value throughout the life cycle of projects across all areas of the energy value chain. This has enabled them to establish as a preferred financing provider for power projects

2) **Strong Parentage & Brand:** PFS is a subsidiary as well as promoted by PTC, which is the market leader for power trading solutions in India and provides comprehensive solutions for the power sector. PTC together with its affiliates provides comprehensive solutions in the energy value chain including services such as power trading, co-development, fuel-intermediation, consulting and is in the process of setting up an energy equity fund. The synergies among the group entities provide them with early access to potential business opportunities and is also benefitted from the associated goodwill of PTC

3) **Flexibility in operations due to NBFC & IFC status:** PFS enjoys dual status of both NBFC and IFC (Infrastructure Finance Company) which provide them with greater flexibility than some of its competitors, particularly banks, and enable them to quickly and efficiently capitalize upon financing opportunities that arise. While banks are subject to more stringent regulation in India and may provide only certain forms of debt financing and equity financing subject to certain specified limits, however as an NBFC it is able to provide a wider range of debt financing, including structured products, as well as equity financing that is subject to fewer restrictions. **The IFC status enhances PFC's ability to raise funds on a cost-competitive basis and enables them to assume higher debt exposure in infrastructure projects**

4) **Demonstration of Strong Growth & Robust Balance Sheet:** PFS business has grown rapidly in recent years, providing them with a robust balance sheet that has laid Strong foundation for PFS's future growth. PFS within a relatively short period of time has seen its portfolio grown significantly as on December 31, 2010, it had outstanding loan financing of Rs 5,951.15 million to 13 companies with projects representing 6,794 MW of aggregate power generation capacity. **As of December 31, 2010 PFS did not have any non-performing assets in its outstanding loan portfolio. The capital to risk-weighted asset ratio as of December 31, 2010 was 60.57% and its return on average total assets for FY 2010 was 3.20%.**

PFS's Business Strategy

1. **Comprehensive structured financing solutions to private power project developers:** PFS continue to focus on the power sector and offer comprehensive, structured financing solutions that address the financing requirements of private power project developers in India. It intends to grow its principal investment and debt financing businesses, as well as expand its fee based and other services, to ensure effective sourcing and cross sell of its financing products and services.

2. **Consolidate its position as a preferred financing solutions provider**: PFS seeks to leverage its strong industry experience, relationships and the goodwill from its association with PTC which in turn will consolidate their position as a preferred financing solutions provider for smaller and medium sized power generation, equipment supply and fuel source projects

3. **Expansion of fee-based services and CER financing:** PFS intend to increase their focus on its current fee-based services that include primarily debt facility agent and security agent services as well as various advisory services such as techno-commercial appraisal services. PFS has commenced financing against carbon credits and believes that this segment will continue to grow. It plans to develop specific expertise in this segment to effectively capitalize on the growing carbon market and develop capabilities to offer carbon credit advisory services going forward

4. **Access to Lower Cost of Funds:** PFS continues to evaluate various funding opportunities to lower its cost of funds, including through the issuance of infrastructure bonds. Further IFC (International Finance Corporation) status enables PFS to avail ECBs (external commercial borrowing) up to 50% of its owned Funds without prior RBI approval. It has entered into a letter agreement with IFC (International Finance Corporation) for a proposed loan of US$ 50mn (Rs 2240.5 mn) to support and expand their lending program to renewable energy projects.

5. **Developing strategic partnerships with international financial institutions:** PFS continues to focus on strategic partnerships via options such as joint ventures/private equity funds. It entered into strategic partnerships with Macquarie Bank Limited and Vitol SA for carbon credit financing business & intends to enter into similar strategic partnerships from time to time to provide various financial services in specific areas of India's power sector

6. **Focus on renewable energy and other emerging segments of the power sector:** PFS has had approved aggregate equity commitment of Rs 822.11 million for four companies and aggregate debt commitment of Rs 3273.30 million for 12 companies in the renewable energy sector. It continues to evaluate strategic initiatives focused on the renewable energy value chain. It has also entered into an ECB agreement with DEG (Deutsche Investitions) for an aggregate amount of US$ 26.00 million (Rs 1165.06 million) for on-lending to renewable energy projects.

Risks & Concerns

1) **PFS is significantly dependent on PTC its Promoter for the growth of its business.**

2) **PFS is affected by the volatility in interest rates which could have an adverse affect on its lending and treasury operations and could cause its net interest income to decline and adversely affect its return on assets and profitability. In fiscal 2010 and in the nine months ended December 31, 2010, interest income represented 51.44% and 70.19%, respectively, total income in such periods.**

3) **PFS has made principal investments which may not perform and it may not be able to control the non-performance of such companies.**

4) **Energy projects, particularly power generation projects, carry certain risks that, to the extent they materialize, could adversely affect its business, financial condition, results of operations.**

5) **PFS may avail foreign currency borrowings in the future, which will expose them to fluctuations in currency exchange rates, which could adversely affect its business, financial condition and results of operations.**

6) **PFS debt finance business is concentrated on a few borrowers in the power sector and if any of the loans to these borrowers become non-performing, the quality of its loan portfolio may be adversely affected. The total documented, unfunded outstanding loan sanctions are Rs 5,247.57 million, and company's ten largest debt commitments approved represent 54.70% of its total debt commitments**

7) **PFS has made and expect to make principal investments in few companies engaged in a few energy projects and write-offs or write-downs or losses in any of these investments could adversely affect its results of operations and financial condition. Moreover, because its principal investments as of December 31, 2010 were in only eight companies in India, losses in any one of these investments could significantly adversely impact its financial condition and results of operations**

8) **The failure on the part of the seller to deliver CERs to PFS under the agreement entered with them would lead to a default by PFS under the agreement entered by them with third parties for onward sale of such CERs.**

Financials

Consolidated Summary Statement of P & L

(Rs in Mn except EPS)

Particulars	9MDec 31, 2010	Mar 31, 2010	Mar 31, 2009
Total Operating Income	822.91	534.72	115.98
Total Operating Expenditure	342.01	167.43	28.96
Operating Profit	**480.90**	**367.29**	**87.02**
Depreciation	40.51	0.47	0.24
Other Income	2.53	0.18	0.02
PBT	**442.92**	**367**	**86.80**
Tax	130.74	112.48	1.50
Adjusted Profit	**312.18**	**254.52**	**85.30**
Exceptional Items	-	-	-
Net Profit	**312.18**	**254.52**	**85.30**
Basic EPS (Rs)	**0.72**	**0.59**	**0.20**
Diluted EPS (Rs)	**0.70**	**0.59**	**0.20**

Consolidated Summary Statement of Balance Sheet

(Rs in Mn)

Particulars	Dec 31, 2010	Mar 31, 2010	Mar 31, 2009
LIABILITIES			
Share Capital **(A)**	4,345.83	4,345.83	4,345.83
Employee Stock Options Outstanding **(B)**	4.28	12.40	1.00
Reserves and Surplus **(C)**	2,313.32	2,001.14	1,746.62
Less : Miscellaneous Exp **(D)**	18.69	-	-
Net worth E(A+B+C-D)	**6,644.74**	**6,359.37**	**6,093.45**
Loan Funds Secured**(F)**	4,773.69	3,108.01	200
Deferred Tax Liability (Net) **(G)**	71.84	43.75	-
Total H(E+F+G)	**11,490.27**	**9,511.13**	**6,293.45**
ASSETS			
Gross Block	**352.31**	**350.48**	**0.92**
Less: Depreciation	41.29	0.78	0.32
Net Block (I)	**311.02**	**349.70**	**0.60**
Capital Work in Progress **(J)**	**0.08**	**0.96**	**-**
Investments **(K)**	**4,405.41**	**4,067.04**	**2,000.12**
Loan Financing **(L)**	**5,951.15**	**2,662.01**	**200**
Net Current Assets **(M)**	822.61	2,431.42	4,089.11
Deferred Tax Liability (Net) **(N)**	-	-	3.62
Total O (I+J+K+L+M+N)	**11,490.27**	**9,511.13**	**6,293.45**

Financial performance snapshot

		FY09	FY10	H1FY11
Total income	Rs mn	116.0	534.9	536.1
Net profit	Rs mn	85.3	254.5	255.1
Adjusted EPS	Rs	0.35	0.59	0.59
Adjusted equity shares	Mn	434.6	434.6	434.6
Net worth	Rs mn	6,093	6,359	6,608
Book value	Rs	14.02	14.63	15.21
RoE	%	2.4	4.1	3.9
RoA	%	2.3	3.2	2.4
CRAR	%	275.4	88.3	60.9
Yield	%	17.7	19.0	16.9
Cost of funds	%	11.9	10.6	10.7
Spread	%	5.8	8.4	6.2
Net interest margin	%	17.2	11.9	8.4

Note: PFS has NIL NPAs as of date

Source: DRHP

Valuation & Outlook

PFS's P/B ratio is currently at 1.83x multiples on the higher band of IPO price &1.70 x on lower end of Ipo price. The Book value of PFS is Rs 15.29 as on 31st Dec, 2010.

Peer Group Comparison

There are no direct comparable peers in India.

Key ratio comparison amongst power-focused NBFCs

	PFS		PFC		REC	
	FY09	FY10	FY09	FY10	FY09	FY10
Yield on loan (%)	17.71	19.02	10.92	10.75	10.45	11.03
Cost of borrowings (%)	11.86	10.6	8.70	8.14	7.32	7.76
Spread (%)	5.85	8.42	2.22	2.61	3.13	3.27
NIM (%)	17.2	11.94	3.84	4.00	3.96	4.32

Source: Companies

PFS has undertaken high yield short term financing which has enabled it to maintain better NIM (net interest margin) as compared to its peers, even though it has higher cost of borrowings

Investment Rationale

- **PFS derives immense strength from its parent company PTC a leading power trading company in India. The company has a sound financial management track record with absolutely nil NPA as on 31st Dec, 2010. . PFS is one of the few Indian financial institutions that are engaged in both equity and debt financing including short-term and long-term debt as well as structured debt financing.**

- **Further company has core competency in appraising power sector projects**

- **The company has tie up for long term funding for financing of long gestation power projects along with comfortable capital adequacy ratio of 60.9% and has diverse resources of institutional funding**

- **NBFC & IFC status to benefit PFS since it enables to evaluate various funding opportunities to lower its cost of funds, including through the issuance of infrastructure bonds**

We recommend the Investors to "Subscribe" to the issue. Listing gains may not materialize therefore investors with long term horizon can invest in the stock.

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