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PAKISTAN
POWER

REP-019
MARKET
VISTA

HUBC: An exciting story; twists and turns ahead

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BUY

TARGET PRICE (PkR)	SHARE PRICE (PkR)
168.0	81.07
UPSIDE/DOWNSIDE	**DIV. YIELD**
107.1	9.2%

- **We revisit our investment case on Hub Power Company Ltd post release of detailed financial accounts. The company posted 46/20% YoY/QoQ higher NPAT of PkR8.4bn (EPS: PkR6.28) in 1QFY21. More importantly, HUBC also announced first interim cash dividend of PkR4.0/sh, after a dry spell since 8 consecutive quarters.**
- **Analyzing details of debt repayments (particularly for equity investments), we flag a prominent FY23 peak burdening cash flows and shaping payouts to trend in a "U-shape" going forward. Aware of the same, management may remain conservative in the near term to avoid any unsustainable bump in payout policy. Based on lower of the two, FCFE/sh and ROEs of existing power projects, we forecast DPS of PkR7.0/10.0 per share in FY21/22F (dividends from CPHGC, a determining factor).**
- **We also tweak our earnings estimates for HUBC, as we incorporate (i) HUBC's 38.3% stake in ThalNova Power Project (financial close achieved in Sep'20; expected CoD: Jun'22), (ii) 6 months' delay in CoD of 60% owned Thar Energy Ltd (TEL), and (iii) 25% tax rate on income from 2015 power policy projects.**
- **Management is also considering multiple plans for utilization of hitherto closed Base plant, where any cash injection after signature of agreements with GoP (Feb'20) should make room for CAPEX. Our revised TP of PkR168/sh implies an upside of 107% at last close—Buy.**

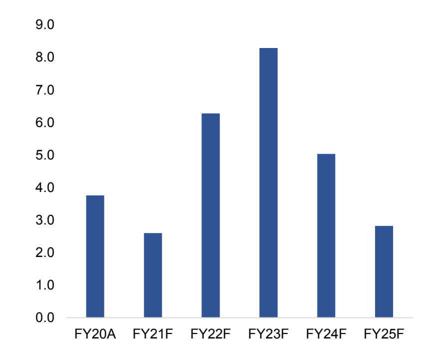
HUBC: Key metrics

(PkRmn)	FY19	FY20	FY21F	FY22F	FY23F
EPS (PkR)	9.37	19.31	19.85	23.72	31.07
EPS Growth	-2.0%	106.1%	2.8%	19.5%	31.0%
DPS (PkR)	-	-	7.00	10.00	12.00
Dividend yield	0.0%	0.0%	9.2%	12.3%	14.8%
PER(x)	8.9	4.2	4.1	3.4	2.6
BVS (PkR)	44.3	64.7	80.0	95.3	117.8
P/BVS(x)	1.8	1.3	1.0	0.9	0.7
ROE	20.8%	32.3%	25.9%	26.2%	28.6%
ROA	5.3%	10.4%	9.1%	11.6%	15.2%

Source: PSX & AKD Research

Payouts to remain conservative in medium term: We revisit our investment case on Hub Power Company Ltd post release of detailed financial accounts. The company posted 46/20% YoY/QoQ higher NPAT of PkR8.4bn (EPS: PkR6.28) in 1QFY21. More importantly, HUBC also announced first interim cash dividend of PkR4.0/sh, after a dry spell since 8 consecutive quarters. This came as a surprise to the market, especially since HUBC raised debt through issuance of PkR6bn of Sukuk on 20th Oct'20. Additionally, payment of PkR9.4bn received as part of the Energy Sukuk II in Jun'20 constituted majorly of energy payments, which were likely passed on to PSO. While the management remains ambiguous with regards to HUBC's payout policy going forward, we highlight that debt repayments and interest cost taken in lieu of equity investment in CPEC projects are yet to peak out, suggesting a U-shaped payout structure. On the flipside, the management may remain conservative in near term to avoid any bump in payout policy. Based on lower of the two, FCFE/sh and ROEs of existing power projects, we forecast DPS of PkR7.0/10.0 per share in FY21/22F. The commencement of all projects in FY23F should likely result in improved payout ratio from then onwards.

Debt repayments yet to peak out



Source: PSX & AKD Research

ThalNova adds PkR10/sh to our valuation: We also tweak our earnings estimates for HUBC, as we incorporate (i) HUBC's 38.3% stake in ThalNova Power Project (expected CoD: Jun'22), (ii) 6 months' delay in CoD of 60% owned Thar Energy Ltd (TEL), and (iii) 25% tax rate on income from 2015 power policy projects. The 38.3% owned mine-mouth coal power project achieved financial close on 30th Sep'20, where we foresee the project contributing PkR1.28/sh (7% of FY20 EPS) to HUBC's bottomline post CoD. The ThalNova project adds PkR10/sh to our TP. The 1QFY21 consolidated result also included higher ETR of 10% vs. 1% in the same period last year, on the back of 25% WHT on income from CPHGC. While the management will likely contest higher WHT for 2015 plants, we have conservatively incorporated higher tax in our estimates for dividend income from its coal power projects. Meanwhile, we await for conversion of MoUs with GoP into final agreements before incorporating changes in PPAs for Narowal and Base plant. Our preliminary working suggests fixing RoE components at USD PKR exchange rate of 148/168 for Narowal/Base Plant to result in downward revision of our valuation by PkR10/sh (6.25% of TP – HUBC still a Buy).

One time receivable settlement to make room for CAPEX: In line with HUBC's long term strategy to become IPWP (independent power and water producer), the management is also considering 50MGD of new water desalination plant capacity, which would cost US$100mn, reportedly,

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with a construction period of two years. The project will likely be undertaken as a public private partnership, with FWO Enjazat as a foreign partner. Furthermore, the company is also considering to convert Base plant from Furnace oil to coal based power plant, where demand will be generated from KEL's decommissioning of its BPQS power plant (1,200MW), as per the management. Based on KEL's feasibility study on coal conversion, potential project cost comes at US$1.2bn (equity portion of ~PkR50bn). Any one-time cash flow settlement of outstanding capacity payments receivable (~PkR49bn) should create room for CAPEX of aforementioned proportion.

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- Relative Valuation (P/E, P/B, P/S etc.)
- Equity & Asset return based methodologies (EVA, Residual Income etc.)

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