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BFSI - NBFCs

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Sector Report | SECTOR REPORT | January 3, 2025 | NIFTY 50: 24,189

We initiate coverage on public sector power financiers with a positive view, and recommend BUY on PFC and REC. Our optimistic stance is underpinned by three factors. 1) With planned capex of over Rs33trn during FY23-32 in Generation, Transmission, and Distribution, including focus on renewables, power storage, and green hydrogen, the growth runway is long and visibility high. 2) Lessons learnt from the previous cycle (ie project gestation risk, PPA/FSA risks, and so on), a host of Central Government-driven reforms addressing the sustainability issue in the sector by attempting to resolve the burning issue of 'who pays the bill', continued benign competition from banks in the power space, and gradual diversification approach adopted by PFC/REC provide reasonable comfort around asset quality issues and, hence, added confidence around profitability. 3) Valuations, despite being higher (1YF Dec-25E P/BV of ~1.5x for REC, and 1.14x for standalone PFC) than the long-term median of 0.7x, remain palatable for the growth and profitability profile, along with near clean-up of past baggage. Against this backdrop, we initiate coverage with a BUY on both – PFC with Dec-25E TP of Rs600 (at standalone FY26E P/BV of 1.5x and 25% holdco discount on ~52.6% stake in REC), and REC with Dec-25E TP of Rs650 (implying 1.9x FY26E P/BV). The controlled upcycle in power capex and lending is here to stay, and both players provide the optimal path to ride it.

Planned capex in the Power ecosystem provides long-term growth visibility

The National Electricity Plan (NEP) envisages Rs33trn capex in the power sector ecosystem over FY23-32, as India continues to meet peak power demand of 458GW (~2x of current) by installing ~1,000GW capacity, consisting of over 500GW of renewable installed capacity. Capex would happen across the power sector ecosystem, including generation (conventional and renewables), and transmission and distribution—including power storage system—to support the ambitious renewable mix plans. Given their sectoral expertise and focus, along with regulatory advantage, PFC and REC are well placed to capture debt-funding opportunities.

Recent reforms, past learnings, conservative approach to growth provide comfort

PFC and REC have significantly benefited from the resolution of legacy NPAs, achieving multi-year lows in GNPA and NNPA ratios. During the current power upcycle, the acquisition of distressed power plants by larger players has facilitated stressed asset resolutions – a trend likely to continue. This recovery, combined with improving cash flows from thermal power plants, positions both lending companies for potential provision reversals, thus further enhancing profitability. Additionally, GoI's Revamped Distribution Sector Scheme (RDSS) aims to strengthen DISCOMs' financial health by modernizing infrastructure, targeting AT&C losses of 12-15%, and eliminating the ACS-ARR gap by FY25. Complementing this, the Late Payment Surcharge (LPS) Rules, 2022 address cash-flow challenges and ensure timely payments in the power sector. Since their implementation, legacy dues have decreased, from Rs1.39trn in Jun-22 to Rs246.8bn by Nov-24, with improved payment discipline and no defaults reported on installment payments. Given such structural tailwinds, PFC and REC are favorably positioned to capitalize on India's energy transition, thus offering compelling investment opportunities supported by enhanced profitability and reduced credit risk.

We initiate coverage with BUY on both, PFC and REC

Sustained double-digit loan growth, stable margins, and improving asset-quality support robust earnings visibility for companies in the sector. Despite offering consistent dividend payouts and maintaining strong return ratios, we believe sector players continue to trade at a discount to their book value. We project ~13%/~18% AUM CAGR for PFC/REC over FY24-27E, along with ~19%/~20% ROE during FY25-27E, respectively, driven by robust credit demand, write-backs, and net credit cost of -5bps to 5bps over FY25-27E.We initiate coverage on PFC and REC with BUY and Dec-25E TP of Rs600 and Rs650 (31% and 25% upside, respectively), valuing REC at FY26E P/BV of 1.9x, and PFC at FY26E standalone P/BV of 1.5x and 25% holdco discount on its REC stake.

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Rating, Target Price and Valuation

	Rating	CMP (Rs)	TP (Rs)	Upside (%)	Loan growth (%) FY25	Loan growth (%) FY26	RoA (%) FY25	RoA (%) FY26
Power Finance Corporation	BUY	459	600	31	14.0	13.5	3.1	3.0
REC Ltd	BUY	518	650	25	17.5	18.0	2.7	2.6

Source: Company, Emkay Research

Index:

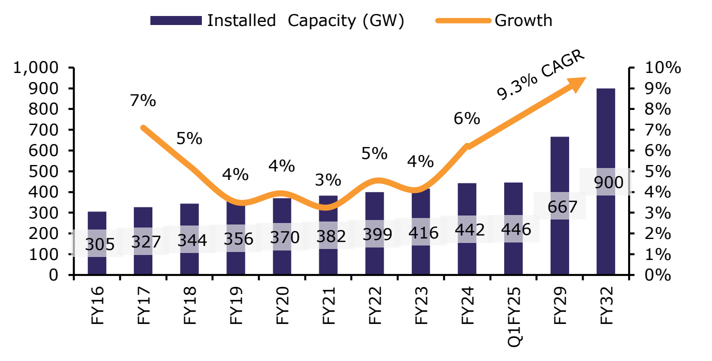
Investment thesis

We initiate coverage on PFC and REC with BUY and Dec-25E TP of Rs600 and Rs650 (~31 and 25% upside, respectively), implying FY26E P/BV of 1.9x for REC, and FY26E P/BV of 1.5x and 25% holdco discount on REC stake for PFC . Our positive stance on the stock is underpinned by three factors, which are: 1) a favorable capital expenditure cycle in power generation and distribution, which creates substantial lending opportunities for infrastructure financiers; 2) improving financial health and profitability of the power sector, supported by government reforms, enhanced cash flows for GENCOs (generation companies) and DISCOMs (distribution companies); and 3) stronger recoveries from stressed projects and improving asset quality, which reduce earnings volatility. Over the past decade, power financiers have successfully navigated significant challenges, including rising stress pool and elevated provisions, by adapting to regulatory and structural reforms. Key measures, such as tripartite agreements and penalties for delayed payments, have addressed legacy issues from the thermal cycle, including poor DISCOM health and PPA (power purchase agreement) unavailability, thereby substantially reducing credit risk. Looking ahead, power financiers are well-positioned to capitalize on macro tailwinds, including heightened power sector capex, government initiatives, and subsidies. Their growth prospects are further bolstered by diversifying loan portfolios, accelerating resolutions of stressed assets, and maintaining stable spreads, thus ensuring robust and sustainable performance. These factors collectively make both stocks an attractive investment opportunity.

Favorable capex cycle supporting growth

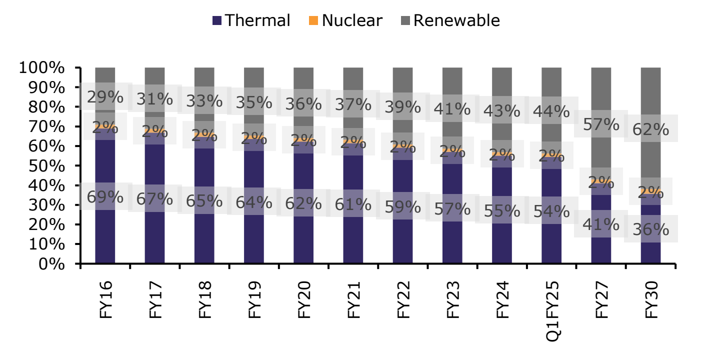
India's installed power capacity has grown, from 356GW in FY19 to 442GW in FY24, at CAGR of 4.4%, and is projected to clock 9.3% CAGR over FY24-32. Government target of 500GW renewable capacity by 2030, along with 50% share of non-fossil fuel-based capacity, necessitates an estimated Rs28.68trn in capex during FY24-32, predominantly funded by debt (75%). This translates into ~Rs21trn debt requirement, with ~Rs10trn needed over FY24-27E, thus presenting a substantial lending opportunity for power-focused financiers. Additionally, Rs4.76trn is projected for an enhanced transmission infrastructure over FY22-27, reflecting government commitment toward energy security, renewable integration, and sustainability, hence creating a robust growth avenue for infrastructure financing companies.

Exhibit 1: Installed capacity to double by FY32



Source: CEA, Emkay Research

Exhibit 2: Share of installed capacity in the RE segment to see higher growth



Source: NEP, Emkay Research

Exhibit 3: Capex in Generation

Capex plan for Generation (Rs bn)	2022-23	2023-24	2024-27	2027-32
Thermal	620	628	936.40	1,858.55
Nuclear	184	294	725	430.51
Renewables	1,419	1,778	7,392	13,848.63
BESS	-	-	566	2,926
Total Investment	**2,223**	**2,699**	**9,619**	**19,064**

Source: NEP, Emkay Research

Exhibit 4: Capex in Transmission expected at ~Rs4.8trn

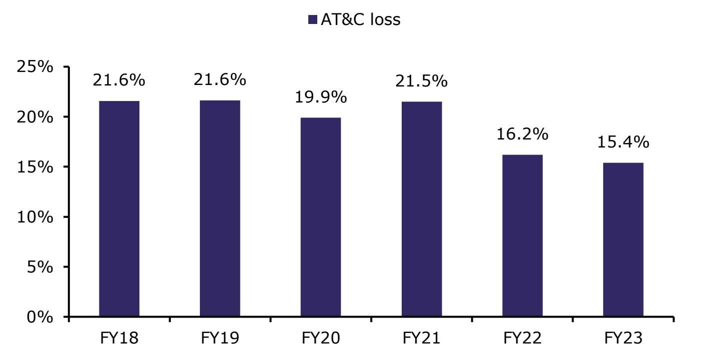
Transmission System (ckm) - Target	FY17	FY17-22	FY22	FY22-27	FY27
HVDC ± 320 kV/ 500 kV/800 kV Bipole	15,556	3,819	19,375	4,300	23,675
765 kV	31,240	19,783	51,023	35,005	86,028
400 kV	157,787	36,191	193,978	38,245	232,223
230/220 kV	163,268	29,072	192,340	46,027	238,367
Total	**367,851**	**88,865**	**456,716**	**123,577**	**580,293**

Source: NEP, Emkay Research

Government initiatives transforming the sector

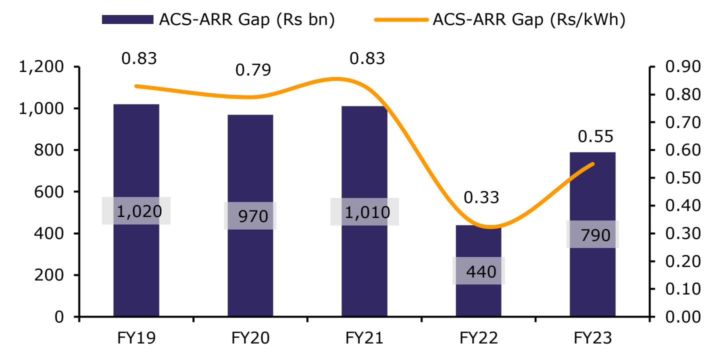
India's power financing sector has historically faced challenges due to distressed assets of private generators caused by project delays, untied capacity, and DISCOMs' financial struggles. Weak DISCOM finances, marked by high AT&C losses, tariff inadequacies, and delayed subsidy recoveries, have constrained power procurement and infrastructure investments, adversely impacting supply quality. However, reforms like the LPS (late payment surcharge) Scheme have improved GENCO cash-flows by enforcing payment schedules and surcharges, while government initiatives such as the Rs3.03-trillion Revamped Distribution Sector Scheme (RDSS) aim to modernize distribution infrastructure, targeting AT&C losses of 12-15% (15.4% in FY23) and a zero ACS-ARR gap by FY25 (0.55/kWh in FY23). Such measures strengthen the sector’s financial stability and cash flow of GENCOs and DISCOMs, thus improving the financial viability of the project and funding opportunities for power financiers.

Exhibit 5: AT&C losses have reduced; near the GoI target of 12-15%



Source: Power Distribution Utilities report, Emkay Research

Exhibit 6: The ACS-ARR gap has narrowed to Rs0.55/kwh

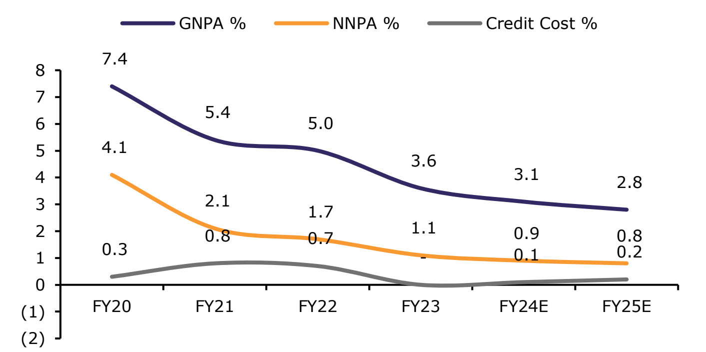


Source: Power Distribution Utilities report, Emkay Research

Stressed project resolution playing out

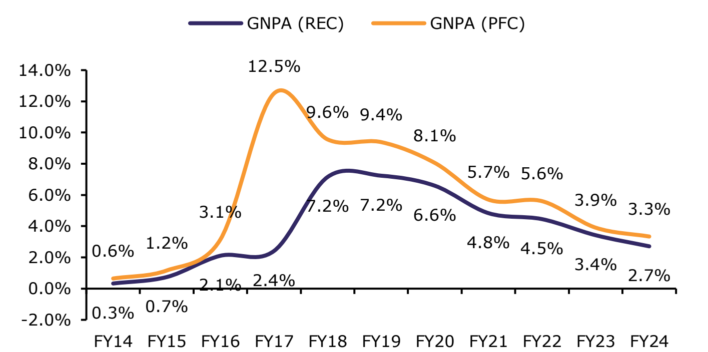
The Indian power sector—historically a significant source of non-performing assets (NPAs), particularly from privately-owned thermal power projects (TPPs)—has faced numerous challenges such as project delays, inadequate fuel supply agreements, land acquisition hurdles, permit issues, and absence of PPAs. Such issues led to substantial bad debts, severely impacting financial institutions. However, the sector has shown a marked recovery in stressed projects, driven by robust provisioning for bad loans, resolutions within and outside the NCLT framework, rising credit demand, and reduced slippages. Strategic acquisitions have gained momentum, with higher bids and lower haircuts reflecting in the improved asset valuations. Such developments have strengthened balance sheets and facilitated the effective resolution of stressed assets, making the sector more resilient and an attractive investment opportunity.

Exhibit 7: NPA trend of Infrastructure finance companies



Source: CARE rating, Emkay Research

Exhibit 8: Improving asset quality of REC and PFC



Source: Company, Emkay Research

Valuation argument

We initiate coverage on public sector power financiers with a positive outlook, assigning BUY to PFC and REC, supported by robust growth prospects and improving fundamentals. The planned capex for FY23–32 across generation, transmission, and distribution—including renewables, power storage, and green hydrogen—provides a long and visible growth runway. Central Government-led reforms aimed at addressing DISCOM sustainability, coupled with PFC and REC's prudent diversification strategies, provide a solid foundation for enhanced asset quality and profitability. While current valuations exceed long-term medians, the near-complete resolution of legacy issues and favorable sector dynamics make them compelling opportunities.

We assign Dec-25E target price of Rs600 for PFC, and of Rs650 for REC, which translates into FY26E P/BV of 1.5x and 25% holdco discount on REC stake for PFC and 1.9x for REC, thus positioning both companies as the prime beneficiaries of the ongoing power capex and lending cycle.

Exhibit 9: REC – Valuation matrix

REC	CMP/TP (Rs)	Upside	Mkt Cap (Rs bn)	P/BV (x)			P/E (x)			RoA			RoE			Book Value (Rs/sh)			Adj EPS (Rs)		
				FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E
At current market price	518	25.4%	1,365	1.7	1.5	1.3	8.6	7.6	6.7	2.7%	2.6%	2.5%	21.3%	20.8%	20.4%	303	351	405	60	68	77
At target price	650			2.1	1.9	1.6	10.8	9.6	8.4							303	351	405	60	68	77

Source: Company, Emkay Research

Exhibit 10: PFC – Valuation matrix

	CMP/TP (Rs)	Upside	Mkt Cap (Rs bn)	P/BV (x)			P/E (x)			RoA			RoE			Book Value (Rs/sh)			Adj EPS (Rs)		
				FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E
At current market price	459	30.6%	1,516	1.7	1.5	1.3	9.1	8.2	7.3	3.1%	3.0%	3.0%	19.5%	19.0%	18.6%	276	315	359	50	56	63
At target price	600			2.2	1.9	1.7	11.9	10.7	9.6							276	315	359	50	56	63

Source: Company, Emkay Research

Exhibit 11: PFC – SOTP-based value

(Rs)	Fair value	No of shares (mn)	Market cap (Rs bn)	PFC's stake	PFC's stake value (Rs bn)	Holdco discount	Value (Rs bn)
PFC - Standalone	400.0	3,300	1,320,040	100%	1,320,040	0%	1,320,040
REC	650.0	2,633	1,711,450	52.63%	900,736	25%	675,552
PFC - Total							1,995,592
PFC - Fair value per share	**600**						
Standalone FY26 P/BV	**FY25E**	**FY26E**	**FY27E**				
Adjusted BV	232	271	315				
Standalone Dec-25E TP	400	400	400				
P/BV (x)	1.7	1.5	1.3				
Standalone P/BV (x) at CMP	1.3	1.1	0.9				

Source: Company, Emkay Research

Key risks

Key risks to our investment thesis include i) slower-than-expected growth, which could be driven by company-specific factors such as increased competition from banks or broader macroeconomic challenges like asset quality deterioration; ii) a decline in asset quality, resulting from macroeconomic pressures or company-specific issues, thus posing significant risk, and potentially leading to rising NPAs, higher provisioning, and increased credit costs; iii) diversification into non-power infrastructure projects, which lack revenue lock-ins or government backing; this could elevate credit risks, especially given the limited expertise in managing private sector exposure; iv) the RBI's proposed stricter provisioning norms if implemented, for project financing, which would increase provisioning requirement to ~5.0% from ~0.4%, thus presenting additional risk; this is subject to gradual reduction.

Exhibit 12: NBFCs – Valuation comparison

Ticker	Rating	CMP (Rs)	TP (Rs)	Upside	Mkt cap (Rs)	P/BV (x)			P/E (x)			ROA (%)			ROE (%)		
						FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E
CIFC	ADD	1,272	1,450	14.0%	1,069	4.5	3.7	2.9	24.8	19.7	15.8	2.4	2.5	2.6	19.9	20.6	20.7
MMFS	BUY	276	360	30.6%	341	1.7	1.5	1.3	15.4	10.9	8.6	1.8	2.1	2.3	11.7	14.9	16.8
SHFL	ADD	3,060	3,500	14.4%	1,151	2.1	1.8	1.6	13.3	11.0	9.2	3.4	3.5	3.6	16.8	17.8	18.5
LTF	REDUCE	143	150	5.0%	356	1.4	1.3	1.2	13.4	10.7	8.5	2.4	2.6	2.8	10.8	12.5	14.3
PIEL	ADD	1,125	1,150	2.2%	254	1.0	0.9	0.9	57.7	18.4	10.5	0.5	1.4	2.4	5.3	7.6	11.1
ABCAP	BUY	184	270	46.8%	479	1.6	1.4	1.2	14.3	10.9	8.9	1.41	1.47	1.54	11.7	13.4	14.4
POONAWAL	REDUCE	321	240	-25.3%	250	3.0	2.7	2.4	81.7	22.1	17.8	1.10	3.10	2.89	3.7	12.7	14.0
UGRO	BUY	231	360	55.9%	21	1.3	1.0	0.9	14.0	10.3	8.0	2.2	3.0	3.7	8.6	11.0	12.2
BAF	BUY	7,389	8,400	13.7%	4,574	4.9	4.1	3.4	28.2	21.8	18.4	3.9	4.1	3.9	19.2	20.7	20.6
PFC	BUY	459	600	30.6%	1,516	1.7	1.5	1.3	9.1	8.2	7.3	3.1	3.0	3.0	19.5	19.0	18.6
REC	BUY	518	650	25.4%	1,365	1.7	1.5	1.3	8.6	7.6	6.7	2.7	2.6	2.5	21.3	20.8	20.4

Source: Company, Emkay Research

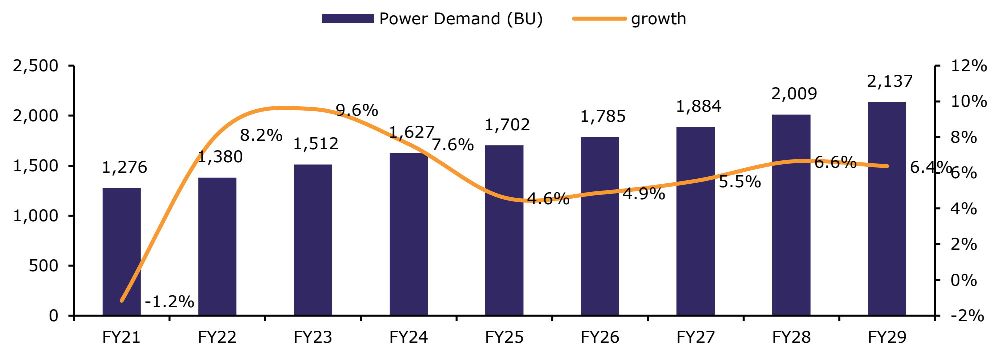
Demand driving capex

Surge in power demand

India ranks the world's third-largest energy producer and the second-largest energy consumer. The country's power generation sector is among the most diverse globally. India's energy production encompasses a wide range of sources, from traditional ones like coal, lignite, natural gas, oil, and nuclear power, to renewable sources like wind, solar, hydro, and energy derived from agricultural and household waste.

According to the 20th Electric Power Survey of India, nationwide peak electricity demand is projected to reach 277GW by FY27, with an energy requirement of ~1.9TU. Power demand is closely linked to the growth of the nation. India has been one of the world's fastest-growing economies over the past decade, and is experiencing rising power demand led by government infrastructure spending, and the commercial and industrial, and residential sectors, with new demand coming from the rising trends of electrification, upticks in data center capacities, rising EV (electric vehicle) adoption, and green hydrogen.

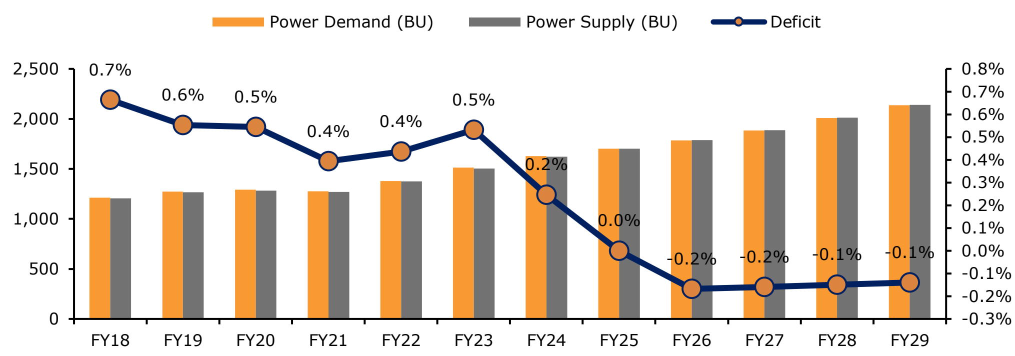
Exhibit 13: Growing power demand



Source: CEA, Emkay Research

Peak electricity demand in India has grown, from 184GW in FY20 to 243GW in FY24, clocking average growth rate of 7.3% in the past five years, and is expected to see CAGR of 5-6% over FY24-29, reaching nearly 315GW, with expected persistently high temperatures, rising urbanization, economic growth, and infrastructure push leading to higher power consumption. This calls for more energy production and capacity addition across the conventional and non-conventional (RE) segment.

Exhibit 14: Power demand and supply trends



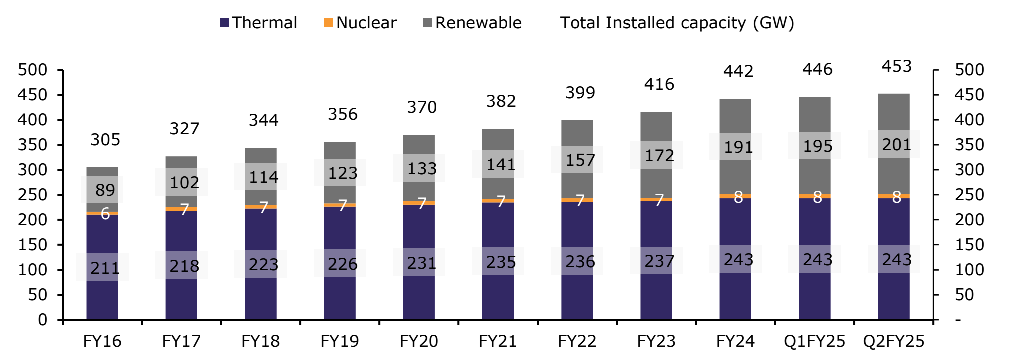
Source: CEA, Emkay Research

The gap between rising demand and limited capacity creates a valuable opportunity for PFC and REC, to fund new power generation projects, especially in renewables, thus supporting steady and profitable loan growth.

Capacity expansion – Renewables remain the focus area

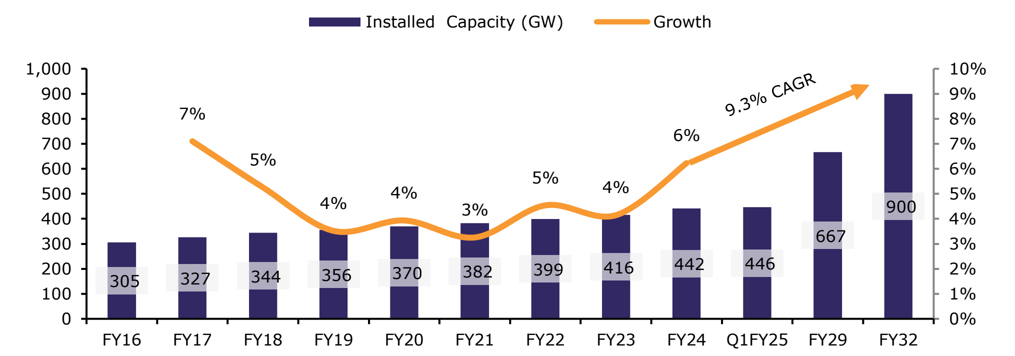
India's installed power capacity grew to 442GW in FY24 from 356GW in FY19, marking a five-year CAGR of 4.4%. Over FY24-32, India's installed power capacity CAGR is likely to be 9.3%. To ensure universal access to reliable and sufficient electricity, investments are being made to expand installed capacity and facilitate the transition to clean energy. The government aims to achieve 500GW of renewable capacity by 2030, and increase the share of non-fossil fuel-based installed capacity to around 50%.

Exhibit 15: RE source of power is expected to see robust growth and capacity expansion



Source: CEA, Emkay Research

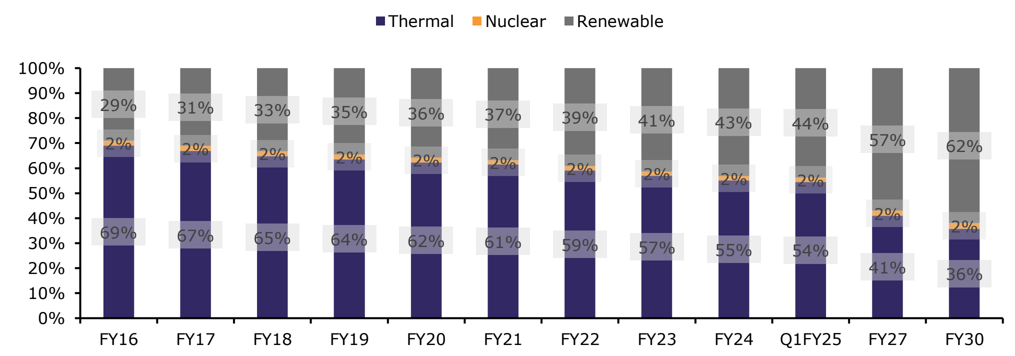
Exhibit 16: Installed capacity addition to reach 667GW by FY29 (9.3% CAGR over FY24-32)



Source: CEA, Emkay Research

The Ministry of New and Renewable Energy (MNRE) has outlined its 'Vision 2047' based on GoI focus on energy independence, security, sustainability, and de-carbonization. A target has been set based on this vision, for an 80% green grid by 2040, 90% green grid by 2047, and a transition to net-zero by 2070. RE (including hydro) capacity is expected to clock 14% CAGR till CY30 to ~500GW, thereby comprising 62% of the total generation capacity vs 45% now.

Exhibit 17: Increasing share of RE generation



Source: CEA, MNRE, Emkay Research

Required capex/funding opportunity in power generation

The increase in capacity addition will necessitate substantial capital expenditure. According to NEP 2022-23, total capital required for expenditure during 2024-23 is estimated at ~Rs28.68trn. Typically, funding is sourced from 25% equity and 75% debt, with the debt component primarily provided through loans from scheduled commercial banks or power-focused infrastructure finance companies (IFCs). Consequently, debt requirement for generation projects is expected to be ~Rs21trn between FY24 and FY32, with approximately Rs10trn needed over FY24-27. This creates a significant opportunity for lending in this sector.

Exhibit 18: Large funding opportunity for all power financiers

Capex plan (Rs bn)	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29	2029-30	2030-31	2031-32
Fund requirement										
Thermal	620	628	294	243	399	560	481	421	264	133
Nuclear	184	294	280	190	255	224	126	57	23	-
Renewables	-	-	-	-	-					
Hydro	147	167	149	103	96	299	333	316	240	109
PSP	34	25	47	154	282	297	251	154	50	-
Wind	259	415	548	556	531	613	744	742	838	371
Offshore Wind	-	-	-	-	-	-	-	45	137	92
SHP	4	4	4	4	4	4	4	4	3	1
Biomass	41	49	51	52	54	55	57	59	42	18
Solar	934	1,118	1,467	1,571	1,720	1,821	1,863	1,915	1,972	397
BESS	-	-	-	-	566	1,450	840	225	82	329
Total Capex	**2,223**	**2,699**	**2,840**	**2,873**	**3,906**	**5,324**	**4,700**	**3,938**	**3,651**	**1,451**

Source: National Electricity Plan, Emkay Research

Exhibit 19: PFC and REC hold considerable share in the overall credit to the power sector

O/s credit to power sector (Rs bn)	Mar-23	Mar-24	Sep-24
Bank	6,202.3	6,440.4	6,416.1
NBFC	9,404.1	11,257.3	11,897.8
Total O/s	**15,606.4**	**17,697.7**	**18,313.9**
PFC – credit to power sector	**4,168.3**	**4,622.8**	**4,722.2**
PFC share in power financing	26.7%	26.1%	25.8%
REC– credit to power sector	**3,937.5**	**4,469.6**	**4,673.4**
REC share in power financing	25.2%	25.3%	25.5%

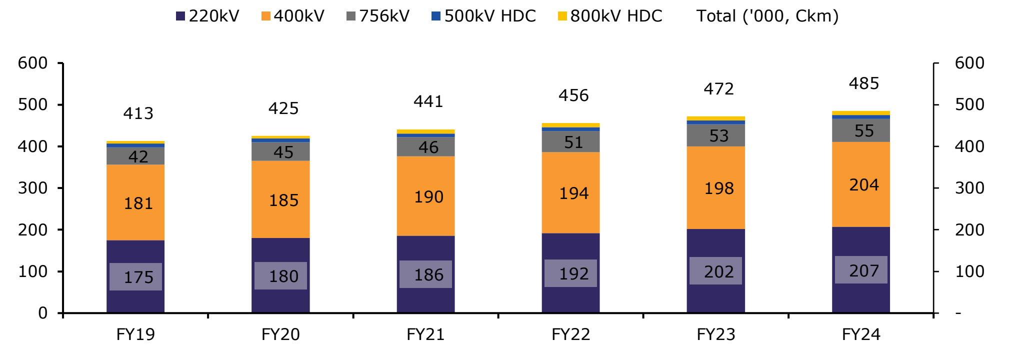
Source: Company, RBI, Emkay Research

Required capex/funding opportunity in Transmission and Distribution

India's energy transition and advancements in power technology systems have witnessed remarkable growth in recent years. This rapid expansion is primarily driven by a combination of factors, including increasing energy demand, government initiatives aimed at electrifying rural areas, and the urgent need to establish robust connectivity between power generation stations. A key aspect of this transition is the integration of renewable energy sources, particularly from resource-rich states that have significant solar and wind energy potential, into the national grid.

To support this ambitious energy transformation, the NEP outlines comprehensive measures for developing an extensive transmission infrastructure. This plan emphasizes the need for expanding transmission systems at the 220kV and above levels, encompassing a wide range of components such as transmission lines, substations, and reactive compensation mechanisms. These systems play a critical role in ensuring the stability, reliability, and efficiency of power distribution across the country.

Exhibit 20: Transmission line network (220kV & above)



Source: CEA, Emkay Research

Exhibit 21: Transmission line network CAGR stands at ~4.4% over FY17-22; expected at ~5% over FY22-27E

Transmission System Type / Voltage Class (ckm)	FY17	Addition during FY17-22	FY22	Addition during FY22-27	FY27
HVDC±320kV/500kV/800kV Bipole	15,556	3,819	19,375	4,300	23,675
765kV	31,240	19,783	51,023	35,005	86,028
400kV	157,787	36,191	193,978	38,245	232,223
230/220kV	163,268	29,072	192,340	46,027	238,367
Total	**367,851**	**88,865**	**456,716**	**123,577**	**580,293**

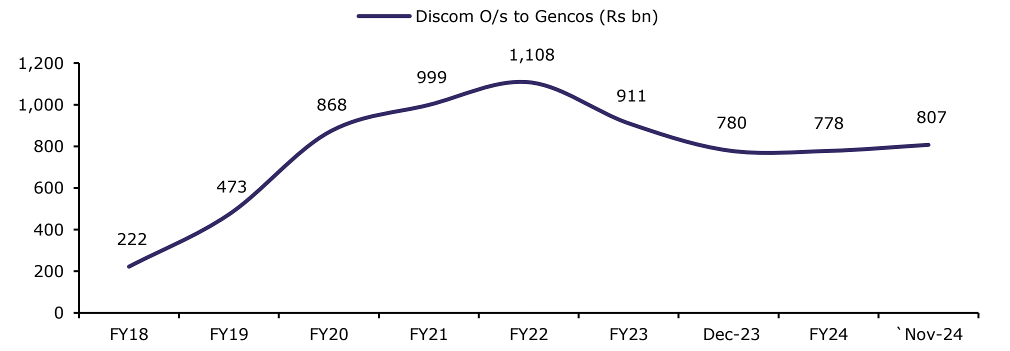
Source: National Electricity Plan, Emkay Research

The NEP projects that implementing this enhanced transmission network will require a substantial investment of Rs4.76trn during CY22-27. This investment underscores GoI commitment to strengthening the power sector for meeting the growing energy needs of the nation, while facilitating the seamless integration of renewable energy sources into the grid. Focus on such infrastructure development not only aligns with India's renewable energy goals but also addresses the long-term requirements for energy security and sustainability.

Strengthening the value chain

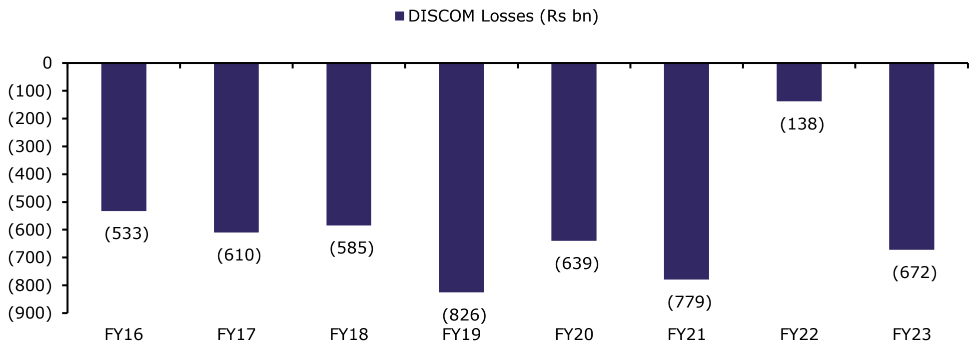
Distribution is the crucial final link in the power sector value chain, yet its financial health has significantly deteriorated over the past decade. This decline is driven by irregular tariff increases, high aggregate technical & commercial (AT&C) losses, and delayed subsidy payments from state governments, which have strained DISCOMs' ability to purchase power and delayed payments to generation companies. Historically, the Indian power financing sector has faced challenges with distressed assets, particularly from private generators, due to delays in project execution, untied capacity, and significant receivables issues caused by DISCOMs' poor financial condition and inadequate fuel supply. Consequently, many banks in India have become reluctant to finance power projects.

Exhibit 22: Outstanding payments by DISCOMs to conventional generation companies



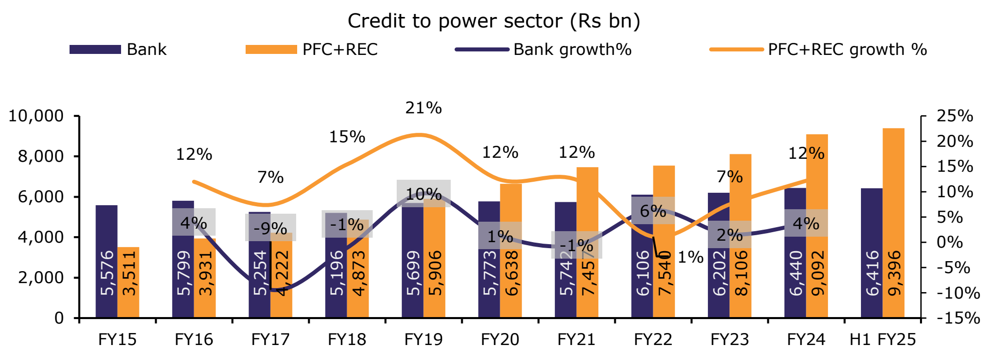
Source: PRAAPTI, Emkay Research

Exhibit 23: DISCOMs continue to see losses despite multiple GoI schemes



Source: Report on Performance of Power Utilities, Emkay Research

Exhibit 24: Stress in the power sector keeps banks at bay

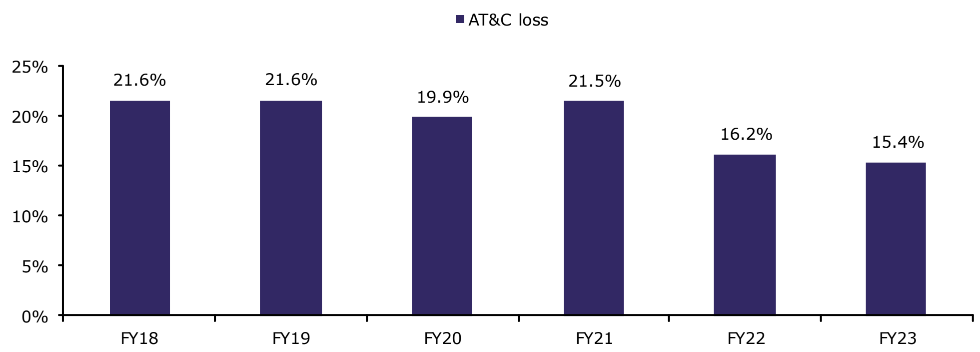


Source: Report on Performance of Power Utilities, Emkay Research

Improving financial stability, supported by the GoI

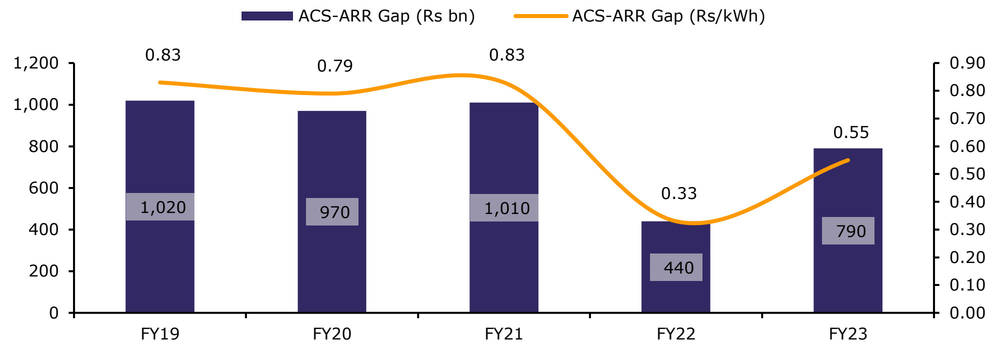
Despite various efforts, reliable 24x7 supply of electricity remains unavailable in many areas, along with high AT&C losses and a persistent ACS-ARR gap. Such issues are due to structural, management, and infrastructure weaknesses in the distribution sector. To meet consumer service standards, DISCOMs need to improve operational efficiency, financial sustainability, and consumer services. The government has implemented large-scale reforms and policies to address such challenges and enhance the entire value chain.

Exhibit 25: AT&C Loss trajectory – Close to it target of <15%



Source: PFC's report on performance of state power utilities, Emkay Research

Exhibit 26: Narrowing ACS-ARR gap



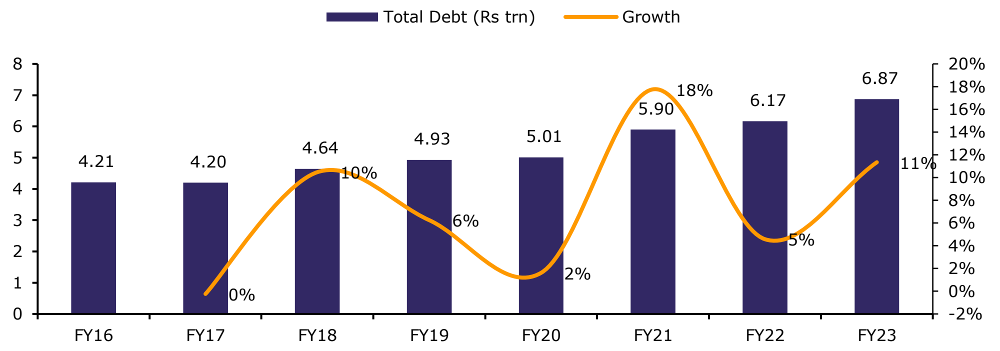
Source: Annual Integrated Rating and Ranking of Power Distribution Utilities, Emkay Research

Historically, DISCOMs have been the weakest link in the power value chain, with poor financial health limiting their ability to purchase power or to invest in distribution infrastructure, thereby affecting the quality of electricity delivered to consumers. Long-standing challenges include high AT&C losses, inadequate tariffs, and delayed subsidy recoveries from state governments. Efforts to reduce AT&C losses and the ACS-ARR gap have shown progress, with the government targeting pan-India AT&C losses of 12-15% and a zero ACS-ARR gap by 2024-25. As of FY23, AT&C losses have decreased to 15.4%, and the ACS-ARR gap has narrowed to Rs 0.55/kWh.

Moderating debt and outstanding dues

The total borrowings of DISCOMs increased to Rs6.87trn in FY23 (5-year CAGR of 8.2%) which we believe is in line with growth of the loan books of power-focused IFCs. Overall, DISCOMs' health is gradually improving, with GoI support through the RDSS scheme, which encourages sustainable practices over freebies or regulatory assets. Additionally, the GoI launched a liquidity relief scheme in 2019, initially allocating Rs900bn and which was later increased to Rs1.25trn; the scheme provides loans against receivables from PFC and REC for state DISCOMs. To qualify, DISCOMs had to meet certain criteria like timely submission of audited accounts, prompt tariff filings, clearing pending subsidies and bills, reducing the ACS-ARR gap and AT&C losses, and ensuring nil defaults.

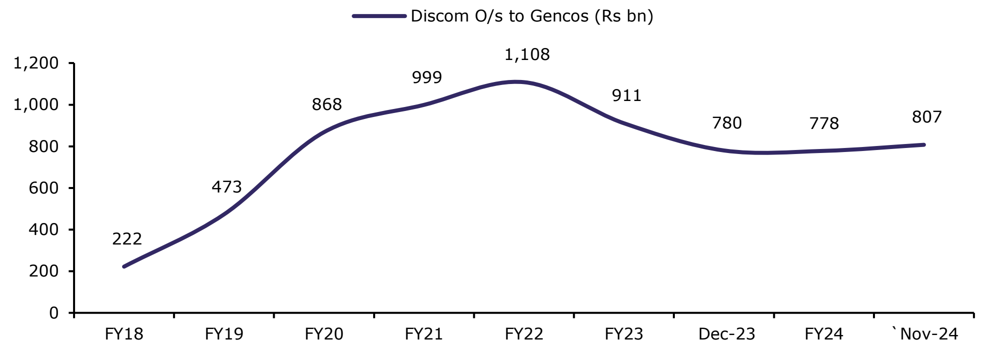
Exhibit 27: Borrowing trend of DISCOMs



Source: PFC's report on performance of state power utilities, Emkay Research

Reducing overdue payments from DISCOMs to GENCOs is vital for financial stability in India's power sector, as such dues limit GENCOs' cash-flow and capacity for expansion. As of Nov-24, DISCOMs' total outstanding dues stand at Rs807.3bn, a 27% reduction from that in Mar-22 due to the Electricity (Late Payment Surcharge and Related Matters) Rules, 2022. The introduction of this rule has strengthened regulatory mechanisms for recovering dues from DISCOMs by enforcing late payment surcharges, payment schedules, and payment adjustments, thus improving the cash-flow of GENCOs.

Exhibit 28: Outstanding payments by DISCOMs to conventional generation companies



Source: PRAAPTI, Emkay Research

Various schemes launched by the GoI to support the power T&D segment

- Deen Dayal Upadhyaya Gram Jyoti Yojana (DDUGJY)-2014: The objective of this scheme is electrification of all un-electrified villages.
- Pradhan Mantri Sahaj Bijli Har Ghar Yojana (SAUBHAGYA)-2017: targets electrification of poor rural and urban households in the country.
- Integrated Power Development Scheme (IPDS)-2014: has an outlay of Rs326.12bn, including budgetary support of Rs253.54bn from the GoI, for strengthening of sub-transmission and distribution networks in urban areas. Metering of distribution transformers/feeders/consumers in urban areas.
- 100% FDI through automatic route for power generation projects (renewable energy sector).
- The Revamped Distribution Sector Scheme (RDSS) was launched in 2021 to enhance financial sustainability and improve operational efficiency in the distribution sector.
- Independent Transmission Projects (ITPs): aim to develop transmission capacities in India and bring in potential investors after developing such projects to the stage of preliminary survey work, identification of route, preparation of survey report, initiation of process of land acquisition, initiation of process of seeking forest clearance if required, and conduct the bidding process.
- Late Payments Surcharge (LPS) Scheme (2022): provides a mechanism for settlement of outstanding dues of generating companies, Inter-State Transmission Licensees and Electricity Trading Licensees.

Revamped Distribution Sector Scheme (RDSS)

The GoI introduced the RDSS with a budget of Rs3.03trn, including support from the central government at an estimated Rs976.31bn over five years (FY21-22 to FY25-26). The scheme provides financial aid to DISCOMs for modernizing and strengthening distribution infrastructure toward improving supply reliability and quality for consumers. It targets reducing Aggregate Technical & Commercial (AT&C) losses to 12-15% nationwide, and narrowing the Average Cost of Supply (ACS)-Average Revenue Realized (ARR) gap to zero by 2024-25.

The RDSS also includes a Smart Meter Program, divided into two parts. Part A focuses on distribution infrastructure upgrades and prepaid smart metering, while Part B covers training, capacity building, and additional support activities.

The GoI has identified nodal agencies (PFC and REC) for implementation of the scheme. REC has been allocated 19 states/UTs under the RDSS, covering 32 DISCOMs; while PFC has been allotted 17 states/UTs with a total of 24 DISCOMs. Till Dec-23, ~Rs1,217bn has been sanctioned for loss reduction works, and Rs1,304bn for smart metering works. As of Dec-23, PFC/REC have disbursed a cumulative Rs535.8bn/Rs588.6bn, respectively, to DISCOMs. The amount of grant received and administered to the eligible entities (net of lapses/surrendered by power utilities) during FY23-24 is Rs28.35bn. The funds are being released based on the progress of works post-tendering by Utilities, subject to meeting the pre-qualification criteria.

Progress so far (Jun-24)

Progress under RDSS shows significant movement. Almost 94% of the sanctioned projects for loss reduction have seen tenders issued, while about 74%, valued at around Rs450bn, have already been awarded. In the area of smart metering, of an estimated 88.7mn meters, roughly 50.8mn consumer and system smart meters have been awarded, with bids for approximately 17.4mn meters currently under review or evaluation.

Exhibit 29: Funds approved under the RDSS

Project (Rs mn)	Approved cost	GoI component (GBS*)	GoI grant disbursement
Metering	566,910	104,010	50
Loss reduction	611,370	378,760	44,300
Total	1,178,280	482,770	44,350

*Source: Company, Emkay Research; Note: * = Gross budgetary support*

Exhibit 30: Number of smart meters installed till Nov-24, under RDSS

	Target	Sanctioned	Installed
Smart Meters (mn)	250.0	197.9	7.3

Source: Company, Emkay Research

Late Payment Surcharge (LPS)

On 3-Jun-22, the Ministry of Power issued the 'The Electricity (Late Payment Surcharge and Related Matters) Rules, 2022' (LPS Rules), providing a framework for tackling cash-flow challenges faced mainly by generation as well as transmission companies, and for promoting timely payments across the power sector. The rules consolidate all dues, including principal and late fees, into an interest-free amount payable in 48 monthly instalments based on total dues. The rules also outline penalties and procedures for late payments. If DISCOMs delay current dues beyond one month past the due date, or two and a half months after receiving the bill, power supply may be restricted.

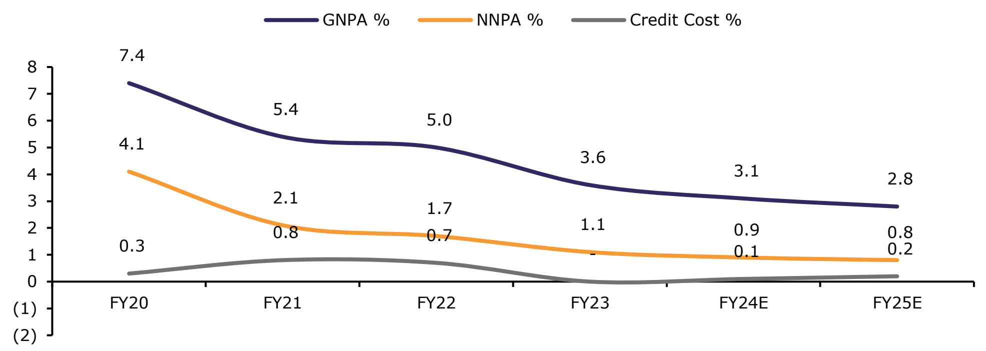
Since the Electricity (LPS and Related Matters) Rules, 2022 took effect, significant progress has been made in recovering dues from DISCOMs to suppliers, including GENCOs and transmission companies. Of the Rs1.39trn in legacy dues from Jun-22, 13 States/UTs have paid ~Rs1.15trn (82%) by Nov-24. As of now, legacy dues have dropped to Rs246.8bn, with no instalment defaults reported; consequently, the overall legacy dues have declined, from Rs1.40trn to Rs246.8.23bn. Additionally, 20 States/UTs reported no outstanding dues from Jun-22. Under the LPS rules, DISCOMs are also settling current dues promptly, with Rs8.47trn paid against a total of Rs9.21trn in bills as of May-24. The rules have effectively reduced payables and receivables timelines, with Days Payable down to 126 and Days Receivable to 119.

Asset quality stress easing

The Indian power sector has historically been a major contributor to the country's non-performing assets (NPA) problem, particularly through thermal power projects (TPPs), most of which are privately owned. These projects have faced several challenges, including delays in implementation, inadequate fuel supply agreements, land acquisition issues, permitting hurdles, the absence of power purchase agreements (PPA), and frequent cost overruns. Collectively, these factors have resulted in a buildup of bad debt within banks and financial institutions, severely impacting their overall performance.

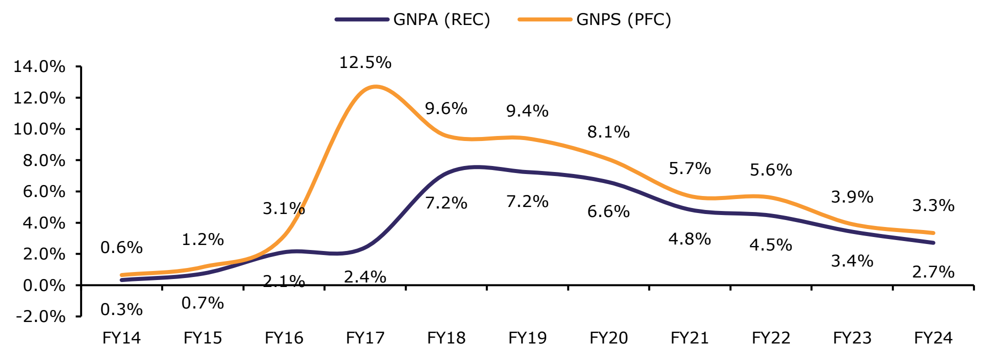
Today, the situation has markedly improved. Significant provisions for bad loans, strong credit demand, and fewer new slippages have led to a remarkable recovery in the lending sector. Strategic acquisitions have been more successful and have resulted in higher bids and lower haircuts for lenders, as strategic buyers assign greater value to underlying assets. This has contributed to more effective resolution of stressed assets and healthier balance sheets.

Exhibit 31: Asset quality trend of Power IFCs



Source: CARE Edge, Emkay Research

Exhibit 32: Substantial improvement in the overall asset quality of power financers



Source: Company, Emkay Research; Note: Spike in NPAs in 2017 was due to the implementation of restructuring norms by the RBI

Exhibit 33: PFC – Resolution of stressed projects under way, with many in the advanced stage

Stressed assets and resolution	FY22	FY23	FY24	Q2FY25	Current status
Under NCLT					
Number of projects	**14**	**13**	**13**	**12**	
Resolution amount (Rs bn)	**153.4**	**139.1**	**139.0**	**115.2**	
Project under liquidation (Rs bn) (7 projects)				26.1	
Project under resolution (Rs bn) (5 Projects)				89.0	
KSK Mahanadi				33.0	Evaluation of the bid is under way, and PFC expects a recovery of more than 100% (PCR of 55%)
Lanco Amarkantak				23.8	The asset has been resolved through NCLT; expect provision reversal of ~Rs. 2bn
Sinnar Power Transmission				30.0	PFC has invited bids and is expected to finalize the evaluation and submit it to the NCLT for approval (PCR of 80%)
Others				2.3	
PCR on these projects	**71%**	**77%**	**77%**	**78%**	
PCR on projects under liquidation				100%	
Outside NCLT					
Number of projects	**9**	**9**	**7**	**6**	
Resolution amount (Rs bn)	**55.78**	**25.9**	**21.74**	**18.2**	
TRN Energy				11.4	In the advanced stage of resolution; expect resolution in current FY (PCR of 50%)
Shiga Energy				5.2	In the advances stage of resolution; expect resolution in current FY (PCR of 50%)
Others				1.6	
PCR on these Projects	**62%**	**51%**	**55%**	**48%**	

Source: Company, NCLT, Emkay Research

Exhibit 34: REC – Resolution of stressed projects under way, with many in the advanced stage

Stressed Assets	FY22	FY23	FY24	Q2FY25	Current Status
Under NCLT					
No of projects	**13**	**12**	**12**	**13**	
Resolution amount (Rs bn)	**119.1**	**116.3**	**122.6**	**123.0**	
KSK Mahanadi				26.0	In the advanced stage of resolution; REC has recovered some amount and reversal in provision has been toward that
Sinnar Thermal				22.3	Expects recovery of ~55%, which is more than ECL on this project. PCR on this project is ~80%
Hiranmaye project				13.5	Expects recovery of >80%. PCR of ~50%
Lanco Amarkantak				22.1	The asset has been resolved through NCLT
Others				39.0	
PCR on these projects	**70**	**77%**	**71%**	**67%**	
Outside NCLT					
No of projects	**12**	**7**	**4**	**4**	
Resolution amount (Rs bn)	**52.54**	**32.65**	**15.48**	**15.28**	
PCR on these projects	**60**	**47%**	**49%**	**50%**	

Source: Company, NCLT, Emkay Research

Exhibit 35: Key GoI schemes and policies supporting the power sector

Timeline	Key Scheme/Policy	Objective
2001	Accelerated Power Development Programme (APDP)	Central Assistance for renovation of power plants Fund sub-transmission & distribution network
2002	Bailout Package	50% waiver of interest payable by state electricity boards to central PSUs
2003	Accelerated Power Development Programme (APDP)	Strengthening of sub transmission & distribution systems Reducing AT&C losses Increasing revenue collection and improved customer satisfaction
2003	Electricity Act	Unbundled SEBs Introduced power trading and Open Access Introduction of multi-year tariff
2005	Rajiv Gandhi Grameen Vidyutikaran Yojana (RGGVY)	Free electricity to rural and poor households Capital subsidy for rural distribution backbone
2006	National Tariff Policy	Power procurement through tariff-based bids Ensure electricity availability to consumers at competitive rates
2008	Restructured Accelerated Power Development and Reforms Programme (R-APDRP)	Aimed at reducing AT&C losses Enabling accurate baseline data IT enabled energy accounting
2012	Financial Restructuring Package (FRP)	States take over 50% of the outstanding short-term liabilities DISCOMs to issue bonds backed by State Government
2013	Model Electricity (Amendment) Bill	Financial restructuring to ensure adequate supply to consumers State Govt. to ensure sustainability of state-owned distribution licensees
2014	The Electricity (Amendment) Bill	Segregated retail supply from distribution Multiple supply licensees
2014	Integrated Power Development Scheme (IPDS)	Metering at multiple levels Strengthen sub-transmission networks
2015	Ujwal DISCOM Assurance Yojana (UDAY)	States to take over 75% DISCOM debt States push DISCOMs toward efficiency improvements.
2015	Deen Dayal Upadhyaya Gram Jyoti Yojana (DDUGJY)	Improving rural electricity access Feeder separation Metering in rural areas
2017	Pradhan Mantri Sahaj Bijli Har Ghar Yojana (Saubhagya)	Universal electricity access 24x7 power to rural and urban households
2018	Kisan Urja Suraksha evam Utthaan Mahabhiyan (KUSUM)	Target - 10GW of distributed grid connected solar Installation of 1.75mn solar pumps Solarization of grid connected pumps
2020	Liquidity Infusion Scheme	DISCOMs get loans worth Rs1.35trn from Power Finance Corporation and REC Limited, to settle outstanding dues of generators; state governments provide guarantee
2022	Revamped Distribution Sector Scheme	Central government to provide result-linked financial assistance for strengthening of supply infrastructure
2022	Late Payment Surcharge	Incentivize timely payments and ensure financial discipline within the power sector by penalizing delayed payments, thus improving liquidity and cash flow for power suppliers and distributors
2023	Electricity (Amendment) Rules	Regular tracking of subsidies disbursed by states to DISCOMs based on their billing records

Source: NITI Aayog, Emkay Research

BUY Power Finance Corporation

Consolidating power-sector capex opportunities

Emkay
Your success is our success

BFSI - NBFCs ▸ Initiating Coverage ▸ **January 3, 2025**

TARGET PRICE (Rs): 600

We initiate coverage on Power Finance Corporation (PFC) with BUY and SOTP-based TP of Rs600 (at standalone FY26E P/BV of 1.5x and 25% holdco discount on PFC's ~52.6% stake in REC). The macroeconomic tailwind, sizable power-sector capex, increased GoI thrust on power reforms, and strengthening balance sheet of power value-chain participants present a robust lending story. Planned power sector capex, coupled with heightened infrastructure spend, is expected to create a large financing opportunity of over Rs20bn by FY27E; this translates into ~13.2% annual growth for PFC over coming three years. Focus on RE and diversification in infra lending would put some pressure on the overall yield. But access to long-term funding at reasonable rates, backed by implicit government guarantees and expectation of the interest rate cycle peaking out, should keep margins broadly stable. We expect overall profitability to improve on the back of better recoveries from legacy assets and lower credit cost (as most loans are guaranteed by the government), with minimal slippages. Supported by these combined factors, we expect PFC AUM CAGR of ~13.2% over FY24-27E, at ~Rs699trn, and RoA and RoE to remain strong at ~3% and ~19%, respectively, over FY25-27E. We initiate coverage on PFC with BUY and Dec-25E TP of Rs600, which implies standalone FY26E P/BV of 1.5x

Power Finance Corporation: Financial Snapshot (Standalone)

Y/E Mar (Rs mn)	FY23	FY24	FY25E	FY26E	FY27E
Net profits	116,055	143,670	165,816	186,180	208,613
AUM growths (%)	13.2	14.0	13.2	13.2	13.3
NII growths (%)	2.4	8.8	16.8	15.4	14.9
NIMs (%)	3.4	3.5	3.5	3.5	3.5
PPOP growth (%)	2.8	10.0	18.5	14.4	14.9
Adj. EPS (Rs)	44.0	45.8	50.2	56.4	63.2
Adj. EPS growth (%)	15.8	4.2	9.7	12.3	12.0
Adj. BV (INR)	258.3	240.0	275.2	314.7	358.9
Adj. BVPS growth (%)	14.9	(7.1)	14.7	14.4	14.1
RoA (%)	2.8	3.0	3.1	3.0	3.0
RoE (%)	18.2	19.5	19.5	19.1	18.8
P/E (x)	10.4	10.0	9.1	8.1	7.3
P/ABV (x)	1.8	1.9	1.7	1.5	1.3

Source: Company, Emkay Research

Sustainable growth led by strong capex and diversification into newer segments

PFC has established itself as a pivotal player in power financing, leveraging its expertise to fund projects with strong returns. While its strategic bent toward renewable energy and infrastructure aligns with market trends, these segments generally offer lower yields than traditional thermal projects. However, PFC is positioned to achieve a robust ~13% AUM CAGR over FY24-27E, driven by opportunities across conventional power, renewables, and Infrastructure financing. Despite potential pressure on yields due to rising competition in non-power sectors, PFC's strong AAA credit rating and access to cost-effective long-term funding—backed by implicit government guarantees—are expected to help maintain stable NIMs of ~3.5%, ensuring steady growth and profitability.

Shedding of legacy NPAs and new GoI initiatives resulting in improved profitability

Power financing NBFCs have achieved notable improvement in asset quality over recent years, reflected in the sharp reduction in gross NPAs. This progress stems from measures such as restructuring stressed assets, writing-off non-performing loans, reducing slippages, higher provisioning levels, and increasing the proportion of state-guaranteed loans in their portfolio. PFC, in particular, has significantly reduced its stressed asset book by approximately 55% over five years, from Rs294.6bn in Sep-19 to Rs133.4bn by Sep-24, aided by successful resolutions through NCLT and other avenues. Further, schemes like RDSS and LPS have improved the overall cash flow of GENCOs and DISCOMs contributed toward system stability and hence reduced risk. We anticipate this positive momentum to continue, driven by strong power demand that ensures robust traction for these projects. Consequently, we expect write-backs to be recognized in the income statements, and credit cost over FY25-27E to remain low, between -5bps and 5bps for FY25-27E, resulting in healthy profitability.

We initiate coverage on PFC with BUY and TP of Rs600

Factoring in the macro tailwind, increased focus on renewable energy and expansion in the non-power segment would drive the overall growth for PFC; we expect AUM CAGR of ~13% over FY24-27E for the company. Further, the improving asset quality coupled with legacy resolution and provision write-backs is likely to result in improved profitability. We estimate credit cost to clock between -5bps and 5bps over FY25-27E and ROA/ROE to range at ~3%/19%, respectively. We initiate coverage on PFC with BUY and Dec-25E TP of Rs600, implying standalone FY26E P/BV of 1.5x and 25% holdco discount on its ~52.6% REC stake.

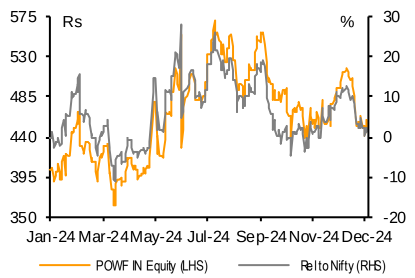
Target Price – 12M	Dec-25
Change in TP (%)	**NA**
Current Reco.	BUY
Previous Reco.	NR
Upside/(Downside) (%)	30.6
CMP (02-Jan-25) (Rs)	459.4

Stock Data	Ticker
52-week High (Rs)	580
52-week Low (Rs)	352
Shares outstanding (mn)	3,300.1
Market-cap (Rs bn)	1,516
Market-cap (USD mn)	17,677
Net-debt, FY25E (Rs mn)	35,290
ADTV-3M (mn shares)	10
ADTV-3M (Rs mn)	4,854.3
ADTV-3M (USD mn)	56.6
Free float (%)	-
Nifty-50	24,189
INR/USD	85.8
Shareholding, Sep-24	
Promoters (%)	56.0
FPIs/MFs (%)	17.7/17.5

Price Performance

(%)	1M	3M	12M
Absolute	(7.3)	(7.0)	17.9
Rel. to Nifty	(7.0)	(0.9)	5.6

1-Year share price trend (Rs)



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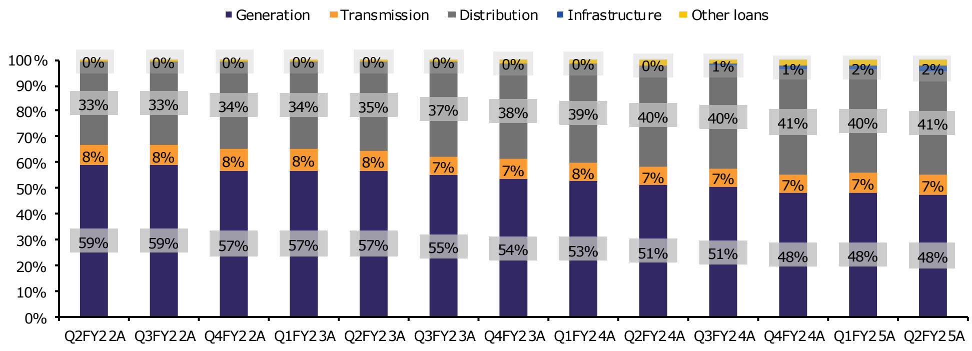
Investment thesis

- Capex cycle and diversification into new sectors to drive growth
- Resilient margins sustained by easing cost of funds
- Improving financial health of borrowers resulting in lower credit cost
- Strengthening asset quality supported by GoI schemes
- Enhanced profitability driven by stable margins and reduced credit costs

Capex cycle and diversification into new sectors to drive growth

Power Finance Corporation (PFC), India's leading financial institution focused on the power sector, has been instrumental in driving transformation since its establishment in 1986. As a Schedule-A Maharatna Central Public Sector Enterprise (CPSE), PFC has traditionally seen its loan growth driven by capital expenditure in the thermal segment. However, evolving industry dynamics have redirected its focus toward renewable energy, thus enhancing attention to transmission and distribution (T&D) infrastructure and supporting logistics and other infrastructure projects.

Exhibit 36: Share of Infrastructure and RE financing to increase, as PFC is intensifying focus in this segment



Source: Company, Emkay Research

Exhibit 37: Generation holds the major share in PFC's overall loan portfolio

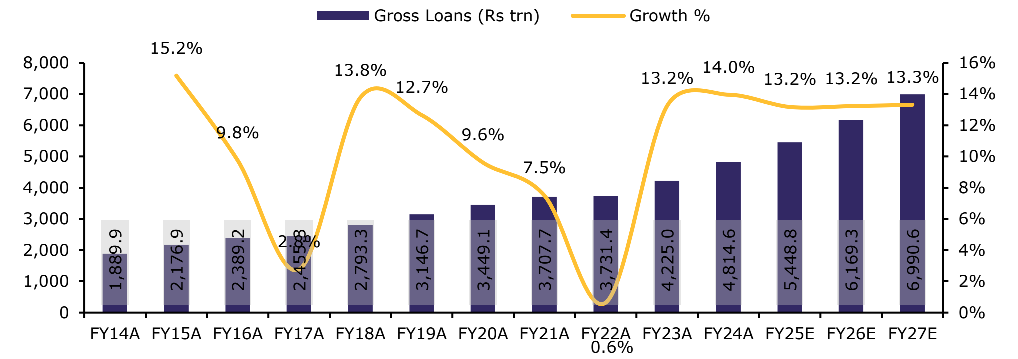
AUM (Rs bn)	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24	Q3FY24	Q4FY24	Q1FY25	Q2FY25
Generation	2,147.8	2,166.1	2,270.2	2,270.5	2,294.2	2,314.2	2,321.3	2,301.2	2,350.0
Conventional					*1,773.0*				*1,707.2*
RE					*521.3*				*642.8*
Transmission	286.7	287.7	311.2	326.3	324.0	327.9	351.4	352.1	369.0
Distribution	1,310.0	1,450.0	1,586.8	1,667.3	1,793.1	1,821.2	1,950.0	1,906.2	2,003.3
Infrastructure	-	-	-	-	-	27.3	70.1	74.2	94.3
Other loans	22.4	30.1	56.7	59.3	83.2	79.6	121.8	116.3	117.1
Total	3,767.0	3,933.9	4,225.0	4,323.4	4,494.6	4,570.3	4,814.6	4,750.0	4,933.6

Source: Company, Emkay Research

(PFC provides a variety of financial products tailored to the power sector, including rupee-term loans, short-term loans, equipment lease financing, and transitional financing for generation, transmission, and distribution projects. Expanding beyond power, PFC has diversified into Infrastructure and Logistics, supporting e-vehicle fleets, charging stations, roads, ports, metro rail, smart cities, and other major projects. Its clientele includes Central and State power utilities, power equipment manufacturers, government departments, and large-scale infrastructure developers.)

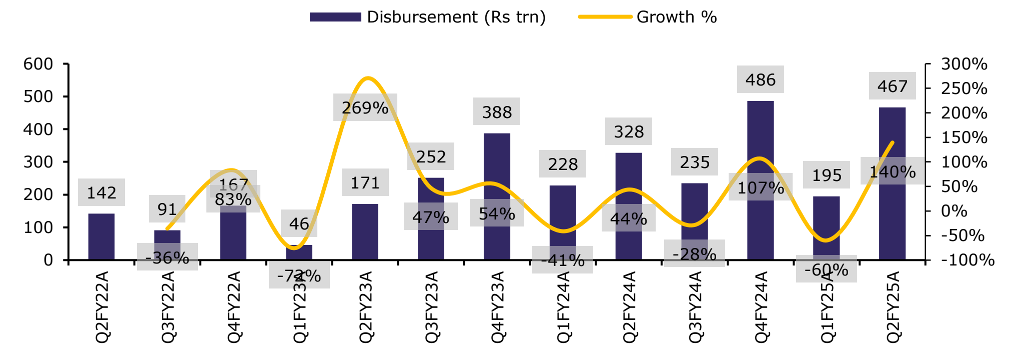
Over the next 5 years, investment of ~Rs25trn (~Rs19.3trn during FY22-27E) is expected in the power sector (generation + T&D) as India scales-up the infrastructure in generation, transmission and distribution. Investment will be dominated by generation capex as well as T&D capex, along with support from the new segment – Infrastructure lending. We estimate that over FY24-27, PFC would log loan CAGR of ~13.2%, led by strong disbursements in RE and Infrastructure financing.

Exhibit 38: AUM growth driven by strong capex and diversification into newer segments



Source: Company, Emkay Research

Exhibit 39: Robust disbursement on the back of a strong sanction pipeline



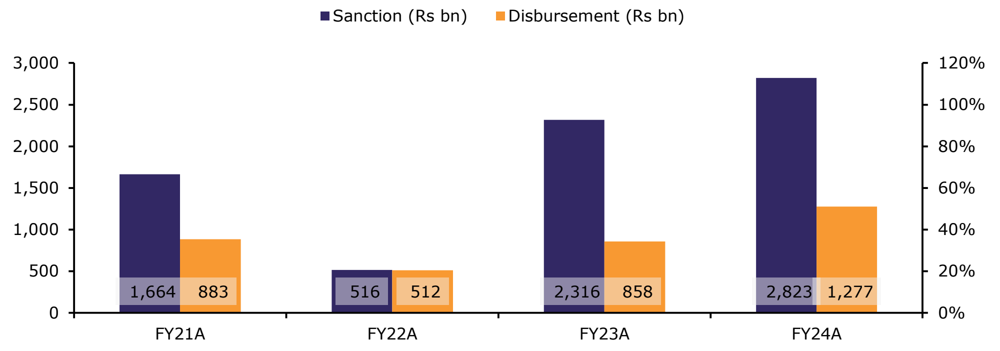
Source: Company, Emkay Research

Exhibit 40: Strong sanction pipeline supporting disbursement and growth

Sanction (Rs bn)	FY21A	FY22A	FY23A	FY24A
State sector	1,152	362	1,493	2,162
Central sector	92	1	267	146
Joint sector	89	67	194	88
Private sector	331	86	362	427
Total Sanction	1,664	516	2,316	2,823
Disbursement (Rs bn)	**FY21A**	**FY22A**	**FY23A**	**FY24A**
State sector	730	415	580	963
Central sector	39	0	31	15
Joint sector	21	8	23	59
Private sector	93	89	224	240
Total Disbursement	883	512	858	1,277

Source: Company, Emkay Research

Exhibit 41: Sanction disbursement trend

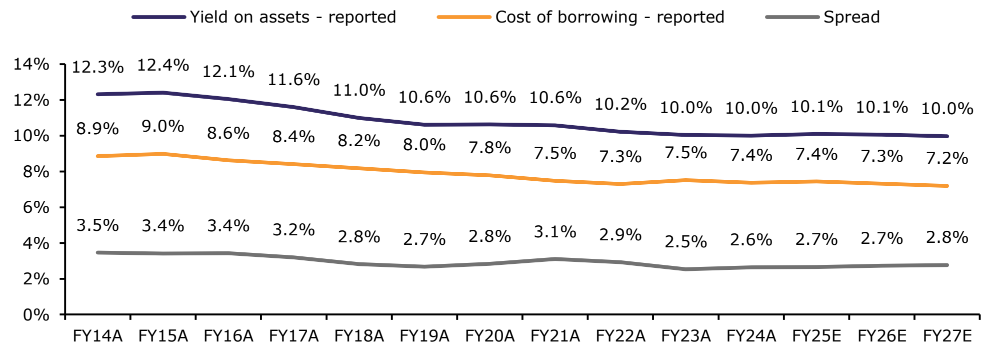


Source: Company, Emkay Research

Resilient margins sustained by easing cost of funds

PFC stands out as a strategic player in power financing, leveraging its deep expertise to identify and fund projects with attractive interest spreads. While the company's growing focus on renewable energy and diversification into infrastructure financing aligns with evolving market dynamics, these segments generally yield lower returns than traditional thermal generation. As a result, we anticipate a yield moderation of ~10bps over the forecast period.

Exhibit 42: Yield to see compression on account of PFC entering newer segments



Source: Company, Emkay Research

PFC's AAA credit rating by multiple agencies reflects its strong financial position and robust liability management. The company employs a diversified funding mix to maintain low borrowing costs, with 60% sourced from domestic bonds, 18% from term loans, and 17% from foreign-currency loans. Even after hedging, foreign loans offer a cost advantage, further enhancing its competitive edge.

Exhibit 43: Best-in-class credit rating

Agency	CRISIL	ICRA	CARE	Fitch Ratings	Moody's
Long-Term Borrowings	AAA	AAA	AAA	-	-
Short-Term Borrowings	A1+	A1+	A1+	-	-
Foreign Borrowings	-	-	-	BBB-	Baa3

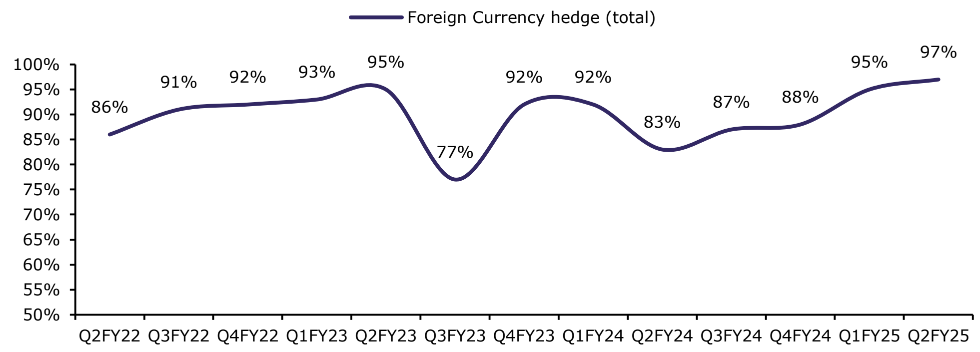
Source: Company, Emkay Research

Exhibit 44: Diverse source of borrowings

Borrowing mix	Q2 FY22	Q3 FY22	Q4 FY22	Q1 FY23	Q2 FY23	Q3 FY23	Q4 FY23	Q1 FY24	Q2 FY24	Q3 FY24	Q4 FY24	Q1 FY25	Q2 FY25
Domestic Bonds	60%	59%	58%	58%	57%	57%	57%	58%	58%	58%	59%	60%	60%
RTL from Banks/FIs	20%	20%	21%	20%	19%	20%	19%	18%	18%	19%	19%	18%	18%
Foreign Currency Borrowing	16%	17%	18%	18%	18%	18%	18%	18%	18%	18%	18%	17%	18%
Subordinated Liabilities	3%	3%	3%	3%	3%	3%	3%	2%	2%	2%	1%	1%	1%
54EC Bonds	1%	1%	1%	1%	2%	2%	2%	2%	2%	2%	2%	2%	2%
CP	1%	0%	0%	0%	0%	0%	0%	1%	0%	0%	0%	0%	0%
Others	0%	0%	0%	0%	1%	1%	1%	1%	2%	1%	1%	0%	0%

Source: Company, Emkay Research

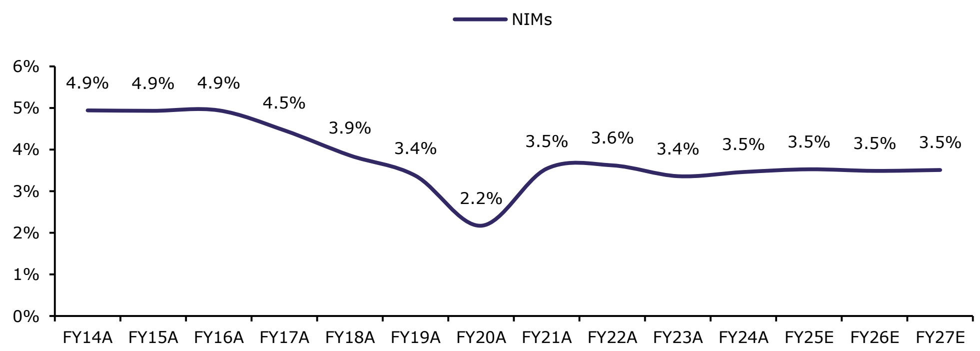
Exhibit 45: Most foreign borrowings are hedged, thus reducing volatility



Source: Company, Emkay Research

With the interest rate cycle expected to peak, we anticipate a shift toward rate cuts in H2FY25E. Combined with PFC's active treasury management and focus on cost efficiency, this should help moderate borrowing costs and sustain overall margins at ~3.5%. These strong points position PFC as a stable and attractive investment option in the evolving energy and infrastructure sectors.

Exhibit 46: NIMs to stay broadly stable despite marginal compression in yields

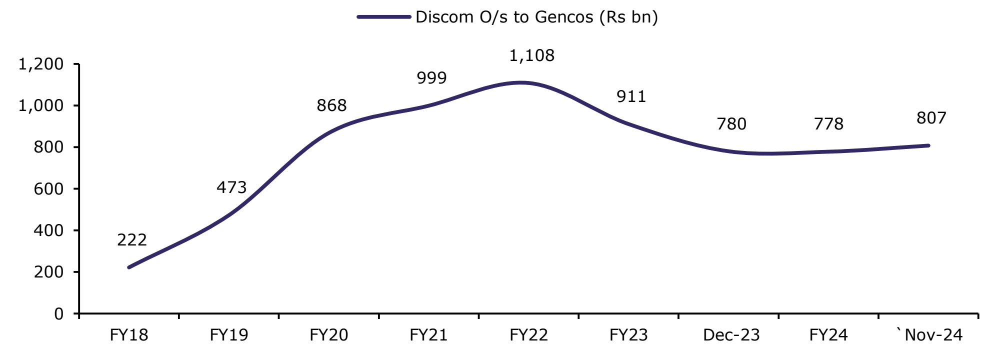


Source: Company, Emkay Research

Improving financial health of borrowers resulting in lower credit cost

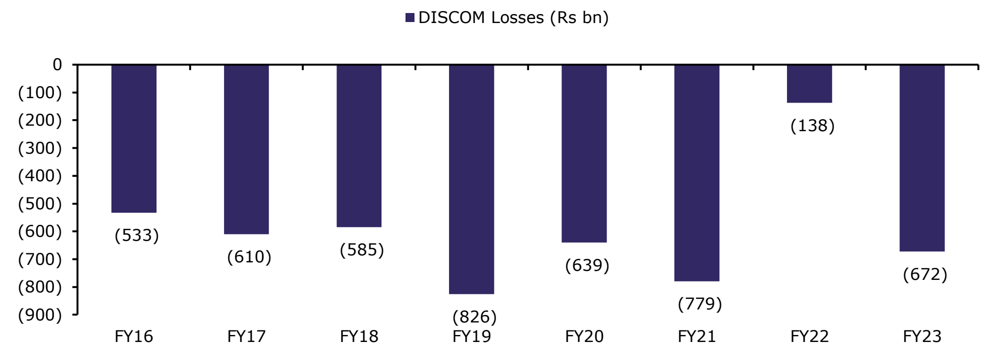
India's power sector has long struggled with the financial instability of state-owned DISCOMs, characterized by persistent cash flow deficits, tariffs set below operating costs, and delayed state subsidy disbursals. These challenges disrupt the entire supply chain, causing delay in payment to transmission and generation companies. In response, the Central Government, supported by PFC, implemented reforms including a centralized portal for tracking payments, penalties for delayed disbursements, and mandatory state-backed loan guarantees. While these initiatives have enhanced DISCOMs' financial discipline and operational metrics, the sector continues to face rising aggregate losses, underscoring the need for deeper structural changes.

Exhibit 47: GoI initiatives resulting in reduction of DICOM dues



Source: PRAAPTI, Emkay Research

Exhibit 48: DISCOMs remain in losses despite multiple supportive schemes by the GoI



Source: Report on Performance of Power Utilities, Emkay Research

PFC is also benefiting from the resolution of legacy assets, primarily thermal power projects, through both – the National Company Law Tribunal (NCLT) and other channels. In many cases, recovery proceeds have exceeded provisioning, contributing positively to PFC's profitability. With an increasing share of renewable energy and state-backed loans in its portfolio, stress in the system has significantly reduced for the company. Further, tighter underwriting standards and improved coal procurement dynamics have mitigated risks, leading to more stable operations.

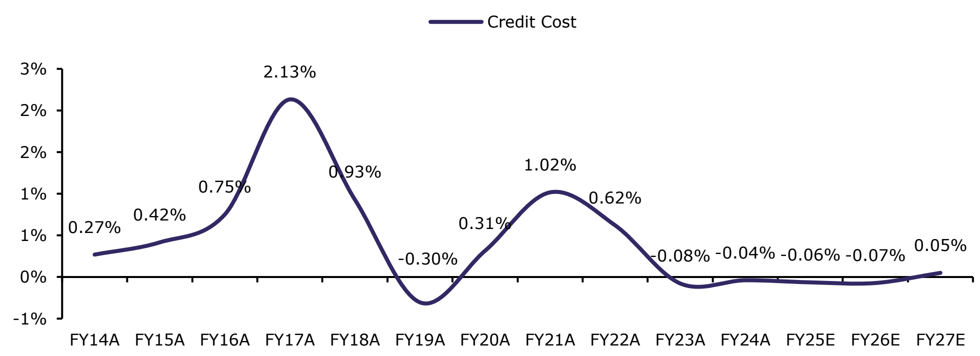
We anticipate PFC's credit costs to remain low, at ~5bps, driven by ongoing asset resolutions, accelerated recovery of stressed assets, and the upgradation of Stage 3 assets, which are expected to generate write-backs over the next two years.

Exhibit 49: Higher write-backs from resolved projects to keep credit cost in check

Stressed Asset and Resolution	FY22	FY23	FY24	Q2FY25	Current Status
Under the NCLT					
Number of projects	**14**	**13**	**13**	**12**	
Resolution amount (Rs bn)	**153.4**	**139.1**	**139.0**	**115.2**	
Project under liquidation (7 projects; Rs bn)				*26.1*	
Project under resolution (5 projects; Rs bn)				*89.0*	
KSK Mahanadi				*33.0*	*Evaluation of the bid is under way, and PFC expects a recovery of more than 100% (PCR of 55%)*
Lanco Amarkantak				*23.8*	*The asset has been resolved through NCLT; expect provision reversal of ~Rs2bn*
Sinnar Power				*30.0*	*PFC has invited bids and is expected to finalize the evaluation and submit it to the NCLT for approval (PCR of 80%)*
Others				*2.3*	
PCR on these projects	71%	77%	77%	78%	
PCR on projects under liquidation				100%	
Outside the NCLT					
Number of projects	**9**	**9**	**7**	**6**	
Resolution amount (Rs bn)	**55.78**	**25.9**	**21.74**	**18.2**	
TRN Energy				*11.4*	*In the advanced stage of resolution; expect resolution in current FY (PCR of 50%)*
Shiga Energy				*5.2*	*In the advanced stage of resolution; expect resolution in current FY (PCR of 50%)*
Others				*1.6*	
PCR on these projects	62%	51%	55%	48%	

Source: Company, NCLT, Emkay Research

Exhibit 50: Credit cost to remain low on account better recoveries and write-back of provision



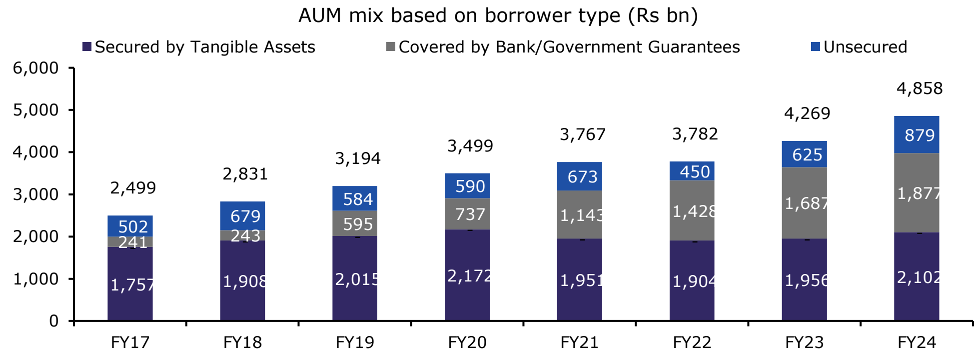
Source: Company, Emkay Research

Strengthening asset quality supported by GoI schemes

PFC has shown an improving trend in standard assets, supported by strong focus on resolving bad assets and by rapid progress in this direction. Over the years, power financing NBFCs have experienced significant enhancements in asset quality, as evidenced in the marked decline in gross NPAs. This improvement has been driven by key measures, including the restructuring of stressed assets, non-performing loan write-offs, reducing slippages, higher provisioning, and growing share of loans backed by State government guarantees. Additionally, recent Central Government schemes have introduced conditions to extend guarantees for these loans, further bolstering asset quality.

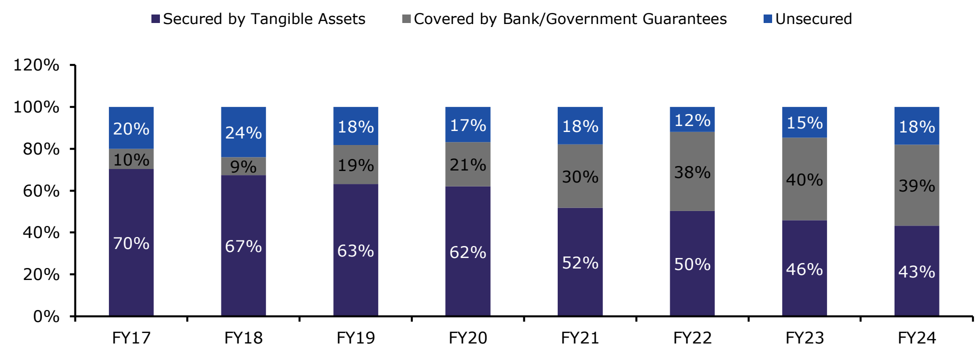
PFC has made significant strides in resolving critical assets, particularly accelerating the pace of resolutions since the pandemic. Over the past five years, the stressed asset book has decreased by approximately 55%, dropping from Rs294.6bn in Sep-19 to Rs133.4bn as of Sep-24. Additionally, net NPAs have declined by around 75%, reflecting substantial financial improvement.

Exhibit 51: Around 82% of the portfolio is secured by assets or backed by government guarantee



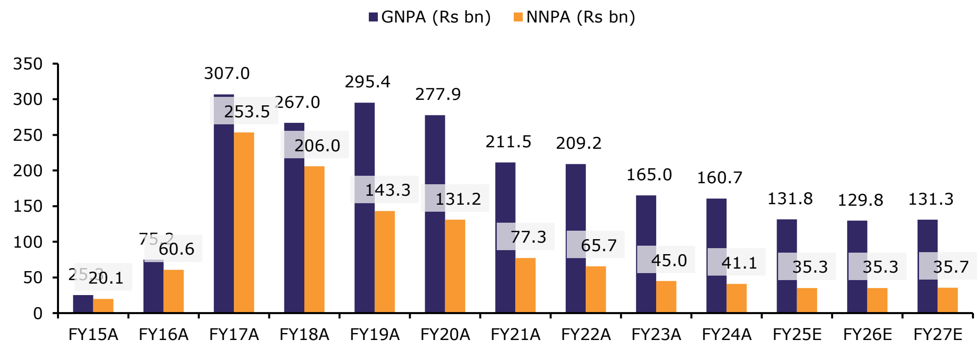
Source: Company, Emkay Research

Exhibit 52: Increasing funding toward projects backed by the government/government guarantee



Source: Company, Emkay Research

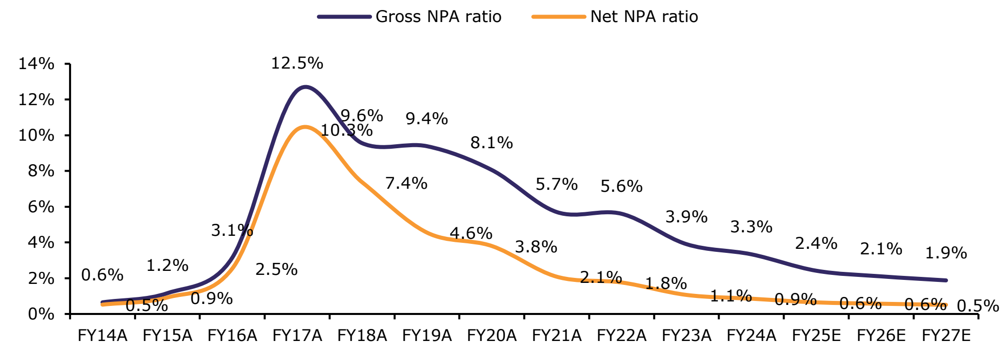
Exhibit 53: Improving asset quality



Source: Company, Emkay Research

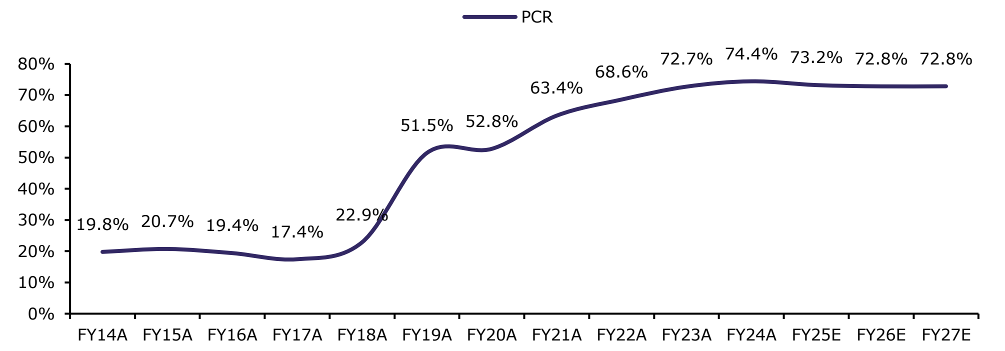
We anticipate this positive momentum to continue, driven by strong power demand that ensures robust traction for these projects. Consequently, we expect write-backs to be recognized in the income statement for FY25/26. Further, credit costs for PFC are projected to remain low, between -5bps and 5bps over FY25-27.

Exhibit 54: Lowest NPA in the last 8 years and zero NPAs added in the last 1 year



Source: Company, Emkay Research

Exhibit 55: Strong provision coverage at Stage 3



Source: Company, Emkay Research

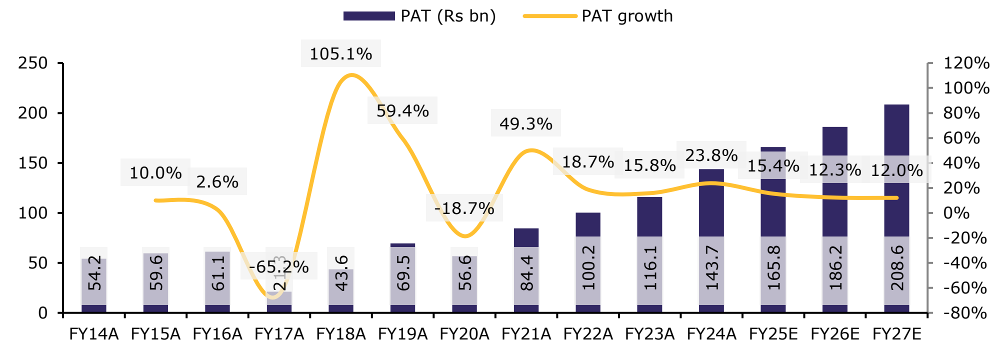
Enhanced profitability driven by stable margins and reduced credit costs

PFC's sanctioned loans are well-positioned to translate into disbursements over the next few years, providing strong visibility for healthy loan growth. We estimate a robust ~13.2% loan CAGR over FY25-27E, driven by a steady pipeline of project funding and disbursement momentum. While there is a possibility of some compression in net interest margins (NIMs), we believe this will be effectively counterbalanced by sustained improvements in asset quality.

The power sector's favorable outlook further strengthens our confidence, as we do not expect the formation of any new stressed assets over the next two years at least. Additionally, the resolution of existing stressed projects is likely to keep credit costs at low levels, reducing provisioning pressure and enhancing profitability. The potential for write-backs during this period adds further upside to earnings.

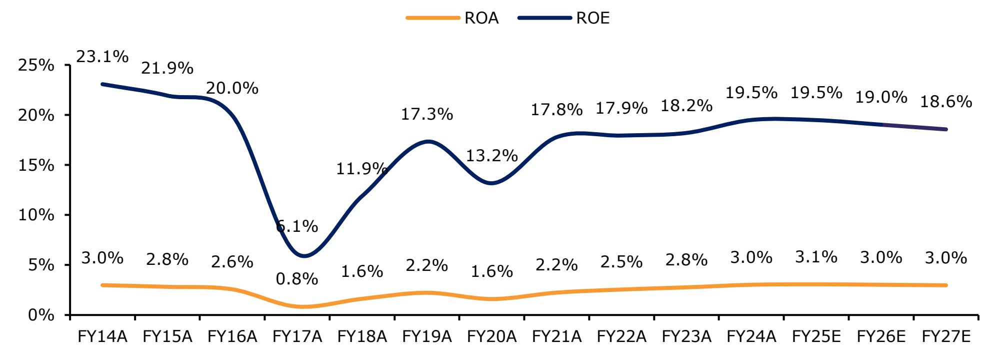
These dynamics create a solid foundation for a stable earnings growth trajectory. We project ~13% PAT CAGR over FY25-27E, supported by efficient capital utilization and improving operational metrics. By FY27E, this growth is likely to result in RoA of ~3% and RoE of ~19%, underscoring PFC's resilience and profitability potential in a competitive financial landscape. This outlook reflects not only the inherent strength of its business model but also its ability to adapt effectively to the evolving sectoral dynamics.

Exhibit 56: PAT to remain strong and continue growing, at 12% CAGR, over the forecast period



Source: Company, Emkay Research

Exhibit 57: Overall profitability to remain healthy, with ROA and ROE remaining broadly at current levels

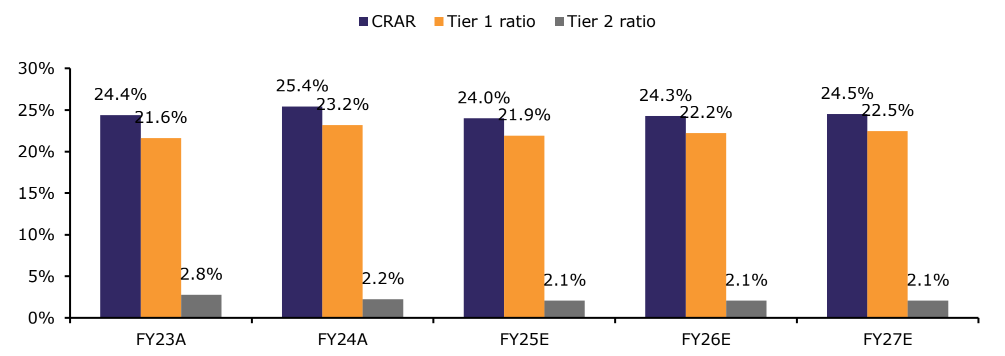


Source: Company, Emkay Research

Capital Adequacy

As of Sep-24, PFC's overall capital adequacy stands at a robust ~24.86%. We expect it to remain at comfortable levels, supported by healthy internal accruals and a loan portfolio predominantly backed by State guarantees, which require lower capital. This strong capital position is well-equipped to sustain a projected 13.2% loan CAGR over the next three years.

Exhibit 58: Strong capital adequacy supporting growth



Source: Company, Emkay Research

ROE Tree

Exhibit 59: DuPont Analysis

(on average assets)	FY23	FY24	FY25	FY26	FY27
Interest income	9.0%	9.2%	9.2%	9.1%	9.1%
Interest expended	5.5%	5.9%	5.8%	5.7%	5.6%
Net Interest Income	3.4%	3.3%	3.4%	3.4%	3.5%
Other Income (Treasury / others) / Avg. Assets	0.5%	0.5%	0.6%	0.5%	0.5%
Income Yield / Avg. Assets	3.9%	3.8%	3.9%	4.0%	4.0%
Op. Cost (Other costs) / Avg Assets	0.1%	0.1%	0.1%	0.1%	0.1%
Operating profit / Avg Assets	3.8%	3.7%	3.8%	3.8%	3.9%
Provisions / Avg. Assets	-0.1%	0.0%	-0.1%	-0.1%	0.0%
Exceptional Item	0.5%	0.0%	0.1%	0.1%	0.1%
Pre-Tax RoAssets	3.4%	3.7%	3.8%	3.8%	3.8%
Tax Retention Rate	82%	82%	80.5%	80.2%	80.0%
Post Tax RoAssets	2.8%	3.0%	3.1%	3.0%	3.0%
Leverage = Avg. Assets / Avg. Equity	6.6	6.4	6.4	6.3	6.2
ROE (Leverage * RoAssets)	18.2%	19.5%	19.5%	19.1%	18.8%

Source: Company, Emkay Research

Valuation argument

Over the past decade (FY14-24), PFC has delivered a steady performance, achieving average ROE of ~17% and AUM CAGR of ~10%. Despite this, the stock has historically traded at an average 1-year forward P/BV of 0.8x (consolidated). This subdued valuation can be attributed to the significant provisions made during FY14-18, primarily due to stress in private-sector thermal power plants. Key challenges during that period included the absence of PPAs, inadequate coal supply, poor financial health of DISCOMs impacting the power sector's supply chain, and application of RBI's stressed asset circulars and retrospective restructuring norms.

As the incremental stress began to ease, the NBFC sector faced a liquidity crunch triggered by the IL&FS crisis, which was further prolonged by Covid-19. However, the post-pandemic recovery brought a significant shift in the power sector, as a power shortage cycle emerged, placing power-generating companies in a more favorable position.

The sector's outlook has been further strengthened by structural reforms, such as the implementation of Revamped Distribution Sector Scheme (RDSS), Late Payment Surcharge (LPS) rules, and Liquidity Infusion Schemes (LIS). Additionally, the improving financial health of DISCOMs has led to a substantial reduction in asset quality risks. The shorter gestation periods of renewable energy projects, coupled with increased participation from corporates with strong balance sheets, have added to the sector's resilience. Further, the acquisition of legacy stressed thermal assets by private players has created opportunities for write-backs, thus enhancing profitability.

Over the past 24 months, PFC's stock has witnessed a significant re-rating, rising from a P/BV of 0.6x to 1.5x (1-year forward - consolidated), well above its 10-year average of 0.8x (consolidated). This re-rating has been driven by strong growth prospects in the current cycle, the resolution of legacy stressed assets, and earnings upgrades supported by write-backs. These developments have fundamentally improved market perception, leading to a notable upward shift in the stock's valuation.

Exhibit 60: Valuation Matrix

PFC	CMP/TP (Rs)	Upside	Mkt Cap (Rs bn)	P/BV (x)			P/E (x)			RoA			RoE			Book Value (Rs/sh)			Adj EPS (Rs)		
				FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E
At current market price	448	33.8%	1,479	1.7	1.5	1.3	9.1	8.1	7.3	3.1%	3.0%	3.0%	19.5%	19.0%	18.6%	276	315	359	50	56	63
At target price	600			2.2	1.9	1.7	11.9	10.6	9.5							276	315	359	50	56	63

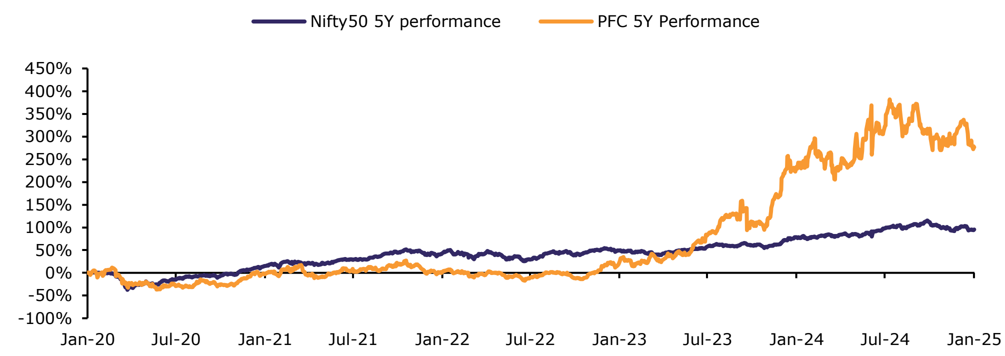
Source: Company, Emkay Research

Exhibit 61: SOTP-based valuation

	Fair value (Rs/sh)	No of shares (mn)	Market cap (Rs bn)	PFC's stake	PFC's stake value (Rs bn)	Holdco discount	Value (Rs bn)
PFC - Standalone	400.0	3,300	1,320,040	100%	1,320,040	0%	1,320,040
REC	650.0	2,633	1,711,450	52.63%	900,736	25%	675,552
PFC - Total							1,995,592
PFC - Fair value per share	**600**						
Standalone FY26E P/BV (x)	**FY25E**	**FY26E**	**FY27E**				
Adjusted BV	232	271	315				
Standalone Dec-25E TP	400	400	400				
P/BV (x)	1.7	1.5	1.3				
Standalone							
Standalone P/BV (x) at CMP	1.3	1.1	0.9				

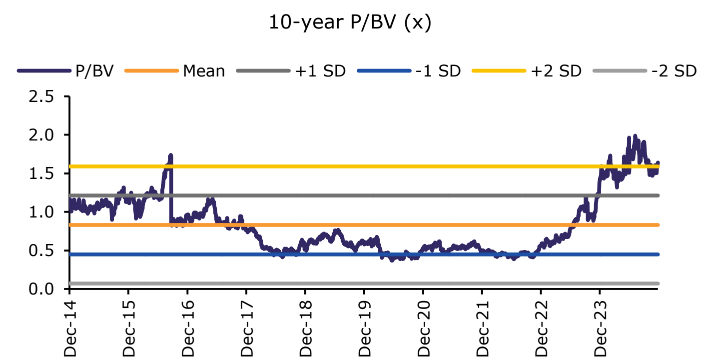
Source: Company, Emkay Research

Exhibit 62: Price performance relative to the NIFTY over the last 24 months



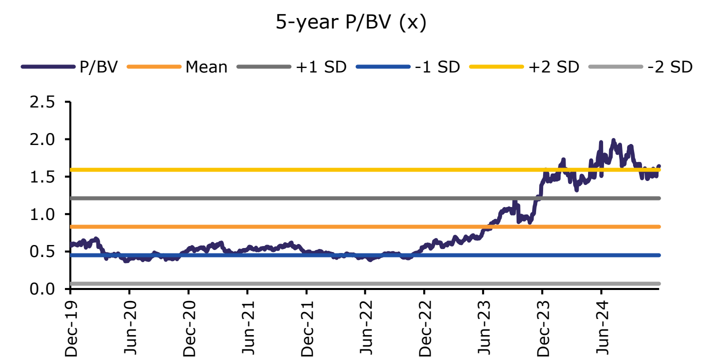
Source: Company, Emkay Research

Exhibit 63: One-year forward P/BV – 10 years



Source: Company, Emkay Research

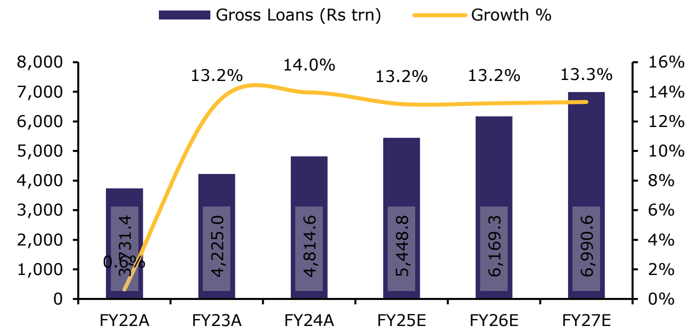
Exhibit 64: One-year forward P/BV – 5 years



Source: Company, Emkay Research

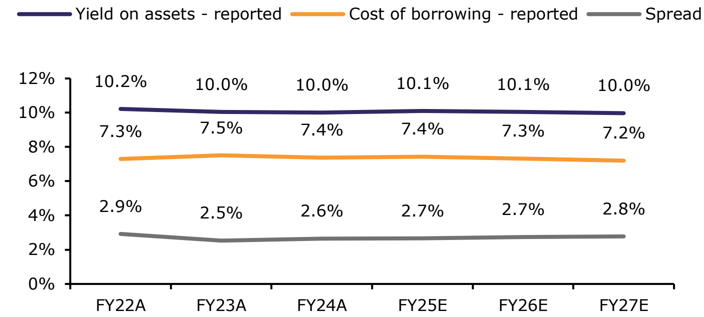
Story in charts

Exhibit 65: Healthy AUM growth



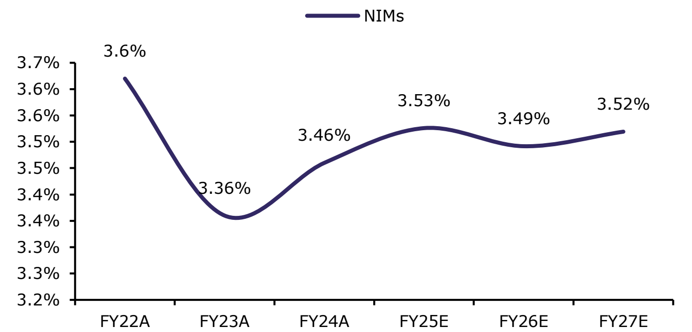
Source: Company, Emkay Research

Exhibit 66: Yield compression to be offset by moderating CoFs



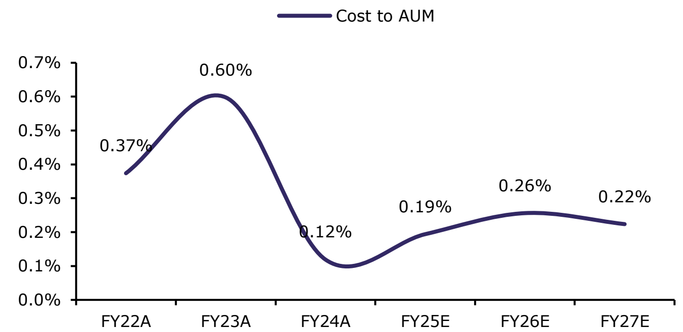
Source: Company, Emkay Research

Exhibit 67: Margins to remain broadly stable



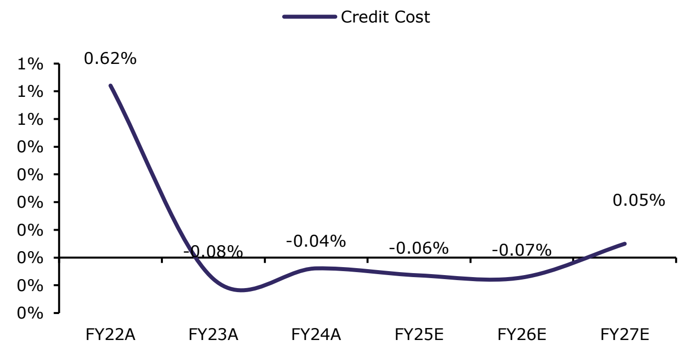
Source: Company, Emkay Research

Exhibit 68: Cost to see a marginal uptick



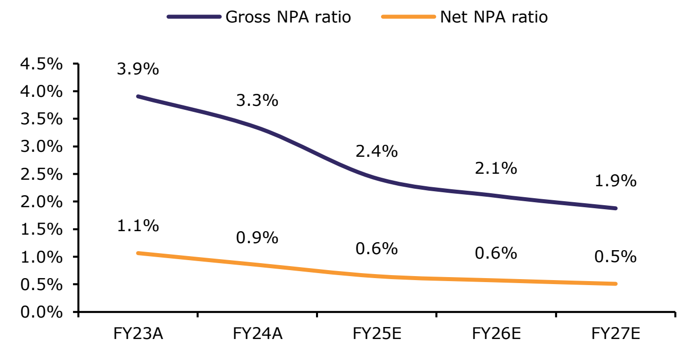
Source: Company, Emkay Research

Exhibit 69: Credit costs remain low on account of write-backs



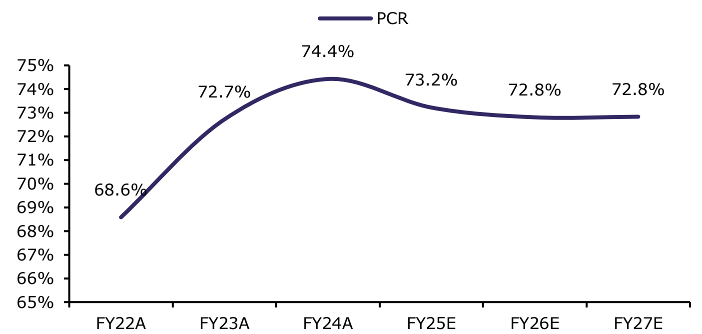
Source: Company, Emkay Research

Exhibit 70: Asset quality continues to improve



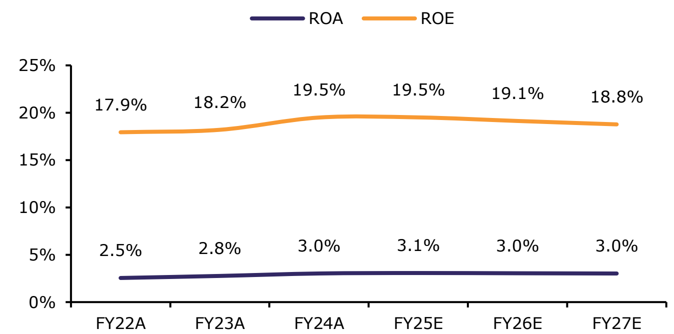
Source: Company, Emkay Research

Exhibit 71: PFC will maintain healthy provision on stressed loans



Source: Company, Emkay Research

Exhibit 72: Margins to remain broadly stable

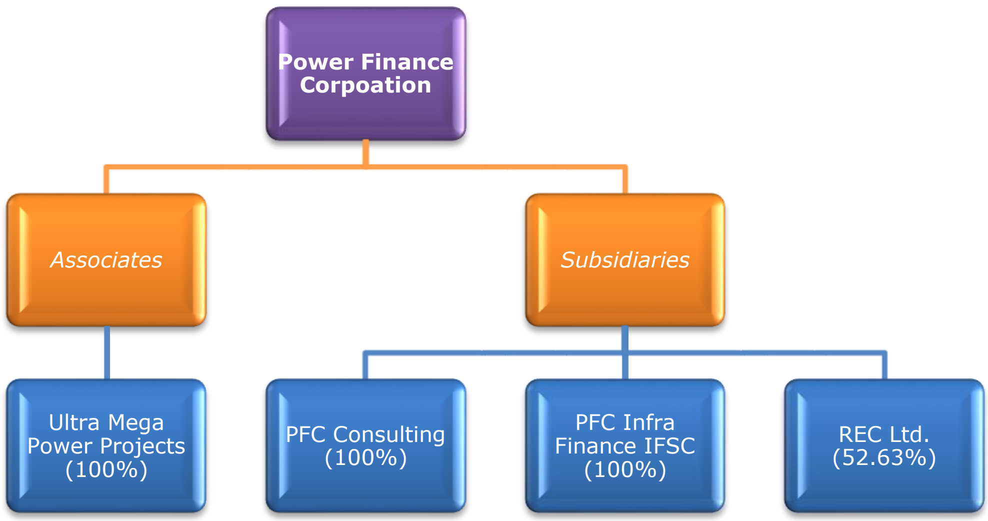


Source: Company, Emkay Research

Key Risks

- **Slower-than-expected growth:** The company's business model is highly reliant on sustaining loan growth. Any disruption—whether stemming from company-specific factors such as intensified competition from banks or from the broader macroeconomic challenges like asset quality deterioration—could adversely impact growth. A slowdown in loan growth is likely to compress ROE and lead to a de-rating of the stock
- **Asset quality issues:** A decline in asset quality, owing to macroeconomic pressures or company-specific issues, poses a significant risk. Rising NPAs and higher provisioning/increased credit costs could compress profitability, leading to EPS downgrades and a potential stock de-rating.
- **Diversification in non-power infra projects:** PFC's current focus on government-backed infrastructure projects ensures low risk. However, a shift toward private infrastructure or industrial loans, which lack revenue lock-ins and government backing, could heighten credit risks. Limited expertise in managing private sector exposure further adds to the challenges.
- **Increasing competition leading to margin compression:** Although banks have largely refrained from lending to the power sector due to perceived lower credit risks, their increased participation could lead to a compression in NIMs for power financiers. Additionally, the growing share of RE projects and a highly competitive sector with lower spreads could further pressure margins.
- **Draft RBI regulations on project financing:** The RBI's draft guidelines propose stricter project financing regulations, raising the provision requirement from 0.4% to 5%, with reductions to 2.5% and 1%, respectively, as projects generate cash flow, subject to specific conditions. These changes would apply to infrastructure, non-infrastructure, and commercial real estate projects for all regulated entities. Although we believe the likelihood of these norms being implemented as currently proposed is low, they still present a risk to the broader sector.

Exhibit 73: Organizational structure



Source: Company, Emkay Research

Exhibit 74: Shareholding pattern

Name	% Holding
Promoter:	
Government of India	**56.0**
Public Shareholders:	
Mutual Funds	**11.6**
Nippon India Mutual Fund	1.6
HDFC Mutual Fund	2.0
Kotak Mutual Fund	1.8
DSP Mutual Fund	1.2
Alternate Investment Funds	0.5
Banks	0.1
Insurance company	**4.5**
LIC	2.1
Provident Funds / Pension Funds	0.7
NBFCs	0.0
Foreign Portfolio Investors	**17.7**
Government of Singapore	1.1
Others	8.8
Total	**100.0**

Source: Company, Emkay Research

Exhibit 75: Key management personal

Name	Designation	Brief Profile
Parminder Chopra	Chairman and MD	Parminder Chopra has been serving as the Chairman and Managing Director (CMD) of Power Finance Corporation Limited (PFC) since August 14, 2023, becoming the first woman to lead India's largest NBFC. With over 35 years of experience in the power and financial sectors, she previously held the position of Director (Finance) at PFC, where she spearheaded record financial performance, achieving the highest net profit and net worth, and the lowest NPAs. Chopra played a pivotal role in implementing the Rs1.2trn Liquidity Infusion Scheme for the power distribution sector under the Atmanirbhar Bharat initiative. A qualified Cost and Management Accountant with a Postgraduate Diploma in Business Management, she has led PFC's efforts in financing clean energy, infrastructure, and India's energy transition goals.
Rajiv Ranjan Jha	Director(Projects)	Rajiv Ranjan Jha has been serving PFC since March 1997 and currently holds the position of Executive Director (Projects) since May 27, 2019. He holds a Bachelor's Degree in Mechanical Engineering from NIT Jamshedpur (Ranchi University) and a Diploma in Management from IGNOU, with over 33 years of experience in the power sector. At PFC, he has managed loan portfolios for the western region, including Maharashtra, Gujarat, Madhya Pradesh, Chhattisgarh, and Goa, and has led Consortium Lending and Renewable Energy financing initiatives. He has significant expertise in project appraisal, particularly for Independent Power Projects and Ultra Mega Power Projects.
Manoj Sharma	Director (Commercial)	Manoj Sharma is a Chartered Accountant and Law graduate (LLB) with over 30 years of experience in the power sector. He joined PFC in 1990 and currently serves as Director (Commercial), after previously holding the position of Executive Director (In-Charge) of the Commercial Division. At PFC, he has managed diverse functions, including institutional and entity appraisal, resource mobilization, financial analysis, debt syndication, and stressed asset resolution. He has played a key role in formulating lending policies, developing appraisal frameworks, and ensuring compliance with regulatory standards. He is also the Chairman of PFC Projects Limited and Jharkhand Infrapower Limited, contributing to PFC's leadership in the power sector.
Sandeep Kumar	Director (Finance)	Sandeep Kumar assumed the charge of Director (Finance) at PFC on July 11, 2024, following his tenure as Executive Director (Finance) and Chief Financial Officer (CFO) since January 2020. A Fellow Member of the Institute of Chartered Accountants of India with over 34 years of experience, he holds a Bachelor's degree in Commerce (Honors). He has extensive expertise in fund mobilization, asset-liability management, lending operations, and policy formulation, significantly contributing to PFC's profitability and market leadership. He has played a key role in IT transformation, loan recovery guidelines, implementation of Ind-AS standards, and execution of government schemes like the Liquidity Infusion Scheme (LIS) and Late Payment Surcharge (LPS).
Manoj Sharma	Nominee Director – Power Finance Corporation Limited.	Manoj Sharma has been serving as the Nominee Director of Power Finance Corporation Limited (PFC) on the Board of REC Limited since July 11, 2023. A Chartered Accountant and Law graduate (LLB), he is currently the Director (Commercial) at PFC and brings over 32 years of experience in the power sector. Through his career at PFC, he has managed diverse areas such as entity appraisal, financial analysis, resource mobilization, debt syndication, and resolution of stressed assets. He has played a key role in shaping lending policies, monitoring loan assets, and ensuring compliance with regulatory frameworks. Sharma also serves as Chairman of PFC Projects Limited, contributing significantly to resolution mechanisms and financial reforms within the power sector.
Shashank Misra	Government Nominee Director	Shashank Misra, an IAS Officer of the 2007 batch (Madhya Pradesh cadre), holds a BTech degree in Electrical Engineering from IIT Delhi and currently serves as Joint Secretary in the Ministry of Power, Government of India. He is also a Government Nominee Director on the Board of REC Limited. Prior to this, he served in the Department of Revenue, Ministry of Finance, and held key leadership roles in Madhya Pradesh, including Managing Director of Madhya Pradesh Road Development Corporation, Building Development Corporation, and State Asset Management Company. He has also served as Chairman of Ujjain Smart City Limited and CEO of Madhya Pradesh Rural Road Development Authority. Misra brings extensive experience in infrastructure development, governance, and policy implementation to his current role.

Source: Company, Emkay Research

Power Finance Corporation: Standalone Financials and Valuations

Profit & Loss

Y/E Mar (Rs mn)	FY23	FY24	FY25E	FY26E	FY27E
Interest Income	376,453	436,411	494,089	558,169	628,479
Interest Expense	232,826	280,138	311,561	347,462	386,428
Net interest income	**143,627**	**156,274**	**182,527**	**210,707**	**242,051**
NII growth (%)	2.4	8.8	16.8	15.4	14.9
Non interest income	20,203	23,930	30,614	33,137	37,427
Total income	**163,831**	**180,203**	**213,141**	**243,844**	**279,478**
Operating expenses	6,040	6,691	7,503	8,682	9,317
PPOP	**157,791**	**173,512**	**205,638**	**235,162**	**270,161**
PPOP growth (%)	2.8	10.0	18.5	14.4	14.9
Provisions & contingencies	(2,962)	(1,712)	(3,223)	(4,111)	3,239
PBT	**160,753**	**175,223**	**208,861**	**239,274**	**266,922**
Extraordinary items	19,047	(1,034)	2,982	6,998	6,156
Tax expense	25,652	32,587	40,062	46,095	52,153
Minority interest	0	0	0	0	0
Income from JV/Associates	0	0	0	0	0
Reported PAT	**135,101**	**142,637**	**168,799**	**193,179**	**214,769**
PAT growth (%)	23.7	5.6	18.3	14.4	11.2
Adjusted PAT	**116,055**	**143,670**	**165,816**	**186,180**	**208,613**
Diluted EPS (Rs)	**44.0**	**45.8**	**50.2**	**56.4**	**63.2**
Diluted EPS growth (%)	15.8	4.2	9.7	12.3	12.0
DPS (Rs)	**13.3**	**13.5**	**15.1**	**16.9**	**19.0**
Dividend payout (%)	**30.1**	**29.5**	**30.0**	**30.0**	**30.0**
Effective tax rate (%)	16.0	18.6	19.2	19.3	19.5
Net interest margins (%)	3.4	3.5	3.5	3.5	3.5
Cost-income ratio (%)	3.7	3.7	3.5	3.6	3.3
PAT/PPOP (%)	73.5	82.8	80.6	79.2	77.2
Shares outstanding (mn)	2,640.1	3,300.1	3,300.1	3,300.1	3,300.1

Source: Company, Emkay Research

Balance Sheet

Y/E Mar (Rs mn)	FY23	FY24	FY25E	FY26E	FY27E
Share capital	26,401	33,001	33,001	33,001	33,001
Reserves & surplus	655,622	759,034	875,105	1,005,432	1,151,461
Net worth	**682,022**	**792,035**	**908,106**	**1,038,433**	**1,184,462**
Borrowings	**3,626,380**	**4,073,830**	**4,586,182**	**5,179,269**	**5,851,121**
Other liabilities & prov.	**139,928**	**189,965**	**247,057**	**266,117**	**289,314**
Total liabilities & equity	**4,448,331**	**5,055,830**	**5,741,346**	**6,483,819**	**7,324,896**
Net loans	4,104,980	4,694,995	5,352,294	6,074,854	6,894,959
Investments	173,041	202,200	222,419	233,540	245,217
Cash, other balances	16,181	2,218	5,514	6,259	7,103
Interest earning assets	**4,294,202**	**4,899,412**	**5,580,228**	**6,314,653**	**7,147,280**
Fixed assets	440	421	442	456	470
Other assets	153,688	155,997	160,677	168,711	177,146
Total assets	**4,448,331**	**5,055,830**	**5,741,346**	**6,483,819**	**7,324,896**
BVPS (Rs)	258.3	240.0	275.2	314.7	358.9
Adj. BVPS (INR)	258.3	240.0	275.2	314.7	358.9
Gross loans	4,224,980	4,814,620	5,448,774	6,169,334	6,990,564
Total AUM	**4,224,980**	**4,814,620**	**5,448,774**	**6,169,334**	**6,990,564**
On balance sheet	4,224,980	4,814,620	5,448,774	6,169,334	6,990,564
Off balance sheet	0	0	0	0	0
Disbursements	0	0	0	0	0
Disbursements growth (%)	0.0	0.0	0.0	0.0	0.0
Loan growth (%)	14.4	14.4	14.0	13.5	13.5
AUM growth (%)	13.2	14.0	13.2	13.2	13.3
Borrowings growth (%)	12.5	12.3	12.6	12.9	13.0
Book value growth (%)	14.9	(7.1)	14.7	14.4	14.1

Source: Company, Emkay Research

Asset quality and other metrics

Y/E Mar (Rs mn)	FY23	FY24	FY25E	FY26E	FY27E
Asset quality					
GNPL - Stage 3	165,020	160,732	131,770	129,770	131,270
NNPL - Stage 3	45,020	41,107	35,290	35,290	35,665
GNPL ratio - Stage 3 (%)	3.9	3.3	2.4	2.1	1.9
NNPL ratio - Stage 3 (%)	1.1	0.9	0.6	0.6	0.5
ECL coverage - Stage 3 (%)	72.7	74.4	73.2	72.8	72.8
ECL coverage - 1 & 2 (%)	0.0	0.0	0.0	0.0	0.0
Gross slippage - Stage 3	0	0	0	0	0
Gross slippage ratio (%)	0.0	0.0	0.0	0.0	0.0
Write-off ratio (%)	0.0	0.0	0.0	0.0	0.0
Total credit costs (%)	(0.1)	0.0	(0.1)	(0.1)	0.0
NNPA to networth (%)	6.6	5.2	3.9	3.4	3.0
Capital adequacy					
Total CAR (%)	24.4	25.4	24.0	24.3	24.5
Tier-1 (%)	21.6	23.2	23.2	23.2	23.2
Miscellaneous					
Total income growth (%)	2.9	10.0	18.3	14.4	14.6
Opex growth (%)	5.2	10.8	12.1	15.7	7.3
PPOP margin (%)	4.0	3.8	4.0	4.0	4.1
Credit costs-to-PPOP (%)	(1.9)	(1.0)	(1.6)	(1.7)	1.2
Loan-to-Assets (%)	92.3	92.9	93.2	93.7	94.1
Yield on loans (%)	10.0	10.0	10.1	10.1	10.0
Cost of funds (%)	7.5	7.4	7.4	7.3	7.2
Spread (%)	2.5	2.6	2.7	2.7	2.8

Source: Company, Emkay Research

Valuations and key Ratios

Y/E Mar	FY23	FY24	FY25E	FY26E	FY27E
P/E (x)	10.4	10.0	9.1	8.1	7.3
P/B (x)	1.8	1.9	1.7	1.5	1.3
P/ABV (x)	1.8	1.9	1.7	1.5	1.3
P/PPOP (x)	7.7	8.7	7.4	6.4	5.6
Dividend yield (%)	2.9	2.9	3.3	3.7	4.1
Dupont-RoE split (%)					
NII/avg AUM	3.6	3.5	3.6	3.6	3.7
Other income	0.5	0.5	0.6	0.6	0.6
Securitization income	0.0	0.0	0.0	0.0	0.0
Opex	0.2	0.1	0.1	0.1	0.1
Employee expense	0.0	0.0	0.0	0.0	0.0
PPOP	**4.0**	**3.8**	**4.0**	**4.0**	**4.1**
Provisions	(0.1)	0.0	(0.1)	(0.1)	0.0
Tax expense	4.0	3.9	4.1	4.1	4.1
RoAUM (%)	**3.4**	**3.2**	**3.3**	**3.3**	**3.3**
Leverage ratio (x)	6.2	6.1	6.0	6.0	5.9
RoE (%)	**18.2**	**19.5**	**19.5**	**19.1**	**18.8**

Quarterly data

Rs mn, Y/E Mar	Q2FY24	Q3FY24	Q4FY24	Q1FY25	Q2FY25
NII	37,289	41,578	42,373	43,280	44,083
NIM(%)	3.4	3.4	3.5	3.6	3.6
PPOP	47,111	45,709	46,495	43,156	54,792
PAT	38,474	33,772	41,355	37,179	43,704
EPS (Rs)	1,165.85	1,023.36	1,253.13	1,126.60	1,324.34

Source: Company, Emkay Research

BUY REC Ltd

Accelerating RE disbursements to catalyze growth

BFSI - NBFCs ▸ Initiating Coverage ▸ **January 3, 2025**

TARGET PRICE (Rs): 650

We initiate coverage on REC with BUY and target price of Rs650, implying FY26E P/BV of 1.85x. Favorable macroeconomic conditions, large-scale power sector capital expenditure, increased government focus on power reforms, and improved financial health across the power value chain create a compelling lending opportunity. Anticipated capex in the power sector, coupled with REC's strategic shift to increase its renewable energy share to 30% of its portfolio and its diversification into infrastructure and logistics, is projected to drive AUM CAGR of ~18.2% over FY24-27E. While diversification efforts and renewable energy financing may exert downward pressure on yields, REC's strong AAA credit rating, access to low-cost (including 54-EC) long-term funding (including foreign capital); and government guarantees mitigate margin risks, keeping net interest margins stable. Profitability is expected to benefit from improved recoveries of legacy assets, lower credit costs (given the high proportion of government-backed loans), and provision write-backs in the near term. Consequently, REC's AUM is estimated to grow to ~Rs8.4trn by FY27E, with robust RoA and RoE metrics of ~2.5% and ~20.5%, respectively, over FY25-27E. Based on these factors, we believe REC is well-positioned to capitalize on India's energy transition and infrastructure expansion.

REC Ltd: Financial Snapshot (Standalone)

Y/E Mar (Rs mn)	FY23	FY24	FY25E	FY26E	FY27E
Net profits	110,540	140,180	158,429	178,875	203,523
AUM growths (%)	12.9	17.1	17.5	18.0	19.0
NII growths (%)	(7.1)	6.2	22.3	16.6	18.7
NIMs (%)	2.4	3.6	3.6	3.4	3.5
PPOP growth (%)	(8.7)	8.0	22.3	12.9	16.2
Adj. EPS (Rs)	42.3	53.2	60.2	67.9	77.3
Adj. EPS growth (%)	0.4	25.7	13.0	12.9	13.8
Adj. BV (INR)	219.1	261.2	303.4	350.9	405.0
Adj. BVPS growth (%)	8.8	19.2	16.1	15.7	15.4
RoA (%)	2.5	2.8	2.7	2.6	2.5
RoE (%)	20.4	22.2	21.3	20.8	20.5
P/E (x)	12.2	9.7	8.6	7.6	6.7
P/ABV (x)	2.4	2.0	1.7	1.5	1.3

Source: Company, Emkay Research

Lending toward renewable energy and Infra loan to boost overall growth

Over the next five years, ~Rs25trn (~Rs19.3trn over FY22-27E) is expected to be invested in the power sector, with ~Rs16.9trn (FY24-30E) allocated for renewable energy. REC aims to capitalize on this growth, targeting an increase in its renewable energy portfolio share to 30% from the current ~10%, and doubling its book over the next five years. New segments likely yielding lower returns compared with conventional thermal power projects due to increased competition from banks is expected to result in marginal moderation (~10-15bps) in overall yields. However, REC's ability to access low-cost funding avenues, such as 54-EC bonds and foreign borrowings, positions it aptly to maintain a competitive borrowing rate. Consequently, we anticipate spreads and margins to be broadly stable at ~2.5% and ~3.5%, respectively.

Strong recoveries and viable project selection set to drive provision write-backs, ensuring low credit costs and robust asset quality

REC plays a pivotal role in advancing the Government of India (GoI)'s power sector reforms as the nodal agency for various schemes (like RDSS, DDUGJY, NEF, etc) under the Ministry of Power. It has been instrumental in developing new infrastructure and upgrading existing networks. REC has also benefited from resolving legacy thermal power assets through mechanisms like the NCLT, with expectation of recovery proceeds exceeding the provisioning over the next two years, thereby boosting profitability. Growing focus on renewable energy projects and on state-backed loans has significantly reduced system-level stress. Additionally, stricter underwriting practices and funding financially-sound projects have further mitigated risks. With ongoing asset resolutions, accelerated recovery of stressed assets and upgrades of Stage 3 assets expected to drive write-backs, we believe REC's credit cost to remain low at ~5bps over the next two years, thus supporting robust profitability and asset quality.

We initiate coverage on REC with BUY and TP of Rs650

We expect REC's AUM CAGR at ~18.2% over FY25-27E, on the back of emerging opportunities in renewable energy, charging infrastructure, modernization of the existing thermal power plants, and smart metering. The GoI's progressive initiatives, including the RDSS, LPS regulations, and Liquidity Infusion Schemes, have strengthened the financial stability of DISCOMs, significantly reducing asset quality risks. Additionally, the acquisition of stressed thermal assets by private players offers potential for write-backs, further enhancing profitability. REC's credit costs are projected to remain low at ~5bps over FY25-27E, while ROA/ROE are estimated at ~2.5%/~20.5%, respectively. REC's Dec-25E target price of Rs650 (implying FY26E P/BV of 1.85x) and growth potential combined with strong asset quality make for an attractive BUY.

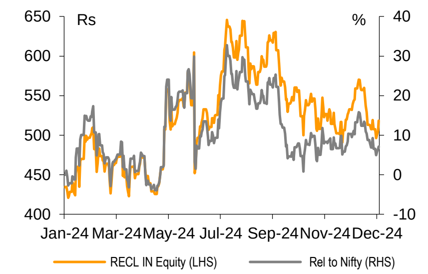
Target Price – 12M	Dec-25
Change in TP (%)	**NA**
Current Reco.	BUY
Previous Reco.	NR
Upside/(Downside) (%)	25.4
CMP (02-Jan-25) (Rs)	518.5

Stock Data	Ticker
52-week High (Rs)	654
52-week Low (Rs)	408
Shares outstanding (mn)	2,633.2
Market-cap (Rs bn)	1,365
Market-cap (USD mn)	15,920
Net-debt, FY25E (Rs mn)	48,524
ADTV-3M (mn shares)	8
ADTV-3M (Rs mn)	4,375.6
ADTV-3M (USD mn)	51.0
Free float (%)	-
Nifty-50	24,189
INR/USD	85.8
Shareholding, Sep-24	
Promoters (%)	52.6
FPIs/MFs (%)	21.2/14.3

Price Performance

(%)	1M	3M	12M
Absolute	(2.5)	(6.9)	23.5
Rel. to Nifty	(2.2)	(0.7)	10.6

1-Year share price trend (Rs)



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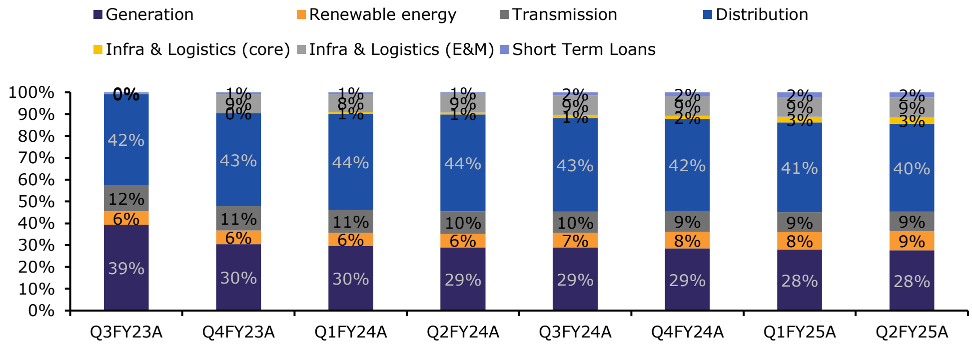
Investment thesis

- Big power capex and enough opportunities in renewable energy capacity
- Margins to remain broadly stable despite some pressure on yields
- Enhanced borrower financial health driving lower credit costs
- Better asset quality through legacy resolution and prudent underwriting
- Improved profitability driven by stable margins and lower credit costs

Big power capex and enough opportunities in renewable energy capacity

REC, with a legacy of 55 years of dedicated service to the nation, has been a pivotal force in India's progress. Originally founded to support the power sector, REC has since expanded its scope to include funding for infrastructure and logistics. The company offers long-term loans and other financial solutions to State and Central entities as well as private companies, for facilitating the development of critical infrastructure assets across the country.

Exhibit 76: REC's loans to DISCOMs dominate its overall loan advance



Source: Company, Emkay Research

Exhibit 77: AUM mix – Increasing share of RE

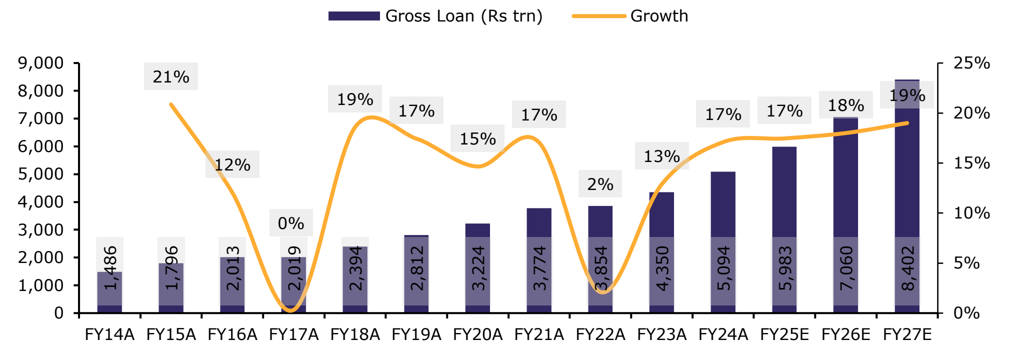
AUM mix (Rs bn)	Q3FY23A	Q4FY23A	Q1FY24A	Q2FY24A	Q3FY24A	Q4FY24A	Q1FY25A	Q2FY25A
Generation	1,616.4	1,325.2	1,341.7	1,375.6	1,442.8	1,452.7	1,479.1	1,509.4
Renewable Energy	254.9	271.0	280.2	298.3	332.5	389.7	429.4	478.2
Transmission	494.0	483.3	477.9	483.9	481.3	480.5	476.5	485.9
Distribution	1,716.0	1,858.1	1,995.1	2,101.7	2,136.6	2,146.7	2,183.1	2,199.9
Infra & Logistics (core)	-	-	36.1	46.9	68.5	76.8	134.3	165.0
Infra & Logistics (E&M)	10.0	382.5	381.5	409.3	437.3	458.8	475.4	493.1
Short Term Loans	20.3	30.2	31.4	27.1	75.7	88.6	119.6	129.7
Total	4,111.5	4,350.1	4,543.9	4,742.8	4,974.7	5,093.7	5,297.4	5,461.2

Source: Company, Emkay Research

(REC provides a variety of financial products tailored to the power sector, including term loans—Short/Medium/Long, equipment financing, revolving bill facility, and transitional financing for generation, transmission, and distribution projects. Expanding beyond Power, REC has diversified into Infrastructure and Logistics, and targets a 33% mix of Infrastructure and Transportation. Its clientele includes Central and State power utilities, power equipment manufacturers, government departments, and dynamic private sector entrepreneurs.)

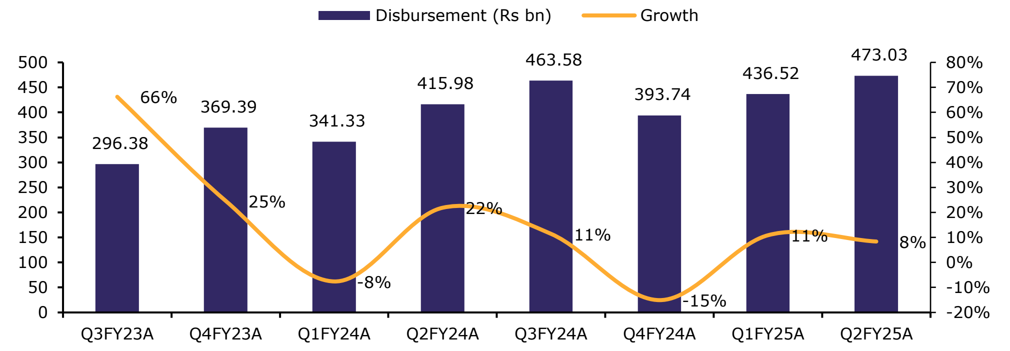
Over the next five years, ~Rs25trn (~Rs19.3trn over FY22-27E) is expected to be invested in the power sector, encompassing generation and transmission & distribution (T&D). Of this, ~Rs16.9trn (during FY24-30) is earmarked for renewable energy, aligning with India's goal of achieving 500GW of renewable capacity by 2030. REC aims to grow its assets under management (AUM) to Rs10trn by or before 2030, with a vision of renewable energy constituting 30% of its total loan book. This ambitious target positions REC to play a significant role in funding RE and infrastructure projects, leveraging the substantial opportunities in these sectors. We estimate that over FY24-27, REC would log 18.2% loan CAGR over FY24-27E, led by strong disbursements in RE and Infrastructure financing.

Exhibit 78: AUM growth driven by robust disbursement in RE and Logistics



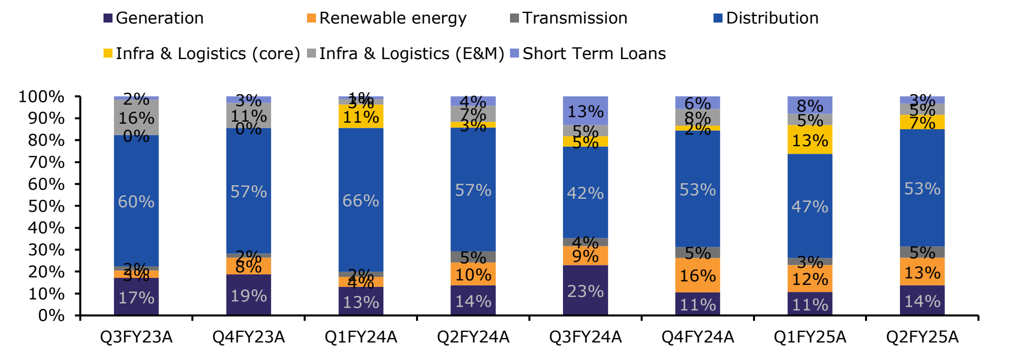
Source: Company, Emkay Research

Exhibit 79: Disbursements to DISCOMs remain strong, with ~50% share of overall disbursement



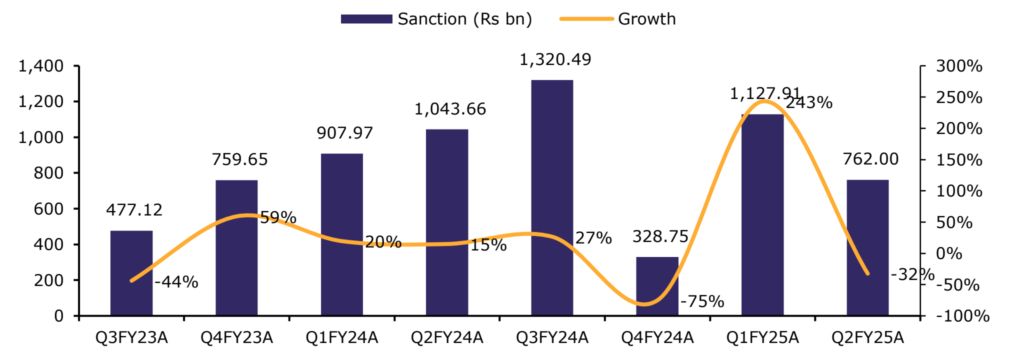
Source: Company, Emkay Research

Exhibit 80: Disbursement in the renewable energy (RE) segment expected to grow, as REC targets 30% of its RE portfolio by 2030



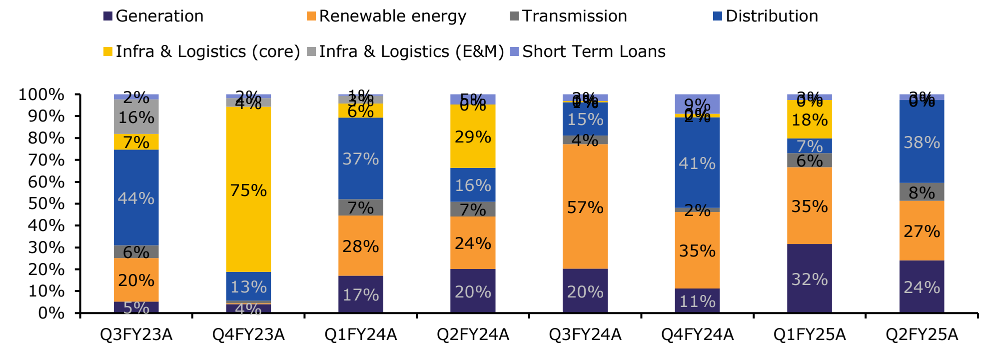
Source: Company, Emkay Research

Exhibit 81: Sanctions remain robust across the products segment



Source: Company, Emkay Research

Exhibit 82: Sanctions toward Infra and Logistics yet to ramp up

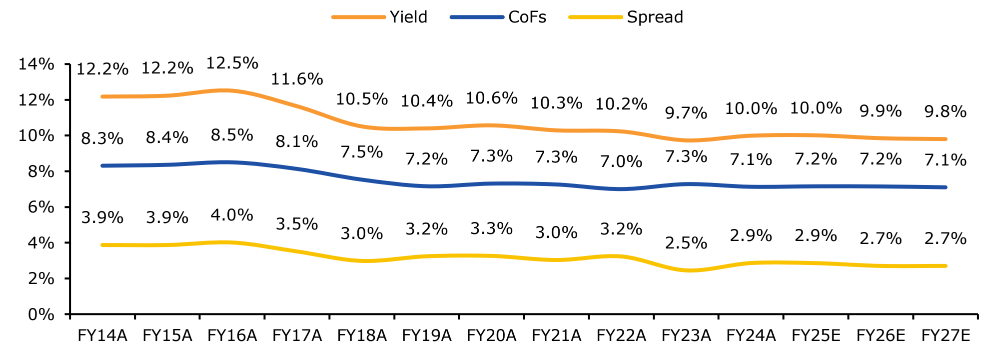


Source: Company, Emkay Research

Margins to remain broadly stable despite some pressure on yields

REC positions itself as a pivotal entity in power financing, drawing on its extensive expertise to pinpoint and support projects that offer favorable interest margins. The company's increasing emphasis on renewable energy and its expansion into infrastructure and logistics financing reflect its alignment with shifting market trends. However, new segments will typically generate lower returns compared with conventional thermal power generation, in our view, driven by heightened competition. As a result, we anticipate a moderation of ~15bps in yields over the forecast period, reflecting the impact of a changing asset mix.

Exhibit 83: Some compression in yields on account of REC entering segments with higher competition from banks



Source: Company, Emkay Research

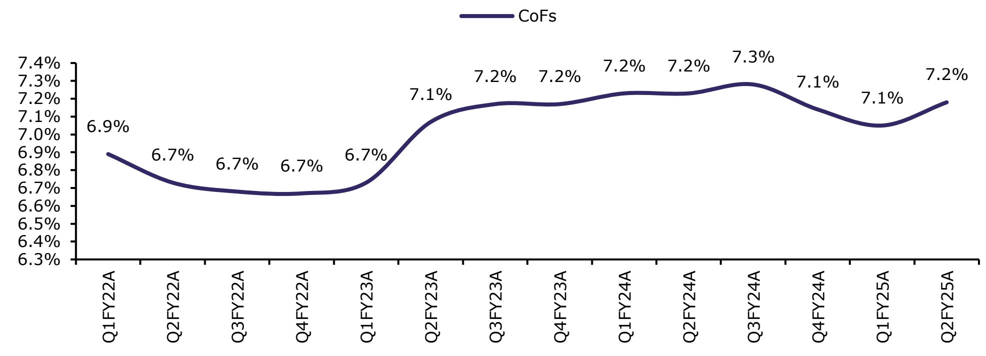
Similar to parent PFC, REC is also rated AAA by various credit rating agencies; it extensively leverages foreign currency borrowings that are 99% hedged for all such borrowings. Apart from these, REC also has the advantage of being allowed to issue 54-EC bonds (since 2006), which cost lower than other sources of borrowing. Additionally, the company employs a diversified funding mix for maintaining low borrowing costs, with ~43% sourced from domestic bonds, 24% from foreign-currency loans, ~9% from 54-EC bonds , and 15% from term loans.

Exhibit 84: Highest domestic credit rating by multiple rating agencies

Agency	CRISIL	ICRA	Indra Rating	CARE	Fitch Ratings	Moody's	Japan Credit Rating Agency
Long-Term Borrowings	AAA	AAA	AAA	AAA	-	-	-
Short-Term Borrowings	A1+	A1+	A1+	A1+	-	-	-
Domestic Perpetual Bonds	AAA			AAA	-	-	-
Foreign Borrowings	-	-	-		BBB-	Baa3	BBB+

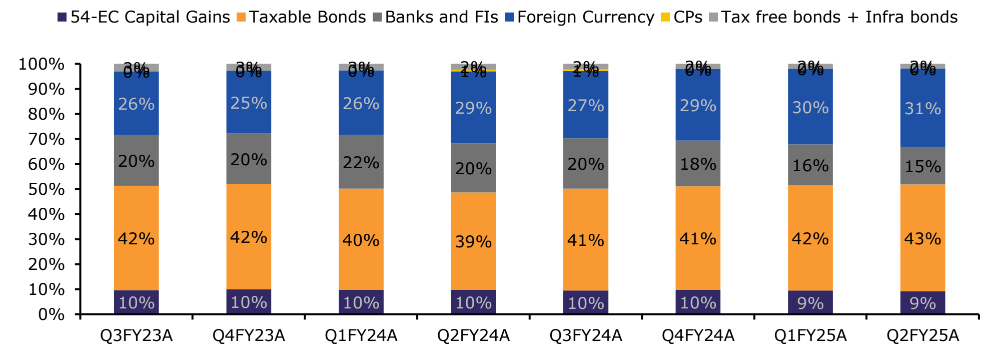
Source: Company, Emkay Research

Exhibit 85: Cost of borrowing expected to moderate, as the rate cut cycle begins



Source: Company, Emkay Research

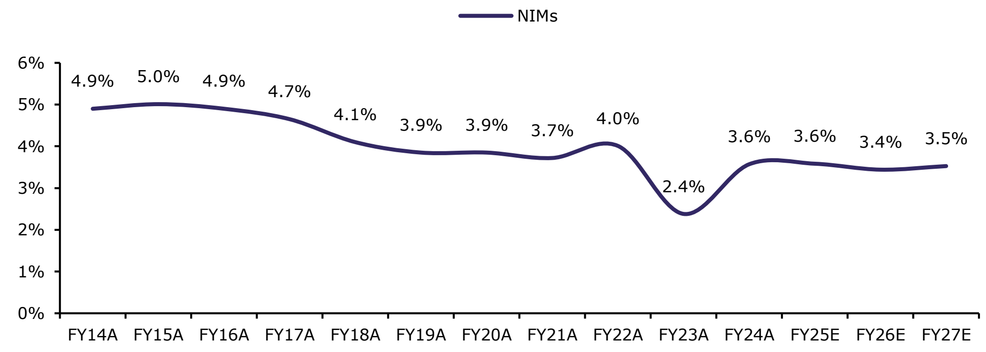
Exhibit 86: Diverse sources of funding



Source: Company, Emkay Research

We anticipate margins to stabilize at ~ 3.5%. We maintain our view that the rising share of low-yield renewable projects will be balanced by the growing contribution of higher-yielding infrastructure and logistics finance portfolios, along with repricing of the existing loan book.

Exhibit 87: Margins to be broadly stable, aided by moderating CoFs

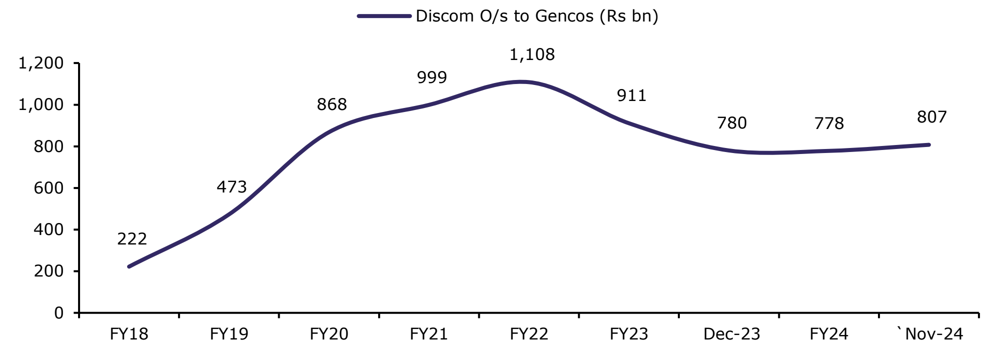


Source: Company, Emkay Research

Enhanced borrower financial health driving lower credit costs

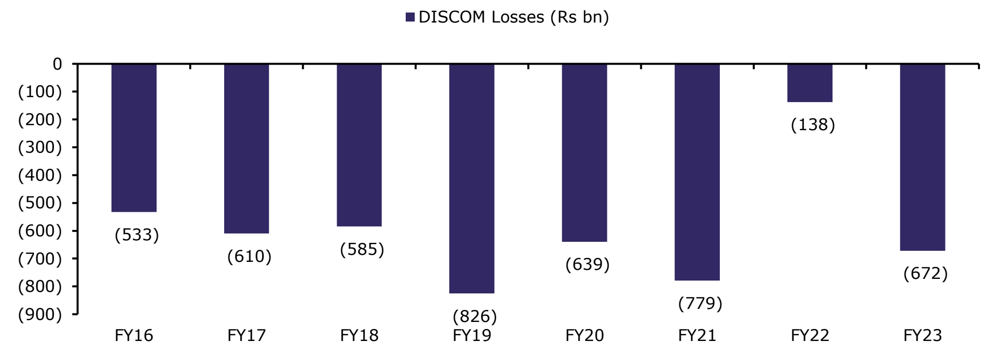
India's power sector has long faced challenges due to the weak financial health of state-owned DISCOMs, plagued by chronic cash flow issues, tariffs set below costs, and delayed state subsidies. Such issues have disrupted the supply chain, causing payment delays to transmission and generation companies, and creating systemic stress. REC, as a key player in the GoI's power sector initiatives, acts as the nodal agency for implementing various schemes under the Ministry of Power. It has significantly contributed to developing new infrastructure and strengthening existing networks. Additionally, the introduction of mandatory state-backed guarantees for loans has bolstered credit security, leading to notable improvements in DISCOMs' operational metrics and payment behavior at an aggregate level.

Exhibit 88: DISCOM dues



Source: PRAAPTI, Emkay Research

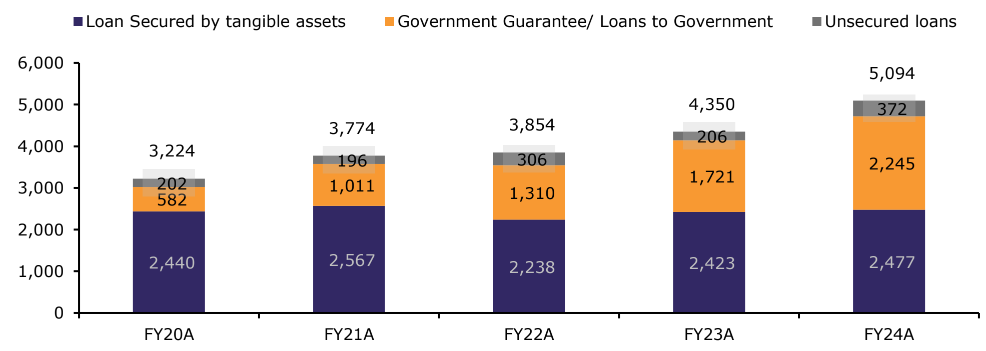
Exhibit 89: DISCOM losses



Source: Report on Performance of Power Utilities, Emkay Research

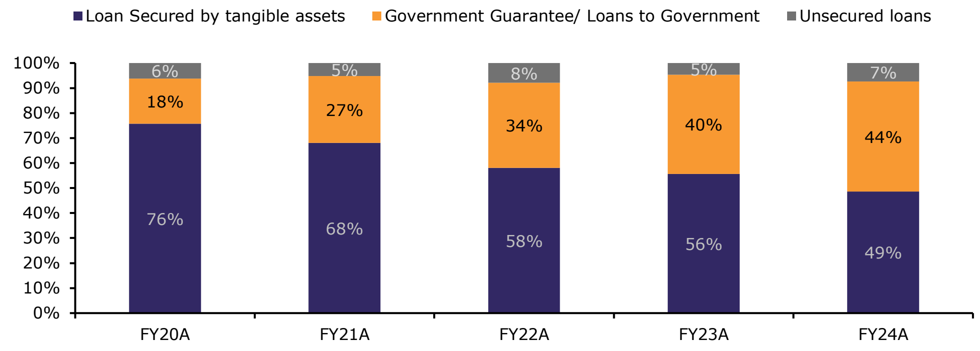
REC is reaping the benefits of resolving legacy assets, particularly thermal power projects, through the National Company Law Tribunal (NCLT) and other mechanisms. In several instances, recovery proceeds have surpassed provisioning, boosting REC's profitability. The portfolio's growing share of renewable energy projects and state-backed loans have substantially alleviated system-level stress. Additionally, stricter underwriting standards and improved coal procurement dynamics have further reduced risks, fostering a more stable operating environment.

Exhibit 90: Almost 90% of the loan assets are secured against assets or government guarantee



Source: Company, Emkay Research

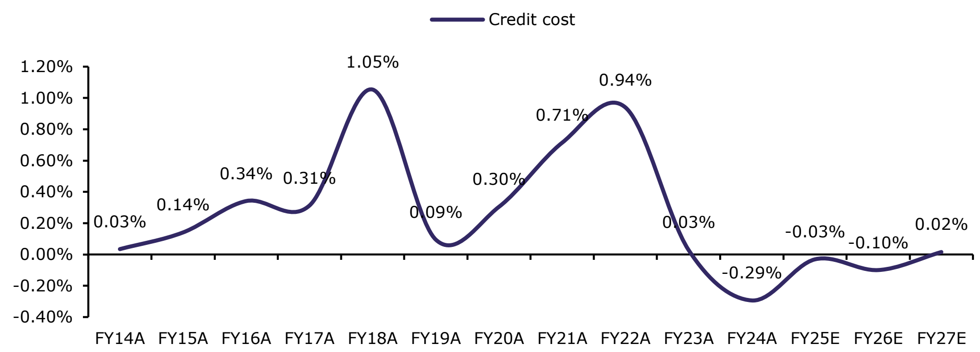
Exhibit 91: Increasing share of loan to government/loans guaranteed by the government



Source: Company, Emkay Research

We anticipate REC's credit costs to remain low, at ~5bps, driven by ongoing asset resolutions as well as accelerated recovery of stressed assets and upgradation of Stage 3 assets – all these are expected to generate write-backs over the next two years.

Exhibit 92: Credit cost expected to remain low, as we expect higher write-backs in the near term



Source: Company, Emkay Research

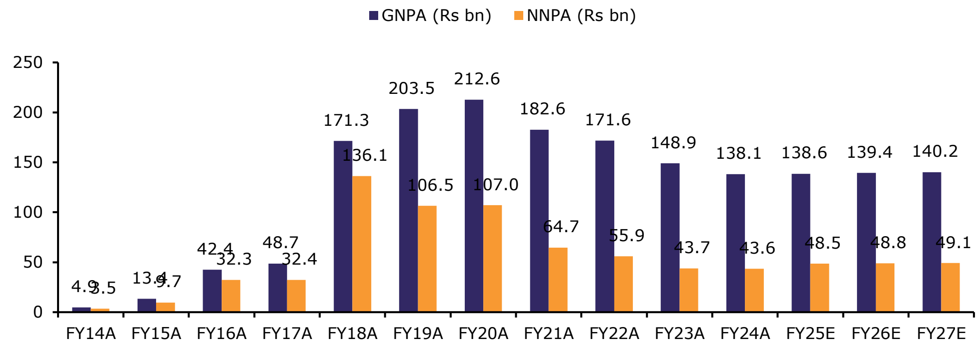
Better asset quality via legacy resolution and prudent underwriting

REC continuously works toward resolution of stressed assets through various frameworks, including RBI framework and resolution under the Insolvency and Bankruptcy Code (IBC).

REC has shown an improving trend in standard assets, with no new NPAs added since the last nine consecutive quarters, supported by strong focus on resolving bad assets and rapid progress in this direction. Over the years, power financing NBFCs have experienced significant enhancements in asset quality, as evidenced in the marked decline in gross NPAs. This improvement has been driven by key measures, including the restructuring of stressed assets, write-offs of non-performing loans, reduced slippages, higher provisioning, and a growing share of loans backed by state-government guarantees. Additionally, recent central government schemes have introduced conditions to extend guarantees for these loans, thus further bolstering asset quality.

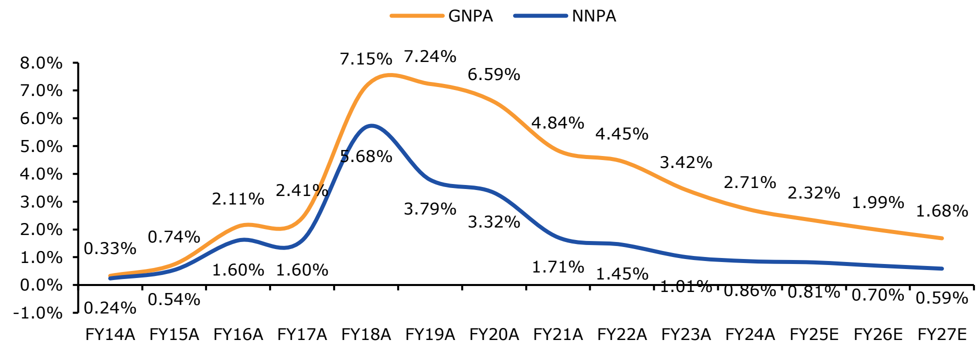
The stressed asset book has reduced by over 33% in the past five years, declining from Rs206.36bn in Sep-19 to Rs138.24bn in Sep-24, while net NPAs have dropped ~53%. The positive trend of REC's GNPA levels improving due to the resolution of legacy assets through both—the IBC route and other mechanisms—is expected to persist, supported by strong power demand driving increased project traction. Consequently, we anticipate the recognition of write-backs in the income statement during FY25 and FY26, with credit costs for REC likely remaining low.

Exhibit 93: REC has not seen any new NPA in the last 9 months



Source: Company, Emkay Research

Exhibit 94: Asset quality improvement on account of better project selection



Source: Company, Emkay Research

Exhibit 95: 60% of the total projects under resolution are in the advanced stage

Stressed assets	FY22	FY23	FY24	Q2FY25	Current status
Under NCLT					
Number of projects	**13**	**12**	**12**	**13**	
Resolution amount (Rs bn)	**119.1**	**116.3**	**122.6**	**123.0**	
KSK Mahanadi				*26.0*	*In the advanced stage of resolution; REC has recovered some amount, and reversal in provision has been for that*
Sinnar Thermal				*22.3*	*Expects recovery of ~55%, which is more than the ECL on this project. PCR on this project is ~80%*
Hiranmaye project				*13.5*	*Expects recovery of >80%. PCR of ~50%*
Lanco Amarkantak				*22.1*	*The asset has been resolved through NCLT*
Others				*39.0*	
PCR on these projects	**70**	**77%**	**71%**	**67%**	
Outside NCLT					
Number of projects	**12**	**7**	**4**	**4**	
Resolution amount (Rs bn)	**52.54**	**32.65**	**15.48**	**15.28**	
PCR on these projects	**60**	**47%**	**49%**	**50%**	

Source: Company, NCLT, Emkay Research

Improved profitability driven by stable margins, lower credit costs

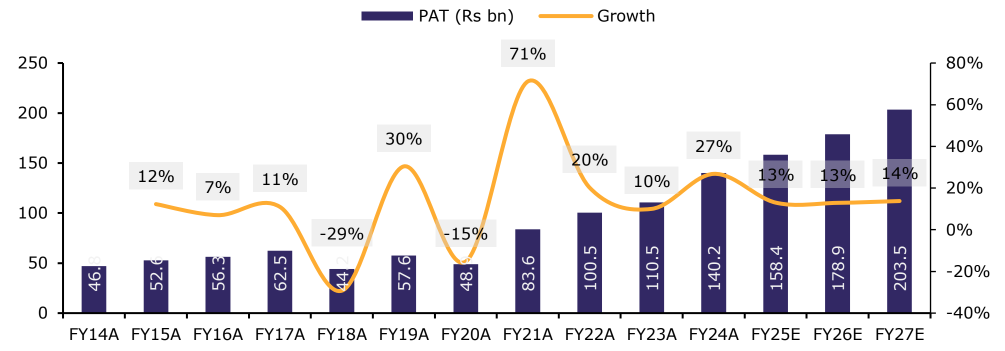
REC's business model is anchored on two core strengths – robust credit growth and strong credit quality. The management is optimistic about sustaining ~18% loan CAGR, along with a high rate of asset resolution. Asset quality is expected to be stable, with credit costs projected to stay low at ~5bps over FY25-27E which is likely to enhance profitability ratios.

The company's scalability is driven by its diversified product portfolio and increased capital expenditure aligned with GoI focus on energy transition. Further, REC's sanctioned loans are well-positioned to convert into disbursements over coming years, ensuring strong visibility for sustained loan growth. While some compression in NIM is possible, it is expected to be effectively offset by continued improvements in asset quality, thus reinforcing REC's financial resilience and growth prospects.

The power sector's positive outlook reinforces our confidence, as we anticipate no new stressed asset formation over the next two years. Further, the resolution of existing stressed projects is expected to maintain credit costs at low levels, easing provisioning requirements and boosting profitability. The potential for write-backs during this period provides additional upside to earnings.

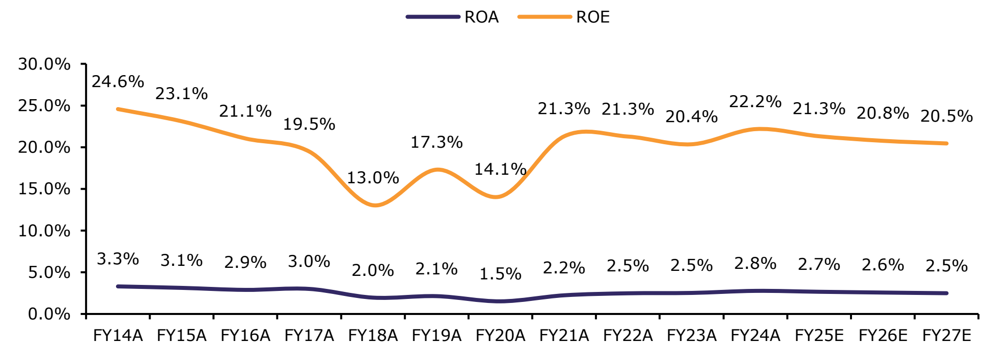
Such factors establish a robust platform for steady earnings growth. We project ~13% PAT CAGR over FY25-FY27E, driven by effective capital deployment and improving operational efficiency. By FY26E, this growth is expected to deliver RoA of ~2.5% and RoE of ~20.5%, highlighting REC's resilience and strong profitability in a competitive financial sector. This outlook reflects not only the company's solid business model, but also its ability to navigate and capitalize on evolving industry dynamics.

Exhibit 96: PAT growth to be maintained at >12% over FY24-27E



Source: Company, Emkay Research

Exhibit 97: ROA/ROE profile to remain robust, as asset quality continues to improve

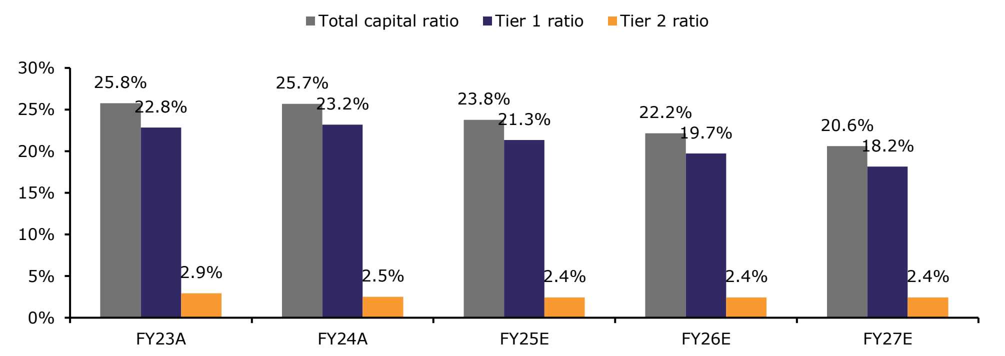


Source: Company, Emkay Research

Capital Adequacy

As of Sep-25, REC's capital adequacy ratio stands at a healthy ~25.31%. This strong position, underpinned by robust internal accruals and a loan portfolio largely secured by State guarantees with lower capital requirements, is expected to comfortably support 18% loan CAGR over the next three years.

Exhibit 98: Strong capital adequacy supporting growth



Source: Company, Emkay Research

ROE tree

Exhibit 99: DuPont Analysis

(on average assets)	FY22	FY23	FY24	FY25	FY26	FY27
Interest income	9.4%	8.8%	9.0%	9.0%	9.0%	9.1%
Interest expended	5.4%	5.4%	5.9%	5.8%	5.8%	5.8%
Net Interest Income	3.9%	3.4%	3.1%	3.2%	3.2%	3.2%
Other Income (Treasury / others) / Avg. Assets	0.2%	0.2%	0.2%	0.2%	0.2%	0.1%
Income Yield / Avg. Assets	4.2%	3.5%	3.3%	3.4%	3.4%	3.4%
Op. Cost (Other costs) / Avg Assets	0.1%	0.1%	0.1%	0.1%	0.2%	0.2%
Operating profit / Avg Assets	4.0%	3.4%	3.2%	3.3%	3.2%	3.2%
Provisions / Avg. Assets	0.9%	0.0%	-0.3%	0.0%	-0.1%	0.0%
Exceptional Item	0.1%	0.2%	-0.1%	0.0%	0.0%	0.0%
Pre-Tax	3.1%	3.1%	3.5%	3.3%	3.2%	3.1%
Tax Retention Rate	80.9%	80.5%	78.8%	79.6%	79.0%	79.0%
Post Tax	2.5%	2.5%	2.8%	2.7%	2.6%	2.5%
Leverage	8.6	8.1	8.0	8.0	8.1	8.2
ROE	21.3%	20.3%	22.2%	21.3%	20.8%	20.5%

Source: Company, Emkay Research

Valuation argument

Over the past decade (FY14-24), REC has delivered a steady performance, achieving average ROE of ~19-20% and AUM CAGR of ~13%. Despite this, the stock has historically traded at an average 1-year forward P/BV of 0.7x. This subdued valuation can be attributed to the significant provisions made during FY14-18, primarily due to stress in private-sector thermal power plants. Key challenges during that period included the absence of PPAs, inadequate coal supply, the poor financial health of DISCOMs impacting the power sector's supply chain, and the application of RBI's stressed asset circulars and retrospective restructuring norms.

As the gradual easing of incremental stress unfolded, the NBFC sector encountered a liquidity crisis sparked by the IL&FS debacle, which was exacerbated by the prolonged impact of the Covid-19 pandemic. However, the post-pandemic period marked a significant turning point for the power sector, as a cycle of power shortages emerged, positioning power-generating companies more favorably.

Sector prospects have been bolstered by transformative reforms, including the rollout of the Revamped Distribution Sector Scheme (RDSS), the Late Payment Surcharge (LPS) regulations, and Liquidity Infusion Schemes (LIS). Moreover, the improving financial stability of DISCOMs has substantially mitigated asset quality risks. The shorter development timelines of renewable energy projects, along with increasing participation from corporates with robust balance sheets, have further strengthened sector resilience. Additionally, the acquisition of legacy stressed thermal assets by private entities has opened avenues for write-backs, contributing to enhanced profitability.

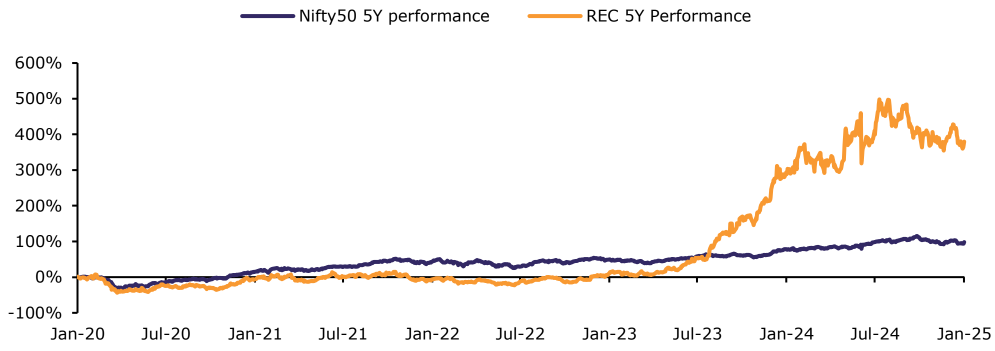
Over the past two years, REC's stock has undergone a remarkable valuation re-rating, with its P/BV increasing, from 0.5x to 1.5x (1-year forward) – significantly exceeding its 10-year average of 0.7x. This re-rating has been fueled by robust growth prospects in the current cycle, successful resolution of legacy stressed assets, and upward revisions in earnings driven by write-backs. These factors have fundamentally reshaped the market sentiment, resulting in a substantial enhancement of the stock's valuation.

Exhibit 100: Valuation matrix

REC	CMP/TP (Rs)	Upside	Mkt Cap (Rs bn)	P/BV (x)			P/E (x)			RoA			RoE			Book Value (Rs/sh)			Adj EPS (Rs)		
				FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E
At current market price	518	25.4%	1,365	1.7	1.5	1.3	8.6	7.6	6.7	2.7%	2.6%	2.5%	21.3%	20.8%	20.4%	303	351	405	60	68	77
At target price	650			2.1	1.9	1.6	10.8	9.6	8.4							303	351	405	60	68	77

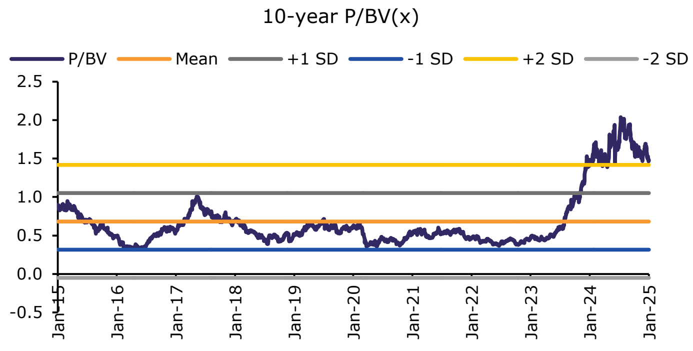
Source: Company, Emkay Research

Exhibit 101: REC has significantly outperformed the NIFTY over the last 2 years



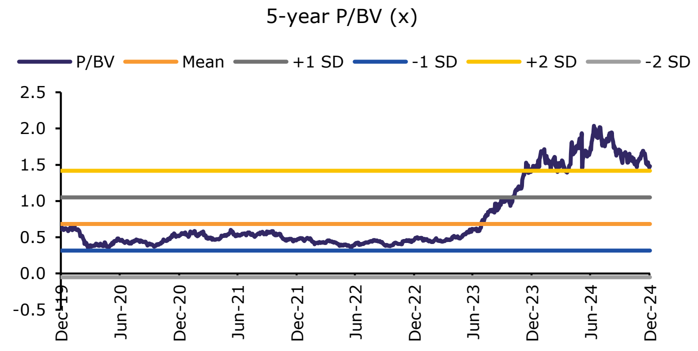
Source: Company, Emkay Research

Exhibit 102: REC – One-year forward P/BV (10 years)



Source: Company, Emkay Research

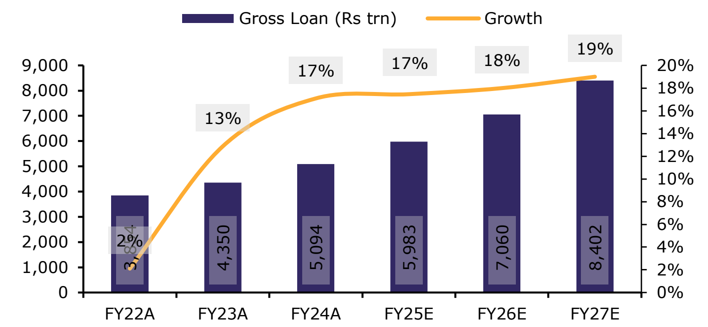
Exhibit 103: REC - One-year forward P/BV (5 years)



Source: Company, Emkay Research

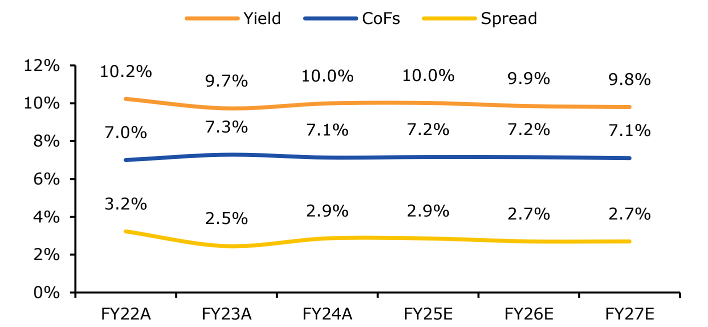
Story in charts

Exhibit 104: AUM growth supported by the RE and non-power segments



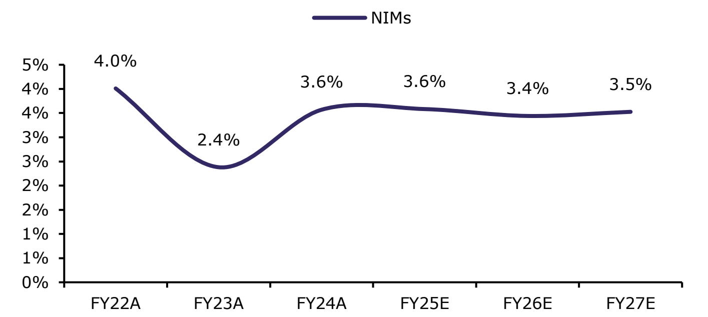
Source: Company, Emkay Research

Exhibit 105: Some compression in yields on account of REC entering segments with lower yields



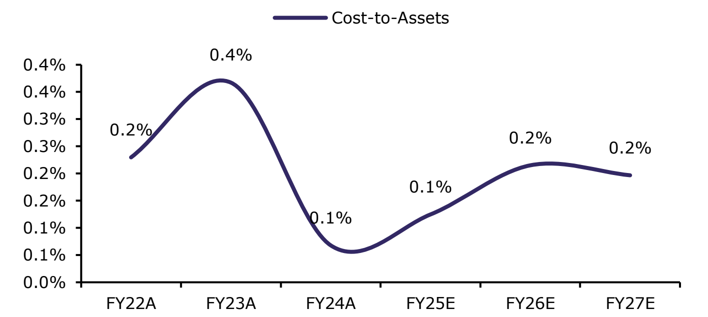
Source: Company, Emkay Research

Exhibit 106: Margins supported by moderating CoFs



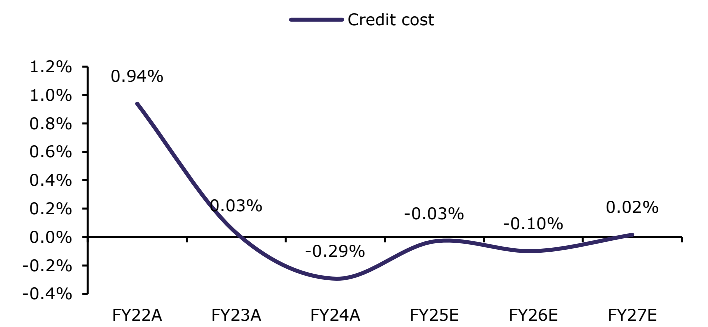
Source: Company, Emkay Research

Exhibit 107: Operating cost to remain low



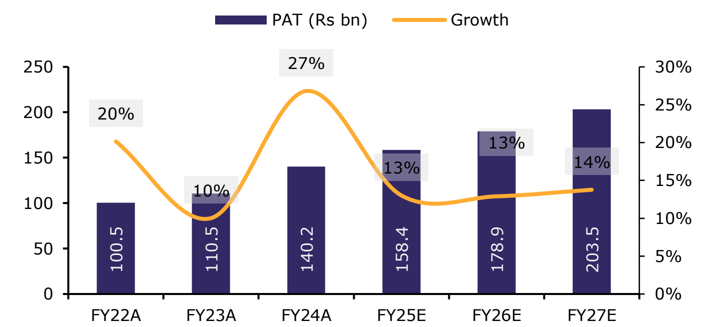
Source: Company, Emkay Research

Exhibit 108: Credit cost to be low on account of write backs



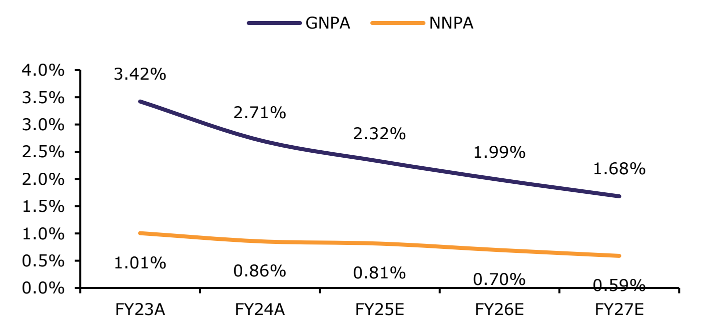
Source: Company, Emkay Research

Exhibit 109: PAT is expected to grow at ~13% over our forecast period



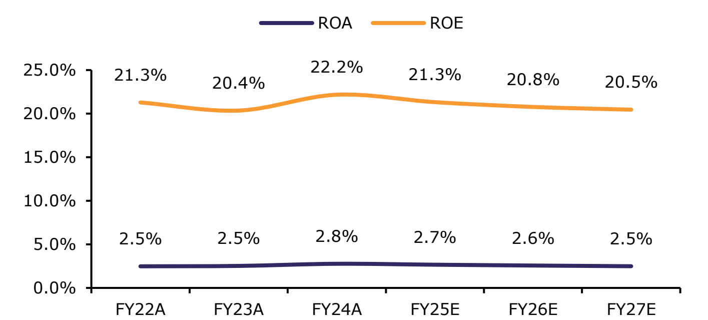
Source: Company, Emkay Research

Exhibit 110: Asset quality improves, as REC continues to lend to financially viable projects



Source: Company, Emkay Research

Exhibit 111: We believe REC will continue delivering 20% ROE



Source: Company, Emkay Research

Key Risks

- **Slower-than-expected growth:** The company's business model is highly reliant on sustaining loan growth. Any disruption, whether stemming from company-specific factors such as intensified competition from banks or broader macroeconomic challenges like asset quality deterioration, could adversely impact growth. A slowdown in loan growth is likely to compress return on equity (ROE) and lead to a de-rating of the stock
- **Asset quality issues:** A decline in asset quality, driven by macroeconomic pressures or company-specific issues, poses a significant risk. Rising NPAs and higher provisioning/increased credit costs could compress profitability, leading to EPS downgrades and a potential stock de-rating.
- **Diversification in non-power infra projects:** REC's current focus on government-backed infrastructure projects ensures low risk. However, a shift toward infrastructure and Logistics, which lack revenue lock-ins and government backing, could heighten credit risks. Limited expertise in managing private sector exposure further adds to the challenge.
- **Increasing competition leading to margin compression:** Although banks have largely refrained from lending to the power sector due to perceived lower credit risks, increased participation from them could lead to a compression in NIMs for power financiers. Additionally, the growing share of renewable energy (RE) projects (RE is a highly competitive sector with lower spreads) could put further pressure on margins.
- **Draft RBI regulations on project financing:** The RBI's draft guidelines propose stricter project financing regulations, raising the provision requirement from 0.4% to 5%, with reductions to 2.5% and 1%, respectively, as projects generate cash flow, subject to specific conditions. These changes would apply to infrastructure, non-infrastructure, and commercial real estate projects for all regulated entities. Further, financial institutions will be required to maintain a minimum exposure of 10% (5% for large projects) for projects involving consortium lending. Although we believe the likelihood of these norms being implemented is low, they still present a risk to the broader sector.

Exhibit 112: Shareholding pattern

Name	% Holding
Promoter:	
Government of India	**56.0**
Public Shareholder:	
Mutual Funds	**11.6**
Nippon India Mutual Fund	1.6
HDFC Mutual Fund	2.0
Kotak Mutual Fund	1.8
DSP Mutual Fund	1.2
Alternate Investment Funds	0.5
Banks	0.1
Insurance company	**4.5**
LIC	2.1
Provident Funds / Pension Funds	0.7
NBFCs	0.0
Foreign Portfolio Investors	**17.7**
Government of Singapore	1.1
Others	8.8
Total	**100.0**

Source: Company, Emkay Research

Exhibit 113: Key management personal

Name	Designation	Brief Profile
Vivek Kumar Dewangan	Chairman and MD	Vivek Kumar Dewangan is the Chairman & Managing Director of REC Limited. He has held this position since 17-May-2022. A 1993-batch IAS officer (Manipur cadre), he holds a BE in Electronics from NIT Bhopal and a postgraduate degree in Optoelectronics & Optical Communication from IIT Delhi. Before joining REC, he served as Additional Secretary in the Ministry of Power, GoI. Through his distinguished IAS career, he has held key positions across various sectors, including Power & Energy, Finance, Petroleum, Education, Rural Development, and District Administration. As CMD of REC and ex-officio Chairman of RECPDCL, Dewangan drives REC's strategic vision to achieve its corporate goals.
Vijay Kumar Singh	Director (Projects)	Vijay Kumar Singh has been the Director (Projects) of REC Limited since 15-Jul-2022, after previously serving as Executive Director in the company. An Electrical Engineering graduate from IIT Roorkee, he brings over 35 years of experience in the Indian power sector, including prior stints at Power Grid Corporation of India Limited and NTPC Limited. In his current role, he oversees REC's technical functions, including project appraisal, infrastructure financing, stressed asset management, and implementation of government programs. He has extensive expertise in transmission project development, procurement, and financial operations, including raising bonds and commercial papers.
Harsh Baweja	Director (Finance)	Harsh Baweja has been serving as Director (Finance) of REC Limited since 14-May-2024. A Chartered Accountant and Fellow Member of ICAI, he brings over 33 years of expertise in financial operations, including a Diploma in Information Systems Audit. Prior to his elevation, he served as Executive Director (Finance) at REC, where he successfully managed diverse financial portfolios and led financing initiatives across state and private sectors. His core competencies include financial planning, resource optimization, tax planning, and liaison with financial institutions and capital market players.
Shashank Misra	Government Nominee Director	Shashank Misra has been serving as the Government Nominee Director on the Board of REC Limited since 21-Aug-2023. An IAS officer of the 2007 batch (Madhya Pradesh cadre), he holds a BTech in Electrical Engineering from IIT Delhi and is currently posted as Joint Secretary in the Ministry of Power, Government of India. Prior to this, he served in the Department of Revenue, Ministry of Finance, and held key leadership roles in Madhya Pradesh, including MD of infrastructure corporations and Chairman of Ujjain Smart City Limited. Misra brings extensive experience in infrastructure development, asset management, and policy implementation to REC's Board.
Manoj Sharma	Nominee Director – Power Finance Corporation Limited.	Manoj Sharma has been serving as the Nominee Director of Power Finance Corporation Limited (PFC) on the Board of REC Limited since 11-Jul-2023. A Chartered Accountant and Law graduate (LLB), he is currently the Director (Commercial) at PFC and brings over 32 years of experience in the power sector. Throughout his career at PFC, he has managed diverse areas such as entity appraisal, financial analysis, resource mobilization, debt syndication, and resolution of stressed assets. He has played a key role in shaping lending policies, monitoring loan assets, and ensuring compliance with regulatory frameworks. Sharma also serves as Chairman of PFC Projects Limited, contributing significantly to resolution mechanisms and financial reforms within the power sector.

Source: Company, Emkay Research

REC Ltd : Standalone Financials and Valuations

Profit & Loss

Y/E Mar (Rs mn)	FY23	FY24	FY25E	FY26E	FY27E
Interest Income	385,140	456,580	537,317	629,028	744,025
Interest Expense	237,480	299,740	345,458	405,238	478,398
Net interest income	**147,660**	**156,840**	**191,860**	**223,791**	**265,627**
NII growth (%)	(7.1)	6.2	22.3	16.6	18.7
Non interest income	6,940	10,810	12,890	11,218	9,260
Total income	**154,600**	**167,650**	**204,750**	**235,009**	**274,887**
Operating expenses	5,360	6,510	7,690	12,515	16,384
PPOP	**149,240**	**161,140**	**197,060**	**222,494**	**258,503**
PPOP growth (%)	(8.7)	8.0	22.3	12.9	16.2
Provisions & contingencies	1,140	(13,580)	(1,691)	(6,386)	1,174
PBT	**148,100**	**174,720**	**198,751**	**228,880**	**257,329**
Extraordinary items	10,710	(3,070)	(270)	2,457	(294)
Tax expense	26,850	37,610	40,592	47,549	54,101
Minority interest	0	0	0	0	0
Income from JV/Associates	0	0	0	0	0
Reported PAT	**121,250**	**137,110**	**158,159**	**181,331**	**203,228**
PAT growth (%)	15.5	13.1	15.4	14.7	12.1
Adjusted PAT	**110,540**	**140,180**	**158,429**	**178,875**	**203,523**
Diluted EPS (Rs)	**42.3**	**53.2**	**60.2**	**67.9**	**77.3**
Diluted EPS growth (%)	0.4	25.7	13.0	12.9	13.8
DPS (Rs)	**12.6**	**16.0**	**18.1**	**20.4**	**23.2**
Dividend payout (%)	**29.8**	**30.1**	**30.0**	**30.0**	**30.0**
Effective tax rate (%)	18.1	21.5	20.4	20.8	21.0
Net interest margins (%)	2.4	3.6	3.6	3.4	3.5
Cost-income ratio (%)	3.5	3.9	3.8	5.3	6.0
PAT/PPOP (%)	74.1	87.0	80.4	80.4	78.7
Shares outstanding (mn)	2,633.0	2,633.0	2,633.0	2,633.0	2,633.0

Source: Company, Emkay Research

Balance Sheet

Y/E Mar (Rs mn)	FY23	FY24	FY25E	FY26E	FY27E
Share capital	26,330	26,330	26,330	26,330	26,330
Reserves & surplus	550,470	661,500	772,400	897,613	1,040,078
Net worth	**576,800**	**687,830**	**798,730**	**923,943**	**1,066,408**
Borrowings	**3,746,160**	**4,379,440**	**5,213,214**	**6,151,592**	**7,320,395**
Other liabilities & prov.	**325,810**	**407,130**	**413,959**	**427,660**	**469,100**
Total liabilities & equity	**4,648,770**	**5,474,400**	**6,425,903**	**7,503,195**	**8,855,903**
Net loans	4,244,920	4,999,170	5,874,025	6,931,349	8,248,306
Investments	31,380	53,200	70,591	76,410	82,709
Cash, other balances	19,870	24,990	44,981	37,516	44,280
Interest earning assets	**4,296,170**	**5,077,360**	**5,989,597**	**7,045,275**	**8,375,294**
Fixed assets	6,430	6,550	6,767	6,904	7,043
Other assets	346,170	390,490	429,539	451,016	473,567
Total assets	**4,648,770**	**5,474,400**	**6,425,903**	**7,503,195**	**8,855,903**
BVPS (Rs)	219.1	261.2	303.4	350.9	405.0
Adj. BVPS (INR)	219.1	261.2	303.4	350.9	405.0
Gross loans	4,350,120	5,093,710	5,983,256	7,060,242	8,401,688
Total AUM	**4,350,120**	**5,093,710**	**5,983,256**	**7,060,242**	**8,401,688**
On balance sheet	4,350,120	5,093,710	5,983,256	7,060,242	8,401,688
Off balance sheet	0	0	0	0	0
Disbursements	0	0	0	0	0
Disbursements growth (%)	0.0	0.0	0.0	0.0	0.0
Loan growth (%)	13.6	17.8	17.5	18.0	19.0
AUM growth (%)	12.9	17.1	17.5	18.0	19.0
Borrowings growth (%)	14.6	16.9	19.0	18.0	19.0
Book value growth (%)	8.8	19.2	16.1	15.7	15.4

Source: Company, Emkay Research

Asset quality and other metrics

Y/E Mar (Rs mn)	FY23	FY24	FY25E	FY26E	FY27E
Asset quality					
GNPL - Stage 3	171,600	148,920	138,100	138,640	139,440
NNPL - Stage 3	43,720	43,560	48,524	48,804	49,084
GNPL ratio - Stage 3 (%)	3.4	2.7	2.3	2.0	1.7
NNPL ratio - Stage 3 (%)	1.0	0.9	0.8	0.7	0.6
ECL coverage - Stage 3 (%)	74.5	70.7	64.9	64.8	64.8
ECL coverage - 1 & 2 (%)	0.0	0.0	0.0	0.0	0.0
Gross slippage - Stage 3	0	0	0	0	0
Gross slippage ratio (%)	0.0	0.0	0.0	0.0	0.0
Write-off ratio (%)	0.0	0.0	0.0	0.0	0.0
Total credit costs (%)	0.0	(0.3)	0.0	(0.1)	0.0
NNPA to networth (%)	7.6	6.3	6.1	5.3	4.6
Capital adequacy					
Total CAR (%)	25.8	25.7	24.5	22.9	21.4
Tier-1 (%)	22.8	23.2	22.1	20.5	19.0
Miscellaneous					
Total income growth (%)	(8.1)	8.4	22.1	14.8	17.0
Opex growth (%)	11.9	21.5	18.1	62.7	30.9
PPOP margin (%)	3.6	3.4	3.6	3.4	3.3
Credit costs-to-PPOP (%)	0.8	(8.4)	(0.9)	(2.9)	0.5
Loan-to-Assets (%)	91.3	91.3	91.4	92.4	93.1
Yield on loans (%)	9.7	10.0	10.0	9.9	9.8
Cost of funds (%)	7.3	7.1	7.2	7.2	7.1
Spread (%)	2.5	2.9	2.9	2.7	2.7

Source: Company, Emkay Research

Valuations and key Ratios

Y/E Mar	FY23	FY24	FY25E	FY26E	FY27E
P/E (x)	12.2	9.7	8.6	7.6	6.7
P/B (x)	2.4	2.0	1.7	1.5	1.3
P/ABV (x)	2.4	2.0	1.7	1.5	1.3
P/PPOP (x)	9.1	8.5	6.9	6.1	5.3
Dividend yield (%)	2.4	3.1	3.5	3.9	4.5
Dupont-RoE split (%)					
NII/avg AUM	3.6	3.3	3.5	3.4	3.4
Other income	0.2	0.2	0.2	0.2	0.1
Securitization income	0.0	0.0	0.0	0.0	0.0
Opex	0.1	0.1	0.1	0.2	0.2
Employee expense	0.0	0.0	0.0	0.0	0.0
PPOP	**3.6**	**3.4**	**3.6**	**3.4**	**3.3**
Provisions	0.0	(0.3)	0.0	(0.1)	0.0
Tax expense	3.6	3.7	3.6	3.5	3.3
RoAUM (%)	**3.0**	**2.9**	**2.9**	**2.8**	**2.6**
Leverage ratio (x)	7.5	7.5	7.5	7.6	7.8
RoE (%)	**20.4**	**22.2**	**21.3**	**20.8**	**20.5**

Quarterly data

Rs mn, Y/E Mar	Q2FY24	Q3FY24	Q4FY24	Q1FY25	Q2FY25
NII	38,560	41,530	42,630	44,740	46,800
NIM(%)	3.5	3.6	3.6	3.6	3.7
PPOP	40,240	41,620	43,590	45,730	49,400
PAT	37,730	32,690	40,160	34,420	40,410
EPS (Rs)	14.33	12.42	15.25	13.07	15.35

Source: Company, Emkay Research

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