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Tata Power, BSES May Gain, Helped by Utilities Law

Tata Power Ltd. and BSES Ltd., India's biggest publicly traded power companies, are counting on a new law to help deliver profit as they spend more than $270 million to upgrade electricity networks in New Delhi.

Shares of the two companies have doubled since the law was passed in May, lending support to their plans in the nation's capital. One-third of electricity users in New Delhi, a city of 14 million people, ignore bills or illegally tap cables. By reducing such abuses and opening a path for investment, the law aims to attract the money India needs to double capacity by 2013 and end power cuts. "More and more States will privatize distribution as they start implementing the electricity bill, and that opens up lots of opportunities" for the two companies, said N. Prasad, who holds Tata Power shares among $500 million of assets he helps manage at Sundaram Newton Asset Management Co. in Mumbai.

India, a nation of 1 billion people, is trying to accelerate power investment to boost economic growth, forecast by the government to exceed 7 percent in the year to March 31. The country needs to spend $800 billion on its energy industry by 2030, the Paris-based International Energy Agency said in November.

Tata Power and the Reliance Group's BSES, are among the companies best placed to profit after India's previous attempts to attract capital failed. As many as 10 overseas utilities, including AES Corp. and Goldman Sachs Group Inc.'s Cogentrix Energy Inc. have quit the country in recent years, citing red tape and contract disputes.

Little Competition

That's left Tata Power and BSES facing little competition except each other. Both are based in Mumbai, India's commercial capital; by adding New Delhi, they now serve a combined 10 million consumers.

Shares in Tata Power have surged 131 percent since May 1 and BSES is up 112 percent, outpacing a 79 percent climb in the benchmark Mumbai Sensex 30 Index.

Tata Power closed at 276.85 rupees today, up 0.8 percent, or 2.05 rupees. BSES ended at 471.65 rupees, up 1.4 percent, or 6.3 rupees.

The law that India's parliament passed in May enables utilities to sell power directly to consumers, instead of marketing it to distribution boards run by state governments. That will prompt states to follow Delhi in selling electricity grids to private companies, raising some of the $8.5 billion the power boards owe to government-owned generators, Sundaram's Prasad said.

Theft, Leakage

Those debts arose because thefts and leaks of power through dilapidated lines and equipment, plus subsidies for farmers, made the electricity business unprofitable. New Delhi last year became the first Indian state to sell distribution networks. Tata Power bought one network for $40 million and BSES paid $60 million for two more, enabling the companies to expand beyond Mumbai, where demand from large customers such as the railways, offices and ports is slowing.

"Delhi is a classic example of what these companies can do to refurbish networks and streamline bill collection systems," said Srinivas Rao, an analyst at Motilal Oswal Securities Ltd. In Mumbai who has a "buy" rating on both stocks.

Part of the $273 million the companies plan to spend in the capital over the next five years will be used to replace aging transmission lines that contribute to frequent power cuts. Tata Power and BSES are aiming for a 17 percent cut in the five-year period in the $870 million they lose annually through leaks and unauthorized tapping of lines.

Meters

The May legislation aims to reduce theft by requiring all customers to have meters. Tata Power, added last month to the Sensex 30 Index, is part of the Tata Group, whose 80 companies span steelmaking to information technology. BSES is controlled by Reliance Industries Ltd., India's biggest non-state company, which produces oil, gas, petrochemicals, and synthetic fibers.

The companies' market values — $1.2 billion for Tata Power, $1.4 billion for BSES — are each more than double the combined $513 million valuation of their four publicly traded competitors, Ahmedabad Electricity Co., CESC Ltd., Gujarat Industries Power Co. and Surat Electricity Co.

"The field is wide open for Tata and BSES," said K.K. Mital, who manages $22 million of stocks, including 70,000 Tata Power shares at New Delhi-based Escorts Asset Management Ltd. "Both are backed by powerful business groups that know how to navigate through the country's power business.''

Drawing Power

Investors are divided on whether the law change will draw overseas power companies back to India. **"Any major company that had an interest in India's power sector got both their hands bitten off," said Jon Thorn, a Hong Kong-based asset manager with India Capital Fund Ltd., which oversees $50 million of Indian stocks.** AES, which produces power in 30 countries, and other overseas utilities such as Cogentrix quit India amid complaints about bureaucratic delays and financial disputes.

In 2001, Enron Corp., then the world's biggest power company, shut a $3 billion power plant at Dabhol, near Mumbai, after its only customer, the Maharashtra State Electricity Board, refused to pay for electricity it claimed was too expensive. Enron later collapsed in an unrelated accounting scandal.

Bechtel Group, General Electric Co., Citigroup Inc. and Credit Suisse Group are among companies still involved in legal actions over the Dabhol case.

Return Expected

Still, the scale of the challenge of modernizing India's power supply, plus possible political resistance to change, may cool investors' enthusiasm for shares of Tata Power and BSES, say fund managers such as Paras Adenwala.

"The benefits of the new electricity bill will flow over time and not immediately," said Adenwala, who oversees the equivalent of $1.9 billion at Birla Sun Life Asset Management Co. in Mumbai and holds Tata Power and BSES in his index fund. "I'd be cautious about buying them at these levels.''

Equipment Makers

For both Tata Power and BSES, keeping prices low is key to capturing more of India's $42 billion electricity market. Energy bills in India eat up 10 percent of consumers' income, compared with 5 percent in China and 0.25 percent in the U.S.

The power law will help BSES cut costs in Mumbai, the company says. Previously, it had to buy 600 megawatts of electricity from Tata Power to meet a shortfall. Now BSES says it has offers of three times that amount from more than 50 producers that will supply power at lower cost through the national grid.

"Reliance is known for its aggressive cost-cutting and focus on efficiency," Motilal's Rao said. "They've brought that quality to BSES."

BSES will also capitalize on its Reliance links by building a 3,000-megawatt gas-fired generating plant on India's east coast, close to where Reliance last year discovered an estimated 14.5 trillion cubic feet of gas, the world's biggest find of 2002.
Rao says the future is bright for both BSES and Tata Power. "Delhi's experiment will prompt other states to follow suit, opening up huge opportunities."

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