

Sterlite Power: Understanding the Business Model & Demerger

September 2024



(A) Overview

Sterlite Power is one of India's leading private sector companies specializing in power transmission infrastructure and solutions. The company's business model revolves around developing, building, and operating transmission systems that are crucial for the reliable distribution of electricity across various regions. Sterlite Power is also engaged in manufacturing products for power transmission and providing innovative solutions to enhance grid efficiency. The company's business is primarily divided into three core segments:

- **Transmission Business**
- **Products Business**
- **Solutions Business**

(1) Transmission Business

The transmission segment is the backbone of Sterlite Power's operations. This segment focuses on the development and operation of high-capacity power transmission lines and related infrastructure.

Business Model: Sterlite Power participates in competitive bidding for transmission projects, primarily through the Tariff-Based Competitive Bidding (TBCB) process. Upon winning a project, the company designs, builds, operates, and maintains transmission lines and substations, ensuring that electricity generated at power plants reaches distribution companies and end consumers efficiently.

Revenue Generation: The revenue in this segment primarily comes from the long-term transmission service agreements (TSA) with distribution companies (DISCOMs) or utilities. These agreements provide Sterlite Power with stable and predictable cash flows over the project life, often spanning 25-35 years.



(2) Products Business

This segment involves the manufacturing and supply of key components used in power transmission infrastructure.

Business Model: Sterlite Power manufactures a range of products, including power conductors, optical ground wire (OPGW), and high-performance cables. These products are essential for building and upgrading transmission networks. The company sells these products to utilities, independent power producers (IPPs), and other infrastructure developers.

Revenue Generation: The revenue is generated through the sale of these products, both in the domestic and international markets. The products are often customized to meet the specific needs of different transmission projects, adding value to the overall business proposition.



(3) Solutions Business

The solutions business focuses on providing end-to-end solutions for enhancing the efficiency and reliability of power grids.

Business Model: This segment offers a range of solutions, including grid optimization, asset management, and innovative technologies for improving the efficiency of power transmission and distribution systems. Sterlite Power uses advanced technologies such as AI, IoT, and machine learning to provide solutions that help utilities reduce transmission losses, manage grid stability, and enhance operational efficiency.

Revenue Generation: The revenue comes from contracts with utilities and other power infrastructure companies for providing these specialized solutions. The solutions often involve long-term service agreements, adding to the recurring revenue stream.

(B) Strategic Initiatives and Growth Areas

Renewable Energy Focus: Sterlite Power is increasingly focusing on projects that support the integration of renewable energy into the grid. This includes the development of transmission lines that connect renewable energy sources like wind and solar farms to the main grid.

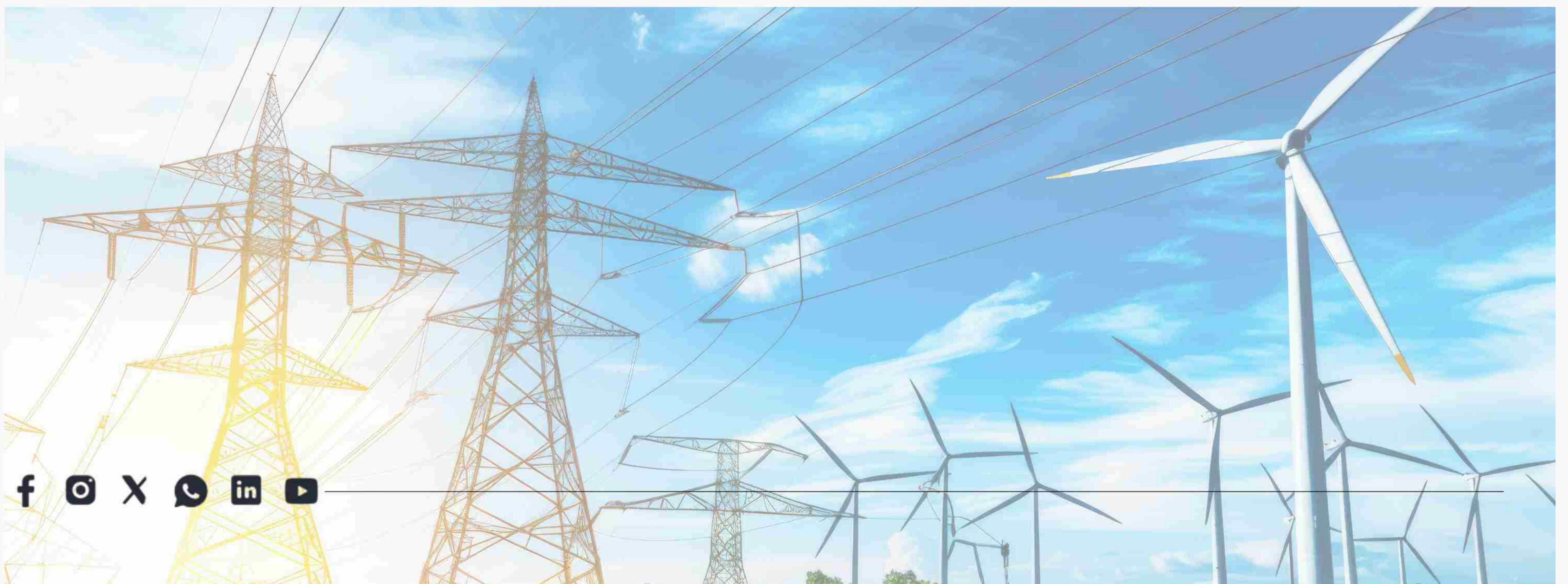
Partnerships and Joint Ventures: The company has entered into strategic partnerships, such as the joint venture with GIC, to expand its transmission business and secure more projects. These partnerships allow Sterlite Power to leverage additional financial and operational resources, enhancing its market position.

Global Expansion: Sterlite Power is exploring opportunities in international markets, particularly in regions where there is a high demand for new transmission infrastructure. This global outlook is critical for diversifying its revenue base and mitigating market-specific risks.

(C) Addressing Challenges in the Power Sector

India's power sector is undergoing significant changes, with a growing emphasis on improving customer service and enhancing the financial health of the distribution sector. Sterlite Power recognizes the importance of addressing these challenges to ensure the sustainable growth of the sector. The company is committed to speeding up the construction of transmission lines to meet the increasing demand for power and to support the government's aggressive buildout of renewable energy projects.

However, challenges such as the lack of large-scale storage solutions at an affordable cost and the need for fundamental distribution reforms remain. Sterlite Power is actively working to overcome these challenges by implementing innovative technologies and collaborating with key stakeholders to drive the sector forward.



(D) Sterlite Power Demerger of Transmission and Product Business and IPO Plans

This move is designed to allow the company to focus more intently on decarbonization and renewable energy—a critical priority in today's global energy landscape. The demerger is expected to create distinct value for shareholders by allowing them to invest in specific segments of the business that align with their investment preferences.

The Demerger Strategy

The decision to demerge the global products and services business from the core transmission assets is rooted in Sterlite Power's vision to become a leader in the renewable energy sector. By separating these businesses, Sterlite Power will unlock value by catering to distinct investor profiles—those interested in the high-growth potential of manufacturing and services versus those seeking the stable, long-term returns associated with infrastructure investments.

After Demerger the Global Products and Service Business IPO will hit the market. And, Transmission business in which GIC is putting money will remain unlisted.

The global products and services business, which boasts a order book of INR 6,000 to 7,000 crores, will now operate independently, allowing Sterlite Power to focus its resources and expertise on its core transmission and renewable energy initiatives. This move is anticipated to not only sharpen the company's operational focus but also provide clarity to investors, thereby enhancing overall shareholder value.

Demerger process on track for closure; NCLT's final order on demerger will be made effective in Sept. '24. The Infra business will get demerged into the entity SGL-5 which shall have mirror shareholding as that of demerged SPTL.

Partnership with GIC: Expanding Transmission Capabilities

Sterlite Power's strategy includes a significant partnership with GIC, a prominent global sovereign wealth fund, to form a \$4 billion joint venture dedicated to transmission projects in India. This partnership is expected to enhance Sterlite Power's market share in the transmission sector, which currently stands at approximately 20-25%. The collaboration will leverage GIC's financial strength and Sterlite Power's deep expertise in the sector, aiming to capture more projects and expand the company's footprint in the market.

The dedicated management team, with over 15 years of experience, will focus on identifying, bidding for, and executing complex transmission projects. This partnership is poised to position Sterlite Power as a leader in the rapidly evolving Indian power sector, particularly in the Greenfield transmission market.

(E) Future Outlook

The Order book of the company as on (Mar. 31st '24) is as follows:

Business Units	In ₹ Cr
Conductors + OPGW	4,748
Power Cables	1,130
MSI	827
Infra	5,456
Total	12,151

Overall Order Book of GPS business is INR 6750 Cr and Infra Business is INR 5456 Cr.

(1) GPS Co – Demerged SPTL

- India conductor market demand in FY26 is expected to be double of FY23; Select segments of Power cable market such as EHV and Solar are growing at a CAGR of 15 – 25%
- To address growing demand, capex of Rs 450Crs is underway towards increasing Conductor capacity by 45% to 1,55,000 MT and foray into Solar and EHV cables segments with sizeable capacity, which will enable
 - ✓ 30% Revenue growth upto FY26, with PAT growth of 62%
 - ✓ Est. avg. ROCE of 33% and avg. ROE of 26% upto FY26, in line with 3yrs historical avg of top peers Apar Industries (ROCE – 34%, ROE – 21%) and KEI (ROCE – 23%, ROE – 18%)
- Convergence business: Has a track record of annual Free cash generation runrate of Rs 100 – 125 Crs which is likely to sustain over next 3 years

(2) SGL5 – Infra Co

- ✓ In FY26, EBIDTA and PAT is estimated to be Rs 943 Crs and Rs 737 Crs respectively owing to EPC margins and CIL claims conversion, leading to a ROCE of 37% and ROE of 29%
- ✓ \$12Bn worth TBCB Transmission Project bids expected by CY2025 of which SGL-32 targets to acquire upto ~18% of the upcoming TBCB Projects at higher than avg. market Equity Returns

(F) Financials

Parameter	Demerged SPTL – GPS Co (consol.)			Infra Business - India		
	FY24	FY23	Growth (Y-o-Y)	FY24	FY23	Growth (Y-o-Y)
Total Income	4,842	3,292	47.1%	1,630	850	94.1%
EBIDTA	522	411	27.0%	112	324	(65.4%)
EBIDTA Margin	10.7%	12.4%		7%	38%	
PAT	241	184	30.9%	(259)	(76)	(240.7%)
Net Margin	4.9%	5.5%		(15.8%)	(8.9%)	

- **Demerged SPTL (GPS Co consol.)** comprises of GPS business and Convergence business. Riding on strong operational performance based on the highest ever sales volumes, the business achieved a high ROCE of 43% and ROE of 66%. It closed FY24 with no long-term debt and optimal working capital debt.
- **Infra business – India** comprises of Transmission Infra SPVs and captive EPC business. The FY24 Revenue was higher than FY23; EBIDTA was lower than FY23 due to higher COGS (owing to slower project progress wherein EPC costs have got booked while corresponding EPC revenue booking has got deferred into FY25) and deferment of Change in Law (CIL) claims of Rs 516 Crs. The impact of the same has got cascaded to PAT as well
- **Infra business – Brazil:** Revenue – Rs 1,545 Crs, EBIDTA – Rs 66 Crs, PAT – (370) Crs; Revenue and EBIDTA was lower as compared to FY23 primarily due to slower network execution; PAT loss resulted from higher Finance cost (~50% higher than FY23). The company is undertaking a strategic review of this business to decide on the future course.
- The long-term & short-term borrowings was Rs 6,739 Crs, which was Rs 5,168 Crs at end of FY23; Borrowings increased by INR 1,571 Cr. primarily due to increase in debt of Brazil Infra business

(G) Valuation of Sterlite Power

Currently, in the unlisted market, it is available at INR 785 price and with ~12 crores shares, the Mcap is close to ₹9500 Cr.

After the demerger, there will be two businesses. One is Transmission Lines and other is Global Product System. Transmission line will remain unlisted. And Global Products and Service Business will be listed.

In FY24, the company has generated revenue of ₹4,842 crore from its Global Products and Service Business, with an EBITDA of 522 Cr and PAT of ₹241 crore. The nearest competitor, APAR Industries, is trading at a P/E multiple of 50x for FY25 (E), although it also has a transformer oil business. Even if we apply a more conservative 35x P/E multiple, the IPO of Sterlite Power Global Products and Service Business could potentially be valued at over ₹8,000 crore.

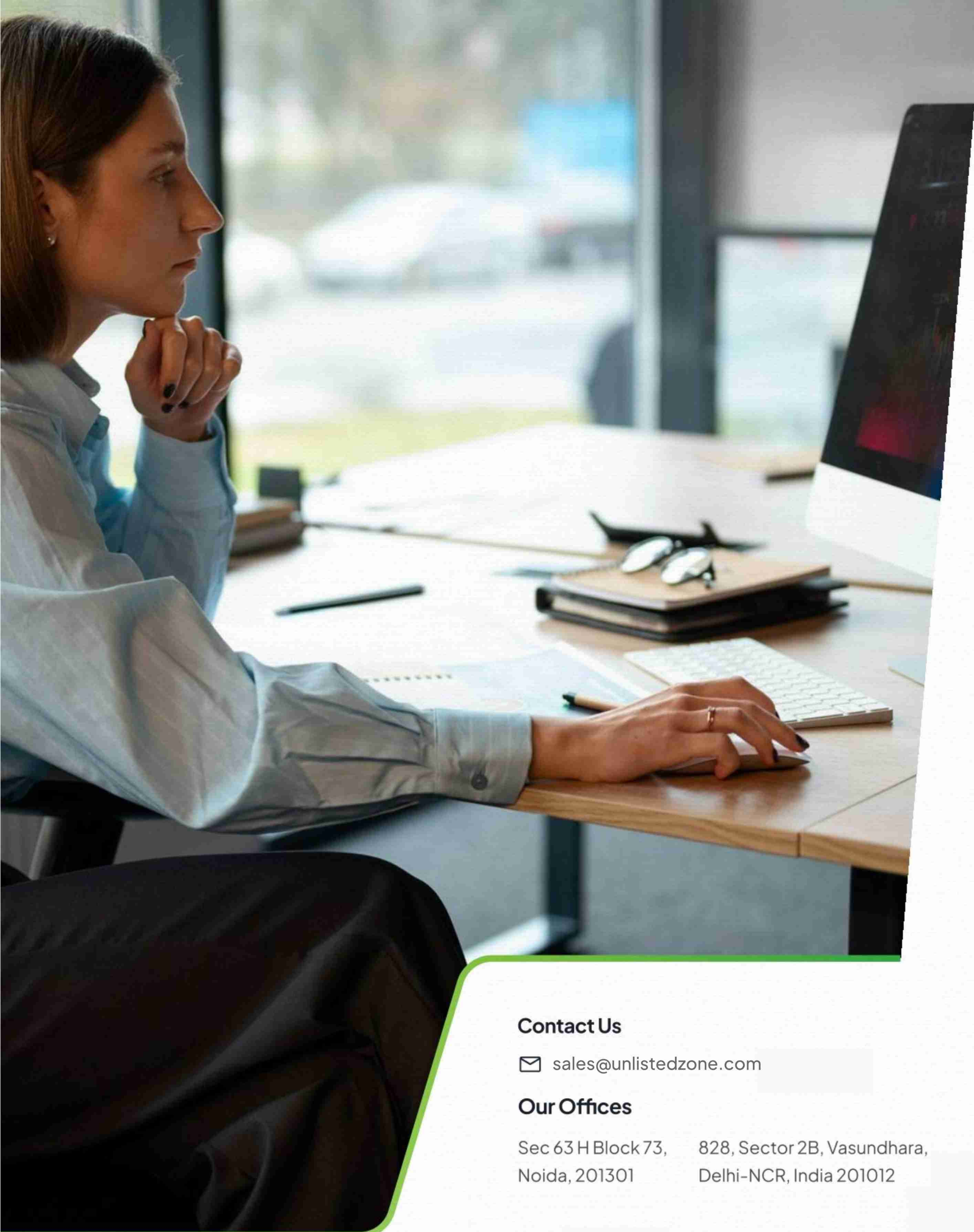
Additionally, the company's Transmission Lines business, in which GIC is investing, is estimated to be worth approximately ₹8,000 crore. This brings the overall valuation of both businesses to above ₹16,000 crore. Currently, the company's valuation stands at around ₹9,500 crore, indicating significant upside potential.

(H) Market Outlook

In FY24 year to date, 22 Tariff-Based Competitive Bidding (TBCB) bids worth ₹43,314 crore have been completed, and Requests for Proposals (RFPs) have been released for an additional 23 TBCB bids worth approximately ₹88,153 crore. Further, 6 bids worth ₹18,914 crore have been approved, and RFP issuance is awaited.

The addressable global market of power conductors for the company in FY24 is 1.35 million metric tons (MT) and is slated to grow at 5-6% over the next 4 years. The India power conductor market volume is expected to grow from the current volume size of 1.5 lakh MT to approximately 2.6 lakh MT in the next 4 years.

The addressable global Power Cable market size is USD 6.7 billion and is expected to grow at a blended CAGR of 8% over the next 4 years; whereas the India addressable power cable market of USD 1.4 billion is estimated to grow at a CAGR of 12% over the next 4 years.



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