



## Sesa Goa

BSE SENSEX 18,969	S&P CNX 5,687	<b>Rs326</b>	<b>Buy</b>
Bloomberg Equity Shares (m)	SESA IN 889.7		
52-Week Range (Rs)	494/287		
1,6,12 Rel. Perf. (%)	9/-16/-26		
M.Cap. (Rs b)	290.1		
M.Cap. (US\$ b)	6.3		

Consolidated

- Sesa Goa's 3QFY11 adjusted PAT increased 28% YoY to Rs10.6b, below our estimate of Rs14.9b, due to lower-than-expected volumes. Reported PAT of Rs3.9b included forex gains of Rs23.8m on an FCCB.
- Iron ore shipments declined 21% YoY to 5.38mt. Sales from Goa declined 18% YoY to 4.2mt (including Dempo) due to extended monsoons and restricted road transport timings.
- Iron ore costs increased due to an increase in rail and road freight, demurrage and third-party mine owner royalties. In Orissa, rail freight increased by US\$25/ton QoQ. The company agreed to a 100% hike in road freight by truckers (to avoid loss of volumes) and expects the cost of production to increase by US\$1.2/t to US\$22/t from its Goa operations.
- Realization for iron ore was US\$87/ton v/s our estimate of US\$82/ton due to higher iron ore prices. Domestic sales increased to 15% of volumes (from 3% in 3QFY10) due to an export ban from Karnataka. The realization in the domestic market for Karnataka iron ore is US\$30-35/ton lower than in export markets.
- FY11 iron ore volumes are expected to be flat at 20.5mt, which implies significantly higher volumes of 7.7mt (up 39% QoQ) for 4QFY11.

### FY12 EPS cut due to higher tax guidance; strong 4QFY11; Buy

- We expect iron ore volumes and realizations to grow in 4QFY11, leading to higher profits as demand from China is strong and bottlenecks due to rains are unlikely. We maintain FY11 estimates but cut FY12 EPS by 7% to Rs43.6, assuming iron ore prices will average at US\$150/ton (lower than the current price of US\$190/ton).
- The stock trades at a P/E of 7.5x FY12E and EV/EBITDA of 3.2x FY12E. Maintain **Buy**.

### QUARTERLY PERFORMANCE (CONSOLIDATED)

Y/E MARCH	(RS MILLION)									
	FY10				FY11				FY10	FY11E
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE		
<b>Net Sales</b>	<b>10,115</b>	<b>5,387</b>	<b>18,892</b>	<b>24,189</b>	<b>24,131</b>	<b>9,183</b>	<b>22,501</b>	<b>27,011</b>	<b>58,583</b>	<b>82,826</b>
Change (YoY %)	-21.7	-37.6	38.9	67.6	138.6	70.5	19.1	11.7	18.1	41.4
<b>EBITDA</b>	<b>4,531</b>	<b>1,527</b>	<b>10,360</b>	<b>15,030</b>	<b>15,507</b>	<b>3,034</b>	<b>12,306</b>	<b>18,825</b>	<b>31,448</b>	<b>49,671</b>
Change (YoY %)	-44.5	-62.6	85.1	99.5	242.2	98.7	18.8	25.2	23.7	57.9
As % of Net Sales	44.8	28.3	54.8	62.1	64.3	33.0	54.7	69.7	53.7	60.0
Interest	20	20	251	227	137	140	134	133	517	544
Depreciation	152	202	225	166	191	194	208	196	745	789
Other Income	752	893	1,325	1,291	1,609	1,004	1,268	1,262	4,260	5,143
<b>PBT (before XO item)</b>	<b>5,110</b>	<b>2,198</b>	<b>11,210</b>	<b>15,928</b>	<b>16,787</b>	<b>3,704</b>	<b>13,232</b>	<b>19,758</b>	<b>34,446</b>	<b>53,481</b>
EO					-911	364	24	0		-523
<b>PBT (after XO item)</b>	<b>5,110</b>	<b>2,198</b>	<b>11,210</b>	<b>15,928</b>	<b>15,877</b>	<b>4,068</b>	<b>13,255</b>	<b>19,758</b>	<b>34,446</b>	<b>52,959</b>
Total Tax	869	503	2,906	3,777	2,832	189	2,573	3,161	8,056	8,755
% Tax	17.0	22.9	25.9	23.7	17.8	4.6	19.4	16.0	23.4	16.5
<b>Reported PAT before MI</b>	<b>4,241</b>	<b>1,694</b>	<b>8,304</b>	<b>12,151</b>	<b>13,045</b>	<b>3,879</b>	<b>10,683</b>	<b>16,597</b>	<b>26,390</b>	<b>44,204</b>
Minority Interest	18	30	29	22	27	30	30	30	99	117
<b>Adjusted PAT</b>	<b>4,223</b>	<b>1,665</b>	<b>8,275</b>	<b>12,129</b>	<b>13,766</b>	<b>3,502</b>	<b>10,634</b>	<b>16,567</b>	<b>26,291</b>	<b>44,523</b>
Change (YoY %)	-34.5	-48.7	75.8	121.5	226.0	110.4	28.5	36.6	32.2	69.3
Fixed assets		22,163		22,557		24,299		23,539	22,557	23,539
Cash etc (net of debt)		24,228		69,566		75,808	82,300	96,359	69,566	96,359
Net Working Capital		13,773		7,842		17,405		12,917	7,842	12,917

E: MOSL Estimates

Sesa Goa 3QFY11 adjusted PAT grew 28% YoY to Rs10.6b, below our estimate of Rs14.9b, due to lower-than-expected volumes.

### Iron ore volumes down 21% YoY, prices up

- Net sales increased 19% YoY to Rs22.5b, below our estimate of Rs25.8b, due to lower iron ore sales volumes.
- Sales tonnage fell 21% YoY to 5.38mt, mainly due to extended monsoons and restricted road transport timings in Goa. An ore export ban in Karnataka since July 2010 also impacted volume growth.
- Iron ore revenue grew 21% to Rs20.9b as realization improved 53% YoY to Rs3,882/ton (higher than our estimates of Rs3,687) as spot iron ore prices trended upward since mid-September.

### 3QFY11 EBITDA up 19% YoY at Rs12.3b

- Despite higher-than-estimated iron ore realizations, margins were lower by ~Rs300 at Rs2,146/ton due to higher transport and other expenditure.
- Segmental EBIT of iron ore grew 18% to Rs11.5b due to higher realizations. EBIT per ton increased 49% YoY to Rs2,146.
- Unallocated capital as of 31 December 2010 was Rs92.7b, cash and equivalents were Rs82.3b.

SEGMENTAL FINANCIALS									(RS MILLION)		
Y/E MARCH	FY10				FY11				FY10	FY11	FY12
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE			
<b>Realization (Rs/ton)</b>											
Iron ore	1,807	2,462	2,542	3,065	4,201	3,528	3,882	3,389	2,554	3,749	3,557
Change (QoQ %)	-29.4	36.3	3.3	20.6	37.1	-16.0	10.0	-12.7	-10.6	46.8	-5.1
Coke	13,616	13,064	15,275	16,080	17,341	17,662	17,005	16,910	14,522	18,606	16,214
Pig iron	18,675	19,179	19,815	21,436	22,293	21,401	21,615	21,832	19,779	23,325	22,631
<b>Sales Qty ('000 tons)</b>											
Iron ore	4,736	1,619	6,792	7,375	5,400	2,019	5,381	7,503	20,522	20,303	20,285
Change (YoY %)	45.7	16.6	24.9	47.2	14.0	24.7	-20.8	1.7	36.0	-1.1	-0.1
Coke	74	58	69	64	67	63	63	63	265	256	265
Pig iron	71	67	71	70	54	84	70	69	279	278	260
<b>Revenue (Rs m)</b>											
Iron ore	8,557	3,986	17,266	22,602	22,685	7,124	20,891	25,425	52,410	76,124	72,146
Change (YoY %)	-24.2	-38.5	38.3	76.2	165.1	78.7	21.0	12.5	21.7	45.2	-5.2
Coke	1,008	758	1,051	1,029	1,160	1,316	1,219	1,071	3,845	4,766	0
Pig iron	1,326	1,285	1,407	1,501	1,368	1,996	1,598	1,513	5,518	6,475	5,884
<b>EBIT (Rs m)</b>											
Iron ore	3,926	1,007	9,816	14,511	14,744	2,170	11,549	18,040	29,259	46,503	48,381
Coke	254	-32	-4	122	281	333	222	287	341	1,122	490
Pig iron	207	356	343	267	310	341	346	303	1,173	1,299	940
<b>Costs (Rs/ton)</b>											
Iron ore	978	1,840	1,097	1,097	1,471	2,454	1,736	984	1,128	1,459	1,605
Coke	10,182	13,612	15,330	14,167	13,136	12,372	13,486	12,387	13,234	14,224	14,366
Pig iron	15,765	13,863	14,985	17,626	16,556	17,338	16,696	17,465	15,576	18,644	19,017
USD/INR	48.7	48.4	46.6	45.1	45.6	46.5	44.75	44.50	47.2	45.3	44.5
Realization (US\$/Ton)	37	51	55	68	92	76	87	76	54	83	80
Iron ore spot (\$/t cfr China)	69	93	100	136	167	145	160	160	100	158	150
Contract prices (\$/ton fob)	60	60	60	60	110	138	148	157	60	138	110
Iron ore cost US\$ per ton	20	38	24	24	32	53	39	22	24	32	36
Iron ore EBITDA US\$ per ton	17	13	31	44	60	23	48	54	30	51	44

### Concall highlights: Volumes to remain flat in FY11 and FY12

- FY11 iron ore volumes are expected to be flat at 20.5mt, which implies significantly higher volumes of 7.7mt (up 39% QoQ) in 4QFY11. This is in line with our expectation. Inventories at end of 3QFY11 were 5.57mt- 3mt in Goa, 270k tons in Orissa (to liquidate in 4QFY11) and 2.3mt in Karnataka.
- FY12 volumes are also expected to be flat YoY at 20.5mt. A loss of ~1.8mt due to termination of a contract for Orissa operations will be offset by expansion of Karnataka capacity. The mining capacity is expected to increase to 10mtpa (6mtpa currently) by the end of FY12.
- China is the largest customer, taking ~78% of the company's volumes. Domestic sales increased to 15% (v/s 3% in 3QFY10) of total volumes due to an export ban from Karnataka. The realization in the domestic market for Karnataka iron ore is US\$30-35/ton lower than the export market.
- 3QFY11 iron ore shipment of 5.38mt included 4.2mt from Goa (including 1.6mt from Dempo), 700k tons from Karnataka and 450k tons from Orissa. Goa shipments were impacted by an extended monsoon and restricted road transport timings.
- Iron ore costs increased due to increased rail and road freight, demurrage, and third-party mine owner royalties. In Orissa, rail freight increased by US\$25/ton QoQ. The company agreed to a 100% hike in road freight by truckers (to avoid loss of volumes) and expects costs of production to increase by US\$1.2/t to US\$22/t from its Goa operations.
- The management expects the export ban in Karnataka to be lifted in February and it expects to ramp up export volumes immediately with 2.3mt of inventories in Karnataka.
- Capex was Rs3b and Rs5.1b in 3QFY11 and 9mFY11 respectively. In FY11 the capex is expected to be Rs9.5b (including Rs2b on sustenance).
- Sesa's reserves and resources were 275mt excluding Orissa.

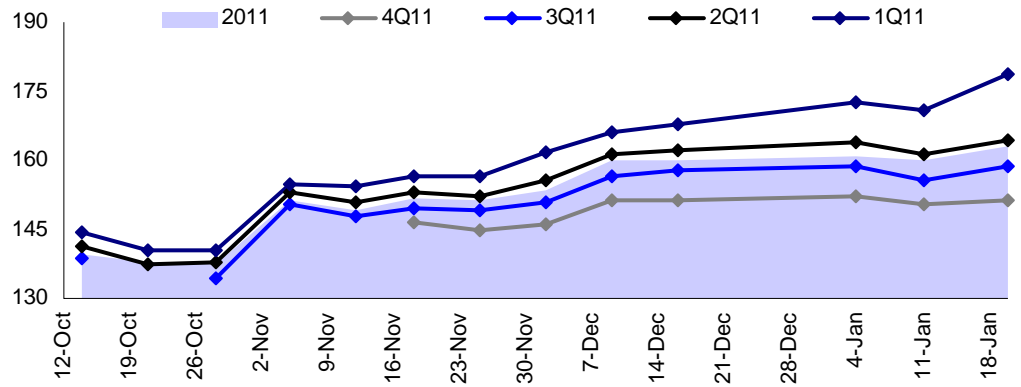
### Tax rate to return to 33% in FY12

- The tax rate for FY11 is ~17% as a few units were operating as EOUs (which will come to an end in March 2011 due to the sunset clause). For FY12 full tax rates will kick in, which will increase the tax burden. We had modeled in ~28% tax rate for FY12 earlier.
- The effective ad-valorem royalty rate in 3QFY11 was Rs233 per ton (a ~40% increase QoQ) due to higher iron ore prices.

### FY12 EPS cut on higher tax guidance; valuations attractive; Buy

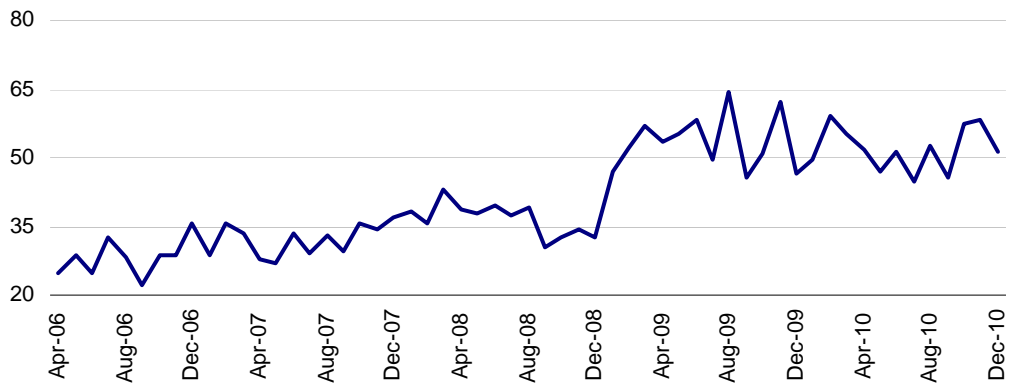
- We expect iron ore volumes and realizations to grow in 4QFY11 leading to higher profits as Chinese demand remain strong and bottlenecks due to rains are likely to be absent.
- We maintain our FY11 estimate but cut FY12 EPS by 7% to Rs43.6 assuming that iron ore prices will average US\$150/ton (much lower than the current price of US\$190/ton).
- Global iron ore supply is expected to be tight in 2011 due to a shortage of new capacities and reduced supply from India in the global seaborne market. However, the outlook for 2012 is more comfortable because several projects are expected to be commissioned. Iron ore prices may cross the highs of 2008 and peak in 2011. FOB realizations are even better due to crashing sea freights.
- Stock is trading at a P/E of 7.5x FY12E and EV/EBITDA of 3.2x FY12E. **Buy.**

**Iron ore swaps (cfr, 62% Fe) for quarterly contracts**

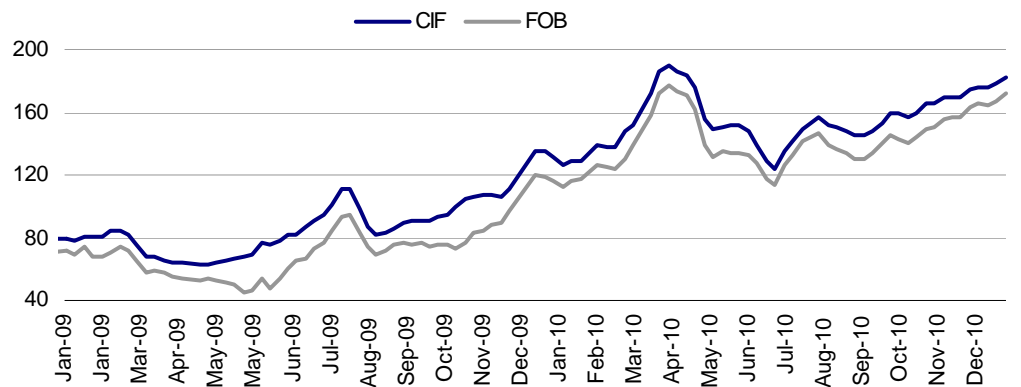


Source: Metal Bulletin/ MOSL

**China's monthly iron ore imports (M tons)**



**Indian iron ore 63% FE grade prices for shipment to china (US\$/ton)**



Source: Bloomberg/ MOSL

## Sesa Goa: an investment profile

### Company description

Sesa Goa has rich iron ore reserves and resources of 275mt in Goa and Karnataka. Goa's ore is medium grade and easy to extract without blasting and crushing. The iron ore from Karnataka is of high grade but is found in rocky form, which necessitates blasting and crushing. Sesa Goa is the largest private sector iron ore exporter in India.

### Key investment arguments

- Sesa Goa is determined to grow inorganically and organically.
- Iron ore volumes are expected to grow from 20.5mt in FY10 to 40mt in 2-3 years.
- Cost of mining and transport is significantly lower in Goa compared with mines in Karnataka and Orissa.
- The company has a strong focus on increasing reserves over 2-3 years from the existing 275mt.
- Indian miners are at an advantage over Brazilian miners due to their proximity to China, the largest customer.

### Key investment risks

- Unexpected softening of spot prices of iron ore led by a slowdown in steel demand will adversely impact earnings.

### Comparative valuations

		Sesa Goa	SAIL	JSW Steel
P/E (x)	FY11E	6.5	13.6	14.4
	FY12E	7.5	12.1	9.2
P/BV (x)	FY11E	2.2	1.8	1.4
	FY12E	1.7	1.7	1.2
EV/Sales (x)	FY11E	2.3	1.5	1.6
	FY12E	2.0	1.6	1.1
EV/EBITDA (x)	FY11E	3.9	8.4	8.6
	FY12E	3.2	8.0	5.6

### Shareholding Pattern (%)

	Dec-10	Sep-10	Dec-09
Promoter	55.7	55.7	57.5
Domestic Inst	4.5	3.4	3.9
Foreign	24.6	26.9	25.7
Others	15.2	14.0	13.0

### Recent developments

- The validity of the Scheme of Amalgamation of Sesa Industries with Sesa Goa has been extended up to 31 July 2011 or the date of the order of the Supreme Court, whichever is later.

### Valuation and view

- The stock trades at a P/E of 7.5x FY12E, and EV/EBITDA of 3.2x FY12E. Maintain **Buy**.

### Sector view

- Demand for iron ore is strong, largely driven by pig iron production growth in China. Though Chinese iron ore production is growing, the average grade is falling every year. As a result, China is becoming increasingly dependent on imports. The cost of iron ore production is high for marginal producers in China due to deteriorating grade and in India due to high logistic costs. Global supply is expected to be tight in 2011 due to the shortage of new capacities and lower supply from India in the global seaborne market. FOB realizations are even better due to crashing sea freight rates. As Indian steel production grows, iron ore exports are likely to stagnate or decline. Supplies in Australia, Brazil and South Africa are highly consolidated. We are positive on the outlook for iron ore prices.

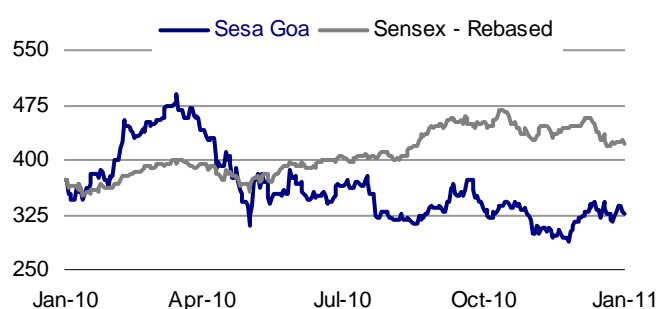
### EPS: MOSL forecast v/s Consensus (Rs)

	MOSL Forecast	Consensus Forecast	Variation (%)
FY11	50.1	48.5	3.3
FY12	43.6	52.5	-17.0

### Target Price and Recommendation

Current Price (Rs)	Target Price (Rs)	Upside (%)	Reco.
326	387	18.7	Buy

### Stock performance (1 year)



## Financials and Valuation

INCOME STATEMENT (CONSOLIDATED)			(RS MILLION)		
Y/E MARCH	2009	2010	2011E	2012E	2013E
<b>Net sales</b>	<b>49,591</b>	<b>58,583</b>	<b>82,826</b>	<b>78,553</b>	<b>83,382</b>
<i>Change (%)</i>	<i>29.7</i>	<i>18.1</i>	<i>41.4</i>	<i>-5.2</i>	<i>6.1</i>
Total Expenses	24,170	27,097	33,155	27,920	30,043
<b>EBITDA</b>	<b>25,421</b>	<b>31,486</b>	<b>49,671</b>	<b>50,633</b>	<b>53,338</b>
<i>% of Net Sales</i>	<i>51.3</i>	<i>53.7</i>	<i>60.0</i>	<i>64.5</i>	<i>64.0</i>
Deprn. & Amortization	517	745	789	824	831
<b>EBIT</b>	<b>24,904</b>	<b>30,741</b>	<b>48,882</b>	<b>49,810</b>	<b>52,507</b>
Net Interest	43	555	544	12	12
Other income	2,240	4,260	5,143	8,584	10,989
<b>PBT before EO</b>	<b>27,102</b>	<b>34,446</b>	<b>53,481</b>	<b>58,381</b>	<b>63,484</b>
EO income			-523		
<b>PBT after EO</b>	<b>27,102</b>	<b>34,446</b>	<b>52,959</b>	<b>58,381</b>	<b>63,484</b>
Current tax	7,100	8,012	8,755	19,521	21,240
Deferred tax	53	44			
Tax	7,153	8,056	8,755	19,521	21,240
<i>Rate (%)</i>	<i>26.4</i>	<i>23.4</i>	<i>16.5</i>	<i>33.4</i>	<i>33.5</i>
<b>Reported PAT</b>	<b>19,949</b>	<b>26,390</b>	<b>44,204</b>	<b>38,860</b>	<b>42,243</b>
Minority interests	69	99	117	74	70
<b>Adjusted PAT</b>	<b>19,880</b>	<b>26,291</b>	<b>44,609</b>	<b>38,786</b>	<b>42,173</b>
<i>Change (%)</i>	<i>29.0</i>	<i>32.2</i>	<i>69.7</i>	<i>-13.1</i>	<i>8.7</i>

BALANCE SHEET			(RS MILLION)		
Y/E MARCH	2009	2010	2011E	2012E	2013E
Share Capital	787	831	890	890	890
Reserves	46,370	78,346	130,220	165,363	203,892
<b>Net Worth</b>	<b>47,157</b>	<b>79,177</b>	<b>131,110</b>	<b>166,252</b>	<b>204,782</b>
Minority Interest	334	433	512	586	656
Total Loans	19	19,606	444	444	444
Deferred Tax Liability	664	750	750	750	750
<b>Capital Employed</b>	<b>48,175</b>	<b>99,966</b>	<b>132,815</b>	<b>168,032</b>	<b>206,632</b>
Gross Block	8,863	27,510	29,310	31,160	33,010
Less: Accum. Deprn.	3,422	5,741	6,558	7,412	8,305
<b>Net Fixed Assets</b>	<b>5,441</b>	<b>21,770</b>	<b>22,752</b>	<b>23,748</b>	<b>24,706</b>
Capital WIP	489	787	787	787	787
Investments	0	1	1	1	1
<b>Curr. Assets</b>	<b>48,084</b>	<b>89,808</b>	<b>118,744</b>	<b>152,595</b>	<b>190,448</b>
Inventory	2,642	5,009	5,278	4,864	5,194
Account Receivables	2,982	3,381	5,255	4,957	5,273
Cash and Bank Balance	31,429	69,566	96,359	130,922	168,130
Others	11,032	11,851	11,851	11,851	11,851
<b>Curr. Liability &amp; Prov.</b>	<b>5,840</b>	<b>12,400</b>	<b>9,468</b>	<b>9,099</b>	<b>9,310</b>
Account Payables	3,120	7,451	4,519	4,150	4,361
Provisions & Others	2,720	4,949	4,949	4,949	4,949
<b>Net Current Assets</b>	<b>42,244</b>	<b>77,408</b>	<b>109,275</b>	<b>143,496</b>	<b>181,138</b>
<b>Appl. of Funds</b>	<b>48,175</b>	<b>99,966</b>	<b>132,815</b>	<b>168,032</b>	<b>206,632</b>

E: MOSL Estimates

RATIOS					
Y/E MARCH	2009	2010	2011E	2012E	2013E
<b>Basic (Rs)</b>					
<b>EPS</b>	<b>25.3</b>	<b>31.6</b>	<b>50.1</b>	<b>43.6</b>	<b>47.4</b>
Cash EPS	26.0	32.7	50.6	44.6	48.4
BV/Share	59.9	95.3	147.4	186.9	230.2
DPS	2.3	3.2	3.5	3.5	3.5
Payout (%)	10.4	12.0	8.2	9.4	8.6
<b>Valuation (x)</b>					
P/E	12.9	10.3	6.5	7.5	6.9
Cash P/E	12.5	10.0	6.4	7.3	6.7
P/BV	5.4	3.4	2.2	1.7	1.4
EV/Sales	4.5	3.8	2.3	2.0	1.5
EV/EBITDA	8.9	7.0	3.9	3.2	2.3
Dividend Yield (%)	0.7	1.0	1.1	1.1	1.1
EV/ton (US\$)	19	13	12	10	8
<b>Return Ratios (%)</b>					
EBITDA Margins (%)	51.3	53.7	60.0	64.5	64.0
Net Profit Margins (%)	40.1	44.9	53.9	49.4	50.6
RoE	42.2	33.2	34.0	23.3	20.6
RoCE	51.7	30.8	36.8	29.6	25.4
RoIC	112.8	79.5	114.4	91.3	92.6
<b>Working Capital Ratios</b>					
Fixed Asset Turnover (x)	5.6	2.1	2.8	2.5	2.5
Asset Turnover (x)	1.0	0.6	0.6	0.5	0.4
Debtor (Days)	21.9	21.1	23.2	23.0	23.1
Inventory (Days)	5.3	8.6	6.4	6.2	6.2
Working Capital Turnover (x)	21.8	13.4	15.6	16.0	15.6
Creditors	43.0	77.3	41.7	42.3	40.8
<b>Leverage Ratio (x)</b>					
Current Ratio	8.2	7.2	12.5	16.8	20.5

CASHFLOW STATEMENT			(RS MILLION)		
Y/E MARCH	2009	2010	2011E	2012E	2013E
Pre-tax profit	27,102	34,446	52,959	58,381	63,484
Depreciation	517	745	789	824	831
(Inc)/Dec in Wkg. Cap.	-6,146	2,973	-5,075	343	-435
Tax paid	-7,100	-8,012	-8,755	-19,521	-21,240
Other operating activities	-585	1,504	-7,915	30	
<b>CF from Op. Activity</b>	<b>13,788</b>	<b>31,657</b>	<b>32,002</b>	<b>40,057</b>	<b>42,639</b>
(Inc)/Dec in FA + CWIP	-1,442	-18,945	-1,800	-1,850	-1,850
(Pur)/Sale of Investments	22	0	0		
Others					
<b>CF from Inv. Activity</b>	<b>-1,420</b>	<b>-18,945</b>	<b>-1,800</b>	<b>-1,850</b>	<b>-1,850</b>
Share Capital raised/(repaid)	394	8,999	19,162		
Debt raised/(repaid)	19	19,587	-19,162		
Dividend (incl. tax)	-2,072	-3,160	-3,643	-3,643	-3,643
Other financing activities					
<b>CF from Fin. Activity</b>	<b>-1,660</b>	<b>25,426</b>	<b>-3,643</b>	<b>-3,643</b>	<b>-3,643</b>
<b>(Inc)/Dec in Cash</b>	<b>10,709</b>	<b>38,138</b>	<b>26,559</b>	<b>34,563</b>	<b>37,146</b>
Add: Opening Balance	20,720	31,429	69,566	96,359	130,922
<b>Closing Balance</b>	<b>31,429</b>	<b>69,566</b>	<b>96,126</b>	<b>130,922</b>	<b>168,068</b>

**N O T E S**



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**Disclosure of Interest Statement**

**Sesa Goa**

1. Analyst ownership of the stock	No
2. Group/Directors ownership of the stock	No
3. Broking relationship with company covered	No
4. Investment Banking relationship with company covered	No

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