Indiabulls

SESA GOA LIMITED RESEARCH

EQUITY RESEARCH December 18, 2007

RESULTS REVIEW

Sesa Goa Limited — Hold

Firm prices augment growth

During the quarter ended Sep'07, Sesa Goa reported a substantial rise of 46.4% yoy in net sales primarily due to higher iron ore sales volume and the surge in prices of iron ore (up 70% yoy to USD 136 per tonne at the Chinese port) and metallurgical coke. However, strong rupee appreciation partially offset the affect of higher prices. EBITDA increased by a whopping 233.7% yoy due to higher net sales and lower operating costs.

On the back of a positive demand environment for iron ore, met coke and pig iron prices we expect the prices to remain firm. In addition, Vedanta's plan to expand Sesa's iron ore production capacity to 15 mtpa along with Sesa's initiative to acquire iron ore mines in Jharkhand and increase its pig iron capacity to 1 mtpa, would give further momentum to the Company's growth in the long run. Based on the abovementioned factors, our outlook on the Company remains positive.

To adjust for the surge in iron ore, met coke and pig iron prices we have revised our FY08E and FY09E revenue estimates upwards by 12.8% and 20.5% respectively. Also, adjusting for the lower incidence of export duty and lower than expected inland transportation costs, we have upgraded our FY08E estimated EBITDA by 17.1% and FY09E estimated EBITDA by 23.5%.

At present, the stock is trading at a forward EV/EBITDA of 13.1x for FY08E and 10.8x for FY09E. However, based on our valuations, we believe that all the positives are factored in and the stock is fairly valued at the current price. Therefore, we reiterate our Hold rating.

Share Data

Market Cap	Rs. 139.6 bn
Price	Rs. 3,543.65
BSE Sensex	19,079.64
Reuters	SESA.BO
Bloomberg	SESA IN
Avg. Volume (52 Week)	0.1 mn
52-Week High/Low	Rs. 3,940.6/1,170
Shares Outstanding	39.4 mn

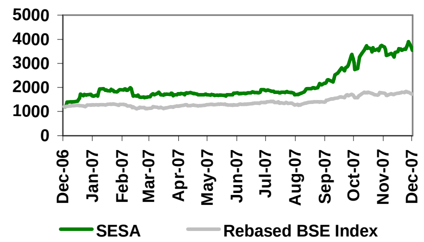
Valuation Ratios (Consolidated)

Year to 31 March	2008E	2009E
EPS (Rs.)	180.7	218.6
EPS Growth (%)	9.7%	21.0%
PER (x)	19.6x	16.2x
EV/ Sales (x)	5.4x	4.5x
EV/ EBITDA (x)	13.1x	10.8x

Shareholding Pattern (%)

Promoters	51
FIIs	21
Institutions	10
Public & Others	18

Relative Performance



Key Figures (Standalone)

Quarterly Data	Q2'07	Q1'08	Q2'08	YoY%	QoQ%	H1'07	H1'08	YoY%
(Figures in Rs. mn, except per share data)								
Net Sales	2,262	4,542	3,311	46.4%	(27.1)%	6,571	7,853	19.5%
EBITDA	320	1,753	1,068	233.7%	(39.1)%	2,274	2,821	24.1%
Adj. Net Profit	257	1,189	821	220.1%	(30.9)%	1,591	2,010	26.3%
Margins(%)								
EBITDA	14.2%	38.6%	32.3%			34.6%	35.9%	
NPM	11.3%	26.2%	24.8%			24.2%	25.6%	
Per Share Data (Rs.)								
Adjusted EPS	6.5	30.2	20.9	220.1%	(30.9)%	40.4	51.1	26.3%

Result Highlights (Standalone)

Iron ore production increased from 4.23 mn tonnes in H1'07 to 4.73 mn tonnes in H1'08

Sesa Goa's Q2'08 net sales increased 46.4% yoy to Rs. 3.3 bn. While net sales of iron ore segment grew 49.9% yoy driven by the surge in iron ore prices (up 70% yoy to USD 136 per tonne at the Chinese port) and higher sales volumes, net sales of metallurgical coke segment increased 32.7% yoy on the back of higher realisations. However, strong rupee appreciation arrested the impact of higher iron ore prices on the top line.

Metallurgical coke segment turned around on the back of rise in met coke prices

EBITDA increased by a whopping 233.7% yoy to Rs. 1.1 bn and EBITDA margin improved 18.1 pts yoy to 32.3%. The growth in EBITDA was led by higher realizations along with lower inland transportation charges, consumption of stores and purchase of ore. Inland transportation charges declined due to the commissioning of new rail lines in Orissa. However, the growth in EBITDA was contained by strong rupee appreciation and export duty expense of Rs. 212 mn. In addition, as a result of the increase in metallurgical coke prices, met coke segment turned around and posted an EBIT of Rs. 112 mn as compared to a loss of Rs. 22 mn in the corresponding period last year.

Despite the increase in pig iron prices, SIL's net profit declined 4% yoy

Adjusted net profit grew 220.1% yoy to Rs. 821 mn and adj. net profit margin improved 13.5 pts yoy to 24.8%. The improvement in adj. net profit margin was a result of higher realizations, lower depreciation expense and rise in other income. The effective tax rate increased 167 bps yoy to 29.2% during the quarter. However, on a consolidated basis, net profit increased 140.6% yoy as compared to a rise of 220.1% yoy on a standalone basis due to a decline of 4% yoy in the net profit of Sesa Industries Limited (SIL).

Key Risks

Key risks to our rating are:

- Sharp increase in the iron ore prices
- Higher than expected increase in the state royalties on mining of iron ore could adversely impact our earnings estimates
- Unexpected changes in the ocean freight charges and other transportation costs
- Sharp appreciation in rupee vis-à-vis US dollar
- Imposition of controls on the exports of iron ore

Outlook

We remain positive on iron ore demand and expect iron ore prices to surge 30% in 2008

Rapid expansion in the global steel sector, particularly in China, is boosting the demand for iron ore considerably. Moreover, higher ocean freight on supplies from Brazil and congestion at Australian ports resulting in delayed supplies is increasing the demand for Indian ore. As a result, the prices of Indian iron ore in the Chinese spot market have surged by more than 100% from the previous year levels and are currently at USD 196 per tonne. The current strong demand scenario is expected to continue, therefore, we have revised our iron ore price forecasts for 2008 and expect the prices to increase by around 30%, as against our earlier forecast of a 20% increase. Moreover, the prices of metallurgical coke and pig iron are also expected to rise in the near future. Thus, we expect higher prices to more than offset the appreciation in rupee, and post revenue CAGR of 18.7% over FY07-09E.

Capacity expansion would enable volume led growth in the long run, even after stabilization of iron ore prices

Further, the Company expects its output to be better during H2'08 and therefore, sell the additional production on spot basis. This will in turn help Sesa to take advantage of higher spot prices. In addition, Vedanta, having 51.2% stake in Sesa Goa, has set out aggressive growth plans for the Company. It plans to:

- Enhance the production capacity of iron ore from 10 mtpa to around 15 mtpa by the end of FY09
- Improve Sesa's share in the Indian iron ore production to one-third

Currently, Sesa has iron ore reserves of around 200 mn tonnes

All these efforts by Vedanta coupled with Sesa's initiative to acquire iron ore mines in Jharkhand and increase its pig iron capacity from 0.2 mtpa to around 1 mtpa in the next 2 years (by investing Rs. 10 bn), would give further momentum to the Company's growth in the long run.

To adjust for the surge in iron ore, met coke and pig iron prices we have revised our FY08E and FY09E revenue estimates upwards by 12.8% and 20.5% respectively. Also, adjusting for the lower incidence of export duty (as a result higher sales in the spot market and higher exports of low grade ore) and lower than expected inland transportation costs, we have upgraded our FY08E estimated EBITDA by 17.1% and FY09E estimated EBITDA by 23.5%.

At present, the stock is trading at a forward EV/EBITDA of 13.1x for FY08E and 10.8x for FY09E. However, based on our valuations, we believe that all the positives are factored in and the stock is fairly valued at the current price. Therefore, we reiterate our Hold rating.

Key Figures (Consolidated)

Year to March	FY05	FY06	FY07	FY08E	FY09E	CAGR
(Figures in Rs. mn, except per share data)						(FY07-09E)
Net Sales	14,933	18,175	21,761	26,001	30,681	18.7%
EBITDA	7,360	8,674	9,596	10,673	12,892	15.9%
Adj. Net Profit	4,732	5,678	6,483	7,115	8,606	15.2%
Margins(%)						
EBITDA	48.3%	47.0%	43.4%	40.4%	41.4%	
NPM	31.1%	30.8%	29.3%	26.9%	27.6%	
Per Share Data (Rs.)						
Adjusted EPS	120.2	144.3	164.7	180.7	218.6	15.2%
PER (x)	6.1x	8.9x	21.5x	19.6x	16.2x	

**Net sales exclude hire charges and service income*

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