

Sterlite Industries

Site Visit Day 1- Aluminum and Power operations - It is going to be all about Coal - ALERT

- **Power update:** The site currently has 3600MW capacity (135MWx9 and 600MWx4). **The 1215MW power plant is operating at 97% PLF and services the 0.5MT aluminum smelter. In terms of coal sourcing, only 35% is linkage coal and the rest is mainly e-auction coal (for captive power plants after 2008, Coal India is supplying 50% of linkage coal). Currently the cost of generation is nearly Rs2.1/unit (cash cost) and in our view, this will slightly move up because of the recent coal price hikes implemented by MCL. Regarding the 600MWx4 units, currently the first 2 units are getting synchronized and management expects steady improvement in PLF. The key issue behind the low PLF was transmission line and only very recently a new line of 25km (carrying capacity of up to 800MW) connecting to the national grid has been constructed and hence generation should increase. The 25km line was delayed because of some protests, which have now been resolved. The existing evacuation line (capacity of up to 450MW) is used for supply to state grid. Another line of 25km is being constructed with carrying capacity of up to 1000MW and this line should be ready by Oct-11, and post this the total evacuation capacity would be nearly 2200MW. As per management, the CoP for the 600MWx4 plant, at steady state PLF, would be Rs1.70/unit with increase from here driven by recent Coal India price rise. The company expects that the first unit of 600MW could hit +90% PLF in Mar quarter and the 2nd unit could have PLF of 86% in the Jun quarter.**

- **Its all about coal:** The sight of dozens of trucks outside the plant loaded with coal seemed surreal until management said that at month end the plant gets nearly 6000 trucks a day (60kt of coal a day) and on average there are 2500 trucks a day. This is because the e-auction coal is transported by trucks. **Currently 2/3rd of coal for the 1215MW plant is from e-auction and the management expects to source 1/3rd coal from non-linkage sources on a steady state basis.** Currently the site buys 0.4MT of coal on e-auction basis which would increase to 0.6MT per month once the 600MWx4 stabilizes. The site is also importing coal at the rate of 50kt per month with the port nearly 400km away. Company expects to import up to 100kt per month when 3600MW is ready. The current landed cost of imported coal (3000GCV) is Rs2800-3000/MT vs Rs2000/MT for e-auction coal prices. The boilers can accept coal of 3000GCV+4000GCV, which essentially means imported coal would need to be blended with domestic coal. **At full 3600MW operating at +90% PLF would require as much as 23MT coal. While management expects to source a third on e-auction, we believe it should be much higher- nearly 50%.** For the Balco coal block (very critical for profitability upside surprise on the upcoming 1200MW

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Overweight

STRL.BO, STLT IN

Price: Rs170.90

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Metals

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project), the company expects to receive the final environment clearance by May-2011, final forest clearance by June-2011 and mining lease by August-2011.

- **Coal movement infrastructure:** We found it interesting that the company is investing in building MGR (merry go round) to evacuate coal from Coal India's mines and also investing in rail infrastructure. Company expects to have railway logistics infrastructure in place by FY13 to move 23MT of coal by rail (including e-auction), which would greatly minimize the average truck movement per day from 2000 trucks level currently. The 1st ash pond would be ready in 2 months. 500-600 acres land is under acquisition at Jharsuguda. Total railway rakes required in 2 years' time would be 28 rakes. The company highlighted that it has purchased 4 box rakes and has given it to eastern railways (one rake cost is Rs200MM). While there is no discount, it eases rake availability and company plans to buy more rakes.
- **Aluminum update:** We last visited the project site in March-09 when work had just started on the 1.25mt smelters with fabrication work starting on line 1&2 and piling work on line 3&4. Currently, lines 1&2 are mostly ready and some work is required on line 3&4. Management highlighted that it would require 3 months to commission the lines (ramp up would take another 6 months) and highlights that once the alumina issue is resolved, the smelting capacity can be quickly brought around. **Currently the 0.5MT aluminum smelter sources alumina from Lanjigarh refinery and imports with Lanjigarh alumina at \$300/MT and freight of \$35/MT while imported alumina at nearly \$500/MT landed at plant. Current aluminum CoP stands at \$1900-\$1950/MT in VAL and \$1750-\$1800/MT at Balco (we estimate sharp increase at Balco CoP given that it gets nearly 70% linkage coal which would be impacted by the 30% Coal India price increase).** On Lanjigarh management highlighted that for the expansion from 1.4MT to 5MT can be done in 6 months.

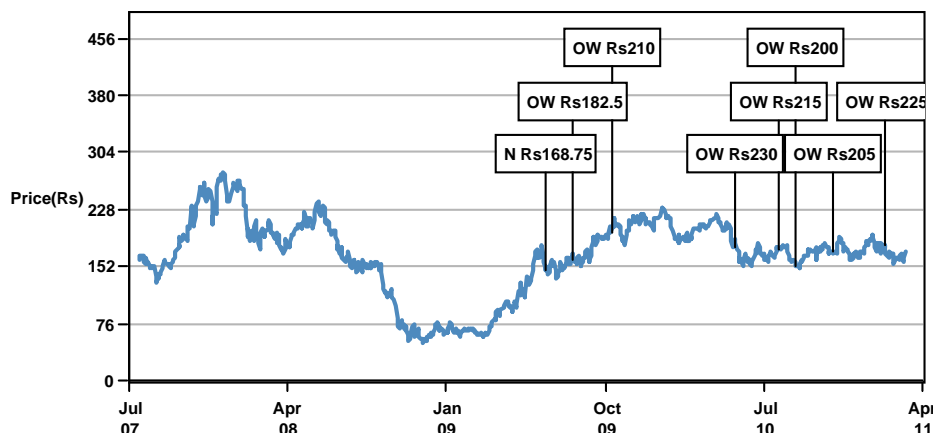
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Sterlite Industries (STRL.BO) Price Chart



Date	Rating	Share Price (Rs)	Price Target (Rs)
18-Jun-09	N	147.23	168.75
03-Aug-09	OW	161.20	182.50
11-Oct-09	OW	197.98	210.00
10-May-10	OW	178.46	230.00
27-Jul-10	OW	173.85	215.00
25-Aug-10	OW	152.15	200.00
27-Oct-10	OW	172.20	205.00
26-Jan-11	OW	179.05	225.00

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Jun 18, 2009. This chart shows J.P. Morgan's continuing coverage of this stock; the current analyst may or may not have covered it over the entire period. J.P. Morgan ratings: OW = Overweight, N = Neutral, UW = Underweight.

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