

Hindustan Zinc Ltd – BUY

CMP Rs332, Target Rs380

Sector: Metals & Mining

Sensex:	8,779
CMP (Rs):	332
Target price (Rs):	380
Upside (%):	14.4
52 Week h/l (Rs):	763 / 215
Market cap (Rscr) :	14,020
6m Avg vol ('000Nos):	57
No of o/s shares (mn):	423
FV (Rs):	10
Bloomberg code:	HZ IB
Reuters code:	HZNC.BO
BSE code:	500188
NSE code:	HINDZINC

Prices as on 21 Jan, 2009.

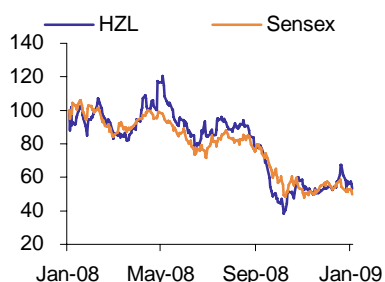
Shareholding pattern

December '08	(%)
Promoters	64.9
Institutions	33.1
Non promoter corp hold	0.5
Public & others	1.5

Performance rel. to sensex

(%)	1m	3m	1yr
HZL	12.3	36.9	2.8
Hindalco	0.7	(9.9)	(18.6)
Sterlite	(2.5)	5.1	(20.2)
NALCO	12.1	(12.3)	(5.5)

Share price trend



- ⊕ Revenues drop 40.3% qoq, despite 24% qoq increase in metal volume
- ⊕ Operating profit plunges 68.9% qoq as by-product realizations decline
- ⊕ Higher other income partially offsets impact of sharp operating margin contraction
- ⊕ Cash and cash equivalents of Rs221 per share provides cushion
- ⊕ Zinc prices expected to remain weak due to surplus capacities globally

Result table

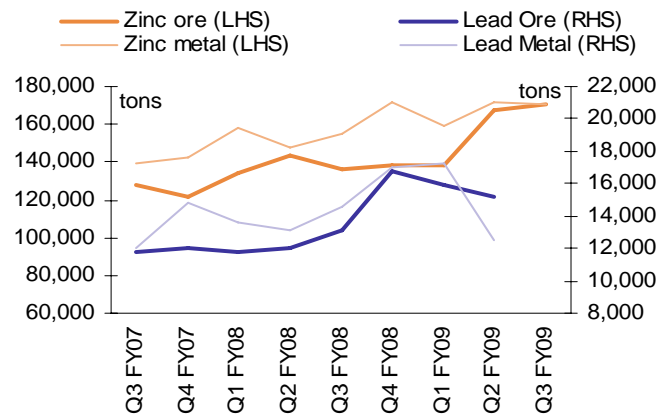
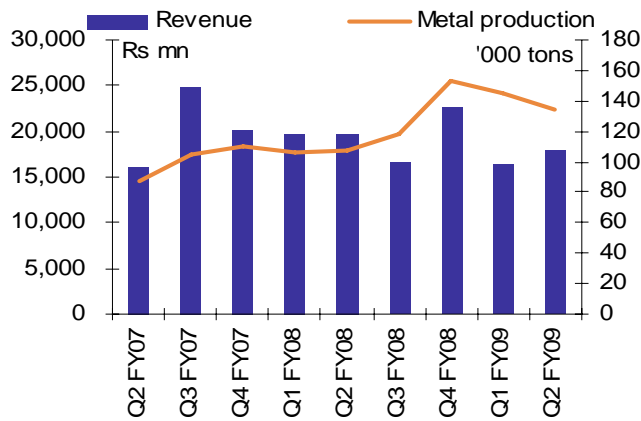
(Rs m)	Q3 FY09	Q3 FY08	% YoY	Q2 FY09	% QoQ
Net sales	10,692	16,840	(36.5)	17,905	(40.3)
Mining & manufacturing	(5,817)	(5,370)	8.3	(6,286)	(7.5)
Personnel costs	(1,065)	(930)	14.5	(865)	23.1
Other overheads	(760)	(770)	(1.3)	(933)	(18.5)
Operating profit	3,051	9,770	(68.8)	9,821	(68.9)
OPM (%)	28.5	58.0	-2,948 bps	54.8	-2,632 bps
Depreciation	(712)	(540)	31.9	(704)	1.1
Interest	(44)	(60)	(27.5)	(71)	(38.9)
Other income	2,363	1,110	112.8	1,807	30.7
PBT	4,658	10,280	(54.7)	10,853	(57.1)
Tax	(969)	(3,100)	(68.7)	(1,257)	(22.9)
Effective tax rate (%)	20.8	30.2		11.6	
Adjusted PAT	3,688	7,180	(48.6)	9,595	(61.6)
Adj. PAT margin (%)	34.5	42.6	-1,410 bps	53.6	-2,506 bps
Ann. EPS (Rs)	34.9	68.0	(48.6)	90.8	(61.6)

Source: Company, India Infoline Research

Revenues drop 40.3% qoq, despite 24% qoq increase in metal volume

Hindustan Zinc Ltd (HZL) reported a 40.3% qoq fall in topline, which was inline with our estimates. The collapse in by-product prices offset higher than expected increase in metal sales volume. Volumes jumped 24.2% qoq to 166,539 tons. The company did not reported any concentrate sales during the quarter, against sales of 97,000 dry tons in Q2 FY09. Prices of by-product like sulphuric acid have more than halved on a qoq basis adding to the pressure on topline. Average LME price for zinc and lead during the quarter was US\$1,189 and US\$1,251 per ton, a drop of 32.9% and 34.6% qoq respectively. This was 55.1% and 61.6% yoy for both the metals respectively.

Quarterly revenue and metal production trends

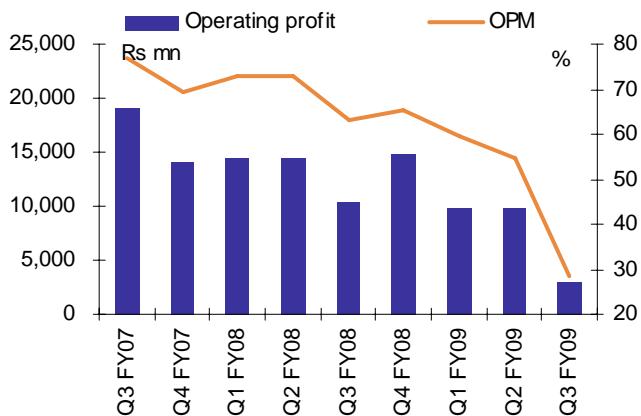


Source: Company, India Infoline Research

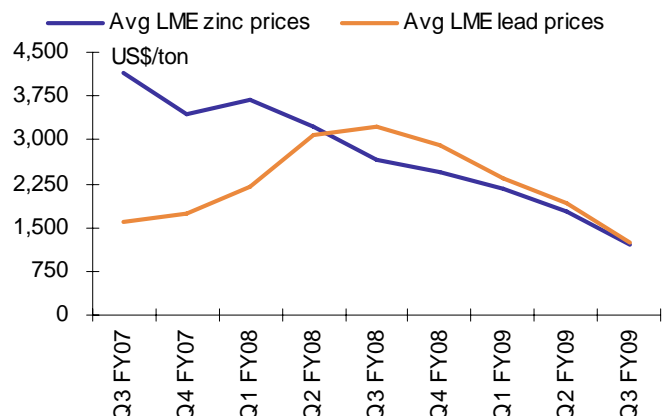
Operating profit plunges 68.9% qoq as by-product realizations decline

HZL reported a 2,632bps operating margin contraction during the quarter on account of lower by-product prices and higher input costs of coal and coke. Coupled with this, lower LME prices of both metals aided 68.9% qoq fall in operating profit to Rs3.1bn. Excluding royalty, mining and manufacturing costs per ton of refined metal rose marginally to Rs27,746 per ton over the sequential quarter. Cost of production net of by-product revenues but including royalty jumped to US\$780 per ton from US\$670 per ton in H1 FY09.

Quarterly OPM lowest in last three years



LME price movement



Source: Company, Bloomberg, India Infoline Research

Cost analysis

As a % of net sales	Q3 FY09	Q3 FY08	bps yoy	Q2 FY09	bps qoq
Mining & manufacturing	54.4	31.9	2,251	35.1	1,929
Personnel costs	10.0	5.5	444	4.8	513
Other overheads	7.1	4.6	254	5.2	190
Total costs	71.5	42.0	2,948	45.2	2,632

Source: Company, Bloomberg, India Infoline Research

Higher other income partially offsets impact of sharp operating margin contraction

HZL's current net cash position stood at Rs9.3bn, which includes Rs6.2bn in debt mutual funds and Rs3.1bn in fixed deposits with banks. Post tax returns on these investments stood at 8.7%. An increase in investments during the quarter resulted into a 30.7% qoq jump in other income. This partially offset the impact of decline in operating profit margin. Also a 38.9% decrease in interest cost helped lower drop in profit. Higher other income translated into higher effective tax rate for the quarter. The company indicated that the rise in sales from its export oriented unit will keep its tax rate in the range of 10-15%. PAT during the quarter, slipped 61.6% qoq to Rs3.7bn.

Cash and cash equivalents of Rs221 per share provides cushion

We expect, HZL to miss its earlier production target of 0.65mn tons in FY09 and 0.75mn tons in FY10. Zinc metal surplus is likely to expand further in 2009, thus keep zinc prices low. Demand for the metal is not expected to revive in the near term leading to further rise in inventory levels. We expect the weakness in zinc prices to extend till H1 FY10 and marginally bounce back in the later half of FY10. The weakness in the zinc market will tap upside for HZL over the next two years. Cash and cash equivalent of Rs221 per share, representing 71% of its current market cap, will limit downside for the stock. We recommend BUY with a price target of Rs380.

Financial summary

Y/e 31 Mar (Rs m)	FY08	FY09E	FY10E	FY11E
Revenues	78,778	51,559	49,621	64,578
yoy growth (%)	(8.0)	(34.6)	(3.8)	30.1
Operating profit	53,784	24,691	21,046	31,785
OPM (%)	68.3	47.9	42.4	49.2
Pre-exceptional PAT	43,961	23,949	21,498	29,140
yoy growth (%)	(1.0)	(45.5)	(10.2)	35.5
EPS (Rs)	104.0	56.7	50.9	69.0
P/E (x)	3.3	6.0	6.7	4.9
Price/Book (x)	1.2	1.0	0.9	0.8
EV/EBITDA (x)	2.4	5.2	6.2	3.9
RoE (%)	45.1	18.4	14.2	16.6
RoCE (%)	59.4	23.1	17.8	20.9

Source: Company, India Infoline Research

Recommendation parameters for fundamental reports:

Buy – Absolute return of over +10%

Market Performer – Absolute return between -10% to +10%

Sell – Absolute return below -10%

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