

# Lowering estimates for metal price changes



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## Lowering estimates on metal price changes

Our Metals Strategist has cut metal price forecasts due to the global slowdown and MTM. ([Metals Strategist, 01 December 2011.](#)) Our global team has cut FY13e price forecasts for Al by 11%, Cu by 7% and Zn by 3%. We also factor in a weaker INR, which cushions the impact. We have cut our FY13e EPS by 6-16% and our POs by 4-11% across our base metal companies. We remain cautious due to macro concerns. Valuations appear reasonable, but downside risks to exist and upside triggers are lacking, in our view. We prefer Sterlite, as it offers deep value and the risk/reward appears positive. In HNDL, triggers are absent, as project issues are unresolved.

## Zn: lower surplus; Al: tight physical mkt., but deficit lower

We expect zinc prices to be capped, as zinc markets are well supplied. But zinc prices should be supported near current levels as we expect concentrate markets to tighten through CY12 and eventually push refined markets into deficit in CY13. In aluminum, despite structural excess capacity, we believe financing deals should support Al prices in CY12. However, we expect physical markets to be less undersupplied due to slowing demand growth. Our FY12/FY13e LME price forecast for zinc is US\$2029/t/US\$2150/t and for Al, it is US\$2247/t/US\$2313/t.

## Sterlite (STLT): Offers deep value, favorable risk reward

We have cut our FY12-13e EPS by 2-7% due to lower metal price forecasts. Downside risk to Zn prices appears low and the medium-term outlook appears positive. Saleable silver (Ag) volume is likely to increase post the expected commissioning of a 350tpa silver refinery in Dec Q. We expect Ag vols. to grow at a CAGR of 26% over next 3 years and should contribute to 8% of FY13e EBITDA. Coal supply issues should persist at SEL, but availability should improve incrementally in 2HFY12, as CIL output improves post monsoon. Valuation, at 3.0x FY13e EBITDA, appears attractive and concerns around SEL and VAL assets appear to be already priced in.

## Hindalco: Reasonable valuations, but catalysts absent

We have cut FY13e EPS by 6% due to the lower Al price est. We have also cut Novelis FY12-13e EBITDA by 2-5% (in US\$ terms) due to softer demand, but the impact on group EBITDA is offset due to the weaker INR est. Govt. approval w.r.t. Mahan coal block is still pending. Govt. decision to scrap Go/No Go classification of coal blocks offers some hope, but production from new coal blocks could take over 12-15 months, even after approval is obtained. Thus, EPS impact will not be meaningful near term, in our view. Valuation, at 0.8x BV, offers downside support.

## NALCO - cost pressures persist, valuation not compelling

Our FY12-13 EPS declines by 2-16% due to the lower AL LME forecast. We expect cost pressures to persist due to coal supply issues. The valuation, at 6.6x FY12e EBITDA, is not yet compelling, in our view. Hence, Underperform.

Table 1: Ratings unchanged

Rs	Rating	PO (Rs)
Sterlite	Buy	142
Hindalco	Neutral	136
NALCO	Underperform	49

Source: BoFA Merrill Lynch Global Research

Table 2: Summary of PO changes

Company	PO		
	New	Old	%chg
Sterlite	142	150	-5.3%
Hindalco	136	141	-3.5%
Nalco	49	55	-10.9%

Source: BoFA Merrill Lynch Global Research Estimates

Table 3: BoFAML Metal Price forecasts

US\$/t	FY12E			FY13E		
	New	Old	%chg	New	Old	%chg
Al	2247	2317	-3%	2313	2588	-11%
Cu	8124	7936	2%	7814	8375	-7%
Zinc	2029	2111	-4%	2150	2225	-3%
Lead	2293	2359	-3%	2276	2400	-5%

Source: BofA Merrill Lynch Global Commodities Research Estimates

\* for Fiscal year ending March

Table 4: Summary of EPS estimates

Rs	FY12E			FY13E		
	New	Old	% Chg	New	Old	% Chg
Sterlite	14.8	15.1	-2%	16.4	17.6	-7%
HNDL	15.4	15.0	3%	14.3	15.3	-6%
NALCO	3.7	3.8	-2%	3.8	4.5	-16%

Source: Sterlite, Hindalco, Nalco, BoFA Merrill Lynch Global Research Estimates

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Table 5: Price forecasts, fundamental drivers and risks

	Price forecasts*		Fundamental drivers	Risks (D = downside; U = upside)
	2012E	2013E		
Aluminium	\$2,275/t \$1.03/lb	\$2,375/t \$1.08/lb	<ul style="list-style-type: none"> <li>■ Although the spot market remains tight, it has eased off somewhat. Overall, aluminium can still be tied up in financing deals economically.</li> <li>■ Smelters have boosted operations. Global aluminium output has hit a new record. The Chinese aluminium market has been comparatively tight given healthy demand.</li> <li>■ Smelters will need to show production restraint in the coming years to restore a degree of normality on the aluminium market; there are signs of hope in China.</li> <li>■ We forecast a small <b>deficit</b> for 2012.</li> </ul>	<ul style="list-style-type: none"> <li>■ D: Deterioration of macro picture in Europe/ US.</li> <li>■ D: Contagion from Europe/ US to EM.</li> <li>■ D: Financing deals are broken and metal becomes available.</li> <li>■ D: There is considerable uncertainty over global aluminium production volumes in the medium term.</li> <li>■ U: Smelters show restraint and/or production disruptions reduce output.</li> <li>■ U: quantitative easing in Europe and the US</li> </ul>
Copper	\$7,750/t \$3.52/lb	\$7,313/t \$3.32/lb	<ul style="list-style-type: none"> <li>■ With global economic growth slowing, demand growth is set to decelerate in 2012.</li> <li>■ China has hardly any excess stocks, so imports should be better supported.</li> <li>■ Chinese demand set to expand at a steady pace, US offtake is ok and European demand should contract.</li> <li>■ The concentrates market remains tight and mine supply will likely constrain refined output in the coming years.</li> <li>■ We forecast a smaller <b>deficit</b> for 2012.</li> </ul>	<ul style="list-style-type: none"> <li>■ D: Deterioration of macro picture in Europe/ US.</li> <li>■ D: Contagion from Europe/ US to EM.</li> <li>■ D: China slows by more than currently factored in.</li> <li>■ U: Production disruptions in a tight concentrates market.</li> <li>■ U: China restocks.</li> <li>■ U: quantitative easing in Europe and the US.</li> </ul>
Lead	\$2,200/t \$1.00/lb	\$2,500/t \$1.16/lb	<ul style="list-style-type: none"> <li>■ Demand has been rising in 2010 as battery shipments have picked up. Offtake has also increased in 2011. Given continued steady activity levels in the automotive industry, this is set to carry over into 2012.</li> <li>■ Lead mine supply is not abundant and the scrap market is tight, so prices should respond to the better demand backdrop.</li> <li>■ We forecast in essence a <b>balanced</b> market in 2012.</li> </ul>	<ul style="list-style-type: none"> <li>■ D: Deterioration of macro picture in Europe/ US.</li> <li>■ D: Contagion from Europe/ US to EM</li> <li>■ D: Destocking in China or higher lead exports from the country.</li> <li>■ D: Lead production is correlated with zinc output. As zinc output may be expanding (see below), there is a risk that supply comes back more quickly than we currently factor in.</li> <li>■ U: quantitative easing in Europe and the US</li> </ul>
Zinc	\$2,075/t \$0.94/lb	\$2,425/t \$1.10/lb	<ul style="list-style-type: none"> <li>■ Zinc demand has been not been strong enough to push the refined market into a deficit.</li> <li>■ Galvanised steel producers have been ramping up production, operating at record rates.</li> <li>■ Mine supply has been relatively tight. Concentrates supply is set to constrain refined zinc production, making a hugely oversupplied market unlikely in 2012.</li> <li>■ Fundamentals are not extremely strong, but huge oversupplies are unlikely.</li> </ul>	<ul style="list-style-type: none"> <li>■ D: Deterioration of macro picture in Europe/ US.</li> <li>■ D: Contagion from Europe/ US to EM.</li> <li>■ D: Unreported inventories exist on the zinc market. More metal could become available.</li> <li>■ D: The zinc market is fragmented. There is evidence that miners consider further output increases.</li> <li>■ U: Subdued mine production increases.</li> <li>■ U: quantitative easing in Europe and the US.</li> </ul>

Source: BofA Merrill Lynch Global Commodity Research

\*= Forecasts refer to CY

Table 6: Comparable Valuation

Company	Mkt Cap* USD m	P/E		EV/EBITDA		P/BV	
		FY12e	FY13e	FY12e	FY13e	FY12e	FY13e
<b>Aluminum</b>							
Nalco	2,636	14.3	13.9	6.5	5.9	1.1	1.1
Hindalco	4,813	8.0	8.6	5.8	5.5	0.7	0.7
Rusal	11,196	6.0	8.2	9.4	11.5	0.8	0.8
Chalco	13,830	32.7	22.9	9.5	8.4	0.8	0.8
Norsk Hydro	9,921	13.3	19.3	5.0	6.3	0.6	0.6
<b>Average</b>		<b>14.9</b>	<b>14.6</b>	<b>7.2</b>	<b>7.5</b>	<b>0.8</b>	<b>0.8</b>
<b>Diversified</b>							
Sterlite	6,801	6.7	6.1	3.1	2.8	0.7	0.7
Vedanta	4,439	9.8	5.5	4.3	3.2	0.8	0.7
BHP Billiton	184,202	8.3	8.0	4.7	4.5	2.3	1.9
RIO	105,116	6.6	7.0	4.2	4.6	1.5	1.3
Anglo American	50,369	7.8	7.1	4.2	4.2	1.0	0.9
Xstrata Plc	47,421	7.6	8.5	4.6	4.7	1.0	0.9
<b>Average</b>		<b>7.8</b>	<b>7.0</b>	<b>4.2</b>	<b>4.0</b>	<b>1.2</b>	<b>1.1</b>

Source: BofA Merrill Lynch Global Research Estimates

\* =Based on prices as on 1 Dec 2011

## Lowering metal price forecasts

Table 7: BofAML metal price forecast\*

US\$/t	Spot	FY12E	FY13E	FY14E
Aluminum	2,103	2,247	2,313	2,476
Copper	7,860	8,124	7,814	7,127
Zinc	2,073	2,029	2,150	2,538
Lead	2,091	2,293	2,276	2,626

Source: BofA Merrill Lynch Global Commodities Research Estimates

\* for Fiscal year ending March

### Cross Reference

Following section has been extracted from our global team's report [Metals Strategist, 01 December 2011](#) authored by our Metals Strategist, Mike Widmer.

Our Metals Strategist has cut metal price forecasts due to the global slowdown and mark to market. ([Metals Strategist, 01 December 2011.](#)) Our global team has cut FY13e price forecasts for zinc by 3%, Cu by 7% and Al by 11%. We also factor in a weaker INR, which cushions the impact. We have cut our FY13e EPS by 6-16% and our POs by 4-11% across our base metal companies. We remain cautious due to the macro headwinds. Valuations appear reasonable, but downside risks to forecasts exist and upside triggers are lacking, in our view. We prefer Sterlite, as it offers deep value and the risk/reward appears positive. We maintain our Neutral rating on Hindalco, as triggers are absent, as project issues are unresolved.

### Macro/Base metals outlook: Crunch time in Europe, headwinds persist

Our global team remains cautious on metals due to macro headwinds and demand slowdown concerns. With governments retrenching, especially in advanced nations, private sector activity is critical for a sustained expansion. However, concerns over debt burdens continue to affect sentiment. Our global team's base case assumes that policy measures by European authorities should stop further escalation of the crisis. This could lead to some upside to metal prices from current spot prices, even though average prices in CY12 should be lower than CY11. However, lack of policy action could impact growth in the World ex Europe and could have severe implications for metals demand and prices.

### Zinc: well supplied, surplus to erode in CY12; deficit likely in CY13

We expect upside to Zn prices to be capped near term, as Zn markets are well supplied at present and are unlikely to move into deficit in FY13. However, concentrates availability has been relatively tight. We expect competition for mine production to increase through 2012. This could eventually push refined zinc markets into a deficit by CY13. Our Zn LME forecasts are US\$2029/t (-4% chg) in FY12e and US\$2150/t (-3% chg) in FY13e.

### Aluminum: less undersupplied in CY12

Despite structural issues around excess capacity and high inventory, the aluminum physical market has been tight due to financing deals and low warehouse load-out rates. While we expect financing deals to support aluminum prices in CY12, we expect physical markets to be less undersupplied in CY12 vs. CY11, due to that slowdown in global growth. Our new Al LME forecasts are US\$2247/t (-3%chg) in FY12e and US\$2313/t (-11%chg) in FY13e.

Table 8: Summary changes in metals price forecasts\*

US\$/t	FY12E			FY13E			FY14E		
	New	Old	%chg	New	Old	%chg	New	Old	%chg
Al	2247	2317	-3%	2313	2588	-11%	2476	2688	-8%
Cu	8124	7936	2%	7814	8375	-7%	7127	7250	-2%
Zinc	2029	2111	-4%	2150	2225	-3%	2538	2238	13%
Lead	2293	2359	-3%	2276	2400	-5%	2626	2675	-2%

Source: BofA Merrill Lynch Global Commodities Research \* = Fiscal year ending March

Table 9: Valuation Summary

Company	Price*	Mkt Cap	P/E		EV/EBITDA		P/BV	
			FY12e	FY13e	FY12e	FY13e	FY12e	FY13e
Nalco	53.4	2,636	14.3	13.9	6.5	5.9	1.1	1.1
Hindalco	131.3	4,813	8.0	8.6	5.8	5.5	0.7	0.7
Sterlite	105.7	6,801	6.7	6.1	3.1	2.8	0.7	0.7

Source: Sterlite, Hindalco, Nalco, BofA Merrill Lynch Global Research Estimates \* = Prices as on 1 Dec 2011

## Change in earnings forecasts and POs

We have cut our FY13e EPS by 6-16% and our POs by 4-11% across our base metal companies, as we have lowered our metal price forecasts. We have adjusted our Fx forecast to reflect a weaker INR. This has cushioned the impact of the metal price changes, in our view.

Table 10: Summary of EPS estimates

Rs	FY12E			FY13E			FY14E		
	New	Old	% Chg	New	Old	% Chg	New	Old	% Chg
Sterlite	14.8	15.1	-2%	16.4	17.6	-7%	18.7	18.5	1%
HNDL	15.4	15.0	3%	14.3	15.3	-6%	16.8	17.5	-4%
NALCO	3.7	3.8	-2%	3.8	4.5	-16%	4.1	4.9	-17%

Source: Sterlite, Hindalco, Nalco, BofA Merrill Lynch Global Research Estimates

- Sterlite (Buy, PO Rs142):** We have cut our FY12E EPS by 2%, to Rs14.8, and FY13E EPS by 7%, to Rs16.4, mainly due to lower metal price forecasts and higher losses at VAL. We have also lowered our power EBIDTA forecasts by 6-8% over FY12-13e, as we factor in lower PLF and higher costs due to coal supply issues. We have also adjusted our other income forecasts to reflect a stronger-than-expected 1HFY12. Our PO has been reduced to Rs142 (Rs150 earlier) as a result. Sterlite trades at 3.3x FY12 EBIDTA and 3x FY13e EBIDTA. We maintain our Buy rating, as Sterlite has multiple growth drivers and the risk/reward is favorable.
- Hindalco (Neutral, PO Rs136):** We have lifted our FY12e EPS marginally to Rs15.4, due to the weaker INR. In FY13, we have cut our EPS forecast by 6%, to Rs14.3, due to lower aluminum forecasts, though the impact is cushioned by the weaker INR. We have also trimmed Novelis' EBIDTA to US\$1.13bn in FY12 (-2%) and US\$1.17bn (-5%) in FY14e, due to a weaker demand outlook. Our PO has been reduced to Rs136 (Rs141 earlier). Hindalco trades at 6x FY12 EBITDA and 5.7x FY13 EBIDTA. We maintain our Neutral rating, as the earnings outlook is unexciting and catalysts are absent. However, valuations are reasonable and should offer downside support, in our view.
- Nalco (Underperform, PO Rs49):** We have cut our FY12 EPS by 2% and FY13 EPS by 16% due to the lower aluminum price forecasts. Our PO has been reduced to Rs49 (Rs55 earlier). We expect cost pressures to remain due to coal supply issues and increased dependence on imported coal. Also, visibility on future expansion remains poor, in our view, as most of the proposed projects are at very preliminary stages. Also, the valuation, at 6.6x FY12 EBIDTA, is not yet compelling, in our view.

# Sterlite

## Sterlite – Key assumption and forecasts

Table 11: Summary of changes in earnings estimates

in mn Rs.	FY12E			FY13E			FY14E		
	Old	New	% Chg	Old	New	% Chg	Old	New	% Chg
Net Turnover	323,482	330,697	2%	354,697	358,827	1%	350,669	367,230	5%
EBITDA	97,583	95,892	-2%	107,945	106,711	-1%	109,703	123,765	13%
EBITDA Margin	30%	29%	-4%	30%	30%	-2%	31%	34%	8%
EBIT	82,252	78,429	-5%	91,332	86,683	-5%	93,781	103,647	11%
Interest Costs, net*	-5,897	-14,749		-6,522	-16,330		-7,989	-11,605	
Pre-tax profit	88,149	93,177	6%	97,854	103,013	5%	101,770	115,252	13%
Tax	17,630	18,636	6%	19,571	20,603	5%	20,355	23,051	13%
Tax rate	20%	20%	0%	20%	20%	0%	20%	20%	0%
Profit After Tax	70,519	74,541	6%	78,283	82,410	5%	81,416	92,201	13%
Minority Interest	-15,891	-18,223		-17,598	-21,657		-18,067	-24,542	
Share of associates	-3,851	-6,536		-1,534	-5,761		-1,016	-4,721	
Attributable PAT	50,777	49,783	-2%	59,150	54,992	-7%	62,333	62,938	1%
EPS	15.1	14.8	-2%	17.6	16.4	-7%	18.5	18.7	1%

Source: Sterlite, BofA Merrill Lynch Global Research Estimates

\*\*= net of other income

Table 12: Summary changes in volume forecasts

	FY12E			FY13E			FY14E		
	Old	New	% Chg	Old	New	% Chg	Old	New	% Chg
Aluminum (kt)	245	245	0%	255	255	0%	255	255	0%
Zinc (kt)	763	763	0%	805	805	0%	815	815	0%
Lead (kt)	115	115	0%	139	139	0%	139	139	0%
Copper (kt)	305	315	3%	303	315	4%	303	315	4%
Power Units mn units	5,802	5,661	-2%	9,487	9,487	0%	13,281	11,384	-14%

Source: Sterlite, BofA Merrill Lynch Global Research Estimates

Table 13: Summary changes in price forecasts

	FY12E			FY13E			FY14E		
	Old	New	% Chg	Old	New	% Chg	Old	New	% Chg
Zinc - \$/ton	2,111	2,029	-4%	2,225	2,150	-3%	2,238	2,538	13%
Aluminum - \$/ton	2,317	2,247	-3%	2,588	2,313	-11%	2,688	2,476	-8%
Copper - \$/ton	7,936	8,124	2%	8,375	7,814	-7%	7,250	7,127	-2%
Lead - \$/ton	2,359	2,293	-3%	2,400	2,276	-5%	2,675	2,626	-2%
Avg Tariff- Rs/unit	3.5	3.6	2%	3.3	3.4	1%	3.2	3.2	1%
FX	46.5	47.5	2%	45.5	48	5%	45	46	2%

Source: Sterlite, BofA Merrill Lynch Global Research Estimates

**Table 14: Summary Consolidated Earnings Forecast**

in mn Rs.	FY11	FY12E	FY13E	FY14E
<b>Revenues</b>	<b>302,481</b>	<b>330,697</b>	<b>358,827</b>	<b>367,230</b>
y-o-y chg	24%	9%	9%	2%
<b>EBITDA</b>	<b>78,690</b>	<b>95,892</b>	<b>106,711</b>	<b>123,765</b>
Margins	26%	29%	30%	34%
- Copper Tuticorin	5,436	7,036	7,036	7,036
- Balco	10,374	5,255	5,329	5,110
- Zinc	57,693	53,583	59,145	69,620
- Power	0	4,368	7,261	6,970
- Anglo	5,010	14,939	15,717	21,426
- Silver	0	6,636	8,429	10,675
- Cu Mine/ Others	178	4,075	3,793	2,928
Depreciation	10,301	17,463	20,028	20,118
Interest (net)	3,012	5,630	8,281	8,195
Other Income	-26,528	-20,378	-24,611	-19,800
Tax	18,116	18,636	20,603	23,051
<b>PAT</b>	<b>73,789</b>	<b>74,541</b>	<b>82,410</b>	<b>92,201</b>
Minority Interest	-19,945	-18,223	-21,657	-24,542
Share of Associates	-2,850	-6,536	-5,761	-4,721
<b>PAT post minority</b>	<b>50,993</b>	<b>49,783</b>	<b>54,992</b>	<b>62,938</b>
YoY Change	26%	-2%	10%	14%
Exceptionals	-568	0	0	0
<b>Reported PAT</b>	<b>50,425</b>	<b>49,783</b>	<b>54,992</b>	<b>62,938</b>
EPS	15.2	14.8	16.4	18.7
YoY Change	26%	-2%	10%	14%
Shares o/s	3,362	3,362	3,362	3,362

Source: Sterlite, BofA Merrill Lynch Global Research Estimates

## iQprofile<sup>SM</sup> Sterlite Industries India Limited

Key Income Statement Data (Mar)	2010A	2011A	2012E	2013E	2014E
<b>(Rs Millions)</b>					
Sales	244,103	302,481	323,482	354,697	350,669
Gross Profit	60,718	78,690	97,583	107,945	109,703
Sell General & Admin Expense	NA	NA	NA	NA	NA
Operating Profit	53,220	68,389	82,252	91,332	93,781
Net Interest & Other Income	16,170	23,516	5,897	6,522	7,989
Associates	NA	NA	NA	NA	NA
Pretax Income	69,390	91,905	88,149	97,854	101,770
Tax (expense) / Benefit	(12,330)	(18,116)	(17,630)	(19,571)	(20,355)
Net Income (Adjusted)	40,407	50,993	50,777	59,150	62,333
Average Fully Diluted Shares Outstanding	3,362	3,362	3,362	3,362	3,362
<b>Key Cash Flow Statement Data</b>					
Net Income	40,407	50,993	50,777	59,150	62,333
Depreciation & Amortization	7,498	10,301	15,331	16,614	15,921
Change in Working Capital	(8,487)	(3,154)	15,381	(3,905)	(465)
Deferred Taxation Charge	NA	NA	NA	NA	NA
Other Adjustments, Net	2,405	406	41,093	42,797	41,782
Cash Flow from Operations	41,823	58,548	122,582	114,656	119,571
Capital Expenditure	(61,819)	(126,923)	(57,052)	(42,454)	(39,066)
(Acquisition) / Disposal of Investments	(36,725)	75,530	0	0	0
Other Cash Inflow / (Outflow)	(34,122)	(24,007)	(14,092)	(14,803)	(16,184)
Cash Flow from Investing	(132,667)	(75,400)	(71,143)	(57,257)	(55,250)
Shares Issue / (Repurchase)	76,529	(16)	0	0	0
Cost of Dividends Paid	(4,352)	(5,018)	(4,052)	(4,720)	(4,974)
Cash Flow from Financing	88,222	16,044	(12,247)	(13,001)	(13,169)
Free Cash Flow	(19,997)	(68,376)	65,531	72,201	80,505
Net Debt	59,222	18,163	(21,029)	(65,426)	(116,578)
Change in Net Debt	24,417	26,393	(39,192)	(44,397)	(51,152)
<b>Key Balance Sheet Data</b>					
Property, Plant & Equipment	232,745	334,720	376,441	402,281	425,426
Other Non-Current Assets	203,800	130,361	126,509	124,975	123,959
Trade Receivables	5,709	15,950	17,058	18,704	18,491
Cash & Equivalents	33,378	99,124	138,316	182,713	233,865
Other Current Assets	136,027	164,317	143,946	147,146	146,309
Total Assets	611,659	744,471	802,270	875,820	948,051
Long-Term Debt	92,600	117,287	117,287	117,287	117,287
Other Non-Current Liabilities	15,524	21,789	21,789	21,789	21,789
Short-Term Debt	0	0	0	0	0
Other Current Liabilities	49,319	88,128	83,311	84,833	81,639
Total Liabilities	157,443	227,204	222,387	223,909	220,715
Total Equity	454,216	517,268	579,883	651,911	727,337
Total Equity & Liabilities	611,659	744,471	802,270	875,820	948,051
<b>iQmethod<sup>SM</sup> - Bus Performance*</b>					
Return On Capital Employed	9.0%	9.0%	9.6%	9.7%	9.1%
Return On Equity	12.9%	13.0%	11.6%	12.1%	11.5%
Operating Margin	21.8%	22.6%	25.4%	25.7%	26.7%
EBITDA Margin	24.9%	26.0%	30.2%	30.4%	31.3%
<b>iQmethod<sup>SM</sup> - Quality of Earnings*</b>					
Cash Realization Ratio	1.0x	1.1x	2.4x	1.9x	1.9x
Asset Replacement Ratio	8.2x	12.3x	3.7x	2.6x	2.5x
Tax Rate (Reported)	17.8%	19.7%	20.0%	20.0%	20.0%
Net Debt-to-Equity Ratio	13.0%	3.5%	-3.6%	-10.0%	-16.0%
Interest Cover	15.5x	22.7x	10.0x	11.0x	11.4x
<b>Key Metrics</b>					

**Table 15: Key assumptions and forecasts**

	FY11	FY12E	FY13E	FY14E
<b>Capacity (kt)</b>				
Aluminum	515	515	932	932
Alumina	1,539	1,539	3,039	3,039
Cu TCRC	500	500	500	500
<b>Volumes (kt)</b>				
Aluminum	542	562	660	830
Alumina	375	364	333	885
TCRC	339.7	322.5	318.2	318.2

Source: Hindalco, BofA Merrill Lynch Global Research Estimates

\*\* Capacity refers to the year end capacity.

## Hindalco

### Hindalco – Key assumption and forecasts

**Table 16: Summarized earnings estimate changes**

in mn Rs.	FY12E			FY13E			FY14E		
	Old	New	%chg	Old	New	%chg	Old	New	%chg
<b>Turnover</b>	757,826	752,064	-1%	827,972	784,628	-5%	874,344	822,633	-6%
<b>EBITDA</b>	85,255	85,181	0%	94,285	88,991	-6%	108,572	103,875	-4%
EBITDA Margin	11%	11%	1%	11%	11%	0%	12%	13%	2%
Depreciation	28,414	28,414	0%	32,521	32,521	0%	37,220	37,220	0%
<b>EBIT</b>	56,841	56,768	0%	61,765	56,470	-9%	71,352	66,655	-7%
Interest	15,656	16,677	7%	19,795	20,542	4%	24,837	24,837	0%
Other Income	3,062	4,300	40%	3,062	4,300	40%	3,062	4,300	40%
Profit bef Tax	44,247	44,391	0%	45,032	40,228	-11%	49,578	46,118	-7%
<b>Net Profit</b>	29,646	30,630	3%	30,171	27,757	-8%	33,217	31,821	-4%
Net Profit after Minority Interest	28,748	29,534	3%	29,292	27,414	-6%	33,412	32,135	-4%
<b>EPS</b>	15.0	15.4	3%	15.3	14.3	-6%	17.5	16.8	-4%
<b>Volumes</b>									
Aluminum (kt)	562	562	0%	660	660	0%	830	830	0%
Alumina (kt)	364	364	0%	370	333	-10%	903	885	-2%
<b>LME</b>									
Aluminum LME (US\$/t)	2,317	2,247	-3%	2,588	2,313	-11%	2,688	2,463	-8%
Copper LME (US\$/t)	7,936	8,124	2%	8,375	7,814	-7%	7,250	7,127	-2%

Source: Hindalco, BofA Merrill Lynch Global Research Estimates

**Table 17: Consolidated Earnings Outlook**

in mn Rs.	FY11A	FY12E	FY13E	FY14E
<b>Turnover</b>	720,779	752,064	784,628	822,633
<b>EBITDA</b>	82,927	85,181	88,991	103,875
% chg	21%	3%	4%	17%
- Aluminum, India	26,047	23,128	27,486	44,387
- Cu Smelter	6,027	6,178	6,129	5,753
- Novelis	48,240	53,235	54,270	53,970
-Cu Mines	4,861	2,640	1,105	-235
- Others/Miscellaneous	-2,248	0	0	0
<b>Depreciation</b>	27,500	28,414	32,521	37,220
<b>EBIT</b>	55,427	56,768	56,470	66,655
% chg	37%	2%	-1%	18%
Interest	19,974	16,677	20,542	24,837
Profit bef Other Income	35,453	40,091	35,928	41,818
Other Income	4308.5	4300	4300	4300
Profit bef Tax	39,762	44,391	40,228	46,118
Tax	9638	13761	12471	14297
Tax rate	24%	31%	31%	31%
<b>Profit after Tax</b>	30,123	30,630	27,757	31,821
% chg	52%	2%	-9%	15%
Minority Interest	3659	524	-228	-884
Sh. of profit of associates	-571.1	-571.1	-571.1	-571.1
<b>Net Profit</b>	25,894	29,534	27,414	32,135
% chg	66%	14%	-7%	17%
Extraordinary Income / (Exp)	-1329.9	0	0	0
Profit after extraordinaries	24,564	29,534	27,414	32,135
% chg	-37%	20%	-7%	17%
<b>EPS (Rs)</b>	13.5	15.4	14.3	16.8
<b>Growth</b>	66%	14%	-7%	17%

Source: Hindalco, BofA Merrill Lynch Global Research Estimates



## iQprofile<sup>SM</sup> Hindalco

Key Income Statement Data (Mar)	2010A	2011A	2012E	2013E	2014E
<b>(Rs Millions)</b>					
Sales	607,221	720,779	757,826	827,972	874,344
Gross Profit	68,317	82,927	85,255	94,285	108,572
Sell General & Admin Expense	NA	NA	NA	NA	NA
Operating Profit	40,481	55,427	56,841	61,765	71,352
Net Interest & Other Income	(10,831)	(15,094)	(12,022)	(16,162)	(21,204)
Associates	(27)	(571)	(571)	(571)	(571)
Pretax Income	29,623	39,762	44,247	45,032	49,578
Tax (expense) / Benefit	(9,742)	(9,638)	(14,602)	(14,860)	(16,361)
Net Income (Adjusted)	15,617	25,894	28,748	29,292	33,412
Average Fully Diluted Shares Outstanding	1,913	1,913	1,913	1,913	1,913
<b>Key Cash Flow Statement Data</b>					
Net Income	15,617	25,894	28,748	29,292	33,412
Depreciation & Amortization	27,836	27,500	28,414	32,521	37,220
Change in Working Capital	(21,575)	(7,680)	311	(3,437)	(2,272)
Deferred Taxation Charge	0	0	(1)	NA	0
Other Adjustments, Net	23,638	(1,330)	1	0	0
Cash Flow from Operations	45,516	44,383	57,472	58,376	68,360
Capital Expenditure	(26,772)	(149,181)	(90,598)	(47,370)	(29,627)
(Acquisition) / Disposal of Investments	7,028	14,334	0	0	0
Other Cash Inflow / (Outflow)	NA	NA	NA	NA	NA
Cash Flow from Investing	(19,744)	(134,848)	(90,598)	(47,370)	(29,627)
Shares Issue / (Repurchase)	214	0	0	0	0
Cost of Dividends Paid	(6,276)	(3,927)	(4,596)	(4,349)	(4,960)
Cash Flow from Financing	(9,139)	90,166	59,150	29,118	15,012
Free Cash Flow	18,744	(104,798)	(33,126)	11,006	38,734
Net Debt	158,997	196,228	233,622	226,658	193,651
Change in Net Debt	(59,744)	37,231	37,395	(6,965)	(33,007)
<b>Key Balance Sheet Data</b>					
Property, Plant & Equipment	303,680	425,361	487,545	502,395	494,801
Other Non-Current Assets	97,753	83,419	83,419	83,419	83,419
Trade Receivables	NA	NA	NA	NA	NA
Cash & Equivalents	80,990	80,692	106,716	146,840	200,585
Other Current Assets	29,764	37,445	37,133	40,571	42,843
Total Assets	512,187	626,917	714,814	773,224	821,648
Long-Term Debt	239,987	276,920	340,338	373,497	394,236
Other Non-Current Liabilities	39,382	37,596	37,596	37,596	37,596
Short-Term Debt	NA	NA	NA	NA	NA
Other Current Liabilities	0	0	0	1	4
Total Liabilities	279,369	314,516	377,934	411,094	431,836
Total Equity	232,818	312,401	336,880	362,131	389,817
Total Equity & Liabilities	512,187	626,917	714,814	773,225	821,652
<b>iQmethod<sup>SM</sup> - Bus Performance*</b>					
Return On Capital Employed	5.5%	7.4%	5.7%	5.6%	6.0%
Return On Equity	8.4%	10.2%	9.5%	9.0%	9.5%
Operating Margin	6.7%	7.7%	7.5%	7.5%	8.2%
EBITDA Margin	11.3%	11.5%	11.2%	11.4%	12.4%
<b>iQmethod<sup>SM</sup> - Quality of Earnings*</b>					
Cash Realization Ratio	2.9x	1.7x	2.0x	2.0x	2.0x
Asset Replacement Ratio	1.0x	5.4x	3.2x	1.5x	0.8x
Tax Rate (Reported)	32.9%	24.2%	33.0%	33.0%	33.0%
Net Debt-to-Equity Ratio	68.3%	62.8%	69.3%	62.6%	49.7%
Interest Cover	2.9x	2.8x	3.6x	3.1x	2.9x
<b>Key Metrics</b>					

## Nalco

### Nalco – Key assumption and forecasts

Table 18: Summary of assumption changes

in mn Rs.	FY12E			FY13E			FY14E		
	Old	New	%chg	Old	New	%chg	Old	New	%chg
Turnover	60209	59881	-1%	73135	69137	-5%	76375	71931	-6%
EBITDA	13570	13313	-2%	17279	14569	-16%	18648	15545	-17%
EBITDA Margin	22.5%	22.2%		23.6%	21.1%		24%	21.6%	
Profit bef Tax	13856	13598	-2%	17305	14595	-16%	18773	15671	-17%
Tax	4157	4079	-2%	5711	4816	-16%	6195	5171	-17%
Net Profit	9699	9519	-2%	11594	9778	-16%	12578	10499	-17%
EPS	3.8	3.7	-2%	4.5	3.8	-16%	4.9	4.1	-17%
LME									
Al LME (US\$/t)	2317	2297	-1%	2588	2313	-11%	2688	2463	-8%
Alumina (US\$/t)	348	345	-1%	388	347	-11%	403	369	-8%
Volumes									
Aluminum (Kt)	423	423	0%	440	440	0%	440	440	0%
Alumina (Kt)	834	834	0%	1080	1080	0%	1164	1164	0%

Source: Nalco, BofA Merrill Lynch Global Research Estimates

Table 19: Summary Earnings Outlook

in mn Rs.	FY11	FY12E	FY13E	FY14E
Turnover	60558	59881	69137	71931
EBITDA	15848	13313	14569	15545
% chg	40%	-16%	9%	7%
EBITDA Margin	26%	22%	21%	22%
Depreciation	4217	4775	5115	5275
EBIT	11630	8538	9455	10271
% chg	43%	-27%	11%	9%
Interest	1	0	0	0
Other Income	3617	5060	5140	5400
Profit bef Tax	15246	13598	14595	15671
Tax	4554	4079	4816	5171
Tax rate	33%	30%	33%	33%
Net Profit	10692	9519	9778	10499
% chg	28%	-11%	3%	7%
Profit after extra ordinaries	10692	9519	9778	10499
% chg	28%	-11%	3%	7%
EPS (Rs)	4.1	3.7	3.8	4.1
Growth	28%	-11%	3%	7%

Source: Nalco, BofA Merrill Lynch Global Research Estimates

**iQprofile<sup>SM</sup> NALCO**

Key Income Statement Data (Mar)	2010A	2011A	2012E	2013E	2014E
<b>(Rs Millions)</b>					
Sales	51,443	60,558	60,209	73,135	76,375
Gross Profit	17,343	22,554	20,566	25,658	27,307
Sell General & Admin Expense	(6,018)	(6,707)	(6,996)	(8,378)	(8,659)
Operating Profit	8,137	11,630	8,796	12,165	13,373
Net Interest & Other Income	3,804	3,616	5,060	5,140	5,400
Associates	NA	NA	NA	NA	NA
Pretax Income	11,941	15,246	13,856	17,305	18,773
Tax (expense) / Benefit	(3,615)	(4,554)	(4,157)	(5,711)	(6,195)
Net Income (Adjusted)	8,326	10,692	9,699	11,594	12,578
Average Fully Diluted Shares Outstanding	2,577	2,577	2,577	2,577	2,577
<b>Key Cash Flow Statement Data</b>					
Net Income	8,326	10,692	9,699	11,594	12,578
Depreciation & Amortization	3,188	4,217	4,775	5,115	5,275
Change in Working Capital	(792)	3,284	2,917	3,874	518
Deferred Taxation Charge	NA	NA	NA	NA	NA
Other Adjustments, Net	392	329	0	0	0
Cash Flow from Operations	11,114	18,522	17,391	20,583	18,371
Capital Expenditure	(5,305)	(5,791)	(16,209)	(6,500)	(1,500)
(Acquisition) / Disposal of Investments	(908)	(3,449)	0	0	0
Other Cash Inflow / (Outflow)	0	0	0	0	0
Cash Flow from Investing	(6,213)	(9,240)	(16,209)	(6,500)	(1,500)
Shares Issue / (Repurchase)	NA	NA	NA	NA	NA
Cost of Dividends Paid	(1,948)	(2,502)	(2,270)	(2,713)	(2,943)
Cash Flow from Financing	(1,948)	(2,353)	(2,418)	(2,713)	(2,943)
Free Cash Flow	5,810	12,731	1,181	14,083	16,871
Net Debt	(31,524)	(37,804)	(36,715)	(48,085)	(62,013)
Change in Net Debt	(2,953)	(6,780)	1,088	(11,370)	(13,928)
<b>Key Balance Sheet Data</b>					
Property, Plant & Equipment	70,797	72,371	83,805	85,191	81,416
Other Non-Current Assets	9,868	13,317	13,317	13,317	13,317
Trade Receivables	20,573	22,499	19,869	21,941	22,912
Cash & Equivalents	31,524	37,952	36,715	48,085	62,013
Other Current Assets	NA	NA	NA	NA	NA
Total Assets	132,761	146,139	153,706	168,533	179,658
Long-Term Debt	0	149	0	0	0
Other Non-Current Liabilities	6,606	6,935	6,935	6,935	6,935
Short-Term Debt	NA	NA	NA	NA	NA
Other Current Liabilities	22,199	27,410	27,696	33,642	35,132
Total Liabilities	28,805	34,493	34,631	40,577	42,067
Total Equity	103,956	111,646	119,075	127,957	137,591
Total Equity & Liabilities	132,761	146,139	153,706	168,533	179,658
<b>iQmethod<sup>SM</sup> - Bus Performance*</b>					
Return On Capital Employed	7.8%	9.3%	7.9%	8.9%	9.0%
Return On Equity	8.3%	9.9%	8.4%	9.4%	9.5%
Operating Margin	15.8%	19.2%	14.6%	16.6%	17.5%
EBITDA Margin	22.0%	26.2%	22.5%	23.6%	24.4%
<b>iQmethod<sup>SM</sup> - Quality of Earnings*</b>					
Cash Realization Ratio	1.3x	1.7x	1.8x	1.8x	1.5x
Asset Replacement Ratio	1.7x	1.4x	3.4x	1.3x	0.3x
Tax Rate (Reported)	30.3%	29.9%	30.0%	33.0%	33.0%
Net Debt-to-Equity Ratio	-30.3%	-33.9%	-30.8%	-37.6%	-45.1%
Interest Cover	NM	NM	NA	NA	NA
<b>Key Metrics</b>					

## Price objective basis & risk

### **Hindalco (HNDF)**

Our PO of Rs136 is based on our DCF valuation. We assume a WACC of 12.5% and perpetuity growth of 0%. Our DCF currently assumes aluminum prices of US\$2247/t in FY12E, US\$2313/t in FY13E and a long-term price of US\$2381/t. At our PO, the stock would trade at 0.8x P/B and 6.0x FY12E EBITDA (5.8x FY13E EBITDA).

Upside risks: Higher aluminum prices due to stronger demand and production cuts in aluminum. Also, stronger margin gains in Novelis. Downside risks: Lower aluminum prices, execution risks and delays in capacity expansion, weaker margins in Novelis.

### **NALCO (NAUDF)**

Our PO of Rs49 is based on our DCF valuation. We assume a WACC of 12.5% and perpetuity growth of 0%. Our DCF currently assumes aluminum prices of US\$2247/t in FY12E, US\$2313/t in FY13E and a long-term price of US\$2381/t. At our PO, the stock will trade at a 1.1xP/B.

Upside risks: Higher aluminum and alumina prices due to a recovery in demand, production cuts in aluminum. Downside risks: Lower aluminum prices, execution risks and delays in capacity expansions.

### **Sterlite Industries India Limited (XTNDF)**

Our PO of Rs142 (US\$11.41) is based on a SOTP valuation of Sterlite's metals and power businesses. Our PO implies Rs122 for the metals business and Rs20 for the power business. At our PO, Sterlite would trade at 8.7x FY13E EPS and 4.1x FY13E EBITDA.

Our NPV for the metals business is Rs122/share, based on WACC of 12.5% and perpetuity growth of 0%. We forecast a long-term zinc price of US\$2072/t and a long-term aluminum price of US\$2,381/ton.

Our valuation of the power business implies Rs20 for Sterlite Energy (including Rs1 for the Talwandi Sabo project).

Upside risks: Higher-than-forecast metal prices and higher-than-forecast power capacity over the next two years. Downside risks: Lower metals prices, delays in expansions, lower PLF and higher costs at SEL due to coal shortages, VAL BS stress and an increase in the VAL stake.

## Link to Definitions

### **Basic Materials**

Click [here](#) for definitions of commonly used terms.

## Analyst Certification

I, Bhaskar N Basu, CFA, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

## Special Disclosures

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BofA Merrill Lynch is currently acting as Financial Adviser to Cairn Energy in connection with its proposed sale of 51% of Cairn India to Vedanta Resources, which was announced on 16th August 2010.

### APR - Metals & Mining Coverage Cluster

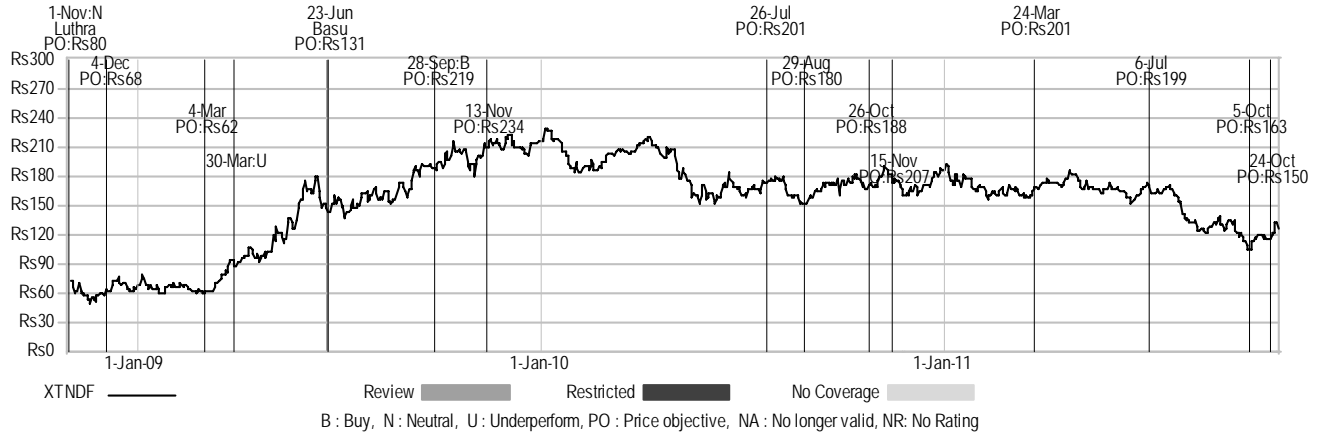
Investment rating	Company	BofA Merrill Lynch ticker	Bloomberg symbol	Analyst
BUY	Banpu Pcl	BPULF	BANPU TB	Komsun Suksumrun
	Baosteel	BAOSF	600019 CH	Yongtao Shi
	China Coal Energy Ltd.	CCOZF	1898 HK	Yongtao Shi
	China Hongqiao	XCGQF	1378 HK	Bruce Wang
	China National Building Material Co Ltd.	CBUMF	3323 HK	Yongtao Shi
	China National Materials	XFCHF	1893 HK	Yongtao Shi
	China Resources Cement	CJRCF	1313 HK	Po Wei
	China Shanshui Cement	CCGLF	691 HK	Po Wei
	China Shenhua Energy Ltd.	CUAEF	1088 HK	Yongtao Shi
	CITIC Dameng Holdings Limited	XCDHF	1091 HK	Yongtao Shi
	Fushan International Energy	YULKF	639 HK	Yongtao Shi
	Hidili	XHILF	1393 HK	Yongtao Shi
	Hyundai Steel	XHDUF	004020 KS	Elli Lee
	Indo Tambangraya	PTIZF	ITMG IJ	Daisy Suryo
	Jiangxi Copper	JIAXF	358 HK	Yongtao Shi
	POSCO	PKXFF	005490 KS	Elli Lee
	POSCO -A	PKX	PKX US	Elli Lee
	PT Adaro Energy Tbk	PADEF	ADRO IJ	Daisy Suryo
	Sterlite Industries India Limited	XTNDF	STLT IN	Bhaskar N Basu, CFA
	Sterlite Industries India Limited	SLT	SLT US	Bhaskar N Basu, CFA
	Straits Asia Resources Limited	SSGDF	SAR SP	Daisy Suryo
	Winsway Coking Coal Holdings Limited	XWNYF	1733 HK	Yongtao Shi
	Yanzhou Coal	YZCHF	1171 HK	Yongtao Shi
	Zijin Mining Group Co Ltd.	ZIJMF	2899 HK	Timothy Bush

**APR - Metals & Mining Coverage Cluster**

Investment rating	Company	BofA Merrill Lynch ticker	Bloomberg symbol	Analyst
<b>NEUTRAL</b>				
	Aluminum Corp. of China	ALMMF	2600 HK	Bruce Wang
	Anhui Conch-H	AHCHF	914 HK	Yongtao Shi
	Borneo Lumbung Energy	PBTLF	BORN IJ	Daisy Suryo
	Coal India Limited	XOXCF	COAL IN	Bhaskar N Basu, CFA
	Hindalco	HNDFF	HNDL IN	Bhaskar N Basu, CFA
	Hyundai Hysco	HYUPF	010520 KS	Elli Lee
	Shougang Concord International	SCGEF	697 HK	Yongtao Shi
	Tambang Batubara	PBATF	PTBA IJ	Daisy Suryo
	Zhaojin Mining Industry Company Limited	ZHAOF	1818 HK	Timothy Bush
<b>UNDERPERFORM</b>				
	Angang Steel	ANGGF	347 HK	Yongtao Shi
	Bumi Resources	PBMRF	BUMI IJ	Daisy Suryo
	Dongkuk Steel	DKUSF	001230 KS	Elli Lee
	Intl Nickel In	PTNDF	INCO IJ	Daisy Suryo
	Jindal Steel and Power Limited	XJDLF	JSP IN	Bhaskar N Basu, CFA
	JSW Steel	XJWJF	JSTL IN	Bhaskar N Basu, CFA
	Maanshan Iron & Steel	MAANF	323 HK	Yongtao Shi
	NALCO	NAUDF	NACL IN	Bhaskar N Basu, CFA
	PT Bayan Resources Tbk	XBAYF	BYAN IJ	Daisy Suryo
	PT Indika Energy Tbk	XIDKF	INDY IJ	Daisy Suryo
	Sesa Goa Limited	XSGAF	SESA IN	Bhaskar N Basu, CFA
	Steel Authority of India	SLAUF	SAIL IN	Bhaskar N Basu, CFA
	Tata Steel	TAELF	TATA IN	Bhaskar N Basu, CFA
<b>RVW</b>				
	Aneka Tambang	XANEF	ANTM IJ	Daisy Suryo
	Medco Energi III	PTGIF	MEDC IJ	Daisy Suryo

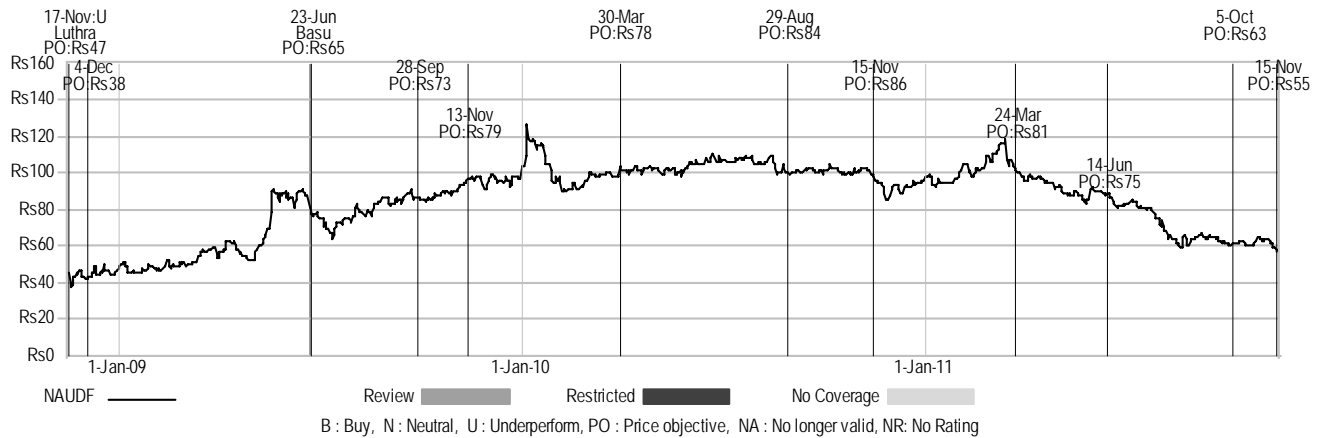
## Important Disclosures

### XTNDF Price Chart



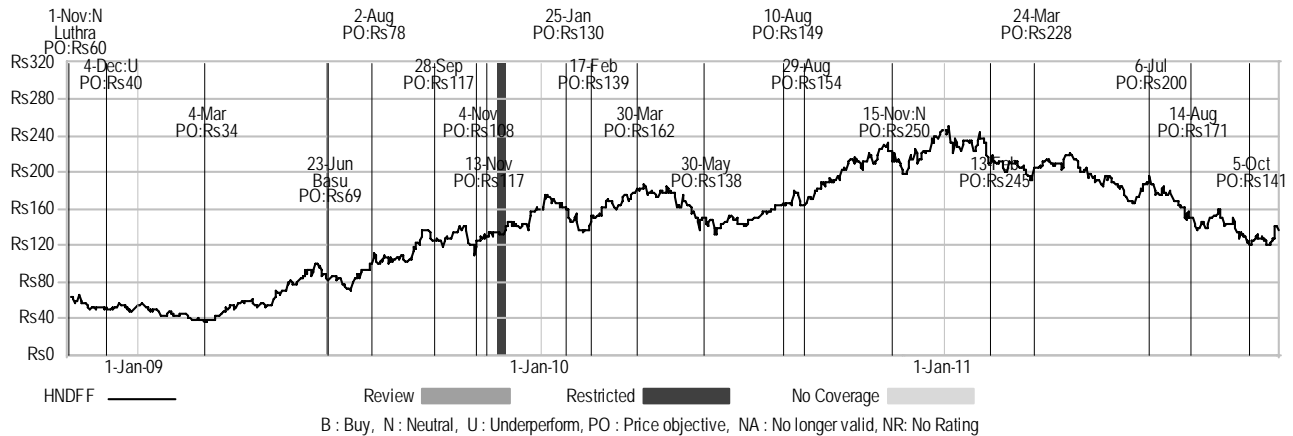
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### NAUDF Price Chart



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### HNDF Price Chart



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Investment Rating Distribution: Non-Ferrous Metals/Mining & Minerals Group (as of 01 Oct 2011)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	117	66.86%	Buy	41	39.42%
Neutral	33	18.86%	Neutral	12	38.71%
Sell	25	14.29%	Sell	2	9.09%

Investment Rating Distribution: Global Group (as of 01 Oct 2011)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	2073	54.13%	Buy	923	49.12%
Neutral	961	25.09%	Neutral	460	52.57%
Sell	796	20.78%	Sell	287	38.32%

\* Companies in respect of which BofA Merrill Lynch or one of its affiliates has received compensation for investment banking services within the past 12 months. For purposes of this distribution, a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
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Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

\* Ratings dispersions may vary from time to time where BofA Merrill Lynch Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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