

**COMPANY QUICK COMMENT**

**Takeaways from our call with CIL's management on non-executive wage revision: [1] Meeting on Sep 22-23 concluded by CIL asking the trade unions to present a common set of demands [2] There is disagreement over the quantum of festival-related bonus/ex-gratia for FY12 [3] Next meeting likely post the festive period in October. Earnings sensitivity – one-day labor strike can lead to production loss of 1-1.2mt and if the demand for higher bonus is met, FY12F employee cost would be higher by 1.7%; combined impact on FY12F EPS would be ~2%. Maintain Buy; wage revision remains a near-term overhang.**

Price target: 433.0 INR

Price (23 Sep 2011): 365.6 INR

Research analyst: Anirudh Gangahar

+91 22 4037 4516

anirudh.gangahar@nomura.com

Research analyst: Nishit Jalan

+91 22 4037 4362

nishit.jalan@nomura.com

Research analyst: Ivan Lee, CFA

+852 2252 6213

ivan.lee@nomura.com

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**Wage revision – negotiation to resume post October festivities****Event**

We had a call with the Coal India (CIL) management to assess the progress on negotiations relating to non-executive wage revision and on news reports suggesting the labor force would be going on a country-wide strike on October 10, 2011 following the breakdown of negotiations with the trade unions on bonus/ex-gratia/coverage for contract workers for 2011.

As per media reports (Press Trust of India, Business Line) on September 23/24, 2011, the labor unions demanded Rs25,000/laborer as productivity-linked bonus (or ex-gratia) whereas CIL has promised a bonus of to Rs17,000/laborer (up YoY from Rs15,000/laborer). As per CIL, the promised increase in bonus would raise total outgo on bonus from Rs5.6bn to Rs6.2bn.

**ANALYSIS****Wage revision negotiations – where do things stand?**

As per our conversation with the CIL management on outcome of the September 22-23, 2011 meeting with the trade unions on wage revision, we gather – [1] Meeting broadly concluded by CIL asking the five trade unions to present a common charter of demands / expectations, [2] There was disagreement over the quantum of festival-linked bonus/ex-gratia for FY2012 (as highlighted by the news reports on this issue), [3] Next meeting is likely to be scheduled after the festive season in October (i.e. potentially in October-end / November).

**Bonus/ex-gratia payment – how material is the amount involved?**

Based on the data available as per the news reports, the festival-linked bonus/ex-gratia accounted for ~3% of CIL's overall employee cost in FY11; CIL's promise to raise the per laborer bonus/ex-gratia from Rs15,000/- to Rs17,000/- would imply a 11.5% YoY rise in this salary component to Rs6.2bn (~3% of our FY12F total employee cost) for CIL. If CIL management agrees to the union's demand for Rs25,000/- bonus/ex-gratia per laborer, ceteris paribus, our FY12F the incremental employee cost would rise by 1.7%.

**Wage revision – sensitivity to earnings**

Our earnings forecast for CIL builds-in [1] A 30% wage would increase for non-executive workers (effective July 2011), which translates into 19% / 9% YoY rise in employee cost in FY12 / FY13 respectively, [2] FY12 production/offtake at 447.5mt and 452.8mt. If the reported strike on October 10 takes place, it would lead to a loss of 1-1.2mn tons of coal production. Ceteris paribus, the potential production loss together with 1.7% increase in FY12F employee cost (if labor demand for higher bonus is met), would lower our FY12F EPS forecast by ~2%.

**IMPLICATIONS**

[1] Although the potential impact of the debated bonus/ex-gratia component is not very significant, we expect the impending wage negotiations (and related threat of potential production/offtake disruption) to remain an overhang on the near-term stock price performance.

Instead, we focus on CIL's capacity to make-up for the shortfall in 1HFY12 production/offtake (following the sharper-than-expected monsoon-related slowdown in production / dispatches) and the magnitude of wage revision as bigger downside risks

to our FY12F/13F earnings forecast for the company.

### Exhibit 1: Coal India – Sensitivity Analysis

| Impact on EPS of 1% rise in          | FY12F | FY13F | FY14F |
|--------------------------------------|-------|-------|-------|
| Volumes                              | 1.6%  | 1.7%  | 1.7%  |
| Offtake                              | 2.9%  | 2.5%  | 2.5%  |
| Blended ASP                          | 3.3%  | 2.8%  | 2.8%  |
| E-auction coal as % of raw coal sold | 2.4%  | 2.3%  | 2.4%  |
| Employee cost                        | -1.1% | -1.0% | -1.0% |
| Realization of e-auction coal        | 0.5%  | 0.5%  | 0.5%  |
| Realization of washed coal           | 0.2%  | 0.2%  | 0.2%  |

Source: Nomura research

Maintain BUY as the structural growth story remains intact. Stock trades at FY12F EV/Resource and EV/reserve of 2x and 0.6x respectively.

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| Issuer name | Ticker  | Price     | Price date  | Stock rating | Disclosures |
|-------------|---------|-----------|-------------|--------------|-------------|
| Coal India  | COAL IN | 365.6 INR | 23 Sep 2011 | Buy          |             |

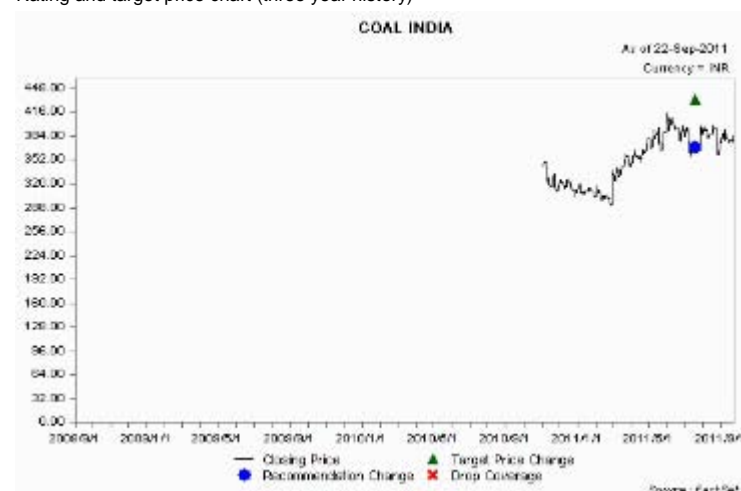
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| Issuer name | Previous Rating | Date of change |
|-------------|-----------------|----------------|
| Coal India  | Not Rated       | 18 Jul 2011    |

### Coal India (COAL IN)

365.6 INR (23 Sep 2011) Buy

Rating and target price chart (three year history)



| Date        | Rating | Target price | Closing price |
|-------------|--------|--------------|---------------|
| 18-Jul-2011 |        | 433.00       | 368.85        |
| 18-Jul-2011 | Buy    |              | 368.85        |

**Valuation Methodology** We arrive at our Rs433/share 12-mth target price for CIL using a sum-of-the-parts of [1] FCFF-based methodology to value the cash flows from its 10.6bn tons of proven reserves, and [2] EV/ton based value of CIL's probable reserves (8.3bn tons) and remaining resources (45.5bn tons) as per the JORC Code.

**Risks that may impede the achievement of the target price** Key risks: 1) Regulatory uncertainty particularly around pricing flexibility, environmental/forest clearance and restriction on e-auction coal sales; 2) lower-than-expected coal despatch due to lower rake availability; 3) delays in land acquisition/possession; and 4) wage revision of non-executives is higher than our expectation of a 30% increase.

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**Nomura Structured Finance Services Private Limited, India**

Tel: 91 22 3053 2345

Nomura, 9th Flr, Hiranandani Business Park  
Powai, Mumbai – 400076, INDIA

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