

Hindustan Zinc Ltd - BUY

CMP Rs626, Target Rs776

Sector: Metals & Mining

Sensex:	14,523
CMP (Rs):	626
Target price (Rs):	776
Upside (%):	23.9
52 Week h/l (Rs):	696 / 215
Market cap (Rscr) :	26,438
6m Avg vol ('000Nos):	198
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 17 Jun, 2009

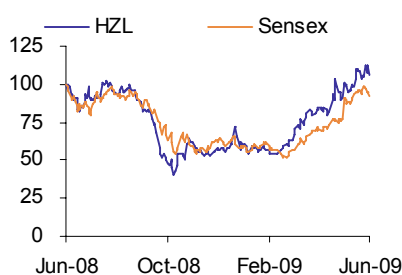
Shareholding pattern

March '09	(%)
Promoters	64.9
Institutions	32.9
Non promoter corp hold	0.7
Public & others	1.5

Performance rel. to sensx

(%)	1m	3m	1yr
HZL	(2.6)	2.9	13.0
Sterlite	11.5	41.8	(17.7)
Hindalco	13.6	50.3	(33.0)
NALCO	9.3	(8.2)	(16.4)

Share price trend



Upgrading zinc and lead price estimates

Zinc prices during the month rose to a high of US\$1,700/ton, levels last seen trading in Sept '08. Zinc prices have been moving higher since it formed a base around the US\$1,000-1,100/ton levels at the start of the year. The stronger than expected resilience shown by the Chinese economy, implementation of huge production cuts and buying by the Chinese Strategic Reserve Bureau (SRB) led to a surge in imports. China imported 0.4mn tons of zinc metal YTD, higher than that imported in the full year of 2008. With the zinc market remaining in depression much longer than most of the other base metals, production cuts (< 1mn tons) have been quite steep.

We believe that prices would stay higher than the bottom formed on account of an increase in demand from the steel industry. Idle capacities globally will continue to remain an overhang and keep a check on prices. We upgrade our zinc price estimate to US\$1,300 for FY10E and US\$1,500 for FY11E.

Volumes to witness 21.4% CAGR over FY09-11E

Hindustan Zinc Ltd (HZL) is set to become the world's largest integrated zinc-lead producer by FY11E. We expect volumes to witness 23.1% CAGR over the period FY09-11. While the volume growth in FY10E would be achieved by the recent de-bottlenecking process, in FY11E it would come from the expansion of production capacity to 1mtpa (by mid-2010). On our revised metal price assumption, we upgrade HZL's topline by 17.2% in FY10E and 17.1% in FY11E.

Upgrade to BUY with a target price of Rs776

HZL falls in the lower quartile of the global cost curve. Even in an environment of high input costs like coal in FY09, the company managed to keep its costs at FY08 levels. With HZL's ability to contain input costs and a scenario of rising price realisations, we expect OPM to expand 309bps over the next two years. We upgrade our previous earnings by 16.2% to Rs26.8bn in FY10E and by 8.7% to Rs34.2bn. We expect net cash per share to rise from Rs236 at the end of FY09 to Rs290 by FY11. We upgrade our target price to Rs776/share and change our rating to BUY from Market Performer. Net of cash, the stock is currently trading at 4.2x P/E on our estimated FY11E EPS of Rs80.9.

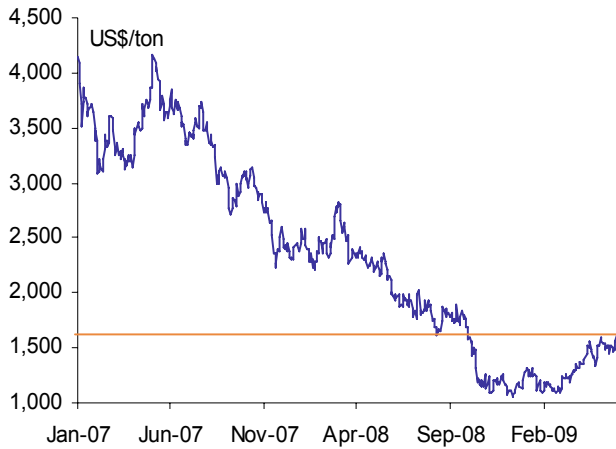
Valuation summary

Y/e 31 Mar	FY08A	FY09E	FY10E	FY11E
Revenues (Rs m)	78,778	58,220	60,318	78,772
yoy growth (%)	(8.0)	(26.1)	3.6	30.6
Operating Profit	53,784	28,759	30,119	41,347
OPM (%)	68.3	49.4	49.9	52.5
Reported PAT (Rs m)	43,961	27,273	26,809	34,185
yoy growth (%)	(1.0)	(38.0)	(1.7)	27.5
EPS (Rs)	104.0	64.5	63.4	80.9
P/E (x)	6.0	9.7	9.9	7.7
Price/Book (x)	2.2	1.8	1.6	1.3
EV/EBITDA (x)	4.7	7.9	7.1	5.0
RoE (%)	45.1	20.8	17.3	18.7
RoCE (%)	59.4	24.8	21.1	23.0

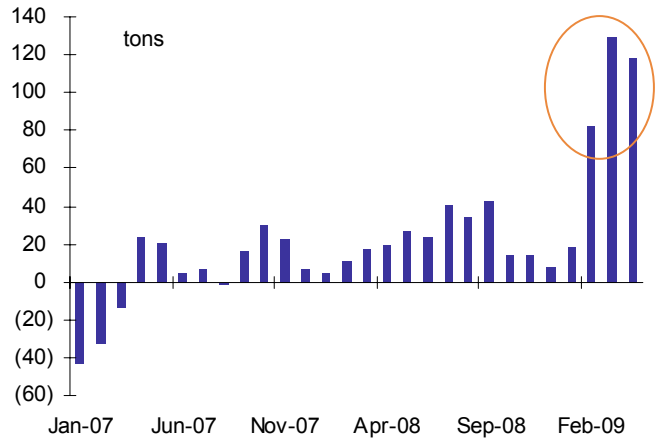
Source: Company, India Infoline Research

Zinc market key indicators

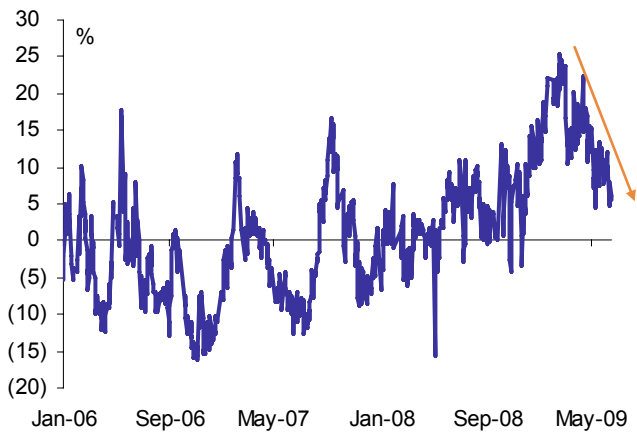
Zinc prices at eight month high, up ~38% YTD



Rally in metal prices has been led by a surge in Chinese metal imports



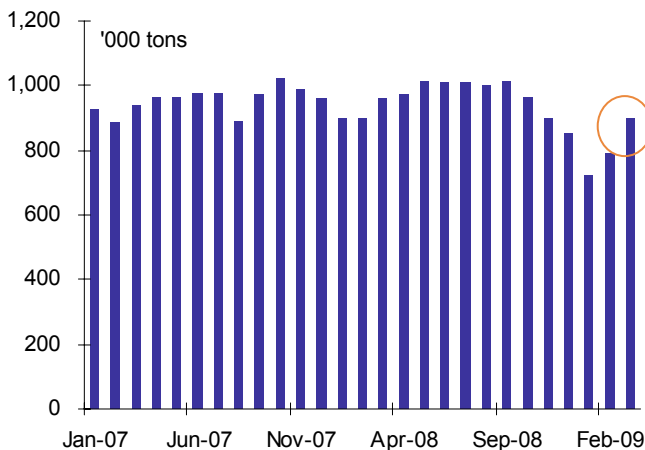
Surge in imports led to reduction in premium of SHFE prices over LME prices



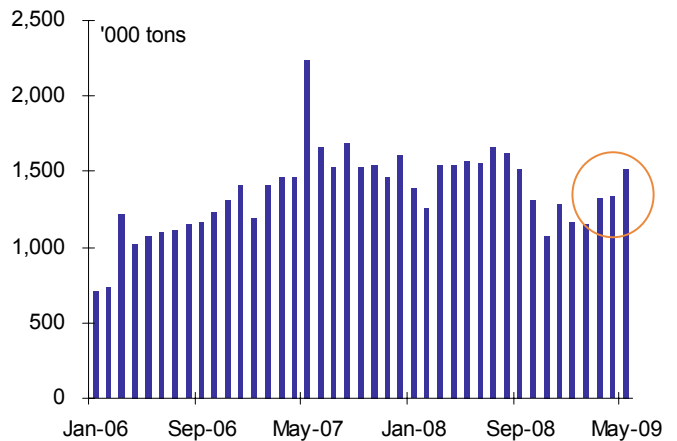
The depreciation of the US dollar has also boosted zinc prices in the recent past



Demand for the metal has picked up in March as galvanized steel producers have increased their consumption

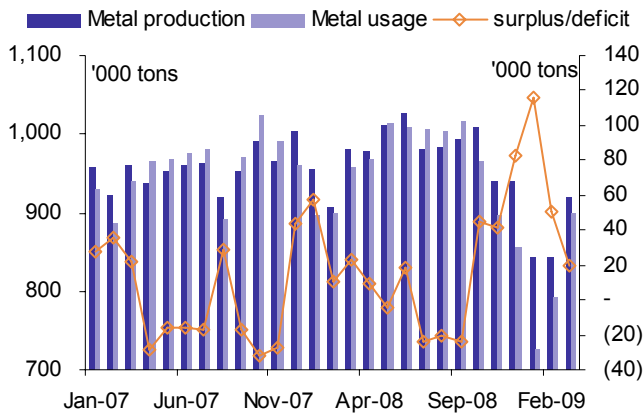


Galvanized steel production in China jumped 14% mom in May, the highest level in the last nine months

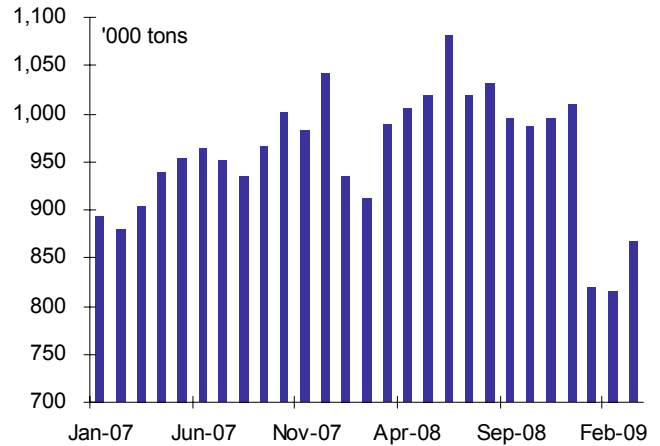


Source: Bloomberg, International Lead and Zinc Study Group (ILZSG)

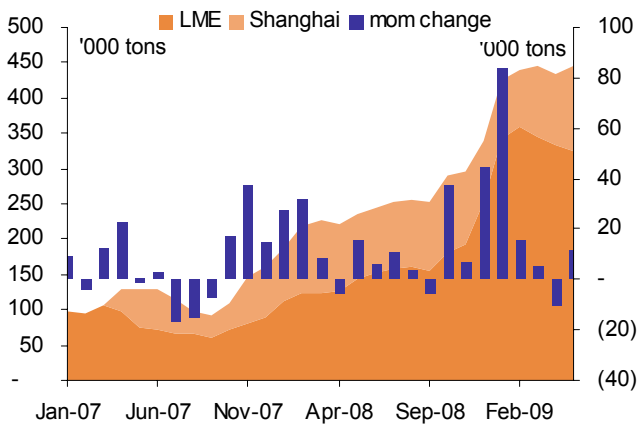
Markets moving towards a balanced state due to huge production cuts implemented in the past six months



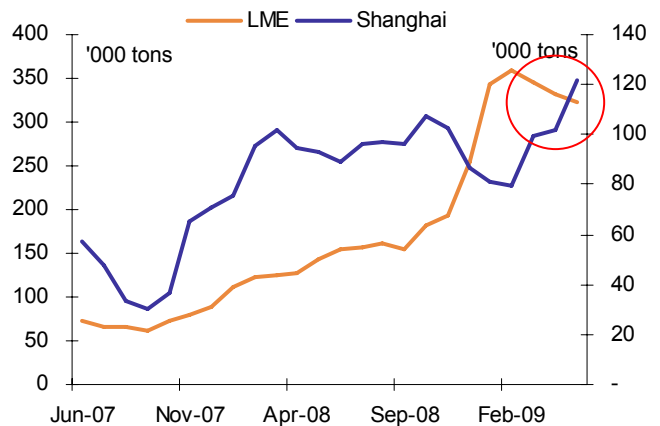
Mine production fell to its 2-1/2 year low in Jan & Feb '09



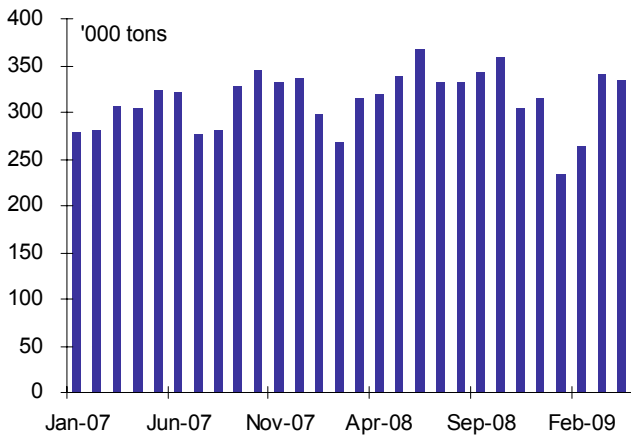
Global inventory levels have remained stable in the last three months



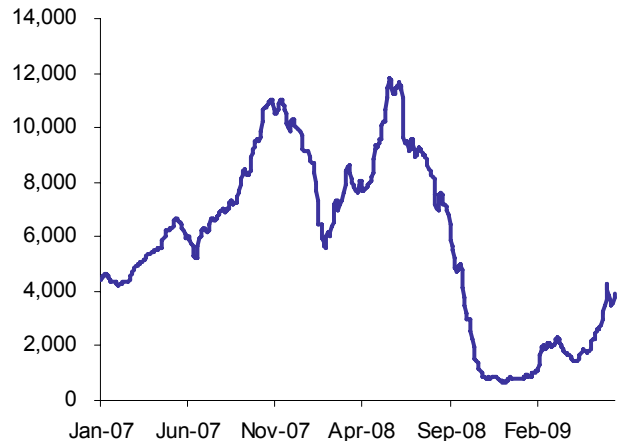
Inventories have shifted from LME to SHFE due to the arbitrage opportunity



Even though Chinese metal production has gone up in the last two months, inventories have not risen significantly



Baltic dry index has jumped 5x YTD



Source: Bloomberg, International Lead and Zinc Study Group (ILZSG)

Financials

Income statement

Y/e 31 Mar (Rs m)	FY08	FY09E	FY10E	FY11E
Revenue	78,778	58,220	60,318	78,772
Operating profit	53,784	28,759	30,119	41,347
Depreciation	(2,205)	(2,853)	(3,373)	(5,194)
Interest expense	(242)	(219)	(240)	(240)
Other income	8,516	7,892	7,283	7,174
Profit before tax	59,854	33,579	33,789	43,087
Taxes	(15,893)	(6,306)	(6,980)	(8,901)
Net profit	43,961	27,273	26,809	34,185

Balance sheet

Y/e 31 Mar (Rs m)	FY08	FY09E	FY10E	FY11E
Equity capital	4,225	4,225	4,225	4,225
Reserves	114,257	139,072	162,933	193,286
Net worth	118,482	143,298	167,158	197,511
Debt	4	-	-	-
Def tax liab (net)	4,597	5,703	5,703	5,703
Total liabilities	123,083	149,001	172,861	203,214

Fixed assets	41,626	47,119	58,746	78,551
Investments	63,325	63,325	63,325	63,325
Net working cap	4,504	2,199	1,565	2,052
Inventories	5,181	4,275	4,429	5,784
Sundry debtors	4,437	3,279	3,397	4,436
Other curr assets	3,871	2,829	2,620	3,412
Sundry creditors	(3,547)	(2,621)	(2,716)	(3,546)
Other curr liabilities	(5,438)	(5,562)	(6,165)	(8,034)
Cash	13,628	36,359	49,226	59,286
Total assets	123,083	149,001	172,861	203,214

Cash flow statement

Y/e 31 Mar (Rs m)	FY08	FY09E	FY10E	FY11E
Profit before tax	59,854	33,579	33,789	43,087
Depreciation	2,205	2,853	3,373	5,194
Tax paid	(15,893)	(6,306)	(6,980)	(8,901)
Working capital Δ	841	2,305	634	(486)
Operating cashflow	47,007	32,431	30,815	38,894
Capital expenditure	(15,125)	(8,345)	(15,000)	(25,000)
Free cash flow	31,882	24,085	15,815	13,894
Equity raised	(514)	0	-	-
Investments	(19,292)	-	-	-
Debt financing/disposal	-	(4)	-	-
Dividends paid	(1,236)	(2,457)	(2,948)	(3,833)
Other items	1,591	1,106	-	-
Net Δ in cash	12,431	22,731	12,867	10,061

Key ratios

Y/e 31 Mar	FY08	FY09E	FY10E	FY11E
Growth matrix (%)				
Revenue growth	(8.0)	(26.1)	3.6	30.6
Op profit growth	(16.1)	(46.5)	4.7	37.3
EBIT growth	(7.3)	(43.8)	0.7	27.3
Net profit growth	(1.0)	(38.0)	(1.7)	27.5

Profitability ratios (%)

OPM	68.3	49.4	49.9	52.5
EBIT margin	76.3	58.1	56.4	55.0
Net profit margin	55.8	46.8	44.4	43.4
RoCE	59.4	24.8	21.1	23.0
RoNW	45.1	20.8	17.3	18.7
RoA	40.0	18.9	15.8	17.2

Per share ratios

EPS	104.0	64.5	63.4	80.9
Dividend per share	2.5	5.0	6.0	7.8
Cash EPS	109.3	71.3	71.4	93.2
Book value per share	280.4	339.1	395.6	467.4

Payout (%)

Dividend payout	2.8	9.0	11.0	11.2
Tax payout	26.6	18.8	20.7	20.7

Liquidity ratios

Debtor days	21	21	21	21
Inventory days	24	27	27	27
Creditor days	16	16	16	16

Component ratios (%)

Mining & manufacturing	16.7	22.4	22.1	20.2
Power and fuel	6.9	16.6	16.0	16.9
Staff cost	3.9	6.3	6.7	5.9
Other op exp	4.2	5.3	5.3	4.6

Du-Pont Analysis

Y/e 31 Mar (Rs m)	FY08	FY09E	FY10E	FY11E
Tax burden (x)	0.73	0.81	0.79	0.79
Interest burden (x)	1.00	0.99	0.99	0.99
EBIT margin (x)	0.76	0.58	0.56	0.55
Asset turnover (x)	0.72	0.40	0.36	0.40
Financial leverage (x)	1.13	1.10	1.09	1.09
RoE (%)	45.1	20.8	17.3	18.7

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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