

January 23, 2012

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Rating	Accumulate
Price	Rs127
Target Price	Rs142
Implied Upside	11.8%
Sensex	16,739
Nifty	5,049

(Prices as on January 20, 2012)

Trading data

Market Cap. (Rs bn)	535.8
Shares o/s (m)	4,225.3
3M Avg. Daily value (Rs m)	93.3

Major shareholders

Promoters	64.92%
Foreign	1.31%
Domestic Inst.	1.78%
Public & Other	31.98%

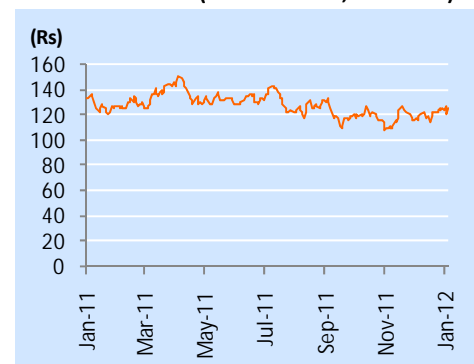
Stock Performance

(%)	1M	6M	12M
Absolute	8.0	(7.5)	(5.2)
Relative	(2.3)	2.0	6.9

How we differ from Consensus

EPS (Rs)	PL	Cons.	% Diff.
2013	15.9	14.9	6.9
2014	16.7	16.6	0.8

Price Performance (RIC: HZNC.BO, BB: HZ IN)



Source: Bloomberg

Hindustan Zinc (HZ) reported Q3FY12 earnings below our expectation. The weakness was primarily attributed to higher-than-expected outsourced raw material cost, coupled with lower mined metal production. We remain **positive** on the stock, given its strong return profile (RoE>22%), attractive valuations and robust free cash flows.

- Temporary fall in ore grade impacted earnings:** Revenue grew in line with expectation at 6% QoQ, with refined volumes of 218kt (+10% QoQ) and silver volumes of 49k kg (+18% QoQ). However, higher-than-expected outsourced raw material cost, coupled with lower mined metal production, weakened the earnings. HZ's cost per tonne of refined metal rose by 8% QoQ to Rs63,505, way ahead of our expectation of Rs57,652. Hence, EBITDA fell by 4% QoQ (8% YoY) to Rs13.6bn, short of our expectation of Rs14.1bn. Lower-than-expected interest income and higher tax rate (20.9% V/s PLe: 19.2%) widened the gap on the PAT level, with adjusted PAT at Rs12.8bn (PLe: Rs13.8bn), down 6% QoQ (1% YoY).
- Key con-call highlights: 1)** With the mining activity moving back to high grade pockets, management guided to produce higher ore grades during the quarter. **2)** Newly commissioned 100ktpa lead smelter at Dariba is operating at 70% utilisation and management expects to exit the utilisation at ~90% during Q4FY12. **3)** Management expects CoP to escalate by US\$15 per tonne or ~2% due to recent pricing change emulated by *Coal India* as domestic linkage coal constitutes 40% of its total coal requirement.
- Maintain 'Accumulate', with TP of Rs142:** We expect strong earnings momentum ahead, with increased contribution from capacities added in lead and margin rich silver operations and mine, expansion of SK mines and improvement in grades. We maintain **'Accumulate'** on the stock, with TP of Rs142, EV/EBITDA of 5x FY13E.

Key financials (Y/e March)	2011	2012E	2013E	2014E
Revenues (Rs m)	99,121	109,345	128,499	133,737
Growth (%)	23.6	10.3	17.5	4.1
EBITDA (Rs m)	54,859	58,861	71,273	73,688
PAT (Rs m)	49,005	56,397	67,319	70,569
EPS (Rs)	11.6	13.3	15.9	16.7
Growth (%)	21.3	15.1	19.4	4.8
Net DPS (Rs)	1.0	2.5	3.5	4.0

Profitability & Valuation	2011	2012E	2013E	2014E
EBITDA margin (%)	55.3	53.8	55.5	55.1
RoE (%)	24.1	22.8	22.9	20.5
RoCE (%)	24.1	22.9	22.9	20.5
EV / sales (x)	4.8	4.0	3.0	2.5
EV / EBITDA (x)	8.7	7.5	5.4	4.5
PE (x)	10.9	9.5	8.0	7.6
P / BV (x)	2.4	2.0	1.7	1.4
Net dividend yield (%)	0.8	2.0	2.8	3.2

Source: Company Data; PL Research

Exhibit 1: Q3FY12 Result Overview (Rs m)

Y/e March	Q3FY12	Q3FY11	YoY gr. (%)	Q2FY12	9MFY12	9MFY11	YoY gr. (%)
Net Sales	27,468	26,015	5.6	25,935	81,616	67,151	21.5
Raw material consumed	1,287	(7)		(387)	2,217	(229)	
<i>% of Net Sales</i>	<i>4.7</i>	<i>0.0</i>		<i>(1.5)</i>	<i>2.7</i>	<i>(0.3)</i>	
Stores and spares consumed	2,702	2,187	23.5	2,648	7,715	6,423	20.1
<i>% of Net Sales</i>	<i>9.8</i>	<i>8.4</i>		<i>10.2</i>	<i>9.5</i>	<i>9.6</i>	
Power and fuel	3,177	2,520	26.0	2,924	9,054	7,378	22.7
<i>% of Net Sales</i>	<i>11.6</i>	<i>9.7</i>		<i>11.3</i>	<i>11.1</i>	<i>11.0</i>	
Mining Royalty Rates	2,005	2,195	(8.7)	2,147	6,087	5,524	10.2
<i>% of Net Sales</i>	<i>7.3</i>	<i>8.4</i>		<i>8.3</i>	<i>7.5</i>	<i>8.2</i>	
Other manufacturing expenses	2,691	2,290	17.5	2,287	6,878	6,258	9.9
<i>% of Net Sales</i>	<i>9.8</i>	<i>8.8</i>		<i>8.8</i>	<i>8.4</i>	<i>9.3</i>	
Employee Cost	1,337	1,130	18.3	1,290	3,902	3,767	3.6
<i>% of Net Sales</i>	<i>4.9</i>	<i>4.3</i>		<i>5.0</i>	<i>4.8</i>	<i>5.6</i>	
Selling, general and administrative	646	914	(29.3)	812	2,260	2,351	(3.9)
<i>% of Net Sales</i>	<i>2.4</i>	<i>3.5</i>		<i>3.1</i>	<i>2.8</i>	<i>3.5</i>	
Total Expenditure	13,845	11,229	23.3	11,720	38,113	31,471	21.1
EBITDA	13,622	14,786	(7.9)	14,215	43,503	35,680	21.9
<i>Margin (%)</i>	<i>49.6</i>	<i>56.8</i>		<i>54.8</i>	<i>53.3</i>	<i>53.1</i>	
Depreciation	1,591	1,195	33.1	1,455	4,391	3,477	26.3
Other income	4,219	2,358	78.9	4,301	12,331	6,359	93.9
EBIT	16,251	15,948	1.9	17,061	51,443	38,562	33.4
Interest	87	1	7,818	120	272	62	342.8
PBT	16,164	15,947	1.4	16,940	51,170	38,501	32.9
Extraordinary income/(expense)	(64)	-		(239)	(347)	(212)	
PBT (After EO)	16,099	15,947	1.0	16,702	50,823	38,289	32.7
Tax	3,363	3,051	10.2	3,255	9,691	6,997	38.5
<i>% PBT</i>	<i>20.9</i>	<i>19.1</i>		<i>19.5</i>	<i>19.1</i>	<i>18.3</i>	
Reported PAT	12,736	12,896	(1.2)	13,447	41,132	31,292	31.4
Adjusted PAT	12,787	12,896	(0.8)	13,639	41,413	31,465	31.6

Source: Company Data, PL Research

Exhibit 2: Operating Metrics

Y/e March	Q3FY12	Q3FY11	YoY gr. (%)	Q2FY12	9MFY12	9MFY11	YoY gr. (%)
Production volume							
- Mined metal (Zinc+Lead)-tonnes	208,900	222,249	(6.0)	209,676	606,979	609,015	(0.3)
- Refined metal (Zinc+Lead)-tonnes	218,020	190,774	14.3	200,473	626,274	560,197	11.8
- Sulphuric acid-tonnes	333,000	287,116	16.0	317,245	974,833	863,915	12.8
- Silver (kgs)	48,413	32,777	47.7	42,081	130,080	105,294	23.5
Sales volume							
- Refined Zinc	190,946	178,357	7.1	184,161	566,677	518,111	9.4
- Refined Lead	27,074	12,338	119.4	14,686	56,471	40,871	38.2
- Sulphuric acid	333,000	300,546	10.8	312,682	964,451	863,940	11.6
- Silver (kgs)	49,000	29,524	66.0	41,454	131,362	102,233	28.5
Realisation (Rs/unit)							
- Refined Zinc	104,951	110,911	(5.4)	108,122	106,893	103,291	3.5
- Refined Lead	113,762	119,271	(4.6)	120,019	118,892	108,585	9.5
- Sulphuric acid	3,500	2,590	35.1	3,013	3,197	2,371	34.9
- Silver (kgs)	52,449	39,398	33.1	57,746	55,151	31,841	73.2

Source: Company Data, PL Research

Income Statement (Rs m)

Y/e March	2011	2012E	2013E	2014E
Net Revenue	99,121	109,345	128,499	133,737
Raw Material Expenses	—	—	—	—
Gross Profit	99,121	109,345	128,499	133,737
Employee Cost	5,108	5,417	6,096	6,846
Other Expenses	39,155	45,067	51,130	53,203
EBITDA	54,859	58,861	71,273	73,688
Depr. & Amortization	4,747	5,797	6,302	6,448
Net Interest	194	219	257	267
Other Income	9,678	15,931	18,395	20,148
Profit before Tax	59,596	68,776	83,109	87,122
Total Tax	10,591	12,380	15,791	16,553
Profit after Tax	49,005	56,397	67,319	70,569
Ex-Od items / Min. Int.	—	—	—	—
Adj. PAT	49,005	56,397	67,319	70,569
Avg. Shares O/S (m)	4,225.3	4,225.3	4,225.3	4,225.3
EPS (Rs.)	11.6	13.3	15.9	16.7

Cash Flow Abstract (Rs m)

Y/e March	2011	2012E	2013E	2014E
C/F from Operations	42,719	47,841	58,666	59,270
C/F from Investing	(36,564)	2,866	10,467	13,622
C/F from Financing	(3,633)	(12,496)	(14,989)	(19,911)
Inc. / Dec. in Cash	2,522	38,211	54,144	52,982
Opening Cash	9,275	56,329	94,541	148,685
Closing Cash	11,779	94,541	148,685	201,666
FCFF	31,741	42,248	74,501	73,753
FCFE	31,141	42,248	74,501	73,753

Key Financial Metrics

Y/e March	2011	2012E	2013E	2014E
Growth				
Revenue (%)	23.6	10.3	17.5	4.1
EBITDA (%)	17.5	7.3	21.1	3.4
PAT (%)	21.3	15.1	19.4	4.8
EPS (%)	21.3	15.1	19.4	4.8
Profitability				
EBITDA Margin (%)	55.3	53.8	55.5	55.1
PAT Margin (%)	49.4	51.6	52.4	52.8
RoCE (%)	24.1	22.9	22.9	20.5
RoE (%)	24.1	22.8	22.9	20.5
Balance Sheet				
Net Debt : Equity	(0.2)	(0.4)	(0.5)	(0.5)
Net Wrkng Cap. (days)	—	—	—	—
Valuation				
PER (x)	10.9	9.5	8.0	7.6
P / B (x)	2.4	2.0	1.7	1.4
EV / EBITDA (x)	8.7	7.5	5.4	4.5
EV / Sales (x)	4.8	4.0	3.0	2.5
Earnings Quality				
Eff. Tax Rate	17.8	18.0	19.0	19.0
Other Inc / PBT	16.5	23.5	22.1	23.1
Eff. Depr. Rate (%)	4.8	4.9	5.2	5.2
FCFE / PAT	63.5	74.9	110.7	104.5

Source: Company Data, PL Research.

Balance Sheet Abstract (Rs m)

Y/e March	2011	2012E	2013E	2014E
Shareholder's Funds	225,332	269,452	319,583	370,508
Total Debt	4	4	4	4
Other Liabilities	9,447	10,135	10,966	11,837
Total Liabilities	234,783	279,590	330,552	382,349
Net Fixed Assets	81,294	87,574	87,772	86,324
Goodwill	—	—	—	—
Investments	93,346	93,346	93,346	93,346
Net Current Assets	60,143	98,671	149,434	202,679
<i>Cash & Equivalents</i>	<i>56,329</i>	<i>94,541</i>	<i>148,685</i>	<i>201,666</i>
<i>Other Current Assets</i>	<i>19,560</i>	<i>20,916</i>	<i>21,295</i>	<i>21,949</i>
<i>Current Liabilities</i>	<i>15,747</i>	<i>16,786</i>	<i>20,545</i>	<i>20,936</i>
Other Assets	—	—	—	—
Total Assets	234,783	279,590	330,552	382,349

Quarterly Financials (Rs m)

Y/e March	Q4FY11	Q1FY12	Q2FY12	Q3FY12
Net Revenue	31,970	28,214	25,935	27,468
EBITDA	19,282	15,666	14,215	13,622
<i>% of revenue</i>	<i>60.3</i>	<i>55.5</i>	<i>54.8</i>	<i>49.6</i>
Depr. & Amortization	1,271	1,345	1,455	1,591
Net Interest	133	65	120	87
Other Income	3,428	3,811	4,301	4,219
Profit before Tax	21,307	18,022	16,702	16,099
Total Tax	3,594	3,073	3,255	3,363
Profit after Tax	17,713	14,949	13,447	12,736
Adj. PAT	17,713	14,986	13,639	12,787

Key Operating Metrics

Y/e March	2011	2012E	2013E	2014E
Mined Zinc metal prod-MIC tns	752,120	727,578	773,649	773,649
Mined Lead metal prod-MIC tns	87,920	94,322	136,861	150,809
Total Mines metal-MIC tns	840,040	821,900	910,510	924,458
Refined Zinc Vol. (tonnes)	712,603	766,488	808,680	808,680
Refined Lead Vol. (tonnes)	57,229	88,825	132,056	146,856
Total Refined metal-tns	769,832	855,313	940,736	955,536
Concentrate sales vol (tonnes)	104,414	—	—	—
Silver Sales Vol. (kg)	146,558	218,891	367,688	429,940
Zinc (US\$)-LME / tonne	2,186	2,070	2,100	2,100
Lead(US\$)-LME / tonne	2,245	2,250	2,150	2,150
Silver (Rs / Kg)	37,090	38,199	54,013	53,473
Cost per tonne of Mined metal (Zn+Pb)	52,691	61,424	62,850	64,955

Source: Company Data, PL Research.

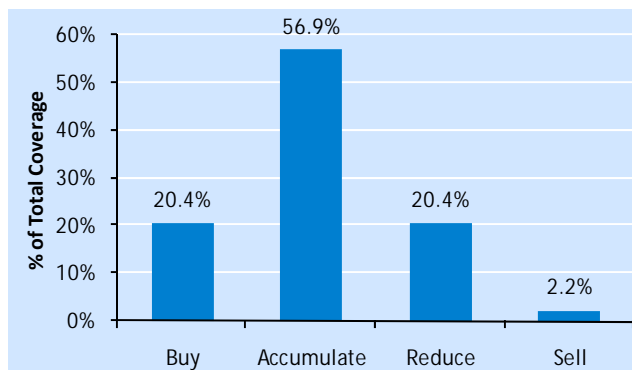


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Rating Distribution of Research Coverage



PL's Recommendation Nomenclature

BUY	: Over 15% Outperformance to Sensex over 12-months	Accumulate	: Outperformance to Sensex over 12-months
Reduce	: Underperformance to Sensex over 12-months	Sell	: Over 15% underperformance to Sensex over 12-months
Trading Buy	: Over 10% absolute upside in 1-month	Trading Sell	: Over 10% absolute decline in 1-month
Not Rated (NR)	: No specific call on the stock	Under Review (UR)	: Rating likely to change shortly

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