

Hindustan Zinc (HZ N)

In-line quarter; volume ramp-up wait gets longer...

INDIA | METALS | Quarterly Update

21 January 2020

Top takeaways from Q3FY20

- ✖ Revenues came 5% lower than expectation at Rs 46.7bn (-16%/+4% yoy/qoq) due to 7% lower zinc volumes.
- ✖ The zinc, lead and silver sales volumes stood at 172KT (-8%/+2% yoy/qoq); 42KT (-22%/-4% yoy/qoq) and 153 tonnes (-14%/+13% qoq/yoy), respectively.
- ⇨ However; EBITDA was broadly in line with expectation at Rs 22.9bn, down 19% yoy but improved 8% qoq (Est. Rs 23.2bn).
- ✖ Other income at Rs 4.5bn was slightly lower than expectation of 5.0bn.
- ⇨ However lower than expected tax rate (22.7%) led to in-line PAT at Rs 16.2bn.
- ⇨ Net cash and equivalents stands at Rs 46/share.

Key highlights: The company continues to suffer from one off events hampering production ramp-up and forcing them to cut production guidance for FY20 (second consecutive cut). 3QFY20 suffered from roster breakdown (impacted US\$ 10/tonne in costs) and temporary issue in DSC lead smelter. Overall mined metal volumes fell 11% yoy to 214KT while CoP (ex-royalty) increased by US\$80/t. leading to 19% yoy fall in EBITDA. Management is hopeful of a significantly better 4Q and FY21 aided by ramp up of growth projects.

Conference call takeaways

- Production guidance was trimmed from 950KT to 910-915KT considering delays in ramp up and technical challenges in SK mines. Silver guidance was maintained at 650 tonne.
- Smelter capacity jumped to 1.13 mn tonnes and expects to reach 1.2 mn tonnes by FY21
- Management remain optimistic on zinc demand scenario as global mine production was c.600KT lower than expectation while zinc inventories are further down to 4 days.
- CoP is expected to fall on better volumes, improving linkage (currently 22%) and lower imported coal cost (c.78% imported). Guiding CoP of US\$ 900/t by FY22.
- Fertilizer plant (740KT) EC is expected to be received in a month or two.
- Major projects (RA from 4.1 to 4.5; Zawar backfill and fumer for silver recovery) to be completed in 4QFY20.
- HZ is guiding for US\$ 500-550 mn capex in FY20 which includes growth capex of US\$ 300mn and sustenance capex of US\$ 200-250 mn (largely mine development).

Outlook and valuation: The wait for volume led growth story is getting longer as it's the second consecutive year where company failed to deliver the annual production guidance. At the same time we believe that incremental volumes from expansion projects across the world would gradually push zinc market into surplus. Though, current very low levels of inventories and temporary production discipline will keep the prices range bound. We continue to maintain our negative bias on zinc prices. Maintain neutral with target price of 215 (7.0x FY21 EV/EBITDA). Expected dividend yield of 6-7%.

NEUTRAL (Maintain)

CMP RS 212 / TARGET RS 215 (+1%)

SEBI CATEGORY: LARGE CAP

COMPANY DATA

O/S SHARES (MN) :	4225
MARKET CAP (RSBN) :	897
MARKET CAP (USDBN) :	12.6
52 - WK HI/LO (RS) :	292 / 193
LIQUIDITY 3M (USDMN) :	2.2
PAR VALUE (RS) :	2

SHARE HOLDING PATTERN, %

	Dec 19	Sep 19	Jun 19
PROMOTERS :	64.9	64.9	64.9
FII / NRI :	30.8	30.9	30.9
FI / MF :	2.6	2.6	2.5
NON PRO :	0.1	0.6	0.6
PUBLIC & OTHERS :	1.5	1.1	1.0

KEY FINANCIALS

Rs mn	FY19	FY20E	FY21E
Net Sales	2,11,180	2,03,172	2,18,801
EBIDTA	1,06,700	99,396	1,06,165
Net Profit	79,560	76,205	73,484
EPS, Rs	18.8	18.0	17.4
PER, x	12.1	11.8	12.2
EV/EBIDTA, x	7.4	7.3	6.9
P/BV, x	2.9	2.5	2.5
ROE, %	23.7	21.6	20.8
Debt/Equity (%)	7.6	-	-

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(Rs bn)	3QFY20	3QFY19	Yoy growth %	1QFY20	qoq vs. expectations growth %	Comments
Net Sales	46,720	55,400	(15.7)	45,110	3.6	(21.5) Broadly in line
EBITDA	22,890	28,380	(19.3)	21,170	8.1	(25.2) Employee cost was marginally lower than expectation.
EBITDA Margin (%)	49.0	51.2		46.9		(4.6)
Other Income	4,450	5,500	(19.1)	5,900	(24.6)	(11.0)
Interest	420	510		250	68.0	110.0
Depreciation	5,970	4,890	22.1	5,950	0.3	1.2
PBT	20,950	28,480	(26.4)	20,870	0.4	(28.9)
Tax	4,750	6,370	(25.4)	60	7,816.7	(40.3) Tax rate at 25% was lower than expectation.
Net Profit	16,200	22,110	(26.7)	20,810	(22.2)	(24.7)
PAT Margin (%)	34.7	39.9		46.1		(4.1)
EPS (Rs)	3.8	5.2	(26.7)	4.9	(22.2)	(24.7)

Volumes and realizations

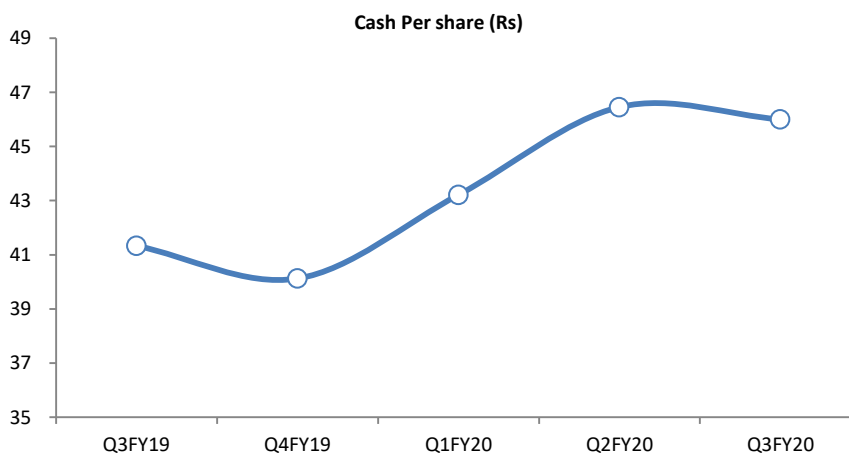
	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3FY20	QoQ (%)	YoY (%)
Volumes - Tonnes							
Zinc	1,87,000	1,77,000	1,67,500	1,67,900	1,72,000	2.4	(8.0)
Lead	54,000	52,000	47,500	43,900	42,000	(4.3)	(22.2)
Silver	178	199	155	135	153	13.3	(14.0)
Realisations (Rs/tonne)							
Zinc	2,05,401	2,08,418	2,09,552	1,81,715	1,84,012	1.3	(10.4)
Lead	1,52,963	1,55,577	1,44,000	1,53,075	1,55,238	1.4	1.5
Silver (Rs/kg)	38,034	37,437	37,161	42,741	45,098	5.5	18.6
US\$/INR	72.0	70.5	69.6	70.3	71.2	1.3	-1.1

Source: Company, PhillipCapital India Research

Cost Incidence

Rs mn	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3FY20
Raw Material	(250)	250	(60)	(140)	(1,710)
% of sales	(0.5)	0.5	(0.1)	(0.3)	(3.7)
Power & Fuel	4,930	3,870	4,450	4,130	4,040
% of sales	8.9	7.0	8.9	9.2	8.6
Mining Royalty	6,700	6,990	5,940	5,390	6,130
% of sales	12.1	12.7	11.9	11.9	13.1
Employee cost	2,150	2,130	1,820	1,920	2,010
% of sales	3.9	3.9	3.6	4.3	4.3
Other expenses	13,490	13,780	12,950	12,640	13,360
% of sales	24.4	25.1	26.0	28.0	28.6

Source: Company, PhillipCapital India Research

Cash per share (Rs)


Source: Company, PhillipCapital India Research

Financials

Consolidated Income Statement

Y/E Mar, Rs mn	FY19	FY20e	FY21e	FY22e
Net sales	2,11,180	2,03,172	2,18,801	2,35,719
Growth, %	-4	-4	8	8
Total income	2,11,180	2,03,172	2,18,801	2,35,719
Raw material expenses	640	0	0	0
Employee expenses	-9,050	-9,141	-9,598	-10,077
Other Operating expenses	-96,070	-94,636	-1,03,039	-1,08,744
EBITDA (Core)	1,06,700	99,396	1,06,165	1,16,897
Growth, %	(13.0)	(6.8)	6.8	10.1
Margin, %	50.5	48.9	48.5	49.6
Depreciation	-18,830	-23,278	-26,857	-29,914
EBIT	87,870	76,118	79,308	86,982
Growth, %	(18.5)	(13.4)	4.2	9.7
Margin, %	41.6	37.5	36.2	36.9
Interest paid	-1,130	0	0	0
Other Income	17,820	19,602	19,994	20,394
Pre-tax profit	1,04,560	95,720	99,302	1,07,376
Tax provided	-25,000	-19,516	-25,819	-27,918
Profit after tax	79,560	76,205	73,484	79,458
Net Profit	79,560	76,205	73,484	79,458
Growth, %	(12.0)	(4.2)	(3.6)	8.1
Net Profit (adjusted)	79,560	76,205	73,484	79,458
Unadj. shares (m)	4,225	4,225	4,225	4,225
Wtd avg shares (m)	4,225	4,225	4,225	4,225

Balance Sheet

Y/E Mar, Rs mn	FY19	FY20e	FY21e	FY22e
Cash & bank	230	9,648	6,576	19,175
Marketable securities at cost	1,94,880	1,59,880	1,59,880	1,59,880
Debtors	1,960	1,886	2,031	2,188
Inventory	15,440	14,855	15,997	17,234
Loans & advances	70	67	73	78
Other current assets	3,140	3,297	3,462	3,635
Total current assets	2,15,720	1,89,633	1,88,018	2,02,190
Gross fixed assets	2,58,410	2,76,442	3,01,966	3,26,736
Less: Depreciation	-1,10,630	-1,33,060	-1,59,720	-1,89,439
Add: Capital WIP	22,540	42,540	49,540	49,540
Net fixed assets	1,70,320	1,85,922	1,91,786	1,86,837
Non-current assets	19,290	19,192	19,383	19,590
Total assets	4,24,580	4,12,072	4,14,780	4,22,650
Current liabilities	62,690	31,563	34,258	36,139
Provisions	2,190	2,234	2,278	2,324
Total current liabilities	64,880	33,797	36,536	38,463
Non-current liabilities	23,650	24,833	24,833	24,833
Total liabilities	88,530	58,629	61,369	63,296
Paid-up capital	8,450	8,450	8,450	8,450
Reserves & surplus	3,27,600	3,44,993	3,44,961	3,50,905
Shareholders' equity	3,36,050	3,53,443	3,53,411	3,59,355
Total equity & liabilities	4,24,580	4,12,072	4,14,780	4,22,650

Source: Company, PhillipCapital India Research Estimates

Cash Flow

Y/E Mar, Rs mn	FY19	FY20e	FY21e	FY22e
Pre-tax profit	1,04,560	95,720	99,302	1,07,376
Depreciation	18,830	23,278	26,857	29,914
Chg in working capital	18,790	-29,297	1,091	148
Total tax paid	-22,170	-17,591	-24,086	-26,359
Other operating activities	-230	-1,730	-3,230	0
Cash flow from operating activities	1,19,780	70,380	99,933	1,11,080
Capital expenditure	-43,930	-38,880	-32,721	-24,966
Chg in marketable securities	7,340	35,000	0	0
Cash flow from investing activities	-36,590	-3,880	-32,721	-24,966
Free cash flow	83,190	66,500	67,213	86,114
Equity raised/(repaid)	-710	1,730	3,230	4,730
Dividend (incl. tax)	-1,01,890	-58,812	-73,515	-73,515
Cash flow from financing activities	-1,02,600	-57,082	-70,285	-68,785
Net chg in cash	-19,410	9,418	-3,072	17,329

Valuation Ratios

	FY19	FY20e	FY21e	FY22e
Per Share data				
EPS (INR)	18.8	18.0	17.4	18.8
Growth, %	(12.0)	(4.2)	(3.6)	8.1
Book NAV/share (INR)	79.5	83.7	83.6	85.1
FDEPS (INR)	18.8	18.0	17.4	18.8
CEPS (INR)	23.3	23.5	23.7	25.9
CFPS (INR)	17.9	18.4	19.7	21.5
DPS (INR)	20.0	12.0	15.0	15.0
Return ratios				
Return on assets (%)	18.9	18.2	17.8	19.0
Return on equity (%)	23.7	21.6	20.8	22.1
Return on capital employed (%)	21.2	20.5	19.3	20.7
Turnover ratios				
Asset turnover (x)	1.9	1.5	1.4	1.6
Sales/Total assets (x)	0.5	0.5	0.5	0.6
Sales/Net FA (x)	1.3	1.1	1.2	1.2
Working capital/Sales (x)	(0.2)	(0.1)	(0.1)	(0.1)
Fixed capital/Sales (x)	0.7	0.7	0.7	0.6
Receivable days	3.4	3.4	3.4	3.4
Inventory days	26.7	26.7	26.7	26.7
Payable days	41.0	41.0	41.0	41.0
Working capital days (Ex-Cash)	(72.7)	(20.6)	(21.2)	(20.1)
Liquidity ratios				
Current ratio (x)	3.4	6.0	5.5	5.6
Quick ratio (x)	3.2	5.5	5.0	5.1
Interest cover (x)	77.8	-	-	-
Total debt/Equity (%)	7.6	-	-	-
Net debt/Equity (%)	(50.5)	(48.0)	(47.1)	(49.8)
Valuation				
PER (x)	12.1	11.8	12.2	11.3
PEG (x) - y-o-y growth	(0.9)	(2.8)	(3.4)	1.4
Price/Book (x)	2.9	2.5	2.5	2.5
Yield (%)	8.8	5.7	7.1	7.1
EV/Net sales (x)	3.8	3.6	3.3	3.0
EV/EBITDA (x)	7.4	7.3	6.9	6.1
EV/EBIT (x)	9.0	9.5	9.2	8.2

Stock Price, Price Target and Rating History



Rating Methodology

We rate stock on absolute return basis. Our target price for the stocks has an investment horizon of one year. We have different threshold for large market capitalisation stock and Mid/small market capitalisation stock. The categorisation of stock based on market capitalisation is as per the SEBI requirement.

Large cap stocks

Rating	Criteria	Definition
BUY	$\geq +10\%$	Target price is equal to or more than 10% of current market price
NEUTRAL	$-10\% > \text{to} < +10\%$	Target price is less than +10% but more than -10%
SELL	$\leq -10\%$	Target price is less than or equal to -10%.

Mid cap and Small cap stocks

Rating	Criteria	Definition
BUY	$\geq +15\%$	Target price is equal to or more than 15% of current market price
NEUTRAL	$-15\% > \text{to} < +15\%$	Target price is less than +15% but more than -15%
SELL	$\leq -15\%$	Target price is less than or equal to -15%.

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