

Hindustan Zinc Ltd

Industry **ZINC**
Bloomberg **HZ IN**
BSE CODE **500188**

Decline in volumes of Zinc, Lead and Silver reduced the guidance for FY20

RATING **NEUTRAL**

CMP **215**
Price Target **228**
Potential Upside **6%**

Rating Change 

Estimate Change 

Target Change 

2QFY20 Result Update

- ❑ HINDZINC reported a revenue of Rs. 4511 Cr. (vs our estimates of Rs. 4899 Cr.) degrew by 5.6% YoY largely on account of lower production volumes of both mined and refined metal. Moreover, management reduced the production guidance of 1.2MT in FY20 to 950KT of mined metal.
- ❑ In 1HFY20 the production of mined metal stood at 432KT and is expected to be around 520KT in 2HFY20. Management expects 650K of production of silver in 2HFY20.
- ❑ Revenue contribution by Zinc of Rs. 3051 Cr. (down by 3%YoY) due to flattish Zinc refined metal volumes on YoY basis while the reduced prices of Zinc LME (\$/MT) by 10% YoY reduced the realization by 5% YoY.
- ❑ Lead contributes Rs. 672 Cr. of revenue (down by 15% YoY) based on reduced Lead LME (\$/MT) prices by 3% YoY reduced the realization by 6% YoY along with the 10% YoY decline in refined lead volume.
- ❑ Lead production was low due to annual maintenance shutdown in July, and also some unanticipated issues at ESC lead smelter during the month of September.
- ❑ Revenue contributed by silver is Rs. 577 Cr. wherein volume reduced by 22% YoY while realization increased by 24% YoY.
- ❑ EBITDA margin contracted by 193bps YoY to 46.9% on account of lower realization. However, management expect Zinc cost of production in 2HFY20 to be a bit about \$1,030 per tonne including the impact of higher electricity duty.
- ❑ Digitalization of Sindesar Khurd mine and Rampura agucha mine will further helps to reduce the cost.
- ❑ PAT during the quarter stood at Rs. 2081 Cr. with a PAT growth of 14.7% YoY on account of higher other income and lower tax rate.

View and Valuation

HINDZINC scaled back the production guidance for FY20 from 1.2MT to 950KT looking towards the production and consumption in China for bolster spending on infrastructure in order to mitigate the impact of its dispute with the US Zinc. No smelting addition is in pipeline for the next 2 years, over there are temporary disruptions and closures in China, Canada, Africa and US in equivalent to 200KTBA refinement of production. Reduced Zinc and Lead LME (\$/T) reduced the realization in 2QFY20. However, management expects the cost for 2HFY20 to be \$1030/T. Digitalization in mines will further reduce the cost of material. We maintain our **NEUTRAL** stance on the stock with an increased target price of Rs. 228 (6.5x FY21e EV/EBITDA).

Key Risks to our rating and target

- ❑ High volatility in LME Zinc prices and lower than expected volume growth.
- ❑ Changing zinc and lead ratio in ore is a concern.

Fig in Rs. Cr

KEY FINANCIAL/VALUATIONS	FY17	FY18	FY19	FY20E	FY21E
Net Sales	17273	22084	21118	20256	25321
EBITDA	9739	12272	10670	9618	11354
EBIT	7928	10789	8787	7417	8943
PAT	8316	9276	7956	7249	8186
EPS (Rs)	20	22	19	17	19
EPS growth (%)	2	10	-15	-8	14
ROE (%)	27	26	23	20	21
ROCE (%)	26	30	26	21	23
BV	73	85	80	85	93
P/B (X)	3.96	3.54	3.48	2.44	2.46
P/E (x)	14.58	13.83	14.85	12.15	11.77

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2QFY20 Results

Reduced metal prices impacted the margins

Fig in Rs. Cr.

Financials	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	YoY %	QoQ%	FY18	FY19	YoY %
Net Sales	4777	5540	5491	4987	4511	-5.6%	-9.5%	22,084	21,118	-4.4%
Other Income	394	550	539	429	590	49.7%	37.5%	1,751	1,782	1.8%
Total Income	5171	6090	6030	5416	5101	-1.4%	-5.8%	23,835	22,900	-3.9%
COGS	-105	-25	25	-6	-14	-87%	-	498	(64)	-
Staff Cost	245	215	213	182	192	-21.6%	5.5%	776	905	16.6%
Other Exp.	1237	1349	1378	1295	1264	2.2%	-2.4%	4,238	5,221	23.2%
Expenditure	2443	2702	2702	2510	2394	-2.0%	-4.6%	9,812	10,448	6.5%
EBITDA	2334	2838	2789	2477	2117	-9.3%	-14.5%	12,272	10,670	-13.1%
EBITDA margin	48.9%	51.2%	50.8%	49.7%	46.9%	-3.9%	-5.5%	1	1	-9.1%
Depreciation	454	489	553	534	595	31.1%	11.4%	1,483	1,883	27.0%
EBIT	1880	2349	2236	1943	1522	-19.0%	-21.7%	10,789	8,787	-18.6%
Interest	0	51	51	29	25	0.0%	-	283	113	-60.1%
PBT	2274	2848	2724	2343	2087	-8.2%	-10.9%	12,257	10,456	-14.7%
Excpt. Item	0	0	0	0	0	0.0%	-	240	-	-
Tax	459	637	712	578	6	-98.7%	-99.0%	3,221	2,500	-22.4%
PAT	1815	2211	2012	1765	2081	14.7%	17.9%	9,276	7,956	-14.2%

Operating Matrix

Volume/Prices	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	YoY %
Refined Zinc ('000 tons)	200	206	172	162	188	175	172	166	2.5%
Zinc LME (USD/ton)	3236	3421	3112	2569	2576	2783	2719	2323	-9.6%
Refined Lead('000 tons)	46	50	42	49	54	53	48	44	-10.2%
Lead LME (USD/ton)	2492	2523	2388	2104	1944	2083	1872	2034	-3.3%
Silver (tons)	132	170	138	172	178	191	159	134	-22.1%
Silver LBMA (USD/oz.)	17	17	16	15	15	16	15	15	2.3%

Zinc volume reduced by 2%YoY

Zinc volume in 2QFY20 was at 166kt (down by 2% YoY and 3.4% QoQ). Reduced YoY volume was on account of lower grades in ore produced and QoQ fall was on account of lower mined metal and annual maintenance shutdown at smelters which was partly offset by WIP conversion. Mined metal production was at 219kt (down 6% YoY, up 13.1% QoQ), moreover ore production guidance was reduced to 950KT from 1.2MT. Lead volume in the quarter was at 44kt (down 10% YoY and 8% QoQ) and silver volume was at 134kt (down 22% YoY and 16% QoQ), silver production is expected to be at 650T in FY20 as per revised guidance.

Lower metal prices led to fall in EBITDA

EBITDA for the quarter was at Rs.2117cr (down 9.3% YoY and 15% QoQ) and EBITDA margin for the quarter was at 46.9% (vs. 48.9% in 2QFY19 and 49.7% in 1QFY20), YoY fall in EBITDA was primarily on account of lower metal prices with zinc, lead and silver realization falling by 10%, 3% and 22% respectively. However, management expects cost to further going down ahead on account of digitalization of SK and RM mines and the cost of production for 2HFY20 is expected to be at \$1030/T. SK shaft utilization will further helps to improve margins.

Higher other income and reduced tax expense help PAT to sustain at a level

PAT during the quarter stood at Rs. 2081 Cr. with the PAT growth of 14.7% YOY largely driven by higher other income of Rs. 590 Cr. due to gain on investments on mark to margin basis and tax expense of Rs. 6 Cr. based on impact of section 115BAA of ITA,1961has introduced by the taxation laws (amendment) ordinance 2019. The company has remeasured its deferred tax balances leading to a deferred tax credit of Rs. 365 Cr. on deferred tax balances as at 31st March, 2019 being recognized in the current quarter statement of P & L.

Conference call highlights**Zinc Market:**

- The Chinese authorities have moved to bolster spending on infrastructure in order to mitigate the impact of its dispute with the US Zinc as consumption growth is healthy in China, at 1.5% this year. The mine production forecast for FY20 and FY21 have been paired down by almost 1 MT due to lower than expected production at several mine across the globe.
- No smelting addition is in pipeline for the next 2 years, over there are temporary disruptions and closures in China, Canada, Africa and US in equivalent to 200KTBA refinement of production. Revenue expected to be around 700 KT for FY19. The global metal market, therefore continues to be in deficit and management expects the short form to remain next year as well, it will take much longer for stocks to reach normal levels.

Operational and Financial Performance:

- Management expects to achieve 1.2 MTPA mined metal capacity in 2HFY20 based on mining projects approaching completion. SK mine commissioned this year.
- The revised guidance for both mine and refine metal projection in FY20 is expected to be around 950 KT, while silver production is expected to be around 650 tonnes
- Management expect Zinc cost of production in 2HFY20 to be a bit about \$1,030 per tonne including the impact of higher electricity duty.
- Investment income increase due to higher rate of return on account of mark-to-market gains, in portfolio resulting from recent decline in interest rates.
- India's first dry tailing plant at Zawar got commissioned, which will reduce land and water consumption as well as improve structural stability of the tailing dams. This plant will recycle more than 90% of the process water, leading to conservation of around 2,500 meter cube of water per day. Moreover, management planned to have similar plant at all mining locations going ahead.
- The lower tax rate is on account of revision of estimate for deferred tax liability pursuant to taxation law amendment ordinance 2019, leading to a reversal of Rs.365 Cr. related to prior years. Excluding this one time reversal, the effective tax rate for the quarter was 18.2%. Tax rate in FY20 is expected to be about 23% excluding impact of 1x deferred tax liability reversal.

Update on expansion projects

- Plant at Agucha, Rajasthan is ramping up based on the ore production growing around 30%.
- Plant at Zawar also performed with all protections up almost 25% along with better grades. Moreover, it achieved its highest mined metal in the month of September.
- Coal mines production volumes and grades affected in 1HFY20 on account of temporary geotech challenges. To mitigate from the same, a rapid development crew for faster declined development and additional levels are being open to dry production.
- SK mine and Wood job pushed by management to another step towards creating mine of the future by starting to track under on vehicles on a real-time basis for centralized control and monitoring. At SK mine centralized path scheduling and management has begun using onboard, connected tablets for seamless communication with underground mining crew. This will allow management for better utilization of equipment and resources, predictive maintenance and higher productivity.
- The project for converting copper matte to copper sulfate will commission in 3QFY20 and cadmium recovery project (for which company has partnered with global technology expert) is expected to commission in 4QFY20.
- Drilling of 85 km was carried out this year across all mines and 30 rigs have been deployed to achieve this year's target of adding 13 MT of resources and upgrading 34 million tons to reserves.
- At Zawar plant, special project was carried out includes 23 km of drilling this year for upgrading resources to reserves.
- Shaft project at Rampura, which is now at an advanced stage is expected to commission in 3QFY20.
- The debottlenecking of our smelters to 1.13 million tonnes will be completed in 3QFY20 and further debottlenecking to 1.2 million tonne is underway.

Exhibit: Net Sales and Growth Trend

Lower volumes and metal prices reduced revenue during the quarter.

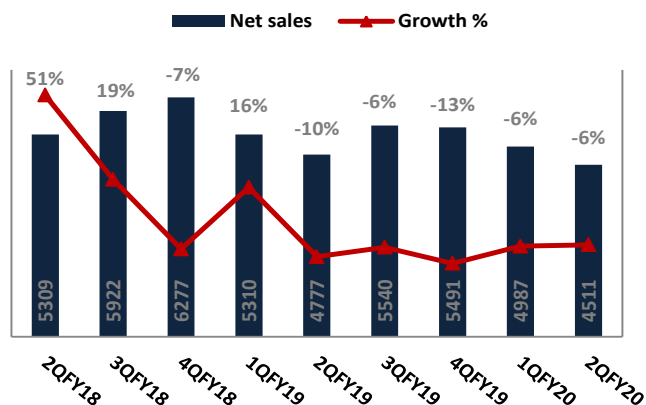


Exhibit: EBITDA and EBITDA Margin Trend

lower metal prices, higher power cost impacted EBITDA....

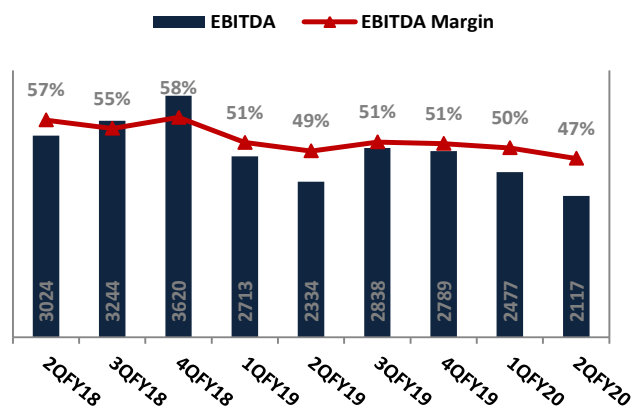


Exhibit: PAT and PAT Margin Trend

Higher other income and reduced PAT expanded the PAT margins

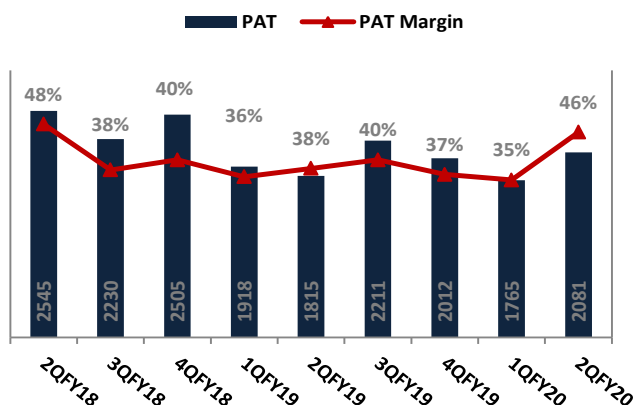


Exhibit: Total Mined Metal Production

Total ore production in the quarter was down and reduced the volume guidance for FY20.

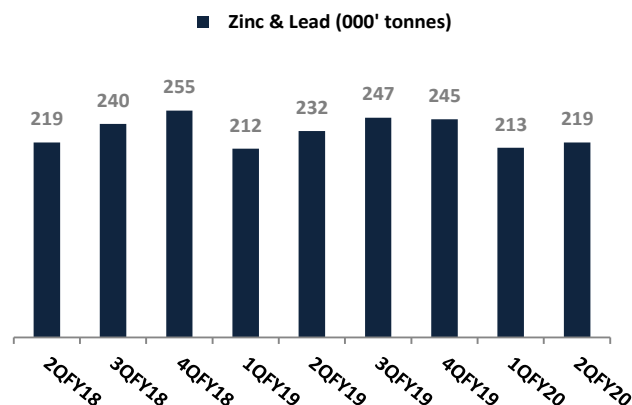


Exhibit: Zinc Volume and Realization Trend

zinc volume declined YoY and was lower QoQ, YoY realization down significantly....

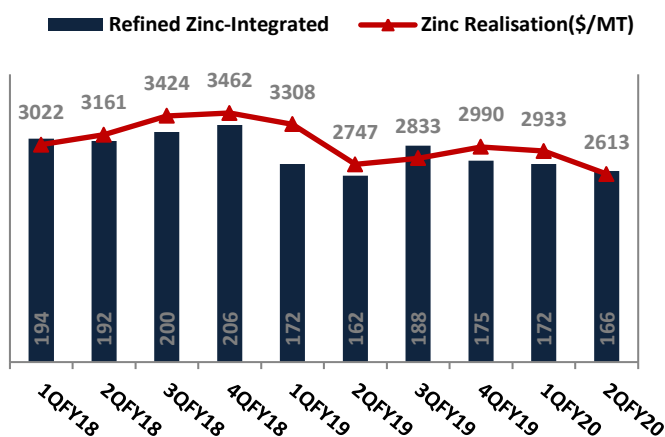


Exhibit: Lead Volume and Realization Trend

lead volume declined YoY growth and realization also reduced YoY....

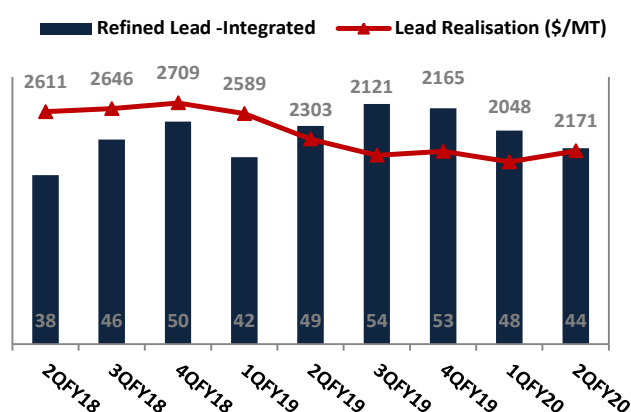


Exhibit: Silver Volume and Realiation Trend

silver volume has also been decreasing in line with decrease in lead volume.....

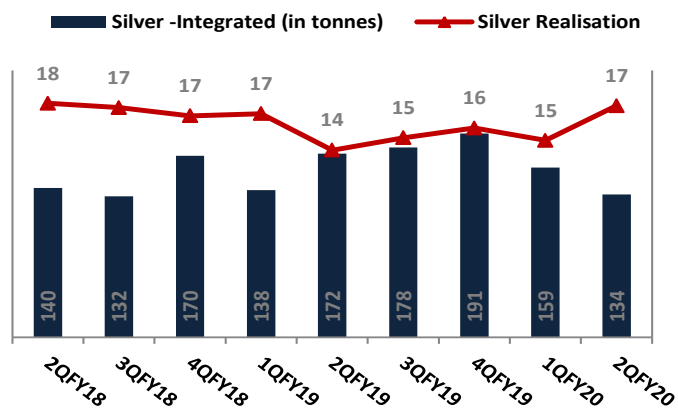


Exhibit: Zinc CoP Trend

higher power cost, lower grades, higher mine development and higher commodity prices impacted CoP.....

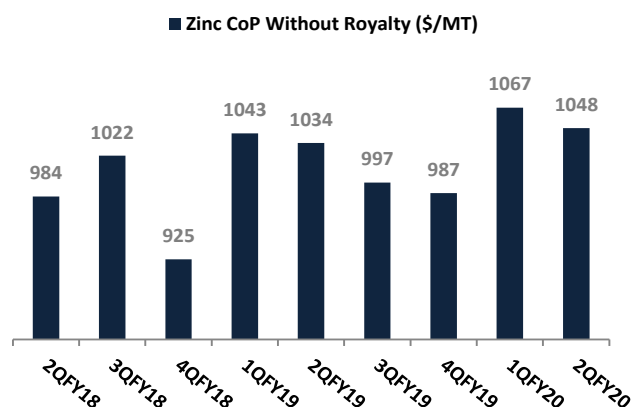


Exhibit: Zinc, Lead and Silver Price Trend

prices continue to remain low.....

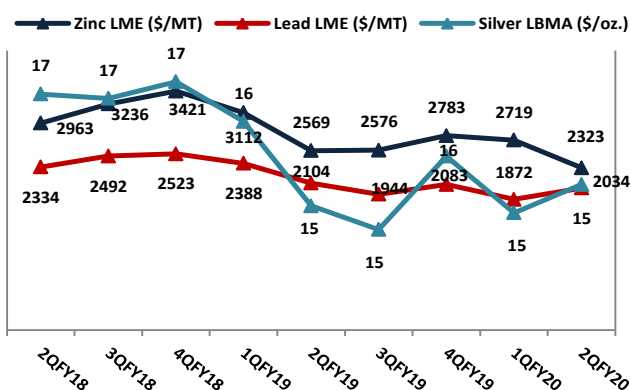


Exhibit: ROE Trend

ROE is expected to fall in FY20 as well....

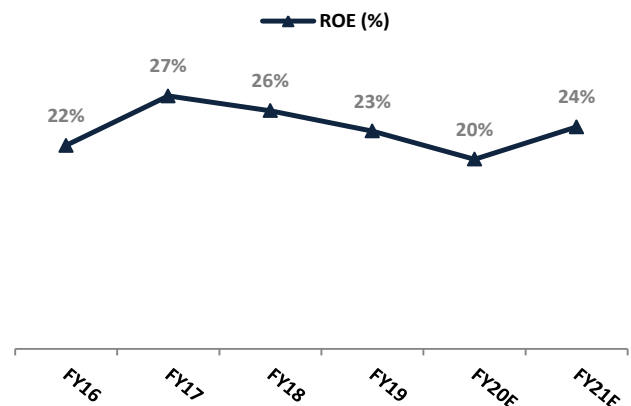
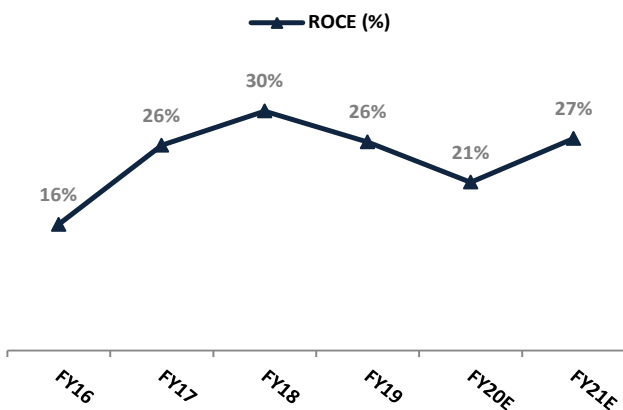


Exhibit: ROCE Trend

ROCE is also expected to follow the trend of ROE.....



Financial Details

Balance Sheet

	Fig. in Rs. Cr.							
Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Share Capital	845	845	845	845	845	845	845	845
Reserves	36,573	42,508	36,540	29,960	35,087	32,760	35,016	38,259
Networth	37,418	43,353	37,385	30,805	35,932	33,605	35,861	39,104
Debt	-	-	-	7,908	-	2,538	-	-
Other Non Cur Liab	56	132	563	556	792	945	945	945
Total Capital Employed	37,418	43,353	37,385	38,713	35,932	36,143	35,861	39,104
Net Fixed Assets (incl CWIP)	10,688	11,451	12,813	13,064	14,522	17,032	17,443	17,621
Non Cur Investments	3	-	-	-	-	-	-	-
Other Non Cur Asst	-	-	952	1,315	1,137	638	688	700
Non Curr Assets	13,630	15,788	16,282	17,146	18,789	20,886	21,015	21,537
Inventory	1,198	1,212	1,058	1,936	1,379	1,544	1,498	1,873
Debtors	400	659	107	136	184	196	169	170
Cash & Bank	3,031	3,532	53	8,380	1,964	23	107	56
Other Curr Assets	630	184	467	408	382	314	478	598
Curr Assets	28,046	33,204	36,913	34,649	24,143	21,572	21,458	25,504
Creditors	510	631	931	1,205	947	1,174	869	1,086
Provisions (both)	1,016	1,312	49	128	220	219	205	216
Other Curr Liab	1,018	1,046	3,504	2,327	1,713	2,397	1,571	1,964
Curr Liabilities	2,545	2,988	15,127	12,322	6,005	5,206	5,514	6,828
Net Curr Assets	25,502	30,216	21,786	22,327	18,138	16,366	15,944	18,676
Total Assets	41,677	48,992	53,195	51,795	42,932	42,458	42,472	47,041

Income Statement

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Revenue from Operation	13,636	14,788	14,181	17,273	22,084	21,118	20,256	25,321
Change (%)	7%	8%	-4%	22%	28%	-4%	-4%	25%
Other Income	1,899	2,821	2,763	2,474	1,751	1,782	1,545	1,828
EBITDA	6,900	7,420	6,652	9,739	12,272	10,670	9,618	11,354
Change (%)	6%	8%	-10%	46%	26%	-13%	-10%	18%
Margin (%)	51%	50%	47%	56%	56%	51%	47%	45%
Depr & Amor.	785	644	745	1,811	1,483	1,883	2,200	2,411
EBIT	6,115	6,775	5,907	7,928	10,789	8,787	7,417	8,943
Int. & other fin. Cost	45	24	17	202	283	113	54	-
EBT	7,970	9,573	8,653	10,200	12,257	10,456	8,908	10,771
Exp Item	-	3	30	-	240	-	-	-
Tax	1,065	1,392	448	1,884	3,221	2,500	1,659	2,585
Minority Int & P/L share of Ass.	-	-	-	-	-	-	-	-
Reported PAT	6,905	8,178	8,175	8,316	9,276	7,956	7,249	8,186
Adjusted PAT	6,905	8,181	8,205	8,316	9,036	7,956	7,249	8,186
Change (%)	0%	18%	0%	2%	12%	-14%	-9%	13%
Margin(%)	51%	55%	58%	48%	42%	38%	36%	32%

Financial Details

Key Ratios

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
ROE	18.45%	18.86%	21.86%	27.17%	25.59%	23.40%	20.08%	20.93%
ROCE	16.34%	15.63%	15.80%	25.74%	30.03%	26.15%	20.68%	22.87%
Asset Turnover	0.33	0.30	0.27	0.33	0.51	0.50	0.48	0.54
Debtor Days	12	11	16	3	3	3	3	3
Inv Days	32	32	30	27	41	23	27	27
Payable Days	14	14	16	24	25	16	20	16
Int Coverage	136.08	288.19	348.91	39.25	38.12	77.76	137.36	0.00
P/E	7.85	8.36	9.49	14.58	13.83	14.85	12.15	11.77
Price / Book Value	1.45	1.58	2.07	3.96	3.54	3.48	2.44	2.46
EV/EBITDA	4.16	5.07	6.35	9.23	8.55	9.12	7.09	6.47
FCF per Share	8.81	9.26	11.60	13.18	16.81	12.74	17.35	20.10
Div Yield	2.4%	2.3%	3.4%	10.2%	2.7%	7.2%	4.8%	4.4%

Cash Flow Statement

Fig. in Rs. Cr.

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
PBT	7,970	9,570	8,623	10,200	12,497	10,456	8,858	10,771
<i>(inc)/Dec in Working Capital</i>	125	95	1,632	198	494	671	489	484
<i>Non Cash Op Exp</i>	(979)	(2,101)	(1,982)	(483)	142	214	2,254	2,411
<i>Int Paid (+)</i>	45	24	10	191	283	113	54	-
<i>Tax Paid</i>	(1,645)	(2,033)	(1,822)	(2,338)	(3,028)	(2,560)	(1,659)	(2,585)
<i>others</i>								
CF from Op. Activities	5,471	5,531	6,451	7,577	9,837	8,781	9,943	11,081
<i>(inc)/Dec in FA & CWIP</i>	(1,748)	(1,617)	(1,550)	(2,008)	(2,733)	(3,400)	(2,611)	(2,589)
<i>Free Cashflow</i>	3,723	3,913	4,901	5,569	7,104	5,381	7,332	8,492
<i>(Pur)/Sale of Inv</i>	(6,825)	(2,285)	(5,692)	13,665	4,620	1,996	288	(3,600)
<i>others</i>								
CF from Inv. Activities	(3,955)	(3,807)	(3,236)	3,816	2,396	(1,092)	(2,323)	(6,189)
<i>inc/(dec) in NW</i>	-	-	-	-	-	-	-	-
<i>inc/(dec) in Debt</i>	-	-	-	7,900	(7,900)	2,536	(2,538)	-
<i>Int. Paid</i>	(45)	(24)	(10)	(183)	(280)	(208)	(54)	-
<i>Div Paid (inc tax)</i>	(1,532)	(1,879)	(3,204)	(18,972)	(10,469)	(11,958)	(4,943)	(4,943)
<i>others</i>								
CF from Fin. Activities	(1,577)	(1,902)	(3,214)	(11,255)	(18,649)	(9,630)	(7,535)	(4,943)
<i>Inc(Dec) in Cash</i>	(62)	(178)	1	138	(6,416)	(1,941)	84	(51)
<i>Add: Opening Balance</i>	290	228	50	51	8,380	1,964	23	107
Closing Balance	228	50	51	189	1,964	23	107	56

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