

MAY 04, 2017

UPDATE

Coverage view: **Attractive**

Price (₹): **280**

Target price (₹): **320**

BSE-30: **29,895**

Building momentum. Coal India commenced the new fiscal with a strong 6.7% yoy growth in coal dispatches (off a favorable base) in April 2017 reversing the inventory build-up seen in March 2017 and reflected in the 4% yoy decline in coal production. Volume trajectory for the month is aligned to expectations, though we remain watchful of realizations in coming months especially on account of continued uncertainty over the impact of coal mine de-gradation starting April 2017. Maintain ADD rating with an unchanged target price of ₹320/share.

Company data and valuation summary

Coal India

Stock data

52-week range (Rs) (high,low) 350-272

Market Cap. (Rs bn) 1,765.7

Shareholding pattern (%)

Promoters 79.8

FIs 6.9

MFs 1.8

Price performance (%)

Absolute (5.2) (14.3) 0.1

Rel. to BSE-30 (5.2) (19.0) (15.5)

Forecasts/Valuations

2017 2018E 2019E

EPS (Rs) 18.1 25.5 28.5

EPS growth (%) (20.0) 40.7 11.7

P/E (X) 15.4 10.9 9.8

Sales (Rs bn) 778.1 882.1 952.5

Net profits (Rs bn) 112.6 158.5 177.0

EBITDA (Rs bn) 145.1 190.0 205.5

EV/EBITDA (X) 9.9 7.3 6.5

ROE (%) 33.5 50.0 51.0

Div. Yield (%) 7.1 6.4 7.1

Strong growth in coal dispatches accommodated by aggressive inventory draw down

Coal India reported strong 6.7% yoy growth in coal dispatches at 45.3 mn tons for April 2017 with double-digit growth in four out of seven subsidiaries, aided by a weak base period with dispatches in April 2016 declining 2.5% yoy. Coal production lagged significantly at 38.5 mn tons with a 4% yoy decline in production volumes during the year. BCCL (-11% yoy), MCL (-6.7% yoy) and ECL (-5.8% yoy) were the laggards while CCL (+33% yoy), SECL (+16.8% yoy) and NLC (+10.7% yoy) reported strong double-digit growth in coal dispatches for April 2017. Interestingly, dispatches at BCCL have remained subdued since February 2017, after the company announced a price increase towards end-January 2017.

Auction premiums remain upbeat, coal-based capacities beginning to show fuel constraints

Stable prices of imported coal have kept e-auction premiums upbeat at 29% in March 2017, even as dispatches of coal to the power sector by Coal India remained tepid (-4.3% yoy). Interestingly, we see tightness in the demand-supply dynamics for coal as eight power plants had critical levels of inventory at end-April 2017—a marked departure from healthy inventory levels seen at power plants for a large part of the past two years. Coal-based generation also showed strength (+6.5% yoy) in March 2017 with improving capacity utilization during the month.

Uncertainty on impact of mine de-gradation likely to keep stock performance in check

The CMP already factors in the earnings drag from wage provision, though (1) weak volume profile in FY2016 and the momentum since 4QFY17, (2) revision in prices of coking coal, and (3) improving trends for e-auction make for a more promising FY2018. The de-grading of several coal mines since April 2017 poses new uncertainty owing to the lack of clarity on the impact already factored in, of grade slippages owing to third party sampling carried out through FY2017. Uncertainty on the grade slippage issue will likely subside only post results for 1QFY18, keeping stock performance in check in the interim.

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Exhibit 1: Coal India reported 6.7% yoy growth in dispatches in April 2017

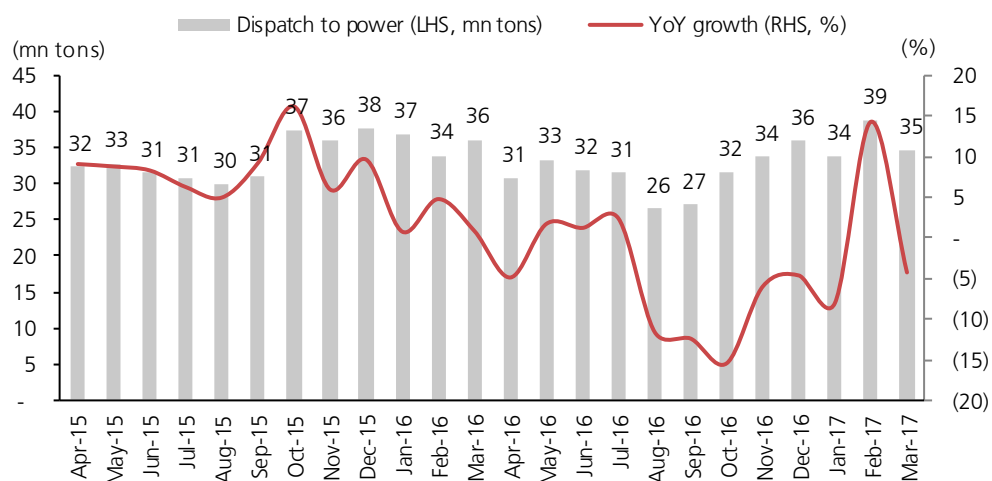
Subsidiary-wise monthly dispatch volumes, March fiscal year-ends (mn tons)

	Apr-17	Apr-16	Mar-17	Growth (%)		Annual			Quarterly		
				yoy	mom	2017	2016	(% chg.)	4QFY17	4QFY16	(% chg.)
Dispatches											
ECL	3.10	3.29	4.14	(5.8)	(25.1)	43.00	38.56	11.5	11.32	11.59	(2.3)
BCCL	2.68	3.01	3.16	(11.0)	(15.2)	34.91	36.14	(3.4)	9.43	9.53	(1.0)
CCL	5.30	3.98	6.57	33.2	(19.3)	60.93	59.61	2.2	18.80	15.27	23.1
NCL	7.11	6.42	8.01	10.7	(11.2)	83.45	78.52	6.3	23.14	21.33	8.5
WCL	3.53	3.21	4.24	10.0	(16.7)	39.46	42.31	(6.7)	12.43	10.82	14.9
SECL	12.44	10.65	13.14	16.8	(5.3)	137.39	136.60	0.6	38.46	35.72	7.7
MCL	11.07	11.87	12.95	(6.7)	(14.5)	143.03	139.74	2.4	37.59	38.63	(2.7)
NEC	0.06	0.01	0.09	500.0	(33.3)	0.78	0.39	100.0	0.22	0.11	100.0
CIL	45.29	42.45	52.30	6.7	(13.4)	542.91	532.33	2.0	151.38	143.04	5.8
Production											
ECL	2.72	2.65	4.62	2.6	(41.1)	40.53	40.21	0.8	11.95	14.12	(15.4)
BCCL	2.22	2.98	4.22	(25.5)	(47.4)	37.05	35.87	3.3	11.27	10.46	7.7
CCL	3.51	4.06	11.64	(13.5)	(69.8)	67.06	61.37	9.3	26.20	19.92	31.5
NCL	6.82	6.62	8.86	3.0	(23.0)	84.11	80.22	4.8	24.90	23.75	4.8
WCL	2.77	2.66	8.20	4.1	(66.2)	45.63	44.82	1.8	18.88	14.51	30.1
SECL	10.10	10.27	14.81	(1.7)	(31.8)	139.75	135.67	3.0	42.51	39.50	7.6
MCL	10.28	10.84	13.57	(5.2)	(24.2)	139.22	137.90	1.0	40.34	40.51	(0.4)
NEC	0.02	0.01	0.16	100.0	(87.2)	0.60	0.49	21.8	0.35	0.31	10.5
CIL	38.44	40.09	66.07	(4.1)	(41.8)	553.87	536.50	3.2	176.36	163.06	8.2

Source: Company, Kotak Institutional Equities

Exhibit 2: Monthly dispatches to power sector were down 4% yoy in March 2017

Monthly trend of coal dispatches to power sector, March fiscal year-ends, Apr-2015 - Mar-2017



Source: Ministry of Power, Kotak Institutional Equities

Exhibit 3: Inventory days are significantly lower at 16 days compared to average of 24 days during the same period last year
Inventory position of coal across power plants in India, March fiscal year-ends, 2017-18

	Apr-2017			Mar-2017			Feb-2017		
	Days	Critical (#)	Super-Critical (#)	Days	Critical (#)	Super-Critical (#)	Days	Critical (#)	Super-Critical (#)
North	28	—	—	31	—	—	25	1	—
West	11	3	3	14	—	—	15	—	—
South	13	1	1	14	1	—	13	1	1
East	15	—	—	17	—	—	15	—	—
All India	16	4	4	19	1	—	17	2	1

	Apr-2016			Mar-2016			Feb-2016		
	Days	Critical (#)	Super-Critical (#)	Days	Critical (#)	Super-Critical (#)	Days	Critical (#)	Super-Critical (#)
North	29	—	—	33	—	—	27	—	—
West	23	—	—	25	—	—	25	—	—
South	24	—	—	26	—	—	27	—	—
East	21	—	—	25	—	—	21	—	—
All India	24	—	—	27	—	—	24	—	—

Source: CEA, Kotak Institutional Equities

Exhibit 4: Coal-based generation grew at 6.5% yoy in March 2017

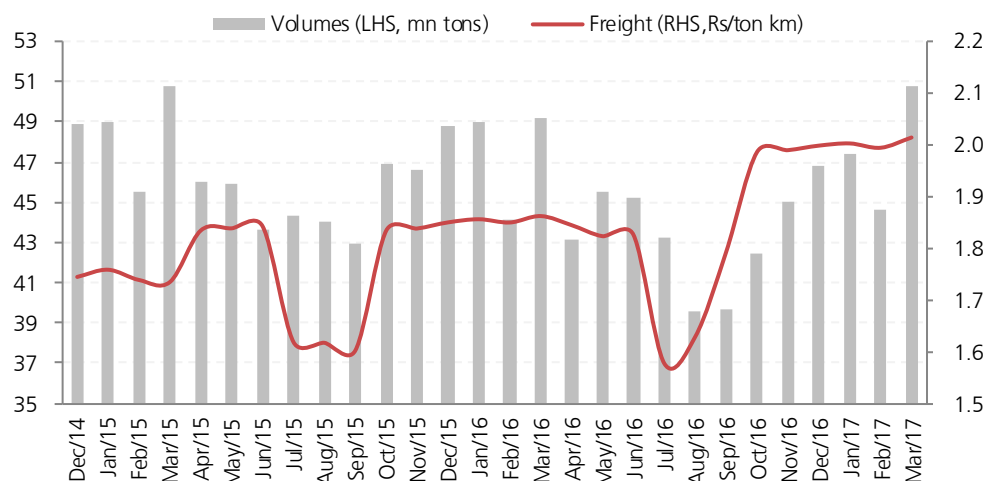
Key details of installed capacity, generation and PLF in India, March fiscal year-ends

	Monthly			Annual		
	Mar-17	Mar-16	yoy (%)	Mar-17	Mar-16	yoy (%)
Overall						
Installed capacity (MW)	319,606	298,059	7.2	319,606	298,059	7.2
Generation (MU)	101,690	96,593	5.3	1,152,511	1,102,245	4.6
PLF (%)	52.7	50.0	261 bps	50.3	51.7	-137 bps
Coal						
Installed capacity (MW)	192,163	185,173	3.8	192,163	185,173	3.8
Generation (MU)	83,025	77,973	6.5	909,231	861,551	5.5
PLF (%)	62.6	58.4	415 bps	57.4	59.7	-221 bps

Source: CEA, Kotak Institutional Equities

Exhibit 5: Railways freights grew 3% yoy in March 2017

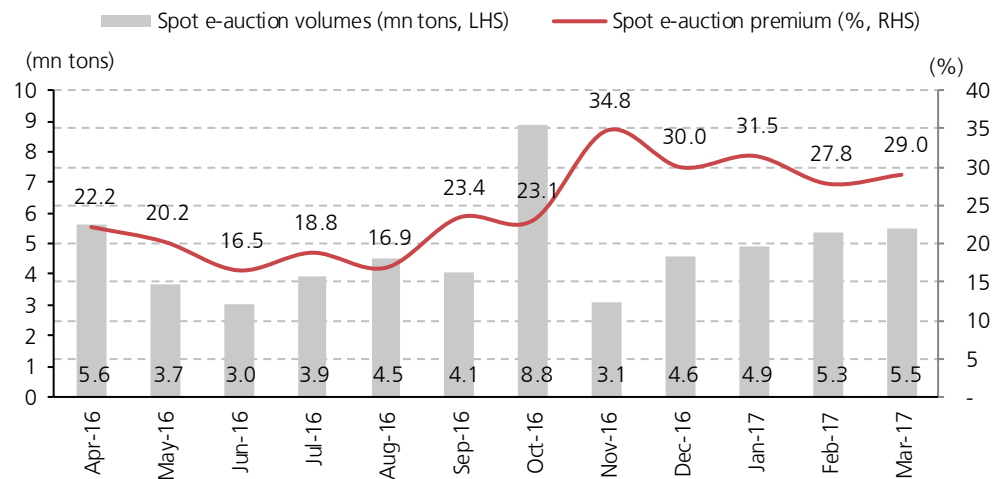
Volume and freight rates for coal movement by railway (mn tons, Rs/ton km)



Source: Indian Railways, Kotak Institutional Equities

Exhibit 6: Spot e-auction premiums remained at 29% in March 2017

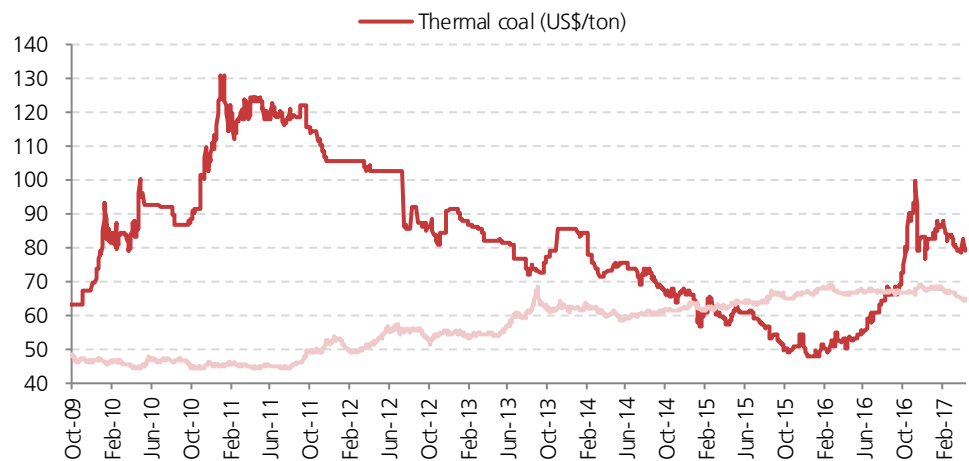
Monthly trend in spot coal volumes and premium for Coal India, March fiscal year-ends, Apr-2016 - Mar-2017



Source: Ministry of Power, Kotak Institutional Equities

Exhibit 7: Imported coal prices have improved significantly since March 2016

Trend in price of imported coal, March fiscal year-ends, Oct-2009 - Jan-2017



Source: Bloomberg, Kotak Institutional Equities

Exhibit 8: Our earnings assumptions factor 7% yoy growth in volumes for FY2018E

Key operational and financial assumptions, March fiscal year-ends, 2015-19E (Rs mn)

	2015	2016	2017E	2018E	2019E	Growth (%)				
						2015	2016	2017E	2018E	2019E
Volumes (mn tons)	489	534	542	580	612	4	9	1	7	5
Realization (Rs/ton)	1,472	1,415	1,396	1,482	1,518	1	(4)	(1)	6	2
Revenue (Rs mn)	720,146	756,443	756,207	859,160	928,271	5	5	(0)	14	8
Employee costs	(298,741)	(296,598)	(328,605)	(346,403)	(365,404)	8	(1)	11	5	5
Overburden	(38,267)	(28,114)	(26,091)	(28,890)	(32,120)	16	(27)	(7)	11	11
EBITDA	172,569	181,791	145,113	189,985	205,518	(2)	5	(20)	31	8
PAT	137,216	142,329	112,618	158,505	176,990	(9)	4	(21)	41	12
EBITDA margins	24	24	19	22	22	(7)	0	(20)	15	0
EBITDA (Rs/ton)	353	340	268	328	336	(6)	(4)	(21)	22	3

Source: Company, Kotak Institutional Equities estimates

Exhibit 9: We arrive at the SOTP value of Rs320/share

	2019E
EBITDA	206
Adj EBITDA (ex OBR adjustment)	238
PAT	177
Adjusted PAT (ex OBR adjustment and interest income)	152
EPS	29
Adj EPS (ex OBR adjustment and interest income)	25
P/E on core earnings	10
Value of core business (Rs/share)	251
Net cash (Rs bn)	424
Net cash (Rs/share)	68
Target price (Rs/share)	320

Notes:

- (a) Adjusted EBITDA is calculated after removing the effect OBR adjustment.
 (b) Adjusted PAT is calculated after removing the effect of OBR adjustment and interest income net of taxes.

Source: Kotak Institutional Equities estimates

Exhibit 10: Profit model, balance sheet, cash model of Coal India, March fiscal year-ends, 2012-19E (Rs mn)

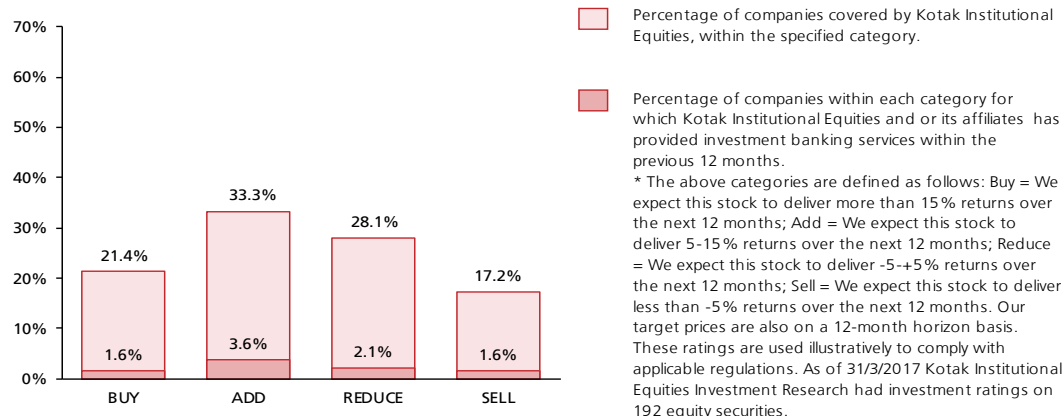
	2012	2013	2014	2015	2016	2017E	2018E	2019E	2020E
Profit model									
Net sales	624,154	683,027	688,100	720,146	756,443	756,207	859,160	928,271	983,882
Transport and loading recovery	13,760	14,690	16,976	20,270	22,386	21,112	22,518	23,731	24,537
Total income	641,726	692,778	704,150	745,721	793,271	778,145	882,099	952,496	1,008,865
EBITDA	170,439	195,527	176,608	172,569	181,791	145,113	189,985	205,518	209,374
Interest income	59,588	61,108	58,084	55,775	48,042	40,981	55,787	68,001	85,354
Other Income (ex transport, interest)	2,021	11,669	14,634	10,716	10,515	12,092	12,092	12,092	12,092
Interest expense	(540)	(452)	(580)	(73)	(207)	(3,027)	(3,037)	(3,037)	(3,037)
Depreciation	(19,692)	(18,130)	(19,964)	(23,198)	(24,664)	(26,955)	(27,590)	(27,590)	(27,590)
Pretax profits	211,815	249,722	228,781	215,789	215,476	168,204	227,236	254,983	276,193
Tax	(64,969)	(76,227)	(77,679)	(78,573)	(73,148)	(55,586)	(68,731)	(77,994)	(85,520)
Net income	146,846	173,495	151,102	137,216	142,329	112,618	158,505	176,990	190,673
Extraordinary items	1,036	69	14	51	415	—	—	—	—
Reported profit	147,882	173,564	151,116	137,267	142,743	112,618	158,505	176,990	190,673
Earnings per share (Rs)	23	27	24	22	23	18	26	29	31
Balance sheet									
Paid-up common stock	63,164	63,164	63,164	63,164	63,164	62,074	62,074	62,074	62,074
Total shareholders' equity	404,530	484,720	424,045	403,531	338,976	270,579	299,280	331,328	365,853
Minority interest	536	636	636	658	1,048	1,048	1,048	1,048	1,048
Total borrowings	15,274	12,017	1,778	4,083	11,988	1,374	1,374	1,374	1,374
Shifting and rehab fund	19,770	23,059	25,200	29,044	31,777	31,777	31,777	31,777	31,777
Total liabilities and equity	440,110	520,432	451,659	437,317	383,788	304,778	333,479	365,526	400,051
Net fixed assets	134,403	134,657	145,949	161,150	183,608	214,153	226,563	238,973	241,383
Capital work-in progress	29,034	34,960	45,053	51,594	58,942	60,644	67,644	74,646	81,657
Investments	19,814	23,950	37,749	28,134	29,019	29,019	29,019	29,019	29,019
Cash	582,028	622,360	523,895	530,925	383,128	330,262	378,860	425,597	486,999
Current assets (excl. cash)	292,247	377,171	270,060	314,015	427,055	380,702	403,580	422,464	437,860
Current liabilities and provisions	629,356	695,216	590,765	668,098	718,408	732,792	798,145	854,851	910,744
Deferred tax asset	11,941	22,550	19,717	19,596	20,445	22,789	25,957	29,677	33,877
Misc. expenditure	—	—	—	—	—	—	—	—	—
Total assets	440,110	520,432	451,659	437,317	383,788	304,778	333,479	365,526	400,051
Free cash flow									
Operating cash flow, excl. working capital	164,366	188,762	172,519	163,355	165,021	137,229	182,927	200,860	214,063
Working capital changes	73,721	(19,064)	2,660	33,378	(62,730)	60,736	42,475	37,822	40,497
Capital expenditure	(20,606)	(15,068)	(28,958)	(45,650)	(43,450)	(59,203)	(47,000)	(47,002)	(37,010)
Investments	(9,177)	(4,136)	(13,799)	9,615	(885)	—	—	—	—
Free cash flow	208,304	150,494	132,422	160,698	57,957	138,763	178,402	191,679	217,549
Ratios									
Net debt/equity (%)	(140)	(126)	(123)	(131)	(109)	(122)	(126)	(128)	(133)
Return on equity (%)	40	39	33	33	38	37	56	56	55
Book value per share (Rs)	64	77	67	64	54	44	48	53	59
ROCE (%)	39	40	35	35	39	39	59	59	57

Source: Company, Kotak Institutional Equities estimates

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Source: Kotak Institutional Equities

As of March 31, 2017

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In case you require any clarification or have any concern, kindly write to us at below email ids:

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