

# VEDANTA

## Mixed picture awaits

India Equity Research | Metals and Mining

We expect Vedanta to benefit from cost control at aluminium (Al) division and higher volumes at oil & gas division in FY20, despite lower base metal prices, due to: 1) Q1FY20 hot metal cost expected at INR1,700-1,750/t compared to USD1,935/t in Q1FY18 and USD1,776/t in Q4FY19; and 2) 15koept additional volume Q2FY20 onwards from commissioning of the RDG early gas facility. Additionally, integration of shaft at SK mine will add 3.75mtpa of hauling capacity, thus boosting the mine's capacity to 6mtpa. On the flip side, lower LME zinc and steel prices are expected to keep performance muted. Maintain 'HOLD' with TP of INR175/share. The stock is currently trading at 3.8x FY21E EBITDA.

### Cost control at Al division and potential uptick in oil & gas

We expect Vedanta's Al business to remain unaffected by lower LME Al, benefitting from cost reduction initiatives and non-integrated business model. As a result of record alumina production of 152kt in April, Lanjigarh CoP remaining in line with Q4FY19 level (USD290/t) and falling spot alumina prices, we estimate Al CoP/t at USD1,700-1,750/t, slightly lower than Q4FY19 level of USD1,776/t. In case of the oil & gas division, management expects the RDG early gas facility to add 15kboept to production Q2FY20 onwards, which will help Vedanta meet its 200-220kboept FY21 guidance.

### Lower commodity prices likely to play spoilsport

Despite SK mine's capacity reaching 6.5mt as a result of addition of 3.75mtpa hauling capacity, we expect lower LME zinc prices to play spoilsport both at Zinc-India and Zinc-International operations. On the steel front as well, margin is likely to drift lower as a result of higher iron ore prices and static steel prices.

### Outlook and valuation: LME Zn plays spoilsport; maintain 'HOLD'

Going ahead, we expect performance at Al and oil & gas divisions to improve owing to cost control and higher production, respectively. However, lower LME Zn prices are expected to dent overall EBITDA. We maintain 'HOLD/SP' with TP of INR175/share, implying an exit multiple of 3.9x FY21E EBITDA.

#### Financials

(INR mn)

Year to March	FY18	FY19E	FY20E	FY21E
Net revenue	918,660	920,480	958,703	1,007,982
EBITDA	248,620	231,030	274,764	293,407
Adjusted Profit	123,690	72,939	81,084	91,206
Diluted equity shares (mn)	3,717	3,717	3,717	3,717
Adjusted diluted EPS (INR)	33.3	19.6	21.8	24.5
EPS Growth (%)	39.9	(41.0)	11.2	12.5
Diluted P/E (x)	4.9	8.4	7.4	6.6
EV/EBITDA (x)	4.2	4.7	4.0	3.8
ROAE (%)	20.5	12.7	13.9	14.6

#### EDELWEISS 4D RATINGS

Absolute Rating	HOLD
Rating Relative to Sector	Performer
Risk Rating Relative to Sector	Medium
Sector Relative to Market	Underweight

#### MARKET DATA (R: VDAN.BO, B: VEDL IN)

CMP	: INR 164
Target Price	: INR 175
52-week range (INR)	: 247 / 146
Share in issue (mn)	: 3,717.2
M cap (INR bn/USD mn)	: 610 / 9,028
Avg. Daily Vol.BSE/NSE('000)	: 944.7

#### SHARE HOLDING PATTERN (%)

	Current	Q3FY19	Q2FY19
Promoters *	50.1	50.1	50.1
MF's, FI's & BK's	18.9	18.9	17.8
FII's	15.8	15.8	16.6
Others	15.1	15.1	15.5
* Promoters pledged shares (% of share in issue)	:		NIL

#### PRICE PERFORMANCE (%)

	Stock	Nifty	#N/A
1 month	(17.6)	(2.6)	1.7
3 months	0.8	3.1	(5.2)
12 months	(44.4)	5.2	(5.0)

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### Company Description

Vedanta Limited is a natural resource company engaged in the business of manufacturing copper and copper products, and aluminum and aluminum products. The Company's segments include Copper, which consists of manufacturing of copper cathode, continuous cast copper rod and anode slime, including from purchased concentrate and manufacturing of precious metal from anode slime, sulfuric acid, phosphoric acid; Iron ore; Aluminium, which consists of manufacturing of alumina and various aluminum products; Power, which consists of power, including power facilities engaged in generation and sale of commercial power, and Other, which consists pig iron and metallurgical coke. Its iron ore business consists of iron ore exploration, mining, beneficiation and exports. The Company has iron ore mining operations in the States of Goa and Karnataka. Its copper business consists of custom smelting.

### Investment Theme

VEDL's portfolio of resources business provides advantages of scale, diversification and strong balance sheet. The company benefits from ownership of low cost, cash rich oil & gas (Cairn) and zinc-lead-silver (HZL) businesses. It has globally competitive unit production costs in zinc, led by its quality captive mines. This aspect will help the company better withstand margin pressures during price downturns. However, we see operating leverage potential being undermined as Zinc prices have likely peaked. In addition, capital allocation risks are likely to keep stock performance muted.

### Key Risks

Capital allocation

Fall in zinc prices or premiums.

Decline in LME aluminium price or premiums

Cairn: Exploration failure, reinvestment of cash generated into low return assets

HZL: Lack of volume growth or increase in cash cost

Lower than expected average tariffs.

## Financial Statements

### Key Assumptions

Year to March	FY18	FY19	FY20E	FY21E
<b>Macro</b>				
GDP(Y-o-Y %)	6.7	7.1	7.1	7.3
Inflation (Avg)	3.6	3.7	4.0	4.5
Repo rate (exit rate)	6.0	6.3	5.8	5.8
USD/INR (Avg)	64.5	70.0	72.0	72.0
<b>Sector</b>				
Aluminium LME (USD/t)	2,045.3	2,036.5	1,807.6	1,790.0
Zinc LME (USD/t)	3,048.8	2,695.2	2,446.2	2,333.8
Lead LME (USD/t)	2,300.0	2,327.4	1,768.0	1,768.0
Copper Tc/Rc (c/lb)	22.5	21.5	18.5	18.5
<b>Company</b>				
HZL-Zn production (tpa)	791,000	751,200	880,610	987,600
HZL-PB production (tpa)	168,000	199,800	203,500	231,250
HZL-Ag production (tpa)	558,000	650,000	750,000	780,000
SA-Cu production (tpa)	400,000	200,000	400,000	-
BALCO-Al production(tpa)	569,000	571,000	579,000	579,000
VAL-Al production (tpa)	1,106,000	1,388,000	1,357,000	1,420,000
Intl Zn production (tpa)	118	108	306	336
Intl PB production (tpa)	53	36	25	24
HZL-Zn premium (USD/t)	227	150	150	150
HZL-PB premium (USD/t)	160	120	120	120
BALCO tariff (INR/unit)	3.2	3.6	3.2	3.2
SEL tariff (INR/unit)	2.3	2.4	2.2	2.2
HZL-mfg cost (INR/t)	61,429	66,853	67,045	67,454
BALCO-Power cost (INR/u)	3.5	3.5	-	-
VAL-Alumina cost (INR/t)	21,000	22,500	18,865	17,747
VAL-Smelting cost(INR/t)	79,600	90,600	88,416	86,126
Intl Zinc-cost (USD/t)	1,603	1,912	1,476	1,443
SEL-Fuel cost (INR/unit)	2.8	4.3	4.9	4.9
Employee exp growth (%)	6.7	21.1	5.0	5.0
Increase in SG&A exp (%)	20.9	23.3	1.5	1.5
Avg. Interest rate (%)	8.7	9.0	9.0	9.0
Depreciation rate (%)	4.0	4.0	4.9	4.9
Tax rate (%)	31.7	39.9	39.9	39.9
Dividend payout (%)	96.1	263.8	101.9	76.8
Capex (INR mn)	75,169	98,570	100,800	100,800
Net borrowings (INR mn)	262,440	324,160	312,946	290,269
Debtor days	15	16	18	20
Inventory days	122	176	195	189
Payable days	205	246	263	254
Cash conversion cycle	(68)	(54)	(50)	(45)

### Income statement

(INR mn)

Year to March	FY18	FY19	FY20E	FY21E
Net revenue	918,660	920,480	958,703	1,007,982
Materials costs	318,020	260,780	248,512	271,506
Employee costs	24,960	30,230	31,742	33,329
Total operating expenses	670,040	689,450	683,939	714,575
EBITDA	248,620	231,030	274,764	293,407
Depreciation	62,830	81,920	87,699	92,638
EBIT	185,790	149,110	187,065	200,768
Less: Interest Expense	51,120	56,890	53,322	54,046
Add: Other income	32,050.00	40,180.00	18,668.64	19,987.97
Profit Before Tax	195,690	135,600	152,411	166,711
Less: Provision for Tax	58,770	38,620	44,462	48,346
Extraordinary item	28,970	3,200	-	-
Minority interest	33,500	26,330	26,865	27,158
Reported Profit	103,420	70,650	81,084	91,206
Adjusted Profit	123,690	72,939	81,084	91,206
Shares o/s (mn)	3,717	3,717	3,717	3,717
Basic EPS (INR)	33.3	19.6	21.8	24.5
Diluted shares o/s (mn)	3,717	3,717	3,717	3,717
Adjusted Diluted EPS	33.3	19.6	21.8	24.5
Dividend per share (DPS)	20.0	18.9	18.9	18.9
Dividend Payout Ratio(%)	96.1	263.8	102.6	76.8
Tax rate (%)	30.0	28.5	28.5	28.5

### Common size metrics

Year to March	FY18	FY19	FY20E	FY21E
Operating expenses	72.9	74.9	71.3	70.9
Depreciation	6.8	8.9	9.1	9.2
Interest Expense	5.6	6.2	5.6	5.4
EBITDA margins	27.1	25.1	28.7	29.1
Net Profit margins	17.1	10.8	11.3	11.7

### Growth ratios (%)

Year to March	FY18	FY19	FY20E	FY21E
Revenues	27.2	0.2	4.2	5.1
EBITDA	16.5	(7.1)	18.9	6.8
Adjusted Profit	75.4	(41.0)	11.2	12.5
EPS	39.9	(41.0)	11.2	12.5

# Metals and Mining

Balance sheet		(INR mn)			
As on 31st March	FY18	FY19	FY20E	FY21E	
Share capital	3,720	3,720	3,720	3,720	
Reserves & Surplus	629,400	619,250	578,630	589,155	
Shareholders' funds	633,120	622,970	582,350	592,875	
Minority Interest	159,610	152,270	178,598	205,756	
Long term borrowings	267,890	347,210	347,210	347,210	
Short term borrowings	219,510	229,820	229,820	229,820	
Total Borrowings	487,400	577,030	577,030	577,030	
Long Term Liabilities	70,580	86,730	86,730	86,730	
Def. Tax Liability (net)	42,180	44,840	44,840	44,840	
<b>Sources of funds</b>	<b>1,392,890</b>	<b>1,483,840</b>	<b>1,469,547</b>	<b>1,507,231</b>	
Gross Block	1,633,840	1,739,379	1,836,879	1,934,379	
Net Block	793,300	955,150	959,440	967,602	
Capital work in progress	161,400	222,360	222,360	222,360	
Intangible Assets	168,640	36,050	36,050	36,050	
Total Fixed Assets	1,123,340	1,213,560	1,217,850	1,226,012	
Non current investments	171,370	208,590	208,590	208,590	
Cash and Equivalents	337,520	365,430	376,644	399,321	
Inventories	119,670	131,980	134,128	146,539	
Sundry Debtors	39,690	39,820	52,532	55,232	
Loans & Advances	820	820	820	820	
Other Current Assets	53,440	60,230	60,230	60,230	
Current Assets (ex cash)	213,620	232,850	247,710	262,821	
Trade payable	178,430	173,520	184,520	192,786	
Other Current Liab	274,530	363,070	363,070	363,070	
Total Current Liab	452,960	536,590	547,590	555,856	
Net Curr Assets-ex cash	(239,340)	(303,740)	(299,880)	(293,035)	
<b>Uses of funds</b>	<b>1,392,890</b>	<b>1,483,840</b>	<b>1,469,547</b>	<b>1,507,231</b>	
BVPS (INR)	170.3	167.6	156.7	159.5	

Free cash flow		(INR mn)			
Year to March	FY18	FY19	FY20E	FY21E	
Reported Profit	103,420	70,650	81,084	91,206	
Add: Depreciation	62,830	81,920	87,699	92,638	
Interest (Net of Tax)	35,768	40,687	38,136	38,653	
Others	321,952	85,262	(18,083)	(25,185)	
Less: Changes in WC	158,291	68,050	(3,860)	(6,845)	
Operating cash flow	365,678	210,469	192,695	204,158	
Less: Capex	75,169	98,570	100,800	100,800	
<b>Free Cash Flow</b>	<b>290,509</b>	<b>111,899</b>	<b>91,895</b>	<b>103,358</b>	

## Peer comparison valuation

Name	Market cap (USD mn)	Diluted P/E (X)		EV / EBITDA (X)		ROAE (%)	
		FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Vedanta	9,028	7.4	6.6	4.0	3.8	13.9	14.6
Hindalco Industries	6,377	10.7	11.0	6.1	5.7	6.8	6.1
National Aluminium Co Ltd	1,312	8.3	7.7	2.9	2.4	10.1	10.5
Median	-	8.3	7.7	4.0	3.8	10.1	10.5
AVERAGE	-	8.8	8.4	4.3	4.0	10.3	10.4

Source: Edelweiss research

Cash flow metrics					
Year to March	FY18	FY19	FY20E	FY21E	
Operating cash flow	365,678	210,469	192,695	204,158	
Financing cash flow	(115,181)	23,949	(80,681)	(80,681)	
Investing cash flow	(79,046)	(3,230)	(100,800)	(100,800)	
Net cash Flow	171,451	231,189	11,214	22,677	
Capex	(75,169)	(98,570)	(100,800)	(100,800)	
Dividend paid	(80,681)	(84,491)	(80,681)	(80,681)	

## Profitability and efficiency ratios

Year to March	FY18	FY19	FY20E	FY21E
ROAE (%)	20.5	12.7	13.9	14.6
ROACE (%)	15.9	14.4	15.3	16.3
Inventory Days	122	176	195	189
Debtors Days	15	16	18	20
Payable Days	205	246	263	254
Cash Conversion Cycle	(69)	(54)	(50)	(45)
Current Ratio	1.2	1.1	1.1	1.2
Gross Debt/EBITDA	2.0	2.5	2.1	2.0
Gross Debt/Equity	0.6	0.7	0.8	0.7
Adjusted Debt/Equity	0.6	0.7	0.8	0.7
Net Debt/Equity	0.2	0.3	0.3	0.2
Interest Coverage Ratio	3.6	2.6	3.5	3.7

## Operating ratios

Year to March	FY18	FY19	FY20E	FY21E
Total Asset Turnover	0.6	0.6	0.6	0.7
Fixed Asset Turnover	1.0	0.9	1.0	1.0
Equity Turnover	1.2	1.2	1.2	1.3

## Valuation parameters

Year to March	FY18	FY19	FY20E	FY21E
Adj. Diluted EPS (INR)	33.3	19.6	21.8	24.5
Y-o-Y growth (%)	39.9	(41.0)	11.2	12.5
Adjusted Cash EPS (INR)	56.8	44.8	45.4	49.5
Diluted P/E (x)	4.9	8.4	7.4	6.6
P/B (x)	1.0	1.0	1.0	1.0
EV / Sales (x)	1.1	1.2	1.2	1.1
EV / EBITDA (x)	4.2	4.7	4.0	3.8
Dividend Yield (%)	12.2	11.5	11.5	11.5

## Additional Data

### Directors Data

Anil Agarwal	Chairman Emeritus	Navin Agarwal	Executive Chairman
Aman Mehta	Independent Director	Lalita D. Gupte	Independent Director
Ravi Kant	Independent Director	Priya Agarwal	Non-Executive Director
Tarun Jain	Wholetime Director	Arun Kumar GR	Whole-Time Director & Chief Financial Officer
UK Sinha	Independent Director	K Venkataramanan	Independent Director

Auditors - S. R. Batliboi & Co LLP

*\*as per last annual report*

### Holding – Top10

	Perc. Holding		Perc. Holding
Twinstar holdings It	34.44	Finsider internation	10.8
Icici prudential ass	4.72	Hdfc asset managemen	2.65
Blackrock	1.79	Vanguard group	1.59
Dimensional fund adv	1.19	Westglobe ltd	1.19
Ptc cables pvt ltd	1.15	Welter trading ltd	1.03

*\*in last one year*

### Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
No Data Available				

*\*in last one year*

### Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
No Data Available			

*\*in last one year*

Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
Coal India	HOLD	SP	M	GMDC	BUY	SO	H
Hindalco Industries	BUY	SO	M	Hindustan Zinc	HOLD	SU	L
Jindal Stainless Ltd	BUY	SO	H	Jindal Steel & Power	BUY	SO	M
JSW Steel	HOLD	SP	M	NMDC	HOLD	SP	M
Steel Authority of India	REDUCE	SU	M	Tata Steel	HOLD	SP	M
Vedanta	HOLD	SP	M				

**ABSOLUTE RATING**

Ratings	Expected absolute returns over 12 months
Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

**RELATIVE RETURNS RATING**

Ratings	Criteria
Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
	Stock return < 1.25 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

**RELATIVE RISK RATING**

Ratings	Criteria
Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

**SECTOR RATING**

Ratings	Criteria
Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
	Sector return < 1.25 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return



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### Coverage group(s) of stocks by primary analyst(s): Metals and Mining

Coal India, GMDC, Hindalco Industries, Hindustan Zinc, Jindal Stainless Ltd, Jindal Steel & Power, JSW Steel, NMDC, Steel Authority of India, Tata Steel, Vedanta

#### Recent Research

Date	Company	Title	Price (INR)	Recos
17-Jun-19	Coal India	Ambitious production ramp up; <i>Company Update</i>	255	Hold
11-Jun-19	Metals & Mining	Euphoria likely to be short-lived; <i>Sector Update</i>		
10-Jun-19	Metals & Mining	Uneasy lies the calm; <i>Sector Update</i>		

#### Distribution of Ratings / Market Cap

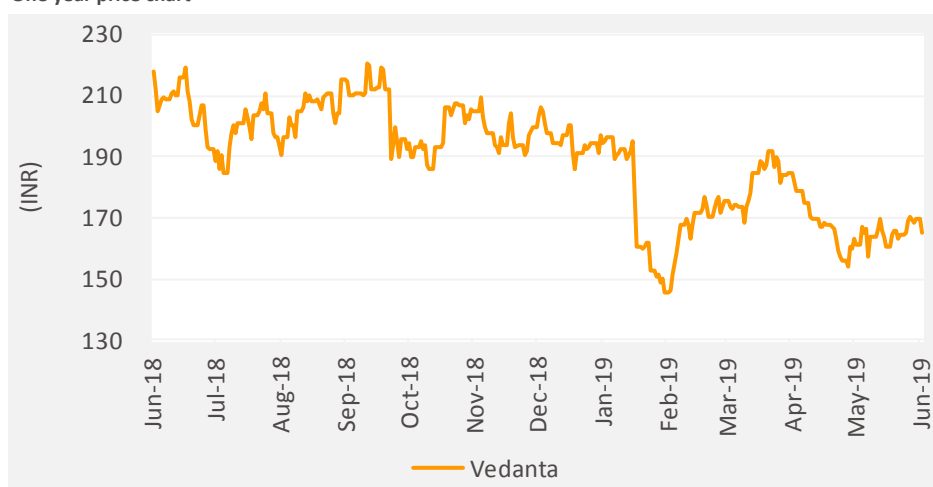
##### Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

#### Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

#### One year price chart



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