Stock Update

Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Coal India Ltd

Robust Q3; strong growth outlook and high dividend yield

Energy & Utilities	Sharekhan code: COALINDIA

Reco/View: Buy	↔	CMP: Rs. 163	Price Target: Rs. 190	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING 38.34

Updated Jan 08, 2022

High Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

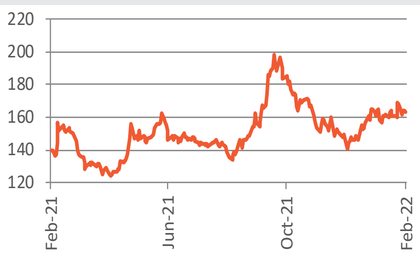
Company details

Market cap:	Rs. 1,01,212 cr
52-week high/low:	Rs. 204 / 123
NSE volume: (No of shares)	148.6 lakh
BSE code:	533278
NSE code:	COALINDIA
Free float: (No of shares)	208.7 cr

Shareholding (%)

Promoters	66.1
FII	6.6
DII	21.3
Others	6.0

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	1	6	18	17
Relative to Sensex	6	9	14	4

Sharekhan Research, Bloomberg

Summary

- Q3FY2022 results reflect strong recovery with sharp 20% beat in PAT at Rs. 4,558 crore, up 48% y-o-y/55% q-o-q, led by sharp improvement in e-auction realisation and control on employee cost.
- E-auction realisation was up 33% y-o-y/22% q-o-q to Rs. 1,947/tonne, while FSA realisations declined 0.9% q-o-q to Rs. 1,370/tonne. Coal offtake volume grew by 13% y-o-y/18% q-o-q to 174 mt (in line), led by strong 17% y-o-y rise in FSA volume offset by a 5% y-o-y decline in e-auction volume.
- CIL's growth outlook is improving with sustained focus to increase volume (offtake growth guidance of 17%/4% for FY2022/FY2023), better realisation (higher e-auction premium), and cost efficiencies. Diversification into solar generation, aluminium value chain, solar cell manufacturing, CBM, and coal gasification bode well for long-term growth.
- The stock trades at an attractive valuation of 4.8x its FY2023E EPS (close to trough valuation) and offers a high dividend yield of 12-13%. Hence, we maintain a Buy on the stock with a revised PT of Rs. 190.

Coal India Limited's (CIL) Q3FY2022 consolidated operating profit at Rs. 6,825 crore (up 32.2% y-o-y; up 73.1% y-o-y) was above our estimates of Rs. 5,489 crore due to higher e-auction realisation of Rs. 1,947/tonne (up 32.8% y-o-y; up 22.2% q-o-q) and lower-than-expected employee cost (stood at 34.9% in Q3FY2022 of revenue versus 51% in Q3FY2021 and 41% in Q2FY2022). This led to better-than-expected EBITDA margin of Rs. 393/tonne (up 17% y-o-y; up 46.9% q-o-q). Coal volume offtake was strong and grew by 12.9% y-o-y and 17.9% q-o-q to 174 million tonne (FSA/e-auction volume of 145mt/26mt, up/down 17%/-5% y-o-y/q-o-q), while FSA realisation stood at Rs. 1,370/tonne (up 1.1% y-o-y; down 0.9% q-o-q). PAT, at Rs. 4,558 crore (up 47.7% y-o-y; up 55.2% q-o-q) was 20% above our estimate of Rs. 3,804 crore, led by strong recovery in operating profit, partially offset by higher tax rate.

Key positives

- Strong growth of 33% y-o-y/22% q-o-q in e-auction realisation to Rs. 1,947/tonne.
- Robust growth in coal offtake volume by 13% y-o-y/18% q-o-q to Rs. 174 million tonne, led by higher FSA volume.
- Declared second interim of Rs. 5/share and, thus, taking total dividend of Rs. 14/share (implies dividend yield of 8.6%) so far in FY2022.

Key negatives

- Decline in e-auction volume by 5% y-o-y to 26 million tonne given high prices.

Management Commentary

- Upbeat FY2022 coal production/offtake guidance of 630mt/670mt implies an increase of 6%/17% y-o-y. FY2023 coal production/offtake target of 700mt/700mmt.
- E-auction premium at 60%/100% of FSA price in December 2021/January 2022 and the benefit of the same would be reflected in Q4FY2022/Q1FY2023.
- FY2022/FY2023 capex guidance of Rs. 15,000 crore/Rs. 17,000 crore. CIL has spent Rs. 10,500 crore in 9MFY2022.
- Cash balance/receivables improved to Rs. 29,138 crore/Rs. 13,428 crore as on December 31, 2021, versus Rs. 27,522 crore/Rs. 14,902 crore as on September 30, 2021. CIL expects receivable to be lower than Rs. 13,000 crore by March 2022.
- Wage negotiations are going on and management expects to conclude it by end-FY2023. CIL is making provision of Rs. 100 crore per month and plans to increase the same in the coming months. During the last wage revision, the cost went up by Rs. 4,500 crore.
- The company is in discussions with all stakeholders to implement FSA price hike and expects the same to happen soon as costs are rising.

Revision in estimates – We have increased our FY2022-FY2024 earnings estimates to factor higher volume/e-auction realisation.

Our Call

Valuation – Maintain Buy on CIL with a revised PT of Rs. 190: Improving earnings growth outlook (expect a 22% PAT CAGR over FY2021-FY2024E), high RoE of ~49%, and dividend yield of 12-13% make the stock's valuation attractive at 4.8x its FY2023E EPS (close to trough levels). Potential efficient capital allocation for non-core investments (aluminium smelting and solar energy projects) could act as key catalysts for the stock. We maintain our Buy recommendation on CIL with a revised price target (PT) of Rs. 190.

Key Risks

Lower-than-expected volume offtake amid any weakness in electricity demand given COVID-19 and realisations (especially for e-auction) could affect margins and earnings outlook. The government's divestment plan could act as an overhang on the stock.

Valuation (Consolidated) Rs cr

Particulars	FY21	FY22E	FY23E	FY24E
Revenue	90,026	1,02,657	1,09,427	1,16,850
OPM (%)	20.6	23.4	24.1	25.3
Adjusted PAT	12,700	17,835	21,016	23,225
% YoY growth	*-24.0*	*40.4*	*17.8*	*10.5*
Adjusted EPS (Rs.)	20.6	28.9	34.1	37.7
P/E (x)	7.9	5.6	4.8	4.3
P/B (x)	2.8	2.5	2.2	2.0
EV/EBITDA (x)	4.8	3.1	2.7	2.2
RoNW (%)	37.0	46.3	49.2	48.8
RoCE (%)	38.9	46.8	50.8	51.6

Source: Company; Sharekhan estimates

Robust recovery in Q3FY2022; PAT above estimates, led by higher e-auction realisation and efficient cost management

Q3FY2022 consolidated operating profit at Rs. 6,825 crore (up 32.2% y-o-y; up 73.1% y-o-y) was above our estimate of Rs. 5,489 crore due to higher e-auction realisation of Rs. 1,947/tonne (up 32.8% y-o-y; up 22.2% q-o-q) and lower-than-expected employee cost (stood at 34.9% of revenue in Q3FY2022 versus 51% in Q3FY2021 and 41% in Q2FY2022). This led to better-than-expected EBITDA margin of Rs. 393/tonne (up 17% y-o-y; up 46.9% q-o-q). Coal volume offtake was strong and grew by 12.9% y-o-y and 17.9% q-o-q to 174 million tonne (FSA/e-auction volume of 145mt/26mt, up/down 17%/-5% y-o-y/q-o-q) while FSA realisation stood at Rs. 1,370/tonne (up 1.1% y-o-y; down 0.9% q-o-q). PAT at Rs. 4,558 crore (up 47.7% y-o-y; up 55.2% q-o-q) was 20% above our estimate of Rs. 3,804 crore, led by strong recovery in operating profit, partially offset by higher tax rate.

Q3FY2022 key conference call highlights

- **Upbeat production and offtake guidance –** Management has guided for coal production/offtake volume of 630mt/670mt, which implies an increase of 6%/17% y-o-y in FY2022. For FY2023, CIL is optimistic of further increase in coal production/offtake target to 700mt/700mmt.
- **Rising e-auction premium -** Management mentioned that e-auction premium was at 60%/100% of FSA price in December 2021/January 2022 and the same would be reflected in Q4FY2022/Q1FY2023.
- **Capex guidance –** FY2022/FY2023 capex guidance of Rs. 15,000 crore/Rs. 17,000 crore. CIL has spent Rs. 10,500 crore in 9MFY2022.
- **Improving cash and reducing receivables -** Cash balance/receivables improved to Rs. 29,138 crore/Rs. 13,428 crore as on December 31, 2021, versus Rs. 27,522 crore/Rs. 14,902 crore as on September 30, 2021. CIL expects receivable to be lower than Rs. 13,000 crore by March 2022.
- **Update on employee wage negotiations –** CIL recently completed the third round of wage negotiations and expects to conclude the same by FY2023-end. CIL is making provisions of Rs. 100 crore per month and plans to increase the same in the coming months. During the last wage revision, the cost went up by Rs. 4,500 crore.
- **FSA price hike –** The company is in discussions with all stakeholders to implement FSA price hike and expects the same happen soon as costs are rising.
- **Focus on cost reduction –** 1) Target to reduce manpower by 5% p.a. or 15,000 p.a. for the next 5-10 years on FY2021 base of 2.6 lakh employees; and 2) implementing projects to increase mechanised evacuation from 150mtpa currently to 620mtpa and this could substantially reduce evacuation and transportation charges (currently at Rs. 3,800 crore p.a.).
- **Aluminium project update –** CIL has received approval from Odisha government for the plant and has applied for allocation of bauxite mine on nomination basis and will take a decision on the project post allocation of bauxite mine. Management indicated that the entire aluminium value chain is profitable. Overall, the investment plan is of ~Rs. 26,000 crore with combination of debt/equity and plan to induct a partner.
- **Foray into renewables energy –** CIL aims to set up a 3GW capacity by FY2024 and has won 100MW capacity at Rs. 2.2/kWh in GUVNL Tender and the project is under commissioning. Moreover, CIL is now in the list of companies for PLI Scheme of MNRE (IREDA) and should get benefit of the same.
- **Coal gasification –** Five surface coal gasification projects identified at Shilpanjal Pariyojana (WB), Project Utkarsh (MH), Dankuni (WB), Ashoka (JH), and Mahamaya SCG (CG). CIL is awaiting clarification with regards to the subsidy level from the government.
- **Other updates –** CIL is looking at opportunities for conversion of coal to ammonium nitrate and, if viable, CIL will put a tender for the same.

Results (Consolidated) Rs cr

Particulars	Q3FY22	Q3FY21	YoY (%)	Q2FY22	QoQ (%)
Revenue	**28,433**	**23,686**	**20.0**	**23,291**	**22.1**
Total Expenditure	21,608	18,521	16.7	19,349	11.7
Operating profit	**6,825**	**5,165**	**32.2**	**3,942**	**73.1**
Other Income	653	649	0.7	782	-16.5
Interest	132	155	-15.3	141	-6.9
Depreciation	1,041	916	13.7	934	11.4
PBT	**6,305**	**4,742**	**33.0**	**3,648**	**72.8**
Tax	1,746	1,658	5.3	711	145.7
PAT before share of profit from JVs and MI	4,560	3,084	47.9	2,938	55.2
Share of profit from JVs	-3	0		-5	-36.9
Minority interest	-2	-1		-4	-55.7
Reported PAT	**4,558**	**3,085**	**47.7**	**2,937**	**55.2**
O/S Shares (cr)	616	616		616	
Reported EPS (Rs.)	7.4	5.0	47.7	4.8	55.2
Margins (%)			**BPS**		**BPS**
OPM	24.0	21.8	220.0	16.9	707.9
NPM	16.0	13.0	300.5	12.6	342.2
Tax rate	27.7	35.0	-728.1	19.5	821.0

Source: Company; Sharekhan Research

Key operating performance

Particulars	Q3FY22	Q3FY21	YoY (%)	Q2FY22	QoQ (%)
Coal production (mt)	164	157	4.5	126	30.2
Coal offtake (mt)	174	154	12.9	147	17.9
Blended realisation (Rs./tonne)	1,496	1,411	6.0	1,444	3.6
FSA realisation (Rs./tonne)	1,370	1,354	1.1	1,382	-0.9
E-auction realisation (Rs./tonne)	1,947	1,466	32.8	1,594	22.2
Adjusted EBITDA excluding OBR (Rs./tonne)	425	413	2.9	282	50.9

Source: Company; Sharekhan Research

Outlook and Valuation

■ **Sector outlook – India's coal demand expected to reach 1,250-1,500 million tonne with rise in power generation**

Coal accounts for 55% of India's total commercial energy production. Although its share in India's overall energy mix is expected to fall over the next decade, it would remain a primary energy source and absolute coal offtake is expected to improve given higher demand from sectors such as power and steel. Industry estimates suggest that India's coal demand could reach 1,250-1,500 million tonne by FY2030, assuming 6-8% growth in power demand and despite considering growth in renewable energy capacity to 450 GW by FY20230 (from 123 GW in FY2019).

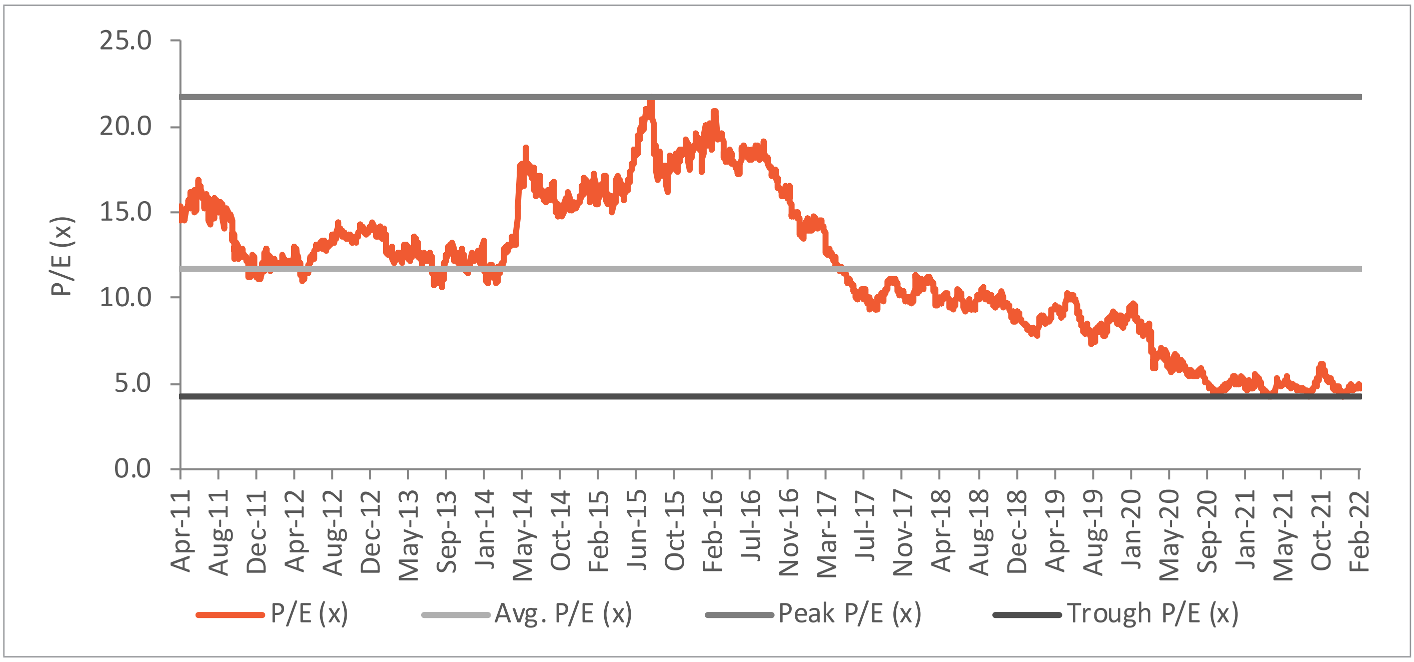
■ **Company outlook – Improving volume and likely higher realisation to drive earnings recovery**

CIL's earnings outlook has improved considerably, led by a sharp 17% y-o-y jump in coal volume offtake during April 2021 to January 2022 and expectation of an improvement in e-auction realisations on a likely rise in coal demand and elevated international coal prices. Thus, we expect a strong earnings revival for CIL with likely PAT growth of 40.4%/17.8%/10.5% y-o-y for FY2022E/FY2023E/FY2024E.

■ **Valuation – Maintain Buy on CIL with a revised PT of Rs. 190**

Improving earnings growth outlook (expect a 22% PAT CAGR over FY2021-FY2024E), high RoE of ~49%, and dividend yield of 12-13% make the stock's valuation attractive at 4.8x its FY2023E EPS (close to trough levels). Potential efficient capital allocation for non-core investments (aluminium smelting and solar energy projects) could act as key catalysts for the stock. We maintain our Buy recommendation on CIL with a revised price target (PT) of Rs. 190.

One-year forward P/E (x) band



Source: Sharekhan Research

About the company

CIL is engaged in the production and sale of coal. The company operates through ~82 mining areas across eight states and contributes to 82% of India's coal production. The company's products include coking coal (used in steel making and metallurgical industries), semi-coking coal (used in steel making, merchant coke manufacturing, and other metallurgical industries), non-coking coal (mainly used in power generation; also used for cement, fertilizer, glass, ceramic, paper, and chemical), and washed and beneficiated coal (manufacturing of hard coke for steel making, used in power generation, cement, and sponge iron).

Investment theme

The government's plans to increase coal production to substitute imports (stands at more than 200 million tonne) would help CIL to register sustainable volume growth over the next couple of years. Moreover, cost-control initiatives such as reduction of manpower (employee cost accounts for 53-54% of overall cost) would cushion margins. Moreover, valuations are at a steep discount to historical averages and the stock offers high dividend yield.

Key Risks

- Lower-than-expected volume offtake and realisation (especially e-auction) could impact margin and earnings outlook.
- The government's divestment plan could act as an overhang on the stock.

Additional Data

Key management personnel

Pramod Agrawal	Chairman and Managing Director
S. Sarkar	Director – Finance
Binay Dayal	Director – Technical

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp of India	11.0
2	HDFC Asset Manangement Co. Ltd	4.2
3	Nippon Life India Asset Management Ltd	2.4
4	Vanguard Group Inc./The	1.1
5	Bharat 22	1.1
6	BlackRock Inc.	0.9
7	ICICI Prudential Asset Management Co. Ltd/India	0.9
8	SBI Funds Management Pvt. Ltd	0.7
9	Aditya Birla Sun Life Asset Management Co. Ltd	0.4
10	Lazard Ltd.	0.3

Source: Bloomberg (Old data 15th Nov 2021)

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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