

Hindustan Zinc

Estimate change

TP change

Rating change

CMP: INR345
TP: INR370 (+7%)
Neutral

4QFY22 result inline, FY23 guidance disappoints

No surprises in its 4QFY22 result

- Revenue stood in line at INR88b (up 27% YoY and 10% QoQ) in 4QFY22, led by higher LME prices, but was partly offset by flat lead prices.
- EBITDA stood in line at INR50b (up 28% YoY and 14% QoQ). Power and fuel costs stood at INR8b, up 10% QoQ, led by higher coal prices. Other expenses rose 11% QoQ to INR19b, but was partly offset by inventory accumulation.
- PAT grew 18% YoY and 8% QoQ to INR29b, marginally below our estimate of INR30b due to lower than estimated other income and higher taxes, which includes taxes for the prior period also. Other income was lower as the benefit of falling interest rates in the previous quarters is behind us.
- Revenue/EBITDA/PAT stood at INR294b/INR162b/INR97b in FY22, up 30%/39%/22% YoY. The growth was driven entirely by 34%/22% YoY growth in LME zinc/lead prices as metal sales volumes remained flat YoY.
- Total metal sales volumes were a paltry 2% higher YoY (at 993kt) in FY22, despite 6% higher zinc sales at 793kt. The same was offset by 9% lower lead sales at 200kt. The management said FY21 had higher lead sales volumes due to higher concentrate availability, which has now normalized.

FY23 guidance disappoints

- The management has guided at a flat production growth in FY23, which hints at the possibility of it reaching peak mine output, unless large-scale expansion is achieved for sustainable mine production.
 - Mined metal production to be marginally higher at 1,050-1,075kt.
 - Silver production to touch 700-725t (v/s 647t in FY22).
 - The cost of production of zinc should be in the USD1,125-1,175/t range (v/s USD1,136/USD1,122/t in 4Q/FY22).
 - Project capex has been guided at USD125-150m, indicating no massive jump in projects either.
- We note that the management has guided at an elevated cost structure. We believe this is largely on account of their expectation of high coal and other input costs. HZ is primarily dependent on imported coal as coal linkages met only 3% of its total requirement in FY22. With thermal coal prices rising 2.35x in the last one year, the cost of production will only escalate further. Since the beginning of FY23, the imported price of 5500NAR Richards Bay thermal coal has risen 10% to INR22,000/t. A sharp jump in met coke prices will also impact the HZ's cost of production.
- Its silver production guidance also disappoints as the top end of the guidance (725kt) is 15% lower than our FY23E estimate.

Production growth continues to elude

- The management has guided at a refined production of 1,000-1,025kt in FY23. This has resulted in a 8% cut in our FY23 volume estimate.
- We believe the growth may have been delayed due to delay in the expansion of its mining operations as the company's mining output has hit a peak of 16mt.

Bloomberg	HZ IN
Equity Shares (m)	4,225
M.Cap.(INRb)/(USDb)	1457.3 / 19.1
52-Week Range (INR)	408 / 286
1, 6, 12 Rel. Per (%)	12/13/-5
12M Avg Val (INR M)	590

Financials & valuations (INR b)

Y/E March	2021	2022E	2023E
Sales	226	294	357
EBITDA	116.8	162.3	195.4
NP	79.8	97.6	123.2
Adj. EPS (INR)	18.9	23.1	29.2
EPS Gr(%)	17.3	22.3	26.2
BV/Sh. (INR)	76.5	81.1	80.3
RoE (%)	22.0	29.3	36.1
RoCE (%)	28.5	38.3	46.7
Payout (%)	200.1	77.9	102.9

Valuations

P/E (x)	18.3	14.9	11.8
P/BV	4.5	4.3	4.3
EV/EBITDA (x)	11.1	7.9	6.5
Div. Yield (%)	11.0	5.2	8.7

Shareholding pattern (%)

As On	Mar-22	Dec-21	Mar-21
Promoter	64.9	64.9	64.9
DII	32.5	32.5	32.2
FII	0.8	0.7	1.1
Others	1.8	1.9	1.8

FII Includes depository receipts

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Investors are advised to refer through important disclosures made at the last page of the Research Report.

 Motilal Oswal research is available on www.motilaloswal.com/Institutional-Equities, Bloomberg, Thomson Reuters, Factset and S&P Capital.

- Any further smelter/refining output growth will require Zawar mines to boost its output to 8mt from 4mt currently and Rajpura Dariba (RD) mines to raise its output as well. The management expects new mining concessions to be put up for auction by the government soon. However, this is a long term plan. Its short term plan is to increase mining output at Zawar and RD mines.
- The pyro smelter at HZ can operate at both 'lead' and 'zinc and lead' mode. In FY21, the availability of lead concentrate was higher and the smelter was run on 'only lead' mode. However, with improvement in the availability of zinc concentrate in FY22, the smelter was operated on 'zinc and lead' mode, leading to a YoY decline in lead production. The management is planning to debottleneck the smelter to increase tonnage.
- The Fumer project continues to be delayed due to non-availability of visa for Chinese specialists needed for its commissioning. The management said the visa issues have now largely been sorted out. It expects commissioning of the Fumer plant by end of 1QFY23 and a full ramp up by the beginning of 3QFY23. This is likely to provide 30kt of additional refined zinc in 2HFY23, provided the Fumer plant ramps up.

Valuation driven entirely by LME

- HZ operates in the first quartile of the cash cost curve among all smelters globally, implying that it is among the lowest cost producers of zinc. Despite this position, it is facing severe cost pressures, especially from rising coal costs, for which it has no alternate.
- In our recent meeting with the Chairman, it guided at a USD50/t reduction in the cost of production from FY22-24, indicating strong cost headwinds.
- We also note that during the meeting with the Chairman, the company had guided at refined metal production of 1,200kt in FY24, which we believe is likely to be deferred further, unless it achieves its mine production growth targets.
- We have cut our zinc and lead mined metal production for FY23 by 10% each and silver production by 12%. We have also cut our FY23 zinc/ lead/silver sales volume by 8%/10%/8%, factoring in the lower management guidance.
- However, we have raised our FY23 zinc/lead LME price assumption by 37%/3%, given the tight zinc market, which is driving LME prices higher. LME zinc prices are only 3% lower than its all-time high of USD4,619.5/t. With higher energy prices in Europe and low physical stocks in the US, prices are likely to remain elevated for some time before normalizing.
- We raise our FY23 EBITDA/EPS estimate by 14%/3% and by 18%/4% for FY24 given the increase in LME prices. The same is partly offset by a decline in FY23 volumes as a result of the disappointing guidance.
- The stock is trading at 6.5x our FY23 EV/EBITDA estimates. The probability of zinc prices correcting from current levels is higher than an up move as the energy and inventory situation normalizes globally. Despite a 37% rise in zinc prices and raising our TP to INR370 per share (from INR325 earlier), we maintain our Neutral rating, an upside of 8% from current levels.
- Delay in volume growth remains a key concern along with rising costs. Slowdown in China is the key risk to zinc prices.

Quarterly performance (INR b)

Y/E March	FY21				FY22				FY21	FY22	FY22E	Variance (%)
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q				
Net sales	39.9	56.6	60.3	69.5	65.3	61.2	79.9	88.0	226.3	294.4	85.9	2.4
Change (YoY %)	-20.0	25.5	29.1	58.3	63.7	8.2	32.4	26.6	21.9	30.1		
Change (QoQ %)	-9.2	41.9	6.6	15.2	-6.0	-6.3	30.5	10.1				
EBITDA	15.8	29.5	32.7	38.8	35.6	33.4	43.7	49.6	116.8	162.3	48.1	3.2
Change (YoY %)	-36.4	39.4	42.8	97.5	125.8	13.0	33.7	28.0	32.0	39.0		
Change (QoQ %)	-19.8	87.3	10.7	18.6	-8.3	-6.3	31.0	13.5				
As a percentage of net sales	39.5	52.2	54.2	55.8	54.5	54.5	54.7	56.4	51.6	55.1	56.0	
Finance cost	0.5	0.7	1.4	1.3	0.9	0.8	0.5	0.7	3.9	2.9	0.9	
DD&A	5.4	6.5	6.4	7.0	6.6	7.0	7.4	8.2	25.3	29.2	7.5	9.0
Other income	6.8	3.9	4.5	3.0	3.5	3.1	2.8	2.8	18.2	12.2	2.8	-1.8
PBT (before EO item)	16.6	26.2	29.5	33.5	31.6	28.6	38.6	43.6	105.8	142.3	42.5	2.5
EO exp./(income)	0.0	0.0	0.0	0.0	1.3	0.0	0.0	0.0	0.0	1.3	0.0	
PBT	16.6	26.2	29.5	33.5	30.2	28.6	38.6	43.6	105.8	141.0	42.5	2.5
Total Tax	3.1	6.8	7.5	8.6	10.4	8.5	11.6	14.3	25.9	44.7	12.8	12.0
Tax (%)	18.3	26.0	25.3	25.8	34.4	29.5	30.0	32.8	24.5	31.7	30.0	
Reported PAT	13.6	19.4	22.0	24.8	19.8	20.2	27.0	29.3	79.8	96.3	29.8	-1.6
Adjusted PAT	13.6	19.4	22.0	24.8	21.2	20.2	27.0	29.3	79.8	97.6	29.8	-1.6
Change (YoY %)	-23.0	-6.8	35.8	85.5	55.8	4.0	22.8	17.9	17.3	22.3		
Change (QoQ %)	1.5	42.8	13.4	12.9	-14.8	-4.7	33.9	8.4				

Source: Company, MOFSL

Operational performance

Y/E March	FY21				FY22				FY21	FY22	FY22E	Variance (%)
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q				
Mine production (kt)	202	238	244	288	221	249	252	295	972	1,017	295	0.0
Sales												
Zinc refined (kt)	163	181	182	198	187	164	212	214	724	777	211	1.4
Lead refined (kt)	45	57	53	62	49	47	47	49	217	192	49	0.0
Silver (tonne)	146	203	183	203	160	152	173	162	735	647	162	0.0
LME/realizations												
Zinc LME (USD/t)	1,961	2,338	2,628	2,749	2,913	2,991	3,364	3,754	2,419	3,256	3,726	0.8
Premium (USD/t)	110	126	227	189	196	240	205	226	177	251	230	-1.6
Zinc realization (USD/t)	2,071	2,464	2,855	2,938	3,109	3,231	3,569	3,980	2,596	3,507	3,956	0.6
Lead LME (USD/t)	1,673	1,875	1,903	2,017	2,123	2,341	2,331	2,335	1,867	2,283	2,331	0.2
Premium (USD/t)	95	153	186	193	161	200	226	213	169	199	200	6.3
Lead realization (USD/t)	1,768	2,028	2,089	2,210	2,284	2,541	2,557	2,548	2,036	2,482	2,531	0.7
Silver LME (INR/t)	45,823	61,000	62,410	67,026	69,700	64,950	62,755	63,667	59,065	65,268	63,667	0.0
Premium (INR/t)	-1,782	-64	213	-425	-575	-279	-269	283	0	0	0	na
Silver realization (INR/t)	44,041	60,936	62,623	66,601	69,125	64,671	62,486	63,951	59,065	65,268	63,667	0.4



Highlights from the management commentary

Acquisition of Zinc International business of Parent

- The management highlighted that they have completed their study of the assets/business of Zinc International and feels it can do a better job of managing that facility by sharing its best practices.
- We believe the best practices would have anyways been shared regularly over the years between the two entities as both companies share the same parent.
- However, the management said there are no at proposals presently for the acquisition.

Coal cost and overall costs

- HZ sources its coal requirements from the international market, majorly from South Africa, Mozambique, and Australia.
- Though it has coal linkages with COAL, the same accounts for ~3% of total coal consumed by the company.
- Coal currently constitutes ~35% of its total cost of production.
- South African coal prices have risen 2.35x in the last one year. The rally continues unabated, which is pushing the cost of production higher for HZ.

Hedging zinc sales

- The management has started the practice of hedging part of its sales volume from FY23.
- It has hedged 15% of its FY23 sales volumes over USD4,000/t.
- Management highlighted that there is a heightened uncertainty in the global markets currently and hence it is prudent to keep booking part of the sales volumes on forward basis.

Expansion

- HZ has not made much headway in its custom smelter project in Gujarat. It has been unable to convene the Gram Sabha meeting needed to move ahead with the project.
- Once the same is complete, it will focus on other parts of the project that include land acquisition, placing orders for equipment, and applying for CTE (consent to establish).

Expansion at its existing plants

- HZ has set a target of 1mt of smelter production and ~15kt from the Fumer plant.
- Its plan to expand capacity to 1.2mt and later to 1.5mt needs investments in mining before such a project can materialize.
- The management is taking steps to expand its mining operations to match the refining capacity of 1.2mt.

Divestment of the government's stake

- The management highlighted that the SC has already cleared the deck for disinvestment of HZ.
- The government is working on the modalities for the stake sale.

Ore production and grade

- Ore production stood near its peak at 16.34mt, while the average zinc grade was 7.08%.
- The ore grade was lower on a YoY basis as underground production peaked in FY22.
- The management expects better ore grade in FY23.

Lower lead production volumes

- The lower lead production volume in FY22 was attributable to running a pyro smelter in zinc and lead mode in FY22, owing to higher production of zinc concentrate as compared to only lead in FY21.
- This led to a YoY drop in lead output.
- The management expects to de-bottleneck the furnace to increase capacity and boost the volume of lead concentrate.

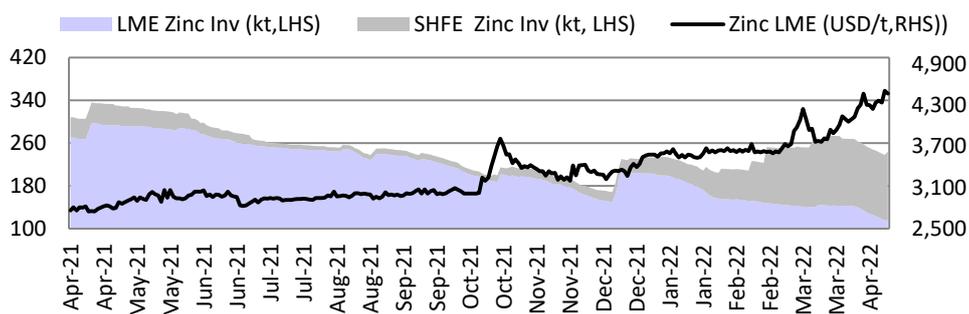
Export mix and share in the domestic market

- HZ sold 60-62% of its total volume in the domestic market. It commands ~83% of the total zinc market in India.
- The balance is supplied by imports.

Debt and cash

- Current gross cash on its books is INR179b. The gross debt comprises NCDs of INR28b (INR7b will be repaid in Sep’21, and the balance will be repaid in Sep’24).
- There is no plan to prepay any NCDs.
- HZ had applied to the Ministry of Corporate Affairs in 3QFY22 for conversion of INR100b of its general reserves into retained earnings.
- This offers the company flexibility to pay out a higher dividend.
- Net cash in its books stood at INR179.66b as of 31st Mar’22.

Exhibit 1: LME Zinc prices have risen 24% CYTD



Source: Bloomberg, MOFSL

Exhibit 2: Silver price is up 11% on CYTD basis

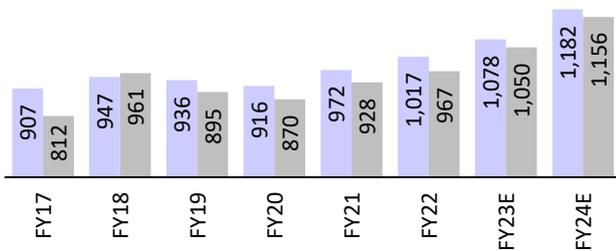


Source: Bloomberg, MOFSL

Story in charts

Exhibit 1: Expect 9.3% CAGR in refined metal production over FY22-24, albeit on a low base

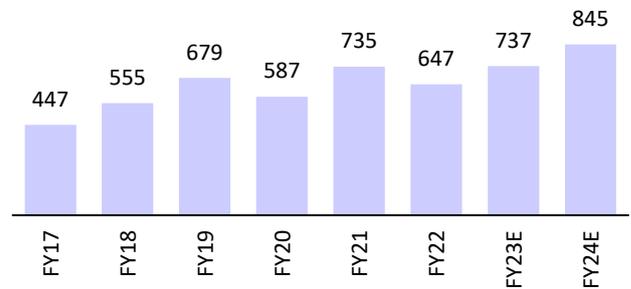
Mine production - kt Refined metal production - kt



Source: Company, MOFSL

Exhibit 2: Expect aggressive silver volumes at 14.3% CAGR over FY22-24

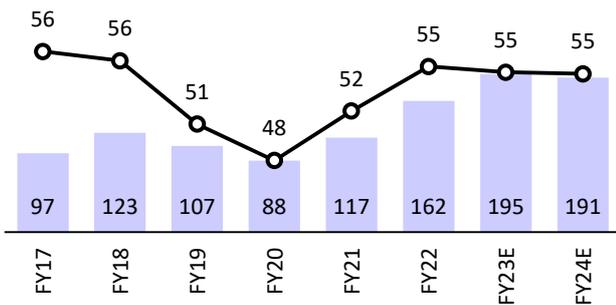
Silver sales - t



Source: Company, MOFSL

Exhibit 3: Silver sales to aid modest EBITDA growth

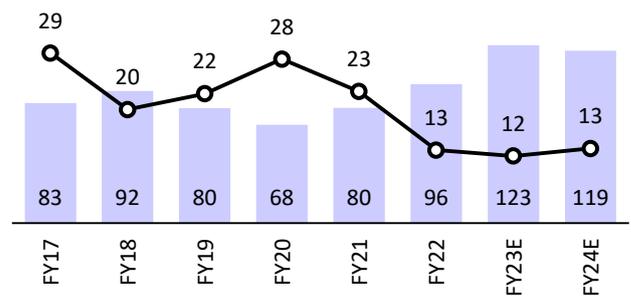
EBITDA (INR b) EBITDA margin (%)



Source: Company, MOFSL

Exhibit 4: Lower yields and higher payouts likely to impact contribution of other income to PAT

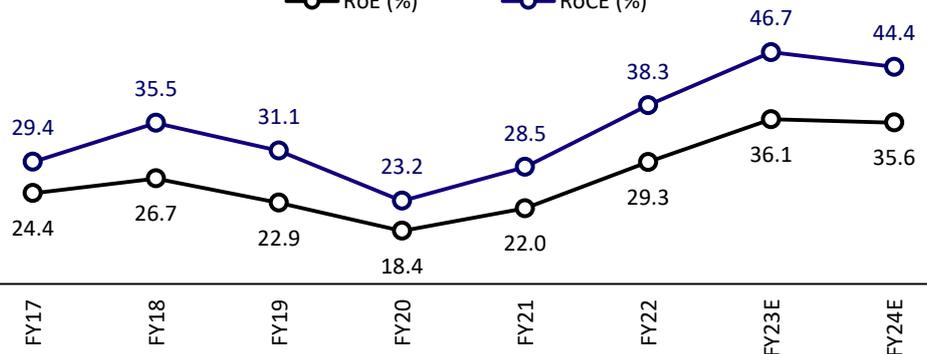
PAT (INR b) Other income as % of PAT



Source: Company, MOFSL

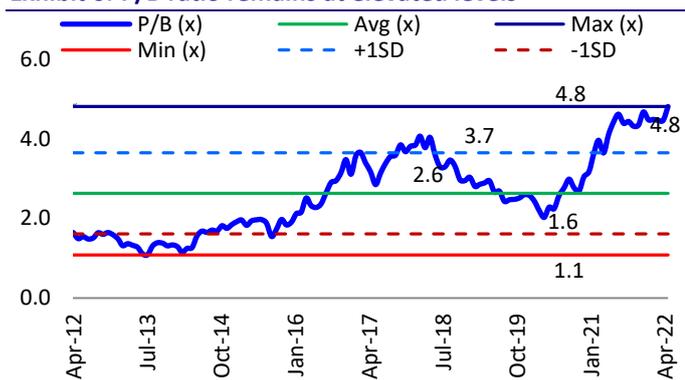
Exhibit 5: Strong return ratios justify premium valuation, but the same is priced in

RoE (%) RoCE (%)



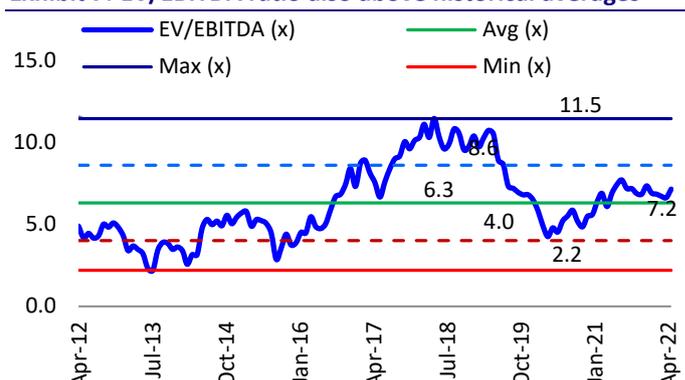
Source: MOFSL, Company

Exhibit 6: P/B ratio remains at elevated levels



Source: MOFSL, Company

Exhibit 7: EV/EBITDA ratio also above historical averages



Source: MOFSL, Company

Exhibit 8: Changes in our assumptions and key financials

		FY23E			FY24E		
		Old	New	Change	Old	New	Change
Price assumptions (LME)							
Zinc	USD/t	2,900	3,975	37%	2,750	3,350	22%
Lead	"	2,200	2,263	3%	2,100	2,025	-4%
Silver	INR/kg	59,668	59,687	0%	60,897	60,860	0%
Sales volume assumptions							
Refined Zinc	kt	887	820	-8%	878	892	2%
Refined Lead	kt	256	230	-10%	268	264	-2%
Silver	mt	805	737	-8%	846	845	0%
Financial estimates							
Revenue	INR b	315	357	14%	310	351	13%
EBITDA	"	172	195	14%	185	191	3%
Adj. PAT	"	104	123	18%	115	119	4%
EPS	INR/share	25	29	18%	27	28	4%

Source: MOFSL, Company

Exhibit 9: Global comparable valuation

Company	M-cap (USD m)	P/E (x)			EV/EBITDA (x)			P/B (x)			RoE (%)		
		CY20/ FY21	CY21/ FY22	CY22/ FY23									
Hind. Zinc*	19,069	14.9	11.8	12.2	7.9	6.5	6.6	4.3	4.3	4.4	29.3	36.1	35.6
Korea Zinc	9,397	13.3	13.6	13.3	6.9	6.7	6.4	1.4	1.3	1.2	11.0	10.1	9.7
Teck	19,993	4.8	6.9	8.8	2.8	3.0	3.3	0.9	0.8	0.8	21.6	12.8	7.3

Source: MOFSL, Company, Bloomberg. (*) denotes MOFSL estimates

Exhibit 10: Valuation continues to remain elevated

	UoM	FY23E
EBITDA	INR b	195.4
EV/EBITDA multiple	x	7.0
Enterprise value	INR b	1368
Add: Net cash	INR b	196
Equity value	INR b	1564
Share count	b	4.23
TP (INR/share)	INR/share	370

Source: MOFSL, Company

Financials and valuations

Income Statement							INR b	
Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Net Sales	173	221	211	186	226	294	357	351
Total Expenses	76	98	104	97	110	132	162	159
EBITDA	97	123	107	88	117	162	195	191
Depreciation	18	17	19	23	25	29	30	33
EBIT	80	106	88	66	91	133	166	158
Finance cost	2	3	1	1	4	3	4	3
Other income	24	18	18	19	18	12	14	15
PBT	102	121	105	84	106	142	176	171
Tax	19	32	25	16	26	45	53	51
Rate (%)	18.5	26.3	23.9	18.9	24.5	31.4	30.0	30.0
PAT	83	89	80	68	80	98	123	119
EO expense (Income)	0	-2	0	0	0	1	0	0
PAT (after EO)	83	92	80	68	80	96	123	119
Change (YoY %)	-0.7	7.2	-10.8	-14.5	17.3	22.3	26.2	-3.1

Consolidated Balance Sheet							INR b	
Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Share Capital	8	8	8	8	8	8	8	8
Reserves	300	351	328	395	315	334	331	323
Net Worth	308	359	336	403	323	343	339	332
Total Loans	79	0	25	6	65	28	21	14
Deferred Tax Liability	-27	-22	-19	-18	-11	9	29	48
Capital Employed	360	337	342	391	377	381	389	394
Gross Block	165	195	249	288	317	352	382	421
Less: Accum. Deprn.	65	82	101	124	149	178	208	241
Net Fixed Assets	100	113	148	165	168	174	174	180
Capital WIP	31	32	23	25	19	21	21	21
WC. Assets	360	262	235	262	259	252	264	263
Inventory	19	14	15	18	14	20	24	24
Account Receivables	1	2	2	4	4	7	6	6
Cash and Bank Balance	322	222	195	222	223	208	217	216
Loans and advances	17	25	23	17	18	17	17	17
WC. Liability and Prov.	131	70	63	61	69	66	70	70
Trade payables	12	9	12	15	15	20	24	24
Provisions and Others	119	61	51	46	54	46	46	46
Net WC. Assets	229	192	172	201	190	186	194	193
Appl. of Funds	360	337	342	391	377	381	389	394

Financials and valuations

Ratios

Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Basic (INR)								
EPS	19.7	21.1	18.8	16.1	18.9	23.1	29.2	28.3
Cash EPS	23.9	25.1	23.3	21.5	24.9	30.0	36.2	36.0
BV/Share	72.9	85.0	79.5	95.4	76.5	81.1	80.3	78.6
DPS	29.4	8.0	20.0	0.0	37.8	18.0	30.0	30.0
Payout (%)	179.3	45.5	127.5	0.0	200.1	77.9	102.9	106.2
Valuation (x)								
P/E	17.5	16.3	18.3	21.4	18.3	14.9	11.8	12.2
Cash P/E	14.4	13.7	14.8	16.0	13.9	11.5	9.5	9.6
P/BV (incl.-goodwill)	4.7	4.1	4.3	3.6	4.5	4.3	4.3	4.4
EV/Sales	0.0	5.6	6.1	6.7	5.7	4.3	3.5	3.6
EV/EBITDA	0.0	10.1	12.1	14.0	11.1	7.9	6.5	6.6
Dividend Yield (%)	8.5	2.3	5.8	0.0	11.0	5.2	8.7	8.7
Return Ratios (%)								
EBITDA Margin	56.3	55.6	50.5	47.7	51.6	55.1	54.7	54.5
Net Profit Margin	48.1	40.4	37.7	36.7	35.3	33.2	34.5	34.1
RoE	24.4	26.7	22.9	18.4	22.0	29.3	36.1	35.6
RoCE (pre-tax)	29.4	35.5	31.1	23.2	28.5	38.3	46.7	44.4
RoIC (pre-tax)	465.8	137.9	67.0	41.6	56.7	81.5	96.0	90.4
Working Capital Ratios								
Fixed Asset Turnover (x)	1.7	2.1	1.6	1.2	1.4	1.7	2.1	2.0
Receivable (Days)	3	3	3	8	7	9	6	6
Inventory (Days)	41	23	27	36	23	24	25	25
Trade payable (Days)	25	16	20	29	25	25	25	25
Leverage Ratio (x)								
Current Ratio	2.8	3.7	3.7	4.3	3.7	3.8	3.8	3.8
Interest Coverage	51.6	43.7	90.4	75.9	28.4	50.1	45.6	52.6
Net Debt/EBITDA	-2.5	-1.8	-1.6	-2.4	-1.4	-1.1	-1.0	-1.1
Net Debt/Equity	-0.8	-0.6	-0.5	-0.5	-0.5	-0.5	-0.6	-0.6

Cash Flow Statement

	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
EBITDA	97	123	107	88	117	162	195	191
Non-cash exp./ (income)	0	0	0	0	0	1	0	0
(Inc.)/Dec. in Wkg. Cap.	-35	5	7	-11	6	-12	0	0
Tax paid	-19	-30	-26	-11	-18	-24	-33	-32
CF from Op. Activity	43	98	88	66	106	127	162	159
(Inc.)/Dec. in FA + CWIP	-10	-27	-34	-36	-24	-30	-30	-38
Free Cash Flow	34	71	54	30	81	97	132	120
Interest & Dividend Income	24	5	3	5	15	9	14	15
Others	0	0	1	5	1	1	0	0
CF from Inv. Activity	15	-22	-31	-26	-8	-20	-16	-23
Debt raised/(repaid)	79	-79	25	-19	65	-43	-7	-7
Dividend (incl. tax)	-168	-105	-120	0	-160	-76	-127	-127
Interest paid	0	-2	-2	-2	-2	-3	-4	-3
Others	0	11	13	9	0	0	0	0
CF from Fin. Activity	-89	-176	-84	-12	-97	-123	-138	-137
(Inc.)/Dec. in Cash	-31	-100	-27	27	1	-15	9	-1
Add: Opening Balance	353	322	222	195	222	223	208	217
Closing Balance	322	222	195	222	223	208	217	216

E: MOFSL estimates

NOTES

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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