Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

Coal India Ltd

Q3 misses mark; attractive valuation & high dividend yield

Energy & Utilities		Sharekhan code: COALINDIA		
Reco/View: Buy	↔	CMP: **Rs. 220**	Price Target: **Rs. 280**	↔

↑ 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 42.55

Updated Dec 08, 2022

Severe Risk

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

Source: Morningstar

Company details

Market cap:	Rs. 1,35,765 cr
52-week high/low:	Rs. 263 / 149
NSE volume: (No of shares)	90.2 lakh
BSE code:	533278
NSE code:	COALINDIA
Free float: (No of shares)	208.7 cr

Shareholding (%)

Promoters	66.1
FII	7.9
DII	21.2
Others	4.8

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	-2.0	-10.1	2.4	34.4
Relative to Sensex	0.4	-8.2	-0.3	34.2

Sharekhan Research, Bloomberg

Summary

- Consolidated Q3FY23 operating profit of Rs. 10,389 crore (up 52% y-o-y) lagged our estimate as margins were hit by higher contractual expenses (up 21%/42% y-o-y/q-o-q) and lower blended realisations. PAT of Rs. 7,756 crore (up 70% y-o-y) was 3.6% below estimates led by miss in margin, higher depreciation and tax rate partially offset by higher other income.
- FSA/E-auction realisation of Rs. 1,482/Rs. 5,047 per tonne, missed our estimate by 4%/5%. E-Auction premium came at 241% versus 329% in Q2FY23. Coal offtake volume at 176 million tonnes (up 1.2% y-o-y; up 13.8% q-o-q) was in-line provisional numbers declared by company. FSA volumes rose by 9% y-o-y to 158 mt but the same was offset by a steep 44% y-o-y decline in e-Auction volumes to 15 mt.
- We thus expect a strong 20% PAT CAGR over FY22-25E. A likely FSA realisation hike could improve earnings growth outlook. Potential stake sale in Bharat Coking Coal Limited (BCCL) and a subsequent listing would unlock value.
- The stock trades at an attractive valuation of 5x/4.5x its FY24E/FY25E EPS (close to trough valuation) and offers a high dividend yield of 12%. Hence, we maintain a Buy with an unchanged PT of Rs. 280.

Q3FY23 consolidated operating profit of Rs. 10,389 crore (up 52% y-o-y; up 43% q-o-q) was 4% below our estimate of Rs. 10,819 crore due to 4% miss in blended EBITDA margin at Rs. 591/tonne (up 50.5% y-o-y; 25.4% q-o-q). Lower-than-expected EBITDA margins were owing to a 2% miss in blended realisations at Rs. 1,845/tonne, while contractual expenses were 27% higher-than-expected (rising 42% q-o-q). Coal offtake volumes of 176 million tonnes (up 14% q-o-q) was in line with provisional volume numbers and were driven by an 11%/41% q-o-q increase in FSA/e-Auction volumes to 158/15 million tonnes. FSA/E-auction realisation of Rs. 1,482/Rs. 5,047 per tonne, up 4.8%/down 16.8% q-o-q missed our estimate by 4%/5%. Consolidated PAT of Rs. 7,756 crore (up 70% y-o-y; up 28% q-o-q) was 3.6% below the estimate of Rs. 8,046 crore due to miss in margin, higher depreciation and tax rate partially offset by higher other income.

Key positives

- Company declared a second interim dividend of Rs. 5.25/share taking the total dividend to Rs. 20.25/ share in FY23 till date, which implies a dividend yield of 9% on CMP.

Key negatives

- Lower-than-expected FSA/E-auction realisation of Rs. 1,482/Rs. 5,047 per tonne (miss of 4%/5%)
- Contractual expenses were 27% higher-than-expected (up 21%/42% y-o-y/q-o-q).

Revision in estimates – We have fine-tuned our FY23-25 earnings estimate to reflect 9MFY23 performance.

Our Call

Valuation – Maintain Buy on CIL with an unchanged PT of Rs. 280: Strong earnings growth outlook (expect a 20% PAT CAGR over FY2022-FY2025E), high RoE of ~51%, and dividend yield of 12% make CIL's valuation attractive at 5x/4.5x its FY2024E/FY2025E EPS (close to troughs). The board has given an in-principle approval to divest a 25% stake in Bharat Coking Coal Limited (BCCL) and awaits the government's nod. A stake sale and a potential listing could help unlock value. We maintain a Buy recommendation on CIL with an unchanged price target (PT) of Rs. 280.

Key Risks

Lower-than-expected volume offtake amid any weakness in electricity demand 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	FY22	FY23E	FY24E	FY25E
Revenue	1,09,714	1,36,122	1,32,474	1,42,949
OPM (%)	22.5	28.3	26.1	27.0
Adjusted PAT	17,358	29,921	27,253	30,227
% YoY growth	36.7	72.4	-8.9	10.9
Adjusted EPS (Rs.)	28.2	48.6	44.2	49.0
P/E (x)	7.8	4.5	5.0	4.5
P/B (x)	3.1	2.7	2.4	2.2
EV/EBITDA (x)	4.5	2.2	2.5	2.0
RoNW (%)	43.6	64.4	51.7	51.2
RoCE (%)	45.1	67.3	55.6	56.2

Source: Company; Sharekhan estimates

PAT missed estimate on lower blended realisation and higher cost

Q3FY23 consolidated operating profit of Rs. 10,389 crore (up 52% y-o-y; up 43% q-o-q) was 4% below our estimate of Rs. 10,819 crore due to 4% miss in blended EBITDA margin at Rs. 591/tonne (up 50.5% y-o-y; 25.4% q-o-q). A lower-than-expected EBITDA margins was led by 2% miss in blended realisation at Rs. 1,845/tonne and 27% higher-than-expected contractual expenses (up 42% q-o-q). Coal offtake volume of 176 million tonnes (up 14% q-o-q) was in-line with provisional volume numbers and was driven by 11%/41% q-o-q increase in FSA/E-Auction volumes to 158/15 million tonnes. FSA/E-auction realisation of Rs. 1,482/Rs. 5,047 per tonne, up 4.8%/down 16.8% q-o-q missed our estimate by 4%/5%. Consolidated PAT at Rs. 7,756 crore (up 70% y-o-y; up 28% q-o-q) was 3.6% below estimate of Rs 8,046 crore due to miss in margin, higher depreciation and tax rate partially offset by higher other income.

Results (Consolidated) Rs cr

Particulars	Q3FY23	Q2FY23	Y-o-Y %	Q2FY23	Q-o-Q %
Revenue	**35,169**	**28,433**	**23.7**	**29,838**	**17.9**
Total Expenditure	24781	21,608	14.7	22,558	9.9
Reported operating profit	**10,389**	**6,825**	**52.2**	**7,280**	**42.7**
Other Income	1585	653	142.8	1761	-10.0
Interest	204	132	54.9	135	50.8
Depreciation	1,262	1,041	21.2	1,077	17.2
Reported PBT	10,508	6,305	66.6	7,829	34.2
Tax	2,875	1,746	64.7	1,643	74.9
PAT before share of profit from JVs and MI	7,633	4,560	67.4	6,186	23.4
Share of profit from JVs	86	-3		-142	-160.6
Minority interest	-36	-2		0	-8,381.8
Reported PAT	**7,756**	**4,558**	**70.1**	**6,044**	**28.3**
O/S Shares (cr)	616	616		616	
Reported EPS (Rs)	12.6	7.4	70.1	9.8	28.3
Margins (%)			**BPS**		**BPS**
OPM	29.5	24.0	553.4	24.4	514.0
NPM	22.1	16.0	602.0	20.3	179.8
Tax rate	27.4	27.7	-32.9	21.0	636.4

Source: Company; Sharekhan Research

Key operating performance

Particulars	Q3FY23	Q2FY23	Y-o-Y %	Q2FY23	Q-o-Q %
Coal production (mt)	180	164	9.9	139	29.3
Coal offtake (mt)	176	174	1.2	155	13.8
Blended realisation (Rs/tonne)	1,845	1,496	23.3	1,782	3.5
FSA realisation (Rs/tonne)	1,482	1,370	8.2	1,414	4.8
E-auction realisation (Rs/tonne)	5,047	1,947	159.2	6,064	-16.8

Source: Company; Sharekhan Research

Outlook and Valuation

■ **Sector View – Domestic coal demand to reach 1,250-1,500 mt with increased power generation**

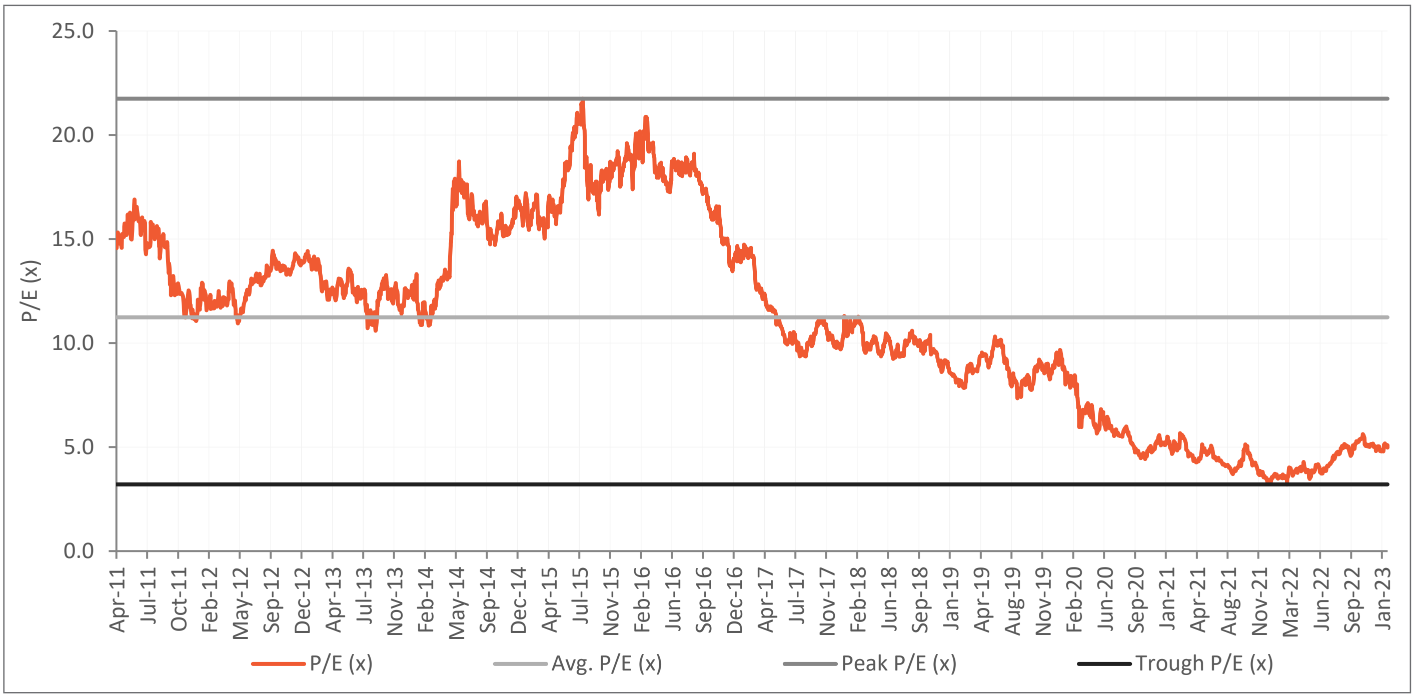
-Coal comprises 55% of India's total commercial energy production. Although its share in India's overall energy mix is expected to fall over the next decade, it would remain a primary energy source and absolute coal offtake is expected to improve given higher demand from sectors such as power and steel. Industry estimates suggest that India's coal demand could reach 1,250-1,500 million tonnes by FY2030, assuming a 6-8% growth in power demand and despite a sharp surge 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 as coal shortage bodes well for volume growth, while improving e-auction realisation as high international coal prices (although have corrected recently) would improve the company's earnings profile. Thus, we expect a strong 20% PAT CAGR over FY2022-FY2025E.

■ **Valuation – Maintain Buy on CIL with an unchanged PT of Rs. 280:** Strong earnings growth outlook (expect a 20% PAT CAGR over FY2022-FY2025E), high RoE of ~51%, and dividend yield of 12% make CIL's valuation attractive at 5x/4.5x its FY2024E/FY2025E EPS (close to troughs). The board has given an in-principle approval to divest a 25% stake in Bharat Coking Coal Limited (BCCL) and awaits the government's nod. A stake sale and a potential listing could help unlock value. We maintain a Buy recommendation on CIL with an unchanged price target (PT) of Rs. 280.

One-year forward P/E (x) band



Source: Sharekhan Research

About 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, fertiliser, glass, ceramic, paper, and chemical), and washed and beneficiated coal (manufacturing of hard coke for steel making, 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	11.00
2	Nippon Life India Asset Management	2.79
3	HDFC Asset Management Co Ltd	2.65
4	PPFAS Asset Management	1.03
5	Vanguard Group Inc/The	1.02
6	BlackRock Inc	0.87
7	SBI Funds Management Ltd	0.70
8	ICICI Prudential Asset Management	0.55
9	UTI Asset Management Co Ltd	0.28
10	ICICI Prudential Life Insurance Co	0.19

Source: Bloomberg

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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