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Company update and
earnings change

Metals

Target price Rs199

Earnings revision

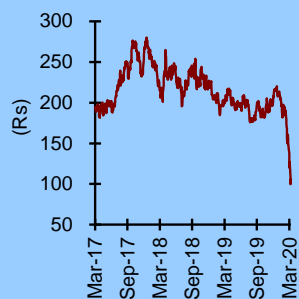
(%)	FY21E	FY22E
Revenue	↓ 22.3	0.0
EBITDA	↓ 36.6	↓ 4.1
EPS	↓ 74.7	↓ 4.0

Shareholding pattern

	Jun '19	Sep '19	Dec '19
	34.7	34.7	34.7
Institutional investors	46.4	46.5	45.9
MFs and others	13.9	13.7	13.6
FIs and Banks	0.3	0.3	0.3
Insurance Cos.	10.1	11.3	11.3
FII	22.1	21.2	20.7
Others	18.9	18.8	19.4

Source: NSE

Price chart



Hindalco Industries

BUY

Maintained

Rs90

Adjusting to new reality – a quarter of shutdown

With the second wave of Covid19 re-emerging in China and India fast moving into a lockdown, a steep cut in earnings of metals pack for FY21E looks likely. We have assumed a quarter of disruption in domestic and Novelis operations for Hindalco. This leads to FY21E EBITDA/PAT reduction of 37% and 75%, respectively. This takes consolidated EBITDA back to CY15 levels (last downturn). We have reduced FY21E Indian Aluminium (integrated) EBITDA by 37% and Novelis EBITDA by 41%. Domestic operations can witness a quarter of negative EBITDA – whenever disruption hits production. Cash position with Hindalco remains comfortable. While we acknowledge the extent of earnings correction possibility, we see deep value in the name purely on the back of our asset-based valuation heuristic (P/B). We maintain BUY with a target price of Rs199/share (equivalent to 0.67x 1-year fwd P/B).

- **US auto industry has started witnessing disruptions.** Temporary shutdown of US plants by US car manufacturers, can meaningfully impact the auto-sheet market. Aluminium auto sheet market has reached 1.2-1.3mnte in the US, with Novelis supplying ~35% of the same. US auto sheet supply forms a significant chunk of Novelis' overall auto shipment supplies (650kte) in FY19 and contributed a revenue of US\$3bn. Sales to Ford itself was US\$1.23bn or 10% of the total Novelis revenue. We estimate these auto volumes (out of US) contribute 22-23% of total Novelis EBITDA (given the high margins) and 13% of consolidated Hindalco EBITDA. We have uniformly pared down volumes and EBITDA estimates across regions for Novelis operations. This results in 41% decline in Novelis EBITDA estimates (this also builds in a drop on account of metal price lag impact).
- **FY21E India earnings reduced to factor in a quarter of plant shutdowns across locations.** We have factored in ~23% drop in aluminium volumes leading to ~37% drop in integrated aluminium EBITDA for FY21E. This is despite the possible drop in fuel oil, pitch, CP coke, and caustic soda prices. We have also increased receivable days for Hindalco (standalone) – an issue seen for businesses across the spectrum. We are yet to reduce the Indian capex (guided at Rs20bn p.a) but as situation deteriorates there is a possibility for the same.
- **Hindalco is enjoying comfortable cash position.** India operations have ~Rs70bn while US\$1bn is currently available with Novelis. Extra fund raised on account of Aleris acquisition (US\$400mn) has helped Novelis liquidity. There is no major immediate refinancing due for Novelis in Q1/Q2FY21. Hence, closure of business activity for a quarter doesn't reveal any particular vulnerability for Hindalco.

Maintain BUY. Our P/B metric is suggesting deep value for Hindalco as it breaches CY08/CY15 lows with an improved balance sheet and hence, a reduced probability of loss. We maintain BUY with a target price of Rs199/share as we shift our valuation methodology to 0.67x 1-year fwd book – in-line with RoE (through cycle) of 7-8% that we see in the name.

Market Cap	Rs202bn/US\$2.6bn	Year to March	FY19	FY20	FY21E	FY22E
Reuters/Bloomberg	HALC.BO/HNDL IN	Revenue (Rs mn)	1,365,902	1,251,408	1,009,492	1,355,668
Shares Outstanding (mn)	2,246	Net Income (Rs mn)	54,952	48,445	9,999	47,050
52-week Range (Rs)	254/90	EPS (Rs)	24.7	21.8	4.5	21.2
Free Float (%)	65.3	% Chg YoY	27.5	(11.8)	(79.4)	370.6
FII (%)	26.2	P/E (x)	3.6	4.1	20.0	4.3
Daily Volume (US\$/'000)	22,309	CEPS (Rs)	46.1	42.8	27.0	44.2
Absolute Return 3m (%)	(51.0)	EV/E (x)	4.3	4.5	9.0	5.3
Absolute Return 12m (%)	(49.1)	Dividend Yield (%)	1.3	1.6	1.6	1.6
Sensex Return 3m (%)	(28.3)	RoCE (%)	10.3	8.6	3.4	7.9
Sensex Return 12m (%)	(22.1)	RoE (%)	9.8	8.4	1.7	7.6

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Earnings reduced to factor in a quarter of business disruption in India and abroad

We haven't readjusted our commodity or currency assumptions yet. Nevertheless, depreciating INR provides an offset to declining LME **(with a 6.5% currency depreciation largely offsetting 4-5% of LME price drop)**.

What we have factored in now is a quarter of disruption in business activity in India and abroad. We have started witnessing the same in the US auto facilities which can directly impact the auto sheet procurement for Novelis. Similar auto makers have started announcing shutdowns across European facilities.

Similarly, India is descending into a major lockdown, which can invariably impact the operations of Hindalco's plants/facilities. Our changes in assumptions (Table 1) reflect the same.

Even when operations are curtailed for a quarter, we don't expect Hindalco to report losses, given the significantly lower leverage in the current cycle compared to the past.

Table 1: Key assumptions change

(Rs mn)	FY21E			FY22E		
	New	Old	% Chg	New	Old	% Chg
Integrated Aluminium EBITDA (India)	24,140	38,491	(37.3)	47,514	48,398	(1.8)
Indian Aluminium Volumes	1,017	1,311	(22.5)	1,311	1,311	0.0
Integrated Aluminium EBITDA (US\$/te)	339	419	(19.1)	518	527	(1.8)
Copper EBITDA (Rs mn)	3,658	7,557	(51.6)	11,950	11,950	0.0
Novelis EBITDA (US\$ mn)	732	1,245	(41.2)	1,170	1,225	(4.5)
Volumes (kte)	3,036	3,514	(13.6)	3,514	3,514	0.0
Novelis EBITDA/te	241	354	(31.9)	333	349	(4.5)
Aluminium (US\$/te)	1800	1800		1950	1950	
US\$/INR	70	70		70	70	

Source: Company data, I-Sec research

Table 2: Earnings change

(Rs mn)	FY21E			FY22E		
	New	Old	% Chg	New	Old	% Chg
Sales	1,009,492	1,298,631	(22.3)	1,355,668	1,355,533	0.0
EBITDA	85,312	134,583	(36.6)	141,427	147,456	(4.1)
PAT	9,999	39,536	(74.7)	46,164	48,095	(4.0)

Source: Company data, I-Sec research

Valuation methodology and key risks

Our P/B metric is suggesting deep value for Hindalco as it breaches CY08/CY15 lows with a much improved balance sheet and hence a reduced probability of loss. **We maintain BUY with a target of Rs 199/share as we shift our valuation methodology to 0.67 1 year fwd. book – in-line with RoE (through cycle) of 7-8% that we see in the name.** We would also like to reiterate the futility of earning analysis as a predictive tool in this sector.

We have factored in a meaningful buildup in receivables over FY20E end and H1FY21E. Yet the same appears manageable, given the current balance sheet of Hindalco.

The risks to earnings are commodity (Aluminium) and currency price fluctuations. Also, we don't ascribe much concern to the declining energy pack price as past 60 years of history highlights the complete divergence between Oil price and Aluminium price.

Table 3: Hindalco valuations (Old)

(Rs mn)

Entity	Assigned EV/E multiple	FY22E
Hindalco Aluminium (Including Utkal Alumina)	5.5	2,63,767
Birla Copper	5.5	65,727
Novelis	6.5	5,52,985
Combined Debt-Cash-Investment +Minority Interest		343,698
Equity value		538,782
SoTP value (Rs/share)		242
Equity investments @ 20% discount		8
Target price (Rs/share)		250
Negative value attributed on account of Aleris		(8)
Target price (Rs/share) - assigning 50% probability		242
TP at 0.5x book – assigning 50% probability		156
Blended target price		199

Source: I-Sec research

Financial summary (consolidated)

Table 4: Profit & loss statement
(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Operating Income (Sales)	1,365,902	1,251,408	1,009,492	1,355,668
Operating Expenses	1,150,425	1,080,352	914,057	1,194,961
EBITDA	154,998	145,519	85,312	142,738
<i>% margins</i>	<i>11.3</i>	<i>11.6</i>	<i>8.5</i>	<i>10.5</i>
Depreciation & Amortization	47,662	46,679	50,013	51,330
Gross Interest	37,780	33,961	32,969	32,205
Other Income	11,271	8,902	10,003	10,173
Recurring PBT	80,826	73,781	12,333	69,376
Add: Extra ordinaries	-	-	-	-
Less: Taxes	25,881	23,579	1,972	20,620
Less: Minority Interest	(7)	1,757	363	1,706
Net Income (Reported)	54,952	48,445	9,999	47,050
Recurring Net Income	54,952	48,445	9,999	47,050

Source: Company data, I-Sec research

Table 5: Balance sheet
(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Assets				
Total Current Assets	501,382	614,326	562,168	548,350
<i>of which cash & cash eqv.</i>	<i>97,866</i>	<i>109,695</i>	<i>94,687</i>	<i>44,358</i>
Total Current Liabilities & Provisions	352,272	321,458	285,601	331,370
Net Current Assets	149,110	292,868	276,568	216,980
Investments	117,342	114,791	113,828	112,866
<i>Strategic/Group</i>	<i>210</i>	<i>210</i>	<i>210</i>	<i>210</i>
<i>Other Marketable</i>	<i>117,132</i>	<i>114,581</i>	<i>113,618</i>	<i>112,655</i>
Net Fixed Assets	713,817	739,460	740,947	733,618
<i>Capital Work-in-Progress</i>	<i>40,971</i>	<i>10,810</i>	<i>10,810</i>	<i>-</i>
Goodwill	185,746	185,746	185,746	185,746
Total Assets	1,166,016	1,332,865	1,317,089	1,249,210
Liabilities				
Borrowings	554,399	676,443	654,308	543,018
Deferred Tax Liability	36,505	36,505	36,505	36,505
Minority Interest	95	1,852	2,215	3,921
Equity Share Capital	2,223.90	2,224	2,224	2,224
<i>Face Value per share (Rs)</i>	<i>1</i>	<i>1</i>	<i>1</i>	<i>1</i>
Reserves & Surplus	572,793	615,842	621,838	663,542
Net Worth	575,017	618,066	624,062	665,766
Total Liabilities	1,166,016	1,332,865	1,317,090	1,249,210

Source: Company data, I-Sec research

Table 6: Cashflow statement
(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Operating Cashflow	136,661	86,222	50,008	88,207
Working Capital Changes	(16,865)	(131,928)	1,292	9,258
Capital Commitments	(60,053)	(72,322)	(51,500)	(44,000)
Free Cashflow	59,742	(118,028)	(199)	53,465
Cashflow from Investing Activities	3,537	11,453	10,966	11,135
Issue of Share Capital	61	-	-	-
Buyback of shares	(5)	-	-	-
Inc (Dec) in Borrowings	(14,443)	122,044	(22,135)	(111,290)
Dividend paid	(3,229)	(3,640)	(3,640)	(3,640)
Extraordinary Items	-	-	-	-
Chg. in Cash & Bank balances	8,666	11,830	(15,008)	(50,329)

Source: Company data, I-Sec research

Table 7: Key ratios
(Year ending March 31)

	FY19	FY20	FY21E	FY22E
Per Share Data (Rs)				
EPS(Basic Recurring)	24.7	21.8	4.5	21.2
Diluted Recurring EPS	24.7	21.8	4.5	21.2
Recurring Cash EPS	46.1	42.8	27.0	44.2
Dividend per share (DPS)	1.2	1.4	1.4	1.4
Book Value per share (BV)	258.6	277.9	280.6	299.4
Growth Ratios (%)				
Operating Income	14.1	(8.4)	(19.3)	34.3
EBITDA	11.3	(6.1)	(41.4)	67.3
Recurring Net Income	23.9	(8.6)	(79.4)	370.6
Diluted Recurring EPS	27.5	(11.8)	(79.4)	370.6
Diluted Recurring CEPS	15.1	(7.3)	(36.9)	63.9
Valuation Ratios (x)				
P/E	3.6	4.1	20.0	4.3
P/CEPS	2.0	2.1	3.3	2.0
P/BV	0.3	0.3	0.3	0.3
EV / EBITDA	4.3	4.5	9.0	5.3
EV / Operating Income	0.5	0.5	0.8	0.6
EV / Operating FCF	4.9	7.6	15.3	8.6
Operating Ratios (%)				
Raw Material/Sales	58.0	69.5	72.5	71.3
SG&A/Sales	13.0	3.6	4.3	3.2
Other Income / PBT	13.9	12.1	81.1	14.7
Effective Tax Rate	32.0	32.0	16.0	29.7
NWC / Total Assets	4.4	13.7	13.8	13.8
Inventory Turnover (days)	86.5	77.0	83.0	64.0
Receivables (days)	28.8	48.3	76.5	57.7
Payables (days)	109.9	113.8	121.2	94.2
D/E Ratio (x)	1.03	1.15	1.11	0.87
Profitability Ratios (%)				
Net Income Margins	4.0	4.0	1.0	3.6
RoCE	10.3	8.6	3.4	7.9
RoNW	9.8	8.4	1.7	7.6
Dividend Payout Ratio	4.9	6.4	31.2	6.6
Dividend Yield	1.1	1.3	1.3	1.3
EBITDA Margins	11.3	11.6	8.5	10.5

Source: Company data, I-Sec research

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