

1 June 2009

India Non Ferrous Metals

Riding the trough; Buy Sterlite, Hindustan Zinc

Overweight

Nifty/Sensex: 4449/14625



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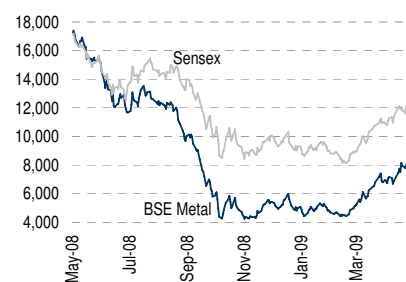
- Initiating at Overweight.** India's low-cost base-metal producers are riding out the current trough with élan, and we expect them to do much better when demand picks up in FY11 as economic stimulus packages percolate into the real economy. We like companies with strong balance sheets, those that can add significant capacity without denting their bottom lines.
- Indian players at the lower end of the cost curve.** Despite the steep fall in metals prices, Indian base metal producers are profitable given they lie at the lower end of the global cost curve. We expect them to show resilience even with subdued demand.
- Domestic demand to provide a cushion.** We expect domestic demand for base metals to grow at 8% in FY10 (1.5 times IIP growth). Relatively strong domestic demand should cushion the impact of the global slowdown, in our view.
- Further slide in base metal prices unlikely.** Prices of most base metals are now below the marginal cost of production. Loss-making producers are slashing capacity and shuttering high-cost operations. We expect this to support prices at current levels.
- Strong balance sheet – key selection criterion.** We prefer companies with healthy balance sheets and large expansion plans. We initiate coverage on Hindustan Zinc and Sterlite with Buy ratings, Nalco with Hold and Hindalco with Sell.

Sector snapshot

	HZL	Sterlite	Nalco	Hindalco
Rating	Buy	Buy	Hold	Sell
Price (Rs) as of 29 May '09	582	622	354	85
Target Price (Rs)	872	748	380	68
Upside (%)	50	20	7	-20
Market Cap. (US\$bn)	5.2	9.4	4.8	3.2
EPS (Rs) – FY10e	69.2	40.3	21.8	2.3
PE (x) – FY10e	8.4	15.4	16.2	36.8
EV/EBITDA (x) – FY10e	4.6	11.2	8.9	5.9
EV/Sales (x) – FY10e	2.2	2.0	4.1	0.6
RoE (%) – FY10e	19.9	13.5	14.0	3.3

Source: Company, Anand Rathi Research

BSE Metals vs. Sensex



Source: Anand Rathi Research

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