

Company Update

Gujarat NRE Coke

MARKETPERFORMER

CMP Rs. 54

Sensex: 15,379

Price Target: Rs 58

ANALYST

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Background: Gujarat NRE Coke Ltd (GNCL) was incorporated in 1986 to produce coke, semi-coke and lignite. It is one of the largest producers of metallurgical coke with capacity in excess of 1 MTPA and having reserves of more than 500 million tons. GNCL also operates a 0.3 MTPA capacity mini steel mill to manufacture TMT bars by recycling steel scraps and using wind energy (27.5 MW). The coke business contributes nearly 70% of the total sales, while the steel business contributed the rest.

AT A GLANCE

Issued Equity Capital (Cr. shrs)	47.69
Mkt. Cap (Rs.in Crs/US\$m)	2766/564
Shareholding pattern	
Promoters (%)	45.08
Free Float (%)	54.92
Avg. Daily Vol.('000)	2079.42
Sector:	Mining
Bloomberg/Reuters Code:	GNC.IN/ GJNC.BO

FORECASTS AND VALUATION

FY Mar(Rs. Crore)	FY08 A	FY09 A	FY10 E
Turnover	887.06	1946.90	2318.50
EBITDA	205.14	446.30	584.25
Pre-tax Profit	217.16	371.70	491.10
Net Profit	169.25	311.20	367.30
Net Pft (Pre Ex.)	169.25	311.20	367.30
EPS (Rs)	5.80	6.60	7.79
DPS (Rs)	2.90	1.00	1.60
BV Per Share (Rs)	32.60	29.30	35.49
PE (X)	9.31	8.18	6.94
Net Div Yield (%)	5.37%	1.85%	2.96%
P/BV (X)	1.66	1.84	1.52
Net Debt/Equity (X)	0.58	0.6	0.54
ROE (%)	19.8	25.2	23.5

Steaming up

Story... Steel production is set to have recovered from its recent lows with major steelmakers across the globe having increased prices in the recent past. Indian steelmakers too have seen demand pick up in recent months. With demand improving from the steel sector, we see improved visibility for metallurgical coke demand.

Point... Gujarat NRE Coke Limited, the largest independent manufacturer of Low Ash Metallurgical Coke in India with capacity in excess of 1 MTPA and having reserves of more than 500 million tons. GNCL also operates a 0.3 MTPA capacity mini steel mill to manufacture TMT bars by recycling steel scraps and using wind energy (27.5 MW). Traditionally, metallurgical coke prices have been determined by the price of the landed cost of Chinese coke. The price of Chinese coke is influenced by quota controls and export taxes determined by the Government of China. Higher Chinese coke prices and lower coking coal prices translate to greater profit for companies like Gujarat NRE Coke.

Gujarat NRE Coke is well placed to tap this and plans to scale up its metallurgical coke production by five times to 5.9 MTPA by 2012 and subsequently to 7.1 MTPA in 2014. As a part of this, Gujarat NRE Coke has acquired mining properties in Australia which would help it secure raw material supplies.

Outlook... Gujarat NRE Coke, being the largest merchant producer of metallurgical coke in India is best poised to benefit from a recovery in coke demand. The company is a good bet in the mining sector in the current market scenario, given that the company caters primarily to the domestic market. In the event of a decline in realisations, the company would be fairly insulated, as it has captive coal mines which enjoy very low production costs.

We expect coke prices to benefit due to growing demand from major consumption sectors and tightening supply of coking coal in the market. The stock is currently trading at 7X its FY10E EPS. We continue to rate Gujarat NRE Coke a MARKETPERFORMER with an enhanced price target of Rs.58.

Financial performance review

Particulars (in Rs. Crs)	Q4 FY09	Q4 FY08	YoY	Q3 FY09	QoQ	Comments
Net Sales	310.04	377.64	-17.90%	214.58	44.49%	Lower price realisation Raw material costs decline
Expenses	293.15	251.16	16.72%	293.99	-0.29%	
EBITDA	16.89	126.48	-86.65%	-79.41	-121.27%	
Depreciation	11.36	7.54	50.66%	11.94	-4.86%	
Other income	24.61	4.48	449.33%	1.79	1274.86%	
interest	24.60	9.73		24.57	0.12%	
PBT	5.54	113.69	-95.13%	-114.13	-104.85%	
Tax	1.90	19.29	-90.15%	-10.95	-117.35%	
EOI	0.00	0.00		-102.22		
PAT	3.64	94.40	-96.14%	-0.96	-479.17%	
EBITDA margin	5.45%	33.49%		-		
Tax rate	34.30%	16.97%		-		
Net profit margin	1.17%	25.00%		-		

For the quarter ended June FY10, Gujarat NRE Coke (GNC) revenues dropped by 17.90 percent YoY to Rs 310.04 crores while its Net Profit declined by 96.14 percent to Rs. 3.64 crores. However, on a sequential quarter basis, sales grew by 44.49 percent pointing towards a recovery in the metallurgical coke market.

Revenue slump on lower price realisations: Q1FY10 net sales declined 17.90 percent to Rs. 310.04 crores compared to Rs. 377.64 crores in Q1FY09 primarily due to lower price realisations. Coke price realisations declined by 44 percent to USD259.00 year-on-year. However, this slide was partially offset by a 20 percent increase in met coke sales volume.

The Q1FY10 results fared better when compared to Q4FY09, as both price realisations and sales volume improved significantly. Sales grew by 44.49 percent driven by a 33 percent surge in volume and a 32 percent increase in realisation.

Earnings take a hit: EBITDA plunged from Rs. 126.48 crores to Rs. 16.89 crores Y-o-Y, bogged down by the impact of lower realisations. However, on the positive front raw material costs were down and the company benefited from improved operating leverage. EBITDA margin was 5.45 percent in Q1FY10 compared to 33.49 percent in Q1FY09.

Depreciation decreased by 50.66 percent to Rs.11.36 crores, while other income grew four fold to Rs.24.61 crores. Overall, net profit declined 96.14 percent from Rs.94.40 crores to Rs.3.64 crores.

Risks & Concerns Our rating carries a risk from a faster than expected recovery in steel demand or a prolonged slowdown in demand for metcoke. Historically, commodity business is risky primarily due to great price-volatility resulting in earnings-volatility. The risk element stems from the cyclical nature of business.

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STOCK RATING: Outperformer: > 20% upside over the next 12 months; Marketperformer: trade within a +/-20% range over the next 12 months; Underperformer: > 20% downside over the next 12 months.