



15th October 2010

Coal India Limited- The Black Gold Behemoth

Recommendation: **Subscribe**



| Issue Summary | | |
|---------------------------------|-------------------------|----------|
| Price Band (Rs)* | 225 | 245 |
| Bid Lot | 25 shares | |
| Face Value | Rs.10 | |
| Opens on | 18 th Oct'10 | |
| Closes on | 21 th Oct'10 | |
| Total no of shares to be raised | 63.16 cr | |
| Pre-issue share capital | Rs 6,316cr | |
| Post-issue share capital | Rs 6,948 cr | |
| Fresh Issue Size (Rs cr) | 14,212 | 15,475 |
| Post Issue Mkt Cap (Rs cr) | 1,56,321 | 1,70,216 |
| P/E on Annualized FY11 | 13.2 | 14.4 |

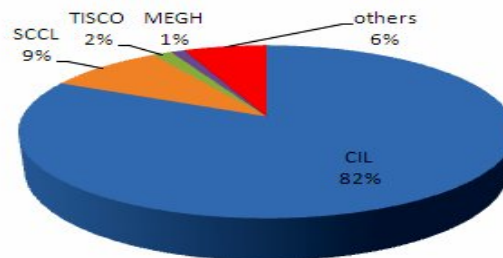
Book Running Lead Managers:

- ENAM Securities
- Kotak Mahindra
- Deutsche Bank
- DSP Merrill Lynch
- Morgan Stanley
- Citigroup

*Note: Discount to retail investors 5%.

Company & Business Profile

Coal India Limited (CIL) is a government of India owned undertaking engaged into coal mining in India. The company has more than 80% of the market share in domestic coal production and operates 471 coal mines in 21 coalfields spanning across 8 states. The mines includes 163 open cast mine, 273 underground mine and 35 mixed mine (inclusive of both open cast and underground mines).



Source: RHP, Arianth Research

The company has estimated coal resources of around 64bn tonne and reserves of 18.8mn tonne. CIL operates through its 9 wholly owned subsidiaries, of which 1 subsidiary is engaged in exploration and feasibility study analysis. CIL has total reserves of 64.3 bn tonne and proved reserves of 52.4bn tonne, of which extractable reserves stand at 21.7 bn tonne. For FY10, CIL's production stood at 431mn tonne of which approx 90% was from open cast mines, while balance was from underground mines. Based on the current reserve base as indicated in the table below, the estimated life of these reserves; based on FY10 production, is more than 100 years.

Coal Reserves and resources

| Resources (bn tonne) | | | Reserves (bn tonne) | | |
|----------------------|----------------------|-------|---------------------|----------|-------|
| Measured | Inferred & Indicated | Total | Proved | Probable | Total |
| 51.3 | 12.9 | 64.2 | 10.6 | 8.2 | 18.8 |

Source: RHP, Arianth Research

Objects of the Issues

| Objects | Amount (Rs cr) |
|---|----------------|
| Divestment of Government's 10% stake in the company | 14212-15475 |

Source: RHP, Arianth Research

CIL is the Largest coal producer in the world, having 6% of global coal reserves.

Investment Positives

- **Strong resource base**

CIL is the world's largest coal company on reserves and production basis with 6% of global coal reserves under it. Unlike many other global coal companies 90% of its production is from open pit mines, while 10% is from under ground mine. This enables it to maintain lower production cost i.e around US\$ 18/tonne and is one of the lowest cost coal producer in the world. The company is also a market leader in india, accounting for more than 80% of the domestic coal production.

- **Expansion of coal production capacity**

CIL, in order to cater to growing consumption of coal in india, is expanding its production capacity. As of FY10 end, 45 projects that includes 22 capacity expansion project from existing mines and 23 new mining projects, have recived approval from its board. Accordingly, CIL would be adding production capacity of 47.5mn tonne by FY12 end and 33.3mn tonne at the end of 12th five year plan (FY12-FY18).

CIL would also be adding 20 beneficiation plants having aggregate capacity of 111mn tonne by FY18. At present company is selling raw coal at a significant discount to global prices. Addition of these facilities would help CIL to garner higher margins as beneficiated coal commands higher realisation compared to raw coal it sales, on account of higher calorific value and lower ash content.

- **Focused towards improving productivity**

CIL intend to enhance its productivity through mix of rationalisation of work force and increased mechanisation. CIL is extensivley doing investments toward mechanisation of its mines and reducing is workforce through natural attrition. At present, CIL has excesee manpower employed at many of its mines, thus resulted into higher employee cost and lower profitability.

- **Strong Balance sheet**

CIL has healthy balance sheet with strong cash at its disposal. The company has just Rs 1,779 cr of debt in its books against cash and cash equivalent of Rs 38,046 cr. On post issue equity capital, on per share basis, this translates into Rs 55 per share, which is approximately 22% of its upper price band.

- **Domestic demand to remain robust going forward**

Demand for coal in India is expected to remain robust. Consumption is expected to grow at 9-10% CAGR over next 5-10 years, while production is not expected to grow in sync with demand. Of the 66GW of power projects that are coming up over the next five years, 80% of them would be coal based, hence we expect CIL to continue to post sustainable volume growth going forward.

Land acquisition and regulatory issues could adversely affect the future plans and profitability

Concerns

■ Environmental and Land issues

Many of the mining projects those are to be developed by miner, have lately been facing regulatory hurdles in getting environmental clearances, as many mines are located in ecologically sensitive areas, and is hampering the progress of these mines. Similarly, acquiring a land for mining operations and rehabilitation of surrounding area is another area of concern for prospective mine developers. All these issues have resulted into delay in opening of these mines.

■ Regulated by Government policies

CIL being a government owned entity has to comply with government directives in pricing its coal and is not free to price coal on the basis of prevailing market rates. CIL had, over the last 11 years, managed effect price hike just five times and that was largely to compensate cost escalation and inflation effect and has not been able to reap the benefits of higher global prices.

■ Risk of sharing 26% of its profit with locals

Government of India, through its proposed Mines and Mineral development bill, is planning to make it mandatory for the companies, having mining operations, to share 26% of their profits with local inhabitants and persons displaced by the mining activity. We believe, implementation of act could affect the future earnings of CIL.

Profit & Loss Account

(Rs.in cr)

| Paticulars | FY 2008 | FY 2009 | FY 2010 | 1QFY2011 |
|------------------------------|------------|------------|-------------|------------|
| Net Sales | 32,634 | 38,789 | 44,615 | 11,436 |
| Other Income | 5,983 | 7,275 | 7,977 | 1,647 |
| Total Income | 38,617 | 46,064 | 52,592 | 13,110 |
| Total Expenditure | 28,858 | 38,538 | 37,123 | 8,902 |
| EBITDA | 3,776 | 255 | 7,420 | 2,534 |
| EBIDTA (%) | 11.6 | 0.7 | 16.6 | 22.2 |
| Depreciation | 1,530 | 1,663 | 1,314 | 409 |
| Interest | 150 | 157 | 137 | 52.1 |
| Prior Period Adjustments | 111.1 | 27.7 | (53.6) | (11.1) |
| Profit Before Tax | 8,190 | 5,739 | 13,965 | 3,736 |
| Provision for Tax | 3,474 | 3,644 | 4,343 | 1,210 |
| Profit after Tax | 4,716 | 2,075 | 9,622 | 2,526 |
| Extra Ordinary Items | 527 | 3.3 | - | - |
| Profit After Tax after EO | 5,243 | 2,079 | 9,622 | 2,526 |
| Adjustment for restatement | (958) | 1,984 | 212 | (4) |
| Profit after tax (Restated) | 4,285 | 4,063 | 9,834 | 2,522 |
| PAT (%) | 13.1 | 10.5 | 22.0 | 22.1 |
| EPS (Rs)(Pre Issue) | 6.7 | 6.4 | 15.6 | 4.0 |
| EPS (Rs) (Post Issue) | 6.2 | 5.8 | 14.5 | 3.6 |

Source: RHP, Arihant Research

CIL is available at 11.8x its annualised FY11 EV/EBITDA on upper end of price band and 14.4x its annualised FY11 EPS.

Valuations

At the upper end of price band of Rs 245, the stock is available at 11.8x its annualised FY11 EV/EBITDA and 14.4x its annualised FY11 EPS, which we believe is at par with its global peers. Going forward, we believe CIL should trade at premium to its peers given its enormous size and scale along with estimated robust coal demand in India. Company's huge cash reserves, which translate into Rs 55 per share (22% of upper price band), further justifies our positive stance on the fundamentals of the company. **We recommend subscribe to CIL IPO.**

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