

Power Costs Eases; More Headwinds than Tailwinds ahead

Est. Vs. Actual for Q3FY23: Revenue –**INLINE**; EBITDA – **BEAT**; PAT – **BEAT**

Growth Estimates YoY for NALCO post-Q3FY23 results:

FY24E/FY25E: Revenue (2%)%/2%; EBITDA (15%)%/14%; PAT (18%)%/16%

Recommendation Rationale

- **Power costs eased in Q3FY23:** Power and fuel costs eased QoQ on account of a drop in coal prices. Going forward, we expect power costs to decline further in Q4FY23 QoQ. However, with the onset of summer in Q1FY24, the domestic coal supply concerns could put pressure on margins again.
- **Aluminium prices retreated** on 10th Feb after the brief rally in Jan'23 (LME went up by 12% since 1st Jan to the peak of \$2,624/t on 25th Jan and retreated to \$2,405/ton on 10th Feb'23). The price rally in Jan'23 was on account of optimism on China's reopening and the Fed reaching a pivot. However, the recent drop in thermal coal prices, uncertainty on Fed pivot, and recent inventory build-up on LME exchanges (~100kt jump in inventory on 8th Feb) led to a drop in prices. We forecast LME aluminium price at \$2,430/2,440/t for FY2024/25E versus the spot at US\$2,405/t.
- **Alumina prices have firmed up** with spot prices at \$363/t surging ahead of the Q3FY23 average of \$320/t on account of supply disruption in Australia which could support Alumina division EBIT in the coming quarter. However, Q3FY23 EBIT/t of the Alumina division stood at \$25/t, much below the peak of \$157/t in Q3FY22 when Alumina prices rose to \$400/t+ (spot at \$363/t).

Sector Outlook: Cautiously positive on Aluminium, prefer Aluminium names over steel.

Company Outlook & Guidance: The 1mtpa capacity expansion of the Alumina refinery is targeted to be commissioned by Jan'24. However, with less than 5% Capex spent till FY22, the commissioning is likely to be delayed and could exceed the initial Capex estimate of Rs 6,436 Cr (on Dec'18 price level). Nalco got approved for the mine plan for Utkal D&E coal blocks in Feb'22. However, coal production has not commenced due to land and other issues and it has now sought an extension on linkages to the Utkal D&E block for 2 more years.

Current Valuation: 5.5x EV/EBITDA on FY25E EBITDA (rollover from FY'24 EBITDA).

Current TP: Rs 84/share (Earlier TP: Rs 70/share)

Recommendation: Capex requirement and probable cost overruns over the next few years on alumina refinery plant expansion along with delay in commissioning of coal blocks could put pressure on the cash flows of the company. We maintain our **HOLD** rating on NALCO.

Financial Performance: Nalco reported a decent set of Numbers with EBITDA/PAT beating our estimate on lower-than-expected power and employee costs. Revenue (largely inline), declined by 13%/6% YoY/QoQ, led by lower Alumina sales and a drop in LME Aluminium prices (down 15%/1% YoY/QoQ). EBITDA de-grew by 61% YoY, but recovered sequentially by 38% beating our estimate on account of lower-than-expected power & fuel expense (down 20% QoQ vs our expectation of a 14% drop), and lower employee costs (7% below our estimate, but up 20% QoQ). PAT at Rs 256Cr, de-grew by 69% YoY, but improved by 104% QoQ led by higher sequential EBITDA.

Outlook: End user demand pick up from China along with the Fed pivot will decide the price trajectory of aluminium from the current uncertainty. With the correction in thermal coal prices, the cost support to the Aluminium prices could be fading further. With the delay in the commissioning of Coal blocks and probable cost overruns at the Alumina refinery expansion, we maintain our **HOLD** rating on NALCO.

Valuation & Recommendation: We value the company at 5.5x FY25 EBITDA (from FY24) and 0.5x book value of CWIP. The TP implies an upside of 9% from the CMP. We maintain our **HOLD** rating on the stock.

Key Financials (Consolidated)

(Rs Cr)	Q3FY23	QoQ (%)	YoY (%)	Axis Est.	Variance
Net Sales	3,290	-6%	-13%	3,225	2%
EBITDA	460	38%	-61%	286	61%
EBITDA %	14%			9%	
PAT	256	104%	-69%	142	81%

Source: Company, Axis Research

(CMP as of 10th Feb 2023)

CMP (Rs)	77
Upside /Downside (%)	9%
High/Low (Rs)	132/67
Market cap (Cr)	14,096
Avg. daily vol. (6m) Shrs.	139,97,207
No. of shares (Cr)	183

Shareholding (%)

	Jun-22	Sep-22	Dec-22
Promoter	51.28	51.28	51.28
FII	16.71	14.69	15.05
Mutual Funds / UTI	10.11	10.79	9.89
Financial Institutions	0.00	0.00	0.00
Others	21.9	23.24	23.78

Financial & Valuations

Y/E Mar (Rs Cr)	FY23E	FY24E	FY25E
Net Sales	14,094	13,829	14,080
EBITDA	2,157	1,839	2,091
Net Profit	1,099	906	1,052
EPS (Rs.)	6.0	4.9	5.7
PER (x)	12.8	15.5	13.4
P/BV (x)	1.1	1.1	1.1
EV/EBITDA (x)	5.2	6.5	5.9
ROE (%)	0.1	0.1	0.1

Change in Estimates (%)

Y/E Mar	FY23E	FY24E	FY25E
Sales	2%	5%	5%
EBITDA	26%	10%	22%
PAT	43%	17%	37%

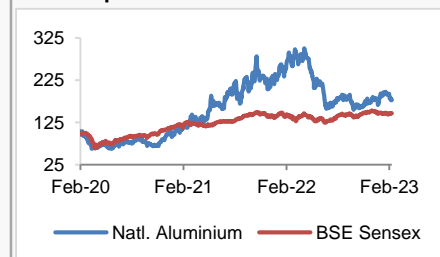
ESG disclosure Score**

Environmental Disclosure	NA
Social Disclosure Score	NA
Governance Disclosure	NA
Total ESG Disclosure Score	NA

Source: Bloomberg, Scale: 0.1-100

**Note: This score measures the amount of ESG data a company reports publicly and does not measure the company's performance on any data point. All scores are based on 2020 disclosures

Relative performance



Source: Capitaline, Axis Securities

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Key Risks to our Estimates and TP

- Higher Aluminium/Alumina prices than our assumption could post an upside risk to our TP.
- Lower/higher-than-expected power costs could pose an upside/downside risk to our TP.

Change in Estimates

	New			Old			% Change		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Sales	14,094	13,829	14,080	13,806	13,224	13,396	2%	5%	5%
EBITDA	2,157	1,839	2,091	1,705	1,665	1,714	26%	10%	22%
PAT	1,099	906	1,052	769	772	765	43%	17%	37%

Source: Company, Axis Securities

Results Review

	Q3FY22	Q2FY23	Q3FY23	Q3FY23	Q3FY23	YoY	QoQ	vs Axis	vs Consensus
	Actual	Actual	Axis Est	Consensus	Actual	%	%	%	%
Revenues	3,773	3,490	3,225	3,184	3,290	-13%	-6%	2%	3%
Consumption of Raw Materials	514	707	689		876	70%	24%	27%	
Changes in inventories	93	163	-		-122	NA	NA	NA	
Power & Fuel	872	1,378	1,270		1,099	26%	-20%	-14%	
Employees Cost	594	391	505		469	-21%	20%	-7%	
Other Expenses	511	515	475		508	-1%	-1%	7%	
Total Expenditure	2,583	3,155	2,939		2,830	10%	-10%	-4%	
EBITDA	1,191	334	286	190	460	-61%	38%	61%	143%
EBITDA margin (%)	32%	10%	9%		14%				
Depreciation	151	154	159		157	4%	2%	-1%	
Other Income	72	69	64		66	-8%	-4%	4%	
Interest Expense	2	4	2		4	121%	3%	130%	
Tax	278	76	47		91	-67%	20%	93%	
Share Of P/L Of Associates	-0.2	-44.7	-		-17.5	NA	NA	NA	
PAT	831	125	142	62	256	-69%	104%	81%	315%
EPS (Rs)	4.52	0.68	0.77		1.4	-69%	105%	82%	
Segmental Results									
Chemicals	1,565	1,507	1,201		1,265	-19%	-16%	5%	
Aluminum	2,515	2,308	2,286		2,416	-4%	5%	6%	
Unallocated Common	8	25	17		16	97%	-35%	-8%	
Less: Inter-segment revenue	-315	-351	-279		-406	NA	NA	NA	
Total Revenue from Operations	3,773	3,490	3,225		3,290	-13%	-6%	2%	
Chemicals	420	88			64	-85%	-27%	NA	
Aluminum	748	177			284	-62%	60%	NA	
Segmental EBIT	1,168	265			347	-70%	31%	NA	
EBIT Margin %									
Chemicals	27%	6%			5.1%				
Aluminum	30%	8%			11.7%				
Segmental EBIT	31%	8%			10.6%				
Aluminum Share of EBIT	64%	67%			82%				
LME Aluminum	2,756	2,362	2,336		2,362	-14%	0%	1%	

Source: Company, Axis Securities

Financials (Consolidated)

Profit & Loss

(Rs Cr)

Y/E March	FY 22A	FY 23E	FY 24E	FY 25E
Total Operating income	14,181	14,094	13,829	14,080
Consumption of Raw Materials	1,971	3,112	3,152	3,164
Increase/Decrease in Stocks	(117)	(100)	-	-
Power & fuel	3,388	4,934	4,751	4,618
Employees Cost	2,356	1,922	1,957	2,013
Other Expenses	2,065	2,069	2,130	2,194
Total Expenditure	9,664	11,937	11,990	11,989
EBITDA	4,517	2,157	1,839	2,091
Depreciation and Amortization	837	864	953	1,016
EBIT	3,681	1,292	886	1,074
Other Income	297	322	329	335
Share Of P/L Of Associates (Net of Tax)	(1)	(83)	-	-
Less: Interest & Fin Chg.	23	14	8	8
Less: Exceptional Items	-	-	-	-
Profit before tax	3,954	1,517	1,207	1,402
Provision for Tax	1,003	419	301	349
Reported PAT	2,951	1,099	906	1,052

Source: Company, Axis Securities

Balance Sheet

(Rs Cr)

Y/E March	FY 22A	FY 23E	FY 24E	FY 25E
Net Block	7,002	6,887	6,684	6,418
CWIP	1,763	2,513	3,263	4,013
Intangible assets	813	813	813	813
Investments	375	375	375	375
Inventories	1,646	1,738	1,705	1,736
Trade Receivables	75	154	152	154
Cash / Bank balance	3,706	2,796	2,245	1,887
Misc. Assets	1,895	1,895	1,895	1,895
Total assets	17,276	17,171	17,132	17,291
Equity capital	918	918	918	918
Reserves	11,634	11,539	11,526	11,660
Borrowings	21	21	21	21
Def Tax Liabilities	868	868	868	868
Other Liabilities	1,989	1,989	1,989	1,989
Provisions	388	388	388	388
Trade Payables	1,457	1,448	1,421	1,447
Capital employed	17,276	17,171	17,132	17,291

Source: Company, Axis Securities

Cash Flow

(Rs Cr)

Y/E March	FY 22A	FY 23E	FY 24E	FY 25E
Profit after tax	2,951	1,099	906	1,052
Depreciation	837	864	953	1,016
Interest Expenses	23	14	8	8
Non-operating / EO item	81	-	-	-
Change in W/C	66	(180)	8	(8)
Operating Cash Flow	3,958	1,798	1,875	2,068
Capital Expenditure	(927)	(1,500)	(1,500)	(1,500)
Free cash Flow	3,032	298	375	568
Other Investments	(1,693)	-	-	-
Investing Cash Flow	(2,619)	(1,500)	(1,500)	(1,500)
Proceeds / (Repayment) of Borrowings	(30)	-	-	-
Payments for buy-back of equity shares	-	-	-	-
Finance cost paid	(8)	(14)	(8)	(8)
Dividend paid	(1,102)	(1,194)	(918)	(918)
Financing Cash Flow	(1,140)	(1,208)	(926)	(926)
Change in Cash	199	(910)	(551)	(358)
Opening Cash	214	413	(498)	(1,049)
Closing Cash	413	(498)	(1,049)	(1,407)

Source: Company, Axis Securities

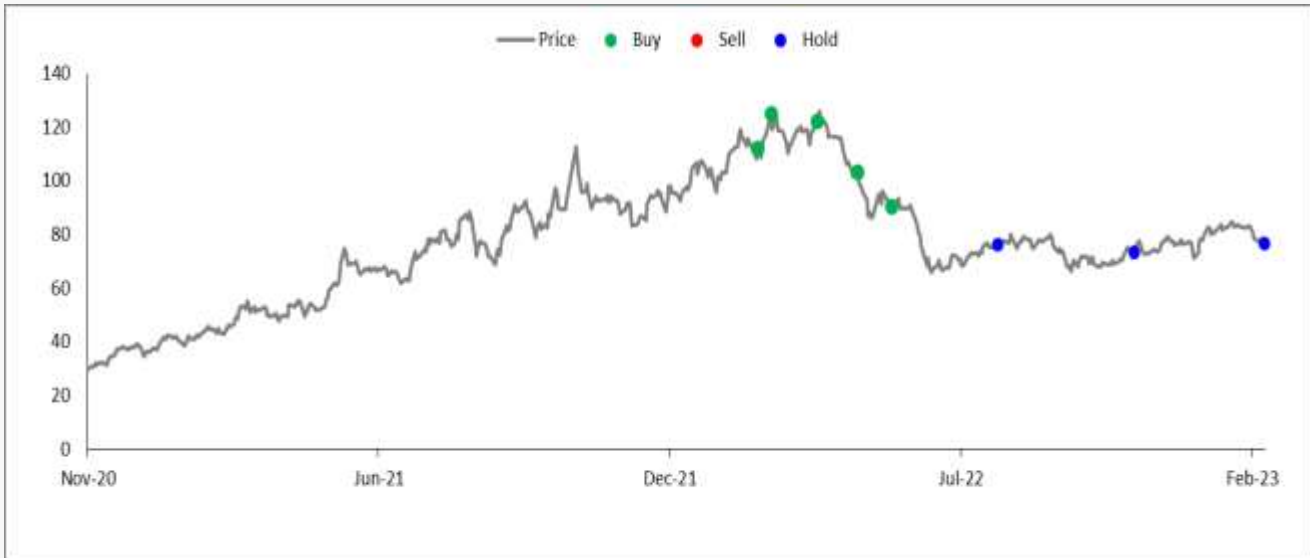
Ratio Analysis

(%)

Y/E March	FY 22A	FY 23E	FY 24E	FY 25E
Operational Ratios				
Sales growth (% YoY)	58%	-1%	-2%	2%
EBITDA growth (% YoY)	153%	-52%	-15%	14%
Op. profit growth (% YoY)	213%	-65%	-31%	21%
Net Profit growth (% YoY)	127%	-63%	-18%	16%
EBITDA Margin %	32%	15%	13%	15%
Net profit Margin %	21%	8%	7%	7%
Tax Rate %	25%	26%	25%	25%
Efficiency Ratios				
Total Asset Turnover (x)	0.9	0.8	0.8	0.8
Sales/Gross block (x)	1.3	1.2	1.1	1.1
Sales/Net block(x)	2.0	2.0	2.1	2.2
Working capital/Sales (x)	0.02	0.03	0.03	0.03
Valuation Ratios				
PER (x)	5.8	12.8	15.5	13.4
P/BV (x)	1.4	1.1	1.1	1.1
EV/Ebitda (x)	3.0	5.2	6.5	5.9
EV/Sales (x)	0.9	0.8	0.9	0.9
Dividend Yield (%)	7.0%	6.5%	6.5%	6.5%
Return Ratios				
ROE	25.4%	8.8%	7.3%	8.4%
ROCE	25.9%	8.3%	5.7%	6.9%
ROIC	16.9%	6.3%	4.5%	5.6%

Source: Company, Axis Securities

NALCO Price Chart and Recommendation History



Date	Reco	TP	Research
22-Feb-22	BUY	150	Initiating Coverage
03-Mar-22	BUY	150	Top Picks
04-Apr-22	BUY	150	Top Picks
02-May-22	BUY	150	Top Picks
26-May-22	BUY	107	Result Update
10-Aug-22	HOLD	85	Result Update
14-Nov-22	HOLD	70	Result Update
13-Feb-23	HOLD	84	Result Update

Source: Axis Securities

About the analyst

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Sector: Metals & Mining

Analyst Bio: Aditya Welekar is PGDBM in Finance with 12 years of experience in Equity Market/Research.

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HOLD	Between 10% and -10%
SELL	Less than -10%
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