

INDIA

Gujarat NRE Coke

3 November 2008

GNC IN

Outperform

Stock price as of 31 Oct 08	Rs	30.00
12-month target	Rs	136.00
Upside/downside	%	+353.3
Valuation	Rs	136.00
- Sum of Parts		

GICS sector		materials
Market cap	Rs m	14,158
30-day avg turnover	US\$m	4.8
Market cap	US\$m	287
Number shares on issue	m	471.9

Investment fundamentals

Year end 31 Mar		2008A	2009E	2010E	2011E
Total revenue	m	8,871	34,913	53,027	56,878
EBITDA	m	2,051	9,896	18,115	17,411
EBITDA growth	%	313.0	382.4	83.1	-3.9
Adjusted profit	m	1,693	4,678	8,798	7,343
EPS adj	Rs	4.80	9.42	17.86	14.91
EPS adj growth	%	349.7	96.1	89.5	-16.5
PE adj	x	6.2	3.2	1.7	2.0
Total DPS	Rs	2.20	2.00	0.68	1.11
Total div yield	%	7.3	6.7	2.3	3.7
ROA	%	6.2	17.8	22.4	17.7
ROE	%	16.6	23.1	29.8	19.9
EV/EBITDA	x	4.3	1.3	0.7	0.8
Net debt/equity	%	32.1	-6.3	-11.6	4.7
Price/book	x	0.7	0.6	0.4	0.4

GNC IN rel SENSEX performance, & rec history



Source: Datastream, Macquarie Research, November 2008 (all figures in INR unless noted)

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Lean season, strong results

Event

- **2Q FY09 results above estimates:** GNC declared its standalone 2Q FY09 results which beat our expectations by 39% on operating level and 42% at the net profit level. We are adjusting our target price from Rs251 to Rs136 to factor in a 40% dilution following the bonus issue and to take into account a slowdown in coke prices.

Impact

- **Strong results in a weak season:** Net sales at Rs4.96bn increased nearly four fold YoY due to 1.4x volumes and 1.5x realization increases. EBITDA at Rs1.5bn increased 737% YoY and net income at Rs1.1bn was up 776% YoY.
- **Adjusting for bonus, rights and warrants:** The company issued bonus shares in the ratio of 2:5, which increased the outstanding share count by 40%. However, the warrants which were issued to the promoters earlier will go unsubscribed in the current market situation. Furthermore, nearly 1.1m shares will be added following the issue of DVR shares. Adjusting for these, the number of fully diluted shares is likely to increase by 28% to 493m shares.
- **Adjusting estimates by introducing discounts to our forecasts:** We have introduced a discount to our coke price forecast to account for current market situation. However, both the depreciating Indian rupee and Australian dollar against USD have led to margin expansion at both subsidiary and parent level.
- **Mine development on schedule:** The company is experiencing extremely encouraging progress on the mine development front. Management remains confident of reaching its 7mtpa coal production target in time. It is also studying the possibility of a long wall opening as early as 2010 and should be able to come up with a feasibility plan in next 3-4 months.

Earnings revision

- We have reduced our EPS estimates by 33%, 25%, and 30%, for FY3/09E to FY3/11E, respectively.

Price catalyst

- 12-month price target: Rs136.00 based on a Sum of Parts methodology.
- Catalyst: Meeting coal production targets and strong coke prices

Action and recommendation

- **Maintain Outperform:** The stock price has fallen sharply on concerns of slowing demand and falling coke prices. However, we see little risk to our FY3/09 numbers as coke shipments are fully sold up to December 2008 and nearly 30% is booked for first half of 2009. The depreciating INR and AUD have also helped to increase margins. The stock is trading at an extremely attractive level of 1.7x FY3/10 PER and 0.7x FY3/10 EV/EBITDA in our view.

Please refer to the important disclosures and analyst certification on inside back cover of this document, or on our website www.macquarie.com.au/research/disclosures.

Changing our target price

- We are reducing our target price from Rs251 earlier to Rs136 (using sum of parts as shown below) mainly to account for equity dilution caused by the bonus share issue and also to reflect the weaker price scenario for coke.

Fig 1 GNC – sum of parts

	NPV (Rs/share)	% of total value
Gujarat NRE Coke - standalone	53	39.1%
60% stake in BNCL	0	0.1%
Gujarat NRE Minerals (GNM AU)	78	57.6%
14% stake in Rey Resources	0	0.3%
12% stake in Pluton Resources	1	0.7%
10% stake in Pike river coal	3	2.1%
Total	136	

Source: Macquarie Research, November 2008

Change in estimates

- We are reducing our EPS estimates by 33%, 25% and 30% for FY3/09, FY3/10 and FY3/11, respectively to account for the equity dilution.

Fig 2 Adjusting our estimates

	Sales (Rsm)			EBITDA (Rsm)			PAT (Rsm)			EPS (Rs)		
	Old	New	% chg	Old	New	% chg	Old	New	% chg	Old	New	% chg
FY3/09E	32,015	34,913	9%	10,761	9,896	-8%	5,241	4,678	-11%	14.3	9.5	-33%
FY3/10E	46,348	53,027	14%	17,628	18,115	3%	9,145	8,798	-4%	23.8	17.9	-25%
FY3/11E	47,080	56,878	21%	18,047	17,411	-4%	8,212	7,343	-11%	21.3	14.9	-30%

Source: Macquarie Research, November 2008

- Number of shares are adjusted due to:
 - ⇒ 2:5 bonus issue which led to increase of 135m new shares.
 - ⇒ 32.5m warrants to go unsubscribed due to current market situation.
 - ⇒ Approximately 1.1m new shares will be issued in form of differential voting rights issue.
- We have taken 10% discount to our coke price forecasts to reflect a realistic scenario of slowdown in demand.
- Price cuts are mainly neutralized by depreciation of both Indian rupee and Australian dollar against USD.

Fig 3 Changing our assumptions

	INR/US\$			US\$/AUD			Coke price (US\$/t)			Number of shares (m)		
	Old	New	% chg	Old	New	% chg	Old	New	% chg	Old	New	% chg
FY3/09E	43.6	47.9	10%	0.92	0.78	-15%	667	601	-10%	385	493	28%
FY3/10E	41.9	49.0	17%	0.88	0.71	-19%	656	591	-10%	385	493	28%
FY3/11E	41.1	42.6	4%	0.84	0.77	-8%	588	529	-10%	385	493	28%

Source: Macquarie Research, November 2008

Quarterly results analysis

- **Beat estimates:** 2Q FY3/09 results beat our estimates by 39% at the operating level and 42% at net profit level.

Fig 4 2Q FY3/09 standalone results – actual vs estimated

	2Q FY09A	2Q FY09E	% diff
Net sales	4,961	3,938	26%
EBITDA	1,464	1,050	39%
EBITDA margin	29.5%	26.7%	11%
EBITDA/ tonne of coke (Rs)	9,463	7,832	21%
Depreciation	87	60	45%
Interest	175	110	59%
Other income	27	200	-87%
PBT	1,228	1,080	14%
Tax	125	302	-59%
PAT	1,103	777	42%

Source: Company data, Macquarie Research, November 2008

- **Strong performance in an otherwise weak season:** the second quarter of the fiscal year is considered lean season due to monsoons across large parts of India. Even then, the company has managed to increase its coke production by 139% YoY and 21% sequentially.

Fig 5 2Q FY3/09 standalone profitability presentation

Profitability (Rsm)	2Q FY09A	2Q FY08A	YoY	1Q FY09A	QoQ
Net sales	4,961	1,021	386%	3,776	31%
EBITDA	1,464	175	737%	1,265	16%
EBITDA margin	29.5%	17.1%	72%	33.5%	-12%
EBITDA/ tonne of coke (Rs)	9,463	2,737	246%	7,955	19%
Depreciation	87	60	45%	75	15%
Interest	175	71	147%	97	80%
Other income	27	115	-77%	45	-41%
PBT	1,228	159	672%	1,137	8%
Tax	125	33	278%	193	-35%
PAT	1,103	126	776%	944	17%
EPS - fully diluted (Rs)	2.24	0.26	776%	1.92	17%

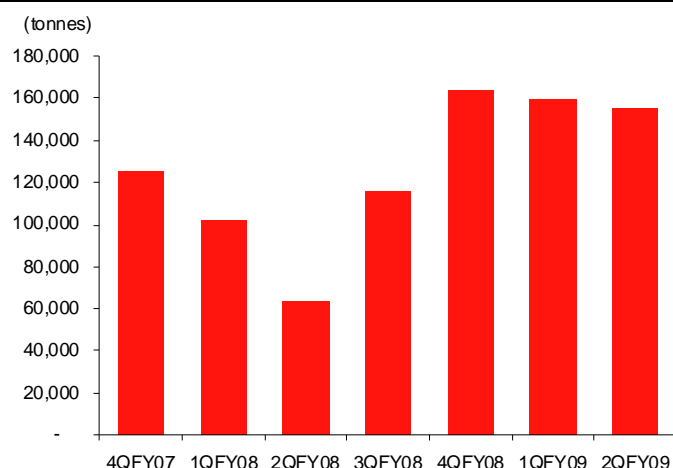
Source: Company data, Macquarie Research, November 2008

Fig 6 2Q FY3/09 volume and realization (standalone)

	2Q FY09A	2Q FY08A	YoY	1Q FY09A	QoQ
Coke production (tonnes)	189,127	79,280	139%	156,489	21%
Coke sales (tonnes)	154,667	63,869	142%	159,000	-3%
Coke realization (US\$/ tonne)	609	242	151%	466	31%

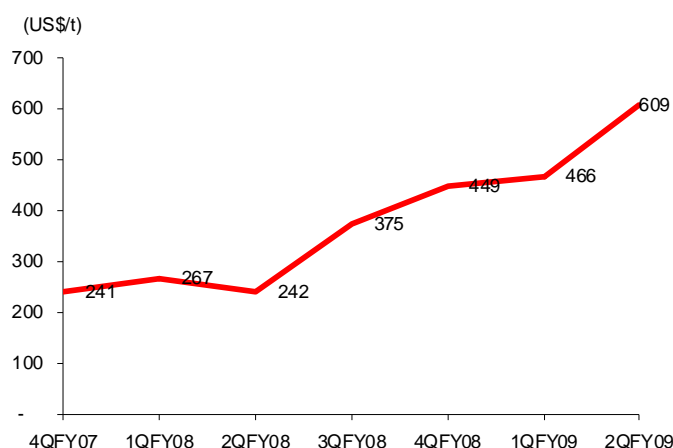
Source: Company data, Macquarie Research, November 2008

Fig 7 Quarterly coke sales volumes



Source: Macquarie Research, November 2008

Fig 8 Quarterly – coke realization



Source: Macquarie Research, November 2008

Fig 9 2Q FY3/09 cost breakup (standalone)

(Rsm)	2Q FY09A	2Q FY08A	YoY	1Q FY09A	QoQ
Change in stocks	(3,252)	(146)	2132%	(374)	771%
Purchases	5,767	789	631%	2,520	129%
Staff	37	22	65%	29	25%
Other expenses	946	181	423%	336	181%
Total cost	3,497	846	313%	2,512	39%

Source: Macquarie Research, November 2008

Key assumptions

Fig 10 Key Macquarie assumptions

(US\$/t)		FY07A	FY08A	FY09E	FY10E	FY11E	FY12E
Hard Coking coal price	USD/t	115	98	300	350	300	275
% change	%	-8%	-15%	206%	17%	-14%	-8%
Coke prices	USD/t	165	340	668	656	588	525
% change	%	2.90%	107%	96%	-2%	-10%	-11%
USD/ INR		44.87	39.97	47.93	49.00	42.63	41.00
AUD/ USD		0.77	0.88	0.78	0.71	0.77	0.81

Source: Company data, Macquarie Research, November 2008

Fig 11 Key assumptions for Indian operations

Indian Operations		FY07A	FY08A	FY09E	FY10E	FY11E	FY12E
Coke sales volume							
GNC (standalone)	tonnes	393,322	440,016	841,520	954,560	1,466,400	1,692,000
BNCL	tonnes		121,900	130,000	146,200	146,200	146,200
Total coke	tonnes	393,322	561,916	971,520	1,100,760	1,612,600	1,838,200
Coke realization	USD/ t	192	278	565	555	498	445
Raw coal consumption	tonnes	552,033	732,832	1,185,254	1,342,927	1,967,372	2,242,604
Raw coal cost	USD/ t	156	104	320	380	340	315

Source: Company data, Macquarie Research, November 2008

Fig 12 Key assumptions for Australian operations

Australian Operations		FY07A	FY08A	FY09E	FY10E	FY11E	FY12E
ROM coking coal production	m tonnes	0.35	0.49	1.10	2.30	3.00	5.00
Coking coal production	m tonnes	0.25	0.34	0.77	1.61	2.10	3.50
ROM coking coal realization	USD/t	50	83	180	215	180	173
Mine Operating cost	AUD/t	55	106	100	101	87	76

Source: Company data, Macquarie Research, November 2008

Gujarat NRE Coke (GNC IN, Outperform, Target price: Rs136.00)

Equifax NRE Book (CNOH, Capex, Fint, Target Price: Rs160.00)											
Profit & Loss		2004A	2005A	2006A	2007A	Profit & Loss		2008A	2009E	2010E	2011E
Revenue	m	2,128	3,281	4,174	5,145	Revenue	m	8,871	34,913	53,027	56,878
Gross Profit	m	0	0	0	0	Gross Profit	m	0	0	0	0
Cost of Goods Sold	m	1,711	2,626	3,357	4,649	Cost of Goods Sold	m	6,819	25,017	34,912	39,467
EBITDA	m	417	655	817	497	EBITDA	m	2,051	9,896	18,115	17,411
Depreciation	m	27	58	91	252	Depreciation	m	459	978	1,191	1,670
Amortisation of Goodwill	m	0	0	0	0	Amortisation of Goodwill	m	0	0	0	0
Other Amortisation	m	0	0	0	0	Other Amortisation	m	0	0	0	0
EBIT	m	390	597	726	245	EBIT	m	1,592	8,918	16,924	15,742
Net Interest Income	m	-16	-63	-125	-273	Net Interest Income	m	-476	-1,303	-1,846	-1,944
Associates	m	0	0	0	0	Associates	m	0	0	0	0
Exceptionals	m	0	777	1,749	0	Exceptionals	m	0	0	0	0
Other Pre-Tax Income	m	358	610	528	633	Forex Gains / Losses	m	0	0	0	0
Pre-Tax Profit	m	732	1,921	2,878	605	Other Pre-Tax Income	m	755	534	412	459
Tax Expense	m	-195	-450	-590	-129	Pre-Tax Profit	m	1,871	8,149	15,491	14,257
Net Profit	m	537	1,471	2,288	476	Tax Expense	m	-598	-3,468	-6,688	-6,908
Minority Interests	m	0	-6	-14	-16	Net Profit	m	1,273	4,681	8,802	7,349
Reported Earnings	m	537	1,471	2,288	476	Minority Interests	m	419	-2	-4	-6
Adjusted Earnings	m	537	700	554	492	Reported Earnings	m	1,273	4,681	8,802	7,349
						Adjusted Earnings	m	1,693	4,678	8,798	7,343
						EPS (rep)		3.61	9.29	17.87	14.92
						EPS (adj)		4.80	9.42	17.86	14.91
						EPS Growth (adj)	%	349.7	96.1	89.5	-16.5
						PE (rep)	x	8.3	3.2	1.7	2.0
						PE (adj)	x	6.2	3.2	1.7	2.0
						Total DPS		2.20	2.00	0.68	1.11
						Total Div Yield	%	7.3	6.7	2.3	3.7
						Weighted Average Shares	m	352	504	493	493
						Period End Shares	m	352	493	493	493
Profit and Loss Ratios						Cashflow Analysis					
		2008A	2009E	2010E	2011E		2008A	2009E	2010E	2011E	
Revenue Growth	%	72.4	293.6	51.9	7.3	EBITDA	m	2,051	9,896	18,115	17,411
EBITDA Growth	%	313.0	382.4	83.1	-3.9	Tax Paid	m	-598	-3,468	-6,688	-6,908
EBIT Growth	%	550.6	460.2	89.8	-7.0	Chgs in Working Cap	m	1,082	-5,887	-3,068	-1,127
Gross Profit Margin	%	0.0	0.0	0.0	0.0	Net Interest Paid	m	-476	-1,303	-1,846	-1,944
EBITDA Margin	%	23.1	28.3	34.2	30.6	Other	m	-459	-978	-1,191	-1,670
EBIT Margin	%	17.9	25.5	31.9	27.7	Operating Cashflow	m	1,600	-1,740	5,322	5,763
Net Profit Margin	%	14.4	13.4	16.6	12.9	Acquisitions	m	-1,938	0	0	0
Payout Ratio	%	45.8	21.3	3.8	7.4	Capex	m	-15,617	-4,265	-3,536	-12,996
EV/EBITDA	x	4.3	1.3	0.7	0.8	Asset Sales	m	0	0	0	0
EV/EBIT	x	5.6	1.5	0.8	0.8	Other	m	0	534	412	459
Balance Sheet Ratios						Investing Cashflow	m	-17,555	-3,731	-3,123	-12,536
ROE	%	16.6	23.1	29.8	19.9	Dividend (Ordinary)	m	-501	-947	-333	-546
ROA	%	6.2	17.8	22.4	17.7	Equity Raised	m	6,805	1,556	1,556	0
ROIC	%	12.8	22.9	37.5	25.8	Debt Movements	m	4,385	3,175	2,532	-1,298
Net Debt/Equity	%	32.1	-6.3	-11.6	4.7	Other	m	-1,836	5,550	-268	-199
Interest Cover	x	3.3	6.8	9.2	8.1	Financing Cashflow	m	8,853	9,334	3,488	-2,043
Price/Book	x	0.7	0.6	0.4	0.4	Net Chg in Cash/Debt	m	-7,102	3,863	5,687	-8,817
Book Value per Share		42.7	51.6	68.3	81.7						
						Balance Sheet					
		2008A	2009E	2010E	2011E		2008A	2009E	2010E	2011E	
						Cash	m	2,401	12,731	17,685	10,264
						Receivables	m	2,538	8,239	9,885	11,407
						Inventories	m	2,620	10,566	15,487	17,193
						Investments	m	0	0	0	0
						Fixed Assets	m	15,130	16,981	19,326	30,652
						Intangibles	m	0	0	0	0
						Other Assets	m	10,448	18,542	21,697	23,836
						Total Assets	m	33,136	67,059	84,080	93,351
						Payables	m	3,784	16,931	22,096	25,319
						Short Term Debt	m	0	0	0	0
						Long Term Debt	m	7,843	11,018	13,550	12,252
						Provisions	m	2,567	5,274	6,764	7,780
						Other Liabilities	m	1,996	6,471	6,103	5,829
						Total Liabilities	m	16,190	39,694	48,513	51,181
						Shareholders' Funds	m	15,025	25,442	33,639	40,237
						Minority Interests	m	1,921	1,923	1,928	1,933
						Other	m	0	0	0	0
						Total S/H Equity	m	16,946	27,365	35,567	42,171
						Total Liab & S/H Funds	m	33,136	67,059	84,080	93,351

All figures in INR unless noted.

Source: Company data, Macquarie Research, November 2008

Important disclosures:

Recommendation definitions

Macquarie - Australia/New Zealand

Outperform – return >5% in excess of benchmark return (>2.5% in excess for listed property trusts)
 Neutral – return within 5% of benchmark return (within 2.5% for listed property trusts)
 Underperform – return >5% below benchmark return (>2.5% below for listed property trusts)

Macquarie – Asia/Europe

Outperform – expected return >+10%
 Neutral – expected return from -10% to +10%
 Underperform – expected return <-10%

Macquarie First South - South Africa

Outperform – expected return >+10%
 Neutral – expected return from -10% to +10%
 Underperform – expected return <-10%

Macquarie – Canada

Outperform – return >5% in excess of benchmark return
 Neutral – return within 5% of benchmark return
 Underperform – return >5% below benchmark return

Macquarie – USA

Outperform (Buy) – return >5% in excess of benchmark return
 Neutral (Hold) – return within 5% of benchmark return
 Underperform (Sell) – return >5% below benchmark return

Recommendations – 12 months

Note: Quant recommendations may differ from Fundamental Analyst recommendations

Volatility index definition*

This is calculated from the volatility of historic price movements.

Very high–highest risk – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.

High – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.

Medium – stock should be expected to move up or down at least 30–40% in a year.

Low–medium – stock should be expected to move up or down at least 25–30% in a year.

Low – stock should be expected to move up or down at least 15–25% in a year.

* Applicable to Australian/NZ stocks only

Financial definitions

All "Adjusted" data items have had the following adjustments made:
 Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives & hedging, IFRS impairments & IFRS interest expense
 Excluded: non recurring items, asset revals, property revals, appraisal value uplift, preference dividends & minority interests

EPS = adjusted net profit / *efpowa**

ROA = adjusted ebit / average total assets

ROA Banks/Insurance = adjusted net profit / average total assets

ROE = adjusted net profit / average shareholders funds

Gross cashflow = adjusted net profit + depreciation

*equivalent fully paid ordinary weighted average number of shares

All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).

Recommendation proportions – For quarter ending 30 September 2008

	AU/NZ	Asia	RSA	USA	CA	EUR
Outperform	43.17%	61.57%	63.08%	53.60%	71.54%	43.00%
Neutral	41.37%	16.43%	30.77%	37.60%	24.61%	48.00%
Underperform	15.47%	22.00%	6.15%	8.80%	3.85%	9.00%

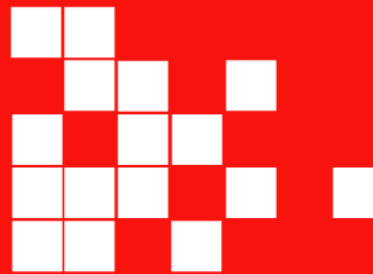
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