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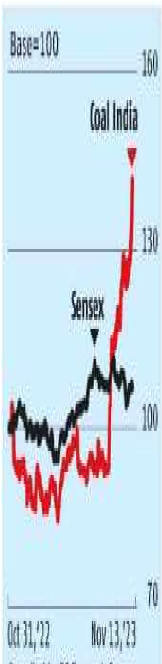
THE COMPASS

Coal India's robust outlook ignites stock to new heights



Compiled by BS Research Bureau

DEVANGSHU DATTA

Coal India's (CIL's) second-quarter (Q2) 2023-24 (FY24) revenue increased by 10 per cent year-on-year (Y-o-Y) to ₹32,800 crore, driven by higher volumes and fuel supply agreement (FSA) realisation.

The blended average selling price (ASP) was down 3 per cent Y-o-Y at ₹1,726 per tonne, but the FSA ASP was up 9 per cent Y-o-Y at ₹1,542 per tonne, while the e-auction ASP declined by 53 per cent Y-o-Y to ₹2,828 per tonne.

Although the e-auction premium cooled off, it is still above its historical average at around 83 per cent, and it is expected to stay between 80 per cent and 85 per cent for FY24.

The adjusted operating profit increased by 11 per cent Y-o-Y to ₹8,900 crore, owing to lower-than-expected employee costs, lower contractual expenses, and input costs.

The adjusted operating profit excludes overburden removal, and the adjusted net profit rose by 13 per cent Y-o-Y to ₹6,800 crore. This was driven by a strong operating performance and lower depreciation. The first interim dividend was ₹15.25 per share on the face value of ₹10 for FY24.

The agreement for salaries and wages for non-executive employees was implemented in June, and employee costs from June onwards are being paid at revised rates. The wage outgo should stabilise at ₹12,000 crore a quarter.

The strong cash position of ₹37,100 crore supports higher other income. The company could generate ₹25,000 crore in cash in FY24 against capital expenditure (capex) needs of ₹16,500 crore in FY24.

Coal production rose by 13 per cent Y-o-Y to 157 million tonne (mt), and sales dispatches grew by 12 per cent Y-o-Y to 174 mt. Dispatches rose by an incremental 28 mt in the first half (H1) of FY24, and dispatches to the power sector increased to 295 mt in H1FY24.

Dispatches to the non-power sector were at 65.7 mt (up 40 per cent Y-o-Y). Overall H1 sales volume was up by 9.5 per cent.

Power demand usually reaches its peak in May due to summer heatwave, but drier monsoons and high economic activity kept demand elevated in Q2FY24. Power demand surpassed the Central Electricity Authority target, with peak demand rising past 240 gigawatt in Q2FY24, driving demand for thermal coal.

CIL maintains its FY24 target for dispatch to the power sector at 610 mt. The Ministry of Power has set the FY24 electricity generation target at 1,750 billion units (up 7.2 per cent Y-o-Y), and the thermal power share is to be over 75 per cent, implying sustained elevated demand for CIL.

The company has begun a fresh round of coal auctions under the Scheme for Harnessing and Allocating Koyala Transparently in India (SHAKTI) B (viii-a) for private power producers who do not have a power purchase agreement. In a first, the coal put on sale is marked for lifting in three months against six months earlier. This comprises 13.09 mt to be auctioned in October-November.

CIL estimates a capex of ₹80,000 crore over the next five years while targeting production of 1 billion tonne per annum. It has current estimates of approximately 780 mt in FY24, and it should hit 935 mt by 2025-26.

The Street beat in Q2 and improved outlook on volume, sustainable e-auction premiums, and stabilised wage costs have made the market happy, with the stock climbing by over 5 per cent to ₹350. Several analysts see an upside to around ₹375-plus.

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RATING: BUY

CIL: Stellar Q2 show, outlook positive

Improved performance through upward trends in e-auction prices & volume

COAL INDIA LTD (CIL) exceeded expectations in Q2FY24 with an EPS of ₹11.9/share, surpassing both our and consensus estimates by 35% and 25%, respectively. Key points include:

Volume growth: Positive volume trends were observed across all categories, offsetting the adverse effects of lower e-auction realization.

Wage cost management: Wage costs, totaling ₹116.4 billion, remained at normalized levels and were within our projected estimates.

Provision adjustment: A significant unwinding of the ₹81.5 billion provision made in FY23 for wage hikes was noted in Q2FY24. This resulted in a reduction of the cash and bank balance to ₹370 billion.

Dividend declaration: The Board has proposed the issuance of the first interim dividend at 115.25/share.

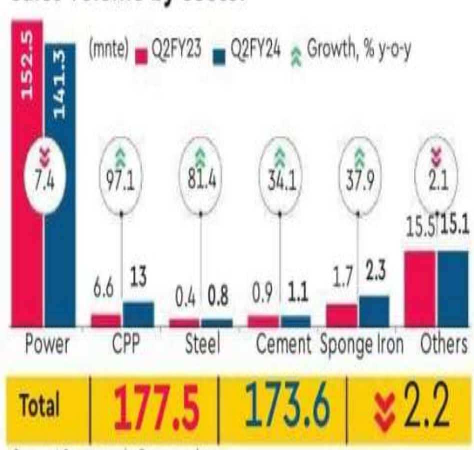
Looking forward, we anticipate continued improvement in CIL's performance, with potential consensus EPS upgrades in the range of 25-30%. We maintain our FY24E/FY25E EPS projections. Our recommendation is to Buy. The TP remains unchanged at ₹395, based on 8x FY25E EPS.

CIL achieved its best-ever Q2 performance driven by increased volumes and higher FSA prices. Key highlights include: (i) FSA prices rose by 9.1% y-o-y to ₹1,542 due to heightened supply to the non-regulated sector (NRS), with NRS offtake increasing by 29.3% y-o-y to 32.3 million tonnes; (ii) e-auction prices fell by 53.2% y-o-y to ₹2,838, partially offset by a 52.6% y-o-y increase in e-auction volume to 15.8 million tonnes; (iii) e-auction premium to FSA price declined to 84%, compared to 329% a year ago; (iv) FSA volume grew by 9.2% y-o-y to 154.7 million tonnes, surpassing power sector requirements in H1FY24; (v) cash & bank balance was impacted by arrear payments, reducing provisions by ₹71 billion; and (vi) the Board recommended an interim dividend of ₹15.25/share, implying a 4.7% yield at the current market price. Looking forward, CIL's performance is expected to further improve, supported by an anticipated uptick in both e-auction prices and volumes.

CIL's Q2FY24 performance challenges the misconception that e-auction prices alone determine profitability. Contrary to this belief, we assert that volume, encompassing both FSA and e-auction, significantly influences CIL's earnings. Despite a substantial drop in e-auction prices by 53% y-o-y and a decline in e-auction premium, Q2FY24 Ebitda still registers an 11.8% y-o-y increase. We see an upside risk to our already leading EPS estimates if the strong performance persists through Oct'23.

I-SEC RESEARCH

Sales volume by sector



Source: I-Sec research, Company data