

30th December 2008**BUY**

Price	Target Price
Rs253	Rs301

Sensex – 9,534

Price Performance

(%)	1M	3M	6M	12M
Absolute	7	(43)	(64)	(76)
Rel. to Sensex	2	(22)	(49)	(49)

Source: Bloomberg

Stock Details

Sector	Metals & Mining
Reuters	STRL.BO
Bloomberg	STLT@IN
Equity Capital (Rs mn)	1417
Face Value (Rs)	2
Number of shares o/s (mn)	708
52 Week H/L (Rs)	1,085/165
Market Cap (Rs bn/USDmn)	179/3,679
Daily Avg Vol (No of shares)	4369356
Daily Avg Turnover (US\$ mn)	24.2

Shareholding Pattern (%)

	30/9/08	30/6/08	31/3/08
Promoters	60.6	62.5	62.5
FII/NRI	21.5	24.6	23.5
Institutions	7.3	5.7	6.4
Private Corp.	3.7	1.6	1.9
Public	6.9	5.6	5.7

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Sailing in turbulent waters

We met the management of Sterlite Industries Ltd (SIL). The management does not expect any significant recovery in metals demand and prices for next 6-9 months. As per the management, the current demand destruction is not being offset by the supply cut to the same extent and hence, base metals are expected to remain in surplus till FY10E. This is expected to keep metal prices under pressure. However, SIL's low cost of production will enable it to maintain its margins. The current LME prices of base metals are ruling below marginal cost of production and the management expects the prices to remain at the current levels for next few quarters. Despite the current slowdown, SIL's expansion plans are on track and the management expects the plants to be operational within time and budget. The 2,400MW IPP under Sterlite Energy is progressing as per schedule. However, the management has said that out of total 2,400MW, only 600MW will be used for commercial purpose and balance will be used captively for Aluminum smelters for the period from Mar '10 to Jun '11 as against the previous plan to operate entire 2,400MW on commercial basis. Currently, SIL has net cash of Rs120bn on consolidated basis. At the CMP of Rs253, the stock is trading at 5.3x FY09E FDEPS of Rs47.9 and at 5.9x FY10E FDEPS of Rs42.5. On EV/EBITDA basis the stock is trading at 2.1x FY09E EV/EBITDA and at 2.5x FY10E EV/EBITDA; while on P/B basis the stock is trading at 0.6x FY09E book value and at 0.5x FY10E book value. We maintain BUY on the stock, with target price of Rs301.

The key takeaways from the meeting are as under:-

- As per the management, there have not been significant production cuts across base metals to offset the current demand destruction and hence, base metals are expected to remain in surplus. In CY08, copper is expected to turn into surplus of 0.1mtpa from deficit of around 54,000t in CY07, while zinc and aluminum are expected to be in surplus of more than 150,000t. This is expected to keep metal prices under pressure and the management does not expect any significant recoveries in base metal demand and prices for atleast next 6-9 months.
 - The current LME prices of zinc and aluminium are trading below the average cost of production. The average cost of production (COP) for aluminium is USD1,800/t and the marginal cost is USD2,600/t, while the LME price is USD1,504/t and average COP of zinc is USD1,600/t and marginal COP is USD1,800/t, while LME price is USD1,127/t. The management expects the prices to remain at current levels for the next few quarters.
 - SIL is the lowest cost producer. The COP of zinc is around USD650/t and for aluminium is USD1,500-1,600/t.
 - SIL is currently renegotiating ASARCO deal and expects some development in next 1-2 months.
 - SIL currently has a net cash of Rs120bn on a consolidated basis, which is equivalent to Rs169/share.
- Copper**
- The company realized ¢12/lb of TC/RC for 2QFY09. The management expects TC/RC to remain subdued.

Zinc

- The expansion project of increasing zinc and lead smelting capacities to 1.065mtpa along with matching expansion of mining output is progressing as per schedule and the management expects the plant to be operational by Jun '10.
- The total estimated capex of Rs33bn will be funded through internal accruals. The company plans to invest 30% of capex in FY09, 60% in FY10 and balance in FY11. SIL has already incurred capex of USD90mn
- The current average realization for sulphuric acid is USD30/t (a decline of 82% from the peak)

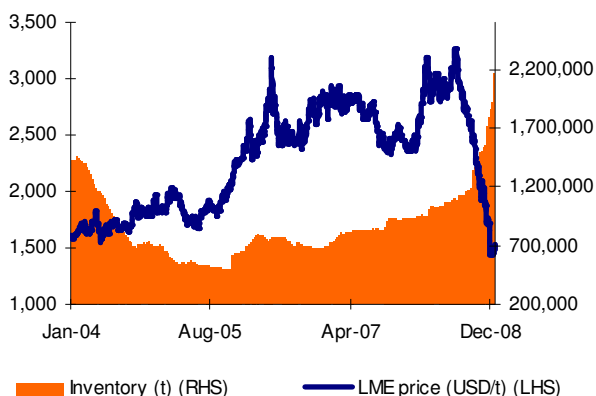
Aluminum

- The capacity expansion program to increase aluminum smelting capacity to 2.6mtpa is progressing as per schedule.
- The total estimated capex of USD6.5bn will be funded through a mix of debt and internal accruals
- The company has received Supreme Court approval for Nyamgiri bauxite mines and expects the mines to start operations by Apr '09, wherein it will start transporting bauxite through road transport and subsequently to start transporting bauxite through conveyors from Oct-Nov '09.
- 2,400MW IPP under Sterlite Energy is progressing as per schedule and the company expects phase-I of 600MW to be operational by 4QFY09. However, out of total 2,400MW, only 600MW will be used for commercial purpose and balance will be used captively for aluminium smelters for the period from Mar '10 to Jun '11. VAL has deferred the 1,980MW power plant at Jharsuguda, which will lead to savings of USD2bn of capital expenditure.

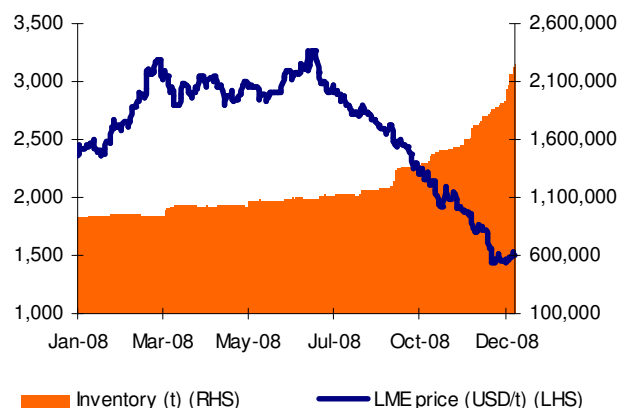
Valuation

At the CMP of Rs253, the stock is trading at 5.3x FY09E FDEPS of Rs47.9 and at 5.9x FY10E FDEPS of Rs42.5. On EV/EBITDA basis, the stock is trading at 2.1x FY09E EV/EBITDA and at 2.5x FY10E EV/EBITDA; while on P/B basis, the stock is trading at 0.6x FY09E book value and at 0.5x FY10E book value. We believe that SIL's low cost of production will enable it to maintain margins in the current slowdown and the ambitious capex program will provide the volume growth. We maintain BUY on the stock with target price of Rs301.

Aluminium prices at LME for last 5 years

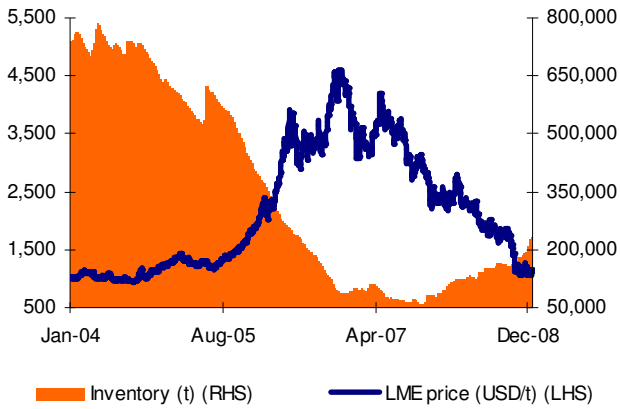


Aluminium prices at LME for last 1 year

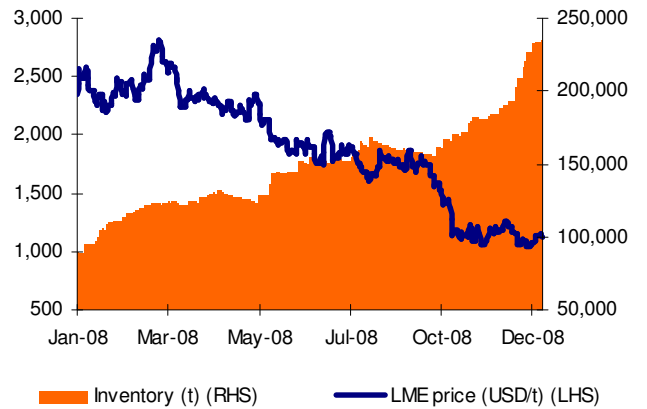


Source: Bloomberg

Zinc prices at LME for last 5 years

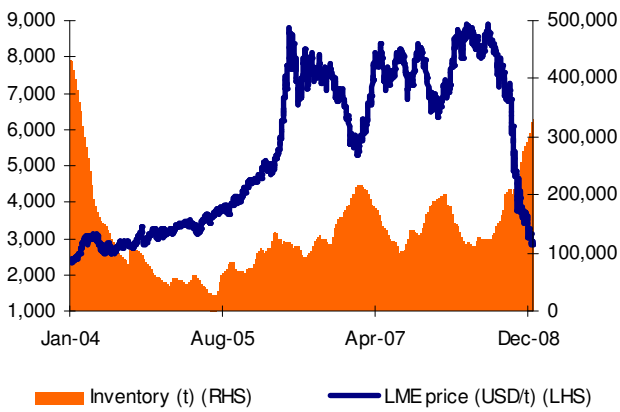


Zinc prices at LME for last 1 year

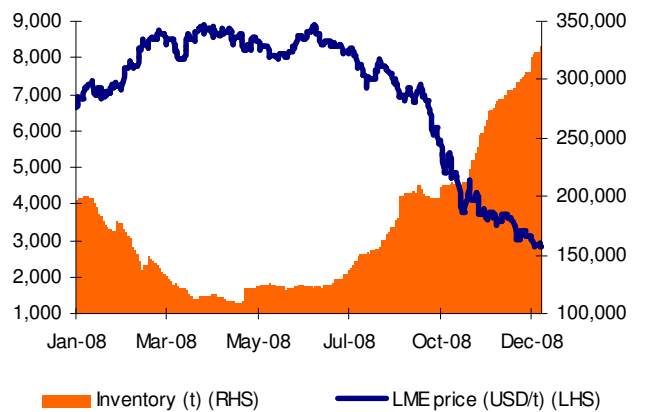


Source: Bloomberg

Copper prices at LME for last 5 years



Copper prices at LME for last 1 year



Source: Bloomberg

Consolidated Financials

Income Statement	Rs Mn			
	FY07	FY08	FY09E	FY10E
Gross Sales	261,930	268,723	235,350	198,297
Less: Excise	18,062	21,669	15,811	13,500
Net Sales	243,868	247,054	219,538	184,797
Other Income	6,817	15,661	19,605	20,176
Total Income	250,685	262,715	239,144	204,973
Raw Material Cons	137,152	153,545	154,012	129,750
% of Sales	56.2%	62.2%	70.2%	70.2%
Staff Cost	5,495	6,592	7,188	7,010
Other Expenses	6,632	8,234	7,051	7,610
Total Exp	149,280	168,371	168,252	144,371
EBIDTA	101,406	94,343	70,892	60,602
EBIDTA margin	41.6%	38.2%	32.3%	32.8%
Depreciation	8,039	5,950	7,566	8,997
EBIT	93,367	88,393	63,326	51,605
Interest	3,791	3,186	2,907	2,311
Extra ordinary exp.	1,572	528	0	0
PBT	88,004	84,679	60,419	49,294
Tax	24,733	21,027	11,773	9,489
ETR (%)	28.1%	24.8%	19.5%	19.2%
Minority Interest	19,042	19,500	14,680	9,695
Pref Div	1	0	0	0
Adj. PAT	44,229	44,152	33,967	30,111

Cash Flow Statement	Rs Mn			
	FY07	FY08	FY09E	FY09E
Pre-tax profit	88,004	84,679	60,419	49,294
Depreciation	8,039	5,950	7,566	8,997
Net Chg in WC	-38,142	-20,854	10,379	-4,644
Others	101	542	0	0
CFO	58,002	70,317	78,364	53,647
Capex	-19,718	-33,141	949	-42,388
Net Inv made	0	0	-76,800	-9,600
Others Inv Activities	-27,268	-110,721	34,969	0
CFI	-46,985	-143,863	-40,882	-51,988
Change in Sh cap	-1,441	80,620	0	0
Change in Debts	-5,499	5,117	45,722	14,161
Div. & Div Tax	-4,451	-387	-5,802	-6,631
Others	356	1,597	0	0
CFF	-11,035	86,947	39,920	7,530
Net Change in Cash	-18	13,401	77,402	9,189
Cash Op Bal	11,153	11,134	24,536	101,938
Cash Cl Bal	11,134	24,536	101,938	111,127

Balance Sheet	Rs Mn			
	FY07	FY08	FY09E	FY10E
Equity Capital	1,117	1,417	1,417	1,417
Res & Surplus (incl MI)	134,959	277,842	320,686	353,861
Networth	136,076	279,259	322,103	355,278
Total Debts	46,103	50,745	96,467	110,628
Net deferred lib	12,729	20,415	21,356	21,678
Capital Employed	194,909	350,420	439,927	487,583
Gross Block	126,414	145,637	151,239	171,739
Less Depreciation	-43,235	-45,883	-53,450	-62,446
CWIP	13,997	24,613	18,063	39,950
Net Fixed Assets	83,179	99,754	97,789	109,293
Inv & Associates	2,967	18,925	95,725	105,325
Inventory	28,092	33,341	29,160	26,522
Debtors	16,521	15,623	15,177	13,777
Cash	11,134	24,536	101,938	111,127
Mktable Sec.	49,252	144,016	109,047	109,047
Loans & Advances	34,846	33,135	19,798	16,876
Total Curr. Assets	139,846	250,650	275,119	277,349
Current Liabilities	21,399	19,941	23,188	20,752
Provisions	23,681	23,581	23,581	23,581
Total Curr. Liabi. & Prov.	45,081	43,522	46,769	44,333
Net Current Assets	94,766	207,128	228,350	233,016
Total Assets	194,909	350,420	439,927	487,583

Ratios				
	FY07	FY08	FY09E	FY10E
EBIDTA margin %	41.6	38.2	32.3	32.8
EBIT margin %	38.3	35.8	28.8	27.9
NPM %	18.1	17.9	15.5	16.3
Adj ROCE (%)	38.9	24.1	12.8	8.9
Adj ROE (%)	42.9	21.5	11.3	8.9
ROIC (%)	66.2	59.7	33.1	19.0
Adj EPS	79.2	62.3	47.9	42.5
Cash EPS	96.4	71.5	58.6	55.2
Book Value	243.6	394.2	454.6	501.5
DPS	5.8	4.0	7.0	8.0
Payout Ratio (%)	7.3	6.4	14.6	18.8
Debt Equity (x)	0.3	0.1	0.0	0.0
PE (x)	3.1	4.0	5.3	5.9
P/BV (x)	1.0	0.6	0.6	0.5
EV/Sales (x)	0.7	0.5	0.7	0.8
EV/EBITDA (x)	1.6	1.4	2.1	2.5
Div Yield (%)	2.3	1.6	2.8	3.2

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