THE COMPASS

Higher prices, demerger to boost margins, unlock value for Vedanta

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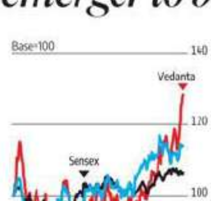
Vedanta, a conglomerate in mining and metals, has seen a surge in its share price on the back of multiple triggers. Its demerger appears to be on track, a strong non-ferrous commodity cycle is boosting margins, and silver bulls are interested in Hindustan Zinc, its subsidiary.

Aluminium and zinc are up 7 per cent and 13 per cent, respectively, on a quarter-on-quarter (Q-o-Q) basis for October-December.

Aluminium is expected to remain deficit next year as well and supply constraints could sustain higher silver prices in 2026. Hindustan Zinc will benefit from rising silver prices (up 32 per cent Q-o-Q), given that it is India's largest silver producer with 800 tonnes of refining capacity.



Vedanta is expanding with the commissioning of a smelting unit (at Balco) with a capacity of 435 kilo tonnes per annum (ktpa). Debottlenecking at Jharsuguda will lift its smelting capacity to 3.1 million tonnes per annum, or mtpa, by FY28. The commissioning of the 1.5 mtpa Lanjigarh alumina refinery is part of a targeted expansion of alumina capacity to 6 mtpa, backed by bauxite and coal mines. A focus on value-added products is expected to drive premium realisations. Aluminium revenue at Vedanta is expected to grow at 12 per cent annually over FY25-27, with operating profit/tonne rising to $1,283 by FY27 (vs $870 in FY25).

A generation of good cash flow, or CFO, at over ₹30,000 crore since FY22 has enabled deleveraging, with net debt/operating profit improving to 1.37 times as of September 2025 and targeted at making them equal by FY27. Despite high dividend payouts, robust free cash-flow generation is expected to sustain a dividend yield of 6 per cent in future. An operating profit of Vedanta could rise annually at 25 per cent over FY25-27.

Approval by the National Company Law Tribunal for demerger paves the way for creating five listed companies, subject to getting other clearances. Given separate capital structures and deleveraging, the demerger could unlock value. The approvals for demerger are still pending (next hearing on January 7) and next steps include asset/liability transfers including mining leases, power-purchase agreements and production-sharing contracts for oil/gas and furnishing corporate guarantees. Vedanta hopes to complete the demerger by March.

Hindustan Zinc contributes 40 per cent to Vedanta's consolidated operating profit. The management reiterated its medium-term visibility on earnings, supported by a secure mine life, high structural-entry barriers, and renewables-led cost cuts. The company is confident of retaining mines in the CY30 re-auction.

Management highlighted high entry barriers, supporting a high probability of mine retention, albeit at moderately higher royalty. The energy-mix transition is a key cost lever, with the use of renewables to increase from 7 per cent in FY25 to 55 per cent in FY27 and to 70 per cent by FY28. Each 2 per cent increase in the share of renewables yields $1/tonne in cost savings.

The FY27 management guidance for zinc output is at least 1,080 kilo tonnes and for silver production 700 tonnes at very competitive global costs. Minimal hedging for FY27 reflects the management's belief about structural silver tightness. Silver hedging is limited to 123 tonnes (34 per cent of H2FY26) at $37/ounce, while FY27 hedging is minimal. Operating profit could have a considerable upside over consensus expectations of ₹22,000 crore since spot prices indicate operating profits of ₹25,800 crore. Each $1/ounce move in silver prices changes Hindustan Zinc's operating profit by 1 per cent.

Vedanta reported consolidated revenues of ₹39,900 crore, up 6 per cent Y-o-Y and up 5 per cent Q-o-Q, driven by higher London Metal Exchange prices, improved premiums, and forex gains in Q2FY26. Consolidated operating profits stood at ₹11,400 crore, up 16 per cent Y-o-Y and up 15 per cent Q-o-Q. The operating profit margin for Q2FY26 stood at 28.6 per cent compared to 26.2 per cent in Q1FY26 and 26.1 per cent in 2QFY25. Adjusted net profits stood at ₹3,350 crore, up 13 per cent Y-o-Y and up 5 per cent Q-o-Q.

The company has maintained its capex guidance at $1.7 billion-$1.9 billion for FY26, with $0.9 billion already invested in H1. Analyst consensus is positive and the stock has hit new highs.