



JSW Steel

STOCK INFO. BLOOMBERG
BSE Sensex: 15,062 JSTL IN
REUTERS CODE
S&P CNX: 4,469 JSTL.BO

21 July 2009

Buy

Rs606

Previous Recommendation: Buy

Equity Shares (m) 187.1
52-Week Range 882/161
1,6,12 Rel. Perf. (%) -3/130/-24
M.Cap. (Rs b) 113.4
M.Cap. (US\$ b) 2.3

YEAR	NET SALES	PAT	EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/
END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
3/08A	123,455	15,367	82.2	9.2	7.4	1.5	20.2	11.5	1.9	7.2
3/09A	164,558	9,729	52.0	-36.7	11.7	1.4	12.0	8.9	1.7	8.1
3/10E	167,853	12,624	67.5	29.7	9.0	1.4	15.2	11.0	1.7	6.4
3/11E	191,328	13,379	71.5	6.0	8.5	1.2	14.0	10.3	1.7	6.4

Consolidated (SISCOL numbers are consolidated for FY09 onwards)

- Standalone adjusted PAT declined 54% YoY to Rs1.7b. Reported PAT of Rs3.4b included Rs2.4b on account of forex gain. US operations contributed loss of US\$14m at EBITDA level and US\$32m at PBT level due to inventory losses. Consolidated PAT was Rs2.3b.
- Net sales increased 18% QoQ to Rs39b. Sales volume increased 24% QoQ to 1.32m tons and blended realization declined 5% QoQ to Rs29,650/ton. Share of domestic sales increased 24pp YoY to 86%.
- EBITDA increased 84% QoQ to Rs7.5b (v/s our estimate of Rs8b) and margins improved ~7pp QoQ to 19% due to reduction in other expenditure. However, EBITDA/tss of Rs5,652/ton (US\$118/ton) was lower than our estimate of Rs6,189/ton due to higher than expected raw material cost. The full benefits of lower coking coal costs are yet to kick in despite earlier guidance of no stocks of high-cost coal. Also, JSW Steel sourced 13% of its coke requirement from third parties v/s its guidance of full self sufficiency in coke capacities.
- We believe JSW Steel is on track to achieve strong volume growth in FY10 and margins are likely to improve in subsequent quarters due to reduction in coking coal costs. However, there could be some increase in iron ore costs due to rise of spot prices. We cut our FY10E EPS to Rs67.5 (earlier Rs74.5) due to lower than expected numbers for 1QFY10 and downward revision of estimates for US operations. The stock trades at an EV of 6.4x FY10E EBITDA. Maintain **Buy** with a target price of Rs635 (6.5x FY10E EV/EBITDA).

QUARTERLY PERFORMANCE (STAND-ALONE)

(RS MILLION)

Y/E MARCH	FY09				FY10				FY09	FY10E
STANDALONE	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE		
Sales ('000 tons)	817	837	711	1,062	1,321	1,400	1,500	1,600	3,427	5,821
Change (YoY %)	13.2	3.7	-18.0	5.2	61.7	67.3	111.0	50.7	0.6	69.9
Realization (Rs per ton)	44,938	51,006	39,178	31,345	29,650	27,911	27,883	28,266	41,012	28,396
Change (YoY %)	36.0	52.8	21.2	-11.3	-34.0	-45.3	-28.8	-9.8	22.0	-30.8
Net Sales	36,714	42,692	27,855	33,288	39,168	39,075	41,825	45,225	140,549	165,293
Change (YoY %)	53.9	58.5	-0.6	-6.7	6.7	-8.5	50.2	35.9	22.7	17.6
Total Expenditure	28,121	31,789	23,941	29,227	31,701	27,704	29,872	31,627	113,077	120,904
EBITDA	8,593	10,904	3,915	4,061	7,467	11,371	11,953	13,598	27,472	44,389
Change (YoY %)	11.0	25.8	-50.8	-49.9	-13.1	4.3	205.3	234.8	-15.4	61.6
As % of Net Sales	23.4	25.5	14.1	12.2	19.1	29.1	28.6	30.1	19.5	26.9
EBITDA (Rs per ton)	10,518	13,027	5,506	3,824	5,652	8,122	7,969	8,499	8,016	7,626
Interest	1,531	1,960	2,333	2,149	2,206	2,317	2,548	2,803	7,973	9,875
Depreciation	1,852	1,975	2,141	2,309	2,718	2,854	2,997	3,146	8,277	11,715
Other Income	273	426	420	973	54	325	375	275	2,092	1,029
PBT (before EO Item)	5,483	7,394	-139	577	2,597	6,525	6,783	7,924	13,315	23,828
EO Items	-2,266	-2,684	-1,768	178	2,360	0	0	0	-6,540	2,360
PBT (after EO Item)	3,217	4,711	-1,907	755	4,957	6,525	6,783	7,924	6,775	26,188
Total Tax	1,024	1,536	-632	263	1,556	2,088	2,171	2,536	2,191	8,351
% Tax	31.8	32.6	33.1	34.9	31.0	32.0	32.0	32.0	32.3	31.9
Reported PAT	2,193	3,175	-1,275	492	3,400	4,437	4,612	5,388	4,584	17,838
Preference Dividend	72	72	72	72	72	72	72	72	289	289
Adjusted PAT	3,665	4,911	-165	304	1,696	4,373	4,548	5,325	8,720	15,941
Change (YoY %)	-4.0	3.6	-104.9	-92.6	-53.7	-11.0	N.A	1,653.8	-45.6	82.8

E: MOSL Estimates

US operations: inventory losses coupled with lack of orders

- ✂ Consolidated EBITDA of Rs6.9b was 8% lower than standalone EBITDA due to losses in foreign subsidiaries.
- ✂ Plate mill continues to operate at below ~11% capacity utilization, while pipe mill capacity utilization has dropped to 5% and is expected to shut down due to lack of orders.
- ✂ US operations contributed loss of US\$14m at the EBITDA level and US\$32m at the PBT level due to inventory losses. Consolidated PAT was Rs2.3b.

US PIPE & PLATE MILL (US\$M)

Y/E MARCH	FY09				FY10 1Q
	1Q	2Q	3Q	4Q	
Operational Performance					
Plate Mill					
Production (tons)	143,077	109,066	47,487	44,061	27,727
Sales (tons)	75,762	59,629	27,660	26,986	14,376
Pipe Mill					
Production (tons)	66,431	34,931	27,198	9,065	5,432
Sales (tons)	65,026	35,927	28,550	9,942	4,308
Capacity Utilization (%)					
Plates	57.9	44.9	19.2	18.2	11.4
Pipes	48.3	25.5	19.8	6.6	4.0
Financials (US Operations)					
Revenues	218	165	88	30	18
EBITDA (incl. oth inc)	45	30	15	-19	-14
PBT	26	11	-5	-97	-32
PAT	18	10	-3	-61	-21

Source: Company/MOSL

CONSOLIDATED QUARTERLY PERFORMANCE (RS M)

Y/E MARCH	FY09				FY10 1Q	FY08	FY09	FY10E
	1Q	2Q	3Q	4Q				
Net Sales	44,562	46,414	32,689	36,221	40,138	123,455	164,558	167,853
EBITDA	10,425	11,568	4,544	2,360	6,884	32,202	33,912	44,768
Interest	2,348	2,788	3,302	3,119	2,983	5,730	9,879	12,719
Depreciation	2,199	2,369	2,588	2,722	3,166	7,419	10,468	14,040
Other Income	276	454	511	973	2,397	3,723	2,092	1,029
Reported PAT	2,502	2,524	-1,878	-399	2,341	15,367	9,729	12,624

E: MOSL

3.5mtpa HSM, 10mtpa iron ore beneficiation plant delayed by three months to March 2010

- ✂ 3.5mtpa hot strip mill, 10mtpa iron ore beneficiation plant and blooming mill are expected to be commissioned with a delay of three months in March 2010.
- ✂ Also, the expansion to 11mtpa has been re-started and the site has been mobilized. The expansion is expected to be completed by March 2011.
- ✂ Capex would be Rs29b for FY10 and Rs68b for FY11. Though the overall debt is unlikely to go up in FY10 from Rs162b currently, FY11 debt will rise by Rs40b.

Favorable high court ruling for 60m ton iron ore mine at Hadimpada

JSW Steel has got a favorable ruling from the High Court on the 60m ton iron ore deposit in Hadimpada, Karnataka. JSW owns the mining lease to the Hadimpada deposit, which has Fe grades of 63-64% and plans to start mining operations by October, 2009. However, the counter party may go to Supreme Court against the ruling which may delay extraction plans of the company. JSW Steel currently meets just about ~20% of its iron ore requirements from its captive mines and sources the balance through linkages and spot purchase. A favorable judgment by the Supreme Court will lead to significant cost savings to the company and insulation from volatile iron ore prices.

IRON ORE RESOURCES

STATE	LOCATION	OUTPUT (MTPA)	STATUS
Karnataka	VMPL	1.5	Operational, right to mine with JV
	Hadimmapade	2.0	60m ton of 63-64% Fe grade
	Donimalai	3.0	Recommended to JSWSL, VMPL, SWML
Tamil Nadu	Kanjamalai	1.0	Allotted to TIMCO; JV of JSW
	Kavuthimalai	1.0	Recommended to TIMCO
Jharkhand	Ankua	8.0	PL to JSW Steel Jharkhand project
Overseas	Chile	20	Project deferred
NMDC (LTA)		2.5	
Total		39.0	

Source: Company/MOSL

On track to achieve volume targets, margins to expand; maintain Buy

- ✂ Crude steel production of ~500,000 tons in the month of June 2009 indicates an impressive ramp-up to achieve the FY10 target of 5.8m tons due to stronger domestic demand. The product mix will change in favor of long products from 8% share in FY09 to 24% in FY10 due to addition of the new bar and wire rod mill.
- ✂ We believe JSW Steel is on track to achieve strong volume growth in FY10 and margins are likely to improve in subsequent quarters due to reduction in coking coal costs. However, there could be some increase in iron ore costs due to rise of spot prices.
- ✂ We cut our FY10E EPS to Rs67.5 (earlier Rs74.5) due to lower than expected numbers for 1QFY10 and downward revision of estimates for US operations. Since JSW Steel has firmed up capex for expansion to 11mtpa, we raise debt estimates accordingly, which would increase financial leverage to 2.2x by FY11-end from 2x currently.
- ✂ The stock trades at an EV of 6.4x FY10E EBITDA. We maintain **Buy**, with a target price of Rs635 (6.5x FY10E EV/EBITDA).

JSW Steel: an investment profile

Company description

JSW Steel is India's second largest steel producer. Its production facilities are located in Karnataka, Tamil Nadu and Maharashtra. It has investments in iron ore mining in Karnataka and Chile. Besides, it has plate and pipe mill operations in USA.

Key investment arguments

- ✎ Crude steel production is expected to increase 67% YoY to 5.8m tons in FY10 – best volume growth in Indian metal space.
- ✎ JSW Steel has lowest conversion cost due to its operational efficiencies.
- ✎ Strategic location of its furnaces in iron ore rich Bellary-Hospet belt helps in keeping iron ore purchase costs low because miners primarily export ore due to absence of significant steel capacities in the region.
- ✎ Steel prices have been moving up, while input costs have eased.
- ✎ Earnings have high sensitivity to steel prices due to high financial and operating leverage.

Key investment risks

- ✎ High financial leverage and aggressive capex ahead would need further equity infusion.
- ✎ USA operations are highly exposed to economic condition of US in general, and investments in oil and gas pipelines, in particular.

Recent developments

- ✎ In 1QFY10, JSW Steel posted 45% growth in crude steel production. Growth in rolled flat and long products was 47% and 103%, respectively.

Valuation and view

- ✎ The stock trades at 9x FY10E EPS of Rs67.5. We recommend **Buy**.

Sector view

- ✎ Global demand has significantly weakened due to economic down cycle triggered by financial crisis. However, steel demand in India continues to remain strong. We remain positive on domestic steel companies.

COMPARATIVE VALUATIONS

		JSW STEEL	TATA STEEL	SAIL
P/E (x)	FY10E	9.0	9.1	12.4
	FY11E	8.5	5.1	11.8
P/BV (x)	FY10E	1.4	2.3	2.1
	FY11E	1.2	1.9	1.9
EV/Sales (x)	FY10E	1.7	0.8	1.6
	FY11E	1.7	0.7	1.7
EV/EBITDA (x)	FY10E	6.4	6.5	7.3
	FY11E	6.4	5.2	7.5

SHAREHOLDING PATTERN (%)

	JUN-09	MAR-09	JUN-08
Promoter	45.7	45.7	47.7
Domestic Inst	5.7	6.1	4.7
Foreign	35.8	35.3	35.5
Others	12.8	12.9	12.1

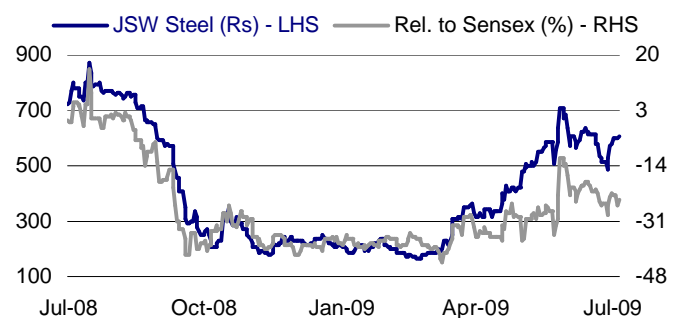
EPS: MOST FORECAST V/S CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY10	67.5	60.9	10.8
FY11	71.5	82.7	-13.6

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET * PRICE (RS)	UPSIDE (%)	RECO.
606	635	4.8	Buy

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT (CONSOLIDATED)					(RS MILLION)					
Y/E MARCH	2007	2008	2009	2010E	2011E					
Net sales	85,944	123,455	164,558	167,853	191,328					
Change (%)	39.1	43.6	33.3	2.0	14.0					
Total Expenses	58,751	91,253.0	130,646	123,085	140,810					
EBITDA	27,194	32,202	33,912	44,768	50,518					
% of Net Sales	31.6	26.1	20.6	26.7	26.4					
Depn. & Amortizatic	4,982	7,419	10,468	14,040	16,166					
EBIT	22,211	24,783	23,444	30,728	34,351					
Net Interest	3,995	5,730	9,879	12,719	14,656					
Other income	489	3,723	2,092	1,029	1,250					
PBT before EO	18,705	22,776	15,657	19,039	20,945					
EO income	447	1,384	-6,540	2,360						
PBT after EO	19,152	24,160	9,117	21,399	20,945					
Tax	6,232	7,658	3,261	7,487	7,662					
Rate (%)	32.5	31.7	35.8	35.0	36.6					
Reported PAT	12,920	16,502	5,856	13,911	13,283					
Preference dividend	279	291	289	289	289					
Adjusted PAT	12,339	15,367	9,729	12,624	13,379					
Change (%)	108.7	24.5	-36.7	29.7	6.0					

BALANCE SHEET					(RS MILLION)					
Y/E MARCH	2007	2008	2009	2010E	2011E					
Share Capital	1,640	1,871	1,871	1,871	1,871					
Reserves	49,562	74,129	79,104	81,128	93,477					
Net Worth	51,202	75,999	80,974	82,998	95,347					
Minority Interest		1,919	2,100	1,707	1,465					
Total Loans	44,521	124,252	166,385	174,385	212,386					
Deferred Tax Liabili	10,127	12,517	13,923	19,566	24,943					
Capital Employed	105,849	214,687	263,382	278,656	334,141					
Gross Block	105,128	188,883	227,172	262,510	336,803					
Less: Accum. Depr	23,237	30,743	41,210	56,075	72,242					
Net Fixed Assets	81,891	158,140	185,961	206,435	264,561					
Capital WIP	20,029	57,708	58,708	58,708	58,708					
Investments	1,929	4,696	4,696	4,696	4,696					
Curr. Assets	24,856	41,207	61,584	48,463	56,399					
Inventory	10,114	21,817	38,106	27,132	32,768					
Account Receivable	2,452	5,391	9,486	7,382	10,140					
Cash and Bank Bal	3,378	4,715	3,503	2,221	238					
Others	8,913	9,284	10,489	11,728	13,253					
Curr. Liability & P	22,857	47,064	47,567	39,646	50,223					
Account Payables	20,279	42,679	45,985	36,521	46,662					
Provisions & Others	2,578	4,385	1,583	3,124	3,561					
Net Current Asse	1,999	-5,857	14,017	8,817	6,176					
Appl. of Funds	105,849	214,687	263,382	278,656	334,141					

E: MOSL Estimates

RATIOS										
Y/E MARCH	2007	2008	2009	2010E	2011E					
Basic (Rs)										
EPS	75.2	82.2	52.0	67.5	71.5					
Cash EPS	109.2	127.9	87.3	149.4	157.4					
BV/Share	312.2	406.3	432.9	443.7	509.7					
DPS	12.5	14.0	1.0	1.0	1.0					
Payout (%)	4.8	20.6	9.5	4.0	7.8					
Valuation (x)										
P/E	8.1	7.4	11.7	9.0	8.5					
Cash P/E	5.6	4.7	6.9	4.1	3.9					
P/BV	1.9	1.5	1.4	1.4	1.2					
EV/Sales	1.6	1.9	1.7	1.7	1.7					
EV/EBITDA	5.2	7.2	8.1	6.4	6.4					
Dividend Yield (%)	2.1	2.3	0.2	0.2	0.2					
EV/ton	36,997	61,309	40,635	42,000	47,880					
Return Ratios (%)										
RoE	24.1	20.2	12.0	15.2	14.0					
RoCE	21.0	11.5	8.9	11.0	10.3					
Working Capital Ratios										
Fixed Asset Turnov	0.8	0.7	0.7	0.6	0.6					
Asset Turnover (x)	0.8	0.6	0.6	0.6	0.6					
Debtor (Days)	10	16	21	16	19					
Inventory (Days)	43	65	85	59	63					
Creditors(Days)	86	126	102	79	89					
Working Capital (D&E)	-5.9	-31.3	23.3	14.3	11.3					
Leverage Ratio (x)										
Current Ratio	1.1	0.9	1.3	1.2	1.1					
Interest Cover Ratic	5.6	4.3	2.4	2.4	2.3					
Debt/Equity	0.8	1.6	2.0	2.1	2.2					

CASHFLOW STATEMENT					(RS MILLION)					
Y/E MARCH	2007	2008	2009	2010E	2011E					
Pre-tax Profit	19,152	24,243	9,117	21,399	20,945					
Depreciation	4,982	7,419	10,468	14,040	16,166					
(Inc)/Dec in Wkg. C.	4,643	9,193	-21,086	3,918	658					
Tax Paid	-6,232	713	-1,855	-3,217	-2,286					
Other operating act	3,550	3,547	-324	-9,133	99					
CF from Op. Activ	26,096	45,115	-3,681	27,006	35,583					
(Inc)/Dec in FA + CV	-22,854	-121,434	-39,289	-35,338	-74,293					
(Pur)/Sale of Invest	-1,079	-2,766								
CF fr. Inv. Activity	-23,932	-124,200	-39,289	-35,338	-74,293					
Equity raised/(repai	70	2,176								
Chg in minorities		1,919	181	-393	-242					
Debt raised/(repaid)	770	79,731	42,133	8,000	38,001					
Dividend (incl. tax)	-614	-3,404	-557	-557	-1,033					
CF fr. Fin. Activity	226	80,422	41,757	7,050	36,726					
(Inc)/Dec in Cash	2,389	1,337	-1,212	-1,282	-1,983					
Add: Opening Balar	989	3,378	4,715	3,503	2,221					
Closing Balance	3,378	4,715	3,502	2,221	238					



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Disclosure of Interest Statement	JSW Steel
1. Analyst ownership of the stock	No
2. Group/Directors ownership of the stock	No
3. Broking relationship with company covered	No
4. Investment Banking relationship with company covered	No

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