Steel Authority of India Ltd

H2FY10E recovery looks . . . distant for now

Overweight

SAIL.BO, SAIL IN

Price: Rs58.95

▼ **Price Target: Rs81.00**
Previous: Rs135.00

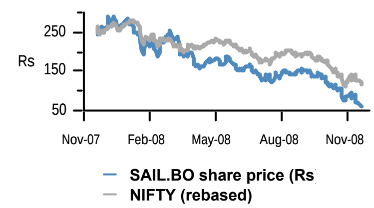
India
India Metals & Mining

Pinakin Parekh, CFA[AC]
(91-22) 6639 3018
pinakin.m.parekh@jpmchase.com

Dr.Prit Pal
(91-22) 6639 3013
prit.x.pal@jpmorgan.com

J.P. Morgan India Private Limited

Price Performance



	YTD	1m	3m	12m
ABS	-79.0%	-41.5%	-57.9%	-77.5%
REL	-21.9%	-27.2%	-18.2%	-22.1%

- **Sharply lower earnings likely over the next two to three quarters, but building in gradual recovery from H2FY10E:** We expect sharp earnings erosion over the next two to three quarters, driven by lower volumes and higher coking coal costs. We expect H2FY09E earnings decline of 79% y/y. However, we expect earnings to improve from June-09 as lower coking coal kicks in. We cut our EPS estimates sharply over FY09E-11E (13-43%).

- **Domestic demand recovery critical:** Given the dependence on imported coking coal, we believe most of India's steel companies are less competitive in the export market compared to CIS/Chinese steel exports, and therefore we believe demand recovery in the domestic market is critical to earnings recovery in H2FY10E. However, we project extremely weak steel demand over the next few months, and we cut our India steel demand growth estimates to 4.5% for FY10E.

- **Positives- sharply lower INR, import duty, lower coking coal:** The sharp INR depreciation (18% since August) and the import duty imposition (5% currently) have to an extent lessened the impact of sharp decline in import prices (current import prices of $550/MT, down 45% from peak in August). We now build in $200/MT coking coal (earlier $260/MT) for FY10E.

- **Capex plans likely to see delays if steel downcycle continues longer:** SAIL's current large cash balance of Rs164B (45% of market cap) means the company is relatively better placed on its capex program (Rs540B, of which Rs340B has been placed so far). However, in the event that a gradual recovery does not take place in H2FY10E, we would expect delays in capex spending.

- **Lacking near-term catalysts, but underleveraged balance sheet remains key positive:** While we agree that SAIL lacks near-term catalysts, driven by weak end demand and lower prices, we believe the current stock price adequately discounts the expected earnings erosion. Over the next few months, on news flow on coking coal contracts and marginal demand recovery as de-stocking gets over, headwinds should decline. Our revised Sept-09 price target of Rs81 is based on 4xFY10E EV/EBITDA. A key risk is if there were to be no recovery in steel prices and demand in H2FY10E.

Table 1: SAIL: Bloomberg SAIL IN; Reuters SAIL.BO

Rs in millions, year-end Mar

	FY08A	FY09E	FY10E	FY11E	52-week range (Rs)	293 - 55
Net Sales (Rs mn)	395,085	435,085	379,327	416,796	Market cap (Rs mn)	242041
Net Profit (Pre Exceptional Rs mn)	75,368	60,021	37,054	52,242	Market cap (US$ mn)	4841
EPS (Pre Exceptional Rs)	18.2	14.5	9.0	12.6	Avg. daily volume (MM)	12.5
Net profit growth (%)	22%	-20%	-38%	41%	Average daily value (US$ MM)	27.5
ROE (%)	38%	24%	13%	16%	Shares O/S (MM)	4130
ROCE (%)	47%	32%	18%	22%	Date of Price	18-Nov-08
P/E (x)	3.2	4.0	6.5	4.6	Index (BSE Sensex)	8451
EV/EBITDA (x)	1.2	1.1	2.3	1.9	Exchange rate	50

Source: Company reports, Datastream, and J.P. Morgan estimates. Priced as of Nov 20, 2008.

Pinakin Parekh, CFA
(91-22) 6639 3018
pinakin.m.parekh@jpmchase.com

Duration and Severity of steel downturn a key variable for our investment thesis on SAIL

While we had earlier built in a strong recovery in H2FY10E, we cut our earnings estimates sharply over FY09E-11E (by 13%, 43% and 25%, respectively), driven by our expectation for much weaker earnings over the next three quarters (till June-09, when the new coking coal contracts kick in) and a more gradual recovery into H2FY10E

Our FY10E EPS estimates are 46% below consensus estimates

While the steel industry globally and in India has been hit be severe de-stocking, collapse in end user demand, sharp decline in steel prices and severe liquidity and credit crunch, and while earnings should be poor over the next two to three quarters, the key question/variable for a longer-term investment thesis for SAIL, in our view, is the expectation of the severity of the steel downturn, its duration, and the subsequent profitability in the recovery phase. **While we had earlier built in a strong recovery in H2FY10E, we cut our earnings estimates sharply over FY0E9-11E (by 13%, 43% and 25%, respectively, and are now46% below consensus FY10E estimates), driven by our expectation for much weaker earnings over the next three quarters (till June-09, when the new coking coal contracts kick in) and for a more gradual recovery into H2FY10E.** We reduce our Sept-09 price target to Rs81, based on 4x FY10E EV/EBITDA (earlier 4.5x multiple), and we expect earnings to decline by 38% in FY10E. While the company currently remains committed to its capex plan, we expect delays for the part which is not ordered if the recovery into H2FY10E does not take place. We also believe a hike in import duty to 10% is likely if import volumes in India continue to rise while steel prices decline.

Table 2: J.P. Morgan estimates vs. consensus

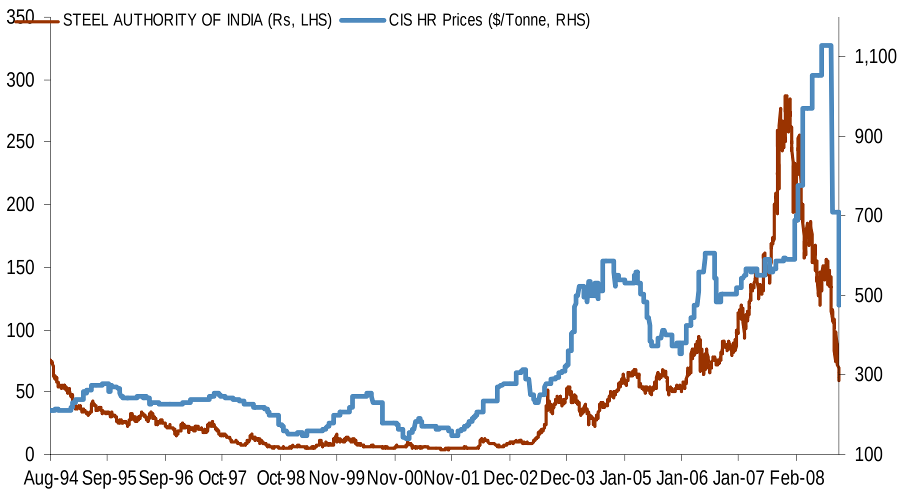
Rs in millions, %, year-end Mar

	FY09E	FY10E	FY11E
Sales			
Consensus	493010	490907	519194
J.P. Morgan ests	435,085	379,327	416,796
% Higher/(Lower)	-12%	-23%	-20%
EBITDA			
Consensus	107058	107557	128594
J.P. Morgan ests	89,899	56,814	86,345
% Higher/(Lower)	-16%	-47%	-33%
EPS			
Consensus	16.95	16.51	18.58
J.P. Morgan ests	14.53	8.97	12.65
% Higher/(Lower)	-14%	-46%	-32%

Source: J.P. Morgan estimates, Bloomberg

Figure 1: CIS steel price and SAIL stock price

Rs. $/MT

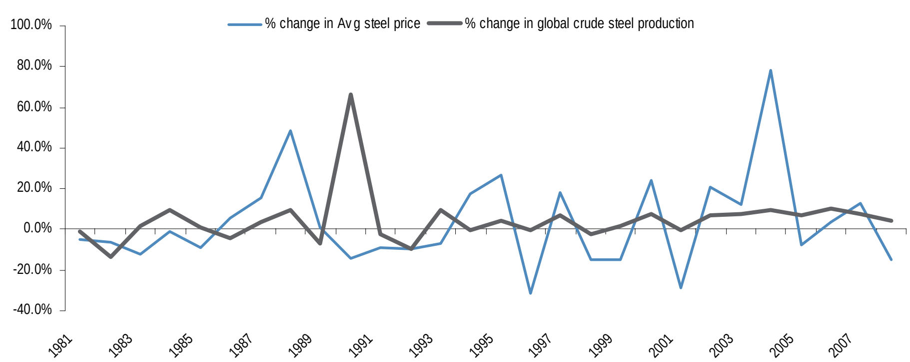


Source: Datastream

We believe a far more consolidated steel industry and subsequently higher production discipline should result in higher than trough margins in the down cycle.

Figure 2: Crude Steel production and steel price % change

% change



Source: Metal Bulletin, IISO J.P. Morgan estimates.

Steel industry - Variables to watch out for

We believe that the credit/liquidity crunch combined with severe de-stocking have been the key reasons behind the sharp fall in steel prices. We believe that while end user demand should remain weak over the next 12 months, the key to steel prices and earnings for next year will be how the following variables move:

- **Continued global steel industry and supply discipline:** We have so far seen a far more proactive global steel industry in the face of severe price and demand declines. Steel companies across India, Europe, CIS, and the US have announced large production cuts. We believe continued industry discipline could potentially mean a higher floor in terms on industry profitability into FY10E (via lower raw material prices and some recovery in steel prices induced by sharp production cuts). However, we believe the key to industry supply discipline is lower Chinese steel exports.

Table 3: Steel Production Cuts (Excerpted from J. P Morgan Global Metals report, “Iron Ore and Coal Worst Case Becoming Base Case,” dated 19 November 2008)

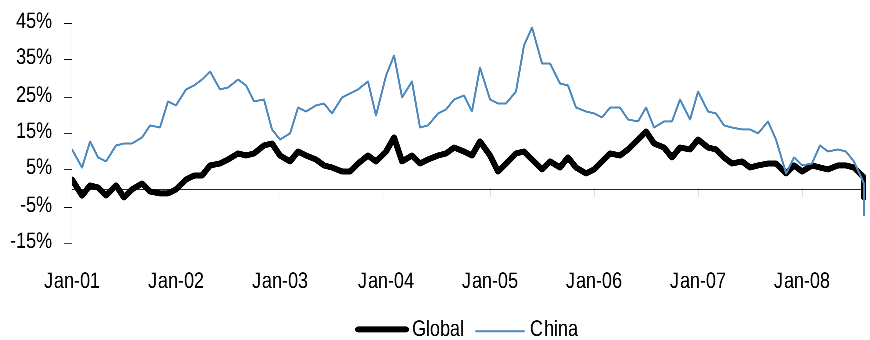
Mtpy

Region/ Country	Company	Cap Shutdowns (Mtpy)	% of Capacity
World	Arcelor Mittal	36.0	35%
North America	AK Steel	2.8	35%
	Severstal		30%
Latin America	Ternium	3.5	35%
EU- 27	Severstal		30%
	TK Steel		20-30%
	Corus		20%
	Salzgitter		30%
	Riva		12%
CIS	Severstal		25%
	NLMK		14%
	MMK		15%
China	Angang Steel		20%
	Maanshan	2.4	20%
	Hebei		10-20%
	Baosteel	1.0	
Other Asia	Ispat		15%

Source: J.P. Morgan estimates, Company data.

Figure 2: Global and China y/y change in steel production

%



Source: IISI

- **Chinese steel exports:** Chinese steel exports declined sharply in Oct-08 (down 36% m/m), but J.P. Morgan Chinese steel analyst Feng Zhang believes this is more due to lack of demand in the overseas market, and he expects steel exports to remain elevated post the removal of export tariffs. We believe continued high Chinese steel exports could potentially nullify the supply discipline in other regions and lead to lower steel prices.
- **Bulk contracts for next year:** Our global metals team have reduced their forecast for iron ore and coking coal and now expect approximately 30% decline in both for next year. While the bulk contracts would only start flowing in from April onwards (for SAIL ,coking coal contracts are from July-June), this should be positive for profitability in H2FY10E.

Table 4: J.P. Morgan Iron Ore Price Forecasts

$c/dmtu

	2007	2008	FY2009E	FY2010E	FY2011E	FY2012E	FY2013E	LT Real
Southern System Fines to Europe								
New	81	134	94	85	76	69	62	65
OLD	81	134	121	109	98	83	75	65
% Change	0%	0%	-22%	-22%	-22%	-17%	-17%	0%
Carajas Fines To Europe								
New	85	141	98	89	80	72	65	68
OLD	85	141	127	114	102	87	78	68
% Change	0%	0%	-23%	-22%	-22%	-17%	-17%	0%
Vale's Lumps to Europe								
New	100	197	138	124	112	101	91	77
OLD	100	197	178	160	144	122	110	77
% Change	0%	0%	-22%	-23%	-22%	-17%	-17%	0%
Hamersley Fines to Asia								
New	80	145	101	91	82	74	66	65
OLD	80	145	130	117	105	90	81	65
% Change	0%	0%	-22%	-22%	-22%	-18%	-19%	0%
Hamersley Lumps to Asia								
New	103	202	141	127	114	103	93	78
OLD	103	202	182	163	147	125	112	78
% Change	0%	0%	-23%	-22%	-22%	-18%	-17%	0%

Source: J.P. Morgan estimates, Company data.

Table 5: J.P. Morgan Coking Coal Price Forecast

$

	2007	2008	FY2009E	FY2010E	FY2011E	Long Term
Thermal coal						
New	55.7	125	100	100	90	70
Old	55.7	125	125	115	100	70
% Change	0%	0%	-20%	-13%	-10%	0%
Semi Soft Coking						
New	62	250	120	120	108	80
Old	62	250	150	138	120	80
% Change	0%	0%	-20%	-13%	-10%	0%
Hard Coking Coal						
New	98.4	300	200	175	150	100
Old	98.4	300	260	250	175	100
% Change	0%	0%	-23%	-30%	-14%	0%

Source: J.P. Morgan estimates, Company data.

- **China stimulus package and recovery:** Our Chinese steel analyst believes that the stimulus package announced by the Chinese government is positive and should aid steel demand recovery in H2CY09E.

Pinakin Parekh, CFA
(91-22) 6639 3018
pinakin.m.parekh@jpmchase.com

Table 6: China Demand/Supply Model

%, Rmb, million tonnes

	Crude Capacity	Change	Crude Prod	Change	Utilization rate	Net Import	Apparent Consumption	Change	HRC Price Rmb $/t	Change
FY02	230		180		78%	24	204		2,710	
FY03	286	24%	219	22%	77%	36	255	25%	3,327	23%
FY04	356	24%	269	23%	76%	13	282	11%	4,517	36%
FY05	432	21%	348	29%	81%	0	348	23%	4,198	-7%
FY06	488	13%	422	21%	86%	-34	388	11%	3,951	-6%
FY07	545	12%	496	18%	91%	-54	442	14%	4,298	9%
FY08E	585	7%	520	5%	89%	-43	477	8%	4,950	15%
FY09E	615	5%	550	6%	89%	-38	512	7%	4,500	-9%
FY10E	645	5%	600	9%	93%	-35	565	10%	4,600	2%

Source: J.P. Morgan estimates, Company data.

For SAIL – we believe domestic demand recovery is more critical than price recovery

Unlike alumina and aluminum, most of India's steel industry is dependent on imported coking coal (only Tata Steel has some captive coking coal), making it relatively higher cost compared to integrated steel companies in CIS, and some of the Chinese steel companies that benefit from sharply lower spot iron ore prices and coking coal, where China is self-sufficient. Therefore, in the current environment we see domestic demand recovery as more critical for the Indian steel industry, as steel companies cannot export out the lower domestic demand. We cut our Indian steel consumption forecasts to 5% in FY09E and 4.5% in FY10E.

Table 7: India Demand/Supply Model

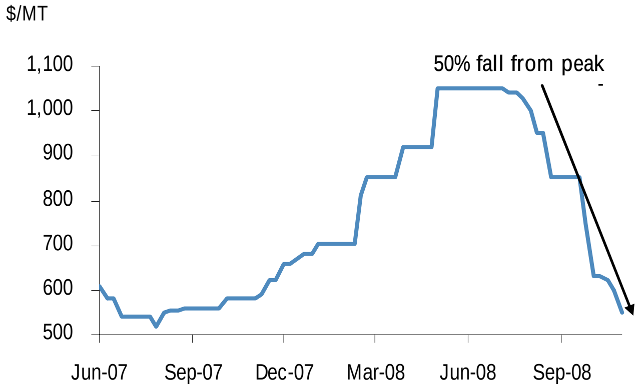
	Long Steel Products		Flat Steel Products		Total finished steel		Production		Export	Consumption (Prod+Import-Export)	% chg
YE March 31	Total	% change	Total	% change	Total	% change					
FY01	12.2	5%	15.8	9%	28.0	7%	29.3	1.4	2.7	28.0	
FY02	12.7	4%	16.5	4%	29.2	4%	30.6	1.3	2.7	29.2	4.2%
FY03	13.5	6%	17.1	4%	30.6	5%	33.6	1.5	4.5	30.6	5.0%
FY04	14.6	8%	19.0	11%	33.6	10%	36.9	1.5	4.8	33.6	9.7%
FY05	15.8	8%	21.9	15%	37.7	12%	40.0	2.1	4.4	37.7	12.2%
FY06	17.8	13%	26.1	19%	43.9	16%	44.5	3.8	4.5	43.9	16.4%
FY07	24.7	39%	25.0	-4%	49.7	13%	50.1	4.4	4.9	49.7	13.1%
FY08	26.6	8%	27.9	12%	54.5	9.7%	52.6	6.5	4.6	54.5	9.7%
FY09E	27.8	4.5%	29.4	5.4%	57.2	5.0%	55.2	6.0	4.0	57.2	5.0%
FY10E	28.9	4.0%	30.9	5.0%	59.8	4.5%	59.8	5.0	5.0	59.8	4.5%
FY11E	30.9	7.0%	33.2	7.5%	64.1	7.3%	64.1	5.0	5.0	64.1	7.3%

Source: J.P. Morgan estimates, Company data.

Lower INR, import duty: key positives for SAIL

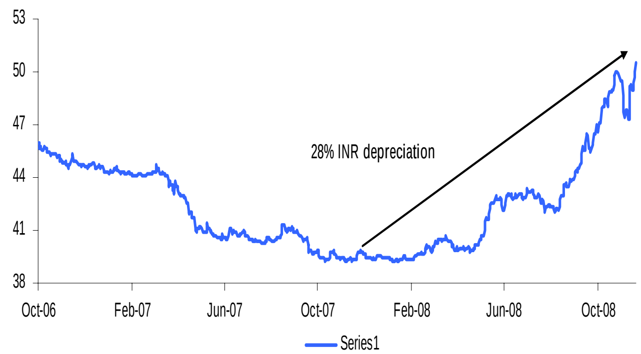
While imported steel prices have declined sharply (current import prices into India $500-550/MT), the domestic steel industry has been somewhat cushioned by the steep INR depreciation. Equally important has been the 5% import duty imposition as it also to an extent has mitigated the impact of lower steel prices. We believe that, in the event that import volumes increase significantly from here while import prices decline, we may possibly see a hike in import duty from 5% to 10%. However, we believe this is unlikely in the near term.

Figure 3: China Export HRC Prices



Source: Metals Bulletin

Figure 4: INR vs USD



Source: Bloomberg

SAIL: We expect sharply lower earnings over next 2-3 quarters, until lower coking coal kicks in

While the company has reduced prices over the last month (Rs5,000-6,000/MT), we believe domestic steel demand has deteriorated sharply since October. **We expect SAIL to report sharply lower earnings over the next 2-3 quarters, driven by lower steel volumes and lower realizations, while the key cost component -- coking coal -- remains contracted at $300/MT till June-09. We expect H2FY09E EBITDA to decline 76% over H1FY09E and 79% over H2FY09E. We also cut our FY10E earnings estimates aggressively and expect y/y EPS declines by 38%. Lower coking coal (J.P Morgan estimate for 2009 coking coal at $200/MT from $300/MT in 2008) should result in a gradual earnings recovery in H2FY10E.** Our FY10E steel import price assumption is $550/MT.

Table 8: Key Assumptions Change Table

Rs, Rs Mn

	FY09E	FY10E	FY11E
Saleable Steel			
New	11.4	11.3	12.8
Old	12.6	13.5	14.9
% Change	-9%	-16%	-14%
Net Realization			
New	38,165	33,486	32,644
Old	38,280	35,006	34,050
% Change	-1%	-4%	-4%
EBITDA			
New	89,899	56,814	86,345
Old	103,048	98,644	115,242
% Change	-13%	-42%	-25%
EBITDA/MT			
New	7,619	4,853	6,568
Old	7,941	7,120	7,544
% Change	-4%	-32%	-13%
EPS			
New	14.53	8.97	12.65
Old	16.63	15.70	16.93
% Change	-13%	-43%	-25%

Source: J.P. Morgan estimates, Company data.

Table 9: Steel price assumption

$/MT

FY10E HRC Price Forecast for India	
Import Price $/MT	550
Freight $/MT	25
CIF Price $/MT	575
Import Duty @5%	29
Landed Price	604
INR	49
Landed INR Price	29,584
Internal Freight/Other Charges	1000
Imported HRC Prices	30,584

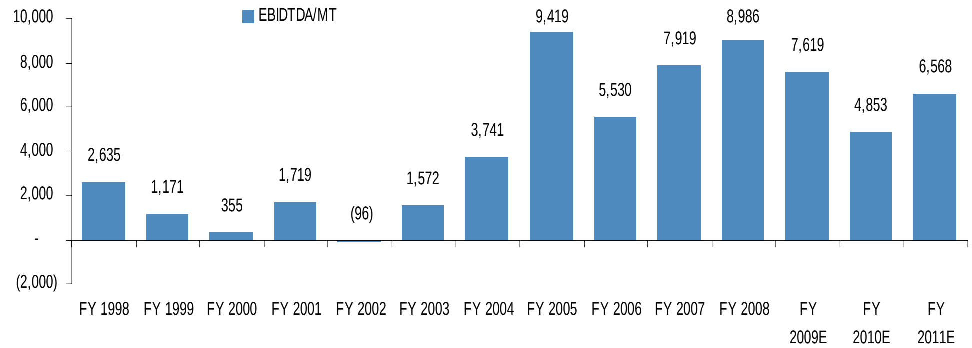
Source: J.P. Morgan estimates.

SAIL: Building in lower profitability/MT

We build in sharply lower EBITDA/MT for SAIL (approximately $110/MT, down 49% from peak levels in FY05). However, this is not at FY01-03 trough levels of $35/MT, driven by our view of a gradual recovery in H2FY10E, a more consolidated steel industry resulting in rational supply response to weak demand, lower coking coal prices, and INR remaining at current levels.

Pinakin Parekh, CFA
(91-22) 6639 3018
pinakin.m.parekh@jpmchase.com

Figure 5: SAIL EBITDA/MT Chart



Source: J.P. Morgan estimates, Company data.

SAIL's capex program likely to see delays if downcycle continues longer

While SAIL remains committed to a large capex plan (declared capex plan of Rs540B), we believe a large part of this has not yet been ordered. We believe while it is positive for a company to be able to increase capacity in a downcycle in order to benefit in the upturn, **we expect delays in the event the expected recovery in H2FY10E does not materialize.** SAIL's current cash balance stands at Rs164B, and we believe this provides for the company to go ahead with the initial spend of Rs340B, which has already been placed. However, we expect the cash outflow for the capex to be staggered over the next few years**.** We expect the company to be free cash flow negative over FY10-11E.

Table 10: SAIL Cash Flow Snapshot

Rs in millions, year-end Mar

	FY08	FY09E	FY10E	FY11E
Net Income (Pre Exceptional)	75,368	60,021	37,054	52,242
Add: Depreciation	12,355	13,408	14,122	16,642
Working Capital Movement	11,898	17,244	733	(4,935)
Operational Cash Flow	99,621	90,672	51,908	63,948
Capital Expenditure	(23,626)	(46,105)	(72,000)	(85,000)
Free Cash Flow	75,995	44,568	(20,092)	(21,052)

Source: J.P. Morgan estimates, Company data.

Underleveraged balance sheet remains key positive

We believe as uncertainty remains on the timing of recovery and also the subsequent profitability for steel companies, we continue to prefer, on a relative basis in India, companies with underleveraged balance sheets. We remain OW on SAIL with a revised Sept-09 price target of Rs81 based on 4xFY10E EV/EBITDA (earlier 4.5x FY10E EV/EBITDA). A key risk to our earnings estimates is that of no recovery in steel prices and demand in H2FY10E.

Pinakin Parekh, CFA
(91-22) 6639 3018
pinakin.m.parekh@jpmchase.com

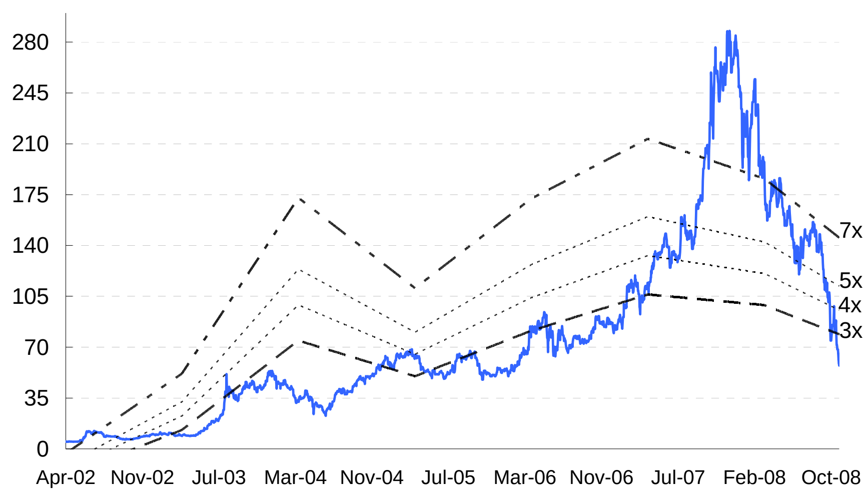
Table 11: Valuations for Ferrous and Non Ferrous Companies across Asia

Local Currency

				Market Cap	P/E		EV/EBITDA	
Company	Ticker	Rating	Market Price	(US $ Mn)	FY09/CY08E	FY10/CY09E	FY09/CY08E	FY10/CY09E
Steel								
India								
JSW Steel	JSTL IN	NR	220	892	2.2	1.7	3.6	3.0
SAIL	SAIL IN	OW	58	4869	4	6.5	1.1	2.3
Tata Steel	TATA IN	N	156	2365	1.7	2.0	3.3	3.6
Asia ex. India								
Maanshaan	323 HK	N	2	3269	6.1	8.1	3.5	3.4
Angang	347 HK	OW	5	7117	5.7	7.5	3.9	4.1
Baosteel	600019 CH	OW	5	13528	8.9	11.0	4.5	4.7
China Steel	2002 TT	UW	22	8060	5.2	5.6	3.7	3.8
Europe								
Thyssenkrup	TKA GR	N	12	7957	2.7	3.3	1.9	1.8
Voestalpine	VOE AV	OW	14	2836	2.1	3.0	2.4	2.8
Americas								
Arcelor Mittal	MT US	OW	18	25688	1.9	4.5	2.0	3.8
US Steel	X US	OW	25	2931	1.1	0.9	0.9	0.2
Nucor	NUE US	OW	28	8897	4.1	6.1	2.4	2.7
CSN	CSNA3 BS	N	22	7474	4.2	3.0	2.9	1.8
Usiminas	USNZY US	OW	20	4167	2.8	2.1	2.0	1.9
Russia								
Evraz	EVR LI	OW	5	1952	0.9	0.9	1.7	1.3
Novolipetsk	NLMK LI	OW	6	3734	1.0	1.0	1.5	1.4
MMK	MAGN RU	N	0	2235	1.7	1.6	2.4	2.5
Severstal	SVST LI	UW	2	2267	3.7	4.6	6.3	6.5

Source: Company reports and J.P. Morgan estimates, Bloomberg. Consensus estimates used for NR stocks. Note: Prices based on Nov 19 market close.

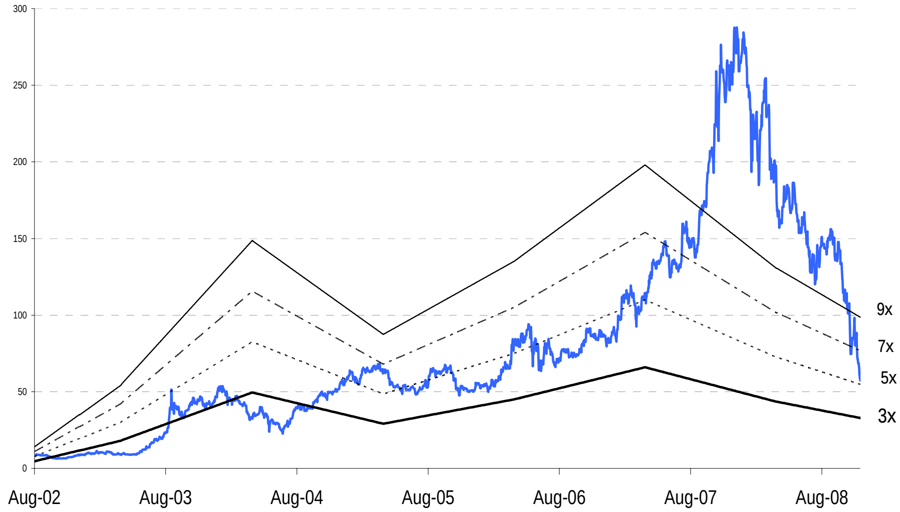
Figure 6: SAIL EV/EBITDA Band Chart



Source: J.P. Morgan estimates, Company data.

Pinakin Parekh, CFA
(91-22) 6639 3018
pinakin.m.parekh@jpmchase.com

Figure 7: SAIL P/E Band Chart



Source: J.P. Morgan estimates, Company data.

Pinakin Parekh, CFA
(91-22) 6639 3018
pinakin.m.parekh@jpmchase.com

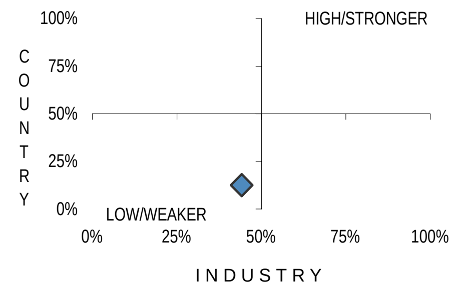
All Data As Of 20-Nov-08

Q-Snapshot: Steel Authority of India Ltd.

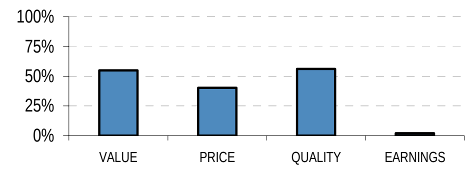
Quant Return Drivers (a Score >50% indicates company ranks 'above average')

Score 0% (worst) to 100% (best)	vs Country	vs Industry	Raw Value
Value			
P/E Vs Market (12mth fwd EPS)	86%	81%	0.5x
P/E Vs Sector (12mth fwd EPS)	74%	77%	0.7x
EPS Growth (forecast)	7%	25%	-12.5%
Value Score	55%	68%	
Price Momentum			
12 Month Price Momentum	16%	17%	-77.0%
1 Month Price Reversion	97%	96%	-41.5%
Momentum Score	40%	39%	
Quality			
Return On Equity (forecast)	72%	81%	27.8%
Earnings Risk (Variation in Consensus)	33%	72%	0.13
Quality Score	56%	85%	
Earnings & Sentiment			
Earnings Momentum 3mth (risk adjusted)	5%	14%	-223.3
1 Mth Change in Avg Recom.	6%	15%	-0.42
Net Revisions FY2 EPS	54%	60%	-71%
Earnings & Sentiment Score	2%	18%	
COMPOSITE Q-SCORE* (0% To 100%)	13%	44%	

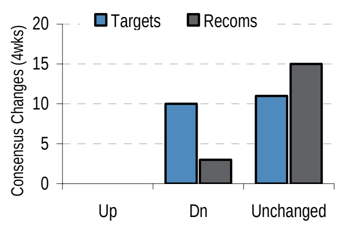
J.P. Morgan Composite Q-Score



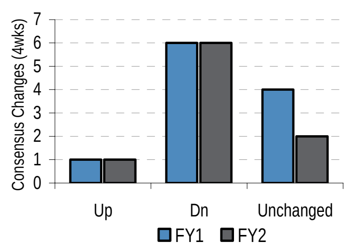
Quant Return Drivers Summary (vs Country)



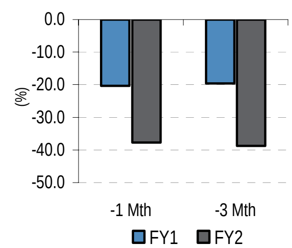
Targets & Recommendations**



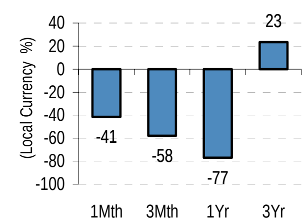
EPS Revisions**



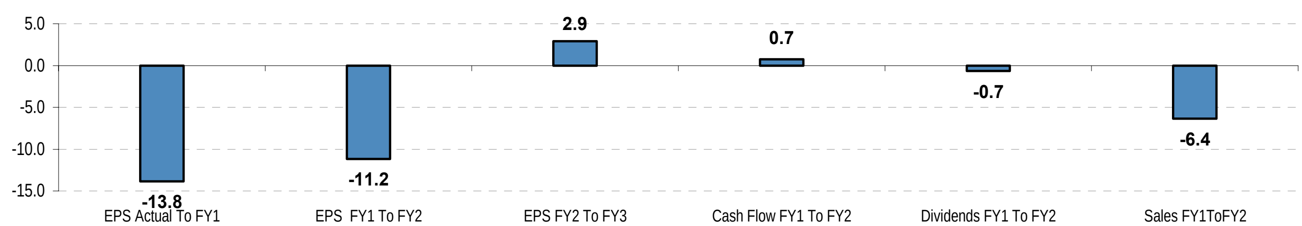
EPS Momentum (%)



Historical Total Return (%)



Consensus Growth Outlook (%)



Closest in Country by Size (Consensus. ADV = average daily value traded in US$m over the last 3 mths)

Code	Name	Industry	USD MCAP	ADV	PE FY1	Q-Score*
500180-IN	HDFC Bank Ltd.	Regional Banks	7,890	8.91	16.6	57%
532868-IN	DLF Ltd.	Real Estate Development	7,742	15.71	4.9	27%
507685-IN	Wipro Ltd.	Information Technology Services	6,814	1.97	8.6	47%
532898-IN	Power Grid Corp. of India Ltd.	Electric Utilities	6,119	2.10	16.3	13%
532792-IN	Cairn India Ltd.	Oil & Gas Production	5,198	4.46	55.7	16%
500113-IN	**Steel Authority of India Ltd.**	**Steel**	**5,139**	**6.18**	**3.7**	**13%**
532939-IN	Reliance Power Ltd.	Electric Utilities	5,007	10.19	130.5	14%
524715-IN	Sun Pharmaceutical Industries Ltd.	Pharmaceuticals: Major	4,964	1.11	13.2	87%
532155-IN	GAIL (India) Ltd.	Gas Distributors	4,911	2.55	7.4	75%
500510-IN	Larsen & Toubro Ltd.	Trucks/Construction/Farm Machinery	4,525	26.52	14.4	18%
500376-IN	Satyam Computer Services Ltd.	Information Technology Services	3,304	6.16	7.0	68%

Source: Factset, Thomson and J.P. Morgan Quantitative Research. For an explanation of the Q-Snapshot, please visit http://jpmorgan.hk.acrobat.com/qsnapshot/
Q-Snapshots are a product of J.P. Morgan's Global Quantitative Analysis team and provide quantitative metrics summarized in an overall company 'Q-Score.'
Q-Snapshots are based on consensus data and should not be considered as having a direct relationship with the J.P. Morgan analysts' recommendation.
* The Composite Q-Score is calculated by weighting and combining the 10 Quant return drivers shown. The higher the Q-Score the higher the one month expected return. On a 14 Year back-test the stocks with the highest Q-Scores have been shown (on average) to significantly outperform those stocks with the lowest Q-Scores in this universe. ** The number of up, down and unchanged target prices, recommendations or EPS forecasts that make up consensus.

Pinakin Parekh, CFA
(91-22) 6639 3018
pinakin.m.parekh@jpmchase.com

Sail Authority of India: Summary of Financials

Rs in millions, year-end Mar

Profit and Loss statement	FY08	FY09E	FY10E	FY11E
Revenues	395,085	435,085	379,327	416,796
% change Y/Y	16%	10%	-13%	10%
EBITDA	110,622	89,899	56,814	86,345
% change Y/Y	18%	-19%	-37%	52%
EBITDA Margin (%)	28%	21%	15%	21%
EBIT	117,197	93,491	58,692	81,704
% change Y/Y	20%	-20%	-37%	39%
EBIT Margin (%)	30%	21%	15%	20%
Net Interest	2,509	2,550	2,550	2,550
Earnings before tax	114,687	90,941	56,142	79,154
% change Y/Y	22%	-21%	-38%	41%
Tax	(39,320)	(30,920)	(19,088)	(26,912)
as % of EBT	34%	34%	34%	34%
Net Income (Pre Exceptional)	75,368	60,021	37,054	52,242
% change Y/Y	22%	-20%	-38%	41%
Shares Outstanding	4,130	4,130	4,130	4,130
EPS (pre exceptional)	18.2	14.5	9.0	12.6
% change Y/Y	22%	-20%	-38%	41%

Cash flow statement r	FY08	FY09E	FY10E	FY11E
Net Income (Pre Exceptional)	75,368	60,021	37,054	52,242
Add: Depreciation	12,355	13,408	14,122	16,642
Working Capital Movement	11,898	17,244	733	(4,935)
Operational Cash Flow	99,621	90,672	51,908	63,948
Net Capex	(23,626)	(46,105)	(72,000)	(85,000)
Free cash flow	75,995	44,568	(20,092)	(21,052)
Equity raised/ (repaid)	970	(1,563)	0	0
Debt raised/ (repaid)	(11,353)	(452)	0	0
Dividends paid	(18,137)	(17,422)	(9,417)	(11,772)
Beginning cash	96,098	137,594	168,981	139,472
Ending cash	137,594	168,981	139,472	106,648
DPS	3.8	3.7	2.0	2.5

Balance sheet	FY08	FY09E	FY10E	FY11E
Inventories	68,572	65,561	62,355	68,514
Debtors	30,481	23,840	20,785	22,838
Cash and bank balances	137,594	168,981	139,472	106,648
Other Current Assets	2,731	855	855	855
Loans and advances	23,795	20,000	20,000	20,000
Investments	5,382	2,920	2,920	2,920
Net fixed assets	139,609	172,306	230,184	298,542
Total assets	408,164	454,462	476,571	520,318
Liabilities				
Sundry Creditors	29,816	35,278	32,755	33,677
Others	102,169	102,422	99,417	101,772
Total current liabilities	131,985	137,700	132,172	135,449
Total debt	30,452	30,000	30,000	30,000
Other liabilities	15,686	15,686	15,686	15,686
Total liabilities	178,123	183,386	177,858	181,135
Shareholders' equity	230,041	271,077	298,713	339,183
BVPS	55.7	65.6	72.3	82.1

Ratio Analysis %, year-end Mar	FY08E	FY09E	FY10E	FY11E
EBITDA margin	28%	21%	15%	21%
Operating margin	30%	21%	15%	20%
Net profit margin	19%	14%	10%	13%
Sales growth	16%	10%	-13%	10%
Net profit growth	22%	-20%	-38%	41%
EPS growth	22%	-20%	-38%	41%
Interest coverage (x)	44	35	22	34
Net debt to equity	-47%	-51%	-37%	-23%
Sales/assets	106%	101%	0%	0%
Assets/equity (x)	1.9	1.7	-	-
ROE	38%	24%	13%	16%
ROCE	47%	32%	18%	22%

Source: J.P. Morgan estimates, Company data.

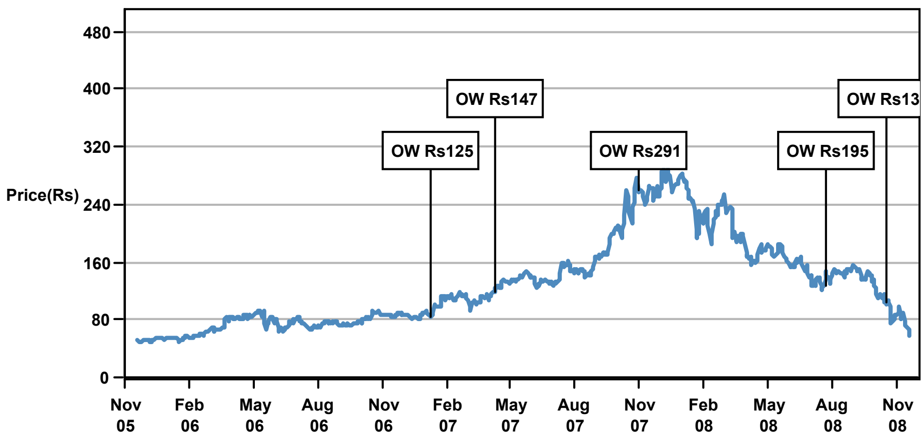
Pinakin Parekh, CFA
(91-22) 6639 3018
pinakin.m.parekh@jpmchase.com

Analyst Certification:
The research analyst(s) denoted by an “AC” on the cover of this report certifies (or, where multiple research analysts are primarily responsible for this report, the research analyst denoted by an “AC” on the cover or within the document individually certifies, with respect to each security or issuer that the research analyst covers in this research) that: (1) all of the views expressed in this report accurately reflect his or her personal views about any and all of the subject securities or issuers; and (2) no part of any of the research analyst’s compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed by the research analyst(s) in this report.

Important Disclosures

- **Client of the Firm:** Steel Authority of India Ltd is or was in the past 12 months a client of JPMSI.

Steel Authority of India Ltd (SAIL.BO) Price Chart



Date	Rating	Share Price (Rs)	Price Target (Rs)
10-Jan-07	OW	84.90	125.00
11-Apr-07	OW	117.70	147.00
31-Oct-07	OW	261.05	291.00
22-Jul-08	OW	125.65	195.00
16-Oct-08	OW	104.20	135.00

Source: Reuters and J.P. Morgan; price data adjusted for stock splits and dividends.
Initiated coverage Jan 10, 2007. This chart shows J.P. Morgan's continuing coverage of this stock; the current analyst may or may not have covered it over the entire period.
J.P. Morgan ratings: OW = Overweight, N = Neutral, UW = Underweight.

Explanation of Equity Research Ratings and Analyst(s) Coverage Universe:
J.P. Morgan uses the following rating system: **Overweight** [Over the next six to twelve months, we expect this stock will outperform the average total return of the stocks in the analyst’s (or the analyst’s team’s) coverage universe.] **Neutral** [Over the next six to twelve months, we expect this stock will perform in line with the average total return of the stocks in the analyst’s (or the analyst’s team’s) coverage universe.] **Underweight** [Over the next six to twelve months, we expect this stock will underperform the average total return of the stocks in the analyst’s (or the analyst’s team’s) coverage universe.] The analyst or analyst’s team’s coverage universe is the sector and/or country shown on the cover of each publication. See below for the specific stocks in the certifying analyst(s) coverage universe.

Coverage Universe: **Pinakin Parekh, CFA:** ACC Limited (ACC.BO), Ambuja Cements Limited (ABUJ.BO), Binani Cement Ltd (BINC.BO), Cipla Limited (CIPL.BO), Dr Reddy's Limited (REDY.BO), Glenmark Pharmaceuticals Ltd (GLEN.BO), Grasim Industries Ltd (GRAS.BO), Hindalco Industries (HALC.BO), Jindal SAW (JIND.BO), Maharashtra Seamless (MHSM.NS), Monnet Ispat & Energy Limited (MNET.BO), National Aluminium Co Ltd (NALU.BO), Ranbaxy Laboratories Ltd (RANB.BO), Steel Authority of India Ltd (SAIL.BO), Sun Pharmaceutical (SUN.BO), Tata Steel Ltd (TISC.BO), UltraTech Cement Ltd (ULTC.BO), Welspun Gujarat (WGSR.BO)

J.P. Morgan Equity Research Ratings Distribution, as of September 30, 2008

	Overweight (buy)	Neutral (hold)	Underweight (sell)
JPM Global Equity Research Coverage	42%	44%	15%
IB clients*	53%	51%	43%
JPMSI Equity Research Coverage	40%	48%	12%
IB clients*	76%	70%	59%

*Percentage of investment banking clients in each rating category.
For purposes only of NASD/NYSE ratings distribution rules, our Overweight rating falls into a buy rating category; our Neutral rating falls into a hold rating category; and our Underweight rating falls into a sell rating category.

Valuation and Risks: Please see the most recent company-specific research report for an analysis of valuation methodology and risks on any securities recommended herein. Research is available at http://www.morganmarkets.com , or you can contact the analyst named on the front of this note or your J.P. Morgan representative.

Analysts' Compensation: The equity research analysts responsible for the preparation of this report receive compensation based upon various factors, including the quality and accuracy of research, client feedback, competitive factors, and overall firm revenues, which include revenues from, among other business units, Institutional Equities and Investment Banking.

Registration of non-US Analysts: Unless otherwise noted, the non-US analysts listed on the front of this report are employees of non-US affiliates of JPMSI, are not registered/qualified as research analysts under NASD/NYSE rules, may not be associated persons of JPMSI, and may not be subject to NASD Rule 2711 and NYSE Rule 472 restrictions on communications with covered companies, public appearances, and trading securities held by a research analyst account.

Other Disclosures

J.P. Morgan is the global brand name for J.P. Morgan Securities Inc. (JPMSI) and its non-US affiliates worldwide.

Options related research: If the information contained herein regards options related research, such information is available only to persons who have received the proper option risk disclosure documents. For a copy of the Option Clearing Corporation's Characteristics and Risks of Standardized Options, please contact your J.P. Morgan Representative or visit the OCC's website at http://www.optionsclearing.com/publications/risks/riskstoc.pdf.

Legal Entities Disclosures
U.S.: JPMSI is a member of NYSE, FINRA and SIPC. J.P. Morgan Futures Inc. is a member of the NFA. JPMorgan Chase Bank, N.A. is a member of FDIC and is authorized and regulated in the UK by the Financial Services Authority. **U.K.:** J.P. Morgan Securities Ltd. (JPMSL) is a member of the London Stock Exchange and is authorised and regulated by the Financial Services Authority. Registered in England & Wales No. 2711006. Registered Office 125 London Wall, London EC2Y 5AJ. **South Africa:** J.P. Morgan Equities Limited is a member of the Johannesburg Securities Exchange and is regulated by the FSB. **Hong Kong:** J.P. Morgan Securities (Asia Pacific) Limited (CE number AAJ321) is regulated by the Hong Kong Monetary Authority and the Securities and Futures Commission in Hong Kong. **Korea:** J.P. Morgan Securities (Far East) Ltd, Seoul branch, is regulated by the Korea Financial Supervisory Service. **Australia:** J.P. Morgan Australia Limited (ABN 52 002 888 011/AFS Licence No: 238188) is regulated by ASIC and J.P. Morgan Securities Australia Limited (ABN 61 003 245 234/AFS Licence No: 238066) is a Market Participant with the ASX and regulated by ASIC. **Taiwan:** J.P.Morgan Securities (Taiwan) Limited is a participant of the Taiwan Stock Exchange (company-type) and regulated by the Taiwan Securities and Futures Bureau. **India:** J.P. Morgan India Private Limited is a member of the National Stock Exchange of India Limited and The Stock Exchange, Mumbai and is regulated by the Securities and Exchange Board of India. **Thailand:** JPMorgan Securities (Thailand) Limited is a member of the Stock Exchange of Thailand and is regulated by the Ministry of Finance and the Securities and Exchange Commission. **Indonesia:** PT J.P. Morgan Securities Indonesia is a member of the Indonesia Stock Exchange and is regulated by the BAPEPAM. **Philippines:** J.P. Morgan Securities Philippines Inc. is a member of the Philippine Stock Exchange and is regulated by the Securities and Exchange Commission. **Brazil:** Banco J.P. Morgan S.A. is regulated by the Comissao de Valores Mobiliarios (CVM) and by the Central Bank of Brazil. **Mexico:** J.P. Morgan Casa de Bolsa, S.A. de C.V., J.P. Morgan Grupo Financiero is a member of the Mexican Stock Exchange and authorized to act as a broker dealer by the National Banking and Securities Exchange Commission. **Singapore:** This material is issued and distributed in Singapore by J.P. Morgan Securities Singapore Private Limited (JPMSS) [mica (p) 207/01/2008 and Co. Reg. No.: 199405335R] which is a member of the Singapore Exchange Securities Trading Limited and is regulated by the Monetary Authority of Singapore (MAS) and/or JPMorgan Chase Bank, N.A., Singapore branch (JPMCB Singapore) which is regulated by the MAS. **Malaysia:** This material is issued and distributed in Malaysia by JPMorgan Securities (Malaysia) Sdn Bhd (18146-x) which is a Participating Organization of Bursa Malaysia Securities Bhd and is licensed as a dealer by the Securities Commission in Malaysia. **Pakistan:** J. P. Morgan Pakistan Broking (Pvt.) Ltd is a member of the Karachi Stock Exchange and regulated by the Securities and Exchange Commission of Pakistan.

Country and Region Specific Disclosures
U.K. and European Economic Area (EEA): Issued and approved for distribution in the U.K. and the EEA by JPMSL. Investment research issued by JPMSL has been prepared in accordance with JPMSL's Policies for Managing Conflicts of Interest in Connection with Investment

Research which outline the effective organisational and administrative arrangements set up within JPMSL for the prevention and avoidance of conflicts of interest with respect to research recommendations, including information barriers, and can be found at http://www.jpmorgan.com/pdfdoc/research/ConflictManagementPolicy.pdf. This report has been issued in the U.K. only to persons of a kind described in Article 19 (5), 38, 47 and 49 of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (all such persons being referred to as "relevant persons"). This document must not be acted on or relied on by persons who are not relevant persons. Any investment or investment activity to which this document relates is only available to relevant persons and will be engaged in only with relevant persons. In other EEA countries, the report has been issued to persons regarded as professional investors (or equivalent) in their home jurisdiction **Germany:** This material is distributed in Germany by J.P. Morgan Securities Ltd. Frankfurt Branch and JPMorgan Chase Bank, N.A., Frankfurt Branch who are regulated by the Bundesanstalt für Finanzdienstleistungsaufsicht. **Australia:** This material is issued and distributed by JPMSAL in Australia to “wholesale clients” only. JPMSAL does not issue or distribute this material to “retail clients.” The recipient of this material must not distribute it to any third party or outside Australia without the prior written consent of JPMSAL. For the purposes of this paragraph the terms “wholesale client” and “retail client” have the meanings given to them in section 761G of the Corporations Act 2001. **Hong Kong:** The 1% ownership disclosure as of the previous month end satisfies the requirements under Paragraph 16.5(a) of the Hong Kong Code of Conduct for persons licensed by or registered with the Securities and Futures Commission. (For research published within the first ten days of the month, the disclosure may be based on the month end data from two months’ prior.) J.P. Morgan Broking (Hong Kong) Limited is the liquidity provider for derivative warrants issued by J.P. Morgan International Derivatives Ltd and listed on The Stock Exchange of Hong Kong Limited. An updated list can be found on HKEx website: http://www.hkex.com.hk/prod/dw/Lp.htm. **Japan:** There is a risk that a loss may occur due to a change in the price of the shares in the case of share trading, and that a loss may occur due to the exchange rate in the case of foreign share trading. In the case of share trading, JPMorgan Securities Japan Co., Ltd., will be receiving a brokerage fee and consumption tax (shouhizei) calculated by multiplying the executed price by the commission rate which was individually agreed between JPMorgan Securities Japan Co., Ltd., and the customer in advance. Financial Instruments Firms: JPMorgan Securities Japan Co., Ltd., Kanto Local Finance Bureau (kinsho) No. [82] Participating Association / Japan Securities Dealers Association, The Financial Futures Association of Japan. **Korea:** This report may have been edited or contributed to from time to time by affiliates of J.P. Morgan Securities (Far East) Ltd, Seoul branch. **Singapore:** JPMSI and/or its affiliates may have a holding in any of the securities discussed in this report; for securities where the holding is 1% or greater, the specific holding is disclosed in the Important Disclosures section above. **India:** For private circulation only, not for sale. **Pakistan:** For private circulation only, not for sale. **New Zealand:** This material is issued and distributed by JPMSAL in New Zealand only to persons whose principal business is the investment of money or who, in the course of and for the purposes of their business, habitually invest money. JPMSAL does not issue or distribute this material to members of "the public" as determined in accordance with section 3 of the Securities Act 1978. The recipient of this material must not distribute it to any third party or outside New Zealand without the prior written consent of JPMSAL.

General: Additional information is available upon request. Information has been obtained from sources believed to be reliable but JPMorgan Chase & Co. or its affiliates and/or subsidiaries (collectively J.P. Morgan) do not warrant its completeness or accuracy except with respect to any disclosures relative to JPMSI and/or its affiliates and the analyst’s involvement with the issuer that is the subject of the research. All pricing is as of the close of market for the securities discussed, unless otherwise stated. Opinions and estimates constitute our judgment as of the date of this material and are subject to change without notice. Past performance is not indicative of future results. This material is not intended as an offer or solicitation for the purchase or sale of any financial instrument. The opinions and recommendations herein do not take into account individual client circumstances, objectives, or needs and are not intended as recommendations of particular securities, financial instruments or strategies to particular clients. The recipient of this report must make its own independent decisions regarding any securities or financial instruments mentioned herein. JPMSI distributes in the U.S. research published by non-U.S. affiliates and accepts responsibility for its contents. Periodic updates may be provided on companies/industries based on company specific developments or announcements, market conditions or any other publicly available information. Clients should contact analysts and execute transactions through a J.P. Morgan subsidiary or affiliate in their home jurisdiction unless governing law permits otherwise.

“Other Disclosures” last revised September 29, 2008.