

1QFY08 result – marginally below consensus

27th July 2007

Not Rated

Price	Target Price
Rs156	N.A.

Sensex - 15,776

Price Performance

(%)	1M	3M	6M	12M
Absolute	20	18	39	123
Rel. to Sensex	11	5	29	76

Source: Bloomberg

Stock Details

Sector	Metals
Reuters	SAIL.BO
Bloomberg	SAIL@IN
Equity Capital (Rs mn)	41304
Face Value (Rs)	10
52 Week H/L (Rs)	167/68
Market Cap (Rs bn)	644
Daily Avg Vol (No of shares)	12550728
Daily Avg Turnover (USD mn)	37

Shareholding Pattern (%)

(30th Jun.'07)

Promoters	85.8
FII/NRI	6.4
Institutions	5.3
Private Corp.	0.5
Public	2.0

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SAIL reported marginally below consensus 1QFY08 results. The company reported Net sales of Rs80.395bn (yoy up 8.4%, qoq down 22.6%). However, during 1QFY07 the company had included extraordinary income of Rs5581mn on account of one-time settlement with a major customer. Excluding this one time income, the net sales have gone up by 17.2%. We report all the number hereunder excluding the one time settlement income adjusted in the net sales for 1QFY07. EBITDA stood at 23.8bn (yoy up 33.8%, qoq down 21.2%), Net profit stood at Rs15.25bn (yoy up 84.1%, qoq down 20%). The company reported Adj EPS of Rs3.69 (yoy up 84.1%, qoq down 20%). At CMP of Rs156, the stock is trading at 6.9x consensus FY09 EPS estimate of Rs22.3. We remain positive on the stock.

SAIL reported EBITDA margin of 29.6% during the quarter (yoy up 368bps, qoq up 53bps). The company currently has cash balance of Rs8.9bn and debt of Rs3.3bn. It has projects worth Rs400bn lined up till FY11 of which it intends to spend around Rs30bn this year. The quarter was marked by substantial capital repairs/annual maintenance which has been reflected in rising cost of stores and spares which have gone up by 19.1% yoy (8.4% qoq). The management does not expect any further planned shut down during the year.

Lower production qoq

In 1QFY08, production volumes were lower as compared to 4QFY07 primarily because of shutdown in Plate mills at Bhilai and Rourkela steel plants, and in hot strip mills at Rourkela and Bokaro steel plants.

Saleable steel production

('000t)	1QFY08	1QFY07	% yoy	4QFY07	% qoq
Saleable steel	2,985	2,955	1.0%	3,253	-8.2%

Source: Company

Capex plan

SAIL has plans to invest Rs400bn over the next 4 years to nearly double its hot metal capacity to 25mt from current capacity of 14.6mtpa. SAIL will follow BF-BOF-CC route under this expansion phase. The company will set up at least 3 large blast furnaces and will also set up additional coke oven batteries. It will also enhance its sintering capacity significantly to ensure that it can utilize the fines generated in the course of mining. SAIL will likely invest Rs30bn in FY08. Further, the production will be converted entirely through 100% concast route as compared to 62% currently. Further, the share of value added products is likely to move up from 15% currently to around 20-25% by FY11.

Capex to be funded by internal accruals and debt – no plans to dilute equity

SAIL plans to fund the capex of Rs400bn primarily through internal accruals and market borrowings. It plans to invest Rs250bn through internal accruals of Rs150bn and cash balance of Rs100bn and borrow the balance Rs150bn through market borrowings. The management does not have any plans to dilute equity to raise resources to meet its capital commitment over the next four years. Currently the company has net cash of Rs5.6bn implying nil leverage.

Product mix

Currently, SAIL's product mix is 55% flat products and 45% longs and semis. Semis form 20% share of the total production, which the company plans to reduce to nil by FY11. However, for FY08 semis' contribution in SAIL's product basket will continue to remain at 20%. SAIL has 62% of its operations under continuous casting route, which it plans to increase to 100% by FY10-11. Currently SAIL has negligible exposure to automobile sector. It plans to increase its exposure to autos significantly over the next few years. It also has plans to expand its product range by setting up color coating lines. Thus, addressing the two major gaps in its product portfolio.

Break-up of saleable steel production

('000 tonnes)	FY07	FY10-11E
Plates	2,516	3,608
HR Coils/sheets	3,019	4,862
Railway materials	1,007	1,628
Structurals	755	3,300
CR Coils/sheets	1,132	2,288
Coated products	377	1,056
Rounds/Bars	1,258	5,126
Semis	2,390	-
Pipes	126	132
Total	12,581	22,000

Source: Company, Emkay Research

Raw material linkages

SAIL has 100% captive iron ore mines, while coking coal is primarily imported. The company is currently importing most of its coking coal requirement and has long-term agreements for importing 75% of its coking coal requirements. SAIL also has long-term freight agreements for 70% of its tonnage inputs.

Allocation of captive coking coal mine

In 1QFY08, SAIL has been allotted two coal blocks in Jharkhand. The company expects the mines to be operational within two years, with an initial output of 0.3mtpa, which will be ramped up gradually.

Expanding hot metal output to 25mtpa by FY11 and saleable steel output to 22mtpa

SAIL has plans to expand the hot metal output to 25mtpa and saleable steel output to 22mtpa by FY11. The IISCO plant's capacity will be significantly raised from 0.4mtpa to 2.0mtpa.

Expansion at various plant locations

Plant	Existing capacities	Increase	Final Capacities
Bhilai	4.2	2.3	6.5
Durgapur	1.6	1.2	2.8
Rourkela	1.9	1.9	3.8
Bokaro	3.8	2.7	6.5
IISCO	0.4	2.0	2.4
Total	11.9	10.1	22

Source: Company,
All figures in mtpa

Modernization project completed during the quarter

Plant	Project	Remark
Bhilai Steel Plant	Blast Furnace-7	Relining and increasing capacity by 30%
Rourkela Steel Plant	Coke oven batteries	Modernization
Durgapur Steel Plant	Bloom Caster	Modernization
Bokaro Steel Plant	Mae-West block in HSM	Modernization

Source: Company

Financials

	1QFY08	1QFY07	% yoy	4QFY07	% qoq
Saleable Steel production -('000 tonnes)	2,985	2,955	1.0%	3,253	-8.2%
Net Sales	80,395	74,164	8.4%	103,851	-22.6%
One time income included in sales	-	5,582	-	-	-
Adjusted Net Sales	80,395	68,583	17.2%	103,851	-22.6%
Expenditure					
Purchase & R/M cons	29,908	28,746	4.0%	31,746	-5.8%
Change in stock	-8,451	-8,954	-5.6%	4,936	-271.2%
Total cost of goods sold	21,457	19,792	8.4%	36,681	-41.5%
Adjusted Gross profit	58,938	48,791	20.8%	67,170	-12.3%
Gross margin	73.3%	71.1%	217 bps	64.7%	863 bps
Personnel exp	14,481	11,876	21.9%	16,314	-11.2%
Purchase of power	6,740	6,324	6.6%	6,556	2.8%
Stores and Spares	7,343	6,163	19.1%	6,776	8.4%
Other exp	6,544	6,624	-1.2%	7,289	-10.2%
Total operating exp	35,109	30,987	13.3%	36,934	-4.9%
EBITDA	23,829	17,803	33.8%	30,236	-21.2%
EBITDA margin	29.6%	26.0%	368 bps	29.1%	53 bps
Depreciation & amortization	3,012	2,959	1.8%	2,822	6.7%
EBIT	20,817	14,845	40.2%	27,414	-24.1%
EBIT margin	25.9%	21.6%	425 bps	26.4%	-50 bps
Interest	796	937	-15.0%	555	43.5%
Other income	3,069	1,513	102.9%	2,388	28.5%
PBT after E/o items	23,090	15,421	49.7%	29,247	-21.1%
Provision for tax	7,839	7,138	9.8%	10,228	-23.4%
As a % to PBT	33.9%	46.3%	-26.7%	35.0%	1132 bps
- Current tax	7,724	8,221	-6.1%	10,052	-23.2%
- Deferred tax liability	47	-1,144	-104.1%	121	-61.0%
- Fringe benefit tax	68	61	11.7%	82	-16.9%
- Earlier Years	-	-	-	-26	-
PAT	15,251	8,282	84.1%	19,019	-19.8%
Net margin	19.0%	12.1%	689 bps	18.3%	66 bps
Equity capital	41,304	41,304		41,304	
Reported EPS					
- Basic	3.69	2.01	84.1%	4.60	-19.7%
- Diluted	3.69	2.01	84.1%	4.60	-19.7%
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- Basic	3.69	2.01	84.1%	4.60	-19.8%
- Diluted	3.69	2.01	84.1%	4.60	-19.8%

All figs in Rs mn except for % and per share data

Common Size Ratios

	1QFY08	1QFY07	% yoy	4QFY07	% qoq
Net Sales	100%	100%	-	100%	-
Raw material cost	37%	42%	-471 bps	31%	663 bps
Change in stock	-11%	-13%	254 bps	5%	-1,526 bps
Cost of goods sold	27%	29%	-217 bps	35%	-863 bps
Personal expenses	18%	17%	70 bps	16%	230 bps
Power cost	8%	9%	-84 bps	6%	207 bps
Stores & Spares	9%	9%	15 bps	7%	261 bps
Other expenses	8%	10%	-152 bps	7%	112 bps
EBITDA	30%	26%	368 bps	29%	53 bps
Depreciation	4%	4%	-57 bps	3%	103 bps
Interest expense	1%	1%	-38 bps	1%	46 bps
Other income	4%	2%	161 bps	2%	152 bps
PAT	19%	12%	689 bps	18%	66 bps

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