

# Tata Steel

12 November 2012

Reuters: TISCO.BO; Bloomberg: TATA IN

## Domestic Performance Disappoints; Retain Sell

Tata Steel's (TSL) 2QFY13 EBITDA was 20%/19% below our/street estimates, respectively, following subdued performance in all segments. Standalone EBITDA was 10%/9% below our/street consensus, respectively, due to lower-than-expected realisation. Tata Steel Europe (TSE) reported a negative EBITDA of US\$2/tn versus our expectation of a positive US\$2/tn, despite achieving a 10% higher volume compared to our estimate. We have cut our EBITDA/PAT estimates by 14%/45%, respectively, for FY13E, while FY14E EBITDA/PAT estimates have been reduced by 3%/8%, respectively. We have retained our Sell rating on the stock with a revised target price of Rs329 (down 6% from our earlier TP of Rs351).

**Domestic operations update:** TSL's Indian operations reported a 4% higher volume compared to our expectation, but this was offset by a 3% lower-than-expected realisation. Subdued realisation coupled with higher costs led to 14% lower EBITDA/tn than our estimate, at Rs14,545. It posted 9%/5% YoY jump in production/volume, respectively, on improvement in capacity utilisation, while they were up 7%/9% QoQ, respectively. TSL posted a 6% drop in realisation QoQ due to fall in global steel prices, but up 6% YoY. The above factors resulted in a 9% cut in EBITDA for 2QFY13, YoY as well as QoQ.

**TSE surprises on volume front, but still fails to report positive EBITDA:** Despite achieving a 10% higher volume versus our estimate, TSE reported a negative EBITDA of US\$2/tn versus our estimate of a positive US\$2/tn following larger-than-expected fall in realisation. It reported a 2% YoY drop in volume due to subdued demand, although it was up 7% QoQ. Realisation was down 2% YoY and 7% QoQ, which led to negative EBITDA.

**South-East Asian operations update:** TSL's South-East Asian operations posted 10% YoY and 3% QoQ drop in volume, which was in line with our estimates. Surprisingly, realisation jumped 25% YoY and 7% QoQ in 2QFY13, but this didn't help in EBITDA performance, which was down 14% YoY and 78% QoQ, implying severe cost pressure.

**Other highlights:** Net debt at the end of 2QFY13 stood at Rs551.7bn versus Rs540.2bn at the end of 1QFY13. Net surplus in British Steel Pension (BSP) and Stichting Pensioenfondsen Hoogovens (SPH) schemes were down from £38mn at the end of 1QFY13 to £34mn at the end of 2QFY13. The company has completed triennial valuation of the above schemes and there is a deficit of £500mn, which needs to be bridged over a 15-year period. The company has indicated minimal cash flow in the initial years.

## SELL

**Sector:** Steel

**CMP:** Rs391

**Target Price:** Rs329

**Downside:** 16%

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### Key Data

Current Shares O/S (mn)	971.2
Mkt Cap (Rsbn/US\$bn)	379.3/6.9
52 Wk H / L (Rs)	501/332
Daily Vol. (3M NSE Avg.)	4,931,242

### Price Performance (%)

	1 M	6 M	1 Yr
Tata Steel	(5.2)	(6.4)	(12.7)
Nifty Index	(0.3)	14.3	8.9

Source: Bloomberg

Y/E March (Rsmn)	2QFY12	1QFY13	2QFY13	YoY (%)	QoQ (%)	1HFY12	1HFY13	YoY (%)
<b>Net sales</b>	<b>327,979</b>	<b>338,212</b>	<b>341,327</b>	<b>4.1</b>	<b>0.9</b>	<b>657,981</b>	<b>679,539</b>	<b>3.3</b>
Raw material costs	174,009	164,404	179,019	2.9	8.9	337,970	343,423	1.6
% of sales	53.1	48.6	52.4			51.4	50.5	
Employee costs	39,811	47,825	45,393	14.0	(5.1)	82,127	93,218	13.5
% of sales	12.1	14.1	13.3			12.5	13.7	
Other operating expenses	86,659	91,951	93,814	8.3	2.0	165,811	185,765	12.0
% of sales	26.4	27.2	27.5			25.2	27.3	
<b>EBITDA</b>	<b>27,500</b>	<b>34,033</b>	<b>23,101</b>	<b>(16.0)</b>	<b>(32.1)</b>	<b>72,073</b>	<b>57,134</b>	<b>(20.7)</b>
<b>EBITDA margin (%)</b>	<b>8.4</b>	<b>10.1</b>	<b>6.8</b>			<b>11.0</b>	<b>8.4</b>	
Depreciation	11,088	13,080	13,349	20.4	2.1	22,596	26,429	17.0
Interest costs	7,161	9,690	9,721	35.7	0.3	17,291	19,411	12.3
Other income	1,204	2,894	2,018	67.5	(30.3)	8,817	4,912	(44.3)
<b>PBT</b>	<b>10,456</b>	<b>14,157</b>	<b>2,048</b>	<b>(80.4)</b>	<b>(85.5)</b>	<b>41,003</b>	<b>16,205</b>	<b>(60.5)</b>
Provision for tax	9,065	8,986	6,608	(27.1)	(26.5)	20,295	15,594	(23.2)
Effective tax rate	86.7	63.5	322.6			49.5	96.2	
Exceptional item	-	-	427			33,619	427	(98.7)
<b>PAT before minority interest</b>	<b>1,390</b>	<b>5,170</b>	<b>(4,133)</b>	<b>(397.3)</b>	<b>(179.9)</b>	<b>54,327</b>	<b>1,038</b>	<b>(98.1)</b>
MI and profit of associate cos.	(734)	(808)	(493)			(1,263)	(1,302)	3.1
<b>PAT after MI</b>	<b>2,124</b>	<b>5,979</b>	<b>(3,639)</b>	<b>(271.3)</b>	<b>(160.9)</b>	<b>55,590</b>	<b>2,340</b>	<b>(95.8)</b>
<b>NPM (%)</b>	<b>0.6</b>	<b>1.8</b>	<b>(1.1)</b>			<b>8.3</b>	<b>0.3</b>	
<b>EPS (Rs)</b>	<b>2.2</b>	<b>6.2</b>	<b>(3.7)</b>	<b>(269.1)</b>	<b>(160.9)</b>	<b>57.9</b>	<b>2.4</b>	<b>(95.8)</b>

Source: Company

## Exhibit 1: Financial summary

Y/E March (Rsmn)	FY10	FY11	FY12	FY13E	FY14E
Revenue	1,023,931	1,187,531	1,328,997	1,360,859	1,428,352
YoY (%)	(30.5)	16.0	11.9	2.4	5.0
EBITDA	80,427	159,956	121,034	131,339	173,529
EBITDA margin (%)	7.9	13.5	9.1	9.7	12.1
PAT	(20,092)	89,827	53,898	21,154	53,571
EPS (Rs)	(22.7)	93.6	55.5	21.8	55.1
YoY (%)	(140.7)	(513.2)	(40.7)	(60.8)	153.2
RoE (%)	(1.4)	18.8	12.5	4.8	11.2
RoCE (%)	6.5	12.1	5.6	4.3	8.4
P/E (x)	(17.2)	4.2	7.0	17.9	7.1
EV/ EBITDA (x)	10.1	5.5	7.2	7.0	5.4

Source: Company, Nirmal Bang Institutional Equities Research

## Exhibit 2: Operational highlights

Description	2QFY12	1QFY13	2QFY13	YoY (%)	QoQ (%)	1HFY12	1HFY13	YoY (%)
<b>Domestic performance</b>								
Production (mt)	1.71	1.74	1.87	9.3	7.5	3.46	3.61	4.3
Sales (mt)	1.65	1.59	1.73	5.0	9.1	3.24	3.32	2.3
Realisation (Rs/tn)	49,830	56,167	52,893	6.1	(5.8)	49,590	54,459	9.8
Costs (Rs/tn)	33,023	38,639	38,349	16.1	(0.8)	31,434	38,488	22.4
EBITDA (Rs/tn)	16,807	17,527	14,545	(13.5)	(17.0)	18,157	15,971	(12.0)
<b>Tata Steel Europe</b>								
Sales volume (mt)	3.48	3.21	3.42	(1.7)	6.5	7.03	6.63	(5.7)
Realisation (Rs/tn)	60,790	63,596	59,392	(2.3)	(6.6)	59,300	61,428	3.6
EBITDA (Rs/tn)	1,449	1,923	(124)	(108.5)	(106.4)	2,453	868	(64.6)
Revenue (Rsmn)	211,550	204,144	203,122	(4.0)	(0.5)	416,879	407,266	(2.3)
EBITDA (Rsmn)	5,044	6,174	(423)	(108.4)	(106.8)	17,246	5,752	(66.6)
<b>Tata Steel South-East Asia</b>								
Sales volume (mt)	0.78	0.72	0.70	(10.3)	(2.8)	1.56	1.42	(9.0)
Realisation (Rs/tn)	39,992	46,818	50,061	25.2	6.9	41,369	48,417	17.0
EBITDA (Rs/tn)	314	1,313	302	(3.8)	(77.0)	730	815	11.6
Revenue (Rsmn)	31,194	33,709	35,043	12.3	4.0	64,536	68,752	6.5
EBITDA (Rsmn)	245	946	211	(13.7)	(77.6)	1,139	1,157	1.6

Source: Company, Nirmal Bang Institutional Equities Research

## Exhibit 3: Our estimates versus actual (consolidated)

Description (Rsmn)	2QFY12	1QFY13	2QFY13	YoY (%)	QoQ (%)	2QFY13E	Devi. (%)	2QFY13BBE	Devi. (%)
Revenue	327,979	338,212	341,327	4.1	0.9	326,944	4.4	315,117	8.3
EBITDA	27,500	34,033	23,101	(16.0)	(32.1)	28,870	(20.0)	28,465	(18.8)
PAT	2,124	5,979	(3,639)	(271.3)	(160.9)	2,356	(254.5)	2,976	(222.3)

Source: Company, Bloomberg, Nirmal Bang Institutional Equities Research

## Exhibit 4: Standalone financial performance

Y/E March (Rsmn)	2QFY12	1QFY13	2QFY13	YoY (%)	QoQ (%)	1HFY12	1HFY13	YoY (%)
<b>Net sales</b>	<b>82,119</b>	<b>89,080</b>	<b>91,506</b>	<b>11.4</b>	<b>2.7</b>	<b>160,722</b>	<b>180,586</b>	<b>12.4</b>
Raw material costs	23,258	25,509	29,671	27.6	16.3	43,580	55,179	26.6
% of sales	28.3	28.6	32.4			27.1	30.6	
Employee costs	6,908	8,591	8,300	20.2	(3.4)	13,778	16,891	22.6
% of sales	8.4	9.6	9.1			8.6	9.4	
Other operating expenses	24,256	27,182	28,373	17.0	4.4	44,518	55,555	24.8
% of sales	29.5	30.5	31.0			27.7	30.8	
<b>EBITDA</b>	<b>27,698</b>	<b>27,798</b>	<b>25,162</b>	<b>(9.2)</b>	<b>(9.5)</b>	<b>58,846</b>	<b>52,960</b>	<b>(10.0)</b>
EBITDA margin (%)	33.7	31.2	27.5			36.6	29.3	
Depreciation	2,871	3,544	3,913	36.3	10.4	5,724	7,457	30.3
Interest costs	2,343	4,544	4,539	93.8	(0.1)	6,879	9,084	32.0
Other income	236	1,519	2,397	916.9	57.8	2,799	3,916	39.9
<b>PBT</b>	<b>22,720</b>	<b>21,229</b>	<b>19,107</b>	<b>(15.9)</b>	<b>(10.0)</b>	<b>49,042</b>	<b>40,336</b>	<b>(17.8)</b>
Provision for tax	7,767	7,663	5,695	(26.7)	(25.7)	17,005	13,358	(21.4)
Effective tax rate (%)	34.2	36.1	29.8			34.7	33.1	
Exceptional item	-	-	96			5,110	96	
<b>PAT</b>	<b>14,952</b>	<b>13,566</b>	<b>13,508</b>	<b>(9.7)</b>	<b>(0.4)</b>	<b>37,147</b>	<b>27,074</b>	<b>(27.1)</b>
NPM (%)	18.2	15.2	14.8			23.1	15.0	
<b>EPS (Rs)</b>	<b>15.6</b>	<b>14.0</b>	<b>13.9</b>	<b>(10.8)</b>	<b>(0.4)</b>	<b>38.7</b>	<b>27.9</b>	<b>(28.0)</b>

Source: Company

## Exhibit 5: Subsidiaries' financial performance

Y/E March (Rsmn)	2QFY12	1QFY13	2QFY13	YoY (%)	QoQ (%)	1HFY12	1HFY13	YoY (%)
<b>Net sales</b>	<b>245,860</b>	<b>249,132</b>	<b>249,822</b>	<b>1.6</b>	<b>0.3</b>	<b>497,259</b>	<b>498,953</b>	<b>0.3</b>
Raw material costs	150,751	138,895	149,348	(0.9)	7.5	294,390	288,243	(2.1)
% of sales	61.3	55.8	59.8			59.2	57.8	
Employee costs	32,904	39,234	37,094	12.7	(5.5)	68,349	76,327	11.7
% of sales	13.4	15.7	14.8			13.7	15.3	
Other operating expenses	62,403	64,769	65,442	4.9	1.0	121,292	130,210	7.4
% of sales	25.4	26.0	26.2			24.4	26.1	
<b>EBITDA</b>	<b>(197)</b>	<b>6,235</b>	<b>(2,061)</b>	<b>944.3</b>	<b>(133.1)</b>	<b>13,227</b>	<b>4,173</b>	<b>(68.4)</b>
EBITDA margin (%)	(0.1)	2.5	(0.8)			2.7	0.8	
Depreciation	8,217	9,536	9,437	14.8	(1.0)	16,872	18,973	12.5
Interest costs	4,818	5,146	5,182	7.5	0.7	10,411	10,328	(0.8)
Other income	969	1,375	(379)	(139.1)	(127.6)	6,018	996	(83.5)
<b>PBT</b>	<b>(12,264)</b>	<b>(7,072)</b>	<b>(17,059)</b>	<b>39.1</b>	<b>141.2</b>	<b>(8,039)</b>	<b>(24,131)</b>	<b>200.2</b>
Provision for tax	1,298	1,323	933	(28.1)	(29.5)	3,290	2,256	(31.4)
Effective tax rate (%)	(10.6)	(18.7)	(5.5)			(40.9)	(9.4)	
Exceptional item	-	-	331			28,509	331	
<b>PAT before MI</b>	<b>(13,562)</b>	<b>(8,395)</b>	<b>(17,662)</b>	<b>30.2</b>	<b>110.4</b>	<b>17,181</b>	<b>(26,057)</b>	<b>(251.7)</b>
MI and profit of associates	(734)	(808)	(493)			(1,263)	(1,302)	
<b>PAT after MI</b>	<b>(12,828)</b>	<b>(7,587)</b>	<b>(17,168)</b>	<b>33.8</b>	<b>126.3</b>	<b>18,443</b>	<b>(24,755)</b>	<b>(234.2)</b>
NPM (%)	(5.2)	(3.0)	(6.9)			3.7	(5.0)	
<b>EPS (Rs)</b>	<b>(13.4)</b>	<b>(7.8)</b>	<b>(17.7)</b>	<b>32.7</b>	<b>127.9</b>	<b>19.2</b>	<b>(25.5)</b>	<b>(232.8)</b>

Source: Company

### Change in our earnings estimates

We have lowered our domestic volume and realisation assumptions after factoring in the current price trend and a slight delay in commissioning of a new facility, although we have retained our FY14E volume estimate. We have also lowered our cost assumption following moderation in international coking coal prices. The above factors led to 10%/2% cut in EBITDA/tn of domestic operations for FY13E/FY14E, respectively, while PAT estimates have been reduced by 15%/3%, respectively, for the same period. We have also revised our realisation and cost assumptions for the company's European and South-East Asian operations following the current price trend. Overall, we have cut our consolidated EBITDA estimates by 14%/3% for FY13E/FY14E, respectively, while PAT estimates have been reduced by 45%/8%, respectively, for the same period.

### Exhibit 6: Change in Tata Steel's earnings estimates

Description	Earlier assumptions		New assumptions		Change (%)	
	FY13E	FY14E	FY13E	FY14E	FY13E	FY14E
<b>Standalone operations</b>						
Steel production (mt)	7.77	8.93	7.54	8.93	(2.9)	-
Steel volume (mt)	7.47	8.75	7.15	8.75	(4.3)	-
Realisation (Rs/tn)	54,521	51,970	53,083	50,838	(2.6)	(2.2)
Total costs (Rs/tn)	36,595	35,448	36,879	34,646	0.8	(2.3)
EBITDA (Rs/tn)	17,926	16,522	16,205	16,192	(9.6)	(2.0)
<b>Std. financials (Rsmn)</b>						
Net sales	407,136	454,541	379,467	444,641	(6.8)	(2.2)
EBITDA	133,862	144,506	115,841	141,620	(13.5)	(2.0)
PAT	66,370	69,008	56,330	66,688	(15.1)	(3.4)
<b>Overseas operations</b>						
<b>Volume (mt)</b>						
Tata Steel Europe (TSE)	13.31	14.00	13.43	14.00	0.9	-
South East Asian operations	3.21	3.32	3.08	3.32	(4.0)	-
<b>Realisation (US\$/tn)</b>						
Tata Steel Europe	1,096	1,070	1,092	1,025	(0.4)	(4.2)
South East Asian operations	848	846	872	840	2.9	(0.7)
<b>Revenue (US\$mn)</b>						
Tata Steel Europe	14,578	14,980	14,653	14,350	0.5	(4.2)
South East Asian operations	2,723	2,809	2,680	2,789	(1.6)	(0.7)
<b>EBITDA (US\$mn)</b>						
Tata Steel Europe	299	547	279	509	(6.7)	(7.0)
South East Asian operations	67	80	54	66	(18.9)	(16.7)
<b>EBITDA (US\$/tn)</b>						
Tata Steel Europe	22.4	39.1	20.7	36.4	(7.5)	(7.0)
South East Asian operations	20.8	24.0	17.6	20.0	(15.4)	(16.7)
<b>Consol. financials (Rsmn)</b>						
Net sales	1,400,799	1,457,111	1,360,859	1,428,352	(2.9)	(2.0)
EBITDA	153,211	178,678	131,339	173,529	(14.3)	(2.9)
PAT	38,640	58,004	21,154	53,571	(45.3)	(7.6)

Source: Company, Nirmal Bang Institutional Equities Research

## Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
24 June 2011	Buy	557	756
16 August 2011	Sell	475	458
7 October 2011	Sell	400	371
11 November 2011	Sell	447	358
9 January 2012	Sell	363	341
10 February 2012	Sell	475	337
21 May 2012	Sell	400	364
14 August 2012	Sell	406	351
12 November 2012	Sell	391	329

## Disclaimer

### Stock Ratings Absolute Returns

BUY > 15%

HOLD 0-15%

SELL < 0%

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