

RESULT UPDATE ✓

Tata Steel (TISCO)

WHAT'S CHANGED...

PRICE TARGET.....	Unchanged at Rs 340
EPS (FY10E).....	Changed to Rs 20.2 from Rs 13.4
EPS (FY11E).....	Changed to Rs 44.8 from Rs 28.8
RATING.....	Unchanged

Current Price Rs 424.3	Target Price Rs 340
Potential upside -20 %	Time Frame 12 months

UNDERPERFORMER

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Corus continues to disappoint....

Tata Steel reported disappointing consolidated Q1FY10 results, with a net loss of Rs 2208 crore as fears on the Corus performance came true. Net sales were down 46.7% YoY to Rs 23180.5 crore. Poor consolidated results were a result of slower demand recovery in Europe leading to low capacity utilisation at Corus and lower reduction in fixed costs than anticipated. The recovery in Europe is expected to take its own sweet time. We remain cautious on the stock as EPS is expected to remain subdued due to uncertain outlook and equity dilution through GDR issue and CCPS conversion.

Highlight of the quarter

Net sales dropped 46.7% YoY to Rs 23180.5 crore due to an ~37% drop in sales volume YoY and 15.4% YoY drop in average realisation. The EBITDA margin fell by 60 bps on a sequential basis. The loss of Rs 2208 crore was due to almost nil reduction in total expenses/tonne on a sequential basis due to old contracted raw material still lying with the company. Total expenses/tonne stood at Rs 42872 in Q1FY10 as compared to Rs 43996 in Q4FY09.

Valuations

At the current market price of Rs 424.3, the stock is trading at 9.5x FY11E EPS of Rs 44.8 and 1.8x FY11E adjusted BV of Rs 246.1. With Corus expected to weigh on the consolidated profits in FY10E, we are shifting our valuation base to FY11 and value the company at 7.5x FY11E EPS and 1.4x FY11E adj. BV. We maintain our **UNDERPERFORMER** rating on the stock with a target price of Rs 340.

Stock Data

Market Cap (Rs Cr)	31007.8
Debt(FY09, Rs Cr)	59900.5
Cash(FY09, Rs Cr)	11383.3
EV (Rs Cr)	79525.0
52 Week H/L (Rs)	785/138
Equity Capital (Rs Cr)	730.0
Face Value (Rs)	10.0
MF Holding (%)	3.6
FII Holding (%)	14.5

Price Performance (%)

	1M	3M	6M	12M
Tata Steel	-6	14	155	-23
JSW Steel	4	29	277	-5
SAIL	-7	1	118	12

Exhibit 1: Key Financials – Consolidated

	Q1FY10A	Q1FY10E	Q1FY09	Q4FY09	YoY Gr. (%)	QoQ Gr. (%)	FY09	FY10E	FY11E
Net Sales	23180.5	18531.3	43508.3	24788.1	-46.7	-6.5	145686.3	101031.8	119726.6
EBITDA	-29.9	1640.8	6987.6	33.0	PL	PL	18127.7	10030.2	13390.9
EBITDA Margin (%)	-0.1	0.1	16.1	0.1	-1620 bps	-60 bps	12.4	9.9	11.2
Depreciation	1089.0	1047.9	1105.0	928.3	-1.4	17.3	4265.4	4218.3	4338.3
Interest	881.9	837.8	824.3	911.4	7.0	-3.2	3290.2	3363.0	3102.0
Other Income	203.9	200.0	84.4	97.0	141.7	110.1	1908.6	700.0	500.0
Reported Adj. PAT	-2208.7	-399.8	4204.3	-4839.0	PL	NA	4950.9	1788.5	3974.4
EPS (Rs)	-30.3	-5.5	57.6	-66.3	PL	NA	67.8	20.2	44.8
Valuation									
PE (x)							6.3	21.0	9.5
Target PE (x)							5.0	16.9	7.6
EV to EBITDA (x)							4.0	7.7	5.9
Price to book (x) (Adj.)							2.4	2.0	1.8
RoNW (%)							17.0	5.6	11.4
RoCE (%)							15.0	6.3	10.0

Source: Company, ICICIdirect.com Research

Overseas subsidiaries continue to struggle

Tata Steel's India operations have continued to do well despite the effects of the the global economic crisis due to sound operations, higher capacity utilisation levels, robust domestic demand and high backward and forward integration ensuring best EBITDA margins in the Indian steel industry. However, overseas subsidiaries have continued to struggle with Tata Steel Europe posting a loss at the EBITDA level due to higher raw material and fixed costs.

Exhibit 2: Tata Steel group performance

Particulars (Rs Crore)	Tata Steel- India	Tata Steel- Europe	NSA	Tata Steel- Thailand	Tata Steel - Group
Deliveries (MT)	1.4	3.3	0.5	0.3	5.4
Turnover	5554.0	15228.0	2431.0	637.0	23292.0
Realisation/tonne (Rs)	39671.6	46145.5	45018.5	24037.7	42792.6
EBITDA	1742.2	-1853.0	41.0	4.0	-29.9
EBITDA Margin (%)	31.4	-12.2	1.7	0.6	-0.1
EBITDA/tonne (Rs)	12444.3	-5615.2	759.3	150.9	-54.9

Source: Company, ICICIdirect.com Research

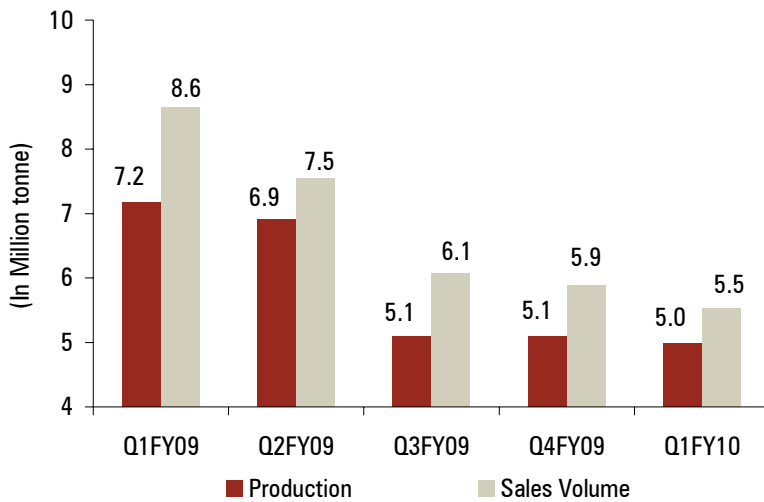
Exhibit 3: Per tonne analysis - Consolidated

Rs/Tonne	Q1FY10	Q1FY09	YoY %
Net Realization	42611.2	54385.4	-21.6
Total Cost	42871.6	45650.9	-6.1
Stock Adjustment	2452.6	-2009.3	
Raw Material Consumed	12963.6	14686.6	-11.7
Employee Expenses	7284.1	6126.5	18.9
Purchase of power	1776.5	2018.8	-12.0
Freight & Handling	2125.7	2155.6	-1.4
Other Expenses	9837.9	10128.7	-2.9
EBITDA	-54.9	8734.5	PL

Source: Company, ICICIdirect.com Research

- **Subdued sales** – The company suffered a 37% YoY drop in sales volume to ~5.4 MT due to a drop in sales of ~3 MT YoY at Corus. Capacity utilisation at Corus remained at ~52% levels in Q1FY10. This was due to subdued demand and mothballing of several plants including Teeside cast products, where a consortium of buyers walked out of their buying agreement.
- **Realisation/tonne** dropped ~22% YoY due to lower steel prices across the globe. Prices have stabilised at the global level and shown improvement in Indian domestic markets of late.
- **Expenses/tonne remained high** – Despite the management's proactive measures to reduce expenses through the cost savings programme at Europe, expenses/tonne dropped by a meagre 6.1% YoY to Rs 42871. This was due to higher raw material cost as the previous year's contract quantities of iron ore and coking coal still remained as inventory with Corus. Also, savings on employee expenses were marginal. With lower sales volumes, employee costs/tonne increased by ~19% YoY.
- **EBITDA neutral** – Due to subdued realisations and lower-than-expected reduction in total expenses, the company remained EBITDA neutral in Q1FY10.

Exhibit 4: Production & sales volume



Source: Company, ICICIdirect.com Research

Exhibit 5: Tata Steel Europe performance

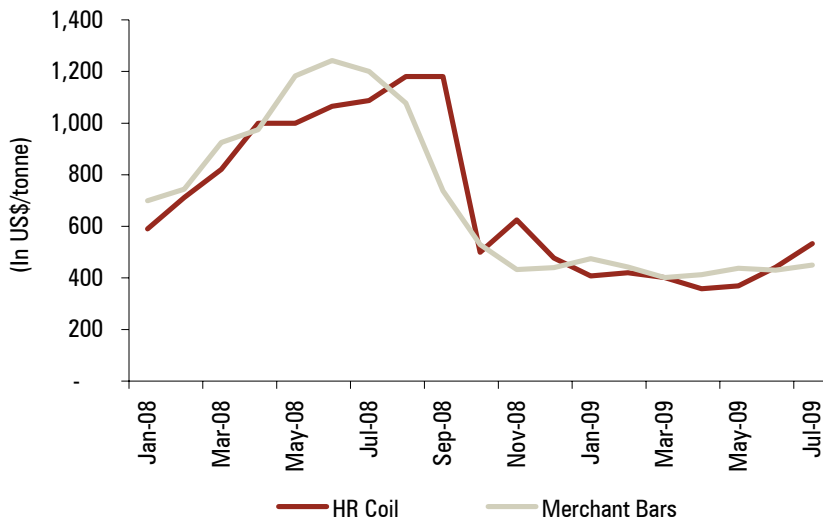
Particulars (US\$ Mn)	Q1FY10	Q1FY09	YoY Gr %	FY10E	FY11E
Liquid Steel production	2.8	5.2	-46.2	13	15
Steel Deliveries	3.3	6.3	-47.6	14.8	17
Turnover	3179.0	6880.0	-53.8	13659	17266.3
Realisation/tonne (US\$)	963.3	1092.1	-11.8	922.9	1015.7
EBITDA	-387.0	777	-149.8	-35.5	652.8
EBITDA Margin (%)	-12.2	11.3		-0.3	3.8
EBITDA/tonne (US\$)	-117.3	123.3	-195.1	-2.4	38.4

Source: Company, ICICIdirect.com Research

Corus expected to show slow recovery

Sales volumes at the group level have dipped continuously for the last three quarters due to severe demand destruction in Europe and lower sales volume in Corus. With European markets starting to stabilise and demand starting to improve, volumes at Corus are expected to improve, going forward. Tata Steel's management has set aggressive capacity utilisation targets of close to 80% by FY10 end. We expect the recovery in Europe to take its own sweet time and Corus to show slow recovery. We expect Corus to achieve 65% capacity utilisation for the full year FY10E leading to 13 MT of liquid steel production and steel deliveries of ~14.8 MT. We expect a negative EBITDA of US\$35.5 million for FY10E. However, FY11E is expected to generate higher sales volume of 17 MT and positive EBITDA of US\$652 million.

Exhibit 6: International steel price trend



Source: Crisil Research Pro, ICICIdirect.com Research

Exhibit 7: Earnings revision (Consolidated)

	FY10E		FY11E	
	Current	Previous	Current	Previous
Net Sales	101031.8	76529.6	119726.6	92940.8
EBITDA	10030.2	9465.8	13390.9	11181.0
PAT	1788.5	1187	3974.4	2556.5
EPS	20.2	13.4	44.8	28.8

Source: Company, ICICIdirect.com Research

Valuations

We have shifted our valuation base to FY11E as there is better clarity on volume and realisations in FY11E. We are valuing the company using the P/E and P/BV methodology. We have also used EV/EBITDA to gauge the fair value of the stock as compared to global peers. We have factored in an ~45-50% earnings uptick in our earlier earnings forecast for FY10E and FY11E (Exhibit 7) due to higher than expected blended realisations at Corus, conditions gradually improving in Europe, cost savings that are expected to continue through management initiatives and stability in Indian operations.

Currently, the stock is trading at of 9.8x FY11E EPS and 1.8x FY11E adjusted BV. We are assigning a multiple of 7.5x FY11E EPS of Rs 44.8 to arrive at a target price of Rs 336 for the stock. At 1.4x FY11E adjusted BV of Rs 246.1, we have arrived at a price target of Rs 344.5 for the stock. We are maintaining our target price of **Rs 340** and continue with our **UNDERPERFORMER** rating on the stock.

We have also valued the company using the EV/EBITDA methodology. We have assigned a multiple of 6x to Tata Steel's standalone FY11E EBITDA, lower than the global average (7x) due to high debt on books, which would keep the overall profitability muted, going forward. As Tata Steel's subsidiaries are expected to make meaningful EBITDA only in FY11E through gradual recovery, we value them conservatively at 3x their FY11E combined EBITDA (discount of ~55% to global average). We have derived a fair value of Rs 337.7 for the stock through EV/EBITDA methodology.

Exhibit 8: EV/EBITDA valuation

(Rs Crore)	FY11E
Tata Steel EBITDA	10085.0
EV/EBITDA(x)	6.0
TISCO EV	60509.7
Corus & Subs EBITDA	3806.0
EV/EBITDA(x)	3.0
Corus & Subs EV	11417.9
Total EV	71927.6
Total Debt	51700.5
Cash	10612.6
Minority Interest	894.9
Market Cap	29944.8
No. of Shares	88.7
Price per Share (Rs)	337.7
Fair Value (Rs)	337.7

Source: Company, ICICIdirect.com Research

Exhibit 9: Global peers valuation

Company	P/E		P/BV		EV/EBITDA	
	2009	2010	2009	2010	2009	2010
Arcelor Mittal	NA	14.1	1.0	0.9	14.4	7.4
US Steel	NA	40.7	1.4	1.4	NA	8.0
Nucor	NA	15.2	1.9	1.8	47.2	7.1
Severstal	NA	13.7	1.0	0.9	13.9	6.1
Gerdau	25.8	11.8	1.3	1.2	11.0	7.0
JFE Holdings	56.9	11.9	1.3	1.2	11.0	6.9
Nippon	1843.1	16.2	1.4	1.3	14.2	8.0
Baoshan	21	13.5	1.2	1.1	7.3	5.7
Angang Steel	34	14.4	1.5	1.4	11.1	6.9
Average		13.9	1.3	1.2	11.8	7.0

Source: Bloomberg, ICICIdirect.com Research

Exhibit 10: Valuation matrix (Consolidated)

	Sales (Rs Cr)	EPS (Rs)	PE (x)	P/BV Adj. (x)	EV/EBITDA (x)	RoNW(%)	RoCE(%)
FY09	145686.3	60.4	6.3	2.4	4.0	17.0	15.0
FY10E	101031.8	20.2	21.0	2.0	7.7	5.6	6.3
FY11E	119726.6	44.8	9.5	1.8	5.9	11.4	10.0

Source: Company, ICICIdirect.com Research

ICICIdirect.com Coverage Universe

Exhibit 11: Valuation Matrix

Adhunik Metaliks					Sales (Rs Cr)	EPS (Rs)	PE (x)	EV/EBITDA (x)	RoNW(%)	RoCE(%)
Idirect Code	ADHMET	CMP (Rs)	99.7	FY09	1270.3	5.1	19.5	9.1	13.3	9.9
		Target (Rs)	132.0	FY10E	1382.4	8.0	12.4	6.9	14.3	12.5
MCap (Rs Cr)	1006.5	Upside (%)	32.4	FY11E	1555.8	11.6	8.6	6.1	17.7	14.9
JSW Steel					Sales (Rs Cr)	EPS (Rs)	PE (x)	EV/EBITDA (x)	RoNW(%)	RoCE(%)
Idirect Code	JINVIJ	CMP (Rs)	691.4	FY09	16081.5	14.7	47.0	9.5	3.0	9.1
		Target (Rs)	576.0	FY10E	18170.9	51.1	13.5	9.0	9.8	9.4
MCap (Rs Cr)	13600.4	Upside (%)	-16.7	FY11E	20292.8	60.6	11.4	7.2	10.7	10.6
Usha Martin					Sales (Rs Cr)	EPS (Rs)	PE (x)	EV/EBITDA (x)	RoNW(%)	RoCE(%)
Idirect Code	USHBEL	CMP (Rs)	54.3	FY09	2949.8	7.4	7.3	5.6	16.3	14.4
		Target (Rs)	60.0	FY10E	2719.3	7.3	7.4	5.5	14.7	12.9
MCap (Rs Cr)	1329.8	Upside (%)	10.5	FY11E	3955.4	12.3	4.4	3.9	20.1	18.2
Visa Steel					Sales (Rs Cr)	EPS (Rs)	PE (x)	EV/EBITDA (x)	RoNW(%)	RoCE(%)
Idirect Code	VISST	CMP (Rs)	33.9	FY09	1035.0	-6.1	NA	NA	NA	NA
		Target (Rs)	25.0	FY10E	1037.6	5.7	6.0	10.1	18.2	8.7
MCap (Rs Cr)	355.3	Upside (%)	-26.1	FY11E	1362.8	7.3	4.6	4.4	19.0	12.8
Tata Steel - Cons					Sales (Rs Cr)	EPS (Rs)	PE (x)	EV/EBITDA (x)	RoNW(%)	RoCE(%)
Idirect Code	TISCO	CMP (Rs)	424.3	FY09	145686.3	67.8	6.3	4.0	17.0	15.0
		Target (Rs)	340.0	FY10E	101031.8	20.2	21.0	7.7	5.6	6.3
MCap (Rs Cr)	31007.8	Upside (%)	-19.9	FY11E	119726.6	44.8	9.5	5.9	11.4	10.0
SAIL					Sales (Rs Cr)	EPS (Rs)	PE (x)	EV/EBITDA (x)	RoNW(%)	RoCE(%)
Idirect Code	SAIL	CMP (Rs)	162.6	FY09	43639.7	14.9	10.9	6.7	22.2	21.0
		Target (Rs)	185.0	FY10E	42291.0	15.7	10.4	5.9	19.7	18.5
MCap (Rs Cr)	70361.4	Upside (%)	13.8	FY11E	48072.7	16.8	9.7	6.2	18.2	16.2
Sesa Goa					Sales (Rs Cr)	EPS (Rs)	PE (x)	EV/EBITDA (x)	RoNW(%)	RoCE(%)
Idirect Code	SESGOA	CMP (Rs)	212.6	FY09	4959.1	25.3	8.4	5.9	42.2	51.9
		Target (Rs)	250.0	FY10E	4990.1	25.0	8.5	6.5	28.6	31.4
MCap (Rs Cr)	19905.3	Upside (%)	17.6	FY11E	5842.1	30.5	7.0	4.5	26.4	29.7

Source: Company, ICICIdirect.com Research

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