March 15, 2011

COMPANY UPDATE

Tata Steel (TISC.BO)

Buy

Equity Research

Jamshedpur plant visit: Expansion project on track; Conviction Buy

What's changed

We visited Tata Steel's integrated plant at Jamshedpur, Jharkhand; our key takeaways include: **1) Execution of growth projects is on track:** 2.9 mtpa capacity expansion project is on schedule with phased commissioning of various facilities from Aug 2011. The pace of project execution is impressive, with about 30,000 people engaged at the project site. More than the scale, the complexity of managing a project of this size within the constraints of space and resources is notable. **2) Downstream expansion to maintain share of value-added products in the medium term:** The downstream 0.6 mtpa continuous annealing and processing line (JV with Nippon Steel) for auto-grade cold-rolled steel is making good progress and is scheduled to be commissioned by 2013. Capacity expansion at Tinplate subsidiary and JV with BlueScope would further strengthen the downstream presence, in our view. **3) Strong focus on achieving higher raw material integration:** Tata Steel remains committed to maintaining 50% self sufficiency in coking coal and 100% in iron ore, post expansion. As such, the focus is on commencing operations at developmental mines at Ankua, Kotre, etc., over the next 3-5 yrs.

Implications

The plant visit reaffirms our positive view on Tata Steel India operations, which hinges upon sustained strong profitability (23% FY10-FY13E EBITDA CAGR, 72% of consolidated EBITDA), driven by strong volume growth, product mix geared to high margin value added products (market leader in auto-grade steel) and highest vertical integration among peers.

Valuation

We reiterate Buy (on CL) on Tata Steel. We fine-tune our FY12E-FY13E EPS and maintain our 12-m P/B-based TP of Rs761, implying 27% potential upside. The stock is currently trading at 4.8X FY12E EV/EBITDA, at 23% disc to the mid-cycle of 6.2X and 25% disc to peers.

Key risks

Delay in project execution, higher-than-expected increase in coal costs.

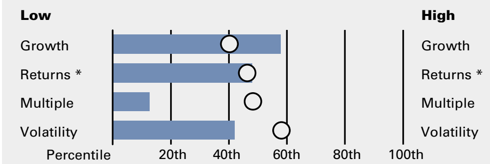
INVESTMENT LIST MEMBERSHIP

Asia Pacific Buy List

Asia Pacific Conviction Buy List

Coverage View: Neutral

Investment Profile

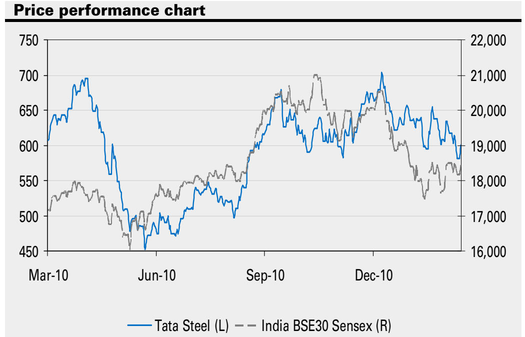


* Returns = Return on Capital. For a complete description of the investment profile measures please refer to the disclosure section of this document.

Key data	Current
Price (Rs)	601.05
12 month price target (Rs)	761.00
Market cap (Rs mn / US$ mn)	577,083.7 / 12,754.6
Foreign ownership (%)	19.5

	3/10	3/11E	3/12E	3/13E
EPS (Rs) New	**(3.93)**	**70.16**	**82.54**	**113.82**
EPS revision (%)	0.0	0.0	0.1	0.0
EPS growth (%)	(103.2)	1,884.5	17.6	37.9
EPS (dil) (Rs) New	**(24.27)**	**64.86**	**76.64**	**105.69**
P/E (X)	NM	8.6	7.3	5.3
P/B (X)	2.2	1.7	1.5	1.2
EV/EBITDA (X)	10.6	5.9	4.8	3.7
Dividend yield (%)	2.4	2.9	3.1	3.8
ROE (%)	(8.0)	23.1	22.6	25.8
CROCI (%)	4.4	8.6	10.2	11.9

Price performance chart



Share price performance (%)	3 month	6 month	12 month
Absolute	(6.9)	0.7	(1.0)
Rel. to India BSE30 Sensex	(0.0)	5.7	(7.9)

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 3/14/2011 close.

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Tata Steel: Summary Financials

Profit model (Rs mn)	3/10	3/11E	3/12E	3/13E
Total revenue	**1,023,931.2**	**1,151,765.5**	**1,386,806.9**	**1,456,724.4**
Cost of goods sold	(831,024.1)	(872,678.2)	(1,044,323.2)	(1,058,209.1)
SG&A	(165,668.8)	(173,887.2)	(212,390.8)	(229,066.5)
R&D	0.0	0.0	0.0	0.0
Other operating profit/(expense)	8,970.8	4,024.8	5,424.6	6,493.6
EBITDA	**81,126.4**	**164,382.5**	**203,474.9**	**249,987.2**
Depreciation & amortization	(44,917.3)	(55,157.7)	(67,957.4)	(74,044.8)
EBIT	**36,209.1**	**109,224.8**	**135,517.5**	**175,942.4**
Interest income	0.0	1,139.5	3,174.8	3,554.8
Interest expense	(30,220.6)	(29,277.7)	(31,362.1)	(31,499.6)
Income/(loss) from uncons. subs.	1,268.6	0.0	0.0	0.0
Others	11,158.7	12,894.1	8,405.7	7,546.7
Pretax profits	**18,415.8**	**93,980.7**	**115,735.9**	**155,544.3**
Income tax	(21,518.4)	(30,846.5)	(36,066.1)	(45,016.3)
Minorities	(152.4)	231.9	(425.4)	(1,247.2)
Net income pre-preferred dividends	**(3,255.0)**	**63,366.1**	**79,244.4**	**109,280.9**
Preferred dividends	0.0	0.0	0.0	0.0
Net income (pre-exceptionals)	**(3,255.0)**	**63,366.1**	**79,244.4**	**109,280.9**
Post-tax exceptionals	(16,837.2)	0.0	0.0	0.0
Net income	**(20,092.2)**	**63,366.1**	**79,244.4**	**109,280.9**
EPS (basic, pre-except) (Rs)	(3.93)	70.16	82.54	113.82
EPS (basic, post-except) (Rs)	(24.27)	70.16	82.54	113.82
EPS (diluted, post-except) (Rs)	(24.27)	64.86	76.64	105.69
DPS (Rs)	14.23	17.65	18.70	22.83
Dividend payout ratio (%)	(58.6)	25.2	22.7	20.1
Free cash flow yield (%)	(3.7)	(3.0)	4.4	10.7

Growth & margins (%)	3/10	3/11E	3/12E	3/13E
Sales growth	(30.5)	12.5	20.4	5.0
EBITDA growth	(55.4)	102.6	23.8	22.9
EBIT growth	(74.0)	201.7	24.1	29.8
Net income growth	(141.7)	415.4	25.1	37.9
EPS growth	(136.7)	389.1	17.6	37.9
Gross margin	18.8	24.2	24.7	27.4
EBITDA margin	7.9	14.3	14.7	17.2
EBIT margin	3.5	9.5	9.8	12.1

Cash flow statement (Rs mn)	3/10	3/11E	3/12E	3/13E
Net income pre-preferred dividends	(3,255.0)	63,366.1	79,244.4	109,280.9
D&A add-back	44,917.3	55,157.7	67,957.4	74,044.8
Minorities interests add-back	152.4	(231.9)	425.4	1,247.2
Net (inc)/dec working capital	46,465.2	(6,467.3)	(2,738.0)	(3,272.1)
Other operating cash flow	(13,177.7)	(12,894.1)	(8,405.7)	(7,546.7)
Cash flow from operations	**75,102.2**	**98,930.6**	**136,483.6**	**173,754.1**
Capital expenditures	(69,471.5)	(96,164.4)	(91,575.2)	(92,012.3)
Acquisitions	0.0	0.0	0.0	0.0
Divestitures	0.0	0.0	0.0	0.0
Others	19,453.9	0.0	0.0	0.0
Cash flow from investments	**(50,017.6)**	**(96,164.4)**	**(91,575.2)**	**(92,012.3)**
Dividends paid (common & pref)	(13,209.1)	(15,938.3)	(17,955.5)	(21,916.1)
Inc/(dec) in debt	(26,866.3)	31,358.4	6,118.4	2,000.0
Common stock issuance (repurchase)	24,464.7	43,770.0	0.0	0.0
Other financing cash flows	(3,079.4)	0.0	0.0	0.0
Cash flow from financing	**(18,690.1)**	**59,190.1**	**(11,837.1)**	**(19,916.1)**
Total cash flow	**6,394.5**	**61,956.2**	**33,071.3**	**61,825.6**

Balance sheet (Rs mn)	3/10	3/11E	3/12E	3/13E
Cash & equivalents	67,878.1	129,834.3	162,905.6	224,731.2
Accounts receivable	116,239.5	141,998.5	170,976.2	179,596.2
Inventory	186,866.4	174,535.6	174,053.9	176,368.2
Other current assets	67,693.9	67,693.9	67,693.9	67,693.9
Total current assets	**438,677.9**	**514,062.3**	**575,629.6**	**648,389.5**
Net PP&E	457,958.3	498,965.0	522,582.9	540,550.4
Net intangibles	146,566.7	146,566.7	146,566.7	146,566.7
Total investments	54,177.9	67,072.0	75,477.7	83,024.4
Other long-term assets	0.0	0.0	0.0	0.0
Total assets	**1,097,380.8**	**1,226,666.0**	**1,320,256.8**	**1,418,530.9**
Accounts payable	119,259.9	126,220.9	151,978.8	159,641.0
Short-term debt	3,684.0	23,323.0	23,323.0	23,323.0
Other current liabilities	180,567.4	180,567.4	180,567.4	180,567.4
Total current liabilities	**303,511.3**	**330,111.3**	**355,869.3**	**363,531.5**
Long-term debt	527,319.5	539,038.9	545,157.3	547,157.3
Other long-term liabilities	29,570.4	29,570.4	29,570.4	29,570.4
Total long-term liabilities	556,889.9	568,609.3	574,727.7	576,727.7
Total liabilities	**860,401.2**	**898,720.6**	**930,596.9**	**940,259.1**
Preferred shares	**0.0**	**0.0**	**0.0**	**0.0**
Total common equity	**228,138.9**	**319,336.7**	**380,625.6**	**467,990.4**
Minority interest	8,840.7	8,608.8	9,034.2	10,281.4
Total liabilities & equity	**1,097,380.8**	**1,226,666.0**	**1,320,256.8**	**1,418,530.9**
BVPS (Rs)	**275.57**	**353.59**	**396.43**	**487.43**

Ratios	3/10	3/11E	3/12E	3/13E
CROCI (%)	4.4	8.6	10.2	11.9
ROE (%)	(8.0)	23.1	22.6	25.8
ROA (%)	(1.7)	5.5	6.2	8.0
ROACE (%)	2.3	11.2	12.7	16.1
Inventory days	88.6	75.6	60.9	60.4
Receivables days	43.9	40.9	41.2	43.9
Payable days	49.4	51.3	48.6	53.7
Net debt/equity (%)	195.4	131.9	104.1	72.3
Interest cover - EBIT (X)	1.2	3.9	4.8	6.3

Valuation	3/10	3/11E	3/12E	3/13E
P/E (analyst) (X)	NM	8.6	7.3	5.3
P/B (X)	2.2	1.7	1.5	1.2
EV/EBITDA (X)	10.6	5.9	4.8	3.7
EV/GCI (X)	0.6	0.7	0.6	0.5
Dividend yield (%)	2.4	2.9	3.1	3.8

Note: Last actual year may include reported and estimated data.

Source: Company data, Goldman Sachs Research estimates.

Analyst Contributors

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Brownfield expansion project on track

The expansion project at Jamshedpur is on track with phased commissioning of various facilities scheduled from August 2011. We believe the pace of project execution is impressive with 30,000 people engaged at the project site. More than the scale, the complexity of managing a project of this size within the constraints of space and resources is notable.

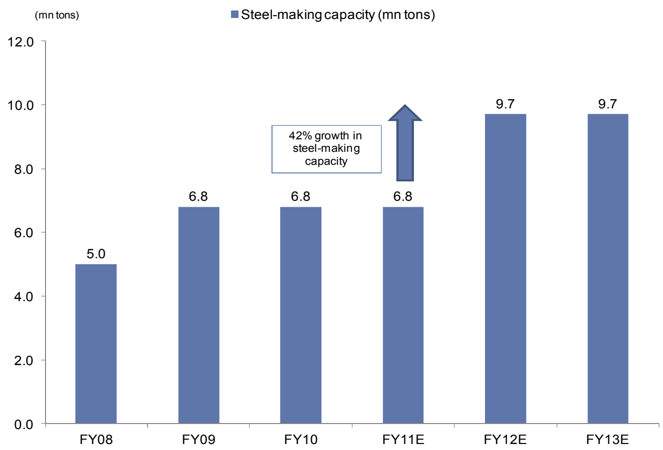
We believe this project will drive 19% FY11E-FY13E volume CAGR, improve furnace productivity (through use of pellets) and raise logistical efficiencies. With this, Tata Steel will be foraying into pelletisation and thin slab casting.

Exhibit 1: Jamshedpur expansion project is on track with phased commissioning of various facilities scheduled from Aug 2011

New facilities	Capacity	Cost (Rs mn)	Details as of 31 Dec, 2010	Expected timeline	Additional comments
Procuring equipment and upgrading facilities in certain existing mines	NA	11,000	Orders worth Rs 1,383mn placed with L&T in June-2009	Sep-11	Iron ore mine expansion to coincide with steel; coking coal mine expansion will be delayed
Blast furnace and upgradation of certain existing blast furnaces	3.1mtpa	21,790	Orders worth Rs 7,045mn placed with L&T, Paul Worth Italia in Oct-2008	Mar-12	New "I" furnace to be commissioned by Sep 2011
Coke oven comprising two coke oven batteries	2*0.7mtpa	25,570	Orders worth Rs 2,259mn placed with ACRE, China in Sep-2009	Feb-12	Battery # 10 - by Feb 2012; Battery # 11 by Dec 2012 - to resort to external conversion of coke in the interim
Lime calcining plant and upgradation of an existing Linz- Donawitz converter	NA	3,320		Mar-12	
Pellet plant	6.0mtpa	18,500	Orders worth Rs 4,275mn placed with L&T, Outotec in Oct-2008	Aug-11	To improve overall BF productivity by replacing part of sinter and lump ore charging
A New LD Converter and a thin slab caster to convert liquid steel into HRC	2.4mtpa	43,230	Orders worth Rs 7,273mn placed with SMS, India & Demag in Dec-2007	Dec-11	Aiming for full ramp up in record time of 12 months
Upgrading Raw Material Handling System	NA	8,220	Orders worth Rs 2,042mn placed with SMS, India & Demag in March-2010	NA	To improve conveyerised transportation from 20% currently to 75% post expansion
Power Distribution System	NA	7,850		NA	
Upgrading existing supporting facilities including pollution control systems, logistics, utilities and water management systems and other costs (Includes costs and fees for setting up laboratories, IT services and engineering consultancy services)	NA	20,170		NA	Share of rail in logistics to improve from 60% to 80% leading to decongestion of traffic
Contingency	NA	4,070		NA	
Total		**163,720**			

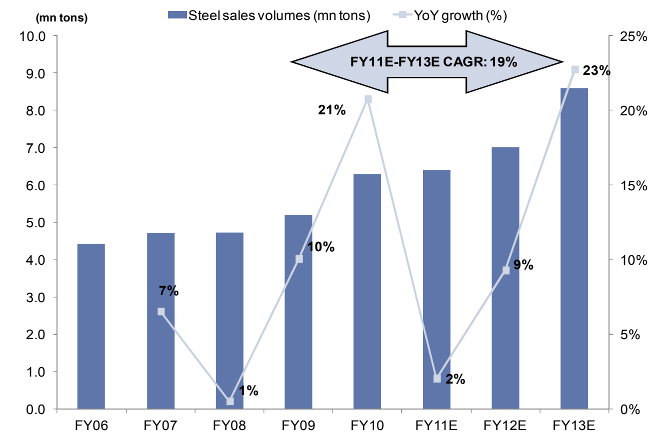
Source: Company data, Goldman Sachs Research.

Exhibit 2: Post 2.9mtpa Jamshedpur expansion, Tata Steel India's capacity will go up by 42%
Tata Steel India's steel making capacity



Source: Company data, Goldman Sachs Research estimates.

Exhibit 3: Strong volume growth in FY12E-FY13E
Tata Steel India's volume growth (%)



Source: Company data, Goldman Sachs Research estimates.

Strong downstream franchise to keep margins resilient

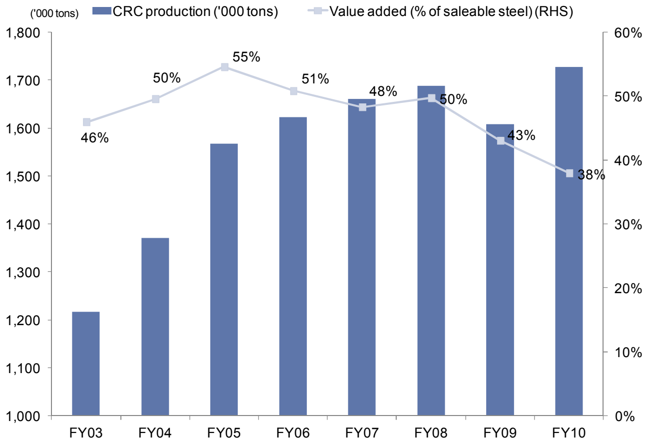
Tata Steel is a leading value-added steel player in India with a current downstream (cold-rolled) capacity of 1.7 mn tons, and more than 40% of sales exposure to the Auto/engineering segment. **Tata Steel's strong downstream franchise is reflected in its higher realizations vs. peers, and stable/resilient margins across the cycle.**

While Jamshedpur expansion project (to be onstream by Dec-2011) does not include any downstream facility, **the company continues to remain focused on maintaining 35%-40% share of value added products in its sales mix.** In order to supplement the increased upstream capacity, Tata Steel is developing integrated downstream operations to enrich its product mix by increasing its production and sales of high value-added steel products (see Exhibit 10).

In January 2011, the company entered into a joint venture with Nippon Steel Corporation for the construction of a continuous annealing and processing line to produce automotive cold-rolled flat products with a planned capacity of 600,000 tpa. The project is making good progress and scheduled to be commissioned by 2013. We believe this will significantly enhance the ultra low carbon IF steel making capability to cater to the high end automotive steel applications (for outer skin panel). **The company targets to double its production of auto-grade steel to 2 mn tons by 2015.**

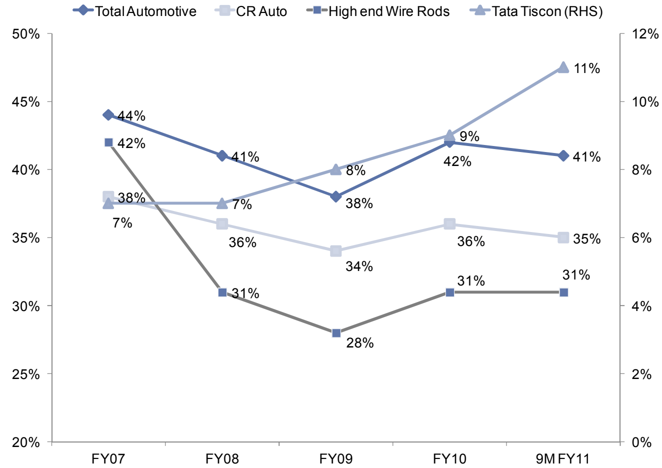
As our India auto analyst expects the auto industry to grow at 15% CAGR in FY10-FY13E, we believe the market leaders in the automotive sector will have an inherent advantage both in terms of products and services offered. Tata Steel's flat products division is a market leader in the Indian automotive segment with a 42% market share. For ytd FY11, Tata Steel is a market leader in both cold-rolled and galvanized coil/plates which are sold at a 15% (US$120-130/ton) premium to HRC price vs. incremental cost of US$40-50/ton. EBITDA margin for auto-grade steel could be as high as 55%-60% vs. 30%-35% for long steel. **We believe that Tata Steel (auto exposure = about 20%) is in the best position vs. its peers to leverage its auto-grade experience, as auto-grade steel customers are very sticky, and the barriers to entry are the highest in this segment, given low margin of error and customization.** Based on our channel checks, Tata Steel's auto-grade value added products are sold on average at a 10%-15% premium to its competitors.

Exhibit 4: Tata Steel is one of the largest producers of value added products, with
CRC production vs. share of value added products



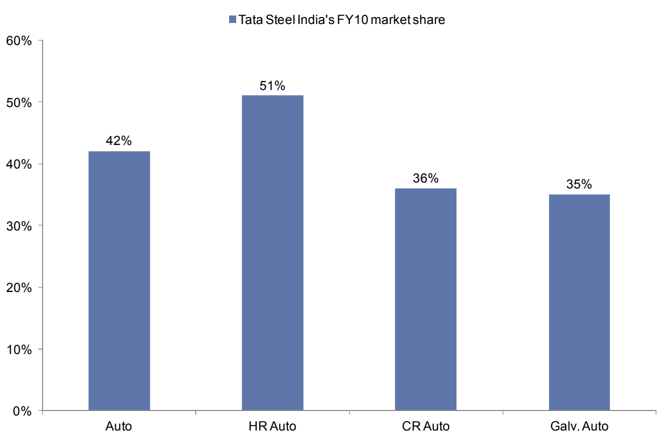
Source: Company data, Goldman Sachs Research.

Exhibit 5: ..leading market share in most products.
Market share in value added products



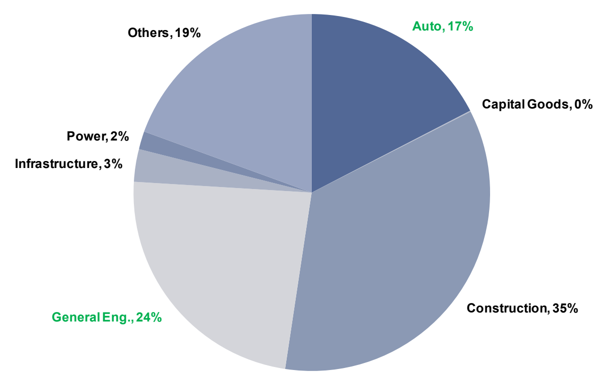
Source: Company data, Goldman Sachs Research.

Exhibit 6: Tata Steel has a significant advantage given its market leader position in value-added steel such as cold-rolled and galvanized steel
Tata Steel's market share in Auto-grade steel



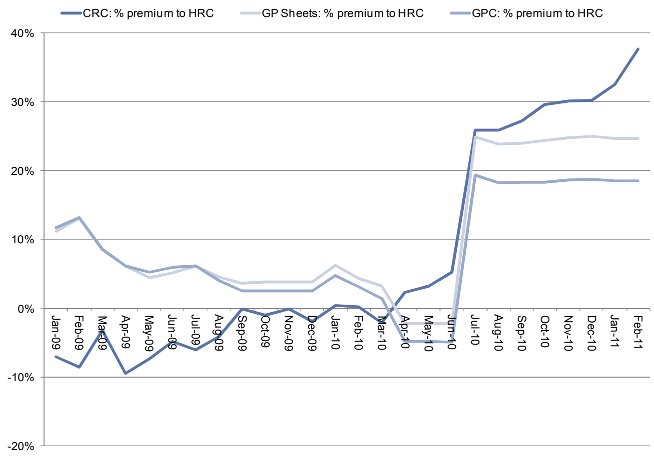
Source: Company data, Goldman Sachs Research.

Exhibit 7: ..with more than 40% exposure to auto/ general engineering
Sectoral exposure for Tata Steel India (FY10)



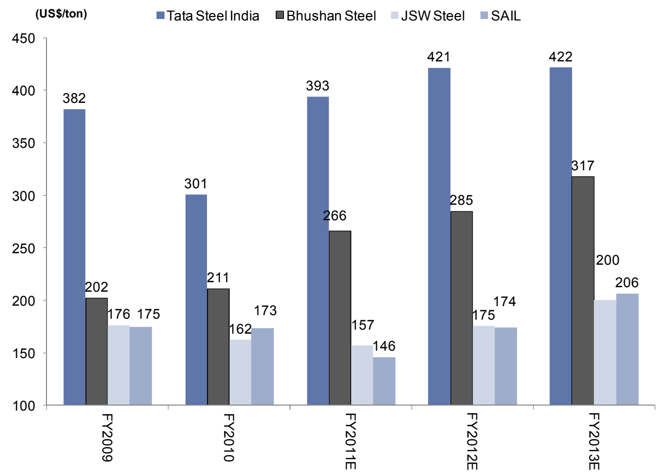
Source: Company data, Goldman Sachs Research.

Exhibit 8: Auto steel (CRC/GP/GC) at 15%-30% premium to HRC…



Source: Company data, Goldman Sachs Research.

Exhibit 9: …leading to higher and more resilient margins vs. peers
EBITDA/ton for India Steel coverage



Source: Company data, Goldman Sachs Research estimates.

Exhibit 10: Tata Steel continues to expand its downstream facilities to maintain its share of value added products (post upstream expansion)
Downstream initiatives by Tata Steel India

Downstream initiatives				
Project	**Stake**	**Capacity**	**Expected year of operations**	**Details**
Capacity expansion at Tinplate Company of India	**45%**	Capacity expansion from 190k tons to 379k tons	Mar-11	The first part of this expansion, including the tinning line, was commissioned in 2008 with the balance of facilities, including the cold-rolling mill, to be commissioned in 2011.
Joint venture with BlueScope	**50%**	Metal coating capacity - 250k Color coating capacity - 150k	Apr-11	A new greenfield project for Tata Bluescope Steel, a 50-50 joint venture company, established with Bluescope Steel that is engaged in the manufacture and sale of high-end building products.
JV with Nippon Steel	**51%**	CAPC line - 0.6mtpa	CY2013	0.6mtpa continuous annealing and processing line to produce automotive cold rolled flat products

Source: Company data, Goldman Sachs Research.

Focus on securing raw material integration

While Tata Steel India is well integrated at the upstream level, Tata Steel at a consolidated level (inc. Tata Steel Europe) has a long way to go in raw material security. At a consolidated level, Tata Steel sources about 35% of its iron ore requirements from captive iron ore mines, with 75% of its coking coal requirements being met through imports.

In the past few years, **the management has taken concrete initiatives to improve its upstream integration, including acquisition of mines, joint ventures, etc**.

In the recent past, Tata Steel's move to increase stake in Australia-listed Riversdale Mining from 24% to 27%, amid a bid by Rio Tinto, implies that the company considers it to be a strategic asset and is focused on improving its coking coal integration.

Moreover, Tata Steel entered into an agreement with New Millennium Ltd to develop the LabMag and KéMag iron ore deposits, known as the Taconite Project. The Taconite Project consists of two magnetite iron ore deposits with 9 bn tons of reserves and resources that could potentially produce 22 mn tons per year of iron ore concentrate. Tata Steel will help develop and pay 64% of the total costs (C$50 mn) related to the feasibility study for the Taconite Project, which is scheduled to be completed in 21 months. After the feasibility study is completed, both companies could potentially form a joint venture to develop the Taconite project, in which NML would hold a 20%-36% equity interest. The project involves a capex of C$4.85 bn if both deposits are developed (and up to C$4.68 bn and up to C$3.76 bn if only the KéMag or LabMag deposits are developed individually).

We believe that this is a long-term strategic positive for Tata Steel, again reflecting the strong intent of Tata Steel's management to improve the upstream integration, in a tight inflationary raw material environment. With Tata Steel Europe's iron ore requirement at 24 mn tons, this project could lead to 50%-60% iron ore integration for Tata Steel Europe, which has no captive iron ore currently. **Moreover, during the phase of the feasibility study, the company would not have to make significant investment (C$32 mn), and would not put the cash flows under pressure in the near-medium term, in our view.**

For India operations, the company remains committed to maintaining 100% self sufficiency in iron ore and 50% in coking coal, post the expansion. It is working towards commencing operations at the developmental mines at Ankua (iron ore), Kotre Basantpur (coking coal) and Ganeshpur (thermal coal) over the next 3-5 years.

Based on the current projects announced (excluding Taconite project), we expect the company to be 50% integrated in both iron ore/coking coal by CY14E, which would lead to significant cost savings and margin expansion.

Exhibit 11: Tata Steel on track to achieve higher upstream integration; we expect 50% integration by FY15E
Initiatives taken by Tata Steel to increase raw material security

Iron Ore Sourcing Mix - from 35% to 50% by FY15E						
New Mines	**Stake**	**Investment**	**Supply (TPA)**	**Reserves**	**Expected year of operations**	**Status**
New Millenium - DSO project	27% stake in parent, 80% stake in project; 100% offtake	C$65mn for 27% stake, capex of C$18mn for feasibility study	4mtpa	64.1mt	CY2012	Awaiting regulatory approvals
New Millenium - Taconite project	64% stake	C$32mn for feasibility study; $4.85bn for development of both deposits	Peak supply - 22 mtpa	9,000mt	Post FY16	Feasibility study for 21 months - Tata Steel and NML will fund 64% and 36% respectively of the cost of the Feasibility Study, which is estimated at C$50 million.
Ivory Coast Project	NA	NA	NA	NA	NA	Feasibilty study on, Exploration license granted to Sodemi in July09
Coking Coal Sourcing Mix - from 25% to 50% by FY15E						
New Mines			**Supply (TPA)**	**Reserves**	**Expected year of operations**	**Status**
Benga Coal Project, Mozambique	35% stake, 40% offtake		2mtpa from FY12; 4.2mtpa from FY14	502mt; mine life of 25 yrs	End CY11	Environmental approval, Mining permit awarded, Phase 1 (5.3mtpa) to start by 2HCY11; Phase 2 (10.6mtpa from 2014)
Coal mining project, Australia	5% stake, 20% offtake		1mtpa	47mt ROM	CY211	A$5.25mn expenses for Tata Steel in FY11
Other raw material initiatives			**Capacity**		**Expected year of operations**	**Benefits**
Port JV with L&T	**50%**		27mtpa		Apr-11	Phase I complete in August 2010; Phase-II almost complete, commercial operations by April 2011
JV with SAIL	**50%**		for identifying, acquiring and developing coal blocks in India.			
MOU with NMDC	**NA**		for exploring possibilities for acquisition, exploration and development of mines, extraction and processing of minerals			
JV with MMTC	**74%**		for acquiring, developing and operating mines and processing of minerals and metals.			

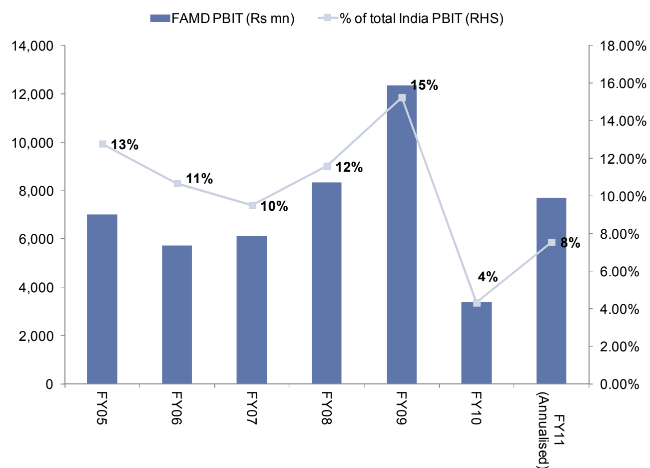
Source: Company data, Goldman Sachs Research.

Ferro-alloy business going strong, high ROCEs across cycles

We believe that Tata Steel's ferro alloys and minerals division (FAMD) is a free cash flow generator for the company, and has consistently enjoyed ROCE of more than 200%.

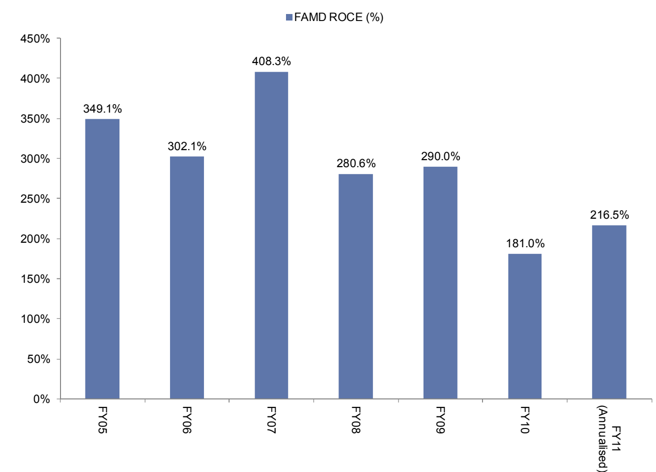
While the FAMD segment constitutes 8% of 9MFY11 Tata Steel India's operating profit, Tata Steel is a significant competitor in the global market and the market leader in ferrochrome business with a market share of around 27% in India and 6% globally. We continue to stay positive on ferro alloy business—in our view, supply would be constrained in the next 2-3 years, as no new ferrochrome capacity is coming on stream in the next 2 years. Moreover, productions cuts are taking place in South Africa, given high electricity tariffs.

Exhibit 12: Ferro-alloy business is a free cash flow generator for Tata Steel India…
FAMD PBIT and share to total PBIT (%)



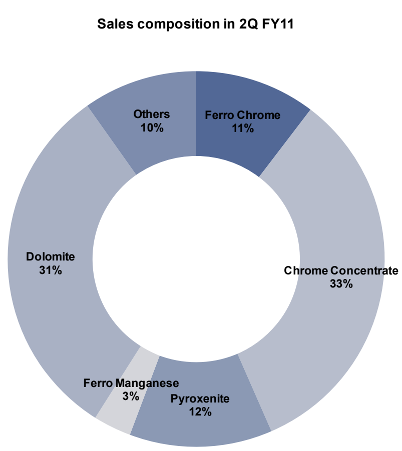
Source: Company data, Goldman Sachs Research estimates.

Exhibit 13: …with ROCE of greater than 200%
Ferro-alloy and minerals division ROCE



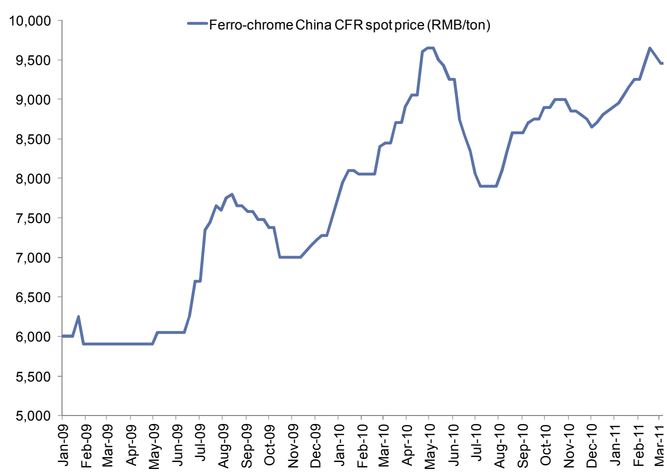
Source: Company data, Goldman Sachs Research estimates.

Exhibit 14: Tata Steel is a large producer of ferro alloys in India
FAMD composition in 2QFY11



Source: Company data, Goldman Sachs Research.

Exhibit 15: Ferro-chrome prices have been strong since Aug 2010
Ferro-chrome China CFR spot price



Source: SBB.

Reg AC

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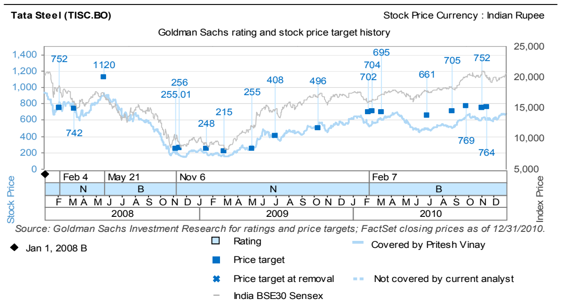

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