

**Sector: Metals & Mining**

Sensex:	20,157
CMP (Rs):	606
Target price (Rs):	685
Upside (%):	13.0
52 Week h/l (Rs):	737 / 449
Market cap (Rscr) :	54,701
6m Avg vol ('000Nos):	8,969
No of o/s shares (mn):	902
FV (Rs):	10
Bloomberg code:	TATA IB
Reuters code:	TISC.BO
BSE code:	500470
NSE code:	TATASTEEL

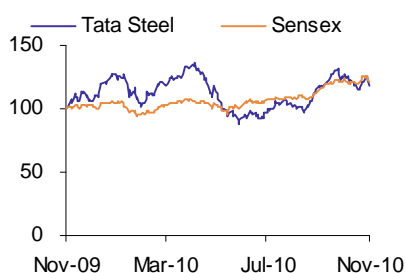
Prices as on 12 Nov, 2010

**Shareholding pattern**

<b>September '10</b>	<b>(%)</b>
Promoters	32.5
Institutions	42.6
Non promoter corp hold	3.4
Public & others	21.6

**Performance rel. to sensex**

(%)	1m	3m	1yr
Tata Steel	(4.1)	4.7	(2.1)
JSW Steel	(3.4)	3.5	33.7
SAIL	(13.4)	(12.6)	(12.1)
JSPL	(3.9)	(7.1)	(21.3)

**Share price trend**


- ✦ Consolidated Q2 FY11 revenue increased 5.3% qoq to Rs286bn higher than the street estimate of Rs269bn; led by higher sales in standalone entity and strong realisations in Tata Steel Europe
- ✦ Standalone revenue of Rs71.1bn is lower than our estimate due to lower realisations
- ✦ Consolidated sales volume declined 3.8% qoq, as the impact of higher sales in Indian operations was off set by a 4.9% decrease in European volumes
- ✦ EBIDTA/ton at Corus decreased from US\$70 to US\$56 on account of higher increase in raw material costs; however, higher than the street estimate
- ✦ The impact of higher raw material costs in Europe was lowered due to increase in realisations by 12.7% qoq
- ✦ Q2 FY11 adjusted PAT stood at Rs20.1bn, 6.6% higher on a qoq basis and against a loss of Rs17.9bn in Q2 FY10
- ✦ We revise upwards our price target to Rs685 on the back of strong operating performance in the European region and on expectations of steady steel prices in FY12

**Result table - Consolidated**

(Rs m)	Q2 FY11	Q1 FY11	% qoq	Q2 FY10	% yoy
<b>Net sales</b>	<b>286,462</b>	<b>271,948</b>	<b>5.3</b>	<b>253,950</b>	<b>12.8</b>
Material costs	(124,064)	(103,481)	19.9	(118,589)	4.6
Power and fuel costs	(9,967)	(9,713)	2.6	(10,128)	(1.6)
Personnel costs	(38,275)	(37,771)	1.3	(43,608)	(12.2)
Other overheads	(77,432)	(76,657)	1.0	(77,908)	(0.6)
<b>Operating profit</b>	<b>36,723</b>	<b>44,326</b>	<b>(17.2)</b>	<b>3,718</b>	<b>887.7</b>
<b>OPM (%)</b>	<b>12.8</b>	<b>16.3</b>	<b>(348) bps</b>	<b>1.5</b>	<b>1,136 bps</b>
Depreciation	(10,781)	(10,439)	3.3	(11,535)	(6.5)
Interest	(6,637)	(5,974)	11.1	(7,172)	(7.5)
Other income	8,143	595	1,269.2	179	4,438.8
<b>PBT</b>	<b>27,448</b>	<b>28,507</b>	<b>(3.7)</b>	<b>(14,810)</b>	<b>-</b>
Tax	(7,450)	(10,005)	(25.5)	(3,275)	127.5
<b>Effective tax rate (%)</b>	<b>27.1</b>	<b>35.1</b>		<b>(22.1)</b>	
Other provisions / minority etc	106	351	(69.8)	126	(15.7)
<b>Adjusted PAT</b>	<b>20,104</b>	<b>18,853</b>	<b>6.6</b>	<b>(17,959)</b>	<b>-</b>
<b>Adj. PAT margin (%)</b>	<b>7.0</b>	<b>6.9</b>	<b>9 bps</b>	<b>(7.1)</b>	<b>1,409 bps</b>
Extra ordinary items	(316)	(599)	(47.3)	(9,113)	(96.5)
<b>Reported PAT</b>	<b>19,788</b>	<b>18,255</b>	<b>8.4</b>	<b>(27,073)</b>	<b>-</b>
Ann. EPS (Rs)	89.2	85.0	4.9	(81.0)	-

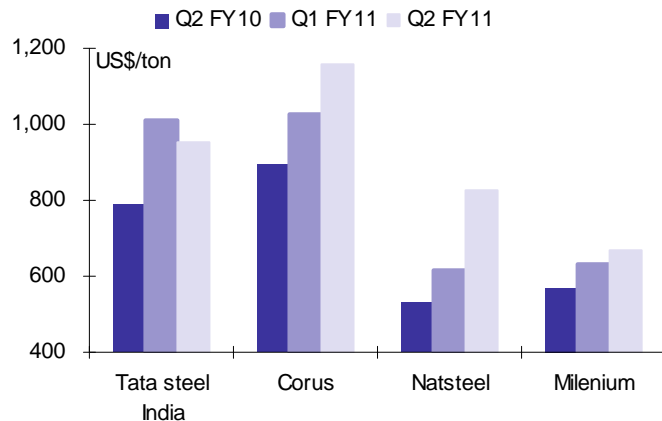
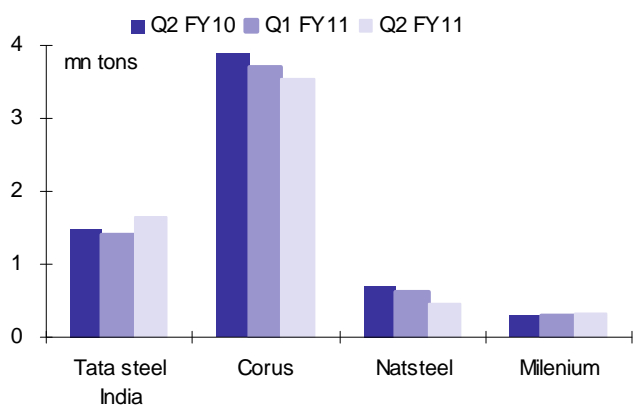
Source: Company, India Infoline Research

**Higher standalone volumes and realisations in Europe led to an 8.9% qoq increase in revenues in dollar terms**

During Q2 FY11, Tata Steel's topline increased 8.9% qoq in dollar terms and 5.3% qoq to Rs286.5bn, was higher than the street estimate of Rs269bn. Higher sales in standalone entity and strong realisations in Tata Steel Europe led to the outperformance in topline. Standalone Indian operations reported a sharp 18.7% qoq increase in sales volume to 1.7mn tons on account of some previous quarter inventory liquidation. Last quarter volumes in the domestic market were affected by cheap imports from China and a decline in demand in the long product category. Sales volume at its European operations declined 4.9% qoq to 3.5mn tons due to seasonality. Volume at its South Asian units remained flat on a qoq basis. Average realisations too increased by 2.7% qoq led by strong performance in its European operations. Average realisations in India declined 5.5% qoq; whereas that in Europe increased by 12.7% qoq. Realisations at its South East Asian operations managed to register an increase in realisations. Average realisations in Tata Steel India decreased from Rs42,871/ton in Q1 FY11 to Rs39,139 in Q2 FY11, lower than our estimate of Rs40,871/ton.

**Sales volume**

**Realization**



Source: Company, India Infoline Research

**Standalone operating profit jumped 30.8% qoq on account of sale of investments**

Tata Steel India registered a 9.9% qoq decline in operating profit to Rs26.3bn, lower than our estimate of Rs28.9bn. The underperformance in operating profit was due to lower realisations and higher than expected increase in raw material costs per ton. OPM during the quarter declined 752bps to 37%. Realisations during Q2 FY11 decreased by 8.7% qoq to Rs39,139/ton, lower than our estimate of Rs40,871/ton. Raw material costs per ton of steel jumped 36.6% qoq to Rs9,420 due to the impact of higher coking coal prices. Total cost of manufacturing per ton of steel increased by a mere 3.9% qoq as the impact of higher raw material costs was negated by a lower power costs and a decline in other expenditure. EBIDTA/ton for the standalone entity declined from Rs16,888 in Q1 FY11 to Rs12,165 in Q2 FY11. Ferro alloy division recorded an operating profit of Rs2bn, flat on a qoq basis and 175% higher on a yoy basis. The impact of higher ferro-alloy deliveries by 21.1% qoq was negated by an 11% decline in average realisations. The increase in sales during the quarter was mainly led by a rise in demand for long products. Long product sales increased from 0.6mn tons in Q1 FY11 to 0.78mn tons in Q2 FY11, while that of flat products increased from 0.79mn tons to 0.89mn tons. Realisations of flat products decline from US\$829/ton in Q1 FY11 to US\$792 in Q2 FY11 and that of long products declined from US\$694/ton to US\$612/ton.

## Per ton cost analysis (Standalone)

	Q2 FY11	Q1 FY11	% qoq	Q2 FY10	% yoy
Steel production	1.61	1.59	1.3	1.52	6.0
Steel sales	1.66	1.40	18.7	1.46	14.0
Sales as a % of production	103.1	88.0		95.9	
Net realisations	39,139	42,871	(8.7)	39,074	0.2
<b>Cost per ton (Rs/ton)</b>					
RM/ton	9,420	6,897	36.6	9,759	(3.5)
Staff cost	4,119	4,133	(0.3)	3,584	14.9
Power and fuel costs	2,178	2,536	(14.1)	2,045	6.5
Other expenditure	11,258	12,417	(9.3)	10,490	7.3
<b>Total cost</b>	<b>26,974</b>	<b>25,983</b>	<b>3.8</b>	<b>25,879</b>	<b>4.2</b>
<b>EBIDTA/ton</b>	<b>12,165</b>	<b>16,888</b>	<b>(28.0)</b>	<b>13,195</b>	<b>(7.8)</b>

Source: Company, India Infoline Research

## Consolidated operating profit increased 61% qoq led by higher contribution from Corus

Tata Steel in Q2 FY11 on a consolidated level, registered a pre-exceptional operating profit of Rs36.7bn (US\$1bn) compared to Rs44bn (US\$975mn) in Q4 FY10. The decline in operating profit was mainly due to increase in raw material costs. During the quarter European operations registered an operating profit of US\$197mn against an operating profit of US\$293mn in Q1 FY11. This was due to higher increase in raw material costs than the increase in steel realizations. Raw material costs in Europe jumped 20% qoq due to an increase in iron ore and coking coal prices, whereas steel realizations increased by 5% qoq. Capacity utilization in Q2 FY11 decreased to 87% from 90% in Q1 FY11 and is expected to remain lower in Q3 FY11 due to seasonality. EBIDTA/ton during the quarter in Europe declined from US\$79/ton in Q1 FY11 to US\$56/ton in Q2 FY11.

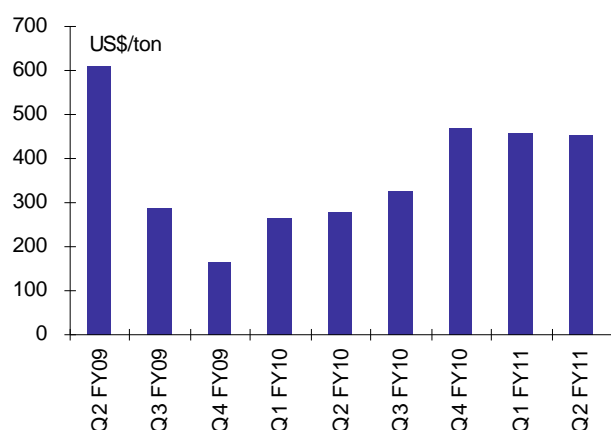
## Cost Analysis

As a % of net sales	Q2 FY11	Q1 FY11	bps qoq	Q2 FY10	bps yoy
Material costs	43.3	38.1	526	46.7	(339)
Power and fuel costs	3.5	3.6	(9)	4.0	(51)
Personnel Costs	13.4	13.9	(53)	17.2	(381)
Other overheads	27.0	28.2	(116)	30.7	(365)
<b>Total costs</b>	<b>87.2</b>	<b>83.7</b>	<b>348</b>	<b>98.5</b>	<b>(1,136)</b>

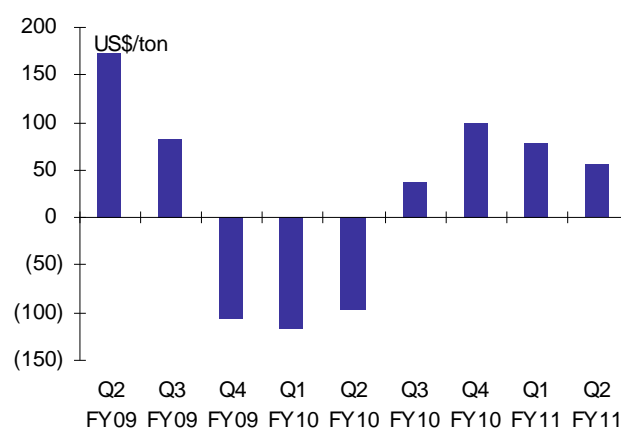
	Q2 FY11	Q1 FY11	% qoq	Q2 FY10	% yoy
<b>Realisations</b>	<b>49,220</b>	<b>44,958</b>	<b>9.5</b>	<b>40,960</b>	<b>20.2</b>
RM/ton	21,317	17,107	24.6	19,127	11.4
Staff cost	1,713	1,606	6.7	1,633	4.8
Power and fuel costs	6,576	6,244	5.3	7,034	(6.5)
Other expenditure	13,305	12,673	5.0	12,566	5.9
<b>Total cost/ton</b>	<b>42,910</b>	<b>37,630</b>	<b>14.0</b>	<b>40,360</b>	<b>6.3</b>
<b>EBIDTA/ton</b>	<b>6,310</b>	<b>7,328</b>	<b>(13.9)</b>	<b>600</b>	<b>952.2</b>

Source: Company, India Infoline Research

## EBIDTA/ton trend for Tata Steel India



## ... &amp; for Tata Steel Europe



Source: Company, India Infoline Research

## Company performance

Tata Steel Standalone	Q2 FY11	Q1 FY11	bps qoq	Q2 FY10	bps yoy
Sales volume (mn tons)	1.7	1.4	18.7	1.5	10.7
Realisation (US\$/ton)	953	1,009	(5.5)	789	20.8
Revenue (US\$ mn)	1,582	1,411	12.1	1,183	33.7
EBIDTA (US\$ mn)	748	638	17.2	415	80.2
OPM (%)	47.3	45.2	207 bps	35.1	1220 bps
EBIDTA/ton (US\$)	451	456	(1.2)	277	62.9

Tata Steel UK - Corus	Q2 FY11	Q1 FY11	bps qoq	Q2 FY10	bps yoy
Sales volume (mn tons)	3.5	3.7	(4.9)	3.9	(9.5)
Realisation (US\$/ton)	1,159	1,028	12.7	894	29.6
Revenue (US\$ mn)	4,090	3,814	7.2	3,486	17.3
EBIDTA (US\$ mn)	197	293	(32.8)	(375)	(152.5)
OPM (%)	4.8	7.7	-287 bps	(10.8)	1557 bps
EBIDTA/ton (US\$)	56	79	(29.3)	(96)	(158.0)

Natsteel	Q2 FY11	Q1 FY11	bps qoq	Q2 FY10	bps yoy
Sales volume (mn tons)	0.5	0.6	(24.5)	0.7	(34.3)
Realisation (US\$/ton)	824	616	33.8	530	55.5
Revenue (US\$ mn)	379	375	1.1	371	2.2
EBIDTA (US\$ mn)	26	20	30.0	20	30.0
OPM (%)	6.9	5.3	153 bps	5.4	147 bps
EBIDTA/ton (US\$)	57	33	72.1	29	97.8

Tata Steel Thailand	Q2 FY11	Q1 FY11	bps qoq	Q2 FY10	bps yoy
Sales volume (mn tons)	0.3	0.3	11.1	0.3	10.0
Realisation (US\$/ton)	667	633	5.3	567	17.6
Revenue (US\$ mn)	220	188	17.0	170	29.4
EBIDTA (US\$ mn)	3	12	(75.0)	17	(82.4)
OPM (%)	1.4	6.4	-502 bps	10.0	-864 bps
EBIDTA/ton (US\$)	9	40	(77.5)	57	(84.0)

Source: Company, India Infoline Research

### Maintain BUY with a revised price target of Rs580

The strong performance in the European operations witnessed in the last three quarters has been due to a combination of higher realizations and capacity utilization levels. The company has managed to increase its capacity utilization level to 88% in H1 FY11. However, it expects it to moderate in Q3 FY11 due to seasonal factors before a strong quarter in Q4 FY11. Average realisation for the company has been higher than its peers due to superior product mix. We believe that the margin contraction will continue in the coming quarters due to the full impact of high raw material prices and a decline in average realisations. We expect the company to remain EBIDTA positive for the year on account of higher utilization rate and the mothballing of Teeside plant. We believe Corus will not be impacted further as the company's exposure to the vulnerable Southern Europe is below 10% and the weak construction sector accounts for only 20% of total sales. Global steel prices too have rebounded from its lows over the last two month and have stabilized due to the regulatory steps taken by the Chinese government. We revise upwards our price target to Rs685 on the back of strong operating performance in the European region and on expectations of steady steel prices in FY12.

### Financial summary

Y/e 31 Mar (Rs m)	FY09	FY10	FY11E	FY12E
Revenues	1,473,290	1,023,930	1,109,314	1,165,245
yoy growth (%)	12.0	(30.5)	8.3	5.0
Operating profit	181,254	88,689	155,878	168,051
OPM (%)	12.3	8.7	14.1	14.4
Pre-exceptional PAT	90,432	5,007	68,104	71,740
Reported PAT	49,487	(11,830)	68,104	71,740
yoy growth (%)	(59.1)	-	-	5.3
EPS (Rs)	123.9	5.6	75.5	78.5
P/E (x)	4.9	107.3	8.0	7.7
Price/Book (x)	1.9	2.2	1.5	1.2
EV/EBITDA (x)	5.7	11.3	6.5	5.8
Debt/Equity (x)	2.6	1.9	1.3	0.9
RoE (%)	34.1	1.9	22.1	17.4
RoCE (%)	15.5	6.5	14.3	13.3

Source: Company, India Infoline Research

**Recommendation parameters for fundamental reports:**

**Buy** – Absolute return of over +10%

**Market Performer** – Absolute return between -10% to +10%

**Sell** – Absolute return below -10%

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