

May 17, 2011

Reco	Previous Reco
Buy	Accumulate
CMP	Target Price
Rs 921	Rs 1,169
EPS change FY12E/13E (%)	-10 / NA
Target Price change (%)	10
Nifty	5,499
Sensex	18,345

Price Performance

(%)	1M	3M	6M	12M
Absolute	(3)	12	(27)	(26)
Rel. to Nifty	4	6	(20)	(31)

Source: Bloomberg

Relative Price Chart



Source: Bloomberg

Stock Details

Sector	Metals & Mining
Bloomberg	JSTL@IN
Equity Capital (Rs mn)	2231
Face Value(Rs)	10
No of shares o/s (mn)	223
52 Week H/L	1,400/752
Market Cap (Rs bn/USD mn)	209/4,657
Daily Avg Volume (No of sh)	697551
Daily Avg Turnover (US\$m)	14.3

Shareholding Pattern (%)

	Mar-11	Dec-10	Sep-10
Promoters	37.7	37.7	45.0
FII/NRI	45.8	47.3	35.6
Institutions	4.9	4.6	6.5
Private Corp	3.5	3.3	4.7
Public	8.1	7.1	8.3

Source: Capitaline

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- JSW Steel posted robust performance for Q4FY11 with topline growing by 33% YoY and 21% QoQ to Rs 72.8 bn (cons) backed by sharp jump in sales volume to 1.733 mt
- Better product mix with lower sales of semis coupled with higher realizations (~Rs 41,000/ tonne) helped the company to post an EBITDA of Rs 16.6 bn, up 26% YoY and 64% QoQ
- Strong operating performance flowed into the bottomline too which rose 30% and 172% on YoY and QoQ respectively to Rs 7.94 bn. Ispat also contributed positively to the reported PAT
- Despite short- term challenges, volume growth and better integration should benefit FY13 performance. Upgrade to Buy with a target price of Rs 1,169 valuing at 6x FY13 EV/ EBITDA

Robust performance backed by strong sales volume and realizations

The Q4FY11 performance of the company has been higher than ours and street estimates mainly on account of significantly higher (up 14% YoY and 9% QoQ) to 1.733 mt. Despite crude steel production of 1.647 mt, higher sales volume can be attributed to transfer sales of 1.66 lakh tonnes of HRC from Ispat Industries during the quarter. Price hike during January and February got reflected in the average blended realizations for the standalone company at Rs 41,000/ tonne against Rs 36,500/ tonne for the previous quarter and ~Rs 38,500/ tonne during Q4FY10. Better product mix with lower sales of semis and higher value added sales by Shoppe helped the EBITDA/ tonne to improve to Rs 9,545 (US\$211), highest since Q2FY09. Use of lower priced coking coal (US\$209/t) in the blend restricted costs to go up. We believe maintaining this kind of margins in next couple of quarters would be extremely difficult for the company, as proportion of US\$330/t coking coal would start from the month of June onwards.

Ispat- a positive surprise; Chile shipments started

Ispat industries posted a net profit of Rs 700 mn for Q4FY11, with EBITDA/ tonne of Rs 5700. This has been a positive surprise and could be achieved because of better realizations of Rs 40,700/ tonne and one time tax benefit to the tune of Rs 350 mn. Consistent with JSW Steel, for Ispat also we believe maintaining this performance for the short- medium term with higher interest rate scenario and also problems on account of supply constraints of gas would be very tough. FY13 performance is likely to be better however due to better integration. The company said that two shipments from Chile have started and 1 mt sales are likely for FY12. We have factored in 0.8 mt for FY12.

Outlook and Valuations

Factoring in the rise in raw material costs, contribution from Chile and Ispat we have cut our FY12 EPS by 10% to Rs 95.6/ share and introduce our FY13 estimates with EPS at Rs 122.8/ share. At the CMP of Rs 921, the stock is trading at 7.5x FY13E EPS and 5.2x FY13E EV/ EBITDA. Considering the positive and concerns we value the company 6x FY13 EV/ EBITDA to arrive at a target price of Rs 1,169/ share. We upgrade the stock to BUY.

Financials

(Rs mn)

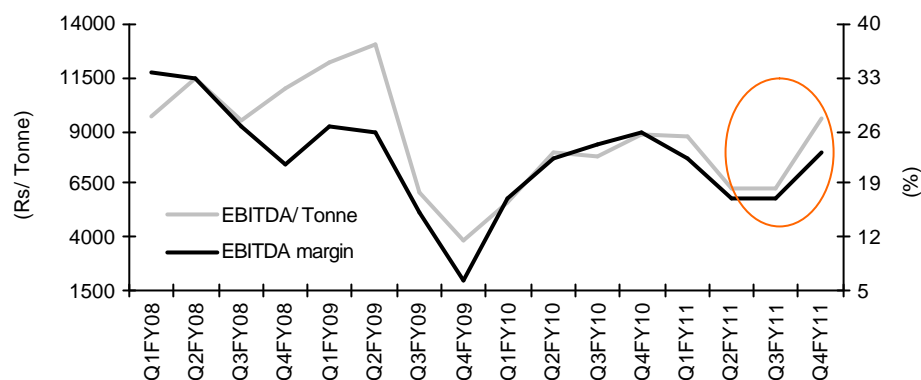
YE-	Net Sales	EBITDA (Core)	EBITDA (%)	APAT	EPS (Rs)	EPS % chg	RoE (%)	P/E	EV/ EBITDA	P/BV
Mar										
FY09	190,738	41,873	22.0	15,976	71.6	36.7	17.8	12.9	7.5	1.9
FY10	241,161	47,795	19.8	17,540	78.6	9.8	11.7	11.7	7.3	1.4
FY11E	325,319	64,748	19.9	22,994	95.6	21.6	13.7	9.6	6.4	1.3
FY12E	377,133	78,095	20.7	29,533	122.8	28.4	15.5	7.5	5.2	1.2

Source: Company, Emkay Research

Key Financials – Quarterly (Consolidated)

(Rs mn)	Q4FY10	Q1FY11	Q2FY11	Q3FY11	Q4FY11	YoY (%)	QoQ (%)	YTD'11	YTD'10	YoY (%)
Revenue	54,807	48,580	59,722	60,026	72,833	32.9	21.3	241,161	190,738	26.4
Expenditure	(41,573)	(37,796)	(49,495)	(49,862)	(56,213)	35.2	12.7	(193,366)	(149,080)	29.7
<i>as % of sales</i>	75.9	77.8	82.9	83.1	77.2			80.2	78.2	
Consumption of RM	(34,458)	(29,563)	(41,335)	(41,725)	(46,497)	34.9	11.4	(159,120)	(122,788)	29.6
<i>as % of sales</i>	62.9	60.9	69.2	69.5	63.8			66.0	64.4	
Employee Cost	(1,244)	(1,682)	(1,563)	(1,524)	(1,598)	28.5	4.8	(6,368)	(4,795)	32.8
<i>as % of sales</i>	2.3	3.5	2.6	2.5	2.2			2.6	2.5	
Other expenditure	(5,871)	(6,551)	(6,597)	(6,613)	(8,118)	38.3	22.8	(27,879)	(21,497)	29.7
<i>as % of sales</i>	10.7	13.5	11.0	11.0	11.1			11.6	11.3	
EBITDA	13,234	10,784	10,227	10,164	16,620	25.6	63.5	47,795	41,658	14.7
Depreciation	(3,267)	(3,612)	(3,791)	(3,906)	(4,288)	31.2	9.8	(15,597)	(12,987)	20.1
EBIT	9,967	7,172	6,436	6,258	12,332	23.7	97.1	32,198	28,672	12.3
Other Income	964	32	1,634	38	-	(100.0)	(100.0)	1,704	4,409	(61.4)
Interest	(2,494)	(2,731)	(2,614)	(1,968)	(2,172)	(12.9)	10.4	(9,485)	(11,080)	(14.4)
PBT	8,436	4,473	5,456	4,328	10,160	20.4	134.8	24,417	22,000	11.0
Total Tax	(2,408)	(1,587)	(1,816)	(1,501)	(2,920)	21.3	94.6	(7,823)	(6,467)	21.0
Adjusted PAT	6,029	2,886	3,640	2,827	7,240	20.1	156.1	16,594	15,533	6.8
(Profit)/loss from JV's/Ass/MI	82	68	92	90	697	754.6	675.6	946	443	113.7
Adj.PAT after MI	6,110	2,954	3,733	2,917	7,936	29.9	172.1	17,540	15,976	9.8
Extra ordinary items	-	-	-	-	-	-	-	-	-	-
Reported PAT	6,110	2,954	3,733	2,917	7,936	29.9	172.1	17,540	15,976	9.8
Reported EPS	32.2	13.2	16.7	13.1	35.2	9.3	169.3	78.3	76.4	2.4

Margins (%)						(bps)	(bps)			(bps)
EBIDTA	24.1	22.2	17.1	16.9	22.8	(133)	589	19.8	21.8	(202)
EBIT	18.2	14.8	10.8	10.4	16.9	(125)	651	13.4	15.0	(168)
EBT	15.4	9.2	9.1	7.2	13.9	(144)	674	10.1	11.5	(141)
PAT	11.0	5.9	6.1	4.7	9.9	(106)	523	6.9	8.1	(126)
Effective Tax rate	28.5	35.5	33.3	34.7	28.7	20	(593)	32.0	29.4	264

Margin improved sharply for the standalone business

Source: Company, Emkay Research

Ispat Industry's performance- a positive surprise

	Q4FY11	Q3FY11	Growth (%)
Production (MT)			
HR Coils	0.729	0.262	178%
Capacity Utilization	88%	32%	
Sales (MT)			
HR Coils	0.672	0.229	193%
Value Added Products	0.04	0.047	-15%
Financials (INR mn)			
Net Sales	26470	9610	175%
EBITDA	4070	(1,570)	LP
EBITDA Margin	14.9%	-16.1%	LP
Net finance charges	1880	2870	-34%
Depreciation	1480	1460	1%
Profit before Tax	700	(5,900)	LP
Profit After Tax	700	(4,090)	LP

Source: Company, Emkay Research

US plate and pipe mills continue to be weak performer

	Q4FY11	Q4FY10	FY11	FY10
Production (NT)				
Plate Mill	12197	69444	119887	195275
Pipe Mill	4776	23788	42148	73969
Sales (NT)				
Plate Mill	27627	42297	106936	119614
Pipe Mill	4875	25917	45217	72508
Financials (US\$ mn)				
Turnover	27.75	56.83	141.33	159.87
EBITDA+ Other income	4.57*	2.25	14.69*	(40.92)
Profit After Tax	(16.25)	(12.90)	(50.00)	70.03

*Excluding one time inventory write down of US\$721 mn

Source: Company, Emkay Research

Key takeaways

Sales volume guidance for FY12 at 9 mt

- JSW Steel targets crude steel production of 8.75 mt and sales of 9 mt for FRY12 with the help of more availability of HRC for sale due to transfer sales from Ispat

Chile iron ore mines- shipments started

- The management has informed that shipments from Chile have started with one consignment left shipped in the month of April. The company still targets to sell 1 mt of iron ore from Chile in FY12 with gradual ramping up taking place after that
- The cost of production of beneficiated iron ore (62%) remains at US\$62/ tonne

US coking coal mines: all approvals in place

- The company has told that it has got all the approvals for US coking coal during May and plans to bring 0.5 mt of coking coal from US in FY12 to India against earlier target of 1 mt. During Q4FY11, the company had sold 36000 tonne of inferior quality of coking coal

3.2 mtpa expansion delayed till mid June

- Due to some technical problems the company has delayed commissioning of its 3.2 blast furnace at Vijaynagar. This is now likely to be commissioned during mid June. Thus, the increased production volume is expected to be visible in Q3FY12
- The company however has already started trial run of its ladle heating furnace-3, converter-3 and caster-4 facilities under the expansion project

Crude steel capacity to be increased to 12 mt at Vijaynagar

- The company plans to increase its crude steel capacity in Vijaynagar from 10 mtpa to 12 mtpa through de-bottlenecking of existing furnaces and setting up of SMS-3 comprising of EAF and slab caster to produce special grade thin slabs
- The total cost of the project remains at Rs 26.95 bn with D/E of 2:1. The expected completion date of the project is June 2013

Numbers of Shoppe increased and so as sales

- JSW Shoppe, the company's retail outlets increased to 280 from 174 a year ago. Sales through the Shoppe also increased 77% YoY to 1.123 mt. Importantly, 46% of these sales were contributed by the value added flat products, followed by 39% rolled HR products and 15% rolled long products

Balance sheet: D/ E still at comfortable level

- The company has a net debt of Rs 141.6 bn and a cash balance of Rs 23 bn as on 31st March 2011
- The consolidated D/E remains at 0.84. The company has repaid Rs 4.5 bn and drawn Rs 7.6 bn new debt during FY11

Earnings revised; introducing FY13 estimates

JSW Steel has posted robust performance for Q4FY11 on the back of sharp rise in realizations and strong sales volume. Raw material as percentage to sales has been lower during the quarter, as the company has been using its comparatively low priced coking coal inventory. The scenario however is not likely to remain same in the short medium term, as the macro economic situation in the country has been getting more challenging with rise in inflation and interest rates. In the spot markets softening of prices are also visible. Along with that, impact of higher cost coking coal would be used from June. These together are expected to weigh on the margins again. We believe the company would not be able to maintain similar performances during the coming year. Steps by Karanataka government and other concerned authorities to stop illegal mining in the state may also proved to be negative for the company, as that might restrict availability of low grade fines at a cheaper price. On the positive side, contribution from Chile iron ore mines are likely to visible during FY12. We have taken sales volume of 0.8 mt and 1 mt for FY12 and FY13 respectively from Chile. Though, the company is expecting 0.5 mt coking coal from US during FY12, we have not taken any direct impact of that and would prefer to wait for further clarity. We have taken Ispat's contribution on a proportionate basis.

We have cut our FY12 EPS by 10% to Rs 95.6/ share. We introduce our FY13 estimates with EPS at Rs 122.8/ share. Despite some pain in the short medium term, we believe the stock has a potential to outperform on a longer term basis backed by strong volume growth and higher integration. The company has indicated its seriousness in having stronger backward integration even by acquisition of mines if available at a right price.

Valuation

At the CMP of Rs 921, the stock is trading at 7.5x FY13E EPS and 5.2x FY13E EV/ EBITDA. Considering the positive and concerns we value the company 6x FY13 EV/ EBITDA to arrive at a target price of Rs 1,169/ share. We upgrade the stock to BUY from Accumulate.

Financials (consolidated)

Income Statement

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
Net Sales	190,738	241,161	325,319	377,133
<i>Growth (%)</i>	18.8	26.4	34.9	15.9
Expenditure	148,865	193,366	260,571	299,038
Raw Materials	122,788	159,120	210,880	241,429
Employee Cost	4,795	6,368	9,760	11,314
Other Exp	21282	27879	37412	43370
EBITDA	41,873	47,795	64,748	78,095
<i>Growth (%)</i>	34.9	14.1	35.5	20.6
EBITDA margin (%)	22.0	19.8	19.9	20.7
Depreciation	12987	15597	20889	22844
EBIT	28,886	32,198	43,859	55,251
EBIT margin (%)	15.1	13.4	13.5	14.7
Other Income	4194	1704	3253	3771
Interest expenses	11080	9485	14569	16881
PBT	22,000	24,417	32,543	42,141
Tax	6467	7823	10088	13907
<i>Effective tax rate (%)</i>	29.4	32.0	31.0	33.0
Adjusted PAT	15,533	16,594	22,455	28,234
(Profit)/loss from JV's/Ass/MI	443	946	540	1298
Adjusted PAT after MI	15,976	17,540	22,994	29,533
<i>Growth (%)</i>	63.0	9.8	31.1	28.4
Net Margin (%)	14.1	14.3	15.1	16.1
E/O items	0	0	0	0
Reported PAT	15,976	17,540	22,994	29,533
<i>Growth (%)</i>	762.2	9.8	31.1	28.4

Cash Flow

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
PBT (Ex-Other income)	17,806	22,713	29,290	38,370
Depreciation	12,987	15,597	20,889	22,844
Interest Provided	11,080	9,485	14,569	16,881
Other Non-Cash items	-10,017	-12,996	-16,384	-22,744
Chg in working cap	-4,710	8,853	11,369	7,000
Tax paid	6,467	7,823	10,088	13,907
Operating Cashflow	33,613	51,475	69,822	76,258
Capital expenditure	33,911	89,572	100,183	37,339
Free Cash Flow	67,524	141,047	170,005	113,597
Other income	128	0	0	0
Investments	-2,033	0	0	0
Investing Cashflow	-29,323	-83,500	-105,000	-50,000
Equity Capital Raised	-99	48,361	175	0
Loans Taken / (Repaid)	11,223	18,000	48,000	34,000
Interest Paid	-11,080	-9,485	-14,569	-16,881
Others	-16,885	-12,731	-17,365	-19,677
Financing Cashflow	-5,762	53,630	30,810	14,323
Net chg in cash	-2,062	21,604	-4,368	40,581
Opening cash position	5,093	3,030	24,635	20,267
Closing cash position	3,030	24,635	20,267	60,848

Balance Sheet

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
Equity share capital	1871	2231	2406	2406
Reserves & surplus	87,911	147,721	165,007	188,651
Net worth	89,781	149,952	167,413	191,057
Minority Interest	2187	2187	2187	2187
Secured Loans	127,355	145,355	193,355	227,355
Unsecured Loans	20,901	20,901	20,901	20,901
Loan Funds	148,256	166,256	214,256	248,256
Net deferred tax liability	16848	16847.8	16847.8	16847.8
Total Liabilities	354,063	458,429	561,389	643,419
Gross Block	284,090	351,993	436,104	463,260
Less: Depreciation	12,987	15,597	20,889	22,844
Net block	214,528	276,931	351,042	363,198
CWIP	69562	75062	85062	100062
Investment	6,282	6,282	6,282	6,282
Current Assets	54,700	91,163	110,011	164,885
Inventories	28,667	37,000	49,912	57,862
Sundry debtors	6,964	9,250	12,478	14,465
Cash & bank balance	3,030	24,635	20,267	60,848
Loans & advances	16,038	20,278	27,354	31,711
Other current assets	0	0	0	0
Current lia & Prov	87,913	112,124	147,209	169,003
Current liabilities	82,582	106,793	141,879	163,672
Provisions	5,331	5,331	5,331	5,331
Net current assets	-33,213	-20,961	-37,199	-4,118
Total Assets	354,063	458,429	561,389	643,419

Key Ratios

Y/E, Mar	FY09	FY10	FY11E	FY12E
Profitability (%)				
EBITDA Margin	21.8	19.8	19.9	20.7
Net Margin	8.4	7.3	7.1	7.8
ROCE	9.4	7.4	8.4	9.2
ROE	17.8	11.7	13.7	15.5
RoIC	17.3	15.1	15.5	17.4
Per Share Data (Rs)				
EPS	71.6	78.6	95.6	122.8
CEPS	129.8	148.5	182.4	217.7
BVPS	480.0	672.1	695.8	794.0
DPS	1.2	1.7	1.4	1.4
Valuations (x)				
PER	12.9	11.7	9.6	7.5
P/CEPS	7.0	6.1	4.9	4.1
P/BV	1.9	1.4	1.3	1.2
EV / EBITDA	7.5	7.3	6.4	5.2
Gearing Ratio (x)				
Net Debt/ Equity	1.5	0.9	1.1	0.9
Net Debt/EBITDA	3.5	3.0	3.0	2.4

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