

COMPANY UPDATE

Tata Steel (TISC.BO)

Buy

Equity Research

The worst may be behind, well poised for recovery; retain Buy

What's changed

Key takeaways from Tata Steel's 3QFY12 results conference call: (1) Group steel deliveries at 5.84mnt (-5% qoq), were impacted by seasonal weakness and market uncertainties in Europe and floods in Thailand. (2) Europe business witnessed price declines on weak demand while higher priced raw materials impacted profitability, resulting in the company making significant mark-to-market provisions on stock. However, this implies that with steel prices recovering, there is low risk of further inventory write-downs. European demand has picked up with prices inching up. The company is targeting to retain FY13E volumes in Europe at FY12E levels, despite planned temporary closure of the BF4 at Port Talbot for rebuild. (3) India business saw stable prices with long product and downstream prices higher than previous quarters. Margins were compressed on account of higher raw material (imported coking coal) prices. (4) The company expects to commission the Jamshedpur brownfield expansion by March 2012 and expects to add 1mn tons to current production levels in FY13. (5) European restructuring measures are progressing per plan, leading to about 2500 redundancies. (6) The Benga coking coal project in Mozambique is expected to commence despatches from March 2012.

Implications

We cut our FY12E-14E EPS by -1% to -11% on inventory write-down, and higher cost assumptions. But we believe the worst may be behind in both India and European profitability, and with the Jamshedpur expansion on track, the company is well positioned for a strong earnings recovery in FY13E.

Valuation

We reiterate our Buy rating and lower our 12-month P/B-based TP to Rs550 (from Rs552) on lower earnings estimates.

Key risks

Slower-than-expected demand recovery in Europe, higher-than-expected raw material costs.

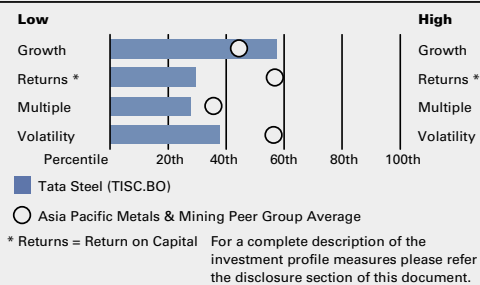
INVESTMENT LIST MEMBERSHIP

Asia Pacific Buy List

Coverage View: Neutral

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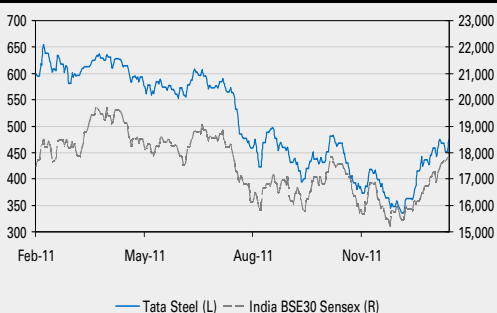
Investment Profile



Key data	Current
Price (Rs)	475.00
12 month price target (Rs)	550.00
Market cap (Rs mn / US\$ mn)	458,020.0 / 9,270.7
Foreign ownership (%)	19.7

	3/11	3/12E	3/13E	3/14E
EPS (Rs) New	73.55	47.82	59.55	83.12
EPS revision (%)	0.0	(6.0)	(10.9)	(0.7)
EPS growth (%)	1,970.6	(35.0)	24.5	39.6
EPS (dil) (Rs) New	92.55	86.93	59.16	82.58
P/E (X)	6.5	9.9	8.0	5.7
P/B (X)	1.2	1.1	1.0	0.8
EV/EBITDA (X)	6.4	7.0	5.9	4.7
Dividend yield (%)	2.7	2.6	2.6	2.6
ROE (%)	30.8	21.5	12.7	15.8
CROCI (%)	8.5	6.3	7.5	8.6

Price performance chart



Share price performance (%)	3 month	6 month	12 month
Absolute	5.8	(2.2)	(20.8)
Rel. to India BSE30 Sensex	3.5	(5.6)	(22.1)

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 2/10/2012 close.

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Tata Steel: Summary Financials

Profit model (Rs mn)	3/11	3/12E	3/13E	3/14E	Balance sheet (Rs mn)	3/11	3/12E	3/13E	3/14E
Total revenue	1,187,531.2	1,267,877.7	1,372,625.2	1,421,451.5	Cash & equivalents	108,926.0	98,849.3	62,065.9	102,373.0
Cost of goods sold	(923,845.8)	(990,938.7)	(1,031,642.0)	(1,044,310.2)	Accounts receivable	148,162.8	173,681.9	188,030.9	194,719.4
SG&A	(154,761.0)	(198,396.1)	(246,357.6)	(252,867.5)	Inventory	240,552.4	198,187.7	229,253.8	232,068.9
R&D	0.0	0.0	0.0	0.0	Other current assets	100,045.2	93,260.2	93,260.2	93,260.2
Other operating profit/(expense)	7,756.6	5,564.5	7,612.9	8,586.2	Total current assets	597,686.4	563,979.2	572,610.7	622,421.6
EBITDA	160,829.2	138,321.4	172,409.2	206,578.0	Net PP&E	523,934.0	581,812.4	605,165.7	623,936.5
Depreciation & amortization	(44,148.2)	(54,213.9)	(70,170.8)	(73,718.1)	Net intangibles	154,737.6	154,737.6	154,737.6	154,737.6
EBIT	116,681.0	84,107.5	102,238.4	132,859.9	Total investments	78,473.4	90,135.9	99,074.0	107,746.3
Interest income	0.0	5,792.0	3,628.1	1,736.8	Other long-term assets	0.0	0.0	0.0	0.0
Interest expense	(27,700.4)	(25,854.7)	(29,924.6)	(29,308.1)	Total assets	1,354,831.4	1,390,665.1	1,431,588.1	1,508,842.1
Income/(loss) from uncons. subs.	663.6	0.0	0.0	0.0	Accounts payable	180,218.0	138,945.5	131,621.6	136,303.6
Others	8,936.8	11,662.5	8,938.1	8,672.3	Short-term debt	4,326.7	4,326.7	4,326.7	4,326.7
Pretax profits	98,581.0	75,707.2	84,880.1	113,960.9	Other current liabilities	157,391.8	157,391.8	157,391.8	157,391.8
Income tax	(32,459.0)	(30,586.7)	(26,763.4)	(31,331.5)	Total current liabilities	341,936.5	300,664.0	293,340.1	298,022.1
Minorities	602.8	993.6	(694.6)	(2,479.1)	Long-term debt	602,516.7	608,164.5	610,164.5	612,164.5
Net income pre-preferred dividends	66,724.8	46,114.1	57,422.1	80,150.3	Other long-term liabilities	45,850.1	45,850.1	45,850.1	45,850.1
Preferred dividends	0.0	0.0	0.0	0.0	Total long-term liabilities	648,366.8	654,014.6	656,014.6	658,014.6
Net income (pre-exceptionals)	66,724.8	46,114.1	57,422.1	80,150.3	Total liabilities	990,303.3	954,678.6	949,354.7	956,036.7
Post-tax exceptionals	23,102.1	38,261.1	0.0	0.0	Preferred shares	0.0	0.0	0.0	0.0
Net income	89,826.9	84,375.2	57,422.1	80,150.3	Total common equity	355,639.1	428,091.1	473,643.4	541,736.3
EPS (basic, pre-exception) (Rs)	73.55	47.82	59.55	83.12	Minority interest	8,889.0	7,895.4	8,590.0	11,069.0
EPS (basic, post-exception) (Rs)	99.01	87.50	59.55	83.12	Total liabilities & equity	1,354,831.4	1,390,665.1	1,431,588.1	1,508,842.1
EPS (diluted, post-exception) (Rs)	92.55	86.93	59.16	82.58	BVPS (Rs)	392.00	443.96	491.20	561.82
DPS (Rs)	12.69	12.37	12.31	12.50	Ratios	3/11	3/12E	3/13E	3/14E
Dividend payout ratio (%)	12.8	14.1	20.7	15.0	CROCI (%)	8.5	6.3	7.5	8.6
Free cash flow yield (%)	(11.9)	(9.0)	(5.8)	10.7	ROE (%)	30.8	21.5	12.7	15.8
Growth & margins (%)	3/11	3/12E	3/13E	3/14E	ROA (%)	7.3	6.1	4.1	5.5
Sales growth	16.0	6.8	8.3	3.6	ROACE (%)	10.8	6.3	7.7	9.8
EBITDA growth	98.2	(14.0)	24.6	19.8	Inventory days	84.4	80.8	75.6	80.6
EBIT growth	222.2	(27.9)	21.6	30.0	Receivables days	40.6	46.3	48.1	49.1
Net income growth	547.1	(6.1)	(31.9)	39.6	Payable days	59.2	58.8	47.9	46.8
EPS growth	508.0	(11.6)	(31.9)	39.6	Net debt/equity (%)	136.6	117.8	114.6	93.0
Gross margin	22.2	21.8	24.8	26.5	Interest cover - EBIT (X)	4.2	4.2	3.9	4.8
EBITDA margin	13.5	10.9	12.6	14.5	Valuation	3/11	3/12E	3/13E	3/14E
EBIT margin	9.8	6.6	7.4	9.3	P/E (analyst) (X)	6.5	9.9	8.0	5.7
Cash flow statement (Rs mn)	3/11	3/12E	3/13E	3/14E	P/B (X)	1.2	1.1	1.0	0.8
Net income pre-preferred dividends	66,724.8	46,114.1	57,422.1	80,150.3	EV/EBITDA (X)	6.4	7.0	5.9	4.7
D&A add-back	44,148.2	54,213.9	70,170.8	73,718.1	EV/GCI (X)	0.6	0.6	0.5	0.5
Minorities interests add-back	(602.8)	(993.6)	694.6	2,479.1	Dividend yield (%)	2.7	2.6	2.6	2.6
Net (inc)/dec working capital	(71,749.0)	(24,426.9)	(52,738.9)	(4,821.7)					
Other operating cash flow	(1,740.7)	(4,877.5)	(8,938.1)	(8,672.3)					
Cash flow from operations	36,780.5	70,030.0	66,610.4	142,853.4					
Capital expenditures	(101,636.1)	(112,092.3)	(93,524.1)	(92,488.9)					
Acquisitions	28,133.3	0.0	0.0	0.0					
Divestitures	0.0	38,261.1	0.0	0.0					
Others	(13,799.8)	0.0	0.0	0.0					
Cash flow from investments	(87,302.6)	(73,831.2)	(93,524.1)	(92,488.9)					
Dividends paid (common & pref)	(7,145.9)	(11,923.3)	(11,869.8)	(12,057.4)					
Inc/(dec) in debt	53,092.0	5,647.8	2,000.0	2,000.0					
Common stock issuance (repurchase)	45,568.1	0.0	0.0	0.0					
Other financing cash flows	(217.2)	0.0	0.0	0.0					
Cash flow from financing	91,297.0	(6,275.5)	(9,869.8)	(10,057.4)					
Total cash flow	40,774.9	(10,076.7)	(36,783.4)	40,307.2					

Note: Last actual year may include reported and estimated data.
Source: Company data, Goldman Sachs Research estimates.

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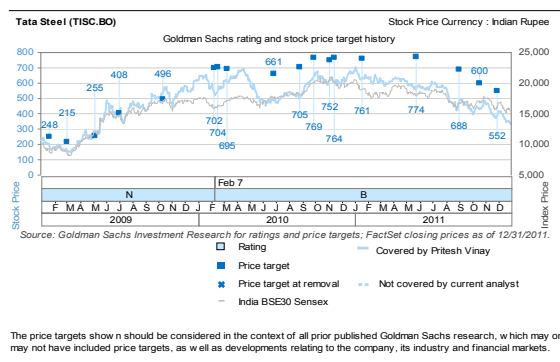
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Price target and rating history chart(s)



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