

Tata Steel (TATA IN)

Rating: BUY | CMP: Rs569 | TP: Rs770

August 14, 2018

Q1FY19 Result Update

☒ Change in Estimates | ☒ Target | ☐ Reco

Change in Estimates

	Current		Previous	
	FY19E	FY20E	FY19E	FY20E
Rating	BUY		BUY	
Target Price	770		770	
Sales (Rs. m)	16,29,907	16,89,189	15,62,889	16,19,837
% Chng.			4.3	4.3
EBITDA (Rs. m)	2,90,499	3,00,997	2,59,896	2,74,525
% Chng.			11.8	9.6
EPS (Rs.)	70.9	68.1	51.0	51.7
% Chng.			39.1	31.6

Key Financials

	FY17	FY18	FY19E	FY20E
Sales (Rs. bn)	1,123	1,313	1,630	1,689
EBITDA (Rs. bn)	170	210	290	301
Margin (%)	15.1	16.0	17.8	17.8
PAT (Rs. bn)	39	29	85	82
EPS (Rs.)	40.7	25.5	70.9	68.1
Gr. (%)	(315.3)	(37.4)	178.5	(4.0)
DPS (Rs.)	10.0	10.0	10.0	10.0
Yield (%)	1.8	1.8	1.8	1.8
RoE (%)	9.7	5.9	11.3	8.8
RoCE (%)	9.2	11.0	12.3	10.6
EV/Sales (x)	1.1	1.0	1.0	0.9
EV/EBITDA (x)	7.5	6.4	5.6	5.3
PE (x)	14.0	22.3	8.0	8.4
P/BV (x)	1.5	1.1	0.8	0.7

Key Data

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52-W High / Low	Rs.748 / Rs.493
Sensex / Nifty	37,645 / 11,356
Market Cap	Rs.651bn / \$ 9,309m
Shares Outstanding	1,126m
3M Avg. Daily Value	Rs.9491.01m

Shareholding Pattern (%)

Promoter's	33.21
Foreign	18.50
Domestic Institution	26.71
Public & Others	21.58
Promoter Pledge (Rs bn)	7.04

Stock Performance (%)

	1M	6M	12M
Absolute	1.8	(20.2)	1.1
Relative	(1.2)	(27.3)	(16.1)

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Strong outlook to allay the concerns on aggressive inorganic expansions

Tata Steel (TATA) reported Q1FY19 earnings above our estimates on the back of beat in TATA Steel Europe (TSE) earnings. Adjusted for one-off charge of Rs1.25bn for rates and taxes in domestic operations and non-cash forex translation loss of Rs5.5bn in South East Asia (SEA) financing arms, EBITDA rose 10% QoQ/44%YoY to Rs71.4bn (PLe:Rs69.5bn). Domestic operations reported 10% QoQ/62% rise in Adj. EBITDA/t to Rs17,500/t (PLe:Rs17,500/t). TSE delivered EBITDA/t of US\$100/t (PLe:US\$70) due to better availability of Hot strip mill and expansion in spreads.

Street is overly cautious on TATA's aggressive inorganic growth plans loading its B/S with high debt (Q1FY19 net debt at Rs1.03 tn). TATA is likely to acquire Bhushan Power and Steel for consideration in excess of Rs180bn. It is also looking to acquire assets in long product where it has last expanded capacity 8-9 years back. Market is treating domestic acquisitions at par with global acquisition overlooking the strong outlook on domestic market, its raw material linkages and tedious process of securing statutory clearances and land. Admittedly, it would load considerable debt on its B/S. However, the structural restructuring of Chinese mill's operating model (with profitability being the top priority), strong fundamentals of domestic market and ample growth options would drive steady return and payback on these acquired assets. We reiterate BUY with TP of Rs770, EV/EBITDA 6x FY20E.

- **Lower than expected costs drove the show:** Volumes fell 2% QoQ (↑8% YoY) to 2.97mn (PLe:2.97mn) t. Blended realisations rose 3.6% QoQ/Rs1,907 to Rs54,392 marginally below our estimate of Rs54,785. Led by lower RM cost, cost/t came below our estimate at Rs37,739 (PLe:Rs38,100); down 0.3% /Rs120 QoQ (↑2.8%/Rs1,023 YoY). EBITDA rose 8% QoQ/75% YoY to Rs52.0bn (PLe:Rs52bn). Due to interest income on inter-corporate loan to Bhushan steel, Adj PAT rose 32% QoQ/190% YoY to Rs26bn (PLe:Rs24.2bn).
- **TSE led the beat on consolidated level:** TSE volumes fell 4% QoQ (↑2% YoY) to 2.5mn (PLe:2.4mn) t. Due to higher than expected spreads, TSE's EBITDA/t came way ahead of our estimates at US\$101 (PLe:US\$70), up 44% QoQ (↑25% YoY). Impacted by higher depreciation and interest cost (due to acquisition of Bhushan steel), Adj. PAT fell 17% QoQ/↑123% YoY to Rs29bn (PLe:Rs27.4bn).
- **Key highlights of con-call:** 1) Expects to secure approvals in a month's time for supplying iron ore to Bhushan Steel and Power Ltd (BSPL) from its captive mines 2) It would supply 3mtpa of iron ore to BSPL, meeting ~50% of the requirement in FY19e 3) Expanding output capacity of Khandbandh iron ore mine by 5mn t at a capex of Rs22bn 4) BSPL posted EBITDA of Rs8.3bn in Q1 with margins at Rs9,745/t and utilisation at 62% 5) Volume guidance for BSPL at 3.6mn t in FY19 and 5mn t in 24 months 6) Maintained capex guidance for FY19 at Rs90bn (Spent Rs19.3bn in Q1FY19); includes sustenance capex of Rs6bn in BSPL and initial capex of phase-II of 5mtpa in Kalinganagar 7) Production volumes to be lower in Q2 and Q3 due to planned shutdown of Blast Furnace (BF) at UK 8) Coking coal cost to remain flat QoQ in Q2 9) Domestic realisations marginally lower by Rs500/t QoQ in Q2 10) Auto segment growing at 20% YoY; TATA has 40-45% market share

Exhibit 1: Q1FY19 Result Overview (Rs mn)

Y/e March	Q1FY19	Q1FY18	YoY gr. (%)	Q4FY18	FY19E	FY18	YoY gr. (%)
Net Sales	3,78,328	2,96,573	27.6	3,61,323	16,29,907	13,17,003	23.8
Raw Material	1,39,995	1,10,699	26.5	1,36,772	6,60,689	5,21,646	26.7
<i>% of Net Sales</i>	<i>37.0</i>	<i>37.3</i>		<i>37.9</i>	<i>40.5</i>	<i>39.6</i>	
Staff Costs	49,333	43,039	14.6	45,827	2,15,735	1,76,062	22.5
<i>% of Net Sales</i>	<i>13.0</i>	<i>14.5</i>		<i>12.7</i>	<i>13.2</i>	<i>13.4</i>	
Other Expenses	1,24,323	93,091	33.6	1,13,735	4,71,921	4,00,385	17.9
<i>% of Net Sales</i>	<i>32.9</i>	<i>31.4</i>		<i>31.5</i>	<i>29.0</i>	<i>30.4</i>	
Total Expenditure	3,13,651	2,46,828	27.1	2,96,334	13,48,346	10,98,093	22.8
EBITDA	64,677	49,745	30.0	64,989	2,81,562	2,18,911	28.6
<i>Margin (%)</i>	<i>17.1</i>	<i>16.8</i>		<i>18.0</i>	<i>17.3</i>	<i>16.6</i>	
Depreciation	18,056	15,011	20.3	15,122	76,753	59,617	28.7
Other income	3,473	1,555	123.4	2,749	7,890	9,095	(13.2)
EBIT	50,093	36,289	38.0	52,616	2,12,699	1,68,388	26.3
Interest	16,701	13,437	24.3	14,809	74,360	55,018	35.2
PBT	33,392	22,852	46.1	37,808	1,38,339	1,13,371	22.0
Extraordinary income/(expense)	(3,436)	(6,168)		1,13,761	-	96,171	
PBT (After EO)	29,956	16,684	79.6	1,51,569	1,38,339	2,09,542	(34.0)
Tax	11,037	7,405	49.0	5,761	59,531	34,054	74.8
<i>% PBT</i>	<i>36.8</i>	<i>44.4</i>		<i>3.8</i>	<i>43.0</i>	<i>16.3</i>	
Reported PAT	18,919	9,278	103.9	1,45,808	78,808	1,75,488	(55.1)
Minority interest	(173)	148	(216.5)	44,522	800	43,285	(98.2)
Share of profit/(loss) of associates	448	59	659.8	586	(1,640)	1,741	
Net Profit attributable to shareholders	19,540	9,189	112.6	1,01,872	76,367	1,33,944	(43.0)
Adjusted Net Profit attributable to shareholders	22,976	13,118	75.1	35,203	76,367	78,449	(2.7)

Source: Company, PL

Exhibit 2: Key Operating Metrics

Subsidiary performance	Q1FY19	Q1FY18	YoY gr. (%)	Q4FY18	FY19E	FY18	YoY gr. (%)
Revenue							
Indian Operations (mn USD)	2,446	2,025	20.8	2,530	10,049	9,177	9.5
UK Operations (mn USD)	2,450	2,183	12.2	2,519	9,000	9,306	(3.3)
South east asian operations (mn USD)	388	309	25.5	409	1,288	1,480	(13.0)
Adjusted EBITDA							
Indian Operations (mn USD)	756	460	64.5	747	3,049	2,447	24.6
UK Operations (mn USD)	248	194	27.9	179	600	588	2.0
South east asian operations (mn USD)	16	3	380.9	15	50	68	(26.0)
Operating Metrics (TSE)							
Sales Volume	2.5	2.4	2.1	2.6	10.0	10.0	0.1
Realisation per tonne	1,000	909	9.9	988	900	931	(3.4)
EBITDA per tonne	101	81	25.3	70	60	59	1.9
Operating Metrics (South east operations)							
Sales Volume (mn tonne)	0.6	0.6	-	0.6	2.5	2.5	(0.4)
Realisation per tonne	647	516	25.5	660	515	590	(12.7)
EBITDA per tonne	27	6	380.9	24	20	27	(25.7)

Source: Company, PL

Financials

Income Statement (Rs m)

Y/e Mar	FY17	FY18	FY19E	FY20E
Net Revenues	11,22,994	13,12,951	16,29,907	16,89,189
YoY gr. (%)	10.1	16.9	24.1	3.6
Cost of Goods Sold	3,93,049	5,21,646	6,56,310	6,80,214
Gross Profit	7,29,945	7,91,306	9,73,598	10,08,975
Margin (%)	65.0	60.3	59.7	59.7
Employee Cost	1,72,522	1,76,062	2,14,305	2,22,111
Other Expenses	(7,647)	(10,009)	-	-
EBITDA	1,70,078	2,10,299	2,90,499	3,00,997
YoY gr. (%)	113.4	23.6	38.1	3.6
Margin (%)	15.1	16.0	17.8	17.8
Depreciation and Amortization	56,729	59,617	76,753	89,549
EBIT	1,13,349	1,50,683	2,13,747	2,11,448
Margin (%)	10.1	11.5	13.1	12.5
Net Interest	50,722	55,018	74,328	74,242
Other Income	5,275	9,095	7,890	8,238
Profit Before Tax	24,660	2,00,750	1,47,309	1,45,444
Margin (%)	2.2	15.3	9.0	8.6
Total Tax	27,780	34,054	59,531	61,096
Effective tax rate (%)	112.7	17.0	40.4	42.0
Profit after tax	(3,120)	1,66,696	87,778	84,348
Minority interest	722	43,285	800	800
Share Profit from Associate	77	1,741	100	100
Adjusted PAT	39,476	29,161	85,338	81,908
YoY gr. (%)	(315.3)	(26.1)	192.6	(4.0)
Margin (%)	3.5	2.2	5.2	4.8
Extra Ord. Income / (Exp)	(43,242)	95,991	-	-
Reported PAT	(3,766)	1,25,153	85,338	81,908
YoY gr. (%)	(117.5)	(3,423.1)	(31.8)	(4.0)
Margin (%)	(0.3)	9.5	5.2	4.8
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	(3,766)	1,25,153	85,338	81,908
Equity Shares O/s (m)	970	1,145	1,203	1,203
EPS (Rs)	40.7	25.5	70.9	68.1

Source: Company Data, PL Research

Balance Sheet Abstract (Rs m)

Y/e Mar	FY17	FY18	FY19E	FY20E
Non-Current Assets				
Gross Block	12,65,617	13,99,263	20,02,887	20,52,787
Tangibles	12,65,617	13,99,263	20,02,887	20,52,787
Intangibles	-	-	-	-
Acc: Dep / Amortization	3,80,498	4,79,209	6,06,998	6,96,547
Tangibles	3,80,498	4,79,209	6,06,998	6,96,547
Intangibles	-	-	-	-
Net fixed assets	8,85,118	9,20,054	13,95,890	13,56,241
Tangibles	8,85,118	9,20,054	13,95,890	13,56,241
Intangibles	-	-	-	-
Capital Work In Progress	1,64,023	1,71,168	2,22,068	3,12,968
Goodwill	34,947	40,995	40,995	40,995
Non-Current Investments	73,258	38,249	54,249	55,399
Net Deferred tax assets	(91,442)	(95,341)	(1,42,772)	(1,55,433)
Other Non-Current Assets	57,777	2,37,984	2,47,834	2,48,184
Current Assets				
Investments	56,731	1,49,090	59,090	59,090
Inventories	2,48,038	2,83,310	3,34,912	3,47,094
Trade receivables	1,15,868	1,24,155	1,46,276	1,49,517
Cash & Bank Balance	49,211	79,379	71,140	84,526
Other Current Assets	22,424	31,742	37,542	43,042
Total Assets	17,33,332	20,97,579	26,32,052	27,19,630
Equity				
Equity Share Capital	9,702	11,450	12,032	12,032
Other Equity	3,68,491	5,97,257	8,85,073	9,52,529
Total Network	3,78,193	6,08,706	8,97,105	9,64,561
Non-Current Liabilities				
Long Term borrowings	8,30,145	9,21,471	10,60,601	10,60,601
Provisions	42,797	43,382	43,382	43,382
Other non current liabilities	49,504	44,013	44,013	44,013
Current Liabilities				
ST Debt / Current of LT Debt	-	-	-	-
Trade payables	1,85,745	2,04,138	2,49,163	2,56,810
Other current liabilities	1,27,744	1,58,897	1,72,585	1,71,598
Total Equity & Liabilities	17,33,332	20,97,579	26,32,052	27,19,630

Source: Company Data, PL Research

Cash Flow (Rs m)

Y/e Mar	FY17	FY18	FY19E	FY20E
PBT	(13,826)	2,11,682	1,47,309	1,45,444
Add. Depreciation	56,898	59,617	76,753	89,549
Add. Interest	50,722	55,018	74,328	74,242
Less Financial Other Income	5,275	9,095	7,890	8,238
Add. Other	82,020	(1,24,445)	(3,483)	(3,831)
Op. profit before WC changes	1,75,814	2,01,871	2,94,906	3,05,404
Net Changes-WC	(49,144)	(92,755)	8,187	(16,181)
Direct tax	(18,427)	(28,882)	(46,179)	(47,514)
Net cash from Op. activities	1,08,243	80,234	2,56,914	2,41,710
Capital expenditures	(85,083)	(75,202)	(90,800)	(1,40,800)
Interest / Dividend Income	2,256	3,656	3,483	3,831
Others	(7,656)	(47,857)	(97,870)	-
Net Cash from Invst. activities	(90,484)	(1,19,403)	(1,85,187)	(1,36,969)
Issue of share cap. / premium	0	90,872	35,838	-
Debt changes	28,823	42,252	(25,000)	-
Dividend paid	(9,498)	(11,800)	(13,815)	(14,452)
Interest paid	(47,328)	(51,456)	(74,328)	(74,242)
Others	2,210	(3,470)	(2,661)	(2,661)
Net cash from Fin. activities	(25,794)	66,399	(79,966)	(91,355)
Net change in cash	(8,034)	27,230	(8,238)	13,386
Free Cash Flow	31,087	5,449	1,66,114	1,00,910

Source: Company Data, PL Research

Quarterly Financials (Rs m)

Y/e Mar	Q2FY18	Q3FY18	Q4FY18	Q1FY19
Net Revenue	3,24,641	3,34,466	3,61,323	3,78,328
YoY gr. (%)	25.2	21.2	6.6	27.6
Raw Material Expenses	1,42,896	1,31,279	1,36,772	1,39,995
Gross Profit	1,81,745	2,03,187	2,24,551	2,38,333
Margin (%)	56.0	60.7	62.1	63.0
EBITDA	47,207	56,969	64,989	64,677
YoY gr. (%)	(5.1)	20.7	14.1	(0.5)
Margin (%)	14.5	17.0	18.0	17.1
Depreciation / Depletion	14,733	14,751	15,122	18,056
EBIT	32,474	42,219	49,867	46,620
Margin (%)	10.0	12.6	13.8	12.3
Net Interest	13,499	13,273	14,809	16,701
Other Income	2,532	2,259	2,749	3,473
Profit before Tax	21,240	20,049	1,51,569	29,956
Margin (%)	6.5	6.0	41.9	7.9
Total Tax	11,380	9,508	5,761	11,037
Effective tax rate (%)	53.6	47.4	3.8	36.8
Profit after Tax	9,860	10,541	1,45,808	18,919
Minority interest	120	(1,505)	44,522	(173)
Share Profit from Associates	198	898	586	448
Adjusted PAT	10,112	20,016	35,203	22,976
YoY gr. (%)	(4,996.8)	639.2	5.3	75.1
Margin (%)	3.1	6.0	9.7	6.1
Extra Ord. Income / (Exp)	(173)	(7,072)	66,669	(3,436)
Reported PAT	9,939	12,944	1,01,872	19,540
YoY gr. (%)	(1,343.3)	434.3	(1,504.9)	112.6
Margin (%)	3.1	3.9	28.2	5.2
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	9,939	12,944	1,01,872	19,540
Avg. Shares O/s (m)	971	971	971	971
EPS (Rs)	10.4	20.6	36.2	23.7

Source: Company Data, PL Research

Key Financial Metrics

Y/e Mar	FY17	FY18	FY19E	FY20E
Per Share(Rs)				
EPS	40.7	25.5	70.9	68.1
CEPS	99.2	77.5	134.7	142.5
BVPS	389.8	531.6	745.6	801.6
FCF	32.0	4.8	138.1	83.9
DPS	10.0	10.0	10.0	10.0
Return Ratio(%)				
RoCE	9.2	11.0	12.3	10.6
ROIC	(1.3)	11.0	7.9	6.6
RoE	9.7	5.9	11.3	8.8
Balance Sheet				
Net Debt : Equity (x)	1.9	1.1	1.0	1.0
Net Working Capital (Days)	58	57	52	52
Valuation(x)				
PER	14.0	22.3	8.0	8.4
P/B	1.5	1.1	0.8	0.7
P/CEPS	99.2	77.5	134.7	142.5
EV/EBITDA	7.5	6.4	5.6	5.3
EV/Sales	1.1	1.0	1.0	0.9
Dividend Yield (%)	1.8	1.8	1.8	1.8

Source: Company Data, PL Research

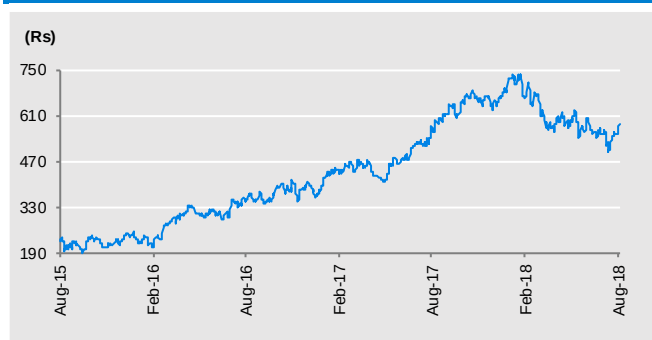
Key Operating Metrics

Y/e Mar	FY17	FY18	FY19E	FY20E
Rev. Indian Op. (US\$ m)	7,157	9,249	10,049	10,362
Rev. Corus (US\$ m)	7,764	9,306	9,000	9,000
Rev. South East (US\$ m)	1,229	1,480	1,288	1,288
EBITDA-India (US\$ m)	1,771	2,448	3,049	3,062
EBITDA-Corus (US\$ m)	702	588	600	600
EBITDA-South East (US\$ m)	79	68	50	50
Volume (mt)-India	11	12	13	13
Real./ Tonne- India (Rs)	31,911	36,066	40,361	40,367
EBITDA/Tonne- India (Rs)	10,823	12,986	16,278	15,966
SalesVol.-Corus (mt)	10	10	10	10
Real./Tonne-Corus (US\$)	781	931	900	900
EBITDA/Tonne-Corus (US\$)	71	59	60	60
Sales Vol.-South East (mt)	3	3	3	3
Real./Tonne-SEAN (US\$)	471	590	515	515
EBITDA/Tonne-SEAN (US\$)	30	27	20	20

Source: Company Data, PL Research

Price Chart

Recommendation History



No.	Date	Rating	TP (Rs.)	Share Price (Rs.)
1	21-Sep-17	BUY	750	688
2	09-Oct-17	BUY	750	691
3	31-Oct-17	BUY	750	719
4	17-Nov-17	BUY	750	687
5	13-Dec-17	BUY	750	682
6	10-Jan-18	BUY	820	772
7	09-Feb-18	BUY	835	684
8	12-Feb-18	BUY	835	684
9	15-Mar-18	BUY	835	611
10	13-Apr-18	BUY	835	595

Analyst Coverage Universe

Sr. No.	CompanyName	Rating	TP (Rs)	Share Price (Rs)
1	ACC	BUY	1,750	1,311
2	Ambuja Cement	Accumulate	250	208
3	Coal India	BUY	340	261
4	Heidelberg Cement India	BUY	200	159
5	Hindalco Industries	Accumulate	285	223
6	Hindustan Zinc	Accumulate	340	277
7	Jindal Steel & Power	BUY	305	204
8	JK Lakshmi Cement	Hold	360	330
9	JSW Steel	BUY	450	317
10	NMDC	Accumulate	145	105
11	Shree Cement	Hold	17,235	15,978
12	Steel Authority of India	Hold	86	80
13	Tata Steel	BUY	727	566
14	The Ramco Cements	Hold	735	693
15	Ultratech Cement	Hold	4,000	3,849

PL's Recommendation Nomenclature (Absolute Performance)

Buy	: > 15%
Accumulate	: 5% to 15%
Hold	: +5% to -5%
Reduce	: -5% to -15%
Sell	: < -15%
Not Rated (NR)	: No specific call on the stock
Under Review (UR)	: Rating likely to change shortly

ANALYST CERTIFICATION

(Indian Clients)

We/I, Mr. Kamlesh Bagmar- CA, Mr. Amit Khimesra- MBA Research Analysts, authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

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