

Management meet

Metals

Target price Rs215

Earnings revision

(%)	FY19E	FY20E
Sales	(1.4)	1.1
EBITDA	(6.8)	(5.3)

Target price revision

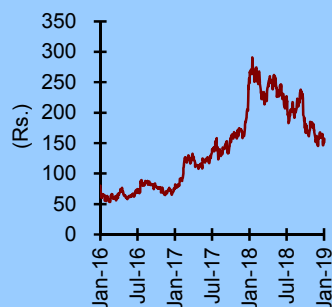
Rs215 from Rs270

Shareholding pattern

	Mar '18	Jun '18	Sep '18
Promoters	58.7	58.7	58.7
Institutional investors	28.6	28.8	29.0
MFs and UTI	6.9	6.8	8.2
FIs/Insurance	2.5	2.8	2.5
FIs	19.2	19.2	18.3
Others	12.7	12.5	12.3

Source: BSE

Price chart



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INDIA

Jindal Steel & Power

BUY

Maintained

Rs152

Continues to focus on deleveraging

Jindal Steel and Power (JSPL) management highlighted the stress points emerging from i) contraction in spreads in domestic business, ii) ramp up pangs leading to domestic volume miss in Q3FY19E, iii) sharp contraction in spreads in the Oman business, and iv) continued shortage of coal impeding full operations of Tamnar 1. All these make Q3FY19E EBITDA lot less prospective with a 12.9% QoQ drop expected now. Also, what seems consuming some part of management bandwidth is handling foreign currency loans (~US\$2bn) as Oman EBITDA endures the impact of compressing spreads. While interest servicing on foreign loans is still being made possible from Oman EBITDA, efforts are required to perhaps ensure better sustainability. Management continues to guide for Rs90bn of debt reduction (over FY19/20E) albeit conceding the risks to commodity price volatility to the baseline forecast. Capex remains pegged at Rs10bn p.a. We have rebased FY19/20E domestic steel volumes to 5/6mnte from 5.5/6.5mnte earlier and adjusted for the sharp decline in Oman EBITDA. While acknowledging cascading near-term risks to earnings and valuations, continued focus on debt deleveraging, inexpensive valuations (~0.5x FY20E book) allow us to be relatively more constructive on the name in the sector. We maintain BUY with a revised target of Rs 215/share.

- **Miss in Angul volumes leads to correction in earnings expectations.** Production guidance for FY20E remains at 6.5mnte (factors 3.3mnte from Raigarh and 3.2mnte from Angul). Q3FY19 production miss was due to a combination of ramp-up issues and a weak market. We have reduced our FY20E volume target to 6mnte from 6.5mnte.
- **Oman witnessing significant spread compression.** This is mainly due to sticky pellet prices as long products witness significant correction, leading to meaningful normalisation of EBITDA/te. We have normalised Oman earnings and factor in ~US\$100/te spreads. This has corresponding impact on earnings and valuations. While interest servicing is still smooth, management is actively engaged to ensure that further spread compression in Oman does not lead to any material stress in overseas debt servicing.
- **JPL continues to face coal shortage.** E-auction markets are extremely tight hence not allowing for continuous operations of two 500 MW units of Tamnar 1. ~ 850MW PPA out of Tamnar 2 continues to generate majority of the JPL EBITDA.
- **Deleveraging target of Rs90bn over two years** (Rs40bn in FY19 of which Rs22bn has been achieved in H1FY19) from operational cash flows. This will have to be linked to spreads. At current spreads it is unlikely that the target for FY19E will be met.
- **We moderate our Q3FY19 estimates** to factor in softer Oman operations. While near-term spread compression in Q4FY19E will be partly offset by reduction in iron ore costs, over the longer run, higher blended NSR and cost improvements through Angul ramp-up can prop EBITDA up by ~Rs1,500/te.

Market Cap	Rs147bn/US\$2.1bn
Reuters/Bloomberg	JNSP.BO/JSP IN
Shares Outstanding (mn)	967.9
52-week Range (Rs)	291/146
Free Float (%)	31.3
FII (%)	18.3
Daily Volume (US\$'000)	32,814
Absolute Return 3m (%)	(13.3)
Absolute Return 12m (%)	(39.0)
Sensex Return 3m (%)	5.8
Sensex Return 12m (%)	6.4

Year to March	FY18	FY19E	FY20E	FY21E
Revenue (Rsmn)	2,79,727	3,76,352	4,07,583	4,36,874
Net Income (Rsmn)	(8,217)	3,871	10,466	13,863
EPS (Rs)	(9.0)	3.8	10.3	13.6
% ChgYoY	NM	NM	170.4	32.5
P/E (x)	NM	39.9	14.8	11.1
CEPS (Rs)	32.8	49.1	55.5	57.4
EV/E (x)	9.1	7.0	6.0	5.4
Dividend Yield	-	-	-	-
RoCE (%)	3.2	5.4	6.3	7.4
RoE (%)	(3.4)	1.2	3.7	4.9

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Q3FY19 result preview

Standalone EBITDA is expected to decrease 10% QoQ and consolidated EBITDA to decline 12.9% QoQ. We reduce our earnings assumptions for Oman and India steel business. Oman EBITDA/te is expected to come down to US\$72/te (vs US\$150/92/te in Q3FY18 and Q2F19). This is mainly due to sticky pellet prices as long products witness significant correction, leading to meaningful normalisation of EBITDA/te.

Table 1: JSPL's standalone result preview

(Rs mn)	Q3FY19E	Q3FY18	% chg YoY	Q2FY19	% chg QoQ
Net sales	64,164	43,267	48.3	68,851	(6.8)
Other operating income	1,100	576	90.8	373	194.8
Total sales	65,264	42,721	52.8	68,488	(4.7)
Change in stock	-	-	NA	939	NA
Consumption of raw materials	29,351	16,981	72.8	29,600	(0.8)
Purchase of traded goods	750	269	178.4	2,299	(67.4)
Employee costs	1,607	1,300	23.6	1,607	-
Other expenditure	12,240	16,083	(23.9)	15,140	(19.2)
Total costs	52,201	33,511	55.8	53,967	(3.3)
EBITDA	13,063	9,211	41.8	14,521	(10.0)
Margin (%)	20.0	21.6		21.2	
Depreciation	5,825	4,650	25.3	5,825	-
EBIT	7,238	4,560		8,695	(16.8)
Interest expense	6,758	5,942	13.7	6,758	-
Other income	-	-		-	
Extraordinary / Forex (gain)/Loss	-	-		(2,555)	
PBT (recurring)	481	(1,382)	NA	1,938	(75.2)
PBT (reported)	481	(1,382)	NA	4,492	(89.3)
Tax (recurring)	144	(644)	NA	666	
Tax (reported)	144	(644)	NA	666	
PAT (recurring)	336	(737)	NA	1,272	(73.6)
PAT (reported)	336	(737)	NA	3,827	(91)

Source: Company data, I-Sec research

Table 2: JSPL's consolidated result preview

(Rs mn)	Q3FY19E	Q3FY18	% chg YoY	Q2FY19	% chg QoQ
Net sales	85,635	70,160	22.1	99,955	(14.3)
Other operating income	650	888	(26.8)	604	7.5
Total sales	86,285	69,926	23.4	99,823	(13.6)
Change in stock	-	-	NA	785	
Consumption of raw materials	36,483	23,017	58.5	39,994	(8.8)
Purchase of traded goods	800	544	47.0	2,796	(71.4)
Employee costs	3,691	2,413	52.9	2,686	37.4
Other expenditure	15,093	21,076	(28.4)	23,337	(35.3)
Total costs	67,065	53,861	24.5	77,749	(13.7)
EBITDA	19,221	16,065	19.6	22,074	(12.9)
Margin (%)	22.3	23.0		22.1	
Depreciation	10,100	9,632	4.9	10,314	(2.1)
EBIT	9,121	6,433	41.8	11,760	(22.4)
Interest expense	8,929	9,670	(7.7)	10,858	(17.8)
Other income	60	10		9	
Extraordinary / Forex (gain)/Loss	-	-		(2,555)	
PBT (recurring)	251	(3,227)	NA	911	NA
PBT (reported)	251	(3,227)	NA	3,466	NA
Tax (recurring)	43	(457)	NA	674	
Tax (reported)	43	(457)	NA	674	
PAT (recurring)	208	(2,770)	NA	237	NA
PAT (reported)	208	(2,770)	NA	2,792	NA
Minority interest	(61)	67		645	
Share of associates	45	43		-	
PAT after minority (recurring)	192	(2,660)	NA	882	
PAT after minority (reported)	192	(2,660)	NA	3,437	

Source: Company data, I-Sec research

Change in earnings estimates

We introduce earnings estimates for FY21. We rebase FY19/20E domestic steel volumes to 5/6mnte from 5.5/6.5mnte and adjust for the sharp decline in Oman EBITDA.

Table 3: Earnings revision

(Rs mn)	New		Old		% Chg	
	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
Revenues	3,76,352	4,07,583	3,81,589	4,03,341	(1.4)	1.1
EBITDA	85,199	92,177	91,458	97,345	(6.8)	(5.3)

Source: Company data, I-Sec research

Change in valuation

Table 4: Valuation methodology (new)

(Rs/share)	Methodology	FY20E
Steel business		128
Standalone +	6.0x EV/EBITDA	128
Contribution from Angul		
Power business		66
Tamnar I	FCFE	15
Tamnar II	FCFE	42
Cash at JPL		9
Overseas assets		20
Shadeed	5.5x EV/EBITDA	48
South Africa	5x EV/EBITDA	(0)
Mozambique + Others	5x EV/EBITDA	(3)
Wollongong (72.92% ownership)	5x EV/EBITDA	(24)
Total		215

Source: I-Sec research

Table 5: Valuation methodology (old)

(Rs/share)	Methodology	FY20E
Steel business		176
Standalone +	6.0x EV/EBITDA	176
Contribution from Angul		
Power business		67
Tamnar I	FCFE	15
Tamnar II	FCFE	42
Cash at JPL		9
Overseas assets		27
Shadeed	5.5x EV/EBITDA	60
South Africa	5x EV/EBITDA	(5)
Mozambique + Others	5x EV/EBITDA	(4)
Wollongong (72.92% ownership)	5x EV/EBITDA	(24)
Total		270

Source: I-Sec research

Risks: Inability to source coal over the longer run and gradual increase in leverage consequently can make JPL forego the benefit of lower fixed costs. This remains the biggest risk to JSPL's business model. The upside risks could be in the form of quick resolution of coal availability issues and a favourable restructuring package bargained from banks.

Summary financials

Table 6: Profit & loss statement

(Rs mn, year ending March 31)

	FY18	FY19E	FY20E	FY21E
Operating Income (Sales)	2,79,727	3,76,352	4,07,583	4,36,874
Operating Expenses	2,15,036	2,91,152	3,15,406	3,37,698
EBITDA	64,691	85,199	92,177	99,175
% margins	23.1	22.6	22.6	22.7
Depreciation	38,830	41,962	41,355	39,762
Gross Interest	38,657	37,863	35,252	34,467
Other Income	29	483	743	1,240
Recurring PBT	(12,767)	5,857	16,314	26,187
Add: Extraordinary	(5,874)	-	-	-
Less: Taxes	(2,398)	2,196	4,729	10,122
Net Income (Reported)	(14,091)	3,871	10,466	13,863
Recurring Net Income	(8,217)	3,871	10,466	13,863

Source: Company data, I-Sec research

Table 7: Balance sheet

(Rs mn, year ending March 31)

	FY18	FY19E	FY20E	FY21E
Assets				
Total Current Assets	1,56,572	1,60,973	1,91,099	1,98,969
of which cash & cash eqv.	4,786	2,466	28,994	32,891
Total Current Liabilities & Provisions	83,788	77,609	81,065	81,384
Net Current Assets	72,784	1,00,162	1,26,937	1,34,598
Investments	1,458	1,458	1,458	1,458
Strategic/Group	1,458	1,458	1,458	1,458
Other Marketable	-	-	-	-
Net Fixed Assets	7,28,353	7,09,790	6,82,378	6,72,558
Capital Work-in-Progress	49,775	53,401	53,401	53,401
Goodwill	5,922	5,922	5,922	5,922
Total Assets	8,08,516	8,17,331	8,16,694	8,14,536
Liabilities				
Borrowings	4,49,982	4,55,049	4,42,738	4,24,428
Deferred Tax Liability	50,284	50,284	50,284	50,284
Minority Interest	4,403	4,282	5,489	7,778
Equity Share Capital	1,016	1,016	1,016	1,016
Face Value per share (Rs)	1	1	1	1
Reserves & Surplus	3,02,830	3,06,701	3,17,167	3,31,030
Net Worth	3,03,846	3,07,717	3,18,183	3,32,046
Total Liabilities	8,08,516	8,17,331	8,16,696	8,14,536

Source: Company data, I-Sec research

Table 8: Cashflow statement

(Rs mn, year ending March 31)

	FY18	FY19E	FY20E	FY21E
Operating Cashflow	66,991	45,141	52,197	54,587
Working Capital Changes	10,252	(12,900)	(142)	(3,654)
Capital Commitments	(25,767)	(23,400)	(13,942)	(29,942)
Free Cashflow	51,476	8,842	38,113	20,991
Cashflow from Investing Activities	11,455	483	743	1,240
Issue of Share Capital	12,199	-	-	-
Buyback of shares	-	-	-	-
Inc (Dec) in Borrowings	(29,809)	5,067	(12,311)	(18,311)
Dividend paid	-	-	-	-
Extraordinary Items	-	-	-	-
Chg. in Cash & Bank balance	174	(2,277)	26,343	1,580

Source: Company data, I-Sec research

Table 9: Key ratios

(Year ending March 31)

	FY18	FY19E	FY20E	FY21E
Per Share Data (Rs)				
EPS(Basic Recurring)	(8.1)	3.8	10.3	13.6
Diluted Recurring EPS	(9.0)	3.8	10.3	13.6
Recurring Cash EPS	32.8	49.1	55.5	57.4
Dividend per share (DPS)	-	-	-	-
Book Value per share (BV)	325	329	341	355
Growth Ratios (%)				
Operating Income	29.2	34.5	8.3	7.2
EBITDA	37.4	31.7	8.2	7.6
Recurring Net Income	NM	NM	216.4	38.7
Diluted Recurring EPS	NM	NM	170.4	32.5
Diluted Recurring CEPS	NM	49.7	13.1	3.5
Valuation Ratios (x)				
P/E	NM	39.9	14.8	11.1
P/CEPS	4.6	3.1	2.7	2.6
P/BV	0.47	0.5	0.4	0.4
EV / EBITDA	9.1	7.0	6.0	5.4
EV / Operating Income	2.1	1.6	1.4	1.2
EV / Operating CF	7.6	18.4	10.7	10.5
Operating Ratios (%)				
Raw Material/Sales	17.4	12.8	11.8	11.0
Other Income / PBT	(0.2)	8.2	4.6	4.7
Effective Tax Rate	12.9	37.5	29.0	38.7
NWC / Total Assets	8.4	12.0	12.0	12.5
Inventory Turnover (days)	164.5	189.3	203.0	218.3
Receivables (days)	20.4	16.4	16.3	16.5
Payables (days)	133.8	132.1	101.2	91.8
D/E Ratio (x)	1.6	1.6	1.5	1.4
Profitability Ratios (%)				
Rec. Net Income Margins	(3.7)	1.0	2.8	3.7
RoCE	3.2	5.4	6.3	7.4
RoNW	(3.4)	1.2	3.7	4.9
Dividend Payout Ratio	-	-	-	-
Dividend Yield	-	-	-	-
EBITDA Margins	23.1	22.6	22.6	22.7

Source: Company data, I-Sec research

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ANALYST CERTIFICATION

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