

Tata Steel

BUY

Maintained

Rs413

Strength in outlook overshadows suboptimal Q1

Tata Steel has reported adjusted consolidated EBITDA of Rs10.4bn against consensus of Rs12.9bn. While standalone numbers were broadly in-line, Tata Steel Europe (TSE) disappointed with EBITDA loss of US\$42/te (expected EBITDA loss of US\$6/te). TSE EBITDA has gains on account of sales of emission rights and wage support from European and UK government, while exchange fluctuations impacted. Lower volumes in standalone operations (down 30% YoY) impacted EBITDA. Management did highlight Rs20bn in costs remain unabsorbed due to lower volumes i.e operating leverage impact. FCF generation has been very impressive at Rs7bn for the group broken into Rs16.8bn in India and Rs9.8bn overseas. This has helped maintain net debt QoQ. Tata Steel remains our top pick, as earnings tailwind (domestic price increases + impending price increase in Europe) and elevated net debt to market cap augurs well. Maintain BUY.

- ▶ **Indian operations reported an in-line print.** Q1FY21 sales volumes in India declined 27% QoQ due to nationwide lockdown amid Covid-19 outbreak; exports were significantly ramped to 1.46mnte by tapping new markets. Auto volumes fell to 0.08mnte from a quarterly run-rate of 0.5mnte. Crude steel production decreased by 37% QoQ as capacity utilisation was curtailed in Apr'20 due to the lockdown, before gradually ramping back from mid-May'20 onwards. With relaxation in lockdown measures, overall deliveries in June'20 improved significantly to ~115% of FY20 average monthly overall deliveries; domestic deliveries in Jun'20 reached ~75% of FY20 average monthly domestic deliveries. Exceptional items in Q1FY21 primarily include gain in fair valuation of preference shares held at Tata Steel BSL amounting to Rs20.3bn.
- ▶ **European EBITDA disappointed.** Oversupply in European steel markets led to adverse product mix and thereby, fall in revenue and profitability. Continuous improvement from transformation programme, careful cost management and wage support from European and UK governments helped limit the EBITDA loss at £67mn. Tata continues to engage with European and UK governments to seek short and long-term support. Q1FY21 EBITDA has been supported by i) carbon credit sales and ii) wage support from EU and UK governments while forex has created a negative contribution of ~US\$13/te as per our calculation. Steel demand recovery in EU is slower; overall 2020 demand is expected to decline by about 16%.
- ▶ **Maintained flat net debt QoQ; maintain BUY and top pick.** Q1FY21 was exceptional and Tata fared poorly vis-à-vis peers in its cost control efforts and faced the highest adverse impact of mix deterioration due to high dependence on autos. TSE remains as unpredictable as ever, yet tailwinds exist in the form of impending price hikes in the region. Growth capex has been curtailed. With reviving domestic prices, improved mix, resilient iron ore prices and sanguine balance sheet management can help Tata meaningfully outperform peers (JSWS, JSPL).

Market Cap	Rs470bn/US\$6.3bn	Year to March	FY19	FY20	FY21E	FY22E
Reuters/Bloomberg	TATA.BO/TATA IN	Revenue (Rs mn)	1,800,826	1,398,167	1,285,334	1,719,204
Shares Outstanding (mn)	1,126.5	Net Income (Rs mn)	104,044	64,716	(28,751)	58,051
52-week Range (Rs)	502/254	EPS (Rs)	86.4	53.7	(23.9)	48.2
Free Float (%)	66.9	% Chg YoY	175.5	(37.8)	(144.4)	(301.9)
FII (%)	11.7	P/E (x)	4.8	7.7	(17.3)	8.6
Daily Volume (US\$/'000)	70,882	CEPS (Rs)	136.4	119.1	41.5	114.4
Absolute Return 3m (%)	53.2	EV/E (x)	5.0	8.9	12.2	6.5
Absolute Return 12m (%)	21.5	Dividend Yield (%)	2.1	2.1	2.1	2.1
Sensex Return 3m (%)	20.5	RoCE (%)	14.3	6.0	3.0	8.9
Sensex Return 12m (%)	4.9	RoE (%)	14.5	8.6	(5.0)	7.6

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Q1FY21 result review

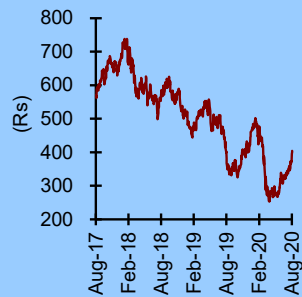
Metals

Target price: Rs594

Shareholding pattern

	Dec '19	Mar '20	Jun '20
Promoters	33.1	34.4	34.4
Institutional investors	44.6	42.1	41.6
MFs and others	14.1	14.3	13.6
FIs/Banks	0.3	0.3	0.3
Insurance Cos	14.8	15.1	16.0
FII	15.4	12.4	11.7
Others	22.3	23.5	24.0

Price chart



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Table 1: Tata Steel's consolidated Q1FY21 result review

Adjusted EBITDA at Rs10.4bn. Adjusted for fair value changes on account of exchange rate movement in investments in Tata Steel Holdings and revaluation in gain/loss on external/internal company debts/ receivables at TS Global Holdings.

A reason for lower other expenses QoQ has been shown as gain on sales of emission rights.

(Rs mn)	Q1FY21	Q1FY20	% Chg YoY	Q4FY20	% Chg QoQ
Net Sales	242,885	359,471	(32.4)	337,700	(28.1)
Expenses	237,830	305,702	(22.2)	291,231	(18.3)
Inc./Dec in stock	7,862	(23,645)		(15,405)	
Purchase of steel	6,085	16,354		10,689	
Raw materials	90,058	144,912		122,268	
Total Raw materials	104,005	137,621		117,552	
Staff expenses	45,456	48,994		47,350	
Other Expenditure	88,369	119,087		126,329	
Total Expenditure	237,830	305,702	(22.2)	291,231	(18.3)
EBITDA	5,055	53,769	(90.6)	46,469	(89.1)
<i>Margins (%)</i>	<i>2.1</i>	<i>15.0</i>		<i>13.8</i>	
Other Income	1,926	2,511	(23.3)	13,159	
Interest	19,983	18,064	10.6	19,251	3.8
Depreciation	21,108	20,828	1.3	22,241	(5.1)
Operational PBT	(34,110)	17,387	(296.2)	18,136	
ExtraOrdinary	584	160	-	(34,059)	
PBT	(33,526)	17,547		(15,923)	
Tax	12,715	11,238		(2,633)	
PAT	(46,242)	6,309		(13,290)	
Adj.PAT	(46,825)	6,149	(861.5)	20,769	
Minority Interest	2,356	100		1,405	
Share of Associates	150	522		928	
Adjusted PAT excluding dis. Operations	(49,031)	23,502		7,389	

Source: Company data, I-Sec research

Table 2: Tata Steel's standalone Q1FY21 result review

(Rs mn)	Q1FY21	Q1FY20	% Chg YoY	Q4FY20	% Chg QoQ
Net Sales	93,388	160,913	(42.0)	142,114	(34.3)
Other Operating Income	1,929	2,786	(30.8)	5,125	(62.4)
Expenses					
Total Raw materials	25,614	47,281	(45.8)	33,577	(23.7)
Staff expenses	13,097	13,523	(3.2)	13,708	(4.5)
Other Expenditure	42,166	60,543	(30.4)	58,343	(27.7)
Total Expenditure	80,877	121,347	(33.4)	105,628	(23.4)
EBITDA	12,510	39,567	(68.4)	36,487	(65.7)
<i>Margin (%)</i>	<i>13.4</i>	<i>24.6</i>		<i>25.7</i>	
Other Income	1,212	1,778	(31.9)	714	69.8
Interest	9,083	7,231	25.6	8,040	13.0
Depreciation	9,693	9,677	0.2	10,023	(3.3)
Operational PBT	(5,054)	24,437	NM	19,138	NM
Extraordinary Exp.	20,589	(408)		(20,095)	
Rep. PBT	15,535	24,030		(957)	
Tax	3,602	8,642		3,411	
PAT	11,933	15,388		(4,368)	
Adj.PAT	(8,656)	15,796	NM	15,727	NM

Source: Company data, I-Sec research

Table 3: Tata Steel's standalone volumes, realisations and EBITDA

Rs mn	Q1FY21	Q1FY20	YoY (%)	Q4FY20	% Chg QoQ
Net Sales	93,388	160,913	(42.0)	142,114	(34.3)
EBITDA	12,510	39,567	(68.4)	36,487	(65.7)
Volumes (mt)	2.11	3.01	(29.8)	2.91	(27.6)
Realisations (Rs/te)	43,346	52,586	(17.6)	47,027	(7.8)
EBITDA (Rs/te)	5,929	13,158	(54.9)	12,526	(52.7)

Source: Company data, I-Sec research

Table 4: Tata Steel Europe's volumes, realisations and EBITDA

US\$ Mn	Q1FY21	Q1FY20	YoY (%)	Q4FY20	% Chg QoQ
Net Sales	1,479	2,084	(29.0)	1,876	(21.2)
EBITDA	(82)	9	NM	9	NM
Volumes (mnte)	2.0	2.3	(12.4)	2.4	(17.2)
Realisations (US\$/te)	747	922	(19.0)	785	(4.8)
EBITDA (US\$/te)	(42)	4	NM	4	NM

Source: Company data, I-Sec research

Tata Steel valuations and assumptions

We maintain BUY with an unchanged target price of Rs594/share. We continue to maintain our valuation methodology at 1x 1-year forward P/B (FY22E).

Key risks to our call are not earnings-linked. We would continue to highlight the irrelevance of earnings-based analysis in the sector. We have subjected FY21E to a heavy loss, just to highlight the relative constancy of the book value and the predictability it imparts to our valuation methodology.

Table 5: Tata Steel Europe estimates

(US\$mn)	FY19	FY20	FY21E	FY22E
Net sales	9,274	7,896	5,969	8,167
Sales volume (mnte)	9.6	9.3	7.5	10.2
Realization (US\$/te)	962	850	796	801
EBITDA	779	(93)	(60)	478
EBITDA (US\$/te)	81	(10)	(8)	47

Source: Company data, I-Sec research

Table 6: Tata Steel India estimates

(Rs mn)	FY19	FY20E	FY21E	FY22E
Net Sales	706,109	604,360	505,175	702,493
Sales volume (mnte)	12.7	12.3	9.9	13.3
Realisations/te	55,599	49,039	48,005	51,824
EBITDA (Rs/te)	16,191	12,059	11,328	12,646

Source: Company data, I-Sec research

Financial summary

Table 7: Profit & loss statement

(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Operating Income	1,800,826	1,398,167	1,285,334	1,719,204
Operating Expenses	1,282,857	1,223,536	1,153,313	1,471,784
EBITDA	293,833	174,631	132,021	247,420
% margins	16.3	12.5	10.3	14.4
D&A expense	73,418	84,407	84,407	85,440
Gross Interest	76,601	75,335	80,000	90,707
Other Income	14,206	18,435	8,000	8,000
Recurring PBT	158,020	33,324	(24,386)	79,273
Add: Extraordinary	(1,210)	(37,521)	-	-
Less: Taxes	67,184	(25,684)	10,073	26,930
Recurring Net Income	104,044	64,716	(28,751)	58,051
Reported Net Income	90,983	11,725	(32,580)	54,222

Source: Company data, I-Sec research

Table 8: Balance sheet

(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Assets				
Total Current Assets	639,834	615,380	609,214	801,784
4,11,041	33,412	80,547	80,901	156,081
Total Current Liabilities	364,837	364,738	349,318	422,241
Net Current Assets	274,997	250,642	259,896	379,543
Investments	57,382	62,852	62,852	62,852
Strategic/Group	32,133	28,533	28,533	28,533
Other Marketable	25,249	34,319	34,319	34,319
Net Fixed Assets	1,390,866	1,414,432	1,409,289	1,406,604
Capital Work-in-Progress	186,413	194,968	177,963	187,963
Goodwill	39,966	40,545	40,545	40,545
Total Assets	1,763,211	1,853,969	1,858,080	1,975,042
Liabilities				
Borrowings	1,128,500	1,270,569	1,321,520	1,398,520
Deferred Tax Liability	116,509	79,911	79,911	79,911
Minority Interest	23,645	25,866	22,037	18,208
Equity Share Capital	12,043	12,043	12,043	12,043
Face Value per share (Rs)	10	10	11	11
Reserves & Surplus	654,458	700,970	657,959	701,751
Net Worth	666,501	713,013	670,003	713,794
Total Liabilities	1,763,211	1,853,969	1,858,080	1,975,042

Source: Company data, I-Sec research

Table 9: Cashflow statement

(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Operating Cashflow	150,036	83,918	41,948	129,782
Working Capital				
Changes	25,905	41,962	(8,901)	(44,466)
Capital Commitments	(430,370)	(140,665)	(79,264)	(82,756)
Free Cashflow	(254,430)	(14,785)	(46,217)	2,560
Cashflow from Investing Activities	138,261	(4,638)	8,000	8,000
Issue of Share Capital	(60)	1,875	-	-
Buyback of shares	-	-	-	-
Inc (Dec) in Borrowings	79,906	76,073	50,950	77,000
Dividend paid	(14,239)	(18,152)	(10,431)	(10,431)
Extraordinary Items	-	-	-	-
Chg. in Cash & Bank balances	(45,477)	39,438	56	74,883

Source: Company data, I-Sec research

Table 10: Key ratios

(Year ending March 31)

	FY19	FY20	FY21E	FY22E
Per Share Data (Rs)				
EPS(Basic Recurring)	86.4	53.7	(23.9)	48.2
Diluted Recurring EPS	86.4	53.7	(23.9)	48.2
Recurring Cash EPS	136.4	119.1	41.5	114.4
Dividend per share (DPS)**	8.7	8.7	8.7	8.7
Adj. BV/share (BV)*	520.2	558.4	522.7	559.0
Growth Ratios (%)				
Operating Income	36.3	(22.4)	(8.1)	33.8
EBITDA	34.2	(40.6)	(24.4)	87.4
Valuation Ratios (x)				
P/E	4.8	7.7	(17.3)	8.6
P/CEPS	3.0	3.5	10.0	3.6
P/BV	0.7	0.7	0.7	0.7
EV / EBITDA	5.0	8.9	12.2	6.5
EV / Operating Income	0.8	1.1	1.3	0.9
EV / Operating FCF	8.4	12.4	48.6	18.9
Operating Ratios (%)				
Raw Material/Sales	45.2	54.1	48.0	48.6
SG&A/Sales	10.7	11.2	12.5	8.1
Other Income / PBT	9.0	55.3	(32.8)	10.1
NWC / Total Assets	42.8	612.0	(41.3)	34.0
Inventory Turnover (days)	13.7	9.2	9.6	11.3
Receivables (days)	102.3	106.3	122.0	114.0
Payables (days)	23.3	20.1	23.9	30.1
D/E Ratio (x)	103.8	108.8	124.1	128.8
Profitability Ratios (%)				
Rec Net Income Margins	5.0	4.2	(2.7)	3.0
RoCE	14.3	6.0	3.0	8.9
RoNW	14.5	8.6	(5.0)	7.6
Dividend Payout Ratio	10.0	16.1	(36.3)	18.0
Dividend Yield	2.7	2.7	2.7	2.7
EBITDA Margins	16.3	12.5	10.3	14.4

Source: Company data, I-Sec research

* Adj. for goodwill. ** On fully diluted no of shares

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