

November 09, 2010

Key Data	₹
CMP (₹)	371
Target Price (₹)	371
Bloomberg code	TTSP IN
Reuters Code	TTSP.BO
BSE Code	513010
NSE Code	TATASPONGE
Face Value (₹)	10
Market Cap. (₹ mn)	5,713
52 Week High (₹)	415
52 Week Low (₹)	215
Avg. Daily Volume (6m)	91,582

Shareholding Patten as on Sept 2010	%
Promoters	43.7
Mutual Funds	2.8
Banks & Financial Institution	4.1
FII's	6.2
Corporate Bodies	6.6
Individuals	36.7
Total	100

## Tata Sponge Iron Ltd

### Q2FY11 Result

TSIL reported revenue growth of 53% to ₹1,759 million YoY on account of improvement in sponge iron realisation. EBITDA margin declined to 11% from 23% YoY on account of increase in raw material cost (due to ₹142.1 million adjustment on account of revision in prices pertaining to previous quarter). PAT declined 29% YoY to ₹104 million. We maintain "HOLD" rating on TSIL, with a revised target of ₹371.

### Key Highlights

- Revenue growth of 53% YoY was higher than our expectation due to improvement in sponge iron realisation by 28% YoY to INR14,850/tonne.
- Sponge iron production grew 18% YoY to 101,500, whereas capacity utilisation was 104% due to better operating performance and demand.
- However, raw material cost increased 94% YoY on account of ₹142.1 adjustment for revision in iron price hike pertaining to Q1FY11 quarter.
- High raw material cost resulted in lower EBITDA margin of 11% in Q2FY11 and EBITDA declined by 27% YoY to ₹195 million.
- Similarly, PAT declined by 29% to ₹104 million YoY.
- Without the adjustment in raw material cost, Q2FY11 was ahead of our expectation, where EBITDA increased by 26% YoY to ₹337 million and EBITDA margin to 19% from actual 11%. Similarly, PAT increased 69% YoY to ₹246 million and PAT margin to 14% from actual 6%.

### Quarterly Financials

Particulars (₹mn)	Q2FY11	Q2FY10	YoY % Change	Q1FY11	QoQ % Change
Net Sales	1,759	1,149	53%	1,414	24%
Total Expenditure	1,597	903	77%	993	61%
Operating Profit	161	247	-35%	421	-62%
Other income	33	20	70%	14	140%
EBITDA	195	266	-27%	435	-55%
<b>Margin %</b>	<b>11%</b>	<b>23%</b>		<b>31%</b>	
Depreciation	46	49	-5%	47	-1%
Interest	-	-		-	
PBT	148	217	-32%	388	-62%
Tax	44	71	-38%	129	-66%
% to PBT	30%	33%		33%	
PAT	104	146	-29%	259	-60%
<b>Margin %</b>	<b>6%</b>	<b>13%</b>		<b>18%</b>	
EPS	6.8	9.5	-29%	16.8	-60%

Source: ACMIIL Research, Company

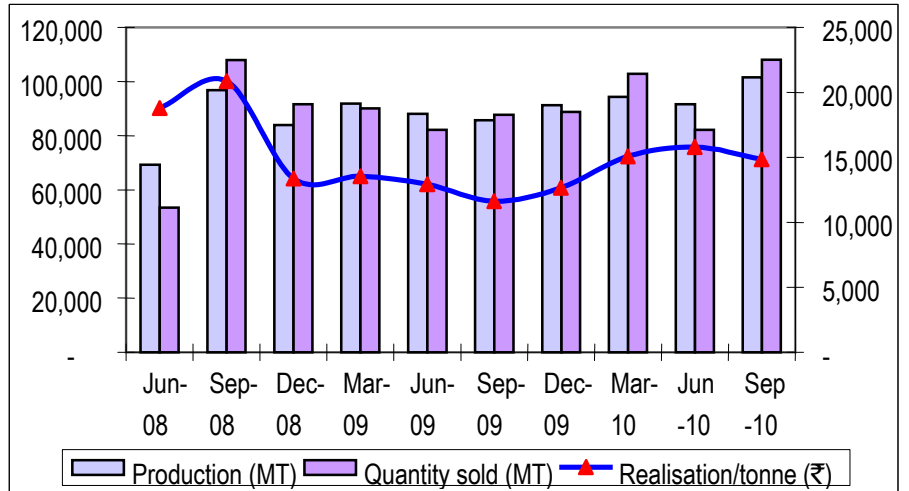
### Analyst

Deepak Chitroda

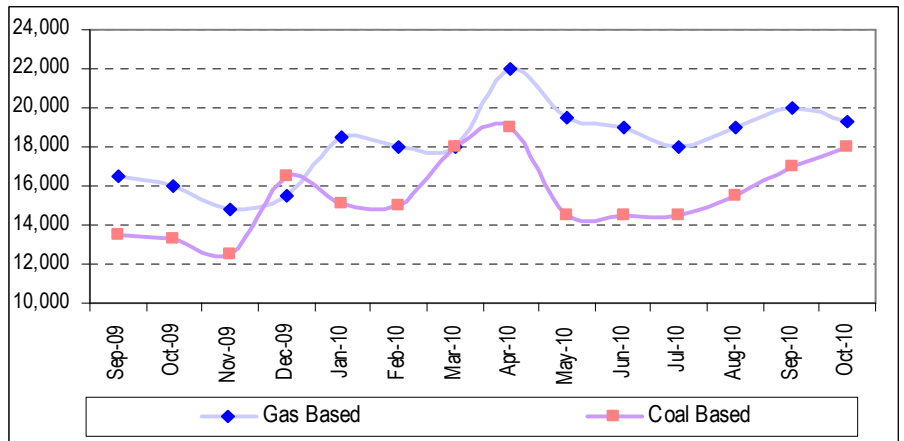
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**Sponge iron production, sales and realisation**

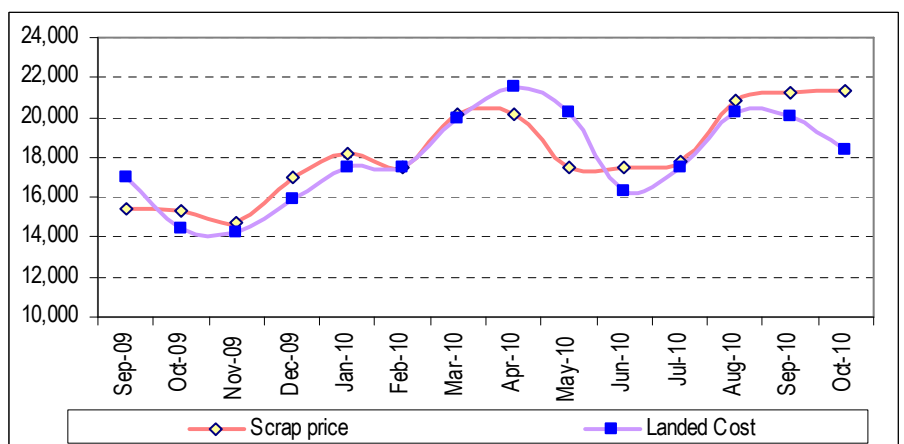


**Domestic sponge iron price movement (₹/tonne)**



Source: ACMIIL Research, Industry

**Domestic scrap price movement (₹/tonne)**



Source: ACMIIL Research, Steel Trade Intelligence

### **Business update**

TSIL's revenue has 94% correlation with Sponge iron prices over past ten years. Sponge iron prices (coal based) has improved in past three months. In past one year, after touching high of ₹19,000/tonne in April 2010, it declined 23% to ₹14,500/tonne in July 2010. However, it has increased 24% to ₹18,000/tonne in October 2010. Considering stable sponge iron outlook, we are revising our sponge price realisation for FY11E and FY12E to ₹15,300 and ₹16,000 respectively.

TSIL is planning for additional AFBC boiler based power plant (25MW) based on waste char. For captive non-coking coal mine, part of a land is yet to be acquired from the government. We have not considered both these development in our valuation, as both these units commence operation after FY12.

### **Valuation**

TSIL's revenue is expected to grow at 5% and 6% in FY11E and FY12E, respectively. The improvement in sponge iron demand and stabilization of raw material cost would improve the revenue and margin going ahead. We expect performance for TSIL to improve from Q3FY11 onwards. Accordingly, we have revised FY11E and FY12E EPS estimates to ₹59 and ₹61.9 respectively. We assign multiple of 6x to FY12E EPS and revise our target price to ₹371. At CMP of ₹371, TSIL is trading at PE of 6.3x and 6x of FY11E and FY12E, earnings respectively. We maintain **"HOLD"** recommendation on the stock.

### Financials

#### Profit and loss account

Particulars (₹ Million)	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011E	FY 2012E
Net Sales	2,785	4,566	6,081	5,200	5,450	5,751
Total Expenditure	2,450	3,119	4,242	3,961	4,129	4,375
EBITDA	335	1,447	1,840	1,239	1,321	1,376
Depreciation	135	196	183	194	194	195
EBIT	200	1,251	1,657	1,045	1,127	1,181
Interest	54	120	46	2	0	0
Other income	183	234	201	219	229	242
PBT	329	1,364	1,812	1,262	1,356	1,423
Taxes	117	409	605	417	447	469
PAT	212	955	1,207	845	908	953
Growth						
Net sales	-	64%	33%	-14%	5%	6%
PAT	-	350%	26%	-30%	7%	5%
EBITDA Margin	12.0%	31.7%	30.3%	23.8%	24.2%	23.9%
PAT Margin	7.6%	20.9%	19.8%	16.3%	16.7%	16.6%

Source: ACMIIL Research, Company

#### Balance sheet

Particulars (₹ Million)	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011E	FY 2012E
<b>Sources of Funds</b>						
Share capital	154	154	154	154	154	154
Reserve & Surplus	1,430	2,281	3,343	4,047	4,829	5,638
<b>Shareholders Funds</b>	<b>1,584</b>	<b>2,435</b>	<b>3,497</b>	<b>4,201</b>	<b>4,983</b>	<b>5,792</b>
Total Loans	1,468	844	1	1	1	1
Deferred Tax Liabilities	307	530	503	459	459	459
<b>TOTAL</b>	<b>3,359</b>	<b>3,808</b>	<b>4,002</b>	<b>4,661</b>	<b>5,444</b>	<b>6,253</b>
<b>Application of Funds</b>						
Gross Block	3,503	3,689	3,591	3,592	3,642	3,657
(-) Accumulated Depreciation	983	1,178	1,357	1,536	1,730	1,925
Net Block	2,521	2,511	2,234	2,057	1,913	1,733
Capital WIP	133	144	213	1,217	2,217	3,217
Investments	8	8	8	8	8	8
Net Current Assets	698	1,145	1,546	1,379	1,305	1,294
<b>TOTAL</b>	<b>3,359</b>	<b>3,808</b>	<b>4,002</b>	<b>4,661</b>	<b>5,444</b>	<b>6,253</b>

Source: ACMIIL Research, Company

### Cash flow

Particulars (₹ Million)	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011E	FY 2012E
Net Profit before tax	329	1,364	1,812	1,262	1,356	1,423
Add:						
Depreciation	135	196	183	194	194	195
Interest charges	54	120	46	2	0	0
Profit before working capital changes	497	1,548	1,931	1,393	1,550	1,618
Change in Working Capital	137	-114	-173	-201	108	-77
Profit after working capital	634	1,434	1,758	1,192	1,657	1,540
(-) Direct Tax	-101	-191	-604	-344	-447	-469
<b>Net cash flow from operating activities</b>	<b>533</b>	<b>1,243</b>	<b>1,154</b>	<b>848</b>	<b>1,210</b>	<b>1,071</b>
<b>Net cash flow from investing activities</b>	<b>-380</b>	<b>-265</b>	<b>15</b>	<b>-937</b>	<b>-1,050</b>	<b>-1,015</b>
<b>Net cash flow from financing activities</b>	<b>621</b>	<b>-805</b>	<b>-996</b>	<b>-124</b>	<b>-126</b>	<b>-144</b>
Net increase/(decrease) in cash	774	172	174	-213	34	-88
Opening balance of cash	26	800	972	1,146	933	967
Closing balance of cash	800	972	1,146	933	967	878

Source: ACMIIL Research, Company

### Ratios

Profitability Ratio	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011E	FY 2012E
EBITDA Margin	12.0%	31.7%	30.3%	23.8%	24.2%	23.9%
PAT Margin	7.6%	20.9%	19.8%	16.3%	16.7%	16.6%
RONW	13.4%	39.2%	34.5%	20.1%	18.2%	16.5%
ROCE	6.6%	38.2%	47.4%	24.9%	22.6%	20.4%
<b>Per Share Ratios</b>						
EPS	13.8	62.0	78.4	54.9	59.0	61.9
CEPS	22.6	74.8	90.2	67.5	71.6	74.6
BV Per Share	102.8	158.1	227.1	272.8	323.6	376.1
<b>Valuation Ratios</b>						
P/E (x)				6.8	6.3	6.0
P/CEPS (x)				5.5	5.2	5.0
P/BV (x)				1.4	1.1	1.0
EV/EBIDTA				3.9	3.6	3.5
<b>Capital Structure Ratios</b>						
Debt/Equity	0.9	0.3	0.0	0.0	0.0	0.0
Current Ratio	2.0	2.2	3.8	2.8	2.6	2.4
<b>Turnover Ratios</b>						
Inventory turnover	14.8	10.9	12.0	7.6	9.0	8.5
Debtors turnover ratio	6.9	7.0	14.3	9.7	9.5	9.1
Creditors turnover ratio	5.0	4.2	14.8	9.9	9.5	9.4
Fixed asset turnover	1.1	1.8	2.7	2.5	2.8	3.3

Source: ACMIIL Research, Company

## Notes

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