

Difficult terrain

 29th June 2009

HOLD

Price	Target Price
Rs397	Rs409

Sensex – 14,785

Price Performance

(%)	1M	3M	6M	12M
Absolute	4	89	83	(49)
Rel. to Sensex	(1)	28	16	(50)

Source: Bloomberg

Stock Details

Sector	Metals & Mining
Reuters	TISC.BO
Bloomberg	TATA@IN
Equity Capital (Rs mn)	7306
Face Value (Rs)	10
Number of shares o/s (mn)	731
52 Week H/L (Rs)	784/146
Market Cap (Rsbn/USDmn)	283/5,870
Daily Avg Vol (No of shares)	19146515
Daily Avg Turnover (US\$ mn)	127.1

Shareholding Pattern (%)

	31/03/09	31/12/08	30/9/08
Promoters	34.0	34.0	33.9
FII/NRI	13.2	13.0	17.7
Institutions	24.8	25.2	22.5
Private Corp.	3.3	3.4	3.3
Public	24.8	24.5	22.6

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Tata Steel reported 4QFY09 and FY09 consolidated results, which were below our estimates. Net sales stood at Rs264.3bn (yoy down 26.7%, qoq down 20.4%), EBITDA stood at Rs330mn (yoy down 99.3%, qoq down 98.8%) and adjusted net loss stood at Rs10.4bn (yoy profit 15.2bn, qoq profit 9.5bn). During the quarter, the company reported restructuring/impairment cost of Rs40.9bn. The average realization for Corus for 4QFY09 stood at USD750/t and average cost of production stood at USD835/t, implying a negative EBITDA of USD85/t. As per the management, the prices in Europe have bottomed out and there may be technical restocking which may push up the prices. At the same time, Corus is also taking various measures to reduce cost of production, the company has a target to reduce cost by around USD1bn in FY10. During the quarter, there was inventory write down to the tune of Rs7.4bn in Corus and other subsidiaries. The outlook on Indian operations is optimistic and management has guided for 20-25% volume growth in FY10. However, the outlook for Tata Steel UK operations for FY10 seems to be a bit uncertain. If the company is unable to achieve the expected cost savings then there may be EBITDA loss in FY10 as well for Corus. Tata Steel has reported actuarial loss on pension fund of Rs54.9bn which has been adjusted through reserves. Currently, Tata Steel has consolidated net debt of USD9.89bn. We are revising our EPS estimates down for FY10 from Rs60 to Rs38.8 and for FY11 from Rs103 to Rs89. At the CMP of Rs397, the stock is trading at 10.2x FY10E EPS of Rs38.8 and at 4.5x FY11E EPS of Rs89. On EV/EBITDA basis the stock is trading at 6.4x FY10E EV/EBITDA and at 4.3x FY11E EV/EBITDA; while on P/B basis, the stock is trading at 1.47x FY10E book value and at 1.16x FY11E book value. We maintain **HOLD** on the stock with revised target price of Rs409 (1.2x FY11E book value) (Previous target Rs489).

Key highlights

- During the quarter, Corus and other subsidiaries reported EBITDA loss of Rs14.1bn and net loss of Rs19.8bn. This was primarily due to lower realization (USD750/t) and higher cost of production of Corus (USD835/t). Corus sells 70% of its products in spot markets, while its raw materials are booked on annual contracts
- Corus is currently operating at 50-53% capacity utilization rate. However, management has guided for full year FY10 capacity utilization rate of 67-68%. The utilization rate will be lower than the previous years as there is significant reduction in demand
- As per the management, the prices in Europe have bottomed out and there may be technical restocking which may push up the prices. The reduction in annual raw material contract prices will provide some cushion to the margins. However, the major savior for FY10 EBITDA will only be the targeted cost savings of around USD1bn, which the management expects to achieve in FY10
- As per the management, the various cost saving measures undertaken in FY09 have yielded savings of around USD1bn in 2HFY09 in Corus. Manufacturing costs have declined by around USD47/t in 2HFY09 as compared to 1HFY09 for Indian and S.E Asian operations. Performance improvement programs have yielded a savings of around USD167mn in FY09 in Indian operations.
- The outlook on Indian operations is optimistic and management has guided for volume growth of 20-25% in FY10. FY09 volumes were to the tune of 5.2mt.
- In 4QFY09, the average realization for Indian operations stood at USD710/t (yoy down 22.7%, qoq down 16.9%)
- 30% of the deliveries of Corus are to the automotive sector, which are on contract. These contracts are still under negotiation.
- In 4QFY09, there was inventory write down of Rs7.4bn in Corus and other subsidiaries.
- In 4QFY09, there was restructuring/impairment cost of Rs40.9bn, which was primarily due to mothballing of Teeside plant.

- The 2.9mtpa expansion program at Jamshedpur is progressing as per schedule and the plant is expected to be operational by Dec '10.
- Tata Steel has reported actuarial loss of Rs54.9bn, which has been adjusted through reserves. As on 31st Mar '09, the pension fund surplus is of USD879mn as against surplus of USD337mn on 31st Dec '08.
- Currently, Tata Steel has consolidated net debt of USD9.89bn. Corus does not have any repayment obligation till Dec '09; however, it plans to prepay GBP200mn of debt in FY10. Tata Steel India has debt repayment obligation of USD284mn in FY10. Tata Steel has reset its debt covenants and the same will not be tested till Mar '10. There has been no increase in interest cost on account of reset of covenants.

Outlook and valuation

At the CMP of Rs397, the stock is trading at 10.2x FY10E EPS of Rs38.8 and at 4.5x FY11E EPS of Rs89. On EV/EBITDA basis the stock is trading at 6.4x FY10E EV/EBITDA and at 4.3x FY11E EV/EBITDA; while on P/B basis, the stock is trading at 1.47x FY10E book value and at 1.16x FY11E book value. The outlook of Corus continues to loom over the ground of perplexity. Corus is expected to be benefited by the reduction in annual raw material contract prices. However, this benefit may not be significant enough to bring the Corus's EBITDA back to positive territory. This will be compounded by the reduction in average realization which has come down in 4QFY09 to around USD750/t (qoq down 40%). The only Green Shoots to be looked into are the targeted cost savings to the tune of USD1bn in FY10. If Corus is able to achieve the targeted cost savings then the EBITDA may come back to positive territory. Considering, Corus was able to achieve USD1bn of cost savings in 2HFY09, we believe the company will be able to achieve cost savings for FY10 as well. Corus is currently operating at 50-53% capacity utilization, which is expected to continue for next few months; while for full year FY10, management has given guidance of 67-68% capacity utilization. In order to achieve this target, Corus will have to operate at around 70-75% rate in 2HFY10. We are revising down our EPS estimates for FY10 from Rs60 to Rs38.8 and for FY11 from Rs103 to Rs89. We have reduced our volume assumptions for Corus for FY10 from 20mt to 14.9mt and for FY11 from 22mt to 18.9mt. We maintain HOLD on the stock with revised target price of Rs409 (1.2x FY11E book value) (Previous target Rs489).

Consolidated quarterly results

	4QFY08	1QFY09	2QFY09	3QFY09	4QFY09	(%) yoy	(%) qoq
Net Sales	360,579	435,083	441,990	331,910	264,310	-26.7%	-20.4%
Expenditure							
Raw Material Cost	170,000	217,844	243,810	159,990	107,733	-36.6%	-32.7%
Change in stock	-10,806	-16,074	-31,754	23,525	44,063	-507.8%	87.3%
Net Raw material cost	159,194	201,770	212,056	183,514	151,796	-4.6%	-17.3%
Gross profit	201,384	233,313	229,934	148,396	112,514	-44.1%	-24.2%
Gross margin	55.9%	53.6%	52.0%	44.7%	42.6%	-1328bps	-214bps
Power Cost	14,249	16,150	17,698	14,429	11,297	-20.7%	-21.7%
Employee Cost	45,818	49,012	47,545	44,579	38,614	-15.7%	-13.4%
Frieght	14,625	17,245	16,067	13,893	13,044	-10.8%	-6.1%
Other Expenses	82,459	81,030	66,127	46,922	49,229	-40.3%	4.9%
Total operating exp	157,152	163,437	147,438	119,822	112,184	-28.6%	-6.4%
EBITDA	44,233	69,876	82,497	28,574	330	-99.3%	-98.8%
Ebitda margin	12.3%	16.1%	18.7%	8.6%	0.1%	-1214bps	-848bps
Depreciation & amortization	9,945	11,050	11,470	10,852	9,283	-6.7%	-14.5%
EBIT	34,288	58,826	71,027	17,722	-8,952	-126.1%	-150.5%
EBIT margin	9.5%	13.5%	16.1%	5.3%	-3.4%	-1290bps	-873bps
Interest	8,261	8,243	8,208	9,114	7,337	-11.2%	-19.5%
Other income	923	527	844	316	970	5.1%	207.3%
Employee separation compensation	506	0	0	0	0		
Contribution for sports infra	0	0	0	0	0		
Forex gain (loss)	-940	-3,034	-3,962	-2,007	9,004	-1058.4%	-548.6%
Actuarial gain/(loss) on pension fund	-1,894	0	0	0	0		
Restructuring, impairment cost					40,945		
PBT	23,611	48,076	59,700	6,916	-47,260	-300.2%	-783.3%
Provision for tax	10,871	8,930	12,664	-405	-2,248	-120.7%	454.7%
ETR (%)	46%	19%	21%	-6%	5%	-4129bps	1062bps
Share of profits of Associates	377	1,003	680	817	-1,893	-601.9%	-331.7%
Minority interest	800	1,140	-	-	-1,550		
Attributable PAT	12,317	39,009	47,717	8,139	-45,355	-468.2%	-657.3%
Net margin	3.4%	9.0%	10.8%	2.5%	-17.2%	-2058bps	-1961bps
less: E/o Items adjusted for Tax	2,848	2,003	2,616	1,325	35,002		
Adjusted PAT	15,165	41,012	50,332	9,463	-10,353	-168.3%	-209.4%
Adjusted net margin	4.2%	9.4%	11.4%	2.9%	-3.9%	-812bps	-677bps
Equity capital	7,301	7,301	7,301	7,301	7,301	0.0%	0.0%
Diluted capital	8,307	8,307	8,307	8,307	8,307	0.0%	0.0%
Reported EPS							
- Basic	16.87	53.43	65.36	11.15	-62.12	-468.2%	-657.3%
- Diluted	14.83	46.96	57.44	9.80	-54.60	-468.2%	-657.3%
Adj EPS							
- Basic	20.77	56.17	68.94	12.96	-14.18	-168.3%	-209.4%
- Diluted	18.26	49.37	60.59	11.39	-12.46	-168.3%	-209.4%

All fig in Rs mn except percentage and per sh data

Common Size ratios

	4QFY08	1QFY09	2QFY09	3QFY09	4QFY09	(%) yoy	(%) qoq
Net Sales	100%	100%	100%	100%	100%	-	-
Raw material cost	47%	50%	55%	48%	41%	-639bps	-744bps
Change in stock	-3%	-4%	-7%	7%	17%	1967bps	958bps
Net Raw Material Cost	44%	46%	48%	55%	57%	1328bps	214bps
Personal expenses	13%	11%	11%	13%	15%	190bps	118bps
Power cost	4%	4%	4%	4%	4%	32bps	-7bps
Frieght	4%	4%	4%	4%	5%	88bps	75bps
Other expenses	23%	19%	15%	14%	19%	-424bps	449bps
EBITDA	12%	16%	19%	9%	0%	-1214bps	-848bps
Depreciation	3%	3%	3%	3%	4%	75bps	24bps
Interest expense	2%	2%	2%	3%	3%	48bps	3bps
Other income	0%	0%	0%	0%	0%	11bps	27bps
PAT	4%	9%	11%	3%	-4%	-812bps	-677bps

Consolidated Full year result

	FY09	FY08	(%) yoy
Net Sales	1,473,293	1,315,359	12.0%
Expenditure			
Raw Material Cost	729,377	595,943	22.4%
Change in stock	19,759	-8,905	-321.9%
Net Raw material cost	749,136	587,038	27.6%
Gross profit	724,157	728,321	-0.6%
Gross margin	49.2%	55.4%	-622bps
Power Cost	59,574	49,293	20.9%
Employee Cost	179,751	166,782	7.8%
Frieght	60,249	60,052	0.3%
Other Expenses	243,307	272,263	-10.6%
Total operating exp	542,880	548,390	-1.0%
EBITDA	181,277	179,931	0.7%
Ebitda margin	12.3%	13.7%	-138bps
Depreciation & amortization	42,654	41,370	3.1%
EBIT	138,623	138,562	0.0%
EBIT margin	9.4%	10.5%	-113bps
Interest	32,902	41,838	-21.4%
Other income	2,657	5,742	-53.7%
Employee separation compensation	0	2,271	
Contribution for sports infra	0	1,500	
Forex gain (loss)	0	5,947	-100.0%
Actuarial gain/(loss) on funds for employee benefits	0	59,068	
Restructuring, impairment cost	40,945		
PBT	67,432	163,711	-58.8%
Provision for tax	18,940	40,493	-53.2%
ETR (%)	28%	25%	335bps
Share of profits of Associates	607	1,682	-63.9%
Minority interest	-409	1,399	-129.3%
Attributable PAT	49,509	123,500	-59.9%
Net margin	3.4%	9.4%	-603bps
less: Extraordinary Items adjusted for Tax	40,945	-60,745	
Adjusted PAT	90,454	62,755	44.1%
Adjusted net margin	6.1%	4.8%	137bps
Equity capital	7,301	7,301	0.0%
Diluted capital	8,307	8,307	0.0%
Reported EPS			
- Basic	67.81	169.15	-59.9%
- Diluted	59.60	75.54	-21.1%
Adj EPS			
- Basic	123.89	85.95	44.1%
- Diluted	108.89	75.54	44.1%

All fig in Rs mn except percentage and per sh data

Common size ratios

	FY09	FY08	(%) yoy
Net Sales	100%	100%	-
Raw material cost	50%	45%	420bps
Change in stock	1%	-1%	202bps
Net Raw Material Cost	51%	45%	622bps
Personal expenses	12%	13%	-48bps
Power cost	4%	4%	30bps
Frieght	4%	5%	-48bps
Other expenses	17%	21%	-418bps
EBITDA	12%	14%	-138bps
Depreciation	3%	3%	-25bps
Interest expense	2%	3%	-95bps
Other income	0%	0%	-26bps
PAT	6%	5%	137bps

Standalone quarterly result

	4QFY08	1QFY09	2QFY09	3QFY09	4QFY09	(%) yoy	(%) qoq
Net Sales	57,367	61,650	68,507	48,021	64,979	13.3%	35.3%
Expenditure							
Raw Material Cost	8,693	10,231	13,818	16,112	16,939	94.9%	5.1%
Trading goods purchased	2,315	1,317	1,205	931	135	-94.2%	-85.5%
Change in stock	1,157	-2,018	-3,844	-6,360	9,329	706.5%	-246.7%
Net Raw material cost	12,164	9,530	11,179	10,683	26,403	117.1%	147.2%
Gross profit	45,203	52,120	57,328	37,339	38,576	-14.7%	3.3%
Gross margin	78.8%	84.5%	83.7%	77.8%	59.4%	-1943bps	-1839bps
Power Cost	2,218	2,619	2,781	2,635	2,878	29.8%	9.2%
Employee Cost	4,766	4,719	5,985	5,689	6,666	39.9%	17.2%
Freight	2,844	2,938	3,315	2,622	3,638	27.9%	38.7%
Other Expenses	11,351	11,599	13,418	11,613	10,915	-3.8%	-6.0%
Total operating exp	21,179	21,874	25,498	22,559	24,097	13.8%	6.8%
EBITDA	24,023	30,246	31,830	14,780	14,479	-39.7%	-2.0%
Ebitda margin	41.9%	49.1%	46.5%	30.8%	22.3%	-1959bps	-849bps
Depreciation & amortization	2,092	2,168	2,488	2,513	2,565	22.6%	2.1%
EBIT	21,932	28,078	29,342	12,266	11,915	-45.7%	-2.9%
EBIT margin	38.2%	45.5%	42.8%	25.5%	18.3%	-1989bps	-721bps
Interest	2,339	2,417	2,548	3,482	3,079	31.7%	-11.6%
Other income	275	122	2,384	85	492	78.7%	479.4%
Employee separation compensation	503	0	0	0	0		
Contribution for sports infra					0		
Forex gain (loss)	-939	-3,034	-3,454	-1,268	7,756	-925.7%	-711.7%
PBT	18,426	22,749	25,723	7,601	17,084	-7.3%	124.7%
Provision for tax	6,371	7,865	7,845	2,939	2,491	-60.9%	-15.3%
ETR (%)	35%	35%	30%	39%	15%	-2000bps	-2408bps
PAT	12,055	14,884	17,878	4,662	14,593	21.0%	213.0%
Net margin	21.0%	24.1%	26.1%	9.7%	22.5%	144bps	1275bps
less: Extraordinary Items adjusted for Tax	952	2,003	2,280	837	-5,120	-637.8%	-711.7%
Adjusted PAT	13,007	16,887	20,158	5,499	9,473	-27.2%	72.3%
Adjusted net margin	35.6%	27.4%	29.4%	11.5%	14.6%	-2098bps	313bps
Equity capital	7,308	7,308	7,308	7,308	7,308	0.0%	0.0%
Diluted capital	8,307	8,307	8,307	8,307	8,307	0.0%	0.0%
Reported EPS							
- Basic	16.50	20.37	24.46	6.38	19.97	21.0%	213.0%
- Diluted	14.51	17.92	21.52	5.61	17.57	21.0%	213.0%
Adj EPS							
- Basic	17.80	23.11	27.58	7.53	12.96	-27.2%	72.3%
- Diluted	15.66	20.33	24.27	6.62	11.40	-27.2%	72.3%

All fig in Rs mn except percentage and per sh data

Common size ratios

	4QFY08	1QFY09	2QFY09	3QFY09	4QFY09	(%) yoy	(%) qoq
Net Sales	100%	100%	100%	100%	100%	-	-
Raw material cost	15%	17%	20%	34%	26%	1091bps	-748bps
Trading goods purchased	4%	2%	2%	2%	0%	-383bps	-173bps
Change in stock	2%	-3%	-6%	-13%	14%	1234bps	2760bps
Net Raw Material Cost	21%	15%	16%	22%	41%	1943bps	1839bps
Personal expenses	8%	8%	9%	12%	10%	195bps	-159bps
Power cost	4%	4%	4%	5%	4%	56bps	-106bps
Frieght	5%	5%	5%	5%	6%	64bps	14bps
Other expenses	20%	19%	20%	24%	17%	-299bps	-738bps
EBITDA	42%	49%	46%	31%	22%	-1959bps	-849bps
Depreciation	4%	4%	4%	5%	4%	30bps	-129bps
Interest expense	4%	4%	4%	7%	5%	66bps	-251bps
Other income	0%	0%	3%	0%	1%	28bps	58bps
PAT	23%	27%	29%	11%	15%	-810bps	313bps

Standalone full year result

	FY09	FY08	(%) yoy
Net Sales	243,158	194,809	24.8%
Expenditure			
Raw Material Cost	57,099	33,552	70.2%
Trading goods purchased	3,589	3,879	-7.5%
Change in stock	-2,893	-387	646.9%
Net Raw material cost	57,795	37,044	56.0%
Gross profit	185,363	157,765	17.5%
Gross margin	76.2%	81.0%	-475bps
Power Cost	10,914	9,328	17.0%
Employee Cost	23,058	18,160	27.0%
Frieght	12,512	11,406	9.7%
Other Expenses	47,544	40,835	16.4%
Total operating exp	94,028	79,728	17.9%
EBITDA	91,334	78,036	17.0%
Ebitda margin	37.6%	40.1%	-250bps
Depreciation & amortization	9,734	8,346	16.6%
EBIT	81,600	69,690	17.1%
EBIT margin	33.6%	35.8%	-221bps
Interest	11,527	8,787	31.2%
Other income	3,083	3,350	-8.0%
Employee separation compensation	0	2,262	-100.0%
Contribution for sports infra		1,500	-100.0%
Forex gain (loss)	0	5,973	-100.0%
PBT	73,156	66,464	10.1%
Provision for tax	21,139	23,793	-11.2%
ETR (%)	29%	36%	-690bps
PAT	52,017	42,671	21.9%
Net margin	21.4%	21.9%	-51bps
less: Extraordinary Items adjusted for Tax	0	-1,700	-100.0%
Adjusted PAT	52,017	40,971	27.0%
Adjusted net margin	21.4%	21.0%	36bps
Equity capital	7,308	7,308	0.0%
Diluted capital	8,307	8,307	0.0%
Reported EPS			
- Basic	71.18	58.39	21.9%
- Diluted	62.62	51.37	21.9%
Adj EPS			
- Basic	71.18	56.06	27.0%
- Diluted	62.62	49.32	27.0%

All fig in Rs mn except percentage and per sh data

Common size ratios

	FY09	FY08	(%) yoy
Net Sales	100%	100%	-
Raw material cost	23%	17%	626bps
Trading goods purchased	1%	2%	-52bps
Change in stock	-1%	0%	-99bps
Net Raw Material Cost	24%	19%	475bps
Personal expenses	9%	9%	16bps
Power cost	4%	5%	-30bps
Frieght	5%	6%	-71bps
Other expenses	20%	21%	-141bps
EBITDA	38%	40%	-250bps
Depreciation	4%	4%	-28bps
Interest expense	5%	5%	23bps
Other income	1%	2%	-45bps
PAT	21%	21%	36bps

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