

RESULTS REVIEW

Tata Steel Limited

Hold

Share Data

Market Cap	Rs. 412.3 bn
Price	Rs. 564.40
BSE Sensex	14,900.76
Reuters	TISC.BO
Bloomberg	TATA IN
Avg. Volume (52 Week)	1.1 mn
52-Week High/Low	Rs.1,048.8/556.25
Shares Outstanding	730.6 mn

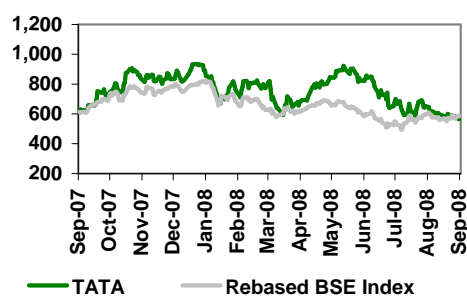
Valuation Ratios (Consolidated)

Year to 31 March	2009E	2010E
EPS (Rs.)	122.5	93.2
+/- (%)	7.4%	(24.0)%
PER (x)	4.6x	6.1x
EV/ Sales (x)	0.5x	0.5x
EV/ EBITDA (x)	4.0x	4.4x

Shareholding Pattern (%)

Promoters	34
FIs	20
Institutions	22
Public & Others	24

Relative Performance



Tough times ahead

For Q1'09, Tata Steel's consolidated net sales increased 39.6% yoy to Rs. 435.1 bn on account of improved realisations and a higher sales volume. In addition, adj. net profit jumped 91.8% yoy, supported by a lower interest expense and net profit margin rose 260 bps to 9.5% on the back of a lower effective tax rate.

In the coming quarters, we believe that:

Steel prices are set to decline: International steel prices have started to trend downwards as the demand for the alloy has declined on account of the adverse global economic conditions. The IMF has further reduced its forecast for world GDP growth in 2008 from the earlier 4.1% to 3.7%. Thus, with inflation at record levels, high interest rates, and the downturn in the global economy, infrastructure development across the globe will be adversely effected. We believe developers will delay the procurement of steel especially in the view of the recent downtrend in prices. Further, supply is expected to improve as China, which had curtailed production because of the Olympic Games, resumes production. Therefore, we expect steel prices to witness a sharp decline before settling at USD 700–USD 750 per ton by the end of FY09E. In FY10E, prices are expected to fall further.

Margins will be under pressure: Contract prices of key raw materials such as iron ore and coking coal have increased by around 65% and 200% yoy, respectively. Nevertheless, till now steel manufacturers have been able to maintain margins as they were able to pass on the increase in costs to the customers due to the strong demand for steel. Going forward, however, a weak global demand scenario will result in falling steel prices. Moreover, the full impact of higher raw material cost will only be witnessed from Q2'09 as new contract prices came into effect from June'08. Thus, we believe that EBITDA margin will reduce from 13.7% in FY08 to 13.3% in FY09E.

Key Figures (Consolidated)

Quarterly Data	Q1'08	Q4'08	Q1'09	YoY%	QoQ%
(Figures in Rs. mn, except per share data)					
Net Sales	311,623	360,501	435,083	39.6%	20.7%
EBITDA	48,118	44,436	69,876	45.2%	57.3%
Adj. Net Profit	21,621	14,228	41,480	91.8%	191.5%
Margins(%)					
EBITDA	15.4%	12.3%	16.1%		
NPM	6.9%	3.9%	9.5%		
Per Share Data (Rs.)					
Adj. EPS	31.7	23.4	56.4	77.9%	141.3%

Valuation

At the current market price of Rs. 564.4 the stock is trading at a forward P/E of 4.6x and 6.1x on its FY09E and FY10E earnings, respectively. We have valued Tata Steel at a P/E of 6.5x its FY10E EPS, and arrive at a target price of Rs. 605. Based on our valuation and result analysis, we downgrade our rating on the stock to Hold.

Result Highlights

Net sales for Q1'09 jumped 39.6% yoy to Rs. 435.1 bn on the back of improved realisations and a higher sales volume. The sales volume increased 8.1% yoy to 8.13 mt in Q1'09. Standalone revenues increased 46.9% yoy to Rs. 61.7 bn, supported by an 11.5% increase in the sales volume.

EBITDA surged 45.2% yoy to Rs. 69.9 bn, and EBITDA margin improved 62 bps yoy to 16.1% on account of several cost-cutting initiatives and higher steel prices. Standalone EBITDA surged 83.9% yoy to Rs. 30.2 bn, and standalone EBITDA margin moved up 9.9 pts to 49.1%. Corus, on the other hand, reported a moderate 11% increase in EBITDA.

Adj. net profit improved 91.8% yoy to Rs. 41.5 bn, supported by a lower interest expense. Adj. net profit margin improved by a substantial 260 bps to 9.5% on the back of sharp fall in the effective tax rate and a lower depreciation charge (as a percentage of sales).

Key Events

Tata Steel Global eyes PE deal

Tata Steel Global Holdings Pte Ltd, the Singapore-based subsidiary that owns the international steel and mining assets of Tata Steel Ltd, is in talks to raise at least USD 1 bn through private equity transactions. The Company is expected to use the money to fund the purchase of a coal or iron ore mine.

Sales volume for Indian operations increased 11.5% yoy to 1.16 mt

Sales volume for Corus improved 7.1% yoy to 6.21 mt

Tata Steel enters the Fortune 500 list

Tata Steel, on the back of its Corus acquisition, entered the famed Fortune 500 list. The Company ranks 231 among the top 500 companies in the world.

Key Risks

The following factors may pose a threat to our rating:

- Any unanticipated change in the government's steel price policy
- A significant increase in raw material prices
- Delay in the commissioning of new capacities

Outlook

International steel prices have increased substantially, rising from USD 648 per ton in December 2007 to USD 1,120 per ton in July 2008 on the back of a strong demand and surging raw material costs. However, during the last two months, steel prices have started to trend downwards following the weakness in demand due to the slowdown in the global economy. Going forward, we believe that demand for steel will weaken further on the back of adverse global economic conditions. With rising inflation, surging raw material prices, high interest rates, and the decline in consumer spending, infrastructure development plans across the globe will be adversely affected. Developers are expected to delay the procurement of raw materials, especially in the view of the recent downward trend in steel prices. Moreover, supply of the alloy is expected to improve as China, which had curtailed production because of the Olympic Games, resumes production. As a result, we expect steel prices to decline sharply before settling at USD 700–USD 750 per ton by the end of FY09. In FY10E, prices are expected to fall further.

Another major concern for steel companies is the surging raw material prices. Contract prices of key raw materials such as iron ore and coking coal have jumped by 65% yoy and 200% yoy, respectively. However, steel manufacturers, including Tata Steel, have been able to maintain margins by passing on the increase in costs to customers, primarily due to the strong demand for the alloy. Going forward, with declining steel demand resulting in lower steel prices, we expect EBITDA margins to fall in FY09E. However, we expect the net profit margin to improve marginally as the management has given a guidance of an effective tax rate of around 20-22%, against our earlier assumption of 33%.

To contain the effect of the rising raw material prices, Tata Steel has undertaken several initiatives to improve its operational efficiency. The Company is also increasing its focus on value-added products—it has increased the sale of branded products in India and has launched value-added products such as high strength steel and engineering steel. Further, the Company is also acquiring stakes in various mineral mining projects around the world to ensure a continuous supply of raw materials. However, these projects are still in their initial stages and will take some time to provide tangible returns.

At the current market price of Rs. 564.4 the stock is trading at a forward P/E of 4.6x and 6.1x on its FY09E and FY10E earnings, respectively. We have valued Tata Steel at a P/E of 6.5x its FY10E EPS, and arrive at a target price of Rs. 605. Based on our valuation and result analysis, we downgrade our rating on the stock to Hold.

Key Figures (Consolidated)

Year to March	FY06	FY07	FY08*	FY09E*	FY10E*	CAGR (%)
(Figures in Rs. mn, except per share data)						(FY08-10E)
Net Sales	203,221	252,124	1,315,359	1,479,779	1,458,229	5.3%
EBITDA	65,912	78,882	179,931	196,071	177,175	(0.8)%
Adj. Net Profit	37,714	42,795	86,458	101,378	77,096	(5.6)%
Margins(%)						
EBITDA	32.0%	30.8%	13.7%	13.3%	12.2%	
NPM	18.3%	16.7%	6.6%	6.9%	5.3%	
Per Share Data (Rs.)						
Adj. EPS	68.3	74.8	114.1	122.5	93.2	(9.6)%
PER (x)	7.9x	6.0x	4.9x	4.6x	6.1x	

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