

## Performance set to improve, going forward....

Tata Steel reported a steady performance at the operational level wherein reported PAT was supported by favourable tax impact. Standalone operations reported sales volume of 3.0 million tonnes (MT), lower than our estimate of 3.2 MT. European operations reported steel sales of 2.3 MT, lower than our estimate of 2.5 MT. Bhushan Steel reported sales volume of 1.04 MT (broadly in line with our estimate of 1 MT). The consolidated topline came in at ₹ 34579.2 crore. Consolidated adjusted EBITDA came in at ₹ 4018 crore, broadly in line with our estimate of ₹ 3972.7 crore. Standalone Indian operations reported adjusted EBITDA/tonne of ₹ 11200/tonne, higher than our estimate of ₹ 10500/tonne. While European operations reported EBITDA/tonne of US\$10/tonne. Tata Steel BSL reported an EBITDA/tonne of ₹ 4600/tonne, lower than our estimate of ₹ 7000/tonne. During the quarter, the company had a favourable tax impact of ₹ 4233 crore, of which ₹ 2425 crore was on adoption of the new corporate tax rate by Tata Steel standalone & some subsidiaries in India while ₹ 1808 crore was on account of recognition/reversal of deferred tax assets & liabilities in offshore subsidiaries. The ensuing consolidated PAT was at ₹ 3302 crore.

## Domestic operations to account for ~71% of capacity by 2025

In India, Tata Steel has operations in Jamshedpur (10 MT), Kalinganagar (3 MT), Tata Steel BSL (5.6 MT) and Tata Long products (1 MT), aggregating to 19.6 MT. Indian operations' key assets viz. Jamshedpur, Kalinganagar, Angul have globally cost competitive position, aiding overall EBITDA margins. Going forward, Tata Steel is planning to increase India capacity to 30 MT by 2025 through organic & inorganic routes, thereby increasing share of higher margin domestic capacity to 71% by 2025, auguring well for company.

## Subdued Q2FY20; H2FY20 be better...

Tata Steel saw a relatively subdued Q2FY20 on the back of weakness in steel prices and muted demand from key user industries. However, post monsoons, the pick-up in economic activity and steps taken by the government to spur investment is expected to result in better H2FY20.

## Valuation & Outlook

Going forward, after a subdued Q2FY20, we expected the performance of Tata Steel to improve in H2FY20E and further in FY21E. The recent down tick in key raw material coking coal augurs well for the company. Coking coal costs are expected to be lower by US\$15/tonne in Q3FY20 compared to Q2FY20 average. Going forward, for standalone operations, we model EBITDA/tonne of ₹ 11750/tonne for FY20E (upward revise from ₹ 11650/tonne) and ₹ 13250/tonne for FY21E (upward revise from ₹ 12500/tonne earlier). We continue to value the company on an SOTP basis and arrive at a target price of ₹ 470, maintaining our **BUY** rating.



### Particulars

Particular	Amount
Market Capitalization (₹ Crore)	48,654
Total Debt (FY19) (₹ Crore)	100,816
Cash & Cash Eq. (FY19) (₹ Crore)	5,937
EV (₹ Crore)	143,533
52 week H/L (₹)	610 / 320
Equity capital	₹ 1145 Crore
Face value	₹ 10

### Key Highlights

- Indian operations EBITDA per tonne at ₹11200/tonne, higher than our estimate of ₹ 10500/tonne
- European operations reported EBITDA/tonne of US\$ 10/tonne, against our estimate of negative EBITDA/tonne of US\$5/tonne
- Maintain our **BUY** recommendation on stock with a target price of ₹470

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### Key Financial Summary

(₹ Crore)	FY17	FY18	FY19	FY20E	FY21E
Net Sales	112,299	131,700	157,669	154,043	162,782
EBITDA	17,008	21,891	29,383	21,307	25,344
Adj PAT	4,092	8,164	8,995	5,073	8,148
EPS (₹)	42.2	71.3	78.6	42.1	67.7
EV/EBITDA (x)	7.0	5.8	5.0	7.0	5.6
RoCE (%)	9.7	11.0	13.4	7.8	10.0
RoE (%)	10.8	13.4	13.0	7.4	10.5

Source: Company, ICICI Direct Research

Exhibit 1: Variance Analysis (Consolidated Performance)

	Q2FY20	Q2FY20E	Q2FY19	YoY (%)	Q1FY20	QoQ (%)	Comments
Revenue	34579.2	35,172.5	43,544.1	-21%	35,947.1	-4%	Topline came in below our estimate on lower-than-expected sales volume
Other Income	183.6	350.0	354.4	-48%	251.1	-27%	
Employee Expense	4604.8	4,750.0	4,996.3	-8%	4,899.4	-6%	
Raw Material Expense	14847.7	14,750.0	17,541.8	-15%	13,762.1	8%	
Other operating Expenses	11307.1	11,699.8	12,086.5	-6%	11,908.7	-5%	
EBITDA	3,819.6	3,972.7	8,919.5	-57%	5,376.9	-29%	
Adjusted EBITDA	4018.0	3,972.7	17.1		17.1		EBITDA came in broadly in line with our estimate
EBITDA Margin (%)	11.6	11.3	20.5	-886 bps	15.0	-334 bps	EBITDA margin came in broadly in line with our estimate
Depreciation	2127.2	2,134.9	1,907.9	11%	2,082.8	2%	
Interest	1871.4	1,761.2	2,153.1	-13%	1,806.4	4%	
Exceptional Item and Share of associates	-11.12	75.0	235.1		68.2		
PBT	(6.5)	501.6	5,448.1		1,807.0		
Tax Outgo	-4050.0	213.2	2,326.4		1,123.8		
PAT	4,043.5	288.4	3,121.7	30%	683.1	NA	
Profit from discontinued operations	-741.1		(5.5)	NA	18.8	c	
Reported PAT for the Group	3,302.3		3,116.2	6%	702.0	370%	Reported PAT supported by tax credit
<b>Key Metrics</b>							<b>Comments</b>
TSI Steel Sales (MT) (Standalone operations)	3.0	3.2	3.2	-6%	3.0	0%	Standalone operations sales volume came in lower than our estimate
TSE Steel Sales (MT)	2.3	2.5	2.3	0%	2.3	0%	European operations sales volume came in lower than our estimate
Adjusted TSI EBITDA/tonne (₹/tonne)	11,200	10,500	18,856	-41%	13,158	-15%	EBITDA/tonne of India operations came in higher than our estimate
TSE EBITDA/tonne (US\$/tonne)	10.0	(5.0)	70	-86%	4	150%	EBITDA/tonne of European operations came in higher than our estimate

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

	FY20E			FY21E			Comments
	Old	New	% Change	Old	New	% Change	
(₹ Crore)							
Total Operating Income (₹ crore)	162,349	154,043	(5.1)	165,866	162,782	(1.9)	Topline revised downward for FY20E and FY21E on lower Tata Steel Europe sales volume estimates
EBITDA (₹ crore)	22,352	21,307	(4.7)	24,834	25,344	2.1	EBITDA revised upward for FY21E on account of upward revision in realisation estimate for domestic India business
EBITDA Margin (%)	13.8	13.8	(100) bps	15.0	15.6	200 bps	EBITDA margin for FY21E revised upwards for FY21E
Adj PAT (₹ crore)	5,139	5,073	(1.3)	7,101	8,148	14.8	PAT revised upwards for FY21E
Adj EPS (₹)	42.7	42.1	(1.3)	59.0	67.7	14.8	

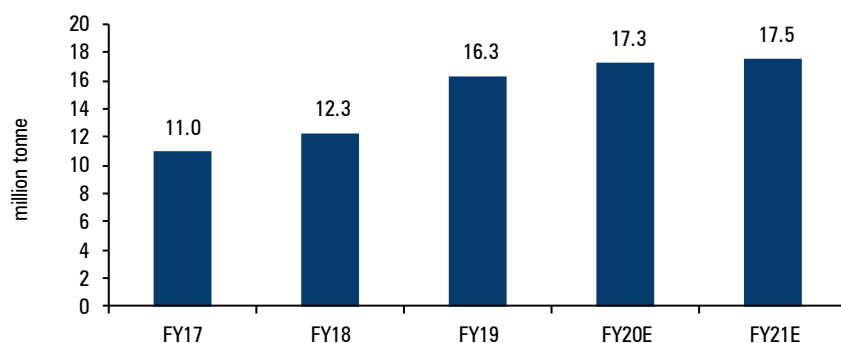
Source: Company, ICICI Direct Research

## Conference Call Highlights

- India steel demand is expected to improve in H2FY20 with the end of monsoon, increase in the government spending and improvement in liquidity.
- Domestic steel prices are expected to improve with an improvement in demand and sentiment. The company has recently taken a price hike and believes the prices have bottomed out. Company has recently taken price hike of ~₹500-750/tonne.
- The management expects working capital release to the tune of ~₹ 1000 crore in Q3FY20
- Exports were at 0.64 MT in Q2FY20. Going forward for FY20, the management has given export volume guidance of 2.4 MT
- For H1FY20, the management has incurred capex to the tune of ~₹ 4500 crore. The management has guided that the capex intensity would reduce notably. Capex for H2FY20 is likely to be in the range of ~₹ 3500 crore
- On a consolidated basis, gross debt has increased from ₹ 106636 crore on June 2019 to ₹ 111549 crore as on September 2019. However, about €370 million debt (~₹ 2900 crore) has been repaid in October 2019
- Coking coal prices, a key raw material used in the steel making process has been on a declining trend. For Q3FY20, average coking coal prices are expected to be lower by ~US\$15/tonne compared to Q2FY20 average for both India as well as European operations
- Tata Steel Kalinganagar Phase 2 expansion is under way. The cold rolling mill (CRM) complex and pellet plant have been prioritised to improve the product mix and bring cost efficiency
- Tata Steel has said it remains committed to divesting 70% stake in Tata Steel Thailand. Currently, Synergy Metals & Mining Fund is carrying out due diligence for the mandatory takeover process. Tata Steel & Synergy are in active conversation to finalise the definitive document.
- Tata Steel will be bidding for the upcoming iron ore auctions as it wants to get into commercial mining
- Tata Steel also recently bid for two chrome ore mines, as a replacement for its Sukinda mine, which should expire by March 2020. While the bid amount appears to be high for the two chrome ore mines, they should benefit from cost optimisation. Also, Sukinda mine would have the required incremental capex to shift from underground to opencast, which would not be the case for the two chrome mines for which it bid. The two mines, on a combined basis, are expected to reach Sukinda's production levels in the next three years
- With the weakness in the steel market, the management is trying to work on below-EBITDA items like capex and working capital, to make Europe a cash-positive geography. It wants to refrain from any support from the India business

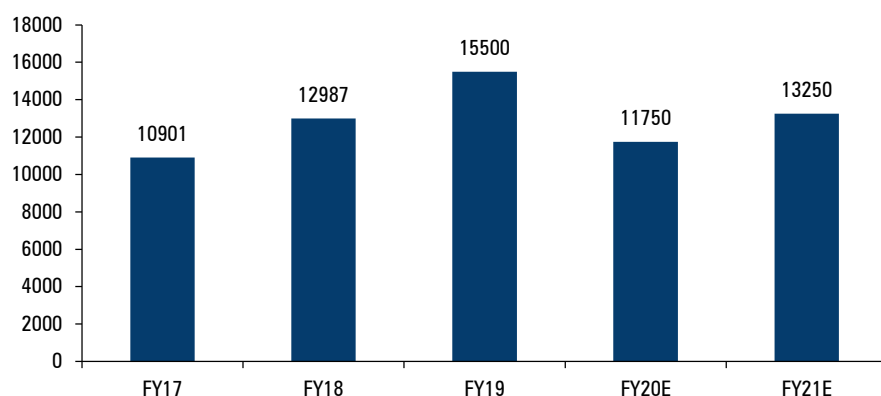
## Financial story in charts

Exhibit 3: Tata Steel + Bhushan Steel volume trend, going forward



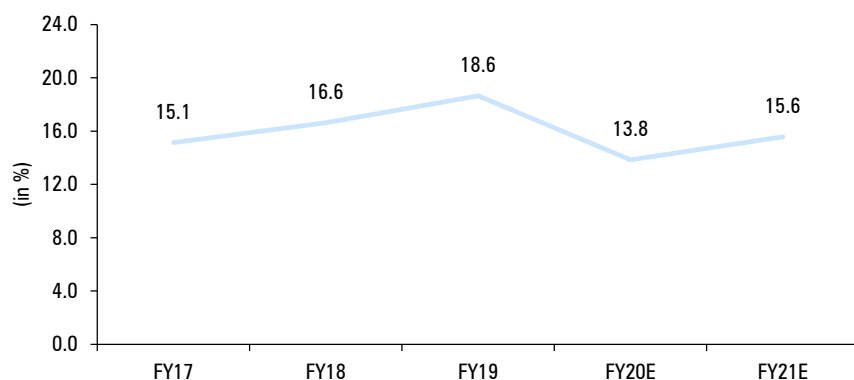
Source: Company, ICICI Direct Research

Exhibit 4: Tata Steel standalone operation EBITDA... (in ₹/tonne)



Source: Company, ICICI Direct Research

Exhibit 5: Consolidated EBITDA margins trend....(in %)



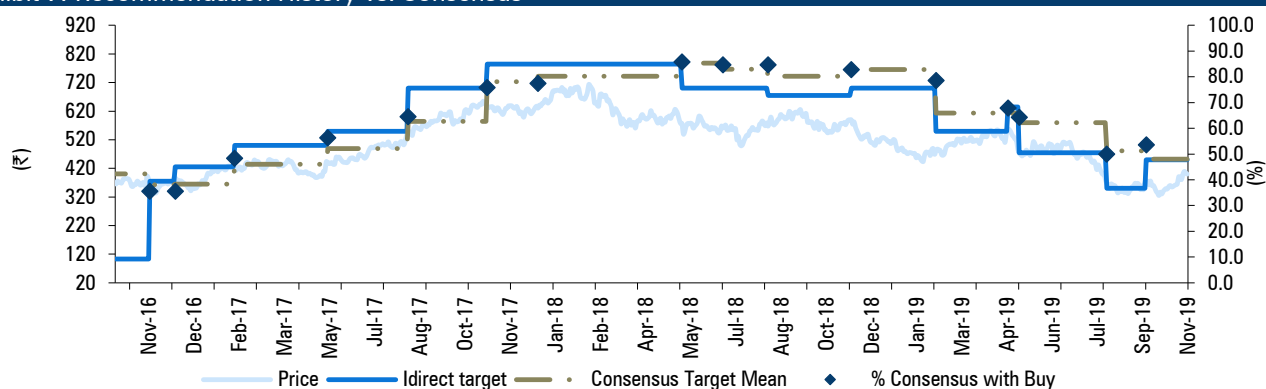
Source: Company, ICICI Direct Research

Exhibit 6: Valuation

	Total Op. Income	Growth	EPS	Growth	PE	EV/EBIDTA	P/ BV	RoNW	RoCE
	(₹ Crore)	% YoY	(₹)	% YoY	(x)	(x)	(x)	(%)	(%)
FY17	112,299	(3.8)	42.2	LP	9.6	7.0	1.0	10.8	9.7
FY18	131,700	17.3	71.3	69.1	5.7	5.8	0.8	13.4	11.0
FY19E	157,669	19.7	78.6	10.2	5.1	5.0	0.7	13.0	13.4
FY20E	154,043	(2.3)	42.1	(46.4)	9.6	7.0	0.7	7.4	7.8
FY21E	162,782	5.7	67.7	60.6	6.0	5.6	0.6	10.5	10.0

Source: Company, ICICI Direct Research

Exhibit 7: Recommendation History vs. Consensus



Source: Bloomberg, Company, ICICI Direct Research

Exhibit 8: Top 10 Shareholders

Rank	Name	Latest Filing	% O/S	Position	Change
1	Tata Group of Companies	30-Sep-19	32%	358.14M	0
2	Life Insurance Corporation of India	30-Sep-19	10%	108.39M	0.00M
3	HDFC Asset Management Co., Ltd.	30-Sep-19	5%	52.95M	0.08M
4	Reliance Nippon Life Asset Management Limited	31-Oct-19	3%	38.23M	-0.81M
5	ICICI Prudential Life Insurance Company Ltd.	30-Sep-19	2%	24.95M	-0.02M
6	ICICI Prudential Asset Management Co. Ltd.	30-Sep-19	1%	16.59M	-0.19M
7	SBI Funds Management Pvt. Ltd.	30-Sep-19	1%	15.68M	0.77M
8	Mirae Asset Global Investments (India) Pvt. Ltd.	30-Sep-19	1%	13.70M	0.89M
9	Norges Bank Investment Management (NBIM)	31-Dec-18	1%	10.10M	-0.66M
10	BlackRock Institutional Trust Company, N.A.	31-Oct-19	1%	9.93M	-0.00M

Source: Reuters, ICICI Direct Research

Exhibit 9: Recent Activity

Buys			Sells		
Investor name	Value (M)	Shares (M)	Investor name	Value (M)	Shares (M)
Mirae Asset Global Investments (India) Pvt. Ltd.	4.55	0.89	Canara Robeco Asset Management Company Ltd.	(8.77)	(1.82)
SBI Funds Management Pvt. Ltd.	3.93	0.77	Kotak Mahindra Asset Management Company Ltd.	(6.27)	(1.23)
First Sentier Investors	2.47	0.34	Causeway Capital Management LLC	(5.25)	(1.03)
UTI Asset Management Co. Ltd.	1.32	0.26	Reliance Nippon Life Asset Management Limited	(4.35)	(0.81)
Research Affiliates, LLC	0.92	0.13	The Vanguard Group, Inc.	(4.13)	(0.81)

Source: Reuters, ICICI Direct Research

Exhibit 10: Shareholding Pattern

(in %)	Mar-19	Jun-19	Sep-19
Promoter	33.1	33.1	33.1
Others	66.9	66.9	66.9
Total	100.0	100.0	100.0

Source: Company, ICICI Direct Research

## Financial summary

Exhibit 11: Profit and loss statement				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Net Sales	130425.5	154691.8	153040.0	161706.8
Other Operating Income	1274.9	2977.2	1002.9	1075.5
<b>Total Operating Income</b>	<b>131700.3</b>	<b>157669.0</b>	<b>154042.9</b>	<b>162782.2</b>
Growth (%)	16.9	18.6	-18.8	5.9
Total Operating Expend.	109809.8	128285.7	132736.2	137437.9
<b>EBITDA</b>	<b>21890.5</b>	<b>29383.3</b>	<b>21306.8</b>	<b>25344.4</b>
Growth (%)	28.7	34.2	-27.5	19.0
Depreciation	5961.7	7341.8	8403.8	8692.4
Interest	5501.8	7660.1	7337.9	7092.9
Other Income	1083.6	1420.6	1168.5	1245.8
PBT	11510.6	15802.0	6733.6	10805.0
Exceptional Item	9599.1	103.7	0.0	0.0
Total Tax	3405.4	6718.4	1708.0	2699.4
<b>PAT</b>	<b>17704.4</b>	<b>9187.3</b>	<b>5025.6</b>	<b>8105.5</b>
Growth (%)	-5916.5	-48.1	-45.3	61.3
Minorities, Associates, etc	58.5	-89.0	47.3	42.6
Rep PAT after Assoc. MI	17762.8	9098.3	5072.9	8148.2
<b>Adj PAT after Assoc. MI</b>	<b>8163.7</b>	<b>8994.6</b>	<b>5072.9</b>	<b>8148.2</b>

Source: Company, ICICI Direct Research

Exhibit 12: Cash flow statement				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Profit after Tax	17762.8	9098.3	5072.9	8148.2
Add: Depreciation	5961.7	7341.8	8403.8	8692.4
(Inc)/dec in Current Assets	-23256.4	-10445.3	16395.5	-10516.5
Inc/(dec) in CL and Prov.	-801.9	9240.5	-17867.3	6366.9
Others	9470.2	10100.6	3000.0	3000.0
<b>CF from operating activities</b>	<b>9136.3</b>	<b>25336.0</b>	<b>15005.0</b>	<b>15690.9</b>
(Inc)/dec in Investments	-5362.8	2762.2	-1000.0	700.0
(Inc)/dec in Fixed Assets	-10285.6	-37808.5	-7500.0	-10109.5
Others	-665.2	-6313.9	-210.5	-292.1
<b>CF from investing activities</b>	<b>-16313.5</b>	<b>-41360.3</b>	<b>-8710.5</b>	<b>-9701.6</b>
Issue/(Buy back) of Equity	174.7	0.0	0.0	0.0
Inc/(dec) in loan funds	5660.1	12141.9	500.0	-7500.0
Dividend paid & dividend tax	-1339.6	-1339.6	-1339.6	-1473.6
Inc/(dec) in Share Cap	6453.4	295.7	-3921.7	3075.3
Others	-754.7	329.7	0.0	0.0
<b>CF from financing activities</b>	<b>10193.9</b>	<b>11427.7</b>	<b>-4761.3</b>	<b>-5898.3</b>
Net Cash flow	3016.8	-4596.5	1533.2	91.0
Opening Cash	4921.1	7937.9	3341.3	4874.5
<b>Closing Cash</b>	<b>7937.9</b>	<b>3341.3</b>	<b>4874.5</b>	<b>4965.5</b>

Source: Company, ICICI Direct Research

Exhibit 13: Balance sheet				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
<b>Liabilities</b>				
Equity Share Capital	1,145.0	1,145.0	1,204.3	1,204.3
Hybrid Perpetual securitie	2,275.0	2,275.0	2,275.0	2,275.0
Reserve and Surplus	57450.7	65505.1	64999.6	74414.7
Total Shareholders funds	60870.6	68925.1	68478.9	77894.0
Total Debt	88674.1	100816.0	101316.0	93816.0
Deferred Tax Liability	10569.9	12459.9	12459.9	12459.9
Minority Interest & Other:	9866.9	2364.5	5411.8	8454.4
<b>Total Liabilities</b>	<b>169981.5</b>	<b>184565.4</b>	<b>187666.5</b>	<b>192624.3</b>
<b>Assets</b>				
Gross Block	193677.1	229688.9	237188.9	239106.0
Less: Impairment	0.0	0.0	0.0	0.0
Less: Acc Depreciation	101217.0	108558.9	116962.7	116962.7
Net Block	92460.1	121130.0	120226.2	122143.3
CWIP	16159.8	17956.5	17956.5	17456.5
Investments	17899.5	5738.2	6738.2	6038.2
Inventory	28331.0	31656.1	24783.5	25466.9
Debtors	12415.5	11811.0	12038.1	12749.3
Loans and Advances	26142.3	27486.0	17236.0	27358.0
Other Current Assets	3276.6	9657.7	10157.7	9157.7
Cash	7937.9	3341.3	4874.5	4965.5
Total Current Assets	78103.4	83952.1	69089.8	79697.3
Current Liabilities	38506.8	44197.1	25329.9	30696.8
Provisions	1269.6	4819.8	5819.8	6819.8
Current Liabilities & Prov	39776.4	49017.0	31149.7	37516.6
Net Current Assets	38326.9	34935.2	37940.1	42180.7
others	5135.3	4805.6	4805.6	4805.6
<b>Application of Funds</b>	<b>169981.5</b>	<b>184565.4</b>	<b>187666.5</b>	<b>192624.3</b>

Source: Company, ICICI Direct Research

Exhibit 14: Key ratios				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
<b>Per share data (₹)</b>				
Adj EPS	71.3	78.6	42.1	67.7
Cash EPS	123.4	142.7	111.9	139.8
BV	531.6	602.0	568.6	646.8
Adj BV (adj for Goodwill)	495.8	567.1	533.7	611.9
DPS	10.0	10.0	10.0	11.0
Cash Per Share	69.3	29.2	40.5	41.2
<b>Operating Ratios (%)</b>				
EBITDA Margin	16.6	18.6	13.8	15.6
PBT / Total Operating income	8.7	10.0	4.4	6.6
Adj PAT Margin	6.2	5.7	3.3	5.0
Inventory days	186	180	185	185
Debtor days	34	29	35	35
Creditor days	187	235	220	220
<b>Return Ratios (%)</b>				
Adj RoE	13.4	13.0	7.4	10.5
Adj RoCE	11.0	13.4	7.8	10.0
<b>Valuation Ratios (x)</b>				
P/E	5.7	5.1	9.6	6.0
EV / EBITDA	5.8	5.0	7.0	5.6
EV / Net Sales	1.0	0.9	1.0	0.9
Market Cap / Sales	0.3	0.3	0.3	0.3
Price to Book Value	0.8	0.7	0.7	0.6
Price to Adj Book Value	0.8	0.7	0.8	0.7
<b>Solvency Ratios</b>				
Debt/EBITDA	4.1	3.4	4.8	3.7
Debt / Equity	1.5	1.5	1.5	1.2
Current Ratio	2.0	1.7	2.2	2.1
Quick Ratio	1.3	1.1	1.4	1.4

Source: Company, ICICI Direct Research

**Exhibit 15: ICICI Direct coverage universe (Metals and Mining)**

	CMP		TP	M Cap (₹ Cr)	EPS (₹)			P/E (x)			EV/EBITDA (x)			ROCE(%)			ROE(%)		
	(₹)	(₹)			Rating	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E
Coal India	214	225	Hold	132838	28.3	28.9	29.9	7.6	7.4	7.2	4.3	5.2	5.0	86.4	67.7	61.4	66.2	54.6	48.3
Hindalco	201	185	Hold	44763	24.7	18.4	21.3	8.1	10.9	9.4	4.8	5.6	5.1	10.3	8.3	8.8	9.6	6.6	7.1
Hind Zinc	208	235	Hold	87887	18.8	18.2	20.6	11.4	11.8	10.4	6.9	6.8	5.3	29.2	24.8	25.4	23.7	19.8	19.6
JSW Steel	248	235	Hold	59947	31.3	20.7	19.9	7.9	12.0	12.5	5.2	8.3	7.3	17.6	9.5	10.9	21.7	15.0	13.1
NMDC	114	95	Hold	34906	15.2	13.8	11.7	7.0	7.7	9.1	4.1	4.5	5.0	25.3	20.8	16.2	17.9	14.5	11.4
Vedanta	159	150	Hold	58941	18.1	21.4	26.0	8.8	7.4	6.1	4.0	3.6	3.0	11.9	13.1	15.0	10.8	11.8	13.1
Tata Steel	404	470	Buy	48654	78.6	42.1	67.7	6.0	11.2	6.9	5.0	7.0	5.6	13.4	7.8	10.0	13.0	7.4	10.5

Source: Company, ICICI Direct Research

## RATING RATIONALE

ICICI Direct endeavors to provide objective opinions and recommendations. ICICI Direct assigns ratings to its stocks according to their notional target price vs. current market price and then categorizes them as Buy, Hold, Reduce and Sell. The performance horizon is two years unless specified and the notional target price is defined as the analysts' valuation for a stock

Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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## ANALYST CERTIFICATION

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