

Tata Steel

BUY

Profitability firm; deleveraging continues

Summary

Tata Steel's Q2FY22 EBITDA was slightly below our estimate. India sales volumes increased by 11% QoQ to 4.58 mn tonnes and India operations EBITDA/t declined 10% QoQ to Rs29,256 due to rising coking coal costs. Nevertheless, European operations EBITDA/t increased 136% QoQ to Rs15,609 led by inventory gain and higher prices despite lower deliveries. Consolidated net debt fell Rs51 bn QoQ to Rs689 bn (\$2 bn deleveraging is likely in FY22 despite growth capex given upswing in steel cycle).

We introduce FY24 estimates in this report and roll over our valuation to FY24 estimates. We raise our FY22/FY23 EBITDA estimates by 10%/15% given firm steel prices which we expect to sustain over the coming one year. We raise our SOTP-based target price to Rs1,825 (earlier Rs1,735) and maintain our BUY rating on the stock.

Key Highlights and Investment Rationale

- European business financial performance stellar:** European EBITDA increased 2.2x QoQ to Rs33 bn despite flattish sales volumes of 2.1 mn tonnes. Tata Steel SEA registered an increase of 12% QoQ EBITDA to Rs4 bn (EBITDA/t of Rs7,244). However, Tata Steel Long Products EBITDA declined by 45% QoQ to Rs3 bn (EBITDA/t of Rs18,010) due to sharp increase in raw material cost.
- Free cash flows strong; expansion on track:** Despite working capital increase of Rs38 bn and capex of Rs21 bn, its free cash flow was strong at Rs39 bn in Q2FY22. Its 5 mtpa expansion continues to progress well while it has fast-tracked 6 mtpa pellet plant. Total capex outlay for FY22 is likely at Rs100-120 bn.
- Outlook:** After a strong profitability performance in H1FY22, we expect H2FY22 to be stronger for Tata Steel India operations as Chinese steel curbs are likely to keep steel prices firm. Also, we believe strong profitability and restructuring at its European operations will lead to further fall in net debt over FY22-FY24 even though Tata Steel will continue to pursue growth capex in India. Hence, we maintain our BUY rating on the stock.

TP	Rs1,825		
CMP	Rs1,287		
Potential upside / downside	42%		
Previous Rating	BUY		

V/s Consensus

EBITDA (Rs bn)	FY22E	FY23E	FY24E
IDBI Capital	277.7	244.1	210.6
Consensus	284.6	178.0	169.3
% difference	(2.4)	37.2	24.4

Shareholding Pattern (%)

Promoters	34.4
FII	22.4
DII	18.2
Public	25.0

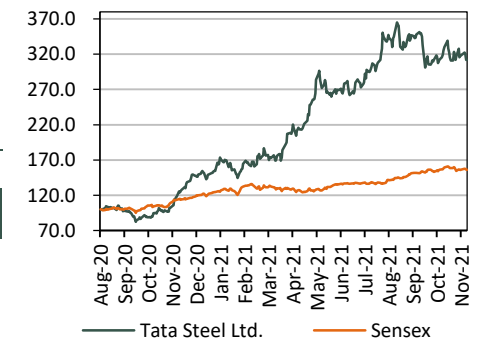
Price Performance (%)

	-1m	-3m	-12m
Absolute	(2.0)	(9.8)	171.2
Rel to Sensex	(2.9)	(21.1)	132.0

Key Stock Data

Bloomberg / Reuters	TATA IN / TISC.BO
Sector	Metal & Mining
Shares o/s (mn)	1,204
Market cap. (Rs mn)	1,549,581
Market cap. (US\$ mn)	20,899
3-m daily average value (Rs mn)	750.3
52-week high / low	Rs1,535 / 465
Sensex / Nifty	60,687 / 18,103

Relative to Sensex (%)



Financial snapshot

Year	FY20	FY21	FY22E	FY23E	FY24E
Revenue	14,89,717	15,62,942	2,113,741	2,026,053	1,769,356
EBITDA	1,78,276	3,05,043	608,238	552,517	496,856
EBITDA (%)	12.0	19.5	28.8	27.3	28.1
Adj. PAT	61,020	92,330	317,969	279,522	241,135
EPS (Rs)	53.3	80.6	277.7	244.1	210.6
EPS Growth (%)	(34.4)	51.3	244.4	(12.1)	(13.7)
PE (x)	26.9	17.8	4.8	5.4	6.3
Dividend Yield (%)	0.9	0.3	0.5	0.7	1.1
EV/EBITDA (x)	15.1	7.6	3.3	3.2	3.1
RoE (%)	8.6	12.5	35.4	23.5	16.8
RoCE (%)	4.7	11.1	27.7	23.3	20.6

Source: IDBI Capital Research;

Exhibit 1: Quarterly Snapshot

(Rs mn)

Financial snapshot	Q2FY22	Q1FY22	QoQ (%)	Q2FY21	YoY (%)
Net Sales	602,828	533,718	12.9	389,399	54.8
Total expenditure	438,267	372,613	17.6	327,272	33.9
EBITDA	164,561	161,106	2.1	62,127	164.9
<i>EBITDA margin (%)</i>	27.3%	30.2%	-289bps	16.0%	1134bps
Interest	10,198	18,114	(43.7)	19,480	(47.7)
Depreciation	22,889	23,245	(1.5)	23,251	(1.6)
PBT	141,196	121,368	16.3	22,742	520.9
Tax	15,719	23,084	(31.9)	6,092	158.0
PAT	125,477	97,684	28.5	16,650	653.6
Diluted EPS	109.6	85.3	28.5	14.5	653.6

Source: Company; IDBI Capital Research

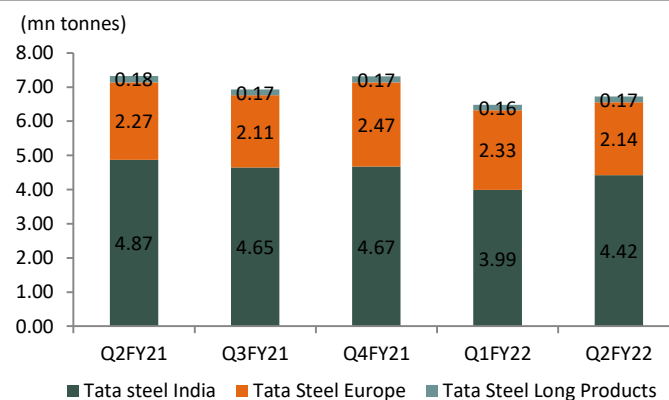
Exhibit 2: Actual vs estimates

(Rs mn)

	Q2FY22E	Q2FY22A	% Variance
Net sales	560,595	602,828	7.5
EBTIDA	176,826	164,561	(6.9)
<i>Margin (%)</i>	31.5	27.3	-424bps
PAT	100,918	125,477	24.3
Dil. EPS	95.6	109.6	14.6

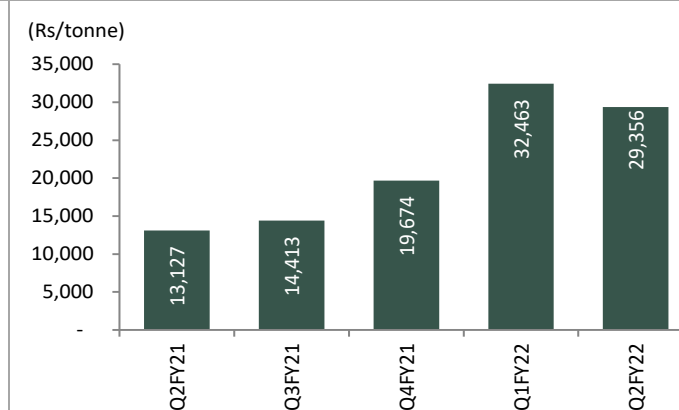
Source: Company; IDBI Capital Research

Exhibit 3: Geographical sales mix



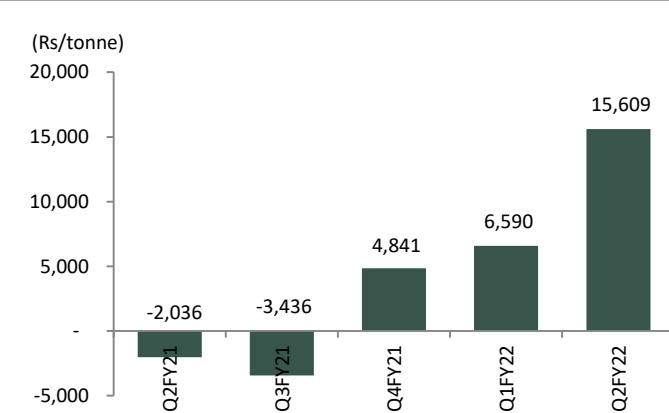
Source: Company; IDBI Capital Research

Exhibit 4: Standalone EBIDTA/tonne fell 10% QoQ



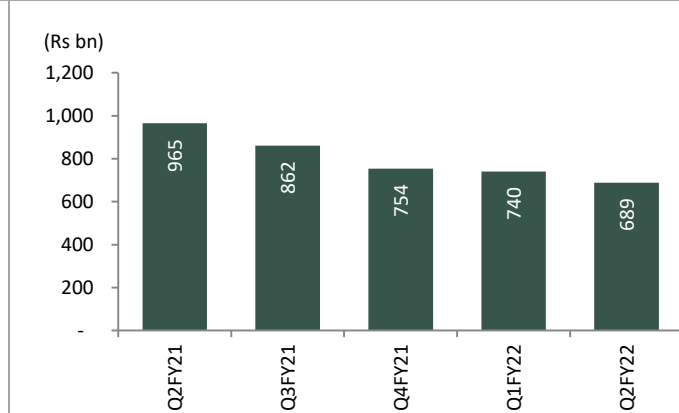
Source: Company; IDBI Capital Research

Exhibit 5: Tata Steel Europe EBIDTA/tonne jumps



Source: Company; IDBI Capital Research

Exhibit 6: Net debt continues to fall



Source: Company; IDBI Capital Research

Conference call highlights

- In Q2FY22, the Indian steel sales volume increased by 11% despite weakness in construction and infrastructure activities. However, sales to automotive segment increased by 18% on sequential basis
- China has cut the production of 4-5 mn tonnes till now to lower carbon emission which is benefiting Indian steel mills.
- The 5 MTPA expansion at Kalinganagar is expected to get commission by Q2FY23. Total capex spent was Rs.21bn during the quarter which includes pellet and Cold roll mill complex as well.
- Tata steel won Gandhalpada (Odisha) Iron ore mine which has 350 mn reserves and strategically located near Kalinganagar plant.
- During the quarter, steel prices remained stable while coking coal prices have jumped sharply to an average of \$223/tonne due to supply chain issues.
- Domestic steel prices were soft during July'21. The domestic realization are likely to be higher by Rs3,400/tonne QoQ.
- Going ahead, company is confident to maintain exports at low level, due to improvement in domestic demand.
- For Q3FY22, the company remains flattish on sales volume for Indian operations as well as European operations.
- The merger of Tata Steel BSL with Tata Steel has been done which has led to restatement in financials.

Exhibit 7: Change in estimates

	FY22E			FY23E			FY24E
	Old	New	(%) Chg	Old	New	(%) Chg	
Revenue (Rs mn)	17,10,207	21,13,741	23.6	18,51,578	20,26,053	9.4	17,69,356
EBITDA (Rs mn)	4,75,914	5,21,305	9.5	4,79,436	5,52,517	15.2	4,96,856
EBITDA margin (%)	27.8	24.7	-317bps	23.0	27.3	427bps	28.1
Net profit (Rs mn)	2,25,343	2,57,116	14.1	2,28,365	2,79,522	22.4	2,41,135
EPS (Rs)	196.8	224.57	14.1	199.5	244.1	22.4	210.6

Source: Company; IDBI Capital Research

Exhibit 8: SOTP-based valuation

	FY24 EBITDA	Multiple	(Rs bn)
India operations	4,14,336	4.5	18,64,512
TSE	38,000	3.0	1,14,000
Other operations	4,485	3.0	13,454
CWIP @ 70%			1,36,478
Derived enterprise value			21,28,444
Less: Net debt			38,367
Derived equity value			20,90,077
Target price (Rs/share)			1,825

Source: Company; IDBI Capital Research

Financial Summary

Profit & Loss Account

(Rs mn)

Year-end: March	FY21	FY22E	FY23E	FY24E
Net sales	1,562,942	2,113,741	2,026,053	1,769,356
<i>Growth (%)</i>	<i>4.9</i>	<i>35.2</i>	<i>(4.1)</i>	<i>(12.7)</i>
Operating expenses	(1,257,899)	(1,505,502)	(1,473,536)	(1,272,500)
EBITDA	305,043	608,238	552,517	496,856
<i>Growth (%)</i>	<i>71.1</i>	<i>99.4</i>	<i>(9.2)</i>	<i>-10.1</i>
Depreciation	(92,336)	(93,260)	(94,192)	(95,134)
EBIT	212,706	514,979	458,325	401,722
Interest paid	(76,067)	(74,926)	(73,802)	(72,695)
Other income	8,956	9,046	9,136	9,227
Pre-tax profit	135,164	449,098	393,659	338,254
Tax	(56,539)	(134,729)	(118,098)	(101,476)
<i>Effective tax rate (%)</i>	<i>41.8</i>	<i>30.0</i>	<i>30.0</i>	<i>30.0</i>
Share in Associates	3,273	3,601	3,961	4,357
Net profit	81,898	317,969	279,522	241,135
Exceptional items	(10,432)	-	-	-
Adjusted net profit	92,330	317,969	279,522	241,135
<i>Growth (%)</i>	<i>51.3</i>	<i>244.4</i>	<i>(12.1)</i>	<i>(13.7)</i>
<i>Shares o/s (mn)</i>	<i>1,145</i>	<i>1,145</i>	<i>1,145</i>	<i>1,145</i>

Cash Flow Statement

(Rs mn)

Year-end: March	FY21	FY22E	FY23E	FY24E
Pre-tax profit	135,164	449,098	393,659	338,254
Depreciation	92,336	93,260	94,192	95,134
Tax paid	(59,816)	(134,729)	(118,098)	(101,476)
Chg in working capital	245,281	(57,689)	18,265	40,214
Other operating activities	60,105	-	-	-
Cash flow from operations (a)	473,071	349,940	388,019	372,126
Capital expenditure	(99,687)	(120,000)	(120,000)	(120,000)
Chg in investments	6,536	-	-	-
Other investing activities	-	-	-	-
Cash flow from investing (b)	(93,151)	(120,000)	(120,000)	(120,000)
Equity raised/(repaid)	527	-	-	-
Debt raised/(repaid)	(408,807)	(100,000)	(300,000)	(250,000)
Dividend (incl. tax)	(4,469)	(7,150)	(10,726)	(16,088)
Chg in minorities	10,104	3,601	3,961	4,357
Other financing activities	-	-	-	-
Cash flow from financing (c)	(402,645)	(103,550)	(306,765)	(261,732)
Net chg in cash (a+b+c)	(22,725)	126,390	(38,746)	(9,605)

Balance Sheet

(Rs mn)

Year-end: March	FY21	FY22E	FY23E	FY24E
Net fixed assets	1,547,826	1,574,566	1,600,374	1,625,239
Investments	34,630	34,630	34,630	34,630
Other non-curr assets	270,297	300,839	335,046	373,358
Current assets	602,119	790,267	711,468	618,567
Inventories	332,764	402,308	385,618	336,761
Sundry Debtors	95,398	104,239	99,915	87,256
Cash and Bank	57,822	154,810	82,845	35,720
Marketable Securities	-	-	-	-
Loans and advances	-	-	-	-
Other current assets	116,135	128,910	143,090	158,830
Total assets	2,454,872	2,700,303	2,681,518	2,651,795
Shareholders' funds	742,388	1,053,207	1,322,003	1,547,049
Share capital	11,976	11,976	11,976	11,976
Reserves & surplus	730,412	1,041,231	1,310,027	1,535,073
Total Debt	724,088	624,088	324,088	74,088
Secured loans	724,088	624,088	324,088	74,088
Unsecured loans	-	-	-	-
Other liabilities	247,028	260,944	276,111	292,644
Curr Liab & prov	708,671	729,367	726,619	705,317
Current liabilities	661,418	682,114	679,365	658,064
Provisions	47,253	47,253	47,253	47,253
Total liabilities	1,679,788	1,614,399	1,326,818	1,072,049
Total equity & liabilities	2,454,872	2,700,303	2,681,518	2,651,795
Book Value (Rs)	648	920	1,155	1,351

Source: Company; IDBI Capital Research

Financial Ratios

Year-end: March	FY21	FY22E	FY23E	FY24E
Adj. EPS (Rs)	80.6	277.7	244.1	210.6
Adj. EPS growth (%)	51.3	244.4	(12.1)	(13.7)
EBITDA margin (%)	19.5	28.8	27.3	28.1
Pre-tax margin (%)	8.6	21.2	19.4	19.1
ROE (%)	12.5	35.4	23.5	16.8
ROCE (%)	11.1	27.7	23.3	20.6
Turnover & Leverage ratios (x)				
Asset turnover (x)	0.6	0.8	0.8	0.7
Leverage factor (x)	3.4	2.9	2.3	1.9
Net margin (%)	5.9	15.0	13.8	13.6
Net Debt/Equity (x)	0.9	0.4	0.2	0.0
Working Capital & Liquidity ratio				
Inventory days	78	69	69	69
Receivable days	22	18	18	18
Payable days	103	84	76	72

Valuation

Year-end: March	FY21	FY22E	FY23E	FY24E
P/E (x)	16.4	4.8	5.4	6.3
Price / Book value (x)	2.0	1.4	1.1	1.0
PCE (x)	8.2	3.7	4.0	4.5
EV / Net sales (x)	1.4	0.9	0.9	0.9
EV / EBITDA (x)	7.1	3.3	3.2	3.1
Dividend Yield (%)	0.3	0.5	0.7	1.1



Notes

Dealing

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Key to Ratings Stocks:**BUY:** 15%+; **HOLD:** -5% to 15%; **SELL:** -5% and below.**IDBI Capital Markets & Securities Ltd.****Equity Research Desk**

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