

BUY

TP: Rs 1,700 | ▲ 32%

TATA STEEL

Metals & Mining

05 May 2022

Results in line; growth allocation to improve – BUY

- Q4 results in line with consensus, dividend payout raised to 15% with improved gearing, and 10:1 stock split announced
- Key catalysts include timely delivery on capital projects, sustained viability of European operations and clarity on next wave of projects
- Maintain BUY with reduced TP of Rs 1,700 (vs. Rs 1,755) based on lower target EV/EBITDA of 6.0x (from 6.5x) to reflect economic uncertainty

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Results in line: TATA's Q4FY22 adjusted EBITDA at Rs 158.9bn and net income at Rs 97.6bn were broadly in line with consensus. The company has reduced net debt by Rs 240bn YoY to Rs 510bn, bringing the net debt/EBITDA ratio below 1x. With lower leverage, TATA has doubled its dividend payout to Rs 51/sh, ahead of consensus estimates of Rs 38, offering a 4% trailing yield. It has also announced a 10:1 stock split.

Capital allocation on growth projects set to improve: With a decline in leverage, TATA is evaluating higher capital allocation to growth projects in order to channelise its surplus cash flow after a US\$ 1bn reduction in net debt and 15-20% shareholder payout. This could help accelerate investments aimed at delivering its 5mtpa Kalinganagar expansion by FY25 and defining the next wave of growth projects. The company is looking to raise steel capacity to 25mtpa by FY25 and 40mtpa by 2030.

Steel margins to stabilise at healthy cycle average: Steel prices have recently been supported by supply disruptions due to the Russia-Ukraine conflict and a tight coking coal market. However, with a weakening demand outlook, prices could eventually soften from current levels as disruptions ease. We expect an improving supply-demand balance to support steel at a healthy cyclical average of US\$ 650/t in FY24 – our base for valuation. Key price supports are (a) stabilisation of real estate demand in China, (b) decarbonisation measures limiting exports out of China, (c) a balanced ex-China market, and (d) gradual stabilisation of coking coal and iron ore supply chains.

Maintain BUY: We raise our FY23 EBITDA estimate for TATA by 29% (no change for FY24) as we cautiously increase our India HRC price forecast to US\$ 800/t. At the same time, we lower our target 1Y forward EV/EBITDA multiple to 6.0x (from 6.5x) to reflect economic uncertainty and also roll valuations forward to FY24 with India HRC price forecast of US\$650/t. Our TP thus reduces to Rs 1,700 (from Rs 1,755). We maintain our rating at BUY given the company's healthy growth and margin profile. TATA is trading at 4.4x FY24E EV/EBITDA compared to its 5Y/10Y mean of 5.5x/5.8x.

Key changes

Target	Rating
▼	◀ ▶

Ticker/Price	TATA IN/Rs 1,284
Market cap	US\$ 20.6bn
Free float	66%
3M ADV	US\$ 141.9mn
52wk high/low	Rs 1,535/Rs 1,043
Promoter/FPI/DII	34%/23%/22%

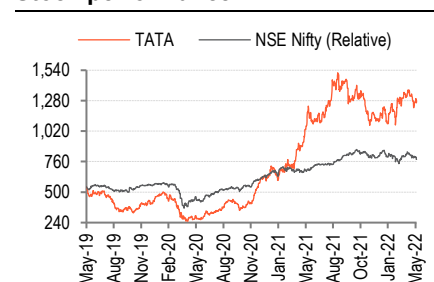
Source: NSE | Price as of 5 May 2022

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	2,423	2,313	2,029
EBITDA (Rs mn)	635	517	419
Adj. net profit (Rs mn)	402	280	200
Adj. EPS (Rs)	328.5	229.4	164.0
Consensus EPS (Rs)	0.0	215.9	188.9
Adj. ROAE (%)	42.6	22.2	13.7
Adj. P/E (x)	3.9	5.6	7.8
EV/EBITDA (x)	3.9	4.3	4.9
Adj. EPS growth (%)	436.1	(30.2)	(28.5)

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Q4 results in line

- Q4 results:** While TATA's Q4FY22 adjusted EBITDA at Rs 158.9bn was in line with consensus, net income at Rs 97.6bn was marginally (3%) ahead. The company has lowered net debt by Rs 240bn YoY to Rs 510bn, bringing the net debt/EBITDA ratio below 1x. With lower leverage, TATA has doubled its dividend payout to Rs 51/sh, ahead of consensus expectations of Rs 38.4. The dividend offers a 4% trailing yield. Management has also announced a 10:1 stock split.

Sequentially, Q4 EBITDA was flat QoQ as a 3% sequential decline in India was offset by a 48% increase in Europe. Standalone India business realisation was better than earlier guidance, restricting the EBITDA decline to Rs 4.9k/t QoQ. The margin contraction was significantly offset by a 17% QoQ increase in sales, liquidating inventory. European business benefitted from an 11% QoQ increase in sales and a 33% improvement in EBITDA/t, with higher contractual realisation flowing through the P&L.

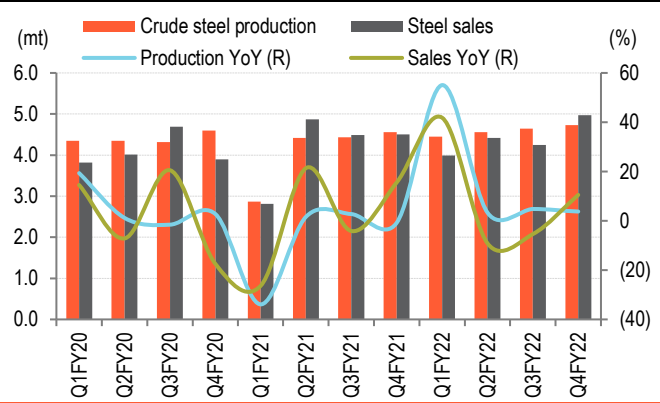
- Possibility of margin uptick in Q1FY23:** TATA has guided for a Rs 8,000-8,500/t QoQ increase in India realisation which is likely to be partially negated by a US\$ 100/t QoQ increase in coking coal costs. For Europe business, realisation is likely to rise by GBP 60/t QoQ, again partly offset by a EUR 60/t QoQ rise in coking coal cost. With 75-80% of the energy costs in Europe being hedged (was 90% in Q4), energy cost is trending flat QoQ till end-April.
- FY23 earnings levers:** TATA is guiding for a modest 0.5mtpa YoY increase in FY23 (excluding NINL) as operations are running close to full utilisation. The company is looking to commission its 6mtpa pellet expansion by early-Q3, a 2.2mtpa PLT CRM line in Q3 and other projects progressively by H1FY24 (annealing 0.9mtpa, galvanising 0.53mt + 0.47mt).
- NINL update:** TATA is aiming to close the NINL (Neelachal Ispat Nigam) acquisition in Q1FY23, restart the latter's blast furnace over the next three months and take operations to rated capacity within a year. The facility could be expanded to 5mtpa over three years with Rs 200bn-250bn of capex.

Fig 1 – Quarterly performance

(Rs bn)	Q4FY22	Q3FY22	QoQ (%)	Q4FY21	YoY (%)	FY22	FY21	YoY (%)
Consolidated P&L								
Revenue from operations	693	608	14.1	500	38.6	2,439	1,565	55.8
Adj. EBITDA	159	159	0.0	139	14.1	655	289	126.4
EBIT	128	136	(6.3)	118	8.4	544	213	155.7
PBT before exceptionals	121	124	(1.8)	103	17.3	504	149	238.3
PAT	98	96	2.5	72	37.3	417	82	409.8
Net income to owners	98	96	1.9	66	46.8	402	75	436.1
EPS (Rs)	80	79	1.0	57	39.7	332	64	420.7
Effective tax rate (%)	16.7	20.8		21.2		16.8	38.0	(55.7)
Adj. EBITDA break-up								
Standalone (incl BSL)	118	122	(3.4)	117	0.4	506	273	85.0
Europe	43	29	47.8	12	264.2	122	(6)	2,068.3
Long Products	2	3	(30.6)	5	(65.0)	13	12	11.5
SEA	1	2	(37.0)	2	(36.3)	-	-	-
Others	(5)	4	(242.9)	4	(243.3)	-	-	-
Consolidated	159	159	0.0	139	14.1	655	289	126.4
Standalone operational parameters								
Production (mt)	4.7	4.6	1.9	4.6	3.7	18.4	16.3	12.9
Sales (mt)	5.0	4.3	16.9	4.5	10.4	17.6	16.6	6.0
Apparent realisation (Rs'000/t)	73.8	75.2	(1.9)	60.8	21.4	73.1	50.6	44.5
EBITDA (Rs'000/t)	23.7	28.7	(17.4)	26.0	(9.1)	28.7	16.4	74.6
Europe operational parameters								
Production (mt)	2.3	2.6	(10.1)	2.7	(13.2)	10.1	9.6	5.9
Sales (mt)	2.4	2.2	11.1	2.5	(2.8)	9.0	8.8	2.3
Apparent realisation (Rs'000/t)	110.0	105.4	4.3	69.9	57.4	99.7	63.5	57.1
EBITDA (Rs'000/t)	18.1	13.6	33.0	4.8	274.9	13.5	(0.7)	2,024.7
EBITDA (US\$/t)	241	182	32.5	66	263.2	181	(9)	2,017.6
Consolidated operational parameters								
Production (mt)	7.6	7.8	(1.8)	8.0	(5.0)	31.0	28.5	8.7
Sales (mt)	8.0	7.0	14.3	7.8	2.3	29.5	28.5	3.6
Apparent realisation (Rs'000/t)	86.5	86.7	(0.2)	63.9	35.5	82.6	54.9	50.5
EBITDA (Rs'000/t)	19.8	22.7	(12.5)	17.8	11.5	22.2	10.1	118.6

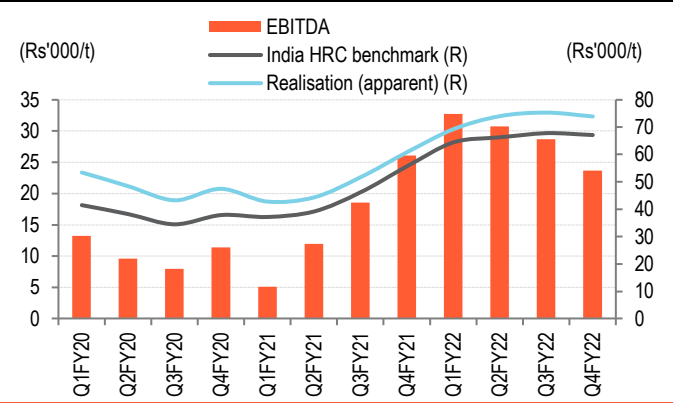
Source: Company, BOBCAPS Research

Fig 2 – Standalone production and sales inched closer to capability



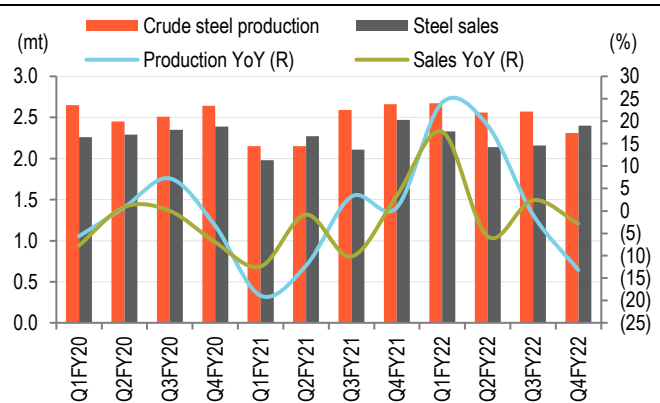
Source: Company, BOBCAPS Research

Fig 3 – Standalone EBITDA remains strong even after some moderation



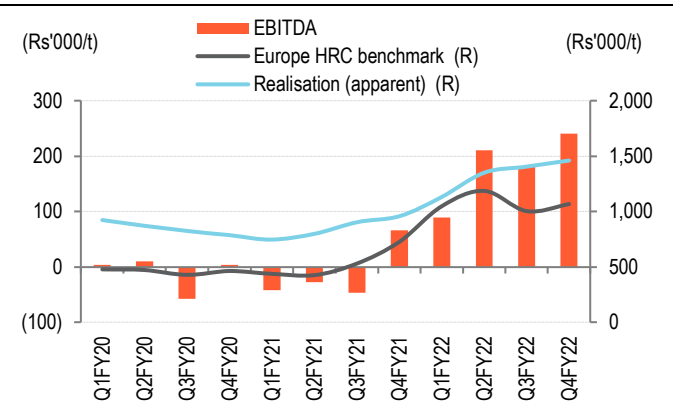
Source: Company, BOBCAPS Research

Fig 4 – Europe sales picked up, liquidating inventory



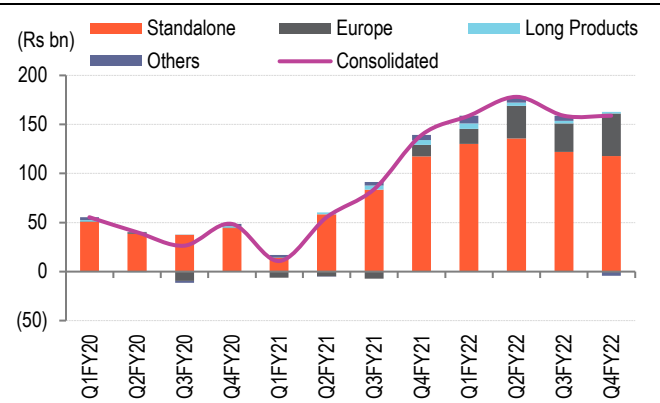
Source: Company, BOBCAPS Research

Fig 5 – Europe EBITDA expanded, benefitting from flow-through of contractual realisation in P&L



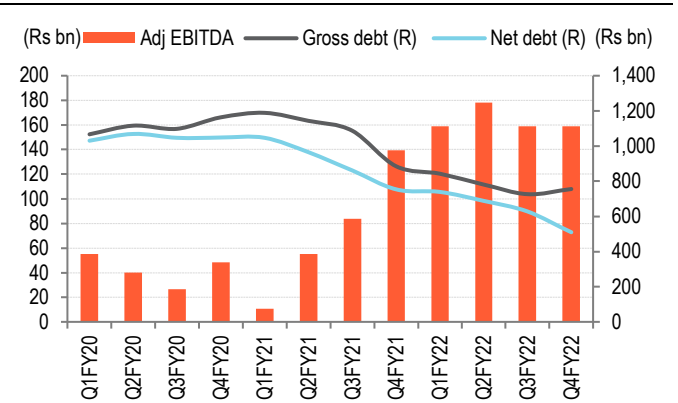
Source: Company, BOBCAPS Research

Fig 6 – Total EBITDA flat QoQ as decline in India margin was offset by higher volumes and higher Europe margin



Source: Company, BOBCAPS Research

Fig 7 – Consolidated net debt down Rs 240bn in FY22



Source: Company, BOBCAPS Research

Valuation methodology

Forecast changes

Accounting for FY22 actuals and our revised commodity assumptions (FY23 India HRC price forecast raised from US\$ 653/t to US\$ 800/t), we revise our FY23 EBITDA estimate up by 29% (no change for FY24). We also roll forward our forecasts to FY25.

Fig 8 – Revised estimates

(Rs bn)	Actual	New			Old		Change (%)	
	FY22	FY23E	FY24E	FY25E	FY23E	FY24E	FY23E	FY24E
Revenue	2,423	2,313	2,029	2,022	1,863	1,850	24.2	9.7
EBITDA	635	517	419	421	400	419	29.2	0.0
EBITDA growth YoY (%)	108	(19)	(19)	1	(22)	5	-	-
Net income	402	280	200	198	189	199	48.4	1.0

Source: Company, BOBCAPS Research

Fig 9 – Key assumptions

Parameter	FY22	FY23E	FY24E	FY25E
Sales India (mt)	19.0	19.3	19.3	19.3
Sales Europe (mt)	9.0	9.0	9.0	9.0
India HRC price (\$/t)	891	800	650	639
EBITDA/t Standalone+Bhushan (Rs'000/t)	26.9	22.9	18.7	17.8
EBITDA/t Europe (US\$/t)	180	133	83	80

Source: Company, BOBCAPS Research

Maintain BUY, TP at Rs 1,700

We roll forward our valuation to FY24 while lowering our target one-year forward EV/EBITDA multiple to 6.0x (from 6.5x), accounting for increased uncertainty due to a slower-than-anticipated recovery in China and risks to global demand from the inflationary impact of the Russia-Ukraine war. This yields a revised TP of Rs 1,700 (vs. Rs 1,755 earlier).

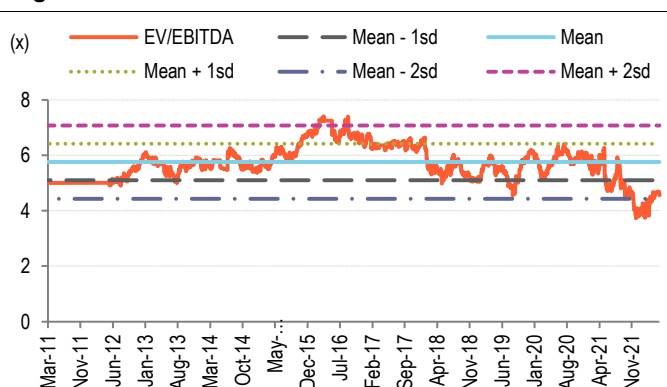
Our valuation multiple is in line with our target 6x multiple for the Indian steel sector and reflects TATA's healthy margin and growth profile. We are also in line with the stock's historical trading average of 5.9x/6.3x over the past five/ten-year period. Maintain BUY.

Fig 10 – Valuation summary

(Rs bn)	Value
FY24E EBITDA	419
Target EV/EBITDA multiple	6
EV	2,514
FY23E Net debt	436
Equity value	2,078
Fair value (Rs)	1,700
Target price Mar'23 (rounded to nearest Rs 5)	1,700

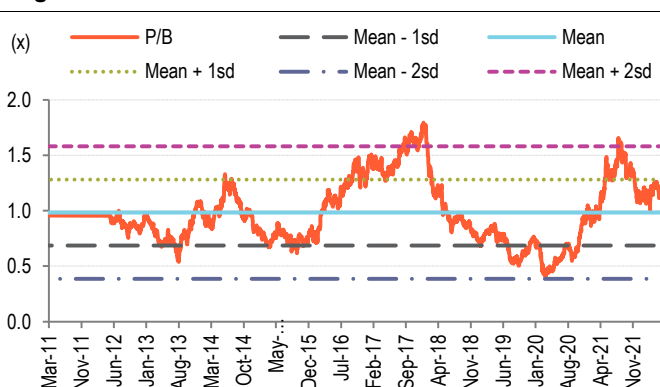
Source: BOBCAPS Research

Fig 11 – EV/EBITDA 2Y forward



Source: Bloomberg, BOBCAPS Research

Fig 12 – P/B 1Y forward



Source: Bloomberg, BOBCAPS Research

Fig 13 – Peer comparison

Ticker	CMP	Rating	Target price	Upside (%)	EV/Sales (x)		EV/EBITDA (x)		Net income (Rs bn)		P/B (x)		P/E (x)	
					FY23E	FY24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
TATA IN	1,284	BUY	1,700	32.4	0.9	0.9	3.9	4.5	280	200	1.4	1.0	5.6	7.8
JSTL IN	708	BUY	810	14.4	1.5	1.5	5.9	5.5	193	196	2.6	1.7	8.9	8.7
JSP IN	523	BUY	555	6.1	1.5	1.4	5.1	4.4	57	67	1.4	1.0	9.4	8.0
SAIL IN	94	HOLD	150	59.4	0.7	0.6	3.7	3.1	80	93	0.7	0.6	4.9	4.2

Source: BOBCAPS Research

Key risks

- Steel producer valuations are highly sensitive to product and raw material prices. Key downside risks to our estimates are unfavourable changes in global demand-supply balance for steel and its raw materials, leading to lower prices and margins than our assumptions.
- TATA is exposed to risk of delay in implementation of its capital investment plan including expansion, which could impact its earnings growth. The company is targeting completion of margin enhancement projects such as the pellet plant and cold rill mill at Kalinaganagar plant by mid-FY24. It is also expanding Kalinaganagar capacity by 5mtpa to raise total India capacity to 25mt by FY25.

Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Jindal Steel & Power	JSP IN	7.0	523	555	BUY
JSW Steel	JSTL IN	22.4	708	810	BUY
SAIL	SAIL IN	5.1	94	150	HOLD
Tata Steel	TATA IN	20.6	1,284	1,700	BUY

Source: BOBCAPS Research, NSE | Price as of 5 May 2022

Financials

Income Statement

Y/E 31 Mar (Rs bn)	FY21A	FY22A	FY23E	FY24E	FY25E
Total revenue	1,547	2,423	2,313	2,029	2,022
EBITDA	305	635	517	419	421
Depreciation	(92)	(91)	(97)	(102)	(106)
EBIT	213	544	420	317	315
Net interest inc./(exp.)	(76)	(55)	(51)	(45)	(39)
Other inc./(exp.)	9	8	13	11	11
Exceptional items	(10)	(1)	0	0	0
EBT	138	502	389	290	294
Income taxes	(57)	(85)	(97)	(81)	(88)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	3	6	6	6	6
Reported net profit	75	402	280	200	198
Adjustments	0	0	0	0	0
Adjusted net profit	75	402	280	200	198

Balance Sheet

Y/E 31 Mar (Rs bn)	FY21A	FY22A	FY23E	FY24E	FY25E
Accounts payables	260	368	369	331	329
Other current liabilities	241	260	244	214	214
Provisions	47	28	28	28	28
Debt funds	885	756	676	596	516
Other liabilities	247	273	261	235	235
Equity capital	12	12	12	12	12
Reserves & surplus	730	1,132	1,368	1,533	1,698
Shareholders' fund	775	1,171	1,418	1,591	1,764
Total liab. and equities	2,455	2,854	2,996	2,994	3,084
Cash and cash eq.	130	244	240	284	354
Accounts receivables	95	122	127	111	111
Inventories	333	488	492	441	439
Other current assets	44	71	66	61	61
Investments	43	54	54	54	54
Net fixed assets	1,190	1,162	1,239	1,191	1,190
CWIP	181	212	282	352	372
Intangible assets	30	45	40	44	48
Deferred tax assets, net	0	0	0	0	0
Other assets	452	510	510	510	510
Total assets	2,455	2,854	2,996	2,994	3,084

Cash Flows

Y/E 31 Mar (Rs bn)	FY21A	FY22A	FY23E	FY24E	FY25E
Cash flow from operations	369	455	408	348	340
Capital expenditures	(85)	(109)	(239)	(129)	(129)
Change in investments	(9)	(11)	0	0	0
Other investing cash flows	75	(40)	13	11	11
Cash flow from investing	(19)	(159)	(226)	(118)	(118)
Equities issued/Others	1	0	0	0	0
Debt raised/repaid	(248)	(129)	(80)	(80)	(80)
Interest expenses	(76)	(55)	(51)	(45)	(39)
Dividends paid	(30)	(62)	(56)	(43)	(41)
Other financing cash flows	19	65	(1)	(18)	7
Cash flow from financing	(335)	(181)	(187)	(186)	(152)
Chg in cash & cash eq.	15	114	(4)	44	70
Closing cash & cash eq.	130	244	240	284	354

Per Share

Y/E 31 Mar (Rs)	FY21A	FY22A	FY23E	FY24E	FY25E
Reported EPS	61.3	328.5	229.4	164.0	161.8
Adjusted EPS	61.3	328.5	229.4	164.0	161.8
Dividend per share	24.5	51.0	45.5	35.4	33.3
Book value per share	607.3	936.2	1,129.2	1,264.3	1,399.2

Valuations Ratios

Y/E 31 Mar (x)	FY21A	FY22A	FY23E	FY24E	FY25E
EV/Sales	1.6	1.0	1.0	1.0	1.0
EV/EBITDA	8.2	3.9	4.3	4.9	4.6
Adjusted P/E	21.0	3.9	5.6	7.8	7.9
P/BV	2.1	1.4	1.1	1.0	0.9

DuPont Analysis

Y/E 31 Mar (%)	FY21A	FY22A	FY23E	FY24E	FY25E
Tax burden (Net profit/PBT)	50.3	79.7	72.1	69.2	67.3
Interest burden (PBT/EBIT)	70.0	92.6	92.5	91.3	93.2
EBIT margin (EBIT/Revenue)	13.7	22.4	18.2	15.6	15.6
Asset turnover (Rev./Avg TA)	62.4	91.3	79.1	67.7	66.5
Leverage (Avg TA/Avg Equity)	3.4	2.8	2.3	2.0	1.9
Adjusted ROAE	10.1	42.6	22.2	13.7	12.2

Ratio Analysis

Y/E 31 Mar	FY21A	FY22A	FY23E	FY24E	FY25E
YoY growth (%)					
Revenue	5.9	56.6	(4.6)	(12.3)	(0.3)
EBITDA	71.1	108.1	(18.6)	(18.9)	0.5
Adjusted EPS	350.7	436.1	(30.2)	(28.5)	(1.3)
Profitability & Return ratios (%)					
EBITDA margin	19.7	26.2	22.3	20.7	20.8
EBIT margin	13.7	22.4	18.2	15.6	15.6
Adjusted profit margin	4.8	16.6	12.1	9.9	9.8
Adjusted ROAE	10.1	42.6	22.2	13.7	12.2
ROCE	11.1	26.9	19.0	13.7	13.2
Working capital days (days)					
Receivables	23	18	20	20	20
Inventory	79	74	78	79	79
Payables	75	74	75	75	75
Ratios (x)					
Gross asset turnover	0.6	0.9	0.8	0.7	0.7
Current ratio	0.8	1.0	1.0	1.1	1.2
Net interest coverage ratio	2.8	10.0	8.3	7.1	8.2
Adjusted debt/equity	1.0	0.4	0.3	0.2	0.1

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Disclaimer

Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

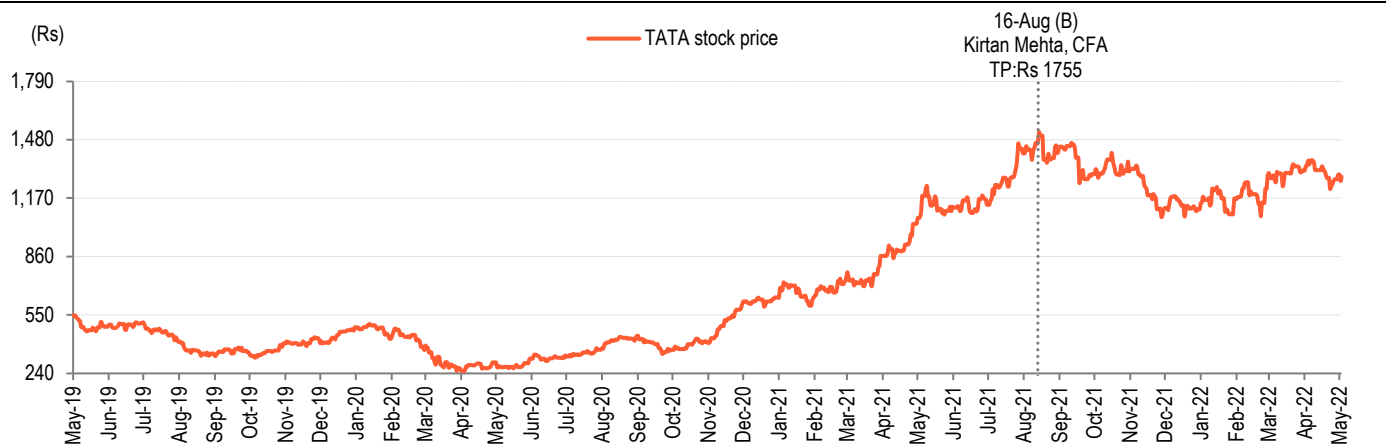
HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

Ratings and Target Price (3-year history): TATA STEEL (TATA IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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