

## Weak Q3; Downgrade to HOLD on European Woes

Est. Vs. Actual for Q3FY23: Revenue – **BEAT**; EBITDA – **MISS**; PAT – **MISS**

Growth Estimates YoY post Q3FY23: FY24E/FY25E: Revenue 1%/1%; EBITDA: (21)%/36%; PAT: (19%)/82%

### Recommendation Rationale

- **European operations to remain under pressure for upcoming three quarters:** Weak demand, higher energy costs, and re-lining of the blast furnace in Netherlands could keep Europe in EBITDA loss for the next three quarters.
- **Indian operations to remain robust** and we expect margin expansion in India business in Q4FY23. However, NINL remained a drag in Q3FY23, though relief is expected as production ramps up to 1MT in FY24.
- **Debt reduction target of \$1 Bn per annum is deferred to the next year** on volatile earnings, TSK capex, NINL acquisition (~Rs 10,000 Cr), and dividend payments (Rs 6,000 Cr) in FY23. Net-debt remained flat QoQ at Rs 71,706 Cr in Q3FY23.

**Sector Outlook:** Cautious

**Company Outlook & Guidance:** Avg. steel prices in India will be up by Rs 1,300-1,500/t in Q4FY23 QoQ. EBITDA/t in India is expected to improve QoQ on higher steel prices and stable costs. At consolidated level, in Q4FY23, additional volume of ~0.5MT QoQ is expected. At Europe, realisations will be £70/t lower QoQ as contract prices are lower than spot. Cost at Europe to come down by £100/t QoQ (Q3 impacted by ~£55m NRV loss), leading to EBITDA/t improvement QoQ. However, EBITDA/t is expected to remain negative until the next 3 quarters as demand is still weak.

**Current Valuation:** 6.0x EV/EBITDA on FY25E EBITDA (Earlier: 5.3x EV/EBITDA on Sep'24 EBITDA). India, Europe, Others : 6.4x, 3.5x, 5.0x (vs earlier at 6.0x, 3.5x, 5.0x)

**Current TP:** Rs 120/share (Earlier TP: Rs 117/share)

**Recommendation:** In light of the drag from TSE, we downgrade Tata Steel from BUY to HOLD.

**Financial Performance:** Tata Steel posted weak results with revenue largely in line with consensus but missed on EBITDA and PAT. Consolidated revenue declined by 6%/5% YoY/QoQ, led by lower realisations across geographies. EBITDA fell by 74%/34% YoY/QoQ (~30% miss against our consensus), primarily led by EBITDA loss in Europe. TSE EBITDA fell to the loss of Rs 1,551 Cr against the profit of Rs 1,788 Cr in Q2FY23 on account of higher energy prices and one time impact of £55 Mn as NRV loss on steel slab inventory in Europe to be consumed during the re-lining of one of the blast furnaces. Losses in Europe offset the EBITDA gain in India on lower coking coal costs. The company reported a net loss of Rs 2,502 Cr against the profit of Rs 1,297 Cr in Q2FY23. Net loss includes the one-time impact of non-cash deferred tax of Rs 2,150 Cr, primarily relating to movement in BSPS.

**Outlook:** Although the Indian operations could see improvement in EBITDA/t in subsequent quarters on the back of higher steel prices, the European operations are expected to remain a drag with negative EBITDA/t for the next 3 quarters. China's reopening has led to optimism on the steel cycle and HRC prices are already up 7% since Jan'23. However, further upside will be contingent on the real demand uptick in China (which will be the key trigger) which is yet to pick up.

**Valuation & Recommendation:** We value the company using SoTP by assigning a 1-year forward EV/EBITDA based on its geographical segments. We ascribe 6.4x, 5.0x, and 3.5x multiple to India standalone, other operations (excl standalone), and Europe on FY25 EBITDA (Rollover from Sep'24E EBITDA) to arrive at a 1-year forward TP of Rs 120/share (from the previous TP of Rs 117/share). The TP implies an upside potential of 9% from the CMP. We downgrade to **HOLD** from BUY.

### Key Financials (Consolidated)

(Rs Cr)	Q3FY23	QoQ (%)	YoY (%)	Axis Est.	Variance
Net Sales	57,084	-5%	-6%	51,737	10%
EBITDA	4,156	-34%	-74%	5,692	-27%
Adj EBITDA/t	3,812	-53%	-83%	7,853	-51%
Underlying Net Profit	-332	NA	NA	1,279	NA
EPS (Rs) Reported	-1.8	NA	NA	1.05	NA

Source: Company, Axis Research

(CMP as of 7<sup>th</sup> Feb 2023)

CMP (Rs)	111
Upside /Downside (%)	8%
High/Low (Rs)	139/83
Market cap (Cr)	1,36,190
Avg. daily vol. (6m) Shrs.	5,56,03,837
No. of shares (Cr)	1,221

### Shareholding (%)

	Jun-22	Sep-22	Dec-22
Promoter	33.92	33.92	33.9
FII	21.95	21.52	21.87
Mutual Funds / UTI	9.21	7.31	8.18
Financial Institutions	0.07	0.09	0.07
Others	34.85	37.16	35.98

### Financial & Valuations

Y/E Mar (Rs Cr)	FY23E	FY24E	FY25E
Net Sales	2,38,744	2,40,484	2,42,784
EBITDA	30,151	23,763	32,271
Net Profit	7,831	6,315	11,504
EPS (Rs.)	6.8	5.5	9.8
PER (x)	16.5x	20.2x	11.4x
P/BV (x)	1.1x	1.1x	1.0x
EV/EBITDA (x)	6.6x	8.4x	6.0x
ROE (%)	6%	5%	9%

### Change in Estimates (%)

Y/E Mar	FY23E	FY24E	FY25E
Sales	3%	2%	4%
Adj EBITDA	-8%	-28%	-12%
Attrib PAT	-42%	-54%	-29%

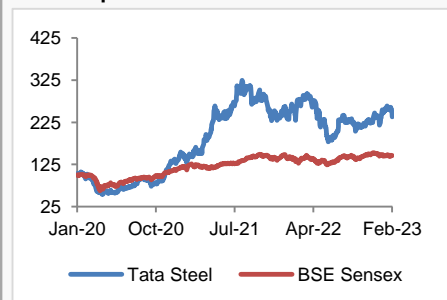
### ESG disclosure Score\*\*

Environmental Disclosure	25.70
Social Disclosure Score	13.88
Governance Disclosure	89.86
Total ESG Disclosure Score	43.20

Source: Bloomberg, Scale: 0.1-100

\*\*Note: This score measures the amount of ESG data a company reports publicly and does not measure the company's performance on any data point. All scores are based on 2020 disclosures

### Relative performance



Source: Capitaline, Axis Securities

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## Key Concall Highlights

- As a plan to grow towards the 40 MTPA capacity target in India, the company has begun operations at Neelachal Ispat Nigam Limited (NINL) and it is being ramped to a rated capacity of around 1MTPA. FY24 should fully reflect the incremental 1mtpa NINL volumes. The company expects the Kalinganagar phase II 5MTPA blast furnace and the ramp-up of the 0.75MTPA Electric Arc Furnace at Punjab to start in FY25. (exact volume guidance for FY25 to be provided in Q4FY23 concall). The downstream facilities of the 6 MTPA pellet plant and 2.2 MTPA Cold Roll Mill at Kalinganagar however are under phased commissioning. The Company will stop buying pellets from Q2FY24 providing cost savings.
- Coking coal consumption costs were lower by \$80-90/t in both India and Europe in Q3FY23 QoQ. In Q4FY23, a \$10/t reduction in coking coal cost is expected QoQ. For Iron ore in Europe, the company saw the benefit of \$20/t in Q3 compared to Q2FY23, however, the benefit will go down to \$10/t as iron ore prices have increased.
- Operating cash flow for Q3FY23 stood at Rs 5,000Cr vs Rs 17,000Cr in Q2FY23, led by WC release in UK and India on account of lower inventory levels, partially offset by the increase in slab stocks in Netherlands. As slab stocks get consumed over the next two quarters, the company expects WC to come down.
- Capex stood at Rs 3,632Cr in Q3FY23 (9M capex at Rs 9,746Cr). The company will spend Rs 3,000Cr capex in Q4 to accelerate the completion of the Kalinganagar expansion project.
- Tata Steel Netherlands (TSN) will undertake BF relining in Q4FY24 (BF shut down for 120 days) with a capex of €250-275Mn. TSN has cash of €600Mn, so no need for cash from India.
- The UK government provided a partial government grant for the green steel transition. The company is evaluating this support and developing investment options which have to be capital efficient and viable. The company ask was 50% of capex as grants and opex support for energy cost (Gas and hydrogen are not correlated with steel prices and can drive volatility in steel margins).

## Key Risks to our Estimates and TP

- The key risk to our HOLD rating is the increase in HRC prices in China (higher than our assumption), which could lead to higher prices in the rest of the world.
- Lower coking coal costs than our assumptions.

## Change in Estimates

	New			Old			% Change		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Sales	2,38,744	2,40,484	2,42,784	2,32,556	2,35,640	2,34,539	3%	2%	4%
EBIDTA	30,151	23,763	32,271	32,867	33,019	36,866	-8%	-28%	-12%
PAT (Attrib)	7,831	6,315	11,504	13,391	13,617	16,166	-42%	-54%	-29%

Source: Company, Axis Securities

## Results Review

		Q3FY22	Q2FY23	Q3FY23	Q3FY23	Q3FY23	YoY(%)	QoQ(%)	vs Axis Est	vs Consensus
		Actual	Actual	Axis Est	Consensus	Actual	%	%	%	%
Total Revenue from Operations	Rs Cr	60,783	59,878	51,737	56,690	57,084	-6%	-5%	10%	1%
<b>Total Segment EBITDA</b>	<b>Rs Cr</b>	<b>15,853</b>	<b>6,271</b>	<b>5,692</b>	<b>5,959</b>	<b>4,156</b>	<b>-74%</b>	<b>-34%</b>	<b>-27%</b>	<b>-30%</b>
<b>Adj EBITDA per tonne</b>	<b>Rs/tonne</b>	<b>22,663</b>	<b>8,045</b>	<b>7,853</b>		<b>3,812</b>	<b>-83%</b>	<b>-53%</b>	<b>-51%</b>	NA
EBITDA margin (%)	%	26.1%	10.5%	11.0%	10.5%	7.3%				
<b>Underlying PAT</b>	<b>Rs Cr</b>	<b>9,242</b>	<b>1,438</b>			<b>(332)</b>	<b>NA</b>	<b>NA</b>	<b>NA</b>	<b>NA</b>
Reported PAT (Attrib)	Rs Cr	9,573	1,514	1,279	1,699	(2,224)	NA	NA	NA	NA
Diluted EPS (Rs)	Rs/sh	7.91	1.24	1.05		(1.82)	NA	NA	NA	NA
Net Debt	Rs Cr	62,869	71,753			71,706	14%	0%	NA	NA

Source: Company, Axis Securities, Bloomberg Consensus

		Q3FY22	Q2FY23	Q3FY23	YoY(%)	QoQ(%)
<b>Segmental EBITDA</b>		Actual	Actual	Actual	%	%
Tata Steel India	Rs Cr	12,167	5,135	5,334	-56%	4%
Tata Steel Long Products	Rs Cr	255	(229)	(352)	NA	NA
Other Indian operations	Rs Cr	429	100	116	-73%	17%
Tata Steel Europe	Rs Cr	2,942	1,788	(1,551)	NA	NA
Other trade-related operations	Rs Cr	(10)	(477)	877	NA	NA
SE Asian operations	Rs Cr	230	109	(2)	NA	NA
Rest of the world	Rs Cr	(325)	(59)	(256)	NA	NA
<b>Total</b>	<b>Rs Cr</b>	<b>15,690</b>	<b>6,366</b>	<b>4,167</b>	<b>-73%</b>	<b>-35%</b>
Less: intersegment eliminations	Rs Cr	(163)	95	13	NA	-86%
<b>Total segment EBITDA</b>	<b>Rs Cr</b>	<b>15,853</b>	<b>6,271</b>	<b>4,154</b>	<b>-74%</b>	<b>-34%</b>

		Q3FY22	Q2FY23	Q3FY23	Q3FY23	YoY(%)	QoQ(%)	vs Axis Est
<b>Production volume:</b>		Actual	Actual	Axis Est	Actual	%	%	%
Tata Steel India	Mnt	4.81	4.86	5.00	5.05	5%	4%	1%
Tata Steel Europe	Mnt	2.57	2.40	2.25	2.24	-13%	-7%	0%
Tata Steel Thailand	Mnt	0.38	0.30	0.27	0.27	-29%	-10%	0%
<b>Total Consolidated</b>	<b>Mnt</b>	<b>7.76</b>	<b>7.56</b>	<b>7.52</b>	<b>7.56</b>	<b>-3%</b>	<b>0%</b>	<b>1%</b>
<b>Delivery volumes:</b>								
Tata Steel India	Mnt	4.41	5.06	4.73	4.87	10%	-4%	3%
Tata Steel Europe	Mnt	2.16	1.87	1.96	1.99	-8%	6%	2%
Tata Steel Thailand	Mnt	0.39	0.30	0.29	0.29	-26%	-3%	0%
<b>Total Consolidated</b>	<b>Mnt</b>	<b>6.96</b>	<b>7.23</b>	<b>6.98</b>	<b>7.15</b>	<b>3%</b>	<b>-1%</b>	<b>2%</b>

Source: Company, Axis Securities

## Financials (Consolidated)

### Profit & Loss

(Rs Cr)

Y/E March	FY 22A	FY 23E	FY 24E	FY 25E
Total Operating income	2,43,959	2,38,744	2,40,484	2,42,784
Total Expenditure	1,80,469	2,08,592	2,16,721	2,10,513
<b>EBITDA</b>	<b>63,490</b>	<b>30,151</b>	<b>23,763</b>	<b>32,271</b>
Depreciation and Amortization	9,101	9,321	10,379	10,984
<b>EBIT</b>	<b>54,389</b>	<b>20,830</b>	<b>13,385</b>	<b>21,287</b>
Other Income	785	1,145	1,202	1,262
Share Of P/L Of Associates (Net of Tax)	649	398	418	438
Less: Interest & Fin Chg.	5,462	6,243	5,289	5,289
Less: Exceptional Items	134	(102)	-	-
<b>Profit before tax</b>	<b>50,227</b>	<b>16,231</b>	<b>9,715</b>	<b>17,698</b>
Provision for Tax	8,478	8,946	3,400	6,194
<b>Reported PAT</b>	<b>41,749</b>	<b>7,285</b>	<b>6,315</b>	<b>11,504</b>
Minority Interest	1,595	(546)	-	-
<b>Attributable PAT</b>	<b>40,154</b>	<b>7,831</b>	<b>6,315</b>	<b>11,504</b>
<b>EPS (Rs/sh) Basic</b>	<b>332.4</b>	<b>6.8</b>	<b>5.5</b>	<b>9.8</b>
<b>DPS (Rs/sh)</b>	<b>51.0</b>	<b>2.5</b>	<b>2.5</b>	<b>2.5</b>

Source: Company, Axis Securities

### Balance Sheet

(Rs Cr)

Y/E March	FY 22A	FY 23E	FY 24E	FY 25E
Net Block	1,16,166	1,28,162	1,30,534	1,32,300
Other Tangible assets	8,338	8,338	8,338	8,338
CWIP + ITUD + Other Intangible Assets	26,518	28,430	30,680	32,930
Goodwill	4,311	4,527	4,753	4,991
Investments	13,140	13,649	14,183	14,744
Inventories	48,824	47,781	48,129	48,589
Trade Receivables	12,246	11,985	12,072	12,187
Cash / Bank balance	15,605	6,510	5,082	9,445
Retirement Benefit Assets	20,399	20,807	21,223	21,648
Misc. Assets	19,898	20,667	21,472	22,316
<b>Total assets</b>	<b>2,85,446</b>	<b>2,90,854</b>	<b>2,96,467</b>	<b>3,07,488</b>
Equity capital	1,221	1,221	1,221	1,221
Hybrid Perpetual Securities/ Share warrants	-	-	-	-
Reserves	1,13,222	1,18,000	1,21,261	1,29,712
Minority Interests	2,655	2,109	2,109	2,109
Total Borrowings	68,829	68,829	68,829	68,829
Def Tax Liabilities	12,326	12,326	12,326	12,326
Retirement Benefit Obligations	3,572	3,751	3,938	4,135
Provisions	7,594	7,974	8,373	8,792
Trade Payables	36,765	35,979	36,241	36,588
Other Liabilities and Provision	39,261	40,666	42,168	43,777
<b>Capital employed</b>	<b>2,85,446</b>	<b>2,90,854</b>	<b>2,96,467</b>	<b>3,07,488</b>

Source: Company, Axis Securities

**Cash Flow**

(Rs Cr)

Y/E March	FY 22A	FY 23E	FY 24E	FY 25E
Profit before tax	50,227	16,777	9,715	17,698
Depreciation	9,101	9,321	10,379	10,984
Interest Expenses	5,462	6,243	5,289	5,289
Non-operating / EO item	1,110	(600)	(618)	(636)
Change in W/C	(9,618)	1,727	1,124	1,166
Income Tax	(11,902)	(8,946)	(3,400)	(6,194)
<b>Operating Cash Flow</b>	<b>44,381</b>	<b>24,522</b>	<b>22,489</b>	<b>28,306</b>
Capital Expenditure	(10,522)	(12,746)	(15,000)	(15,000)
<b>Free cash Flow</b>	<b>33,859</b>	<b>11,776</b>	<b>7,489</b>	<b>13,306</b>
Other Investments	(359)	(11,207)	(761)	(799)
<b>Investing Cash Flow</b>	<b>(10,881)</b>	<b>(23,953)</b>	<b>(15,761)</b>	<b>(15,799)</b>
Proceeds from the issue of Equity shares	326	(546)	-	-
Proceeds / (Repayment) of Borrowings	(15,231)	-	-	-
Finance cost paid	(4,687)	(6,243)	(5,289)	(5,289)
Dividend paid	(3,020)	(3,053)	(3,053)	(3,053)
Other Financing activities	(789)	179	188	197
<b>Financing Cash Flow</b>	<b>(23,401)</b>	<b>(9,664)</b>	<b>(8,155)</b>	<b>(8,145)</b>
Change in Cash	10,099	(9,095)	(1,427)	4,362
Opening Cash	5,532	15,605	6,510	5,082
<b>Closing Cash</b>	<b>15,607</b>	<b>6,510</b>	<b>5,082</b>	<b>9,445</b>

Source: Company, Axis Securities

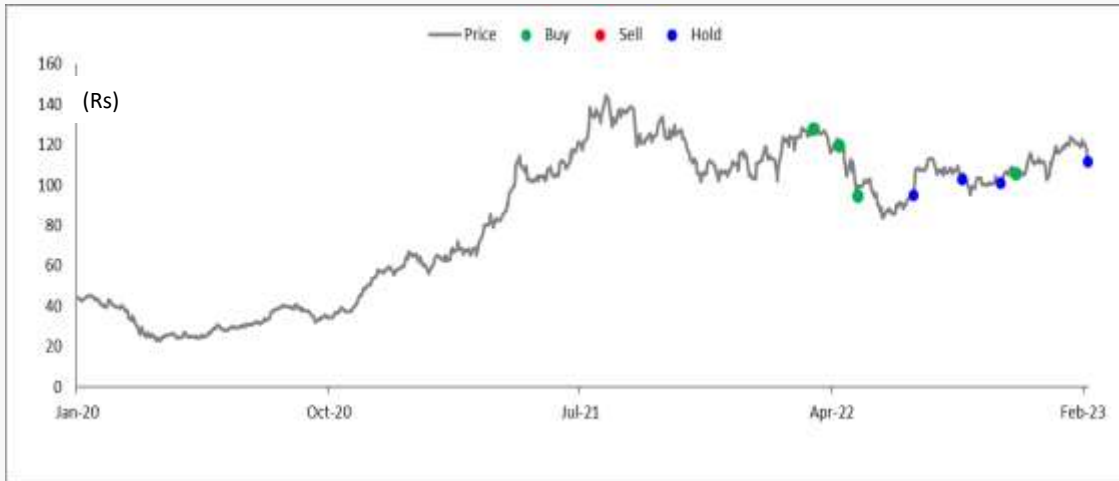
**Ratio Analysis**

(%)

Y/E March	FY 22A	FY 23E	FY 24E	FY 25E
<b>Operational Ratios</b>				
Sales growth (% YoY)	56%	-2%	1%	1%
EBITDA growth (% YoY)	108%	-53%	-21%	36%
Op. profit growth (% YoY)	156%	-62%	-36%	59%
Net Profit growth (% YoY)	436%	-80%	-19%	82%
EBITDA Margin %	26%	13%	10%	13%
Net profit Margin %	16%	3%	3%	5%
EBITDA/t (Rs/tonne)	0%	0%	0%	0%
Tax Rate %	17%	55%	35%	35%
<b>Efficiency Ratios</b>				
Total Asset Turnover (x)	0.92	0.83	0.82	0.80
Sales/Gross block (x)	1.27	1.18	1.10	1.05
Sales/Net block(x)	2.07	1.95	1.86	1.85
Working capital/Sales (x)	0.10	0.10	0.10	0.10
<b>Valuation Ratios</b>				
PER (x)	4.0x	16.5x	20.2x	11.4x
P/BV (x)	1.4x	1.1x	1.1x	1.0x
EV/Ebitda (x)	3.4x	6.6x	8.4x	6.0x
EV/Sales (x)	0.9x	0.8x	0.8x	0.8x
Dividend Yield (%)	3.9%	2.2%	2.2%	2.2%
<b>Return Ratios</b>				
ROE	0.41	0.06	0.05	0.09
ROCE	0.29	0.11	0.07	0.10
ROIC	0.27	0.08	0.05	0.07
<b>Leverage Ratios</b>				
Debt / equity (x)	0.66	0.63	0.62	0.58
Net debt/ Equity (x)	0.53	0.50	0.49	0.43
Net debt/Ebitda (x)	0.80	1.98	2.56	1.73
Interest Coverage ratio (x)	11.62	4.83	4.49	6.10

Source: Company, Axis Securities

## Tata Steel Price Chart and Recommendation History



Source: Axis Securities

Date	Reco	TP	Research
05-Apr-22	BUY	170	Initiating Coverage
04-May-22	BUY	170	Result Update
25-May-22	BUY	139	Sector Update
26-Jul-22	HOLD	104	Result Update
19-Sep-22	HOLD	115	Sector Update
01-Nov-22	HOLD	110	Result Update
21-Nov-22	BUY	117	Sector Update
08-Feb-23	HOLD	120	Result Update

Source: Axis Securities

**About the analyst**

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Sector: Metals & Mining

Analyst Bio: Aditya Welekar is PGDBM in Finance with 12 years of experience in Equity Market/Research.

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DEFINITION OF RATINGS	
Ratings	Expected absolute returns over 12-18 months
<b>BUY</b>	More than 10%
<b>HOLD</b>	Between 10% and -10%
<b>SELL</b>	Less than -10%
<b>NOT RATED</b>	We have forward looking estimates for the stock but we refrain from assigning valuation and recommendation
<b>UNDER REVIEW</b>	We will revisit our recommendation, valuation and estimates on the stock following recent events
<b>NO STANCE</b>	We do not have any forward looking estimates, valuation or recommendation for the stock

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