

SELL

Price	Rs410
Target Price	Rs287
Investment Period	12 months

Stock Info

Sector	Steel
Market Cap (Rs cr)	7,670
Beta	1.3
52 WK High / Low	1,203/170
Avg Daily Volume	395935
Face Value (Rs)	10
BSE Sensex	11,876
Nifty	3,621
BSE Code	500228
NSE Code	JSWSTEEL
Reuters Code	JSTL.BO
Bloomberg Code	JSTL@IN

Shareholding Pattern (%)

Promoters	45.0
MF/Banks/Indian FIs	10.0
FII/ NRIs/ OCBs	35.2
Indian Public/others	9.8

Abs.	3m	1yr	3yr
Sensex (%)	27.7	(30.5)	(4.7)
JSW Steel (%)	94.8	(53.6)	18.9

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Performance Highlights

- Topline lower on lower Steel prices:** For 4QFY2009, JSW Steel posted a decline of 7.4% yoy in its Standalone Topline to Rs3,275cr (Rs3,537cr) mainly on account of the decline in average Steel realisations led by the fall in Steel prices during the quarter. Average Sales realizations fell by 12% yoy and 21% qoq to Rs30,838 during the quarter. However, the company's Sales volumes increased marginally by 5.3% yoy to 1.06mn tonnes (1.0mn tonnes). For FY2009, Revenues increased by 22.6% to Rs14,001cr (Rs11,420cr) on account of strong Steel prices during 1HFY2009. Average Steel realisation during FY2009 increased by 22% to Rs40,844/tonne (Rs33,539/tonne). However, the Sales Volumes were almost flat at 3.43mn tonnes (3.41mn tonnes) during the year. The slowdown in Steel demand led by the slowdown in overall economic activities impacted the company's offtake.
- EBIDTA/tonne declined sharply:** JSW Steel reported a sharp decline in EBIDTA Margins by 1,520bp yoy to 10.8% (26.0%) during the quarter mainly on account of high coking coal costs and lower realisation. This was despite the company re-negotiated its coal contract at the lower prices. High cost inventory of the previous quarter also impacted Margins. EBIDTA/tonne during the quarter fell sharply to Rs3,318 (US \$67) due to the increase in production cost by US \$31/tonne and decline in Steel realisation by US \$85 yoy. For FY2009, Standalone EBIDTA Margin stood at 20.2% (29.4%).
- Net Profit disappoints...losses on consolidated entity:** Even though Topline declined marginally during the quarter, JSW reported a substantial decline of 90% yoy in its Standalone Net Profit to Rs49.2cr (Rs370.2cr) mainly due to Margin erosion and higher leverage. On a Consolidated basis, in fact, JSW reported a Loss of Rs40cr (Rs357cr) due to the dismal performance by its Plate and Pipe mill Division on account of poor demand and inventory write downs of US \$58.4mn. Higher Interest (59.6% yoy) and Depreciation (24.4% yoy) during the quarter also impacted Bottomline. For FY2009, Net Profit declined 74% to Rs458.5cr (Rs1,728cr).

Key Financials (Consolidated)

Y/E March (Rs cr)	FY2008	FY2009	FY2010E	FY2011E
Net Sales	12,457	15,935	16,783	19,645
% chg	45.6	27.9	5.3	17.0
Adj. Net Profit	1,640	887	956	1,210
% chg	25.8	(45.9)	7.9	26.5
OPM (%)	27.9	18.7	20.9	21.3
Adj. EPS (Rs)	89.3	41.5	48.1	60.9
P/E (x)	4.6	9.9	8.5	6.7
P/BV (x)	1.0	1.0	0.9	0.8
RoE (%)	23.0	12.5	10.5	12.1
RoCE (%)	13.3	9.5	8.5	9.2
EV/Sales (x)	1.5	1.4	1.4	1.3
EV/EBITDA	5.5	7.3	6.8	6.1

Source: Company, Angel Research

Management Guidance appears optimistic

Management has guided Steel Volume growth of 78% to 6.1mn tonnes in FY2010. JSW plants to achieve this Volume growth by penetration into the rural and semi urban area and setting up retail stores through its new initiative, JSW Shoppe. The company also targets to wrest marketshare from the small and high-cost manufacturers.

We however believe that the Volume guidance given by management is quite optimistic in view of the slowdown in Steel demand globally as well as India. Steel demand globally is expected to decline by 10% in 2009 while India would manage to grow by 5-6% in line with the GDP growth, which is however lower than the growth rate of 10-12% over the last couple of years. Also, other players like Tata Steel, SAIL, Essar and Ispat have embarked on capacity expansions, which would enhance competition in the domestic market. Hence, we have factored in 50% growth in Saleable Steel Volumes to 5.14mn tonnes in FY2010.

Re-negotiation in Coking coal, Iron ore to save costs; fall in realisations to offset it

Worldwide negotiations for contract coking coal and Iron ore are currently progressing. The talks signal reduction of 30-40% and around 50% in the iron ore and coking coal, respectively. The fall in these steel making inputs would help non-integrated companies like JSW Steel to save on costs and improve Margins going forward. However, the steep fall in the Steel prices, which are currently hovering at US \$400-425/tonne, would offset the savings in Raw materials costs to some extent.

Outlook and Valuation

After the steep run up in the Steel prices since January 2008, over the last few months prices have collapsed by more than 60% in the global markets and by around 40% in the domestic market owing to the sharp decline in Spot raw material prices and uncertainty over the demand for Steel led by adverse macro-economic factors globally. In perspective, the benchmark World export HRC prices have dipped to US \$450/tonne from a peak of US \$1,113/tonne in July 2008. Consequently, the domestic HRC prices have fallen to Rs27,000/tonne from the peak of Rs48,000/tonne during July-August 2008.

Following the recovery in Steel demand in India, robust guidance given by management and the company's aggressive Marketing strategies, we upgrade our FY2010 Volume estimate by 18% to 5.14mn tonnes from 4.34mn tonnes earlier. We are simultaneously pruning our steel price estimates by 13.6% for FY2010 due to the continued weakness in the Steel prices. Consequently, we upgrade our FY2010 EPS estimate by 13.3% to Rs48.1. At the CMP of Rs410, JSW Steel is trading at a P/B of 0.9x and EV/EBIDTA of 6.8x FY2010E consolidated Earnings, which is expensive. Even at the optimistic 78% volume growth guided by the management, we believe that stock is fully priced at the current levels. **Hence, we recommend Sell on JSW Steel with a Target Price of Rs287, at which level it would trade at an EV/EBIDTA of 6x , P/B of 0.6x and P/E of 5.6x FY2010E consolidated Earnings.**

Exhibit 1: What-if-analysis (FY2010 estimates, Consolidated)

	Lower than Base Case	Base Case	JSW Steel estimates
Sales Volumes growth yoy (%)	30	50	78
Revenues (Rs cr)	14,685	16,783	18,092
EBIDTA (Rs cr)	3,047	3,501	3,972
EBDITA Margins (%)	20.7	20.9	22.0
EPS (Rs)	31.4	48.1	65.4
Target Price (Rs)	140	287	423

Exhibit 2: 4QFY2009 Performance (Standalone)

Y/E March (Rs cr)	4QFY2009	4QFY2008	% chg	FY2009	FY2008	% chg
Net Sales	3,275	3,537	(7.4)	14,001	11,420	22.6
Raw Materials	2,283	1,963	16.3	8,450	5,694	48.4
(% of Net Sales)	69.7	55.5		60.4	49.9	
Power & Fuel	179.8	149.1	20.6	673.1	539.2	24.8
(% of Net Sales)	5.5	4.2		4.8	4.7	
Staff Costs	62.5	73.3	(14.7)	288.8	274.0	5.4
(% of Net Sales)	1.9	2.1		2.1	2.4	
Other Expenditure	397.2	433.8	(8.4)	1,756	1,558	12.7
(% of Net Sales)	12.1	12.3		12.5	13.6	
Total Expenditure	2,923	2,619	11.6	11,168	8,065	38.5
Operating Profit	352	918	(61.6)	2,833	3,355	(15.5)
OPM (%)	10.8	26.0		20.2	29.4	
Interest	214.9	134.7	59.6	797.3	440.4	-
Depreciation	230.9	185.6	24.4	827.7	687.2	20.4
Other Income	151.1	33.2	355.7	259.6	152.3	70.5
Exceptional Items	17.8	(98.9)		(790.1)	104.9	
Profit before Tax	75.5	532	(85.8)	678	2,484	(72.7)
(% of Net Sales)	2.3	15.0		4.8	21.8	
Current Tax	26.3	161.9	(83.7)	219.1	755.9	(71.0)
(% of PBT)	34.9	30.4		32.3	30.4	
Profit After Tax	49.2	370.2	(86.7)	458.5	1,728	(73.5)
(% of Net Sales)	1.5	10.5		3.3	15.1	
FDEPS (Rs)	2.1	20.2	(89.4)	22.7	94.2	(75.9)

Source: Company, Angel Research



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Ratings (Returns) : Buy (Upside > 15%)
Reduce (Downside upto 15%)

Accumulate (Upside upto 15%)
Sell (Downside > 15%)

Neutral (5 to -5%)