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Q1FY22 results review and earnings revision

Metals

Target price Rs99

Earnings Revision

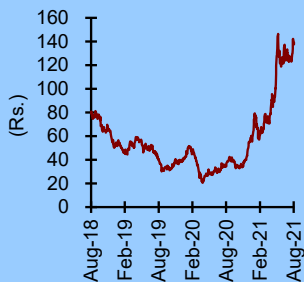
(%)	FY22E	FY23E
Sales	↓ 9.8	↓ 4.5
EBITDA	↓ 20.7	↓ 18.0
PAT	↓ 25.9	↓ 25.7

Shareholding pattern

	Dec '20	Mar '21	Jun '21
Promoters	75.0	65.0	65.0
Institutional investors	17.1	21.0	20.6
MFs and others	1.5	5.7	5.6
Banks & FIs	0.4	0.3	0.1
Insurance Cos.	11.1	10.6	9.8
FIs	4.1	4.4	5.1
Others	7.9	14.0	14.4

Source: NSE

Price chart



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INDIA

Steel Authority of India

SELL
Maintain
Rs141

Headwinds pile up

Steel Authority of India (SAIL) reported inline EBITDA at Rs65.8bn; on the back of lower than expected volumes. The investment thesis continues to face the dual headwinds of i) higher employee costs and ii) possibility of higher capex. Management has announced Rs650bn of capex to increase capacity by 13mnte across three plants. Coupled with peak spreads and most of the deleveraging expectations in the price, the investment thesis looks clouded. The pace of deleveraging, given capex programs will take time to ramp-up, limits downside risks to an extent, unlike past cycles. We maintain SELL with an unchanged target of Rs 99/share.

- ▶ **Dual headwinds of higher employee costs and higher capex, at peak spreads.** Employee wage revisions are due, and ~Rs14bn has been provided on an estimated basis till Q1FY22 (provided for past five quarters). Higher profits will bring in the headwind of higher employee costs. Management announced ~13mnte of new expansion across Burnpur, Bokaro and Rourkela for a total capex of Rs650bn. Expansion capex will witness a pickup from FY24; management suggested a possibility of preponing the expansion capex as well. Target capex (as directed by GoI) is Rs80bn for FY22E, management guided to achieve Rs60bn capex in FY22E.
- ▶ **Significant reduction in Net debt; difficult to sustain the trajectory.** Net Debt (ex of capital advances) has reduced by ~ Rs 50bn to ~Rs300bn in Q1FY22. If a controlled capex trajectory is followed, SAIL has the option to reduce Net Debt to EBITDA to 0.7x and 0.37x by FY22/23E. The significant deleveraging prospects can only materialise and benefits maintained if capital discipline is witnessed.
- ▶ **Maintain SELL with a target of Rs99/share (unchanged):** Notwithstanding the present earnings scenario, we continue to ascribe ~ 0.6x P/B to FY23E. We have started witnessing earnings downgrade across the sector; our FY22/23E EBITDA reduces by 20/25% on the back of i) weaker volumes in FY22E and ii) start of a steel price correction cycle (also iron ore has corrected ~US\$40/te in a couple of weeks, coking coal has doubled in the past month).
- ▶ **Upside and downside risks.** Its still not clear, whether royalty incidence on sale of captive iron ore can allow the same level of profitability as was previously anticipated. Steel sales volume is expected to touch 16mnte in FY22E (ticked down from previous expectations). Also, higher long product mix in Bhilai, Durgapur and IISCO may lead to underperformance of margins (due to diverging prices of flats and longs) in the medium term.

Market Cap	Rs582bn/US\$7.9bn
Reuters/Bloomberg	SAIL.BO/SAIL IN
Shares Outstanding (mn)	4,130.5
52-week Range (Rs)	146/33
Free Float (%)	35.0
FII (%)	5.1
Daily Volume (US\$/'000)	110,117
Absolute Return 3m (%)	5.5
Absolute Return 12m (%)	281.3
Sensex Return 3m (%)	11.6
Sensex Return 12m (%)	44.3

Year to March	FY20	FY21	FY22E	FY23E
Revenue (Rs mn)	616,642	692,164	908,428	890,947
Net Income (Rs mn)	(21,792)	40,297	155,567	99,279
EPS (Rs)	(5)	10	38	24
% Chg YoY	(42)	(285)	286	(36)
P/E (x)	(27)	14	4	6
CEPS (Rs)	4	20	49	36
EV/E (x)	23	7	3	4
Dividend Yield (%)	-	2	4	1
RoCE (%)	2	10	26	16
RoE (%)	(6)	8	27	15

Please refer to important disclosures at the end of this report

Table 1: Q1FY22 result review*(Rs mn, year ending March31)*

	Q1FY22	Q1FY21	YoY chg (%)	Q4FY21	QoQ chg (%)
Net sales	206,430	90,675	127.7	232,849	(11.3)
Other Income	1,117	2,787		2,483	
Net sales ex other income	206,430	90,675	127.7	232,849	(11.3)
Expenses					
Inc/Dec in stock	(7,852)	(2,713)		6,483	
Raw material consumed	63,743	43,783	45.6	65,170	(2.2)
Staff	27,728	19,968	38.9	40,742	(31.9)
Power & fuel	-	15,627		16,135	
Other expenditure	57,130	34,215	67.0	58,915	(3.0)
Total expenditure	140,748	95,253	47.8	171,310	(17.8)
EBITDA	65,682	(4,578)	NM	61,539	6.7
<i>Margins (%)</i>	<i>31.8</i>	<i>(5.0)</i>		<i>26.4</i>	
Other income	1,117	2,787	(59.9)	2,483	(55.0)
Interest	5,030	8,863	(43.2)	5,404	(6.9)
Depreciation	10,263	9,735	5.4	11,579	(11.4)
Operational PBT	51,507	(20,389)		47,039	
Exceptional items	-	600		(1,664)	
PBT	51,507	(19,789)	NM	45,375	13.5
Taxes	13,149	(7,038)		11,911	
Reported PAT	38,974	(12,265)	NM	34,699	12.3
Adj PAT	38,974	(12,865)	NM	36,363	
Sales volume (mn te)	3.3	2.2	48.7	4.4	(23.5)
Realisation (Rs/te)	62,047	40,534	53.1	53,528	15.9
Raw material cost (Rs/te)	16,799	18,359	(8.5)	16,472	2.0
Total cost (Rs/te)	42,305	42,581	(0.6)	39,382	7.4
Margin (Rs/te)	19,742	(2,047)	NM	14,147	39.6

Source: Company data, I-Sec research

Key concall takeaways

- Q1FY22 production has been low. This allowed SAIL to convert semis into finished products allowing for a surprise in realisations. **Sales target for FY22 is 16.5mn te.**
- Railway receivables stand at Rs71bn. SAIL has received cashflow from Indian Railways in Q1FY22 which allowed the deleveraging of Rs50bn. Also capex incurred in Q1FY22 is Rs7.47bn.
- SAIL has booked 1.12mn of iron ore through auction in Q1FY22. This includes of 0.7mn te of fresh and 0.5mn te of subgrade iron ore. Fresh mined ore fetched Rs7600-9500/te while dumps and subgrade fetched much lower. Sales of iron ore for the quarter stood at 860,000te, at a turnover of Rs4.53bn.

Change in earnings and valuations

We have changed our earnings to adjust for lower volumes in FY22E (16mnte from 17mnte previously) and incrementally lower steel prices. Also iron ore sales are turning out to be much lower than initially expected/guided.

Table 2: Change in earnings

(Rs mn)	FY22E			FY23E		
	New	Old	% chg.	New	Old	% chg.
Sales	908,428	1,007,366	(9.8)	890,947	932,572	(4.5)
EBITDA	268,323	338,305	(20.7)	189,281	230,906	(18.0)
Adj. PAT	155,567	210,004	(25.9)	99,279	133,667	(25.7)

Source: I-Sec research

We maintain **SELL** rating with a price target of Rs99/share (unchanged). We value the company at 0.6xP/B (unchanged) based on FY23E.

Key upside and downside risks

Key downside risks are i) Cycle corrects itself ii) Higher organic capex announcement. Key upside risks are i) Higher iron ore sales to continue fetching additional EBITDA ii) better than expected deleveraging over FY21-23E.

Financial summary

Table 3: Earning statement

(Rs mn, year ending March 31)

	FY20	FY21	FY22E	FY23E
Operating Income (Sales)	616,642	692,164	908,428	890,947
Operating Expenses	565,201	565,377	640,105	701,666
EBITDA	51,441	126,787	268,323	189,281
% margins	8.3	18.3	29.5	21.2
Depreciation & Amortization	37,557	41,028	46,692	47,901
Gross Interest	34,868	28,172	21,008	15,808
Other Income	9,058	8,607	6,800	6,800
Recurring PBT	(11,926)	66,195	207,423	132,372
Add: Extra ordinaries	42,999	1,184	-	-
Less: Taxes	11,809	30,575	51,856	33,093
Less: Minority Interest	(1,943)	(4,677)	-	-
Net Income (Reported)	21,207	41,481	155,567	99,279
Recurring Net Income	(21,792)	40,297	155,567	99,279

Source: Company data, I-Sec research

Table 4: Balance sheet

(Rs mn, year ending March 31)

	FY20	FY21	FY22E	FY23E
Assets				
Total Current Assets	438,775	393,048	466,960	482,123
of which cash & cash eqv.	4,450	7,964	5,017	1,118
Current Liabilities	265,295	351,852	368,280	403,698
Net Current Assets	173,480	41,196	98,680	78,425
Investments	32,404	34,423	34,423	34,423
Strategic/Group	31,073	32,976	32,976	32,976
Other Marketable	1,331	1,447	1,447	1,447
Net Fixed Assets	755,825	744,446	767,745	799,845
Capital Work-in-Progress	87,533	88,806	96,867	145,876
Total Assets	983,760	840,606	921,390	933,234
Liabilities				
Borrowings	588,879	373,203	323,203	243,203
Deferred Tax Liability / (Asset)	(20,222)	13,341	13,341	13,341
Minority Interest	0	0	0	0
Equity Share Capital	41,305	41,305	41,305	41,305
Face Value per share (Rs)	10	10	10	10
Reserves & Surplus	373,797	412,757	543,541	635,385
Net Worth	415,102	454,062	584,846	676,690
Total Liabilities	983,760	840,606	921,390	933,234

Source: Company data, I-Sec research

Table 5: Cashflow statement

(Rs mn, year ending March 31)

	FY20	FY21	FY22E	FY23E
Operating Cash flow	65,561	105,435	195,459	140,380
Working Capital Changes	(106,582)	100,643	(60,431)	16,357
Capital Commitments	(47,544)	(35,297)	(69,991)	(80,000)
Free Cash flow	(88,565)	170,780	65,037	76,736
Cash flow from Investing Activities	4,938	1,170	6,800	6,800
Issue of Share Capital	-	-	-	-
Buyback of shares	-	-	-	-
Inc (Dec) in Borrowings	89,074	(163,350)	(50,000)	(80,000)
Dividend paid	(2,505)	(4,131)	(24,783)	(7,435)
Extraordinary Items	-	-	-	-
Chg. in Cash	1,250	3,277	(2,942)	(3,894)

Source: Company data, I-Sec research

Table 6: Key ratios

(Rs mn, year ending March 31)

	FY20	FY21	FY22E	FY23E
Per Share Data (Rs)				
EPS(Basic Recurring)	(5.3)	10	38	24
Diluted Recurring EPS	(5.3)	10	38	24
Recurring Cash EPS	3.8	20	49	36
Dividend per share (DPS)	-	3	6	2
Book Value per share (BV)	101	110	142	164
Growth Ratios (%)				
Operating Income	(8)	12	31	(2)
EBITDA	39	146	112	(29)
Recurring Net Income	(33)	(250)	337	(36)
Diluted Recurring EPS	(42)	(285)	286	(36)
Diluted Recurring CEPS	(512)	416	149	(27)
Valuation Ratios (x)				
P/E	NM	14.3	3.7	5.8
P/CEPS	37	7	3	4
P/BV	1	1.3	1.0	0.9
EV / EBITDA	23	7.4	3.3	4.3
EV / Operating Income	2	1	1	1
EV / Operating FCF	NM	5	7	5
Operating Ratios (%)				
Raw Material/Sales	48	39	35	39
Other Income / PBT	(76)	13	3	5
Effective Tax Rate	38	45	25	25
NWC / Total Assets	17	4	10	8
Inventory Turnover (days)	565	286	216	284
Receivables (days)	53	38	38	38
Payables (days)	629	513	334	441
D/E Ratio (x)	1	1	1	0
Profitability Ratios (%)				
Rec.Net Income Margins	(4)	5	17	11
RoCE	2	10	26	16
RoNW	(5.7)	7.8	26.6	14.7
Dividend Payout Ratio	-	29	16	7
Dividend Yield	-	2	4	1
EBITDA Margins	8	18	30	21

Source: Company data, I-Sec research

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