

# India Steel

Preeti Dubey  
(91 22) 6628 2417

Materials/Metals & Mining

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SO WHAT? THE BNP PARIBAS ANGLE

INDUSTRY OUTLOOK: ← →

- We have the lowest steel price assumption with HRC at USD750/tonne and billets at USD600/tonne.
- We have built in 10% decline in coking coal prices in FY10.
- We have the lowest TP on the Street.

## Stock Picks

Company	BBG code	Rec	Share price (INR)	Target price (INR)	Upside (%)	Mkt cap (USD m)	Rec P/E		
							2008A (x)	2009E (x)	2010E (x)
Tata Steel	TATA IN	HOLD	393.00	370.00	(5.9)	7212	2.7	2.8	5.3
JSW Steel	JSTL IN	REDUCE	411.05	280.00	(31.9)	1759	4.2	6.3	5.8
SAIL	SAIL IN	REDUCE	114.60	80.00	(30.2)	10076	6.3	7.6	7.1

Source: BNP Paribas estimates

- Downgrading steel sector to NEUTRAL as we expect steel prices to fall upto 15% and profitability to hit 3-year low.
- Reducing EPS estimates by 27%-49% for steel companies on declining price outlook.
- Valuing sector companies at 4.0x-5.0x FY10 EPS; reducing TPs by 54%-75%.

## Steel prices to get worse; Downgrading sector to NEUTRAL

### Downgrading India steel sector to NEUTRAL

Taking forward our view published on September 10, 2008 that steel prices cuts are imminent, we are downgrading India steel sector to NEUTRAL as we see profitability of steel producers to touch three-five year low. We expect steel prices will bottom-out in the next three-six months with HRC reaching USD700/tonne from USD800/tonne and average USD750/tonne (INR33,000) in FY10 (previous estimate: INR35000). We have lowered estimates for companies under coverage to reflect trough pricing.

In India, cheap imports from China and CIS, and inventory liquidation are pressuring steelmakers to cut prices, a scenario we expect will continue in the next three-six months. We expect prices will stabilise and move up after negotiation of annual input contracts expected in April 2009.

Across the board EPS cuts to factor trough pricing  
We are cutting EPS estimates for steel companies by 27%-49%. Key to our estimates is our assumption that coking coal contracts for FY10 will be finalized 10% lower from FY09 level. A rollover of coking coal contracts at current prices will negatively impact EPS by 9%-33% for steel companies. An imposition of import duty on steel will provide upside to our numbers.

### More downside in the near-term

We are reducing our target prices on SAIL from INR165 to INR80, Tata Steel from INR800 to INR370 and JSW Steel from INR1100 to INR280. The steep decline in TPs is due to high sensitivity of EPS to steel prices and lower P/E multiple. We will turn positive as and when we see steel prices stabilising at higher level and inputs costs declining.

Our target prices on steel stocks reflect our trough valuation. Given the recent meltdown in metal stocks, steel stocks are trading close to trough valuation. Among stocks under coverage, JSW and SAIL are more than 15% from our TP while Tata Steel is less than 10% from TP. Therefore, we are downgrading JSW from BUY to REDUCE, SAIL from HOLD to REDUCE, and Tata Steel from BUY to HOLD.

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Preeti Dubey, CFA (91 22) 6628 2417

BNP Paribas Securities India Pvt Ltd  
preeti.dubey@asiabnpparibas.com

Karan Gupta (91 22) 6628 2427

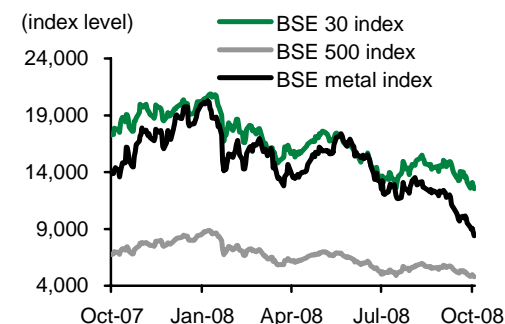
BNP Paribas Securities India Pvt Ltd  
karan.gupta@asiabnpparibas.com

## Revision In Estimates

	JSTL IN (INR)	SAIL IN (INR)	TATA IN (INR)
Previous EPS estimate (FY10)	137.36	22.06	125.20
Revised EPS estimate (FY10)	70.47	16.04	74.52
Previous PE multiple (x)	8.00	7.50	6.50
Revised PE multiple (x)	4.00	5.00	5.00
Previous TP	1,100.00	165.00	800.00
Revised TP	280.00	80.00	370.00
Previous rating	BUY	HOLD	BUY
Revised rating	REDUCE	REDUCE	HOLD

Source: BNP Paribas estimates

## Performance Of The BSE Metal Index



Source: Bloomberg

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