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A Study On Equity Analysis and Valuation of Selected Steel Firms in India

Arihant Bengani

Student, St. Mary's College, Yousufguda, Hyderabad, India

Abstract

The steel is one of the core industries of the economy that has been in a down trend for a couple of year due to less liquidity and profitability and only 6% growth every year. The 2017 steel policy states that the government plans to boost steel production and demand to meet domestic and global needs, these macro-economic factors will overall leave a positive impact on the steel industry which will help it get a justifiable valuation with regard to other sectors and its intrinsic value. The aim of this study is to find out the value, discount and premiums of the steel industry stocks. This Research is an explanatory research that emphasizes on the Future and Growth of the Steel sector taking into consideration the government policies and the financial performances of the major steel corporations.

Keywords: *Liquidity, Profitability, Steel Industry, Valuation, Equity*

Introduction

Steel, Coal, Crude Oil, Natural Gas, Petroleum Products, Fertilizers, Cement And Electricity Generation Are The Core Sectors Of The Economy, Out Of These One Of The Most Undervalued Sector Is The Iron & Steel Sector. India Is The 2nd Largest Producer Of Crude Steel After China. India Produces Around 10 Mt Of Crude Steel Where As China Produces 90 Mt. One Of The Major Indices Of Analyzing The Steel Sector Is The Nifty Metal That Gives Us An Idea About The Prevailing Trend Of Profitability Of The Iron And Steel Industry In The Country. The New Industrial Policy Of The Government Of India Has Liberalized The Steel Sector For Private Investment By Removing It From The Monopoly, Exempting It From Compulsory Licensing Through Automatic Route Import Of Foreign Technology. Also, Foreign Direct Investments Are Permitted Free Up To Certain Limits. The New Steel Policy, 2017 Aims To Achieve 300mt Of Steel Making Capacity By 2030. This Would Translate Into Additional Investment Of Rs. 10 Lakh Crore By 2030- 31. New Steel Policy Seeks To Increase Per Capita Steel Consumption To The Level Of 160 Kgs By 2030 From Existing Level Of Around 60 Kg. This Has Encouraged Private Sector In This Steel Industry To Participate And Grow.

Objectives of The Study

- To understand the importance of the steel industry in economic growth
- To understand valuation of steel industry and are the stocks of the industry trading at a good price
- To understand the profitability and liquidity of the steel industry.

Research Methodology

This Research is an explanatory research that emphasizes on the Future and Growth of the Steel sector taking into consideration the government policies and the financial performances of the major steel corporations. The sample set of this study is the major listed companies of the Steel industry in India. The present study is based on secondary data comprising the financial statements of selected steel firms in India. The data has been collected from annual reports, reports of the steel industry and websites. The data is secondary in nature.

Social Relevance of the Study

- Helps Us Understand Future Prospects Of The Steel Industry
- Helps Derive Rightful Valuations Of The Steel Industry
- Improves The Efficiency Of The Markets.

List Of Selected Companies In The Steel Industry

Table No. 1

Company Name	Last Price As Of 15/7/21	% Change	52 Wk High	52 Wk Low	Market Cap (Rs. Cr)
Jsw Steel	695.80	0.91	773.00	185.65	168,190.20
Tata Steel	1,180.85	1.36	1,246.80	312.25	133,021.53
Hindalco	384.00	2.14	428.30	143.40	86,280.98
Sail	124.50	0.88	151.10	29.20	54,750.11

Via moneycontrol.com

Top Constituents By Weightage Of Nifty Metal

Table No. 2

Company's Name	Weight(%)
Tata Steel Ltd.	24.94
JSW Steel Ltd.	15.85
Hindalco Industries Ltd	15.85
Adani Enterprises Ltd.	8.69
Vedanta Ltd.	8.49

Coal India Ltd	6.68
NMDC Ltd	6.68
Steel Authority Of India Ltd.	4.57
Jindal Steel & Power Ltd	3.92
APL Apollo Tubes Ltd.	2.52

Note- The Sample Size Chosen Constitutes to 61.27% of the Entire Index

Literature Review

Kulshrestha (1980), has made a study on "corporate liquidity". He has found from his study that excessive liquidity would reflect lower profitability and deterioration in managerial efficiency has been exhibited through inappropriate decisions taken in the area of expansion, credit policies, and dividend policies.

Banerjee B (1982), in his study on "corporate liquidity and profitability in India" has identified the relationship of liquidity with profitability by analysing the trend of liquidity position of medium and large public limited companies in India.

Padmaja Manoharan, (2010), in her study "micro finance institutions in india – a study on financial performance", has studied the trend of liquidity and the relationship between liquidity and profitability of 30, listed core manufacturing companies from six industrial groups. the study period is five years from 2003-04 to 2007-08.

Prof. Ketan H.Popat (2012), has conducted" a comparative study of profitability analysis of selected steel industries" the profitability ratios are calculated to measure the operating efficiency of the business enterprise. besides management of the company, creditors and owners are interested in the profitability of the firm. investor wants to get reasonable return on their investments. this is only possible when the company is having satisfactory profit.

P. Rajang am and V. Selvaraj (2013), have attempted to study the financial health of West Coast Paper Mill Limited. The study covers a period a twelve financial years from 2000-01 to 2011-12. The research is fully based upon the secondary data which has been collected from the official directory of Bombay stock exchange, Capitoline plus corporate data base. To evaluate the financial health of a company, the authors

Dr. Mrs.A.Rajamani, Dr.P. Jayasubramanian (2019) , have conducted a study to examine the financial performance of pharmaceutical companies. They have taken two public sector drug and pharmaceutical enterprises which have been listed on BSE. Researchers have undertaken twelve years from 1998-99 to 2009-2010. In this study researchers have used liquidity, solvency, profitability, various accounting ratios and linear multiple regression analysis and the test of hypothesis: t-test. The study has concluded that the liquidity position has been strong and the Indian pharmaceutical industry will witness an increase in the market share.

Data Analysis

Nifty Metal V/S Nifty 50- An Industry Overall Outlook

Figure No. 1

- Nifty Metal – Purple Line
- Nifty 50 – Candle Sticks
- As We Can Clearly See Above Nifty Has Been Underperforming From 2018, Even Though Nifty 50 Was In An Uptrend, Metal Has Continuously Falling Down And Now There Is Been A Significant Move In The Nifty Metal And Hence We Expect The Market Leaders To Outperform.

Formula Used For Valuation

V= EPS*(8.5+2G)*RF/Y - Graham Value

Where V Is The Intrinsic Value, EPS Is The Trailing 12 Month EPS, 8.5 Is The PE Ratio Of A Stock With 0% Growth And G Being The Growth Rate For The Next 7-10 Years. At The Risk Free Interest Rate To Be Adjust To The Present, We Divide This Number By Today's AA Corporate Bond Rate, Represented By Y In The Formula Above

Current Risk Free Rate of Return(RF) is 6.3%

Current AA Corporate Bond Rate (Y) is 10%-11%

Growth Rate Is Taken as Average ROE of 3 Yrs.

Intrinsic Value And Current Market Price

JSW Steel

CMP= 695.80

I.V = 32.73*(8.5+2*19) *6.3/10

=917.54

Since I.V > CMP, The Stock Is Undervalued.

Tata Steel

CMP=1180.85

I.V= 62.60*(8.5+2*9.62)*6.3/10

=1094.01

Since I.V > CMP, The Stock Is Undervalued.

Hindalco

CMP= 384

I.V=15.5*(8.5+2*8)*6.3/10

=239.24

Since I.V CMP, The Stock Is Overvalued.

SAIL

CMP= 124.50

I.V= 8.4*(8.5+2*7.62)*6.3/10

=125.63

Since I.V > CMP, The Stock Is Undervalued.

Intrinsic Value And Current Market Price (Earning capitalization formula)

JSW Steel

CMP= 695.80

I.V = 59.5(1+0.18) / (0.2-0.18)

= 3510

Since I.V > CMP, the Stock Is Undervalued.

Tata Steel

CMP=1180.85

I.V= 62.60(1+.06) / (0.10-0.06)

=1658.9

Since I.V > CMP, the Stock Is Undervalued.

Hindalco

CMP= 384

I.V= 31.1(1+0.07)/ (0.10-0.07)

=1109.23

Since I.V< CMP, the Stock is undervalued.

SAIL

CMP= 124.50

I.V= 22.4(1+.07)/ (0.10-0.07)

= 798.33

Since I.V > CMP, the Stock Is Undervalued.

Findings

- 3 companies out of the 4 we undervalued
- As an index, nifty metal is undervalued but is in a reasonable uptrend currently
- There is an approximate upside of 10-15% in these stocks as well as the overall index
- The contingent liabilities of the firms have significantly improved resulting in higher liquidity and profitability and in turn a positive overall outlook
- The industry has a high liquidity
- The profitability and margins of the companies are improving significantly
- The overall contingent liabilities of the companies have reduced
- The sector is showing better prospects
- There is a bullish sentiment for the industry
- Governments reforms of 2017 are providing support and helping in the improvement and performance upgrades of the industry
- Valuations and market capital of the major companies have significantly improved
- Balance sheet and profit & loss statements are sound and there is scope for further growth