



Executive Summary

MSP Steel & Power Ltd. is an integrated Steel Manufacturer in Eastern India having plant at Raigarh, Chattisgarh. The promoters of the company are Mr. Puran Mal Agrawal and Mr. Suresh Kumar Agrawal. The products of the company include sponge iron, billets, TMT and structurals (angels, channel, flats). The company is undertaking backward integration program to increase its pelletization and power generation capacity.

Concerns

Falling commodity prices particularly steel.

A weaker than expected economic recovery.

MSP Steel & Power Ltd.	BUY
Horizon	12 months
CMP (Rs.)	60
Target Price (Rs.)	78
Upside	30%

Key Investment considerations

Capacity expansion to drive volume.

Improvement in operating margins.

Focus on merchant power.

Traction in steel prices.

Investment Strategy

Period	Cash
Short Term	Buy
Mid Term	Buy
Long Term	Accumulate

Please read our detailed report below for further information, analysis and details of the Greshma CSI Ranking model and the Greshma Risk Return Matrix

Index

1. Investment Rationale	3
2. Valuation	4
3. Company Overview	4
4. SWOT Analysis	5
5. Investment Thesis	6
6. Industry Overview	9
7. Peer Comparison	11
8. Sensitivity Analysis	12
9. Financial Summary	13
10. Football Valuation	16
11. Greshma CSI	17
12. Technical View	18
11. Disclaimer	19

Investment Rationale

Capacity expansion to drive volume

MSP Steel & Power Ltd. is on an expansion spree. It is increasing its sponge iron capacity from 1,92,000 MTPA to 423,000 MTPA by end of CY12. This capacity addition will be done in a phased manner. The increased capacity will drive volume growth for the company.

Table.1: Sales Volumes

Sales (in MT)	FY2009	FY2010
Sponge Iron	33557	55907
M.S. Ingots/Billets	57230	47227
TMT Bars	57026	64811

(Source: Company)

Improvement in operating margins

The company is undertaking backward integration program to increase its pelletization from 3,00,000 MTPA to 9,00,000 MTPA by end of CY12. This will take care of lower grade iron ore (58- grade) and will lead to savings of Rs.2500/ton. Cost reduction will help the company to improve EBITDA margins by about 300 bps.

Focus on merchant power

MSP Steel is expanding its power generation capacity from 24 MW to 76 MW by FY12. Out of this, 36 MW will be used for captive consumption and rest 40 MW will be sold as merchant power. Power contributed 2% of overall revenues in FY10. This share will increase to 7-10% by FY12.

Traction in steel prices

Recovery in global economy has pushed up steel prices. They are expected to increase from \$455 per ton in FY09 to \$625-675 per ton in FY10 and \$675-725 per ton in FY11. Domestic TMT prices increased to Rs.36,000 per ton in April 2010 as compared to Rs.30,000 in April 2009.

BUY

CMP (Rs.)	60
Target price (Rs.)	78
Potential upside	30%
Holding Period	12 Months

Stock Matrix

No. of shares(mn)	58
FV(Rs.)	10
BV	35
Market Cap(Rs. Mn)	3364
52 week high / low(Rs.)	74/33
Beta	0.72
3 months Avg. vol.. (in lacs)	0.13
BSE Code	532650
NSE Code	MSPL

Shareholding Pattern (%)

	Dec - 10	Sep - 10	QoQ % Change
Promoters	71.8	71.8	0
FII	0.33	0.33	0
DII	0.77	0.26	0.51
Others	27.1	27.61	-0.51

Price Trend:



Contact:

research@greshma.com

91-22- 3005 6400

Valuation

Rising infrastructure spending will lead to demand for steel products. MSP Steel & Power Ltd. is into sponge iron, Billets, TMT and Structural. Alongside this, the company is undertaking backward integration which will result in cost reduction and expanding EBITDA margins. We expect FY12 EPS of Rs.13. At 6 times FY12E earnings, we recommend BUY on the script with a price target of Rs.78 for a 12 month investment horizon.

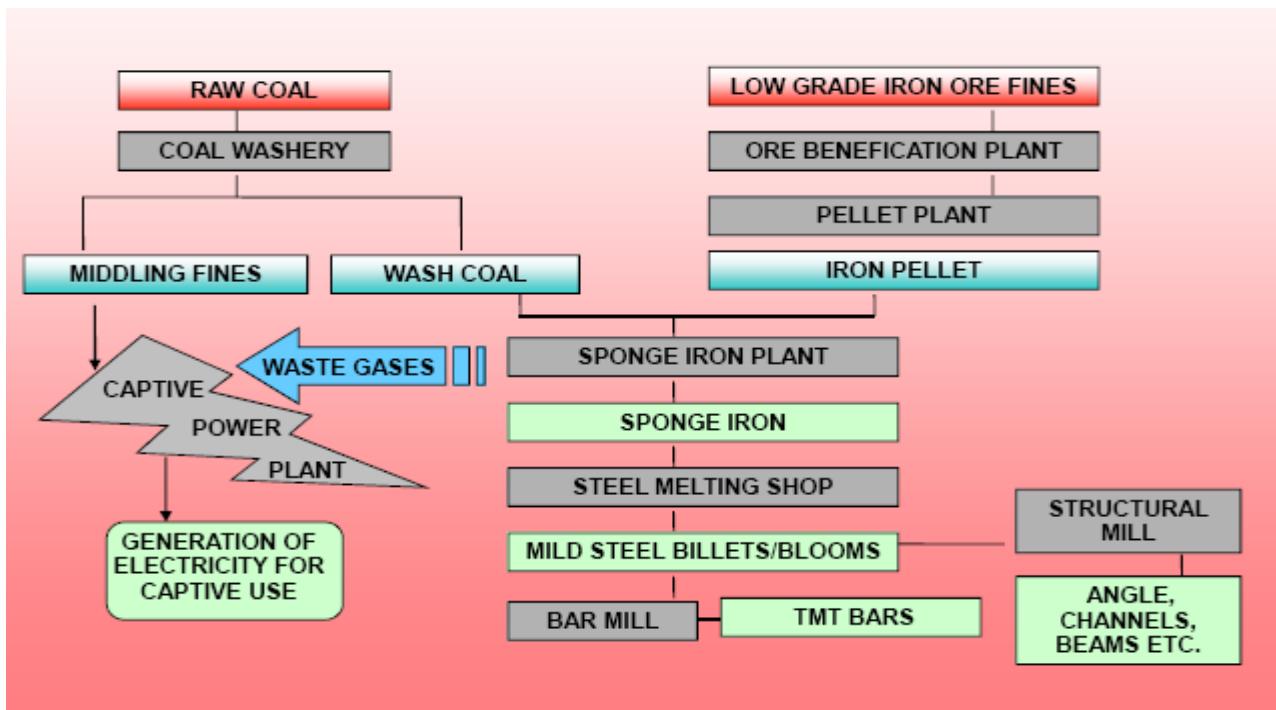
Company Overview

MSP Steel & Power Ltd. is an integrated Steel Manufacturer in Eastern India having plant at Raigarh, Chattisgarh. The promoters of the company are Mr. Puran Mal Agrawal and Mr. Suresh Kumar Agrawal. The products of the company include sponge iron, billets, TMT and structurals (angels, channel, flats). The company is undertaking backward integration program to increase its pelletization and power generation capacity.

Table 2: Existing Facilities.

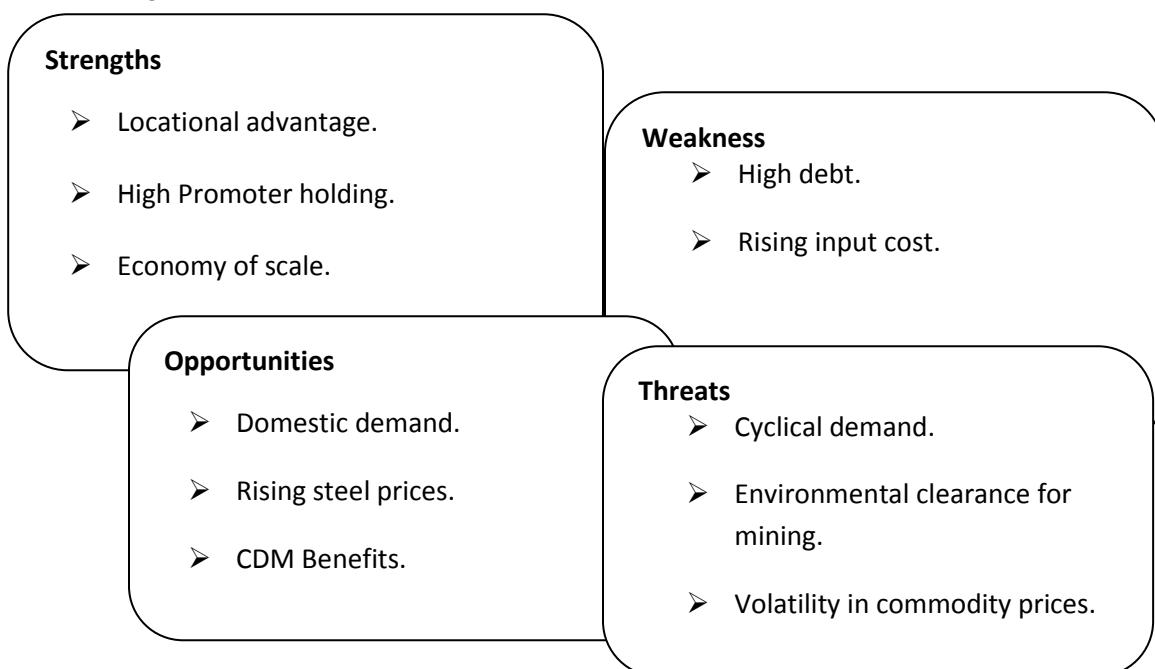
Production Field	Capacity
Iron Ore Pellets	300,000 tpa
Sponge Iron	192,000 tpa
Mild Steel Billets	144,109 tpa
Construction Bars (TMT)	80,000 tpa
Heavy Structural Sections	128,000 tpa
Coal Washery	345,600 tpa
Power	24 MW
Railway Siding	2.4 km

(Source: Company)



(Source: Company)

SWOT Analysis



Investment Thesis

Capacity Expansion to drive volumes:

The company is increasing its manufacturing capacity in a phased manner. The sponge iron capacity would be in MSP Steel & Power Ltd. is on an expansion spree. It is increasing its sponge iron capacity from 1,92,000 MTPA to 423,000 MTPA by end of CY12. This capacity addition will be done in a phased manner. The increased capacity will drive volume growth for the company.

Table 3: MSPL Expansion program.

	Existing	Phase-I	Phase-II	Total
Pellet	3,00,000		6,00,000	9,00,000
Sponge Iron	1,92,000	1,15,500	1,15,500	4,23,000
Coal Washery	3,45,600		3,83,525	7,29,125
Billets	1,44,109			1,44,109
Power Plant (MW)	24	18	34	76
TMT	80,000			80,000
Structural	1,28,000			1,28,000
Railway Siding	2.4 km		4 km	6.4 km
Completion Date		October '10	July-Oct.'11	

(Source: Company)

Operating margins to improve:

Pelletization and Beneficiation process converts low grade iron ore fines (58 Fe content) into pellets which can be used in DRI kiln for production of sponge iron. There is not much export demand for iron ore fines and thus are available at cheaper rates. The company is expanding its pellet plant capacity from 300,000 ton per year to 900,000 ton per year. The expanded capacity is expected to be operational by FY12. Increasing capacity will lead to cost reduction resulting in margin expansion.

Table 4: Cost Analysis.

Rs. Per tone	Fine	Iron Ore Sized	Total Saving
Landed Cost	1500	6500	2500
Processing Cost	2500	-	
Total	4000	6500	

(Source: Company)

Raw Material Security

The company has been allotted coal and high grade iron ore mines in Chattisgarh. These allotments will take care of the capacity expansion program of the company.

Table 5: Status of mines.

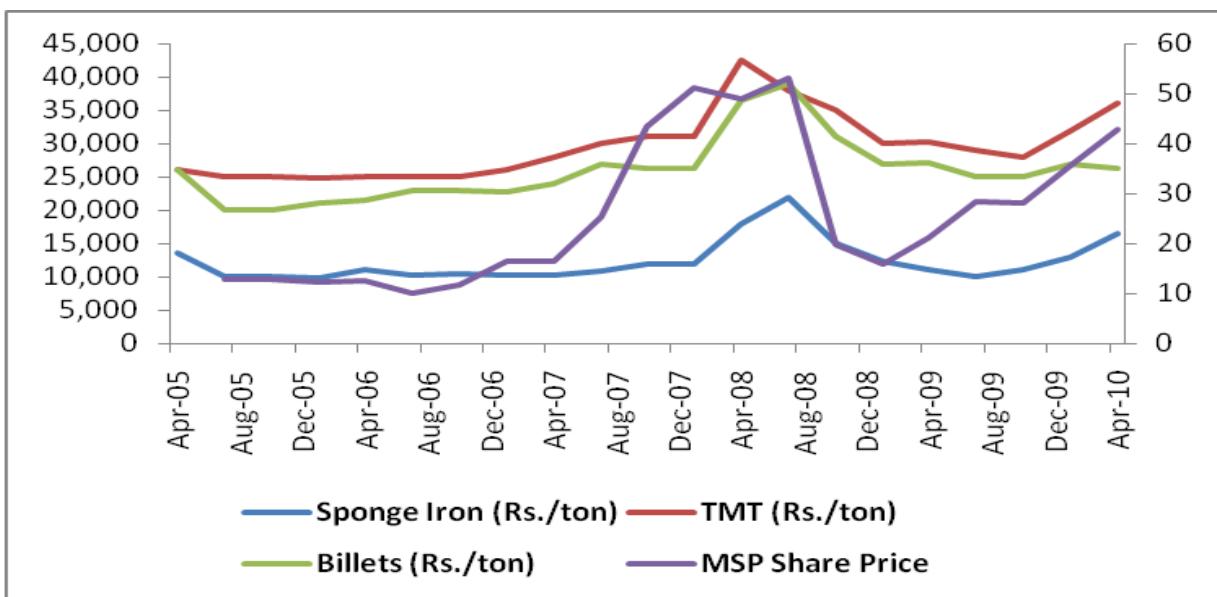
Nature of mines	Location	Mining Area	Reserves	MSP's share
Coal Block	Chhattishgarh	714 hectares	175 mn tonnes	26 mn tonnes
Iron Ore Block	Chhattishgarh	150 hectares	35 mn tonnes	35 mn tonnes

(Source: Company)

Traction in steel prices

Recovery in global economy has pushed up steel prices. They are expected to increase from \$455 per ton in FY09 to \$625-675 per ton in FY10 and \$675-725 per ton in FY11. Domestic TMT prices increased to Rs.36,000 per ton in April 2010 as compared to Rs.30,000 in April 2009.

Fig.1: Steel products price trend.



(Source: Company)

Management

Company's top management are first generation entrepreneurs with more than two decades of experience in steel and allied industry. Management in the past has shown high proactiveness with continuous focus on business integration.

Key personnel include:

Mr. Puranmal Agarwal (Chairman) & Mr. Suresh Agarwal (Managing Director).

Q3 FY11 Highlights

For the quarter ending December 2010, the company reported 50% increase in topline from Rs.963 mn in Q3, FY10 to Rs.1442 mn in Q3, FY11. EBITDA grew by 100% from Rs.178 mn to Rs.356 mn. Operating margins increased from 18% to 25%. However, Interest out-go climbed marginally by 7%. PAT jumped up by 188% from Rs.65 mn in Q3, FY10 to Rs.188 mn in Q3, FY11.

Fig.2: Quarterly Results.

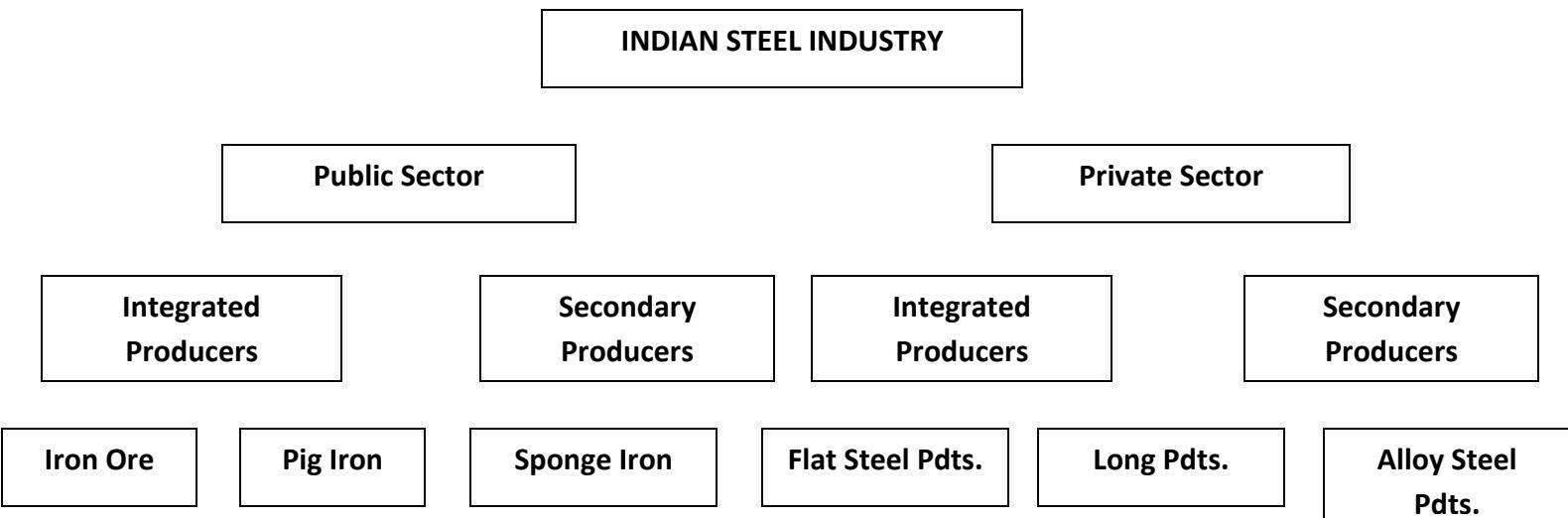
Particulars (in Rs. mn)	Q3, FY11	Q3, FY10	Y-o-Y change
Total Income	1442	963	50%
Raw Material	663	537	23%
Raw Material as % of Total Income	46%	56%	
Purchase of Traded Goods	235	104	126%
Purchase of Traded Goods as % of Total Income	16%	11%	
Employee Cost	35	30	17%
Employee Cost as % of Total Income	2%	3%	
Other Expenditure	153	114	34%
Other Expenditure as % of Total Income	11%	12%	
Total Expenditure	1086	785	38%
EBITDA	356	178	100%
EBITDA margins	25%	18%	
Depreciation	41.4	31.6	31%
EBIT	314.6	146.4	115%
EBIT margins	22%	15%	
Other Income	2.3	0.4	475%
Interest	63.2	58.8	7%
Profit before prior period items & Taxes	251.4	88	186%
Prior period items	3	0.5	500%
Profit before tax (PBT)	248.4	87.5	184%
PBT as % of Total Income	17%	9%	
Tax Expenses	60	22	173%
Effective tax rate	24%	25%	
Net Profit after tax	188.4	65.5	188%
EPS	3.25	1.13	188%

(Source: Greshma Research)

Industry Overview

We can summarize the Indian steel industry as shown in the below diagram.

Fig. 3: Components and Structure of the Indian Steel Industry.



India's iron and steel industry contributes about 2% of gross domestic product or about USD 20 billion to the country's USD 1 trillion economy. India produced 55.1 mn tonnes of steel in 2009. Its steel producing capacity is likely to touch 120 mn tonnes by 2012 according to government projections. Based on planned projects, capacity can go up to 293 mn tonnes by 2020.

Steel demand in India rose more than 8% in 2009, buoyed by the government's focus on infrastructure and revival in the automobile and consumer goods sectors of India's third-largest economy. However, global steel production fell 8% in 2009 as demand from key industries shrank amid the economic downturn. About half of India's steel industry comprises a large number of makers of high-end re-rolled steel with less than 1 million tonne of capacity each.

Current per capita consumption of steel is about 40 kg, compared with 100 kg in Brazil, 250 kg in China and a global average of 198 kg. Steel demand is expected to rise by 5-6% until 2019-20.

State-run Steel Authority of India is the largest producer with 13.8 mn tonnes.

Competitive Structure of Industry

Steel Industry Attractiveness:

- A) Competition:** The steel industry is highly fragmented. There are numerous small steel companies located in the mineral rich belt of Chhattisgarh and Jharkhand. With presence of such small players, the competition within the industry is intense. On the global front, the steel industry at times being affected by cheaper imports particularly from China. Such cheap imports have led to margin decline of Indian Steel companies. To counter the move, the steel companies have often sought for government intervention so as to increase import duty on steel products. Major Steel companies across the world are looking for consolidation through mergers and acquisitions. Arcelor Mittal & Tata Corus has been well known examples. Consolidation will keep a check on intensifying competition within the sector.
- B) Entry Barriers:** Steel is a capital intensive industry. Therefore, entry barriers are large particularly for the integrated steel producers (ISP). Also, these ISP have to sought various clearances like land, environment, forest, etc. which is a cumbersome process. Currently, India is facing problems in land acquisition for steel plants. Therefore, companies like JSW Steel are going for acquisition mode rather than setting up Greenfield projects. The company recently bought Ispat Industries to increase its manufacturing capacity. Indian steel companies are also facing hurdles in getting environment clearances for coal/iron oremines and their upcoming projects. Therefore, entry barriers remain high in this sector.
- C) Bargaining power of supplier:** The main raw material for steel production is coking coal and iron ore. Iron ore industry is a supplier's market with miners having strong negotiating powers compared to the steel industry. Good quality Coking Coal is a scarce commodity. Iron ore and coking coal are also subjected to price fluctuations. Therefore, the bargaining power of the supplier is high. To counter this move, steel companies are looking for raw material sufficiency by acquiring mines.
- D) Bargaining power of buyer:** Steel industry is a highly fragmented industry dominated by small manufacturers. Therefore, they do not enjoy substantial bargaining power as compared to their suppliers. This is very much evident from the fact that the steel companies had to bow down to the new agreement put forward by the iron miners. As per the new agreement, raw material contracts will be renewed every quarter instead of earlier practice of yearly contract.
- E) Threat of substitute:** Steel is primarily used in construction and automobile industry. Long products find application in the construction sector while Flat products are used in the automotive sector. Steel is a lighter material compared to other construction components like concrete. Therefore, there is no real threat of substitute for steel.

Peer Valuation and Growth

Fig.4: Relative Valuation.

Peer Group Comparison (Rs. in Millions)									
Company Name	Net Sales	PBDIT	PAT	EPS	EBITDA %	PAT %	ROCE %	RONW %	TTM PE (x)
SAIL	412302.7	98354.7	67543.7	16.4	23.9	16.4	24.6	22	11.7
Jindal Steel	73675.9	25372.7	14796.8	15.9	34.4	20.1	17.6	24.4	31.5
Tata Steel	250219.8	88577.6	50468	56.4	35.4	20.2	14.9	16.4	7.8
JSW Steel	182024.8	42729	20227.4	106.6	23.5	11.1	18.4	23.9	10.7
MSP Steel	3887.4	640.3	320.5	5.5	16.5	8.2	10.4	17.3	6.2

(Source: Greshma Research)

Among its peers, MSP Steel & Power Ltd. has lower operating margins and net profit margins. Companies like Steel Authority of India Ltd. (SAIL) and Tata Steel are largely backward integrated in terms of raw material. SAIL has good reserves of iron ore for its manufacturing facilities. Likewise, Tata Steel's Indian operations are substantially self-sufficient in terms of raw materials. The European operation in the form of Corus faces raw material volatility. Therefore, the company However, with the ongoing CAPEX on backward integration, the margins of the company are expected to improve. Better operational efficiencies will boost return ratios like RoE and RoCE. We expect expansion in valuation ratios on back of integrated business model which the company is currently working on.

Sensitivity Analysis

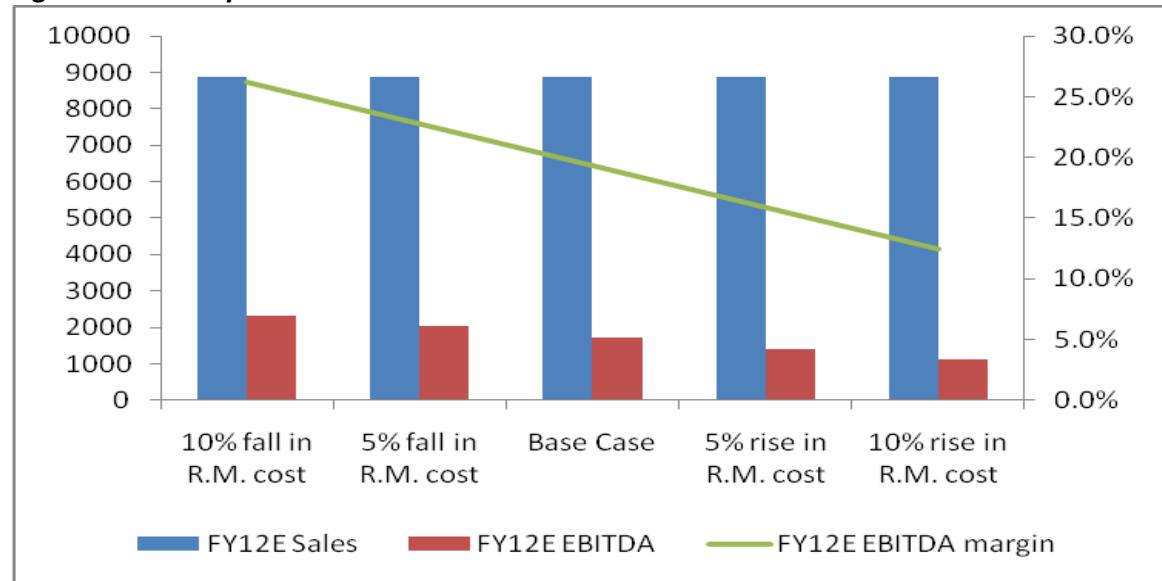
The main raw materials are iron ore and coal. The company is exposed to rising commodity prices which will directly impact the operating profit of the company. If the company is unable to pass on the increase in input cost then the EBITDA margins will be affected. Following are the different scenarios to test the sensitivity of changing raw material cost on operating margins of the company. The assumption is that the company is not passing on the change in input cost.

Fig.5: Effect of Raw Material Cost.

FY12E	Sales (in Rs. mn)	EBITDA (in Rs. mn)	EBITDA margin
10% fall in R.M. cost	8874	2329	26.2%
5% fall in R.M. cost	8874	2023	22.8%
Base Case	8874	1717	19.3%
5% rise in R.M. cost	8874	1410	15.9%
10% rise in R.M. cost	8874	1104	12.4%

(Source: Greshma Research)

Fig.6: Trend Analysis



(Source: Greshma Research)

Financial Summary

Fig.7: Profit/Loss Statement

Particulars (in Rs. mn)	FY09	FY10E	FY11E	FY12E
Net Sales	3989	3887	6646	8874
Expenditure				
Consumption of Raw Material	2910	2619	4765	6123
Staff Cost	68	113	127	170
Power & Fuel Cost	52	142	158	195
Other manufacturing cost	196	251	299	382
Gen. & Admin. Expenses	38	51	96	128
Selling & Distribution Expenses	61	27	75	106
Miscellaneous Expenditure	61	45	40	53
Total Expenditure	3384	3247	5560	7157
EBITDA before Other income	605	640	1086	1717
Depreciation	74	126	266	400
EBIT before Other income	531	514	820	1316
Other Income	156	72	123	164
Interest	194	204	349	466
EBT (PBT)	492	382	594	1014
Tax Expenses	93	62	96	164
PAT	399	321	498	851

(Source: Company Data, Greshma Research)

Fig.8: Balance Sheet

Particulars (in Rs. mn)	FY09	FY10E	FY11E	FY12E
Sources of Funds				
Share Capital	581	803	803	803
Reserves & Surplus	1111	1432	1930	2780
Loans	2727	4611	7164	9287
Total Liabilities	4419	6846	9896	12870
Application of funds				
Fixed assets				
Net Block & CWIP	3325	5013	7300	9570
Investments	67	450	450	450
Current Assets				
a) Inventories	393	683	970	1259
b) Sundry Debtors	418	668	887	1235
c) Cash & Bank Balance	194	379	327	324
d) Other Current Assets	562	729	1104	1475
Total Current Assets	1567	2460	3288	4293
Less Current Liab. & Prov.				
Current Liab.	216	642	732	962
Provisions	166	236	211	282
Total Current Liab.	382	878	943	1244
Net Current Assets	1185	1582	2345	3049
Deferred Tax Assets/Liab.	-158	-199	-199	-199
Total Assets	4419	6846	9896	12870

(Source: Company Data, Greshma Research)

Capacity expansion to drive top-line.

Margins to improve due to backward integration.

Debt to increase because of increasing CAPEX

Fixed assets to rise because of upcoming capacity.

Fig.9: Cashflow Statement.

Particulars (in mm)	FY09	FY10	FY11	FY12
Net income	399	321	498	851
Dep.	74	126	266	400
Other items	40	72	-105	0
Changes in Working Capital	131	-212	-815	-706
Cash flow from operating activities	644	307	-156	545
Capital Expenditure	997	2222	2670	2670
Change in investment	6	382	0	0
Cash flow from investing activities	1003	2604	2670	2670
Issue of equity	0	222	0	0
Repayment/issue of debt (net)	674	2481	2553	2123
Dividend Paid	0	0	0	0
Cash Flow from financing activities	674	2703	2553	2123
Net Cash	315	406	-273	-2
Opening Balance	215	194	600	327
Closing Balance	194	600	327	324

(Source: Company Data, Greshma Research)

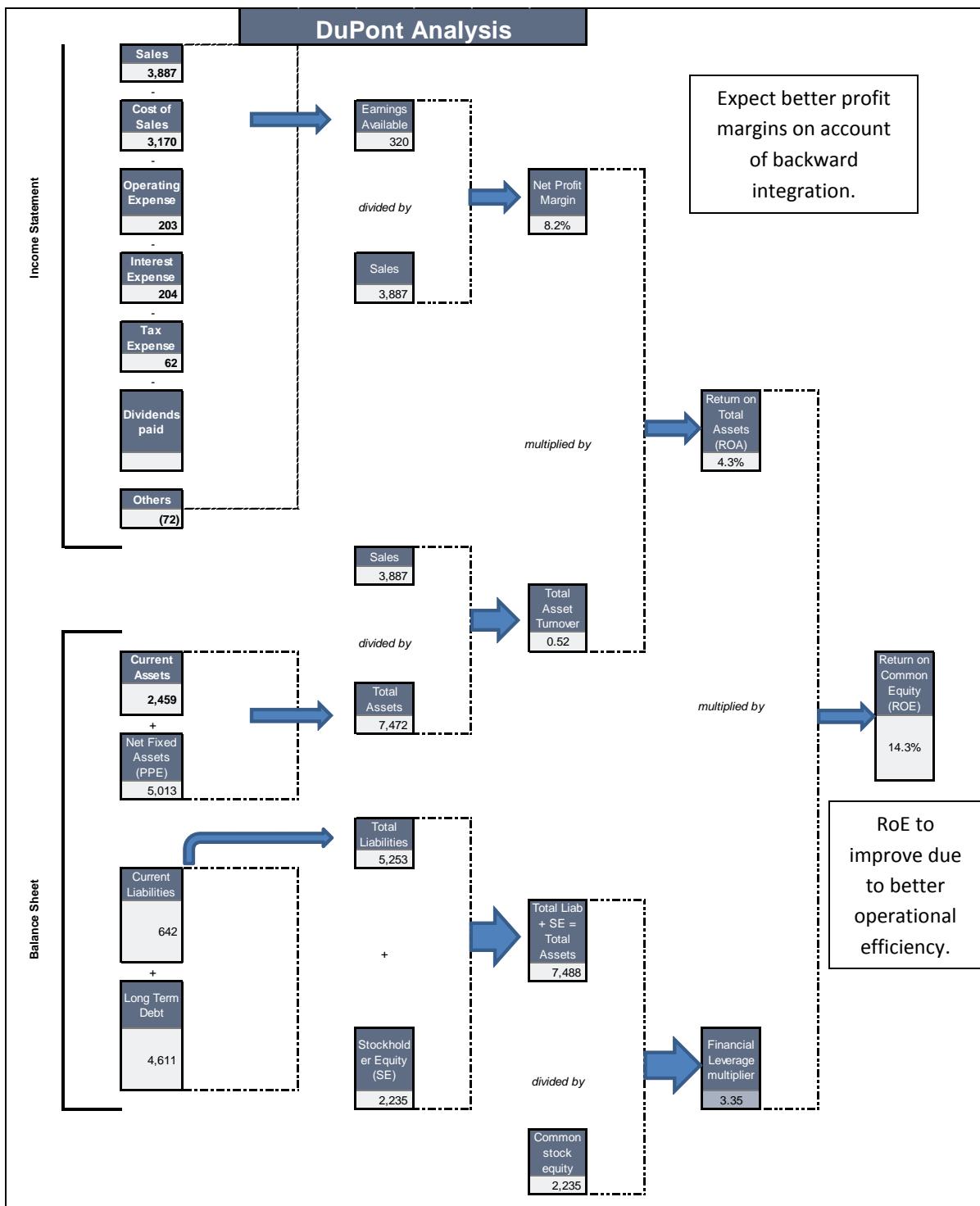
Depreciation to increase because of increased capacity coming online.

Fig.10: Ratios

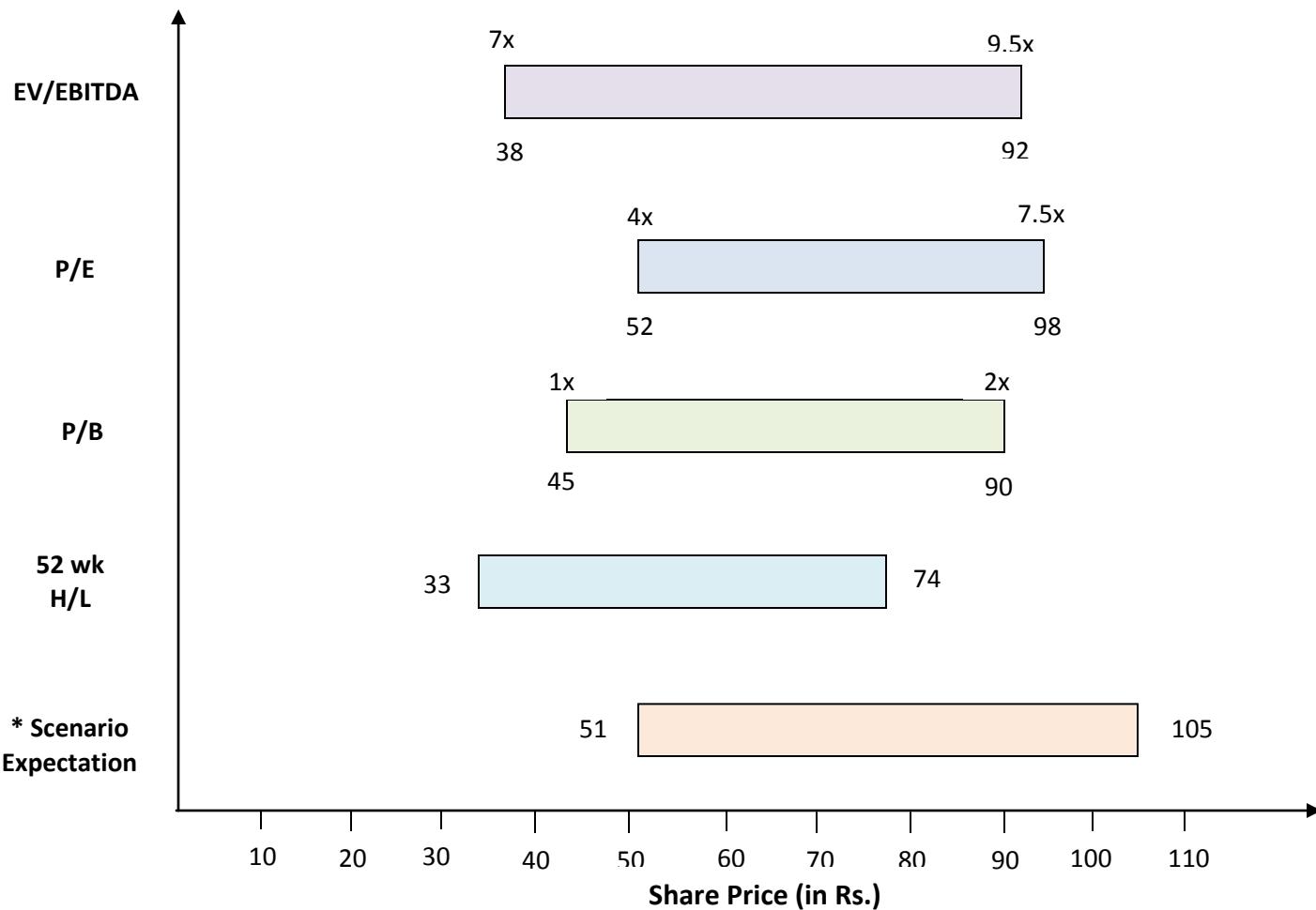
Particulars	FY09	FY10	FY11	FY12
EBITDA (in Rs.mn)	604.6	640.3	1086.099	1716.561
EBITDA margin (%)	15.16%	16.47%	16.34%	19.34%
PAT (in Rs.mn)	399	321	498	851
NPM (%)	10.0%	8.2%	7.5%	9.6%
RoE (%)	23.6%	14.3%	18.2%	23.7%
RoCE (%)	14.4%	9.9%	11.6%	14.1%

(Source: Company Data, Greshma Research)

RoCE to improve because of operational efficiency.



Football Valuation



*Scenario Expectation: Bull Case: Rs.51; Base Case: Rs.78; Bear Case: Rs.105.

Table 6: Valuation Summary

Particulars	FY09	FY10	FY11E	FY12E
EBITDA (Rs. mn)	604.6	640.3	1086.0	1716.5
EV/EBITDA (x)	12.4	14.4	10.9	8.1
EPS (Rs.)	6.9	5.5	8.6	14.7
PE (x)	9.0	11.3	7.2	4.2
BV (Rs.)	21.2	27.9	34.2	44.8
P/BV	2.9	2.2	1.8	1.4

(Source: Greshma Research)

Greshma's CSI Ranking Model

Valuations: A

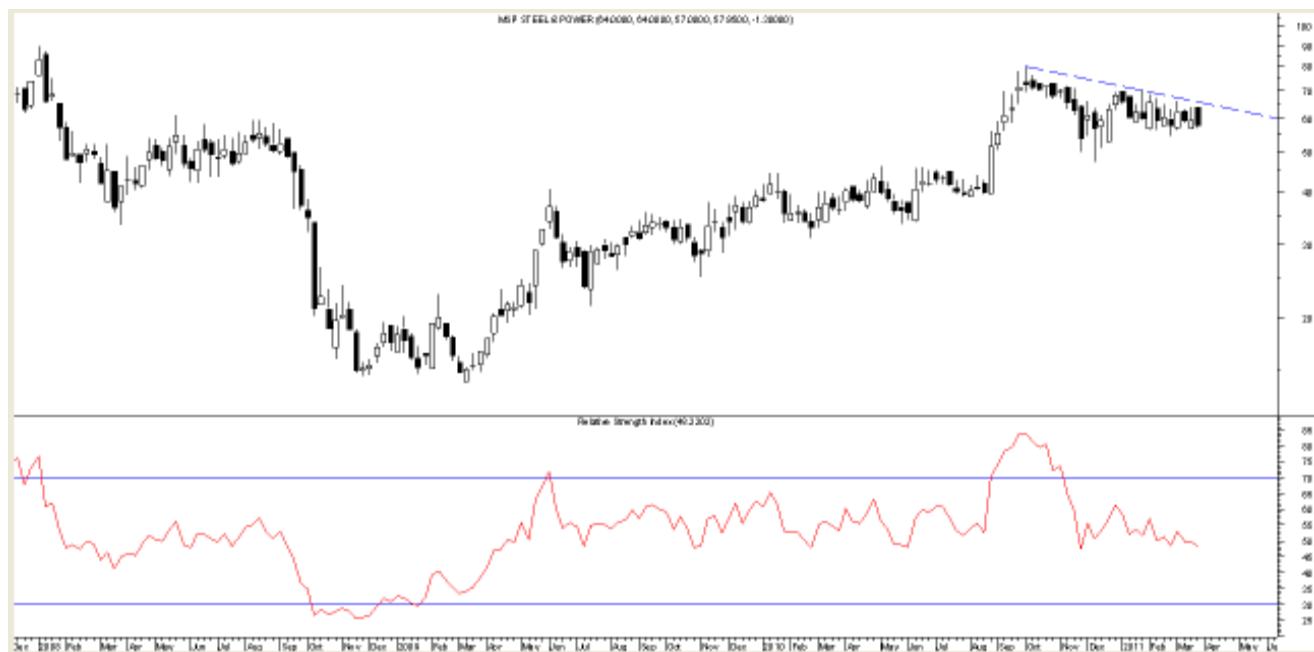
CSI: 3/5

(CSI is arrived on the basis of the underlying strength of the company on the basis of fundamentals and growth prospects)

Valuation	> 20%	A	HOLD		BUY MSPSP Ltd.	STRONG BUY		
	+5% TO +20%	B	HOLD			HOLD		
	-5% TO +5%	C	REDUCE			HOLD		
	-5% TO -20%	D	SELL			SELL		
	< -25%	E	SELL			SELL		
			1	2	3	4	5	
		VERY POOR	POOR	MODERATE	GOOD	VERY GOOD		
Core Strength Index								

Core Strength Index	Weightage
Industry/market structure	25%
Company track record	25%
Investor orientation	25%
Opportunity spectrum	25%

Technical View



- The counter has been in an uptrend since March '09 forming a series of higher tops and bottoms.
- Currently, the stock is in consolidation phase and formed lower highs; we expect current uptrend to continue if the prices breach the descending trend line.
- The RSI indicator is slipping below the 50 mark and if prices close below 53 levels, we expect 47 and 44.

Supports	Resistance
1 64-66	53-52
2 70-72	45-43

Expected Stock Performance

Period	Performance
Short Term (1-3 months)	Accumulate
Mid Term (6-12 months)	Buy
Long Term (more than 12 months)	Buy

DISCLAIMER

This Report is published by Greshma Shares & Stocks Ltd for private circulation. This report is meant for informational purposes and should not be construed as a solicitation or an offer to buy or sell any securities or related financial instruments. While utmost care has been taken in preparing this report, we claim no responsibility for its accuracy. Recipients should not regard the report as a substitute for the exercise of their own judgment. Any opinions expressed in this report are subject to change without any notice and this Report is not under any obligation to update or keep current the information contained herein. Past performance is not necessarily indicative of future results. This Report accepts no liability whatsoever for any loss or damage of any kind arising out of the use of all or any part of this report. Greshma and its associated companies, directors, officers and employees may from time to time have a long or short position in the securities mentioned and may sell or buy such securities, or act upon information contained herein prior to the publication thereof. Greshma may also provide other financial services to the companies mentioned in the report.