



INDEPENDENT EQUITY RESEARCH

MSP Steel and Power Ltd

Q2FY11 Result Update

Enhancing investment decisions

Explanation of CRISIL Fundamental and Valuation (CFV) matrix

The CFV Matrix (CRISIL Fundamental and Valuation Matrix) addresses the two important analysis of an investment making process – Analysis of Fundamentals (addressed through Fundamental Grade) and Analysis of Returns (Valuation Grade) The fundamental grade is assigned on a five-point scale from grade 5 (indicating Excellent fundamentals) to grade 1 (Poor fundamentals) The valuation grade is assigned on a five-point scale from grade 5 (indicating strong upside from the current market price (CMP)) to grade 1 (strong downside from the CMP).

CRISIL Fundamental Grade	Assessment	CRISIL Valuation Grade	Assessment
5/5	Excellent fundamentals	5/5	Strong upside (>25% from CMP)
4/5	Superior fundamentals	4/5	Upside (10-25% from CMP)
3/5	Good fundamentals	3/5	Align (+-10% from CMP)
2/5	Moderate fundamentals	2/5	Downside (- 10-25% from CMP)
1/5	Poor fundamentals	1/5	Strong downside (<-25% from CMP)

Analyst Disclosure

Each member of the team involved in the preparation of the grading report, hereby affirms that there exists no conflict of interest that can bias the grading recommendation of the company.

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MSP Steel and Power Ltd

Robust margins; speedy expansion

Fundamental Grade 2/5 (moderate fundamentals)

Valuation Grade 3/5 (CMP is aligned)

Industry Metals & Mining

MSP Steel and Power Ltd's (MSP's) Q2FY11 revenues were below CRISIL Equities' expectations due to a shift in mix towards lower-value products and lower realisations of intermediates as compared to our forecasts. It is difficult to predict MSP's top line since raw materials (i.e. sponge iron and power) can be directly sold (selling price ~Rs 16,000 per tonne and Rs 5 per unit respectively) or can be processed for making higher-realisable products - billets (~Rs 25,000)/ TMT bars (~Rs 28,000). The product mix variance can significantly impact the top line as well as EBITDA margins. MSP's expansion plans are on track and, therefore, we expect it to register significant growth going ahead. However, concerns relating to high leverage (net debt:equity 2.8x for FY11E) remain. Hence, we maintain our fundamental grade of 2/5.

Q2FY11 result analysis

- Q2FY11 revenues decreased by 7.6% q-o-q and increased by 8.4% y-o-y to Rs 988.7 mn. Overall sales declined due to lower sales of higher-value products - billets and TMT bars (~3,000 MT vs. 12,500 MT in Q1FY11 and 34,682 MT in Q2FY10).
- EBITDA margin expanded by 418 bps q-o-q and 912 bps y-o-y to 24%. This was on account of higher sales of better-margin products - power and structural steel - and better realisation of power in the merchant market.
- PAT increased by 28% q-o-q and 98% y-o-y to Rs 110.3 mn due to improved operating performance and lower tax rate. The company is paying a lower tax rate of 22% as compared to our assumptions because of higher power sales, which qualifies for tax rebate under Section 80IA.

Capacity expansion ahead of expectation

MSP started operations of its 115,500 MTPA sponge iron plant and 18 MW power plant in October 2010, which were actually expected to come on line in March 2011. Following this, we have changed our forecasts and we now believe that MSP will be able to complete the remaining capacity expansion (115,500 MTPA sponge iron, 34MW power plant and 600,000 MTPA pellet plant) on time – Q2FY12 - compared to our earlier expectations of end-FY12.

Valuations: Current market price is aligned with fair value

We continue to value MSP based on the discounted cash flow method. Factoring in lower sales but higher PAT margins, we have raised MSP's earnings estimates. We have also rolled forward our estimates by one year. Based on the revised estimates, we have increased our fair value to Rs 57 from Rs 44. We maintain our valuation grade of '3/5'.

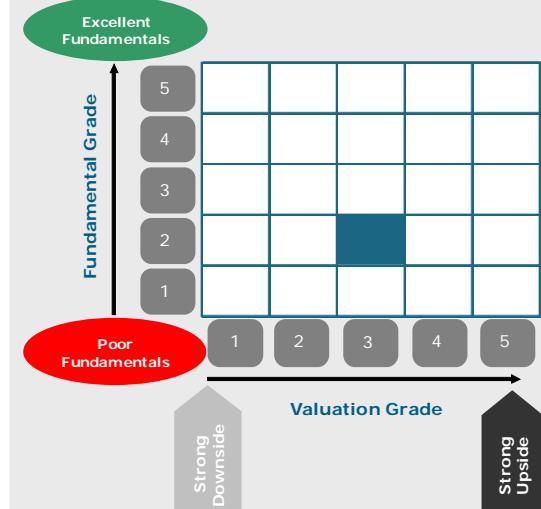
KEY FORECAST

(Rs mn)	FY08	FY09	FY10	FY11E	FY12E
Operating income	3,628	4,039	3,959	6,049	9,931
EBITDA	691	643	701	1,258	2,055
Adj PAT	343	268	314	509	846
Adj EPS-Rs	5.9	4.6	5.4	8.8	14.6
EPS growth (%)	131.2	(18.6)	(15.6)	58.7	66.37
Dividend yield	-	-	-	-	-
RoCE (%)	23.2	14.5	10.2	12.0	14.0
RoE (%)	32.4	18.0	16.0	21.4	28.7
P/E (x)	10.3	13.1	11.2	6.9	4.2
P/BV (x)	2.7	2.1	1.6	1.4	1.0
EV/EBITDA (x)	7.8	9.4	10.5	8.4	6.7

Source: Company, CRISIL Equities estimate

NM: Not meaningful; CMP: Current Market Price

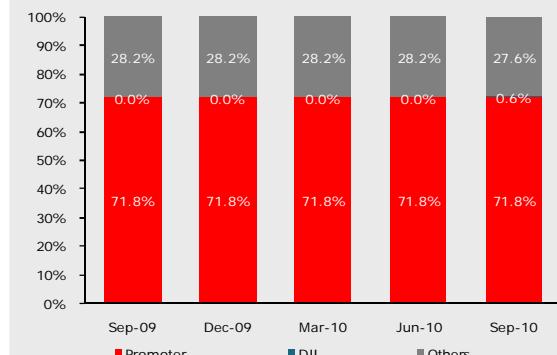
CFV MATRIX



KEY STOCK STATISTICS

NIFTY / SENSEX	5863/19521
NSE ticker	MSPL
Face value (Rs per share)	10
Shares outstanding (mn)	58.1
Market cap (Rs mn)/(US\$ mn)	3527/77
Enterprise value (Rs mn) /(US\$ mn)	7759/171
52-week range (Rs) (H/L)	80/31
Beta	1.3
Free float (%)	30%
Avg daily volumes (30-days)	200881
Avg daily value (30-days) (Rs mn)	13

SHAREHOLDING PATTERN



PERFORMANCE VIS-À-VIS MARKET

	Returns			
	1-m	3-m	6-m	12-m
MSP	-11%	15%	68%	74%
NIFTY	-3%	8%	16%	16%

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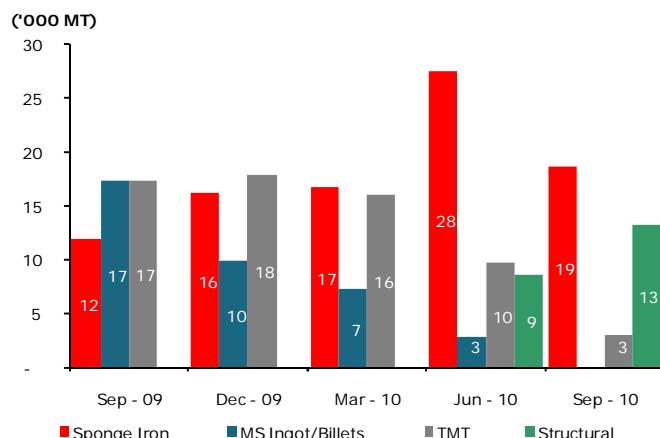
Q2FY11 Result Summary

(Rs mn)	Q2FY11	Q1FY11	Q2FY10	q-o-q (%)	y-o-y (%)
Net sales	989	1,071	912	(7.6)	8.4
(Increase)/decrease in stock in trade and WIP	(67)	(68)	(60)	(0.5)	12.7
Raw materials cost	505	756	691	(33.2)	(26.9)
Raw materials cost (% of net sales)	51.1%	70.6%	75.7%	-1955 bps	-2462 bps
Purchase of traded goods	114	-	-	NM	NM
Employees cost	36	36	29	(2.2)	21.4
Other expenses	167	137	119	22.1	40.2
EBITDA	234	209	133	12.2	76.1
EBITDA margin	23.7%	19.5%	14.6%	419 bps	912 bps
Depreciation	43	42	31	1.0	36.4
EBIT	192	167	102	15.0	88.4
Interest and finance charges	58	56	45	3.8	30.4
Operating PBT	133	111	57	20.7	133.7
Other Income	8	0.2	6	3,717.1	n.m.
PBT	142	111	63	27.5	124.5
Tax	31	24	7	29.7	330.6
PAT	110	87	56	26.9	97.6
Adj PAT	110	87	56	26.9	97.6
Adj PAT margin	11.2%	8.1%	6.1%	304 bps	504 bps
No of equity shares (mn)	58.1	58.1	58.1	-	-
Adj EPS (Rs)	1.9	1.5	1.0	26.9	97.6

EBITDA margin
expanded due to higher sales of better-margin products - power and structural steel

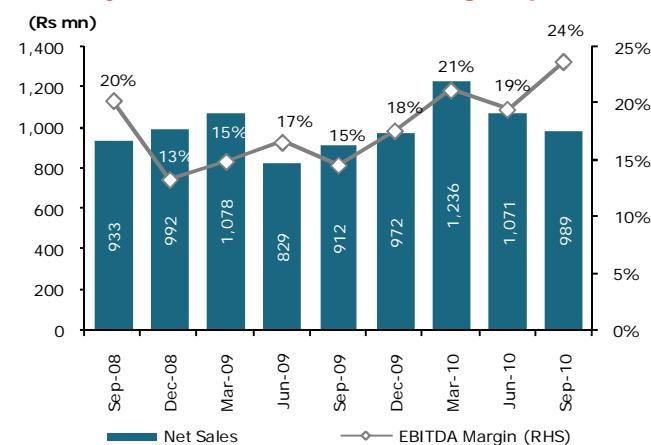
Source: Company, CRISIL Equities

Lower sales of billets and TMT



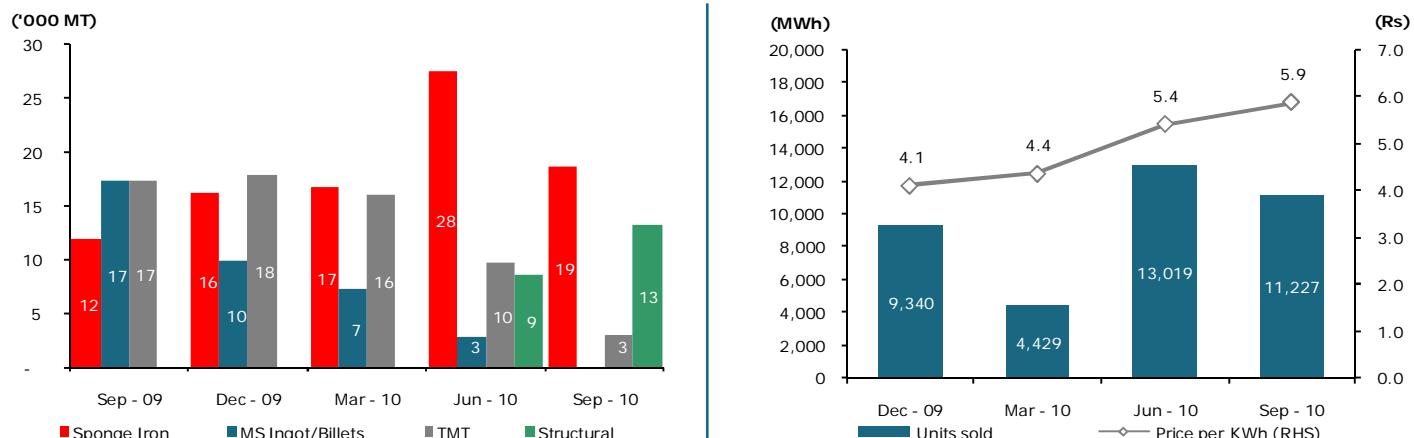
Source: Company, CRISIL Equities

Quarterly sales down, EBITDA margin up



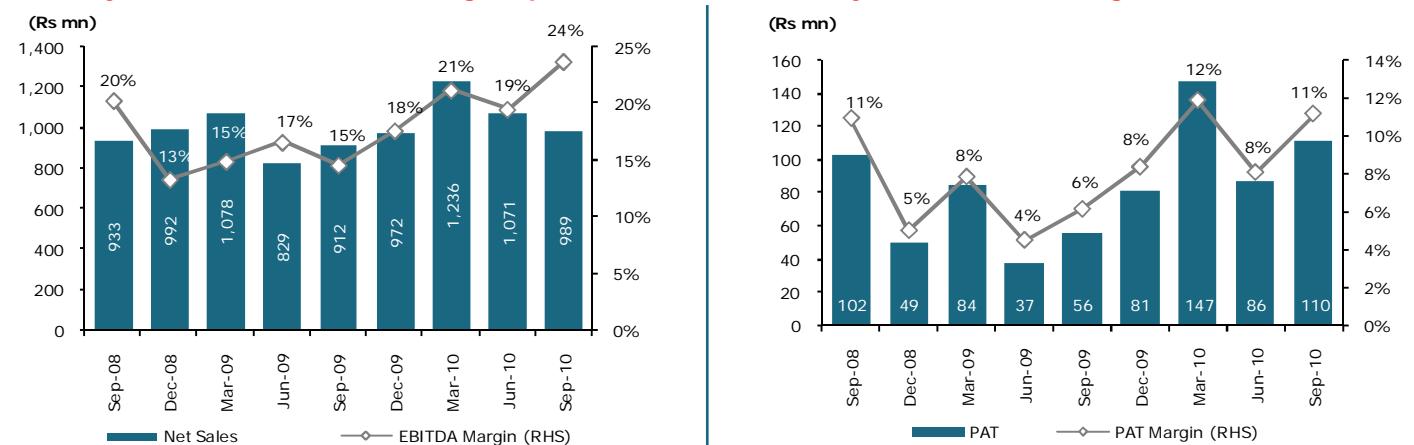
Source: Company, CRISIL Equities

Higher power sales at better rate boosted margins



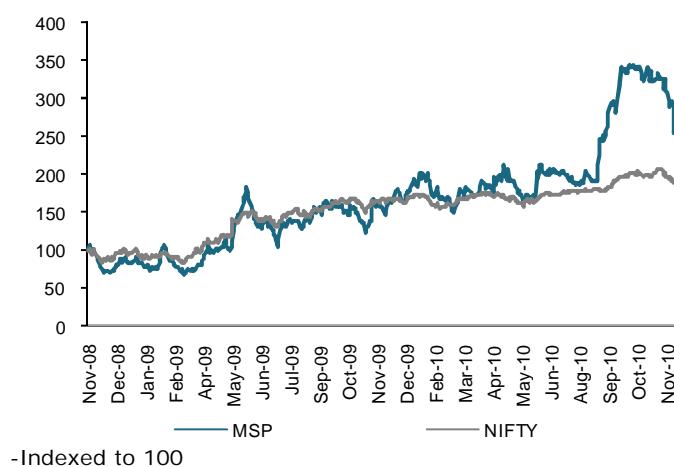
Source: Company, CRISIL Equities

Quarterly PAT and PAT margin on the rise

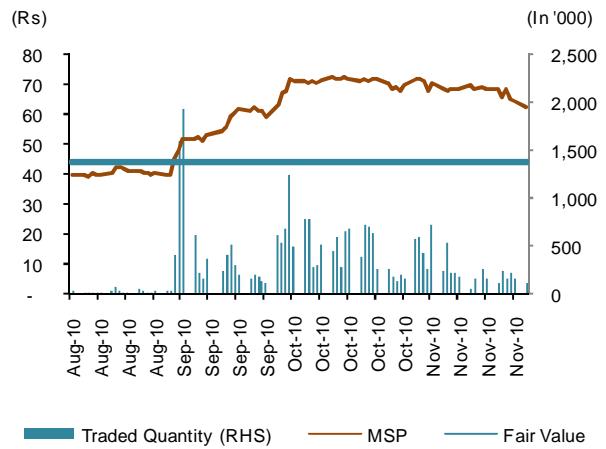


Source: Company, CRISIL Equities

Share price movement



Fair value movement since initiation



EARNINGS ESTIMATES REVISED UPWARDS

We have reduced our revenue forecast as MSP reduced sales of higher-value products – billets and TMT - because of lower realisations compared to the conversion cost. Instead, the company sold sponge iron and power in the open market which helped it get better margins.

Due to increased integration benefits from the recently installed sponge iron and power plants, growing scale and high merchant power rates we have raised our EBITDA margin estimate to 20.8% in FY11 from 17.7%. We have also reduced our tax rate assumption to 22% from 33%, pushing the PAT margin estimate higher to 8.1% from 5.7%.

Particulars	Unit	FY11E			FY12E		
		Old	New	% change	Old	New	% change
Revenue	(Rs mn)	8,376	5,989	-28.49%	11,713	9,833	-16.05%
EBITDA	(Rs mn)	1,501	1,258	-16.21%	2,178	2,055	-5.62%
EBITDA margin	%	17.7	20.8	3.05 pps	18.4	20.7	2.29 pps
PAT	(Rs mn)	484	509	5.03%	857	846	-1.24%
PAT margin	%	5.7	8.4	2.68 pps	7.2	8.5	1.28 pps
EPS	Rs	8.3	8.8	5.57%	14.7	14.6	-0.73%

VALUATION

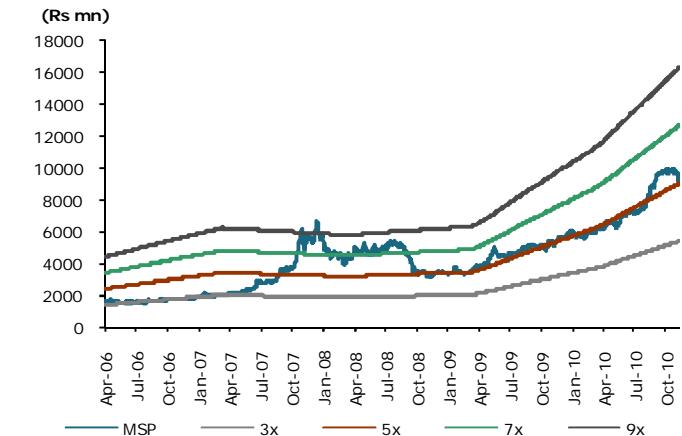
We continue to value MSP based on the discounted cash flow method. Following a revision in our earnings estimates - lower sales but higher margins - and rolling forward of projections by a year to FY12, we have increased our one-year fair value to Rs 57 from Rs 44. At this value, the implied P/E multiples are 6.5x FY11E EPS of Rs 8.8 and 4.0x FY12E EPS of Rs 14.6.

Fair value revised to Rs 57 per share

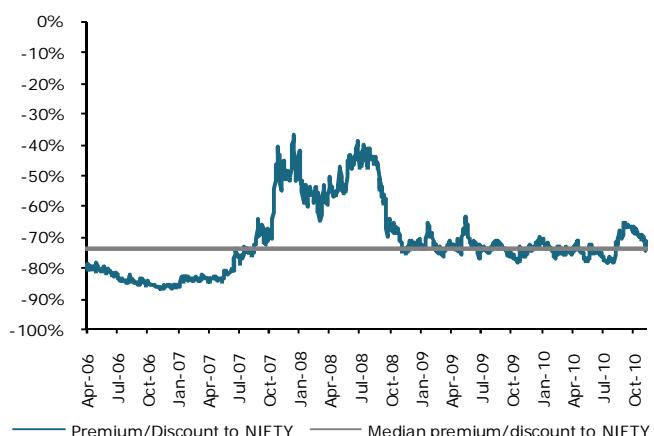
One-year forward P/E band



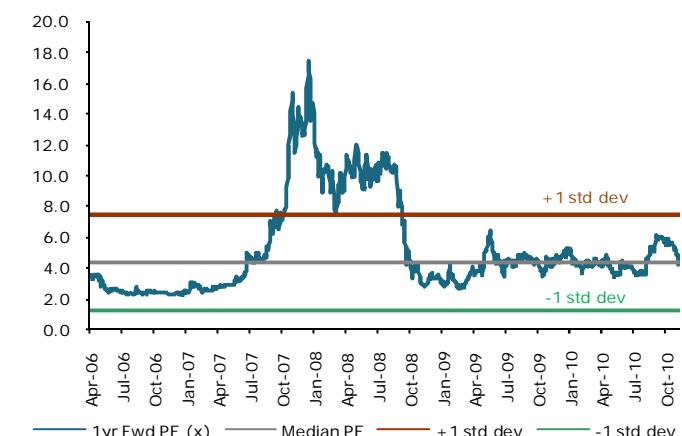
One-year forward EV/EBITDA band



P/E – premium/discount to NIFTY



P/E movement



CRISIL IER reports released on MSP Steel and Power Ltd

Date	Nature of report	Fundamental grade	Fair value	Valuation grade	CMP (on the date of report)
29-Jul-10	Initiating coverage*	2/5	Rs 44	3/5	Rs 40
01-Dec-10	Q2FY11 result update	2/5	Rs 57	3/5	Rs 61

* For detailed initiating coverage report please visit: www.ier.co.in

CRISIL Independent Equity Research reports are also available on Bloomberg (CRI <go>) and Thomson Reuters.

FINANCIALS

Income statement						Balance Sheet					
(Rs mn)	FY08	FY09	FY10E	FY11E	FY12E	(Rs mn)	FY08	FY09	FY10E	FY11E	FY12E
Operating income	3,628	4,039	3,959	6,049	9,931	Liabilities					
EBITDA	691	643	701	1,258	2,055	Equity share capital	581	581	581	581	581
EBITDA margin	19.0%	15.9%	17.7%	20.8%	20.7%	Reserves	712	1,111	1,654	1,941	2,787
Depreciation	73	79	127	245	368	Minorities	-	-	-	-	-
EBIT	618	564	573	1,013	1,688	Net worth	1,293	1,692	2,235	2,522	3,368
Interest	141	215	205	371	619	Convertible debt	-	-	-	-	-
Operating PBT	476	348	368	642	1,068	Other debt	2,053	2,727	4,611	7,493	10,793
Other income	4	7	7	10	17	Total debt	2,053	2,727	4,611	7,493	10,793
Exceptional inc/(exp)	124	111	7	-	-	Deferred tax liability (net)	93	158	199	199	199
PBT	605	466	382	652	1,085	Total liabilities	3,439	4,578	7,044	10,213	14,359
Tax provision	138	87	62	143	239	Assets					
Minority interest	-	-	-	-	-	Net fixed assets	1,347	2,273	2,559	4,827	7,198
PAT (Reported)	467	380	321	509	846	Capital WIP	693	1,052	2,454	2,654	2,994
Less: Exceptionals	124	111	7	-	-	Total fixed assets	2,040	3,325	5,013	7,481	10,192
Adjusted PAT	343	268	314	509	846	Investments	61	67	70	70	70
Ratios						Current assets					
	FY08	FY09	FY10E	FY11E	FY12E	Inventory	463	393	683	994	1,632
Growth						Sundry debtors	675	418	669	746	1,224
Operating income (%)	62.3	11.3	(2.0)	52.8	64.2	Loans and advances	612	400	500	764	1,253
EBITDA (%)	44.5	(7.0)	9.0	79.6	63.4	Cash & bank balance	215	194	379	64	75
Adj PAT (%)	70.3	(21.6)	16.8	62.2	66.4	Marketable securities	-	-	380	380	380
Adj EPS (%)	70.3	(21.6)	16.8	62.2	66.4	Total current assets	1,966	1,406	2,611	2,948	4,566
Profitability						Total current liabilities	628	220	649	285	468
EBITDA margin (%)	19.0	15.9	17.7	20.8	20.7	Net current assets	1,338	1,185	1,962	2,663	4,097
Adj PAT Margin (%)	9.4	6.6	7.9	8.4	8.5	Intangibles/Misc. expenditure	-	-	-	-	-
RoE (%)	32.4	18.0	16.0	21.4	28.7	Total assets	3,439	4,578	7,044	10,213	14,359
RoCE (%)	23.2	14.5	10.2	12.0	14.0	Cash flow					
RoIC (%)	19.8	13.6	10.0	10.9	12.4	(Rs mn)	FY08	FY09	FY10E	FY11E	FY12E
Valuations						Pre-tax profit	480	355	375	652	1,085
Price-earnings (x)	10.3	13.1	11.2	6.9	4.2	Total tax paid	(73)	(21)	(21)	(143)	(239)
Price-book (x)	2.7	2.1	1.6	1.4	1.0	Depreciation	73	79	127	245	368
EV/EBITDA (x)	7.8	9.4	10.5	8.4	6.7	Working capital changes	(528)	131	(212)	(1,016)	(1,423)
EV/Sales (x)	1.5	1.5	2.0	1.8	1.4	Net cash from operations	(48)	544	270	(262)	(209)
Dividend payout ratio (%)	-	-	-	-	-	Cash from investments					
Dividend yield (%)	-	-	-	-	-	Capital expenditure	(831)	(1,364)	(1,816)	(2,712)	(3,080)
B/S ratios						Investments and others	(7)	(6)	(382)	-	-
Inventory days	59	44	77	78	78	Net cash from investments	(838)	(1,370)	(2,198)	(2,712)	(3,080)
Creditors days	72	23	72	21	21	Cash from financing					
Debtor days	73	37	61	45	45	Equity raised/(repaid)	-	(5)	-	-	-
Working capital days	86	96	101	103	108	Debt raised/(repaid)	898	674	1,884	2,882	3,300
Gross asset turnover (x)	2.6	2.0	1.5	1.4	1.5	Dividend (incl. tax)	-	-	-	-	-
Net asset turnover (x)	3.0	2.2	1.6	1.6	1.7	Others (incl. extraordinaries)	126	136	229	(222)	0
Sales/operating assets (x)	2.2	1.5	0.9	1.0	1.1	Net cash from financing	1,024	804	2,113	2,660	3,300
Current ratio (x)	3.1	6.4	4.0	10.3	9.7	Change in cash position	139	(21)	185	(315)	11
Debt-equity (x)	1.6	1.6	2.1	3.0	3.2	Closing cash	215	194	379	64	75
Net debt/equity (x)	1.4	1.5	1.7	2.8	3.1	Quarterly financials					
Interest coverage	4.4	2.6	2.8	2.7	2.7	(Rs Mn)	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11
Per share						Net Sales	912	972	1,236	1,071	989
	FY08	FY09	FY10E	FY11E	FY12E	Change (q-o-q)	NM	7%	27%	-13%	-8%
Adj EPS (Rs)	5.9	4.6	5.4	8.8	14.6	EBITDA	133	171	262	209	234
CEPS	7.2	6.0	7.6	13.0	20.9	Change (q-o-q)	NM	29%	53%	-20%	12%
Book value	22.3	29.1	38.5	43.4	58.0	EBITDA margin	14.6%	17.6%	21.2%	19.5%	23.7%
Dividend (Rs)	-	-	-	-	-	PAT	56	81	147	86	110
Actual o/s shares (mn)	58.1	58.1	58.1	58.1	58.1	Adj PAT	56	81	147	86	110
						Change (q-o-q)	NM	45%	81%	-41%	28%
						Adj PAT margin	6.1%	8.3%	11.9%	8.1%	11.2%
						Adj EPS	1.0	1.4	2.5	1.5	1.9

Source: Company, CRISIL Equities estimate

Note: All ratios are computed on adj. PAT

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