



# **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-realizable 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

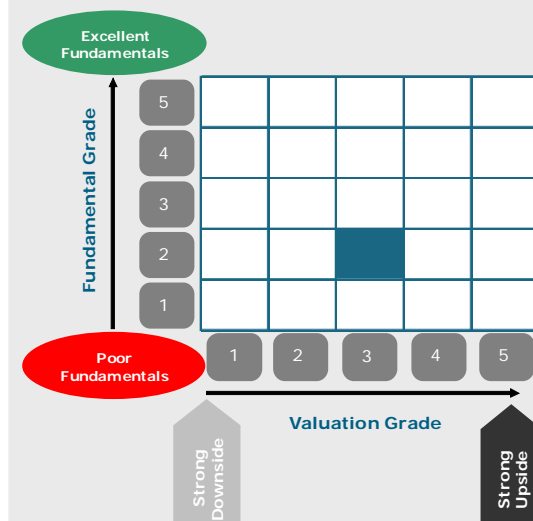
Source: Company, CRISIL Equities estimate

NM: Not meaningful; CMP: Current Market Price

December 01, 2010

Fair Value Rs 57  
CMP Rs 61

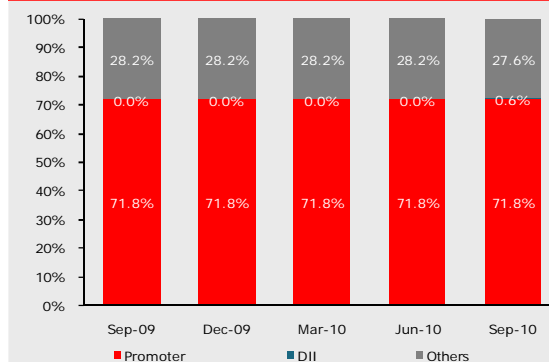
## CFV MATRIX



## 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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# MSP Steel and Power Ltd

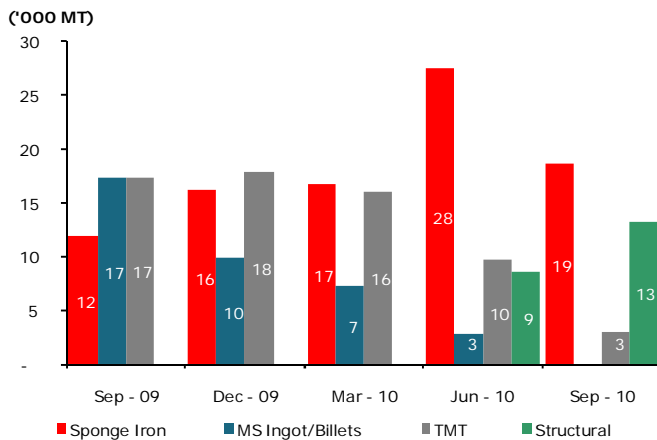
## Q2FY11 Result Summary

(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**

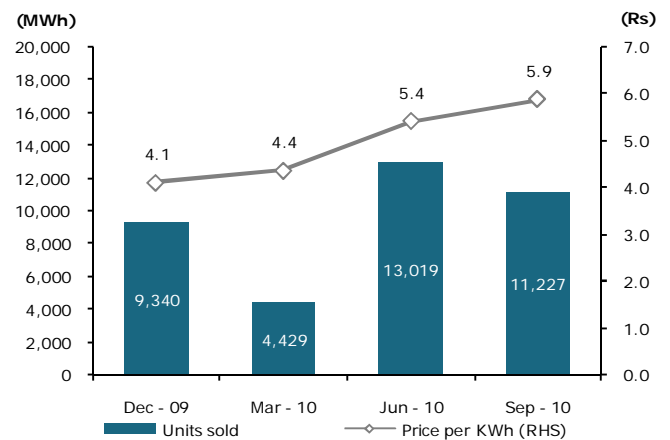
Source: Company, CRISIL Equities

### Lower sales of billets and TMT



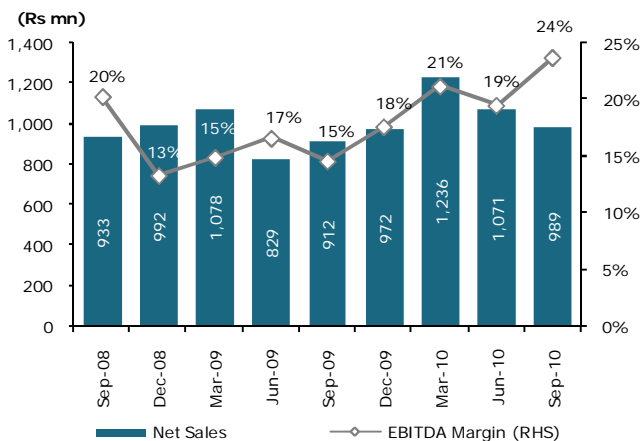
Source: Company, CRISIL Equities

### Higher power sales at better rate boosted margins



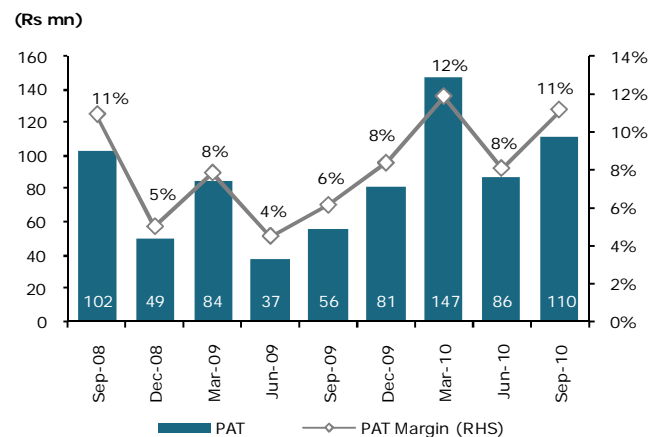
Source: Company, CRISIL Equities

### Quarterly sales down, EBITDA margin up



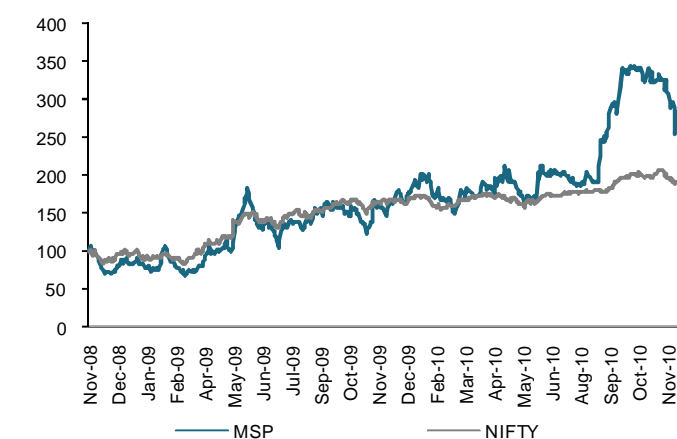
Source: Company, CRISIL Equities

### Quarterly PAT and PAT margin on the rise



Source: Company, CRISIL Equities

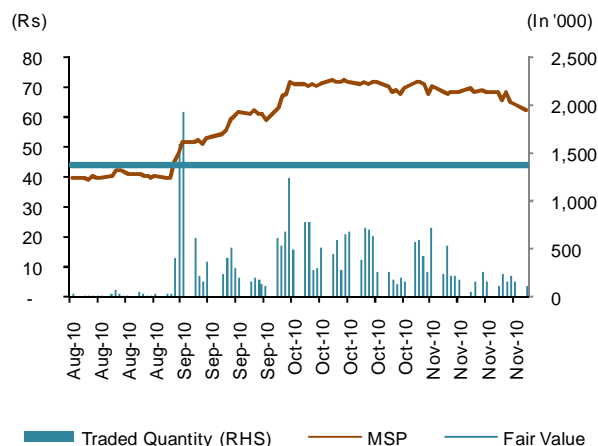
## Share price movement



-Indexed to 100

Source: NSE, CRISIL Equities

## Fair value movement since initiation



Source: NSE, CRISIL Equities

## 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%

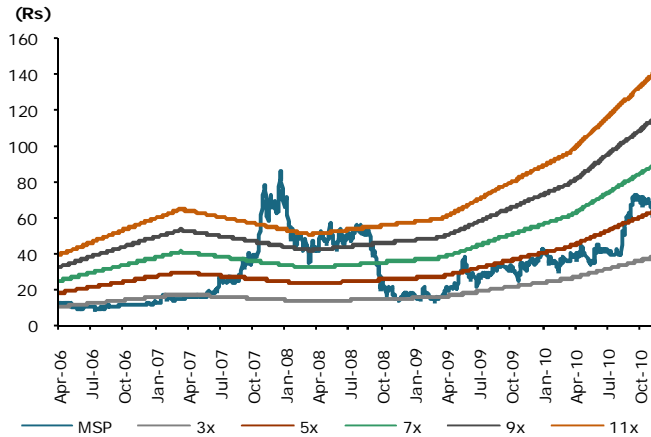
# MSP Steel and Power Ltd

## 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.

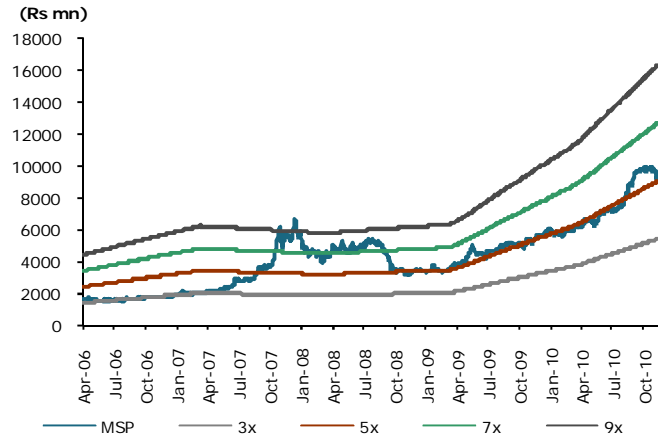
**Fair value revised to Rs 57 per share**

### One-year forward P/E band



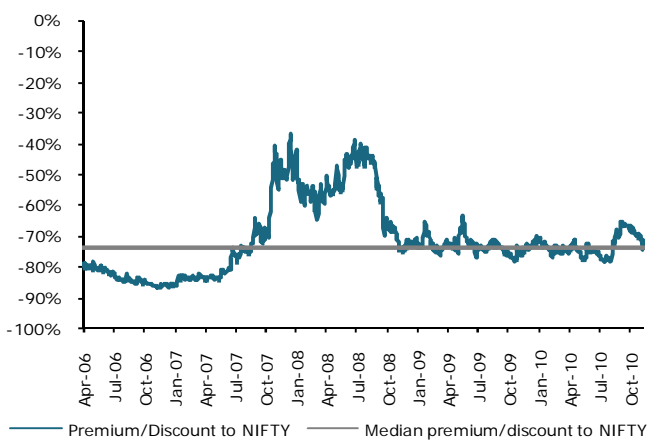
Source: NSE, CRISIL Equities

### One-year forward EV/EBITDA band



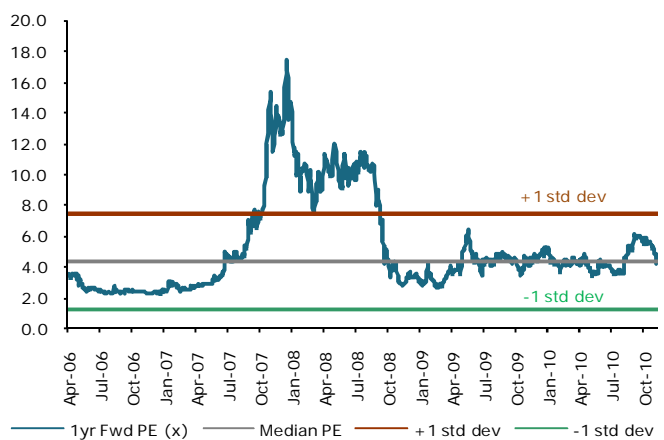
Source: NSE, CRISIL Equities

### P/E – premium/discount to NIFTY



Source: NSE, CRISIL Equities

### P/E movement



Source: NSE, CRISIL Equities

### 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](http://www.ier.co.in)

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



# MSP Steel and Power Ltd

## FINANCIALS

### Income statement

(Rs mn)	FY08	FY09	FY10E	FY11E	FY12E
<b>Operating income</b>	<b>3,628</b>	<b>4,039</b>	<b>3,959</b>	<b>6,049</b>	<b>9,931</b>
<b>EBITDA</b>	<b>691</b>	<b>643</b>	<b>701</b>	<b>1,258</b>	<b>2,055</b>
<b>EBITDA margin</b>	<b>19.0%</b>	<b>15.9%</b>	<b>17.7%</b>	<b>20.8%</b>	<b>20.7%</b>
Depreciation	73	79	127	245	368
<b>EBIT</b>	<b>618</b>	<b>564</b>	<b>573</b>	<b>1,013</b>	<b>1,688</b>
Interest	141	215	205	371	619
<b>Operating PBT</b>	<b>476</b>	<b>348</b>	<b>368</b>	<b>642</b>	<b>1,068</b>
Other income	4	7	7	10	17
Exceptional inc/(exp)	124	111	7	-	-
<b>PBT</b>	<b>605</b>	<b>466</b>	<b>382</b>	<b>652</b>	<b>1,085</b>
Tax provision	138	87	62	143	239
Minority interest	-	-	-	-	-
<b>PAT (Reported)</b>	<b>467</b>	<b>380</b>	<b>321</b>	<b>509</b>	<b>846</b>
Less: Exceptionals	124	111	7	-	-
<b>Adjusted PAT</b>	<b>343</b>	<b>268</b>	<b>314</b>	<b>509</b>	<b>846</b>

### Ratios

	FY08	FY09	FY10E	FY11E	FY12E
<b>Growth</b>					
Operating income (%)	62.3	11.3	(2.0)	52.8	64.2
EBITDA (%)	44.5	(7.0)	9.0	79.6	63.4
Adj PAT (%)	70.3	(21.6)	16.8	62.2	66.4
Adj EPS (%)	70.3	(21.6)	16.8	62.2	66.4
<b>Profitability</b>					
EBITDA margin (%)	19.0	15.9	17.7	20.8	20.7
Adj PAT Margin (%)	9.4	6.6	7.9	8.4	8.5
RoE (%)	32.4	18.0	16.0	21.4	28.7
RoCE (%)	23.2	14.5	10.2	12.0	14.0
RoIC (%)	19.8	13.6	10.0	10.9	12.4
<b>Valuations</b>					
Price-earnings (x)	10.3	13.1	11.2	6.9	4.2
Price-book (x)	2.7	2.1	1.6	1.4	1.0
EV/EBITDA (x)	7.8	9.4	10.5	8.4	6.7
EV/Sales (x)	1.5	1.5	2.0	1.8	1.4
Dividend payout ratio (%)	-	-	-	-	-
Dividend yield (%)	-	-	-	-	-
<b>B/S ratios</b>					
Inventory days	59	44	77	78	78
Creditors days	72	23	72	21	21
Debtor days	73	37	61	45	45
Working capital days	86	96	101	103	108
Gross asset turnover (x)	2.6	2.0	1.5	1.4	1.5
Net asset turnover (x)	3.0	2.2	1.6	1.6	1.7
Sales/operating assets (x)	2.2	1.5	0.9	1.0	1.1
Current ratio (x)	3.1	6.4	4.0	10.3	9.7
Debt-equity (x)	1.6	1.6	2.1	3.0	3.2
Net debt/equity (x)	1.4	1.5	1.7	2.8	3.1
Interest coverage	4.4	2.6	2.8	2.7	2.7

### Per share

	FY08	FY09	FY10E	FY11E	FY12E
Adj EPS (Rs)	5.9	4.6	5.4	8.8	14.6
CEPS	7.2	6.0	7.6	13.0	20.9
Book value	22.3	29.1	38.5	43.4	58.0
Dividend (Rs)	-	-	-	-	-
Actual o/s shares (mn)	58.1	58.1	58.1	58.1	58.1

Source: Company, CRISIL Equities estimate

Note: All ratios are computed on adj. PAT

### Balance Sheet

(Rs mn)	FY08	FY09	FY10E	FY11E	FY12E
<b>Liabilities</b>					
Equity share capital	581	581	581	581	581
Reserves	712	1,111	1,654	1,941	2,787
Minorities	-	-	-	-	-
<b>Net worth</b>	<b>1,293</b>	<b>1,692</b>	<b>2,235</b>	<b>2,522</b>	<b>3,368</b>
Convertible debt	-	-	-	-	-
Other debt	2,053	2,727	4,611	7,493	10,793
<b>Total debt</b>	<b>2,053</b>	<b>2,727</b>	<b>4,611</b>	<b>7,493</b>	<b>10,793</b>
Deferred tax liability (net)	93	158	199	199	199
<b>Total liabilities</b>	<b>3,439</b>	<b>4,578</b>	<b>7,044</b>	<b>10,213</b>	<b>14,359</b>
<b>Assets</b>					
Net fixed assets	1,347	2,273	2,559	4,827	7,198
Capital WIP	693	1,052	2,454	2,654	2,994
<b>Total fixed assets</b>	<b>2,040</b>	<b>3,325</b>	<b>5,013</b>	<b>7,481</b>	<b>10,192</b>
<b>Investments</b>	<b>61</b>	<b>67</b>	<b>70</b>	<b>70</b>	<b>70</b>
<b>Current assets</b>					
Inventory	463	393	683	994	1,632
Sundry debtors	675	418	669	746	1,224
Loans and advances	612	400	500	764	1,253
Cash & bank balance	215	194	379	64	75
Marketable securities	-	-	380	380	380
<b>Total current assets</b>	<b>1,966</b>	<b>1,406</b>	<b>2,611</b>	<b>2,948</b>	<b>4,566</b>
<b>Total current liabilities</b>	<b>628</b>	<b>220</b>	<b>649</b>	<b>285</b>	<b>468</b>
<b>Net current assets</b>	<b>1,338</b>	<b>1,185</b>	<b>1,962</b>	<b>2,663</b>	<b>4,097</b>
<b>Intangibles/Misc. expenditure</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Total assets</b>	<b>3,439</b>	<b>4,578</b>	<b>7,044</b>	<b>10,213</b>	<b>14,359</b>

### Cash flow

(Rs mn)	FY08	FY09	FY10E	FY11E	FY12E
Pre-tax profit	480	355	375	652	1,085
Total tax paid	(73)	(21)	(21)	(143)	(239)
Depreciation	73	79	127	245	368
Working capital changes	(528)	131	(212)	(1,016)	(1,423)
<b>Net cash from operations</b>	<b>(48)</b>	<b>544</b>	<b>270</b>	<b>(262)</b>	<b>(209)</b>
<b>Cash from investments</b>					
Capital expenditure	(831)	(1,364)	(1,816)	(2,712)	(3,080)
Investments and others	(7)	(6)	(382)	-	-
<b>Net cash from investments</b>	<b>(838)</b>	<b>(1,370)</b>	<b>(2,198)</b>	<b>(2,712)</b>	<b>(3,080)</b>
<b>Cash from financing</b>					
Equity raised/(repaid)	-	(5)	-	-	-
Debt raised/(repaid)	898	674	1,884	2,882	3,300
Dividend (incl. tax)	-	-	-	-	-
Others (incl extraordinary)	126	136	229	(222)	0
<b>Net cash from financing</b>	<b>1,024</b>	<b>804</b>	<b>2,113</b>	<b>2,660</b>	<b>3,300</b>
Change in cash position	139	(21)	185	(315)	11
Closing cash	215	194	379	64	75

### Quarterly financials

(Rs Mn)	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11
<b>Net Sales</b>	<b>912</b>	<b>972</b>	<b>1,236</b>	<b>1,071</b>	<b>989</b>
Change (q-o-q)	NM	7%	27%	-13%	-8%
<b>EBITDA</b>	<b>133</b>	<b>171</b>	<b>262</b>	<b>209</b>	<b>234</b>
Change (q-o-q)	NM	29%	53%	-20%	12%
<b>EBITDA margin</b>	<b>14.6%</b>	<b>17.6%</b>	<b>21.2%</b>	<b>19.5%</b>	<b>23.7%</b>
<b>PAT</b>	<b>56</b>	<b>81</b>	<b>147</b>	<b>86</b>	<b>110</b>
<b>Adj PAT</b>	<b>56</b>	<b>81</b>	<b>147</b>	<b>86</b>	<b>110</b>
Change (q-o-q)	NM	45%	81%	-41%	28%
<b>Adj PAT margin</b>	<b>6.1%</b>	<b>8.3%</b>	<b>11.9%</b>	<b>8.1%</b>	<b>11.2%</b>
<b>Adj EPS</b>	<b>1.0</b>	<b>1.4</b>	<b>2.5</b>	<b>1.5</b>	<b>1.9</b>

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