



# CRISIL IER

Independent Equity Research

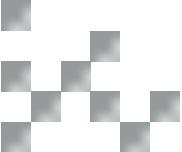
## MSP Steel and Power Ltd

**Q4FY12 Result Update**

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Enhancing investment decisions

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## 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 (negative 10-25% from CMP)
1/5	Poor fundamentals	1/5	Strong downside (<-25% from CMP)

### About CRISIL Limited

CRISIL is a global analytical company providing ratings, research, and risk and policy advisory services. We are India's leading ratings agency. We are also the foremost provider of high-end research to the world's largest banks and leading corporations.

### About CRISIL Research

CRISIL Research is India's largest independent and integrated research house. We provide insights, opinions, and analysis on the Indian economy, industries, capital markets and companies. We are India's most credible provider of economy and industry research. Our industry research covers 70 sectors and is known for its rich insights and perspectives. Our analysis is supported by inputs from our network of more than 4,500 primary sources, including industry experts, industry associations, and trade channels. We play a key role in India's fixed income markets. We are India's largest provider of valuations of fixed income securities, serving the mutual fund, insurance, and banking industries. We are the sole provider of debt and hybrid indices to India's mutual fund and life insurance industries. We pioneered independent equity research in India, and are today India's largest independent equity research house. Our defining trait is the ability to convert information and data into expert judgments and forecasts with complete objectivity. We leverage our deep understanding of the macro economy and our extensive sector coverage to provide unique insights on micro-macro and cross-sectoral linkages. We deliver our research through an innovative web-based research platform. Our talent pool comprises economists, sector experts, company analysts, and information management specialists.

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**Last updated: 30 April, 2012**

### 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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High operating profit boosts PAT despite high interest cost

Fundamental Grade	2/5 (Moderate fundamentals)
Valuation Grade	5/5 (CMP has strong upside)
Industry	Metals & Mining

MSP Steel and Power Ltd's (MSP's) Q4FY12 earnings were below CRISIL Research's expectations. However, revenue growth of 7% q-o-q and EBITDA margin of 18.3% were largely in line. Growth was largely driven by increase in blended realisation of steel and sponge iron. PAT margin was adversely impacted due to high interest cost on account of increase in working capital. Going forward, we believe margins will improve as the company ramps up production at the newly commissioned pellet capacity. Also, considering the current weak demand of steel and better margins in pellet sales, the company has decided to expand steel capacity instead of the sponge iron plant. Factoring in the same, we have lowered our revenue and earnings estimates for FY13. We have introduced FY14 estimates. We maintain our fundamental grade of 2/5.

#### Q4FY12 result analysis (standalone)

- Revenues grew by 6.6% q-o-q and 16.8% y-o-y to Rs 1,864 mn primarily on account of increase in blended realisation of sponge and steel, which grew by 6% q-o-q and 11% y-o-y to Rs 31,300 per tonne. Sequentially, MSP reported an increase of 12% in sales volume (sponge + steel). But nil trading sales in the quarter offset its effect on revenues. Yearly, metal sales remained flat but higher power sales added to total sales.
- EBITDA margin improved by 305 bps q-o-q and 169 bps y-o-y to 18.3%. Other expenses surged on account of higher freight cost. To push the sales, the company sold structural steel from a newly opened depot.
- Interest and finance charges increased 33% q-o-q (up 210% y-o-y) to Rs 179 mn primarily on account of increased working capital as the company has piled up inventory for its newly commissioned pellet plant.
- Following the growth in operating profit, PAT grew 43% q-o-q (down 37% y-o-y due to increase in interest cost) to Rs 72 mn.
- Accordingly, EPS was Rs 1.25 as against Rs 0.87 in Q3FY12 and Rs 1.99 in Q4FY11.

#### Change in estimates

In light of the current weak demand scenario, the company has decided to expand steel capacity (billet and SMS) instead of sponge iron capacity. Earlier, we had assumed the sponge iron plant will come on stream in June-July 2012 and contribute to sales for the three quarters in FY13. Now, we factor in the change in capex plan and a weak demand scenario and lower our revenue and PAT estimates for FY13 by 20% and 26%, respectively. We have introduced FY14 estimates.

#### Valuation: Current market price has a strong upside

We roll forward our valuation to FY14 and lower our fair value to Rs 49 per share. At the current market price of Rs 28, the valuation grade is 5/5.

#### KEY FORECAST

(Rs mn)	FY10	FY11	FY12#	FY13E	FY14E
Operating income	3,959	5,079	6,963	9,952	11,245
EBITDA	701	1,068	1,161	2,039	2,373
Adj Net income	314	496	260	656	762
Adj EPS-Rs	5.4	8.5	4.5	9.6	11.2
EPS growth (%)	16.8	58.3	(47.5)	114.8	16.2
Dividend Yield (%)	-	3.6	0.9	3.6	3.6
RoCE (%)	10.2	10.7	8.3	12.8	14.6
RoE (%)	16.0	21.2	9.4	18.5	17.7
P/E (x)	5.2	3.3	6.3	2.9	2.5
P/BV (x)	0.7	0.7	0.5	0.5	0.4
EV/EBITDA (x)	7.8	8.0	8.5	5.1	4.1

NM: Not meaningful; CMP: Current market price # based on abridged financials

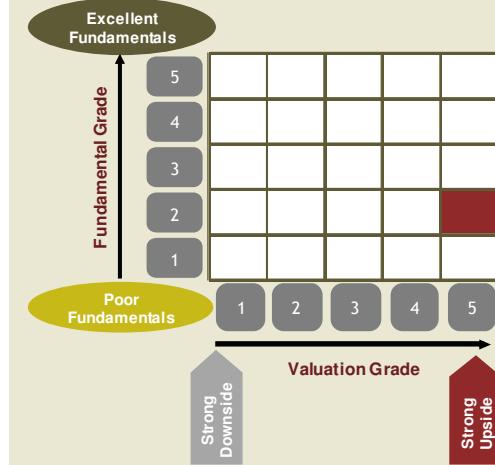
Source: Company, CRISIL Research estimates

June 20, 2012

Fair Value Rs 49

CMP Rs 28

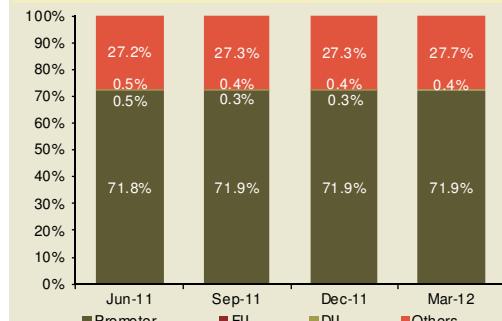
#### CFV MATRIX



#### KEY STOCK STATISTICS

NIFTY/SENSEX	5104/16860
NSE/BSE ticker	MSPL / MSPSTEEL
Face value (Rs per share)	10
Shares outstanding (mn)	58
Market cap (Rs mn)/(US\$ mn)	1,627/29
Enterprise value (Rs mn)/(US\$ mn)	9,857/177
52-week range (Rs)/(H/L)	62/26
Beta	1.4
Free float (%)	28%
Avg daily volumes (30-days)	11,745
Avg daily value (30-days) (Rs mn)	0.34

#### SHAREHOLDING PATTERN



#### PERFORMANCE VIS-À-VIS MARKET

	Returns			
	1-m	3-m	6-m	12-m
MSP	-3%	-13%	-6%	-42%
NIFTY	4%	-4%	8%	-6%

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**Q4FY12 Result Summary**

(Rs mn)	Q4FY12	Q3FY12	Q4FY11	q-o-q (%)	y-o-y (%)	FY12*	FY11*	y-o-y (%)
<b>Net sales</b>	<b>1,864</b>	<b>1,749</b>	<b>1,595</b>	<b>6.6</b>	<b>16.8</b>	<b>6,963</b>	<b>5,079</b>	<b>37.1</b>
(Increase)/decrease in stock in trade and WIP	(90)	(91)	(75)	(1.3)	19.4	(180)	(269)	(32.9)
Consumption of Raw Materials	1,282	1,109	1,068	15.6	20.0	4,612	3,395	35.8
Purchase of traded goods	0	201	0	(100.0)	NM	580	349	66.0
Raw materials cost (% of net sales)	64.0%	69.7%	62.3%	(577) bps	168 bps	72.0%	68.4%	353 bps
Employees cost	43	47	46	(9.5)	(6.7)	184	153	20.0
Other expenses	288	215	291	33.6	(1.1)	607	382	58.8
<b>EBITDA</b>	<b>341</b>	<b>267</b>	<b>265</b>	<b>27.9</b>	<b>28.8</b>	<b>1,161</b>	<b>1,068</b>	<b>8.8</b>
<b>EBITDA margin</b>	<b>18.3%</b>	<b>15.3%</b>	<b>16.6%</b>	<b>305 bps</b>	<b>169 bps</b>	<b>16.7%</b>	<b>21.0%</b>	<b>(434) bps</b>
Depreciation	75	72	67	4.2	12.5	291	193	50.5
<b>EBIT</b>	<b>266</b>	<b>195</b>	<b>198</b>	<b>36.6</b>	<b>34.3</b>	<b>871</b>	<b>874</b>	<b>(0.4)</b>
Interest and finance charges	179	134	58	33.4	209.7	586	248	136.5
Operating PBT	87	61	140	43.6	(37.9)	285	627	(54.6)
Other Income	16	12	28	30.0	(44.4)	52	39	35.0
Extraordinary Income/(expense)	-	(0.2)	0	(100)	NM	-	6	(100.0)
<b>PBT</b>	<b>103</b>	<b>72</b>	<b>168</b>	<b>41.7</b>	<b>(39.0)</b>	<b>337</b>	<b>671</b>	<b>(49.8)</b>
Tax	30	22	53	39.4	(42.5)	77	169	(54.7)
<b>PAT</b>	<b>72</b>	<b>51</b>	<b>116</b>	<b>42.7</b>	<b>(37.3)</b>	<b>260</b>	<b>502</b>	<b>(48.2)</b>
<b>Adj PAT</b>	<b>72</b>	<b>51</b>	<b>116</b>	<b>42.7</b>	<b>(37.3)</b>	<b>260</b>	<b>496</b>	<b>(47.6)</b>
<b>Adj PAT margin</b>	<b>3.9%</b>	<b>2.9%</b>	<b>7.2%</b>	<b>98 bps</b>	<b>-336 bps</b>	<b>3.7%</b>	<b>9.8%</b>	<b>(604) bps</b>
No of equity shares (mn)	58.1	58.1	58.1	-	-	58.1	58.1	-
<b>Adj EPS (Rs)</b>	<b>1.25</b>	<b>0.87</b>	<b>1.99</b>	<b>42.7</b>	<b>(37.3)</b>	<b>4.5</b>	<b>8.5</b>	<b>(47.6)</b>

\*Yearly financials has been reclassified as per CRISIL standards

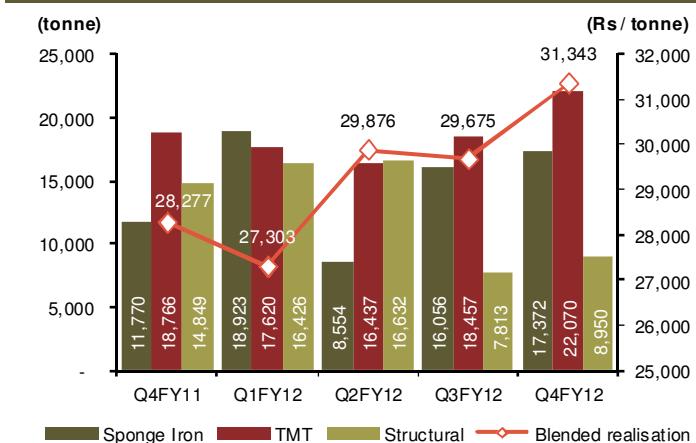
Source: Company, CRISIL Research

**Standalone FY12 financials – estimates vs. actuals**

(Rs mn)	FY12E	FY12A	Variation
Net Sales	7,066	6,963	-1.5%
<b>EBITDA</b>	<b>1,182</b>	<b>1,161</b>	<b>-1.7%</b>
EBITDA margin	16.7%	16.7%	(4) bps
Depreciation	297	291	-2.1%
<b>EBIT</b>	<b>885</b>	<b>871</b>	<b>-1.6%</b>
Interest and finance charges	568	586	3.0%
<b>PAT</b>	<b>286</b>	<b>260</b>	<b>-8.9%</b>
<b>PAT margin</b>	<b>4.0%</b>	<b>3.7%</b>	<b>(31) bps</b>
<b>EPS</b>	<b>4.9</b>	<b>4.5</b>	<b>-8.9%</b>

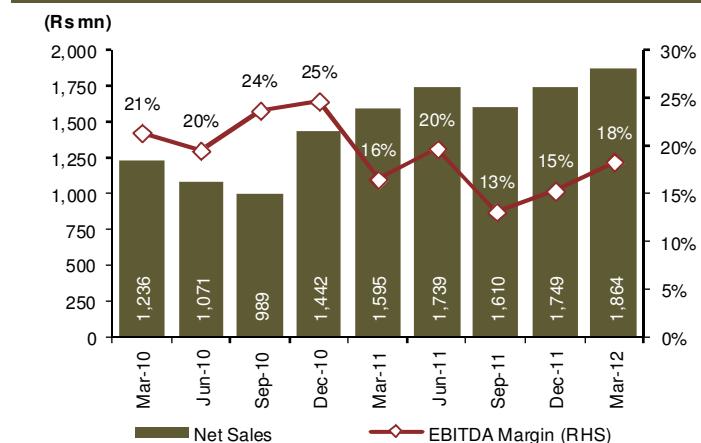
Source: CRISIL Research

## Increase in realisation supported revenue growth



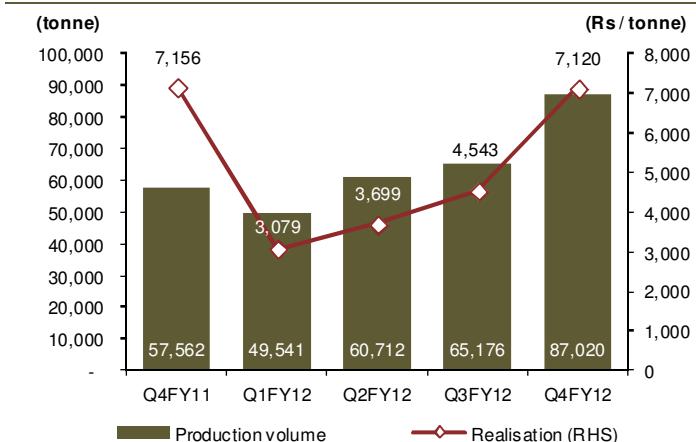
Source: Company, CRISIL Research

## Net sales and EBITDA margin trend



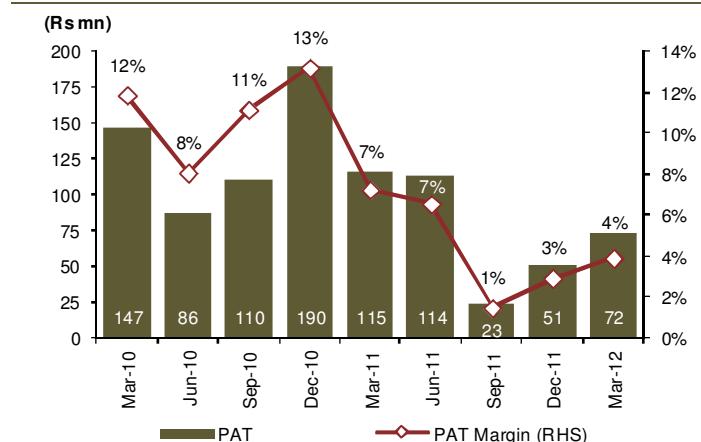
Source: Company, CRISIL Research

## Increase in pellet production...



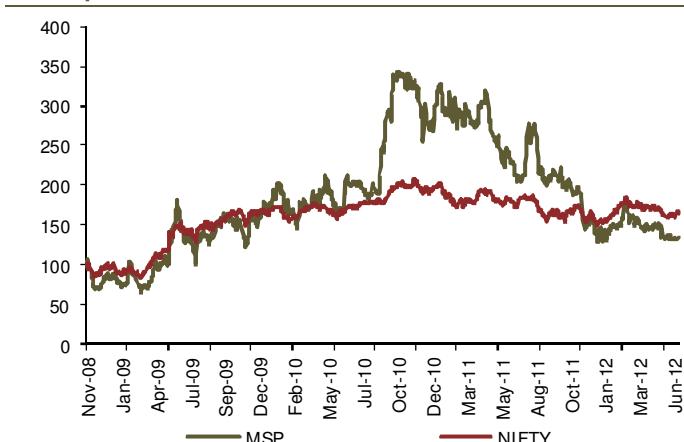
Source: Company, CRISIL Research

## ... supported PAT margin



Source: Company, CRISIL Research

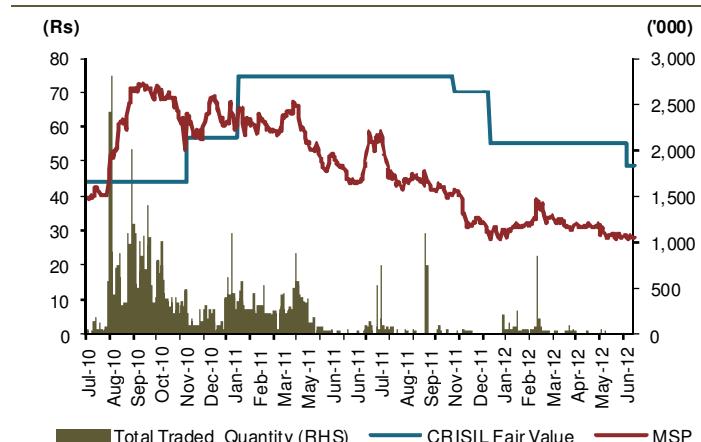
## Share price movement



-Indexed to 100

Source: NSE, CRISIL Research

## Fair value movement since initiation

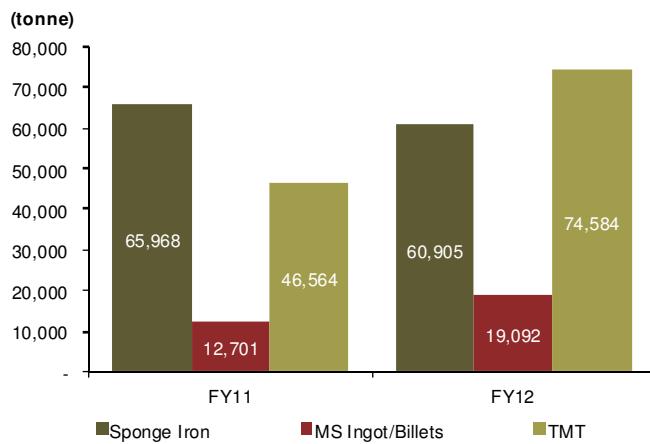


Source: NSE, BSE, CRISIL Research

## FY12 result analysis

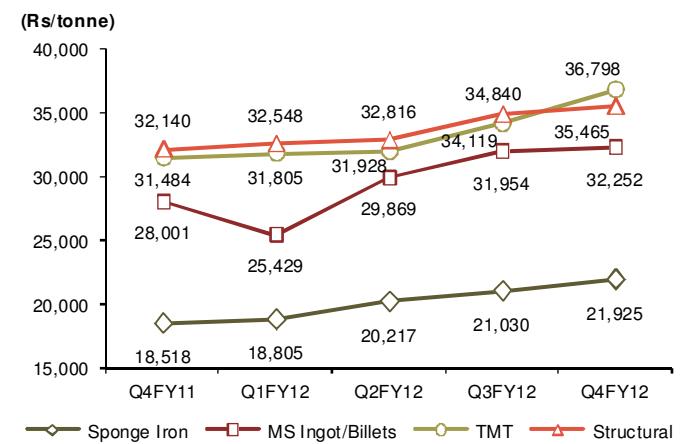
**Net sales:** Increased by 37% to Rs 6,963 mn. Higher volume sales, on account of increased capacity utilisation, and increase in blended realisation (sponge + steel) fuelled growth.

### Increase in sales volume...



Source: Company, CRISIL Research

### ... and increase in realisation drove revenue growth



Source: Company, CRISIL Research

**EBITDA margin:** EBITDA margin contracted by 434 bps to 16.7%. The increase in price of iron ore fines and higher other expenses led to the contraction. To push sales in a bleak demand scenario the company opened a sales depot to sell structural steel directly to end consumers. Because of this, it had to incur freight costs which increased its other expenses.

**PAT margin:** PAT margin contracted by 604 bps to 3.7% due to higher interest cost (increased 136% to Rs 586 mn). The company capitalised the sponge iron plant and coal washery in FY11 due to which its interest and depreciation cost increased in FY12. Also, higher working capital requirement in Q4FY12, due to the company's strategy of increasing its iron ore fine inventory, has put additional pressure on profitability.

## Status on capacity expansion

**Sponge Iron:** The company has cancelled the phase - II (1.15 lakh tonne) expansion of the sponge iron plant. However, it is on track to expand its steel capacity (Billet and SMS) by 1.27 lakh tonne to become an integrated steel player. The total cost of this expansion is Rs 1,300 mn, out of which the company has already spent ~Rs 600 mn in FY12. Once the upcoming steel capacity runs at optimum utilisation, the company will stop selling sponge iron in the market and will consume it to produce steel. We have assumed that the capacity will come on stream in FY13-end.

**Pellet plant:** In March 2012, MSP commissioned 0.6 mn MTPA pellet capacity, taking the total capacity to 0.9 mn MTPA. Given the high iron ore prices and expansion in capacity, we believe the company is poised to benefit from the existing price differential between iron ore and pellets. As per the company, the cost of conversion of fines to pellet was Rs 4,944 per tonne in Q4FY12 which provides a contribution margin of Rs 2,556 per tonne, considering the selling price of Rs 7,500 per tonne. We believe the company will focus on running the pellet capacity at optimum utilisation level; we have assumed 70% and 75% utilisation rate for FY13 and FY14, respectively.

## Earnings estimates revised downwards

Particulars	Unit	FY13E			FY14E
		Old	New	% change	
Revenues	(Rs mn)	12,516	10,018	-20.0%	11,335
EBITDA	(Rs mn)	2,384	2,041	-14.4%	2,436
EBITDA margin	%	19.0%	20.4%	133 bps	21.5%
PAT	(Rs mn)	737	542	-26.4%	707
PAT margin	%	5.9%	5.4%	(48) bps	6.2%
EPS	Rs	12.7	8.0	-37.2%	10.4

Source: CRISIL Research estimate

## Reasons for changes in estimates

To factor in the change in capacity expansion plan, we have reduced our revenue estimates by 20% for FY13. Earlier, we had assumed sponge iron plant will come on stream by July 2012 and will contribute to sales for three quarters in FY13. We increase our EBITDA margin estimate by 133 bps to 20.4% in FY13, as the company will now sell high-margin pellets in the market. The total requirement of pellets (as raw material for sponge iron) in FY13 will be ~0.6 mn tonne (considering 70% utilisation rate for the sponge iron plant), which would leave the company with ~0.3 mn tonne excess pellets.

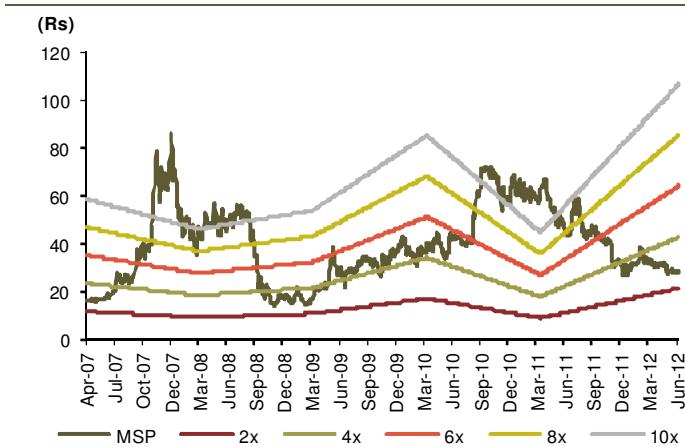
The expansion in EBITDA margin estimate has been more than offset by the decline in sales estimate, resulting in the reduction of EBITDA estimate by 14% to Rs 2,384 mn. PAT estimate is also revised downwards in line with EBITDA estimate. EPS decline will be higher than the PAT decline, as we factor in the share dilution. The company plans to issue 10 mn shares to the promoters at Rs 60 per share.

## Valuation

Grade: 5/5

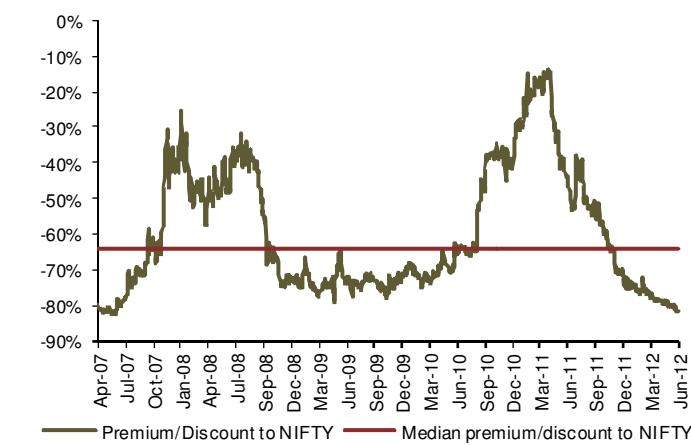
We continue to use the EV/EBITDA multiple method to value MSP. We roll forward our projections by one year to FY14 and incorporate the change in the capacity expansion plan. We assign EV/EBITDA multiple of 5x FY14E EBITDA of Rs 2,373 mn and lower our fair value to Rs 49 per share. At current market price of Rs 28 per share, the valuation grade is 5/5.

### One-year forward P/E band



Source: NSE, CRISIL Research

### P/E – premium / discount to NIFTY

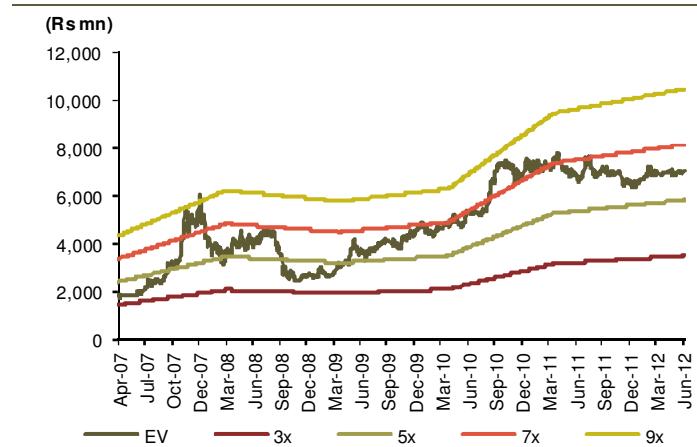


Source: NSE, CRISIL Research

### CRISIL IER reports released on MSP Steel and Power Ltd

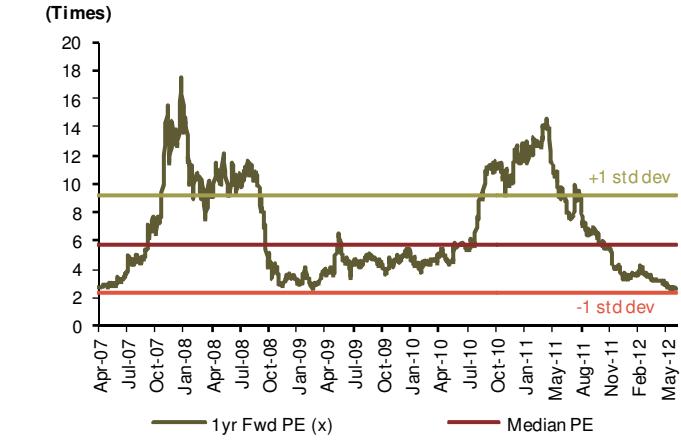
Date	Nature of report	Fundamental grade	Fair value	Valuation grade	CMP (on the date of report)
29-Jul-10	Initiating coverage	2/5	Rs 44	3/5	Rs 40
01-Dec-10	Q2FY11 result update	2/5	Rs 57	3/5	Rs 61
03-Feb-11	Q3FY11 result update	2/5	Rs 75	4/5	Rs 62
21-Jun-11	Q4FY11 result update	2/5	Rs 75	5/5	Rs 45
12-Aug-11	Q1FY12 result update	2/5	Rs 75	5/5	Rs 47
02-Nov-11	Detailed report*	2/5	Rs 70	5/5	Rs 42
19-Dec-11	Q2FY12 result update	2/5	Rs 55	5/5	Rs 30
21-Feb-12	Q3FY12 result update	2/5	Rs 55	5/5	Rs 38
20-June-12	Q4FY12 result update	2/5	Rs 49	5/5	Rs 28

### One-year forward EV/EBITDA band



Source: NSE, CRISIL Research

### P/E movement



Source: NSE, CRISIL Research

## Annexure: Financials

Income statement					Balance Sheet						
(Rs mn)	FY10	FY11	FY12#	FY13E	(Rs mn)	FY10	FY11	FY12#	FY13E	FY14E	
<b>Operating income</b>	3,959	5,079	6,963	9,952	11,245	<b>Liabilities</b>					
EBITDA	701	1,068	1,161	2,039	2,373	Equity share capital	581	581	581	681	
<b>EBITDA margin</b>	17.7%	21.0%	16.7%	20.5%	21.1%	Reserves	1,654	1,859	2,528	3,286	
Depreciation	127	193	291	491	500	Minorities	-	-	-	-	
<b>EBIT</b>	573	874	871	1,548	1,873	<b>Net worth</b>	2,235	2,440	3,109	3,967	
Interest	205	248	586	744	937	Preference Share capital	-	760	772	835	
<b>Operating PBT</b>	368	627	285	804	936	Other debt	4,611	7,055	8,303	8,803	
Other income	7	39	52	70	79	<b>Total debt</b>	4,611	7,814	9,075	9,637	
Exceptional inc/(exp)	7	6	-	-	-	Deferred tax liability (net)	199	334	381	381	
<b>PBT</b>	382	671	337	874	1,015	<b>Total liabilities</b>	7,044	10,588	12,565	13,985	
Tax provision	62	169	76	219	254	<b>Assets</b>					
Minority interest	-	-	-	-	-	Net fixed assets	2,559	4,999	4,958	8,477	
<b>PAT (Reported)</b>	321	502	260	656	762	Capital WIP	2,454	3,419	5,166	1,856	
Less: Exceptionals	7	6	-	-	-	<b>Total fixed assets</b>	5,013	8,418	10,124	10,333	
<b>Adjusted PAT</b>	314	496	260	656	762	<b>Investments</b>	70	74	324	324	
Ratios					Current assets						
	FY10	FY11	FY12#	FY13E	FY14E	Inventory	683	1,209	2,101	2,590	
<b>Growth</b>						Sundry debtors	669	424	460	763	
Operating income (%)	(2.0)	28.3	37.1	42.9	13.0	Loans and advances	500	1,081	1,526	1,194	
EBITDA (%)	9.0	52.4	8.8	75.5	16.4	Cash & bank balance	379	103	72	264	
Adj PAT (%)	16.8	58.3	(47.5)	151.8	16.2	Marketable securities	380	-	-	-	
Adj EPS (%)	16.8	58.3	(47.5)	114.8	16.2	<b>Total current assets</b>	2,611	2,816	4,159	4,812	
<b>Profitability</b>						<b>Total current liabilities</b>	649	720	2,042	1,484	
EBITDA margin (%)	17.7	21.0	16.7	20.5	21.1	<b>Net current assets</b>	1,962	2,097	2,117	3,328	
Adj PAT Margin (%)	7.9	9.8	3.7	6.6	6.8	<b>Total assets</b>	7,044	10,588	12,565	13,985	
RoE (%)	16.0	21.2	9.4	18.5	17.7	<b>Cash flow</b>					
RoCE (%)	10.2	10.7	8.3	12.8	14.7	(Rs mn)	FY10	FY11	FY12#	FY13E	FY14E
RoIC (%)	10.0	10.0	8.8	12.7	14.7	Pre-tax profit	375	665	337	874	1,015
<b>Valuations</b>						Total tax paid	(21)	(34)	(29)	(219)	(254)
Price-earnings (x)	5.2	3.3	6.2	2.9	2.5	Depreciation	127	193	291	491	500
Price-book (x)	0.7	0.7	0.5	0.5	0.4	Working capital changes	(212)	(790)	(51)	(1,019)	(318)
EV/EBITDA (x)	7.8	8.0	8.5	5.1	4.0	<b>Net cash from operations</b>	270	35	547	127	944
EV/Sales (x)	1.5	1.9	1.4	1.1	0.9	<b>Cash from investments</b>					
Dividend payout ratio (%)	-	11.8	5.6	10.4	8.9	Capital expenditure	(1,816)	(3,598)	(1,997)	(700)	(0)
Dividend yield (%)	-	3.6	0.9	3.6	3.6	Investments and others	(382)	376	(250)	-	-
<b>B/S ratios</b>						<b>Net cash from investments</b>	(2,198)	(3,222)	(2,247)	(700)	(0)
Inventory days	77	112	132	119	114	<b>Cash from financing</b>					
Creditors days	72	60	124	64	64	Equity raised/(repaid)	-	679	-	100	-
Debtor days	61	34	24	27	29	Debt raised/(repaid)	1,884	2,519	1,260	562	(800)
Working capital days	101	115	106	94	105	Dividend (incl. tax)	-	(69)	(17)	(80)	(80)
Gross asset turnover (x)	1.5	1.2	1.2	1.3	1.1	Others (incl. extraordinary)	229	(216)	425	182	(1)
Net asset set turnover (x)	1.6	1.3	1.4	1.5	1.3	<b>Net cash from financing</b>	2,113	2,913	1,669	765	(881)
Sales/operating assets (x)	0.9	0.8	0.8	1.0	1.1	Change in cash position	185	(275)	(32)	192	63
Current ratio (x)	4.0	3.9	2.0	3.2	3.2	Closing cash	379	103	72	264	327
Debt-equity (x)	2.1	2.2	2.1	1.8	1.7	<b>Quarterly financials</b>					
Net debt/equity (x)	1.7	2.2	2.1	1.8	1.4	(Rs mn)	Q4FY11	Q1FY12	Q2FY12	Q3FY12	Q4FY12
Interest coverage	2.8	3.5	1.5	2.1	2.0	<b>Net Sales</b>	1,595	1,739	1,610	1,749	1,864
Per share						<b>Change (q-o-q)</b>	11%	9%	-7%	9%	7%
	FY10	FY11	FY12#	FY13E	FY14E	<b>EBITDA</b>	263	343	211	267	341
Adj EPS (Rs)	5.4	8.5	4.5	9.6	11.2	<b>Change (q-o-q)</b>	-26%	30%	-39%	27%	28%
CEPS	7.6	11.9	9.5	16.8	18.5	<b>EBITDA margin</b>	16.5%	19.7%	13.1%	15.3%	18.3%
Book value	38.5	42.0	53.5	58.3	68.3	<b>PAT</b>	115	114	23	51	72
Dividend (Rs)	-	1.0	0.25	1.0	1.0	<b>Adj PAT</b>	115	114	23	51	72
Actual o/s shares (mn)	58.1	58.1	58.1	68.1	68.1	<b>Change (q-o-q)</b>	-39%	-2%	-79%	116%	43%
						<b>Adj PAT margin</b>	7.2%	6.5%	1.5%	2.9%	3.9%
						<b>Adj EPS</b>	2.0	2.0	0.4	0.9	1.2

**Note:** FY12 Financials are not strictly comparable with that of the previous years due to the new format of disclosure under Schedule VI of the Companies Act

**Source:** CRISIL Research

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