

## Metals &amp; Mining

## Visit Note

## Chhattisgarh: Steeling march to Power

We recently undertook a week-long visit of Chhattisgarh state, located in north central India, to get a visual feel of its rich iron ore, coal and water resources. We have higher conviction on Jindal Steel & Power (JSPL), which we have upgraded to Buy, and are more convinced on Sarda Energy & Minerals (SEML) as well, where we reiterate Buy. We were not impressed by Monnet Ispat and retain our Sell rating. We also visited Prakash Industries & Godawari Power (Not Rated).

- **Chhattisgarh – An emerging power hub:** The state government has signed memorandum of understanding (MoUs) with several steel and power companies to set up power projects. If all these MoUs are actually implemented, an additional 22,000MW of power-generation capacity would be created in the state within a decade.
- **Unique model – steel and power:** Further, most companies operating steel plants in the state have also set-up captive power plants. This model has helped de-risk their business from the volatility associated with steel prices. Power is a low-risk stable business that provides a steady stream of revenues and profits over decades.
- **State to benefit from new mining policy:** Chhattisgarh, along with other mineral-rich states, would benefit from the new mining policy as it would earn more royalty which would be decided on the basis of the market price vs fixed basis previously.
- **Jindal Steel & Power (JSPL) – Upgraded to Buy:** We have upgraded the stock to Buy (from Hold) as we believe its fully-integrated business model and increasing contribution from merchant power would boost profits and margins. Besides, Jindal Power's (a 100% subsidiary) IPO is also expected to boost valuations.
- **Sarda Energy & Minerals (SEML) – Reiterate Buy:** The commissioning of a pellet unit is likely to ensure healthy margins. At CMP, the stock trades at 8x FY10E and 3.6x FY11E earnings and 8.6x FY10E and 4x FY11E EV/EBITDA. We value the stock at 7x FY11E EBITDA and reiterate our Buy rating.
- **Monnet Ispat – Sell:** We believe current valuations (6.8x FY10E EV/EBITDA and 9.1x FY11E) is expensive. We reiterate our Sell rating.
- **Positive bias on Prakash Industries:** We have a positive bias on Prakash Industries (Not Rated) given its volume expansion and margin improvement due to captive resources and foray into merchant power. Godawari Power & Ispat (Not Rated) suffers from poor visibility of growth in future in the absence of projects.

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## Key Data

## Jindal Steel &amp; Power

Bloomberg Code	JSP IN
Reuters Code	JNSP.BO
Current Shares O/S (mn)	924
Diluted Shares O/S(mn)	924
Mkt Cap (Rsbn/USDbn)	585.8/12.2
52 Wk H / L (Rs)	667/86
Daily Vol. (3M NSE Avg.)	871,677
Face Value (Rs)	1

## Sarda Energy &amp; Minerals

Bloomberg Code	SEML IN
Reuters Code	SAEM.BO
Current Shares O/S (mn)	34
Diluted Shares O/S(mn)	34
Mkt Cap (Rsbn/USDmn)	5.1/106.6
52 Wk H / L (Rs)	224/50
Daily Vol. (3M NSE Avg.)	39,323
Face Value (Rs)	10

## Monnet Ispat &amp; Energy

Bloomberg Code	MISP IN
Reuters Code	MNET.BO
Current Shares O/S (mn)	48
Diluted Shares O/S(mn)	57
Mkt Cap (Rsbn/USDmn)	17.4/361.9
52 Wk H / L (Rs)	514/111
Daily Vol. (3M NSE Avg.)	105,256
Face Value (Rs)	10

## Prakash Industries

Bloomberg Code	PKI IN
Reuters Code	PRKI.BO
Current Shares O/S (mn)	115.5
Diluted Shares O/S(mn)	115.5
Mkt Cap (Rsbn/USDmn)	18.8/390.5
52 Wk H / L (Rs)	165/32
Daily Vol. (3M NSE Avg.)	333,910
Face Value (Rs)	10

## Godawari Power &amp; Ispat

Bloomberg Code	GODPI IN
Reuters Code	GDPI.BO
Current Shares O/S (mn)	28.1
Diluted Shares O/S(mn)	28.1
Mkt Cap (Rsbn/USDmn)	4.1/85.5
52 Wk H / L (Rs)	166/39
Daily Vol. (3M NSE Avg.)	192,987
Face Value (Rs)	10

1 USD = Rs48.1

Source: Bloomberg, Centrum Research  
\*as on 18 Sep 2009

Company	Rating	Mkt Cap (Rsbn)	CMP (Rs)	Target Price (Rs)	FY10E (x)			FY11E (x)		
					P/E	EV/EBITDA	P/BV	P/E	EV/EBITDA	P/BV
Jindal Steel & Power	Buy	585.8	634	752	17.1	11.6	5.7	12.8	8.9	3.9
Sarda Energy & Mineral	Buy	5.1	151	290	8.0	8.6	0.9	3.6	4.0	0.7
Monnet Ispat & Energy	Sell	17.4	363	280	6.4	6.8	0.9	7.6	9.1	0.8

Source: Company, Centrum Research Estimates

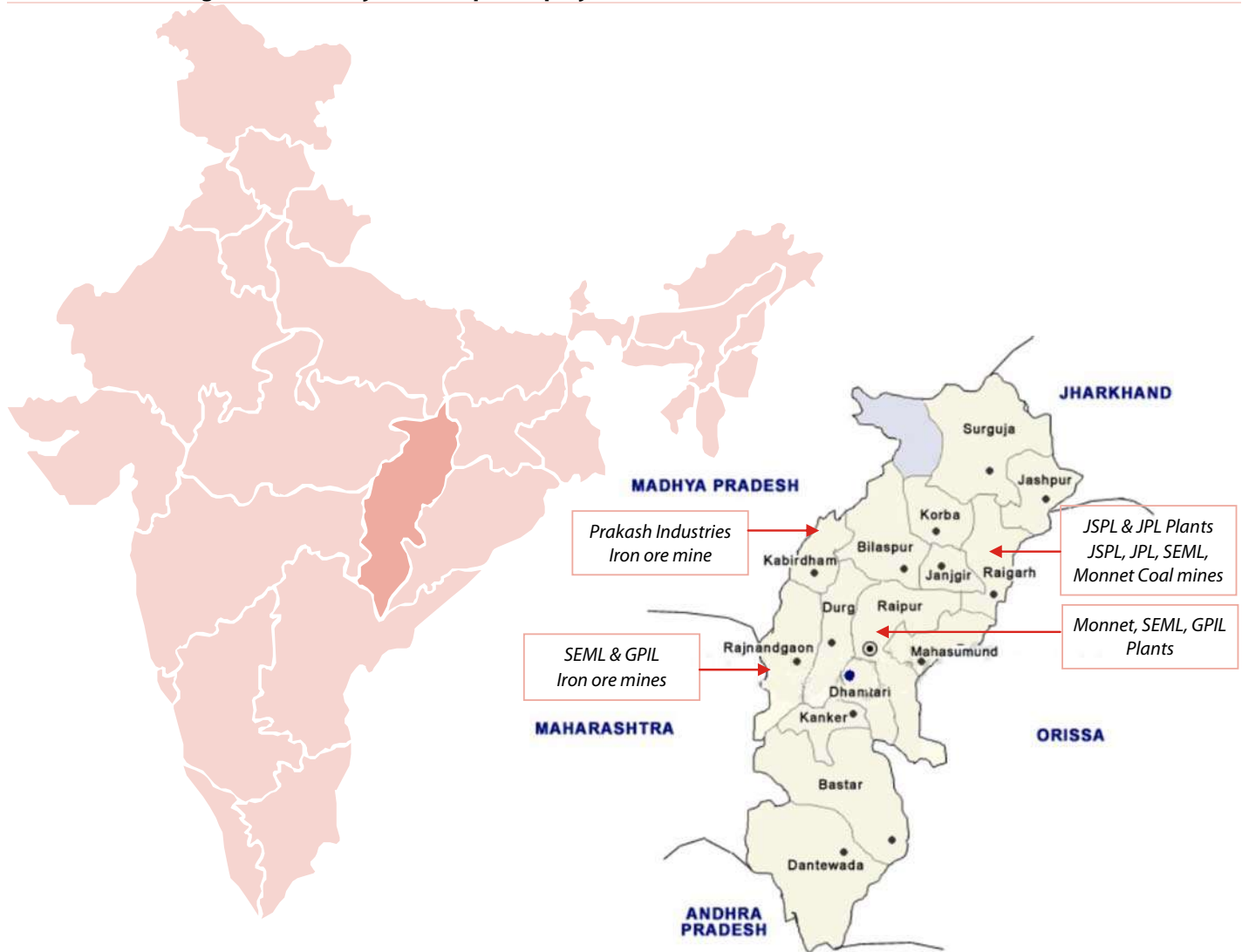
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## Chhattisgarh – An emerging power hub

We recently visited Chhattisgarh and returned convinced that the state, endowed with rich natural resources like iron ore, coal and water, is an ideal destination for steel and power projects. There is great scope for private participation in the mining sector in Chhattisgarh. The state government has created a conducive business environment to attract private investment, both domestic and international. The added advantage is availability of large technically qualified human resources. We visited the plants and facilities of Jindal Steel & Power (JSPL), Sarda Energy & Minerals (SEML), Godawari Power & Ispat (GPIL), Prakash Industries and Monnet Ispat.

**Exhibit 1: Chhattisgarh- Site of major steel & power projects**



Source: Google, Centrum Research

The state government has signed MoUs with several various steel and power companies to set up power projects. If all the MoUs are actually implemented, an additional 22,000 MW of power capacity would be created within a decade.

### Exhibit 2: Major companies setting up power plants in Chhattisgarh

Company	Project cost (Rsbn)
Bhushan Power & Steel	40
Bhushan Steel	10
Chhattisgarh Energy	53
Chhattisgarh Gujarat Power Generation	20
Chhattisgarh State Electricity Board	49
Chhattisgarh State Power Generation	55
Essar Power	86
Godawari Energy	40
Indiabulls Power Generation	80
Jai Balaji Industries.	24
Jindal India Thermal Power	52
Jindal Power	145
Jindal Steel & Power	183
Karnataka Power Corporation	60
Korba West Power	24
NTPC	348
NTPC-Sail Power Co	27
Prakash Industries	25
Sarda Energy & Minerals	52
Sterlite Energy	48
Tata Power	50
Torrent Power	40
Visa Power	50

Source: CMIE, Centrum Research

India faces a peak-hour power deficit of 12.6%, according to the Central Electricity Authority (CEA). The Central government plans to spend Rs569.6bn to set up additional power plants and transmission lines during the 11<sup>th</sup> Five-Year plan (2007-12). The Central government has set a target of adding 78,700 MW of generation capacity over 2007-12 and 100,000 MW during the next five years (2012-17).

### Unique business model – steel and power

Most companies operating steel plants in the state have also set-up captive power plants. This model has helped de-risk their business from the volatility associated with steel prices (steel prices are influenced by global supply-demand equations and directly impact profitability of producers). Power is a low-risk stable business that provides a steady stream of revenues and profits over decades.

The manufacturing of steel and ferro-alloys is highly-energy intensive process. For instance, producing 1 tonne of ferro-alloys requires about 4,000 units of electricity. So power is major cost constituting about 25% of total cost. When demand for ferro-alloys slackens, companies can cut back or totally stop production and divert power for merchant sales. This helps in stabilizing revenues, and could even improve average margins. Due to the high consumption of power and volatility of input prices, we believe companies with captive resources (iron ore, coal and power) are better placed. For such companies, the volatility associated with steel prices is offset by steady returns from the power business.

In Chhattisgarh, most of the small and medium-sized steel companies like SEML, GPIL, Monnet, Prakash, etc, also produce ferro alloys. Profits from ferro alloys was high till prices of raw materials like manganese ore were low at about Rs4,000-5,000/tonne and product prices were about Rs35,000-36,000/tonne, but after Sept-Oct 2008, prices of ferro alloys declined sharply from peak of Rs100,000/tonne to less than Rs50,000/tonne, but raw material prices remained firmer at about Rs20,000/tonne.

We observed that most steel manufacturers had cut back production of both steel and ferro alloys due to depressed prices. Now, with prices looking up again, these companies have started increasing production. It is the flexibility of this model (steel and power) that gives companies the much-needed stability in margins and earnings as they can switch from power to steel and ferro alloys and back to power depending on pricing.

### Steel industry – A perfect example of recycling

The steel industry is very efficient in recycling even so-called waste. For example, a coal-based sponge iron-based steel plant consumes about 1.3 tonnes of coal to produce 1 tonne of steel. The coal is used as a reducing agent (reduces oxygen from iron ore) rather as fuel which in turn generates heat and gases like carbon monoxide which is then recycled to heat water to generate steam and ultimately generate power.

Most of the coal produced domestically is low-grade (D, E, F) with high ash content. This coal is first washed and then used for sponge iron and rejects like middling and chars are used as fuel for power plant. Depending on grade and calorific value of coal, about 30MW power can be generated from a 500tpd kiln. A sponge iron plant with 1mtpa capacity can generate about 170 MW of power. When steel is manufactured using the blast furnace route, the coke oven batteries generate lot of waste heat and gases that are used for power generation. Further, the slag generated from blast furnace and EAF is used for roads construction.

### Chhattisgarh offers advantages over Orissa and Jharkhand

The steel-cum-power business model can also be replicated in other mineral-rich states like Jharkhand and Orissa. Even though Chhattisgarh is land-locked (unlike Orissa), it offers many advantages compared to these states. First is the state government's investor-friendly policy. Secondly is the availability of skilled and peaceful manpower. During our tour, we got the impression that the people of the state welcome industrial development. Orissa is plagued by land acquisition issues and a militant labour force, while Jharkhand suffers from political instability and Naxalite violence.

### New mining policy, change in royalty rate to spur industrial revolution

The new mining policy aims to accelerate prospecting and development of the country's vast natural resources. Time-limits have been framed regarding the development & exploration and commissioning of mines. According to the new policy, mining should commence within 36 months after the prospecting license (PL) has been issued. The licensee is supposed to get environmental and other related clearances within this period. Otherwise, the government could cancel the license and repossess the land, unless the delay is due to regulatory and government issues.

The latest changes in royalty rates are also expected to encourage states facilitate mining. Previously, the royalty rates for minerals like iron ore, manganese, etc. were fixed which was very low. With effect from 13 Aug 2009, royalty has been changed to advalorem rate of 10%. Royalties will increase with the increase in market price of the mineral. This change has happened due to persistence and insistence of state governments like Chhattisgarh, Jharkhand and Orissa. Increased royalties would boost the state governments' revenues.

### Chhattisgarh at the forefront demanding higher royalty rates

The increase in royalty rates would encourage mineral-rich states push for faster clearance of allocation of mines and would enable rapid growth of mining. Chhattisgarh has been at the forefront in pushing for higher advalorem royalty rates as it is pushing for higher growth of mining in the state. We believe more steel and power projects would be set-up in the Chhattisgarh (vs other states) as bureaucratic hurdles in getting approvals and clearances in the state are fewer.

#### Exhibit 3: Projects coming up in mineral-rich states

	Number of projects	Project Cost (Rsbn)
Chhattisgarh	290	4,047.7
Jharkhand	159	4,631.8
Orissa	277	7,375.7

Source: CMIE

## Chhattisgarh can throw up another success story like JSPL

We believe Chhattisgarh has all the ingredients – both tangible (raw materials) and intangibles (investor-friendly government, peaceful labour, etc) – for setting up steel and power projects. This reinforces our view that another success story like JSPL could emerge in the state. Most companies based in Chhattisgarh – SEML, Prakash Industries, Godawari Ispat and Monnet Ispat – have emulated JSPL business model.

### Valuations

**JSPL – Upgraded to Buy:** JSPL offers good visibility on back of demand from various government projects and power business. Moreover, its healthy cash flow will allow it to execute its expansion projects. The company is better placed among peers given its fully integrated business model coupled with major contribution from merchant power. Besides, Jindal Power's (100% subsidiary of JSPL) IPO plans would be huge boost to JSPL's valuation. At CMP, the stock trades at 17.1x FY10E and 12.8x FY11E earnings. On EV/EBITDA, it trades at 11.6x FY10E and 8.9x FY11E. We have upgraded the stock to Buy from Hold with a target price of Rs752.

**Sarda Energy – Reiterate Buy:** Despite lowering our earnings estimates, we feel that SEML is better placed vs peers. The company, which had cut its production of ferro-alloys, is again increasing production and is likely to increase the same to 175tpd from 100tpd at moment on back of two-fold jump in realization to Rs60,000/tonne. We believe that increased ferro-alloy volume would boost revenue. The commercialization of its pellet unit is likely to ensure healthy margins and insulate from iron ore pricing pressure. At CMP, the stock trades at 8.0 x FY10E and 3.6x FY11E earnings and 8.6x FY10E and 4x FY11E EV/EBITDA. We reiterate our Buy rating.

**Monnet Ispat - Reiterate Sell:** The Company posted better margins in Q1FY10 on the back of higher power sales despite depressed steel market. In fact, 75% of profits came from power business. We believe the company would be able to post decent FY10 numbers on back of power sales. However, it is unlikely to sustain these earnings as the company would be consuming power for captive purpose for its steel production starting in FY11.

During our tour we found that the plant is very old and needs a complete makeover. Equipment has to be replaced and new technology adopted. This would require the company incur a huge capex. We reiterate our Sell rating as current valuations (6.8x FY10E EV/EBITDA and 9.1x FY11E) are expensive.

**Prakash Industries (Not Rated):** The stock currently trades at 9.2x FY09 earnings and 7x FY09 EV/EBITDA. We feel these valuations are attractive vs peers. We feel the company would register robust growth due to captive consumption of raw materials and improvement in margin after FY10.

**Godawari Power & Ispat (Not Rated):** The stock currently trades at FY09 P/E of 7x and EV/EBITDA of 5.9x. We believe that with operating iron ore mine, commissioning of pellet unit, coupled with captive power generation would ensure a healthy margin. Incremental revenue will be mainly on the back of higher power sales from the commissioning of additional 20MW of power plant. However, company suffers from poor visibility of growth in future due to absence of projects.

## Jindal Steel &amp; Power

Visit Note/Rating change

22 September 2009

## Buy

Target Price: Rs752

CMP: Rs634

Upside: 19%

\*as on 18 Sep 2009

## On 'power' growth trajectory

We regard Jindal Steel & Power (JSPL) as a power company with about 70% of profits coming from this business and expected to increase further, going forward. The company is a pioneer in adopting the integrated steel and power business model and has lined up aggressive expansion plans in both the segments.

- **Upgraded to Buy:** At CMP, the stock trades at 17.1x FY10E and 12.8x FY11E earnings. On EV/EBITDA, it trades at 11.6x FY10E and 8.9x FY11E. We believe the company would sustain its robust margins due to its fully integrated business model. Further upside is likely due to higher-than-estimated power tariffs. We upgrade the stock to Buy (earlier Hold) with a target price of Rs752.
- **JPL's IPO to boost valuations:** Jindal Power (JPL), JSPL's 100% subsidiary, plans to raise about Rs40bn through an IPO to partly fund its 2,400MW power project in Chhattisgarh. We believe JPL's IPO would command a hefty premium given JSPL's commendable track record. This would also help boost JSPL's valuations.
- **Estimates raised:** We have raised our FY10 earning estimate by 19.8% and 19.4% for FY11 to factor in higher power sales. JSPL is likely to commission Unit 1 of its 135x10 MW power plant at Raigarh (4 x 135MW) and Angul (135 x 6 MW) by the end of Dec 2009 and remaining units will be commissioned every 2 months after that which would help it increase power sales volumes.
- **Lowest cost power producer due to captive coal mines:** JSPL has been allotted two coal blocks in Tamnar at Raigarh, spread over 700 hectares with estimated reserves of 110mt. Captive coal mines have helped the company become one of the lowest cost power producer.

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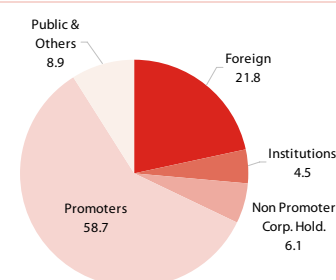
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## Key Data

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Reuters Code	JNSP.BO
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Diluted Shares O/S(mn)	924
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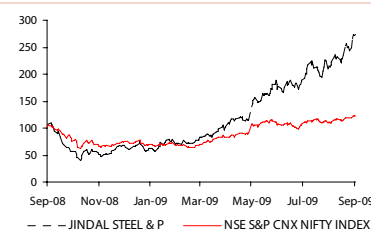
1 USD = Rs48.1

## Shareholding Pattern (%)



\*as on 30 June 2009

## One year Indexed Stock Performance



## Price Performance (%)

	1M	6M	1Yr
JSPL	26.9	233.4	173.9
NIFTY	11.4	77.7	23.0

Source: Bloomberg, Centrum Research  
\*as on 18 Sep 2009

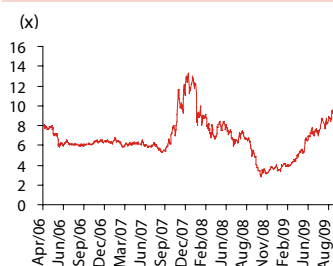
Y/E Mar (Rsmn)	Rev	YoY (%)	EBITDA	EBITDA (%)	Adj PAT	YoY (%)	Fully DEPS	RoE (%)	RoCE (%)	P/E (x)	EV/EBITDA (x)
FY07	35,198	35.9	14,023	39.8	7,028	22.7	45.6	27.5	9.5	83.3	45.6
FY08	54,890	55.9	22,197	40.4	12,496	77.8	81.1	32.4	11.8	46.9	29.3
FY09	108,510	97.7	51,695	47.6	30,072	140.7	195.5	42.7	20.1	19.5	12.8
FY10E	111,816	3.0	57,668	51.6	34,240	13.9	37.1	33.1	18.5	17.1	11.6
FY11E	138,773	24.1	74,671	53.8	45,776	33.7	49.5	30.7	19.5	12.8	8.9

Source: Company, Centrum Research Estimates

## Upgraded to Buy with target price of Rs752

We have upgraded the stock to Buy (earlier Hold), with a price target of Rs752. We believe the company would be able to sustain its high margins due to its fully integrated business model. We also expect further upside on account of higher-than-estimated power tariffs (JSPL is a merchant power company). At CMP, the stock trades at 17.1x FY10E and 12.8x FY11E earnings. On EV/EBITDA, it trades at 11.6x FY10E and 8.9x FY11E.

### Exhibit 1: One-year forward EV/EBITDA



Source: Bloomberg Centrum Research Estimates

### Exhibit 2: SOTP valuation

Rsmn	Average EV/EBITDA	FY10E EBITDA	FY11E EBITDA	EV	Price (Rs)	Weight	Avg. Price
<b>Valuation of steel business</b>							
Average EV/EBITDA	7	18,877		132,140	55	0.6	33
Average EV/EBITDA	7		28,218	197,525	128	0.4	51
Price (Rs)							<b>84</b>
<b>Valuation of power Business</b>							
Average EV/EBITDA	15	38,767		581,504	629	0.6	378
Average EV/EBITDA	15		44,714	670,704	726	0.4	290
Price (Rs)							<b>668</b>
<b>Total (Rs)</b>							<b>752</b>

Source: Centrum Research Estimates

## JPL's IPO expected to boost valuations

JSPL plans to raise about Rs40bn by listing JPL, its 100% subsidiary. We believe the IPO would be priced at a hefty premium given JSPL's commendable track record. This would also help boost JSPL's valuations.

JSPL has a unique record of not raising money from the equity market during the last 6 years. All its capex was funded through internal accruals and the company maintained an annual growth rate of 70%. Now after successful commissioning of a 1,000 MW merchant power plant at Raigarh, it is undertaking brown-field expansion to set up a 2,400MW power plant at the same site.

## Estimates raised to factor in higher power volumes

We have raised our earning estimate by 19.8% and 19.4% for FY10E and FY11E respectively to factor in higher power sales. JSPL is likely to commission Unit 1 of its 135x10 MW power plant at Raigarh (135x4 MW) and Angul (135x6 MW) by the end of Dec 2009 and remaining units will be commissioned every 2 months after that, which would allow the company to increase power sales volume.

### Exhibit 3: Revised estimates

Y/E March (Rsmn)	Revised Estimates		Earlier Estimates		% Change	
	FY10E	FY11E	FY10E	FY11E	FY10E	FY11E
Net Sales	111,816	138,773	112,018	137,395	(0.2)	1.0
EBITDA	57,668	74,671	48,618	64,601	18.6	15.6
PAT	34,240	45,776	28,588	38,351	19.8	19.4
EPS (Rs)	37.1	49.5	30.9	41.5	19.8	19.4

Source: Centrum Research Estimates

## Aggressive expansion plans in both steel and power segments

JSPL has lined up an aggressive capex plan to increase its steel manufacturing capacity to 18mtpa by FY13 from 3mtpa currently. Pellet plant of 4 mtpa is expected to be commissioned by March 2010, which would increase its total metallics capacity to 3.87mtpa. We believe the commissioning of incremental capacity would significantly contribute to increased sales volume in FY11. The company also intends to set-up a state-of-the-art 1.5mtpa plate mill in Angul at Orissa. Its current plate mill at Raigarh is not successful in rolling plates above API-60 grades (the requirement of end users in the oil & gas industries is API-70 and above).

JSPL is also in the process of setting up 10x135MW (4x135MW in Raigarh and 6x135MW in Angul) power capacity. Unit 1 of the 4x135MW plant in Raigarh is likely to get commissioned by January 2010. The remaining units will be commissioned every two months after that. JPL, which currently operates a 1000MW merchant power plant, has also lined up a 4x600 MW expansion at Raigarh. The first unit is scheduled to get commissioned in May 2012. The boiler-turbine-generator (BTG) order for the 2,400MW power plant has already been placed with BHEL. After the expansion, the total power generation capacity (JSPL and JPL) would increase by over 5x to 6,090MW.

#### Exhibit 4: Capacity for steel and power to increase

Product	Existing capacity	Expansion					Capacity post expansion
		FY10	FY11	FY12	FY13	FY14	
Sponge and DRI (mt)	1.37		2.00				3.37
Steel (mt)	3.00			9.0	6.0		18
Power (MW)	1,340	135	810	540	2,400	865	6,090

Source: Company

#### Power segment likely to be growth driver

JSPL currently has a total power generating capacity of 1,340MW (JPL -1,000 and JSPL 340MW) and plans to increase this capacity by over 5x by FY13. The management indicated that the additional power is likely to be commissioned before the expansion of its steel manufacturing capacity. In the interim period, the company will be selling the power generated on merchant basis, thereby increasing the return on equity.

Consolidated revenue (including JPL) in FY09 grew 97.7% YoY to Rs108.5bn, largely due to the over 6x increase in contribution from the power segment (Rs40.7bn in FY09b vs 6.6bn in FY08) coupled with 41.9% increase in contribution from the steel business to Rs74.8bn. While EBITDA grew 132.9%, margin increased 720bp to 47.6% on the back of higher power tariff. JPL reported revenues of Rs32.5bn and PAT of Rs15.8bn for FY09. JPL achieved a PLF of 96% during Q1FY10.

#### Exhibit 5: JPL – Key financial highlights

Particular	FY08	FY09				
		Q1	Q2	Q3	Q4	Total
Gross generation (MU)	125.3	962	1,490	1,951	1,966	6,369
PLF (%)	66	59	70	88	91	79
Net Sales (Rsmn)	1,253	2,936	6,539	11,607	11,494	32,575
PAT (Rsmn)	194	413	3,147	5,746	6,513	15,819

Source: Company

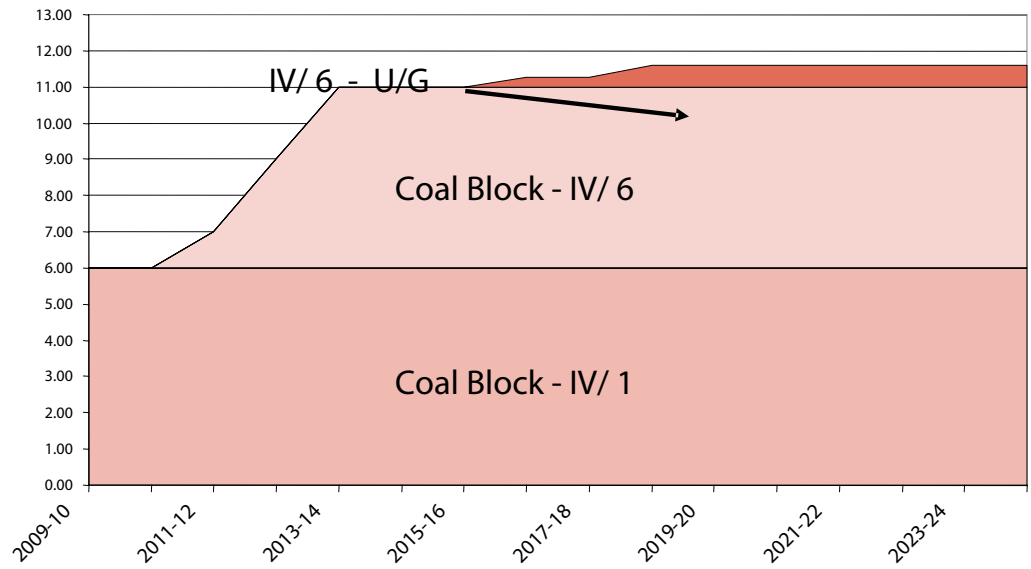
With steel demand still depressed, we believe the company would sell more power on merchant basis, rather than consuming captive. As a result, the power business would drive earnings and margin growth and contribution from this business at the EBITDA level is slated to increase to more than 70% in FY10.

#### Lowest cost power producer due to captive coal mines

JSPL has been allotted a coal mine at Tamnar in Raigarh, which has an estimated reserve of 100mt. Since JSPL's power plants are pit-head based, its cost of generation is among the lowest in the world (about Rs0.5/unit) giving it a competitive edge over others. It is currently mining 6mt of coal from block IV/I and is likely to ramp up to 11mt, with the commencement of coal block IV/6 as additional power capacities get added.

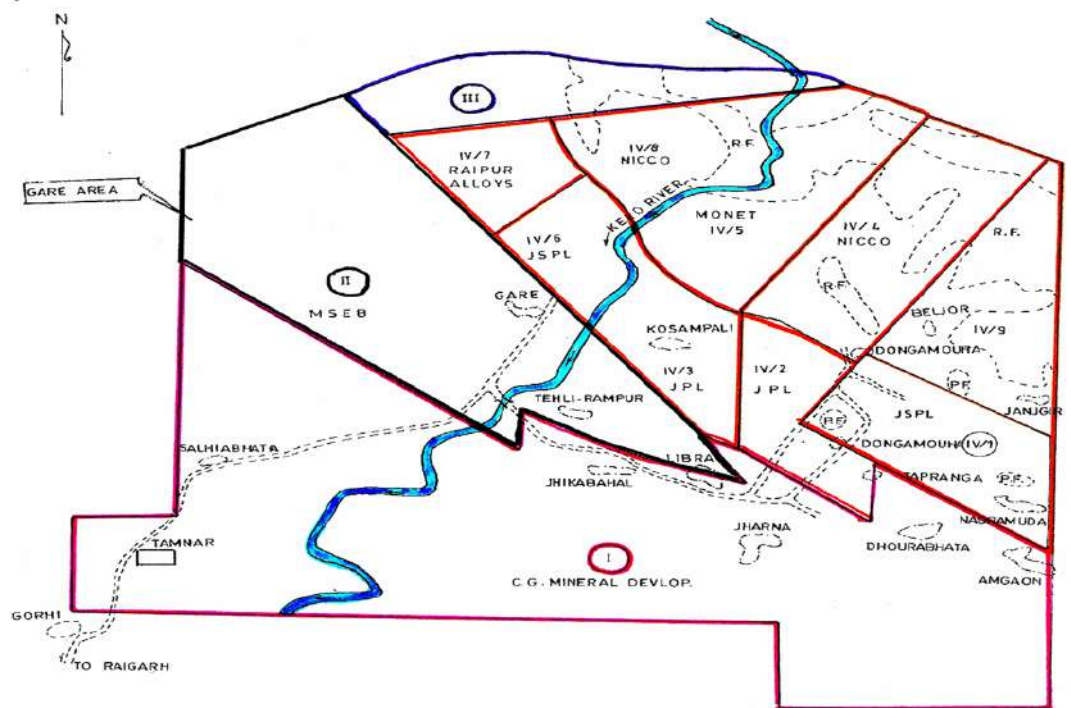
**Exhibit 6: Raw coal production schedule**

(Prod. in M. Tons)



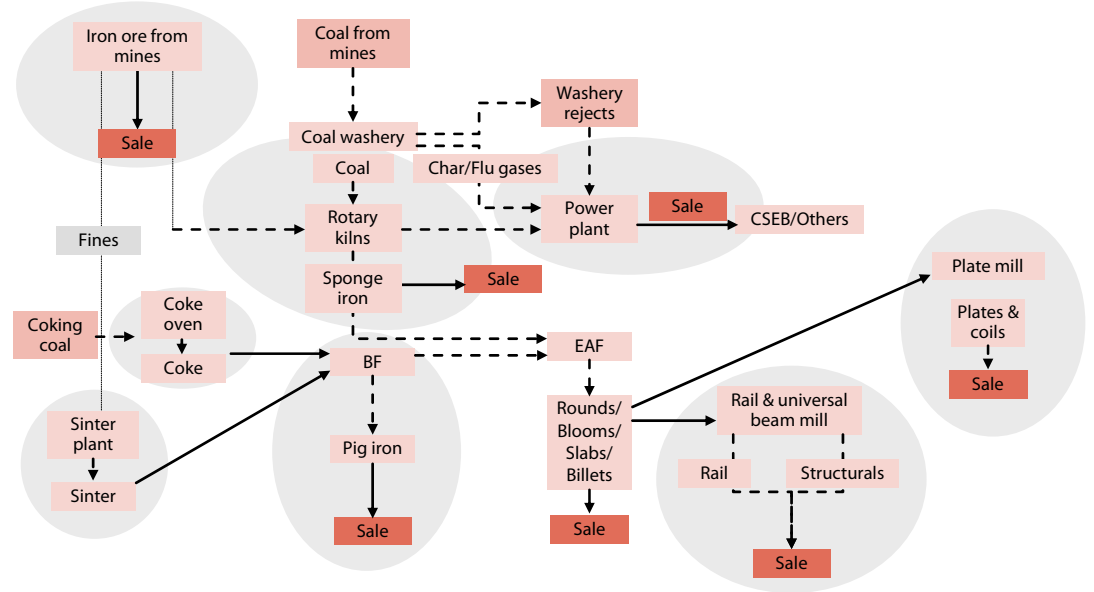
Source: Company

**Exhibit 7: GARE Coal Block**



Source: Company

**Exhibit 8: Integrated steel manufacturing process**



Source: Company

**Exhibit 9: Site photographs**

**Blast furnace model (1,680 cu meters)**



**Sponge iron rotary kiln**



**Slab casting in progress ...**



**Blast furnace operation parameters**



Source: Company

JSPL's coal mines



Overburden of coal



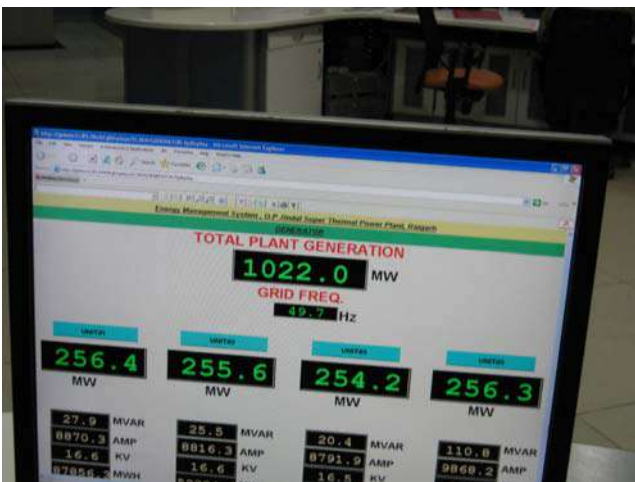
JPL's 1,000MW power plant



Inside the power plant



A computer showing actual power generation



1<sup>st</sup> unit of the 135x4 MW power plant at Raigarh



Source: Company

**Milestone dates of 4x600 MW**

**MAJOR MILESTONE DATES FOR UNIT 1, 2, 3 & 4 OF 4 X 600 MW**

Zero Date of Project: 27-Dec-08

Sl. No.	Name of the Major Activity	UNIT # 1		UNIT # 2		UNIT # 3		UNIT # 4	
		Schedule Date (Unit-1)	Actual Date	Schedule Date (Unit-2)	Actual Date	Schedule Date (Unit-3)	Actual Date	Schedule Date (Unit-4)	Actual Date
1	Boiler Erection Start	28-Dec-09		28-Apr-10		28-Aug-10		28-Dec-10	
2	Boiler Drum Lifting	25-Apr-10		25-Aug-10		25-Dec-10		25-Apr-11	
3	Boiler Hydro Test (Drainable)	25-Apr-11		25-Aug-11		25-Dec-11		25-Apr-12	
4	TG Erection Start	19-Sep-10		19-Jan-11		19-May-11		19-Sep-11	
5	Stator Lifting	6-Jun-11		6-Oct-11		6-Feb-12		6-Jun-12	
6	Turbine Box-up	23-Jul-11		23-Nov-11		23-Mar-12		23-Jul-12	
7	Generator Box-up	23-Jul-11		23-Nov-11		23-Mar-12		23-Jul-12	
8	Oil Flushing Completion	22-Oct-11		22-Feb-12		22-Jun-12		22-Oct-12	
9	Turbine on Barring Gear	23-Dec-11		23-Apr-12		23-Jun-12		23-Dec-12	
10	Boiler Light up	25-Oct-11		25-Feb-12		25-Jun-12		25-Oct-12	
11	Steam Blowing Completion	23-Dec-11		23-Apr-12		23-Aug-12		23-Dec-12	
12	Synchronisation	27-Jan-12		27-May-12		27-Sep-12		27-Jan-13	
13	Coal Firing	27-Mar-12		27-Jul-12		27-Nov-12		27-Mar-13	
14	Commercial operation	29-May-12		29-Sep-12		29-Jan-13		29-May-13	

**Site of JPL's 4x600 MW power plant**



**Coal conveyor belt for power plant**



**Aerial view of 1,000MW power plant**



Source: Company

## Financials (Consolidated)

### Exhibit 10: Income Statement

Y/E Mar (Rsmn)	FY07	FY08	FY09	FY10E	FY11E
<b>Net Sales</b>	<b>35,198</b>	<b>54,890</b>	<b>108,510</b>	<b>111,816</b>	<b>138,773</b>
<b>Expenditure</b>	<b>21,175</b>	<b>32,693</b>	<b>56,816</b>	<b>54,148</b>	<b>64,102</b>
Raw Materials	10,683	12,033	34,046	37,794	46,905
Power and fuel	3,807	4,182	6,652	7,827	9,714
Employee cost	937	1,471	2,050	2,684	3,331
Other Expenses	5,748	15,007	14,068	5,844	4,152
<b>EBITDA</b>	<b>14,023</b>	<b>22,197</b>	<b>51,695</b>	<b>57,668</b>	<b>74,671</b>
Margin (%)	39.8	40.4	47.6	51.6	53.8
Other income	290	498	624	1,200	1,200
Depreciation	3,365	4,793	9,641	9,600	11,000
EBIT	10,948	17,902	42,678	49,268	64,871
Interest	1,501	2,725	4,567	4,800	6,184
PBT	9,447	15,177	38,111	44,468	58,688
Ex-od items (prior period)	-	-	-	-	-
PBT-Adjusted	9,447	15,177	38,111	44,468	58,688
Taxes	2,419	2,681	8,040	10,228	12,911
etr %	25.6	17.7	21.1	23.0	22.0
<b>PAT</b>	<b>7,028</b>	<b>12,496</b>	<b>30,072</b>	<b>34,240</b>	<b>45,776</b>
Pat Margin %	20.0	22.8	27.7	30.6	33.0

Source: Company, Centrum Research Estimates

### Exhibit 11: Balance Sheet

Y/E Mar (Rsmn)	FY07	FY08	FY09	FY10E*	FY11E
Capital	164	164	165	934	934
Reserves and Surplus	25,427	38,394	70,350	98,972	139,353
<b>Total Net worth</b>	<b>25,591</b>	<b>38,558</b>	<b>70,515</b>	<b>99,906</b>	<b>140,287</b>
Minority Interest	54	62	45	45	45
<b>Total Loan Funds</b>	<b>54,360</b>	<b>69,961</b>	<b>81,133</b>	<b>91,133</b>	<b>95,133</b>
Deferred Tax Liability	4,150	4,947	7,170	4,750	5,225
<b>Total Cap. Employed</b>	<b>84,155</b>	<b>113,528</b>	<b>158,863</b>	<b>195,834</b>	<b>240,690</b>
Gross Block	50,267	78,999	116,724	160,724	194,724
Accumulated Dep	7,839	12,160	22,415	32,015	43,015
<b>Net Fixed Assets</b>	<b>42,428</b>	<b>66,839</b>	<b>94,309</b>	<b>128,709</b>	<b>151,709</b>
Capital WIP	36,630	27,798	32,554	9,000	17,000
Investments	1,087	2,709	5,139	11,000	12,000
Goodwill	57	247	363	363	363
Inventories	6,424	9,961	12,403	13,217	23,310
Sundry Debtors	3,203	3,550	5,741	5,874	10,041
Cash and Bank Balances	986	6,207	6,694	7,163	8,785
Loans and Advances	9,315	14,833	35,823	42,370	39,315
<b>Total Current Assets</b>	<b>19,929</b>	<b>34,550</b>	<b>60,661</b>	<b>68,624</b>	<b>81,450</b>
Current Liabilities	12,131	13,716	21,901	20,769	20,585
Provisions	3,878	5,868	12,293	1,125	1,280
<b>Total Current Liabilities</b>	<b>16,009</b>	<b>19,584</b>	<b>34,194</b>	<b>21,894</b>	<b>21,865</b>
<b>Net Current Assets</b>	<b>3,920</b>	<b>14,967</b>	<b>26,467</b>	<b>46,730</b>	<b>59,586</b>
Miscellaneous Expenditure	32	969	31	31	31
<b>Total Assets</b>	<b>84,155</b>	<b>113,528</b>	<b>158,863</b>	<b>195,833</b>	<b>240,690</b>

Source: Company, Centrum Research Estimates

### Exhibit 12: Cash flow

Y/E Mar (Rsmn)	FY07	FY08	FY09	FY10E	FY11E
<b>Net operating cash flow</b>	<b>14,871</b>	<b>13,467</b>	<b>38,787</b>	<b>41,809</b>	<b>41,574</b>
<b>Net cash flow from investing</b>	<b>(35,640)</b>	<b>(22,351)</b>	<b>(38,520)</b>	<b>(49,861)</b>	<b>(43,000)</b>
<b>Net cash flow from financing</b>	<b>20,754</b>	<b>14,105</b>	<b>220</b>	<b>8,522</b>	<b>3,047</b>
<b>Free Cash Flow</b>	<b>(16)</b>	<b>5,221</b>	<b>487</b>	<b>469</b>	<b>1,622</b>
Opening Cash Balance	1,002	986	6,207	6,694	7,163
Closing Cash Balance	986	6,207	6,694	7,163	8,785

Source: Company, Centrum Research Estimates

### Exhibit 13: Key Ratios

Y/E Mar	FY07	FY08	FY09	FY10E*	FY11E
Diluted Shares (mn)	154.0	154.0	154.0	924.0	924
<b>Per Share (Rs)</b>					
EPS	45.6	81.1	195.5	37.1	49.5
BV	166.2	250.4	457.9	112.0	161.5
DPS	15.0	4.0	5.5	5.5	5.5
<b>Return Ratios (%)</b>					
ROCE	9.5	11.8	20.1	18.5	19.5
ROE	27.5	32.4	42.7	33.1	30.7
<b>Valuation (x)</b>					
P/E	83.3	46.9	19.5	17.1	12.8
P/BV	22.9	15.2	8.3	5.7	3.9
EV/EBITDA	45.6	29.3	12.8	11.6	8.9
EV/Sales	18.2	11.8	6.2	6.0	4.8
<b>Margin (%)</b>					
EBITDA	39.8	40.4	47.6	51.6	53.8
PAT	20.0	22.8	27.7	30.6	33.0
EBIT	31.1	32.6	39.3	44.1	46.7

Note:\* Bonus Issue (5:1)

Source: Company, Centrum Research Estimates

### Exhibit 14: Key Assumption

	FY10E	FY11E
<b>Steel segment</b>		
Volume(tonnes)	1,900,000	2,100,000
Average realization (Rs/tonne)	31,000	32,000
<b>Power segment</b>		
PLF (%)	93.0	93.0
Unit sold (MUs)	9,230	10,646
Tariff rate (Rs/unit)	5.5	5.5

Source: Company, Centrum Research Estimates

## Sarda Energy &amp; Minerals

Visit Note/Estimate revision

22 September 2009

## Buy

Target Price: Rs290

CMP: Rs151

Upside: 92%

\*as on 18 Sep 2009

## Pellet unit to boost margins

**Sarda Energy & Minerals (SEML) recently started trial production at its new iron ore pelletisation plant, which when fully operational in 1-2 months would help reduce cost. This, along with the two-fold increase in ferro alloy prices is expected to help the company improve revenue and boost margins.**

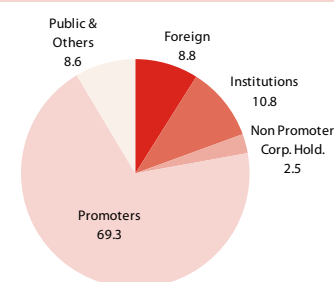
- **Estimates cut:** We have cut our earnings estimates by 6.4% to Rs18.8 for FY10E and 36.6% to Rs41.6 for FY11E to factor in the sharp decline in prices of long products and increase in prices of raw materials like iron ore, coal and manganese ore.
- **Pellet unit to boost margins:** We estimate the pellet unit would help the company save about Rs2,000/tonne on iron ore costs. This would lower its cost of production for sponge iron by about Rs3,300/tonne, leading to an improvement in margins. Margins would be further boosted by the increase in captive coal consumption to 100% by April 2010 from the current 35%.
- **Ramping up ferro alloy production:** SEML, which had temporarily suspended production of ferro alloys due to lower price realizations, has started ramping up production, largely due to two-fold increase in prices from bottom of Rs35,000/tonne in April-May 2009. It currently produces 100tpd, which is likely to get increased to 175tpd by the end of Sept 2009.
- **Enhancing power generation capacity:** SEML plans to increase its power generation capacity by 350MW, out of which 80 MW is likely to get commissioned by April 2011 and 270MW (2x 135MW) would be commissioned in phases by September 2012. The benefits of additional power generated would start accruing from FY12E onwards.
- **Attractive valuations, maintain Buy:** At CMP, the stock trades at 8x FY10E and 3.6x FY11E earnings. On an EV/EBITDA basis, it trades at 8.6x FY10E and 4x FY11E EBITDA, which though not quite attractive but worst seems to be behind and growth visibility is getting clear. As such we maintain our Buy rating with revised target price of Rs290 (Rs167 earlier).

## Key Data

Bloomberg Code	SEML IN
Reuters Code	SAEM.BO
Current Shares O/S (mn)	34.0
Diluted Shares O/S(mn)	34.0
Mkt Cap (Rsbn/USDmn)	5.1/106.6
52 Wk H / L (Rs)	224/50
Daily Vol. (3M NSE Avg.)	39,323
Face Value (Rs)	10

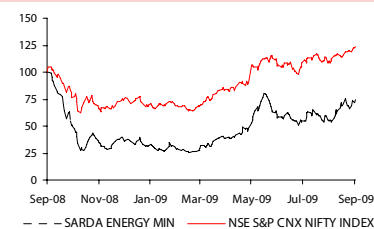
1 USD = Rs48.1

## Shareholding Pattern (%)



\*as on 30 Jun 2009

## One year Indexed Stock Performance



## Price Performance (%)

	1M	6M	1Yr
Sarda Energy	34.8	153.8	(25.6)
NIFTY	11.4	77.7	23.0

Source: Bloomberg, Centrum Research  
\*as on 18 Sep 2009

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Y/E Mar (Rsmn)	Rev	YoY (%)	EBITDA	EBITDA (%)	Adj PAT	YoY (%)	Fully DEPS	RoE (%)	RoCE (%)	P/E (x)	EV/EBITDA (x)
FY07	3,642	(31.6)	366	10.0	427	(59.7)	14.2	20.5	13.2	10.6	17.5
FY08	6,248	71.6	1,684	26.9	1,214	184.4	35.7	30.2	20.3	4.2	4.4
FY09	9,487	51.8	2,324	24.5	1,232	1.5	36.2	23.5	16.1	4.2	5.3
FY10E	5,985	(36.9)	1,314	22.0	638	(48.2)	18.8	11.2	7.4	8.0	8.6
FY11E	8,176	36.6	2,468	30.2	1,416	121.9	41.6	20.5	14.6	3.6	4.0

Source: Company, Centrum Research Estimates

Please refer to important disclosures/disclaimers inside

## Estimates cut on lower realisation

We have cut our earnings estimates by 6.4% to Rs18.8 for FY10E and 36.6% to Rs41.6 for FY11E to factor in the sharp decline in prices of long products and increase in prices of raw materials like iron ore, coal and manganese ore.

### Exhibit 1: Revised estimates

Rsmn	Revised estimates		Earlier estimates		% Change	
	FY10E	FY11E	FY10E	FY11E	FY10E	FY11E
Net Sales	5,985	8,176	6,431	8,777	(6.9)	(6.8)
EBIDTA	1,314	2,468	1,369	3,558	(4.0)	(30.6)
PAT	638	1,416	682	2,234	(6.4)	(36.6)
EPS(Rs)	18.8	41.6	20.1	65.7	(6.4)	(36.6)

Source: Centrum Research Estimates

## Pellet plant, captive coal mine to help boost margins

SEML has been constantly integrating backward in a bid to keep its costs under control. It recently started trial production at its new 0.6mtpa iron ore pellet plant, which is expected to get stabilized in 1-2 months before it starts operating at fully capacity. We estimate the pellet plant would help the company save about Rs3,300/tonne in producing sponge iron. The pelletisation unit will also help the company reduce its iron ore cost, as it will use iron ore fines which are available in plenty within a 50km of Raipur to produce pellets which could be used for producing sponge iron instead of the more expensive iron ore lumps (pellets cost about Rs2,500/tonne vs Rs4,500/tonne for iron ore lumps).

The company has been allotted a coal mine at Raigarh with an estimated reserve of 90mt (open cast – 60mt and underground 30mt). According to the management, the company currently meets 35% of its coal requirement from captive sources, which would eventually increase to 100% by April 2010. At about the same time, the company's coal washery would also get commissioned. We feel that stabilization of pellet unit and 100% captive coal would help the company boost margins, going forward.

## Ramping up ferro alloys production

After the global economic meltdown in Oct 2008, many steel and ferro alloys manufacturers either cut down or totally suspended production as prices fell even below production cost. Ferro alloys prices, which had risen to a peak of Rs100,000/tonne in H1FY09 plunged to below Rs50,000/tonne in H2FY09 and went as low as Rs35,000/tonne in April-May 2009. Prices have started looking up in the last two months and are currently hovering at about Rs65,000/tonne.

Management has indicated that they have already ramped up ferro alloy production in Q2FY09 (production was negligible in Q4FY09 and Q1FY10). The company currently produces 100tpd which is likely to increase to 175tpd by the end of Sept 2009. The company is expected to produce 10,000 tonnes in Q2FY10.

The company currently has an inventory of 40,000 tonnes of manganese ore, which was purchased at lower rate. As a result, it expects to make margin of around Rs20,000/ per tonne of ferro alloys in Q2FY10. SEML would not be producing steel billets due to the lower realization and higher input cost (iron ore). We believe most of the revenue in Q2 would be from ferro alloys, sponge iron and power.

## Increasing power generation capacity

In order to increase coal consumption from its captive mines, SEML plans to increase its power generating capacity by 350MW, out of which 80 MW is likely to get operational by April 2011 and 2x 135MW would be commissioned in phases by September 2012. The full benefits of additional power generated would start accruing FY12E onwards. Currently, it has got 78MW power capacity based on waste heat recovery gas produced from sponge iron production.

It plans to set up a 2x135 MW and 80MW power plant. It has already acquired land for the additional power plant and obtained 1st phase of environmental clearance. It has got boiler for 80 MW and order for TG(Turbine and Generator) set would be given once the final clearance comes. Its 80 MW power plant would likely to get commissioned by April 2011 with 135x2 MW expected to follow in phases in 18 months post April 2011.

**Exhibit 2: Expansion timeline**

Product (Tonne)	Existing capacity	Expansion plan					Post Expansion
		FY10	FY11	FY12	FY13	FY2014	
Sponge	360,000						360,000
Steel	240,000						240,000
Ferro manganese	66,000						66,000
Pellet s		600,000					600,000
Wire Rods		200,000					200,000
Power (MW)	78			80	135	135	428

Source: Company

**Q1FY10 snapshot**

Q1 results were below expectations with revenue falling 63.7% YoY to Rs931mn largely due to 48.2% decline in average realisation of sponge iron and billets and 62.5% decline in ferro alloy realization. As a result EBITDA plunged 95.3% YoY to Rs46mn, while margin compressed 3,300bp. However, sales volume during the quarter was flat, but production volume decline by 27.3% as company's manufacturing facilities remained operative for major part of the quarter on account of a fire in its captive power plant. PAT slipped by 91.3% to Rs60mn. If adjusted for the forex gain of Rs139.2mn, the company would have posted a loss of Rs79mn.

**Valuations attractive; maintain Buy**

At CMP, the stock trades at 8x FY10E and 3.6x FY11E earnings. On an EV/EBITDA basis, it trades at 8.6x FY10E and 4x FY11E EBITDA, which though not quite compelling in near term but worst seems to be behind and growth visibility is getting clear. As such we maintain Buy with revised target price of Rs290 (Rs167 earlier) valuing it at 7x FY11E EBITDA.

**Exhibit 3: One year forward EV/EBITDA**

Source: Bloomberg, Centrum Research Estimates

**Exhibit 4: Site photographs**

**Pellet unit**



**Power house**



**Sponge iron rotary kiln**



**9 MVA ferro alloy furnace**



Source: Company

## Financials

### Exhibit 5: Income Statement

Y/E Mar (Rsmn)	FY07	FY08	FY09	FY10E	FY11E
<b>Net Sales</b>	<b>3,642</b>	<b>6,248</b>	<b>9,487</b>	<b>5,985</b>	<b>8,176</b>
<b>Expenditure</b>	<b>3,276</b>	<b>4,565</b>	<b>7,163</b>	<b>4,671</b>	<b>5,708</b>
Raw Materials	2,710	3,979	6,176	2,873	3,270
Power and fuel	155	38	53	80	100
Employee cost	72	113	173	180	204
Other Expenses	339	435	761	1,538	2,133
<b>EBITDA</b>	<b>366</b>	<b>1,684</b>	<b>2,324</b>	<b>1,314</b>	<b>2,468</b>
Margin (%)	10.0	26.9	24.5	22.0	30.2
Other income	435	50	37	50	50
Depreciation	227	221	279	367	380
EBIT	574	1,512	2,082	998	2,138
Interest	75	121	495	200	250
PBT	499	1,391	1,587	798	1,888
Ex-od items (prior period)	-	8	(95)	-	0
PBT-Adjusted	499	1,399	1,492	798	1,888
Taxes	72	184	260	160	472
etr %	14.4	13.2	17.4	20.0	25.0
<b>PAT</b>	<b>427</b>	<b>1,214</b>	<b>1,232</b>	<b>638</b>	<b>1,416</b>
Pat Margin %	11.7	19.4	13.0	10.7	17.3

Source: Company, Centrum Research Estimates

### Exhibit 6: Balance Sheet

Y/E Mar (Rsmn)	FY07	FY08	FY09	FY10E	FY11E
Capital	296	340	340	340	340
Reserves and Surplus	1,786	3,680	4,908	5,355	6,580
<b>Total Net worth</b>	<b>2,082</b>	<b>4,020</b>	<b>5,249</b>	<b>5,695</b>	<b>6,920</b>
Minority Interest	-	-	-	-	-
<b>Total Loan Funds</b>	<b>2,087</b>	<b>3,233</b>	<b>7,438</b>	<b>7,438</b>	<b>7,438</b>
Deferred Tax Liability	171	194	300	300	300
<b>Total Cap. Employed</b>	<b>4,340</b>	<b>7,447</b>	<b>12,987</b>	<b>13,434</b>	<b>14,659</b>
Gross Block	2,954	3,312	5,011	6,761	8,511
Accumulated Dep	999	1,214	1,473	1,839	2,219
<b>Net Fixed Assets</b>	<b>1,955</b>	<b>2,098</b>	<b>3,538</b>	<b>4,922</b>	<b>6,292</b>
Capital WIP	946	2,547	3,605	2,150	500
Investments	219	204	3,767	3,767	3,767
Goodwill	-	-	-	-	-
Inventories	683	1,499	996	656	896
Sundry Debtors	483	678	226	246	336
Cash and Bank Balances	215	984	367	1,315	2,680
Loans and Advances	364	661	1,069	1,069	1,069
<b>Total Current Assets</b>	<b>1,745</b>	<b>3,822</b>	<b>2,658</b>	<b>3,286</b>	<b>4,981</b>
Current Liabilities	521	1,107	479	512	626
Provisions	9	125	102	178	255
<b>Total Current Liabilities</b>	<b>530</b>	<b>1,232</b>	<b>581</b>	<b>690</b>	<b>881</b>
<b>Net Current Assets</b>	<b>1,215</b>	<b>2,590</b>	<b>2,077</b>	<b>2,596</b>	<b>4,100</b>
Miscellaneous Expenditure	5	10	0	-	0
<b>Total Assets</b>	<b>4,340</b>	<b>7,448</b>	<b>12,987</b>	<b>13,434</b>	<b>14,659</b>

Source: Company, Centrum Research Estimates

### Exhibit 7: Cash flow

Y/E Mar (Rsmn)	FY07	FY08	FY09	FY10E	FY11E
<b>Net operating cash flow</b>	<b>768</b>	<b>628</b>	<b>2,117</b>	<b>1,358</b>	<b>1,579</b>
<b>Net cash flow from investing</b>	<b>(673)</b>	<b>(1,956)</b>	<b>(5,738)</b>	<b>(295)</b>	<b>(100)</b>
<b>Net cash flow from financing</b>	<b>35</b>	<b>1,874</b>	<b>3,017</b>	<b>(115)</b>	<b>(115)</b>
<b>Free Cash Flow</b>	<b>130</b>	<b>546</b>	<b>(604)</b>	<b>948</b>	<b>1,365</b>
Opening Cash Balance	85	215	984	367	1,315
Other Adjustment		223	(13)		
Closing Cash Balance	215	984	367	1,315	2,680

Source: Company, Centrum Research Estimates

### Exhibit 8: Key Ratios

Y/E Mar	FY07	FY08	FY09	FY10E	FY11E
Diluted Shares (mn)	30.0	34.0	34.0	34.0	34.0
<b>Per Share (Rs)</b>					
EPS	14.2	35.7	36.2	18.8	41.6
BV	69.4	118.2	154.4	167.5	203.5
DPS	2.0	3.0	3.0	3.0	3.0
<b>Return Ratios (%)</b>					
ROCE	13.2	20.3	16.1	7.4	14.6
ROE	20.5	30.2	23.5	11.2	20.5
<b>Valuation (x)</b>					
P/E	10.6	4.2	4.2	8.0	3.6
P/BV	2.2	1.3	1.0	0.9	0.7
EV/EBIDTA	17.5	4.4	5.3	8.6	4.0
EV/Sales	1.8	1.2	1.3	1.9	1.2
<b>Margin (%)</b>					
EBIDTA	10.0	26.9	24.5	22.0	30.2
PAT	11.7	19.4	13.0	10.7	0.0
EBIT	15.8	24.2	21.9	16.7	26.1

Source: Company, Centrum Research Estimates

### Exhibit 9: Key Assumption

Y/E March	FY10E	FY11E
<b>Sales Volume (Tonnes)</b>		
Sponge Iron	154,800	127,200
Steel	12,000	-
Wire Rod	60,000	150,000
Ferro Alloys	36,300	46,200
Power (MU)	191.1	182.0
<b>Average Realisation (Rs/T)</b>		
Sponge Iron	12,000	12,500
Steel	21,000	22,000
Wire Rod	25,000	25,000
Ferro Alloys	50,000	50,000
Power (Rs/Unit)	3	3

Source: Company, Centrum Research Estimates

# Monnet Ispat & Energy

Visit note/Estimate revision

22 September 2009

## Sell

Target Price: Rs280

CMP: Rs363\*

Downside: 23%

\*as on 18 Sep 2009

## Merchant power sales prop up profits

**Monnet Ispat & Energy (MIEL) is one of the largest coal-based sponge iron producer in India and also engaged in the manufacturing of steel and ferro alloys. It is also setting up a 1,000MW power plant with captive coal mines, which we believe is a far-fetched plan. It is one of the three companies in the race to acquire stake in Orissa Sponge (it has already spent Rs2bn for a 26% stake).**

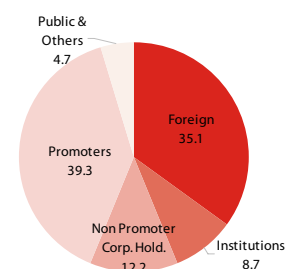
- **Merchant power sales boost profits:** The depressed steel market compelled the company to cut its steel production and shut down its ferro alloys units. As a result, it sells power meant for production of steel and ferro alloys on a merchant basis at spot rates. We estimate the company would sell about 1,10MW of power on a merchant basis, which would boost its profitability.
- **1,000 MW power plant 3-4 years away:** The Company is setting up a 1,000-MW coal-based pit head merchant power plant at Angul, Orissa, and recently gave orders to BHEL for boiler turbine generator (BTG). Although the company expects to fund the equity portion through internal accruals, we believe it would have to raise money through equity dilution. Besides, the company's cash-flow projections are based on higher and robust steel prices that are difficult to predict.
- **Choosing Orissa Sponge acquisition over Raigarh expansion:** MIEL is one of the three companies in the fray to acquire Orissa Sponge and has already spent Rs2bn to acquire a 26% stake. It would require a further Rs2bn to raise its stake to 51%. We expect the company to defer its 1.2mtpa steel manufacturing capacity expansion plan at Raigarh in Chhattisgarh and divert the funds to increase its stake in Orissa Sponge.
- **Estimates revised:** We have raised our earnings estimates for FY10E by 69.1% to Rs41.6 and 24.3% to Rs34.7 for FY11E to factor in higher profit from sale of merchant power.
- **Valuations expensive:** At CMP, the stock trades at 6.8x FY10E EV/EBITDA and 9.1x FY11E, which we believe is expensive. We reiterate our Sell rating with a revised target price of Rs280 (Rs237 earlier), valuing the stock at 7x FY10E EV/EBITDA.

## Key Data

Bloomberg Code	MISP IN
Reuters Code	MNET.BO
Current Shares O/S (mn)	48
Diluted Shares O/S(mn)	57
Mkt Cap (Rsbn/USDmn)	17.4/361.9
52 Wk H / L (Rs)	514/111
Daily Vol. (3M NSE Avg.)	105,256
Face Value (Rs)	10

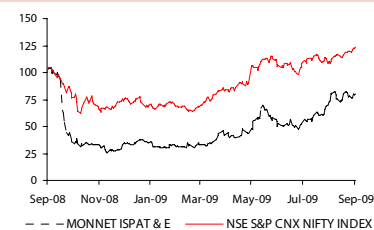
1 USD = Rs48.1

## Shareholding Pattern (%)



\*as on 30 Jun 2009

## One year Indexed Stock Performance



## Price Performance (%)

	1M	6M	1Yr
Monnet Ispat	10.6	139.2	(20.2)
NIFTY	11.4	77.7	23.0

Source: Bloomberg, Centrum Research  
\*as on 18 Sep 2009

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Y/E Mar (Rsmn)	Rev	YoY (%)	EBITDA	EBITDA (%)	Adj PAT	YoY (%)	Fully DEPS	RoE (%)	RoCE (%)	P/E (x)	EV/EBITDA (x)
FY07	6,378	19.8	1,742	27.3	1,348	27.3	39.3	23.6	10.0	6.7	9.7
FY08	11,616	82.1	2,488	21.4	1,739	29.0	36.3	16.0	10.0	7.3	8.1
FY09E	15,685	35.0	3,152	20.1	1,703	(2.1)	35.6	13.7	11.9	7.4	6.4
FY10E	13,502	(13.9)	4,072	30.2	1,992	17.0	41.6	13.7	10.5	6.4	6.8
FY11E	15,045	11.4	4,346	28.9	1,977	(0.8)	34.7	10.8	7.8	7.6	9.1

Source: Company Centrum Research Estimates

## Enhancing capacities...

The management intends to increase the capacity of its Raigarh plant by installing a 500,000 tpa steel-making shop, 500,000 tpa blast furnace and 1mtpa plate mill, in addition to its existing 500,000 tpa sponge iron capacity and 90 MW power generation capacities. From its total installed capacity of 800,000 tpa of sponge iron, it is likely to produce less than 600,000 tpa, due to depressed market conditions and steep fall in price realization. Moreover, the company has shut its ferro alloy unit due to more than 50% decline in realization from a peak of Rs100,000/t.

### Exhibit 1: Expansion plans

(Tonnes)	Existing capacity		Expansion		Post expansion
	Raipur	Raigarh	Raipur	Raigarh	
Sponge Iron	300,000	500,000			800,000
Steel	300,000			500,000	
Rolling Mill	150,000			1,000,000	1,200,000
Ferro Alloys	60,000				60,000
Power (MW)	60	90			150

Source: Company

## ...but driving profits through merchant power sales

The company currently sells 110 MW out of 150 MW power generated on merchant basis at spot tariff. Of the 150MW of captive power generation, the company would consume mere 40MW to produce sponge iron and steel and sell the balance on merchant basis, resulting in the power business generating 75% of FY10E profit. On the adverse side, ferro alloys prices have shot up sharply over the last two months and at the prevailing price of Rs65,000/tonne it would be more profitable to make and sell ferro alloys rather than sell power.

### 1,000 MW power plant 3-4 years away

The company is setting up a 1000 MW coal-based pit head merchant power plant at Angul, Orissa, and recently gave orders to BHEL for BTG. Although it expects to fund the equity portion through internal accruals, we believe the company would need to raise money through equity dilution. Moreover, the company's cash flow projections are based on higher and robust steel prices which are difficult to predict.

## Choosing Orissa Sponge acquisition over Raigarh expansion

MIEL is one of the three companies in the fray to acquire Orissa Sponge, with the other two being Bhushan Steel and Bhushan Power & Steel. It has already spent Rs2bn to acquire a 26% stake and would require further Rs2bn to raise its stake to 51%. Orissa Sponge has 250,000tpa of sponge iron capacity apart from captive iron ore and coal mines with estimated combined reserves of 120mt. The company currently has about Rs2.75bn cash and we expect the company to defer its 1.2mtpa steel manufacturing capacity expansion plan at Raigarh and divert the funds to increase its stake in Orissa Sponge.

## Estimates revised

We have raised our estimates for FY10E by 69.1% to Rs41.6 and 24.3% for FY11E to Rs34.7 to factor in higher profit from sale of merchant power.

### Exhibit 2: Revised estimates

Y/E March (Rsmn)	Revised estimates		Earlier estimates		% Change	
	FY10E	FY11E	FY10E	FY11E	FY10E	FY11E
Net Sales	13,502	15,045	12,361	14,726	9.2	2.2
EBITDA	4,072	4,346	3,055	4,650	33.3	(6.5)
PAT	1,992	1,977	1,178	1,590	69.1	24.3
EPS (Rs)	41.6	34.7	24.6	27.9	69.1	24.3

Source: Centrum Research Estimates

**Valuations expensive**

At CMP, the stock trades at 6.8x FY10E EV/EBITDA and 9.1x FY11E, which we believe is expensive. We reiterate our Sell rating with a revised target price of Rs280 valuing it at 7x FY10E EBITDA.

**Exhibit 3: One-year forward EV/EBITDA**



Source: Bloomberg, Centrum Research Estimates

**Exhibit 4: Site photographs**

**Sponge iron kiln (Raipur plant)**



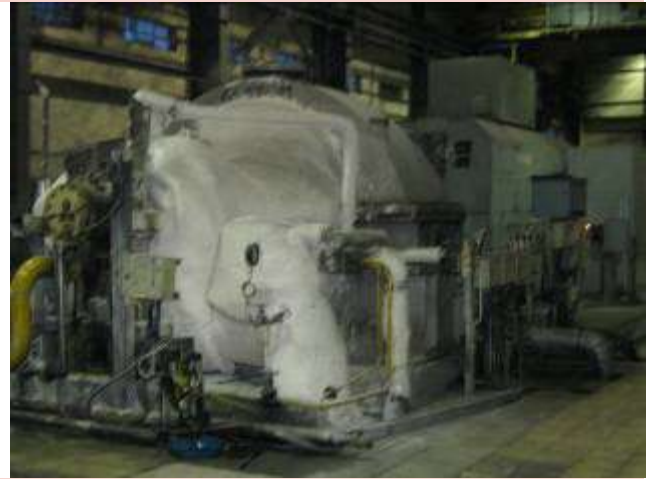
**Structural rolling mill**



**Rolling in progress**



**Power unit of 7.5 MW (Raipur)**



**60 MW power plant building at Raipur**



**3 T induction furnace in steel melting shop**



Source: Company

## Financials

### Exhibit 5: Income Statement

Y/E Mar (Rsmn)	FY07	FY08	FY09E	FY10E	FY11E
<b>Net Sales</b>	<b>6,378</b>	<b>11,616</b>	<b>15,685</b>	<b>13,502</b>	<b>15,045</b>
<b>Expenditure</b>	<b>4,636</b>	<b>9,128</b>	<b>12,533</b>	<b>9,429</b>	<b>10,699</b>
Raw Materials	3,528	7,310	10,205	7,426	7,522
Power and fuel	247	483	442	405	451
Employee cost	234	417	621	540	602
Other Expenses	627	918	1,265	1,058	2,123
<b>EBITDA</b>	<b>1,742</b>	<b>2,488</b>	<b>3,152</b>	<b>4,072</b>	<b>4,346</b>
Margin (%)	27.3	21.4	20.1	30.2	28.9
Other income	247	267	485	150	150
Depreciation	331	441	687	894	962
EBIT	1,658	2,314	2,950	3,328	3,534
Interest	(3)	71	733	837	1,000
PBT	1,661	2,243	2,217	2,491	2,534
Ex-od items (prior period)	-	-	-	-	-
PBT-Adjusted	1,661	2,243	2,217	2,491	2,534
Taxes	313	504	514	498	558
etr %	18.8	22.5	23.2	20.0	22.0
<b>PAT</b>	<b>1,348</b>	<b>1,739</b>	<b>1,703</b>	<b>1,992</b>	<b>1,977</b>
Pat Margin %	21.1	15.0	10.9	14.8	13.1

Source: Company, Centrum Research Estimates

### Exhibit 6: Balance Sheet

Y/E Mar (Rsmn)	FY07	FY08	FY09E	FY10E	FY11E
Capital	343	479	479	479	569
Reserves and Surplus	5,366	10,407	11,985	14,068	17,678
<b>Total Net worth</b>	<b>5,709</b>	<b>10,886</b>	<b>12,464</b>	<b>14,547</b>	<b>18,247</b>
Minority Interest	51	100	100	100	100
<b>Total Loan Funds</b>	<b>10,185</b>	<b>11,259</b>	<b>11,259</b>	<b>16,259</b>	<b>26,259</b>
Deferred Tax Liability	628	908	908	908	908
<b>Total Cap. Employed</b>	<b>16,573</b>	<b>23,154</b>	<b>24,732</b>	<b>31,815</b>	<b>45,515</b>
Gross Block	8,303	12,355	14,355	22,355	34,355
Accumulated Dep	1,303	1,748	2,431	3,325	4,287
<b>Net Fixed Assets</b>	<b>7,000</b>	<b>10,607</b>	<b>11,924</b>	<b>19,030</b>	<b>30,068</b>
Capital WIP	3,821	3,393	4,000	5,000	3,000
Investments	386	1,010	1,700	3,500	3,500
Inventories	1,220	2,217	2,578	2,219	2,473
Sundry Debtors	462	1,051	1,117	962	1,072
Cash and Bank Balances	2,964	3,741	3,671	1,217	1,590
Loans and Advances	1,837	3,151	3,206	3,051	6,866
<b>Total Current Assets</b>	<b>6,482</b>	<b>10,160</b>	<b>10,573</b>	<b>7,449</b>	<b>12,001</b>
Current Liabilities	895	1,473	2,575	1,938	2,198
Provisions	223	545	906	1,244	1,073
<b>Total Current Liabilities</b>	<b>1,117</b>	<b>2,018</b>	<b>3,481</b>	<b>3,182</b>	<b>3,271</b>
<b>Net Current Assets</b>	<b>5,365</b>	<b>8,143</b>	<b>7,092</b>	<b>4,268</b>	<b>8,729</b>
Miscellaneous Expenditure	2	1	17	17	218
<b>Total Assets</b>	<b>16,573</b>	<b>23,154</b>	<b>24,733</b>	<b>31,815</b>	<b>45,516</b>

Source: Company, Centrum Research Estimates

### Exhibit 7: Cash flow

Y/E Mar (Rsmn)	FY07	FY08	FY09E	FY10E	FY11E
<b>Net operating cash flow</b>	<b>705</b>	<b>(99)</b>	<b>3,065</b>	<b>2,763</b>	<b>2,836</b>
<b>Net cash flow from investing</b>	<b>(4,098)</b>	<b>(4,012)</b>	<b>(2,690)</b>	<b>(9,800)</b>	<b>(12,000)</b>
<b>Net cash flow from financing</b>	<b>1,816</b>	<b>4,888</b>	<b>(444)</b>	<b>4,583</b>	<b>9,537</b>
<b>Free Cash Flow</b>	<b>(1,577)</b>	<b>777</b>	<b>(70)</b>	<b>(2,454)</b>	<b>373</b>
Opening Cash Balance	4,541	2,964	3,741	3,671	1,217
Closing Cash Balance	2,964	3,741	3,671	1,217	1,590

Source: Company, Centrum Research Estimates

### Exhibit 8: Key Ratios

Y/E Mar	FY07	FY08	FY09E	FY10E	FY11E
Diluted Shares (mn)	34.3	47.9	47.9	47.9	56.9
<b>Per Share (Rs)</b>					
EPS	39.3	36.3	35.6	41.6	34.7
BV	166.4	236.5	261.1	303.7	320.7
DPS	4.5	4.5	5.0	4.5	4.5
<b>Return Ratios (%)</b>					
ROCE	10.0	10.0	11.9	10.5	7.8
ROE	23.6	16.0	13.7	13.7	10.8
<b>Valuation (x)</b>					
P/E	6.7	7.3	7.4	6.4	7.6
P/BV	1.6	1.2	1.0	0.9	0.8
EV/EBITDA	9.7	8.1	6.4	6.8	9.1
EV/Sales	2.6	1.7	1.3	2.1	2.6
<b>Margin (%)</b>					
EBITDA	27.3	21.4	20.1	30.2	28.9
PAT	21.1	15.0	10.9	14.8	13.1
EBIT	26.0	19.9	18.8	24.6	23.5

Source: Company, Centrum Research Estimates

### Exhibit 9: Key Assumption

	FY10E	FY11E
<b>Sales Volume (Tonnes)</b>		
Sponge Iron	480,000	520,000
Steel	160,000	160,000
Ferro Alloys	10,000	30,000
Power (MU)	760.3	661.0
<b>Average Realisation (Rs/T)</b>		
Sponge Iron	12,000	12,000
Steel	22,000	25,000
Ferro Alloys	42,000	50,000
Power (Rs/Unit)	5	5

Source: Company, Centrum Research Estimates

## Prakash Industries

Visit Note

22 September 2009

## Not Rated

CMP: Rs163\*

\*as on 18 Sept 2009

## Captive mines to boost margin

**Prakash Industries is an integrated steel player manufacturing sponge iron, billets and has a structural rolling mill with captive power generation capacity located at Champa, Chhattisgarh. We believe that the company's margins and bottomline would improve significantly going forward as iron ore start coming from its captive mines from Jan 2010 onwards.**

- **Scouting QIP/FCCB option to meet its aggressive capex plans:** The Company has embarked on an aggressive capex plan of Rs30bn over next five years to increase its steel-making and power generation capacities. It expects to raise Rs5bn via QIP/FCCB route to fund the capex with the rest coming from internal accruals and debt.
- **Enhancing capacity to 1mtpa:** Prakash Industries plans to increase its sponge iron capacity to 1.2mt from 0.4mt by March 2012 and steel-making to 1mt from 0.55mt by March 2011. It also intends to increase its power capacity from 100MW to 775MW in five years.
- **Captive raw materials to boost margin:** While it meets its 100% coal requirement through captive mines, it expects to start production from captive iron ore mines by Jan-Feb 2010, which would meet 50% of its requirement in FY11E and 100% in FY12E. The captive mines would enable the company to withstand raw material pricing pressures, enabling cost control and thereby, margin expansion.
- **Q1FY10 snapshot:** Net sales fell 7% to Rs3,650mn, largely attributed to the fall in realization. The company could sustain its margin at 21.7% in Q1, largely due to its captive coal mines and power consumption. However, the operation of its iron ore and coal mines would significantly add margin going forward. PAT declined 12.4% to Rs590mn during Q1.
- **Valuations:** The stock currently trades at 9.2x FY09 earnings and 7x EV/EBIDTA of FY09. We have positive bias on the stock.

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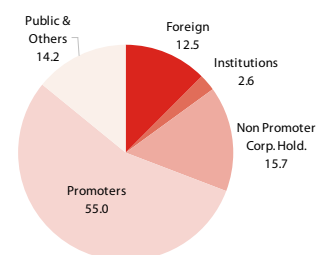
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## Key Data

Bloomberg Code	PKI IN
Reuters Code	PRKI.BO
Current Shares O/S (mn)	115.5
Diluted Shares O/S(mn)	115.5
Mkt Cap (Rsbn/USDmn)	18.8/390.5
52 Wk H / L (Rs)	165/32
Daily Vol. (3M NSE Avg.)	333,910
Face Value (Rs)	10

1 USD = Rs48.1

## Shareholding Pattern (%)



\*as on 30 Jun 2009

## One year Indexed Stock Performance



## Price Performance (%)

	1M	6M	1Yr
Prakash Indu.	21.6	291.1	41.5
NIFTY	11.4	77.7	23.0

Source: Bloomberg, Centrum Research  
\*as on 18 Sep 2009

Y/E Mar (Rsmn)	Rev	YoY (%)	EBITDA	EBITDA (%)	Adj PAT	YoY (%)	Fully DEPS	RoE (%)	RoCE (%)	P/E (x)	EV/EBITDA (x)
FY07	9,329	-	2,019	21.6	1,173	-	12.8	17.5	15.6	12.7	10.7
FY08	12,537	34.4	2,965	23.6	1,988	69.4	17.2	21.1	19.8	9.4	7.2
FY09	15,256	21.7	3,002	19.7	2,039	2.6	17.7	17.8	20.3	9.2	7.0
FY10E*	19,725	29.3	3,938	20.0	2,471	21.2	21.4	-	-	7.6	-
FY11E*	20,863	5.8	6,059	29.0	3,817	54.4	33.0	-	-	4.9	-

Note: \* First cut Estimates

Source: Company, Centrum Research Estimates

## Aggressive expansion plans on the anvil

The company has lined up aggressive capex plans of Rs30bn over 4-5 years to increase its sponge iron capacity from 0.4mtpa to 1.2mtpa by March 2012 and steel-making capacity to over 1mt and power capacity to 775MW from 100MW (inclusive of waste heat recovery). It is scouting the QIP/FCCB route to fund its capex requirement of Rs5bn, while balance is expected to come from internal accruals and debt.

The company plans to increase its sponge iron and steel capacities capacity to over 1mt over the next three years. The management expects margin expansion along with marginal volume growth going forward as it has mainly undertaken expansion to balance the capacity of raw materials side against requirement for finished rolled products.

### Exhibit 1: Capacity expansion plans

Product	Existing capacity	Expansion plan			Post Expansion
		FY10	FY11	FY12	
Sponge Iron (mt)	0.40	0.20	0.20	0.40	1.2
Steel (mt)	0.55	0.20	0.25		1.0
Power (MW)	100	10	160	150	775

Source: Company

Currently, the company is short of sponge iron and steel billets (intermediary products) to feed its finished goods production (rolling mill capacity 0.75 mtpa), which it purchases directly from the market. To insulate itself from price fluctuations in the intermediary products, it hopes to increase its sponge iron and steel-making capacities, which it uses to feed its requirement of value-added products such as wire rods, structurals and thermo mechanically treated (TMT) bars. In addition to its steel products, the company also has four ferro alloys units of 7.5MVA each (approximately 48,000 tpa), running at full capacity utilization. Prakash Industries was the only company that operated its ferro alloy unit during the last 6 months and did not sell power. Its steel-making and rolling mills too operate at full capacity and it has to purchase about 20MW of power from Chhatisgarh State Electricity Board (CSEB) to meet its requirement.

## Power business to drive growth beyond March 2011

The company is expanding its power capacity from 100MW currently to 775MW (inclusive of 50 MW waste heat recovery plant). Its current power generation is based on waste heat recovery plant and it expects to add further 10MW in a month with the commissioning of a 0.2mtpa sponge iron kiln. Power capacities would be added in phases, whereby the first unit of 150MW would commence generation by March 2011 and post which 1 unit of 150MW would be commissioned every year until 2014. The company would use about 300MW of power to meet its internal requirement and use the remaining to sell merchant power.

## Captive resources to boost margin

Securing backward linkages is crucial to control cost and fight sharp volatility in prices to achieve stable margins. In such scenario, Prakash Industries has its captive coal mine of high grade (Grade B) suitable for production of sponge iron. It also has two other coal mines, one of which is located at Fatehpura and is expected to turn operational by March 2010 with estimated reserves of 150mt. We believe the company would use coal from Fatehpura mines to meet the requirement for its power plants.

Besides, the company also has a captive iron ore mine at Bilaspur, which is expected to start production by March 2010. This mine has an estimated reserves of 70-75mt. The management indicated that it would use 50% of its captive capacity in FY11E and 100% in FY12E for iron ore. With complete control over its crucial inputs (coal and iron ore), the company is well insulated from raw material pricing pressures, which would have a positive impact on its margins, going forward.

## Q1FY10 snapshot

The company's Q1FY10 net sales declined 7% to Rs3,650mn, largely due to the fall in realisation. It could sustain its margin at 21.7% in last quarter, thanks to its captive coal and power consumption. However, with its iron ore mines and other coal mines operating, margins could improve significantly. PAT fell 12.4% to Rs590mn during the quarter.

**Valuation and recommendation**

The stock currently trades at 9.2x FY09 earnings and 7x EV/EBITDA of FY09. Taking into consideration last quarter results, we believe that company is likely to show about 40% growth in FY11E on FY10E annualized basis. We have positive bias on the stock.

**Company Overview**

Prakash Industries, part of the Surya Roshni Group, operates an integrated steel plant in Champa, Chhattisgarh. The company uses rotary kilns (based on SL/RN technology of Lurgi, Germany) to tap the waste gases released from its sponge iron kiln. It has also installed a power cogeneration plant with waste heat recovery boilers in collaboration with Lurgi. It has set up a crushing and screening plant at Koira, Orissa. The company has also installed latest technology submerged arc furnaces to produce high quality ferro alloys to meet its in house requirements and also to cater export as well as domestic market.

**Exhibit 2: Site photographs**

**7.5 MVA ferro alloys furnace in operation**



**Steel melting shop**



**Sponge iron kiln**



**Power unit**



**Manganese ore**



**Dolomite**



Source: Company

## Financials

### Exhibit 3: Income Statement

Y/E Mar (Rsmn)	FY07	FY08	FY09	FY10E*	FY11E*
<b>Net Sales</b>	<b>9,329</b>	<b>12,537</b>	<b>15,256</b>	<b>19,725</b>	<b>20,863</b>
<b>Expenditure</b>	<b>7,310</b>	<b>9,572</b>	<b>12,254</b>	<b>15,787</b>	<b>14,803</b>
Raw Materials	5,838	7,203	9,636	12,427	12,518
Employee cost	349	440	540	789	835
Other Expenses	1,123	1,929	2,078	2,571	1,451
<b>EBITDA</b>	<b>2,019</b>	<b>2,965</b>	<b>3,002</b>	<b>3,938</b>	<b>6,059</b>
Margin (%)	21.6	23.6	19.7	20.0	29.0
Other income	258	38	39	39	39
Depreciation	459	477	425	600	1,000
EBIT	1,818	2,526	2,616	3,377	5,098
Interest	258	440	632	400	500
PBT	1,560	2,086	1,984	2,977	4,598
Ex-od items (prior period)	187	(94)	61		
PBT-Adjusted	1,373	1,992	2,045	2,977	4,598
Taxes	200	4	6	506	782
etr %	14.5	0.2	0.3	17.0	17.0
<b>PAT</b>	<b>1,173</b>	<b>1,988</b>	<b>2,039</b>	<b>2,471</b>	<b>3,817</b>
Pat Margin %	12.6	15.9	13.4	12.5	18.3

Note: \*First cut estimates

Source: Company, Centrum Research Estimates

### Exhibit 4: Balance Sheet

Y/E Mar (Rsmn)	FY07	FY08	FY09
Capital	1,081	1,155	1,155
Reserves and Surplus	5,607	7,943	9,137
<b>Total Net worth</b>	<b>6,687</b>	<b>9,098</b>	<b>10,291</b>
Minority Interest	-	-	-
<b>Total Loan Funds</b>	<b>4,972</b>	<b>3,631</b>	<b>2,593</b>
Deferred Tax Liability	(782)	0	702
<b>Total Cap. Employed</b>	<b>10,878</b>	<b>12,729</b>	<b>13,587</b>
Gross Block	13,415	13,836	15,242
Accumulated Dep	5,499	6,067	6,370
<b>Net Fixed Assets</b>	<b>7,916</b>	<b>7,769</b>	<b>8,872</b>
Capital WIP	495	1,760	2,413
Investments	-	1	22
Goodwill	-	-	-
Inventories	935	986	820
Sundry Debtors	929	1,148	1,085
Cash and Bank Balances	94	845	313
Loans and Advances	836	1,207	1,935
<b>Total Current Assets</b>	<b>2,796</b>	<b>4,186</b>	<b>4,153</b>
Current Liabilities	493	1,111	1,349
Provisions	69	84	715
<b>Total Current Liabilities</b>	<b>561</b>	<b>1,194</b>	<b>2,064</b>
<b>Net Current Assets</b>	<b>2,234</b>	<b>2,993</b>	<b>2,089</b>
Miscellaneous Expenditure	233	207	191
<b>Total Assets</b>	<b>10,878</b>	<b>12,730</b>	<b>13,587</b>

Source: Company, Centrum Research

### Exhibit 5: Cash flow

Y/E Mar (Rsmn)	FY07	FY08	FY09
<b>Net operating cash flow</b>	<b>1,801</b>	<b>1,729</b>	<b>2,689</b>
<b>Net cash flow from investing</b>	<b>(981)</b>	<b>(1,672)</b>	<b>(2,301)</b>
<b>Net cash flow from financing</b>	<b>(817)</b>	<b>693</b>	<b>(921)</b>
<b>Free Cash Flow</b>	<b>3</b>	<b>751</b>	<b>(532)</b>
Opening Cash Balance	92	94	845
Closing Cash Balance	94	845	313

Source: Company, Centrum Research

### Exhibit 6: Key Ratios

Y/E March	FY07	FY08	FY09
Diluted Shares (mn)	103.8	115.5	115.5
<b>Per Share (Rs)</b>			
EPS	12.8	17.2	17.7
BV	44.5	62.1	73.7
DPS	0.0	0.0	0.0
<b>Return Ratios (%)</b>			
ROCE	15.6	19.8	20.3
ROE	17.5	21.1	17.8
<b>Valuation (x)</b>			
P/E	12.7	9.4	9.2
P/BV	3.6	2.6	2.2
EV/EBIDTA	10.7	7.2	7.0
EV/Sales	2.3	1.7	1.4
<b>Margin (%)</b>			
EBIDTA	21.6	23.6	19.7
PAT	12.6	15.9	13.4
EBIT	19.5	20.1	17.1

Source: Company, Centrum Research

## Godawari Power &amp; Ispat

Visit Note

22 September 2009

## Not Rated

CMP: Rs147\*

\*as on 18 Sept 2009

## Power sales boost profit

Godawari Power & Ispat (GPIL) recently forayed into manufacturing sponge iron, steel billets and power generation. The company has been awarded rights for iron ore and coal mining for captive consumption, as a result of which it is now a fully-integrated manufacturer, traversing the entire value chain (raw material to final product) in steel wires.

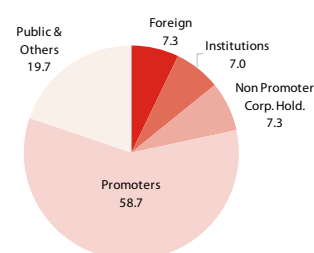
- **Iron ore mines, pellet plant to help boost margins:** GPIL was awarded two iron ore mines for captive consumption and recently commissioned one mine with estimated reserves of 15mt. The second mine is likely to start operation by the end of Q3FY10. The company expects to commission its pellet plant, which will use iron ore fines instead of high-cost lumps, by the end of Q3FY10. The mines and pellet plant are expected to boost revenue and margins.
- **Consortium allotted coal mine:** GPIL, in a consortium with other four companies, has been allotted a non-coking coal mine. The total reserves of mine are estimates at 243mt and the company's share is 63mt. The management says the mine will get commissioned within 1 year, which we believe is too optimistic.
- **Power sales contribute 75% to profits:** GPIL has 53MW captive power generation capacity. Currently, it generates about 45MW and sells 32MW on merchant basis at spot rates. It has stopped production of steel and ferro-alloys and is selling all the power generated on merchant basis. It plans to add another 20MW by Dec 2009 and sell the additional power on merchant basis.
- **Q1FY10 performance:** Net sales declined 32.9% YoY to Rs2,169mn largely due to the decline in average realizations for steel billets and ferro alloys. PAT declined 61.3% to Rs145mn. The Company reported an EBITDA of Rs316mn, largely on account of merchant power sales.
- **Valuations:** At CMP, the stock trades at is trading at 7x FY09 EPS. On EV/E it is trading at 5.9x EBITDA of FY09. Though valuations look cheap compared to peers like Sarda Energy, Monnet Ispat, Prakash Inds, etc. but because of lack of future growth projects, visibility is blurred beyond 2 years. We do not have a rating on the stock.

## Key Data

Bloomberg Code	GODPI IN
Reuters Code	GDPI.BO
Current Shares O/S (mn)	28.1
Diluted Shares O/S(mn)	28.1
Mkt Cap (Rsbn/USDmn)	4.1/85.5
52 Wk H / L (Rs)	166/39
Daily Vol. (3M NSE Avg.)	192,987
Face Value (Rs)	10

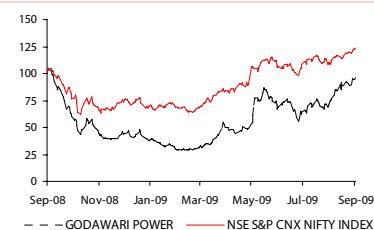
1 USD = Rs48.1

## Shareholding Pattern (%)



\*as on 30 Jun 2009

## One year Indexed Stock Performance



## Price Performance (%)

	1M	6M	1Yr
GPIL	34.2	199.5	(3.7)
NIFTY	11.4	77.7	23.0

Source: Bloomberg, Centrum Research  
\*as on 18 Sep 2009

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Y/E Mar (Rsmn)	Rev	YoY (%)	EBITDA	EBITDA (%)	Adj PAT	YoY (%)	Fully DEPS	RoE (%)	RoCE (%)	P/E (x)	EV/EBITDA (x)
FY07	4,788	-	849	17.7	542	-	21.8	26.1	10.6	6.7	7.6
FY08	8,085	68.9	1,680	20.8	986	81.8	35.1	21.7	13.5	4.1	3.8
FY09	10,355	28.1	1,225	11.8	572	(42.0)	20.4	11.6	8.8	7.0	5.9
FY10E*	9,348	(9.7)	1,400	15.0	532	(7.0)	18.9	-	-	7.7	-
FY11E*	10,957	17.2	2,321	21.2	1,215	128.4	43.3	-	-	3.4	-

Note: \*First cut Estimates

Source: Company, Centrum Research Estimates

### Captive iron ore mines, pellet plant to help boost margins

GPIL was awarded the mining lease for two iron ore mines in Ari Dongri and Boria Tibu in Chattisgarh spread over 215 hectares. It commissioned the Ari Dongri mine in Q1FY10 and the mine is currently operating at production levels of 1,000tpd. The company has also received final approval for the Borai Tibu mine and expects to commission it by the end of Q3FY10. GPIL plans to ramp up production from both the mines to 600,000tpa by Dec 2010, which would meet its captive requirement for sponge iron production. With the ramp-up in production, it expects to be 100% captive in iron ore from FY11E onwards. We believe the captive mines would contribute significantly to operating profit and become a key driver for margin expansion.

The company is also setting up 600,000tpa pellet plant, which is likely to get operational by the end of Q3FY10. The iron ore mines are likely to generate fines (iron ore fines are created as a result of mining, crushing and processing the larger pieces of ore). These fines cannot be used in the manufacturing process. However, they can be converted into pellets for using in sponge iron plants as a replacement for iron ore lumps or sold directly (the latter generally fetch 10% premium to high-grade iron ore lumps). This would translate into cost savings for the company, boost operating profit and improve margins. In addition, to its own pellet plant, GPIL has acquired a 75% stake in Ardent Steel which is setting up an iron ore pellet plant (60,000tpa capacity). The project is expected to get commissioned by FY11.

### Consortium allotted coal mine

GPIL, in a consortium with other four companies, has been allotted a non-coking coal mine. The total reserves of mine are estimates at 243mt and the company's share is 63mt. The management says the mine will get commissioned within 1 year, which we believe is too optimistic. The record of mining consortiums in India has not been impressive and in some cases have not been able to commission the allotted mine even after 3-4 years

It should be also noted that stabilizing operations at the mines and ramping-up production would be a challenge. Any delays would also have an adverse impact on the company's financial performance. Besides, there is always risk of Naxalite violence hampering or even stopping mining activities.

### Merchant power sales contributes 75% to profits

GPIL has decided to increase its captive power generation capacity to 73MW from the current 53MW by setting up a boiler and other auxiliary equipment at an estimated cost of Rs350mn. The Company already has stand-by turbine generators which would be utilized for generating additional power. At present, the company has suspended production of steel and ferro alloys in a bid to increase power sales volume. It generates 45MW of power (out of the installed capacity of 53MW) and sells about 32MW on spot tariff. With the addition of 20 MW, GPIL would sell more power on merchant basis and boost its revenue.

#### Exhibit 1: Expansion plans

Product (tonnes)	Existing Capacity	Expansion	Post Expansion
	FY09	FY10	FY2010
Sponge iron	495,000		495,000
Steel billets	400,000		400,000
HB wire	120,000		120,000
Ferro alloys	16,500		16,500
Power (MW)	53	20	73
Pellet (units)		600,000	600,000

Source: Company

### Q1FY10 performance

Net sales declined 32.9% YoY to Rs2,169mn largely due to decline in average realisations for steel billets and ferro alloys. PAT plunged 61.3% to Rs145mn. The company reported an EBITDA of Rs316mn, was on account of merchant power sales. The management has indicated that the company would continue selling power on spot basis, till prices or demand for steel and ferro alloys improves.

## Valuations

At CMP, the stock trades at is trading at 7x FY09 EPS. On EV/E it is trading at 5.9x EBIDTA of FY09. Though valuations look cheap compared to peers like Sarda Energy, Monnet Ispat, Prakash Inds, etc. but because of lack of future growth projects, visibility is blurred beyond 2 years. We do not have a rating on the stock.

## Company Background

GPIL is the flagship company of Raipur-based Hira Group of Industries, an integrated steel manufacturer with a major presence in the long product segment of the steel industry, mainly mild steel wire. Today, GPIL is an end-to-end manufacturer of mild steel wires. In the process, the company manufactures sponge iron, billets, ferro alloys, captive power, wires rods (through subsidiary company), steel wires, oxygen gas, fly ash brick and pellets, which is likely to get commissioned by Q3FY10.

GPIL is also awarded rights for iron ore and coal mining for captive consumption, as a result of which, the company has managed to traverse the entire value chain (raw material to final product) in steel wires and is now a fully integrated manufacturer. GPIL has already started operation of one of 2 allotted iron ore mines and extraction of coal mine is likely to start in early FY11. During FY09, company posted a revenue of Rs10,55mn, up 24.9% YoY, and PAT of Rs573.6mn.

**Exhibit 2: Site photographs**

**Plant layout**



**Sponge Iron Kiln**



**Sponge Iron**



**Coal**



Source: Company

## Financials

### Exhibit 3: Income Statement

Y/E Mar (Rsmn)	FY07	FY08	FY09	FY10E*	FY11E*
<b>Net Sales</b>	<b>4,788</b>	<b>8,085</b>	<b>10,355</b>	<b>9,348</b>	<b>10,957</b>
<b>Expenditure</b>	<b>3,940</b>	<b>6,405</b>	<b>9,130</b>	<b>7,948</b>	<b>8,635</b>
Raw Materials	3,540	5,641	8,394	6,995	7,599
Employee cost	57	106	125	159	173
Other Expenses	343	658	611	795	864
<b>EBITDA</b>	<b>849</b>	<b>1,680</b>	<b>1,225</b>	<b>1,400</b>	<b>2,321</b>
Margin (%)	17.7	20.8	11.8	15.0	21.2
Other income	24	18	104	12	12
Depreciation	122	258	264	350	400
EBIT	750	1,440	1,065	1,062	1,933
Interest	130	315	342	350	400
PBT	621	1,125	723	712	1,533
Ex-od items (prior period)	(0)	1	71	71	70
PBT-Adjusted	621	1,124	652	641	1,463
Taxes	79	139	80	109	249
etr %	12.7	12.3	12.3	17.0	17.0
<b>PAT</b>	<b>542</b>	<b>986</b>	<b>572</b>	<b>532</b>	<b>1,215</b>
Pat Margin %	11.3	12.2	5.5	5.7	11.1

Note: \*First cut Estimates

Source: Company, Centrum Research Estimates

### Exhibit 4: Balance Sheet

Y/E Mar (Rsmn)	FY07	FY08	FY09
Capital	237	269	269
Reserves and Surplus	1,837	3,644	4,220
<b>Total Net worth</b>	<b>2,075</b>	<b>3,913</b>	<b>4,489</b>
Minority Interest	0	0	67
<b>Total Loan Funds</b>	<b>2,894</b>	<b>2,926</b>	<b>3,548</b>
Deferred Tax Liability	19	19	18
<b>Total Cap. Employed</b>	<b>4,987</b>	<b>6,858</b>	<b>8,122</b>
Gross Block	3,162	4,688	4,953
Accumulated Dep	344	602	887
<b>Net Fixed Assets</b>	<b>2,818</b>	<b>4,086</b>	<b>4,066</b>
Capital WIP	1,034	153	2,016
Investments	49	194	101
Goodwill	0	0	46
Inventories	761	1,744	1,449
Sundry Debtors	281	447	311
Cash and Bank Balances	125	635	438
Loans and Advances	407	409	470
<b>Total Current Assets</b>	<b>1,575</b>	<b>3,235</b>	<b>2,668</b>
Current Liabilities	388	666	588
Provisions	101	143	186
<b>Total Current Liabilities</b>	<b>489</b>	<b>810</b>	<b>774</b>
<b>Net Current Assets</b>	<b>1,086</b>	<b>2,426</b>	<b>1,894</b>
Miscellaneous Expenditure	0	0	0
<b>Total Assets</b>	<b>4,987</b>	<b>6,859</b>	<b>8,122</b>

Source: Company, Centrum Research

### Exhibit 5: Cash flow

Y/E Mar (Rsmn)	FY07	FY08	FY09
<b>Net operating cash flow</b>	<b>453</b>	<b>663</b>	<b>1,550</b>
<b>Net cash flow from investing</b>	<b>(2,003)</b>	<b>(740)</b>	<b>(1,999)</b>
<b>Net cash flow from financing</b>	<b>1,632</b>	<b>586</b>	<b>251</b>
<b>Free Cash Flow</b>	<b>81</b>	<b>510</b>	<b>(197)</b>
Opening Cash Balance	44	125	635
Closing Cash Balance	125	635	438

Source: Company, Centrum Research

### Exhibit 6: Key Ratios

Y/E Mar	FY07	FY08	FY09
Diluted Shares (mn)	24.8	28.1	28.1
<b>Per Share (Rs)</b>			
EPS	21.8	35.1	20.4
BV	82.6	136.8	154.3
DPS			
<b>Return Ratios (%)</b>			
ROCE	10.6	13.5	8.8
ROE	26.1	21.7	11.6
<b>Valuation (x)</b>			
P/E	6.7	4.1	7.0
P/BV	1.8	1.0	0.9
EV/EBIDTA	7.6	3.8	5.9
EV/Sales	1.3	0.8	0.7
<b>Margin (%)</b>			
EBIDTA	17.7	20.8	11.8
PAT	11.3	12.2	5.5
EBIT	15.7	17.8	10.3

Source: Company, Centrum Research

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**Key to Centrum Investment Rankings**

**Buy:** Expected outperform Nifty by >15%, **Accumulate:** Expected to outperform Nifty by +5 to 15%, **Hold:** Expected to outperform Nifty by -5% to +5%, **Reduce:** Expected to underperform Nifty by 5 to 15%, **Sell:** Expected to underperform Nifty by >15%

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