

### IPO Note

#### IPO Details

Face Value	Rs. 10
Offer Price (Rs)	Rs. 35
Issue Opens	October 18, 2007
Issue Closes	October 23, 2007
Bloomberg	RATH IN
BRLM	Chartered Capital and Investment Ltd.
Registrar to issue	MAS Services Ltd.
Shares on offer for sale	7.1 mn

#### Pre issue shareholding pattern

Shareholders	% Stake
Promoters	100.0

#### Post issue shareholding pattern

Shareholders	% Stake
Promoters	56.3
NRIs / FIIs	12.2
Public	30.3
Employees	1.2

#### Segmented Allocation

NRIs / FIIs	2,000,000
Public	4,942,857
Employees	200,000

#### IPO Details

	Offer Price
Offer Price (Rs)	35
Equity Shares prior to issue (mn)	9.2
Fresh Issue of shares (mn)	7.1
Total Equity Shares (mn)	16.3
Share Capital (mn)	Rs. 163.3
Implied market cap (mn)	Rs. 571.6
Debt (mn) (as on 30/06/2007)	Rs. 171.4
Cash (mn) (as on 30/06/2007)	Rs. 8.4
Implied EV (mn)	Rs. 734.5

### Rathi Bars Limited

### Do not subscribe

Rathi Bars Limited (RBL) is engaged in the manufacturing of steel bars, which is used in the construction of multi-storeyed buildings, dams, bridges, flyovers, and power plants as a basic reinforcement material. The Company manufactures Cold Twisted Deformed (CTD) bars and Thermo-Mechanically Treated (TMT) steel bars of various dimensions. Currently, the Company has a production capacity of 80 ktpa and plans to expand it to 100 ktpa with the IPO proceeds.

Though RBL would be benefited from the upsurge in demand from the infrastructure sector in India, poor credentials of management, increasing operational inefficiencies, and highly competitive environment are a cause for concern. We believe, these concerns would overrun its positives.

The Company is expected to raise Rs. 250 mn by offering 7.1 mn shares having a face value of Rs. 10 at a fixed price of Rs. 35. RBL is expected to use the proceeds to fund its expansion and modernization plans. In addition, it will be used to provide security deposit to State Electricity Board.

### Valuation and Recommendations

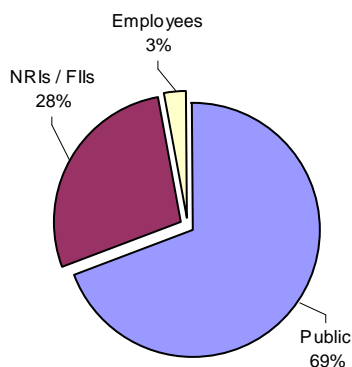
On a post issue basis, RBL is valued at a P/E of 9.5x FY07 earnings and is at a slight premium to the industry average of 7.2x. The Company's ROE of 18% is in line with the average return on equity in the industry.

Though, the issue is aggressively priced, but, in the light of above mentioned factors, we feel that at present the investors have better alternatives in the steel sector. We, therefore, recommend the investors not to subscribe to the issue.

Valuation	P/E	EV/EBITDA	ROE
Kamdhenu Ispat Limited	5.0x	3.7x	20.9%
Zenith Birla Ltd.	5.5x	9.9x	8.4%
MSP Steel & Power	11.2x	6.5x	24.3%
<b>Industry Average</b>	<b>7.2x</b>	<b>6.7x</b>	<b>17.8%</b>
<b>Rathi Bars (post issue)</b>	<b>9.5x</b>	<b>4.5x</b>	<b>18.0%</b>
<b>Premium/Discount to Industry Average</b>	31.0%	(32.5)%	(54.9)%

### IPO

#### Segment allocation of the IPO



■ Public ■ NRIs / FIs ■ Employees

#### Issue details

Rathi Bars plans to raise Rs. 250 mn through an IPO of 7.1 mn equity shares having a face value of Rs. 10 each, at an offer price of Rs. 35. Pre-issue, the promoters hold 100% of the issued and paid-up share capital of the Company. After the issue, the promoters will own 56.3% of the post-issue paid-up equity share capital. The Company has reserved 2 mn shares for allotment to NRIs/FIs, 0.2 mn shares for allotment to the employees and 4.9 mn shares for allotment to the public.

#### Issue objective

The IPO is being carried out to raise funds for the following purposes:

- To finance expansion and modernization plans that include purchase of plant and machinery, building and civil works, preliminary expenses, production launch expenses and, to meet working capital requirements
- To provide for security deposit to State Electricity Board
- To meet the issue expenses

Sources of Funds	(Rs. mn)	Uses of Funds	(Rs. mn)
IPO proceeds	250.0	Purchase of plant and machinery	191.6
Internal Accruals	50.2	Building and civil works	9.2
Term Loan	40.0	Working capital requirement	110.9
		Preliminary expenses	1.0
		Production Launch expenses	4.1
		Expenses of the Issue	20.0
		Security Deposit to SEB	3.4
<b>Total</b>	<b>340.2</b>	<b>Total</b>	<b>340.2</b>

### Promoters

Mr. Kamlesh Kumar Rathi (Managing Director), aged 66 years, is a graduate with around 46 years of experience in the steel industry and is in-charge of general administration of the organization.

Mr. Anupam Rathi (Whole Time Director), aged 39 years, is an Engineering graduate having an experience of 18 years in the industry, and is in-charge of the finance, inventory, and sales department of the Company.

Mr. Anurag Rathi (Whole Time Director), aged 35 years, is a graduate and is in-charge of the production, technical, and stores purchase departments.

### Rationale

#### *Several litigations pending against the Company*

There are several litigations pending against the Company including 2 excise cases involving an amount of Rs. 100.2 mn, 11 sales tax cases involving an amount of Rs. 96.5 mn and a winding up petition. Any unfavorable decision against the Company could result in significant adverse impact on profits.

#### *Poor credentials of the management*

The promoters of RBL have poor credentials. A case attracting the provisions of criminal breach of trust, cheating and criminal conspiracy is pending against Mr. Kamlesh Kumar Rathi and Mr. Anupam Rathi. Also, name of Mr. Anupam Rathi was appearing on the RBI list of willful defaulters till June 30, 2005. However, after resolution of the matter his name was deleted from the list.

Further, there are 16 ventures of the promoters which are yet to commence business operations and hence the income flow generation has not started, as a result, 4 out of these 16 ventures have incurred notional losses during the last three financial years. This raises questions regarding the promoters capability to manage efficiently.

#### *Highly competitive environment*

Rathi Bars operates in a segment which is highly competitive. The Company faces intense competition from low cost producers in various small companies specializing in limited segments of the market. Its competitors also include

bigger players who have greater financial resources. In addition, the Company faces competition from a group company Rathi Special Steels Limited (RSSL), which manufactures similar product under the same brand name. This might result in conflicting interest of promoters.

#### *Capacity expansions to be completed by December 2008*

Currently, RBL has an installed capacity of 80 ktpa. In FY07, the Company produced around 73.5 ktpa at a utilization rate of 92%. RBL plans to utilize the issue proceeds for expanding its existing production capacity to 1 mtpa and to commence in-house production of steel billets, the main raw material for production of CTD and TMT bars. However, these capacity expansions are expected to be completed by December 2008. Therefore, we do not expect these expansions to contribute to the Company's top line in FY08 and FY09.

#### *Increasing operational inefficiencies*

RBL's manufacturing costs are continually increasing as a result of increasing operational inefficiencies, putting pressure on existing low margins. Though, the raw material costs are declining, the uptrend in the prices of iron ore and coal would put further pressure on margins. The Company operates at low margins. Its net profit margin for FY07 was a tad above 3%. If the Company is not able to shift the burden of increased costs to customers by increasing prices of the finished product, which seems difficult in a highly competitive environment, it would reduce its profits considerably or could also result in losses.

#### **Outlook**

The demand for long products is dependent on general economic and business conditions in a country. Being dependent upon the state and condition of the infrastructure, construction and housing industry, the demand for steel bars is a derived demand. As a result of increasing investment in these sectors, the demand for steel bars is expected to remain buoyant.

During the last five years, RBL's revenues grew at a CAGR of 27.9% and earnings grew at a CAGR of 37.1%. However, as the capacity expansion program is likely to be completed by December 2008, we do not expect any growth in earnings for FY08 and FY09.

Based on poor credentials of management, increasing operational inefficiencies, and highly competitive environment, we believe the issue is not very attractive. Hence, we recommend the investors not to subscribe to the issue.

### Company Background

Rathi Bars Ltd. was incorporated on August 10, 1993 and received the certificate for commencement of business on March 18, 1994. Currently, the Company is involved in the business of manufacturing Cold Twisted Deformed (CTD) bars and Thermo Mechanically Treated (TMT) steel bars, which are used in the construction of multistoried buildings, dams, bridges, flyovers, and power plants as a basic reinforcement material.

The Company's manufacturing facility is situated in Alwar district of Rajasthan. It started commercial production on July 27, 1996 with a production capacity of 48 ktpa and as of June 30, 2007 has reached a capacity of 80 ktpa. In FY07, the Company produced around 73.5 ktpa at a capacity utilization of 92%. It sells its products through more than 800 retail outlets spread throughout Northern India. The Company has a strong customer profile including names like DLF, Ansals, Omaxe, Eldeco, DMRC, Hero Honda, Haldiram, and Exide.

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