

USHA MARTIN LTD.

BUY
CMP Rs 54
TP Rs 81

01 Sept. 2009

We recently held the conference call with the Management of Usha Martin Ltd. (UML) to get an understanding of the company's ongoing capacity expansion programme to increase capacity to ~1mn mt and also to review the status of the captive coal mines.

The key takeaways from the interaction were as follows

UML is nearing completion of the ongoing capacity expansion to augment capacity by ~2.5x to ~1mn tpa. The same will also be supported by metallic capacity in the form of pig iron and sponge iron and other related infrastructure. The expansion also entails increasing the value added product capacity to maintain its share at ~45-50%. The entire expansion is progressing satisfactorily and is expected to be fully commissioned by Mar'10 (except certain power capacities).

However, delay in commencement of the captive coal mines present an area of concern as the same was scheduled to start production in Q4FY09 and are now expected to start extraction by the end of Q3FY10. UML's management expects 25% and 100% coal integration in FY10 and FY11 respectively.

VALUATIONS AND RECOMMENDATION

At the CMP of Rs54, the stock trades at a P/E of 4.6x and EV/EBITDA of 3.1x, discounting its FY11E earnings. In our view, these valuations do not factor in the degree of value chain post the completion of the ongoing expansions and the commencement of the coal mines. We remain positive on the overall business of UML, and value the stock at 4x EV/EBITDA to arrive at a price target of Rs81/share. We reiterate our 'BUY' recommendation on the stock.

KEY FINANCIALS (CONSOLIDATED)					Rs mn
	FY07	FY08	FY09	FY10E	FY11E
Net Sales	19,647	23,088	29,498	26,101	31,484
YoY Gr. (%)	9.2	17.5	27.8	(11.5)	20.6
Op. Profits	3,510	4,276	5,137	5,800	8,004
OPM (%)	17.9	18.5	17.4	22.2	25.4
Adj. Net Profit	1,374	1,754	1,853	1,710	2,932
YoY Gr. (%)	63.0	27.6	5.7	(7.7)	71.5
KEY RATIOS					
Dil. EPS (Rs)	5.5	7.0	7.4	6.8	11.7
RoCE (%)	16.9	20.0	24.1	16.4	17.5
RoE (%)	19.8	20.1	17.6	14.1	20.7
PER (x)	9.9	7.8	7.4	8.0	4.6
EV/Net sales (x)	1.1	1.1	1.0	1.1	0.8
EV/EBDITA (x)	6.0	5.5	5.5	4.8	3.1

Pawan Burde +91-22-6618 6381
pawan.burde@pinc.co.in

Faisal Memon +91-22-6618 6389
faisalm@pinc.co.in

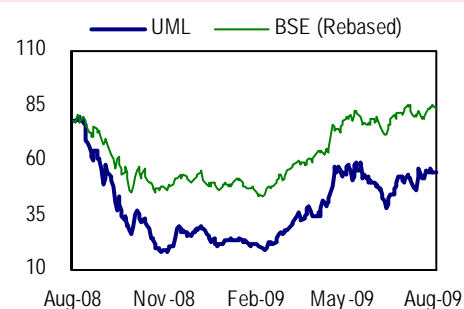
STOCK DATA

Market Cap	Rs13.6bn.
Book Value per share	Rs46
Eq Shares O/S (F.V. Rs1)	251mn.
Free Float	53.8%
Avg Traded Value (6 mnths)	Rs13mn
52 week High/Low	Rs83/18
Bloomberg Code	USMIN
Reuters Code	USBL.BO

PERFORMANCE (%)

	1M	3M	12M
Absolute	5.9	(1.8)	(30.8)
Relative	5.9	(8.3)	(35.6)

RELATIVE PERFORMANCE



Investment Rationale

Stable steel pricing environment

The global financial crisis caused steel demand to plummet as well as prices to correct by 45-50% of their highs. This caused many steel companies to operate at half of their rated capacities. Post stabilization of the economy, steel prices have now started looking up and are expected to settle at the current levels, at least in the short to medium term.

Capacities to be enhanced by ~2.5x

UML is on the verge of completing its ongoing capacity expansion to raise capacity across the product spectrum. The expansion incorporates both forward as well as backward integration to capture the highest degree of integration from iron ore and coal mines to the most value added products (wire ropes, bright bars etc.). The chart below depicts the current and upcoming capacities along with the expected date of completion.

Expansion of capacities in the steel/wire rod division as well as the value added products division

UML's Current and Expanded Capacities ('000 Mt)

	Current Capacity	Post Expansion	Completion
Pig Iron	200	600	Mar'10
Sponge Iron	100	300	Oct'09
Steel	400	1000	Oct'09
Wire Rods	348	400	Completed
Wire Ropes and Stands	120	150	Mar'10
Wire	120	120	Mar'10
Bright Bars	18	48	Mar'10
Captive Power (MW)	73	118	Mar'12

Source: PINC Research

Backward integration to result in OPM expansion

Captive iron ore mines from the Badajamda iron ore mines suffice 100% of the requirement for pig iron and sponge iron. These mines carry estimated reserves of ~80 mn mt and are operational for the past couple of years. Moreover, the mines boasts of high quality reserves containing 62-64% Fe content and are located at a distance of ~160kms from the plant.

Captive iron ore mines from the Badajamda iron ore mines suffice 100% of the requirement

Additionally, UML has also been allotted a high grade (A-C grade) captive coal block in Kajari having estimated reserves of ~40 mn mt. These mines were supposed to commence production in the last quarter of FY09 but have got delayed due to local rehabilitation issues. The management seems confident of kick starting production from the coal mines by the end of Q3FY10 and assume 100% integration from that quarter onwards. We have conservatively factored in no captive coal in our estimates in FY10 and ~50% captive coal for FY11.

Production from the coal mines to start by the end of Q3FY10

Valuations and Recommendation

At the CMP of Rs54, the stock trades at a P/E of 4.6x its FY11E EPS of Rs11.7 and an EV/EBITDA of 3.1x. Considering the potential volume growth emanating post expansion coupled with the scope for margin and profitability expansion due to backward linkages for iron ore, coal and power, UML is comfortably placed to cement its position as a specialty value added steel producer. Also, we believe that current valuations do not factor in the expected volume growth and backward integration program. We reiterate our 'BUY' recommendation on the stock with a 12-month price target of Rs81.

Year Ended March (Figures in Rs mn)

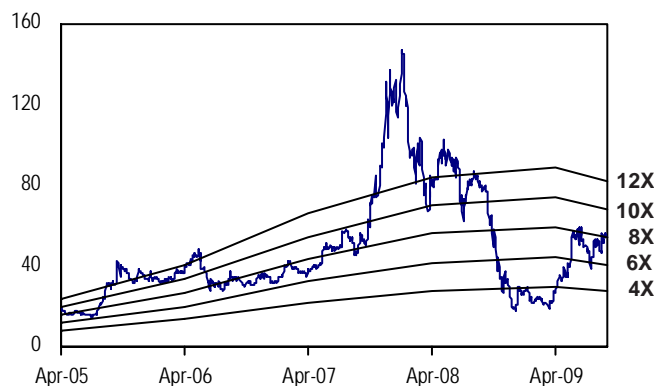
Income Statement	FY07	FY08	FY09	FY10E	FY11E
Net sales	19,647	23,088	29,498	26,101	31,484
Growth (%)	-	17.5	27.8	(11.5)	20.6
Operating Profit	3,510	4,276	5,137	5,800	8,004
Other operating income	-	-	-	-	-
EBITDA	3,510	4,276	5,137	5,800	8,004
Growth (%)	-	21.8	20.1	12.9	38.0
Depreciation	935	975	1,086	1,949	2,459
Other Income	169	174	176	200	200
EBIT	2,745	3,475	4,227	4,051	5,745
Interest Paid	915	1,006	1,422	1,457	1,297
PBT (before E/o items)	1,829	2,468	2,806	2,594	4,448
Tax Provision	441	704	922	856	1,468
E/o loss/(income)	-	-	-	-	-
Net Profit	1,388	1,765	1,884	1,738	2,980
Adjusted Net Profit	1,374	1,754	1,853	1,710	2,932
Growth (%)	-	27.6	5.7	(7.7)	71.5
Diluted EPS (Rs)	5.5	7.0	7.4	6.8	11.7
Diluted EPS Growth (%)	-	27.6	5.7	(7.7)	71.5

Cash Flow Statement	FY07	FY08	FY09	FY10E	FY11E
Pre-tax profit	1,829	2,468	2,806	2,594	4,448
Depreciation	935	975	1,086	1,949	2,459
Total Tax Paid	(367)	(619)	(1,091)	(406)	(1,018)
Chg in working capital	(547)	(842)	2,799	(35)	(645)
Other operating activities	579	691	2,555	1,257	1,097
Cash flow from oper (a)	2,429	2,673	8,154	5,359	6,341
Capital Expenditure	(2,921)	(3,863)	(10,669)	(3,500)	(1,500)
Chg in investments	-	85	-	-	-
Other investing activities	(14)	(82)	89	200	200
Cash flow from inv.(b)	(2,935)	(3,860)	(10,580)	(3,300)	(1,300)
Free cash flow (a+b)	(506)	(1,186)	(2,426)	2,059	5,041
Equity raised/(repaid)	499	634	-	-	-
Debt raised/(repaid)	904	2,035	4,568	1,500	(2,000)
Change in minority interest	-	-	-	-	-
Dividend (incl. Tax)	(139)	(228)	(304)	(251)	(251)
Other financing activities	(937)	(1,025)	(1,471)	(1,457)	(1,297)
Cash flow from fin (c)	328	1,417	2,793	(208)	(3,548)
Net chg in cash (a+b+c)	(178)	231	367	1,851	1,493

Balance Sheet	FY07	FY08	FY09	FY10E	FY11E
Equity Share Capital	240	251	251	251	251
Reserves & surplus	7,495	9,423	11,104	12,563	15,244
Shareholders' funds	7,735	9,674	11,355	12,814	15,495
Minorities interests	119	118	168	195	243
Total Debt	9,630	11,375	16,713	18,213	16,213
Capital Employed	17,484	21,167	28,235	31,222	31,951
Net fixed assets	13,779	17,410	26,232	27,783	26,824
Cash & Cash Eq.	490	721	1,088	2,939	4,432
Net Other current assets	4,703	4,568	2,217	2,252	2,897
Investments	4	4	4	4	4
Net Deferred tax Assets	(1,492)	(1,536)	(1,306)	(1,756)	(2,206)
Total Assets	17,484	21,167	28,235	31,222	31,951

Key Ratios	FY07	FY08	FY09	FY10E	FY11E
OPM (%)	17.9	18.5	17.4	22.2	25.4
Net Margin (%)	7.0	7.6	6.3	6.6	9.3
Yield (%)	1.8	2.1	1.8	1.8	1.8
Net debt/Equity (x)	1.2	1.1	1.4	1.2	0.8
Working Capital Days	44.8	2.6	(17.7)	(18.0)	(18.0)
ROCE (%)	16.9	20.0	24.1	16.4	17.5
RoE (%)	19.8	20.1	17.6	14.1	20.7
EV/Net Sales (x)	1.1	1.1	1.0	1.1	0.8
EV/EBITDA (x)	6.0	5.5	5.5	4.8	3.1
PER (x)	9.9	7.8	7.4	8.0	4.6
PCE (x)	5.9	5.0	4.6	3.7	2.5
Price/BV (x)	1.7	1.4	1.2	1.0	0.9

P/E Band



EV/EBITDA Band



T E A M

EQUITY DESK

Gealgeo V. Alankara	Head - Institutional Sales	<i>alankara@pinc.co.in</i>	91-22-6618 6466
Sailav Kaji	Head Derivatives & Strategist	<i>sailavk@pinc.co.in</i>	91-22-6618 6344

SALES

Anil Chaurasia	<i>anil.chaurasia@pinc.co.in</i>	91-22-6618 6483
Alok Doshi	<i>adoshi@pinc.co.in</i>	91-22-6618 6484
Sundeep Bhat	<i>sundeepb@pinc.co.in</i>	91-22-6618 6486
Gagan Borana	<i>gagan.borana@pinc.co.in</i>	91-22-6618 6485

DEALING

Amar Margaje	<i>amar.margaje@pinc.co.in</i>	91-22-6618 6327
Ashok Savla	<i>ashok.savla@pinc.co.in</i>	91-22-6618 6400
Raju Bhavsar	<i>rajub@pinc.co.in</i>	91-22-6618 6301
Manoj Parmar	<i>manojp@pinc.co.in</i>	91-22-6618 6326
Hasmukh D. Prajapati	<i>hasmukhp@pinc.co.in</i>	91-22-6618 6325
Pratiksha Shah	<i>pratikshas@pinc.co.in</i>	91-22-6618 6329

DIRECTORS

Gaurang Gandhi	<i>gaurangg@pinc.co.in</i>	91-22-6618 6400
Hemang Gandhi	<i>hemangg@pinc.co.in</i>	91-22-6618 6400
Ketan Gandhi	<i>ketang@pinc.co.in</i>	91-22-6618 6400

COMPLIANCE

Rakesh Bhatia	Head Compliance	<i>rakeshb@pinc.co.in</i>	91-22-6618 6400
---------------	-----------------	---------------------------	-----------------



Infinity.com

Financial Securities Ltd

SMALL WORLD, INFINITE OPPORTUNITIES

Member : Bombay Stock Exchange & National Stock Exchange of India Ltd. : Sebi Reg No: INB 010989331. Clearing No : 211
1216, Maker Chambers V, Nariman Point, Mumbai - 400 021; Tel.: 91-22-66186633/6400 Fax : 91-22-22049195

Disclaimer: This document has been prepared by the Research Desk of M/s Infinity.com Financial Securities Ltd. (PINC) and is meant for use of the recipient only and is not for public circulation. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors

The information contained herein is obtained and collated from sources believed reliable and PINC has not independently verified all the information given in this document. Accordingly, no representation or warranty, express or implied, is made as to the accuracy, completeness or fairness of the information and opinions contained in this document.

The Disclosures of Interest Statement incorporated in this document is provided solely to enhance the transparency and should not be treated as endorsement of the views expressed in the report. The opinion expressed or estimates made are as per the best judgement as applicable at that point of time and PINC reserves the right to make modifications and alternations to this statement as may be required from time to time without any prior approval

PINC, its affiliates, their directors, employees and their dependant family members may from time to time, effect or have effected an own account transaction in, or deal as principal or agent in or for the securities mentioned in this document. They may perform or seek to perform investment banking or other services for, or solicit investment banking or other business from, any company referred to in this report. Each of these entities functions as a separate, distinct and independent of each other. The recipient should take this into account before interpreting the document

This report has been prepared on the basis of information, which is already available in publicly accessible media or developed through analysis of PINC. The views expressed are those of analyst and the PINC may or may not subscribe to all the views expressed therein

This document is being supplied to you solely for your information and may not be reproduced, redistributed or passed on, directly or indirectly, to any other person or published, copied, in whole or in part, for any purpose. Neither this document nor any copy of it may be taken or transmitted into the United State (to U.S. Persons), Canada, or Japan or distributed, directly or indirectly, in the United States or Canada or distributed or redistributed in Japan or to any resident thereof. The distribution of this document in other jurisdictions may be restricted by law, and persons into whose possession this document comes should inform themselves about, and observe, any such restrictions

Neither PINC, not its directors, employees, agents or representatives shall be liable for any damages whether direct or indirect, incidental, special or consequential including lost revenue or lost profits that may arise from or in connection with the use of the information.

Copyright in this document vests exclusively with PINC and this document is not to be reported or circulated or copied or made available to others.

Our reports are also available on Reuters, Thomson Publishers and Bloomberg PINV <GO>