



Bhushan Steel

STOCK INFO.	BLOOMBERG
BSE SENSEX: 18,513	BHUS IN
	REUTERS CODE
S&P CNX: 5,496	BSSL.BO

24 October 2007

Sell

Previous Recommendation: Sell

Rs1,016

Equity Shares (m)	42.5
52-Week Range	1,125/318
1,6,12 Rel. Perf. (%)	0/62/158
M.Cap. (Rs b)	43.1
M.Cap. (US\$ b)	1.1

YEAR	NET SALES	PAT	EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/
END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
3/07A	38,377	3,133	73.8	97.1	13.8	3.7	26.9	9.8	1.8	11.3
3/08E	47,316	4,119	97.0	31.5	10.5	2.8	26.4	10.8	1.6	9.5
3/09E	51,198	4,325	101.8	5.0	10.0	2.2	21.9	8.8	1.8	10.1

- During 2QFY08, Bhushan Steel's PAT grew 49% YoY to Rs1b, in line with our estimate. EBITDA margins expanded 340bp YoY to 18.5% due to higher margins in the Orissa plant and savings from switching of fuel in power generation in the cold rolling division at Sahibabad.
- Net sales increased 7.4% YoY to Rs10.7b. Revenue of cold rolling division declined 2% YoY to Rs9.4b due to pressure on realizations for coated products, though prices of special products like HTSS, H&T and CR improved. Revenue of Orissa division grew 144% YoY to Rs2.2b due to increase in sales of long products from 3,600 ton to 32,108 ton. Sponge iron sales too jumped from 1,600 ton to 36,000 ton, and realizations improved 32% YoY to Rs13,600/ton (incl. excise).
- EBITDA increased 31.4% YoY to Rs2b and margins improved 340bp to 18.5% due to higher contribution from long products and non-galvanized products. The company has switched fuel at its Sahibabad plant for power generation & reheating furnaces from LPG to natural gas, which resulted in savings of ~Rs70m and contributed to margin expansion.
- We expect EBITDA margins to improve substantially from 16.4% in FY07 to 36.2% in FY10 (at HRC price assumption of Rs25,000/ton) after start of its HRC mill in Orissa by the end of CY08. The stock trades at 10x FY09E earnings and an EV of 10.1x FY09E EBITDA. We had recently revised our target price upward to Rs914, to factor growth in earnings in FY10 on account of backward integration. However, current valuations appear stretched. We maintain **Sell**.

QUARTERLY PERFORMANCE (STANDALONE)

(RS MILLION)

Y/E MARCH	FY07				FY08				FY07	FY08E
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE		
Net Sales	7,876	9,947	10,008	10,547	9,380	10,681	12,139	14,416	38,377	46,616
Change (YoY %)	6.1	55.2	49.7	42.4	19.1	7.4	21.3	36.7	37.4	21.5
Total Expenditure	6,450	8,444	8,469	8,733	7,837	8,705	10,012	11,889	32,096	38,443
EBITDA	1,426	1,504	1,539	1,814	1,543	1,976	2,127	2,526	6,281	8,173
Change (YoY %)	43.6	127.7	52.7	43.5	8.2	31.4	38.2	39.3	62.8	30.1
As % of Net Sales	18.1	15.1	15.4	17.2	16.5	18.5	17.5	17.5	16.4	17.5
Interest	229	194	206	144	145	312	338	401	773	1,195
Depreciation	503	506	508	573	452	454	623	740	2,089	2,269
Other Income	54	49	51	150	292	135	4	5	304	435
PBT (before EO item)	748	853	877	1,247	1,239	1,346	1,170	1,390	3,724	5,144
Extra-ordinary Income	-	-	-	-	-	-	-	-	-	-
PBT (after EO item)	748	853	877	1,247	1,239	1,346	1,170	1,390	3,724	5,144
Total Tax	125	157	159	150	257	312	166	197	591	932
% Tax	16.7	18.4	18.2	12.0	20.8	23.2	14.2	14.2	15.9	18.1
Reported PAT	623	696	717	1,097	981	1,034	1,004	1,192	3,133	4,212
Adjusted PAT	623	696	717	1,097	981	1,034	1,004	1,192	3,133	4,212
Change (YoY %)	57.3	371.2	99.1	71.3	57.7	48.6	40.0	8.7	102.8	34.5

E: M0St Estimates

Topline boosted by Orissa project

Net sales increased 7.4% YoY to Rs10.7b. Revenue of cold rolling division declined 2% YoY to Rs9.4b due to pressure on realizations for coated products, though prices of special products like HTSS, H&T and CR improved. Revenue of Orissa division grew 144% YoY to Rs2.2b due to increase in sales of long products from 3,600 ton to 32,108 ton. Sponge iron sales too jumped from 1,600 ton to 36,000 ton, and realizations improved 32% YoY to Rs13,600/ton (incl. excise).

GROSS SALES (RS M)

	1QFY07	2QFY07	3QFY07	4QFY07	1QFY08	2QFY08
Flat Products	7,574	9,585	9,189	9,643	8,561	9,355
Long Products	774	863	1,137	1,389	1,315	1,655
Sponge Iron	-	17	232	310	271	492
Others	253	356	394	306	280	354
Total	8,600	10,822	10,952	11,647	10,427	11,856

Source: Motilal Oswal Securities

SALES VOLUMES (TON)

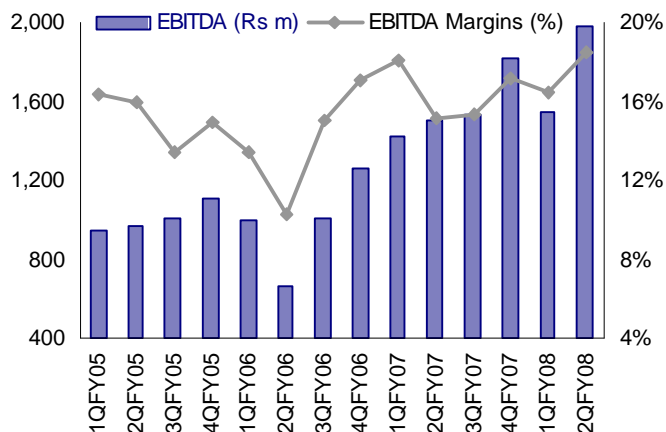
	2QFY07	3QFY07	4QFY07	1QFY08	2QFY08
Flat Products	220,494	218,037	223,052	192,849	216,998
Long Products	21,188	32,906	44,011	39,667	51,980
Total Saleable Steel	241,682	250,943	267,063	232,516	268,978
YoY (%)	38	22	16	15	11
Sponge Iron	1,681	18,460	24,287	20,721	35,960

Source: Motilal Oswal Securities

EBITDA margins expand, aided by fuel cost savings

EBITDA increased 31.4% YoY to Rs2b and margins improved 340bp to 18.5% due to higher contribution from long products and non-galvanized products. The company has switched fuel at its Sahibabad plant for power generation & reheating furnaces from LPG to natural gas, which resulted in savings of ~Rs70m and contributed to margin expansion.

EBITDA MARGINS



Source: Motilal Oswal Securities

Orissa project is on schedule

The company had undertaken a backward integration project in Orissa at a capex of Rs50b. The first phase of this project, comprising SMS 1, 4 kilns, 110 MW captive power plant, and raw material handling plant has been completed. Phase 2, comprising of 1.9m ton hot strip mill is expected to start production by March 2009. The company had recently signed an MoU with L&T and Paulwirth for the supply of a 2.5m ton blast furnace worth Rs12b to expand the capacity further to 4m ton (phase 3) at the Orissa site.

Valuations stretched; Sell

The stock trades at 10x FY09E earnings and an EV of 10.1x FY09E EBITDA. We had recently revised our target price upward to Rs914. Margins are expected to improve significantly in FY10 on account of backward integration. The company has already got coal linkages for power generation and sponge iron production. However, allotment of iron ore mines continues to elude the company due to lack of clarity on government policies and elaborate procedure. Current valuations appear stretched. We maintain **Sell**.

Bhushan Steel: an investment profile

Bhushan Steel Ltd (BSL) is the market leader in CR products in India, and value-added products contribute 60% to its revenues. Bhushan Steel is the first Indian company to set up a cold rolling mill with capability to roll out 1,700mm wide strips for application in the auto industry. The company can be credited with several firsts products such as high tensile steel strap used in packaging and hardened & tempered steel used in making saw blades (these command a high premium). After having grown to a size of approximately 1m tpa in cold rolled and coated products, the company has rightly initiated a project of 1.9 tpa of HRC production in Orissa for backward integration enabling it to meet its current and future internal requirements.

Key investment arguments

- ✍ The company is currently undertaking a 1.9m tpa HR and 0.3m tpa billet greenfield project at a Capex of Rs50b in the mineral-rich state of Orissa to meet the current and future raw material requirement of the cold rolling mill complexes.
- ✍ Proximity of the Orissa plant to coal and iron ore mines enables the cost of production of HRC to be amongst the lowest in the industry.

COMPARATIVE VALUATIONS

		BHUSHAN STEEL	SAIL	JSW STEEL
P/E (x)	FY08E	10.5	12.8	9.3
	FY09E	10.0	12.0	8.9
P/BV (x)	FY08E	2.8	4.5	2.5
	FY09E	2.2	3.4	2.1
EV/Sales (x)	FY08E	1.6	2.4	2.2
	FY09E	1.8	2.2	2.1
EV/EBITDA (x)	FY08E	9.5	7.3	6.5
	FY09E	10.1	7.0	6.4

SHAREHOLDING PATTERN (%)

	SEP-07	JUN-07	SEP-06
Promoter	64.2	64.2	66.1
Domestic Inst	1.2	1.2	1.7
Foreign	2.6	2.5	0.2
Others	32.0	32.1	32.0

Key investment risks

- ✍ Unexpected fall in steel prices would adversely impact the earnings.

Recent developments

- ✍ The company had recently signed an MoU with L&T and Paulwirth for the supply of a 2.5mtpa blast furnace worth Rs12b to expand the capacity further to 4mtpa (phase 3) at Orissa site.

Valuation and view

- ✍ The stock is trading at PE of 10x FY09 and EV/EBITDA of 10.1x FY09. We maintain **Sell**

Sector view

- ✍ We maintain our view that business dynamics are moving in favor of Indian steel producers that have much better iron ore linkages. Indian steel producers are key beneficiary of rising iron ore prices and softening coking coal prices. We maintain our positive view on the Indian steel industry.

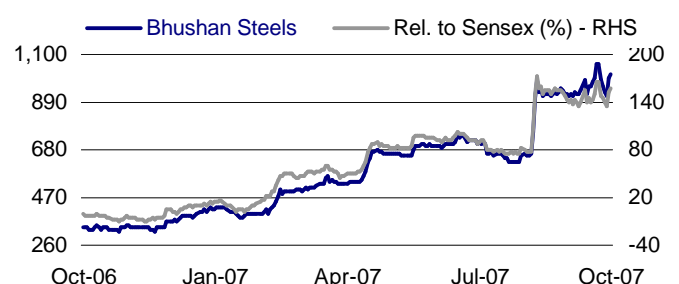
EPS: MOST FORECAST V/S CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY08	97.0	89.1	8.9
FY09	101.8	103.6	-1.7

TARGET PRICE AND RECOMMENDATION

*CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
1,016	-	-	Sell

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT						RATIOS						
Y/E MARCH	2005	2006	2007	2008E	2009E	Y/E MARCH	2005	2006	2007	2008E	2009E	
Net sales	26,750	27,940	38,377	47,316	51,198	Basic (Rs)						
Change (%)	71.0	4.4	37.4	23.3	8.2	EPS	37.9	37.4	73.8	97.0	101.8	
Total Expenses	22,721	24,081	32,096	39,125	42,163	Cash EPS	78.6	77.6	123.0	153.5	167.8	
Raw materials	20,444	21,437	28,301	34,779	37,378	BV/Share	170.5	205.6	274.5	367.4	464.6	
% of Net Sales	76.4	76.7	73.7	73.5	73.0	DPS	2.5	2.5	3.0	3.5	4.0	
Power & Fuel	1,083	1,266	1,636	1,840	1,731	Payout (%)	7.5	7.7	4.8	4.2	4.6	
Employee Cost	233	360	283	506	770	Valuation (x)						
Other Manufac. Exp.	960	1,019	1,876	1,999	2,284	P/E		27.1	13.8	10.5	10.0	
EBITDA	4,030	3,859	6,281	8,191	9,035	Cash P/E			13.1	8.3	6.6	6.1
% of Net Sales	15.1	13.8	16.4	17.3	17.6	P/BV		4.9	3.7	2.8	2.2	
Deprn. & Amortization	1,647	1,658	2,089	2,400	2,800	EV/Sales		2.2	1.8	1.6	1.8	
EBIT	2,382	2,201	4,192	5,791	6,235	EV/EBITDA		15.9	11.3	9.5	10.1	
Net Interest	794	754	773	1,200	1,400	Dividend Yield (%)		0.2	0.3	0.3	0.4	
Other income	68	149	304	304	304	Return Ratios (%)						
PBT before EO	1,657	1,597	3,724	4,895	5,139	EBITDA Margins	15.1	13.8	16.4	17.3	17.6	
EO income						Net Profit Margins	5.7	5.5	8.2	8.7	8.4	
PBT after EO	1,657	1,597	3,724	4,895	5,139	RoE	22.2	18.2	26.9	26.4	21.9	
Tax	123	52	591	776	815	RoCE	11.2	7.4	9.8	10.8	8.8	
Rate (%)	7.4	3.3	15.9	15.9	15.9	RoIC	14.0	13.8	23.7	30.7	17.0	
Reported PAT	1,534	1,545	3,133	4,119	4,325	Working Capital Ratios						
Minority interests						Asset Turnover (x)	13	0.9	0.9	0.9	0.7	
Preference dividend						Debtor (Days)	46	53	55	55	55	
Adjusted PAT	1,534	1,545	3,133	4,119	4,325	Inventory (Days)	79	62	70	70	70	
Change (%)	69.8	0.7	102.8	31.5	5.0	Leverage Ratio (x)						
BALANCE SHEET						Current Ratio	2.7	2.2	2.5	2.4	2.3	
Y/E MARCH	2005	2006	2007	2008E	2009E	Interest Cover Ratio	3.0	2.9	5.4	4.8	4.5	
Share Capital	405	413	425	425	425	Debt/Equity	1.9	2.3	2.4	2.2	2.4	
Reserves	6,901	8,484	11,660	15,605	19,731	<i>E: M OSt Estimates</i>						
Share holders funds	7,306	8,897	12,084	16,030	20,156	CASHFLOW STATEMENT						
Loans	13,175	20,362	29,362	36,362	49,362	Y/E MARCH	2005	2006	2007	2008E	2009E	
Deffered tax liability (net)	749	663	1,237	1,463	1,699	Pre-tax profit	1,657	1,597	3,724	4,895	5,139	
Capital Employed	21,229	29,922	42,683	53,854	71,216	Depreciation	1,465	1,650	2,089	2,400	2,800	
Gross Block	16,578	17,959	18,959	20,959	40,959	(Inc)/Dec in Wkg. Cap.	-1,540	777	-2,819	-1,592	-691	
Less: Accum. Deprn.	6,108	7,758	9,848	12,248	15,048	Tax paid	-131	-138	-17	-551	-578	
Net Fixed Assets	10,470	10,201	9,112	8,712	25,912	CF from Op. Activity	1,451	3,886	2,977	5,153	6,670	
Capital WIP	3,857	12,952	22,952	32,952	32,952	(Inc)/Dec in FA +CWIP	-5,144	-10,476	-11,000	-12,000	-20,000	
Investments	190	192	192	192	192	CF from Inv. Activity	-5,144	-10,478	-11,000	-12,000	-20,000	
Curr. Assets	10,683	12,019	17,401	20,441	21,242	Equity raised/(repaid)		8	204			
Inventories	5,817	4,748	7,360	9,074	9,819	Debt raised/(repaid)	3,869	7,187	9,000	7,000	13,000	
Sundry Debtors	3,394	4,045	5,783	7,130	7,715	Dividend (incl. tax)	-114	-119	-149	-174	-199	
Cash and Bank	174	815	1,847	1,826	1,297	CF from Fin. Activity	3,754	7,233	9,055	6,826	12,801	
Loans and Advances	1,298	2,411	2,411	2,411	2,411	(Inc)/Dec in Cash	61	641	1,032	-21	-529	
Curr. Liability & Prov.	3,970	5,442	6,973	8,443	9,081	Add: opening Balance	113	174	815	1,847	1,826	
Sundry Creditors	3,504	4,778	6,309	7,778	8,416	Closing Balance	174	815	1,847	1,826	1,297	
Other Liabilities & prov.	466	665	665	665	665							
Net Current Assets	6,712	6,577	10,428	11,999	12,161							
Application of Funds	21,229	29,922	42,683	53,854	71,216							

N O T E S



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Bhushan Steel

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|---|----|
| 1. Analyst ownership of the stock | No |
| 2. Group/Directors ownership of the stock | No |
| 3. Broking relationship with company covered | No |
| 4. Investment Banking relationship with company covered | No |

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