

INDUSTRY
STEEL

VISA STEEL LIMITED

TURNING POINT

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VISA Steel Ltd. (Visa Steel), a part of ₹ 5000 crore VISA Group, is an emerging integrated specialty steel company. It is engaged in the manufacturing of pig iron, lam coke, ferro chrome, sponge iron, captive power and soon entering into special steel products with its operations in Orissa and Chhattisgarh. **Currently the stock is quoting at 8.4x on TTM EPS of ₹ 4.2. We give BUY rating on Visa Steel Limited at current levels with FY12 price target of ₹ 52, an upside of 47%.**

Investment Rationale

Growth Prospects: The management is expecting to double its sales to ₹ 2400 crore by FY12. EBITDA for FY10 is ₹ 198 crore with EBITDA margin at 16.8%. The management expects to improve its EBITDA by about 127% to ₹ 450 crore by FY12 with EBITDA margin at 18.7%. The company has taken measures to control costs which will result in an improvement in its profitability.

Raw Materials: The raw material prices have been a major concern for the steel industry and therefore the company has opted for captive mineral resources.

Captive Mineral Resources:

Coal:	54 mn tons Steam Coal Block at Patrapara in Talcher, Orissa to be operational by FY13
Iron Ore:	Lease under process in Orissa & Chhattisgarh, expected to be operational in a few months
Chrome Ore:	Developing a deposit in Orissa through Ghotaringa Minerals Ltd. (a subsidiary), expected to be operational by FY14.

In the mean time, company has following tie-ups by :

Current Raw Material Linkages:

Coking Coal:	Long term purchase agreement with BHP at quarterly prices
Steam Coal:	Agreement with Mahanadi Coalfields with Linkage price
Chrome Ore:	Tie up with OMC at quarterly price

Fundamental Stock Idea

Rating	BUY
Target Price	₹ 52
CMP	₹ 35.85
Upside	47%
Sensex	₹ 18,286

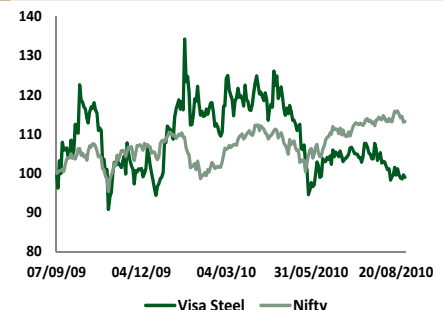
Key Data	
Bloomberg Code	VISA IN
Reuters Code	VISA.BO
NSE Code	VISASTEEL
Current Share o/s (mn)	110.0
Diluted Share o/s (mn)	110.0
MktCap (₹bn/\$mn)	3.9/83.2
52 WK H/L (₹)	50.3/31
Daily Vol. (3M NSE Avg)	215143
Face Value (₹)	10
Beta	1.25
1USD/₹	46.9

Shareholding Pattern (%)	
Promoters	73.0
FII	4.8
Others	22.2

Price Performance (%)			
	1M	6M	1yr
VISA	-8.2	2.2	8.4
NIFTY	1.5	9.6	17.7

Source: Bloomberg; *As on 1st Sept. 2010

Price Chart



Source: Company, Networth Research

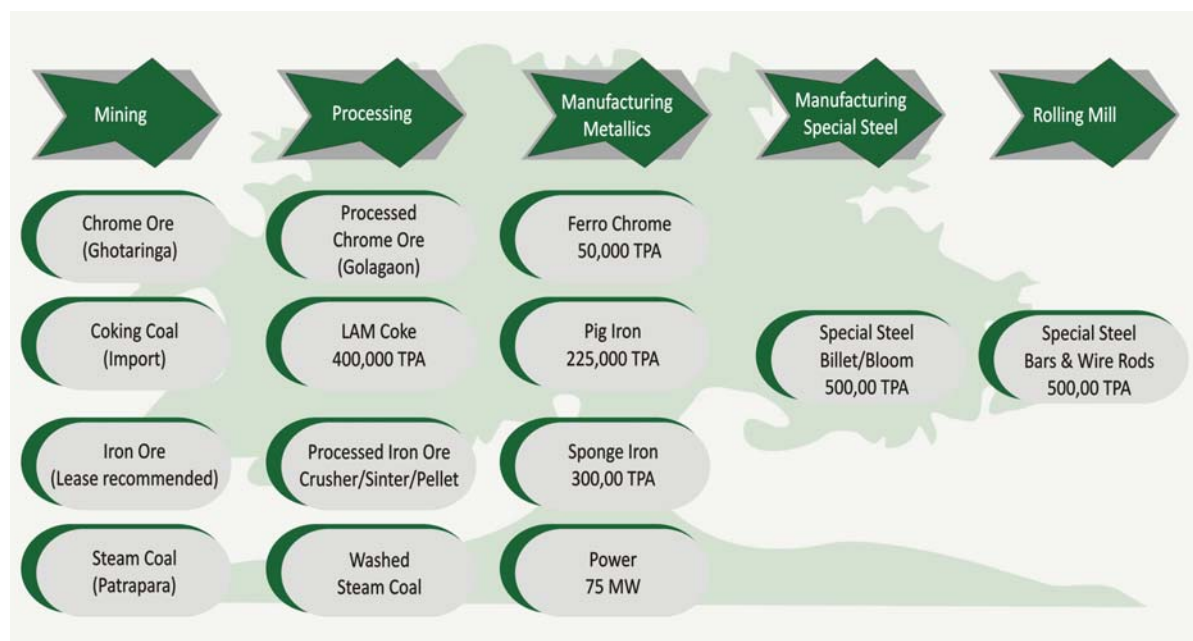
Power: Currently the company has captive capacity of 50MW and is building captive power plant with a capacity of 25mw, which is expected to complete by 3Q FY11. Also the company is planning to build two power projects with a capacity of 300 mw each at Orissa and Chhattisgarh.

Location & Logistics: All the plants of Visa Steel enjoy the advantage of strategic locations in terms of mining resources, water as well as connectivity through ports and railways. Therefore the transportation costs will reduce significantly. The following are the details of the proximity of the projects to the vital resources, ports and railway stations.

Raw Material		
	Orissa	Chattisgarh
Iron Ore	Daitari: 30km	200km
Coal	Pradip: 120km (Coking)	50 km
	Talcher: 110km (Steam)	
Chrome Ore	Sukinda: 35km	
Infrastructure		
	Orissa	Chattisgarh
Port	Pradip: 120km	
Rail	Kolkata-Chennai Line: 2km	Kotarlia: less than 1km
Power	Duburi Grid: 10 km	Kotra Grid: 25km
Water	Brahmani River: 5km	Sapnai: 1km

Integrated Value Chain:

Visa Steel will have an integrated value chain from mining minerals to manufacture of finished products after 3Q FY11 as shown in the diagram.



Capex Plans:

The following are the projects under implementation:

PROJECTS	CAPACITY	PROGRESS
Steel Melt Shop (SMS)	0.5 mtpa	99%
Rolling Mill	0.5 mtpa	85%
Visa BAO Ferro Chrome Plant	0.1 mtpa	10%

The Steel Melt Shop and the Rolling Mill are expected to be completed by 3Q FY11 while the Ferro Chrome Plant is expected to be completed by 3Q FY12. The production process will go on the floors as and when the projects get completed.

Also the company is planning to build two rolling Mills at Orissa and Chhattisgarh with a capacity of 0.5 mtpa and 1 mtpa respectively.

Once the Rolling Mill is commissioned in 3Q FY11, the company will start producing steel billets and blooms.

Price Outlook

The metal industry was badly hit in recession mainly because of collapse in realization prices. However, it is believed that the worst phase is over on the back of following reasons:

- **Steel** prices have bottomed out and have started firming up. Steel billets are currently trading at USD 500 (per ton) on LME and as per our technical analysis, are expected to reach target levels of USD 600 in two months' time, while support exists at level of USD 400.
In India, steel prices are hovering in the range of ₹ 30000 – 35000 per ton. Many domestic steel players have announced an increase in steel prices by ₹ 1000 – 1500. In Europe, prices are expected to pick up from September while prices in the US would increase in November.
- As far as **Coke** prices are concerned, China has been a threat. However export taxes in China have been raised to 40%, resulting in negligible exports. Therefore coking coal prices are likely to remain stable in FY11.
- **Ferro chrome** consumption has increased as global stainless production is shifting from austenitic to ferritic grade. 40% of global ferro chrome production is from South Africa, however, due to power shortages, there has been a reduction in its supply. As a result, ferro chrome prices are expected to remain firm.

With improvement in market prices of steel, coke and ferro chrome, Visa Steel is will achieve better realization and thereby improved profitability.

Strong Demand For Steel

The company expects to double its sales to ₹ 2400 crore by FY12. The company management is of the view that despite of the global slump, the **demand for steel seems promising**.

- The **automobile industry** is growing at over 14% per annum and is emerging as a global hub for outsourcing of auto components. This will result in higher demand of steel products.
- The Government has been taking a lot of **Infrastructure development projects** especially power, roads, railways, and construction projects. So this will directly and indirectly result in higher demand.
- The **engineering sector** including Agriculture and Industrial machinery as well as Oil & Gas sector for its exploration and transportation will require steel.

- Finally the **Railway & Defense sectors** are also major users of steel.
- The **major clients** of the company are: Mahindra, TVS, Ashok Leyland, Tata Motors, Eicher, Bajaj, Hero Honda & General Engineering MRF, JK, Apollo, L&T, Gammon, Hindustan Construction, NHAI, Railways which will drive volumes in coming quarters.

Rocky Patch Left Behind

In 1Q FY11, there was a disruption in supply of Iron Ore as the mines of OMC, Orissa were shut for 5-6 months on environmental grounds. Moreover, the company could not rely on any other source for Iron Ore for logistic reasons and it was not feasible to move the blast furnace to any other place. As a result, hot metal production was NIL. However this problem is not expected to continue as the mines are expected to start in September 2010.

Also production of Coke in 1Q FY11 was deliberately lowered as a precautionary measure due to declaration of force majeure by BHP Billiton. However in 2Q, the production will be normal as the supply of coal has reached normal levels.

Major Concern: High Gearing Ratio

The debt of the company stood at ₹ 1057 as on March 31, 2010 and pays an interest of 11%. The company has a high debt equity ratio of 3:1. The company management says that the debt levels are high due losses incurred in FY09 and they expect to improve its leverage by 2012.

Consolidated Profit & Loss a/c of Visa Steel Ltd			(₹ Cr.)
Particulars	FY10	FY09	FY08
Net Sales	1156.94	1035.01	680.77
Other Operating Income	14.54	5.45	2.04
Total Income	1171.48	1040.46	682.81
Materials	813.66	810.24	484.70
Expenses	161.32	149.51	104.20
	974.98	959.75	588.90
EBITDA	196.50	80.71	93.91
EBITDA Margins (%)	17%	8%	14%
Depreciation & Amortization	46.83	30.79	18.26
EBIT	149.67	49.92	75.65
Interest & Financial Charges	60.28	29.63	8.51
EBT	89.39	20.29	67.14
Loss on Exchange Fluctuation	0.00	118.46	0.00
Tax	39.52	-32.18	23.99
PAT	49.87	-65.99	43.15
PAT Margins	4%	-6%	6%

Consolidated Balance Sheet of Visa Steel Ltd.

(₹ Cr.)

Particulars	FY10	FY09	FY08
SOURCES OF FUNDS			
Share Capital	110.00	110.00	110.00
Reserves & Surplus	207.95	170.69	236.97
Shareholders' Funds	317.95	280.69	346.97
Minority Interest	33.70	32.23	0.11
Secured Loan	1107.70	889.17	698.77
Unsecured Loan	35.04	3.80	0.00
Loan Funds	1142.74	892.97	698.77
Deferred Taxation	30.11	1.45	34.92
	1524.50	1207.34	1080.77
APPLICATION OF FUNDS			
Net Block	813.83	778.15	391.35
Capital WIP	772.84	541.59	605.12
Fixed Assets	1586.67	1319.74	996.47
Current Assets, Loans & Advances			
Inventories	341.71	356.51	278.83
Sundry Debtors	64.88	82.37	96.34
Cash & Bank Balances	136.47	134.25	86.10
Interest accrued on Deposits	3.74	3.57	1.95
Loans & Advances	141.43	122.92	97.58
	688.23	699.62	560.80
Less: Current Liabilities & Provisions			
Liabilities	738.91	816.42	470.92
Provisions	13.95	0.73	13.39
	752.86	817.15	484.31
Net Current Assets	-64.63	-117.53	76.49
Miscellaneous Expenditure	2.46	5.13	7.81
	1524.50	1207.34	1080.77

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Key to NETWORTH Investment Rankings

Buy: Upside by>15, **Accumulate:** Upside by +5 to 15, **Hold:** Upside/Downside by -5 to +5, **Reduce:** Downside by 5 to 15, **Sell:** Downside by>15

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