

VISA STEEL (VISST)

Rs 38

WHAT'S CHANGED...

PRICE TARGET Changed from Rs 52 to Rs 45
 EPS (FY09E) Changed from Rs 6.7 to Rs 5.0
 EPS (FY10E) Changed from Rs 15.4 to Rs 10.4
 RATING..... Changed from STRONG BUY to BUY

Operational bottlenecks drag performance...

Visa Steel reported disappointing numbers for Q1FY11. Topline of the company was reported at Rs 220.5 crore (down ~13% and ~45% on YoY and QoQ respectively), way below our expectations of Rs 349.9 crore. This was due to shut down of the pig iron plant on no supply of blast furnace grade iron ore from OMC and also lower sales volume QoQ in other product categories. Average realisations however improved QoQ for all products barring pig iron due to higher scrap mix. Despite lower captive consumption, coke sales volume saw a decline (down 15% QoQ and YoY) due to shutdown of many blast furnaces in the eastern region during Q1FY11. EBITDA margin came at ~18% (up 60 bps QoQ and 550 bps YoY), while bottomline for Q1FY11 came at Rs 7.6 crore (down 54% QoQ and 24% YoY) against our expectations of Rs 14.5 crore. We revise our target price to Rs 45/ share with a BUY rating.

Operational bottlenecks dragged topline

Temporary closure of OMC mines had impacted the production volumes (blast furnace is still kept shut) with no pig iron production during Q1. Declaration of force majeure by BHP Billiton for 20- 25 days disrupted coking supply and thereby coke production. Coke sales were also affected due to closure of some blast furnaces in the Eastern India on lack of iron ore availability hitting the topline.

Higher realisation helped improving margin

Higher realisations across all the product segments viz. coke (up 25% QoQ and 37% YoY), ferro chrome (up 11% QoQ and 42% YoY) and sponge Iron (up 31% YoY) except pig iron (down 22% QoQ and 5% YoY) helped margins to improve by 60 bps even on QoQ. basis.

Valuation

At the CMP of 38, the stock is discounting its FY12E earnings EPS by 4.8x. On the other hand, it also discounts FY12E EV/ EBITDA by 4.8x. At this point we value the stock at 5x FY12E EV/ EBITDA to arrive at a target price of Rs 45/ share. We assign a **BUY** rating on the stock.

Exhibit 1: Financial performance

(Rs Crore)	Q1FY11	Q1FY11E	Q1FY10	Q4FY10	YoY (Chg %)	QoQ (Chg %)
Net Sales	220.5	349.9	254.1	407.3	-13.2	-45.9
EBITDA	38.9	61.6	30.8	69.1	-26.2	-43.7
EBITDA Margin (%)	17.6	17.6	12.1	17.0	+550 bps	+60 bps
Depreciation	12.0	18.6	11.0	11.8	9.3	2.0
Interest	16.9	16.5	11.1	26.7	53.0	-36.7
Reported PAT	7.6	14.6	10.1	16.5	-24.3	-53.8
EPS (Rs)	0.7	1.3	0.9	1.5	-24.3	-53.8

Source: Company, ICICIdirect.com Research

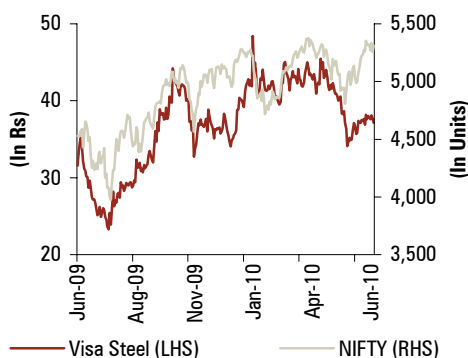
Rating matrix	
Rating	: Buy
Target	: Rs 45
Target Period	: 12 months
Potential Upside	: 18 %

Key Financials				
(Rs Crore)	FY09	FY10	FY11E	FY12E
Net Sales	1035.0	1156.9	1123.9	1743.9
EBITDA	-38.0	197.6	229.7	357.2
Net Profit	-66.8	47.4	54.8	114.8

Valuation summary				
	FY09	FY10	FY11E	FY12E
PE (x)	NA	8.6	7.5	3.6
Target PE (x)	NA	12.1	10.4	5.0
EV/EBITDA (x)	NA	6.8	6.9	4.8
P/BV (x)	1.5	1.2	1.1	0.8
RoNW (%)	-23.8	14.5	14.3	23.1
RoCE (%)	-5.2	14.3	9.9	15.3

Stock data	
Market Capitalisation	Rs 409.8 Crore
Debt-Cons. (FY10)	Rs 1043 crores
Cash & Invst.-Cons. (FY10)	Rs 114 crores
EV	Rs 1338.5 Crore
52 week H/L	50.2/25.2
Equity capital	Rs 110 Crore
Face value	Rs 10
DII Holding (%)	0.03
FII Holding (%)	4.8

Price movement



Analyst's name

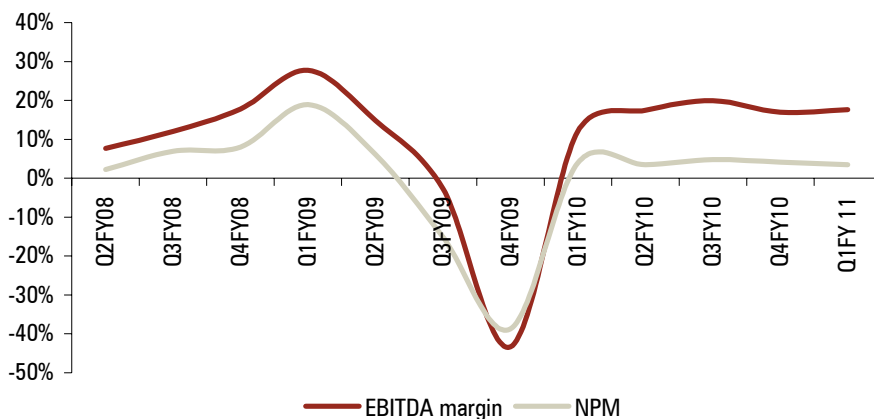
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Result Analysis

The top line of the company came at 220.5 crore, much lower than our estimates of ~Rs 350 crore. On both YoY and QoQ basis top line fell by 13% and 45% respectively. EBITDA margins though improved YoY by 520 bps, however, declined by 280 bps QoQ to Rs 17.3%. Reduction in other expenses by 42% QoQ prevented further erosion on the margin front. Following the fall in topline, PAT also declined to Rs 7.6 crore (down 54% QoQ and 24% YoY).

The top line registered decline both on a QoQ and YoY basis. However EBITDA margins improved by 550 bps and 60 bps respectively, as raw material costs as a percentage to net sales fell to ~82% in Q1FY11 from 83% and ~87% on QoQ and YoY respectively

Exhibit 2: Margins remain stable

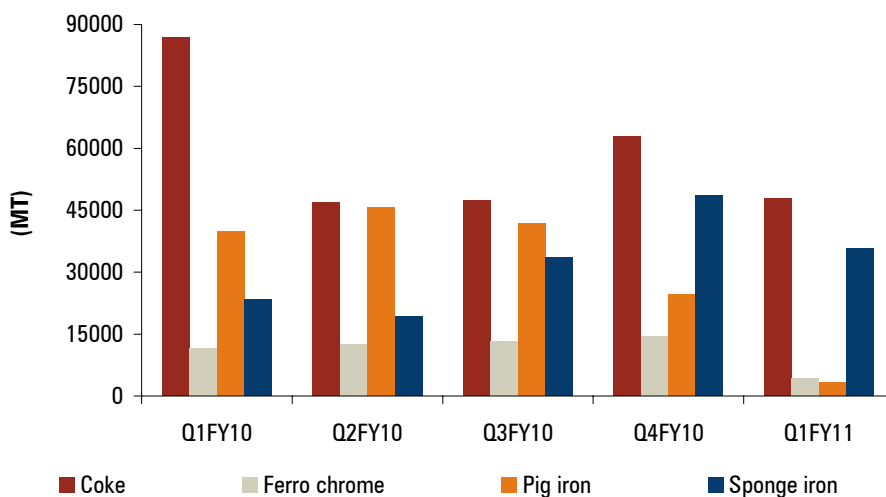


Source: Company data, ICICIdirect.com Research

Sales volume registered decline YoY in all categories except sponge iron, which saw a decent jump of 52% in sales volume. Ferro chrome (down 62% YoY and 71% QoQ), coke (down 45% YoY and 24% QoQ) and pig iron (down by 92% YoY and 86% on QoQ basis) led to muted topline performance during Q1FY11.

Volumes declined YoY and QoQ across all the product categories except sponge Iron due to various operational bottlenecks observed during the quarter

Exhibit 3: Sales volumes dip across all products except sponge iron



Source: Company, ICICIdirect.com Research

Operational bottlenecks to ease

Realisations improved across all the categories except the pig Iron segment both on a QoQ and YoY basis. Coke sales contributed significantly to the top line in the quarter with healthy realization levels. Coke production was lower due to declaration of force majeure by BHP Billiton as a precautionary measure to combat cyclone storm in Australia during early part of the quarter. Production however is expected to improve in Q2 FY2011 since supply of coal has reached normal levels. Blast furnace and sponge iron production was hampered due to disruption in supplies of iron ore due to temporary closure of OMC mines. Though, the sponge iron grade mine has started operating, however, the blast furnace grade mines are still to restart production. Some normalcy is expected to return with regard to supply of BF grade iron ore during later part of Q2FY11E. Work progress on the 0.5 million TPA Steel Melt Shop (SMS) and bar and wire rod mill is on track and the additional 25MW power plant is also on schedule to be operational by Q3FY11. Though, any delay in normal iron ore supply may have negative impact on proper operation of the SMS, however, that mill is likely to be commissioned irrespective of availability of own pig iron. In that case the company would procure pig iron from the market. This is however would pull down margins. The company also has got necessary permission for coal mining in Patrapada coal mine (its reserve share is 54 mt) and the benefit is likely to flow from FY13. Thus, going forward we expect better performance by the company as the recent operational glitches are likely to ease.

Product prices are likely to remain stable across all the categories

Exhibit 4: Realisations show modest rise

Product	Realisation (Rs/ tonne)	Change (%)	
		YoY	QoQ
Coke	20517	43.5	25.1
Ferro chrome	62689	60.7	10.9
Sponge iron	14456	19.5	1.4
Pig iron	15221	-3.7	-21.7

Source: Company data, ICICIdirect.com Research

Valuations

On the macro economic front the demand for iron and steel products in the last quarter remained subdued due to the European debt crisis and slowdown in China due to its effort to cool off its overheating property market. Some improvement has been seen in that regard in the past couple of weeks, however concerns are still there. We are not very optimistic on the improvement of global macro economic scenario, however, India is likely to continue witnessing good demand growth, which is evident from the GDP growth forecast of 8.5%- 9.0% for FY11. This is likely to help domestic companies to stay at a better position compare to their global peers.

Looking at Visa Steel, with forward integration of SMS, bar and wire rod mill, additional power generation, and better raw material availability the company is likely to show better performance going forward. Near- term concerns persists however, in terms of delay in normalcy with regard to availability of BF grade iron ore and its impact on the upcoming 0.5 mt SMS.

Taking into account the above scenario and factoring in all the concerns on a conservative basis we have revised down our earning estimates for the company for both FY11E and FY12E.

Exhibit 5: Revised earnings

Before revising		After revising	
FY11E	FY12E	FY11E	FY12E
6.7	15.4	5.0	10.4

Source: Company, ICICIdirect.com Research

At the CMP of 38, the stock is discounting its FY12E earnings EPS by 4.8x. On the other hand, it also discounts FY12E EV/ EBITDA by 4.8x. Though, the company has the significant growth potential from Q4FY11 onwards after the commissioning of bar and wire rod mill, we would like to remain cautious on the execution part. At this point we value the stock at 5x FY12E EV/ EBITDA to arrive at a target price of Rs 45/ share. We assign a **BUY** rating on the stock.

Exhibit 6: Valuation matrix

	Sales *	EPS (Rs)	PE (x)	EV/EBITDA (x)	P/ BV (x)	RoNW (%)	RoCE (%)
FY09	1035.0	-6.1	NA	NA	1.5	-23.8	-5.2
FY10E	1156.9	4.3	8.6	6.8	1.2	14.5	14.3
FY11E	1123.9	5.0	7.5	6.9	1.1	14.3	9.9
FY12E	1743.9	10.4	3.6	4.8	0.8	23.1	15.3

Source: Company, ICICIdirect.com Research; * Sales in Rs crore

ICICIdirect.com coverage universe (Metals & Mining)

				Sales (Rs Cr)	EPS (Rs)	PE (x)	EV/EBITDA (x)	RoNW(%)	RoCE(%)	
Adhunik Metaliks										
Idirect Code	ADHMET	CMP (Rs)	111.3	FY09	1270.3	5.1	21.8	10.4	13.3	9.1
		Target (Rs)	134.0	FY10	1449.7	11.1	10.0	6.4	17.5	14.1
		Upside (%)	20.4	FY11E	1743.8	13.7	8.1	5.7	18.1	16.2
MCap (Rs Cr)	1374.1			FY12E	1873.0	16.0	8.4	5.1	17.9	16.3
JSW Steel										
Idirect Code	JINVIJ	CMP (Rs)	1,112.6	FY09	16081.5	14.7	75.7	11.8	3.5	9.3
		Target (Rs)	1,298.0	FY10	19073.8	85.4	13.0	8.8	17.3	13.0
		Upside (%)	16.7	FY11E	21744.0	91.8	12.1	7.7	15.3	13.4
MCap (Rs Cr)	20811.2			FY12E	30676.8	123.1	10.5	5.5	20.9	17.1
Usha Martin										
Idirect Code	USHBEL	CMP (Rs)	84.4	FY09	2949.8	6.6	12.8	7.4	14.6	13.9
		Target (Rs)	98.0	FY10	2534.4	5.5	15.3	7.2	10.0	13.4
		Upside (%)	16.1	FY11E	3318.3	9.0	9.4	5.6	14.2	16.0
MCap (Rs Cr)	2577.6			FY12E	3697.0	11.5	8.5	4.5	15.6	18.0
Visa Steel										
Idirect Code	VISST	CMP (Rs)	37.6	FY09	1035.0	-6.1	NA	NA	NA	NA
		Target (Rs)	45.0	FY10	1156.9	4.3	8.7	6.8	14.5	14.3
		Upside (%)	19.7	FY11E	1123.9	5.0	7.6	6.9	14.3	9.9
MCap (Rs Cr)	409.8			FY12E	1743.9	10.4	4.3	4.8	23.1	15.3
Tata Steel - Cons										
Idirect Code	TISCO	CMP (Rs)	540.6	FY09	145686.3	67.8	8.0	4.5	17.4	15.0
		Target (Rs)	517.0	FY10	101757.8	-22.6	-23.9	11.1	-7.1	4.2
		Upside (%)	-4.4	FY11E	112789.4	42.6	12.7	7.1	12.3	10.2
MCap (Rs Cr)	47930.6			FY12E	123045.4	62.0	8.7	5.5	15.6	12.8
SAIL										
Idirect Code	SAIL	CMP (Rs)	199.0	FY09	43639.7	14.9	13.3	6.1	32.7	37.4
		Target (Rs)	232.0	FY10	41307.2	16.4	12.2	7.9	22.1	21.0
		Upside (%)	16.6	FY11E	41897.7	15.0	13.3	7.5	20.4	16.9
MCap (Rs Cr)	82195.0			FY12E	55297.3	19.7	10.1	6.6	18.4	15.5
Sesa Goa										
Idirect Code	SESGOA	CMP (Rs)	372.2	FY09	4959.1	25.3	14.7	9.9	42.1	51.9
		Target (Rs)	397.0	FY10	5858.3	31.6	11.8	8.2	33.2	30.7
		Upside (%)	6.7	FY11E	9889.1	56.0	6.6	4.0	35.6	38.1
MCap (Rs Cr)	30925.7			FY12E	11029.3	59.5	6.3	3.1	27.9	29.9
Hindustan Zinc										
Idirect Code	HINZIN	CMP (Rs)	1,072.3	FY09	5680.3	64.6	16.6	12.4	20.8	19.8
		Target (Rs)	1,117.0	FY10	8017.0	95.6	11.2	7.1	24.7	27.2
		Upside (%)	4.2	FY11E	8906.9	94.0	11.4	6.6	19.3	20.8
MCap (Rs Cr)	45307.9			FY12E	10924.3	122.6	8.7	4.2	20.7	22.9
Sterlite Industries										
Idirect Code	STEIND	CMP (Rs)	178.2	FY09	21144.2	12.5	14.3	7.1	14.8	16.4
		Target (Rs)	189.0	FY10	24410.3	11.1	16.0	7.1	12.0	15.0
		Upside (%)	6.1	FY11E	27117.8	13.7	13.0	6.3	11.8	13.9
MCap (Rs Cr)	59903.7			FY12E	39492.3	24.4	7.3	3.1	18.3	19.3
GPIL										
Idirect Code	GODPOW	CMP (Rs)	235.8	FY09	1092.0	22.8	10.3	7.2	14.6	13.6
		Target (Rs)	279.0	FY10E	822.4	20.8	11.3	7.2	11.7	11.3
		Upside (%)	18.3	FY11E	1015.5	42.5	5.6	3.9	20.3	19.0
MCap (Rs Cr)	636.6			FY12E	1086.9	55.8	4.2	2.7	21.9	20.4

Source: Company, ICICIdirect.com Research

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Buy: Between 10% and 20%;
Add: Up to 10%;
Reduce: Up to -10%
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