

## Sarda Energy Ltd

9 February 2017

 BSE: 504614 | Sector: **Steel-Sponge Iron**
**vScore : 60** | **Gain%: 23.29%**
**Buy Date: 09-Feb-2017** | **Buy Price : Rs. 249.00**
**Exit Date: 24-July-2017** | **Exit Price : Rs. 307.0**

### BUSINESS BACKGROUND

Sarda Energy & Minerals Limited is a producer of steel and ferro alloys. The Company is engaged in the manufacturing and selling of pellets, sponge iron, steel billets, wire rod, wire and ferro alloys from its plant located at Raipur, Chhattisgarh. Its segments include Steel, Ferro and Power. It produces sponge iron for its own captive use to produce steel ingots and billets through induction furnace route. It produces and exports manganese-based ferro alloys with exports to 60 countries. Ferro alloys are produced in sub-merged arc furnaces using electro-thermic process. It manufactures bricks mainly from the fly-ash generated from its captive power plant. The Company operates an 81.5 megawatt (MW) thermal power plant at its Siltara plant. The energy generated is used in its sponge iron, billet, ingot and ferro alloys plants. The Company produces pellets from iron ore fines using grate-kiln technology. The pellets are used in house for production of direct reduced iron (DRI).

### INVESTMENT HIGHLIGHTS

**Q2FY17 results:** It recorded sales of INR 330 Cr, compared to INR 318 in Q2FY16, EBITDA of INR 73Cr compared to INR 59 Cr in Q2FY16. Net profit of INR 37.6 Cr compared to 29.4 Cr in Q2FY16. Adj. EPS: INR 8.6/share compared to INR 6.7/share last year same quarter. (All figures are on standalone basis.)

### Segment Highlights:

The company as operations in mainly three segments Steel, Ferro Alloys, Power. For first half of FY17, from the overall revenue Steel segment contributed around 55-60%, Ferro Alloys contributed around 30-33% and 10-12% was contributed by Power segment.

### KEY DATA

FACE VALUE	Rs	10
DIVD YIELD %		2
52 WK HI/LOW		76/296
NSE CODE		SARDAEN
MARKET CAP	Rs.	890 Cr

### SHAREHOLDING PATTERN-DEC16

PROMOTERS	-	71.20%
BANKS, MFs & DIs	-	0.48%
FIs	-	2.31%
Others	-	26.01%

### KEY FUNDAMENTALS

Year Ending	FY16A	FY17E	FY18E
Rev Gr%	-15	-4	3
Net Profit Gr%	-70	540	-
ROE%	2	8	6
RoCE %	6	8	9
EPS (Rs)	4	27	21
P/E (x)	-	9	12

**A well integrated steel product company and reduction in debt level is providing comfort:**

The company is one of the lowest cost producer of Steel parts and manufacture plus exporter of Ferro Alloys. The steel products of the company include pellets, sponge iron, wire rods, TMT bars. The company is well integrated since from mining iron ore to manufacture of wire rods and plus has its own thermal power. It saves lot of cost for them.

As the company operates in Steel related sector, it is subject to affect from global prices of these materials and their raw materials. Revenues of the company have not really gone anywhere in last 3 years due to fluctuating steel and other metal prices.

For the first two quarters the company has posted good numbers, the overall operating margin has improved from around 13% levels to 15%. The debt level of the company is coming down and hence overall interest cost for first two quarters was down by almost 30-35% compared to last year. This trend is expected to be there for next 2 quarters as well. The company also recorded exceptional gain of assets in Q1 (63 Cr) which has also helped them to record higher earnings in first quarter and which will help them for overall higher EPS for entire year. Ferro alloys division is also expected to do well for rest of the year since there is already a price hike by major players in the country.

**Overall government support of MIP and other majors will continue to support overall steel related sectors and infra-construction boost and increasing automobile demand again post demonetisation can further improve the demand of Steel related products in coming quarters:**

The company's main product is Steel related parts for various sectors. The overall improvement in domestic steel related demand is a trigger of growth for the company. In recent times government has put Minimum Import Price restrictions for steel related products to protect domestic players from cheaper production of China and other country. This has started helping them in terms of overall pricing and domestic supply. The oversupply of products was earlier a problems due to many products from other countries but after this move it has been addressed to a certain extent.

The government has again focused on speeding up overall infra and construction activities from recent budget to increase the overall growth rate of country's GDP and improve overall job creations and Industrial activities post the demonetisation event. This will help the Steel-related production companies in medium to long term to get more demand for such products.

Earlier there was a fear of sales slowdown after demonetisation was announced, but looking at most of the company's sales numbers it is visible that post those 2 months again demand is coming to normal levels which is

visible from the sales numbers of front line companies such as Maruti, Eicher and some other companies from Steel sector. Also infrastructure and construction related (Road, Railways and other infrastructure) companies will see more contracts in next few quarters which will also increase the overall steel and related products demand.

## Business Outlook and Valuation :

At the moment at current price of 246 the stock is trading at FY17 forward P/E of 8-10 times. Going ahead we expect revenue growth of -4% for FY17 and 3-4% FY18. Hence our expectations for revenue for FY17 and FY18 are INR 1426 Cr and INR 1469 Cr respectively.

We expect company to maintain EBITDA margin around 15-16% for next two years. Going ahead we expect PAT margins of 5-7% for next two years. Our PAT expectations for FY17 and FY18 are INR 98 Cr, INR 72 Cr respectively. Our EPS expectations for FY17 and 18 are INR 27, INR 21 respectively.

The consolidated book value of the company is around 337/share compared to which the share price is at a discount and trading at 246/share at the moment . We believe Sarda Energy and Minerals Ltd at forward PE of 9-10 and trailing at 30-35% discount to its book value is attractively valued. For FY17 EPS expectations of 27-28, and book value of 335-340 we expect target price of 310 with a stop loss at 215.

## FINANCIALS:

For the Year Ended March (INR)	FY15A	FY16A	FY17E	FY18E
Net Sales (Cr)	1759	1485	1426	1469
EBIDTA (Cr)	377	195	215	231
EBIDTA %	21	13	15	15.7
Profit Before Tax (Cr)	87	47	149	108
Interest (Cr)	120	108	95	89
Depreciation (Cr)	93	74	75	80
Tax (Cr)	31	31.3	50	36
Profit After Tax (Cr)	54	15.3	98.5	72.6
PAT%	3.1	1	6.9	5
Diluted EPS (INR)	15.3	4.3	27.4	20.2
Shareholder's Funds (Cr)	1209	1215	1310	1379
Borrowings (Cr)	1293	1165	1114	1069
Gross Block (Cr)	1888	1906	1999	2080

## Key Risks and Concerns:

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- Any downturn in the overall economic activity and uneven global metal prices can impact company's financials.
- Steel and related raw material product prices can create margin and sales pressure and hence can impact company financially up to certain extent though not completely. MIP if cancelled by government can create a competition again in the industry.
- Any adverse policies introduced by government can affect the overall sector and hence a company.

vScore: Value Score is our proprietary company rating system based on last 5 years of historical data and value investing philosophy at its core. v360 combined with Macroeconomic indicators, projections, fundamental and technical trigger makes it a 360 degree view.

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Source: Niveza Research Desk