Shyam Metalics and Energy

Metals

Capex is what capex does

We see Shyam Metalics and Energy (SMEL) effectively evolving on its 3C principle: Comprehensive products, Capex focus and Cost efficiencies. The recently announced capex plan of INR 39bn illustrates the company's sharp focus on both scope and scale. In our view, the payback period of this capex is likely to be less than 4 years, even with our estimate of declining commodity prices and EBITDA margin persisting in the range of 12-13%. Considering the headroom in balance sheet, we believe the company has enough on the table to pursue further growth opportunities. Taking cognisance of prevailing commodity prices, we trim our FY24E/FY25E EBITDA by 6% and 8% respectively. However, based on the growth potential beyond FY25E, we raise our EV/EBITDA multiple to 6x (earlier: 4.5x). Our revised target price works out to INR 690 (earlier: INR 570). Maintain **BUY**.

Capex directed in niche, value-added and adjacent areas

SMEL's recently announced capex of INR 39bn through to FY26 dovetails into the existing product range and increases the company's exposure into value-added products such as parallel flange beams, cold-rolled products and DI pipes. Besides, backward integration into iron ore beneficiation and aluminium mill with caster will likely lead to cost efficiencies. Company is also augmenting its power capacity to meet the increased internal requirement for power. We believe the capex of INR39bn could potentially lead to an additional EBITDA of INR 10.6bn p.a. (at current price levels), implying payback period of less than 4 years. As a result, EBITDA and EBITDA margin are likely to reach INR 40bn and 12.3% respectively by FY28E.

Aspirations of a conglomerate, execution of a monolith

SMEL offers a unique business model comprising longs, value-added flats, stainless steel – both flats and longs – and downstream aluminium products. Now the company is focusing on going further down the value chain, filling in the gaps left by the major players. The diversification is also an effective hedge for earnings. On the execution front, SMEL has put up its capacities in less time and less capex than peers. Besides, the management has met the capacity expansion plans detailed during the IPO and is on course to meet the capacity expansion plan it committed to in Mar'22. We believe there is sufficient headroom in the balance sheet and enough land bank to embark on further capacity expansion post FY25E.

Financial summary

Y/E March (INR mn)	FY22A	FY23A	FY24E	FY25E
Net Revenue	1,03,940	1,26,102	1,74,496	2,50,396
EBITDA	25,998	14,859	24,194	30,382
EBITDA Margin (%)	25.0	11.8	13.9	12.1
Net Profit	17,240	8,483	13,436	17,981
EPS (Rs)	67.6	33.3	52.7	70.5
EPS % Chg YoY	87.2	(50.8)	58.4	33.8
P/E (x)	6.9	14.0	8.8	6.6
EV/EBITDA (x)	4.3	7.7	4.8	3.9
RoCE (%)	34.6	12.8	15.9	17.7
RoE (%)	42.0	14.9	18.2	20.2

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Market Data

Market Cap (INR)	119bn
Market Cap (USD)	1,433mn
Bloomberg Code	SHYAMMET IN
Reuters Code	SHYE BO
52-week Range (INR)	480 /253
Free Float (%)	12.0
ADTV-3M (mn) (USD)	2.3

Price Performance (%)	3m	6m	12m
Absolute	54.4	57.7	58.9
Relative to Sensex	6.5	8.7	11.6

ESG Disclosure	2021	2022	Change
ESG score	-	-	-
Environment	-	-	-
Social	-	-	-
Governance	-	-	-

Note - Score ranges from 0 - 100 with a higher score indicating higher ESG disclosures.

Source: Bloomberg, I-sec research

Earnings Revisions (%)	FY24E	FY25E
Revenue	(6.3)	(3.2)
EBITDA	(5.7)	(8.4)
EPS	(6.4)	(8.6)

Previous Reports

29-07-2023: Q1FY24 results review
07-06-2023: Company Update

Outlook: Still a significant upside left

Despite giving an impressive return of 72% in past five months, we believe that there is still steam in the stock as the current capex has a low payback period and is expected to be RoE-accretive. We have trimmed our FY24E/FY25E EBITDA by 6% and 8% respectively, factoring-in the currently prevailing steel and raw material prices. We raise SMEL's EV/EBITDA multiple to 6x (earlier: 4.5x) taking into account the growth opportunities and our currently low margin estimates. Our revised target price works out to INR 690, implying almost 50% upside in the stock even at the current levels. Maintain **BUY**.

Exhibit 1: Earnings Revision

(INR mn)	FY24E			FY25E		
	New	Old	% Chg	New	Old	% Chg
Sales	1,74,496	1,86,327	(6.3)	2,50,396	2,58,578	(3.2)
EBITDA	24,194	25,663	(5.7)	30,382	33,156	(8.4)
PAT	13,436	14,352	(6.4)	17,981	19,683	(8.6)

Source: I-Sec research, Company data

Evolution through to FY28

Downstream focus on capacity…

At SMEL, we see unwavering focus on adding value-added, downstream capacity. Unlike other players in the DRI-IF value chain, we find SMEL augmenting steel capacity. From FY20 to FY24, the company has increased steel capacity from 820ktpa to 2.07mtpa with commensurate upstream expansion in pellets and sponge iron. In FY22 and FY23, the management added aluminium foils and LC ferrochrome capacities – both niche and export-oriented products.

Now, we see SMEL embarking on the next leg of growth with focus on stainless steel, DI pipes, heavy structural products. In order to support upstream requirements, the company is setting up a 'ladle refining furnace' (LRF) and 'continuous casting machine' (CCM) to further enhance the quality of crude steel.

Exhibit 2: Capacity through FY28E

Capacity (ktpa)	FY21	FY22	FY23	FY24E	FY25E	FY26E	FY27E	FY28E
Pellet	2,400	3,600	4,800	6,000	6,000	6,000	6,000	6,000
Sponge Iron	1,390	2,100	2,694	3,048	3,576	4,104	4,104	4,104
Billet	892	940	1,692	2,007	2,007	2,007	2,007	2,007
TMT	820	900	1,670	1,954	1,954	1,954	1,954	1,954
Wires		-		120	120	120	120	120
Ferroalloys	206	206	206	206	230	230	230	230
Low carbon ferrochrome	-	-	14	14	14	14	14	14
Aluminium foils	-	24	24	24	24	24	24	24
Stainless steel	-		150	150	220	220	220	220
CRM	-			-	250	450	450	450
Pig Iron	-			1,050	1,220	1,220	1,220	1,220
DI pipes						400	400	400
Heavy structural mill						400	400	400
Stainless steel CRM						-	200	200
Stainless steel flats						-	500	500

Source: I-Sec research, Company data

…resulting in increase in value-added products sales volume

As downstream capacity ramps up, we are likely to witness decline in pellet and sponge iron sales volume as these would be utilised in heavy structural mill, DI pipe mills and stainless steel mill. Also, the external sales volume of ferroalloys is also likely to decline. In our view, the captive use of ferrochrome (in liquid form) at the Sambalpur plant is likely to result in lower raw material costs due to lower yield loss and less power requirement.

Exhibit 3: Sales volume through to FY28E

Sales volume (kte)	FY21	FY22	FY23	FY24E	FY25E	FY26E	FY27E	FY28E
Pellet	1,770	1,477	1,214	1,378	1,855	1,538	968	968
Sponge Iron	326	579	603	800	1,238	1,502	1,373	1,382
Billet	241	180	207	191	78	78	78	78
TMT	614	801	1,034	1,469	1,671	1,671	1,671	1,671
Wires			90	97	103	103	103	103
Ferroalloys	140	161	180	174	190	195	103	97
Low carbon ferrochrome	-	-	-	10	13	13	13	13
Aluminium foils	-	1	11	19	22	22	22	22
Stainless steel	-	-	4	90	223	198	198	198
CRM	-	-	-	-	75	385	385	401
Pig Iron	-	-	-	-	614	666	536	536
DI Pipe	-	-	-	-	-	50	320	320
Heavy structural mill	-	-	-	-	-	180	356	320
Narrow strip mill	-	-	-	-	-	-	-	-
Stainless steel CRM	-	-	-	-	-	-	80	160
Stainless steel Flats	-	-	-	-	-	-	320	265

Source: I-Sec research, Company data

New capex likely to result in additional EBITDA of INR 10bn

Low capex intensity results in low payback period

The next leg of expansion through to FY26 focuses on all the points in the value chain. While finished steel capacity is expected to be expanded by 1.59mtpa to 3.67mtpa, the low carbon ferrochrome capacity is likely to be expanded by 0.02mtpa to 0.034mtpa.

On upstream side, management has planned a 3mtpa iron ore beneficiation plant and aluminium mill with caster. Capacity for intermediates – DRI and billets – is also likely to be augmented to dovetail with the increased finished steel capacity.

In order to meet the enhanced power requirement, the company is setting up coal-based captive thermal power plant of 220MW and 110MW solar power plant.

Exhibit 4: Fine print of newly announced capex

Projects	Category	Process	Units	Capacity Increase	Cost (INR mn)	Capex intensity (USD/te)	EBITDA/te (INR)	EBITDA (INR mn)
Captive Power Plant	Power	Ancillary	MW	220	7,800		-	-
Solar Power Plant	Power	Ancillary	MW	110	4,500		-	-
Power Total				**330**	**12,300**			-
Aluminium Mill with Caster	Aluminium	Backward integration	mtpa	0.010	750	915	10,000	80
Battery Foil plant	Aluminium	Downstream Products	mtpa	0.005	250	610	-	-
Aluminium Total				**0.015**	**1,000**			80
Beneficiation Plant	Pellet	Backward Integration	mtpa	3.00	3000	12	500	1,200
Pellet Total				**3.00**	**3000**			1,200
Ferro Alloys	Ferro	Downstream Products	mtpa	0.02	600	366	55,000	660
Ferro Total				**0.02**	**600**			660
Billet (for Hot Flat products)	Intermediary	Backward Integration	mtpa	0.50	2000	49		
Billet (for Parallel Flange Beam)	Intermediary	Backward Integration	mtpa	0.40	1100	34		
Billet SS	Intermediary	Backward Integration	mtpa	0.13	1300	122		
DRI	Intermediary	Backward Integration	mtpa	1.06	4000	46		
Intermediary Total				**2.09**	**8,400**			-
CRM (Stainless)	Finished Product	Downstream products	mtpa	0.20	1500	91	11,000	1,870
Ductile Iron Pipe	Finished Product	Downstream products	mtpa	0.40	4000	122	-	-
Hot Flat Product	Finished Product	Downstream products	mtpa	0.50	5500	134	7,000	2,975
Parallel Flange Beam	Finished Product	Downstream products	mtpa	0.40	2400	73	7,000	2,380
Steel Wire Drawing	Finished Product	Downstream products	mtpa	0.09	450	61	7,000	536
Intermediary Total				**1.59**	**13,850**			8,421
Grand Total				**6.72**	**39,150**			**10,361**

Source: Company data, I-Sec research

At capacity utilisation of 85% for downstream and intermediate capacities and power load factor of 20% for the solar plant, we expect an additional EBITDA of INR 10.4bn, implying less than 4 years of payback period.

The capex intensity for all the facilities is less than the industry standards, potentially yielding better returns.

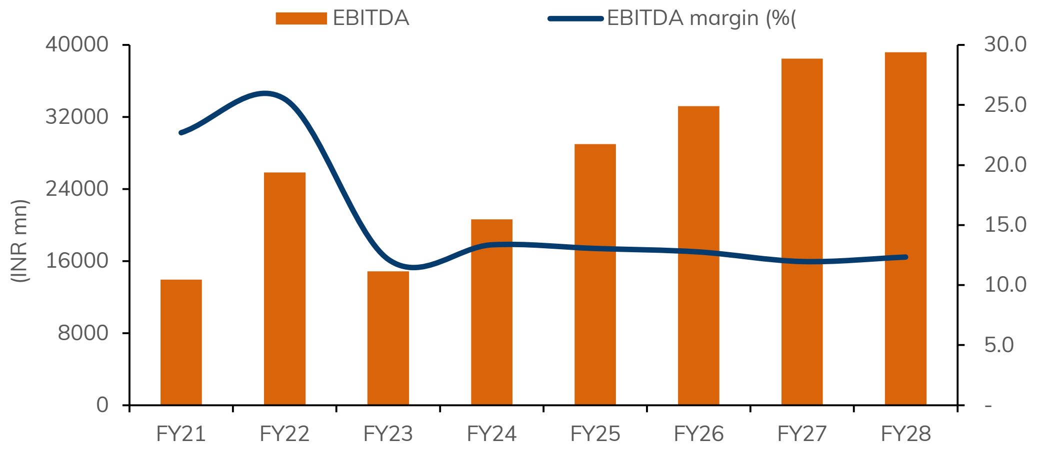
Going by the company's track record, we expect capex of INR 30bn-40bn with a gap of 2-3 years as management explores new opportunities to fill in, by focusing on niche areas and small capacities.

EBITDA likely to touch INR 40bn by FY28E

EBITDA growth likely at 21% CAGR through to FY28E

We expect the new capex to start contributing to earnings progressively from FY25E. Our scenario analysis based on current price levels suggests EBITDA CAGR of 21% to reach almost INR40bn by FY28E with EBITDA margin between 12-13% all through FY24E-FY28E.

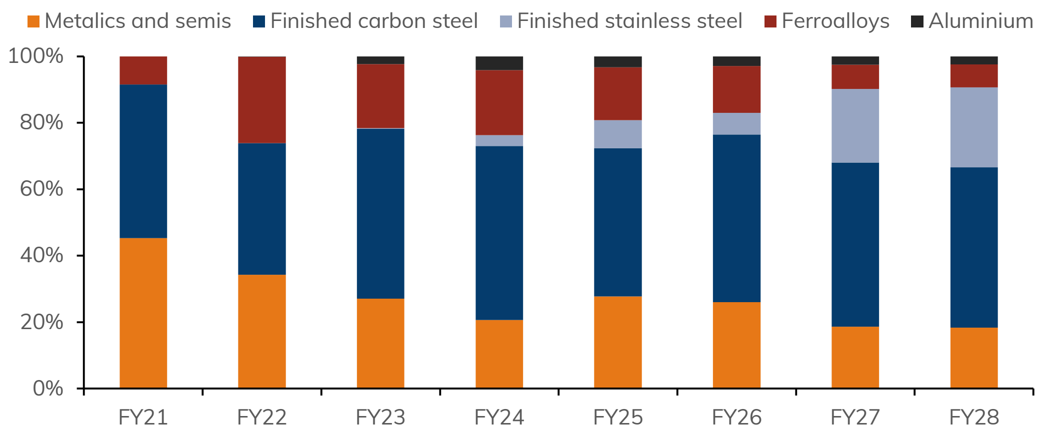
Exhibit 5: EBITDA and margins through to FY28E



Source: I-Sec research, Company data

We expect downstream products, i.e. finished carbon and stainless steel, to contribute 72% of EBITDA in FY28E compared to 51% in FY23. We expect the EBITDA contribution from semis to fall from 27% in FY23 to 17% in FY28E as more semis is utilised towards making steel. From just 3 revenue streams in FY21, we see 5 revenue streams in FY28E, thus diversifying the earnings effectively.

Exhibit 6: Revenue contribution from different products



Source: I-Sec research, Company data

Valuations: Putting money on growth

We value SMEL at INR 690/share

Going by the capex track record and management aspirations, we believe the capex journey of SMEL does not stop at INR 39bn. The company's capital allocation policy is clear about 70% of cash generated being directed towards growth. In our view, growth projects in future as well are likely to be in niche, value-added areas with low capex intensity. Furthermore, we trim our existing FY24E/FY25E EBITDA by 6% and 8% respectively, taking cognisance of the current level of prices.

We raise SMEL's valuation multiple to 6x EBITDA (earlier: 4.5x) taking cognisance of the currently low level of prices (hence there is a better probability of our estimates being achieved) and growth opportunities in future. This results in a revised target price of INR 690 (earlier: INR 570), implying a further upside of 48% from the current levels, despite the stock yielding a return of 72% in past five months.

Exhibit 7: We value SMEL at INR 690

	FY25E
EBITDA (INR mn)	30,382
Multiple (x)	6.0
EV (INR mn)	1,82,293
Net debt (INR mn)	5,991
Market cap (INR mn)	1,76,302
Number of shares (mn)	255
Fair value (INR)	**690**

Source: I-Sec research

Alternate methodology

We value SMEL's current business and cashflow from the new capex separately. As we have lowered our estimates, we raise SMEL's EV/EBITDA multiple to 5x (earlier 4.5x). We value the cashflow from new capex separately and discount it to FY25E levels at 20%. Our target price works out to INR 690 by this approach as well.

Exhibit 8: Our SoTP methodology also values SMEL at INR 690

Existing business	
EBITDA (INR mn)	30,382
Multiple	5.0
EV	1,51,911
New capex	
EBITDA (INR mn)- FY28	10,361
Discounted @20% to FY25	5,996
Multiple	5.0
EV	29,978
Market cap	1,81,889
Net debt- FY24	5,991
Market cap	1,75,899
Number of shares	255
Fair Value	**690**

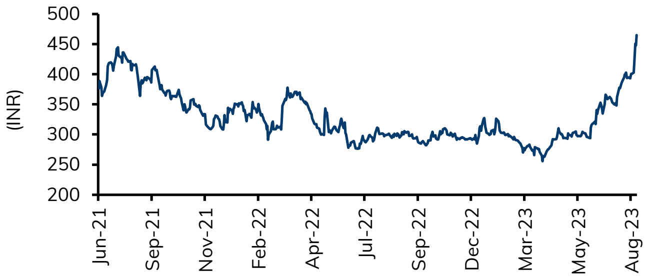
Source: I-Sec research

Exhibit 9: Shareholding pattern

%	Dec'22	Mar'23	Jun'23
Promoters	88.4	88.4	88.4
Institutional investors	3.9	3.8	3.8
MFs and others	2.8	2.7	2.7
FIs/Banks, Insurance	0.4	0.4	0.4
FIIs	0.7	0.7	0.7
Others	7.7	7.8	7.8

Source: Bloomberg, I-Sec research

Exhibit 10: Price chart



Source: Bloomberg, I-Sec research

Financial summary

Exhibit 11: Profit & Loss

(INR mn, year ending March)

	FY22A	FY23A	FY24E	FY25E
Net Sales	**1,03,940**	**1,26,102**	**1,74,496**	**2,50,396**
Operating Expenses	77,942	1,11,243	1,50,302	2,20,014
EBITDA	**25,998**	**14,859**	**24,194**	**30,382**
EBITDA Margin (%)	25.0	11.8	13.9	12.1
Depreciation & Amortization	2,724	4,631	5,404	5,114
EBIT	23,274	10,228	18,790	25,268
Interest expenditure	232	931	884	1,063
Other Non-operating Income	600	1,120	1,288	1,481
Recurring PBT	**23,642**	**10,417**	**19,194**	**25,687**
Profit / (Loss) from Associates	-	-	-	-
Less: Taxes	6,402	1,934	5,758	7,706
PAT	17,240	8,483	13,436	17,981
Less: Minority Interest	-	-	-	-
Extraordinaries (Net)	-	-	-	-
Net Income (Reported)	**17,240**	**8,483**	**13,436**	**17,981**
Net Income (Adjusted)	**17,240**	**8,483**	**13,436**	**17,981**

Source Company data, I-Sec research

Exhibit 12: Balance sheet

(INR mn, year ending ??March)

	FY22A	FY23A	FY24E	FY25E
Total Current Assets	39,880	37,696	40,579	51,652
of which cash & cash eqv.	919	748	783	1,566
Total Current Liabilities & Provisions	17,198	21,346	26,426	37,351
Net Current Assets	**22,683**	**16,350**	**14,153**	**14,300**
Investments	10,359	14,631	11,631	10,631
Net Fixed Assets	24,546	29,461	51,746	67,632
ROU Assets	-	-	-	-
Capital Work-in-Progress	7,683	27,689	21,000	23,000
Total Intangible Assets	-	-	-	-
Other assets	1,782	2,410	2,410	2,410
Deferred Tax assets	-	-	-	-
Total Assets	**67,052**	**90,541**	**1,00,940**	**1,17,973**
Liabilities				
Borrowings	**5,619**	**11,793**	**10,061**	**10,873**
Deferred Tax Liability	**1,073**	**712**	**712**	**712**
provisions	140	202	202	202
other Liabilities	1,834	2,353	2,353	2,353
Equity Share Capital	2,551	2,551	2,551	2,551
Reserves & Surplus	55,796	69,074	81,166	97,349
Total Net Worth	**58,347**	**71,625**	**83,717**	**99,900**
Minority Interest	40	3,856	3,895	3,934
Total Liabilities	**67,052**	**90,541**	**1,00,940**	**1,17,973**

Source Company data, I-Sec research

Exhibit 13: Quarterly trend

(INR mn, year ending March)

	Sep-22	Dec-22	Mar-23	Jun-23
Net Sales	30,852	29,217	33,801	33,068
% growth (YoY)	23.7	13.3	18.3	2.6
EBITDA	2,436	2,223	4,135	4,049
Margin %	7.9	7.6	12.2	12.2
Other Income	217	376	309	330
Extraordinaries	-	-	-	-
Adjusted Net Profit	1,143	673	2,612	2,374

Source Company data, I-Sec research

Exhibit 14: Cashflow statement

(INR mn, year ending March)

	FY22A	FY23A	FY24E	FY25E
Operating Cashflow	**16,896**	**15,069**	**24,957**	**25,793**
Working Capital Changes	(3,244)	2,770	5,233	1,635
Capital Commitments	(10,714)	(15,789)	(21,000)	(23,000)
Free Cashflow	**6,182**	**(721)**	**3,957**	**2,793**
Other investing cashflow	**(8,551)**	**(3,760)**	**-**	**-**
Cashflow from Investing Activities	(19,265)	(19,550)	(21,000)	(23,000)
Issue of Share Capital	(4)	-	-	-
Interest Cost	(232)	(717)	(884)	(1,063)
Inc (Dec) in Borrowings	(2,533)	7,174	(1,732)	812
Dividend paid	(1,837)	(1,148)	(1,344)	(1,798)
Others	6,256	(1,000)	39	39
Cash flow from Financing Activities	1,651	4,310	(3,921)	(2,010)
Chg. in Cash & Bank balance	**(719)**	**(171)**	**36**	**783**
Closing cash & balance	919	748	783	1,566

Source Company data, I-Sec research

Exhibit 15: Key ratios

(Year ending March)

	FY22A	FY23A	FY24E	FY25E
Per Share Data (INR)				
Reported EPS	67.6	33.3	52.7	70.5
Adjusted EPS (Diluted)	67.6	33.3	52.7	70.5
Cash EPS	78.3	51.4	73.9	90.5
Dividend per share (DPS)	7.2	4.5	5.3	7.0
Book Value per share (BV)	228.7	280.8	328.2	391.6
Dividend Payout (%)	10.7	13.5	10.0	10.0
Growth (%)				
Net Sales	65.1	21.3	38.4	43.5
EBITDA	86.5	(42.8)	62.8	25.6
EPS (INR)	87.2	(50.8)	58.4	33.8
Valuation Ratios (x)				
P/E	6.9	14.0	8.8	6.6
P/CEPS	5.9	9.0	6.3	5.1
P/BV	2.0	1.7	1.4	1.2
EV / EBITDA	4.3	7.7	4.8	3.9
Dividend Yield (%)	1.5	1.0	1.1	1.5
Operating Ratios				
Gross Profit Margins (%)	35.1	24.2	27.3	22.3
EBITDA Margins (%)	25.0	11.8	13.9	12.1
Effective Tax Rate (%)	27.1	18.6	30.0	30.0
Net Profit Margins (%)	16.6	6.7	7.7	7.2
Net Debt / Equity (x)	(0.1)	0.0	0.0	0.0
Net Debt / EBITDA (x)	(0.2)	(0.2)	(0.1)	0.0
Fixed Asset Turnover (x)	3.0	3.0	3.1	3.3
Inventory Turnover Days	107	82	66	70
Receivables Days	27	30	23	24
Payables Days	64	58	56	63
Profitability Ratios				
RoCE (%)	34.6	12.8	15.9	17.7
RoE (%)	42.0	14.9	18.2	20.2
RoIC (%)	39.3	15.2	18.8	20.4

Source Company data, I-Sec research

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