SHYAM METALICS & ENERGY LTD.

AUM CAPITAL
YOUR TRUST IS OUR WEALTH

September 22, 2021

SHYAM METALICS & ENERGY LTD.	
Industry	Steel & Iron Products
No. of Shares (Crore)	25.51
Face value (Rs.)	10
Mkt. Cap (Rs. Crore)	9573.90
Price (21/09/2021)	375.30
Book Value (Rs)	195.73
P/BV	1.92
BSE Code	543299
NSE Code	SHYAMMETL
Bloomberg	SHYAMMET:IN
Reuters	SHYE.NS
Avg. Weekly Volume (NSE)	521,954
52 W H/L (Rs)	461.15/306.00

Shareholding Pattern	%
Indian Promoters	88.35
Institutions	4.63
Non- Instutions	7.02
Total	**100**
(As on June 30, 2021)	

Recommendation
BUY

Company Background

Shyam Metalics & Energy (SMEL) is a leading integrated metal producing company based in India with a focus on **long steel products and ferro alloys**. They are amongst the **largest producers of ferro alloys**, one of the leading players in terms of pellet capacity and the **fourth largest player in the sponge iron** industry, in terms of capacity in India. They have a diversified product mix which enables them to sell both **intermediates and final products across the steel value chain**.

Investment Rationale

- SMEL operates three manufacturing plants: one in Odisha and two in West Bengal. The aggregate installed metal capacity of the manufacturing plants **is 5.9 Million Tonne Per Annum (MTPA)**, comprising intermediate and final products. The plants house **captive power plants** with an aggregate **installed capacity of 227 MW.**
- Its manufacturing plants are **strategically located** in close proximity to the mineral belt in eastern India, which is rich in iron ore, iron ore fines, manganese ore, chrome ore and coal mines. Not only this, the plants are also in close proximity to ports. Thus, the company is able to source raw materials and offer products at **cost effective and competitive prices**.
- The company is in the process of expanding capacities of existing manufacturing plants and captive power plants. The expansion of capacities will result in further integration of its plants, **augmentation of revenue and better cost control**, not to mention a presence across the **steel value chain**. Furthermore, ongoing capacity expansion will enable SMEL to **widen its presence in premium products such as wire rods and Ductile Iron (DI) pipes**.
- SMEL is progressively shifting towards **value-added products**. Capacity addition in value-added products such as **Thermo Mechanical Treatment (TMT)** bars, structural products, ferro alloys and diversification into new business of conversion of aluminum foil will further bolster & underpin healthy double digit revenue growth.
- SMEL houses captive power plant of 227 MW capacity as of FY2021 which typically **meets 90% of its power requirement and is self-sufficient**. While average grid power is estimated to cost Rs.5–7/- per unit at an all India basis, however, SMEL's **power and fuel cost is significantly lower at Rs.2.06 per unit as of Q1FY22**. Further the captive power plant uses waste heat and Dolochar (non-fossil fuel) as the main feed. Since power is a major raw material this significantly adds to **economic moat and scalable advantage**.
- In the quarter gone by i.e. Q1FY22 the company reported a consolidated net profit of Rs.458 crores, up around 470% from Rs.80 crores in the same quarter last year. The company's total **revenue from operations jumped ~2.7x to Rs.2465 crores** as compared to Rs.911.8 crore year-on-year (YoY). **EPS** for the quarter bolstered over **~5 times to Rs.17.95** as against less than Rs.3.5.

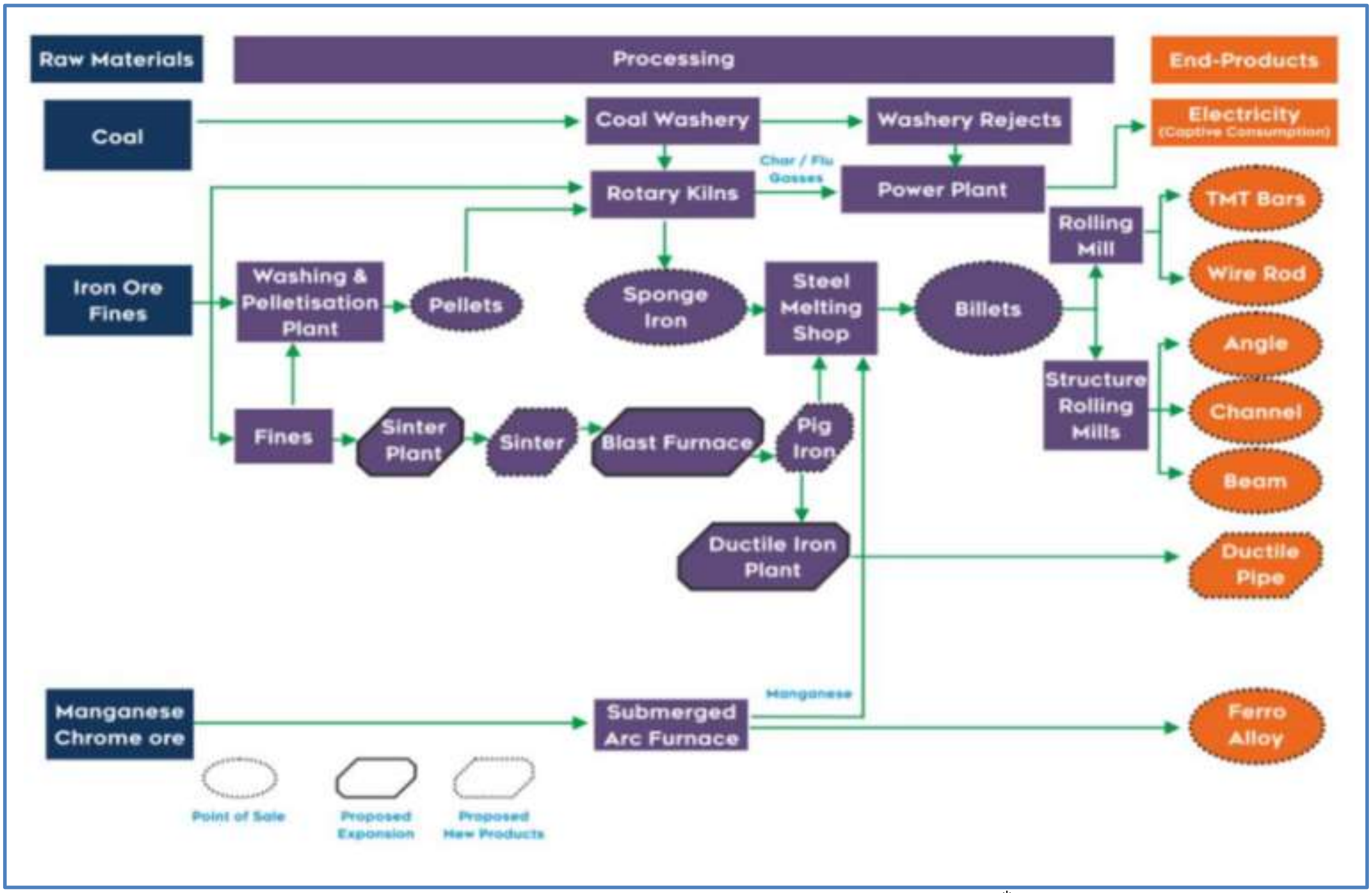
Recommendation

SMEL is expected to reap benefits out of capacity augmentation/enhancements and low leverage. Besides, Value-added products and cost efficiencies are likely to strengthen/aid margin further. At the CMP of Rs.375.30 the scrip is trading at a PE of 5.77 times its FY22e earnings. Hence, we recommend a buy on the stock with a target price of Rs.450/- which implies a prospective and potential upside of ~19.90% with an investment horizon of 9-12 months.

Particulars (In Rs.Crs)	Q1FY22	Q1FY21	Var%	FY21	FY20	FY19
Net Sales	2,465.03	911.84	170.34	6,297.07	4,376.35	4,606.40
Operating Profit	695.41	155.55	347.07	1,417.51	677.92	1,022.91
Consolidated net Profit	457.98	80.29	470.41	843.36	340.24	604.13
PBIDTM%	28.21	17.06	65.37	22.51	15.49	22.21
PATM%	18.58	8.81	111.00	13.39	7.77	13.82
Equity	255.08	233.61	9.19	233.61	233.61	233.61
EPS (Rs.)	17.95	3.44	422.40	36.10	14.56	25.86

*Source: Company, Ace Equity, AUM Research

Integrated Operations across the Steel Value Chain



*Source: Company, Ace Equity, AUM Research

Key Operating Indicators:

- SMEL's operations are well integrated across the **value chain**. Like other companies in the secondary steel sector, the company sells anything from pellets to steel, depending on prevailing market conditions in order to **optimize margins**.
- SMEL has achieved **cost efficiencies** by utilizing waste materials/by-products as raw material inputs for other products and processes. Besides, the **integrated nature of operations** eliminates re-heating at multiple points, resulting in savings in power cost to the extent of Rs.500/tonne.
- SMEL's manufacturing facilties are located in **close proximity** to its raw material sources—within 250km of the mineral belt in eastern India. The company has **long term linkages for coal** as well as chrome ore with Mahanadi Coal Fields and Odisha Mining Corporation, respectively.
- Strategic locations – close to raw material sources/ports and captive railway sidings at both Jamuria and Sambalpur plants – lower logistics cost for the company. Plant locations help optimize the sales and marketing cost as **both plants cater to different markets**.
- SMEL's plants are well connected by national highways. The plants in Odisha and West Bengal are in proximity to NH 16 and NH 19, respectively. SMEL is one of the very few players in the secondary steel space to have **captive railway sidings**. The captive railway sidings at both Jamuria and Sambalpur plants are sufficient to cater to the current and future requirements. Transportation by rail has resulted in a **reduction of freight cost** and turnaround time for both raw materials and finished products. For distances above 500km, railways are 20–30% cheaper than road.

- Both the plants are also located in the vicinity of ports. Dhamra and Paradeep ports are located within a radius of 300km from the Sambalpur plant while the Haldia port is located within a radius of 300km from the Jamuria plant.

Wherewithal & bandwidth of sales across value chain underpins optimal margins

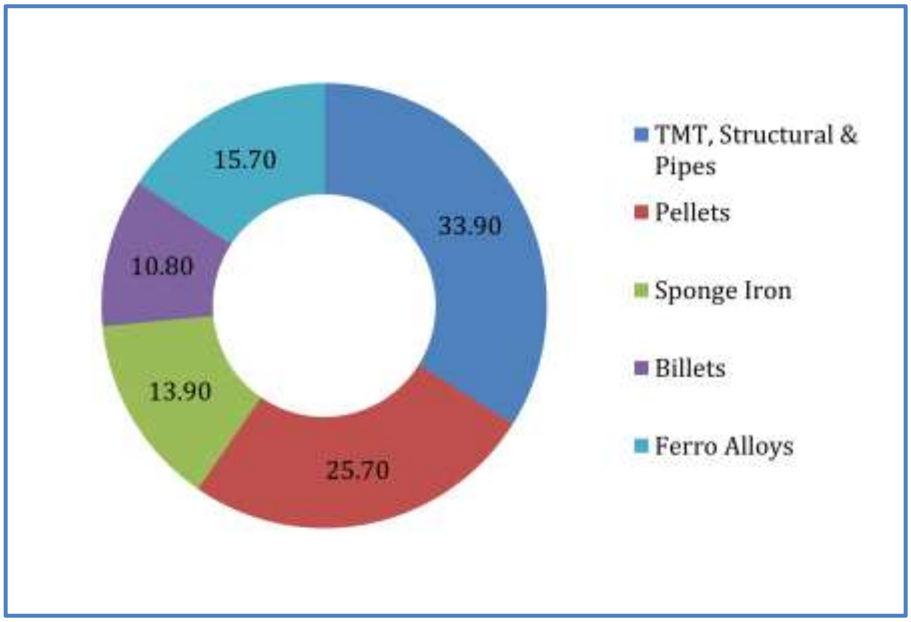
- Flexibility to sell intermediate products depending on demand environment
- Diversified revenue mix largely de-risks business model

SMEL houses captive power plant of 227 MW capacity as of FY2021 which typically **meets 90% of its power requirement and is self-sufficient**. While average grid power is estimated to cost Rs. 5–7/- per unit at an all India basis, SMEL's **power and fuel cost is significantly lower at Rs.2.06 per unit as of Q1FY22**. Further the captive power plant uses waste heat and Dolochar (non-fossil fuel) as the main feed. Since power is a major raw material this significantly adds to **economic moat and scalable advantage**. Since, **one tonne of ferro alloys consumes about ~4000 unit of power it results in tremendous cost saving for SMEL**

Product Portfolio:

- The product portfolio comprises: a.) **long steel products**, which ranges from intermediate products such as iron pellets, sponge iron and billets, and **final products such as TMT and structural products**; and b.) ferroalloys, forward and backward integration of manufacturing plants allows for multiple points of sale across the steel value chain. This has provided the company with flexibility to sell intermediate products as well as use them for captive consumption, depending on demand. This in turn has resulted in a **diversified product mix**, which has **reduced dependency on a particular product and de-risked revenue streams**.
- SMEL has rejigged its sales mix depending on market conditions and its own capacity ramp-up plans. The revenue share of ferroalloys has gone down from 30% in FY16 to 12% in FY21 as: a.) The prices of steel products have gone up while the ones for ferrochrome have remained range-bound; and b.) capacity/sales of steel products have increased. Similarly, the share of billets in revenue mix has gone down in FY21, coinciding with the ramp-up in capacity of rolled products.

Revenue pie across products (%)



*Source: Company, Ace Equity, AUM Research

Deleveraging provides an impetus to flexibility of growth:

- SMEL debt as on ~Q1FY22 stood at Rs.314 crores. In terms of debt segregation long term debt stood at Rs.120 crores followed by working capital debt at Rs.194 crores. Besides company has **parked about Rs.1000 crores in treasury with investments in mutual funds, other equity instruments & bank Fixed Deposits (FDs)** etc.

- Going forward, the company will continue to benefit from **established market position** in **key long steel products**, **diversified revenue streams**, **healthy demand** for its steel products and its integrated nature of operations, ensuring healthy cash generation.

- SMEL's **ROCE** has seen a **tremendous rise from high single digit – 9.7% to 25.3% in FY21** while its **ROE lopsidedly doubled to 23.2% from 12%**

Brand Ambassador at the anvil – Salman Khan

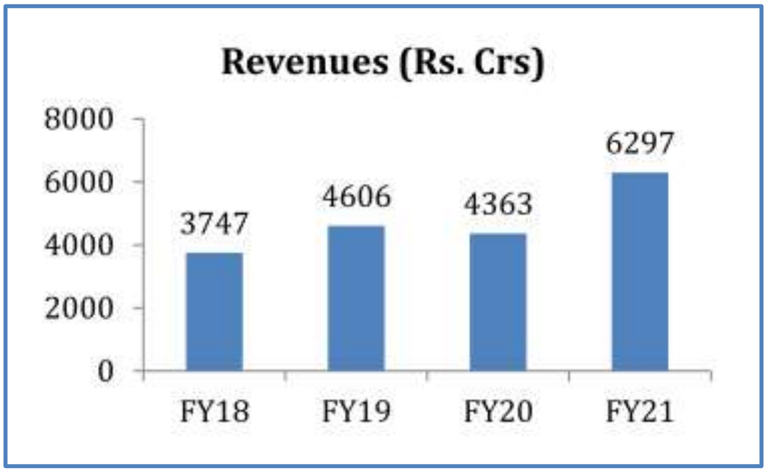
- As a part of company's thrust entailing and envisaging **four-fold expansion** plan in metal capacity comprising intermediate and final products, SMEL recently has brought in ***Salman Khan*** as **brand ambassador** for endorsing **S-E-L TMT rebars**. Its **long products (comprising TMT Rebars, Wire Rods and Structural products)** are sold under the **brand name S-E-L that deliver attributes of Strength, Elasticity and Longevity**. These attributes are synonymous with celebrity Salman Khan and makes him a perfect fit for the brand.

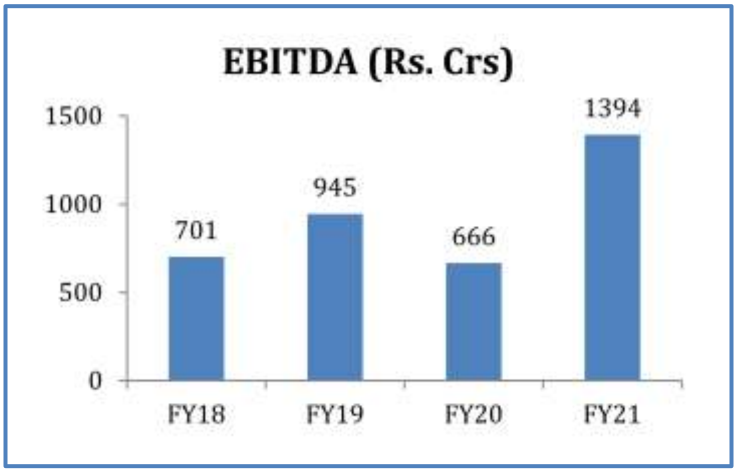
- Bellwether association with Salman Khan will **strengthen SMEL's brand recall** and **position** their **unique offering**, both to its customers and end-users. **Management resonates and believes** that key to their **brand cementation & acceleration** is to stay relevant to the emergent needs of the consumer at every point of the construction journey.

Expansion Plans

SMEL is **ramping up** capacities across its manufacturing plants (located in Odisha's Sambalpur and West Bengal's Jamuria and Mangalpur) and captive power plants. From sale of 1.07 lakh tons of Long Steel products in FY17, it has grown to sell 6.37 lakh tons in FY 2020-21. Post the current **brownfield expansion** under implementation, it proposes to ramp up this capacity to **20 lakh tons of branded value-added products**. Additionally, the company is in the process of commissioning an aluminium foil rolling mill at Pakuria in West Bengal. Company's endeavor in continuing to focus on making high quality products to reach the last mile would help in posting strong numbers going ahead.

Strong Operating Scorecard





*Source: Company, Ace Equity, AUM Research

Sectoral Outlook:

Indian steel demand–supply dynamics:

- India is among the fastest growing major economies of the world. It is also the sixth largest economy on a nominal basis. **Steel demand is closely & profoundly correlated to GDP growth**, with steel demand to GDP growth multiplier varying across phases.
- After lagging India's GDP growth since 2012–13, steel demand growth outpaced macroeconomic growth in FY21. With GDP expanding gradually, the rise in incomes led to r**obust growth in Auto, Consumer Durables, Railways, Affordable Housing and Rural Housing** coupled with a low base effect.
- Over the last decade, India's steel demand growth has outpaced the world's average, except for a brief period from 2010 to 2013 that was impacted by the slowdown in key end-use segments in the domestic market. However, **post-2013, domestic demand has invariably exceeded global demand, which was marred by a slowdown in China (which accounts for half of global steel demand)**. In contrast, India's steel demand growth has remained modest driven by soft growth in the auto and building & construction segments.
- According to the World Steel Association (WSA), global steel demand is expected to recover to 1.874bln tonne and grow 5.8% in CY21. **India is expected to outpace global steel demand with growth anticipated at 19.8% in CY21.**
- India's per capita steel consumption is very low at a meagre 74kg against global average of 229 kg. Developed economies such as USA, the EU, Japan and China have much higher spending on infrastructure and relatively more steel-intensive housing/ commercial establishments, leading to higher per capita consumption of steel. **An underpenetrated Indian steel market represents high future growth potential.**
- Given the impact of pandemic and subsequent lockdowns, **steel demand is expected to rise 12% in FY22, followed by 6% each for FY22–23.** In conjunction with healthy demand growth, **capacity utilization levels are also expected to move on an upward trajectory.**
- India added nearly 22 MTPA of crude steel capacity in the past five years (FY16–21) amid tepid demand growth, which led to a declining trend in utilization level. Another **19 MTPA is expected to be added over the next three years (FY22–24).** However, **prudent additions amid healthy demand growth of 6% will lead to utilization ramping up to 78.5% by FY24 from 70% in FY21.**

Steel Demand– Key Growth Drivers:

Building & Constructions: **Steel demand from building and construction (B&C) accounts for 32–34% of aggregate finished steel demand.** Contemporarily, B&C demand is going **through the roof, in medium- long term led by solid structural/cyclical upturn in spaces e.g. rural housing, affordable housing, and commercialization of Tier III/IV cities**. On the other hand, a **multiyear realty cycle** has kick started at the anvil, which would infer **exponential, super normal growth** for the industry at large and the said cycle would **flourish and last at least for 5 – 6 years** which in itself will provide an **enormous boost to steel demand** in near as well as distant future.

Infrastructure: **Infrastructure segment is currently the second largest segment in terms of steel consumption comprising 25–30% share in overall steel demand end use mix. Demand from the sector is expected to be healthy with increasing activities and swift pace of execution in steel-intensive segments such as railways and particularly metros**. Demand from the infrastructure sector has also received support in the budget, which laid emphasis on infrastructure development.

Automotive: **Steel demand from the automotive sector accounts for 8% to 10% of aggregate finished steel demand**. The automobile industry has begun to recover post contraction caused by the covid-19 outbreak. **The sector is expected to recover in FY22 across most segments, after sharp declines witnessed in FY21**.

Demand Outlook:

Long Steel: Finished long steel products are normally produced by hot rolling/forging of bloom/ billets/ pencil ingots into useable shape/ sizes. These are normally supplied in straight length/cut length except wire rods, which are supplied in irregularly wound coils. The different types of long products include bar and rods, CTD/TMT, wire rod, angles, shapes and sections. **Long steel demand is driven by housing and infrastructure.** It is estimated that **long steel demand** is likely to grow **5–6% through FY25 driven by strong demand in infrastructure and housing**.

Unlike flat steel, long steel market is fairly fragmented with top five large players constituting about 35% of the market and the rest being distributed among more than 850 Interstitial-Free (IF) and Electric Arc Furnace (EAF) units. Further, India also houses 1020 rolling units as of FY20 who are **primarily dependent on billet providers**. Of these **only 116 re-rolling units with nearly 18 MT capacity (approximately 23% of overall re-rolling capacity) are situated in East** with North and West housing over 690 re-rolling units (around 41 MT of re-rolling capacity). **This is primarily on back of more integrated long steel players being present in East, wherein SMEL is a key beneficiary.**

Sponge Iron: Sponge iron, also termed Direct-Reduced Iron (DRI), is produced by reducing (removing oxygen) from iron ore to increase free iron content. This also makes the ore porous. Sponge iron is popularly used as a feed in electric/induction furnaces and as a substitute for steel scrap, because high-quality scrap is costly and scarcely available. It is also used as a coolant by integrated steel plants, again as a substitute to melting scrap (Sponge iron is added as a solid only to hot metal. It then melts inside and stabilizes the temperature. Sponge iron melts faster than iron ore or scrap).

India is the second largest sponge iron producer; however, the domestic industry is fairly fragmented with around 285 units with an operational capacity of approximately 47.85 MTPA operating as of FY20. These units had a gross production of around 37.1 MT as of FY20 thereby yielding a utilization level of around 77.5%. The total capacity as well as number of units have decreased between FY18 and FY20. The capacity decreased from 49.6 MT (FY18) to 47.9 (FY20) and the number of working units have reduced by 27 over the same time period, which exhibits large players gaining more traction.

Pellets: Pellets are normally produced in the form of globules from very fine iron and mostly used for production of sponge iron in gas based plants, though they are also used in blast furnaces in some countries in place of sized iron ore.

Pellet production has risen at a robust pace led by **healthy domestic demand** along with exceptional stride in export volumes. Share of exports in overall production has increased from 1.5% in FY16 to around 18% in FY20. Domestic sales of pellets is estimated to have grown at 9% CAGR, against 13% CAGR growth in exports from FY17 to FY20. India houses **80–85 MTPA of pellet capacity** which operates at around **80% of utilization**. No significant capacity additions has been done from FY15 to FY20. However **~25 MTPA of incremental pellet capacity is proposed to be added** by integrated steel producers over the medium term.

Crude Steel – Capacity, Production & Capacity Utilization

Year	Capacity (MT)	Production (MT)	Capacity Utilization (%)
2016	128.28	95.48	74
2017	137.98	101.45	74
2018	142.24	109.25	77
2019	142.30	111.34	78
2020	142.72	99.57	70

*Source: Company, Ace Equity, AUM Research

Financials

Quarterly Results (Value in Rs. Crs)						
Particulars	**Q1FY22**	**Q1FY21**	**Var%**	**Q4FY21**	**Q4FY20**	**Var%**
Net Sales & Other Operating Income	2,465.03	911.84	170.34	2,350.51	1,083.68	116.90
Total Expenditure	1,777.40	759.96	133.88	1,723.75	893.95	92.82
PBIDT (Excl OI)	687.63	151.88	352.75	626.76	189.73	230.34
Other Income	7.78	3.67	111.99	9.26	2.25	311.56
Operating Profit	695.41	155.55	347.07	636.02	191.98	231.29
Interest	6.71	19.57	-65.71	6.63	25.03	-73.51
PBDT	688.70	135.98	406.47	629.39	166.95	276.99
Depreciation	61.38	68.73	-10.69	80.35	93.11	-13.70
Tax	169.33	-13.04	1,398.54	161.46	-6.60	2,546.36
Consolidated Net Profit	457.98	80.29	470.41	387.50	79.73	386.02
Equity	255.08	233.61	9.19	233.61	233.61	0.00
EPS (Rs.)	17.95	3.44	422.40	16.59	3.41	386.02

Income Statement (Value in Rs. Crs)			
Particulars	**FY21**	**FY20**	**FY19**
Net sales	6,297.07	4,376.35	4,606.40
Total Expenditure	4,952.93	3,714.90	3,661.69
Operating Profit (Excl OI)	1,344.14	661.45	944.71
Other Income	73.37	16.47	78.20
Operating Profit	1,417.51	677.92	1,022.91
Interest	62.46	85.89	64.43
PBDT	1,355.05	592.03	958.47
Depreciation	300.36	296.68	194.58
Provision for Tax	211.40	-44.86	127.11
Consolidated Net Profit	843.36	340.24	604.13
EPS (Rs.)	36.10	14.56	25.86

*Source: Company, Ace Equity, AUM Research

Balance Sheet (Value in Rs. Crs)			
Particulars	**FY21**	**FY20**	**FY19**
EQUITY AND LIABILITIES			
Share Capital	233.61	233.61	233.61
Total Reserves	3,400.44	2,592.84	2,256.05
Shareholder's Funds	**3,634.05**	**2,826.45**	**2,489.66**
Minority Interest	4.35	4.15	4.43
Secured Loans	119.86	350.67	212.77
Unsecured Loans	0.32	0.64	0.51
Deferred Tax Assets / Liabilities	-6.76	-29.02	72.69
Other Long Term Liabilities	222.67	288.50	234.62
Long Term Provisions	10.59	27.18	5.97
Total Non-Current Liabilities	**346.68**	**637.97**	**526.57**
Trade Payables	367.06	582.78	310.61
Other Current Liabilities	359.88	282.64	277.91
Short Term Borrowings	664.78	698.61	442.77
Short Term Provisions	36.34	0.55	0.49
Total Current Liabilities	**1,428.06**	**1,564.58**	**1,031.78**
Total Liabilities	**5,413.14**	**5,033.15**	**4,052.43**
ASSETS			
Gross Block	3,218.05	3,128.64	2,596.58
Less: Accumulated Depreciation	1,415.84	1,116.01	822.49
Net Block	**1,802.21**	**2,012.47**	**1,774.09**
Capital Work in Progress	506.40	235.45	357.70
Non Current Investments	66.58	72.43	68.42
Long Term Loans & Advances	254.74	151.30	58.98
Other Non Current Assets	37.49	29.78	6.49
Total Non-Current Assets	**2,667.42**	**2,501.43**	**2,265.69**
Currents Investments	215.24	71.59	205.43
Inventories	1,030.23	1,486.71	732.13
Sundry Debtors	533.54	159.02	212.91
Cash and Bank	323.78	121.24	97.84
Other Current Assets	70.05	56.24	7.90
Short Term Loans and Advances	572.88	636.92	530.53
Total Current Assets	**2,745.72**	**2,531.72**	**1,786.75**
Net Current Assets (Including Current Investments)	1,317.66	967.14	754.97
Total Current Assets Excluding Current Investments	2,530.48	2460.13	1,581.31
Total Assets	**5,413.14**	**5,033.15**	**4,052.43**

*Source: Company, Ace Equity, AUM Research

Aum Capital RESEARCH DESK

Rajesh Agarwal	Head of Research	033-4057 21221	rajesh.agarwal@aumcap.com
Tanya Kothary	Manager – Equity Research	033-4057 21221	tanya.kothary@aumcap.com

Disclosure & Disclaimer

This document is solely for the personal information of the recipient and must not be singularly used as the basis of any investment decision. Nothing in this document should be construed as investment or financial advice. Each recipient of this document should make such investigations as they deem necessary to arrive at an independent evaluation of an investment in the securities of the companies referred to in this document (including the merits and risks involved) and should consult their own advisors to determine the merits and risks of such an investment.

Reports based on technical and derivative analysis center on studying charts of a stock's price movement, outstanding positions and trading volume, as opposed to focusing on a company's fundamentals and as such, may not match with a report on a company's fundamentals.

The information in this document has been printed on the basis of publicly available information, internal data and other reliable sources believed to be true but we do not represent that it is accurate or complete and it should not be relied on as such, as this document is for general guidance only. AUM Capital Market Private Limited (hereinafter referred to as "AUM Cap") or any of its affiliates/group companies shall not be in any way responsible for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. AUM Cap has not independently verified all the information contained within this document. Accordingly, we cannot testify nor make any representation or warranty, express or implied, to the accuracy, contents or data contained within this document.

While, AUM Cap endeavors to update on a reasonable basis the information discussed in this material, there may be regulatory compliance or other reasons that prevent us from doing so.

This document is being supplied to you solely for your information and its contents, information or data may not be reproduced, redistributed or passed on, directly or indirectly. Neither, AUM Cap nor its directors, employees or affiliates shall be liable for any loss or damage that may arise from or in connection with the use of this information.

AUM Cap is registered under SEBI (Research Analysts) Regulations, 2014. Further, AUM Cap hereby declares that –

• AUM Cap/its associates/research analysts do not have any financial interest/beneficial interest of more than one percent/material conflict of interest in the subject company.

• AUM Cap/its associates/research analysts have not received any compensation from the subject company(s) during the past twelve months.

• AUM Cap/its research analysts has not served as an officer, director or employee of company covered by analysts and has not been engaged in market making activity of the company covered by analysts.

AUM Capital Market Private Limited
Registered Office: 5, Lower Rawdon Street, Akashdeep building 1st Floor, Kolkata – 700020;
Phone: +91(33) 40572222; Fax: +91(33) 24760191
Website: www.aumcap.com; Email: aumresearch@aumcap.com
SEBI Research Analyst Registration No.: INH300002423