

August 4, 2010

Shri Ashutosh Agarwal
Additional Director – Finance
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Confidential

Dear Sir,

Grading of Initial Public Offering (IPO)

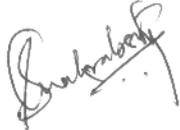
This is in supercession of our earlier letter dated Mar.26, 2010 addressed to the erstwhile Electrosteel Integrated Ltd., on the captioned subject.

2. As per the discussion, the revised rationale for the captioned grading is enclosed as *Annexure I* to this letter.

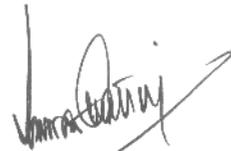
If you have any further clarifications, you are welcome to approach us.

Thanking you.

Yours faithfully,



(Sumit Chakraborty)
Dy. Manager



(Saurav Chatterjee)
Sr. Manager

Encl. – As above

Grading Rationale
Electrosteel Steels Limited (ESL)

Grading

Particulars	No of equity shares (in lakh)	Grading ¹	Remarks
IPO Grading	4240.9 shares* of Rs.10 each	'CARE IPO Grade 3'	Assigned

* including Green Shoe portion of 553.1 lakh equity shares

Grading Rationale

The above grading draws strength from the long experience and proven track record of the promoter company i.e. Electrosteel Castings Ltd., strategic location of the plant with proximity to market & nearness to the source of the raw materials, group's established position in the DI pipe industry, captive mines (coal and iron-ore) of the group, renowned international and domestic strategic partners for the project, achievement of financial closure and stable outlook of the DI pipe & steel industry. Considerable advancement made in project implementation by the company and the presence of experienced professionals in the management & Board of Directors of the company also support the grading. The grading is however, constrained by the risks associated with implementation of the large greenfield project, downturn in the industry during FY09 impacting the implementation of the project, uncertainty with respect to success of the group's new line of business (steel related products) together with its capability to offload the envisaged level of production, cyclicity in the steel industry and stiff competition from existing large integrated steel players.

Company Background

Electrosteel Steels Limited (ESL; erstwhile Electrosteel Integrated Limited), promoted by Electrosteel group of Kolkata, was incorporated in December, 2006 to set up a 2.2 million tones per annum (MTPA) integrated steel plant (including DI pipe capacity & Captive Power Plant (CPP) of 120 MW) near Village – Babugram, Distt. – Bokaro, Jharkhand. The project is being set-up in technical-cum-financial collaboration with Stemcor Mesa DMCC, UAE - a group company of Stemcor, UK (Stemcor). The entire project is expected to commence commercial production, in phases, from October, 2010. The project cost of Rs.7,362.0 crore is being financed at a debt-equity ratio of 2.84:1.




¹ Complete definitions of the ratings assigned are available at www.careratings.com and in other CARE publications

Promoters

Electrosteel Castings Ltd. (ECL), the promoter company, is the leading producer of DI Pipes, DI fittings and CI pipes in the country, besides offering turnkey solutions for water transportation and sewerage management. Shri Umang Kejriwal and Shri Mayank Kejriwal, the current promoters of the group, are reputed industrialists with over three decades of experience in the iron pipe and fittings manufacturing industry. The promoters & their family, currently, hold 42.03% of equity of ESL. Further, several renowned strategic investors like IFCI, IL & FS, Stemcor holds majority of the balance equity stake in the company.

Management

ESL has a broad-based seven member Board of Directors (BOD). The board comprises only one member from the promoters’ family, two whole-time directors, one nominee and three non-executive directors. Shri V. V. Jamnis and Shri N. C. Bahl, the two whole-time directors of the company, are looking after the day-to-day affairs of the company including execution of the proposed project.

Corporate Governance

All the independent Non-Executive Directors have rich industrial experience. The company is, by and large, in compliance with the applicable provisions of the listing agreement and clause 49 pertaining to corporate governance. ESL has formed different committees of Board, like Audit Committee, Remuneration Committee, Share Transfer & Investor Grievance Redressal Committee and IPO Committee.

Project Details

ESL is setting up a 2.2 MTPA integrated steel and ductile iron pipe plant near in Jharkhand, in an approximate area of 1,300 acres of land with another 300 acres required for construction of storage space. The proposed plant will consist of the following facilities:-

Product	Proposed Capacity
TMT bars	7,00,000 TPA
Wire rods	5,00,000 TPA
DI pipe	3,30,000 TPA
Pig iron	4,00,000 TPA
Commercial billets	2,77,650 TPA

Till Feb, 2010, ESL acquired about 2,000 acres of land, keeping in view the low cost of acquisition and the scope for future expansion. The site has been selected due to better proximity to the sources of iron-ore (major raw material), coke and coal, reasonable proximity to end users and availability of necessary infrastructure like railways, roadways, power, labour and water.




The company has fully tied-up its entire debt requirement for the project. As regards the equity infusion, ESL has entered into agreement with several strategic investors (like Stemcor, PGS Investment, IFCI, IL & FS) for part financing the amount required for the project. The balance portion of the equity requirement (Rs.250 crore) will be met out of the proposed IPO. Further, most of the equity partners are renowned player worldwide, having long track record in financing international projects and the required fund has already been infused by them.

ECL has invested Rs.700 crore for the project. Stemcor, the technical-cum-financial collaborator for the project, is an international entity having been in the business of international trade and marketing of steel for over five decades. IL&FS Investment Managers Ltd (IIML), the private equity investment arm of IL&FS Financial Services Limited, is another strategic investor in ESL, has contributed equity for the project. Till February, 2010, the company incurred about Rs.3,722.8 crore on the project.

The company has entered into contracts for procuring the major plant and machinery as well as erecting and commissioning of the same with Stemcor (UK) and SDM (China) for major plant and equipment, Morgan (USA) for finishing end equipment of Wire Rod Mill and China First Manufacturing Company Limited (CFMCL) & 23rd MCC for construction works at the plant site. The basic engineering of the plant has been completed. The detailed engineering work is progressing on schedule and is expected to be over soon. Till February 2010, ESL ordered for majority of its required equipment.

ESL's major raw materials are iron-ore, coking coal, ferro-alloys, limestone and dolomite. ESL's entire requirement of iron ore and 30% of its total coking coal requirement are proposed to be procured from the captive mines allocated to ECL by the Government of Jharkhand. ESL proposes to procure the required limestone from Thailand. It is already in negotiation with several vendors for supply agreement.

ECL already has, in place, a well developed and established marketing network and clientele in India and abroad for DI pipes, which is proposed to be used by ESL for marketing its own production of DI pipes. About 25% of the production is proposed to be exported, for which purpose ESL has entered into an agreement with Stemcor which will facilitate ESL to market its product overseas. The company has already obtained comprehensive insurance cover for its ongoing project.

ESL has already received majority of clearances and approvals required for the purpose of setting up & running the plant.

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Industry outlook

Steel industry

After dismal performance in CY08, global steel industry recovered considerably in CY09. Since latter part of CY09, with revival in steel off take, prices of various steel products are on the rise. Steel companies have been able to negotiate a downward revision in the long term contract prices of key raw materials for FY10. This is expected to provide a relief to domestic steel manufacturers, especially the non-integrated ones, by way of reduction in the input cost and in turn to improve profitability in FY10 compared to the previous year. CARE Research has estimated that during FY10 & FY11, demand for steel would grow at a CARG of 8.3%. However, steel demand would largely depend on the government spending on infrastructure development, growth in real estate sector driven by stimulus packages and recovery in steel consuming sectors like automobiles, consumer durables etc.

DI pipe industry

The fortunes of domestic DI pipe industry are directly linked to the quantum of funds allocated for water supply & sewerage disposal projects by GoI. Over the years, GoI has laid emphasis on creating water & sewage infrastructure as demonstrated by the fact that the eleventh five year (FY08-FY12) plan envisages USD 83 bn of investments in irrigation and water supply and sanitation. Accordingly, demand for DI pipes is expected to grow at 15% p.a. over the next few years. This is also due to conversion of demand from other varieties of pipes to DI pipe, stemming from estimated growth in demand for water in India from 800 bn cu.m. in 2007 to 1,100 bn cu.m. by 2010.

DISCLAIMER:

CARE's IPO grading is a one time assessment and the analysis draws heavily from the information provided by the issuer as well as information obtained from sources believed by CARE to be accurate and reliable. However, CARE, does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. CARE's IPO grading does not take cognizance of the price of the security and it is not a recommendation to buy, sell or hold shares/securities. It is also not a comment on the offer price or the listed price of the scrip. It does not imply that CARE performs an audit function or forensic exercise to detect fraud. It is also not a forecast of the future market performance and the earnings prospects of the issuer; also it does not indicate compliance/violation of various statutory requirements. CARE shall not be liable for any losses incurred by users from any use of the IPO grading.

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