



CREDIT ANALYSIS & RESEARCH LTD.

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Mr. Viral Mukundbhai Shah,
Chairman & Managing Director
Gyscoal Alloys Limited,
2nd Floor, Mrudul Tower,
Behind Times of India,
Ashram Road,
Ahmedabad - 380009

September 03, 2010

Dear Sir,

IPO Grading

1. Please refer to our letter dated August 31, 2010 on the above subject.
2. The rationale for the grading is attached as an **Annexure - I**. Kindly note that the rationale would be published in the forthcoming issue of our quarterly journal, 'CAREVIEW'.
3. A write-up on the above grading is proposed to be issued to the press shortly. A draft of the press release is enclosed for your perusal as **Annexure - II**.
4. We request you to peruse the Rationale and Press Release and offer your comments, if any. We are doing this as a matter of courtesy to our clients and with a view to ensure that no factual inaccuracies have inadvertently crept in. Kindly revert as early as possible. In any case, if we do not hear from you by September 09, 2010 we will proceed on the basis that you have no comments to offer.

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

Thanking you,

Yours faithfully,

Vishal Srivastav

[Vishal Srivastav]
Analyst

Dhimant Kothari

[Dhimant Kothari]
Sr. Manager

Encl: As above

September 03 2010



Annexure - I

Grading Rationale

Gyscoal Alloys Limited

Grading Assigned

Particulars	Number of equity shares (in lakh)	Grading¹	Remarks
IPO Grade	77 shares of face value Rs.10 each	'CARE IPO Grade 2' [Two]	Assigned

CARE has assigned a **'CARE IPO Grade 2'** to the proposed IPO of Gyscoal Alloys Limited (GAL). **'CARE IPO Grade 2'** indicates **Below Average Fundamentals**. CARE assigns IPO grades on a scale of Grade 5 to Grade 1, with Grade 5 indicating strong fundamentals and Grade 1 indicating poor fundamentals. CARE's IPO grading is an opinion on the fundamentals of the issuer. The grade assigned to any individual issue represents a relative assessment of the 'fundamentals' of the issuer.

GAL proposes an initial public offering of 77, 00,000 equity shares of face value of Rs.10 through 100% book building process.

Grading Rationale

The grading is constrained by the inherent cyclical nature of stainless steel industry and project execution risk associated with the proposed large sized expansion project of melting facility which is to be funded by the proposed IPO. Instances of overdrawn working capital limits from banks, instances of delay in servicing term loan interest and statutory payments and moderate corporate governance practices also constrain the grading.

¹ Complete definition of the grading assigned is available at www.careratings.com and other publications of CARE





The grading positively factors in the experience of the promoters, growth in sales during last three years ended FY09 and stable demand outlook for stainless steel industry.

Background

Ahmedabad based Gyscoal Alloys Limited (GAL), a closely held public limited company, was incorporated in 1999 as a private limited company. Initially, GAL started its business with the trading of iron and steel scrap, billets and steel long products. In 2005, the company took over a steel rolling mill with capacity of 6,000 Metric Tonnes Per Annum (MTPA) from Shah Alloys Group at Ubkhal, Mehsana in Gujarat and entered into manufacturing of rolled products. The rolling capacity was increased to 18,000 MTPA in FY06. In FY07, the company set up steel melting shop with a capacity of 12,000 MTPA which was further increased to 18,000 MTPA in the year FY09.

GAL manufactures alloy ingots & billets and stainless steel long products including angles, flats, hexagonal and Round Corner Squares (RCS), primarily from stainless steel scrap. It also undertakes rolling business on job-work basis by purchasing ingots / billets. These products have principal application in automobile forging, construction activities, infrastructure, kitchen equipments & appliances etc.

Objects of the proposed IPO are to finance its expansion project to increase its melting capacity by 1,00,000 MTPA, fund the long term working capital requirements and other general corporate purposes.

Management

The main promoters of GAL are Shri Viral M. Shah (Chairman and Managing Director), Smt. Giraben K. Solanki (Chief Executive Officer) and Shri Manish M. Shah (Whole-time Director). GAL's Board of Directors consists of 8 Directors, of which 4 are independent Directors. The Board is assisted by a team of senior executives.



Corporate Governance

Separation of ownership and management

GAL has a total of four independent directors on Board out of total of eight directors. The independent directors have been recently appointed by the company, with three of them appointed in February 2008 and the fourth in November 2009. GAL has delegated limited powers to senior / middle level management of the company and major decision-making and control rests with the promoters.

Board Committees

In order to comply with the provisions of Clause 49 of the Listing Agreement, GAL has constituted the Audit Committee, Remuneration Committee and Shareholders Grievance Committee. These committees are constituted in view of the IPO

Pending legal cases & their status

The Company is a defendant/plaintiff in various legal proceedings incidental to its business and operations. These legal proceedings are pending at different levels of adjudication before various courts.

A summary of these cases as on Feb.2010 is as follows:

Particulars	Total No. of cases	Amount (Rs. in Crore)
Under Criminal Laws		
Cases filed by the Company	10	0.85
Cases filed against the Company/Directors	3	0.42
Under Tax Laws		
Cases filed against the Company	2	Not Quantifiable
Cases filed against the Group Company	1	0.03
Under Civil Laws		
Cases filed against the Company / Directors	3	13.92

Operations

GAL's product portfolio includes alloy ingots & billets and stainless steel long products including angles, flats, hexagonal and round corner squares (RCS). The

company also manufactures squares and flats as per the customer's specifications. At present, the plant has the capacity to manufacture different grades of stainless steel products ranging between 200 series to 400 series. The present manufacturing set up of GAL is for production of lower grade of stainless steel like 200 series and some of the grades of 300 and 400 series which fetches moderate realisations as compared to other high grade steel. GAL has most of the sales in domestic market.

	FY07	FY08	FY09	6MFY10
Installed Capacity in MTPA				
Melting Section	12,000	12,000	18,000	18,000
Rolling Section	18,000	18,000	18,000	18,000
% Capacity Utilisation				
Melting Section	4.84	72.45	98.27	92.69
Total – Rolling	56.16	71.52		

- Company has changed its reporting policy from FY09 and hence, shown combined utilization in FY09 and 6MFY10.
- The pattern of raw material purchases entails that constitution of rolling operations is high viz-a-viz melting in FY09 and 6MFY10.

Top two customers constituted about 60% of total sales in FY09 and FY10, which reflects high level of customer concentration risk. Moreover, one of the top two customers of FY10 is a shareholder in one of the group companies of GAL.

Stainless steel (SS) industry is inherently cyclical in nature. The demand and prices of SS has experienced major fluctuation in the recent past and any adverse fluctuation in prices and / or downturn in demand could potentially affect GAL's profitability.

Ongoing Projects

Considering the demand potential of steel long products from sectors like infrastructure, construction, railway, etc. GAL has planned an expansion of its existing melting facilities of 18,000 MTPA to 118,000 MTPA with a total cost of Rs.57.70 crore [(1.67 times of net worth as on Mar.31, 2010 (prov.))] which is proposed to be funded by IPO proceeds and internal accruals.

This project was initially proposed in FY08. However, it got delayed due to deferment in IPO on account of adverse market conditions prevailing at that time. Upon improvement in market conditions, the company has again proposed to go ahead with

this project which is highly contingent upon the success of IPO. Project development is expected to start from Oct.'2010 and the likely commercial operation date (COD) is Oct.'2011.

The company has not made any major expenditure for the project and it is at preliminary stage. Though requisite land has been acquired, GAL has not converted the same to 'non-agriculture land'. The size of the project is very large as compared to its present scale of operations. GAL's proposed capacity of melting division is approx. 5 ½ times of its existing melting capacity. Major raw material purchases (60% of raw material cost) in FY09 were semi-finished goods like ingots/billets which signify under-utilisation of melting capacities. Despite the underutilized melting capacities (~70% utilization, as derived for FY09), GAL is planning for further expansion in capacity. Efficient utilisation of proposed capacity of melting hence appears uncertain.

IPO Details

Size of the Issue

GAL proposes to make a public offer of 77,00,000 equity shares at face value of Rs.10 each for cash at a premium to be determined through a book-building process.

Terms of the issue

- Out of 77,00,000 equity shares, 38,50,000 equity shares (being 50% of the issue size) will be available for allocation to the Qualified Institutional Bidders (QIBs), 5% of the QIB portion (1,92,500 equity shares) will be available for allocation on a proportionate basis to Mutual Funds only and remainder of the QIB portion shall be available for allocation on a proportionate basis to all QIBs, including Mutual Funds, subject to valid Bids being received at or above issue price (not yet finalised).
- At least 11,55,000 equity shares (being 15% of the issue size) will be available for allocation to Non Institutional Bidders and at least 26,95,000 equity shares (35% of the net issue size) will be available for allocation to Retail Individuals Bidders.

- Under-subscription, if any, in any category would be met with spill over from other categories or combination of other categories at the sole discretion of GAL in consultation with the book running lead manager. In case of inadequate demands from the Mutual Funds, the Equity Shares would be made available to QIBs other than Mutual Funds.

Purpose of the issue

- To finance the capital expenditure for enhancing the production capacity of melting section by 100,000 MTPA
- To meet the Long Term Working Capital requirements of the Company
- To meet General Corporate Purpose and
- To meet Issue Expenses

Financial Analysis

Total income grew at a CAGR of 29% during last 3 years ending FY10. PBILDT margin reduced significantly in FY09 due to inventory losses from sudden and steep decline in metal prices. In FY10, PBILDT margin remained almost in line with FY09 despite the increase in power & fuel as well as employee costs on the back of relatively lower manufacturing and administrative overheads and decline in selling expenses. PAT margin improved marginally in FY10 due to lower proportion of increase in interest & financial charges and lower tax outgo. On back of improvement in PAT, EPS & RONW in FY10 improved.

Interest coverage remained comfortable in FY10. Long term debt equity ratio and overall gearing improved as on Mar.31, 2010 mainly on account of infusion of equity during FY10. In spite of moderate current ratio, high amount of inventory holding kept quick ratio low at 0.65 times as on Mar.31, 2010. Working capital cycle and working capital turnover shows deterioration on y-o-y basis in FY08-FY10.

Stretched working capital position and cash flow mismatches led to overdrawn of working capital limits and instances of delay in interest servicing, apart from few delays in statutory payments.

Industry Review

Stainless Steel (SS) prices are largely determined by the demand-supply dynamics and the prices of the alloying elements. Since 70% of global SS is of austenitic variety, the price of nickel is an important determinant of SS price. Historically, nickel prices have exhibited significant volatility primarily because of its lower reserves, and the consequent inability to augment mine production quickly. The pricing of SS is typically bifurcated into two components – the base price and the alloy surcharge.

There has been an increase in production of SS from Q3CY09 after the slowdown in CY08 and part of CY09 on account of global economic recession.

Domestic SS production has grown at a CAGR of 13.4% in the period of FY 2000 to FY2009. Production of SS flat products has grown at a CAGR of 12.6% in the same period whereas the production of SS longs has grown at a CAGR of 16.7%. Usage of long SS products has picked up in the past few years especially from the construction and transportation sectors. Besides, domestic SS industry witnessed a notable capacity addition in the last two years. As a result, capacity utilisation of the industry has declined from the average level of 85% in FY 05-07 to the level below 80% in the past two years.

Overall, in view of the stable demand for the SS products, on the back of increased usage in construction industry, its outlook seems positive.

Prospects

The prospects of GAL in the medium term would be governed by its ability to manage raw material price fluctuation & thereby improve its profitability, implementation of proposed expansion project without time & cost overrun and effective management of working capital.

Financial Performance

(Rs. crore)

<i>For the period ended / as at,</i>	31/3/08	31/3/09	31/3/10
	(12m, A)	(12m, A)	(12m, UA)
<u>Working Results</u>			
Total income	122.03	129.90	156.84
PBILDT	17.31	9.55	11.41
Depreciation	2.75	2.08	2.59
Interest and finance charges	3.07	4.35	4.44
Profit from operations (before Tax)	11.55	3.17	4.41
PAT	7.31	1.79	3.01
Gross cash accruals	10.60	4.74	6.30
<u>Financial Position</u>			
Equity share capital	6.59	6.59	8.13
Net-worth	18.37	24.69	34.62
Total capital employed	35.58	49.68	63.70
<u>Key Ratios</u>			
<i>Growth (%)</i>			
Growth in Total Income	65.29	6.45	20.74
Growth in PAT (after D. Tax)	160.74	-75.52	68.30
<i>Profitability (%)</i>			
PBILDT / Total income	14.18	7.35	7.28
PAT / Total income	5.99	1.38	1.92
ROCE	50.20	17.81	15.61
RONW	54.60	8.31	10.15
<i>Solvency</i>			
Long-term debt equity ratio	0.30	0.18	0.11
Overall gearing ratio	0.93	1.00	0.83
Interest coverage (times)	4.74	1.72	1.99
Current ratio	1.20	1.25	1.30
Quick ratio	0.46	0.63	0.65
<i>Turnover</i>			
Working capital turnover ratio	7.38	4.79	4.13
Average Collection Period (days)	43	49	54
Average Inventory (days)	87	95	81
Average Creditors (days)	92	71	55
Operating cycle (days)	38	73	80
<i>Earnings</i>			
Dividend (%)	0%	0%	0%
Earnings per Share (Basic) - (Rs.)	11.09	2.71	3.70

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.