

India

Underweight (no change)

Highlighted Companies

Steel Authority of India

REDUCE, TP Rs58, Rs85 close

SAIL faces the risk of incurring losses in 1QFY24F due to a lower-than-expected volume. Retain REDUCE rating on SAIL with a target price of Rs58.

Tata Steel

REDUCE, TP Rs70, Rs111 close

Performance disparity likely between Tata Steel's Indian and European businesses. We retain our high conviction REDUCE rating on Tata Steel.

JSW Steel

REDUCE, TP Rs330, Rs763 close

JSW Steel remains one of the costliest steel stocks, but we struggle to find out the fundamental reasons for the same. The consensus earnings of JSW Steel are highly elevated. We retain REDUCE rating on the stock with a target price of Rs330.

Summary Valuation Metrics

P/E (x)	Mar22-A	Mar23-A	Mar24-F
Steel Authority of India	2.92	-39.52	13.27
Tata Steel	3.24	10.71	21.03
JSW Steel	10.98	64.33	-25.96

P/BV (x)	Mar22-A	Mar23-A	Mar24-F
Steel Authority of India	0.67	0.73	0.69
Tata Steel	1.18	1.09	1.05
JSW Steel	3.42	3.39	4.1

Dividend Yield	Mar22-A	Mar23-A	Mar24-F
Steel Authority of India	0%	0%	0%
Tata Steel	22.57%	1.81%	1.81%
JSW Steel	0.85%	0.85%	0.85%

Steel

1QFY24 Preview - Disappointment likely

- India's steel demand is growing but the global slowdown and Chinese imports pose challenges. However, consensus earnings estimate still highly inflated.
- In 1QFY24F, costs are in control with stable coking coal prices, and a minor correction in domestic HRC and steel long prices but rising Indian iron ore prices are negative for unintegrated players.
- Disappointment may come from SAIL (REDUCE) if its sales remain below 3.8-3.9mt while a lower volume poses risk for JSW Steel (REDUCE) and in case of Tata Steel (REDUCE), the European market remains a challenge.

Disappointment likely in 1QFY24F earnings

India's steel demand continues to grow at a healthy pace of 8-9% but the industry is facing challenges due to the global slowdown and a rise in Chinese imports. 1QFY23 cost management was effective with coking coal prices stable at US\$220-230/t. While there has been a slight decline in domestic hot rolled coil or HRC and long steel prices, coking coal also experienced a similar correction. While we are still slowly moving towards the earnings bottoming out, consensus estimates are still factoring in a higher than mid-cycle EBITDA/t.

Rising imports and thus lower domestic sales pose risk to steel firms

SAIL needs to register steel sales of more than 3.8mt in 1QFY24F to achieve profitability. Our assumption of 3.8mt reflects a growth of approximately 20% vs. 1QFY23 level. This target is still attainable due to mandatory shutdown of JSW Steel's plant. However, SAIL faces the risk of incurring losses in 1QFY24F as the company's profitability, like JSW Steel, is dependent on the volume of steel sold in the domestic market. For JSW Steel, if standalone steel sales remain below 4.5mt, it would negatively impact the bottom line. While Tata Steel's India business continues to thrive, its European business is likely to face challenges due to the decline in electricity prices in Europe which is expected to drive an increase in steel production via the electric arc furnace or EAF route, thereby leading to a fall in blast furnace or BF-based steel volume and margins.

Favourable outlook on HEG

Graphite electrode cycles in CY17 and CY18 were driven by China's steel production growth causing supply chain shock and higher electrode prices. Capacity ramp-up lag led to supply chain scarcity, and this led to a rise in graphite electrode prices. Despite challenges, steel production grew in 2021, but faced a setback in 2022 due to high power prices and Covid-19 pandemic policies. There are some signs indicating a rebound in Chinese steel production in 2023F, driven by EAF-based production. Both Europe and China are expected to see a rise in EAF-based steel production due to environmental concerns. The rise in EAF-based steel production is good for graphite electrode demand and hence, its prices.

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Figure 1: Ratings of various stocks in our steel coverage universe

Ticker	Company Name	Rating
JSP IN	Jindal Steel and Power	ADD
HEG IN	HEG	ADD
JSTL IN	JSW Steel	REDUCE
SAIL IN	Steel Authority of India	REDUCE
TATA IN	Tata Steel	REDUCE
NMDC IN	NMDC	HOLD

SOURCE: INCRED RESEARCH, COMPANY REPORTS

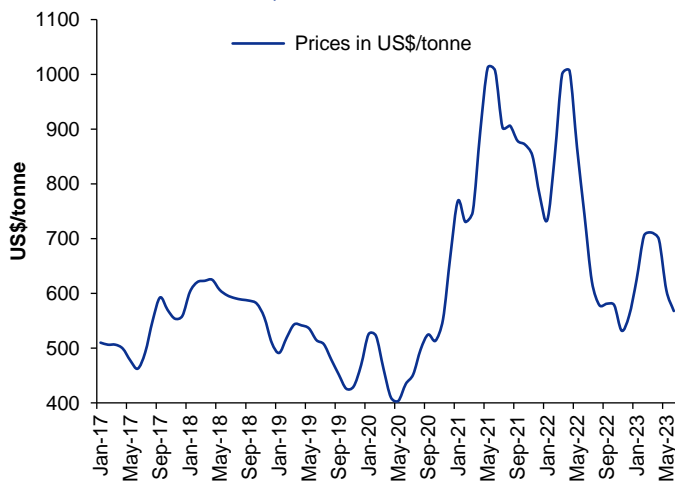
1QFY24F Preview - Disappointment likely

While a YoY comparison will be futile for 1QFY24F, as last year the same quarter fared much better, but consensus earnings are quite far from reality and may be after this quarter, there will be a downward correction in consensus earnings estimates. Steel Authority of India or SAIL will struggle to make profits for the quarter and if its sales are below 3.8-3.9mt, then it will make losses on PBT. Like Indian cement, Indian steel demand is also growing at a healthy 8-9% pace but the global slowdown and Chinese imports are making the industry struggle.

Costs remain under control and realization flat in 1QFY24F vs. 4QFY23

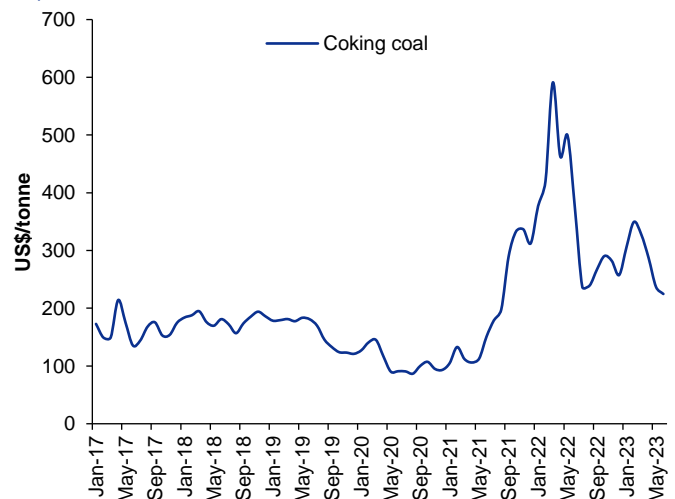
In 1QFY24F, overall costs were under control as coking coal prices remained around US\$220-230/t level. There has been a minor downward correction in domestic HRC and long steel prices, but coking coal also witnessed a similar correction. As we had expected, Indian domestic iron ore prices are rising, which will negatively impact unintegrated players in the country.

Figure 2: HRC export prices are trending downwards, but they should stabilize near US\$525-550/t



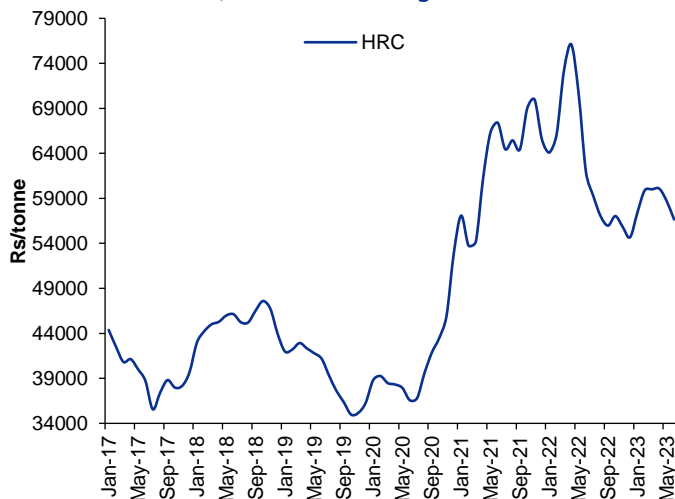
SOURCE: COMPANY REPORTS, INCRED RESEARCH

Figure 3: Coking coal prices are back to the stable level of US\$225/t



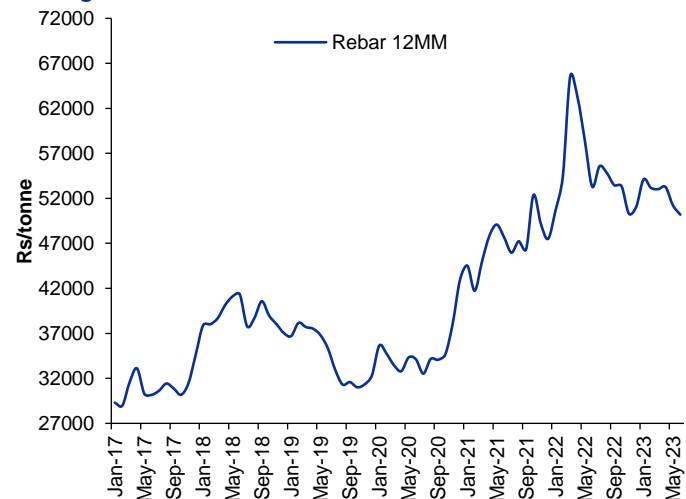
SOURCE: COMPANY REPORTS, INCRED RESEARCH

Figure 4: Domestic HRC prices have some scope for a correction to ~Rs55,000/t in the coming months



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 5: Rebar prices can fall to Rs 47,000-48,000/t in the coming weeks



SOURCE: INCRED RESEARCH, COMPANY REPORTS

SAIL needs to achieve a volume of more than 3.8mt to make positive PBT

SAIL must sell more than 3.8mt of steel to make profits in 1QFY24F. We have assumed 3.8mt of steel sales, which is ~20% growth over 1QFY23 level. This kind of sales level can still be achieved as JSW Steel is running a mandatory plant shutdown. However, SAIL carries a risk of making losses in 1QFY24F.

Figure 6: SAIL must sell more than 3.8mt of steel to make PBT in 1QFY24F; we have assumed 3.8mt sales as we believe the plant shutdown by JSW Steel will help SAIL

	1QFY23	2QFY23	3QFY23	4QFY23	1QFY24F	YoY	QoQ
Net Revenue	2,40,286	2,62,463	2,50,419	2,91,306	2,32,730	-3%	-20%
Total Cost of Goods Sold	1,14,832	1,64,182	1,35,252	1,55,044	1,21,600	6%	-22%
Employee Cost	30,150	28,326	27,730	34,331	30,309	1%	-12%
Other Expenses	72,297	62,629	66,669	72,793	64,600	-11%	-11%
Total Expenses	2,17,278	2,55,137	2,29,651	2,62,167	2,16,509	0%	-17%
EBITDA	23,008	7,326	20,768	29,139	16,222	-29%	-44%
Other Income	3,054	4,412	1,208	4,875	3,054	0%	-37%
Operating Profit	26,062	11,738	21,975	34,013	19,276	-26%	-43%
Depreciation	11,939	11,832	12,210	13,644	13,644	14%	0%
EBIT	14,123	-94	9,765	20,369	5,632	-60%	-72%
Interest Expenses	3,740	5,062	6,403	5,170	5,170	38%	0%
Extraordinary Items	0	0	2,984	-404			
Profit Before Tax	10,383	-5,156	6,347	14,795	462	-96%	-97%
Total Tax Expense	2,620	-1,298	1,712	4,305	116	-96%	-97%
Profit After Tax	7,763	-3,858	4,635	10,490	346	-96%	-97%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Tata Steel – European market to be the key deciding factor

Tata Steel's India business is robust as ever but it's the European business which remains in trouble. The fall in electricity prices in Europe will lead to an inevitable rise in EAF-based steel production, which will lead to a fall in BF-based steel volume as well as margins.

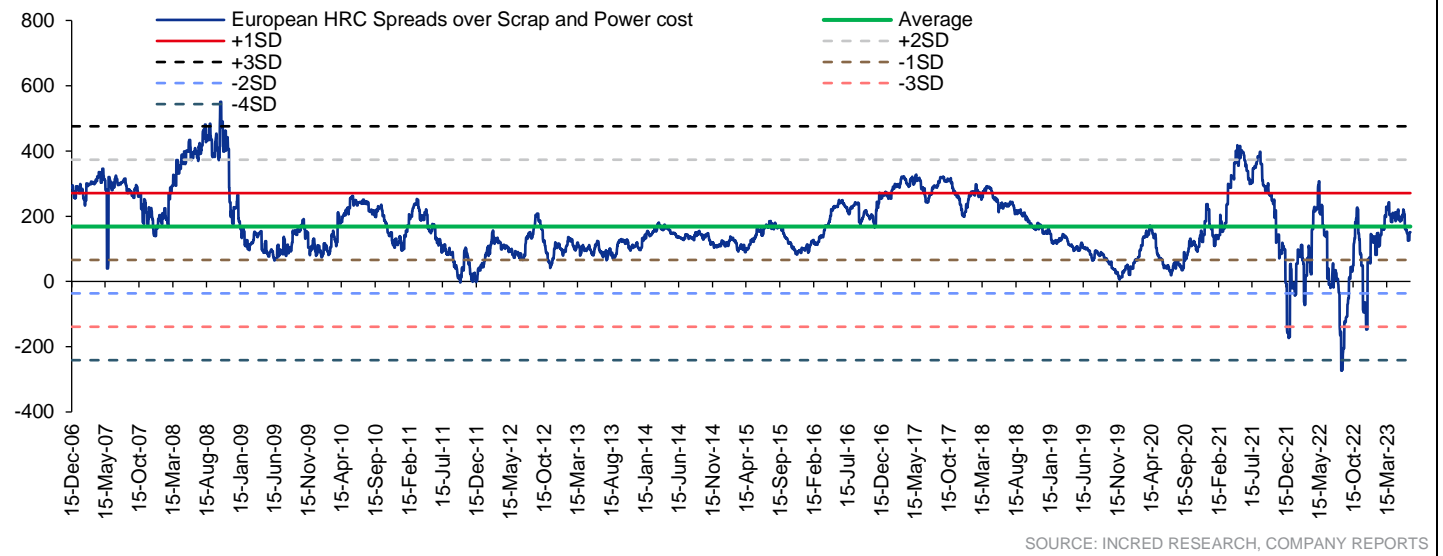
Figure 7: Unless otherwise there are some extraordinary items, Tata Steel's European operations shall make negative EBITDA

	4QFY21	1QFY22	2QFY22	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23	4QFY23	1QFY24F	YoY	QoQ
Deliveries (mt)	2.5	2.3	2.1	2.2	2.4	2.1	1.9	2.0	2.2	2.04		
Total revenue from operations	1,72,580	1,94,410	2,14,240	2,27,688	2,63,890	2,59,610	2,15,588	2,07,446	2,20,360	201960	-22%	-8%
Expenses												
Total cost of goods sold	72,190	83,270	81,400	84,150	1,02,660	85,990	96,900	1,14,800	1,12,800	1,02,453	19%	-9%
Employee costs	88,450	35,880	37,620	36,730	38,550	39,290	31,140	31,960	34,480	34,480	-12%	0%
Other expenses		60,010	62,220	77,470	79,390	74,150	69,720	76,290	89,420	76,290	3%	-15%
Total expenses	1,60,640	1,79,160	1,81,240	1,98,350	2,20,600	1,99,430	1,97,760	2,23,050	2,36,700	2,13,223	7%	-10%
EBITDA	11,940	15,250	33,000	29,338	43,290	60,180	17,828	-15,604	-16,340	-11,263	-119%	-31%

SOURCES: INCRED RESEARCH, COMPANY REPORTS

EAF-based steel production becomes profitable by putting BF-based steel supply under pressure

Figure 8: After a couple of years of volatility, power prices are in control in Europe, thereby leading to higher EAF-based steel spreads; relatively cleaner EAFs are back in top production (with carbon tax benefits) which will exert pressure on BF-based steel volume



We believe that LNG prices will remain under pressure, which will keep power prices under check in Europe

Figure 9: Total European gas imports are trending downwards...

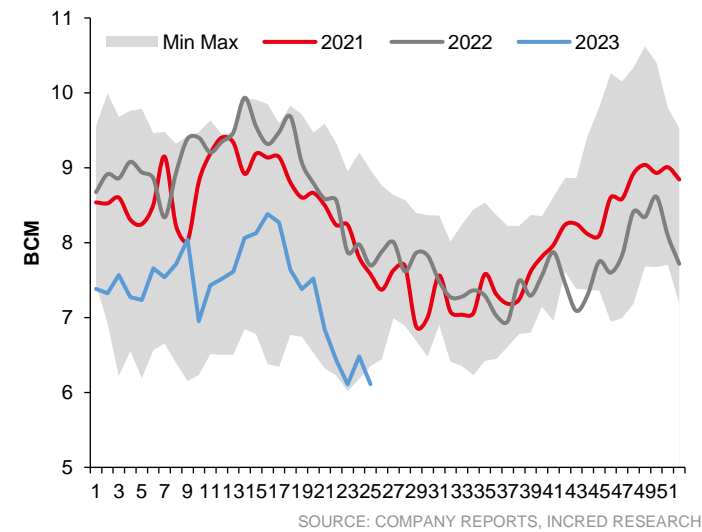
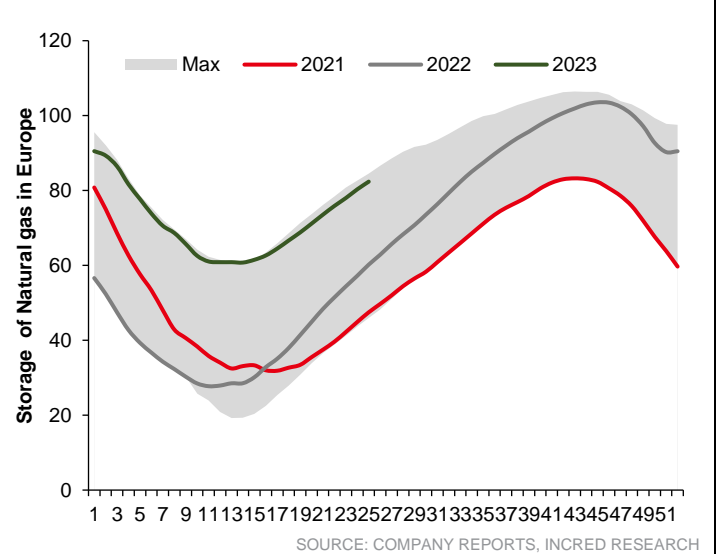


Figure 10: ...as gas storage is filled to all-time high levels



Relative to EAF-based steel, European BF-based steel's margins are going down ➤

Figure 11: BOF-EAF steel spread differential is near its historical average and as power prices go down further, it will only increase the pressure on overall prices of HRC in Europe



SOURCE: INCRED RESEARCH, COMPANY REPORTS

India business to remain healthy but may not be able to fill the gap in Europe ➤

Figure 12: We expect standalone profits to decline 61% YoY and 40% QoQ; EBITDA/t to remain at ~Rs12,500/t

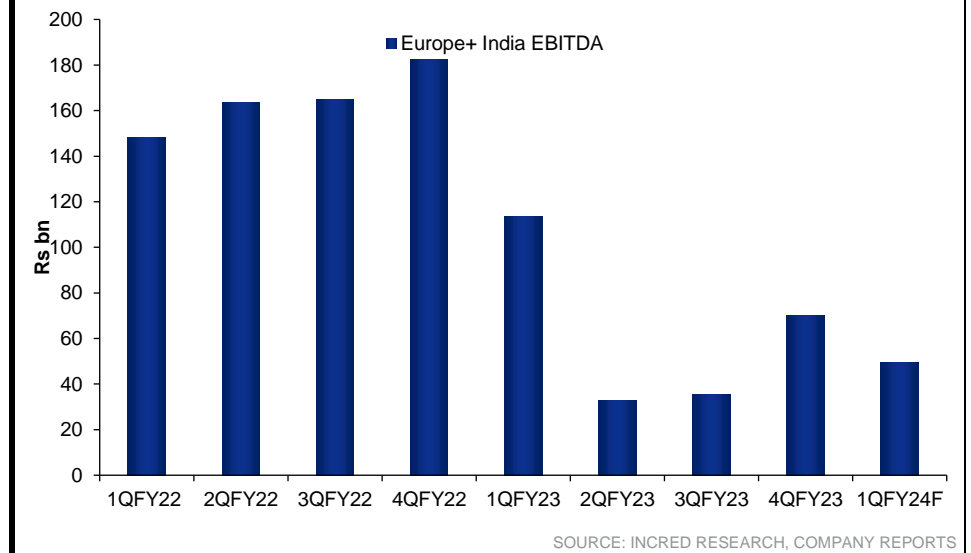
	1QFY22	2QFY22	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23	4QFY23	1QFY24F	YoY	QoQ
Net Sales	2,68,626	3,23,820	3,16,234	3,62,455	3,16,866	3,18,608	3,01,211	3,37,981	2,67,470	-16%	-21%
Other Operating Income	7,334	3,046	3,408	4,354	3,345	3,842	3,442	4,772	3,345	0%	-30%
Net Revenue	2,75,959	3,26,866	3,19,643	3,66,809	3,20,211	3,22,450	3,04,653	3,42,753	2,70,816	-15%	-21%
Total Cost of Goods Sold	56,787	81,247	93,372	1,44,723	1,27,735	1,78,343	1,50,493	1,46,797	1,17,909	-8%	-20%
Employee Cost	15,464	15,431	15,531	17,232	15,402	16,468	16,098	18,195	16,942	10%	-7%
Other Expenses	70,733	95,888	89,059	82,512	81,394	79,198	86,466	96,459	86,466	6%	-10%
Total Expenses	1,42,984	1,92,566	1,97,962	2,44,467	2,24,531	2,74,010	2,53,056	2,61,450	2,21,316	-1%	-15%
EBITDA	1,32,975	1,34,300	1,21,680	1,22,343	95,680	48,440	51,597	81,302	49,500	-48%	-39%
Depreciation	13,717	13,520	13,602	13,798	13,440	13,489	13,705	13,712	13,712	2%	0%
EBIT	1,19,258	1,20,781	1,08,078	1,08,545	82,241	34,951	37,892	67,591	35,788	-56%	-47%
Other Income	2,838	3,821	2,799	5,062	7,356	10,176	9,070	6,653	6,653	-10%	0%
Interest Expenses	7,726	7,298	6,441	6,456	7,224	9,582	10,733	10,384	10,384	44%	0%
Extraordinary Items	1,527	-1,307	-1,810	-765	-548	-194	-56	-6,990	0		
Profit Before Tax	1,15,897	1,15,997	1,02,627	1,06,386	81,825	35,351	36,173	56,870	32,057	-61%	-44%
Total Tax Expense	28,096	28,914	25,793	27,991	20,684	8,802	9,122	16,661	8,078	-61%	-52%
Profit After Tax	87,801	87,083	76,834	78,395	61,142	26,550	27,051	40,209	23,979	-61%	-40%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Europe+ Indian business EBITDA to remain way below 1QFY23 level ➤

More than the decline, the absence of balance sheet deleveraging will hurt Tata Steel's share price.

Figure 13: Europe+ Indian business EBITDA to decline by 56% YoY and 29% QoQ



JSW Steel's earnings likely to decline YoY and QoQ

Like SAIL, JSW Steel's profit or loss will be dependent on the volume sold in domestic market. A sale of 4.5mt of steel will have an exponentially negative impact on its bottom line.

Figure 14: We expect its standalone profits to decline 50% YoY and 83% QoQ

	1QFY22	2QFY22	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23	4QFY23	1QFY24F
Net Revenue	2,59,590	2,80,000	2,88,500	3,60,110	3,11,050	3,24,940	3,09,350	3,71,530	2,85,346.0
Cost of Goods Sold	59,800	1,08,850	1,28,490	1,88,650	1,70,850	2,17,530	1,69,610	1,98,950	1,53,118.8
Employee Expenses	4,410	4,540	4,980	4,770	4,370	4,990	5,290	5,100	4,800.0
Power & Fuel Costs	17,330	20,210	24,410	27,350	36,190	36,080	33,820	32,330	31,000.0
Other Expenses	83,140	59,670	62,650	70,270	66,120	48,920	60,330	72,680	64,120.0
EBITDA	94,910	86,730	67,970	69,070	33,520	17,420	40,300	62,470	32,307.1
Depreciation	9,980	10,510	12,370	12,250	11,770	12,070	12,630	13,050	13,050.0
EBIT	84,930	76,220	55,600	56,820	21,750	5,350	27,670	49,420	19,257
Other Income	2,000	9,190	3,940	4,160	2,830	4,220	3,150	5,520	2,830.0
Interest Expenses	8,430	8,020	8,870	13,170	10,300	10,930	13,440	15,560	15,560.0
Exceptional Items	0	0	0	-7,220	0	0	0	0	0
Profit Before Tax	78,500	77,390	50,670	40,590	14,280	-1,360	17,380	39,380	6,527.1
Tax Expenses	25,920	23,560	16,430	14,220	4,720	-450	5,040	11,000	1,644.8
Profit After Tax	52,580	53,830	34,240	26,370	9,560	-910	12,340	28,380	4,882.3

SOURCE: INCRED RESEARCH, COMPANY REPORTS

JSPL's earnings likely to decline YoY and QoQ

Figure 15: We expect its EBITDA to decline by 49% YoY and 20% QoQ

JSPL Standalone (Rs m)											
	1QFY22	2QFY22	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23	4QFY23	1QFY24F	YoY	QoQ
Net Revenue	1,03,846	1,32,612	1,19,548	1,38,308	1,28,485	1,31,071	1,18,323	1,33,923	1,19,777	-7%	-11%
Expenses											
Total Cost of Goods Sold	28,733	52,832	52,887	66,179	53,279	68,421	54,144	67,964	58,987	11%	-13%
Employee Cost	1,778	1,777	1,909	1,782	2,025	2,228	2,231	2,258	2,025		
Other Expenses	28,291	32,931	33,270	42,380	41,739	43,018	41,755	42,411	41,739		
Total Expenses	58,609	87,423	87,873	1,10,043	95,377	1,12,694	95,878	1,12,521	1,02,751	8%	-9%
EBITDA	45,237	45,189	31,675	28,266	33,108	18,377	22,445	21,402	17,026	-49%	-20%

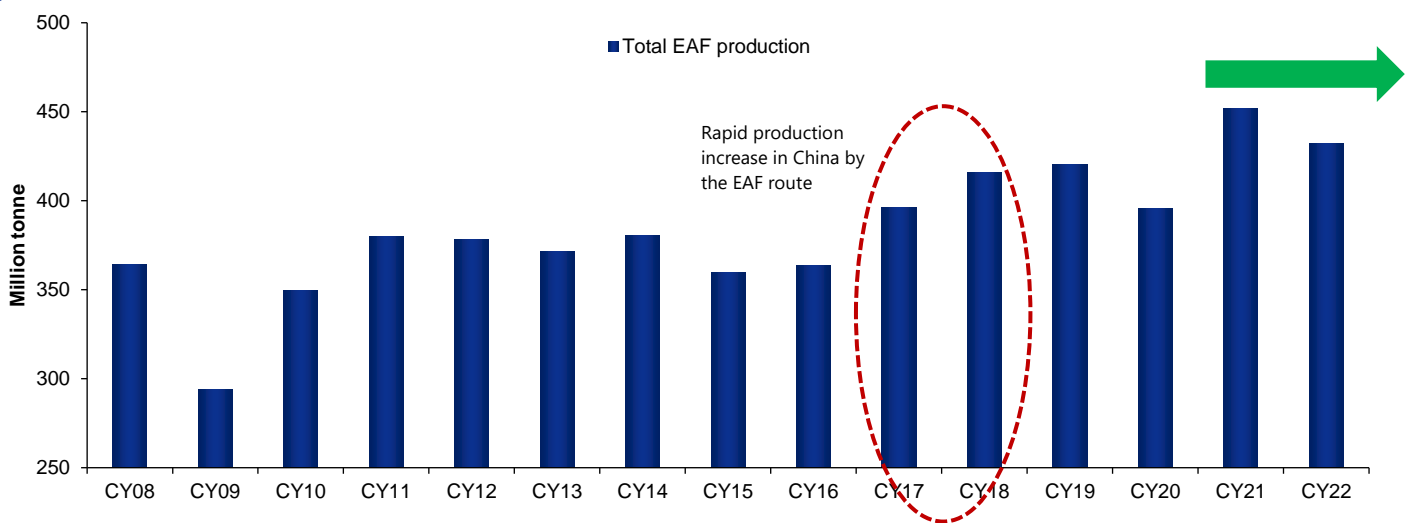
SOURCE: INCRED RESEARCH, COMPANY REPORTS

HEG likely to post a sequential improvement in its earnings but witness a fall YoY

The cycle is changing for HEG and we are near the bottom of the graphite electrode cycle ➤

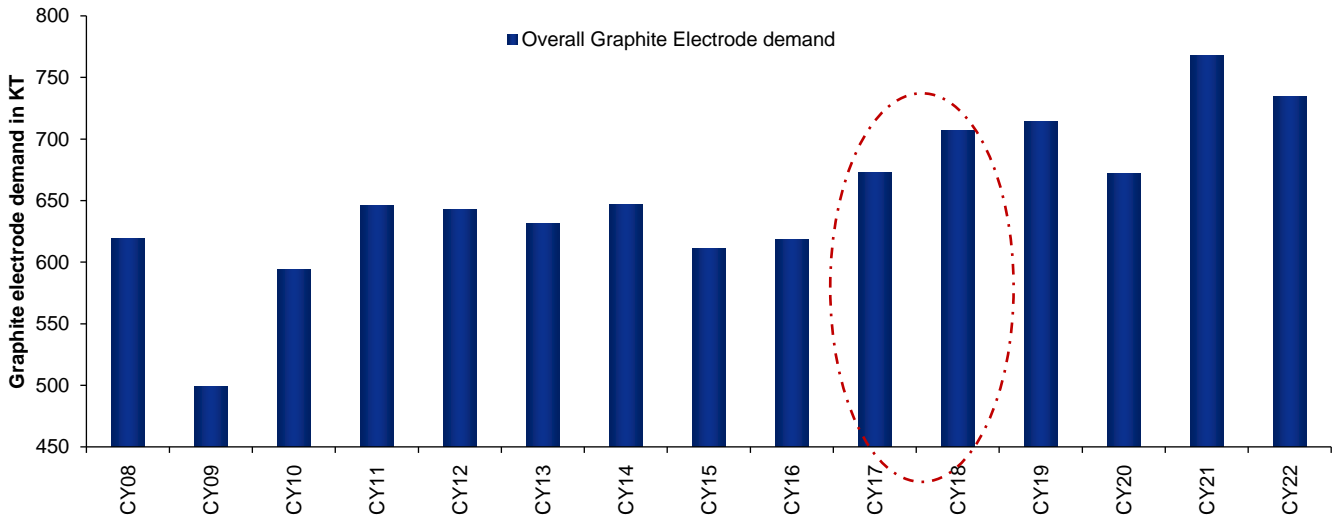
- CY17 and CY18 bull cycles in electrodes were driven by rising steel production in China. In fact, in two years, China's EAF-based production more than doubled, which led to supply chain shock and electrode prices rose.
- Please note that while the capacity was always available to manufacture electrodes, ramping up capacity needs a time of around six months. Hence, there was supply chain scarcity-led rise in graphite electrode prices.
- The year 2021 saw the same phenomenon, as against all doomsday predictions, steel production rose by 3.8% and EAF-based production rose by 14%. 2022 was a washout as higher power prices in Europe led to a decline in EAF-based steel production. Also, China's steel production declined because of stringent Covid-19 pandemic policies.
- In 2023, all signs are indicating that Chinese steel production is rising and, as usual, it will be led by the rise in EAF-based production. Please note that when scrap prices were low, China had accumulated a huge quantity of scrap. So, we are unlikely to witness a huge influx of scrap into China. Don't wait for a signal of rising scrap imports to assume that EAF-based steel production is rising.
- Power prices in Europe have collapsed as European consumers have shown remarkable resilience and cut their power consumption. We expect LNG prices to remain subdued, which will lead to subdued power prices. Please click our report: [IN: Gas Transmission & Dist - Volume growth concerns are behind us](#).
- EAF-based steel production is bound to rise again in Europe as well as in China, more so as environmental concerns are growing in Europe and the EAF route is at least 80% less polluting compared to the blast furnace route for making steel.
- On the flip side, rising production will be bad for steel prices as such but European EAF-based steel will easily make historical average gross spreads over power and scrap prices.

Figure 16: The first major change in EAF-based steel production happened in CY17 and CY18 when China's EAF-based steel production doubled from 50.9mt in CY16 to 109mt in CY18



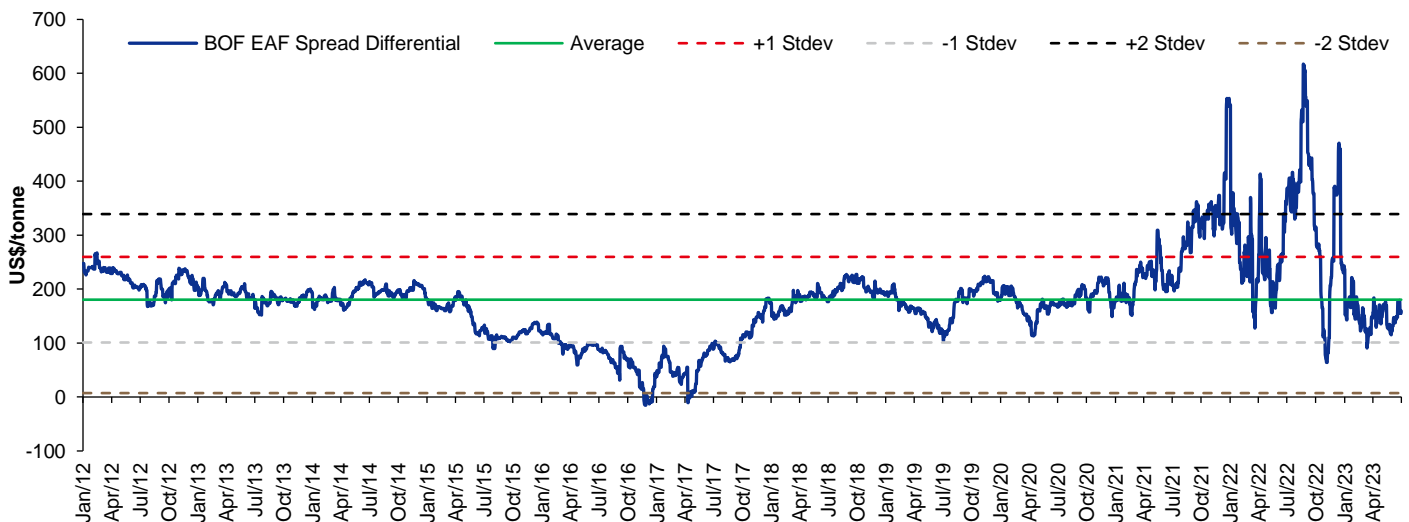
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 17: As a result, graphite electrode demand rose by ~95kt in 24 months; please remember that ramping up capacity of electrode plants is not easy and the demand shock led to a slow production response and thus, the rise in electrode prices



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 18: EAF-based steel production will revive in Europe as the spreads over scrap and power have revived; its gross profitability is equal to that of BF-based steel and is also more environment friendly



SOURCE: INCRED RESEARCH, COMPANY REPORTS

HEG's 1QFY24F numbers have to be seen in this perspective - that we are nearing the beginning of the new cycle ➤

Figure 19: The company's profits to improve sequentially but will be down YoY

	1QFY22	2QFY22	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23	4QFY23	1QFY24F	YoY	QoQ
Net Revenue	4,140	5,180	5,970	6,730	7,220	5,980	5,300	6,170	5,926	-17.9%	-4%
EBITDA	720	1,420	1,560	1,570	1,840	1,790	1,320	1,230	1,422	-22.7%	16%
EBITDA/t	40,000	78,889	86,667	87,222	1,00,000	97,283	1,10,000	82,000	1,04,575	4.6%	28%
Profit After Tax	570	1,320	1,130	1,290	1,590	1,690	1,050	1,000	1,152	-27.5%	15%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

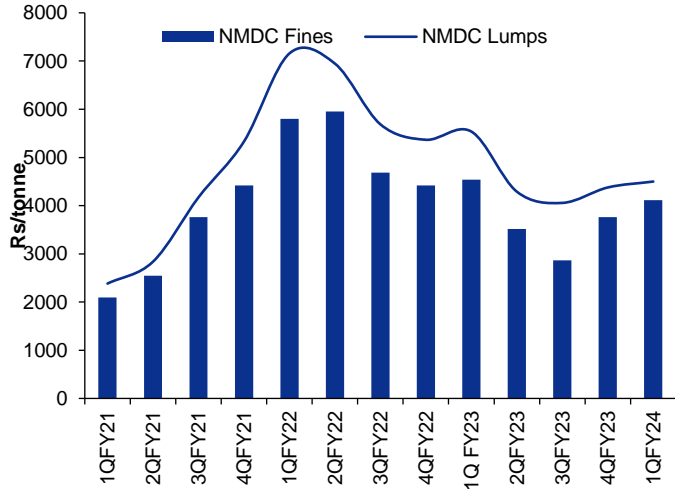
NMDC's profits to improve YoY and QoQ

As expected, Indian iron ore prices are rising >

Please click our report: [IN: Steel - Rise in raw material cost & fall in steel price](#)

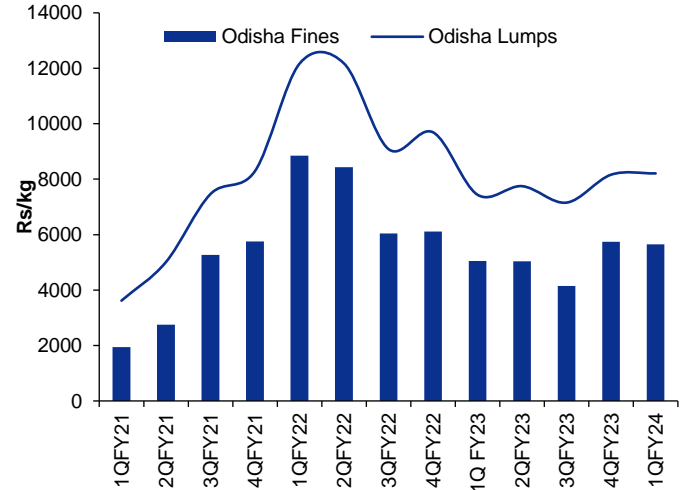
As we had written in this report, Indian iron ore prices are rising.

Figure 20: NMDC fines' prices have risen by 9% QoQ and lumps' prices have increased by 3% QoQ



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 21: Odisha fines' prices are flat QoQ but lumps' prices have risen by 1% QoQ



SOURCE: INCRED RESEARCH, COMPANY REPORTS

NMDC's profits likely to rise by 10% YoY but may fall by 30% QoQ >

Figure 22: NMDC's PAT likely to rise by 10% YoY

	1QFY22	2QFY22	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23	4QFY23	1QFY24F	YoY	QoQ
Net Revenue	65,122	67,935	58,738	67,022	47,671	33,285	37,200	58,514	55,201	16%	-6%
Total Cost of Goods Sold	-4,418	386	-435	-2,504	-2,442	7,371	-1,235	-2,391	2,230		
Employee Cost	2,681	2,894	3,116	4,645	3,269	3,969	3,449	4,579	3,497	7%	-24%
Royalty & Other Levies	20,155	27,608	25,089	27,015	23,626	8,695	18,689	26,241	23,576	0%	-10%
Selling Expenses incld Freight	500	520	378	880	366	521	770	972	892	144%	-8%
Other Expenses	4,426	5,381	4,466	10,143	3,851	4,186	4,094	7,459	4,000	4%	-46%
Total Expenses	23,345	36,789	32,614	40,179	28,670	24,743	25,766	36,860	34,196	19%	-7%
EBITDA	41,777	31,146	26,124	26,844	19,001	8,542	11,434	21,654	21,006	11%	-3%
Depreciation	552	596	606	1,115	848	738	836	932	932	10%	0%
EBIT	41,224	30,550	25,518	25,729	18,153	7,804	10,598	20,722	20,074	11%	-3%
Other Income	1,441	888	1,529	3,326	1,460	4,260	1,879	-120	1,460		
Interest Expenses	30	17	92	252	153	182	299	118	118	-23%	0%
Extraordinary Items								12,373			
Profit Before Tax	42,635	31,421	26,955	28,803	19,459	11,882	12,177	32,857	21,416	10%	-35%
Total Tax Expense	10,705	8,010	6,457	10,650	4,763	2,994	3,276	10,085	5,397	13%	-46%
Profit After Tax	31,930	23,411	20,498	18,153	14,696	8,888	8,901	22,773	16,019	9%	-30%

SOURCE: COMPANY REPORTS, INCRED RESEARCH

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