

India

Underweight (no change)

Highlighted Companies

Jindal Steel and Power

ADD, TP Rs476, Rs417 close

(The stock looks overvalued on all parameters, in our view. European asset sales are factored into its price)

JSW Steel

REDUCE, TP Rs330, Rs669 close

(We value JSW Steel at +1SD 8x FY22F to arrive at a TP of Rs 330. We have valued the stock at +1SD of its long-term mean as its balance sheet is deleveraging, and value-added products are increasing in the portfolio)

Tata Steel

REDUCE, TP Rs750, Rs1316 close

(We expect the company to fare well based on its value-added offerings but expect its profitability to fall, leading to a 6% EBITDA CAGR over FY21-23F)

Summary Valuation Metrics

P/E (x)	Mar21-F	Mar22-F	Mar23-F
Jindal Steel and Power	31.62	34.31	32.77
JSW Steel	25.53	31.18	30.77
Tata Steel	18.86	5.46	16.27
P/BV (x)	Mar21-F	Mar22-F	Mar23-F
Jindal Steel and Power	2.86	2.64	2.44
JSW Steel	3.46	3.22	3
Tata Steel	2.12	1.58	1.48
Dividend Yield	Mar21-F	Mar22-F	Mar23-F
Jindal Steel and Power	0%	0%	0%
JSW Steel	0.97%	0.97%	0.97%
Tata Steel	1.9%	1.9%	1.9%

Analyst(s)



Satish KUMAR

T (91) 22 4161 1562

E satish.kumar@incredcapital.com

Shaily RUPARELIA

T (91) 22 4161 1556

E shaily.ruparelia@incredcapital.com

Steel

Coking coal: High prices likely for long time

- Lack of investment in mining capacity and supply chain problems are leading to high coking coal prices.
- Some of the supply problems can be sorted out by increased EAF usage in China but increased Indian demand will act as a counterbalance.
- Coal can fall if steel demand falls, but then steel will also collapse as in any case steel spreads are bound to decline by US\$150-200/t in coming quarters.

Coking coal is in short supply and its prices to remain elevated

Production decline in Australia, high demand from India and China as well as supply chain problems are leading to elevated coking coal prices. The data on new mining investment from the ministry of mines in Australia doesn't paint a rosy picture. Only a single project by Glencore (8.5mt capacity for combined thermal and coking coal) in Mount Owen is slated in the near-term (i.e., in CY22F) and all others are likely to come in or after CY23F. Ministry of mines in Australia projects only 176mt of coal exports in CY21F and 183mt in CY22F, which is insufficient to balance the export market. The saving grace can be increased supply from USA (but ESG issues are impeding mining investment) or Russia (its supply is uncertain). However, if demand for steel slows down, then coking coal needs of blast furnaces will also go down. We are factoring in a big decline (6% in CY22F) in Chinese demand for coking coal as we believe China will shift to electric arc furnaces or EAFs. If China doesn't shift to EAFs (and steel demand there doesn't fall), then even higher prices of coking coal are likely, in our view.

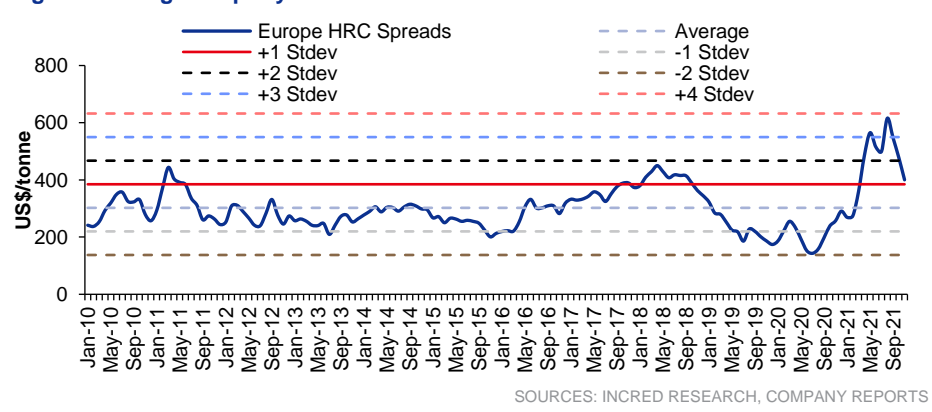
Steel is caught between a rock and a hard place

Indian steel companies are caught between a rock and a hard place. If steel demand collapses, then cost pressure will ease but steel prices will go down. And if steel demand remains strong, then Indian buying alone will lead to higher coking coal prices. In a nutshell, the decline in steel spreads is inevitable. All steel companies will report a significant decline in EBITDA/t in Q3FY22F, in our view. We expect at least a US\$100-125/t EBITDA decline in Q3FY22F over Q2. In Q4FY22F, steel companies like Steel Authority of India Ltd or SAIL would be barely making operational profits (given current realisation and coking coal prices).

Steel valuations are not factoring in significant profit decline; Reduce

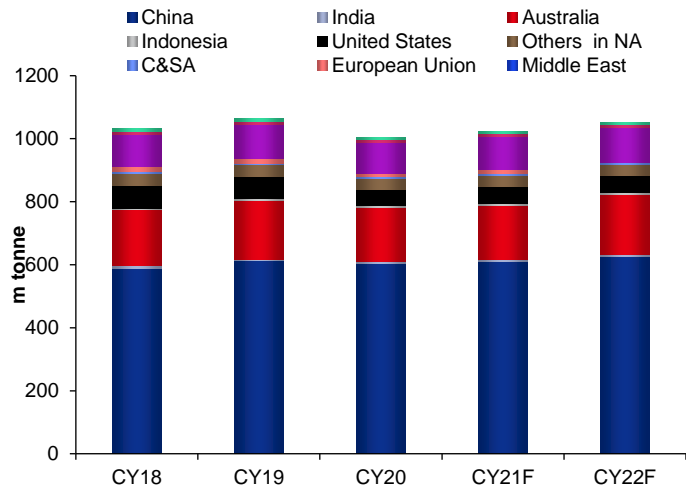
Indian steel universe (equally weighted index of JSW Steel, JSPL, Tata Steel and SAIL) is trading above 2X P/BV, which is near its all-time high. Ergo, they are not factoring in any decline in profitability of steel companies. Sell all steel stocks barring Jindal Steel and Power Ltd (JSPL). This company (JSPL) can still do well because of product fungibility and a relatively cheaper valuation. Within Indian steel space, we like only JSPL.

Figure 1: The global party for blast furnaces is over



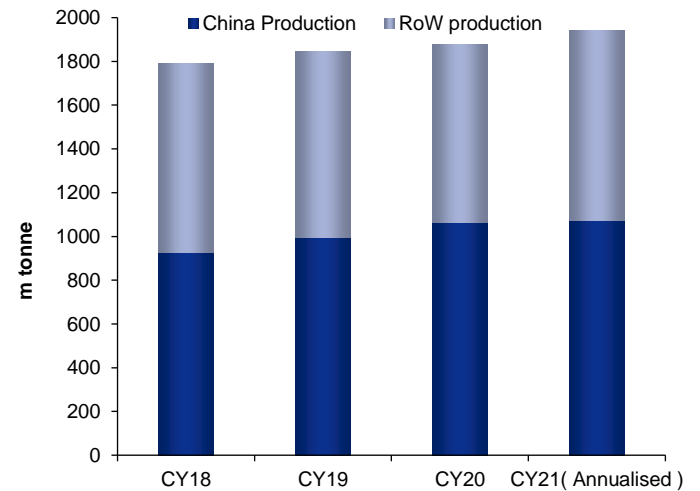
KEY CHARTS

Figure 2: Coking coal production has barely increased in last three years



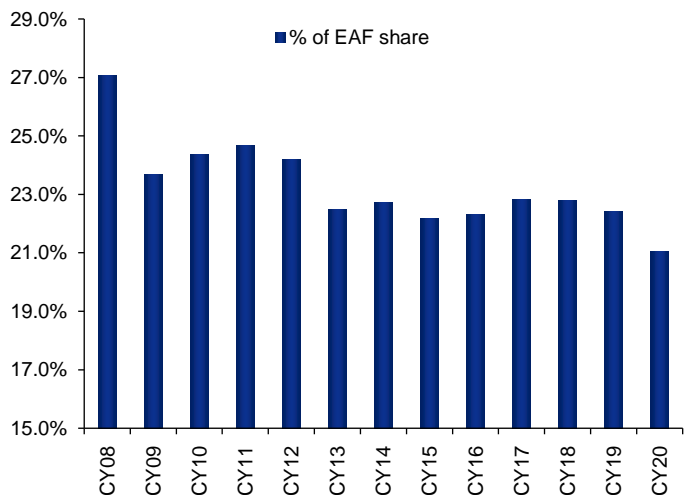
SOURCES: INCRED RESEARCH, IEA COAL REPORT

Figure 3: However, crude steel production has increased



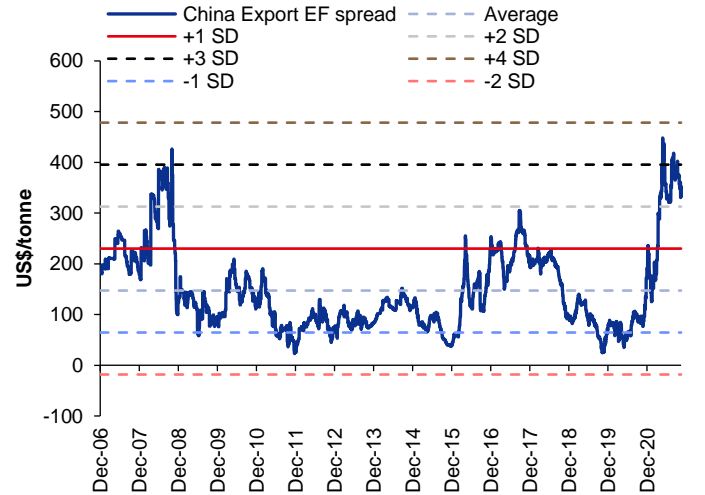
SOURCES: INCRED RESEARCH, IEA COAL REPORT

Figure 4: EAF production share has been declining



SOURCES: COMPANY REPORTS, INCRED RESEARCH

Figure 5: ...but EAF spreads over scrap are at a multi-year high



SOURCES: COMPANY REPORTS, INCRED RESEARCH

Figure 6: Scrap availability is increasing in China

STEEL SCRAP USE FOR STEELMAKING IN KEY COUNTRIES AND REGIONS (MILLION TONNES)

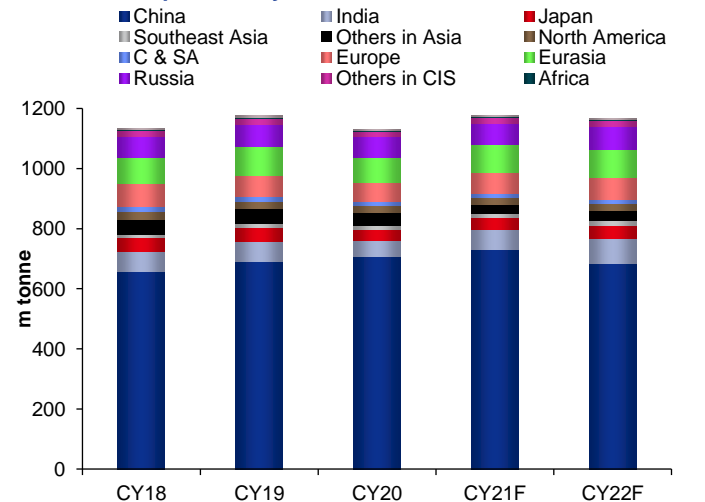
	2016	2017	2018	2019	2020	% 2020/2019
China	90.1	147.9	187.8	215.9	220.3	+2.0
EU-28	88.4	93.3	90.939	86.473	77.539	-10.3
USA	56.7	58.8	60.1	60.7	50.0	-17.6
Turkey	25.9	30.27	31.317	27.900	30.077	+7.8
Russia	27.8	29.34	31.776	30.173	29.929	-0.8
Japan	33.57	35.77	36.513	33.682	29.179	-13.4
Republic of Korea	27.4	30.67	29.956	28.601	25.831	-9.7
Canada	*	6.29	6.67	6.28	*	

*Not available at editorial deadline

Source: EUROFER, CAMJ, USGS/ISRI-calculations, Japan Ministry of Economy, RUSLOM, KOSA, TCUD, CARI

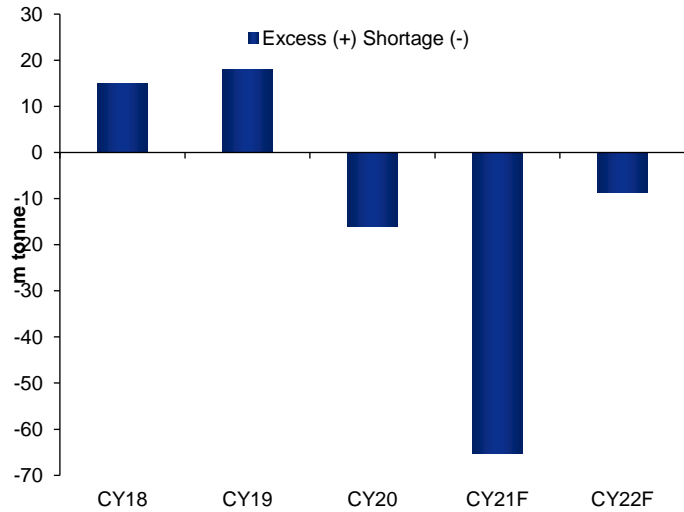
SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 7: Hence, going forward we may see a decline in coking coal demand, particularly in China



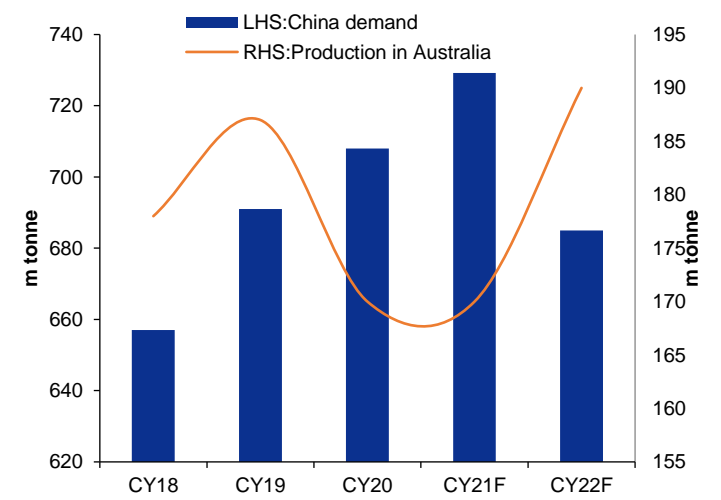
SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 8: Demand-supply gap will be still wide



SOURCES: COMPANY REPORTS, INCRED RESEARCH

Figure 9: Our hypothesis is based on a decline in China demand as well as ramp-up of production in Australia



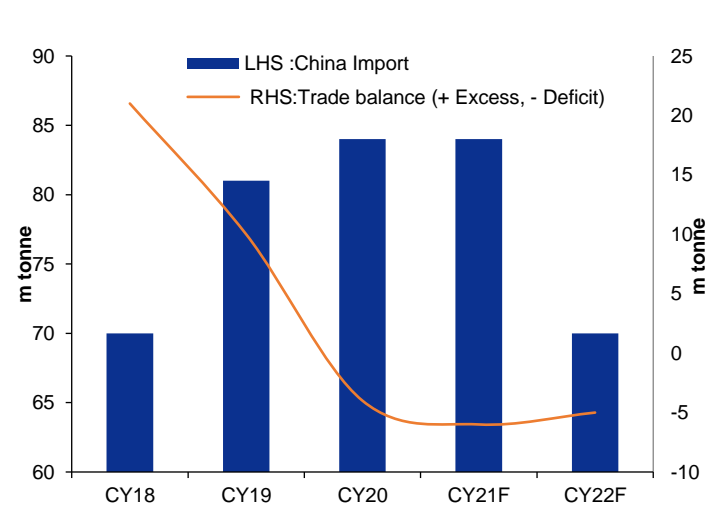
SOURCES: COMPANY REPORTS, INCRED RESEARCH

Figure 10: Delay in production ramp-up or rapid demand growth in India will keep lead to a severe coal shortage (our projection is 81mt India demand and 190mt production in Australia)

India coking coal demand	Australia coking coal production					
	165	170	175	180	185	190
67.0	-19.65	-14.65	-9.65	-4.65	0.35	5.35
71.0	-23.65	-18.65	-13.65	-8.65	-3.65	1.35
73.0	-25.65	-20.65	-15.65	-10.65	-5.65	-0.65
75.0	-27.65	-22.65	-17.65	-12.65	-7.65	-2.65
77.0	-29.65	-24.65	-19.65	-14.65	-9.65	-4.65
79.0	-31.65	-26.65	-21.65	-16.65	-11.65	-6.65
81.0	-33.65	-28.65	-23.65	-18.65	-13.65	-8.65
83.0	-35.65	-30.65	-25.65	-20.65	-15.65	-10.65
85.0	-37.65	-32.65	-27.65	-22.65	-17.65	-12.65

SOURCES: COMPANY REPORTS, INCRED RESEARCH

Figure 11: Chinese imports of coking coal are key in the overall balance; we factor in a decline in imports in our projections



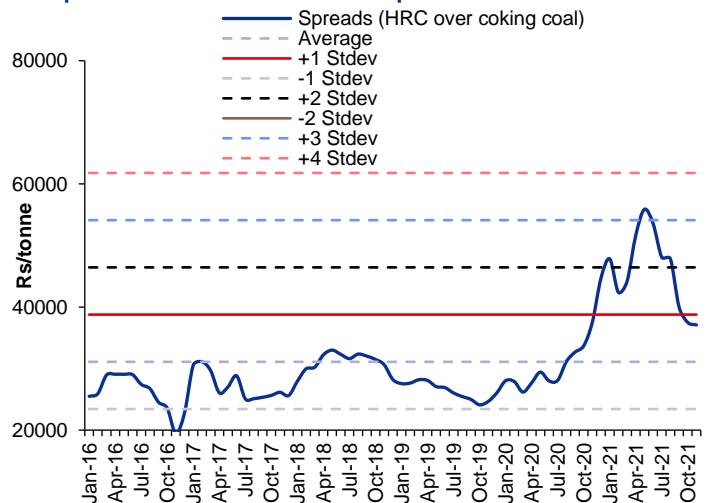
SOURCES: GOVERNMENT OF AUSTRALIA, INCRED RESEARCH

Figure 12: Unfortunately, Australia doesn't have much planned capex for coking coal in the near-term

Type	Status	Annual Estimated New Capacity	Estimated Start Commercial Operation
Expansion	Publicly announced		2022
New Project	Publicly announced	3.2	2026+
New Project	Publicly announced	0.5	2024+
New Project	Publicly announced	5	2026+
New project	Publicly announced	5	2026+
New project	Publicly announced	7	2024

SOURCES: GOVERNMENT OF AUSTRALIA WEBSITE, COMPANY REPORTS

Figure 13: Steel companies are caught between a rock and a hard place - fall in Indian demand will not only soften coking coal prices but will also lower steel prices and vice versa



SOURCES: INCRED RESEARCH, COMPANY REPORTS

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Score Range:	90 - 100	80 – 89	70 - 79	Below 70	No Survey Result
Description:	Excellent	Very Good	Good	N/A	N/A

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Corporate Governance Report of Thai Listed Companies (CGR). CG Rating by the Thai Institute of Directors Association (Thai IOD) in 2020, Anti-Corruption 2020

ADVANC – Excellent, Certified, **AMATA** – Excellent, Certified, **ANAN** – Excellent, n/a, **AOT** – Excellent, n/a, **AP** – Excellent, Certified, **ASP** – Excellent, n/a, **AU** – Good, n/a, **BAM** – Very Good, Certified, **BAY** – Excellent, Certified, **BBL** – Very Good, Certified, **BCH** – Good, Certified, **BCP** - Excellent, Certified, **BCPG** – Excellent, Certified, **BDMS** – Excellent, n/a, **BEAUTY** – Good, n/a, **BH** - Good, n/a, **BJC** – Very Good, n/a, **BLA** – Excellent, Certified, **BTS** - Excellent, Certified, **CBG** – Very Good, n/a, **CCET** – n/a, n/a, **CENTEL** – Excellent, Certified, **CHAYO** – Very Good, n/a, **CHG** – Very Good, n/a, **CK** – Excellent, n/a, **COM7** – Very Good, Certified, **CPALL** – Excellent, Certified, **CPF** – Excellent, Certified, **CPN** - Excellent, Certified, **CPNREIT** – n/a, n/a, **CRC** – Very Good, n/a, **DELTA** - Excellent, Certified, **DDD** – Very Good, n/a, **DIF** – n/a, n/a, **DOHOME** – Very Good, n/a, **DREIT** – n/a, n/a, **DTAC** – Excellent, Certified, **ECL** – Excellent, Certified, **EGCO** - Excellent, Certified, **EPG** – Excellent, Certified, **ERW** – Very Good, Certified, **GFPT** - Excellent, Certified, **GGC** – Excellent, Certified, **GLOBAL** – Very Good, n/a, **HANA** - Excellent, Certified, **HMPRO** - Excellent, Certified, **HUMAN** – Good, n/a, **ICHI** – Excellent, Certified, **III** – Excellent, n/a, **INTUCH** - Excellent, Certified, **IRPC** – Excellent, Certified, **ITD** – Very Good, n/a, **IVL** - Excellent, Certified, **JASIF** – n/a, n/a, **JKN** – Excellent, Declared, **JMT** – Very Good, Declared, **KBANK** - Excellent, Certified, **KCE** - Excellent, Certified, **KEX** – n/a, n/a, **KKP** – Excellent, Certified, **KSL** – Excellent, Certified, **KTB** - Excellent, Certified, **KTC** – Excellent, Certified, **LH** - Excellent, n/a, **LPN** – Excellent, Certified, **M** – Very Good, Certified, **MAKRO** – Excellent, Certified, **MC** – Excellent, Certified, **MEGA** – Very Good, n/a, **MINT** - Excellent, Certified, **MTC** – Excellent, Certified, **NETBAY** – Very Good, n/a, **NRF** – n/a, n/a, **OR** – n/a, n/a, **ORI** – Excellent, Certified, **OSP** – Very Good, n/a, **PLANB** – Excellent, Certified, **PRINC** – Very Good, Certified, **PR9** – Excellent, n/a, **PSH** – Excellent, Certified, **PTT** - Excellent, Certified, **PTTEP** - Excellent, Certified, **PTTGC** - Excellent, Certified, **QH** – Excellent, Certified, **RBF** – Good, n/a, **RS** – Excellent, n/a, **RSP** – Good, n/a, **S** – Excellent, n/a, **SAK** – n/a, n/a, **SAPPE** – Very Good, Certified, **SAWAD** – Very Good, n/a, **SCB** - Excellent, Certified, **SCC** – Excellent, Certified, **SCGP** – n/a, n/a, **SHR** – Very Good, n/a, **SIRI** – Excellent, Certified, **SPA** – Very Good, n/a, **SPALI** - Excellent, Declared, **SPRC** – Excellent, Certified, **SSP** - Good, Declared, **STEC** – n/a, n/a, **SVI** – Excellent, Certified, **SYNEX** – Very Good, n/a, **TCAP** – Excellent, Certified, **THANI** – Excellent, Certified, **TIDLOR** – n/a, n/a, **TISCO** - Excellent, Certified, **TKN** – Very Good, n/a, **TMB** - Excellent, Certified, **TOP** - Excellent, Certified, **TRUE** – Excellent, Certified, **TU** – Excellent, Certified, **TVO** – Excellent, Certified, **VGI** – Excellent, Certified, **WHA** – Excellent, Certified, **WHART** – n/a, n/a, **WICE** – Excellent, Certified, **WORK** – Good, n/a.

- CG Score 2020 from Thai Institute of Directors Association (IOD)

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Recommendation Framework

Stock Ratings

Definition:

Add	The stock's total return is expected to exceed 10% over the next 12 months.
Hold	The stock's total return is expected to be between 0% and positive 10% over the next 12 months.
Reduce	The stock's total return is expected to fall below 0% or more over the next 12 months.

The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

Sector Ratings

Definition:

Overweight	An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
Neutral	A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
Underweight	An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

Country Ratings

Definition:

Overweight	An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
Neutral	A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
Underweight	An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.