

India

**Underweight** (no change)

**Highlighted Companies**

**JSW Steel**

**REDUCE, TP Rs330, Rs569 close**

We value JSW Steel at +1SD or 8x FY22F E/EBITDA to arrive at a TP of Rs330. 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

**Steel Authority of India**

**REDUCE, TP Rs60, Rs85 close**

Despite having captive iron ore capacities, SAIL's operational cost/t is the highest among its peers. Its mining costs are rising, negating the advantages.

**Tata Steel**

**REDUCE, TP Rs750, Rs1074 close**

We expect the company to fare well based on its value-added offerings but see its profitability falling, leading to a 1% EBITDA CAGR over FY21-24F.

**Summary Valuation Metrics**

P/E (x)	Mar22-F	Mar23-F	Mar24-F
JSW Steel	14.67	42.45	50.53
Steel Authority of India	5.71	79.26	71.79
Tata Steel	4.46	13.28	11.7

P/BV (x)	Mar22-F	Mar23-F	Mar24-F
JSW Steel	3.05	2.94	2.88
Steel Authority of India	0.71	0.7	0.69
Tata Steel	1.29	1.21	1.12

Dividend Yield	Mar22-F	Mar23-F	Mar24-F
JSW Steel	1.14%	1.14%	1.14%
Steel Authority of India	0%	0%	0%
Tata Steel	2.33%	2.33%	2.33%

# Steel

## Multiple headwinds in the offing

- Inevitable sanctions on Russia by EU and USA can lead to spiraling coking coal prices and lifting of trade barriers on China.
- High energy cost in EU and spiraling inflation can impact demand and at the same time, a depreciating rouble can lead to pricing pressure on steel.
- Indian steel stocks are still trading at 1.6xP/BV. Given the uncertainty, projected earnings have no meaning. Tata Steel and SAIL are our top Reduce.

### Russia is new nemesis for steel stocks, keep away from value buying

There are two aspects of trade in global steel market - the first is China but the second one is much subtle and often ignored i.e. Black Sea export prices. Please note that Russian blast furnaces are totally integrated and hence, any fall in its currency will lead to windfall profits. The question is while it's sure that the West will levy sanctions on Russia, but will India, China and other countries follow suit? The answer is an emphatic no. So, material will flow from Russia to India and other countries, which will be negative for prices. China slowdown was a threat and now Russian currency slide is a further negative for Indian steel prices. Brace for a rocky ride and do not indulge in value-picking steel stocks. Keep away from these stocks. Even if they bounce by 10-15%, sell in that rally. Steel is months away from entering the buy zone. SAIL and Tata Steel are our top Reduce-rated stocks.

### On cost side, coking coal prices may rise further

Russia exports ~32mt of coking coal (Data for 2021, Source: SteelMint), and most of that goes to blast furnaces in EU. While it's likely that now EU may not import coking coal from Russia and hence, it needs to search for an alternative market. Please note that India doesn't import coking coal from Russia and hence search for alternative market by EU can result in sourcing competition for India. While Indian importers can source coking coal from Russia, the trust element, trade terms negotiations and banking-related issues will make sourcing from Russia extremely tough in the short run. While ultimately the market will balance, but in the interim, it will lead to a big chaos and coking coal prices can skyrocket. We cannot guess the peak but suffice to say that next few months are going to be tough for coking coal importers.

### Valuations are still too high

Valuations are still too high in a scenario where earnings are uncertain. 3QFY22 was bad for steel companies and 4QFY22F will be worse. Most steel companies have booked export cargo for flat steel and so don't expect prices to collapse in Mar 2022F, but 1QFY23F can be an entirely different ball game. Earnings in FY23F are totally uncertain and investors will do well to take normalized earnings based on 3QFY22 results. In this regard, valuations at 1.6xP/BV are just too high. Sell steel stocks.

**Analyst(s)**



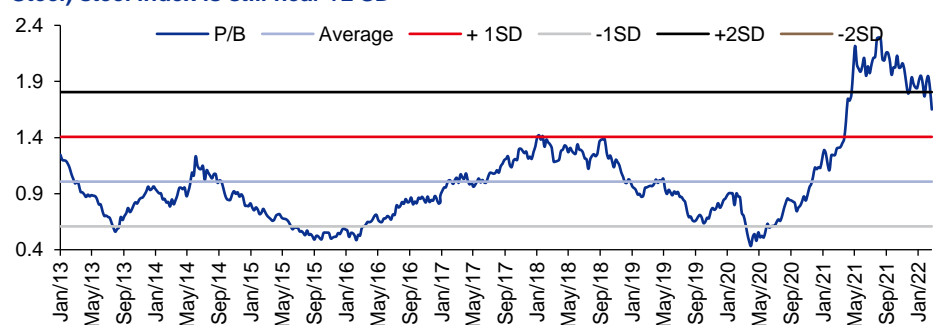
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**Figure 1: While stocks have fallen, our equally-weighted (JSW, JSPL, SAIL and Tata Steel) steel index is still near +2 SD**



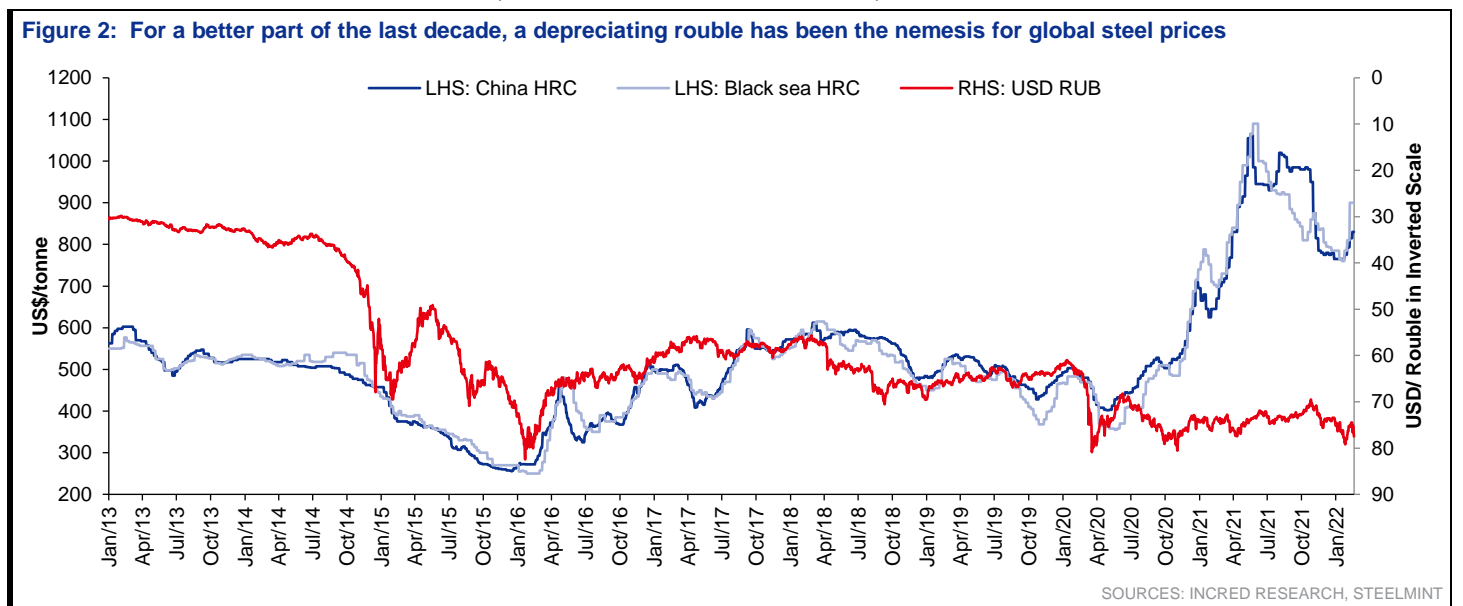
SOURCES: INCRED RESEARCH, COMPANY REPORTS

The fall is steep, but that doesn't make us positive

**Massive correction likely in steel stocks that are leveraged to price**

**Correlation between Russian currency/USD Black Sea HRC exports and China HRC prices is depicted in the graph below >**

For a better part of the last decade, a depreciating rouble has been the nemesis for global steel prices. The correlation broke during the post-Covid-19 period as supply chain uncertainty led to a shortage. We had written on this issue in our May and Jun 2021 reports: ([IN: Steel - Recent market exuberance close to its end](#)), ([IN: Steel - Irrational enthusiasm](#))



**Russian companies are self-sufficient in iron ore and coking coal and hence, a falling rouble is beneficial for them >**

It's a well-known fact that Russian companies are self-sufficient in iron ore and coking coal and hence, a fall in the rouble doesn't impact costs but makes them more competitive in export markets. Hence, a falling rouble leads to a fall in global hot-rolled coil or HRC prices.

**After China, CIS (including Russia) is a major exporter of steel >**

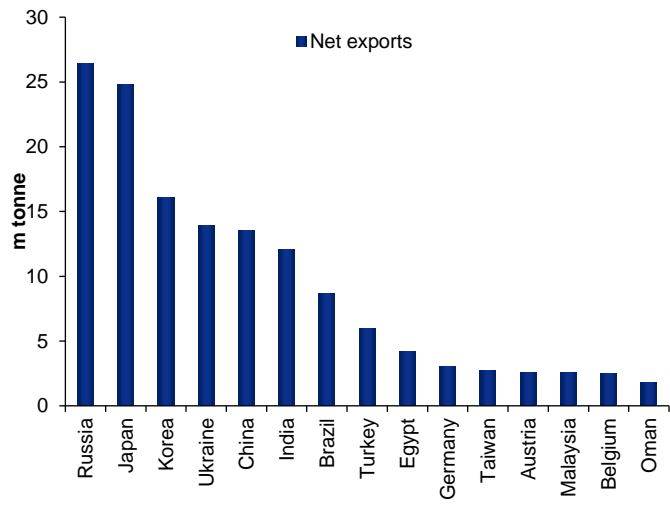
**Figure 3: The graph below denotes the exports from different regions of the world and its destination in the year 2020**

Destination	Exporting Region									
	EU	Other Europe	CIS	USMCA	Other America	MENA	China	Japan	Other Asia	Oceania
EU	95.8	8.4	12.9	0.2	0.6	1.1	2.1	0.3	6.9	0.1
Other Europe	7.8	0.8	6.1	0.0	0.7	0.1	0.9	0.6	1.1	0.0
CIS	1.0	0.5	10.3	0.0	0.0	0.0	1.6	0.0	0.4	0.0
USMCA	4.7	0.8	2.6	14.4	4.5	0.6	1.3	2.1	5.0	0.3
Other America	0.9	1.4	1.0	2.8	3.0	0.0	3.1	1.1	1.1	0.0
Africa	3.5	3.6	4.1	0.1	0.5	1.8	8.3	1.1	2.6	0.0
Middle East	1.3	4.4	3.3	0.1	0.2	5.9	5.1	1.0	4.3	0.0
China	1.4	0.2	2.6	0.4	1.5	3.0	-	5.0	23.8	0.0
Japan	0.0	0.0	0.0	0.0	0.0	0.0	0.9	-	4.2	0.0
Other Asia	1.9	1.5	7.9	0.4	0.4	2.4	27.5	18.3	-	0.3
Oceania	0.2	0.1	0.0	0.1	0.0	0.0	0.7	0.2	1.2	0.2

SOURCES: INCRED RESEARCH, WORLD STEEL ASSOCIATION

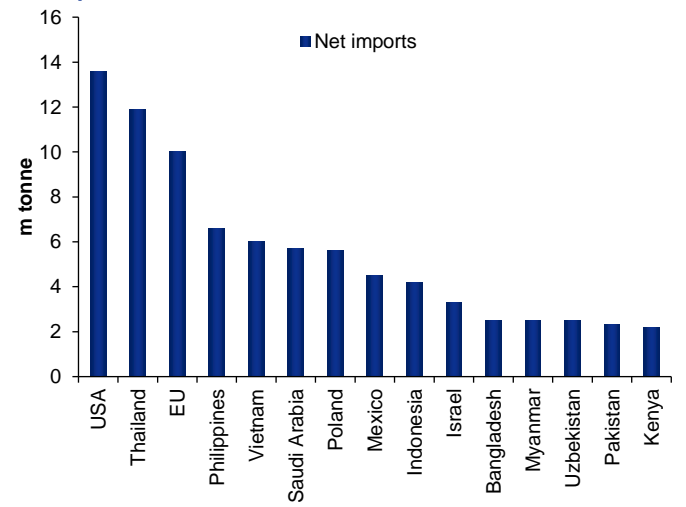
**On a standalone basis, Russia is one of the biggest exporters of steel ➤**

**Figure 4: In 2020, Russia was the biggest net exporter of steel in the world**



SOURCES: INCRED RESEARCH, STEELMINT

**Figure 5: USA and EU were the biggest importers of steel in the same period**



SOURCES: INCRED RESEARCH, STEELMINT

**Trade sanctions on Russia will lead to flow of steel to Asia ➤**

1. We are pretty sure that Asian countries, including India and China, are not going to impose any trade sanctions on Russia.
2. It is more or less certain that even if it hurts badly, EU will have to impose trade sanctions on Russia.
3. So, 26mt of steel will have to search for alternate markets and the easiest one of them is in Asia.
4. A depreciating rouble will make steel exports very attractive for Russia.

**Europe cannot fight an inflationary trade war with Russia as well as China and therefore, expect trade sanctions on China to go away ➤**

EU and USA have imposed significant tariff barriers on Chinese steel. The problem is that it's leading to a rise in domestic steel prices. Removing anti-dumping duty will provide some respite to EU.

**European steel demand is at risk and so does its prices ➤**

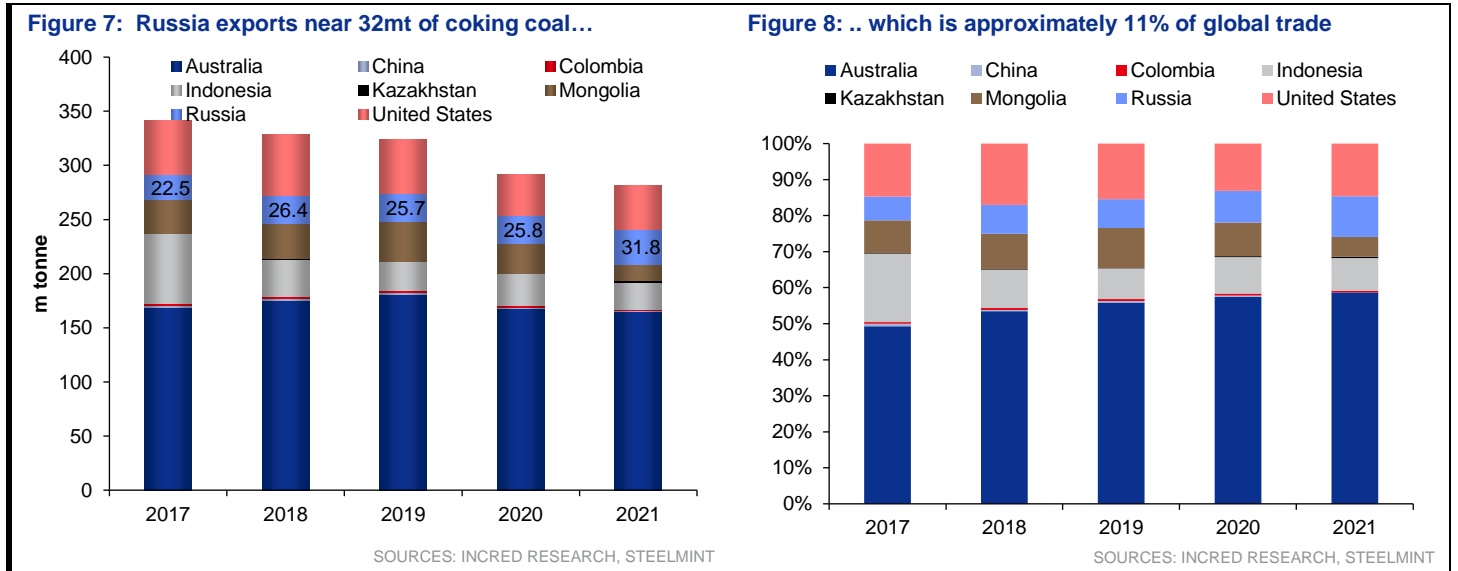
**Figure 6: Energy prices on the rampage will impact EU's economy and thus, expect a decline in steel demand**



SOURCES: INCRED RESEARCH, [HTTPS://TRADINGECONOMICS.COM/COMMODITY/EU-NATURAL-GAS](https://tradingeconomics.com/commodity/eu-natural-gas)

**Lack of investment in mining assets keeps coking coal prices high and sanctions on Russia will exacerbate the problem ➤**

Russia will be sanctioned by EU and USA. Please remember that India doesn't import coking coal from Russia and it's EU which runs blast furnaces from Russian coal. While ultimately the market balances, but in the interim period it will be very painful for Indian companies. Costs will skyrocket and there will be significant impact on end-product demand as well.



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<b>Score Range:</b>	90 - 100	80 – 89	70 - 79	Below 70	No Survey Result
<b>Description:</b>	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 2021, Anti-Corruption 2021**

**ADVANC** – Excellent, Certified, **AMATA** – Excellent, Certified, **ANAN** – Excellent, n/a, **AOT** – Excellent, n/a, **AP** – Excellent, Certified, **ASP** – Excellent, n/a, **AWC** – Excellent, Declared, **AU** – Good, n/a, **BAM** – Very Good, Certified, **BAY** – Excellent, Certified, **BBL** – Excellent, Certified, **BCH** – Very Good, Certified, **BCP** - Excellent, Certified, **BCPG** – Excellent, Certified, **BDMS** – Excellent, n/a, **BEAUTY** – Good, n/a, **BEM** – Excellent, n/a **BH** - Good, n/a, **BJC** – Very Good, n/a, **BLA** – Very Good, Certified, **BTS** - Excellent, Certified, **CBG** – Very Good, n/a, **CGET** – n/a, n/a, **CENDEL** – Excellent, Certified, **CHAYO** – Very Good, n/a, **CHG** – Very Good, n/a, **CK** – Excellent, n/a, **COM7** – Excellent, Certified, **CPALL** – Excellent, Certified, **CPF** – Excellent, Certified, **CPN** - Excellent, Certified, **CPNREIT** – n/a, n/a, **CRC** – Excellent, Declared, **DELTA** - Excellent, Certified, **DDD** – Excellent, n/a, **DIF** – n/a, n/a, **DOHOME** – Very Good, Declared, **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** – Excellent, n/a, **HANA** - Excellent, Certified, **HMPRO** - Excellent, Certified, **HUMAN** – Good, n/a, **ICHI** – Excellent, Certified, **III** – Excellent, Declared, **INTUCH** - Excellent, Certified, **IRPC** – Excellent, Certified, **ITD** – Very Good, n/a, **IVL** - Excellent, Certified, **JASIF** – n/a, n/a, **JKN** – n/a, Certified, **JMT** – Very Good, n/a, **KBANK** - Excellent, Certified, **KCE** - Excellent, Certified, **KEX** – Very Good, Declared, **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** – Very Good, Declared, **OR** – Excellent, n/a, **ORI** – Excellent, Certified, **OSP** – Excellent, n/a, **PLANB** – Excellent, Certified, **PRINC** – Very Good, Certified, **PR9** – Excellent, Declared, **PSH** – Excellent, Certified, **PTT** - Excellent, Certified, **PTTEP** - Excellent, n/a, **PTTGC** - Excellent, Certified, **QH** – Excellent, Certified, **RAM** – n/a, n/a, **RBF** – Very Good, n/a, **RS** – Excellent, Declared, **RSP** – Good, n/a, **S** – Excellent, n/a, **SAK** – Very Good, Declared, **SAPPE** – Very Good, Certified, **SAWAD** – Very Good, n/a, **SCB** - Excellent, Certified, **SCC** – Excellent, Certified, **SCGP** – Excellent, Declared, **SECURE** – n/a, n/a, **SHR** – Excellent, n/a, **SIRI** – Excellent, Certified, **SPA** – Very Good, n/a, **SPALI** - Excellent, Certified, **SPRC** – Excellent, Certified, **SSP** - Good, Certified, **STEC** – Excellent, n/a, **SVI** – Excellent, Certified, **SYNEX** – Very Good, Certified, **TCAP** – Excellent, Certified, **THANI** – Excellent, Certified, **TIDLOR** – n/a, Certified **TISCO** - Excellent, Certified, **TKN** – Very Good, n/a, **TOP** - Excellent, Certified, **TRUE** – Excellent, Certified, **TTB** - 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 2021 from Thai Institute of Directors Association (IOD)

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**Recommendation Framework**

**Stock Ratings**

Definition:

<b>Add</b>	The stock's total return is expected to exceed 10% over the next 12 months.
<b>Hold</b>	The stock's total return is expected to be between 0% and positive 10% over the next 12 months.
<b>Reduce</b>	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:

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

**Country Ratings**

Definition:

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