FIRST LIGHT

12 July 2022

RESEARCH

Metals & Mining | Q1FY23 Preview

Buffeted by headwinds

Daily macro indicators

Indicator	07-Jul	08-Jul	Chg (%)
US 10Y yield (%)	2.99	3.08	9bps
India 10Y yield (%)	7.35	7.42	6bps
USD/INR	79.18	79.25	(0.1)
Brent Crude (US$/bbl)	104.7	107	2.3
Dow	31,385	31,338	(0.1)
Hang Seng	21,644	21,726	0.4
Sensex	54,178	54,482	0.6
India FII (US$ mn)	**06-Jul**	**07-Jul**	**Chg ($ mn)**
FII-D	116.6	(2.8)	(119.4)
FII-E	(100.3)	(111.6)	(11.3)

Source: Bank of Baroda Economics Research

SUMMARY

Metals & Mining: Q1FY23 Preview

- Metals players likely to post sharp EBITDA decline QoQ in Q1 amid double whammy of margin and volume contraction
- Management commentary on possible bottoming out of steel margins in Q2 a key monitorable
- Retain constructive view on sector as we expect margins to stabilise at a healthy mid-cycle level once current volatility abates

Click here for the full report.

BOBCAPS Research
research@bobcaps.in

BOBCAPS
TRUST | INNOVATION | EXCELLENCE

METALS & MINING | Q1FY23 Preview | 11 July 2022

Buffeted by headwinds

- **Metals players likely to post sharp EBITDA decline QoQ in Q1 amid double whammy of margin and volume contraction**
- **Management commentary on possible bottoming out of steel margins in Q2 a key monitorable**
- **Retain constructive view on sector as we expect margins to stabilise at a healthy mid-cycle level once current volatility abates**

Kirtan Mehta, CFA
research@bobcaps.in

Q1 faces double whammy of margin and volume decline: We expect a sharp 47% QoQ drop in aggregate EBITDA for Indian operations of the four domestic steel majors as both margins and volumes contract. The decline is likely to be lower at the consolidated level, at 35% QoQ, as TATA's European operations benefit from contractual prices and JSP's coal subsidiaries benefit from higher coal prices.

Margins below company guidance: We expect the decline in steel margins to be sharper than company guidance during Q4 calls due to weaker-than expected realisations. Coking coal cost increases are likely to be in line with company guidance of a US$ 100-150/t QoQ increase in cost base. On an aggregate basis for Indian operations, we expect EBITDA/t to fall by Rs 5.1k/t QoQ to Rs 10.4k/t. JSTL and SAIL look headed for a steeper margin drop-off this quarter.

Sales to plummet as well: While we expect resilient steel production in Q1, we anticipate a sharp 21% QoQ decline in sale volumes given weaker demand in the second half of the quarter as users wait in the wings amid a 20%+ QoQ fall in prices from the peak. Our channel checks show initial signs of domestic demand stabilising, but we expect muted offtake during the monsoon months. We also foresee a slowdown in export orders in Q2 as contracts executed prior to the levy of export duties wind down.

Key monitorables: We await management commentary on the possibility of a bottoming out of steel margins in Q2. In domestic markets, signs of demand stabilisation, outlook on export levels during the downturn, and commentary on production cuts/advancing of maintenance shutdowns will be important aspects to monitor. On the raw material front, the quantum of pullback in global coking coal prices and stabilisation levels for domestic iron ore/pellet prices are key.

Constructive outlook on sector: While we acknowledge a higher level of volatility amid uncertainty, we believe steel margins will stabilise at mid-cycle levels over the next year with the restoration of market balance and deflation in the raw materials chain. Steadying of demand in China will be a key trigger for the sector.

Recommendation snapshot

Ticker	Price	Target	Rating
JSP IN	351	555	BUY
JSTL IN	577	810	BUY
SAIL IN	73	150	HOLD
TATA IN	913	1,700	BUY

Price & Target in Rupees | Price as of 11 Jul 2022

Disclaimer

Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

Rating distribution

As of 30 June 2022, out of 118 rated stocks in the BOB Capital Markets Limited (BOBCAPS) coverage universe, 73 have BUY ratings, 23 have HOLD ratings, 5 are rated ADD*, 1 is rated REDUCE* and 16 are rated SELL. Of these, 2 companies rated BUY and 1 rated ADD have been investment banking clients in the last 12 months. (*Our ADD and REDUCE ratings are in the process of being migrated to the new recommendation structure.)

Analyst certification

Each of the analysts mentioned in this research report certify, with respect to the sections of the report for which they are responsible, that (1) all of the views expressed in this report accurately reflect his/her personal views about the subject company or companies and its or their securities, and (2) no part of his/her compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) in this report. Analysts are not registered as research analysts by FINRA and are not associated persons of BOBCAPS.

Important disclosures

This product is a compilation of previously published research notes. To view the complete report along with the associated Analyst certifications and Company-specific disclosures, please click on the hyperlink accompanying each excerpt.

General disclaimers

BOBCAPS is engaged in the business of Stock Broking and Investment Banking. BOBCAPS is a member of the National Stock Exchange of India Limited and BSE Limited and is also a SEBI-registered Category I Merchant Banker. BOBCAPS is a wholly owned subsidiary of Bank of Baroda which has its various subsidiaries engaged in the businesses of stock broking, lending, asset management, life insurance, health insurance and wealth management, among others.

BOBCAPS's activities have neither been suspended nor has it defaulted with any stock exchange authority with whom it has been registered in the last five years. BOBCAPS has not been debarred from doing business by any stock exchange or SEBI or any other authority. No disciplinary action has been taken by any regulatory authority against BOBCAPS affecting its equity research analysis activities.

BOBCAPS has obtained registration as a Research Entity under SEBI (Research Analysts) Regulations, 2014, having registration No.: INH000000040 valid till 03 February 2025. BOBCAPS is also a SEBI-registered intermediary for the broking business having SEBI Single Registration Certificate No.: INZ000159332 dated 20 November 2017. BOBCAPS CIN Number: U65999MH1996GOI098009.

BOBCAPS prohibits its analysts, persons reporting to analysts, and members of their households from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover. Additionally, BOBCAPS prohibits its analysts and persons reporting to analysts from serving as an officer, director, or advisory board member of any companies that the analysts cover.

Our salespeople, traders, and other professionals may provide oral or written market commentary or trading strategies to our clients that reflect opinions contrary to the opinions expressed herein, and our proprietary trading and investing businesses may make investment decisions that are inconsistent with the recommendations expressed herein. In reviewing these materials, you should be aware that any or all of the foregoing, among other things, may give rise to real or potential conflicts of interest. Additionally, other important information regarding our relationships with the company or companies that are the subject of this material is provided herein.

This material should not be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. We are not soliciting any action based on this material. It is for the general information of BOBCAPS's clients. It does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients. Before acting on any advice or recommendation in this material, clients should consider whether it is suitable for their particular circumstances and, if necessary, seek professional advice.

The price and value of the investments referred to in this material and the income from them may go down as well as up, and investors may realize losses on any investments. Past performance is not a guide for future performance, future returns are not guaranteed and a loss of original capital may occur. BOBCAPS does not provide tax advice to its clients, and all investors are strongly advised to consult with their tax advisers regarding any potential investment in certain transactions — including those involving futures, options, and other derivatives as well as non-investment-grade securities —that give rise to substantial risk and are not suitable for all investors. The material is based on information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied on as such. Opinions expressed are our current opinions as of the date appearing on this material only. We endeavour to update on a reasonable basis the information discussed in this material, but regulatory, compliance, or other reasons may prevent us from doing so.

We and our affiliates, officers, directors, and employees, including persons involved in the preparation or issuance of this material, may from time to time have "long" or "short" positions in, act as principal in, and buy or sell the securities or derivatives thereof of companies mentioned herein and may from time to time add to or dispose of any such securities (or investment). We and our affiliates may act as market makers or assume an underwriting commitment in the securities of companies discussed in this document (or in related investments), may sell them to or buy them from customers on a principal basis, and may also perform or seek to perform investment banking or advisory services for or relating to these companies and may also be represented in the supervisory board or any other committee of these companies.

For the purpose of calculating whether BOBCAPS and its affiliates hold, beneficially own, or control, including the right to vote for directors, one per cent or more of the equity shares of the subject company, the holdings of the issuer of the research report is also included.

BOBCAPS and its non-US affiliates may, to the extent permissible under applicable laws, have acted on or used this research to the extent that it relates to non-US issuers, prior to or immediately following its publication. Foreign currency denominated securities are subject to fluctuations in exchange rates that could have an adverse effect on the value or price of or income derived from the investment. In addition, investors in securities such as ADRs, the value of which are influenced by foreign currencies, effectively assume currency risk. In addition, options involve risks and are not suitable for all investors. Please ensure that you have read and understood the Risk disclosure document before entering into any derivative transactions.

In the US, this material is only for Qualified Institutional Buyers as defined under rule 144(a) of the Securities Act, 1933. No part of this document may be distributed in Canada or used by private customers in the United Kingdom.

No part of this material may be (1) copied, photocopied, or duplicated in any form by any means or (2) redistributed without BOBCAPS's prior written consent.

Other disclosures

BOBCAPS does not have any financial interest in the subject company. BOBCAPS does not have actual/beneficial ownership of one per cent or more securities in the subject company at the end of the month immediately preceding the date of publication of this report.

BOBCAPS is not engaged in any market making activities for the subject company.

BOBCAPS or its associates may have material conflict of interest at the time of publication of this research report.

BOBCAPS's associates may have financial interest in the subject company. BOBCAPS's associates may hold actual / beneficial ownership of one per cent or more securities in the subject company at the end of the month immediately preceding the date of publication of this report.

BOBCAPS or its associates may have managed or co-managed a public offering of securities for the subject company or may have been mandated by the subject company for any other assignment in the past 12 months.

BOBCAPS may have received compensation from the subject company in the past 12 months. BOBCAPS may from time to time solicit or perform investment banking services for the subject company. BOBCAPS or its associates may have received compensation from the subject company in the past 12 months for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory services in a merger or specific transaction. BOBCAPS or its associates may have received compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past 12 months.