FIRST LIGHT

06 September 2022

RESEARCH

BOB Economics Research | Financial Soundness

Comparative study on global financial soundness indicators

Metals & Mining

China's Q2 steel results signal slower demand recovery

Daily macro indicators

Indicator	01-Sep	02-Sep	Chg (%)
US 10Y yield (%)	3.25	3.19	(6bps)
India 10Y yield (%)	7.22	7.23	2bps
USD/INR	79.56	79.80	(0.3)
Brent Crude (US$/bbl)	92.4	93	0.7
Dow	31,656	31,318	(1.1)
Hang Seng	19,597	19,452	(0.7)
Sensex	58,767	58,803	0.1
India FII (US$ mn)	**29-Aug**	**30-Aug**	**Chg ($ mn)**
FII-D	(85.4)	(1.1)	84.3
FII-E	257.7	534.3	276.6

Source: Bank of Baroda Economics Research

SUMMARY

India Economics: Financial Soundness

The study is based on IMF's Financial Soundness Indicators database. Aim of the study is to see India's position amongst its global peers in terms of the health of the financial system. Key takeaways: India's regulatory capital-RWA ratio at 15.3% is relatively low when compared to countries like UK, Indonesia, Netherlands. India's NPA ratio is on the higher end of the scale in global comparison. Amongst the set of countries, India has relatively better provisioning to NPA ratio. Returns on Assets in India are similar to that of Australia and Canada and slightly lower than the US. Returns on Equity in India is also similar to that of Spain. India's reliance on interest income is higher than most countries, like France, UK, Malaysia. Non-interest expense to gross income ratio for India is on the lower side in global comparison.

Click here **for the full report.**

Metals & Mining

- China's Q2CY22 steel sector performance flags subpar demand in Q3 and only a gradual recovery from Q4
- Auto and infrastructure seeing signs of revival, but industry must align steel production with softer demand amid protracted real estate slump
- We expect margins to gradually stabilise over H2FY23; prefer defensive play TATA amid volatile environment

Click here **for the full report.**

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FINANCIAL SOUNDNESS

05 September 2022

Comparative study on global financial soundness indicators

Sonal Badhan
Economist

The study is based on IMF's Financial Soundness Indicators database. Aim of the study is to see India's position amongst its global peers in terms of the health of the financial system. Key takeaways: India's regulatory capital-RWA ratio at 15.3% is relatively low when compared to countries like UK, Indonesia, Netherlands. India's NPA ratio is on the higher end of the scale in global comparison. Amongst the set of countries, India has relatively better provisioning to NPA ratio. Returns on Assets in India are similar to that of Australia and Canada and slightly lower than the US. Returns on Equity in India is also similar to that of Spain. India's reliance on interest income is higher than most countries, like France, UK, Malaysia. Non-interest expense to gross income ratio for India is on the lower side in global comparison.

Note: Data used is the latest available for the chosen countries. For most countries data pertains to Mar'22 or Dec'21. For some, it is also as of Mar'21.

- India's regulatory capital-RWA ratio at 15.3% is relatively low when compared to countries like UK, Indonesia, Netherlands.
  - It is on par with ratios of Greece and China. US maintains slightly higher ratio than India.
- India's NPA ratio is on the higher end of the scale in global comparison.
  - Amongst major economies, only Russia and Greece have ratios higher than India.
  - Korea, Canada, US, UK have some of the lowest NPA ratios.
- Amongst the set of countries, India has relatively better provisioning to NPA ratio.
  - However, it is still lower than Brazil, China, Mexico, Argentina.
  - UK provisions to NPA ratio is the lowest.
- Returns on Assets in India are similar to that of Australia and Canada and slightly lower than the US.
  - Countries like China, Italy, France and UK have the lowest RoAs.
- Returns on Equity in India is also similar to that of Spain.
  - It is lower than countries like, Russia, Indonesia, Australia, US.
  - However it is higher than Spain, Korea, UK, China.
- India's reliance on interest income is higher than most countries, like France, UK, Malaysia.
  - This signifies greater dependence on loan book and less on fee income.
  - Countries like US, Korea, China Greece, have even higher dependence.
- Non-interest expense to gross income ratio for India is on the lower side in global comparison.
  - Levels are similar to/better than US, UK, France, Italy, Turkey.
  - China, Malaysia, Indonesia, Korea, Australia have ratios less than India.

METALS & MINING

05 September 2022

China's Q2 steel results signal slower demand recovery

- **China's Q2CY22 steel sector performance flags subpar demand in Q3 and only a gradual recovery from Q4**
- **Auto and infrastructure seeing signs of revival, but industry must align steel production with softer demand amid protracted real estate slump**
- **We expect margins to gradually stabilise over H2FY23; prefer defensive play TATA amid volatile environment**

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Q2CY22 results flag demand weakness: China's steel sector performance in Q2CY22 highlights a challenging environment through H2CY22 given weaker domestic demand and declining profitability. With high-cost inventory, Chinese steel margins are likely to be under pressure in Q3CY22. The industry has shifted its focus toward improving operational efficiency, curtailing production and cutting costs to work through the downturn.

Gradual demand recovery from Q4: Management commentary suggests the easing of Covid-led restrictions and revival in infrastructure demand as stimulus feeds through the economy could aid demand recovery by the year-end. While Baosteel expects real estate demand to remain anaemic, it highlights strong demand from the transformer segment, recovery underway in auto and a gradual rise in infrastructure offtake over H2CY22. We believe these segments have the potential to partly offset the weakness in real estate and arrest the decline in Chinese steel demand to lower single digits.

Supply cuts key to rebalancing Chinese industry: With real estate demand failing to gain traction, it is imperative that the Chinese steel industry align production with underlying demand. Baosteel and some other players are looking to shutter less profitable operations. However, the Chinese industry has recently increased steel production amid a seasonal pickup in demand coming through from September. We believe rebalancing in China is important for the stabilisation of regional margins.

Read-across for Indian steel players: With Chinese demand likely to make a gradual recovery from Q4CY22, we believe steel prices will also see only a marginal recovery. Raw material prices have already corrected sharply. We expect steel margins to stabilise over H2FY23 as rebalancing in China reduces export pressure on regional markets.

Prefer defensive play TATA: Amongst our steel coverage, we prefer TATA (BUY, TP Rs 140) for its ability to generate sector-leading margins via better integration all the way to iron ore and its focus on downstream and retail to capture value-add. We also have a BUY on JSP (TP Rs 460) which has scope for a gradual rerating as the company demonstrates capital discipline and delivers on the next wave of growth.

Recommendation snapshot

Ticker	Price	Target	Rating
JSP IN	418	460	BUY
JSTL IN	661	655	HOLD
SAIL IN	79	90	HOLD
TATA IN	106	140	BUY

Price & Target in Rupees | Price as of 2 Sep 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.

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