FIRST LIGHT

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RESEARCH

Metals & Mining: Ferrous Chartbook

Margins to gradually stabilise at healthy cycle average

SUMMARY

Metals & Mining: Ferrous Chartbook

- While demand deceleration in China has resulted in price correction, we expect sharper production cuts to constrain exports
- Global steel margins likely to stabilise as China demand gradually steadies and coking coal sees reversal to mean price over 6-9 months
- Indian steel margins to gradually revert to mean in medium term; we prefer TATA and JSP

Click here for the full report.

Daily macro indicators

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	1.62	8bps	(1bps)	77bps
India 10Y yield (%)	6.35	1bps	(1bps)	45bps
USD/INR	74.40	(0.2)	0.7	(0.4)
Brent Crude (US$/bbl)	79.70	1.0	(6.8)	73.0
Dow	35,619	0.0	(0.2)	20.4
Shanghai	3,582	0.6	0.0	4.9
Sensex	58,466	(2.0)	(3.9)	32.6
India FII (US$ mn)	**18-Nov**	**MTD**	**CYTD**	**FYTD**
FII-D	150.9	481.2	410.9	2,438.1
FII-E	316.2	2,937.2	9,195.8	1,869.5

Source: Bloomberg

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China exports likely to remain in check with large production cuts: The sharp demand deceleration in China driven by property weakness and energy shortage has continued into October. However, China's production cuts have been even sharper and are extending into November. Winter restrictions further extend curtailments into Q1CY22 with at least a 30% YoY cut for ~40% of production in China over 1 Jan to 15 Mar 2022. While an intermittent rise is possible, we believe the cuts will keep exports in check. A seasonal recovery in Q2CY22 coupled with stabilising real estate demand could support the market thereafter.

Healthy demand outside China continues to provide support: Construction demand in developed markets has been offsetting the weakness in automobiles. On the lines of the WSA forecast in Oct'21, AMNS also expects ex-China demand to hold up and retained its CY21 forecast of 12-13% YoY growth.

Coking coal shows initial signs of correction: While Australia coking coal prices have dropped to US$ 364/t (from US$ 400), China prices have eased to US$ 440 (from US$ 540), as per SteelMint. This is led by steep contraction in Chinese demand and better supply post plant maintenance. Though the upcoming wet season in Australia poses a near-term risk, we expect prices to revert to mean over 6-12 months. Increased exports from Mongolia and production in China will be key drivers.

Indian steel margins to normalise over medium term: Steel margins have started softening, with the latest guidance from Tata Steel (TATA) implying a Rs 4-5k/t decline from its Q2FY22 EBITDA margin of Rs 30.7k/t for standalone operations. We believe steel margins will soften over the next 6-12 months as prices ease to an estimated US$ 650/t by FY23.

Prefer TATA, JSP: With the steel cycle peaking out, we prioritise capital discipline over expansion projects. Accordingly, we are positive on TATA and Jindal Steel & Power (JSP) who are now focusing on responsible growth (see **Disciplined capital allocation key to improving payout, 16Aug21**).

Recommendation snapshot

Ticker	Price	Target	Rating
JSP IN	381	555	BUY
JSTL IN	683	795	HOLD
SAIL IN	111	150	HOLD
TATA IN	1,190	1,755	BUY

Price & Target in Rupees | Price as of 23 Nov 2021

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

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