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Q3FY21 result review
and earnings revision

Metals

Target price: Rs292

Earnings revision

(%)	FY21E	FY22E	FY23E
Sales	↑ 4.2	↓ 5.1	↓ 3.3
EBITDA	↑ 26.6	↑ 26.0	↓ 7.1
EPS	↑ 45.3	↑ 58.3	↓ 5.8

Target price revision

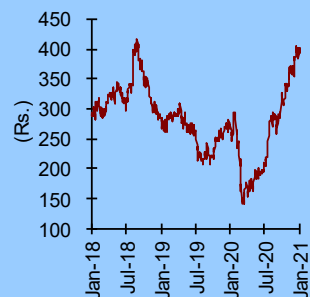
Rs292 from Rs265

Shareholding pattern

	Jun '20	Sep '20	Dec '20
Promoters	43.1	44.1	44.1
Institutional investors	20.3	19.2	19.6
MFs and others	2.3	2.4	2.3
Banks & FIs	2.6	3.4	4.0
FII	15.4	13.4	13.3
Others	35.6	36.7	36.3

Source: www.nseindia.com

Price chart



INDIA

JSW Steel

SELL

Maintained

Rs375

Peak margins expected in Q4FY21

JSW Steel (JSWS) reported higher than expected standalone EBITDA at ~ Rs 14,444/te, up ~ Rs 4,300/te QoQ. Higher auto sales (up 33% QoQ) and lower exports (down 60% QoQ) helped margins. The realisation increase is higher at Rs 8,600/te QoQ, given ~Rs5bn of iron ore sales, which given the duties and royalties fail to garner any EBITDA. JSWS has witnessed Rs 11bn of deleveraging in Q3FY21, despite Rs 15.5bn acquisition of Asian colour coated. Bhushan power acquisition, if completed may not allow deleveraging in Q4FY21. Iron ore integration has reached 49% post Odisha mines ramping up, as Dolvi looks to integrated commissioning in Q1FY22. JSWS trades at 1.5x FY23E P/B. Risk reward is not conducive. We maintain SELL at revised target price of Rs 292/share (from Rs 265/share earlier).

- ▶ **Q4FY21 EBITDA/te expected at cyclical peak.** With Q4FY21 margins expected at Rs 19100/te (Expected increase of Rs 5000/te QoQ), we are perhaps looking at peak margins for JSWS in this cycle. In a deep cyclical sector, one needs to anticipate the downward trajectory of EBITDA/te as and when such peak is visible. Deleveraging can happen, but experience suggests, with visibility of higher EBITDA/te, capex also gets rebased quickly.
- ▶ **Overseas subsidiaries continue to incur EBITDA losses.** (Adjusted) EBITDA losses for Q3FY21 stood at Rs830bn against Rs2.3bn (loss) QoQ. Adjusted for the provision in, overseas EBITDA loss was restricted to Rs520mn (reported). This has been a drag on consolidated (reported) EBITDA.
- ▶ **Projects update – Integrated Dolvi operations expected to start from Q1FY21 now; delayed by a quarter.** The expansion project at Dolvi from 5 to 10mtpa is nearing completion, with majority of operations to be commissioned in Q4FY21. Full integrated operations and stabilization will take place in Q1FY22. In the CRM-1 complex in Vijaynagar, one out of two continuous Galvanising Lines (CGL) has been commissioned, and the second will be commissioned by Q1FY22. The 8mtpa pellet plant is under commissioning. In Vasind and Tarapur, all expansions except 0.45 mtpa CGL at Vasind are under commissioning, and will be fully commissioned by Mar, '21. The 0.45mtpa CGL is to be commissioned in Q1FY22.
- ▶ **Maintain SELL.** ~15% price increase in Dec, '20 underlines the cyclicity of the sector and at current prices; the entire set of steel producers is making EBITDA/te unseen in the past 20 years. Capex announcements are slowly resurfacing, and given the compressed cycle duration, it doesn't look like sectoral leverage may permanently trend down. We retain our cautious stance on the sector, and maintain SELL rating on JSWS. We continue to value JSWS at 1.2x FY23E P/B. The bulge in FY21/22E earnings reflects the sharp rise in recent steel prices.

Market Cap	Rs907bn/US\$12.4bn
Reuters/Bloomberg	JSTL.BO/JSTL IN
Shares Outstanding (mn)	2,417.2
52-week Range (Rs)	405/141
Free Float (%)	55.9
FII (%)	13.3
Daily Volume (US\$'000)	36,515
Absolute Return 3m (%)	15.3
Absolute Return 12m (%)	42.7
Sensex Return 3m (%)	20.7
Sensex Return 12m (%)	20.4

Year to March	FY20	FY21	FY22E	FY23E
Revenue (Rs mn)	733,260	814,379	922,565	945,203
Net Income (Rs mn)	49,040	79,800	87,988	54,535
EPS (Rs)	20.3	33.0	36.4	22.6
% Chg YoY	(34.8)	62.7	10.3	(38.0)
P/E (x)	18.2	11.2	10.2	16.4
CEPS (Rs)	37.9	51.7	59.5	47.3
EV/E (x)	12.4	7.3	6.4	7.9
Dividend Yield (%)	0.5	0.0	0.0	0.0
RoCE (%)	7.6	13.9	14.3	9.3
RoE (%)	13.7	19.7	18.0	9.7

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Table 1: JSWS's standalone Q3FY21 result review

Standalone	Q3FY21	Q3FY20	% Chg YoY	Q2FY21	% Chg QoQ
Net Sales	192,390	155,170	24.0	167,970	14.5
Raw Material Consumed	75,850	77,170	(1.7)	71,200	6.5
Stock Adjustment	(12,130)	9,430		9,760	
Employee Expenses	3,930	3,740	5.1	3,630	8.3
Power, Oil & Fuel	12,900	13,070	(1.3)	12,310	4.8
Other Expenses	24,870	27,590	(9.9)	22,580	10.1
Total Expenditure	136,060	131,000	3.9	126,210	7.8
EBITDA	56,330	24,170	133.1	41,760	34.9
Margin %	29.3	15.6		24.9	
Other Income	1,690	1,350	25.2	1,510	11.9
Miscellaneous Income (Exp)	-	-		-	
Interest	8,790	9,880	(11.0)	8,850	(0.7)
EBIT	49,230	15,640		34,420	43.0
Depreciation	9,790	8,930	9.6	9,240	6.0
Extra-ordinary Items	-	(2,500)		-	
PBT (reported)	39,440	9,210	328.2	25,180	56.6
PBT (recurring)	39,440	2,050	1,823.9	25,180	
Tax (reported)	6,420	160		4,380	
Tax (recurring)	-	513		-	
Reported PAT	28,290	6,910	309.4	16,920	67.2
Adjusted PAT	39,440	1,538	2,465.2	16,920	133.1
Sales volume (mnste)	3.90	4.03	(3.2)	4.12	(5.3)
Raw Material cost (Rs/te)	16,338	21,489	(24.0)	19,650	(16.9)
Power cost (Rs/te)	3,162	3,251	(2.8)	3,197	(1.1)
Blended Cost (Rs/te)	34,887	32,506	7.3	30,633	13.9
EBITDA/te (US\$) (Adjusted)	186	73	154.6	126	47.4

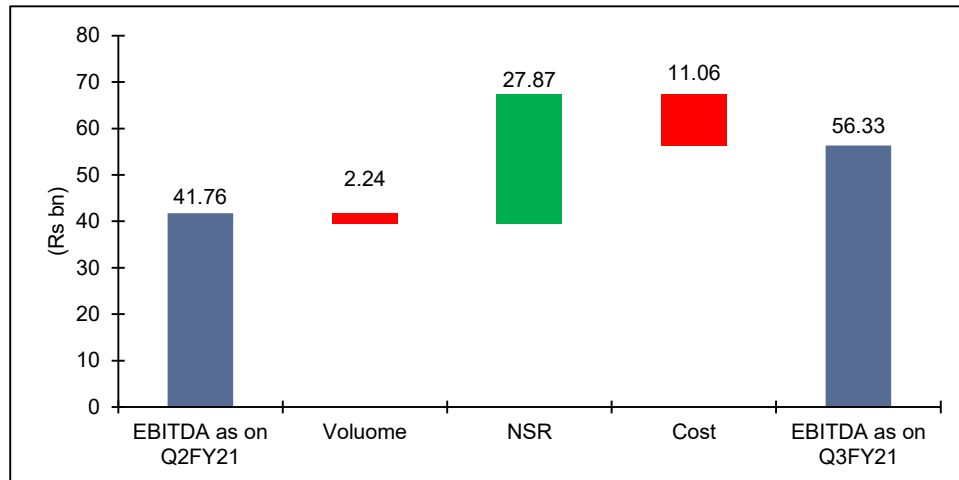
Source: Company data, I-Sec research

Table 2: JSWS's consolidated Q3FY21 result review

	Q3FY21	Q3FY20	% Chg YoY	Q2FY21	% Chg QoQ
Net Sales	218,590	178,050	22.8	192,640	13.5
Total expenditure	159,130	156,040	2.0	148,500	7.2
EBITDA	59,460	22,010	170.1	44,140	34.7
Margin %	27.2	12.4	120.0	22.9	18.7
Other Income	1,470	1,270	15.7	1,520	(3.3)
Interest	9,770	10,600	(7.8)	9,590	1.9
PBDT	51,160	12,680	303.5	36,070	41.8
Depreciation	12,300	10,550	16.6	11,490	7.0
PBT (recurring)	38,860	2,130	1,724.4	24,580	58.1
PBT (reported)	38,860	4,630	739.3	24,580	58.1
Tax (recurring)	12,120	470	2,478.7	-	NM
Tax (reported)	12,120	2,490	NM	9,100	33.2
Reported PAT	26,740	2,140	1,149.5	15,480	72.7
Adj Net Profit Ater MI and associate	26,690	1,870	1,327.3	15,950	67.3

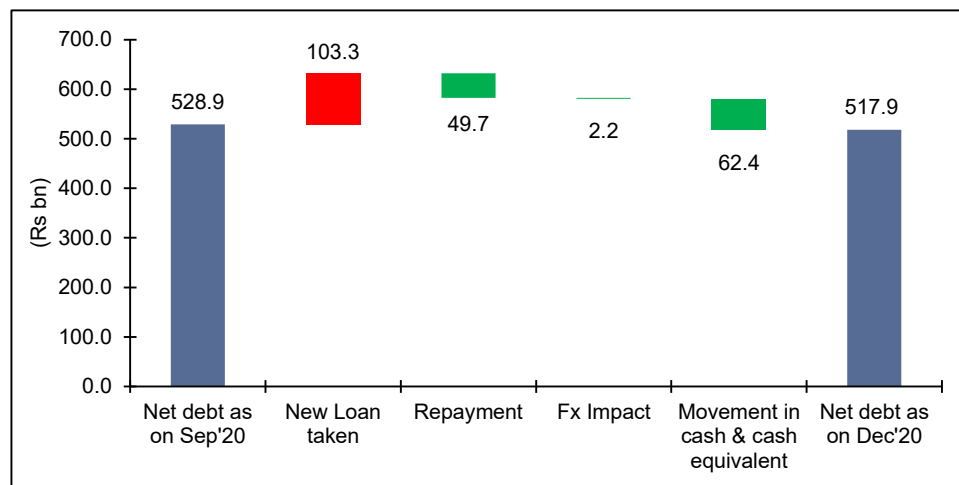
Source: Company data, I-Sec research

Chart 1: Operating EBITDA movement (standalone)



Source: Company data, I-Sec research

Chart 2: Net debt movement (consolidated)



Source: Company data, I-Sec research

Table 3: US – Plate and pipe mill quarterly performance

(US \$mn)	Q3FY21	Q3FY20	% Chg YoY	Q2FY21	% Chg QoQ
Sales (te)					
Plates	18,183	52,749	(65.5)	51,719	(64.8)
Pipes	150	11,328	(98.7)	447	(66.4)
Revenue	10	64	(83.7)	36	(70.9)
EBITDA	(8)	(13)	NM	17	NM

Source: Company data, I-Sec research

Table 4: US – Ohio quarterly performance

(US \$mn)	Q3FY21	Q3FY20	% Chg YoY	Q2FY21	% Chg QoQ
HRC Production (te)	-	74,272	(100.0)	4,501	(100.0)
HRC Sales (te)	10,892	58,611	(81.4)	20,837	(47.7)
Revenue	5	37	(85.0)	18	(70.3)
EBITDA	(21)	(25)	NM	(11)	NM

Source: Company data, I-Sec research

Table 5: Italy – Piombino quarterly performance

(Euro mn)	Q3FY21	Q3FY20	% Chg YoY	Q2FY21	% Chg QoQ
Production (te)					
Rolled Products (Bars, Wire Rod & Rails)	72,866	156,778	(53.5)	61,919	17.7
Grinding Ball	11,196	17,745	(36.9)	10,713	4.5
Sales (te)					
Rolled Products	76,617	144,825	(47.1)	50,622	51.4
Grinding Ball	7,377	11,852	(37.8)	7,514	(1.8)
Revenue	61	1,161	(94.7)	43	41.6
EBITDA	(0.5)	(10.0)	NM	(12.6)	NM

Source: Company data, I-Sec research

Table 6: JSW Steel Coated Products quarterly performance

(Rs mn)	Q3FY21	Q3FY20	% Chg YoY	Q2FY21	% Chg QoQ
Production (kt)	0.47	0.47	-	0.51	(7.8)
Sales (kt)	0.61	0.52	17.3	0.61	-
Revenue	41,820	29,820	40.2	37,820	10.6
Realisations (Rs/te)	68,557	57,346	19.6	62,000	10.6
EBITDA	3,970	1,340	196.3	2,880	37.8
EBITDA (Rs/te)	6,508	2,577	152.6	4,721	37.8
PAT	2,690	500	438.0	1,720	56.4

Source: Company data, I-Sec research

Key takeaways from conference call

- Management sees **demand greenshoots** all around and expects demand momentum to continue. Steel demand has increased from 1mnte to 10mnte April to Dec, '20. Agri packaging, large infra projects, warehousing are key demand areas. Management expects restocking demand to sustain in Q4FY21, as system/channel inventory has gone down ~ 3mnte in 9MFY21.
- **Iron ore integration** went up to 49% in Q3FY21 from 26% in Q2FY21. Higher iron ore availability led to capacity utilisation moving to 96% in Q3FY21 from 86% in Q2FY21. Easing of logistics constraints also helped availability. Management is planning to increase EC limits of iron ore mining from 25mnte to 35mnte, as requirement from Dolvi is going to increase from FY22E. The current production and despatch runrate of 1.8-2mnte per month will continue. Q3FY21 topline from iron ore sale has been ~ Rs5bn.
- **Product mix.** Exports have been moderated to 12% of the product mix in Q3FY21 from 28% QoQ, Auto volumes are up 33%QoQ, value added product sales went up to 57% of the total mix (from 50% QoQ). Improved product mix and moderation of exports led to higher margins in the quarter. -2.5 months financials of Asian colour coated performance is included in the results.
- **EBITDA/te performance.** Q3FY21 witnessed 20% QoQ increase for blended net sales realisation (NSR). Iron ore was Rs1960/te in June, '20, went up to Rs4610/te in Dec,'20 and witnessed another Rs200/te in Jan, '21. QoQ costs have gone up by 8% for Q3FY21 (as per management)
- **Subsidiary performance.** Overseas subsidiary operating loss was Rs840mn, including one-off, operating loss was Rs2.08bn. Baytown and Mingo will start in Sept, '2021. Indian subs contributed Rs7bn in EBITDA.
- **Projects.** Dolvi commissioning delayed by one quarter. Integrated operation may shift to Q1FY22, particularly for the melt shop. While iron ore mine capacity expansion will be undertaken, there is no incremental capex as the OnM has been handed over to a MDO.
- **Net Debt at Rs517.9bn in Q3FY21, ND/EBITDA is 3.53x.** Revenue acceptances are US\$947mn while capital acceptances are US\$491mn. Q3FY21 witnessed ~ Rs11bn in net debt reduction after investment in *Asian colour coated* of Rs15.5bn. Rs26.6bn of working capital release is seen for 9MFY21 and the same has been utilised towards deleveraging. FY21E capex will be within Rs90bn. If Bhushan power acquisition goes through then equity investment in the JV/associate entity will have to be made, which may not allow for deleveraging in Q4FY21.
- **Guidance** JSWS will be at 95% of guidance for production (previous guidance at 16mnte). Management believes with ~4mnte of sales in Q4FY21 company should achieve sales guidance. **Coking coal price increase should reflect in Q1FY22.** A request has been forwarded to Auto OEMs to break up the contract price scheduled from Sept, '20 to Mar, '21 and to have a price reset clause introduced from 1st Jan, '21 given the sharp price increase seen in the market.
- **Turnaround in Monnet Ispat operations.** Monnet Ispat has been renamed as JSW Ispat speciality product and recorded an EBITDA of Rs1.52bn and net profit of Rs290mn. JSWS is not looking to acquire majority stake and integrate / consolidate Monnet's financial in near to medium term.

Table 7: Rolling capex plan

<i>(Rs mn)</i>	
Announced Capex (FY18-FY22)	485,150
Capex Spent (FY18-FY20)	239,280
FY21 - Project Capex	82,000
FY21 - Mining Capex	8,000
Capex to be spent over FY22-FY23	163,870

Source: Company data

Valuation – Maintain SELL

We maintain **SELL** with a revised target price of Rs292/share (previously Rs 265/share). We maintain P/B of 1.2x on FY23E book value.

Key risks

Key upside risks to our earnings and target price are i) Steel prices staying higher for longer – clearly a low probability event as corrections in the secondary market has already started and ii) Higher than expected debt deleveraging as management curtails capex plans – another low probability scenario in our view. Downside risks are i) lower steel prices and more importantly lower spreads given that peak spreads are estimated to be reached at Q4FY21 and ii) higher raw material integration benefits.

Revision of earnings and estimates

Table 8: Earnings and key assumption changes

	New			Old			% Chg		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Sales	814,379	922,565	945,203	781,282	972,328	977,937	4.2	(5.1)	(3.3)
EBITDA	191,916	208,716	162,760	151,556	165,608	175,163	26.6	26.0	(7.1)
PAT	79,800	87,988	54,535	54,908	55,589	57,866	45.3	58.3	(5.8)
Standalone Realisations (Rs/te)	43,166	43,473	40,442	42,866	42,200	42,142	0.7	3.0	(4.0)
Standalone Volumes	15.0	17.4	19.3	15.0	18.5	19.3	-	(6.0)	-
Standalone EBITDA/te (US\$/te)	169	155	106	139	122	115	21.7	26.7	(8.1)

Source: I-Sec research

We have increased steel price assumptions for FY21/22E given the sharp price increase witnessed in Dec, '20 while adjusting for interest and depreciation for FY21E given 9MFY21 print.

Financial summary

Table 9: Profit & loss statement

(Rs mn, year ending March 31)

	FY20	FY21	FY22E	FY23E
Operating Income (Sales)	733,260	814,379	922,565	945,203
Operating Expenses	614,530	622,462	713,848	782,442
EBITDA	118,730	191,916	208,716	162,760
% margins	16.2	23.6	22.6	17.2
Depreciation & Amortization	42,460	45,268	55,760	59,891
Gross Interest	42,650	39,506	34,192	31,593
Other Income	5,460	5,500	5,500	5,500
Recurring PBT	39,080	112,642	124,265	76,776
Add: Extra ordinaries	(8,050)	-	-	-
Less: Taxes	(9,060)	33,291	36,726	22,691
Less: Minority Interest	(900)	(450)	(450)	(450)
Net Income	40,990	79,800	87,988	54,535
Recurring Net Income	49,040	79,800	87,988	54,535

Source: Company data, I-Sec research

Table 10: Balance sheet

(Rs mn, year ending March 31)

	FY20	FY21	FY22E	FY23E
Assets				
Total Current Assets	293,730	233,830	265,921	281,179
of which cash & cash eqv.	120,030	73,479	109,850	120,227
Total Current Liabilities & Provisions	243,730	218,064	252,769	279,045
Net Current Assets	50,000	15,766	13,153	2,134
Investments	12,590	12,590	12,590	12,590
Strategic/Group	12,570	12,570	12,570	12,570
Other Marketable	20	20	20	20
Net Fixed Assets	852,990	897,980	921,434	940,834
Capital Work-in-Progress	271,910	119,648	122,362	125,154
Goodwill	4,150	4,150	4,150	4,150
Total Assets	1,074,470	1,038,674	1,095,886	1,114,645
Liabilities				
Borrowings	697,460	582,641	552,641	517,641
Deferred Tax Liability	16,770	16,770	16,770	16,770
Minority Interest	(5,750)	(6,200)	(6,650)	(7,100)
Equity Share Capital	2,417	2,417	2,417	2,417
Reserves & Surplus	1	1	1	1
Net Worth	365,990	445,464	533,126	587,334
Total Liabilities	1,074,470	1,038,674	1,095,886	1,114,645

Source: Company data, I-Sec research

Table 11: Cashflow statement

(Rs mn, year ending March 31)

	FY20	FY21	FY22E	FY23E
Operating Cashflow	66,260	124,742	143,422	114,099
Working Capital Changes	16,390	34,234	2,613	11,019
Capital Commitments	(128,740)	(90,258)	(79,214)	(79,292)
Free Cashflow	(46,090)	68,718	66,821	45,827
Cashflow from Investing Activities	(10,410)	(450)	(450)	(450)
Issue of Share Capital	-	-	-	-
Buyback of shares	-	-	-	-
Inc (Dec) in Borrowings	114,700	(114,819)	(30,000)	(35,000)
Dividend paid	(11,950)	(326)	(326)	(326)
Extraordinary Items	-	-	-	-
Chg. in Cash	59,050	(46,551)	36,371	10,377

Source: Company data, I-Sec research

Table 12: Key ratios

(Year ending March 31)

	FY20	FY21	FY22E	FY23E
Per Share Data (Rs)				
EPS(Basic Recurring)	20.3	33.0	36.4	22.6
Diluted Recurring EPS	20.3	33.0	36.4	22.6
Recurring Cash EPS	37.9	51.7	59.5	47.3
Dividend per share (DPS)	2.0	0.1	0.1	0.1
Book Value per share (BV)	151.4	184.3	220.6	243.0
Growth Ratios (%)				
Operating Income	(13.5)	11.1	13.3	2.5
EBITDA	(37.4)	61.6	8.8	(22.0)
Recurring Net Income	(34.8)	62.7	10.3	(38.0)
Diluted Recurring EPS	(34.8)	62.7	10.3	(38.0)
Diluted Recurring CEPS	(20.9)	36.7	14.9	(20.4)
Valuation Ratios (x)				
P/E	18.2	11.2	10.2	16.4
P/CEPS	9.8	7.2	6.2	7.8
P/BV	2.4	2.0	1.7	1.5
EV / EBITDA	12.4	7.3	6.4	7.9
EV / Operating Income	2.0	1.7	1.4	1.4
EV / Operating FCF	NM	NM	20.0	28.2
Operating Ratios (%)				
Raw Material/Sales	52.8	37.6	40.4	45.2
SG&A/Sales	10.4	7.6	7.8	8.1
Other Income / PBT	14.0	4.9	4.4	7.2
Effective Tax Rate	(23.2)	29.6	29.6	29.6
NWC / Total Assets	4.7	1.5	1.2	0.2
Inventory Turnover (days)	94	85	83	83
Receivables (days)	22	16	16	16
Payables (days)	142	125	127	128
D/E Ratio (x)	1.9	1.3	1.0	0.9
Profitability Ratios (%)				
Rec. Net Income Margins	6.7	9.8	9.5	5.8
RoCE	7.6	13.9	14.3	9.3
RoNW	13.7	19.7	18.0	9.7
Dividend Payout	29.2	0.4	0.4	0.6
Dividend Yield	0.5	0.0	0.0	0.0
EBITDA Margins	16.2	23.6	22.6	17.2

Source: Company data, I-Sec research

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