Research

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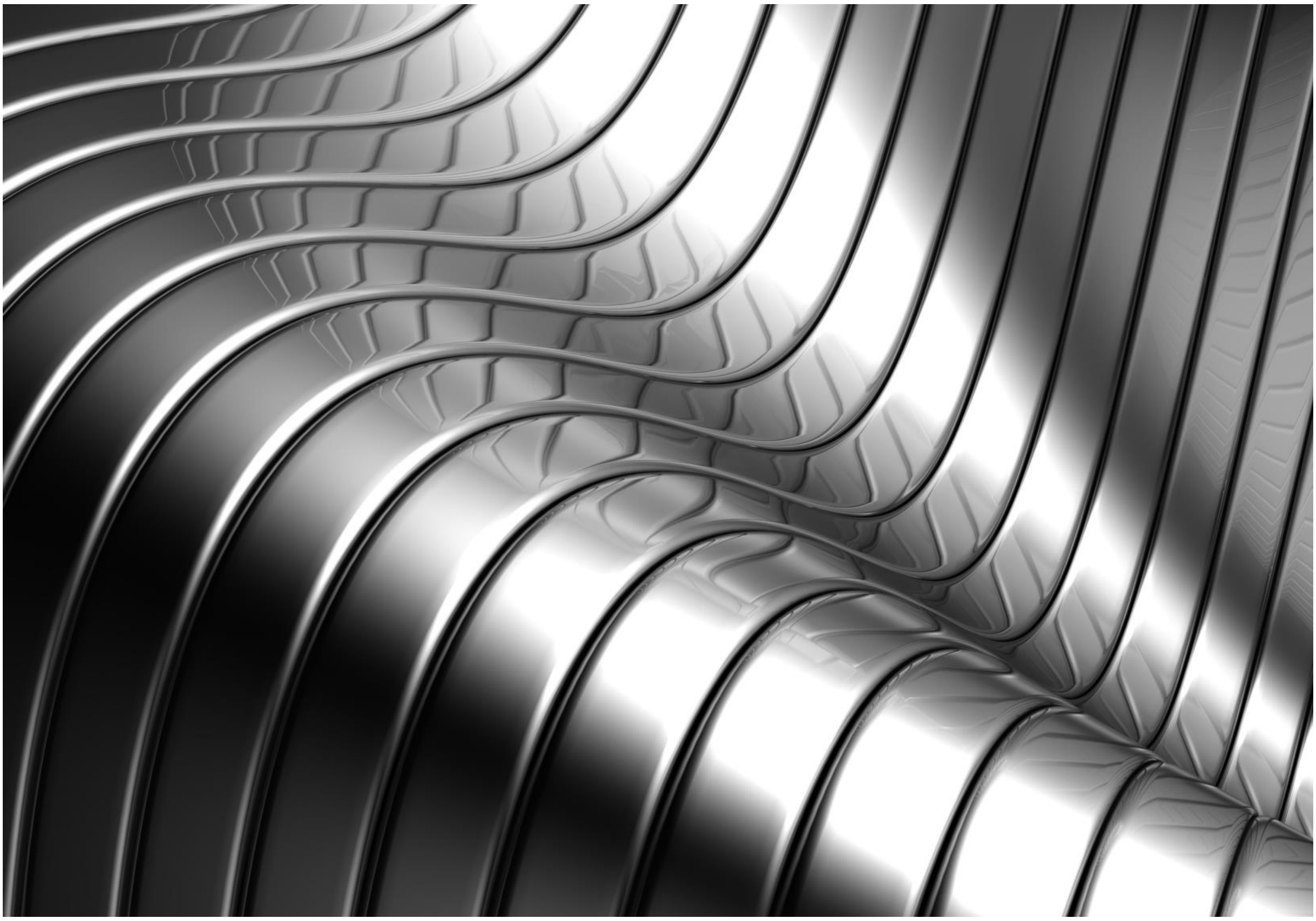
Price lift for steelmakers

Decadal high domestic steel prices augur well for large producers



Chartbook | January 2021

Domestic steel prices defied predictions and ascended through the December quarter as three tailwinds converged: high global prices, tight domestic supply on account of iron ore shortage, and healthy demand growth.

Taking cue, steel makers have raised the prices of hot-rolled coils (HRC; average monthly price) multiple times since August, rising by as much as Rs 13,800 per to Rs 51,050 per tonne in December (37% on-year growth).

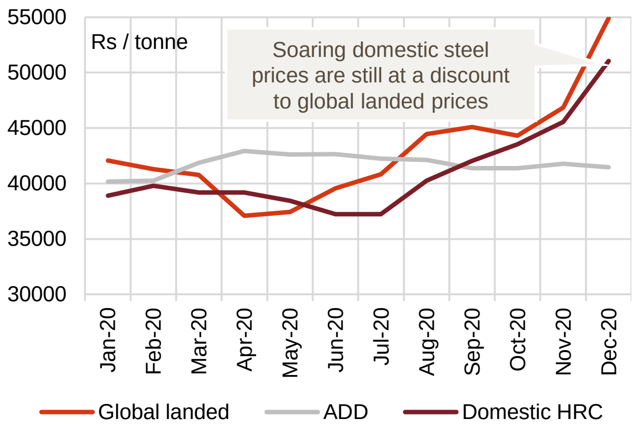
Importantly, despite this material increase, domestic prices are still 6-8% below global landed prices. Put another way, there is room to raise domestic prices further given they move in sync with the world trend.

China HRC f.o.b. (free on board) prices, after plunging to $409 per tonne in April from $499 per tonne in January 2020, rebounded to $647 per tonne between April and December 2020.

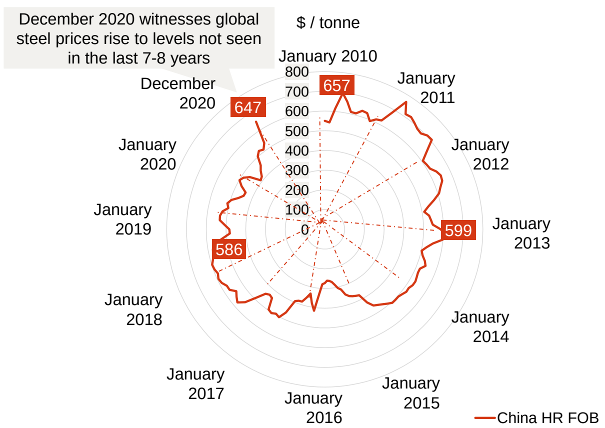
Global prices also touched an 8-year high in December on healthy demand and cost push from soaring iron-ore prices. Chinese crude steel production increased 8% in the period, while exports and inventories remained low indicating robust demand growth there.

We expect steel prices to remain high in the January-March 2021 quarter with a sequential price hike of Rs 7,000-8,500 per tonne. Consequently, flat steel prices are seen 14-15% higher on-year this fiscal.

Domestic flat steel (HRC) prices soar



Global HRC prices touch previous peaks



Source: Industry, CRISIL Research

Note: The spider chart depicts monthly price trend for China HRC f.o.b. from January 2010 to December 2020.

Domestic demand recovered to the pre-pandemic (February) level in August itself with normalisation of activities in the construction and consumption-linked sectors, but a full-blown recovery was seen only in November when sales volume surged 11% on-year.

The demand momentum should continue in January-March. Growth will also be bolstered by the statistical low-base effect of fiscal 2020.

That would limit the contraction in steel demand this fiscal to 9-11%**,** compared with our previous forecast of a 17-20% de-growth.

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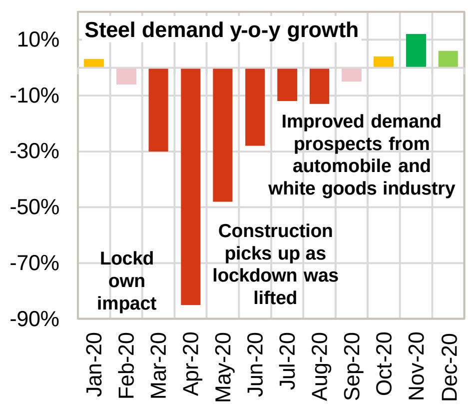
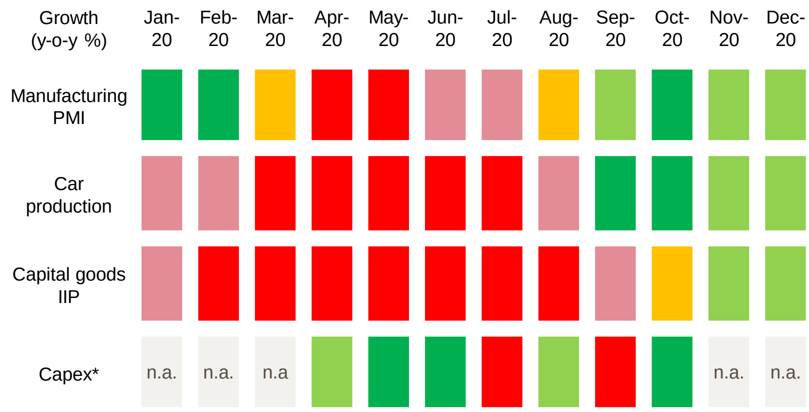
Syncing with economic green shoots



End-use sector indicators

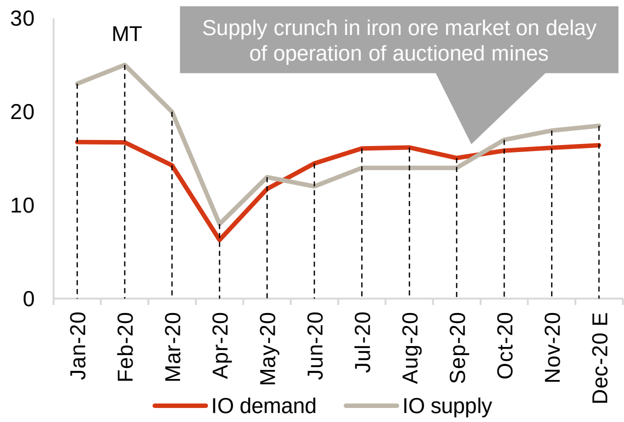


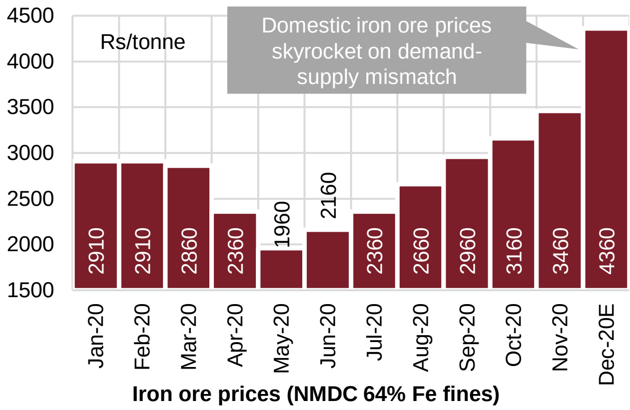
*Note: *Central government capital expenditure for roads, railways, housing; n.a. – not available*

Source: Joint Plant Committee, the Ministry of Statistics and Programme Implementation, industry, CRISIL Research

On the raw materials front, domestic iron ore supply could not match demand from steel mills as only 6-7 of the 19 auctioned mines in Odisha could begin mining operations. Of these, most were won by steelmakers for captive consumption. The 19 mines used to sell 65-70 million tonne of iron ore to merchant markets in eastern India. The tight supply augured well for domestic iron ore prices, which more than doubled from May-June levels to Rs 4,360 per tonne in December. However, it remains 60-65% cheaper than landed iron ore prices.

Iron ore prices more than doubled in May-December

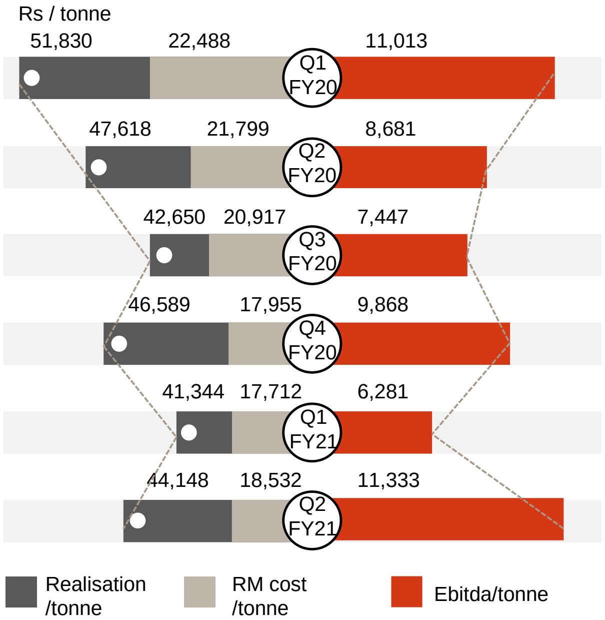


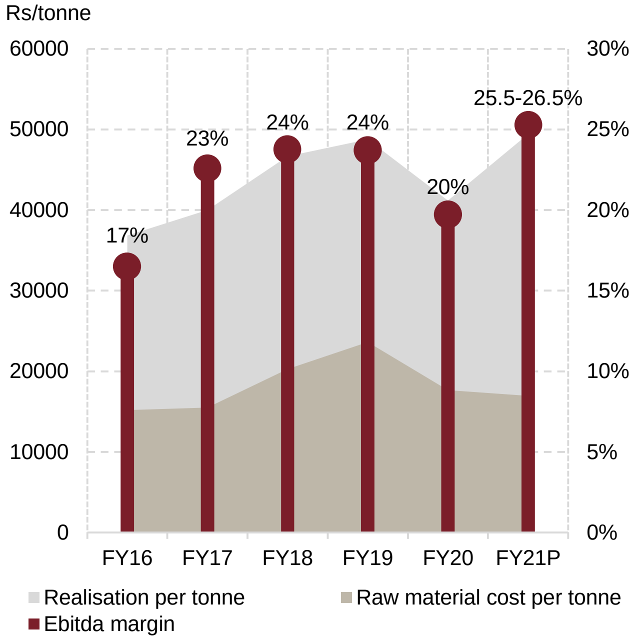


Source: Ministry of Mines, company reports, industry, CRISIL Research

Coking coal prices, on the other hand, have declined, led by low procurement from China amid stable supply. Improved realisation, healthy demand and lower coking coal prices augur well for the operating margins of steel mills, especially in the second half of the current fiscal. As a result, large steel mills, excluding the public sector ones, should see a 550-650 basis points (bps) Ebitda margin expansion this fiscal. In the second quarter, their margins expanded 740 bps, after plunging 600 bps in the first quarter.

Robust bounce-back in margins forged in the second quarter





Source: Company reports, industry, CRISIL Research

Note: Financials for only large private players (JSW Steel, JSPL and Tata Steel)

Given all this, we expect the large steelmakers (excluding the public sector ones) to clock an impressive 800-1000 bps improvement in their Ebitda margins (on-year) in the second half of this fiscal, riding on the tailwinds of a 35% increase in domestic steel prices, a 30-35% decline in coking coal prices, and surging demand.

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