

Turkey — Steel

Eregli Steel

Continues To Shine

Adding Erdemir to our Model Portfolio with a 12-month TRY39 price target and 39% return potential. Our positive view is based on i) HRC, CRC and rebar steel prices staying above its 3-year average in 2022, ii) FX based revenue generation and upside risks to EBITDA, iii) c20% dividend yield in 2022 (March) and 2023, iv) attractive valuation multiples and discount compared to peers. Our valuation is equal weighted DCF (20% risk free rate, 5% equity premium, 21.5% WACC) and peer multiples comparison. (2022E EV/EBITDA 5.1x, including local peers KRDM). Details of our valuation are on Page 3-4.

Steel prices continue to stay above 3-year averages. After reaching historical high levels in the first half of 2021 with around \$1100/ton for HRC (hot-rolled coil), \$1350/ton for CRC (cold-rolled coil) and \$740/ton for rebar, steel prices declined c25% to its current levels of HRC \$835/ton, CRC \$975/ton, rebar \$705/ton. Despite this sharp decline, steel prices are still looking healthy and stay above last 3-year averages of HRC \$617/ton, CRC \$732/ton and rebar \$529/ton, according to Bloomberg data. Being at the mid cycle, we expect these prices to continue to stay above previously mentioned average levels and contribute to Erdemir operating profitability in 2022.

Downward trend in raw material costs supports high EBITDA per ton levels. With coal and iron ore prices decreasing respectively c.40% and c.30% from their historical highs in the first half of 2021, we expect 4Q21 EBITDA per ton as \$355 and \$340 for the 2021 all year. For 2022, our EBITDA per ton expectation is at \$256, which is still %33 above \$192 last 3-years average. With declining demand for coal and iron ore in China due to decline in construction activity, we expect global prices for raw materials will continue to decline.

Recent regulation change favors dividend payers. With the current regulation change lowering the withholding tax on dividends from 15% to 10%, we expect Erdemir to take the spotlight as payment season kicks off in 1Q. On 2021E TL 16.4bn net profit and a 85% payout-ratio, we estimate TL4 per share as dividends, corresponding to 14% yield. Erdemir plans USD 1bn capacity expansion related investment in 2022, to be financed on a long-term basis and low capital employment. We therefore estimate the Company's dividend policy to remain unchanged, as the free cash flow generation from operations would remain robust.

Attractive multiples and discounts to peer averages. Erdemir's global & local peers are trading at a 2022E median P/E of 6.1x; EV/EBITDA of 5.1x (Page 4). Accordingly, Erdemir is trading at 2022E P/E ratio of 4.3 and EV/EBITDA ratio of 3.1. Erdemir's past three year EV/EBITDA multiple average is 4.4x (Page 5). Our 2022 revenue, EBITDA and net income estimates are 37%, 20% and 16% above Bloomberg consensus, our USD/TRY estimations are 9.5 average for 2021 and 15.5 for 2022.

EREGL	2018	2019	2020	2021E	2022E	2023E
Net Income (TL mn)	5,598	3,317	3,309	16,431	22,976	23,682
Revenue (TL mn)	27,015	27,465	32,048	68,074	102,847	108,692
EBITDA (TL mn)	8,630	5,458	6,665	25,184	32,028	32,935
Net Debt/EBITDA (x)	-0.3	-0.5	-1.0	-0.6	-0.4	-0.3

Source: Company Data, INFO Research Estimates

BUY

Price: TL27.82

Price Target: TL39

Company Data

Stock Ticker	EREGL
Stock Rating	BUY
Price Target	39
Up/downside to PT	39%
Share Price	27.82
52-week range (TL)	11.65 - 36.26
No. of shares (mn)	3,500
Free Float	48%
MCAP (TL mn)	97,370
MCAP (USD mn)	8,231
Net Debt (TL mn)	-1,836
3M ADV (USD mn)	104
3M ADV/FF MCAP (%)	2.6%

Valuation

	2020	21E	22E	23E
P/E (x)	30.0	6.0	4.3	4.2
EV/EBITDA (x)	14.8	3.9	3.1	3.0
P/B (x)	2.5	2.0	1.7	1.6
Div. Yield	6.2%	14.1%	19.7%	20.3%

Source: INFO Research Estimates

Stock Performance



INFO Research

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Table 1. Financials

Income Statement					Financial Analysis				
(TLmn)	2020	2021E	2022E	2023E		2020	2021E	2022E	2023E
Net Sales	32,048	68,074	102,847	108,692	Growth (%)				
Gross profit (loss)	5,925	25,556	32,967	33,703	Sales	16.7	112.4	51.1	5.7
Operating Expenses	-785	-2,003	-3,000	-3,070	EBITDA	22.1	277.8	27.2	2.8
Core EBIT	5,140	23,552	29,967	30,633	Net Profit	-0.2	396.6	39.8	3.1
Inc.& Exp. from Other Operations	433	824	1,059	995	Margins (%)				
Reported EBIT	5,573	24,376	31,026	31,628	Gross Margin	18.5	37.5	32.1	31.0
Financial Income/Expenses	11	-279	-21	282	EBITDA Margin	20.8	37.0	31.1	30.3
Other income	65	139	210	222	EBIT Margin	16.0	34.6	29.1	28.2
PBT from continuing operations	5,658	24,236	31,215	32,132	Net Margin	10.3	24.1	22.3	21.8
Tax on Continuing Operations	-2,148	-7,165	-9,205	-9,471	Efficiency				
Net Profit	3,309	16,431	22,976	23,682	Receivables Days	41	40	40	40
EBITDA	6,665	25,184	32,028	32,935	Inventory Days	136	120	120	120
					Payables Days	53	53	53	53
					Working Capital/Net Sales (%)	30	22	23	24
					Profitability (%)				
					ROA	5.7	20.0	20.0	18.7
					ROE	8.3	32.8	38.9	37.4
					ROIC	9.5	45.8	45.4	40.7
					Leverage (x)				
					Asset/Equity	1.46	1.64	1.94	2.00
					Net Debt/EBITDA	-1.05	-0.56	-0.40	-0.35
					Capex/Revenues (%)	6.2	7.0	7.0	6.0
Balance Sheet									
(TLmn)	2020	2021E	2022E	2023E					
Current Assets	28,507	49,057	75,981	83,175					
Cash and Marketable Securities	13,581	25,611	38,704	43,404					
ST Trade and Related Receivables	3,874	7,460	11,271	11,911					
Inventories	10,107	13,978	22,974	24,654					
Other Short-Term Assets	945	2,007	3,033	3,205					
Long Term Assets	29,487	33,017	38,730	43,519					
TOTAL ASSETS	57,994	82,074	114,711	126,694					
Short Term Liabilities	9,434	16,383	31,766	36,791					
ST Financial Payables	3,786	7,633	17,727	21,788					
ST Trade and Other Payables	4,436	6,174	10,147	10,889					
Other Short-Term Liabilities	1,213	2,577	3,893	4,114					
Long Term Liabilities	7,438	13,651	22,862	25,668					
LT Financial Payables	2,813	3,826	8,018	9,981					
Other Long-Term Liabilities	4,625	9,825	14,844	15,687					
Equity	39,809	50,119	59,129	63,281					
Minority Interest	1,312	1,920	954	954					
TOTAL LIABILITIES AND S.HOLDERS' EQUITY	57,994	82,074	114,711	126,694					

Source: Company Data, INFO Research Estimates

Table 2. Cash Flow

DCF	2017	2018	2019	2020	2021E	2022E	2023E	2024E	2025E	2026E
EBIT	4,756	7,721	4,309	5,140	23,552	29,967	30,633	29,963	28,048	26,559
+ Depreciation & amortisation	720	908	1,150	1,525	1,632	2,061	2,302	2,922	3,273	3,604
- Capex	-751	-940	-1,399	-1,984	-4,765	-7,199	-6,522	-6,892	-7,355	-7,924
- Change in working capital	0	-4,969	1,342	-78	-5,719	-8,833	-1,579	-1,932	-2,574	619
- Taxes	-1,016	-2,495	-1,357	-2,010	-7,066	-8,990	-9,190	-8,989	-8,414	-7,968
- Other										
Free cash flow to firm (FCFF)	3,708	225	4,045	2,594	7,634	7,005	15,645	15,072	12,978	14,890
Discount factor					0.86	0.71	0.58	0.48	0.40	0.33
Discounted cash flow for projected period	37,944				6,588	4,975	9,144	7,249	5,137	4,850
Discounted cash flow for perpetuity	51,207									
Enterprise value	89,151									
- 21/9M Net Debt	-1,836									
- Minority interest	1,745									
+ Participations	275									
Equity value	89,517									
Implied Price	25.60									
12M Equity Value	108,776									
12M Price Target	31.11									
Potential upside	12%									
WACC										
Risk free rate										20.0%
Beta										0.96
Equity risk premium										5.0%
Cost of equity										24.8%
Cost of debt, after tax										15.0%
Debt ratio										33.4%
Weighted average cost of capital										21.5%
Terminal growth rate										11.0%

Source: Company Data, INFO Research Estimates

Table 3. Valuation

Valuation Method	Weight	Implied Value	Contribution
DCF	50%	108,814	54,407
Peer Comparison	50%	162,127	81,064
Target Value (TL mn)			135,470
Target Price (TL)			39
Current Price (TL)			27.82
Upside Potential			39%

Source: Info Research Estimates

Table 4. Peer Multiples

RT Kodu	Şirket Adı	Piyasa Değeri (USD mn)	2021(T)		2022(T)	
			F/K	FD/VAFÖK	F/K	FD/VAFÖK
MT:NL	Arcelormittal Sa	31,627	2.5	1.9	3.5	2.5
2002:TW	China Steel Corp	20,166	11.6	5.3	11.8	5.3
STLD:USN	Steel Dynamics Inc	12,235	3.8	3.0	4.9	3.8
2002:TW	China Steel Corp	20,166	9.1	6.4	8.6	6.4
TRMK:RUM	Tmk	1,006	4.4	6.6	3.4	5.4
500470:INM	Tata Steel Ltd	18,167	2.7	4.1	6.1	5.1
323:HK	Maanshan Iron And Steel Co Ltd (H)	2,903	2.3	2.2	9.1	4.6
JSWSTEEL:INN	Jsw Steel Ltd	20,989	6.9	5.5	8.9	6.5
KRDMD	Kardemir (D)	892	3.8	2.2	3.3	2.3
	Medyan		3.8	4.1	6.1	5.1
EREGL	Eregli Demir Celik	8,825	6.0	3.9	4.3	3.1
			-36%	4%	42%	64%

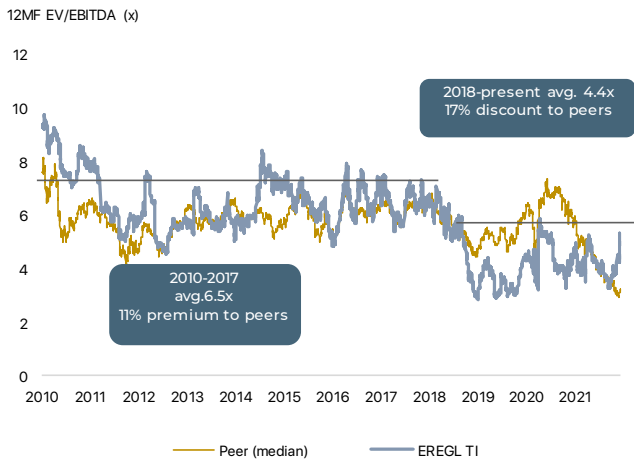
Source: Equity RT, Info Research Estimates

Table 5. Peer Performance

	Absolute Return in Local Currency (%)				Relative Return in Local Currency (%)			
	YTD	1M	3M	12M	YTD	1M	3M	12M
Arcelormittal Sa	52.0	17.3	9.4	51.0	52.0	17.3	9.4	51.0
China Steel Corp	44.8	7.6	-1.1	48.1	44.8	7.6	-1.1	48.1
Steel Dynamics Inc	69.5	-2.9	0.2	73.0	69.5	-2.9	0.2	73.0
China Steel Corp	44.8	7.6	-1.1	48.1	44.8	7.6	-1.1	48.1
Tmk	53.8	-10.7	-24.0	53.2	53.8	-10.7	-24.0	53.2
Tata Steel Ltd	77.2	0.3	-12.2	83.3	77.2	0.3	-12.2	83.3
Maanshan Iron And Steel Co Ltd (H)	44.0	4.3	-17.6	40.1	44.0	4.3	-17.6	40.1
Jsw Steel Ltd	69.9	3.6	0.4	79.6	69.9	3.6	0.4	79.6
Kardemir (D)	62.3	8.8	47.3	74.0	26.3	1.9	8.0	30.8
Eregli Demir Celik	118.6	27.8	70.5	129.9	70.2	19.6	25.1	72.8

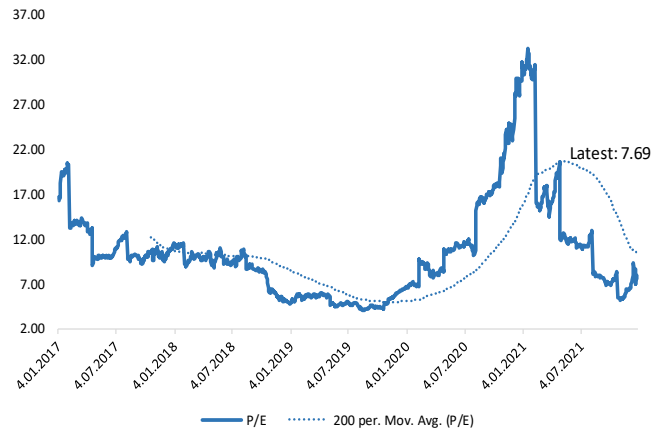
Source: Equity RT

Table 6. Historical EV/EBITDA Multiple



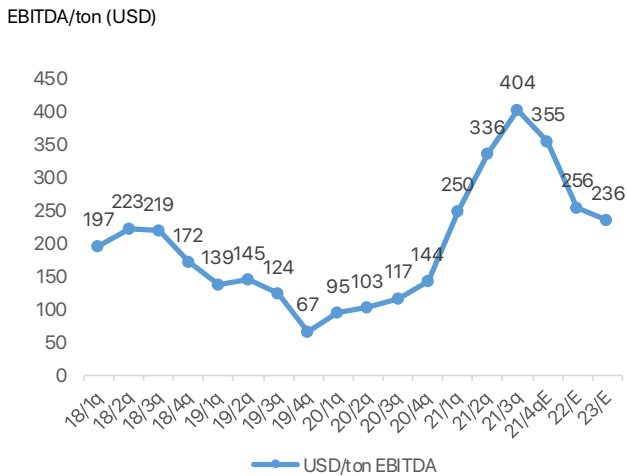
Source: Bloomberg

Table 7. Historical P/E Multiple



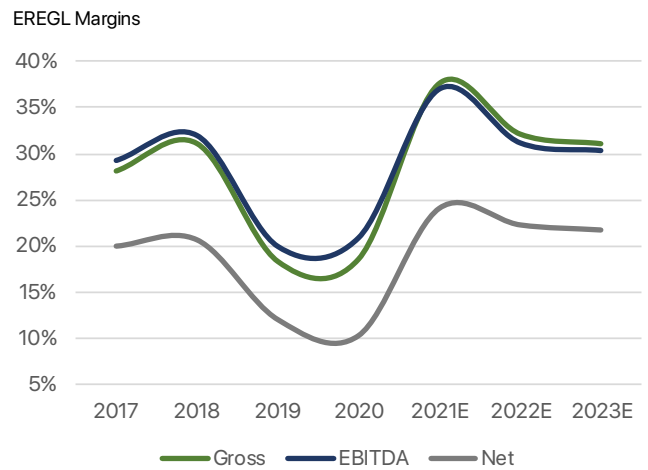
Source: Equity RT

Table 8. Quarterly EBITDA/ton (USD)



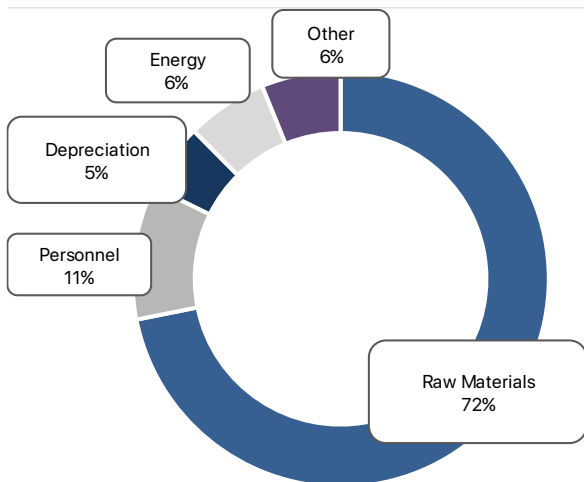
Source: Company Data, INFO Estimates

Table 9. EREGL Margins



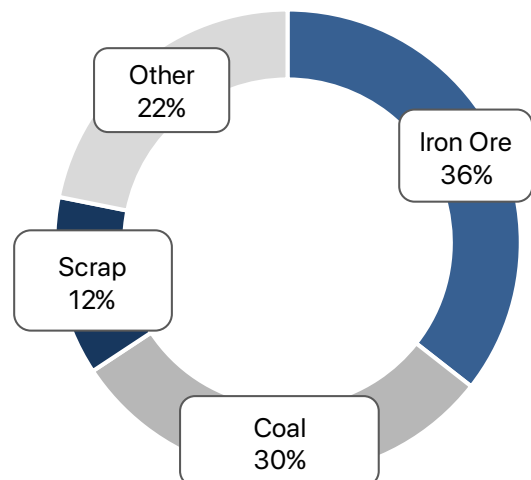
Source: Equity RT, INFO Estimates

Table 9. 5-Year Average COGS Mix (%)



Source: Company Data

Table 10. 5-Year Average Raw Material Mix (%)



Source: Company Data

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