

Turkey — Steel

Kardemir

Looks Like a Steal

We are raising our TP for Kardemir from TL11 (last update May'21) to TL23, keeping the stock in our Model Portfolio on 62% potential upside. Our revision is based on i) escalation in Russia-Ukraine conflict keeping steel prices at elevated levels with a positive outlook on Turkey exports, ii) increase in average USDTRY rate from 11.50 in 4Q to 13.61 so far in 1Q22, iii) high cash generation prospects rendering 6% dividend yield in 2022 & 15% in 2023, and iv) attractive valuation multiples. Our valuation is DCF based with 22% risk free rate, 5% equity risk premium and 27% WACC (details on Page 3).

Supply & Demand dynamics keeping steel prices and EBITDA per ton at elevated levels.

Kardemir reported strong 4Q results on the back of EBITDA per ton reaching USD282 level, bringing the 2021 average to USD236. Escalation in Russia-Ukraine crisis caused 5-6% spike in steel prices to USD700 per ton for billet, USD900 for bar & wire rod, USD940 for profile and USD840 round products in March. Our average price expectation for the said products for 1Q is USD810. While the price escalation may hinder construction sector demand, billet production share may increase and act as a compensating factor. Kardemir has been well stocked in terms of coal inventories to weather increase in input costs and would report 2022 USD240-250 EBITDA per ton, in our view.

Turning to a net cash, dividend paying company in 2021. Kardemir benefitted massively from strong steel sector dynamics last year and reported 2x net sales, 4x EBITDA, TL3.9bn net income vs. TL61m in 2020. 4Q results underpinned an increasing trend within the year, TL4.7bn net sales, TL1.9bn EBITDA and TL1.7bn beating estimates by 2%, 25% and 56%, respectively. The key drivers of the positive numbers were 800bps quarterly increase in gross margin, TL200m FX gains on receivables and TL290m deferred tax. Turning from TL107m net debt position in 1Q to TL1.8bn in 4Q, Kardemir has announced TL1bn cash dividends from 2021 earnings, corresponding to a 40% payout ratio and 5.8% dividend yield, which would increase to 15% next year on TL5.4bn net income estimate and 50% payout assumption.

Trading at deep discounts vs. global peers. 2022E 2.7x PE and 1.4x EV/EBITDA look a 'steal' not only in nominal terms but in comparison with global peers (ex-Russia) trading at 4.8x and 2.6x, respectively (Page 4).

Risks. We are well aware of steel sector cyclicity but do not expect a downturn in the current market conditions and find safety in Kardemir's undemanding valuation multiples. We see key risk to the investment as Turkey specific; namely a reversal of current monetary policy disconnect with inflation. Sharp increase in TL interest rates to lower inflation would prop TL and pressure Turkey exporters & commodity producers.

BUY

Price: TL13.52

Price Target: TL23

Company Data

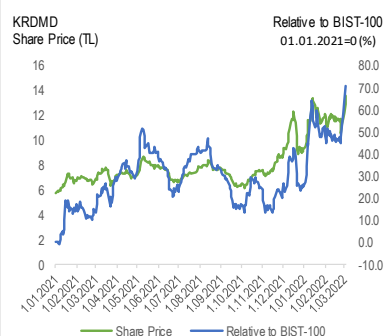
Stock Ticker	KRDMD
Stock Rating	BUY
Price Target	23
Up/downside to PT	62%
Share Price	13.52
52-week range (TL)	5.94 - 14.
No. of shares (mn)	780
Free Float (%)	89
MCAP (TL mn)	10,549
MCAP (USD mn)	744
Net Debt (TL mn)	-1,879
3M ADV (USD mn)	187
3M ADV/FF MCAP (%)	0.3%

Valuation

	2020	2021	2022E	2023E
P/E (x)	173.9	3.8	2.7	2.4
EV/EBITDA (x)	7.0	2.4	1.4	1.4
P/B (x)	2.7	1.1	0.7	0.6
Div. Yield	0.0%	5.8%	14.7%	17.0%

Source: INFO Research Estimates

Stock Performance



INFO Research

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KRDMD	2018	2019	2020	2021E	2022E	2023E
Net Income (TL mn)	814	81	61	3,853	5,401	6,236
Revenue (TL mn)	5,583	6,076	7,520	14,765	28,917	29,230
EBITDA (TL mn)	1,765	651	1,246	4,885	8,684	8,841
Net Debt/EBITDA (x)	1.0	2.6	0.6	-0.6	-0.5	-0.7

Source: Company Data, INFO Research Estimates

Table 1. Financials

Income Statement					Financial Analysis				
(TL mn)	2020	2021E	2022E	2023E		2020	2021E	2022E	2023E
Net Sales	7,520	14,765	28,917	29,230	Growth (%)				
Gross profit (loss)	1,144	4,782	8,907	9,030	Sales	23.8	96.4	95.9	1.1
Operating Expenses	-123	-143	-463	-585	EBITDA	91.5	292.1	77.8	1.8
Core EBIT	1,021	4,640	8,445	8,445	Net Profit	-24.8	6252.2	40.2	15.5
Inc.& Exp. from Other Operations	-478	158	-1,762	-700	Margins (%)				
Reported EBIT	544	4,797	6,682	7,745	Gross Margin	15.2	32.4	30.8	30.9
Financial Income/Expenses	-480	-466	-15	4	EBITDA Margin	16.6	33.1	30.0	30.2
Other income	11	135	264	267	EBIT Margin	13.6	31.4	29.2	28.9
PBT from continuing operations	77	4,467	6,932	8,015	Net Margin	0.8	26.1	18.7	21.3
Tax on Continuing Operations	-16	-614	-1,531	-1,780	Efficiency				
Net Profit	61	3,853	5,401	6,236	Receivables Days	58	38	38	49
					Inventory Days	102	92	100	104
EBITDA	1,246	4,885	8,684	8,841	Payables Days	137	164	152	144
					Working Capital/Net Sales (%)	7.9	-9.7	0.6	6.0
					Profitability (%)				
Balance Sheet					ROA	0.6	17.7	18.7	19.8
(TL mn)	2020	2021E	2022E	2023E	ROE	1.6	38.7	37.3	33.6
Current Assets	4,932	12,338	18,535	20,410	ROIC	16.3	55.2	86.4	62.5
Cash and Marketable Securities	1,440	5,357	6,117	6,772	Leverage (x)				
ST Trade and Related Receivables	1,300	1,793	3,011	3,948	Asset/Equity	2.77	2.19	2.00	1.70
Inventories	1,820	3,197	5,508	5,748	Net Debt/EBITDA	0.65	-0.56	-0.50	-0.69
Other Short-Term Assets	371	1,991	3,900	3,942	Capex/Revenues (%)	4.5	2.0	3.0	3.0
Long Term Assets	5,888	9,477	10,381	11,139					
TOTAL ASSETS	10,820	21,815	28,916	31,549					
Short Term Liabilities	4,818	9,590	12,367	11,468					
ST Financial Payables	716	1,037	870	315					
ST Trade and Other Payables	2,528	6,428	7,333	6,944					
Other Short-Term Liabilities	1,575	2,126	4,164	4,209					
Long Term Liabilities	2,098	2,263	2,087	1,543					
LT Financial Payables	1,533	1,575	870	315					
Other Long-Term Liabilities	482	551	1,079	1,090					
Equity	3,903	9,962	14,462	18,538					
Minority Interest	0	0	0	0					
TOTAL LIABILITIES AND S.HOLDERS' EQUITY	10,820	21,815	28,916	31,549					

Source: Company Data, INFO Research Estimates

Table 2. DCF Valuation

Our valuation is DCF based with 22% risk free rate, 5% equity risk premium and 27% WACC

DCF	2017	2018	2019	2020	2021	2022E	2023E	2024E	2025E	2026E
EBIT	594	1,618	450	1,021	4,640	8,445	8,445	7,969	9,203	9,583
+ Depreciation & amortisation	140	146	200	225	245	239	396	419	441	457
- Capex	-129	-359	-547	-341	-294	-868	-877	-862	-921	-975
- Change in working capital	0	-998	559	-27	2,031	-1,624	-1,566	137	193	396
- Taxes	-119	-356	-99	-225	-1,160	-1,942	-1,942	-1,833	-2,117	-2,204
- Other										
Free cash flow to firm (FCFF)	487	51	564	654	5,461	4,250	4,456	5,830	6,798	7,257
Discount factor						0.82	0.65	0.51	0.40	0.32
Discounted cash flow for projected period	14,338					3,487	2,878	2,964	2,721	2,287
Discounted cash flow for perpetuity	14,152	KRDMD	KRDMA	KRDMA						
Enterprise value	28,490	19,373	5,983	2,849						
- Last year's net debt	-2,745	-1,867	-577	-275						
- Minority interest	0	0	0	0						
+ Participations	26	18	6	3						
Equity value	25,771	17,524	5,412	2,577						
Implied Price Target (PT)	23									
Potential upside	62%									

Source: Company Data, INFO Research Estimates

Table 4. Peer Multiples

RT Kodu	Şirket Adı	Piyasa Değeri (USD mn)	2022(T)		2023(T)	
			F/K	FD/VAFÖK	F/K	FD/VAFÖK
TKA:DEX	Thyssenkrupp Ag	6,451	5.2	1.3	6.3	1.5
MT:NL	Arcelormittal Sa	30,206	3.4	2.6	5.9	4.1
VOE:AT	Voestalpine Ag	5,818	5.8	4.0	8.6	4.8
SZG:DEX	Salzgitter Ag	2,633	6.8	3.9	7.9	4.7
X:USY	United States Steel Corp	8,039	3.3	2.2	13.1	5.0
CSNA3:BR	Companhia Siderurgica Nacional	7,832	4.8	3.4	7.9	4.2
BSL:AU	Bluescope Steel Ltd	7,519	4.1	2.5	7.6	4.3
EVR:GB	Evrax Plc	1,031	0.7	0.9	1.2	1.4
EREGL:IS	Eregli Demir Celik	8,394	6.3	3.8	7.5	4.8
	Medyan		4.8	2.6	7.6	4.3
KRDMD	Kardemir (D)	1,037	2.7	1.4	2.4	1.4
			76%	87%	222%	215%

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
Thyssenkrupp Ag	-3.4	6.2	0.6	-18.5	0.0	12.0	17.1	11.4	-16.4
Arcelormittal Sa	3.3	7.0	18.5	46.1	0.0	16.9	13.3	29.7	36.2
Voestalpine Ag	-8.1	-0.8	-2.6	-13.8	0.0	6.6	9.3	7.9	-11.5
Salzgitter Ag	25.9	28.1	47.5	58.4	0.0	46.0	41.2	63.3	62.5
United States Steel Corp	29.7	38.8	36.8	76.7	0.0	50.4	53.0	51.5	81.3
Companhia Siderurgica Nacional	14.9	7.0	23.4	-15.0	0.0	4.6	4.3	12.5	-16.9
Bluescope Steel Ltd	2.0	11.3	4.1	18.0	0.0	24.8	37.3	22.1	15.3
Evrax Plc	-91.2	-89.1	-90.7	-89.4	0.0	-90.8	-88.7	-90.7	-90.1
Eregli Demir Celik	20.7	27.4	42.9	145.2	0.0	12.7	24.4	37.1	89.4
Kardemir (D)	46.6	22.2	44.9	83.7	0.0	36.8	22.2	44.9	83.7

Source: Equity RT,

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