

TURKEY– Steel

KARDEMİR

Riding the cycle - Initiating with a Buy

Impressive performance in a tough year. While the Industrial Production Index in Turkey has risen by 10% y/y by the end of 2020 on the back of the government's expansionary fiscal and monetary policies, the overall economic growth has been subdued (up 1.9% y/y) and unevenly spread across the sectors. The manufacturing industries have performed far better compared to the services and construction sectors, where the Main Metal and Machinery Industrial Production Index jumped by 25% y/y as of the end of 2020. Despite the on-going weakness in the construction sector, Kardemir increased its annual sales volume to 2.37 mn tons (up 5.8% y/y) by the end of 2020 mainly on the back of higher sales volumes in round and bar-wire rod products– widely used in machinery manufacturing.

Long steel product prices have increased sharply in the last 6 months. Long steel prices have fallen by as much as 20% y/y in 2Q/2020, as global demand plummeted in the aftermath of the pandemic. However, as wide-spread fiscal and monetary stimulus measures put in place, particularly in the developed economies, helped buoy economic activity in the second half of the year, long steel prices recovered rapidly in the second half of 2020, rising about 60% from the lows of May-2020. The long steel prices continued to rise in Jan-Apr/2021, as vaccinations helped avoid lock-downs and buoyed economic activity globally. Along with a sharp rise in global commodity prices, steel prices rose by another 10% ytd, pushing Kardemir's average product prices up by 50% y/y to USD630 per ton in 1Q/2021. Despite market expectations for a cyclical decline in long steel prices in 2H/2021, China's decision to revive taxes on steel exports and cut tariffs for ferrous imports starting on May 1, 2021, will likely keep steel prices at elevated levels for a prolonged period of time.

Can Kardemir keep up this exceptional performance? Steel prices exhibit high cyclicity depending on the global supply and demand conditions. The most recent long-term up-cycle has started in 2015, where average global long steel product prices have risen from about 300 US/ton in 2015 to 650 USD/ton by the end of 2017. After falling by about 30% at the onset of the pandemic from the peaks seen in 2017, average long product prices (including billet) rose again reaching USD700 by the end of Apr-2021. Despite a concomitant rise in raw material prices (up by 70% y/y), the implied average gross margins (avg. product prices - avg. raw material prices) have risen sharply by 50% y/y to USD250/ton. Accordingly, Kardemir's EBITDA margin per ton shot above USD200 in 1Q/2021. We expect the company's EBITDA margin to remain at these elevated levels in 1H/2021, gradually falling in 2H/2021. We penciled in an avg. EBITDA margin of ~USD170 per ton for 2021E, which might prove conservative given the recent market dynamics. However, due to new global capacity coming online, rising raw material prices and long-term cyclicity of steel prices, we believe the company's EBITDA margins will likely stabilize at about USD110-120 per ton in 2022E-2025E.

That said, in our view, despite the expected long-term fall in steel prices, Kardemir can deliver high single digit sales volumes in 2021-2025 largely on the back of: 1) increasing its liquid steel production capacity (the 6th blast furnace) by about 1.1mn ton/year in 2022-2023 (a 50% increase in capacity from 2.5 mn to 3.8mn tons), 2) shifting its product mix away from low-value added billet to higher value-added products such as wire bar and rod, profiles, railroad tracks and wheels, 3) the expected recovery in the Turkish construction sector in 2022E-2025E after years of stagnation, and 4) supportive global economic backdrop.

We initiate KARDEMİR (KRDMD) coverage with a BUY rating. As we believe the company's recent performance will prove sustainable going forward given the underlying dynamics, we initiate coverage on the stock with a **target price of TL11.00** based on our DCF model. On our numbers, at 3.0x 2022E EV/EBITDA, (35% discount to 5 y avg.) the stock is trading at a 40% discount to its global peers, which we think is unjustified due to 1) **lower leverage**, 2) **high dividend pay-out potential** and 3) **strong top-line growth dynamics**. In our view, investors will likely take notice the positive underlying long-term dynamics beyond the short-term tailwinds.

KARDEMİR*	2018	2019	2020	2021E	2022E	2023E
Net Income (TL mn)	814	81	61	2,161	1,667	1,923
Consensus Net Income (TL mn)	814	81	61	1,716	1,384	1,649
Revenue (TL mn)	5,583	6,076	7,520	13,407	14,834	17,209
EBITDA (TL mn)	1,765	651	1,246	3,589	3,038	3,566
EBITDA (USD per ton)	166	51	75	170	121	119

Source: Company data, INFO Research estimates, *Consolidated figures for KRMD, KRDMA, KRDMB

BUY

Price: TL7.16

Price Target: TL11.00

Company Data

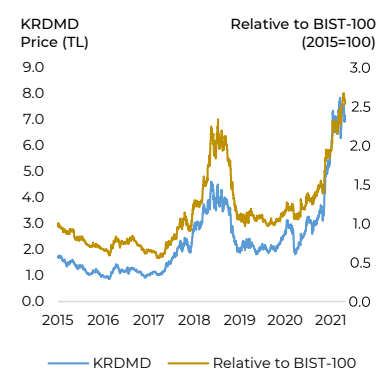
	KRDMD
Stock Ticker	KRDMD
Stock Rating	BUY
Price Target	11.00
Up/downside to PT	54%
Share Price	7.16
52-week range (TL)	2.2 -7.2
No. of shares (mn)	780
Free Float	89%
MCAP (TL mn)	5,586
MCAP (USD mn)	679
EV (TL mn)	6,140
EV (USD mn)	960
Net Debt (TL mn)	554
Net Debt (USD mn)	75
3M ADV (USD mn)	112
3M ADV/FF MCAP (%)	19%

Valuation

	2020	21E	22E	23E
P/E (x)	134.6	3.8	4.9	4.2
EV/EBITDA (x)	7.2	2.5	3.0	2.5
EV/Sales (x)	0.8	0.5	0.4	0.4

Source: INFO Research estimates

Price Performance



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For analyst certification and other important disclosures, refer to the Disclosure Section, located at the end of this report.

Exhibit 1. Financial Summary

Income Statement

(TL mn)	2020	2021E	2022E	2023E
Net Sales	7,520	13,407	14,834	17,209
Cost of Sales	-6,375	-9,842	-11,819	-13,652
Gross profit (loss)	1,144	3,565	3,016	3,557
Operating Expenses	-123	-215	-237	-275
Core EBIT	1,021	3,351	2,778	3,282
Inc.& Exp. from Other Operations	-478	-240	-207	-266
Reported EBIT	544	3,111	2,571	3,015
Financial Income/Expenses	-480	-264	-377	-485
Other income	11	31	26	30
PBT from continuing operations	77	2,881	2,222	2,563
Tax on Continuing Operations	-16	-720	-556	-641
Profit from continuing operations	61	2,161	1,667	1,923
Net Profit	61	2,161	1,667	1,923
EBITDA	1,246	3,589	3,038	3,566

Balance Sheet

(TL mn)	2020	2021E	2022E	2023E
Current Assets	4,932	6,883	9,699	10,374
Cash and Marketable Securities	1,440	1,341	2,967	2,581
ST Trade and Related Receivables	1,300	2,130	2,439	2,829
Inventories	1,820	2,750	3,562	4,114
Other Short-Term Assets	371	662	732	849
Long Term Assets	5,888	6,212	7,050	8,389
Fixed Assets	5,821	6,116	6,943	8,264
Intangible Assets	32	33	37	44
LT Receivables	3	6	7	8
Other Long-Term Assets	32	57	63	73
Total Assets	10,820	13,095	16,750	18,764
Short Term Liabilities	4,818	5,620	6,826	7,783
ST Financial Payables	716	382	873	824
ST Trade and Other Payables	2,528	3,505	4,048	4,862
Other Short-Term Liabilities	1,575	1,732	1,906	2,096
Long Term Liabilities	2,098	1,423	2,205	2,173
LT Financial Payables	1,533	892	1,621	1,531
Other Long-Term Liabilities	482	531	584	642
Equity	3,903	6,052	7,719	8,808
Total Paid-in Capital	1,140	1,140	1,140	1,140
Treasury Stock	-82	-82	-82	-82
Accumulated Profit/Loss	1,195	3,356	5,022	6,112
Reserves and Other Items	1,638	1,638	1,638	1,638
Total Liabilities and Sh. Equity	10,820	13,095	16,750	18,764

Cash Flow Statement

(TL mn)	2020	2021E	2022E	2023E
Earnings before Adjustments	61	2,161	1,667	1,923
Depreciation and Amortization	225	238	259	284
Other Adjustments	480	46	-127	-31
Changes in Working Capital	926	-916	-475	-55
Cash Flow from Operating Activities	1,691	1,528	1,325	2,121
Investing Cash Flow	-292	-503	-1,039	-1,560
Capital Expenditures (CapEx)	-341	-478	-1,033	-1,550
Cash from Other Investment Operations	48	-25	-6	-10
Financing Cash Flow	-173	-945	1,249	-938
Changes in Financial Debt	-221	-972	1,219	-139
Net Cash from Capital Increase /(Decrease)	0	0	0	0
Dividends Paid	0	0	0	-833
Cash from Other Financing Operations	48	27	30	34

Financial Analysis

	2020	2021E	2022E	2023E
Growth (%)				
Sales	23.8	78.3	10.6	16.0
EBIT	126.7	228.1	-17.1	18.1
EBITDA	91.5	188.0	-15.4	17.4
Net Profit	-24.8	3462.2	-22.9	15.3
Margins (%)	0.0	0.0	0.0	0.0
Gross Margin	15.2	26.6	20.3	20.7
EBITDA Margin	16.6	26.8	20.5	20.7
EBIT Margin	13.6	25.0	18.7	19.1
Net Margin	0.8	16.1	11.2	11.2
Efficiency	0.0	0.0	0.0	0.0
Receivables Days	57.8	58.0	60.0	60.0
Inventory Days	102.1	102.0	110.0	110.0
Payables Days	137.1	130.0	125.0	130.0
Opex/Net Sales (%)	1.6	1.6	1.6	1.6
Profitability (%)				
ROA	0.6	16.5	10.0	10.2
ROE	155.4	3570.1	2159.4	2182.8
ROIC	17.1	42.0	29.5	29.4
Leverage (x)				
Asset/Equity	2.8	2.2	2.2	2.1
Net Debt/Equity	0.2	0.0	-0.1	0.0
Net Debt/EBITDA	0.6	0.0	-0.2	-0.1

Key Operating Indicators

	2020	2021E	2022E	2023E
Total Product Sales (mn ton)	2,372	2,403	2,583	2,806
Billet	945	936	954	973
Round	576	576	605	635
Bar and wire rod	434	456	524	603
Profile	352	370	425	510
Rail	56	59	68	78
Other	9.0	7.2	7.3	7.3

Key macro assumptions

	2020	2021E	2022E	2023E
GDP growth, real	1.9%	4.0%	3.0%	3.0%
CPI	14.6%	13.5%	11.0%	10.0%
USDTL, ave	7.0	8.8	9.7	10.7
USDTL, eop	7.4	9.3	10.2	11.2

Valuation

We value KARDEMİR with a DCF valuation utilizing our free cash flows to firm (FCFF) estimates. The key valuation assumptions are as follows:

- 1) Risk-free rate of 18%, in the range of current 10-yr Turkish government bonds,
- 2) Equity risk premium of 7%, a higher rate compared to 5.5-6.0% we use to compensate for market volatility and perceived risks,
- 3) Stock beta of 1.2 based on the last 3-year trading history,
- 4) Terminal growth rate of 10%

KARDMD shares are currently trading at 3.0x of our 2022E EV/EBITDA estimate, This implies a nearly a 40% discount to its global peer averages. We believe the stock should trade at a long-term EV/ABITDA of 3.8x to 4.0x (vs. yr average of 6.5x).

Exhibit 2. KARDEMİR DFC Valuation

DCF	2020	2021	2022	2023	2024	2025
EBIT	1,021	3,351	2,778	3,282	3,639	4,161
- Taxes	16	720	556	641	758	859
=NOPAT	1,005	2,630	2,223	2,641	2,880	3,302
+ Depreciation	225	238	259	284	331	369
- Capex	341	478	1,033	1,550	723	842
- Change in working capital	926	-916	-475	-55	-221	549
Free cash flow to firm (FCFF)	-37	3,306	1,924	1,429	2,709	2,281
Discount factor		0.87	0.70	0.56	0.45	0.37
Discounted cash flow for projected period	7,077	2,863	1,343	805	1,230	835
Discounted cash flow for perpetuity	5,466					
Equity value	12,544		8,585	2,644	1,315	
- Participations	32		22	7	3	
+ Latest net debt	808		553	170	85	
+ Minority interest	0		0	0	0	
Enterprise value	12,544		8,585	2,644	1,315	
Implied Price Target (PT)			11.0	11.0	11.0	
Potential upside			54%	75%	74%	

WACC

Risk free rate	18%
Beta	1.2
Equity risk premium	7%
Cost of debt, after tax	15%
Capitalisation rate	24%
Weighed average cost of capital	24.0%
Terminal growth rate	10%

Source: Company data, INFO RESEARCH estimates

Exhibit 3. KARDEMIR Relative Valuation

BBERG Ticker	Company Name	Country	MCAP (USD mn)	P/E*		EV/EBITDA		EV/SALES	
				2021E	2022E	2021E	2022E	2021E	2022E
TKA GR	Thyssenkrupp AG	Germany	8,322		19.9	1.9	1.3	0.1	0.1
MT Lx	ArcelorMittal SA	Luxembourg	31,924	5.8	8.5	3.8	5.0	0.7	0.7
VOE AV	Voestalpine AG	Austria	7,944		12.3	9.6	5.9	0.9	0.8
SSABA SS	SSAB AB	Sweden	5,702	8.2	11.0	4.8	5.7	0.7	0.7
SZG GR	Salzgitter AG	Germany	1,993	6.6	7.7	3.4	3.6	0.3	0.3
NUE US	Nucor Corp	USA	24,367	7.5	16.8	4.9	8.7	0.9	1.1
CLF US	Cleveland-Cliffs Inc	USA	9,155	5.8	11.7	4.7	7.2	0.9	1.0
X US	United States Steel Corp	USA	6,255	5.5	25.4	3.5	6.3	0.6	0.7
CSNA3 BZ	Cia Siderurgica Nacional	Brazil	13,199	8.1	10.4	5.2	6.5	2.3	2.5
005490 KS	POSCO	Korea	21,346	9.1	9.1	4.4	4.4	0.6	0.6
SAIL IN	Steel Authority of India Ltd	India	5,740	9.4	4.5	6.8	4.7	1.3	1.1
BSL AU	BlueScope Steel Ltd	Austria	8,483	11.3	10.1	6.3	6.1	2.2	2.2
EVR LN	Evrax PLC	UK	13,432	6.8	8.9	4.9	6.1	1.4	1.5
MAGN RM	Magnitogorsk	Russia	9,925	5.9	7.6	3.9	4.7	1.1	1.2
MTLR RX	Mechel PJSC	Russia	430			6.4	20.8	1.1	1.2
NLMK RM	Novolipetsk Steel PJSC	Russia	21,551	7.4	11.3	5.5	7.4	1.9	2.1
CHMF RX	Severstal PAO	Russia	20,052	8.0	11.2	5.5	7.0	2.4	2.7
EREGL TI	Eregli Demir ve Celik	Turkey	8,098	7.3	9.4	4.4	5.3	1.3	1.3
	Median			7.4	10.4	4.8	6.0	1.0	1.1
KRDMD TI	Kardemir (D)	Turkey	940	4.2	5.1	3.0	4.1	0.9	0.8
KRDMA TI	Kardemir (A)	Turkey	940	3.6	4.3	3.0	4.1	0.9	0.8
KRDMB TI	Kardemir (B)	Turkey	940	3.7	4.4	3.0	4.1	0.9	0.8

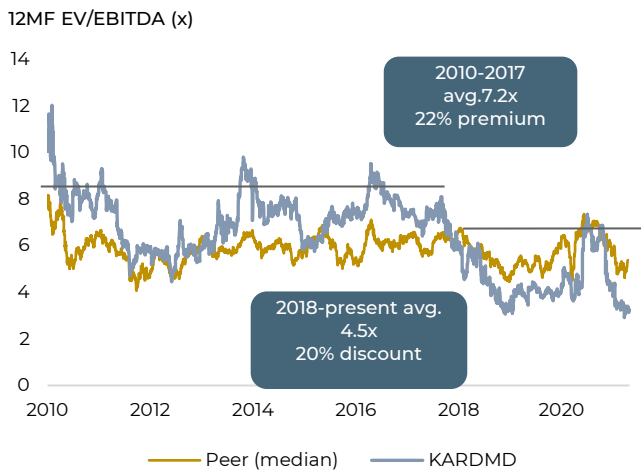
Source: Bloomberg estimates, INFO RESEARCH estimates

Exhibit 4. KARDEMIR Relative Valuation

	Absolute Return in USD Currency				Relative to MSCI EM Index			
	YTD	1M	3M	12M	YTD	1M	3M	12M
thyssenkrupp AG	34	3	15	97	27	-1	17	30
ArcelorMittal SA	-2	2	-1	11	-7	-2	1	-27
voestalpine AG	24	9	22	115	18	4	24	42
SSAB AB	55	11	29	123	47	7	32	47
Salzgitter AG	25	12	28	132	18	7	30	53
Nucor Corp	54	4	68	98	46	0	72	30
Cleveland-Cliffs Inc	26	13	20	290	20	9	22	157
United States Steel Corp	39	-1	31	192	32	-5	34	92
Cia Siderurgica Nacional SA	55	51	71	472	47	45	75	276
POSCO	-2	2	0	9	-7	-2	2	-28
Steel Authority of India Ltd	39	31	78	254	32	26	82	133
BlueScope Steel Ltd	26	11	34	167	20	7	37	75
Evrax PLC	49	19	39	190	41	15	42	91
Magnitogorsk	22	17	31	81	16	12	33	19
Mechel PJSC	-3	18	12	15	-8	14	15	-24
Novolipetsk Steel PJSC	27	19	30	134	21	14	32	54
Severstal PAO	34	26	44	127	27	21	47	49
Eregli Demir ve Celik	31	29	34	130	24	24	37	51
Median	29	12	30	129	22	8	33	50
Kardemir (D)	10	1	-6	166	5	-3	-4	75
Kardemir (A)	-6	1	-4	132	-11	-3	-2	53
Kardemir (B)	7	1	-3	136	1	-3	-1	55
MSCI EM Index	5	4	-2	52				

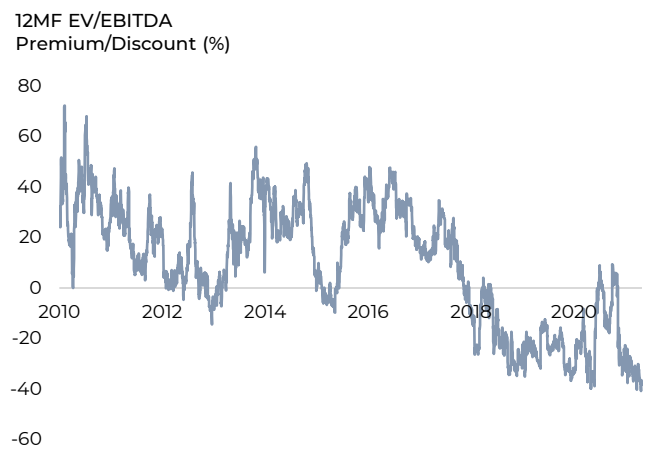
Source: EquityRT, INFO RESEARCH estimates

Exhibit 5. KARDEMIR vs Peers: 12MF EV/EBITDA



Source: Bloomberg consensus

Exhibit 6. KARDEMIR vs Peers: 12MF EV/EBITDA Premium/Discount



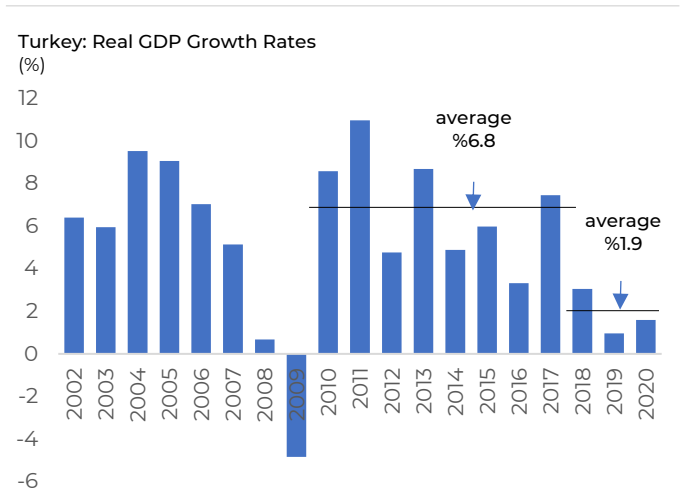
Source: Bloomberg consensus

Risks

- 1) Slower than expected domestic and global recovery in 2021-2023
- 2) Sharper cyclical price and margin declines
- 3) Delays in Kardemir's new capacity investments
- 4) Lower share of export sales in the company's revenues
- 5) Slower medium-term recovery in the domestic construction sector

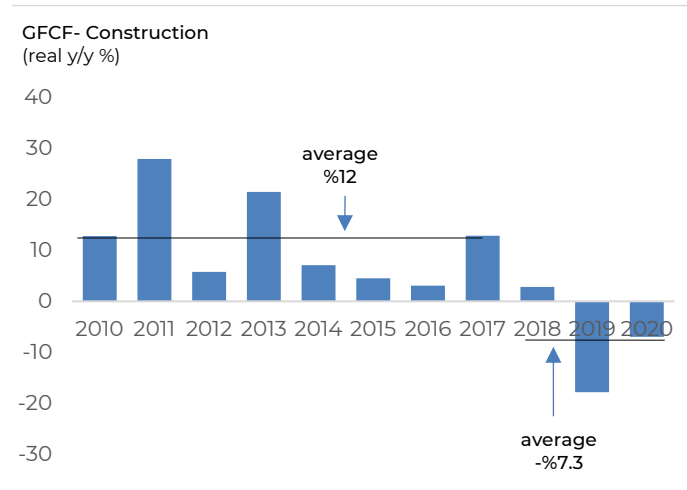
The long-steel demand in Turkey has been adversely impacted by the protracted downturn in the construction sector, which contracted by 7.5% annually in 2018-2020 (**Exhibit 8**). Due to the sharp decline in construction activity, total domestic long-steel consumption has plummeted by 40% to 10.8mn tons by the end of 2019 from its peak of 18.1mn tons in 2017 (**Exhibit 10**). In the aftermath of the pandemic, construction activity has bounced back temporarily on the back of lower mortgage rates and a wide array of monetary and fiscal measures that revived economic activity. Although the pick-up in the construction sector turned out temporary, industrial production continued to grow at a rapid clip. We note that the recovery in the manufacturing industries has been very strong, particularly in metal production and machinery manufacturing industries. The Industrial Production Index in metal and machinery industries recovered by 75% by the end of 2020 from the lows of April-2020. This recovery has extended into 2021 where the production index has risen to peak levels in Feb-2021, increasing by about 20% compared to the –pre-pandemic levels (**Exhibit 9**). On the back of this sharp recovery in the manufacturing industries and a modest recovery in the construction sector, total domestic demand for long-steel products increased by 27% y/y by the end of 2020 to 13.7 mn tons.

Exhibit 7. Turkey: Real GDP growth rates



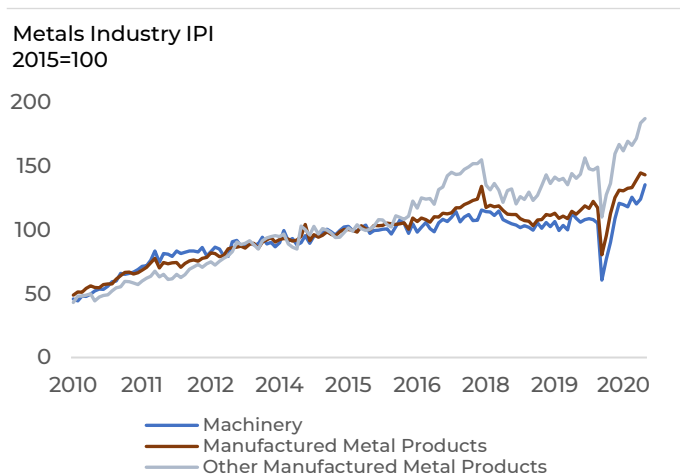
Source: TurkStat

Exhibit 8. Turkey: Gross Fixed capital Formation: Construction



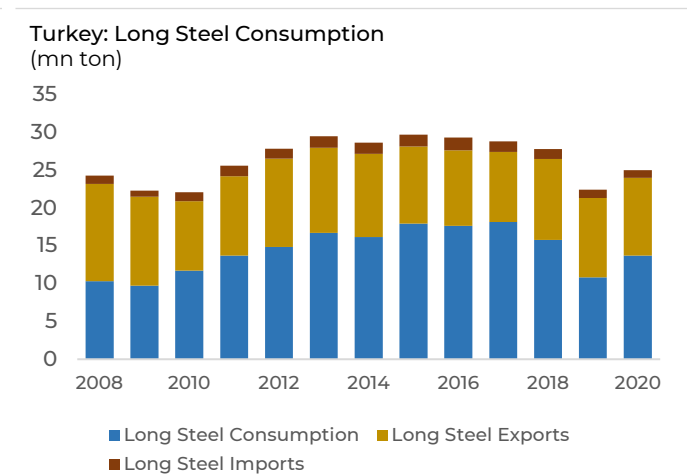
Source: TurkStat

Exhibit 9. Metals manufacturing industry activity bounced back sharply in 2H/2021



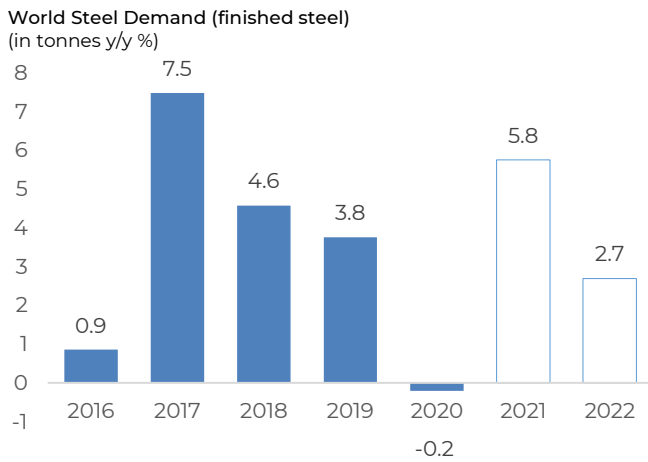
Source: TÜİK

Exhibit 10. Long steel demand has peaked in 2014-2017, falling after 2017 due to slower construction activity



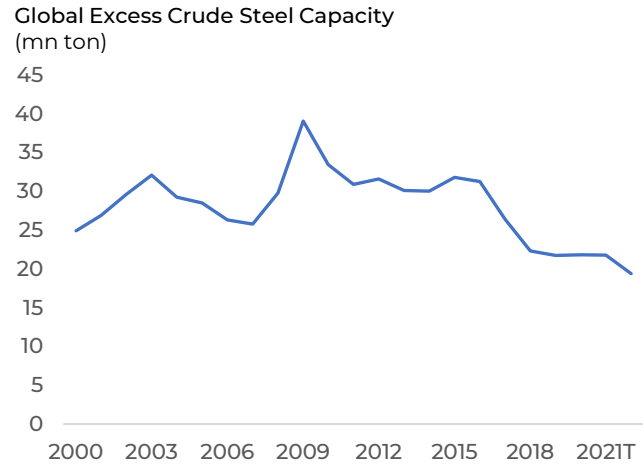
Source: Source: Company data

Exhibit 11. According to the World Steel Organization forecasts, the global steel demand will pick up in 2021-2022



Source: WSO

Exhibit 12. Global excess capacity in crude steel production has declined 50% in 2009-2020



Source: OECD

Although the impact of pandemic on the headline global steel demand was modest (down 0.2% y/y in 2020), the decline in demand has been actually quite large and widespread with China counterbalancing the entire global decline in demand in 2020 (**Exhibit 13**). The Turkish market was one of the few economies where the demand for steel products rose sharply.

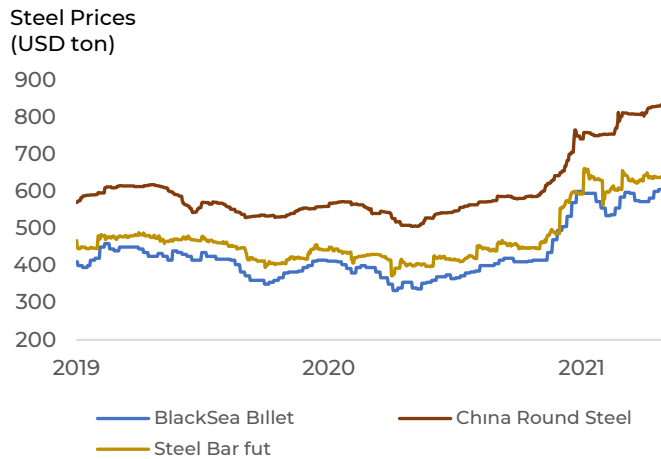
That said, according to the World Steel Organization forecasts, the global steel demand is poised to pick up in 2021-2022 by avg. 4.2 annually. The recovery is expected to be broad-based with the demand EM (ex-China) and DM economies bouncing back by avg. 7.5 annually in 2021-2022.

Exhibit 13. Global steel demand forecasts by region (2021-2022)

mn tonnes	2019	2020	2021F	2022F
World	1,775	1,772	1,874	1,925
World (-ex-China)	863	777	849	890
Developed Economies	393	343	371	386
China	912	995	1,025	1,035
EM and DM (ex-China)	470	434	478	503
ASEAN (5)	78	69	73	78
MENA	69	62	66	69
<i>for info:</i>				
EU (28)	159	141	155	162
y/y/ % change		2020	2021F	2022F
World		-0.2	5.8	2.7
World (-ex-China)		-10	9.3	4.8
Developed Economies		-12.7	8.2	4.2
China		9.1	3.0	1.0
EM and DM (ex-China)		-7.8	10.2	5.2
ASEAN (5)		-11.9	6.3	6.4
MENA		-9.5	6.1	4.1
<i>for info:</i>				
EU (28)		-11.4	10.2	4.8

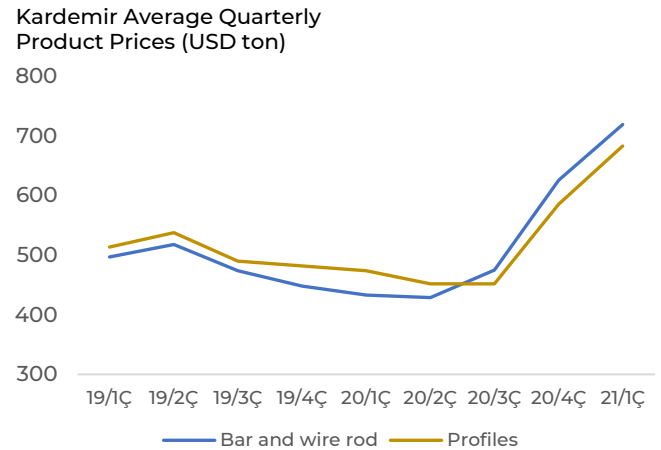
Source: WSO

Exhibit 14. Global long steel prices have increased sharply in the second half of 2020, extending gains into 1H/2021



Source: Bloomberg

Exhibit 15. Kardemir has also benefitted from global product price increases



Source: Source: Company data, Bloomberg

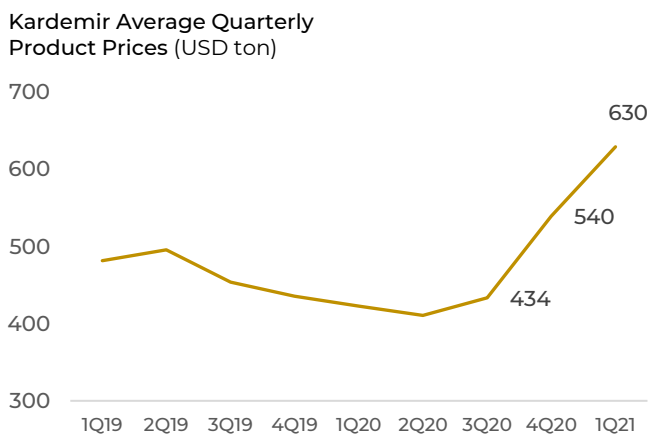
Global long-steel prices have risen sharply in the last 6 months

Long steel prices have fallen by as much as 20% y/y in 2Q/2020, as global demand plummeted in the aftermath of the pandemic. However, as wide-spread fiscal and monetary stimulus measures put in place, particularly in the developed economies, helped buoy economic activity in the second half of the year, long steel prices recovered rapidly in the second half of 2020, rising about 60% from the lows of May-2020 (Exhibit 14).

The long steel prices continued to rise in Jan-Apr/2021, as vaccinations helped avoid lock-downs and buoyed economic activity globally. Along with a sharp rise in global commodity prices, steel prices rose by another 10% ytd, pushing Kardemir's average product prices up by 50% y/y to USD630 per ton in 1Q/2021 (Exhibit 16).

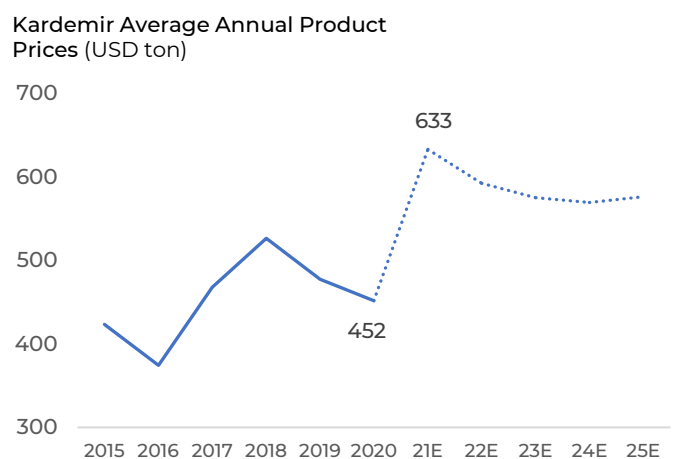
Despite market expectations for a cyclical decline in long steel prices in 2H/2021, China's decision to revive taxes on steel exports and cut tariffs for ferrous imports starting on May 1, 2021, will likely keep steel prices at elevated levels for a prolonged period of time.

Exhibit 16. While Kardemir's average quarterly product prices rose to USD630 per ton 1Q/21...



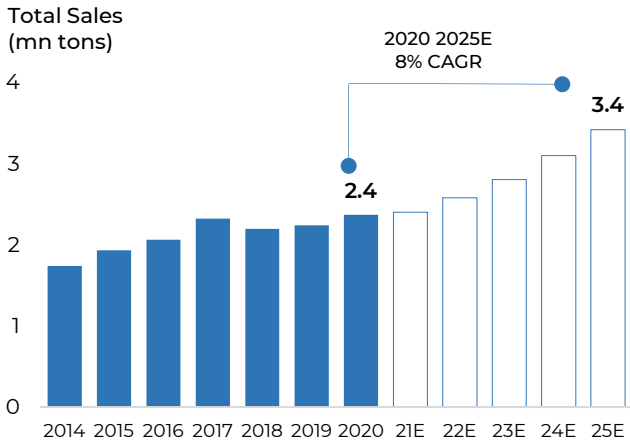
Source: Bloomberg, Source: Company data

Exhibit 17. ... we expect prices to start falling in 4Q/21 levelling at about USD550 per ton in 2022-2025



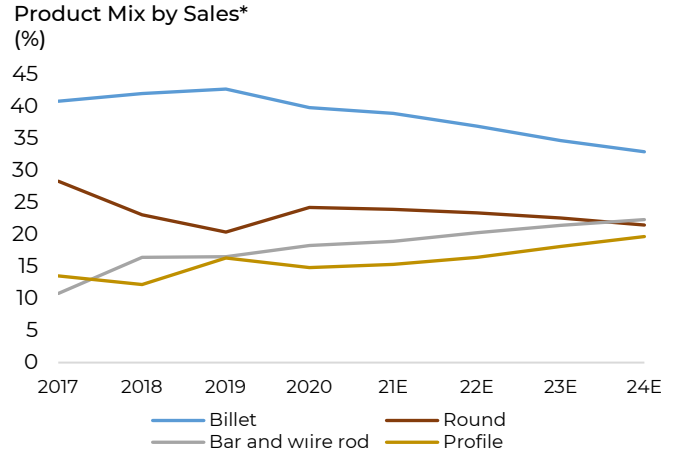
Source: Bloomberg, Source: Company data

Exhibit 18. We expect Kardemir's total sales volumes to increase by 8% CAGR in 2020-2025



Source: Source: Company data, INFO Research estimates

Exhibit 19. Product mix has already started to shift to higher value-added products which will support margins



Source: Source: Company data, INFO Research estimates

Exhibit 20. China round steel prices (2010-2021)



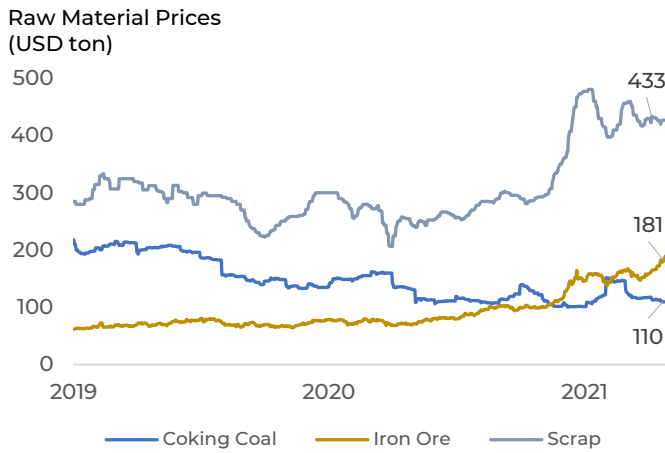
Source: Bloomberg

Exhibit 21. LME Rebar Steel prices (2015-2021)



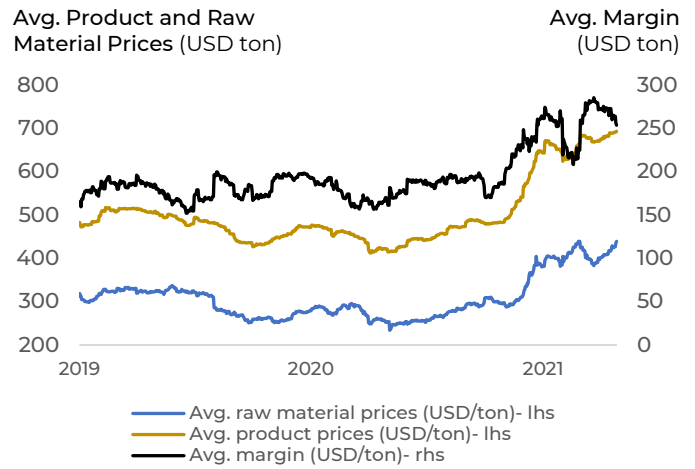
Source: LME Ice

Exhibit 22. Raw material prices have increased significantly in the last 6 months on the back of higher demand, supply-chain interruptions and higher global liquidity



Source: Company data, INFO Research estimates

Exhibit 23. Average Implied gross margins rose to USD200-250 per ton in 1Q/2021 from below USD200 a year ago



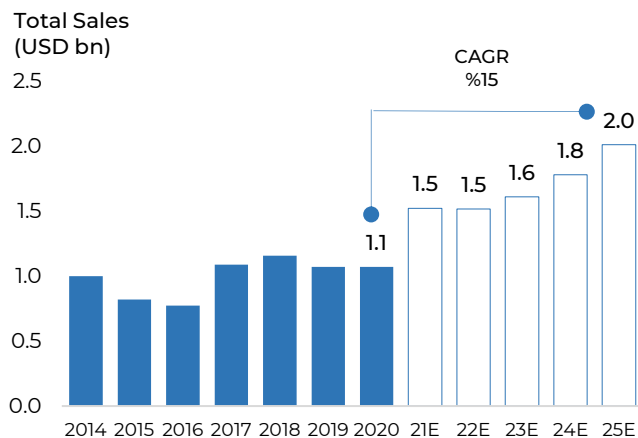
Source: Company data, INFO Research estimates

Steel prices exhibit high cyclical dependency on the global supply and demand conditions. The most recent long-term up-cycle has started in 2015, where average global long steel product prices have risen from about 300 US/ton in 2015 to 650 USD/ton by the end of 2017. After falling by about 30% at the onset of the pandemic from the peaks seen in 2017, average long product prices (including billet) rose again reaching USD700 by the end of Apr-2021.

Despite a concomitant rise in raw material prices (up by 70% y/y), the implied average gross margins (avg. product prices - avg. raw material prices) have risen sharply by 50% y/y to USD250/ton. Accordingly, Kardemir's EBITDA margin per ton shot above USD200 in 1Q/2021. We expect the company's EBITDA margin to remain at these elevated levels in 1H/2021, gradually falling in 2H/2021.

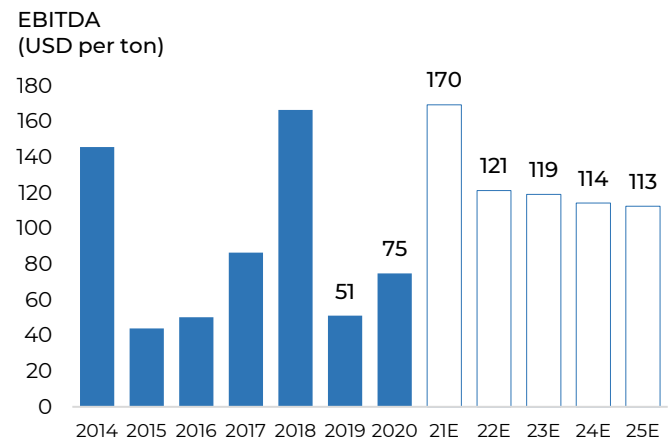
We penciled in an avg. EBITDA margin of ~USD170 per ton for 2021E, which might prove conservative given the recent market dynamics. However, due to new global capacity coming online, rising raw material prices and long-term cyclical nature of steel prices, we believe the company's EBITDA margins will likely stabilize at about USD110-120 per ton in 2022E-2025E (**Exhibit 25**).

Exhibit 24. We expect Kardemir's total sales to increase by 15% CAGR in USD terms in 2020-2025



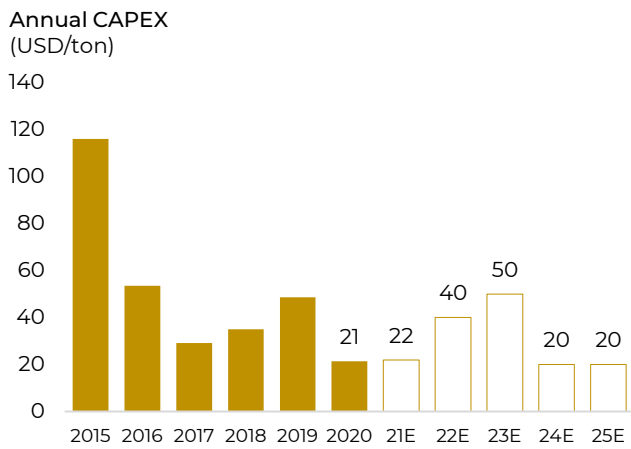
Source: Source: Company data, INFO Research estimates

Exhibit 25. Kardemir's EBITDA margins per ton will likely peak 2021 and stabilize at about 100-110 in the next 5 years



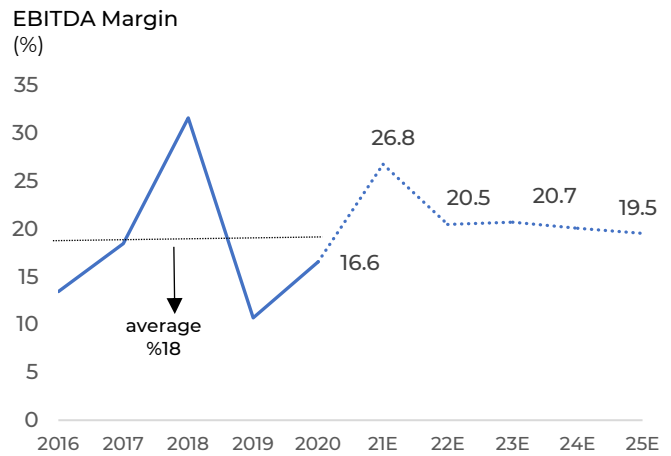
Source: Source: Company data, INFO Research estimates

Exhibit 25. With the planned capacity increase in 2022-2023 (the 6th blast furnace), CAPEX will stay high, but the new investment will add significant new capacity



Source: Company data, INFO Research estimates

Exhibit 26. We forecast the company's sustainable EBITDA margins at avg. 20% in 2022-2025 compared to avg. 18% in 2016-2020



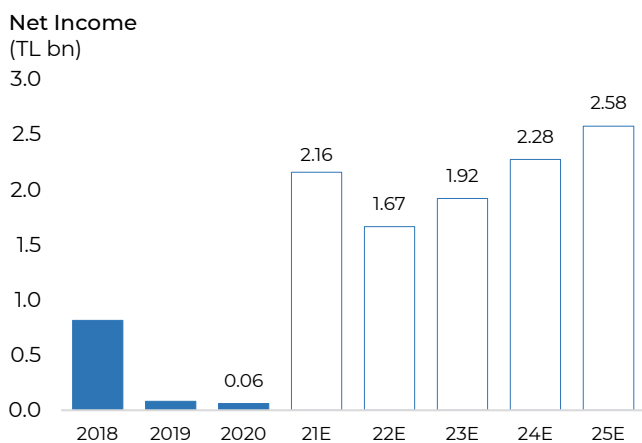
Source: Company data, INFO Research estimates

That said, in our view, despite the expected long-term fall in steel prices, Kardemir can deliver high single digit sales volumes in 2021-2025 largely on the back of: 1) increasing its liquid steel production capacity (the 6th blast furnace) by about 1.1mn ton/year in 2022-2023 (a 50% increase in capacity from 2.5 mn to 3.8mn tons), 2) shifting its product mix away from low-value added billet to higher value-added products such as wire bar and rod, profiles, railroad tracks and wheels, 3) the expected recovery in the Turkish construction sector in 2022E-2025E after years of stagnation, and 4) supportive global economic backdrop.

Based on our financial model, we forecast Kardemir's net income at TL2.16 bn in 2021E, which will likely fall by 23% y/y in 2022 due to cyclical factors. However, given the underlying favorable dynamics, we expect the company to deliver avg. 20% ROE in 2021-2025E.

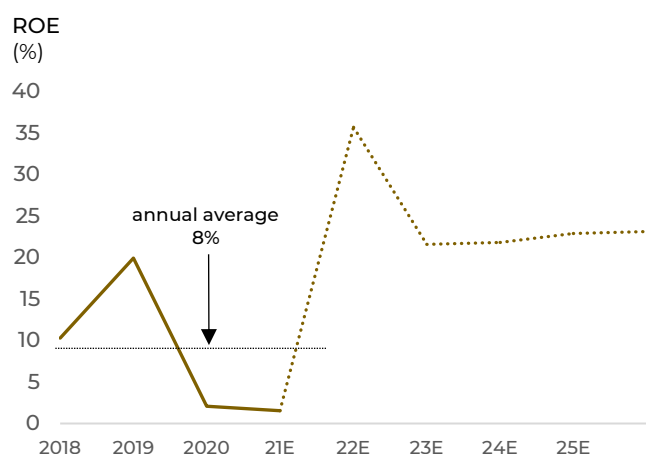
As we believe the company's recent performance will prove sustainable going forward given the underlying dynamics, we initiate coverage on the stock with a **target price of TL11.00** based on our DCF model. On our numbers, at 3.0x 2022E EV/EBITDA, (35% discount to 5 y avg.) the stock is trading at a 40% discount to its global peers, which we think is unjustified due to 1) **lower leverage**, 2) **high dividend pay-out potential** and 3) **strong top-line growth dynamics**. In our view, investors will likely take notice the positive underlying long-term dynamics beyond the short-term tailwinds.

Exhibit 27. Net Income is forecast to top TL2 bn in 2021E on the back of an exceptionally favorable price dynamics



Source: Source: Company data, INFO Research estimates

Exhibit 28. Kardemir's ROE should hover at about avg. 20% in 2021-2025



Source: Source: Company data, INFO Research estimates

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I, Oytun Altaşlı Widmer, hereby certify that the views expressed in this research report accurately reflect the personal views of the INFO Research team, regarding the securities and issuers referred to therein and that no part of their compensation was, is, or will be directly or indirectly related to the specific recommendations or views contained in the research report.

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We employ Discounted Cash Flow (DCF) model and peer multiple analysis to derive at our target prices. Our recommendation methodology is as follows:

Buy: If Target Price is 5 percentage points higher than the estimated Cost of Equity

Hold: If Target Price is within -5 and 5 percentage points of the estimated Cost of Equity

Sell: If Target Price is lower than 5 percentage points of the estimated Cost of Equity

Please note that the analyst's short-term view may occasionally diverge from the stock's longer-term fundamental rating.

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