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## Company Update

## Metals

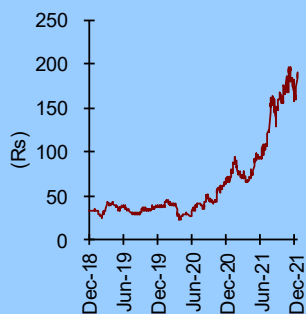
Target price Rs250

## Shareholding pattern

	Mar '21	Jun '21	Sep '21
Promoters	68.1	68.1	68.6
Institutional investors	20.5	20.8	21.0
MFs and others	1.0	1.7	2.6
Insurance Cos.	0.1	0.1	0.3
FII's	19.4	19.0	18.1
Others	11.4	11.1	10.4

Source: BSE

## Price chart



## Jindal Stainless

**BUY**  
Maintained

Look downstream, look converter series – case for value creation intact

Rs178

Decline in Chinese stainless steel prices has compressed the converter spreads (Chart 1). We are not sure when exactly the spot will percolate into Jindal Stainless (JSL) or Jindal Stainless (Hissar) (JSHL) spreads, but we continue to build in ~Rs17,500/te of normalised spreads for FY23/24E (from Rs27,000/te expected in Q3FY22). With ~1mtpa volume expansion underway, we see progressive deleveraging/FCF generation, improvement in consolidated RoCEs (because of significantly lower capex intensity) and improvement in valuation multiples which a converter business model deserves. NCLT approval for merger of JSL and JSHL is awaited. We maintain BUY. We present the key takeaways from our recent management interactions in this report.

- **Cost leadership in 400 series meets domestic demand surge, allowing strong volume visibility in the medium term.** 400 series stainless steel demand continues to move up in India and has increased its volume share from ~15% to ~30% of JSL + JSHL sales in the last couple of years. JSL is also gradually vacating the 200 series market. Process industries (healthcare/chemicals/oil and gas/nuclear), auto, railways have helped 400 series demand grow at healthy double digits (in India). JSL's sales mix has seen Indian Railways expand its share from 4% to 12% over the past 2-3 years; similarly, automobile volume share has doubled in the past three years (from 5% to 10%). Utensils have dropped to 40% of JSL's product mix (from more than 80%), where imports dominate. JSL has clear cost advantage in 400 series, which will eventually move 400 series to be the highest volume contributor progressively.
- **The through cycle EBITDA has moved up to Rs18,000-20,000/te (against spot Rs27,000/te) from ~Rs13,000/te five years back.** This has been driven by i) higher volumes leading to ~ Rs1,500-2,000/te of higher fixed costs absorption as well as better cost efficiency; ii) from 60% of the volumes competing with Chinese imports two years back, as against 25% at present - JSL has gradually vacated 200 series market and increased 400 series in volumes. 400 series witnesses limited import pressures (our interpretation is less Nickel implies more cost effective option for India). The shift in product basket helps improve EBITDA by Rs3,000-3,500/te, iii) **Cost efficiency measures and reduced inventory holding costs through near sourcing have added ~ Rs3,500/te to EBITDA/te.** Cost efficiency measures like improved power plant PLF, improving coal GCV, work on induction furnace, rail sidings have added Rs 2,000-3,000/te to throughcycle EBITDA. Also, from more than 60% of the raw material getting imported previously, JSL has been able to reduce the same to 30%. Reduced working capital along with reduced logistics costs and reduced inventory holding/valuation costs along with reduced forex volatility has also helped EBITDA margins by ~ Rs1500/te.

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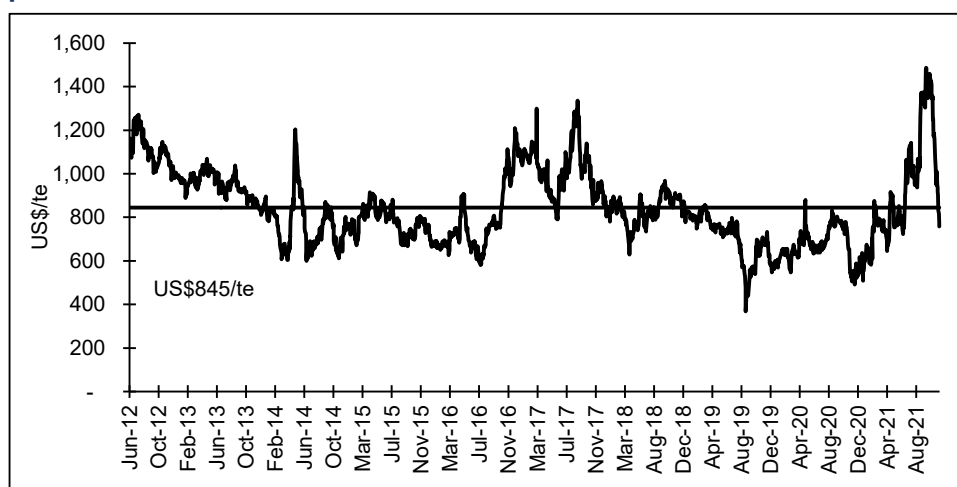
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Market Cap	Rs90bn/US\$1.2bn	Year to Mar	FY21	FY22E	FY23E	FY24E
Reuters/Bloomberg	JIST.BO/JDSL IN	Revenue (Rs mn)	121,885	302,830	279,970	331,200
Shares Outstanding (mn)	504.3	EBITDA(Rs mn)	14,242	45,577	31,796	37,684
52-week Range (Rs)	198/65	Net Income (Rs mn)	4,192	26,098	16,195	20,449
Free Float (%)	31.4	EPS (Rs)	5.1	31.7	19.7	24.8
FII (%)	18.0	P/E (x)	35.0	5.6	9.0	7.2
Daily Volume (US\$'000)	6,821	CEPS (Rs)	10.0	39.9	28.4	34.5
Absolute Return 3m (%)	14.5	EV/E (x)	12.5	3.8	5.0	3.8
Absolute Return 12m (%)	148.8	Dividend Yield	-	-	-	-
Sensex Return 3m (%)	(4.4)	RoCE (%)	7.1	15.7	9.9	10.9
Sensex Return 12m (%)	20.0	RoE (%)	13.1	32.6	16.8	17.5

Please refer to important disclosures at the end of this report

- ▶ **Reducing working capital and operational risks through near sourcing.** Scrap dealer ecosystem is developing in India improving domestic scrap availability. Largest stainless steel scrap is generated in US, Canada and Europe with 40-45 days of voyage time previously exposing JSL to long inventory valuations and forex loss risks. Part of the risk has been passed on to scrap processors, traders who are either opening scrap yards in India like Trafigura or in nearby ports (like ME) with limited transit time.
- ▶ **Risk mitigation through theory of constraints.** JSL monitors Nickel exposure daily while trying to maximise margins through each order booking. Sourcing team has been divided into account managers and given separate geographies to track availability of scrap. As the floating margin exposure because of Nickel crosses ~ Rs6000/te, all booking for Nickel scrap (200/300 series) stops. Manufacturing process is allowed to have a flexibility to move to different product lines (auto/process industry/exports) within 30-40 days and sourcing is accordingly controlled. The requirement has been more pronounced during volume volatility Covid has exposed JSL to.

**Chart 1: Conversion spreads for Stainless steel (300 series) using Chinese prices**



Source: Bloomberg, I-Sec Research

*Conversion margin cyclicality, as per management, is linked to restocking and destocking cycle (of the ecosystem) driven by demand supply, which we have tried to capture in Chart 1. As it normalises, we feel more and more comfortable. This spread has closely correlated with JSL gross spreads in the past.*

## Valuations and key risks

We maintain **BUY** on Jindal Stainless (JSL). We value it at 1.8x FY24E P/B. The P/B multiple is reflective of long-term through cycle RoE of 20%.

### Key risks to business model

#### Political, legal and regulatory risks

We see a possibility of a change in the overall duty structure on key raw materials / finished goods by the Government of India. Further, Jindal Stainless (JSL) has been exporting its products to many countries that have varying degrees of political and commercial instability. Any instability in such countries could impact the company and pose challenges to its overall performance.

#### Disruption risks

JSL operates in a global environment and can be affected by general unprecedented crises such as the recent outbreak of covid pandemic. This crisis has severely impacted economic activity across the globe. The manufacturing industry globally has been under stress as the supply chain was disrupted with restrictions on movement of goods and growing market uncertainty. Unprecedented situations like lockdown may also JSL's impact business. The pandemic also disrupted the domestic and international demand for stainless steel.

#### Rising stainless steel imports from FTA countries

Change in the demand-supply scenario can cause disruptions in the global market, which could have an adverse effect on the company's overall performance. Higher production in Asean countries, as well as China, could pose a threat to the outlook of the Indian stainless steel industry. Indian stainless steel manufacturers are exposed to a threat **of increased dumping of irrationally priced imports**. This scenario of rising imports under FTAs into the country could force Indian manufacturers including JSL to underutilise its capacities.

Increased dumping could lead to a steep rise in channel inventories, which would severely impact the overall pricing in the Indian market and have an adverse effect on JSL's performance.

#### Volatility in key raw materials

JSL is exposed to price changes in some of its key raw materials. This aspect could lead to a scenario of demand deterioration when prices fluctuate. Volatility in these materials could lead to an increase in inventories leading to some impact on the company's performance.

#### Financial risks

JSL's debt servicing capabilities could get affected due to any volatility in financial markets. It could face incremental challenges in a changing interest rate scenario. Further, JSL is also exposed to currency risks due to its considerable imports and exports of goods.

## Financial summary

**Table 1: Profit and Loss statement**

(Rs mn, year ending Mar 31)

	FY20	FY21	FY22E	FY23E	FY24E
<b>Operating Income (Sales)</b>	<b>129,509</b>	<b>121,885</b>	<b>302,830</b>	<b>279,970</b>	<b>331,200</b>
<b>Operating Expenses</b>	<b>118,114</b>	<b>107,643</b>	<b>257,253</b>	<b>248,174</b>	<b>293,516</b>
<b>EBITDA</b>	<b>11,395</b>	<b>14,242</b>	<b>45,577</b>	<b>31,796</b>	<b>37,684</b>
<i>% margins</i>	8.8	11.7	15.1	11.4	11.4
Depreciation & Amortisation	4,252	4,030	6,743	7,221	7,959
Gross Interest	5,855	4,801	4,557	3,519	2,989
Other Income	399	409	500	500	500
<b>Recurring PBT</b>	<b>1,731</b>	<b>6,845</b>	<b>34,777</b>	<b>21,556</b>	<b>27,235</b>
Add: Extraordinaries	44	1,024	-	-	-
Less: Taxes	926	2,702	8,729	5,410	6,836
Less: Minority Interest/Share in profit loss of Equity accounted Investments	13	2	2	2	2
<b>Net Income (Reported)</b>	<b>713</b>	<b>4,192</b>	<b>26,098</b>	<b>16,195</b>	<b>20,449</b>
<b>Recurring Net Income</b>	<b>713</b>	<b>4,192</b>	<b>26,098</b>	<b>16,195</b>	<b>20,449</b>

Source: Company data, I-Sec research

**Table 2: Balance sheet**

(Rs mn, year ending Mar 31)

	FY20	FY21	FY22E	FY23E	FY24E
<b>Assets</b>					
Total Current Assets	38,238	41,180	106,366	108,001	134,985
<i>of which cash &amp; cash eqv.</i>	687	1,163	10,401	18,064	27,978
Total Current Liabilities & Provisions	34,100	34,417	75,919	73,388	85,514
<b>Net Current Assets</b>	<b>4,137</b>	<b>6,762</b>	<b>30,447</b>	<b>34,612</b>	<b>49,471</b>
<b>Investments</b>	<b>1,384</b>	<b>1,126</b>	<b>1,126</b>	<b>1,126</b>	<b>1,126</b>
<i>Strategic/Group</i>	1,359	1,120	1,120	1,120	1,120
<i>Other Marketable</i>	25	6	6	6	6
<b>Net Fixed Assets</b>	<b>61,484</b>	<b>58,281</b>	<b>74,679</b>	<b>81,958</b>	<b>92,971</b>
<i>Capital Work-in-Progress</i>	126	527	12,431	12,431	1,959
Goodwill	1	1	754	754	754
<b>Total Assets</b>	<b>72,675</b>	<b>72,928</b>	<b>126,400</b>	<b>137,897</b>	<b>153,348</b>
<b>Liabilities</b>					
<b>Borrowings</b>	<b>39,029</b>	<b>32,067</b>	<b>35,806</b>	<b>31,106</b>	<b>26,106</b>
Deferred Tax Liability	1,903	4,610	4,780	4,780	4,780
Minority Interest	130	133	135	137	139
Equity Share Capital	975	975	1,647	1,647	1,647
<i>Face Value per share (Rs)</i>	2	2	2	2	2
Reserves & Surplus	26,198	31,077	70,786	86,981	107,430
<b>Net Worth</b>	<b>27,172</b>	<b>32,051</b>	<b>80,151</b>	<b>96,346</b>	<b>116,795</b>
<b>Total Liabilities</b>	<b>72,675</b>	<b>72,928</b>	<b>126,400</b>	<b>137,897</b>	<b>153,348</b>

Source: Company data, I-Sec research

**Table 3: Cashflow statement***(Rs mn, year ending Mar 31)*

	FY20	FY21	FY22E	FY23E	FY24E
<b>Operating Cashflow</b>	<b>11,804</b>	<b>13,078</b>	<b>29,086</b>	<b>29,883</b>	<b>25,903</b>
Working Capital Changes	(59)	(1,806)	(7,762)	3,497	(4,945)
Capital Commitments	(1,968)	(1,678)	(14,500)	(14,500)	(8,500)
<b>Free Cashflow</b>	<b>9,835</b>	<b>11,400</b>	<b>14,586</b>	<b>15,383</b>	<b>17,403</b>
<b>Cashflow from Investing Activities</b>	<b>(1,878)</b>	<b>(1,520)</b>	<b>(14,000)</b>	<b>(14,000)</b>	<b>(8,000)</b>
Issue of Share Capital	-	537	-	-	-
Buyback of shares					
Inc (Dec) in Borrowings	(5,178)	(8,281)	(1,500)	(4,700)	(5,000)
Dividend paid					
<b>Extraordinary /Exchange impact</b>					
<b>Chg. in Cash &amp; Bank balance</b>	<b>18</b>	<b>372</b>	<b>9,029</b>	<b>7,663</b>	<b>9,914</b>

Source: Company data, I-Sec research

**Table 4: Key ratios***(Year ending Mar 31)*

	FY20	FY21	FY22E	FY23E	FY24E
<b>Per Share Data (in Rs)</b>					
EPS(Basic Recurring)	0.9	5.1	31.7	19.7	24.8
Diluted Recurring EPS	0.9	5.1	31.7	19.7	24.8
Recurring Cash EPS	6.0	10.0	39.9	28.4	34.5
Dividend per share (DPS)					
Book Value per share (BV)	33.0	38.9	97.3	117.0	141.9
<b>Growth Ratios (%)</b>					
Operating Income	(4.5)	(5.9)	148.5	(7.5)	18.3
EBITDA	(2.2)	25.0	220.0	(30.2)	18.5
Recurring Net Income	(49.9)	487.8	522.5	(37.9)	26.3
Diluted Recurring EPS	(49.9)	487.8	522.5	(37.9)	26.3
Diluted Recurring CEPS	0.5	65.6	299.4	(28.7)	21.3
<b>Valuation Ratios (x)</b>					
P/E	219.3	35.0	5.6	9.0	7.2
P/CEPS	31.5	17.8	4.5	6.3	5.2
P/BV	5.8	4.6	1.8	1.5	1.3
EV / EBITDA	17.1	12.5	3.8	5.0	3.8
EV / Operating Income	1.5	1.5	0.6	0.6	0.4
EV / Operating FCF	19.8	15.6	11.8	10.4	8.3
<b>Operating Ratios (%)</b>					
Raw Material/Sales	63.5	61.2	64.1	65.4	66.3
SG&A/Sales	23.4	22.8	19.4	21.7	20.9
Other Income / PBT	23.0	6.0	1.4	2.3	1.8
Effective Tax Rate	53.5	39.5	25.1	25.1	25.1
NWC / Total Assets	7.5	5.7	9.3	23.4	24.5
Inventory Turnover (days)	116.5	130.3	114.5	114.3	116.1
Receivables (days)	19.9	28.0	31.3	31.3	30.9
Payables (days)	83.6	90.7	85.2	85.2	85.8
D/E Ratio (x)	1.41	0.96	0.32	0.14	(0.02)
<b>Return/Profitability Ratios (%)</b>					
Recurring Net Income Margins	0.6	3.4	8.6	5.8	6.2
RoCE	5.9	7.1	15.7	9.9	10.9
RoNW	2.6	13.1	32.6	16.8	17.5
Dividend Payout Ratio	-	-	-	-	-
Dividend Yield	-	-	-	-	-
EBITDA Margins	8.8	11.7	15.1	11.4	11.4

Source: Company data, I-Sec research

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