

June 4, 2021

Aggregate capital expenditures remained at the 2019 level amid lower financial indicators of steel companies included in the sample and lower dividend payments.

Do steel companies have excess profits?

Analysis of the dynamics of financial indicators of Russia's largest steel companies based on 2020 and Q1 2021 results

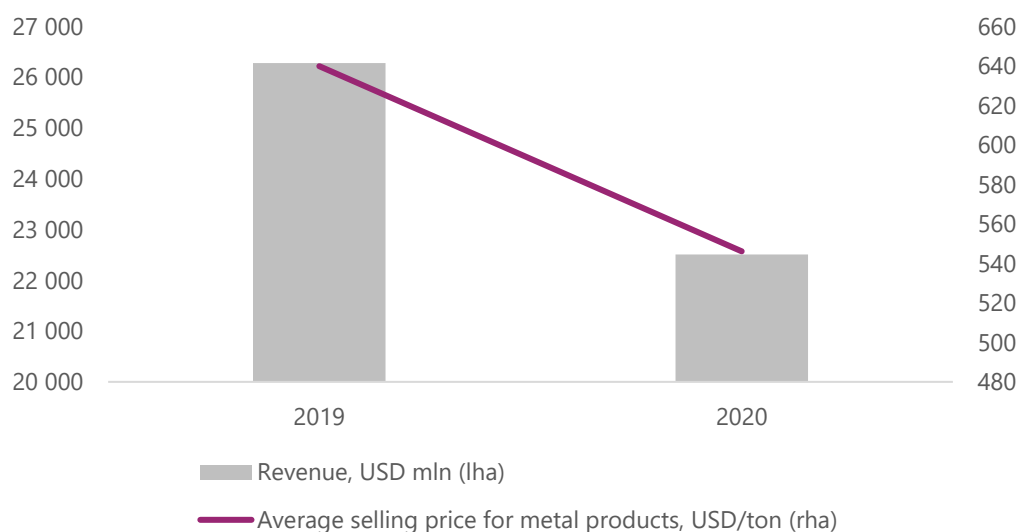
The Russian steel industry was affected by the restrictions imposed in 2020 to fight against the COVID-19 pandemic to a lesser extent and consequently the operating results of the sector's companies did not demonstrate the decline observed in the global steel production. Last year Russia produced 73.4 mln tons of steel (a 2.6% increase on 2019), while global steel production declined by 0.9% year-on-year.

Although total production volume increased last year, from the point of view of internal consumption of steel in Russia, 2020 was a challenging year as it fell by 2.5% (to 41 mln tons). The quarantine restrictions impacted industries that consume products of the metallurgy sector, such as transport, construction, machine building, and pipe manufacturing. Due to this, vertically integrated Russian steel companies that are flexible in terms of their choice of sales markets were able to instead export part of their products in order to maintain capacity utilization and their share in export markets.

On the whole, last year was not an easy one for steel companies, despite higher production. The main reason for this is low prices for steel products in the global market.

Aggregate revenue posted by the three companies of the sector analyzed as part of this research (MMK, NLMK and Severstal) fell by 14% year-on-year in 2020, while the average annual selling price for a ton of products declined by 15% to USD 546 (in 2019, the average price was 4% lower than the 2018 price).

Figure 1. Aggregate revenue and average price for steel products of the three analyzed companies



Source: companies' data

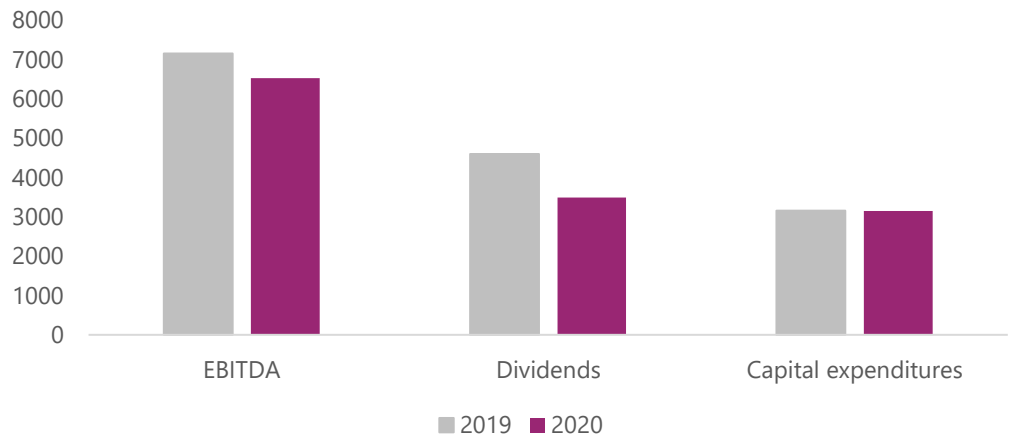
At the same time, the average volume of capital expenditures for the companies of the analyzed sample in 2020 not only did not decrease, but even increased for NLMK and Severstal by 4% and 9%, respectively, compared to the 2019 indicators.

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Figure 2. Consolidated indicators for the three analyzed companies, USD mln



Source: companies' data

Russian steel companies were forced to cut dividend payments to shareholders due to the fall in operating profit. The volume of annual dividends in 2020 decreased by 24% on average for the three analyzed companies.

The results of MMK, NLMK and Severstal for the period from January to March 2021 allow us to be moderately optimistic with regard to the possible recovery of the financial indicators of these companies to the pre-crisis level. This is mainly due to the recovery of global steel prices — in Q1 2021, the average selling price grew by 18% quarter-on-quarter and 20% year-on-year.

Can we say that this recovery is sustainable? Unfortunately, no. There are risks of new waves of the COVID-19 pandemic in the world, as well as the likelihood of a seasonal decrease in demand and prices for steel products as the construction season ends. In addition, the average prices for metal products in 2021 may still turn out to be lower than in 2019, and there is no signs of their recovery to the price level of 2018.

And what about dividends and capital expenditures? The Q1 2021 performance indicators of the companies under review show a significant decrease in dividends. At the same time, the volume of capital expenditures did not decrease as significantly. The aggregate dividend payments of MMK, NLMK and Severstal for the period from January to March this year declined by 65% quarter-on-quarter and 24% year-on-year. However, capital expenditures dropped 20% quarter-on-quarter and 14% year-on-year.

According to the quarterly operating and financial results of the leading Russian steel companies, market volatility has persisted both domestically and globally. The recovery in steel prices in Q1 2021 does not indicate the sustainability of this trend. Consequently, an increase in dividend payments announced by some companies in the industry amid growing financial performance in the first quarter (for example, Severstal approved quarterly dividends of RUB 46.77 per share, which is 71% higher than the dividend for Q1 2020 and to be paid in Q2 2021) speaks of the recovery of financial indicators to pre-crisis levels. In addition, it is important to note that the recovery in steel prices is contributing to an increase in taxes paid to the national budget: the growth of the aggregate income tax for the three analyzed companies in Q1 2021 amounted to 68% quarter-on-quarter and 196% year-on-year.

Table 1. Operating and financial performance of the three analyzed companies

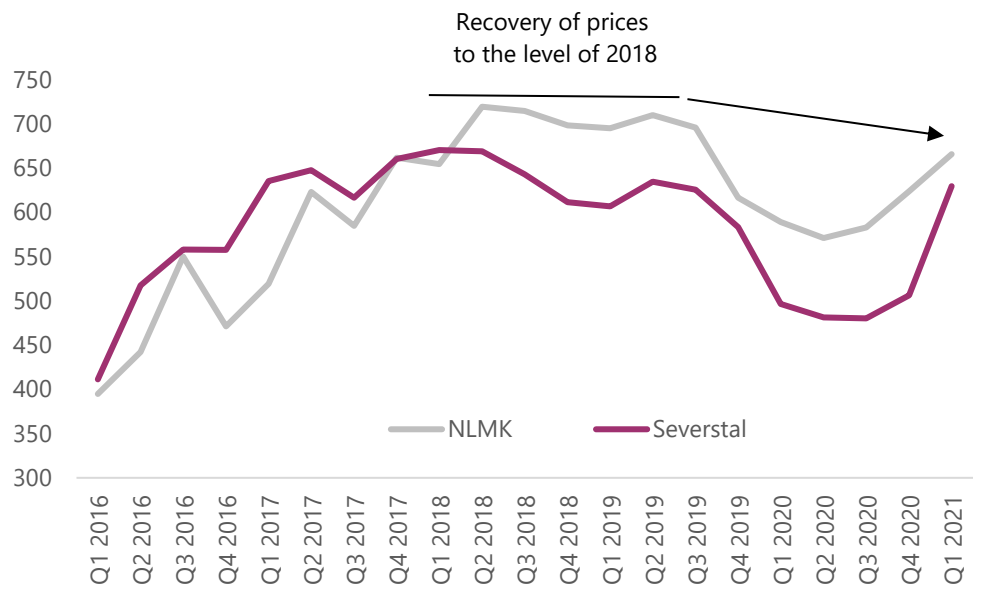
MMK	2018	2019	2020	%, y-o-y	Q1 2020	Q2 2020	Q3 2020	Q4 2020	Q1 2021	%, q-o-q	%, y-o-y
Steel products sold, thousand tons	11,664	11,316	10,755	-5%	2,745	2,223	2,742	3,045	2,904	-5%	6%
Revenue, USD mln	8,214	7,566	6,395	-15%	1,710	1,268	1,565	1,852	2,185	18%	28%
EBITDA, USD mln	2,418	1,797	1,492	-17%	442	226	350	474	726	53%	64%
Dividends*, USD mln	833	907	623	-31%	297	238	1	87	357	310%	20%
Profit tax, USD mln	392	271	156	-42%	39	37	28	52	93	79%	138%
CAPEX, USD mln	871	857	694	-19%	130	176	159	229	142	-38%	9%
Average selling price for metal products, USD/ton	659	627	556	-11%	591	522	535	575	713	24%	21%
NLMK	2018	2019	2020	%, y-o-y	Q1 2020	Q2 2020	Q3 2020	Q4 2020	Q1 2021	%, q-o-q	%, y-o-y
Steel products sold, thousand tons	17,591	17,069	17,520	3%	4,505	4,352	4,443	4,220	3,908	-7%	-13%
Revenue, USD mln	12,046	10,554	9,245	-12%	2,457	2,174	2,229	2,385	2,867	20%	17%
EBITDA, USD mln	3,589	2,564	2,645	3%	594	582	579	890	1,166	31%	96%
Dividends*, USD mln	1,888	2,120	1,637	-23%	308	271	266	792	100	-87%	-68%
Profit tax, USD mln	577	381	285	-25%	53	63	72	97	177	82%	234%
CAPEX, USD mln	680	1,080	1,124	4%	288	219	344	273	232	-15%	-19%
Average selling price of metal products, USD/ton	697	680	592	-13%	589	571	583	624	666	7%	13%
Severstal	2018	2019	2020	%, y-o-y	Q1 2020	Q2 2020	Q3 2020	Q4 2020	Q1 2021	%, q-o-q	%, y-o-y
Steel products sold, thousand tons	10,480	10,667	10,028	-6%	2,371	2,406	2,877	2,229	2,371	6%	0%
Revenue, USD mln	8,580	8,157	6,870	-16%	1,740	1,555	1,852	1,723	2,219	29%	28%
EBITDA**, USD mln	3,112	2,791	2,390	-14%	543	492	651	704	1,021	45%	88%
Dividends*, USD mln	1,971	1,574	1,228	-22%		641	166	421			
Profit tax, USD mln	464	401	229	-43%	41	35	68	85	124	46%	202%
CAPEX, USD mln	688	1,218	1,327	9%	344	331	341	311	278	-11%	-19%
Average selling price of metal products, USD/ton	648	613	491	-20%	496	481	480	506	630	24%	27%
Consolidated data for the three companies	2018	2019	2020	%, y-o-y	Q1 2020	Q2 2020	Q3 2020	Q4 2020	Q1 2021	%, q-o-q	%, y-o-y
Steel products sold, thousand tons	39,735	39,052	38,303	-2%	9,621	8,981	10,062	9,494	9,182	-3%	-5%
Revenue, USD mln	28,840	26,277	22,510	-14%	5,907	4,997	5,646	5,960	7,271	22%	23%
EBITDA, USD mln	9,119	7,152	6,527	-9%	1,579	1,300	1,580	2,068	2,913	41%	84%
Dividends*, USD mln	4,692	4,601	3,488	-24%	605	1,150	433	1,300	457	-65%	-24%
Profit tax, USD mln	1,433	1,053	670	-36%	133	135	168	234	394	68%	196%
CAPEX, USD mln	2,239	3,155	3,145	0%	762	726	844	813	652	-20%	-14%
Average selling price of metal products, USD/ton	668	640	546	-15%	559	525	533	568	669	18%	20%

* According to the cash flow statement.

** ACRA's calculations.

Source: companies' data

Figure 3. Average prices for steel products



Source: companies' data

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