



# STEEL Sector Study

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## A Brief Overview

Steel Industry plays a pivotal role in the progress of an economy. With its permanent nature and recycling capabilities, the demand for steel continues to grow in significant industries such as infrastructure, construction, automotive, appliances, manufacturing and others.

### What is Steel made of?

**Steel** is an alloy of iron and carbon. The carbon content ranges up to 2% (with higher carbon content, the material is defined as cast/pig iron).

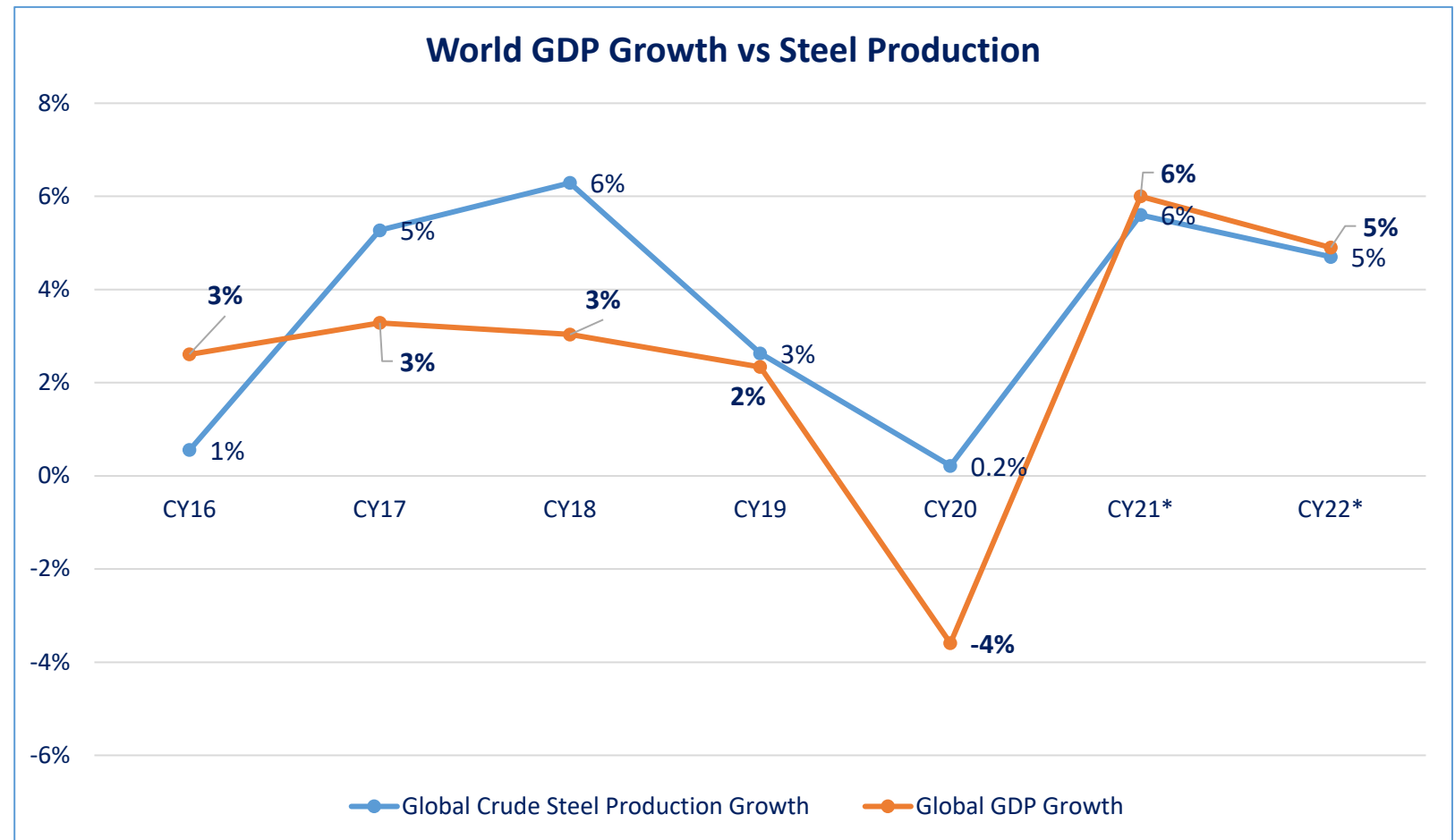
Major Raw Materials used in steel production are **Iron Ore** (a mineral substance which is heated to yield metallic iron), **Coal** (to produce Carbon) and **Steel Scrap** (due to its recyclable nature).

The primary **difference between iron and steel** is that the former is a metal, whereas the latter is an alloy. **Iron** is a metal element that occurs naturally on Earth. In comparison, **steel** is a man-made alloy that's made by mixing **iron** and carbon together.



## Global Overview

- World GDP and Steel Industry have a direct correlation.
- Average growth rate of the Industry from CY15-CY19 was recorded around ~3%. Owing to COVID-19, global steel output contracted by almost ~4% in 1HCY20, but the production rebounded fairly in 2HCY20. Resultantly, global steel production recorded a growth of ~0.2% in CY20.
- As global vaccination drive continues to contain the outspread of the virus and normalize economic activity, world steel output is expected to register healthy growths of ~6% and 5% in CY21 and CY22 respectively.

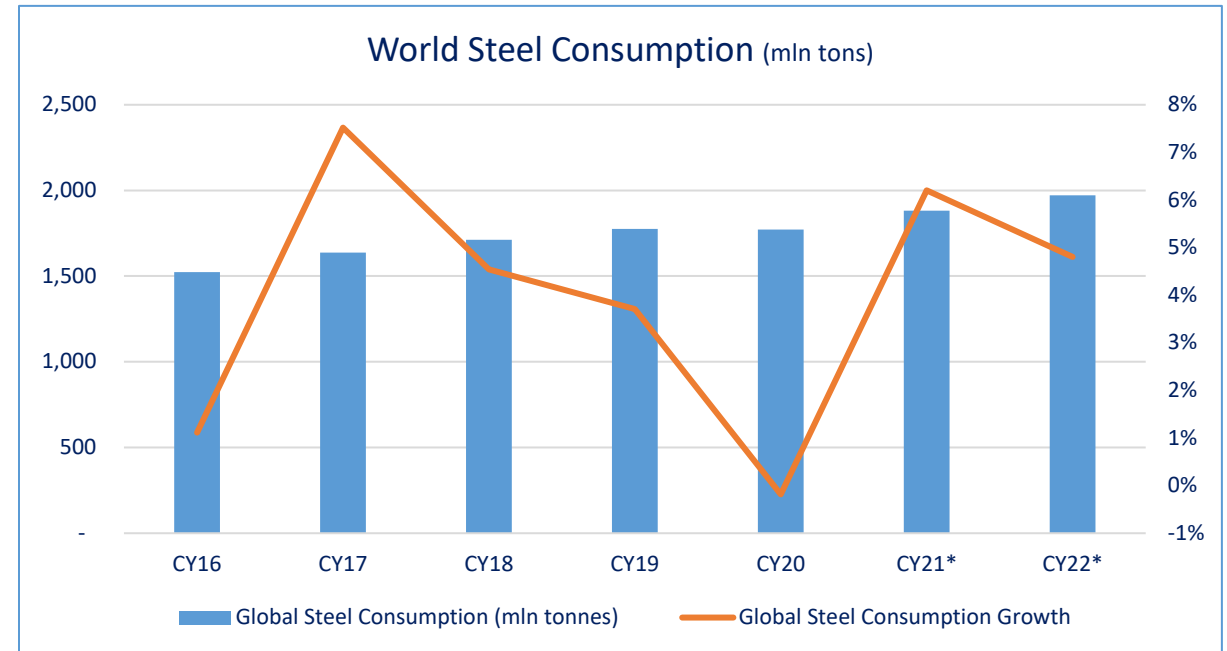
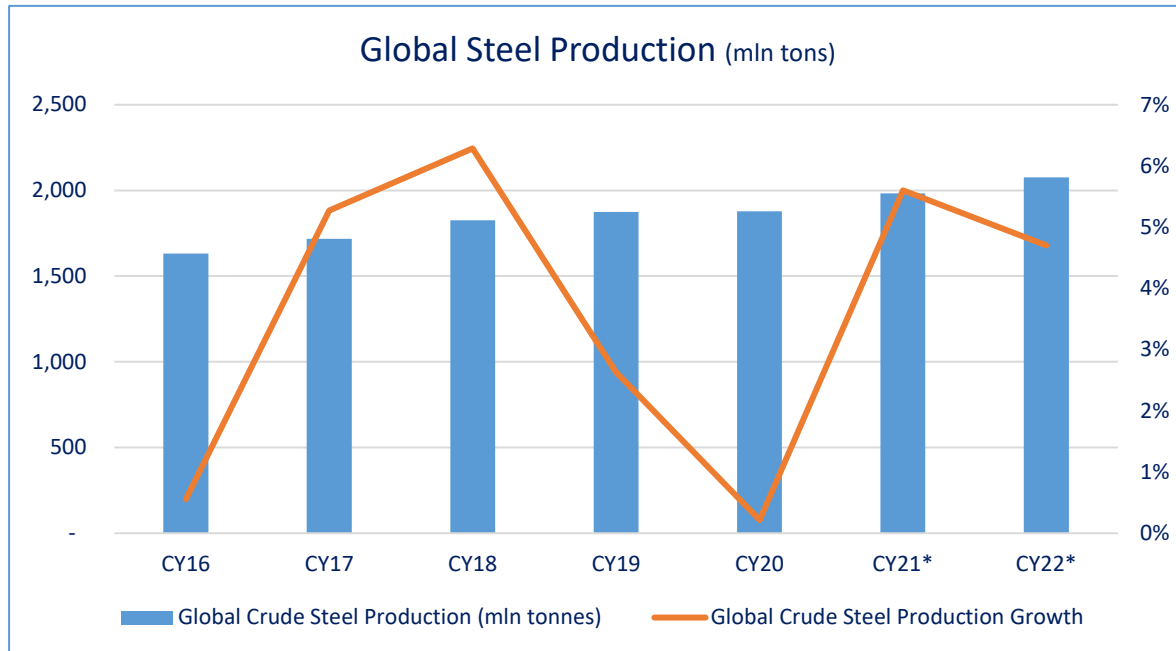




# STEEL

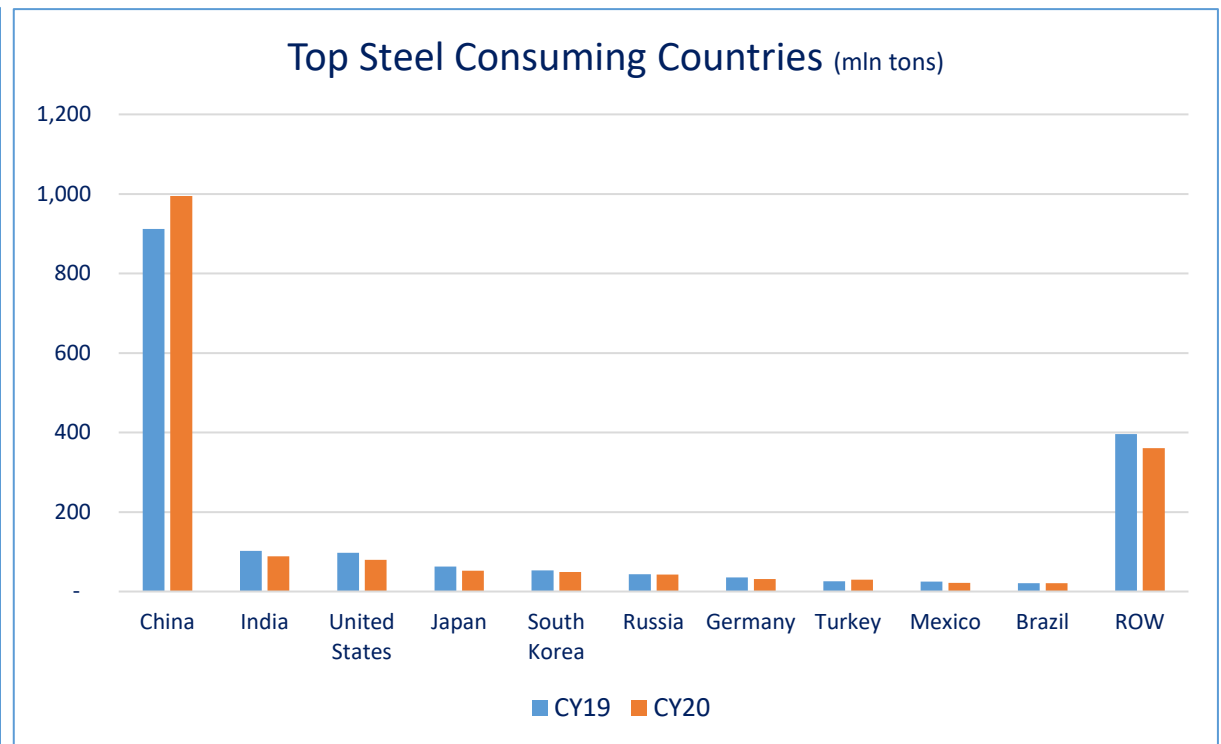
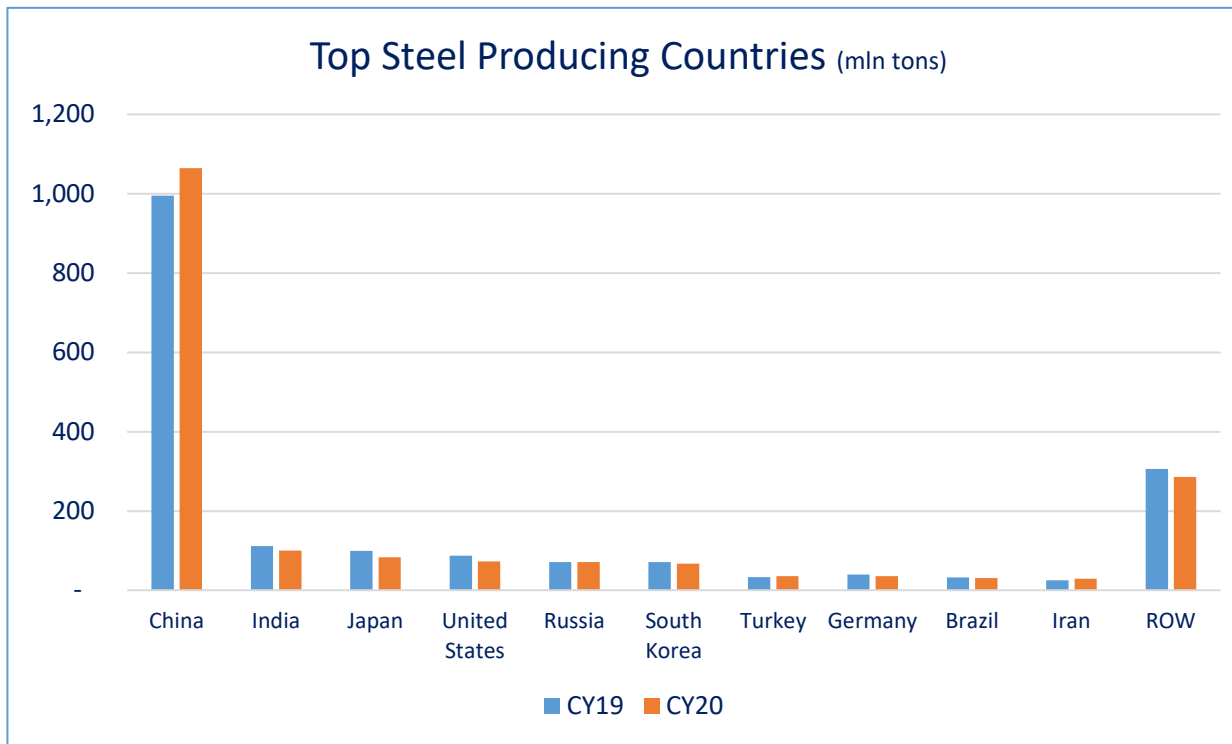
## Global Production & Consumption

- Decrease in global steel consumption in CY20 was led by slowdown in China and significant consumption decrease in Europe and North America. China, world's largest steel consumer, registered a consumption growth of ~4.5 in CY20 (CY19: ~9.0%). Consumption in Europe decreased by ~18% in CY20 (CY19: ~-3%). Manufacturing accounts for ~60% of total steel consumption, this demand driver has been in recession since 2019, and the pandemic further reinforced this trend.
- The US accounts for ~75% of steel consumption in North America. According to American Iron and Steel Institute (AISI), in 2018 ~43% of steel was consumed by construction sector, ~27% by automotive sector and ~10% in fuel and power complex. Slumping energy prices in CY20 have affected direct investments and related construction business. Automotive plant remained close for 6 weeks during CY20.



## Top Countries

- World Steel Production has a stark outlay. It is clearly China and Rest of the World (ROW). China accounted for ~57% of global production in CY20 (CY19: ~53%). ROW is fragmented in many countries. The second largest producer, India, constituted ~6% of total production in CY20 (CY19: ~5%).
- China is also the largest consumer of steel products as the country made up ~56% of total world consumption in CY20 up from ~51% in CY19.



## Global Per Capita Consumption

- Average World per capita consumption of steel is recorded around ~230Kgs. The highest per capita consumption is recorded in South Korea (~955kgs) while the lowest is recorded in Venezuela around ~3Kgs. Pakistan's per capita consumption of steel (~49Kgs) is way lower than the world average as well as lower than its regional country, India, but slightly above Bangladesh (India: ~64Kgs, Bangladesh: ~45Kgs).

Global Steel Consumption (Kg/Per capita)						
Sr #	Company	CY16	CY17	CY18	CY19	CY20
1	South Korea	1,120	1,102	1,050	1,039	955
2	China	482	545	586	636	691
3	Japan	487	505	514	498	416
4	Germany	492	496	477	421	371
5	Turkey	427	445	372	313	350
6	Poland	346	358	393	360	340
7	Italy	391	410	417	413	329
8	Canada	367	382	381	347	323
9	Russia	267	282	284	299	291
10	Spain	270	284	296	283	250
11	World	204	217	225	230	228
12	<b>Pakistan*</b>	54	62	53	42	49

## Global | Top Steel Producing Companies

- World Steel Sector can be termed fragmented since top 10 Companies (majorly origin being China) account for ~27% of the Global Production, meanwhile top 20 Companies make up ~39% of the market share in terms of production.

Top Steel Producing Companies (mln tons)				
Sr #	Company	Country	CY20	% Share
1	China Baowu Group	China	115	6%
2	ArcelorMittal	Luxembourg	78	4%
3	HBIS Group	China	44	2%
4	Shagang Group	China	42	2%
5	Nippon Steel Corporation	Japan	42	2%
6	POSCO	South Korea	41	2%
7	Ansteel Group	China	38	2%
8	Jianlong Group	China	36	2%
9	Shougang Group	China	34	2%
10	Shandong Steel Group	China	31	2%
11	Companies Ranked 11-20	China, India, Japan, USA, South Korea, Iran	223	12%
	Others		1,154	61%
<b>Total Production</b>			<b>1,878</b>	<b>100%</b>



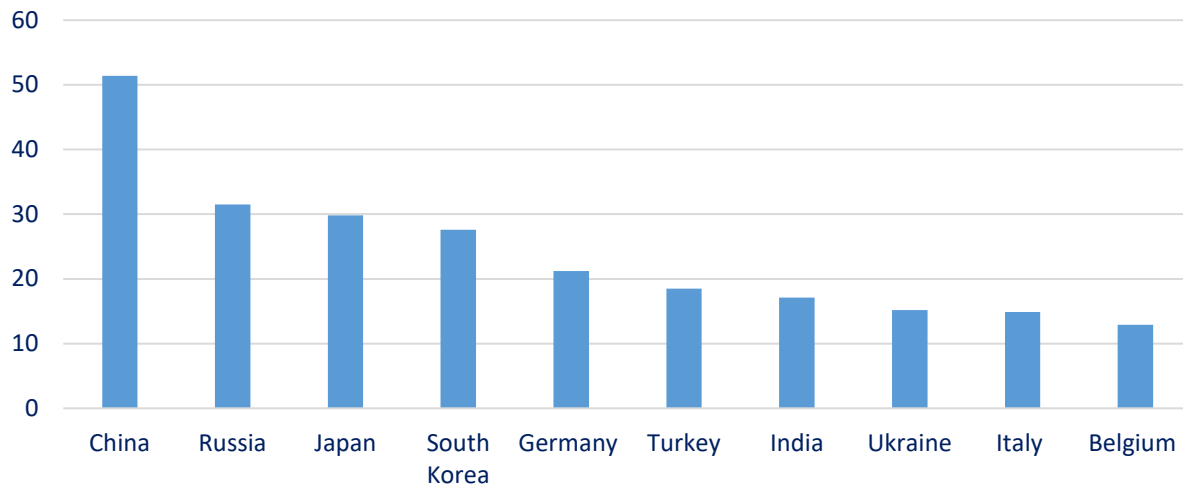


## Global Trade | Gross

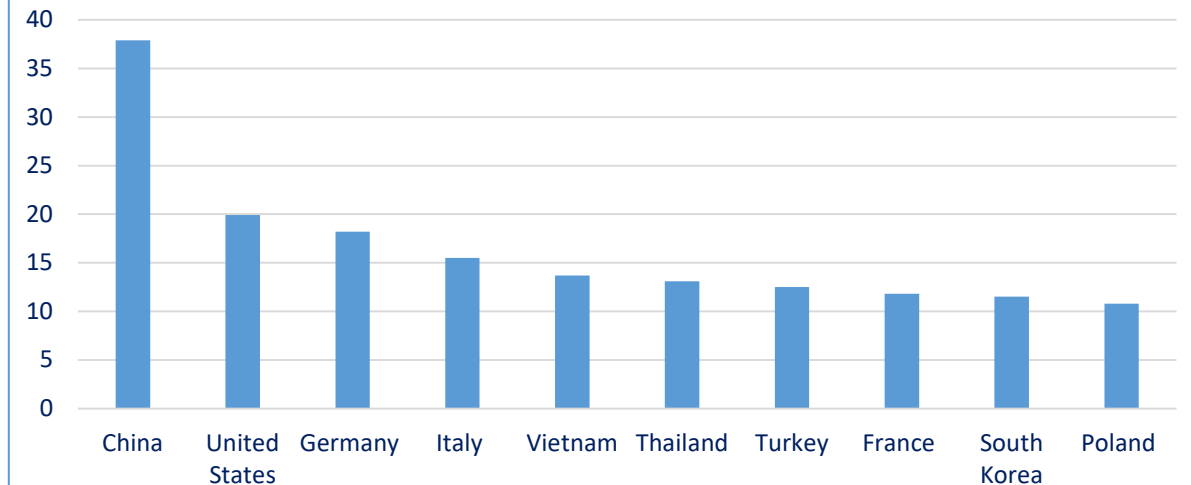
Volume in mln tons	CY16	CY17	CY18	CY19	CY20
Export Volume	477	463	457	439	401
Total Finished Steel Production	1,522	1,619	1,702	1,747	1,751
Trade Volume as % of Total Production	31%	29%	27%	25%	23%

- Steel is a moderately traded commodity with ~23% of world consumption met through Exports/Imports. China is the largest exporter and importer of steel on gross basis.

Top Steel Exporters | CY20 (mln tons)



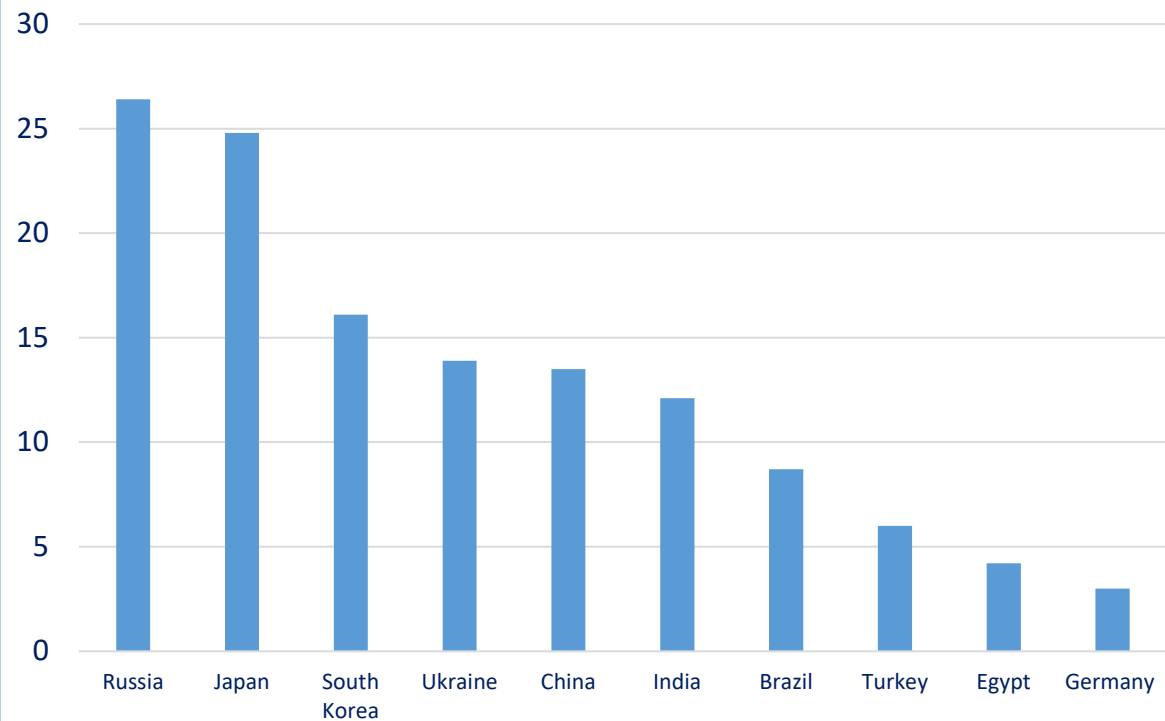
Top Steel Importers | CY20 (mln tons)



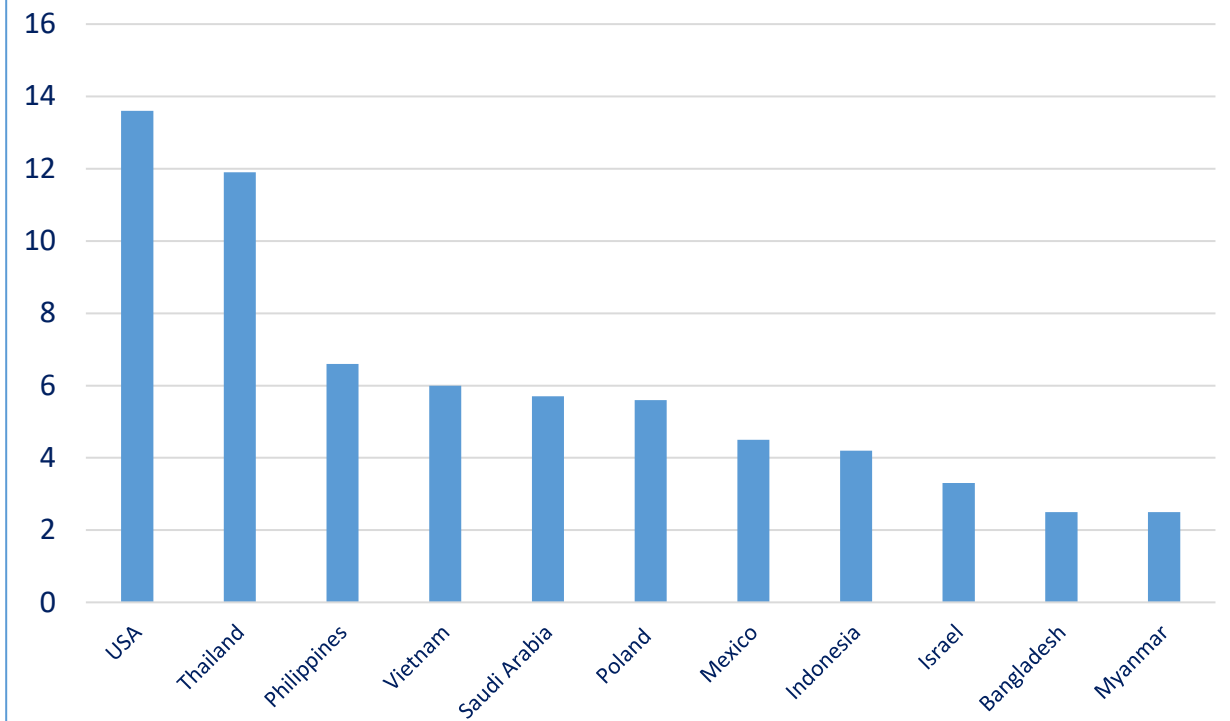
## Global Trade | Net

- Russia is the largest net exporter of steel products in the world as the country's net export was recorded at ~26.4mln tons in CY20. Whereas, USA is the world's largest net importer with net imports of ~13.6mln tons in CY20.

### Net Steel Exporters | CY20 (mln tons)

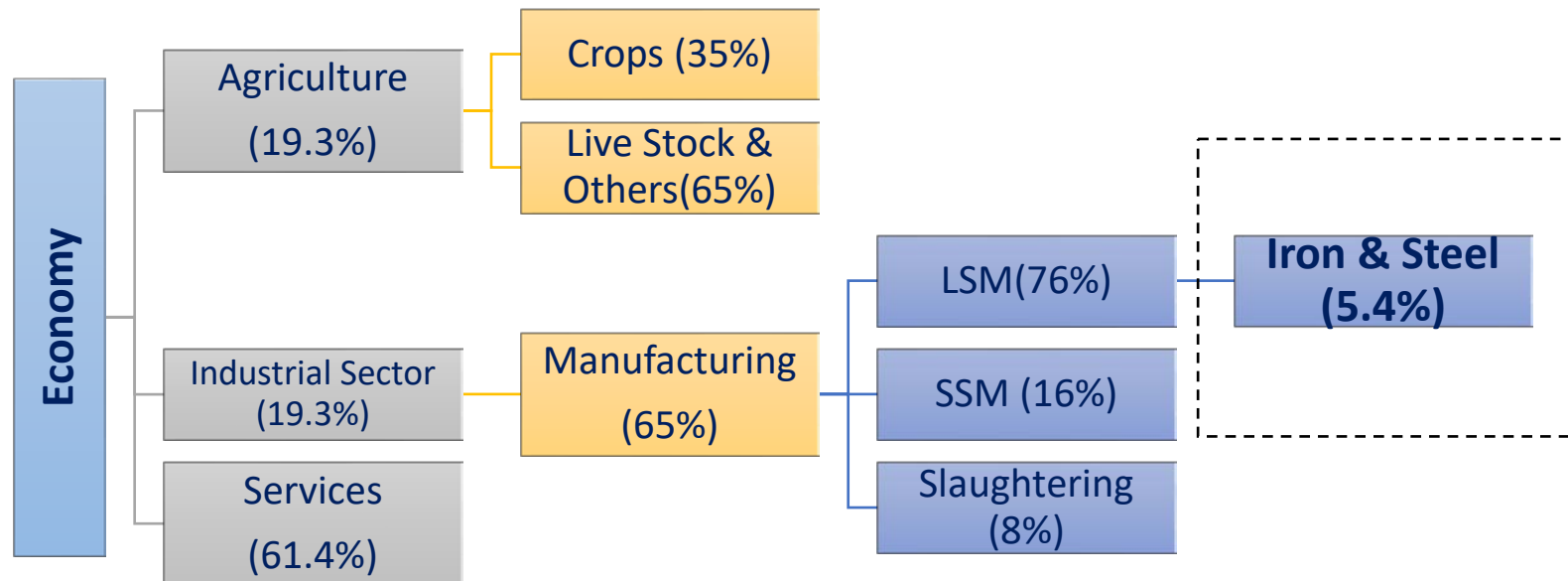


### Net Steel Importer | CY20 (mln tons)



## Large Scale Manufacturing (LSM) | Overview

- The Large Scale Manufacturing (LSM) is a significant component of the Manufacturing Segment of the Industrial sector. It is considered essential for the country's economic growth considering its strategic importance and linkages with other sectors of the economy. It contributes ~9.5% to the GDP. The Steel Sector, bearing notable weightage in LSM, holds a share of ~5.4% in its composition.
- In FY21, the country's GDP registered a V-shape growth recovery of ~3.9% after witnessing a contraction of ~0.4% in FY20. This was attributed to a steady pickup in economic activities post COVID-19 lockdown in 4QFY20. The growth rate surpassed the targeted growth of 2.1 percent, for the outgoing fiscal year.
- The Government of Pakistan (GoP) and SBP announced series of incentives during 4QFY20 to support businesses and to stimulate business activity. The stimulus measures yielded positive results for the economy as the LSM posted a growth of ~14.9% during FY21 (FY20: ~-9.8%). The GoP has set an economic growth target of ~4.8% for FY22.



## Local | Industry Snapshot

- Pakistan Steel Sector is largely fragmented with over ~170 players registered with The Pakistan Steel Re-Rolling Mills Association. Key players in the Industry are, however, less than 20 in number, yet account for over ~40-50% production capacity of the sector. Out of these, 12 players are listed on the PSX.
- Pakistan steel sector is majorly driven by private corporates. Pakistan Steel Mills (PSM) – a state owned giant with a capacity of 1.1mln tons has been offline since June 2015.
- The country’s annual steel products’ demand hovers around ~11mln tons (FY21). Steel products are broadly classified into long & flat products and tubes & pipes. Almost ~73% of the country’s demand is met through local production, while the remaining portion is imported.
- The major raw materials used in steel industry is steel scrap. Pakistan is an importer of raw iron and steel scrap, although, the country produces Iron ore (less than a million ton in a year). On the other hand, Pakistan also imports finished steel products (as stated above) to fulfill the country’s demand.

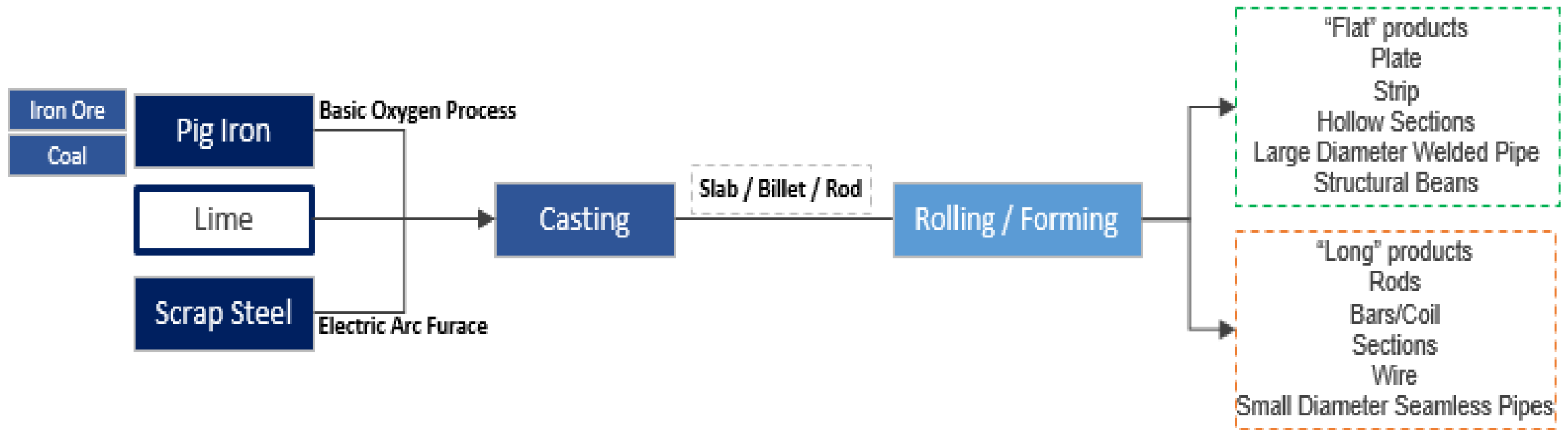
Overview	FY20	FY21
Sector Valuation* (PKR bln)	69.6	162.9
Sector Growth (production)	-17.4%	15.6%
Billet/Ingots Growth	-18.3%	50.9%
Coils & Plates Growth	-16.6%	-9.8%
Structure	Fragmented (12 companies listed on PSX)	
<b>Consumption (mln tons)</b>	<b>9.3</b>	<b>11.1</b>
Local Production (mln tons)	6.8	8.1
Import (mln tons)	6.4	7.7
Import (PKR bln)	482.9	609.6
Regulator	Securities and Exchange Commission of Pakistan (SECP)	
Associations	Pakistan Steel Melters & Re-Rolling Association	

\*Listed Steel Companies

# STEEL

## Production Process

A brief overview of Steel production process is illustrated below. In the first stage, crude steel/semi-finished products are produced, from which final products - flat and long products are manufactured.





## Major Steel Products

- **Long Steel Products:**

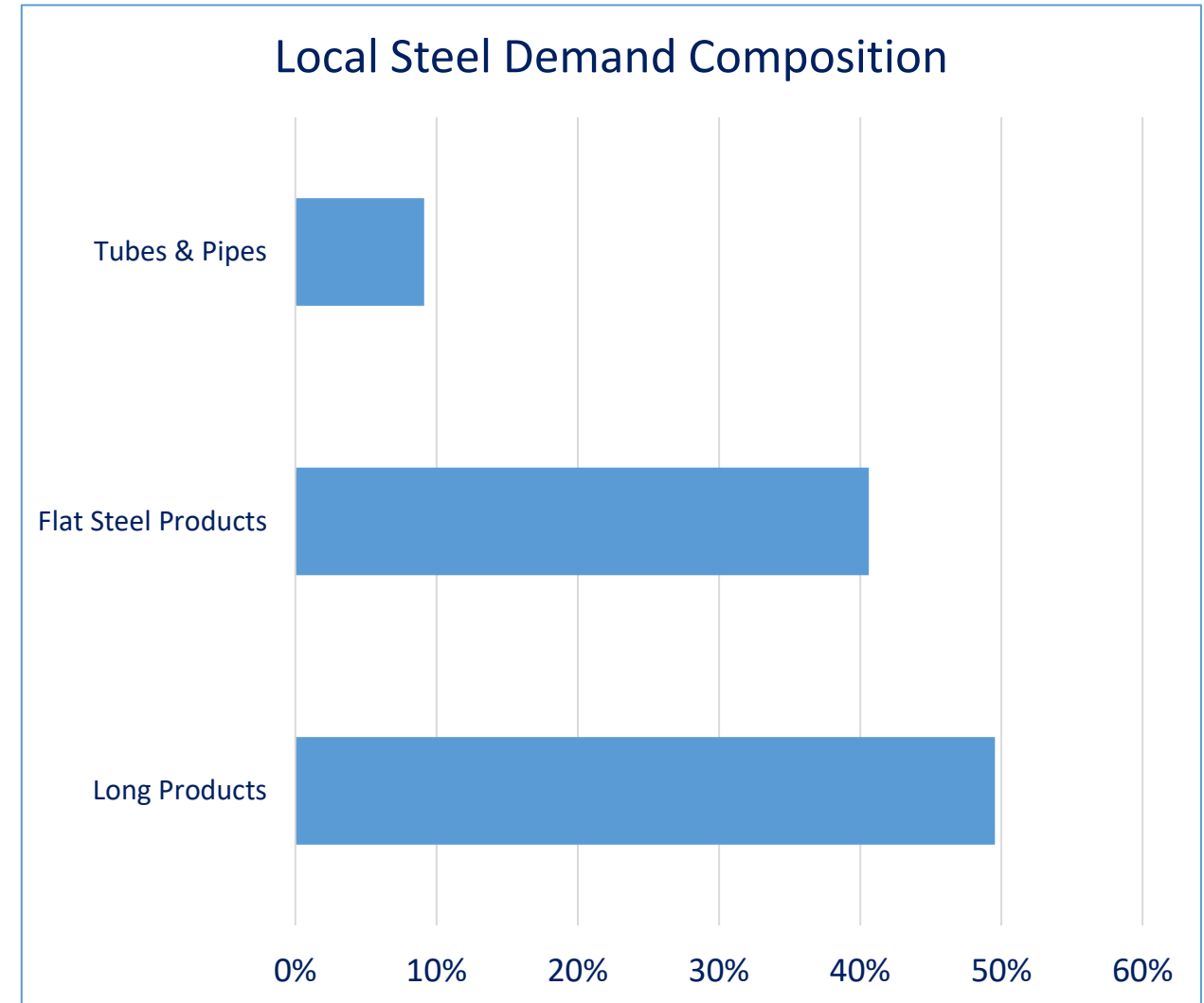
The term long steel refers to the products made from billets and blooms, which are mainly used in the construction sector. Usually, they are made through EAF furnaces. Long steel products include rebar, wire rod, merchant bars, rails and sections.

- **Flat Steel Products:**

Flat steel products consist of sheets and plates. They are rolled from slabs, which are a semifinished steel product. These products are used in a wide range of industries such as automobile, domestic appliances, and construction.

- **Tubes & Pipes:**

Steel tubes & pipes are most commonly used to transport products such as oil, gas, and water, and are suitable for long-term installations. The demand is driven by large engineering projects.





# STEEL

## Product Portfolio

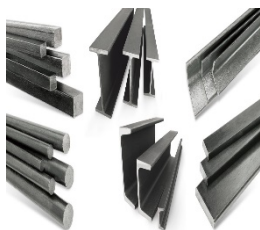
### Common Long Steel Products:



Rebar



Wire Rods



Merchant Bars



Rails

### Common Flat Steel Products:



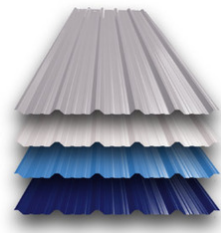
Plates



Hot Rolled Sheets



Cold Rolled Sheets

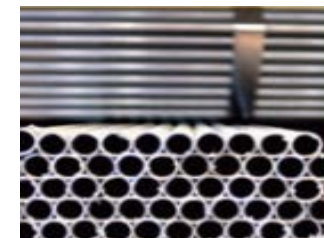


Coated Sheets

### Steel Pipes & Tubes:



Galvanized Iron Pipes



CRS Tubes

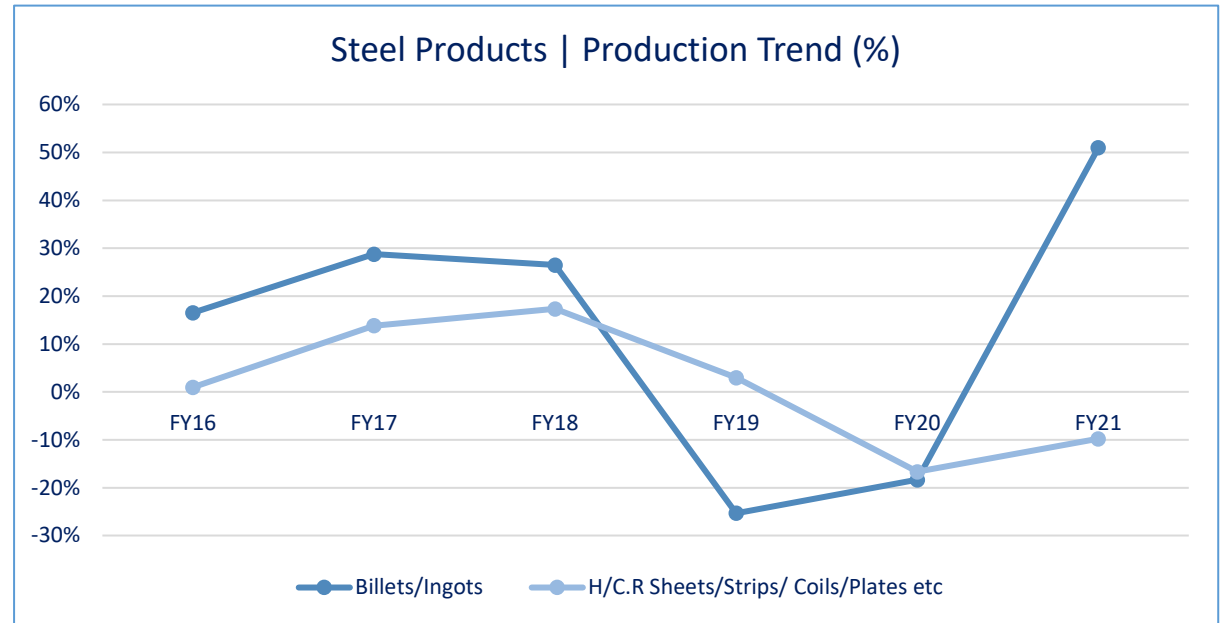
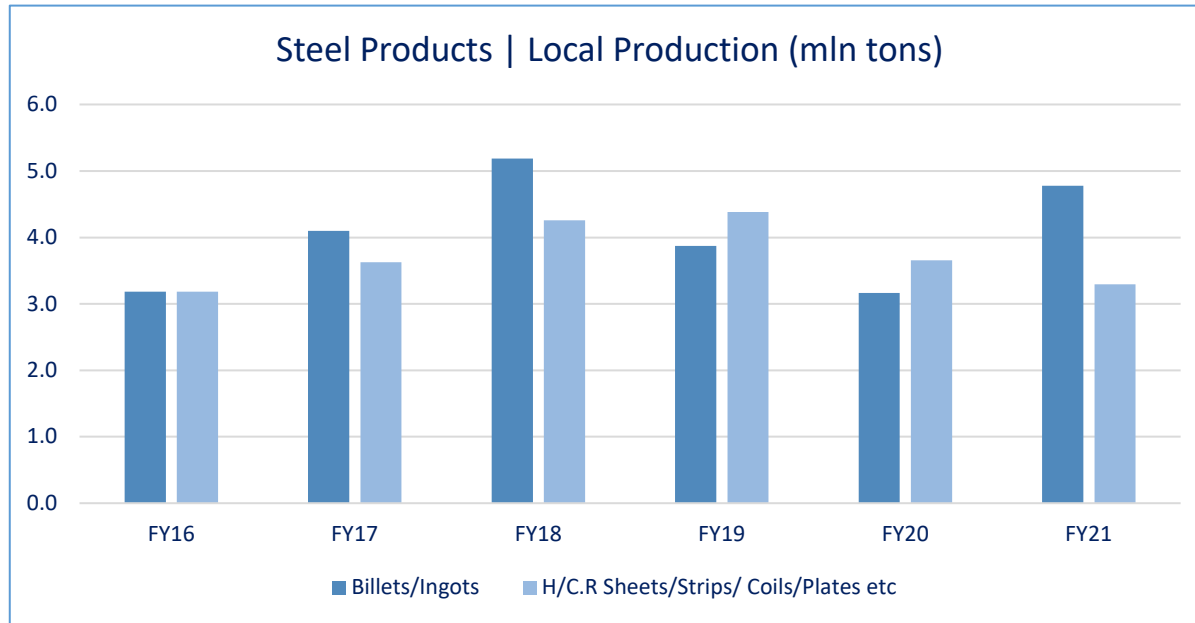


Pre-Galvanized Tool



Stainless Steel

## Supply Side | Production



- Production of billets were recorded at ~4.8mln tons during FY21 with YoY growth of ~51% (FY20: ~3.16mln tons). The significant increase in construction activity across the country led to the increase in demand of flat steel products. However, a lower demand from H/C.R Sheets (Flat products) was continued in FY21, mainly driven by drop in electronics production.
- Among billets manufacturers Amreli Steel, Mughal Iron & Steel and Agha Steel are major listed companies. This segment of the industry is highly fragmented with scores of small players.



## Supply Side | Production Capacity

- Long Steel Products:**

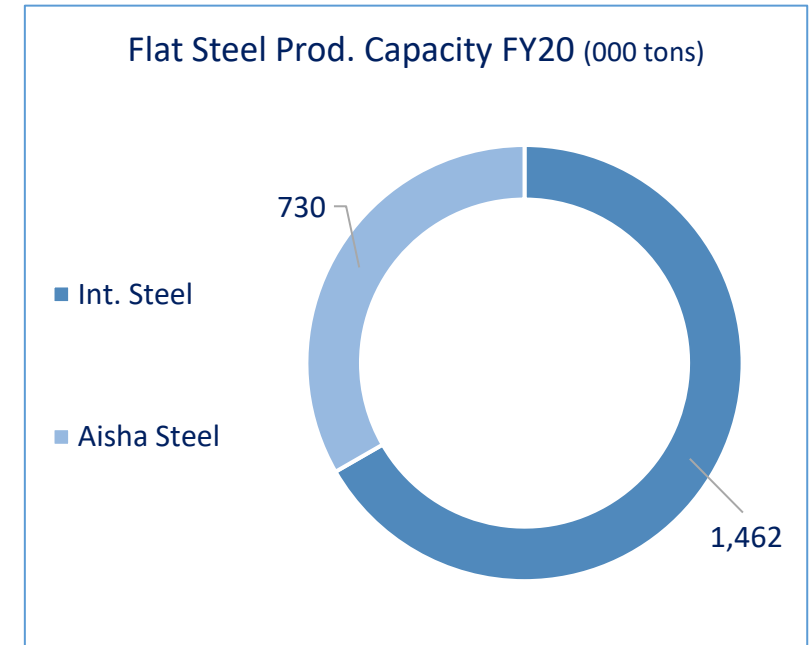
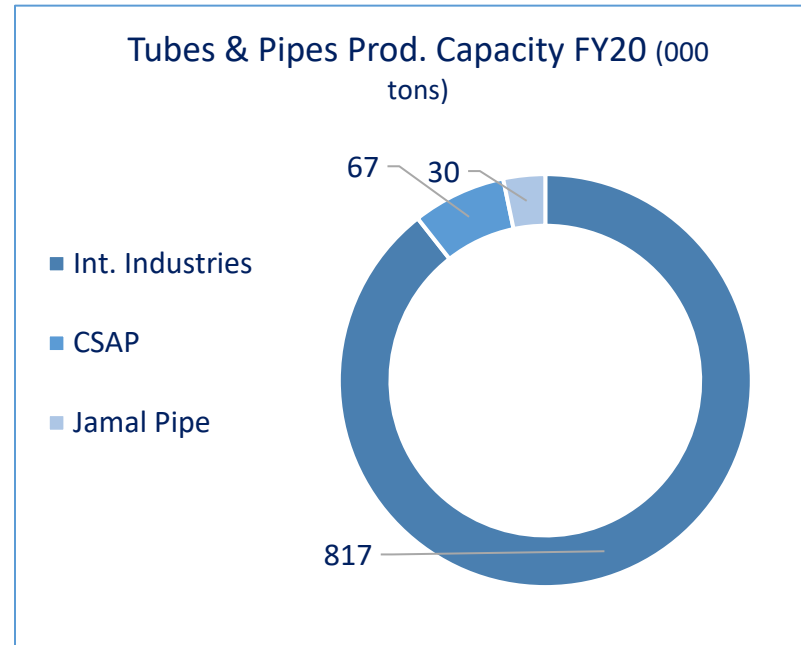
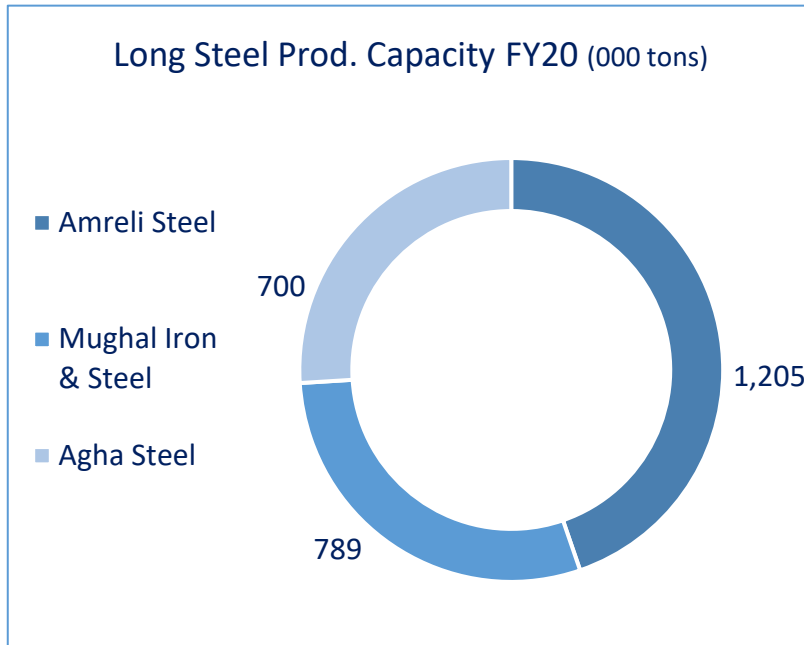
Top listed players in long steel segment are Amreli Steel, Mughal Steel and Agha Steel.

- Tubes & Pipes:**

International Industries is the market leader in Tubes & Pipes market of Pakistan.

- Flat Steel Products:**

International Steel has flat steel production capacity of ~1.4mln tons, more than double as compare to Aisha Steel .



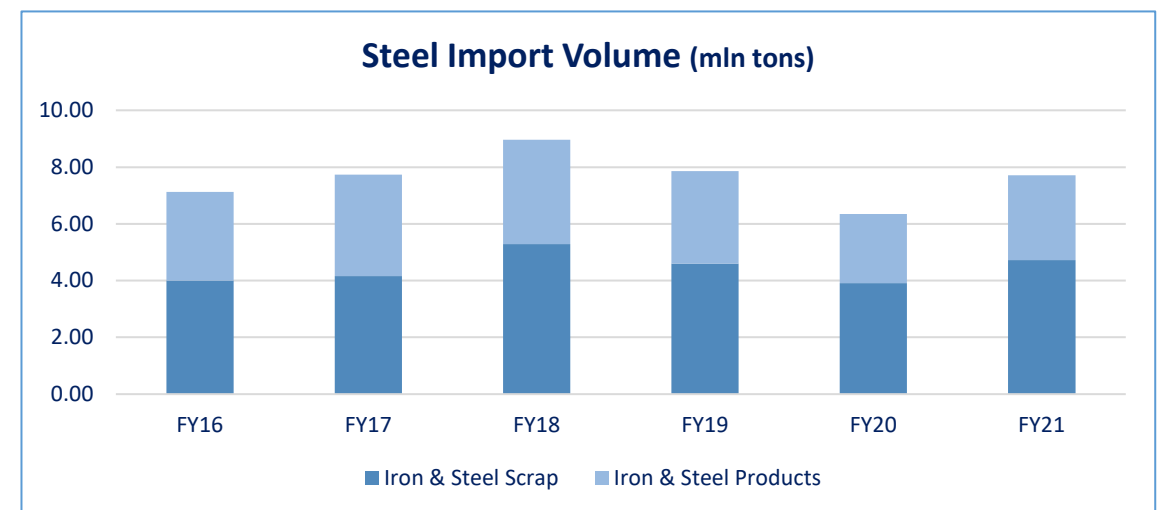
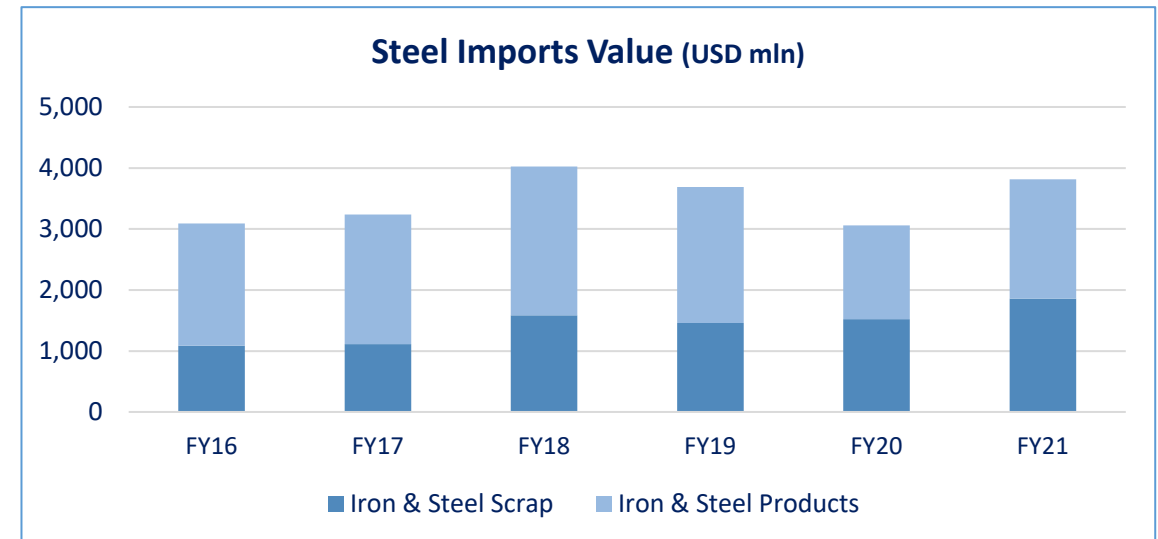
## Supply Side | Capacity Utilization

- Capacity utilization decreased during FY20 owing to overall slow down in economic activity. However, with an uptick in construction activity, capacity utilization of companies is expected to rise.

(Figures in 000 tons)					
Capacity Utilization					
Long Products					
	FY16	FY17	FY18	FY19	FY20
Actual Capacity	1,167	1,167	1,438	2,691	2,694
Production	663	680	834	1,354	1,330
<b>Capacity Utilization (%)</b>	<b>57%</b>	<b>58%</b>	<b>58%</b>	<b>50%</b>	<b>49%</b>
Flat Products					
Actual Capacity	1,232	1,232	1,682	1,760	2,192
Production	622	776	790	1,115	1,052
<b>Capacity Utilization (%)</b>	<b>50%</b>	<b>63%</b>	<b>47%</b>	<b>63%</b>	<b>48%</b>
Tubes & Pipes					
Actual Capacity	812	812	807	882	882
Production	345	365	436	320	223
<b>Capacity Utilization (%)</b>	<b>42%</b>	<b>45%</b>	<b>54%</b>	<b>36%</b>	<b>25%</b>

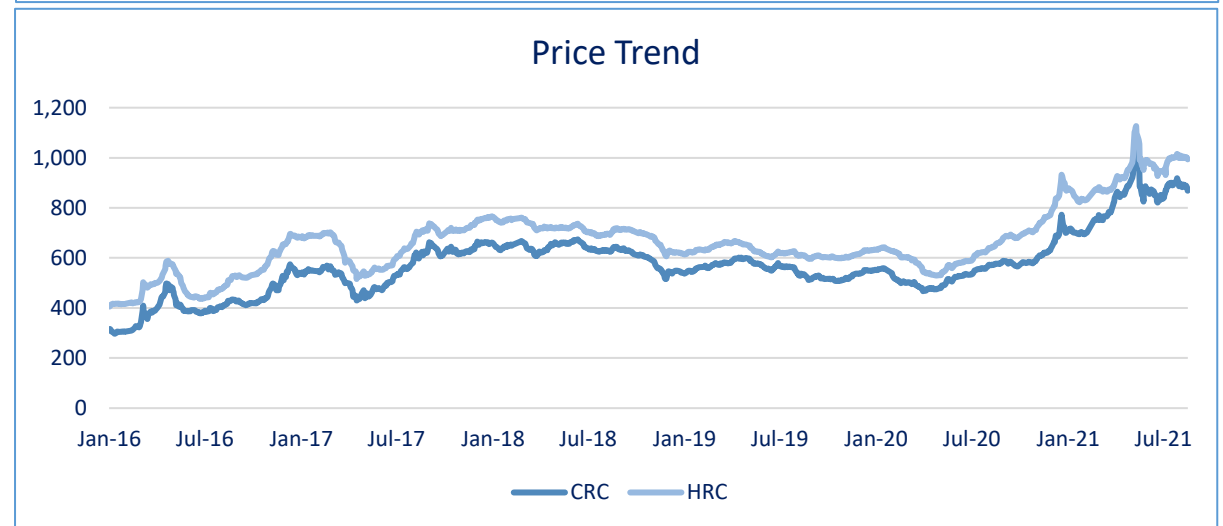
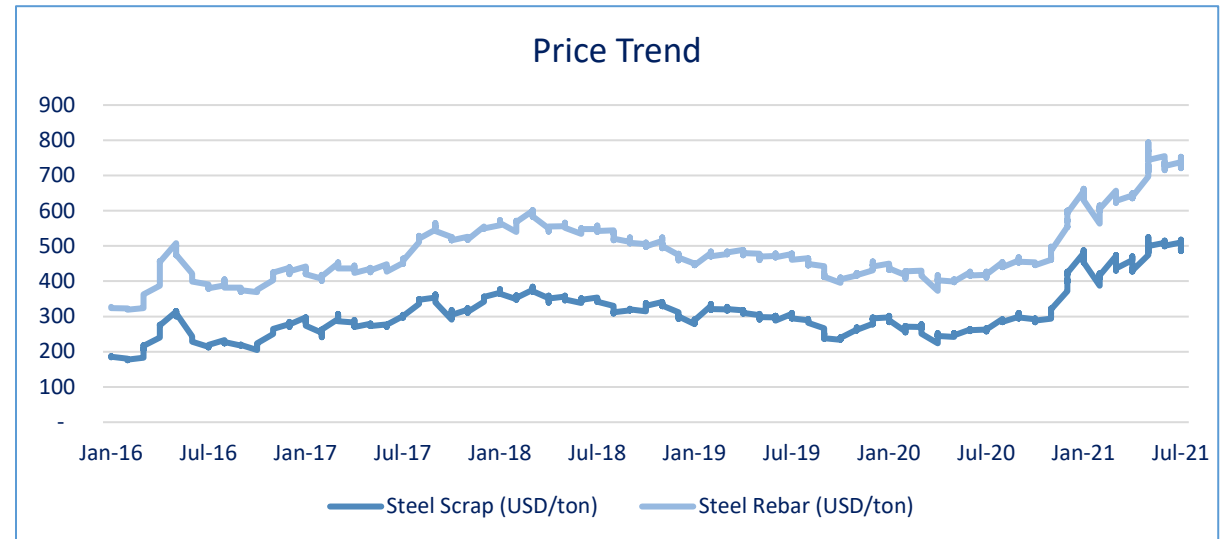
## Supply Side | Raw Material

- Pakistan is an importer of steel raw materials, i.e., majorly steel scrap, although a small share of iron ore is locally procured too.
- Most of the raw materials used in steel production are imported from China.
- During FY21, total iron and steel scrap imported was recorded around USD~1.9bIn (USD~1.5bIn in FY20), a share of ~3.4% to the country's total imports.
- Total quantity of iron and steel scrap imported was recorded around ~4.7mln tons up ~21% YoY (FY20: ~3.9mln tons).
- High dependence on imported raw material exposes the sector to changes in international raw material prices and exchange rate fluctuations.
- During FY21, the country produced ~725k tons of iron ore, a nominal contribution to the sector's requirement.
- Along with raw materials, Pakistan is also a partial importer of finished steel products (discussed later in demand slides).

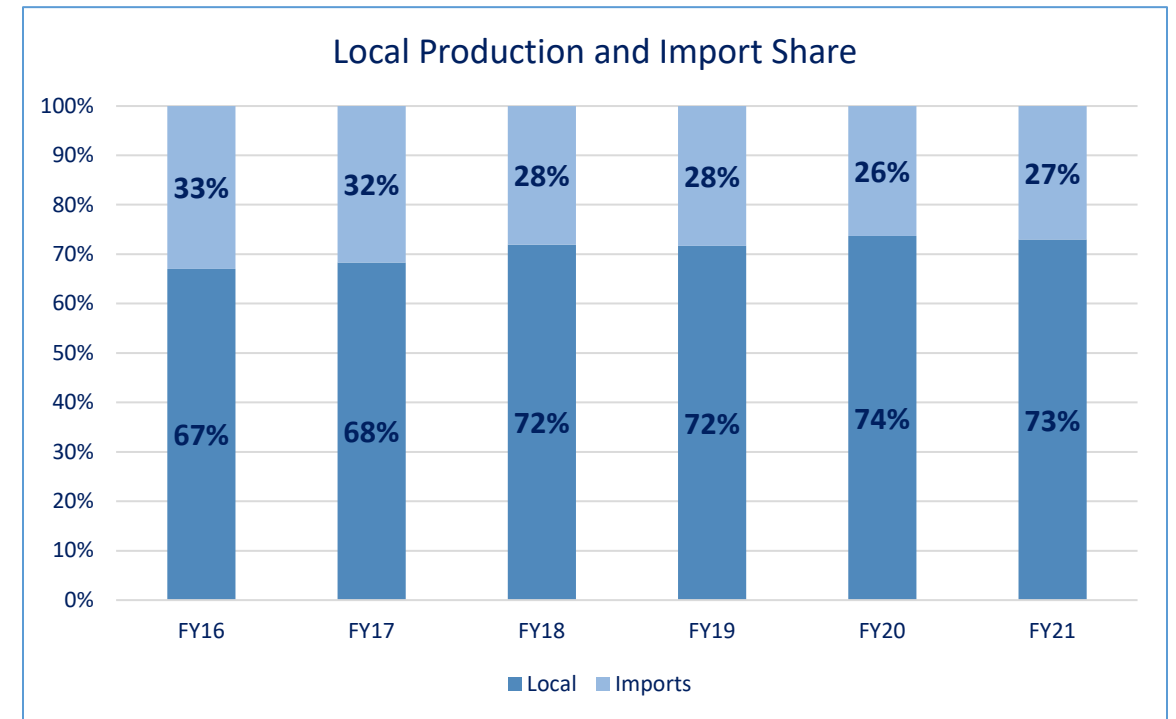
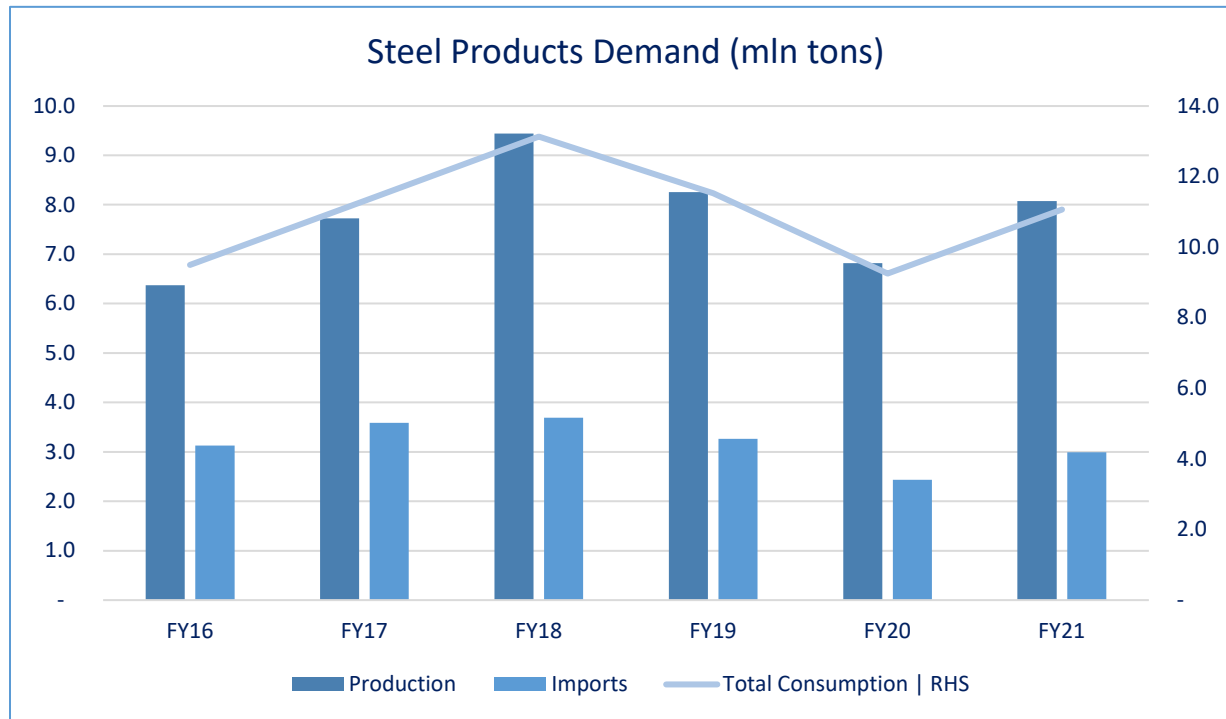


## Supply Side | Prices

- Global prices of steel raw materials observed significant increase starting from Sep-2020 to July-2021 amid increased construction activity and tightened supplies.
- Iron ore prices reduced significantly during August-2021 from above US\$200/ton to a low of US\$133/ton during second week of August-2021 owing to China's slowing steel output on environmental cuts and weakening demand from the property and infrastructure sectors and improved global supply of Iron ore.
- Manufacturers of long products are major importer of scrap steel. Amid high demand, the local players ability to pass on impact of increased to customer is increased and thus margins of companies are expected to remain robust. Flat steel producing companies imports hot rolled coil (HRC) as the major raw material for their final product are cold rolled coils (CRC).
- Global prices of iron ore as well as steel rebars are expected to remain under pressure during CY21 amid no signs of significant increase in China's construction activity. The reduction in iron ore price would be positive for Pakistan's steel companies considering their high dependence on imported raw material.



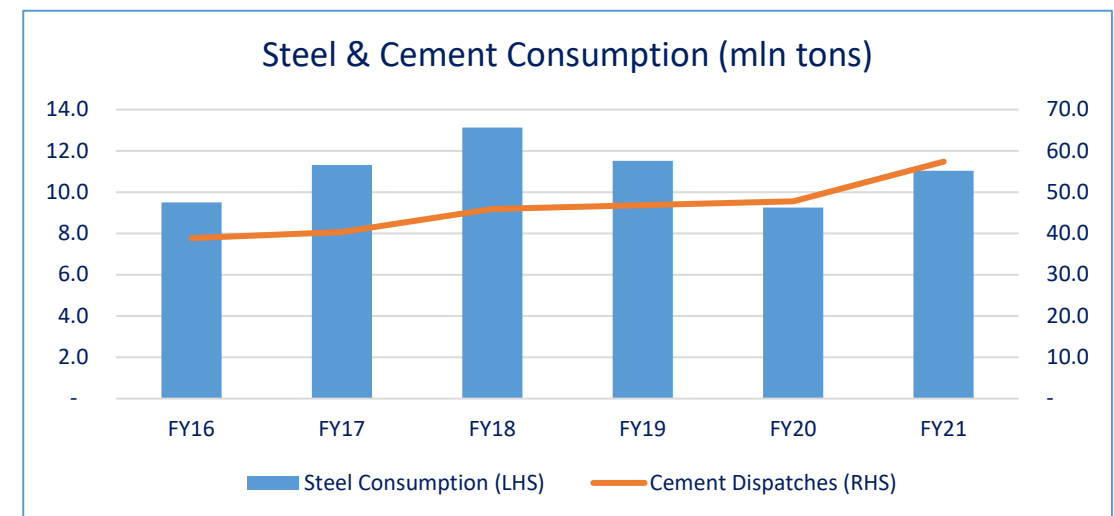
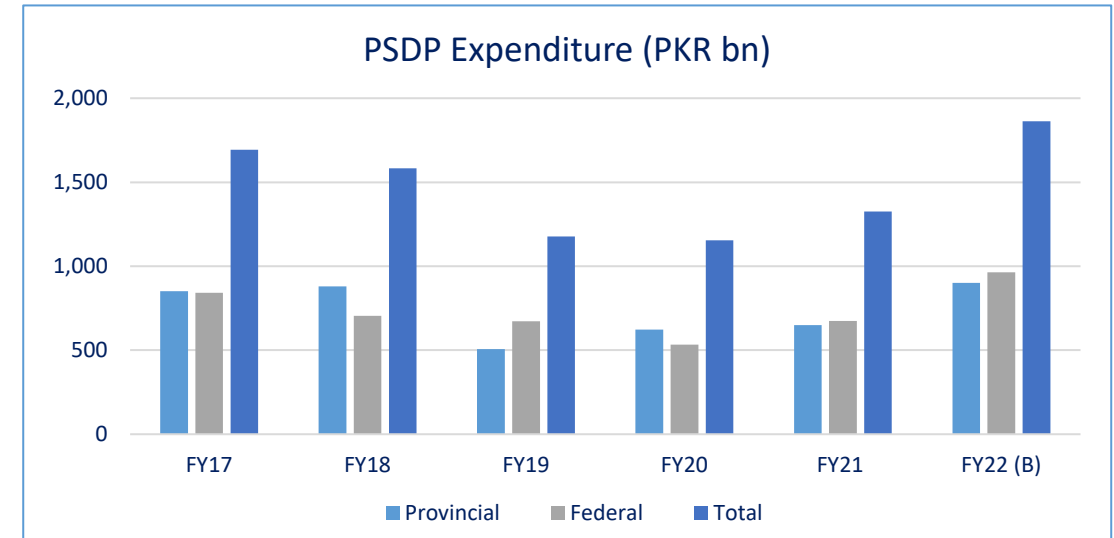
## Demand Overview



- Pakistan's total Steel Products' consumption was recorded at ~11.0mln tons in FY21 (~9.3mln tons in FY20) up ~19% YoY basis. The increase was majorly witnessed in Billets/ingots local production from which long steel products are produced that are used in the construction sector. Meanwhile, a decline was witnessed in the production of HRC/CRC Sheets/Strips Segment due to muted demand from the electronics segments.

## Demand | Construction

- Majority of the construction revenue is from government contracts ranging from building of Infrastructure to Highways, Offices and Airports. The budgeted size of PSDP allocation for FY22 is PKR 1,864bn (FY21: PKR~1,325bn) up 41% on YOY basis.
- The COVID-19 pandemic has made the demand for public investment essential in order to trigger job creation, support the economic activity and alleviate increased poverty. With significantly increased allocation coupled with other initiatives, the outcome looks encouraging. PSDP expenditure is highly correlated to construction sector's activity.
- Construction package announced by the government in FY20 including PKR~36bn subsidy for low-cost housing finance have already started to yield positive results as total housing and construction financing reached an all time high of PKR~259bn in June-2021 (June-2020: PKR~158bn) with YoY growth of 64%. Moreover, commercial banks were directed by SBP to increase construction sector loans to 5% of their total loan book.
- Advances are expected to maintain upward trajectory as government has further relaxed the requirements to obtain house construction loan at subsidized rates.





## Demand

### Major Public Sector Projects to boost up steel demand:

- Dams: Initial/preparatory works for the construction of Diamer Bhasha Dam and Mohmand Dam is in progress.
- Construction of new green field Gwadar International Airport and Gwadar Port Free Zone. The construction of Free Zone Phase-I has been completed with all infrastructures. More than 30 enterprises from various sectors have registered in Gwadar Port Free Zone.
- Construction of 'Panahgahs' in major cities to provide shelter to the homeless. Construction of Nuclear Power Plants near KANUPP site in Karachi, i.e., K-2/K-3 and a power plant at Chashma near Mianwali (C-5).
- Expansion of Pipeline Network: PAPCO is expanding its pipeline network from Machhike (Sheikhupura) to TaruJabba (Peshawar). The pipeline is expected to be dual purposed (MOGAS and HSD) and the contract for construction has already been initiated. It is expected to be completed in FY23. The ~427km long pipeline is divided into three section, aimed at ensuring a smooth supply chain of petroleum products from Karachi to Peshawar.
  - Machhike-Chak Pirana (~135km)
  - Chak Pirana-Rawat (~117km)
  - Rawat-TaruJabba (~175km)
- Pakistan Stream Gas Pipeline (formerly “North-South Gas Pipeline”): Pipeline with the length of ~1,122km connecting Port Qasim (Karachi) to Kasur (Punjab) would be built under the Inter Governmental Agreement for North South Gas Pipeline (NSGPP) between Russian Federation and Pakistan.

## Business Risks | Overview

### Operating Risks:

- **Dumped Imports:** Despite huge potential for growth, the steel sector's growth momentum has historically remained subdued. One of the major risks that the Sector has faced over time is Import Substitution. Pakistan imports finished steel products from countries including China, Ukraine, Canada and Russia. Many of the steel products were historically being imported at dumped prices. In a response to the Sector Players' and Association's plea, the NTC imposed anti dumping duties (~24%) on import of billets/ingots from China effective from June, 2017 for a period of five years. The NTC also imposed dumping duties of ~14% on imported H/C.R Coils/Sheets from Canada and Russia w.e.f. Sep 20, 2019 for a period of five years.
- **Availability of Cheaper Steel Products from other major markets:** Another key risk for the development of steel sector is the availability of cheaper products (other than dumped) from other markets such as FATA. In Budget FY22, the GoP has abolished FED on 40 units located in the FATA region. This is expected to make their products cheaper by around PKR~27,000-30,000 per ton, thus creating price distortion for the local producers and forcing them to lower their prices to remain competitive.
- **Inefficient Energy Utilization:** Steel is an energy intensive sector. Many of the small sized players rely on obsolete and energy inefficient steel making technology. The quality of steel products from these mills is substandard as well as costly in comparison to big manufacturers.

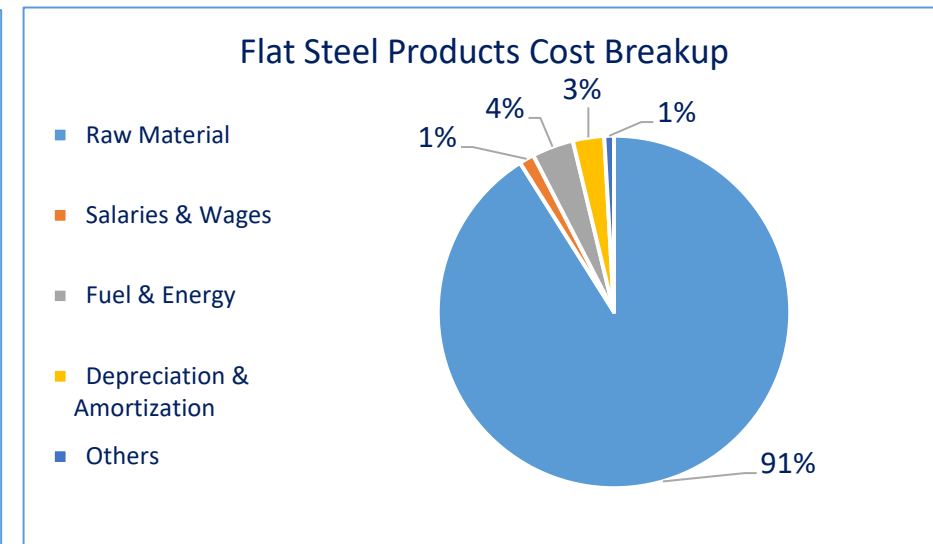
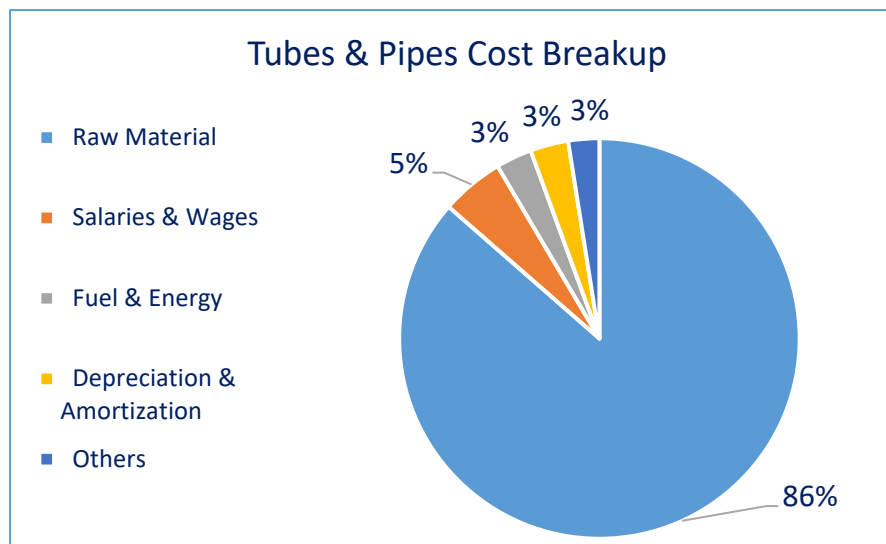
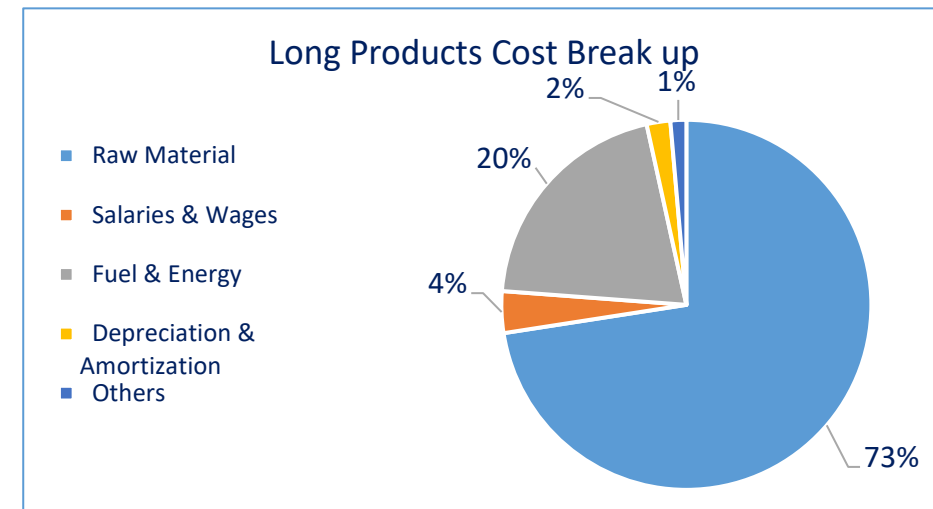
### Sales Risks:

- The demand for Steel Sector is linked to a number of other essential sectors of the economy, the foremost being construction, automotive and electronics sectors. Prospects for the construction and automotive sectors are positive, therefore, demand for long steel products are expected to foster in the near future. However, flat products, which are majorly used in electronics production, may continue to witness a slowdown in the upcoming days, till the electronics segment revives.



## Business Risk | Cost Break up

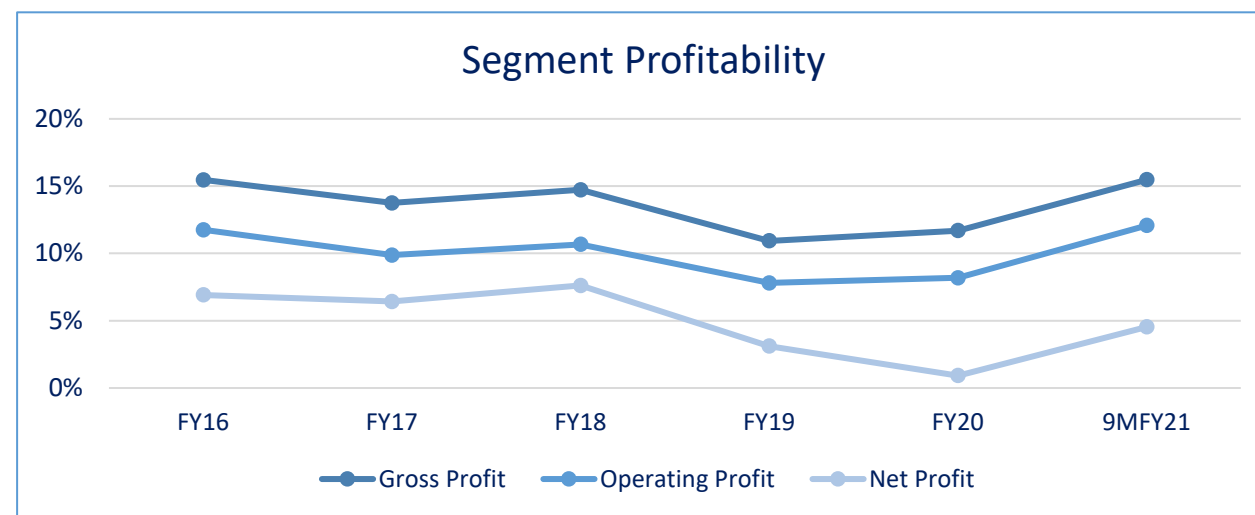
- Major raw materials used in steel manufacturing process is steel scrap. Raw Materials constitute a significant portion of the companies' manufacturing cost.
- High reliance on imported raw material to meet sector's demand exposes the sector to changes in international raw material prices and exchange rate fluctuations. As mentioned earlier, international scrap steel prices are expected to remain range bound, which will have a positive impact on sector's profitability.
- Fuel & energy cost is the second largest component of the cost as it constitutes ~20% of the total cost of the production in case of flat steel products. Electricity is the major source of energy of the sector.
- Fluctuation in electricity prices and load shedding affects the cost of sales and the sector's operations accordingly. Companies with captive power plants are less exposed to operations disruptions.



## Business Risk | Long Products

- Total revenue of the long products segment was recorded at PKR~67,264mln during FY20 (FY19: PKR~69,906mln) with a YoY decrease of ~4%.
- FY20 was a tough year for the steel sector in terms of pressure on the margins on account of rising exchange rate, interest costs (for most part of the year) and subdued demand. GP margins plunged to as low as ~12% from ~15% in FY18. The benefit of low international scrap prices during FY20 was eroded by high average exchange rate during the period. Bottomline of the segment reduced significantly to PKR~623mln during FY20 (FY19: PKR~2,174mln) as a consequence of shrunk demand and increased costs.
- Despite the dip, the segment's indicators have turned around well in 9MFY21 with gross profits recording a 2x YoY growth during 9MFY21. Strong local prices, stable exchange rate and historically low interest rates during 9MFY21 are the major contributors.
- With an uptick in construction activity, the demand of long steel products are expected to remain strong and hence the pricing power of companies.

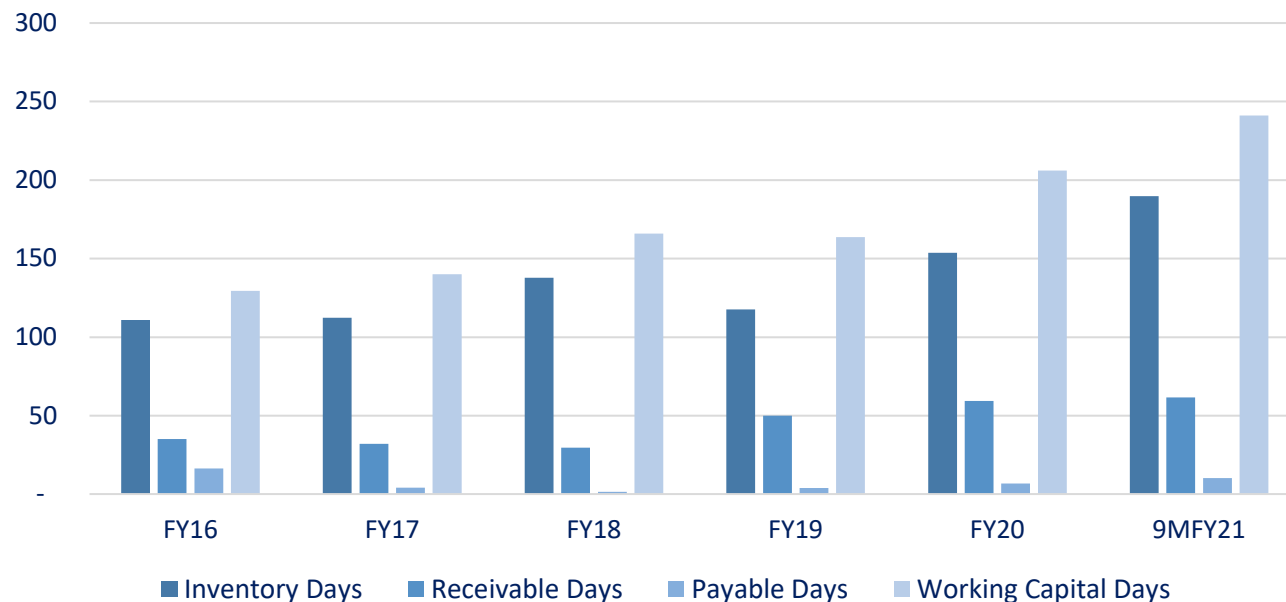
Sector: Financial Highlights							
Company	FY16	FY17	FY18	FY19	FY20	9MFY20	9MFY21
Net Sales	31,384	32,087	37,726	69,906	67,264	42,687	72,604
Cost of Sales	26,533	27,677	32,174	62,262	59,401	38,939	61,371
<b>Gross profit</b>	<b>4,851</b>	<b>4,410</b>	<b>5,553</b>	<b>7,644</b>	<b>7,863</b>	<b>3,748</b>	<b>11,233</b>
Operating Expense	1,165	1,242	1,529	2,188	2,356	1,544	2,466
<b>Operating Profit</b>	<b>3,686</b>	<b>3,168</b>	<b>4,024</b>	<b>5,456</b>	<b>5,507</b>	<b>2,204</b>	<b>8,767</b>
Finance Cost	648	501	1,026	3,179	5,345	3,047	3,101
<b>Profit/(Loss) before Tax</b>	<b>3,038</b>	<b>2,667</b>	<b>2,998</b>	<b>2,277</b>	<b>162</b>	<b>-844</b>	<b>5,666</b>
Taxation	869	603	123	103	-461	414	2,371
<b>Profit/(Loss) after Tax</b>	<b>2,169</b>	<b>2,064</b>	<b>2,875</b>	<b>2,174</b>	<b>623</b>	<b>-1,257</b>	<b>3,295</b>



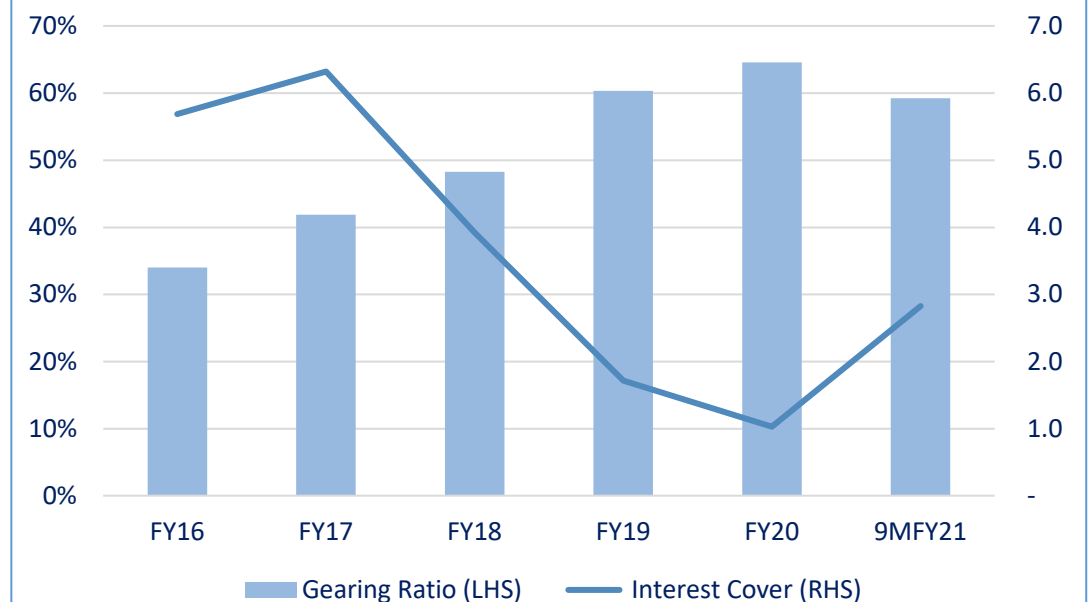
## Financial Risk | Long Products

- The segment's working capital structure is characterized by high inventory and receivable days. Considering the long lead time required for procurement of raw material, this segment usually maintains high inventory levels.
- The segment's working capital cycle was recorded at ~241 days during 9MFY21 (FY20: ~206 days) mainly driven by inventory days rising to ~190 days during 9MFY21 (~154 days in FY20). The Sector's exposure to Raw Material volatility in terms of price and exchange rate fluctuation is high, which can lead to fragility in its profitability.

### Working Capital Management



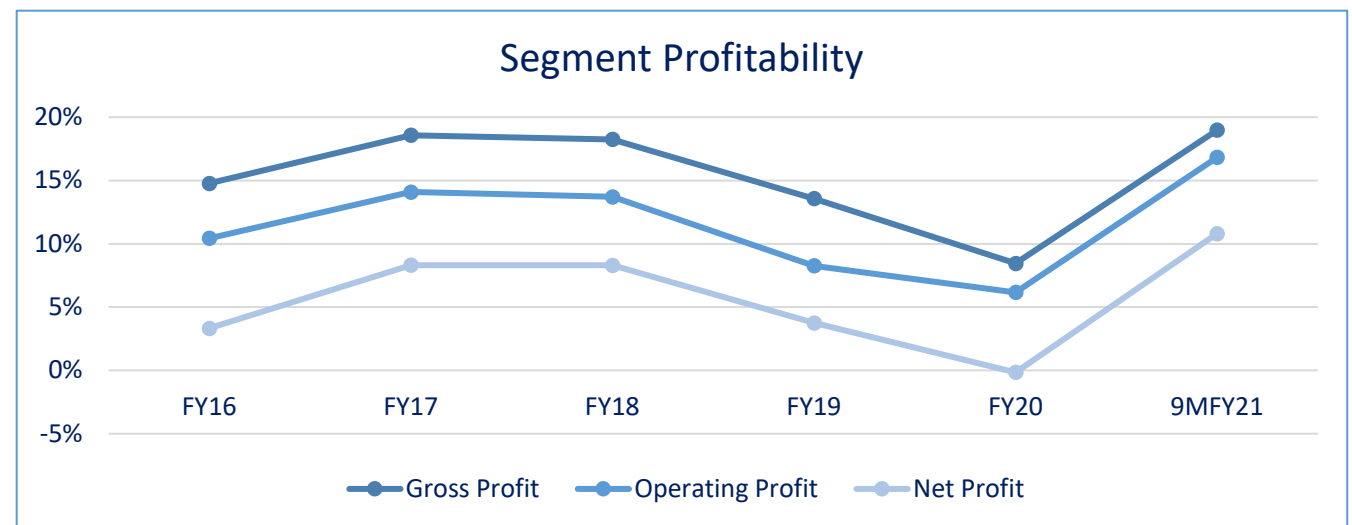
### Leverage Ratio



## Business Risk | Flat Products

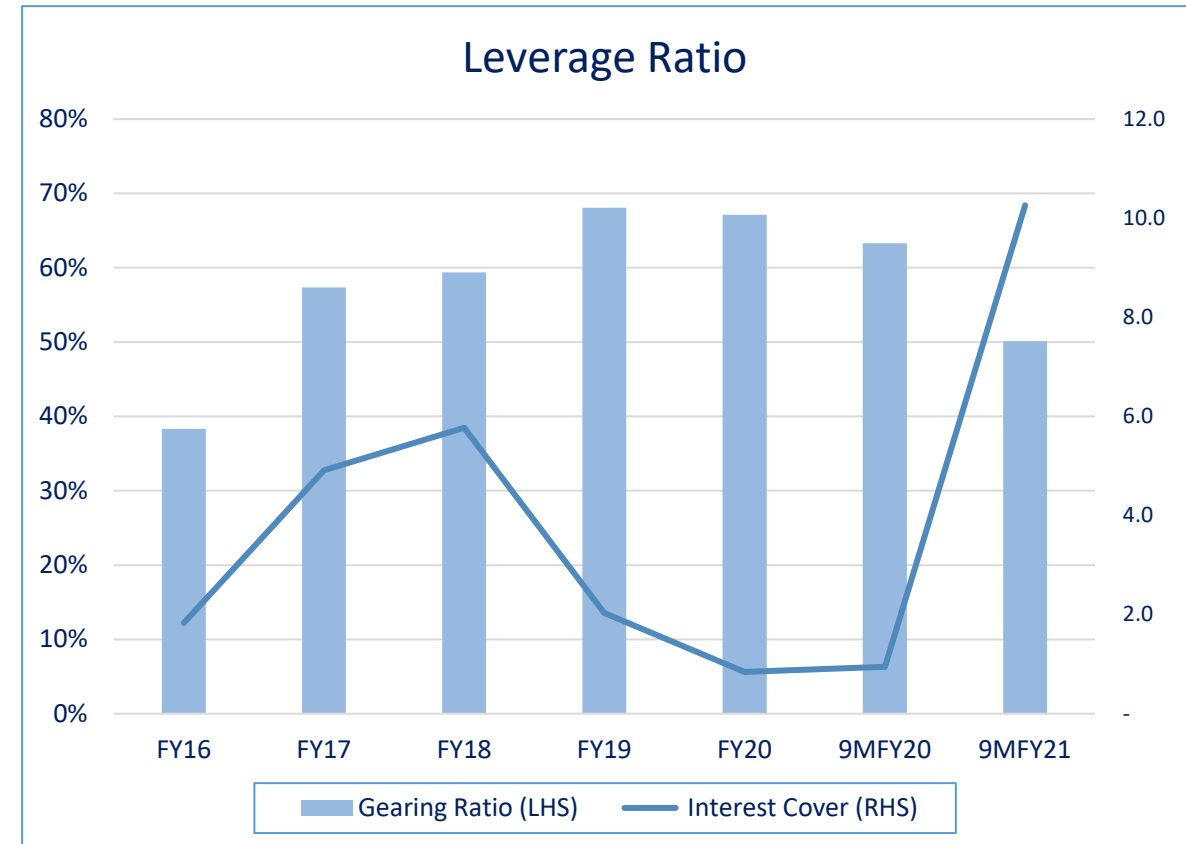
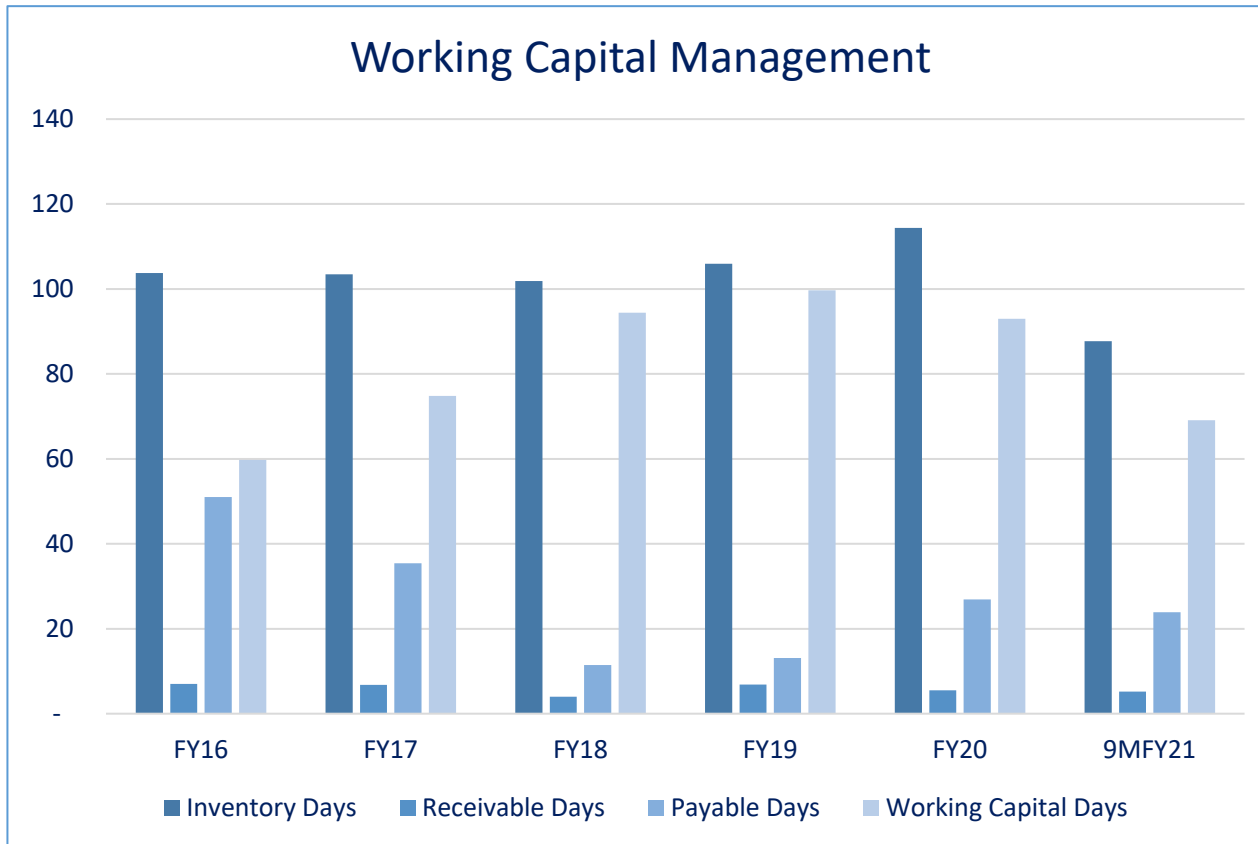
- Inline with the whole steel sector the demand of flat products also remained subdued as the segment's revenue was recorded at PKR~77,859mln during FY20 (FY19: PKR~77,714mln) with very minimal growth.
- FY20 was a tough year for the sector in terms of pressure on the margins on account of rising exchange rate, interest costs (for most part of the year) and subdued demand. GP margins plunged to as low as ~8% from ~18% in FY18. The benefit of low international scrap prices during FY20 was eroded by high average exchange rate during the period. Bottomline of the sector turned negative as it plunged to negative PKR~123mln (loss) during FY20 (FY19: PKR~2,919mln) as a consequence of shrunk demand and increased costs.
- Despite the dip, the sector's indicators have turned around well in 9MFY21 with gross profit recording a 1x YoY growth during 9MFY21. Strong local prices, stable exchange rate and historically low interest rates are the major contributors.

Figures in PKR mln		Segment: Financial Highlights					
Company	FY16	FY17	FY18	FY19	FY20	9MFY20	9MFY21
Net Sales	30,786	48,897	68,062	77,714	77,859	63,070	91,672
Cost of Sales	26,239	39,814	55,636	67,164	71,279	54,691	74,266
<b>Gross profit</b>	<b>4,547</b>	<b>9,083</b>	<b>12,426</b>	<b>10,550</b>	<b>6,580</b>	<b>8,379</b>	<b>17,406</b>
Operating Expense	2,011	2,190	3,091	4,129	1,781	6,174	1,967
<b>Operating Profit</b>	<b>3,214</b>	<b>6,893</b>	<b>9,335</b>	<b>6,421</b>	<b>4,799</b>	<b>4,169</b>	<b>15,439</b>
Finance Cost	1,751	1,403	1,617	3,154	5,700	4,388	1,505
<b>Profit/(Loss) before Tax</b>	<b>1,463</b>	<b>5,490</b>	<b>7,718</b>	<b>3,267</b>	<b>-901</b>	<b>-219</b>	<b>13,934</b>
Taxation	439	1,427	2,069	348	-778	-443	4,030
<b>Profit/(Loss) after Tax</b>	<b>1,024</b>	<b>4,063</b>	<b>5,649</b>	<b>2,919</b>	<b>-123</b>	<b>224</b>	<b>9,904</b>



## Financial Risk | Flat Products

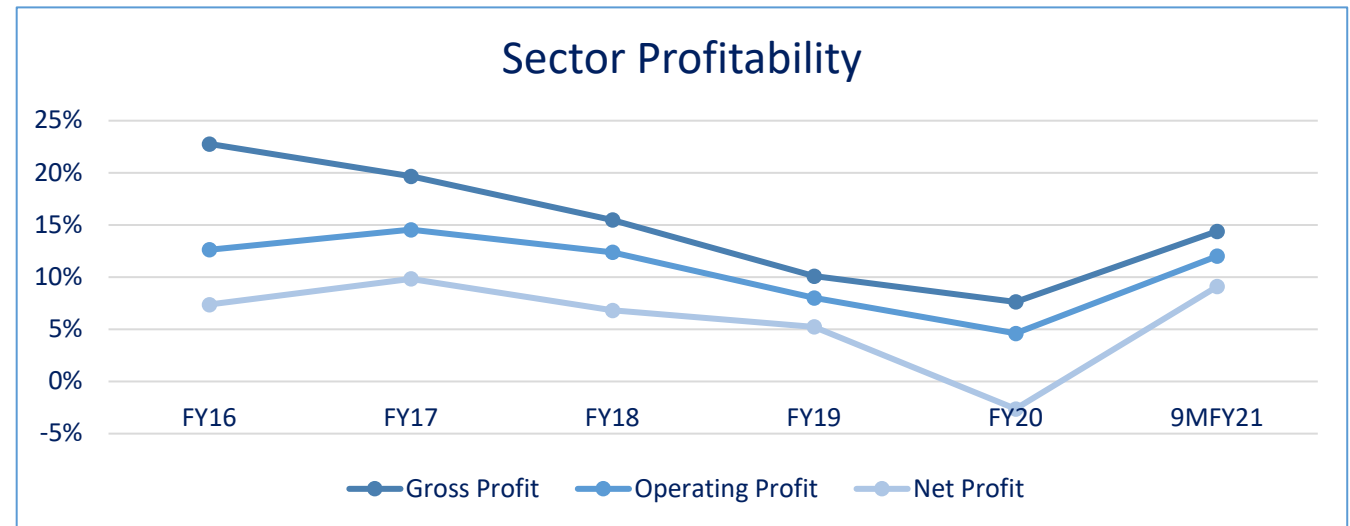
- The segment's working capital structure is characterized by high inventory days and moderate payable days.
- The segment's working capital cycle was reduced to ~69 days during 9MFY21 (FY20: ~93 days) mainly due to decrease in inventory days to ~88 days during 9MFY21 (~114 days in FY20).



## Business Risk | Tubes & Pipes

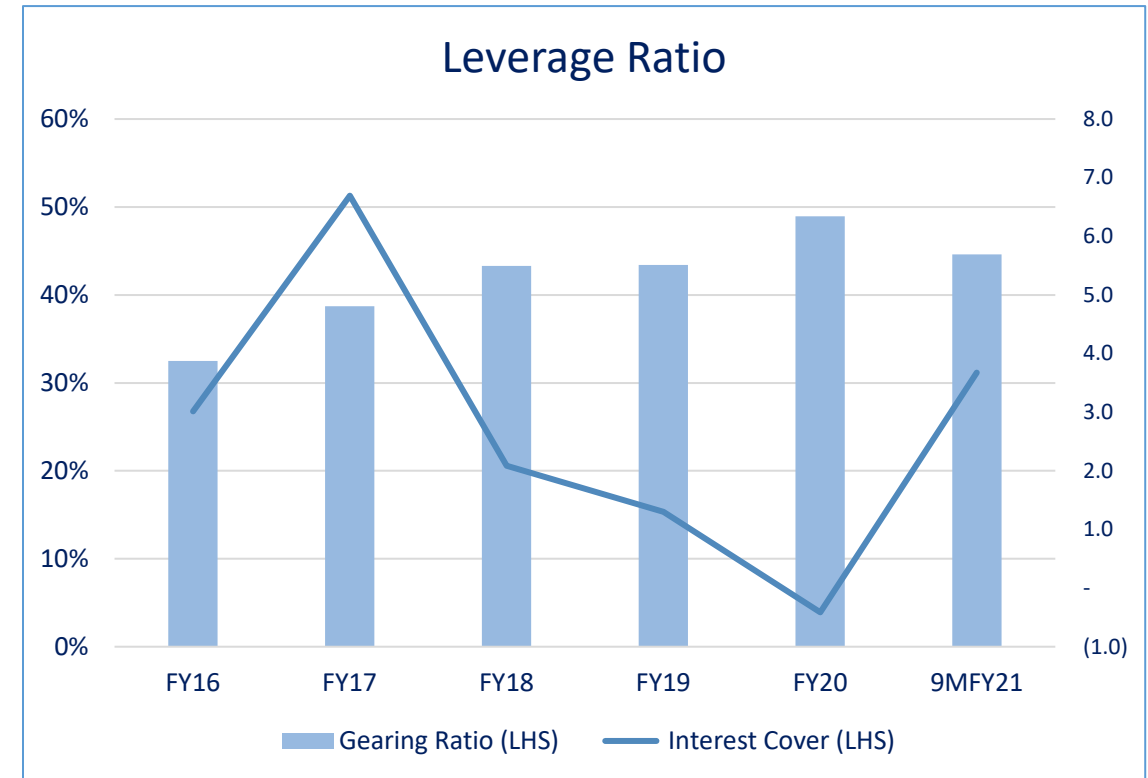
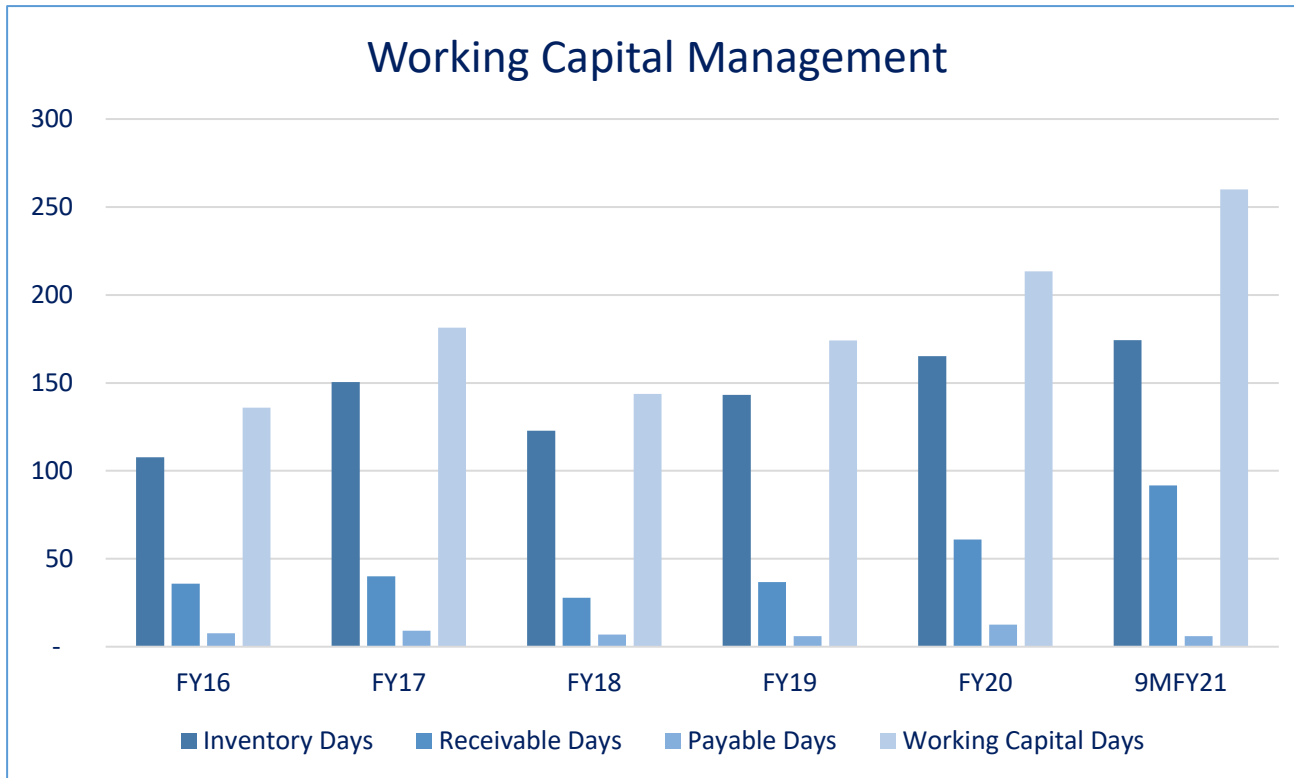
- Steel tubes & pipes segment registered a revenue of PKR~25,231mln in FY20 (FY19:PKR~32,081mln) with a YoY dip of ~21%. This decline is the highest among all three segments, attributable to highly fragile demand of steel tubes & pipes.
- The steel tubes and pipes demand is strongly linked to the government spending as most of the segment's demand emanates from large engineering projects.
- The government's agenda to revitalize economic activity and support the construction sector encourages the commencement of mega engineering projects. This fosters the growth of all allied construction sectors including this segment of the steel industry. The segment posted a revenue of PKR~23,566mln during 9MFY21 (9MFY20: PKR~16,093mln) reflecting a YoY hike of ~46%.
- Profit margins of the segment have also showed strong rebound owing to improved pricing, amid strong demand, and historically low interest rate that kept the finance cost of the sector low.

Figures in PKR mln		Sector: Financial Highlights					
Company	FY16	FY17	FY18	FY19	FY20	9MFY20	9MFY21
Net Sales	24,399	29,632	35,483	32,081	25,231	16,093	23,566
Cost of Sales	18,847	23,807	29,995	28,842	23,310	14,905	20,176
<b>Gross profit</b>	<b>5,552</b>	<b>5,825</b>	<b>5,488</b>	<b>3,239</b>	<b>1,921</b>	<b>1,188</b>	<b>3,390</b>
Operating Expense & Other Income	2,473	1,517	1,097	-152	762	371	562
<b>Operating Profit</b>	<b>3,079</b>	<b>4,308</b>	<b>4,391</b>	<b>3,391</b>	<b>1,159</b>	<b>817</b>	<b>2,828</b>
Finance Cost	596	435	1,158	1,290	1,627	1,089	583
<b>Profit/(Loss) before Tax</b>	<b>2,483</b>	<b>3,873</b>	<b>3,234</b>	<b>2,101</b>	<b>-468</b>	<b>-272</b>	<b>2,245</b>
Taxation	687	962	817	424	199	169	103
<b>Profit/(Loss) after Tax</b>	<b>1,796</b>	<b>2,911</b>	<b>2,416</b>	<b>1,677</b>	<b>-667</b>	<b>-441</b>	<b>2,143</b>



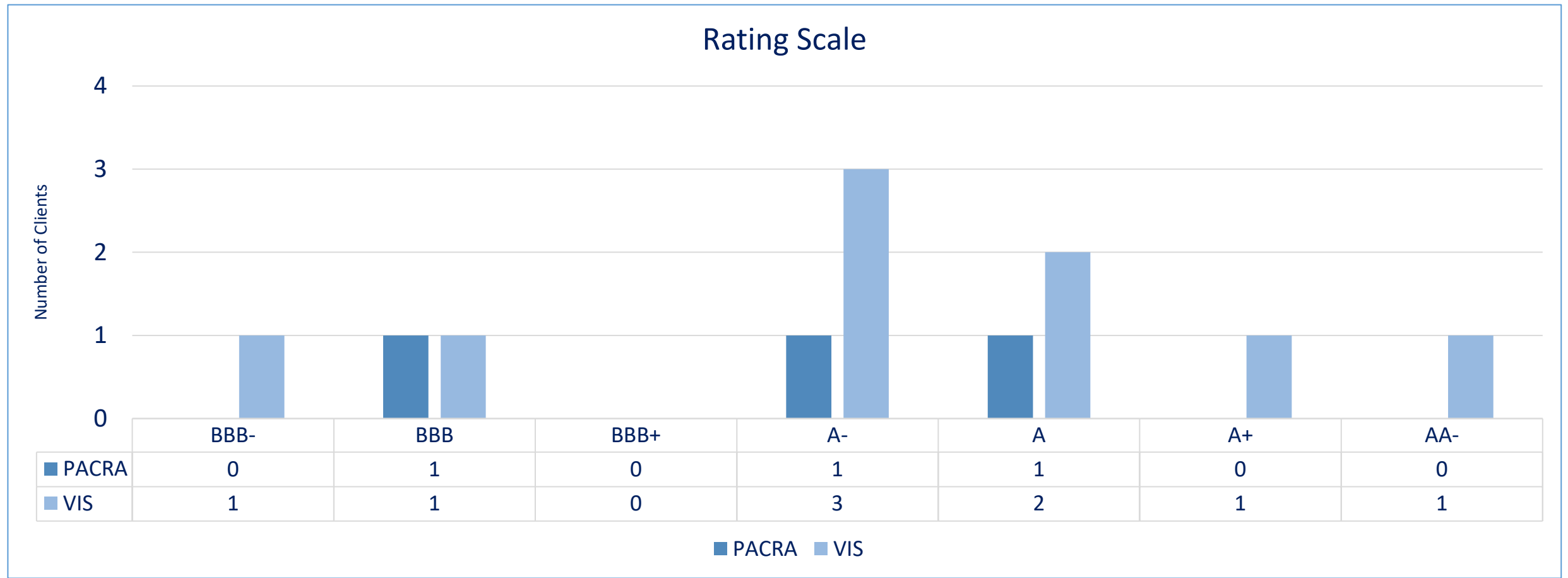
## Financial Risk | Tubes & Pipes

- The segment's working capital structure is characterized by high inventory days and receivable days.
- The segment's working capital cycle skyrocketed to ~311 days during 9MFY21 (FY20: ~213 days) mainly due to a hike in receivable days from ~61 in FY20 to ~143 days in 9MFY21.



## Rating Curve

- PACRA rates 3 clients in the steel sector. Rating bandwidth of the sector is BBB to A.





## SWOT

- Capital intensive sector
- Good margins in periods of demand boom.
- Significant Potential demand
- Strong dealership and distribution network
- Non-availability of substitute

- Heavy reliance on imported raw material
- Exposure to exchange rate volatility
- Seasonality and uncertainty in demand
- Inability to pass on impact of increased cost in times of depressed demand



- High Production capacity – supply surplus
- Increasing cost of energy
- Inability of the government to spend on PSDP projects
- Fourth wave of COVID-19 and possible lockdown

- Low per capita consumption
- Government initiatives to spur construction activities and establish a large number of low cost houses.
- Pakistan GDP recovery and reduced finance costs leading to opportunities for investment
- Improving infrastructure under CPEC related projects
- Initiation of large engineering projects

## Duties & Taxes

- Duty structure of the sector is designed to encourage local production of the cement.

PCT Code	Description	Custom Duty		Additional Custom Duty		Regulatory Duty		Sales Tax		Income Tax		
		Raw Material for Cement	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22
7204.3000	Scrap		0%	0%	2%	2%	5%	5%	17%	17%	11%	11%
7206.1000	Ingots		3%	3%	2%	2%	0%	0%	17%	17%	11%	11%
7207.1110	Billets		11%	11%	2%	2%	15%	15%	17%	17%	11%	11%
7209.1510	Flat Rolled Products		20%	20%	6%	6%	5%	5%	17%	17%	11%	11%
7213.1010	Bars & Rods		20%	20%	6%	6%	30%	30%	17%	17%	11%	11%

## Outlook: Positive

- Post COVID-19 lockdown, steel sector has shown tremendous growth mainly led by the significant increase in demand for long products. During FY21, the government has announced construction package along with other regulatory relaxations to support construction activity. These measure are yielding positive results as the sector has shown healthy growth signs since then.
- The government has also increased the size of budgeted PSDP allocation for FY22 to PKR 1,864bn (FY21: PKR~1,325bn) up 41% on YoY basis. Total spending of PSDP allocation by the government is highly likely, subject to availability of funds. Moreover, the growth of financing under Naya Pakistan Housing schemes is also encouraging and is expected to enhance further in the coming periods.
- Improved demand prospects have strengthened the pricing power of the sector players. On the other hand, steel scrap prices have recently witnessed a decline in the International market, yet local product prices continue to improve. This will expand the margins room of the players more. Additionally, the sector's bottom-line has benefitted from historically low interest rates. Any increase in the Interest rates in the near term will add to the finance cost of the players and thus impact bottom-line margins.
- Recent decline in international scrap steel prices has largely nullified the pressure of currency depreciation impact. Raw material prices are expected to remain range bound in FY22 which will bode well for the sector's overall profitability.
- Any unforeseen demand dip from individual housing construction or from major engineering projects may cast a downward impact on the sector's profitability.

- World Steel Association
- World Bank
- Pakistan Bureau of Statistics (PBS)
- Federal Board of Revenue (FBR)
- Securities & Exchange Commission of Pakistan (SECP)
- Ministry of Planning, Development and Reform
- National Steel Advisory Council
- Trading Economics
- State Bank of Pakistan (SBP)
- Pakistan Stock Exchange (PSX)
- Bloomberg

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