

Wednesday, February 20, 2019 | update

# JSW: hold (upgraded)

JSW PW; JSW.WA | Coal Mining, Poland

## 2019 Slowdown Priced In After Correction

Prices of metallurgical coal are up at over \$200/t after rising from about \$190/t in the course of the last few weeks due to tighter supply from Australia where heavy rainfall had caused rail disruptions. This gives a more upbeat view on the coal market, underpinned by a rebound in China's steel PMI over 50 points in January. Nevertheless the growth potential of met coal prices is curbed by low margins earned by BOF steel producers in China, where the steel stockpile is seen to be rising. Against this backdrop, JSW shares have posted a correction over recent weeks, and at the current level all the earnings risks expected in FY2019 seem largely priced in, with downside risk reined in by yesterday's statement from Deputy Energy Minister denying any knowledge of JSW's equity-raising plans after statements to the contrary made by the Company's CEO in an interview on Monday. JSW is scheduled to release its FY2018 earnings report on March 21st, and if this is accompanied by a dividend declaration the potential payout at the current share price level could make for a very handsome dividend yield. We uphold our PLN 60.68 target price for JSW, but we upgrade the Coal Miner from reduce to hold after the recent price declines.

## CEO on Capital-Raising Plans

In Monday's interview for Parkiet TV, CEO Daniel Ozon said JSW was working to increase production this year (we expect a 3% rise in output), as well as aiming for a higher, 70% share of coking coal in the production mix (we think 67% is a more realistic goal). Capital expenditures in 2019 are tentatively budgeted at PLN 1.4bn. Mr. Ozon also said the Management Board were currently weighing paying one-off performance bonuses to JSW's employees (we expect PLN 200m) against raising their base salaries, with the CEO leaning toward the first option. In the part of the interview that most agitated investors, Mr. Ozon talked about JSW contemplating a share issue which could raise about PLN 0.5-1.0 billion toward future growth, but done in such a way as not to take away controlling interest from the Treasury. The statement was followed a day later by a stunned response from the Deputy Energy Minister saying it was the first time he was hearing of JSW's equity-raising plans.

## Large Cash Pile Means No Capital Raise Necessary

We estimate that JSW ended 2018 with a net cash position worth close to PLN 26 per share, and PLN 3.8 billion in total, which is more than enough to fund all the capital projects the Company has lined up for the next two years without the need to raise equity.

## Improving Momentum In China

New orders at Chinese steel mills improved dramatically in January, with the corresponding PMI sub-index up to 53pts from 40pts in December and 35pts in November. Steel demand can be expected to continue growing after China improved access to credit to help further local infrastructure projects. Higher steel demand implies higher demand for metallurgical coal.

(PLN m)	2016	2017	2018E	2019E	2020E
Revenue	6,731.3	8,877.2	9,664.2	8,971.5	8,688.2
EBITDA (adj.)	1,054.5	3,508.8	3,211.4	1,766.6	1,465.5
EBITDA margin	15.7%	39.5%	33.2%	19.7%	16.9%
EBIT (adj.)	215.7	2,684.1	2,471.0	885.1	419.2
Net profit (adj.)	-2.1	2,188.7	1,996.5	719.7	338.1
P/E (adj.)	-	3.2	3.5	9.8	20.8
P/CE	8.3	2.1	2.3	4.4	5.1
P/B	1.8	1.1	0.8	0.8	0.8
EV/EBITDA (adj.)	7.2	1.6	1.3	2.8	3.8
DPS	0.0	0.0	0.0	5.9	2.5
Dividend Yield	0.0%	0.0%	0.0%	9.9%	4.1%

Current Price	PLN 59.96
Target Price	PLN 60.68
MCap	PLN 7.0bn
Free Float	PLN 3.2bn
ADTV (3M)	PLN 29.6m

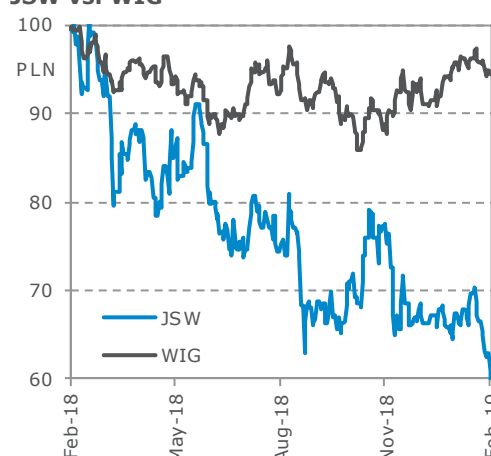
## Ownership

State Treasury of Poland	55.17%
Others	45.83%

## Business Profile

JSW is the largest coking coal producer in the European Union with 2017 production at 10.8 million tonnes, equivalent to 18-22% of the total EU demand. The Company also extracts more than 4 million tonnes of thermal coal, and produces 3.5 million tonnes of coke per year. JSW derives about 50% of its revenues from sales in Poland, with 38% generated in other EU countries and 7% coming from India. Its mines are located in southern Poland, near the border with the Czech Republic. JSW's coking plant "Przyjaźń" is the largest non-vertically integrated facility of this type in the EU.

## JSW vs. WIG



Company	9MTP		Rating	
	new	old	new	old
JSW	60.68	60.68	hold	reduce

Company	Current Price	9MTP	Upside
JSW	59.96	60.68	+1.1%

Forecast Update	2018E	2019E	2020E
EBITDA (adj.)	0.0%	0.0%	0.0%
Net profit (adj.)	0.0%	0.0%	0.0%
Coking coal (US\$/t)	0.0%	0.0%	0.0%
Thermal coal (PLN/t)	0.0%	0.0%	0.0%
Coke (US\$/t)	0.0%	0.0%	0.0%
Coal production (kt)	0.0%	0.0%	0.0%
Coking coal prod. (kt)	0.0%	0.0%	0.0%
Coke production (kt)	0.0%	0.0%	0.0%

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**List of abbreviations and ratios contained in the report:**

**EV** – net debt + market value  
**EBIT** – Earnings Before Interest and Taxes  
**EBITDA** – EBIT + Depreciation and Amortisation  
**P/CE** – price to earnings with amortisation  
**MC/S** – market capitalisation to sales  
**EBIT/EV** – operating profit to economic value  
**P/E** – (Price/Earnings) – price divided by annual net profit per share  
**ROE** – (Return on Equity) – annual net profit divided by average equity  
**P/BV** – (Price/Book Value) – price divided by book value per share  
**Net debt** – credits + debt papers + interest bearing loans – cash and cash equivalents  
**EBITDA margin** – EBITDA/Sales

**OVERWEIGHT (OW)** – a rating which indicates that we expect a stock to outperform the broad market  
**NEUTRAL (N)** – a rating which indicates that we expect the stock to perform in line with the broad market  
**UNDERWEIGHT (UW)** – a rating which indicates that we expect the stock to underperform the broad market

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**ACCUMULATE** – we expect that the rate of return from an investment will range from 5% to 15%  
**HOLD** – we expect that the rate of return from an investment will range from -5% to +5%  
**REDUCE** – we expect that the rate of return from an investment will range from -5% to -15%  
**SELL** – we expect that an investment will bear a loss greater than 15%  
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**DCF** – acknowledged as the most methodologically correct method of valuation; it consists in discounting financial flows generated by a company; its weak point is the significant susceptibility to a change of forecast assumptions in the model.

**Relative** – based on a comparison of valuation multipliers of companies from a given sector; simple in construction, reflects the current state of the market better than DCF; weak points include substantial variability (fluctuations together with market indices) as well as difficulty in the selection of the group of comparable companies.

**Economic profits** – discounting of future economic profits; the weak point is high sensitivity to changes in the assumptions made in the valuation model.

**Discounted Dividends (DDM)** – discounting of future dividends; the weak point is high sensitivity to changes in the assumptions as to future dividends made in the valuation model.

**NAV** – valuation based on equity value, one of the most frequently used method in case of developing companies; the weak point of the method is that it does not factor in future changes in revenue/profits of a company.

**mBank issued the following recommendation for JSW in the 12 months prior to this publication:**

recommendation	reduce	reduce	sell	buy	buy	buy	buy	buy	buy	buy
issued on	2019-02-04	2018-12-05	2018-11-26	2018-09-03	2018-08-02	2018-07-04	2018-06-06	2018-05-09	2018-04-06	2018-03-05
target price (PLN)	60.68	59.14	59.14	98.00	108.69	107.00	115.23	109.12	108.14	120.71
price on rating date	68.30	71.20	72.56	77.00	79.50	77.50	86.66	79.32	86.78	92.80

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