



Focus  
Ukraine

Scope  
Bonds

Analyst  
Alexander Martynenko

# Metinvest

## 1H results solid, Donbass conflict has yet to take its toll

### Despite slipping revenues, EBITDA and balance sheet strengthen.

Metinvest reported revenues down 8% YoY to US\$6bn while EBITDA increased 29% YoY to US\$1.6bn and net income increased 46% YoY to US\$653m. The company also managed to reduce its total debt by 10% to US\$3.87bn as of 30 June 2014 from US\$4.3bn as of 31 December 2013. Metinvest's net debt/LTM EBITDA ratio declined to 1.5x as of 30 June 2014 from 1.9x as of 31 December 2013.

**Cheaper hryvnia and inputs offset lower sales.** Declining sales of finished steel, falling benchmark prices for iron ore, and weakening steel markets in Ukraine and Russia were among the key factors of the negative US\$238m effect for Metinvest's 1H14 EBITDA versus 1H13. However, the favorable movement in the UAH/USD rate gave Metinvest US\$820m of EBITDA savings, thus offsetting losses not only from weaker sales, but also from higher electricity, labor and other operating costs. Furthermore, lower prices for raw materials and natural gas contributed another US\$59m of earnings savings.

**Iron ore business withstands Donbass crisis.** During the 1H14 results conference call, management stated that Metinvest managed to redirect roughly 95% of its iron ore sales from internal and external consumers battered by military actions in the Eastern Ukraine to Europe and Southeast Asia. We find this development particularly positive for Metinvest in the current situation, although it is likely to cause additional costs of transportation and exposure to spot markets.

**Production in the conflict zone struggles to recover.** Management stated that Metinvest's assets, which had their production shut down in August because of combat, are on track to resume production. Management stated that while the restart costs are insignificant, the conflict stabilization and effective ceasefire remain the key issue as they would allow the full restoration of railway and electricity communications in two to four weeks. By year-end, Metinvest expects that its steel-making capacity utilization will grow from the current 0% to 20-50% at Yenakieve Steel and from 50% to 70% at both Azovstal and Mariupol Ilyich Steel.

**EBITDA under great pressure in 2H14.** Although hardly visible in 1H14, the impact of the military conflict should be reflected in the company's earnings in 2H14, with the most negative effect coming from production assets located in the uncontrolled zone that accounted for 12% of Metinvest's EBITDA in 1H14. The rest of the assets in the endangered region remain close to the battlefield and are subject to logistics problems which could result in capacity utilization coming in below the management's target. Weak global iron ore and steel markets do not look promising as we expect FOB Black Sea prices to be largely flat HoH in 2H14 and TSI 62% Fe prices for iron ore to be down 10-15% HoH.

THURSDAY, 23 OCTOBER 2014

### Key financial figures and ratios

	2011	2012	2013
<b>P&amp;L (US\$m)</b>			
Revenues	14,189	12,569	12,807
EBITDA	3,655	1,996	2,291
Net income	1,854	445	392
<b>Balance sheet (US\$m,eop)</b>			
Cash	792	531	783
Total debt	3,981	4,278	4,308
Net debt	3,189	3,747	3,525
<b>Cash flow (US\$m)</b>			
Net operating CF	1,944	1,146	1,465
Net investing CF	-1,454	-1,094	263
Incl. Capex	-1,064	-699	-763
Net financing CF	-148	-313	-1,476
Incl. dividends	-937	-575	-544
<b>Ratios</b>			
EBITDA mrg (%)	25.8	15.9	17.9
Net mrg (%)	13.1	3.5	3.1
EBITDA int cov (x)	10.3	6.2	6.7
Debt-to-EBITDA (x)	1.1	2.1	1.9
Net debt-to-EBITDA (x)	0.9	1.9	1.5
ST debt (% of total)	26.6	32.4	39.9

Note: eop – end of period; ST – short-term; CF – cash flow; ann – annualized; int – interest. Sources: Metinvest, ICU.

### Credit ratings

Moody's	S&P	Fitch
Caa2	--	CCC

### Outstanding Eurobonds

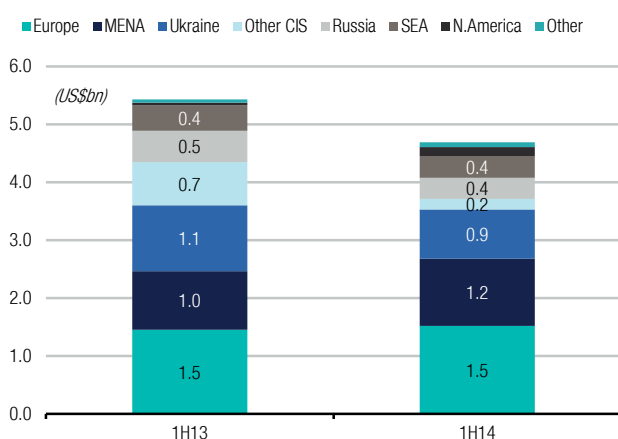
Maturity	Coupon (%)	Volume (US\$m)	Price (%)	YTW (%)	Spread (bp)
20-May-15	10.25	500	57.586	79.25	5,754
14-Feb-18	8.75	750	66.375	24.02	2,325

Source: Bloomberg

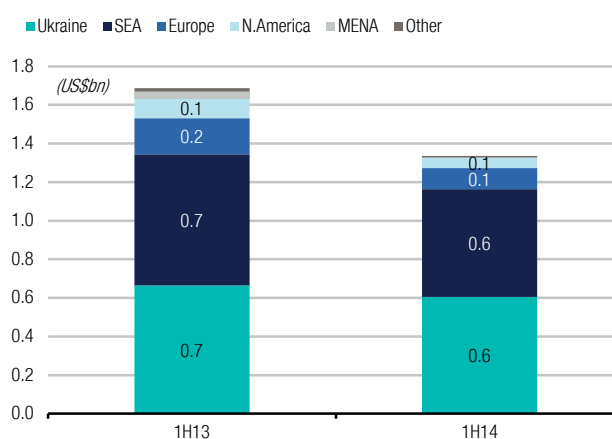
**Table 1. Summary of Metinvest's financial highlights**

US\$m	1H13	1H14	Change, YoY	
			US\$m	%
<b>Income statement highlights</b>				
Revenues	6,576	6,023	-553	-8
Adjusted EBITDA	1,252	1,609	357	29
EBITDA margin (%)	19	27		8pp
Net profit	446	653	207	46
Net margin (%)	7	11		4pp
<b>Cash flow highlights</b>				
Net cash from operations	889	766	-123	-14
Net cash used in investing activities	-242	-280	-38	16
incl. Capex	-290	-279	11	-4
Net cash used in financing activities	-796	-710	86	-11
incl. dividends	-284	-250	34	-12
<b>Balance sheet highlights</b>				
Gross debt	4308	3,865	-443	-10
Short-term debt	1,718	1,760	42	2
Long-term debt	2,425	1,980	-445	-18
Seller notes	165	125	-40	-24
Cash at the end of period	783	530	-253	-32
Net debt	3,525	3,335	-190	-5
<b>Key ratios</b>				
Total debt to EBITDA (x)	1.9	1.5		
Net debt to EBITDA (x)	1.5	1.3		

Source: Metinvest.

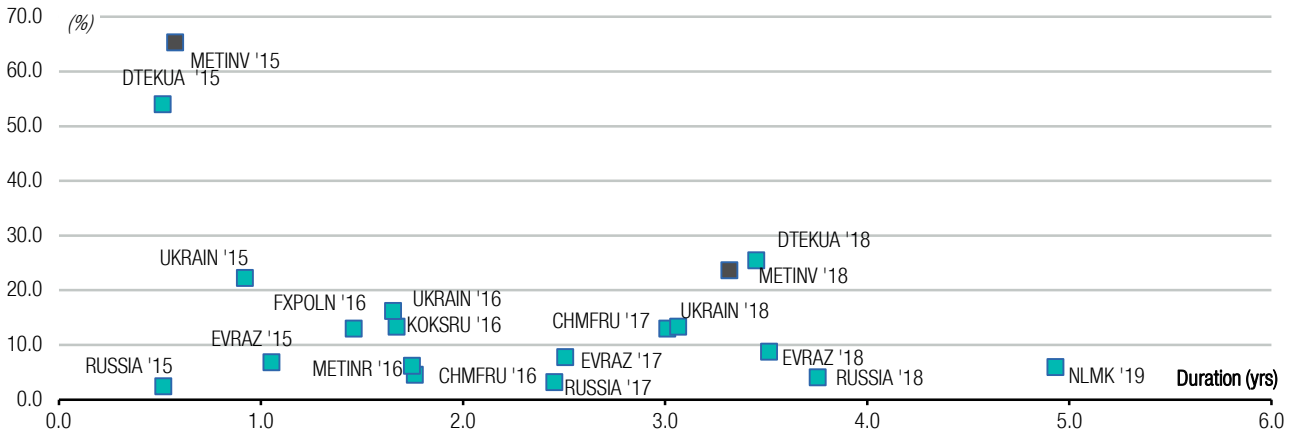
**Chart 1. Sales of Metinvest's metallurgical division by region**

Source: Metinvest.

**Chart 2. Sales of Metinvest's mining division by region**

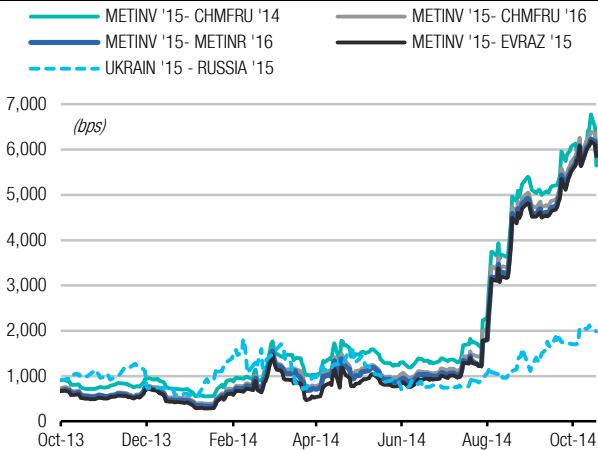
Source: Metinvest.

**Chart 3. Yields vs. duration of select Ukrainian and Russian issuers (%)**



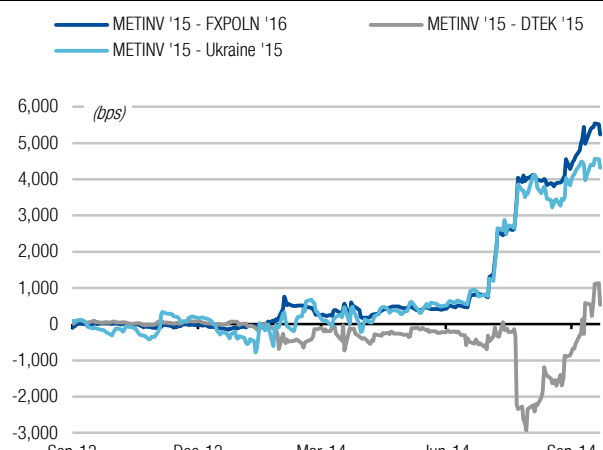
Sources: Bloomberg, ICU.

**Chart 4. Metinvest-15 spreads over select Russian issuers (bps)**



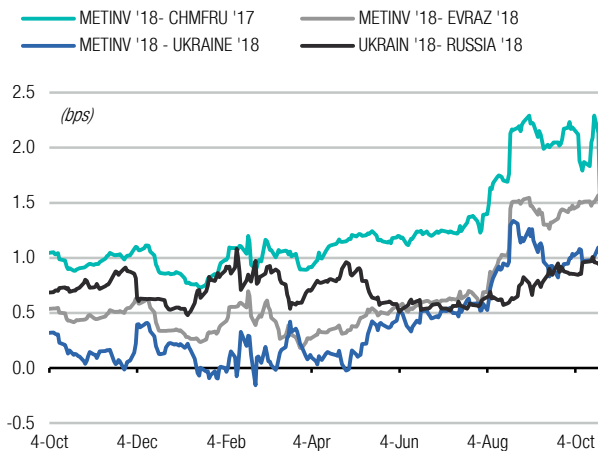
Sources: Bloomberg, ICU.

**Chart 5. Metinvest-15 spreads over select Ukrainian issuers (bps)**



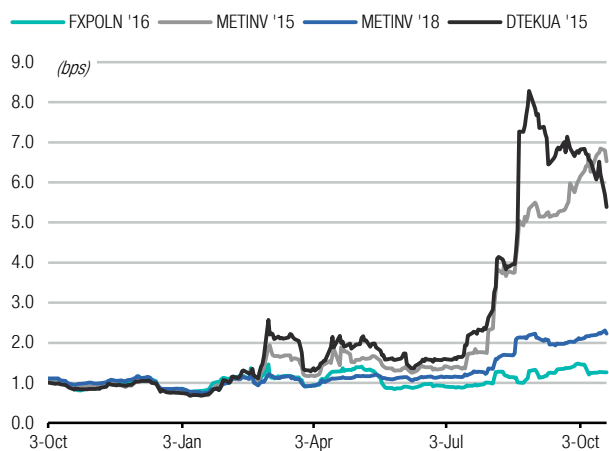
Sources: Bloomberg, ICU.

**Chart 6. Metinvest-18 spreads over select issuers (bps)**



Sources: Bloomberg, ICU.

**Chart 7. Mid benchmark spreads of Ukrainian industry issuers over US T-notes (bps)**



Sources: Bloomberg, ICU.

# Disclosures

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**Buy:** Forecasted 12-month total return greater than 20%

**Hold:** Forecasted 12-month total return 0% to 20%

**Sell:** Forecasted 12-month total return less than 0%

Note: total return is share price appreciation to a target price in relative terms plus forecasted dividend yield.

## DEBT RATING DEFINITIONS

**Buy:** Forecasted 12-month total return significantly greater than that of relevant benchmark

**Hold:** Forecasted 12-month total return is in line with or modestly deviates from relevant benchmark

**Sell:** Forecasted 12-month total return significantly less than that of relevant benchmark



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