ArcelorMittal Research

Description: They are based in Luxembourg and owns and operate steel manufacturing and mining facilities in Europe, North and South America, Asia, and Africa.

Ticker: MT

Price: $20.72

Market Cap: $20.8B

Performance: -35.7% YTD

Analysis:

This is now our second analysis done on a company in the steel industry. We did some research a couple months ago saying that we would avoid U.S. Steel (X) when it was trading at $27-28 per share, today it's at $18. Similar to X, MT has also pulled back very hard. In the same time frame, MT has fallen from $25 to $20.

We didn't think the industry was a buy then so the question is do we think it's a buy now? We are siding with not yet. There are still a lot of headwinds in the industry but the investment is starting gain attraction.

MT is one of the largest steel manufacturers in the world. For reference, over the last twelve months they've raked in $75.4B in revenue while others like Nucor (NUE), U.S. Steel (X), Steel Dynamics (STLD) have brought in $23.9B, $13.6B, and $11.3B, respectively.

MT is a very tough business to analyze as they have a lot going on. For example, the company is very aggressive on their international expansion. Here are some recent examples on top of the 160 countries they do business in:

- They've acquired Essar, largest flat integrated steel company in Western India, for an upfront payment of $5.7B and an additional capital injection of $1.1B to kickstart the business
- They've restarted their $330M investment program at their Vega unit in Brazil
- They're investing $1B in Mexico over the next 3 years to better serve the market

We view these investments as a positive as India, Mexico, and Brazil should outpace a large percentage of markets for demand in steel.

MT operates in three main businesses:

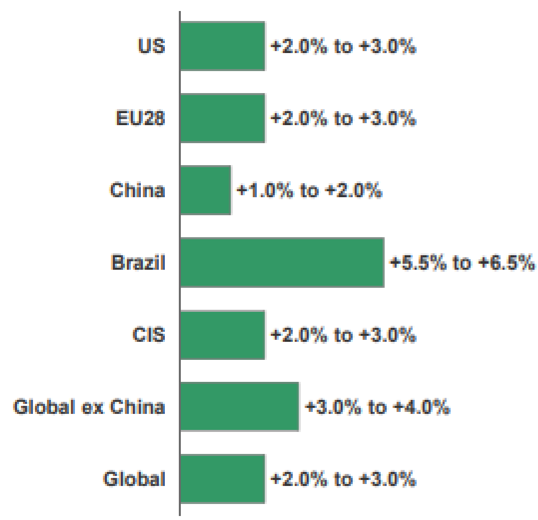
1. Steel
    a. Through 9M'18 steel-only EBITDA is up +43.9% YoY primarily due to positive price-cost effect with all segments improving
    b. On a QoQ basis, 3Q'18 steel-only EBITDA fell 11.5% vs. 2Q'18
2. Mining
    a. In 3Q'18 EBITDA declined 8.1% QoQ primarily due to lower market priced iron ore shipments (-14.4% QoQ)
    b. Growth: Market priced iron ore shipments are expected to grow ~5% in 2018 YoY (down from previous guidance of ~10% growth)
    c. Free cash flow breakeven is $40/mT
3. Investments
    a. Income from associates, joint ventures and other investments for 9M 2018 was $425M as compared to $323M for 9M 2017

Overall, year-to-date this is how MT is performing:

- Total steel shipments for 9M 2018 were 63.6 million metric tonnes representing a decrease of 1.0% as compared to 9M 2017, primarily due to lower steel shipments in ACIS (-7.8%) offset in part by improvement in Brazil (+8.0%), NAFTA (+1.1%) and Europe (+0.4%).
- Sales for 9M 2018 increased by 13.2% to $57.7 billion as compared with $51.0 billion for 9M 2017, primarily due to higher average steel selling prices (+15.3%) offset in part by lower steel shipments (-1.0%).

- Net interest expense was lower at $475 million for 9M 2018, as compared to $635 million for 9M 2017, driven by debt repayment and lower cost of debt.
- Foreign exchange losses for 9M 2018 were $227 million primarily related to the effect of the depreciation of the U.S. dollar in 1Q 2018 against the euro on the Company's euro denominated debt as compared to foreign exchange gains of $463 million in 9M 2017
- ArcelorMittal's net income for 9M 2018 was $4.0 billion, or $3.89 basic earnings per share, as compared to a net income in 9M 2017 of $3.5 billion, or $3.46 basic earnings per share.

On regional basis, this is what MT expects 2018 steel demand to end up at:



*Note that CIS is Azerbaijan, Armenia, Belarus, Kazakhstan, Kyrgyzstan, Moldova, Russia, Tajikistan, Turkmenistan, Uzbekistan and Ukraine. If there is an A in front of CIS, that's referring to Africa.

Let's take a minute and analyze some of these stats we just covered that we believe deserve some light. Off the bat, rev growth and EPS growth is healthy along with the net interest expense coming down due to deleveraging (more on debt later). Earlier we spoke about how MT has a large international presence. This is a good thing but also has some negative side effects. For example, take a look at what happened. Since the dollar is having a great year against the Euro they've realized a loss of $227M on their debt vs. the strong Euro in 2017 that led to a gain of $463M. We believe the dollar will continue to strengthen against the Euro in

2019 and that could in fact lead to more losses in this department. (More on why we think this will happen in our 2019 outlook).

Moving onto the balance sheet. MT looks to be okay in this area but not amazing. The company has gross debt of $13.0B as of September 30, 2018. After deducting their $2.5B in cash, their net debt sits at $10.5B. While this is a lot, the company also has a $5.5B line of credit so they shouldn't have a problem paying off their next two maturities of $2.3B in Dec 2019 and $2.1B in 2020. As far as the credit rating agencies go (take with a grain of salt LOL), they have MT as investment grade with Moody's rating them Baa3 and S&P & Fitch both rating them BBB-.

Before we wrap up let's compare MT with NUE, X, and STLD.

	MT	NUE	X	STLD
Forward P/E	12.2x	7.5x	2.9x	6.1x
P/S	0.3x	0.7x	0.2x	0.6x
Levered Free Cash Flow	$1.1B	$457M	$202M	$492M
Net Debt / EBITDA	1.0x	0.6x	0.9x	0.7x
Y/Y Rev Growth Rate as of latest Q	5.0%	30.4%	14.8%	32.0%
YTD Performance	-35.7%	-16.0%	-50.6%	-32.4%
PEG	0.3x	0.8x	0.2x	0.5x
Dividend Yield	2.29%	2.90%	1.09%	2.50%

Looking at the table above, we still favor Nucor (NUE) over all of the other names. This has proven to be the best trade out of all of them so far as it has held up the best and still holds the highest dividend yield. We still wouldn't own these names just yet though but some major catalysts would be any kind of U.S. trade deal with China and the EU, as well as stronger data out of all of the countries mentioned already. It should also be noted that MT is a big player for providing steel for automobiles and we are seeing a bit of a trend of auto manufacturers coming back to steel blends to build their cars due to increased technology to make them lighter and sturdier than aluminum. Examples include the 2019 Chevy Silverado, Audi A8's, and the new Tesla Model 3's. It is also worth noting that in MT's core markets, they have 40% market share in the auto industry.