

OSAKA STEEL CO LTD (5449: TYO)

SECTOR: BASIC MATERIALS (SMALL-CAP)

Current Price:	2092 ¥
1 YR Change:	-6.23%
Incorporation:	1978
Beta (Public Source):	0.9247
Valuation Type:	Value

Company Description

OSAKA STEEL CO., LTD. is a company mainly engaged in the steel business. The Company is engaged in the manufacture and sale of various types of (recycled) steel products, such as shape steels, flat steels, steel bars, square steel bars and steel processed products. Through subsidiaries, the Company is also engaged in the provision of delivery services and premises operation business. Ready for acquisitions, Osaka Steel is relatively cheap.

SWOT

Strength	Weaknesses
<ul style="list-style-type: none"> - Core EAF steelmaker for parent group. - Strong balance sheet with higher profitability than industry. - Recycled steel is environment friendly and besides, there will always be steel available to recycle. 	<ul style="list-style-type: none"> - Japanese & small cap. Portfolio restrictions like daily turnover may not be appealing to many. - Steel industry is still in a rough patch towards recovery. - Volatile scrap prices and reduced Japanese steel exports.
Opportunities	Threats
<ul style="list-style-type: none"> - Merger of Nippon & Sumitomo Group provides more growth opportunities. - Market share in recycled steel will increase through acquisitions as balance sheet can support acquisitions. 	<ul style="list-style-type: none"> - Further weakening of sales. - Fall in infrastructure spending. - Overseas cheaper competitors like Bao Steel subsidiaries.

Poor Man's Valuation:

(millions ¥)	Cash From Operations 5 Years	Capex 5 Years	Free Cash Flow 5 Years	1 Yr Current Assets - All Liabilities	WACC	Shares Outstanding (m)	Expected Market Cap.	Share Price	Cheap or Expensive
Basic Valuation									
Historical	37466	14948	22518	80409				¥2.092	Cheap
Forecasted									
Base Case 20 Years	149864	59792	90072	80409	10%	42,28	105855	¥2.504	20%
Bull 20 Year Forecast (+40%)	209810	83709	126101	80409	10%	42,28	128226	¥3.033	45%
Bear 20 Year Forecast (-40%)	89918	35875	54043	80409	10%	42,28	83484	¥1.975	-6%

Investment Summary

Essentially an ESG case, Osaka Steel is the core Electric Arc Furnace (EAF) steelmaker for Nippon Steel & Sumitomo Group. Osaka Steel is relatively cheap on free cashflow basis and greatly undervalued considering its balance sheet strength. Total Japanese steel production is ~ 120 million tons whereas 30% is recycled by EAF operators. Osaka produced 1.1 million tons of the recycled production and with clean balance sheet, consolidated parent, I believe the company can turn into a mid-cap in five years of time. What market currently prices is free cashflows, but not the balance sheet where current assets essentially cover the entire liability side many times over. Even with falling revenues, operating income increased showing management resilience. A good enterprising firm that is being overlooked by the market, risks include large holdings from the parent which essentially limit the free float or daily turnover available for investors.

CHEAP

Average volume	18.12k
Free float	15.11m
P/E (TTM)	8.64
EPS (TTM)	234.34 JPY
Shares outstanding (m)	42.28
Market cap	85.57bn JPY

FINANCIALS

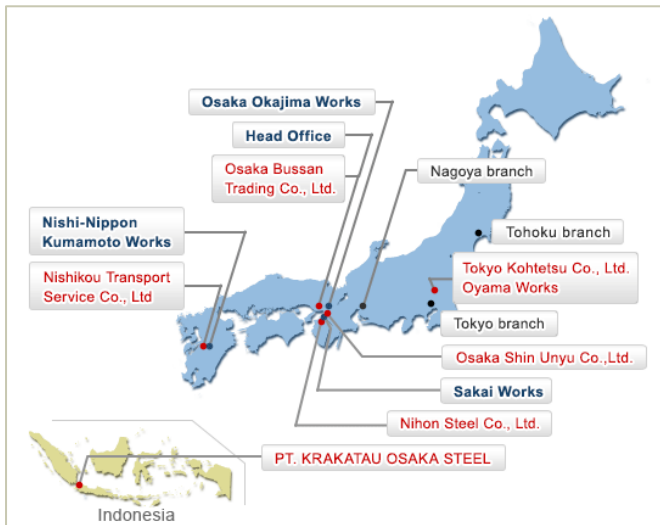
	Osaka	Industry
Current Ratio (MRQ)	9.42	1.56
Quick Ratio (MRQ)	8.45	1.09
LT Debt/ Equity (MRQ)	3.25	55.96
Price to Sales (TTM)	1.63	0.98
Price to Book (MRQ)	0.59	0.80
Price/ Tang. Book (MRQ)	0.64	0.83
Inventory Turn. (TTM)	4.03	2.99
Payout Ratio (TTM)	16%	13%

VALUATION

Base Growth Rate	2%
Wacc	10%
Forecast Period FCF (m)	11014
Terminal value (m)	140432
PV terminal value (m)	87197
Total EV	98212
Debt	372
Cash	12469
Equity Value	110309
Shares Outstanding (m)	42.28
Fair Value Share Price	¥2,609

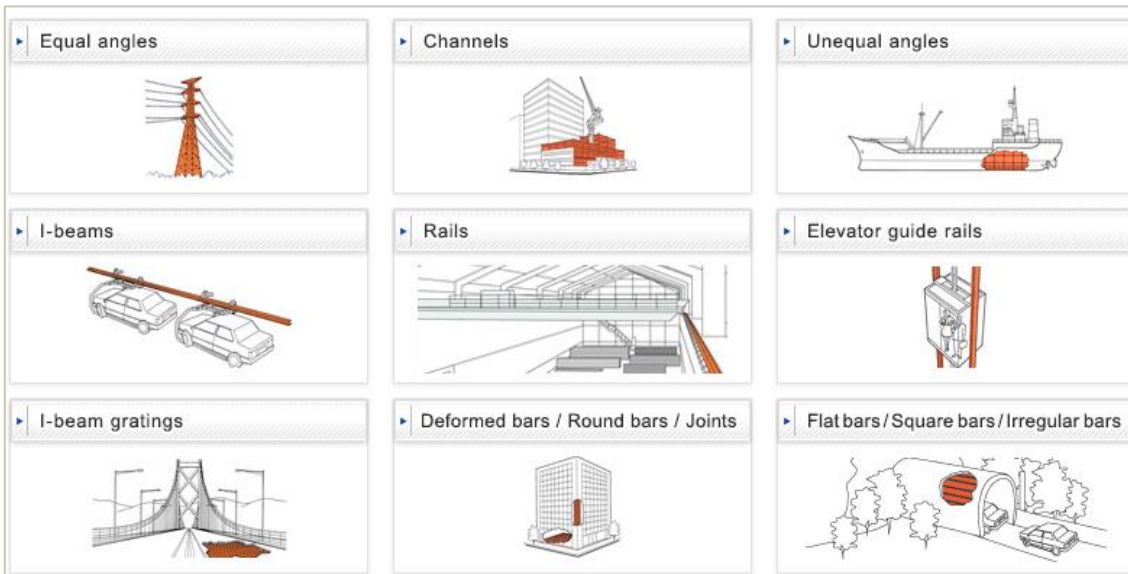
Segments Source: Annual Report/Company Website

Locations



- Rising steel production across Japan.
- Acquisitions include Tokyo Kohetsu Co. The company was also engaged in the manufacturing of structural steel beams.

Product Applications.



World Steel Association

MONTHLY CRUDE STEEL PRODUCTION
thousand tonnes

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	2016 21 Nov 16 Total
China	62 555 e	58 515 e	70 653	69 421	70 504	69 469	66 807	68 571	68 170	68 510			672 960
India	7 501	7 451	8 316	7 694	7 989	8 036	8 082	8 141	8 044	8 267			79 521
Japan	8 768	8 345	8 726	8 500	8 940	8 770	8 977	8 909	8 453	9 062			87 450
South Korea	5 677	5 087	5 731	5 643	5 821	5 482	6 020	5 870	5 717	5 961			57 009
Pakistan	250	382	349	257	260	250	273	290	270 e	290 e			2 871
Taiwan, China	1 790	1 660	1 807	1 799	1 862	1 826	1 855	1 841	1 800 e	1 860 e			18 100
Thailand	304	316	329	331	358	286	287	327	340 e	350 e			3 229
Asia	86 846	81 755	95 911	93 646	95 735	94 119	92 300	93 949	92 794	94 300			921 140

MONTHLY CRUDE STEEL PRODUCTION
thousand tonnes

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	2015 21 Nov 16 Total
China	67 455	60 925	68 659	69 074	69 253	68 309	65 117	66 573	65 611	65 875	63 315	64 372	803 823
India	7 506	7 201	7 797	7 426	7 593	7 422	7 477	7 442	7 264	7 359	7 234	7 305	89 026
Japan	9 022	8 441	9 282	8 403	8 923	8 532	8 842	8 785	8 570	9 010	8 740	8 585	105 150
South Korea	5 932	5 049	5 927	5 745	6 019	5 859	5 919	5 763	5 654	6 086	5 847	5 870	69 670
Pakistan	201	251	240	251	262	251	204	250	230	236	260	255	2 892
Taiwan, China	1 987	1 777	2 081	1 876	1 899	1 791	1 817	1 708	1 609	1 692	1 515	1 619	21 370
Thailand	367	321	323	298	326	317	318	304	326	280	246	293	3 718
Asia	92 470	83 966	94 309	93 073	94 275	92 481	89 695	90 825	89 264	90 538	87 157	88 299	1 095 650

Model & Assumptions

Revenue Builder	2015	2016	2017e	2018e	2019e	2020e	2021e
Total Revenue	67.678	54.677	49.209	46.749	47.684	50.068	55.075
% growth	-2%	-19%	-10%	-5%	2%	5%	10%
EBIT	8.813	10.614	10.334	8.882	9.537	10.514	12.116
% sales	13%	19%	21%	19%	20%	21%	22%
Capex	6.152	3.240	2.934	2.788	2.843	2.985	3.284
% sales	9%	6%	6%	6%	6%	6%	6%
Depr. & Amort.	2.276	2.400	1.968	1.870	1.907	2.003	2.203
% sales	3%	3%	4%	4%	4%	4%	4%

Explanation

- > Sales conservatively modelled. Upside visible even with harsh revenue forecasting.
- > EBIT rises gradually peaking at 22%. Management is relatively efficient in fast cost cutting.
- > Capex forecasted per historical figures and kept constant going forward.
- > Depreciation and amortization expected to be stable at 4%.

Reporting Quality

Annual Report	No comprehensive annual report available.
Auditor's Opinion for Parent Organization	KPMG: Clear.
ESG & Sustainability reporting	High.

Explanation

- > No comprehensive annual report was available in English besides the consolidated financial results. Little data was available from the annual report of Osaka's parent.
- > Auditor's opinion was clear for the parent.

ESG Materiality Matrix Reported & Assessed	N/A
Quantitative Identification of all key ESG metrics	N/A

Usefulness of ESG metrics in current scenario?

The company produces recycled steel and is majority owned by the parent. Apparently, it serves as the "ESG" image portfolio for its parent company. The nature of business is a bit more stable than the parent since Osaka is more focused on recycling steel and building products for different applications.