



Recommendations & Relative Value

ArcelorMittal (MTNA): Initiating on all USD-denominated bonds with Buy Ratings

Investment Rationale

We initiate on all of MTNA's USD-denominated bonds with a Buy rating owing to our belief that the company will benefit from increased cash flow in 2018 on the back of stabilizing to growing global demand trends and apply that cash to further deleverage the organization. MTNA's net debt has declined almost 45% over the last 5 years and its bond ratings reflect that (Ba1, BB+). Management continues to make achieving investment grade credit ratings its highest priority. MTNA benefits from very strong leverage to increasing steel prices; hence, with global pricing increasing YoY in Q4-2017, cash flow and leverage should continue on their positive trajectory. With a FCF yield is greater than 20% amid minimal 1.5x net leverage and an almost entirely unsecured capital structure, we view MTNA as likely to achieve IG ratings at some point in the near-term and their decision to repurchase some of the more expensive 2039 and 2041 notes as a sign of strength. Therefore we believe the bonds will trade closer to IG indices than HY indices going forward and see MTNA as a "rising star."

Risks

Risks to the downside include growth-oriented M&A, slowing Chinese demand trends, input cost inflation, a reversal of MTNA's decision to achieve IG ratings, softer global economic trends, regulatory changes and lower steel prices.

Company Description

ArcelorMittal (MTNA) is the world's top integrated steel and mining company. As of 2016 MTNA had steel production capacity of 113 million tonnes. For the LTM period ended September 2016 MTNA shipped 84.2mn tonnes of steel. Created in 2006 owing to the merger between Mittal Steel Company N.V. and Arcelor, MTNA is the largest steel producer in the Americas, Africa and Europe, the fifth largest steel producer in CIS and has operations in 18 countries on four continents. MTNA's asset base includes 51 integrated and mini-mill steel-making facilities. MTNA also has a leading market share in its core markets in the automotive steel business and is a leader in the fast-growing advanced high strength steels segment. Geographically, MTNA is well diversified across both developed and developing markets. MTNA produces ~37% of its crude steel in the Americas, ~47% in Europe and ~16% in other countries such as Kazakhstan, South Africa and the Ukraine. The company produces a broad range of high-quality finished and semi-finished steel products including flats (sheet and plate) and long products (bars, rods etc.). In addition, MTNA makes pipes and tubes for various applications. The company sells its steel products primarily in local markets and through its centralized marketing organization to a diverse range of customers including the automotive, appliance, engineering, construction and machinery industries in approximately 160 countries.

MTNA also has vertically integrated iron-ore and coal mining operations across the Americas, Africa, Europe and CIS. The Company produces various types of mining products including iron ore lump, fines, concentrate and sinter feed, as well as coking, PCI and thermal coal. In 2016, ~55% of the company's iron-ore requirements and ~15% of its PCI and coal requirements were supplied from its own mines or pursuant to strategic contracts with third-party suppliers. Furthermore, it is a significant producer of coke and ~92% of its coke needs are satisfied through its own production facilities. The company's facilities have good access to shipping facilities, including through its own 16 deep-water port facilities and linked railway sidings. MTNA benefits from its own downstream steel distribution business primarily run through its European segment. MTNA also provides value-added and customized steel solutions.