



Steel Dynamics, Inc. (STLD): Reiterate Hold Ratings due to the increased likelihood of a debt-funded acquisition

On October 19, 2017 we published an earning's update for Steel Dynamics, Inc. (STLD). Excerpts from that publication are supplied below for review.

3Q17 Earnings Summary

STLD announced 3Q17 results largely in line with consensus' expectations. EBITDA of \$347mn (-3% y/y) came in 1% lower than consensus' \$352mn estimate as average scrap costs expanded more than average selling prices in the period, resulting in some near-term margin compression. Revenue of \$2.443bn (+16% y/y) outperformed consensus' estimate for \$2.389bn by 2% due to stronger infrastructure shipments that offset softening auto volumes.

Cash Flow, Leverage & Liquidity

OCF before changes in W/C of \$245mn was \$8mn lower y/y primarily owing to increased cash taxes. W/C consumed \$18mn resulting in OCF of \$226mn. We estimate STLD generated organic FCF of ~\$183mn after subtracting capex of \$43mn from OCF. STLD also spent \$6mn on acquisitions, paid dividends of \$37mn and repurchased \$99mn of stock bringing net cash flow to ~\$41mn. Cash was \$1.1bn against debt of \$2.534bn, resulting in 1.0x net and 1.8x total leverage off \$1.377bn of LTM EBITDA. Liquidity was substantial at \$2.1bn.

Recommendation

STLD's cash balance ballooned to over \$1.0bn in 3Q17 and management made it clear to investors that they are evaluating several inorganic opportunities in the market but would seek to keep a lid on leverage ~3.0x should they proceed with one. Hence, given the increasing likelihood STLD executes a debt-funded acquisition that could prime or layer existing senior notes (which are already trading at tight spreads), we maintain our Hold recommendations on STLD's existing notes despite our opinion that STLD is a great operator with a solid >20% FCF yield.

Risks

Upside and downside risks to our recommendation include: growth or declines in the value between scrap steel prices and market selling prices, which in turn benefits/hurts profits at STLD; possible leveraging acquisitions given STLD's modest 1.0x of net leverage, robust cash balance and pristine balance sheet; high exposure to cyclical end markets including the automotive sector, the construction sector, energy and manufacturing; any rise/decline in imported steel products into the U.S., which could impact STLD's capacity utilization, sales volumes, selling price realizations and, in turn, credit metrics.

Figure 6: Steel Dynamics, Inc. (STLD) 3Q17 Capitalization

Capitalization	Amount	Bid / NL	Mkt Value	YTW / NL
Cash & Equivalents as of 9/29/17	\$1,102		\$1,102	
(L+150) \$1.2BN Sr RCF due Nov-19	0		0	
Other Secured Debt	34		34	
Sr Secured Debt	\$34	(0.8x)	\$34	(0.8x)
\$700MM 5.125% Sr Nts due Oct-21	700	102.250	700	3.8%
\$400MM 5.250% Sr Nts due Apr-23	400	102.750	400	4.3%
\$500MM 5.500% Sr Nts due Oct-24	500	105.750	500	3.6%
\$350MM 4.125% Sr Nts due Sep-25	350	100.375	350	4.0%
\$400MM 5.000% Sr Nts due Dec-26	400	105.500	400	4.1%
Other Debt	150		150	
Total Debt	\$2,534	1.0x	\$2,534	1.0x
Market Capitalization as of 12/22/17	\$10,251	7.4x	\$10,251	7.4x
Total Enterprise Value	\$12,785	8.5x	\$12,785	8.5x

Source: Deutsche Bank, Company Reports