

Steel Firms Eye Bond Market Issuance

By [The Moscow Times](#)

March 20, 2013

The  **Moscow Times**

If Russian issuance last year was dominated by financials raising capital ahead of the transition to Basel III, then 2013 could turn out to be the year that the metals and mining sector leads the way.

Companies such as Evraz, MMK, Norilsk Nickel and Severstal are rumored to be preparing bond issues, with others, particularly gold firms, thought to be waiting in the wings.

So far, NLMK is the only Russian company from the sector to have raised funds in the international bond market this year, selling an \$800 million five-year deal in early February.

But the pipeline, which is led by Russia's largest steel manufacturers, is under construction. There are several request for proposals (RFP) for steel makers, one debt capital market (DCM) syndicate banker said, and a number of companies are likely to be eyeing issuance over the coming weeks, if conditions allow.

The sector is a key one this year because demand is as strong as it has ever been as U.S.

investors and others are desperate for credits that offer comparatively high yields. Issuers, meanwhile, are aware that a recession in Western Europe, a key export market, may lead to worse figures this year and a weaker credit story in the future.

Now is the perfect time to issue, bankers and analysts agree. "U.S. investors in particular are showing more interest in mining companies in Russia," said Peter Archbold, head of basic materials, EMEA (Europe, Middle East and Africa) corporate finance, at Fitch Ratings. "That really is in contrast to previous years: Previously, I had very few calls from the American market for European and Russian metals and mining issuers."

This demand is already seen in the secondary markets, with cash prices on the Evraz curve, for example, climbing steadily since summer 2012. This is because it is one of the only "yieldy" names in emerging EMEA, a trader told the International Financing Review.

Unlike their oil and gas counterparts, most steel companies are sub-investment grade, with the exception of NLMK, and the biggest ones are in the double B category. This means they offer a decent amount of yield, but the risk is not high enough to scare away investors.

Shrinking Profit Margins

The other reason is that several of these companies want to issue debt based on 2012 or early 2013 accounts because profit margins are expected to shrink, a syndicate official said. "They want to finish it off now, because the situation is only going to get worse with Europe the way it is at the moment."

Large parts of Europe, a key export market for Russian steel firms, are either in recession or experiencing a slowdown in GDP growth. China, another key market, is expected to have GDP growth closer to 7 percent than the 10 percent it recorded in the past.

"The steel sector is mired in a recession given the chronic overcapacity and lack of supply side discipline, and we expect razor thin steel making margins to last [into the] next decade," said Mikhail Stiskin, a senior analyst with Sberbank investment research. "The equity valuations of most Russian steels look stretched given the headwinds, and we broadly retain a downbeat stance."

However, there is a risk that if companies increase their debt pile as EBITDA margins shrink, it may adversely affect their leverage ratios.

"It depends on what they are doing with the debt that they raise," Archbold said. "If they are using it to extend their maturity of their debt profile or to refinance existing debt, that is not necessarily an issue."

Indeed, one banker said he believes that most of the activity will be refinancing driven, in particular of loans, rather than new money being raised for expansion.

The high-yield names that have strict covenant packages stipulating debt-to-EBITDA ceilings will, in particular, seek to refinance outstanding loans before they roll off, the banker said, as once the debts mature and the earnings environment deteriorates, these issuers will have less room for maneuver in case they breach their terms.

"It will be a matter of looking at the outstanding debt stock in a challenging market for metals and mining companies and making it more efficient," the banker said, adding that with yields at near historical lows, the bond market was a more attractive option than the loan market.

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