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Evraz Sees Weaker Q3, Rising Domestic Demand

By The Moscow Times

September 02, 2010



Evraz Group expects that core profit will have slipped in the third quarter, despite improving Russian demand, because of volatile prices and concerns about a sustainable economic recovery, the company said Thursday.

The weaker profit outlook and a wider-than-expected first-half net loss drove the company's London-listed stock down 1.9 percent to $26.75, while the market finished up 0.1 percent.

Evraz — which also has operations in the United States, Canada, Italy, Ukraine, Czech Republic and South Africa — said its three Russian mills were running at full capacity, and its foreign plants had boosted capacity use.

Major Russian steelmakers increased output in the second quarter in the hopes that the trend of weaker prices in the early summer months would turn around in the fall.

In May, Evraz forecast a sharp rise in second-quarter earnings before interest, taxes, depreciation and amortization to $725 million to $825 million, after $424 million in the first quarter.

First-half EBITDA was $1.15 billion, suggesting that the second-quarter figure was at the lower end of the range. The company cautioned, however, that core earnings would decline in the third quarter to the $480 million to $550 million range.

Evraz recorded a net loss of $270 million in the first half, which it blamed on depreciation-related one-off items.

CEO Alexander Frolov told a conference call that there would be no dividend for the year.

Interest expense on the company's $7.2 billion in net debt was the biggest loss maker, Renaissance Capital said in a note.

"In our view, Evraz could not avoid losses at the net profit line, taking into account the downturn in steel prices in May-June," Renaissance said.

The company must repay $1.1 billion in the next 12 months, chief financial officer Giacomo Baizini told a conference call. It will refinance the full amount, though the company has $700 million in cash, he added.

"We don't really see profit or returning to profit as one of our major targets," Baizini said in an interview to Reuters.

Evraz instead focused on healthy volumes, especially in Russia, where an acceleration of government-funded construction projects in particular boosted demand by 30 percent from the first half of 2009.

Key projects included infrastructure development in preparation for the 2012 Asia-Pacific Economic Cooperation summit in the Far East and the 2014 Sochi Olympics, Frolov said.

"There is potential for continued growth because, in volume terms, the pre-crisis level has not been reached. There is another 15-20 percent to go," Frolov told the conference call.

Analysts said that might be cold comfort for investors, as the outlook for Russia's own growth dims.

"The main future driver of Evraz's equity story should be the recovery of construction activity in Russia," Citi analyst Daniel Yakub wrote. "Recovery of the domestic construction market demand back to pre-crisis levels may take some time, unless growth rates accelerate."

Evraz expects to raise prices for its semi-finished steel by as much as 31 percent in the fourth quarter, rebounding from a slump in June and July.

The company has begun talks with clients on supplying slab steel and sees prices reaching $600 per metric ton, senior vice president Pavel Tatyanin said on a conference call. The figure compares with the average second-quarter semi-finished steel price of $457 that Evraz reported July 15.

(Reuters, Bloomberg)

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