Flashnote

HSBC Global Research

Natural Resources & Energy
Metals & Mining
Equity – Global

HSBC Steel Weekly

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Signs of weakness in the Chinese iron ore market

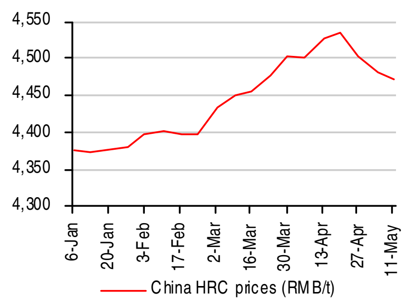
- **Chinese HRC and iron ore prices continue to decline**
- **Narrowing spread between 58% and 62% Fe-content iron ores is a sign of cost-cutting by Chinese steel mills**
- **Unusually, some recent Vale cargoes have sold below index pricing, possibly a sign of distressed cargoes reaching China**

Chinese steel and iron ore prices still falling

Chinese prices of both HRC and spot iron ore continue to decline, reflecting concerns of over-production of Chinese steel and weakening demand into the slower summer months. China's RRR cut on 12 May failed to buoy the market; in fact it was widely interpreted as confirmation the economy is slowing.

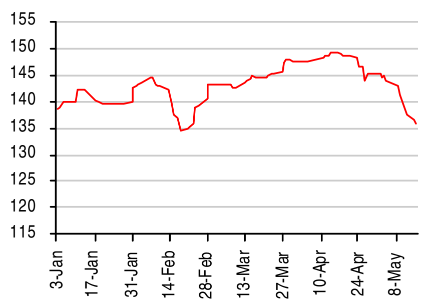
Confidence in the market is waning. Steel producers are reluctant to cut production for fear of losing market share, and yet demand is weak. Chinese steel traders cut HRC prices by another RMB100/t this week in an effort to shift inventories.

Chinese HRC prices (RMB/t)



Source: Steel Business Briefing

62% Fe-content iron ore, CFR China (USD/t)



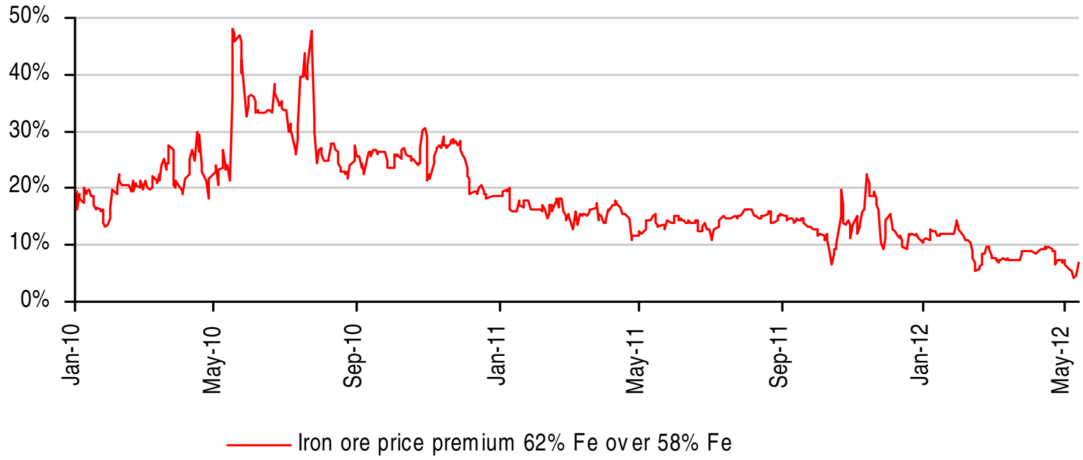
Source: Steel Business Briefing

Narrowing spreads between grades

We note that the spread between the price for 62% Fe-content iron ore and the lower-grade 58% Fe-content material has declined sharply over the past few weeks. It reached an all-time low of just 5.5% on May 9, with 62% material trading at USD141.3/t CFR China and 58% material trading at USD133.9/t, and has since rebounded to 6.9%.

In fact, the spread has been declining since mid-2010. The average price premium of 62% material over 58% material was 26% in 2010, 15% in 2011 and just 9% so far this year. *Continued next page.*

Iron ore price premium 62% Fe over 58% Fe



Source: Steel Business Briefing, HSBC analysis

Since iron ore prices were effectively 'floated' in April 2010 – one factor behind the destruction of Chinese steel making margins – steel makers have sought to reduce costs by using a greater proportion of lower-grade iron ore. Demand for lower-grade ores has strengthened relative to demand for higher-grade ores, resulting in a narrowing of the 'grades spread'.

The Steel Index's 58% Fe-content iron ore index includes material with 55-60% Fe-content, with a maximum of 8% silica and 5% alumina, regardless of origin. It includes, for instance, most mid-grade Australian iron ores such as BHP's Yandi fines (57.5% Fe-content, 5.5-6.0% silica). What the indices do not show is that most Indian iron ore supplied into China this year has been 50-55% Fe-content material. This is too poor a quality to be included in the iron ore price indices – but not too poor to be used by many Chinese steel makers.

It is worth noting that the Platts indices for differing ore grades actually show the opposite trend; the Platts 62%/58% premium has risen from 12% in early February to 14% now. One reason for this is the Platts index excludes much of the mid-grade Australian ores because of a silica content cut-off of 5% but does include Indian ore from producers such as Sesa Goa and Fomento, who sell less than 55% Fe-content material. Australian ores tend to attract a premium to Indian mid-grade material. As a result, the Steel Index indices tend to narrow more than the Platts indices when times are tough.

Vale trades seen below index spot prices

Another sign that demand is weak is that since late April, a number of shipments of Vale iron ore have been sold at (adjusted) prices that are below the 62% Fe-content index. This is unusual because Vale's iron ore enjoys both a quality and, in China, brand premium and usually trades above the index price. Adjusting the Vale prices for the differing silica and alumina contents shows that a typical Vale cargo may attract a premium to the index of roughly USD2/t. Yet some recent trades have been priced at USD2-4/t below the index price.

We acknowledge the contribution of Sumit Shekhar, Associate, Bangalore, in the preparation of this report.

There are a couple of possible explanations. First, some recent cargoes have been of <64% Fe-content material; the standard specification for Vale's Standard Sinter Feed Tubarao (SSFT) fines is 65%.

Second, we may be seeing some distressed European cargoes coming into China. Typically for trades to be included in the iron ore price indices, they have to fall within the 2-8 week 'forward delivery window'. For trades that are priced less than 2 weeks before delivery there is the concern the seller was 'panic selling' at prices not representative of the market. This rarely happens with Australian cargoes because they are usually sold prior to loading, but the long shipping time between Brazil and China means that Brazilian cargoes are often sold en route.

According to Platts, Vale has sold at least 12 cargoes on spot market terms so far this month. According to Steel Business Briefing, Platts rejected one cargo of 104,000 tonnes of 63.9% FE-content SSFT fines, traded on 9 May, precisely because the forward delivery window was too short. Another cargo being shipped now – 167,854 tonnes of 61.1% Sinter Feed High Silica Guaiba – is expected to reach China on 23 May, and will also miss the forward delivery window.

It's hard to be too bullish, at least in the short term

We view the recent price data, the narrowing 'grades spread', the fact that China is sourcing lower-grade material from India and the advent of potentially distressed cargoes as good evidence of a weakening market. We have been encouraged by the spot iron ore market over the past couple of months holding above cash-cost support around USD120-130/t, suggesting that early indications of very poor steel output in China were wrong. But with the summer lull about to begin, things are unlikely to improve over the next couple of months and this cost support level may be freshly tested.

Results

ThyssenKrupp (TKAG.DE, N(V)) reported Q2 FY12 on 15 May, with underlying numbers beating expectations. Adjusted EBIT (which is normally the number focussed on by the market) was EUR134m (+61% qoq, -69% yoy), clearly beating Reuters consensus adj EBIT estimate of EUR99m. Marine systems was notably strong whereas Steel Americas did cut losses by only EUR60m instead of the previously guided EUR100m. Most other divisions came in as expected. The major problem was on the EPS level with a reported EPS of -EUR0.59 from continuing operations (down from +EUR0.51 a year ago) and -EUR1.14 all in (including -EUR0.55 fair value adjustments on divestments with the major portion coming from the lower Outokumpu share price) versus a consensus of -EPS0.10. TKA reported tiny operating cash flow from continuing operations of EUR150m leading to a negative FCF of EUR268m and an increase of net financial debt to EUR6.48bn (excluding pension liabilities of EUR7.4bn) and yielding a gearing of 73% and 156% including pensions. Management guided for only a mid three digit million adjusted EBIT for FY-12. At H1, Thyssen has generated EUR217m so the guidance might be prudent but bearing in mind that a normal quarter should add EUR300-400m, the message seems to be for a few more difficult quarters ahead, despite the solid order intake of EUR11.6bn (+15% qoq, +2% yoy)

Evraz (EVR LN, N(V)) reported weak Q1 FY12 results on 15 May, implying downside risk to consensus expectations. As Evraz reports its financial statements on a semi-annual basis, its quarterly financial reports are limited to the disclosure of just several headline numbers. Evraz's Q1FY12 revenue was reported to be in line with Q1FY11 revenue (which was USD3.9bn), while the Q1FY12 financial performance reported to be "broadly in line with the Q4FY11 performance". We interpret this as EBITDA margin in Q1FY12 being at the level of Q4FY11, or 13%, which implies Q1FY12 EBITDA of USD507m (vs USD497m in Q4FY11). Based on the reported timing of production cuts and the size of production capacity, we have calculated implied potential reduction in crude steel production volumes at up to 10% q-o-q. The planned repair works in Q2FY12 could lead to a loss of approximately 200kt of crude steel production at BF5 at Evraz NTMK mill and BF3 at ZSMK mill (c6% of Evraz's crude steel production of 3.2mt in Russia in Q1FY12). On top of that, cuts will also include a temporary shutdown of 860ktpa EAF, which could lead to a total loss of approximately 400kt of crude steel in Q2FY12 (approximately 9% of Evraz's crude steel production of 4.3mt in Q1FY12). The temporary shut downs will also affect ZSMK rail mill, which will be shut starting from April for 5 months for an upgrade of capacity from 720ktpa to 950ktpa (incl. 450ktpa of high speed 100m rails) and a related shut down of a continuous caster, which is scheduled for expansion from 725ktpa to 1mtpa.

JSW Steel (JSTL IN, N(V)) reported 4QFY12 results on 14 May: JSTL reported standalone EBITDA of INR16.5bn (+32% q-o-q/ 2% y-o-y), 5% ahead of Bloomberg consensus and in line with HSBCe of INR16.6bn. NPAT at INR6.1bn was 5% below consensus due to higher than expected interest expenses. Results were good on a consolidated basis, with EBITDA of INR18.9bn (consensus INR15.9bn) following better than expected earnings at the US operations which reported EBITDA + other income of USD42.6m as plate/pipe utilizations rose to 44%/16%. This however includes an insurance claim settled during the quarter, the quantum of which was not disclosed by management, but which was hinted as a significant part of reported EBITDA. Outlook: In the event that the Category A mines take time to start or Category B mines (both in Karnataka) do net get approved, utilization levels for JSTL could fall drastically post July 2012. For now, visibility is only until July with c 5mt (HSBCe) of iron ore available for JSTL until July, which equates to a max of 3.2mt of steel production.

CSN (CSNA3.BZ, UW) reported disappointing Q1 2012 results: CSN reported revenue of BRL3.9bn (-7% q-o-q) below consensus estimate of BRL4.1bn and HSBC estimate of BRL4.3bn due to low iron ore volumes and lower steel prices. Steel volumes of 1.3mt (79% sold domestically) were 3% higher than our estimates but offset by lower-than-expected net revenue per ton (BRL1,806/t, -4% q-o-q) due to worse-than-expected product mix and more volumes exported. Iron ore volumes of 6.7mt (100% basis) were less than our 7.1mt forecasts, but can predominantly be explained by the poor weather in Q1 FY12. EBITDA of BRL1.1bn (-24% q-o-q) was below consensus estimate of BRL1.4bn and HSBC estimate of BRL1.4bn. The shortfall was predominantly in the iron ore division, with reported EBITDA BRL590m (49% margin) well short of our BRL856m estimate due to lower volumes and higher-than-expected costs, which could also be attributed to the poor weather. EPS of BRL0.08 was well below consensus estimate of BRL0.36 and HSBC estimate of BRL0.32. Worse-than-expected financial results loss of BRL628m versus our expectation of a loss of BRL537m, predominantly due to an increased debt level, combined with lower-than-expected EBITDA contributed to a poor net income.

Macro News

Asia

China: More stimulus needed - PBoC cut RRR by 50bp: Barely a day after the release of April's disappointing data, the PBoC announced its second 50bp RRR cut this year, effective 18 May. This was a well expected and much-needed move, signalling that Beijing is ramping up easing efforts to control downside risks to growth. Additional easing measures will be critical for stabilizing China's growth. Thankfully, the downtrend in inflation allows Beijing to do so. HSBC economists expect more aggressive delivery of policy stimulus via quantitative easing, substantial tax breaks, fiscal spending and investment deregulation in the coming months to ensure a soft landing.

EMEA

Eurozone Q1 2012 GDP - recession avoided but few signs of re-balancing: The eurozone economy narrowly avoided recession, with GDP flat in Q1 2012, following a 0.3% q-o-q contraction in Q4 2011. This was better than consensus expectations of a 0.2% q-o-q contraction. The country breakdown showed that Germany continues to power on while other countries, especially in the periphery, moved further into recession. Spain fell back into recession (-0.3% q-o-q) while other economies witnessed another quarter of negative growth such as Italy (-0.8% q-o-q), Portugal (-0.1% q-o-q) and the Netherlands (-0.2% q-o-q). Available data also shows limited signs of re-balancing within the eurozone, with Germany still very dependent on export growth for its strong Q1 performance.

Germany: ZEW expectations hurt by political worries - ZEW expectations took a leg down in May but stayed in positive territory. The ongoing political uncertainties in the eurozone seem to have left their mark. Meanwhile, the ZEW current conditions managed to rise. Overall, the ZEW survey signals that the economy is likely to keep on growing but maintaining the growth dynamics of Q1 (+0.5% q-o-q) over the course of the whole year is unlikely.

Germany: Strong start to 2012 - German GDP surprised heavily to the upside in Q1 2012, rising by 0.5% q-o-q compared to consensus expectation of a small increase of 0.1%. This expansion has not only meant that a recession has been avoided but also that a solid basis has been laid for overall growth in 2012. Overall, indicators in Germany point to a continuation of growth over the coming quarters, but it is unlikely that pace will stay as strong as in Q1. In particular, headwinds from the eurozone seem to have intensified according to the latest PMI figures.

Americas

US retail Sales, Empire Manufacturing, CPI: Recent US data releases were mixed, but overall they corroborate our economists' impression that GDP is moving gradually along a 1.5% to 2.0% growth path. April retail sales rose 0.1% m-o-m versus consensus of +0.1% rise, partly reflecting lower sales at gasoline stations and building material stores. Sales excluding autos, gasoline, and building materials rose 0.4% m-o- m. The May Empire manufacturing index rose to 17.1 versus consensus of 9.0 from 6.6 in April. Finally, the April headline CPI was unchanged in m-o-m terms, taking the y-o-y rate down to 2.3% from 2.7%. The core CPI rose 0.2% m-o-m, keeping the y-o-y rate at 2.3%.

US Industrial Production: Utilities output recovers after warm winter - Industrial output climbed 1.1% m-o-m in April, nearly double the consensus estimate of +0.6%. The increase was led by strong gains in utilities and autos output. The rise in utilities has limited implications, as it simply reflects a normalization in activity after unusually warm weather this past winter. The rise in auto production is a welcome sign, but further improvement may be slower if auto sales trend sideways for the rest of this year, which we think is likely. Manufacturing production excluding vehicles rose 0.3% m-o-m in April. This indicates moderate ongoing growth but does not suggest any acceleration.

Industry-Specific News

Asia

Chinese steel prices decline further amid bearish sentiment: Chinese domestic steel prices declined further by RMB100/t w-o-w, a fourth consecutive monthly decline, to RMB 4130-4170/t amid bearish sentiment. We note that Chinese steel inventories had been running high and now with signs of poor demand, the inventory situation is not expected to improve meaningfully. But production rates continued at a high rate putting further pressure on inventories and prices – so we think China domestic steel prices do not have an upside in the short term.

BIS norms to come in force from September 2012: The Economic Times reported that the implementation of the Bureau of Indian Standards (BIS) in the long products category is likely to commence in September 2012. These standards specify quality requirements specifically in the chemistry of steel being produced and could, by means of higher costs, lead to the closure of some of the smaller induction furnace based producers which cumulatively account for c30% of Indian steel capacity. The move could also lend some push to long product prices which although significantly higher y-o-y due to raw material issues, have seen a sharp downtrend (2% in less than a month vs. flattish flat product prices) due to weak demand conditions and the seasonal dip as India heads into the monsoon seasons.

EMEA

European steel prices expectations remain bearish and prices fall: North European domestic HRC prices continued to grind down, falling EUR3/t w-o-w to EUR525-535/t while sentiment deteriorated further leaving bearishness at its highest since October 2011. We note that the premium versus China export prices continues to contract (now below USD30/t), partly due to the depreciation of the EUR against the USD. We continue to see a weak demand environment in Europe, which has been confirmed by European steel companies in their outlook for Q2. However, we also think that inventory is much better controlled in the system than it was a year ago. Steel prices are close to marginal costs, we also do not expect to see much downside unless raw material prices fall sharply.

ThyssenKrupp (TKAG.DE, N(V)):Management to investigate strategic options in all directions for both the US and the Brazil plants – Management indicated during a post-result conference call that it might use a partnership with or a sale to a buyer whose strategy can better utilize the quality and the specific market capability and competitiveness of these plants. The move had been mentioned in the press and we think it is actually a negative sign as management seems to have lost confidence in being able to make Steel Americas work. The assets are on the books at EUR6.5bn and we would doubt that all of that would be realizable in a sale. For Thyssen, equity is EUR8.9bn and a EUR2bn impairment would be felt, given the a group has a gearing of 152%. On the positive side, selling these assets would enable the group to free itself of the significant portion of the EUR6.3bn financial debt (another EUR7.2bn are pensions), cut the losses for FY-13 (we expect Steel Americas to have a negative EBIT of cEUR400m) and narrow the conglomerate discount that is currently above 30%.

ThyssenKrupp (TKA.GR, N(V)) Stainless: Proposed Outokumpu merger to be taken up by EU commission on 21 May – The European Commission's anti-competitive authority will review the merger on 21 May. It may extend that by 10 to 35 working days from filing, to consider either a company's proposed remedies or an EU member state request to handle the case. Most mergers usually win approval but occasionally the Commission opens a detailed second-stage investigation for up to 90 additional working days, which it may extend to 105 working days. ThyssenKrupp already stated that it might be by the end of the calendar year before they would have all approvals.

Voestalpine (VOE AV, OW(V)) has raised USD514m in loans: Voestalpine has raised USD514m (EUR400m) in Schuldschein loans, promissory notes issued privately under German law, in fixed and variable interest tranches due in three, five and seven years. European steelmakers have been using the liquidity window provided by the ECB to European banks to raise relatively cheap funding.

Mechel (MTL US, OW(V), USD6.4, TP USD15.8) unveiled new strategy. Mechel's new strategy puts financial deleverage and asset disposal at the forefront, aside from completing ongoing projects such as Elga and Universal rolling mill. Management is allowing two-three months to complete the strategic review of assets post which a decision regarding divesting unprofitable assets would be made. Management is also considering the possible consolidation of Estar (a zero operating margin business with USD1bn of debt, bearing zero interest) despite challenging market conditions. Complete details of the new strategy can be accesses in our recent note *Mechel Oao (MTL US), OW(V): New strategy – asset review and deleverage*, dated 11 May 2012.

Raspadskaya (RASP RM, OW(V), USD2.4, TP USD6.10) board recommended not paying H2FY11 dividends. Raspadskaya said in a regulatory filing that its board has recommended not paying any dividend for the second half of 2011, as reported by Bloomberg on 15 May.

Americas

North American steel prices continue to slide amid bearish price expectations – The North American domestic steel prices continued its weekly decline and decreased by USD14/t w-o-w to USD720-730/t while price expectations remained ultra bearish for the week. We note that the premium over China export prices continued to contract, now standing at USD75/t. This is already well below the import trigger threshold level of USD100/t which should ease import pressure on prices for the coming months. Demand expectations, which had been in optimistic zone, started to deteriorate w-o-w suggesting that underlying demand environment remains uncertain. We think import pressure on steel prices has already gone but high domestic production rate along with contracted imports (arriving now) could be putting pressure now.

North American rig count remains stable: According to data from Baker Hughes, North American rig count remained largely stable. The US rig count increased by 9 w-o-w to 1,974. Rigs employed in oil production increased by 17 w-o-w, while rigs geared for natural gas production declined by 8 w-o-w. Canada's rig count declined by 11 w-o-w to 120.

US crude steel capacity utilisation again above the 80% mark: According to the American Iron and Steel Institute, for the week ending 12 May, US crude steel production increased 2.1% w-o-w to 2.0m s.t. The utilisation rate at 81.1% increased from 79.4% the week prior, rising above the 80% mark again.

US flat steel lead times inched up: For the week ending 13 May, US HRC lead times increased to 3.8 weeks (from 3.3 the week prior) while CRC lead times increased to 6.5 weeks from 6.0 the week prior. However, HDG lead times decreased slightly from the week prior.

US imports licenses increased in April: According to the US Department of Commerce, licenses for import for April were 2.93mt, up from imports of 2.78mt of steel products in March. This increase was primarily led by Korea, Russia, China, India and the United Kingdom. However, licenses to import from Japan and Mexico decreased. Imports continue to remain high but should come down in coming months as prices have decreased and US HRC price premium over China is close to USD100/t.

Raw materials

Iron ore prices decline sharply: 62% Fe iron ore prices (China CFR) declined sharply by USD5 w-o-w to USD136/t reflecting steel demand sentiments in China, the biggest consumer of sea borne iron ore. Prime coking coal prices remained stable for the week at USD208/t.

Next week's events

Events Calendar

Date	Company	Event
24 May 2012	Severstal	Q1 Results (IFRS) - 2012

Source: HSBC, Thomson Reuters Datastream

Recent research

'Dislocation barometer' for South African resource stocks - Gold Fields, AngloGold Ashanti and Harmony oversold; Royal Bafokeng, Assore and Amplats overbought, 16 May 2012

JSW Steel Ltd (JSTL IN) N(V): Good 4Q results but problems far from over, 14 May 2012

Gerdau (GGBR4) First Cut: 1Q12 – Weak results due partly to weather issues, 02 May 2012

Jindal Steel & Power Ltd (JSP) : OW: 4Q results good; projects delayed, 30 April 2012

Sesa Goa Ltd (SESA IN) - N(V): 4Q - Good results, but outlook timid, 26 April 2012

VALE First Cut: 1Q12 – Weak as expected, but looking forward, 26 April 2012

A Commodity Cycle Health Check - Is the Super Cycle reaching middle age?, 25 April 2012

Metals Quarterly - Q2 2012, 25 April 2012

Usiminas (USIM5) First Cut: 1Q12 – Tough start to the year, 24 April 2012

Metals & Mining – Notes from the Road - Feedback from our Brazil marketing trip, 23 April 2012

Latam Metals & Mining - 1Q 2012 results preview, 20 April 2012

VALE - N(V): 1Q12 production report – Brighter days ahead, 18 April 2012

Latin America Metals & Mining - Brazil steel: Grin and bear it, 13 April 2012

Erdemir (EREGL) N – ArcelorMittal's stake sale is a major negative catalyst, 02 April 2012

Novolipetsk Steel (NLMK) N (V) – Margin leadership is lost, at least in the current cycle, 02 April 2012

CSN First Cut: Q4 2011 – In line operating results, 27 March 2012

Jindal Steel & Power Ltd (JSP) Upgrade to OW: CAG versus CAGR, 27 March 2012

Russian Steel and Pipes 4Q11 preview: negative surprises to damp the sentiment, 23 March 2012

VALE Vale tax saga – third party case may set precedent, 20 March 2012

Voestalpine (VOE AV) – OW (V): On track , 15 March 2012

Turkish Steel and Gold – Prefer Koza and Kardemir, 09 March 2012

Usiminas (USIM5.SA) – First Cut: 4Q2011– Still all about costs, 07 March 2012

'Dislocation barometer' for EM metals and mining stocks – Shifting the focus from Oversold to

Overbought names, 7 March 2012

VALE N(V): Vale securing BRL1.6bn in assets to continue tax dispute, 6 March 2012

Salzgitter (SZG GR) – Downgrade to N on missing valuation upside and catalysts

Jindal Steel & Power Ltd (JSP) – Downgrade to N: Love the company, but stock expensive, 23 February 2012

Russian steel: Already too late or still too early? – Turning away from steel to pipes and coal, 21 February 2012

Ezz Steel Rebars (ESRS EY) – OW (V): Value hidden by legal issues, 22 February 2012

China steel sector – Structural changes needed, but unlikely to happen in 2012, 16 Feb 2012

VALE – First Cut: 4Q11 – Weak iron ore prices drive the quarter, 15 Feb 2012

ThyssenKrupp N(V):Where is the catalyst?, 15 February 2012

Russian Steel – Read-across to Russian stocks from the seasonality in the European steel sector,

23 January 2012

Bell-shaped and range bound – Why upside is capped for European steel, 18 January 2012

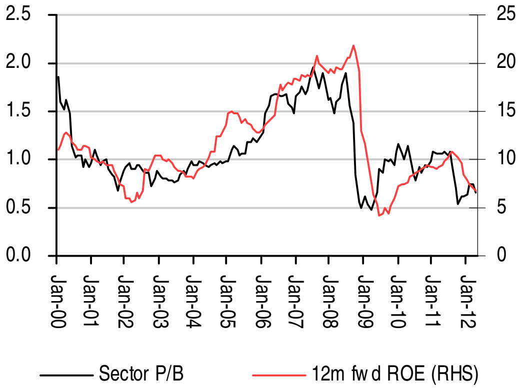
Global Steel Valuation

Company	BBG Code	Ccy	Closing Price	Target Price	HSBC Rating	Market cap USD m	PE (x) 2012	PE (x) 2013	PBV (x) 2012	PBV (x) 2013	EV/EBITDA (x) 2012	EV/EBITDA (x) 2013	Div Yield (%) 2011	Div Yield (%) 2012	ROE (%) 2011	ROE (%) 2012
North America																
Nucor	NUE US	USD	35.1	NR	NR	11,119	14.9	9.5	1.4	1.3	6.6	4.8	3.7%	3.8%	11%	13%
US Steel	X US	USD	22.8	NR	NR	3,278	9.0	6.1	0.9	0.8	4.8	3.7	0.8%	0.8%	2%	10%
AK Steel	AKS US	USD	6.5	NR	NR	718	17.5	6.1	1.8	1.4	4.8	3.8	2.7%	2.7%	3%	15%
Average							**13.8**	**8.6**	**1.3**	**1.2**	**6.1**	**4.5**	**3.0%**	**3.1%**	**8%**	**12%**
Latin America																
CSN*	CSNA3 BZ	BRL	13.6	17.5	UW	9,894	8.4	6.6	2.1	1.7	4.2	3.8	4.9%	3.7%	39%	23%
Gerdau*	GGBR4 BZ	BRL	15.9	19.0	N	12,903	11.7	8.7	1.0	0.9	6.4	5.1	2.5%	2.4%	8%	7%
Usiminas*	USIM5 BZ	BRL	10.1	12.5	UW	6,175	24.6	14.3	0.6	0.6	9.7	8.4	1.1%	1.5%	2%	2%
Ternium ADRs	TX US	USD	19.0	NR	NR	3,803	5.7	5.6	0.6	0.6	3.1	2.9	4.7%	4.1%	10%	11%
Average							**12.5**	**8.8**	**1.2**	**1.1**	**6.0**	**5.1**	**3.2%**	**2.8%**	**17%**	**12%**
Europe																
Arcelor Mittal*	MT US	USD	14.6	21.4	N(V)	22,743	7.2	5.3	0.4	0.4	4.0	3.5	4.5%	4.5%	5%	5%
Thyssen Krupp*	TKA GR	EUR	15.6	24.7	N(V)	10,212	16.9	6.6	0.9	0.8	6.4	4.5	3.3%	4.6%	11%	13%
Voestalpine AG*	VOE AV	EUR	21.0	31.2	OW(V)	4,529	6.8	5.5	0.9	0.8	5.1	4.2	5.8%	6.8%	14%	14%
Salzgitter *	SZG GR	EUR	35.7	48.0	N	2,735	10.0	7.1	0.5	0.4	3.4	2.8	2.8%	3.1%	4%	6%
SSAB	SSABA SS	SEK	59.4	NR	NR	2,600	9.7	7.3	0.6	0.6	6.3	5.1	4.3%	5.1%	6%	7%
Rautaruukki	RTRKS FH	EUR	6.0	NR	NR	1,065	20.6	7.9	0.7	0.6	6.8	4.7	6.7%	6.7%	2%	4%
Average							**10.1**	**5.9**	**0.6**	**0.5**	**4.8**	**3.9**	**4.3%**	**4.7%**	**7%**	**8%**
EEMEA																
NLMK*	NLMK LI	USD	16.6	22.0	N(V)	9,943	6.1	4.4	0.9	0.7	5.7	4.0	3.9%	4.6%	17%	18%
Severstal*	SVST LI	USD	11.7	16.0	N(V)	11,770	5.7	6.2	1.4	1.1	3.8	3.7	4.9%	5.1%	30%	24%
Evraz*	EVR LN	GBP	3.3	4.4	N(V)	6,990	8.4	6.9	1.1	1.0	4.6	3.9	6.8%	2.3%	11%	15%
MMK*	MMK LI	USD	4.3	5.5	UW(V)	3,731	7.3	5.1	0.4	0.3	4.0	3.4	1.5%	1.6%	3%	6%
Erdemir *	EREGL TI	TRY	2.3	2.8	N	3,855	8.2	6.0	0.9	0.8	6.5	4.7	8.9%	9.7%	15%	12%
Arcelor Mittal SA	ACL SJ	ZAR	54.1	58.0	UW	2,903	16.4	8.6	0.9	0.9	6.9	4.2	0.9%	1.8%	2%	6%
TMK*	TMKS LI	USD	11.3	18.0	OW(V)	2,471	5.7	4.2	1.3	1.1	4.7	4.0	6.4%	8.1%	32%	31%
EZZ Steel *	ESRS EY	EGP	7.0	10.0	OW(V)	632	10.0	6.4	0.8	0.8	5.2	4.0	10.5%	15.8%	8%	32%
Evraz Highveld Steel	HVL SJ	ZAR	26.0	34.0	UW(V)	310	11.4	6.0	1.0	0.9	3.3	2.0	0.0%	3.1%	0%	9%
Kardemir *	KRDMD TI	TRY	1.0	1.4	OW	539	4.8	4.5	0.7	0.6	4.0	3.0	0.0%	0.0%	17%	14%
Average							**7.4**	**5.8**	**1.0**	**0.9**	**4.9**	**3.9**	**4.7%**	**4.5%**	**18%**	**17%**
Korea																
Posco *	005490 KS	KRW	372,500	470,000	OW	24,205	8.0	7.8	0.8	0.7	2.3	2.2	2.6%	2.6%	11%	11%
Hyundai Steel	004020 KS	KRW	87,900	NR	NR	6,434	7.9	7.1	0.7	0.7	7.8	6.8	0.5%	0.5%	12%	13%
Dongkuk Steel	001230 KS	KRW	16,600	NR	NR	881	11.9	8.3	0.4	0.4	8.5	7.5	3.3%	3.3%	8%	9%
Average							**8.1**	**7.7**	**0.8**	**0.7**	**3.6**	**3.3**	**2.2%**	**2.2%**	**11%**	**11%**
Japan																
Nippon Steel	5401 JP	JPY	179	NR	NR	15,163	13.3	9.1	0.6	0.6	6.0	4.9	1.6%	2.0%	5%	6%
JFE Holdings	5411 JP	JPY	1297	NR	NR	9,918	nm	7.6	0.5	0.5	7.0	5.6	2.0%	2.4%	2%	5%
Sumitomo Metal	5405 JP	JPY	130	NR	NR	7,775	nm	8.2	0.8	0.7	7.7	6.6	2.5%	3.3%	2%	8%
Kobe Steel	5406 JP	JPY	97	NR	NR	3,760	24.6	11.6	0.5	0.5	5.3	4.9	2.1%	2.4%	6%	5%
Average							**nm**	**8.8**	**0.6**	**0.6**	**6.5**	**5.5**	**2.0%**	**2.5%**	**3%**	**6%**
China & Taiwan																
Baosteel *	600019 CH	CNY	4.8	6.3	OW(V)	13,267	12.3	11.0	0.8	0.7	6.2	5.8	8.4%	9.1%	14%	14%
Angang H *	347 HK	HKD	4.4	6.8	N(V)	4,722	40.8	16.5	0.5	0.5	7.7	6.5	6.8%	7.0%	8%	8%
Wuhan	600005 CH	CNY	2.8	NR	NR	4,486	13.4	11.7	0.8	0.8	5.2	4.2	6.0%	8.0%	6%	8%
Maanshan H *	323 HK	HKD	1.8	3.1	N(V)	2,665	20.4	7.0	0.4	0.4	5.1	4.0	5.1%	5.6%	8%	8%
China Steel	2002 TW	TWD	28.0	NR	NR	14,274	24.6	18.2	1.5	1.4	16.4	13.5	8.9%	9.4%	15%	15%
Average							**18.7**	**11.7**	**0.7**	**0.7**	**6.2**	**5.4**	**7.8%**	**8.6%**	**12%**	**12%**
India																
JSPL*	JSP IN	INR	451	590	OW	7,747	10.0	7.5	1.9	1.5	8.7	6.6	0.3%	0.3%	26%	20%
Tata Steel*	TATA IN	INR	401	500	OW	7,153	6.3	5.3	0.8	0.7	5.2	4.5	2.0%	2.0%	16%	16%
JSW Steel*	JSTL IN	INR	619	650	N(V)	2,539	8.1	6.0	0.7	0.6	4.8	4.5	1.8%	1.8%	9%	12%
Average (ex JSP)							**6.8**	**5.5**	**0.8**	**0.7**	**5.1**	**4.5**	**1.9%**	**1.9%**	**14%**	**15%**
Australia																
OneSteel	OST AU	AUD	1.0	NR	NR	1,305	6.0	3.8	0.3	0.3	5.4	3.8	11.6%	14.2%	5%	6%
Bluescope Steel	BSL AU	AUD	0.3	NR	NR	1,116	5.7	6.6	0.3	0.3	6.7	2.7	3.4%	4.6%	-11%	2%
Average							**5.9**	**5.1**	**0.3**	**0.3**	**6.0**	**3.3**	**7.3%**	**9.1%**	**-3%**	**4%**
Global average							**11.9**	**8.3**	**0.9**	**0.8**	**6.1**	**5.0**	**3.9%**	**4.1%**	**11%**	**12%**

Source: Thomson Reuters DataStream, HSBC estimates, * covered by HSBC , OW = Overweight, UW= Underweight, N = Neutral, V = Volatile, NR = Not Rated

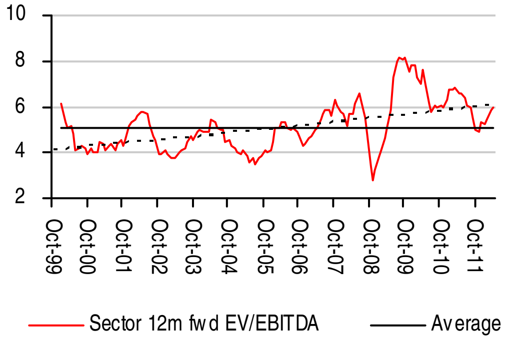
Regional sector valuation multiples

European steel sector P/B vs. forward ROE



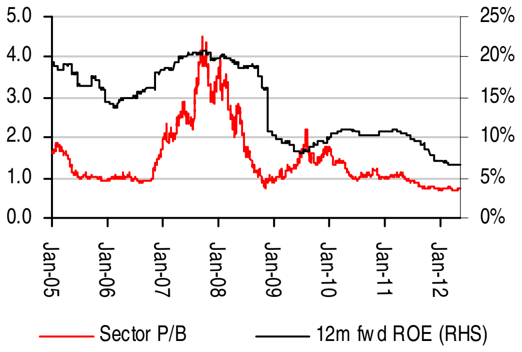
Source: Thomson Reuters DataStream, HSBC

European steel fwd EV/EBITDA



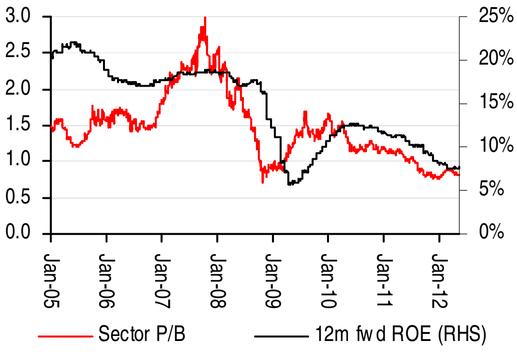
Source: Thomson Reuters DataStream, HSBC

China steel sector P/B vs. forward ROE



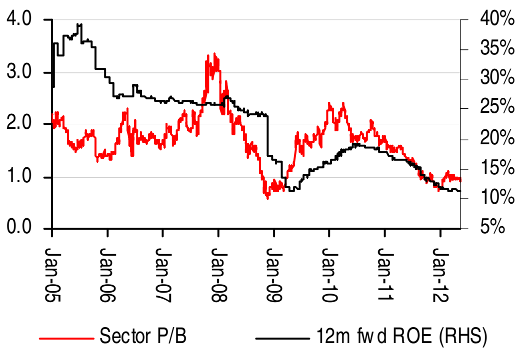
Source: Thomson Reuters DataStream, HSBC

Asia steel sector P/B vs. forward ROE



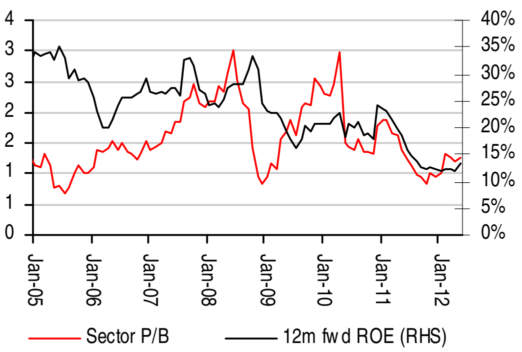
Source: Thomson Reuters DataStream, HSBC

India steel sector P/B vs. forward ROE



Source: Thomson Reuters DataStream, HSBC

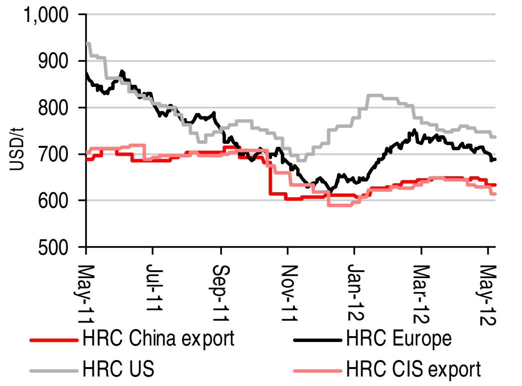
LatAm steel sector P/B vs. forward ROE



Source: Thomson Reuters DataStream, HSBC

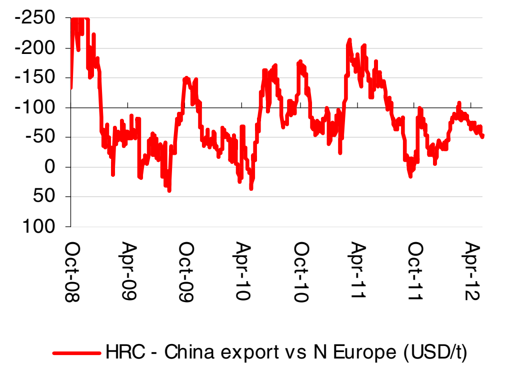
Global steel price development

Regional HRC prices (USD/t)



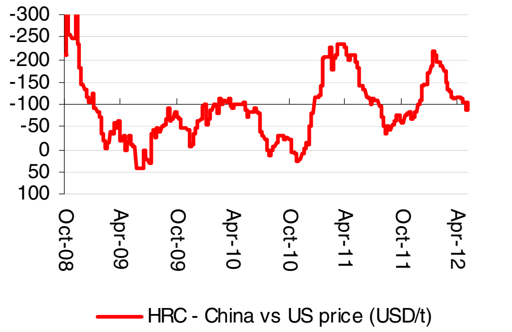
Source: Steel Benchmarker, SBB, Metal Bulletin

HRC Delta- China vs N. Europe (USD/t)



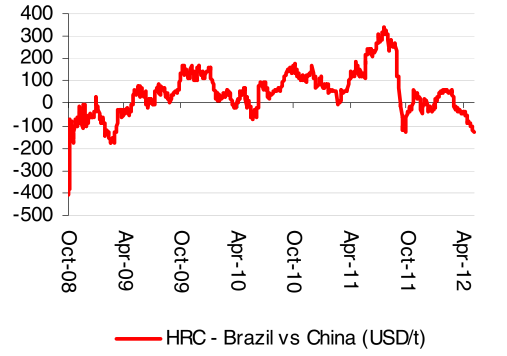
Source: SBB, Metal Bulletin, Steel Benchmarker

HRC Delta- China vs. USA (USD/t)



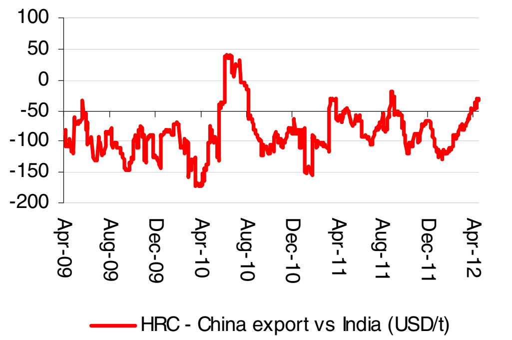
Source: SBB, Metal Bulletin, Steel Benchmarker

HRC Delta- Brazil versus US (USD/t)



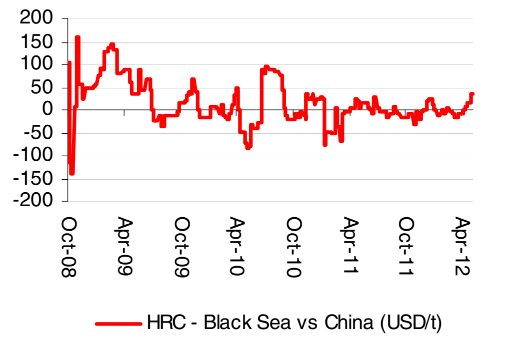
Source: SBB, Metal Bulletin

HRC Delta- China export versus India (USD/t)



Source: SBB, Metal Bulletin

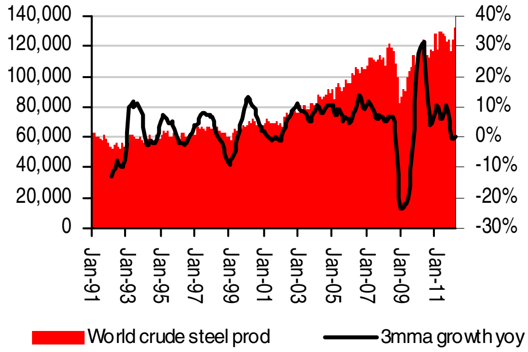
HRC Delta- Black Sea export vs. China export (USD/t)



Source: SBB, Metal Bulletin

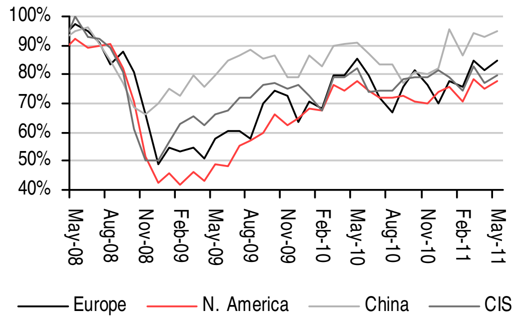
Steel production

Global monthly steel production (mt)



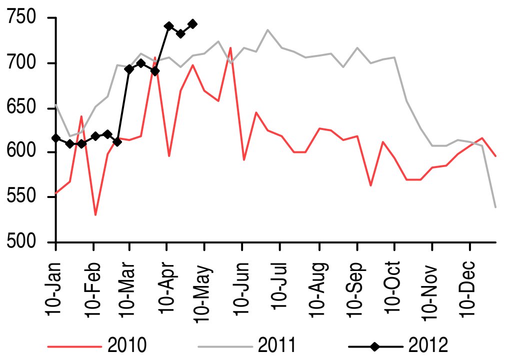
Source: Worldsteel

Regional monthly capacity utilisation



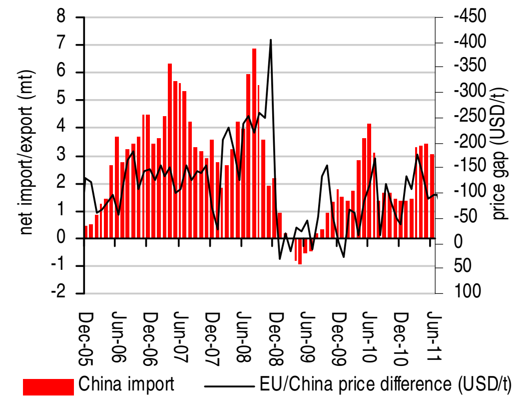
Source: Worldsteel, HSBC estimates

China crude steel production seasonality (annualised)



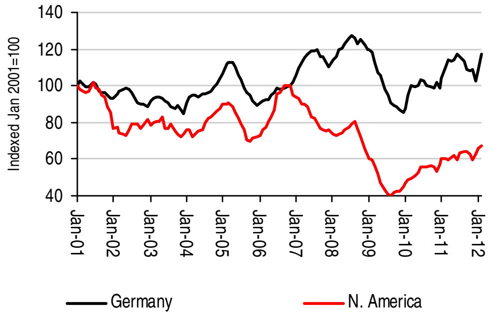
Source: CISA, HSBC

China net steel export (mt) vs price delta to Europe (USD/t)



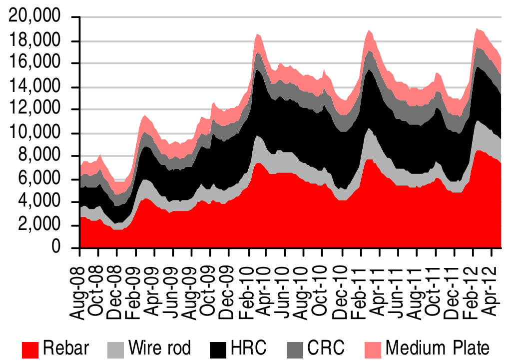
Source: CEIC, CRU

Germany and US steel inventory index



Source: CRU

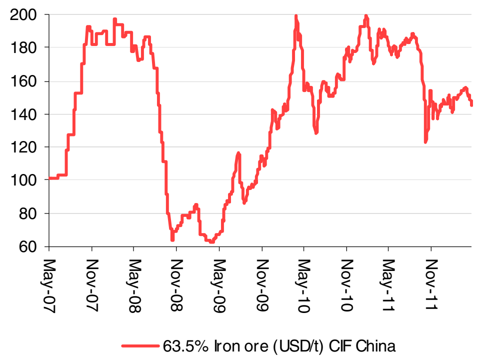
China steel inventory (mt)



Source: MySteel

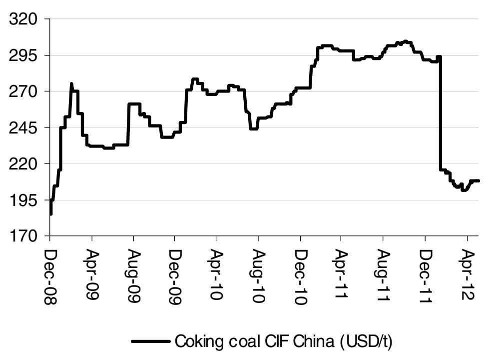
Steel production cost indicator

Spot iron ore CIF China (USD/t)



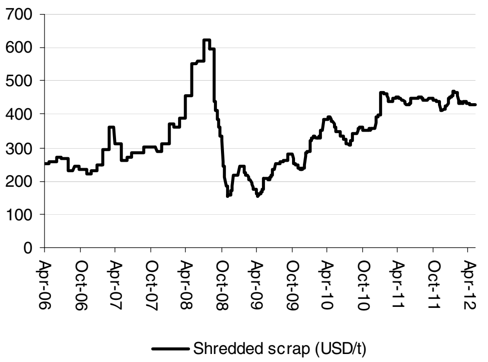
Source: Steel Business Briefing, Metal Bulletin

Spot coking coal CIF China (USD/t)



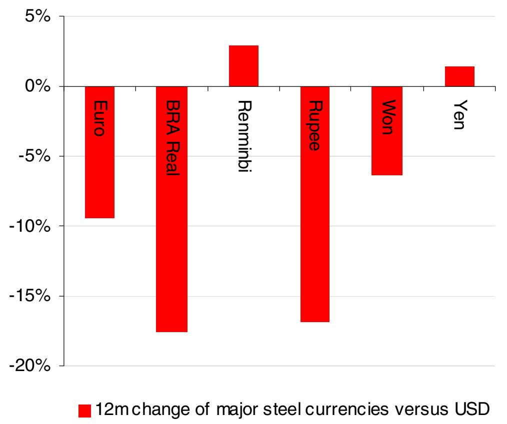
Source: Steel Home

Shredded scrap (USD/t)



Source: Steel Benchmarker

FX movements



Source: Thomson Financial Datastream

Global steel prices

	5/16/2012	5/9/2012	4/25/2012	w-o-w (%change)	m-o-m (%change)
HRC China (USD/t)	650	650	645	0.0	0.8
HRC CIS (USD/t)	595	648	648	-8.1	-8.5
HRC Europe (USD/t)	674	687	709	-1.8	-5.8
HRC US (USD/t)	725	739	714	-1.8	-4.6
Stainless base price (EUR/t)	1140	1165	1165	-2.2	-3.0
Stainless surcharge (EUR/t)	1392	1451	1451	-4.0	-4.1

Source: Metal Bulletin, Thomson Reuters Datastream

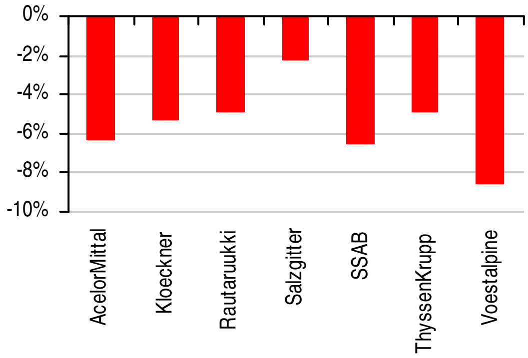
Raw material prices

	5/16/2012	5/9/2012	4/25/2012	w-o-w (%change)	m-o-m (%change)
Iron ore spot (CIF) (USD/t)	144	148	150	-2.7	-4.7
Shredded scrap (USD/t)	422	421	421	0.2	-0.2
Nickel (USD/t)	16942	17136	17521	-1.1	-2.8
Ferrochrome (USD/lb)	1.19	1.19	1.190.0	0.0	0.0

Source: Metal Bulletin, Thomson Reuters Datastream

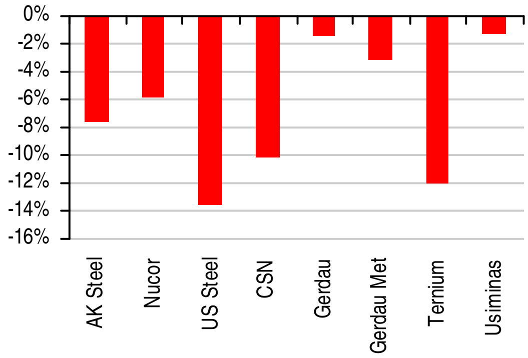
Weekly stock price return

Europe steel equities



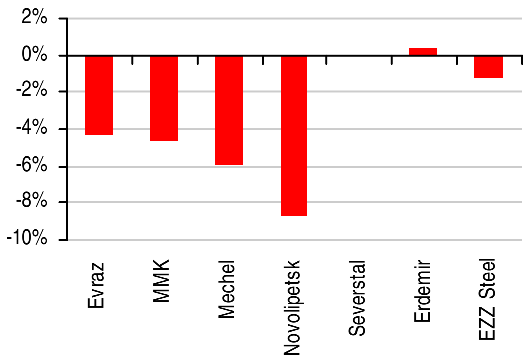
Source: Thomson Reuters Datastream

Americas steel equities



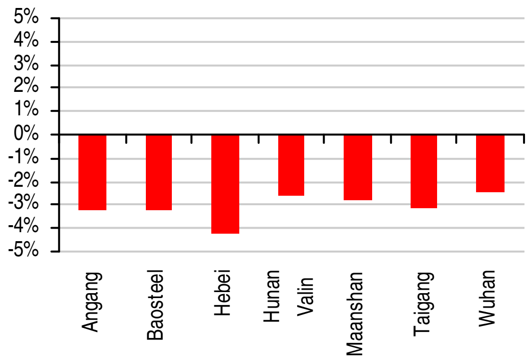
Source: Thomson Reuters Datastream

CEEMEA steel equities



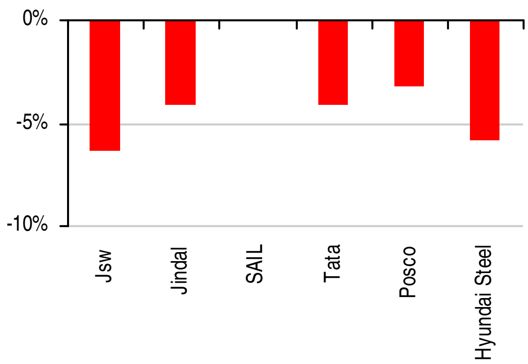
Source: Thomson Reuters Datastream

China steel equities



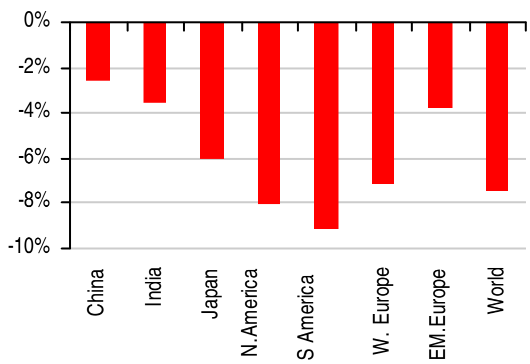
Source: Thomson Reuters Datastream

India / S. Korea steel equities



Source: Thomson Reuters Datastream

MSCI Steel Indices (in USD)



Source: Thomson Reuters Datastream

Disclosure appendix

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For each stock we set a required rate of return calculated from the cost of equity for that stock’s domestic or, as appropriate, regional market established by our strategy team. The price target for a stock represents the value the analyst expects the stock to reach over our performance horizon. The performance horizon is 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, must exceed the required return by at least 5 percentage points over the next 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock must be expected to underperform its required return by at least 5 percentage points over the next 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands are classified as Neutral.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation of coverage, change of volatility status or change in price target). Notwithstanding this, and although ratings are subject to ongoing management review, expected returns will be permitted to move outside the bands as a result of normal share price fluctuations without necessarily triggering a rating change.

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Neutral (Hold)	38%	(25% of these provided with Investment Banking Services)
Underweight (Sell)	14%	(16% of these provided with Investment Banking Services)

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2 All market data included in this report are dated as at close 18 May 2012, unless otherwise indicated in the report.
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