INDOPREMIER

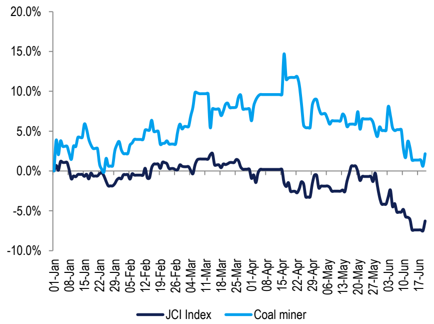
Metals & Coal

OVERWEIGHT *(unchanged)*

Sector Update | 20 June 2024

Sector Index Performance

	3M	6M	12M
Absolute	-6.4%	0.0%	3.6%
Relative to JCI	0.7%	5.6%	1.9%



Summary Valuation Metrics

P/E (x)	2024F	2025F	2026F
ADRO IJ	4.3	5.7	7.5
ITMG IJ	4.9	6.7	13.7
PTBA IJ	8.0	9.5	9.7
UNTR IJ	4.5	4.5	4.3
HRUM IJ	7.6	7.7	5.9
ADMR IJ	8.6	8.4	6.6

EV/EBITDA (x)	2024F	2025F	2026F
ADRO IJ	1.5	2.0	2.0
ITMG IJ	2.2	2.8	5.3
PTBA IJ	4.6	5.1	4.9
UNTR IJ	2.1	1.9	1.6
HRUM IJ	4.7	5.7	3.8
ADMR IJ	7.3	8.1	7.3

Div. Yield	2024F	2025F	2026F
ADRO IJ	11.4%	9.2%	7.0%
ITMG IJ	18.4%	13.2%	9.7%
PTBA IJ	14.7%	4.4%	3.7%
UNTR IJ	9.6%	9.4%	9.6%
HRUM IJ	N/A	N/A	N/A
ADMR IJ	N/A	N/A	N/A

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La Nina is a boon for 2H24F outlook; prefer thermal over met coal

- La Nina could bring a tailwind to both thermal & metallurgical-coal prices in 2H24F, affecting seaborne supply in Australia.
- ST S-D balance could tilt into surplus on rising China's coal production post safety-inspection and soft real-estate market.
- However, we think demand (for thermal) could pick-up following winter re-stocking in 2H24F. Thus, we prefer thermal over met-coal.

Thermal coal: ST demand risk, supply-disruption to support price

We see seaborne demand for thermal coal to be skewed to the downside in ST, considering that domestic coal production in China (5M24: -3% yoy) is set to recover after safety inspections are concluded in May24, in addition to high inventory in India (17 days, above 3-yr avg of 11 days) with summer demand already behind – China & India accounts for c.50% seaborne demand. However, we expect a supply disruption on the back of potential La Nina in Aug-Nov24 (70% chance) and winter restocking season in 2H24F. Additionally, although the strength of the upcoming La Nina remains uncertain, we observed that even moderate La Nina is often accompanied by flooding in Queensland and New South Wales, where all coal miners are located in Australia, an upside risk to price in our view.

Metallurgical coal: flat demand, supply-disruption to lift price

We think supply-disruption shall be the only factor that could lift coking-coal price, as from demand side, the positive infrastructure development in India – reflected in c.14% yoy finished steel consumption in 4M24 was offset by China's weak real-estate market (-3% yoy) as China consumes c.50% of global crude steel as opposed to India's c.10%. Similar to thermal coal, we also expect the current La Nina cycle, which could affect supply in Australia (c.50% of seaborne supply) to be a positive tailwind to coking-coal prices in 4Q24F, similar to 2010-2011 and 2021 & 2022.

Prefer thermal over met-coal on more inelastic demand

We prefer thermal coal over metallurgical coal owing to its more inelastic demand and raised our Newcastle's thermal coal price assumption to US$130/t (from US$120/t) ahead of Winter's restocking season in 2H24F. However, in the short-term, we see potential downside risks for both thermal & met-coal as China mining safety inspection in Shaanxi (c.30% China's domestic production) is concluded, which could negatively affect seaborne demand. On the other hand, met-coal, unlike thermal, is still facing soft demand in China's real-estate market, offsetting the positive infrastructure development from India. Thus, we maintain our coking-coal price assumptions at US$260/t in FY24F (vs. YTD price of US$291/t).

ADRO as our top pick in energy/coal space, followed by ADMR

In-line with our preference on thermal over coking-coal, we like ADRO (Buy) as our top pick, as we think the company is set to benefit from higher Newcastle coal price during winter re-stocking season in 2H24F in addition to potential consensus earnings upgrade as 1Q24 result was a beat (1Q24 is still c.35% of consensus estimates even after +7% EPS upgrade since result release). Our pecking order (from most to least preferred) are: ADRO > ADMR > UNTR > HRUM > ITMG > PTBA, while putting ADMR second due to its bottom-up volume growth story despite relatively limited upside in ASP outside from supply-disruption.

La Nina to disrupt supply from Indonesia and Australia
Latest forecast from World Meteorological Organization (WMO) indicated a 50% chance of current El Nino cycle to transition into La Nina in Jun-Aug24, with the chance of occurrence increasing to 60% in Jul-Sep24 and 70% in Aug-Nov. La Nina typically results in increase in rainfall in Southeast Asia, where key coal miners such as Indonesia, China, and India are located. Thus, in the event of La Nina, we can expect coal production in respective countries to slow down.

The strength of a La Nina cycle is usually assessed using the Oceanic Nino Index (ONI), which measures the deviation of sea surface temperature from its long-term average. Looking at La Nina cycles in the past 10 years (Fig. 1), we observed that moderate cycles, indicated by ONI reading of -1 or above, are often accompanied by flooding in Australia, particularly in Queensland and New South Wales where c.100% of coal are produced in the country. Although the strength of the upcoming La Nina remains uncertain, we see this as a positive tailwind to both thermal and coking coal price.

Fig. 1: La Nina and natural disaster in Australia

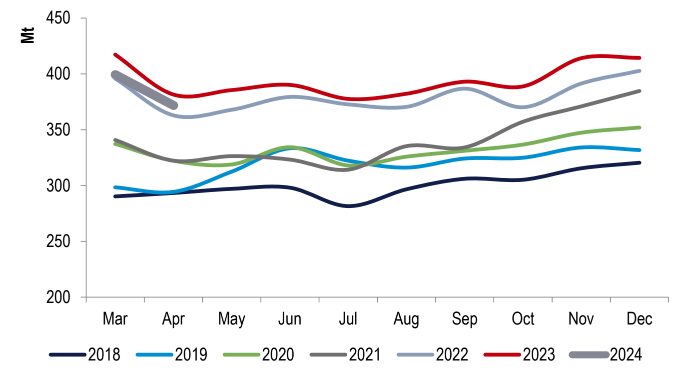
La Nina	Peak ONI	Indication	Natural disaster in Australia
2010-2011	-1.7	Strong	Flooding in Queensland
2011-2012	-1.1	Moderate	Flooding in Queensland
2016-2017	-0.9	Weak	
2017-2018	-1.0	Moderate	
2020-2021	-1.3	Moderate	Flooding in Queensland and New South Wales
2021-2022	-1.0	Moderate	Flooding in Queensland and New South Wales
2022-2023	-1.1	Moderate	

Source: Various sources, Indo Premier

Meanwhile in Indonesia, we observed that flooding is less likely to happen in key coal producing regions such as Kalimantan and Sumatra. However, data shows that precipitation is typically higher in those regions during La Nina and miners within our coverage are already expecting lower production in 2H24F which is already factored in into each company's production target.

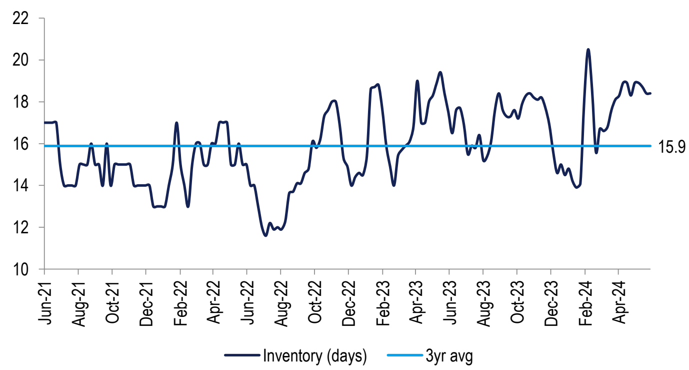
Thermal: ST downside risk lingers from China and India
China electricity consumption recorded +6% yoy growth in 4M24, driven by both electricity generated from coal (+5% yoy) and renewables (+13% yoy). The increase in electricity consumption is likely to be driven by a rebound in industrial activity (Apr24: +6.7% yoy).

Fig. 2: China coal production



Source: Bloomberg, Indo Premier

Fig. 3: China coal inventory



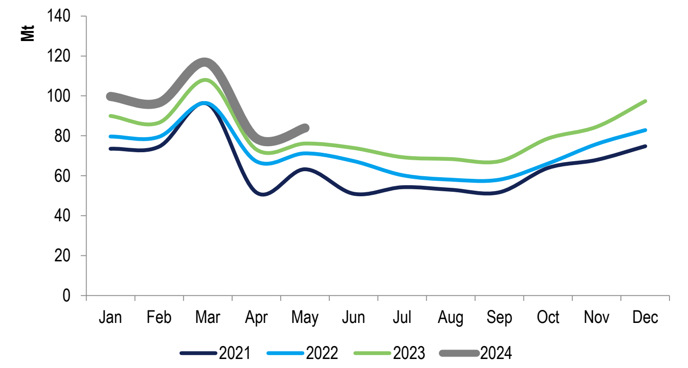
Source: Bloomberg, Indo Premier

Combined with lower domestic coal production (5M24: -3% yoy), attributed to safety inspections in mining sites located in Shaanxi (contributes c.30% to China's total production), China seaborne demand has remained robust in 5M24 (+13% yoy). However, safety inspections had been already conducted from Mar24 until May24, and as such, we expect domestic coal production to start ramping up starting in Jun24 onwards, indicating a downside risk to seaborne demand in the short-term.

To add, current inventory level of 18 days is also 16% above 3yr average (Fig. 3). But considering that there is 70% chance of La Nina occurring in Aug-Nov24, we expect coal inventory to remain above average in anticipation of higher rainfall, which could potentially disrupt production.

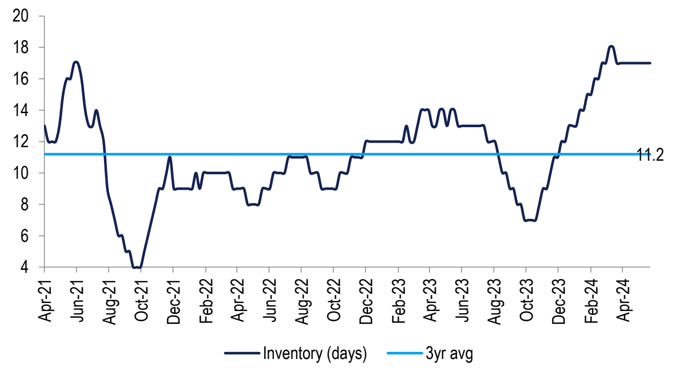
Meanwhile in India, electricity consumption spiked 10% yoy in 5M24 amid strong economic growth (1Q24: 7.8% yoy). The increase in electricity consumption was primarily driven by higher electricity generated from coal (+11% yoy) amid lower hydropower output (-10% yoy) attributed to severe drought from El Nino. However, higher domestic coal production (5M24: +10% yoy) coupled with robust coal imports (5M24: +12% yoy) have led to elevated stockpile level (Jun24: 17 days, above 3-yr avg of 11 days). Thus, we see ST downside risk to India seaborne coal demand, considering that summer demand period (Mar-May) is already behind us.

Fig. 4: India coal production



Source: Bloomberg, Indo Premier

Fig. 5: India coal inventory

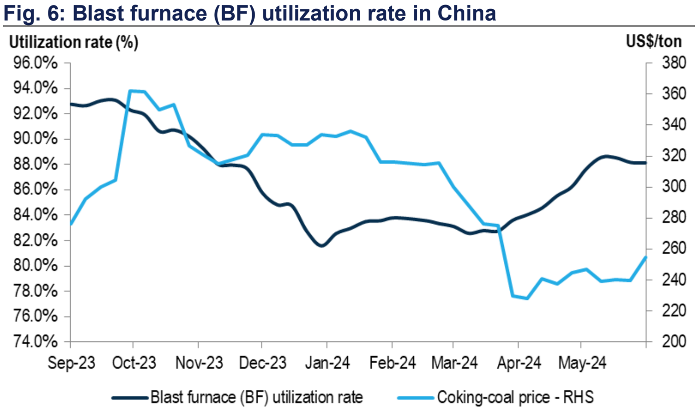


Source: Bloomberg, Indo Premier

Metallurgical coal: flat demand, supply-disruption to lift price

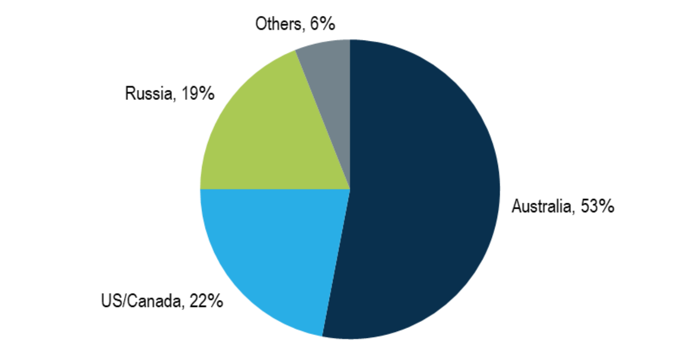
Australian hard coking coal (HCC) prices currently trades at US$250/t, as price fell from above US$300/t in Jan24 and Feb24, with low blast furnace (BF) utilization rate (Fig. 6) started to affect seaborne demand while weather-related supply-disruption in Australia's Queensland and New South Wales (NSW) – equivalent to c.50% seaborne supply – has been muted since Mar24 (see report).

Fig. 6: Blast furnace (BF) utilization rate in China



Source: Bloomberg, MySteel, Indo Premier

Fig. 7: Metallurgical coal seaborne supply origin

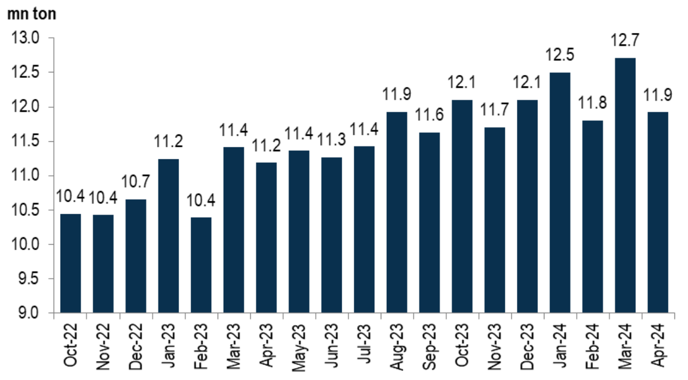


Source: Bloomberg, Indo Premier

The price decline was also mainly due to slower demand from India (Fig. 8), which may coincide with the uncertainty during Lok Sabha elections in Apr and May24.

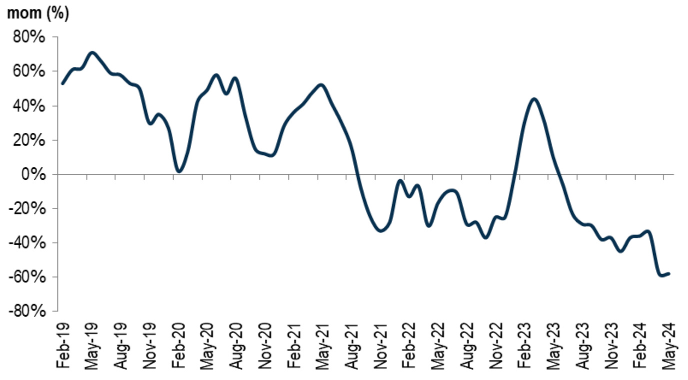
However, going forward, we think coking coal price is set to trade sideways in the short-term but could potentially trade higher by 4Q24F, as we believe that downside is already relatively limited owing to robust demand from India, while demand from China has remain soft (-3% yoy) despite came relatively better than expected, considering very limited signs of recovery in their real-estate market (Fig. 9) – which accounts for c.40% of crude-steel demand, a primary end-use of coking-coal products.

Fig. 8: India crude steel production



Source: World Steel Association, Ministry of Steel India, Indo Premier

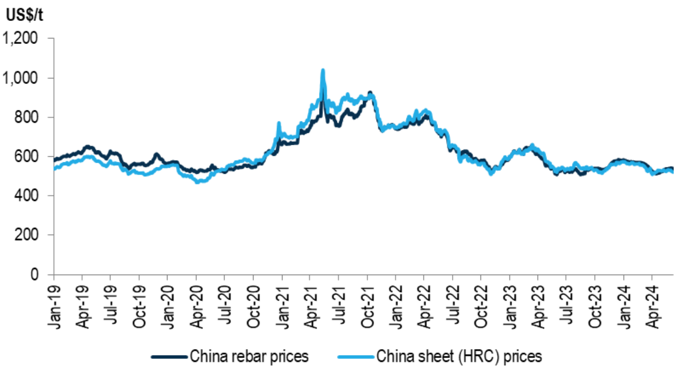
Fig. 9: 70-cities new home prices (mom %)



Source: Bloomberg, Indo Premier

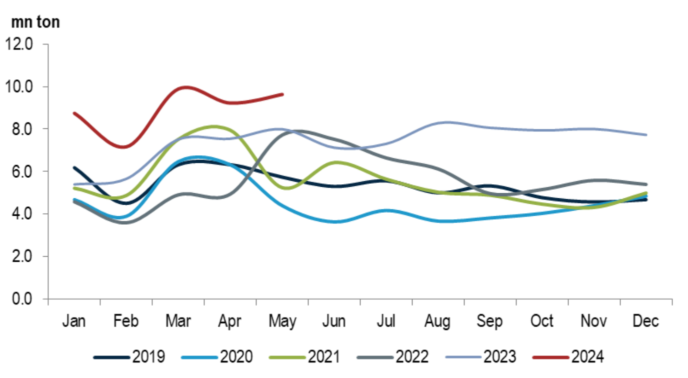
The ongoing softness in China's real-estate market is also apparent in the crude-steel prices in China with HRC steel and Rebar both declined by 8% and 9% YTD (Fig. 10) as pressure on domestic consumption persist despite production decline YTD (-3% yoy); at the same time, China's steel exports in 5M24 grew by c.30% yoy, which meant that majority of steel produced in China is not being consumed domestically but being exported to rest of the world (RoW), though in the context of coking-coal S-D balance, this may meant that as long as China can export their products while demand in the U.S, Europe, and other Asian countries (incl. India) remain robust, coking-coal demand would relatively be stable.

Fig. 10: China Rebar and HRC prices



Source: Bloomberg, Indo Premier

Fig. 11: China's monthly steel exports (in mn ton)

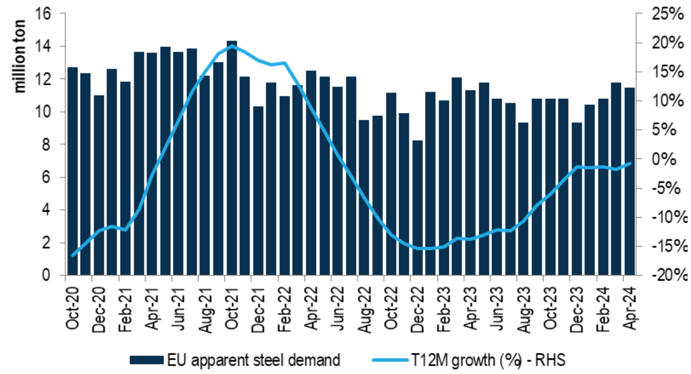


Source: Bloomberg, Indo Premier

Thus, we observed how demand would fare in RoW. In European Union (EU), steel demand (c.8% of global consumption) has been relatively weak with apparent steel demand in 4M24 declined by 2% yoy, which also has been reflected in the lacklustre European steel price YTD (-7% yoy).

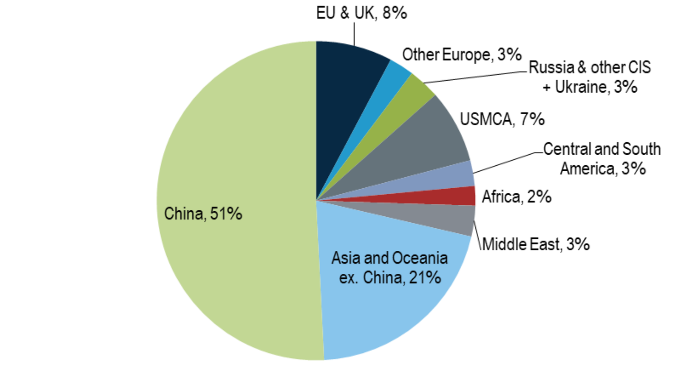
However, ECB 25bps interest-rate cut might give a demand relief, albeit not in a structural way. Outside China, India stood out the most with significant increase in steel consumption set to grow by +8% yoy in FY24F, according to World Steel Association; YTD, the growth in finished steel consumption (+14% yoy) exceed those of production in 4M24 (+13% yoy), and has been faring far better compared to World Steel Association forecast.

Fig. 12: European Union (EU) apparent steel demand



Source: Bloomberg, Indo Premier

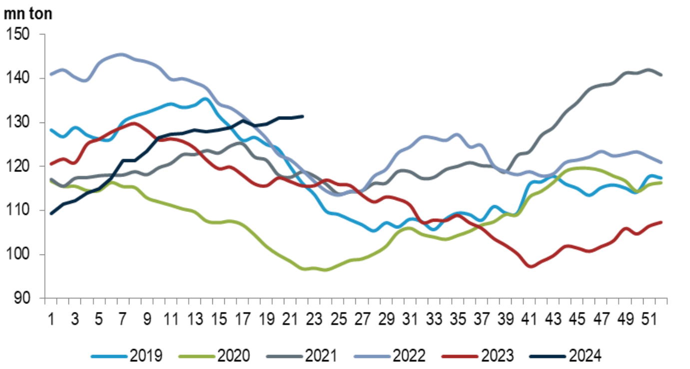
Fig. 13: World crude steel consumption breakdown



Source: Bloomberg, Indo Premier

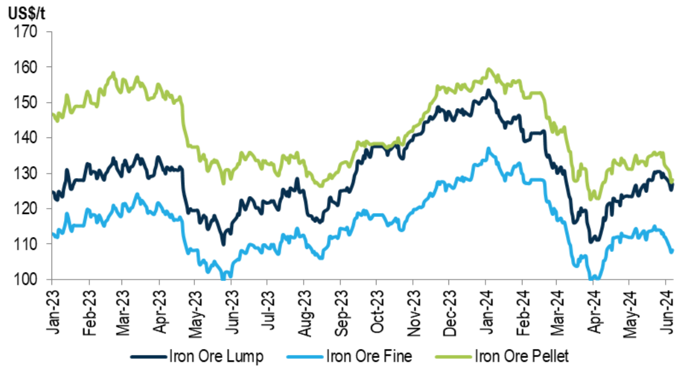
Another leading indicator that we observed to track demand is also the price of iron-ore – another raw material for steel – along with inventories, export-import data, and others. So far, Australian iron-ore fines, lumps, and pellets prices have been relatively soft following the domestic demand concern in China and RoW (Fig. 15) as China's iron ore inventory has continue to build-up overtime with the current position is already higher vs. last five-year average (Fig. 14).

Fig. 14: China's iron-ore inventory buildups



Source: Bloomberg, Indo Premier

Fig. 15: Iron ore prices

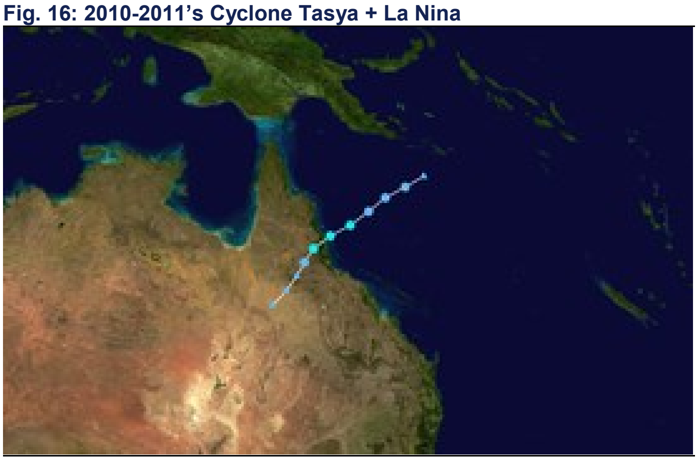


Source: Bloomberg, Indo Premier

With demand expected to be relatively flat given the current real estate market in China as well as government's steel production annual cap (1bn Mt), we believe coking-coal price could only trade higher on potential supply disruption. In this case, we think La Nina could also affect the production in Australia's Queensland and New South Wales (NSW) and thus we observed the historical price movement during previous La Nina that occurred in the past decades and found that:

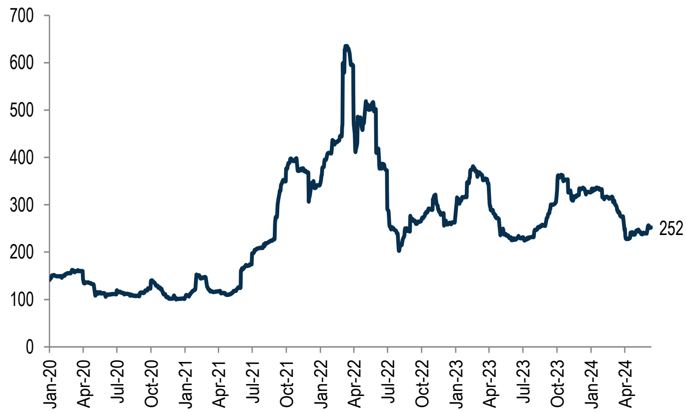
2010-2011's La Nina that coincides with the Cyclone Tasya, which enabled coking-coal prices to rally from US$200/t level to above US$300/t level. Current La Nina cycle starting 2020 has also bode well for coking-coal price as price often rallied starting 4Q to 1Q two years in a row (2022-2023 & 2023-2024) in addition to 2021-2022 (Fig. 17). Combined with China's coal import-ban from Australia, such supply-disruption has been able to lift coking-coal prices. While climate & weather could be unpredictable, we think could be a positive tailwind to coking-coal prices in 4Q24F, albeit only seasonally.

Fig. 16: 2010-2011's Cyclone Tasya + La Nina



Source: Bloomberg, Indo Premier

Fig. 17: Australia's hard coking coal (HCC) prices

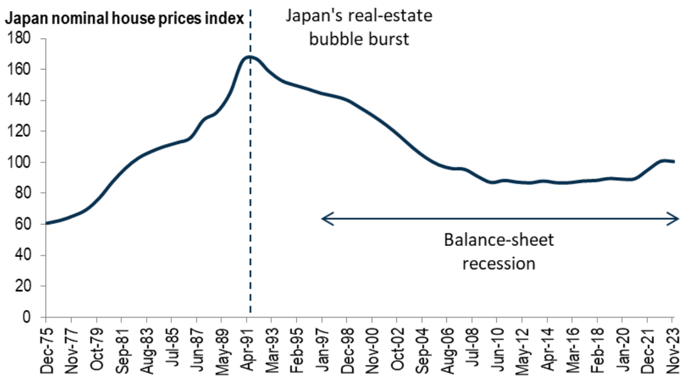


Source: Bloomberg, Indo Premier

India is the next commodity demand-driver, not China
As highlighted in our previous report on China, we think China property and real-estate market is currently facing a balance-sheet recession – similar to Japan's 1990, in which massive monetary stimulus may not be able to create a turnaround in the property-market. Urbanization rate have also slowed down while birth-rate is already on the decline. In addition, leading indicators (i.e. home prices in 70-cities, property floor space) has yet to reflect any turnaround in the property market despite continuous stimulus boost by People's Bank of China (PBOC).

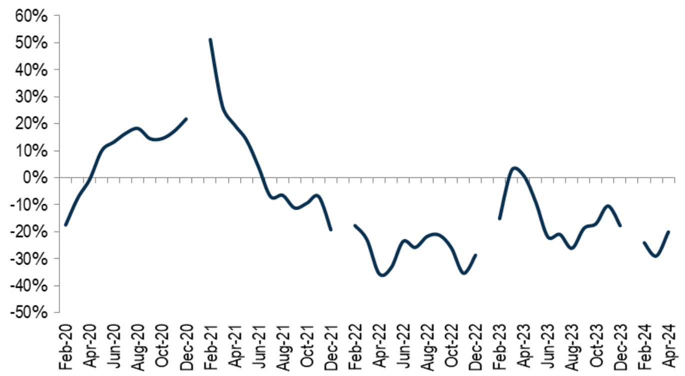
Instead, we think **India – and not China – is going to drive infrastructure spending in medium to long-term**, especially with the re-election of Narendra Modi amid the continuity over Modi's plan to boost infrastructure spending as well as manufacturing activity (+ve to crude steel & coking-coal, and thermal coal demand).

Fig. 18: We expect China to experience balance-sheet recession in property-market similar to Japan's 1990s, unless massive fiscal stimulus is given



Source: Bloomberg, Indo Premier

Fig. 19: Total funds-raised by property developers in China (yoy %)



Source: Bloomberg, Indo Premier

ADMR is the pick to play India theme owing to its coking-coal assets (India accounts for c.30% of coking-coal seaborne demand) combined with India's long-term plan to boost infrastructure spending coupled with continuously growing population. We think thermal coal demand could also improve as India's energy demand should go in parallel with its +7% GDP growth outlook, however to thermal seaborne demand, India's exposure is less in comparison to coking-coal, as India only accounts for c.15% of thermal coal seaborne demand vs. coking's c.30%.

Fig. 20: Peers comparison table

Ticker	Company	Rating	Target price (Rp/share)	P/E			EV/EBITDA			Dividend yield (%)		
				24F	25F	26F	24F	25F	26F	24F	25F	26F
ADRO IJ	Adaro Energy Indonesia	Buy	3,000	4.3	5.7	7.5	1.5	2.0	2.0	11.4%	9.2%	7.0%
ITMG IJ	Indo Tambangraya Megah	Hold	22,000	4.9	6.7	13.7	2.2	2.8	5.3	18.4%	13.2%	9.7%
PTBA IJ	Bukit Asam	Sell	2,000	8.0	9.5	9.7	4.6	5.1	4.9	14.7%	4.4%	3.7%
UNTR IJ	United Tractors	Buy	27,500	4.5	4.5	4.3	2.1	1.9	1.6	9.6%	9.4%	9.6%
HRUM IJ	Harum Energy	Hold	1,450	7.6	7.7	5.9	4.7	5.7	3.8	N/A	N/A	N/A
ADMR IJ	Adaro Minerals Indonesia	Buy	1,650	8.6	8.4	6.6	7.3	8.1	7.3	N/A	N/A	N/A

Source: Bloomberg, Indo Premier

SECTOR RATINGS

OVERWEIGHT	:	An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation
NEUTRAL	:	A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation
UNDERWEIGHT	:	An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation

COMPANY RATINGS

BUY	:	Expected total return of 10% or more within a 12-month period
HOLD	:	Expected total return between -10% and 10% within a 12-month period
SELL	:	Expected total return of -10% or worse within a 12-month period

ANALYSTS CERTIFICATION

The views expressed in this research report accurately reflect the analyst’s personal views about any and all of the subject securities or issuers; and no part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in the report.

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