

DAIDO STEEL CO., LTD. (5471 JP)

SOME POSITIVE FACTORS IN Q1 EARNINGS YET NO CHANGE IN 1H AND FY24 GUIDANCE FIGURES.

FY24 Q1 RESULTS

Daido Steel (5471 JP) produced FY24 Q1 (March year-end) results on 29 July 2024, with FY24 Q1 OP of ¥10,067mil (+15.2% YoY) on sales of ¥142,094mil (+0.1% YoY). Key points are:

Steel products sales volume declined -1.5% YoY (or -4,000 tonne YoY) to 262,000 tonne in Q1, due to a fall in sales volume of structural steel on the back of weak auto production.

Q1 OP was in line with the firm's expectation despite one-off loss related to closure of a magnet subsidiary in China (-¥2,016mil), thanks to 1) improved throughput of the open die forging business which led to improved production and shipment reflecting strong demand, and 2) higher volumes of stainless steel sales.

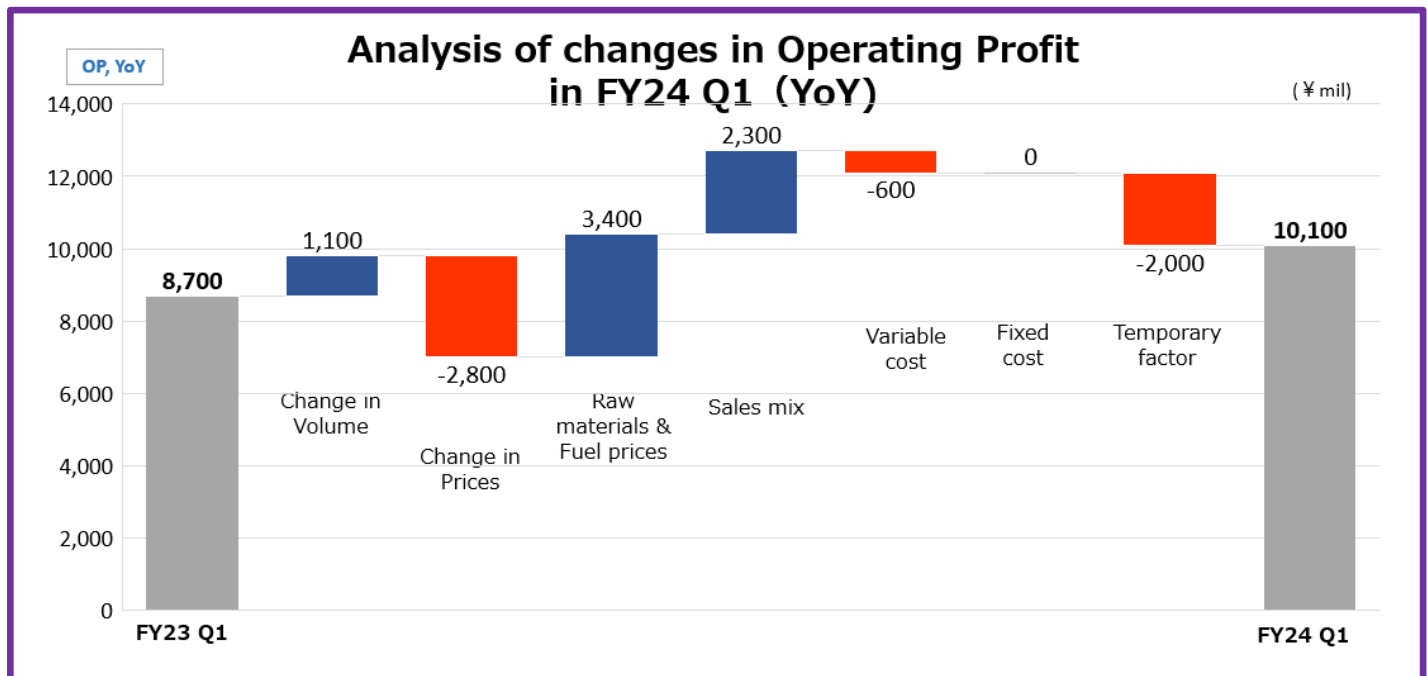
Daido Steel (5471 JP): Earnings Summary				
(¥mil)	FY23		FY24	
	Q1(IFRS)	FY(IFRS)	Q1(IFRS)	YoY (%)
Steel Products Sales Volume (tonne)	266,000	1,072,000	262,000	-1.5
Sales	141,886	578,564	142,094	0.1
COGS	119,605	480,618	115,949	-3.1
COGS / Sales (%)	84.3	83.1	81.6	-2.7ppt
GP	22,280	97,946	26,144	17.3
GPM (%)	15.7	16.9	18.4	+2.7ppt
SG&A	14,123	59,073	14,855	5.2
SG&A / Sales (%)	10.0	10.2	10.5	+0.5ppt
OP	8,739	42,250	10,067	15.2
OPM (%)	6.2	7.3	7.1	+0.9ppt
Pretax profit	9,948	45,068	11,425	14.8
Corporation Tax	-2,870	-12,493	-4,004	N/A
NP*	6,528	30,555	6,776	3.8

Source: Nippon-IBR based on Daido Steel's earnings results presentation materials
*NP attributed for the parent's shareholders

FY24 Q1 OP improved by +¥1,328mil (+15.2% YoY), with the largest impact from lower raw material and energy costs (+¥2,600mil), an increase in sales volumes (+¥1,100mil), as well as a +¥2,300mil positive impact from the improvement in throughput of open die forging. These positive factors (+¥3,400mil in total) were partially offset due to price changes (-¥2,800mil) that reflected (1) the fall in input prices, such as nickel and energy, and (2) one-off costs (-¥2,016mil) related to the closure of a Chinese subsidiary that handles magnets.

EXECUTIVE SUMMARY

- Daido Steel (5471 JP) saw a +15.2% YoY improvement in FY24 Q1 (March year-end) OP to ¥10,067mil on sales of ¥142,094mil (+0.1% YoY).
- Q1 OP was in line with the firm's guidance despite a one-off loss, thanks to 1) improved throughput of the open die forging business, and 2) an increase in sales volumes of stainless steel.
- Despite the better-than-expected Q1 performance, Daido Steel has not revised its 1H and FY24 forecasts. The firm guides for FY24 1H OP of ¥22,000mil on sales of ¥290,000mil and FY24 OP of ¥48,000mil (+13.6% YoY) on sales of ¥600,000mil (+3.7% YoY).
- Segment guidance figures also remain unchanged although there were some better-than-expected factors in Q1, such as 1) the OP improvement in the Specialty Steel segment, 2) the recovery in stainless steel HDD-related demand amid a recovery in data centre CAPEX, and 3) continued improvement in open die forging throughput.
- The FY24 dividend policy remains the same, with a benchmark pay-out ratio of more than 30%. During the ongoing medium-term management plan (ending FY26), the firm may boost shareholder returns depending on cash allocation status.
- Daido Steel became a constituent of the JPX400 Inclusion index which is constructed by the Nikkei and Japan Alternative Data Accelerator Association [JPX], thanks to its efforts to improve asset efficiency by proactively unwinding strategically held shares.



FY24 Q1 EARNINGS BY SEGMENT

The key factors regarding the performance of Daido Steel's three major segments are discussed below:

1. Specialty Steel Segment

[FY24 Q1 Sales ¥53,427mil (-3.2% YoY) / OP ¥3,319mil (+25.3% YoY) / OPM 6.2% (+1.4ppt YoY)]

Positive contributions to segment OP include (1) lower raw materials and energy costs (+¥2,600mil), (2) a positive surcharge (+¥400mil YoY) and (3) price revision in tool steel. Fixed cost coverage was also improved on the back of increased production for stockpiling, thus mitigating the impact of higher energy cost during the summer.

These factors offset the negative impact to earnings from (1) a -1.5% YoY dip in steel products sales volumes due to production declines by Japanese OEM makers in China, which lowered segment OP by -¥1,000mil and (2) the impact from price adjustments to reflect fall in energy costs (-¥1,000mil).

2. High Performance Materials & Magnetic Materials Segment

[FY24 Q1 sales ¥49,694mil (-2.9% YoY) / OP ¥2,962mil (-16.8% YoY) / OPM 6.0% (-1.0ppt YoY)]

Without the one-off cost associated with closure of a subsidiary in China (-¥2,016mil), segment OP would have come in at around ¥5,000mil (approx. +40.0% YoY / +¥1,500mil YoY). The largest positive factor was the increase in sales volumes (+¥1,800mil) on the back of solid demand for HDDs used at data centres.

In the past, HDD-related sales comprised as much as 10% of Stainless Steel sales. In FY23, the ratio fell to just 4%. While Daido had assumed that HDD-related sales would gradually begin to recover in FY24, the Q1 demand was ahead of plan.

Declining raw materials and energy costs (+¥1,000mil) and positive factors including change in sales mix (+¥700mil) also contributed to segment OP growth. However, price reductions reflecting lower input costs led to a negative impact of -¥1,700mil.

3. Parts for Automobiles / Industrial Equipment Segment

[FY24 Q1 sales ¥27,196mil (+12.8% YoY) / OP ¥2,800mil (+220.4% YoY) / OPM 10.3% (+6.7 ppt YoY)]

The substantial surge in OP was due to an improvement in production throughput in open die forging (+¥2,500mil), supported by strong demand remained from the aircraft, heavy electric and oil and gas industry. Demand for engine valves in US was also solid due to limited new supply by US makers.

By March 2025, the firm plans to have completely withdrawn from the less profitable turbine housing products business included in its precision casting products.

Daido Steel (5471JP): Sales, OP and OPM by Segment (Cumulative)					
(¥mil)		FY23		FY24	
		Q1	FY	Q1	YoY(%)
Specialty Steel	Sales	55,221	218,743	53,427	-3.2
	OP	2,648	13,724	3,319	25.3
	OPM (%)	4.8	6.3	6.2	+1.4ppt
High Performance Materials & Magnetic Materials	Sales	51,169	202,384	49,694	-2.9
	OP	3,561	10,275	2,962	-16.8
	OPM (%)	7.0	5.1	6.0	-1.0ppt
Parts for Automobile and Industrial Equipment	Sales	24,115	104,996	27,196	12.8
	OP	874	5,719	2,800	220.4
	OPM (%)	3.6	5.4	10.3	+6.7ppt
Engineering	Sales	5,021	23,091	4,616	-8.1
	OP	474	2,136	240	-49.4
	OPM (%)	9.4	9.3	5.2	-4.2ppt
Trading & Service	Sales	6,358	29,347	7,159	12.6
	OP	1,176	10,369	754	-35.9
	OPM (%)	18.5	35.3	10.5	-8.0ppt
Total	Sales	141,886	578,564	142,094	0.1
	OP	8,739	42,250	10,067	15.2
	OPM (%)	6.2	7.3	7.1	+0.9ppt

Source: Nippon-IBR based on FY24 Q1 Earnings Results Materials published by Daido Steel
Total numbers are after adjusted for inter-segment trades.

FY24 OUTLOOK

Daido Steel maintained its FY24 1H and full-year company estimates despite the solid Q1 performance. The firm has started using IFRS as its accounting standard from FY24, and guides for FY24 1H OP of $\text{¥}22,000\text{mil}$ on sales of $\text{¥}290,000\text{mil}$ and FY24 OP of $\text{¥}48,000\text{mil}$ (+13.6% YoY) on sales of $\text{¥}600,000\text{mil}$ (+3.7% YoY). On a Japanese GAAP basis, the FY24 guidance would call for OP of $\text{¥}50,000\text{mil}$ (+18.7% YoY) on sales of $\text{¥}600,000\text{mil}$ (+3.2% YoY). Compared to Japanese GAAP, IFRS OP will be approx. $\text{¥}2,000\text{mil}$ lower – the gap due to differences in accounting for retirement benefits ($\text{¥}1,700\text{mil}$) and itemisation ($\text{¥}300\text{mil}$).

Daido Steel maintains an annual payout ratio of more than 30% as a benchmark for its shareholder return policy. In FY24, the firm plans to pay an annual dividend of $\text{¥}47/\text{share}$ (a 1:5 stock split was implemented on 1 January 2024), or a pay-out ratio of 30.4%.

Key assumptions by management for the FY24 outlook include:

- 1 Auto production levels will reflect real demand after adjustments runs their course amid normalised components supply – including semiconductors.
- 2 Demand from the industrial machinery sector will likely gradually recover towards the latter half of FY24.
- 3 Demand from the semiconductor sector might suddenly see a pickup in momentum.
- 4 The current ongoing global geopolitical issues might continue to cause sudden inflationary pressure and further supply chain disruptions.

Daido Steel (5471 JP): Earnings Results and Guidance Summary						
(¥mil)	FY22		FY23		FY24 (IFRS)	
	1H	FY	1H	FY	1H CE	FY CE
Steel Products Sales Volume (tonne)	540,000	1,085,000	529,000	1,072,000	526,000	1,080,000
Sales	281,857	578,564	288,594	581,287	290,000	600,000
COGS	230,921	476,224	240,953	479,772	N/A	N/A
COGS / Sales (%)	81.9	82.3	83.5	82.5	N/A	N/A
GP	50,935	102,340	47,640	101,515	N/A	N/A
GPM (%)	18.1	17.7	16.5	17.5	N/A	N/A
SG&A	27,710	55,353	28,637	59,401	N/A	N/A
SG&A / Sales (%)	9.8	9.6	9.9	10.2	N/A	N/A
OP	23,225	46,986	19,003	42,113	22,000	48,000
OPM (%)	8.2	8.1	6.6	7.2	7.6	8.0
RP / Pre-tax profit (IFRS)	24,092	48,122	21,083	45,031	23,000	50,000
Extraordinary Profit / Loss	-407	1,241	-2,680	28,529	N/A	N/A
Corporation Tax	-4,225	-10,867	-5,941	-21,238	N/A	N/A
NP*	18,294	36,438	11,465	49,759	15,000	33,000

Source: Nippon-IBR based on Daido Steel's earnings results presentation materials
* NP attributed to the parent's shareholders

Raw Materials Price Trend							
			FY20	FY21	FY22	FY23	FY24
			Result	Result	Result	Result	Assumption
Scrap	H2	¥000/t	24.9	47.6	46.3	43.7	47.5
	Factory Bundle		28.9	53.9	50.7	47.9	52.0
Nickle	LME	\$/Lb	6.8	9.3	11.6	8.7	7.5
Crude Oil	Dubai Brent	\$/bbl	45.8	76.6	90.3	81.3	85.0
FOREX	TTM	¥/\$	107.1	113.4	135.5	144.6	150.0

Source: Daido Steel FY20~FY23 Earnings Results Tanshin

FY24 FORECASTS BY SEGMENT

The FY24 earnings outlook for Daido Steel's three major segments are as follows:

1. Specialty Steel

[FY24 sales ¥225,000mil, OP ¥12,500mil, OPM 5.6%]

Daido Steel guides for FY24 1H Specialty Steel segment OP of ¥5,500mil on sales of ¥110,000mil, and FY24 OP of ¥12,500mil on sales of ¥225,000mil (IFRS basis). On a Japanese GAAP basis, guidance for OP would come in at ¥13,500mil (-8.8% YoY) on sales of ¥225,000mil (+2.7% YoY).

The YoY decline in the segment OP is primarily due to management's assumption that steel product sales volumes to the auto sector will likely decline YoY, and that fixed costs will rise. Although Q1 OP reached 60% of the 1H forecast, Daido Steel has maintained its 1H forecast because the Q1 performance includes stockpiling before the summer to avoid seasonally higher energy prices.

FY24 steel products sales volumes are expected to be almost flat at 1,080,000 tonnes (+0.7% YoY), with 1H guidance for 526,000 tonnes (-0.5% YoY / -3.1 % HoH). The firm assumes global auto production by Japanese OEM makers in CY24 to be 26.2mil units (13.1mil units semi-annually – with domestic production of 4.2mil units and overseas production of 8.9mil units) and global auto demand of 91.7mil units. Moreover, the industrial machinery sector is also expected to recover from 2H.

Daido Steel's conservative view on 1H steel production is due to the seasonally lower numbers of operating days. However, the firm has ample production capacity to meet any unexpected surge in demand. In the event of this happening, management anticipates upside to earnings.

2. High Performance Materials & Magnetic Materials

[FY24 sales ¥210,000mil, OP ¥20,500mil, OPM 9.8%]

Here, the firm is guiding for FY24 1H segment OP of ¥9,500mil on sales of ¥100,000mil, and full-year FY24 OP of ¥20,500mil on sales of ¥210,000mil. Due to one-off cost spent to close a Chinese subsidiary, segment Q1 OP achieved only 31.2% of 1H guidance.

Although Daido Steel has not revised segment 1H and FY24 forecasts, the following factors suggest upside potential to its earnings:

1. Without such a one-off cost, Q1 segment OP would have landed in line with expectation.
2. HDD-related demand is stronger than expected due to likely recovery in data centre CAPEX.
3. Although stainless steel demand for SPEs has not yet shown signs of fully-fledged recovery, there are signs that orders are gradually recovering, with once former customers reactivating orders during Q1 and inventory in the SPE value chain returning to optimal levels. This supports management's view that demand may start recovering from 2H. Daido Steel aims to be proactive in its production management so as to capture any sudden jump in demand from the SPE sector.
4. Nickel prices rebounded to \$8.3/lb+ during Q2 vs Daido Steel's assumption of \$7.5/lb but it is currently at \$7.2/lb level. If the Nickel price falls below \$7.5/lb for a prolonged period of time, the risk is that the firm will need to write down revaluation loss. However, with inventory reduced, it is unlikely that customers hold back on buying stainless steel as in FY23.
5. The gradual recovery of orders from the industrial machinery sector with FY23 Q4 marking the bottom.

3. Parts for Automobile and Industrial Equipment Segment

[FY24 sales ¥115,000mil, ¥11,000mil, OPM 9.6%]

Daido Steel is guiding for FY24 1H segment OP of ¥5,000mil on sales of ¥55,000mil and full-year FY24 OP of ¥11,000mil on sales of ¥115,000mil. Q1 segment OP reached 56% of 1H forecast. Since FY23 Q1, when the firm faced production throughput issues and cost increases as it had to subcontract out orders to meet the demand, throughputs gradually improved. Consequently, segment OP (Japanese GAAP basis) has steadily risen from ¥529mil in FY23 Q1, ¥2,047mil in FY23 Q2, ¥2,584mil in FY23 Q3, ¥2,379mil in FY23 Q4. Although the FY24 IFRS-based Q1 figure is ¥2,800mil, quarterly segment OP, as a trend, further recovered.

As stated in its medium-term plan, Daido Steel plans to invest in large-sized radial forging machines and vacuum induced machinery [VIM] that will improve throughput. For the time being, the firm has secured sufficient production capacity to meet its FY24 earnings forecast. Thanks to productivity improving, segment OP of approx. ¥2,500~¥3,500mil per quarter will likely be achieved.

Daido Steel (5471JP): Sales, OP and OPM by Segment (FY24 numbers adjusted for Japanese GAAP)								
(¥mil)		FY23			FY24 CE (adjusted for Japanese GAAP)			
		1H	FY	YoY (%)	1H CE	YoY (%)	FYCE	YoY (%)
Specialty Steel	Sales	108,904	219,021	2.0	110,000	1.0	225,000	2.7
	OP	6,322	14,797	51.4	5,500	-13.0	13,500	-8.8
	OPM (%)	5.8	6.8	+2.3ppt	5.0	-0.8ppt	6.0	-0.8ppt
High Performance Materials & Magnetic Materials	Sales	102,609	202,832	-7.7	100,000	-2.5	210,000	3.5
	OP	7,066	14,432	-40.6	9,500	34.4	21,000	45.5
	OPM (%)	6.9	7.1	-4.0ppt	9.5	+2.6ppt	10.0	+2.9ppt
Parts for Automobile and Industrial Equipment	Sales	51,402	105,633	4.3	55,000	7.0	115,000	8.9
	OP	2,576	7,539	-8.3	5,000	94.1	11,500	52.5
	OPM (%)	5.0	7.1	-1.0ppt	9.1	+4.1ppt	10.0	+2.9ppt
Engineering	Sales	11,014	23,117	22.0	10,000	-9.2	20,000	-13.5
	OP	1,066	2,424	70.1	500	-53.1	1,500	-38.1
	OPM (%)	9.7	10.5	+3.0ppt	5.0	-4.7ppt	7.5	-3.0ppt
Trading & Service	Sales	14,662	30,681	28.5	15,000	2.3	30,000	-2.2
	OP	1,951	2,900	-11.9	1,500	-23.1	2,500	-13.8
	OPM (%)	13.3	9.5	-4.3ppt	10.0	-3.3ppt	8.3	-1.2ppt
Total	Sales	288,594	581,287	0.5	290,000	0.5	600,000	3.2
	OP	19,003	42,113	-10.4	22,000	15.8	50,000	18.7
	OPM (%)	6.6	7.2	-0.9ppt	7.6	+1.0ppt	8.3	+1.1ppt

Source: Nippon-IBR based on FY23 Earnings Results Materials published by Daido Steel
Total numbers are after adjusted for inter-segment trades.

Daido Steel (5471JP): Sales, OP and OPM by Segment (Cumulative)				
(¥mil)		FY24 CE (IFRS)		
		1H CE	2H CE	FYCE
Specialty Steel	Sales	110,000	115,000	225,000
	OP	5,500	7,000	12,500
	OPM (%)	5.0	6.1	5.6
High Performance Materials & Magnetic Materials	Sales	100,000	110,000	210,000
	OP	9,500	11,000	20,500
	OPM (%)	9.5	10.0	9.8
Parts for Automobile and Industrial Equipment	Sales	55,000	60,000	115,000
	OP	5,000	6,000	11,000
	OPM (%)	9.1	10.0	9.6
Engineering	Sales	10,000	10,000	20,000
	OP	500	1,000	1,500
	OPM (%)	5.0	10.0	7.5
Trading & Service	Sales	15,000	15,000	30,000
	OP	1,500	1,000	2,500
	OPM (%)	10.0	6.7	8.3
Total	Sales	290,000	310,000	600,000
	OP	22,000	26,000	48,000
	OPM (%)	7.6	8.4	8.0

Source: Nippon-IBR based on FY23 Earnings Results Materials published by Daido Steel
Total numbers are after adjusted for inter-segment trades.

RESPONDING TO TSE'S PBR1X INITIATIVE

Daido Steel aims to maintain a PBR above 1x (as of 08 August 2024, PBR is 0.64x) and has set the following strategies to improve ROE:

1. Expand sales of high value-added products, such as open die forging, high-performance stainless steel, and titanium products.
2. Efficient use of assets by 1) optimal control of inventory, 2) the liquidation of strategically held stocks and real estate.
3. Dividend policy: Daido Steel commits to a stable dividend pay-out ratio with more than 30% pay-out ratio. Under the ongoing medium-term management plan, the firm will consider boosting shareholder returns with some variation in capital allocations.

The Nikkei and Japan Alternative Data Accelerator Association [JPX] announced on 7 August 2024 that Daido Steel is one of the new constituents of JPX400, one of the benchmark indices, thanks to the firm's efforts to improve asset efficiency by unwinding strategically held shares.

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