

Due Diligence Report: Steel is Getting Heavier and Sinking Faster: AK Steel on a Downward Trend

Summary

AK Steel Holding Corporation (AK Holding), incorporated on December 20, 1993, is an integrated producer of flat-rolled carbon, stainless and electrical steels and tubular products through its wholly-owned subsidiary, AK Steel Corporation (AK Steel and, together with AK Holding, the Company). The operations of the Company and its wholly owned subsidiaries consist primarily of eight steelmaking and finishing plants, two coke plants and two tube manufacturing plants across six states, which include Indiana, Kentucky, Michigan, Ohio, Pennsylvania and West Virginia. These operations produce flat-rolled carbon steels, including coated, cold-rolled and hot-rolled carbon steel products, and specialty stainless and electrical steels that are sold in sheet and strip form, as well as carbon and stainless steel that is finished into welded steel tubing. These products are sold to the automotive, infrastructure and manufacturing, and distributors and converters markets. The Company has interests in iron ore through its 49.9% equity interest in Magnetation LLC (Magnetation), a joint venture that produces iron ore concentrate from previously-mined ore reserves, and in metallurgical coal through its AK Coal Resources, Inc. (AK Coal) subsidiary, which produces metallurgical coal from reserves. In addition, the Company's operations include Mexican and European trading companies that buy and sell steel and steel products and other materials. The Company's flat-rolled carbon steel products are sold primarily to automotive manufacturers and to customers in the infrastructure and manufacturing market. The infrastructure and manufacturing market includes electrical transmission, heating, ventilation and air conditioning equipment, and appliances. The Company sells coated, cold-rolled and hot-rolled carbon steel products to distributors, service centers and converters. It sells its stainless steel products to manufacturers and their suppliers in the automotive industry, to manufacturers of food handling, chemical processing, pollution control, medical and health equipment, and to distributors and service centers. The Company sells its electrical steel products in the infrastructure and manufacturing market. These products are sold primarily to manufacturers of power transmission and distribution transformers, both for new and replacement installation. The Company also sells electrical steel products for use in the manufacture of electrical motors and generators. The Company's facilities include Ashland Works, Butler Works, Coshocton Works, Dearborn Works, Mansfield Works, Middletown Works, Rockport Works and Zanesville Works. All of these facilities are owned by the Company, either directly or through wholly owned subsidiaries. Ashland Works is located in Ashland, Kentucky, and produces carbon steel. It consists of a blast furnace, basic oxygen furnaces and continuous caster for the production of carbon steel and a coating line. Butler Works is located in Butler, Pennsylvania, and produces stainless, electrical and carbon steel. The Butler Works also includes a hot rolling mill, annealing and pickling units and two fully automated tandem cold rolling mills. It has various intermediate and finishing operations for both stainless and electrical steels. Coshocton Works is located in Coshocton, Ohio, and consists of a stainless steel finishing plant containing two Sendzimer mills and two Z-high mills for cold reduction, four annealing and pickling lines, nine bell annealing furnaces, four hydrogen annealing furnaces, two bright annealing lines and other processing equipment, including temper rolling, slitting and packaging facilities. Dearborn Works is located in Dearborn, Michigan. Its operations include carbon steel melting, casting, hot and cold

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rolling and finishing operations for carbon steel. It consists of a blast furnace, basic oxygen furnaces, two ladle metallurgy furnaces, a vacuum degasser and two slab casters. Also located at the Dearborn site are a hot rolling mill, a pickle line/tandem cold mill, batch anneal shops, a temper mill and a hot-dip galvanizing line for finishing products. Mansfield Works is located in Mansfield, Ohio, and produces stainless steel. Its operations include a melt shop with two electric arc furnaces, a ladle metallurgy furnace, an argon-oxygen decarburization unit, a thin-slab continuous caster and a hot rolling mill. Middletown Works is located in Middletown, Ohio. It melts carbon and processes carbon and stainless steel. It consists of a coke facility, blast furnace, basic oxygen furnaces and continuous caster for the production of carbon steel. Also located at the Middletown site are a hot rolling mill, cold rolling mill, two pickling lines, four annealing facilities, two temper mills and three coating lines for finishing products. Rockport Works is located near Rockport, Indiana, and consists of a continuous cold rolling mill, a continuous hot-dip galvanizing and galvannealing line, a continuous carbon and stainless steel pickling line, a continuous stainless steel annealing and pickling line, hydrogen annealing facilities and a temper mill. Zanesville Works is located in Zanesville, Ohio, and consists of a finishing plant for some of the stainless and electrical steel produced at Butler Works and Mansfield Works and has a Sendzimer cold rolling mill, annealing and pickling lines, high temperature box anneal and other decarburization and coating units. AK Tube LLC (AK Tube), a Company subsidiary, has a plant in Walbridge, Ohio, which operates six electric resistance welder tube mills and a slitter. AK Tube also has a plant in Columbus, Indiana, which operates eight electric resistance welder and two laser welder tube mills. AK Coal produces metallurgical coal from reserves in Somerset County, Pennsylvania. Mountain State Carbon, LLC, a Company subsidiary, is located in Follansbee, West Virginia. It is a coke making facility and consists of four batteries with total permitted coke making capacity of approximately 700,000 tons per year.

AK Steel Holding Corporation has a current market capitalization of \$481.94 M with 177.81 M outstanding shares. Its daily average volume traded is 7.84 M shares.

Key Indicators (Q2 2015)

Shares Outstanding	177.81 M
Revenue (FY 2014)	1689.40 M
Gross Profit	101.80 M
Net Loss (basic/diluted)	-64.0 M
Cash and Short-term Inv	75.0 M
Total Debt	2442.50 M

Performance (6 months)



Recent News and Analysis:

The company recently announced it will suspend some operations at its Ashland Works facility in Kentucky in December, due to challenges to the domestic steel industry. The idling of certain operations, such as its blast furnace and other steelmaking processes, could last more than six months. The hot-dip galvanizing line, which services the automotive sector, will not be affected. The company could lay off as many as 733 workers in Kentucky as early as Dec. 18. A union leader said the notice would impact 613 of his union members out of the 940 people at the Kentucky plant. This news has sent the stock downwards even more so than the sagging steel industry. Shares have been on a falling trend for the past several weeks, falling from a high of \$3.11 in early October to a close of \$2.53 on Wednesday. Technical analysts have spotted several bearish indicators of which the fall of the 50 day moving average below the 200 day moving average signals a long term bearish trend. However, from a comparison standpoint relative underperformance over the last year has improved more recently. AKS's share price performance of -56.03% over the last 12 months is below its peer median. However, its 30-day trend of -1.42% is now around the peer median suggesting that the company's recent performance has improved relative to peers. According to data released by the American Iron and Steel Institute, the US steel industry has operated at capacity utilization rates below 75% for the most part of 2015. AK Steel (AKS) operated its plants at ~78% capacity in 2Q15. AK Steel's capacity utilization rates have fallen in recent quarters after its acquisition of the Dearborn plant. This could solidify the trends observed by the technical analysts.

Conclusions:

Analysts have rated the stock unfavorably as a result of several key factors; these include its feeble growth in its earnings per share, deteriorating net income, poor profit margins and generally disappointing historical performance in the stock itself. AK Steel has experienced a steep decline in earnings per share in the most recent quarter in comparison to its performance from the same quarter a year ago. Earnings per share have declined over the last year. During the past fiscal year, AK Steel reported poor results of -\$0.74 versus -\$0.34 in the prior year. For the next year, the market is expecting a contraction of 4.7% in earnings (-\$0.78 versus -\$0.74). The company, on the basis of change in net income from the same quarter one year ago, has significantly underperformed when compared to that of the S&P 500 and the Metals & Mining industry. The net income has significantly decreased by 274.3% when compared to the same quarter one year ago, falling from -\$17.10 million to -\$64.00 million.

Sources:

1. <http://www.reuters.com/finance/stocks/companyProfile?rpc=66&symbol=AKS>
2. <http://stockcharts.com/h-sc/ui?s=AKS&p=D&b=5&q=0&id=p09736356888>
3. <http://www.google.ca/finance?q=NYSE%3AAKS&fstype=ii&hl=en&gl=ca&ei=rfgwnVsC9KpDKjAHsq6P4DQ>
4. <http://www.bizjournals.com/dayton/news/2015/10/16/ak-steel-plans-layoffs-as-flood-of-imports-hits.html?ana=yahoo>
5. <http://www.capitalcube.com/blog/index.php/ak-steel-holding-corp-breached-its-50-day-moving-average-in-a-bearish-manner-october-20-2015/>

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Disclosure: I, Robert Borowski, research analyst have no positions in any stocks mentioned, and no plans to initiate any positions within the next 72 hours. I wrote this article myself, and it expresses my own opinions and I have no business relationship with any company whose stock is mentioned in the article.

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