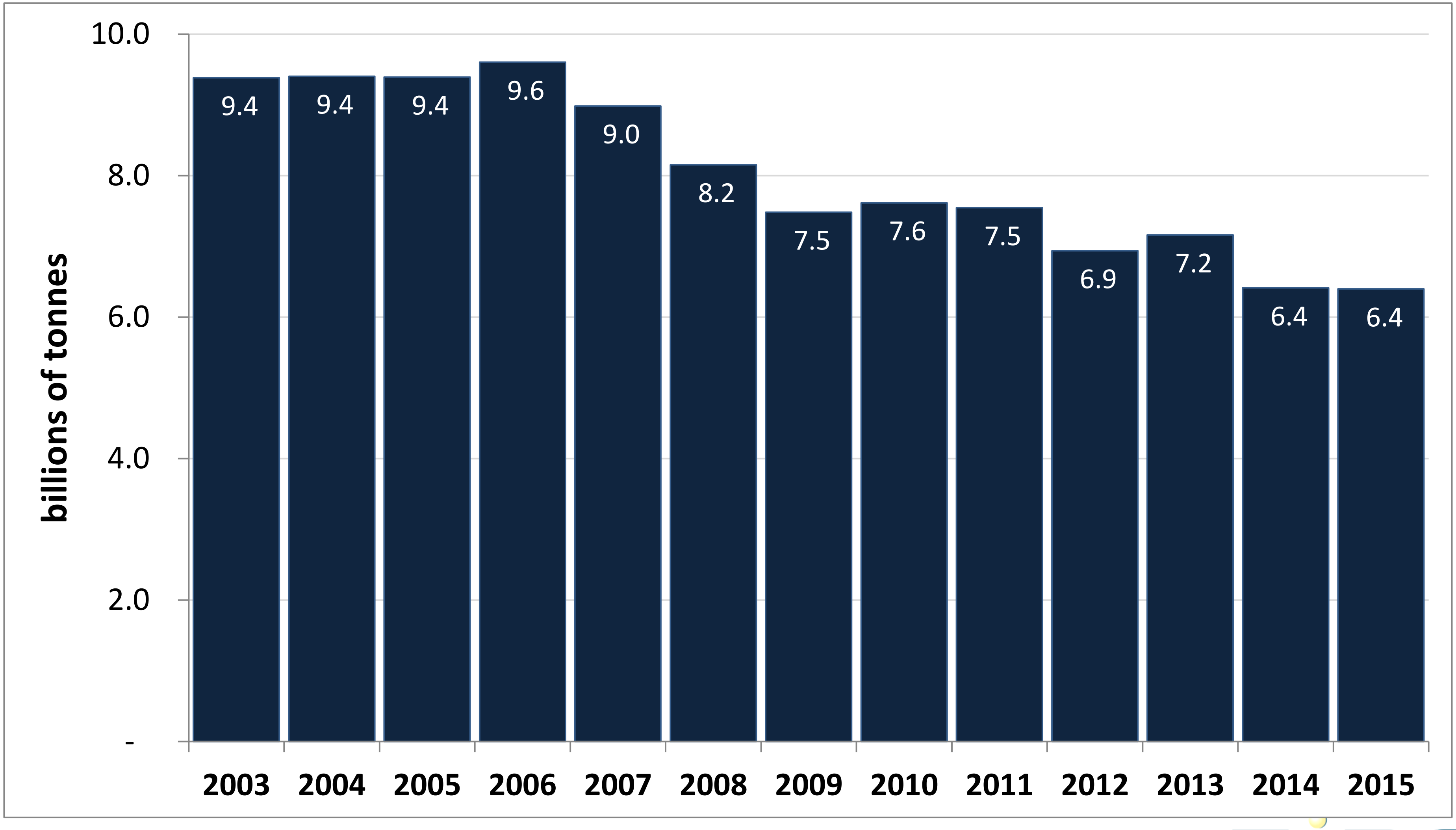
The Steel Crisis and Levers for Addressing It

May 2016

Overview

- The nature of the crisis
- Thinking about industrial policy and steel

What constitutes a crisis…

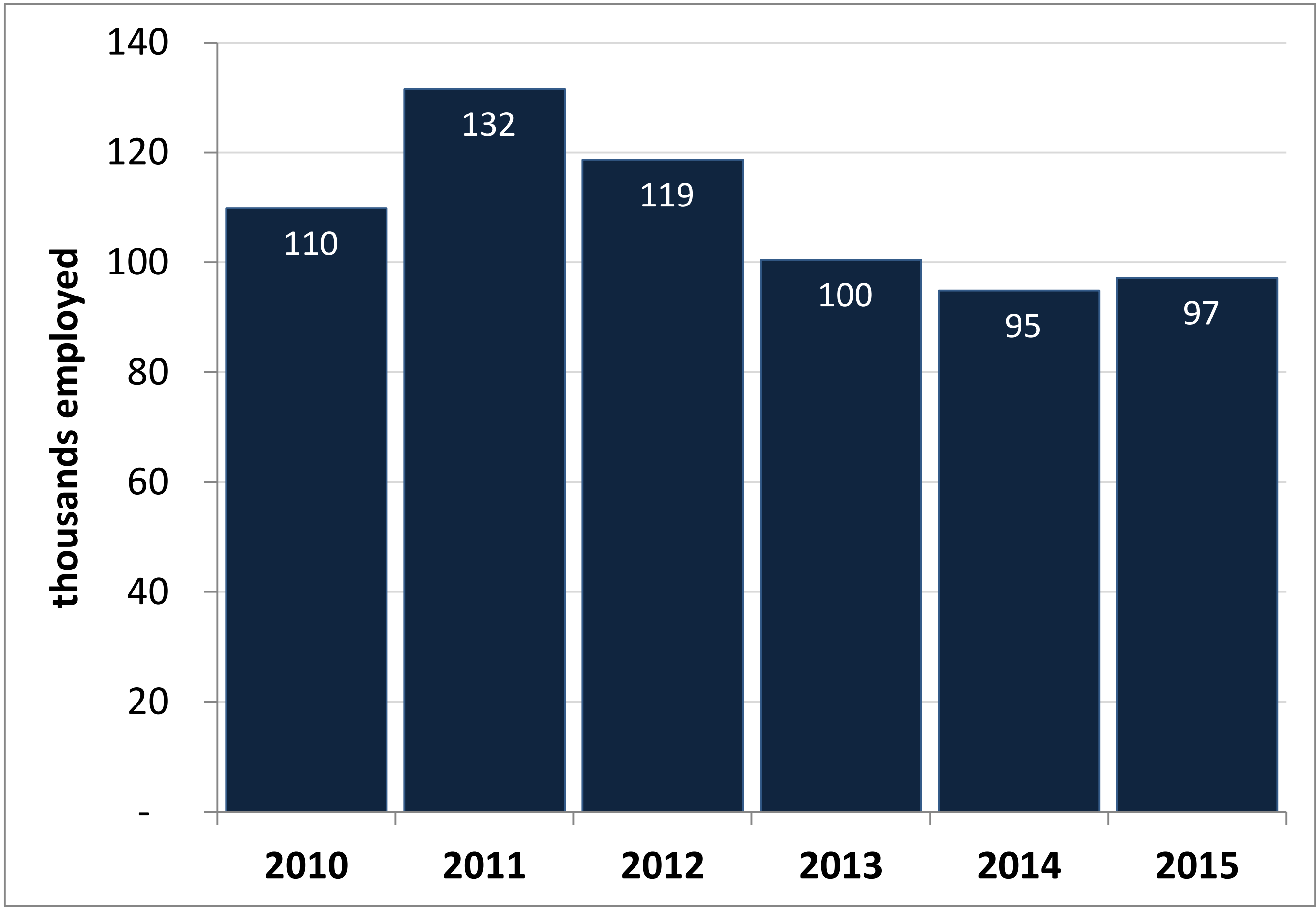


...and whose?

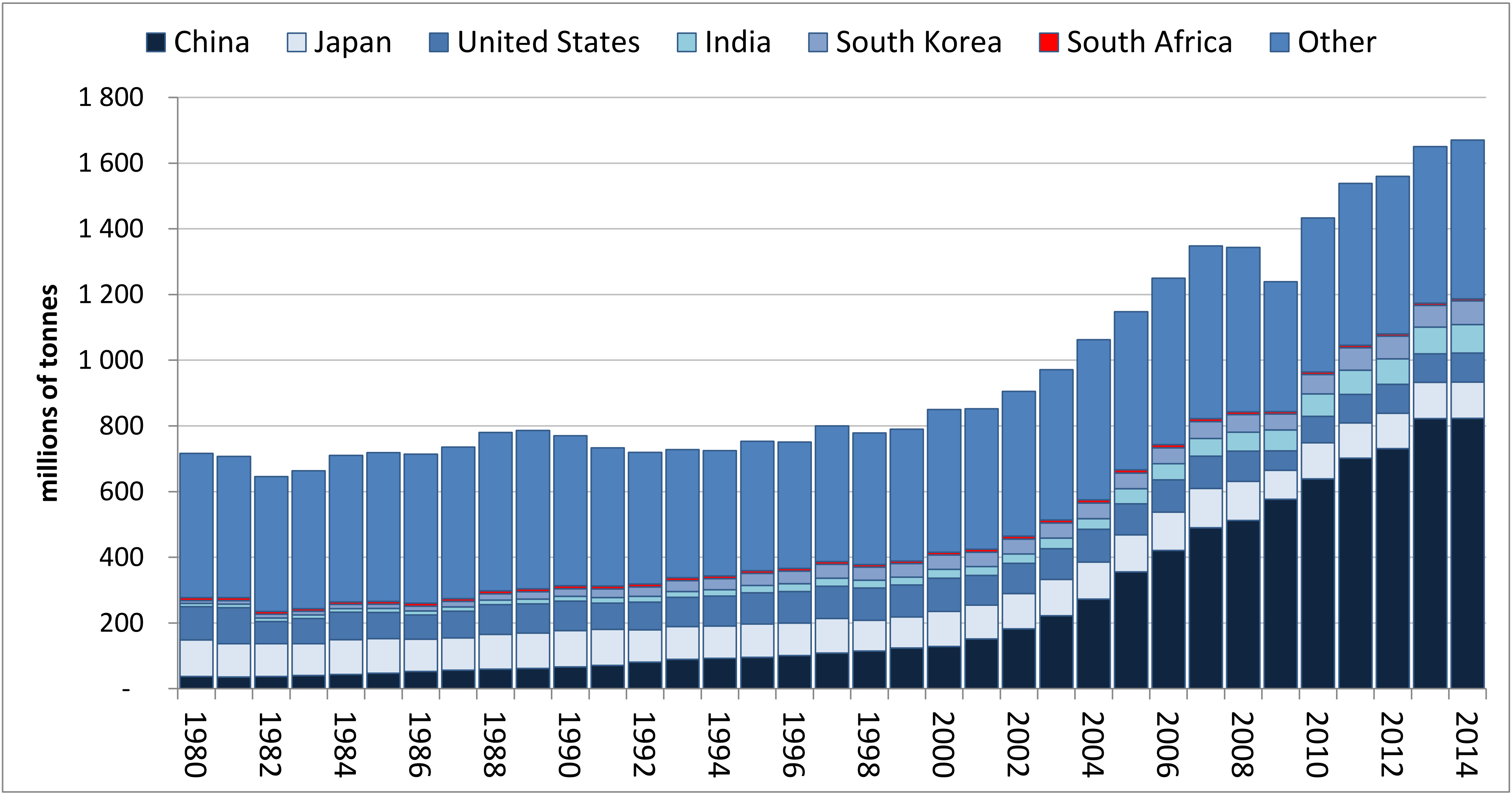
- Basic iron and steel made losses for most of the past five years.
- The pre-tax profits of the largest steel producer, AMSA, fell from R9 billion in 2008 to losses averaging R300 million a year from 2009 to 2014. In 2015, it lost R8,6 billion.
- A major ferro alloy producer, Evraz Highveld, was undergoing business rescue in mid-2016, with much of its capacity being broken up. Samancor was also looking at major downsizing.
- The number of foundries in South Africa fell from 140 in 2009 to 95 in 2014, while their output dropped 28%, from 406 000 tonnes to 310 000
- Steel users have never gotten much benefit from iron ore and steel rents – dumped imports may be an advantage

Employment

- Employment in basic metals and metal products fell from 350 000 in first quarter 2008 to 250 000 in 2016
- Employment fell by over 30% from 2011, compared to under 20% in the rest of manufacturing

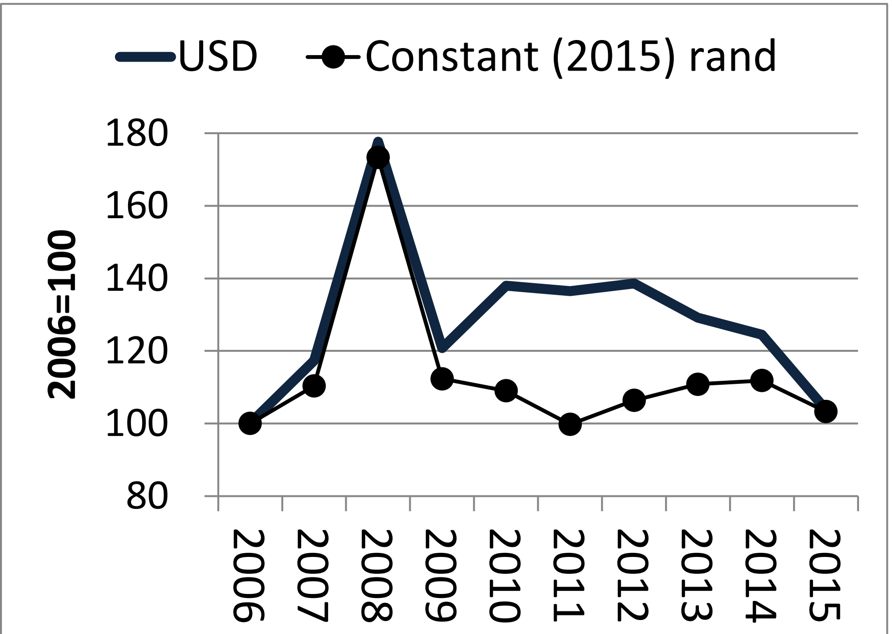


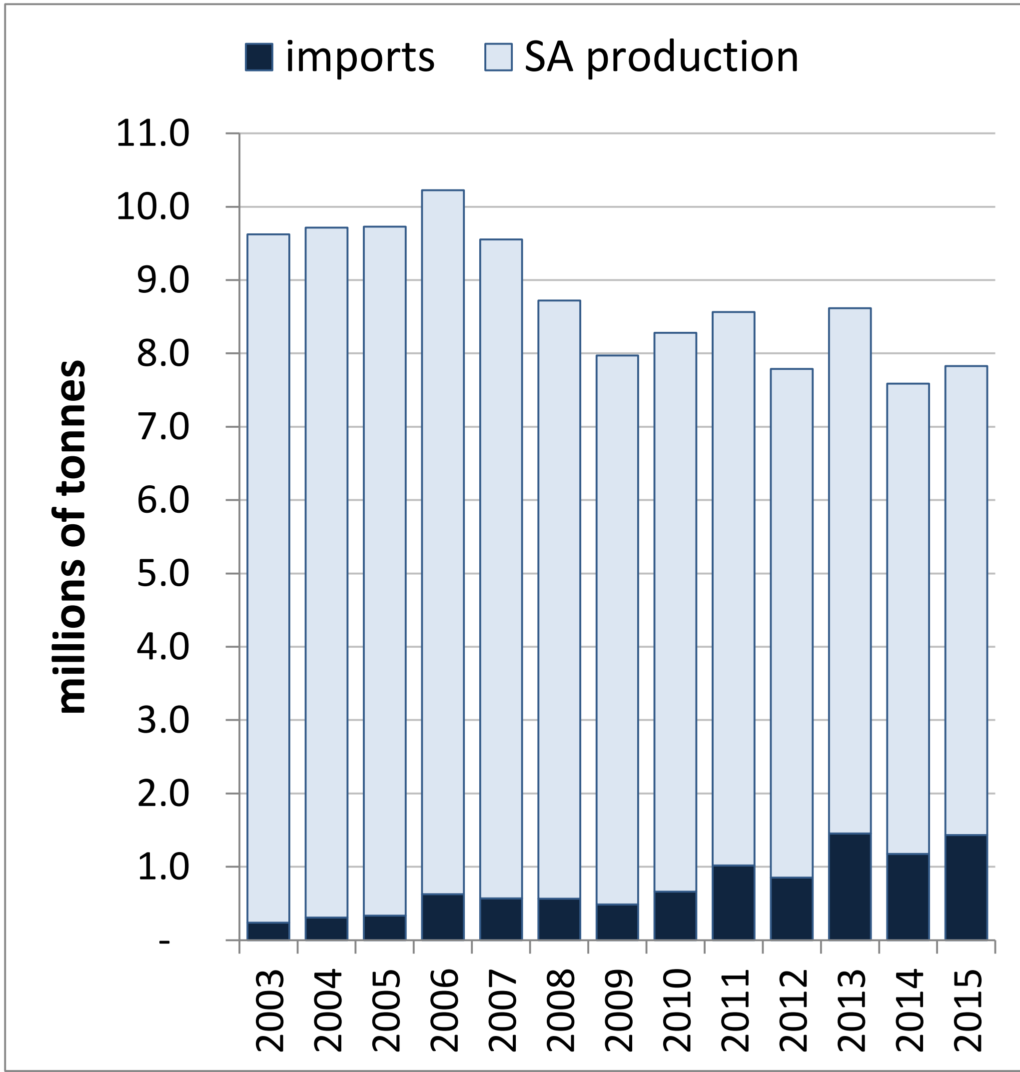
The steel glut



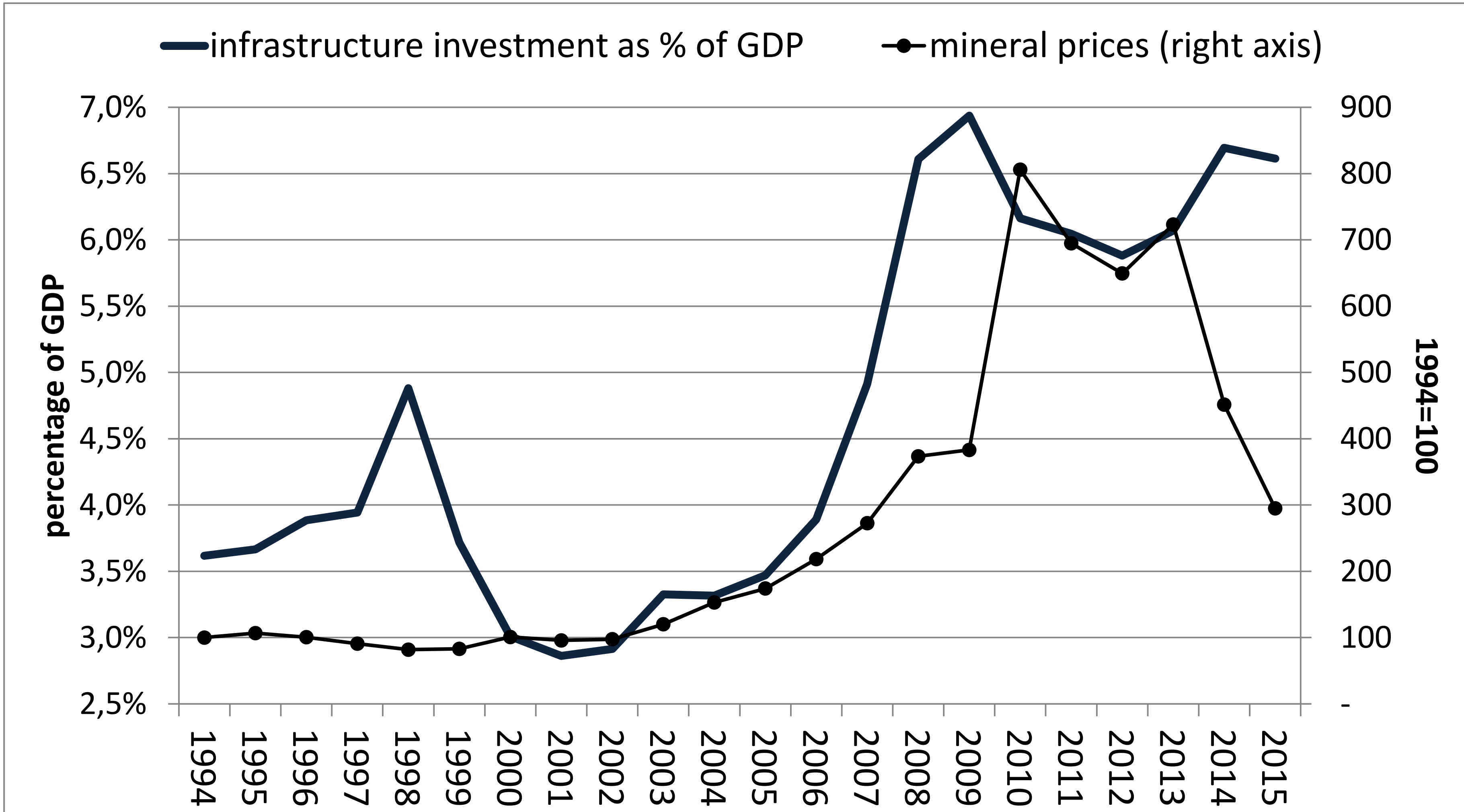
Steel imports

- Steel imports climbed from 3% in 2003 to 12% in 2012
- They then climbed to between 18% and 23% from 2013 to 2015





Domestic demand

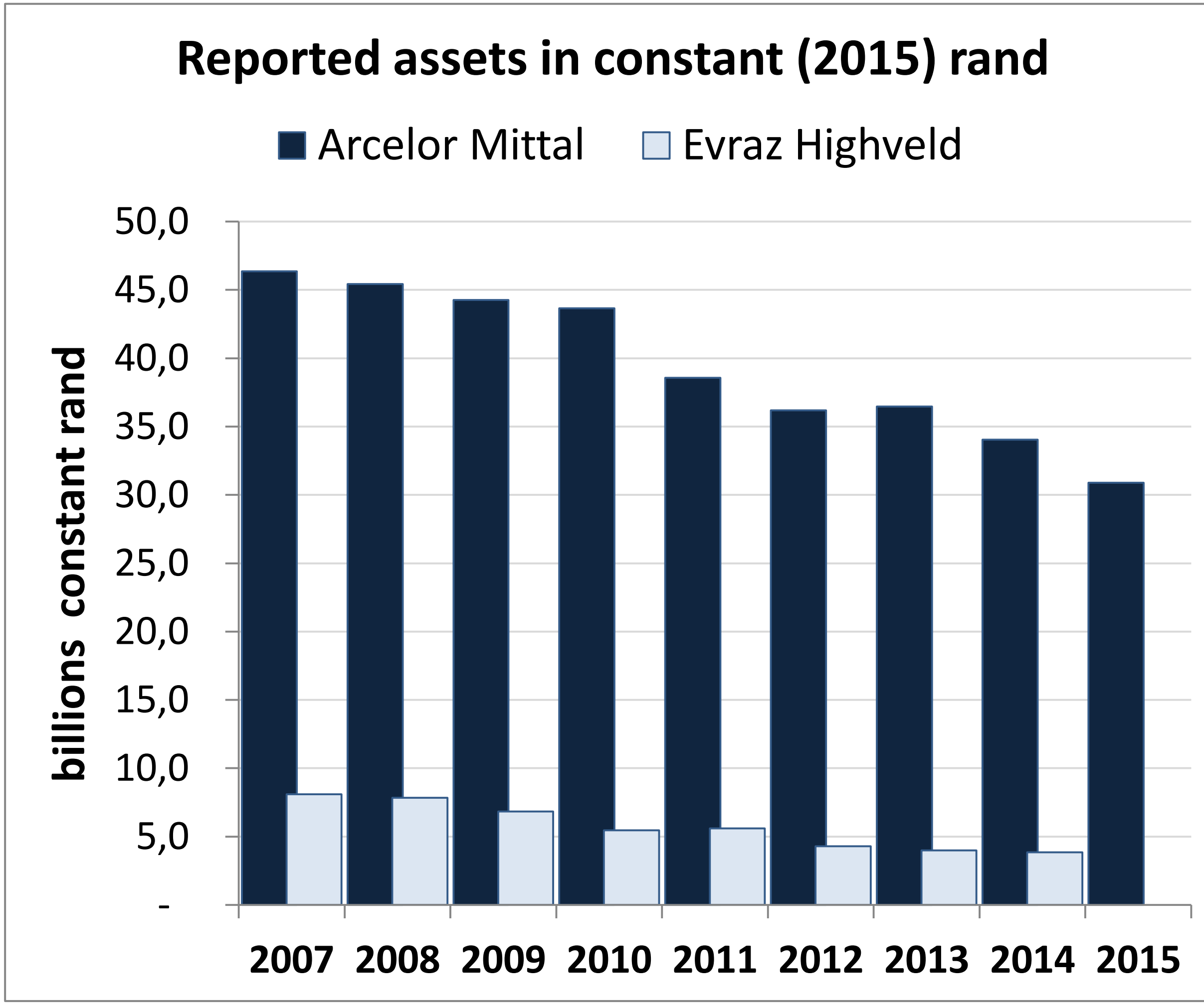


Supply side issues

- End state: When the glut moderates, SA should be left with a steel industry that is sustainable and competitive, with strong downstream fabrication and moderate prices for local manufacturers
  - Based on high-class iron ore and extensive capabilities and logistics built up over a Century
  - May be smaller
- Will require that address factors that undermine competitiveness

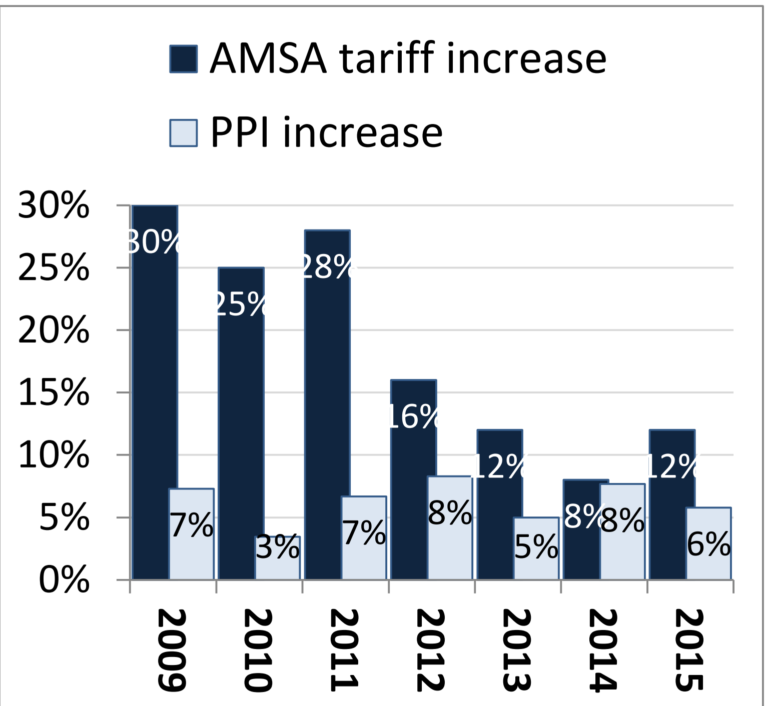
Sweated assets

- During the commodity boom, easy to sweat assets
- Especially as key mines and refineries owned by foreign mining conglomerates
- Value of assets of major producers declined from early '00s

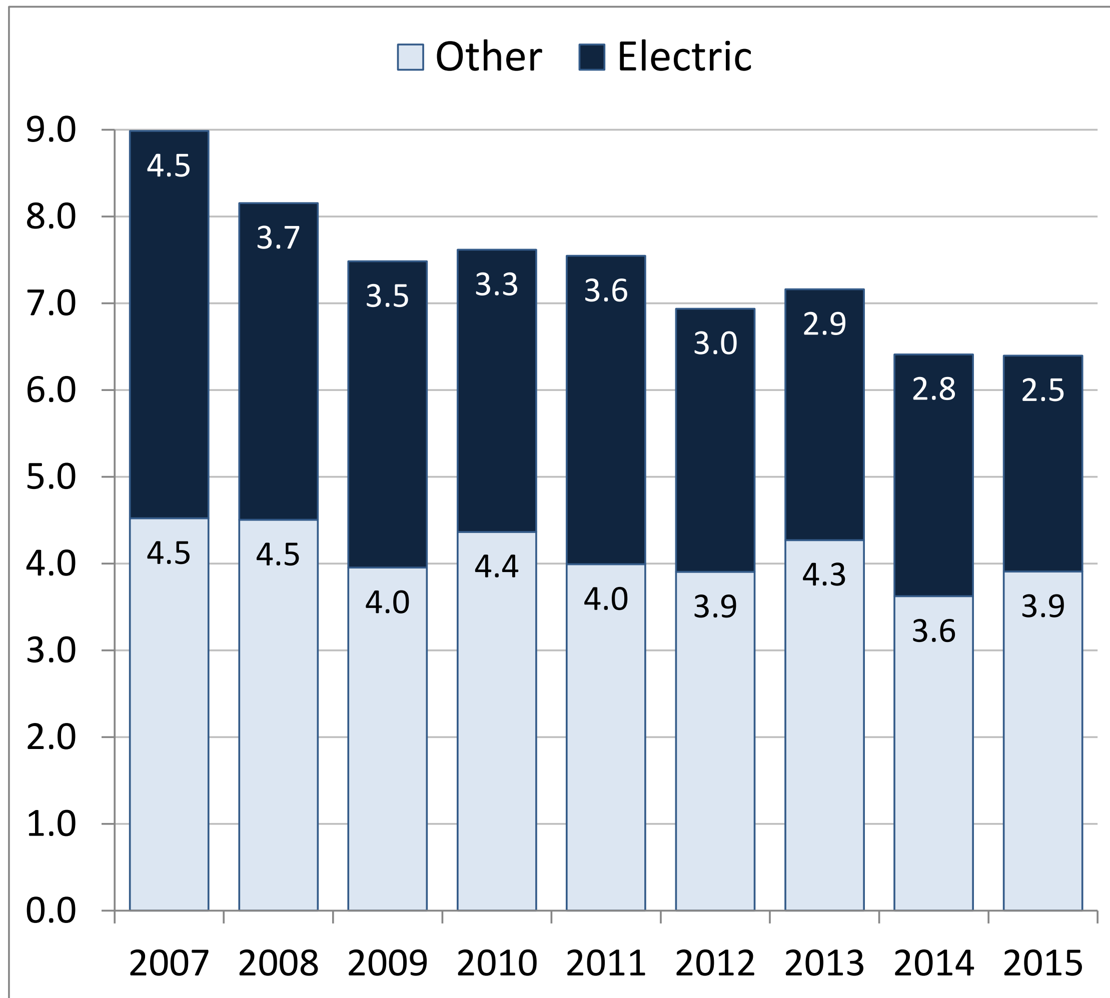


Electricity

- Electricity price to industry more than tripled from 2008
- Result: Closure of electric furnaces
- Companies that could not reduce electricity use – such as foundries – often closed down

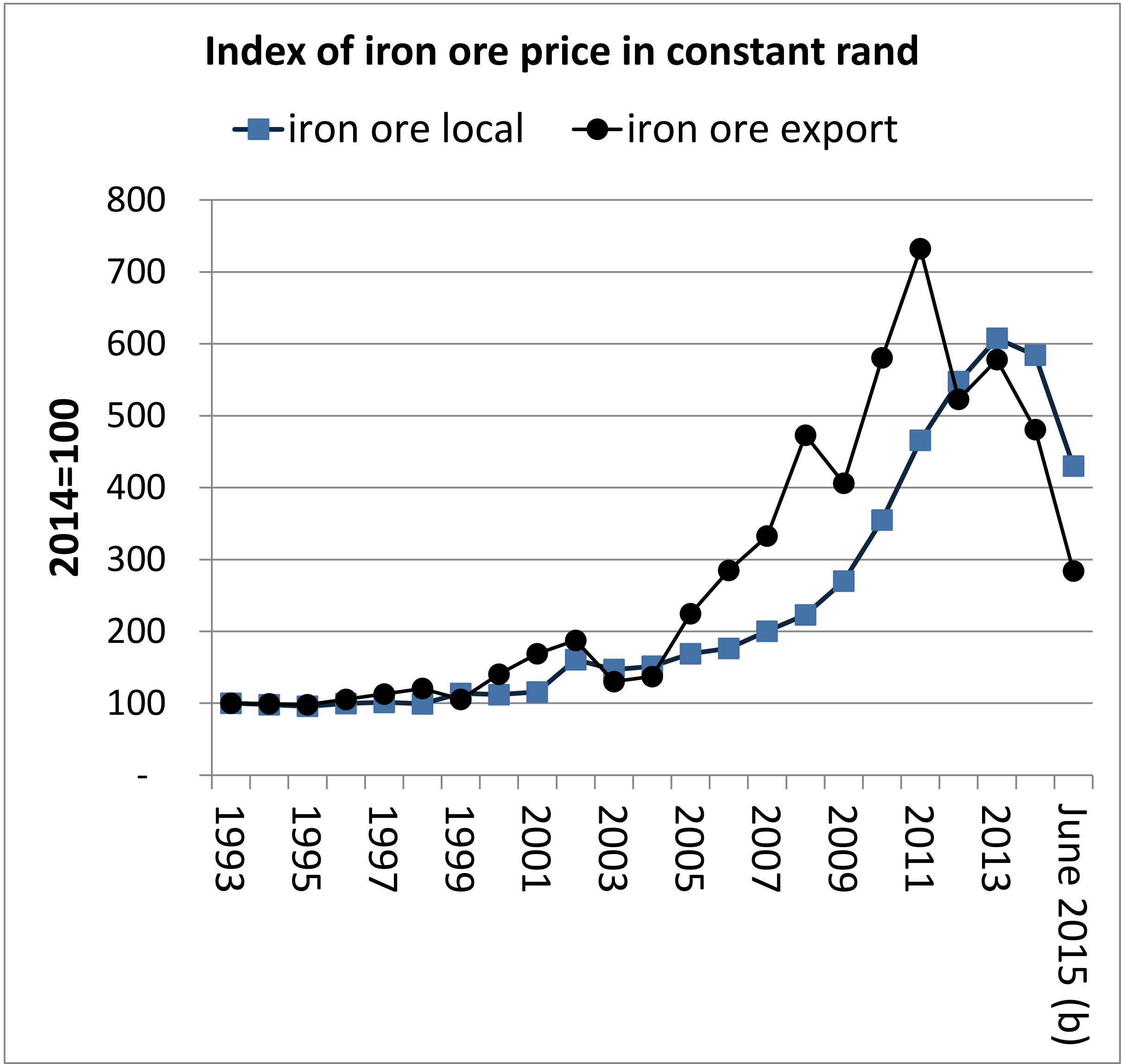


Production by type of process, in millions of tonnes



Iron ore prices

- Ferro alloys were vertically integrated, so they could manage ore prices
- AMSA faced Kumba, which sought to charge export parity prices as a minimum
- When iron ore prices crashed after 2011, AMSA ended up paying more than exports



Regulatory burdens

- Competition issues – AMSA set aside R1,2 billion in 2015, equal to 4% of its gross revenue
- Until recently, steel deemed to be local in designations
- Tariffs to protect AMSA harm downstream producers at least in short run
- Historic clean-up costs and carbon tax
- Arguably, failure to manage ore and scrap prices

… How to prioritise and ensure alignment – especially given end of the commodity boom?

TIPS

Levers

Supply

Input costs (ore, coal, scrap)
Infrastructure (access, costs)
New investment
Rationalisation
Labour costs
Regulatory costs

Stake-holders in the steel value chain

Demand

Tariffs
Designation
Deeming for steel
SOE procurement planning
Agreements with private sector
Regional marketing
Stockpiling

Sector strategy; Support for national champions

Aims

Exports (regional and overseas)

Iron ore and coal producers (Kumba, coal mines); scrap traders

Steel and ferro alloys producers (AMSA, Evraz, Columbus, Scaw)

Construction/ Infrastructure (Eskom, Transnet, mines)

Traders (MacSteel)

Fabricators (tanks, machinery, transport equipment)

Lower prices to domestic users

Avoid unnecessary closures

Modernisation

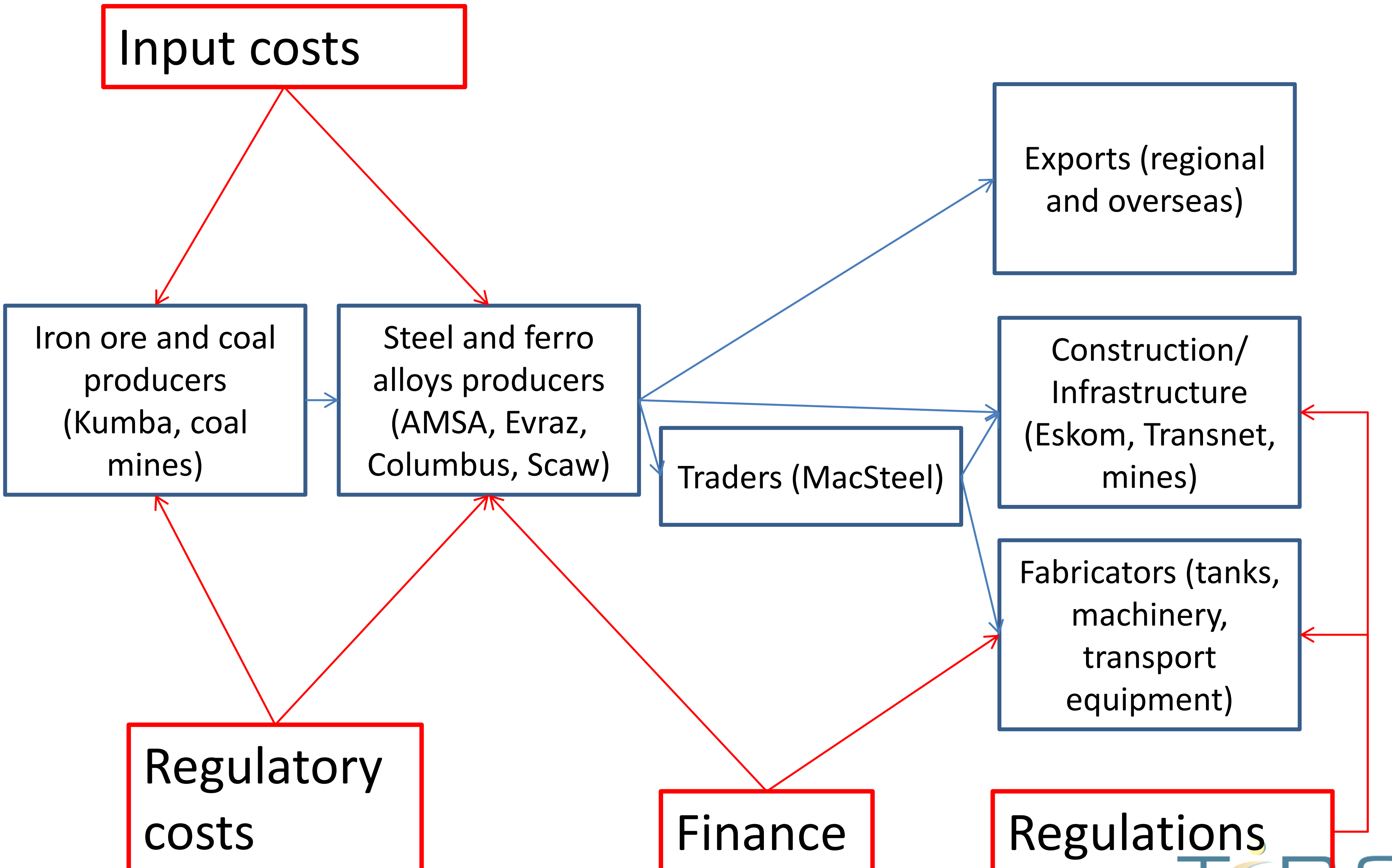
SA champions

Lower prices to steel producers

Lower mark ups

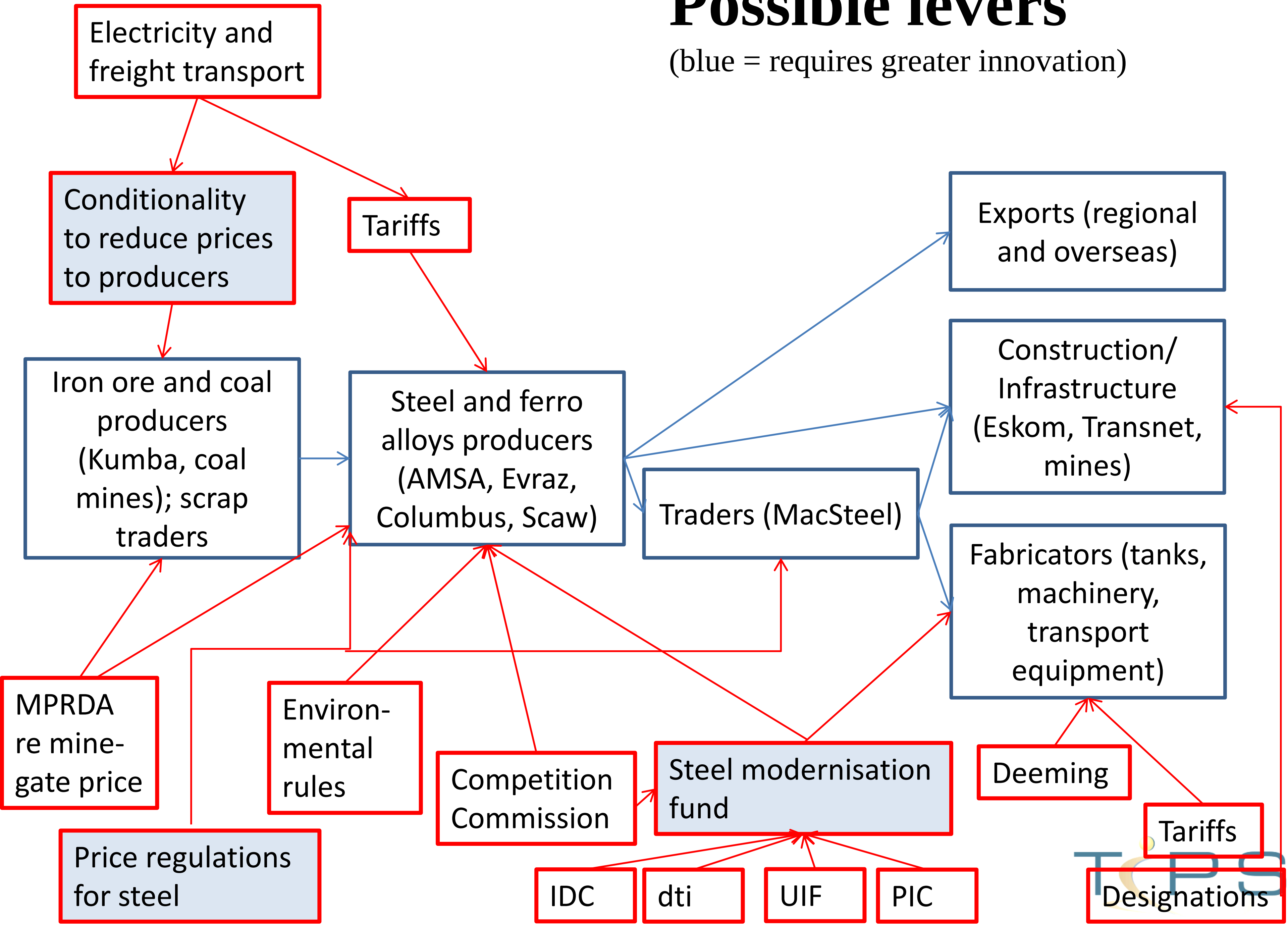
Increased local procurement

Available levers



Possible levers

(blue = requires greater innovation)



Re a leboha!