# Briefing Note 1: Downsizing at AMSA: Impacts, causes, and industrial policy implications

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On 28 November, ArcelorMittal South Africa (AMSA) announced that it was closing down its production of long steel products, around a third of its capacity, located mostly in Newcastle and Vereeniging. These products, which include coil and rods, account for a quarter of its steel output and a third of its employment. The decision does not affect AMSA's flat steel production, which covers steel plate and structural beams and is located at Vanderbijlpark.

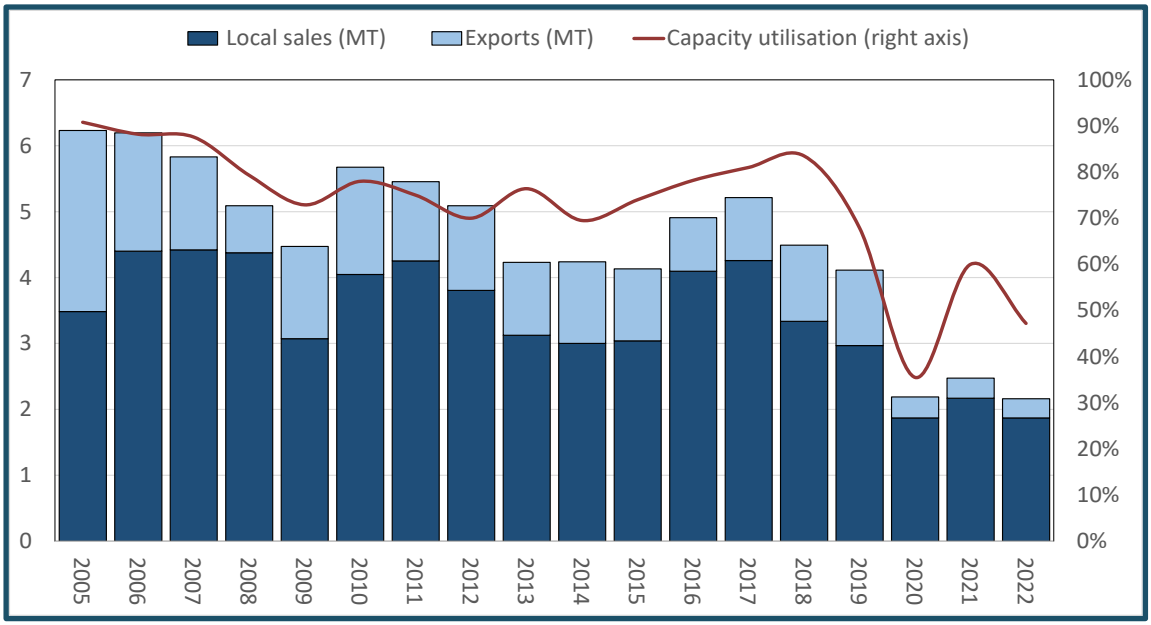
AMSA's downsizing will not have large direct economic impacts in the short run. Still, it is a warning signal for industrial policy. From the 1920s, the steel value chain has been central to South African industrialisation. From this standpoint, downsizing at AMSA reflects the crumbling of the minerals-energy complex (MEC) that underpinned mining-based growth through the apartheid era. The decline in AMSA also points to areas for improvement in the master plan process. After all, the Steel Master Plan was only published two years ago.

The AMSA decision affects 3 200 employees and probably about R10 billion in sales, although AMSA stopped publishing separate figures for flat and long steel 10 years ago. Basic steel products can increasingly be produced by mini-mills or imported at competitive prices. By extension, downstream users – mostly in metals fabrication (which has around 100 000 employees) and construction – should be able to adapt, although delays on imports remain a problem.

AMSA faced a perfect storm in 2022/23, with falling sales and rising competition coinciding with increasingly disrupted and expensive electricity and freight.

In the 2020s, AMSA's sales collapsed by 50%. (Graph 1) Exports, which go almost exclusively to other African countries, dropped particularly sharply. But AMSA's sales have been gradually shrinking for much longer. In the late 2010s, before the pandemic, its sales by volume were already lower than a decade earlier.

**Graph 1. AMSA local and export sales in millions of tonnes and capacity utilisation, 2005 to 2023**




*Source: AMSA Annual reports for relevant years.*

The collapse in steel demand had three obvious roots. Slow growth after the recovery from the pandemic bit into sales in general. Rising imports also hurt. They climbed from 4% of total steel sales in South Africa in 2003 to 16% in the first nine months of 2023. More recently, growing production by scrap-based mini-mills increased competition with AMSA's vastly larger and older plants.

At the same time, AMSA began to pay an increasingly heavy price for the dysfunction at Eskom and Transnet. In 2022, it estimated that loadshedding reduced output by R95 million. The escalating problems at Transnet proved even more costly. AMSA argued that, in 2022, it lost R600 million in sales because of transport delays. In addition, its freight costs rose by R500 million as it shifted to road carriers.

It is telling that Eskom and Transnet contributed so much to AMSA's woes. AMSA originated as the state-owned Iscor in 1928; it was privatised in 1989, and in 2006 ultimately integrated into ArcelorMittal, the international steel firm. Iscor's success was predicated on high quality, cheap local iron ore; low-cost coal-fuelled electricity from Eskom; and efficient, affordable freight transport from Transnet. The trinity of Eskom, Transnet and Iscor formed the central pillar of the MEC, understood here as the collaboration between mining, the state and the metals and coal refineries that drove South African industrialisation through the 1970s.

A complex of economic and political factors unravelled this pathway to industrialisation over the past 30 years. Key issues included the emergence of more competitive and smaller scale technologies; the opening of the economy from 1989; and increased contestation around government policies.

- On the technological front, AMSA is dealing with the emergence of steel mini-mills that have far lower initial costs. Eskom faces even steeper challenges. Above all, renewable energy is now both cheaper and cleaner. Meanwhile Eskom's coal plants are aging and badly managed.

In response, it has tended to raise its tariffs, further squeezing demand and pushing up its unit costs. In 2009, AMSA used 2% of Eskom's electricity. By 2022, as it shifted to less electricity-intensive technologies, its share had fallen below 1%.

- The opening of the economy is most obviously associated with the surge in steel imports. The opening of the economy also boosted input costs. A tenet of the MEC was that upstream coal and iron ore mines charged cost-plus prices to domestic partners, effectively relinquishing some rents to expand domestic demand. In the past two decades, however, both the coal and iron ore mines have increased their domestic prices closer to international levels, raising costs for both AMSA and Eskom.

  Some observers have argued that after the acquisition by ArcelorMittal, AMSA used export pricing and management contracts to shift liquidity out of the country. In constant rand, the value of AMSA's assets dropped by half over the past 20 years. AMSA reports that, despite lower production costs per tonne than the rest of Arcelor Mittal, its EBITDA[1] hovered near zero through the late 2010s, far below its parent company's norm.

- The transition to a vibrant, inclusive democracy made it more difficult for the state to prioritise a few big industrial companies and capital-intensive heavy industry. After all, these activities provided little visible benefit to most citizens. The result was often long delays in addressing challenges such as loadshedding, ports congestion and excessive delays in freight rail. Even after solutions were nominally agreed on, implementation often proved halting.

The Steel Master Plan did little to resolve these systemic challenges. To start with, it did not define an over-arching strategy for the industry. Instead, it included a list of competing claims from different segments of the value chain. The trade-offs emerged graphically around proposals to reduce the price of scrap by limiting exports. The master plan presents this as a consensus position that benefited all producers. AMSA now contends, however, that it effectively subsidised competing mini-mills.

The negotiation of claims and proposals in the Steel Master Plan contrasted with the approach in the auto industry, which was supposed to be its model. The published auto master plan centres on a coherent analysis of core strategic constraints and options. Absent that kind of evidence-based narrative, master plans may just reflect short-term lobbying and horse-trading by competing interests.

In addition, it has proven difficult to mobilise government agencies to secure fulfilment of the Steel Master Plan, notably to improve Transnet services for inland producers. As initially envisaged, the master plan process would ensure that all state agencies prioritised and supported industrial policy. In practice, the master plans have at best opened some new communication lines.

Ultimately, the downsizing at AMSA highlights three industrial-policy tenets. First, if government lacks capacity to do everything, then it should focus on its core functions – which in the economy means infrastructure, building human and social capital, and maintaining security. Second, government's role in industrial policy is to shape an environment that improves the alignment between national and business aims. It is not to mediate short-term compromises between

[1] Earnings before interest, taxes, depreciation and amortisation.

stakeholders. Finally, industrial policy should be used to rescue uncompetitive industries or companies only when the long-term socio-economic benefits – in terms of employment and opportunities for small business, technological advances, or exports – unambiguously outweigh the costs. By extension, before considering trade protection or incentives, industry-level initiatives should identify the potential for more inclusive growth, and propose strong strategies to manage down the main cost drivers.