

Unclassified

CCNM/EMEF/SC(98)12



Organisation de Coopération et de Développement Economiques
Organisation for Economic Co-operation and Development

OLIS : 22-May-1998
Dist. : 25-May-1998

Or. Eng.

**CENTRE FOR CO-OPERATION WITH NON-MEMBERS
STEEL COMMITTEE**

Emerging Market Economy Forum

WORKSHOP ON STEEL TRADE ISSUES

**PERSPECTIVES ON STEEL MARKETS AND TRADE
STATEMENT BY DUFERCO**

The Workshop will be held in Paris on 27-28 May 1998.

Contact: Mr. Wolfgang Hübner, Head of DoT and the Steel Unit, STI; tel.: (33 1) 45 24 91 32;
fax: (33 1) 45 24 88 65; Internet: Wolfgang.Hubner@oecd.org

65795

Document complet disponible sur OLIS dans son format d'origine
Complete document available on OLIS in its original format

CCNM/EMEF/SC(98)12
Unclassified

Or. Eng.

**WORKSHOP ON STEEL TRADE ISSUES
PERSPECTIVES ON STEEL MARKETS AND TRADE:
COMMERCIAL OPPORTUNITIES IN THE FERROUS
OR NON FERROUS METAL SECTORS OF THE CIS
STATEMENT BY DUFERCO
PARIS, 27-28 MAY 1998**

GLOBAL MARKET AND ITS IMPLICATIONS ON CIS

GLOBAL STEEL MARKET OVERVIEW

- Slow growth in consumption
- Far East crisis
- Consolidation in the developed countries
- Restructuring in the CIS
- Technological changes
- The battle to be the “low cost producer”
- Protectionism

INDUSTRIALISED COUNTRIES

- Western Europe: flat consumption, consolidation
- Japan: declining in spite of continued efforts to improve productivity and quality
- North America: productivity and efficiency improvements, new capacity, new players

ASIA AND NIC'S

- Korea: consumption falling, excess of capacity
- China: previous plans were grossly exaggerated, productivity and modernisation of existing plants have reduced the future needs by 2 to 3 green field sites
- NIC's (Thailand, Malaysia, Indonesia, Philippines): domestic consumption falling, excess of capacity, demand for semifinished bound to stay.
- India: consumption steady, building capacity

SOUTH AMERICA

- After decades, the macroeconomic environment is showing stability. Growth in domestic consumption. Imports growing. Decline of exports. New capacity planned in selective regions with large availability of raw materials. Domino effect of Far Eastern crisis lower than expected.

SOUTH AFRICA:

- Slight growth in consumption. New capacity being added for export.

AUSTRALIA

- With large availability of raw materials and energy new capacity for the production of scrap substitutes and increased focus on export in fare east markets.

CIS: PRESENT SITUATION

Business environment and individual plant fundamentals vary substantially from case to case. Following considerations are necessarily a generalisation and do not all apply to every steel facility.

FACILITIES

- Several obsolete plants, costly processes in use
- Several plants running at half original capacity
- Locations of plants generally not ideal for market reach and raw materials logistics
- Productivity per worker at sometimes one tenth of American-West European standards.
- Slow adjustment of quality level to international standards
- Small and illiquid local market, difficulties of payment from local customers
- Lack of cash for working capital and basic investments
- Difficult environment for a focused management

MARKET

- Low domestic consumption due to minimal infrastructure investment, and low private disposable income for consumable goods.
- Need to export up to 75 per cent of capacity to reach a reasonable production level.

- Export revenues penalised by geographical distances from the ports
- Export prices penalised by quality level and reliability of delivery compared to Western competitors.
- Developed countries protecting their own industries

OVERALL BUSINESS CONDITIONS

- Unstable business environment
 - Monetary uncertainties
 - Changing taxation
 - Unclear civil code
 - Law enforceability questions
 - Changing rules
 - Transportation and utility cost escalation
- Capital availability
 - Very high of cost of capital
 - Reduced availability even at high cost
 - Business partners chosen not on economics but on their availability to take risks
- Materials, yield and energy efficiency
 - Negative effects of working capital shortages on efficient flow of raw materials and optimisation of blending
 - Relatively little focus on yield and energy efficiency due to “distraction” from more impelling problems.
- Labour
 - Low wages
 - Generally low production per man employed
 - Necessity to increase real wages, reduce numbers of employees. Social amortisers, alternative job creation.

CIS: POSSIBLE ACTIONS

GOVERNMENT TO

- Provide stable macroeconomic situation
- Reinforce and clarify civil code
- Strengthen law enforcement
- Sponsor solutions for job creation programs (to employ workers made redundant by restructuring)
- Create a national investment and development bank with the mission to provide part of the funds (long terms loans) needed for **sound** investment projects
- Create the general conditions for attracting foreign capital and reducing the relative cost of both equity (expected returns) and borrowing
- Provide competitive local services (transportation, port facilities, energy, infrastructures)
- Legislate reasonable and stable taxation
- Negotiate with governments of developed countries and NIC to minimise the protectionist measures

SHAREHOLDERS TO

- Appoint competent and reliable management
- Agree the strategical plan with the management and support it financially, if necessary with new cash equity
- Look for a reasonable return on equity (versus unreasonable)

MANAGEMENT TO

- Conduct a transparent way of business
- Create conditions to provide incentives for middle management towards strategic goals of efficiency/effectiveness

POTENTIAL FOREIGN PARTNERS

- Local partners have a natural priority but may be financially and technologically a limiting factor

- Foreign partners may be minority or majority shareholders
- Which foreign partner:
 - Financial institutions (investment fund)
 - Foreign steel mill
 - Traders
- Financial institutions do not usually meddle with management in the short term but are looking at high returns on investment and have a relative short outlook (exit strategy of 2 to 4 years)
- Steel mills can contribute financially and technologically and would be long term players; they may however be a limiting factor commercially.
- Traders can bring financial, commercial and even technical contribution. They can be long term players. On the negative side, they may look more to “side” advantages than to the long term well being of the company.

TRADING COMPANIES

- They have a suspicious reputation of being only interested in making a “quick buck”
- There are “traders” who only use local influence to make a profit while bringing little contribution
- There are traders whose obvious mission is to make a commercial profit but try to earn it through a real contribution in the financial, commercial, logistical and technical areas.
- “Goods traders” serve a key economic function in being pioneers in taking risk under difficult macroeconomic environments, and actually open the way to the more conservative financially institutions to become progressively more comfortable with the potential borrowers

CONCLUSIONS

- The question of whether metallurgy can survive in CIS countries is probably redundant: it is a must. The social impact of the reconversion of these economies is already very difficult and extremely painfully due to the necessary restructuring of the industry. It would become explosive if a large part were to disappear.
- A large part of the industry has good competitive cost advantages and reasonable equipment. It needs investments to keep up with the global rush to cut costs and improve product performances, and it needs working capital to get away from primitive form of trade (barter) and function normally.

- Management has to learn to become transparent and work closely with the shareholders.
- Restructuring is painful, but increased productivity is the only mean to raise wages. Increased wages create domestic consumption. Domestic consumption increases steel consumption and a reduced need to export.
- Steel is capital intensive. The industry cannot be abandoned “to the market” in its market infancy. A concerted effort must be implemented by governments to help its restructuring and become a competitive world player. Subsidies are a drug and therefore are lethal and wasteful. Long term development financing for sound projects, stable macroeconomics and taxation, certainty and enforceability of the law, competitive infrastructure, co-operation of governments with the companies for alternative jobs creation are instead the necessary answers.