
Stimulus plans - Led to steel overcapacity in China

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It is reported that Chinese steel industry has again been picked up as a negative example in a recently held cabinet meeting for massive overcapacity and redundant constructions after it was requested by MIIT in mid of this month to conduct structural adjustment.

The overcapacity problem was covered by China CNY 4 trillion stimulus based on higher spending on construction of highways and other public works which has generated and inflated demand for steel.

Insiders warned that the steel embarrassment will be more difficult to solve under dual pressure of less pricing power for up stream raw materials prices and passiveness in volatile down stream prices if no measures to be hammered out as fast as possible.

1. Structural Surplus Lead to Overall Overcapacity

Capacity surplus is an old story. And China Iron & Steel Association has forecasted an annual crude steel output of 460 million tonnes at the year start, leading to nearly a 200 million tonnes surplus by factoring in 660m tons domestic production capacity.

The forecast has aroused much concern and most are expecting a real and forceful structural readjustment under prevailing great pressure. However, things are getting worse. And latest figures from national statistics bureau show China's total steel production in the first seven months hit 317 million tonnes or translating into annual output of 546 million tonnes far beyond that of CISA forecasts.

Capacity utilization ratio for some products like rebar also reached above 90% since most steel mills were cranking up these products' production since mid April lured by high profit and recovering demand. Under this condition, nobody cares about overcapacity, but only sticks to production more.

Official from Baosteel's research institute also concerned about this phenomenon, saying demand is too fragile for high end products, and was easily driven up by investment and fiscal stimulus for low end products like rebar. However, these measures are both temporary demand support, once the demand boom cools down, the reignited capacity would be very hard to scrap. As a result, state council emphasized in a recent meeting to strictly control the releasing of production licenses for rebar and wire rod etc.

Mysteel analyst Mr Liu Jianzhao said "Overcapacity is certain existing in China, but it is only structural overcapacity."

2. New Model Required in Mergers & Acquisitions

The Ministry of Industry and Information Technology said in an earlier meeting that steel mergers and acquisitions seem the only way to solve overcapacity problem. And guidelines for steel M&As are likely to be released at around October.

Problems still exist in how to weed out old capacity in consolidating cases. And inefficient capacity was determined by the volume of blast furnaces according to the prevailing rules. But local mills generally upgrade the volume to above the required standards to circumvent government policy resulting in increasing capacities instead of closure.

To handle the problem, the state council said to strictly enforce environmental standards and market access. Any project failed to pass it would be washed out.

And problem also lies as how to position smaller mills products mix when it was acquired by big mills. A senior insider said "Big mills can transfer its advanced management and brand to its target, but not necessary to copy its high end products line since overcapacity also exists for these products."

(Sourced from MySteel.net)

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