Strategies for steel manufacturers during current financial crisis

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The steel industry witnessed a massive swing in demand and prices for its products during 2008. The global financial meltdown did not spare steel industry either. Expert opinions vary whether or not the worst is over. We, however, believe that 2009 would be the year when industry puts the worst behind and starts on the growth curve.

The Middle East based steel producers with somewhat easier access to finances in part due to oil wealth may lead the growth of the steel industry in coming months and years. More over, many of the Middle East governments regard steel as a strategic industry for long term economic growth of the region. This helps in reducing the negative impacts of recent down turn.

The key question faced by the executives of steel manufacturing companies as to what can they do to prepare for this change in macro operating environment?

We believe that a steel manufacturing company should follow a "portfolio approach" to substantially enhance/consolidate its position amongst leading producers of steel. We separate the portfolio of strategies into two simple categories that a company could pick and choose based on its risk taking appetite and access to capital.

1. Aggressive growth
    a. Acquisition – The valuation of both publicly listed and privately owned companies have dropped significantly. For a company with access to funds, it provides a superb opportunity to strengthen its portfolio either across geography or by the product line. The acquisition could also be focused on upstream raw material producers such as iron ore mines

    b. Brownfield expansion – Many of the companies put their Greenfield plans on hold. These plans were drawn during good times. The prices and delivery time for equipment and other services have dropped significantly. The brown field expansion during this time would be less expensive and time consuming

    c. Vertical integration – steel industry has traditionally ignored downstream integration. The change in current operating environment offers a unique opportunity to expand further downstream in a higher value add environment

2. Preserve and prepare
    a. Steel industry has been a slow adapter of information technology. As a result operating cost of a plant and materials logistics cost are high. IT provides a significant area of cost saving while enhancing the competitiveness of the company

b. Study and Debottlenecking of plant operation logistics by utilizing planned shutdown for addition/modification work, which will be less complex in the downturn

c. Maintenance management is often an ignored area resulting in tremendous build up of inventory. This inventory goes obsolete with time while one keeps on purchasing new inventory

d. Reduce cash-to-cash cycle. In our discussions with many of the CFOs, this was an area that was paid little attention. An improved cash-to-cash cycle reduces the working capital requirement thus providing cash for other strategic improvements.

e. Invest in strategic products and technologies to enable the company to have economic benefits.

These strategies are by no means comprehensive. However, they do provide a flavor of what steel manufacturer can do over next 8-18 months to take advantage of current economic downturn to better prepare for tomorrow.

The current financial market will no doubt make financing a capital intensive project more expensive and difficult to finance as projects across industries compete for limited set of resources. A properly designed portfolio of projects could significantly lower the capital requirement while improving the competitiveness.