Southeast Asian Steel Sector on Massive Growth Path

- Steelworld Research Team

After a mere 0.8% average annual growth between 2008 and 2013, Southeast Asia (SEA) has recovered in terms of steel consumption thereafter propelled largely by an influx of direct foreign investment, fuelled by cheap borrowing in the USA and Japan, and the region's growth rates exceeded those of Asia Pacific's mature economies.

SEA's growth in consumption of flat products exceeded that of long finished steel, suggesting it was experiencing changes in structural demand as the industrial production base strengthened in this emerging market. Whereas steel consumption in Asia Pacific's mature economies is forecast to grow at an average of just 1% per year between 2014 and 2020, Southeast Asia's demand for finished steel is forecast to see compound growth of 2.5% between 2014 and 2020 on estimated robust economic growth.

The region's emerging economies are expected to show robust expansion, via urbanisation and infrastructure expansion as well as by the gradual shift towards an investment-driven economic model. This will propel steel demand in the region's emerging economies to a compounded annual growth rate of 5.5% between 2014 and 2020. Construction is the largest steel end-using sector, accounting for about 75% of the take-up of long products and some 18% of the consumption of flat steel products. Ongoing urbanisation and the expansion of the industrial production base in the region's emerging markets will by 2020 see the construction sector's uptake of flat steel products to more than 20% of their uptake.

Supply Shortage

The SEA steel markets are short on domestic steel supply despite the region's own established steel industries and considerable potential growth in demand. Over the past few years, most of the demand has been served by imports of material from China and the region's other mature steel producing countries. Mills in this region have suffered from unsustainably high operating costs and a reliance on EAF steelmaking, which has imposed raw material limitations on steelmakers. This situation, however, is expected to change as a new large-scale BOF operation is being set up in Indonesia by Krakatau, and new capacity is also being planned in the region's other countries. Improvements in regional supply will come through as steelmakers from the mature markets of Japan, South Korea and Taiwan bid to introduce new business practices by establishing a foothold in the emerging markets to challenge Chinese dominance over Southeast Asian steel supply.

If it is achieved, such a shift of the production base to the end-markets will not only speed up the service to local buyers, but will also allow the regional mills to secure a market presence amid the intensifying protectionism seen in Southeast Asia in response to the surging supply of cheap steel products from China. Although prone to chronic overcapacity and seeing deteriorating margins on the looming indebtedness of the steel sector, China has dominated finished steel trade in the region.

SEA destinations account for 40% of the region's total shipments of steel exports. By way of comparison, intra-ASEAN finished steel trade stood at just above 5% in 2013.

Indonesia Steel Sales Up 6%

Steel sales in Indonesia rose 6 per cent to 15.1 million tonnes in 2014. Meanwhile, the global average steel price has been USD $536 per ton this year, implying that the market value of Indonesian steel sales is to reach USD $8 billion this year. In recent years, the country's steel sales have been rising on development of infrastructure, defense industry, and manufacturing. The sales are expected to continue rising in the years ahead due to commitment of the government to boost infrastructure development. Major bottlenecks are infrastructure for limited economic growth in SEA's largest economy. However, a master plan made by the government of Indonesia in 2011 is expected to give a fillip to country's steel sector. This masterplan is particularly focussed on infrastructure development. Three years after the introduction of the masterplan, success has been limited primarily due to the lack of funds. As the government has limited funds at its disposal it relies heavily on the private sector to finance projects within the MP3EI framework. However, private participation - particularly foreign participation - is still limited due to Indonesia's notorious bureaucracy, difficulty of land acquisition, and regulatory/legal uncertainties. Furthermore, infrastructure projects are not the most popular investment choice of the private sector as they usually involve high investments and a relatively long time before profits can be taken.

The government announced to slash energy subsidies and relocate available funds to infrastructure development (as well as social development). Currently, the lack of quality and quantity of infrastructure in Indonesia causes high logistics costs and low competitiveness of Indonesian businesses. Meanwhile, Irvan Kamal Hakim, President Director of Krakatau Steel, estimates that the domestic steel market expands by between 8 to 12 percent per year with the exception of this year amid slowing economic growth and the political uncertainties triggered by the country's legislative and presidential elections (which made some investors decide to postpone projects).

However, the domestic steel industry faces several challenges. The most important one is that domestic steel production capacity is limited. Indonesian steel demand was about 14 million tons in 2013, while domestic production capacity was only seven million tons per year. The deficit thus needs to be imported from abroad. This situation is reason why two major Japan-based steel producers, Mitsubishi Steel Manufacturing and Nippon Steel & Sumitomo Metal Corporation (NSSMC), invest a total of USD $450 million in Indonesia for the acquisition of Jatim Steel Manufacturing as well as for the establishment of a special steel factory in a joint venture with Indonesia's largest steelmaker Krakatau Steel.

Other challenges are the quality of domestically produced steel and the chronic global oversupply, primarily caused by China, the world's largest steel producer.

INDONESIA SALES VOLUME

YEAR	SALES (MILLION TONNES)
2014	15.1
2013	14.3
2012	12.5
2011	10.9
2010	8.9

Source : Mckinsey

Consumption growth in Thailand

Currently, Thailand demands about 18 million tonnes of steel each year. However, Thai producers supply only about 8 million tonnes, with the rest imported. Some steel users have chosen to use cheaper, lower-quality imports, prompting calls by the local steel-makers for government safeguards or anti-dumping duties. Thailand's steel consumption is expected to rise by 6.8% this year on downstream industry growth after a 3.5% decline in 2014, according to the latest figures from the Iron & Steel Institute of Thailand. Apparent steel use is projected to reach 18.53 million tonnes in 2015, up from last year's 17.33 million tonnes. Last year saw steelmakers in Thailand produce 6.8 million tonnes of steel products, down 4.6% year-on-year, while imports slid 2.9% to 11.9 million tonnes. Exports also fell 3.1% to 1.35 million tonnes. In the long steel segment, production of wire rod recorded a sharp 29.8% year-on-year decline to 430,454 tonnes. Imports of the product rose 17% to 1.65 million tonnes. As for flat steel, hot rolled plate output fell 22.1% to 240,586 tonnes, while imports climbed 3.7% to 261,007 tonnes. Hot rolled sheet output fell

3.2% to 2.6 million tonnes, while imports reached 4.2 million tonnes, down 10.3% from a year earlier. Japan remained Thailand's largest source of imports last year, at 5.09 million tonnes, up 3.9% year-on-year. China came in second, at 3.39 million tonnes (up 19%) while South Korea accounted for 1.47 million tonnes (down 6.3%) of imports. Construction accounted for the bulk of the country's steel demand last year, at 53.4%; followed by automotive, at 18.6%; machinery, shipbuilding and industrial, at 12.5%; appliances, at 11%; and packaging, at 4.5%. Thailand's steel demand per capita in 2014 was 268kg, compared with 274kg in 2013, the 1st figures showed. Some enterprises in Thailand called for the government to allow more imports of cheap steel, as different applications called for different types of this product.

However, the steel producers called for maintaining protectionist measures, as the use of imports by many enterprises was already keeping the steel-makers' production capacity at only 30 per cent of its potential. Thailand imposes duties on imported steel ranging from 7-27 per cent depending on type. Iron and Steel Institute of Thailand (ISIT) has predicted that domestic demand in 2015 will be up to 18.53 million tonnes, an increase of 6.8% from 2014. Steel demand in automotive and engineering industries will keep rising by around 15 per cent while the same from building, home appliance and machinery sectors may rise by 8.3%, 3% and 2% respectively. The country's consumption stood at 17.34 million tonnes in 2014, a decline of 3.5% from previous year.

Falling output in Malaysia

2014 saw Malaysia's steel producers experience falling output and revenues as a flood of cheap imports squeeze prices and margins. With much of this extra supply arriving in the form of cheap products from countries such as China, Indonesia and South Korea, local producers have found themselves hit by falling orders for hot rolled coils as well as other heavily imported steel products. The impact on local steel mills has been considerable with many firms forced to cut capacity in response to growing oversupply. Malaysia is estimated to have imported almost 1.83mnt of steel from China in 2013, including 924,000 tonnes of wire rods, equivalent to 80% of Malaysia's total import volume of the product.

Analysts observe that Malaysia's steel sector's near to medium outlook is still challenging, premised on the absence of anti-dumping trade action by the government. The research arm of Kenanga Investment Bank Bhd (Kenanga Research) in a recent report said, despite a decline in raw material prices which could boost steel players' margins, the local steel consumption is growing in tandem with the increase in imports from China. Without the implementation of trade action by the government, the research firm pointed out that steel consumption will be driven by the amount of cheap import from China, therefore hampering locally manufactured steel market share.

Local steel players may face earnings risks towards financial year 2015 (FY15) given the uncertainty of steel prices following the potential growing steel import activities in the local market. Of note, in January 2015, MITI announced that the anti-dumping probe found that the import of steel concrete reinforcing bars (rebar) from China and South Korea does not cause material injury to the domestic industry.

The local steel industry is still viable and competitive given the increasing demand in the apparent steel consumption (ASC), which has crossed the 10 million tonnes mark last year, said Malaysian Iron and Steel Industry Federation (MISIF) president Datuk Soh Thian Lai. The ASC is expected to grow by 4% per annum from 2014 to 2016, he said, adding that the projection is 10.5 million tonnes this year, 10.8 million tonnes in 2015 and 11 million tonnes in 2016 based on the baseline growth.

This was despite the industry facing significant risks such as increased dumping of cheaper imported steel, high costs and volatile prices of raw materials such as scrap and iron ore as well as the hikes in electricity and gas prices in recent years. Given the continued dumping of cheaper imported goods, crude steel production in Malaysia has dropped sharply while finished steel production was flat, totalling 4.7 million tonnes and 7.5 million tonnes respectively. The low facility utilisation with significant under-utilisation included bars and wire rods, sections, plates and flat rolled products. Contrary to the perception that the local steel outlook is quite bad and Malaysian steel millers are not competitive, he pointed out that Malaysia has the strategic location, good infrastructure, stable road transportation and utilities which are conducive to develop a strategic steel sector.

Growth to continue in Philippines

Philippine iron and steel industry is poised to continue its growth. In a presentation before the Organization for Economic Cooperation and Development in France earlier this month, the Philippines Board of Investments said that the demand for steel products would be driven largely by the implementation of big ticket government infrastructure projects, reconstruction efforts for the typhoon and earthquake affected areas and the housing backlog and redevelopment of urban centers across the country. The projects are expected to translate into increased local production of rebars, shapes and sections as well as increased importation of billets and coated steel products. Data provided by the bureau showed that apparent steel consumption grew by 9.2% to 6.58 million tonnes in 2013 from the 6.03 million tonnes recorded the previous year. The increase was attributed to the continuing growth in real estate developments and higher infrastructure spending by the government. Of the total demand for steel, 81% went to the construction industry; 9% were used for light and heavy fabrication; 5% for shipbuilding; 4 % for packaging; and the rest went to cover other requirements.

Crude steel production last year grew by 3.8% to 1.31 million tonnes while finished steel production rose 30% to 4.17 million tonnes. Finished steel imports and exports stood at 3.67 million tonnes and 100,000 MT, respectively. At present, the growth of the steel and iron industry is hampered largely by the high cost of power, technical smuggling, outdated facilities and tariff distortions concerning imported steel products.

The Philippine steel sector expects a 15-percent growth in 2015, on expectations of more construction activities. The Philippines steel industry is estimated at 6.7 million MT, with imported steel accounting for 3.67 million MT. Demand was expected to grow 5 percent to 7 percent in 2014, after rising 8 percent in 2013. Domestic production of billets and rebars grew 4 percent in 2013. Domestic demand for rebars reached 2.7 million metric tons in 2013, a figure that was expected to grow 6 percent to 7 percent annually, on strong demand from the construction sector.

Forty percent of the steel industry is comprised of flat products and 60 percent by long products. Flat products include slabs, hot-rolled coil, cold-rolled coil, coated steel products, tinplate and heavy plate used in automotive, heavy machinery, pipes and tubes, construction, packaging and appliances. Long products are mostly billets, blooms, rebars, wire rod, sections, rails, sheet piles and drawn wire which are used for construction, mechanical engineering, energy and automotive. Long products produced locally are pipes and tubes as well as some nails and wires from imported wire rods.

Strongest Growth in South Korea

South Korea is expected to see the strongest growth in steel demand among the wider region's developed nations, thanks to the rising take-up from the expanding shipbuilding and automotive sectors.