Chinese State-owned Steel Trader may Default in its Debts

Sinosteel, a major Chinese state-owned miner and steel trader, is poised to default on its bonds according to a letter sent to investors.

Citing a copy of the letter sent recently, Sinosteel told investors that, “The Company's business has stagnated and cash flow has dried up at headquarters and a portion of subsidiary enterprises”.

It stated that, “a subsidiary lacked the funds to repay principal and interest on 2 billion yuan ($315m) in bonds sold in 2010 scheduled to mature.”

According to the Sinosteel's website, the company is a central enterprise under the administration of the State-Owned-Asset Supervision and Administration Commission, and one of China's largest and most influential companies.

It states that it is active in the development, mining, and processing of metallurgical mineral resources, trading, research and logistics. It has a global sales network and logistics system.

The prospect of a bond default from one of China's 112 state-owned enterprises, coming at a time when concerns over the health of the Chinese economy are already

heightened, may test Beijing's resolve to allow market forces to play a greater influence in pricing market risk appropriately.

China's government will modernise state-owned enterprises (SOEs), enhance state assets management, promote mixed ownership and prevent the erosion of state assets.

The reforms will improve the competency of SOEs and turn them into fully independent market entities, stating that the government aims to have them fully implemented by 2020.

While the reforms, designed to make SOEs more robust, influential and have greater ability to avoid risks, aren't expected to be fully implemented, markets will be watching events carefully to determine whether or not the government will allow such a high profile firms to default upon its obligations. Based on recent form, it's debatable whether it will.

Recently state-owned heavy machinery producer China National Erzhong Group narrowly averted a default on its debt obligations when its parent company said it would buy outstanding bonds from investors.

Going further back, Chaori Solar, the first domestic-based Chinese firm to default on its debts in March last year, saw investors subsequently bailed out when Great Wall Asset Management, a state-owned bad-loan bank, stepped in to ensure a 90 million yuan interest payment was paid to investors.

Should China's government take a similar approach to Sinosteel's debt obligations tomorrow, it will once again bring into question the government's mandate of championing market-based reforms.

China Steel Output may Collapse 20% - Baosteel Chairman

China's steel industry, the largest in the world, is bleeding cash and every producer is feeling the pain, according to the head of the country's second-biggest mill by output, which raised the prospect that nationwide production may shrink 20 percent.

Losses for the industry totaled 18 billion yuan ($2.8 billion) in the first eight months of the year compared with a profit of 14 billion yuan in the same period a year earlier, Shanghai Baosteel Group Corp. Chairman Xu Lejiang said. Output may eventually contract by a fifth, matching the experience seen in the U.S. and elsewhere, he said.

After decades of expansion, China's steel industry has been thrown into reverse as local demand contracts for the first time in a generation amid slowing economic growth and a property downturn. The slowdown has pummeled steel and iron ore prices and prompted Chinese mills to seek increased overseas sales, boosting trade tensions. The country is the linchpin of the global industry, accounting for half of worldwide production.

“If we extrapolate the previous experience in Europe, the United States, Japan, their steel sectors have all gone through painful restructuring in the past, with steel output all contracting by about 20 percent,” Xu told at a forum in Shanghai. “China will eventually get there as well, regardless how long it takes.”

Crude-steel output in China surged more than 12-fold between 1990 and 2014, and the increase was emblematic of the country's emergence as Asia's largest economy. Output probably peaked last year at 823 million metric tons, according to the China Iron & Steel Association. The country produced 608.9 million tons in the first nine months, 2.1 percent less than the same period last year, the statistics bureau said.

“The whole steel sector is struggling and no one can be insulated,” Xu said. “The sector is facing increasing pressure on funding as banks have been tightening lending to the sector both loans and the financing provided for steel and raw material stockpiles.”

Losses in China's steel industry are unprecedented, Macquarie Group Ltd. said in a report that summarized deteriorating sentiment in the industry. While small mills have already cut production significantly, big mills are still holding out, the bank said, forecasting further cuts.