

10/12/1998

Need to create stronger local steel entities

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AS THE heat from the economic downturn slowly melts the steel industry, a pressing issue which has arisen is the long-term future of the sector, with some suggesting a bleak future if steps to create stronger steel producers are not implemented now, in the light of the impending market liberalisation.

There are too many negative factors surrounding the local steel industry now. A weaker ringgit has led to higher cost of production, the softening of the construction sector caused an oversupply and capacity and dumping of steel by foreign producers led to unfair competition.

Analysts argued that our steel industry was complacent once. In a cartel-like environment, local steel millers were enjoying the boom time.

A well-guarded local market effectively barred imported steel, and "foreign competition" were two alien words to steel millers.

Production were mainly concentrated on the construction sector, with bars and rods being the millers' favourite.

In a sluggish local market, exports became the next focus for some millers. In the international field, the local producers need to compete head-on with other major steel producers from Russia, Thailand and South Korea.

Nevertheless, local producers were at a disadvantage as the production cost of some foreign steel producers were lower, due to cheaper raw materials which are mined locally as well as cheaper sources of energy.

To further aggravate the problem, many steel millers undertook expansionary programmes, borrowings billions of ringgit, only now saddled with debts as returns on investments are not as projected.

So, what do local steel producers do now?

Suggestions from industry players and observers pointed out to strategic alliance, merger of the big names to create a stronger entity and lastly, allowing foreign companies to take up stakes in the steel companies.

Perwaja Steel Sdn Bhd chief executive officer Datuk Abu Talib Mohamed in a recent interview recommended strategic alliance, saying that Perwaja had thrown the idea to the other players "over coffee".

But the issue is how to make the idea work, he noted.

Tapping each other's strong points, rationalising the production of steel by each steel miller to ensure capacity and resources are fully optimised, are among the advantages of a strategic alliance.

Strategic alliance, he said, need not only be confined to local partners. Alliance with foreign parties will provide a ready platform in the international market, thus allowing easier market penetration.

A merger is another suggestion. A stronger entity will be created in a merger, allowing the streamlining of activities, thus increasing productivity, said an analyst.

Allowing foreign parties to take up a stake in a steel company, akin to the purchase of a 65 per cent stake in cement producer Kedah Cement Bhd by Blue Circle Industries Plc, a UK building material giant, is another suggestion.

Transfer of technology is just one of the benefits that may arise with the participation of foreign partners, though the acquisition of the stake itself may not be an easy process as a lot of issues need to be considered.

Undeniably, mergers or strategic alliances, too, are easier said than

done.

The banking sector is an example. Mergers are still at a slow pace despite an active role played by the Government via Bank Negara to promote mergers.

But the steel industry needs to take any kind of measure to heal the industry.

Despite the Government's effort to kick-start the economy with the RM5 billion infrastructure fund which is hoped to rejuvenate the steel industry, the industry needs to re-evaluate its performance.

Prime Minister Datuk Seri Dr Mahathir Mohamad has said it clearly.

"The pause that has been forced upon us should enable us to re-examine the industry. We must consider how we can become more efficient and cost-effective."

No doubt, the Government will do its best to help the industry. Encouraging the use of structural steel, for instance, is one of the calls that the Government has made.

Nevertheless, the steel industry, like the banking sector, does not have much time to waste.

Free market, through the Asean Free Trade Agreement and World Trade Organisation, is to be implemented by the year 2003 and 2005 respectively, and this will open the gate to steel at an extremely competitive price.

"Now the Government wants to re-start the construction sector but as far as the economy is concerned, tangible effects will only be felt when the funds are disbursed. This will take a much longer time than mere decision-making," said the Prime Minister.

Already there are vicious rumours in the market that certain steel millers, which have spent billions of ringgit on expansion programmes without anticipating the economic slowdown, will be closed down.

As painful as it may sound, unfortunately, this may be the case now. Steel producers need to act fast before they bleed further and be ready for any challenges that may arise in the next millennium.

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