EVALUATING CAPACITY UTILISATION AND FINANCIAL PERFORMANCE IN THE STEEL INDUSTRY:

A Comparative Study of SOEs and POEs

95th session of the Steel Committee
Paris, 26 March 2024

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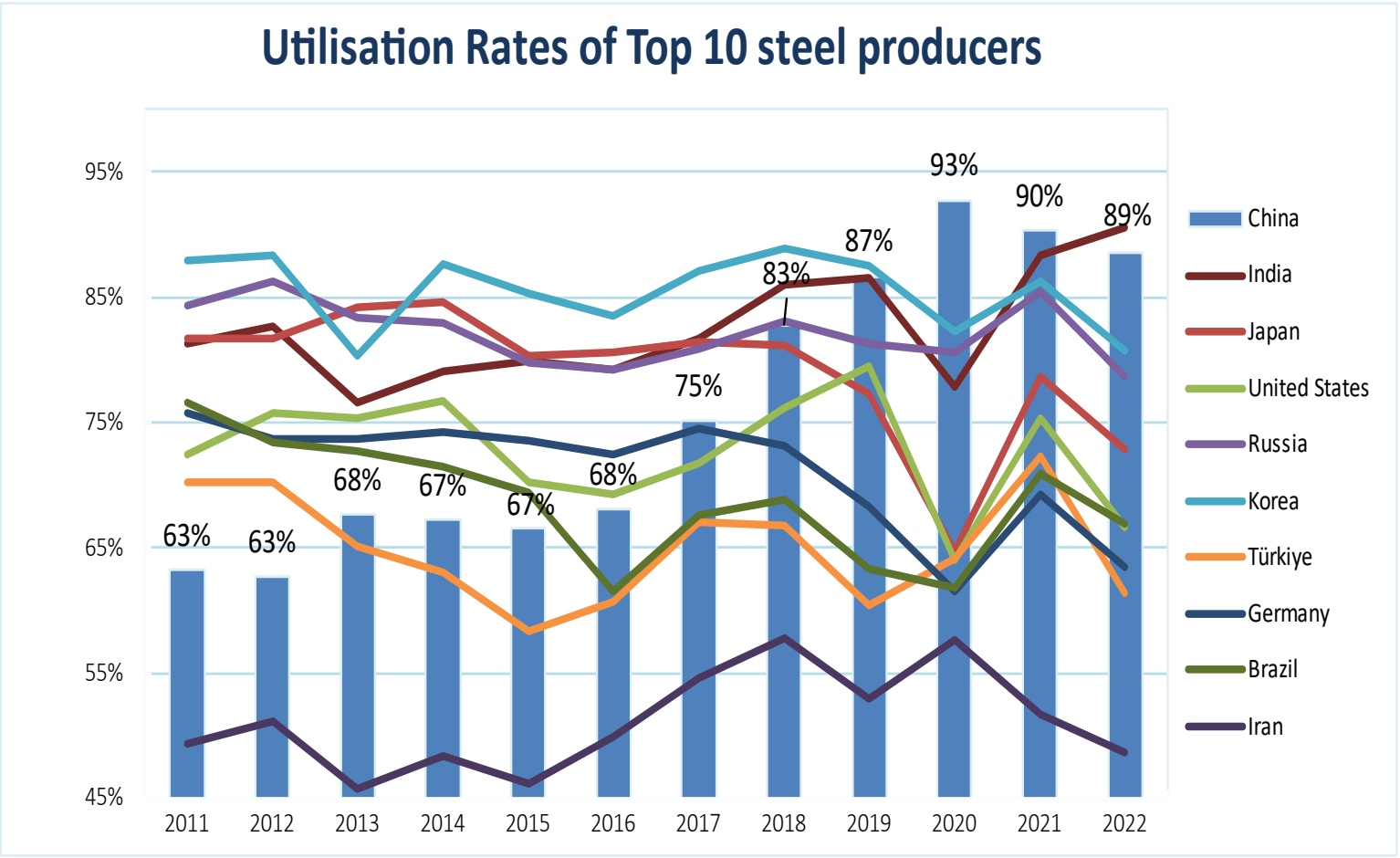
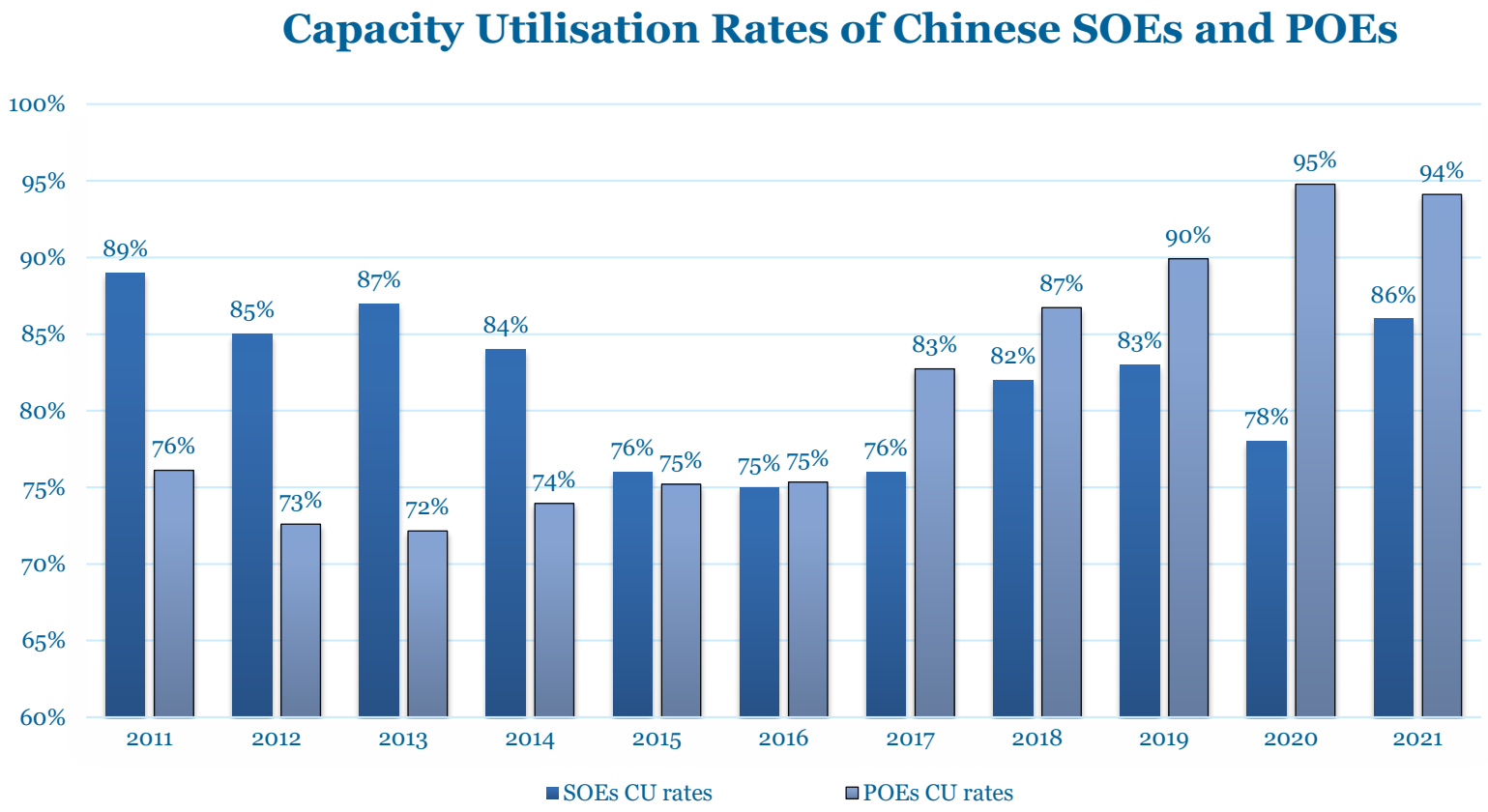
Capacity Utilisation rates: What insights does it provide?



- CU rates in the steel industry can reflect various economic and market conditions.
- The impact of the Covid-19 pandemic and the Russian aggression against Ukraine reflected in the CU rate.
- China CU rates hovered around 60% through the 2011-2015. Increased in 2016 due to government's supply side reforms aimed at addressing steel excess capacity and reached 89% in 2022.

Chinese SOEs can maintain or increase utilisation rates even in less favourable market conditions.



Between 2011 and 2014, Chinese SOEs displayed CU rates above 84%, a figure much higher compared to the country average of 63-67% during the same period.

Since 2014, there has been gradual convergence of utilisation rates between SOEs and POEs and in 2017 CU rate rise for SOEs signals initial steps in supply-side reforms to drive restructuring among leading steel "National Champions".

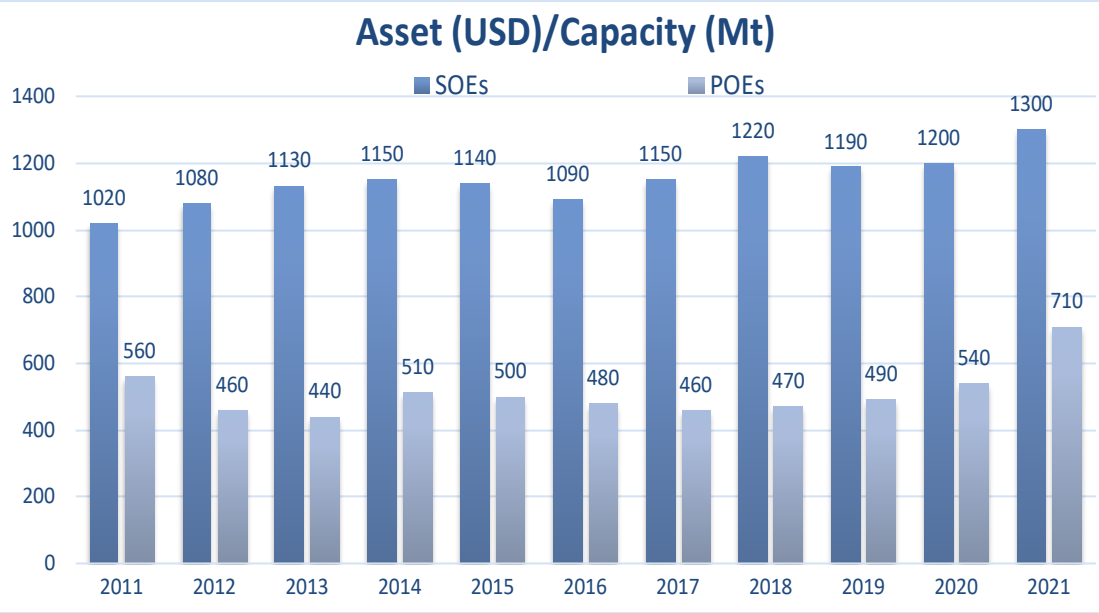
The decrease in capacity utilisation among SOEs in China's steel industry in 2020 can be attributed to the relocation of capacity to coastal areas of some firms in the sample

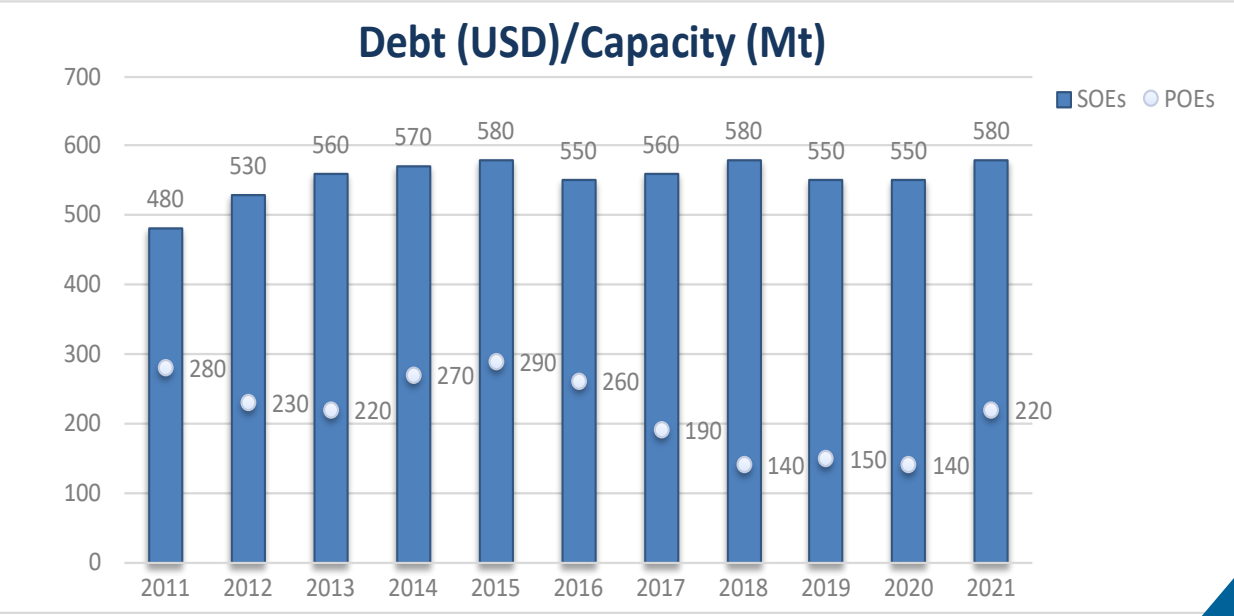
Note: SOEs in the sample represented 27% of China's total capacity in 2011 and 34% of China total's capacity in 2021 while the POEs in the sample represented around 10% of China's total capacity across the entire decade.

SOEs invest heavily in assets through increased debt levels

Over the past decade, SOEs have maintained a higher asset-to-capacity and debt-to-capacity ratio compared to POEs, with the gap widening over time

Despite the mid-2010s global steel downturn, SOEs persisted in asset investment, supported by policies aimed at creating "National Champions" that enabled them to expand assets and operate with higher debt levels without the immediate market pressures that POEs face.





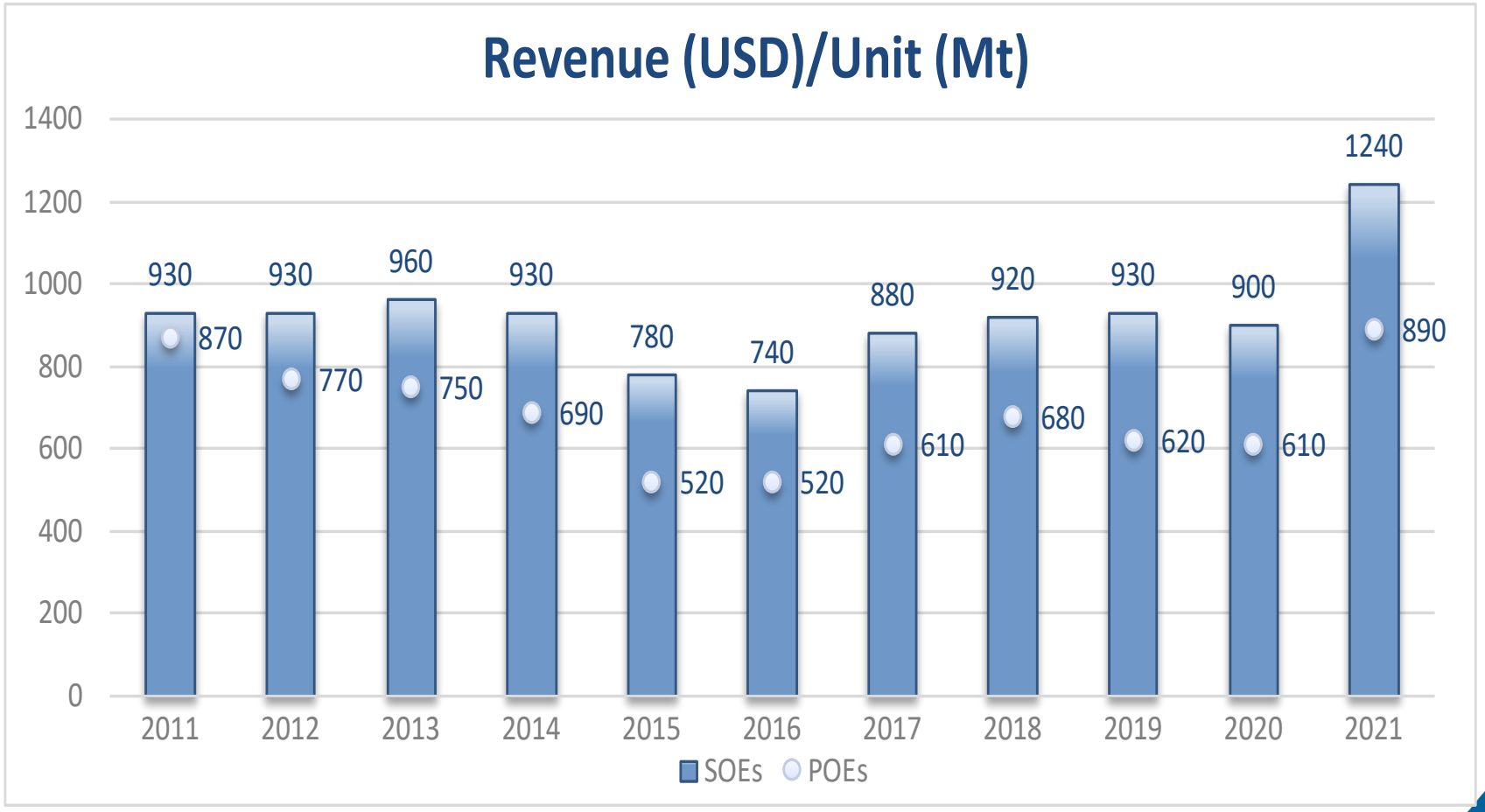
Note: Assets refer to all the resources owned by the steelmaking firms, encompassing inventory, accounts receivable, and long-term assets such as property, plant, equipment, patents, and other intangibles.

SOEs have higher revenue per unit of steel produced

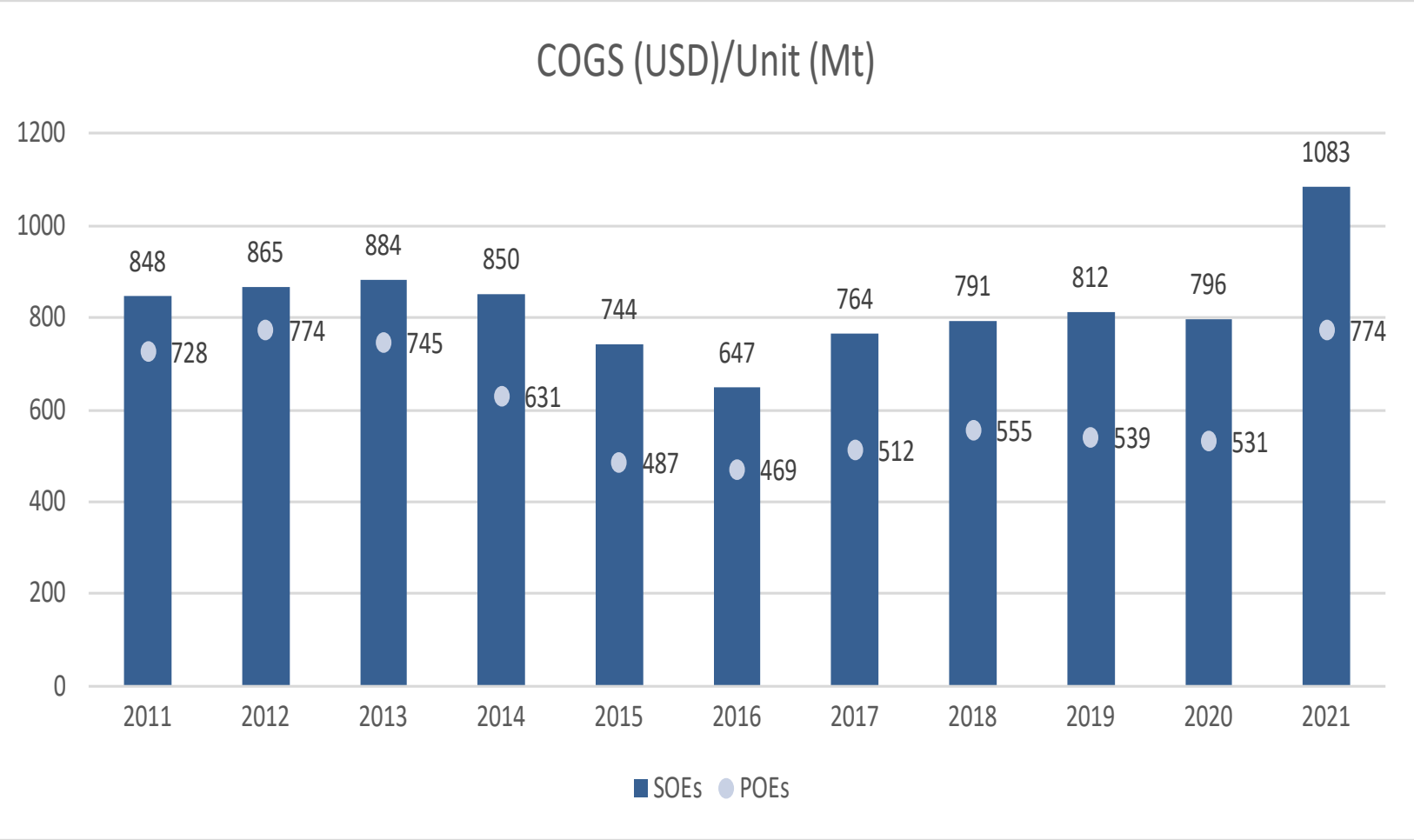
SOEs' revenue growth may result from a focus on higher-value products and state-backed consolidation since 2016, enabling market share expansion in premium segments.

POEs' lower revenue is likely due to market oversupply, competitive pressures, and a volume-over-value strategy, as indicated by rising CU rates since 2013.

To fully understand the underlying reasons for these differences in revenue performance, further research into these specific firms is necessary.



SOEs display higher costs per unit of production



POEs demonstrate lower production costs than SOEs.

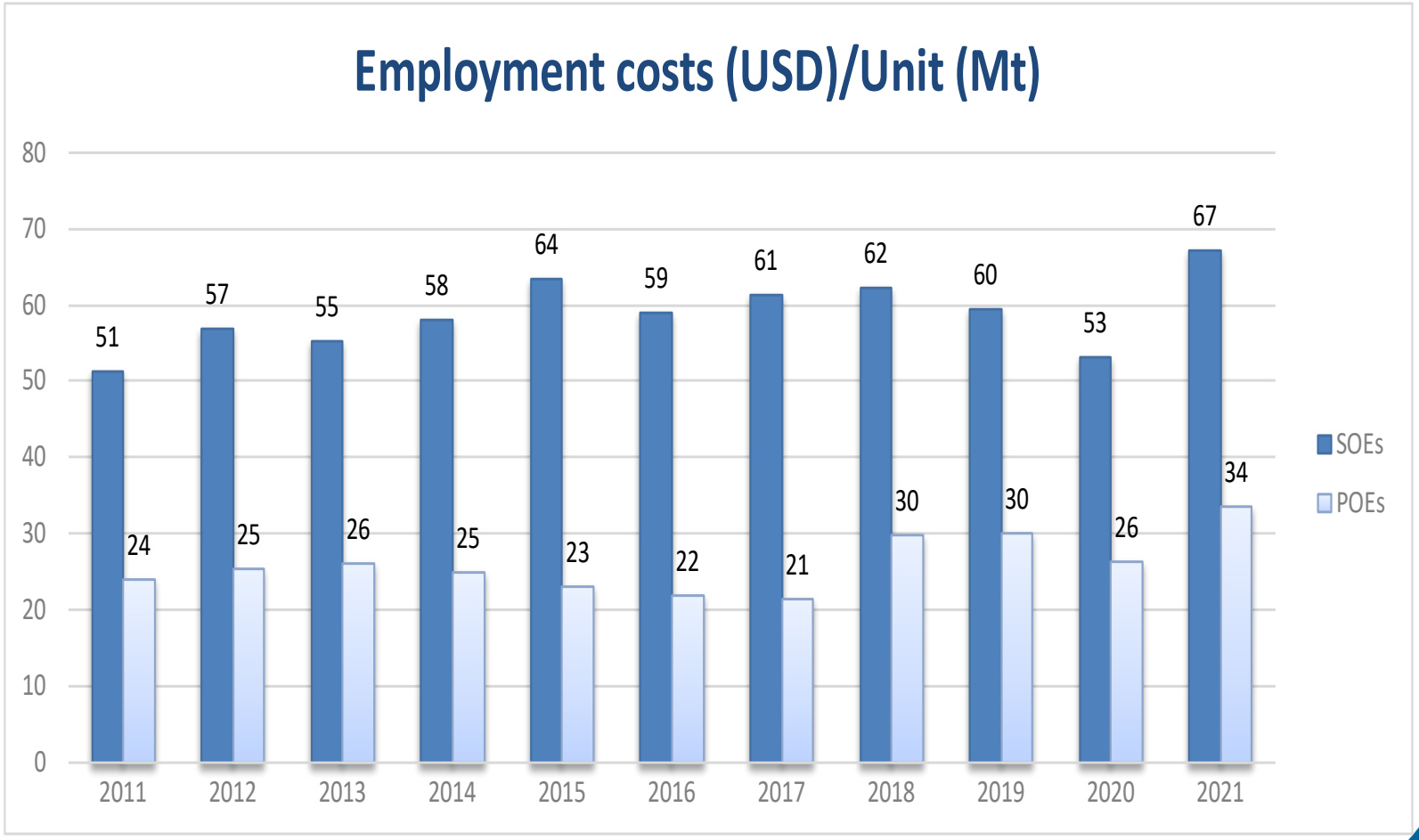
The differences in COGS per unit of steel production between SOEs and POEs highlight the government's support for SOE to align with state-driven policies of high-quality steel production and their social mandate.

In contrast, POEs, with their lower COGS, demonstrate a tactical response to market dynamics, focusing on cost efficiency to compete.

SOEs display higher labour costs

SOEs vs. POEs Labor Costs: SOEs have higher employment costs due to government-mandated wage structures and socio-economic responsibilities.

POEs maintain significantly lower salary expenditures, demonstrating tight labor cost management for competitiveness.



Conclusion

- **SOEs' Strategic Priorities**: SOEs prioritize social, political, and strategic goals, leading to larger operations and higher costs but potentially compromising economic efficiency.
- **POEs' Market-driven Efficiency**: POEs are more exposed to market changes. They focus more on maintaining leaner and efficient operations, enhancing their competitiveness.
- **Concerns with SOEs**: Activities of SOEs may lead to market distortions, including steel overcapacity and unfair competition, due to advantages in accessing credit, technology, and market expansion.
- **Need for Further Analysis**: While initial findings suggest policy practices have skewed the competitive landscape, further detailed studies are required to fully understand the government's impact on China's steel sector.