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High cost of production delays recovery of secondary steel companies

Synopsis
CARE reported that India's top six integrated steel producers (ISPs) together produced 5.9 mt of crude steel out of the total 9.2 mt in November, up 7.5% on year. By contrast, the output at smaller players fell 6%.

Integrated steel players said that the situation is likely to turn around in a couple of months.

MUMBAI: Steel prices are rising, but the responses of primary and secondary makers of the alloy to the defining price movements are markedly different. Big, integrated players have reported a quicker return to normalcy, but weaker financials, limited product range and higher costs have combined to delay the recovery for secondary **steel companies**.

"Most of the secondary steel plants are likely to be completely closed and it is a matter of time due to really high manufacturing cost. After the pandemic, the cost of production between an integrated steel plant and the secondary players has widened by around Rs 10,000 per tonne," said RK Goel, managing director of **Kalyani Steel** NSE -0.11 %, one of the top secondary steel companies in India.

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Secondary steel players continued to report on-year decline in production for the 19th consecutive month ended December.

India's steel making consists of two sectors; integrated primary steel players contributing nearly 55% and the secondary steel players comprising the remaining 45%. The ratio isn't the same as the industries clamber out of the pandemic-induced contraction.

"Limited scale of operations and weaker financial flexibility to cope with the multiple challenges thrown by the pandemic have further delayed their recovery. Consequently, the share of the six ISPs have gone up to 65% in November 2020 from 62% in November 2019," said the report by CARE ratings.

"For secondary steel makers, operating margin will test the lower range of 5.5-6.5%, marking a fall of nearly 100 basis points. This is largely due to the pandemic-driven shutdown in the first quarter of this fiscal, which led to a near-complete shutdown of operations for many producers," said Mohit Makhija, Director, **CRISIL** NSE 0.26 % Ratings.

What led to this?
During the peak lockdown period, primary steelmakers were able to catch up with the lost domestic demand through exports, which the secondary players could not due to limited reach and infrastructure.

A secondary steel player that owns a steel re-rolling mill in Chhattisgarh said that the rise in steel prices had very little impact on their profitability as the **iron ore price** too shot up at the same time.

"We had labour issues, logistics issues, liquidity crunch during Apr-Sep period. We slowly revived only to get hit by the sharp cost pressure," the person quoted above said.

The primary reason behind the adjustment of prices has been on account of the sharp rise in the main raw material cost which is iron ore and its overall shortage besides surging global steel prices. As per Industry body **Indian Steel Association** (ISA) rise in sponge iron prices are around 70% and pellets around 104% in the last 6 months.

"Bearing the brunt of the current situation are the smaller steel producers, who are faced with the double whammy of high input prices and non-availability of iron ore. As a result, they are unable to scale up production and stocks in smaller plants are less than 15 days of requirement," said Indian Steel Association in a letter to the Prime Minister's office last week.

Kalyani Steel's Goel added that the secondary steel manufacturers that cater to auto companies, could not increase prices to a great extent and long product players took a hike of around Rs 4,750 per tonne. However, integrated steel players increased it by around Rs 18,000 per tonne.

Light at the end of the tunnel?
Integrated steel players said that the situation is likely to turn around in a couple of months.

“I feel this is quite temporary, maybe today the secondary players are not able to get iron ore and they are also suffering due to lower working capital and liquidity and third, many secondary players do not have the manpower availability,” said SAIL’s ex-chairman, Anil Kumar Chaudhary.

Several secondary steel companies ET spoke to are seeking a ban on exports of iron ore and iron ore pellets in order to bring down their raw material costs.