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STEEL SECTOR CREDIT BULLETIN ISSUE 8

The voice of steel distribution

Our bulletin in October last year looked at what could have realistically been viewed as two separate economies. The second half of the year saw successive quarters of growth, upward revisions of growth forecasts and bullish figures being posted in relation to PMI indices and high levels of growth in both construction and manufacturing.

Whilst all of this positive news from analysts and investors provided us all with some much needed feel-good factor in the run up to the year end, it should be noted that the final GDP results for 2013 were not quite as good a first anticipated and despite a solid performance in the second half of the year this was offset by a poor first half year which at the time showed all of the signs of a triple dip recession.

Overall the UK Economy grew by 1.7% last year. This was less than the previous estimate of 1.8 % and is the second revision from the initial estimate of 1.9%. Whilst the UK economy posted growth figures of 0.8% for the final quarter of 2013 it still remains 1.4% below its downturn peak at the beginning of 2008.

Whilst there has been some rebalancing of statistics for 2013 it should not be ignored that the second half of the year did show a significant improvement in both economic performance and consumer confidence and this momentum has continued into the first quarter of 2014.

In relation to current sector performance, manufacturing indices have shown a slight slowing in pace. This is seen by analysts as more of a stabilising effect than a downturn and further growth in the sector and job creation are forecast for 2014.

Confidence in the UK's construction market continued to gather pace in the three months to March 2014. House building remains the driving force behind the growth in the sector with resurgent demand for development programmes and supported funding conditions being at the core of its activities. This remains very encouraging albeit there are some concerns emerging over possible limitations of supply in relation to materials and labour.

Whilst sentiment and confidence have been short on supply in the Steel Industry over recent times, there appears to be genuine optimism that the increase in confidence in these two key sectors will enable our industry to experience some tangible signs of recovery. Steel consumption within the construction sector is expected to rise to circa 1m tonnes during 2014 with usage within manufacturing also remaining buoyant.

The signs for the first quarter are encouraging but challenges remain within the Steel Sector. Over recent times stockholders have been squeezed by low margins and low demand and whilst there is some considerable way to go it is encouraging to see demand and confidence returning.

Mark Powell
Executive Director
AON Risk Solutions

AON

atradius

managing risk, enabling trade

2012 and 2013 proved turbulent for the industry

European volatility, the slowing of the Chinese market, and an overall decrease in global demand have all resulted in excess capacity and problematic market conditions, as evidenced in the significant full year losses posted by certain producers.

Closer to home, the UK market faced the ongoing contraction of the construction sector. Though offset in part by demand from automotive and engineering – both of which grew in this period - on a macro-economic basis, exchange rate volatility, high energy costs, competition and ongoing austerity measures have combined to create precarious market conditions.

This has compromised revenue, margins, profitability and cash flow for many of the buyers in this sector. Consequently, in a bid to mitigate the risk to liquidity, we saw inventories being unwound, non-core assets being disposed, cost cutting programmes and vigilant cost management strategies being implemented.

At the same time, considered capital investment to enhance operational efficiencies, USP and business retention also remained strategically imperative.

The year saw several key insolvencies, including Metalrax and Rowecord with smaller companies Penistone Reinforcements, Hi Tech Steel and McKechnie Brass failing later in the year. In early 2014, we have already seen the demise of Redirack and Coupe Foundry, underpinning our view that the steel and metals market will remain both fragile and volatile for some time yet. Eurozone austerity and the slowdown in Chinese growth are constant pressure points, alongside high raw material and energy costs.

The sector also remains exposed to the volatility of high risk industries such as construction which, against a backdrop of uneven global financial recovery, means that the global steel and metals industry continues to be characterised by overcapacity - as articulated in recent downsizing announcements by Thyssenkrupp and ArcelorMittal. This is compounded by low cost competition from Asia, bringing extra volatility to the commodity markets, negatively impacting the UK business climate.

But it isn't all doom and gloom. There is optimism that we will see sector improvement later in 2014, as the wider economy shows strong signs of recovery, particularly in construction and automotive, and to a limited extent, housebuilding.

As in most sectors, access to liquid finance will be key for business growth and development, particularly for the service centres, so that they can re-stock in order to meet the anticipated rise in demand and capitalise on further opportunities.

Mary Ravenscroft
Manager Birmingham Regional Office Commercial UK
Atradius

GRAYDON
open in business

"Steady as she goes"

The heading as you know is a Naval term, and certainly the recession of the last few years has been a very stormy one but, dare I say it, the waters are a little less choppy than previously; however we are still a long way from a mill pond scenario. Coming out of recession brings with it as many problems as entering one. Tradition says so and I fear it will be no different this time and insolvencies will increase.

The opposite of recession is growth - growth needs to be funded and, in most cases, from an external source, i.e. banks or other third party lenders, or even a combination of both. I doubt this lending will be in the form of overdrafts which are fast becoming a thing of the past. It's all about asset based lending these days, if you can get access to borrowing in the first place. As I have alluded to before, alternative lenders do prove to be expensive, and often very expensive. The 0.5% Bank of England lending rate is based on lending to banks and not what you will get from normal lending sources for your own requirements. A lack of financial support will hinder growth for companies and businesses trying to expand into the better trading conditions which we all hope will be arriving sooner rather than later.

The Government is quick to point out good economic data in whatever format it comes but statistics can be misleading. To give you an example, we are hearing good news on construction at long last but this is being led by the house building sector and not commercial construction. How much steel goes into a 3 bed-semi? Hardly anything. Only recently, the Purchasing Managers Index (PMI) revealed good growth figures in construction, and these were backed up by our colleagues at Euler Hermes who also revealed positive figures on claims in construction - these figures are accurate but I would again reiterate that this is a generalisation and I would separate commercial from social housing; two very different animals. Government spending is key to the commercial sector taking off. Let me remind all of you, public sector spending accounts for a third of commercial construction and I don't see the Government loosening the public purse strings just yet.

Don't get me wrong, there are some really positive aspects to the economy which are and will support the Steel sectors. Energy is a buoyant area, as is the Automotive trade which was backed up recently by some very positive production and profit figures from "JLR", boosted by excellent sales particularly in China and North America.

Market conditions remain stable and this was emphasised recently at a steel credit circle jointly hosted by Graydon and the P&A Partnership where, in most cases, attendees including many NASS members, reported that sales were either steady or a little higher than this time last year. There do remain serious issues though with slow payments as buyers struggle with cash flow. Again I reiterate, borrowing, and by that I mean affordable borrowing, is still difficult to come by and, as a result, you, the seller, are effectively providing additional liquidity through a slowness in paying accounts.

Banks have generally received only a finger wagging from the Government and are therefore a law unto themselves when it comes to helping industry through and out the other side of a recession.

I'm not in danger of repeating myself - I am repeating myself, but there is a serious danger that complacency will set in as more good news appears from various sources and gathers pace, and it's a fear that this will lead to a relaxing of selling arrangements. If a business looks bad and pays bad, then it is bad. If a business says it is doing better, then let them prove it, and back it up by providing evidence that they have turned the corner. By this I mean obtaining post filed trading figures from either management or draft accounts. It's all about knowing what your customer or potential customer is doing now, not where it has been and what it did previously.

By the same token, know that the subject company who looked good continues to look good, and by the same methods as previously mentioned. It's about the NOW position of any business. Getting the latest financial figures should also become an on-going habit, even after we have come out of the recession, as this may give you an insight if bad news is coming. Be the first to know.

Also, get to know your customer's customer. Their bad news could end up also being bad news for you and how you get paid. Join a reputable credit circle such as the one run by Graydon/P&A - it will serve you well and will give you a greater insight into market trends, troublesome businesses and possible company failures, thereby giving you the opportunity to hopefully get out before any ultimate failure. It will also help in the battle against fraud which is on the increase, albeit from a very small standpoint. Recently one of our Steel members was just a whisker away from releasing goods to the value of £20,000 and also getting stung for a further £60,000 in cash.

The message remains the same: stay vigilant and utilise every avenue to know your customer/potential customer. Knowledge is still king and will remain so.

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The voice of steel distribution

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