OECD STEEL COMMITTEE
Developments In World Steelmaking Capacity

Russia: Steel Market Developments

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Recent Economic Developments in Russia

- Russian economic growth started to lose momentum since H2 2012 due to global market weakness and slowdown in domestic demand
- Industrial production is almost flat in H1 2013 with freight rail transportation volumes falling y-o-y
- Economic growth projections for 2013 are reduced

Sources: Metal-Expert, Metal Courier, Russian Statistics Agency
Growing Costs as a Cause for Concern

- Prices for domestic energy resources are growing faster than consumer prices index (CPI)
- Russian inflation is far exceeding the ones at mature economies
- Industrial sector profits suffers from increasing utilities and labor costs

Sources: Rosstat
• Domestic energy costs grew significantly over the last decade reaching and in some extent exceeding the level of developed markets
  • Prices for gas are equal to the level of USA
  • Electricity cost is close to that in the EU
• Global steel prices are falling largely due to overproduction and lack of supply discipline
• Russian domestic prices largely replicate the international market situation
• There is growing pressure from steel imports
  • long products import increased 39% in 2011 and 26% 2012

**Sources:**
Steel consumption in Q2 2013 is predicted to grow about 9% over Q1 2013

However, Q2/Q1 traditionally shows strong growth in Russia (due to severe winter)

Q-on-q growth (Q2 2013 over Q2 2012) is only 2,8%

Steel use for the whole of 2013 is expected to rise only 2,5% y-o-y
Steel Consumption in Russia

Steel Consumption Breakdown by Sector, mmt 2012

- Russia’s steel consumption structure remains traditional, with construction, pipes & tubes, metalware and machinery as its most important sectors.
- These sectors varied in performance over the last 5 years, some growing moderately and some stagnating.
- Automotive and home appliances are two promising sectors, though still small in absolute numbers.

<table>
<thead>
<tr>
<th>Sector</th>
<th>CAGR 08-12</th>
</tr>
</thead>
<tbody>
<tr>
<td>Automotive</td>
<td>-6%</td>
</tr>
<tr>
<td>Home appliances</td>
<td>8%</td>
</tr>
<tr>
<td>Machinery</td>
<td>0%</td>
</tr>
<tr>
<td>Metalware</td>
<td>-3%</td>
</tr>
<tr>
<td>Construction</td>
<td>2%</td>
</tr>
<tr>
<td>Pipes &amp; tubes</td>
<td>2%</td>
</tr>
<tr>
<td>Others</td>
<td>2%</td>
</tr>
</tbody>
</table>

Sources: Metal-Expert, Metal Courier, Russian Statistics Agency, Ministry of Industry and Trade; NLMK research
Russia’ Steel Consuming Sectors Output Dynamics

Transport Machinery Production Index, y-o-y, %

Pipes & Tubes Production Index, y-o-y, %

Mechanical Engineering Production Index, y-o-y, %

Automotive Industry Production Index, y-o-y, %

Sources: Russian Statistics Agency
Steel demand will continue to growth in long term supported by strong fundamentals

- Russia has delayed steel demand of almost 170 mt due to economic slump in 1990s
- Russian infrastructure is highly underinvested

Steel demand have been recovering strongly in 2002-2007 and in 2009-2012

Sources: McKinsey, NLMK
Steel Demand Fundamentals

**Floor space per capita**

- USA
- Southern Europe
- Central and Northern Europe
- China
- Eastern Europe
- Russia

**Automobiles per 1000 people**

- USA
- Canada
- Germany
- Czech Republic
- Poland
- Bulgaria
- Hungary
- Russia
- Romania

- Construction sector is seriously underinvested
  - Floor space per capita is lower than in developed economies
  - 82% of housing was built more than 17 years ago
  - Commercial construction is actively developing
- Car ownership per 1000 people is 3 times less than in USA

Source:
Steel Consumption Forecast

Flat Product Consumption Forecast, mmt

Long Product Consumption Forecast, mmt

Coated Products Consumption Forecast, mmt

Pipes & Tubes Consumption Forecast, mmt

Sources: Metal Courier
Steel Consuming Sectors Output Forecast

Industry Production Forecast, y-o-y, %

Steel Industry Production Index Forecast, y-o-y

Energy Machinery Production Index Forecast, y-o-y, %

Machinery Production Index Forecast, y-o-y, %

Source: Ministry of Economic Development
Russia’s steelmakers have been actively investing into the modernization of the assets

- ab. $8 billions of investments per year in 2005-2012
- Steelmaking capacities have been restructured in favor of more efficient and less environmentally harmful way of production
  - A number of OHF capacities has been closed down in 2008-2013 with some replaced by new EAF and BOF capacities, some simply taken out of the market
  - Share of OHF in steel production is targeted at 0% by 2015

Source: Rosstat, Worldsteel Association
• Modernization results in better environmental and efficiency industry performance
  • Air pollution has been reduced by 12% although steel production increased 6.5%
  • Energy efficiency is reaching best available technology level

Sources:
Environmental Legislation

Law about BAT
(to be passed before 2014)

Upgrade to Best Available Tech

• Huge investment costs
• BAT not as a reference for setting the permit conditions, but as a universal direct limit
• Pollution tax payable even after achieving BAT
• Only 8 years to complete the transition which the EU hasn’t fully managed in 16 years

OR face crippling penalties

• Non-complying companies will end up paying $x100 in environmental charges

• Russian producers face pollution-related costs similar to or worse than those of their international counterparts
• This places Russian steel industry on an equal footing with OECD countries
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THANK YOU

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