



# Laying the foundations for a financially sound industry

Steel Committee meeting  
Paris, December 5<sup>th</sup>, 2013

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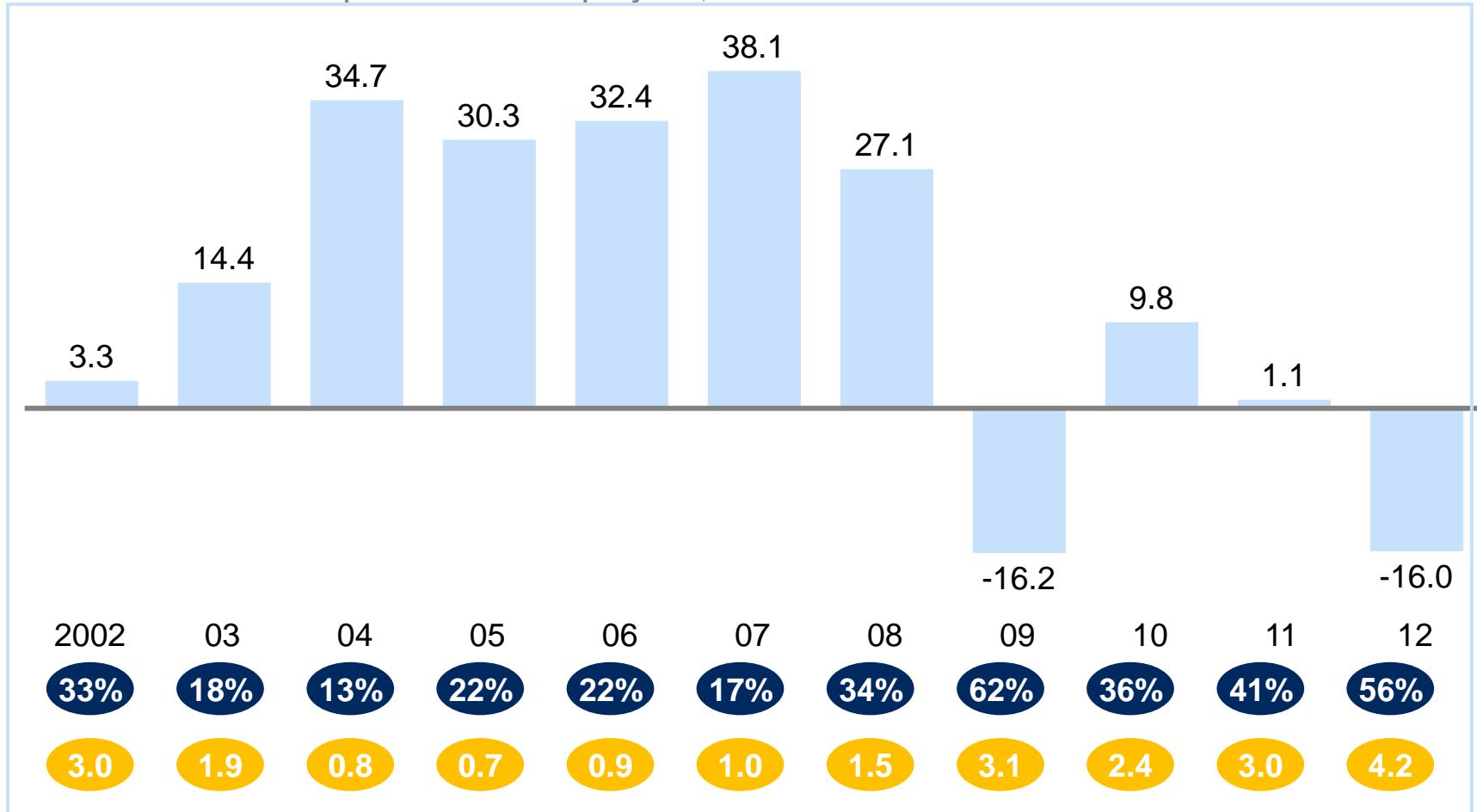
## Contents

- **The global steel industry is not financially sustainable**
- The outlook remains challenging
- Long term financial health might be elusive without significant restructuring

# A large portion of the steel industry has operated with negative cash flows even in benign conditions

● Average net debt to EBITDA ratio    
 ● % players with negative cash flow

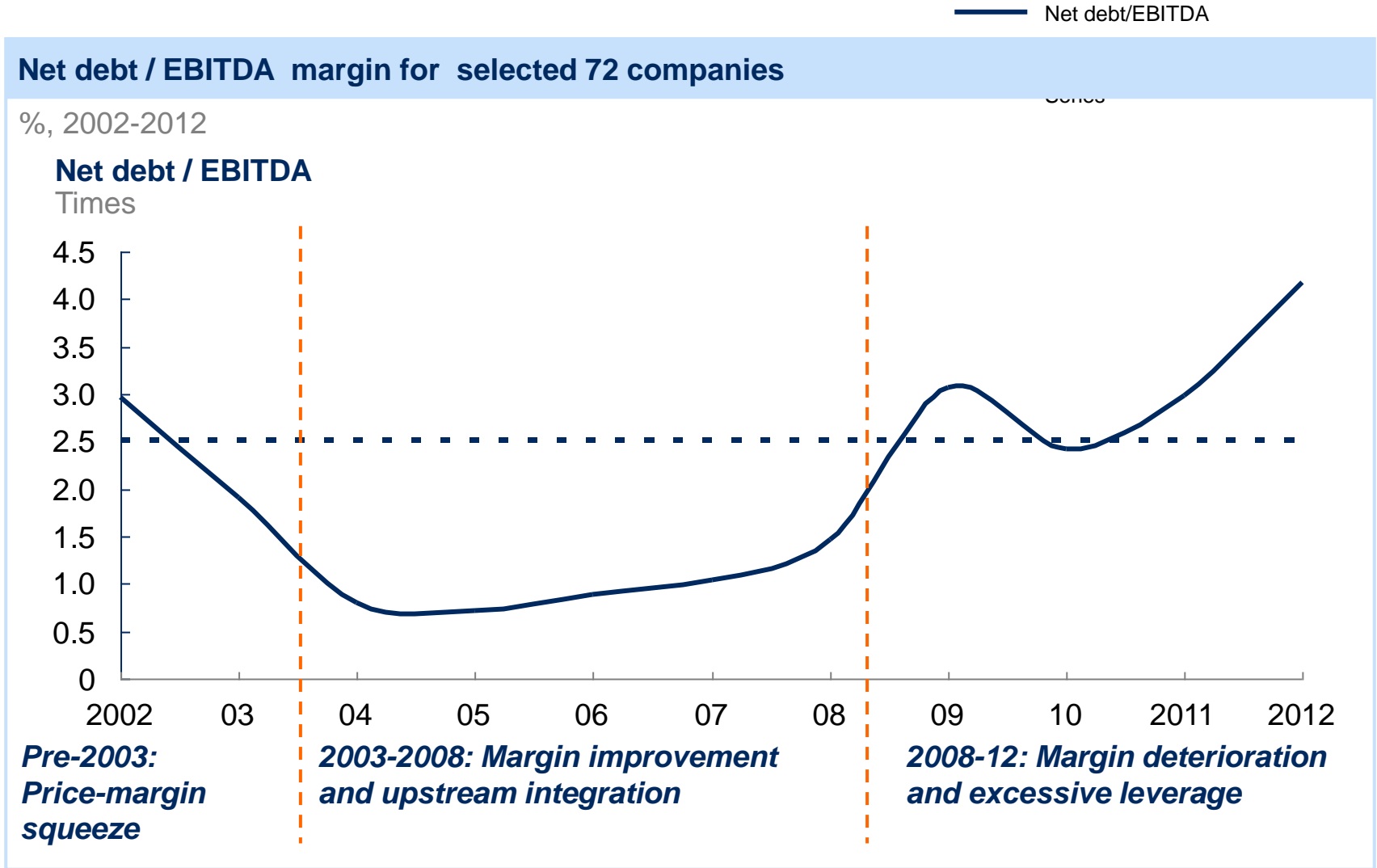
Cash flow<sup>1</sup> for sample of 72 steel players, USD billion



<sup>1</sup> Total operating cash flow minus capital expenditures minus interest expenses

SOURCE: S&P Capital IQ

# The leverage level of the steel industry is increasing

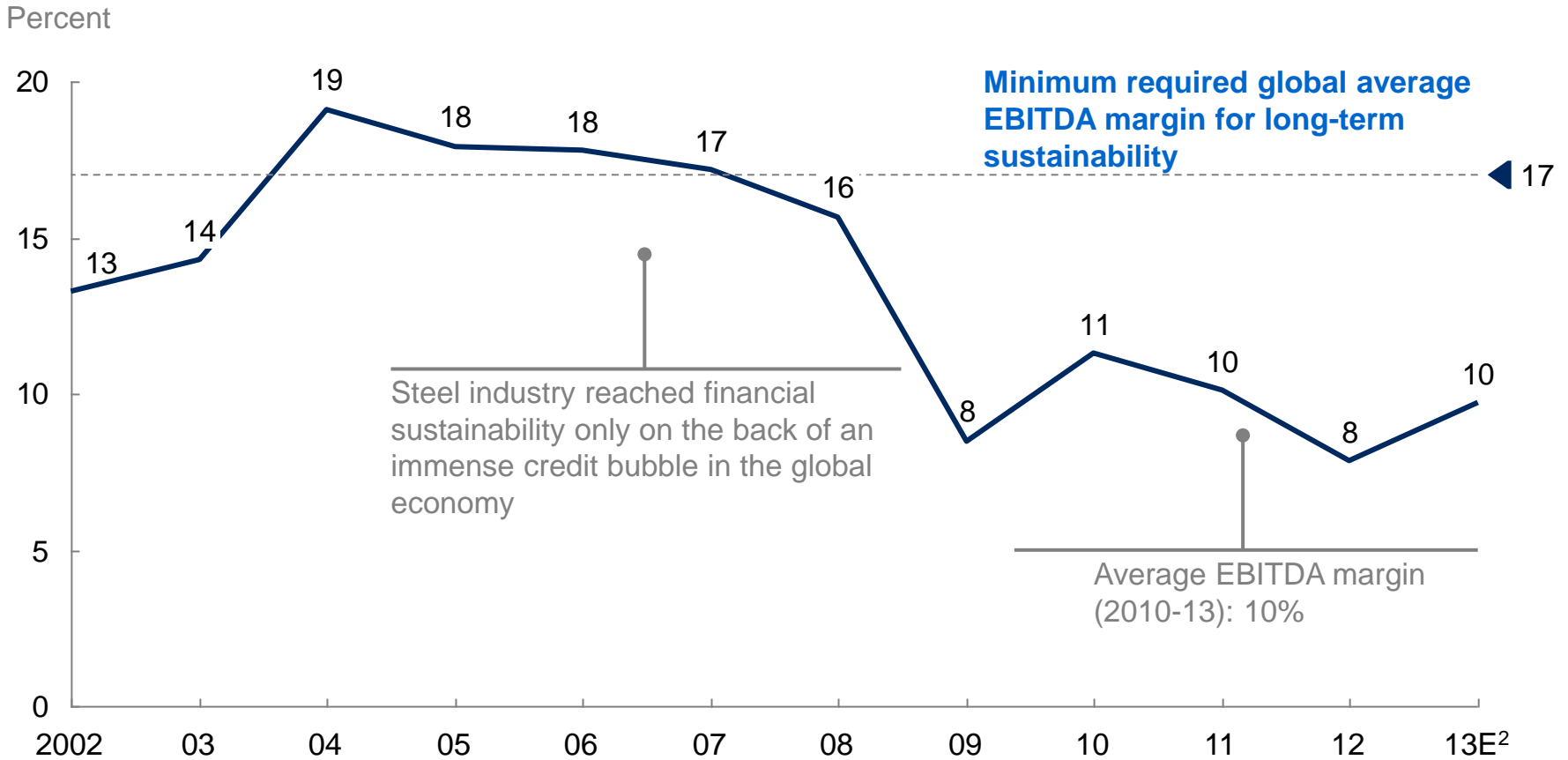


SOURCE: S&P Capital IQ

# EBITDA margins have deteriorated

PRELIMINARY

## Average EBITDA margin in the steel industry<sup>1</sup>



<sup>1</sup> Considering sample of 65 companies

<sup>2</sup> Consensus forecast

# EBITDA must cover all stakeholder obligations

PRELIMINARY

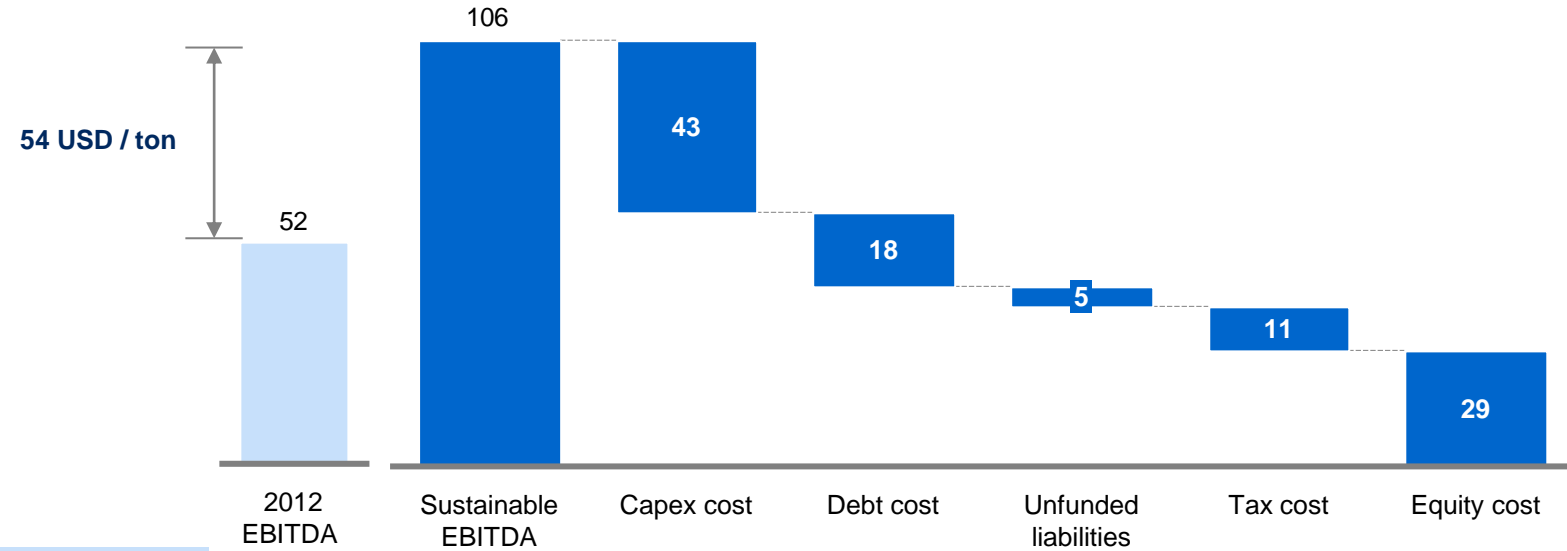
		Measurement used
EBITDA must cover all stakeholder costs	Net earnings (after stakeholders costs)	
	Investment / reinvestment into the business	<ul style="list-style-type: none"> <li>CAPEX (during period of low investment, i.e. mostly maintenance CAPEX occurring)</li> </ul>
	Interest payment to debt holder	<ul style="list-style-type: none"> <li>Average cost of debt</li> </ul>
	Tax to government	<ul style="list-style-type: none"> <li>Effective tax rate</li> </ul>
	Unfunded liabilities (e.g., pension funds, ...)	<ul style="list-style-type: none"> <li>Unfunded liabilities, gap to be closed in medium term</li> </ul>
	Return to shareholders	<ul style="list-style-type: none"> <li>Average cost of equity</li> </ul>

# Meeting current stakeholder obligations requires a 17% global average EBITDA margin

## Required EBITDA for long term sustainability (global average)<sup>1</sup>

USD / ton, Hot rolled 2012

GLOBAL AVERAGE



The global steel industry must generate additional **USD 76 Bn** at current production level to become sustainable

Percent of turnover <sup>2</sup>	2012 EBITDA	Sustainable EBITDA	Capex cost	Debt cost	Unfunded liabilities	Tax cost	Equity cost
	8%	17%	7%	3%	0.5%	2%	4.5%

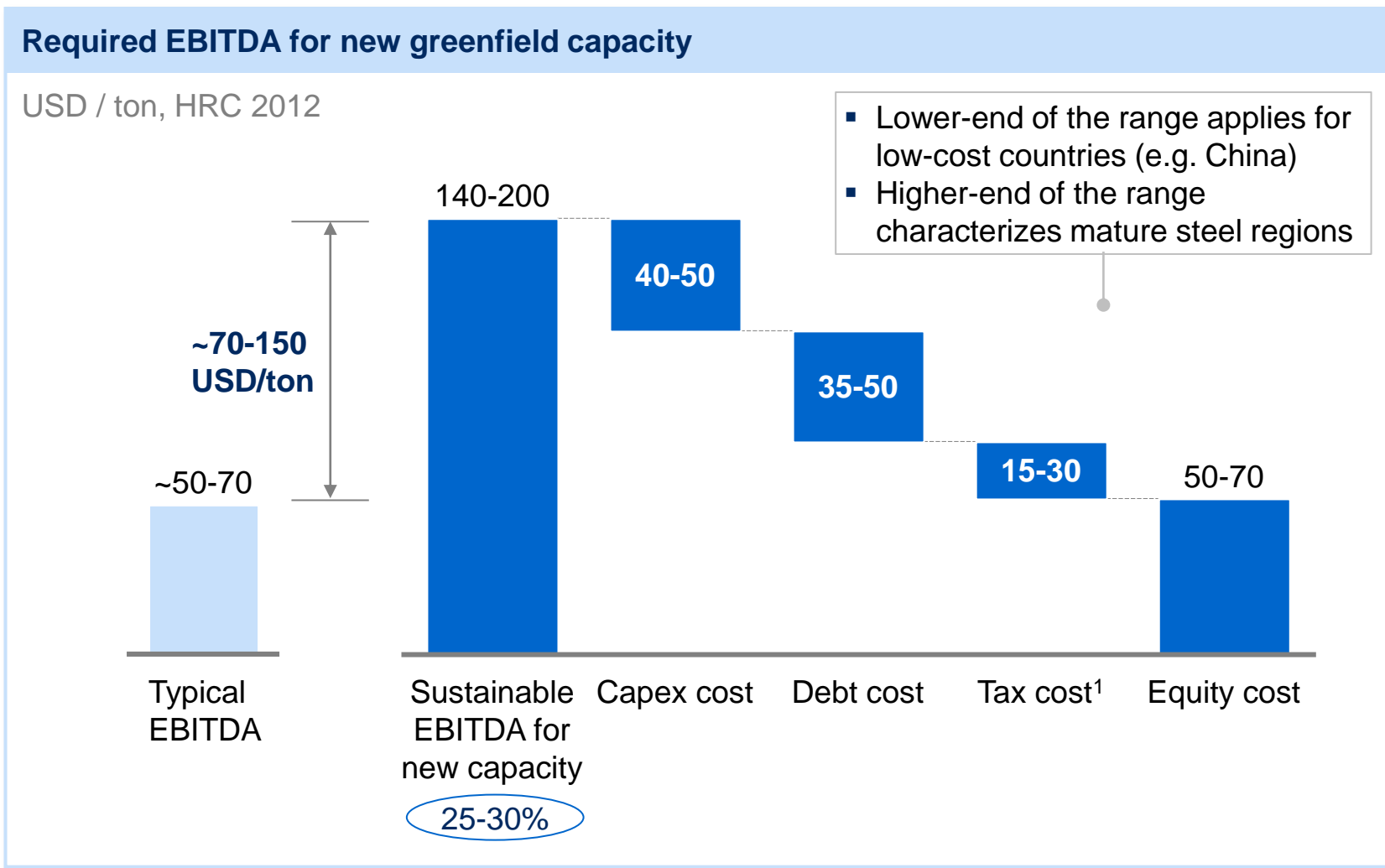
Assumptions <sup>1</sup>	Capex cost	Debt cost	Unfunded liabilities	Tax cost	Equity cost
	▪ Capex ~7% of revenues	▪ 7% cost of debt ▪ ~250 USD/ton of debt	▪ Average unfunded liabilities (gap to be closed in medium term)	▪ 25% effective tax rate	▪ 9% cost of equity ▪ ~325 USD/ton of equity

1 Considering sample of 83 companies  
2 Assumes a price of 634 USD/ton in 2012 for hot rolled



# For any greenfield capacity expansion, the sustainable EBITDA margin is even higher

xx EBITDA margin

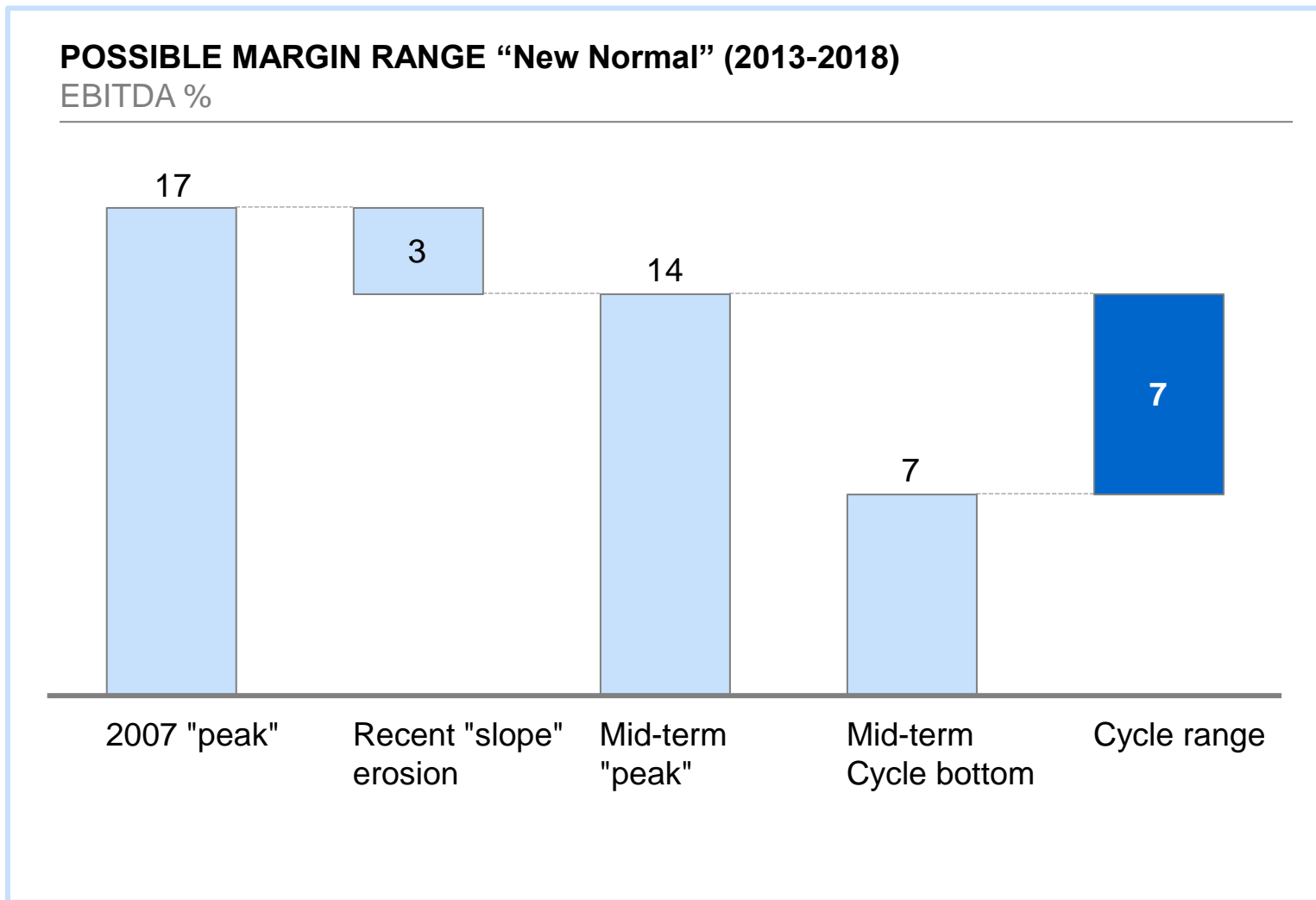


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# EBITDA margin range expected to be lower than in the past

ROUNDED NUMBERS



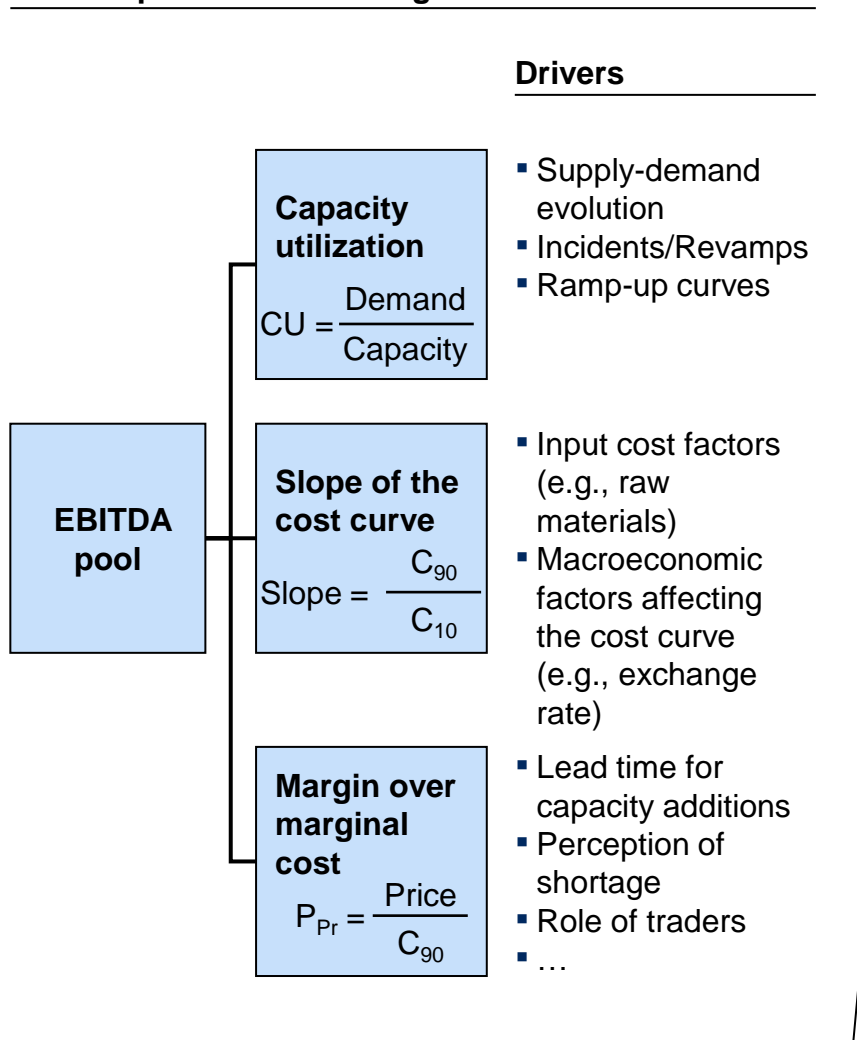
1 Overcapacity defined as (crude steel capacity) - (crude steel equivalent of finished steel apparent steel demand)

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# The size of the EBITDA pool in any industry is driven by 3 factors

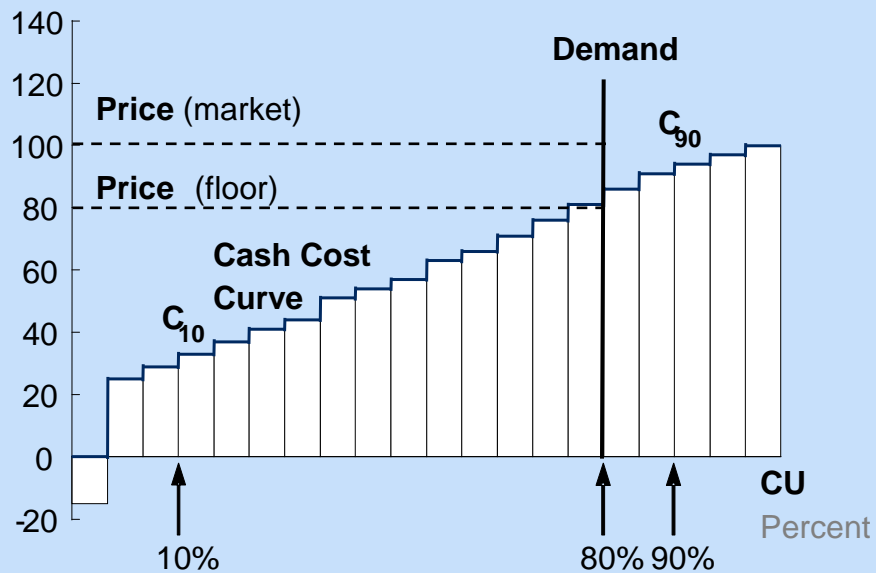
## EBITDA pool simulation logic



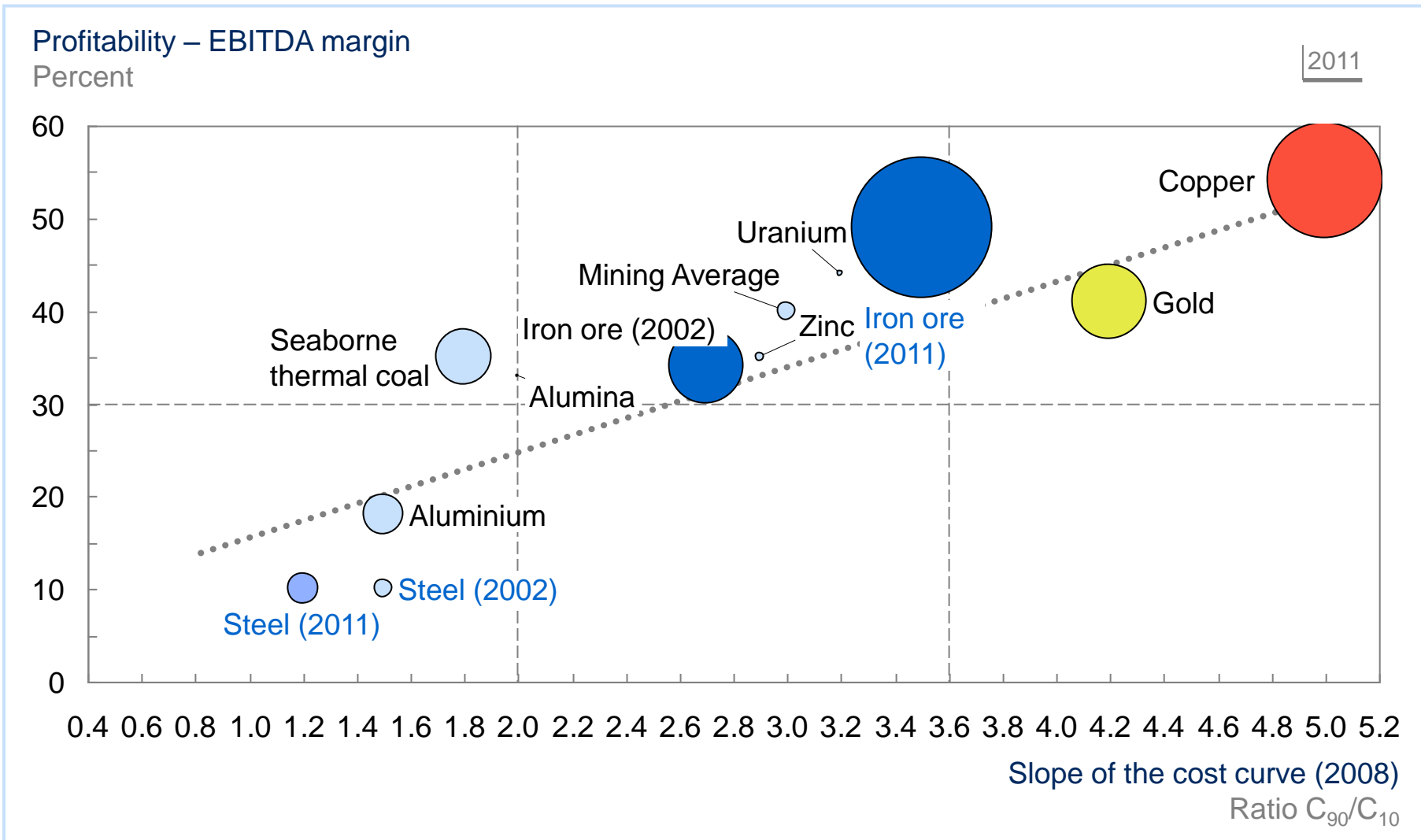
## EBITDA pool simulation

$$EBITDA_{\%} = CU - \frac{(1+1/\text{Slope}) \times (1+CU)}{4 \times P_{Pr}}$$

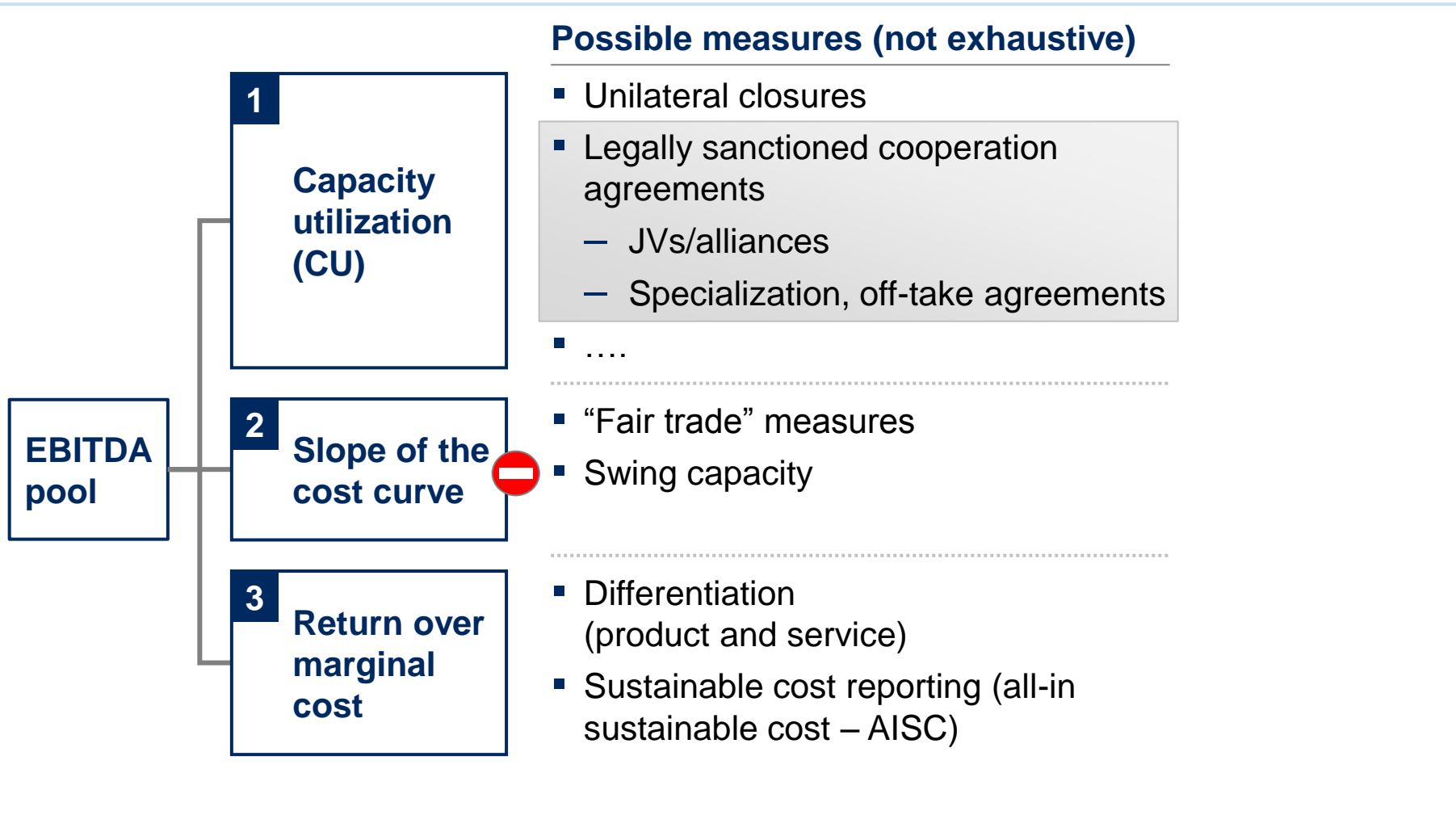
### C1 Cash Cost



# The average commodity attractiveness is “structurally” underpinned by the slope of its cost curve



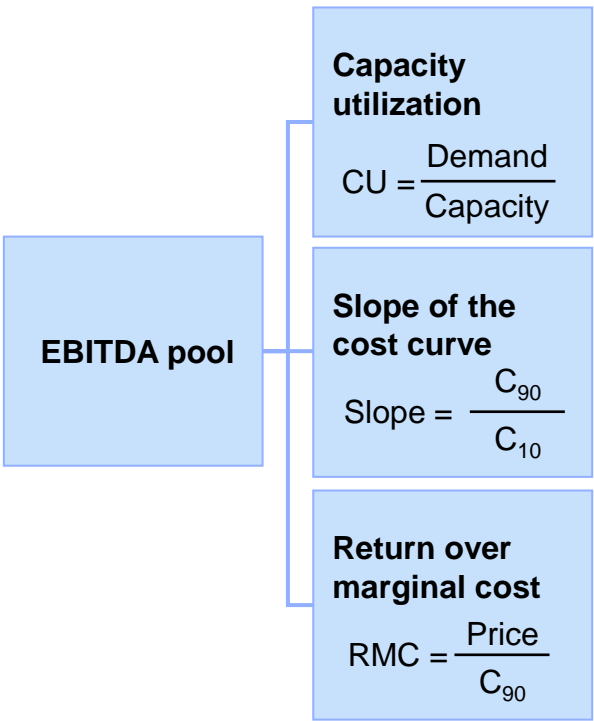
1 Rich ore equivalent





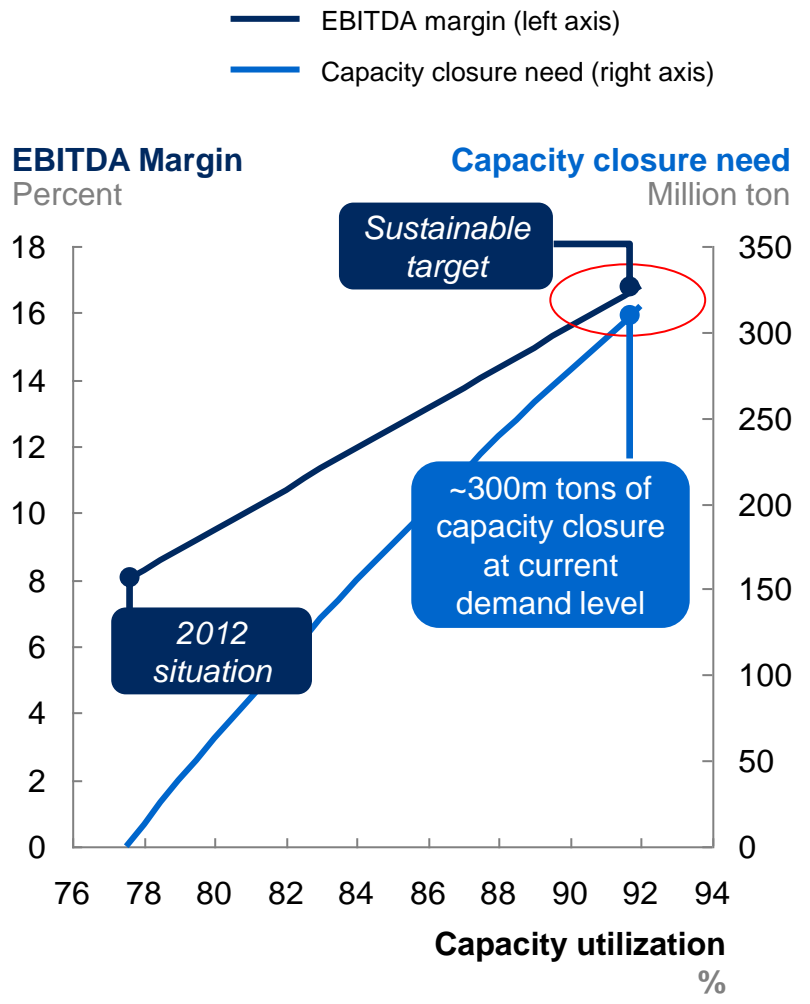
# Bridging the ~50 USD/ton margin gap to reach a sustainable EBITDA margin would require closing ~300m tons of global capacity

## EBITDA pool simulation logic



## EBITDA margin formula

$$\text{EBITDA}_{\%} = CU - \frac{(1+1/\text{Slope}) \times (1+CU)}{4 \times RMC}$$







# Beyond unilateral closures , several restructuring options have been mentioned

	Description	What is shared			
		Sourc.	Prod.	Com.	Log.
1 Unilateral closures	<ul style="list-style-type: none"> <li>Players unilaterally and independently reduce excess capacity according to their own timetable</li> </ul>	X	X	X	X
2 Unilateral closures and off-take agreement	<ul style="list-style-type: none"> <li>Some players close all or majority of production and negotiate agreement to source needed steel from remaining players, potentially at preferential rates</li> </ul>	X	✓	X	<i>Example</i>
3 Unilateral closures and leasing	<ul style="list-style-type: none"> <li>Closures same as above. In addition, players negotiate a lease of capacity, potentially at preferential rates</li> </ul>	X	✓	X	<i>Example</i>
4 Combined upstream steel utility	<ul style="list-style-type: none"> <li>Upstream capacity is pooled into a subset of entities with joint ownership</li> </ul>	✓	✓	X	<i>Example</i>
5 Asset specialization with off-take agreement	<ul style="list-style-type: none"> <li>Two or more payers agree to specialize in certain products and either exit noncore areas or swap assets</li> </ul>	X	X	X	X
6 Alliances or “code sharing”	<ul style="list-style-type: none"> <li>Players agree to partner in certain areas and reduce/ eliminate production where one partner is stronger and relies on the other for future production needs</li> </ul>	X	✓	X	✓

Require upfront anti-trust review

Likely the basis of ongoing dialogue with OECD and regional authorities