

Quick Supply-Demand Adjustment Comes from Our DNA

– Global Steel Boom Will Continue for Some Time –

Interviewer: Hamamoto Noriko

BACKED by the following wind of expanding domestic demand and increased foreign steel demand, particularly from China, major Japanese steelmakers are continuing to post brisk earnings. All the steelmakers are expected to rewrite their profit records after absorbing cost increases stemming from price hikes for raw materials such as iron ore and coal. Japan's steel industry went through "bitter experiences" in the past – a vicious spiral of expansion in output facilities during a boom became excess capacity causing a slump. What kind of strategy is the steel industry sketching out this time? Tomono Hiroshi, President of Sumitomo Metal Industries, Ltd., speaks about his company's business strategy in fast growing China, realignment and alliance moves in the industry, and a review of the industry's production systems.



Photo : Sumitomo Metal Industries, Ltd.

Steel Sheets for Automobiles Desperately in Short Supply

Japanese steelmakers have the global competitive edge in technologies for high-quality steel sheets used for car bodies. How do you estimate the future demand for these high-quality steel sheets?

Tomono: Steel sheets for motor vehicles are desperately in short supply. Automakers and electrical appliance makers have urged us to review our quarterly output plans and to supply more steel products. The supply-demand situation is extremely tight. On another front, a cutback in inventories of commodity-type steel products (used for construction and other general purposes) will be achieved in a short period of time. Steelmakers in the world have learned a lesson from the past severe tough decade and have come to act quickly – "never make products that do not sell well." It was a very expensive lesson. A quick action for supply-demand adjustment will continue to be a DNA for steelmakers.



The steel industry has repeatedly experienced boom-and-bust cycles. How long do you think the current favorable conditions will last?

Tomono: Waves of boom and bust hit all steel-using industries. The steel industry technically undergoes changes in association with such waves. The current favorable condition will last for some time. From the past lessons, all managers of steel mills in the world want to maintain sustained growth, though the level of growth may be small. Keeping stable stock prices for a

long time is what we would like to achieve. We feel embarrassed if our share prices undergo major fluctuations in a short period of time. In general terms, steelmaking was called a mature industry and its stock prices had long been low. It is desirable to be given a fresh look on the stock market and our reputation to come up.

How do you see the future of the Chinese market that is the driving force of current steelmakers' brisk performance?

Tomono: Steel is necessary for China to grow economically and to become affluent. Demand for steel could continue to expand at a fairly high speed now that China must narrow the gap between the rich and the poor. All steelworks in China, regardless of the size, are however producing steel to their full capacity, and commodity-type steel products remain in excess supply. The Chinese government, with a strong will, issued its first policy on the iron and steel sector to create a balance in July 2005. The policy is designed to curb the construction of small and medium-sized mills that lack environmental protection measures. We hope it will produce good results. Especially, environmental measures are extremely important for China to achieve sustainable economic growth.

Steady and Cautious Strategy in China

Nippon Steel Corp. has already established a joint venture with Chinese and European steelmakers to launch high-quality steel sheet production in Shanghai. How will you expand your business in China?

Tomono: If we are to launch production in China, it is on condition that we receive requests from Japanese manufacturers and are assured of clients. We do not have plans for conducting a big project such as the construction of a blast furnace. China's labor cost is low, but a huge amount of money will be needed to build facilities, including infrastructure, from the very beginning. We once studied whether to expand to China to build a production line for hot-dip galvanized steel sheets for automobiles' outside plates. We eventually decided to produce at the Kashima Steelworks at home. We will pursue a steady and cautious strategy in China.

South Korea's Pohang Iron and Steel Co. (POSCO) plans to build an integrated steel plant in India. Don't you think India is important, along with China, from the viewpoint of a long-term strategy?

Tomono: At present, we have no plans in India. People may see us getting a late start, but such a plan must be made from a long-range point of view. We will take a cautious stance in our business in India and other emerging economies as is the case with China.

Ready to Face Global Realignment of Steel Industry

How do you expect to respond to mid- to long-term changes in the demand for steel? It might be a good time to consider the realignment of production facilities with favorable business.

Tomono: We ceased the operation of hot-rolled steel output facilities at the Wakayama Steelworks and shifted the production to the Kashima Steelworks. Now we can launch full-scale production of hot-rolled steel. We implemented tough restructuring in addition to the structural reforms of plants. Favorable elements like a demand increase, particularly from China, may lose steam some time, but we have been wiping out risk factors thoroughly to prepare for such an unfavorable situation.

What kind of impact are you anticipating when the following wind from China has fallen silent?

Tomono: Steelmakers with high export ratio posted certain short-term profits in 2004 when export prices were higher than domestic prices. Our company, however, has long placed more importance on the domestic market, so we had no choice but to look enviously at export-oriented rivals. Sumitomo Metal will be stronger structurally if export prices turn lower.

The steel industry is facing global realignment. Do you think such moves may also hit Japan?

Tomono: I have no idea, but we have to prepare for such a case. We are now in an era of corporate mergers in which corporate managers are suddenly informed that their company shares are seized all at once just as seen in the case of Hanshin Electric Railway Co. – investor group M&A Consulting, or the so-called Murakami Fund, tried to take over the company. Corporate managers must look into all possibilities to simulate responses to takeover bids.

Sumitomo Metal is promoting an alliance with Nippon Steel and Kobe Steel through cross shareholding, and the three firms are making efforts for production streamlining through group purchases of raw materials and the introduction of a more efficient distribution system. How is the alliance progressing?

Tomono: We are currently working out an action plan. We have agreed to study possible takeover defense measures while deepening the alliance. It may take a while to find what types of defense measures are allowed. I think other companies are also in a similar situation.

The three steelmakers are studying mutual cooperation in the field of computer systems. What kind of cooperation is to be achieved?

Tomono: We are studying how to cover each other in the event of a system breakdown caused by natural disasters such as a major earthquake. As there are many technical aspects to be fully studied, we must take our time to deal with it adequately.

Work is under way at Sumitomo Metal to map out its next mid-term management plan starting in April 2006. What will be the key points?

Tomono: We did achieve the current mid-term management target ahead of our schedule. We would like to work out a target for the coming three years based on the ideal company goal in the next decade. We would like to spend some 10 years to establish Sumitomo Metal's individuality. I think this will be the key factor in the next mid-term plan. **JS**

Hamamoto Noriko is a reporter for the Economic News Section of Kyodo News.