

Harsh Climate for Smaller Manufacturers

The Japanese economy, which began to show clear signs of slowdown during the second half of fiscal 1997 as a result of the debilitation of the financial system's intermediary function and the currency crisis in Asia, is expected to show stronger deceleration in fiscal 1998, because no recovery of private-sector demand is foreseen while structural reform is progressing and because public demand is almost certain to decline in the worsening public finance situation. In such an economic climate, domestic demand for iron and steel in fiscal 1998 will decline for the second straight year, though some slowing of decline will be seen in the second half. Steel demand from the construction industry will remain stagnant due to government cuts in public investment, no recovery of housing investment is foreseen and investment in plant and equipment by the private sector is likely to level off. Demand for steel from manufacturing industries will stay low, because production activities at steel user industries have declined except at shipbuilding, which has a large order backlog.

Steel exports, which were brisk during the first half of fiscal 1997 and propped up production, were hit by the currency crisis in Asia, the main export market, and steel exports to Asia took a downward direction in the final quarter of fiscal 1997. In particular, steel exports to South Korea, Thailand and Indonesia, which were in a financial crisis, dropped sharply as steel demand in these countries plummeted, and no export recovery in fiscal 1998 is in sight. Japanese steel makers are endeavoring to promote exports to non-Asian regions and countries, particularly the United States, but cannot make up for the decline in exports to Asia. Total steel exports in fiscal 1998 on a global basis will decline sharply from an estimated 23.4 million tons in fiscal 1997 to 19.1 million tons in fiscal 1998. Moreover, there are fears

that import pressure from neighboring countries and regions such as South Korea and Taiwan will intensify.

In addition to the stagnation of domestic demand and the deterioration of the import/export balance, steel inventories, which piled up during fiscal 1997, will have to be adjusted during the first half of fiscal 1998. As a result, crude steel production in fiscal 1998 will decline sharply to about 96.0 million tons from an estimated 102.8 million tons in the preceding fiscal year. This is the first decline below 100 million tons in five years since fiscal 1993.

Regarding the domestic market outlook, no steel products are likely to show vigorous recovery, because domestic demand is sluggish. Developments will continue to depend on steel manufacturers' production policies.

The combined profits of Japan's top five integrated steel mills, which rose about 18.7% in fiscal 1997, will decline for the first time in five years despite continued cost cutting centering on fixed costs under each company's restructuring plan, because marginal profit will decline sharply, mainly as a result of the decline in sales volume and a rise in the dollar base price of iron ore.

Japan's smaller manufacturers of ordinary steel are not doing any better. Whereas it is feared that demand for steel from the domestic construction industry, the main user, will decline, there is excess production capacity as a result of positive plant and equipment investment made during the bubble period. Because the steel product market is depressed, improvement of the profit situation is currently out of the question. Therefore, the business cli-

Crude Steel Supply and Demand

(Unit: 1 million t)

	FY1996	FY1997 (E)	FY1998 (F)
Domestic demand	3.1% 85.6	▲1.8% 84.1	▲3.3% 81.3
Exports	▲8.3% 22.1	15.4% 25.5	▲13.7% 22.0
Imports	▲2.8% 6.9	▲1.4% 6.8	7.4% 7.3
Production	0.8% 100.8	2.0% 102.8	▲6.6% 96.0

Note 1: Domestic demand=apparent domestic consumption=production+imports-exports (includes inventory fluctuations)

Note 2: Top left numbers indicate year-on-year growth rate change (%)

Note 3: The fractions may not add up to the total, because of rounding off.

Source: Compiled by the Industrial Bank of Japan's Industrial Research Department from Tekko Tokei Yoran (Steel Statistics Survey) However, the figures for fiscal 1997 and fiscal 1998 are based on estimates or forecasts by IBJ's Industrial Research Department.

mate for smaller steel manufacturers will remain harsh in fiscal 1998.

Every small steel manufacturing company is endeavoring to bolster its profits by streamlining, such as (1) shifting working hours to nighttime in order to save on the cost of electricity and (2) by cutting manpower. However, streamlining carried out by each company in isolated endeavors produces only a limited effect, because variable costs centering on the cost of steel scrap and the cost of electricity represent more than 70% of the total cost and because a great many small and medium-sized enterprises have little room for maneuver in attempting to lower fixed costs. Every company is trying to ride out the present difficulty by using "savings" accumulated during the bubble period. At some companies, however, savings are nearly exhausted. Several attempts at reorganizing the steel industry are being made. Such attempts will accelerate hereafter. ■

(Kagami Akiyuki, economist)