

Higher Industry Concentration Can Enhance Top Steel Producers' Competitiveness

August 26, 2020

The acquisition of a majority stake in Taiyuan Iron & Steel (Group) Co., Ltd. (TISCO) by China Baowu Steel Group Corporation Limited (China Baowu) is, in our view, conducive to increasing industry concentration and reducing competition within the sector. The move falls in line with the national strategy of making the steel sector bigger and stronger. For the two companies, this deal may also be a boost to overall competitiveness and further stabilize their business.

According to an announcement by TISCO on August 21, 2020, Shanxi State-owned Capital Operation Co. Ltd. and China Baowu reached an agreement stipulating that a 51% stake in TISCO would be transferred to China Baowu, for no fee. Once the transfer of equity is complete, actual control of TISCO will be transferred from Shanxi's State-owned Assets Supervision and Administration Council (SASAC) to the SASAC under the State Council. China Baowu will take control of TISCO, and through TISCO will also assume control of Shanxi Taigang Stainless Steel Co., Ltd.

In our opinion, this development can further enhance China Baowu's overall competitiveness. China Baowu is China's largest steel producer, with crude steel output of around 100 million tons per year. The firm stands out for its production of steel plates for the auto sector and silicon steel, but had until now not gained a significant foothold in the stainless-steel sector. We anticipate that through taking control of TISCO, China Baowu can benefit from the former's leading position in the stainless-steel market and further broaden its line of products. We also expect this equity transfer to further consolidate China Baowu's overall business scale and position in the steel industry.

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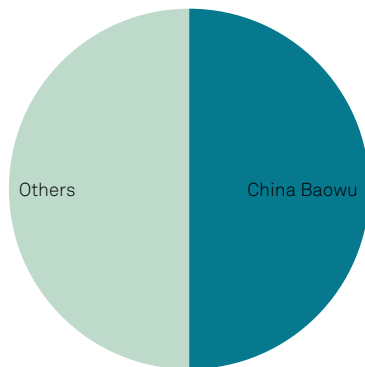
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Chart 1

Market Share of Automotive Cold-rolled Steel Plates, 2019



Note: China Baowu has disclosed that its market share of automotive cold-rolled steel plates is more than 50%, but has not provided specific values.

Source: Public information, S&P Global (China) Ratings.

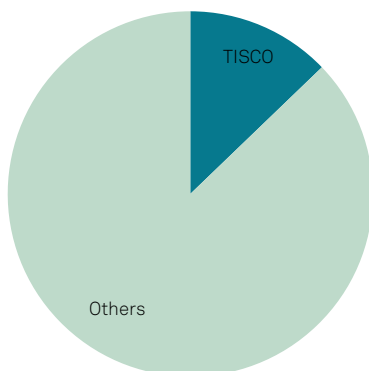
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At the same time, we view China Baowu as playing an important role in consolidating China's steel industry and making this industry larger and stronger, improving concentration within the sector. In 2019, China Baowu took a majority stake in Magang (Group) Holding Co., Ltd. (Masteel), and in June this year reached an agreement with Chongqing Iron & Steel Co., Ltd. (Chongqing Steel) to take over actual control of the company. The takeover of TISCO would further strengthen China Baowu's role in consolidating the steel sector.

Once the transfer is complete, we expect TISCO to integrate its internal resources with China Baowu, while moving to prevent both companies from competing in the same sectors. TISCO may also receive some group support through China Baowu, allowing it to better bargain with upstream and downstream sectors while further developing its stainless steel business. TISCO is a large-scale stainless-steel producer, with capacity to produce around 12 million tons of crude steel, 4.5 million of which is stainless steel. With advanced production equipment, TISCO has relatively strong competitiveness in stainless steel segment.

Chart 2

Market Share of Stainless Steel Production in China, 2019



Source: Public information, Wind, S&P Global (China) Ratings.
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Supply-side reform has, in our view, cleared a large quantity of outdated production capacity, leading to increased industry consolidation. The operating efficiency and financial risk of most steel producers have improved, while ability to manage risk and fluctuations in prices of raw materials have been strengthened across the industry. This latest transaction would be beneficial to elevating industry concentration in the stainless-steel sector and wider steel industry while reducing competition. Going forward, we expect further consolidation within the industry to continue as the industry consolidation level remains below targets set by the National Development and Reform Commission and Ministry of Industry and Information Technology.

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