ArcelorMittal

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news release

ARCELORMITTAL SOUTH AFRICA INTERIM RESULTS FOR SIX MONTHS ENDED 30 JUNE 2017

Salient features

- Steel imports continued to affect local production and sales in H1 2017
- Domestic steel demand at a seven-year low
- Safeguard duties on hot rolled products approved, but yet to be implemented
- Coal prices increase to $300 per tonne in quarter 2 2017
- Higher iron ore prices add to increasing cost base over the quarter
- Additional sales of 6 000 tonnes of heavy sections and rails as a result of manufacturing agreement with Highveld Steel
- Borrowing based facility of R4 500 million was concluded
- Financial performance negatively impacted by volatile exchange rate
- ArcelorMittal South Africa improves to Level 3 B-BBEE status

Johannesburg, 27 July 2017: ArcelorMittal South Africa has experienced a difficult and challenging first half of its financial year.

The operating and headline losses, which increased by R714 million and R1 161 million respectively, were affected by higher coking coal and iron ore costs, the relatively strong Rand/USD exchange rate and the continued weakening of the South African economy.

"Declining business confidence as a result of the recession, a 0,7% decrease in GDP during the first quarter of 2017, a downgrade to junk status and the highest unemployment rate since 2004 are all contributing factors to a weakened economy in South Africa," said Wim de Klerk, chief executive officer of ArcelorMittal South Africa. "In turn, this has resulted in minimal local investment and infrastructural spend, particularly in the construction and manufacturing sectors, and it has seriously constrained the local steel market."

Apparent steel consumption decreased by 3.8% as a result of subdued economic growth. In addition, South Africa and key African markets continue to import large quantities of steel, especially from China.

"Despite the import duties and the designation of local steel for Government infrastructure projects, half a million tonnes of steel were still imported into South Africa in the first half of the year," said De Klerk.

"We will continue to engage government around safeguard duties as further protection against the ongoing imports. We are grateful to government for its recent approval of safeguards on hot rolled products, and we look forward to the urgent implementation of these duties."

The fair pricing model approved by government last year is being implemented for flat steel products.

Operational review

Safety remains our number one priority and it is with great regret that we report three fatalities at our plants this year, all contractor employees. "This is completely unacceptable and we have initiated an enhanced process to better understand the nature of these accidents and improve communication between the company and contractors so that we maintain the highest safety standards across the entire business," said De Klerk.

On a positive note, the lost time injury frequency rate improved from 0.90 in the corresponding period to 0.62 in H1 2017.

Capacity utilisation in the first half of the year was 79%, compared to 83% the previous year. Liquid steel production for the period was 2.4 million tonnes, a decrease of 146 000 tonnes (5.8%) against H1 2016.

Production at ArcelorMittal South Africa's long products business was reduced as a result of the price decrease in scrap prices and the price increase in coking coal, which is used in the manufacturing process of long products, making these more expensive. The long products business was further impacted negatively by the deteriorating market conditions, however, the restart of the Highveld Steel heavy structural mill contributed 6 000 more sales tonnes of heavy sections and rails in the second quarter.

Flat products' liquid steel output decreased by 83 000 tonnes and plant utilisation decreased to 79% from 83% in 2016. This was due to a rupture of the stove at blast furnace C at Vanderbijlpark Works in the fourth quarter of 2016, and an incident at blast furnace D that resulted in a decrease in production of some 80 000 tonnes.

Cash cost per tonne of liquid steel produced increased by 27% to R8 063. This was largely as a result of a 43% increase in the cost of raw materials, essentially iron ore, coal and scrap, which account for 50% of total costs. Consumables and auxiliaries, which represent approximately 27% of costs, increased by 15%, and fixed costs per tonne increased by 13%. Electricity costs also increased due to annual electricity price increases.

The loss from operations increased by R714 million to R983 million, primarily due to the higher coal and iron ore prices, and the subdued economy. This contributed to a R1 773 million increase in the loss for the period.

The company implemented several initiatives to improve operational efficiencies, increase volumes and/or reduce costs. These include:

- The N2 battery refurbishment at Newcastle Works, planned to be completed by the third quarter of 2017, will improve the sustainability of the coke batteries and the batteries' coke-making capability (traditionally a significant EBITDA contributor) is expected to be restored to 381 000 tonnes per year
- The boiler project completed at Vanderbijlpark Works in June 2017 will enable optimal use of the power station in generating approximately 10MW additional power per annum – an anticipated benefit of R60 million.

Further restructuring, cost cutting and efficiency measures will be considered in the next quarter.

Financial review

Revenue increased by 12.6% to R19 151 million, mainly due to an 18.9% increase in average net realised steel prices, from R6 845 per tonne to R8 138 per tonne. This was partly offset by lower sales volumes.

In line with expectations, revenue from the Coke and Chemicals business decreased by 9.4% to R735 million due to scheduled but extended repairs to coke batteries at Vanderbijlpark and Newcastle Works. Commercial coke and tar prices increased by 117.9% and 5.5% respectively.

The net borrowing position worsened from a net cash positive of R1 010 million this time last year, to a net borrowing position of R2 577 million, mainly due to capex spending on the refurbishment of the coke batteries, lower operating results and higher financing costs.

ArcelorMittal South Africa has restructured its balance sheet by replacing overnight facilities with a three-year borrowing based facility of R4 500 million.

An impairment of R600 million was recognised against property, plant and equipment for the long products business, primarily as a result of the strengthening of the Rand against the US dollar and loss of volumes due to higher coal prices compared to competitors who do not use coal in their production process.

Markets

Total steel sales volume decreased by 95 000 tonnes over the six-month period. Local sales declined by 9.2% compared to the previous period due to the difficult trading conditions. This was partially offset by export sales which improved by 15.9%. The implementation of safeguards is expected to improve sales volumes of flat products.

Global steel demand has shown some improvement in the first half of 2017, mainly attributed to the positive market environment in developed countries. However, China's steel demand has been relatively flat compared to the last half of 2016. Demand was better, primarily as a result of an improvement in finished steel prices in key markets such as China, Europe and particularly in the USA, where imports of steel have increased in recent months after declining in the second half of 2016.

Overall, African markets have remained positive due to the drive towards infrastructure investments in rail, road and energy projects, specifically in the West and East Sub-Saharan regions. In the Southern African region, fiscal concerns and weak commodity prices have hampered investment progress. South African producers have lost sales in other African markets due to cheap imports into the continent.

Licence to operate

Air emissions are currently a key focus area for ArcelorMittal South Africa. Significant challenges regarding sinter emissions at Vanderbijlpark and blast furnace emissions at Newcastle Works are being addressed. An abatement system at Newcastle Works' blast furnace failed in February 2017 and a project to renew and replace the system will be completed in July 2018.

Our newly installed water treatment facilities at Newcastle Works are performing as expected, but in the case of Vanderbijlpark Works more work is scheduled at the effluent treatment facilities in order to sustainably conform to legislative requirements.

ArcelorMittal South Africa has proudly achieved a level 3 status as a B-BBEE contributor, compared to level 4 in 2016. De Klerk commented: "This is a significant achievement considering the constrained and challenging local environment, but we accept our role and acknowledge our duty to South Africa and its people. We have worked hard to achieve this rating and I would like to extend my personal thanks to all stakeholders who have contributed to the process, specifically our internal teams and the relevant authorities that have assisted and guided us."

Outlook

Volatility in the Rand/US dollar exchange rate will continue to have a material impact on the company's financial results. ArcelorMittal South Africa has implemented various initiatives to return the company to profitability and to generate positive cash flows.

"In order to address the serious challenges that we are facing, we are in the process of exploring several initiatives, including additional cost cutting interventions, assessing the profitability of various product lines and the implementation of structural changes within the next six months," concluded De Klerk.

Domestic steel demand is expected to remain subdued in the second half of the year due to the continued low economic growth and ongoing lack of infrastructure spend.

The flat steel business is expected to benefit from the implementation of safeguard duties in the second half of the year, while the long products business should improve, depending on coal and scrap prices, as the full benefit of the heavy sections and rail volumes is realised.

Export markets are likely to be more resilient. Projections are that Africa will experience growth in demand in the order of 2,3%, and as previously indicated, ArcelorMittal South Africa intends to aggressively pursue the Africa Overland (AOL) market.

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