

CASE STUDY
Restructuring in the Steel Sector in the CR

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Steel industry in the CR - Introductory characteristics

The steel industry of the Czech Republic demonstrated in recent years that it belongs to those manufacturing branches with very high know-how and very strong position at the market

However, the situation in steel industry was and still is hard. Here it was not possible to succeed in placing a sufficient volume of production in foreign markets, as the excess supply over demand in the world markets did not enable it (except demand from the China). Therefore, the fallen out export possibilities to the countries of the former Soviet Union could not be sufficiently replaced.

Steel is an important industrial sector in the Czech Republic, reflected by the level of employment in the sector and the added value created by steel producers in the country. The steel Industry is the dominant supplier of the metallurgical materials for the Czech industry with production over 6 mil. tons of steel yearly. Share on footage of evident domestic product of metallurgicy is more then 45%.

Over the last decade, significant restructuring of the steel industry in the Czech republic has been achieved, reinforcing the competitiveness of the sector. A large number of non-viable facilities have been permanently closed. Existing plants have been modernised so as to enable the production of the grades and quality of steel required by the markets. Changes in management structures have taken place in parallel with the ongoing privatisation and concentration process. The change from a product oriented to a market oriented culture is to be seen in the improvements in operational results of most companies.

The continued existence of the Czech steel industry is based on the following factors:

- The real market for steel products in processing industries and other sectors is capable of supporting an apparent domestic consumption of around 5 million tonnes per annum,
- The sector's competitiveness as manifested in the export volumes achieved is based on the specific strong aspects of the steel industry and partly on comparative advantages.

The marked reduction in manpower resulted in significant increase in productivity levels and made the adoption of social measures a necessity to reduce the impact of the restructuring process. The technical restructuring of steel producers show not only a reduction of input costs, but also a considerable cut in emissions to the environment.

Despite these efforts, the restructuring process in the steel sectors in the Czech Republic is not yet complete. Further restructuring is necessary if the companies concerned are to achieve viability and be competitive enough to operate under normal market conditions, especially those concerning competition.

For many companies in the country, up to now, viability could only be reached with the financial support of the Governments. For this reason, transitional periods were negotiated European Commission and the Czech Republic to allow the granting of state aid to specific companies. The maximum amount of state aid permitted corresponds to the financial projections made in the National Restructuring Programme and the Individual Business Plans of the companies, which were adopted by the Czech Governments and agreed by the Commission during 2002.

“National Czech Steel Sector Restructuring Programme” (NCSRP)

On 29th August 2001 the Czech Government accepted the decree on proposal of the Restructuring Plan of the Czech Steel Industry. This decree (No 840) has been published on the Government’s web site address <http://www.vlada.cz>.

This Programme is built on following steps:

- To start the Integration of the Steel Industry (to create the integrated Czech steelwork Company),
- To find out its strategic partner,
- To realize the property and financial restructuring including the debt write-off.

The structure of financing till 2010 is anticipated:

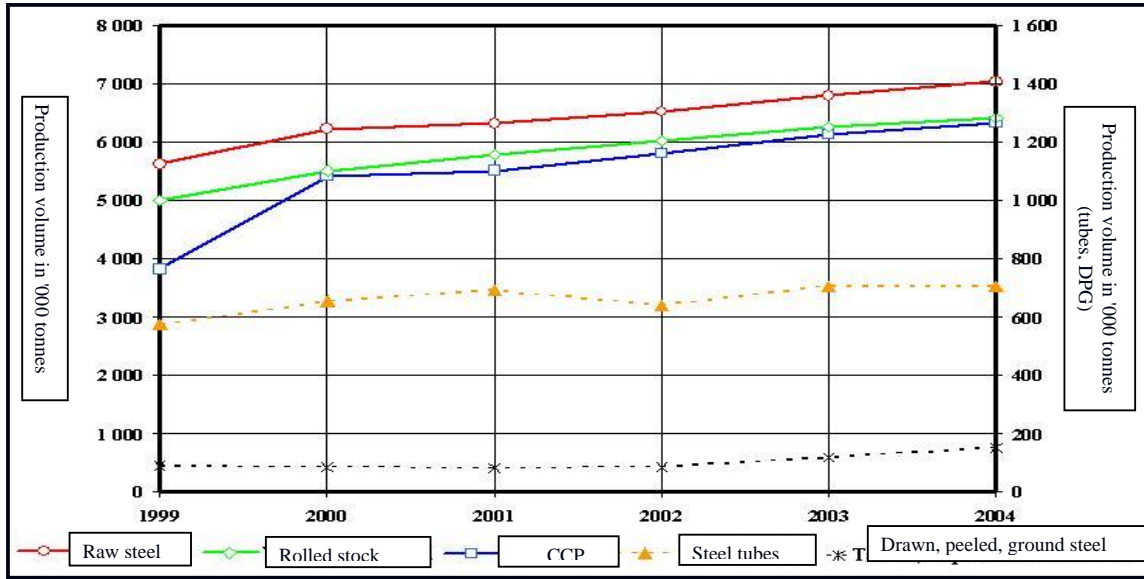
- The work’s own means CZK 41 billions,
- The state participation CZK 22.225 billions,
- The strategic partner, the consortium respectively CZK 10.8 billions,
- The EU financial help CZK 4.825 billions.

Comparison of basic steel productions included in the NCSRP:

Development of basic steel product assortment production volumes in the Czech Republic

Assortment	Unit	Production					
		1999	2000	2001	2002	2003	2004
Raw steel	'000 tonnes	5 615,54	6 215,84	6 315,87	6 511,97	6 783,27	7 032,99
Cont.cast.product (CCP)	'000 tonnes	3 814,48	5 417,33	5 500,52	5 795,98	6 127,95	6 334,00
Ratio of continuous casting	%	67.93	87.15	87.09	89.00	90.34	90.06
Rolled stock	'000 tonnes	4 987,75	5 501,30	5 774,48	6 019,34	6 261,33	6 395,21
Steel tubes	'000 tonnes	574,20	652,37	688,34	639,32	703,57	705,89
Drawn, peeled and ground steel	'000 tonnes	89,20	84,27	79,14	85,68	118,54	149,86

Development of basic steel product assortment production in the Czech Republic



Source: Ministry of Industry and Trade, Metalworkers' Federation

Apparent consumption of steel products in CR by customer sectors

Name	Share in apparent consumption / % /						
	1998	1999	2000	2001	2002	2003	2004
Mining of coal, oil, ores and other minerals	2.8	2.7	2.8	2.6	2.4	2.2	2
Production of basic metals and metallurgical products	1.9	1.2	1.3	1.5	1.6	1.8	1.5
Production of metal-working products, production of machinery and equipment	46.7	48.1	45.6	45.7	43.1	41.6	41
Production of electronic, electric, medical, optical machinery and equipment and time meters	2.4	2.6	2.9	3	3.4	3.1	3.7
Production of motor vehicles and other transport means and equipment	18.6	18.2	18.3	18.3	18.3	17.9	17.8
Production and distribution of electricity, gas and heat energy; collection, treatment and distribution of water	1.1	1	1.1	1.1	1.2	1.3	1.5
Construction	15.8	16.2	16.6	17.8	17.4	18.6	18.4
Wholesale and retail trade, trade mediation	7.2	6.8	7.9	6.6	8.5	7.9	7.6
Other consumer branches	3.5	3.1	3.4	3.3	4	5.7	6.5
TOTAL	100	100	100	100	100	100	100

Source: Ministry of Industry and Trade, Metalworkers' Federation

Overview of the development of basic steel product assortment import and export volumes in CR (ths t.)

Assortment	Export			Import		
	2002	2003	2004	2002	2003	2004
Ingots and semi-products	283,75	247,20	252,70	260,67	265,98	356,70
Long products	2 249,56	2 366,98	2 305,65	579,21	591,15	712,84
Flat products	997,57	994,98	950,58	1 541,98	1 512,21	1 814,73
Steel tubes	456,97	502,00	532,07	262,80	262,06	310,58
Other products *	427,82	458,39	485,25	369,94	394,02	537,69
TOTAL	4 415,67	4 569,53	4 526,24	3 014,60	3 025,41	3 732,55

Source: Ministry of Industry and Trade, Metalworkers' Federation

The steel industry in Czech Republic consists of a number of companies which are grouped in the Steel Federation.

They include:

- ISPAT NOVÁ HUŤ a.s., Ostrava – www.novahut.cz
- VYSOKÉ PECE Ostrava, a.s. – www.novahut.cz
- Třinecké železářny, a.s., Třinec – www.trz.cz
- VÍTKOVICE, a.s., Ostrava – www.vitkovice.cz
- VÍTKOVICE STEEL, a.s., Ostrava – www.vitkovice.cz
- VÍTKOVICE – Válcovna trub, a.s., Ostrava – www.tube.cz
- ŽDB, a.s., Bohumín – www.zdb.cz
- Válcovny plechu, a.s., Frýdek – Místek – www.vpfm
- JÁKL Karviná, a.s., Karviná – www.jakl.cz
- ŽĎAS, a.s., Žďár nad Sázavou – www.zdas.cz
- Ferromet Group s.r.o. (includes the firms Železářny Hrádek, Železářny Veselí, Železářny Chomutov, Válcovny trub Chomutov) www.pvtnet.cz/www/zch.cz/
- Sochorová válcovna TŽ, a.s., Kladno – Dříň

All companies except VÍTKOVICE STEEL are already privately owned. Privatization of VÍTKOVICE STEEL is to begin in the first half of year 2005.

European Commission approved the National Programme of the Czech Steel Industry Restructuring. Monitoring of its realisation included capacities' reduction will be made regularly twice a year till March 2007.

4 Half –yearly monitoring reports have already been submitted to EC with respect to the implementation of the Czech Steel Sector Restructuring Programme, elaborated for the periods of 2002 and 2003.

Labour



At the beginning of the nineties the metallurgical works were facing severe over-employment. The reasons for this situation can be traced back to the seventies:

- Metallurgy (like a number of other branches of the national economy) employed in addition to its main productive activity a large part of the labour force in the field of so-called social consumption (recreational centres, special-interest activity and the like).
- Another aspect was the fact that the metallurgical organisations have been built up as fully autonomous production and economic units with own power engineering, housing economy, training and apprentice centres and the like. In the interest of higher valorisation, further power, engineering and other departments have been linked up to the integrated iron and steel works. The units formed, in this way, complied in the accepted philosophy neither with the intentions nor with practically possibilities of privatisation and with the entry of Czech and foreign capital in particular.
- The other side of the coin of over-employment in metallurgical works at the beginning of the nineties was the already above-mentioned decreasing production in connection with the difficulties in trading the Czech metallurgical production in local and foreign markets. This resulted in several times lower labour productivity in comparison with abroad.

Therefore, reduction of labour force is caused by:

- Decreased sales and production (competitive ability, new construction solutions, quality, savings in steel works),
- "Elimination" of non-productive and service facilities and departments,
- Preparation for privatisation of new structured production units.

Development of employment and labour productivity in the steel sector during 2001 - 2004

Year	2002	2003	2004
No. of employees	29 500	28 250	25 914
Of which: steel workers	13 500	12 740	10 960

Source: Ministry of Industry and Trade, Metalworkers' Federation

Labour productivity assessed in terms of steel volume produced per employee (t./year)

Year	2002	2003	2004
Production per employee in CR	466	509	611

Source: Ministry of Industry and Trade, Metalworkers' Federation

Labour productivity is the fundamental factor affecting the viability of steel companies and also a criterion for wage trends assessment.

Associated Social Programme for the steel industry restructuring

To solve the social and employment consequences of the restructuring of the Czech steel industry, the government adopted the “Comprehensive Plan for the Associated Social Programme for Steel Industry Restructuring”(ASP) in 2000.

Meetings are held regularly between the consultative team of the Ministry of Industry and Trade (MIT) and the Metalworkers' Union KOVO, Employers Union, representatives of trade unions and key representatives of steel companies, as well as representatives of involved state administration sectors, Ferrous Metallurgy Association and Confederation of Industry of the Czech Republic. The issue of the sector restructuring and implementation thereof is being discussed also in the Government's Economic and Social Reconciliation Board. This dialogue is focused on resolving the social and employment impacts of Czech steel sector restructuring.

The Associated Social Programme was amended at the turn of 2003/2004 due to the continuous outsourcing of auxiliary activities outside the steel production sector. Government Resolution no. 50/2004 has extended the term of ASP until 31.12.2006 so as to comply with the individual business plans of the steel companies concerned and the implementation of the Programme, particularly with the terms of winding-up and liquidation of non-efficient final mills capacities, which the Czech Republic has undertaken to.

By the end of 2006 certain technological equipments stated in the obligations of the Czech Republic in Protocol no. 2 to the Accession Treaty will be liquidated, in accordance with business plans of steel companies presented to the European Commission. This means that the termination of certain jobs in the companies by the end of 2006 will require a settlement of the claims for contributions even after this term, not later than on 30 October 2007. The term specification of the application of the mentioned ASP does not require any additional financial sources; it only harmonizes the time aspects according to the final wording of the decisive documents approved by EU.

The programme includes motivation for redundant employees:

- a) in the event of job loss outside the steel sector, with a contribution 10-20 % higher,
- b) in the event of self employment, with a contribution 30 % higher.

Contributions are paid from the state budget through Ministry of Industry and Trade.

Simultaneously during 2004 the steel companies disbursed CZK 1 040 million in the settlement of severance pay to compensate for redundancies.

State budget allocation for ASP implementation

Year	Number of persons	Disbursed (million CZK)
2000	1971	130
2001	988	215
2002	1261	171
2003	1180	203
2004	785	167

Source: Ministry of Industry and Trade

Other instruments for the settlement of social and employment consequences of the Czech steel industry restructuring are included in:

- The implementation of the START programme - a programme supporting business activities. 403 non-interest-bearing loans were extended in the total volume of CZK 176 million across the entire business sphere in 2004. More than 2/3 of these loans provided by Czech-Moravian guarantee and development bank (Českomoravská záruční rozvojová banka) were directed to support the entrepreneurial activities of persons redundant in scope of the steel companies restructuring,
- The Regional Development programme - stimulating the generation of new jobs in regions affected by restructuring,
- The implementation of Balance programme – this programme is based on the creation of individual restructuring projects and the implementation of restructuring plans.

Payments to workers made redundant due to steel sector restructuring are governed by Government Resolutions and subsequent amendments. Contributions are paid from the state budget through the budget of the MIT. MIT, which releases these obligatory contributions each year, makes checks to ensure that the designated funds are spent effectively and economically, while fully respecting the terms and conditions set forth. A control program was developed enabling across-the-board checks of contributions paid to all steel company employees made redundant due to

steel sector restructuring since 2000. Checks of documents proving that all applicable terms and conditions for these payments have been met are carried out at the steel companies themselves. These checks had the result of defining a set of measures aimed at improving the system of disbursing the entitlements to individual companies. In 2004 checks of funds disbursements for ASP were performed at all the companies. The hitherto results of the checks to date show that companies are disbursing the allocated funds in a responsible manner. The amounts paid out meet applicable criteria. Currently the Supreme Control Office is performing an independent control of MIT and the steel companies.

Anticipated disbursement of ASP funds by the end of restructuring phase of the Programme

Year	million CZK
2005	160
2006	110
Settlement of outstanding claims in 2007 (overlap)	60

Source: Ministry of Industry and Trade

Summary of standard social welfare instruments (used to address the impacts of restructuring):

- Early retirement (2 to 3 years before entitlement),
- Financial contributions for redundant employees paid from company reserves - according to collective bargaining agreements. Example - bonuses paid to redundant workers of INH, when upon an application of a particular worker for a termination of employment the company awards a bonus amounting up to 25 monthly wages. This solution excludes a concurrent drawing of ASP funds,
- Services of employment agencies (to assist adaptation of redundant employees),
- Employee retraining,
- Labour Pool (adaptation for a preset period, work experience, retraining, secondment of employees...),
- Financial support and consulting to business start-ups - e.g. the START programme.

The current challenges of the steel industry are:

- The financial position of Czech steel companies is stabilised. Steel companies that had received state aid under the exemption approved by the EU Council achieved positive financial results and their operating profits rose. Their improved financial positions had an impact on positive developments in viability indicators.
- Total debt reduced by 10.2 %,
Wage intensity decreased by 23.8 %,
Work productivity (based on revenue) rose by 51.7 %.

- There are companies today which are profitable and effective (INH, Třinecké železářny, a. s.), as well as loss-making companies which do not generate the resources required for their reproduction (Ferromet Group of Z-Group). The viability criteria for individual companies receiving state aid are listed and assessed in the appendix, as assessments of individual business plans.
- Operating profits have continued to grow in comparison to the same period in 2003, while the accounting income rose by more than 43 %.
- From the point of view of liquidity assessment the situation has improved particularly with respect to the ability of the individual companies to cover their short-term liabilities.
- Higher revenues have also resulted in a higher utilisation of assets and in shorter turnaround times for stocks which were cut by 1 day (by 3 %) in a year-to-year comparison.

Source list:

The Ministry of Industry and trade, www.mpo.cz

The Czech Moravian Confederation of trade Unions, www.cmkos.cz

The Steel Federation, Inc, www.hz.cz

The Confederation of Industry of the Czech Republic, www.spcr.cz

The Chamber of Commerce, www.hk.cz