

## Trade Measures Investigation - Hot Rolled Coil exported from Malaysia – Verification Visit to Megasteel Sdn Bhd

### Background

Megasteel Sdn Bhd ("Megasteel") is a unit of Lion Corporation Berhad (referred to as the "Lion Group"), a diversified conglomerate which established its first rolling mill in 1978 and expanded to upstream steelmaking thereafter. Relevant information concerning Megasteel's financial performance is included in the Lion Corporation 2011 Annual Report.

Megasteel commenced its operations in 1999 with investment of MYR 3.8 billion and is the sole HRC producer in Malaysia with annual HRC capacity of 3.2 million and CRC capacity of 1.45 million.

### HRC Production

Megasteel uses Direct Current Electric Arc Furnace Compact Strip Production (EAF) process in its flat steel mill. Its HRC is supplied to downstream manufacturing and infrastructural developments (e.g. highway guardrails, cargo freight containers and cranes, water pipes, gas cylinders, vehicle chassis and parts). Its CRC applications include pipe and tubes, office furniture, automotive and motorcycle body panels.

Megasteel's HRC range is included at Attachment 1.

### Megasteel's 2011 performance

Megasteel's current HRC and CRC capacity utilization is less than 40% and its business is badly affected by the influx of cheaper imported products into Malaysia. It launched safeguard measure (which was terminated by Government last year) that requested for additional 35% duty on top of the current import duty at 25% and subsequently requested the Government to consider reducing import duty on flat products to 15% from 25% (decision still pending). For the financial year ended June 30, 2011, Megasteel recorded a net loss of RM146mil on the back of RM2.8bil in revenue (in 2010 profit was RM249 million). It had short-term debt commitments of RM2.99bil while its long-term borrowings stood at RM457.5mil (i.e. a combined debt-level of RM3.3 bil – approx A\$1 billion).

In 2011, Megasteel accounted for approximately 97 per cent of the Lion Group's domestic sales<sup>1</sup>. The 2011 loss for the Lion Group was driven by Megasteel. The value of Megasteel's assets in the Lion Group is approx \$4.4 bil – representing approximately 95 per cent of the Lion Group's assets.

### Losses in 2011

Note 2 of the Lion Group's 2011 Annual Report indicates the following:

*"The Group reports the following conditions and events:*

- (i) Current liabilities exceeded current assets by RM2.21 billion as at 30 June 2011;*
- (ii) A subsidiary of the Company, Megasteel Sdn Bhd ("Megasteel") had exceeded certain credit terms in relation to trade and other payables, and product financing liabilities as disclosed in Note 33. In the financial year ended 30 June 2010, Megasteel has entered into deferral payment plans with a significant constitution of these creditors. However, Megasteel had not met with the rescheduled*

<sup>1</sup> Lion Corporation Berhad 2011 Annual Report, P.114.

*repayment of the overdue outstanding balances with these creditors in the current financial year.*

(iii) *Megasteel entered into a Restructured Scheme for the Syndicated Term Loans in the financial year ended 30 June 2010 with the following terms:*

- (a) *The rescheduled payment terms of the RM denominated Term Loan and USD denominated Term Loan as disclosed in Note 28(A);*
- (b) *The sale of quoted shares of a related party as disclosed in Note 28(A)(i); and*
- (c) *The sale of certain property, plant and equipment of the Group as disclosed in Note 28(A)(ii).*

*Megasteel was unable to comply with the rescheduled payments in (iii)(a) above. A consent from a requisite majority of lenders of the Syndicated Term Loans was obtained to defer the balance payment of RM115.6 million to September 2011. A further extension was granted in September 2011 where a requisite majority consent was obtained from its Syndicated Term Loan Lenders to defer the balance amount after certain progressive payments up to December 2011.*

*Due to the weak market condition, megasteel has yet to complete the sale of certain property, plant and equipment of the group as mentioned in (iii)(c) above."*

The Note 2 further indicates that in light of the issues relating to repayment of the liabilities and borrowings, the Lion Group is discussing with third parties arrangements for the injection of working capital into the Group. It is further stated that these circumstances are cause for *"material uncertainty that may cast significant doubt about the Group's ability to realise its assets and discharge its liabilities in the normal course of business."*

#### **Reduced domestic supply**

Megasteel's performance in 2011 has been hampered by the increased availability of HRC imports into Malaysia from China, Korea, Japan and Taiwan. On 6 August 2012, MITI announced a formal investigation into the alleged dumping of HRC from Taiwan. The recent safeguard inquiry and dumping investigations in Malaysia are indicative that Megasteel's domestic performance is lagging (with cited utilisation rates of 40 per cent).

A reduced utilisation rate impacts Megasteel's production costs. On the basis of Megasteel's performance in 2011 and its request for anti-dumping measures in 2012, it can be assumed that Megasteel's performance in 2012 is comparable with 2011 and losses are again likely. Further losses will impact the basis for normal values for Megasteel for HRC exported to Australia during the period April 2011 to March 2012.

#### **Sales to related parties**

The Lion Group 2011 Annual Report identifies a number of related/associated parties that are members within the Lion Group of companies. For example, the Lion Corporation Berhad has 100 per cent ownership in Total Triumph Investments Limited (a British Virgin Islands company) which in turn has subsidiaries including a 100 per cent ownership in Bright Steel Sdn Bhd that is involved in the sale and distribution of steel and iron products. Further, Bright Steel Sdn Bhd has a 100 per cent owned subsidiary company Brights Steel Service Centre Sdn Bhd which is involved in the processing and selling of steel coils and sheets.

In its examination of domestic sales, C&BP must be alert to sales to associated/related entities within the Lion Group of companies (refer to P. 77-81 of the Lion Corporation Berhad 2011 Annual Report). Lion Corporation Berhad also has interests in a company involved in the sale of hot rolled steel plate – a further entity that may be purchasing HRC from Megasteel.

**Conclusions on Megasteel HRC**

The Malaysian market for HRC is the subject of a 25 per cent import tariff. Imports of HRC from ASEAN countries, however, are at duty free rates. In 2011 and 2012, imports of HRC from China, Japan, Korea, and Taiwan have increased in Malaysia. The sole HRC producer – Megasteel – has sought to address increasing HRC import volumes through applications for Safeguard and anti-dumping measures.

Megasteel's applications for remedies, combined with its widely-known reduced utilization rate for HRC, are indicative of reduced performance in 2011 and 2012. The extent of the loss experienced in 2011 – expected to be replicated in 2012 – support a position that selling prices for HRC in Malaysia across the period April 2011 to March 2012 are depressed and suppressed.

In its examination of Megasteel's costs for HRC, it is expected that the low utilization rate and the high debt burden will weigh heavily of the cost per tonne of HRC produced by Megasteel. There exists a high likelihood that normal values for Megasteel may be based on the company's costs of production plus appropriate amounts for selling & administration, plus profit.

C&BP is requested to exercise caution in its verification of costs and to ensure that all costs are examined (particularly borrowing costs).

**Attachment 1**

**Product Range:**

| <b>Product</b>                  | <b>Thickness</b> | <b>Width</b>   | <b>Coil Diameter</b>         | <b>Coil Weight</b> |
|---------------------------------|------------------|----------------|------------------------------|--------------------|
| Hot Rolled Coil                 | 1.0mm - 21.0mm   | 900mm - 1575mm | Inner Diameter : 760mm       | 10 MT - 30 MT      |
| Hot Rolled Coil Pickled & Oiled | 1.5mm - 6.0mm    | 900mm - 1575mm | Inner Diameter : 610mm       | 8 MT - 30 MT       |
| Cold Rolled Coil                | 0.35mm - 3.2mm   | 900mm - 1575mm | Inner Diameter : 508mm/610mm | 8 MT - 30 MT       |

**Quality Specification:**

|                            |                |                   |
|----------------------------|----------------|-------------------|
| Hot Rolled for Cold Rolled | SAE<br>BS 4360 | 1006, 1008<br>43A |
| Cold Rolled Coil           | JIS G 3141     | SPCC, SPCC-ID     |

*Note: Test methods according to standard requirements following ASTM, JIS or equivalent standards*