

HONG KONG METALS INDUSTRY 2014 OUTLOOK AND TRENDS

JANUARY 2014

ABOUT THE SURVEY

In developing this report, Australia and New Zealand Banking Group Limited ("ANZ") commissioned the Hong Kong Productivity Council ("HKPC") to conduct the survey. The survey was conducted during November and December 2013 and intended to gauge perceptions of future business performance and likely challenges facing companies in the Hong Kong Metals Industry. For the purposes of the survey, we understand from the HKPC that around 200 companies were interviewed and focus groups were held.

2014 INDUSTRY OUTLOOK AND TRENDS:

Highlights

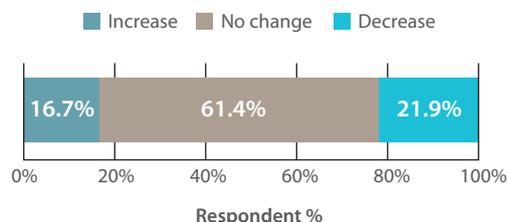
- > 40.3% of respondents expect a decline in gross margins during 2014, while only 12.6% of respondents predict an increase.
- > Metals manufacturers with operations in China are under increasing pressure from rising labor and material costs.
- > RMB appreciation has exacerbated rising production and operating costs.
- > 20.2% of respondents expect a longer accounts receivable cycle in 2014.
- > A majority of respondents do not exercise any financial risk control measures.
- > Faced with extensive competition, respondents suggest that research and development and talent development are two critical factors for the sustainability of the industry in Hong Kong.

DECREASING ORDERS & THINNER MARGINS IN 2014

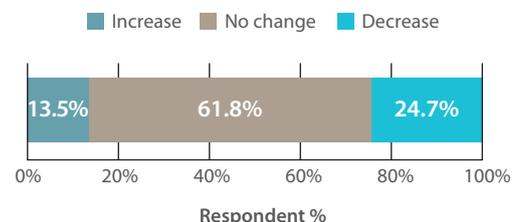
Demand for Iron and Copper to Decrease

Survey participants were asked to estimate the 2014 demand for the four major types of metals; namely iron, steel, copper, and aluminum. The survey results indicate an expected decrease in demand for iron and copper, only a slight increase for steel and flat growth for aluminum.

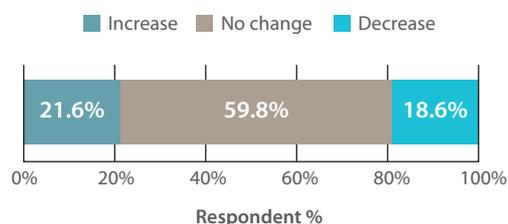
2014 Demand for Iron



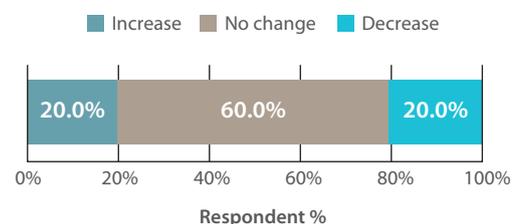
2014 Demand for Copper



2014 Demand for Steel



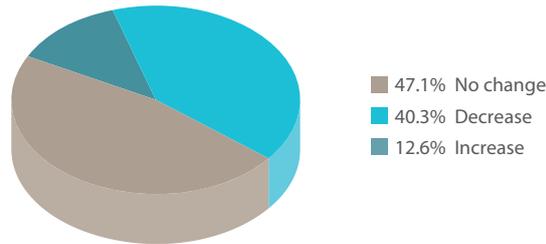
2014 Demand for Aluminium



Respondents Expect a Drop in Gross Margins

40.3% of respondents expect a decline in gross margins in 2014, while only 12.6% of respondents expect an increase. The remaining 47.1% of respondents predict no significant change in gross margins.

2014 Fiscal Year Gross Margin Change



RISING LABOR AND MATERIAL COSTS

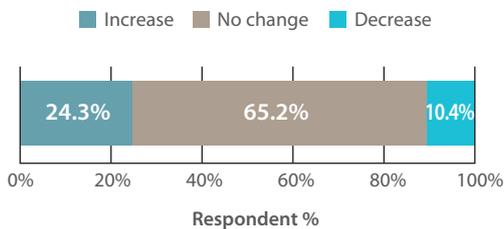
Expected Increase in the Prices of Major Types of Metals

Respondents expect the prices of the four major types of metals namely iron, steel, copper and aluminium to increase in 2014. The weighted average price increment increases¹ expected by respondents are as follows:

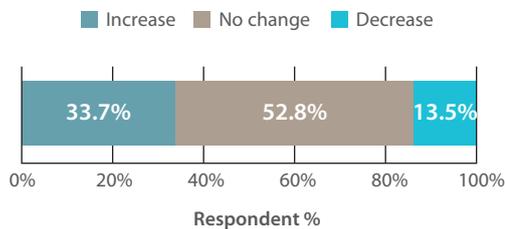
Metal	Increase
Iron	8.4%
Steel	7.7%
Copper	10.8%

In addition to increasing metal prices, a double digit wage increase is widely expected in 2014 for the major cities in China. These compounding costs will have a significant impact on gross margins in the metals industry.

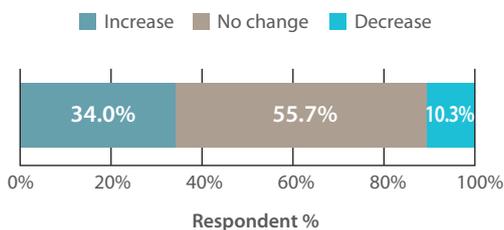
2014 Price of Iron



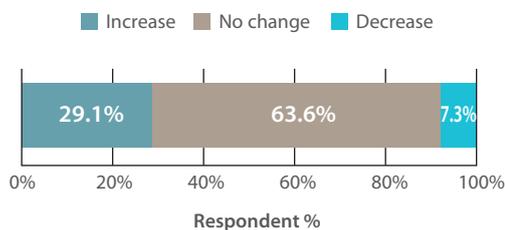
2014 Price of Copper



2014 Price of Steel



2014 Price of Aluminium

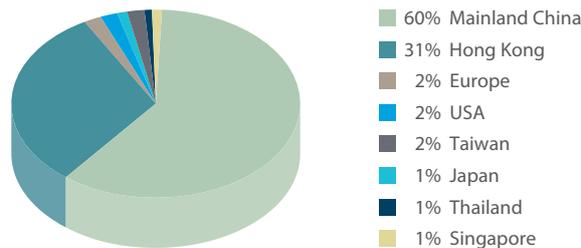


1. Unable to estimate weighted average price increment percentage for Aluminium as the sample size is smaller than 30

RMB Appreciation Exacerbates Rising Cost Impact

A majority of respondents (60%) maintain their manufacturing facilities in China while selling to customers outside China. This means that payments are received in other currencies while RMB is used for input costs and wages in China. RMB appreciation will increase production costs, thereby reducing overall profitability.

Location of Manufacturing Processes

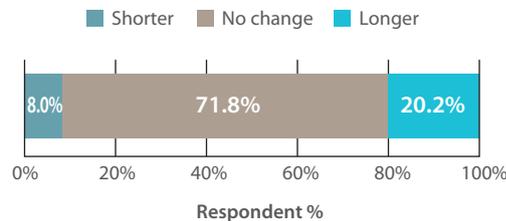


LONGER ACCOUNTS RECEIVABLE CYCLE

Longer Accounts Receivables Cycle Expected in 2014

Some 20.2% of respondents expect their accounts receivable cycle to be longer in 2014, compared to 8.0% expecting a shorter accounts receivable cycle.

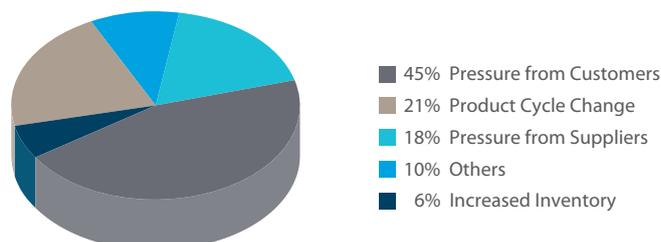
2014 Change in Accounts Receivable Cycle



Pressure from Customers the Major Impact on the Working Capital Cycle

Most of the respondents cited pressure from customers as the major factor affecting working capital cycles. In addition, changes in product cycle times and pressure from suppliers are also major factors lengthening the working capital cycle.

Factors Impacting the Working Capital Cycle



GROWING THE TALENT POOL KEY FOR SUSTAINABLE GROWTH

Key Challenges for the Metals Industry in 2014

The top 3 challenges for the metals industry as cited by respondents include:

- > Increasing cost of production (RMB appreciation and exchange rate risk),
- > Decreasing orders, market shrinkage and lack of profitability
- > Keen market competition.

According to the survey, Hong Kong's major competitors in the metals industry are Taiwan and Mainland China.

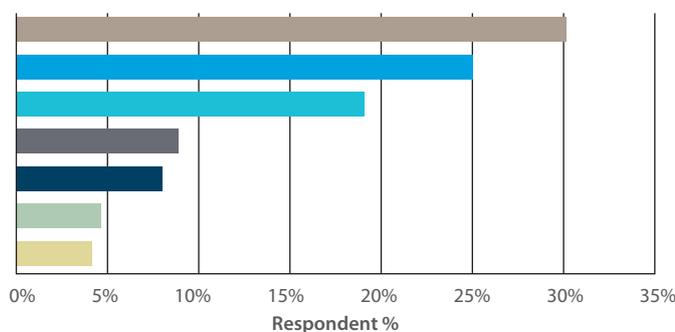
Taiwan is seen as having a relatively stable workforce supply, while the Taiwanese Government is seen as providing effective research and development (R&D) support for the industry. Chinese metals manufacturers are seen as being very good at imitating product design at lower costs, however quality standards are perceived as low.

Government Support for Growing Talent Pool and R&D

Respondents cited mould design and electroplating technology as the key competitive advantages of the Hong Kong metals industry. However, the industry is experiencing a shortage of new talent and companies have limited resources for R&D expenditure.

Respondents expressed that more government support for nurturing talent and providing R&D funding are essential for the long-term viability of the industry.

Challenges for The HK Metals Industry

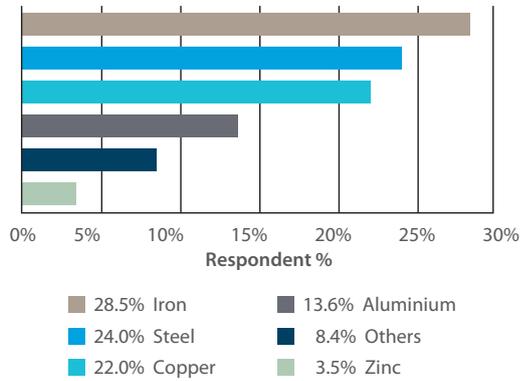


- 29.9% Increasing Cost of Production (RMB Appreciation/Exchange Rate Risk)
- 25.2% Decreasing of Orders/Market Shrinkage/Not Profitable
- 19.0% Keen Market Competition
- 8.8% Weak/Unstable Economy
- 8.2% Others
- 4.8% Fluctuating Raw Material Price
- 4.1% Lack of Human Resources/Expertise

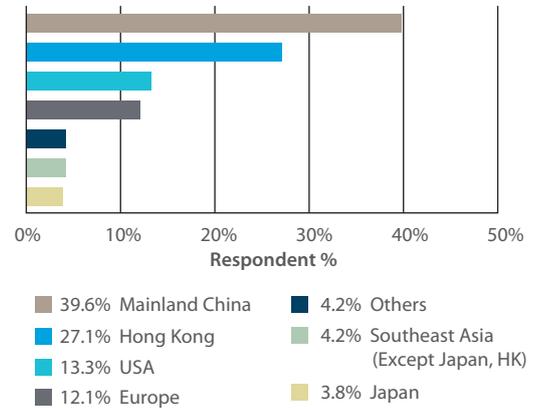
APPENDIX

Major Types of Metals and the Major Sales Markets

Major Types of Metals

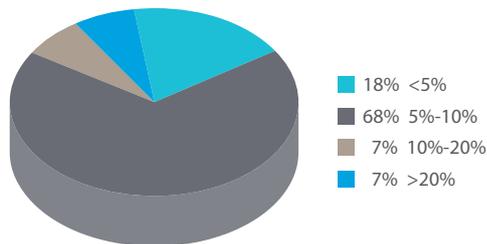


Major Sales Market for Metals

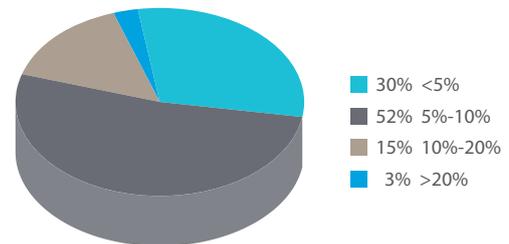


Price Increment of Major Types of Metals

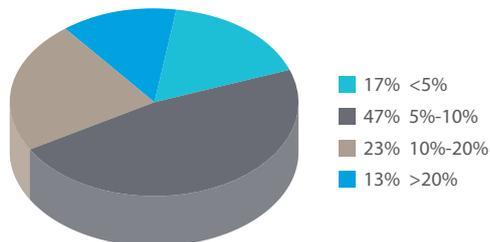
Price Increment of Iron



Price Increment of Steel



Price Increment of Copper



ENQUIRY CONTACT

If you would like to make an appointment with one of our Relationship Managers, please contact:

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