

# [Problems facing tata steel company](https://assignbuster.com/problems-facing-tata-steel-company/)

The Tata Iron and Steel Company (name later changed to Tata Steel) was established by Sir Jamsetji Tata in 1907. By 2006 it was India’s largest integrated private sector steel company. With its recent acquisitions and mergers, the company has become a multinational with operations in various countries. It was recognized as the world’s best quality steel producer in 2005. Though domestically the company had seen significant growth in the 100 years, it ranked a poor number 56 globally in terms of steel output. In order to enhance its market share in the global market Tata steel made several smaller foreign acquisitions, including Singapore’s NatSteel and Thailand’s Millennium Steel. But these small incremental deals would not enable Tata Steel to capture the sudden opportunity that had arisen in the steel market.

We believe that Tata Steel had to act in response to the changing environment, the industry structure and to exploit its competencies and resources at its disposal, which led to its decision of acquiring Corus, a steel firm much bigger in size compared to Tata Steel. We propose to explain the need for the related linked diversification, logic and reasoning behind the deal through the Resource-Based Model of Above Average Returns and the I/O Model of Above Average Returns.

## Resource-Based Model of Above Average Returns

## Deriving Synergies

There were a lot of apparent synergies between Tata Steel which was a low cost steel producer in fast developing region of the world and Corus which was a high value product manufacturer in the region of the world demanding value products. Synergies also existed in terms of sharing and manufacturing practices, shared services and purchasing. Also there were other synergies between the two companies; Corus was a large player in value-added services while Tata Steel was one of the lowest cost producers of steel in the world. According to Tata Steel Annual Report of 2007-08 the expected synergies and efficiencies had already started flowing in and would bring in annual benefits of USD 450 million per annum by year 2010.

## Raw Material

Tata Steel also has a relative cost advantage because it owns iron-ore mines which Corus did not. Corus was fighting to keep its productions costs under control and was on the lookout for sources of iron ore. (Tata Steel owns enormous volumes of high-quality iron ore and other minerals needed for steel-making. Captive raw materials linkages have given the modernizing and expanding Jamshedpur mill a competitive edge. Tata Steel is set to build greenfield mills in iron ore-rich states of Orissa, Jharkhand and Chhattisgarh). The joint entity will have a self sufficiency in raw material.

## Cultural

There was a strong culture fit between the two organizations both of which highly emphasized on continuous improvement and ethics. Tata steel’s Continuous Improvement Program ‘ Aspire’ with the core values: trusteeship, integrity, respect for individual, credibility and excellence. Corus’s Continuous Improvement Program ‘ The Corus Way’ with the core values: code of ethics, integrity, creating value in steel, customer focus, selective growth and respect for our people.

Importantly, the rest of cultural differences between the two companies had been taken care of and the two merged entities were working under their joint management. Tata Steel’s earnings per share had improved after the merger.

## Sharing Competencies

According to Ratan Tata, post-merger the immediate focus would be on extracting synergies from Corus. He felt that there was scope to make Corus a competitive steel company by inculcating the creativity and cost-consciousness in Corus as had been generated in Tata Steel.

## Product Mix

Geographical and product mix possibilities. The combined entity will emerge as the second most geographically diversified steel company. It will have access to high valued- added product mix and strong market positions in automotive, construction and packaging.

## Reputation

The Corus acquisition allowed Tata Steel to enhance its reputation and acquire a Global name. This has the potential to open up other markets for steel for Tata Steel, improve its bargaining power with respect to suppliers and customers.

## Sharing Complimentary Strengths

Corus has a strong Research and Development (the number one position in the entire world) and product development for value added products in auto, construction and packaging which compliment what Tata Steel is doing in the fast growing Asian markets. A merger would complement their respective strengths.

## Low Cost Slabs

Tata Steel has large supply of iron ore slabs from its green fields established in India in places like Orissa, Jharkhand, etc. Tata Steel can supply this slabs to Corus once these green fields in India are complete.

In addition, there will be other ways to create value, linked to the projects of Tata Steel in India today.

## Patents and Technological know-how

Corus has eighty-one patents that have been filed and assigned to the Corus by the United States Patent Trademark Office. Tata’s completion of the acquisition meant it ended up becoming the owner of these patents. There would be technology transfer and cross-fertilization of R&D capabilities between the two companies that specialized in different areas of the value chain.

## Distribution Network

Tata has a strong retail and distribution network in India and SE Asia. This would give the European manufacturer a in-road into the emerging Asian markets. Tata was a major supplier to the Indian auto industry and the demand for value added steel products was growing in this market. Hence there would be a powerful combination of high quality developed and low cost high growth markets.

With Tata Steel the cheapest manufacture of steel in the world the new company will become highly profitable.

## Strategic and Integration Committee

A ‘ Strategic and Integration Committee’ was formulated to develop and execute the integration and further growth plans. Appropriate cross functional teams were formed under this committee to look into specific issues.

There were some concerns over the lower return of capital employed and EBIDTA margins in 2007-08 which seemed to have declined. As debt would be repaid over the years, the EBIDTA margin as well as return of capital employed were likely to improve, but would need to be carefully watched.

## I/O Model of Above Average Returns

## Scanning

At around eight per cent of GDP growth, India is seen well poised for a burst in development, a high increase in production output and a surge in demand for various goods from the common people of India.

Industry experts are buoyant and bullish on the economic, demographic (in terms of young workforce, increase in incomes and hence an increase in consumption), and the helpful political environment (in terms of tax reliefs to industries, a commitment from the government to implement and introduce policies which further the interests of commerce).

The Tata’s were able to identify the early signals of potential changes in the environment and detect the changes that were underway. They were able to connect the dots and realize that as a result of the above changes in the environment the steel industry would look more and more attractive. There would be more need of steel due to the growth of car and aviation industries.

## Monitoring

It was clear that in a fragmented steel industry to get the cost advantages and a competitive edge to exploit the emerging opportunities consolidation was needed in the steel segment. This logic was the basis for a spree of mergers and acquisitions pursued by Tata Steel. The rapid progress of the Indian automobile, engineering and construction industries means that the country will need more and more high-quality steel and it is seen that the global steel prices are on an incline.

Access to Corus’ technology will, in course of time, allow Tata Steel to move up in the value chain. The acrimonious but successful Mittal-Arcelor deal also gave Tata’s sufficient signal on consolidation being the emerging trend in the steel industry.

## Forecasting

Although, Tata Steel was India’s largest integrated private sector steel company but globally ranked number 56 in terms of steel output. The Tata’s realized that the Corus buy would instantly catapult Tata Steel to the position of 5th largest steel producer in the world, and provide access to the latest technology and strategic European markets as Corus had plants in Britain, Germany, France, the Netherlands and Belgium. It was also expected that Tata Steel would benefit from reduced production costs due to large volume, combined R&D operations and broader product range. Corus acquisition would also dovetail with Tata Steel’s efforts to move up the value chain, as the former had built a reputation as an established supplier to the aviation and auto industries.

## Assessing

Brazilâ€Ÿs CSN and other players were also trying hard to acquire Corus which meant that a quick acquisition was the only alternative. Tata’s had and assessed the situation realized the need to act quickly and swiftly. It was clear that a small window for a big opportunity had opened up for Tata steel.

This was a risky consolidation, considering that the future of Tata Steel is dependent mostly on Corus’ performance but it is well known that entrepreneurial decisions involve risk. We can understand that it may be one of the entrepreneurial decisions that Tata Steel had to make for the future success of the company.