

## INTERNATIONAL BUSINESS

# Upsides for Steel Industry in a Russian Downturn, Despite Sanctions

By **ANDREW E. KRAMER** JUNE 16, 2015

CHEREPOVETS, Russia — Burly steel workers in this gritty industrial town have their choice of free services at the company spa in a leafy park down the road from the factory.

Thirty masseuses are on hand to treat aching backs and sore muscles. The spa menu at Rudnik, or the Spring, also includes hot mineral baths, mud wraps, acupuncture and a sauna — all served with organic, stress-reducing teas made with local honey.

Life is good for workers at the steel company, Severstal.

Along with the spa perks, Severstal covers the cost of vacations to Sochi on the Black Sea. A company dental office offers two free fillings annually. Workers also got 8 percent pay raises this year, along with bonuses.

“A crisis has supposedly occurred,” Andrei G. Meledin, who works on a production line, said. “But we don’t feel it here.”

As the rest of Russia retrenches in the face of recession, steel companies like Severstal are booming. In the first quarter, Severstal swung to a \$343 million profit, after reporting a loss in the same period a year ago.

Falling oil prices, rising geopolitical tensions and Western sanctions have broadly wreaked havoc on the Russian economy. The World Bank estimates that the economy will shrink by 2.7 percent this year.

But those same conditions have proven extraordinarily favorable to a certain class of Russian commodity companies, particularly in the steel and chemicals industries. It's the type of success story that Russia's government intends to highlight at an economic forum in St. Petersburg later this week.

Such companies, which have not been ensnared by sanctions, are benefiting from a weak ruble. These companies have significant costs for raw materials and labor, all of which are denominated in rubles. Their goods, though, are sold on the global markets, where prices are generally set in dollars.

While the ruble has recovered somewhat in recent months, it still remains 39 percent off its high of last year. And the central bank is intentionally trying to keep a lid on the ruble's value, boding well for the companies' profits.

As an unexpected pocket of strength in the Russian economy, steel is helping the country weather the onslaught of Western sanctions and bringing runaway gains for investors who got in this winter.

Shares in Mechel, a Russian steel and coal company, are up more than 180 percent since the start of the year, making it one of the best-performing stocks in the world.

Share prices for a dozen or so other steel and nonpetroleum commodity exporting companies also shot up this year, leading an overall rise in the Morgan Stanley index of Russian stocks of 19 percent.

"We have it all" in the Russian steel industry, Vladimir V. Zaluzhsky, the head of investor relations at Severstal, said of the benefits of a weak currency and still relatively strong global prices of steel.

The success of steel reflects the scattershot effect of sanctions on the economy. Certain industries are shrugging off the restrictions, as others teeter.

Strangely, sanctions hit hard in communities with a history of opposing President Vladimir V. Putin politically, such as the urban middle class in Moscow, which is reeling from inflation. The restrictions missed core supporters of Mr. Putin in some industrial and mining towns, while strikes and economic protests have broken out in others.

“Small and medium businesses are hurt by the sanctions” more than large commodity enterprises, said Daniel Treisman, a professor of political science at the University of California, Los Angeles. “The lower ruble obviously helps exporters and hurts consumers.”

Steel has a long history in Russia.

The plant here was founded by Joseph Stalin, who liked the metal enough to take the Russian word for steel as his name. Amid the bucolic swamps and fields of the Russian north, the gargantuan smokestacks arose.

Central planners poured substantial resources into steel mills, with a special emphasis on giant blast furnaces. The largest of them all, nicknamed Severyanka, or the Northern Woman, opened here in 1986.

The Northern Woman is a gigantic cylinder of heat-resisting ceramic tiles, swathed in tubes and scaffolding, continually rumbling and emitting a hissing mist of orange, iron oxide fumes. Valves in this artificial volcano release streams of liquid iron that burble out at a rate of 12 tons a minute.

Soviet planners’ fascination with steel soon proved illogical, as plants pumped out vastly more metal than needed. Western economists took to snickering at the bloated size of the Soviet steel industry. By the early 1990s, the factories faltered and the furnaces went cold.

But the industry, with its excess capacity, was well positioned for the rise



apartment blocks nestled in the northern forests.

A shiny Kia car dealership opened on the edge of town. With tax revenue from the factory, municipal workers were laying a new ribbon of asphalt on the airport road. The hockey team hired a Canadian defenseman. In a park, boys climbed on the pedestal of a statue of a steelworker.

The company spa, too, does a brisk business. It is so strong that Severstal has recently expanded it, opening an offshoot in a picturesque pine forest outside the city. The factory pays all the spa fees for workers.

“We make steel, and we make a lot of it,” said Nikolai G. Vaulin, a steel mill worker, as he soaked in a hot mineral water bath at the spa. “So we make a lot of money. And some of it ends up here.”

“Boy this feels good,” he added. “I feel light. My circulation has improved.”

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