

Office and Plant:
2800 South 61st Court
Cicero, Illinois 60804-3091

(708) 735-8000
(800) 323-2750



Mailing Address:
P.O. Box 5137
Chicago, Illinois 60680-5137

Facsimile:
(708) 735-8100

November 17, 2004

CONSOLIDATION – THE IRRESISTABLE FORCE?

For the first time in many months, the big story in the world of steel did not involve China, at least directly. This was the announcement that the Ispat International/LNM Group was buying the International Steel Group. The acquisition would make the new company, to be called Mittal Steel, the largest in the world, with a capacity of around 70 million tons.

This development is probably not the last consolidation in the world steel industry. Europe's Arcelor had become the former "Number 1" by putting together a group of smaller companies, and you will recall that my last letter reported China's desire to consolidate its industry into four or five companies with 40 million ton capacities. After the Mittal announcement, the *Financial Times* reported that Thyssen Krupp is thinking of a merger with Corus.

President Bush's program for steel rested on three legs: the Section 201 duties on injurious steel imports (now discontinued), efforts to address international overcapacity, and rationalization of the domestic industry. The latter objective has been to a large extent realized. ISG was formed out of the bankruptcies of Bethlehem, LTV, Acme Metals and Weirton Steel. A number of other mergers and acquisitions have also occurred.

The Mittal and Arcelor consolidations may be showing that what lies ahead are much larger companies than could be assembled solely from elements of the U.S. industry. U.S. Trade Representative Zoellick has remarked that it is puzzling that the North American steel industry is not more multinational, like so many other sectors of our economy. The Mittal interests had already broken ground in that respect by acquiring Inland several years ago, and, now, the ISG purchase will assure that the largest U.S. company will be a world-wide operator.

I believe that this trend will continue. It apparently makes economic sense, not the least by permitting steel producers to bargain more effectively with large customers, like the automotive sector. The question for our company (and probably yours) is what are the implications for our operations, which are downstream from basic steel production. We can see pluses and minuses, and our task will be to make sure that the former outweigh the latter.

Turning to marketplace specifics, it appears that the trends towards higher input costs are unabated:

- Scrap. The record prices I reported last month didn't last long. This month, the price of #1 Dealer Bundles hit \$430 per mt and #1 Busheling (Chicago) was higher at \$435 per mt. In early November, the *American Metal Market* reported that auto bundles had been sold at \$442.50. Thus, the recent suggestions by some prognosticators that scrap prices would moderate in the fourth quarter seem ill founded.
- Pig Iron. Brazilian spot prices (New Orleans) rose \$15 to \$365 a mt. The outlook is for more increases as scrap availability in the U.S. is curbed by cold weather. In addition, exports from Brazil (80% of which are sent to the U.S.) are being slowed by port backlogs – it has been reported that some 600,000 tons will not be exported due to this problem. Another factor here is the tight world supply of iron ore. Prices for this commodity are expected to rise 20% in 2005.
- Coke. Prices for Chinese coke have declined significantly from over \$400 per ton a few months ago to \$239, apparently due to China's decision to lower its export licensing fees, which were over \$200 per ton. China will export 13 million mt of coke this year, down 1.7 mt from 2003. Further price declines are unlikely, as coal supplies become scarcer. One independent specialist reported to the International Iron and Steel Institute that he expects 2005 coal prices will be around \$100 per mt, compared with \$45 - \$55 this year.
- Ocean Rates. The continuation of port bottlenecks in Brazil, China and, recently, Australia and increased demand (principally from China, which now is the world's largest importer of iron ore) have caused freight rates to climb again. The Baltic Capesize Index stood at 7140 early this month compared with 5580 in October (and 1076 in October, 2001).
- Natural Gas. No surprise here in light of crude oil prices recently. The Nymex contract price this month soared to \$8.75 per mcf, up \$2 from last month.
- Exchange Rates. This cost factor of imported steel and some raw materials has come back to bite buyers. Canada's dollar is up 6.5% since September, and the Euro has risen just short of 6% in the same period.

On these not too happy notes, I close for this month. As always, this letter and my others can be found on our website -- www.coreysteel.com.