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An Invitation to Dialogue

Last month, we recalled the first of our letters, sent in February, 2004, which addressed steel market conditions. We pointed out that raw materials prices and other cost factors, which we considered extraordinary in those earlier days, look pretty tame by today's standards. Both letters were written to set a factual context for our discussions with our customers.

This month, we want to approach the current market from another angle – how market participants can react to stressful conditions.

An old and good friend in the steel industry, now passed on, had a colorful way of describing how things went in earlier times: "This year, I'll be on my knees to my suppliers. Next year, they'll be on their knees to me." His suppliers would be saying the same thing, only referring to their customers.

This kind of approach may have been good for the knee pad industry, but it achieved little lasting satisfaction for suppliers or their customers. We all know about the resentment that shifted back and forth even in long-standing commercial relationships. One factor in the growth of imported steel mill products was probably customers' reactions against perceived market arrogance by the major producers at a time when foreign suppliers were happy to step in.

We all also know about the legendary purchasing agent "who would sell his grandmother for a half-cent a pound". Suppliers would shake their heads and dream about what they would do when the shoe was on the other foot.

We believe that there can be a better way to confront the kind of market conditions we face today. We and you are being squeezed between suppliers whose costs are going up and customers who refuse to budge on prices they will pay. One way to cushion the effects is to take unilateral action – customers can impose new terms on payments or require quality add-ons at no increase in price; suppliers can cut their costs in ways neither apparent nor beneficial to their customers. We think that the end result of that approach harms both sides – mutually advantageous business become compromised, product quality (both the supplier's and the customer's) can suffer and company planning can go awry.

We all complain about government regulations and taxes that keep changing – we plead just to know what we can expect over the long term. “Tell us, and we can live with it,” we beg the regulators and legislators. Yet, when it comes to market conditions, we often do exactly the same to ourselves, letting the inevitable ups and downs of costs and prices cause more disruption than is necessary.

What do we offer as an alternative? The best we can hope for is better communication before we undertake unilateral measures to protect ourselves. We know, for example, in many cases we can help our customers meet the market conditions they face without the kind of cost shifting that might otherwise occur. We tell our sales reps to make sure that our customers know about the conditions that we face and we expect them to know about yours. Operating with knowledge is always better than groping in the dark.

We are not naive. We know that economic conditions won't improve just because we have a better dialogue with our customers. But we do know that longer term considerations, like supplier-customer relations, can best be brought into the calculations on both sides if there is a continuing conversation. We hope that you will join us in those conversations.

Here are some cost specifics for this month:

- Scrap and Pig Iron. Last month, we recalled how in February, 2004, we used words like “exploded” and “zoomed” to describe price increases. Those increases looked pretty tame by what had happened more recently. But where in the lexicon do you find words to describe what happened last month to scrap? Prices for #1 dealer bundles and #1 busheling (Chicago) have now hit \$600 per mt, up \$180 and \$170, respectively. Those increases, about 65% in a single month, shattered the old price high of \$435 per mt. What more can be said? By comparison, the \$70 increase in the spot price for Brazilian pig iron (cif New Orleans) looked mild; although the current price of \$590 per mt sets a new record and reflects an increase of \$190 since last October.
- Natural Gas. The Nymex contract price for natural gas moderated slightly this month, down 11 cents to \$9.91 per mcf. That price for the month is still the sixth highest on record, however.
- Ocean Freight. The Baltic Capesize Index was down again this month, dropping about 900 points to 7741. Things may be returning to normal after the sharp spikes between August and December last year.

- Exchange Rates. The euro is clobbering the dollar; it was up another 5¢ in the last month and now costs \$1.59. This is a 12¢ increase in two months, a huge movement. The pound was unchanged, however, at \$1.99, perhaps reflecting the economic problems Britain seems to be confronting. The Canadian dollar was also unchanged at \$0.99.

We appreciate the many comments we have received on these letters. If you haven't yet given us your reaction, please do. If you have, we still want to hear from you. This letter, like all the others, will be on our website, www.coreysteel.com and on the international site, www.steelonthenet.com.