

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

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“CAUSES AND EFFECTS – – THIS YEAR’S CHICKENS COME HOME TO ROOST”

This month’s news is not surprising, since it echoes many of the matters we have addressed in recent letters. Basically, we are seeing the expected results of events and decisions that have gone before.

- Several major steel producers have reported third quarter results down sharply from a year ago. Nucor’s profits were off almost 30%, SDI was down 60%, and US Steel’s profits declined almost 70%. In each case, increased energy and raw material costs were blamed. A decline in demand also affected results with these and other companies.
- The International Iron and Steel Institute (“IISI”) met in Korea recently. Prognosticators suggested that 2006 world steel demand, excluding China, will be about the same as in 2005. Demand in China is expected to go up by 10%. Production next year might be higher because there was a significant work off of high inventories in 2005. Experts suggested that China will make between 20 and 30 million mt more steel next year and that production in the rest of the world will increase by 20 to 25 million mt.
- Speakers at the IISI meeting also sang the old song about the cyclical nature of the steel industry, which deters potential investors. Overcapacity is the culprit, since problems in one market quickly spread to others as producers seek to get rid of their steel. One solution suggested was the effort to reach international agreements on capacity, like those that have been attempted within the Organization for Economic Cooperation and Development (“OECD”). These efforts have been underway for many years, so far without success. A more likely cure to some of the overcapacity problem may be increased concentration of production. Mittal Steel, for example, recently bought a plant in the Ukraine, which brought its capacity to over 75 million tons, and it announced a deal with a state government in India to build a plant with another 13 million ton capacity.

- The trade talks sponsored by the World Trade Organization – the so called “Doha Round” – received another blow this month in London, when delegates from the US, the EU and other countries seeking to sell their farm products were unable to clear away any significant disputes. This failure makes it very likely that the ministerial meeting in Hong Kong next month will achieve little or nothing, thereby putting unprecedented pressure on the viability of the talks.
- At this writing, the budget problems in the US continue to be very difficult, but there are some signs that the Congress is getting serious about doing something. The leaders in the Senate were forced to pull legislation that would add to the deficit by making some tax cuts permanent and adding others. There is also growing sentiment to revisit the transportation bill’s thousands of “set-asides” for pet (or pork) projects, totaling tens of billions of dollars. Apparently, the voters have convinced many legislators that deficits do matter.

Turning to some specifics:

- Scrap and Pig Iron. The yo-yoing of scrap prices continued this month. After dropping \$60 per mt last month, #1 dealer bundles and #1 busheling (Chicago) shot back up \$60. They are both at \$295 per mt. Pig iron has remained relatively steady; the spot price for Brazilian pig iron (cif New Orleans) was up only slightly to \$258 per mt. One statistic of interest reported at the IISI meeting in Korea – the major iron ore producers, which supply 75% of internationally traded ore, have raised their prices by 256% since the beginning of 1999, compared with an increase in steel prices of 156% over the same period.
- Ocean Freight. The Baltic Capesize Index is plugging along without any significant increase in the last three months. It is still about 20% higher than in the first half of 2003, but it is well below the wild pricing that we experienced in the following 24 months.
- Natural Gas. It was hard to believe that prices could continue to climb, and they didn’t. However, the \$2.10 drop in the Nymex contract price still leaves the cost at \$11.76 per mcf, the second highest ever. Warm weather had a beneficial effect, but demand during the winter may prevent further decreases.
- Foreign Exchange. The dollar continued to strengthen last month. The euro declined to \$1.18 and the pound went down another 2¢ to \$1.73. The Canadian dollar was down a penny to 84¢.

Amidst the many problems we confront, it is easy to overlook all the blessings that we in America enjoy. So it is good that we are approaching Thanksgiving, with its power to get us to see and appreciate all the good things in our lives. We at Corey wish you a pleasant holiday.

As usual, this letter will be posted on our website, www.coreysteel.com and on www.steelonthenet.com.