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UNCERTAINTY – FOR SURE

My July letter suggested that a “return to normalcy” might be underway, in the sense that the U.S. might be becoming an attractive export market, as Chinese demand eases. We have further evidence of this trend in the most recent data. At the same time, input costs are on the increase again, some to record levels. Thus, at least for the present, the outlook is not for lower domestic steel prices.

The highlights:

- China. For the first six months of 2004, China’s steel imports fell by about 3% from the same period in 2003. The decline is largely due to increased Chinese production – output for January-May was up from the previous year by 23%. The country’s iron ore imports increased by 35% over the same period.
- U.S. and World Capacity Utilization and Demand. Domestic raw steel production was up by about 4% through July, hovering around a 90% capacity utilization rate. Similarly, slab production world-wide is reportedly at 90% utilization. Many U.S. mills are on allocation, as demand has increased by over 10% this year. *Steel Buyers’ Forum* reported that its survey shows that service centers will be maintaining higher inventories than during the first half of 2004.
- Imports. Imports for the first half of 2004 were up by 30% over the same period of 2003. Import prices are said to be similar to U.S. mills’ prices. Thus, while imports are on the rise, we are not back to the “normal” conditions where foreign steel is offered well below market. August 26, 2004
- Scrap. Prices for #1 Dealer Bundles and #1 Busheling (Chicago) sky-rocketed to \$405 per ton in July. Since May, those prices have increased by \$185. This appears to be a world-wide phenomenon driven by demand for steel and coke shortages that have curbed production. (US Steel reported that 10 of its coal suppliers had declared “force majeure” making it hard to maintain a steady supply of coke.) Scrap prices were reportedly up by \$25 to \$43 per tonne in Germany and \$62 in Italy.
- Pig Iron. The Brazilian spot price (delivered to New Orleans) has gone up, probably in concert with scrap prices. In just two months, the price has increased from \$250 to \$340 per ton, or 36%.

- Ocean Freight Rates. These rates have leveled off at \$35 for three months now, but there are pressures for increases, including the cost of new regulations to improve security, as well as fuel costs and higher demand.
- Natural Gas. Despite record crude oil prices, natural gas (Nymex contract) continued to decline in August to \$5.82 per mcf. It seems likely, however, that volatility will return before too long. We know that price futures increased during August by around 25¢.
- Surcharges. Most U.S. producers add a surcharge to their steel prices. There are many different approaches to these surcharges, so it is difficult to compare them, one against another. However, month-to-month changes in surcharges by individual companies show substantial increases in August. For example, Nucor increased its surcharge from \$80 to \$180, and ISG raised its from \$100 to \$165. Both US Steel and ISG have announced price increases for September.

These changes leave us in familiar territory: uncertainty. There seems to be no end in sight to high input costs, particularly scrap and coke. The hot world market has cooled somewhat, but increased demand in the U.S., coupled with these high raw materials costs, have prevented much in the way of easing prices for steel products. The recent spike in crude oil prices is playing out by bringing pressure on producers and retail consumers alike, and no one knows where the Fed will be taking us on interest rates. No one can accuse these times of being boring.

As usual, we shall be posting this letter on our website: www.coreysteel.com.