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IS THERE A FORD IN OUR FUTURE?

The economic news this past month has been significant, more so than in some time. Housing sales have declined, signaling a slowdown in the economy; gas prices have come down around 20%; auto sales are off; and the Fed has left interest rates alone for two straight months.

Amidst all of these developments, the travails of one company, Ford, seemed to be in the news almost daily. The company's performance and restructuring plan recently caused Moody's to cut its rating of senior unsecured debt to a B3 "junk bond" status. A series of announced layoffs, buy-outs, plant closings, corporate reshuffling (including bringing in a new CEO to replace Bill Ford) has seemingly not been enough to restore confidence in the company's future. Ford will no longer be the number 2 producer in the U.S., losing that place to Toyota.

The basic problem for Ford, in addition to the high built-in labor costs that plague American automakers, is its sales profile. More than other producers, Ford has marketed the SUVs, pick-up trucks, and other low mileage vehicles that buyers are spurning in the face of $3 a gallon gas. Ford's sales of those vehicles were off 25% in August.

For any long time veteran of the steel industry, the situation at Ford is reminiscent of our troubles in the late 1970s and early 1980s. We were then facing imports of good quality steel sold at low prices. We also had excess capacity and employed more workers, hourly and salaried, than we needed. We faced high energy costs due to the second "oil shock" of 1977. And, of course, we had the additional burden of extremely high interest rates.

What resulted was the worst steel economy since the Depression. Capacity utilization plummeted, in many cases to below 50%. Workers were laid off by the tens of thousands, and many companies vanished. But, once the dust had settled, the remaining steel producers were leaner and smarter and began to claw their way back to profitability. The road back was not entirely smooth, however. At the turn of the century, another industry downturn occurred, caused in good part by floods of low priced imports. That crisis was weathered more easily; although a very large number of companies went through bankruptcy before reappearing, often as part of newly created consolidations. The rigors of the earlier crisis had steeled our industry to hard times – we were making better products at lower costs and with fewer people.

While no direct comparisons can be made between steel and autos, there are some similarities. The inherent labor cost disadvantages of American car makers, due to a dwindling labor force supporting the pension and health care claims of large populations of retired workers, will have to be addressed. The production profiles that rely on the sale of high profit margin gas-guzzlers will have to be changed. Consolidation will have to be explored. But, most of all, the companies will have to make their plans for the world we live in, where the pressure for energy efficiency is becoming relentless.

The specifics for this month:

- Scrap and Pig Iron. Prices were virtually steady this month, for the first time since the beginning of the year. Number 1 dealer bundles remained at $275 per mt, while #1 busheling (Chicago) climbed only $5 to $280 per mt. Pig iron (Brazilian spot price cif New Orleans) also was up by $5, to $315 per mt.

- Ocean Freight. We have now seen the same story for eight months. The Baltic Capesize Index stayed at last month's 3176, about the same as three years ago in September, 2003. It appears that, at least for the time being, the pressure is off.

- Natural Gas. Following the lead in crude prices, natural gas was off sharply. The Nymex contract price declined $1.58 to $5.67 per mcf, a drop of 22%. These prices, too, are around those of two and one half years ago.

- Exchange Rates. As of this writing, the euro is at $1.28, unchanged from last month, the pound is worth $1.90, up a penny, and the Canadian dollar is at 89¢, down a penny.

As usual, we request your comments and suggestions. Also as usual, we are posting this letter on our website, www.coreysteel.com, and it will appear on the international site, www.steelonthenet.com.