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## **TAX DAY – DID YOU ENJOY?**

Tax day is now behind us, and it might be appropriate to look at some of the things the government is doing, now that we have provided the financing.

- Inflation and the Fed. The other day, the Dow was up almost 200 points on news that the Fed's Open Market Committee believed in March that their "tightening process" was likely nearing its end. The very next day, however, observers took a step back in the face of a 0.4 % increase in the consumer price index and a 0.3 % rise in core inflation (i.e. disregarding price movements for food and energy). Those increases threw into doubt the Committee's conclusion, also made in March, that core inflation was not moving up in response to higher energy prices. Thus, while most assume that there will be another interest rate hike in May – to 5% – we are still in the dark as to what will happen thereafter.

It is interesting to note the attitude of the Fed towards energy prices, which climbed over 17% in the year ending in March. Apparently, those increases, by themselves, will not cause the Fed to raise interest rates. Only when the increases are passed through into core items, like housing, clothing, transportation and the like will the Fed act. One reason is that energy prices are not effectively influenced by the kind of rate increase the Fed could reasonably impose, since they are determined primarily by worldwide supply and demand. Moreover, energy price increases operate in a similar manner as an interest rate increase itself – they make it more expensive to conduct business operations and thus deter economic expansion. Consequently, when energy costs go up, there is an accompanying anti inflationary effect.

- International Trade Negotiations. Among the recent staff changes at the White House was the nomination of Rob Portman to head the Office of Management and Budget. Portman had been the United States Trade Representative, the lead U.S. negotiator in the Multilateral Trade Negotiations (the so-called "Doha Round") now underway. Those talks have been in trouble from the day they started in 2001. The current "drop dead" date is April 30, when the parties

pledged to reach framework for the negotiations. The loss of Portman makes the chances of getting that deal even slimmer than they were before. The President's authority to conclude the agreement runs out in June 2007, and many see Portman's change of jobs to be an acknowledgement that the talks will not succeed by then and that he could serve the country better in another position.

- The National Agenda. Beyond the prosecution of the war in Iraq and taking measures to protect the country from terrorism, there seems to be little left of a presidential agenda for the remainder of his term. Social security reform is dead for now, and the prospects for dealing with rising health care costs are dim at best. While the Congress may resume its debate on immigration reform, it is hard to see how the opposing sides could compromise on a measure that could pass both the House and the Senate. What remains on the table are budgetary and tax issues, which may dominate the remaining months before the mid-term elections. Given all the unfinished business that needs to be addressed, this is a sad commentary on our public leaders.

Looking to some specifics on costs:

- Scrap. The prices for #1 dealer bundles and #1 busheling (Chicago) edged up last month to \$294 per mt. Since August, 2005, scrap prices have "stabilized" within a range of about 15% between \$240 and \$295. While this is volatile by historic standards, it is much less so than the 300% swing between mid 2003 and the last months of 2004.
- Pig Iron and Iron Ore. The spot price for Brazilian pig iron (cif New Orleans) remained unchanged last month at \$265 per mt. Nucor announced that, in June, they would be starting up their second blast furnace in Brazil to produce 200,000 mt of pig iron. Last November, they brought on a similar sized furnace. Meanwhile, a Brazilian producer of pig iron fines is asking for a 14% increase in their 2006 contracts, on top of a 71% increase in 2005.

The Chinese government has opposed increases in iron ore prices charged to Chinese consumers. They have threatened intervention in the negotiations to prevent those hikes in contract prices. In response, the Australian government has warned the Chinese not to intervene. Nonetheless, it appears that prices for Australian ore over \$54 per mt (\$70 for Brazilian ore) are not being accepted.

- Ocean Freight. The Baltic Capesize Index remained steady for the third month at 2865.

- Natural Gas. The Nymex contract price was up last month to \$7.15, an increase of over 10%, but still below the \$7.85 in February and the very high spikes of October-December, 2005.
- Exchange Rates. At this writing, the euro stands at \$1.23, an increase of a cent and a half since last month. The pound was up 2¢ to \$1.775, and the Canadian dollar was up slightly to 87.7¢.

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