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Steel Market Conditions
An Update

When we, at Corey Steel, began sending these letters back in February, 2004, our focus was on the "turbulent and sometimes chaotic" steel market conditions. Then, we and you were feeling ourselves squeezed between the increased prices we had to pay for raw materials and a relentless pressure from our customers to keep our own prices down.

At that time, we were able to pinpoint most of the raw material pricing problems on a single actor – China. That country's entry into the world steel market caused major disruptions in pricing for scrap, coke, ocean freight, alloying metals and many other steel-making components.

What we saw four years ago looks positively tranquil compared with what is happening today. For example, take a look at what we said about some prices:

- Scrap prices had "exploded" to $266 per mt. This month, that price is $430.
- Natural gas prices had "zoomed" to $6.90 per mcf. This month, the price is $10.02.
- In February, 2004, pig iron had gone up by 47% from the year before – all the way to $254 per mt. Today, the price is $520.
- The dollar was at its "weakest level in years"; the euro then cost about $1.30. Today, it takes $1.54 to buy a euro.

Chinese demand is still a cause of many of these price increases. China has become the world's largest steel maker by far. Its production demands scrap, ore, energy and other raw materials for which it must scour world supplies. But, today, a lot else is going on besides the effects of Chinese demand, developments that contribute to our economic woes.

A major new factor is the extraordinary weakness of the dollar. For a variety of reasons – budget deficits, trade imbalances, the low interest rates the Fed is using to combat a slowdown, to name a few – the dollar has been critically wounded. As the largest debtor nation in world history, the United States no longer receives deference to its currency. Simply put, foreign holders of dollar obligations are not so certain that their investments are safe, particularly as our economy has come under strong pressure from the credit crisis.

In this time of uncertainty, it is no wonder that commodity prices have soared. As usual, the price of gold goes up in times like these. But the same is true for other metals and oil. Since most of these commodities are traded in dollars on the world market, as the dollar sinks, those prices will rise, as they have done.

Whatever the causes, we are facing in spades the kinds of pressures we saw in 2004. At that time, we were not intending to be bearers of bad news. Who wants to be the messenger that gets shot, no matter how unfair it might be? No, as we said then, we were recounting the state of the steel market "to provide a framework for our talking about those conditions with you". Today, again, we hope you will join us in seeking realistic solutions to the problems we jointly face.

Here is some more detail on this month's specific cost factors:

- Scrap and Pig Iron. Prices for #1 dealer bundles and #1 busheling (Chicago) crept to within a whisker of their all time records, which were set in November, 2004. Dealer bundles were at $420 and busheling at $430 per mt, increases of over 40% just since last November. Pig iron has set a new record level every month since that same month, and the spot price for Brazilian product (cif New Orleans) is now $520 per mt, up by 27% in four months.

- Natural Gas. Natural gas prices are still far below the Katrina era, but still pretty high by historical standards. Moreover, the trends are ominous. The Nymex contract price this month was $10.02 per mcf, up $1.96 from February. That's a 24% increase in one month and 87% since last September.

- Ocean Freight. These costs eased somewhat last month and are down sharply from the recent past. The Baltic Capesize Index declined by 766 to 8624 in March.

- Exchange Rates. After declining to record levels against the euro recently, the dollar has firmed a bit, despite the lower rates imposed by the Fed. There may be a sentiment that the Europeans and, more likely, the British will be lowering rates themselves to head off credit squeezes. Nonetheless, the dollar sank since last month against the euro ($1.54, up 7 cents) and the pound ($1.99, up 3 cents). The Canadian dollar actually declined a penny to $0.98.

We are always interested in your comments and reactions, perhaps more now than ever, so let us hear from you. As usual we shall post this letter on our website www.coreysteel.com and on the international site, www.steelonthenet.com.