
ASA MATERIALS MARKET DIGEST

DECEMBER 8, 2008

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Published Monthly by the American Supply Association Web: www.asa.net; Email: info@asa.net

MARKET OVERVIEW

Carbon Steel. Three themes currently dominate the carbon steel market: operation cutbacks, layoffs, and falling steel prices. Steel production in the U.S. has declined steadily for 24 weeks, and the current operating rate is just slightly above 50%. Most if not all of the major and not-so-major steel mills have reduced staffing. Flat-rolled pricing has eroded significantly with hot-rolled sheet available for as little as \$600 per ton, down from the July peak of \$900.

Tubular Goods. Oil and gas drilling in the U.S. remains strong, but there has been some slowdown. The U.S. rig count, above 2,000 for the past several months, is now significantly below that level. Opinion is divided as to whether or not this decline is the start of a major slowdown. But some observers see the count dropping to 1,500 by early 2009.

Copper. Prices appear to have stabilized at around \$3,500 per metric ton, far below the \$9,000 peak reached early in this past summer. There is little likelihood of a recovery in copper prices before well into 2009. To make matters worse, the copper scrap market has weakened considerably. But a proposed power grid construction project in China would provide a major shot in the arm not only to the Chinese economy but also to the copper market globally.

Stainless Steel. Demand for stainless steel, both domestic and offshore, has slumped badly. Additionally, alloy prices have been under pressure because of falling nickel prices to which finished stainless steel prices are often geared. Reflecting these conditions, all three of the Stainless Steel Big Three have made sharp reductions in flat-rolled surcharges.

CARBON STEEL

OPERATIONS AND PRICING. As the year 2008 heads for the finish line, the U.S. steel industry can be characterized by three themes: Operational Cutbacks, Layoffs, and Falling Prices. These woes are by no means exclusive to American steel mills. Indeed, it would be difficult to find a steelmaking venue where they were not evident.

Production. As tracked by the American Iron & Steel Institute, raw steel production in the U.S. has been in a steady slide for no fewer than 24 weeks. At the latest count, the

weekly tally of raw steel output was down to 1.348 million tons and the operating rate to 56.5% of nameplate capacity. These figures contrast sharply with the 2008 peak of 2.167 million tons and a 90.8% operating rate during the week of August 16.

The steady decline in U.S. steel output reflects the mills' deliberate efforts to avoid a steel glut in the present downturn. In past industry slumps many steelmakers continued to stoke their furnaces, irrespective of the needs—of lack thereof—of the market. As often as not, this sort of overproduction has led to a steel glut and ruinous price-cutting.

Layoffs. As managements strive to match production to the market's needs, layoffs become inevitable. The downtrend in mill employment got under way in October and became pandemic in November. As is often the case the largest producers such as U.S. Steel and ArcelorMittal led the charge in staff reductions. Arcelor was particularly active in November, making sharp cuts in U.S. steel operations and furloughing 5,000 workers for the holiday season. Any number of mills have followed suit, including among others: AK Steel, Oregon Steel, Atlas Tube, Rocky Mountain Steel, Iosco and 2,444 of the 4000 employees at the Burns Harbor, Indiana mill of ArcelorMittal.

In addition to banked furnaces and pink slips, there is plenty of other evidence of a steel industry slump. For one thing, shipments by service centers recently hit a 10-month low with October volume 22.8% below the year-ago figure. Another straw in the wind came with the premature beaching of five Great Lakes iron ore carriers well in advance of the usual layup date. The vessels were simply not needed by the ore shippers.

Prices. Despite mill managers' strenuous efforts to maintain pricing "discipline," production cuts and staff reductions inevitably lead to lower prices and current market conditions are no exception. Items:

- In early November, hot-rolled sheet was trading at \$760-780 per ton and cold-rolled at \$880-890, reductions of \$50-70 from the prices prevailing two weeks earlier.
- Midway through November, *American Metal Market (AMM)* described the hot-rolled market as being "in freefall." The publication quoted hot-rolled sheet at \$650 per ton with some spot-market transactions closing at \$600. These figures are reminiscent of the \$560 price prevailing in December 2007 just before the steel boom began.
- Plate prices, which had been firm right up to the end of October, started to come under pressure in November, but the market wasn't anything like a fire sale. From October into mid-November, plate prices eased a relatively modest 10%, resulting in a base price of \$1,240-1,260, off from \$1,400 in early October.

In the recent International North American Steel Conference, two speakers expressed different views of the steel price outlook. According to CRU executive Paul Scott, flat-rolled prices will ease somewhat. He sees a price of \$693 for hot-rolled coil in the first quarter of 2009. For the year as a whole, Scott predicts an average price of \$694, about \$180 less than in 2008.

Another speaker at the session expressed a more positive view, arguing that the emerging consumer economies—Brazil, Russia, India and China—“will provide a solid demand base for global steel”—despite current credit problems.

RAW MATERIALS. *Ferrous Scrap.* Toward the end of October the U.S. scrap export business appeared to be going nowhere. Then, after a long period on the sidelines, Turkish scrap buyers stepped up to the plate. *AMM* called the spate of buying a “tsunami” as ships for Turkey loaded up with 500,000-600,000 tonnes of medium-grade scrap at prices ranging up to \$140 per tonne.

But the Turks’ buying binge proved to be short-lived, within a few days the talk was of market collapse, with nary a tsunami in sight. When the dust settled, top grade industrial scrap, which sold for \$900 a tonne in mid-summer, was a memory. No. 1 busheling and No. 1 bundles were being quoted at \$150 or less. The so-called “obsolete grades” such as No.1 heavy melting steel were selling for \$100 with some traders expecting the price to go even lower.

At prices such as these, a lot of scrap dealers would just go fishing. As a consequence, some mills turned to “home scrap” to accommodate their blast furnaces.

While all this was going on, U.S. scrap exports to Asia headed for the tank. Shipments to the Far East, especially South Korea and China, were falling off the chart. The Chinese cutbacks on scrap purchases hinted at a slowing economy. As it turned out, the Chinese industrial complex did need government help in the form of a multi-billion bailout. Beijing, ever aware of potential restlessness among the unemployed, was quick to respond. The government’s newly announced economic stimulus package will run two years and put heavy emphasis on housing and public sector projects such as water supply, electrification, and the worst air pollution on the planet.

TUBULAR GOODS.

Operations. Drilling operations in the U.S, and Canada remained strong and steady through early November. But then there were indications of a slowing, as some market watchers had predicted, In the mid-November report, the U.S. rig count was down by 51 units. This was a real attention-getter. As Logic, Inc. executive Kurt Minnich put it, “Down 50 actually says something. It’s not just 12 here and 20 there. We’re starting to see that a slowing, if not the downturn, is here.” Minnich added that the U.S. rig count could fall by as much as 400 to 500 in the first half of 2009.

A more optimistic note was sounded by the Paris-based International Energy Agency: That organization predicts that the recent drop in crude oil prices is a temporary development—that demand for petroleum isn’t going to end or even slow down. Instead, says the agency, newly emerging consumer economies—China, India *et al*—will push the price of crude up again, possibly to as much as \$100 a barrel within seven years, and \$200 by 2030. All of this, says the agency, argues for an ongoing need for oil-field operations as strong as or perhaps stronger than at present.

Oil Country Tubular Goods (OCTG). In the well supply sector, opinions are divided on whether the current slowing in rig operations is significant. For several months suppliers have been more concerned about OCTG imports from China than about weak demand at home. But with the Chinese economy in at least some trouble, the import threat seems less menacing. But given China's industrial achievements over the past decade, it seems unwise to sell any Chinese enterprise very short.

Maneely. The long-awaited acquisition of Maneely Co. by NMLK, a major Russian steel producer, came unglued in early November after a prolonged and sometimes acrimonious courtship. Maneely is a long-established major producer of tubular goods—standard and line pipe, conduit and a broad line of related pipe products. In the plumbing and piping fields, Maneely is best known for its Wheatland Tube operation.

Maneely has been a wholly owned property of The Carlyle Group, a large and highly respected venture capital firm headquartered in Washington, DC. The initial purchase agreement was signed by the two principals in August 2008.

The acquisition started to look shaky when the Russian firm failed to take some preliminary actions required by the purchase agreement. Additionally, NLMK tried to bargain the price down, insisting that economic conditions (a week before the U.S. credit crunch) had changed. Maneely sued require NLMK to complete the preliminary actions required by November 20. As of early December the litigation continues, with both sides ordered to make further filings no later than December 15.

COPPER

Prices. October was a dismal month in the copper market, some traders saying that it was the worst month ever. When it ended, copper was at \$3,990 per metric ton. This was a far cry from the peak of \$9,000 reached earlier this year. Market watchers attributed the nosedive not only to weak demand, but also to the credit crunch that crippled trading in the red metal and most other commodities.

But as November progressed, October's \$3,900 price started to look like the Good Old Days. As trading resumed, the red metal continued to lose ground, hitting a low of \$3,475 on November 19. No significant recovery had developed by month-end.

Other news pertaining to the red metal reflects severe price erosion. Items:

- According to the Copper and Brass Servicenter Association, warehouse shipments fell again in its latest reporting month. Over-all volume was down 4.2%, with the sharpest losses in pipe and tube.
- Freeport McMoRan, a major copper miner, announced plans to lay off as many as 600 employees, most of them from Arizona. Many of those affected were new hires, added to the work force in anticipation of expanding mining operations, for which plans are no longer urgent.

- At the recent meeting of the American Copper Council the mood was decidedly downbeat. Delegates talked of a market turnaround and slow recovery from the bottom. But no one seemed to know when the bottom would develop.
- The International Copper Study Group has reported a 75,000-tonne copper surplus worldwide. The figure is more than triple the year-ago figure of 22,000 tonnes. In August, always a weak month for copper, the surplus ballooned to 125,000 tonnes.

Scrap. The copper scrap market continues to be roiled. Chinese demand dried up suddenly in early fall, largely as the result of government action. As a result, Chinese importers find themselves having overbought in copper scrap and in many cases have been renegeing on their contracts, driving down the price of scrap and creating serious disorder in the market. Needless to say, all of these broken commitments have led to a welter of bad feeling. And many U.S. sellers no longer want any part of Chinese scrap purchases.

Coupled with these problems and slack domestic demand, scrap prices inevitably weakened. In a recent week the Comex market for No. 1 copper scrap fell 7%, from \$1.47-1.50 to \$1.37-1.40.

Futures. The copper market will receive a strong shot in the arm if a proposed power grid construction contract is approved by Beijing. The work is part of a proposed \$550 billion economic stimulus announced by the Chinese government. The two-year plan would concentrate not only on electrification, but also housing, transportation, and remediation of industrial China's chronic and mephitic air pollution.

STAINLESS STEEL

Pricing and Demand. Stainless steel mills are being hit with a double whammy as (1) demand has weakened badly; and (2) the price of nickel, to which stainless steel prices are customarily geared, continues to falter. Given a prevalence of these two factors, some market watchers are predicting that the price for finished stainless will fall by 50% before then end of 2008.

In our view, such a precipitous drop is unlikely. But stainless prices *are* falling. And all three members of the stainless Big Three—AK, Allegheny, and North American—have pruned their materials surcharges, effective with December shipments. Following are typical reduced surcharges and percent reductions for major types:

Type 304 - 71.43 cents per pound, down 36.4%

Type 316 - 131.66 cents per pound, off 32.1%

Type 201 (nickel free) 60.32 cents per pound, down 32.6%.

Stainless Scrap. – Stainless steel scrap demand continues to languish. Little improvement is expected before the second quarter of 2009, according to the Stainless Steel Committee, an arm of the Bureau of International Recycling. The Committee's conservative estimate is based on a new measure of global stainless consumption in the

coming year, initially forecast at 30 million tonnes but recently revised to 27.2 million tonnes.

PRODUCER PRICE INDEXES – KEY INDUSTRY PRODUCTS

The table below is extracted from the Bureau of Labor Statistics' monthly report on the Producer Price Index or PPI. The Producer Price is defined as the price at which a given commodity or product is sold at its *first* sale after being manufactured, mined, refined or otherwise produced.

	Latest 10/08	Previous 09/08	Year Ago 10/07	2 Yrs Ago 10/06
PIPE, VALVES & FITTINGS:				
Copper & copper-alloy tube	266.3	288.9	321.1	290.2
Steel pipe & tube	224.4	224.8	167.1	168.8
Industrial valves - metal	185.4	185.2	176.1	164.8
Plastic pipe and fittings	231.0	228.5	194.7	214.2
PLUMBING FIXTURES:				
Vitreous china fixtures	97.0	97.0	96.5	101.4
Fixture fittings & trim	237.7	238.2	227.7	214.6
HVAC EQUIPMENT:				
Warm air furnaces	130.0	129.3	127.0	119.1
Unitary air conditioners	151.9	151.9	140.3	138.1
Cast iron heating boilers	146.4	146.4	135.3	128.2

NOTES: 1) Sources: Bureau of Labor Statistics, US Department of Labor; compiled for the American Supply Association. 2) Data for 2007 are subject to revision.

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