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# ASA MATERIALS MARKET DIGEST

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#### **MARKET OVERVIEW**

**Carbon Steel.** No matter how you measure it, the U.S. steel industry is in a steep downhill slide. In October the operating rate fell from 81.4% of capacity to 70.4%. Hot-rolled steel prices have slipped from \$1,100 per ton to as little as \$900. And mills are banking as much as 50% of their productive capacity.

**Tubular Goods.** Oil and gas production in both the U.S. and Canada continue at near-capacity levels. But while demand for oil country tubular goods (OCTG) remains brisk, prices are leveling off after ten months of steady increases. Market watchers attribute the easing of OCTG price pressures to an ongoing flood of imports, especially from China.

**Copper.** October saw the red metal's price take a major nosedive, driven both by lack of user demand and speculative selling brought on by the financial crisis. Copper scrap was equally hard hit as the price for No. 1 grade fell 22.8% in a single trading day. To add to the scrap dealers' woes, Chinese buying, which normally accounts for 67% of U.S. copper scrap exports, appears to have dried up completely.

**Stainless Steel.** Nickel, the alloying agent for most stainless steel formulations, has fallen to a price where some producers have been forced to suspend operations. With nickel costs reduced sharply, stainless steel producers have announced surcharge reductions of up to 14.6%.

**Resins.** Heavy price pressures are being exerted all across the entire resin spectrum. Two major factors weakening prices are: (1) falling monomer and feedstock prices which are moving in synch with the decline of crude oil; and (2) a severe fall-off in demand both domestically where the housing slump continues, and overseas where resin imports have shrunk to a trickle.

#### **CARBON STEEL**

**SUPPLY, DEMAND AND PRICING.** *Operations.* In our October edition we noted that demand for carbon steel had "eased considerably." Currently it would be safer to say that said demand has all but collapsed. The weekly raw steel production figures for U.S. mills tell a grim story:

<b>Week Ending</b>	<b>Output</b>	<b>Operating Rate</b>
September 27	1,986,000 tons	83.2%
October 4	1,942,000 tons	81.4%
October 11	1,869,000 tons	78.3%
October 18	1,744,000 tons	73.1%
October 25	1,680.000 tons	70.4%

Production cuts began with the two major West Coast mills. In late September USS-Posco shut down its No. 1 galvanizing line, a unit normally producing 120,000-140,000 tons of sheet annually. About the same time California steel banked a hot strip line, ostensibly for maintenance, but with no guarantee of a new start-up date. Both of these outages were motivated at least in part by the need to limit production or face an unwanted glut of unsold and perhaps unsalable flat-rolled product.

About midway through October U.S. Steel weighed in by announcing the shutdown of one of its two Canadian blast furnaces, an outage that may last up to two months. According to unconfirmed press reports, Nucor is also said to be reefing sail for what one executive terms a “few days.”

Next to be heard from was AK Steel, something of the maverick among U.S. steelmakers. The company has not announced any intention of cutting output, but it reportedly did acknowledge an inability to “run full-out at 24/7.” Barely a week after an AK spokesman sniffed at the idea of cutbacks, the firm idled its Mansfield, OH rolling and finishing mill. About 350 employees will be laid off when the shutdown is implemented. On an even larger scale, ArcelorMittal has banked four of its nine Chicago blast furnaces for an unstated period.

*Pricing.* It goes without saying that the above described production cuts have been made in an atmosphere of weakening prices. Hot-rolled sheet has been particularly vulnerable. After peaking at \$1,100 per ton in August, this price had fallen to \$960 in early October with some deals closing at \$900. Cold-rolled and galvanized sheet were under comparable pressure and by mid-October both cold-rolled and galvanized were trading in the \$1,030-1,050 range. Even carbon steel plate, which has been in strong demand throughout 2008, saw prices fall from \$1,500 per ton to \$1,390 or less.

Needless to say, the steel industry’s current travails have elicited all kinds of forecasts, dire and otherwise, from market watchers. For example:

- UPS Investment Research sees further price declines and continued demand weakness over the “near-term future.” The steel slowdown which the firm initially expected to end in late 2008 is now forecast to continue into 2009.
- Bargain-basement pricing on flat-rolled steel won’t last forever, according to service center bigwig Wayne Bassett. He expects hot-rolled sheet to form a cyclical bottom of around \$800 toward year-end. Thereafter, Bassett sees the price recovering to \$850 in the first quarter of 2009 and \$950 by the following quarter.

- Industry analyst Tony Taccone told a recent industry meeting that the steel market could stay depressed for as much as four years. In his scenario steel output would decline 10% per month, ultimately resulting in a net loss of 130 million tons, approximately the current annual output of all U.S. mills.

*Other Issues.* While all this is playing out, the American steel industry continues to be a major factor in the economic success or failure of a whole host of subordinate industries. Among these, the steel service centers are currently having the worst of times. From early in October, center operators have been jittery because of falling steel prices. In a number of ways the warehouses are between a rock and a hard place: if steel prices drop, the centers could end up in a ruinous price war. But if prices rise, the warehouse sector is always in jeopardy of sudden price breaks that could leave service centers with an abundance of over-priced inventory. But currently the centers' main problem is a sharp decline in demand with no improvement in sight.

On another front, there are once again indications of a flood of low-priced tubular imports from China and elsewhere. Already the Chinese are reportedly saturating the OCTG market and, as noted in the following "Tubular Goods" section of this report, exerting heavy pressure on drillers' piping supplies.

Additionally, steelmakers continue to worry about ongoing weakness in the automotive market, one of the major buttresses of the steel industry. According to a speaker at a recent *AMM* seminar, the auto market is headed toward of "tsunami" of consolidation that will cut auto output sharply. The speaker predicts vehicle output for the second half of 2008 at an annual rate of 12 million units, down from an earlier forecast of 13 million. Then, in 2009, the output is predicted to sink to *under* 12 million cars and trucks, making '09 the worst auto year in at least a decade.

**RAW MATERIALS.** *Ferrous Scrap.* The price erosion in iron and steel scrap that began in September continued through the month of October. Early on, prices of factory bundles and busheling—both premium grades—skidded to \$400 per long ton, a decline of \$175 in the preceding three or four weeks.

By the end of October, scrap prices had reached levels that market watchers were describing as "ridiculous" or "silly." As an example of the current scrap climate, *AMM* cites two mini-mill purchases of shredded scrap and busheling at \$130-140 per ton, \$100 less than the same purchase would have fetched earlier in October. And demand for premium-grade factory bundles has essentially vanished.

The scrap market's near-collapse has strongly impacted pig iron pricing. From a July peak of \$970-1,000 per metric ton, the going rate has slipped to \$500-520 with some sales reported at \$470 per tonne.

*China's Problems.* Adding to the domestic scrap market's woes has been a virtual cessation of Chinese buying. Normally, China's voracious appetite for ferrous scrap has kept U.S. exporters busy and profitable. But even as in the case of the U.S. industry, China's steel industry

is experiencing hard times. Recent reports tell of banked furnaces, slow payments to suppliers, and even a few bankruptcies.

Underlying these difficulties is a sharp slowdown in Chinese construction activity. Additionally, government efforts to cool the overheated Chinese economy have forced cutbacks in steel markets other than the construction industry.

Chinese scrap importers have been hard hit by the steel cutbacks. Indeed, at a recent meeting of the Bureau of International Recycling, there was visible bad blood between scrap sellers and their Chinese customers. *AMM* reports tell of Chinese scrap buyers renegeing on contracts, refusing deliveries, and/or failure to pay for delivered shipments. Terms such as “reprehensible” and “inexcusable” are being used to describe bad-faith efforts by importers to evade their obligations.

## **TUBULAR GOODS**

*Operations.* Drilling in North American oil and gas fields continues at full speed. During October, operations on American sites involved rig counts ranging from 1,964 to 2,018, 11-13% ahead of the comparable periods in 2007. In Canada the rig counts varied from 431 to 470 and topped the year-ago levels by 30-37%.

*OCTG Pricing.* After ten consecutive months of rising prices, the OCTG market softened in late October. According to Pipe Logix, Inc., the industry’s top analyst for piping economics, the average price for a ton of OCTG fell 1.6% from \$3,220 to \$3,170. Pipe Logix and other source attribute the slippage to a new flood of OCTG imports, mostly from China; a seasonal pattern that normally sees slowing OCTG in the final three months of the year; and the widespread decline in steel prices which directly affects the cost of almost all OCTG products.

The table on the following page shows OCTG prices for a representative sampling of products. The prices are averages for a ton of product f.o.b. the Houston Oil Patch.

**(Price chart appears on the following page)**

**Representative OCTG Prices (per ton)**

<b>Product</b>	<b>Oct 2008</b>	<b>Sep 2008</b>	<b>Sep-Oct % Chng</b>
Tubing: Carbon ERW	\$2,943	\$2,982	-1.3%
Tubing: Carbon seaml's	\$3,354	\$3,346	+0.2%
Tubing: Alloy ERW	\$3,383	\$3,367	+0.5%
Tubing: Alloy seamless	\$3,624	\$3,625	0.0%
Casing: Carbon ERW	\$2,808	\$2,853	-1.6%
Casing: Carbon seaml's	\$2,507	\$2,480	+1.1%
Casing: Alloy ERW	\$3,325	\$3,439	-3.3%
Casing: Alloy seamless	\$3,487	\$3,460	+0.8%

Source: Pipe Logix, Inc., Santa Fe NM

With respect to OCTG imports from China: In the August-October period, average monthly OCTG imports to the U.S. rose to 290,022 tonnes, up from an average of 187,694 tones per month in the preceding two quarters. China was the major factor in this influx, with its three-month average OCTG shipments of 182,679 more than double the preceding three-month average of 91,030 tons.

*Other News.* The widely publicized merger of John Maneely Co. into the Russian steelmaker NLMK has hit the skids, at least temporarily. The Maneely firm, now owned by the Washington-based Carlyle Group, is best known in the piping industry for its Wheatland Tube pipe and tube subsidiary.

A merger of the above-named principals was negotiated months ago, and the deal was set to close on September 29. But as late as October 15, the Russians had failed to act on certain obligations expressed in the merger agreement, and Maneely sued. As plaintiff it sought a bench order compelling the Russians to comply with all provisos of the merger agreement. At this writing Maneely interests insist that the deal hasn't been irreparably harmed and that the lawsuit will persuade NLMK to complete the closing.

**COPPER**

*Commodity Trading.* Along with nickel and other base metals, copper took it on the chin in the recent credit crisis. Amid non-stop reporting of financial calamity, investors and speculators

alike joined the “flight to quality.” Panicky selling developed as few investors opted to stay long on “things” (including copper futures) for a moment longer than necessary. On the metals exchanges copper prices nosedived. Following are the red metal’s October statistics in trading on the London Metals Exchange:

Open (October 1)	\$6,381.00
High (October 1)	\$6,381.00
Low (October 27)	\$3,709.00
Close (October 30)	\$4,500.00

While the month’s trend was decidedly downhill, the red metal staged a few brief rallies. But with demand deep in the doldrums, there was little chance for a significant recovery beyond the closing price.

Even when copper prices return to a semblance of normal, the news won’t be all good. In a recent report, the International Copper Study Group reports that global demand for the red metal is on the wane and that the current global copper surplus of 275,000 tonnes is here to stay for a while. Indeed, the Group predicts that if copper production continues as scheduled, the surplus could reach 800,000 tonnes in another year or two.

*Copper Scrap.* As the recent financial crises seemed to worsen, the woes of the copper scrap market multiplied. Midway through October *AMM* was describing the situation using such quotes as “It’s a disaster out there,” and “The bottom has fallen out” and “Nobody is quoting prices right now.” What prompted such remarks was essentially a shutdown of the domestic scrap market coupled with a complete cessation of Chinese buying. The market climax came when prices for No. 1 ingot maker’s copper scrap fell 22.8% a single trading day—from \$2.56 per pound to \$1.90. But even at the rock bottom price, there were no Chinese buyers.

*Light in the Housing Tunnel?* Amid all the business gloom and doom, there is a faint beam of light involving the home building industry. Housing, of course, has been at the root of the current financial crisis, and a full business recovery won’t happen until home building gets back on its feet. Fortunately, there appear to be signs that housing has entered the early healing stage. Items:

- **New Home Construction.** The late home building boom peaked in 2005 when some 2.1 million new houses were built. In each successive year the construction pace weakened until in 2008, a mere 800,000 houses are being built—just 38% of the grossly overbuilt 2005 total of 2.1 million. This year, for the first time since much earlier in this decade, new-home demand equals and may actually *exceed* supply.
- **Affordable Home Prices.** Single-family home prices have fallen 30% since the peak in 2005. What was a \$250,000 house in 2005 can now be had for \$175,000.
- **Manageable Household Debt.** Total household debt obligations—mortgage, insurance, etc.—as a percentage of household income is at the lowest level since 1995.

From a 2002 peak of 33%, household obligations have fallen to 26% of disposable income, a substantial improvement in housing affordability.

None of this is to say that a housing boom is going to start next week. But most signs suggest that the worst of the housing crisis is over, and that a recovery is under way, albeit slowly. Over time this is likely to contribute to a higher home building rate and the consequent increase in demand for copper and a wide range of other home building materials.

## **STAINLESS STEEL**

*Commodity Trading.* As in the case of copper, nickel is often subject to price fluctuations above and beyond the needs of end users. The figures below largely reflect speculative buying and selling rather than any sharp fluctuations in user demand.

Open (October 1)	\$16,200.00
High (October 1)	\$16,200.00
Low (October 24)	\$ 9,025.00
Close (October 30)	\$12,810.00

*Production.* Commenting on the wild swings in nickel prices, one analyst quoted by *AMM* sees the bear market persisting for another year. Whether or not this forecast is fulfilled, the current \$12,000 price is well below the estimated cost of \$15,000 to mine and refine a tonne of nickel. Given this disparity, some market observers conclude that nickel producers may have to reconsider proposed new mining projects and/or expansion of existing sites. In fact, at least one nickel producer shut down recently because of plunging market prices. Ceasing operations for an indeterminate period is the Levack plant of FMX Mining Co., an integrated facility located in the mineral-rich Sudbury Basin in Ontario.

Bear market or not, a major new nickel and copper mining facility is under construction in Marquette, Michigan. Developing the new mine is Kennecott Eagle Minerals, a subsidiary of Rio Tinto. The project had been delayed repeatedly by bureaucratic foot-dragging on the part of various state and federal authorities, but the project has finally been given a green light, however grudgingly, by the necessary authorities.

Reflecting current and prospective mine closures, the International Nickel Study Group has trimmed its 2008 production forecast from 1.43 million tonnes to 1.41 million. But in 2009 the Group expects mine production to rise to 1.55 million tonnes and consumption to increase proportionally.

*Stainless Prices.* With nickel prices down, a new round of stainless steel surcharge reductions was inevitable and was recently announced by members of the Stainless Steel Big Three. The following quotes from Allegheny Technology's new price sheet are representative of the reduced surcharge pricing:

Type 304, down 13.3% to \$1.123 per pound;  
Type 316, down 9.4% to \$1.94 per pound;  
Type 201, down 14.6% to 89.51 cents per pound.

## **RESINS**

According to the current issue of *Plastics Technology* ( *PT*), resin prices continue to fall. Most formulations have been hit by a new double whammy, this one consisting of weak global demand coupled with falling monomer and feedstock prices. The effects on some representative resins are as follows:

**Polyethylene.** September shipments were down seven cents a pound and further price declines are a distinct possibility. Exports to Pacific Rim destinations have essentially vanished while South American orders are weakening.

**Polypropylene.** After a modest 2-cent drop in August, PP pricing fell out of bed with September quotes off 15-20 cents per pound and no expectation of higher prices any time soon. *PT* characterizes the market as “moribund.”

**Polyvinyl Chloride.** PVC remains a prisoner of the housing slump which (see p. 6) is in the very early stages of a slow and uncertain recovery. While it develops, PVC suppliers expect that further price cuts for both resin and feedstocks will be announced before year-end.

**Polystyrene.** Spot benzene prices have nosedived to \$2.50-2.60 per gallon, far below the contract level of \$4.24. As a result, PS resin prices have fallen another 5-7 cents in the current reporting period.

**Polyesters.** After a 4-cent drop in October, one market watcher quoted by *PT* cautions sellers and buyers to “ expect prices to soften at least 8 cents more by the end of the year.”

**(Producer prices appear on the following page)**

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## 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 09/08	Previous 08/08	Year Ago 09/07	<sup>2</sup> Yrs Ago 09/06
<b>PIPE, VALVES &amp; FITTINGS:</b>				
Copper & copper-alloy tube	289.9	319.1	311.7	316.9
Steel pipe & tube	224.8	227.6	167.0	165.3
Plastic pipe and fittings	228.5	227.9	196.1	217.3
Industrial valves – metal	185.2	184.9	175.4	162.1
<b>PLUMBING FIXTURES:</b>				
Vitreous china fixtures	97.0	97.0	103.6	101.4
Fixture fittings & trim	238.2	237.4	227.2	212.8
<b>HVAC EQUIPMENT:</b>				
Warm air furnaces	129.3	130.7	127.0	119.1
Unitary air conditioners	151.9	151.9	140.3	138.1
Cast iron heating boilers	146.4	145.3	135.3	128.2

NOTES: 1) Sources: Bureau of Labor Statistics, US Department of Labor; compiled for the American Supply Association. 2) Data for 2008 are subject to revision.

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