

AIST 2010 President's Award Breakfast

Keynote Address

John P. Surma, Chairman and Chief Executive Officer, United States Steel Corporation
May 4, 2010 • Pittsburgh, Pennsylvania

AIST President Anthony Bridge presented John P. Surma with the 2010 AIST William T. Hogan, S.J. Lecture Award in appreciation for his keynote address, "Steel Trends 2010: What Would Father Hogan Say?" Surma spoke before a crowd of 1,200 people at the AISTech 2010 President's Award Breakfast in Pittsburgh, Pa., USA, on May 4.

Thank you, President Bridge. We know the AIST president very well at U. S. Steel, and I think everyone here would like to thank you for putting on another fantastic AISTech conference. Thanks and congratulations to executive director Ron Ashburn and the AIST board for your outstanding stewardship of this important organization, and congratulations to all the award winners who have been recognized. Your contributions to our industry are so vitally important.

When Tony asked me to give this address, he was, as usual, very gracious. He gave me a choice of topics to cover. He said I could comment on either: (a) "2010 Steel Trends" or (b) "A New Method to Study the Effect of Cooling Rate on the Decomposition of Austenite in Advanced High-Strength Sheet Steels."

I told him that, in the interest of time, I'd better stick with the less technical subject, so here I am, talking about business trends for our sector. To be perfectly honest, the technical side of the business is always better left to the experts, like my cousin, Dr. Anthony DeArdo from the University of Pittsburgh, who just moments ago received the Benjamin F. Fairless Award.

Continuing with the trend of continuity, you will note that my colleague, our company's CFO and my Mt. Lebanon High School classmate, Gretchen Haggerty, will participate as a panelist at the Town Hall Forum tomorrow morning. While this is her first appearance as a panelist, I would call her a legacy participant, since her late father,

Russ Robinson, served as the public relations director and organizer of this event throughout the '70s and '80s.

I am proud that AIST has long been – and continues to be today – a valued and valuable resource for the steel sector. The statistics and accomplishments that Mr. Ashburn just reviewed made that so clear.

AIST helps each of us in the steel sector understand both the macro and micro issues we face. The association offers us not only critical information, but also practical ideas on how to deal with those issues. For these and many other reasons, we all owe a debt of gratitude to AIST, and it is my sincere honor to offer these comments to this conference this morning.

Now, having said all that, let me start out by telling you how envious I am of a certain individual you just heard about and perhaps some of you may even have known – the late Father William Hogan.

This one-time employee of U. S. Steel earned a doctorate, having written a dissertation on steel production. He taught at Duquesne University here in Pittsburgh, as well as at my alma mater, Penn State, and at Loyola, Purdue and Fordham. He counseled five different American presidents on steel, trade and tax policies. He became a worldwide, highly respected resource on all matters steel-related. And perhaps most unfairly of all, and for this reason alone I could envy him, he had a full head of shocking red Irish hair.

Father Hogan was the "Steel Priest," a longtime friend of our company and this organization and in whose memory I will be accepting the AIST William T. Hogan Lecture Award today.





Figure 1 – John Surma presents his keynote address.



Figure 2 – The “Steel Priest,” Father William T. Hogan.

Father Hogan saw, studied and documented the rise, fall and rebirth of our great sector. He wrote volumes on our business that survive today in a special archive named for him at Fordham.

Yet for all of his academic achievements and impressive credentials, Father Hogan was, more than anything else, a realist. He understood industry, the means of production, the need for profit, and the interdependence of different industries to keep the overall economy strong. That’s why his name evoked such respect and his ideas commanded such eager acceptance among leaders of both industry and government.

This sector needs to apply – and I believe we are – the same kind of reality-based, sober strategies driven by business principles, as Father Hogan championed during his long life and illustrious career. And from my perspective, that’s a very good thing.

Here’s what I mean. Last year at this time, we all thought the world was about to end. It didn’t. The dark times will come – they always do – but so do the brighter times. I think we are headed for the light again. It may take a while longer this time before it gets to be brilliant sunshine, but it does appear to be getting lighter.

How so? First of all, our sector has good leadership, which means we should come out of this period better than in previous downturns. Let’s not forget that this downturn was not of the steel sector’s making. Rather, we were swept along with everyone else when the entire economy began to swoon. Everyone has struggled – the steel sector, our customers and our suppliers. All have made sacrifices, and we all have suffered through it together.

In prior downturns for our sector, we hit hard times, but the overall economy was still good. This time, our sector was strong, but the

overall economy went bad. We’ve already gone through a good bit of restructuring earlier in the decade, so we are better prepared, and we better managed to come out of the abyss quicker than in other downturns. We continue to believe at U. S. Steel that the national and world economies are in the early stages of recovery, although we’re being practical about our expectations on how long this particular recovery will take.

At our company, all of the steps we took early in this decade to improve our focus, cost position and productivity resulted in improving our overall competitiveness. And the consistent, strong financial performance that has resulted from this has allowed us to



Figure 3 – Raw materials and today’s steel industry.



do a number of things to strengthen our company further, one of those being increased capital spending.

We have chosen to invest in rebuilding and upgrading our existing steel industry infrastructure in the United States and Europe. From 2005 through 2007, we spent more than \$2 billion on capital expenditures across the company, with nearly half of that on our flat rolled segment in the United States. A large portion of that investment has been directed to our coke, iron and steel producing operations to improve efficiency and reliability while reducing energy usage and CO₂ emissions.

And here's another reason for the steel sector to feel good about ourselves as this important recovery develops. Despite difficult business conditions, safety remained our collective top priority. None of us cuts corners when it comes to safety, and that's a tremendous complement to each of you, your leadership and your employees. At U. S. Steel, besides being driven by top-down leadership, we believe in a bottom-up process with our represented workforce that engages their thoughts on the new safety best practices and programs. Working in this cooperative manner with our labor unions – including the United Steelworkers in North America – reinforces our belief in the safety process. And I imagine similar programs are in place across our sector.

Again, it's a wonderful thing to be able to say – even amid these terribly challenging economic conditions – that this sector never even thinks about cutting costs or corners when it comes to the safety of our people.

So, taking a snapshot of the past 18 months, what would Father Hogan say? I believe he would confirm that we had made the tough decisions and taken the strategic actions needed to lift the steel sector back toward a positive position sooner than many would have thought possible.

But what about today? What current mega-trends affect our sector's ability to return to the promised land of sustained profitability?

We all know the answer: raw materials are the new dynamic influencing how these markets operate. Costs to purchase nearly all iron and steelmaking raw materials have risen dramatically. Fully 70% of steel sector costs are devoted to raw materials and energy today. Many companies don't own their own raw material, which means that, as raw materials costs go up, our sector may be claiming less of the total economic value created by steel.

Did you know that more value creation exists today from the blast furnace back to the source of the raw materials than from the blast furnace forward to the end product? This is a complete reversal of conditions from 30 – or even 10 – years ago. For that reason, we as steel producers must be aware of the need to increase the value we create to provide raw materials suppliers a reasonable market and end-users a profit on their steel consuming products.

The world's three largest iron ore miners account for nearly 70% of the world's seaborne-traded iron ore market. Two of the companies announced plans last year to create a joint venture that has been opposed by some steelmakers around the world, particularly those that depend on the seaborne trade for a substantial portion of their iron ore requirements. The issue, of course, is that the raw materials industry is highly concentrated. Suppliers have opportunistically enjoyed significant pricing power for several years and, if anything, this power is increasing.

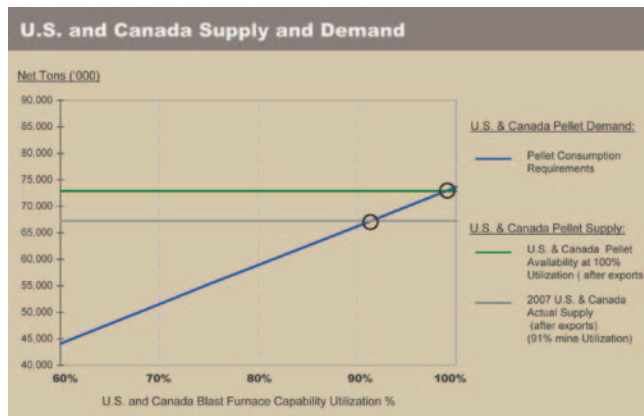


Figure 4 – U.S./Canada pellet balance analysis.

China's high demand for imported iron ore is also a contributing factor in driving up ore prices globally and stimulating cost-driven price increases in steel products worldwide. The degree to which a steel producer is integrated with captive iron ore mines (and to a lesser extent metallurgical coal) dictates how much economic value can be captured from this new dynamic. That means those mills with higher open-market purchases of raw materials, and therefore exposure to spot prices of iron ore in their cost structures, are playing catch-up and in some cases losing value as market prices lag the run-up in raw materials costs.

So, rather than ore playing the role of enabling steel production to create end-market value, steel is playing the role of a conduit for miners to harvest value of their ore in the marketplace. This explains my comment earlier about the shift in where the most value is created in the entire production process.

China's immense appetite for higher-quality ores from Brazil, Australia and India (628 million tonnes in 2009 and 59 million tonnes in March 2010) creates a huge pull by itself.

However, there may be a silver lining here for some in our sector – like North American integrated producers. Here's why. Most of the anxiety over raw materials exists among producers in Asia and Western Europe, but not so much among those in North America, because the balance of resources is better here.

Figure 4 shows that the 34 blast furnaces in the United States and Canada, when operated at a 90% utilization, require about 67 million tons of pellets. The mines in the United States and Canada can produce about 93 million tons of pellets and can supply this 67-million-ton demand level comfortably, even after normal export levels of 15–20 million tons. North America, as a continent, is in a decent position with good relative balance, and similar conditions prevail for metallurgical coal.

At U. S. Steel today, we are largely self-sufficient for our North American iron ore needs and about 80% self-sufficient for our coke needs. In Europe, we contract for needed supplies in both. We are not directly subject to the seaborne price changes affecting many Asian and Western European steelmakers, but we will certainly feel the effect to some degree. We're also taking steps to expand our capabilities in this area by investing in our existing facilities and exploring acquisitions and joint-venture opportunities when appropriate.



Figure 5 – A shared environment.

As an added bonus, due to shale gas availability made possible through the Marcellus Shale deposit, among others, the North American steel sector’s natural gas position appears slightly more favorable than much of the rest of the world.

So, examining the effect of raw materials and associated costs on our sector’s ability to achieve and sustain profitability over the immediate horizon, what would Father Hogan say?

I believe he would be encouraged by the North American competitive advantage based on a more balanced level of access to these materials, but at the same time encourage steel producers to always keep a strategic eye on the long-term – by always looking for greater efficiencies, actively searching for new sources of raw materials, and leveraging every opportunity to keep the cost of needed materials as reasonable as possible.

Beyond the question of raw materials, other public policy matters continue to touch the steel sector. Here, AIST serves a vital function in helping our sector identify, analyze and promote those key manufacturing issues affecting us. I returned last night from a joint annual meeting of AISI and MSCI, where we discussed matters such as currency reform, the rebalance of trade, the AISI Manufacturing

Initiative, and establishing a feasible, reasonable and logical energy policy that includes nuclear, clean coal and natural gas.

We continue to hear how the Obama Administration plans to pursue its “Cap and Trade” approach in the U.S. Senate, following the House of Representatives’ passing of a similar bill last year. While the steel sector believes in reducing our environmental impact, the question remains: Will Cap and Trade, or something like it, really protect the environment?

Our sector can take just as much justifiable pride in the tremendous progress made in reducing our environmental impact as we can in our safety record, which I talked about earlier. As an industry, we have reduced the energy it takes to make a ton of steel by 29%, or roughly one-third, since 1990, thanks to all the extraordinary work you and your colleagues have done to make that happen. Steelmaking contributes only about 3% of greenhouse gas emissions globally. In the United States, our industry’s contribution is less than 2%.

This underscores America’s status as having some of the cleanest-running industrial technology and toughest waste emissions standards in the world. By the same token, carbon is absolutely essential to the integrated steelmaking process. While we are working on developing new ironmaking technologies, it will likely be many years before such technology will be deployed at scale.

With this in mind, our priority is to find ways of reducing global CO₂ emissions and avoid merely shifting production and our jobs to countries with lower environmental performance – the very definition of Cap and Trade legislation – which would have the perverse and foolish effect of dismantling strategically important and competitive industries like steel, increasing global CO₂ emissions and putting thousands of Americans out of work. Who votes for that policy? We commend our local congressmen, Mike Doyle, Jason Altmire and Tim Murphy, for their work to maintain our local manufacturing base as we deal with these environmental concerns.

The fact is, environmental stewardship is a core value at U. S. Steel, and we continue to invest millions of dollars annually to meet and exceed increasingly rigorous requirements. We also support efforts by groups such as AIST, AISI, the World Steel Association, Eurofer, the Asia-Pacific Partnership and others to develop cutting-edge technologies that will aid efforts by all steelmakers to meet whatever regulations may ultimately be adopted in the future. Again, I have no doubt Father Hogan would agree with this view.

Looking forward to the second quarter, we recently indicated that we anticipate being profitable in all three of our operating segments – flat rolled, U. S. Steel’s European operations and tubular. Gradually improving business conditions – including reports that customer inventories remain low across all segments – should be reflected in our operating results, most notably in flat rolled. Our production levels should continue to increase due to the healthy order rates we are experiencing in most of our end-markets. We remain cautiously optimistic in our outlook. Figure 6 illustrates a few reasons why.

As Figure 6 indicates, apparent demand in the United States has remained relatively steady at roughly 125 million tons for nearly 15 years, with imports at about 25 million tons to make up the difference between our industry’s production and material consumption. For nearly two decades, U.S. companies have produced about 100 million tons and operated at about 85% utilization. While the numbers fluctuated slightly over time, they never got far from that 125-ton mark. Then came the financial crisis of late 2008, followed

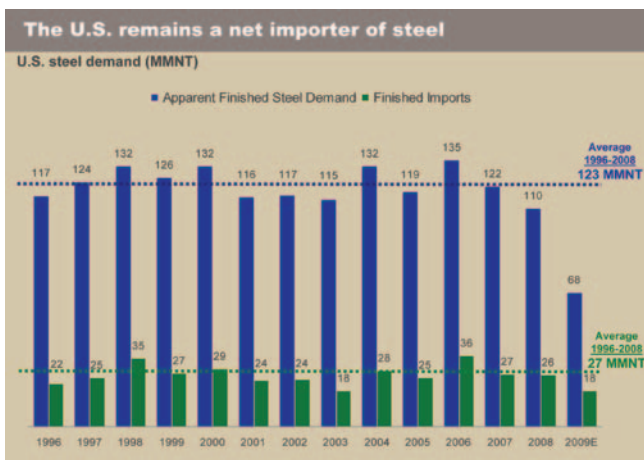


Figure 6 – U.S. demand and imports.



quickly by the recession that extended throughout 2009. What was the result of these truly historic events on our industry? A roughly 45% decrease in U.S. demand based on the trend.

From Figure 7, you can see what that translates to, on a per capita basis, for both total steel and flat rolled steel consumed. In normal times, according to the World Steel Association, apparent finished steel use in the United States ranges between 360 and 405 kg per person, with sheet making up about half of the total. In 2009, however, that figure plummeted to 187 kg per person – roughly equivalent to the average annual rate of consumption in Romania.

Some experts say this is the “new normal.” Well, it may be the normal for Romania, which is all well and good. Romania’s a fine nation. But the United States does not operate at the same level of expectation as Romania, which means that, if this is normal, we have a major issue. We expect a higher standard of living. If this is normal, all of us should be very concerned.

The dramatic decline in steel consumption last year was not the result of something our industry did or didn’t do. This decline was caused by a recession of historic proportions. Our view is, no matter the market trends in the past, steel consumption always returned to the trend line over time. You can check that back as far as 1930. Thus far, there is nothing to suggest that demand won’t return in time. It will just have further to go and may take more time than usual.

Today, steel – our remarkable material – still remains the best material available for building a modern world. Steel is essential to meeting mankind’s basic human needs: food, water, shelter, transportation and energy. U. S. Steel alone manufactures more than 1,500 different types of steel, each designed with special attributes tailored to the ultimate application.

My message to you today, from our perspective as a company, as a member of the steel sector, and as a participant in the greater domestic and global economy, is that a return to a true “normal” should be our goal. We have a lot of work to do to get there, but we should not be content with where we are today.

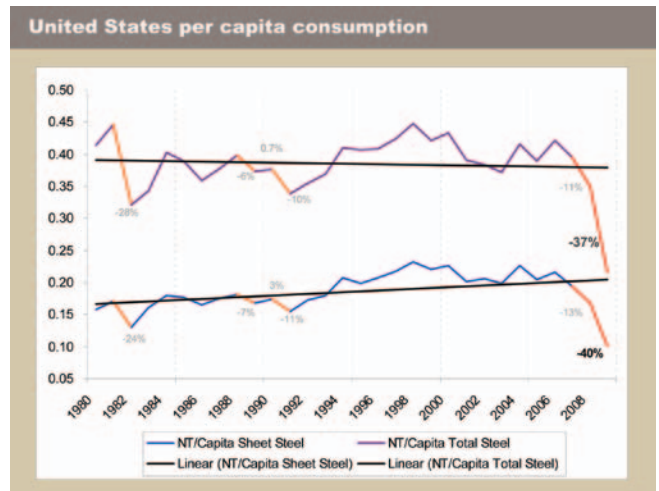


Figure 7 – Steel consumption trends.

It was said of the “Steel Priest,” Father Hogan, that “he had shrewd insight into the directions available to the industry in the shifting circumstances of supply and demand and in times of fierce international competition.” What was true of his day remains just as true – maybe even more so – for each of us today.

It is my hope that everyone here, and all leaders across our industry, continue to approach the noble pursuit of our steelmaking business with the same level of integrity, dedication to the truth, and pursuit of excellence that Father Hogan called on us to embody.

So, in the end, what would Father Hogan say about steel trends in 2010? I believe he’d say, “Well done, but why are you sitting around talking about it? Get up! Get going! There’s a new day and we have steel to make.”

Thank you very much for your attention. ♦



A crowd of 1,200 gathered for the President’s Award Breakfast in Pittsburgh, Pa., to hear U. S. Steel chairman and CEO John Surma’s keynote address.