

World Steel Dynamics (WSD) is a leading steel information service in Englewood Cliffs, N.J. WSD's steel experience, steel database and availability of steel statistics are the principles for performing steel forecasts, studies and analysis for international clients. WSD seeks to understand how the "pricing power" of steel companies the world over will be impacted by changes in the steel industry's structure. To submit your questions for WSD, e-mail WSD@aist.org.



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Q: Currencies, much like stock markets, have experienced relentless volatility over the last several months. What effect, if any, do currencies have on steel pricing?

A: Currency shifts strongly impact steel prices on the world export market. For example, when a steel mill's costs are fairly low, and then its currency weakens versus the U.S. dollar, the mill typically becomes far more price-aggressive on its export offerings if there is excess capacity in its home market. We are witness to this combination of factors at present for the steel mills in Russia, Ukraine and India.

WSD's World Cost Curve assessment indicates, for example, that the operating cost to produce hot rolled band in September 2008 at a Russian steel plant, with its own raw material supply, was about \$440 per tonne when the ruble was 24 per U.S. dollar. The mid-March 2009 cost is estimated at \$300 per tonne with the ruble at 35 per U.S. dollar. (Note: These cost estimates assume a high operating rate.)

Currency is also one of the reasons why WSD believes that the Indian steel companies may be among the best performers in 2009. Among other factors supporting a better year for Indian steel producers than most others may be that:

- Steel demand in India may decline only slightly this year.
- The leading steel mills have access to low-cost iron ore.

- The leading steel mills with blast furnaces will be purchasing coking coal from Australia at a much reduced price.

Q: China, unlike other parts of the world, does not appear to be curtailing steel production to any significant degree. In fact, production has risen during Q109 as compared to the same time period in 2008. Does WSD view this as a sustainable phenomenon?

A: The Chinese steel industry outlook for 2009 is very much "up in the air," just like a bubble. This year, WSD forecasts that Chinese steel production may amount to only about 475 million tonnes, notwithstanding the annualized production rate of 514 million tonnes for the first three months of the year. Production in 2008 amounted to 500 million tonnes.

Steel demand in China may decline about 5% in 2009 because the Chinese economy is suffering from the bursting of three bubbles:

- Fixed asset investment (FAI) in real estate, which accounted in 2008 for about 25.5% of overall fixed asset investment in the country.
- Fixed asset investment by manufacturers seeking to expand capacity. Manufacturers in 2008 accounted for about 32% of fixed asset investment.

China Apparent Steel Products Consumption Analysis (million tonnes)

	2006	2007	2008	2009e	
				FAI 12%	FAI 8%
Railway products	3.26	3.20	3.93	4.8	4.8
Large section	7.34	5.71	6.45	6	5.8
Middle and small section	23.35	26.80	29.23	27.2	26.9
Bar	35.62	41.98	40.71	37.7	37.4
Rebar	79.36	95.22	95.95	92.1	90
Wire rod	66.67	73.66	75.70	72.7	72
Super heavy plate	2.83	3.52	3.80	3.52	3.3
Heavy plate	12.34	15.11	18.64	17.2	17
Middle plate	22.19	27.02	30.60	28.3	27.8
Hot rolled thin sheet	4.66	5.61	4.98	4.8	4.7
Middle thick HR strip	42.15	57.61	66.23	62.3	62
HR thin wide strip	16.34	17.06	19.63	18.5	18.4
HR narrow strip	35.76	39.00	35.86	33.7	31
CR thin sheet	13.39	15.61	16.13	15.2	15
CR thin wide strip	15.14	19.24	18.34	17.2	17
CR narrow strip	4.30	5.81	6.24	5.9	4.8
Coated sheet or strip	15.40	17.78	18.04	17.2	17.2
Colored sheet or strip	2.06	2.22	1.11	1.2	1.2
Electrical sheet	4.02	5.03	5.32	5.3	5.3
Seamless tube	13.02	14.76	14.64	14.2	14.2
Welded pipe	16.99	18.69	20.69	19.9	18.8
Others	6.16	5.35	5.93	5.6	5
Total*	442.35	515.99	538.15	510.4	499.6
		16.6%	4.3%	-5.2%	-7.2%

* Including double counting in production. e = estimate. Source: WSD estimate.

- Exports of manufactured products. These exports in 2008 accounted for about 34% of GDP and, perhaps, about 20% of GDP on a value-added basis.

A negative indicator for fixed asset investment in China is the declining foreign direct investment (FDI) in China over the past five months. WSD forecasts the following based on the mid-case scenario:

- Real GDP growth in China in 2009 may rise only 3–4%, if that.
- Fixed asset investment growth will be up only about 8%, despite a possible 45% increase in investment in infrastructure. Investment in real estate may decline 10%, and investment by manufacturers may also decline 10%.
- Apparent steel demand in 2009 may fall about 5%.
 - On a market basis, there may be declines of 7% in construction, 10% in shipbuilding and 11% in manufacturing.
 - On a product basis, there may be an 8% drop for sections, 8.5% for plate and 7% for sheet products, and 7.4% for rebar, despite the surge in infrastructure spending.

Fixed asset investment, not consumption, is the key to the Chinese economy because it amounts to at least 45% of GDP. A

slowdown in the growth of fixed asset investment is a big problem because FAI has lots of “multipliers” attached to it. For example, more fixed asset investment = more manufacturing capacity = more jobs. Household consumption expenditures, which amount to about 48% of GDP in China, are not believed to be a sizable economic growth driver because so many of the people are so poor. In Western China, where the government is boosting its efforts to add to income, the average income of a worker may be just \$80 per month; hence, such stimuli as the recent tax credits on the purchases of appliances and small tractors may not significantly impact the overall economy.

China’s situation is the opposite of that in the United States, where FAI is only about 14% of GDP and consumption amounts to about 70% of GDP. In the U.S. case, a sharp recovery of consumer spending would have a much greater impact on the economy. Unfortunately for the States, the low ratio of FAI to GDP means that the underlying growth rate of the economy is probably no more than 2% on a long-term basis. ♦

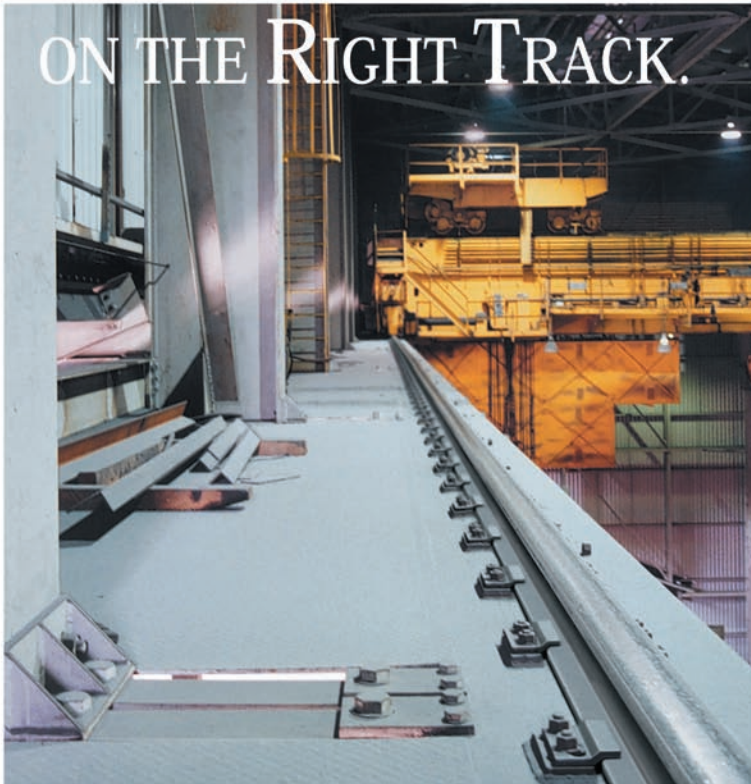
– *Peter F. Marcus*, managing partner, World Steel Dynamics, pmarcus@worldsteeldynamics.com, (201) 503-0902

– *Philipp Englin*, manager – special projects, World Steel Dynamics, penglin@worldsteeldynamics.com, (201) 503-0908

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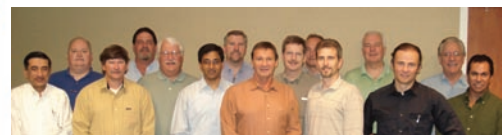
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