

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.



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## Q. What type of steel industry environment does WSD forecast for 2012?

**A.** Apparent steel demand seems likely to be disappointing in early 2012. Steel buyers may not be interested in adding to inventory because they perceive the steel mills' costs will be falling. Current economic indicators in the advanced countries are quite negative, and demand growth is temporarily gone in India and the Middle East. China's economic indicators, as WSD reads them, are signaling the possibility of a temporary sizable decline in the country's economic growth rate due to far lower export growth and tightened monetary conditions (which are forcing steel traders to pay 18–36% to borrow from private sources because their access to low-cost bank loans is diminished). Lower oil prices may dampen the economic growth rate for the Middle East and Russia.

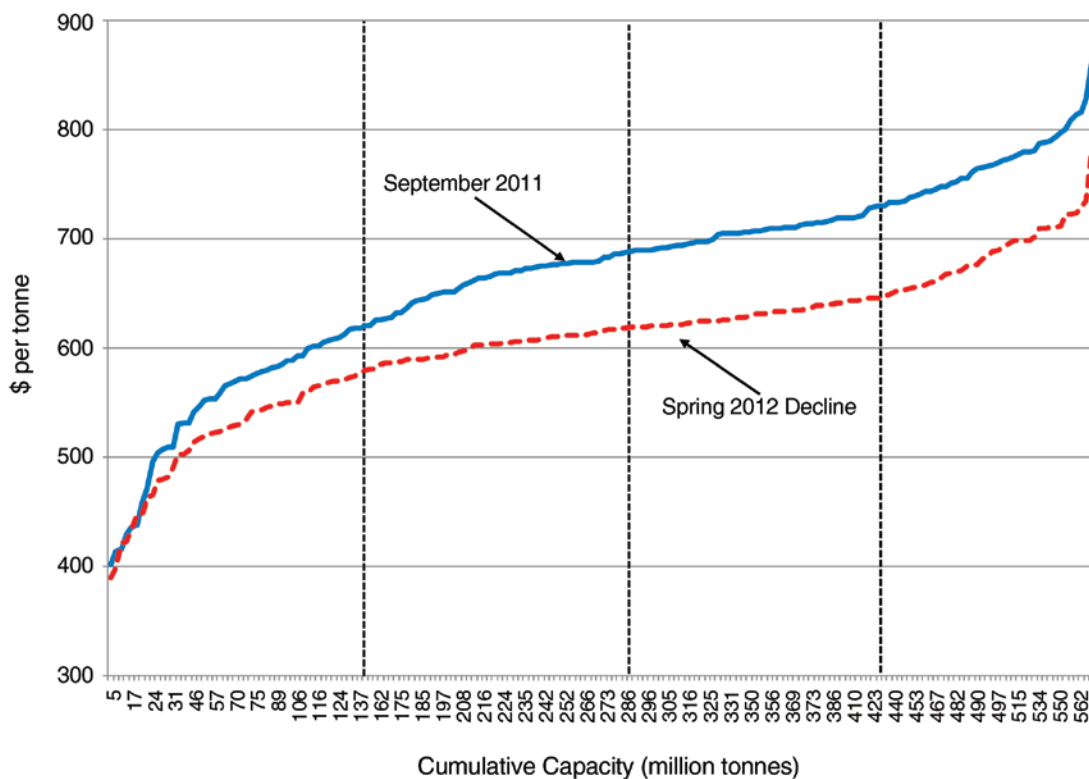
By the spring of 2012, steel mills will have much lower operating costs to produce hot rolled band, granted that the price of steelmakers' raw materials plummets as forecast.

WSD predicts that steel production in China and the rest of the world will ease back moderately in the fourth quarter of 2011 and the first two quarters of 2012. At the same time, the supply of iron ore and coking coal will continue to rise.

Non-Chinese annualized steel production in the fourth quarter of 2011 and first two quarters of 2012 is forecast to be in the 796–811 million tonne range, down from an average of 833 million tonnes annualized in the first three quarters of 2011. For China, annualized production in the next six months may be 674–699 million tonnes versus the high of 729 million tonnes in June 2011 (and a peak rate of 737 million tonnes during the last 10-day period of June).

The World Cost Curve to produce hot rolled band in 2012 will be flatter than at present because of the decline in raw material costs (Figure 1). WSD thinks a flatter cost curve tends to create more price competition than a steeper one. When prices start to decline, fewer steel mills are forced to cut back output when the cost differential between the mid- and high-cost mills becomes narrower. The variation in marginal cost between the 50th percentile and 75th percentile steel mill next spring may be only \$30 per tonne if WSD iron ore and coking coal spot price forecasts come about. From the 25th to the 50th percentile on the World Cost Curve, the variation in cost is larger, at about \$50 per tonne.

**Figure 1**



World hot rolled band operating cost including overhead.

- Steel scrap prices may decline sharply. If this happens, steel buyers will delay their purchases of steel products usually tied to the price of steel scrap, which exacerbates the oversupply of these products.
- The combination of reduced steel production and supply additions in iron ore and coking coal is likely to produce an even greater glut for these materials in the first half of 2012 than in the fourth quarter of this year. Current projects to add to the capacity of these products, which may exceed \$50 billion annualized at present, cannot be turned off like a spigot.

When comparing global steel output in the second quarter of 2011 and the forecast for the first quarter of 2012, the annualized demand for iron ore falls to 1.78 billion tonnes from 1.83 billion tonnes – a decline of 54 million tonnes. Also, the capacity additions globally during this period, which are probably at least 75 million tonnes, must be added. (Note: When taking into account China's peak annualized steel production rate of 737 million tonnes earlier this year and WSD's forecast of 699 million tonnes in the first quarter of 2012, the decline in global iron ore requirements from the peak in 2011 is 83 million tonnes of iron ore, annualized.) Hence, even when taking into account lower deliveries of iron ore from India to China, WSD foresees a sizable glut of iron ore beginning now

and extending well into 2012. Chinese iron ore production, unless steel production in the country falls substantially, is not expected to be significantly impaired until the price drops to about \$140 per tonne versus the current figure of about \$180 per tonne.

Coking coal oversupply is also expected to occur, particularly in non-low-volatile grades, reflecting: (a) high Australian output given the sizable production recovery after floods eliminated most of the country's output earlier this year; (b) USA coking coal producers will seek to sustain market share on the export market; (c) exports to China will remain low since the coking coal price in China is about \$40 per tonne below the Australian price delivered to China; (d) lower demand for coking coal due to reduced Chinese and non-Chinese steel output; and (e) some shift to the usage of lower grades of coking coal that take more time to be converted to coke in the coke ovens, but are substantially lower in price than the better grades of coking coal. ♦

- *Peter F. Marcus*, managing partner, World Steel Dynamics, pmarcus@worldsteeldynamics.com, +1.201.503.0902
- *Phil Englin*, manager – special projects, World Steel Dynamics, penglin@worldsteeldynamics.com, +1.201.503.0908

Comments are welcome. To submit your questions for WSD, email [WSD@aist.org](mailto:WSD@aist.org). Please include your full name, company name, mailing address and email in all correspondence.

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