

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: As companies throughout many different industries are suffering the consequences of the economic crisis and subsequent demand collapse, is the steel industry any more/less vulnerable than others?

A: If steel mills give away their "pricing power" in the next few years, the consequence will be a sizable rise in steel mill bankruptcies. In such an environment, a number of financially troubled steelmakers, in order to avoid bankruptcy, will sell out at bargain-basement prices to their better-positioned competitors. WSD expects the Chinese steel mills to become active participants in the purchase of Western steel mills at bargain prices, if this development occurs.

Pricing Power

Since he began researching the steel industry in the spring of 1961, Peter Marcus has believed that a security analyst is an industrial structure economist who needs to understand, as the industry changes structure, the extent to which various companies in the industry, in different phases of the industry cycle, have the "pricing power" to pass on their costs.

Q: What is the condition of the steel sheet mills' pricing power in 2009?

A: In many cases, the steel mills' pricing power is still fair to good, depending on the market.

Q: What has sustained the mills' pricing power?

A: Some factors include the following: (a) the increased concentration in the industry; (b) steel buyers are still on their heels due to the loss of the psychological pricing war with the mills in the mid-2003 to mid-2008 period; (c) the amazing speed at which steel mills cut back steel production starting in the summer of 2008; (d) the sizable capacity closures and delays in capacity expansions (more than 100 million tonnes of delays in "greenfield" expansions in China alone since last summer); and (e) extreme steel price volatility and complexity, which steel buyers find unsettling.

Table 1 — Steel Mills' Hot Rolled Band Pricing Power in 2009–2010
(O = 2000–2002, X = 2009–2010)

Market type/ region	Very weak	Weak	Fair	Good	Strong
EXPORT MARKET					
Tier I–II mills		O	X		
Tier IV mills	O	X			
Russian mills		O	X		
HOME MARKET					
Chinese steel mills	O		X		
USA steel mills		O	X		
Russian steel mills			O		X
EU steel mills			O, X		
South American steel mills				O, X	
Japanese steel mills					O, X

Q: Which steel mills will have the most pricing power in the next two years, assuming continued overcapacity to produce steel and a glut of steelmakers' metallics (steel scrap, pig iron and steel scrap substitutes)?

A: Overall, the mills' pricing power should be sizable in countries in which there are just a few producers (Table 1).

Ironically, the steel mills' production cutbacks since mid-2008 may not have been a function of the mills' increased concentration. The force pushing down steel output has been the extraordinary collapse of new orders. Steel mills cut output rapidly because: (a) they are not set up to produce steel for inventory; and (b) they were seeking to maximize cash holdings in the "Cash is King" environment. Typically, most steel products are made to order because the product range is so vast within each product category.

Of course, it makes no sense to cut the price when there are almost no domestic or export orders. However, when new orders pick up, there's a greater incentive to cut the price because it can result in more volume. For sure, the mills' actions in the next six months, individually and collectively, will provide an insight into the extent to which the steel mills' behavior pattern has changed from that in 1995–2002 (see Table 2, below, and Figure 1, on next page).

Table 2 — U.S. Raw Steel Production Utilization Rate

Year	Rate	Year	Rate	Year	Rate
1986	62	1996	90	2006	85
1987	76	1997	90	2007	86
1988	89	1998	86	2008	82
1989	84	1999	81	2009	44 YTD*
1990	84	2000	86		
1991	73	2001	75		
1992	80	2002	89		
1993	87	2003	81		
1994	91	2004	90		
1995	90	2005	87		

Source: American Iron and Steel Institute.

*Through Feb. 17, 2009.

— 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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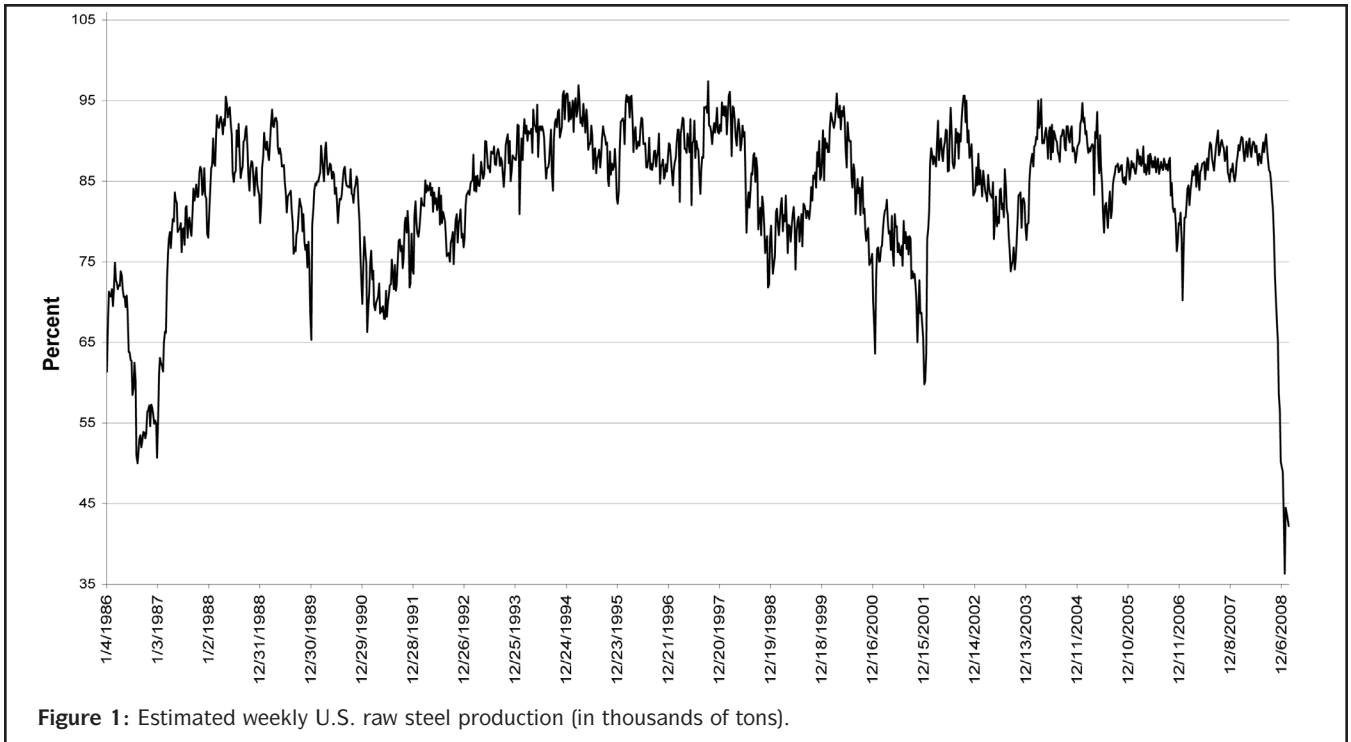


Figure 1: Estimated weekly U.S. raw steel production (in thousands of tons).

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