Steel Export Price Versus Steel Company Stock Performance: They Are Almost Always in Sync

As indicated in Fig. 1, the WSD Global Steel Stock Group Index and the hot-rolled band (HRB) export price, FOB the port of export, since 1997 have often moved in sync with one another. However, note that the vertical axis for the HRB price is about double that on a value basis versus the Steel Stock Group Index price — it ranges from a low of 100 to a high of 1,300, while that for the Steel Stock Group Index goes from zero to 600. Hence, given that both pricing series tend to move together, it appears that the Steel Stock Group Index is about twice as volatile as the HRB price. Perhaps the higher volatility for the steel stocks is because the HRB export price that usually impacts the prices in many home markets — including the U.S., Western Europe and China — is viewed by many observers to be a highly reliable leading indicator.

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The Global Steel Stock Group is a composite of the steel company common stock prices in the U.S., Asia, Japan, China, Europe, Russia and Latin America. This composite had a high of about 500 in mid-2008, when the world export price rose briefly to about US$1,100/metric ton, and then fell in March 2009 to an index value of 115. During this time, the HRB export price dropped to about US$370/metric ton. Hence, in this case, the two-for-one price movement assumption did not hold up. The Steel Group Common Stock Index from its peak fell about 75%, while the HRB price declined about 65%.

The steel mills, their customers and their suppliers, in WSD's opinion, have a huge need to hedge the steel price risk. Reasons for this need include: (a) the HRB export steel price swings trigger sizable volatility in the steel mills' common stock prices; (b) HRB export price swings, with a lag, instigate substantial steel company profit swings — especially outside of China; (c) many banks don't like to make loans on steel in inventory because they fear that the inventory may collapse in value; and (d) the steel mills' enterprise values are suppressed severely reflecting their company's huge sensitivity to swings in the steel export price. (Note: This sensitivity will be somewhat alleviated if, and when, there are liquid steel futures curves outside of China for steel products and steel scrap.)

The common stock of Baowu, which will soon become the world's No. 1 steelmaker given its ongoing acquisition spree, has had somewhat similar volatility over the years as ArcelorMittal when considering the percentage change in the price swings from the extremes (Fig. 2).

In five years, Baowu could become a 250-million-metric-ton-per-year enterprise versus perhaps 110 million metric tons for ArcelorMittal.

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