



METALS CONSULTING

PRESS RELEASE
London, 17th November 2005

FOR IMMEDIATE DISTRIBUTION

Steel Market Outlook: End of Year Concerns

In its latest analysis of the steel market (The Steel Market Forecast Briefing), GFMS Metals Consulting concludes that November and December may be a desperate couple of months for commodity hot-rolled coil suppliers to international markets. Increasingly aggressive prices from CIS and Chinese mills are dragging down prices from higher-quality mills in Asia.

Outside of the USA, big buyers are simply not interested in importing large cargoes. High inventories, or the fact that domestic suppliers have dropped prices in their local markets to ensure competitiveness and can supply on short notice, are the reasons behind the lacklustre nature of current demand. We note for example that in India, a decline in domestic prices will probably shut CIS suppliers out of one of their best volume and price markets.

Meanwhile higher-quality Asian suppliers have dropped prices into the Australian market that will put domestic supplier Bluescope under even greater price pressure after its profit warning. Chinese strip products have also landed in Europe and are being offered from stock in a worrying development for EU suppliers, although they have yet to undermine local prices.

US market: prices remain firm for now

While production numbers have been flat to date, we believe they may increase in November. US Steel is likely to start up its Gary furnace shortly and minimills will look to operate at full capacity given strong profitability. US prices are the highest in the world at the moment at around \$570/tonne for HR coil and \$680/tonne for CR material. The increase in the base price last month allowed minimills some margin improvement and higher November delivered prices should see margins hold up for this month at least. Ipsco has noted that it intends to run at full capacity in Q4 as end-use demand for plate is strong as is service centre demand.

Little change in Europe

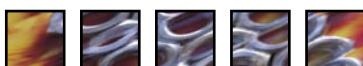
European prices continue at recent levels. We understand that significant volumes of Chinese flat products have landed, and are available from stock in northern Europe, but strong demand in Turkey, the Middle East and North Africa is limiting Mediterranean-sourced material being offered into southern Europe at discount levels at present. For now, there is little evidence of other Asian strip products being offered into continental Europe, although there are more widespread offers for plate.

Domestic EU mills continue to target €400/tonne (\$480/tonne) on an ex-mill basis as the regional HR coil price, but continue to fall short of this in southern Europe and also in Germany and France for most grades. Nevertheless, economic data continues to bode well for European demand in 2006, and we suggest that the current price situation will improve at that time.

Are cutbacks likely in Asia?

While we have noted that the Japanese steel mills have cut back and to a large extent have absented themselves from the Asian commodity HR coil market, there appears to be little other evidence of cutbacks. Taiwanese suppliers, Chung Hong and China Steel, have announced cutbacks, but these are likely to be minimal. While CISA has called for a 5% cut in Chinese output, we doubt whether this will be fully matched, although maintenance stoppages are likely in Q4, with larger (and more profitable) mills leading the way.

Posco has announced cutbacks in stainless output, but has not publicly announced cuts in carbon output, and as one of the lowest-cost integrated producers it has less incentive than most. Nevertheless, it has been forced to compete on price, and Chinese offers of HR coil into South Korea continue to fall – now to below \$400/tonne cif, although there is only limited buying.





Low slab prices buoy margins

One key issue in our view is that the weakness of the slab price has meant that for many Asian suppliers that are non-integrated, supplying HR coil remains very profitable. Despite the current weakness in HR coil, the regional slab-HR coil margin is still over \$100/tonne for commodity products, allowing positive margins for converters. This suggests that converters are unlikely to cut back on output volumes in the short term, which may keep the over-supply in the region going longer than some expect.

Chinese domestic prices have shown little upward movement in the last few weeks with domestic inventories remaining stubbornly high. This is due to high output levels. Crude steel production rose 22% year-on-year in September to 30.4m tonnes. Baosteel had held off dropping prices in Q3 thanks to its strong order book for its higher-quality products, and was hoping that the market would turn upwards in Q4 to allow it to rollover prices, but it was forced to play catch-up with other market players to secure orders. Baosteel was forced to be most aggressive on HR coil prices – cutting them by 800yuan/tonne (almost \$100/tonne), as this product has suffered more than most in terms of over-production.

The bottom line is that the steel mills which instigated the largest cuts (the US producers) are now starting to gain the benefits. The European mills have also taken pre-emptive steps in cutting output. Unfortunately for them their action has been undermined by still weak demand.

© **Copyright GFMS Metals Consulting - November 2005.** Whilst every effort has been made to ensure the accuracy of the information in this document, GFMS Metals Consulting Ltd cannot guarantee such accuracy. Furthermore, the material contained herewith has no regard to the specific investment objectives, financial situation or particular needs of any specific recipient or organisation. It is published solely for informational purposes and is not to be construed as a solicitation or an offer to buy or sell any commodities, securities or related financial instruments. No representation or warranty, either express or implied, is provided in relation to the accuracy, completeness or reliability of the information contained herein. GFMS Metals Consulting Ltd does not accept responsibility for any losses or damages arising directly, or indirectly, from the use of this document.

Note to Editors about GFMS Metals Consulting Ltd:

GFMS Metals Consulting was established to build upon GFMS Limited's unparalleled reputation for providing authoritative analysis on the precious metals markets. GFMS Metals Consulting will utilise the same in-depth research techniques to meet the industries' demands for market information and analysis on the base metals, steel and related sectors.

Press Contacts: Neil Buxton, GFMS Metals Consulting Ltd, Hedges House, 153-155 Regent Street, London, W1B 4JE, UK, tel: +44 (0)20 7478 1752, fax: +44 (0)20 7478 1779, email: info@gfms-metalsconsulting.com, web site: www.gfms-metalsconsulting.com