



AMERICAN INSTITUTE FOR INTERNATIONAL STEEL

NATIONAL ASSOCIATION OF STEEL PIPE DISTRIBUTORS

2005 ANNUAL CONVENTION

LOOKING INTO THE FUTURE OF STEEL ON THE INTERNATIONAL STAGE

PRESENTATION BY

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THANK YOU FOR INVITING ME TO SPEAK AT YOUR MEETING. THE STEEL BUSINESS MAY NO LONGER BE THE ROULETTE GAME IT WAS IN RECENT YEARS, AT LEAST THAT'S OUR HOPE, BUT LAS VEGAS IS ALWAYS A GREAT PLACE TO BE.

WHILE CHINA IS THE MAJOR INTERNATIONAL SOURCE OF THE CHANGES IN THE INTERNATIONAL STEEL MARKET WE EXPERIENCED IN 2004, THE STORY DOES NOT START AND END THERE. NATURALLY, THE AMERICAN MARKET'S SURGE OUT OF A 3-YEAR RECESSION FOR STEEL ALSO PLAYED AN IMPORTANT ROLE LAST YEAR, PUSHING PRICES IN THE US TO LEVELS WE HAVE NEVER SEEN BEFORE – HOT-ROLLED SHEET SELLING AT NEARLY \$800.00 PER NET TON ON THE SPOT MARKET IN LATE SUMMER, EARLY FALL!

THE GOOD NEWS FOR STEEL IS THAT THE AMERICAN STEEL MARKET IS STRONG, AND HAS BEEN SINCE CHINESE STEEL DEMAND JUMP-STARTED THE WORLD STEEL MARKET IN EARLY 2004. STRONG DEMAND, HIGHER PRICES AND HEALTHY PROFITABILITY FOR THE STEEL MARKET ALSO BRINGS OTHER GOOD NEWS; VERY LOW LIKELIHOOD OF PROTECTIONIST DUMPING OR OTHER TRADE ACTIONS BEING FILED BY THE AMERICAN STEEL INDUSTRY.

OUR EXPERIENCE IN 2004 TELLS US A LOT ABOUT WHERE WE ARE NOW. LAST YEAR THE CHINESE MARKET ACCELERATED ITS GROWTH FROM A STRONG 2003 EARLY IN THE YEAR, AND CHINESE STEEL PRICES BECAME THE HIGHEST IN THE WORLD BY MID-SECOND QUARTER. WITH THE CHINESE GOVERNMENT'S CONCERNS ABOUT THE OVERHEATING STEEL MARKET AND LOGISTICS ISSUES AT THE PORTS ATTEMPTING TO DELIVER THE HUGE QUANTITIES OF RAW MATERIALS AND STEEL PRODUCTS, CHINESE STEEL PRICES DECLINED.

THIS HAPPENED AT ABOUT THE SAME TIME THE AMERICAN ECONOMY WAS TAKING OFF. OUR CAPITALIST ECONOMY HAD HIT FULL STRIDE, AND EVEN WITH RECORD STEEL PRICES, THERE WERE MANY COMPLAINTS FROM STEEL CONSUMERS THAT THEY COULD NOT GET ENOUGH STEEL. NATURALLY, THOSE PRICES ATTRACTED STEEL IMPORTS FROM ALL OVER THE WORLD.

TOTAL IMPORTS WERE UP BY 54.8 PERCENT IN 2004, OR OVER A 12.5 MILLION TON INCREASE. CHINA, LIKE OTHER COUNTRIES, WITH THEIR PRICES LAGGING THE HOT AMERICAN MARKET, PARTICIPATED TOO, WITH IMPORTS UP 187%, OR OVER A 1.2 MILLION TON INCREASE. OTHER COUNTRIES WHO INCREASED THEIR SHIPMENTS TO THE HOT AMERICAN MARKET INCLUDED, THE EUROPEAN UNION UP 43 PERCENT OR OVER A 1.7 MILLION TON INCREASE; BRAZIL UP 58.5 PERCENT OR OVER A 1.5 MILLION TON INCREASE; MEXICO UP 32.9 PERCENT OR OVER A 1 MILLION TON INCREASES; TURKEY UP 121 PERCENT OR A 1.2 MILLION TON INCREASE; RUSSIA UP 640.9 PERCENT OR OVER A 2 MILLION TON INCREASE; KOREA UP 38.2 PERCENT, NEARLY A .5

MILLION TON INCREASE. STEEL CONSUMERS IN THE USA BENEFITED GREATLY FROM THE IMPORTED STEEL.

BY THE WAY, NOTWITHSTANDING THE CONCERNS OFTEN STATED BY THE AMERICAN DOMESTIC STEEL INDUSTRY, WE DO NOT SEE THE CHINESE STEEL INDUSTRY AS BECOMING A MAJOR NET STEEL EXPORTER ANY TIME SOON. AS MY COLLEAGUES AT FERROSTAAL AND MANY EXECUTIVES OF THE OTHER TRADING HOUSES I AM SURE WOULD TELL YOU, WE SEE THE DEMAND CURVE FOR STEEL IN CHINA STRETCHING OUT AT A STRONG PACE FOR MANY YEARS TO COME, AND EVEN WITH THE AMBITIOUS CAPACITY ADDITIONS ALREADY IN PLACE AND ON THE BOOKS, WE DO NOT THINK THAT WILL CHANGE CHINA FROM A NET IMPORTER TO A NET EXPORTER OF STEEL, EXCEPT FOR POSSIBLY SHORT PERIODS OF TIME WHEN STEEL PRICES IN POTENTIAL EXPORT MARKETS PROVIDE OPPORTUNITIES WHEN STEEL PRICES LAG IN CHINA, AS THEY DID LATE IN 2004 WHEN CHINESE EXPORTS WERE SLIGHTLY LARGER THAN IMPORTS FOR A MONTH OR TWO.

OTHER STEEL MARKETS AROUND THE WORLD PLAYED A ROLE IN OUR 2004 EXPERIENCE TOO, AND CAN BE EXPECTED TO DO SO AGAIN IN 2005. FOR EXAMPLE, LATE IN 2004, BRAZILIAN MILLS REDUCED THEIR PARTICIPATION IN EXPORT MARKETS IN RESPONSE TO SURGING DOMESTIC DEMAND. WE BELIEVE THAT THIS REFLECTS A STRUCTURAL CHANGE IN THE HEALTH OF THEIR ECONOMY ONTO A MORE SUSTAINED GROWTH PATH FOR THE LONG-TERM. LIKEWISE, WE SEE THIS KIND OF LESS DEVELOPED COUNTRY GROWTH PATTERN EMERGING IN RUSSIA AND THE UKRAINE AND OTHER PARTS OF EASTERN EUROPE AS THEIR ECONOMIES ARE BEGINNING TO EXPERIENCE GROWTH THAT LOOKS SUSTAINABLE TOO. NATURALLY, THESE KINDS OF GROWTH RATES ARE HIGHLY STEEL INTENSIVE – INFRASTRUCTURE, CONSUMER DURABLE, PLANT AND EQUIPMENT INVESTMENT, ETC.

FINALLY, THERE IS INDIA. ECONOMIC ANALYSTS NOW SEE INDIA, WITH ITS POPULATION SECOND ONLY TO CHINA, AS THE NEXT LESS DEVELOPED COUNTRY TO TAKE OFF ON A PATH THAT, EVEN AT THIS EARLY STAGE, LOOKS A LOT LIKE THE BEGINNINGS OF THE CHINA EXPERIENCE. ALL OF THIS BODES WELL FOR STEEL DEMAND, AND IMMEDIATELY BEGS THE QUESTION OF STEEL SUPPLY. WHERE WILL IT COME FROM? WHO WILL BUILD IT? WHERE WILL THE RAW MATERIALS COME FROM? TO ANSWER THESE QUESTIONS, I WOULD BE HERE A LOT LONGER THAN MY ALLOTTED TIME. THEREFORE I WILL SPARE YOU.

THE EUROPEAN UNION IS ON A GROWTH PATH, EVEN THOUGH A SLOW ONE. JAPAN, AFTER MORE THAN 10 YEARS OF EXPERIENCING NEGATIVE GROWTH, TURNED THE CORNER LAST YEAR. THE TIGER STATES AND AUSTRALIA/ NEW ZEALAND HAVE GOOD GROWTH RATES. LATIN AMERICA IS A MIXED BAG. BUT BRAZIL AND CHILE ARE ON THE RIGHT TRACK. THE NAFTA REGION IS DOING

WELL, THE MAJOR ENGINE BEING THE AMERICAN ECONOMY. CHINA WE MENTIONED ALREADY. ONE MORE WORD ON INDIA, WHO WOULD HAVE THOUGHT THAT INDIA WHOSE DIFFERENT GOVERNMENTS OVER THE LAST FIFTY YEARS HAVE TOYED WITH SOME KIND OF SOCIALISM WOULD FINALLY BE ON THE VERGE OF EXPLOSIVE GROWTH. NOWADAYS INDIAN GOVERNMENTS HAVE RECOGNIZED THAT A FREE MARKET ECONOMY IS THE SOLUTION. I BELIEVE WE WILL SEE GROWTH RATES OF THE INDIAN ECONOMY OF 5-10 PERCENT ANNUALLY FOR YEARS TO COME.

IN THE SHORT LIVED STEEL SHORTAGE CRISIS IN 1973-74, WHEN DEVELOPED ECONOMIES ALL HIT CYCLICAL PEAKS AT THE SAME TIME, WE SAW CAPACITY EXPANSION PLANS DEVELOP THAT SOME MIGHT SAY, SOWED THE SEEDS OF THE LONG-TERM WORLD OVERCAPACITY PROBLEMS THAT DID NOT SORT THEMSELVES OUT FOR 30 YEARS. OF COURSE, COUPLED WITH GROWTH IN CAPACITY WAS AN UNWILLINGNESS OF MANY COUNTRIES AND COMPANIES TO SHUTTER OUTDATED AND INEFFICIENT CAPACITY, TOO OFTEN BY USING TRADE PROTECTION AND LARGE GOVERNMENT SUBSIDIES. PUT SIMPLY, TOO MUCH CAPACITY, TOO MUCH GOVERNMENT INTERFERENCE IN THE MARKETPLACE.

THE DIFFERENCE THIS TIME IS THAT THIS HOT INTERNATIONAL STEEL MARKET IS NOT THE RESULT OF THE DEVELOPED WORLD'S MAJOR ECONOMIES HITTING A CYCLICAL UPTURN AT THE SAME TIME. INSTEAD, FROM OUR PERSPECTIVE, IT IS THE RESULT OF THE DEVELOPING WORLD FINALLY TAKING OFF STRUCTURALLY. AND WHEN A DEVELOPED ECONOMY ALSO HITS A CYCLICAL PEAK, AS WE EXPERIENCED IN THE USA IN 2004, WATCH OUT! AS FREE TRADERS, WE WOULD LIKE TO BELIEVE THAT FOR SOME OF THE DEVELOPING COUNTRIES LISTED ABOVE, THE STRUCTURAL GROWTH BEING EXPERIENCED IS THE RESULT OF INTERNATIONAL TRADE LIBERALIZATION POLICIES BORNE OF THE GATT AND THE WTO. IN SHORT, FREE TRADE WORKS.

WELL, BACK TO THE BIGGEST ENGINE OF GROWTH IN THE STEEL SECTOR IN RECENT YEARS, CHINA. WE HAVE ALL BEEN SWAMPED WITH STORIES OF CHINA'S PHENOMENAL GROWTH. FOR EXAMPLE, IN JUST A LITTLE OVER TWO YEARS CHINA ADDED AS MUCH STEEL OUTPUT AS THE US INDUSTRY TURNS OUT IN A YEAR.

HALF A DOZEN YEARS AGO, NO ONE ANTICIPATED SUCH SPECTACULAR GROWTH. IN JULY 1999, ANALYSTS FROM WORLD STEEL DYNAMICS (WSD) PREDICTED THAT CHINA WOULD PRODUCE ABOUT 150 MILLION TONS IN 2005. AS IT TURNED OUT, THE LEVEL OF PRODUCTION WAS ALREADY OVERTAKING THAT NUMBER BY 2001. (BY THE WAY, ALL MY NUMBERS REFER TO SHORT OR NET TONS.) EXPERTS FROM THE INTERNATIONAL IRON AND STEEL INSTITUTE AND CHINESE GOVERNMENT OFFICIALS LIKEWISE SAW THEIR EARLIER FORECASTS LEFT IN THE DUST BY THE EXPLOSIVE GROWTH OF STEEL

PRODUCTION AND DEMAND IN CHINA. AND THERE HAS BEEN NO LET-UP IN THE EXPANSION, DESPITE WORSENING CONGESTION OF PORTS AND TRANSPORT ARTERIES AND SHARP INCREASES IN ESSENTIAL COST COMPONENTS LIKE ELECTRICITY, IMPORTED SCRAP, IRON ORE, AND OCEAN FREIGHT. LAST YEAR, CHINA PRODUCED MORE THAN 300 MILLION TONS OF RAW STEEL.

THE RAPID EXPANSION OF CHINA'S STEEL INDUSTRY HAD A WORLDWIDE IMPACT ON THE COST OF MATERIALS AND OCEAN SHIPPING. BY THE MIDDLE OF LAST YEAR, INTERNATIONAL PRICES OF SCRAP AND BLAST FURNACE COKE AS WELL AS FREIGHT CHARGES HAD SOARED INTO THE STRATOSPHERE. THEY HAVE SINCE COME DOWN BUT REMAIN FAR ABOVE THEIR HISTORICAL LEVELS. TO MEET RISING DOMESTIC DEMAND FOR BLAST-FURNACE COKE AND ALSO SHUT DOWN POLLUTING COKE OVENS, THE CHINESE GOVERNMENT CURTAILED COKE EXPORTS BY MEANS OF EXPORT PERMITS, WHICH LED FOREIGN GOVERNMENTS AND INDUSTRIES TO FILE PROTESTS. THE WORLDWIDE COKE SHORTAGE IN TURN LED TO TIGHT SUPPLIES AND THE DOUBLING OF COKING COAL PRICES.

IN ADDITION TO MINING HUGE QUANTITIES OF LOW-QUALITY DOMESTIC ORES, CHINA ALSO BECAME THE WORLD'S LARGEST IMPORTER OF IRON ORE, TAKING WELL OVER A THIRD OF INTERNATIONAL ORE SHIPMENT. THE GLOBAL IRON ORE INDUSTRY, WHICH IS DOMINATED BY AUSTRALIA AND BRAZIL, REACTED TO THE STRONGER DEMAND WITH A SERIES OF PRICE INCREASES. BUT THE REAL SHOCKER CAME LAST MONTH, WHEN PRICE INCREASES RANGING FROM 50-90 PERCENT WERE PUT ON THE TABLE. CVRD AND NIPPON STEEL FINALLY SETTLED BEGINNING OF THIS WEEK AT AN INCREASE OF 71.5 PERCENT ABOVE LAST YEAR'S CONTRACT PRICES.

INCREASES IN THE GLOBAL COST OF ENERGY RESOURCES LIKE OIL, NATURAL GAS AND EVEN STEAM-RAISING COAL CAN LIKEWISE BE ATTRIBUTED TO CHINA'S RAPID EXPANSION. IN CHINA, SEVERE WATER AND ELECTRIC POWER SHORTAGES AS WELL AS PORT, RAIL, AND ROAD CONGESTION HAMPER INDUSTRIAL GROWTH. IN THE FACE OF ALL THESE PROBLEMS, IT APPEARS DOUBTFUL THAT CHINA CAN KEEP ON ADDING LARGE CHUNKS OF STEELMAKING CAPACITY FOR ANY LENGTH OF TIME, BUT NOTE THAT THE INFRASTRUCTURE NEEDS OF CHINA WILL CONTINUE TO FUEL GROWTH IN STEEL DEMAND, WHETHER DOMESTIC OR IMPORTED.

COMING ON THE HEELS OF OUR EXPERIENCE IN 2004, THIS YEAR IS SHAPING UP AS ANOTHER STRONG YEAR FOR STEEL DEMAND AND NOT ONLY IN THE USA. I AM NOT AWARE OF ANY PUNDITS SUGGESTING THAT THE AMERICAN OR OTHER IMPORTANT STEEL MARKETS ARE POISED FOR A DOWNTURN THIS YEAR. THE ONLY DEBATE APPEARS TO BE ABOUT HOW FAST THE MARKET WILL GROW AND HOW HIGH THE PRICE OF STEEL WILL GO. IN FACT, DURING THE FIRST TWO MONTHS OF THE YEAR, THE MARKET HERE WAS RATHER

SLOW, BUT DEMAND WILL IMPROVE AS WE APPROACH THE SEASONALLY STRONG SECOND QUARTER. WITH AMERICAN RAW STEEL PRODUCTION HITTING 92.9 PERCENT IN LATE JANUARY, OR ESSENTIALLY AT FULL CAPACITY GIVEN MILL OUTAGES AND NORMAL MAINTENANCE SCHEDULES, BAD NEWS IS HARD TO FIND IN THE STEEL SECTOR.

INTERNATIONAL TRADE, AND NOT JUST THE TRADE IN STEEL, WILL CONTINUE TO GROW. THIS WILL CREATE OPPORTUNITIES ALSO FOR AMERICAN STEEL PRODUCERS TO EXPORT AND BECOME A REGULAR SUPPLIER TO WORLD MARKETS. I KNOW THAT SOME REPRESENTATIVES OF SALES AND MARKETING ORGANIZATIONS PRESENT IN THIS ROOM WOULD LIKE TO SEE THIS HAPPEN, INCLUDING THE ONE WHO SPEAKS TO YOU NOW.

LOOKING AT TODAY'S SITUATION IN THE WORLD, DOES ANYBODY IN THIS ROOM REMEMBER A TIME WHEN ALL THE IMPORTANT ECONOMIES OF THE WORLD WERE SIMULTANEOUSLY HEADING IN THE RIGHT DIRECTION?

I DON'T THINK ANYBODY RECALLS HAVING LIVED IN SUCH PERIOD OF GROWTH SPREAD AROUND THE GLOBE LIKE WE ARE EXPERIENCING TODAY. FREE TRADE IN STEEL, THE AIIIS REASONING FOR BEING, STILL CONTINUES TO BE A CHALLENGE WORTH PURSUING.