

# NAFTA Steel Industry Pulse

North American Steel Trade Committee  
Halifax, Nova Scotia, November 20-21, 2008



**CSPA**  **ACPA**  
Canadian  
Steel  
Producers  
Association

L'Association  
canadienne des  
producteurs  
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**American  
Iron and Steel  
Institute**



  
**SPECIALTY STEEL INDUSTRY  
OF NORTH AMERICA**





# Key Topics

- Economic and Financial Update – World and NAFTA Steel Market Conditions
- China Trade and Industrial Policies
- Major Developments and Concerns about Raw Materials
- Trade and Climate Change



## First Topic: Economic and Financial Update – World and NAFTA Steel Market Conditions

- Conditions Are Worsening Worldwide and in NAFTA
- Steel Demand Is Falling Both Globally and in NAFTA
- IISI Could Not Issue Its Fall 2008 Short Range Outlook Due to Market Uncertainty



# The United States Is Almost Certainly in a Recession

- **US GDP continued to grow during the first half of 2008, but at a slower rate than in prior years**
- **Consumer confidence is at a record low level**
- **While the U.S. has so far averted a “technical” recession, government estimates for the 3<sup>rd</sup> quarter indicate that the economy shrank by 0.3 percent during that period.**
- **In October 2008, as the U.S. and global financial crisis spread far beyond subprime loan problems, the U.S. Congress passed a \$700 billion economic emergency stabilization bill intended to unfreeze credit markets and restore confidence in financial markets**
- **The U.S. economy is in uncharted territory and in a period of unprecedented uncertainty.**

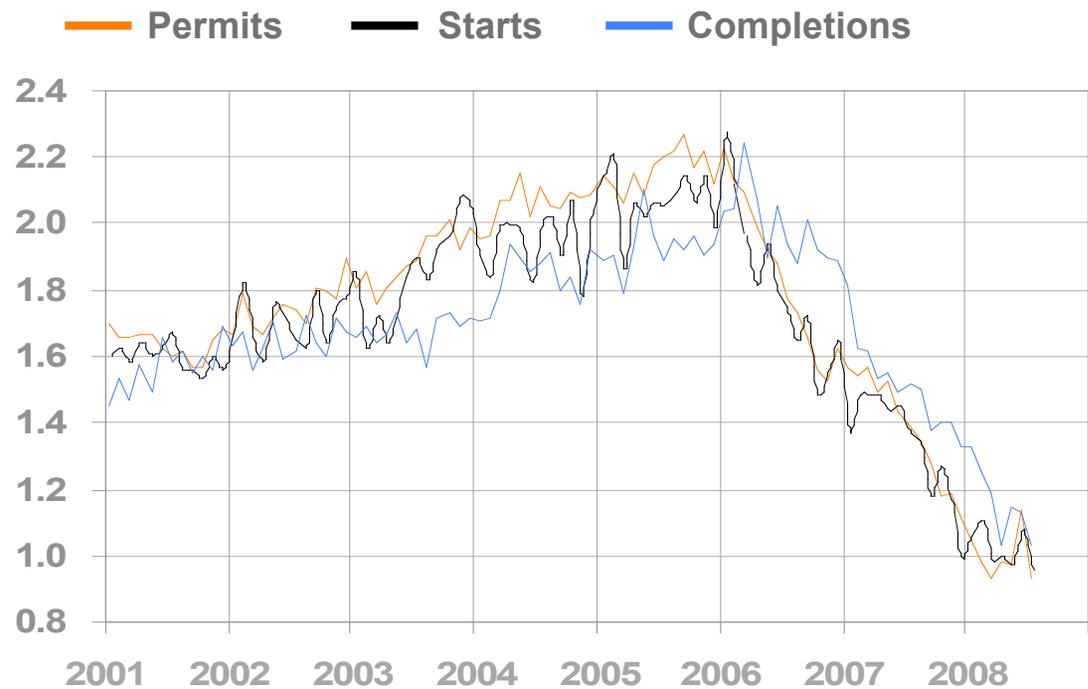
Source: Federal Reserve Board



# The U.S. Housing Market Is Plummeting

- The housing market and home values have continued to slide in 2008.
- The inventory of unsold homes is at 11 months vs. less than 4 months in normal times.
- Residential construction activity is 500,000 units below historical levels.
- Roughly 9 percent of mortgages are in foreclosure or in default.
- It is not yet clear that the housing market has hit bottom.

## Residential Construction Market





# More Evidence of a Potentially Severe Recession

- **The subprime loans made by U.S. financial institutions have begun to affect significantly other parts of the overall U.S. and global economies.**

- **The U.S. stock market has lost roughly 40% of its value in the past year.**

- **While GDP growth has remained positive for the first nine months of 2008, the U.S. has lost over 1.2 million jobs, and the unemployment rate has increased to 6.5%.**

- **The auto industry has its lowest sales figures in recent memory.**

- **Consumer spending is in decline, and is expected to be further reduced by the credit crisis and job losses.**

The Dow Jones Industrial Index Hit a High of 14,164 on 10/9/07. It has since fallen dramatically.





# Canadian Economy: Gathering Storm?

- Real GDP declined 0.3% in August, leading to a downward revision of Q3 growth forecasts to +1.5% (from +2.5%)
  - Retail sales down 0.3%
  - Manufacturing output down 1.2%, shipments down 3.7%
- Total employment increased by 9,500 in October led by public sector, but also the unemployment rate (to 6.2% from 6.1%)
  - But private sector jobs **fell** by 20,000
- Housing starts roughly flat yoy in September
- Ontario on pace to receive federal “equalization” payments for the first time in history (CBC News, <http://www.cbc.ca/canada/story/2008/11/03/flaherty-ministers.html>)



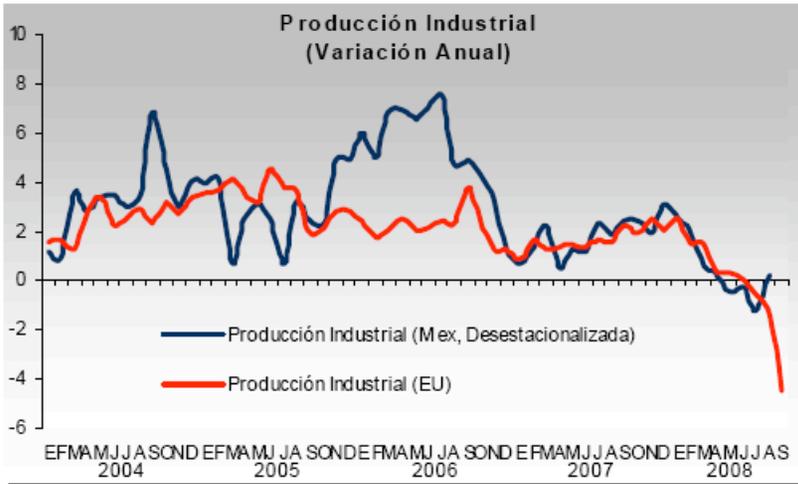
# México Political and Economic Situation

- Mexican Congress approved an energy reform. This is the first step in a process that will require future changes if Mexico wants to have a dynamic energy sector.
- Political parties are starting to prepare for mid-term election next July 2009 to renew the Congress and some state governorships.
- In the context of a global economic crisis, Mexican Government has reacted with an anti-cyclical policy focusing on four main issues: the expenditure side, the national fund for infrastructure, financial support for the banking system, and a further opening of the economy through a general reduction of tariffs. The main economic goal is to stimulate the domestic market.
- The government and the Central Bank are working to ease the credit crunch as well as the FX/currency problems.
- The U.S. economic slowdown, weaker commodity prices and limited access to capital leave little room for optimism, so it is expected that, by year's end, Mexico's real GDP growth will be around 1.5%-2%, while inflation will be 6%.
- The 2009 GDP growth is forecast to decline to around zero. The IMF forecast is for 0.9%. Others are less optimistic, putting the forecast at 0.6%-0.8%.

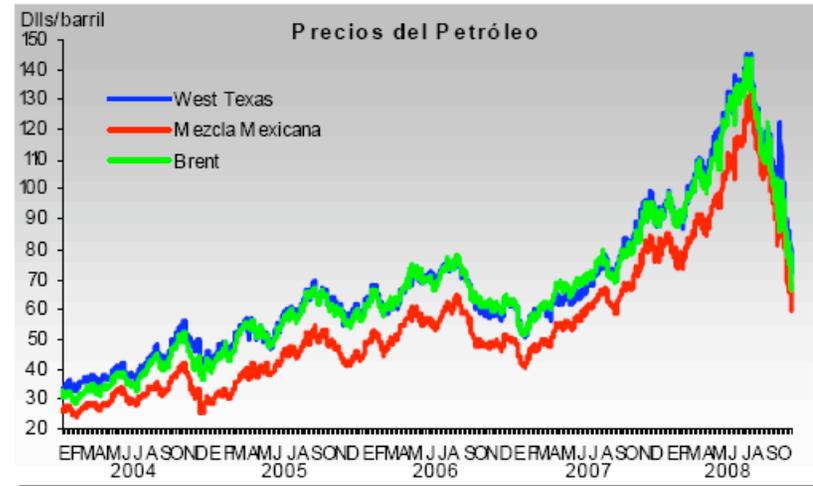


# Mexico: All Indicators Showing a Drastic Change

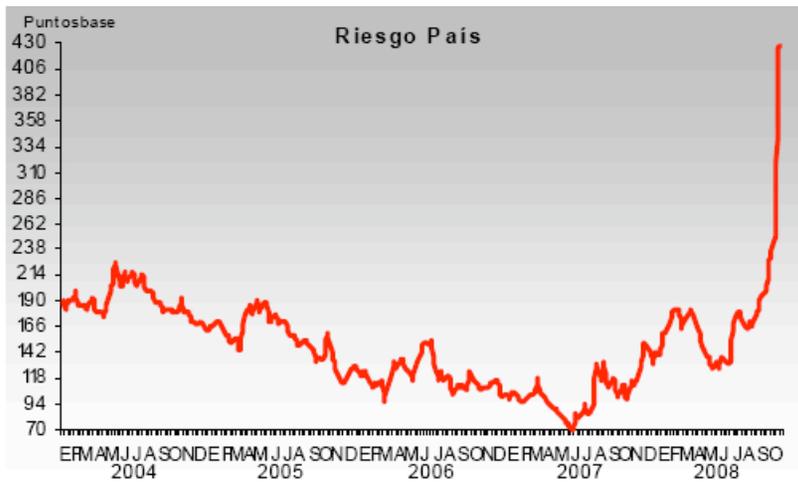
## Industrial Production: Mex & US



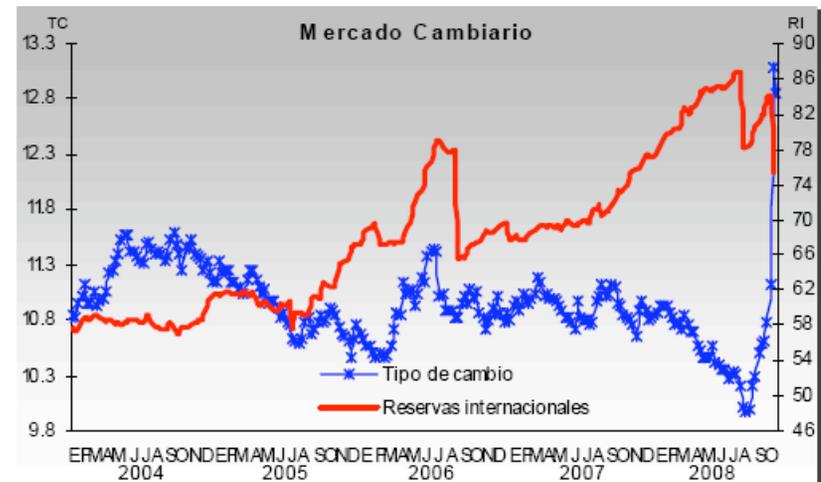
## Oil export prices



## Risk: Restrictions to Credit



## Reserves and Exchange Rate



Source: Oxford Economic & Capem



# Press Reports Show that Market Conditions Are Worsening

## **US Car Sales Sink To Lowest Level For 25 Years**

*Financial Times, Nov. 3* “Sales of light vehicles in the US sank to their lowest level in a quarter of a century last month, with generous discounts failing to offset evaporating consumer confidence and scarce credit.”

## **Whirlpool To Cut More Jobs, Capacity**

*The Wall Street Journal, Oct. 29* “Whirlpool Corp. more than doubled its planned layoffs through next year to about 5,000 people as its profit fell 6.9% in the third quarter.”

## **Home Building at Slowest Pace Since 1991**

*The Associated Press, Oct. 17* “Government data released Friday showed that construction of new homes declined more than expected in September as builders cut production to the slowest pace since early 1991.”

## **Nonresidential Construction in For a ‘Long Slide’**

*AMM, Nov. 4* “Nonresidential construction is ‘on the verge of a potentially long slide’ brought on by the credit squeeze and economic slump...”

## **Failure of Auto Industry Could Set Off Catastrophe**

*Associated Press, Nov. 12* “Advocates for the nation’s automakers are warning that the collapse of the Big Three — or even just General Motors — could set off a catastrophic chain reaction in the economy...”

## **U.S. Economy Contracts Most Since the 2001 Recession**

*Bloomberg, Oct. 30* “The economy suffered its biggest decline since 2001 in the third quarter, ushering in what may be the worst recession in a quarter century.”

## **Manufacturing Falls to 26-Year Low**

*The Washington Post, Nov. 4* “Activity in the nation’s manufacturing sector, beleaguered by tightfisted consumers and the global credit crisis, declined last month to the lowest level in more than two decades...”

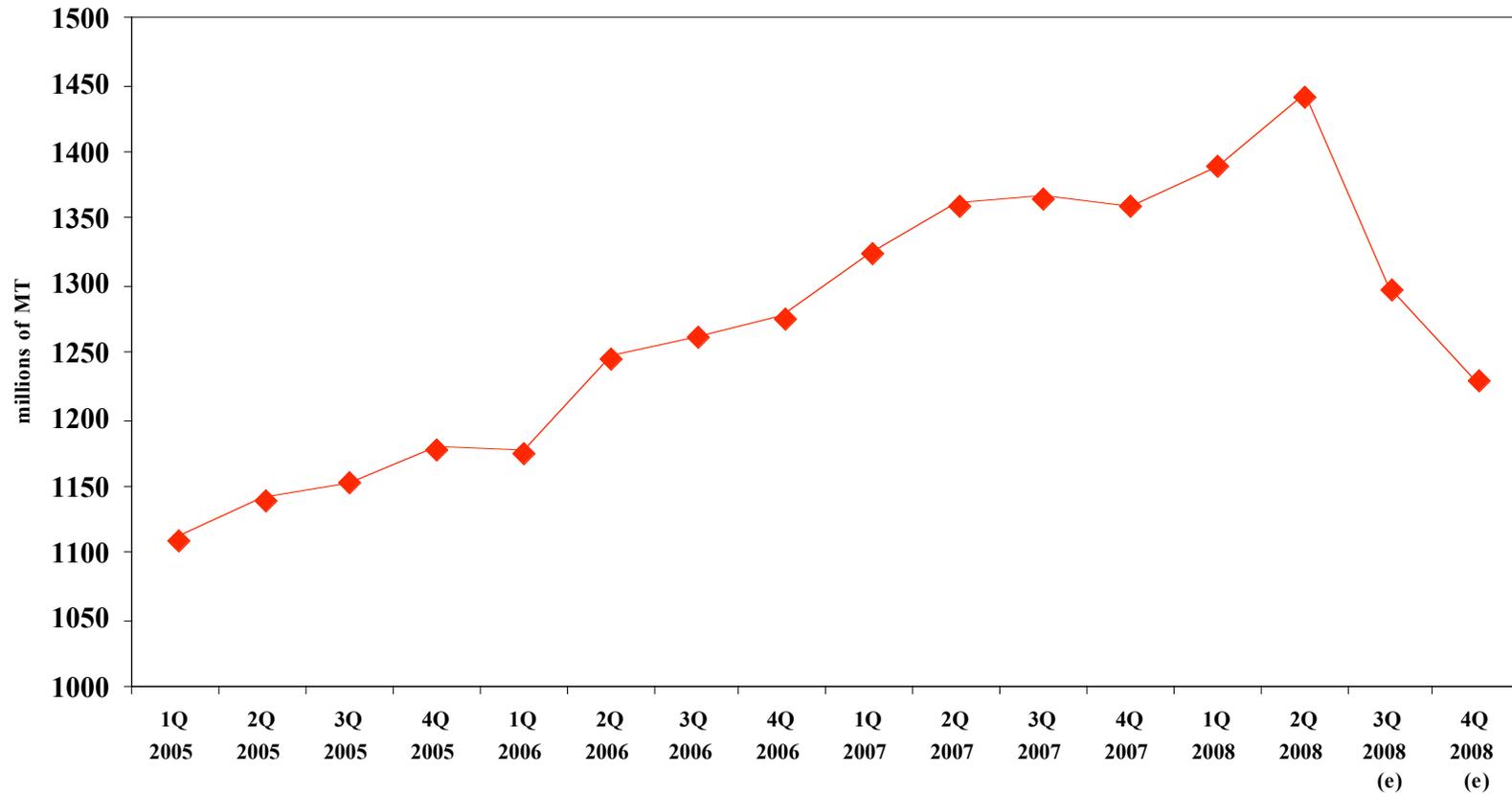
## **Evidence of a Global Recession Mounting**

*The Washington Post, Nov. 13* “Some of the underlying problems – the credit crunch, falling real estate values – have a ‘long way to go’ before they begin to abate, agency says.”



# After Years of Growth, Global Steel Consumption Has Fallen

## Global Apparent Steel Consumption (Annualized)



Source: World Steel Dynamics, "Global Alert # 31" (Oct. 1, 2008) at 12.



# The Fall 2008 Short Range Outlook Historically Provided By IISI (“Worldsteel”) Was Not Issued Due To The Unprecedented Level Of Market Uncertainty

**worldsteel**  
ASSOCIATION

## PRESS RELEASE

### World Steel Association Revised Short Range Outlook (SRO)

*Washington DC, 6 October 2008* – The World Steel Association Executive Committee reviewed its original Short Range Forecast issued in April 2008. The Executive recognized that the market is demonstrating rapidly changing circumstances but noted that 2008 will be another year of growth for the steel industry.

Ku-Taek Lee, Chairman of the World Steel Association and Chairman & CEO of POSCO said, “We are in a period of high economic uncertainty. The impact on steel markets is becoming more apparent as we move into the later part of this year. We are currently reviewing our forecasts for 2009, which had been prepared this summer before current events. However, we continue to expect growth in steel demand in 2009 and for the medium term, above the world GDP growth rate.”

The next World Steel Association Short Range Outlook (SRO) will be issued in April 2009.

“A Confluence of a rapid economic deterioration in the US and Europe, a slowdown in emerging markets like China, and increasing difficulty in financing new projects in both industrial and construction sectors has taken the steam out of the steel sector. Accordingly, we are revising our shipment volumes and earnings estimates as well as significantly reducing price targets for the entire sector.”

Sal Tharani – Goldman Sachs  
*(Comments made in recent Steel Market analysis report)*



## Growing Threat of Foreign Market-Distorting Practices Due to the Crisis

- China has announced a plan to eliminate the export tax on certain steel products and increase the tax rebate on over 3,000 products effective Dec. 1, 2008
- The Indian minister of steel was quoted as saying that the government would consider imposing 5% import duty on steel and scrapping exports levy of up to 15%. “It is a matter of survival for our steel firms.”
- The Ukrainian Ministry of Industrial Policy has reportedly completed a plan to invest \$15 billion into its metallurgical sector

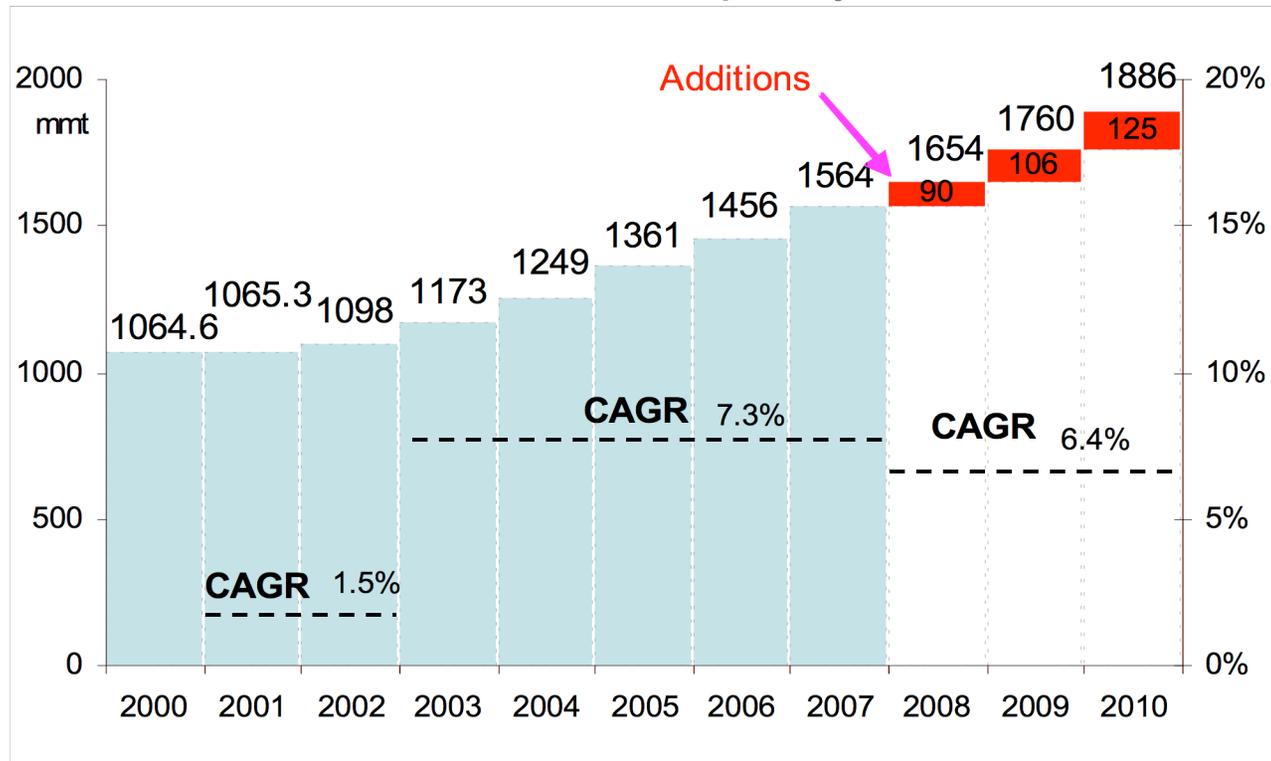
Source: SteelGuru 10/16/2008



# Global steel capacity 2008~10

- During 2008~10, world steel capacity will grow by 322 mmt, 21% increase over 2007, CAGR of 6.4%

World Crude Steel Capacity 2000~10



Source: German Steel Federation and IISI verifications



# Key Messages

- After years of relatively stable growth, NAFTA steel producers now face severe deterioration with regard to current demand, and extreme uncertainty with regard to near-term demand.
- Economic turmoil is pronounced in key market segments – automotive, construction, appliances.
- There is a high risk of over-capacity in offshore markets and foreign governments and producers may feel the need to use the export markets to counterbalance their weak domestic markets.
- In terms of exports, worldwide economic difficulties will impact export opportunities for NAFTA producers and their customers.
- In terms of imports, NAFTA governments must be alert to potential surges of unfairly-traded steel and steel-intensive products.



# Discussion Questions Regarding World and NAFTA Steel Market Conditions

- How long and how deep will the current financial crisis affect steel demand in NAFTA and the rest of the world?
- What steps can and should NAFTA governments take to prevent dumped and subsidized imports from flooding this market during a time of weak demand?
- Are there opportunities for NAFTA governments to coordinate with each other and with other governments to prevent unfairly-traded imports from disrupting markets worldwide?



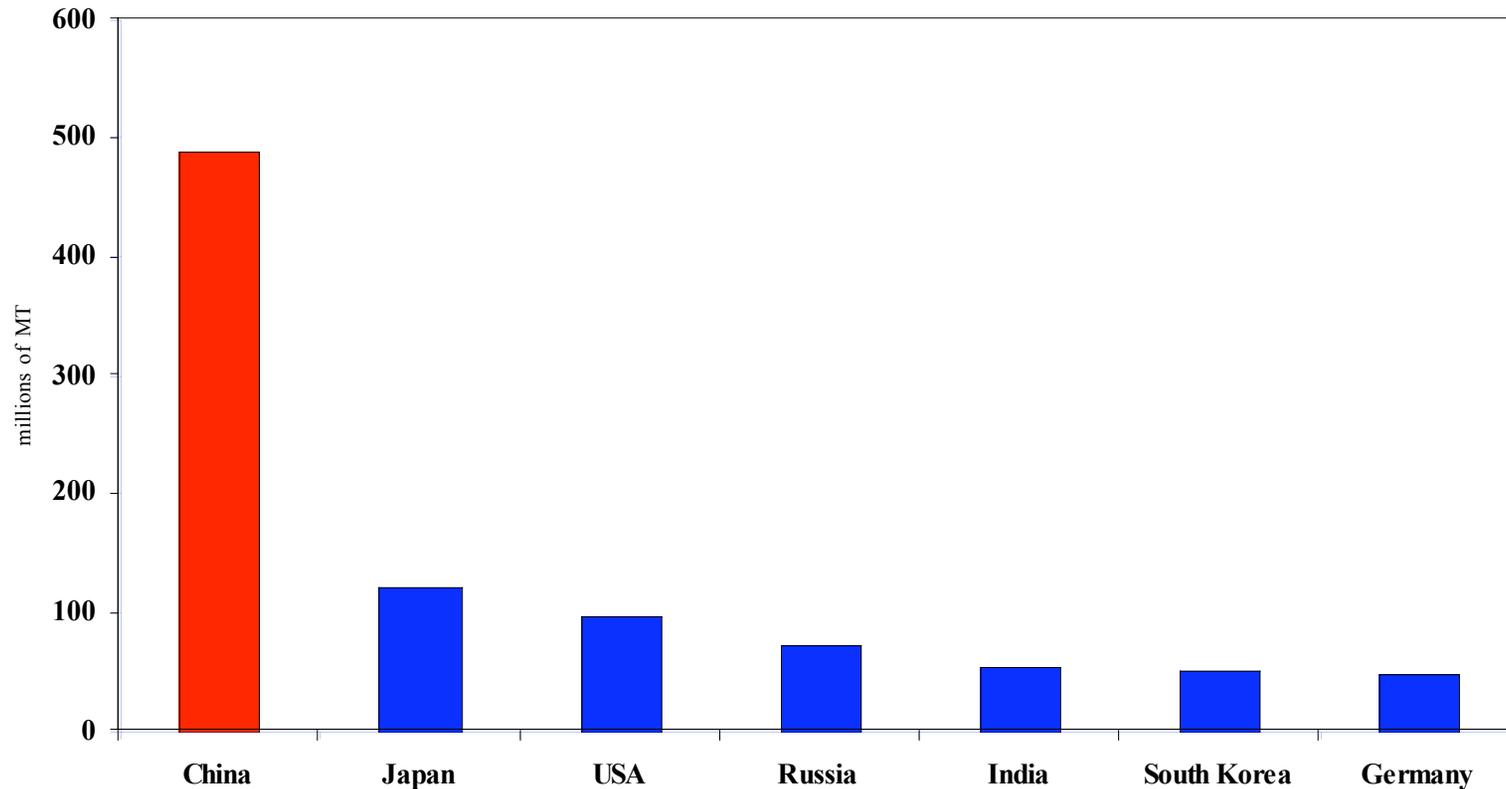
## Second Topic: China Trade and Industrial Policies

- China Is a Massive Net Exporter of Steel
- Subsidized Chinese Steel Capacity Significantly Exceeds Chinese Demand
- China's Excess Capacity Is Projected to Grow without Regard to Market Forces
- China Has Not Complied With Numerous WTO Obligations
- All of these Concerns Are Exacerbated by the Current Economic Crisis, Including a Slowdown in China



# Chinese Steel Production Far Exceeds that of Any Other Country

## 2007 Crude Steel Production

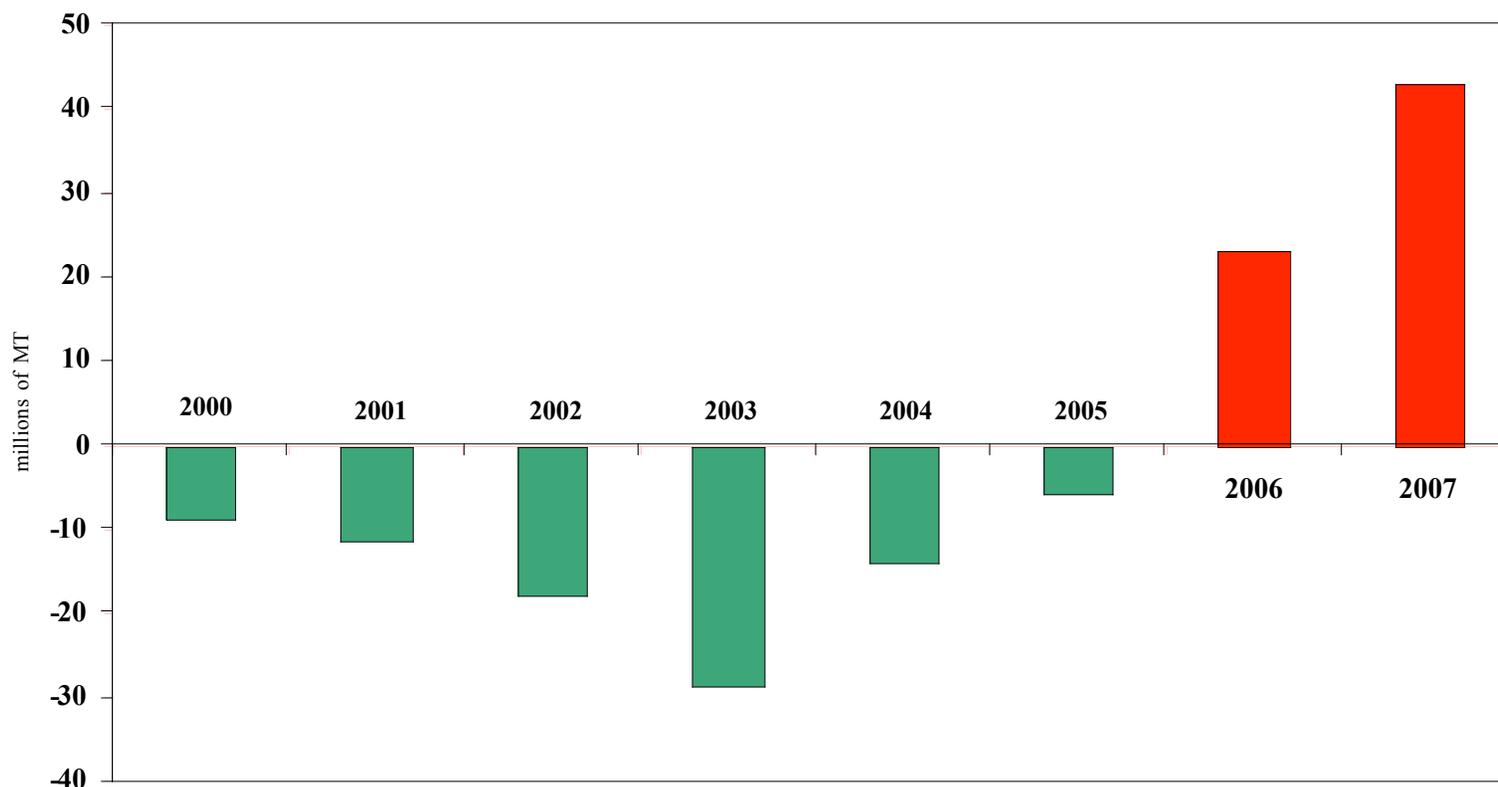


Source: World Steel Association "World Steel in Figures 2008: 2<sup>nd</sup> Edition" at 11 (2008).



# China Is Now a Massive Net Exporter of Steel

## China's Net Exports of Finished Steel Products, 2000-2007

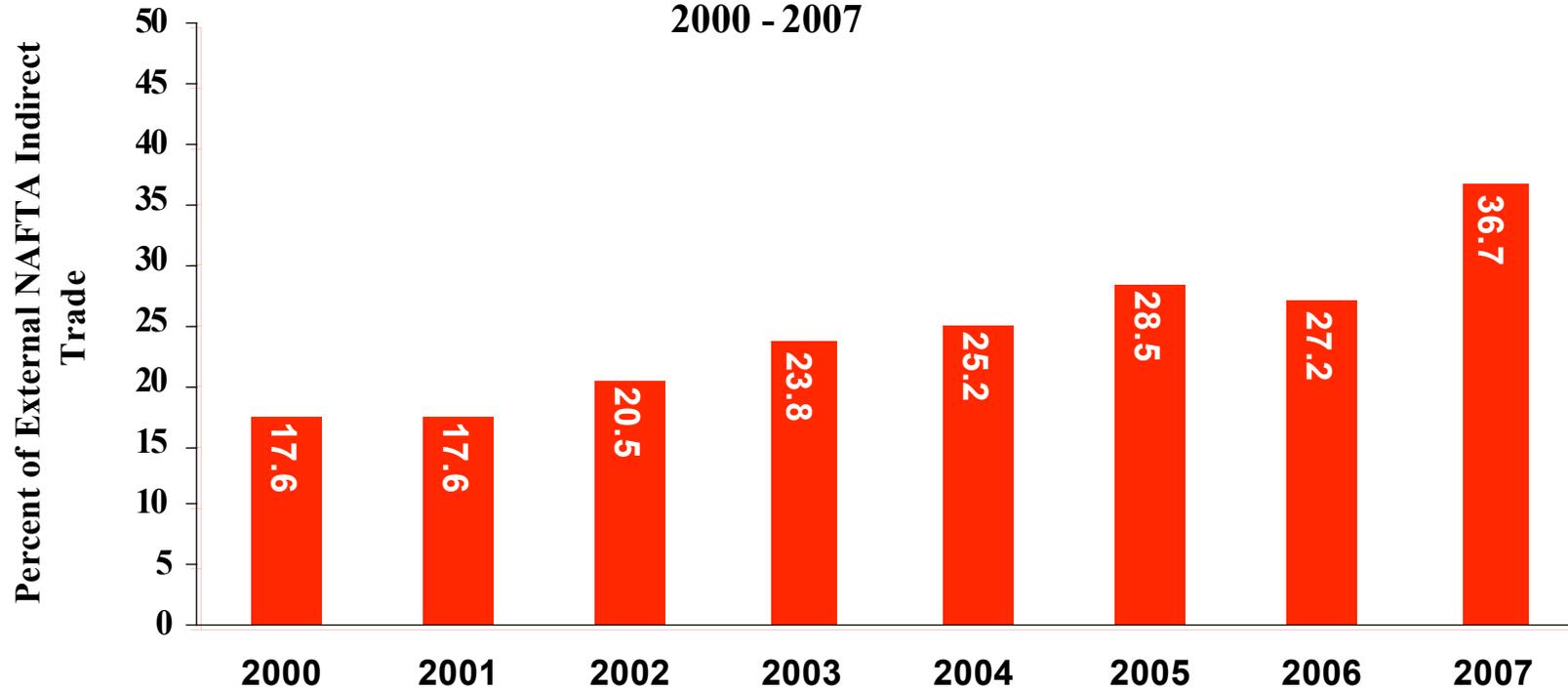


Source: World Steel Dynamics, "Global Steel Alert # 31" (Oct. 1, 2008) at 7.



# China Is Also Driving NAFTA's Indirect Steel Trade Deficit

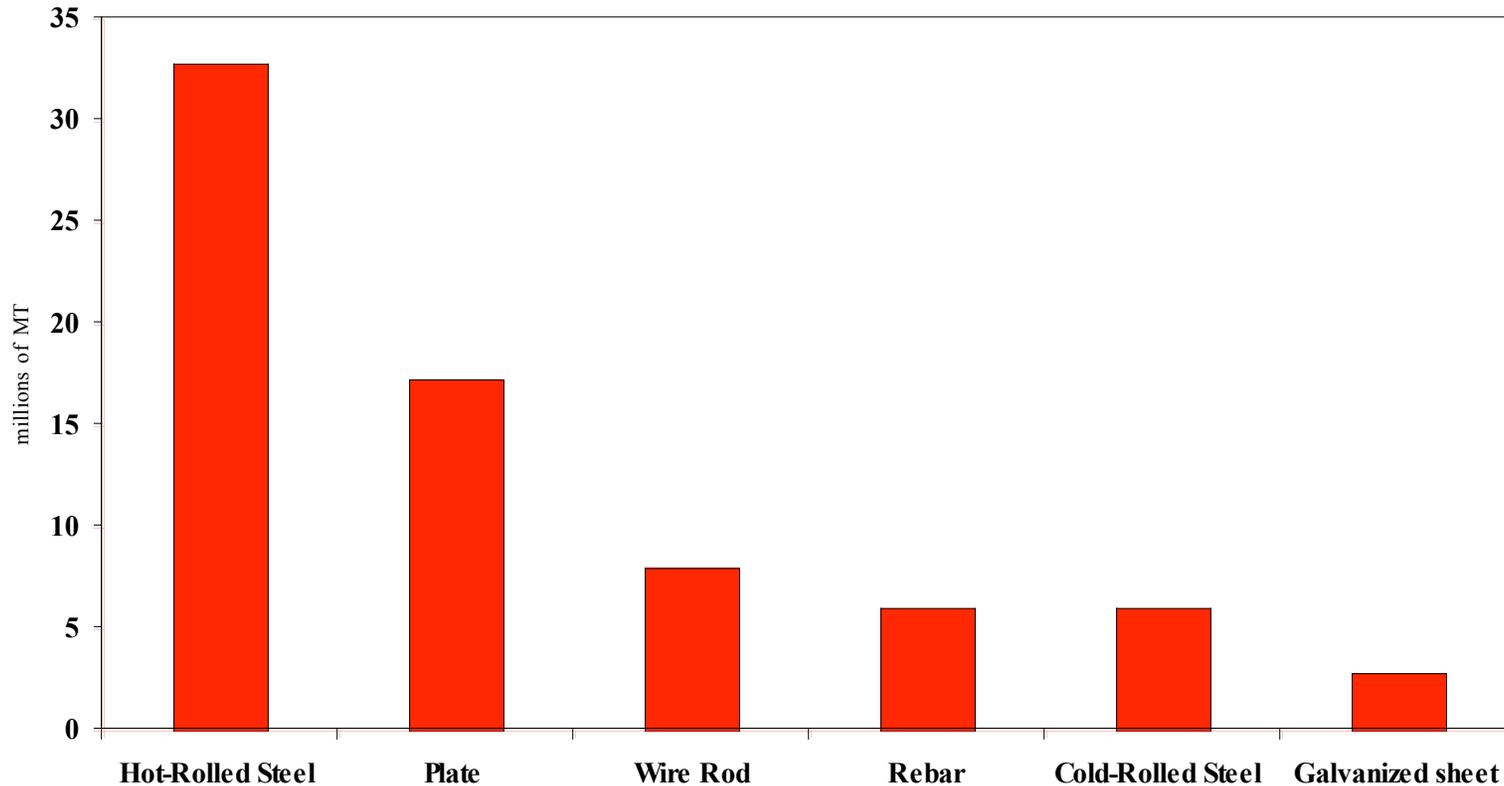
**NAFTA Indirect Steel Trade Balance with China  
Percent of Total External NAFTA Trade Deficit  
2000 - 2007**





# China's Capacity Now Exceeds Chinese Demand For Many Key Steel Products

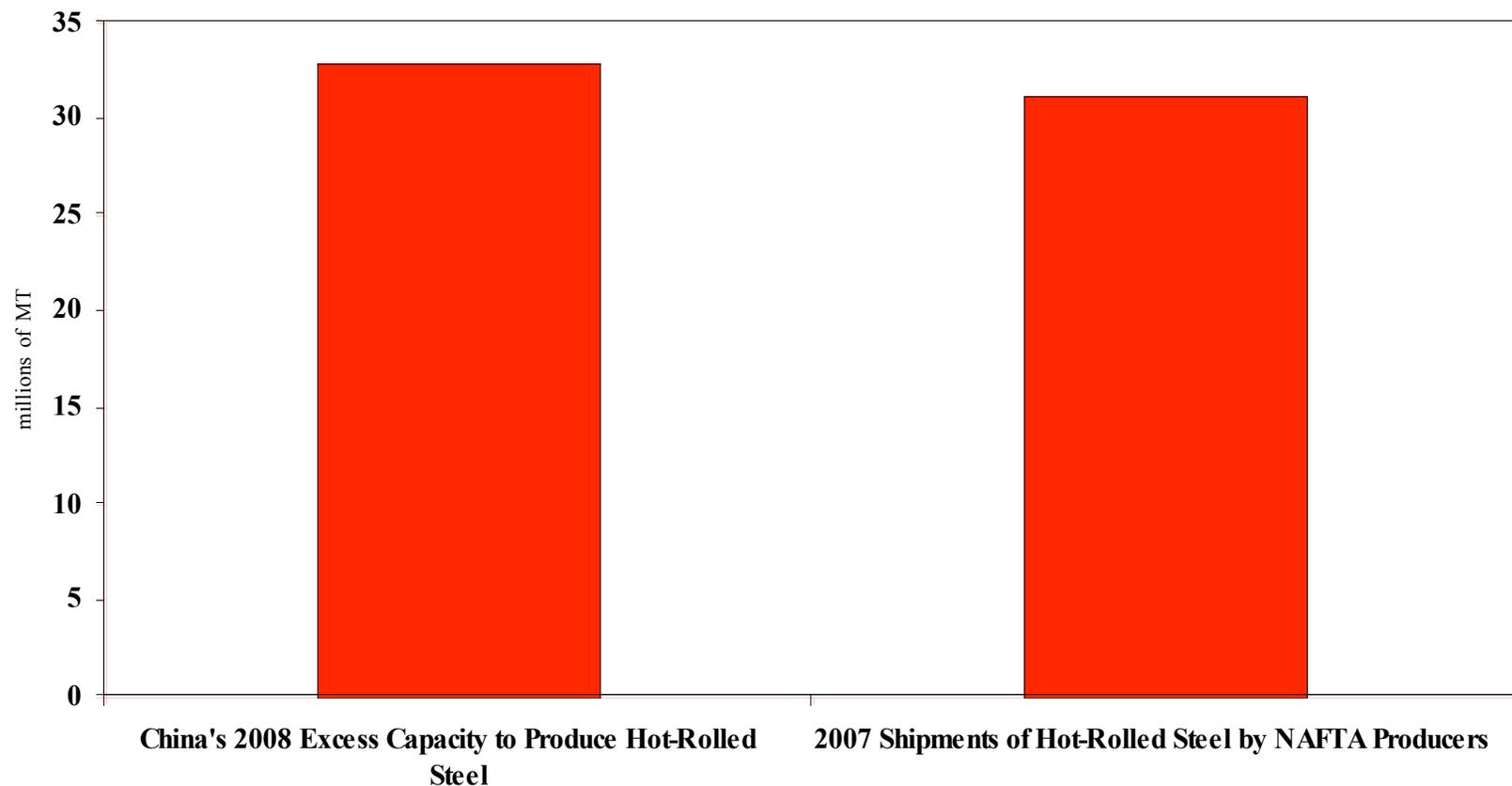
## 2008 Difference Between Chinese Capacity and Chinese Demand



Source: World Steel Dynamics, "Global Steel Alert # 31" (Oct. 1, 2008) at 17, 25.



# The Difference between Chinese Capacity and Chinese Demand for Hot-Rolled Steel Exceeds *Total* Hot-Rolled Shipments by NAFTA Producers

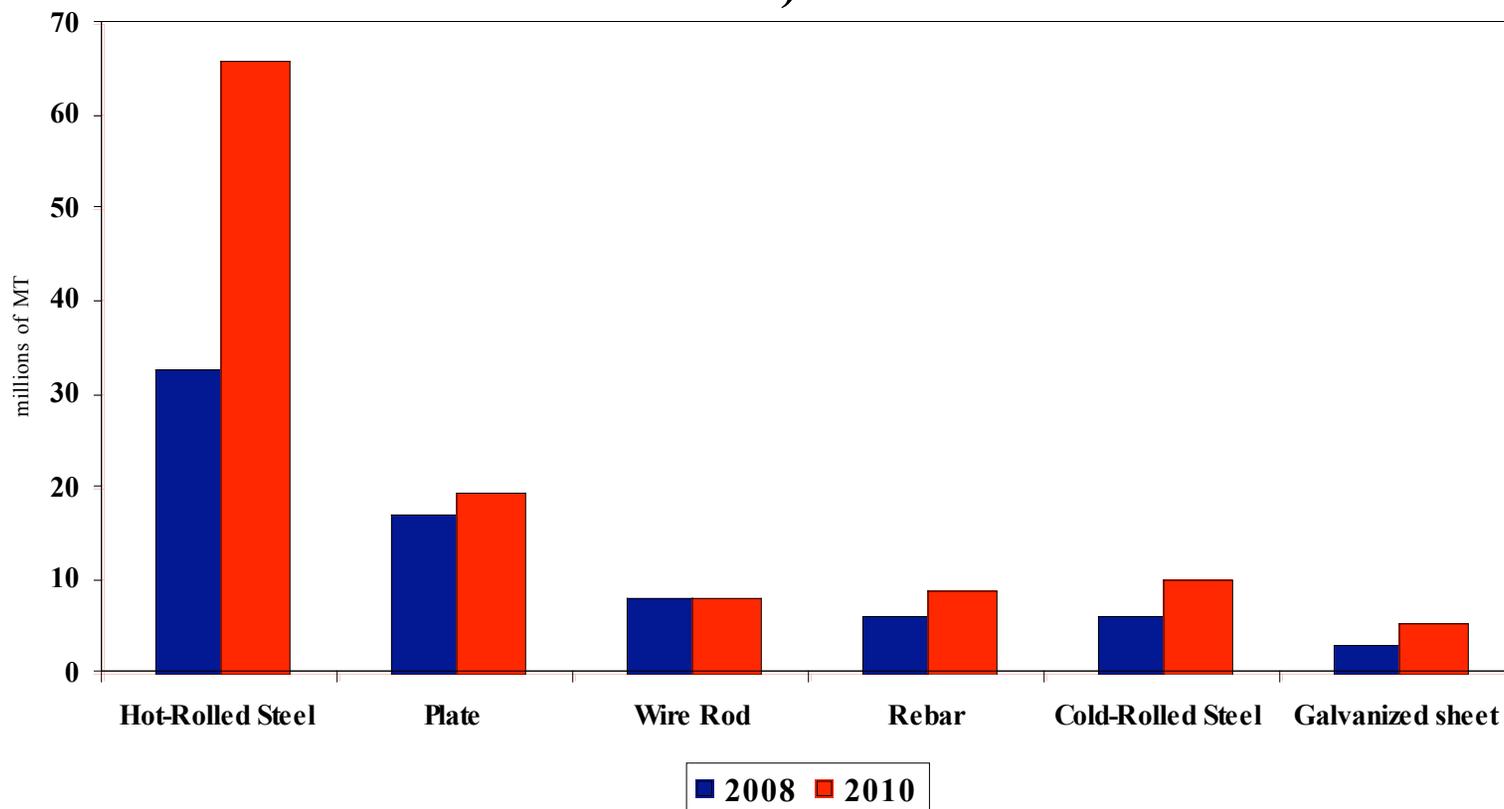


Source: China Excess Capacity Data from World Steel Dynamics, "Global Steel Alert # 31" (Oct. 1, 2008) at 17, 25; NAFTA shipment data from AISI.



# China's *Excess* Capacity Is Projected to Grow Over the Next Two Years

### China's Excess Capacity (the Difference Between Capacity and Chinese Demand) in 2008 and 2010

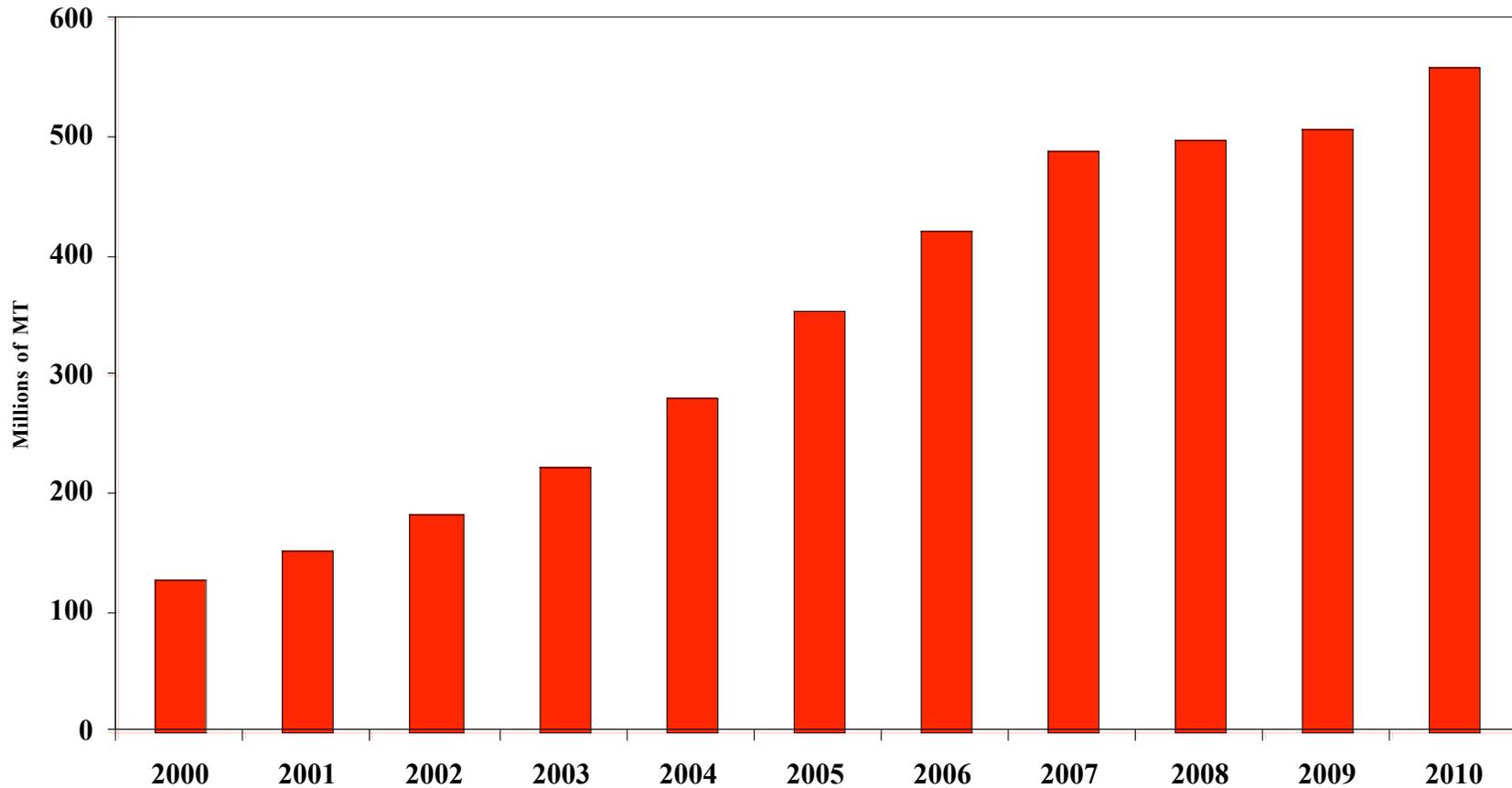


Source: World Steel Dynamics, "Global Steel Alert # 31" (Oct. 1, 2008) at 17, 25.



# Chinese Production Is Projected to Increase Through 2010

## Chinese Crude Steel Production, 2000-2010



Source: World Steel Dynamics, "Inside Track # 91" (Oct. 30, 2008) at 27.



# Chinese Demand Growth Is Slowing Dramatically

*“It now appears commodity prices are close to our Armageddon Case: assuming OECD economies are in recession in 2009, and China can only grow metals / commodities demand by 3% {per annum}. **This is the lowest level of demand growth in China for more than 20 years.**”*

-- Merrill Lynch, “Commodity Price Review”  
(October 25, 2008)



# AISI Recently Documented Numerous Continuing Problems with China's WTO Compliance

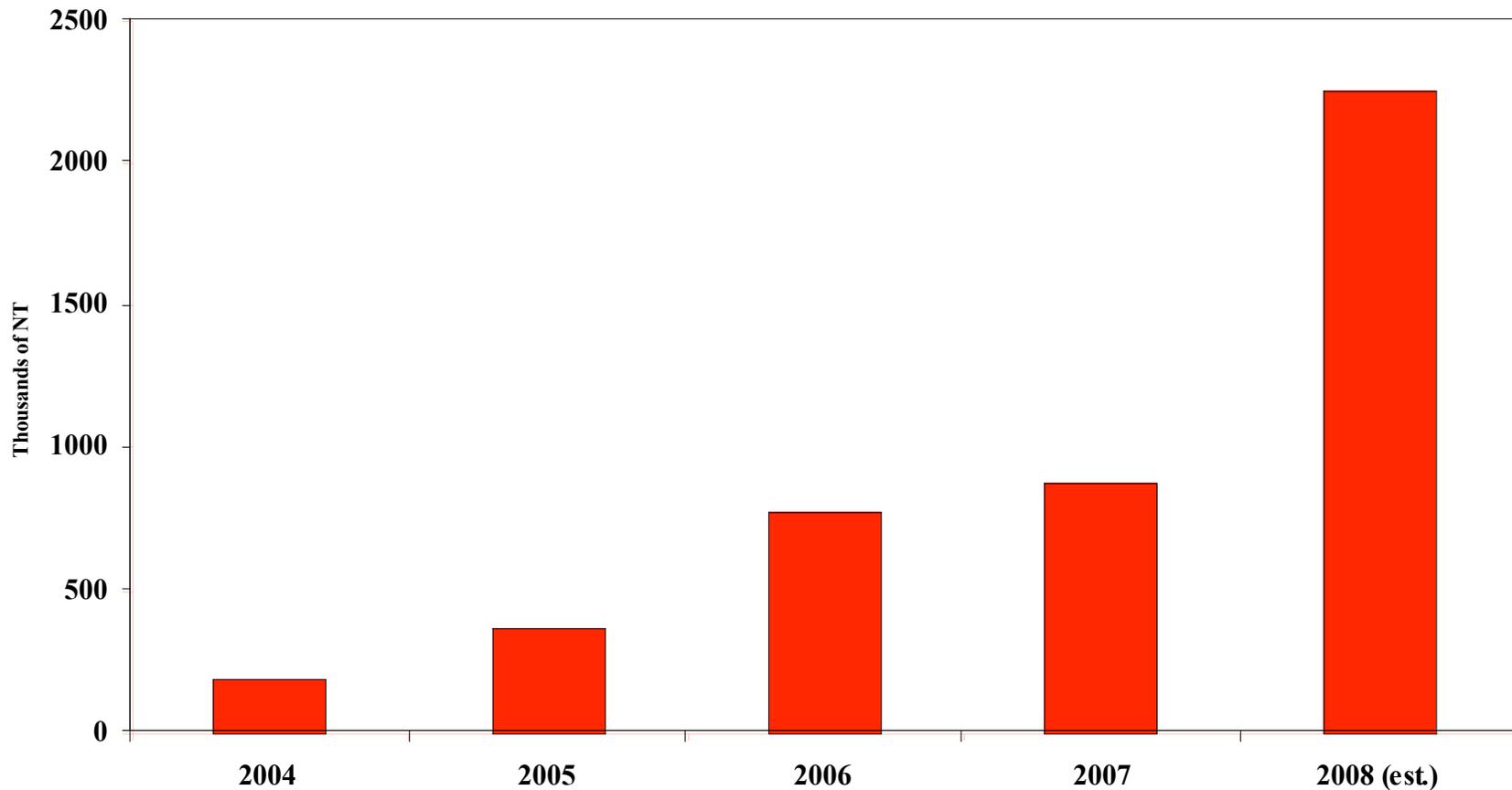
China continues to:

- provide *massive government subsidies* to its steel producers
- *influence decisions of state-owned enterprises*
- *restrict exports of key raw materials*
- *manipulate its currency*
- distort export flows by *manipulating its value-added tax system*
- have significant problems with *product safety*
- violate other countries' *intellectual property rights*



# China's Differential VAT Rebates Encourage Exports of Higher-Valued Products Such as OCTG

## Chinese Exports of OCTG to the NAFTA Region, 2004-2008



Source: World Trade Atlas. Estimate for 2008 based on January to September data. Note that while China has eliminated the VAT rebate for some steel products, it maintains a 13 percent rebate for exports of OCTG.



## Unfair Trade from Other Countries Is Also a Major Concern

- **Korea:** has *a long history of engaging in unfair trade*; currently being hit particularly hard by the global financial crisis;
- **Ukraine:** rapidly becoming a major player in this market; *shipments to the United States soared almost 1400 percent from 2003 to 2007*;
- **Russia:** *shipped over 3.3 million NT of steel products to the U.S. market as recently as 2006*; flooded the U.S. market during the Asian crisis; currently facing economic turmoil due to global financial problems;
- **India:** implementing a government policy that will *more than double steel production by 2012*, and will make India the world's second-largest steel producer by 2020.



## Since 201 Relief Was Revoked, U.S. Imports of Steel Products from Korea, Ukraine, Russia, and India Have Surged

Source	2003 Imports (NT)	2007 Imports (NT)	Increase (%)
<b>Korea</b>	1,362,972	1,928,903	41.5
<b>Ukraine</b>	83,392	1,247,764	1,396.3
<b>Russia</b>	338,373	1,170,193	245.8
<b>India</b>	449,705	878,293	95.3



# Key Messages

- The size and pace of growth of China's steel industry are not the result of market forces. They have been deliberately brought about by government policy and subsidization.
- Not surprisingly, Chinese government subsidies and other market interventions have resulted in an industry where capacity far exceeds Chinese demand.
- Chinese subsidized exports are distorting steel markets worldwide.
- NAFTA governments must strictly enforce trade rules and insist that China comply with all of its WTO obligations.



## Discussion Questions Regarding China Trade and Industrial Policies

- How are steel markets worldwide affected by the fact that the world's largest steel producer and exporter is a non-market economy?
- In the late 1990s, a financial crisis in Asia and an economic depression in Russia led to an enormous surge of dumped and subsidized imports that caused severe harm to NAFTA steel producers. In the context of today's global economic crisis, what can NAFTA governments do to ensure that China's subsidized capacity does not result in a similar devastating surge of imports of steel and steel-containing products?
- What steps can NAFTA governments take to convince China to comply fully with all of its WTO obligations?



## Third Topic: Major Developments and Concerns about Raw Materials

- Foreign Governments Are Distorting Trade in Raw Materials
- These Practices Place NAFTA Mills at an Unfair Disadvantage
- Market-Based Trade in Raw Materials Is Essential to Fair Competition in NAFTA Markets
- NAFTA Governments Should Explore All Options to Address this Problem



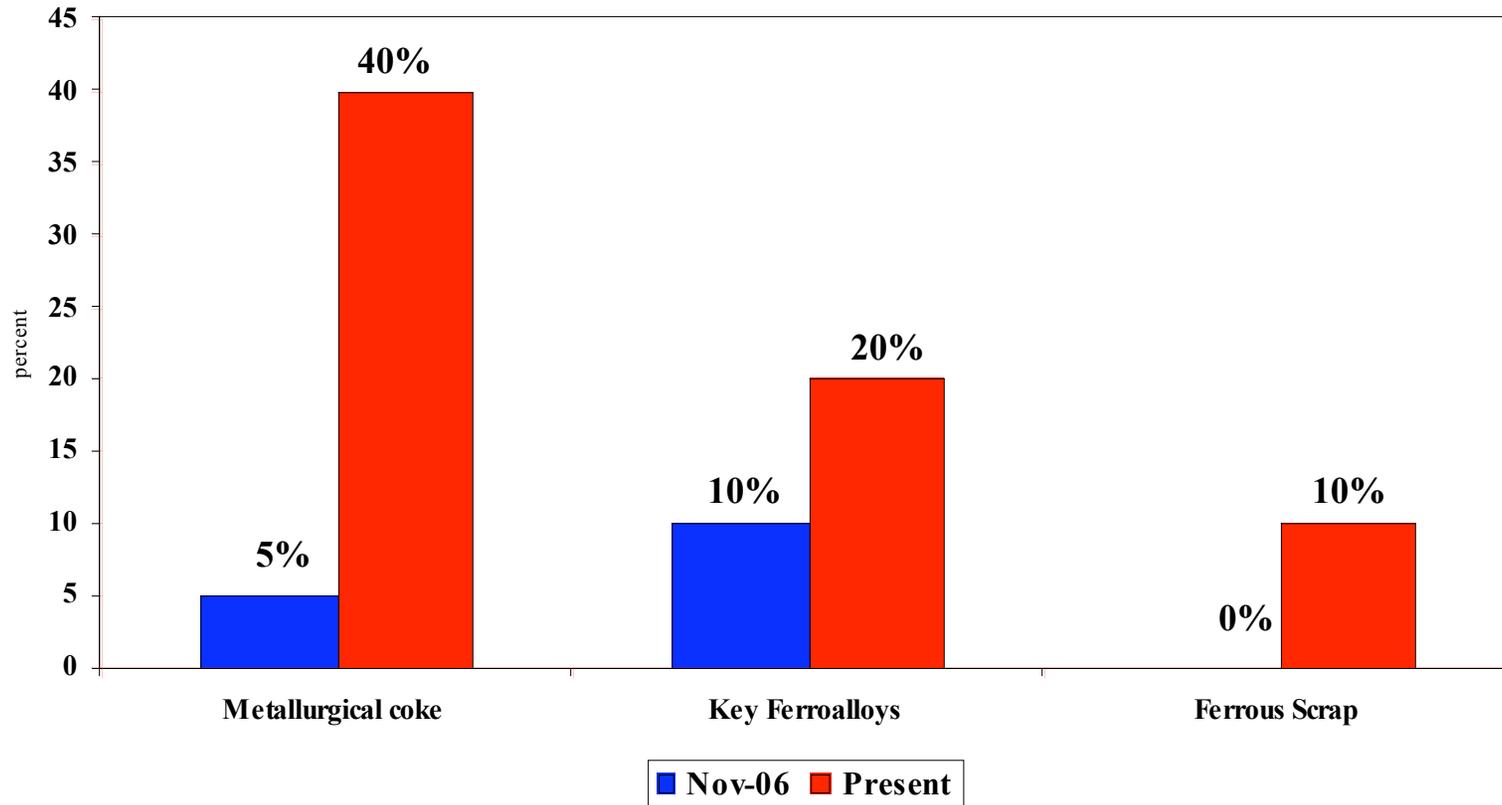
# Market-Distorting Policies: China

- Export quotas on steel inputs (in violation of WTO obligations)
- Export taxes on steel inputs (in violation of WTO obligations)
- Export licensing requirements
- Government-supported financing for raw material projects
- Barriers to foreign investment in China's raw material resources
- Government intervention in global raw material transactions



# China Has Increased Export Taxes Significantly On Key Raw Material Since November 2006

### Export Duties for Key Raw Materials, November 2006 and Present





# Market-Distorting Policies: Russia

- Export duties on ferrous scrap and other key inputs
- Uneven enforcement of customs regulations
- Selective enforcement of environmental rules
- New legislation severely restricting the ability of foreign firms to invest in “strategic” Russian industries



# Market-Distorting Policies: Ukraine

- Export duties on ferrous scrap
- Failure to comply with WTO obligations to eliminate export restrictions
- Registration requirements and fees for exporters
- Restrictions on land use rights
- Government subsidies to the mining sectors



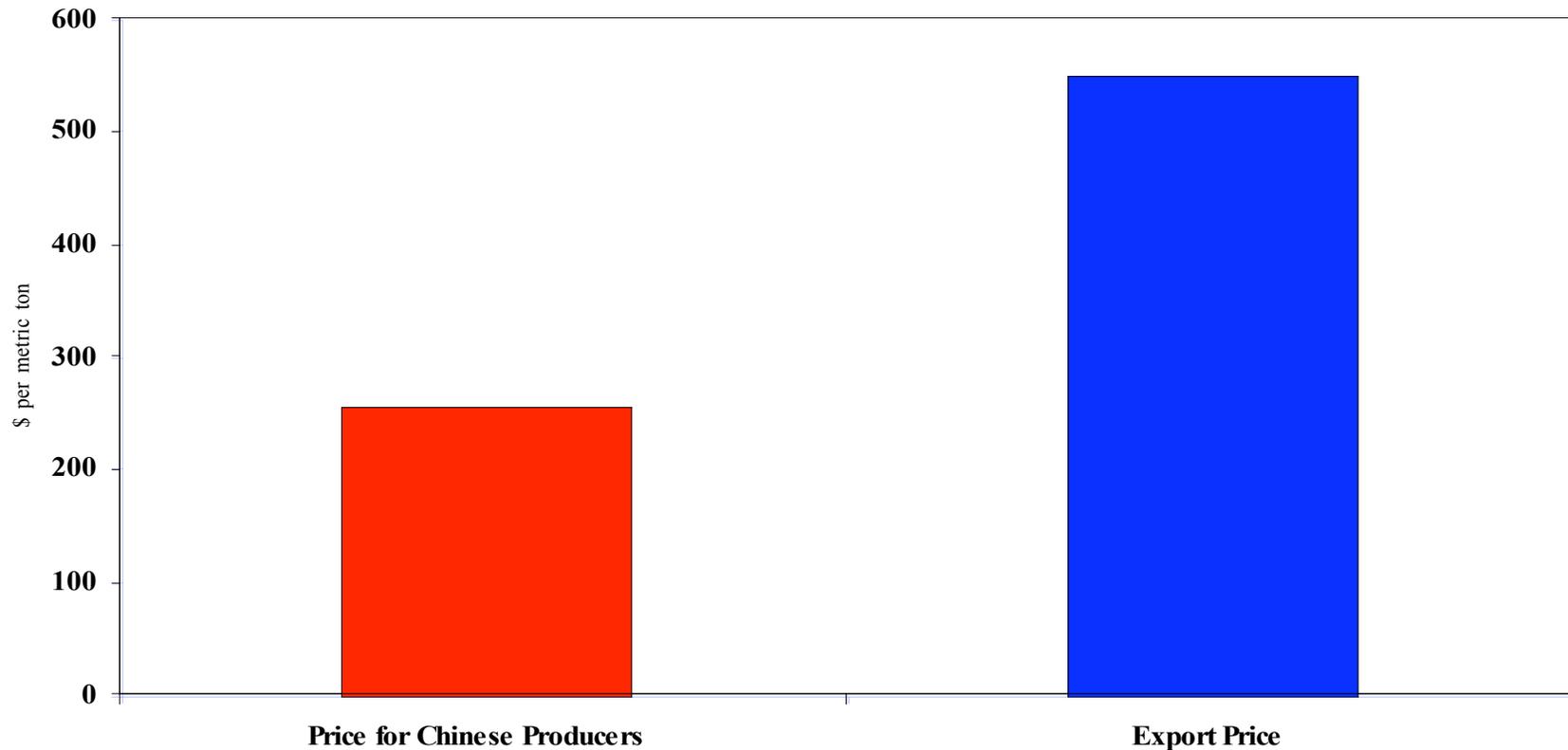
# Market-Distorting Policies: India

- Export tax on all iron ore, pig iron and ferrous scrap
- Provision of subsidized iron ore and coal to Indian steel producers
- Requirement that exports of most raw materials pass through State Trading Enterprises
- Significant regulatory hurdles to foreign investment



# Foreign Government Restrictions on Raw Material Exports Place NAFTA Producers at a Significant Disadvantage

### Chinese Coke prices, October 2008



Source: World Steel Dynamics, Inside Track # 91at 12 (Oct. 30, 2008)



# Key Messages

- Countries such as China, India, Russia, and Ukraine have taken numerous steps to restrict trade in key steel inputs, including coke and critical ferroalloys.
- These steps often place NAFTA producers at a significant and unfair disadvantage.
- NAFTA governments should pursue all available options to stop market-distorting practices in raw materials, including WTO litigation where necessary.



# Discussion Questions Regarding Trade in Raw Materials

- What burdens are being placed on NAFTA producers as a result of foreign market-distorting practices with regard to raw materials?
- What opportunities are there for NAFTA governments to address these market-distorting practices (e.g., bilateral consultation, cooperation with other governments, WTO litigation)?



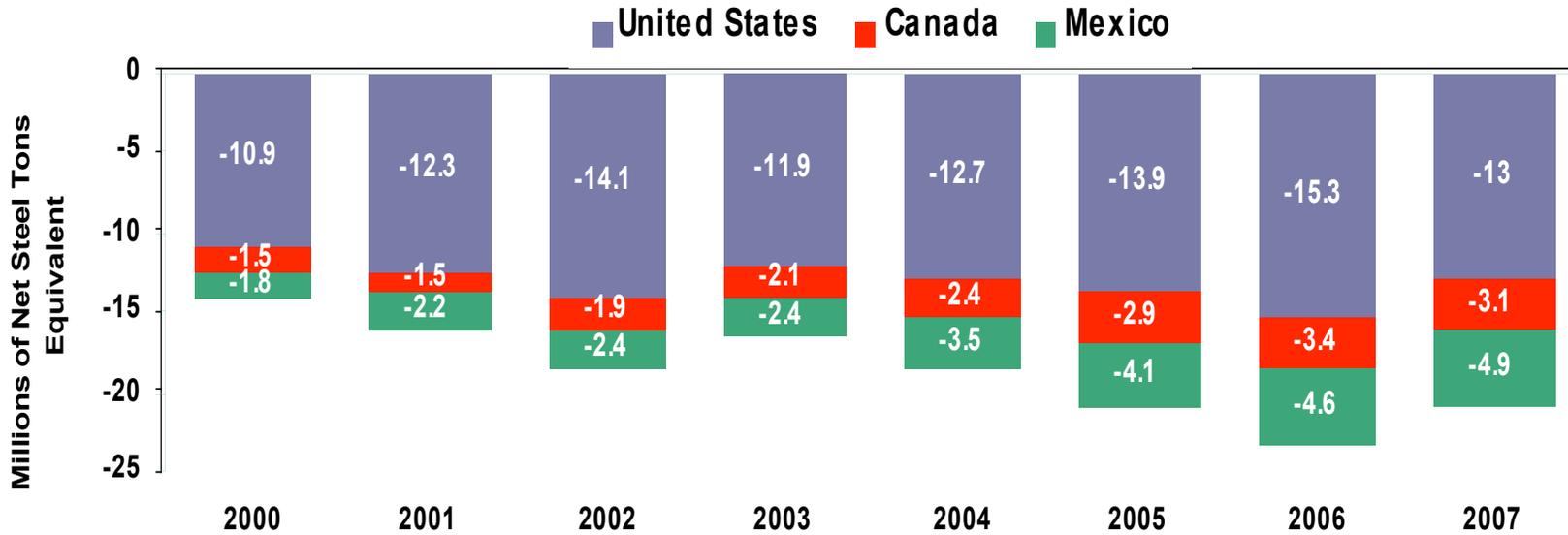
## Fourth Topic: Trade and Climate Change

- Climate Change Policy *Is* Trade Policy
- Climate Change Legislation Could Put Manufacturers in Jurisdictions with More Demanding Environmental Regulations at a Significant Disadvantage
- If NAFTA Governments Do Not Successfully Address the “Carbon Leakage” Issue, Climate Change Legislation Will Result in Higher Greenhouse Gas Emissions Worldwide
- NAFTA Producers Are Concerned about Regulatory Overlap and Confusion Resulting from State and Provincial Actions that Are Separate from National Actions



# NAFTA Manufacturers Face Intense Competition from Imports

NAFTA Indirect Steel Trade Balance with Rest of World  
(excluding intra-NAFTA trade) 2000 - 2007



Source: AISI Indirect Steel Trade Report, Global Trade Atlas



## NAFTA Producers Support Efforts to Develop a Global Steel Sectoral Approach on Carbon Emissions

- The Sectoral Approach would apply to all major-steel producers, including those in the BRIC countries
- World Steel Association plan includes a commitment to multilateral R&D to create “breakthrough” technologies
- Initiative was presented at the UNFCCC meetings in Bali in December 2007
- NAFTA governments should support a global steel sectoral approach



## In the Absence of a Global Agreement, National Governments May Act Independently

- NAFTA governments must be prepared to address competitiveness impacts as an essential component of their domestic climate change policies
- One set of options entails “border adjustment” measures
- Other options involve allocation or pricing of emissions credits
- Other governments, including the EU and Australia, are also looking at these issues



# Key Messages

- Any climate change regulatory regime must address the competitiveness issue to ensure that manufacturing does not simply move offshore to countries like China.
- Failure to address the competitiveness issue will lead to higher carbon emissions worldwide.



# Discussion Questions Regarding Climate Change

- What steps can NAFTA trade and industry authorities take to ensure that competitiveness concerns with respect to climate change are fully addressed in any regulatory action?
- What is the outlook across the NAFTA region for climate change policy (cap-and-trade, intensity-based, voluntary commitments) and how does that compare with trade partners?
- Other countries, including the EU, have shown concern with trade impacts of climate change regulations. Are there prospects for NAFTA governments to work more closely together and with others to address the climate issue and competitiveness concerns?



# Critical Alerts

In recognition of the seriousness of the economic downturn and the need to avoid a recurrence of the recent steel crisis, need to address all of the following points in a *proactive manner*:

- Strong and effective enforcement of trade laws throughout the NAFTA region
- A more effective approach to dealing with market-distorting practices in China
- Ensure that market forces operate properly with respect to raw materials
- Ensure that legislation to limit carbon emissions does not place NAFTA producers at an unfair disadvantage
- Reverse the widening North American indirect steel trade deficit with China