ASA MATERIALS MARKET DIGEST
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MARKET OVERVIEW

Carbon Steel. After a summer without price changes, flat-rolled steelmakers are increasing their quotes for October deliveries. With the major mills going up $20 to $30 per ton, hot-rolled sheet will go to $520-540, cold-rolled to $620-630 and hot-dip galvanized at $750-760. American steel mills continue to operate in the high eighty percent range, but steel service centers are trimming inventories, thereby slowing their demands on the steel mills.

Tubular Goods. The *AMM* research department has published a comprehensive market report on oil country tubular goods. The report forecasts sharp increases in demand, especially for high performance alloy and seamless materials suitable for harsh drilling conditions. It also names Latin America, the Middle East, former Soviet satellite states and especially Africa as growth markets for OCTG.

Stainless Steel. All three of the stainless Big Three announced *reductions* in materials surcharges ranging for popular types from 36 to 48 cents per pound. Nickel prices seesawed during August and finished the month on the down side. But there are growing concerns that molybdenum prices will rise in the face of increased demand and limited supplies.

Copper. Prices of the red metal also fluctuated sharply in August, driven largely by stock market selloffs and recoveries. Some labor problems still persist in Latin America, but the industry's biggest worry involves substitution of plastic pipe for copper tubing in residential construction. This year copper's substitution deficit is expected to reach 160,000 to 170,000 tons.

Resins. In most product sectors, price increases are tapering off. Demand remains firm but monomer and feedstock prices are easing in a number of formulations.

CARBON STEEL

PRICING AND OPERATIONS. *Pricing.* The steel industry's pricing mechanism was idle for most of the summer months. But as mills prepared their sheets for October deliveries, activity quickened. The first increase came in ferrous scrap at Chrysler's late-July auction of factory bundles. Scrap prices had been flat since May, but when the July bidding was done, factory bundles were up $10 per ton. Several weeks later a second Chrysler auction did even better, posting an additional gain of $18 per ton. These successive increases were driven by a tight supply situation in consumer inventories as well as rising prices for alternative charging metals such as pig iron.

After little price action during the summer months, major U.S. mills readied for what many see as a strong upsurge in flat-rolled demand in the final quarter of 2007. This expectation triggered higher prices for October delivery, with most mills going up $20 or $30 per ton. On the spot market these increases will result in a price of $520-$540 for hot-rolled sheet, $620-630 for cold-rolled, and $750-760 for hot-dip galvanized.

Some market watchers question whether current and prospective demand is sufficient to sustain the announced increases. Others argue that the increases are not intended to be demand-driven but reflect the mills' need to recoup higher scrap costs. Whatever underlies the recently announced prices, a majority of observers agree that they are likely to stick when October deliveries get under way.

Operations. Activity in U.S. steel mills began August on a downgrade, with weekly production falling from 89.5% of capacity in late July to a low of 86.3% in the week of August 11. But toward month-end the industry regained the lost ground as plant utilization rose to 89.3%. At that point cumulative U.S. production of raw steel for the current year totaled 68.926 million tons, 5.3% below output at the same point in 2006.

After a promising report in June, the Institute for Supply Management's July survey showed some reduction in buying plans. As of the June poll, 20% of the responding steel buyers indicated that they would be increasing their orders in the next three months. By the July survey that number had fallen to 15% of the reporting ISM members. Similarly, the June survey found 10% of the buyers planning to increase steel inventories over the next three months. By July that figure was down to 5%.

These survey findings dovetail with the most recent report of the Metal Service Center Institute. This organization's July poll showed service center inventories down 3.3% from June and 12% below the level of July 2006. The Institute's poll also showed that service center shipments in June trailed the preceding month and were 6.3% below shipments in June of 2006. Additionally, a market analyst quoted by *American Metal Market (AMM)* predicted that service center stocks would continue to decline well into this year's final quarter.

CHINA. Chinese trade policies, many of them unfair, illegal or both, are stirring a growing level of militancy in and out of the U.S. government. In Congress all sorts of legislation has been introduced for the purpose of bringing the Chinese to book. And even in the White House, where hands-off has been the rule in dealing with trading partner shenanigans, there is a growing level of impatience and even hostility.

This altered mood is reflected in the "U.S.-China Steel Dialogue," one of the World Trade Organization's mechanisms for resolving trade disputes. As structured by the WTO, this "Dialogue" is a surrogate for nose-to-nose negotiation and operates something like a high school debate. Under the rules, first one side states its case, then the other airs its views, criticizing the opposition and restating its position, but never in the give-and-take format where most negotiations bear fruit.

The Chinese are using this forum to push back against growing U.S. impatience with China's trade practices, using such pejorative terms as "misconceptions," "propaganda" and "hypocrisy." Among the key areas of dispute are China's oft-repeated statement that it is trimming its steelmaking capacity to prevent overproduction and the flooding of world steel markets.

In point of fact the Chinese have not offered a bit of evidence that this goal is being implemented in any way. Quite the reverse. At one dialogue session a Chinese delegate argued that China needs half a billion tons of annual steel production to support its 1.3 billion population. But no mention was made of the huge outflow of Chinese steel to every part of the globe.

Notwithstanding growing toughness in U.S. political and business circles, some in and out of the government continue to fear that the U.S. is going too far in standing up to the Chinese. Their principal concern, featured in a recent issue of London's *Daily Telegraph* newspaper, is that the Chinese will "punish" the U.S. by liquidating its entire $1.3 trillion in dollar reserves. Such a move, the doves argue, would flood the world with U.S. currency and drive our economy into deep recession.

Actually, such a move by China would be suicidal. It would be the equivalent of assassinating one's best customer, Without the steady flow of U.S. trade dollars, China's industrial growth would grind to a halt, many of its factories would be forced to close for want of customers, and millions—perhaps tens of millions—of Chinese would be thrown out of work, Beijing's worst nightmare!

TUBULAR GOODS. *AMM's* research staff recently completed a comprehensive study of the oil country tubular goods (OCTG) market outlook for the next five years. The complete study is available for purchase from *AMM* and provides detailed analysis of such developments as the following:

- The OCTG market has enjoyed unprecedented growth in the past several years because of stepped-up drilling activity in the U.S. and globally, as well as very attractive gross profit margins, often in the 40-50% range.

- Demand for OCTG will remain strong. But the growth will be largely in high-performance alloys rather than commodity grades. This reflects rising activity in deep formations and offshore sites where drilling conditions are the harshest.

- Generous OCTG profits have attracted new suppliers for high-performance piping products. The report forecasts demand for an additional 5 million tons of seamless pipe annually as well as 300,000 tons of welded pipe—both figures double the tonnage now in demand.

- After 2007, OCTG production will begin to outpace demand, even for high-performance products. This will generate pressure on pricing and slow the rate of price increases.

- Major offshore markets for OCTG will include the NAFTA area, the Middle East, the former Soviet Union countries now constituting the Commonwealth of Independent States and most importantly, Africa.

- China has every intention of becoming a major player in the OCTG market. Its major producers in this product sector plan to add 1.5 million tons of new capacity in each of the next three years.

August proved to be a growth period for the U.S. rig count. From 1,781 active sites early in the month the count grew to 1,818 operating units, the highest yet in 2007 and 3.4% better than at the same week in 2006. But in Canada the count continued to decline, closing the month at 319 rigs, 34.8% below the year-ago total. The decline in Canadian operations is largely structural and reflects a shift to greater production activity in Canada's extensive tar sands regions.

Also on the subject of Canada, that country is considering the imposition of anti-dumping duties on Chinese seamless carbon and alloy casings, both widely used in that nation's oil fields. After a complaint by Algoma Tenaris and others, the Canadian International Trade Tribunal launched an investigation that could likely lead to anti-dumping duties or other sanctions. Typically, Chinese authorities expressed "disappointment" at the Canadian move.

STAINLESS STEEL

The stainless steel news in August largely concerned fluctuations in the price of nickel and its impact on stainless prices and consumption. After trading on the LME for several weeks in the range of $26,000 to $27,000 per metric ton, the key alloying metal got caught in several downdrafts generated by sharp stock selloffs on Wall Street and elsewhere. But after each dip the metal recovered and ended the month up slightly at $27,400. This was just one-half of the price prevailing in mid-May of this year.

Molybdenum, another alloying metal in high-performance stainless, was also in the news. In its August 13 edition, *AMM* reported that moly consumption was growing at 6% annually, the equivalent of 24 million additional pounds per year. The publication noted that no significant new sources of the ore will go on line this year and that China has announced sharp cutbacks in its exports. Normally these conditions would be exerting heavy upward pressure on prices, but such has not yet been the case. In a stainless market that *AMM* characterized as "dead," traders were barely able to sustain the existing price of moly, let alone realize any increase.

The plunge in nickel prices is already starting to be a factor in stainless steel pricing. Early in August AK Steel announced substantial reductions in its materials surcharges. The cuts included 35.88 cents for Type 304, bringing the charge down to $1.53213, Type 316, down 47.75 cents to $2.9480, and Type 321 down 40.83 cents to $1.6822. The other Big Three stainless producers, Allegheny and North American, quickly followed AK's lead. Additional cuts are expected for October deliveries, when the mills' surcharge formulas will fully reflect the halving in the price of nickel.

Early in August, *AMM* reported strong ongoing demand for low-nickel and no-nickel stainless formulations, a group of alloys used as cheaper substitutes for 300 series alloys in some stainless applications. Then, toward the end of the month, the publication ran a front page story saying that Type 201 and other non-nickel bearing alloys were "losing their luster." It quoted numerous service center executives who reported slack demand or none at all, for alloys in the 200 series.

COPPER

Prices. Copper prices spent most of August riding a seesaw. But for once the fluctuations were not driven by labor problems, though these still persist. As in the case of nickel, the culprit in the month's copper selloffs was the stock market. Often when stocks take a dive, investors switch funds into commodities and other tangible assets. But in the convoluted logic of the copper trader, falling equity prices were interpreted as a sell signal for the red metal.

In the first of the month's several stock "corrections," copper on the LME sold off $210 per tonne to close at $7,640. A week later another selling wave hit Wall Street and the three-month LME contract dropped another $330 to close at $7,310. That decline amounted to a minus 4.6% and proved to be the lowest price in almost a year. After a few trading days during which the price rallied a bit, the bears once again took over and the red metal received a prodigious hit—down 7.7% to $6,750. Toward month end the price had recovered part of the preceding declines, but closing at $7,010 it fell far short of the $7,970 at which the August market opened.

Labor. Strikes did indeed contribute to copper's price recovery during the turbulent month recently ended. But their impact was limited. This was particularly true of labor actions at three Grupo Mexico venues. These strikes have been declared illegal by an arm of the Mexican government, but little action has been taken to enforce this ruling. In addition, management has adopted a somewhat conciliatory posture regarding the strikers, a rare development which sometimes precedes settlement. Elsewhere, a Peruvian miners strike has generated much posturing but little in the way of negotiation progress. However, even a prolonged walkout there will have only a modest impact, if any, on copper prices.

Markets. The housing slump has proved to be a double whammy for the copper market. Not only are far fewer new homes being built, but those that do go up are less likely to use copper plumbing. That's the message of John Barnes, a prominent consultant to the copper industry.

This source estimates that materials substitution in residential plumbing cost the copper industry 120,000 tons last year. This year the substitution deficit is expected to reach 160,000-170,000 tons. Barnes notes that the high cost of copper is only one reason for the substitution. In addition he cites for plastic pipe the advantages of minimal installation times and little installer skill required.

Scrap. The market for scrap copper and brass has been heavily impacted by a Chinese government campaign against customs hanky-panky on the part of importers. It seems that many in this business have made a practice of "salting" their incoming containers of high-grade scrap with a top layer of lesser quality. The buyer then declares the entire container at the cost of the cheaper scrap used for camouflage.

Chinese customs officials apparently either just tumbled to this widely used scam or just lately decided to do something about it. In either case, they have launched a massive crackdown, ordering incoming vessels to await boarding and inspection before releasing their cargos to the buyers.

Needless to say, this process has created monumental traffic jams in major Chinese ports. The laborious container-by-container searches now in progress have proved to be a logistic nightmare that has driven many would-be scrap importers out of the market. The net effects have been a buildup of unsold copper and brass scrap in U.S. yards as well as the imposition of heavy price pressures on domestic scrap supplies. As August drew to a close there were indications that the gridlock in Chinese ports is starting to clear. But it will be several weeks more before the scrap industry in China reverts to business as usual.

RESINS

The following report is abstracted from the monthly price report of *Plastics Technology*, the leading technical and marketing publication serving the resin industries.

Polyethylene. PE price increases appear to be near an end as suppliers' efforts to impose and additional 4-cent increase is meeting strong resistance, and feedstock quotes are leveling off.

Polypropylene. Price increases went into effect in July and August and another boost is pending. While domestic demand is essentially flat, exports are booming, especially to Latin America and Africa.

Epoxys. Despite demand growth of 6-7% annually, prices are likely to remain flat because of overcapacity at the producer level. The last increase that stuck was in May and no major effort to increase prices is in the offing.

Polyvinyl Chloride. Two major suppliers announced a September 1 increase, but a third refused to go along, effectively aborting the attempted boost.

Polystyrene. Benzene prices are under heavy market pressure, softening the cost of feedstocks. As a result, the next price change may be a decrease.

PRODUCER PRICE INDEXES – KEY INDUSTRY PRODUCTS

The table below is extracted from the Bureau of Labor Statistics' monthly report on the Producer Price Index or PPI. The Producer Price is defined as the price at which a given commodity or product is sold at its *first* sale after being manufactured, mined, refined or otherwise produced.

	Latest 07/07	Previous 06/07	Year Ago 07/06	2 Yrs Ago 07/05
PIPE, VALVES & FITTINGS:				
Copper & copper-alloy tube	320.3	315.3	349.8	156.4
Steel pipe & tube	167.9	165.8	166.0	156.4
Plastic pipe and fittings	200.8	198.4	214.5	157.1
Industrial valves – metal	173.4	172.8	160.1	145.9
PLUMBING FIXTURES:				
Vitreous china fixtures	103.5	103.6	101.4	99.8
Fixture fittings & trim	226.3	226.3	212.3	200.4
HVAC EQUIPMENT:				
Warm air furnaces	127.6	127.6	117.2	116.5
Unitary air conditioners	140.9	140.9	136.4	137.6
Cast iron heating boilers	131.2	135.4	124.4	121.9

NOTES: 1) Sources: Bureau of Labor Statistics, US Department of Labor; compiled for the American Supply Association. 2) Data for 2006 are subject to revision.

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