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Steelmakers look for new links

Peter Marsh / London October 01, 2005

Companies likely to concentrate on expansion in Asia and South America.

Amid the razzmatazz of this year's biggest meeting for steel industry executives, starting this weekend in Seoul, some serious talking will be going on.

On the agenda for the heads of the world's largest steelmakers will be possible deals to continue the moves over the past five years towards consolidation that has put the sector in a much healthier financial position.

One of the most active in private discussions on the fringe of the annual conference of the Brussels-based International Iron and Steel Institute is likely to be Indian steel magnate Lakshmi Mittal, chairman and owner of Mittal Steel, the world's biggest steelmaker.

The billionaire is expected to devote significant time to sizing up deal opportunities for his company, already active in 14 countries on four continents. Mittal is particularly interested in building up his company's operations in China - where it is constructing a new plant in the north and also has a minority stake in Hunan Valin, a mid-sized steelmaker.

Mittal Steel is also among a number of companies - others include Severstal of Russia, US Steel and Luxembourg-based Arcelor - that are keen to take over two state-owned businesses on Europe's eastern fringes that could be privatised in the coming months.

An auction for Erdemir in Turkey could fetch \$2 billion, while a similar amount could change hands in the mooted sale of Kryvorizhstal in the Ukraine.

Other company chiefs likely to be using the five-day gathering to review potential purchases of other companies - or study joint ventures with other businesses - are B. Muthuraman and Lee Ku-taek, the respective heads of Tata Steel of India and Posco of South Korea.

Both companies are expanding domestically and are also considered to have a lot of potential to build up strength outside their home nations.

Companies such as Arcelor and Germany's Thyssen-Krupp, which have most of their plants in high-cost countries, are expected to want to continue their efforts to expand in regions such as Asia and south America. Here, steel plants not only cost less to run but are closer to what are likely to be the main markets for the metal in the next 20 years.

"The industry's strength in the past few years has increased the appetite of many steel companies for merger deals," says Michael Locker, president of Locker Associates, a New York metals consultancy. "All around the world there is a hunt for new assets."

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The biggest factor that has lifted the fortunes of the industry in the past three years has been rapid growth in demand for steel in China - the world's biggest steel producer and also the largest steel market - which has led to a doubling of global steel prices over this period.

The drive towards mergers - led by Mittal, which has pushed through several acquisitions including taking over several companies in eastern Europe - has also created bigger companies with more power to dictate prices.

"The number of rogue companies in the business that are likely to disturb the market, by announcing additional capacity when demand is fairly high, is a lot lower than a few years ago," says Peter Fish, managing director of Meps, a UK steel consultancy. "That has given the sector greater stability."

These changes have been evident in the past few months. Following a big downturn in steel prices in the first half of 2005, prices for basic steel have unexpectedly started to climb since mid-summer.

According to global price indices published by Meps, basic steel has been selling this month for \$568 a tonne, compared with \$528 in July and \$653 in December 2004.

Mirroring this pattern, share prices of quoted steel stocks since early July have outperformed world stock markets by 18 per cent, resuming the generally good record of steel share prices between 2000 and the end of 2004 (see chart).

Most analysts' profit projections for steelmakers for next year are fairly high, particularly for the low-cost producers outside western Europe and north America.

As far as the future is concerned, not everyone is particularly upbeat.

Bruno Bolfo, chairman and owner of Switzerland-based Duferco, the world's biggest steel trader, says he is "pessimistic" about the direction of prices in 2006.

That is mainly because he sees steel producers in China starting to add to capacity.

That could lead to more metal from the country channelling into world markets, leading to lower prices and reduced earnings by the industry as a whole.

According to some analysts, higher Chinese output and a slowing of consumption in the country mean China is likely to move from being a net importer of 13m tonnes of steel last year to a net exporter - of 7m tonnes this year, and of 10m tonnes next.

While this does not sound like a huge change, it could be enough to alter the fairly healthy state of the inter-national industry.

Assuming steel chiefs accept the likelihood of this scenario, they are all the more likely to want to continue the effort towards consolidation as a way to protect themselves from the potentially negative consequences.

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