

Short Insight - Steel

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US, European steel sectors face challenges

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The pressure on steel prices is intensifying. The coronavirus and the Great Lockdown are causing a strong macroeconomic downturn. Demand from the construction and automotive sectors is weak, while the availability of steel is accumulating. This has an impact throughout the value chain. The decline in demand for steel also means less demand for iron ore, coking coal and scrap. This will bite as many mines continue to produce, which is, after all, still financially feasible due to the lower energy costs.

- **Pressure on steel prices outside China intensifies**
- **Optimism about purchasing activity among Chinese steel end-users**
- **Coking coal price drops sharply due to weak demand and high supply**
- **Oversupply of iron ore is looming**
- **Demand for steel scrap is cooling down in Europe**

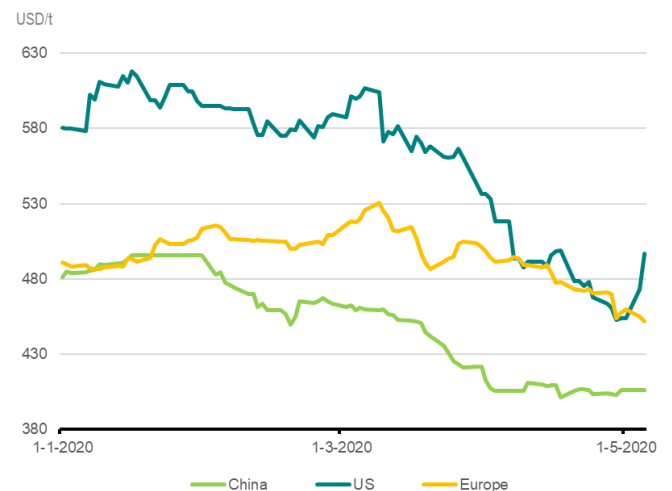
Pressure on steel prices outside China is intensifying

Pressure on the Chinese steel price increased from 1 February with the spread of the coronavirus and ensuing the lockdown. More than a month later, the coronavirus tightened its grip on the economy in the US and Europe. From then on, steel prices in these regions also started to fall. Now, with the further easing of the corona measures in China, large steel users are cautiously restarting their production facilities. This cautious upturn has stabilized the steel price since mid-April. However, steel prices in China remain weak for the time being. Steel mills continued to produce during the crisis, with no demand in return. This created large inventories and the overhang will weigh on prices. Due to the sharp drop in steel prices in the US, many mills have announced price increases to turn the tide and prevent worsening of conditions. Some steel mills Europe closed capacity in earlier stages of the crisis in an effort to avoid this situation. Nevertheless, the pressure on steel prices in the US and Europe will continue in the coming month, in tandem with the pattern in China.

Optimism among Chinese end-users of steel

Hope is on the horizon in China. Macro data for March confirm that the Chinese economy is recovering gradually from the deep trough in February caused by Covid-19. The upturn was strongest in the industrial sector. In mid-April, approximately 99% of large industrial companies and 85% of SMEs resumed operations. The mood among purchasers in major steel-using sectors in China has also improved sharply now that the economy is reopening. Activity in the construction sector is experiencing a relatively smooth recovery, thanks largely to government policy. Car production increased fivefold in March compared to February, but still remained strongly negative on an annual basis (-40%). Thus industrial growth in March was still negative, but at -1.1% year-on-year, this was much less than in January and February combined (-13.5%).

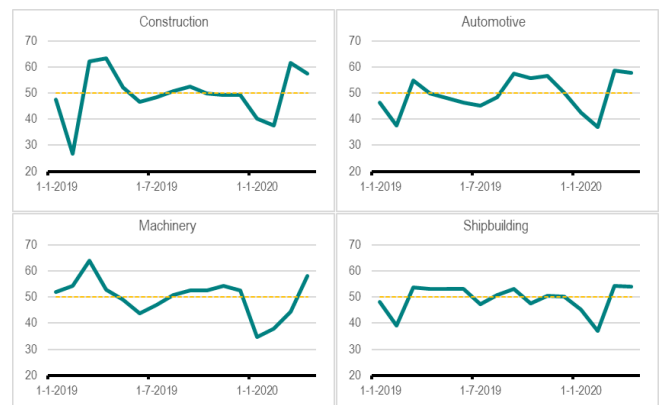
Price trends in steel sector



Source: Refinitiv

Sentiment steel purchasers (PMI) China

(more than 50 = expansion; 50 = neutral; below 50 = contraction)



Source: Refinitiv, Shanghai Metals Markets (SMM)

Coking coal price drops sharply on weak demand, high supply

The coking coal price has fallen by a spectacular 23% in the past two weeks. The sector has not experienced such a sharp drop in prices in such a short period of time since 2010. The cause of the decline is a combination of weaker demand and higher supply. Due to the lockdowns in the US, Japan, Europe and India, the demand for steel in these countries has plummeted. Many steel mills have chosen to reduce their utilization rates and sometimes close capacity. A wise decision, but this deals a blow to demand for coking coal. After severe weather disruptions earlier this year, supply in Australia, China and Mongolia has improved almost simultaneously. The difference between supply and demand increased sharply in a short time, resulting in strong price pressure. This mismatch will continue for the time being. With the lockdowns and limited mine curtailments or shutdowns, prices will remain relatively low for the time being.

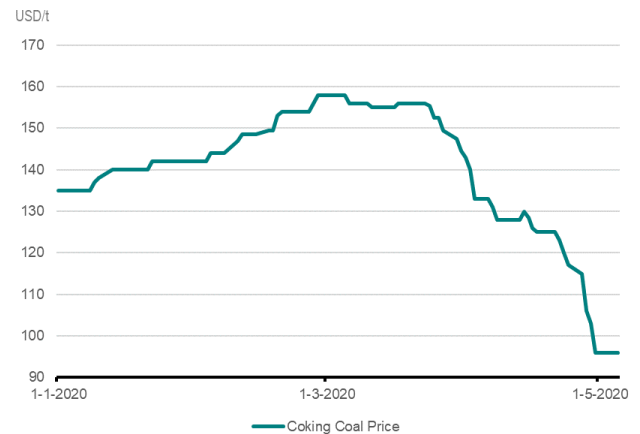
Oversupply of iron ore is looming

There is still limited panic among mining companies. Although iron ore prices have weakened this year, energy costs have fallen significantly due to the sharply lower oil price. This means that many mining companies are able to produce, despite lower prices for their end product. Also the less profitable mines have higher chances of survival. Given the weakening demand for steel due to the corona crisis, the problems for the iron ore miners will only increase. Oversupply is looming and this will hit the sector hard in the long run. A bright spot in the iron ore market, however, is that China is by far the largest importer of iron ore and Chinese steel mills are slowly starting up again. The coking coal market differs in this respect because Japan, Europe and India are also major importers. In addition, Chinese iron ore inventories in ports and at mills are lower. The combination of a new restocking cycle and oversupply will result in persistently weak prices.

Demand for scrap is cooling down in Europe

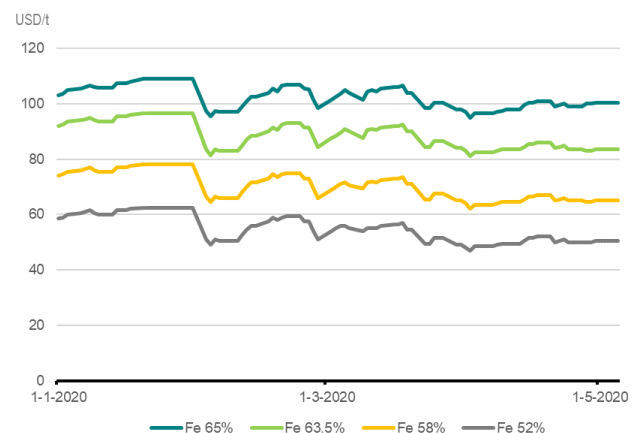
The price trend of steel scrap broadly follows that of crude steel. Scrap is an important ingredient in the production of crude steel, in particular via the so-called Electric Arc Furnace (EAF) route. The pressure on scrap prices has intensified during 2020 with the demand for steel evaporating due to the corona crisis. Prices in the US have fallen by 20% since 1 January and those in China by 13%. In Europe, scarcity on the scrap market caused an upturn in the scrap price in the first quarter of this year. Since the beginning of March, however, scrap prices have also started to decline due to an intensification of the corona measures and weaker economic activity. Europe in particular produces a large share of its steel via the EAF route. Indeed, 44% of all European steel is produced via EAF. By comparison, EAF production in Russia is 33%, in Japan 22% and in China only 10%. Given imminent weaker steel demand in the US and Europe, for now scrap prices will also remain weak.

Price of coking coal



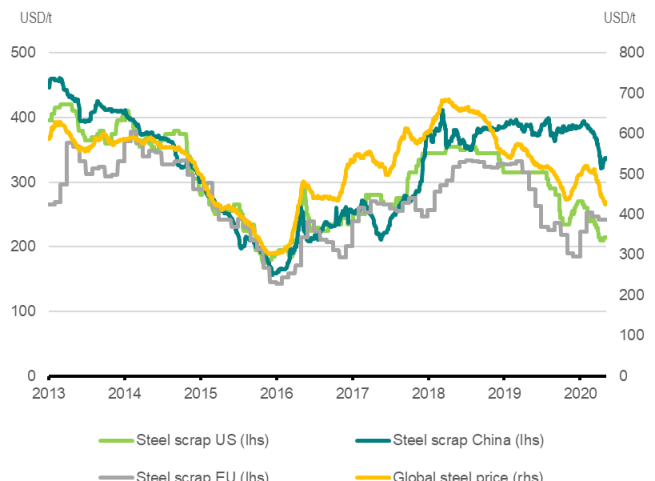
Source: Refinitiv

Prices of iron ore (Fe-content)



Source: Refinitiv, Argus Metals

Steel scrap prices by region



Source: Refinitiv, Argus Metals

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