

OUTLOOK

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Update: Steel Industry - US

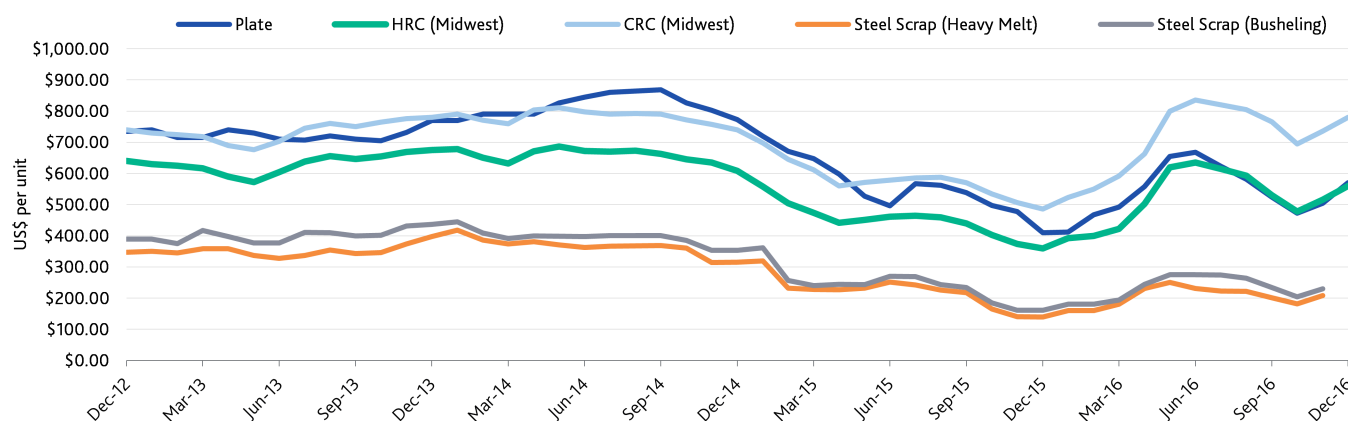
Price Increases, Improving Capacity Utilization, Fewer Imports Bring Stability

Our outlook for the US steel industry is stable. This outlook reflects our expectations for the fundamental business conditions in the industry over the next 12 to 18 months.

- » **We changed our outlook for the US steel industry to stable, from negative.** Steel prices have risen steadily to about \$560 per ton for hot-rolled coil (HRC), after bottoming at about \$470/ton in October (see Exhibit 1). Steelmakers have been able to raise prices three times since then, supported by continued strength from the automotive sector, higher oil & gas rig counts boosting demand for steel pipe, slowly improving construction markets, and rising costs for materials (see Exhibit 2) including iron ore, coking coal and steel scrap. A fourth increase taking HRC to \$600/ton was recently announced. We anticipate 2017 will continue to build on this year's advances and our price sensitivities range from \$550/ton to \$600/ton.
- » **Capacity utilization continues to improve incrementally.** Capacity utilization was 68.9% for the week ending on December 3 (see Exhibit 3). While that is below our stable outlook trigger of 75%, the metric continues to increase week-on-week and we expect the trend to continue, though at a slow pace. Also utilization varies widely by company — SDI's sheet steel mill utilization rate was 97% in the third quarter and Nucor's 76%, while US Steel's flat-rolled US segment was at 64%. For 2017, we expect capacity utilization to range between 70% and 74%.
- » **PMI readings continue to indicate modest economic growth.** The Institute for Supply Management's Purchasing Managers' Index advanced in November to 53.2 — from 51.9 in October, and 51.5 in September (see Exhibit 4) — with the manufacturing and petroleum & coal products leading the increase. A US PMI reading between 50 and 55 for two straight months is one of our triggers for a stable outlook. Any increased infrastructure spending under President-elect Trump would also be positive, though likely spread out over a lengthy time frame.

- » **Trade-case rulings in favor of US steelmakers have cut imports.** Positive outcomes in anti-dumping trade cases particularly for cold-rolled and coated steel, but also HRC, have led to lower total and finished steel imports, a positive for US steelmakers, particularly those that make niche products. Year-on-year through October, total steel imports are down 19% to 27.5 million tons (see Exhibit 5) and finished steel imports fell 19.8% to 22 million tons. This is also in part due to improved steel industry performance on a global basis narrowing price differentials between the US and other countries.
- » **Metal service center inventories are low, which should help sustain higher prices.** Service centers have materially reduced their inventories for the second straight year in 2016 in the face of volatile steel prices and lackluster demand. That could set the stage for restocking and possibly panic buying, as prices rise and mill lead times extend. Mill lead times have lengthened, with HRC said to be in the 3-to-4 week range, from 2 weeks or less early in autumn.
- » **Higher raw material costs are baked in.** Current steel prices have higher input costs built in, offering potential upside for those that signed long-term supply contracts before raw-material prices jumped. Fourth-quarter benchmark met coal prices rose to \$200 per metric tonne (MT), largely due to supply disruptions and increased steel production in China on stimulus-driven demand. While the [current price is unsustainable](#) in our view, it is unlikely to return to lows near \$75/ton and should settle back in the range of \$90 - \$120/MT in the H1 2017. Seaborne iron ore prices have also been on a strong upward trend, largely for similar reasons, but also due to supply reduction in China, with prices (62% Fe) recently hovering in the \$80/MT range, versus a January 2016 average low of just under \$42/MT. Scrap steel prices look to be increasing about \$50/ton to approximately \$258/ton for heavy melt.

Exhibit 1

Steel and Steel Scrap Pricing

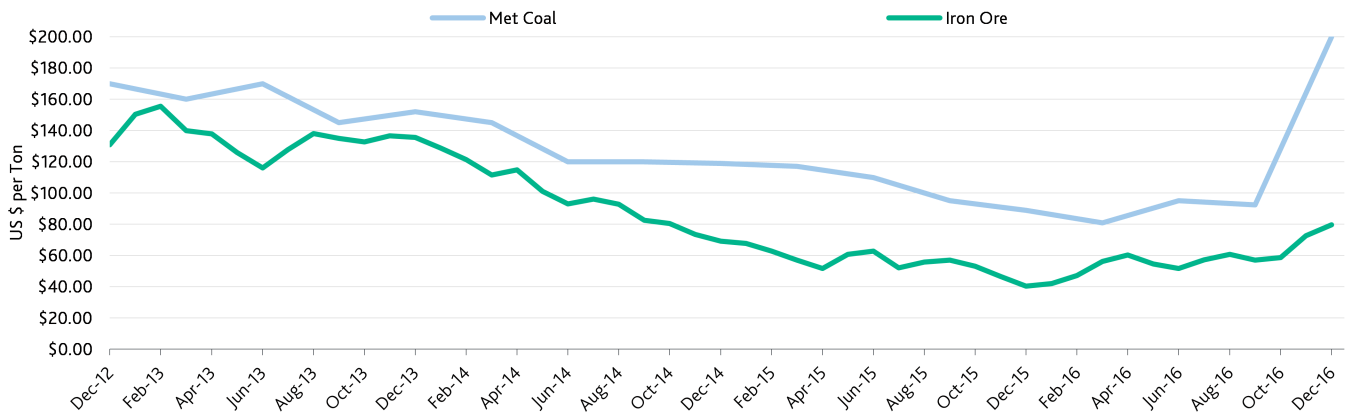
HRC, CRC, and Plate prices are monthly averages through December 8, 2016. Steel Scrap prices are monthly averages through November 30, 2016.

Source: *Steel First*

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Exhibit 2

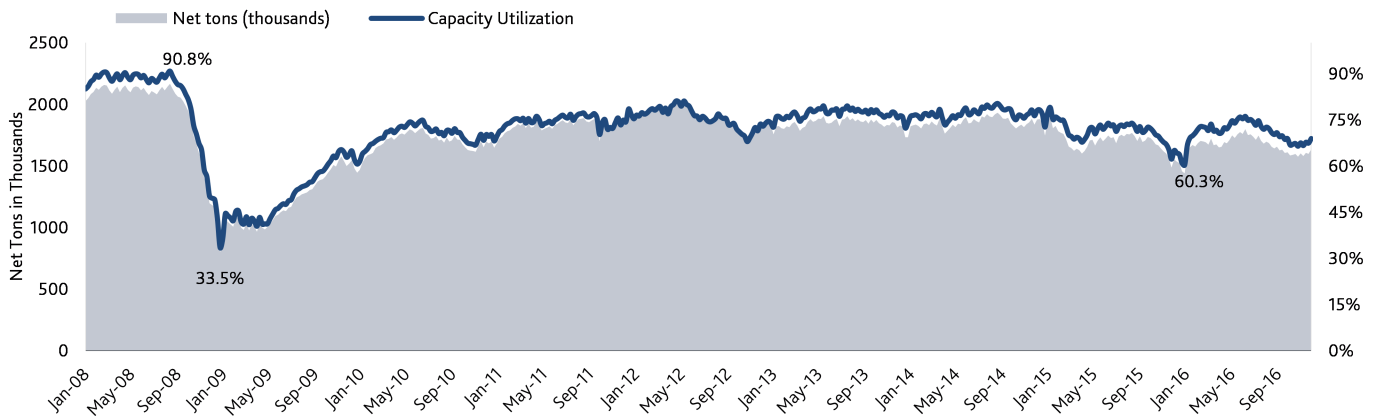
Iron Ore and Metallurgical Coal Prices



Iron Ore prices are monthly averages through December 8, 2016. Met Coal prices are quarterly benchmark prices.

Source: Steel First, Platts

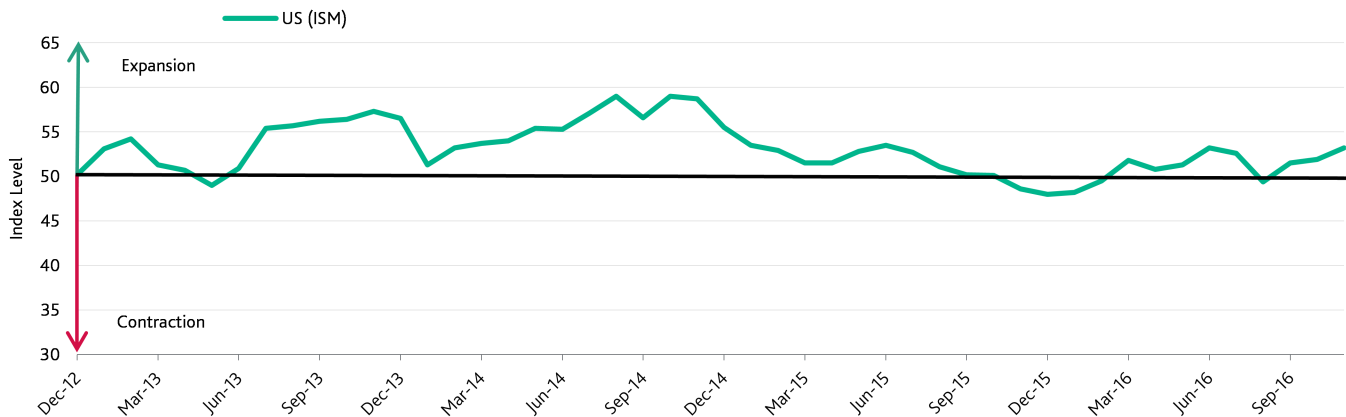
Exhibit 3

U.S. Raw Steel Output & Utilization
As of the week ending December 3, 2016

Source: American Iron & Steel Institute

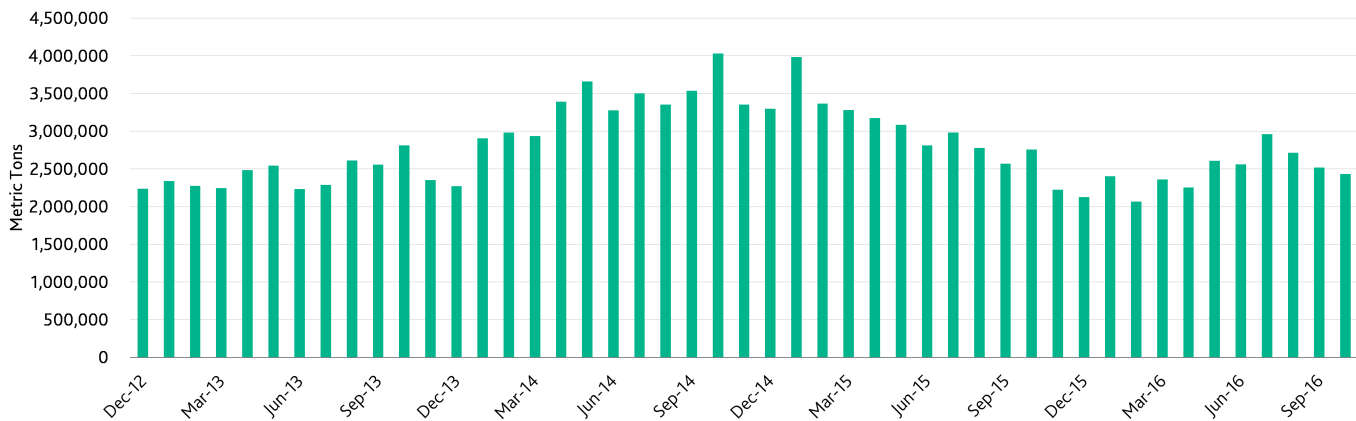
Exhibit 4

US Manufacturing PMI



Source: Institute of Supply Management

Exhibit 5

Steel Imports

Source: US Department of Commerce

Our outlook could change to positive if the PMI in the US exceeds 55 for at least two consecutive months and capacity utilization is sustained above 80%. Our outlook could return to negative if the PMI in the US tracks below 50 for at least two consecutive months and capacity utilization is sustained at less than 75%.

Moody's Related Research

Sector In-Depth

- » [Global Macro Outlook 2017-18: Global Growth Outlook Stabilizes at Low Levels; Medium-Term Risks On the Rise](#), November 2016
- » [Steel Industry - US: Trade Cases Lift Value-Added Product Spreads, But Fundamentals Still Limit Prices](#), October 2016

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