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China's Growing Hunger for Steel Dominates Sector

Rising Production Looks Unlikely to Exceed Demand, Propelling Prices Higher World-Wide for Raw Materials

By **ROBERT GUY MATTHEWS**

China's surging demand for steel this year is expected to dominate the landscape of the steel industry as never before.

Already the world's largest producer by far, China is expected to rev up output nearly 10%. But output likely won't exceed demand, pushing prices higher world-wide for steel, its raw materials and even coal.

Steelmakers, which idled dozens of mills and cut production as the global economy slowed, are now ramping up. **Rio Tinto**, which sells the most iron ore to China, is restarting production. Iron ore is a key ingredient in steel. **Arcelor Mittal**, the world's largest steel producer, is raising prices, as is China's largest steelmaker Baosteel Group Corp.

China also is trying to unify a fragmented and sprawling domestic industry to present a strong, unified voice in price negotiations for sales and purchases of raw materials. The idea: Capitalize better on the country's huge appetite for the materials that make everything from refrigerators to bridges.

China is expected to produce a record 600 million metric tons this year—about half the world's total output. The next biggest producer, Japan, will make just one-sixth of what China is expected to produce. The U.S. was fourth in production, behind Russia, last year.

China's resilience was the dim light in an otherwise dreary year for miners and steelmakers, marked by layoffs, mine closings and production and investment pullbacks as prices for commodities tumbled. And it looks to be the beacon going forward, along with India, to a lesser extent.

While other economies are strengthening, they don't offer the same potential for growth as China, which makes penetrating that market critical.

"Chinese steel production and demand is likely to continue its inexorable rise," says Peter M. Fish, economist for MEPS International, a steel consulting firm.

That, in turn, is good news for metals and minerals sellers.

Iron-ore spot prices, about \$110 a metric ton, have been climbing toward their highest level in more than a year. Coal prices for steel mills and electricity production have surged more than 30% as China last year curbed production due to environmental concerns.

Copper, aluminum and zinc prices also have risen. "The recovery of all commodities has exceeded expectations," says David Butler, analyst at J.P. Morgan Cazenove.

Australian ports are becoming congested again, with coal ships in line on the ocean, waiting to load and unload.

Robin Walker, a spokesman for Rio Tinto, the largest seller of iron ore to China and which sells a substantial amount of coal, says its economists are revising projections from August regarding Chinese demand. "The new update could show that growth is stronger," he says.

BHP Billiton, Rio Tinto, Australia's **Fortescue Metals Group Ltd.** and Brazil's **Vale** all are increasing production of iron ore, and in some cases coal, to meet the expected increased demand in China.

China's Baosteel, a bellwether, told buyers last week that it would increase steel-sheet prices by 5% beginning in February, marking the third steel price increase in as many months.

"With January hikes now sticking well, we expect to see further price increases announced in China as well as Europe and the US," says Michelle Applebaum, an analyst at steel research firm MARI in Chicago. "Chinese steel demand is profound, and rising raw-material costs are driving an inflationary spiral in the region as steelmakers and their customers clamor for material."

Massive government stimulus and infrastructure plans—including for rails, roads and bridges in eastern China and for general construction and factory building in western China—are fueling demand. Most of the steel output will be consumed internally, says the China Iron and Steel Association, the country's main steel trade group.

China's exports have dropped between 10% and 50%, depending on the product and country in the past year, which is welcome news for ArcelorMittal Chief Executive Lakshmi Mittal.

Mr. Mittal says that last fall, China's steelmakers were fairly disciplined about keeping steel from flooding foreign markets, which has helped steelmakers around the world raise prices.

The downside for ArcelorMittal and other steelmakers is that raw-material prices will likely rise as the companies compete with Chinese steel mills to secure the coal and iron ore needed for steel plants.

Recently, Australia and China signed a \$3 billion coal deal, the largest buyout by a Chinese firm in Australian mining history. The purchase of Australia's Felix Resources Ltd. by Yanzhou Coal Mining Co. could open the door to more acquisitions this year.

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