

7 August 2009



Steel Monthly

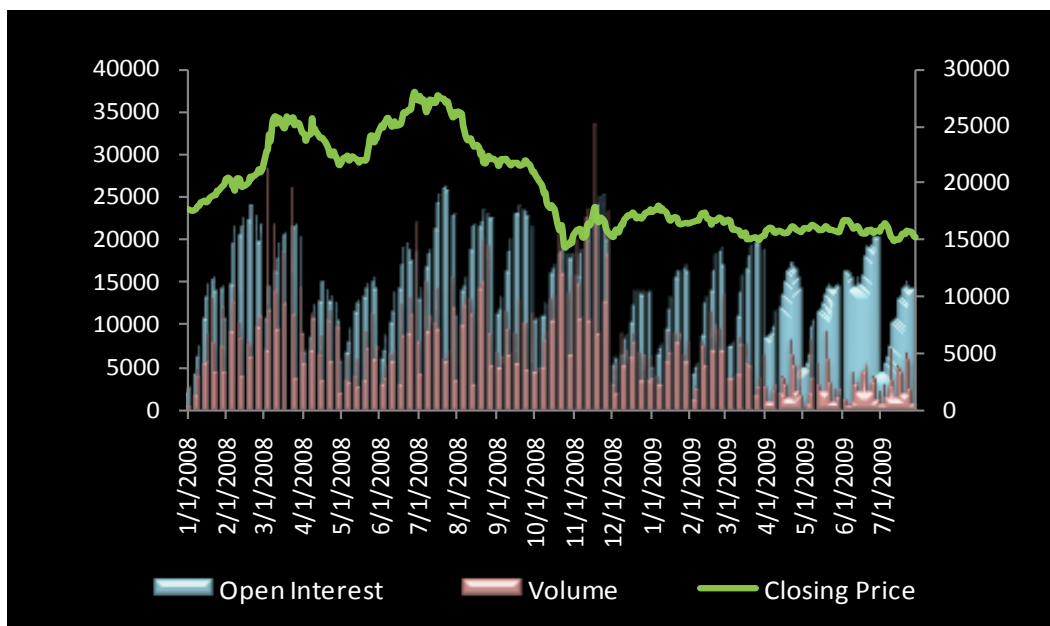
August-2009



MARKET RECAP

Steel consumption has been tattered by the economic crisis, with global prices dropping 68.31% in last one year, from highs of \$1,220 per tonnes. The decline in global demand for steel has reflected in production cuts by steel producers and rapid drops in prices of basic raw material such as iron ore and coal. Steel is a vital commodity input for the automobiles, infrastructure and machinery. With the credit markets coming to a halt and consumer confidence jolted, demand for steel has dropped rapidly.

The **NCDEX steel long futures** prices extended there falling spree for the last seven-months on subdued global demand and production outpacing consumption. Prices shattered by 5.70% in July from Rs. 21420 per tonne to Rs. 20200 per tonne as on 28th July 2009. The fall in last month i.e. June was close to 5.50%. Prices have registered a fall of close to 14% in the last 7 months in the current year, as against the rise of more than 47% in the same period last year. In the month of July alone, total volumes surged by whopping 132% to 3180 contracts from 1370 contracts whereas the open positions fell by 29.24% to 14,060 lots from 19870 lots. Prices on the international front, for 3-month **LME steel billets forward** contract fell by 1.30% to \$382.5 per tonne on 27th July 2009, as compared to rise of 16.67%, ending the month at \$385 per tonne. The factor that led to the fall in prices in spite of stable economic recovery nearing is the supply concerns yet to hold high against demand and high cost of production. The fall in imports and exports also weigh down on prices.



GLOBAL PRODUCTION

World crude steel production for the 66 countries reporting to the World Steel Association (world steel) was 99.8 million tonnes in June 2009. This is 16% lower than in June 2008. China, the largest steel producer's, crude steel production for June 2009 was 49.4 million tonnes, 6% higher than June 2008. This drop has been attributed to rapid de-stocking, the process of players clearing out the inventory rapidly while cutting production. The pace at which steel production has dropped has certainly been sharp when compared to how global industrial activity has contracted over the same period. While world GDP contracted by 2.5% according to the IMF, steel saw more than 20% decline in output. This could indicate that the process of de-stocking has been more severe than warranted by the slowdown and that the worst could, therefore, be behind us.

Total crude steel production for the first six months of 2009 was 549 million tonnes, a decrease of 21.3% over the same period of 2008. Asia produced 360 million tonnes of crude steel, a decline of 7.8% over the first half of 2008. However, China produced 266.6 million tonnes of crude steel for the first half of 2009, an increase of 1.2% during the first six months of 2009. This marginal increase in its production was instilled by the positive outcomes of stimulus package. The government is pushing its production to utilize the capacity and thus minimize the cost of production.

Country	Jan-June	% Change over	Jan-May 2009	% Change over
World	549	-21.30%	449	-22.4%
Asia	360	-7.8%	294	-8.8%
EU	62.2	-43.2%	50.7	-44.4%
North America	35.8	-48.5%	29	-49.3%
China	266.6	+1.2%	217.2	+0.4%
Iran	5.6	+12.1%	4.7	+12.6%

*MMT is Metric Million Tonnes

Country	June 2009	% Change from	May 2009	% Change from
WORLD	99.8	-16%	95.6	-21%
China	49.4	+6.0%	46.5	+0.6%
Japan	6.9	-33.6%	6.5	-38.5%
South Korea	4.0	-14.4%	4.2	-11.8%

Germany	2.5	-41.1%	2.2	-47.8%
Italy	1.6	-31.4%	1.7	-41.6%
Spain	1.2	31.4%	1.2	-41.3%
France	1.1	-37.9%	1.0	-41.3%
U.S.	4.4	-46.9%	4.3	-50.6%
Brazil	1.9	-33.9%	1.9	-36.3%
Russia	4.9	-22.1%	4.7	-31.2%
Ukraine	2.3	-36.8%	2.4	-40%
Turkey	2.2	-12.7%	2.1	-16.1%
Iran	0.9	9.4%	0.9	+11.6%

*MMT is Metric Million Tonnes

Demand for steel has declined the most since World War II, according to World Steel Association and output is set to plummet 15% this year. China Iron & Steel Association states the stockpiles at Chinese major ports reached 62 million tonnes in April with iron ore surplus this year. The Chinese imports exceeded demand leading to over-stocking. Automakers are expected to report steep sales declines with the U.S. economy on a hold. The automobile industry is stumbling from Chrysler's bankruptcy on April 30 and General Motors Corp's bankruptcy followed on.

DOMESTIC FRONT

Showing *stable signs of economic recovery*, the six core infrastructure sectors recorded a growth of 6.5% in June compared to 2.8% in May 2009. In June 2008, the six core sectors - coal, cement, crude oil, electricity, and finished steel and petroleum refinery products grew at 5.1%.

India is among nine countries across the globe to post positive steel production figures for the first half of the year ended June 2009, according to the World Steel Association. India produced 27.5 million tonnes of steel in the six months ended June 2009 as against 27.1 million tonnes for the same period last year, posting an increase of 1.3%. Other countries that reported an increase were Macedonia (43%), Norway (0.3%), Belarus (2.5%), Uzbekistan (11%), Ecuador (154.4%), Venezuela (6%), Iran (12.1) and China (1.2%).

Indian Steel production increased 3.4% to 13.98 million tonnes during April-May 2009, compared to 13.53 million tonnes in the same period the previous fiscal. The consumption grew by 5.2% to 12.83 million tonnes in Q1FY09-10 from 12.2 million tonnes in the same period a year ago.

However, Indian exports declined from 1.032 million tonnes to 0.642 million tonnes, a fall of 37.8%, while Imports also fell 5.3% from 1.493 million tonnes to 1.414 million tonnes during April-May 2009. India's steel production is expected to almost double to 124 million tonnes a year by 2011-12 from 65 million at present levels. There is massive expansion going on in the steel sector in the country, both in the public and private sector that will see India becoming a major steel producer by 2011-12.

INDUSTRIAL UPDATE

Looking at industry specific production we see that, among state-controlled companies, ***Steel Authority of India Ltd (SAIL)*** increased production by 3.73% to 3.06 million tonnes during April-June, compared to 2.95 million tonnes during April-June 2008. Another public sector unit, ***Rashtriya Ispat Nigam Ltd (RINL)***, also upped production by 2.09% to 685,000 tonnes from 671,000 tonnes. ***Tata Steel's crude steel production*** in the April-June period went up 20%, while JSW Steel's rose 45% to 14.09 lakh tonnes.

However, ***dwindling sales realization*** and higher input cost is pulling down the operating profits significantly. The producers had entered into long term contracts in the initial phase of year when the input prices were high, coking coal at around \$110-120 per tonne and iron ore at \$65-70 per tonne. The prices now have come down more than 50% in the spot market, thereby companies ended up paying higher cost of raw material and thus increasing the cost of production, whereas the sales realization had fallen to a large extent. Current international steel prices are 50% lower than year-ago levels and in India the decline has been 25-35 %.

GOVERNMENT CONTROL

Counting on to the domestic factors we see that, the ***Union Steel Minister Virbhadra Singh*** ruled out any hike in import duty on steel products but assured to protect the interest of domestic steel producers by restricting iron ore exports. He turned down the demand of steel producers for a hike in duty from 5% to 20%. The emphasis would be on discouraging iron ore exports for its optimal use by domestic steel producers and encouraging ore exports only in value added form to fetch higher foreign exchange for the country. By ensuring domestic use of iron ore reserves India could become a global hub for steel manufacturing. The country too would have to follow the same course as ***China reserves*** its iron ore for its domestic consumption and the U.S. preserves its reserves of crude.

Further on, Mr Virbhadra Singh stated India's steel consumption continue to grow at a pace between 6% and 8% during the current financial year, fully backed by the various fiscal, monetary and administrative measures taken by the Government from time to time.

The Indian Steel Ministry plans to propose two-tier empowered committees to address mining disputes and other issues evocating the growth of the domestic steel sector. Steel **Secretary Pramod Rastogi**, estimated steel demand may gain close to 10% this fiscal year, almost double the pace previously estimated, as the government spends more on infrastructure.

The current slowing down of construction activities owing to the monsoon, add to price woes. The monsoon has caused a lull in market, driving investors apprehensive about the revival on constructions sector and thereby demands of raw material like steel. Governments denying imposing import duty on dumping by China and other nations have set back invertors interest. The post budget week witnessed Steel sector stocks losing more than 10% on domestic stock market, as people reversed their positions after budget posted disappointing numbers.

FUNDAMENTAL OUTLOOK

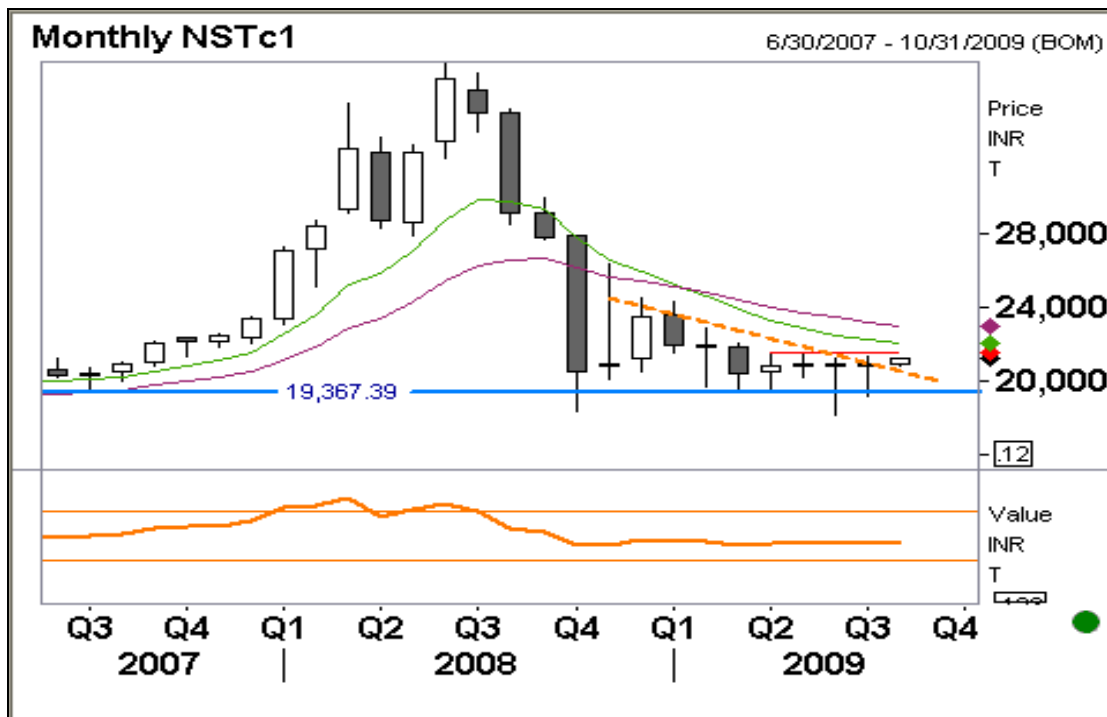
However, despite all the talk of optimism and government laborious efforts, the global demand for steel continues to look far from rosy. Hopes are still maintained high with demand for steel driven mainly by China and India. China's heavy infrastructure spending has fuelled domestic steel production there and India moots over huge infrastructural spending this year.

Strengthening of steel prices from here appears to depend mainly on how several factors such as government stimulus spending across key economies pan out and the pace and direction of such spending. However, it would not be wrong to say, long-term growth in demand for steel will outpace the long-term growth of the general economy, exclusively because of the widespread usage for the metal. Shipping and automobiles sector show influential signs of revival and holds good potential for steel producers.

Bearish sentiments prevail in the market over higher cost of production and lower sales realization leading to meager operating profits. Yet the steel tycoons continue with high production over optimism in infrastructural sector. Further the construction sector is to recover after the monsoon comes to a halt.

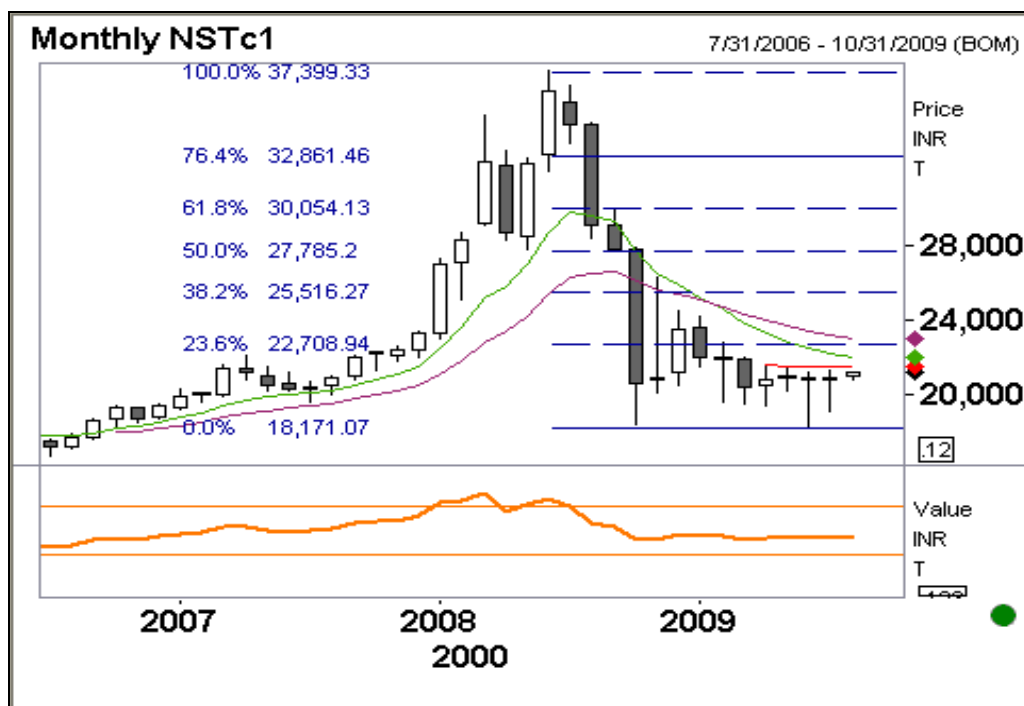
On the concluding note, in the near term demand retort and loosely held market portrays a hazy picture of steel prices to recover from lows and reach the pinnacles. To get over with the current market conditions would still take some time, but lately gains are unstoppable.

TECHNICAL OUTLOOK



After a massive fall of 37500 to 18330 market is in a major consolidation range (November 2008 to July 2009). Recently, Steel prices are forming an **ascending triangle** of which break out has already seen and if market sustain above 21000 levels then it can test 24000 to 26000 levels in near to short term.

Normally, the Ascending triangles are of continuation pattern but sometime, it makes a reversal. Although steel prices made an ascending triangle but it broke higher suggesting a minor reversal. Now, the immediate resistances can be seen at 22960 and breach of the same it may extend the rally to 24500 and then 25000 levels. On the other hand, the presences of averages on the chart making a worrisome on the investors as the prices are still trading below the averages (50-month EMA).



Furthering, **Fibonacci retracement** is indicating that the prices are still in a weak trend as they still have not managed to trade above its 23.6% levels (22708 levels) which is also its 20 month EMA's resistance levels. Any close above the same would certainly boost the prices to move higher to test their next Fibonacci level that is around 25516 levels.

Our stance: We expect steel prices to trade higher and sustains above 22000 may push the prices to 22950-23000 and then 24500-25000 levels.

Recommendation: We recommend buying 1st lot around 22150/22100, 2nd at 21900/21850 targeting 23000/23200 then 23600/23800 with stop loss below 21500

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