

Iron-Ore Miners Seek a Price Rise

Ahead of Contract Talks, Producers See Hints of Firmer Demand in China

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ROBERT GUY MATTHEWS

Despite concerns about the length and depth of the global recession, iron ore miners are pushing for as much as a 5% increase in the annual contract price beginning in April, according to people familiar with the negotiations.

The miners, which only a month ago were hoping to avoid a decline and keep prices flat, say a recent uptick in demand from China may signal that the market has bottomed out. They also note that spot prices have inched up since late last year.

But an increase of any amount isn't assured. At this point, China is the only country showing increased steel production and although it is the world's largest steel producer, consumer and exporter, it may not be enough to buoy the entire market for iron ore.

A price increase of 5%, though well below the 70% to 85% levels of last year, will be strongly opposed by the biggest consumer of iron ore -- the global steel industry. "We are not conceding anything yet," said an official with the China Iron & Steel Association, which is leading negotiations with the world's top three iron ore producers, London-based Rio Tinto PLC, Melbourne-based BHP Billiton Ltd., and Brazil's Companhia Vale do Rio Doce. The negotiations seek to set a benchmark price for iron ore that steelmakers around the world will follow.

China was the only major country last month to record an increase in steel production, up 2.4% from January 2008. According to the World Steel Association, steel production by all countries fell 24% in January from the year-earlier month. Increased steel usage in China tends to tighten supply in other countries and provide a lift in pricing.

Fabio Barbosa, Vale's finance director, said that it has seen an uptick in iron ore demand in China. "This is very positive development. It is still too early to say that a turnaround is near," said Mr. Barbosa, who declined to talk about current negotiations. Vale shipped nearly twice as much iron ore, 30 million short tons, to China in January compared to December.

BHP has also noted that there seems to be a slight recovery in iron ore demand in China.

Steelmakers around the world are cutting production, shutting plants and laying off workers, as their own end markets -- autos, appliance, heavy equipment and construction -- contract. In the U.S., raw steel production has fallen to about 1 million short tons a week, about half the amount of its normal weekly production. The story is much the same in Europe and elsewhere as steelmakers seek to firm up prices, which have fallen by 50% or more since last year.

Their need to conserve cash and control costs will conflict with the mining industry's effort to raise prices. While some steelmakers, including ArcelorMittal and U.S. Steel Corp., have some iron ore reserves, most steelmakers don't. They also may have a harder time passing on their own higher raw material costs because their customers are struggling.

As in recent years, the Chinese steel industry is leading negotiations on a benchmark price. China's steel industry is expected to consolidate, which could eventually give it more leverage in iron ore contract talks. Those moves aren't expected to impact this year's talks, which aren't likely to conclude before April.

The spot market price for iron ore is about \$10 below last year's contract price of \$80-\$90 a metric ton. Spot prices have recovered from late last year, when iron ore was selling as much as \$30 below contract prices. Iron ore producers have drastically cut production since September when demand fell along with the strength of the economy. Rio Tinto and Vale said that they had cut production of iron ore between 18% and 25%. Rio Tinto, the world's second-largest provider of seaborne-traded iron ore, said that some of its production out of Australia has also been halted because of heavy rain. While the miners are generally negotiating as a unit this year, their resolve to do so may not last. BHP wants to move the selling and pricing of iron ore away from establishing a yearly benchmark, preferring to sell based on market spot prices. Vale, on the other hand, wants to retain a benchmark price. A benchmark generally offers stable but lower pricing while spot prices can swing from very high to very low, depending on demand.