

## **Economic and Steel Market Outlook 2009-2011**

**October '09 Report from EUROFER's Economic Committee <sup>1)</sup>**

### **EU macro-economic overview (y-o-y change in % )**

	Eurofer Forecast October 2009 EU			
	2008	2009 (f)	2010 (f)	2011 (f)
<b>GDP</b>	0.9	-4.0	0.8	1.7
<b>Private consumption</b>	0.5	-1.2	0.0	1.4
<b>Government consumption</b>	2.1	1.8	1.0	0.6
<b>Investment</b>	0.0	-11.1	-1.9	2.3
<b>Investment in mach. equip.</b>	0.1	-14.5	-0.8	3.0
<b>Investment in construction</b>	-0.3	-7.9	-2.9	1.6
<b>Exports</b>	1.1	-15.1	3.1	5.7
<b>Imports</b>	1.2	-13.2	1.3	5.0
<b>Unemployment rate</b>	7.3	9.2	10.3	9.3
<b>Inflation</b>	3.3	0.7	1.3	1.6
<b>Industrial production</b>	-1.2	-14.7	1.6	3.7

(f) = forecast

### **I. EU Macro-economic overview**

- ***EU approaching inflection point in economic downturn***
- ***Recovery will be slow and surrounded by mostly downside risks***
- ***Rising unemployment key concern***

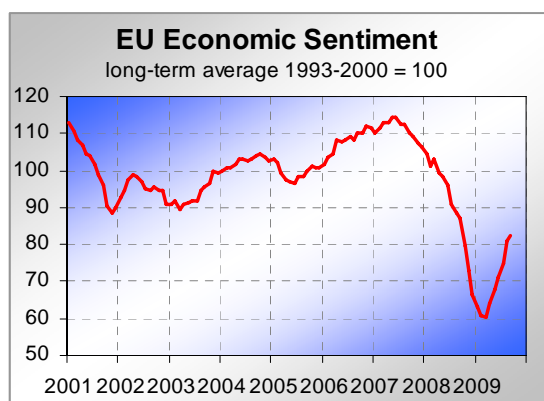
In the second quarter of 2009, the GDP decline in the EU eased to -0.3% quarter-on-quarter, coming from a 2.4% contraction in Q1'09. At the country level this relative improvement hides significant differences in economic performance across Europe. Both in Germany and France, GDP increased 0.3% quarter-on-quarter. Owing to a pick-up in private and public spending in Germany - supported by government rescue packages - and an improvement in the contribution of net trade in France, the recession in the two largest EU economies ended earlier than expected. Meanwhile, most other countries – most notably Spain and Central European emerging economies such as Bulgaria, Rumania and the Baltic states - have fared less well and remained in recession.

Nevertheless, it is expected that the EU passed the trough during the third quarter. Since late summer, signals of improving economic conditions – both globally and in the EU – have become stronger and support the view that EU

<sup>1)</sup> Based on information available as of October 14<sup>th</sup>, 2009

GDP could register positive growth again in the second half of the year.

The EU economic sentiment indicator continued its upward trend in September, supported by improving expectations from consumers and enterprises in industry, services and the retail sector.

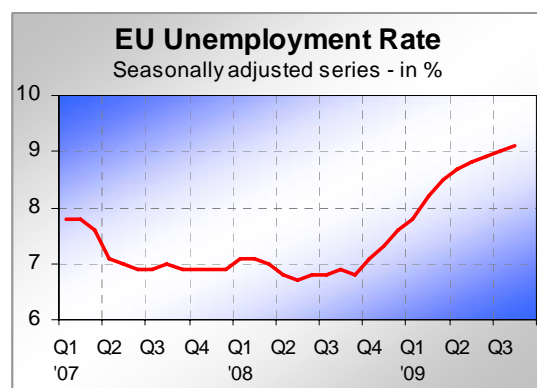


The Eurozone Purchasing Managers' Index for the manufacturing sector rose in August to 48.2, reaching a 14-month high following its record low in February. While forward looking indicators have been rising steadily since early 2009, even the latest readings remain well below their long-term average.

While these soft data signal that the recession may have ended and the EU economy probably resumed growth in the 3<sup>rd</sup> quarter, hard data continue to show at best a mixed picture. The recovery pencilled in for the coming quarters will be slow and is still surrounded by high levels of uncertainty.

A major concern is the potential drag of unemployment on economic growth in the EU. The EU27 unemployment rate rose to 9.1% in August and even to 9.6% for the Euro area; for the Eurozone this is the highest rate since March 1999. The expectation is that unemployment will continue to rise

during 2010. By the end of this year, many of the short-time working schemes and labour market safety nets financed by national governments will come to an end. Inevitably this will lead to a surge in unemployment in early 2010. This will prevent private consumption from bouncing back from the lows reached in 2009.



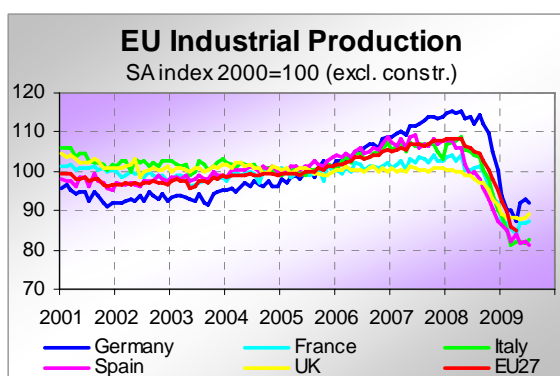
Also the outlook for investment remains extremely weak. EUROFER's October '09 Economic Committee outlook sees investment falling further by almost 2% in 2010 following the 11% decline estimated for 2009. Low capacity utilisation rates, continued sluggish demand for capital goods and overall still low confidence levels will keep corporate investment subdued for a prolonged period.

Another factor limiting business investment as well as private consumption is the still difficult financing situation. While the financial markets appear to have stabilised, supported by the central banks' rapid response, banks have basically used the massive liquidity injections to beef up their balance sheets and strengthen their solvency ratios. Meanwhile, the functioning of the banking system in terms of credit supply to non-financial markets has not yet returned to normality. The ECB Lending Survey

shows that growth of credit in the Eurozone is reported to have come to a near-standstill. Particularly credit insurance is reported to be a major problem for most enterprises.

Credit supply is also threatened by the rising number of loan defaults. However, the slowdown is probably not just supply-driven but also the result of weakened appetite for credit from the business sector due to low confidence levels and risk aversion. In addition, households in EU countries that suffered residential property price busts continued to rebuild savings.

The EU manufacturing sector in particular has been dealt a major blow by the recession. While the latest available production data confirm that EU manufacturing activity did not deteriorate any further since Q2 '09, output appears to be stuck in slow motion with the y-o-y decline in output still around 15% in summer. A positive sign, however, is that EU industrial new orders rose slightly month-on-month in July. This suggests higher output in the months ahead, while remaining at overall depressed levels.



The mild improvement in orders and companies becoming more upbeat on short-term production trends fuelled a further improvement in industrial confidence.

The key question is how sustainable the upturn in manufacturing orders will be. Most likely the rise in order intakes is to a large extent driven by the downstream inventory cycle. All participants in the value chain have been cutting back on their inventory levels since the start of the year, in a response to extremely uncertain business conditions. Since summer, significantly reduced stocks and improving leading indicators have taken away the need to cut back much further and probably triggered companies to selectively fill the holes in their processing and maintenance stocks.

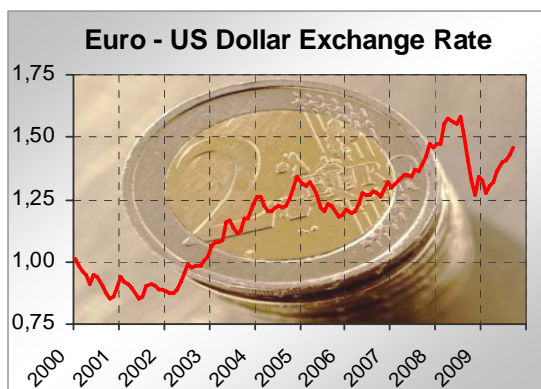
This inventory-led pick-up could support orders and production for a while. However, a full-fledged industrial recovery does require a return to sustainable growth in demand for capital and intermediate goods.

It is unlikely that internal EU dynamics will gain sufficient strength to fuel a significant rise in domestic demand in the coming quarters. While short-term policy stimulus has been put in place in the EU and appears to be effective in the case of car scrapping premiums, these funds are temporary and nearing depletion. Other stimulus packages – such as increased infrastructure spending – will require more time to kick in and stimulate economic momentum.

This implies that EU industry will continue to depend on an improvement in international trade in support of order books and utilisation of production capacity.

So far, the reportedly strong recovery of the Chinese economy had a positive spin-off to other Asian emerging

countries since the second quarter of this year. Intra-regional trade in the Asian region picked up from the depressed levels still registered at the start of the year. It remains to be seen whether EU industry will be able to benefit from this development. Depending on the degree of industrial specialisation some countries - such as



Germany - should be relatively well placed to benefit.

In this respect, the continued strength of the Euro against the dollar in particular but also against other currencies remains an obstacle to those EU exporters which are largely exposed to trade with third countries. Since early 2009 the Euro appreciated by around 14% against the US dollar and the Chinese Renminbi. This could limit the potential improvement of EU industrial production through international trade.

Meanwhile, inflation continued to trend downwards in recent months. According to the latest Eurostat flash estimate, Euro area annual inflation amounted to -0.3% in September. In September 2008, inflation stood at 4%. Approximately three-quarters of this marked reduction in inflation can be attributed to the recent volatility in energy and commodity prices. Assuming that the current slide into negative inflation will be temporary, it

should be welcomed as positive news for the consumer given its positive effect on purchasing power. The outlook for 2010-11 sees inflation remaining relatively low as weak money supply and credit growth and the output gap remaining large should compensate for upward pressure from energy and commodity prices. Low inflation and the persisting weakness of the EU economy resulted in the ECB leaving interest rates unchanged.

All in all, uncertainties continue to set the tone in the outlook for the EU economy. However, compared with the preceding provisions from EUROFER's Economic Committee published this year, the October outlook is more broadly balanced in terms of the risk profile.

As the European economy appears to be nearing an inflection point, also some upward risks can be identified. A faster than expected recovery of the global economy (driven by China and with a lag, the USA) could lead to international trade growing more rapidly. This in turn could extend the positive impact of the stock cycle. Supported by effective policy measures, EU industry could recover more rapidly.

In the base case scenario, economic fundamentals look set to remain fragile. The weak economy will continue to take its toll on jobs and public finances.

The October outlook sees EU GDP falling by 4% this year whereas for next year 0.8% growth is forecast. As such, the October outlook is slightly less pessimistic than the June forecast.

For 2011, a moderate acceleration to 1.7% GDP growth is pencilled in.

### **Macro-economic overview: USA**

- *Drop Q2'09 GDP slows to 0.7%*
- *Indicators signal recovery*
- *Labour market to remain weak, keeping growth slow*

The decline in GDP slowed to 0.7% (annualised rate) in Q2'09, supported by government investment, an improvement in the contribution of net trade and easing negative influence from inventory decumulation.

Mounting evidence from leading indicators and hard data underpins that a return to positive GDP growth in the 3<sup>rd</sup> quarter seems likely. The ISM PMI Indexes have all passed the 50-points level indicating expansion in the economy. Notwithstanding a minor downward correction in August, orders steadily improved from their March '09 low. The housing sector is also showing tentative signs of a recovery. The "cash for clunkers" programme and the federal stimulus package stepping up have provided a welcome boost to domestic demand in the 3<sup>rd</sup> quarter. The negative effect of the stock cycle is also expected to have faded.

Although the economy may have turned a corner recently, the outlook remains fragile and it may take a while before sustainable growth sets in. The labour market will continue to act as drag on economic growth through weak private consumption and a rising savings rate, partially offsetting the positive impulse from an improving business cycle. Moreover, once the economic activity starts to strengthen again, the Fed could decide to withdraw some of the specific measures it had put in place in support of the US economy.

Following a decline in GDP of 2.5-3% in 2009, growth in 2010 could be in the range of 1-1.5% and around 2.5% in 2011.

### **Other regions**

- *Japan: recession ended in Q2'09*
- *Emerging countries: China in the driver seat once more*

Recession in Japan ended in Q2'09 as GDP growth moved again into positive territory (0.6% quarter-on-quarter) mainly supported by a positive contribution from net trade.

Nevertheless, the outlook for Japan continues to be weak. Rising unemployment does not bode well for private consumption. The outlook for the corporate sector is improving but remains heavily exposed to China. GDP is seen falling by 5.4% this year, followed by 1-1.5% growth in 2010/11. China has taken up its role as powerhouse in the Asian region once again. Supported by the government stimulus programme and pressure on the banking sector to ease credit supply, domestic demand boomed in Q2'09: official figures show 7.9% (AR) GDP growth. Exports continued to be weaker than imports and as a result, China's trade surplus has declined substantially in recent months. This helped intra-regional trade in Asia to recover from a low level. However, the credit surge is not without risk. A large proportion has been used to finance property and equity purchases, with a potential negative effect of bad loans on the financial sector.

While the Asian emerging countries registered positive GDP growth in Q2'09, economic conditions were less favourable in other regions. Particularly Russia and Mexico continued to suffer from falling investment and private consumption.

After contracting by approx. 1% in 2009, global GDP is forecast by the IMF to rise by about 3% in 2010. Within this timeframe, developing Asia is seen remaining a cornerstone of global growth.

## II. The EU Steel Market

### Overview Steel Using Sectors

**Development of the main steel using sectors – Eurofer forecast October 2009**  
 % change year-on-year in the SWIP (Steel Weighted Industrial Production) index

	Steel Consumption by sectors in %	Year 2008	Q109	Q209	Q309	Q409	Year 2009	Q110	Q210	Q310	Q410	Year 2010	Year 2011
Construction	27	-0.8	-11.0	-5.9	-6.3	-4.1	-6.7	-2.3	-1.3	0.7	0.6	-0.5	2.8
Structural steelwork	11	-1.8	-16.1	-13.1	-15.7	-10.3	-13.9	-1.7	0.5	1.2	1.5	0.4	2.9
Mechanical engineering	14	-1.0	-20.6	-26.7	-22.4	-17.3	-21.8	-5.1	2.0	2.5	3.7	0.8	4.7
Automotive	16	-5.9	-41.2	-36.1	-23.5	-7.3	-28.9	10.2	1.3	-3.9	-2.0	1.2	4.5
Domestic appliances	4	-4.6	-15.2	-19.3	-12.0	-4.5	-12.8	-0.3	1.2	1.2	2.1	1.2	0.6
Shipyards	1	6.2	-7.3	-15.0	-31.4	-36.2	-22.7	-14.9	-16.0	-4.9	-1.9	-10.2	2.0
Tubes	12	-1.1	-29.2	-34.1	-23.7	-14.5	-26.0	-1.5	5.0	5.1	6.1	3.6	5.8
Metal goods	12	-2.3	-27.4	-28.4	-20.6	-11.8	-22.6	1.6	3.5	2.4	3.0	2.6	5.3
Miscellaneous	3	2.3	-14.4	-22.4	-16.9	-12.9	-16.6	0.8	2.9	2.0	1.4	1.7	4.4
<b>TOTAL</b>	<b>100</b>	<b>-2.0</b>	<b>-23.0</b>	<b>-22.2</b>	<b>-16.9</b>	<b>-10.1</b>	<b>-18.2</b>	<b>-0.4</b>	<b>1.0</b>	<b>1.1</b>	<b>1.7</b>	<b>0.9</b>	<b>4.0</b>

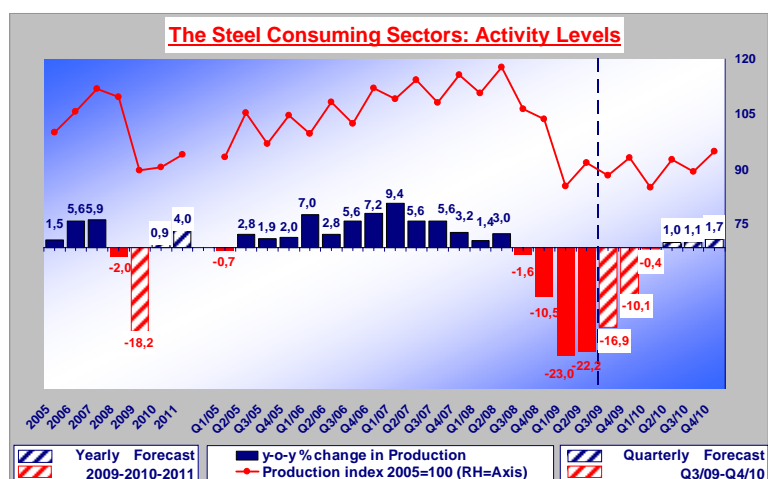
- *EU steel using sectors stuck in slow motion to well into 2010*
- *2011: more pronounced recovery*

Activity in the EU steel using sectors continued to decline sharply in the 2<sup>nd</sup> quarter of 2009. As a result, output in the 1<sup>st</sup> half of the year was almost 23% down on the same period of 2008. Companies had to cope with an unprecedented drop in demand for industrial goods, both in the EU and in global export markets. Despite stabilising financial markets, financing remained a major bottleneck for most companies. Significantly reduced industrial activity and extremely uncertain business conditions led to sharp inventory reductions in the downstream processing chain. Business prospects for the coming quarters remain bleak although overall sentiment appears to be improving. Since July, new industrial orders started to recover slightly from the lows reached earlier in the year. The latest PMI survey data for the manufacturing

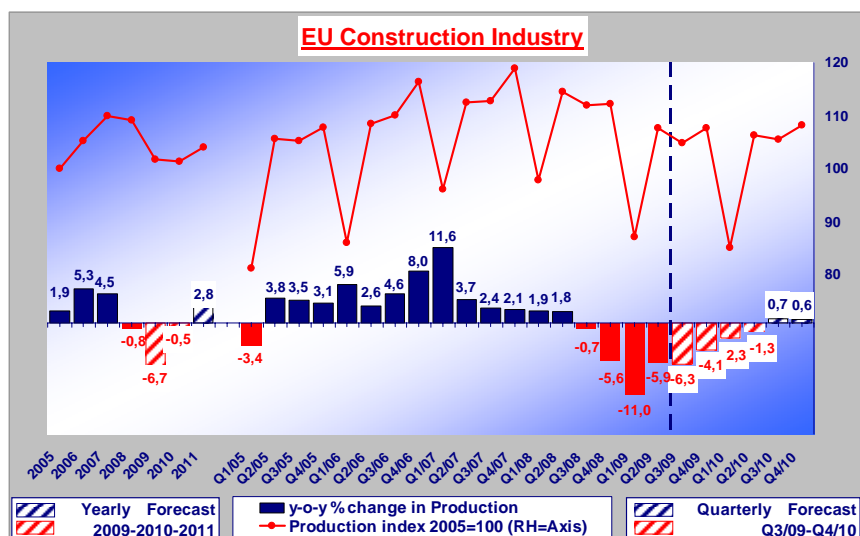
sector also suggest some recovery in output from a low level in the months ahead. This should reduce the overall drop in production in the steel using sectors to 18% this year.

The forecast for 2010 shows a gradual further improvement; from Q2 onwards year-on-year growth could become slightly positive again. On balance, output is expected to register only a very modest growth.

Improving economic conditions should lead to a more pronounced recovery in 2011; the first estimate for steel-weighted industrial production shows a 4% rise.



## Construction



- **Construction downturn seen continuing into 2010**
- **Civil engineering awaits impulse public investment**

Following a sharp contraction in output in the 1<sup>st</sup> quarter, EU construction output fell almost 6% in the 2<sup>nd</sup> quarter of 2009, leading to a decline of more than 8% in the 1<sup>st</sup> half of the year. This figure hides significant differences at the country level. While Spain and the UK continued to register very sharp declines, growth in output was reported to be still positive in Poland.

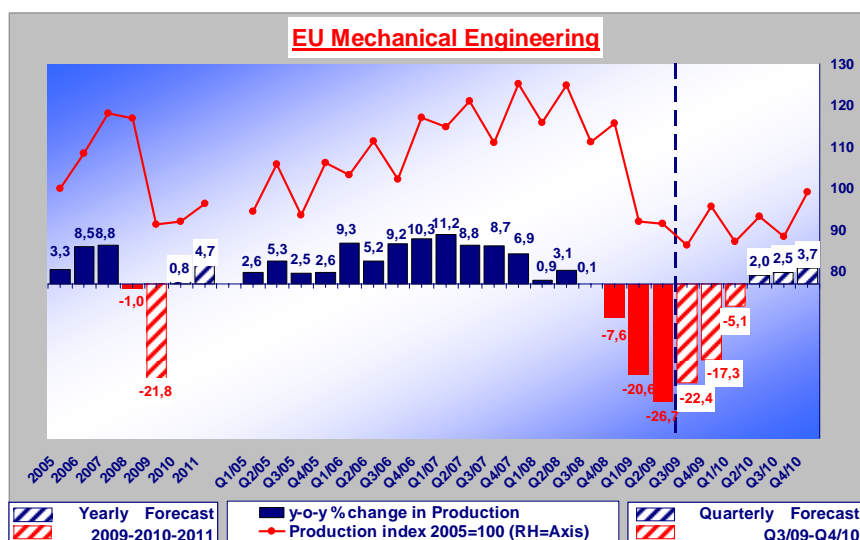
As far as the different construction sectors are concerned, the downturn in the non-residential sector has deepened markedly. This is reflected by the almost 15% y-o-y drop in output of structural steel fabricators in the 1<sup>st</sup> half of 2009. Low confidence levels and difficult financing conditions have led to very few new projects starting up recently. Meanwhile, new residential construction activity appears to have stabilised at a depressed level. The relatively best performing construction sector is currently the renovation and modernisation sector, more specifically

in infrastructural works owing to increased government spending.

The short-term outlook remains rather grim. Construction confidence has stabilised at a low level since May; construction companies continue to be very pessimistic on the overall order situation. Particularly for the non-residential construction sector, the most important consumer of constructional steel products in the EU, prospects are negative. Particularly private commercial and industrial building projects will continue to be hampered by the large stock of non-residential buildings, difficult project financing and weak confidence levels. Meanwhile, the civil engineering sector awaits the potential impulse from increased public spending; so far, the positive effect has been limited to renovation work but is expected to spread to new projects in 2010.

While this may reduce the overall decline in EU construction output to 0.5% in 2010, the sector will have to wait until 2011 before output growth will be positive again supported by a pickup in construction investment.

## Mechanical Engineering



- ***Downturn deepened in Q2'09***
- ***Output flat in 2010 and seen rising by almost 5% in 2011***

The mechanical engineering sector is one of the steel-using sectors most impacted by the global downturn. The year-on-year decline in production deepened to almost 27% in the 2<sup>nd</sup> quarter of this year. Strong investment in machinery and equipment in previous years and manufacturing activity falling off a cliff resulting in under-utilisation of capacity, heavy inventory decumulation in the processing industries, financing restrictions and low confidence levels resulted in a global collapse in EU and international export demand.

The latest projections for activity in the coming quarters show the negative growth trend in output continuing into the 1<sup>st</sup> quarter of 2010. The latest order surveys signal that mechanical engineering companies in the EU have remained extremely pessimistic on incoming order intakes and the order book situation. New orders in Germany fell in August 43% y-o-y, only slightly less negative than in the first half of

2009. Underlying demand conditions are seen remaining difficult for the time being. Investment in machinery and equipment in the EU looks set to decline slightly further in 2010 following a massive 15% drop this year. While international trade appears to be picking up from a low level – particularly in the Asian region – the improvement is basically driven by rising demand for commodities and intermediate goods. Moreover, the continued strength of the Euro is not supportive to the competitive position of Eurozone exporters.

While it is expected that the decline in output in the 2<sup>nd</sup> half of 2009 will be less negative than in the first half of the year, the overall drop in production in 2009 could still amount to almost 22%. Next year is forecast to see marginal growth owing to a mild growth in output turning positive again from the 2<sup>nd</sup> quarter onwards. On balance production could rise by almost 1%.

In 2011, improving business conditions should lead to a recovery in demand and output in the mechanical engineering sector.

## Automotive



- **Incentives soften downturn car market, reduce stock overhang**
- **Recession hits commercial vehicle market extremely hard**
- **EU output to rise again in 2011**

EU car sales registered 3.3% growth in August following fairly similar growth rates in June and July; this reduced the overall decline in sales over the 1<sup>st</sup> 8 months to 7.9% y-o-y. Scrapping premiums and generous producer incentives fuelled sales in most large EU markets – particularly in Germany - in summer while reducing the decline in registrations in smaller countries.

Meanwhile, commercial vehicle registrations continued their strongly downward trend during the summer months. Total CV sales fell 35.5% in August and 37.4% y-o-y in the 1<sup>st</sup> 8 months of the year. Demand for heavy trucks in Central Europe is especially hit by the downturn with sales falling by 73% in this period.

Weak demand in Europe and elsewhere and inventory clearance by most producers resulted in output falling by close to 40% in the first half of 2009. Thanks to scrapping premiums and other incentives stimulating demand, the stock

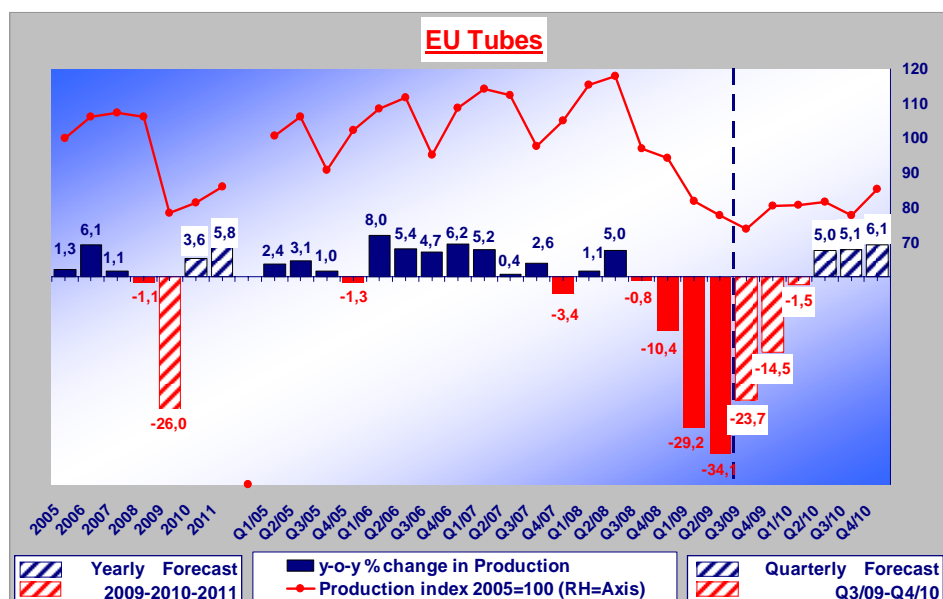
overhang of passenger cars has been largely reduced and currently demand and output are assessed to be better aligned than at the start of the year.

However, the artificial stimulation of passenger car sales in 2009 through incentives also implies that the market would weaken again next year. In most EU countries, the scrapping scheme funds have been exhausted and will not be extended into 2010. Moreover, rising unemployment and private consumers rebuilding savings will have a negative effect on private consumption.

The market outlook for the commercial vehicle segment is probably even worse: strongly reduced transport activity, difficult financing and weak business confidence will depress vehicle demand for the time being. In addition, significant fleet renewal has taken place in recent years.

All in all, EU automotive production is expected to decline by almost 22% in 2009. Output in 2010 is expected to be more or less flat compared with 2009. Projections for 2011 signal that output - supported by improving economic conditions - could rise by 4.5%.

## Tubes



- **Drop in output deepened in Q2'09**
- **Stock cycle drives 2010 pickup**
- **Output will gain strength once final demand improves**

Steel tube production in the EU has been hit hard by the recession. Output in the 2<sup>nd</sup> decreased by more than 34% y-o-y, following a close to 30% drop in production in the 1<sup>st</sup> quarter of this year. Extremely weak activity levels at the customer level of the tube producers and massive inventory reductions by customers in the distribution and processing chain resulted in an unprecedented drop in tube production in the 1<sup>st</sup> half of 2009.

Against the background of the persisting weak business activity expected for basically all end-user sectors of the steel tube industry in the EU, the short-term market outlook for the tube industry is very subdued.

While the decline in tube output in the 2<sup>nd</sup> half of 2009 could be slightly less deep than in 1<sup>st</sup> half, output is seen falling by 26% this year.

The downward trend in production is seen easing in early 2010 and growth may turn positive again from the 2<sup>nd</sup>

sector onwards. A positive impulse could come from the stock cycle; some restocking by distributors and end-users seems plausible. However, without final demand improving as well, the restocking effect will be limited. The current outlook suggests that end-use consumption could gradually strengthen from mid '10 onwards.

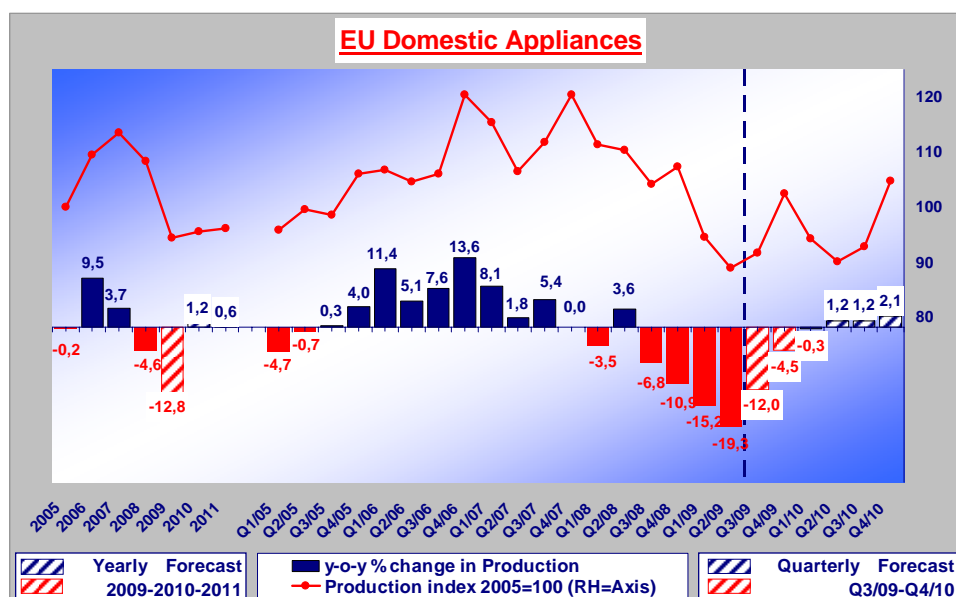
By market segment the situation is differentiated. So far this year, global drilling and exploration activity has been relatively weak due to reduced levels of energy consumption in most economic regions. OCTG demand should improve during 2010 as the economic situation in developing Asia and in the US start to improve.

The outlook for large welded tube projects is seen remaining weak, mainly because of financing restrictions. Current projects will not be fully replaced by new ones.

Small welded tube demand will not recover before mid 2010.

All in all, output may rise modestly in 2010 supported by the stock cycle and shift into a higher gear once the business cycle picks up in 2011.

## Domestic Appliances



- **Consumer retrenchment reduces demand and output**
- **No major improvement expected for 2010-2011**

Output of electrical domestic appliances fell 19.3% y-o-y in the 2<sup>nd</sup> quarter of 2009, to the lowest level since the late nineties. Production in the 1<sup>st</sup> half of 2009 was 13% down on the same period of 2008.

The major factors leading to this drop in output have been overall weak confidence levels, rising unemployment, restrictions in consumer credit and depressed property markets across Europe. The latter impacted both sales of new existing homes while having negative wealth effects as well. The number of residential property transactions has seen a significant reduction since the start of the year. Consequently, demand for electrical domestic appliances is well below levels registered in previous years.

The outlook for the coming quarters is for a continuation of difficult business conditions for the electrical domestic appliance producers in Europe.

Demand will continue to suffer from weak consumer sentiment due to the expected rise in unemployment. This will certainly act as drag on private consumption growth.

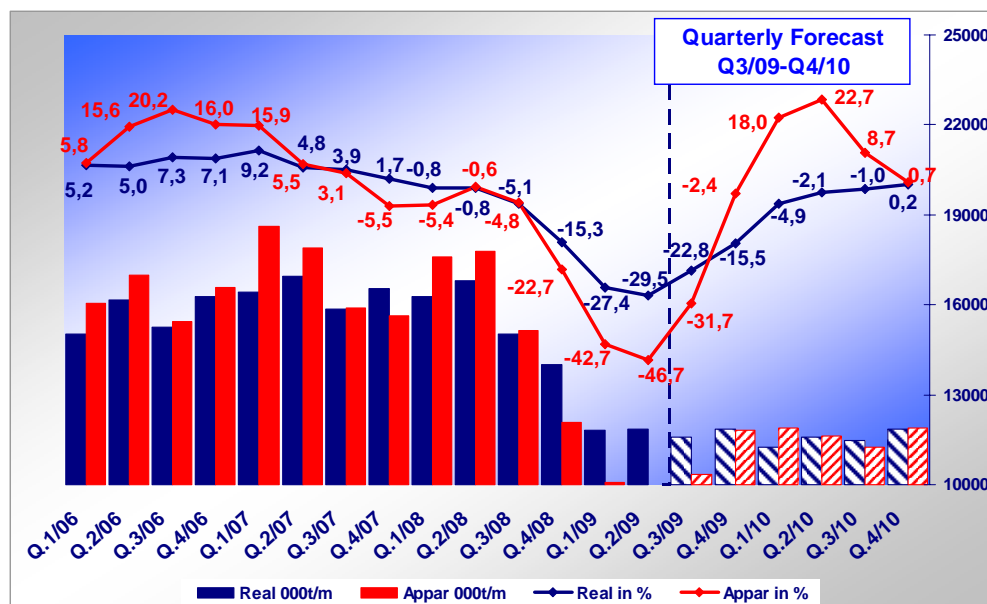
The housing sector downturn is also forecast to hold on for the time being. Another concern is increasing competition from Asian producers trying to expand their potential market share in Europe.

Following the close to 13% drop in EU output expected for 2009, the outlook is for a marginal pickup in the 2010-2011 timeframe. Prospects for Central European countries are relatively positive owing to recent investment in modern production facilities and their advantage in terms of labour costs and availability of skilled workforce.

## Real Consumption

### Forecast for real consumption - % change year-on-year

Period	Year 2008	Q109	Q209	Q309	Q409	Year 2009	Q110	Q210	Q310	Q410	Year 2010	Year 2011
	-5,5	-27,4	-29,5	-22,8	-15,5	-24,2	-4,9	-2,1	-1,0	0,2	-2,0	4,1



- **Depressed end-user activity continues to slash real steel consumption**
- **2010 to remain weak**
- **Recovery expected in 2011**

EU real steel consumption fell by almost 30% y-o-y in the 2<sup>nd</sup> quarter of 2009 reflecting the persisting weakness of activity in the steel-using sectors. The decline was slightly deeper than in the 1<sup>st</sup> quarter and resulted in an overall drop in real consumption of 28.5% y-o-y in the first 6 months of 2009.

The latest estimates and forecasts for the evolution of real steel consumption in the EU in the remainder of this year and in 2010 signal that demand side fundamentals in the EU steel market will remain extremely depressed.

The estimate for the 3<sup>rd</sup> and 4<sup>th</sup> quarter of 2009 sees real steel consumption falling quite sharply although the

anticipated rate of year-on-year decline will ease to some extent towards the end of the year. All in all, real steel consumption is expected to decrease by approx. 24% this year.

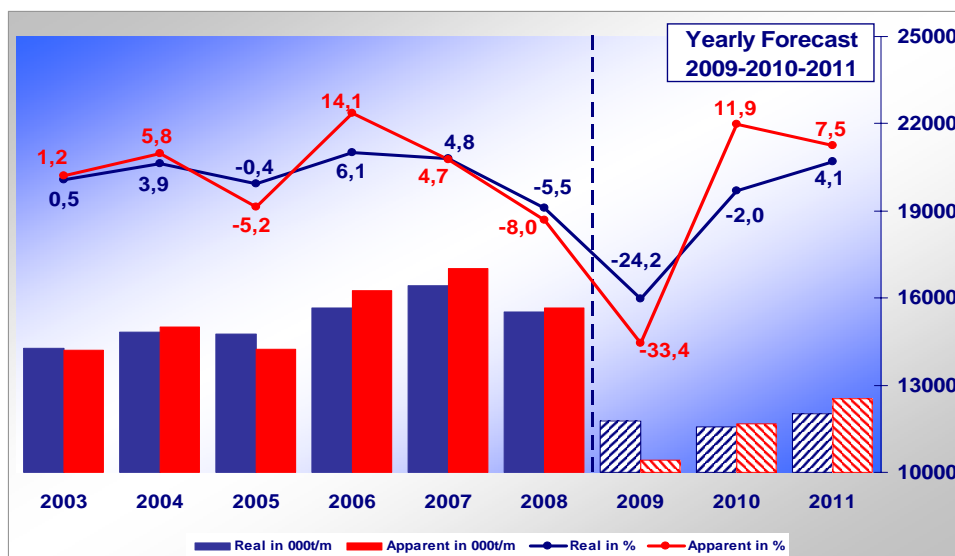
According to the latest forecasts from EUROFER's Economic Committee a return to positive growth is not to be expected before the final quarter of 2010. Next year will see a further easing in the negative growth trend of real consumption. A low level stabilization is to be reached during the final quarter of the year. On balance this translates into a further 2% drop in real consumption in 2010.

With a forward view to 2011, some improvement in market conditions seems plausible in line with the expected recovery in end-user activity. Real consumption could rise by 4%.

## Apparent Consumption

### Forecast for apparent consumption - % change year-on-year

Period	Year 2008	Q109	Q209	Q309	Q409	Year 2009	Q110	Q210	Q310	Q410	Year 2010	Year 2011
	-8,0	-42,7	-46,7	-31,7	-2,4	-33,4	18,0	22,7	8,7	0,7	11,9	7,5



- **Q3'09 stocks better aligned with dramatically reduced demand**
- **2010: stock cycle sets the stage**
- **Improving market fundamentals in 2011**

The decline in apparent steel consumption accelerated to almost 47% y-o-y in the 2<sup>nd</sup> quarter as the drop in real consumption deepened and the inventory correction process in the steel supply chain intensified. It resulted in apparent consumption falling by 45% in the 1<sup>st</sup> half of 2009.

Estimates for the 3<sup>rd</sup> quarter show apparent consumption remaining at an extremely low level and still falling by almost 32% y-o-y due to continued weak end-user demand and further inventory reductions. However, as a result of several quarters of heavy destocking, the overall inventory situation in Q3'09 is better aligned with the current weak level of demand. Drastic production cuts at EU mills and substantially reduced third country imports supported the process of balancing supply with demand.

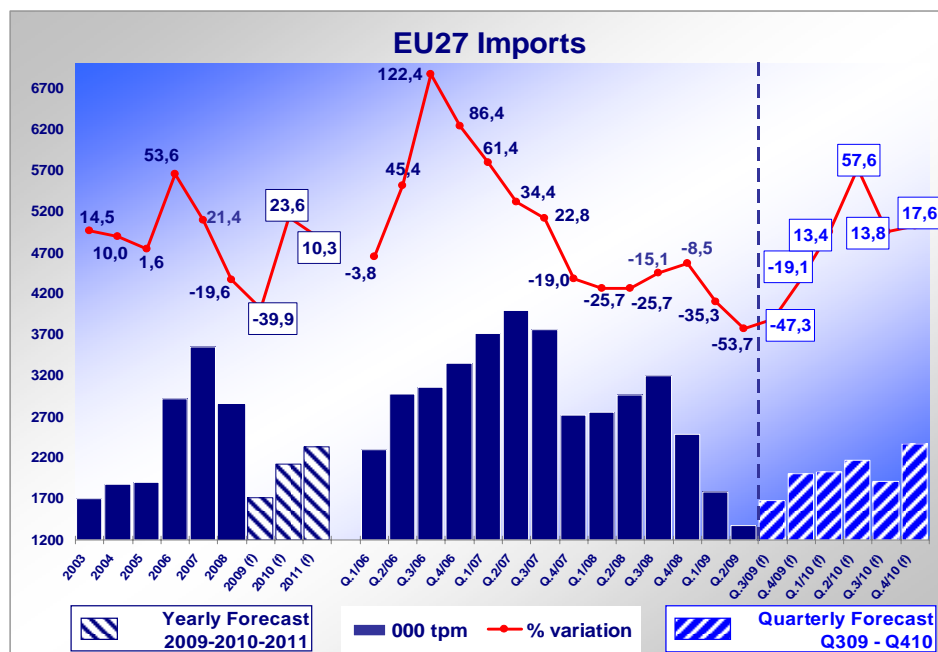
Significantly reduced steel inventories resulted in some customers cautiously returning to the market in recent months to fill gaps in their stocks. This led to the downward trend in orders and deliveries bottoming out.

The stock cycle effect is expected to be neutral in the final quarter of 2009. On balance, apparent consumption will fall by approx. 33% this year.

The stock cycle will also set the stage in 2010. The supply-demand situation is expected to be roughly balanced over the year while remaining vulnerable to supply side disruptions such as rising imports. The absence of severe destocking as registered in 2009 will lead to a 'technical' recovery in apparent consumption which is forecast to rise by almost 12%.

Market fundamentals should improve in 2011, as rising end-user activity will support a recovery in real steel consumption. This will also trigger the need to align stocks with higher downstream output. Apparent steel consumption could grow by 7.5%.

## Imports



- **H1'09 imports down 45% y-o-y**
- **Sharp drop Chinese exports**
- **Imports seen rising again in 2010-2011**

In the 2<sup>nd</sup> quarter of 2009 third country suppliers withdrew further from the EU steel market forced by the absence of buying interest and low price levels. This resulted in imports falling by almost 54% y-o-y and a 45% reduction in imports over the 1<sup>st</sup> half of the year. Particularly exports from China to the EU have diminished compared with the high levels registered in 2007 and 2008. Meanwhile, depending on the product, other countries such as Turkey, Ukraine, South Korea, Serbia and Taiwan have stepped up their deliveries to the EU market.

Against the background of the continued fragility of the EU steel market – expected to last well into 2010 – the import situation remains a major issue of concern.

Rising international steel prices in combination with the reported

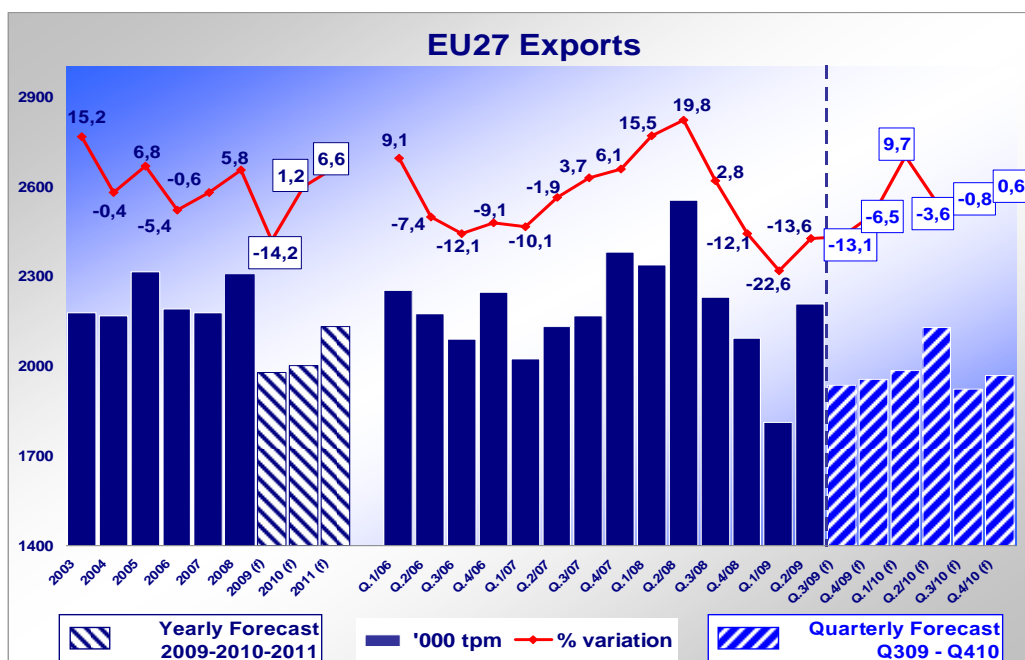
overcapacity in the Chinese steel market could lead to Chinese exporters increasingly targeting overseas markets again. Chinese finished steel exports increased in the June-August period. Although Southeast Asia so far remained the main outlet, the continued surge in production – outpacing demand – could lead to rising exports to the EU.

On balance, third country imports are seen falling by 40% in the whole of 2009.

This trend is expected to reverse in 2010. Underpinned by the recent rise in import licenses, imports are seen bouncing back from the low levels reached in 2009. Total imports could increase by almost 24% in 2010 and further 10% in 2011.

Global crude steel production being increased in anticipation of a recovery in steel demand which yet has to materialise remains a major risk for the EU supply-demand balance.

## Exports



- **H1'09 exports fell 18% y-o-y**
- **EU temporary net exporter**
- **Trend to reverse in Q4'09**
- **Exports seen rising very mildly**

In the 2<sup>nd</sup> quarter of 2009, export deliveries by EU27 mills to third countries fell by almost 14% y-o-y and by 18% in H1'09.

Since imports fell more sharply than exports, resulting in overall lower imports than exports, this implies that the EU became a net exporter of steel products in this period. Especially long product producers have been able to find some compensation for the sharp decline in demand from the domestic EU market in other regions such as

North Africa and the Middle East. While this situation probably continued in the 3<sup>rd</sup> quarter of this year, the trend is expected to reverse in the final quarter of this year.

The main reason for the EU becoming a net importer again is the anticipated rise in 3<sup>rd</sup> country imports.

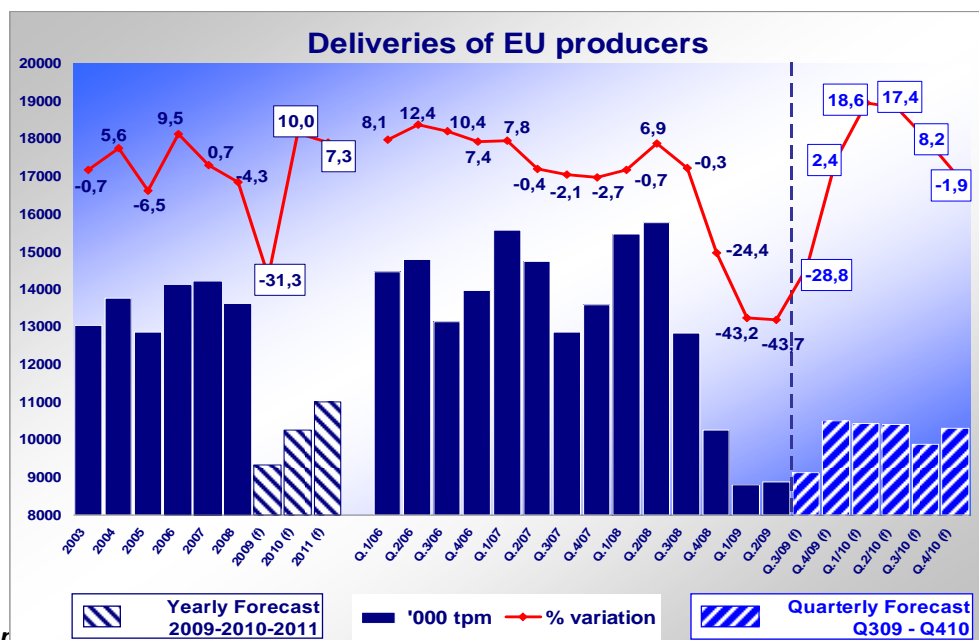
Meanwhile, actual export volumes are not seen increasing significantly in the 2010-2011 period.

The latest forecasts from EUROFER's Economic Committee show exports rising by only 1% in 2010 and just below 7% in 2011 in tandem with improving demand fundamentals in international export markets.

Changes in %	IMPORTS Third Countries	EXPORTS Third Countries	COMMUNITY DELIVERIES OF EU PRODUCERS
Year 2008	-19.6	5.8	-4.3
Q.I/2009	-35.3	-22.6	-43.2
Q.II/2009	-53.7	-13.6	-43.7

### FORECAST

Q.III/2009	-47.3	-13.1	-28.8
Q.IV/2009	-19.1	-6.5	2.4
Year 2009	-39.9	-14.2	-31.3
Q.I/2010	13.4	9.7	18.6
Q.II/2010	57.6	-3.6	17.4
Q.III/2010	13.8	-0.8	8.2
Q.IV/2010	17.6	0.6	-1.9
Year 2010	23.6	1.2	10.0
Year 2011	10.3	6.6	7.3



1) Based on