



**Analysts:**

**BOB RICHARD, CFA**

T: 216-525-8430

E: brichard@longbowresearch.com

**LUKE FOLTA**

T: 216-525-8408

E: lfolta@longbowresearch.com

Industry: **STEEL**

Coverage:

<b>Ticker</b>	<b>Rating</b>	<b>Price</b>
AKS	Buy	\$12.43
CMC	Neutral	\$9.73
GNA	Buy	\$5.20
GTI	Neutral	\$6.64
NUE	Buy	\$33.88
RS	Neutral	\$19.91
SCHN	Neutral	\$23.39
STLD	Neutral	\$9.41
WOR	Neutral	\$11.14
X	Buy	\$35.51
ZEUS	Neutral	\$18.03

## The Steel Weekly

- Per the enclosed analysis, based on historical data, we believe the decline in long product pricing will be less than that for flat products in the current steel sell-off.
- Due to the domestic industry being coke short, we estimate blast furnace steelmaking would have to fall nearly 25% for any impact to be felt on met coal demand or pricing.
- Australian recycler SMS writes down inventory in its recently reported September-ending fiscal quarter as overseas customers are either demanding a lower price than earlier agreed to amounts or turning back material all together.
- Metals USA 3Q08 earnings recap is enclosed.
- The ABI, a harbinger for non-residential construction spending, declined 6.2 points sequentially in September to 41.4.

*Important Disclosures are found on last page.*



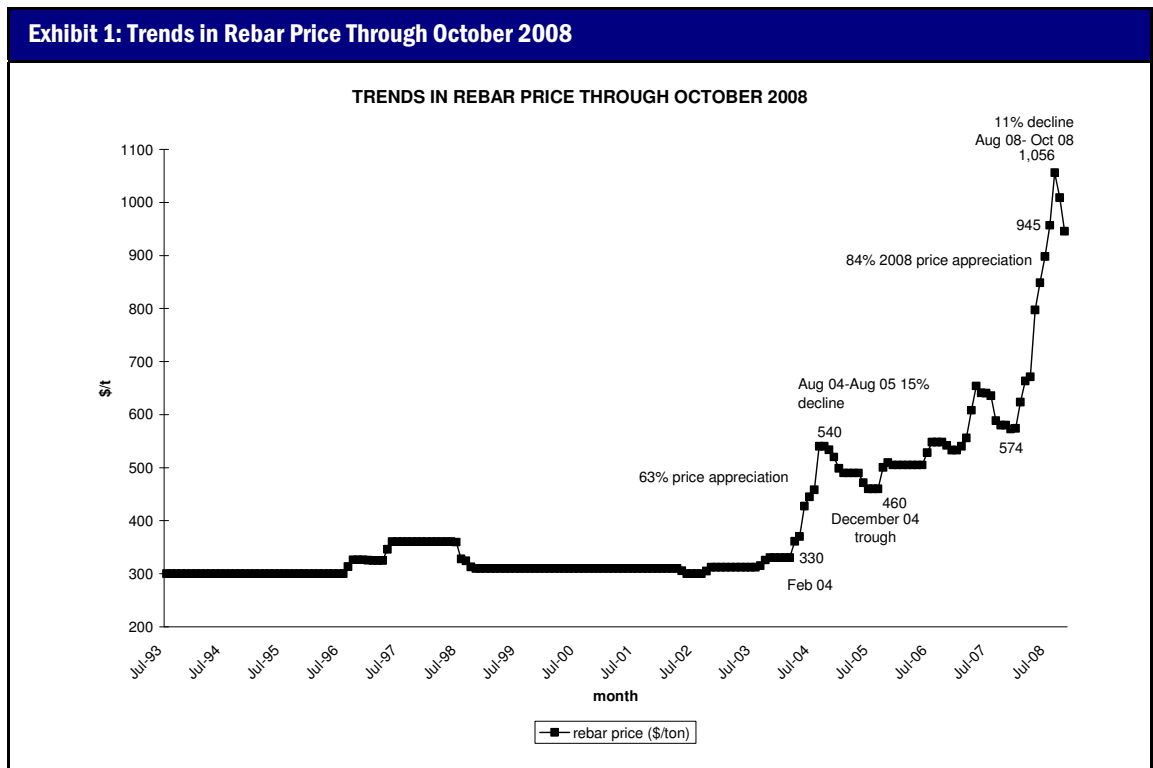
### Long Product Pricing Trends Versus Service Center Inventory

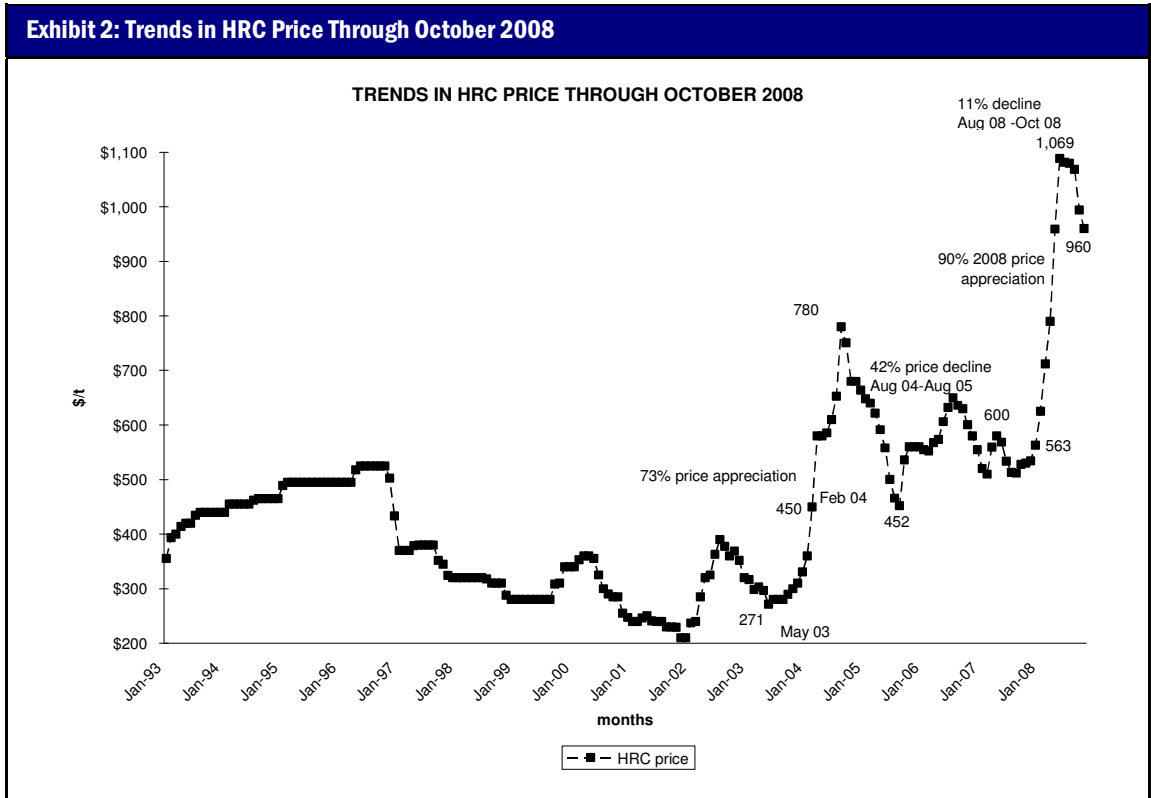
We analyzed long product pricing trends against service center bar inventories and rebar imports to get a feel of what realizations could do in the pending downturn. In summary:

- Rebar selling price has been less volatile than hot rolled coil, even though MSCI monthly demand trends for bar products have been more variable than those for flat rolled.
- During the 2003-2005 pricing cycle and 1H08 steel product appreciation, rebar price swings have been less than those for hot rolled.
- There is significantly less bar inventory in the service center channel than in the 2003-2005 pricing cycle.
- Over the last fifteen years, rebar pricing has seemingly been impacted very little by import volumes.

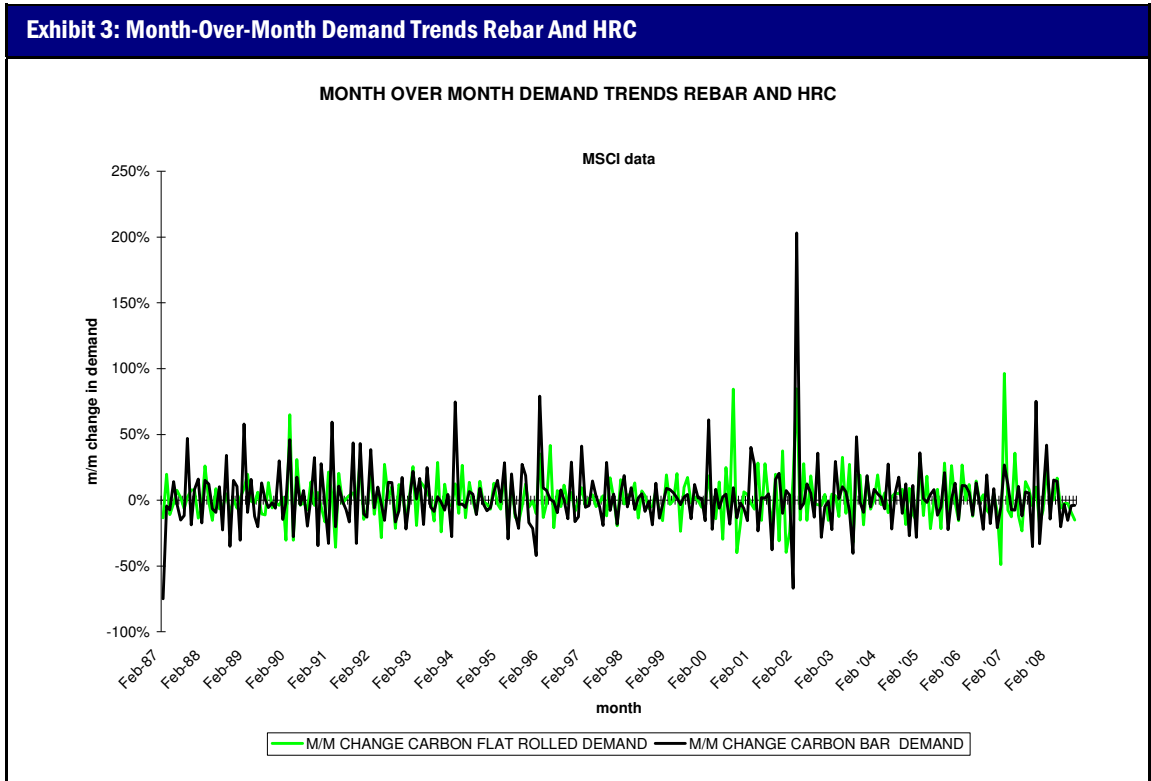
The above would imply the pending downturn in rebar pricing will be less severe than that for flat rolled products. A graphical discussion follows.

Rebar pricing has, through 2007, been much more stable than hot rolled coil over the same course of time. Per the below, rebar has appreciated slightly less in 2008, on a percentage basis, than hot rolled has, and its price swings in 2003-2004 were less.





The lesser volatility in rebar pricing than that for hot rolled is modestly surprising, given that month-over-month demand changes for bar products, per MSCI data, are greater than that for flat rolled. All things being equal, we would expect hot rolled, with its seemingly flatter demand schedule, to have lesser pricing variability. That is not the case.



MSCI bar inventories have not shown the volatility that flat rolled inventories have over the last fifteen years. The former have shown a mostly downward trend, while flat rolled inventories have been much more variable. There is strikingly less long product inventory now than in the last 2004-2005 price decline, with bar product inventories at fifteen-year lows.



Exhibit 4: Carbon Bars Non Seasonally Adjusted Inventory Tons

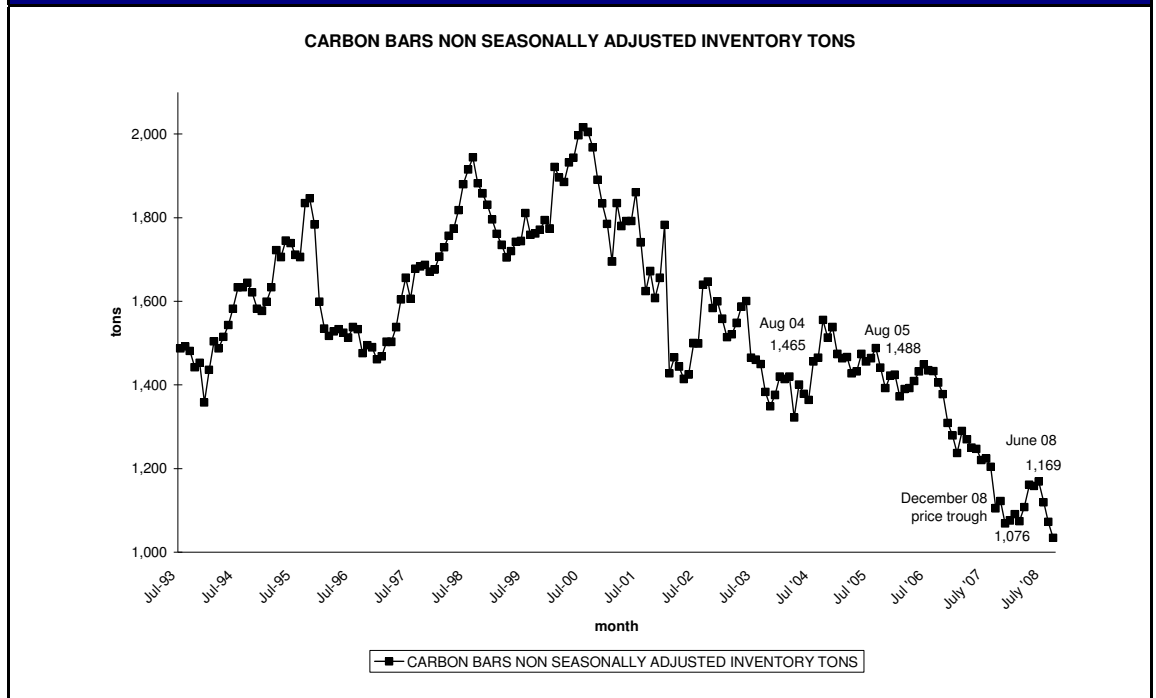
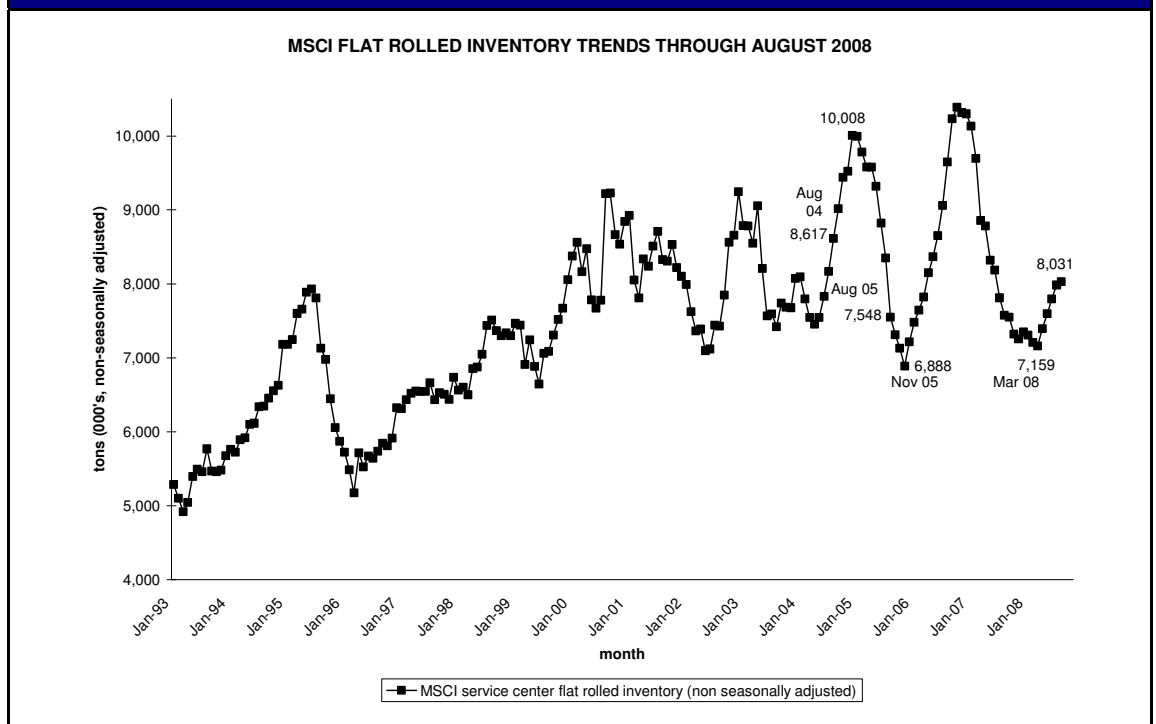
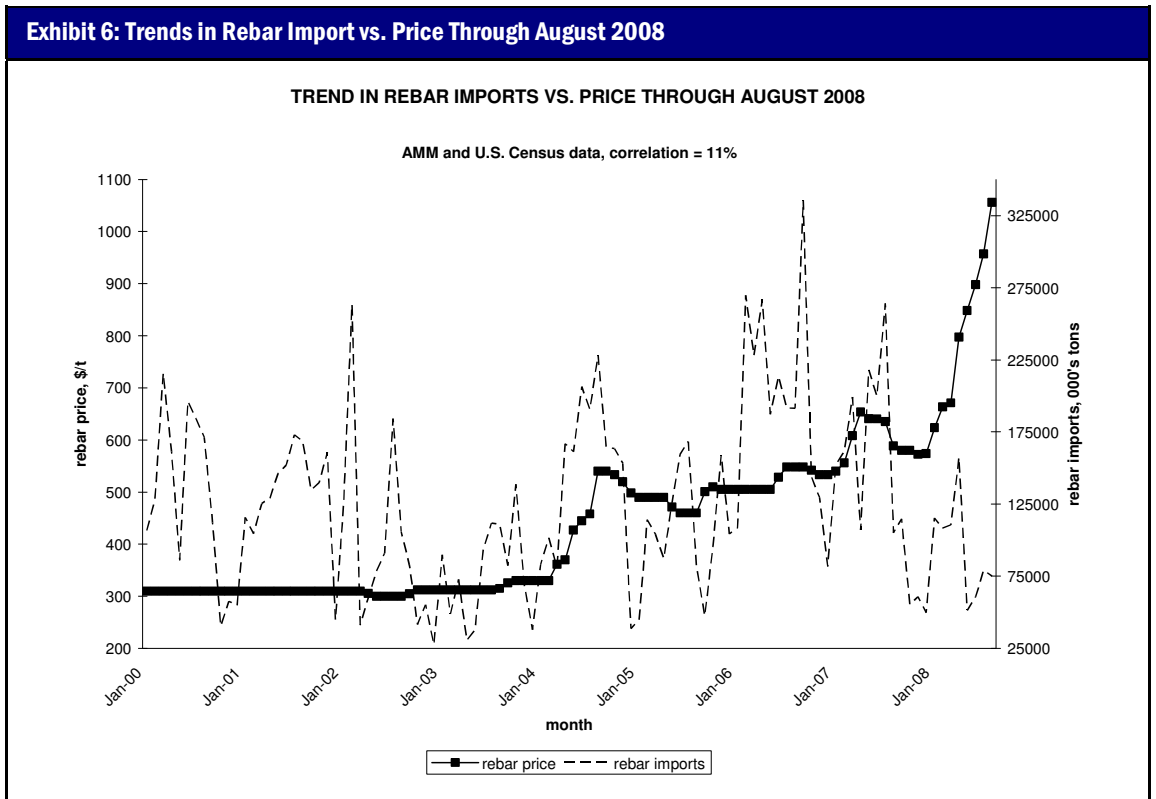


Exhibit 5: MSCI Flat Rolled Inventory Trends Through August 2008





We note the little correlation between rebar import levels and pricing over the long term, and the lack of current imports even at this historically highest sales price is surprising.





**Why Domestic Met Coal Demand Should Stay Strong**

We remind readers that our domestic steel industry is coke short, with imports supplying a formidable portion of our requirements. At all ranges of reasonable met coal prices, it is far more economically attractive to use own make coke than imports. Per the below, we estimate that domestic steelmaking capacity would have to decline nearly 25% for 2009 met coal demand to be affected.

<b>Exhibit 7: Estimated Met Coal Requirements</b>	
2008 estimated US blast furnace production (000 tons)	37,697
tons of coke required to support above steel production (000 tons)	15,079
2008 estimated imported coke (000 tons)	3,414
2008 calculated own make coke (000 tons)	11,665
annual steel production supported by own make coke (000 tons)	29,162
% reduction in BF utilization needed to impact domestic met coal requirements	23%
Source: US Census & IISI	

This is why we expect met coal pricing should hold up much better than other steelmaking materials' price in the current downturn.



#### **Met Coal Iron Ore Update**

The 10%-40% Indian iron ore contract price increase, backdated to April 1 of this year and announced early last week for its domestic customers, was significantly less than what would have been in line with the recent Australian-Sino annual price agreement. The 10% increase is slated for lowest quality fines while the higher 40% adjustment will be for lump ore. Contract negotiations between the Indian sellers and Asian contract consumers are expected to commence the first week of November.

China's comments of the need to maintain one worldwide iron ore price is noted. Its threat that Indian spot ore will not be imported next year if there is a discrepancy between it and Australian price is newsworthy. The Chinese are intent on setting the worldwide iron ore price based on their negotiations with the Australians, minimizing the impact Indian selling price has on the market. To date we have heard little Indian resistance.

#### **Scrap Space Update**

Local business press reported that SCHN Hawaii has stopped accepting deliveries of ferrous materials, effective immediately. The bulk shipper that removes auto body scrap has dropped SCHN from its pick-up schedule, highlighting the weakness in demand from the Asian consumer.

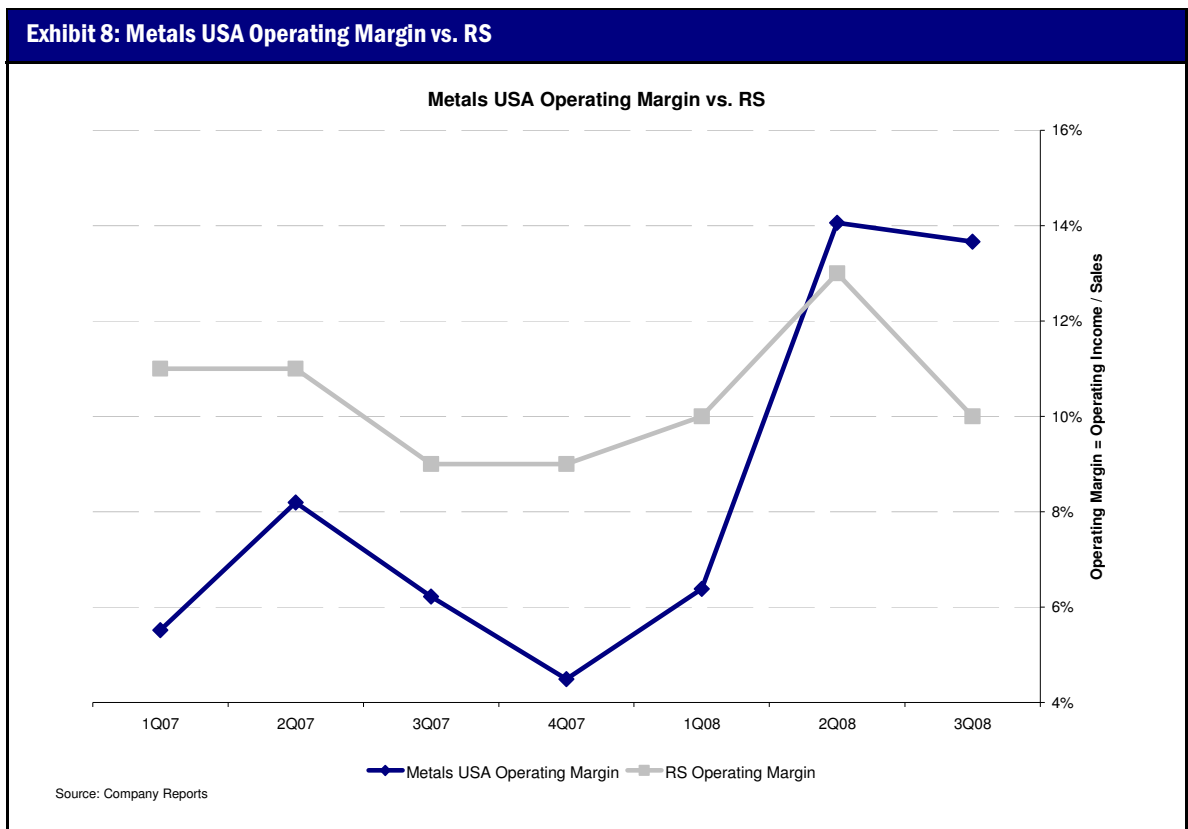
**Recycling Today** has reported that with October's drastic decline in scrap realizations, buyers are demanding significant concessions on already agreed to sales prices. This has caused significant disruption to the market, and has destabilized price significantly. We take away from Australian recycler SMS' earnings call last week that write-downs of European inventory were recorded for the accounting period ending in September, and that no guidance was being offered for the Company's next fiscal quarter due to high uncertainty in the market.



### Metals USA Reports 3Q08 Earnings

Last week Metals USA reported 3Q08 net income of \$36.0, compared to a \$3.4 million dollar loss the previous year. Adjusted EBITDA was \$90.1 million versus \$36.1 million in last year's comparable period. Market conditions were reportedly favorable; the Company's CEO expects 4Q08 to be comparable to past fourth quarters. (In 4Q07, Metals USA earned \$8 million on \$420 million revenues.) Book inventory values were reported reasonable, but the Company intends to bring tonnage levels down significantly in 4Q08. Although both housing-related end markets and automotive remain weak, the roofing segment was reported strong. Metals USA stated it has taken advantage of export opportunities to Central America and regions of Africa. Defense spending is expected to remain favorable going forward.

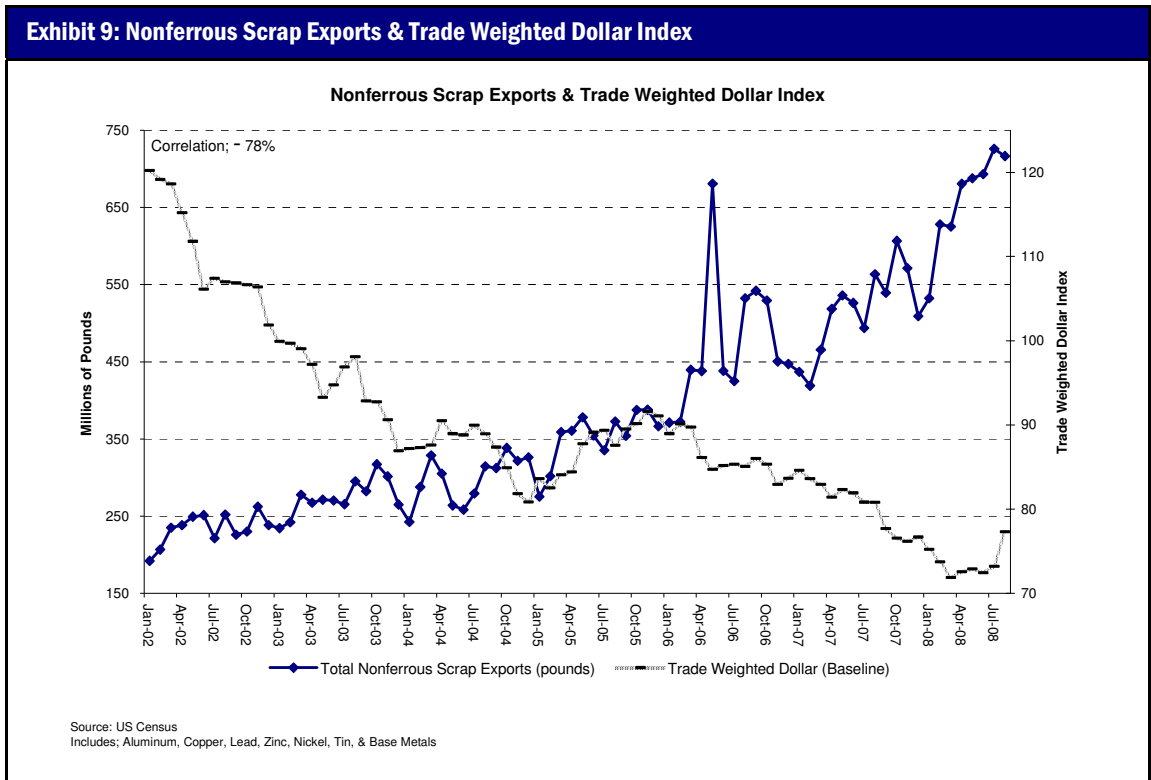
The below graph illustrates Metals USA outperforming its peer, RS, with respect to operating margins in the past two quarters.





**August's Nonferrous Scrap Export Volumes Remain Elevated**

Although we expect them to be off considerably in September, nonferrous scrap export volumes declined only 1% in August from the previous month, and remain 27% higher than last year's comparable period. Aluminum, 59% of total, decreased by 9% sequentially, and was slightly offset by copper, 31% of total, which increased 14%. Year-to-date nonferrous scrap export volumes are up 34%. The following graphs and table provide an overview of recent nonferrous scrap export trends through August.



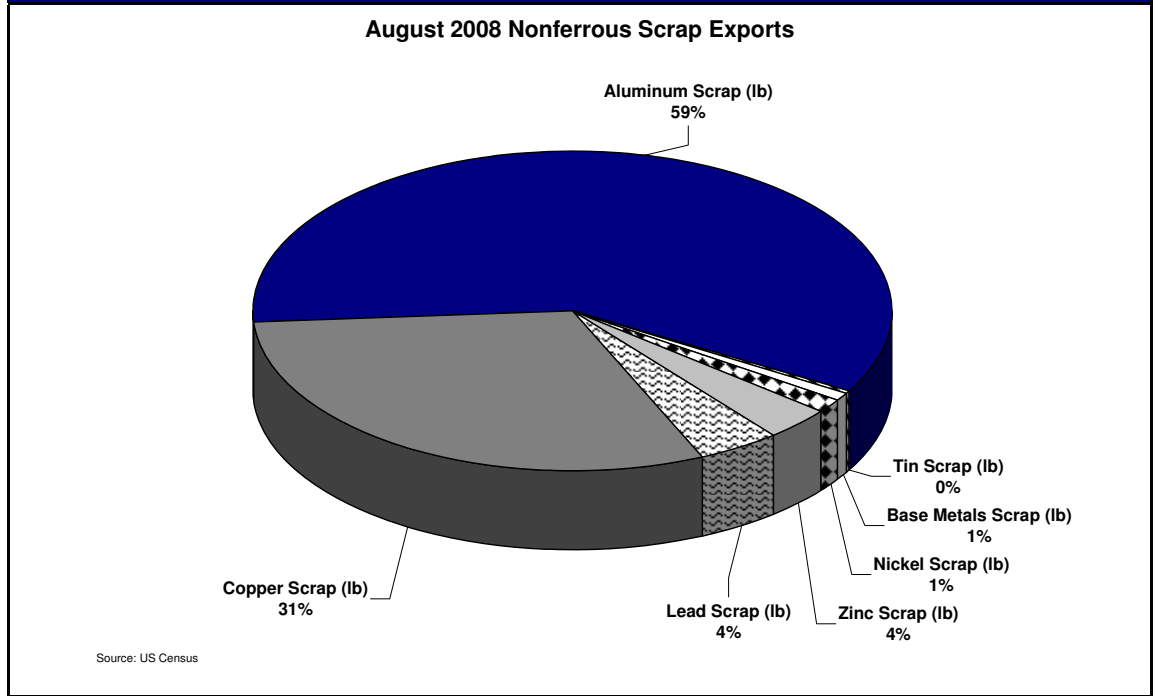
**Exhibit 10: August 2008 Nonferrous Scrap Exports**

August 2008 Nonferrous Scrap Exports				
	Pounds	m/m Δ	y/y Δ	YTD Δ
Tin Scrap (lb)	2,059,104	-43%	-1%	14%
Base Metals Scrap (lb)	6,842,179	55%	218%	11%
Nickel Scrap (lb)	8,320,594	7%	-36%	-48%
Zinc Scrap (lb)	25,280,580	12%	34%	-1%
Lead Scrap (lb)	29,400,589	-1%	18%	72%
Copper Scrap (lb)	219,213,978	14%	11%	5%
Aluminum Scrap (lb)	425,524,860	-9%	40%	57%
<b>Total Nonferrous Scrap Exports</b>	<b>716,641,884</b>	<b>-1%</b>	<b>27%</b>	<b>34%</b>

Source: US Census



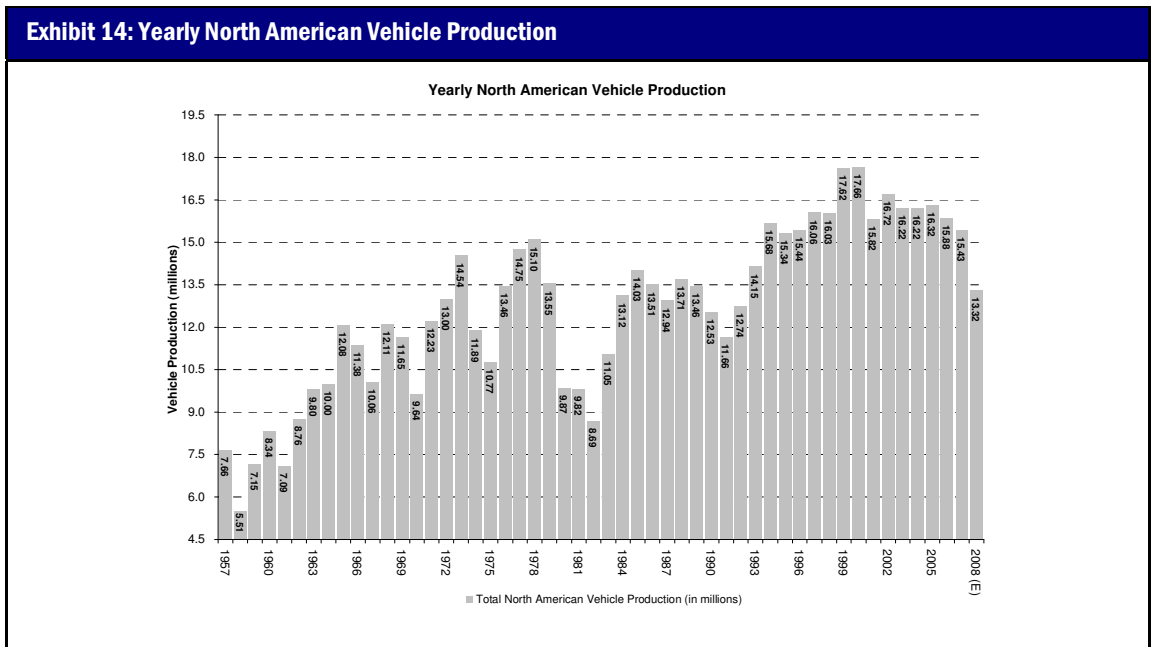
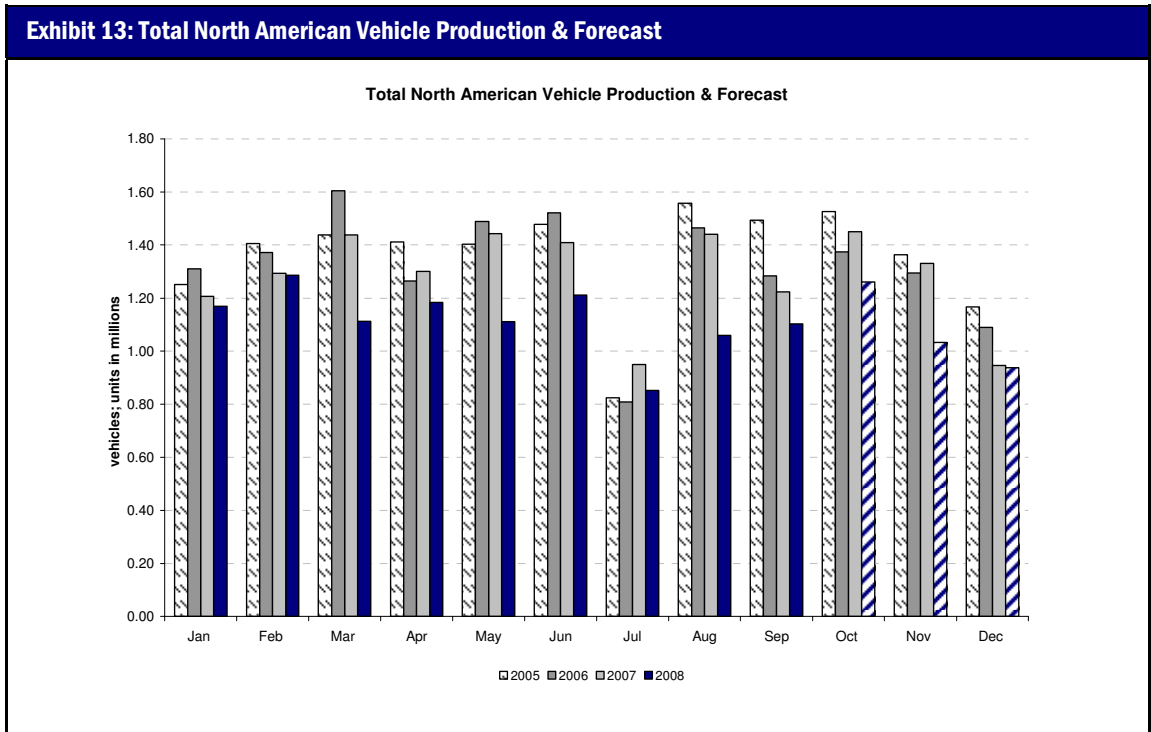
Exhibit 11: August 2008 Nonferrous Scrap Exports





**September North American Vehicle Production Updated**

Total vehicles produced in North America during September were 1.1 million units. Actual production was 4% lower than *Ward's* most recent forecast. On a year-over-year basis, September's production has decreased 10%. The following graphs show recent monthly and historical yearly trends. FY08 total North American vehicle production is forecast 13.32 million units.

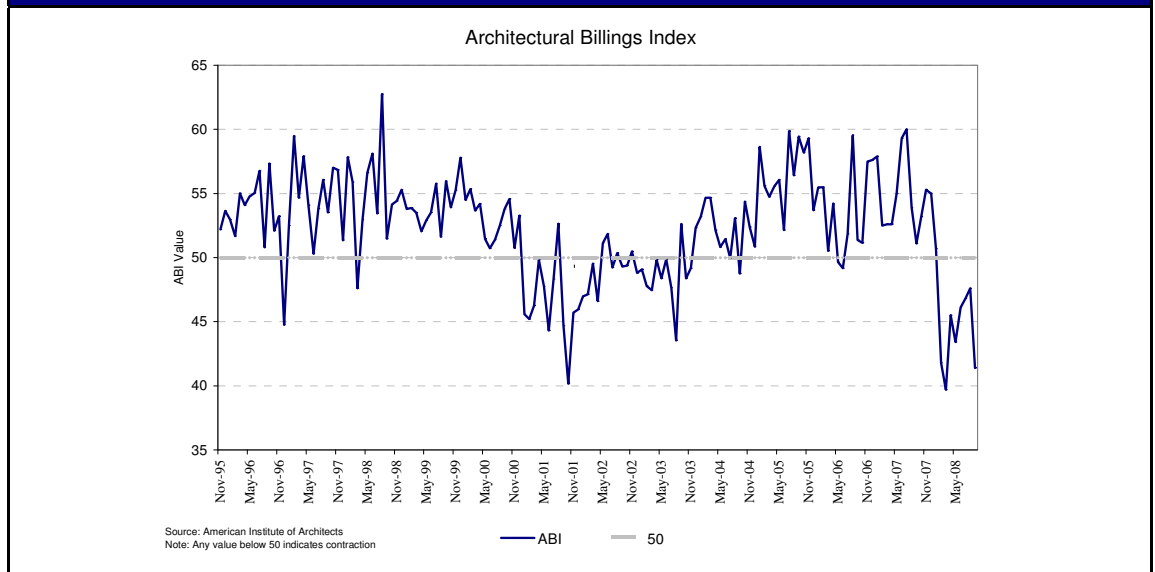




### The ABI Declines Month Over Month in September

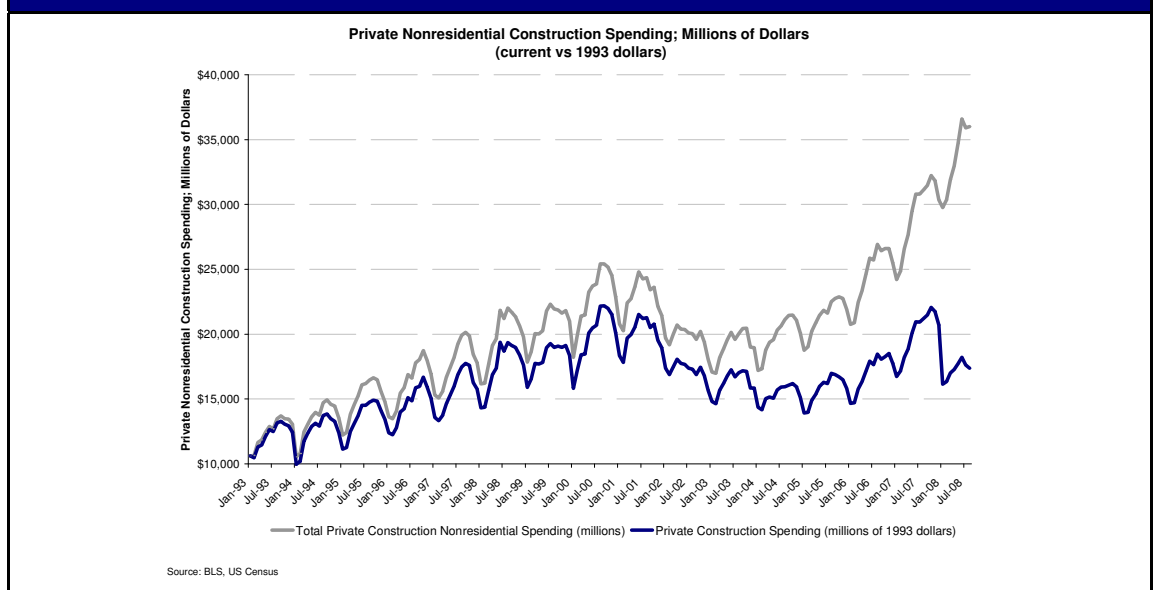
September's Architectural Billings Index (ABI) decreased to 41.4, down from 47.6 in August. The ABI is a leading indicator for nonresidential construction spending, and is best correlated when lagged five months.

**Exhibit 15: Architectural Billings Index**



Below we have graphed current construction spending versus deflated spending through August of this year. This trend shows how volumes of materials used in nonresidential construction are beginning to trend downward year-over-year in recent months, even though being higher in current dollar terms.

**Exhibit 16: Private Construction Spending Nonresidential (current vs. 1993 dollars)**





### Electrical Steel Cost Inputs Continue to Decline in October

The below graph illustrates the main cost inputs factored into ATI's electrical steel surcharge. The posted surcharge is set to decline through December and be \$0.263 per pound in that month. Natural gas is used as the energy cost due to extensive annealing during the manufacturing process. Using the below cost inputs, we see lagging them with the surcharge two months provides the best correlations. Electrical steel surcharges have come down significantly from their September peak of \$0.5835 per pound. Despite costs declining, domestic producers stated they received double-digit price increases for FY09.

Exhibit 17: ATI Grain Oriented Electrical Steel vs. Cost Inputs

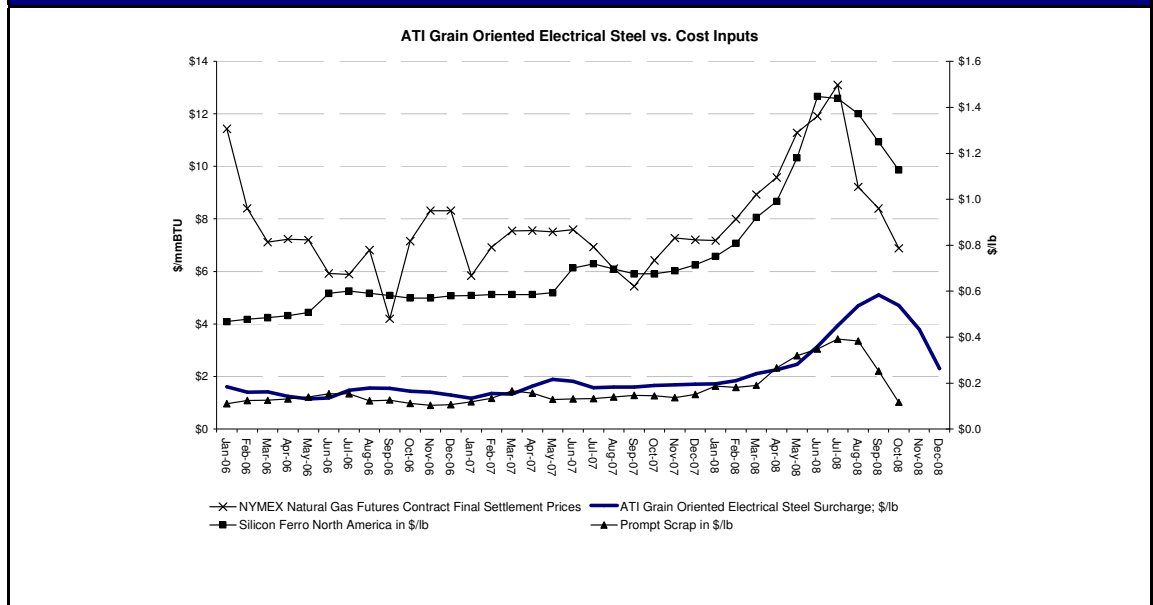
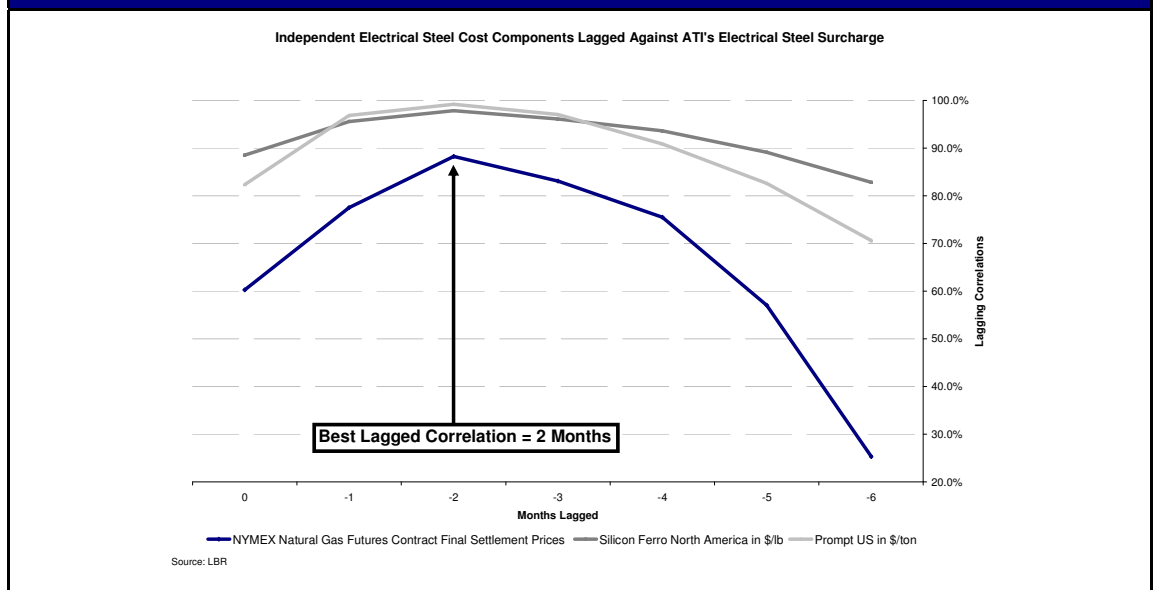


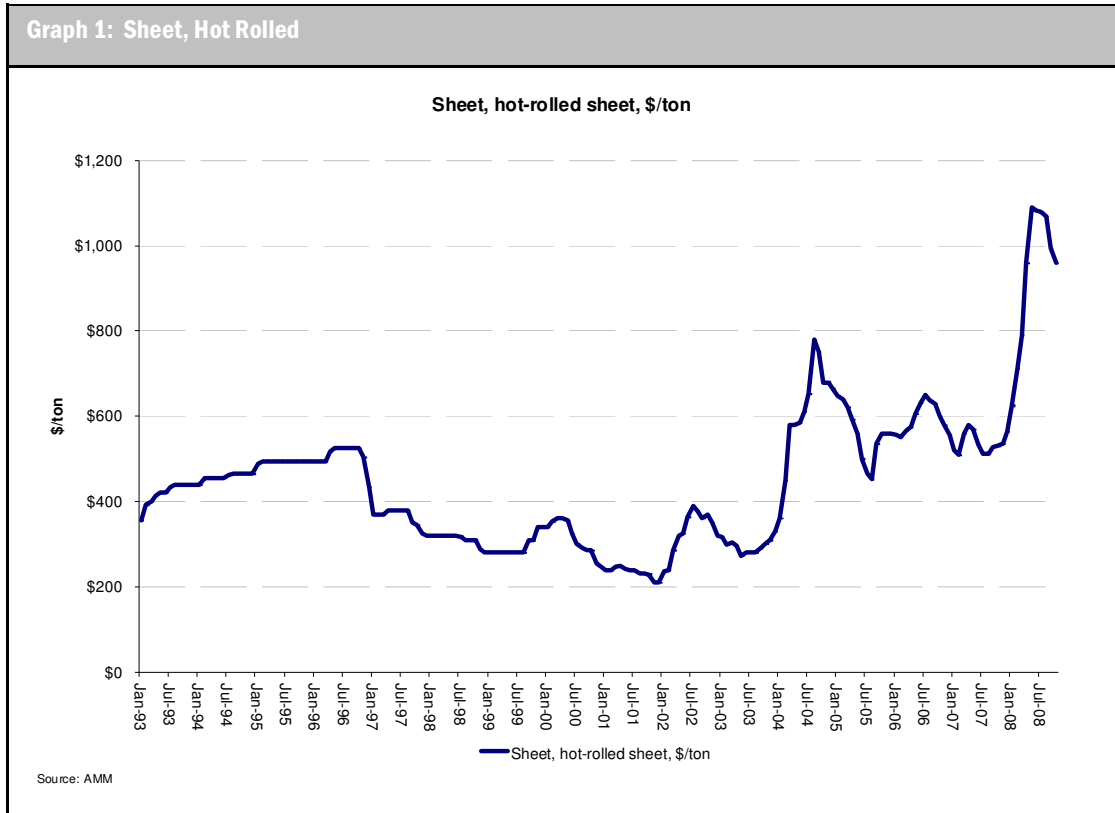
Exhibit 18: Independent Electrical Steel Cost Components Lagged Against ATI's Surcharge



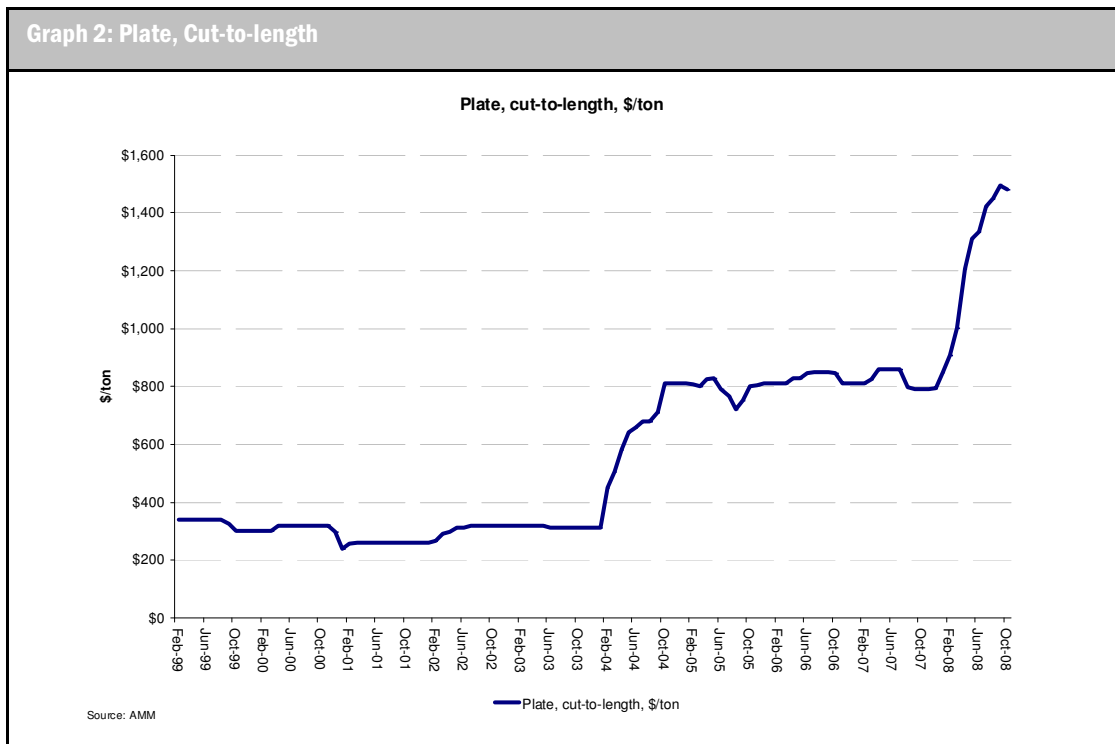


### Steel Industry Charts

October's hot rolled coil price is \$960 per ton, a 3% sequential decrease. **SBB** had reported prices of \$760 per ton last week.



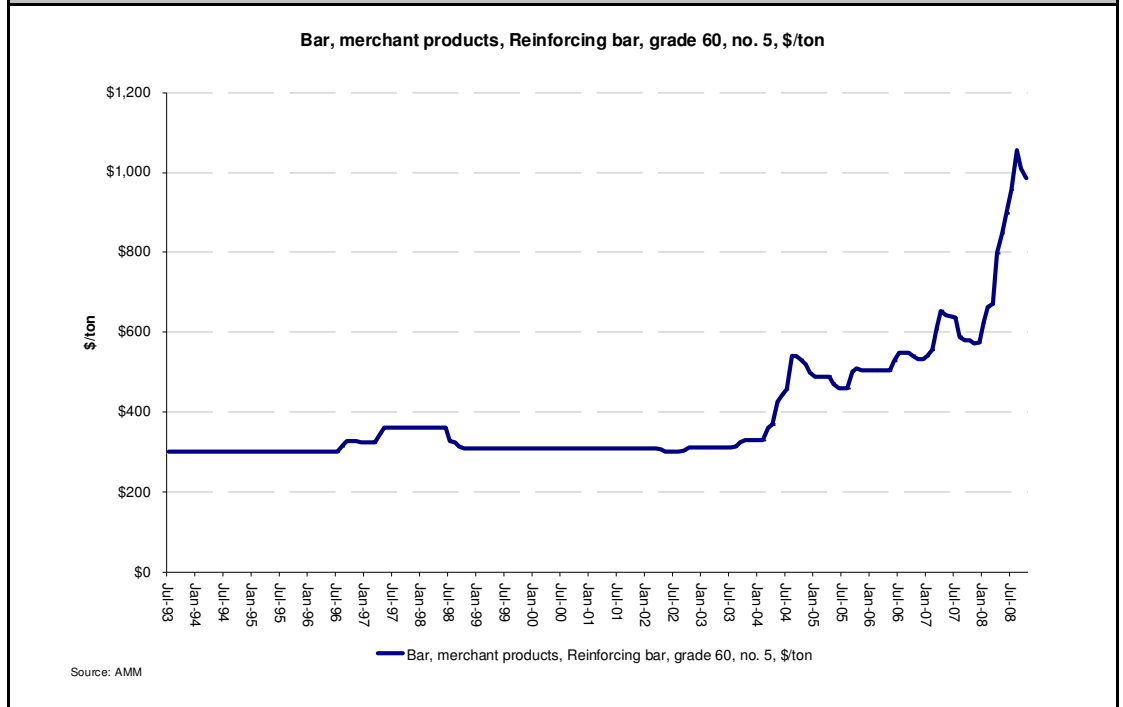
October's plate price is \$1,480 per ton, representing a \$16 sequential decrease. Effective November 1, list prices will be down \$80.





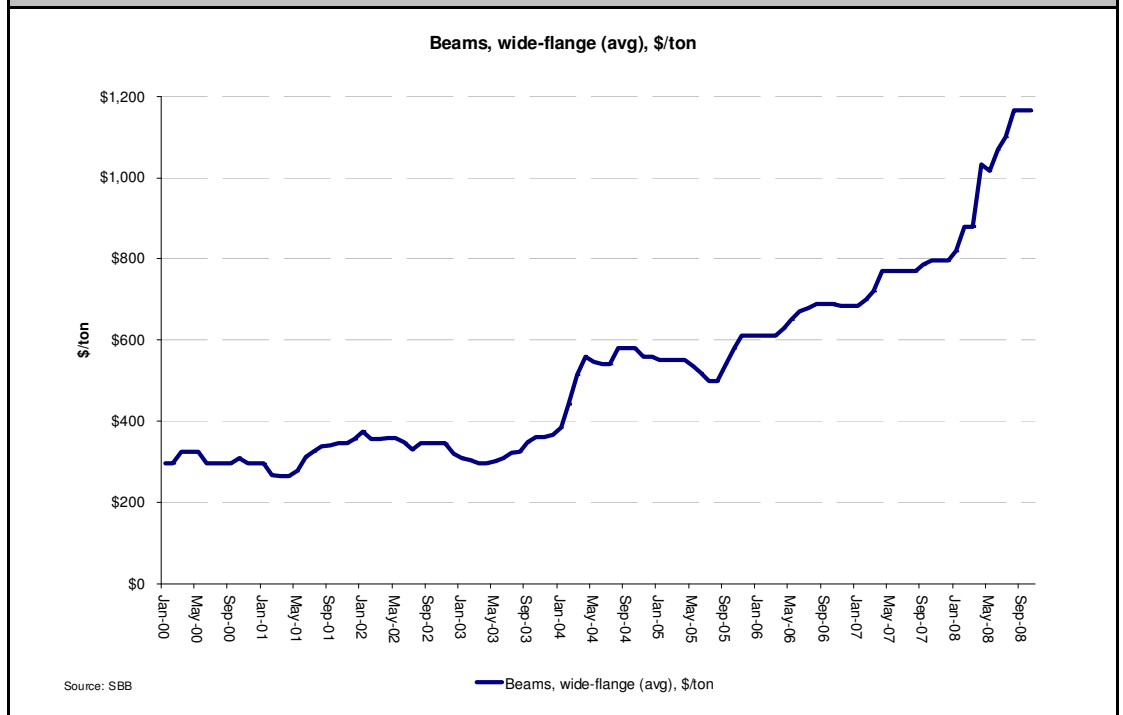
Rebar prices are \$986 per ton in October, a 2% decrease from the previous month. With the most recent price adjustment, current rebar prices are \$856.

Graph 3: Bar, Merchant Products, Rebar



According to SBB data, October's beam price is flat at \$1,165 per ton. Effective November 1, list prices will be down \$80. Last Friday STLD decreased beam prices to \$950 per ton; we are awaiting information whether that will be matched by NUE.

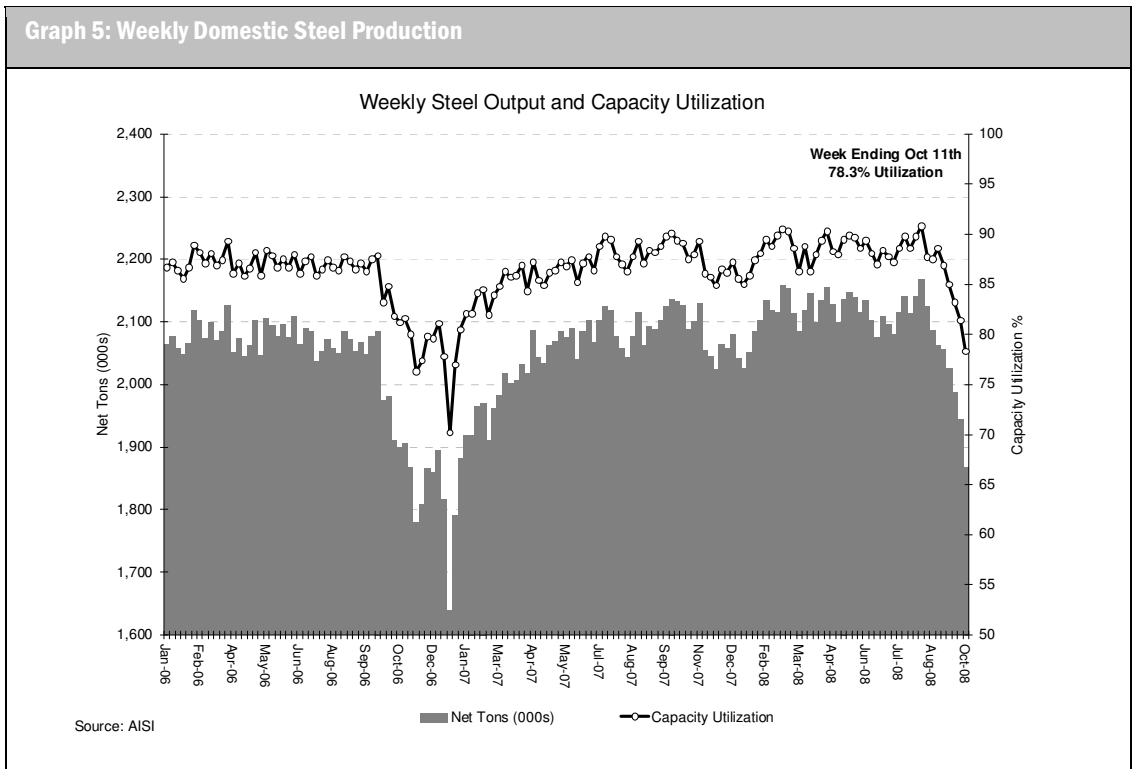
Graph 4: Beams, Wide-flange





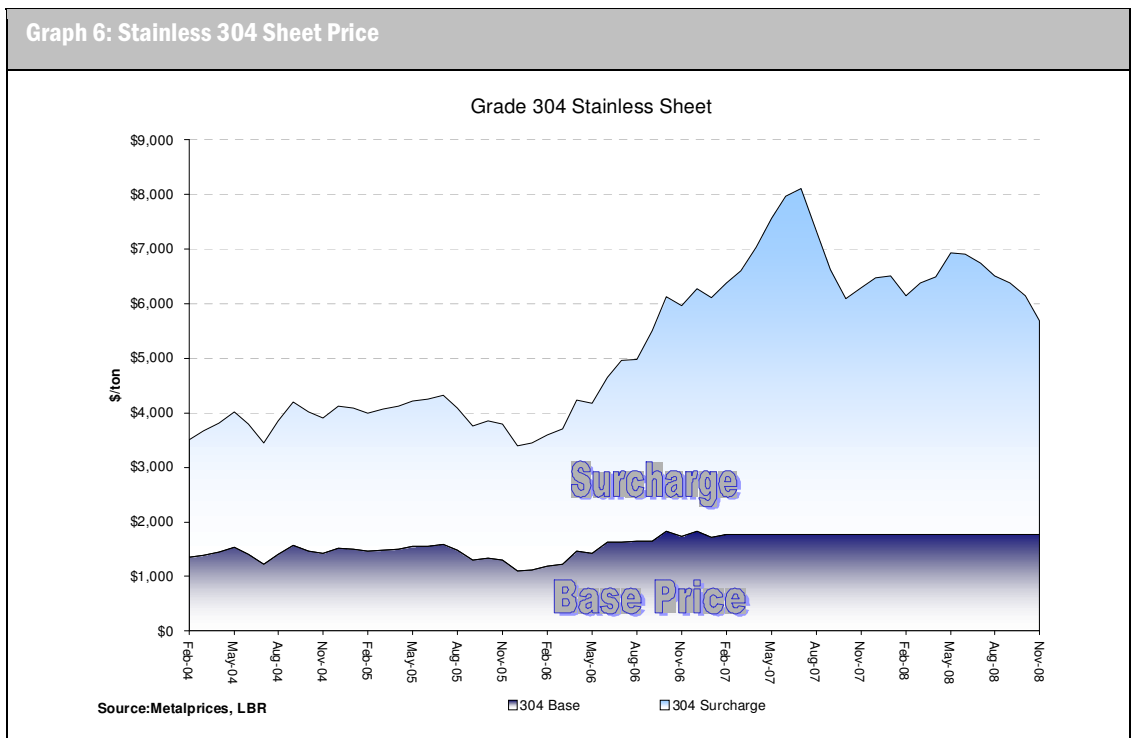
Weekly domestic steel production was 1,744,000 tons and capacity utilization is 73.1%. Year-to-date production is up 1.1%. These are the lowest utilization levels since 4Q06.

Graph 5: Weekly Domestic Steel Production



Stainless steel (grade 304) prices will decrease in November (-10% sequentially to \$1.9548/lb). Base prices are unchanged.

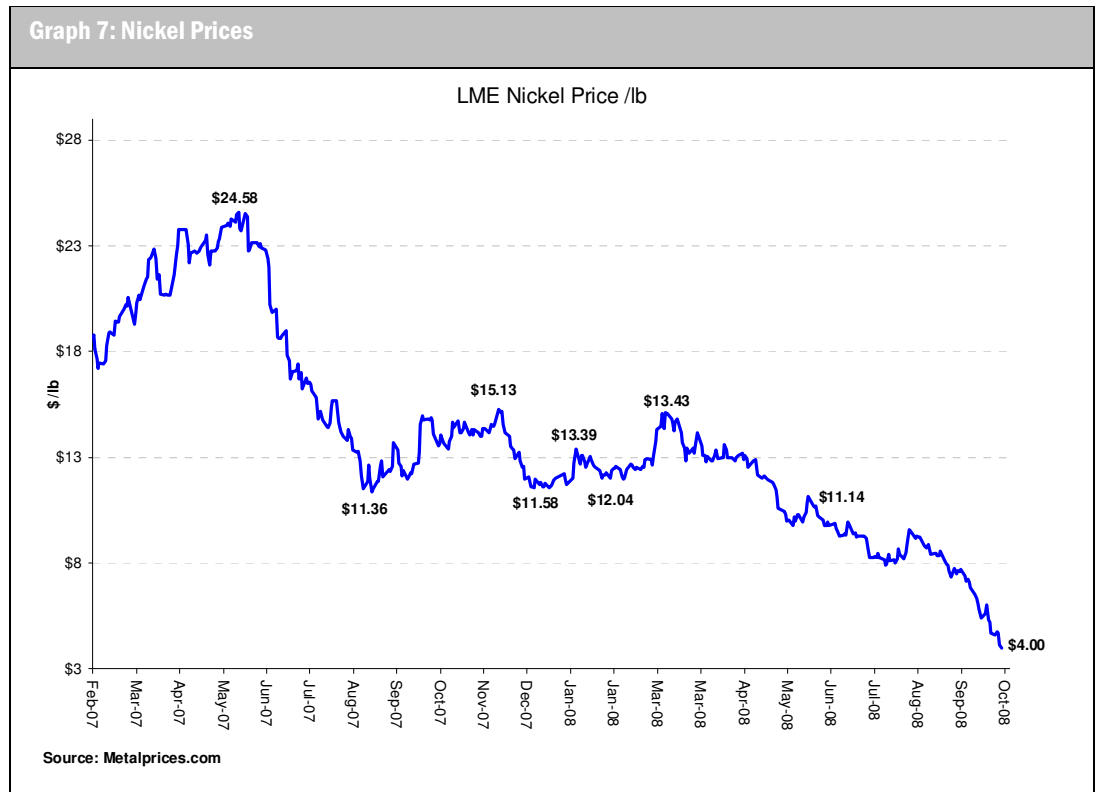
Graph 6: Stainless 304 Sheet Price





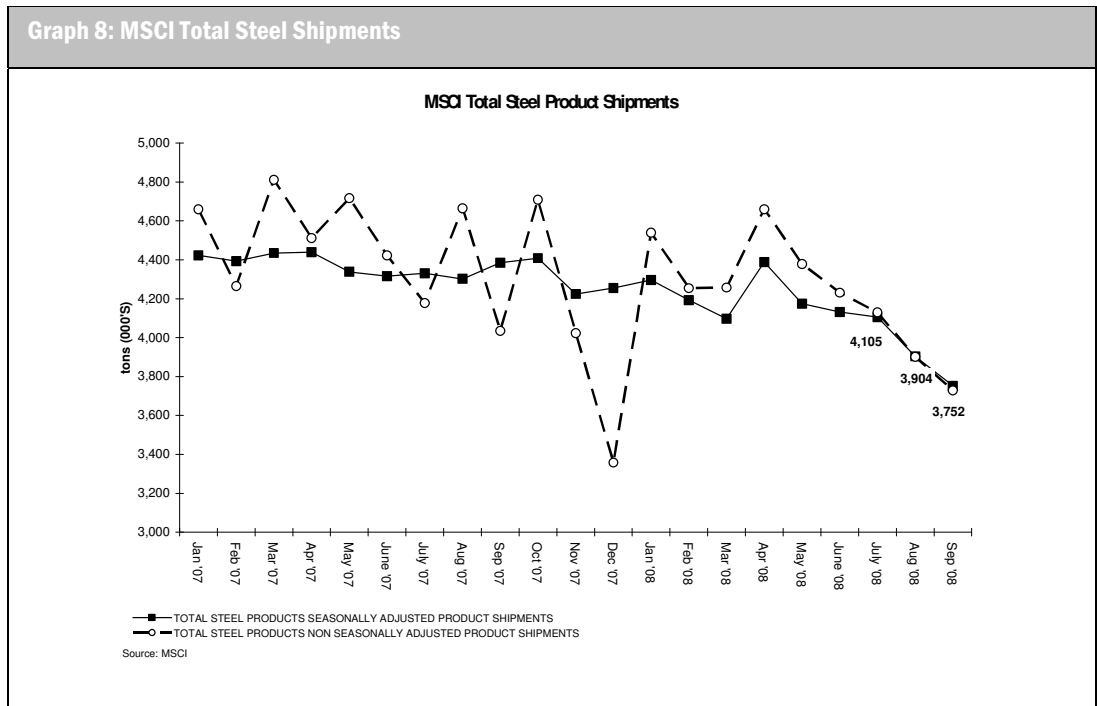
Graph 7: Nickel Prices

Nickel closed last week trading for \$4.00 /lb.



Graph 8: MSCI Total Steel Shipments

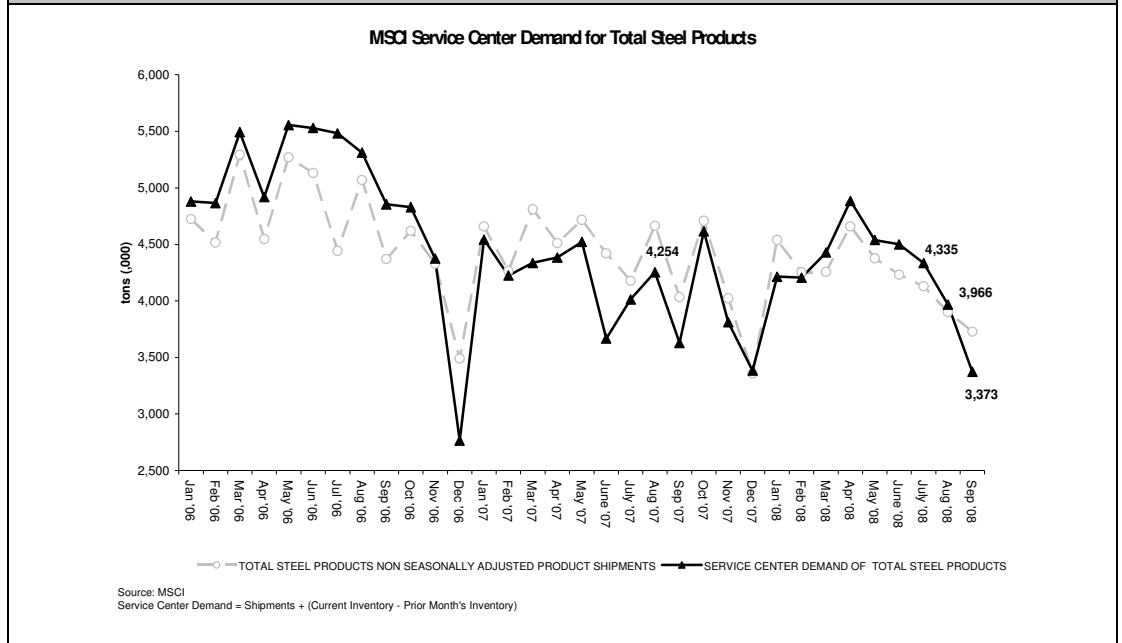
September's seasonally adjusted total steel product shipments decreased 4% sequentially and 14% year over year. Unadjusted total steel product shipments also decreased 4% over last month and were 8% below last year.





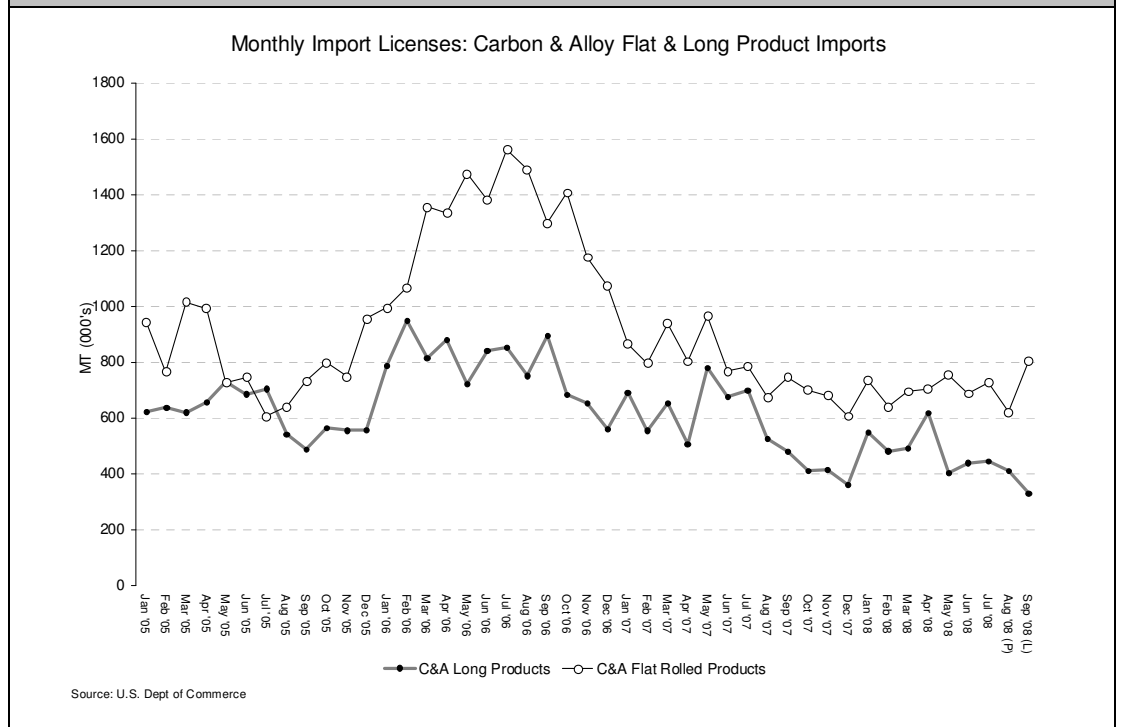
Service center demand for steel products declined 7% year over year in September.

**Graph 9: MSCI Service Center Demand for Total Steel Products**



Imports licenses for carbon and alloy flat increased 30% sequentially and long products decreased 19% in preliminary census data.

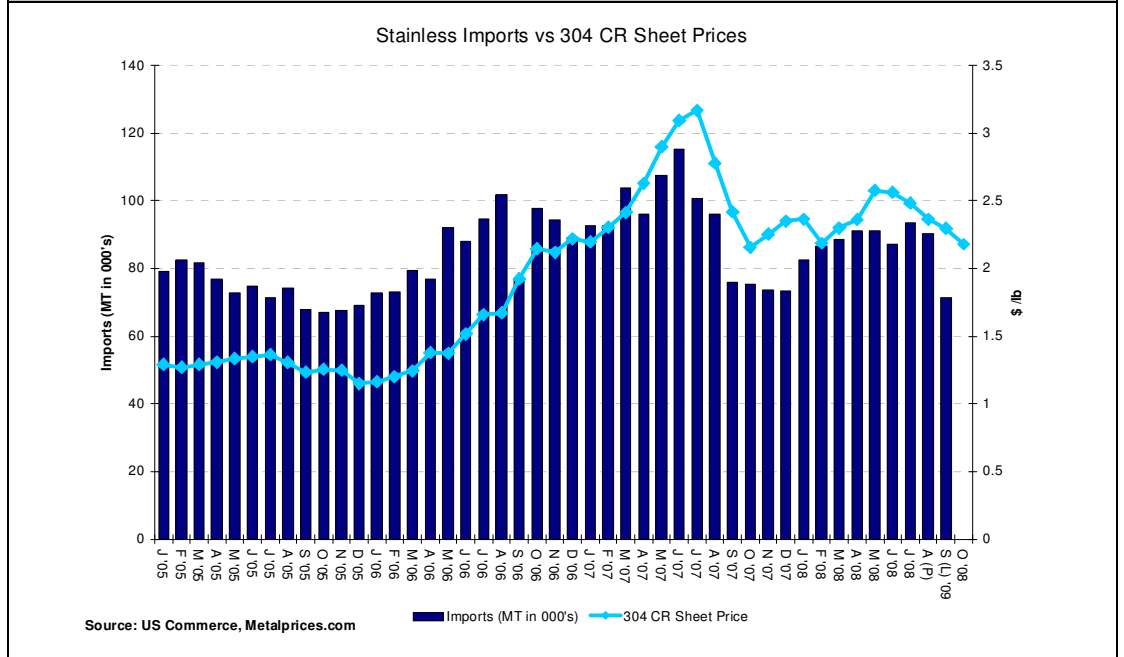
**Graph 10: Flat Product Import Licenses**





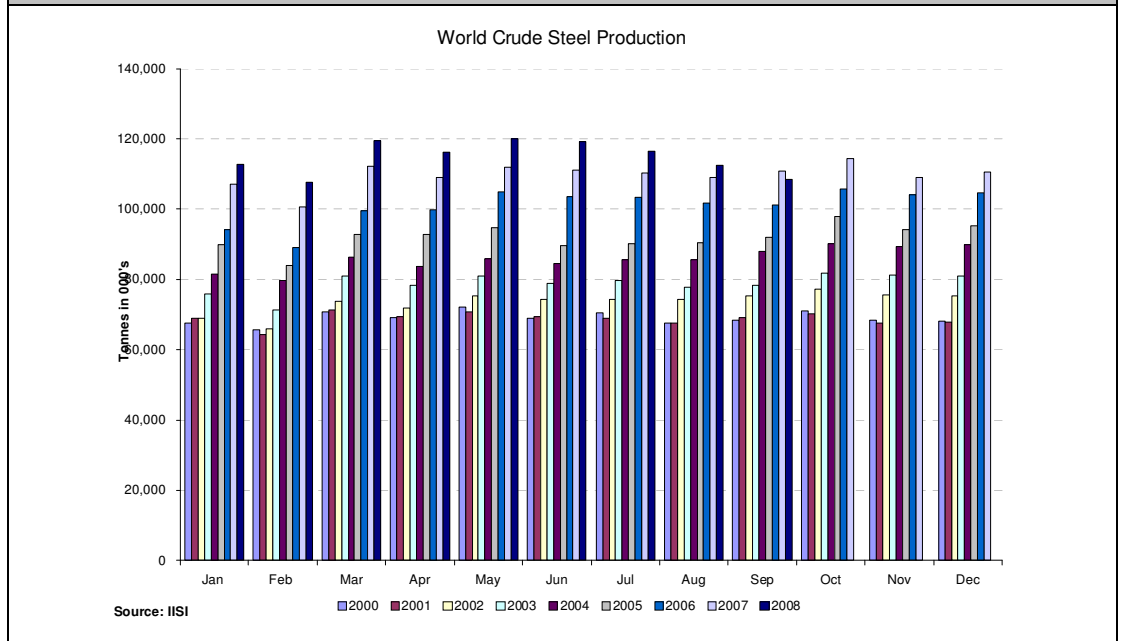
Stainless steel imports, strongly correlated with domestic prices, are likely to decline in October.

Graph 11: Stainless Import Licenses and Prices



World steel production in September is 2% lower than the similar period last year.

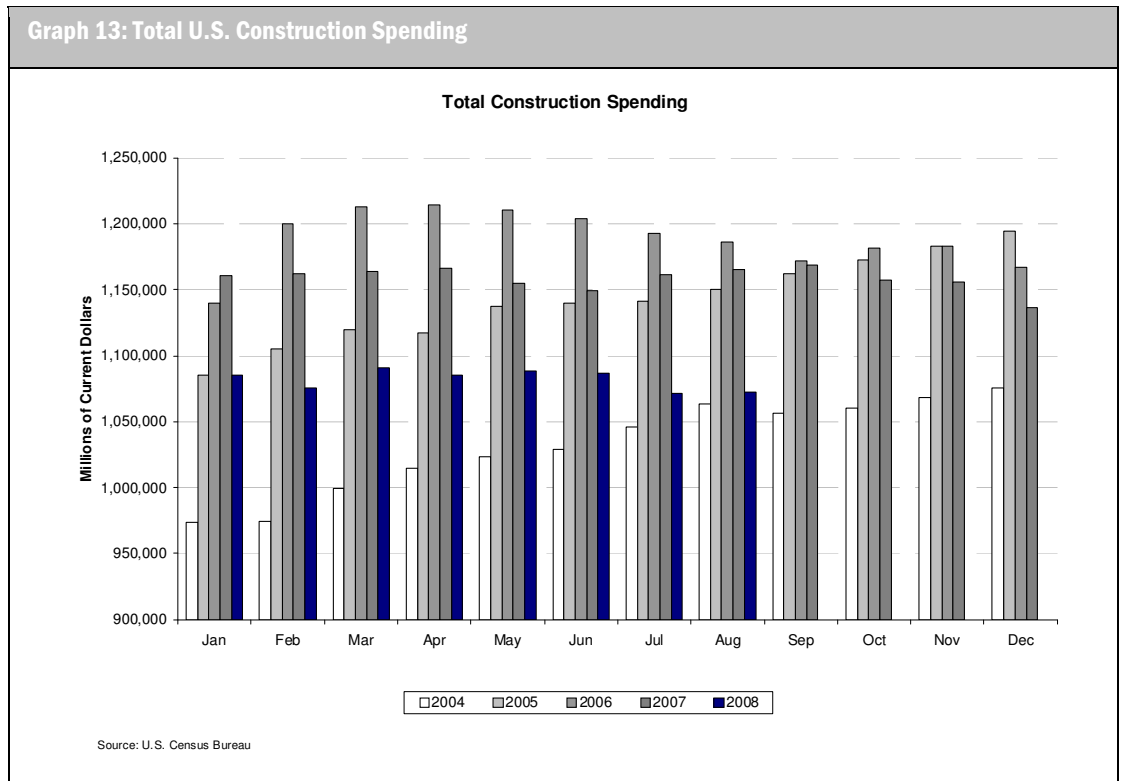
Graph 12: World Crude Steel Production





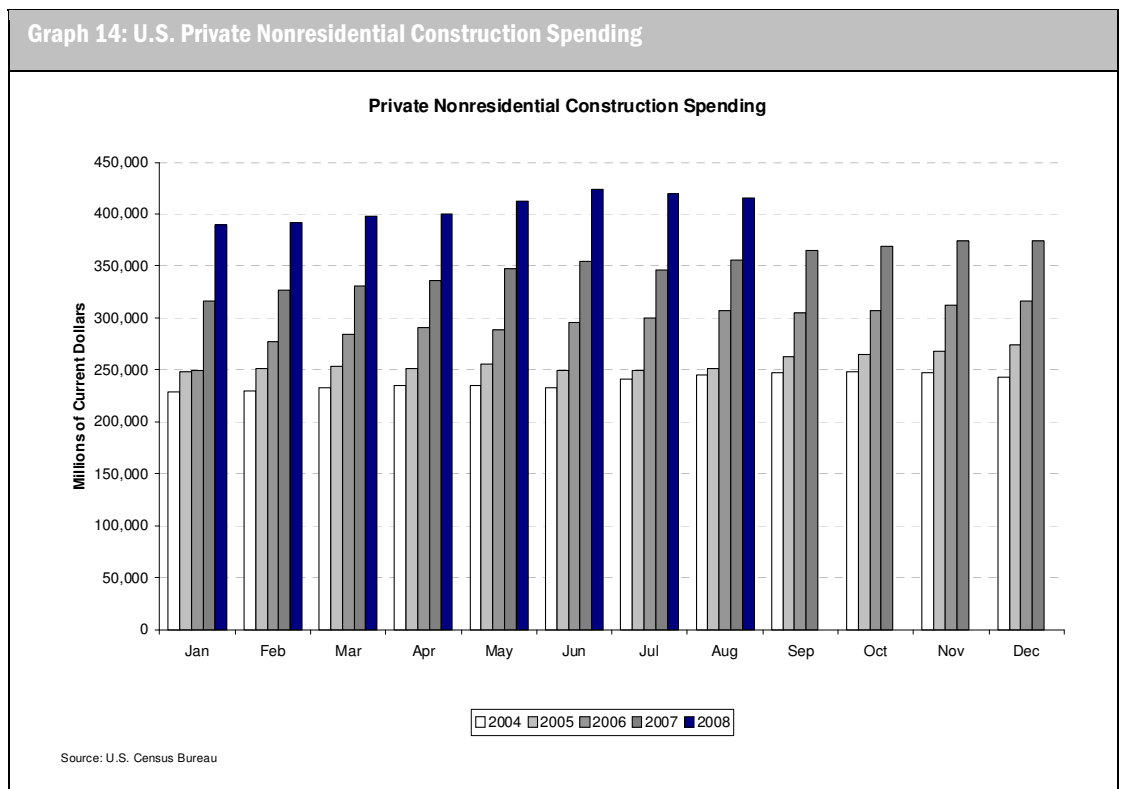
Graph 13: Total U.S. Construction Spending

Total U.S. construction spending in August was down 8% compared to the same period last year.



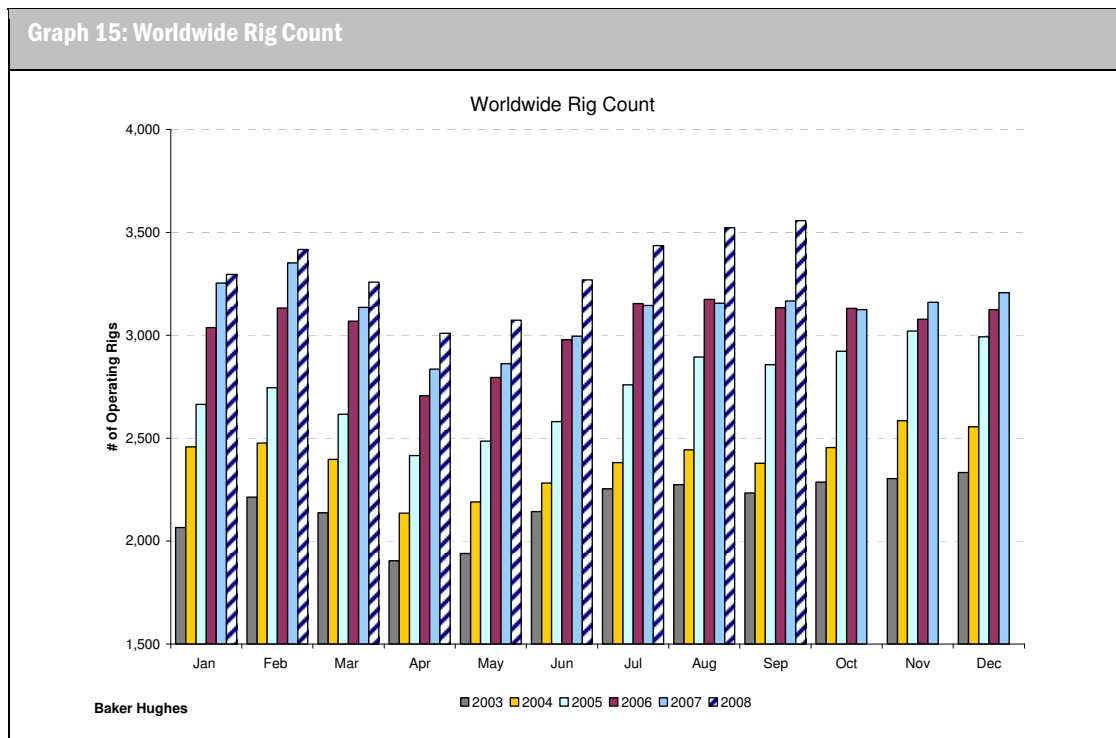
Graph 14: U.S. Private Nonresidential Construction Spending

Private U.S. nonresidential construction spending in August was up 16.9% over the prior year.

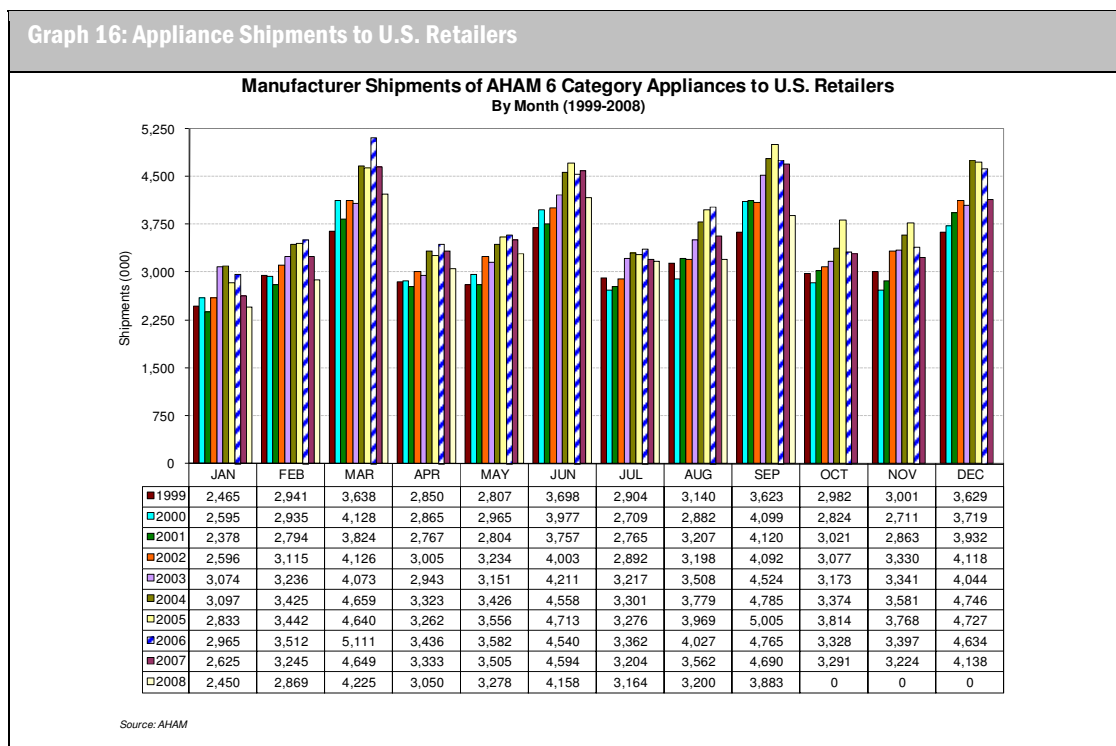




Worldwide rig counts were up 12% in September over the prior year.

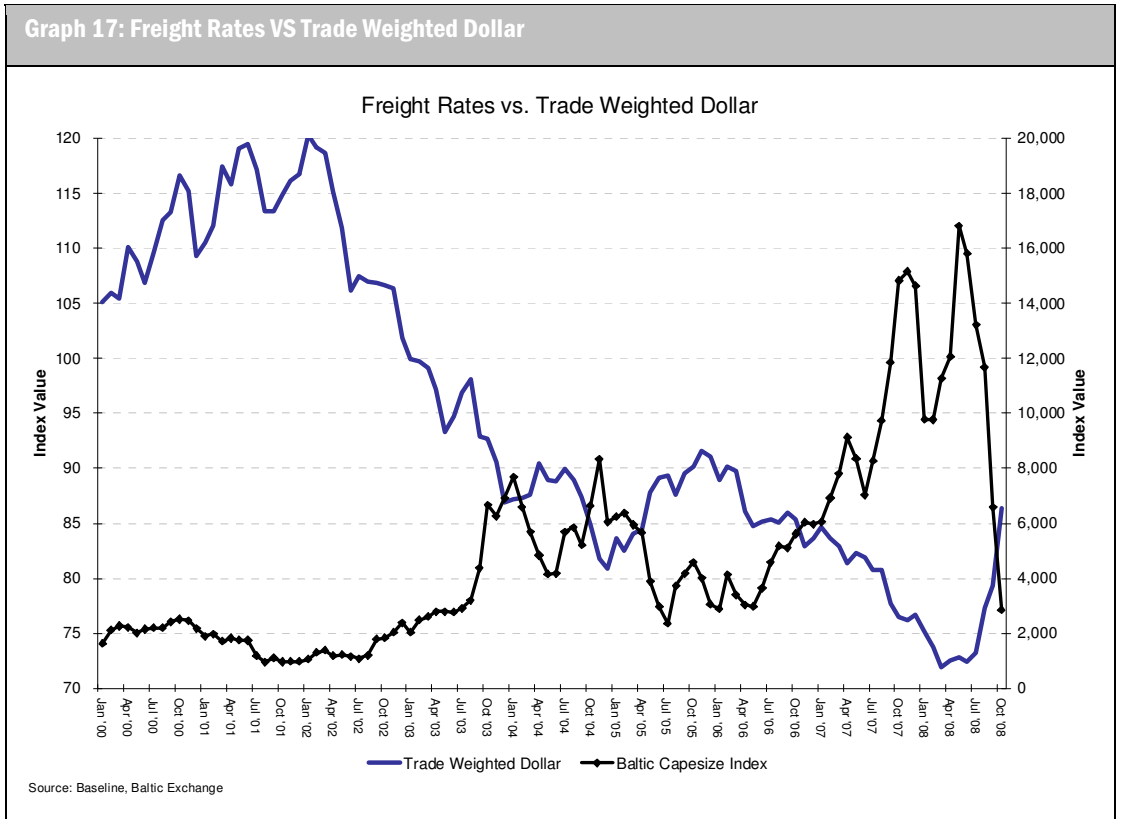


Appliance shipments to retailers in September declined 17% year over year to 3.9 million.



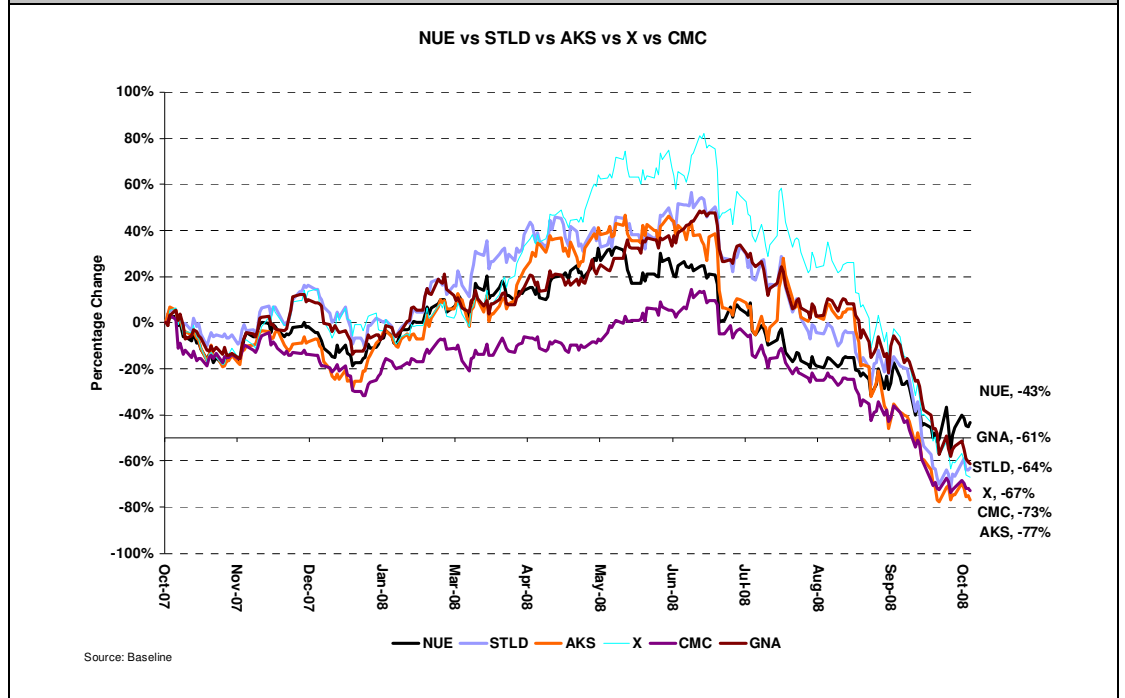


The Baltic Capesize Index is averaging 2,862 in October, a sequential decrease of 56%. The index is down 81% year over year. The trade weighted dollar index is up 9% sequentially to 86.36.

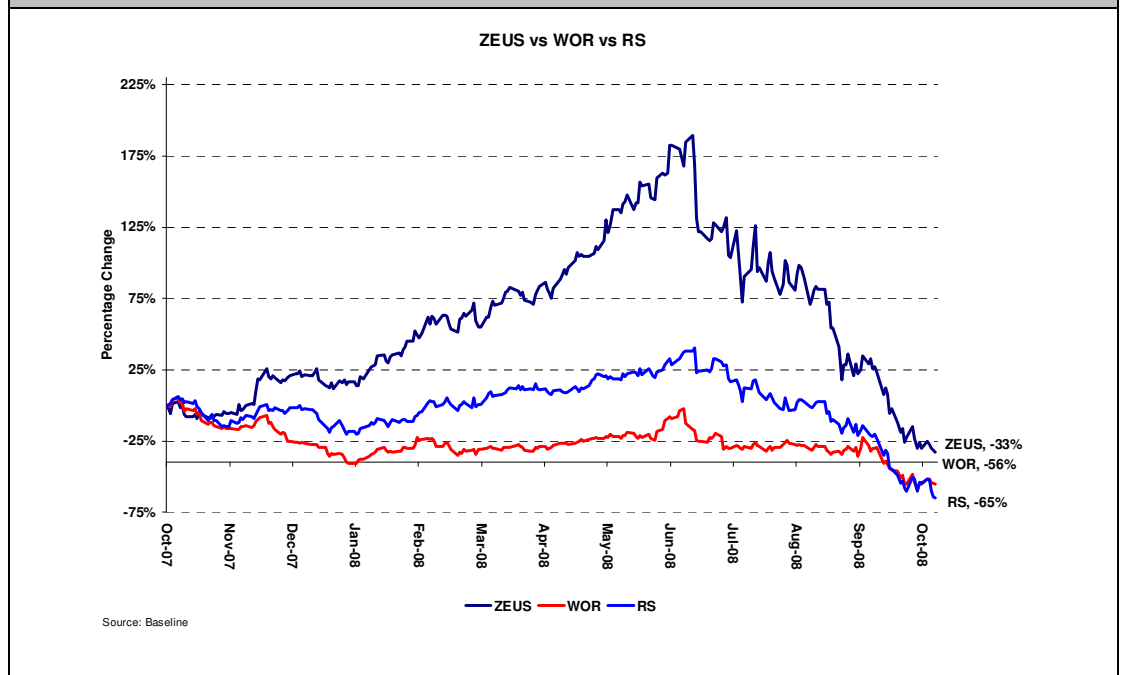




Graph 18: Steel Producers Stock Performance

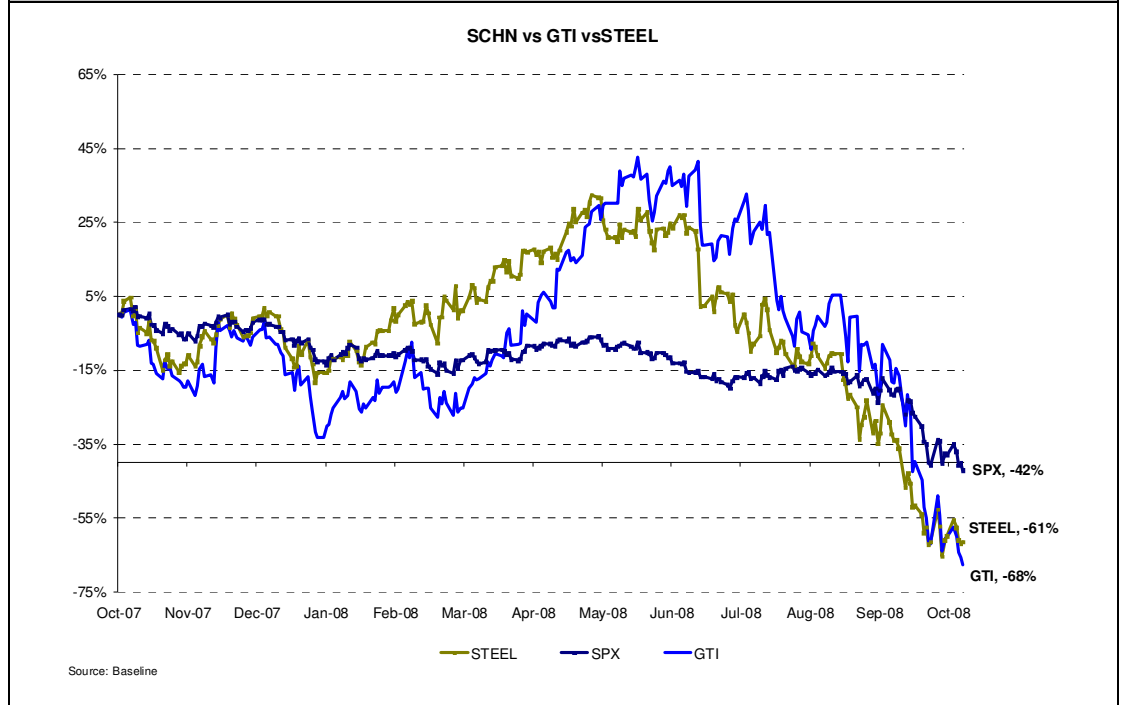


Graph 19: Steel Service Centers Stock Performance





Graph 20: Recyclers Stock Performance



Graph 21: Baseline Steel Index VS S&P 500

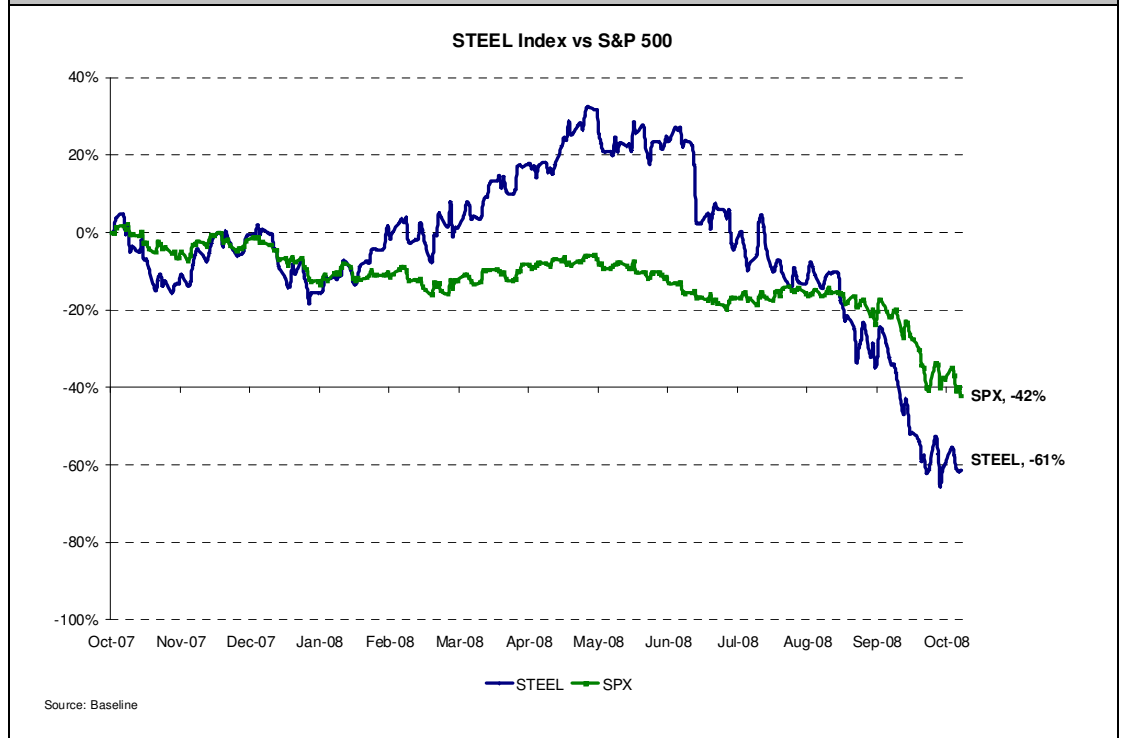




Table 1: Steel Industry Valuation Summary

Steel Industry Valuation Summary													
Classification \$ values in millions	Market Cap	Most Recent Year End				Consensus			Valuation				
		Rev. per Share	E.P.S.	EBITDA/Book Val/ Share	Ent Val/ Share	Current Quarter	Current Year	Next Year	Price/ Fwd Earnings	Price/ Sales	EV/ EBITDA	Price/ Book	
Mini-mills	4,073	54.59	2.91	7.10	14.76	22.31	0.93	3.79	3.37	3.5	0.27	3.32	0.89
Integrated Mills	6,029	85.07	4.47	11.19	24.36	29.38	2.22	7.42	6.35	2.9	0.23	2.72	0.81
<b>All Steel Producers</b>	<b>5,277</b>	<b>73.34</b>	<b>3.87</b>	<b>9.62</b>	<b>20.66</b>	<b>26.66</b>	<b>1.72</b>	<b>6.02</b>	<b>5.20</b>	<b>3.1</b>	<b>0.25</b>	<b>2.89</b>	<b>0.84</b>
Distributors	610	93.73	3.39	8.72	25.79	28.10	1.14	5.03	3.48	3.5	0.16	3.10	0.59
Recyclers	1,746	18.90	0.54	2.09	4.71	9.00	0.15	0.93	NM	3.3	0.2	4.3	0.6
Fabricators	1,736	41.74	2.90	6.60	19.65	24.09	0.72	3.04	3.10	6.7	0.47	3.57	0.96
Pipe & Tube	3,446	30.93	2.06	4.67	16.98	20.06	0.72	2.59	3.87	6.1	0.54	3.66	0.91
<b>Total Steel Industry</b>	<b>3,383</b>	<b>60.72</b>	<b>3.21</b>	<b>7.86</b>	<b>20.02</b>	<b>24.70</b>	<b>1.25</b>	<b>4.54</b>	<b>4.16</b>	<b>4.4</b>	<b>0.33</b>	<b>3.23</b>	<b>0.84</b>

Table 2: Recent Stock Performance

Recent Stock Performance of Our Steel Coverage Universe						
Company	Ticker	October 26, 2008	Week	YTD	6 months	LTM
U.S. Steel (B)	X	\$34.68	-15.9%	-71.3%	-76.7%	-67.0%
Nucor Corp (B)	NUE	\$35.01	4.3%	-40.9%	-52.3%	-43.8%
Steel Dynamics (N)	STLD	\$9.59	9.6%	-67.8%	-72.3%	-64.5%
Commercial Metals (N)	CMC	\$9.39	-5.0%	-68.1%	-68.6%	-72.7%
Gerdau Ameristeel (B)	GNA	\$5.11	-16.4%	-64.1%	-67.0%	-60.5%
A K Steel (B)	AKS	\$11.61	-8.3%	-74.9%	-81.9%	-77.5%
Reliance Steel & Aluminum (N)	RS	\$19.53	-22.5%	-64.0%	-67.3%	-65.3%
Olympic Steel (N)	ZEUS	\$17.67	-3.7%	-44.3%	-61.6%	-28.7%
Worthington Industries (N)	WOR	\$10.90	0.0%	-39.0%	-36.9%	-55.1%
Schnitzer Steel (N)	SCHN	\$22.86	-14.9%	-66.9%	-73.1%	-69.4%
Graftech (N)	GTI	\$6.21	-19.5%	-65.0%	-69.4%	-67.6%
Cleveland Cliffs (B)	CLF	\$24.56	-12.3%	-51.3%	-68.9%	-48.7%

\*(B) - BUY, (N)- Neutral, (S) - Sell, (NR)- Not Rated

Table 3: Steel Peer Group Valuations

Steel Peer Group Valuation																		
Company Name	Rating	Research Ticker	Market Stats			Rev. per Share	Most Recent Year End			Consensus			Valuation					
			Current Price	52 Week High	52 Week Low		Market Cap	E.P.S.	EBITDA/Share	Book Value/Share	Ent Val/Share	Current Quarter	Current Year	Next Year	Price/ Earnings	Price/ Sales	EV/ EBITDA	Price/ Book
<b>Integrated Producers</b>																		
Arcelor Mittal Adr	-	MT	21.96	105	20	20,529	129.61	7.41	19.06	45.37	44.06	4.01	12.55	10.54	1.7	0.2	2.3	0.5
United States Steel	BUY	X	34.68	196	30	4,074	177.29	8.75	20.97	54.51	58.74	7.08	19.55	16.56	1.8	0.2	2.8	0.6
Ak Steel Holdg	BUY	AKS	11.61	73	9	1,303	70.21	3.50	9.91	11.61	13.60	0.78	4.66	3.86	2.5	0.2	1.4	1.0
<b>Mini-mills</b>																		
Nucor	BUY	NUJE	35.01	84	26	11,083	75.52	4.95	12.23	25.00	40.07	1.66	7.32	6.24	4.8	0.5	3.3	1.4
Steel Dynamics	NEU	STLD	9.59	41	7	1,923	41.50	2.08	6.56	10.03	21.81	0.45	3.31	3.01	2.9	0.2	3.3	1.0
Commercial Metals	NEU	CMC	9.39	40	8	1,075	83.52	2.91	6.17	14.36	15.89	0.94	2.39	2.36	3.9	0.1	2.6	0.7
Gerdau Ameristeel	BUY	GNA	5.11	20	5	2,212	17.81	1.68	3.43	9.63	11.48	0.65	2.13	1.87	2.4	0.3	3.3	0.5
<b>Pipe &amp; Tube Producers</b>																		
Friedman Industries	-	FRD	4.80	10	5	33	27.63	0.67	1.75	7.12	3.01	-	0.67	-	NM	0.2	1.7	0.7
Northwest Pipe	-	NWPX	25.02	65	25	229	46.65	2.25	6.30	29.71	37.64	0.70	3.23	3.32	7.7	0.5	6.0	0.8
Tenaris Adr	-	TS	17.07	75	16	10,076	18.51	3.26	5.95	14.10	19.52	0.83	3.86	4.41	4.4	0.9	3.3	1.2
<b>Steel Service Center</b>																		
Olympic Steel	NEU	ZEUS	17.67	78	16	192	104.08	2.35	8.76	28.46	20.24	1.65	6.25	3.55	2.8	0.2	2.3	0.6
Castle (A.M.)	-	CAS	9.07	34	9	207	64.03	2.45	4.51	17.97	14.03	0.44	1.81	1.50	5.0	0.1	3.1	0.5
Reliance Steel/Almu	NEU	RS	19.53	78	17	1,430	113.09	5.36	12.90	30.93	50.02	1.34	7.03	5.39	2.8	0.2	3.9	0.6
<b>Steel Fabricators</b>																		
Gibraltar Industries	-	ROCK	11.22	25	10	336	45.29	1.13	4.40	19.80	24.97	0.49	1.58	1.49	7.1	0.2	5.7	0.6
Harsco	-	HSC	18.55	67	18	1,564	47.32	3.02	9.27	20.92	31.18	0.94	3.52	3.67	5.3	0.4	3.4	0.9
Insteel Industries	-	IIN	8.21	20	7	144	20.24	2.48	4.35	9.32	6.69	0.24	2.48	1.11	3.3	0.4	1.5	0.9
Precision Castparts	-	PCP	52.29	155	48	7,287	51.25	6.93	12.49	35.02	51.65	1.77	6.93	7.71	7.5	1.0	4.1	1.5
Worthington Indus	NEU	WOR	10.90	26	10	859	40.90	1.45	4.02	12.48	15.60	0.42	1.45	2.12	7.5	0.3	3.9	0.9
Foster (L.B.)	-	FSTR	21.64	60	20	230	45.46	2.36	5.06	20.37	14.42	0.47	2.25	2.52	9.6	0.5	2.8	1.1
<b>Graphite Electrodes</b>																		
Grattech Int'L	NEU	GTL	6.21	28	6	742	9.46	1.34	2.95	4.25	7.59	0.45	1.96	2.55	3.2	0.7	2.6	1.5
<b>Metal Recyclers</b>																		
Schnitzer Steel Ind	NEU	SCHN	22.86	119	22	675	104.16	4.32	10.48	30.94	31.05	2.53	6.76	4.94	3.4	0.2	3.0	0.7
Metalico	-	MEA	3.04	19	3	110	18.90	0.54	2.09	4.71	9.00	0.15	0.93	1.00	3.3	0.2	4.3	0.6
<b>TOTALS</b>			<b>16.89</b>	<b>61</b>	<b>15</b>	<b>3383</b>	<b>60.72</b>	<b>3.21</b>	<b>7.86</b>	<b>20.02</b>	<b>24.70</b>	<b>1.25</b>	<b>4.54</b>	<b>4.16</b>	<b>4.4</b>	<b>0.3</b>	<b>3.2</b>	<b>0.8</b>



**B. Richard, CFA**  
216-525-8430

**L. Folta**  
216-525-8408

**Analyst Certification:**

The research Analyst(s) who prepared the research report hereby certifies that the views expressed in the research report accurately reflect the analyst(s) personal views about the subject companies and their securities. The Research Analyst(s) also certifies that the Analyst(s) have not been, are not, and will not be receiving direct or indirect compensation for expressing the specific recommendation(s) or view(s) in this report.

**Ratings Distributions for Longbow Research:**

<b>Rating Category</b>	<b>Count</b>	<b>Percent</b>
Buy	56	34.8%
Neutral	103	64.0%
Sell	2	1.2%

**RATING SYSTEM:** “Buy” means that Longbow Securities expects total return to exceed 10% over a twelve-month period. “Neutral” means that Longbow Securities expects total return to be within a range of plus or minus 10% over a twelve-month period. “Sell” means that Longbow Securities expects total return to be negative by greater than 10% over a twelve-month period.

**DESCRIPTION:** Longbow Securities is a third-party research provider established in 2003 and headquartered at 6000 Lombardo Center, Suite 500, Independence, Ohio 44131 USA. The company provides research services to institutional investors, investment advisers, and professional money managers.

**DISCLAIMER:** The information, opinions, estimates, and projections contained in this report were prepared by Longbow Securities and constitute the current judgment of Longbow Securities as of the date of this report. Additional information may be available from Longbow Securities upon request. The information contained herein is believed to be reliable and has been obtained from sources believed to be reliable, but Longbow Securities makes no representation or warranty, either expressed or implied, as to the accuracy, completeness, or reliability of such information. Longbow Securities does not undertake, and has no duty, to advise you as to any information that comes to its attention after the date of this report or any changes in its opinion, estimates, or projections. Prices and availability of securities are also subject to change without notice. Longbow Securities does not make a market in any securities, nor does it hold a principal position in any security. However, any officer, director, or stockholder of Longbow Securities or any member of their families may have a position in and may from time to time purchase or sell any of the securities mentioned or any related securities. Additional information concerning Longbow Securities is contained in its Disclosure Brochure, which contains information required by Part II of Form ADV and is available at [www.longbowresearch.com](http://www.longbowresearch.com), or by calling (216) 986-0700. By accepting this report, the reader acknowledges that the report does not purport to meet the objectives or needs of specific investors, and, accordingly, constitutes only “impersonal advisory services” as that term is defined in Rule 204-3 under the Investment Advisers Act of 1940 and that any advice in this report is furnished solely through uniform publications distributed to subscribers thereto within the meaning of Section 2(a)(20)(i) of the Investment Company Act of 1940.