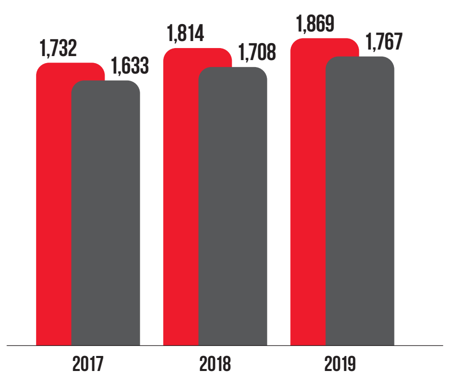
NAVIGATING A VOLATILE MARKET

In 2019, pressure on steel prices built up during the year, as global steel production continued to rise despite weak consumption in some key regions and a worsening economic outlook due to heightened trade tensions. Meanwhile, iron ore prices remained robust amid greater demand from China and significant supply disruptions in the world's main iron ore exporting countries.

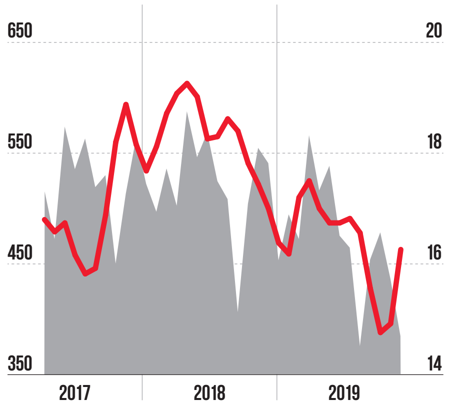
Global steel industry



Crude steel production, MT
Finished steel consumption, MT

Source: World Steel Association

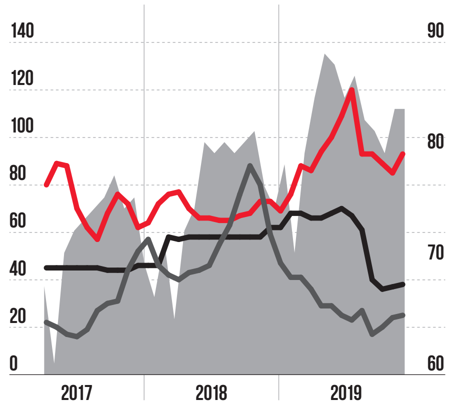
Steel price



Steel production in Europe, MT (RHS)
HRC, FOB Black Sea, US$/tonne (LHS)

Source: World Steel Association, Metal Expert

Iron ore price and premiums



Steel production in China, MT (RHS)
62% Fe iron ore fines, CFR China, US$/tonne (LHS)
Atlantic basin pellet premium, US$/tonne (LHS)
Pellet premium in China, US$/tonne (LHS)

Source: Bloomberg, Platts

Hard coking coal price

Daily spot index, FOB Australia, US$/tonne

Source: Platts

GLOBAL STEEL MARKET

In 2019, the global steel market was shaped by weaker demand in certain key regions, intensified trade tensions worldwide, stronger iron ore prices and heightened expectations of global recession.

Global steel production rose by 3.0% year-on-year to 1,869 tonnes and apparent consumption of finished steel products climbed by 3.4% to 1,767 million tonnes. Both indicators were primarily driven by China.

During the year, Chinese steel output and apparent consumption grew by 8.3% and 8.5% year-on-year to 996 million tonnes and 907 million tonnes, respectively, both reaching a new record, mainly due to fiscal stimulus and credit easing measures by the government. Consequently, China's share in global production and consumption reached 53% and 51%, respectively, compared with 50% and 45% four years ago.

Meanwhile, steel supply and demand trends in other regions were multi-directional. Consumption was down in several of Metinvest's most important steel markets, dropping by 5.6% year-on-year in the EU, where Germany saw a decline of 12.0% over the period, mainly driven by weak industrial production and the impact on demand from a sluggish automotive sector. Turkey saw the steepest demand decline of the world's top-10 steel markets, falling by 15.4% year-on-year, amid sluggish domestic economic growth in 2019. Meanwhile, demand in Russia grew by 5.0% year-on-year amid higher machinery production.

Production rose in the Middle East, where Iran reported a 4.5% rise in output after launching new capacity and higher exports. In addition to China, other countries in Asia saw growth, as well, with production in Vietnam surging by 29.7% due to increased internal consumption and the introduction of trade barriers in the region against Chinese manufacturers. At the same time, output fell in such regions as Europe, North America (mainly Mexico) and South America (primarily Brazil).

Trade disputes persisted as major global players continued to protect their markets and local producers. In addition to the 25% steel tariffs that the US introduced in 2018 and the anti-dumping tariffs that the EU introduced in 2017 covering some 60% of hot-rolled coil (HRC) imports to the region, the EU tightened the tariff rate quotas that it introduced on imports of several steel products in 2018 and effectively extended them until July 2021.

Since peaking in spring 2018, global steel prices have been under pressure from the factors described above. In 2019, the HRC FOB Black Sea benchmark retreated by 16.5% year-on-year to an average of US$468 per tonne. Its sharpest drop was in the fourth quarter, which saw a 10.9% quarter-on-quarter decline to an average of US$415 per tonne and a low of US$388 per tonne in October.

Sluggish demand in Europe amid high prices for raw materials pushed European steel producers to reduce output, which fell by as much as 5.9% year-on-year in 2019. Together with the announcement of economic stimulus measures in major economies, this was sufficient to reverse the benchmark steel price trend in November 2019.

GLOBAL RAW MATERIALS MARKET

On the raw materials market, different forces were at work for iron ore and coking coal.

China is the world's largest consumer and importer of iron ore. While its iron ore producers are focused on the domestic market, their quality and capacity are insufficient to meet the country's needs. Consequently, China accounts for some 65% of global imports, according to the World Steel Association (WSA), which is served primarily by the "Big Four" multinational iron ore producers. Australia and Brazil are the two largest iron ore exporting countries. While they accounted for around 70% of global iron ore trade in 2019, according to Bloomberg and WSA data, and accounted for around 80% of global seaborne shipments in 2019, according to Metinvest's estimates, they also saw operational disruptions during the year. Brazil was hit in January 2019 by the collapse of a tailing dam that caused production stoppages at one of the world's largest iron ore producers. In Australia, cyclone Veronica interrupted shipments during the first half of the year. Combined exports from both countries totalled 1,175 million tonnes, down 4.6% year-on-year. On the demand side, Chinese steel output reached a new record during the reporting period.

As a result, iron ore experienced a price rally in the first half of 2019. While there was a moderate contraction in the second half, prices remained at elevated levels. The 62% Fe iron ore fines CFR China benchmark averaged US$94 per tonne in 2019, compared with US$70 per tonne in 2018.

In this environment, European steelmakers sought to cut costs as much as possible. They exhibited a preference for lower-quality iron ore concentrate instead of pellets, which traditional suppliers including Metinvest had redirected to other regions, including China. This caused pellet premiums in both Europe and China to fall beginning in July 2019. Overall, in the second half of the year, the European and Chinese pellet premiums fell by 31.3% and 32.8, respectively, to US$46 per tonne and US$23 per tonne compared with the first half of 2019.

The global coking coal market has seen supply side volatility in recent years, amid such factors as bad weather constraining output in Australia, increasing exports from Mongolia and the imposition of import restrictions in China. In 2019, the spot hard coking coal FOB Australia benchmark decreased by 14% year-on-year to US$177 per tonne. Despite a flat trend in the first half, prices collapsed in the second half, driven by demand factors, such as production cutbacks by large steelmakers late in the year, as well as restrictions on coal imports instituted at Chinese ports. As a result, the price fell by 26.5% half-on-half to an average of US$150 per tonne in July-December 2019.

OUTLOOK FOR 2020

The outlook for 2020 remains profoundly uncertain. While the steel price recovery continued in early 2020 as the US and China signed the first phase of a new trade deal in January, the trend reversed in March. The outbreak of the coronavirus pandemic led to lockdowns in many countries, broke international supply chains and shut down multiple economic sectors, triggering a global recession. Countless industries have been forced to face simultaneous supply and demand shocks.

Governments worldwide have responded with unprecedented fiscal and monetary stimulus, including by EU countries, as well as the UK, the US and China.

However, many important questions have yet to be answered, including but not limited to: how quickly the world will return to anything resembling normal life; how deep the economic decline will prove to be; how strongly it will affect the global steel, iron ore and coking coal markets, in terms of both the supply/demand balance and the subsequent impact on prices; and how fast global economies will recover.