

# Iron ore price fuelled by Chinese import norm

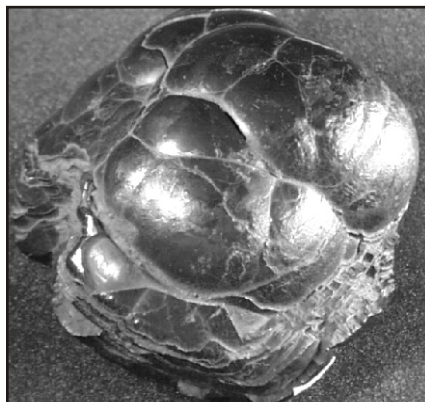
According to Visa Steel chairman Vishambar Saran China would have been spared the pains of galloping rises in iron ore prices had the country, following in Japan's footsteps, acquired rights to mines abroad before pressing ahead with its steel industry's capacity expansion. In India, the nimble Japanese have not only made a resounding success of their promoted Sesa Goa, this country's largest private sector exporter of iron ore, but they have also remained significant buyers of the mineral from publicly owned NMDC and Kudremukh. China has gone terribly wrong in its planning for import of ore for which it is now paying very high prices. India sadly has also been a late starter in offshore coking coal deposits acquisition drive.

Global mining giants like CVRD of Brazil and Anglo-Australian groups BHP Billiton and Rio Tinto will attribute their booming profits to spikes in all minerals prices made possible by demand surge in Asia, particularly China. The next demand burst for steel-oriented minerals will be in India as it chases a metal production of 110 million tonne by 2019-20 against 40 million tonne last year.

## Steel production needs coking coal supply

Steel production of 110 million tonne will need supply of 70 million tonne of coking coal. But neither Indian

reserves of prime coking coal of 4.6 million tonne are large, nor their quality necessarily makes the grade for steel making. We are not mining more than 10 million tonne of steel grade low ash coking coal. But what is mined here becomes usable only after blending with high grades of imported coal. Local supply shortages are leading Indian steel makers to import 15 million tonne of coal and another 2.5 million tonne of metcoke annually.



The search for coking coal security has now led the government to "encourage joint ventures and equity participation by steel and coal companies" in foreign coal mines. Though it has not come a day too soon, SAIL chairman V S Jain's overtures to Vizag Steel for joint bidding of offshore coal deposits makes good sense.

In the meantime, SAIL is funding new mines development by the government owned Bharat Coking

Coal. Recent easing of coal prices has given some relief to steel makers. But where is the guarantee that last year's crisis resulting from 119 per cent coal price rise will not visit them in the future. Full or part ownership of coal mines abroad can only buy them peace of mind. China does not have peace at the moment over the 19 per cent iron ore price hike secured by the world's three leading mining groups for 2006-07. The current season was the second occasion in the last 25 years when ore price negotiations saw their denouement as late as the final week of May. Such negotiations generally start in February and agreement is reached by April 1.

## China queered by European producers

China's strategy this time was to wear out ore producers through a holding on operation. But the pitch for China was queered first by European producers such as Arcelor and ThyssenKrupp and then by Nippon Steel, which somewhat tamely conceded ore price revision. Till the time China Steel Corporation finally agreed to the 19 per cent price rise that CVRD, the world's largest producer and exporter of ore, demanded, China used a mix of economic diplomacy and some astute reasoning to buck what the mining groups managed to extract from European and Japanese steel makers. The recent round of ore price

revision has to be read with last year's record 71.5 per cent hike to understand the concern of Chinese steel makers. The Chinese press is full of stories saying anything that the country buys (read iron ore) is expensive. But what it sells goes cheap (read inadequate returns on steel products). China, which is targeting crude steel production of 384 million tonne in the current year, up from 349 million tonne in 2005, will need to import 10 per cent more ore at 301 million tonne.

It will not be wrong in believing that mining groups are taking unreasonable advantage of rapid rises in Chinese steel production causing phenomenal import demand for ore. Last year, the world production of iron ore at 1,250 million tonne was a fourth time in a row record. So, also the world exports of the mineral at over 700 million tonne. No doubt, all this happened largely because of the unquenchable Chinese thirst for the mineral.



### No exclusive price for Europe

In negotiations that lasted over seven months, China made the point that 2006-07 ore prices should not be fixed exclusively on the basis of European steel prices, which are

amongst the highest in the world, but allowance also made for comparatively low Asian steel prices. This is buttressed by the fact that while by April end, the global composite steel price index at 149 was inching towards last year's peak of 153.4. For China it was down 23.6 per cent at 105.67 from the March peak of 138.33. China, therefore, is not to be blamed if it had reservations in accepting what European steel makers are to pay for ore as the benchmark price. There was nothing that China did not do to



encourage domestic steel makers not to concede what the mining groups were demanding. First, liberal ore imports of nearly 81 million tonne in the first quarter of 2006, a 27.7 per cent jump over the same period last year, created an inventory of over 60 million tonne allaying fears of any "near-term shortages".

In fact, even at this point 18 major Chinese ports are awaiting evacuation of 40 million tonne of imported ore. Poor quality of domestic ore has made China over-dependent on foreign stuff. The country is trying to build

future defence against the "marauding tactics" of leading ore producers by developing new supply sources. For example, China has become the biggest buyer of the mineral from India. Chinese industry officials believe that the "very aggressive pricing of ore" is evidence that the next few years could lead to "hard landing" for the steel industry and in the process pull down mining groups from their cozy perches. Have ore suppliers misread the "China steel factor" as many have come to suspect? Is there

any truth in Chinese complaints that mining majors, enjoying super profits and pampering shareholders in every possible way, had not conducted negotiations on "principles of equality and mutual benefit?"

### China's notice

China has served notice that whatever happened in the course of protracted negotiations "will not be helpful in building long-term and stable cooperative relations between suppliers and buyers of iron ore." Mining giants must take note that this year China will cut 43 million tonne of pig iron production, equivalent to 60 million tonne of ore use. The country has also decided to speed up the steel industry restructuring involving phasing out of unviable capacity and creating four to five very large groups. All this will add muscle to Chinese negotiators when they return to the table for fixing next season's ore prices.

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