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CANADA: THE STEEL MARKET IN 2000 AND THE OUTLOOK FOR 2001

Overview:

In 2000, real GDP grew by 4.7% compared to 4.32% in 1999 and 3.01% in 1998. In the fourth quarter of 2000, economic growth fell to 2.6% from 4.5% in the third quarter. The average private sector forecast is calling for real GDP growth of 2.9% in 2001 and 3.6% in 2002. Recently though, one bank has revised its real GDP target for 2001 down to 2.1%. The Consumer Price Index (CPI) rose 2.7% in 2000 after rising 1.7% in 1999 and 0.9% in 1998. Private sector forecasts expect the CPI to rise by 2.4% in 2001 and 2.5% in 2002.

The unemployment rate for 2000 was 6.8%, down from 7.6% in 1999 and 8.3% in 1998. Private sector forecasters expect that the unemployment rate should average 6.9% in 2001 and 6.6% in 2002.

In December 2000, the prime rate charged by banks on loans was 7.50% compared to 6.50% a year earlier and 6.75% in December 1998. For all of 2000, the prime rate averaged 7.27% compared to 6.44% in 1999 and 6.60% in 1998. Private sector forecasts anticipate the prime rate to average 7.50% in 2001 and 7.50% in 2002. The average value of the Canadian dollar, expressed in U.S. funds, was \$0.6733 in 2000 up from \$0.673 in 1999 but below the 1998 rate of \$0.674. Private sector forecasts expect the exchange rate to decline, averaging about \$0.669 in 2001 before rising to \$0.680 in 2002.

Employment:

Employment, hourly and salaried, at primary iron and steel producers was 34,276 in 2000, down 0.7% from 1999 levels when 34,517 were employed in the industry. Employment in 1998 - at 34,443 - was basically unchanged from the 1997 level. Employment in the pipe and tube sector of the steel industry was 6,512 in 2000, up from 6,095 in 1999 and 5,733 in 1998. Therefore, employment in these two sectors of the industry was 40,788 in 2000, up from 40,612 in 1999 and 40,176 in 1998.

For 2001, employment totals for primary iron and steel producers should remain at about 34,500 people. Operating levels in the industry, while good, have declined from the high levels achieved in 1999 or earlier in 2000. Employment in the pipe and tube sector is expected to remain at current levels. Major pipeline projects underway are increasing demand for tubular goods while current high prices for oil and gas are stimulating drilling activity. Therefore, industry employment in 2001 is anticipated to be about 40,700.

Supply:

For 2000, crude steel production was 16,496,339 tonnes, up from 16,136,095 tonnes in 1999 and 15,832,839 tonnes in 1998. Indeed, the total for 2000 is the highest on record.

In 2000, continuously cast steel amounted to 16,223,360 tonnes or 98.4% of crude steel production. In 1999 and 1998, continuously cast steel amounted to 98.2% and 98.5% (respectively) of crude steel production.

The percentage of continuously cast steel is not expected to change since, with the exception of castings, all steel production in Canada is now continuously cast.

Import volumes increased in 2000 leading to strong growth in apparent steel consumption (ASC). In 2000, total import volumes increased 33.2% over 1999 levels while ASC was up 9.1%. As a result, import penetration figures increased to 44.4% in 2000 from 37.5% in 1999. Import penetration figures for 2000 were the highest ever recorded, exceeding the previous peak of 41.9% in 1998. In fact since 1989, when import penetration levels have been increasingly steadily from 18.6%, there have been two major step level increases. In 1990, import penetration levels increased to 24.5% (from 18.6% the previous year) and in 1997 they increased to 37.0% (from 27.9% the year before). In fact, import volumes in 2000 (8.336 million tonnes) were at record levels. In 1999 imports amounted to 6.256 million tonnes, in 1998 7.441 million tonnes and in 1997 6.343 million tonnes. By contrast, in 1995 Canadian steel imports totalled 5.189 million tonnes and in 1992 those imports totalled just 2.359 million tonnes. Therefore, since 1992, Canadian steel imports have risen by 253%.

In 2000, import volumes increased from Eastern Europe and the CIS by 165.2%, Russia (56.4%), the E.U.(15) (20.2%), Central and South America (45.6%), Asia (57.8%) (with increases from Japan (15.2%), Korea (85.6%), China (561.7%), India (83.4%), Taiwan (48.1%), Thailand (176.7%), the Philippines (76.1%)), South Africa (8.9%), New Zealand (69.0%), Turkey (43.4%) and Egypt (185.3%). Imports from the U.S. also increased by 16.4%. Decreases in import volumes occurred from Malaysia (6.9%), Indonesia (57.1%), Australia (72.4%) and Cuba (100%). While total import volumes increased, this was also reflected in imports of specific steel products. Hot rolled sheet imports were 2.222 million tonnes in 2000, up 68.9% over 1999 levels; cold rolled sheet imports were .758 million tonnes, up 25.5%; stainless steel round bar imports were 7,678 tonnes up 116.1% and concrete rebar imports were .449 million tonnes, up 64.7%. Canadian imports of hot rolled and high strength low alloy plate imports were .316 million tonnes in 2000, down 2.1% and imports of corrosion resistant sheet products were .451 million tonnes, down 13.8%.

The 2000 import figure has increased, not surprising given the continuing strong demand for steel for much of the year. In fact, demand for steel (as calculated by Canadian steel makers) has exceeded 16 million tonnes since 1997 and in 2000 increased by 1.5 million tonnes to about 17.8 million tonnes. Domestic mills increased their imports of semis in 2000. These imports exceeded 1999 levels but were less than in 1998. During 2000, Canadian authorities had unfair trade investigations underway involving hot rolled carbon steel plate (dumping and subsidy investigation) from six countries, stainless steel round bar (dumping and subsidy investigation) from two countries, concrete rebar (dumping) from seven countries, and corrosion resistant steel sheet (dumping and subsidy investigation) from seven countries. Despite the fact that a large number of trade actions were ongoing, overall import volumes did not decline as might have been expected. Instead, what has occurred is that imports of product from countries subject to unfair trade actions were replaced with imports of such goods from countries not being investigated or not currently subject to an injury finding. The result of such "source switching" is to undercut the effect of trade remedy actions and the relief that they are designed to offer domestic producers who have sought protection from injuriously traded imports. In 2001, demand for steel is expected to fall from current levels although it will remain generally good. Decreased demand and the impact of trade actions should reduce steel imports to perhaps 6.0 to 6.5 million tonnes.

To date in 2001, Canadian authorities have initiated two additional unfair trade investigations: hot rolled carbon steel sheet (dumping and subsidy) from 13 countries on January 19, 2001 and cold rolled steel

sheet (dumping) from 9 countries on March 12, 2001. Details about any of these unfair trade investigations is available at the following web site: <http://www.cca-adre.gc.ca/customs/business/sima/sor-list-e.html>.

Demand:

Overall, steel demand in 2000 was excellent, with demand in Canada at an all time high. In fact, Canadian steel demand has increased continuously since 1995. The year 2001 is expected to be another year of relatively good steel demand - at least by historical standards. However, the economic slowdown being experienced to date in 2001 and mounting concerns that the economy may experience at least one or two quarters of very modest growth means that demand will likely be well below 2000 levels, perhaps reaching a level not seen since 1997 or 1998.

In the Automotive sector, Canadian motor vehicle production decreased 2.4% to 2.670 million units in 2000 compared to 1999. However, sales of new vehicles rose 3.0% to 1.588 million units in 2000 compared to 1999. Both passenger cars and trucks contributed to the increase in 2000, with car sales up by 5.3% while trucks increased by 0.8%. Indeed, Canadian motor vehicle sales exceeded their previous peak attained in 1988 when 1.566 million units were sold. However, slumping sales in late 2000 have led auto makers (DaimlerChrysler, G.M., Cami, Ford) to announce plant closures and production cut backs in 2001. At least one analyst anticipates that these announcements will cut Canada's 2001 auto production by 8 to 10%. In addition, at least one auto maker has announced that it will be negotiating price cuts with its suppliers when it enters into new contracts.

Direct steel industry shipments for motor vehicles and parts decreased by 1.5% (to 2.907 million tonnes) in 2000 from the level reached in 1999.

In the Construction sector, activity as measured by the value of building permits issued for residential and non-residential construction, increased 3.6% in 2000 compared to 1999. While the value of non-residential building permits increased 5.6% in 2000, the value of residential permits grew by 2.1%. Housing starts in 2000 totalled 153,400, up from 149,500 in 1999 and 138,300 in 1998. Private sector forecasts anticipate housing starts to increase to 154,000 in 2001 before declining to 151,000 in 2002.

In the Pipe and Tube sector, steel shipments to the sector increased by 11.5% (to 1.957 million tonnes) in 2000 from the level reached in 1999. Although production of pipe and tube products in 2000 increased by 6.2% (to 2.640 million tonnes) over 1999 levels, total shipments of such goods increased by 8.4% (to 2.735 million tonnes). While domestic shipments of pipe and tube products increased by 2.4% in 2000, exports increased by 24.1%. The overall increase in pipe and tube shipments was due primarily to increased total shipments of hollow structural sections (up 8.1%), mechanical tubing (up 14.0%), oilwell casing (up 50.3%), oilwell tubing (up 82.1%) and other tubular products (up 21.0%) offsetting decreases in welded and seamless line pipe (down 11.3%) and welded and seamless standard pipe (down 12.6%).

In the Distribution sector, shipments to Service Centres decreased by 1.3% (to 3.796 million tonnes) in 2000 compared to 1999. This follows an increase in mill shipments to this sector of 10.8% in 1999.

Steel shipments to the Manufacturing sector decreased by 0.2% (to 7.222 million tonnes) in 2000 over 1999 levels. In 1999, shipments to this sector had increased by 5.9% over 1998 levels.

Steel shipments in the Machinery & Equipment sector increased by 12.4% (to .184 million tonnes) in 2000 compared to 1999.

Steel shipments to the Wire & Wire Products sector decreased by 0.7% (to .839 million tonnes) in 2000 over 1999 levels. This follows an increase of shipments to this sector of 1.0% in 1999 compared to 1998.

Overall, in the Canadian market for all of 2000 compared to the same period in 1999, total (domestic and export) shipments fell by 0.2%, exports were up 5.7% and imports were up 29.1% (imports from the U.S. were up 13.8%). As a result, total shipments (from domestic sources only) decreased by 3.0% while apparent domestic consumption increased by 9.1%.

Apparent Domestic Consumption (ADC):

ADC in 2000, calculated based on data reported to the OECD, is estimated to be 18.649 million tonnes. This is up 10.8% from the level of 16.824 million tonnes in 1999.

Trade Data:

In 2000, total imports (as reported to the OECD) increased by 33.2% (to 8.336 million tonnes) from 1999 levels while exports (as reported to the OECD) increased by 5.1% (to 4.607 million tonnes) over the same period.

In 2000, imports of semi-finished steel increased by 35.4% (to 0.530 million tonnes) while imports of other steel products increased by 33.1% (to 7.804 million tonnes). In 1999, imports of semi-finished steel decreased by 53.0% (to 0.392 million tonnes) while imports of other steel products fell by 11.3% (to 5.864 million tonnes). Imports of semi-finished steel totalled 0.833 million tonnes in 1998 and 0.823 million tonnes in 1997.

Sales and Profit Levels:

In 2000, Canada's 3 largest steel makers reported a combined net income of \$142.8 million on sales of \$7.144 billion. In 1999, those companies reported a combined net income of \$281.1 million on sales of \$7.365 billion. This represents a 49.2% decrease in profits and a 3.0% decrease in revenues between 1999 and 2000. Between 1999 and 2000, total shipments fell by 2.5% to 10.030 million tonnes.

With the lower net income and reduced sales, price per unit has fallen from 1999 levels. This is reflected in the average revenue per ton shipped for these 3 firms which decreased from \$646 in 1999 to \$643 in 2000. If the shipments and revenues for U.S. based operations are excluded so that only shipments and revenues from Canadian facilities are used, the average revenue per ton shipped for these 3 firms decreased from \$649 in 1999 to \$643 in 2000.

The market slowdown can be more clearly seen if the fourth quarter of 2000 is compared to the fourth quarter of 1999. In the fourth quarter of 2000, total industry shipments fell by 5.8% to 2.404 million tonnes. The combined net loss for these 3 firms was \$55.1 million on sales of \$1.599 billion. In the fourth quarter of 1999, those companies reported a net income of \$117.5 million on sales of \$1.838 billion. This represents a decline in profits of \$172.6 million and a 13% decline in revenues in one year.

Given the reduced net income and lower sales between these two periods, lower prices per unit result. For these 3 firms, the average revenue per ton shipped has declined from \$650 in the fourth quarter of 1999 to \$600 in the fourth quarter of 2000. If the shipments and revenues for U.S. based operations are excluded so that only shipments and revenues from Canadian facilities are used, the average revenue per ton shipped for these firms decreased from \$650 in the fourth quarter of 1999 to \$603 in fourth quarter

of 2000. The fourth quarter information reveals that the Canadian steel market situation has deteriorated more dramatically than an examination of the annual data would appear to indicate.

The three firms cited above accounted for over 60% of Canada's crude steel production and about 66% of Canada's domestically produced steel shipments in 2000.

Publication Date: 2001-04-04
Author: Industry Canada

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