Trade groups associated with the U.S. steel industry are talking about export controls again. Every time the cyclical price of scrap starts to increase, the steel industry starts looking for ways to control prices through artificial controls on their scrap inputs. They tried in 1953, 1973, 1979, and considered another try in 2004.

Each time the steel industry has sought government help through export controls, the effort has failed. And the reason for that unbroken record is simple: artificial barriers to the free and fair trade of commodity materials have a detrimental effect on the economy. Worse yet, studies suggest that efforts to control prices through export controls can result in further increases in prices.

The global ferrous scrap market is one of the purest examples of supply and demand economics. Scrap is a world-traded commodity that becomes less dependent on local supplies or local markets every day. The movement of material responds directly to market forces regardless of location. And the long-term cyclical nature of the scrap economy makes it clear that the market is adept at correcting irregularities in price or supply quite naturally. Any attempt to artificially alter that cycle will, at best, do no good. Instead, history indicates that it can do unanticipated harm.

Increasing demand for ferrous scrap as a result of U.S. steelmakers’ increased steel production earlier this year has driven the price of ferrous metals upward. This price increase was demand-driven, not supply-driven. The potential availability of scrap materials is not in question. Studies commissioned by ISRI earlier this decade (Robert Damuth, “Iron and Steel Scrap Accumulation and Availability as of

CHART 1: Brazilian Pig Iron, HBI and No. 1 HMS 2000-2010 (Gross Tons)

CHART 2: Spread Between No. 1 Heavy Melt Steel And Rebar 2000-2010 (Short Tons, Actual Dollars)
December 31, 2003" Nathan Associates, Inc. (July 2005) estimated that U.S. scrap reserves (obsolete scrap) are in excess of one billion tons.

Just as the need for specification-grade scrap by the steel industry is driven by orders from their consumers, the supply of obsolete materials used to process specification-grade scrap is driven by price. Studies such as Robert R. Nathan Associates “Price-Volume Relationships for the Supply of Scrap Iron and Steel: A Study of Price Elasticity of Supply” Jan. 1974, show this price elasticity and suggest that supply/demand vacuums are quickly restored to equilibrium as the price for obsolete scrap rises.

Scrap recyclers do not buy scrap inherently expecting to hold it until prices increase. They buy scrap to meet their customers' monthly requirements. After acquiring and then processing the scrap into specification-grade material, scrap processors then deliver the material based on current market conditions dictated by the customer. Customers have orders to fill and thus buy scrap. Scrap processors are the price taker, not the price setter, hence the phrase, “Scrap is bought, not sold.”

Ferrous scrap is a global commodity, just like iron ore, coke, pig iron, DRI and HBI. Chart 1 shows that as global demand for finished steel has grown, so too has the global demand and price for ferrous scrap and all the other raw materials used in steel production. This growing demand for finished steel has allowed steel manufacturers to increase prices to their customers, often at margins that exceed the additional cost of steel inputs. Chart 2 shows the spread, in actual dollars, between No. 1 HMS (scrap) and its finished steel counterpart, rebar. The median spread over the last 10 years is $283.41. At the same time, however, the spread has actually widened over the past six years despite rising scrap prices. Thus, higher scrap prices alone have not eroded this differential.

Scrap recyclers understand and appreciate the price pressures U.S. steel producers are feeling, but history also shows this price cycle will likely be short-lived. Chart 3 shows it was only a year or so ago that scrap prices were at record lows, forcing many scrap processors into bankruptcy and/or consolidation. The cyclical nature of the industry points out that the prices of today do not last indefinitely.

And while we’ve seen ferrous scrap prices climb from the lows of late 2009/early 2010, more recently published prices for both obsolete scrap and prompt industrial scrap, as measured by No.1 HMS and Chicago bushelings, have eased by 20% and 11% respectively over the latest April
to mid-July time frame. The near-term further suggests that scrap prices will again be lower over the ensuing third quarter of 2010.

**Export Restrictions Not the Answer**

The rise in U.S. scrap exports since 2000 is also neither alarming nor unprecedented and today’s scrap prices are not at record levels. As shown in Chart 4, when viewed in constant 1998 dollars (the U.S. Geological Survey benchmark), record prices for ferrous scrap actually peaked in 1974, the last time export controls were imposed.

The imposition of export controls caused what is known as “control reverse,” whereby scrap prices actually rose. As a result, artificial interference with the scrap market from those export controls ended up costing the steel industry some $2 billion more for ferrous scrap than it would have otherwise paid.

Time and time again, history has shown that export controls are the wrong solution. The cyclical nature of the scrap market makes it abundantly clear that concerns about price or supply will correct themselves naturally. Attempts to artificially alter that cycle, such as the current calls for scrap export controls, do not work. More likely, such controls will cause great harm not only to scrap processors, but to steel producers as well.

Should scrap export controls be established, an important raw material supply source would be artificially removed from the global marketplace. As a result, the global market price for ferrous scrap (as natural resource materials for making steel) would increase significantly. Foreign and domestic end-users (i.e., manufacturers) would likely see price increases for finished steel far higher than what has occurred in the last several months. While higher steel prices on the world market might be welcomed by domestic steel producers who are exporting their product, it would be left to U.S. manufacturers, and ultimately, U.S. consumers to bear the higher costs created by this unwarranted market distortion.

Guided by history, we know export controls to be detrimental to the economy locally, nationally, and globally. History has also shown that the domestic steel industry’s efforts to affect export controls have regularly failed and that despite these failures the industry has gone on to achieve record levels of production and record profits.