



July 25, 2012

A Global Steel Giant Scales Back

By STANLEY REED

LONDON — Steel is a notoriously volatile industry. But four years ago, Lakshmi Mittal, the Indian-born tycoon, appeared to have mastered the business.

He was still aglow from his 2006 victory in an epic takeover battle for his nearest rival, Arcelor of Luxembourg, which made the merged company, [ArcelorMittal](#), the world's largest steel maker by far. With a fast-growing world economy hungry for steel, ArcelorMittal reported operating income of nearly \$12 billion for 2008.

Things are different now, with Europe in a deep economic funk and once-roaring construction markets like India and China also slowing. Last year, the company had operating income of \$4.9 billion. And on Wednesday, [it reported](#) second-quarter operating income of \$1.1 billion, on sales of \$22.48 billion. While the sales were down 10 percent from a year earlier, income was down more than 50 percent as the cost of the industry's raw material, iron ore, rose even as steel prices slumped.

“Clearly, this performance is not acceptable at all,” Mr. Mittal said by telephone on Wednesday, while noting that the severity of the various downturns had been unexpected.

The company has already started curtailing production in Europe to match reduced demand. And it is bracing for resistance from unions and governments to other planned cost cuts. Those include the major wage and benefit concessions it is seeking from workers in the United States, where it employs thousands of workers at 12 major facilities in states including Indiana and Pennsylvania.

Back in the boom times, Mr. Mittal's strategy was to consolidate a fragmenting industry. Putting production into fewer hands would make it easier to adjust output to cushion the cyclical downturns that have always played havoc with steel makers. Among the American companies he bought were Inland Steel and the International Steel Group, which owned plants once operated by companies like LTV and Weirton Steel.

Beginning with the global [recession](#) in 2009, though, ArcelorMittal has faced one setback after another.

The latest and perhaps the most serious hazard is the protracted euro zone financial turmoil that has all but killed demand for steel in Western Europe. ArcelorMittal, with headquarters in Luxembourg, produced more than a third of its worldwide crude steel in Europe last year. Nearly 100,000 of the company's 260,000 employees work in Europe.

ArcelorMittal's share price has fallen steeply since 2008, reducing the value of the Mittal family's controlling stake of 40 percent to \$9 billion from an estimated \$55 billion in 2008.

The benchmark price of European steel in 2008 was about 850 euros (\$1,030 at today's exchange rates) a metric ton. By last month, that price was 573 euros, according to Meps, a consulting firm in Sheffield, England.

And the lower the price drops, the more reluctant buyers are to commit, "because the material they have in stock is worth less as each week passes," said Peter Fish, the chairman of Meps.

Inexpensive Chinese steel, heavily subsidized by its government, has also been a big drag on global prices. Even as steel production in Western Europe and the United States has declined over the last five years, China's output has grown about 60 percent, and China now makes 46 percent of the world's steel.

Mr. Mittal said almost all Chinese companies lost money in the first half of the year. "That is good news in the sense that they will have to work on restructuring the steel industry," eventually putting profit ahead of volume, he said.

But largely because of China's ravenous appetite for iron ore, the industry's main raw material, its price has quadrupled since 2006, to about \$134 a metric ton.

"The steel makers like ArcelorMittal are caught in the middle," said Jeff Largey, an analyst at Macquarie in London. "On the one hand, the end markets are weak and they don't have any pricing power. On the other hand, they can't do anything about high raw materials prices driven by demand from China."

Mr. Mittal started out in the 1970s building and operating a minimill in Indonesia. He built his fortune in the next three decades by buying and fixing a network of gigantic but poorly performing

plants in places like Kazakhstan, Romania and Mexico.

But now Mr. Mittal finds himself in a tough fight just to control costs and reduce the company's \$22 billion in debt. In Europe, he has idled nine of his 25 blast furnaces, the huge machines that turn iron ore into liquid metal.

And in contrast to his earlier acquisition spree, he is now selling properties. ArcelorMittal recently sold two North American steel foundation businesses called Skyline Steel and Astralloy to a rival, **Nucor**, for \$605 million — part of \$2.7 billion in divestitures since September.

Because of its mergers, ArcelorMittal has “a lot of low-hanging fruit,” said Wen Li, an analyst at Credit Sights in New York.

The company also benefits from its global reach. The mills in the United States are doing better than those in Europe, thanks to demand from heavy-equipment makers like Caterpillar and for steel pipe to feed the North American shale gas boom. And unlike its rivals, ArcelorMittal has its own major iron ore operations, helping buffer high prices.

In Europe, where the company faces its deepest problems, it says it wants to keep its best plants — like those in Ghent, Belgium and Dunkirk, France — running at high rates while sidelining the poor performers. But ArcelorMittal probably needs to close some plants permanently, analysts say. And as the automakers know too well, closing plants in Europe requires months, if not years, of talks.

Labor problems are also looming in the United States. The company and the United Steelworkers union are now in intensive talks in Pittsburgh, trying to reach a new agreement before the current contract covering 12,500 workers expires at the end of August. ArcelorMittal is pushing for lower costs and more flexible work rules that the union says would add up to wage and benefit reductions of \$28 an hour.

The company says the workers make an average of \$170,855 a year in pay and benefits, of which \$82,471 is gross pay. A union spokesman, Anthony Montana, said the company's figure was “an inflated noncash cost calculation,” but he would not provide a union estimate.

The union says that in addition to upfront compensation cuts, the company also wants the right to cut wages during periods of reduced operation. The company is proposing cuts in retirement benefits, too, seeking to eliminate retiree health care for employees hired after Sept. 1, 2012, and switch those employees to a 401(k) from a pension plan.

Mr. Largey, the Macquarie analyst, said the company might think it was worth enduring a strike if needed to reduce costs.

But an ArcelorMittal spokesman, William C. Steers, said on Wednesday, “We are optimistic we will reach a fair agreement because ultimately the union and the company want the same thing — a successful business throughout the cycle that provides good job security and industry-leading pay for industry-leading performance.”

This article has been revised to reflect the following correction:

Correction: July 25, 2012

An earlier version of this article misstated the number of blast furnaces that Lakshmi Mittal of ArcelorMittal has idled in Europe. It is nine of 25, not 16 of 25.