Commentary:

Dealers are scrambling to find enough obsolete scrap after several mills cut prices by as much as $35 per gross ton this month and the usual bumper crop of obsolete scrap failed to materialize. Busheling and bundles also are in tight supply though at least one major EAF-sheet steel producer has countered that by purchasing several cargoes of prime scrap and pig iron from overseas suppliers. These are scheduled to be delivered in May and June and may ease the pressure on those grades.

The steep price cuts in shredded, heavy melt and other cut grades has discouraged many dealers in the Midwest and South who were already having problems filling orders for obsolete scrap. The mild weather kept obsolete scrap flowing into their yards throughout the winter. Dealers are not seeing an uptick in intake, said a Chicago area trader, and the now lower scale prices because of this month’s drop in mill buying prices is discouraging auto wreckers and other feedstock suppliers.

Some dealers pre-sold more heavy melt and shredded scrap this month because they expected to produce more from the additional feedstock that normally flows into their yards in April. However, the supply deluge may have already passed through their hands. “We experienced the spring thaw back in February,” the trader added, “so there is no huge flow of obsolete scrap now.”

Some are processing scrap as soon as it comes through the gates and quickly shipping to the mills. Another Midwest trader said shipments from at least two of his yards are late, but he expects to catch-up this week. It’s not simply reduced scrap flows, he said. Orders from some mills came in later this month because the buy week negotiations took longer. Resistance to the price drops has also prompted some dealers to hold back scrap. Some mills and brokers were still buying scrap in the second week of the month, he said.

Mills got the scrap they needed this month, but are still listening to new offers.

Most mills have gotten what they need this month, he said, but a few are still accepting more offers of scrap at the same prices they paid earlier this month. That may help them build inventories, but it also may be encouraging some dealers to view the mills as expecting supplies to be tight again in May. That may be encouraging them to hold back some scrap and look for prices to rise next month, he said.
Several dealers said they expect obsolete scrap prices to bounce back in May. Some are looking for increases of as much as $20 per ton, but one Chicago-based broker doesn’t expect much more than a modest $5 or $10-per-ton uptick in obsolete scrap prices and no rise in busheling and bundles prices. Mills have adequate inventories in their supply pipelines, he said, and because deliveries are slow, scrap will still be arriving at month’s end and during the first week of May. That may enable them to hold the line on prices.

If the heavy melt and shredded scrap prices bounce back, they may have to do it without much help from offshore steelmakers. A modest buying flurry saw export prices to Turkey rise to $276 per tonne for 80/20 heavy melt and $281 for shredded scrap delivered to a Turkish port. But that was more than a week ago and several European suppliers now are selling scrap to the Turkish mills at lower prices.

East Coast exporters have reacted as expected, and cut their buying prices, said one Eastern trader. They had been paying the largest local dealers and a few inland suppliers as much as $250 per ton for export heavy melt, he said, but have cut those offers drastically. Some are now offering $225 per ton and even less to the smaller nearby yards that have fewer outlets other than the docks.

A new concern in the Detroit area is a decline in the output of prime industrial scrap from auto stamping plants and auto industry component makers. Bundles and busheling are in demand from both sheet steel producers and other steelmakers, but their availability is limited by the pace of manufacturing. This reduced scrap output reflects the decline in sales of mid- and full-size passenger cars. However, sales of light trucks, crossovers, and SUVs are still strong, and these are bigger steel users than the other auto plants.

But scrap dealers who are worried about the pace of domestic steel output and its likely impact on scrap demand, got two positive reports this week. U.S. raw steel production rose to 1,740,000 net tons last week while the industry capability utilization rate climbed to 74.6%, the American Iron and Steel Institute said. That is the second increase in as many weeks and is up 2.2% from the previous week when steel output totaled 1,703,000 tons and the mill operating rate was 73.0%.

Also, steel service centers shipped 2,460,000 tons of flat-rolled steel to users in March. That is an increase of 10.3% from 2,230,000 tons shipped in February and 17.1% ahead of the year-ago pace. Service center inventories of sheet products have slipped to 4,460,000 million tons or the equivalent of 1.82 months’ supply. That is off by 3.4% from the 4,990,000 tons on hand in February and is the lowest level for the service centers’ stocks of flat-rolled steel products in almost eight years. Stronger shipments and lower inventories are regarded as an indicator of rising sheet steel demand.

Access to gondola railcars and their availability are a growing problem.

In addition to the spring scrap drought, some dealers are having trouble getting enough railcars to ship scrap. That may be further complicating supply shortages now. In some regions, said a Pittsburgh-based broker, railcars are not available because they have been
relocated to other areas of the country. Sales of shredded from East Coast shredders and export yards to the mills in the Midwest have depleted the supply of available railcars along the coast. Without an immediate backhaul, many can be found left sitting on sidings in the Midwest.

Domestic mills in the Midwest and the South have become more attractive markets for some coastal scrap processors when offshore demand and prices are weaker. The mills and their brokers buy this so-called “springboard scrap” (scrap from more distant sources) to minimize their purchases from local scrap yards. Their goal may be to lower the local prices or limit an anticipated price increase that month.

In other words, a steelmaker might offer to buy half its usual monthly needs from local suppliers in order to gain leverage in its play to negotiate lower prices. This works if those local dealers fear losing orders to rivals and being stuck with excess scrap which they may end up selling elsewhere at a lower price.

Some mills are conserving cash by slowing down the unloading of scrap shipments.

Some mills also use delayed unloading as a cash conservation measure. Normally the meter on paying for scrap doesn’t start running until the mill inspects the shipment and unloads it. Some mills have added to the processor’s pain, said one dealer, by extending the payment dates from the usual net price in 30 days, to 60 days. And even worse, there are one or two mills with reputations as slow payers who have kept some scrap dealers waiting from six months or longer for a check.

Today, said the Pittsburgh area broker, it also takes longer for the mills to finish their purchases each month because they are buying from distant suppliers. These shipments may require moving or switching cars from a major rail line to a smaller short-line railroad that may not be able to move those cars for several days. The reverse can occur as well when transferring cars from a short-line to a major rail carriers’ lines.

Anytime, there’s a switch, explained the broker, scrap will sit for a few days in the rail yard. One reason is that scrap is not a priority commodity for the railroads. Perishable items like food or hazardous materials like crude oil from the Midwest to the East Coast refineries will get more attention. Also, food and fuel may be shipped in special purpose cars that provide more revenue to the railroads than general purpose cars like the gondola cars that scrap shippers use. Years ago, one major U.S. railroad tried to classify all its gondola cars as special purpose cars to get them back faster and raise the freight rates, but it was forced to discard that plan.

It’s common practice for the mills to unload the railroad-owned cars before they unload railcars owned or leased by the major dealers and brokers. The reason: railroad-owned cars will impose demurrage charges for the time it waits to be unloaded. On the other hand, the brokers and dealers won’t impose demurrage fees, and treat the waiting/stalling time as the “cost of doing business” with certain mills. This can’t be done with truck
shipments because the scrap dealer’s drivers are expected back at the yard by a certain time. Railcars, however, can sit on a siding for weeks and not be reported to the police as hijacked.

Mills are not the only offenders. A few years ago, a Canadian steel mill was singing the blues about the excess number of empty gondola cars parked at its steel mill and not folksinger Gordon Lightfoot’s famous “Canadian Railroad Trilogy.” Those excess cars delayed both deliveries of scrap and shipments of its steel products. The railroad, said a broker who bought scrap for that mill, had less demand for those railcars and chose to use the steel mill as a rent-free storage site.

**Shredded Scrap Thermometer: Narrowing the price spread.**

One concern voiced by some scrap dealers in recent months is the rising spread between shredded scrap and busheling prices. Busheling tags have soared to as high as $390 per ton in a few regions while shredded prices have slipped by $30 per ton this month and now are averaging about $295 per ton in the Midwest, almost $100 less than busheling. Normally, dealers and brokers expect to see about a $20 or $30 per ton spread between these grades, with busheling at the higher end and shredded available at a modest discount. The widening price spread can pose problems for mills and the dealers. These include:

- That shredded is available at a significantly lower price than busheling could spur demand for the fragmented scrap at a time when intake of shredder feedstock is tight or shredding operations and dealers’ ability to produce enough in a timely manner is hampered.

- Feedstock suppliers like auto wreckers and demolition contractors track all scrap prices. As the price spread grows, dealers worry that suppliers will hold back material with the hope that it will spur an increase in feedstock prices.

- Busheling may offer advantages like cleanliness and higher metal recovery rates, but shredded producers argue that their product provides more density. This raises both the metal yield in the furnace and lowers per ton scrap shipping costs.

Busheling lacks the same sensitivity to prices that determines the supply of shredded scrap; and thus, the wild cards in its outlook can shift with scrap consumption. These include:

- When flat-rolled steel, demand was weaker in 2015, busheling and shredded prices were upside-down with shredded selling at a premium over busheling and more of the usual shredded users shifting their melt mix to use the then-cheaper industrial scrap. That not only reduced shredded production but also raised the operating expenses for some shredders.
U.S. shredded producers get only a modest premium of $5 per tonne over 80/20 heavy melt in the offshore market and sell their shredded at a discount of $5 per tonne to the bonus grade (five-foot plate and structural scrap) whereas in the U.S. market they can obtain premium prices of more than $30 per gross ton over both cut grades which has encouraged them to sell more of their output at home.

The Nasdaq Futures Exchange (NFX) expects to start trading in the Midwest US shredded scrap index futures on June 15, 2017. The contract will trade in 20-gross ton units with the prices settled on the 11th day of each month against the TSI Midwest US Shredded Scrap Index published by Platts. For additional information about shredded futures trading, contact John Conheeney at WSEM. His phone number is 201-503-0922 and his email is jconheeney@wsemgroup.com.

Note: Each issue, Mike Marley gives his opinion on the one-month steel scrap price outlook. He explains the key reasons for his view and highlights the “wild cards” that might cause him to be wrong.
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