

Stahlzentrum – 10 November 2006

Theme: Crossing frontiers
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(TITLE SLIDE)

Mr President, Ladies and Gentlemen, thank you for the invitation to make some remarks on the theme of “Crossing Frontiers”.

As an industry we are faced with fundamental trends of “crossing frontiers” in terms of interconnected global market trends and international competition and cooperation. Some of these trends are well addressed by our own industry and the regulatory frameworks – others are not.

(AGENDA SLIDE)

Let me start by highlighting some of the key global trends that are shaping the steel industry, namely

- **The rise of the BRIC nations** (BRIC = Brazil, Russia, India, China) and their impact on a number of aspects of the global steel industry
- **Consolidation** of producers, why I believe its happening and why it will continue to happen
- **Trade flows** – we operate in an increasingly global industry
- **People** – management teams and workforces are becoming increasingly international and highly skilled.

I'll then conclude by highlighting some areas where the industry and the regulatory environment needs to improve for European producers to remain competitive, namely

- **Energy markets** - The EU energy market needs reform
- **Climate change regulation** - The Emissions Trading Scheme is broken and needs fixing.
- **Trade regulations** need to ensure a fair and level playing field

Let me begin this overview of key trends with the rise of the BRIC nations

The rise of the so-called BRIC countries marks a permanent shift in steel production and in steel consumption. Whereas a few years ago it was the “old” world of Europe and North America that dominated the steel world, now the balance has moved to the developing world, with China making more than twice as much steel as the EU25 – 2006 estimates are of around 425mt compared to around 180mt. The BRICs now make up exactly half of all world crude steel production [on the basis first 3 quarters of 2006].

(SLIDE 1) Strong forecast growth of the BRICs markets demand is by far the largest factor in the healthy outlook for the global steel industry – around 70% of the long-term growth estimated by the IISI at a very respectable 4-5% per year to 2015 is provided by the BRICs.

The BRICs producers are also directly transforming the European industry landscape in addition to their ‘global trends’ impact. Russian, Brazilian and Indian producers have been active in acquiring or merging with companies and assets in our more ‘mature’ but technically demanding steel markets (such as Severstal acquiring Rouge in the US Lucchini in Italy, CSNs much discussed bid for Wheeling Pitt and of course Corus’ combination with TATA). BRICs producers are also developing ‘structural’ commercial access to the European market. This is in addition to the large import trade flows that we are now seeing.

The transformational impact of BRICs producers also extends to the capital markets. Many Russian producers have or are in the process of listing shares this week on the London and New York stock markets – the flotations of Severstal and TMK are only the most recent examples. [More London than New York thanks to Sarbanes-Oxley.]

But before we move on – should we be surprised? In 1820, before the industrial revolution, China and India were the two largest economies in the world, combined providing 48% of global GDP. Is this not just the re-emergence of an older order?

After the BRIC, let’s turn to the second trend, consolidation

Up until now as an industry we have been increasingly squeezed between a consolidated supply base, where 73% of global seaborne supply of iron ore is in the hands of five companies, and key customer sectors: top 5 auto makers have 75% global market share and top 3 can makers have a 90% European market share.

(SLIDE 2)

However, over recent years we have seen a number of examples where steel companies are beginning to consolidate into larger groupings – the clearest example being the recent Arcelor Mittal combination but we also can mention Tata and Corus. But even with the combination, the global market share of the top 5 steel producers remains at around 22%.

(SLIDE 3) As this simple illustration shows, this concentration is relatively low compared with a number of other metals and mining sectors, such as Nickel and Alumina, which have **achieved** a step change in average returns. The experience of these sectors suggests that a global top 5 share of around 40% is related to **the ability to achieve** such a step change **in returns**. This implies for our industry a top 5 of 100-150mt production each. Clearly this process has a long way to go.

Such a step change in financial performance for the steel industry will not merely be a case of matching size with size. I am convinced that a far more effective value level will be changing the business model and value chain of the new, global companies:

- Developing primary steel making closer to raw materials and
- Focusing 'downstream market' operations close to the customer with value addition and service,

The new consolidated Groups have the opportunity to make a decisive break with the industry's boom and bust history.

Let's comment on the third trend, the increase of international trade

The removal of trade barriers has, in general, been a good thing, not just for the countries that find it easier to export their products, but for the consumer in the importing country who has experienced stable or even falling prices for many products.

Whilst this has been good for consumers and good for Governments to have low inflation, for us as manufacturers with large capital assets located in Western Europe, this has presented a challenge to become ever more competitive. This competitiveness will be achieved by adding value to the products we sell through improved product quality, through better surface finishes, through better delivery performance and through a closer partnership with our major customers.

(SLIDE 4)

Looking at the statistics, in 1975, when the EU took the brave step of allowing the UK to join, only 22% of the world's 500Mt production was traded across a frontier. i.e. just over 110Mt.

In 1990, that had risen to 26%. But by 2004, 42% was traded across a frontier.

However, the pattern of greater global trade flows and freedom of movement also affects our customers. We have seen a major migration of steel-using companies away from the developed economies of the USA or Western Europe towards lower cost locations. So one of the challenges for us in the future will be to change our business model to keep us close to our customers, which clearly links to the two previous trends of BRICs growth and consolidation.

I will return later to 'international trade' as one of the areas for improvement.

Lastly in this 'context' section, let us turn to people - international management and skills levels

The free movement of people and skills has been another key emerging industry feature. This has allowed me, a Frenchman, to run a UK-based multi-national, with an executive committee that includes a Dutchman, a Belgian, a Brazilian, a Welshman, a Scotsman and even a token Englishman. This might be someone's definition of a nightmare, but except for the World Cup we play to our various strengths and it works well for us.

More seriously, the steel industry needs a wide range of skills. **(SLIDE 5)** This is a technology driven industry and we no longer employ people for their physical strength or ability to withstand a hot working environment.

To be successful today, our employees must be literate and numerate, and capable of working in a workplace that looks more like Mission Control for the Space Shuttle, than an operator's cabin in a steel works.

Our workforce is ageing and all over "old" Europe we see a problem with the output from schools and colleges.

As an industry we have become more involved in the education process to improve the quality of the people coming to work for us and to make our industry more attractive to work in.

Corus sponsors the development of national skills academies in the UK and supports graduate and post-graduate training. In the Netherlands, we support the National Institute for Metals Research, which works with Dutch universities on metals related research.

But although these schemes will help create better-trained people in the UK or Netherlands, we have a significant interest in gaining access to skilled people from across the enlarged EU.

And also an interest in taking advantage of the more traditional education provided in the newest member states. We are now providing some safety documentation in Polish for people working at our Scunthorpe works!

So, crossing frontiers is a core feature of the new steel environment through the rise of the BRIC nations, through the consolidation, through trade flows and through international skills.

As an industry we are positively responding to this trend. However, there are areas where we, in the EU, need to do better.

On energy, the European energy market gives our industry competitive disadvantages.

(SLIDE 6) Electricity doesn't have a single price even in the EU. Although some of the difference can be explained by the different ways electricity is generated – UK largely dependent on gas, Germany on coal and France on nuclear - we know that there are other factors at work, some of which are under investigation by the European Commission, but the result is up to 40% difference between the highest and lowest cost markets.

- We have different, changing costs against what are frequently 'global' steel price levels
- Secondly, we have little predictability – a crucial element of making the long-term investment decisions the steel industry requires

Against this background, I strongly support the Commission's work and the strong statements made recently by Commissioner Kroes that there may need to be substantial changes to the structure of the EU's energy markets.

(SLIDE 7)

In our view this market need fundamental reform. We are looking for:

1. Vigorous and consistent enforcement of European competition rules
2. Price transparency and real unbundling of the networks from the generators
3. Improved conditions for cross-border competition and increased interconnections (10% of interconnections is a good target)
4. Encouragement of investment in new electricity generation capacity. I believe long-term contracts, for instance with steelmakers, could provide the necessary stability to support the massive investment required.
5. Re-enforcement of the EU's security of supply, which must become a foreign policy priority

The second area to improve, the way we address the climate change issue, one of the most important challenges ever met by our industry.

The EU's Emissions Trading Scheme is inappropriate because it does not create a change in behaviour.

1. Inappropriate because it distorts competition between steel manufacturers in different EU countries. Allocations are made on the plant by plant basis. There is no relation between the allocation and the performance of the plant.
2. Inappropriate because it distorts competition between EU manufacturers and those outside the EU – **(SLIDE 8)** We must continue to point out that only 30% of the world's steel producing countries have signed up to the obligations of the Kyoto agreement, whereas 90% of all new capacity is being developed in the 70% not covered by a Kyoto obligation. We need a scheme that can be extended globally so that steel companies across the globe can make their contribution to overall CO2 reductions.
3. Inappropriate because it is giving electricity companies excess profits without requiring them to do anything in terms of abatement. Governments throughout the EU have woken up to this. Many are considering ways of taking some of that money away from the electricity generators. However, energy intensive industry will still pay the same elevated electricity price, even if some of the money finds its way into the pockets of our various finance ministries.

4. Finally inappropriate because it fails to reward innovation or to recognise the significant efforts already made over many decades to reduce the carbon intensity of the steel industry.

You will know that the ULCOS project is looking at the potential for new technologies to reduce the carbon impact of ore-based steelmaking, including technology like Carbon Capture & Storage. In our view, Finance Ministers must accept that unless the money they raise is recycled back to energy intensive companies through investment in new technologies. The sort of breakthrough in CO2 emissions that we need, will take longer.

Two weeks ago, on 30th October, the UK Government published the 'Stern Report' looking at the economic cost of climate change. The key messages are that this is a global problem that needs a global solution and that action must be taken now, not in the future.

There is no merit in continuing to dispute the need to do something about carbon dioxide emissions.

Emissions trading is here to stay, but it is essential that the scheme changes in the period after 2012.

As Eurofer we are working on a solution that would make emissions trading more efficient. A solution where efficiency in manufacturing performance within the steel sector in the EU25 becomes the basis of allocation, adjusted for actual output.

The benefits are that:

- It removes reliance on imperfect forecasts of output, or on auctioning which would put us at a major economic disadvantage compared to those sectors that can easily pass on the cost of carbon to their customers.
- It allows efficient installations to grow
- It removes the distortions to competition within EU and could be extended outside the EU

After energy and climate change, there is another area of concern for our industry: Trade Defence Instruments

A globalised economy needs clear rules to ensure fair competition. But this also means that there are occasions where we must rely on trade defence instruments as a means of dealing

with unfair trade practices or illegal state intervention. Under those circumstances it is essential that we receive the same level of protection as applies in our major trading partners.

So we welcome the debate within the EU started by Commissioner Mandelson. But, in our view a trade defence system is indispensable, otherwise competitive European industries and jobs are at risk. It cannot be in Europe's interest to see imports of dumped or subsidised goods.

The EU's anti-dumping regime is already the most liberal in the world. Rather than dismantling the current EU system, the Commission should concentrate on getting its standards applied by all its WTO partners.

Final Remarks

(SLIDE 9)

So, in conclusion, on balance crossing frontiers has been, and remains, a good thing. It is a core feature of the new steel industry environment. It has given us many challenges, some of which will be with us for many years to come. As an industry, we are responding to the opportunities presented by those challenges, but it is increasingly in the hands of the politicians to play their part in giving us a competitive environment that allows us to meet those challenges and win through.

That means:

- Encourage skills development
- Reform the EU's energy market
- Reform the EU Emissions Trading Scheme
- Maintaining a free and fair trade system

Thank you