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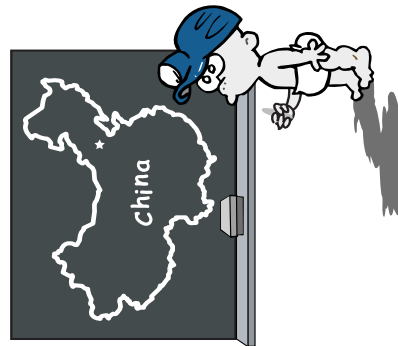
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Steel and the Price at the Pump

By Jim Stavis

Everyone has noticed and been alarmed at the high cost of filling up their gas tanks. It seems that retailers are raising prices on a daily basis with no end in sight. And as consumers, what choice do we have? Rapid transit?

The pricing policy for gasoline appears to be rather arbitrary and many believe to be collusion amongst the oil companies. But what is at work is the same dynamics that is now occurring in the steel industry.

With any commodity there are accepted prices. We get used to paying a certain price for a certain amount of... whatever. When that price rises too quickly we believe that some shenanigans must be taking place. The first effect you see is a rippling of price increases throughout the area. Different gas stations will adjust to the increase at different times. Nobody wants to gratuitously raise their prices, because that will send consumers elsewhere. Gasoline is, after all, a

(Continued Inside)

Steel and the Price at the Pump *(Continued from Front)*

commodity and retailers understand they must be competitive. Everyone who raises the price of gasoline has a good reason for doing so.

When a station buys a tanker of gas, they all pay about the same price for every gallon of it. Once they have bought it, the cost is immaterial. That price is history. The price they want to charge for that gasoline is the cost of the next tanker of gasoline. That's why prices rise so quickly, even before the next tanker arrives. If a gas station sells most of its gas at a lower price, it will have to dig deep to pay for the new tanker at the higher price.

Prices rise on bad news. If a station anticipates that the prices will rise in the future, then they will raise the current price. The worse the news, the higher the increase. Even rumors of bad news will cause the prices to increase. Price setting is always a gamble, a risk, a guess. You have to buy in the past and sell in the future. Anything can happen in the meantime. When there is a war in

Iraq, when refineries are having trouble, when Venezuelans are upset over their banking policy, when pipelines burst, the cost will rise.

None of this speaks to the demand portion of the equation. There are times of the year when gas volume must be increased because more people are driving (i.e. vacation months). This too will generate a rise in prices. The question is: what makes prices go down? Prices fall more slowly than when they rise. The fall in prices is a discovery process: how much will a retailer lower his prices and yet maintain volume? Lower them too far too fast and it will cause a price war and lower profits.

To many, steel is another commodity that has similar market dynamics at work. The raw material that the steel is produced from is not infinite in supply. The scrap and iron ore has risen in value, therefore causing the steel to be more costly to produce. Demand in others parts of the world (can you say China) has sucked a significant amount of tonnage away from the United States. Many steel mills have also disappeared from the scene due to

The China Syndrome

By Jim Stavis

Once again trade is a hot topic these days and now China and the effect it is having on the world trade balance is at the forefront. During the last months of 2003, there was a flurry of legislative action introduced in Congress to add tariffs on Chinese imports. What is driving the effort is the valuation of the Chinese currency in relation to the U.S. dollar. As the dollar has weakened in value,

bankruptcies and a weakened economy. This has created uncertainty in the marketplace that is fueling the price increases. The fear that prices will rise going forward and that supply will be short is what has caused the current increases. Prices will not recede until the uncertainty passes or demand decreases (whichever comes first).

For now, all we can do is try and understand or make some sense out of what is happening. Let's hope that we don't get to the point with steel as we did with gas, when we said "I remember when gas was only 19 cents a gallon." ■

the Chinese Yuan has increased. China has been reluctant to put currency revaluation on its agenda in spite of the meetings they have had with U.S. representatives. Revaluing the Yuan would expose a weak banking structure, massive unemployment and potentially disrupt China's most important economic engine—exports.

China has plans to increase its imports of U.S. products, including billions of dollars in

telecommunications, aviation and chemical equipment. But these numbers pale in comparison to the amount of goods and services flowing out of China. The U.S. trade deficit with China increased to \$103.2 billion for the first 10 months of 2003. At year end, that number should top \$130 billion. Steel and steel products increased year to year by 23.3%.

China's voracious appetite has created shortages in raw materials such as ferrous and non-ferrous scrap, coke, ocean shipping capacity and even electricity.

This is causing major repercussions around the globe as countries try to keep us with the changing trade dynamics.

Experts believe that China will soon end there decade old fixed exchange rate. Many believe it will happen by the end of 2004. Inflation from its booming economy and the fast pace of money and credit growth are major concerns. One economist predicted the change to occur by late October 2004—just in time for the U.S. election. Stay tuned. ■

