Iron Ore Market Outlook

Iron is almost the cheapest mineral in the world, but it makes the largest mining companies; CVRD, BHPH and Rio Tinto, all have substantial iron ore operations as their major revenue and profit contributor.

Like everyone else generally in this down cycle, the spot prices of iron ore have come down substantially from its peak due to the global recession. Unlike most other minerals, iron is not traded on the London Metal Exchange and does not have a futures market; its performance depends on sheer economics.

The outlook of iron ore is certainly tied to the global economic recovery, but one customer makes all the difference. China, produced about 20% of global steel in 2002, grew its volume to 500 mt (million tonnes) by 2008 representing 37.5% market share. When everyone is shrinking, China's share reached half of the global market in January 2009. China is the most important factor in the recovery of this sector.

China's economic problems are different from the rest of the world, though it has an export sector (25% - 30% of the economy) depending on the West. Its banking system has remained relatively intact from the financial crisis sweeping around the world providing a key stability in the system. Its key strength is its domestic consumption fire power from a growing massive middle class family population in the world's largest country by population. China's downturn is the result of a string of government fiscal and monetary policies designed to curb inflation and contain its bubbling real estate market in the last two years. With the exception a quite hard hit export sector, the fundamentals of the Chinese economy are comparatively in much better shape.

Following the governments around the world, China announced its US$600 billion economic stimulus package last November; however, all the money is going "into the ground" instead of rescuing crumpling financial institutions. With 38% of the package allocated to infrastructure, 25% rebuilding Sichuan (the earthquake zone) and 9% rural development, its total fixed asset investment comes to about US$450 billion. This should generate some 100 mt demand for steel or 150 mt of mill-feed grade iron ore over 2009 and 2010. This is very substantial considering China imported 444 mt of iron ore in 2008 representing roughly half of the global seaborne iron ore market.

In the short term, this China factor is expected to keep the 2009 iron ore contract price at about the 2007 level and the 2009 volume from a sharp fall. Over the long run when the multiplier economic impact of the package sets in, its steel industry should resume its substantial growth in a couple of years' time continuing the "super cycle" at a moderate pace.

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