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Putin at the Door

Ten years ago, China became a member of the World Trade Organization, subscribing to the various rules that govern the international trade practices of signatory countries. That step capped fifteen years of negotiations, the results of which were set out in a 900 page document. To celebrate the anniversary, the head of the WTO recently wrote that membership had materially aided China in making rapid progress in growing its gross domestic product, in modernizing the country and in raising workers' wages.

Whatever the value of the WTO to China, its value to other member countries has been more problematic. Over many of the years since 2001, the Chinese have taken a variety of measures to assure that its currency is undervalued, a tactic that is equivalent to granting an export subsidy to every one of its products that is sold abroad. Of course, export subsidies are prohibited by WTO rules. On another front, the Chinese have done very little to address their massive production of counterfeit and pirated products that undermine sales of genuine products world-wide.

On balance, therefore, the optimism that accompanied Chinese accession has not been realized.

Now comes Russia to the WTO.

Just last week, after 18 years of negotiation, the WTO accepted Russia's application for membership. The accession is accompanied by 30 side deals with individual countries on trade in services and 57 such agreements on trade in goods.

Given the experience with China, should we have only modest expectations for Russia? First of all, the agreement will result in fairly small reductions of Russian import duties, from 9.5% on goods and from 13.2% to 10.8% on agricultural products. (By comparison, the average U.S. tariff rate in 2010 was 1.3%.) Moreover, for two-thirds of imports, the reductions will be phased in over three to seven year periods. Initially, none of these reductions would be granted to U.S. products, since for many years, we have denied Russian products most favored nation treatment because of the "Jackson-Vanik Amendment" requiring Russia to permit Jewish emigration. Modifying that amendment will be considered by Congress next year.

But, beyond the issue of tariff parity, one must question whether Russia will be able to curb its willingness to blatantly use trade measures for political objectives. The accession agreement was held up for some time by concerns of Georgia about trade between the two countries. That dispute was resolved by agreement that a Swiss private company would oversee the border trade, an extraordinary surrender of national sovereignty over the collection of taxes.

Even more daunting may be Russia's use of its energy exports to coerce neighboring countries and even those in Western Europe to hew to its demands. Does anyone think that Putin will be deterred during those kinds of disputes by provisions in the WTO rules?

Finally, there is the issue of human rights in Russia. This has been a bone of contention between the West and the Russians for many years, but there is a distinct possibility that matters could escalate if the protests against Putin's power grab during the recent parliamentary election grow into a continuing movement like the Arab Spring. If things get out of hand, other countries might well consider imposing the kind of trade sanctions imposed against Libya and Syria.

It might be argued and may be true that the WTO would provide a dampening effect on Russia's politicization of trade, but history has not shown that international undertakings are high on the list of considerations for Russian policy makers.

Here are the trade data for this month:

- Scrap and Pig Iron After dipping a bit last month, the prices for #1 dealer bundles and #1 busheling (Chicago) returned to their October levels of \$495 and \$500 per mt., respectively. Prices have hovered around those levels for the past twelve months. The spot price for Brazilian pig iron (cif New Orleans) remained unchanged at \$498 per mt.
- Natural Gas The Nymex contract price continued to ease, by a dime this month, to \$3.45 per mmBtu. This runs counter to the usual price movements in December, and it may reflect the continuing growth in supply from new extraction techniques.
- Ocean Freight The Baltic Capesize Index was up by about 20% this month to 3695. After eight months of very low levels from the beginning of the year through August, the last four months have reflected a 50% to 75% increase, likely due to increased demand.

- Exchange Rates The euro has been battered by the EuroZone crisis. The UK tossed a spanner into the works with its refusal to join all other EU countries in supporting a plan to address the problem. At this writing, the euro is at \$1.30, down a nickel from last month and almost a dime from the month before. The pound is off a penny at \$1.55, and the Canadian dollar was unchanged at \$0.96.

We want to close 2011 by sending you and your employees our sincere best wishes for a warm holiday season with your families and friends and for a happy and prosperous New Year. This year has been fraught with many problems, but good things have happened, too, and we must hold to the optimistic belief that our great country can, as it always has, surmount our problems.

As usual, we are posting this letter on our website, www.coreysteel.com and on the international site, www.steelonthenet.com.