



State Must Demand Investment for Sparrows Point

By Jay Hancock

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To last another century, the Sparrows Point steel mill needs maybe \$1 billion invested in new equipment or an act of God that moves Baltimore closer to Detroit and the manufacturing customers there.

Which event is more likely to occur is debatable.

Ira Rennert, whose Renco Group has agreed to buy Sparrows Point and two other mills owned by Severstal North America, does not have a reputation as a big spender. (On his companies. What he spends on himself is another matter entirely.)

So Sparrows point, which has been bought and sold like a garage-sale Beanie Baby, could have its fifth owner in a decade within a few weeks. Maryland politicians are exultant. Analysts expect Sparrows Point under Renco to rejoin the economy after having been largely idle since the financial crash.

But the pols should be very careful about offering Rennert training money or anything else until he demonstrates that he's ready to give Maryland as much as he takes.

Don't be impressed by the announced sale price of \$1.2 billion for the three plants. That's about half what Severstal paid.

And much of the \$1.2 billion is not hard money. That's the Renco way. Severstal gets \$125 million in cash and another \$317 million in debt paid off. The rest is seller financing from Severstal and \$650 million in "employee-related and environmental liabilities."

Rennert has made a career out of trying to avoid pension and environmental liabilities, in bankruptcy court and out. Analysts will be surprised if he ends up owning Sparrows Point much longer than the mill's other recent proprietors.

"Obviously, they walked away with a good deal" in buying the plants, says steel analyst Michael Locker of New York City-based Locker Associates. "When the market improves, which it will in a year or two, they'll sell it."

Renco spokesman Andrew Shea declined to comment on the company's plans.

If the steelworkers aren't much focused on the long term, either, don't blame them. Hundreds have been out of work. They're embracing Renco. The Russian Severstal, which bought Sparrows Point in 2008, has invested little money in the facility and half-mothballed it since the steel-market collapse two years ago.

To seize on higher prices and a slowly recovering economy, Renco is expected to restart Sparrows Point's hot mill and possibly relight its blast furnace, which converts ore into metal. Hot rolled steel, which fell below \$350 per ton in 2009, has popped past \$700 in recent weeks.

Give credit to stronger North American demand and less steelmaking capacity, thanks to closures over the past decade. At the same time, a weaker dollar and Chinese inflation are making American steel more competitive against imports.

Another positive: I heard nothing but good things from industry insiders last week about John Goodwin, whom Renco has hired to run Sparrows Point and former Severstal mills in Ohio and West Virginia.

But even in the short term, Goodwin's job will be challenging. Sparrows Point, built a century ago by Bethlehem Steel, needs millions in working capital to restock its input materials -- steel slabs and iron ore. Costs for both have soared, which will crimp profit margins despite higher prices for finished steel. Competitors own ore mines, which gives them an advantage. Renco doesn't.

The market for construction steel, Sparrows Point's sweet spot, is still softer than baby bunnies. And Goodwin might not realize how much talent has drained out of the mill. The people who know how to run the machines are getting other jobs and may not be coming back.

The bigger challenge, however, is the long haul.

Analyst John Anton at IHS Global Insight in Washington paints a seductive picture, in which a falling dollar and stronger Chinese yuan will give American steelmakers their biggest boost in decades.

"The dollar is weak. It's going to get weaker," Anton says. "That'll simply choke off imports. It will really help not just Sparrows Point but every other steel mill in the United States. It actually means that the U.S. will need more capacity."

But to fully join the party, Sparrows Point needs hundreds of millions of dollars in capital investment. Its blast furnace may need relining as soon as 2014, at a cost of \$200 million or so. Because of the planning and financing involved, that decision might need to be made as soon as next year, says steel analyst Charles Bradford with New York-based Affiliated Research.

Sparrows Point should also replace its aging and too-narrow hot mill, at a cost of millions more. A new hot mill would let it sell automobile-quality steel to Detroit and the assembly plants of the South.

But neither investment is a sure thing. Steelmakers have been pinning their hopes on a weaker dollar for decades.

And while Sparrows point's deepwater port is a big plus, the factory's distance from auto plants is not. Thanks to more expensive fuel, it costs almost as much to send a ton of steel to Chicago these days as it does to China. Rivals close to car factories in Michigan and Alabama will have an edge even if Sparrows Point builds a new hot mill.

There is also the environmental challenge. Do you spend millions upgrading a blast furnace when carbon dioxide regulations could soon make it uneconomical?

Besides, how will Ira Rennert maintain a lifestyle that includes what Vanity Fair magazine reported is the largest private residence in America -- a 29-room, 40-bathroom Versailles in the Hamptons on Long Island -- if he has to upgrade a plant in Maryland?

The state stands "ready to help" Renco "return, retrain and retain nearly 2,000 steelworkers in Sparrows Point," says Gov. Martin O'Malley.

Slow. Down. Governor. Maryland should give Rennert nothing until he commits to build Sparrows Point for the long term.
