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New steel firm was forged on failures

By Connie Mabin
The Associated Press

CLEVELAND - As the giants fell, International Steel Group Inc. began picking up the pieces: Acme. LTV. Bethlehem. Today, the upstart is the second-largest integrated steel producer in North America.

In the year and a half since it was formed, privately held ISG has made a name and fortune buying bankrupt steel companies for bargain prices, cutting costs and reinventing the companies to produce more steel cheaper than nearly anyone else in the United States.

Now the business world is watching as the company prepares to go public at a time when even more steel companies are crumbling. ISG's $250 million initial stock offering - the company won't say when it will come - will either solidify the steel maker's mark as one of the industry's heavyweights or set it up for the kind of fall it's made its riches from.

Industry experts say ISG's ability to succeed in tough times makes it attractive to potential investors.

"It showed the way and most people were convinced that there was no way," said Mike Locker, president of Locker Associates Inc. in New York and author of the *Steel Industry Update Newsletter*.

Bucking steel tradition, ISG pulls back production when it needs to, preventing an abundance of product that pushes prices lower. It keeps costs low by having every worker do every job in the mill instead of specializing. Management was thinned out, getting the powerful United Steelworkers of America on board with ISG.

Mark Granakis, president of Steelworkers Local 979, said the ISG contract is landmark because of the friendly tone it sets.

Employees now have a say in day-to-day operations and an interest in ISG's success: They get profit-sharing checks at the end of each financial quarter.

"It's a pleasure to go into there to solve problems instead of filing grievances," Granakis said.

"We want to see the company succeed obviously for our own security but in addition, make a lot of money so they can share that money with us."

Analysts say the friendlier labor relationship is a big plus for ISG.

"They are setting a new pattern in this industry, an industry that is in grave distress," Locker said. "Why didn't it happen earlier? I don't know. It should have happened earlier. I think more importantly, it happened."

Leo Gerard, USWA president, said the union appreciates ISG Chairman Wilbur Ross' creative approach despite the pain that sometimes accompanies it, such as dumping pensions and benefits for 82,000 retirees when the company took over LTV.

"ISG and Wilbur Ross, in particular, provided an opportunity to revitalize a company," Gerard said in an interview.

Although the two sides don't always agree, the union likes Ross' open-door policy, his demands that management have an occasional after-work beer with shop workers and his battle for protective steel tariffs.

Ross said he was unable to answer any questions about ISG because of the company's application with the Securities and Exchange Commission to go public.

Profits and losses

Filings with the SEC show ISG posted a $58 million operating profit for the first half of this fiscal year, despite a first-quarter loss of $1.6 million on net sales of $461.7 million. The loss was due to ISG's first payments to the USWA's pension fund and one-time costs related to setting up inventory at new plants.

The nation's largest integrated steel maker - U.S. Steel Corp. of Pittsburgh - lost $87 million in the first half, in part because of higher pension and natural gas costs.

Integrated steel is made from raw materials rather than recycled metals.

Granakis said rank-and-file employees have mixed feelings about ISG's plans to go public. They realize it's a good way to make money to invest in the company.

"But I am a little skittish about the corporate-level relationship with workers," he said. For example, he's worried that he no longer will be able to call Ross whenever he wants.

In the SEC documents, ISG lauds its relationship with the union.

The company also says it wants to keep adding to its arsenal, started in April 2002 when WL Ross & Co. LLC purchased steel giant LTV Corp.

Acme Metals Inc. of Riverdale, Ill., and heavyweight Bethlehem Steel of Bethlehem, Pa., were next. Based in suburban Richfield, ISG has acquired plants in 10 states.

Since 1997, 41 steel companies have gone bankrupt. Every time a bankruptcy is filed, speculation swirls among companies, workers, analysts and investors that ISG is waiting in the wings with its checkbook open.

Not every struggling steel company is anxious for an ISG buy.

West Virginia-based Weirton Steel Corp., the nation's fifth-largest integrated steel producer, sought bankruptcy protection in May after racking up more than $700 million in losses over five years.

The company, which employs many Ohioans, has acknowledged it's been in sale talks with ISG, but it's also been vocal about its desire to remain an independent producer.

Advocate of tariffs

Ross has loudly defended the three-year tariffs President Bush imposed last year on foreign steel after it flooded the market at prices below the cost of production. ISG was able to reopen LTV in Cleveland with a boost from the tariffs.

ISG is viewed as a pioneer because of its move to consolidate an industry saturated with high-cost, struggling companies into a handful of low-cost businesses, said Dan Ikenson, a steel trade policy analyst with the Washington, D.C.-based Cato Institute, which advocates free trade.

That makes Ross' support of the tariffs surprising, Ikenson said, because without the taxes, more companies likely would have gone bankrupt sooner, and ISG could have bought them at bargain prices.

What happens with the tariffs will affect steel's future, but it's not the most important thing ISG must focus on while going public, Locker said.

Investors will be looking for ISG to pay down its $750 million in debt and put money earned from the stock sale back into the company, he said. How much steel China buys from the United States next year also is key, Locker said, because an expected increase could mean millions in profits.

China is expected to consume 300 million tons of steel next year, Ikenson said. That's compared to 120 million in the United States.

According to the SEC filings, ISG would have to use half of the proceeds from the stock offering to pay on its loans. The other half would be required to go toward debt or general corporate purposes.

Some on Wall Street have voiced concern about ISG's debt, but Locker said it's not as huge as the debt steel companies have traditionally carried.

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