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FEATURE

U.S. Steel Shares Could Rise 50% in a Year

Battered by China and high costs, U.S. Steel is fighting back. It looks like a good bet for certain investors.

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By JACK HOUGH
October 15, 2016

The U.S. has become a relatively minor player in the global steel market. *Photo: Mark H. Milstein/Bloomberg News*

China is "dumping vast amounts of steel all over the United States, which essentially is killing our steelworkers and our steel companies," said Donald Trump on Oct. 9. True, said Hillary Clinton, "and Donald Trump is buying it to build his buildings."

During a second presidential debate that mostly resembled a circus bear pawing a beehive, that exchange qualified as chummy agreement. It's why risk-tolerant investors should consider a gamble on United States Steel (ticker: X). A backlash against predatory Chinese trade practices helped send the stock from $8 at the end of last year to $27 by the end of July, as steel prices jumped 50%. Those prices have given up some of their gains since then, and the shares are back to $16.42. From here, they could rise 50% or more over the next year as U.S. Steel continues pushing for fair play while slashing its costs—and renewing supply contracts at now-higher steel prices.

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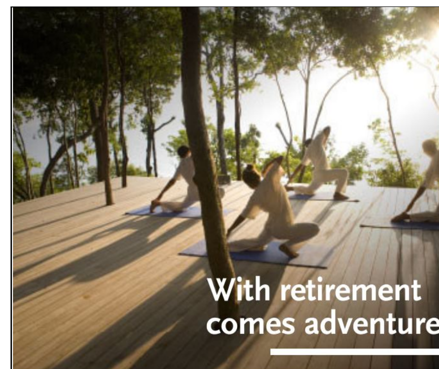
We call the shares a gamble for a reason. Wall Street analysts have 18 different price targets on the stock, ranging from a high of $37 to a low of $7. (The average is $20.75.)



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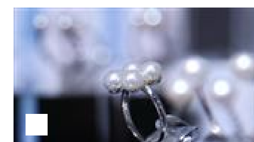

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Statistically, only one company in the Standard & Poor's MidCap 400 index has a more scattered range of predicted returns: struggling oil driller [Denbury Resources](#) (DNR), with a share price below $3.

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One reason is the recent volatility in steel prices. Another is that U.S. Steel, for now, has relatively high costs and low margins. It relies on blast furnaces, which have high but inflexible steel-making capacity. And it's too dependent on commodity products, especially now while a key market for more lucrative specialty steel, the oil industry, is slumping. A rebound in prosperity for U.S. Steel could spark a virtuous cycle, whereby the company gradually invests in nimble electric arc furnaces to help it better control output, and shifts to making more high-value steel, while quickly paying down debt and shoring up its pension.

The result could be a blistering pace of improvement. Consider the forecast of Curt Woodworth at [Credit Suisse](#), who is bullish and then some with a $29 price target. He

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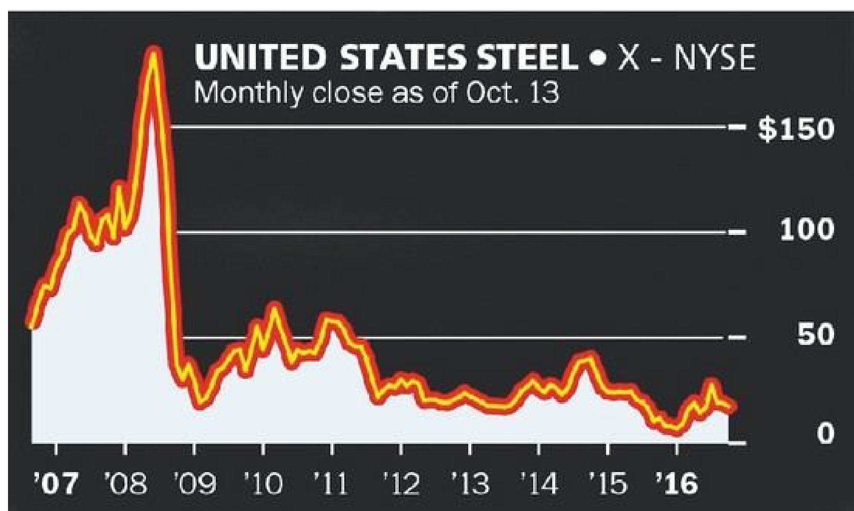
These are massive swings for a company with a market value of $2.7 billion, or less than four times Woodworth's 2018 earnings estimate.



Source: Thomson Reuters

Self-help will be one key. Brazilian-born Mario Longhi, who joined U.S. Steel in 2012 and was named chief executive a year later, launched an efficiency drive that year called the Carnegie Way. Last year, it delivered $815 million in savings. Details are few, but cutting output and head count clearly plays a part. After a round of layoffs this year, U.S. Steel has about 20,000 workers in North America, down from 29,000 eight years ago—and hundreds of thousands immediately following World War II. Eventually, says Longhi, he wants to earn the right to grow again. That will mean standing up to China.

That U.S. Steel is part of an index for midsize companies—it was dropped from the Standard & Poor's 500 in 2014—speaks to its diminished scale. The Pittsburgh company that once controlled two-thirds of the U.S. steel market today is second in share to Charlotte, N.C.–based [Nucor](#) (NUE). But more important is that the U.S. has become a relatively minor global player. China now produces 50% of the world's steel, up from 13% in 1996. Its furnaces made 10 times as much steel as the U.S. last year.

"China doesn't play by any proper trade rules," Longhi told *Barron's* last week. "We're going after them, and we're getting results." Of the 804 million metric tons of steel China made last year, an estimated 40% was overproduction. Even as China's economic growth slows, its companies have been reluctant to cut steel capacity, under what critics see as government pressure to avoid layoffs that could create unrest. So China has been dumping loss-making steel in the U.S., an unwinnable situation for U.S. steel makers. Under pressure from trade groups, China promised to cut 100 million to 150 million tons from production over five years, but has shown little progress. Total U.S. production is about 79 million tons per year.

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EARLIER THIS YEAR, U.S. STEEL and other domestic players scored a victory when the U.S. Department of Commerce hiked tariffs on some Chinese steel products to punitive levels of more than 500%. In the U.S., one domestic steel benchmark rose from $391 a ton at the end of last year to over $600 by summer. But imports have remained elevated, and steel has recently dipped below $500 a ton.

Longhi says China is circumventing U.S. laws by shipping cheap steel to Vietnam, relabeling it, and then sending it to U.S. buyers. He also accused China of hacking the computer of a U.S. Steel scientist who was developing a new type of high-strength steel to compete with aluminum in cars and other products, perhaps even military vehicles. Newly signed legislation should close the Vietnam back door, and more trade cases are pending. There could be more than U.S. jobs at stake. “Steel-making is a matter of national security,” says Longhi.

The Bottom Line

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down shares, recently $16.42, could rebound to $25.

The $37 price target is held by JPMorgan 's Michael Gambardella. He argues that China has begun to reduce steel capacity, and that U.S. Steel’s profits should rise quickly as its supply contracts expire and new ones factor in this year’s higher steel prices. His target is based on the company fetching its historic average of 5.8 times estimated earnings before interest, taxes, depreciation, and amortization by December 2017.

Morningstar has the $7 target, or “fair value estimate.” Its rationale? The stock is probably worth zero, but there’s a 25% chance that things could go well, in which case it’s worth $28, or 71% more than its recent price. All told, this is not a stock for little Suzy’s college fund. But for risk capital, the payoff could be—to borrow a term from a businessman turned politician we know—big league.

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Frederick A. Green Oct 19, 2016

U.S. Steel Shares Could Rise 50% in a Year

They could also fall by 50% in a year.

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Frank Anderson Oct 17, 2016

The stock just as easily drop 50%. Barron's has gotten as bad as comedy central (cnbc) about hyping the bull.

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Bernard Diggins Oct 16, 2016

Barrons darn near said Trump was right about something. Shocking this article got past the editorial board.

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John Goscinski Oct 15, 2016

Totally moronic analysis by the bulls. It only reafirms my belief never to rely on an analyst's opinion for any stock in any indutry.

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shivam airon Oct 15, 2016

i am not sure how the analyst come up with price target.? t\The cost of steel will stay @ or around 1.00 dollar? .Further, the production cost of USS is 25%-35% higher than those of Chinese. We all know that share can rise only when the profit increases. I would like to know if USS will see earning increase in coming years that would boost its share price by 50%?

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Fred Jablonski Oct 15, 2016

@shivam airon Actually if the markets are going to "correct" from the FED increasing rates in December why not wait until everyone simply heads for the exits and consider it then.

Right now the market's in "wait and see" mode.

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