



## Entrepreneurs Men of Steel

By Emily Lambert

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Four years ago Esmark didn't exist. Now it's out to transform the U.S. steel industry.

On the face of it, Wheeling-Pittsburgh Corp.'s shareholders meeting on Nov. 17 seemed a polite affair. You'd hardly know that an audacious, hostile grab for control of the steel company was taking place behind the scenes. Outside Wheeling Park's White Palace Ballroom in Wheeling, W.Va., Craig Bouchard, president of the little-known, closely held Esmark of Chicago, was frantically calling large investors, pulling off a long-shot coup. His competitor, a Brazilian steelmaker seven times Esmark's size, had the support of Wheeling-Pittsburgh. But within 22 minutes, thanks to weeks of lobbying, Bouchard had turned the tide, winning 69% of the vote.

In four years Craig, 53, and his brother James, 45, have welded together what will soon be a \$3 billion-plus (sales) company. They aim to transform the industry by reviving a business model--a steel mill that distributes its products--that failed in the U.S. two decades ago but still works overseas. Esmark now consists of nine distribution companies that buy cold-rolled coil and sheet, slice it up and sell it. Assuming the merger goes through, Wheeling-Pittsburgh gives the brothers their first steel mill, along with likely headaches. Unlike, say, Wilbur Ross, who had quick success rolling up broken steel companies by slashing production costs, the Bouchards say they'll order no layoffs among the 2,600 employees (out of 3,100) who are unionized. Still, vows Jim, Esmark's chief executive, "We can build the most profitable steel company in the U.S."

These guys know the business. Their dad, Robert, was a sales manager for Inland Steel, now part of titan Arcelor Mittal; their mom was an assistant at Inland. Jim worked there, too, as a service rep, before becoming a vice president for U.S. Steel, restructuring a plant in Slovakia. Craig headed up derivatives trading at First National Bank of Chicago, then cofounded a risk-management software outfit, but he took an interest in 2003, when Jim said he wanted to return from Eastern Europe. Why not pick up on the cheap a few of the 4,000 distribution centers in the U.S.? Some of these wholesalers were sickly and could be had for 90 cents on the dollar of net assets. The Bouchards figured they could run them better, with, for instance, only two months of inventory, while focusing on customers that were less cyclical than auto and appliance makers. They settled on a 500-mile radius from Chicago. "Some people say dead zone, we say growth corridor," Craig says.

The first deal came out of their own pockets. In June 2003 they paid \$2.4 million for bankrupt Electric Coating Technologies in East Chicago, Ind.; its zinc-coating equipment was worth \$100 million. After Jim leaned on friends to become customers, ECT ended the year with \$1 million in operating income (earnings before interest, taxes, depreciation and amortization) on sales of \$8 million. In February 2004 the Bouchards mortgaged their homes and hit up family and friends to buy distributor Sun Steel in Chicago Heights, paying \$11 million for \$13 million worth of assets, including \$9 million of inventory and receivables. By rearranging production, adding new truck docks and persuading the union to drop morning and afternoon breaks, Jim hauled in \$13 million in operating profit in 2004. Thanks to such acquisitions, Esmark cranked out a \$19 million Ebitda on revenue of \$413 million in 2005.

In 2005 the brothers hunted down some equity capital (Esmark has no debt). The Franklin Resources mutual fund operation kicked in \$115 million for 65% (now 72%) of Esmark's shares, distributed among 11 Franklin Mutual Series funds. (The brothers own 25% of Esmark.) They used cash to buy another seven service centers in the Midwest.

Wheeling-Pitt is a different order of beast. The 86-year-old maker of flat-rolled and fabricated steel products has been in the dumps for a quarter of a century, in and out of bankruptcy since 1986. In 2005 it lost \$34 million on \$1.6 billion in sales; last year, through the third quarter, it broke into the black but forecast a losing fourth quarter. Because it still relies on an old, inefficient blast furnace, it remains the highest-cost steel producer in the U.S.--\$23 operating profit per ton versus \$85 for the industry.

Why go to all this trouble? The Bouchards are convinced that the old mill-cum-distribution model still has life in it. Even streamlined old companies had high labor costs and leaned on blast furnaces, which couldn't be shut off easily and, so, led to overproduction. Esmark will rely on an electric arc furnace that can quickly be switched off as demand and prices fluctuate. Today, says Craig, costs are down (Esmark is less than half unionized) and operating margins run 8% to 10%; efficiencies and retirements, he argues, will reduce manpower per ton over the next five years.

A union executive from Wheeling approached Jim in 2004, figuring Esmark could provide ready customers and the mill could offer a steady supply of steel. In April 2006 Esmark made an unsolicited offer of \$450 million (including \$200 million from Franklin), or \$20 a share, a 4% premium to the market price. By then \$4 billion (sales) Companhia Siderúrgica Nacional, the Brazilian steelmaker, had proposed to merge its North American assets with Wheeling-Pitt, giving Wheeling shareholders 50.5% of the combined company. It also offered to invest \$225 million as convertible debt, which, once converted, would dilute the shareholders' stake to 36%. The Bouchards' no-layoff promise helped win union support. But Wheeling's board liked the boys from Brazil.

The competing suitors raised their antes--and their fists. After Wheeling-Pitt announced it would align with CSN, Esmark threatened a proxy fight against the board and offered shareholders the chance to buy up to \$200 million worth of stock in a merged Esmark-Wheeling entity. CSN then offered \$30 a share to shareholders who cashed out after four

years. Each side met with investors and mouthed off in press releases and securities filings. Institutional Shareholder Services, with plenty of throw weight to move big investors, initially backed Esmark. Yet two days before the Nov. 17 vote, after CSN considerably sweetened the pot, ISS split the baby, endorsing the Brazilian deal but supporting Esmark's board, which had union backing.

The night before the meeting executives from both companies called shareholders, trying to win them over; the outcome was a toss-up. Craig says he called one "top five" investor who controlled 1 million-plus shares. "We made them a promise that we would make this company a great investment for them," he recalls. An hour later Esmark won those votes. Another round of calls during the meeting cemented Esmark's victory.

Now, as they say, for the tough part. While they're bringing in an experienced group, the Bouchards have never run a mill before. Even success could trigger untenable demands for fatter paychecks from the union. Bring it on, says Craig: "This is about personal relationships." Not to investors it isn't.