

Consensus and Conflict in the Steel Market

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Key Words: Investment Policies, Competition, Imports, Minimills, Trade Interventions, Subsidies

### **INTRODUCTION**

Global steel consumption has been on a slow upward trend since the mid-1970s. Cyclical fluctuations around this trend have been a major cause of international trade friction. With the entry of more steel-producing nations into the global arena, this friction deteriorated into conflicts whenever the U.S. steel market came under severe pressure from imported steel. Mounting structural obsolescence and regional concentration of the U.S. steel industry's integrated sector, as well as the frequently overvalued U.S. dollar, facilitated the market entry of both imports and of new domestic competitors, the so-called minimills. After taking most of the bar, rod, and sections markets, the minimills began to invade flat product markets with help from newly developed technologies. The integrated producers have been further handicapped by assuming generous pension and healthcare obligations, now called "legacy costs." This extra burden has been a major cause of bankruptcy in that industry sector. Last year, abysmally low prices, mounting company losses, and a rash of bankruptcies have moved imports and legacy costs into the political limelight. While all factions of the steel industry, the labor unions, and their supporters in Congress reached a consensus that additional barriers be raised against imported steel, sharp divisions emerged on the issue of government assistance with the burden of legacy costs. Removal of this burden is essential for the integrated mills to improve their competitive position and merge into larger, more efficient units.

### **THE TURBULENT GLOBAL MARKET**

Global steel consumption expanded at a rapid six percent rate from 1950 to 1974, but at a much slower rate of 1.1 percent since then. Even that slower rate was far from steady. Consumption dropped as much as 60 million tons within a two or three year period, only to set a new record several years later. The rate dropped to 0.4 percent in the 1980s, but then moved up to 1.5 percent in the following decade.<sup>1</sup>

Market downturns are often accompanied by severe turbulence in trade relations. Although globally recognized trade rules have been established, no consensus has as yet been reached concerning their interpretation. Unstable exchange rates and regional financial crises continue to upset international trade flows and provoke conflicts among trading nations, as we have seen during the past four years. Indeed each consumption dip--in the mid-'70s, the early '80s and '90s, and again after the Asian financial crisis of

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\* This paper was presented in a preliminary form on March 11, 2002, at the 85<sup>th</sup> Steelmaking and 16<sup>th</sup> Ironmaking Conference of the Iron & Steel Society, held March 10-13, 2002, in Nashville, Tennessee.

1997/'98—triggered a flood of trade-law petitions from steel producers seeking protection from imports, both in the United States and abroad.<sup>2</sup> National steel industries have also put increased pressure on their governments for direct intervention via quotas, tariff quotas, tariffs and, more recently, the safeguard clause (to curb import surges). In contrast, trade relations usually take a turn for the better during upswings of the business cycle. Unfortunately, during such times of relative harmony the seeds are sown for renewed discord, as steel producers in many parts of the world develop a tendency towards excessive optimism. It only just takes a few years of good financial performance and they launch ambitious expansion projects that, in the aggregate, tend to overshoot future market needs.

**Table I Global steel consumption for 2000 and estimates for 2001 and 2005 (million metric tons●)**

Year	2000	2001	2005
Americas	<u>173</u>	<u>158</u>	<u>178</u>
NAFTA	146 *	131 *	146 *
(of which USA)	115	103	122
South America	27	28	32
Europe	<u>180</u>	<u>175</u>	<u>180</u>
EU of 15	145	142	145
Other Europe	35	33	35
CIS	30	32	35
Asia	<u>315</u>	<u>315</u>	<u>357</u>
China	118 **	122 **	155
Japan	76	73	72
Other Eastern & Central Asia	121	120	130
Other Regions	<u>38</u>	<u>40</u>	<u>43</u>
Africa	15	16	16
Middle East	16	18	20
Australia/New Zealand	6	6	7
World	736	720	793

Sources: IISI and own estimates.

Notes: \*Trade among NAFTA member nations was excluded. \*\*Based on World Steel Dynamics data.

●Steel consumption data are in terms of rolled or finished steel mill products.

Since the end of the Second World War, global steel trade has generally flourished, rising from 25 million short tons (mt) in 1950 to 200mt in 2001, not including trade within the European Union.<sup>3</sup> There have been no major trade disruptions, or threats of disruptions. With the exception of a short period in the 1970s, steel has been available in sufficient quantities and for the entire gamut of grades and dimensions required by steel users around the world. Large additional quantities of steel came on the global market following the collapse of the Soviet Union (now known as the CIS). Many developing nations and China relied heavily on imported steel to sustain their industrialization efforts. However, rising demand in the second half of the 1980s and especially the boom of the '90s caused many of those nations to pursue a policy of becoming more self-sufficient in steel. Even countries lacking basic steel-making resources undertook expensive greenfield projects.<sup>4</sup> During times of

political upheaval, the desire for assured supplies is no doubt a valid reason for gaining some degree of national self-sufficiency. Latin American nations learned this the hard way during two World Wars, when their fledgling manufacturing industries were cut off from most of their foreign sources. However, as noted, not only have there been no threats of total trade disruption in recent decades, but steel has generally been available in ample supply and at relatively low prices. Many of the mills constructed to achieve steel self-sufficiency had trouble achieving profitability which, predictably, led to calls for protection from imports. Additionally, whenever local consumption weakened, attempts were made to push excess domestic production into foreign markets, including those of the United States and Western Europe.

In cyclical markets, the occurrence of excess capacity and low prices during a downturn should not be a cause of concern as long as the losses suffered in slow periods are offset by higher prices and earnings during economic booms. But that is not what happened during the last 25 years. What has marred such a balanced outcome over the longer term was the entry into the global market of too many producers that had neither the experience nor the raw material support to become globally competitive suppliers of steel.

To some extent, the accelerated build-up of steelmaking capacity in China deserves a similar comment, because it takes place behind a curtain of artificially high prices. Data collection in China is not yet fully reliable and consumption statistics coming out of that country are probably inflated by at least 10 percent.<sup>5</sup> Because China is the world's largest steel-producing and consuming country, these inflated data lend an upward bias to the steel consumption forecasts issued periodically by the International Iron and Steel Institute (IISI). In view of the respect these forecasts enjoy among the world's steelmakers, they may have encouraged capacity expansion by companies intent on preempting their share of a presumably growing world market.

## **THE CHANGING U.S. STEEL MARKET**

### **Delayed Basic Restructuring Of The Integrated Steel Sector**

Immediately following World War II, the United States was the undisputed leader in steel production, accounting for nearly two thirds of the world's raw steel output.<sup>6</sup> Despite its huge size, the U.S. industry had quite a few small and aging integrated plants. Hemmed in by rivers, hills, and urban growth, these plants were difficult to expand and modernize. This would have been a good time to shut down these obsolete, poorly located plants and channel available funds into more promising capacity. However, pent-up civilian demand and the military requirements of the Korean War put pressure on the industry to expand in a hurry. President Truman even invited West European exporters to help alleviate the tightness of the market. The building or rebuilding of steel capacity in Europe, the Soviet Union, Japan, and elsewhere gradually reduced the American share of global output to 40 percent in 1955, 20 percent in 1970, and 12 percent last year.

While the industry added almost 50 million ingot tons of capacity during the 1950s, most of this came from the expansion of existing plants. Considerable amounts were spent on plants that were originally constructed decades previously and as a consequence were undersized, poorly laid-out, and often not well located as markets shifted toward the West and South of the country. Only one new plant was built, the U.S. Steel Fairless works in eastern Pennsylvania, with a capacity of about four million tons. Another new plant, Bethlehem's Burns Harbor works, was constructed in the following decade on the southern shore of Lake Michigan, where other companies were already operating several large plants. Generally, throughout the 1960s and most of the '70s, the U.S. integrated steelmakers industry continued their policy of spreading investment funds for technological modernization and environmental protection over a large number of plants. It would in any case have taken extraordinary stamina on the part of management, except under crisis conditions, to shut down old plants that were located in isolated regions and supported entire communities. Such closures, which always provoke vociferous protests from union officials, local politicians, and members of Congress, became easier when they could be blamed on foreign trade practices.

### **Long Term Effects: Higher Unit Costs and Lost Market Opportunities**

Modernizing and “de-bottlenecking” existing plants was an inexpensive and quick way to add more capacity. But over the longer term, it pushed both investment and operating costs above those of new plants incorporating the latest best-practice features. Absent an investment strategy focussing on long-term efficiencies, expenditures were wasted on the perpetual rounding out of sub-optimal facilities, many of which had to be shut down anyway during subsequent recessions. By 1980, the U.S. industry had 14 integrated plants in the 1-2mt size range, compared to only one in Japan, while it operated four plants with a capacity of more than 6 million tons, versus 12 in Japan.<sup>7</sup> All the large plants in Japan had modern straight-line lay-outs and deep-water access for both raw materials and finished products. Most Japanese as well as European producers had installed new American-designed equipment that was capable of turning out steel of more consistent specifications than many of their U.S. counterparts.

The conservative investment policy of the integrated U.S. producers had another negative consequence, an excessive concentration of steelmaking capacity in the country’s northeastern quadrant. Newly emerging markets in the West, Southwest, and part of the South were to a large extent neglected, except during recessions when demand in the mills’ home market had weakened.<sup>8</sup> These neglected markets offered good picking for offshore competitors as well as for the domestic minimills that had sprung up in all regions of the country since the early 1960s. Both groups offered their customers more reliable and often lower-cost supplies than the integrated mills in the eastern and mid-western states. In sum, the integrated sector’s conservative investment policy--it can hardly be called a strategy--had the result of freezing outdated structural features into many of its plants and clustering too much capacity into one region of the country. It left a lasting negative imprint on the sector’s global and domestic competitiveness and represents one type of “legacy-cost” that detracts from company performance, although not as much as the onerous obligations to retired steelworkers.

### **Costly Deals With Labor**

Ever since the end of World War II, steel managers have been engaged in an endless tug-of-war with labor unions, chiefly the United Steelworkers, over demands for higher wages and added fringe benefit as well as for more union control over the work place. The U.S. government occasionally entered the fray by putting pressure on the companies to come to terms with the union rather than risk a strike that could disrupt the economy. The government also took to “jawboning” to rein in price increases exceeding estimated growth in worker productivity.<sup>9</sup> The combination of union power and government partiality added to the cost pressure on the companies. Steel industry observers began to wonder just how long the integrated mills could continue to pay among the highest wages and fringe benefits in the manufacturing sector and, at the same time comply with the union’s system of work rules.

With their backs against the wall, the steel producers turned to the union for concessions.<sup>10</sup> The USW reluctantly agreed. But as a trade-off for those concessions the USW demanded long-term benefits in the form of improved pensions and healthcare plans. Eager to assure their survival, steel companies grasped at the offer. One could blame the union for relentlessly squeezing the companies during their darkest hour, wrenching concessions from a weakened industry to grant retiree benefits that far exceed the level enjoyed by most retired persons.

Today, the term “legacy cost” is generally reserved for the huge obligations that unionized steel mills incurred to finance generous retiree pensions in addition to healthcare plans that had not been sufficiently capped against run-away cost increases. It happened at a time when executives in the integrated sector could not yet foresee the dramatic shrinkage of their workforce and healthcare costs still seemed manageable.<sup>11</sup> A wave of plant closures in the ‘80s and a policy of encouraging early retirement caused the retiree population to swell. Depending on the steel company, the number of retirees is now three to six times larger than their active

workforce. Many firms did not have sufficient earnings to keep funding their programs up to date. A metals analyst put the U.S. industry's unfunded portion of the obligations at \$15 billion<sup>12</sup>. This financial burden has eroded the companies' competitive position and greatly reduced their attractiveness as potential merger partners.

Is it right for the government to shoulder these costs? Steel producers that are not saddled with this type of legacy cost, minimills in particular, have raised objections to a government bailout, because the subsidy would give a competitive edge to their rivals. In more general terms, the question should be asked why taxpayers, many of whom can look forward only to social security pensions and Medicare, should help finance deluxe pension and healthcare plans for retired steelworkers. Furthermore, having the government absorb steel industry retiree costs will set a precedent for firms in other industries that are in a similar predicament.

## CHALLENGERS OF THE INTEGRATED SECTOR'S PREMINENCE

### Imports

In the 1960s, the competitive position of the integrated mills was challenged by the increased presence of two groups of competitors, imports and domestic minimills. It was the 116-day strike by the USW in 1959 that caused the U.S. steel-trade balance to turn negative. The deficit remained relatively modest for several years, but then widened sharply in 1965 and 1968, when new contracts with the USW were being negotiated. The majority of imports came from Western Europe and Japan.<sup>13</sup> The rise in imports can also be attributed to an increasingly overvalued dollar and to the progress made by offshore producers with the cost and quality of their products. When low profits began to trouble the U.S. industry, management and labor joined hands to put the blame on rising imports. By 1969, their political lobbying resulted in a system of government-negotiated quotas on imports from the European Common Market and Japan. After several years, a strong, worldwide boom in steel demand made the quotas redundant. But when the market entered a recession in the middle of the decade, imports accelerated and the lobby demanded renewed protection. Simultaneously, steel industry lawyers were working hard to transform U.S. trade law into a more effective weapon against imports.

In 1978, all imported steel was subjected to the so-called Trigger Price Mechanism, a system of minimum prices geared to Japanese production costs, then presumed to be the lowest in the world. By the early '80s, faltering demand and the strengthening dollar, which widened the gap between Japanese and U.S. costs, brought down the price-control system. The integrated steel sector then made use of the now tougher trade law to file trade cases *en masse*, with some assistance from a sympathetic U.S. Commerce Department.<sup>14</sup> The U.S. government, trying to avoid a frontal attack against its allies at a time when the Cold War was intensifying, negotiated a system of import quotas covering many nations and products. The quotas insulated the U.S. market from low international prices until global export prices began to soar in the late 1980s. Immediately after the quota system was abolished in the spring of 1992, the U.S. steel industry filed numerous trade cases against all major exporters of sheet and plate products. The industry victory against most imported plate and galvanized sheet products came at a time, 1993, when steel consumption was taking a sharp upwards turn. During the next several years, an expanding U.S. economy drew in more imported steel than ever before to bridge the widening gap between the domestic steel industry's limited capability and the requirements of America's steel-using industries.

### Minimills

Small steel mills have been around for over a hundred years. Building on the continuous billet caster and electric arc furnace (EAF) improvements, a new kind of mill sprang up in the early 1960s. These companies, soon dubbed "minimills," could convert scrap into bars, rods, or sections in a matter of hours rather than days. Favored by low scrap prices, reasonable electric power rates as well as the integrated sector's high unit costs

and regional concentration, the minimills made steady progress and now supply about forty percent of all the steel made in the United States.

**Table II Market shares of U.S. steel producers and imports: 1981, 1991, 1997, 2000, and 2001**  
(in percent of total consumption)

Year	<u>1981</u>	<u>1991</u>	<u>1997</u>	<u>2000</u>	<u>2001</u>
Minimills and Specialty Steel Producers	13.2	31.1	33.9	35.7	39.2
Integrated Mills and Slab-Rerollers	68.6	54.8	48.3	42.9	41.4
Imports by Steel Users and Service Centers	18.2	14.1	17.8	21.4	19.4

Sources: AISI, Metal Bulletin

After minimills had conquered most of the non-flat product markets, one of them, Nucor, adopted a German-developed technology, the thin-slab caster, and in 1989 began to produce wide hotrolled coils. Coldrolling and galvanizing followed a few years later. By now, Nucor has expanded its sheet coil capacity to over eight million tons.<sup>15</sup> Four other entrants, all with some foreign participation, added a combined sheet capacity of seven million tons. In addition, some of the seven EAF-based plate mills (four of them foreign-controlled) can also roll sheet gauges. Although by the end of 2001 Nucor was the largest domestic steel company and individual plants can turn out well over two million tons of coils or sections per year, the term minimill continues to be applied to EAF-based carbon steel companies and their plants. Last year, about 35 such companies, operating 50 plants, accounted for 43 percent of raw steel output and 40 percent of domestic shipments. Their share of the U.S. steel market (apparent steel consumption) was 35 percent, versus 24 percent in 1990, 11 percent in 1980, and 6 percent in 1970. This does not include the share of stainless and tool steel producers, or such firms as Timken and MacSteel, among others, that are more appropriately listed under the “specialty steel” rubric.

### **RAPID MARKET GROWTH IN THE MID- 90S CONTINGENT ON IMPORTED STEEL**

Although other periods had their exciting moments, the far most interesting was that of the “90s. This decade began and ended in recession. But in between it took the steel industry on a wild ride of seemingly unending growth, called by some the “New Economy” era. The boom came as a surprise because forecasters had predicted stagnation for the North American and West European steel markets. Neither the International Iron and Steel Institute nor the usually optimistic forecasters from World Steel Dynamics had detected any sparks coming from the traditional industrialized regions of the world. In 1990, actual U.S. steel consumption stood at 94mt, not a bad result by the standards of the preceding decade. After plunging deeply in the following year, it recovered to 93 my in 1992. But then it took off at a fast pace. By 1997, annual steel requirements increased 32mt, 30mt for domestic consumption and 2mt for additional exports.<sup>16</sup> Of the 32mt, almost 24mt were met by accelerating domestic shipments while the remaining supply gap was filled by rising finished steel imports. What seems puzzling is that a 24mt rise in domestic shipments was accompanied by raw steel expansion of less than 16mt. Part of the answer is provided by the rising volume of semifinished material imported by domestic steelmakers, slabs in particular. Several mills also imported hot and coldrolled coils for conversion into value-added products. The remainder of the gap between domestic finished products and raw steel output was accounted for by improved yields derived in part from a higher continuous casting ratio. Altogether, steel products directly imported by domestic steelmakers accounted for about one third of the 14mt

higher import volume in 1997 as compared with 1992. This increased reliance on imported steel was largely the result of a strategic decision made by the integrated producers to channel their investments primarily into the rolling and finishing end of their mills.

Almost the entire expansion in raw steel output from 1992 to 1997 was achieved by minimills, in large part via the construction of greenfield capacity. There was little overhang of excess domestic capacity during this period, with the exception of some cut-to-length plate and wire rod. As noted, much of the integrated sector's higher shipment volume was contingent on adding value to increased quantities of imported steel. By 1997, when the industry was pushing against the limits of its capacity, such direct mill-to-mill imports had risen to more than 9mt.

However, the high domestic shipment volume of 106 mt achieved in 1997 was far from sufficient to meet total demand of close to 131mt (122mt for consumption, 6mt for exports--mostly to U.S. customers operating in the NAFTA region--and the remainder for inventory accretions by steel users and service centers). That left a gap of 21mt between the domestic industry's best effort and total steel requirements. Had additional tonnage not been available, the buoyant U.S. manufacturing and construction sectors could not have maintained their growth rate. The import dependence of these sectors, which resulted from the domestic industry's lacking capability, almost doubled from 1992 to 1997. It should be added that the domestic deficiencies were not limited to quantities alone. There were, and still are, many specialized product qualities that domestic steelmakers can either not produce at all or not in sufficient volume. In sum, most of steel imported during this period helped both U.S. steel producers and steel users to remain in an expansion mode. Replacing those import quantities would have required an investment of \$18 to \$25 billion for the construction of additional domestic capacity.

### **UNSTABLE CONDITIONS LEAD TO RENEWED TRADE INTERVENTION**

U.S. "actual" steel consumption, which excludes steel moving in and out of customer inventories, set new historic records in three successive years from 128mt in 1998, 130mt in 1999 and 134mt in 2000. In ordinary times, this information would suggest good times for all sellers of steel, both domestic and foreign. Unfortunately, the period was marked by severe quantitative distortions that eventually played havoc with prices and led to a record number of bankruptcies and plant closures in the U.S. steel industry.

The first disturbance was a large 10mt import surge in 1988, a delayed reaction to the financial crisis affecting Eastern Asia the year before. Only about 3mt of the rise in imports was justified by stronger U.S. steel demand in 1998. An estimated 4mt of the additional imports displaced an equivalent volume of domestic shipments, while the remainder turned into inventory or remained unsold.

The end of 1988 would have been a fitting moment for applying the safeguard clause (Section 201) of the trade law. The purpose of this clause is to afford a domestic industry temporary relief from imports, without bothering with lengthy investigations whether or not the imports were traded fairly. Had it been possible to apply the 201 clause as a strictly technical instrument, quickly targeting the six or seven countries chiefly responsible for the accelerated imports, the effect of the surge could in large part have been neutralized within a year or less. Stripped of its high political profile, such a measure would have had a good chance for success in the generally favorable market climate prevailing at the time in the United States and globally.

U.S. steel demand was so strong that even in the absence of an effective anti-surge measure, domestic shipments had recovered to their "pre-crisis" strength as early as the second quarter of 1999. Shipments continued to strengthen and in the first half of 2000 reached an all-time peak which, had its rate been sustained for the year, would have exceeded the historic 1973 record. The trouble was that domestic shipments continued at an excessive rate after prices had begun to fall. The result was net industry losses in a year in which sales were booming.

**Table III U.S. Steel Consumption, Shipments, Imports, and Exports**  
(In million net tons)

Year	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>
ASC	127.9	131.9	116.4	116.9
Shipments	106.2	109.1	98.9	101.5
Fin. Steel Imports	27.2	29.4	23.6	21.2
Semifin. Imports	8.6	8.6	6.4	8.3
Exports	5.4	6.5	6.1	5.8
Total Imports	35.7	37.9	30.1	29.5

AISI data for the years 1999 and 2000. Own estimates for the current year.

The import surge of 1998 did not have an immediate impact on earnings. In fact, profits increased moderately in that year. But the surge no doubt left an adverse impact on prices, which lingered on while the inventory bulge was being worked off. Strong domestic shipments in 1999 and inventory reductions further weakened prices, despite a significant drop in imports. Paradoxically, whereas imports of finished steel registered a sharp decline in 1999, the volume of semifinished steel—imported by domestic steelmakers themselves-- rose 26 percent in that year. As noted, the first half of 2000 presented the industry with the greatest boom in its entire history. Imports of semifinished steel remained at a very high level.

The domestic producers obviously expected the boom of 2000 to be of some duration and, disregarding high user inventories, announced rapid-fire price increases to restore their profitability. Strong demand and rising prices in turn attracted additional imports. Unfortunately, demand began to stall in the third quarter and plummeted in the fourth quarter. The supply spigots could not be turned down fast enough to keep prices from tumbling. Imports, with their usual time lag of several months after orders are placed, added to the excess supply. Unusually low prices in 2001 plus a 10mt drop in shipments caused all but the most efficient U.S. steelmakers to incur losses. Low prices and oppressive legacy costs drove approximately 15 steel producers, including giants like LTV and Bethlehem, into bankruptcy. Plants were shuttered or put on “idle” status, taking a total of more than 12mt of shipments out of the market, although much of it only temporarily.

The 1998 import surge as well as excessive domestic shipments towards the end of 2000 and in the first quarter of 2001 were the main causes of low prices and earnings last year. However, there were two other factors that also contributed to the plight of the U.S. steel industry, its integrated segment in particular. One was the entry of too many producers into several product markets, among them plate and galvanized sheet. Another negative factor was the low contract prices exacted by powerful customers in the automotive, appliance, and electronics industries.<sup>17</sup>

## **ONCE AGAIN, STEEL IN THE POLITICAL LIMELIGHT**

Last year, the domestic steel industry was in dismal financial straits and suffered a large number of bankruptcies and plant closures. This situation had come about although in previous years the industry had filed and won numerous antidumping and countervailing duty cases against foreign steel exporters. Like president Clinton before him, president Bush soon came under enormous pressure from the congressional “steel caucus” to take the safeguard, or 201, initiative on behalf of the domestic steel industry. There was a weighty reason for taking the bold step of engaging in massive trade intervention, namely, gaining the support of politicians from six or seven influential steel states in two upcoming events, the administration’s fight to resuscitate the dormant Trade Promotion Authority (TPA) and, later in the year, congressional elections.

In an effort to camouflage a blunt trade intervention as a program with far-ranging foreign policy objectives, the administration widened the initiative to include a series of negotiations with the governments of steel-exporting nations. The stated purpose of these negotiations is to restore order in the global steel market by putting a stop to steel industry subsidization and by eliminating huge amounts of excess capacity, the presumed result of past subsidies. All this is to be achieved by the time the temporary protection of the U.S. steel industry runs out.<sup>18</sup> Very likely, little will come of this. U.S. government officials will attend many conferences, rub shoulders with foreign officials, and multinational committees will issue resolutions. The main purpose of this diplomatic initiative is to deflect attention from domestic protectionism to alleged foreign unfair trade practices and one of their perceived consequences, a mountain of excess capacity.

### **PRESENT TRADE LAW, INCLUDING 201 ACTION, FAILED IN EMERGENCIES**

One problem that has not been addressed is the still overvalued U.S. dollar, which is a major force behind the import pressure on many U.S. markets, not just steel. Another unresolved problem is the lack of a quickly enforceable defense against import surges that severely disrupt the supply/demand balance in national steel markets. Surges may be triggered by the financial collapse of economies or a panic affecting several major exporters. The antidumping law is far too slow to cope with such emergencies. Failure of this law to deal adequately with recent import surges is the reason why the U.S. steel lobby and its congressional supporters fought tenaciously for the current 201 import restrictions. But in its present form, the Section 201 remedy is a ponderous, sledgehammer-like instrument that creates as many problems as it resolves. That is a pity. If it were kept out of the political limelight, the safeguard clause could be an ideal remedy for pinpointing foreign exports that rise at a much faster pace than warranted by domestic consumption needs. The brakes could be applied to such imports well before they have a chance to swell into a surge. Moreover, it could be done without stirring up the deafening polemics that accompany the present mode of Section 201 application.

### **IMPACT OF THE 201 INTERVENTION ON THE U.S. STEEL MARKET**

It could be argued that, except for the 1998 surge, import volume fairly well tracked fluctuations in domestic steel consumption. When in the middle of last year the 201 initiative was first announced, imports were already in steep decline. Should there still be merit in the claim that U.S. industry needed a multi-year “breathing space” to consolidate its structure and reduce its costs, questions remain concerning the details of the 201 provisions. The majority of the commissioners of the U.S. International Trade Commission (ITC) had recommended import tariffs up to 20 percent.<sup>19</sup> Flatrolled products, which account for close to half of total steel consumption and domestic shipments, were to be assigned the top 20 percent rate. Because these tariffs were to be imposed on top of the many antidumping and countervailing duty penalties already in force, the barriers to imported sheet products would have been raised considerably. On March 2, 2002, the administration then

imposed tariffs, for a period of three years, that were 50 percent higher than those recommended by the majority of the ITC commissioners.<sup>20</sup> Very likely, this represented a concession to strong political pressures by the steel lobby and its political allies for a four-year 40 percent tariff, or twice the level recommended by the ITC.

Spot prices for sheet products had registered modest increases during the first two months of this year. But hardly anyone was braced for the speed at which these prices shot up during the following months. In the Midwest region of the United States, spot prices for hotrolled coils rose from \$210/short ton in December 2001 to \$230/t in February 2002 and to \$400/t in July of this year. For coldrolled coils the prices during these months were \$300/t, \$320/t, and \$525/t; for hot-dip galvanized coils they were \$320/t, \$330/t, and \$535.<sup>21</sup> Such large price increases, compressed into a very short time span, put all but the largest steel users in a difficult competitive position. Moreover, many manufacturers have to wait three or four months for their orders to arrive. Steel users competing in the global market face the additional problem of a widening gap between the steel prices they are charged and the prices paid by their offshore competitors. The gap has widened to well over \$100/t in recent months despite increases in foreign steel prices and a weakening of the U.S. dollar in foreign markets.<sup>22</sup> However, there are rumors that U.S. prices of hotrolled coils fell slightly in August 2002 due to the reentry into the market of some LTV facilities (now ISG).

**Table IV**                      **Spot Prices of Sheet Products**  
(dollars per ton)

	<b>Hotrolled Sheet and Coils</b>			<b>Coldrolled Sheet and Coils</b>		
	<u>U.S. Midwest</u>	<u>EU avg</u>	<u>Japan</u>	<u>U.S. Midwest</u>	<u>EU avg</u>	<u>Japan</u>
Dec. '01	220	222	150	290	291	240
Jan. '02	240	210	154	310	286	236
Feb. '02	250	209	168	310	278	236
March '02	290	210	186	360	275	254
April '02	305	227	200	390	326	272
May '02	320	249	218	400	328	290
<u>June '02</u>	<u>370</u>	<u>254</u>	<u>236</u>	<u>470</u>	<u>322</u>	<u>336</u>

Source: Metal Bulletin Research, *Coated Steels Monthly*,  
Issue No 41, June 2002, p. 3 (Converted from metric to short tons)

Total steel consumption during the first six months of this year was less than one percent above that of the last six months in 2001.<sup>23</sup> It was primarily restrictions on the supply side of the U.S. steel market that triggered the surge in prices. The 201 tariffs represent one of these restrictions. After allowance is made for the exemptions granted to NAFTA members and to developing nations as well as to product grades not sufficiently supplied domestically, around 37 percent of finished steel imports were affected by the tariffs. Among the semifinished products imported by steelmakers only slabs were subjected to a tariff quota. The inclusion of slabs in the 201 coverage resulted from infighting within the industry, with a small group of integrated

producers forming an alliance with minimills to deny other steelmakers access to low-cost foreign slabs. Typically, the administration arrived at a compromise by giving the tariff-free quota an ample dimension.

Another important restriction on the supply side was caused by the closure of marginal facilities. Since the middle of last year, the shuttering or idling of steel plants has taken 12 mt of domestic shipments off the market, with flatrolled products making up more than 90 percent of this volume.<sup>24</sup> In conjunction with high 201 tariffs, it is not surprising that the brunt of the price increases affected the flat-products category. The high percentage of sheet products that had to be earmarked for long-term supply agreements with large steel users put additional pressure on spot prices.

Steel prices have gone up in many other countries as well. Deliberate output restrictions, reinforced by plant closures, have been principal cause of those increases in Western Europe and East Asia. In the EU, Japan, and Korea output cuts for the purpose of boosting prices have been facilitated by the enormous size of the leading steel producers.<sup>25</sup> The restocking of steel user inventories in many parts of the world further helped firm up prices. But, overall, international price increases have lagged far behind those attained in the United States, despite the weakening dollar. Moreover, in response to the U.S. 201 action, the EU and many individual nations in different parts of the world have likewise erected barriers to imported steel. What used to be a relatively open global steel market is now divided into a number of regional protectorates.

## **THE EXCESS CAPACITY DEBATE**

### **Some Historic Background**

In 1967, the American Iron and Steel Institute launched its first major campaign for blanket protection from imported steel. The AISI claimed that the U.S. steel industry needed a “breathing space” from import pressures, during which it could “revitalize” its facilities. On October 20, AISI president John Roche, testifying before the Senate Finance Committee, listed “the availability of substantial unused steel producing capacity elsewhere in the world and the policies of certain foreign countries with respect to this capacity” first among the basic forces driving the growth of imports. He also pointed out that, if steel imports continued to rise, “the most dangerous consequences would be to national security.”<sup>26</sup> Why is it necessary to reproduce 35-year old arguments? Mainly because the claim of excess global capacity destabilizing markets has since become a mantra that was repeated again and again during later campaigns for protection, including last year’s high-decibel effort to have the government intervene with imports via Section 201 of the trade law. The national security was likewise resuscitated during the recent debate.<sup>27</sup>

### **The MSA Proposal, or Gesture, of 1989**

It is not surprising that similar verbiage eventually entered into the vocabulary of politicians making a case for steel industry protection. For instance, in November 1988, then vice president and top-office contender George Bush was well aware of the steel lobby’s political influence in the heavily populated “steel states.” Just days before the election, he sent a letter to the congressional Steel Caucus with assurances that he would continue the steel import quotas (also called voluntary restraint agreements) put in place by president Reagan. The letter contained the following paragraph: “Unfortunately, while the voluntary restraints have clearly had a positive impact on the U.S. industry, we have not at the same time made as much progress toward eliminating market distorting practices. Global overcapacity remains a serious problem, and there is still substantial dumping and subsidizing. The only way to produce a permanent solution to the domestic steel industry’s problems is to bring an end to these unfair practices and restore a competitive market in steel.”<sup>28</sup> That solution was a “Multilateral Steel Agreement”(MSA), which was to take the form of frequent meetings among government experts of steel trading nations with the objective to restore free trade principles by ending unfair practices and overcapacity. Other nations insisted that such meetings also precede any large-scale filing of

antidumping and countervailing duty cases but this idea was fiercely resisted the U.S. steel lobby, worried about any weakening of its “trade law remedy.”<sup>29</sup> Very likely, the MSA proposal merely served as a face-saving device for an avowed free trader coerced into the role of an interventionist.

### **Here we go again in 2002: Déjà vu and Plus ça change ...**

As was mentioned, the purpose of the massive Section 201 intervention with U.S. steel trade was to pull the rug from a potential political threat posed by six or seven steel states. President George W. Bush was in need of congressional support for his proposal to reactivate the Trade Promotion Authority (TPA), popularly known as “fast track.” Political goodwill would also be at a premium at the congressional elections in November 2002 and the general elections in November 2004. Moreover, as happened in 1989, the trade intervention was accompanied by a proposal—in essence similar to the earlier one—which, if carried out, would dispense with the need of further interventions for many years to come.

One could argue that the gambit of sacrificing open steel trade for advancing the free-trade principle was already vindicated by the TPA passage on August 1, 2002. However, unless the foreign-war issue should overwhelm all other considerations, the administration will want to nurture any political advantage it may have gained with its 201 initiative at least until November 2004. It is therefore unlikely that it will have lost interest in pursuing the goals of trimming excess capacity and ending subsidies.

### **Definitional Complexities**

The AISI stopped publishing capacity estimates after 1960 because critics were interpreting falling utilization rates as a loss in efficiency. It resumed publishing estimates in 1975 with the obscure explanatory note “tonnage capability to produce raw steel for a sustained full order book.” For most of the years they are overstated. Thus, for 1978, capability is more than 20mt above raw steel output, although the year was marked by sporadic shortages.<sup>30</sup> A similar large excess existed in the years 1999-2000, according to the AISI data. That raises the question, with such a large raw steel reserve on hand, why did the industry rely on record quantities of foreign semifinished steel for processing in its plants? The answer is that some integrated producers channeled most of their limited investment funds into rolling and finishing, making up raw-steel deficiencies by importing large quantities of slabs.<sup>31</sup> Raw steel data, whether they refer to output, capability, or utilization rates, therefore no longer provide a complete picture of steel production in the United States. For completeness, we shall have to look at industry shipments. The AISI does not publish capability numbers for this category, but we can estimate them from periods during which supplies were tight and, according to press reports, the industry was shipping all it could.<sup>32</sup> To be sure, peak shipment data may also overstate an industry’s capacity. That was the case in 1973, when the U.S. steel industry operated at unsustainably high rates by deferring scheduled maintenance, greatly extending their delivery periods, and diluting product quality.<sup>33</sup> But such incidents have been rare and it is generally fairly safe to equate shipments at the top of a cycle with industry capacity over a three-to-four year period.

### **Origin of Some Numbers**

Claims of vast quantities of excess global steelmaking capacity crop up regularly in times of stagnation or recession. But many of the gigantic excess capacity numbers cited in recent years by governments and trade associations significantly exceed the 60-70 mt dips in capacity utilization caused by business cycles and the accompanying inventory fluctuations. Those numbers, which range from 150 to 250 million metric tons of raw (or crude) steel capacity, often draw on estimates compiled by the Organization for Economic Cooperation and Development (OECD).<sup>34</sup> These are theoretical meltshop capacities that were projected forward from a 1996-'98 working base. In many cases, they far exceed the output that individual plants were able to attain in the preceding 10-12 years, even in years when delivery periods in the global market were abnormally long and

prices had soared. Maintaining such a huge quantity of equipment to keep it from rusting away is expensive. Furthermore, having fallen into disuse for so many years, this equipment cannot be reactivated without a great deal of refurbishing and, in many cases, a minimum of technological and environmental upgrading. The required amounts would be of staggering proportions, going into many billion dollars per year.

### **Political Tailwind for a Hypothesis**

The question raised by the OECD estimates is, who is able to finance the continued existence of all this capacity? Those who support the idea of massive excess capacity in the global market point to government subsidies, without providing detailed evidence. This hypothesis gained a great deal of currency in June last year when the Bush administration announced its 201 initiative, explaining that the U.S. steel industry “has been affected by a 50-year legacy of foreign government intervention in the market and direct financial support of their steel industries. The result has been significant excess capacity, inefficient production and a glut of steel on world markets.”<sup>35</sup> It should be noted that this passage was redundant from a legal viewpoint, because safeguard actions do not require proof of unfair practices on the part of the foreign countries or exporters. However, as in 1989, an administration espousing free trade could not perpetrate a crass trade intervention without offering a face-saving alibi. In this instance, two salient points were made, first, the administration had its hands forced by decades of foreign government intervention and, second, this U.S. intervention can be transformed into an opportunity for engaging foreign governments in negotiations that will ultimately make the global steel market safe for free trade. In other words, a preemptive protectionist strike was the only available means for restoring free trade in steel. Moreover, the initial message was also mercantilistic in its tone. It implied that steel imports have inflicted harm on the U.S. industry and made no admission that steel imports have benefited American manufacturers by supplying them with products that were not available from domestic sources and by serving regional markets that had been neglected by the domestic industry—as those of the West and Southwest. And large slab imports permitted the integrated segment to maintain its volume of shipments without investing some \$6-8 billion in new front-end capacity.

### **Some Excess Capacity Estimates.**

What about the extent of overcapacity when these various episodes occurred? At the Senate Hearings in 1967, John Roche mentioned a figure of 55 mt.<sup>36</sup> He had obtained this information from a hastily prepared staff study that had been commissioned by the same Senate Finance Committee.<sup>37</sup> Its authors freely acknowledged that this estimate of global surplus capacity had been obtained with the use of weak data and fragile methodology.

In November 1988, when the elder Bush pledged that he would keep the Reagan quotas in force, the global steel market was doing exceptionally well compared to earlier years. Demand in the United States and abroad was at the peak of the cycle and prices were unusually high. According to analysts of World Steel Dynamics, whose estimates correspond closely to those derived from maximum sustainable shipments, excess capacity in 1988 amounted to 56mt.<sup>38</sup> This was about normal for a cyclical peak, given the unavoidable geographical and product mismatches between capacity and demand. Three years earlier, the surplus was much higher, 122mt, and the remarks made by Mr. Bush probably reflected those conditions. Unfortunately, the common tendency to mistake conditions of a few years back for present-day reality can lead to serious errors when it enters into policies affecting cyclical markets.

In the meantime, the supply side of the global steel market was weighed down by the near-collapse of steel consumption in the Former Soviet Union (now the CIS region) and then by the Asian financial crisis. CIS steel consumption fell more than 100mt and shipments 50mt from 1989 to 2000, while net exports rose more than 50mt.<sup>39</sup> After reaching a low point in 1998, consumption has regained 10mt by 2000 and increased further since then. Some capacity expansion has been achieved in recent years via investment in improved productivity.

It should also be mentioned that about a quarter of CIS exports have been sold to foreign steelmakers in the form of semifinished products. Moreover, at least until 1997, CIS exports of finished steel products helped maintain industrial growth rates in Southeast Asia. Following the 1997 Asian crisis, consumption in East Asia suffered a drop of 50mt, of which only 30mt has meanwhile been restored. It is not surprising that global excess capacity grew sharply in the next two years. Even so, with the exception of one year, 1999, it remained under 100mt, considerably less than the numbers cited in industry and government circles.<sup>40</sup>

**Table V** **Global Crude Steel Capacity and Output**  
(million short tons)

<b>Years</b>	<b>Capacity</b>	<b>Output</b>	<b>Op. Rates</b> (percent)
1985	916	794	86.7
1986	909	787	86.5
1987	908	814	89.6
1988	917	861	93.9
1989	926	866	93.6
1990	927	850	91.7
1991	935	808	86.5
1992	909	794	87.3
1993	885	802	90.7
1994	860	799	92.9
1995	890	829	93.3
1996	906	827	91.3
1997	928	881	94.9
1998	950	857	90.3
1999	988	869	87.9
2000	1014	934	92.1
<u>2001</u>	<u>1016</u>	<u>931</u>	<u>91.8</u>

Source: P. Marcus and K. Kirsis, Global Steelmaking: Supply/Demand Outlook, Sept. 1999, p. I-2; Analysis, Nov. 30, 2001, pp. 20-21; Global Steel Alert #6, July 11, 2002, pp. 16-17. Data from these publications were converted from metric to short tons in both the tables on this page.

**Table VI** **Crude Steel Capacity and Output, by Country or Region, Year 2001**  
(million short tons)

	USA	Japan	EU	Oth. Dev'd W. World	Develop'g World	CIS	Eastern Europe	China*	World
<b>Capacity</b>	117	126	186	51	220	115	38	161	1016
<b><u>Output</u></b>	<u>99</u>	<u>113</u>	<u>175</u>	<u>45</u>	<u>194</u>	<u>109</u>	<u>31</u>	<u>165</u>	<u>932</u>

Source: P. Marcus and J. Innace, Global Steel Alert #6, July 11, 2002, p. 16.

\*Estimates for China include small quantities for North Korea and Vietnam (together about 0.7mt)

### **What is the right capacity?**

Given the market's cyclical nature, steelmakers cannot be expected to anticipate future global demand growth with any degree of accuracy. Are government officials better qualified to determine the capacity levels that will be adequate for hard-to-predict future consumption peaks? The world's steel producers would be quite contented if global capacity fell short of peak requirements, which would probably guarantee them record profits for several years. New steel plants, besides being expensive, take a minimum of four to five years to build and operate as planned. Obviously, steel users and final goods consumers would be angered if projections made by bureaucrats led to sizable capacity shortfalls. But these groups lack the necessary cohesion to form influential political lobbies with a chance to balance the power of the steel lobby.

### **Cutting Capacity may not bring Order during a Market Downturn**

Capacity is no doubt the key determinant of a shortage and its consequences like high prices and extended delivery periods. In contrast, excess capacity does not necessarily cause a glut, just as a powerful engine is not always a cause of speeding. It is the driver who controls the speed of a car and it is the chief company officers who determine the utilization rates of steel mills. Steel company managers are under pressure from the cost side to keep plants operating at high rates. But regardless of the effect on costs, during a downturn in demand operating rates need to be reduced or the result will be a glut, even when little or no excess capacity existed at the peak of the cycle. Given the inelasticity of the demand for steel, the drop in prices caused by excessive production is likely to result in greater losses than a reduction in output and the related increase in unit costs. This problem of adjusting production to falling demand is more easily resolved by firms commanding a large share of the market, as in the European Union and Japan. In many segments of the U.S. steel market, intensive competition among domestic sellers will force prices down even where imports exert no significant influence. In the absence of seller discipline, relatively small quantities of excess production can pose a threat to stable prices. Although capacity plays a role in this process, it is discipline, or the lack of it, among sellers that is the main determinant of excess production.

### **What can be done?**

One method to induce greater price discipline among U.S. steel producers would be to increase the degree of concentration, or consolidation, in the industry. In fact, greater industry consolidation is one of the conditions stipulated by the Bush administration in return for providing the Section 201 protection. While companies like U.S. Steel and Nucor have expressed an interest in acquiring other domestic steelmakers, the main problem is that the acquisition targets—Bethlehem, National, and Rouge—carry the burden of high legacy costs. Eliminating the pension element of those costs, via transfer to the U.S. government, would require that these companies first enter into Chapter 7 of the bankruptcy law which, if the judges approve, permits the asset sale at auction. Concerning the second element, health-care costs, the companies may have to provide some assistance at least to those workers who do not yet qualify for Medicare. Ultimately, this matter may have to be resolved by the courts.

To tighten price discipline in the U.S. steel market, it will also be necessary that minimill managers modify their historic method of expansion. Traditionally, this method consisted of raiding the market shares of integrated producers and, in some product lines, imports. In the more recent past, minimills have switched from an adversary stance toward integrated producers to full cooperation with them in one area, their joint campaign against imported steel. To transfer this positive relationship to the market place and avoid upsetting the domestic output/consumption balance, minimills may have to control their aggressiveness. That may include resisting the lure of building new capacity on the strength of innovative, cost-reducing technology. Such technology played a major role in the construction of sheet and plate mills using thin and medium slabcasters.

Still newer methods, like sheetcasting for carbon and stainless steels, have already entered commercial production in the United States and the European Union. One example of a minimill entering an already crowded market is the modern heavy section and rail mill started up by SDI, a minimill, that in the past has competed successfully in the sheet market. The company claims that its mill can produce longer rails at a lower cost than its domestic competitors, Bethlehem and Oregon Steel, which already have more capacity than is required to meet peak U.S. demand.

Enjoying the benefits of good location and short lead times, minimills have been displacing imports for more than two decades. They have also battled offshore competitors by filing numerous antidumping cases. Application of the antidumping law is expensive to petitioners and respondents alike. It is also time-consuming and therefore not an effective measure for preventing import surges. And it relies on dubious criteria by which imports are judged to have been unfairly traded, i.e., at prices that are less than either unit production costs or home market prices. The first of these criteria implies that, if in a deep recession all exporting companies are losing money, all exports would have to cease or be subject to dumping penalties. Needless to say, no equivalent law regulates domestic commerce. Otherwise the majority of American steel companies would have been guilty of violations in recent years. The second criterion might have made sense in an era of fixed exchange rates. But with today's fluctuating rates, exporters could be driven out of export markets by a sudden appreciation of their home country's currency.

The safeguard clause was meant to prevent market disruptions caused by import surges. In the recent U.S. example, it was applied long after the disruption occurred and import pressures had eased. Perhaps the worst feature of this 201 initiative is that it was primarily applied for political reasons and will do little or nothing to make the weaker companies creditworthy at home or competitive internationally. But, as noted earlier, the 201 is potentially an effective instrument for controlling disruptive imports. To achieve that objective, it would first of all have to be kept out of politics. Having it administered solely by the International Trade Commission or jointly with the U.S. Trade Representative's office might do that. Secondly, administering it in moderate doses at one time might help to keep it out of the limelight of public attention and avoid overreaction by the targeted foreign exporters. In short, as a non-political mini-201 instrument it would be quickly applied to any imports that are increasing at a significantly faster pace than the growth in demand for a specific product. Making use primarily of the "threat of serious injury" clause, application of this instrument might not require a change in the law, only in procedures. The mini-201 route would permit speedy enforcement against individual foreign companies caught accelerating shipments disproportionately to changes in demand. Those that are caught could be subjected to quotas, perhaps for one year, and at half the volume they normally ship. A licensing requirement could be imposed as well. The purpose would be to have the instrument work like a prod rather than a sledge hammer. Once the word spreads that a mini-201 was enforced in a few instances, other foreign exporters would probably feel motivated to exercise caution. They are likely to react as many highway users do when they see someone being ticketed. As a consequence, the actual enforcement plus the demonstration effect may suffice to check an incipient import surge.

### **Almost any Change of the Existing System will be an Improvement**

There is no guarantee that this will prove to be a workable system for steering U.S. and, possibly, global steel trade through the cliffs and maelstroms in its course. As was noted earlier, the existing system is ponderous and ill-adapted to deal with rapidly changing trade flows. Moreover, the dumping law applies fundamentally different standards of legality to international trade as compared with the standards applied by other U.S. laws to strictly domestic transactions. Depending on their origin, goods sold in the same geographical market are subject to different rules of competition. As national economies become more intertwined, or "globalized," such discrimination is bound to lead to increasingly complex problems and absurd results.

Furthermore, for more than three decades, U.S. steel trade has sporadically been subjected to highly politicized government interventions, including the recent 201 initiative. They have taken the form of quotas minimum prices as well as tariffs and tariff quotas. Each came with ambitious goals for a more efficient and competitive industry by the time the intervention ended. In fact, the opposite occurred during some of those periods. Labor contracts were signed that jeopardized the long-term survival of integrated producers and operations were spun off from larger firms that never had a chance to be viable except by means of further trade interventions.

More recently, as in 1989 and again last year, interventions had programs attached to them that were (or are) thought capable of restoring some order to the global steel market. If that could be done, global disorder would be less likely to cause disruptions in the U.S. steel market. That, in turn, would reduce or eliminate the need for future steel trade interventions. The 1989 program, had it been taken seriously and actually put to work, would have meant setting up a committee of government bureaucrats from various countries for the purpose of jawboning steel industries into compliance with international rules. The goal of the new program is some sort of supra-national regulation of capacities. More likely than not, little will come of the current effort to reform the global market, because the main problem is not a vast amount of excess capacity but relatively small amounts of excess production. A higher degree of consolidation may be the answer, but that would require some alignment of antitrust and antidumping rules. Absent a thorough structural reform, another crisis will erupt in the U.S. steel market within a decade or so. As has been the case for 35 years, imported steel will be named the sole or, at least, principal culprit. Another U.S. administration, expressing consternation over foreign excesses, will intervene with the flow of imports and propose another original method for putting an end—once and for all—to persistent distortions of global steel trade.

### **SOME FINAL COMMENTS**

For the time being, U.S. steelmakers and many of their foreign counterparts have become better off than they were a year ago. The opposite is true for many small and medium-sized firms who pay spot prices for their steel. Steel producers continue to announce price increases for future deliveries. But in the United States clouds are gathering on the horizon and it may rain on the price parade before the year is over. First, several large-tonnage producers will come back on stream, among them several of the former LTV works (under the new acronym ISG) and the former Trico works (acquired by Nucor). Second, the widening gap between U.S. and international spot prices plus the multitude of trade barriers in the world will likely motivate some foreign steel exporters to pay the tariffs and other penalties in order to reenter the U.S. market. And, third, there are signs that the U.S. economy will experience very little growth or, possibly, stagnation during the remainder of the current year.

In return for the 201 breathing space from global competition, the U.S. government expects the steel industry to consolidate its structure and become more efficient. But, as was already mentioned, large retiree pension and healthcare costs have so far presented a major obstacle to any acquisitions or mergers involving integrated steel companies.<sup>41</sup> Furthermore, regulatory questions may arise if the U.S. industry should succeed in achieving a high rate of concentration. For example, the Department of Justice or the Federal Trade Commission may investigate whether parallel volume and price policies of giant producers reflect normal managerial practice or collusive behavior. In contrast, the ITC is not concerned about the impact that its decisions may have on the competitive practices of domestic producers. A potential conflict arises from the fact that over the past two decades the antitrust authorities have given more weight to the welfare of consumers in their decisions, whereas the ITC sees as its only mission the protection of producers, regardless of the cost this imposes on consumers.<sup>42</sup> It is easy to foresee the absurdity of a situation where the Department of Justice or the

FTC might wish to reduce the price setting powers of a tight domestic oligopoly (e.g., in heavy beams), while an ITC decision might put an end to the only viable competition that may be left, i.e., imports.

It will be interesting to watch how the leading West European steelmakers will manage to balance their potentially conflicting needs. There is a need for satisfactory earnings, another for prices and qualities that ensure the survival of customers, and yet another for a high degree of skill to maintain the right volume/price balance in their markets while steering clear of national and supra-national competition laws. Very likely, the steelmakers will also want assurances from the EU Commission that during future recessions their home markets will not be left undefended from import surges. Nevertheless, in normal times they are more likely to favor a return to freedom of movement in the global market. The leading steel producers remain heavily engaged in foreign markets as exporters, importers, investors, and partners in cooperation agreements. Their global entrepreneurial orientation can be expected to go hand in hand with a positive view regarding international specialization and trade.

In contrast, the U.S. industry is likely to adhere to its insular siege mentality for some time into the future, especially now that most minimills have begun to share the traditional steel lobby's views regarding international trade issues. What might eventually break this mentality may be the large steel-using manufacturers engaging themselves more intensively on the political front in opposition to trade barriers. On the other hand, whether the acquisition of U.S. firms by foreign groups would influence the industry's collective view of international trade is far from clear. In the past, heavy foreign investment in the U.S. steel industry did little or nothing to cause the industry to shift away from its parochial attitudes and almost xenophobic rhetoric. That might change, of course, if several of today's international steel giants acquired a large stake in U.S. steel companies and fostered sympathies in U.S. political circles. One other factor that might also have an impact on inveterate U.S. attitudes toward foreign trade is the changing international value of the U.S. dollar. Should the dollar continue to lose value abroad, U.S. steelmakers would become more competitive in the global market. If they became more interested in exporting beyond the NAFTA perimeter, they might gradually shed their siege mentality vis-à-vis the rest of the world. However, it may take a while to clear global steel trade of the many barriers that have come into existence since the 201 action. In the eyes of many governments, the U.S. action has made steel-trade intervention internationally acceptable. The World Trade Organization faces the difficult task of restoring unrestricted trade as a general principle, at least during relatively normal years.

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- 34 See, e.g., Organisation for Economic Co-operation and Development, Development in Steelmaking Capacity of Non-OECD Countries, 1999 Edition, passim. It is difficult to understand how analysts of the International Trade Administration, U.S. Commerce Department, who are well versed in global steel market problems can uncritically accept such data. See their publication Report to the President, Global Steel Trade, p. 3. This comment can be extended as well to a study authored by G. Hufbauer and B. Goodrich of the Institute for International Economics, “Time for a Grand Bargain in Steel?,” pp. 3-4.
- 35 Metal Bulletin, June 28, 2001, p. 3.
- 36 J. P. Roche, p. 828.
- 37 Steel Imports, Staff Study of the Committee on Finance, U.S. Senate, pp. 17-30, especially p. 28. The study is sometimes referred to by the name of its collaborator, Dr. Robert Weidenhammer of the University of Pittsburgh.
- 38 P. Marcus and J. Innace, World Steel Dynamics, Analysis, Nov. 30. 2001, p. 22 and Global Steelmaking: Supply/Demand Outlook, September 1999, p. I-2. For example, a partially idle bar mill on a land-locked site

in the Eastern United States will not be able to benefit from a construction boom in California due to prohibitive freight costs. Obviously, the mill will likewise not benefit from a surge in the demand for galvanized sheet.

- 39 International Iron and Steel Institute, Steel-Statistical Yearbook, 1999 and 2001, and World Steel in Figures, 1998-2002.
- 40 P. Marcus and J. Innace, World Steel Dynamics, Analysis, Nov. 30. 2001, p. 22.
- 41 Thomas Usher, chairman, U.S. Steel Corp. and Guy Dollé, chief executive officer, Arcelor, in separate presentations, at the conference *Steel Success Strategies*, organized jointly by American Metal Market and World Steel Dynamics at the Plaza Hotel, New York, June 17-19, 2002.
- 42 U.S. International Trade Commission, The Economic Effects of Antidumping and Countervailing Duty Orders and Suspension Agreements, Publication 2900, June 1995, Views of Vice Chairman Janet Nuzum and Commissioner David Rohr, p. VIII, “Finally, when viewing the conclusions of this report, it must be remembered that the purpose of the antidumping and countervailing duty laws is not to protect consumers, but rather to protect producers. ... So it should not come as a surprise that the economic benefits of the remedies accrue to the producers, and the economic costs to the consumers.”

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