

## CHAPTER 2

# The U.S. Steel Import Crisis

### Introduction

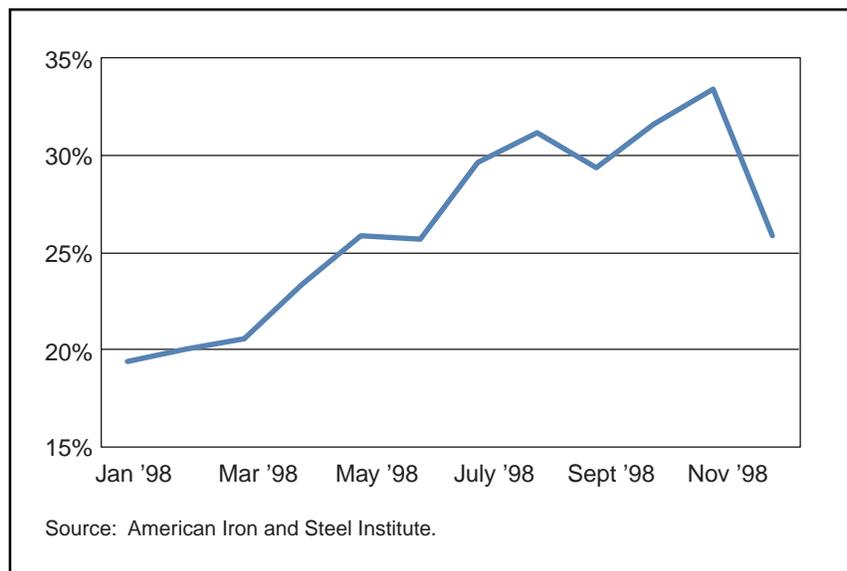
The U.S. steel crisis of 1998 began to take hold in the middle of the year and then came on quickly. In the last six months of the year, import penetration reached record levels, domestic shipments fell 11 percent and capacity utilization rates dropped dramatically (*Charts 2-1, 2-2*).<sup>1</sup> The speed and severity of the crisis, and the abrupt deterioration of the U.S. industry's fortunes, caused steel companies and workers to fear that they might soon be facing one of the worst crises to hit the industry in recent years.

Imports were killing us. All of a sudden, we went from three shifts down to two—you knew what was coming. Each day I'd look and see my order sheets dropping. Then you start looking to see if your name's on the list, asking you to report to the front office. One day it's up there, and your job is gone.

Harry Thuedaus, steel worker at Acme Steel, laid off after seven years with Acme

The rapid growth in imports coupled with the drop in prices hit many U.S. steel companies hard. During the second half of 1998, a number of U.S. companies saw their sales drop sharply.

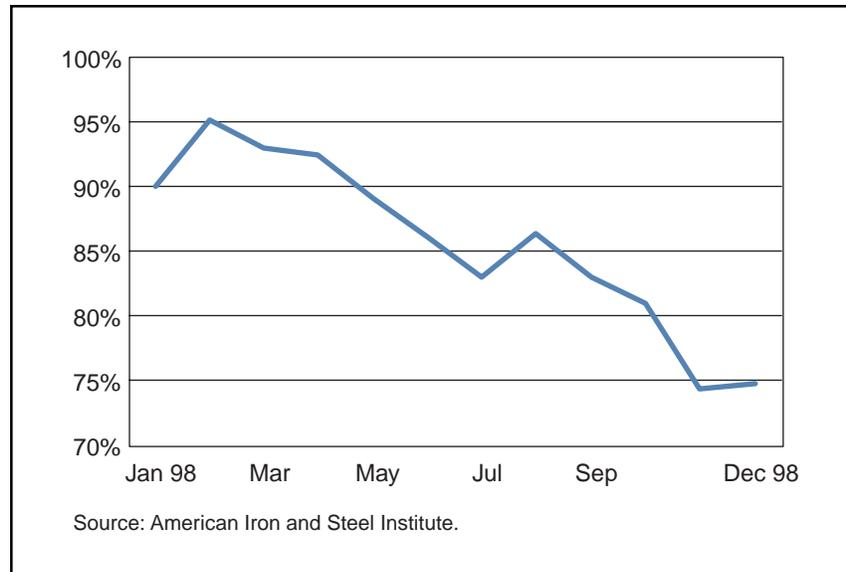
- North Star BHP's order books dropped from 227,000 metric tons (MT) to less than 55,000 MT in a period of less than six weeks.<sup>2</sup>
- In September 1998, Wheeling-Pittsburgh saw 143,000 MT vanish from its order books in a ten-day period.<sup>3</sup>
- From November 1998 to February 1999, Northwestern Steel's business fell off by 40 percent. According to Fred Rocchio, president and CEO, the impact of the import surge became evident in late 1998 when



2-1. Import Penetration: Finished Steel

orders for beams and channels “just up and died.” Even after the company drastically slashed prices to match those of imports, it was forced to close its wire and wire rod operations and lay off 320 steel workers.<sup>4</sup>

- Acme Steel saw 63 percent of its order book disappear in two months—to a level below the practical running capacity of the blast furnaces.<sup>5</sup>
- Six firms—Acme Steel, Geneva Steel, Gulf States Steel, Laclede Steel, Qualitech Steel, and World Class Processing—were driven into bankruptcy, typically citing the increase in steel imports and the fall in prices as one of the reasons they filed for protection under Chapter 11.



2-2. Monthly Capacity Utilization Rates

Thousands of steel employees were laid off in 1998 and 1999.<sup>6</sup> Throughout the fall of 1998, steel firms shut down lines and cut back their workforces.

### Steel Users' Views

Steel-consuming companies have noted the benefits of steel imports to the U.S. economy. They argue that steel imports can improve the competitiveness and profitability of steel-consuming industries. They also argue that trade cases may result in higher input costs or supply disruptions for their industries. In testimony before the Senate Finance Committee, J. B. Porter, Chief Procurement Officer for Caterpillar (one of America's largest importers of steel) stated that lower-priced steel imports benefit the metal fabrication, transportation, industrial machinery and construction industries, which depend upon steel as an essential input, and, which combined, employ many more workers than the steel industry.

As a net importer of steel, the United States depends upon foreign steel to supply part of its needs. Moreover, the U.S. steel industry depends upon semifinished steel imports to supplement its own production. In 1999, more than 7 million MT of semifinished steel was imported for use by U.S. steel companies to convert into finished steel products.

- U.S. Steel's Fairless Works laid off 300 of its 850 workers the day before Thanksgiving.<sup>7</sup>
- In December, Bethlehem Steel laid off 650 employees, while Northwestern Steel laid off 250 employees.<sup>8</sup>
- At Weirton Steel, 747 workers spent their holidays in the unemployment line.<sup>9</sup>

The situation in 1998 was different from previous downturns. The U.S. industry was not in the midst of a recession as it had been in the early 1980s. Following painful restructuring, a more efficient industry emerged in the 1990s, making the United States a competitive and relatively low-cost producer of steel products. Nor was the U.S. steel market weak (*see box, this page*).<sup>10</sup> Demand was up, and 1998 had been predicted to be a banner year for U.S. industry. Instead, thousands of steel workers lost their jobs (*see box, next page*).<sup>11</sup>

The crisis was triggered by economic downturns abroad. The Asian financial crisis began with Thailand in mid-1997, and spread throughout Asia, bringing with it the worst economic downturn to hit the region in thirty years. As

### *The Steel Workers' Perspective on the 1998 Crisis*

There were several reasons U.S. steel workers reacted so strongly to the 1998 crisis. First, steel workers believed that they had paid their dues. U.S. steel companies and workers had gone through fifteen years of painful restructuring that had resulted in a much stronger and leaner U.S. steel industry. But increased productivity came at a heavy cost. With steel shipments remaining level, more efficient steel-making resulted in a dramatic drop in employment. Between 1979 and 1994, total steel industry employment fell 58 percent, a loss of more than 330,000 jobs.

Second, at a time when they believed that they should have been reaping the benefits of a strong U.S. market, steel workers were instead facing layoffs, shorter shifts and reductions in pay. The U.S. steel market was not in the throes of a cyclical downturn—demand in the U.S. market increased in 1998, up six percent compared to 1997, a year in which demand was already strong. However, with so much foreign supply entering the U.S. market, prices declined in the face of increased U.S. demand.

Finally, steel workers believed that maintaining a strong domestic steel industry was important to the nation. As Jerry Bugg, President of USW, Local 1053 said, "Steel is a critical industry for the United States—critical for the economy, critical for our defense. Cut the basement out of the house and it won't be long before you'll have the roof down on your head."

economies collapsed, demand for steel in Asia quickly dried up. Asian steel producers and traditional exporters to the region, such as Russia and Brazil, needed to find other markets and turned to the United States and Europe, where demand was still strong. The situation was further exacerbated as the Asian financial crisis went global, spreading to Russia and Brazil by mid-1998.

One would have expected U.S. imports to increase as a result of these financial crises. Few, however, anticipated the magnitude of the increase in imports that took place in 1998. A large amount of steel was diverted to the United States from other markets as imports increased 33 percent over 1997 (which had been a record year for U.S. imports).<sup>12</sup> The largest increases came from Japan, Korea, and Russia. Imports from these three countries alone accounted for 76 percent of the 9.4 million MT increase in total U.S. steel imports.

The 1998 steel crisis was not simply an issue of increased volume. Imported steel was coming in at extremely low prices in many instances, assisted by the declining value of foreign currencies that buoyed dollar-denominated export revenue in home currency units. Led by Japan and Russia, and often followed by Korea and Brazil, it appeared as if foreign producers were trying to beat each other in a race to the bottom.<sup>13</sup> As Nicholas Tolerico, executive vice president of Thyssen Inc. (Detroit), the U.S. importing and processing division of Thyssen AG (Germany), noted during the crisis, "I've seen fliers advertising Japanese-quality steel at Russian prices. There's only one place for the Russians to go: even lower."<sup>14</sup>

It's bad enough to lose money when the market is down. But we were at the height of the market from the demand side, so that all this happening [the lost orders, sharp price declines, subsequent financial losses and layoffs] is doubly unfortunate when you consider you're in a cyclical market.

Fred Rocchio, President  
Northwestern Steel

By the second half of 1998, steel prices in the U.S. market had plummeted, falling to levels well below where U.S. companies could price profitably. Strikingly, this occurred while demand for steel in the U.S. market was booming. Although the General Motors strike in mid-1998 caused some uncertainty just as increasing imports began to hit U.S. soil, overall demand was strong in 1998 and remained strong in 1999. Nevertheless, U.S. steel companies, which had been profitable in 1997 and early 1998, faced significant losses by early 1999.

### *The Economics of the Steel Industry*

The steel industry is characterized by high fixed costs and relatively inelastic demand, particularly in the short term. Because a large proportion of steel mill costs are fixed, producers have a strong incentive to maintain or increase capacity utilization. In addition to large capital investments, many of the major costs associated with the operation of a facility are fixed (*e.g.*, depreciation, costs associated with starting up blast furnaces). These factors put pressure on companies to keep mills running even when market signals may be indicating the need for production cutbacks, the temporary idling of facilities or even the elimination of capacity. Once a mill is idled, it is very costly to restart production. Thus, mills may continue running even when prices fall below average total costs, or even below marginal costs. While output can be reduced, each reduction raises the cost per ton of steel produced.

Construction of a large integrated steel mill runs into the billions of dollars. Even for a much smaller mini-mill, construction and equipment costs run into hundreds of millions of dollars, especially since the advent of the hot-rolled coil flat-rolling mini-mills with downstream processing (*e.g.*, cold-rolling and galvanizing lines), and upstream material facilities (*e.g.*, direct-reduced iron production). Increasingly, in the United States and other industrialized countries, labor is a fixed cost as well, due to substantial legacy costs relating to former employees, and labor contracts that have emphasized job security over wage and benefit hikes.

With respect to demand, a number of factors limit the elasticity of steel demand in the short term. These include automotive model-year plans and, more generally, material processing constraints associated with end user equipment. In the short term, manufacturers cannot easily switch to steel from other inputs, even if steel becomes more attractive due to falling prices. For example, steel frame housing construction can be economical during periods when lumber prices are high and steel prices are low. However, given the dominance of wood frame construction and the price volatility of both commodities, builders may be unwilling to invest in the special equipment and training needed to make the switch.

These cost and demand realities of the steel business lead to situations where sudden sharp declines in demand put severe pressure on market prices for steel products as producers fight to maintain or gain market share. When demand slumps, companies are reluctant to incur the costs associated with idling and restarting mills, and so may be willing to reduce prices to marginal costs in order to maintain capacity utilization. Added to these costs are also long-standing structural problems, such as significant overcapacity in the global steel industry, government assistance to maintain older capacity, barriers to imports, anticompetitive practices and, in some countries, the direct or indirect involvement of the government in the steel industry. The result is the suppression of prices during times of crisis and even over the long term. Such price suppression contributes to the generally low levels of return on investment that steel analysts have noted and that steel industry figures have complained about.

The increasing globalization of the steel industry has meant that firms must adapt to demand conditions in other markets. In open steel markets, such as the United States, steel companies find themselves facing pressures caused by collapsing markets on the other side of the world, pressures which may quickly undercut strong or healthy market conditions at home. Such pressures may be further exacerbated if structural conditions in other countries insulate those markets from the effects of the economic conditions of the global steel market, and help explain the recurring concerns over trade practices in the steel industry.

Given the strong demand in the U.S. market, U.S. steel companies expected to be able to build a cushion for the lean years that tend to follow in a cyclical industry like steel. Instead, they were losing money on sale after sale. As 1998 came to a close, what started as a promising year for the U.S. steel industry ended with the industry in crisis.

## 1997: A Cloud Behind Every Silver Lining

In 1997, the financial health of the U.S. steel industry, the strong U.S. market, and the forecast of more good times to come masked problems in the global steel industry. Even as late as June 1998, the debate was still strong over whether the financial crisis in Asia would have a severe impact on the U.S. steel market. While some correctly predicted that economic downturn in Asia would lead to a surge in steel imports, others predicted a drop in the market share of imports in 1998 due to canceled expansion plans and export financing difficulties of producers in Asia.<sup>15</sup>

The forecasts of import declines seemed to be borne out by the trend in imports in early 1998. March 1998 import statistics, released in May, showed that imports fell in the first quarter compared to the same period in 1997, even as demand continued to rise. The first indications of an impending import surge did not appear until the release of April statistics in late June 1998. Randy Cousins, an analyst with Nesbitt Burns, commented at the time, “Consider that Asia has thrown a boulder into the world steel pond and it is beginning to ripple out.”<sup>16</sup>

### Strong U.S. Market in 1997 Results in a Good Year for the U.S. Industry

Nineteen ninety-seven was a good year for the U.S. steel industry, in fact, one of the better years for the industry during the 1990s. The healthy U.S. economy sparked increases in sales of automobiles and appliances—both heavy users of steel, particularly flat-rolled products. The economy also spawned a construction boom which, coupled with major infrastructure projects such as highway and bridge repair, led to strong markets for long products such as heavy structurals and rebar. Demand for steel products had increased steadily in the mid-1990s. 1997 was no exception. U.S. apparent consumption for total steel mill products increased almost 5 percent compared to 1996, an increase of approximately 5.4 million MT. U.S. steel mills were in high gear with capacity utilization above 85 percent throughout 1997 even though overall U.S. capacity had grown the previous three years.

Imports rose in 1997 but were largely absorbed by increasing demand. Steel imports in 1997 reached a record 28 million MT, an increase of approximately 7 percent over 1996. Yet the market share of imports increased only a slight 0.5 percent over 1996.

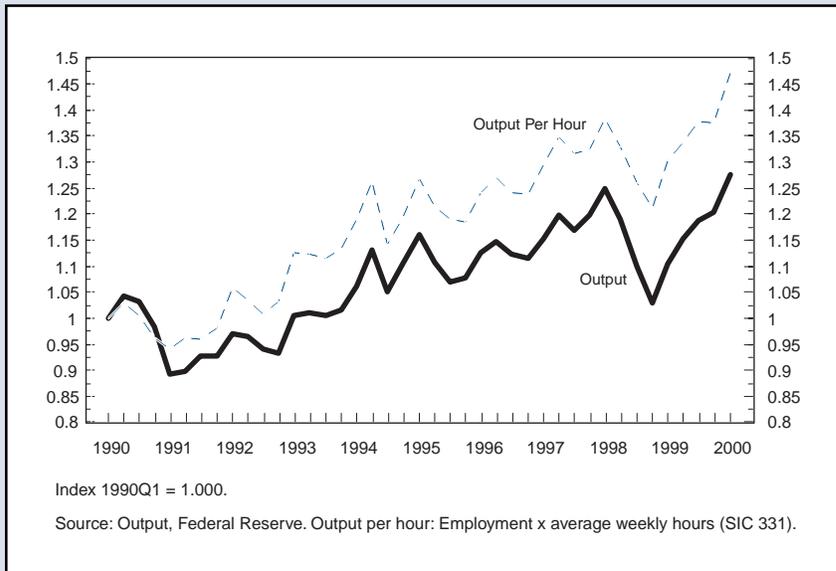
Prices were strong in 1997 with price increases in most major product lines compared to the previous year. For example, as reported by *Purchasing Magazine*:<sup>17</sup>

- Spot prices for carbon hot-rolled sheet rose 20 percent from about \$331 per MT in January 1996 to \$397 in February 1997 and then held steady through May 1997 before tapering off somewhat toward the end of 1997.<sup>18</sup>
- Similarly, spot prices for cold-rolled sheet rose 16 percent from \$474 per MT in January 1996 to \$551 in February 1997, holding steady at this price through May 1997.
- While prices for wide flange beams (a heavy structural product) initially declined in 1996 and early 1997, prices began to recover in the summer of 1997, rising 7 percent in the fall of 1997 to \$424 per MT and leveling off until the end of June 1998.

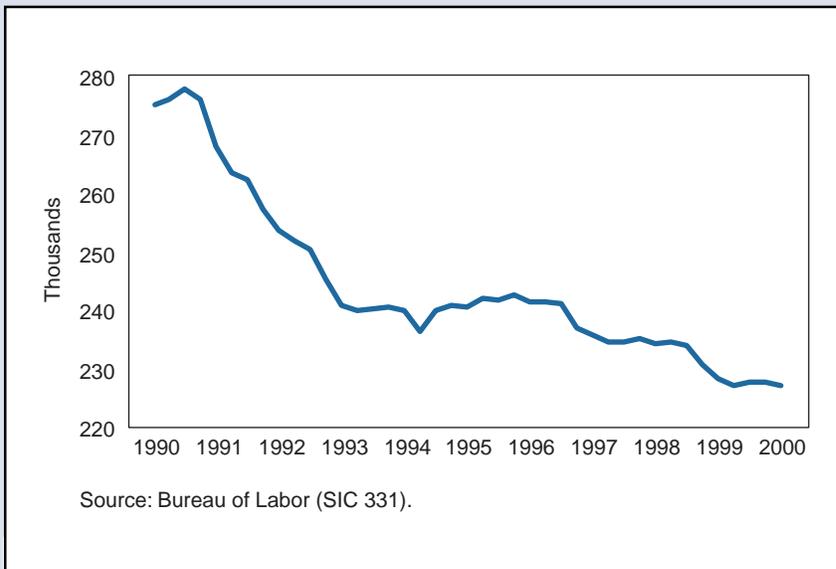
Given continued strong demand and higher prices, steel companies experienced fairly strong sales, net income and operating profits in 1997 and through the first half of 1998. Reflecting the financial health of the industry, steel industry employment remained fairly steady throughout 1997 and into early 1998, abating, at least temporarily, the long-term downward trend in steel employment<sup>19</sup> (*see box, next page*).<sup>20</sup>

## *Productivity and Employment in the U.S. Steel Industry*

Throughout the 1980s and 1990s, the U.S. steel industry underwent massive restructuring and reorganization, investing well over \$50 billion in steel plant modernization, according to an AISI estimate. The restructuring greatly increased productivity, as obsolete and inefficient mills were shut down, aging lines updated and newer, more productive plants brought on line. As steel companies became more efficient, the actual tonnage of steel shipped remained fairly steady, contributing to a decline in employment.



**2-3. Output and Productivity, Steel Mill Products**



**2-4. Employment, Steel Mill Products**

Two technological trends contributed to the increase in productivity and decline in employment. First, raw steel production shifted from the relatively labor intensive and less efficient open hearth furnaces to electric furnaces. Second, the percentage of total U.S. raw steel production continuously cast increased from 65 percent to 96 percent between 1989 and 1998. Recent developments in thin slab casting by Nucor Corp. and other mini-mills have pushed productivity in flat-rolled steel production up even further.

The industry also saw a significant shift in demand for steel in the United States in the 1980s and early 1990s as the demand for smaller, lighter automobiles and the growing use of steel substitutes such as aluminum and plastic took hold. This downward trend reversed prior to the 1998 crisis. Steel demand, as measured by apparent consumption, had been strong since the mid-1990s, and in 1998, demand increased by 6 percent compared to 1997. But the recent increases in steel demand did not offset the decades-long decline in steel employment.

These productivity increases and shifts in demand over the past two decades have resulted in a significant decline in employment in the steel industry. In the fifteen years between 1979 and 1994, total steel industry employment fell 58 percent, from 570,500 to 239,200, a loss of 331,300 jobs. However, by the mid-1990s, the major restructuring efforts were complete, and the sharp drops in employment leveled off.

While finished steel product shipments, as of the late 1990s, were down only slightly from the peaks of the early 1970s, employment in the industry had fallen by more than 60 percent. According to AISI, man-hours per ton of finished steel decreased from about ten in the early 1980s to well below four by the late 1990s.

With few inefficient producers left, a very lean and highly productive U.S. steel industry emerged. It is in this context that the industry saw an abrupt decline in employment in 1998 when thousands of steel workers were laid off at the end of the year.

## **Storm Clouds on the Horizon**

### **Financial Crisis in Asia**

The financial crisis in Asia began in mid-1997 in Thailand and quickly spread to Malaysia, Indonesia, the Philippines and Korea. In country after country, currencies collapsed and stock prices plummeted despite efforts at intervention. During the last half of 1997, the Thai baht lost 49 percent of its value against the dollar, while the Malaysian ringgit, Indonesian rupiah, Philippine peso, and Korean won lost 35 percent, 44 percent, 34 percent, and 48 percent of their values, respectively.<sup>21</sup> In the same six-month period, Thai stocks fell 29 percent while stocks in Malaysia, Indonesia, the Philippines, and Korea fell 45 percent, 45 percent, 34 percent, and 50 percent, respectively.<sup>22</sup> Banks began to fail due to over lending and the high costs incurred through dollar denominated debt payments which could not be met after very large currency devaluations.

The crisis was the worst economic downturn in the region in thirty years. Three countries—Thailand, Indonesia, and Korea—sought International Monetary Fund (IMF) assistance. In August 1997, Thailand agreed to an IMF Program that included a \$17 billion package of loans, provided by the IMF, World Bank, Asian Development Bank, and selected governments. In October, Indonesia agreed to an IMF loan that included \$40 billion in multilateral and bilateral support. In December, Korea agreed to \$57 billion in multilateral and bilateral support. The economic policies pursued under the IMF-supported program, combined with emergency financial support, helped these countries begin the slow and painful process of economic recovery.

In the first year of the crisis, an additional 40 to 50 million people in the region fell below the poverty line, not only in Indonesia and the Philippines, but also in Korea, Thailand and Malaysia, countries that had made considerable strides in alleviating poverty.<sup>23</sup> Millions of children in the region left school as a result of the crisis to either work as laborers or beg on the streets.<sup>24</sup> Fears of widespread hunger and malnutrition in Indonesia arose as government officials in 1998 estimated that 100 million Indonesians, close to half the nation's population, would be unable to afford food and basic necessities by year's end.<sup>25</sup>

In the years prior to the financial crisis, the massive amount of available capital in Asia encouraged unsound lending practices, which were exacerbated by government interference in the financial sector, crony capitalism, and corruption.<sup>26</sup> Foreign lenders had been rushing in to take advantage of new opportunities in a growing region. For example, total foreign debt in Korea almost tripled between 1992 and 1997, increasing from roughly \$43 billion at the end of 1992 to \$121 billion at the end of 1997.<sup>27</sup>

This “easy money” led to extensive borrowing for risky investments in real estate and industrial capacity, especially in the automobile, petrochemical, semiconductor and steel sectors. Companies became highly leveraged. As the *1999 Economic Report of the President* concluded, “Borrowers that should have been foreclosed upon, or at least cut off from further lending, were allowed to continue borrowing, which increased their losses and those of their banks.”<sup>28</sup> In Korea, the average debt to equity ratio for the top thirty industrial conglomerates (or chaebols) in 1996 was 387 percent, ranging from 250 percent to 8,500 percent. By 1997, this average rose to 519 percent.<sup>29</sup> In contrast, the average ratio in the United States was 70 percent.<sup>30</sup>

Easy credit led to substantial overcapacity in the manufacturing sector before the financial crisis began. By 1997, uncompetitive investments in capacity expansion projects resulted in severe gluts in regional steel, semiconductor, petrochemical, and automobile markets.<sup>31</sup>

- Thailand had estimated excess capacity of 192 percent in the automotive industry, 195 percent in the petrochemical industry, and 150 percent in the steel bar industry.<sup>32</sup>
- In Korea, according to the Organization for Economic Cooperation and Development (OECD), an investment-led boom in 1994 and 1995 gave way in 1996 to falling prices in several important export sectors. As stated by the OECD, “There is little doubt that over-capacity in key industries was a major structural weakness of the Korean economy, and that the excessive private debt which contributed to its build-up was a factor in rendering the economy vulnerable to the crisis.”<sup>33</sup>
- The *1999 Economic Report of the President* also discussed the relationship between the region’s financial practices and overcapacity. “It appears, for example, that some Asian firms, unchecked by external market discipline, developed excess capacity in industries such as steel and electronics. Many Asian economies are currently struggling to overcome the adverse real consequences of these misguided financial decisions.”<sup>34</sup>

Large shares of bank lending for real estate fueled a construction boom, particularly in office buildings and luxury condominiums.<sup>35</sup> An analysis of Bangkok in late 1994 noted that 62 percent of the 4 million square meters of office space had been added since 1992. The analysis predicted another 3 million square meters to be built by the end of 1997, despite the fact that the vacancy rate at the time was already 20 percent.<sup>36</sup>

The financial systems that had helped drive high growth rates during the 1990s were themselves highly dependent on sustaining those growth rates. As time went on, abundant credit led to more and more speculative ventures or noncompetitive expansion projects.<sup>37</sup> Companies with heavy debt loads became ever more vulnerable to even slight economic downturns.<sup>38</sup> The high proportion of foreign loans left them vulnerable to currency devaluations.

As returns on investment dwindled and growth rates in the region declined, companies were unable to meet their loan payments. In early 1997, major bankruptcies revealed the extent of the underlying structural problems in the corporate and financial sectors behind the miracle growth in the region and provided a glimpse of the problems to come.<sup>39</sup> As weaknesses of the financial systems in each country were exposed, domestic and foreign investors began leaving, resulting in capital flight and extreme pressure on these countries’ currencies. Panic set off a spiral of currency devaluations, stock crashes and bankruptcies that rippled throughout the region. By the end of 1997, what might have been a series of isolated national economic downturns quickly turned into a regional crisis poised to spread throughout the global economy.

### **Financial Crises in Russia and Brazil**

**Russia.** By early 1998, the Asian financial crisis began to have an impact on Russia by driving world oil and gas prices down. Because these sectors had accounted for 43 percent of Russian exports, Russia’s export earnings fell, putting pressures on currency reserves. Russian steel exports to Asia also began to fall, putting further pressure on foreign currency revenues. The Asian financial crisis undermined investor confidence in emerging markets including Russia and led to a reduction in foreign and domestic investment.

In mid-1998, financial crisis hit Russia. The long-term inability of the Russian government to balance its budget caused it to respond by issuing an ever-increasing amount of government bonds and by not paying its workers, soldiers, or pensioners. More than 40 percent of the budget expenditures in August 1998, for example, were earmarked for debt service.<sup>40</sup> Interest rates on short-term bonds climbed to 200 percent as the Russian government tried to maintain capital inflows. Eventually, the lack of confidence in the government's ability to repay its debt caused investors to pull out of the bond market. With no money coming in, the Russian government could no longer support its debt. On August 17, 1998, the government announced a ninety-day moratorium on external debt repayments and a de facto devaluation of the ruble. Within days, the ruble lost 30 percent of its value. These events had serious economic and political ramifications for the country and its struggle toward a market economy. By mid-October, the Russian stock market was down 88 percent from its January 1, 1998, level, and the ruble had lost two-thirds of its value.<sup>41</sup> When the ruble finally stabilized in early 1999, it had lost 74 percent of its value.<sup>42</sup>

**Brazil.** A financial crisis also hit Latin America, precipitating regional economic declines, sharp drops in commodity prices, and distortions in global trading relationships. Losses from the Russian stock market crash forced many investors to pull money out of Brazil to meet margin and other calls for their assets. After the Asian and Russian debacles, investor perception was that the South American economies, particularly Brazil, would not be spared.

When the Brazilian real came under attack in mid-1998, the Brazilian government raised short-term interest rates to almost 50 percent in an attempt to stall or prevent the currency's collapse. Many market analysts believed that the steps taken by the Brazilian government undermined the confidence of foreign investors and led to the real's dramatic devaluation in early 1999.

With major steel-producing countries such as Korea, Russia, and Brazil locked in a financial crisis and with Japan, the world's third largest steel-producing country, entering its eighth year of economic downturn, the stage was set for a global steel crisis.

### **Financial Crises Trigger the U.S. Steel Crisis**

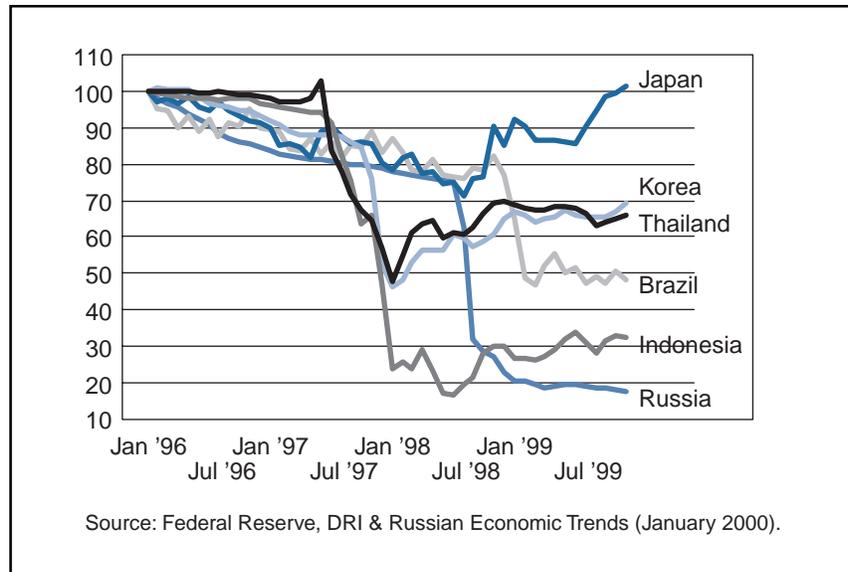
Changes in three short-term variables in 1997 to 1998—a reduction in Asian steel demand, a fall in Asian currency values, and an increase in U.S. steel demand—are key to understanding what triggered the U.S. steel crisis. While in theory these variables could have been either reinforcing or offsetting, in 1998 they individually and collectively contributed to an increase in U.S. steel import volumes.

**Effects on Asian Steel Producers.** The Asian financial crisis severely curtailed economic activity in many Asian countries, depressing demand for steel in the construction and manufacturing sectors. The crisis was particularly severe given its suddenness and magnitude, due in large part to the fact that it came at a time of robust and sustained economic growth and high expectations. Asian steel producers faced not only shrinking domestic markets, but shrinking regional export markets as well, and were left to find new buyers for their steel products.

Currency devaluations made Asian steel producers' products more competitive from a price standpoint, but not in the same markets and not necessarily to the same degree. For example, between January 1996 and the middle of 1998, the yen, the won, the rupiah and the baht all fell in value, but at different rates. In dollar terms, the Indonesian rupiah fell the most (83 percent), followed by the Korean won (44 percent), the Thai baht (40 percent), and the Japanese yen (26 percent) (*Chart 2-5*).<sup>43</sup>

**Effects on Russian and Brazilian Producers.** Asia was a major export market for both Brazil and Russia. When Asian steel markets contracted, Brazilian and Russian steel producers, like their Asian counterparts, were left to find new buyers for their steel products.

Russian and Brazilian steel producers initially faced the additional problem of a loss of price competitiveness vis-à-vis their Asian competitors as Asian currencies fell against the ruble and the real. Their competitive position improved with depreciations of both the ruble and the real in the second half of 1998, which came at a time when many of the Asian currencies had already begun to rebound. Although the depreciation of the ruble came too late in 1998 to be a factor in U.S. steel crisis, the ruble and real depreciations gave Russian and Brazilian steel exporters a significant price advantage in virtually all steel markets in which they competed, both in Asia and in the United States.



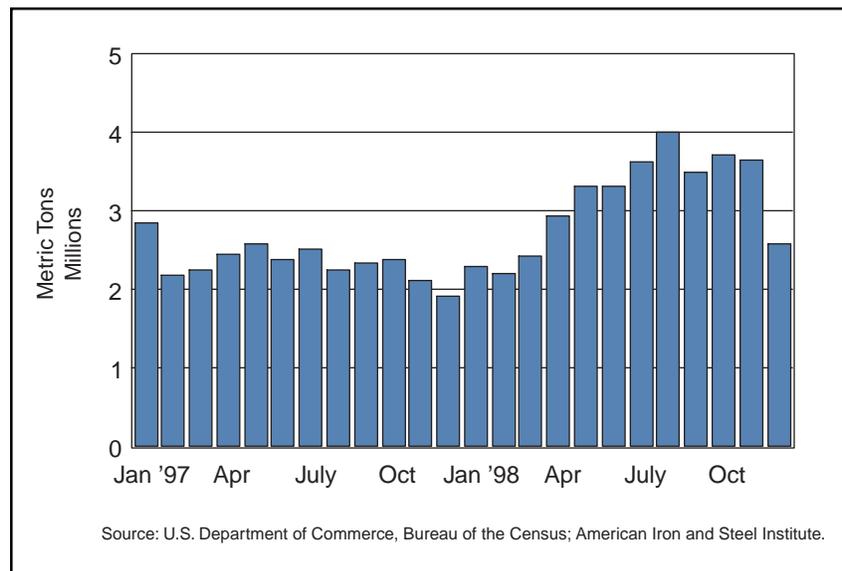
**2-5. Index of Currency Values: 1996–1999**  
(Based on Exchange Rates, January 1996=100)

In light of the initial devaluation of Asian currencies, steel producers in Russia and Brazil likely saw rising U.S. demand and the strong U.S. steel market as their best opportunity.

## 1998: U.S. Industry in Crisis

### Up Sharply in April, Imports Climb Steadily Throughout the Year

Beginning in April 1998, steel imports began to rise dramatically, up 21 percent from both March 1998 and the previous April. By the end of 1998, steel imports had increased to almost 38 million MT, a 33 percent increase over the 28 million MT imported in 1997, the previous record year for imports (*Charts 2-6, 2-7*).



**2-6. U.S. Imports of Steel Mill Products**

Foreign producers have said that they were simply meeting the rising demand in the United States during 1998, demand that they claimed U.S. steel mills were unwilling or unable to supply. General Motors has noted that starting in late 1997, parts suppliers were reporting that certain U.S. steel makers were placing customers on allocation and encouraging them to look elsewhere for additional product.<sup>44</sup> Similar

concerns regarding purchase allocations and potential shortages were raised with respect to the structurals market.<sup>45</sup>

Strong U.S. demand certainly made for an attractive U.S. market. However, the increase in steel imports into the United States far outstripped the 6 percent increase in U.S. demand. Steel imports increased by 9.40 million MT, compared to an increase of 6.75 million MT in U.S. steel demand—an overhang of almost 40 percent. This pattern held true for individual product categories as well. Demand for

hot-rolled steel in 1998 grew by 3.5 million MT, while imports increased by 4.6 million MT. Demand for structural steel in 1998 increased by 1.2 million MT, while imports increased by 1.6 million MT. With respect to import levels, Father William Hogan, director of Fordham University’s Industrial Economics Research Institute and a noted industry expert, stated:

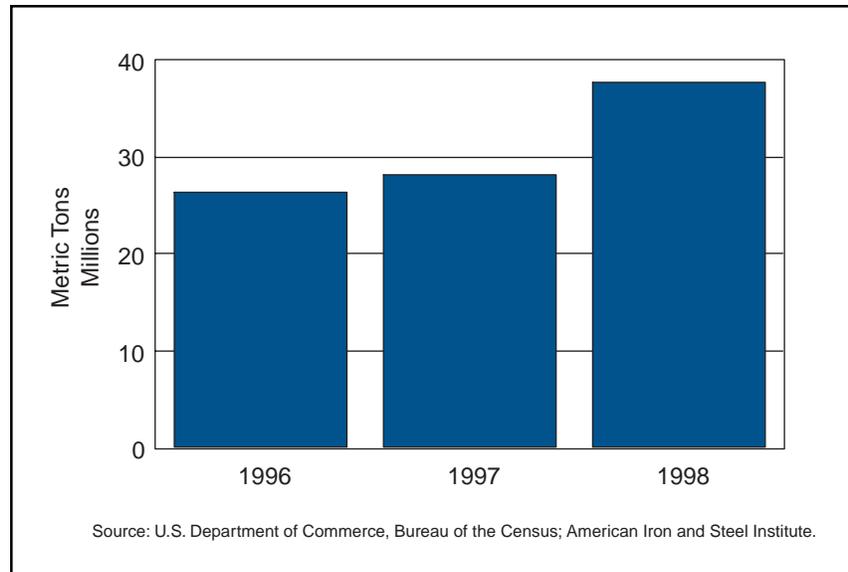
I cannot conceive of any situation where the United States would need 20 to 30 million net tons of finished steel imports. From a peak demand standpoint, the United States would need only about 10 to 15 million net tons of imports, given current U.S. finished steel product capacity.<sup>46</sup>

Because the U.S. market could not absorb the import oversupply, U.S. steel mill inventories rose approximately 5 percent by December 1998 compared to pre-crisis levels in autumn 1997. By mid-1999, inventories were up 11 percent compared to autumn 1997 levels.<sup>47</sup> Service center inventories rose approximately 20 percent from the second half of 1997 to the end of 1998—from an average of roughly 6.5 million MT to almost 8 million MT.<sup>48</sup>

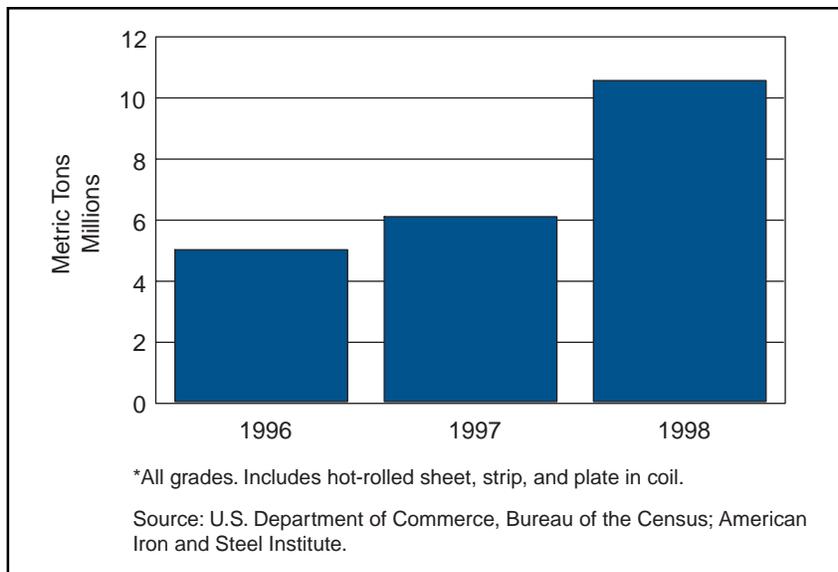
Noting concerns about steel price declines in the face of strong U.S. demand, as measured by the increase in U.S. apparent consumption to about 130 million MT in 1998, James Collins, former president and now policy advisor to the Steel Manufacturers Association, said:

In that phrase “apparent consumption,” the key word is “apparent.” For we know the U.S. market will not have consumed 130 million tons of steel in 1998. How many excess tons are sitting on docks, in bonded warehouses, or in the inventories of service-center distributors? Many are guessing that the overhang on the market is at least 5 million tons of finished steel, certainly enough to depress steel prices to levels below costs of production for many U.S. producers. 1998 is turning into a year in which 9 to 10 million tons of additional imported steel, over and above the 31 million tons imported last year, is the straw that broke the camel’s back.<sup>49</sup>

Anecdotal evidence suggests that a buildup of inventories may have also taken place among nontraditional holders of steel, such as traders and importers. Some market observers have alleged that importers brought in and warehoused large quantities of steel during 1998 at the low prevailing prices to avoid problems associated with future trade cases. These observers reported large inventories built up right at or near the



**2-7. U.S. Imports of Steel Mill Products**



**2-8. U.S. Imports Of Hot-Rolled Steel\***

No one can recall a time when U.S. steel prices have fallen this far this fast in a period of record U.S. market demand.

Peter Kelly, CEO, LTV Steel,  
before Senate Finance Committee

ports, presumably in large part by traders.<sup>50</sup> In New Orleans, steel was being piled up wherever there was room, both inside the warehouses and outside in parking lots and along the roads. As noted by New Orleans port official Robert Landry at the time of the crisis, “We’re using every square inch we have for cargo, and most of it is steel.”<sup>51</sup>

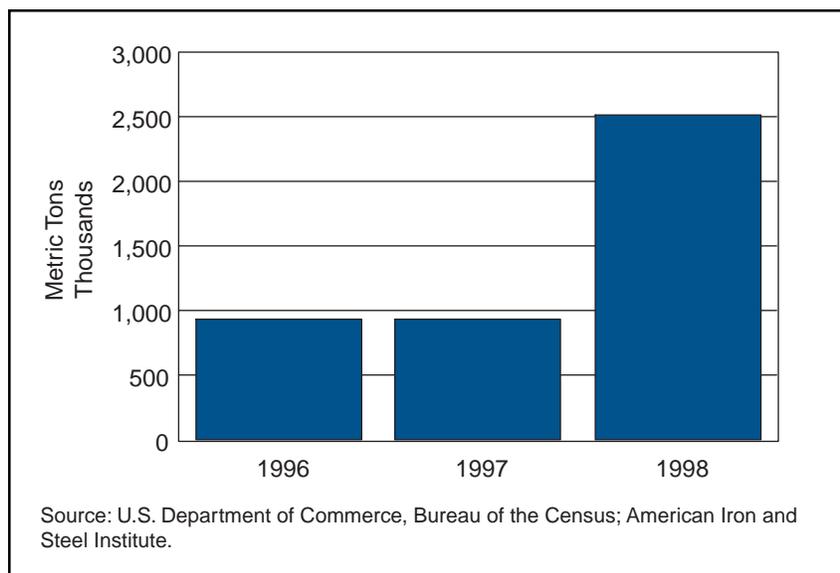
As the imports arrived, they not only exceeded U.S. demand, but also took significant market share. In particular, imports of finished steel products increased 40 percent, accounting for

roughly 9 million MT of the 9.4 million MT increase in steel imports. The import penetration level for finished steel (*i.e.*, the share of the U.S. market accounted for by imports) climbed to 33.4 percent in November 1998—up from 23 percent in March and the highest monthly level in more than twenty years. At the same time, U.S. capacity utilization fell considerably, indicating that increased imports were not merely filling a void that U.S. producers could not fill. Import increases occurred across all segments of the domestic industry. While the

increases in flat-rolled products, particularly hot-rolled steel, received the most attention, dramatic increases occurred in a variety of long products and pipe and tube (*Charts 2-8, 2-9, 2-10, 2-11, 2-12*).

### Import Surge Traceable to a Few Countries

Three countries—Japan, Korea, and Russia—accounted for the vast bulk of the import increases in 1998. Compared to 1997, steel imports rose 162 percent from Japan, 108



**2-9. U.S. Imports of Heavy Structural**

percent from Korea, and 59 percent from Russia. These three countries alone accounted for 7.13 million MT, or about 76 percent of the overall 9.40 million MT increase in steel imports in 1998 (*Chart 2-13*).

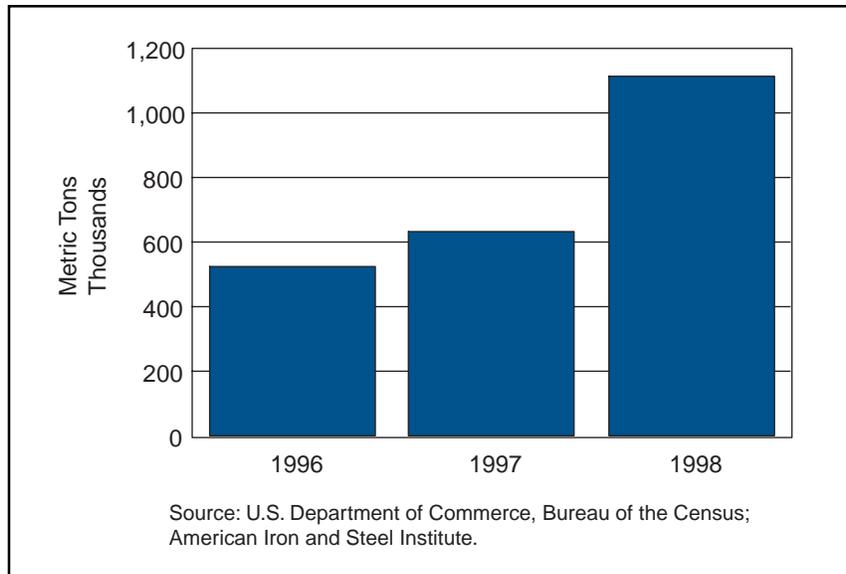
In sharp contrast to the large import increases from Japan, Korea, and Russia, 1998 imports from other major foreign steel suppliers to the United States fell or remained at roughly the same level.

- Imports from the EU fell 4 percent.
- Imports from Mexico fell 5 percent.
- Imports from Canada increased slightly, up 3 percent compared to 1997.

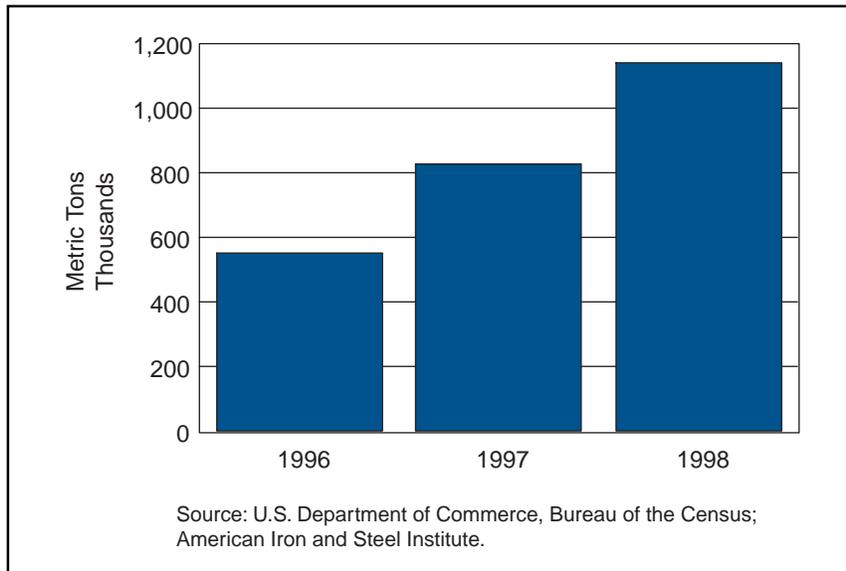
### As Imports Rise, Prices Tumble: Product-by-Product Review

An examination of individual product categories underscores the major role that imports from Russia, Japan and Korea played in 1998. Although imports from each of these countries did not necessarily surge in every product category (*e.g.*, Russian import increases were confined primarily to hot- and cold-rolled steel, while imports of Korean hot-rolled steel fell in 1998),<sup>52</sup> in most product categories, rising imports from one or more of these three countries were a significant factor behind the overall increase in that product category.<sup>53</sup>

The increases in imports, coupled with aggressive pricing by suppliers of Russian,



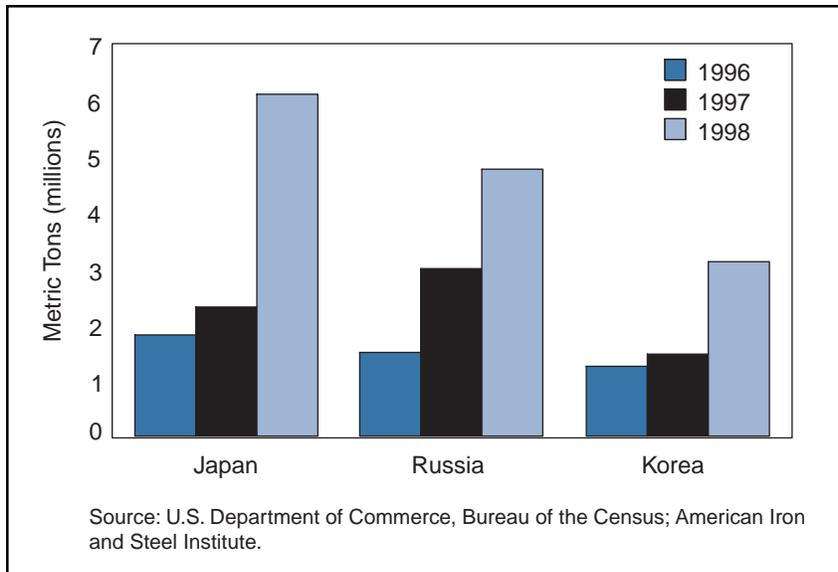
2-10. U.S. Imports of Rebar



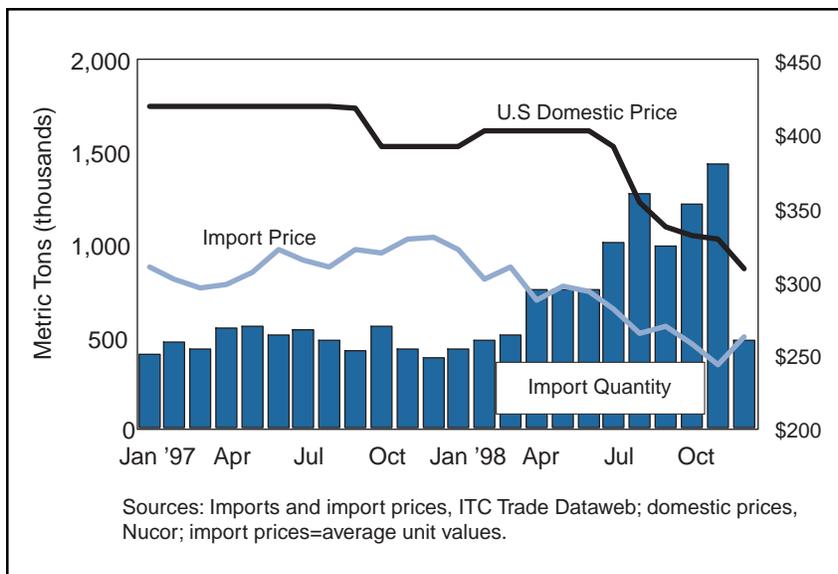
2-11. U.S. Imports of Line Pipe

Product Group	1997 Imports (metric tons)	1998 Imports (metric tons)	Percent Change 1997–1998
Total Steel Mill Products	28,264,788	37,666,050	33
Finished Steel	22,496,615	31,519,107	40
Hot-rolled Steel	6,092,967	10,608,242	74
Cold-rolled Steel	3,699,821	4,055,110	10
Cut-to-length Plate	1,259,123	1,927,470	53
Heavy Structural	933,170	2,518,343	170
Rebar	636,218	1,115,118	75
Line Pipe	832,014	1,141,965	27

Source: U.S. Department of Commerce, Bureau of the Census; American Iron and Steel Institute.



**2-13. U.S. Steel Imports from Japan, Russia & Korea (1996-1998)**



**2-14. U.S. Imports of Carbon Hot-Rolled Steel Products (1997-1998)**

Japanese, Korean, and Brazilian steel led to a dramatic drop in U.S. steel prices despite increased demand. A product-by-product review of prices shows how the crisis developed.

### Hot-Rolled Steel

The first indications of aggressive pricing tactics came in the spring of 1998, particularly on the West Coast where increased imports of hot-rolled steel from Japan and plate and line pipe from Korea first appeared. Overall prices for imported hot-rolled steel fell 18 percent, by \$59 per MT (*Chart 2-14*).<sup>54</sup> Prices for hot-rolled steel from Brazil, Japan and Russia fell as much as 24 percent, 27 percent, and 23 percent, respectively from their highs in January to their lows the last three months of 1998.<sup>55</sup>

Prices for hot-rolled steel from Russia and other nonmarket economies (which are traditionally lower because of perceived quality differences for these products) fell even lower in 1998, causing concern not only for U.S. integrated producers but also for many mini-mill producers. In August 1998, John Correnti, then CEO of Nucor (the largest U.S.

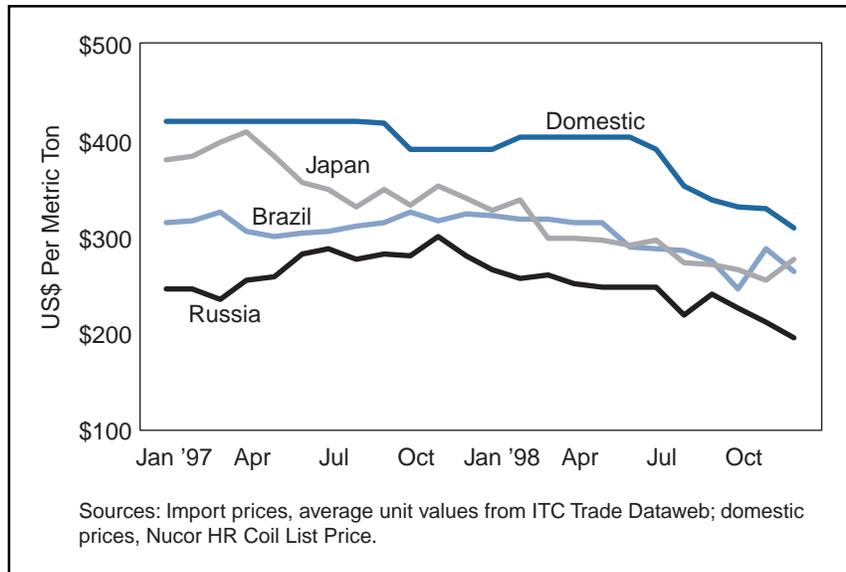
mini-mill and one of the lowest cost producers), wrote in a letter to Commerce Secretary Daley, “These [Russian mills] are some of the least efficient mills in the world and we have no idea how they can afford to sell steel at these prices.”<sup>56</sup>

Russian prices apparently became a target for exporters of Japanese and Brazilian hot-rolled steel (*Chart 2-15*). Pressure to match the Russian import price in the United States was also noted by a number of steel service centers and distributors who reported receiving faxes from Japanese companies offering to provide Japanese-quality steel at Russian prices. The press also reported on this pricing pressure.<sup>57</sup>

**Dumping Cases.** In September 1998, twelve steel companies, along with the United Steelworkers of America and the Independent Steelworkers Union, filed dumping petitions on imports of hot-rolled steel

from Brazil, Japan, and Russia.<sup>58</sup> A countervailing duty petition on imports of these products from Brazil was filed at the same time.

- Imports of hot-rolled steel were found to have been dumped at substantial margins in all three investigations: from 41 to 43 percent for Brazil, 18 to 67 percent for Japan, and 74 to 185 percent for Russia.<sup>59</sup>
- The dumped imports of hot-rolled steel were also found to have injured the U.S. industry. In its final affirmative injury



**2-15. Carbon Hot-Rolled Steel, U.S. Import vs. Domestic Prices**

determination on hot-rolled steel from Brazil, Japan and Russia, the ITC found that imports from these countries suppressed prices in the U.S. market.

U.S. firms reported that they generally reduced prices and/or rolled back announced price increases to avoid losing sales to competitors selling imports from the three subject countries. Despite these cutbacks, U.S. firms reported losing \$423 million in sales.<sup>60</sup>

Imports were not the sole factor behind price declines or industry woes. Other factors—including preexisting problems, increased domestic competition, and the strike at General Motors during the summer of 1998—played a role as well.

**Preexisting Problems.** Although 1997 was a good year for the U.S. steel industry, some U.S. companies were facing problems with start-up operations or were in the midst of modernization efforts that left them vulnerable to the events of 1998. Adam Ritt, the executive editor of *New Steel*, cautioned steel makers against using imports as the sole explanation for the industry’s problems:

Imports set a record last year, and a significant portion of the steel was dumped or otherwise sold in violation of trade laws. Domestic steelmakers are right to object to unfairly traded imports that have led them to lay off thousands of workers and idle facilities. They’re right to tell the government and public how they’ve been injured in campaigns such as Stand Up for Steel.

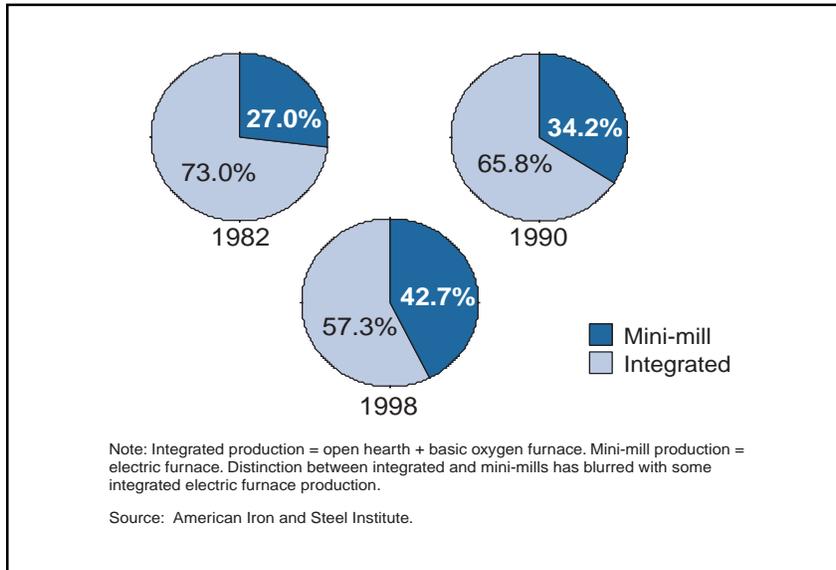
But in telling this story, we run the risk of allowing steelmakers’ other problems to stay in the shadows. This would be a disservice to workers, shareholders, and the public. Some of the companies that are most troubled today, including Acme Metals, Laclede, Geneva Steel, and Northwestern Steel and Wire, had problems dating to before the current imports crisis.<sup>61</sup>

In his editorial, Ritt noted that the rough start-up of Acme’s new thin-slab mill and the incomplete modernization efforts at Geneva Steel had caused both companies problems prior to the import crisis and were at least partially to blame for the companies’ current woes.<sup>62</sup>

**Domestic Competition.** Some have suggested that domestic competition between large integrated mills and more efficient mini-mills<sup>63</sup> was the driving force behind the drop in U.S. steel prices in 1998.

Industry restructuring in the 1980s and 1990s led to an increasing mini-mill presence in the U.S. industry. Initially producing low end products such as concrete reinforcing bar (rebar), mini-mills now produce a wide range of products including hot-rolled sheet, cold-rolled sheet, plate-in-coils, wide-

flanged beams and high quality bar products.<sup>64</sup> Cost advantages and willingness to price aggressively had resulted in mini-mills dominating certain segments of the market such as high quality bar or, in the case of rebar and structural beams, taking them over completely from domestic integrated producers.<sup>65</sup>



**2-16. Share of Raw Carbon Steel Production, Integrated vs. Mini-mill**

According to this theory, sharp declines in scrap prices set the stage for the 1998 crisis. The mini-mills' significant cost advantage on their chief input product enabled them to price aggressively in order to increase sales and market share (*Chart 2-16*).<sup>66</sup> Unable to meet low mini-mill prices, U.S. integrated

producers were driven from the market and forced to lay off workers. In this scenario, steel imports did not drive down prices in the U.S. market; foreign steel companies were forced to follow the mini-mill lead or be driven from the market. There was no U.S. steel crisis per se, only a crisis for U.S. integrated producers caused by increased domestic competition within the U.S. market.

However, U.S. mini-mills did not lead the price declines for hot-rolled steel in the U.S. market. Following a small dip in the fall of 1997, prices charged by Nucor, the leading U.S. mini-mill, remained flat until the summer (*Chart 2-14*). During that same time, import prices of hot-rolled steel from Brazil, Japan and Russia fell steadily.<sup>67</sup> The role of mini-mill price competition was addressed in the ITC's injury determination in the hot-rolled steel investigation. In discussing whether increased competition within the domestic industry accounted for the price declines in 1998, the ITC stated:

It is significant that the hot-rolled steel prices of Nucor (which is regarded by the domestic industry and importers alike as an established and efficient mini-mill and widely looked to as a domestic price leader) declined dramatically during the latter half of 1998 as subject import volumes increased at their fastest rate during the period of investigation. Nucor's prices recovered only as the subject imports exited the market. These facts suggest that factors other than increased competition within the domestic industry contributed to the significant price declines in the latter part of the investigation period.<sup>68</sup>

In addition, although average scrap prices in 1998 were 17 percent below scrap prices in 1997, financial data reported by Nucor, the largest volume mini-mill producer of flat-rolled steel, suggests that the overall mini-mill cost reductions were not that large.<sup>69</sup> In its 1998 annual report, Nucor stated that "the major component of cost of products sold is raw material costs" and that the "average price of raw materials was substantially unchanged in 1998, 1997 and 1996."<sup>70</sup> Furthermore, Nucor states that "[s]crap and scrap substitutes are the most significant element in the total cost of steel" and that "their average cost in 1998 was comparable to the \$145 per gross ton in 1997."<sup>71</sup> The price relationship between scrap prices and

finished steel prices is very complex and declines in scrap prices do not necessarily lead to declines in finished steel prices.<sup>72</sup>

The explanation of 1998 as an “integrated mill crisis” ignores the fact that mini-mills were also hard hit by low-priced steel imports in 1998—in some cases, even harder than their integrated mill counterparts.<sup>73</sup> In examining the domestic industry in 1998, the ITC noted:

Indeed, the same trends for the industry as a whole are also apparent in the separate results of both integrated mills and mini-mills. . . . In fact, mini-mills fared even worse than integrated mills from 1997 to 1998. . . . The worse financial performance of [mini-mill] producers reflects in part their greater dependence on the merchant market, where imports are concentrated.<sup>74</sup>

The ITC did not find that the industry’s poor performance in 1998 was driven by increased domestic competition rather than the effect of increased imports.

Mini-mill competition was an important condition of competition in 1997, yet the domestic industry performed well that year. The incremental increase in mini-mill capacity from 1997 to 1998, particularly in light of the substantially larger increase in mini-mill capacity from 1996 to 1997, does not account for the bulk of the downturn in the domestic industry’s financial indicators from 1997 to 1998.

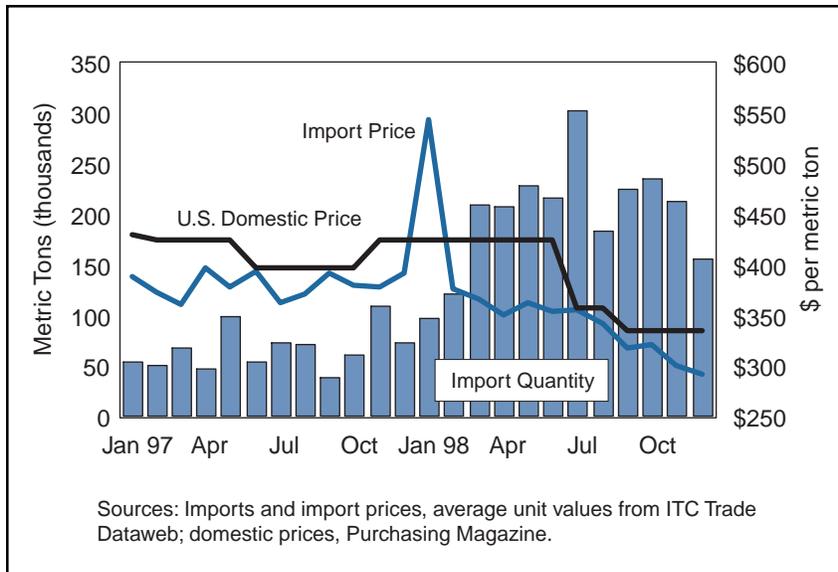
Thus, while we recognize increased competition within the domestic industry has contributed to the domestic industry’s poorer performance in 1998, it only partially explains the substantial declines in the domestic industry’s performance in 1998.<sup>75</sup>

**General Motors Strike.** The 1998 strike at General Motors also played a role in the price declines and industry misfortunes seen that year. The strike came at a sensitive time, as financial crises abroad impacted the world steel market and as U.S. imports were beginning to increase. When the strike began in June 1998, it was also unclear how long it would last and what effect it would have on U.S. mills and other suppliers.

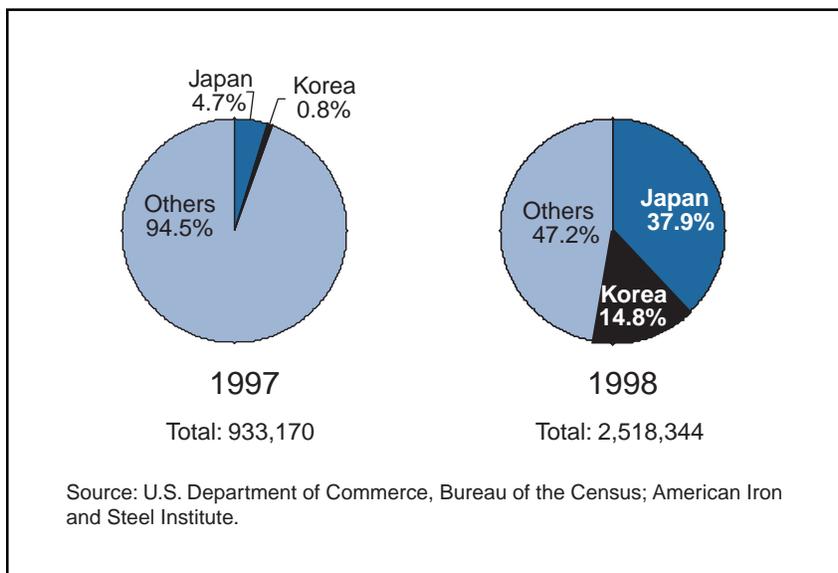
According to G. Mustafa Mohaterem, GM’s chief economist, the GM strike resulted in a considerable loss of revenue for U.S. integrated mills given the fact that GM purchases almost all of its high-quality, high-priced steel from integrated mills in the United States and Canada.<sup>76</sup> In addition, the uncertainty about the length of the strike exerted downward pressure on prices in the steel market.<sup>77</sup>

In the end, the strike lasted only fifty-four days. While some short-term shutdowns and layoffs were attributed to the strike, the strike appears to have had a relatively limited impact on the steel market outside the cold-rolled and corrosion-resistant steel segments of the industry where most of GM’s purchases are concentrated.<sup>78</sup> Taking into account increased GM purchases after the strike, mills in the United States and Canada lost roughly 400,000 MT of sales to GM as a result of the strike.<sup>79</sup> Even assuming that none of these lost sales were offset by increased steel consumption by other U.S. automakers, the lost volume represents less than half of 1 percent of total U.S. apparent consumption in 1998 and accounts for less than 1 percent of flat-rolled steel shipments.<sup>80</sup> Even during the strike, the unadjusted 620,000 MT figure only represents approximately 3 percent of total steel apparent consumption and approximately 7 percent of flat-rolled apparent consumption in those two months. For comparison purposes, the increase in imports of steel mill products in 1998, compared to 1997 exceeded 9 million MT, while the increase in imports of flat-rolled products in 1998 exceeded 5.5 million MT.

The ITC considered the effects of the GM strike in making its determination in the investigation on hot-rolled steel from Japan and acknowledged that by having some effect on overall demand in 1998, the strike



**2-17. U.S. Imports of Heavy Structural (1997-1998)**



**2-18. U.S. Imports of Heavy Structural, Share of Total Imports**

played some role in the price declines. However, at the same time, the ITC noted:

The strike only lasted five weeks and the total quantity of material not purchased during the GM strike ... was not enough to explain the kind of price declines that occurred in 1998. ... Thus, at most, we consider the GM strike to be only a partial explanation for declining prices in 1998.<sup>81</sup>

This view was echoed by other experts on the U.S. steel industry, including Father William Hogan and Frank Koelble, Director and Associate Director of Fordham University's Industrial Economics Research Institute.<sup>82</sup>

### Heavy Structural

In 1997, imports of heavy structural from Japan and Korea, combined, were less than 52 thousand MT. By the end of 1998, imports of heavy structural from these two countries exceeded 1.3 million MT, an increase of more than 2,450 percent over 1997 (Chart 2-17). In 1997, imports from Japan and Korea

accounted for less than one percent of the U.S. market. One year later, their combined share of the U.S. market increased to 19 percent and the two countries accounted for more than 50 percent of U.S. imports, up from less than 6 percent in 1997 (Chart 2-18). In early 1998, Japanese and Korean trading companies began offering wide flange beams at delivered prices to Gulf-state and Midwestern ports that were significantly below then prevailing spot prices.<sup>83</sup> As prices for domestic wide flange beams fell 21 percent in 1998 (by \$88 per MT), import prices continued to drop further, remaining below U.S. mill prices throughout 1998.

**Dumping Cases.** Nucor joined Chaparral Steel and Northwestern Steel and Wire in filing antidumping cases on imports of structural beams (a heavy structural product) from Japan and Korea. According to John Correnti, then President and CEO of Nucor, "Five to ten years ago, Nucor was not of the opinion [that] steel was dumped, but just was produced for less. In beams, that's not the case."<sup>84</sup> The U.S.

Department of Commerce determined that imports of structural beams from Japan and Korea were dumped in the U.S. market, with dumping margins ranging between 32 and 65 percent for Japan and 26 and 50 percent for Korea. The ITC has issued a final affirmative injury determination with respect to imports of these products from Japan. A decision on Korea is scheduled for later this summer.

### **Cold-Rolled Steel**

Prices for domestic cold-rolled steel fell 14 percent in 1998 (by \$72 per MT) while import prices fell 26 percent (by \$129 per MT). Cold-rolled steel prices from Brazil, Japan, and Korea fell more sharply—by 37 percent, 27 percent, and 51 percent, respectively—while Russian prices fell 10 percent.

**Dumping Cases.** After cases were filed by the U.S. industry, the Commerce Department found dumping margins ranging upward of 164 percent in the cold-rolled steel investigations against Argentina, Brazil, China, Indonesia, Japan, Russia, Slovakia, South Africa, Taiwan, Thailand, Turkey, and Venezuela. However, the ITC determined that the U.S. steel industry was not injured by imports of cold-rolled steel.<sup>85</sup> The ITC disagreed with the U.S. industry's position that production committed to joint ventures should not be used in calculating market share. The ITC included such production in determining the size of the U.S. market, and as a result, attributed a lesser degree of importance to the impact of imports and a greater degree of importance to domestic factors such as mini-mill competition and the GM strike.<sup>86</sup>

As these ITC decisions indicate, the GM strike had a greater impact on the cold-rolled and corrosion-resistant markets than it did on other segments of the steel market—approximately 80 percent of GM's purchases are of these two products.<sup>87</sup> Various service centers that deal with GM indicated they lost a considerable amount of business during the strike,<sup>88</sup> and several steel companies cited the GM strike as a factor depressing earnings in their quarterly financial statements (the strike spanned two quarters, second quarter 1998 and third quarter 1998).<sup>89</sup>

### **Stainless Steel Flat-Rolled Products**

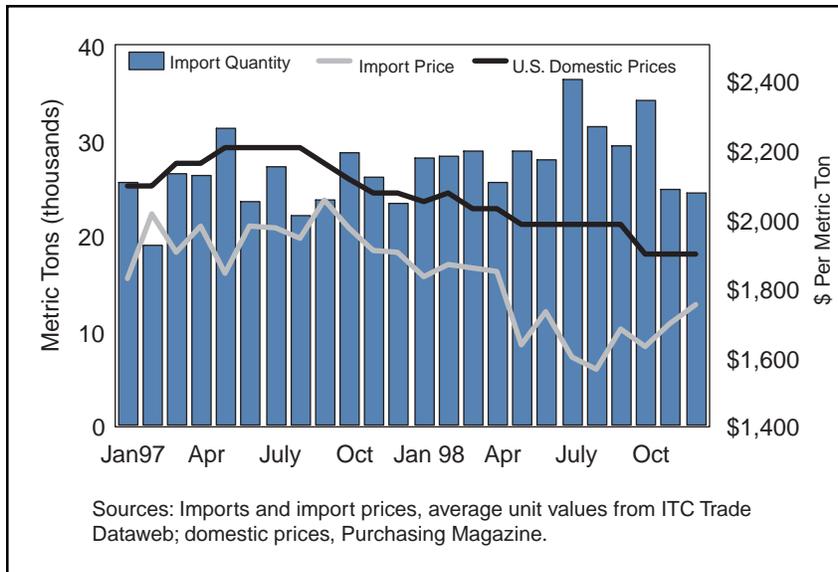
Specialty steel producers were also hit hard by low-priced imports during 1998, including producers of stainless plate-in-coils and stainless sheet and strip. Again, a familiar pattern emerged of falling prices in “an environment of almost unprecedented demand growth.”<sup>90</sup>

**Stainless Plate-in-Coils.** The specialty steel industry initially filed antidumping and countervailing duty cases against stainless plate-in-coil imports from Belgium, Canada, Italy, Korea, South Africa, and Taiwan.

- The Commerce Department found dumping margins of 16 percent in the Korean dumping investigation and issued a negative determination in the Korean subsidy investigation.
- In the remaining cases against Belgium, Canada, Italy, South Africa, and Taiwan, Commerce found dumping margins ranging between 7 percent and 45 percent and subsidy margins ranging between 2 percent and 15 percent.

The ITC determined that the U.S. industry was materially injured by dumped and subsidized imports of stainless hot-rolled plate-in-coil imports.

**Stainless Cold-Rolled Sheet.** A closer examination of the situation in 1998 for stainless cold-rolled sheet and strip provides an example of prevailing pricing pressures. U.S. imports of stainless steel cold-rolled sheet and strip were fairly even throughout 1997. Overall import prices, however, were on a continuous downward trend, from \$2,053 per MT in September 1997 to \$1,565 per MT in August of 1998—a 24



2-19. U.S. Imports of Stainless Cold-Rolled Steel

percent decline (*Chart 2-19*). U.S. domestic prices also trended downward during this period even though demand for stainless products was rising.

Imports from Japan and Korea played an important role. Japan and Korea have historically been significant suppliers of stainless steel sheet and strip to the United States. However, between 1997 and 1998, import prices for cold-rolled sheet and strip from Japan and Korea showed considerable volatility. Prices of imports from Japan fell from \$2,151 per MT in December 1997 to \$1,363 per

MT in May 1998—a 37 percent drop. Korean prices fell from around \$1,700 per MT in the last quarter of 1997 to \$1,073 per MT in November 1998—a nearly 40 percent drop. During this period, the won devalued significantly.<sup>91</sup>

In July 1998, the Commerce Department initiated antidumping and countervailing duty proceedings on imports of stainless steel sheet and strip (both hot-rolled and cold-rolled) from a number of countries, including Japan and Korea, in response to a petition filed by the major U.S. stainless steel producers.

- Commerce found dumping margins for Japanese producers ranging from 37 percent to 58 percent.
- For Korea, Commerce found dumping and subsidy margins ranging from *de minimis* to 59 percent.
- In the remaining cases against France, Germany, Italy, Mexico, Taiwan, and the United Kingdom, Commerce found dumping and subsidy margins ranging from 1 percent to 35 percent.

The ITC determined that the U.S. industry was materially injured by dumped and subsidized imports of stainless steel sheet and strip, noting that U.S. domestic price declines could be “attributed to a significant degree to the increasing volume of subsidized and LTFV [less than fair value] (*i.e.*, dumped) imports.”<sup>92</sup>

### Other Steel Products and Dumping Cases

Similar pricing patterns appear in other product lines. For example, import prices for cut-to-length plate fell 11 percent during 1998 and continued to decline in early 1999. In response, the industry filed antidumping and countervailing duty cases on cut-to-length plate imports from eight countries. The cases resulted in final affirmative decisions by both Commerce and the ITC against six countries.<sup>93</sup> Final dumping margins ranged between *de minimis* and 72 percent. Final subsidy margins ranged between *de minimis* and 48 percent.

By the end of 1999, antidumping investigations had also been filed on imports of seamless pipe from various countries and tin mill products from Japan. Commerce found dumping margins ranging from 11 percent to 108 percent in the seamless pipe investigations and from 32 percent to 95 percent in the tin mill products investigation.

## The Role of Trading Companies

Trading companies have been at the forefront of the globalization in steel trade. If trade is fair and markets are open, their role is a positive force for globalization.<sup>94</sup> But when markets are structurally distorted, trading companies are the conduit through which these distortions spill over into the global marketplace.

There are basically four means by which trading companies, at least by some accounts, made the effects of the 1998 global steel downturn worse for the U.S. market: their flexible purchasing and selling operations, their impact on certain countries' price structures, their potential for fueling speculation, and their attempts to beat antidumping duty deadlines. For the most part, these commercial practices are normal responses to market forces and factors influencing the market. With the possible exception of their role in marketing steel from Russia, trading companies usually make markets more efficient. Trading companies generally are not themselves responsible for subsidies, anticompetitive behavior, or other market-distorting practices. However, when producers, who sell to the trading companies, engage in or benefit from these practices, trading companies, inadvertently as it were, spread the market distortions to all their customers.

### Flexible Operations

Most trading companies purchase steel based on three basic market principles: the best product, the best price, and the best way to satisfy the requirements of the customer. Flexible operations help trading companies satisfy these criteria. Since global trade in steel is dominated by a relatively small number of large, multinational trading companies, they can change their suppliers with relative ease and speed, reorient their sales focus to the market with the strongest current prices (provided that market is open), and sell to different customers on the spot market. Some trading companies, particularly Japanese traders, that act as the distribution arm of a particular steel maker or makers may be restricted to purchasing steel produced by those companies (*see box*). However, most trading companies are free to buy steel from any steel producer in any country.

In 1997, during the Asian financial crisis, trading companies demonstrated this flexibility. When Asian steel markets collapsed, trading companies shifted to suppliers who had been serving Asia and now had available large amounts of steel. Just as quickly, trading companies replaced lost Asian customers with U.S. customers. In a matter of one or two months,<sup>95</sup> trading companies had redirected their purchasing and selling operations from Asia to the United States.

### *Japanese Trading Companies*

Most Japanese trading companies still purchase the majority of their steel from Japanese steel mills. Japanese trading companies have long-term relationships with Japanese mills. These relationships have enabled the trading companies to become essentially the sole exporters of Japanese-produced steel. Although Japanese traders selling steel in the United States do not appear to switch their source of supply from one country to another to the degree that other trading companies do, Japanese trading companies interviewed for this report indicated that over the last five years they have increased their purchases from steel mills in countries other than Japan. One Japanese trader claimed that approximately 50 percent of the steel it purchases is from non-Japanese producers. Thus, Japanese traders are moving in the direction of more flexibility in their steel purchasing.

Japanese mills do not appear to be following suit with respect to their selling practices. One trading company interviewed for this report asserted that Japanese steel mills allocate their export sales to their preferred Japanese trading companies. For example, a Japanese mill may allocate its export sales among four Japanese trading companies, with each company getting 25 percent of the sales. In this scenario, each Japanese trading company recognizes that the mill expects it to sell a certain tonnage of steel over the year and, if sales are slow, may lower its prices to increase its volume in order to meet its obligation. According to the trader making this assertion, this arrangement reinforces the relationship between the mill and the trading company.

Such flexibility has positive and negative impacts on global steel trade. By quickly sourcing and selling steel in response to changing market conditions, trading companies have furthered the integration of individual steel markets into the global marketplace. By the same token, trading companies can precipitate significant fluctuations in the quantity of imported steel into or out of any individual market.

### **Impact on Prices**

Trading steel is a competitive, low-cost, low-margin business. Traders do not produce or further manufacture steel, but instead provide services that can (for the most part) be duplicated by anyone with a phone and fax machine. They survive on their ability to buy steel at a low price from a mill and sell it for a higher price to a customer. The selling price is the sum of the mill's price, a markup to cover costs (*e.g.*, selling/administrative and transportation) and profit. Stiff competition from other traders often puts a ceiling on how high the selling price can be and also keeps profit margins low—usually under 5 percent according to the trading companies interviewed.

Trading companies cannot, individually, cause market prices to increase or decrease. Each company in isolation is subject to market forces. Although traders occasionally recount instances when they are forced to sell at a loss during times of precipitously falling markets, thin profit margins limit their motivation for independently offering large price cuts to their customers.<sup>96</sup> Thus, significant declines in steel prices, for the most part, must originate with steel producers.

***Japanese Trading Companies.*** The role of steel mills in pricing was demonstrated during the U.S. steel import crisis when Japanese mills decided to drop their prices. According to several sources, Japanese trading companies offered high-quality Japanese steel at Russian prices during the 1998 steel crisis.<sup>97</sup> A trading company official said that these low prices began with the Japanese mills dropping their prices to the Japanese trading companies. Offering high-quality Japanese steel at Russian prices dragged the entire upper tier of the market down.

Japanese trading companies, however, have stated that they did not lower their prices to match the prices being charged on Russian steel. According to Japanese traders, high-quality Japanese steel typically sells for \$40–50 per MT more than lower-quality Russian steel. They assert that when U.S. market prices drastically fell, the price of Japanese steel fell in line with the overall fall in the market. One Japanese trader said that while the price gap may have narrowed by \$10 to \$30–40 per MT, it never disappeared completely. Another Japanese trader said that the normal time lag between placing an order and receiving delivery, in the context of a dramatically falling market, may give the appearance of Japanese steel prices matching Russian prices.<sup>98</sup>

***Foreign Mills and Affiliated Distributors.*** Several of the largest trading companies belong to industrial conglomerates that own and operate steel mills, trading companies, and service centers. Although the companies that are part of industrial conglomerates claim that their trading and service center operations conduct business at arm's length, one service center said that these conglomerates occasionally use their corporate distribution chain (*i.e.*, subsidiary trading companies and service centers) to move large volumes of steel produced by affiliated mills into the United States at low prices. While foreign mills can also move large quantities of steel using unaffiliated trading companies, the lack of transparency for transfer prices within the corporate family may make use of affiliated distribution chains more attractive.

***Russian Mills.*** For a number of reasons, the normal connection in the selling prices between mills and traders is more ambiguous in the case of Russian mills. After the breakup of the Soviet Union, Russian steel mills lacked marketing and exporting experience. They had inherited unsophisticated accounting systems that obscured the true cost of producing steel. During Russia's severe economic turmoil of the late 1990s, steel mills increasingly turned to a system of barter to trade finished steel products for desperately needed raw materials and working capital.

Trading companies viewed these atypical circumstances as an opportunity to increase their profits by integrating themselves into the mills' operations to a greater degree than they had in other countries. Trading companies supplied Russian mills with raw materials, working capital, and, in some instances, established equity stakes in mills. In return, these trading companies gained influence over the mills in determining the purchase price of the Russian steel. The extremely low purchase prices these trading companies extracted from Russian mills allowed them to undercut prevailing market prices and still make a profit.

These examples show that trading companies can affect U.S. price in a number of ways. Trading companies serve as the conduit for significant price cuts originating from foreign mills and, in aggregate, can induce large, fast swings in supply that, in situations of oversupply, depress prices. Trading companies capitalized on an atypical situation that allowed them to sell Russian steel at low prices and still make a profit. As Russian mills increase their sophistication and decrease their reliance on trading companies, this situation will, most likely, no longer exist.

### **Potential for Speculation**

Some observers have claimed that the 1998 import surge was primarily caused by trading companies speculating during strong U.S. market demand in late 1997 and early 1998. Under this scenario, trading companies, prior to having customers' orders, purchased and imported huge quantities of steel to sell on the rising U.S. spot market for a quick profit.

Many traders interviewed for this report stated that their companies did not speculate in the U.S. steel market. However, sources indicate that during early 1998, most traders were speculating and steel was being imported for inventories and piling up on the docks.<sup>99</sup>

### **Beating the Antidumping Duty Deadline**

Trading companies are often the importer of record for steel imports and, as such, are responsible for paying antidumping duties on imported merchandise subject to an antidumping order. Given the potentially high cost of antidumping duties, trading companies take notice when domestic steel mills discuss the possibility of filing new antidumping petitions. Several trading companies interviewed for this report acknowledged that they closely track the progress of antidumping investigations and calculate the likely effective date for imposing potential antidumping duties (usually the date of the preliminary determination) and attempt to bring in as much steel as possible before that date. Trading companies increased imports in mid- to late 1998 in order to beat the deadline on the antidumping cases. This increase may have helped to depress prices by increasing the already abundant supply.

### **Overall Impact of Trading Companies**

The steel crisis of 1998 was the result of the confluence of many factors that led to a large increase in the supply of steel in the U.S. market and downward pressure on prices. Trading companies, by rapidly transmitting the changes to the global economy, affected the crisis in several ways. They rapidly shifted focus from the collapsed Asian steel markets to the U.S. market. Trading companies selling Japanese and Russian steel tended to undercut U.S. market prices.

### **Lost Sales and Falling Prices Hit the U.S. Steel Industry**

In the second half of 1998, a number of U.S. steel companies lost customers to low-priced steel imports. Lost sales were combined with lowered revenue on the remaining sales as companies tried to keep up with import prices. The result was a sudden drop in sales revenue, operating income and profits in the second half of 1998 that lasted well into 1999.

The effects were particularly hard felt by smaller U.S. companies, such as Acme Steel, which had been modernizing and upgrading production. Between 1994 and 1996, Acme Steel invested more than \$400 million to modernize its facilities and preserve its business. In conjunction with Acme's investment, employees made labor concessions in the form of new work rules and reduced employment levels. At the time imports hit, start-up at the new facility was 90 percent complete; the plant was coming on line just as prices dropped \$90 per MT on low-carbon products and \$65 per MT on low-alloy products.<sup>100</sup> In discussions held with Commerce Department officials, Jim Howell, President and CEO of Acme Steel, stated that increased imports, coupled with lost sales and falling prices, led to Acme's loss of access to capital and subsequent liquidity problems "which pushed us into Chapter 11."<sup>101</sup>

Along with Acme, five other small and medium-sized steel companies filed for bankruptcy in 1998 and 1999, while others were reportedly near bankruptcy. Throughout the U.S. steel industry, companies were affected by the 1998 import crisis. For example, steel industry operating income, as compiled by the American Iron and Steel Institute from its reporting members, began to decline noticeably in third quarter 1998, resulting in operating losses by first quarter 1999 which continued well into 1999.

A comparison of 1997 and 1998 annual operating income for certain product sectors within the steel industry shows the same pattern of sharp declines in operating incomes in 1998 compared to 1997 (*Chart 2-20*).<sup>102</sup>

<b>2-20. Steel Industry Operating Income for Various Finished Steel Product Categories (In millions of dollars except as noted)</b>				
<b>Sector</b>	<b>1996</b>	<b>1997</b>	<b>1998</b>	<b>Percent Change 1997-1998</b>
Hot-rolled Flat Products	173	470	43	-91
Cold-rolled Flat Products	358	334	120	-64
Structural Steel Beams	311	339	258	-24
Wire Rod	-9	49	-102	-308
Line Pipe	17	35	11	-69
Stainless Sheet and Strip	224	153	45	-71

Source: Various ITC Investigation Reports.

Lost sales and falling prices led to cutbacks in production. As imports took market share, capacity utilization fell. Capacity utilization rates slid from more than 90 percent at the beginning of the year to less than 75 percent. By the end of the year, the crisis was having a direct impact on workers and their communities (*see box, next page*).<sup>103</sup>

For those laid off, employment opportunities in the surrounding area were often hard to come by. Harry Thuedaus, a corrugated machinery operator laid off by Acme Steel, found it difficult to find a new job that came close to what he was making at Acme.<sup>104</sup> The few jobs in the area that he came across paid about half of what he was making previously, and did not include insurance for either him or his family.

In Sterling, Illinois, home of Northwestern Steel, the situation was similar. When Northwestern Steel shut down its wire and wire rod division after losing 80 percent of its sales to imports, it laid off 320 steel workers; as of June 2000, fewer than fifty have returned to work.<sup>105</sup> Those that have found other manufacturing jobs in the Sterling area are paid, on average, less than half of what they made at Northwestern. Those working at nonmanufacturing jobs are generally paid even less.<sup>106</sup> With an average age of forty-five, this is a considerable economic blow to these workers (and their families).

### ***Weirton, W.V.: A Community Unites in Support of its Steel Mill***

Press reports, trade journal articles, and the Stand Up for Steel Campaign and Weirton, W.V., Web sites have noted the close link between Weirton Steel and the community of Weirton and the difficulties that the steel mill and the surrounding community faced during 1998 and 1999.

Located in the Ohio River Valley near Pittsburgh, Weirton is one of the few remaining traditional steel mill towns. Named after Ernest Weir, who located his steel mill there in 1909, Weirton came close to collapse in the early 1980s, when National Steel announced that it would cease investing in its Weirton facility. The mill's employees and the community rallied together to purchase the mill from National Steel. In 1984, newly formed Weirton Steel became the largest employee-owned company in the United States.

The town and the mill are inextricably linked. Even the town's mayor works at Weirton Steel, the fifth of eight mayors to do so. Therefore, when the crisis hit, steel workers weren't the only ones worried. Problems at the mill rippled throughout the local economy, directly or indirectly affecting everyone in the community.

Steel workers weren't the only ones to heed the call to action. The community came out in full force to assist the company and its employees in their struggle. Signs and banners urging Americans to Stand Up for Steel were posted throughout the town in businesses, along the streets, and even on the local Chamber of Commerce's Web site. Thousands of Weirton residents—men, women, and children—boarded buses at 3:00 a.m. on a cold January morning to make the trek to Washington, D.C., in order to let Congress and the Administration know what low-priced imports were doing to their community. Those who could not make the rally signed petitions and sent in letters urging members of Congress and the Administration to take action against unfairly priced imports.

The community expressed its support in other ways as well. Food banks were heavily stocked, the town ensured that utility service was not interrupted, and local banks allowed laid-off steel workers to miss occasional payments. In coming together as a community to confront a common problem, the citizens of Weirton proved that the mill towns of the past continue to have a place in the industry of the future.

Another indicator of the effect of the import surge on U.S. steel workers is the number of workers approved for Trade Adjustment Assistance in 1998 and 1999. Trade Adjustment Assistance is provided by the Department of Labor to workers who are laid off, or whose work hours are cut back, because of import competition. Assistance was approved for more than 6,000 steel industry workers in 18 states in 1998 and 1999.<sup>107</sup>

Workers also suffered in more subtle but pervasive ways. It is estimated that reduced work weeks, assignments to lower paying jobs, and early retirement affected more than 10,000 workers beyond those laid off in 1998. By the end of 1998, even Nucor, one of the most efficient and low-cost producers in the world, found itself hurt by surging imports.<sup>108</sup>

### **From Boom to Bust: 1998 Ends With Concerns for the Future**

In looking back at the events of 1998, one can trace the factors that turned a booming market into a crisis for U.S. steel companies and workers. By the end of the year, sales of domestic producers were down, prices had plummeted, and production was being cut. Trade cases had been filed, but it was still too early to determine whether they would be effective in turning back the tide of imports.<sup>109</sup>

While strong U.S. demand and other factors played a role in attracting imports, they do not tell the whole story. Other factors, such as structural problems affecting supply and prices in key countries—Russia, Japan, Korea, and Brazil—played a role in aggravating the 1998 U.S. steel crisis and in giving rise to concern about unfair trade as the crisis unfolded.

