CASE STUDY: Standing Up for Steel (1998-2001)
(Kennedy School of Government Case: C15-02-1651.0)

This case is an inside detailed look at steel politics and the making of government policy in the steel industry.

I. History

Steel has a history of protectionism. Since the 1970’s it has declined in output and world market share.

Economics of steel:

Big fixed investment, so barriers to entry high. Until 1970’s only competitors were Japan and Europe.

Huge excess capacity in steel.

- Nixon in 1968-69: Voluntary restraint agreement (VRA) on imports from Japan and Europe. Why not quotas? Because political costs on restricting trade of allied countries considered large.
Though imports declined, not financially beneficial and low profitability due to recession in 1970.

- Renewed call for protection and in 1972 VER extended for 3 years.

By 1974 steel market boomed and industry profitability increased rapidly. Heavily unionized industry. Workers wages increased rapidly as well. In 1975 steel workers earned 70% above the average wage in manufacturing (in 1969 they earned the average).

- Protection withdrawn in 1974.

NOTE: The steel industry should have used the 1968-74 years to restructure the industry through consolidations and bankruptcies. But exit or expansions were expensive.

- Expansions into other countries through FDI was not an option as countries were intent on growing indigenous steel industries (governments provided basic investments, employment potential was large, and technology was straightforward).

- Too much excess capacity in steel so expansions did not make sense.

Since industry made no fundamental adjustment (and was less cost-competitive after the VRA due to higher wages), imports increased after 1974. Large unemployment began to occur in the steel industry. By 1977 AD cases appeared.
Carter in 1977: “Trigger price” mechanism. (This headed off protectionist legislation being prepared in Congress, which was lobbied by the politically powerful steel industry, and unemployment in the mid-west) Set minimum price based on Japanese costs, below which there would be automatic presumption of dumping. This was the deal made to drop all AD cases.

- By basing price on lower Japanese costs, TPM forced US producers to cut costs
- Allowed cartel behavior among Japan, EC, US producers, and higher prices.

But by that time, barriers to entry were much lower (as governments got involved in those industries with investment subsidies) and new entrants like Taiwan and Korea

- Reagan, 1982: Dropped TPM (which applied to specific countries). New VRA. By 1985 VERs extended to all major exporters.

Because of the role foreign governments have played in subsidizing their steel industries, there was greater willingness on the part of the US government to “level the field” with protection.

Mini-mills with specialized niche products (carbon steel), modern steel furnaces, and non-unionized workers have emerged since 1980’s. They have successfully competed with imports. In the mid-1980s they earned 14% return on equity compared with 5-6% for integrateds (US Steel, Bethlehem Steel)

• Clinton: Did not renew VRA, though steelmakers continued to use whatever laws would protect them.

Big steel (integrateds) vs. domestic mini-mills (p 6)

Consolidations did not occur due to protection (second-tier integrateds were just not competitive and should have been allowed to be taken over, which would have happened if unprotected. So by 1998 this industry was in poor state to compete w/o protection.
II. Section 201

At least the VRAs did not shut out imports of certain product lines, like other measures like antidumping duties (AD) and countervailing duties (CVD) had the potential to do.

Section 201 does not involve unfair trade (like AD and CVD cases), but rests on proving that large import volumes cause or threaten “injury” to domestic industry. Case went straight to ITC, which made a decision in 6 months. If positive, then president had 60 days to decide on any action (tariff, quota, combination, trade adj. assistance).

Difference between 201 and AD actions are that AD focuses on specific product lines, and hence easier to get favorable decision. 201 potentially reduces imports for entire industry (steel), and harder standards to get favorable decision.
III. 1998 Crisis

By 1997 Steel industry was very healthy due to the boom. 20% of demand met by imports, but capacity utilization was at 90%.

1997 Asia crisis (i) contracted GDP in several countries (Korea, Taiwan, Malaysia, Thailand, Indonesia), reducing their demand for steel, and (ii) severely devalued their currencies, making imports from those countries much cheaper. In 1998 Russian demand also collapsed as did their economy.

In 1998 much lower priced steel imports poured into the US. Steel producers were faced with drastically cutting prices to remain competitive.

Politically the steelmakers and unions were of different views. Steel companies wanted to file AD complaints. The unions wanted not just to accuse exporters of dumping (which would have led to action on some product lines against some countries), but to go for legislation with a wider scope using 201 (which would lead to action on all steel products against most exporters). But 201 carried higher standards and a lower likelihood of passing congress and the president.

Unions went along with firms on AD cases against Brazil and Korea.
The Clinton administration bought the industries demand for “fair” trade, and threatened AD (with retroactive effect from the date case was filed).

Administration wanted a WTO-compatible emergency measure (i.e. 201) but did not want to appear protectionist, which would hurt Democrats in the next election. Most of the economists (CEA, OMB, NEC) wanted to be as free-trade as possible.

Treasury Secretary Rubin was the single most influential person on international policy, and he wanted to keep US markets open to the crisis-torn Asian economies, so as to not destabilize them. He was against government or firm initiated 201.

Tough for Union and steel firms to convince the administration to get a 201 initiative.
In 1998 steel capacity utilization fell to 75%, prices dropped 20% and 10,000 workers were laid off.

Problem was that imports had surged in only a few product lines, the steel industry sales in 1998 were their highest in history, other than 1997, and most of the steel companies were profitable. Also, it was the peak of an economic boom. Hence, industry lawyers did not want to push for 201 since they didn’t think 201 stood a chance with the ITC (draw a chart with who does what to get 201, AD etc.).
Currently, antidumping cases in the U.S. proceed through a five step process involving two federal agencies, the International Trade Commission and the Department of Commerce.

- The process begins with a petition filed simultaneously with both agencies.
- It continues with the two agencies acting in nearly alternating fashion, whereby the ITC determines if U.S. producers were injured by the actions of foreign producers and the DOC determining the extent of injury.
- A final decision on the case rests with the ITC Commissioners. This process is illustrated in Figure 1, along with the statutory time limits for each phase of the process. At best, a final decision may be reached within 280 days after it is filed. However, some cases may take up to 420 days. While these times are upper limits, some industry observers view the process to be very time consuming and costly. These costs are initiated with the preparation of the initial petition.
STATUTORY TIMETABLES FOR ANTIDUMPING AND COUNTERTOLLING INVESTIGATIONS

Statutory timetable for antidumping investigations (in days)

1 Normal case, ITA may extend the time allowed for it to initiate an investigation from 20 days to up to 40 days after a preliminary determination and all following dates would be increased by the amount of the extension.
The case is an excellent example of how politics interacts with economics.

- Clinton had a moderate, even conservative, view of interfering in trade matters, and resisted protectionism in steel till he left office.
- The Steel industry was well represented/connected at the congressional district level and was able to influence representatives in the House. It had influential representatives who could gather a pro-steel coalition.
- The Steel industry was much less influential in the Senate, which killed any protectionist bill that passed the House.
- Gore did not seem to be influential in imposing his demands on Clinton. Democrat support for Steel may have won him W. Virginia or other states that were crucial on the margin.
- Bush recognized the political importance of Steel and led the effort for a self-initiated (government-led) 201 petition for curtailment of imports.
- Bush also recognized that the deeper malaise was overcapacity in the U.S. and worldwide, and intends to use his bargaining power (once 201 imposed) to
  - Reduce Steel capacity in the US
  - Reduce Steel capacity in other countries