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Protectionism and Steel: The Need to Replace Outworn Perspectives

by *Bela Gold**

The paper by Professors Dirlam and Mueller seeks to disguise the mustiness and narrowness of its one-sided adversarial presentation by implying some relevance to our current national problems of “re-industrialization”. Their virtual failure to deal with these urgencies is especially disappointing because the problems of the domestic steel industry represent only one special case within the larger context of a rapidly developing foreign assault on an expanding array of major domestic industries with which our trade policies have not yet managed to cope. Nor are we likely to develop effective trade policies in respect to steel except within the framework of policies designed to deal with these broader challenges to the re-vitalization of major U.S. industries.

I. KEY ISSUES RAISED

Their paper centers around three foci. Most of it is devoted to the traditional pattern of combining an attack on the greedy, slothful, powerful domestic integrated steel industry with some alarming, but highly vulnerable, estimates of the burdens imposed on our economy by the protectionary measures that have been invoked. In addition, their paper offers an artful evasion of the central issue of the relative efficiency and cost competitiveness of the major sources of steel imports, by consistently discussing them as a group instead of recognizing the substantial differences among such exporters. Finally, they offer a thoughtful, though unpersuasive, effort to evaluate alternative trade policies relating to steel imports.

My comments will focus on three issues:

1. What represents a realistic conception of “protection”?
2. What is the relative cost competitiveness of foreign and U.S. steel producers?
3. What should be done to strengthen the market position of steel *and* other major domestic industries relative to imports?

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II. ON THE NATURE OF "PROTECTION"

In its conventional meaning, "protection" refers to governmental measures designed to safeguard domestic industries from the full market effects of failing to achieve and maintain cost competitiveness. Does this mean that U.S. measures such as tariffs, voluntary restraints, and trigger prices represent attempted protections for the domestic steel industry? Of course it does!

But does this mean that only the United States has been clever enough or devious enough to introduce such protective schemes? Obviously not, although the singular focus of the Dirlam-Mueller paper on the reprehensible behavior of this country might lead one to think so. Have U.S. protective practices been more restrictive or more protective than those of other countries? No evidence is offered to support such an implication.

Shouldn't a concern with governmental protections for non-competitive producers have included other forms of protection in addition to those for which the United States is so roundly condemned?¹ Consider subsidies to the steel industry, for example. In this respect, U.S. offenses pale into insignificance when compared with foreign practices. The Japanese government participated actively in enabling its steel producers to acquire massive investments on patently less than commercial terms in order to build their magnificent new facilities during the 1960's and 1970's. Furthermore, virtually all Western European governments have provided, and continue to provide, enormous capital allocations and grants to cover operating losses as well as other forms of aid to their steel producers — contrary to the implication in the Dirlam-Mueller paper that such subsidies have been largely devoted to training and relocation purposes. *The Economist (London)* has estimated that the British Steel

¹ The forms of subsidization are numerous and widespread. Some examples taken from the countervailing duty petitions filed against European Community producers:

- interest-free or below-market interest-rate loans to cover losses;
- interest-free or below-market interest-rate loans to help fund capital investment projects;
- government guarantees for loans from private lenders;
- cancellation of loan obligations and conversion of the amounts to equity;
- cash grants to provide additional capital;
- employment subsidies;
- subsidies to lower the cost of coal to producers;
- subsidies for export financing;
- loans from the European Investment Bank on terms more favorable than market;
- research and development subsidies;
- writing off of interest charges;
- rollover of loans made possible only by government action;
- regional subsidies.

Corporation, for example, has been losing more than \$1,000 per minute for more than a decade; yet it continues to export to the United States as well as elsewhere.

Such major subsidies and protective efforts are obfuscated in the Dirlam-Mueller paper within a cloud of ostensibly insoluble difficulties of definition, measurability and justifiability, unlike the treatment of what are emphasized as U.S. offenses. GATT (the General Agreement on Tariffs and Trade) itself has condemned subsidies as not consistent with free trade, although effective methods for dealing with them have yet to be developed. And in addition to subsidies, a fair analysis should also have called attention to the variety of other restrictions on steel and other imports imposed formally or informally by a variety of countries including Canada, Japan and Mexico.

In short, unless one were advocating unilateral free trade policies, a balanced assessment of U.S. practices would seem to require comparisons with those of other major steel producers. The absence of such comparisons surely helps to distort the perspectives conveyed by the Dirlam-Mueller paper.

III. ON THE COST COMPETITIVENESS OF MAJOR FOREIGN STEEL PRODUCERS

The Dirlam-Mueller paper contains extensive discussion of, and references to, domestic and foreign steel *prices* but no serious evidence relating to comparative costs and no comprehensive analysis of technological competitiveness is presented. Their focus on prices reminds me of a Japanese steel official's response to my query on learning that his company was buying some machinery from West Germany. "Can they really produce such equipment more cheaply than in Japan?" I asked. His reply was, "I didn't say that they could produce it more cheaply. I said that they were selling it at a lower price."

Are foreign steel producers more cost effective than U.S. producers? My field studies of Japan's integrated steel mills have convinced me that the Japanese have been substantially superior to U.S. plants for more than 10 years and are maintaining or increasing their cost advantages.² However, I have not seen any conclusive evidence that any Western European steel industry is more cost effective than the United States, except during occasional periods where there were significant changes in foreign exchange rates; nor do Dirlam and Mueller provide such evidence.³ In-

² Gold, *Factors Stimulating Technological Progress in Japanese Industries: The Case of Computerization in Steel*, 18 Q. REV. ECON. & BUS. (1978). See also Gold, *Steel Technologies and Costs in the U.S. and Japan*, IRON & STEEL ENGINEER, April 1978, at 32.

³ See Appendix Tables 1 and 2.

deed, my field visits, discussions and evaluations of relevant data in Western Europe have led me to believe that most of these industries are significantly less cost effective.⁴ Of course, there are a few relatively new plants in West Germany, France, Holland, Italy and Britain which are technologically quite modern. However, several of these continue to experience problems affecting their production and costs.⁵

It seems to follow, therefore, that a substantial proportion of the European steel exports to the United States have involved selling below costs.⁶ Any review of the hundreds of millions or even billions of dollars lost by European steel producers during the past five years is strong support for such a conclusion.⁷ Further support can be found in a careful review of the contributions to their steel industries acknowledged in government reports. Moreover, one serious inquiry into charges of selling below costs resulted in a finding in 1980 by the U.S. International Trade Commission that all of the leading carbon steel exporting countries in Western Europe were guilty of dumping in U.S. markets.⁸ Moreover, additional charges against various other countries are now being considered by U.S. government agencies.⁹

Dirlam and Mueller state that "predatory competition should be condemned and penalized in international trade," and I certainly agree with

⁴ S. EILON, B. GOLD & J. SOESAN, *APPLIED PRODUCTIVITY ANALYSIS FOR INDUSTRY* (1976).

⁵ B. GOLD, *PRODUCTIVITY, TECHNOLOGY AND CAPITAL: ECONOMIC ANALYSIS, MANAGERIAL STRATEGIES AND GOVERNMENTAL POLICIES* (1979, 1982). Incidentally, Dirlam-Mueller's footnote 55 citing my publication *Steel Technologies and Costs in the United States and Japan*, (prepared for the OTA Select panel on the Steel Industry (Dec. 1, 1977), *supra* note 2, as support for the following statement misrepresents my position: "Until the late 1970's the industry made little progress in bringing its technological level and plant efficiency up to the levels achieved in Japan and Europe."

⁶ See Appendix Table 3.

⁷ The sheer scale of the subsidization in the current petitions to the Department of Commerce and the U.S. International Trade Commission is staggering. One of the petitions summarizes it thus: "During the past six years, the steel manufacturers in these countries have received more than \$30 billion of state and private funds as a result of governmental grants, loans, guarantees or other forms of state intervention. Subsidy programs are now being adopted in these countries that will make available even larger sums within the next four years." And these subsidies are being provided to companies whose losses to date are reported as totaling over \$20 billion.

⁸ U.S. INT'L TRADE COMMISSION, *Certain Carbon Steel Producers From Belgium, the Federal Republic of Germany, France, Italy, Luxemburg, the Netherlands, and the United Kingdom*, Pub. No. 1064 (1980) at 1.

⁹ Preliminary rulings by the U.S. Department of Commerce on trade actions filed by domestic producers found the following subsidies: "40.362% for structural and plate steel and hot rolled carbon steel bars made by British Steel Corporation. Subsidies of 20.097% to 30.029% were found on steel products from France, while a range of 20.602% to 21.773% was identified on some products from Belgium. For Italy, the subsidy was 18.3%. . . West Germany was found to subsidize as much as 3.594%. . .". Wall St. J., June 14, 1982, at 4, col. 2.

that statement. But they do not offer the slightest evidence to disprove that this has been the nature of most European steel exports to the United States in recent years. Nor do they criticize the Europeans for such actions. Instead, they concentrate their attack on the United States for its inadequate efforts to limit such dumping.

IV. ON THE ADEQUACY OF SUGGESTED REMEDIAL MEASURES

Why have European governments supported such costly exports? Remedial efforts are likely to prove ineffective if they ignore the motivations which have led these governments to persist in economically draining subsidies to their steel industries.

One major reason for the continuation of such aid has been fear of the political repercussions if sharp reductions occur in steel industry employment. Most political parties in power in Western European countries during recent years have only had very slim parliamentary majorities. Accordingly, they have been eager to minimize the political threats and economic turmoil likely to result from shutting down steel mills that are no longer competitive, especially because of the concentrated impact in certain regions. These political considerations are reinforced by the economic argument that it is cheaper to maintain employment in sub-marginal mills, and then sell the output than to eliminate production and bear the full cost of the resulting unemployment and other social benefits when there is no offsetting revenue.

The result has been a classic case of exporting unemployment to the United States. Dirlam and Mueller properly express concern about the impact on the U.S. economy of the higher steel costs to domestic customers attributable to the voluntary restraint and trigger pricing programs, although the quoted estimates of up to \$1 billion annually in higher costs may be exaggerated. They also fail to consider the impact on the U.S. economy of the enormous displacement of domestic steel workers by the imports which have been admitted. This could easily account for 75,000 of the 167,000 jobs lost by steel workers here between 1965 and 1980. The income loss suffered by unemployed steel workers coupled with the decline in local economic activity dependent on the expenditure of such incomes probably surpasses the extra costs borne by steel customers.

What constructive measures do Dirlam and Mueller propose? Their general principle is to "support a trade policy that, by keeping the market open to the hard competition afforded by efficient foreign steel producers, forces the integrated steel suppliers and their employees to seek the highest possible level of operating efficiency and technological performance." I agree completely!¹⁰

¹⁰ For more comprehensive discussions of other critical problems, see: Gold, *Manage-*

Unfortunately, Dirlam and Mueller fail to demonstrate that most European steel exports meet the test which they have enunciated in their attacks upon trade policies. Nor are such laudable principles consistent with their review of trade policy options. For example, they attack enforcement of the long existing "import injury, anti-dumping and countervailing duty" provisions of the trade act by using weak arguments of imprecise meaning and measurement. This is a common refuge of critics unable to challenge the basic objectives and principles which underlie regulations. They seem more favorably disposed toward the application of Section 2 of the Clayton Act "which would permit foreign suppliers to meet the realized price of their domestic competitors." One cannot help noticing that Dirlam and Mueller do not discuss the fact that foreigners may avoid restrictions by selling below their costs in order to export unemployment to the United States. Thus Dirlam and Mueller ignore their previous insistence on keeping markets open to "efficient foreign steel producers." In general, they seem to be more concerned with simplifying administrative procedures and minimizing legal restrictions on imports than with preventing the displacement of tens of thousands of American workers by foreign producers supported and subsidized by their respective governments.

Let me hasten to add that the domestic steel industry suffers from a variety of other problems as well. Unfair competition, however, from imports is undoubtedly one of the primary problems which must be dealt with in order to encourage advances in other critical areas.

V. SOME OBSTACLES TO, AND POTENTIALITIES OF, MORE CONSTRUCTIVE APPROACHES

Before suggesting some elements of a more constructive approach to improving the competitive position of the steel industry, and other major industries under growing pressure from imports, it may help to clarify perspectives by asking why the U.S. government has been relatively unresponsive for many years to the numerous violations of our trade laws by foreign steel producers. In my opinion, one of the most important reasons has been its overriding concern with maintaining and strengthening NATO. Enforcement of U.S. trade laws against unfair competition by European steel exporters would contribute to increasing unemployment in the steel industry of Western Europe. As a result, governments favoring NATO and co-operation with U.S. foreign policy would be undermined. This is obviously an important consideration for the United States to take into account from the standpoint of the national welfare. It is likely

to increase in importance if similar pressures from unfair competition should substantially affect other industries. Also raised is the question of whether successive concessions which weaken an increasing number of domestic industries, and result in injury to U.S. economic growth and stability, are more likely to increase or decrease the United States' influence in international affairs.

Further, it is important to ask whether Dirlam and Mueller are correct in implying that the domestic integrated steel industry is politically powerful enough to ensure effective protection of its economic interests even when these interests do not conform with what the government regards as the nation's best interests. The events of recent years do not offer much support for such a viewpoint. The industry has been unable to effectively resist governmental pressures to curb price increases, and has had to cope with the most unfavorable depreciation allowances granted to any major steel industry. In addition, the industry must be responsive to trade union demands and divert a major proportion of its available capital resources to meet one of the highest pollution control standards in the world. Under these circumstances, the U.S. steel industry has been unable to prevent subsidized steel imports from taking significant portions of the domestic market. As a result, this reputedly powerful industry has been averaging one-half of the average profit rate for manufacturing as a whole.¹¹

This fact suggests that Dirlam and Mueller are using outdated images. Government policies are helping to drive capital out of the domestic integrated steel industry instead of encouraging its modernization. Contrary to the logic of static economic theory, resulting decreases in production capability do not necessarily engender the immediate rebuilding of capacity when it falls short of demand. Instead, the nation will face a long and costly interim period for allowing this deterioration of the industry since it will take 6-10 years to build new integrated mills. The existing steel cartel in Europe and the quasi-cartel behavior of Japanese steel firms in foreign markets make it highly probable that domestic steel shortages will ensure sharply increased prices for needed imports. It is hard to believe that these prospects are favorable to the nation's economic future.

What can be done? This question is particularly important since the steel industry is one of the basic industries in the United States that faces

¹¹ For further discussion see the author's testimony and supporting submission in "Challenges to Governmental, Managerial and Trade Union Policies Posed by the Declining Competitiveness of the Domestic Steel Industry", and associated testimony, reprinted in *Hearings on the Steel Industry by the Subcommittee on Oversight and Investigations of the House of Representatives Committee on Energy and Commerce, March 22, 1982*. (Washington, D.C.: Government Printing Office 1982).

the increasing invasion of its markets at home as well as abroad. Other industries currently facing this pressure include tires, autos, machine tools, semi-conductors, computers and consumer and commercial electronic goods. Moreover, additional industries likely to face increasing foreign competition within the next five years are high-technology industries such as aircraft, robotics, telecommunications, flexible manufacturing systems and pharmaceuticals.¹²

As was noted earlier, trade policy only represents one aspect of the array of constructive policies and actions necessary to revitalize our major industries.¹³ Within the area of trade policy, however, three primary principles should guide our government's efforts:

1. If predatory pricing is not permitted for domestic companies, it should also be prohibited for foreign producers;
2. If competition with private firms by domestic government agencies is considered to be incompatible with the basic values of our economic system, it should also be denied to foreign producers which are owned, controlled or subsidized by their governments, unless appropriate controls are enforced to prevent their engaging in unfair competition; and
3. If foreign governments restrict imports from the United States, then equivalent restrictions should be applied reciprocally to their exports to the United States.

Despite Dirlam and Mueller's concern over the complexities of enforcement, there is no reason to regard such rules as posing greater problems than many other regulations. In short, the single most important requirement regarding trade policy for steel, as well as other industries, is a fundamental commitment by the U.S. Government to offer its industries effective protection from unfair foreign competition, and to ensure its industries access to foreign markets on the same terms offered to imports into the United States from such areas.

A practical example of an alternative trading policy that has achieved notable benefits during recent years is the Canadian policy and practice relating to steel imports. Canada encourages the continuing expansion and modernization of its private steel industry by maintaining relatively high levels of capacity utilization, which make moderate costs and prices possible. What is the secret of their success? Although imports are welcomed during periods when demand exceeds domestic production capabilities, imports are actively discouraged during periods when demand falls short of domestic capacity. This approach merits careful study, not because it excludes demonstrably cost-effective competitors, but because it does not have the consequences which theoretical economists would be

¹² B. Gold, *U.S. Technological Policy Needs: Some Basic Misconceptions* in *TECHNOLOGY, INTERNATIONAL ECONOMICS, AND PUBLIC POLICY* 141 (H. Miller & R. Piekarz 1982).

¹³ See *supra* notes 5 and 10, for a fuller discussion.

inclined to predict; that is, stagnating technology and productivity that lead to uncompetitive costs and prices. Therefore, this scheme may offer some practical guidelines for increasing the competitiveness of the U.S. steel industry.

In conclusion, it is necessary to emphasize that if the United States is to achieve the urgently needed revitalization of its major industries, constructive trade policies must be effectively integrated with a wide array of other policies. This necessarily involves contributions from the respective industry's management and trade union, as well as from the appropriate sectors of government.

TABLE I

**LANDED PRODUCTION COSTS OF SELECTED NATIONS
AT DIFFERENT OPERATING RATES DURING 1981**
(Nominal dollars per ton)*

Adjusted	<u>(1981 values at 1979-80 exchange rates)**</u>				
	USA	Japan	West Germany	France	Great Britain
Operating at 70 percent of capacity	562	567	652	729	753
Actual Conditions (Operating Rate)	553 (77.5)	558 (58.0)	664 (62.1)	724 (74.6)	771 (61.3)
Operating at 90 Percent of Capacity	534	506	596	678	678

* Production costs include freight charges and duties to the port of entry into the United States

** The data has been adjusted to the following foreign exchange rates (home currency \$)

	<u>1979 - 1980</u>	<u>1981</u>
Japan	222.96	222
W. Germany	1.825	2.29
France	4.24	5.43
Gt. Britain	.4515	.498

SOURCES: *Original source of this Table:* Letter from J. F. Collins, Executive Vice President of the American Iron and Steel Institute, to Larry Oppenheimer, Natural Resources Division, Congressional Budget Office, dated March 10, 1982, com-

menting on the latter's "Briefing Paper on the Steel Industry (Draft 3/8/82)" reprinted in *Hearings on the Steel Industry by the Subcommittee on Oversight and Investigations of the House of Representatives Committee on Energy and Commerce, March 22, 1982* (Washington, D.C.: Government Printing Office, 1982). (Letter available at the office of *The Case Western Reserve Journal of International Law*.) For later, only slightly modified estimates, see Peter F. Marcus and K. M. Kirsis, *World Steel Dynamics - The Steel Strategist #5*, Feb. 1982 (New York: Paine Webber Mitchel Hutchins, Inc.), at 20-22 and Tables 5 and 6.

TABLE II

COST COMPONENTS FOR THREE NATIONS IN 1981

Disaggregated Cost (\$/net ton)*

Adjusted (1981 values at 1979-80 exchange rates)**

	West		
	Germany \$/ton	Japan \$/ton	USA \$/ton
Production Csts			
Materials	344-383	293-251	326
Labor	179	111-107	184
Financial	70	104-109	43
Total Prod'n Costs	593-632	508-467	553
Transportation	71-95	81-110	—
Total Costs	664-727	589-577	553

*Certain totals do not add.

**SEE EXCHANGE RATE USED at Table 1.

SOURCES: See SOURCES at Table 1. The operating rate is the same as shown in Table 1.

TABLE III
CONSOLIDATED RETURN ON SALES
 Net Income / Sales (%)
 (Major Producers)

Year	U.S.	Luxembourg	U.K.	France	Italy	Belgium
1973	4.5	5.3	2.8	1.5	1.9	1.7
1974	6.5	3.5	3.2	1.4	0.9	1.7
1975	4.6	-3.3	-10.8	-15.9	-4.0	-7.9
1976	3.4	-3.8	-3.1	-10.7	-5.9	-2.6
1977	0.1	-13.4	-14.1	-23.5	-17.6	-13.9
1978	2.5	-5.1	-9.4	-14.0	-13.4	-10.2
1979	2.0	-0.5	-17.6	-10.1	-8.3	-2.5
1980	3.0	-3.5	-22.6	-11.5	-20.4	-9.4

SOURCE: See SOURCES at Table 1.

