April 16, 1999

No. 4

The Steel "Crisis" and the Costs of Protectionism

by Brink Lindsey, Daniel T. Griswold, and Aaron Lukas

Executive Summary

Claims of the imminent demise of America's domestic steel industry—at the hands of "unfair" and "illegal" imports—have generated a crisis atmosphere in Washington. Antidumping, countervailing duty, and Section 201 actions now under way already threaten draconian cutbacks of steel imports. But U.S. steel mills and their unions want additional protection, including highly restrictive quotas already approved by the U.S. House of Representatives in March.

It is vitally important that policymakers gain a measured understanding of the full facts of the steel import question.

There is no steel crisis. U.S. steel mills shipped 102 million tons in 1998, the second highest annual total in the past two decades. Eleven of the 13 largest steel mills were profitable in 1998, earning collective profits of more than $1 billion. U.S. steel makers still supply more than two-thirds of domestic steel consumption.

The problems confronting the steel industry are already lessening. Steel imports in February 1999 fell to 2.2 million tons, below the monthly average of 2.7 million tons imported during the last "precrisis" quarter of April–June 1997.

Steel protectionism is incapable of saving steel jobs. Employment in the steel sector has declined by more than 60 percent since 1980 largely because of rising productivity, and employment will continue to fall even if trade barriers are imposed.

Consumers and steel-using producers will pay a heavy price for steel protection. Workers in the major steel-using sectors—transportation equipment, industrial machinery, fabricated metal products, and construction—outnumber workers in the steel industry by 40 to 1.

Quotas are a direct violation of our international obligations under the World Trade Organization and would encourage copycat protectionism in other countries. An outbreak of protectionism around the world would directly threaten continued U.S. prosperity.

Congress and the administration should reject protection for the U.S. steel industry.

Brink Lindsey is director and Daniel T. Griswold is associate director of the Center for Trade Policy Studies at the Cato Institute. Aaron Lukas is a policy analyst with the center.

CATO INSTITUTE

It is vitally important that policymakers resist the crisis atmosphere and instead gain a cool and measured understanding of the full facts of the steel import question.

Introduction

> The domestic steel industry has been flooded by imported products pouring in from Asia, Russia and Latin America, swamping more efficient American producers and drowning thousands of jobs. This tsunami threatens to wash away a strategic industry that has been a keystone of our manufacturing sector for generations.
>
> —Rep. Phil English (R-Pa.)

> Please do not wait too long to act or there will be no steelworkers and no steel industry to stand up for.
>
> —George Becker, United Steelworkers of America

> We are fighting for the survival of the entire domestic steel industry.
>
> —Mark Glyptis, Independent Steelworkers Union

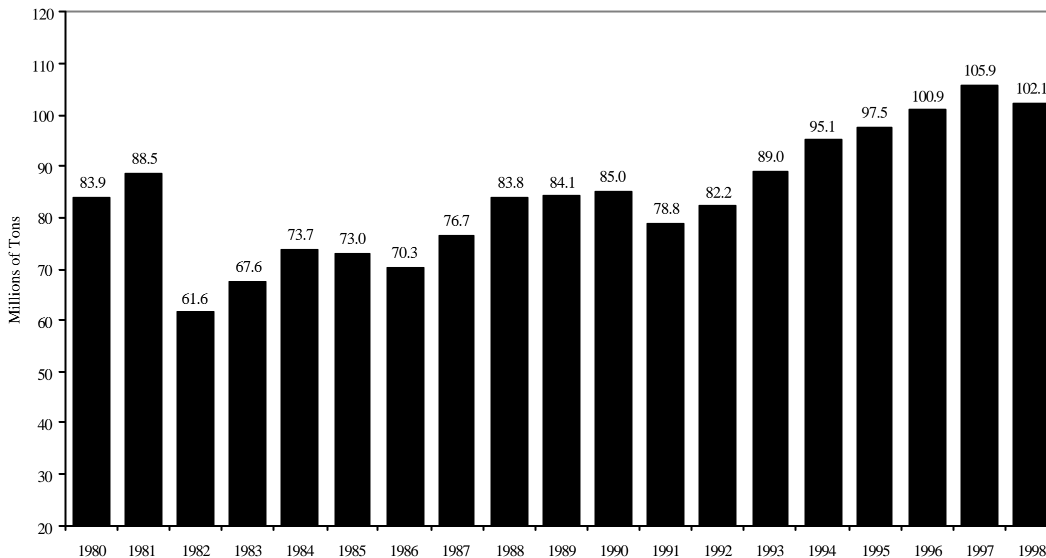
Those statements[1] are typical of the apocalyptic rhetoric that dominates the current debate over steel imports. Claims of the imminent demise of a major American industry—at the hands of "unfair," "illegal," and "predatory" imports—have generated a crisis atmosphere in Washington. Antidumping, countervailing duty, and Section 201 actions now under way already threaten draconian cutbacks of steel imports from targeted countries. But U.S. steel mills and their unions remain unsatisfied. They are now lobbying Congress for additional protection, including highly restrictive quotas, against a broad range of steel imports. On March 17, the U.S. House of Representatives voted 289 to 141 to impose steel quotas.

It is vitally important that policymakers resist the crisis atmosphere and instead gain a cool and measured understanding of the full facts of the steel import question. In particular, the following facts are jarringly inconsistent with both the descriptions and the prescriptions advanced by the steel lobby:

- U.S. steel mills shipped 102 million tons in 1998, the second highest annual total in 25 years. Domestic steel shipments in 1998 were up 21 percent from 1989, the last cyclical peak, and up 66 percent from the 1982 recession.
- American steel mills actually increased their share of global production in 1998, to 12.6 percent from 12.3 percent in 1997. U.S. steel makers still supply more than two-thirds of domestic steel consumption.
- Eleven of the 13 largest U.S. mills were profitable in 1998; 9 of the 13 were profitable even during the fourth quarter of 1998, the supposed depths of the "crisis."
- Steel imports in February 1999 fell to 2.2 million net tons, 45 percent below November imports and far below the monthly average of 2.7 million tons imported during the last "precrisis" quarter of April–June 1997.
- U.S. steel mills themselves accounted for about 20 percent of 1998 steel imports.
- Steel protectionism is incapable of saving steel jobs. Employment in the steel sector has declined by more than 60 percent since 1980 largely because of rising productivity, and employment will continue to fall even if trade barriers are imposed. From 1984 to 1992, the last time the United States imposed import quotas, employment in the steel industry fell by 78,300.
- While the steel industry has reduced its workforce by 10,000 in the last year, the rest of the American economy has created 2.5 million net new jobs. So for every steel job eliminated, 250 net new jobs have been created in other sectors of the economy.
- Workers in the major steel-using sectors—transportation equipment, industrial machinery, fabricated metal products, and construction—outnumber workers in the steel industry by 40 to 1.
- Quantitative restrictions on steel imports during the 1980s cost the U.S. economy up to an estimated $6.8 billion a year.
- Quotas are a direct violation of our inter-

Figure 1

Domestic Steel Shipments, 1980–98



Source: American Iron and Steel Institute.

national obligations under the World Trade Organization. Such violations by the United States would encourage copycat protectionism in countries suffering much greater economic problems than we face. An outbreak of protectionism around the world would directly threaten continued U.S. prosperity.

This paper is an attempt to set the record straight—to provide a reasoned analysis of actual conditions in the U.S. steel market and current proposals to address those conditions. The conclusion of this analysis is that the U.S. government has already gone too far in favoring U.S. steel mills with unfair protection from imports. Further favoritism for the steel industry is completely unwarranted.

Steel "Crisis"—What Crisis?

Imports of steel mill products rose sharply in 1998, reaching a record 41.5 million tons, up 33 percent from 1997.[2] Prices of steel products, especially of commodity products in sensitive spot markets, fell; the spot-market price for hot-rolled steel fell by 18 percent.[3] In the face of falling prices, earnings of U.S. steel mills deteriorated sharply, and some smaller mills, including Geneva Steel, Acme Metals, and Laclede Steel, recently filed for bankruptcy. Employment in the steel sector fell in 1998 compared to 1997.

As those facts demonstrate, American steel mills have certainly faced adverse market conditions in recent months. Nevertheless, claims of a "crisis" that threatens the viability of the industry are wildly overblown. An examination of the broader historical record shows that overall industry performance in 1998 was negative only by comparison with that during the string of immediately preceding banner years. Look at the total U.S. steel shipment figures in Figure 1. Domestic steel mill shipments in 1998 were 21 percent higher than in 1989, at the peak of the last expansion, and a whopping 66 percent higher than during the trough of the 1982 recession. While domestic shipments dropped slightly in 1998 compared to record-

While domestic shipments dropped slightly in 1998 compared to record-setting 1997, they were still at their second-highest level in the past 25 years.

Major American steel producers enjoyed combined profits of more than $1 billion in 1998.

setting 1997, they were still at their second-highest level in the past 25 years.[4] This is hardly the picture of an industry at death's door.

Not only is the U.S. steel industry strong by the standard of its own past performance, it is strong in comparison with other industries around the world. The impression given by the steel lobby is that American mills are being displaced by relentlessly expanding foreign production. In fact, many steel industries around the world are suffering far worse at present than is our own. The Japanese steel industry, for example, sank to its lowest production levels in 30 years in 1998.[5] With world steel output falling, U.S. producers actually increased their share of world steel output in 1998 to 12.6 percent from 12.3 percent in 1997.[6]

Although earnings fell from the previous year, most domestic steel companies continued to operate profitably in 1998. Eleven of the 13 domestic steel makers with annual sales of more than $1 billion posted profits in fiscal 1998. Even in the fourth quarter of 1998, in the depths of the supposed crisis, 9 of the 13 posted profits. Major American steel producers enjoyed combined profits of more than $1 billion in 1998.[7]

The steel companies and their unions point again and again to the 10,000 jobs lost in the past year as proof that emergency action is needed. First, although statistics do show a decline in steel-sector employment of roughly 10,000 workers in the past year,[8] there is no evidence that indicates how much of that total was due to normal attrition (i.e., retirements not offset by new hires) rather than layoffs, or the percentage of layoffs due to rising imports rather than other factors. Furthermore, as discussed below, declining employment has been the norm in the steel industry for the past two decades. A continuation of that secular trend is hardly evidence of a crisis. And finally, the figure of 10,000 job losses, even if taken at face value, is hardly alarming in comparison with the 2.5 million net new jobs created in the whole U.S. economy in 1998.[9] Total jobs eliminated in the steel industry over the course of the past year come to little more than a single business day's worth of net job creation in other sectors of the economy.

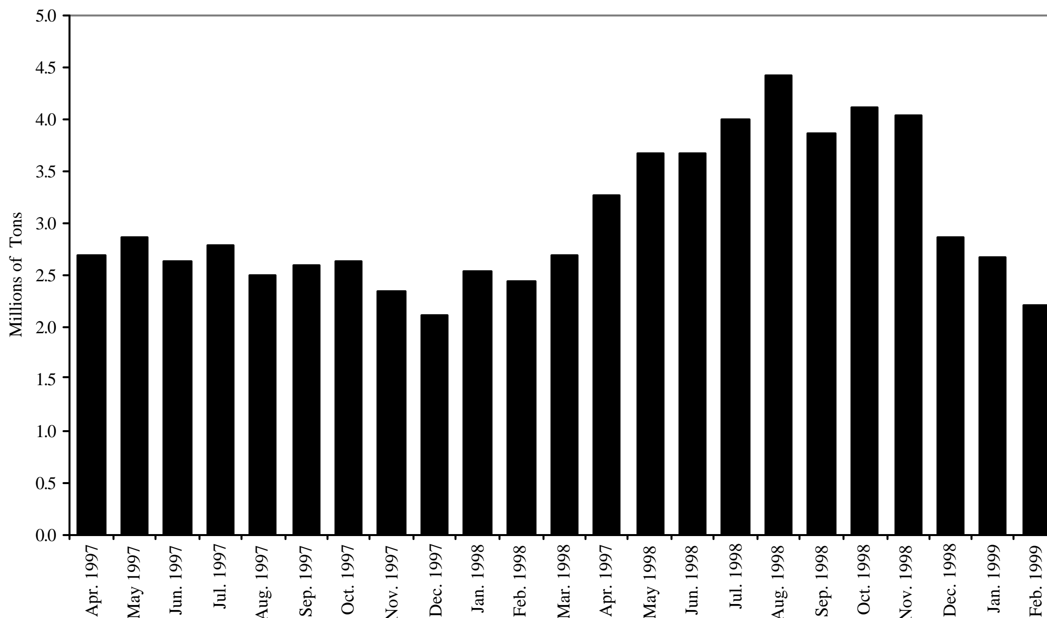
Meanwhile, the 1998 import surge shows every sign of being a passing phenomenon. According to Commerce Department figures, imports of steel mill products peaked in the fall of 1998 and have been declining sharply since November. Normal marketplace reactions to falling prices and rising inventories, compounded by the threat of retroactive antidumping duties, caused steel imports to plunge by 29 percent from November to December and another 7 percent from December to January. Hot-rolled steel imports from Japan, Brazil, and Russia—products targeted by antidumping petitions—have virtually halted, falling in January to only 4 percent of their November 1998 levels.[10] Total steel imports in February 1999 fell to 2.2 million net tons, 45 percent below November imports and far below the monthly average of 2.7 million tons imported during the last "precrisis" quarter of April–June 1997 (Figure 2).[11]

Another factor that contributed to the steel industry's difficulties during 1998 is no longer doing so. The General Motors labor dispute in June and July sharply cut domestic demand for steel. The sudden fall in demand left domestic steel mills with significant overcapacity and rising inventories, driving down prices further. That temporary disruption of the steel market ended with the resolution of the GM strike on July 28, 1998.

Despite recent problems, prospects for the U.S. steel industry look positive. Domestic demand is expected to remain strong, especially in the automotive sector, and exports could pick up in 1999 as demand in East Asia begins to recover. After bottoming out in the fourth quarter of 1998, steel prices are expected to rise in 1999; indeed, numerous U.S. mills have announced 10 percent price hikes in the past few weeks even as they lobby for more protection.[12]

American steel makers admittedly have experienced a tough couple of quarters. These challenging times, though, do not constitute a "crisis." They do not threaten the future of the industry. And they certainly do not justify resort to ill-conceived protectionist policies

Figure 2
Monthly Steel Imports Decline to "Precrisis" Levels



Source: American Iron and Steel Institute.

The steel industry is by no means alone in feeling the effects of worldwide economic volatility.

that would injure downstream U.S. industries and flout our international obligations.

Steel's Problems in Perspective

The U.S. steel industry's problems must be understood in light of past performance and present conditions in foreign steel sectors. To put the steel "crisis" in its full context, though, it is necessary to look at developments outside the industry. This broader perspective reveals that the steel industry's recent troubles are by no means unique; they are the result of deeper underlying factors, the effects of which extend far beyond the steel industry.

Specifically, the primary cause of rising steel imports and falling prices during 1998 was the Asian economic crisis that began the previous year. That sudden, dramatic, and utterly unexpected reversal of economic fortunes resulted in (1) a collapse in demand for steel in that region and (2) a realignment of currency values that makes foreign steel much more price competitive in the United States. In light of those circumstances, it is only natural that prices fell and that the still-vibrant U.S. market pulled in extra imports.

Many other U.S. industries have been hit by the recent turbulence in the world economy. Exporters, in particular, have experienced slumping sales because of distress in foreign markets. U.S. exports of all commodities were down 1.3 percent for 1998, after increasing 10.5 percent in 1997. Exports of refined fuels (schedule B of the U.S. Exports Classification, chapter 27) fell 19.2 percent last year; exports of grains, oils, and other agricultural products (schedule B, chapter 12) dropped 28.6 percent; and exports of wood and articles of wood (schedule B, chapter 44) declined by 18.5 percent.

Meanwhile, many import-competing industries have faced stiffer competition at home because of currency shifts and falling demand in other markets. While U.S. imports of iron and steel (Harmonized Tariff Schedule of the United States, or HTSUS, chapter 72) increased 19.0 percent in 1998, that import surge was not unique. Imports of aerospace products (HTSUS chapter 88) jumped by 34.5 percent; pharmaceutical imports (HTSUS

chapter 30) rose by 31.8 percent; imports of vegetables (HTSUS chapter 7) increased by 22.9 percent; and imports of railway products (HTSUS chapter 86) shot up by 57.1 percent.[13]

The steel industry is not alone in feeling the effects of worldwide economic volatility. Nevertheless, the steel lobby has portrayed this single industry as uniquely victimized and deserving of assistance. There is no reason why the steel industry should receive special treatment at the expense of its customers and American consumers, just because it is experiencing temporarily unfavorable conditions that affect many other industries as well.

Steel Jobs: The Real Story

Despite the record of ongoing protectionism, the domestic steel industry has shed more than 60 percent of its workforce since 1980.

The steel lobby contends that protectionist barriers against steel imports are needed to save jobs in the industry. But the evidence shows that import restrictions cannot stop steel jobs from disappearing.

Steel protectionism has been the rule rather than the exception for the past 30 years. Quotas were first imposed in 1969, followed in the late 1970s by the Carter administration's "trigger price" mechanism that imposed a price floor for steel imports. In 1984, after the steel industry filed a series of antidumping and countervailing duty petitions, the Reagan administration negotiated voluntary restraint agreements (VRAs) with virtually all steel exporters. After those VRAs were finally allowed to lapse in March 1992, the steel industry responded with another wave of antidumping and countervailing duty cases against imported steel. Today about a third of all outstanding antidumping and countervailing duty orders in force—more than 100 in all—are directed at steel products.[14] The latest round of protection—with major investigations under U.S. trade laws of hot-rolled steel, steel plate, and steel wire rod—threatens to continue the war against steel import competition.

Yet despite the record of ongoing protectionism, the domestic steel industry has shed more than 60 percent of its workforce since 1980.[15] How can that be? It turns out that the main threat to American steel jobs isn't imports but rising productivity in the domestic industry. In 1980 a ton of domestically produced steel required 10 man-hours to produce; today the industry average is less than 4 man-hours.[16] With productivity rising faster than domestic demand, the industry has required fewer workers. The resulting decline in employment has been relentless, with the number of employed steelworkers falling in 16 of the past 18 years.[17]

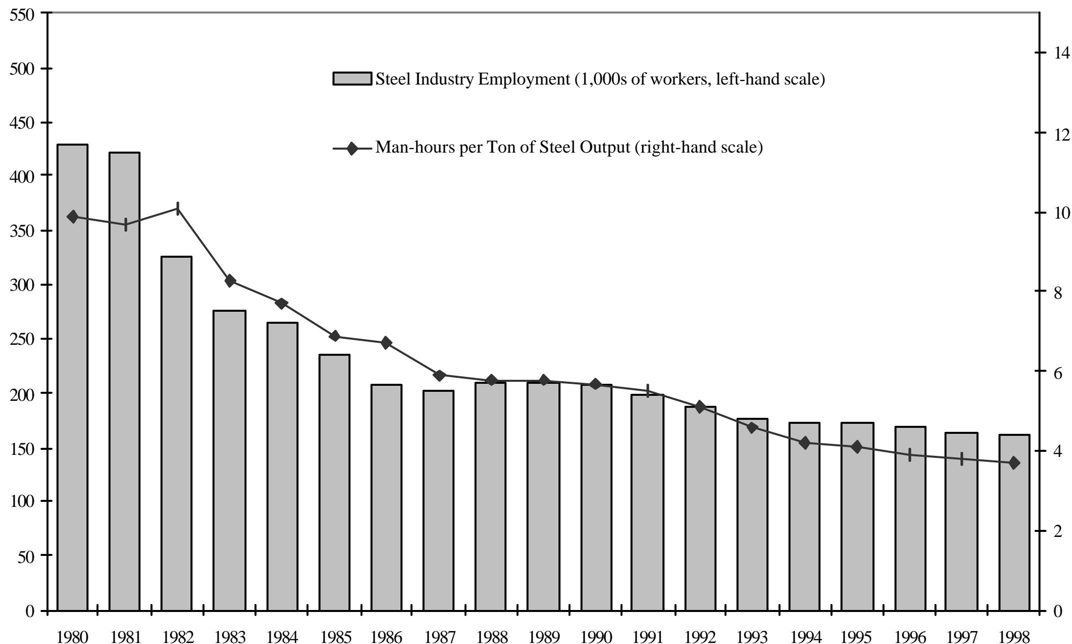
Figure 3 tells the story. Employment has moved steadily downward in sync with the falling man-hours-per-ton figures. Employment has fallen at a time when shipments have recovered from their lows of the early 1980s and reached record levels. The drop in steel industry employment has been caused not by falling production but by rising productivity.

During this same period, employment levels have borne no relationship whatsoever to variations in import penetration. Under the previous system of VRAs, imports as a percentage of new supply (shipments plus imports) fell from a peak of 26.2 percent in 1984 to 17.2 percent in 1992 (Figure 4). Yet during that same period, employment in the steel industry fell by 78,300—an average decline of almost 10,000 steelworkers a year.[18] (Doesn't that figure sound familiar?)

Foreign competition has helped to spur the progress in productivity, but the most ferocious competition has come from within our borders, from so-called mini-mills. The more efficient of these smaller mills can produce a ton of steel in under two man-hours and are relentlessly expanding the scope of products they can make. In 1981 mini-mills accounted for 15 percent of U.S. steel production; today they account for nearly half of U.S. steel-making capacity.[19] With or without protection, the industry will continue to economize and shed workers, with production shifting from the larger integrated mills to the smaller, more flexible and efficient mini-mills.

The facts thus show that steel protectionism is an exercise in futility. It cannot save steel jobs from rising productivity. All it can do is injure the rest of the U.S. economy.

Figure 3
Domestic Steel Jobs and Productivity



Source: American Iron and Steel Insititute; Bureau of Labor Statistics.

Costs of Protectionism

Raising barriers against steel imports imposes a real cost on the American economy. Millions of American workers and tens of millions of American consumers will be made worse off so the domestic steel industry can enjoy temporary benefits. Consumers will pay more than they would otherwise for products made from steel, such as household appliances, trucks, and cars. Artificially propping up the domestic cost of steel will only raise the cost of final products to U.S. consumers. If protectionist measures succeed in raising the average price of steel mill products by $50 a ton, Americans will pay the equivalent of a $6 billion tax on the more than 120 million tons of steel they consume each year.

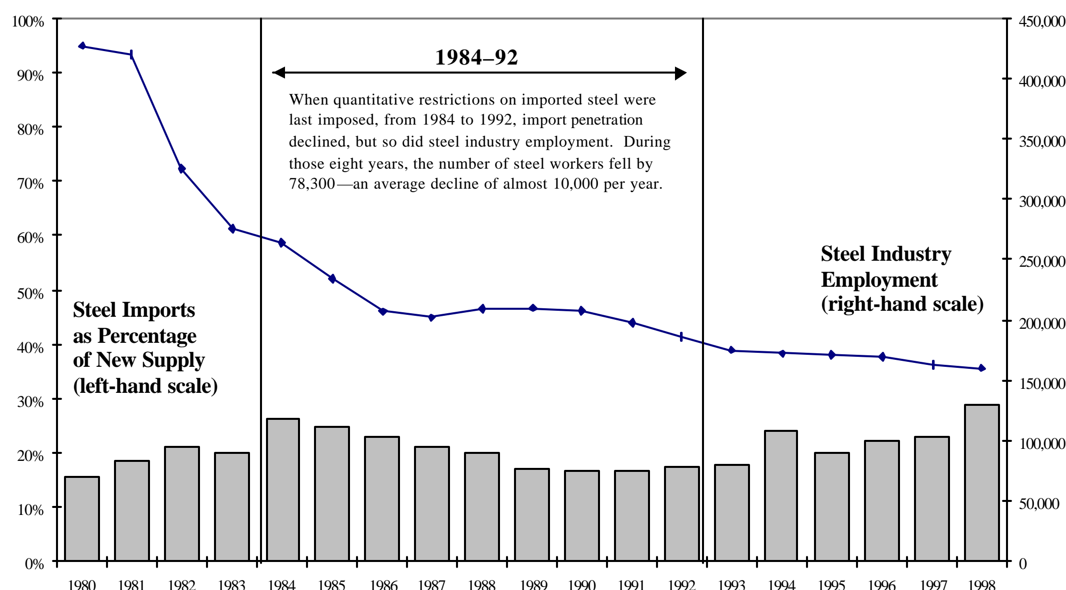
Steel protection will impose a heavy cost on the huge segment of American industry that consumes steel as a major input to production. The major steel-using manufacturing sectors—transportation equipment, fabricated metal products, and industrial machinery and equipment—employ a total of 3.5 million production workers. Production workers in manufacturing industries that use steel as a major input outnumber steelworkers by 20 to 1.[20]

A prime example is General Motors Corp., which buys 4.7 million tons of steel directly each year and another 2.5 million tons indirectly through independent suppliers. GM buys most of its steel through long-term contracts, and is thus insulated from short-term price fluctuations, but any price increase caused by protection will eventually filter through when contracts are renegotiated. In a brief filed with the International Trade Commission in October 1998, GM warned that antidumping duties against steel imports could negatively affect its ability to compete in global markets. GM's domestic operations "become less competitive in the international marketplace to the extent those operations are subjected to costs not incurred by offshore competition, and to the extent that U.S. import barriers impede access to new products and materials being developed offshore, or remove the competitive incentives to develop new products in the United States."[21]

Steel protection will impose a heavy cost on the huge segment of American industry that consumes steel as a major input to production.

The 8 million employees in steel-using industries dwarf the fewer than 200,000 steelworkers by a ratio of more than 40 to 1.

Figure 4
Decline of Steel Jobs Unrelated to Imports



Source: American Iron and Steel Institute; Bureau of Labor Statistics.
Note: New supply equals domestic shipments plus imports.

One of the largest direct consumers of steel is the construction industry, which accounts for about 35 percent of domestic steel consumption. Duties and tariffs against imported steel will result in higher prices for homes and commercial office space. The jobs of thousands of construction workers could be put in jeopardy. When construction and other nonmanufacturing industries are included, the 8 million employees in steel-using industries dwarf the fewer than 200,000 steelworkers by a ratio of more than 40 to 1.[22]

Especially vulnerable to rising import prices are workers in smaller companies that manufacture metal products. Those firms, which typically buy on the spot market rather than on long-term contracts, are the first to feel the pinch of higher steel prices. Many of them also act as suppliers to larger corporations and are thus less able to pass along a hike in steel costs in the form of higher prices for their final products. The result of higher domestic steel prices for these companies will be lower sales, declining profits, and fewer jobs created.

One such sector is the metalforming industry, which turns sheet metal into intermediate and final products such as precision parts. Jon E. Jenson, president of the Precision Metalforming Association, testified before Congress on February 25, 1999, that steel protection is damaging to the 1,600 companies that belong to the PMA and to their 380,000 employees (which makes the PMA alone about twice as big as the steel-producing industry in terms of workers employed). "Steel is an essential raw material in our products," Jenson testified. "It represents from 40 to 70 percent of the cost of manufacturing our products. So steel prices are critical. They are all the more critical because our members compete globally with businesses abroad. If our members have to pay more for steel than our foreign competition, our members will lose orders and be forced to cut back or cease production."[23]

That unintended consequence of steel protection was confirmed by another congression-

al witness for downstream users, H. O. Woltz III, president and CEO of Insteel Industries and vice president of the American Wire Producers Association. Woltz told Congress at the same hearing that AWPA members were facing the same import pressures as the steel industry and that steel protection would raise the cost of a major input at a time its members can least afford it. "Restricting the availability of raw materials to companies like Insteel through protectionist legislation will result in reduced competitiveness of our products and job losses in our industry," he said. "Those jobs will be lost to producers of wire rod products in foreign countries that have access to world-market steel."[24]

If the steel industry succeeds in gaining protection from imported steel, an even larger gap will open between domestic and international prices for steel mill products. That will give an advantage to foreign firms competing against American steel-using industries. Faced with artificially high steel prices at home, Americans will simply buy their steel indirectly by importing more finished products made abroad from steel available at cheaper global prices. If the federal government blocks the import of steel mill products through the front door, steel will come in the back door in the form of automobiles, industrial equipment, machine tools, and other steel-based products. As Jenson said in his congressional testimony, "The United States cannot afford to become an island of high steel prices."[25]

The steel industry itself has been a major importer of semifinished steel products. In 1998 more than 6 million tons of steel slabs, billets, and blooms were imported for use almost exclusively by steel mills.[26] When combined with wire rod and other semifinished products, imports by the steel industry reach 20 to 25 percent of overall steel imports. In November 1998 the International Trade Commission heard testimony that several of the major steel mills that have petitioned against steel imports were themselves placing orders to import large amounts of the very same products as recently as August 1998.[27] In the view of the big U.S. steel mills, apparently, these are "good" steel imports, while steel products that compete directly with what they produce are "bad" imports.

Aside from its direct negative impact on the domestic economy, steel protectionism will reverberate internationally to our detriment. Many steel-exporting countries are currently reeling from serious economic problems. U.S. protectionism will only worsen their plight and darken their prospects for recovery. At the same time, it will send a very dangerous signal to foreign governments contending with their own protectionist pressures.

Although the United States has been relatively insulated thus far, much of the rest of the world has been buffeted by a series of economic shocks over the past couple of years. With Japan's prolonged malaise, the acute crises elsewhere in Asia, the collapse of Russia, and the recent currency crash in Brazil, the world economy has stumbled into a highly precarious condition. During these turbulent and difficult times, the best thing America can do to encourage growth and stability abroad is to keep our markets open. Instead, at the behest of the steel lobby, the U.S. government is poised to deliver further body blows to ailing countries by restricting their steel industries' access to the American market.

Meanwhile, steel protectionism is sending the wrong message to the rest of the world. Many countries today are suffering violent economic contractions; as a result, their governments are facing formidable pressure to abandon market-oriented policies and erect protectionist barriers of their own. If the United States—the largest and richest country on earth, with 4.2 percent unemployment, low inflation, and 4 percent growth in 1998—is unable to say no to an industry with only 160,000 workers in a civilian labor force of 138 million, how can we expect other countries to hold the line? A U.S. surrender to special-interest pressure from the steel lobby would be a virtual green light for copycat protectionism around the world. Steel protectionism thus threatens to unleash on the world economy destructive forces that could easily bring an end to the prosperity Americans currently enjoy.[28]

A U.S. surrender to special-interest pressure from the steel lobby would be a virtual green light for copycat protectionism around the world.

America's Unfair "Unfair Trade" Laws

Despite complaints from the steel lobby that Congress and the administration are not doing enough, the system is already stacked in favor of domestic steel producers. U.S. antidumping law has become nothing more than a protectionist weapon for industries feeling the heat of global price competition.

U.S. antidumping law allows domestic producers to petition against imports that are being sold in the U.S. market at below "fair value." Fair value is defined as the price in the home market or the cost of production plus profit.

The problem with this definition is that it has no meaning in the real world of business and trade. As a consequence, the antidumping law punishes foreign producers for engaging in practices that are perfectly legal, and common, in the domestic market. U.S. firms, including steel makers, routinely sell the same product at different prices in different markets depending on local conditions, or temporarily sell at a loss (or a lower than "normal" profit) to liquidate inventories and cover fixed costs. Any steel company that lost money in the fourth quarter of 1998 was selling its goods at below total average cost and was consequently "dumping" its products on the domestic market according to the definition contained in U.S. law. If every domestic sale was required to be at a "fair" price according to the antidumping law's definition, most American companies would be vulnerable to government sanction, and U.S. consumers would find far fewer bargains.

The steel lobby argues that it isn't seeking special treatment; it merely wants redress of allegedly unfair trade practices abroad. But it is clear that unfair trade practices, under any plausible definition, had nothing to do with the hard times the U.S. industry has seen recently. It is regrettably true that protectionism and subsidies distort steel markets around the world. But nobody can argue seriously that policies around the world are any more unfair today than they were a couple of years ago, when U.S. steel mills were booming.

The aim of the latest batch of antidumping petitions has not been "fair" trade but rather no trade at all. The high preliminary duties announced in February make it difficult for the targeted products to be sold at all in the U.S. market. Secretary of Commerce William Daley, in announcing the preliminary dumping margins on February 12, said, "The impact, what this will do, by virtue of the fact that you've got such substantial ranges here, is basically price these products out of the U.S. market."[29] Richard Riederer, chief executive officer of Weirton Steel Corp., one of the petitioners in the case, agreed that the initial duties would be high enough to "lock out" hot-rolled steel imports from Japan and Brazil.

It is a misnomer to say that steel is being "dumped" on the U.S. market. Every ton of steel that enters the United States has been ordered by a willing American buyer, often months in advance of its actual delivery. Antidumping duties not only stop foreign producers from selling in the U.S. market; they also stop American citizens from buying the types and amounts of steel they need at prices that benefit them most as shareholders, workers, and consumers.

The aim of the latest batch of antidumping petitions has not been "fair" trade but rather no trade at all.

Proposed Legislation Would Compound Damage

The steel industry and labor unions complain that existing antidumping laws aren't enough—that the industry deserves special attention.[30] The reality is that the steel industry has benefited unfairly from trade barriers for decades and continues to enjoy advantages that are not available to other U.S. industries facing import competition. The Commerce Department's expediting of the antidumping process in the current case and the administration's proposed tax breaks worth an estimated $300 million for steel companies are merely the latest examples of special treatment.

Meanwhile, little attention is being given to the fact that the array of new protectionist proposals now in the works will seriously threaten the ability of other U.S. manufacturers to

obtain imported steel. None of the proposed legislation would increase general economic welfare, and much of it would be in violation of U.S. international commitments.

The following is a list of the most egregious legislative proposals that would benefit U.S. steel makers to the disadvantage of virtually everyone else.

Quotas on Imported Steel

This proposal would limit monthly steel imports from all nations to 1997 levels for a period of three years. Although the bill passed by the U.S. House of Representatives in March states that the import limits could be accomplished by "quotas, tariff surcharges, or negotiated enforceable voluntary export restraint agreements, or otherwise," it is in essence a quota bill that would set strict limits on the volume of foreign steel U.S. companies would be allowed to purchase. Whatever the mechanics of imposing the limits, the legislation would be a clear violation of our international obligations under the GATT.

Being in compliance with the GATT matters because the United States professes to be an honorable nation that keeps its word and upholds the rule of law. But beyond that, the United States voluntarily accepts international trade rules because they are in our best interest. Such rules restrain protectionism abroad and provide an impartial framework for adjudicating disputes, the benefits of which greatly outweigh any potential short-term costs to a single industry. Unilaterally closing the U.S. steel market through quotas would undermine respect for the rules-based international trading system that America has worked so hard to establish. If we expect other nations to honor their obligations, we must do the same.

Even if the United States had not pledged to forgo them, quotas are still unwise. Indeed, they are one of the most damaging forms of trade restriction. They redistribute wealth from consumers to domestic producers and to those foreign producers lucky enough to get quota rights, while the U.S. government does not receive tariff revenues. In other words, quotas would tax U.S. steel users to benefit major steel companies, both here and abroad. Moreover, they would endanger the ability of U.S. steel-using industries to obtain the materials they need. According to calculations by the Precision Metalforming Association, for example, the quota levels approved by the House would leave U.S. manufacturers nearly 4 million tons short, judging by 1998 levels of demand.[31]

Section 201 Reform and Import Monitoring

The legislation approved by the House would amend the Trade Act of 1974 to make an injury finding easier under Section 201. First, it would drop the requirement that imports be a "substantial cause" of serious injury (i.e., "not less than any other cause") and instead require that imports be only a cause of injury, however insignificant. The standard for what constitutes "serious" injury would also be broadened to include nearly any impact on domestic industry. Even supporters of "safeguards" against import surges should oppose such changes. They will allow troubled industries whose problems have little to do with imports to seek relief from normal market competition—a sure-fire prescription for abuse. The "substantial cause" standard is needed to ensure that the integrity of the Section 201 remedy is preserved.

Proponents of Section 201 reform argue that the proposed changes would merely bring U.S. law into compliance with WTO rules. Rep. Phil English, for example, says that he supports bringing Section 201 language "into conformity with the WTO."[32] But the WTO Safeguards Agreement is intended to be a minimum standard—to restrain the protectionist impulses of member nations, not to serve as model legislation. Indeed, it makes no more sense for the United States to bring its Section 201 law into "conformity" with WTO rules than it does for a driver to consume two martinis before getting behind the wheel in order to "conform" to blood-alcohol limits. In both cases, less is more.

Also troubling is a proposal to create a permit and monitoring program that would

Unilaterally closing the U.S. steel market through quotas would undermine respect for the rules-based international trading system that America has worked so hard to establish.

Changes in steel prices show up, eventually, in the price of an automobile, or a plane ticket, or rental space in an office building, but the causal connections are complex and subtle.

require all steel importers to register with the Commerce Department and report information on the cost, quantity, source, and ultimate destination of all steel shipments. Legislation approved by the House authorizes Commerce to collect "reasonable fees and charges" to defray the costs of issuing permits. The proposed import-reporting regime, in addition to being an unfair burden that falls only on steel importers, has the potential to choke off beneficial steel trade through paperwork.

Retroactive Antidumping Duties

Another proposal would assess retroactive antidumping duties for a period of up to one year prior to the filing of the original antidumping petition. Such a change is ill-advised for at least two reasons. First, it is in direct violation of U.S. commitments under the World Trade Organization, which sets universal standards for the imposition of retroactive antidumping duties. Second, extending the potential for imposing antidumping duties after the fact places U.S. importers and steel-using industries in a risky position that could threaten their access to adequate steel supplies. As Woltz recently pointed out, "The existing system of retroactive assessment of dumping duties already creates uncertainty and often results in unfairness for American importers and customers."[33] Extending the time period would only make the current problems with retroactive duties worse.

Three-Month Ban on Steel Imports

An alternative quota bill would impose a three-month ban on imports of steel and steel products from Japan, Russia, South Korea, and Brazil, in disregard of the needs of American consumers and steel-using industries. An outright trade ban—even a brief one—would seriously damage private business relationships and undermine the global competitiveness of dynamic U.S. companies. As written, the bill includes no provision for preserving the sanctity of existing contracts, nor does it specify what would happen to steel shipments already en route to the United States. This bill would deprive the U.S. economy of all the gains from steel trade and offer only temporary benefits to domestic steel companies. It would, in short, be a disaster.

Voluntary Export Restraints

The Clinton administration is pursuing its own nonlegislative approach, generally known as voluntary export restraints, or VERs. That approach entails trying to jawbone foreign industries—especially Japan's—into reducing steel exports "voluntarily." Of course, a VER is in reality an informal quota that is hardly voluntary. Like all quotas, VERs distort the economy and reduce national welfare. In the 1980s a comprehensive system of VERs against steel imports imposed a net loss on the U.S. economy of as much as $6.8 billion a year.[34] Furthermore, VERs are yet another violation of WTO rules.

Steel companies and unions have spent large sums of money in an attempt to convince Congress and the public that they are in dire need of protection from imports. The raft of new protectionist legislation shows that many lawmakers have been listening. All of the current proposals, however, would damage U.S. economic health, undermine the international trading system, and deprive American consumers and steel users of their legitimate right to trade. Despite that hefty price tag, the legislation would do nothing to halt the long-term downward employment trend in the U.S. steel industry. Given those facts, Congress should reject the pending steel bills.

Conclusion

During the so-called steel crisis, another major and highly visible American industry—the oil industry—has been suffering as well. Worldwide excess supply has driven prices down to record lows. Major producers posted sharply reduced earnings or outright losses for the fourth quarter of 1998. During the same period in which 10,000 steelworker jobs were eliminated, the American oil and gas extraction industry was shedding 38,000 jobs.[35]

So where is the all-out lobbying campaign

urging America to "stand up for oil"? The relative absence of pressure for oil protectionism may reflect the fact that Americans can see the impact of oil prices directly—at the gas pump and in their heating bills. Accordingly, there would likely be a strong popular reaction against any effort to raise taxes to bail out the oil companies.

Unfortunately, changes in steel prices are invisible to ordinary Americans. Those changes show up, eventually, in the price of an automobile, or a plane ticket, or rental space in an office building, but the causal connections are complex and subtle. The effect of a tax on foreign steel just doesn't show up in the average family's budget in any direct or immediate way. As a result, steel producers are free to equate their interest with the national interest without generating much in the way of grassroots opposition.

The campaign for steel protectionism thus highlights a classic problem of political economy: concentrated benefits and dispersed costs. The benefits of restrictions on foreign steel are concentrated in the relatively small steel-producing sector, while the costs are dispersed throughout the entire economy. Steel producers therefore have a very clear and powerful incentive to lobby for protectionism, while most of the rest of us who stand to lose don't have a big enough or clear enough stake to oppose them with any vigor.

Worldwide economic developments have combined to produce conditions that at present are unfavorable for U.S. steel producers and favorable for American steel users. In this situation it is not the business of the U.S. government to intervene in the marketplace and favor one U.S. industry at the expense of other U.S. industries. In particular, it makes no sense to penalize the industries that, in terms of employment and value added, are of much greater significance to the overall national economy.

The federal government should not use its power to confer special benefits on a small but vocal segment of producers at the expense of the nation's general welfare. Congress should reject calls for steel protection and reform the antidumping law to prevent future abuse.

Notes

1. Phil English, Statement before the Subcommittee on Trade of the House Committee on Ways and Means, February 25, 1999, p. 1; George Becker, international president, United Steelworkers of America, Testimony before the Subcommittee on Trade of the House Committee on Ways and Means, February 25, 1999, p. 9; and Mark Glyptis, president, Independent Steelworkers Union, Testimony before the Subcommittee on Trade of the House Committee on Ways and Means, February 25, 1999, p. 6.

2. American Iron and Steel Institute, "1998 Steel Imports of 41.5 Million Tons Highest Ever," Press release, February 19, 1999, http://www.steel.org/news/index.html.

3. Leslie Wayne, "American Steel at the Barricades," *New York Times*, December 10, 1998, p. C1.

4. AISI, "December U.S. Steel Shipments Down 14.9 Percent," Press release, February 8, 1999, http://www.steel.org/news/pr/1999/pr990208.htm. The 1989 production figure is from AISI, *1997 Annual Statistical Report* (Washington: AISI, 1998), Table 10, p. 27.

5. Alexandra Harney, "Troubles Grow for Japanese Steel Executives," *Financial Times*, November 20, 1998, p. 5.

6. "Economic Indicators," *The Economist*, February 6, 1999, p. 108.

7. Compiled by John Reilly, Nathan Associates Inc., Arlington, Va.

8. According to the Bureau of Labor Statistics, the number of workers employed in the blast furnace and basic steel product sector fell from 236,000 in January 1998 to 226,100 in January 1999. See BLS, *National Current Employment Statistics*, February 2, 1999, Table B-1, http://stats.bls.gov/

webapps/legacy/cesbtab1.htm.

9. According to the BLS, 133.4 million Americans were employed in the civilian economy in January 1999 compared to 130.9 million employed in January 1998. See Joint Economic Committee of Congress, *Economic Indicators*, January 1999, p. 11.

10. U.S. Department of Commerce, "Steel Imports Continue to Fall," Press release, February 25, 1999, http://www.ita.doc.gov/media/225stlpr.htm.

11. U.S. Department of Commerce, "Trend in Steel Imports Continues Down," Press release, March 25, 1999, http: //www.ita.doc.gov/media/ steelmar.htm.

12. Michael Arndt, "Steel on Up-Curve after Hammering," *Chicago Tribune*, February 2, 1998.

13. Data on export and import trends derived from analysis of trade analyst Daniel J. Ikenson of the Library of International Trade Resources. Supporting export and import data are available online at http://www.litr.com.

14. See White House, *Report to Congress on a Comprehensive Plan for Responding to the Increase in Steel Imports*, January 7, 1999, reprinted in *Inside U.S. Trade*, January 8, 1999, p. 20.

15. BLS, Table B-1.

16. AISI, "The New Steel Industry," http://www.steel.org/facts/newindus.htm.

17. BLS, Table B-1.

18. For the import and shipment data for the U.S. steel industry, see AISI, *1997 Annual Statistical Report* and previous years' annual reports. For the employment data, see BLS, Table B-1.

19. See the home page for the Steel Manufacturers Association, a trade group representing 60 mini-mill steel producers, http://www.steelnet.org.

20. Bureau of the Census, *Statistical Abstract of the United States, 1998* (Washington: Government Printing Office, 1998), Table 1233, pp. 742–43.

21. Brief filed with International Trade Commission, Re: Certain Hot-Rolled Carbon Steel Flat Products from Brazil, Japan and the Russian Federation, Investigation nos. 701-TA-384P and 731-TA-806-808P, October 26, 1998.

22. BLS, Table B-1.

23. Jon E. Jenson, "Steel Availability: A Growing Concern," Testimony before the Subcommittee on Trade of the House Committee on Ways and Means, February 25, 1999.

24. H. O. Woltz III, Testimony before the Subcommittee on Trade of the House Committee on Ways and Means, February 25, 1999.

25. Jenson.

26. David J. Cantor and Gwenell L. Bass, "The Steel Import Surge: Causes and Proposed Remedies," Congressional Research Service, February 24, 1999, pp. 13–14.

27. Scott Robertson, "Mills Said to Get Dumped Steel," *American Metal Market*, November 17, 1998, p. 1; see also Chris Adams, " Trade Secrets: Steelmakers Complain about Foreign Steel; They also Import It," *Wall Street Journal*, March 22, 1999, p. 1A.

28. A recent study suggested that antidumping duties on steel imports will enhance overall U.S. economic welfare. See Greg Mastel and Andrew Szamosszegi, "Leveling the Playing Field: Antidumping and the U.S. Steel Industry," Economic Strategy Institute, Washington, February 8, 1999, which purports to show that steel dumping, however that term might be defined, reduces U.S. economic well-being and that antidumping duties are needed to prevent this harm. ESI's findings rest ultimately on the fact that wages in the steel industry are higher than average and that displaced steelworkers frequently are forced to accept lower paying jobs. Thus, according to the ESI study, net U.S. welfare is reduced by dumping that causes job losses in the

steel sector; antidumping is good for us because it prevents those job losses.

First, this argument gets causation backwards: it assumes that high-paying jobs are the cause of economic welfare rather than the consequence of it. If applied across the board, the ESI analysis would mean that public policy generally should protect our high standard of living by discouraging or even outlawing layoffs from high-paying jobs. That is basically the European approach, and its effects are all too visible in low growth and chronic double-digit unemployment. Second, and more narrowly, the ESI analysis assumes that job losses in the steel sector wouldn't occur in the absence of low-priced import competition—an assumption refuted by the industry's steadily declining employment over the past two decades. Third, the study fails to adequately account for the offsetting production and employment gains that lower prices would stimulate in the far larger steel-using sectors.

Even if one accepts the study's methodology, the hypothetical gains from imposing antidumping duties against foreign steel are tiny—less than .005 percent of annual gross domestic product—and not worth the far more real danger that the law will be used for protectionist purposes.

29. Quoted in Chad Bowman, "Commerce Sets Preliminary Margins in Steel Cases against Brazil and Japan," BNA *International Trade Reporter*, February 17, 1999, p. 258.

30. See, for example, Becker.

31. See Jenson.

32. English.

33. Woltz.

34. Gary Clyde Hufbauer, Diane T. Berliner, and Kimberly Ann Elliott, *Trade Protection in the United States: 31 Case Studies* (Washington: Institute for International Economics, 1986), p. 179.

35. BLS, Table B-1.

CENTER FOR TRADE POLICY STUDIES

The mission of the Cato Institute's Center for Trade Policy Studies is to increase public understanding of the benefits of free trade and the costs of protectionism. The center publishes briefing papers, policy analyses, and books and hosts frequent policy forums and conferences on the full range of trade policy issues.

Scholars at the Cato trade policy center recognize that open markets mean wider choices and lower prices for businesses and consumers, as well as more vigorous competition that encourages greater productivity and innovation. Those benefits are available to any country that adopts free trade policies; they are not contingent upon "fair trade" or a "level playing field" in other countries. Moreover, the case for free trade goes beyond economic efficiency. The freedom to trade is a basic human liberty, and its exercise across political borders unites people in peaceful cooperation and mutual prosperity.

The center is part of the Cato Institute, an independent policy research organization in Washington, D.C. The Cato Institute pursues a broad-based research program rooted in the traditional American principles of individual liberty and limited government.

For more information on the Center for Trade Policy Studies, visit www.freetrade.org.

Other Trade Studies from the Cato Institute

Economic Casualties: How U.S. Foreign Policy Undermines Trade, Growth, and Liberty, edited by Solveig Singleton and Daniel T. Griswold (March 1999)

"Free Trade, Free Markets: Rating the 105th Congress" by Daniel T. Griswold, Trade Policy Analysis no. 6 (February 3, 1999)

"Opening U.S. Skies to Global Airline Competition" by Kenneth J. Button, Trade Policy Analysis no. 5 (November 24, 1998)

"A New Track for U.S. Trade Policy" by Brink Lindsey, Trade Policy Analysis no. 4 (September 11, 1998)

"Revisiting the 'Revisionists': The Rise and Fall of the Japanese Economic Model" by Brink Lindsey and Aaron Lukas, Trade Policy Analysis no. 3 (July 31, 1998)

"Free Trade and Human Rights: The Moral Case for Engagement" by Robert Sirico, Trade Briefing Paper no. 2 (July 17, 1998)

"America's Maligned and Misunderstood Trade Deficit" by Daniel T. Griswold, Trade Policy Analysis no. 2 (April 24, 1998)

Freedom to Trade: Refuting the New Protectionism, edited by Edward L. Hudgins (July 1997)

Nothing in Trade Briefing Papers should be construed as necessarily reflecting the views of the Center for Trade Policy Studies or the Cato Institute or as an attempt to aid or hinder the passage of any bill before Congress. Contact the Cato Institute for reprint permission. Additional copies of Trade Briefing Paper are $2 each ($1 for five or more). To order, contact the Cato Institute, 1000 Massachusetts Avenue, N.W., Washington, D.C. 20001. (202) 842-0200, fax (202) 842-3490, www.cato.org.

CATO INSTITUTE