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**WORKSHOP ON THE SITUATION IN THE STEEL INDUSTRY IN THE NIS**

**ROLE AND PLACE OF RUSSIA IN WORLD STEEL PRODUCTION AND TRADE**  
by Serafim Z. AFONIN, President of the Russian Union of Metal Exporters

*The Workshop was held in Paris on 2-3 November 1999.*

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## **ROLE AND PLACE OF RUSSIA IN WORLD STEEL PRODUCTION AND TRADE.**

Dear Mr.Chairman,  
Dear ladies and gentlemen,

First of all, let me thank the organisers of this Workshop for the kind invitation and the opportunity to discuss the present situation in world steel production and trade.

The Russian Union of Metal Exporters (RUME), which I represent here, respects greatly the activity of the OECD Steel Committee, which unites the most industrially developed countries of the world. We consider that at present the OECD Steel Committee has become the most authoritative international entity monitoring and analysing the situation in world steel production and trade. We support its efforts in co-ordinating this important sector of global economy.

We completely agree with the reasonable statement, made in November 1998 by the Chairman of the OECD Steel Committee Ambassador Hans Colliander in which he appealed to governments of steel-importing countries to refrain from protectionism and to producers to abide by international rulings. I will demonstrate below that Russia, despite of the extremely grave economic situation, has decreased significantly its volumes of production and exports of steel products.

Since the appearance of steel making technology and especially in the 20-th century the metallurgical industry has had a considerable or even decisive influence upon the economics and thus upon the political strength of the nations. Thus, the volume and geographical location of world steel capacity, which had established by the end of the "cold war", as well as resulting flows of steel products are largely the reflection of political rather than economic decisions.

As evidenced by historical experience, a trade, to be exact - a free trade is the motive power of human progress and the best counteraction to an appearance of economic disparity.

In Russia, the country where some years ago one could not even think about free trade, we believe as well as our supporters in USA (1), that "the freedom to trade is a basic human liberty, and its exercise across political borders unites people in peaceful co-operation and mutual prosperity". Open markets provide wider choices and lower prices of goods as well as create conditions for more vigorous competition that encourages growth in labour productivity and improvement of labour instruments.

### **Today's situation in the world steel trade**

Annually over 200 mill. t of steel products are exported in the world. This is more than each fourth ton made. A gradual build-up of export volume is also observed. By the OECD Steel Committee

estimation for the last five years, without account of inter-European trade, world export grew from 160 till 180 mill. t.

In the last decade of the 20th century, despite the general steady growth of world steel consumption, the situation in the world steel markets began to sharpen, which was caused by unbalanced demand and supply. There are several reasons for it. In our opinion, the main reason was the change in geopolitical situation after the “cold war” that has resulted in the lowering of military opposition along with the movement of the ex-Eastern block countries towards building of market economy. In connection with this the whole number of countries reduced their demand for heavy military equipment, which caused the fall in steel consumption for manufacture of this equipment and led to the formation of extra capacities.

Simultaneously, the liberalisation of foreign trade in countries with controlled economies, which to a great extent had long been isolated from the world scientific and technological progress, caused a disastrous slump in production in the majority of steel consuming industries, which products appeared to be non-competitive. Immediately, the above mentioned factors made redundant the work of millions of people that resulted in a dramatic decline of jobs and sharp decrease in living standards. Absence of public funds for crediting the conversion and renovations of the industry, political and financial instability (for example, in Russia) deterring private investors, have resulted in a severe and lingering economic crisis in the former USSR countries.

At last, the reason for which the situation in the world steel market became utterly aggravated was the large-scale financial and economic crisis in 1997-1998 in the South-East Asian countries. The fall in steel demand in these countries was reflected in a growth of exports to North America and Europe whose markets were still expanding.

The response to these phenomena were dramatic sharpening of competitive fight. The steelmakers of the USA, Canada and the EU try to move aside foreign competitors from national markets, using national trade law. Charges with “unfair” competition and trade resting on state support of inefficient and unprofitable excess capacity are used as a ground for sanctions against competitors.

### **Does Russia have excess steel capacity?**

Before the break-up of the USSR the production capacity of Russian Federation could make 96 mill. t of crude steel. According to the data of the Ministry of Economy of Russia, in 1990-1997 at the Russian iron & steel works and plants there were shut down of service and dismantled capacities about 27 mill. tpy of crude steel.

Nowadays, the production capacity of crude steel is about 69,5 mill. t and the estimated average level of its utilisation amounts to 63 % (see **table 1**).

**Table 1. Steelmaking capacity - 1998**

	<b>Capacity</b>	<b>Population</b>	<b>Capacity</b>
	<b>million tonnes *)</b>	<b>thousand ***)</b>	<b>per capita, kg</b>
EU (15)	194.4	374153	527.59
Japan	149.5	125981	1187.25
China	127.7	1255091	101.8
USA	113.3	273754	413.87
Russia **)	69.5	147231	472.0
Korea	49.2	46115	1066.89
Brazil	33.8	165158	204.65
Canada	17.0	30194	563.02
Mexico	16.5	95831	172.17

Sources:

\*) *OECD Steel Committee*

The Russian metallurgy is practically completely privatised. The holding of shares owned by the state has small affect on a management of steel plants. Relations with fuel and energy complex as well as with transport complex, remaining largely under the government control, are built basing on market principles.

As a result of a lingering economic crisis the per capita consumption of steel production in Russia (see **table 2**) dropped to a very low level, which makes it problematic to maintain vital transport and power arteries (main lines, marine and river transport, gas and oil pipelines, bridges, overpasses, urban engineering communications etc.) and to support an infrastructure in such a geographically vast country, as Russia.

Western producers and experts consider difficulties in the world steel trade are connected, first of all, with the excess of steelmaking capacity. According to OECD Steel Committee estimation of such excess amounts to nearly 300 mill. t. In this regard, in the "Steel Action Program", for example, the U.S. Administration directly refers to Japan, Republic of Korea, Russia and the Ukraine as the countries carrying out "unfair practices supporting excess capacity".

As far as Russia is concerned, I would like to comment on this issue.

In our opinion this estimation is of a formal character and results from the desire to preserve for the future the today's huge difference in per capita steel consumption in economically advanced countries as compared to developing ones (see **table 2**). This view from year to year is traced in minds of western experts and is not transformed in any way according to political changes in the world. If they consider that Russia have to "freeze" a consumption of rolled product at present level of 100 kg per capita, it will be difficult for us to understand each other. We do not doubt, that our country will return to pre-crisis level of metal consumption, when western producers practically did not feel the presence of Russia in the world

markets. If excess capacity exists in the world, it is first of all in the EU, which makes 160 mill. t of steel of which 30 mill. t are sold as a merchandise. There is a similar situation in Japan. Is the present-day volume of steel production inside these countries justified from the viewpoint of extra energy and ecology load which is borne by their citizens, taking into account leading positions of these countries in the field of high technologies?

It is necessary to take into account that the metallurgy now is one of few branches of the Russian economy which is "afloat" and provides the country with the currency. For Russian steel producers export is practically the only source of money, as approximately half of domestic trade is carried out by barter trade and bill operations. Shrinkage of external markets forced Russian producers to decrease their production in 1998: of crude steel - by 9.7%, of rolled products - by 9.8%, of steel pipes and tubes - by 19%.

Thus, the strategy of the Russian metallurgists over all these years after the beginning of market reforms has been to get and to keep a share in the world steel market in order to preserve the metallurgical branch as a basis of the future rise of the Russian economy.

The submitted data testify that the situation in the Russian economy in general and in steel industry in particular still remains extremely difficult. Objectively, the Russian ferrous metallurgy practically exhausted its opportunities on capacity withdrawal. The continuation of this process will result in a complete stop of a number of large enterprises and can cross out hopes for improvement of the Russian economy, leading to the hardest social consequences.

Table 2. Production, consumption and trade of steel mill products in 1997-1998

*million tonnes*

	Steel production		Export	Import	Trade balance (-)exp.(+) imp.	Apparent consumption of rolled products		Rolled products	
	crude steel	rolled products				total	per capita, kg	export vs production	import vs consumption
								%%	%%
<u>1997</u>									
USA	97,5	84,2	5,6	28,9	23,3	107,5	392,8	6,7	26,9
EU (15)	159,9	143,6	30,0	13,3	-16,7	126,9	339,1	20,9	10,5
Japan	104,6	97,4	22,8	6,4	-16,4	80,9	642,4	23,4	7,9
Russia	48,4	36,4	27,1	4,0	-23,1	13,3	90,3	74,5	30,3
<u>1998</u>									
USA	97,7	83,4	5,0	37,7	32,7	116,1	423,7	-6,0	32,5
EU (15)	160,0	144,0	24,0	23,4	-0,5	144,5	386,4	16,7	16,2
Japan	93,6	87,2	27,7	6,6	-21,1	66,1	524,6	31,8	10,0
Russia	43,8	32,9	20,4	3,4	-17,0	15,9	108,1	62,0	21,4

Sources: OECD Steel committee

State Custom Committee of Russian Federation

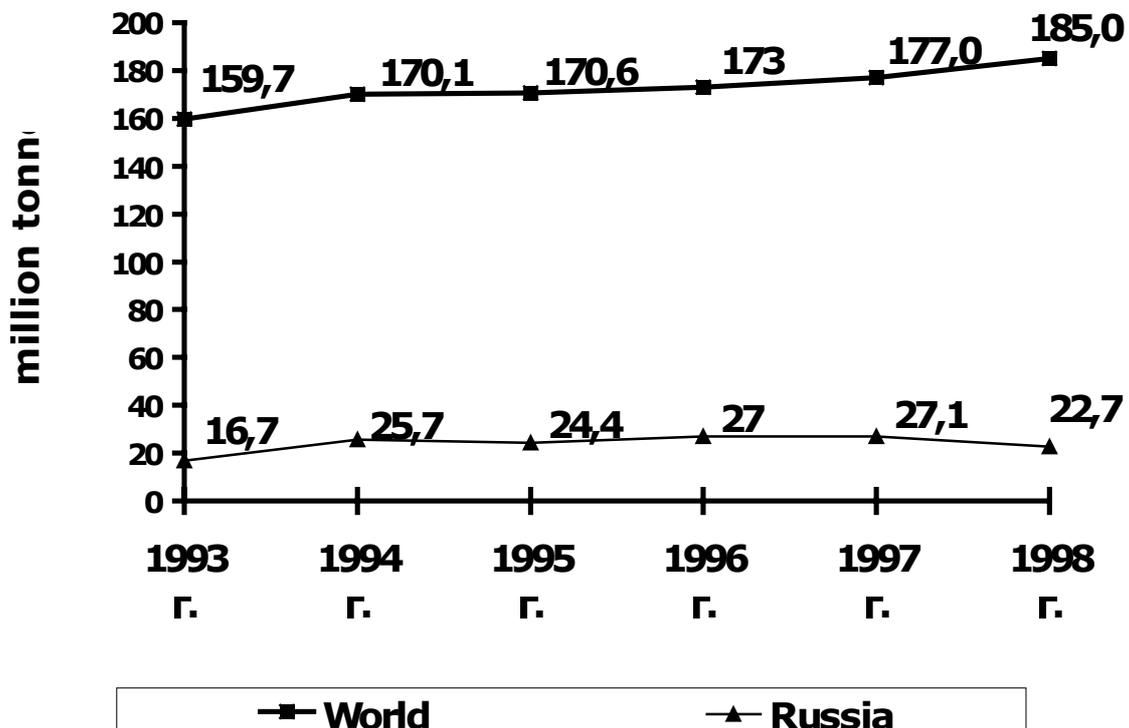
### Protectionist trade barriers against Russian steel export.

The collapse of steel-consuming sectors of Russian industry rised a problem of survival and rescue from destruction of steel branch. The only opportunity to survive was to fastly get a share in the global steel market, using the liquidity of steel products. Ten years ago Russia practically did not participate in the world steel trade. In 1994 Russia became the world largest steel exporter and the main target in trade wars in the world markets.

One must note that the dynamics of the Russian exports for the last five years was adequate to the changes in the world exports (fig.1), and the share of the Russian exports only to a small extent exceeded 15% of the world export of steel products.. Export form Russia reached its peak level in 1996 - 1997. Then exports decreased due to the crisis of the Asian market which absorbed more than 50% of the Russian steel exports.

Figure 1

### World and Russian Steel Mill Export



I would like to pay attention to the fact that the growth by 8 mill. t in world exports in 1998 was accompanied by recession in the Russian exports by 4.4 mill. t. Therefore, all speculations that the surge of Russian exports crushed prices in the world steel market do not have any grounds.

With a large-scale entering of the Russian steel in the world markets, the surge of investigations rose against the Russian exporters. Everybody is aware of recent anti-dumping investigation in the USA concerning imports of steel from Japan, Russia and Brazil. Russia as NME country was forced to conclude agreements establishing quotas on a range of steel products that account for more than 90% of imports of Russian steel. The agreements reduce imports of Russian basic kinds of products – hot rolled steel and cold rolled steel by 80% and 50% respectively.

The U.S. antidumping law, as its apologists claim, protects American industries from supposedly unfair import competition. They claim that dumping is unfair trade practice that takes two different forms: price discrimination (i.e., selling at lower prices in the United States than at home) and below-cost sales. They argue that the both forms result from open or latent interventionist foreign government policies. Those governments suppose domestic producers by accessing to credits on noncommercial terms or by closing or restricting home markets. In the latter case one may use the so-called “cross-subsidization” strategy at which low-price sales at foreign market are subsidized by high-price sales at large and protected home market.

What is revealed in the above-mentioned investigation? It was only determined that Russian steel was selling at lower prices than average market prices. However it's not yet the proof of dumping. Sales at a lower price and even temporary sales below cost with the aim to get or to protect market share are a normal, competitive market phenomena widely using by market players including the famous U.S. corporations. It's naturally that Russian producers as the new entrants at American market had much weaker bargaining position than domestic producers in such factors as time of delivery, customer service, brand identification and customer loyalties stemming from past advertising. So, they were forced to accept a lower price on its products in order “to level playing field” (using a terminology of our American colleagues).

Such favourable production factors as proximity of sources of raw material and fuel and energy resources which create competition advantages for Russian producers made possible the realisation of such price policy. And it's not our fault, but it's our common trouble that a general price situation in the market in 1998 was sharply worsened as a result of the Asian crisis.

The purpose of the US antidumping legislation, however, is not to establish reasonably the fact of dumping and to reveal the real degree of guilt of market participant, against which the investigation has been initiated by the domestic producers. Instead, any positive difference between the price which the domestic producers consider as "fair" and the price set by the competitor, is considered as infringement by the competitor of “a level of a playing field ” with the help of unfair support from its government.

Cato Institute's Center for Trade Policy Studies examined the U.S. Antidumping Law (1). The authors of the investigation concluded that various dumping calculation methodologies used for determination of price discrimination or sales below cost are far from correct.

As to the NME countries to which the U.S. Commerce still relates Russia (in spite of the fact that practically completely privatised Russian steel enterprises already have been operating in market conditions for some years), there is a complete arbitrary rule because the price and cost data are not those of the producers under investigation.

Is it possible to speak about the direct financial support by the state of the Russian producers in present conditions of severe budget deficit in Russia? Or may be Russia closed its market for imports of steel having imposed high tariff duties and quotas? Or might it be the fact that Russian steel producers use the so-called "cross subsidising" and thus have an opportunity to trade in the world market at rather low prices at the expense of large sales at the high prices in the closed domestic market?

The home market of Russia now is, perhaps, the most open one in the world. As I have mentioned earlier, even at a very limited capacity of the Russian steel market, imports amount to 20-30% of steel consumption (i.e. almost the same as in the USA) (**Tabl. 2**). There is practically no difference between import duties on standard steel in Russia (5%) and those in the USA (2.9-3.6%), and there are no non-tariff import barriers on steel in Russia. At last, only 1/3 of rolled steel produced is sold in the home market.

Unfortunately, only few of the American politicians and businessmen realise what difficulties Russia is facing today on the way to a modern market economy.

The true price for drama, created by the American steel companies and trade unions, on which background the antidumping investigation against Japan, Russia and Brazil was conducted, is shown by the analysts of the above mentioned Center for trade policy studies (2). Simply taking the advantage of the next turmoil in the global economy, caused by an unexpected and dramatic Asian economic crisis, the American steel companies and trade unions with the help of well-staged mass media campaign and the support of powerful Steel caucus in Congress did not miss the chance to press on the Administration to use "legal" way of clearing the national market from the competitors. As a matter of fact the decision of the U.S. Commerce and the Commission on International Trade on antidumping investigation against imports of steel from Japan, Russia and Brazil is nothing but next U.S. government grant to the domestic steel companies at the expense of other branches of the American industry and American consumers. And they call it fair trade!

As far as the U.S. antidumping legislation is concerned, the authors of the above quoted research (1) came to the conclusion, that the practice of its application does not at all correspond to the ideology declared in it, and in its present form this legislation is not the tool for fair trade maintenance, and it only creates the illusion of legitimacy of actions taken by the US Government against foreign market participants. We entirely support these conclusions.

There is the following saying in Russia: "a bad example is a catching thing". So, taking the example of the US and Canadian legislation dozen of other countries now adopted similar laws. Russian legislators are not the exclusion in this process though we still do not have any precedent of application of this legislation. One may ask: where are we going to and what will the world trade turn into?

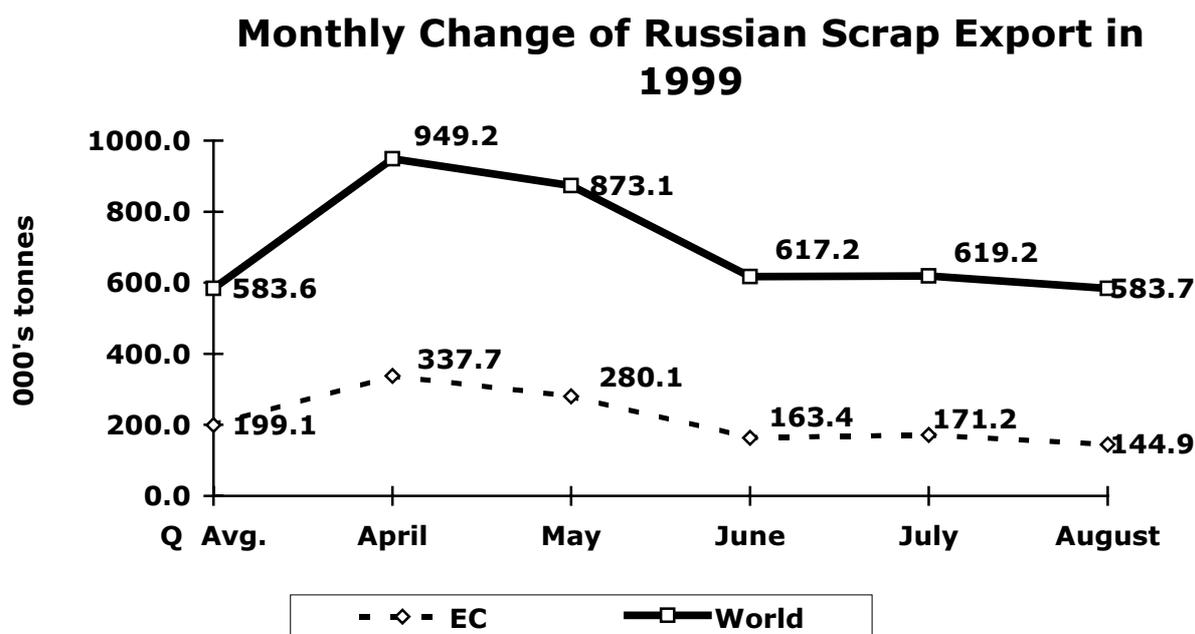
The policy of the European Union towards the Russian reforms is more benevolent. Unlike the American steel producers, our European colleagues do not refuse to communicate with us and we more often find mutual trade-off decisions. Nevertheless, the European steel market capacity is not less than that of the American one, but the volume of quotas imposed by the EU on imports of the Russian steel amounts to nearly 1.9% of the total EU steel imports (in terms of money), which corresponds to shares of such countries, as Norway (1.9%) or Switzerland (1.6%) (3).

In spite of that Russia forced to take an obligation that it will not restrict scrap export to EC. When the Russian government, experiencing difficulties with the budget, recently imposed a fiscal export duty on ferrous scrap, this followed by a threat from Brussels to reconsider even this negligible quota under the pretext of infringement of the obligation. Meanwhile, the statistics shows (see **fig.2, table 3**), that after a "surge" concurring with the moment when duty was imposed, the exports of ferrous metal scrap stabilised at a previous level. In the period of 1995-1998 the exports of ferrous scrap to the countries of the EU grew 4-fold, while our quota increased only by 17% and an annual increase in the quota on imports of the Russian steel rolled products under the Agreement with ECSC amounts to nearly 2.5%.

**Table 3. Russian scrap Export***000' tonnes*

	1995	1996	1997	1998	Q1 99	Q2 99	1 sem. 99
<b>Total</b>	1742,2	2735,2	5250	7617,6	1750,8	2524,5	4275,3
<b>Including ES</b>	660,4	1038,8	1601	2554,8	597,4	827,1	1424,5

Source: State Custom Committee of Russian Federation

**Figure. 2**

It is evident, that steel producers in the advanced countries, using antidumping legislation and having a support of their governments try to force out Russia into an ineffective sector of the global steel market and make it the supplier of scrap and semifinished products for their own steel industry.

We think that the deep political changes, which took place in the world, must be followed by the modifications in the world economic building which would promote free transfer of capital and, consequently, rational international labor division, usage of labor force, natural and energy resources, and ultimately rational location of production capacities.

Despite the old traditions of steel industry in globalisation of raw materials and finished products flows as well as in proliferation of technologies, this sector fell behind the other branches in globalisation of operational ties.

The formation of international steel alliances accelerated late in the 80s and in the 90s, when investors became attracted by the rapidly developing economies of Asian-Pacific Ocean region. Then, quite recently, foreign capital began investing into steel companies of Latin America as well as Central and East Europe, where privatisation and economic reforms created favorable investing climate. The motive force for investing was favorable market prospects and prime cost of products.

The restructuring of the steel industry of West Europe which has been going on for several decades brought about growth of transnational connections among companies (USINOR as an example). The investing motivation was an increase in competitiveness through production rationalisation and more effective utilisation of facilities of united companies.

As reasonably pointed out by the OECD Steel Committee In case of steel industry a set-up of international alliances would be useful because they would be able:

- to improve production efficiency by means of free overflow of investments to the regions where their usage would be more feasible,
- to reduce extra capacity due to rationalisation and phasing-out of inefficiently operating facilities,
- to enhance service opportunities owing to better flexibility of alliances in provision of requirements of multi-national clients
- to ensure support to free trade in steel in accordance with requirements of alliances and, in so doing, to advocate the opening of markets,
- to assist in more rapid development of studies and implementation of their findings in practice due to unification and more effective usage of enterprises' resources allocated for this purpose.

Some objective shortcomings of this process (related with a natural willing of investors to receive a maximal profit, and the willing of invested countries to attract investors), which can distort free competition, should be regulated by international community.

We stay for the development of the process of globalization of operational links and for creation of international alliances in steel industry as well as extension of this process to Russia. An economy and ecology require a minimization of raw materials and energy streams.

We advocate for renewal of negotiations concerning of the Multilateral agreement on steel trade. The Russian steel producers support the proposal of the U.S. Administration to organise global high level conference regarding the problems of world steel production and trade. We suppose the object of this conference should be well prepared. They shouldn't cover only a problem of "fair trade practice".

It is quite obvious that protectionism and different kinds of trade restrictions which are getting stronger today hamper rational capacity location and the process of globalisation of operational links. We suppose that antidumping legislation doesn't correspond with a fair competition because it is just a legal form of elimination of competitors with the hands of the government. Freedom of world trade in steel products and globalisation of operational links are two processes which stimulate each other, and the future of steel industry depends on their development. These processes are an integral part of general world economic progress aimed at decrease in disproportions of economic, scientific & technical and social advance of individual regions and peoples living in them.

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