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## Global Forum on Competition

**CRISIS CARTELS**

**Contribution from Mr. Ian Christmas**

**-- Session III --**

*This contribution is submitted by Mr. Ian Christmas (Director General, World Steel Association) under session III of the Global Forum on Competition to be held on 17 and 18 February 2011.*

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**CRISIS CARTELS: LESSONS FROM STEEL**

**-- Contribution from Mr. Ian Christmas [*]--**

## 1. Summary

1. This paper discusses examples of crisis in the steel industry in the last 50 years that have led to temporary changes to competition policy either in the form of government subsidies or use of protectionist trade measures. Since most of the world's steel is now produced and used in developing countries, the industry has particular interest for competition authorities in these countries.

## 2. The world steel industry

2. In 2010 the world produced and used over 1.3 billion tons of steel. Steel is vital to sustainable development and used in every aspect of modern life from construction, power stations, hospitals, schools, cars, ships, railways, machine tools to hypodermic needles for vaccinations.

3. Steel use in the world has grown over 5% p.a. during the last 10 years and at rates closer to 10% in China, India and other developing countries. China alone accounts for close to 50% of total steel use and production and over 60% world steel is now made and used in developing countries.

4. As a relatively high-value product, international trade is very important for steel accounting for over 40% of all steel shipments. Unlike many other materials, the concentration of production is very low with even the largest steel company accounting for less than 8% of total world steel production.

## 3. World Steel Association

5. The World Steel Association is based in Brussels and Beijing. Its members are over 100 steel companies and 60 national / regional associations which together account for over 85% of total world steel production. Its main role is to provide a strategic forum for the industry's chief executive officers to address common issues on sustainable development. It is the source of statistics for the industry and its Economics Department is the leading authority on forecasting the future demand for steel.

6. Other priorities include the promotion of steel in sustainable housing and new passenger cars, the collection of life cycle assessment data, the collection and reporting of $CO_2$ emissions by steel plants on a common basis worldwide, and a push towards zero accidents in the industry.

## 4. Competition

7. Since our members are separate companies operating as competitors in a single market, we are very mindful of our responsibilities to avoid any anti-trust or competition issues. We maintain a strict anti-trust compliance policy which bans any discussion of future pricing, production or investment by our member companies. A legal counsel is present at all our Board and Executive meetings. We strongly

[*] Note prepared by Mr. Ian Christmas, Director General, World Steel Association.

believe it is in the best interest of society, our customers and steel companies if individual steel enterprises are completely free to make their own business decisions. Competition between steel companies is in the best interests of the industry.

## 5. Anti-competitive behaviour in the steel industry

8. However, it would be wrong to suggest that the steel industry has been free from anti-competitive behaviour. Whilst many steel products are very specific in their design and application, others are commodities differing only in terms of price and service.

9. Over the years, particularly in construction products, there have been cases where competition authorities around the world have taken action against anti-competitive behaviour amongst steel producers and suppliers. In recent years there have been cases against steel companies in South Africa, Korea, Brazil and the European Union.

10. However, the factors leading to anti-competitive behaviour have sharply changed in the industry and I suspect the level of anti-competitive behaviour at national / regional levels is now insignificant compared with the past. However I have no way of knowing this.

11. The steel industry has also suffered from anti-competitive behaviour. A few years ago there was the break-up of a cartel operated amongst the suppliers of electric arc electrodes. This cartel was on a major scale and covered most of the world. The companies found guilty were subject to considerable fines.

## 6. Crisis in the steel industry

12. One company's crisis is another company's dynamic competition. For a company or an industry a crisis is manifest where the enterprise(s) are losing money on a significant basis and becoming unsustainable. Whether the crisis deserves favourable consideration by the general public and authorities is another matter. If the crisis of an enterprise is the result of its poor management and operations, then there is not a strong case for any government involvement. However, if the enterprise in question is a significant employer whose collapse would generate severe social problems, or if there is a real possibility that the business can be re-structured to restore its international competitiveness, then there may be a case for public acceptance of some extraordinary measures.

13. The most common form of public intervention to address a crisis in the steel industry has been either subsidies for continued operation and support for redundant workers, or the introduction of tariffs, quotas and other trade measures to protect the company from international competition over a period of time. There are plenty of past examples, but the consensus in the industry today is that subsidies that distort competition amongst steel companies and the use of protective tariffs are not in the interests of the industry nor its consumers and should be resisted.

14. The economic argument for the protection of an industry at some stage of its development is often based on the need to give an enterprise time to achieve an economy of scale. In the past the technology associated with the production of steel, particularly by the blast furnace route based on virgin iron ore, did indeed imply significant economies of scale. However today given that the total size of the markets in all countries is larger and the rapid developments in technology, it is true to say that economies of scale are less significant than in the past and that it is quite possible for a new steel company to be established in a developing country which could quickly move to a competitive level of operation. It is also the case for steel that technology is generally available from plant equipment manufacturers worldwide and that access to this technology is open to both existent and new entrants, including in developing countries.

## 7. Crisis cartels in the public interest

From the above arguments that steel is a high-value product with a very important role in international trade, it follows that the scope for national cartels is becoming more limited. Nevertheless, since most trade is on a regional basis and there is still a very high element of fixed costs in the total cost of producing steel (today labour costs are a very small part of total cost) there is still scope for anti-competitive behaviour at a national / regional level and requirement for vigilance from the competition authorities.

15. Steel companies can make the case to governments for some form of temporary protection or cartel to give them time to re-structure provided such requests are fully transparent and what is put in place is in the full knowledge of the market and the consumers. Any attempt to establish crisis cartels privately without the involvement or approval of public authorities, is clearly illegal and not in the public interest. However, in some countries certain industries have particular political leverage and therefore even if the measures are accepted by the government and in the public domain, we should not always accept that this is in the public interest.

## 8. Some examples of crisis in the steel industry

### *8.1 European Union*

16. The rapid growth of the steel industry and the reconstruction of west European economies came to a halt in the ‘70s following the first oil crisis. Steel companies in Europe started to accumulate considerable losses since it became clear that there was too much capacity and too many small uncompetitive enterprises. The ‘70s can be categorised as a period of increasing levels of state subsidies, significant state ownership and major financial losses. At the time, the Vice President of the European Commission, Etienne Davignon was responsible for the steel industry and he decided to invoke a state of manifest crisis in the industry as allowed under the Treaty of Paris establishing the European coal and steel community. Davignon said he saw a huge risk to the breakdown in the market for steel in Europe given the mounting financial and social problems associated with the industry, which at that time was a major employer in particular regions and towns.

17. The founding fathers of the European Union had given the European Commission tools to do the job since the European Coal and Steel Community gave the High Authority, subsequently the European Commission, the power to regulate pricing regimes, levels of production etc.

18. From the late 70’s to the mid ‘80s under the “Davignon Plan”, the European steel industry was highly regulated in an officially sponsored cartel. Production was allocated to individual steel plants and minimum prices were set. Inspectors were stationed at the end of manufacturing lines to ensure that steel plants did not exceed their quota. These draconian measures were introduced against the objections of many steel using industries. These measures merely froze the unsatisfactory state of affairs of the industry but were a prelude to major restructuring of the European steel industry which proceeded over the next 15 to 20 years.

19. It is interesting to note that some of the restructuring required the re-nationalisation of steel companies as is the case in Sweden and France. When the restructuring process was complete these companies were then privatised. The process of plant closures and restriction of subsidies to only social measures and retraining of redundant workers took a long time. In reality it is only the last ten years that the European steel industry has remerged as fully competitive, much leaner and dynamic business.

### *8.2 India*

20. Following independence the Indian Government took the view that steel as a “commanding height” of the economy should mainly be in public ownership. As a result, the state owned Steel Authority

of India was given a near monopoly in steel production. No private steel company was allowed more than 2 million tons production and until the end of the '90s only SAIL and TATA were the major suppliers. The steel industry was relatively unprofitable, investment levels low and India as a whole lacked investment in infrastructure and steel which was required for its growth.

21. In the early '90s the Indian Government changed its view and disbanded the cartel allowing new private companies to invest in steel with a liberalisation of steel prices and a reduction in import tariffs.

22. Fifteen years on, the Indian steel industry is dramatically more competitive with a number of new Indian based companies having entered the market such as Jindal and Essar. Both SAIL and TATA have also grown and become more competitive in the ensuing period.

### *8.3 United States of America*

23. The '80s and '90s saw rapid growth in the USA of steelmaking based on the re-melting of steel scrap. Companies such as Nucor and Commercial Materials using new technology developed a new business model for steel with much greater flexibility in operations and production costs over the business cycle. Meanwhile the former major steel companies based on integrated steelmaking technologies continued to experience low growth, lack of investment and poor profitability. The US became a major importer of steel.

24. In 2003 the US steel industry convinced the Bush Administration that some special measures were required to give them breathing space for fundamental restructuring of the industry. Against the protest by major steel using sectors, this was agreed and the government introduced tariffs and quotas to give temporary breathing space to American industry. It also took over responsibility for pension liabilities.

25. Over the next three to four years the trade unions changed their negotiating stance and US Steel took over National Steel and Stelco in Canada, whilst ArcelorMittal consolidated LTV, Bethlehem, Inland, Weirton, and Dofasco. As a consequence, today the electric arc sector and the integrated sector in North America are more competitive and able to compete equally with others around the world.

## 9. Issues for developing countries

26. The issue for governments in industrialised countries in the steel industry is how to manage the problem of overcapacity and maintenance of competitiveness.

27. In developing countries the issue is how to foster investment in steel which will create a growing and internationally competitive industry. Common incentives used in many countries include state investment in developing infrastructure such as roads, railways and ports; financial support for training new workforce, and tax deductions and credits to reduce investment costs. The use of such incentives runs the risk of objections from competitors in other countries who consider such measures as unfair competition. The use of trade protection which allows higher steel prices in the country may also harm the competitiveness of steel using industries.

28. In recent years some developing countries have favoured domestic steel enterprises. For example, in China the State refuses to allow foreign steel companies to acquire majority shares in Chinese steel companies. It claims the policy is to enable the Chinese steel enterprises to become "global leaders". It is difficult to see the justification for this in economic terms. Similarly in India it has been much easier for Indian based steel companies to expand than for foreign owned steel companies.

## 10. Lessons from steel

29. As for all industries, competitive authorities need to be vigilant of anti-competitive behaviour in a major industry such as steel. Where domestic prices are significantly above international levels and steel products being traded are relatively undifferentiated, these may be warning signs of some inefficiency in the steel markets. However the fierce competitive nature of the steel industry, its low levels of concentration, the importance of trade, and the availability of technology for new market entrants, make the industry much less of a concern today than was the case in the past.

## 11. Competition issues for steel

30. The steel industry has some concerns on competition policy in two important areas. Firstly where governments in a particular country allow subsidies or other anti-competitive behaviour which creates artificially high profit levels and prices in the home market, this is an indirect subsidy that distorts competition in the industry on a global basis.

31. Secondly the steel industry faces a very high degree of concentration in the supply of key materials such as seaborne iron ore.

32. The international iron ore companies have exercised their market position with a dramatic increase in the prices of raw materials for the steel industry and society as a whole. Whether it is in the public interest that so much of the economic rent of the steel production cycle should be captured by these mining companies requires the continued close scrutiny by competition authorities. In this regard, because it is a global business, the national / regional competition authorities need to work together.