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and welfare impact of the 2002 US emergency steel
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Read, R

The Department of Economics
Lancaster University Management School
Lancaster LA1 4YX
UK

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**The Political Economy of Trade Protection:
the Determinants & Welfare Impact of the 2002 US Emergency Steel
Safeguard Measures**

Robert Read*

Abstract

This paper analyses the political economy of trade protection in the context of the factors determining the US Emergency Safeguard Measures for steel imposed March 2002. The paper identifies several factors in addition to the official justification stated problems of global over-capacity and the penetration of imports in the US market, namely the continued failure to restructure poorly performing firms, failure of previous attempts at protection and the influence of the domestic steel lobby and short-term political gains to the Bush Administration of protectionist action. The paper also reviews several *ex ante* and *ex post* empirical studies of the impact of the steel Safeguards on the steel industry and downstream steel-consuming activities. All of these studies find that the costs of the Safeguard Measures outweighed their benefits in terms of aggregate GDP and employment as well as having an important redistributive impact. The paper provides a brief summary of the subsequent WTO steel case and the final resolution of the dispute. The evidence suggests that the steel Safeguards owed more to political expediency than justification for protection under the WTO rules.

Key words: WTO, steel dispute, Emergency Safeguard Measures, costs and benefits of protection.

The Political Economy of Trade Protection: the Determinants & Welfare Impact of the 2002 US Emergency Steel Safeguard Measures

Robert Read

In June 2001, the US Trade Representative (USTR) Robert Zoellick launched a Section 201 investigation by the US International Trade Commission (USITC) into the difficulties being encountered by the US steel industry. The objective was to establish whether foreign imports were causing injury and therefore whether they merited the imposition of Emergency Safeguard Measures. The USITC investigation covered imports with a combined value of some \$17 billion, more than half of total US imports of steel in 2001.

The preliminary findings found that 85 per cent of the steel imports subjected to scrutiny were causing serious injury (USITC, 2001). Further, US steel prices were found to be at 20-year lows and around 30 per cent of the industry (by capacity) was in bankruptcy with accumulating losses. The USITC Report found 16 categories of items in four broad steel product groups to be causing serious injury, detailed in Table 1. These products comprised some 60 per cent of EU exports of steel and steel products to the United States, worth a total of \$4 billion. Many of these items were already subject to pre-existing protective measures in the form of anti-dumping and countervailing duties.

While unanimous in their findings of serious injury being caused, the members of the USITC differed concerning the appropriate remedy. Tariffs ranging from 20 to 40 per cent as well as quotas were recommended.¹ The affected steel companies and labour unions submitted requests for tariffs of 40 per cent while half of the House of Representatives wanted quotas on steel imports. On 5 March 2002, President George W. Bush announced the unilateral imposition of a combination of up to 30 per

¹ The USITC Report also proposed that further assistance be provided to steel workers and affected communities through the National Emergency Grants programme, including effective job training and direct assistance with the industry's legacy costs. These legacy costs comprise an estimated \$13 billion of contract commitments by struggling steel firms, primarily integrated mills, in the provision of employee health-care and pensions coverage. The result of unionisation and long-standing labour contracts in the integrated mill sector, they have been a major impediment to the restructuring of the sector. The newer mini-mills generally operate with more flexible labour contracts and have opposed US Government funding of legacy costs in the integrated mill sector. The USITC recommended that the legacy cost problem should be dealt with by Congress (Zoellick, 2002a).

cent tariffs and some tariff quotas, effective 20 March for three years. These were introduced as Emergency Safeguard Measures against:

Surges in foreign imports ... to ensure that American industries compete on a level playing field [given] the harm from 50 years of foreign government intervention in the global steel market [in terms of 30] bankruptcies, serious dislocations and [20,000] job losses [from the] glut of cheap imports, global over-capacity and ... falling prices leading to falling profitability [and] to give the US steel industry time to restructure without harming the US economy (Bush, 2002).

With only limited exceptions, President Bush imposed protection that was significantly *higher* than that recommended by the USITC Commissioners (see Table 1) to provide the domestic industry with ‘breathing space to restructure and become newly competitive’ (Zoellick, 2002a). The margin of protection was to be reduced annually over the three-year span of the measures. The first annual reduction was made on 21 March 2003, when the steel Safeguard Measures were reduced by at least 20 per cent (US Department of Commerce and Office of the US Trade Representative, 2003). Not surprisingly, the US imposition of the Safeguards provoked a powerful response from some of its major trading partners, notably the European Union (EU).

This paper examines the origins of the 2002 US Emergency Safeguard Measures on steel and the domestic benefits and costs of the Action. The US Safeguards are identified as being the culmination of several inter-related factors: the poor international competitive position of the domestic US steel industry; the downturn in the US economy at the end of the 1990s; the strength of the US steel industry lobby; and political expediency. These factors are analysed in turn. It is argued that none of these factors, individually or collectively, accord with the necessary conditions for Emergency Safeguard Measures as laid out in GATT 1994 Article XIX or the WTO Agreement on Safeguards which permit the use of Emergency Safeguards to prevent domestic injury resulting from a surge in imports (WTO, 1999). This is followed by a review of the empirical studies of the impact of the Emergency Safeguard Measures on the US economy, all of which find that they resulted in a net loss in employment and GDP. A brief summary of the trade dispute and the WTO steel Panel’s findings is then provided. The final section draws some conclusions.

1. The Determinants of the 2002 US Emergency Safeguard Measures on Steel

The US justification for the Emergency Safeguard Measures on steel was set out by both President Bush and USTR Robert Zoellick. Their arguments for the unilateral tariff were framed in terms of Article XIX.1 of the GATT 1994 and Article 2.1 of the Agreement on Safeguards. They cited the damage being done to the US steel industry by a surge in imports of 16 categories of steel product (listed in Table 1) from the EU, China and Japan, among others, and stressed the temporary nature of the measures. Official statements also emphasised the extensive use of unfair trading practices by steel exporters to the United States and that the Safeguards were ‘launched to restore market forces to world steel markets’ (Bush 2002). USTR Zoellick referred to the heavy use of subsidies by the EU (\$50 billion since the 1970s) and China (\$6 billion in 2001), the high import penetration of the EU and Japan in the US market ‘even though they are no more productive’ and the use of similar measures by the EU against steel imports from Russia and Ukraine (Zoellick, 2002b).

It is interesting to consider the principal factors determining the imposition of the US steel Safeguards more closely. These are: the international competitive position of the US steel industry; the impact of the economic downturn in the United States at the end of the 1990s; the influential role of the domestic steel industry lobby; and the need for political expediency. These factors are analysed in turn and then discussed in the context of the WTO rules on the use of Emergency Safeguard Measures.

The Declining International Competitive Position of the US Steel Industry

The international competitiveness of the US steel industry has been declining since the 1970s. The primary domestic cause has been a lack of investment in new technologies, inflexible labour contracts and increasing legacy (health and pension) costs. There has also been a substantial expansion of low-cost steel production in many industrialising countries, notably China and Korea, giving rise to global over-capacity and increasing import penetration. The 2002 Emergency Safeguards were the most significant of a series of restrictive trade measures on US steel imports in recent years.

The Domestic Problems of the US Steel Industry

The US steel industry is almost dualistic sectoral in structure with large-scale integrated mills producing basic steel and bulk steel products alongside smaller mini-mills producing batch niche steel products. The mini-mills tend to be profitable specialised enterprises utilising advanced technology to produce high value added output. Many large integrated mills however, are loss-making producers of standard steel products reliant upon old technologies.

Many of the firms in the US integrated mill sector have yet to complete the fundamental restructuring of the sector begun in the 1980s, requiring investment in new cost-reducing technologies, the closure of capacity and consolidation. This meant that their high costs stifled their profitability and constrained new investment, even during the boom years of the mid- to late 1990s. Basic steel production is a large-scale capital-intensive activity but many US integrated mills are below the critical size necessary to be internationally competitive. Two-thirds of US output is produced by twelve firms, with an average annual output of 8.5 million tonnes each. This compares with just six firms taking a similar share of the substantially larger EU market, producing an average of nearly 27 million tonnes each (Commission of the European Communities, 2001).

The US integrated mill sector has the features generally associated with a declining industry – high costs, out-dated technology, low profitability and increasing import penetration. Many of the most vulnerable steel plants were located in the key northeastern ‘rust-belt’ states of Ohio, Pennsylvania and West Virginia and had been badly affected by high unemployment and industrial decline since the 1970s. The failure of the integrated mills to restructure meant that, unlike the more efficient mini-mills, they were unable to take full advantage of the economic recovery in the 1990s.

The strength of the dollar during the 1990s boom reduced the cost of imported steel and steel products, leading to increased import penetration in the US market. The United States became a significant net importer of steel, reaching a peak of 34 million tonnes in 2000 with import penetration of 30 per cent. At the same time, US steel output also expanded: by nearly 15 per cent (19 million tonnes) between 1993 and 2000 (Commission of the European Communities, 2001). This compares with a one per cent (two million tonnes) fall in EU steel output in the same period and its switch to

being a net importer of steel between 1997 and 2000, with import penetration reaching 16 per cent (Commission of the European Communities, 2001).

Much of the growth in US output however, came from the mini-mills in the form of higher value added steel products; they were responsible for almost 50 per cent of US steel output in 1998, up from 15 per cent in 1981. The growth of the mini-mill sector is reflected in the average productivity data, which rose from ten man hours per ton to four and, in some mini-mills, just two (Lindsey *et al.*, 2001). Import penetration was greatest in basic steel products that competed with output from the integrated mills. These developments occurred in the face of anti-dumping and countervailing duties being imposed on US steel imports from several sources, including the EU (see below).

Over-Capacity in the Global Steel Industry

The United States has been at the forefront of international efforts to reduce and rationalise the global steel industry under the OECD High-Level Steel Initiative. At first, the major producing countries pledged to reduce global excess capacity by cutting annual production by 115 million tonnes by 2005 (OECD, 2003a). This figure has since been raised to 140 million tonnes, around 13 per cent of global capacity, out of total excess capacity estimated at 180 million tonnes. Excess capacity of 105 million tonnes was closed between 1998 and 2002. The recovery of steel consumption, with four per cent growth recorded in the first half of 2003, has meant that over-capacity is now falling rapidly (OECD, 2003b).

The December 2002 High-Level Meeting launched preparatory discussions paving the way for the elimination of many market-distorting subsidies through the drafting of a Steel Subsidies Agreement. This Agreement has yet to be finalised and may, ultimately, be brought under the auspices of the WTO (OECD, 2003c).

Protective Measures Against Steel Imports by the United States Since 1990

From a US viewpoint, over-capacity in the global steel industry is primarily the result of state intervention in many other countries, creating trade distortions through unfair trading practices such

as subsidies, and fuelled by the desire of countries for ‘commanding heights’ industries (Zoellick, 2002b). The increasing penetration of the US market by low-cost steel imports has provided the necessary justification for trade intervention. The 2002 steel Safeguards therefore need to be considered in the context of the recent US track record of trade protection in steel.

The United States has a long-standing history of protectionism against steel imports. US imports of steel were, from 1984 to 1992, subject to Voluntary Restraint Agreements (VRAs) negotiated with the major steel exporting countries by the first Reagan Administration. Both Clinton Administrations responded aggressively to any positive finding of injury by the USITC while adhering to WTO disciplines (see Brainard, 2001) such that the VRAs were therefore allowed to lapse in March 1992. There followed a wave of more than one hundred Section 201 complaints to the USITC by the steel industry calling for anti-dumping and countervailing duties on low cost imports (Lindsey *et al.*, 1999). Most of the USITC investigations however, found little evidence of ‘substantial injury’.

A second surge of USITC steel complaints in mid-1998 resulted from the global downturn caused by the 1997 Asian Crisis, the subsequent diversion of exports to the US market and a two-month strike at General Motors. Although US output in 1998 was down on the record high of 1997, it was still the second best year on record (see Griswold, 1999; Lindsey *et al.*, 2001). The US steel industry lobbied extensively for the introduction of retroactive anti-dumping duties, a three-month universal quota on steel imports from selected countries and the revision of Section 201 to eliminate the need for a finding of ‘substantial’ injury. Anti-dumping and countervailing duties were nevertheless imposed on steel imports from the EU, Japan, Korea, India and Russia, among others. The magnitude of these duties varied greatly, both between countries and targeted firms, but some were very large.² The steel imports targeted by the most substantial of these measures fell sharply as a consequence. Many of the anti-dumping and countervailing actions were referred to the WTO and subsequently found to be illegal. The steel quota proposal was vetoed by President Clinton in spite of a majority vote in the House of Representatives (289 to 141) and Section 201 remained unchanged.

² For example: Taihan of Korea faced a duty of 58.79 per cent on sheet steel (WTO, 2000a); Kawasaki Steel of Japan, a duty of 67.14 per cent on hot-rolled steel (WTO, 2001); Steel Authority of India Ltd., a duty of 72.49 per cent on steel plate (WTO, 2002a); Aceralia of Spain and ILVA of Italy, duties of 36.84 and 26.12 per cent respectively on steel plate (WTO, 2000b).

The record therefore suggests that successive US Administrations have had a predisposition to ‘supply’ protection to the steel industry to reduce import competition. The 2002 complaint against the US Emergency Safeguard Measures was the *sixth* steel case to be launched by the EU against the United States at the WTO since 1998 and a further action was launched in July 2002. Many of the anti-dumping duties and countervailing measures imposed in 1998 were subsequently removed because the creation of the WTO, its more effective Dispute Settlement Understanding (DSU) and new Agreements on Subsidies & Countervailing Duties and Safeguards have increased the leverage of affected trade partners where such measures are not WTO-compatible. This applies equally to the 2002 Emergency Safeguard Measures for steel.

The Impact of the 2000 Economic Downturn on the US Steel industry

The economic boom of the 1990s provided some respite for the US steel industry, in spite of the increasing penetration of low-cost imports. The vulnerability of the least competitive parts of the industry, primarily the integrated mills however, was aggravated by the economic downturn in 2000. This downturn was of a much greater intensity than that in 1998 and necessitated urgent intervention if the restructuring and/or closure of the poorest performing firms were to be deferred. This adverse impact arose in spite of the array of anti-dumping and countervailing duties on steel imports from the EU, Japan, Korea and Russia that had been put in place by the Clinton Administration in 1998.

The downturn was accompanied by an appreciation of the US dollar during 2000 and 2001, by around eleven per cent with respect to Sterling. Domestic steel producers were therefore hit by both depressed domestic demand and cheaper imports although US steel imports actually fell from 34 million tonnes in 2000 to 23.5 million tonnes in 2001 - almost ten per cent of the market. All of this occurred during the USITC investigation and prior to the initiation of the 2002 steel Action.

The Influence of the US Steel Industry Lobby

The US steel lobby comprises the industry association, The American Iron & Steel Institute, labour unions, notably the United Steelworkers of America (USWA), and congressional representatives from the major steel-producing states. This lobby has been highly successful in securing support from successive US Administrations for protection against imports during domestic downturns, although it is evident that President Clinton was less receptive to these demands than his immediate predecessors. In spite of the steel industry's declining domestic economic importance, its spatial concentration in the northeastern rust-belt means that the national political leverage of the steel constituencies in these states remains strong.

The onset of the economic downturn in 2000 intensified the efforts of the steel lobby to stave off further lay-offs and firm closures in the industry, exacerbated by the appreciation of the dollar, in spite of falling imports. President George W. Bush was viewed as being more receptive to protectionist sentiments than was the Clinton Administration such that the protection originally sought in 1998 could now be introduced. The consensus among the steel lobby was that enhanced protection would provide sufficient leeway for the less competitive firms without affecting the general recovery of the US economy. The American Iron & Steel Institute also claimed that the impact on consumer prices would be minimal and there would be no meaningful employment effects on steel-consuming industries (BBC, 2002). USTR Robert Zoellick however, admitted that the Safeguards would raise domestic steel prices by between six and eight per cent (Zoellick, 2002a).

The Need for Political Expediency

During the presidential election campaign of 2000, George W. Bush promised help for the steel industry in Ohio and West Virginia over and above that provided by President Clinton in 1998. With the mid-term elections for the US House of Representatives in November 2002 also finely balanced, President Bush needed to win the key steel-producing states of Ohio and Pennsylvania where many of the affected integrated mills were located. The USITC Section 201 investigation and the subsequent Emergency Safeguard Measures in March 2002 can therefore be seen as an attempt to assuage a key

domestic political swing constituency. The Safeguards did not address the long-term structural problems of the steel sector – a lack of investment and competitiveness – but were rather a politically expedient strategy that *appeared* to assist the industry and appeased its protectionist sentiments.

The steel Safeguards provided a temporary panacea by again targeting low-cost imports as well as raising additional tariff revenue at a time of fiscal restraint so as to fund pledged tax cuts. The term-structure of the Safeguard Measures meant that the benefits were immediately visible in terms of reduced imports and higher domestic prices. The costs however, would be delayed and more dispersed. The problematic \$13 billion legacy costs – on which restructuring was dependent – were left to Congress while the costs of any nullification or impairment and retaliation would be borne by US exporters and would not necessarily have any direct link to steel. Further, the domestic public perception of retaliatory moves by US trade partners might not be linked to the steel issue at all.

The Bush Administration is likely to have regarded the anti-dumping and countervailing duties, introduced by President Clinton, as inadequate in the context of the 1998 House vote for blanket protection and also expendable in the light of the succession of adverse WTO decisions against them starting in 2001. From this perspective, the steel Safeguards were not providing supplementary or ‘double’ protection but rather constituted measures that should have been imposed in 1998. Further, President George W. Bush was not as concerned with the legal issues of evidence of serious injury and WTO consistency as the Clinton Administration. The predominance of domestic factors suggests that the US Safeguards were neither a retaliatory response to the success of the EU and others in the WTO steel anti-dumping cases nor an exercise of US muscle given the failure of the EU to comply in the WTO beef hormones dispute.

The steel Safeguards have also been viewed as a bid to secure Congressional support for the fast-track Trade Promotion Authority (TPA) which grants the President greater authority to negotiate trade agreements in return for enhanced oversight by Congress.³ TPA was the principal first-term trade legislative priority of George W. Bush and was approved by Congress and signed into law as the Trade Act of 2002 less than five months after the imposition of the steel Safeguards.

³ The author is grateful to the anonymous referee for this insight.

Exceptions to the US Emergency Safeguard Measures on Steel

The Emergency Safeguard Measures were not applied to imports from those countries with which the US had free trade agreements, i.e. the members of NAFTA (Canada and Mexico) together with Israel and Jordan (USITC, 2002). Tariff exclusions were also made for Australia and South Korea, along with ‘generous’ tariff quotas for Brazil and Russia, based on import levels in 2000. The principal countries affected were therefore China, the EU and Japan.

The USITC and the US Department of Commerce announced that they were willing to consider objections to the Safeguard Measures submitted by US steel consumers as well as foreign suppliers (for the exclusion criteria, see US Department of Commerce and Office of the US Trade Representative, 2002). By the time of the seventh and final round of exclusions in March 2003, some 1,022 separate steel product categories had been exempted. This large number of exclusions undermined the USITC’s original recommendations, given their blanket application and lack of precision at the individual product category level.

The broad-brush targeting of the US steel Safeguards had several effects. Protection applied to steel products that were not causing injury and/or were unavailable domestically. Domestic users of such products therefore experienced temporary shortages and large short-term price hikes, sometimes leading to lay-offs and job losses. The exclusion process required firms, many of which were relatively small, to divert scarce resources to lobbying. There were also suggestions of bias; half of the exclusions (by volume) applied to unfinished steel imports (Hufbauer and Goodrich, 2003a). The USWA alleged that some steel firms increased their profits at the expense of US jobs by sourcing steel offshore and processing it domestically. The extensive exclusion process also damaged the credibility of both the USITC and the Safeguards at the WTO and in the broader domestic public sphere.

3. The WTO and the US Emergency Steel Safeguard Measures

The GATT 1947 rules governing safeguards were dealt with under Articles XII and XIX. The former was designed primarily to assist developing countries experiencing Balance of Payments crises and

would have been well nigh impossible for the United States to justify. Article XIX is widely known as the Safeguard Provision or Escape Clause under which countries can cite domestic injury:

[A]s a result of unforeseen developments [arising from any product being imported] in such increased quantities ... as to cause or threaten serious injury to domestic producers of like or directly competitive products ... and to the extent and for such time as may be necessary to prevent or remedy such injury' as justification for the suspension of concessions. GATT 1947, Article XIX.1(a).

The original Article was very opaque in its reference to 'unforeseen developments' such that it was open to very broad interpretation. Some of this opacity was removed by the WTO Agreement on Safeguards, which limits the scope of emergency action to serious injury as a result of increased imports and requires that its application is non-discriminatory. Any action can only be taken as a result of an investigation by a competent authority (the USITC) and must provide detailed robust evidence that serious injury is attributable to increased imports. Safeguard Measures may only be applied 'to the extent necessary to prevent or remedy serious injury' (WTO, 1999).

The primary justification for the US Emergency Safeguard Measures was government intervention and unfair trading practices in many steel-exporting countries. There is certainly some merit in the view that the steel industry in many countries is characterised by state involvement and the use of subsidies. These practices however, are covered by specific Articles in the GATT 1994 and the Agreement on Subsidies & Countervailing Measures. A critical issue is therefore why the United States did not use this Agreement but instead relied upon GATT Article XIX and the Safeguards Agreement, particularly given its claim of international trade being affected by extensive state intervention and subsidies. Many US imports of steel products however, were already subject to countervailing duties and on-going WTO complaints (see Section 2a.iii). There are strict time limits on the application and re-imposition of such duties so that the United States could not initiate further action that amounted to 'undue double protection' (Commission of the European Communities, 2001).

The arguments presented by the United States to justify its Emergency Safeguard Measures for steel however, did not fall within the purview of GATT Article XIX or the Safeguards Agreement. While they might have been permissible under the original GATT 1947 Article XIX, the greater

rigour of the Safeguards Agreement in defining the precise circumstances under which such actions are permissible suggested that the US action was unlikely to accord with the requirements of the WTO.

4. The Domestic Benefits & Costs of the US Emergency Steel Safeguard Measures

Domestic support in the United States for the 2002 Emergency Safeguard Measures on steel was by no means unanimous. Many steel-consuming firms opposed the tariffs, primarily because of their knock-on effects on production costs at a time of sluggish economic growth. The US consumer lobby group Consuming Industries Trade Action Coalition (CITAC) contended that the new tariffs would cost far more jobs in steel-using industries than they would save in the steel industry itself.

The Direct Impact of the Emergency Safeguard Measures on US Steel Producers

An initial *ex ante* study undertaken for CITAC, using the original USITC recommendations (Table 1), estimated that an anticipated 9.2 per cent rise in steel prices would save some 8,900 steel jobs at a cost of \$450,000 each (Francois and Baughman, 2001). A second study estimated that steel tariffs of 15 to 20 per cent would cost \$2 billion and save 3,500 jobs – at a cost of \$584,000 each (Hufbauer and Goodrich, 2002).

The most comprehensive study of the actual impact of the steel Safeguards is the USITC Mid-Point Report, published in September 2003 (USITC, 2003a). The Report found that, in the 18 months following the imposition of the Safeguards, the US steel industry underwent major restructuring and consolidation. This included several large mergers and acquisitions, the closure of out-dated plant, substantial investment in new capacity, increases in output, improvements in capacity utilisation and productivity and more flexible labour contracts. Not all of these developments were viewed as being the direct result of the steel Safeguard Measures (USITC 2003a).⁴

The steel Safeguard Measures had a relatively consistent and predictable impact on trade. Reduced imports from targeted countries (generally by between 20 and 50 per cent) were replaced by

increased purchases of domestic output and imports from other sources. The greatest impact was on Tin Mill Products and Rebar, with falls of nearly 63 per cent and 78 per cent respectively in imports, possibly because of easily available alternative supplies (USITC, 2003a). The recovery of the industry however, was constrained by weak demand caused by the general economic downturn, compounded by across-the-board rises in domestic steel prices. New construction activity, a major end-user of steel products, was particularly weak. In spite of increased domestic sales at higher prices, firms' operating margins in Carbon Alloy & Tubular Steel, Stainless & Tool Steel and Rebar deteriorated. Margins in the former were aggravated by higher rates of protection on its steel inputs (30 as opposed to 15 per cent) while negative margins in the latter two actually deteriorated (USITC, 2003a).

The Indirect Impact of the Emergency Safeguard Measures on US Steel Consumers

The *ex ante* study by Francois and Baughman estimated that some 74,500 jobs would be lost, including 15,300 in steel-consuming industries, as a result of the anticipated 9.2 per cent price rise (Francois and Baughman, 2001). The same authors found *ex post* that almost 50,000 jobs had been lost in Fabricated Metals, Machinery & Transport Equipment and over 197,000 in all steel-consuming industries during 2002 (Francois and Baughman, 2003). The latter figure is greater than the 187,500 employed in the US steel industry as a whole. These broad findings were confirmed by Hufbauer and Goodrich (2003b), who ascribed some 39 per cent of the rise in US steel prices in 2002 to the tariffs with an estimated direct employment effect of around 19,500 jobs. The American Iron & Steel Institute hotly disputed these findings and claimed that jobs were created in both upstream and downstream industries (Morici, 2003).

The USITC also analysed the impact of the Safeguard Measures on US steel-consuming industries (USITC, 2003b). Using a computable general equilibrium (CGE) model and 1997 benchmark US input-output data, the study found that the aggregate welfare impact ranged between plus \$65.6 million and minus \$111.0 million, with a central estimate of minus \$41.6 million. The impact on GDP was a fall in the returns to capital of \$294.3 million and \$386 million to labour offset

⁴ A US Government agency, the Pension Benefit Guaranty Corporation, also acquired more than \$8 billion in

by increased tariff revenue of \$649.9 million (USITC, 2003b). Actual tariff receipts were \$294 million, such that the USITC study greatly underestimated the adverse effects on domestic prices and imports (Hufbauer and Goodrich, 2003b). The USITC estimate of the aggregate impact on GDP of minus \$30.4 million was almost negligible but its redistributive effects were more substantial. US Government revenue benefited significantly at the expense of falling private sector profits and wage payments, including increased unemployment.

US steel prices rose steeply in the first half of 2002, notably hot-rolled sheet by 81.8 per cent and cold-rolled sheet by 69.4 per cent. The price rises over the whole of 2002 however, were much lower – 27 per cent and 19 per cent respectively (Francois and Baughman, 2003). The domestic steel-consuming industries most adversely affected were motor vehicle parts and some steel fabricating activities (USITC, 2003b). The price squeeze in the car and defence equipment industries was curbed by their monopsony power and use of long-term supply contracts. Many US steel-consuming industries however, are highly atomistic - some 98 per cent of the 193,000 steel-using firms have less than 500 employees (US Small Business Administration, 2000). As price-takers, the steel price rises had a severe impact on their costs, profit margins and employment, shifting demand towards imported manufactures, although these effects were partly mitigated by the higher cost of imported steel.

The tightening of the US steel market had several additional effects as steel-consuming firms attempted to reduce their costs. There was a suspected increase in trade deflection to avoid the higher steel duties, whereby affected products were imported via third countries, particularly Canada and Mexico. The American Iron & Steel Institute also expressed concern about: ‘substantial transformation’ in third countries for customs reclassification; in-bond shipments re-crossing NAFTA borders to obscure their origin; and simple circumvention through the false classification of products (American Iron & Steel Institute, 2002).

5. The WTO Steel Case

The EU responded to the announcement of the US Emergency Safeguard Measures on 5 March 2002 almost immediately by submitting a complaint to the WTO on 7 March 2002. This was followed by complaints from Japan and Korea, China, Switzerland and Norway. The grounds for the complaints were that the US Measures breached its obligations under several Articles of the GATT 1994 and the Agreement on Safeguards (see Commission of the European Communities, 2002a; WTO 2002b). A Procedural Agreement meant that all of the complaints could be considered simultaneously by a single Panel. The WTO steel dispute is discussed at greater length in Read (2005).

The Threat of Retaliatory Action Against the United States

The EU and several other targeted countries had already threatened retaliatory action against the United States after the publication of the USITC's preliminary findings in October 2001 but this threat failed to deter the imposition of the steel Safeguard Measures. The EU introduced its own steel Safeguards on 27 March 2002 for an initial period of six months, to last no longer than those of the United States, as a legitimate response to the surge in its steel imports - which rose by 73 per cent between 1997 and 2001 (Commission of the European Communities, 2002b).

The EU argued that it was also entitled to compensation of around €2.4 billion per annum for the lost value of trade concessions (Commission of the European Communities, 2002c). Most of the other plaintiffs however, took a more conciliatory stance (*Bridges Weekly Trade News Digest*, 2002). The intention of the EU (and Japan) to take immediate retaliatory action provoked a strong reaction from the United States since its legal basis could only be established retrospectively by a WTO Panel. The EU retaliatory measures against the United States targeted products in 'short' and 'long' lists, the former being a specific sub-set of the latter (see Commission of the European Communities, 2002d, Annexes I, II). The imports targeted were specifically chosen because of their importance exports to key marginal states in the 2004 US Presidential Election. The USITC exclusion process however, led the EU to postpone the 'short' list of sanctions in July 2002 and then suspend it in September 2002.

By this time, some 50 per cent of EU steel exports to the United States had been exempted from the US Safeguard Measures (Commission of the European Communities, 2002e).

The WTO Panel Decision on Steel

The WTO steel Panel published its findings on 11 July 2003 that the US Safeguard Measures were inconsistent with the GATT 1994 and the Agreement on Safeguards (WTO, 2003a). The principal findings are summarised in Read (2005, Table 4). The Panel Report acknowledged the merit of the claim that the US steel industry was adversely affected by the increasing encroachment of imports. The US case however, was undermined by flaws in the USITC Section 201 investigation and compounded by the imposition of greater protection by President Bush than the levels recommended by the USITC. The Emergency Safeguard Measures were therefore more substantial and applied to a broader range of product categories than was justified by the USITC investigation. There was insufficient evidence to support the case of unforeseen developments, increased steel imports (either absolute or relative), causation and parallelism. Even for those steel products for which there was supporting evidence, the USITC investigation was not product-specific and failed to explicitly exclude other possible causal factors, except for Stainless Steel Rod (WTO, 2003a). The WTO Panel was also unhappy about the inconsistent product definitions for Tin Mill Products and Stainless Steel Wire used by the US Trade Commissioners.

The US Appeal Against the WTO Panel Decision on Steel

The United States announced that it would appeal against the WTO findings almost immediately and that the Safeguard Measures would remain in place (US Department of State, 2003). The principal grounds for the appeal were that the findings were based upon error on issues of law and interpretation of GATT Article XIX and the Agreement on Safeguards and that the Panel was not objective and failed to set out the basic rationale behinds its findings and recommendations (WTO, 2003b).

In its Report published on 10 November 2003, the WTO Appellate Body upheld the general findings of the steel Panel although decisions on Tin Mill Products and Stainless Steel Wire were reversed (WTO, 2003c). The Appellate Body therefore recommended that the United States bring its Emergency Safeguard Measures for steel into conformity with its obligations under the WTO.

The Removal of the US Emergency Safeguard Measures & Conclusion of the WTO

Steel Dispute

The Appellate Report generated considerable controversy in the United States as well as presenting President George W. Bush with a critical policy dilemma amid fears of a major trade war with the EU. While domestic US steel users and consumers welcomed the WTO Decision and urged the President remove the Emergency Safeguard Measures, there was trenchant opposition from the domestic steel industry, among others. The President had until 10 December 2003 to decide upon a course of action before EU retaliatory action was permitted. The United States came under substantial international pressure to abide by the WTO rules. This policy dilemma was intensified by the sensitive exports to be targeted by the EU's 'long' list - including Florida citrus, Louisiana rice, California nuts and North Carolina pyjamas along with a large number of steel products (Crutsinger, 2003). The President was therefore faced with a 'negative sum' domestic policy game that required an irreconcilable choice to be made between two different sets of marginal states.

On 4 December 2003, USTR Robert Zoellick announced that the US steel Safeguards were to be lifted on the grounds that they had been successful, that the domestic economic situation had improved and that their cost now outweighed their benefit (Zoellick, 2003). The United States therefore avoided a major potential trade war and the possible electoral consequences of EU retaliation in favour of adhering to the international rules on trade. In so doing, the President was forced to eschew the unilaterally protectionist sentiments of the domestic steel lobby and possibly risk the marginal steel states of Ohio, Pennsylvania and West Virginia in the 2004 Presidential Election. In the event, George W. Bush won Ohio and West Virginia but not Pennsylvania.

6. Conclusions

The US Emergency Safeguard Measures on steel highlights several important issues relating to the political economy of international trade policy. The Safeguards were the result of interaction between several critical factors. The deteriorating international competitive position of parts of the US steel industry was compounded by increasing import penetration during the 1990s, giving rise to a series of protective trade measures, and the subsequent economic downturn in 2000. Intense pressure for further protection against steel imports arose from an effective lobby comprising steel firms, the industry federation, unions and political representatives in key marginal 'rust-belt' states. The steel Safeguards probably achieved their primary political objective of Republican gains in the key marginal states in the November 2002 mid-term elections and may also have contributed to determining the 2004 Presidential election.

In recent decades, the United States has exhibited a predisposition towards trade intervention in steel. During the second Clinton Administration, this was tempered by the proviso that such intervention was WTO-compatible. The Bush Administration has had no such proviso but its greater protectionist sentiments, partly in the interest of short-term domestic political expediency, have nevertheless ultimately been subject to the same compatibility criterion.

The conduct of the USITC Section 201 investigation also raises the issue of possible domestic political pressure to find evidence of injury. The WTO steel Panel criticised the USITC for its blanket recommendations made on the basis of 'broad brush' product categories rather than a product-by-product methodology. The lack of focus in the USITC investigation suggests excessive haste and political expediency to assuage the demands of the influential US steel constituency, particularly in the light of the extensive subsequent process of product exclusions from the Safeguards. This lends further support to the view that the primary motivation of the US Emergency Safeguard Measures for steel was to appease domestic protectionist sentiments.

As expected, the Safeguards had direct beneficial impacts on prices, employment and profits in the steel industry. The negative effective protection effects on downstream industrial activities were also substantial however, because of steel's importance as an intermediate input and led to price and

profit squeezes, lay-offs, redundancies and firm closures. Empirical studies indicate that the aggregate impact of the Safeguards on US GDP and employment was negative. Further, this was accompanied by a sizeable redistribution of welfare from the private sector in terms of lost revenues, jobs and profits towards the US Government as increased tariff revenue. The Safeguards may almost certainly, although perhaps inadvertently, have increased the cost of the Iraq War to the US taxpayer.

The settlement of the WTO steel dispute in 21 months demonstrates the speed and effectiveness of the new DSU with respect to the previous GATT system. The relatively rapid resolution of the dispute is important in both the specific and broader contexts. The world's two leading traders were pitched against each other in an acrimonious dispute that could possibly have threatened the very existence of the multilateral trade system. It can be argued however, that the DSU has emerged stronger and more credible as a result because the United States opted to back down and accept the primacy of the WTO as the multilateral arbiter of the rules on trade.

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*Robert Read is Senior Lecturer in International Economics, Lancaster University Management School, Lancaster, LA1 4YW, UK (e-mail r.read@lancaster.ac.uk). The author is grateful for helpful comments from Nick Perdikis and Steve Bradley as well as the constructive insights of an anonymous referee. Any errors of interpretation, argument and opinion remain the sole responsibility of the author. A more detailed analysis of the EU-US steel dispute itself and the subsequent WTO case can be found in Read (2005).

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Table 1: USITC Recommended and Actual Protection for Steel

Product Category	USITC Recommendation (%)	Tariff Imposed (%)
<i>Carbon & Alloy Flat Products</i>		
Slab	TRQ+20	TRQ+30
Flat Products ¹	20	30
Tin Mill Products	u	30
<i>Carbon & Alloy Long Products</i>		
Hot-Rolled Bar	20	30
Cold-Finished Bar	20	30
Rebar	10	15
<i>Carbon & Alloy Tubular Products</i>		
Certain Tubular Products	?	15
Carbon Alloy Fittings & Flanges	13	13
<i>Stainless & Tool Steel Products</i>		
Stainless Steel Bar	15	15
Stainless Steel Rod	?	15
Stainless Steel Wire	u	8

Source: Based upon USITC (2001)

u – divided on whether injury caused

? not stated, TRQ – Tariff rate quota

¹ includes, plate, hot-rolled and cold-rolled sheet and coated sheet.