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TOWARDS GREATER COMPETITIVENESS IN THE STEEL INDUSTRY :
THE NEED FOR FURTHER RESTRUCTURING.

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TOWARDS GREATER COMPETITIVENESS IN THE STEEL INDUSTRY: THE NEED
FOR FURTHER RESTRUCTURING

INTRODUCTION

Following the steel boom of 1988-90, the sector is going through a difficult period, necessitating a review of its prospects before the end of 1992, as promised in the General Objectives Steel (GOS) 1992-95.¹⁾

In general, the cyclical downturn in the steel sector triggered off by a general slowing-down in the economy has resulted not only in a stagnation or slight falling-off in production but also in a slump in steel prices. There are various external and internal causes. In a climate of cyclical slowing-down, the weakness of the dollar and the international market (as a result, for example, of the slump on the markets of the countries of Central and Eastern Europe and the former Soviet Union), uncertainty engendered by the complaints lodged by the USA industry and increased imports (in particular from the EFTA countries and the countries of Central and Eastern Europe, following the rapid liberalization of trade since 1991) have increased the pressure of internal oversupply reflecting the difficulty of adjusting supply to a less buoyant market and confirming the continued existence of overcapacity. As a result, the financial situation of most undertakings worsened in 1992, and in some cases there have been major problems since 1991.

In this context, on 2 June 1992 the ECSC Consultative Committee held an extraordinary meeting to discuss the situation in the sector²⁾. It urged the Commission to take steps concerning commercial and market aspects and, in the framework of the ECSC budget, to help improve the competitiveness of the sector and facilitate its restructuring in compliance, of course, with the Aid Code. Likewise, at a meeting on 26 June it emphasized the structural nature of the problems of the sector. On 9 October, many of the chairmen of the Community steel undertakings sent the Commission a memorandum in which they emphasized the seriousness of the situation, committed themselves to embark upon an urgent process of restructuring and rationalization, and requested the Commission to prepare proposals for a package of measures to encourage and promote this difficult process. Also the European Parliament has adopted during its sitting of the 26 October 1992 a resolution underlining its extreme preoccupation with the situation and demanding urgent Community action³⁾.

This communication makes a new overall assessment of the market situation and production structures and sets out a package of flanking measures - which the Commission would be prepared to put in place as quickly as possible in order to encourage and facilitate the urgently needed process of restructuring - accompanying the measures to be taken by the steel undertakings in this process.

1) COM(90)201 final of 7 May 1990.

2) OJ C 161 of 27 June 1992.

3) Doc. PE 161.995.

With regard to the possibility of financial support for restructuring from the ECSC budget, the Commission is, in connection with the preparation of long-term financial perspectives* (for 2002, when the ECSC Treaty expires) considering the twin objective of gradually reducing the ECSC levy and of taking into account of the social and regional needs related to the restructuring of the sector.

1. STEEL MARKET SITUATION AND PROSPECTS

1.1 The development of European Community steel demand

It is generally agreed that the economic growth prospects for the next few years give little hope of an increase in steel consumption in the European Community and that the most likely scenario is one of stagnation at around the present level. The best possible assessment of the present state (1991/92) of the Community market (see Table) still indicates consumption in excess of the forecast in the GOS for 1992, on the basis of an economic scenario more favourable than the actual performance of the Community economy, and even comparable with real consumption in the steel boom years of 1989 and 1990. Consequently, the present market level can be considered to be indicative of the trend in the real demand for steel in the Community in 1995, even in the event of economic recovery at the end of 1993 or early in 1994.

1.2 External trade in steel

The trend in trade in steel has been less favourable than forecast in the last GOS. The annexed table indicates for 1991/92 a trade balance 2.7 million tonnes below the forecast in the GOS-95. This figure breaks down into a deficit of around 2 million tonnes on exports (the main destinations being the USA and the former Soviet Union) and an unexpected increase in imports of around 0.7 million tonnes (the main origins being the countries of Central and Eastern Europe and the EFTA countries).

It is clear that the international context does not suggest any hope of a reversal in this situation by 1995. On the contrary, recent developments would seem to indicate that between now and 1995 the steel industry will be moving towards a Community market fallback scenario.

This worsening of the balance of trade would be the result of international competition, with an increase on the part of the countries of Central and Eastern Europe and the possible risk of an increase of deliveries from the CIS, a loss of outlets in that area and in other recently industrialized areas, and lastly the direct and indirect effects on the Community's trade in steel which would be likely to occur if the American market is closed.

1.3 1995 production scenarios

Taking account of the above factors, the foreseeable production scenarios for 1995 can be based on internal demand in the Community

* Draft communication from the Commission to the Council on the future of the ECSC Treaty: financial activities (SEC(92)1899).

comparable to the present levels (observed between mid-1991 and mid-1992) and a reduced external trade balance in function of two scenarios reflecting the level of fulfillment of the negative trends described under point 1.2.

In both scenarios flat products would be more affected by the worsening in the balance of trade than long products.

1.4 Price situation (1988-92)

The fall in prices is a significant factor in the present difficult situation: following the record price levels of 1989, there was a rapid reduction of 20% on average, and as much as 30% for certain long products, between the end of 1989 and the end of 1991, reaching a floor price in 1992 very close to international prices. Given the current weakness of the dollar and of the international markets it is now very difficult to raise this price level.

1.5 Conclusions

The above analysis clearly indicates that the present demand conditions are structural in nature for the next few years. In the absence of any firm prospects of recovery and with a world market in surplus a recovery in prices is unlikely.

Consequently, undertakings must adopt a strategy based on comparatively inelastic volumes and prices, which means that they must reduce their costs in order to remain competitive.

To achieve this goal, particular attention must be paid to production capacities and the possibilities available to the undertakings to bring their production costs into line with the level of market prices.

2. STRUCTURAL IMPLICATIONS

The imbalance between supply and demand is likely to get even worse in the medium term.

Preliminary analyses based on the two scenarios indicated in 1.3 concerning the MPP declared by undertakings for 1995 and "ideal" utilization rates which also take account of the record utilization of capacities during the boom period 1989/90 when prices reached record levels suggest that there may be uncompetitive overcapacity where utilization rates are below these levels and prices have fallen considerably. This overcapacity is between 19 and 26 million tonnes (11 to 15% of capacity) for hot-rolled products (of which nearly two-thirds for long products), between 3 and 4 million tonnes (5 to 13%) for hot-rolled and coated products and between 31 and 42 million tonnes (16 to 23%) for crude steel.

While admitting that the excess capacities for hot rolled products are those which have a direct incidence on the equilibrium of the market it would now also be appropriate to pay attention to surplus capacity upstream, i.e. for crude steel (where the surplus is in excess of that for hot-rolled products) and, generally speaking, in the liquid phase. In effect it is in the latter installations that are concentrated a large part of the fixed costs of the undertakings as well as the employment, which will accentuate the social consequences of the restructuring and the rationalization needed.

The overcapacity indicated is of a global nature and must be refined by contacts with each undertaking in order to better determine its ideal utilization rates.

This restructuring will have a major impact on employment with job losses according to industry estimate of the order of 50.000.

3. ACTIONS

3.1 Community action framework

The steel industry will in future have to undergo adjustment taking into account conditions on the Community market - i.e. the new conditions of competition which the single market, the European economic area, the Europe agreements with certain countries of Central and Eastern Europe and the accession of new Member States will create - and the reduction in exports to the world market, to the extent that they are marginal and uncompetitive. To ensure that this adjustment takes place in accordance with the principles of Community industrial policy approved by the Council,* the Community must endeavour to ensure first of all:

- the maintenance of an environment favourable to firms and an effective market economy whereby the initiative and responsibility for structural adjustment lie primarily with the economic operators;
- the provision by the Commission of an adequate system of information for firms on the basis of Article 46 of the ECSC Treaty about recent and foreseeable developments in the short and medium term in the steel market and structures;
- the promotion of research and technical innovation, an important element for the maintenance and reinforcement in the medium term of the competitiveness of the Community steel industry;
- the application of the rules of competition and the continued pursuit of a very strict State aid policy; and
- the maintenance of an open approach respectful of fairness in international trade and of international rights and obligations.

When applying these principles, account must be taken in particular of the ECSC Treaty which provides for special tasks for the Community institutions in Articles 3 and 4, for example, and instruments for carrying out these tasks in Articles 46 to 57, 65 and 66 and 71 to 74.

The adjustment of production structures is a process for which direct support may be provided in the form of various Community measures, e.g. private financial arrangements provided for in Article 53(a), investment monitoring provided for in Article 54, by aiding research as provided for in Article 55, and social or regional flanking measures provided for in Article 56 of the ECSC Treaty; the latter which have traditionally been assigned considerable resources from the ECSC budget, could be stepped up to assist the undertakings' restructuring efforts.

3.2 Measures proposed

In agreement with the Communication of the Commission on industrial policy in an open and competitive environment, it is in the first

* COM(90)556 final of 16 November 1990.

place the responsibility of the individual steel undertakings to take decisions on the reduction of capacities in respect of the competition rules. However, the Commission is ready, to facilitate those decisions, to offer a package of measures capable of giving rise to capacity reductions.

3.2.1 Financial incentives for restructuring

These financial incentives can be financed from different public or private sources and can have three main applications:

- partial coverage of the social costs relating to the workers affected by the closure of installations. Community finance of these costs is developed under point 3.2.2;
- partial coverage of the financial costs of the process resulting either from the net asset reduction or contribution to the fixed costs of the undertakings affected by irreversible plant closures, internal rationalization and/or synergy with other undertakings, and the possible winding-up of all their steel activities; these financial costs can only be covered from ECSC sources after unanimous authorization by the Council;
- partial coverage of redevelopment costs (investment, training, etc.) involved in the creation of alternative jobs in the regions most affected by this process.

3.2.2 Social support

The restructuring of the Community Steel Industry will have major consequences for employment which warrant making an effort to extend the measures to protect the workers affected in order to facilitate the adaptation of the labour force to the development of production systems and promote mobility towards new employment.

- Social measures funded under the ECSC budget under article 56 of the ECSC Treaty will be introduced for workers affected by the plans to adapt production structures. They will be geared to extending and stepping up the measures to be implemented to this end. These measures will come under the heading of ECSC intervention covering aid for early retirement, unemployment, internal transfer, external redeployment and training. Additional support must therefore be provided for in the ECSC budget to fund these social measures.

Given the present amount of social aid covered by the ECSC budget - even adjusted to maintain it at its 1988 level¹ - and to enable this action to have a significant impact, this new package would have to entail a substantial increase in the Community contribution; this could cover new types of aid and, taking into account variations in the cost of the measures, would be more intensive for certain typical situations, in particular early retirement and training, where it should help remove obstacles to the efforts of the undertakings, with a view to the internal or external redeployment of workers whose jobs are affected.

¹Year of introduction of the new common intervention system.

On the basis of a preliminary estimate of the jobs affected, the amount necessary for the social measures in question would be around ECU 240 million over three years (1993-95), a period which is regarded as necessary but also sufficient for the urgent implementation of this difficult restructuring process.

This additional financial outlay would make it possible for the Community contribution to the coverage of social costs to be at least doubled, since it could amount to as much as ECU 9 000 per worker in the case of early retirement.

- Similarly, with the present structures, the ESF could optimize and strengthen the programmes more specifically linked to the development of the steel industry.

3.2.3 Competition rules

In the European Community, which is based on the market economy, it is primarily the responsibility of undertakings to judge individually whether and from what point in time their overcapacity or uneconomic activities become economically unsustainable and to make the necessary adjustments.

However, within the steel sector in difficulties economic circumstances do not necessarily guarantee the adjustment of the least profitable overcapacity. In fact the risk of recourse to State aids is always there.

On the basis of this finding, the Commission may, in order to reduce the structural problems of sector, consider the support of an initiative which aims to identify activities suitable for closure on the basis of economic criteria and in particular those with the highest costs. Therefore, consideration should be given to incentives - including Community aids - of which the overall amount and conditions would have to be decided (see Annex).

The Commission could also authorize rationalization agreements or agreements which are similar in their nature and effects if it finds that the conditions of Article 65(2) of the ECSC Treaty are fulfilled.

The Commission is taking steps to accelerate the handling of cases covered by Articles 65 and 66 ECSC.

3.2.4 External measures

The measures proposed for the internal market must be accompanied by an appropriate external package so that the restructuring effort may not be compromised by factors disturbing our trade in this sector. It is thus essential to promote fair international trade and adopt a consistent policy with regard to the steelmaking areas which mainly determine the market conditions, in particular, the countries of Central and Eastern Europe, the CIS and the USA.

a) International trade rules

To this end, since June 1991 the Commission has been negotiating a multilateral agreement on steel which is broadly based on the

discipline imposed within the Community and which aims at a clear definition of aid, the prohibition of aid not covered by the exceptions provided for in the agreement, and the removal of barriers to international trade. It is working for a rapid resumption of these negotiations and an early conclusion of an acceptable MSA.

If circumstances justify it, it may be necessary to resort to instruments of commercial defence (AD/CVD measures, safeguard measures). To this and the Commission services will deploy the resources in order to respond effectively and rapidly to the legitimate demands of the Community industry. The Commission will continue to make the Member States and the steel undertakings more aware of the fact that this presupposes their active cooperation.

In addition, through surveillance measures, it will monitor the development of imports and the conditions under which they take place. It will take all necessary steps to persuade the countries liable to cause commercial problems to refrain from destabilizing trade by charging abnormal prices or increasing exports excessively at a time when the Community industry is confronted with serious difficulties.

(b) Policies vis-à-vis the main steel-producing partners

- Countries of Central and Eastern Europe

The Commission's vigilance will of course apply to the countries of Central and Eastern Europe from which certain exports, because of the weakness of internal demand and the decline of their trade with the CIS which has directed them towards the Community, have already disturbed the Community market. On this subject we would recall that in the month of August the Community has introduced a safeguard clause vis-à-vis Czechoslovakia in order to avoid serious injury to Community producers due to directly competitive products from this country. In addition the agreements concluded with the three Central and Eastern European countries allow specific solutions of a quantitative nature within the ECSC framework to handle problems created by imports. The mandate of the Council for the conclusion of an association agreement with Bulgaria and Romania contains a safeguard clause specific to the ECSC sector (Art. 5). Romania has already accepted such a formula.

However the disturbances in steel trade with the Eastern and Central European countries does not result solely from the growth in volume which is sometimes considerable (exceeding 50%) but above all by deliveries at low prices. In consequence the solutions which may be considered should take account of this factor.

Taking into account our relations with these countries, the Commission could, without excluding the possibility of using existing instruments, seek in priority negotiated solutions which could have an effect, for the products involved, on their price level which is the principal cause of the disturbances.

In general and in normal circumstances the Commission follows closely with these countries the development of trade and that more particularly in the existing bodies, such as the contact groups or mixed committees.

With regard to the countries of Central and Eastern Europe which have concluded association agreements with the Community, the Commission will act under Article 8 of the ECSC Protocols, whereby it can apply competition rules and verify the conditions regarding the restructuring of undertakings. Where appropriate, it will continue, in conjunction with other institutions concerned, to help the steel undertakings of these countries in the difficult process of transition towards a market economy and of achieving balanced and commercially viable production. At the appropriate time, it will apply this policy to the CIS countries.

The Commission will continue with its cooperation activities vis-à-vis the countries of Central and Eastern Europe initiated with the industry with a view to progressively reducing the sources of commercial conflict and helping the steel undertakings in those countries in the difficult process of transition towards a market economy, in particular in the area of training and technical assistance in business management.

- CIS

With regard to the CIS countries, number one producer of steel in the world, but whose internal demand has collapsed, the Commission, in taking into account the current situation of the Community steel industry and the potential effect of a liberalisation of trade with these countries, can only propose for 1993 the fixation of a Community quota replacing the existing five national quotas. It will propose to the CIS Republics a steel cooperation programme which is similar to that offered to the countries of Central and Eastern Europe in the context of the steel contact group recently set up with Russia and which will also be offered to the other Republics with a significant level of steel production (Ukraine and Kazakhstan, in particular).

- USA

For the Commission the dispute with the USA, which puts into question 2 million tonnes of steel exports and a thousand million dollars, has a certain political dimension and a solution must necessarily be found in the political domain. In the meantime the Commission has made two interventions in the Anti-Dumping Committee of GATT putting on guard the USA in relation to the respect of the conformity of their internal procedures with the GATT rules. It will continue to watch over the correct application of the AD/CVD complaints filed by the American steel industry. In so doing the Commission is following the recommendation of the Council.

In fact the Council has, on the proposition of the Commission and the Presidency, adopted on the 6 October 1992 a recommendation on this subject, which will be applied with diligence and rigour.

ANNEX: PROCEDURE TO IDENTIFY CAPACITIES FOR CLOSURE.

Uneconomic structural overcapacity exists when over a long period, all the undertakings concerned suffer from an important reduction in their utilisation rates, a fall in the sales revenue from their products and, as a result, make substantial losses, and when it does not appear, on the basis of the information available, that these losses will be reduced permanently in the medium term. An improvement in the profitability of the sector needs, in particular, and among other measures a reduction of capacity. This appears to be the present situation of the Community steel industry.

The Commission could envisage authorising an initiative designed to lead to a reduction of capacity by the identification of the activities eligible for closure:

- participation of the steel companies would be voluntary.
- the Commission and the industry should agree on an estimate of the structural overcapacity which might be closed. It might be appropriate to identify the extent of structural overcapacity separately for certain kinds of steel products.
- a person would be appointed by the Commission to:
 - a. receive the proposals for closure of every company or group of companies which want to participate in this process;
 - b. report to the Commission.
- the Commission will evaluate the report and will agree with each company concerned on the conditions of and timetable for closures.
- when appropriate commitments have been given by the owners that the operations in question will be permanently closed by a given date, the Commission would announce the agreed closures.
- assistance from Community and/or private funds would be provided for closures.
- with the exception of social aid covered by the ECSC Treaty and the Steel Aids Code, no assistance should be paid for closures carried out in the context of authorisation of state aids, if this implies that the same closure would be counted twice as counterpart for financial assistance;
- an appropriate reduced level of assistance should be given for the closure of plant that has not been operated recently.
- companies that did not close their operations by the agreed date would be required to repay immediately any assistance they had received.

Any parallel agreements between producers, particularly those:

- setting production or delivery quotas
 - fixing prices
 - involving the exchange of information on individual companies which could influence the commercial behaviour of competitors (1)
- would be contrary to Article 65.1.

As a result of such closures, some of the companies concerned might need to make new links with suppliers or other competitors. Such agreements cannot be foreseen precisely in advance, and would have to be considered by the Commission in accordance with its usual practice under the competition rules.

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- (1) Individual exchanges of information which are not liable to influence the behaviour of the undertakings in market since they will have only an historical interest may be permitted. Only a case by case examination in respect of the nature of the information in question, the degree of aggregation and the market concerned would however permit an appreciation of the possible restraint of competition. It follows from the preceding text that one would not a priori exclude individual exchanges of information between undertakings when those would not be liable to influence their competitive behaviour and this absence of influence is principally a function of the nature of the information, its status and the market concerned.

Table

STEEL CONSUMPTION AND EXTERNAL TRADE BALANCE 1991/ 1992

million tonnes

| PRODUCT | CONSUMPTION | | EXTERNAL BALANCE | |
|--|----------------------|-----------------------|------------------|------------|
| | GOS 92 ¹⁾ | 1991-92 ²⁾ | GOS 92 | 1991/92 2) |
| LIQUID STEEL FOR CASTING INGOTS AND SEMIS | 12,7 | 12,7 | 1,2 | 0,9 |
| HEAVY SECTIONS | 7,1 | 7,7 | 1,9 | 1,7 |
| LIGHT SECTIONS | 20,9 | 21,2 | 1,1 | 1,3 |
| WIRE ROD | 12,6 | 13,5 | 0,6 | 0,4 |
| LONG PRODUCTS | 40,6 | 42,4 | 3,6 | 3,4 |
| STRIP AND SHEET | 43,4 | 47,3 | 5,8 | 4,2 |
| COATED SHEET | 14,0 | 15,9 | 2,4 | 1,8 |
| FLAT PRODUCTS | 57,4 | 63,2 | 8,2 | 6,0 |
| TOTAL | 110,7 | 118,3 | 13,0 | 10,3 |

1) Excluding the former GDR the consumption of which amounts to 1.8 million tonnes of long products and 1.7 million tonnes of flat products.

2) 1991-92 = 2nd half of 1991 - 1st half of 1992.