

CHINESE STEEL OVERCAPACITY

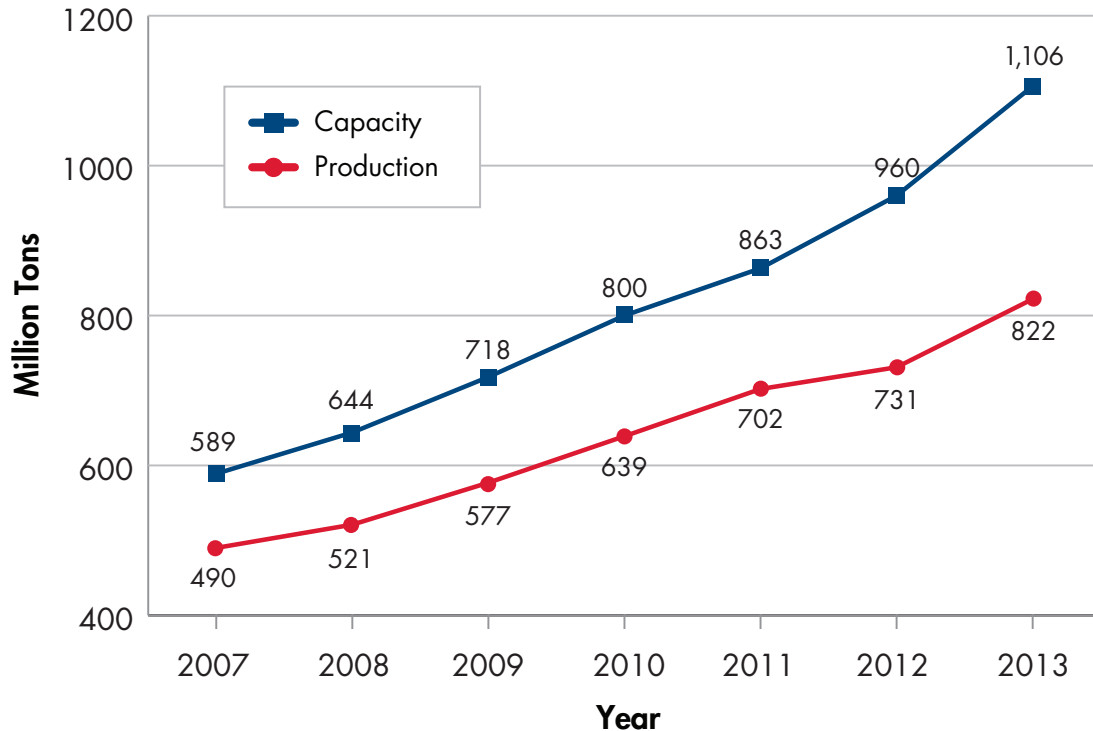
A Legacy of Broken Promises

The American steel industry and the hundreds of thousands of jobs it supports are facing an unprecedented threat from excess global capacity. This critical issue is often overlooked as a driver of import growth into the United States.

Each year, the world's steel producers are making hundreds of millions of tons beyond what global demand suggests would be the appropriate amount of production. This practice is commonly referred to as "overcapacity," and in the steel industry the term has become synonymous with China, who in 2014 accounted for over 400 million tons of global excess capacity in steel.¹ Driven by significant government intervention, subsidies, and currency manipulation, China's steel industry has grown at an extraordinary rate over the past 15 years.² This growth has taken place at a rate far faster than domestic and international demand would dictate. As a result, China's steel industry is actively and deliberately flooding the international market with over a hundred million tons of steel each year. Steel plants in the United States and around the world are being forced to close, laying off thousands of workers in the face of China's torrent of excess steel.³

From 2000 to 2014, China's steelmaking capacity⁴ and production⁵ increased dramatically. (See Figure 1)⁶ Over that time, China went from having roughly the same annual steelmaking capacity as the United States to 1.2 billion tons of capacity, or 10 times that of the U.S.⁷ In fact, China accounted for more than 75 percent of global steelmaking capacity growth, and last year China's steelmaking capacity exceeded that of the United States, European Union, Japan, and Russia combined, according to the U.S. Trade Representative.⁸ This growth has been far beyond what Chinese domestic and international demand requires, and the Chinese government has been pledging to curb this rampant overcapacity since 2007. Despite these promises, however, Chinese steelmaking overcapacity continues to grow, and as a result the American steel industry announced 12,000 layoffs in just the last year.⁹

Figure 1. Chinese Steelmaking Capacity and Production, 2001-2014



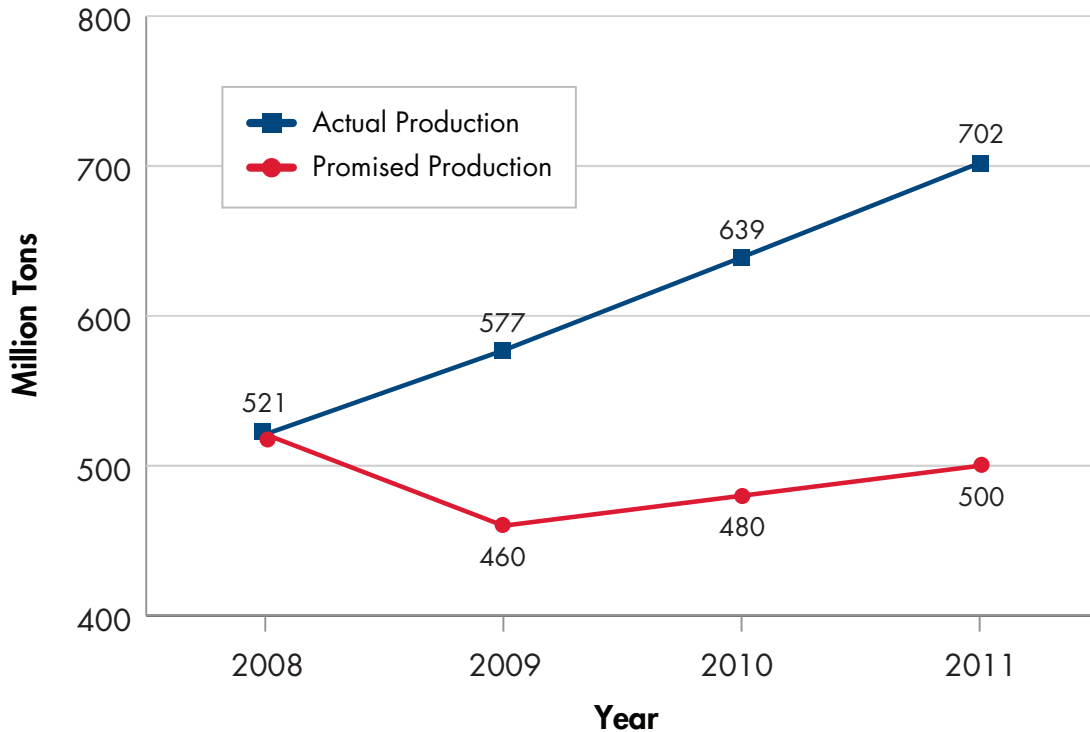
Source: German Steel Federation and World Steel Association. See: Note 6

Broken Promise #1: The Steel Industry Revitalization Plan, 2009

In 2009, the Chinese government released its Steel Industry Revitalization Plan (SIRP) with the goal of modernizing steel production and eliminating excess capacity. This plan pledged to cut Chinese steel output in 2009 to 460 million tons, down from 521 million tons in 2008.¹⁰ From that lower baseline, production would slowly rise to 500 million tons in 2011.¹¹ Instead of that promised reduction, Chinese steel production in 2009 increased to 577 million, and in 2011 surpassed 700 million tons.¹² (See Figure 2)¹³

The 2009 SIRP and the actual behavior of the Chinese government and steel industry is a pattern that continues to be repeated. Promises are made that purport to bring the Chinese industry into line with global market trends, then those promises are immediately broken and the massive overcapacity increases and overproduction continues unabated.

Figure 2. Actual vs. Promised Chinese Steel Production Under SIRP, 2008-2011



Source: : Congressional Research Service and World Steel Association. See Note 13.

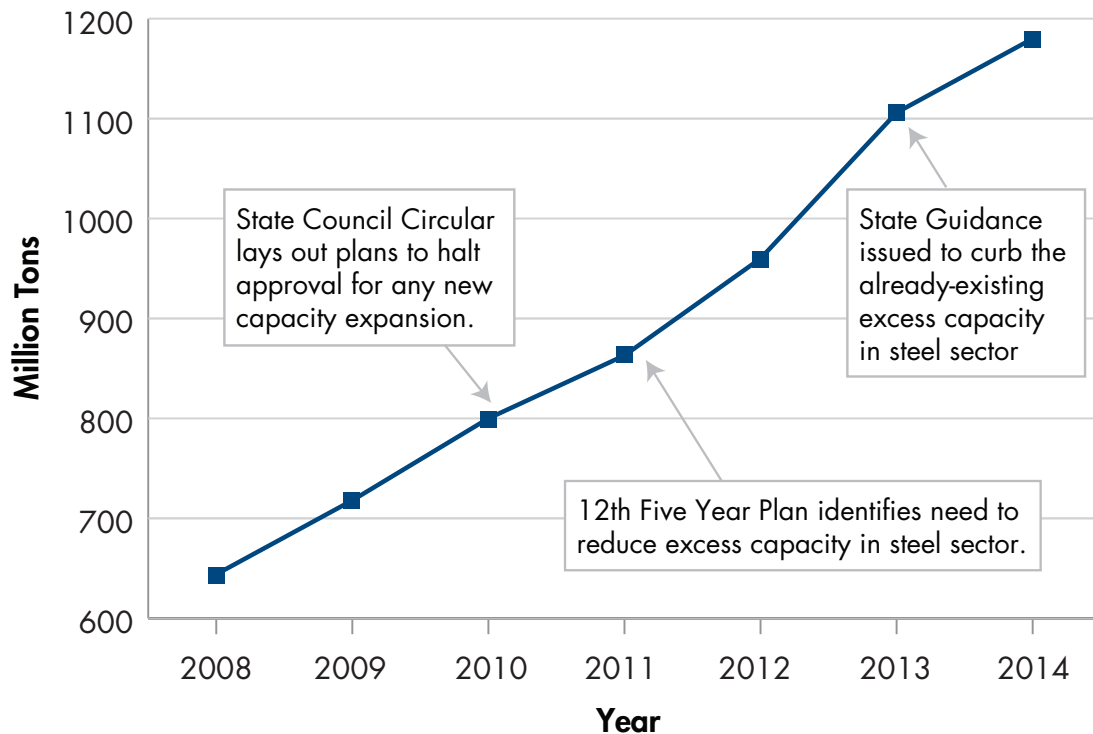
Broken Promise #2: The State Council Circular, 2010

Even as China was in the midst of breaking the promises on production made in the 2009 SIRP, it was making more promises with regard to capacity. In 2010, China's State Council issued a circular in which it laid out plans to halt approval for any new capacity expansion projects in the steel sector.¹⁴ At the time, China's existing capacity was approximately 800 million tons.¹⁵ By 2011, despite this plan to prevent the development of any more steelmaking capacity, an additional 60 million tons per year of capacity had been brought online.¹⁶

Broken Promise #3: The 12th Five Year Plan, 2011

A year after the State Council Circular laid out its plan to halt approval of new capacity, and the 60 million tons of new capacity that nevertheless followed, the Chinese government released the 12th Five Year Plan.¹⁷ The 2011 Plan, which laid out a roadmap of priorities for the Chinese Communist Party over the next five years, identified the need to suppress and channel off excess capacity in the steel and other sectors. Despite this call for reducing steelmaking capacity, another additional 96 million tons of capacity had been brought online by 2012.¹⁸

Figure 3. Chinese Steelmaking Capacity and Selected Government Actions, 2008-2014



Source: German Steel Federation and World Steel Association. See: Note 6

Broken Promise #4: State Council Guidance on Excess Capacity, October, 2013

In October 2013, Beijing once again identified overcapacity in steel as a serious problem and issued new guidance to curb the excess capacity of steel and four other sectors.¹⁹ This guidance instructed the steel industry to effectively absorb the already-existing excess steel by both boosting domestic demand and increasing exports. Despite this call to employ the existing overcapacity, yet another additional 70 million tons of capacity had been brought online by 2014.²⁰

The Next Promises To Be Broken:

The Strategic and Economic Dialogue, 2014; and the Joint Commission on Commerce and Trade, 2015

The Sixth Meeting of the U.S.-China Strategic and Economic Dialogue (S&ED) took place in 2014 amidst China's capacity additions. In this negotiation, excess production was identified as a key to fostering an economy in which resource allocation is market-driven. China once again pledged to establish "mechanisms that strictly

prevent the expansion of crude steelmaking capacity and that are designed to achieve, over the next five years, major progress in addressing excess production capacity in the steel sector.²¹ One year later, at the 26th meeting of the U.S.-China Joint Commission on Commerce and Trade, U.S. and Chinese authorities announced that discussions would be held the following year to review what progress has been made in addressing steel overcapacity since the 2014 S&ED agreements.²²

As U.S. negotiators prepare for those discussions this spring, they must consider the Chinese government's legacy of repeated broken promises and false statements regarding overcapacity.

The Current Situation

As discussed above, Beijing has been issuing plans, writing memoranda and guidance, and making promises in bilateral negotiations to address its overcapacity in the steelmaking sector. Despite these promises, Chinese overcapacity continues to increase. The American Iron and Steel Institute found in 2014 that global steel production overcapacity was more than 700 million tons.²³ The majority of that amount – 425 million tons – is specifically Chinese overcapacity.²⁴

In assessing the state of both the American and the global steel industries, it is important to understand that production and capacity are linked, and that massive overcapacity of the sort that exists today drives overproduction, which in turn unfairly and artificially puts pressure on both American and other foreign steel companies, with increasingly disastrous results. The American steel industry is one of the most efficient in the world, often producing a ton of finished steel in under one man-hour.²⁵ But even with this world-class performance, plants are closing in the United States as a direct result of this overcapacity and the overproduction that comes with it, at the cost of thousands of American steelmaking jobs.²⁶

China's motives in pursuing this buildup of overcapacity are clear and obvious. Chinese officials have long admitted that the nation is not especially well-suited to steel production. In fact, in 2009, the Chinese Academy of Sciences reported that China lacks the natural resources and environmental capacity to be the world's steel supplier.²⁷ Despite this, China continues to overbuild its steel industry as a result of a state-run economy that has long considered steel a "strategic industry" and fostered industrial policies designed to help the industry grow – whether the resources, environmental capacity, and market conditions supported growth or not.²⁸

Additionally, China's overcapacity was built and continues to be built with an eye toward social stability rather than long-term market viability.²⁹ Steel mill jobs and the economic stability they provide to communities have been and continue to be a driving force in keeping unneeded Chinese production online. When the 2008 global recession caused global demand for steel to slow, rather than cutting back on steel production like it promised to in the 2009 SIRP, Beijing poured state capital into the steel industry in hopes of preserving industry employment and, therefore, social stability. This stability is extremely fragile. Citing fears of instability and a convoluted provincial system of small- and medium-sized steel producers, Beijing has fostered the growth of overcapacity in the Chinese steel sector.³⁰

Moving Forward

Even before this year's discussions on the commitments made during the 2014 S&ED commence, China has continued making promises with regard to steel overcapacity. In 2015, China's Ministry of Industry and Information Technology announced a new effort to cut capacity and consolidate its steel industry over the next two years.³¹ And in February the Chinese Communist Party's State Council – the same governing body that “promised” in 2010 to halt approval for any new capacity expansion – announced it would eliminate between 100 million and 150 million tons of annual crude steel capacity by 2020.³²

This relatively small step might help improve the situation in which the American and global steel industry finds itself, drowning under a flood of Chinese steel exports driven by overcapacity. However, after almost a decade of inaction, China's latest promises – even if enacted – would continue to saddle American workers with a staggering 300 million tons of Chinese overcapacity. Unfortunately, if one thing has been made clear from China's years and years of broken promises and obvious falsehoods regarding overcapacity, the international community simply can no longer trust China to actually address this problem.

The Chinese government views this overcapacity as a strategic interest and a driver of domestic social stability. It simply will not give up this advantage on its own, no matter how often it makes and breaks promises to do so.

If China will not act on its own, America must. It is incumbent on the U.S. government to address the problem, if the American steel industry – which is every bit as vital to America's economy as it is to China's – is to survive. It is time for comprehensive action.

Endnotes

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- 12 World Steel Association, *supra note 5*.
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- 15 German Steel Federation, *supra note 4*.
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