A NAFTA Industry Perspective on the Impact of SOEs on the Global Steel Market

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American Iron and Steel Institute
CSPA ACPA Canadian Steel Producers Association L'Association canadienne des producteurs d'acier
CPTI The Committee On Pipe And Tube Imports
CANACERO
SSINA Specialty Steel Industry of North America
SMA Steel Manufacturers Association

Overview

- State-owned enterprises ("SOEs") represent a growing challenge to fair competition in the global steel industry
- SOEs are a primary means by which governments can exercise ownership and control over strategic sectors, including steel
- SOEs often do not operate based on market principles and therefore introduce market-distorting behavior and other imbalances in the global steel market
- SOEs also pose challenges to normal investment and commercial decision-making in the upstream raw materials market, as governments are increasingly using SOEs to secure access to natural resources

State Capitalism and the Rise of SOEs

- After decades of retreat, the degree of state involvement in global economic activity is growing
- Many governments are increasingly pursuing ownership, control, and direction of key industries through SOEs
  - SOEs account for 80% of stock market capitalization in China, 62% in Russia, 38% in Brazil, 30% in Indonesia, and 20% in India
  - SOEs in many of these countries are dominant in mining, energy, steel, logistics, and other sectors critical to manufacturing and raw materials
- SOE investment abroad is also on the rise, increasing the likelihood of potential harm to market-based companies worldwide
  - According to *The Economist*, four-fifths of global foreign direct investment comes from state-owned companies

The Impact of SOEs on the Global Steel Industry

- Governments in a number of countries are asserting ownership and control over steel companies
- The rise of steel-producing SOEs poses significant challenges in the global steel market, including market-distorting behavior and other imbalances
- SOEs often receive substantial subsidies and other government assistance, which bestow an unfair competitive advantage on SOEs in their worldwide operations
  - These benefits artificially lower SOEs' costs and enhance their ability to sell at lower prices
  - SOEs are often able to sustain losses for longer periods of time and do not have to earn a commercial rate of return

The Impact of SOEs on the Global Steel Industry

- As a result, SOEs have less incentive to make production, pricing, or other decisions based on market principles. In fact, SOEs often pursue policies based on national interest (e.g., production, employment), not profitability

- In these ways, state ownership of steel producers allows for expansion that is not based on market forces, thereby distorting investment, production, and operations in the global steel market
  - *"The big state-owned [Chinese] steel mills are motivated not so much to seek profits but to seek government support. There is actually no mechanism to put them out of business, no sense of the survival of the fittest, and that is probably the biggest problem facing the industry."* – Jiang Feitao, Steel Policy Researcher at the Chinese Academy of Social Sciences
- Preferential treatment of SOEs essentially forces market-based steel companies to compete in global markets against foreign governments, with all of their resources and power

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The Impact of SOEs on the Raw Materials Trade

- SOEs are purchasing stakes in raw material projects around the world as part of a concerted strategy to secure access to critical inputs
- Subsidies and other benefits bestowed on SOEs put private companies at a significant disadvantage in gaining access to raw materials
- Other market-distorting effects that provide an unfair advantage to domestic downstream industries include:
  - Lower prices and increased access for domestic industries
  - Higher prices and increased price volatility for the rest of the world
  - Reduction in the global supply of raw materials, including the potential for shortages
- In times of supply shortages, SOEs may supply domestic consumers instead of customers in other countries, despite the willingness of the latter to pay market prices

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Addressing the Challenges Posed by SOEs

- Governments should increase efforts to address the market-distorting effects of SOEs and ensure that the global steel market remains free from government interference
- Governments should ensure that SOEs:
  - Act in a manner consistent with commercial considerations (e.g., SOEs should not receive subsidies or other benefits not available on commercial terms)
  - Do not receive preferential legal or regulatory treatment that distorts commercial conditions
  - Adhere to fair pricing practices
  - Adhere to sound corporate governance standards and observe a high degree of transparency