

China's subsidies threaten 'harsh winter' for global steel industry

Steel Market Update

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Last week, the Chair of China's Baowu Steel Group predicted a "harsh winter" for the Chinese industry, as it faces a structural economic slowdown and a property market crisis. As steel industries elsewhere know all too well, China's "harsh winters" have an unfortunate tendency to blow back on them.

The winds have been picking up for more than a year already. According to the U.S. Commerce Department, China's 2023 steel exports increased by 39% compared to 2022 volumes. In 2024, exports are on pace to exceed 100 million tons. This is causing flashbacks to the mid-2010s, when Chinese steel exports hit a record of 110 million metric tons and threw the global industry into crisis.

Harsh steel industry winters originating in China are no longer a question of "if," but of "when." Their periodic emergence is not the unexpected result of sudden market downturns. It is the inevitable consequence of decades of failed industrial policy and generous government financial support driving overcapacity that China's planners are unwilling or unable to confront.

China's official statements of concern regarding "blind investment" and overcapacity in the steel industry go back to at least 2003. Repeated attempts since then to address overcapacity have harbored illusions that the solution lies with government-directed consolidation and government-funded facility upgrades. In practice, these policies are counterproductive vectors for ongoing subsidization

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that sustains and even expands all but the most decrepit, non-operational facilities through financial bailouts and other government support.

Wiley has closely tracked these policies and the market distortions they have created. In a series of previous reports dating back more than 15 years, we have documented the ways in which China's pursuit of subsidized self-sufficiency and market dominance in steel and other sectors has affected U.S. producers.

Our most recent analysis, *Shell Game: Case Studies in Chinese Steel Subsidies*, will be issued in the coming days. It examines a selection of oil country tubular goods (OCTG) producers and confirms that the same pattern continues today. If anything, the Chinese government has only expanded the scope of intervention and subsidization.

First, it continues to rely on state-directed mergers and acquisitions in pursuit of industry consolidation and capacity reductions. Far from reducing capacity, these transactions often operate as massive financial bailout schemes that sustain uncompetitive capacity and create mammoth conglomerates that are insulated from domestic competition so that they can more effectively target global markets.

Second, policies with stated environmental objectives continue to operate as counterproductive vectors for additional subsidization that do little but move capacity from one place to another. In the process, these state-supported relocations expand capacity and facilitate export orientation by concentrating it logistically optimized regions like coastal ports.

Third, industrial policy support that has historically favored large state-owned enterprises has been expanded to cover even the smaller, non-state firms that were in theory to spur more market-oriented competition and outcomes in the industry. These policies call on the state to dramatically increase the scope of grants, subsidized financing, and other support throughout the steel industry.

We examined these policies through recent examples from the OCTG sector, but this is just a snapshot of what is happening throughout the steel industry. As long as this continues, China's overcapacity is here to stay. This will remain the case unless and until policymakers elsewhere accept the hard truth that China's ability to access demand in their markets only enables the policies that are the root cause of the problem. As long as foreign markets, whether for direct steel imports or imports of major steel-consuming downstream goods, can be flooded by subsidized Chinese steel, harsh winters in China will become an ice age for the rest of the global industry.

It may be difficult and complicated in the short-term, but concerted action among like-minded partners to deny the Chinese steel industry any outlets may be the only way to end this pattern. Steel producers around the world are ringing alarm bells, from North America to South America, from Europe to Southeast Asia. Given globalized markets and interconnected supply chains, countries acting individually to respond to immediate crises on an ad hoc basis remains necessary, including by updating and strengthening trade remedies laws, but more will be needed.

China's steel industry also remains overwhelmingly composed of high-emission blast furnaces and still relies largely on coal fired electricity. Nearly every ton of steel exported from China into markets with lower-emission industries displaces a ton of steel made by less carbon-intensive processes. Downsizing the Chinese steel industry is therefore also perhaps the most effective and efficient way to dramatically reduce global steel industry CO₂ emissions.

For the sake of both the global economy and the global climate, China will need to shut down around 30% of its steel industry, at least according to some of its own companies' estimates. But as long China's policymakers have outlets to force those painful decisions onto other countries, we can expect that they will continue to do so, just like they have in the past.