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United States - China Steel Dialogue
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Mr. Chairman, and other members of the Congressional Steel Caucus, I welcome this opportunity to discuss our views on the steel dialogue with China and related issues.

First, I want to emphasize that we at the Department of Commerce believe it is important to engage with other countries and to use the tools at our disposal to ensure a level playing field for U.S. companies across all sectors, including steel.

China is a particularly large economy and one that has not yet completed its transition to a market economy. For this reason it poses particularly complex challenges. It was with this in mind that Commerce and USTR proposed the establishment of the steel dialogue under the U.S.-China Joint Commission on Commerce and Trade. We were pleased that the Chinese accepted this proposal. The first session of the dialogue was held on March 24, 2006, in Beijing.

Before talking in further detail about the steel dialogue, I want to offer a few comments on several additional topics, including the status of our steel industry today and on China's role in the global steel market.

State of the Steel Industry

Conditions in the U.S. steel market are favorable now, owing to strong demand from the nonresidential construction and metalworking industries, the underlying strength of the economy, tight domestic supply, and an end to the inventory liquidation that took place during much of last year. During the first quarter of 2006, apparent consumption of steel mill products jumped 10 percent compared to the same period of last year. Crude steel production and domestic shipments rose 2.4 percent and 3.7 percent, respectively, over the same period.

In this positive environment, steelmakers have been able to boost prices for a number of key products. After falling sharply from records reached during the third quarter of 2004, sheet products began to recover during the fall of 2005 and have continued to increase. The price of bellwether hot-rolled sheet rose by 32 percent between August 2005 and May 2006 and, according to reports in the press, additional price increases of up to 10 percent are being booked for July. These prices are still well short of the $756 per net ton ($833 per metric ton) peak of two years ago. Some analysts believe that prices will continue to rise through the second and third quarters of 2006 due to the strength of the market.

As a result of these positive conditions, a number of companies reported strong, and in some cases, record earnings in the first quarter of 2006, following upon solid earnings in

2005. During the first quarter of 2006, net income for seven representative steelmakers increased 53 percent from the previous quarter to $814 million.

It is noteworthy that market conditions are also improving worldwide, including such key markets such as China, the European Union, and Japan. World export prices have been moving up since November and are expected to continue to rise at least for the next several months. These increases have reduced the spread between U.S. domestic and foreign prices for key products.

The principal downside for steel producers among all these positive market factors are the prices for key steel inputs, which have been rising sharply, reflecting soaring production worldwide, especially in China. In 2005, the three leading international iron ore companies were able to obtain record increases of about 70 percent in the price of iron fines, a key raw material used in integrated steelmaking. These companies have apparently obtained an additional 19 percent increase in the price of iron ore fines this year.

However, more than half of U.S. steel production relies on scrap, and the price of scrap also is rising. Analysts suggest that prices for the benchmark grade of scrap (No.1 heavy melt) and other grades could reach record levels in the next several months.

The price for another key input to production, coke (as measured by the export price for China, the world's largest producer and exporter of coke), by contrast, remain well below last year's levels. The current price is estimated to be about $140 per ton, versus $240 per ton a year ago. The Administration exerted considerable pressure on the Government of China to amend its export controls on coke, and this reduction reflects a decision by the Chinese government to ban the sale of the licenses required for exports that had driven up coke prices and to increase its export quota.

The Importance of China in the Global Steel Market

China's steel industry, the world's largest, has grown dramatically and is expected to continue to do so during the remainder of this decade. In 2005, Chinese steel production reached 349 million metric tons, an increase of 25 percent over 2004. China's steel production that year amounted to 31 percent of the world total, up from just 15 percent in 2000. Moreover, production is expected to continue to grow albeit at a slower rate. The Chinese Iron and Steel Association (CISA) projects a nearly 15 percent increase to 400 million tons in 2006. Through April, production totaled 126 million tons or 379 million tons annualized.

Real consumption of steel mill products in China has also soared. From 120 million tons in 2000, it jumped to 335 million tons by 2005. Earlier this month, CISA revised its forecast for this year upward to 397 million tons as GDP and fixed asset investment growth topped previous forecasts. Construction accounts for over half of consumption; machinery and motor vehicles, the next largest markets, are less than 20 percent.

China's emergence as the world's dominant steel producer clearly has profound implications for steelmakers elsewhere, especially since the growth in capacity is apparently outpacing domestic demand. According to CISA data, crude steelmaking capacity totaled 414 million tons in 2005, vastly exceeding production of 349 million tons and the even lower consumption. Last fall, China's State Council Development Research Center predicted that excess capacity could total 116 million tons this year, a figure greater than the entire production of the United States. This forecast was challenged by CISA, but experts elsewhere in the Chinese government and in industry recognize that substantial excess capacity exists.

A key development and concern to us is China's recent shift from being a major net importer to a net exporter, resulting in a swing in trade of nearly 35 million (metric) tons since 2003. Imports peaked at 43 million tons in 2003 and declined to 27 million tons in 2005 even as exports rose from 8 million tons to 26 million tons. For the first four months of 2006, China was a net exporter of 4.3 million tons of all steel products. CISA, which earlier this year had forecast that trade would be roughly in balance, cautioned that factors, such as the reduction of VAT rebates, might reduce exports later in the year.

U.S. Trade Flow Update

Solid demand and higher prices in the United States are encouraging an increase in imports. During the first quarter of 2006, total imports rose 34.8 percent compared to the same period of 2005 to 11.2 million net tons (10.2 million metric tons). Imports' share of the market (excluding semifinished imports) for the first quarter rose from 21.1 percent to 25.4 percent. The peak annual share was 27.2 percent in 1998.

Imports from China jumped 58.3 percent during the first quarter compared to year ago levels. As a result, its share of total imports increased from 7.2 percent to 8.5 percent during this period. Between 2000 and 2004, China's share of imports ranged from 2.5 percent to 5.2 percent. By product, the most significant increases this year have been for galvanized sheet, standard pipe, and wire rod.

It is evident that the dynamics of the steel industry globally, in ever greater amounts, are revolving around China. Therefore, we believe that is necessary to engage China and other prominent actors in the global steel market in an effort to create market transparency that will allow free market economics to direct the growth of the industry.

JCCT Steel Dialogue

As noted above, we currently are enjoying relatively positive trends in the U.S. steel industry. However, as I have also noted, China's rapid and enormous growth of steel production poses a significant challenge to the U.S. and global steel industries. With this in mind, we intend in the steel dialogue with China to discuss the full range of issues which could have a bearing on the development of the steel industries in our two countries and globally. These topics will include issues of subsidies, other forms of government intervention in the market, current plans in additional investment in this sector, and issues related to raw materials and energy efficiency.

One important part of this effort will be involvement of the U.S. and Chinese steel industry representatives in the dialogue.

Our steel industry has been very supportive of the objectives of the China steel dialogue and would like to have a participatory role. They have established their own outreach to China, including frequent travel there, and are becoming very knowledgeable about its industry. We are meeting regularly with the private sector to discuss the dialogue, either formally through our Steel Industry Trade Advisory Committee (ITAC) or more informally with a full range of stakeholders, including labor unions, distributors, and steel consumers.

While we are carefully monitoring developments in China, our industry is also keeping us informed about significant developments that may be a concern to them.

At the next steel dialogue meeting, which we hope will take place in late Summer, we intend to have active participation from our steelmakers. We have begun to develop an agenda for the next meeting and we will consult closely with U.S. producers and other stakeholders before submitting our proposal to China. We also hope that this session of the dialogue will include visits to some Chinese producers, to enable the U.S. government and industry to get a more detailed first-hand understanding of key issues.

The steel dialogue is intended to allow us and our Chinese counterparts to better understand the range of issues that affect current and future trends in the steel sector. That said, it is also the case that as we get a clearer picture of problems arising from Chinese policies or actions, we will seek solutions, both by working cooperatively with China where possible and, as necessary, by using the full range of trade tools at our disposal.

Asia-Pacific Partnership on Clean Development and Climate

ITA also is engaged with China and its steel industry in other fora, including the Asia-Pacific Partnership on Clean Development and Climate (APP), a Presidential initiative. This partnership, which was launched in January 2006, will create a voluntary framework for international cooperation to facilitate the development, diffusion, deployment, and transfer of cleaner, more efficient technologies and practices among the six partner countries through concrete and substantial cooperation. In addition to the United States, partners are China, India, Japan, South Korea, and Australia. Our industry is actively engaged with the Departments of Commerce and Energy in carrying out the work of this action plan.

The objective is to promote sustainable economic growth and energy security while enabling significant reduction in greenhouse gases. It also can be expected that through efforts to benchmark current conditions and practices among the partners, a greater understanding of these industries will be obtained. Furthermore, it should assist in leveling the environmental playing field among partners.

A key provision of the APP is the establishment of eight public-private sector task forces covering important energy-producing and consuming sectors, including steel. The steel industry is a key element of any domestic or international greenhouse gas emissions or related pollution abatement activity since it is among the largest energy consumers manufacturing. Also, steel is a key industry in all six countries and together their industries account for over 50 percent of total world steel production.

The Steel Task Force, co-chaired by Japan and India, approved a results-oriented action plan at a conference in Berkeley on April 18-21. The Task Force will first identify effective technologies that reduce energy consumption and greenhouse gas emissions and develop indicators of energy efficiency and recycling. The Task Force will then conduct research and diagnosis of plants for energy saving and in "field tests" promote the introduction of cost-effective existing and emerging technologies that reduce energy consumption and protect the environment. The field tests will likely take place in China or India.

Conclusion

ITA has a long history of working with the U.S. steel industry, and, over the years, has engaged in numerous activities designed to assist the U.S. industry in overcoming the impediments to the unencumbered functioning of free markets globally. We seek a level playing field in ensuring the competitiveness of the industry in all aspects of competition within the marketplace, be it trade, regulatory, environmental, or any future issue yet to be unveiled. We look forward to continuing our working relationship with the industry, and together addressing the challenges confronting it.

Thank you.