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G20, Trade and Steel: Shaping New Alignments

The Group of Twenty (G20) Summit at Hangzhou took place in September 2016 in the backdrop of adverse prospects for global trade given its sluggish growth and the rising protectionist sentiments. While committing to tackling protectionism, the summit expressed concerns on the overcapacity in global steel production and state- support that was distorting global markets. It established a global mechanism for monitoring overcapacity in world steel production. This marked the success of a rare strategic alignment between some major developed- and developing-country members of the G20, notably the United States, Europe and India, in tackling China's command over the global steel industry. It also marked a shift in the discourse on the role of market-distorting state-support in global trade – with China, rather than industrial nations, now being accused of resorting to such support in greater measure.

Amitendu Palit[1]

Global Trade: Sluggish Growth, Rising Protectionism and G20

The G20 Summit at Hangzhou in early-September 2016 was preoccupied with concerns over global trade. Global trade growth has been sluggish for some time now and is arguably a major factor behind global economic recovery not assuming robust

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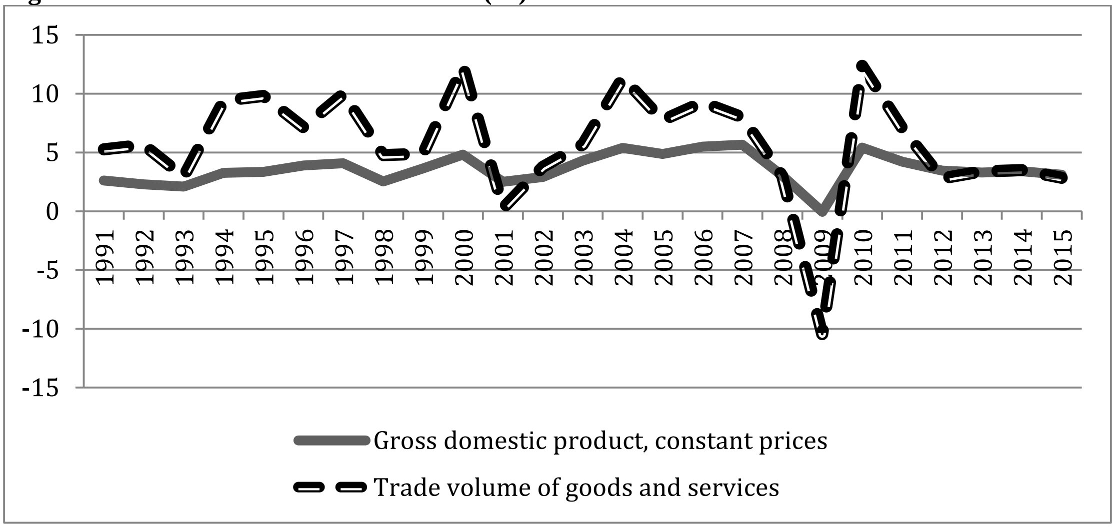
proportions. During a period of 25 years since 1991, global trade growth has mostly outpaced global GDP growth (Figure 1). But it has begun declining since 2011 and has been almost on par with global GDP growth. During 2015, trade growth (2.8 per cent) dropped below GDP growth (3.1 per cent) prompting the OECD (Organization for Economic Cooperation and Development) Secretary General to express worries over the low rate and the failure of trade to act as a key mover of world economic growth.[2]

Figure 1: Global GDP and Trade Growth (%): 1991-2015



Source: International Monetary Fund (IMF), World Economic Outlook (WEO) Database

Cyclical factors, particularly economic contractions, and exogenous economic shocks (e.g. global financial crisis of 2008, terrorist attacks of 9/11), often affect global trade growth as can be seen from the decline in trade growth in years like 2001 and 2009 (Figure 1). These impacts usually wear out over time enabling trade to recover. Global trade looked well poised for robust growth at the beginning of this decade after growing by 12.4 per cent in 2010, a rate much higher than its pre-crisis level. The optimism proved misplaced, with global trade growth stagnating at around 3.0 per cent for the last four years (2012-2015). Recent empirical research on determinants of global trade identifies structural factors influencing the current slowdown, particularly maturing of

2 'OECD warns on global trade growth amid TTIP criticism by Trump, Clinton', CNBC, 5 September 2016; http://www.cnbc.com/2016/09/05/g-20-summit-hangzhou-oecd-warns-on-global-trade-growth-amid-ttip-criticism-by-trump-clinton.html Accessed on 11 September 2016.

global supply chains and greater substitution of foreign inputs by domestic inputs in large economies like the United States and China.[3]

Prospects of global trade have weakened further with flare-up in anti-trade sentiments in various parts of the world. The political discourse dominating the run-up to the US presidential elections features prominently trade and its alleged adverse impact on industrial and labour markets. Trade agreements providing greater access to contracting members in each other's markets have been main targets of political ire. The 12 nation Trans-Pacific Partnership (TPP) – President Obama's signature trade initiative – is facing an uphill task in being ratified by the US Congress. The US's efforts to steward global trade through trade agreements outside the WTO (World Trade Organization) has been further damaged by the stalling of negotiations on the TTIP (Transatlantic Trade and Investment Partnership) with the US and EU unable to agree on most issues.

Concerns over prospects of global trade were evident in the remarks by the Director General of the WTO after the G20 Summit through his emphasis on correcting prevailing misperceptions on trade and making global trade more inclusive.[4] The G20 decided to give a firm push to trade by working towards building a more open world economy by rejecting protectionism and promoting global trade and investment.[5] But whether protectionism will actually recede depends significantly on the perspectives of major G20 members, such as the US, EU and India, on their trade with China. These perspectives, in turn, would be shaped by correction of capacity in the global steel industry.

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3 Cristina Constantinescu, Aaditya Mattoo, Michele Ruta 'Explaining the global trade slowdown', 18 January 2015; http://voxeu.org/article/explaining-global-trade-slowdown Accessed on 12 September 2016.

4 'DG Azevêdo calls on G20 leaders to make the credible case for trade', World Trade Organization (WTO), 5 September 2016; https://www.wto.org/english/news_e/news16_e/dgra_05sep16_e.htm Accessed on 13 September 2016

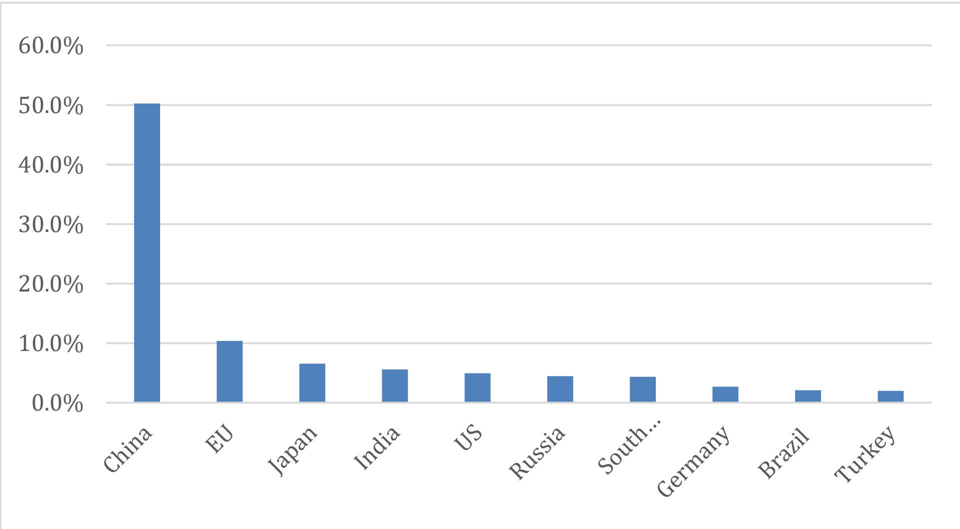
5 G-20 Leaders Communique, Hangzhou Summit, 4-5 September 2016; https://www.wto.org/english/news_e/news16_e/leaders_communique_hangzhou_summit_e.pdf Accessed on 13 September 2016

Steel & China: Flashpoints in World Trade

China was probably the strongest advocate of the G20 recommending a global policy agenda shunning trade protectionism. The Chinese imperative was understandable given the high protective actions taken against Chinese exports in recent times. Most of the protective anti-dumping actions have been targeted against Chinese steel exports.

China is currently the world's largest steel producer and accounts for half of the global steel output (Figure 2). Over the years, it has built up huge capacities in its domestic steel industry. These capacities supported the sustained expansion in the Chinese economy, particularly in infrastructure and real estate, for several years. While domestic demand for steel has reduced following a slowdown in the Chinese economy, the steel industry continues performing to full capacity. The excess steel has flooded global markets. Domestic steel industries in the US and Europe have been hit hard by the deluge of Chinese steel, as have been the emerging markets of India, Korea, Brazil and Mexico. The result has been a sharp increase in the number of anti-dumping actions against Chinese steel exports by affected countries.

Figure 2: Major Steel Producers (% of Total Output) in 2015



Source: Computed from World Steel Association statistics.

The overcapacity problem could not have occurred at a worse time for China. China is eagerly awaiting the status of a 'market economy' at the WTO, which is due at the end of 2016. The terms accompanying China's accession to the WTO in December 2001 allowed it a period of fifteen years for reforming its institutions and pricing policies influencing its exports to shift from state-driven to market-driven actions. Till then, other WTO members can initiate anti-dumping actions against Chinese exports much easily than they can against other members.

The consequences of overcapacity in Chinese steel industry has led to severe repercussions in various parts of the world. Steel producers in the US and Europe have lobbied hard with governments to impose anti-dumping duties on Chinese exports and deny China the market economy status. Earlier this year, the European Parliament legislated against granting the status to China.[6] The US has also indicated its unwillingness to grant the status by citing China's inability to implement market-based rules and trade practices in steel and aluminium industries.

Steel: Splitting the Developing World

The implications of overcapacity in Chinese steel industry have also extended to emerging market developing country producers of steel. India – the fourth largest steel producer in the world (Figure 2) – has been among the topmost initiators of anti-dumping investigations against Chinese steel exports this year. Tata Steel, the leading global steelmaker from India, has been incurring huge financial losses, particularly from its overseas operations in the UK, on account of deluge of Chinese steel exports.[7] It has had to lay off several workers from its UK plants creating major ripples in the local job market and has been contemplating selling off its UK operations. Along with the US and EU, India is inclined to the view that prices of industrial products in China continue to be significantly determined by state support such as input subsidies and controlled interest rates on bank credits to exporters. Such state support, while preventing market determination of prices, enable China to 'dump' exports at cheap rates in global markets.[8] It is evident that India would be inclined to support the US and

6 See Amitendu Palit, 'Chinese take-over threat looms over Europe', *Financial Express*, 24 June 2016 (http://www.financialexpress.com/fe-columnist/canvassing-china-europe-gets-anti-china/295222/) Accessed on 13 September 2016_and Amitendu Palit, 'G20, Free Trade and China', Financial Express, 10 September 2016 (http://www.financialexpress.com/fe-columnist/canvassing-china-g-20-free-trade-and-china/372632/) Accessed on 13 September 2016

7 'Tata Steel posts loss of $476 million', *The Wall Street Journal*, 12 September 2016; http://www.wsj.com/articles/tata-steel-posts-loss-of-476-million-1473686972 Accessed on 13 September 2016

8 'India studying impact of market economy status for China', *The Hindu*, 24 February 2016; http://www.thehindu.com/business/Economy/india-studying-impact-of-market-economy-status-for-china/article8264686.ece Accessed on 13 September 2016

EU in not allowing China the market economy status unless the overcapacity issue is sorted out.

Apart from India, another major emerging market developing country and member of G20 - Brazil - is also unlikely to welcome grant of market economy status to China and continue anti-dumping actions for protecting local industries.[9] Mexico, Korea and Australia – all members of G20 – have resorted to anti-dumping investigations against Chinese steel exports in recent months.[10] The protective responses by India and Brazil are particularly significant, since both, along with China, also comprise the BRICS, a significant global grouping among emerging markets.

G20 on Steel: New Strategic Alignment

The concern of most G20 members on overcapacity in steel and dumping of Chinese exports crept into the G20's decisions with the Communique explicitly mentioning 'excess capacity in steel and other industries' as a global issue demanding collective response. The G20 also noted the role of government support in creating market distortions and contributing to excess capacity. The concerns have led the G20 to propose creation of a Global Forum on steel to be facilitated by the OECD. The Forum will report the progress on shedding excess capacity from global steel output in the next G20 summit of 2017.

The G20 decisions reflect a major part of the current angst against global trade visible in several parts of the world, where China is visualized as the biggest beneficiary of expansion in global trade, thanks to generous state support that helps its producers in compressing prices of exports and capturing global markets. According to the perceptions fuelling the anti-trade angst, more trade, while benefitting Chinese exporters, marginalizes local industrial producers, in both developed and developing countries. The outcome of these perceptions has been to create an alignment among

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9 'Brazil to stay quiet on China market status at WTO : sources', Reuters, 9 September 2016; http://mobile.reuters.com/article/idUSKCN11F2MS?utm_campaign=trueAnthem:+Trending+Content&utm_content=57d3553604d3016f93f1f4bd&utm_medium=trueAnthem&utm_source=twitter Accessed on 13 September 2016

10 'Why Chinese Steel Exports are Stirring Protests', *The Wall Street Journal*, 15 March 2015; http://www.wsj.com/articles/why-chinese-steel-exports-are-stirring-protests-1426466068 Accessed on 14 September 2016

several major economies cutting across the developed and developing world to work towards an agenda aiming to diffuse China's trade expansion.

The strategic alignment has brought into sharp focus the role of state support in influencing trade prices. In this respect, the global narrative on subsidies in trade appears to have turned full circle. Instead of industrialized nations and their agricultural subsidies, the international community, including developing country emerging markets like India and Brazil, now appear more worried about the impact of state subsidies in China on national comparative advantages and global trade.

With several major members of the G20 unlikely to refrain from taking protective actions against China, the G20's call for reducing protectionism might remain only wishful thinking. The anti-China strategic alliance manifesting in the G20 through its decision on steel draws sustenance from the common ground of protection against Chinese expansion. There's little reason to assume that the ground will erode in the near future.

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