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Presents

*Japan’s Steel Cartel and the 1998 Steel Export Surge*

A Japan Information Access Project Working Paper

by

Dr. Mark Tilton
Department of Political Science
Purdue University

Presented for Discussion at
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*Session I*

*Critical Trade Issues Between the United States and Japan*

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About the Author
Mark Tilton is Chair of the Asian Studies Program and an Associate Professor of Political Science at Purdue University who specializes in the political economy of Japan. His work over the last several years has been on the relationship between competition policy, industrial policy and international trade in Japan. Professor Tilton is the author of Restrained Trade: Cartels in Japan's Basic Materials Industries (Cornell University Press, 1996) and co-editor of Is Japan Really Changing Its Ways? Regulatory Reform and the Japanese Economy (The Brookings Institution Press, 1998). Professor Tilton’s B.A., M.A. and Ph.D. are in political science from U.C. Berkeley. He has spent five years in Japan, mostly as a Research Fellow (joshu) and as a Visiting Scholar at the Institute of Social Science and the Faculty of Economics of the University of Tokyo. He is fluent in Japanese, German, French, Spanish, and Portuguese. His research on Japan’s steel industry has been funded by grants from the Japan-U.S. Friendship Commission and the Abe Fellowship Program of the Social Science Research Council. He is a member of the board of the Japan Information Access Project.

For More Information
Japan Information Access Project
2000 P Street, NW, Suite 620, Washington, DC 20036
(202) 822-6040/fax (202) 822-6044
e-mail: access@nmjc.org
Website: http://www.jiaponline.org/

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This Working Paper has been posted on the Japan Information Access Project’s website at http://www.jiaponline.org/
I: Executive Summary

In 1998, record levels of artificially low-priced Japanese steel mill products are flooding the American market. Current thinking might suggest this is fallout from the Asian financial crisis and reduced domestic demand in Japan. While those are factors, in today’s global steel market they are secondary to a more complex and cumulative condition: Japan’s legacy of restrictive market access.

To best understand the reasons for the large volume of low-price exports from Japan—and the problem they pose for international trade at a time of global financial crisis—there must be an examination of the restrictions on competition within Japan’s steel industry and on steel imports into the Japanese market.

The Japanese steel industry has long been governed by what can be called a cartel among steel producers. This cartel today appears to be still supported by the government and accepted by many steel users. What is known to some as a “miezaru karuteru” or “unseen cartel” has historically kept domestic prices high. It has been reinforced by anti-import government procurement practices and fears of retaliation that restrict competitive imports into Japan.

Japan’s long-standing protectionism has shielded it from global trade realities. The Japanese government, by restricting low-priced steel imports, has not forced the tough adjustments on the Japanese steel industry experienced by the U.S. steel industry. During the 1986-1996 period, when the yen was strong and Japanese steel was especially uncompetitive, restrictions on imports allowed Japan to remain a major net exporter of steel. Japan artificially maintained uncompetitive steel capacity that has been the basis for this year’s large exports to the U.S. and other countries.

Now, in the global throes of 1998’s financial crisis, Japan’s legacy of distorted trade damages other country’s economies as well. Japan’s export surge to the United States should be viewed as a global bellwether. The fundamental solution to the problem Japanese imports are posing for the American steel industry is to insist that Japan break up its steel cartel and open its steel market to imports from around the world.

Imports are good for the American steel industry. They have stimulated improvements in productivity and quality. Keeping its markets open to the rest of the world, the United States is boosting the stability of beleaguered economies in Asia, Latin America, and Russia. The United States has the right to expect that Japan offer other nations the same access to its markets that Japan enjoys in the U.S. Japan could contribute to nations around the world by opening its steel market and stimulating its own industry to improve productivity, cut prices, and contribute to the larger Japanese economy.

This Working Paper examines the history, politics, and economics of Japan’s steel policies and how these policies impact world trade as well as the American steel industry. The author offers recommendations on how Japan can better carry out its responsibility as an international leader.
II: Japan Steel Market Dynamics

1. The Mechanics of the Cartel

Japanese steel exports to the United States increased 130 percent from July 1997 to July 1998.¹ Some economists view Japan’s export “success” as evidence of its commitment to the virtues of flexibly working with markets to beat international competitors.² A closer look at the actual operation of the Japanese steel market questions this interpretation. It is merely naïve to attribute the causes of the 1998 Japanese steel export surge solely to market forces.

The Japanese steel industry has invested heavily in capacity and cut costs. It also has employed a cartel to maintain high prices in Japan and used informal trade protection to keep imports from undermining domestic prices or market share. Both the import protection and the cartel, furthermore, do not appear to be simply private customs. These practices are actively supported by government authorities.

Thus, import protection maintains an artificially high level of Japanese steel capacity through long years of extreme international competitive weakness. Japan releases the excess production from this capacity onto world markets, but does not allow reciprocal access to its own markets.

“Big Buyers” and Japanese Pricing

As in other nations, the Japanese steel industry is composed of integrated steel makers, which produce steel products from iron ore, and mini-mills, which produce steel products from scrap. Although mini-mills present an increasing challenge to integrated producers, there are a number of products they are not able to make. Japan’s five major integrated steel producers run what is in effect a cartel, but they do not sell uniformly at their high cartel prices. Rather, the steel market is segmented into a “big buyer” market, characterized by very high prices, and a “spot” market, in which prices are closer to international levels.

The big buyer price in Japan was originally developed to provide discounted prices to large users, but has become a premium price paid by Japan’s large industrial users. This price is higher than the dealer, or spot price in Japan. Both these prices are higher than the export price, as Chart 1 shows below.
The domestic big buyer price has ranged from 67 to 105 percent over the export price from 1993 to 1998, as shown in Chart 2 below.

Chart 3 below shows that the Japanese big buyer price and dealer price have been higher than American spot prices. This chart compares Japanese domestic prices to American West Coast spot prices, which are about 10 percent higher than spot prices east of the Rockies, nearer the major American steel plants.
A better comparison to the big buyer price is the American contract price. Chart 4 below compares the Japanese big buyer price for cold-rolled sheet steel with the American contract price for the same commodity. The fluctuations in the Japanese price largely represent changes in the yen/dollar exchange rate.

Japanese prices, in yen terms, have only dropped about 10 percent over the period. During 1993-1995, the Japanese big buyer price averaged approximately 80 percent above the U.S. contract price. Even when the yen was at ¥133/dollar early in 1998, the price was still 18 percent higher than the U.S. price. One might wonder whether the Japanese big buyer price accurately reflects the real prices that are paid. The United States, for example, has a list price that exists on paper, but which is ignored in setting actual prices. In the U.S., the list price is a convenience for not having to publish new prices continually.\(^3\)

In contrast to the U.S. list price, which does not reflect actual prices, the Japanese big buyer price does in fact reflect the approximate price for at least 60 percent of integrated steel makers’ sales, or
about 40 percent of the total Japanese steel market. This can be verified by comparing the big buyer price with the price that can be calculated from the securities reports of Nippon Steel.

Rationalizing the Differential

Japanese steel insiders argue that the big price differential between Japanese domestic prices and international prices reflects the superior quality of Japanese steel as well as the high level of service that is provided to big users, such as delivery on “just-in-time” schedules. There is undoubtedly some truth to this argument. Nevertheless, Japanese newspapers have long reported that there are real price differences between Japanese and international prices for identical steel commodities. Many are large enough to tempt Japanese users to purchase imported steel.

In addition to its high prices, the other remarkable feature of the Japanese steel market is its unusually low level of imports. Table 1 below shows that Japan has by far the lowest share of steel imports of any of the major steel-using nations.

Table 1. Exports and Imports Compared with Apparent Steel Consumption (metric tons; 1996)

<table>
<thead>
<tr>
<th></th>
<th>Imports</th>
<th>Exports</th>
<th>Apparent Consumption</th>
<th>Imports/Consumption</th>
<th>Exports/Consumption</th>
<th>Net trade/Consumption</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S.</td>
<td>26.6</td>
<td>4.7</td>
<td>106.7</td>
<td>25%</td>
<td>4%</td>
<td>-21%</td>
</tr>
<tr>
<td>Canada</td>
<td>4.8</td>
<td>4.9</td>
<td>13.3</td>
<td>36%</td>
<td>37%</td>
<td>1%</td>
</tr>
<tr>
<td>Germany</td>
<td>15.4</td>
<td>20.4</td>
<td>31.6</td>
<td>49%</td>
<td>65%</td>
<td>16%</td>
</tr>
<tr>
<td>France</td>
<td>11.1</td>
<td>13.1</td>
<td>23.3</td>
<td>48%</td>
<td>45%</td>
<td>-3%</td>
</tr>
<tr>
<td>Italy</td>
<td>11.1</td>
<td>10.4</td>
<td>23.3</td>
<td>48%</td>
<td>45%</td>
<td>-3%</td>
</tr>
<tr>
<td>U.K.</td>
<td>6.3</td>
<td>9.3</td>
<td>13.1</td>
<td>48%</td>
<td>71%</td>
<td>23%</td>
</tr>
<tr>
<td>Belgium/Lux</td>
<td>6.1</td>
<td>14.7</td>
<td>3.6</td>
<td>169%</td>
<td>408%</td>
<td>239%</td>
</tr>
<tr>
<td>Russia</td>
<td>3.7</td>
<td>27</td>
<td>16.4</td>
<td>23%</td>
<td>165%</td>
<td>142%</td>
</tr>
<tr>
<td>Japan</td>
<td>6</td>
<td>19.3</td>
<td>80.6</td>
<td>7%</td>
<td>24%</td>
<td>17%</td>
</tr>
<tr>
<td>S. Korea</td>
<td>11.1</td>
<td>10.4</td>
<td>37.6</td>
<td>30%</td>
<td>28%</td>
<td>-2%</td>
</tr>
<tr>
<td>China</td>
<td>16.4</td>
<td>7</td>
<td>97.3</td>
<td>17%</td>
<td>7%</td>
<td>-10%</td>
</tr>
</tbody>
</table>

Source: Data from American Iron and Steel Institute.

In 1996, imports accounted for only 7 percent of Japanese steel consumption. In contrast, all European countries have high shares of both imports and exports, reflecting their geographical proximity and high levels of trade openness. The United States imported 25 percent of its steel needs.

The reason for the small volume of imports is not that Japan is too far geographically from the rest of the world to import steel. Japan did manage to export steel equivalent to 24 percent of domestic consumption. It might be argued that the low level of imports in 1996 was due to Japan’s surplus capacity and the fact that neighboring Asian nations were using all their own steel to fuel their economic booms.

But, if simple supply and demand explained Japan’s trade patterns, how can Japan’s very high prices be explained? Why didn’t the glut of supply in Japan bring down prices within Japan to levels...
below those of the U.S., where there was a steel shortage? Why didn’t high prices in Japan attract imports from other countries, and away from the U.S., where prices were low? The evidence cited below suggests that the explanation is a combination of a price cartel and import restrictions in Japan.

2. What Insiders Say

One of the startling things I found in talking with people in the Japanese steel industry is how frank and open many are about the existence of a cartel. I asked one Japanese marketing executive of a large Japanese steel firm, who had worked for several years in the United States, to compare competition in the Japanese and American steel markets. He replied, “Oh, it’s totally different. In the U.S. you have free competition. Here it’s like we’re violating the Antimonopoly Law everyday. The steel companies get together and talk about what the price ought to be.” Another steel executive, retired from one of the large Japanese integrated steel firms, told me when I first met him, that the steel industry has an “unseen cartel (miezaru karuteru).”

It is commonly said that the integrated sector of the steel industry is very cohesive (matomari ga yoi), both in the sense that firms do not compete with one another over prices and that they speak with a single voice with the bureaucracy, banks, and other firms. Although the steel companies may discuss prices, their ongoing agreements on production appear to be the true bedrock of the cartel. Market shares of the steel producers have been very stable since about 1973. The five integrated steel producers have invited the most troublesome outsider to the cartel, mini-mill producer Tokyo Steel, to join their cartel, but have never offered enough market share to tempt Tokyo Steel into joining. The above cited retired steel executive told me in 1997 that the Ministry of Trade and Industry (MITI) helps coordinate the production cartel. “Once a quarter, MITI asks each steel company to submit a projection of production. If a company wants to expand production, it has to give MITI a reason. This still happens. MITI provides administrative guidance as to how much steel should be produced. It gives its views on production amounts.” MITI of course has considerable experience with helping manage legal cartels, but most of the legal cartels in large industries were abolished in the late 1980s.

The same retired steel executive argued that the steel industry gets MITI involved, not because it needs help to organize the cartel, but to protect itself from the Japan Fair Trade Commission (JFTC, the agency charged with enforcing Japan’s Antimonopoly Law). “One of the principles in Japanese government is that one agency can’t get involved in another agency’s affairs. What the Steel Association [Japan Iron and Steel Federation] does is get MITI involved so that it can avoid an investigation by the JFTC.”

The JFTC has, in fact, obliged by leaving the steel cartel in peace. As Leonard Lynn and Timothy McKeown noted in their 1988 study of trade associations in the American and Japanese steel industries, while American executives were careful to have lawyers present at meetings between
rivals for fear of antitrust suits, Japanese firms were unconcerned. Steel executives still note this striking contrast between the U.S. and Japan.

Japan’s Construction Ministry supports the cartel as well. The Ministry refuses to buy goods from outside the cartel for public works projects. Why would the construction industry want to miss out on lower-priced products for its projects? According to a recent MITI survey report from its affiliated trade promotion arm, the Japan External Trade Organization (JETRO), construction costs in Japan are 84 percent higher than in the U.S. and civil engineering costs are 2.52 times as expensive. It is also documented that the Construction Ministry has tolerated bid-rigging among construction firms that provide kick-backs to the Liberal Democratic Party (LDP). Steel insiders in Japan report that the Construction Ministry is dead-set against buying even from Japanese producers outside the cartel, much less from importers.

Domestic firms have tried to challenge the steel cartel. Mini-mill operator Tokyo Steel contends that, although it has a license from MITI to produce sheet piles (the interlocking steel sheets used to support building foundations), the Construction Ministry refuses to buy from outsiders to the steel cartel. In 1995, Tokyo Steel was selling its sheet piles for ¥55,000/ton, much lower than the ¥87,000 demanded by the integrated steel producers. According to Tokyo Steel President Masanari Iketani, construction goods have a standard price, listed in two books put out by groups affiliated with the Construction Ministry. For sheet piles, the price is standard nationwide, except in Okinawa where there is a ¥2,000 premium for shipping.

Iketani reports that while some municipalities and prefectures use his company’s sheet piles, when the Construction Ministry is involved Tokyo Steel’s sheet piles are never used. According to Iketani, the steel cartel’s ability to keep outsiders from selling to the Construction Ministry affects the private market as well. Sheet piles are sometimes pulled up and reused, and therefore are often leased. The large leasing companies will not handle Tokyo Steel’s sheet piles because, insiders say, they fear retribution in the public sector. This leaves only the small leasing and trading companies that will use Tokyo Steel’s products.

As the above-cited retired Japanese steel executive told me, “Government construction projects will never buy from the mini-mills, even though they can supply the products.” In regard to imports, a MITI survey report released in September 1998 on access to the construction materials market acknowledged informal barriers are keeping imported steel out of Japanese construction.

The report finds that foreign companies have difficulty entering Japan’s construction materials market because of a complex licensing system and exclusionary business practices by affiliated companies. The survey data suggests that construction costs for Japanese public works projects are on average 34 percent higher than in the United States.

**The Pricing Paradox**

In order to understand the politics of the Japanese steel market, it is important to understand an essential paradox. Many users support the cartel that keeps their inputs expensive. Prices for big users are, in principle, to be based on cost, rather than supply and demand. Supply and demand are
understood to influence price rather than determine it. Negotiations take place between the leading users, at one time the shipbuilding industry, but for the last two decades the automobile industry, and the steel industry over price. Once the auto industry establishes the base price, other user industries follow their lead with minor adjustments.

Prices do not float, but are negotiated on an industry-to-industry basis once a year or less often if markets are relatively stable. Japan’s basic steel price is negotiated between the two price leaders, Nippon Steel and Toyota. Although steel companies are careful not to copy too quickly the Nippon Steel price for fear of being accused of joint sales increases by the JFTC, in fact they follow Nippon Steel’s lead. Steel companies are disciplined enough in their cartel that they all charge exactly the same price. Although the cost of the steel makers is the basic determinant of the price, the financial situation of the users is also taken into account. Because of this, for instance, the hard-pressed shipbuilding industry receives discounts on its steel.

3. “Steel is the State”

Although a weaker yen has narrowed the gap between Japanese steel prices and international prices, between 1986 and 1996 the strong yen made Japanese steel very expensive. Nevertheless, domestic steel users largely did not defect and buy imports. Imported steel rose to a peak of only 9 percent of the domestic market in 1991 and dropped back to 7 percent in 1992, a level at which it has remained.

It is hard to think of an industry harder pressed to cut costs than shipbuilding, an industry dependent on exports for 60 percent of its sales. It competes with South Korea where costs are as much as 25 percent below those of Japan. From 1987 until at least 1994, Japanese firms were paying 40 percent more for steel than their Korean competitors. In 1994, the cost of Japanese steel alone put Japanese shipbuilders at an $8 million cost disadvantage per oil tanker.

In interviews with steel users, it is clear that one reason steel users pay high prices for Japanese steel and resist switching to imports is that they are committed to their relationships with particular Japanese suppliers. A more important reason is that they choose to honor their larger commitment to the Japanese steel industry as a whole. Prices are supported by the steel industry cartel, but they are also supported by the buyers’ willingness to pay what it costs to keep the domestic steel industry going.

It does not appear that the price gap between domestic and international prices is due solely to quality differences between Japanese and foreign steel. Fine gradations of quality are not important for the ordinary grade steel used in construction, which accounts for 43 percent of Japanese steel demand. Seventy-five percent of the steel used by shipbuilders is thick plate, a basically standardized commodity. Two shipbuilders I interviewed said that there was no quality problem with ordinary grade South Korean steel. One of them pointed out that steel from South Korea’s Pohang steel plant was essentially the same as Japanese steel, since it was made with equipment supplied by Mitsubishi Heavy Industries.
It is true that Japanese steel makers produced steel plate in some 400 different sizes for their various customers, and that shipbuilders valued this variety. By 1994, however, shipbuilders were begging the steel companies to standardize these sizes and to give them some price relief in return. Although the large number of sizes was supposed to simplify shipbuilding, some argued that fewer sizes would actually increase shipbuilders’ efficiency and save them more money in building costs than the steel companies would save by standardizing sizes. If this is true, it suggests that the proliferation of sizes in the steel market has acted more as a barrier to imports than as a genuine contribution to production efficiency.

I asked one shipbuilder—whom one would expect to represent the epitome of internationalized Japanese business, having spent many years selling ships in the West—why his firm didn’t buy less-expensive South Korean steel, given the competitive pressures from Korean shipbuilding companies. Although he acknowledged imports were sufficient to provide most of the ordinary quality steel needed, he said it was important to have a domestic industry for the sake of security of supply. He went on to note that, “People often say, ‘Steel is the state’ (tetsu wa kokka nari), or ‘Steel is the rice of industry’. It’s true. If steel gets weak all of industry will get weak. If we switch to imported steel, the country will stop developing.”

This shipbuilder believes that his company should support steel because it is important for the economy as a whole. I and other scholars have found this sentiment echoed many times throughout Japanese industry. Japan’s executives are insistent on remaining loyal to domestic suppliers in order to maintain Japan’s manufacturing base.

4. Refusal-to-Deal Threats

In addition to an interest in security of supply and overall national economic vitality, Japanese steel consumers also avoid imports in fear of retaliation from steel makers. Threats of industry-wide boycotts are strongly suggested by a Nikkei Sangyô Shimbun article on Mitsubishi Heavy Industries’ (MHI) first purchases of imported steel (from Pohang Steel in South Korea). Based on an interview with an official of the Materials Division of MHI, the article reports that the company wanted to buy Korean sheet steel for some time because Japanese steel, at ¥80,000 per ton, cost 60 percent more than Korean steel.

Although MHI was concerned that Korean steel might be somewhat inferior to Japanese steel and delivery less convenient, the quality of the Pohang steel was “quite sufficient” for all but the most-exacting uses. The article reports that “Mitsubishi Heavy Industries has been unable to [buy Korean steel] because it has been concerned with the fact that [Japanese] steel manufacturers were both its suppliers and among its principal customers.” That is, MHI feared that buying Korean steel would endanger both its sales of steel-making machinery and its supplies of steel from the Japanese steel industry. It is crucial to note that MHI was not simply concerned about a relational contract with a specific firm, but was afraid it might be shut out of dealings with the entire steel industry.

The article quoted a Nippon Steel official as saying, “There is no mistake that [MHI] is importing steel in Nagasaki. ... What we’d like to tell them is, ‘Fine. In return we will not supply you with any of the high quality steel that Korea can’t produce.’” Thus, Japan’s largest steel manufacturer thinks of its sales relationships as a broad, all-encompassing commitment rather than simply an agreement to buy specific products. It considers a customer’s decision to switch to another buyer for one
product a betrayal that should be retaliated against by withholding other products it alone can provide. Mitsubishi Heavy Industries, which was the steel buyer and one of Japan’s largest manufacturing firms, also seems to think in terms of inter-industry relational contracts that are enforceable with refusals-to-deal.

As much as Nippon Steel would have liked to use a refusal-to-deal threat to keep MHI from buying Korean steel, it did demure. It feared that making MHI’s imports an issue might lead other buyers to push harder for price cuts and possibly desert domestic suppliers altogether in favor of imports. The company officially treated MHI’s imports as a matter of little importance; the purchase was small and MHI had been asked to buy the Pohang steel in exchange for Pohang’s purchase of MHI steel-making machinery. Mitsubishi never increased the percentage of imports over 10 percent and Japan’s other shipbuilders have remained completely loyal to the domestic industry. In interviews with two shipbuilders and a retired steel executive, this threat of retaliation was confirmed as an important factor deterring shipbuilder plans to buy imports. In describing the relationship between steel and shipbuilding companies, no one used such strong terms as “retaliation.” Instead, all used language of “mutual obligation” and “power” on the part of steel companies to make sure shipbuilders do not abandon them. This “power” also is used to ensure buyers do not try to play domestic steel companies off one another for lower prices.

For most of the major shipbuilders, such as Mitsubishi Heavy Industries, Ishikawajima Harima, or Sumitomo Heavy Industries, shipbuilding is only a small part of their larger operations in industrial machine production. Given this larger relationship, steel companies have considerable retaliatory power over major manufacturing firms. For example, the threat to cut off purchases of new manufacturing equipment, or to tell the shipping companies which handle their imports and exports to stop buying ships from particular firms is effective.

As one shipbuilder put it, “The shipbuilding industry can’t do much about getting the steel industry to lower its prices. If we increase purchases from one steel company to try to get lower prices, then the steel company whose purchases were cut wouldn’t have its shipping company buy ships from our firm.” A retired steel executive also acknowledged the “power” the steel industry had to oblige shipbuilders to reject imports. He said steel companies had some similar power over construction companies, whose services they used when they built new production facilities. He noted, however, that the industry’s recent stagnation had weakened its ability to coerce these industries.

The threat of retaliation also appears to affect the small intermediary shearing and coil center firms that cut and process steel, as well as the large trading firms that buy and sell steel. The Nihon Keizai Shim bun reported, “...[i]t is common knowledge that the domestic steel makers use tacit pressure to keep out imports and support the price structure. The shearing and coil center firms haven’t spoken openly about using imported steel because of fear of reaction from the blast steel makers. The big trading firms haven’t handled imports openly.” The article doesn’t specify what retaliatory measures steel firms threaten, though presumably it would be to withhold supplies or business.
5. Maintaining the Cartel

A previously cited retired executive of one of Japan’s large integrated steel companies told me, “There is pressure on the coil companies by the steel companies in Japan not to buy imports. ... The coil companies worry about whether they will be able to get supplies of high quality steel.” He noted the contrast to the U.S. where nobody pressures small distributors not to buy imports. Coil companies do to some degree find ways to trick the Japanese steel companies by going through intermediaries to buy imports indirectly: “But there are ways to avoid having to comply with the steel companies’ demands. Small importers buy from Korea, and then sell domestically to domestic firms. This way the coil center is not directly buying imports.”

An electronics maker I spoke with said that his company’s fear of the reaction of steel companies to imports was much less in 1994 than it had been 20 years ago. He said that although his firm was reluctant to buy any imported steel, it did arrange for some of its subcontractors to buy imported steel. Although steel companies would have protested before, now they accept small subcontractors’ buying imports. In addition, even though his firm does not actually buy imported steel directly, he thought it could if it gave domestic steel makers advance warning, to give them a chance to match import prices. He said the threat of buying imports can persuade steelmakers to provide discounts on the portion of steel the user might have bought from overseas. In this way, although users buy the vast majority of their steel at standard big buyer prices, they may get discounts on the 5 percent or so of the steel they tell steel companies they are tempted to buy from abroad.

Masanari Iketani of Tokyo Steel commented that the integrated steel companies have, in fact, retaliated for a challenge to their cartel in the Chinese market. According to Iketani, Japan’s five big steel companies have handled their exports as a cartel. In China, for instance, the five companies negotiated a single price with Min Metal, the state trading company handling most of China’s steel imports. All allocated sales among both themselves and among the Japanese trading companies which served as intermediaries.

In 1993, the Mitsubishi Corporation, one of the trading companies, offered Tokyo Steel a contract to sell 20,000 tons of hot rolled coil to Min Metal. Though Tokyo Steel had been selling bar steel in China, its hot coil sales were seen as a threat to the Japanese cartel. The five major steel companies retaliated against the Mitsubishi Corporation by excluding it from rail sales to China. Joint sales negotiations by the five companies with Min Metal were officially stopped as of 1995, but Iketani thinks that in fact they continue.

Mini-mill steel producers also charge that integrated steel makers have harassed them by exporting scrap while refusing to sell it domestically. This apparently is part of the reason for the rise of Japanese scrap prices in the 1990s, as well as why Tokyo Steel lost money in 1996 and 1997. The mini-mills’ trade association has demanded that domestic integrated producers sell them the scrap that they are currently exporting.

6. What Should Japan Do
In September 1998, the Japan Iron and Steel Federation chairman Akira Chihaya told MITI Minister Kaoru Yosano that, in response to American concerns about the export surge, Japanese steel firms would voluntarily curb exports to the United States. "Each company will act in a manner that will not cause trade friction." Chihaya seems to have acknowledged that Japan has a domestic steel cartel capable of manipulating international trade levels at will.

If Japan had lived up to its previous international trade commitments, it would have genuinely opened its markets to steel imports in the 1980s and its Fair Trade Commission would have dismantled the steel cartel. Imports would have pushed prices in Japan downward toward world levels, just as they did in the United States. Japan would then have absorbed its share of steel imports from around the world and, like in the United States, imports would have been forced it to shut down a much greater proportion of its production capacity.

The root problem behind the 1998 surge of exports to the United States is the closure of the Japanese market. This enables the Japanese steel industry to sell more cheaply overseas than it sells domestically. To make its steel market more open, Japan needs to enforce its Antimonopoly Laws and fulfill its international commitments to fair and open government procurement.

The U.S. and Europe have been pushing for years to get Japan to enforce its anti-monopoly laws with limited results. A study of the Structural Impediments Initiative talks showed that American attempts to establish alliances with domestic interests as a way of getting policies adopted were largely a failure. On antitrust policy, the Japanese refused the kind of substantial changes Americans wanted.

Since 1995, both the United States and the European Union have submitted extensive lists of proposed deregulatory measures to Japan. The most recent recommendations were presented to the Japanese government in early October. The housing and construction materials market always has been an important sector of concern in these reports. The reports have also emphasized the need for enforcement and enhancement of Japan’s antimonopoly laws.
III. Recommendations

1. Steel’s Strategic Opportunities

In a powerful new book, Edward Lincoln of the Brookings Institution argues that the United States should avoid pursuing broad, structural issues such as antitrust, deregulation, or keiretsu ties because they are so large and amorphous that it is difficult to make real progress on them. He argues that the U.S. should instead focus on specific sectors where one can achieve tangible results, and in doing so may indirectly make progress on the larger, structural issues.

The steel industry offers an excellent opportunity for just such a strategy. There are two main lessons from the steel case that should be taken into account in planning a course of action:

1. While the United States may act on trade issues bilaterally, in its own self-interest it needs to make multilateral access to the Japanese market its main goal.
   The problem for the United States is not simply that American steel does not get into the Japanese steel market or that the Japanese steel industry sells cheaply in the United States. The larger problem is that Japan keeps out the products of third nations, which allows Japan to maintain a high priced “sanctuary” market. Trade from third nations is diverted from Japan to the U.S., and Japanese industry maintains an artificially large production capacity from which it exports its surplus to the United States. The United States must work energetically to encourage the Japanese to open their market to third nations. Even if the United States were to export negligible amounts of steel itself to Japan, the opening of the market to third nations needs to be an important objective for American trade negotiators. Working on behalf of other nations would have the added benefit of garnering third country diplomatic support to the United States.

2. A market-opening campaign must be long-term.
   Had the United States pushed Japan on opening its steel market in the 1986-1996 period, when the yen was stronger, the larger international price gap would have made it easier to push open doors and establish import channels. The United States should make a ten-year commitment to opening the Japanese steel market and not let up if the yen strengthens and Japan is exporting less vigorously to the United States. Voluntary export restraints by the Japanese steel industry certainly should not be cause for the U.S. to forget about market access issues in Japan. If the American steel industry wants to solve its trade problem with Japan over the long-term it must stand behind U.S. trade officials over the long haul.

2. Japan’s Global Role

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Japan should realize that free trade is a two-way street. It should offer other nations the same access to its markets that it enjoys in the United States. By opening its steel market, Japan could contribute to nations around the world and stimulate its own industry to improve productivity, cut prices, and contribute to the larger Japanese economy.

Japan would do well to heed a recent “Recommendation” issued by the Organization for Economic Co-operation and Development (OECD). The OECD is a Paris-based intergovernmental forum that provides its 29 member countries an exchange of ideas, problems, and solutions toward achieving sustainable economic growth. In March 1998, the OECD issued a “Recommendation” entitled *Effective Action Against Hard Core Cartels* in which it called price fixing and anticompetitive agreements “…the most flagrant violations of competition laws.”

The OECD reported that it is “…important to take action against hard core cartels because they distort world trade and create waste and inefficiency in countries where markets otherwise would be competitive.” It further urged its member countries—which include Japan—to “ensure their own competitive laws are effective…(and) should review their laws periodically to ensure that exemptions are not broader than necessary to achieve their overriding policy objective.”

*In the spirit of the OECD Recommendation, the following are specific actions Japan should consider:*

1. Ensure fair access in government procurement. Establish numerical targets on import penetration in the public works market.
2. Ensure MITI resists helping coordinate the production cartel.
3. Ensure major new resources in staff and budget be given to the Japan Fair Trade Commission in order to scrutinize the steel industry.
4. Ensure that Japan follows international accords on competition policy.
IV. Acknowledgments, Bibliography, & Endnotes

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Dr. Mark Tilton
Purdue University
Department of Political Science
Liberal Arts and Education Building, 1363
Purdue University
West Lafayette, Indiana 47907-1363
Tel: (765) 494-4318 (office until 12/98)
Tel: (765) 494-4176 (office after 12/98)
Fax: (765) 494-0833
E-mail: tilton@polsci.purdue.edu
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ENDNOTES

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3 Personal interview with retired executive from major integrated steel firm, March 1997. This paper draws on a limited number of personal interviews by the author. My method is to seek out interviewees who are in a good position to know how industries are governed and who are willing to be candid. It can be difficult to find candor when one is talking about business secrets, especially regarding such a topic as illegal cartel activities, and the number of interviews that I use intensively is small. Wherever possible, I try to corroborate interview material with published sources.


5 See *Restrained Trade*, p. 176.


7 Personal interview with marketing executive at large Japanese steel firm, Tokyo, October 1996.

8 Interview, retired steel company executive, March 1997.


10 See, for example, the production figures published for 1995 and 1996 in *Tekkō Shimbun* (Steel newspaper), March 12, 1997. Also see chart from Japan Fair Trade Commission produced by *Nikkei Business*, July 4, 1994.

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