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REGARDING STEEL-CONSUMING INDUSTRIES: COMPETITIVE CONDITIONS WITH RESPECT TO STEEL SAFEGUARD MEASURES (INV. NO. 332-452)
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Members of the Commission, thank you for holding this hearing today on this critical economic issue. I am Scott C. Meyer, President and Chief Operating Officer of Ken-Tool. Ken-Tool is a leading manufacturer of specialty tools for automotive repair. The company has been in operation since 1920 and is based in Akron, OH. I am also Chairman of the Motor and Equipment Manufacturers Association (MEMA) and am testifying today in my capacity as Chairman of that organization. MEMA exclusively represents and serves manufacturers of motor vehicle components, tools and equipment, automotive chemicals and related products used in the production, repair and maintenance of all classes of motor vehicles. In the industry, we are referred to as "automotive suppliers," the term I will use in my remarks today. MEMA was founded in 1904 and has approximately 700 member companies. MEMA has offices in Detroit, MI, Washington, DC, Mexico City and Tokyo, Japan; MEMA is headquartered in Research Triangle Park, NC. Sales in our industry totaled approximately $370 billion in 2002 and the industry employs approximately two million workers. MEMA membership encompasses some of the largest manufacturers in America, as well as hundreds of medium and small sized companies located in every part of the country. For example, just my colleagues and I on the automotive supplier panel appearing before the Commission today employ workers affected by the tariffs in 24 states.

Industry Background: The steel tariffs have been so damaging in large part because steel is such an extremely important raw material to our industry. The average vehicle contains about 1,800 net pounds of steel parts made from flat-rolled, bar, tubular, rod and wire stock. Steel accounts for about 55 percent of the total weight of a typical passenger car or light truck. Automakers divested themselves of virtually all of their capacity to manufacture automotive parts and components several years ago. Therefore, automotive suppliers now purchase and process most of the steel used to build any motor vehicle. Any change in the market, like the tariffs, that quickly alters the price and supply of steel has a big effect on our industry.

Three other characteristics of our industry today also tend to intensify the damage done by the tariffs. The first is "cost-down" pricing, and the "cost price squeeze." With extremely few exemptions, automotive suppliers <u>cannot</u> pass on raw material or other price increases to their customers (such as the auto makers or large "first tier" suppliers.) In fact, in the automotive industry, customers expect annual price <u>decreases</u> from their suppliers. While "cost down" formulas differ from one customer to another (such as from one auto maker to another), it is not uncommon for the expected price reductions to equal 20 percent or more over a three or four year period. In other words, if a customer purchased a particular part from an auto supplier for 100 dollars in the year 2000, this year, 2003, the customer expects to purchase the exact same part for 75-80 dollars.

Head to head global competition is also a factor. For example, one U.S. automaker recently sent a strong letter to more than one-hundred of its automotive suppliers informing them that they must meet the lowest possible price worldwide for specific parts or "risk losing future business". Our industry cannot afford tariffs that raise our costs in the face of competition on a global scale. The automaker who sent this letter had benchmarked the suppliers prices against the best prices available in Europe and Asia, and put their supplier on notice to meet the price or loose the business. The combination "cost down" pricing for finished product and rising steel prices and the costs incurred due to delivery and quality problems have caught many automotive suppliers into an unsustainable "cost price squeeze."

The second factor is the industry's production part approval process and five-year platforms. Most automotive parts suppliers, particularly those that manufacture "safety critical" parts, must "qualify" their parts, production processes, and raw material inputs, with their customers in a process known in the industry as P-PAP (production part approval process.) Depending on the part to be "P-PAPed," the process may take twelve months from start to finish. Once the P-PAP qualification process has been accomplished with a customer, an automotive parts supplier is loathe to change any aspect of production; changing even one element, without re-qualification, could subject the supplier to severe penalties, including cancellation of the contract. The P-PAP qualification process mean automotive suppliers must be able to rely on their sub-suppliers for their survival. When steel prices jump, and quality and delivery fail, switching from one steel supplier to another involves, at the very least, a huge risk, and may simply not be possible in a short time frame.

Another unique, but related, aspect of the automotive sector is typically referred to as the "vehicle platform." Broadly speaking, a platform refers to what a particular car model will look like for a set period – usually 4 to 5 years. Thus, once a contract is awarded for a part of a particular vehicle, the automotive parts supplier(s) who was awarded the contract can expect to have that business for the 4 or 5- year period that the platform is in production, assuming they abide by the quality terms of the P-PAP and price terms of the customer's cost-down schedule. If however, a supplier fails to win a bid for a part on a particular platform, it may be years before he will have the opportunity to bid again. The steel tariffs, and the disruption to planning that they have caused, are making it extremely difficult for some suppliers to bid and successfully compete for future business. This will affect their companies and workers for years to come. The damage will far outlive the tariffs.

In the upcoming testimony, you will hear that the steel tariffs have affected automotive suppliers in many different ways. Before my colleagues discuss those details, I would like to state MEMA's basic position that we think many of the negative consequences of the tariffs were unanticipated or significantly underestimated by the U.S. Government, and perhaps frankly by the automotive industry itself, before the tariffs went into effect. Nevertheless, the effects on our industry are very serious.

I would also point out that MEMA understands the importance to America of having a domestic steel industry as part of its manufacturing base. It is also important to have a domestic automotive parts and components industry. A solution that serves one at the great expense and damage to another will leave us with more problems and with less time and fewer options to solve them.

<u>The steel tariffs caused disruptions in the normal business relationships between steel suppliers and automotive suppliers:</u> Immediately after obtaining protection under the steel tariffs, MEMA members reported that some steel companies, emboldened by the tariff protection, suddenly and unilaterally disregarded contracts with automotive suppliers and unilaterally altered terms on pricing, product, time of delivery and quantity of delivery, with no warning.

Automotive suppliers, locked into contracts with their customers to deliver product, had no choice but to quickly capitulate to any price demands and turn to other steel companies or the spot market to make up for late or undelivered steel. Essentially, some steel companies used the protection provided by the steel tariffs to re-write contracts and gouge customers.

As a practical matter, diverting finances from running a business to pursuing legal action in such cases is simply not a practical option for most small and medium sized manufacturers. Even many large companies cannot devote the resources to legal action against their steel suppliers. What our companies want and desperately need is the steel they were promised under contract, on time, as agreed. MEMA expects that further details of this problem and its effects will be revealed over the course of the ITC's 332 investigation.

<u>Foreign trade effects:</u> Since the tariffs went into effect, sourcing for some finished and semi-finished products have shifted out of the United States as a result of the sudden increase in steel prices, supply problems and quality problems. U.S. automotive suppliers who were successfully competing before the tariffs went into effect were not able to retain certain projects after the tariffs went into effect. We are quick to acknowledge that many, various factors affect international competitiveness. But, our experience in the market clearly indicates that certain shifts from domestic to foreign sources of supply were not just a "coincidence" that was going to occur anyway, as some have claimed. The sudden increase in the price of steel, combined with supply problems and quality problems that occurred when the steel tariffs went into effect created a tipping point. Unfortunately, Dana Corporation is not able to testify today, but I would refer the Commission to the Statement of Dana Corporation submitted to the Committee on Ways and Means on April 9, 2003 for further details on this point.

According to data from the Department of Commerce, the U.S. trade deficit in automotive parts increased by 54 percent to a total of nearly $6 billion during the first quarter of 2003. I offer this fact to illustrate that the tariffs undercut a specific group of manufacturers, automotive suppliers, that is already facing significant challenges from abroad. MEMA would, again, quickly point out that many factors are at play. But it is clear to us, and we believe USITC investigators will find, that automotive suppliers and other steel consumers are made *significantly worse off as a result of the tariffs and the steel industries use of those tariffs.*

In the production of automotive parts and components, a shift from domestic to foreign sourcing also leads to shifts in capital investment in plant, equipment and worker training from U.S. to foreign plants and facilities. While loss in business may be quite swift and appear in census data rather quickly, shifts in capital investment and worker training in this industry becomes evident over a longer period of time. We are very concerned that if the tariffs remain in effect for the full three years, the loss of international competitiveness and capital investment on the steel consumer side will grow. The loss of international competitiveness, shift to foreign sources of supply for finished and intermediate products, and the related loss of domestic investment are having negative effects that will certainly extend beyond the life of the steel tariffs.

<u>Erosion of the U.S. steel industry's U.S. customer base:</u> As an industry, automotive suppliers in all parts of the supply chain, (i.e. first tier, second tier, and third tier), and our customers, the automakers, are the largest direct and indirect consumers of many kinds of rolled steel products in the United States. Approximately 90 percent of the steel consumed by U.S. automotive suppliers is made in America. Our health and competitiveness is critical to the future success of the U.S. steel industry. We would therefore urge the ITC to examine what the impact on the U.S. economy and U.S. employment – in the steel industry and in the economy in general-- is going to be as the tariffs erode the steel industry's domestic customer base. What will it mean for the U.S. economy and employment -- and to the steel industry -- if more production, employment and capital investment flow out of the U.S. as a result of the tariffs? Again, the negative effects will certainly extend beyond the life of the steel tariffs, for our industry and the steel industry.

<u>The Steel Industry's Reference to Historical Pricing in a Global Marketplace:</u> While my primary purpose in testifying is to discuss some of the negative impacts of the steel tariffs on automotive suppliers, I do need to comment on at least one argument for relief posed by the steel industry. The steel industry appears to have based its need for relief on the assertion that it is facing the lowest prices for their products in decades. We would note, however, that automotive suppliers, as well as many other manufacturers, also have been in an extended period of strong downward price pressure on our products. This pressure results from a complex combination of global over-capacity for our products, foreign competition (including competition protected by foreign governments and business practices), domestic competition, customer demand for higher value in our products, technology and other factors. The logic behind the steel industry assigning itself a special relief status on the basis of low historic prices in the current global marketplace is not clear from the perspective of an industry such as ours, which in the past and currently faces

the same problem for many of the same reasons. No automotive supplier could hope to command a certain price from its domestic or foreign customers, or base its cost structure on getting a certain price tied to a historical standard.

In closing, I would draw the Commissions attention to these points:

- As major consumers of American-made steel, manufacturers of automotive parts, components and related equipment are seriously impacted by the 201 steel tariffs.
- Some steel companies took advantage of the tariffs to rapidly run up prices and abruptly cut supply and quality to their customers. Clearly, this was not the Government's intention when it set out to help the steel industry, yet these unanticipated side-effects have hurt our industry badly.
- The steel tariffs are causing a shift from domestic to foreign sourcing of some finished and intermediate products.
- We urge the ITC to examine how the tariffs are damaging the overall U.S. manufacturing base, including -- over the long run -- the steel industry itself.
- And finally, please consider that fact that many manufacturers, including automotive suppliers, have been facing strong downward price pressure in the global marketplace. And, under these conditions, what are the reasons for continuing to give a special status to the steel industry at the expense of its U.S. customers and their workers?

I would like to thank the Commission for holding this hearing. This concludes my remarks.

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