

## Steel shutdown reveals 15-25% industrial decline

by David Goldman

*EIR* warned in December 1985 that the U.S. physical economy would begin a 15-25% annual rate of decline sometime early in 1985, and declared in June 1986 that such a decline had begun in the primary manufacturing sector, e.g., metals, as of May. Events in the steel industry demonstrate the accuracy of this judgment. Although the financial press headlines Nov. 28 made much of LTV's announced \$2.08 billion loss for the third quarter, one of the worst in U.S. corporate history, the more important news was buried. LTV's sales of steel during the quarter fell by 24%, from \$1.35 billion during the second quarter to only \$1.02 billion during the third quarter—and this despite the continuing strike at the nation's largest steelmaker, USX.

As the USX strike moves towards its fifth month, steel inventories have not fallen, imports have not risen, and sales of other companies have, on the whole, stagnated. USX, the former U.S. Steel, accounts for one-fifth of former U.S. primary steel capacity, and will probably close permanently half the capacity it had left before the lockout.

An uptick in orders for the other companies (among the major manufacturers, only Bethlehem reported some improvement, while LTV showed a devastating decline) would have occurred under normal circumstances. Imports also would have risen. In fact, the elimination of most USX primary-steel capacity over four months merely forestalled a price collapse in the industry. Primary metals orders (to the extent the Commerce Department figures can be relied upon) fell by 3.9% in September, and by an additional 1% during October. Raw steel output, at about 8 million tons during March 1986, and at 9 million tons in March 1985, averaged less than 6 million tons between August and October of this year.

Yet, steel imports fell during August to 1.53 million tons, about a quarter less than July's 2.1 million tons. Steel "demand" has collapsed, because the principal steel users, namely construction and automobile, are winding down drastically, especially in the commercial construction sector, a heavy user of basic steel products.

The continued fall in orders, the failure to reduce steel inventories, and the low import level all demonstrate that American basic industry is operating at a lower level of the depression ratchet than last spring. Measured by steel consumption, the level has fallen off by roughly 25%; it is impossible to calculate, on the basis of existing data, how far down primary production has fallen, but the underlying level of activity appears to have been declining at an annual rate consistent with the 15-25% annual band projected by *EIR*, starting with the third quarter of 1986.

What complications may ensue for the steel industry is evident in the huge LTV financial write-off, motivated largely by a \$2.1 billion special charge for unfunded pension liabilities. The object of the write-off is to force the bankruptcy courts to, in turn, force the Pension Benefit Guarantee Board to pick up the bill for LTV's unfunded pension plans.

### 'Not optimistic'

As in the story of the desperate vaudevillian who offered to commit suicide on stage, the steel industry will have trouble arranging an encore to LTV's performance. The brokerage house Oppenheimer and Co. had already warned Sept. 11, "Unfortunately, integrated steelmakers have experienced difficult volume, price cost and earnings conditions for the past five years. . . . The likelihood of successful steel industry reorganizations, whether achieved through bankruptcy,

employee-ownership or other changes in ownership, has been diminished due to recent legislation and court rulings strengthening the rights of labor unions during bankruptcy proceedings. . . . In addition, we expect the ability of companies to terminate their pension plans and transfer large liabilities to the Pension Benefit Guarantee Corporation will be greatly reduced by future legislation, as such practice would exhaust the PBGC's assets and is viewed very adversely by policymakers. . . . We are not optimistic about the prospects for steel industry reorganization."

In fact, the \$236 million of unfunded liabilities which the pension agency assumed in September, plus the additional \$336 million LTV has already demanded it assume—both for steel division pensions—pretty much exhaust the agency's assets. Rather than allow the steel companies to dump enough pension liabilities onto the unfortunate PBGC to force Congress to put money in directly, legislators will more likely take legislative precautions against this. The problem is that the steel industry really is going under. This suggests that its only alternative is to undertake massive workforce and capacity reductions, and eliminate potential pension liabilities, in advance.

### **The broad industrial decline**

Steel's underlying strategy, supported by the Reagan administration, involves layoffs and capacity reduction in advance of the underlying collapse of steel utilization by the rest of industry. The immediate objective is to prevent a price collapse in the industry, which seemed inevitable before the USX lockout began last July. However, judging by data available, the collapse of steel output is proceeding only slightly in advance of the collapse of the sectors which utilize steel.

Commercial construction is now running about 30% below previous-year levels, as the 25% national vacancy rate turns into a rout in most of the important urban markets. Construction activity has virtually ceased in the oil-producing states, where even ongoing projects have been abandoned midway, and real-estate interests in the East Coast boom areas are more concerned with forestalling a collapse of existing building prices, than with bringing new ventures onto an already-saturated market.

More broadly, October's data for durable-goods orders and for the manufactures trade deficit indicate how rapidly this unraveling is, in fact, proceeding. Despite administration nonsense about a supposed improvement in the trade deficit, the deficit for manufactured goods actually rose in October, to \$11.1 billion, from \$10.5 billion in September. This was attributed to the increasing deficit with Japan, which rose by nearly a quarter, from \$4.1 billion to \$5.0 billion. Since the dollar-yen rate deteriorated during September, a certain portion of the increased deficit may be attributed to currency changes, but the huge size of the increase testifies to the American economy's continued dependence on what amounts,

after all, to a foreign subsidy in manufactures.

The modest decline in the month-to-month size of the deficit, from \$13.3 billion in August to \$12.6 billion in September, occurred mainly in exchange with the developing sector. Oil imports by volume fell by 15% over the month, reflecting the already-overflowing level of above-ground oil stockpiles accumulated in the United States; this saved about \$300 million on the deficit. Another \$200 million reflected declining imports from Mexico, and imports from developing nations fell generally. Although the complete breakdown is not yet available, the pattern likely reflects lower consumption of raw materials by American industry, and higher imports of finished goods.

### **Drop in capital goods**

That would help make sense of the largest-ever drop in durable-goods orders—6%—posted during October. Without defense capital goods, orders fell by "only" 2.7% in virtually every category. Non-defense capital goods fell by 7.2%—not a surprise, since October was the first month in which the elimination of the investment tax credit under the President's "reform" program was taken into account as a matter of law.

However, the 43.1% drop in defense orders may reflect more than a monthly blip. Defense Department procurement spending appears to have peaked in fact, after a year in which the Pentagon ran largely off earlier-year spending authorizations. The cuts in the defense budget which began in 1985 may have choked off a substantial portion of defense orders.

### **More layoffs in auto industry**

The auto industry's disappearing act continued through Nov. 26, when General Motors announced a new set of layoffs, this time at its Detroit Fiero plant. Six hundred hourly workers will be laid off, following the earlier announcement of 28,000 permanent layoffs at GM.

Overall, the industry has produced 6% fewer cars this year than last (through the third week in November). Counting only the American producers, the fall would have been 8.2%, since the Japanese producers all showed large increases. For General Motors alone, the decline was 16%.

Although most public attention has centered on the floundering of GM management, Ford and Volkswagen are restructuring their overseas operations in a fashion with potential implications for domestic U.S. production. They will integrate their Argentine and Brazilian operations into a single new company, Autolatina, with capacity to build 900,000 cars per year. The merger will promote "permanent technological advance, greater operating efficiency, and greater utilization of existing productive capacity," a joint press release said. Since an increasing portion of basic auto components, including motors, transmissions, and electrical systems, are out-sourced to Ibero-America, the rationalization has implications for the world automobile market.