

Why Stelco, Canada's largest steel producer, failed

Muhammad Mustafa Moeen

The Steel Company of Canada, officially named Stelco in 1980, was incorporated in 1910 by consolidating existing companies engaged in the production of iron, steel and products similar in nature. For more than half a century, Stelco dominated Canada's steel industry, accounting for almost 50% of Canada's total domestic output¹. However, despite its prolonged dominance and sustained rise during The Great Depression, Stelco faltered during the recession of the early 1980s. Stelco's sharp decline was facilitated largely by its toxic labor-management relations, failure to keep up with disruptive innovation and its position at the wrong end of globalization. While Stelco was able to remain profitable during the World War II and The Great Depression by diversifying its product base, its problems were rooted deeply into its structure and ultimately began disrupting organizational functions. Along with being illustrative of all the challenges the manufacturing industry has faced in the past 30 years, Stelco's underperformance is largely reflective of its low productivity and efficiency issues. Eventually, Stelco presented itself as a ripe opportunity for debt investors to profit from, leaving it with no choice but to file for bankruptcy in 2007. The purpose of this paper is to investigate the different factors that contributed to Stelco's decline and argue how they could have been avoided or their effects minimized by the company.

Strained labor relations were central to all of traditional Stelco's problems. In 1936, the Steel Workers Organizing Committee at Stelco formed the Local 1005. Workers were represented by the United Steelworkers of America, the largest, and historically one of the most militant private-sector unions in Canada. In 1946, Local 1005 staged the first of six strikes Stelco found itself at the opposing end of during its lifetime. Regarded as the tipping point for improved

1. Loschiavo, Michael A. *Stelco's Lake Erie Works*. McMaster University. April, 1984. Accessed October 10, 2017. https://macsphere.mcmaster.ca/bitstream/11375/18710/1/Loschiavo_Micheal_A_1984_Geo4C6.pdf.

industrial relations in Canadian history, the 85-day strike was the culmination of worker demands for a wage hike, a 40-hour workweek and, the most important of all, formal recognition of their union. Hugh Hilton, president of Stelco at that time, declared that he would “fight unions until my dying breath.”² It was evident that Stelco’s policies, reflective of Hilton’s viewpoint, actively advocated the industrial relations system that did not allow for unionization of labor, wages were meager, and had no concept of job security or holidays. Workers realized that if the company succeeded in moving steel in-and-out of the production facility, the strike would lose its value. For the strike to achieve its purpose and put the management on alert, the workers pushed to halt steel production and, in the process, garnered support from the working class of Hamilton. Ultimately, the union did emerge victorious and collective bargaining was introduced. More than the modest wage increase and tangible gains, the workers had achieved union recognition and the right to register their protests.

In the same year when the Local 1005 was established at Stelco, Dofasco, Stelco’s biggest competitor in the steel industry, crushed all attempts made by its workers to form Local 1004 by immediately firing its organizers. In addition to that, Dofasco launched a plethora of financial incentives and fringe benefits including the establishment of a recreation center and the introduction of a savings and profit-sharing programs. By recognizing and addressing the need for constructive labor-management relations, Dofasco laid the platform for a sustainable organizational model that would facilitate the company’s long-term growth. On the contrary, Stelco’s organizational structure lacked flexibility and required a more consultative set-up.

2. "The Siege of '46." Cradle of Collective Bargaining. Accessed November 25, 2017. <http://www.humanities.mcmaster.ca/~cradle/html/siege1.htm>.

Communication channels followed a top-to-bottom approach with the workers having no influence on decision-making processes that directly affected them.

Both of Stelco's primary stakeholders, workers and investors, had to bear the cost of a tense and frictional industrial relations atmosphere that had been given rise to by the violent strike. An individual worker needed a very long time to recoup the loss of 81 days' worth of wages. For Stelco, the losses came through disruption of supply continuity and other costs of hard collective bargaining that would continue to pester it for the remaining of its existence. In 1958, workers at Hamilton Works went on an 86-day strike while expressing their unhappiness over the company's decision to not share profits with its employees. Following this were other strikes in 1966 and 1969 that would continue the deteriorating relations between workers and Stelco's upper management.³

In 1981, Stelco employees went on strike for 125 days, the longest in its history. To Stelco's dismay, the strike was combined with the recession of 1981– 82' which led to a significant decrease in the demand for steel. Despite Stelco warning its workers about the possible consequences of continuing the strike, which included lay-offs due to a loss in the company's market share, the union held its ground. The belligerence of the labor force, predictably, resulted in lost markets to key competitors, including Dofasco, because Stelco could not guarantee deliveries. Dofasco benefitted from having no union and, hence, no legal obligation towards serving the increasing demands of workers. Consequently, Stelco went to record the first loss in its history \$41 million, a sum that grew to \$200 million by 1990. Stelco's loss turned out to be a

3. Arnold, Steve. "Hamilton's steel industry from birth, to boom and beyond." TheSpec.com. February 13, 2012. Accessed October 10, 2017. <https://www.thespec.com/news-story/2234571-hamilton-s-steel-industry-from-birth-to-boom-and-beyond/>

loss for the city of Hamilton with the company laying off 3,700 workers accounting for 30 percent of the company's entire labor force⁴.

In a bid to reduce costs and cope with declining steel prices, Stelco began offering early retirement packages with pension provisions being negotiated and agreed upon. The union believed that Stelco not being able to afford pension provisions was a managerial problem and, given that these costs were part of the initial agreement, they would not be willing to make any compromises. As the steel industry continued to deteriorate, Stelco reached a point where it had to have more costs allocated to pension plans than to the wages of its employees due to the high number of pensioners. Stelco's attempts at reducing costs reeked of desperation as it laid off another 800 workers in 1992 and relocated its main headquarters back from Toronto to Hamilton. Between 1991 – 92', Stelco's single-share price came crashing down from \$26 to less than a dollar⁵.

Despite sharing a difficult relationship with its workers for more than half a century, it was Stelco's pension negotiations that turned out to be the decisive blow. Stelco's underfunded pension liabilities and post-retirement obligations to its employees amounted to a \$1.3 billion deficit, leaving the company with no other choice but to file for bankruptcy. Stelco was not the only company suffering from the massive shortfall in global demand for steel, other companies in the industry suffered too. However, unlike Stelco, all other companies were more proactive in their approach and took the necessary steps to modernize their cost base and improve their work culture. When negotiating terms with the union, Stelco should have pushed for the adoption of a two-tiered

4. "Century Of Steel." Biz Magazine. Accessed November 25, 2017. <http://www.bizmagazine.ca/sitepages/?aid=2100&cn=FEATURES&an=CENTURY OF STEEL %7C Q1 2010>.

5. TheSpec.com. "U.S Steel: The end of an era?" TheSpec.com. October 09, 2010. Accessed November 25, 2017. <https://www.thespec.com/news-story/2173428-u-s-steel-the-end-of-an-era-/>.

pension system resulting in the company's senior, more experienced workers receiving higher wages and benefits as compared to the relatively newer recruits. As a result, Stelco would have been able to hire new workers at a wage less than that of its existing workers and reduce its overall wage bills. Furthermore, a two-tiered pension system takes into account shifts in the industry and economic downturns, with the employer being free of any obligations to increase compensation until its financial goals are met.

Stelco's rigidity was not confined to its management of human capital, rather Stelco exhibited a similar attitude towards the acceptance of technologies that had begun to alter the course of the steel industry. In 1954, when Dofasco became the first company in Canada and the entire North America to replace the open-hearth method with basic oxygen technology. The basic oxygen furnace was a more efficient way of producing steel both in terms of costs and time. While Dofasco adopted the new method to increase profitability and gain a competitive advantage in the industry, Stelco continued its use of the traditional open-hearth method until 1984 when the last of Stelco's open-heart furnace was closed.

Between 1978 – 88', Stelco showed increased willingness to make capital investments worth \$2 billion that would reap them high amounts of profit. Following 15 years of planning and construction, Stelco successfully launched the first phase of their Lake Eerie mill, globally recognized as one of the most advanced steel mills, located near Nanticoke⁶. Unfortunately, the timing of Stelco's decision clashed with a time of high economic downturn. Due to an annual decline in the global demand for steel and the exploration of cheaper substitutes, Stelco was unable

6. Mercury, Nicole. "Who killed Stelco?" The Globe and Mail. June 19, 2017. Accessed October 10, 2017. <https://beta.theglobeandmail.com/report-on-business/rob-magazine/who-killed-stelco/article32106645/?ref=http%3A%2F%2Fwww.theglobeandmail.com&>.

to extract the monetary benefits it had expected from the facility. Its construction could not be completed and steel had to be transported back to Hamilton for further processing. Since the facility's construction was curbed by surging costs and decreased investment, it could only manage to produce steel at a fraction of what it would have at its intended final capacity.

Stelco's decision to expand operations to a newer facility was necessary for its survival. It would have allowed Stelco to benefit from the anticipated growth in steel demand and share the burden of production with Hamilton Works. However, Stelco's execution came at a time when the markets did not allow for any growth. At a time when Dofasco computerized its strip mill and overtook its largest competitor as the leading producer of steel in Canada, Stelco suffered from having a cautious approach towards investment decisions. As a result, it delayed the execution of its plan to a point where the idea had lost the competitive advantage it could have originally provided.

In addition to Dofasco being a resisting force between the company and its success as a market leader, Stelco had to face the growing threats of mini-mills and globalization. Mini-mills made use of latest, electric arc furnaces technology to produce steel with low labor involvement required. These mills, along with benefitting from the gains of latest technology, also benefitted from not having to deal with unions or having liabilities in the form of employee compensation packages, unlike companies like Stelco and Dofasco. Apart from the electric furnace technology that it did adopt eventually, Stelco failed to recognize the drastic change in market requirements and demand that had been brought about by the introduction of mini-mills. Stelco was slow to realize that the market's focus had begun to shift from commodity products, what it specialized in, to value-added products. Due to increased globalization and trade, Stelco had to compete with the steel industries from East Asian and European, predominantly Russian. Under new agreements,

tariffs had fallen and exporting good made easier than ever. Stelco could not compete with the cheaply priced steel these industries were continuing to push into Canadian and North American markets. In order to provide resistance to these new companies and industries, Stelco should have increased its investments in research and development to explore cost-effective methods of production that would have ultimately cut down on costs and increased profit margins.

Already struggling to shake off stiff competition from local and international companies, Stelco was rocked by accusations that the company's installed equipment system was, in reality, only 25% effective in controlling pollution. As part of the steel-making processes, Stelco had to make use of and dispose oil, heavy metals and solvents that were poisonous for marine life. Pollutants from Stelco's Lake Eerie and Hamilton Works facilities totaled 41.1 kg, 4kgs in water and the remaining 37.1kg in the form of air emissions and mercury leakages from various openings⁷. These results emerged at a time of growing public concern to reduce environmental damage taking place in the form of both land and water pollution. Stelco was pressured by the government and general public to increase its efforts to reduce emission of life-threatening toxins into the air and the Hamilton harbor. The release of sulfur dioxide, ammonia and carbon into the air resulted in serious health hazards for the public and, once released into the water, killed fish. In an attempt to control the effects and by-products of its steel-making process, Stelco had to invest in the installation of systems and equipment that would facilitate in cleansing waste water and the air. At a time when Stelco was trying to minimize expenses and fighting for costs, these investments further strained Stelco's financials and indirectly added to its growing list of costs.

7. "Mercury pollution here is a problem." The Oakville Beaver. December 29, 2001. Accessed November 25, 2017. <http://www.elgar.ca/Mercury%20Pollution%20Oakville.pdf>.

Stelco's hapless situation could be summarized through its 1996 Annual Report⁸ in which the company recorded a 6% increase in material costs and 2% increase in total employment costs. Increase in variable costs have a high positive correlation with an increase in production and revenues, but Stelco revealed a shocking 49% decrease in its net income from the previous year. Stelco's mismanagement of its resources made it extremely hard to associate the costs it incurred with revenue-generating activities and attributed to its demise. Stelco continues to fight against bankruptcy, lawsuits pertaining to violations of government regulations and the United Steelworkers demanding compensation for contractual violations. While there were certainly external, macroeconomic factors that the company had no control over, Stelco's decline was sped-up more by internal problems stemming from poor labor management, ill-planned schemes and keeping a conservative approach in the eye of technological disruption. Stelco failed to control the financial and organizational strains caused by these issues. Moreover, the company was unable to identify and capitalize on growth opportunities that its competitors benefitted largely from. Once considered the engine of the Canadian steel industry, Stelco ended all steelmaking operations at its Hamilton Works facility in 2013.

Word Count: 2,396

8. "U.S. Steel Canada Inc. Annual Report." Sedar (Profiles). April 7, 1997. Accessed October 10, 2017. <http://www.sedar.com/docClass=2&issuerNo=001549&issuerType=3&projectNo=008012&docId=1479>

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6. "The Siege of '46." Cradle of Collective Bargaining. Accessed November 25, 2017. <http://www.humanities.mcmaster.ca/~cradle/html/siege1.htm>.
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8. "U.S. Steel Canada Inc. Annual Report." Sedar (Issuer Profiles). April 7, 1997. Accessed October 10, 2017.

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