CHAPTER 2: INTERNATIONAL SHIPPING ENVIRONMENT

Shipping and world sea borne trade

Shipping is an economic activity undertaken within an environment of global trade. The demand for shipping services will thus be sensitive to changing patterns of trade and economic activity. In a free market, freight rates would be determined by market forces and would depend on demand and supply. Although on the demand side there has been a steady annual growth of overall sea-borne trade, on the supply side, investment in shipbuilding has contributed to an oversupply of ships in the liner, bulk and tanker markets. The increase in tonnage has brought pressure on freight rates forcing shipping lines all over the world to seek greater levels of efficiency. A desire to achieve greater economies of scale, particularly in the liner shipping industry has seen a remarkable increase in the size and capacity of container vessels and new vessels with a capacity of 6,600 TEU have come on stream.

Shipping markets

"Shipping markets" could refer to several markets related to shipping, such as the market for sale and purchase of ships or the market for the chartering of ships. In this chapter the term refers to the market for shipping services.

World seaborne trade which creates the demand for shipping services stood at 4.95 billion in 1997. Bulk cargo constitutes by far the largest percentage of world seaborne trade with approximately 77.5% of total tons carried. General cargo constitutes the remaining approximately 22.5%.¹

¹ UNCTAD Review of Maritime Transport (1998) page 6. Also note that there is a slight difference in the tonnage recorded as goods loaded (4,953 million) and goods unloaded (5,037 million).
Figure 2.1: Relationship between World Seaborne Trade and World Fleet

World Seaborne Trade
4.95 billion tons as of 1997

77.5% of tons (approximately)

Bulk cargo trade
- Liquid bulk
- Dry bulk
- Specialist bulk

22.5% of tons (approximately)

General cargo trade
- Container
- Break bulk cargo
- Reefer cargo
- Wheeled cargo

Bulk shipping market

75.1% deadweight tons

Fleet of bulk vessels
- Tankers
- Bulk carriers
- Combined carriers
- Specialist bulk

20.6% deadweight tons

Fleet of general cargo vessels
- Container vessels
- General cargo vessels
- Multi-purpose vessels
- Ro-Ro vessels

World Fleet
775.9 million dwt as of 1987

Source: Based on UNCTAD 1998 Review of Maritime Transport
Trends of freight rates from 1974 to 1997 are shown in figure 2.2
Dry bulk and tanker markets

Bulk and tanker trades are subject to free market conditions, and information on cargo and freight rates are offered to prospective players in this market through a network of brokers operating throughout the world. Due to the well-established second-hand market, it is relatively easy for newcomers to join this market provided they can raise the funds required to buy or charter second-hand tonnage. The bulk and tanker sector is not short of entrepreneurs who enter the market with the intent of making a quick return on the investment. The active second-hand market, coupled with new buildings which are now manufactured in a shortened period of time, has resulted in over-tonnaging and depressed freight rates. The low level of freight puts pressure on shipowners to extend the life of ships. It is observed that the average age of a bulk carrier is 14 years, while the average age of a container carrier is 10 years.

Cargo movements of four bulk cargoes, namely, crude oil, coal, iron ore, and grain are shown in figure 2.3.

Figure 2.3: World bulk trades by area (1996)
Liner shipping markets

Liner shipping services operate on fixed itineraries or regular schedules at established rates available to all shippers. The freight rates which are charged are based on the shipping company’s tariff or if the company is a member of a liner conference, the tariff of that conference. A liner ship would thus carry an assortment of goods, in large or small quantities, belonging to a number of shippers, in identifiable lots, on advertised routes, destined to a single or to multiple ports, at fixed intervals, on a fixed tariff, with mark and count.

Liner shipping bears high network costs and tends to be more capital intensive than bulk shipping. The routing and scheduling challenge in container shipping is also quite different to that of bulk shipping.

Liner conferences which have been an essential feature of liner shipping services have been subject to change due to multilateral instruments, regulatory regimes, structural change in the industry and market forces. With the advent of container transport and development of intermodalism the liner shipping market has structured into a single global market. In the process of restructuring, liner shipping companies have devised various forms of horizontal and vertical operative agreements amongst them and accelerated their business concentration.

Growth in liner trade

The explosive economic growth which has prevailed since the mid 1980's has led to the growth of exports and imports of manufactured goods between Asia and the European and North American countries and within the Asian region itself.

This expansion of demand for transport to and from Asian countries and within the Asian region, has given rise to a vast Asian-related shipping market, and an unprecedented growth in container traffic.

Figure 2.4 illustrates how world container movements have grown between 1993 and 1996.
Intra-Asian trade links have developed dramatically over the last decade, and in 1996 more than half of Asia’s trade was intra-regional. Global carriers have accordingly increased their presence in these markets. In 1998, nine<sup>2</sup> of the world top twenty carriers were from Asia as shown in Table 2.1. The deployment of post-panamax vessels between 4,000-6,000 TEU have provided opportunities for economies of scale.

APL not reflected as Asian carrier in spite of purchase by NOL.
Table 2.1: The World's Top 20 Carriers' Containership Capacity in Operation

<table>
<thead>
<tr>
<th>Ranking</th>
<th>Carriers</th>
<th>TEU</th>
<th>Ranking</th>
<th>Carriers</th>
<th>TEU</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Evergreen</td>
<td>84,116</td>
<td>1</td>
<td>Maersk</td>
<td>346,123</td>
</tr>
<tr>
<td>2</td>
<td>USL</td>
<td>71,219</td>
<td>2</td>
<td>Evergreen / Uniglory</td>
<td>280,237</td>
</tr>
<tr>
<td>3</td>
<td>Maersk</td>
<td>56,151</td>
<td>3</td>
<td>P&amp;O Nedlloyd</td>
<td>250,858</td>
</tr>
<tr>
<td>4</td>
<td>Sea-Land</td>
<td>46,917</td>
<td>4</td>
<td>MSC</td>
<td>220,745</td>
</tr>
<tr>
<td>5</td>
<td>Hapag-Lloyd</td>
<td>39,154</td>
<td>5</td>
<td>Hanjin -includes DSR-Senator</td>
<td>213,081</td>
</tr>
<tr>
<td>6</td>
<td>OCL</td>
<td>36,266</td>
<td>6</td>
<td>Sea-Land</td>
<td>211,358</td>
</tr>
<tr>
<td>7</td>
<td>NYK</td>
<td>35,164</td>
<td>7</td>
<td>COSCO</td>
<td>202,094</td>
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<tr>
<td>8</td>
<td>OOCL</td>
<td>34,084</td>
<td>8</td>
<td>APL</td>
<td>201,075</td>
</tr>
<tr>
<td>9</td>
<td>K-Line</td>
<td>28,964</td>
<td>9</td>
<td>NYK / Tokyo Senpaku</td>
<td>163,930</td>
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<tr>
<td>10</td>
<td>APL</td>
<td>27,396</td>
<td>10</td>
<td>MOL</td>
<td>133,681</td>
</tr>
<tr>
<td>11</td>
<td>MOL</td>
<td>27,353</td>
<td>11</td>
<td>Hyundai</td>
<td>116,644</td>
</tr>
<tr>
<td>12</td>
<td>COSCO</td>
<td>24,940</td>
<td>12</td>
<td>ZIM</td>
<td>111,293</td>
</tr>
<tr>
<td>13</td>
<td>Nedlloyd</td>
<td>23,916</td>
<td>13</td>
<td>CP Ships</td>
<td>105,322</td>
</tr>
<tr>
<td>14</td>
<td>UASC</td>
<td>23,862</td>
<td>14</td>
<td>CMA-CGM</td>
<td>91,600</td>
</tr>
<tr>
<td>15</td>
<td>CGM</td>
<td>23,454</td>
<td>15</td>
<td>Hapag-Lloyd</td>
<td>90,879</td>
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<tr>
<td>16</td>
<td>ZIM</td>
<td>20,282</td>
<td>16</td>
<td>OOCL</td>
<td>90,063</td>
</tr>
<tr>
<td>17</td>
<td>YMIC</td>
<td>20,086</td>
<td>17</td>
<td>K-Line</td>
<td>89,717</td>
</tr>
<tr>
<td>18</td>
<td>Wilhelmsen</td>
<td>19,624</td>
<td>18</td>
<td>Yangming</td>
<td>79,840</td>
</tr>
<tr>
<td>19</td>
<td>Baltic</td>
<td>18,371</td>
<td>19</td>
<td>UASC</td>
<td>59,331</td>
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<tr>
<td>20</td>
<td>NOL</td>
<td>15,803</td>
<td>20</td>
<td>SCL</td>
<td>55,584</td>
</tr>
<tr>
<td>TOTAL</td>
<td>677,122</td>
<td></td>
<td>TOTAL</td>
<td>3,113,455</td>
<td></td>
</tr>
</tbody>
</table>

New developments in trade and shipping

Until a few years ago economists referred to growth in "international trade". They now refer to growth in "global trade". Are these then different concepts? The term ‘international trade’ is increasingly used to refer to trade between two countries. The term ‘Global trade’ is an extension of the term ‘international trade’ where the market place is no longer perceived to be two overseas countries but the entire world i.e. the global market place. Is this a new phenomenon or is it a new way of looking at an old scenario. Perhaps it is a little of both. Three factors have assisted in the creation of the global market place: liberalization of trade, technology of communication and modern transport.
In order to understand the new developments in the shipping sector, in the presence of increasing global trade, it is necessary to reflect on the nature of modern international production and distribution. The following scenarios may help to convey the essence of globalization in the context of production and distribution.

Cotton picked by Pakistani villagers is shipped in break bulk form to factories in Japan for processing. The bales of cloth are then shipped in containers to garment manufacture in Fiji. The finished garments are shipped back to the fashion markets in Japan and Europe.

Cashew nuts harvested mechanically in Western Australia are partly processed locally and then shipped to China to complete the labour intensive process of removing the outer layer of the cashew nut. The cashew nuts are then shipped back to Australia for further processing, packaging and distribution to overseas markets.

Components for television sets manufactured by Japanese companies located in Malaysia are produced partly in Japan and partly in Malaysia. The components produced in Japan are shipped to Malaysia and the television sets are assembled in Malaysia. The television sets are finally shipped to markets in Asia, USA and Europe.

Vegetables picked in the evening in Harare, using appropriate technology are on supermarket shelves in London the next morning. The appropriate technology in this instance is hand picking by villagers. Liberalization of trade enables the exporters from Harare to access the UK vegetable market. The Boeing takes the place of the old steamer, and orders are transmitted to the village through the new technology of the fax and the phone. New opportunities, and new terms that reflect these opportunities.3

The above examples highlight the fact that manufacturers and producers seek comparative advantages to sell their products in the global market. Comparative advantages are subject to change. Pakistan may choose to develop its ability to process the cotton and “value add” to its exports. Japanese buyers may then decide to arrange the shipment of cloth directly from Pakistan to Fiji, thus cutting out a link in the transport chain. Australian farmers seek new

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3 Paul Krugman; The Accidental Theorist, P. 85; Penguin Group 1999. Krugman elaborates this example in his discussion on the driving forces behind globalization.
technology to remove the husk from the cashew nut and may have no need to first ship the product to China. If the labour costs in Malaysia increase beyond a point Japanese companies would seek to re-locate their industry in a new location. Transport patterns would have to follow these changing trends in production and distribution.

Structural change in the liner shipping markets

Globalization of production has led to the creation of a demand for competitive global transport services. Shippers are becoming highly conscious of the benefits of logistic management on a global scale. Shippers now require a service that would ensure the right product in the right place, at the right time with one operator assuming responsibility for the door-to-door service. Shippers have thus begun to build partnerships with reliable carriers who can provide global transport networks. Leading liner carriers therefore have no option but to develop business strategies to expand their service network to meet the changing needs of the market place and offer a fixed day/weekly service at a global level.

To cope with the intense competition, and provide the frequency and scope of services required by shippers, liner shipping companies have devised various forms of horizontal and vertical integration with each other.
Vertical cooperative agreements in the form of global alliances are also being formed by individual carriers of different nationalities for the purpose of strengthening their marketing activities, including sales networking and value added services. Each carrier belonging to a particular alliance may have the flexibility to make further alliances so as to further expand its activities on a global basis.

Mergers between leading shipping lines which commenced around 1996, heightened in 1997 with a total of five merges and has tapered of in 1998 and 1999.
### Table 2.3: Mergers from 1996-1999

<table>
<thead>
<tr>
<th>Year</th>
<th>Mergers</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>1996</strong></td>
<td>CMA ➔ CMA-CGM</td>
</tr>
<tr>
<td><strong>1997</strong></td>
<td>P &amp; OCL ➔ P &amp; O NEDLLOYD</td>
</tr>
<tr>
<td></td>
<td>NEDLLOYD ➔ P &amp; O NEDLLOYD</td>
</tr>
<tr>
<td></td>
<td>HANJIN ➔ HANJIN_DRS-SENATOR</td>
</tr>
<tr>
<td></td>
<td>DSR SENATOR ➔ HANJIN_DRS-SENATOR</td>
</tr>
<tr>
<td></td>
<td>NOL ➔ NOL APL</td>
</tr>
<tr>
<td></td>
<td>APL ➔ NOL APL</td>
</tr>
<tr>
<td></td>
<td>CP SHIPS ➔ CP SHIPS</td>
</tr>
<tr>
<td></td>
<td>LYKES LINE ➔ CP SHIPS</td>
</tr>
<tr>
<td></td>
<td>CONTSHIP ➔ LYKES LINE</td>
</tr>
<tr>
<td></td>
<td>PRESSAG ➔ PRESSAG</td>
</tr>
<tr>
<td></td>
<td>HAPAG LLOYD ➔ HAPAG-LLOYD</td>
</tr>
<tr>
<td><strong>1998</strong></td>
<td>NYK ➔ NYK</td>
</tr>
<tr>
<td></td>
<td>SHOWA LINE&lt;sup&gt;4&lt;/sup&gt;</td>
</tr>
<tr>
<td><strong>1999</strong></td>
<td>MITSUI OSK LINE ➔ MITSUI OSK LIINES</td>
</tr>
<tr>
<td></td>
<td>NAVIX LINE&lt;sup&gt;5&lt;/sup&gt;</td>
</tr>
</tbody>
</table>

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<sup>4</sup>  Japanese bulk & tanker carrier

<sup>5</sup>  Japanese bulk & tanker carrier
For developing country shipping companies that wish to enter or continue to provide liner shipping services, the emergence of global carriers has meant increasingly strong competition. Inability to invest in capital intensive container shipping and the provision of extensive market networks may result in developing country shipping lines losing their traditional role in all but niche markets.

The impact of the Asian economic crisis on liner shipping

The economic turmoil that has been affecting the Asian region since July 1997 has resulted in the following:

- depreciation of currencies;
- weakening of economies;
- sharp reduction in asset value;
- erosion of investor confidence

This economic contagion effecting the region and in particular Southeast Asia, is different to other economic cycles that have been experienced in the past. The current economic crisis has adversely affected all countries in one way or another. The crisis which first hit Thailand and then spread to Indonesia, South Korea, and other Southeast Asian countries, have also affected the rest of the world.

Until the middle of 1997, Asia was the fastest growing region in the world. With freer trade opening up of world markets to South East Asian goods, and the growth and expansion of export oriented industries, Southeast Asia was for several years, the most dynamic and prosperous region in the world. Southeast Asia was also a good market for the products of other countries. The economic crisis and the rapid depreciation of currency however has had the effect of drastically reducing, within months, the wealth of Southeast Asia, that had taken a decade to achieve. It has also taken away important export markets from the rest of the world. Introduction of budgetary restraint as part of austere fiscal measures, has led to the cancellation or postponement of infrastructure projects. The world’s richest nations now at different stages of the economic cycle, from a gloomy Japan, to a recovering Europe, and a buoyant United States, find themselves facing a slowdown in the global economy at a time when they need a growing world market into which they can export. It is evident that the turmoil in the Asian economies has had a direct and indirect effect on the demand for shipping services.
The short-term consequences in countries which have experienced currency depreciation has been a surge in exports creating serious imbalances in trade flows and equipment requirements beyond anything carriers had envisioned. Shipping lines have been forced to alter vessel schedules and make special arrangements to reposition empty containers to meet demand. Repositioning has become an increasingly serious problem for major shipping lines, particularly in countries such as Indonesia, which have been hardest hit by the regions economic woes.

In the long term, the price advantage of exports from Southeast Asia may not last as currencies adjust themselves and the cost of components of manufactured/assembled goods increase. Nevertheless it is anticipated that as the economies of Southeast Asia recover, the demand for shipping services to and from Asia as well as within Asia will continue to grow. There is already optimism of a strong export led recovery in some of the countries which were worst affected such as Thailand, Malaysia, Philippines and South Korea.

Shipping Policy Trends

Liberalization vs protectionism

Liberalization aims at free trade and services on the basis of non-discriminating commercial principles. Statistical links have been drawn between free trade and economic growth. The economic rationale for free trade is that all countries have assets, whether they be human, industrial, natural, financial, which could be used to produce goods and services for the domestic or overseas market. Economic activity is generated and thus economic benefit is derived when these goods and services are traded. For countries to be able to trade overseas, they have to take advantage of their assets in concentrating on what they can produce best and trade this product (s) with other counties for different products. Economists refer to this as the comparative advantage of countries.
Liberal trade policies not only help exporters and importers of goods but also provide opportunities for those involved in the transport of goods.

Liberalization through the removal of tariff and non tariff barriers to trade may of course have the immediate result of a flood of imports which are more competitive than the domestic products with adverse repercussion on some domestic industries. Over a period of time however the ‘open economy’ and market access should help domestic industries to become competitive in the manufacture and trade in some other commodities. Market forces alone may not be sufficient for industries affected by competitive imports to survive the onslaught and find niche markets. Governments thus have an important role to play in ensuring the gradual liberalization of markets and in helping domestic industries to find new areas to grow into. Fledgling industries may also require fiscal and other support measures.

Protectionism aims at safeguarding the trade and services of a country by preventing or restricting the entry of overseas goods and services through discriminatory measures.

The shipping sector has a strong history of protectionism and in the past countries have adopted direct and indirect protectionist measures to establish, develop and sustain their national shipping industry. With some exceptions most obvious and direct protectionist measures have been adopted by the developing countries. These measures have to be viewed in its historical context.

**Historical perspective - the advent of protectionism**

A national merchant shipping fleet has traditionally been considered important by countries for strategic purposes in that the ships could be requisitioned in times of strife to ensure that essential trade could go on as usual. A shipping fleet has also been considered important to carry the import and export trade of a country and assist in the movement of domestic trade.

When one examines the development of shipping fleets in a global sense, the mid twentieth century was characterized by the traditional maritime countries possessing large fleets while the newly emerging countries strived to establish fleets of their own. With a few notable exceptions such as India and some countries in Latin America, such as Brazil and Chile, which had been striving to promote the development of a national fleet or had a long tradition of national shipping, by the 1950's and 1960's the shipping industry in the developing countries was dominated by the traditional maritime powers.
During the 1950's and 1960's the developing countries began examining the economic systems which they had inherited from the colonial powers. They quickly observed that they were operating under a system in which economic activity was substantially or exclusively geared to the production of primary commodities. The commodities were then sold in the markets of the developed countries in exchange for manufactured consumer and capital goods. Many colonies were also heavily dependent on foreign supplies of essential food stuff and petroleum products.

For countries that were so heavily dependent on foreign trade, the adequacy of shipping services was an important consideration. The newly emerging countries recognized the need to diversify their export commodities and saw the importance of establishing their own shipping lines.

When the national lines of the developing countries attempted to access the cargo generated by the foreign trade of their countries however, they found that this was not possible due to the trade routes being dominated by liner shipping conferences controlled by foreign shipping lines. As these conferences were "closed" conferences, the new national lines could gain membership of the conference only with the approval of the existing member lines. Such approval was not forthcoming and the new national lines found themselves in the position of not being able to operate in their own market.

Multilateral instruments such as the United Nations Code of Conduct for Liner Conferences (UN Liner Code), bilateral shipping agreements which sought to divide the trade between two groups of shipping lines on a 50-50 basis and unilateral cargo reservation measures practiced by developing countries in the 1970's and the early 1980's have to be understood in the above context.

The adoption of the UN Liner code in 1974 appears to have encouraged the interventionist policy of developing countries. Although the U.N. Liner Code did not come into force for 10 years after its adoption, its existence seems to have indicated an endorsement of measures designed towards cargo sharing. Thus after 1974, many countries adopted legislation which provided for liner cargoes to be distributed between respective groups of national lines and third country lines on a 40:40:20 basis. Some countries established freight booking offices to implement this principle. Liner Conferences and the international liner shipping industry in general sought to accommodate these legislative and administrative measures as part of a new international economic order in liner shipping.
Towards liberalization of shipping

Ironically, the coming into force of the U.N. Liner code in 1983 saw a marked change in climate towards protectionism in maritime services. The developed countries of Western Europe whose ratification brought the Convention into force made clear reservations or declarations that the code should only apply to liner conference cargo and not to all liner cargo. Developed countries also stated that measures taken by developing countries to restrain access to cargo which were not in conformity with the Convention would give rise to retaliatory action.

The EEC, (now EU) and its member governments also exerted diplomatic pressure on developing country governments to abandon their restrictive regulations on access to cargo. Similar pressure was exerted by the Federal Maritime Commission of the United States of America, including the use of penalties to persuade trading partners in Latin America to move away from bilateralism and open their trades to third country carriers.

There were also several domestic factors within developing countries that accelerated the pace of liberalization of shipping as there was a recognition that:

- Cargo reservation schemes were restricting the shipping opportunities available to exporters and hampering the expansion of exports and imports.
- Relatively high freight rates charged by national shipping lines operating in a protected market was adding to the cost of exports and imports.
- National shipping lines were not being subject to the forces of outside competition and technological change and therefore became outmoded and operationally inefficient.
- In many cases national shipping lines which were state owned were running at a loss and required subsidies instead of being a revenue earner for the state.

It was a combination of these international and national factors that led to the dismantling of the cargo reservation policies of the developing countries in the early nineties.
Liberalization of shipping must, however, also be seen in the context of the wave of economic liberalization that has been sweeping across the developing world. Frustration caused by long years of inadequate development, the worsening terms of trade and the disillusionment with socialist policies brought about in countries political change which favoured private enterprise. This has led to a market oriented and deregulated approach to development, with the state seeking to increasingly withdraw from the direct operation of economic enterprise.

In the long-term, a liberal and global trade regime will be to the benefit of all countries. Active participation of all countries in the WTO and the development of common policies will help to ensure that liberalization takes place at a pace that is acceptable to developing countries in the ESCAP region.

The World Trade Organization (WTO)

The World Trade Organization (WTO) was created in January 1995 as a result of the final round of the General Agreement on Tariffs and Trade (GATT), otherwise known as the Uruguay round with the participation of 111 countries. GATT was an international agreement formulated in 1947 to facilitate multilateral trade negotiations. It was supported by an ad hoc international agency which was set up later.

One of the main objectives and in fact its main achievement has been the opening up of markets. GATT was organized as a series of trade talks, or rounds, and the Uruguay round (the 8th round) included non-tariff barriers, trade in goods (particularly agricultural goods) and trade in services. Earlier trade rounds dealt mainly with the reduction of tariffs.

The WTO which replaced GATT is a full fledged international Organization with a permanent secretariat administering three major agreements, including the GATT.
International trade in goods arise where a product is transported from one country to another. This is an easy idea to understand. International trade in services is a little more difficult to conceptualize as it refers to the buying and selling of services between different countries. The rules that apply to one type of service may not be applicable to another type of service. Banks, shipping lines, airlines, accounting firms, telecommunication firms are all engaged in serving overseas markets. The diversity of services offered are recognized in that annexes to the GATS deal with different services.

The General Agreement on Trade in Services (GATS) is the first set of multilateral, legally enforceable rules covering international trade in services and has several components.

- General principles and obligations of countries, in the main text
- Rules for specific sectors in the annexes
- Individual countries specific commitments to provide access to their markets
- Lists where countries are temporarily not applying the "most favoured nation principle"

Most favoured nation treatment (MFN)

Favour one, favour all. MFN means treating one’s trading partners equally. Under GATS, if a country allows foreign competition in a sector, equal opportunities in that sector should be given to service providers from all other WTO members. MFN applies to all services, but some special temporary exemptions have been allowed.
MFN exemptions: temporary and one-off

WTO members have also made separate lists of exception to the MFN principle of non-discrimination. When GATS came into force, a number of countries already had preferential agreements in services that they had signed with trading partners, either bi-laterally or in small groups. WTO members felt it was necessary to maintain these preferences temporarily. They gave themselves the right to continue giving more favourable treatment to particular countries in particular service activities by listing MFN exemptions alongside their first set of commitments. In order to protect the general MFN principle, the exemptions could only be made once; nothing can be added to the lists. They will be reviewed after five years (in 2000) and will normally last no more than 10 years. The exemption lists are also part of the GATS agreement.

GATS cover all services including maritime services. The maritime sector is an important service and the openness of such services are considered important for the development of world trade and for which multilateral trade disciplines have to be formulated. GATS is a powerful instrument which will exercise pressure for progressive liberalization of all trade in services including shipping.

Negotiations conducted by WTO to include a specific chapter on the liberalization of services in the maritime sector however failed due to the reluctance of the major players to agree to a multilateral instrument. The USA wished to continue bi-lateral negotiations and unilateral sanctions. Under the circumstances negotiations relating to the liberalization of shipping services were suspended in June 1996, to be resumed in the year 2000. The negotiating group has identified three main areas where rules will have to be developed: Access to and use of port facilities, auxiliary services, and ocean transport. The rationale behind the WTO efforts to liberalize maritime services is based on the premise that open markets will benefit participating nations through greater business

http://www.wto.org/wto/about/facts.2.htm

See further http://www.wto.org/wto/about/facts.1.htm. The output of the WTO or the way in which it operates is often referred to as “multilateral trading systems”. The term “multilateral” is used in stead of “global or world” to describe the system because although almost all the main trading nations are members of the WTO, some are not. So multilateral refers to activities on a global or near global level. It contrasts with actions taken regionally or by other smaller groups of countries.
opportunities. Agreement on a set of international competition rules could play a central role in the GATS on shipping. The WTO system forbids unilateral action and has a dispute settlement mechanism to examine trade rows, issue verdicts, and monitor whether countries comply with their international obligations.

The framework: GATS articles

Basic principles:

- All services are covered
- Most favoured nation treatment in areas where commitments made
- Transparency in regulations
- Regulations have to be objective and reasonable
- Internal payments: normally unrestricted
- Individual countries commitments: negotiated and bound
- Progressive liberalization: through further negotiation

The WTO has more than 134 members accounting for over 90% of world trade, while 30 others are negotiating membership. The over riding objective of the WTO is to help trade flow smoothly, freely, fairly and predictably. It is the only international organization dealing with global rules of trade between nations. These rules contained in the WTO agreements and known as the multilateral trading system\(^9\), are negotiated and adopted by member states and later ratified by them. They become the legal ground rules for international commerce and governments have to keep their trade policies within agreed limits. On the other hand the rules guarantee member countries important trade rights.

The rationale behind the WTO efforts to liberalize shipping services is based on the premise that open markets will benefit participating nations through greater business opportunities. A specific chapter on shipping in the General Agreements in Trade in services of the WTO could result in a multilateral instrument that ensures free markets and fair competition. Agreement on a set of international competition standards could thus play a central role in the GATS on shipping.

\(^9\) See further http://www.wto.org/wto/about/facts.1.htm
Once the negotiations relating to the maritime sector resumes in the year 2000, all governments will have the right to participate in the discussions and provide an input. It is therefore important that governments in the ESCAP region understand the way in which the WTO negotiations are carried out. It is also important that Governments in the region review their shipping policies to determine the market access provided to overseas service providers and the extent to which they wish to liberalize the shipping and port sector.

The WTO is conscious of the fact that over three-quarters of its members are developing countries or least developed countries and special provisions are included in all WTO agreements.

The special provisions include the following:

- Longer time periods for implementing agreements and commitments
- Measures to increase trading opportunities
- Provisions requiring all WTO members to safeguard the trading interests of developing countries
- Support to help developing countries build the infrastructure for WTO work, handle disputes, and implement technical standards.

Organization for Economic Co-operation and Development (OECD)

Shipping has been one of the main concerns of the OECD from its inception in 1947. The OECD has always sought to defend the principles of liberalization and the code of liberalization of current invisible operations (called the Code) of 12 December 1961 affirmed this. The Code has become a successful example in promoting liberalization. The OECD’s activities relating to the shipping industries are conducted through the Maritime Transport Committee (MTC) whose functions mainly relate to the exchange of views, consultation and cooperation.

In 1987, the OECD agreed to a series of principles and guidelines amongst member states on the following:

- common principles of shipping policy for member countries; and
- liberalization of current invisible operations relating to maritime transport.
The main body of the recommendations were based on four elements:

- The maintenance of open trade and free competitive access to international shipping operations;
- Coordinated response to external pressure, based on full consultation between member countries;
- Active opposition to regimes which restrict access to cargo (moving internationally) by shipping companies adhering to the principle of free competition on a commercial basis;
- A common approach to the application of competition policy in the shipping sector.

These elements embodied in 12 principles formed a new and coherent, common approach to international shipping policy between OECD member countries and their relations with countries outside the organization.

In the 1987 guidelines the developed market economy countries had for the first time, a detailed document covering a large number of aspects of international maritime transport, which could be used as a yardstick for national policies. The recommendations and resolutions were essentially aimed at preserving and encouraging the freedom of world-wide seaborne trade.

Problems relating to shipping policies between OECD member and non-member countries usually arise due to protectionist pressures from developing countries. Conflict among member countries are caused by different approaches towards the regulation of liner conferences, restrictions upon free access to specific types of cargo and by the different fiscal regimes to promote the development of national fleets.

**The European Union (EU)**

The maritime policy direction of the European Union (EU) is contained in the paper issued in 1996 titled “Towards a New Maritime Strategy”. Although the paper only has the status of a communication at present, it will no doubt be one of the main instruments in the development of shipping policy within the EU.

The main components of the new Maritime Strategy of the EU relate to the following areas:
Maintaining open markets

Safeguard free access and fair competitive conditions throughout the global shipping market.

Acting against market access barriers.

Acting against unfair competition.

Forging international agreement on the application of competition principles in maritime transport.

Safety

Increased port state control through operational links with other third countries.

Increase responsibility placed on the cargo owner to use quality vessels and operators.

A safety policy based on internationally agreed rules.

Common rules for community ship registers.

Competitiveness of the EU shipping sector

Promote maritime training programmes to attract young people to the profession.

Foster maritime Research and Development (R&D) including high technology in safety and environmental protection and human resources.

Allowing greater individuality to member states to develop individual solutions in terms of favourable corporate tax schemes, relief on personal tax and social security payments to encourage use of EU crews and promotion of maritime R&D.

The port state control measures emphasize and encourage the use of quality vessels and operators. The proposed policy also suggests that strong support for a free market with free competition should go together with measures to regulate markets and support schemes to be developed by individual
governments to make European shipping companies more competitive. The implementation of these policies will be observed by all maritime nations and will have an impact on the shipping policies being developed by other countries.

The United States of America (USA)

The United States of America (USA) is the largest market place in the world. The carriage of its foreign trade is open to commercial competition from both national and foreign shipping companies. The United States of America advocates principles of free and fair competition in international shipping and is opposed to cargo sharing agreements. The open nature of its shipping markets go a long way in establishing “the free market” as an important principle in international shipping policy. In practice, however, there are areas where shipping policies and strategies of the USA do not appear to match the ideology and principles of the free market.

The basic principles of the United States of America shipping policy is to achieve the following objectives:

- Increase the competitiveness of shipping serving its international trade.
- Enhance the competitiveness of its national fleet to serve the interests of consumers by providing low cost and efficient shipping services.
- Maintenance of a national merchant fleet able to meet national security needs.

Competitiveness of shipping services

The policy of ensuring competitiveness which applies to all industries has been implemented in the United States of America through a series of legislative enactments being with the Sherman Act of 1890\(^\text{10}\). This main anti-trust legislation which forbids the restriction of trade contains the following important principles:

\(^{10}\) “Antitrust Laws” refer to the Act of July 2, 1890, as amended; the Act of October 15, 1914, as amended; the Federal Trade Commission Act as amended, Sections 73 and 74 of the Act of August 27, 1894, as amended; the Act of June 19, 1936, as amended, the Antitrust Civil Process Act, as amended and amendments and Acts supplementary thereto [section 3, OSRA 1998, USA].
Contracts/agreements/understandings between two or more persons/companies restricting free competition in the market are illegal;

Monopolizing of trade is prohibited.

The structural organization of the shipping industry with its monopolistic tendencies, particularly the liner conference system, required special provisions having to be made for the shipping sector. This has been done over the years through several Shipping Acts - the Shipping Act of 1916 and 1984, and most recently the Ocean Shipping Reform Act of 1998.

The Shipping Act of 1984 and the new Ocean Shipping- Reform Act of 1998 provide a good insight into development of trade and service related shipping policies in the United States of America. The Shipping Act of 1984 contained three policy declarations:

To establish a non-discriminatory regulatory process for liner services to and from the United States with a minimum of governmental intervention and regulation;

To provide an efficient and economic transportation system that is in so far as possible in harmony with and responsive to international shipping practices;

To encourage the development of an economically sound and efficient United States - flag liner fleet capable of meeting national security needs.

The Shipping Act of 1984 retained many of the provisions of the 1916 Act, but included changes which facilitated approval of the conference agreements and broadened the anti-trust exemption that approval bestows. Among the changes applicable to the conference system, broadening of carriers’ anti-trust immunity, intermodal authority, mandatory independent action (I/A) and service contracts (S/C) were the most significant. The impact of the Act has been far reaching in the liner shipping industry, particularly on the structure of the industry’s organization, rate levels, and its competitive environment.
The practical impact of the Shipping Act of 1984 is briefly discussed below:

The simplified approval procedure relating to agreements enabled carriers to enter into cooperative agreements between themselves more easily. This led to the filing of agreements between conference lines as well as between conference lines and independent lines to be filed with the Federal Maritime Commission (FMC).

Rates and terms of services have become the contractual agreements between individual carriers and shippers. These are known as independent action (I/A) or service contracts (S/C). Thus the negotiating power of the shippers has been enhanced.

In this regard, the two following points are worthy of note:

A conference agreement must provide that any member of the conference may take independent action on any rate or service item required to be filed with FMC; e.g. an individual rate may be agreed upon with a shipper.

Service contracts between conference (carriers) and shippers have been authorized. A service contract contains a commitment by the shipper to provide a minimum quantity of cargo over a fixed time period, and the other party commits himself to a certain rate (or rate schedule) and a certain service level.

The Act authorized various forms of cooperative arrangements like joint service/consortium agreements as well as sailing and space charter agreements.

The Act triggered rate reductions in trades through numerous offers of independent action or service contracts to shippers and thus has undermined the collective strength of shipping conferences.

When one of the conference lines eager to increase its market share took independent action (I/A) to set rates lower than the conference, tariff rates, all the remaining lines had no option but to follow suit to match or undercut the rates. This tendency has exerted downward pressure on freight levels.

The powers of the FMC have been broadened in order that it could take counter measures in case of discrimination of United States Flag vessels. The following are two examples:
The FMC and the Trans-Atlantic Conference Agreement (TACA) agreed to a settlement of the proceedings against the conference.

The FMC opened an investigation into port restrictions and requirements in Japan concerning the prior consultation system of mandatory discussions and approval of shipping operations in 1995. A fine was imposed on three major Japanese shipowners in 1997.

The most significant contribution of the Shipping Act of 1984 has been to facilitate the creation of new types of agreement among carriers and to clarify the scope of carriers’ anti-trust immunity and ensure its predictability.

Debates bringing about substantial change to the Act has been going on since 1992 and the Ocean Shipping Reform Act of 1998 (OSRA) was introduced in October 1998. The Act came into force on 1st May 1999.

The OSRA brings in a further policy objectives as follows: “To promote the growth and development of US exports through competitive and efficient ocean transportation and by placing a greater reliance on the market place”.

The ocean-shipping business will be largely deregulated, setting off a scramble among shipping lines to lure customers with discounts of rates. Container shipping lines for the first time will be able to sign individual, confidential contracts with importers and exporters. The competition to sign up such customers is expected to greatly loosen the grip of the shipping conferences that have legally set rates for ocean shipping for more than a century.

Main changes of the Act would be as follows:

Shipping conferences will not be allowed to hamper the negotiation of service contracts which are the contractual arrangements between individual carriers and shippers.

(The reason is that shippers prefer to deal with individual lines rather than conferences because they are reluctant to reveal commercially sensitive information to a group of carriers. They prefer to develop a long-term partnership with selected carriers to minimize the risk of disclosing sensitive information to their competitors).
With regard to service contracts and agreements, the FMC would require information relating to five aspects only. These relate to the origin and destination port ranges, the commodity, minimum volume and the duration of the voyage.

Shippers and carriers would thus no longer have to disclose essential terms of service contracts and agreements such as line haul rate and service commitments.

Through amendment to Section 19 of the Merchant marine Act of 1920, the FMC will have the right to investigate and take action against foreign carriers on pricing practices employed by owners, operators, agents or masters of vessels of a foreign country.

The regulatory powers of the FMC have always been a matter of great interest to all countries involved in shipping. The role and powers of the FMC was subject to debate in 1995 with the introduction of the Ocean Reform Bill. The bill sought to abolish the FMC and transfer some of its functions to the Department of Transportation. This issue appears to have died a natural death and the regulatory powers of the FMC are in fact being strengthened.

**Measures to develop national merchant fleets**

The United States of America shipping policy is characterized by its commitment to the principles of free trade and services and objection to protectionist measures. Its policy to maintain an adequate national merchant marine, however, is supported by strategies which use subsidies and cargo preference schemes directed at the national shipping fleets. This inconsistency is the result of the dilemma which is faced not only by the United States of America but all countries. The developing countries in the ESCAP region have acknowledged if not the ideology, at least the practical advantages of free trade and the need for competitive shipping services provided by overseas shipping lines. On the other hand, countries in the region also wish to develop their national shipping capabilities. The rationale for the development of a national merchant marine in the United States of America is primarily defence oriented. The rationale for the development of national fleets by the developing countries include factors other than defence. Developing countries have seen through experience that the presence of a national merchant fleet gives rise to other related industries. They also wish to maintain a presence in the carriage of foreign trade generated by the country. These are legitimate interests and the tangible and intangible costs of furthering these interests should be assessed.
The strategies adopted by the United States of America, may provide countries in the ESCAP region with some models that could be used in the development of their own shipping policies.

The basic elements of the United States of America subsidy programme consist of Constructional Differential Subsidy (CDS) and Operating Differential Subsidy (ODS) introduced in 1937.

**Fiscal support measures**

*Constructional Differential Subsidy (CDS)*

CDS was aimed at developing the shipping industry as well as the shipbuilding industry. An American shipping company which intends to build a vessel for the purpose of operating in foreign trade was able to obtain a CDS subsidy for the construction price at an American yard. The purpose of the CDS was to cover the difference between possibly higher construction costs at an American yard compared with costs of a foreign yard.

The CDS was an important instrument for the development of the shipping industry up to the fiscal year 1981 but has since been suspended due to the policies of budgetary constraint.

*Operating Differential Subsidy (ODS)*

This regime is granted to some United States of America flagged vessels operating in the carriage of essential foreign trade, to place US-flag vessels’ operating costs on parity with those of foreign competitors. Subsidy is paid pursuant to 20-year ODS contracts between the United States of America Government and the operators, who agree to equip their vessels with defence-related features and also to make their vessels available in time of national emergency.

In the 60 year period between 1937-1997, the aggregate amount of subsidies provided to United States of America flag operators have exceeded US$ 10 billion.
Maritime Security Programme (MSP)

The MSP established in 1996 provides operating assistance to United States of America flag liner vessels serving in foreign trade on the condition that the participating carriers provide intermodal sealift support in time of war and national emergency. The 10 year programme can provide funding of up to US$ 100 million annually.

Table 2.3: Maritime Security Programme Participants

<table>
<thead>
<tr>
<th>Company</th>
<th>Type of Vessels</th>
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<tbody>
<tr>
<td>American President Lines, Ltd.</td>
<td>9 containerships</td>
</tr>
<tr>
<td>Central Gulf Lines, Inc.</td>
<td>1 LASH (barge carrying ship) 2 roll-on/roll-off vessels</td>
</tr>
<tr>
<td>Crowley Maritime Corp.</td>
<td>3 container/roll-on roll-off vessels</td>
</tr>
<tr>
<td>First American Bulk Carrier Corp.</td>
<td>2 containerships</td>
</tr>
<tr>
<td>Farrell Lines Incorporated</td>
<td>3 containerships</td>
</tr>
<tr>
<td>Lykes Bros. Steamship Co., Inc.</td>
<td>3 containerships</td>
</tr>
<tr>
<td>Maersk Line, Ltd.</td>
<td>4 containerships</td>
</tr>
<tr>
<td>OSG Car Carriers, Inc.</td>
<td>1 roll-on/roll-off vessel</td>
</tr>
<tr>
<td>Sea-Land Service, Inc.</td>
<td>15 containerships</td>
</tr>
<tr>
<td>Waterman Steamship Corp.</td>
<td>4 LASH</td>
</tr>
<tr>
<td>Total</td>
<td>47 vessels</td>
</tr>
</tbody>
</table>

(Source: MARAD 1997 Annual Report)

MSP is expected to be gradually replace the ODS when it expires.

Cargo preference schemes

Shipping policies in the United States of America have traditionally utilized cargo preference/reservation schemes to support the national fleet. The schemes relate to cargoes that are directly or indirectly financed and generated by the government. This means that only a minor part of the seaborne transport of the United States of America’s foreign trade is covered by preferential legislation. The present system of cargo preferences can be divided into the following three types:
(i) Preference for United States vessels in the carriage of various forms of Government financed cargoes and Alaskan Crude oil.

The Cargo Preference Act of 1904, the Cargo Preference Act of 1954 and the Public Resolution 17 of the 73rd U.S. Congress provide the legislation for the preference of United States of America vessels for government financed cargoes.

With regard to the carriage of Alaskan crude oil, the preference of United States of America vessels is contained in one of the clauses in the instrument that lifted the ban on the export of Alaskan crude oil in 1995.

The case of the Alaskan crude oil amounts to the introduction of a new cargo reservation policy and is a major departure from the establishment of free shipping markets. The OECD has expressed concern over this policy which is in clear conflict with OECD common practice on shipping. The OECD common practice is based on the policy of freedom in shipping and prohibits preferential treatment of vessels registered in one's own country.

The United States of America policy also appears to contravene the negotiations on maritime transport services contained in the declaration of the WTO Marrakesh Ministerial Conference in April 1994. The decision states that no government should adopt any measures that may affect trade in maritime transport services while the WTO negotiations (through NGMTS) are suspended.

Item No. 7 of the decision requires that member countries should refrain from any measures that would affect trade in maritime transport services, unless the measures were in response to measures applied by other countries or directed at improving the freedom of maritime transport services. The decision also precludes governments from adopting measures that would improve their negotiating position and leverage.

(ii) Bilateral cargo sharing agreements: the bilateral maritime agreements with the People’s Republic of China, provides for parity in the carriage of bilateral liner cargo. These agreements which cover import and export of commercial cargoes are directed to ensure that the vessels of each nation carry at least one-third of such cargoes.
Coastal trade is exclusively reserved for American built, American manned and American crewed vessels (cabotage).

**Recent trends in shipping policy**

The international focus on liberalization and the establishment of the WTO will have a profound effect on shipping policies being developed by countries in this region. The international shipping environment is subject to rapid changes and shipping companies are locked in an intense internationally competitive business environment.

The shipping market has become global. Global carriers are constantly restructuring the shipping market according to their business strategies. They are the market shapers.

The liner shipping conferences which operated between specific trade routes between groups of countries have weakened. The dispute settlement machinery which was effective in balancing the relationship between liner conferences and the exporters and importers appears to be no longer applicable to the global carriers and alliances. Countries in the ESCAP region must thus give serious thought whether the dispute settlement mechanism, should move from the national arena to a global forum such as the WTO.

Some of the recent trends in shipping policy are noted below.

- **Deregulation and liberalization**

  Countries have eased regulations on private shipping companies participation in the carriage of overseas trade and have made provision for the following:

  - allow foreign carriers access to carry overseas trade;
  - transform a licensing system of sea going vessels/operators to a filing system;
  - review regulations and practices applying to the provision of shipping services and bring them in accordance with international practices.
Removal/relaxation of restrictions on foreign investment

Restriction on foreign investment in shipping related business including shipping agency and ocean freight forwarding services are being gradually removed.

- Privatization of public sector shipping lines

Move towards increasing private sector participation in the government owned and operated shipping lines. Proposals considered vary from sale of shipping line to national or overseas operators to the formation of joint ventures or consortiums.

Although governments are willing to accept the poor performance of public sector shipping companies and the need to infuse capital and management expertise, governments still have reservations when considering the formation of new public/private sector partnerships.

Abolishing of cargo reservation schemes

Cargo reservation schemes that were originally introduced to promote the national shipping lines have been drastically reduced or abolished. A few countries that still practice cargo reservation schemes are in the process of undertaking a serious review.

Flexibility of crew nationality requirements

The employment of foreign crews are being increasingly allowed. This is also taking place in developing countries which have a scarcity of qualified national seafarers.

- Maritime cabotage

Countries are reviewing the cabotage systems taking into account the costs involved.