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CANADIAN TRANSPORTATION RESEARCH FORUM
LE GROUPE DE RECHERCHES SUR LES TRANSPORTS AU CANADA

20th ANNUAL MEETING

PROCEEDINGS

TORONTO, ONTARIO
MAY 1985

SHIPPING, DECEPTION AND POLITICS 1.

Paper presented at the Twentieth Annual Meeting of the Canadian Transportation Research Forum on May 29,1985

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INTRODUCTION

Like a captain's chair, the shipping industry stands on four legs;

1. Ship Operations
2. Finance
3. People
4. Politics

This paper argues that politics is the most important and least understood of the four. It also forecasts that government supported National Flag Ship Lines will fade away as their evils become apparent to the people who pay for them,chiefly farmers, miners, factory workers, and forresters.

This is not an attack on third world attempts to solve their maritime problems. The saddest tales concern Australia, France, New Zealand, Spain, Italy, Ireland and the USA. This is proof that a government inspired line which needs subsidies and protection works against the interest of its people.

Every ship at sea is touched by political facts. She is Liberian if her true owner decides not to fly the flag on his passport. She was built in a subsidized rich country yard, or elce in a low cost Asian yard. If she has a US operating subsidy most of her crew wages are paid by the government. If her cargo is for Venezuela, it must be vetted by a complex flag preference system. If her owner is a Bermuda corporation , there are tax benefits. If she carries the right charts, navigation gear and officer licenses, she satisfies IMO (an agency of the United Nations) conventions and can pass port state inspections. Eighty percent of the loan that financed her was probably guaranteed by some government to assist a politically sensitive shipyard. If she is headed down the African coast her cargo must bear the right rubber stamp showing that it is in tune with the UNCTAD Code of Conduct as interpreted by the official gent weilding the stamp.

Most important, about a third of the ships at sea are owned by governments. In this category fall fleets of the Russians and their affiliates, big lines such as LLoyd Brasiliero, and the national shipping companies of Australia, India, New Zealand,France, Venezuela and Argentina.One party governments in Africa, Ghana and Guinea for example, own most of their industries including ship lines.

A container ship is part of a system which includes ports, railroads, truck lines, seaways and rivers. Government grants and loan guarantees build most ports, especially in Canada .The Canadian National Railroad, a Crown Corporation might like to own a Montreal based ship line. Liberal Party appointees in the Canadian Transport Commission may well say yes. An American shipping company , APL (American President Lines) runs trains across the USA via Los Angeles, but asks the US Government to say no when the Port of Seattle tries to do the same thing.What would happen if the Polish Ocean Line tried to run a train across Texas? What kind of ship lines can integrate with the Trans Siberian Railway, or will NVO's (non vehicle operators) solve the problem?. Being integrated and intermodal, container ships touch the political heart of every nation.

3.

TWO POLITICAL SYSTEMS

A Toronto ship owner can choose between two political systems if he decides to join the "salties" and go into deep sea foreign trades. If he selects the Canadian flag, he will have trouble avoiding the Seamen's International Union. On a standard Seaway type bulk carrier his officers and crew will cost four million dollars each year. These will resist compulsory arbitration and insist on the right to strike. He will need ship plan approval by a classification society such as Lloyd's Register. In addition he needs to deal with a separate Canadian Ship inspection service run by the Coast Guard. Naturally he will pay Canadian Federal, Provincial and local taxes and amortize his ship over many years. An antique code of difficult maritime laws will govern his activities, and many of his disputes will be litigated in Canadian Courts. He will be pressed to build his ship in a Canadian yard. If he does not, he will pay a large import duty. These are samples,- an incomplete list of the things he must do under the his home flag.

If he decides against the Canadian flag, he can form a Bermuda ship owning corporation and fly a Flag of Convenience (FOC), say Liberian. Now his costs for a good Asian crew will be eight hundred thousand dollars. His excellent Korean built ship will cost about a third of the Canadian yard price, and he will pay no duties or taxes. To be insured and credible in the eyes of big customer corporations he will need ship plan approvals from a classification society, but not the Canadian Coast Guard.

These conveniences save money. A US flag ship will need about $30.00 a ton to carry grain to Europe. A free market ship will do the job for less than ten.. Some US grain AID cargoes must by law (PL 480) be carried under the US flag. If Canada had similar laws, our farmers would also have their rates tripled.

Opponents of convenience flags argue that they lead to unsafe ships and abuse of seamen. The opposition is led by rich country seamen's unions, and the United Nations delegations of Russia, her affiliates and those of many Third World nations. They have mounted a series of efforts to "phase out" Flags of Convenience (FOC's). However the campaign is running out of steam. FOC's are here to stay. The opposition will now settle for reform.

If our Toronto owner turns his back on the Canadian flag he still must live with a well developed international political/ regulatory system. Stung by criticism, Liberia has tightened conditions for the use of her flag. The Liberian Maritime Administration, largely managed in New York City, is influenced by big cargo owners(oil, steel, aluminum, grain, coal,ores and chemicals). These insist that unscrupulous ship owners be weeded out, and that an inspection system have real teeth. Owners banished from the Liberian flag have other options, in Cyprus for example.

At sea ships are ruled by international conventions on safety of life (SOLAS), pollution and navigation. In ports a new system is gaining strength. Known as "Port State Control", this involves inspection of ships and their documents by host ports eager to guard against sub standard vessels. Ship owners who don't pay their bills are often caught in an international data exchange system that grows more sophisticated every day.

In addition a UK based labour organization,the International Transport Workers Federation (ITF) has its own "de facto" disciplinary system. It issues blue cards to FOC vessels that meet its standards on crew wages and working conditions. Enforcement rests on cooperation with sympathetic labor unions (mostly port workers) in each host port.

The Toronto owner can select the courts in which he litigates disputes with his customers. Not eager to deal with Liberian or Panama courts, he can stipulate in his freight contract that certain issues will be arbitrated in New York and others decided by the courts and laws of the United Kingdom. No sensible cargo owner will deal with a ship that is not "in class", that is inspected and approved by the American Bureau of Shipping (ABS), Lloyds or another good classification society.

There is a third option for ship owners who reject their home flag, but worry about FOC's. Great Britain welcomes foreign owners, and the Union Jack was once popular with Europeans and Americans. In 1982 two fifths of the British fleet was beneficially owned abroad. Singapore, Hong Kong and South Korea and Taiwan are not FOC nations. However, through the use of bare boat charters, special contracts and other devices their flags are available. Evergreen, one of the giant container ship owners, is a Taiwan line. But the press suggests that there is Japanese money in the background. A ship built, manned, and flagged in South Korea can match any FOC for efficiency and low cost. Though far below rich country wage levels, her officers and crew are handsomely paid by Asian standards.

The variations are endless. It is normal for a Canadian corporation to contract with the Bermuda office of a Hong Kong ship owner for movement of Brazilian cargo to Spain on a Liberian ship with Packistan officers and a Philippine crew. The ship could have been built in Korea and, financed in Geneva. Such a package deal would be routine for a London ship broker, though the parties might seek advice from a New York lawyer on tax and liability questions.

Since World War II the heart and soul of shipping have changed. General cargo ships once spent most of their time in port and most of their money on people. Now longshoremen have priced themselves out of jobs, replaced by container cranes and computer based automated terminals. A fifty man ship crew was normal, but the standard is twenty five now. It will be fifteen in a few years. The Japanese are experimenting with crewless ships. Many of these will be at sea in the year 2000.

In the good old days a politician could say that shipping creates jobs. Today according to a World Bank Staff Working Paper (No. 502 by H. Hansen Nov. '81)

> "... shipping is, despite large variations, a relatively capital intensive industry in terms of capital cost per job." (3.36)

> "The net (unrevalued) fixed assets of the Shipping Corp. of India in 1978 was about $58,000, as compared with an average of $5,000 per employee for 22 other major Government of India undertakings." (3.42)

A new containership will cost about sixty million dollars and produce about thirty jobs.- two million dollars per job. Most other industrial investments produce ten or fifteen times that number off jobs for the same capital outlay. Shipping has a negative impact on employment because it takes large sums of money away from labour intensive industries.

No one knows where the size limit will be for fourth and fifth generation containerships. Evergreen and the United States Lines have in 1985 begun express round world services with massive (3000 to 4000 TEU) ships designed to barely squeak through the Panama Canal. The fourth ship generation will be too big for Panama, but at the Suez maximum. These will ply the "Horseshoe Trade ", that is from the US/Canadian Atlantic Coast to Europe, the Mediterranean, Suez, Asia, Japan, the US West Coast and return. Like tankers, containerships can lower their costs per ton carried by going up in size. Crew, capital and management costs do not go up in porportion.

With these big ships come sophisticated feeder ship systems and marriages with land carriers. The American President Lines owns and runs trains between Los Angeles and Chicago, also New York. That gives them a transport system that links most of the USA (and central Canada) with Asia and the Far East all moving under one management at a cost of about two cents a ton mile.

Once shipping people could tell politicians that they were a " Fourth Arm " of the national defence system. Merchant ships fought well in both world wars. But the modern military machine needs small fast versatile ships that can service the fleet and go into shallow draft ports. Containership monsters, tankers and bulk carriers are not what the armed services want. They are too specialized and too slow.

Norway, England and Greece were homes of the most brilliant shipping men. Now the bright stars are Japanese, Korean and Chinese. The center of world shipping has, in one generation, shifted from the Atlantic to the Pacific.

Shipyards on the Tyne, in Piareus and Oslo built great and profitable vessels after World War II, but now government subsidies protect them from bankruptcy. There is a surplus of ships in every category, shipping rates are depressed , and this will not soon change. Shipyards and steel mills are filled with votes. Political leaders can only close them in slow painful stages. But close they must because the Japanese and Koreans build cheaper better ships, and have sixty percent of the orders.

A hungry shipyard may not hesitate if some Minister of Transport mentions a "commission" for his Swiss numbered bank account. Such deals have launched too many ships. Worse still is the easy money that flows to any brave soul who wants to be a shipowner. An agreed limit was eighty percent for eight years at eight percent interest, but better deals are easy to find. In today's climate almost any " Joe " in the street can be a shipowner.

Salen in Sweden, Hansa in Germany, Hellenic in Greece, these were once solid rocks in the European shipping scene. They are now bankrupt. In the USA American Export, Grace and a half dozen other subsidized stars are gone via sales, mergers, and section eleven of the US Bankruptcy Act.

POLITICAL PHILOSOPHY
Adam Smith vs Ed Broadbent

Political philosophy is rarely discussed in shipping circles. But just beneath the surface lies the classic struggle between protection and free trade, between Harold Laski socialists and Thatcher/Reagan/Mulroney capitalists. Today, like break dancing, the current fads are deregulation, private enterprise and free trade. The US government is trying to sell Conrail, its northeastern railway complex. Mrs. Thatcher seeks a buyer for British Airways and Brian Mulroney will sell shares in Air Canada. Australia's Labor Party Prime Minister , Bob Hawke wants to sell The Australian National Line. Even in France and Spain, where socialists rule, there is a hold on government takeovers.

The pendulum swing carries with it all transport modes . US airline deregulation has inspired a house cleaning inside big airlines such as United and American. Labor costs are down and management is sharper because the government has opened the game to People's Express, and a host of non union newcomers. Sir Freddy Laker terrified the European establishment with his threat to compete on the Continent. There inefficient government airlines cling to inflated but protected fares.

Sadly there is a second stage as the pendulum swings back to something economists call ologopoly. Already many of the upstart US airlines have gone broke.In 1984 the big five (United,American Delta,Northwest and US Air) had about half of US passenger miles, but they had 94% of the profits. Leaner and meaner, they are ready to eat the newcomers including People's Express. There is a pattern. Fifty years ago in free enterprise America there were two dozen auto makers. Today there are four, and three of these are struggling. From a mass of airplane builders there are only three big time survivors, Boeing, McDonnell Douglas and Airbus. These openly collude to stay alive.

9.

Like passengers on People's Express, containership customers are happy now. Rates are low on main lines where most (80%) of the traffic moves. These main lines cover much of the developed world, the Americas, Europe,Asia,Japan,and Arabia, but not South America or Africa.The big operators of third generation superships (Evergreen and US Lines) and their rivals are in the early jungle warfare stage. All weapons are fair game including any tax breaks,subsidies, preferences or cheap loans that may be lying around. Overstaffed government lines and small timers will be easy prey. After that comes the real shakeout when old timers like Maersk, Hapag-Lloyd, Sea-Land, Canadian Pacific, Wilhelmsen, Tung and Pao must either go it alone or consort.

The charms of maritime ologopoly were neatly displayed in the recent gyrations of US Defence Department ocean rates. In 1982 an outsider American Coastal Line (AMCO) challenged the established US Lines and Sea-Land. AMCO managed to capture 67 percent of the enormous the US Military Sea Lift Command tonnage. Promptly Sea-Land reduced its rate (USA-Europe) from $49.15 per measurement ton to $24.45. Later the US Lines quoted $16.74. Today AMCO is gone and the establishment is again in command.

The current leap forward in container shipping is partly a product of Ronald Reagan deregulation. The USA generates about a third of the world's package freight tonnage. Under the US Shipping Act of 1984 the lines gained something called "single factor intermodal pricing". This allows the American President Line (APL) to quote one rate Chicago to Singapore (via Los Angeles) and do the job in one system which APL controls all the way. The Russians are eager to promote their Trans Siberian Railway, and the Mexicans dream of a Trans Isthmus land bridge starting at Coatzacoalcos .

10.

In Canada there is an unanswered political question about Crown Corporations. The Canadian National Railroad thought it could prosper by buying CAST, a Montreal based ship line. But the CNR is the only rail link between Halifax and North America. While enjoying such a monopoly, can it place its chips on a Quebec port? If it does, should Canadians not expect that the monopoly be surrendered by giving the Canadian Pacific free access to Halifax? Logic will overflow in this debate, but politics will play a part.

Politicians seem less interested in bulk cargo trades where success flows with skill. Scandinavian ,British and Greek owners thrived in the early post war days because they ventured into greater sizes and novel ore/oil combinations. Their shipyards built good bulk carriers at modest prices. They were great ship operators and knew their market well. Today in the Pacific Japanese cargo owners bank Hong Kong ship owners who incorporate in Bermuda and fly FOC flags. The game has lossened up. There is abudant ship managenemt talent in Hong Kong. Singapore Asia-Pacific yards have most of the building business because they do a better job. This raises a political concept which haunts Democrats in the USA, Liberals in Canada, and the Labour Party in England.,-something called "Industrial Strategy".

Every nation cannot have steel mills, a Silicon Valley, a banking center and an oil refinery. There must be selection. Worse still, things change. Smokestack industries in Pittsburg and Gary, Indiana, once enjoyed cheap handy raw materials and competitive labour forces. Today the Mesabi Ore Range is tired,and third world labour is hungry. Eventually even politicians must face reality. Gary Hart and some Cambridge, Mass. liberal thinkers toyed with this subject during the primary days. But they dared not be specific about their new ideas. The Democrats nominated an old style "New Dealer" who promised to protect the auto workers.

Why is it that nations with no maritime skills still want to have their own merchant fleets? Why would Canadian farmers agree to having their ocean freight rates multiplied by three? The best answer involves balance of payments.

BALANCE OF PAYMENT DECEPTION

There are three levels of accuracy in balance of payment discussions. The lowest is practiced by those who claim that changing a vessel's flag transfers a hundred percent of her revenue to the home national account. On the surface this seems right , and many people beleive it.

At the second level one admits that eighty percent of a ship's expenditures are constant and not changed by a flag transfer. A Chilean named Brown (World Bank consultant) devised a simple formula for balance of payment score keeping. He noted that about 30% of liner costs are for stevedoring (say in Rotterdam) inland transport, and port expenses. These are not influenced by vessel flag. Another 25% is for capital, - the purchace price for the ship plus finance costs. The best and cheapest ships are built in Japan and Korea, while most money is borrowed in big US/UK/European banks, or from rich Arabs. For a nation without finance or competitive shipyards, again no gain. Fuel is 20%, purchaced where it is cheapest and best. Insurance, say 7% usually comes in the London market. When all cost elements are looked at separately, only two offer balance of paymment gains, for a total of about twenty percent. This covers management and crew.

At the third and only honest level the costs of subsidy and protection are included. Unbiased maritime studies are rare jewels. Third level honesty was evident in a 1984 report of the US Congressional Budget Office. (U.S.SHIPPING AND SHIPBUILDING-TRENDS AND POLICY CHOICES). The budget office looked at a proposal to reserve twenty percent of bulk cargo and thus to induce commercial orders for about 20 U.S. flag ships per year. The price would be three to four billion each year, this to come out of the pockets of farmers, miners and forresters. They concluded;

> "..it seems doubtful today, however, that the cost of supporting the U.S. flag merchant marine could be justified solely by commercial considerations... The substantial gap in costs between U.S. and foreign operators must be filled by some kind of subsidy or cargo reservation program for the U.S. operators to survive. The costs of these programs are borne either by the taxpayers or by the economy through higher prices arising from increased shipping costs."(page xvi)

When the cost of protection is added shipping gains (say 20%) vanish. This is true because a quota or percentage plan gives some part (say 50 or 60 %) to non national ships. With rates artificially held up, the foreigners enjoy windfall profits at the expense of the host country. Several U.S. flag lines have enjoyed this happy situation in Latin American trades where tight 50-50 deals are in force.

Venezuela offers a good example. Her general cargo freight payments are about 600 million dollars (US) a year.(.04% of 15 billion). Shipper studies indicate that rates would by 33% lower (and services better) if Venezuelan trades were completely open. This means that Venezuelans are paying two hundred million dollars more than they should. .(one third of their annual bill) If, per the 40-40-20 Code, outsiders carry 60% of Venezuelan general cargo, 120 million of these overcharges go overseas.- a negative entry in the balance of payment account. That is a high price to pay for the twenty million that the Venezuelan Line may contribute on the positive side.

The World Bank staff working paper (No.502) suggested that a nation should hesitate if its shipping enterprise could not earn profits. The author was too polite to say that government shipping lines are famous for cooking their books. The opportunities are great. Private lines pay taxes, but their government rivals pay less (or none). Ship values can be juggled; preferences reduce sales cost; overhead is buried in operating accounts or carried by another government agency. Subsidies are treated as revenue, and loans carry low (or zero) interest rates. It would be difficult to find a government shipping line that earns a profit under strict commercial accounting standards. The Shipping Corporation of New Zealand offers an entertaining example. In 1982 they lost about five million dollars (NZ) on their service between Aukland Tahiti, The Cook Islands and Niue. An efficient service could easily break even in that trade without raising rates. However, the loss was charged as "Foreign AID" to the Cook Islands. Thus on the books the service showed a small profit.

Canadians are often told that they must indulge in cargo preference because "everybody is doing it". This is not supported by many facts. While most OECD nations have signed the UNCTAD Code, they have in "The Brussels Package" said that they will play by their own rules. The USA, Canada, Australia and New Zealand did not sign up. Since the Code touches only conference cargo, outsider shipping is not covered. This means that it influences about seven percent of general cargo and no tanker or bulk business. The greater threat comes from the 50-50 deals that prevail in US-Latin America trades. These are being questioned on both coasts of South America (especially in Brazil, Argentina and Chile), and the Reagan administration would dearly love to get rid of them. Washington has refused to make similar deals in the Philippines and China. The French protect part of their coal and oil import movements, and the Americans protect some AID grain exports. However, more that ninety percent of bulk cargo and tanker shipments move free of preferences.

14.

CONCLUSION

This is a plea for honest numbers. Shipping in the post war years has become more visible, - thanks to a host of good papers and magazines. Everywhere people are bolder in questioning subsidies and protection. South Korea was once a champion of restrictions, but recently Choi Hoon, Director General of the Korean Maritime and Port Authority told Seatrade; (4/84)

> "A system of strong protectionism is a sign of weakness in shipping and disturbs the world pattern."

That same issue found Alhaji Banda, Chairman of the OT Africa Line wondering about West African capital expenditures on shipping,and concluding;

> "Has it been worthwhile? There is a growing feeling that it has not."

These remarks are modest compared to some of the things that Brazil"s Minister of Transport (Cloraldino Severo) is saying as he wades through the tangled finances of Sunamam, his maritime administraton.

The debate is more open and fair.