Asian Shipowners' Association

Submission of the Asian Shipowners' Association
In Response to the Hong Kong Competition Commission's
Proposal to Issue a Block Exemption Order in Respect of Vessel Sharing Agreements

The Asian Shipowners' Association ("ASA") appreciates this opportunity to comment on the Hong Kong Competition Commission's 14 September 2016 Statement of Preliminary Views, with respect to the liner shipping industry's request for a block exemption for all types of liner shipping agreements. Therein, the HKCC has proposed to exempt Vessel Sharing Agreements (VSAs) from the Competition Ordinance, but not to extend an exemption to Voluntary Discussion Agreements (VDAs). ASA strongly supports the HKCC's tentative decision with respect to VSAs, but urges the Commission to seriously reconsider its proposal with respect to VDAs for the reasons set forth below.

The ASA is an organisation of the national shipowners' associations of Australia, China, Chinese Taipei, Hong Kong, India, Japan, Korea and the Federation of ASEAN Shipowners' Associations comprising Singapore, Indonesia, Malaysia, Myanmar, the Philippines, Thailand, Vietnam and Brunei. The ASA membership together is estimated to represent approximately 50% of the world merchant fleet today. The role of the ASA is to promote the interests of the Asian shipping industry and express its views on key issues affecting this industry, such as the importance of continued exemptions for all types of cooperative liner shipping agreements in Hong Kong and other international shipping trades.

Liner shipping companies are the engines of international trade, providing regularly scheduled ocean transportation service at key ports for essential manufactured goods, raw materials, and foodstuffs worldwide. Hong Kong in particular relies heavily on container shipping services for its ability to participate in international trade. Despite a relatively small population base, Hong Kong has historically been one of the world's leading countries in terms of overall port traffic. Importantly, both VSAs and VDAs have existed in Hong Kong for decades. During this time, Hong Kong has maintained its position as a premier international maritime centre and trans-shipment hub in Asia. For the ocean carrier members of ASA, participation in both of these types of agreements has helped to mitigate wild market instability, provided a forum to exchange and review market data led to more investment, expanded service options, provided access to more ports and sailings, resulted in significant cost savings, greater efficiency, and environmental benefits. For shippers (the carriers' customers), this has meant more service to more ports on better ships at lower costs. In short, VSAs and VDAs have unique and complimentary benefits, and both helped Hong Kong remain a highly competitive world maritime centre. The efficiencies from both of these agreements have helped all Hong Kong consumers, and the wider economy as a whole.

But the HKCC's proposed exemption for only VSAs and not VDAs threatens to jeopardize these well-recognized benefits. Maintaining consistent, quality service is a significant challenge for liner shipping companies. International shipping is a particularly challenging industry. The combination of high capital and fixed costs with unique supply and demand trends in the liner shipping industry can lead to both prolonged depressed rates and highly fluctuating rates, which can

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have a debilitating effect on service levels. As carriers have struggled to maintain sustainable rates, cost containment and efficient operations have become paramount. In order to moderate the extreme market volatility and promote more efficient use of vessels, the liner shipping industry developed a business model of cooperative arrangements many years ago. This is and has been the prevailing business model in virtually all major trading nations. As such, the majority of countries in Asia have extended broad exemptions to both VSAs and VDAs in recognition of their unique benefits. Indeed, these types of exemptions are the international standard. As these countries have found, these agreements play a critical role in the ability of the industry to continue to make the investment of billions of dollars in ships, new vessel services, equipment, infrastructure, information technology, and other technological innovations needed to keep up with rapidly growing trade volumes.

The HKCC's proposal to not extend an exemption for VDAs would not just hurt the carriers, their customers, and Hong Kong consumers in general, but also presents great risks to the Hong Kong economy as well, which relies so heavily on international liner shipping. As the HKCC's Preliminary Statement of Views notes, Hong Kong in particular has a very high share of trans-shipment cargoes (i.e., they do not originate in Hong Kong). These cargo volumes are discretionary, and can be easily moved to other neighbouring ports in Asia if those ports offer a more attractive business climate. There are an increasing number of credible alternatives to Hong Kong, particularly in China (e.g., Shenzhen, Shanghai), which has for many years recognized and authorized carrier agreements to operate. Singapore is another competing alternative, and it just renewed its broad block exemption for both VSAs and VDAs. A similar exemption for all types of agreements in Hong Kong will ensure a favorable regulatory environment for ocean carriers' standard business model. This, in turn, will encourage carriers to continue making investments in shipping services to Hong Kong, rather than considering moving to other alternative gateways. Upsetting the status quo treatment of these agreements, on the other hand, forces carriers to re-evaluate whether Hong Kong's new regulatory climate merits their considering other service options instead of Hong Kong.

Respectfully, ASA submits that the HKCC has not fully considered the broad efficiencies that result from ocean carriers' participation in VDAs. First, agreements like VDAs promote rate and service stability, which in turn creates a positive environment for carriers to make investments in vessels, equipment, port facilities, and related infrastructure. As discussed above, these agreements mitigate destructive pricing that historically has plagued this industry. Continued investment in vessels and equipment will ensure that there is adequate capacity in the coming years to meet the growing needs of Hong Kong's importers and exporters, which in turn promotes the efficient distribution and transportation of goods. It also helps maintain high levels of direct and trans-shipment service to Hong Kong. With VDAs in place and serving Hong Kong for many years, ASA submits there has been no shortfall in capacity or service to meet the needs of its importers and exporters, and the HKCC has not cited any such issues in tis Preliminary Statement of Views.

Second, these agreements have not resulted in anti-competitive pricing behaviour or negative results in the many years that they have existed in Hong Kong and elsewhere throughout the world. As the HKCC is aware, all guidelines on rates and charges agreed to in VDAs are purely voluntary and non-binding. And the evidence shows that this is in fact true. While these agreements have promoted trade stability, they have not generally speaking resulted in carrier profitability. Container shipping has a long history of poor returns and thin operating margins. Indeed, the returns for carriers are often well below those of their customers. In the current market climate, many ocean carriers are losing millions of dollars a year, and have been for several years. Current market rates for shippers are at historically low levels, and are continuing to decline. Despite these very poor economic conditions, VDAs have at least helped carriers moderate prolonged depressed rates. Without these important agreements, the long-term impact on competition, and in turn the deterioration of carrier service, could be devastating.

In this regard, VDAs actually promote competition. As experience has shown, prolonged depressed rates can lead to fewer overall competitors, either because carriers are forced out the trade, forced out of business, or forced to consolidate. This would leave fewer carriers to make the necessary investments and offer service to shippers in Hong Kong. It would also ultimately result in higher transport costs for shippers if there is a lack of viable competition or adequate shipping capacity. The unique challenges of the liner shipping industry have been demonstrated just in the past year. The industry is already starting to see some consolidation as a result of the challenging economic conditions. The three major Japanese carriers (NYK Line, K-Line, and MOL) have recently announced they intend to merge their liner operations following a collective $500 million losses. In the last year alone, CMA CGM has acquired APL, COSCO has acquired China Shipping, and Hapag Lloyd is in the process of acquiring United Arab Shipping Company. In short, the industry is suffering and the overall number of competitors is declining. Failing to exempt VDAs in Hong Kong would only accelerate this negative trend.

Third, VDAs provide organizations to represent carrier interests in consultations with government regulatory bodies and with designated shipper organizations, which help facilitate important dialogue between these parties and address important trade issues. Absent these agreements, it would be considerably more difficult for shippers and carriers to address trade-wide problems or concerns.

As the above indicates, the benefits and efficiencies of VDAs are not academic or theoretical. There are over 100 years of experience in the liner shipping industry that proves VDAs support service enhancement and competitive options. Hong Kong itself has decades of experience with these agreements, with nothing but positive results for customers, consumers, and the economy at large. In contrast, there is no evidence that shows eliminating these agreements by not providing them a competition law exemption in Hong Kong would yield any benefits. Indeed, all of the available evidence shows that absence of VDAs leads to negative consequences for liner service and stability. Thus, ASA respectfully urges the HKCC not to upset the existing system that permits operation under these important agreements.

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For all of the above reasons, the ASA strongly supports the HKCC's proposal to provide a block exemption for VSAs, but impresses on the Commission to reconsider its views with respect to VDAs. The ASA appreciates the opportunity to convey the voice of Asian shipowners on this important issue, and remains at the disposal of the HKCC should it desire any further data or information.

Respectfully submitted
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