

Secretary

From: Elvin Tan [elvintan@asf.com.sg]
Sent: Monday, January 17, 2011 11:59 PM
To: Secretary
Cc: 'YS ASF YS '; 'ASF PO Sec Julieng'
Subject: FMC EU Study - Response to NOI from ASF
Attachments: ASF Comments to FMC EU Study.DOC

TO
Karen V. Gregory, Secretary Federal Maritime Commission

18 January 2011

FMC EU Study – Response to NOI from ASF

Dear Sir,

The Asian Shipowners' Forum (ASF) would like to submit our comments to FMC's Notice of Inquiry concerning the study on EU's repeal of Liner Conference Block Exemption.
Please find attached our comments for your reference. Thank you.

Best Regards,

Elvin Tan
Executive Officer, ASF

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18 January 2011

Federal Maritime Commission

Karen V. Gregory, Secretary
800 North Capitol Street, N.W. Room 1046
Washington, D.C. 20573-0001

Comments of Asian Shipowners' Forum On the Federal Maritime Commission's Notice of Inquiry Analyzing the European Union's Repeal of the Liner Conference Block Exemption

The Asian Shipowners' Forum ("ASF") appreciates the opportunity to comment on the Federal Maritime Commission's Notice of Inquiry ("NOI") concerning the effects on international liner shipping of the European Union's ("EU") repeal of the liner block exemption from EU competition laws that took effect on October 18, 2008.

The ASF consists of the 14 shipowners' associations of Australia, China, Chinese Taipei, Hong Kong, India, Japan, Korea and the Federation of ASEAN Shipowners' Associations comprising Indonesia, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Vietnam. The role of the ASF is to promote the interests of the Asian shipping industry and to express its views on key issues that affect this industry, such as the critical importance of continued antitrust immunity for all types of ocean carrier agreements in the U.S. and other international liner shipping trades.

In the NOI, the Commission poses a number of general questions relating to the potential impact that carrier agreements have on rates and services in major trade lanes, and has also requested specific data relating to individual stakeholders' commercial experiences in these trades since the EU's withdrawal of immunity. As a trade association, ASF does not have this latter kind of commercial data available – we expect that this information will be included in a number of submissions by individual carriers or

other interested parties. Nonetheless, ASF wishes to take this opportunity to respond to the Commission's more general questions relating to carrier agreements and, by extension, antitrust immunity for these agreements. As a group of Asian-based associations, the ASF is uniquely qualified to comment on this issue since carriers which belong to ASF members primarily operate in the Asia-Europe and Transpacific trades, and thus ASF has been closely monitoring trends in these key trades for many years. As demonstrated below, the ASF firmly believes that the overall rate and service level trends in these trades provide strong evidence that antitrust immunity for carrier agreements is indeed necessary for a healthy international shipping industry.

Antitrust Immunity for Carrier Agreements is Essential

Cooperative agreements amongst liner shipping companies have played a critical role in the shipping industry for over 100 years, and continue to be of great significance to carriers, importers and exporters, customers, and national economies around the world. These agreements are essential in promoting regular and reliable liner shipping services and preserving competitive choices for importers and exporters.

Through participation in voluntary rate discussion agreements, ocean carriers exchange and review market data, supply and demand forecasts, trade flows, and industry trends, and discuss voluntary and non-binding guidelines for rates and charges, service contract terms and conditions, and other similar topics. These agreements allow participating carriers an opportunity to mitigate the effects of below cost pricing practices that have historically plagued the liner shipping industry, and provide macro-economic trade information for better overall decision-making, all with the purpose of promoting service and investment, and preserving competition in the trade.

Virtually all of the major trading nations in the world have recognized the importance of carrier agreements, and have also recognized that their ability to continue largely depends on immunity from those countries' competition laws. Antitrust immunity for liner shipping agreements is still the international standard; it is permitted in virtually every major trade lane in the world, including the United States, Canada, China, Singapore, Japan, South Korea, Taiwan, and Australia. The most recent development in this area is Singapore's decision in December 2010 to extend its block exemption for liner shipping agreements until December 31, 2015. This decision was based on studies in 2005 and 2010 by the Competition Commission of Singapore ("CCS"). In making this decision, the CCS noted that "antitrust exemptions remain the regulatory norm for the liner industry globally, and for most of Singapore's trading partners," and "will provide continued certainty to the shipping industry." The CCS concluded, after an extensive year-long review, that liner shipping agreements have a "net economic benefit" and that the presence of these cooperative agreements provides "a higher degree of connectivity and service choice for Singapore's importers and exporters." Similar conclusions were reached by other countries in the Asia Pacific regions in the past 12 years.

Lack of Immunity in the EU Trades Has Had Several Negative Impacts

As Singapore stated in its decision to renew and extend its exemption, the only major exception to this international standard is the EU, which withdrew liner conference immunity in October 2008. Although it has been less than three years since the EU's decision, and that decision also coincided with the global economic downturn that began in the latter half of 2008, the negative impacts of the EU's decision on liner shipping rates and services in the EU trades are still cognizable. Though the impact of the global recession impacted the entire shipping industry and was felt by carriers operating in all global trade lanes, it has been well documented over the past few years that there has been considerably more rate and service level volatility in EU trades than in comparable US trades where there is still antitrust immunity for rate agreements.

A key example is two of the three largest trades in the world, which are quite similar in terms of key characteristics—the Asia-Europe and Transpacific trades. As the figures below demonstrate, prior to the EU's policy change, Asia-Europe Westbound rates were on average 1.2 times higher than Transpacific Eastbound rates. However, after the EU's policy change, the Asia-Europe rates rose to 2.5 times that of the Transpacific rates. While the Transpacific rates experienced some volatility from 2008 to the middle of 2010 as a result of the global financial crises, rates in the EU trade suffered significantly more severe drops that were followed by sharp increases throughout this same period.

Figure 1: Rate Stability Before EU Policy Change
Standard deviation of AET WB rate is 1.2 times higher than TPT EB
Source: CI Quarterly Rate Index Data

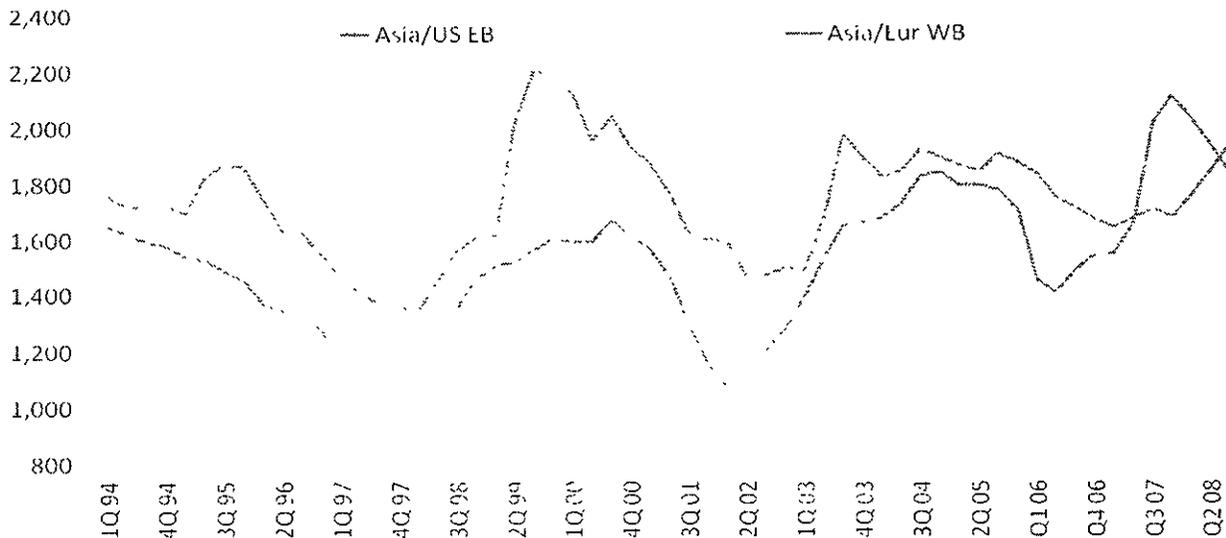
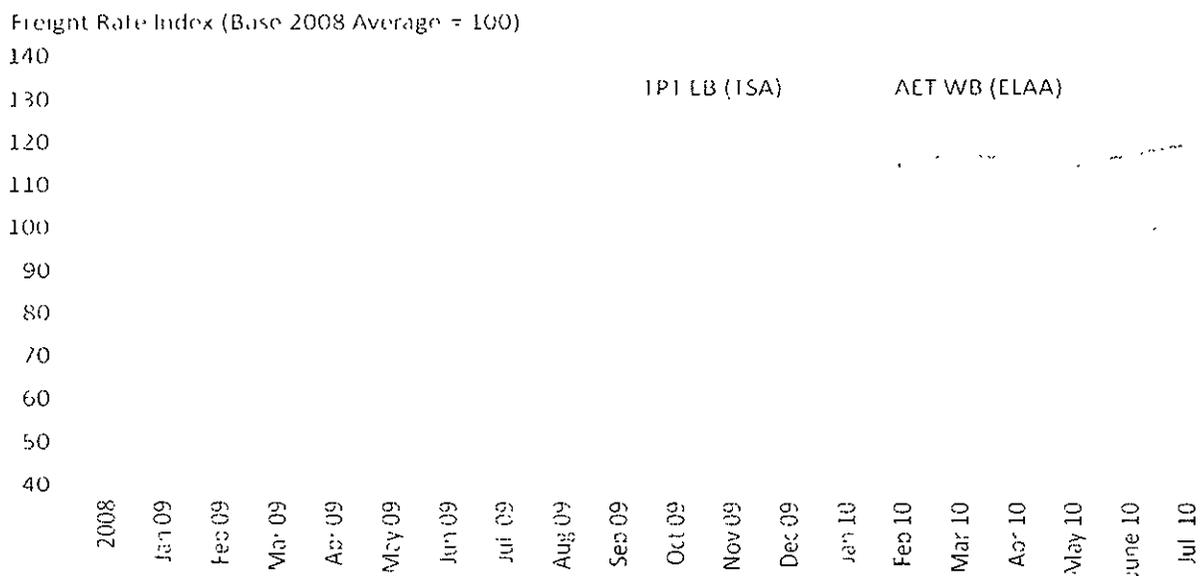


Figure 2: Rate Stability After EU Policy Change
Standard deviation of AET WB rate index is 2.5 times higher than TPT EB
Source: TSA and ELAA/CTS Data



In addition, since the EU's repeal of antitrust immunity, there has been a rise in new, higher, and less consistent surcharges, as carriers have each sought to recover a number of escalating costs related to serving this trade. This is perhaps best reflected in a report commissioned by and prepared for the EU on Terminal Handling Charges ("THCs") before and after the EU's repeal of conference immunity. That report concluded that virtually all EU trade THCs increased after 2008 from their conference levels, and that carriers appeared to have abandoned the old formula for calculating THCs, but instead based their current charges on varied cost analyses, leading to higher and considerably less consistent charges.¹

Finally, since the EU's withdrawal of immunity, carriers which belong to ASF member associations have reported a significant increase in shippers' complaints in the EU trades, as shippers have repeatedly informed carriers that wild rate and service swings must be avoided, and that they desire the same stability and predictability that is experienced in other trades in the EU trades as well. Difficulties in comparing and negotiating rates and surcharges have also become a serious concern for many shippers.

Continued Rate and Service Volatility Could result in Serious and Lasting Consequences

Liner shipping is an essential utility for international trade. It must be looked at not just in terms of service and rates available today, but what will also be needed in the medium and long term. Continued rate and service volatility of the kind that has existed in the EU trades since its decision to repeal antitrust immunity for liner conferences could result in several lasting consequences. First, prolonged depressed freight rates can and have led to service reductions, in terms of available capacity, port coverage, direct ports calls, frequency of sailings, and overall service quality. Rate agreements play an important role in mitigating predatory and other destructive pricing practices that undermine the continuation of high level services, making antitrust immunity for these agreements so essential. Without antitrust immunity, is it realistic to assume that the combination of below cost rates and prolonged rate volatility in the EU trades will somehow result in increased or better service over time?

Second, as the Commission is well aware, the liner shipping industry is highly capital intensive, and involves a large amount of high fixed vessel and system costs. Given the huge capital commitment required to operate a liner service, extreme and prolonged rate volatility can lead to destructive competition between carriers. As has been the experience in the EU over the past few years, in an effort to recover high fixed costs, carriers will often take short term pricing actions above marginal cost levels to fill empty capacity that drives rates below total costs. These kinds of rate wars if left unchecked could result in carriers leaving the trade, reducing service, being forced out of business, or being forced to consolidate, all of which would reduce competitive

¹ See Hackett/Raven Trading Limited, "Terminal Handling Charges During and After the Liner Conference Era," Paras. 74-81 (Oct. 2009).

options for shippers. It would also ultimately result in higher transport costs if there is a lack of viable competition or adequate capacity.

Third, prolonged rate and service volatility could have a long-term negative effect on overall carrier investments in new and more efficient tonnage, and that inadequate investment could result in insufficient resources to meet expected trade growth and future demand. Rate agreements are designed to 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. If carriers continue to invest in vessels and equipment, it will ensure that there is adequate capacity to provide service in the coming years to meet the growing needs of importers and exporters. However, if there is lingering uncertainty and volatility, carriers will have much less incentive to invest.

Put differently, in order to operate a vessel service in either the U.S. Transpacific or EU-Asia trades, a carrier must commit eight to ten 8,000 TEU vessels, which is an investment of approximately US \$1.3 Billion per vessel string. This includes, among others, the cost of the vessels, shoreside terminal and intermodal infrastructure, fuel, insurance, crew wages, berth fees, and periodic maintenance and repair fees. From a purely business perspective, it is logical that carriers would be much less inclined to make such huge investments over time in a trade where there are sharp rate declines, destructive competition or harmful rate wars among carriers, and continually escalating costs.²

There are of course other indirect benefits of rate agreements on potential carrier investments, such as improved access to more accurate trade data, market information, and supply and demand trends, which allow carriers to make more informed business decisions and investments. Better decision-making means fewer errors, smarter decisions on deployment and ultimately lower cost and better service to shippers.

Finally, through rate agreements, there are carrier organizations to represent carrier interests in consultations with government regulatory bodies and with designated shippers' organizations, which help facilitate dialogue between these parties and address important trade issues. In the absence of these agreements, it will be considerably more difficult for shippers and carriers to address trade-wide problems or concerns.

Conclusion

As stated above, the EU's decision to repeal immunity took place less than three years ago. As of today, in ASF's view, there is still too short a period for the Commission to fully gauge the longer term impact of the EU's decision on carrier investments in the trade because these kinds of decisions are made over the course of many years. It takes between three and four years for carriers to order, build, and deploy vessels alone.

² This is particularly the case since liner shipping returns on investment have been below most other industries, including many shippers of goods carried on liner vessels.

The effects of volatility will take years to play out. Thus, whether there will be adequate carrier service and investment to meet future demand in the EU and other trades still remains to be seen. However, the results so far are not promising. The prolonged depressed rates, sharp and sudden rate drops, service reductions, new and less consistent surcharges, and increasing shippers' complaints all suggest that the EU experiment has not been working.

These negative results also show why antitrust immunity for rate agreements is so important. In providing carriers a buffering mechanism to promote stable service patterns in essential trade routes, and encourage continued investment and technological innovation in vessels and related infrastructure, antitrust immunity for all types of carrier agreements continues to be essential for the healthy development of the liner shipping industry and the international trading community as a whole.

Yours Faithfully
Asian Shipowners' Forum

Yuichi Sonoda
Secretary General
