Some Thoughts on Non-Finance Oriented Shipping Instruments in the pre-WTO Era

Pak, Myong Sop* · Kim, Eun Joo**

Ⅰ. INTRODUCTION
Ⅱ. THE DEVELOPMENT OF PROTECTIONISM IN SHIPPING
Ⅲ. NON-FINANCE ORIENTED PROTECTION
Ⅳ. CONCLUSIONS

Ⅰ. INTRODUCTION

Recently, there is an emerging world-wide consensus on the importance of competition policy following the implementation of market-oriented economic reforms, including deregulation, price liberalization, privatization and liberalization of trade and foreign direct investment. Much work in this area has been led by WTO (World Trade Organization).

The problem of protectionism in international shipping was not confined to any one group of countries in the pre-WTO era. Most if not all countries in the international shipping community have at one time or another engaged in such practices to varying degrees to assist their national fleets. The last several decades after the second world war have witnessed increased government involvement, particularly by developing countries and state trading nations in international maritime transport

* Professor, Business School, SungKyunKwan Univ.
** Ph.D. in Economics, PuKyung National Univ.

services

Although the aim of an increasing and equitable participation of developing countries in the world shipping tonnage can be best met by attempting to increase the competitiveness of fleets and by eliminating obstacles to free and fair competition, protectionist measure have been increasingly adopted by a large number of developing countries. These trends have been based on the infant industry argument. According to this argument, a particular industry may not be competitive on world markets today, but, if encouraged by protective government policies, that industry may be competitive within a reasonable period of time.

The forms and measures of protectionist policy in shipping are extremely varied (Ademuni-Odeki 1985, 1988, OECD 1987, Chrzanowaski 1985, and Drewry 1982). Odeki classified protectionist measures largely into three categories; flag preference, flag discrimination and maritime subsidies. But his classification was not clear-cut because it did not identify the distinct differences between flag preference and flag discrimination. Drewry and the OECD categorized protectionist measures as either overt or covert, and this is a general and popular approach.

A first way to affect international competition is to provide finance-oriented assistance like subsidies, which either directly or indirectly discriminate against foreign shipping. A second form of protection is achieved by the use of non-finance oriented instruments of cargo reservation which retain cargoes for vessels under the national flag. All forms of non-finance oriented protection presuppose a national flag fleet large enough to transport a significant portion of exports and imports.

Ⅱ. THE DEVELOPMENT OF PROTECTIONISM IN SHIPPING

A subject of considerable contention and debate for many years, protectionist policies were most often used by developed countries or companies to support their merchant marines. Protectionist policies are also being used by developing countries in order to expand their merchant fleets to the size and structure desired or determined by the needs or their national economies.

In the pre-modern age protective shipping policy was based on discrimination against the foreign flag ship. Flag discrimination reached its climax when the navigation law was enacted by Oliver Cromwell. With the abolition of the navigation law in 1849, shipping subsidy temporarily formed the keynote of shipping policy.

During the period between the two world wars, the tendencies in shipping that had their origin in the final two decades of the nineteenth century - intensified competition, government intervention, protectionist policies, and monopolistic agreements - were accentuated by the general crisis of world economy. Following the universal idea of restoration of free trade on a world-wide scale after World War Ⅱ, the abolition of trade restrictions has made comparatively steady progress in international trade.

However a different development has taken place in shipping. Cargo sharing and shipping subsidy coexisted throughout the world in protective shipping policies after World War Ⅱ. After the second world war, in general the traditional maritime countries tended to neglect cargo sharing for shipping subsidy.

Developing countries, on the other hand, have tended to adopt cargo sharing as the instrument of shipping policy. The establishment of

UNCTAD in 1964 marked the Third World as a force in shipping and heralded the rise of shipping nationalism.

The Third World's vision of a new regime is expressed in the UNCTAD Code of Conduct for Liner Conferences, in which the national interest replaces the market as the constitutive principle. The Code for Liner Conference came into 1984 as a super-multinational agreement on conference cargo sharing.

Free trade is conducted nominally in the world shipping market. However most developing countries have adopted protective practice such as cargo sharing and shipping subsidy to develop their shipping industries.

Subsidies have been considered a better protectionist measure than cargo sharing; they do not directly impose trade barriers, and they discriminate equally against all foreign shipowners. Whether direct or indirect in form, subsidy levels constitute an easily quantifiable form of government intervention in shipping. In general the level of subsidy was low in the postwar period and has tended to decrease except in the special case of United States (Cafruny 1987, 133).

It is impossible to measure precisely the amount of cargo reserved from the open market by flag discrimination. Based on world trade data from 1957, Sturmy (1962, 206) concluded that less than 15 per cent of trade flowed to and from discriminating countries and that no more than 5 per cent of this fraction was actually subject to discrimination, because most countries with protectionist laws lacked the ships to enforce them. The Rochdale Report (1970) made a similar conclusion that as late as 1967, less than 5 per cent of world trade by weight was subject to cargo protection laws. Cafruny (1987) presented an estimate of the extent of flag discrimination in 1978 based on Sturmy's procedures. His results reveal significant increases, both absolute and relative, in the trade of discriminating countries. He yielded an estimate of 12 per cent of world trade by weight flowing to or from discriminatory countries. The above figures suggest that protectionist measures were not quantitatively important in world shipping and international trade. However, many developing countries have established laws or provisions concerning cargo sharing regardless of their actual fleet size in 1980s.

Ⅲ.NON-FINANCE ORIENTED PROTECTION

1. Cargo Reservation

Cargo reservation served to direct a proportion of cargo to vessels of the national flag. Cargo reservation may be unilaterally applied by a government in favour of its national fleet to which a specific quota of the total cargo carried in that country's foreign trade or certain cargoes are reserved wholly or partially.

Cargo reservation may be also agreed upon by both trading partners who may reserve the whole of their bilateral trade, or part thereof, with the rest being left open for foreign-flag vessels.[1] Cargo sharing can be the object of a multilateral convention, as shown by the UNCTAD Code of Conduct for Liner Conferences. It is then intended to form a universal basis of maritime transport incorporating the principle of multilateralism in conference cargo. In many cases, only certain types of cargoes are subject to cargo reservation. These are most likely to be government-owned cargoes or cargoes in which government has an interest. Cargo sharing and cargo reservation are also applied by the pooling agreements of shipping conferences and may also be applied by methods of cargo control such as exporting c.i.f. and importing f.o.b. policies.

1) In this case cargo sharing is a more correct terminology.

2. Types of Cargo Sharing

In spite of the fact that cargo sharing schemes are often initiated unilaterally, they are generally implemented bilaterally or multilaterally by two or more trading partners who mutually agree on a division of their seaborne trade in the form of a shipping agreement.

1) Unilateral Cargo Reservation

A universally applied, and accepted form of unilateral cargo reservation to which only a few countries are an exception is the reservation of a country's coastal trade for the national flag under the so-called "cabotage legislation" . Cabotage laws generally stipulate 100 per cent reservation for the national flag and are thus the most extensive forms of such policies.

2) Bilateral Cargo Sharing

Bilateralism is a long established form of discriminatory trade policy, and its practice, in maritime commerce is borrowed from the international trade practice of bilateral negotiations and agreements. Two countries conclude a trade agreement with a maritime clause, or alternatively a purely maritime agreement that seeks to divide cargo, involved in the trade between them, between their two respective national fleets. Normally, it is in the ratio of 50-50 and may be embodied in a treaty, an underatanding or, intended a convention. Originally, the 50-50 division restricted the share between only the two parties to the treaty and/or understanding, excluding any other third parties. This formula or guideline has now been extended from 50-50 to 40-40-20 or some other similar agreements that might be worked out by the parties.

Most bilateral agreements in shipping usually embrace a series of reciprocal clauses, including:

① mutual recognition of ship's documents and the nationality of the vessel
② treatment of vessels, their cargo, and crew in ports of both countries
③ promotion of the national merchant marine in the carriage of goods generated by mutual trade
④ exemption from double taxation of freight incomes, fully or partially
⑤ assistance to crew and the ship in case a vessel of either of the contracting parties suffers shipwreck in their territorial waters
⑥ mutual consultation to eliminate obstacles to and/or to implement the agreement.

Most governments acknowledge that, when situations warrant, a combination of competition and bilateral shipping agreements may be necessary. Carriers perceive that bilateralism could lead to cargo increases and permit rationalism of service. On the other hand, shippers are fearful that bilateral relationship could adversely increase the cost of transport.

3) Mutilateral Cargo Sharing

Multilateral agreements basically involve three or more countries who agree to share their cargo in some forms. These may be introduced in isolation or in the context of a wider process of economic integration as was the case with the LAFTA Convention on Water Transport (Stemmer 1978, 129). The UN Code of Conduct for Liner Conference is an example of international efforts at a multilateral approach. Apart from this, one of the earliest known attempts by the traditional maritime countries is the British Commonwealth Merchant Shipping Agreement (Odeki 1985, 164). On the other hand one of the examples of shipping in general is probably the

LAFTA Convention on Water transport of May 1966, providing for a cargo sharing system, though by then national preference legislation and cargo sharing treaties were already common, covering both regional and international trade.

Bilateralism places limits upon consumer's freedom to buy goods in the cheaped market and prevents the realization of full international specialization with each country producing, for export, the products in which it has the largest comparative advantage. Under multilateral agreements, such inefficiencies can often be reduced or eliminated by structuring agreements in such a way that the trades complement each other, and assure a best use of shipping capacity employed.

Governments and international institutions have tried to restore the free multilateral trade of goods and services. The purpose of multilateralism is to assure fair participation in mutual trade, while providing more effective use of shipping capacity than is usually feasible under bilateral cargo sharing agreements and cargo reservation schemes. In these points, multilateralism approaches the basic spirit of free trade rather more closely than bilateralism.

Although multilateral cargo sharing in shipping industry may have its advantage, it also has its disadvantages as a departure from freedom of shipping. Implementation is also difficult, there being basic sources of disagreement in the criteria adopted for the distribution of reserved shipments. Generally speaking, countries controlling a large volume of trade will aspire to reserve a substantial part for their own carriers. On the other hand members whose foreign trade is sufficient to sustain the development of the viable merchant marine industry will favour an integrated multilateral approach expecting to obtain a share in the carriage of trade between their bigger partners.

3. Cargo Reservation according to Commodity

Cargo sharing scheme can also be classified by the kinds of commodities to which they are applied.

1) Cargo reservation on all cargoes

By law, several countries claimed all the cargoes for the carriage by their merchant marines.

2) Cargo reservation on government cargoes

Government cargoes encompass a broad range of goods imported or exported by government departments, quasi-government bodies and nationalized corporations.

3) Cargo reservation on specific commodities

Certain countries provide for a share of specific commodities to be carried by national flag ships. In most cases, this form of cargo reservation concerns major export products such as coffee, beans, cotton and petroleum products.

4. Cargo Control

Cargo reservation may also be exercised through a number of direct measures of cargo control, such as:

1) exporting c.i.f. and importing f.o.b.
2) freight bureau
3) restrictive carrying licensing
4) transhipment reservation

5) bill of lading or letter of credit control

Such controls have an economic impact in terms of cargo delays and increased shipping cost. Among these, it is worth while to review the trade terms in this section. Governments may intervene in the commercial determination of terms of shipment for a variety of reasons and in a number of ways. Countries short of foreign currency and with national flag shipping may prefer c.i.f. sales and f.o.b. purchases in order to improve their balance of payments position.

The use of standard terms and definitions facilitates international transactions. The most widely used set of definition for terms of shipment is in the interpretation of trade terms by the International Chamber of Commerce, the Incoterms 2000.

The terms of shipment define the responsibility of the buyer and seller for arranging, controlling and paying for the various stages of carriage. The ship or line by which the goods are to be delivered is sometimes specified in the contract. Where this is not done, the seller has the right to choose the carrier under c.i.f. terms. On f.o.b. contracts, however, the situation is reversed and it is the buyer who chooses the carrier[2] Therefore, the relevance of c.i.f. and f.o.b. shipments, regarding trade policies, lies especially in the way they affect the preferential and discriminatory status of various flag vessels in relation to access to cargoes and other related treatments.

However, this ignores actual or competitive conditions by the trading partners. Under c.i.f. terms, shipping costs are paid by the seller who has the right to choose the carrier; under f.o.b. terms, they are paid by the

2) Lord Wright observed that c.i.f. contracts are more widely and more frequently used than any other for the purpose of seaborne commerce. An enormous number of transactions, in value amounting to untold sums, are carried out every year under c.i.f. contracts. The traditional f.o.b. arrangement is often felt to be inconvenient because the seller, who conduct his business in the country where the goods are situated before dispatch, has better facilities for arranging these items than the buyer (Schmitoff 1986, 22-29).

buyer. However, the incidence of the cost does not necessarily lie with the party in the best position to control trade terms.

Rather the incidence of transport cost depends on the elasticity of supply and demand. Therefore, it is not good to apply the policy of c.i.f. export and f.o.b. import unconditionally, without examining the economic factors which determine its effect on the balance of payments.

Some developing countries also controled cargo by establishing a central booking arrangement. This arrangement is known as the Central Freight Bureau (CFB), which has some control of its country's ocean transport market. Central Freight Bureau or its designated agent arranges the shipments to and from the country concerned. Therefore, CFB has the powers to allocate cargoes to national flag ships.

According to Gajawira (1991), the Sri Lankan freight bureau had the powers of cargo centralization, reservation and allocation, as well as of negotiation on freight rates and service quality by legislation. He found that the central freight bureau in Sri Lanka was a stronger countervailing force against strong liner conferences than the Shippers' Council. However,, in the late 1980s the Bureau's power reduced by a combination of interest groups; the shipper, shipowner, shipping agent and the port which asked a proposal of liberalizing allocation of freight space and removing the power of allocation granted to CFB exclusively.

Transhipment reservation and letter of credit[3] control are also used to promote national fleets in a few developing countries. In Venezuela, transhipment of import cargo was not allowed when there existed direct services by the national line and associated lines. In Ghana, for all imports by means of Bank of Ghana letter of credit two L/Cs had to be issued i.e., one in the name of Shippers Council to cover the freight, and one in the name of the supplier. Freight payments shall be made directly from the

3) Shippers may be required to conform exactly to the requirements of a letter of credit; otherwise transport that they will not be paid. This can lead to fragmaented decisions about transport that do not help the operation of an integrated logistics approach.

Shippers Council foreign account to the line concerned. The Ghana Shipper Council appointed agents abroad to carry out the function of freight allocation. Futhermore, it levied a charge to U.S. $ 2 per ton for imports and $1.20 per ton exports on carriers in the late 1980s.

Ⅳ. CONCLUSIONS

Shipping protectionist measures are imposed to help the national fleets based on the perception that there are economic benefits from increasing them. Relative to the complexity of the objective, protection is a fairly simple and blunt instrument of policy. Ultimately, the bluntness of protection as a policy instrument means that its precise effects- the extent of the benefits and their distribution- are extremely difficult to predict when the policy is being designed; while the outcome frequently fails to meet the objectives in some important respect. There are cases where the assistance being provided through protectionist measure has imposed costs for in excess of the conceivable benefits. Ultimately, choosing among protective options depends on careful and ongoing assessment of the costs and benefits of policy not only from a narrow budgetary point of view but in terms of the economy as a whole.

Non-finance oriented protection has been the most popular instrument in developing countries. This is because most developing countries have not enough revenue to support their shipping industry. They have sought to establish or maintain national fleets as a form of import substitution by cargo reservation. It is easier, because of budgetary constraint and lack of flexibility in financial structure, to use reservation rather than subsidies.

The ineffectiveness of cargo sharing has pervasive impact on freight rates. The indirect costs of cargo sharing which are less tangible and more difficult to quantify must be also added to its adverse effects. For example, the increase in freight rates, due to cargo sharing, leads to a reduction in the demand for export cargo. It is obvious that the magnitude of this reduction depends on the initial freight increase as well as on the elasticity of the demand. The economic disadvantages of cargo sharing can be summarized as follows;

1) cargo sharing leads to overtonnage
2) cargo sharing transfers the cargo from the low-cost operator to the high-cost operator
3) cargo sharing inhibits the technological progress of shipping industry.

References

Ademuni-Odeki, Protectionism and the Future of International Shipping, University of Aberdeen. 1985.

____________, Shipping in International Trade Relations, Gower Publishing Company. 1988.

Cafruny, A.W., Ruling the Waves - The Political Economy of International Shipping, University of California, Berkely. 1987.

CENSA, List of discriminatory measures affecting shipping.

Chrzanowski, I., An Introduction to Shipping Economics, Fairplay Publications, London, 1985.

Drewry Shipping Consultant Ltd., Protectionism and the Bulk Shipping Industry, London, 1982.

Gajawira, B.P., The Central Freight Bureau of Sri Lanka; A Critical Review, Ph.D. Thesis, The University of Liverpool, 1991.

Hawkins, J.E., Shipping subsidies and the balance of payments, Lloyd's of London Press, 1989.

Jansson, J.O. and Shneerson, D., Liner Shipping Economics, Chapman and Hall, 1987.

Mari, B.E., Cargo Sharing through a Policy of Bilateralism, Marine Policy, Vol.11, No.2, 1987.

OECD, Maritime Transport, Paris., 1987.

Richard G. and Gilsoo K., Logistics and International Shipping, Korea Maritime University, 2000.

Schmitoff, Export Trade, The Law & Practice of International Trade, Stevens & Sons, 1986.

Stemmer, E.O., Flag Preference in Latin America, Journal of Maritime Law and Commerce, Vol.10, No.1, 1978.

Sturmy, S.G., British Shipping and World Competition, Athlone London, 1962.

Totland T., Protectionism in International Shipping and Some Economic Efffects, Maritime Policy and Management, Vol.7, No.2, 1980.

UNCTAD, Imbalance between supply and demand in world shipping, TD/B/C.4/312, 1987.

ABSTRACT

Myong-Sop Pak · Eun-Joo Kim

Shipping protectionist measures are imposed to help the national fleet based on the protection that shares are low and that there are economic benefits from increasing them. Relative to the complexity of those objectives, protection is fairly simple and blunt instrument of policy.

Shipping protectionist measures are classified into two groups on the basis of the nature of protectionist tools; finance-oriented and non-finance oriented instruments. The thesis aims to show non-finance oriented shipping instruments in the pre-WTO Period. Chapter 2 deals with the development of protectionism in shipping. Chapter 3 Classified non-finance oriented protection such as Cargo Reservation, Cargo Sharing and Cargo Control. Chapter 4 outlined and examined the effect of Non-Finance Oriented Shipping Instruments which was the most important in developing countries.

Keyword : shipping, cargo reservation, protectionist policy