

**PRODUCTIVITY COMMISSION INQUIRY INTO INTERNATIONAL LINER
CARGO SHIPPING: A REVIEW OF PART X OF THE *TRADE PRACTICES
ACT 1974***

**SUBMISSION BY THE DEPARTMENT OF
FOREIGN AFFAIRS AND TRADE**

The Department of Foreign Affairs and Trade (DFAT) has an interest in shipping matters, including this Review, given the importance of efficient and reliable shipping services for Australia's international competitiveness, its trade performance and national economic welfare. DFAT suggests that the objective of this Review should be:

- To ensure that Australia's liner shipping legislation maximises Australia's trading interests in terms of continuing access to the types and quality of shipping services required to maximise export potential, at the lowest possible cost.
- To identify strategic gains to Australian exporters of any proposed changes to Part X of the Trade Practices Act.

DFAT is attracted to the following arguments in favour of retaining Part X of the Trade Practices Act:

- There is general consensus among Australia's exporters that Part X provides the level of service they require, at a competitive cost.
- The retention of Part X provides guarantees that smaller volume ports such as those in South Australia and Western Australia are serviced, thereby assisting exporters in those states.
- Part X provides essential countervailing powers for exporters, especially small to medium exporters, in negotiating service agreements with large international carriers for the carriage of their exports.

Whilst supporting the retention of Part X, DFAT recognises that there is a need to ensure that appropriate safeguards are in place to prevent possible abuse of market power arising from the existence of cartels arrangements permitted under Part X. In particular, exporters need continuing access to reliable and competitively priced shipping services. DFAT expects refinements in this area would be the focus of any amendments to Part X resulting from this current Review.

DFAT considers that the Review should examine, *inter alia*

- The level of competition currently applying in the liner industry under Part X exemptions, and the price and quality of services this competition has delivered to exporters.
- The impact on the specific interests of exporters of any changes to Part X.

In addition to examining these issues, this submission outlines developments in the World Trade Organisation (WTO) on maritime issues.

A. COMPETITION IN THE LINER INDUSTRY

One of the key issues of importance to exporters in the current Review is to determine whether the existence of liner conferences under Part X inhibits competition in the industry or provides sufficient competition to provide exporters with continuing access to the type and quality of shipping services required, at the lowest possible cost to maximise Australia's trading interests.

Liner conferences have operated on major world trade routes for over a hundred years. Conferences are groupings of liner shipping operators which co-ordinate the supply of costly shipping services. Shipping companies often are members of several conferences. The conference system provides scheduled shipping services to and from particular ports at set freight rates and other conditions. The benefits to exporters are access to reliable, efficient and frequent shipping services.

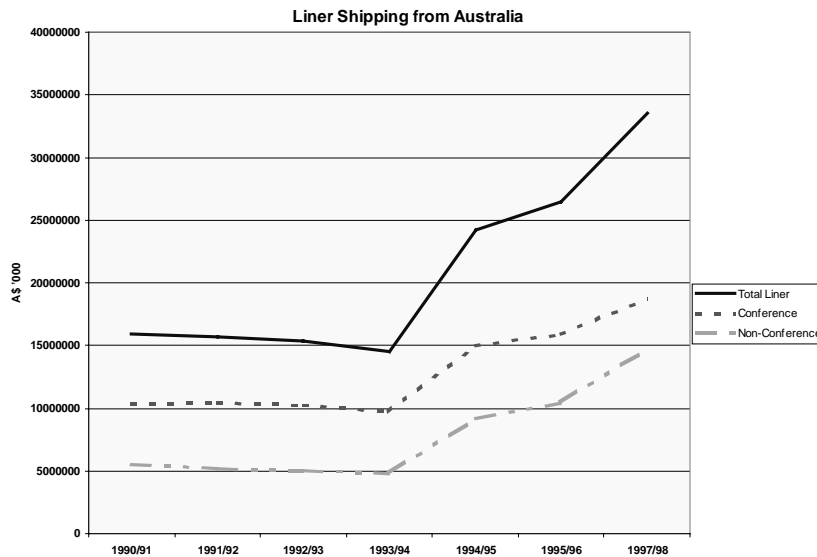
Almost all countries allow provision for liner conferences in their competition legislation but attempt to regulate conference behaviour. Australian shippers and successive governments have generally accepted that the conference system can benefit Australia's trade, provided safeguards are in place to prevent possible abuse of cartel power. The rationale is that the public benefits outweigh the anti-competitive effects of allowing collusion in setting prices.

The continued decline in freight rates and increase in the market share of non-conference services point toward competition within the industry (see Attachment A).

It is widely accepted that freight rates for Australia are generally competitive given that shippers are somewhat disadvantaged by Australia's geographical position. Rates tend to be similar for conference and non-conference vessels alike. The East Asian economic crisis has seen a drop in exports to the Asian region since mid-1997 causing a surplus of shipping space and a resultant fall in freight rates to the lowest level since the 1970s.

There was a dramatic reduction in the share of liner services taken up by conference vessels from the mid-1970s, when conference ships carried over 90-95 per cent of Australia's liner trade, to around 1990. In the 1990's this decline has continued, but has not been as marked.

In the four years up to 1994/95, the share of conference trade in liner shipping from Australia remained quite stable at between 65 per cent and 67 per cent. In 1994/95, this share dropped to around 62 per cent, fell to around 60 per cent in 1995/96 before dropping to 56 per cent in 1997/98.



Data sourced from Bureau of Transport

B. INTERESTS OF EXPORTERS IN PART X REVIEW

Any Review of the legislation needs to identify strategic gains to Australian exporters of any proposed changes.

Countervailing Powers

Part X provides Australian exporters with countervailing powers against international conference arrangements which, in the absence of Part X, could exercise market power over price and quality of service provided to exporters. In short Part X provides some protection to exporters from powerful foreign ocean carriers. The Australian Peak Shippers Association (APSA) is the designated peak shipper body under Part X, representing Australia's liner shipping exporters generally and providing a negotiating voice for Australia's diverse and largely uncoordinated exporters. Part X ensures that:

- Conference carriers participate in negotiations with exporters
- All Australian exporters have access to export markets
- Shipping rates are competitive
- Carriers are not able to disregard the interests of exporters
- Carriers have to provide cost information to exporters

Any alternative to Part X, such as an authorisation process, would need to ensure exporters are not disadvantaged in their ability to negotiate the level and cost of service they require from international carriers. We are concerned to ensure that any examination of the advantages and disadvantages of an authorisation process address whether the provision of such an arrangement would be no less efficient, cost exporters no more, be no more time consuming, and no less predictable than the current Part X provisions.

International Practice

Consideration of the merits of abolishing Part X exemptions would need to take account of the fact that such action would put Australia at odds with international practice and could place Australian exporters at a competitive disadvantage. Carriers may be tempted to register with a third country authority and they could then operate without regard to Australian law. Any such result could be of real detriment to exporters.

A number of our trading partners and competitors, including the United States, European Union, New Zealand, Japan and the Republic of Korea, have similar exemptions to Part X contained in their competition policy. A major feature of competition policy regimes adopted by most OECD member states is that they give conference agreements some form of predictable, but conditional, exemption from national competition legislation.

Media reports indicate that Asian shippers are seeking a legal mechanism similar to Australia's Part X in order to protect their exporters interests in the face of rising freight rates and terminal handling charges stemming from handling imbalances. The East Asian economic crisis has seen ships entering Asian ports under full capacity in the face of falling import demand and leaving Asian ports at near full capacity as countries in the region attempt to export their way out of their current economic difficulties.

Service quality

Although the relevance of Part X is sometimes questioned at a time when freight rates are falling, Part X ensures that other matters including minimum levels of service, surcharges and inland haulage charges are also negotiated. DFAT notes the view of the Australian Peak Shippers Association (APSA) that negotiations on service quality have provided service frequencies and shipping capacity to a range of destinations which have contributed as much, if not more, to Australia's increase in exports in recent years than declining freight rates.

Currently, under Part X negotiations, conference lines are obliged to service low volume ports such as those in South Australia and Western Australia. There is concern that without Part X exemptions, the fall in revenue resulting from declining freight rates could result in a reduction in the number of services through mergers or through services being abandoned. These services may not be considered commercially viable by lines operating independently. DFAT recommends that consideration of any changes to Part X include analysis of the impact on exporters currently using low volume ports.

DFAT considers that any removal of Part X exemptions would need to analyse the impact on Australia's export interests of the removal of countervailing powers of export bodies. This would need to include the impact on the cost and frequency of shipping services provided to Australian exporters. DFAT notes the argument advanced by some shippers that removal of Part X exemptions would result in less choice of services and operators, fewer direct services, and fluctuating freight rates. These claims will need to be closely examined during the course of the Review.

Australian exporters rely heavily on access to competitively priced high quality liner services as an important component of their business strategies. Competitively priced high quality liner services are also important for government-led export initiatives. For instance, access to high quality reliable scheduled refrigerated services are important to the Prime Minister's "Supermarket to Asia" export initiative.

Amendments to Part X

Whilst the general view by exporters is that Part X has provided an efficient quality of service at a reasonable cost, a range of options have been put forward to strengthen the position of exporters. Refinements in this area should be a major focus of amendments to Part X in this current Review.

Any amendments to Part X should be aimed at increasing competition within the industry and be in accordance with the Government's competition policy principles. Changes to Part X should work to improve efficiency and competition in the liner shipping industry servicing Australia and work to improve the competitiveness of Australian exporters on global markets and their access to these markets.

WORLD TRADE ORGANISATION: MARITIME ISSUES

Maritime negotiations in the WTO

DFAT is responsible for the management of the Government's multilateral trade negotiations in the WTO. At the end of the Uruguay Round, WTO members agreed to further negotiations in maritime services. These negotiations continued under the auspices of the General Agreement on Trade in Services (GATS) which entered into force on 1 January 1995 (see Attachment B). The GATS provides a multilateral framework of rules for trade in services and a timetable for progressive trade liberalisation throughout the services sector.

A successful conclusion of the maritime negotiations was not reached by June 1996. The major factor contributing to the suspension of the maritime negotiations was the lack of a U.S. offer, due to domestic sensitivities to reform of the Jones Act¹.

The next set of services negotiations is required to commence no later than 1 January 2000. These and other negotiations will be launched at a meeting of WTO Trade Ministers' in Seattle in November-December this year. Based on initial consultations, the approach to services being developed is aimed at ensuring that the negotiations are comprehensive and cover all sectors. This has been Australia's position as well. Accordingly, maritime services should be covered in these negotiations.

¹ The Jones Act is the United States *Merchant Marine Act* of 1920. Section 27 of the Act requires that all goods transported by water between United States ports must be carried in vessels built and registered in the United States, owned by United States citizens and fully crewed by United States citizens. Australian built fast ferries, which have about a quarter of the world market, are excluded from the United States by the Jones Act. Along with services negotiations under the GATS, negotiations are occurring within the Organisation for Economic Co-operation and Development (OECD) on the Shipbuilding Agreement which are aimed at removing measures or practices which distort competition in the international marketplace.

At the suspension of the maritime negotiations most WTO members, including Australia, agreed that offers that were on the table would remain frozen until the 2000 services negotiations and countries will not impose any measures which would improve their negotiating leverage. This is effectively a standstill ("peace clause") on new measures which would reduce market access.

Australia's "standstill" offer includes commitments covering the so-called "three pillars", ie, international shipping, auxiliary services (such as storage and warehousing and customs clearance) and port services (such as pilotage, towing, provisioning and fuelling). Under the GATS, we are obliged to extend to all members the most favourable trading terms given to any other country (ie Most Favoured Nation, MFN, principle). The Part X exemption is listed in the Australian schedule as it provides for exemptions from Australian competition legislation so that liner shipping conferences can operate in and out of Australia. Part X also requires that every ocean carrier who provides international liner cargo shipping services to or from Australia shall, at all times, be represented by a person who is an individual resident in Australia (but not necessarily an Australian citizen) and has been appointed by the ocean carrier as the ocean carrier's agent for the purposes of Part X.

Australia's negotiating position for the services negotiations is currently being developed. DFAT advertised widely this year for public comment on Australia's negotiating approach to the forthcoming WTO negotiations. 130 submissions have to date been received from industry, interest groups and the public on our general approach. However, only a few of the peak industry groups have to date touched upon maritime issues. Our negotiating strategy will be developed based on ongoing extensive industry consultations.

Internationally, substantial barriers to maritime services remain across the three pillars, including: restricted or regulated access to port and port services, preferential cargo allocation, restrictions on establishment of branch offices and discriminatory measures favouring the use of national carriers.

Our negotiating priorities will be guided by industry interests and concerns. Our initial view is that we should push for WTO members to match Australia's standstill commitments on maritime. Australian domestic maritime reform may provide us with some negotiating leverage.

At the suspension of the last negotiations, we were encouraged that most members left their best offers on the table and hope this will provide a good basis for negotiations when they restart. There has, as yet, been no substantial discussion in the WTO on guidelines for a maritime negotiation. One key determinant of the success of the negotiations will be whether the U.S. will be prepared to Review the protectionist policies it maintains in the sector.

WTO Trade and Competition

There has been some suggestion that the newly established WTO Working Party on Domestic Regulation will address competition policy in the GATS. This work, however, is unlikely to be undertaken in the near future.

A Working Group on Trade and Competition Policy was established in 1997 to study issues relating to the interaction between trade and competition policy, including anti-

competitive practices, in order to identify areas that may merit further consideration in the WTO framework. Recommendations on future work are likely to be considered at the next WTO Ministerial Conference (30 November – 3 December 1999), when Ministers will decide on the structure, scope and timeframe for future negotiations. As work on trade and competition remains at an exploratory stage, it seems unlikely that there would be agreement to commence negotiations on trade and competition issues in 2000.

AUSTRALIA'S LINER SHIPPING TRADE

Around 80 per cent of Australian merchandise exports by value were transported by sea in 1997/98. The Australian shipping fleet is small by international standards. As a consequence Australia relies heavily on foreign vessels to meet its demand for international shipping services. As distinct from bulk carriers, liners generally tend to carry relatively high value/low volume cargoes. Liner vessels carried around 38 per cent of the *value* of Australia's merchandise exports in 1997/98.

Direction of Liner Trade

Conference and non-conference liner services service roughly the same export destinations. The major exceptions are China and Hong Kong SAR which are serviced primarily by non-conference shippers. The major countries of destination for conference and non-conference services have remained broadly unchanged since 1990/91. The largest 10 conference destinations by value account for nearly 40 per cent of total liner (conference plus non-conference) shipping and nearly 70 per cent of conference shipping. A similar pattern can be seen for non-conference services where the 10 largest destinations account for around 30 per cent of total liner shipping and around 65 per cent of non-conference shipping.

Table 1 **Major Export Destinations for Liner Shipping: 1997/98**

	Country of Final Destination	Value \$'000	% of Liner (conference + non-conference) Shipping)	% of Conference Shipping
Conference	Japan	3,449,618	10.3	18.3
	New Zealand	1,990,327	6.0	10.6
	USA	1,940,430	5.8	10.3
	Taiwan	1,042,828	3.1	5.5
	Korea	881,955	2.6	4.7
	Malaysia	778,675	2.3	4.1
	Italy	774,752	2.3	4.1
	Indonesia	751,669	2.2	4
	Singapore	707,117	2.1	3.8
	United Kingdom	655,037	1.9	3.5
	Country of Final Destination	Value \$'000	% of Liner (conference + non-conference) Shipping)	% of Non-Conference Shipping
Non-Conference	Japan	1,993,543	5.9	13.5
	Hong Kong SAR	1,192,605	3.5	8.1
	USA	1,180,131	3.5	8.0
	China	1,152,916	3.4	7.8
	New Zealand	770,854	2.3	5.2
	Taiwan	727,290	2.2	4.9
	Indonesia	701,542	2.1	4.7
	Korea	557,199	1.7	3.8
	Philippines	551,862	1.6	3.7
	United Kingdom	524,769	1.6	3.6

Source: Data sourced from Bureau of Transport Economics database

Composition of Liner Trade

Most of the major exports carried on liner services use both conference and non-conference services. The major exceptions to this are road vehicles, which primarily use conference services, and iron and steel which tend to make greater use of non-conference services. Because conferences provide more refrigerated capacity, the value of perishables such as meat, dairy and fruit and vegetables is greater on conference than on non-conference services. Increasing competition from airfreight has resulted in a declining importance in short life perishables, such as fish, being exported by liner services. An increase in beverages exports, particularly wine exports, has resulted in beverages becoming a major commodity on liner services, both conference and non-conference alike.

Major Export Commodity Composition of Liner Shipping: 1997/98

	Commodity	Value \$'000	% of Liner (conference + non- conference Shipping)	% of Conference Shipping
Conference	Textile fibres	2,981,529.00	8.9%	15.9%
	Meat and meat preparations	2,666,605.00	7.9%	14.2%
	Non-ferrous metals	1,477,782.00	4.4%	7.9%
	Other commodities and transactions	1,353,643.00	4.0%	7.2%
	Dairy products and birds eggs	1,197,241.00	3.6%	6.4%
	Road vehicles	610,806.00	1.8%	3.2%
	Beverages	578,785.00	1.7%	3.1%
	Power generating machinery & equipment	552,941.00	1.6%	2.9%
	Vegetables and fruit	478,726.00	1.4%	2.5%
	General industrial machinery & equip nes	429,247.00	1.3%	2.3%
	Commodity	Value \$'000	% of Liner Shipping	% of Non- Conference Shipping
Non- Conference	Non-ferrous metals	2,545,250.00	7.6%	17.2%
	Other commodities and transactions	2,352,475.00	7.0%	15.9%
	Textile fibres	1,673,006.00	5.00%	11.3%
	Meat and meat preparations	751,150.00	2.2%	5.1%
	Dairy products and birds eggs	607,937.00	1.8%	4.1%
	Iron and steel	468,865.00	1.4%	3.2%
	Machinery specialized particular indust.	405,745.00	1.2%	2.7%
	Metalliferous ores and metal scrap	378,503.00	1.1%	2.6%
	Vegetables and fruit	366,368.00	1.1%	2.5%
	Beverages	335,645.00	1.0%	2.3%

Source: Data sourced from Bureau of Transport Economics database

THE GENERAL AGREEMENT ON TRADE IN SERVICES

The General Agreement on Trade in Services (GATS), which entered into force in January, 1995, introduced a set of multilateral rules for trade in services. The GATS, like other WTO agreements, is subject to the dispute settlement mechanism introduced following the Uruguay Round of trade negotiations.

The GATS covers the vast majority of traded service sectors and applies to all measures affecting trade in services taken by all levels of government or non-governmental bodies exercising powers delegated to them by government. (An exception exists for Government Procurement.) It applies to services supplied across the border, through the establishment of a commercial presence and through movement by individual consumers and suppliers across borders.

The GATS principles and rules comprise general obligations which apply, with limited exceptions, to all services in all sectors, as well as particular obligations which apply only to those services where a Member has made a specific commitment in its schedule. One of the most important general obligations is the requirement for most-favoured-nation (MFN) treatment. This requires a Member to give to services and service suppliers from any other Member treatment no less favourable than it gives to like services and suppliers from any other country. Other important general obligations include transparency of laws and regulations; providing foreign service suppliers with access to review of administrative decisions; and non-discriminatory application of criteria for recognising foreign standards and qualifications.

Additional rules apply only to sectors in which a Member has made a binding commitment in its country schedule, that is, a specific commitment. The most important of these are market access and national treatment. Where a country undertakes to provide full market access in a particular sector, it agrees to eliminate quantitative restrictions on the sector, including limitations on the total number of firms and the permitted level of foreign equity, and to eliminate any restrictions on legal form of business entities (e.g., it would require countries to eliminate requirements for foreign investment to take the form of joint ventures.) The national treatment principle requires that WTO Members afford services and service supplies from other Members the same treatment enjoyed by their own services and suppliers.

Negotiated Commitments

Members' schedules of commitments identify the service sectors in which they will grant market access and national treatment to trading partners and any qualifications applying to those commitments. They also contain details of sectors in which Members have withheld application of MFN. (As a key principle of fair trade, however, Members are discouraged from suspending MFN.) These schedules contain the results of multilateral negotiations. The commitments entered in these schedules represent the *minimum* level of access Members are willing to make themselves legally bound to provide. Members frequently accord a greater level of access in reality.

The commitments and limitations are entered with respect to each of four modes of supply embodied in the definition of trade in services. The four modes are

Cross-border supply - non-resident service firms supplying services cross-border into the Member's territory

Consumption abroad - Member's residents purchasing services in the territory of another Member

Commercial presence - foreign services suppliers establishing, operating or expanding a commercial presence in the Member's territory, such as a branch, agency or wholly-owned subsidiary

Presence of natural persons - entry and temporary stay in the Member's territory of foreign individuals in order to supply a service

Negotiations took place on the basis of an agreed set of services, using definitions in the UN Central Product Classification code. Services fall broadly into two groups, basic services (or real-time services) (a. to g.) and value-added services (h. to n.). In general, countries are slower to liberalise basic services than value-added services.