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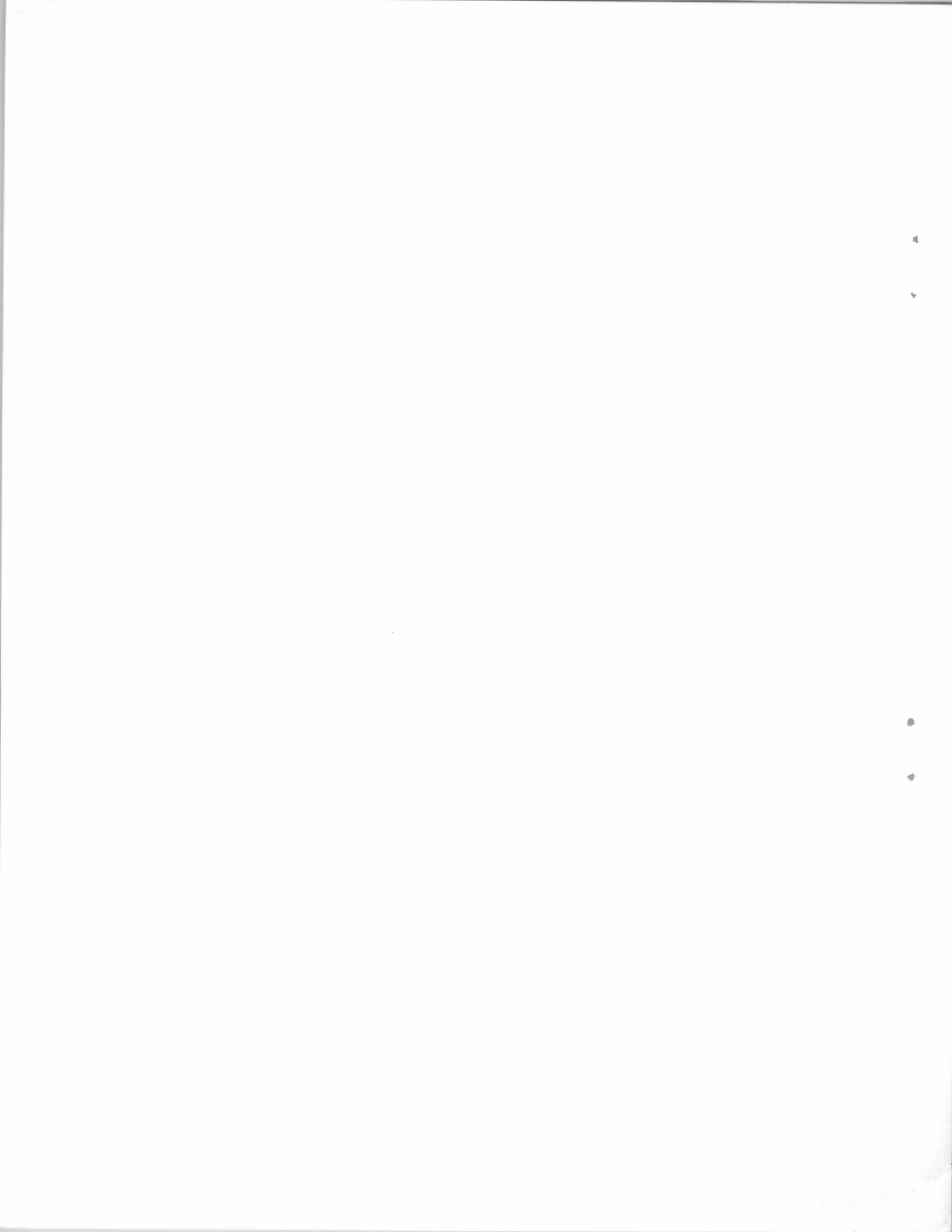
POLÍTICAS DE TRANSPORTE Y PREPARACIÓN
Y EVALUACIÓN DE PROYECTOS DE TRANSPORTE

Cabotaje Marítimo en el Mercosur
El Temor de la Competencia Internacional

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Cabotage and liner shipping in Mercosur

– the fear of foreign competition –

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The usual disclaimer: The opinions are not necessarily of Intermodal South America or ECLAC.
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When discussing if and how to promote cabotage services within Mercosur, one question that arises again and again is whether or not intra-mercotur trades should be opened to foreign companies. The observed global process of concentration in liner shipping – larger ships, hub ports, mergers, and alliances – has caused fears of monopoly abuses among shippers and politicians. Such fears are then used as arguments against opening the Mercosur cabotage to foreign companies.

This paper argues that these fears are generally not justified because in spite of the observed process of concentration, the intensity of competition is increasing. Importers and exporters benefit from the prevailing trends because scale economies help to achieve cost reductions, and competition makes sure that these cost reductions are being transferred to the shipper.

The twelve reasons why competition is increasing globally and in Mercosur are:

1. Concentration takes place on a global scale; on individual routes, the number of players may actually increase as carriers expand into additional markets.
2. Shippers have more options due to transshipment.
3. Containerization implies that services are ever more homogenous, which facilitates the entrance of new service providers.
4. Higher fixed costs and lower marginal costs encourage marginal pricing.
5. In order to achieve economies of scale, carriers are expanding their capacity.
6. Through the internet, customers can compare competing services more easily.
7. Traditional conferences are weakened due to deregulation.
8. The counterparts of carriers also merge and form alliances.
9. The cargo carried also competes.
10. Shipping competes with other modes of transport.
11. Inter-port competition has also increased – and not all carriers call at all ports.
12. Due to economic liberalization national players receive less protection.

So far, the process of concentration together with the intensifying competition has been bad news for regional shipping lines and good news for shippers, and this is not likely to change in the foreseeable future. Liner shipping is unlikely to become a natural monopoly. Even if the described developments towards more competition were to slow down or to stop one day, it would still be a long way from actually reversing the trend, leading to monopoly abuses equivalent to the old days of liner shipping conferences and protected national shipping. If for economic and environmental reasons cabotage in Mercosur is to be promoted, opening these trades to international shipping lines should be considered as a viable option.

Introduction: Concentration versus competition

At present, coastal shipping within in Mercosur is not generally open to foreign shipping companies with foreign flags. One of the reasons can be exemplified by the following quote from Fairplay (8 April 1999, page 8), where a Brazilian Ship owner

“warns that international lines have more money to lose than those of MERCOSUR and, if the routes open up, they will be able to drop rates for long enough to knock out the local competition. ‘if we agreed to opening MERCOSUR,’ he said, ‘they will come with low rates and, after they kill us, the higher rates will come back stronger’ ”

This paper argues that **in spite of the process of concentration in liner shipping, the intensity of competition among carriers has increased.** To avoid misunderstandings: concentration in liner shipping is not a cause of intensifying competition, but rather both tendencies are the result of the same underlying developments. Growing trade and globalization have encouraged deregulation of transport services. Similarly, a growing market has encouraged technological advances which help to achieve economies of scale. Deregulation and technological progress contribute to the process of concentration. At the same time, they are also contributing factors to the intensifying competition.

The impacts of both these trends – increased concentration and competition – have so far been to the benefit of importers and exporters. **Scale economies due to concentration have allowed for cost reductions, and the intensified competition has assured that these cost reductions are being transferred to the shippers.** This is also the case in Mercosur and other South American markets, where the expansion of bigger players and freight rate reductions have been particularly strong.

This paper argues that the fears expressed by the Brazilian ship owner quoted above are only partly justified. It is true that some smaller players are likely to be driven out of the market. But it seems unlikely that in the long run freight rates will actually increase as a result. Even if this possibility really existed, it is questionable whether it would justify the protection of smaller players (and with them scale-diseconomies and less competition) at present.

A few basic facts about shipping in Mercosur and South America

Foreign trade and maritime transport

Brazil accounts for almost 70% of the volume of foreign trade of Mercosur. Taking just maritime transport into account, this percentages reaches 78%. All countries export bigger volumes than their imports.

Table 1: Mercosur foreign trade

Country	Direction of trade	Total volume (ton) of foreign trade	% of volume via maritime transport
Argentina	Exports	79 million	82.6%
Argentina	Imports	25 million	76.0%
Brazil	Exports	230 million	97.6%
Brazil	Imports	93 million	93.8%
Uruguay	Exports	4 million	56.1%
Uruguay	Imports	4 million	67.9%
Paraguay	Exports	1 million	48.1%

Source: *Base de datos de Transporte Internacional - BTI, CEPAL. For further information contact Gastón Rigollet, email GRigollet@ECLAC.cl.*

National fleets

With regards to the number of ships of 300 gt and above, Brazil has the largest national flag fleet of South America, followed by Chile, and Argentina. With regards to dwt, Brazil is again number one in South America, followed by Venezuela and Chile.

Table 2: National flag fleet, January 2000

Country	Dwt	Gt	Average age	No. of ships
Argentina	578,917	407,398	22	76
Brazil	6,302,056	3,799,905	18	215
Chile	802,316	576,747	19	82
Colombia	48,985	36,196	27	18
Ecuador	374,297	223,056	25	30
Guayana	1,972	1,040	30	1
Paraguay	24,372	11,986	31	10
Peru	113,937	74,983	8	31
Uruguay	105,393	69,298	18	11
Venezuela	883,292	562,237	24	55

Source: *Perfil Marítimo (http://www.eclac.cl/espanol/investigacion/transporte/perfil/index.htm, March 2000), based on Fairplay. Includes all ships of 300 gt and above, independent of the nationality of the shipping company.*

National shipping companies

Chilean companies are the most active South American international liner shipping companies. Together, they control 36,000 TEU, versus just 21,000 TEU for Brazilian companies, and 7,000 TEU of companies from Argentina. With regard to tonnage, Brazilian companies are far stronger with 9.5 million dwt, because they are more active in the bulk trades, versus 1.6 million dwt controlled by Chilean interests, and 1.1 million dwt by companies from Venezuela.

At the beginning of 2000, the Latin American shipping company which controlled most dwt was Fronape (Brazil), followed by Petrobras (Brazil), Docenave (Brazil), and PdV (Venezuela). The company that controlled most TEU was CSAV (Chile), followed by CCNI (Chile), TMM (Mexico), and Maruba (Argentina).

Table 3: Ships operated by South American national ship operators, January 2000

Country	Dwt	Gt	Teu	Average age	No. of ships
Argentina	1,320,746	847,907	7,316	21	97
Brazil	9,549,423	5,565,774	20,879	18	254
Chile	2,279,926	1,624,357	36,182	17	123
Colombia	99,334	80,282	97	28	29
Ecuador	368,377	218,377	0	24	26
Guayana	13,002	8,172	124	30	7
Paraguay	20,466	10,864	455	28	51
Peru	383,046	249,328	2,318	13	49
Uruguay	16,027	21,985	48	20	10
Venezuela	1,846,649	1,104,081	457	21	66

Source: *Perfil Marítimo* (<http://www.eclac.cl/espanol/investigacion/transporte/perfil/index.htm>, March 2000), based on Fairplay. Includes all ships of 300 gt and above, independent of the flag they use.

Liner shipping services

Most shippers in South America only have reasonable access to ports on one coast of South America, i.e. either the eastern, western or northern seaboard. Some, such as shippers in Mendoza or Bolivia, may choose between one of the two coasts. For such shippers, the ports and shipping services on the east coast offer several advantages with regard to frequencies, costs, and length of journey.

Table 4: Comparison of liner shipping services, east coast and west coast

	West coast: Chile, Colombia (Buenaventura), Ecuador, Peru	East coast: Argentina, Brazil, Uruguay
Ports: number of ports with regular services, January 2000. ^a	Total 13. Chile 7, Colombia 1, Ecuador 2, Perú 3.	Total 25. Argentina 5, Brazil 19, Uruguay 1.
Main ports: number of regular services, January 2000. ^a	San Antonio (Chile) 20 Callao (Perú) 20	Buenos Aires (Argentina) 25 Santos (Brazil) 27
Services: total number of departures, per month, January 2000. ^a	Total: 356, Asia: 74, North America: 221, Europe: 61	Total: 556, Asia: 98 North America: 196, Europe: 273
Movements per service: Estimated average number of teus moved annually per service. ^b	All services: 9,195 Asia: 8,708, North America: 8,093 Europe: 13,125	All services: 12,500 Asia: 10,906, North America: 18,121 Europe 9,302
Journey: Minimum duration of regular services, January 2000. ^a	San Antonio – Singapore: 36 days San Antonio – Hong Kong: 33 days San Antonio – Yokohama: 26 days San Antonio – New York: 19 days San Antonio – Hamburg: 31 days Callao – Singapore: 34 days Callao – Hong Kong: 25 days Callao – Yokohama: 21 days Callao – New York: 14 days Callao – Hamburg: 25 days	Buenos Aires – Singapore: 25 days Buenos Aires – Hong Kong: 29 days Buenos Aires – Yokohama: 35 days Buenos Aires – New York: 16 days Buenos Aires – Hamburg: 19 days Santos – Singapore: 21 days Santos – Hong Kong: 25 days Santos – Yokohama: 31 days Santos – New York: 14 days Santos – Hamburg: 15 days
Frequencies: number of days between departures per service, weighted average, January 2000. (example: a weekly service gives the number 7,0).	San Antonio – Asia: 10.2 San Antonio – North America: 11.0 San Antonio – Europe: 13.8 Callao – Asia: 10.2 Callao – North America: 11.0 Callao – Europe: 13.8	Santos – Asia: 9.6 Santos – North America: 9.4 Santos – Europe: 9.3 Buenos Aires – Asia: 8.4 Buenos Aires – Am. del Norte: 9.7 Buenos Aires – Europe: 9.2
Shipping companies: number of companies which offer liner shipping services, January 2000. ^a	Asia: 08 North America: 20 Europe: 12	Asia: 14 North America: 30 Europe: 23
Ships: Maximum size in TEU, January 2000.	2200 TEU, geared	3428 TEU, gear less
Containerized trade: total container moves, imports and exports, thousand TEU, 1998.	Total: 1131 Asia: 209, North America: 607 Europe: 315	Total: 2200 Asia: 349, North America: 1051 Europe: 800
Balances: Exports/ imports 1998.	Total: 1.11, Asia: 2.48, North America: 0.79, Europe: 1.30	Total: 0.96, Asia: 2.23, North America: 0.68, Europe: 1.07

Source: Own calculation, based on American Shipper (www.compairedata.com, 3 January 2000); Datamar Consultores Associados (lorimer@amcham.com.br, 4 January 2000); DRI/McGraw-Hill WSTS Review, Third Quarter, 1998.

Note: Northern seaboard (Cayenne, Colombia, Guayana, Surinam, and Venezuela) not included

^a Only direct services. ^b Estimate based on services in January 2000 and trade moves in 1998.

Freedom of access

The following is a quoted from **ECLAC's FAL Bulletin No. 155, July 1999** (<http://www.eclac.cl/english/news/Falbulletin/bol155/Fal155eng.htm>):

Study of the similarities and differences in national and subregional legislations as regards freedom of access to cargoes and traffic flows between the countries of the region, or to and from other countries, presented at the Fifth Ordinary Meeting of the Conference of Ministers of Transport, Communications and Public Works of South America, held in Cochabamba, Bolivia, in April 1999.

At the Fourth Ordinary Meeting of the Conference of Ministers of Transport, Communications and Public Works of South America, held in Buenos Aires, Argentina, on 26, 27 and 28 November 1997, Resolution 36 Point 2 assigned the Uruguayan delegation, acting as coordinator of the Working Group on Ocean Transport, the task of carrying out a survey of all agreements and measures that restrict access to the region's cargoes and traffic. Accordingly, a study was made of the similarities and differences existing in national or subregional legislations on freedom of access to cargoes and trade flows both between the countries of the region, and to and from other countries.

Survey of agreements and measures

A survey was made of agreements and measures, using as information base the replies given by the countries involved to the Questionnaire on Ocean Transport Services prepared by the Latin American Integration Association (LAIA) as; in addition, to ensure uniformity of criteria, countries were asked to clarify certain aspects of their respective national legislations that could give rise to restrictive measures.

The following countries answered these questions on aspects of national legislation: Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Peru, Uruguay and Venezuela.

Andean Community

The countries belonging to the Andean Community (Bolivia, Colombia, Ecuador, Peru and Venezuela), and which have ratified the Decisions of the Commission of the Cartagena Agreement, and in particular Decision 314, on freedom of access to cargoes transported by sea and policies for the development of merchant marine in the Andean Com-

munity, have established freedom of access to cargo transport generated by the external trade of the countries of the subregion, subject to the principle of reciprocity. Reciprocity is defined as mutual concessions made by countries or groups of countries to permit access to cargoes carried between them, to or from third countries. (This does not cover the coastal shipping of each member country).

For reciprocity to exist, the free access granted by one country must be matched by the other. This freedom of access to cargoes is total, as indicated by the countries of the Community, since there are no intrinsic restrictions affecting access to their transport market, nor limitations, bureaucratic obstacles or any other similar elements impeding access, even though these may not be directly related to transport.

This total freedom is not absolute, however, as certain limits have to be observed. These relate to the action and conduct of other countries that establish some sort of restriction on free access to their cargoes. When this happens, legal action and conducts arise whereby the country or group of countries affected react against the restriction. The Cartagena Agreement establishes the principle of reciprocity within freedom of access to the freight transport market between the countries of the Community and with third countries.

As an exception, **Ecuador** restricts access to its hydrocarbons and bulk iron ore in complete sea-borne shipments, reserving such transport for vessels operating under its own flag.

Venezuela, while maintaining free access to the transport of its cargoes in general, in a bilateral agreement with the United States exempts cargoes financed by Eximbank. These have to be carried by ships flying the United States flag.

MERCOSUR

In Mercosur, agreements are being drawn up to eliminate the existing bilateral agreements between member countries, with a view to replacing them with a regime establishing free access to regional cargoes traded between member States. Given that the documents have not yet been agreed and are under discussion, it is not possible to give them detailed consideration in this study.

Bilateral Agreements

Bilateral Agreements exist which reserve volumes traded between two countries to vessels operated by the shipping companies of one or the other, on a 50-50 basis. This denies free access to carriers trading partners, unless no carrier from a member country is in a position to carry the cargo, in which case the cargo is made available to carriers of other countries.

Some agreements exclude certain types of cargoes, such as hydrocarbons and bulk liquid petroleum products, and also bulk iron ore, the transport of which is open to ships flying any flag. They also exclude national coastal shipping and transport on inland waterways.

Argentina has bilateral agreements to share cargoes generated by its trade with Brazil and Paraguay, in equal proportions, and also with Cuba, China and Russia.

Brazil has similar bilateral agreements on sharing the transport of cargoes in its reciprocal trade with Argentina, Chile and Uruguay.

Chile has a bilateral agreement with Brazil.

Uruguay has a bilateral agreement on the transport of reciprocal sea-borne cargoes with Brazil; and

Venezuela has one with the United States.

National Legislations

In this regard, in the different national legislations there are no reserved cargoes, or if these exist they are recurrently suspended, except for those arising out of bilateral agreements that are still in force.

In principle, there is freedom of access to cargoes arising from countries' foreign trade transported by sea, but this is subject to the principle of reciprocity as defined above.

Coincidences and Differences

Coincidences. Member countries of the Andean Community that are also signatories of the Cartagena Agreement (Bolivia, Colombia, Ecuador, Peru and Venezuela) coincide in

accepting free access to their traffic and the cargoes arising from their external trade, under conditions of effective reciprocity.

Other countries that are not members of the Andean Community also accept free access to their traffic and the cargoes arising from their external trade, except for the non-application of effective reciprocity and restrictions arising from bilateral agreements on ocean transport that are still in force.

Differences. The most notable differences in free access to cargoes stem from restrictions on certain cargo types. In Brazil, the sea-borne transport of crude oil of national origin, together with basic petroleum products produced in the country and natural gas derivatives, is a national monopoly enshrined in the Federal Constitution.

Exceptions in Ecuador and Venezuela, relating to certain types of cargo and vessel, have already been mentioned in the section on subregional legislation.

Countries that maintain bilateral agreements also establish reserved cargoes in bilateral trade with the countries involved.

Other differences, although not directly linked to cargo access, may also affect such access, such as restrictions on the number of foreigners employed, the involvement of foreign capital in local firms, among others.

Conclusions

Even considering that negotiations have not yet been concluded in one of the subregional integration schemes (Mercosur), the general conclusion can be drawn that there are coincidences among the countries of South America as regards free access to transport of cargoes, subject to the principle of effective reciprocity.

The differences pointed out arise from pre-existing bilateral agreements and restrictions on certain cargo types.

Maritime Safety

One argument against opening up cabotage to foreign competition is the fear of worsening maritime safety indicators. A preliminary study undertaken in 1996 (Jan Hoffmann: "How safe are Latin American Flags? And why?"), with data from 1994 and 1995 from port state control statistics in Europe and the United States, IMO, and Lloyds Register, concludes that *"the available data suggest that the flags of Chile and Panama have a safety record of about world average. Colombia, Brazil, and Uruguay (the latter with a particularly small data base) have safety records that are better than world average. All other Latin American fleets have a least twice as many losses/ casualties/ deficiencies/ detentions than they should have if they had a world average safety record. The worst risk indicators are calculated for Ecuador, Mexico, and Peru"*.

Table 5: Maritime risk indicators for national flags, 1994/1995, world average = 1.0

Country	Maritime risk indicator
Argentina	3.16
Brazil	0.81
Chile	1.00
Colombia	0.78
Cuba	1.97
Ecuador	9.13
Honduras	3.63
Mexico	4.62
Panama	1.11
Paraguay	3.36
Peru	4.97
Uruguay	0.32
Venezuela	2.78
Total Latin America	1.33
Total Latin America, excluding Panama and Honduras	2.07
World average	1.00

Source: Jan Hoffmann, *How safe are Latin American Flags? And why? Working Paper of the Office of the IMO Regional Co-ordinator for Latin America, Santiago de Chile, 1996*

The quoted study is preliminary, and the statistical information can now be considered out-dated. Nevertheless, it has to be noted that at least for the years 1994 and 1995, the so-called open registries did not have worse safety records than Latin American flags in general. Nowadays, port state control is ever more important as compared to flag state control, and it is thus ever more difficult to use the desire to improve maritime safety as a justification towards not opening regional shipping to international competition.

One dozen points why competition in liner shipping is increasing

1. The expansion of major carriers into secondary trades

Although on a global level the number of players is decreasing, **on individual routes, this is more than compensated by the entrance of new players who previously were only active in other markets.** Especially major east-west carriers are entering north-south trades that used to be considered niche markets for specialized liner shipping companies. In MERCOSUR, companies such as Crowley, are even entering the waterway transport of the “Hidrovia”.

Among the reasons for this expansion of major carriers is the need to fill the bigger ships that are being used on the east-west routes. Also, the replaced medium sized vessels are seeking employment in secondary trades. In this context, one curious aspect is the fact that shipping companies sometimes prefer to use the ships themselves because otherwise the buying company receives commercially relevant information about previous uses of the vessel (These records need to be maintained in the ship’s documentation due to international regulations).

In the case of the South American east coast, there are now 14 liner shipping companies competing for cargo for Asia, 30 for North America, and 23 for Europe. This is more than on some east-west routes, and it is a very high density if compared to the number of traded containers.

2. More options due to transshipment

In the past, a shipper in Sao Paulo or Buenos Aires had a given number of regular direct services, but today he has **additional options due to connections that involve transshipment services.**

In addition, a virtuous cycle develops in which more transshipment leads to more routing options, which in turn lead to more transshipment. Once a transshipment service is established, additional shippers will use that option. The process of concentration in shipping leads to relatively stronger east-west carriers who have a strong incentive to fill their main-haul east-west ships by transshipping cargo from the north-south trades.

Although on a case by case basis, it can be discussed whether the additional port and insurance costs involved in the transshipment really outweigh the cost savings on the shipping side, without a doubt, the intensity of competition has increased. In the case of South American west coast cargo, this occurred because of transshipment in Panama, the Caribbean, and the US West Coast. In the case of Mercosur, transshipment of cargo for the US West Coast takes place, inter alia, in Puerto Cabello (Venezuela). Other transshipment ports for Mercosur cargo outside South America are Panama and Algeciras. If, as is expected by many industry observers, in some medium term future more transshipment takes place within Mercosur, for example in Suape, this will also actually increase the number of options available to shippers.

3. Homogenous services

Due to containerization, the services provided by liner shipping operators become increasingly homogenous. Service providers compete increasingly by focusing on cost savings and price reductions rather than specializing on a particular service. By just focusing on price, it is easier for shippers to benefit from the competition because it is easier to compare different offers. All carriers use the same technology (i.e., containers) and are ever less involved in the actual handling and storage of cargo.

The containerization of cargo has reduced the possibility for carriers to compete on quality. Often, it is no longer the shipping company but rather the exporter or forwarder that handles the actual cargo. In the United States and Great Britain, for example, one-third of all cargo is handled by trade forwarders; in Germany it is more than three-quarters. Even if the carrier does fill the container, the actual ocean transport of containers has become a homogeneous service. There is now more competition to sell just the transport of containers, whereas in the past, carriers used to compete on the quality and reliability of cargo handling as well. Carriers are thus confronted with more competing capacity than in the past, when they still had some kind of “monopoly” on their particular service.

Although this trend is not new, it intensifies competition and the perception of over capacity. It is **easier for lines to enter new markets**, using gear-less vessels and without experience transporting a particular type of cargo, because in most ports the same con-

tainers are handled by the same type of ship and gantry crane. As ports in Mercosur have been privatized and new gantry cranes being introduced, the rate of containerization will also continue to increase.

4. Low short term marginal costs

Higher fixed costs and relatively lower variable costs lead to an increasing opportunity cost of not using existing capacity; it **now hurts (i.e. costs) more not to use available container slots, which increases competition among lines to fill the available space.**

For example, the latest Maersk and P&O vessels with a capacity of 6,000+ TEUs imply an initial investment of almost US\$ 100 million, which is equivalent to daily capital costs of around US\$ 40,000.- (Assuming a linear depreciation over 10 years and an interest rate of 10% over the average of the remaining capital). Other examples of high fixed costs include the necessary investment in information and communication technologies, as well as expenditures to comply with international regulations related to maritime safety and environmental protection, such as the International Safety Management (ISM) code and the revised STCW convention.

It is often stated that, provided large vessels are full, they facilitate scale economies. It is also true, however, that if they are not full, the opportunity costs are particularly high and consequently intensify the incentive to sell the existing capacity at a low price – which intensifies competition. To fill the ships on the East-West route, carriers are thus inclined to aggressively attempt to attract cargo from traditional North-South routes such as the ones serving Mercosur.

5. The creation of new (over) capacity

The creation of additional capacity by many shipping lines is happening because these lines anticipate continued growth and because in response to lower freight-rates they are attempting to reduce costs by achieving economies of scale. Thus, the choice of many individual companies to expand their own capacity by adding container slots or by using existing slots more efficiently contributes to a vicious cycle (from the liner's perspective) in which increasing capacity leads to lower freight-rates which leads to **increasing capacity in order to reduce unit costs in response to the lower freight-rates.**

This tendency to build has recently been fostered further by low new-building prices, subsidies, and tax incentives in Germany. Expanding capacity is a long-term decision which anticipates an increase in demand. It is thus only logical that at the beginning some over capacity is created, which will diminish as demand increases over time – unless an unexpected reduction in demand takes liner shipping by surprise, as has happened recently in Latin America.

6. Better informed customers

One of the major aspects mentioned by specialized niche carriers serving secondary markets such as Mercosur is the “I know my market and my clients know me” argument. Trust and individual contacts were crucial in times of specialized services and unreliable legal regimes.

Today, freight rates for homogenous services can be obtained on the internet. In fact, the new (de-)regulations in the USA, which entered into force on May 1, 1999, actually oblige shippers to publish their tariffs on the internet, simultaneously abolishing the need to file tariffs with the government agency. Specific offers can be obtained by phone and fax. **Local presence of a liner shipping company is ever less important**, which increases competition for companies with a traditional local stronghold in Mercosur.

7. Weaker rate setting mechanisms

The **weakening or demise of many conferences makes previously disguised over capacity visible and increases competition**. The difficulty controlling the supply of shipping services has also reduced the possibilities of establishing common rates. From a carrier’s perspective, it thus “creates” over capacity because it becomes more difficult to sell existing space for the same price. Its effect on freight-rates has been significant.

From the liners’ perspective, strong competition might be considered “unsophisticated pricing”. For example, by the end of 1997, ships in the Europe-Asia trades were running at full capacity and still incurring losses, whereas in the transatlantic trades, ship utilization rates were averaging around 80% and the participating lines still managed to generate a profit. Both – the spare capacity and the generated profit – are probably the result of better pricing co-ordination among lines on the transatlantic route.

In the case of the Mercosur-North America route, conferences ceased to be relevant. According to North American shippers, one of the major benefits of the US deregulation is thus just this: the debilitation of traditional liner shipping conferences.

8. Mergers and alliances in other industries

Concentration in liner shipping should not be seen in isolation. Other industries, too, experiences mergers and alliances. This implies that the **liner shipping companies' counterparts, such as shippers, freight forwarders, and port operators, also become more powerful** when freight rates and port tariffs are to be negotiated.

9. The cargo also competes

Not only liner shipping services compete, but also the cargo they transport. Transport is one of the four cornerstones of globalization. Together with telecommunications, trade liberalization and computer technology, the increased efficiency of port and shipping services has made it ever easier to buy and sell merchandise goods, raw materials, and components almost anywhere in the world. Information technology is the basis for the post-industrial service economy. Trade liberalization allows the efficient allocation of resources on a global scale. Finally, telecommunication and transportation are the necessary tools to move information and goods on a global scale. As a recent article in *The Journal of Commerce* rightly emphasizes, "Despite all the headlines and political bluster surrounding the World Trade Organization, NAFTA and other trade pacts, the real driving force behind globalization is something far less visible: the declining costs of international transport" (*The Journal of Commerce*, 15 April 1997).

As a percentage of the value of imports, the total expenditure on transport has decreased from 6.64% in 1980 to 5.27% in 1995, which is a decline of 21% (UNCTAD, 1997, p. 64). This decline, however, does not reflect the true efficiency gains: because of lower transport costs many goods were internationally traded in 1995 which in 1980 could not bear the (then) prohibitive costs of international transport. On the other hand, the relative costs of transport have decreased not only because of increased efficiency, but also because the value of traded goods has gone up faster than its volume.

At first sight it might seem a contradiction to say that in the global economy transport matters more than it did before and, at the same time, that the costs of transport matter ever less. Yet both statements are true: Trade and the necessary shipping services are growing faster than the world's GDP. The same applies to the world total paid for transport services, though not quite as much.

Similarly, while "in theory, a reduction in shipping costs should have resulted in significantly lower physical distribution costs," that has not happened, because the average value of the goods carried is increasing at the same time. Although the costs of transporting these goods may decline, the inventory costs (e.g., depreciation, foregone interest) are rising. In the United States between 1970 and 1994, the relative cost of carrying inventories, measured as a percentage of total physical distribution expenses, rose by 88.2%, maintaining warehouses rose by 17.6% and transportation costs fell by 20.7%. (*Shipping Times* 12 February 1998).

The costs of transporting a final product, such as a car, from one country to another have decreased, yet the **proportion of transport costs within the price of the final product has gone up**. Today, the consumer not only pays for the transport of his new car "made in Germany" from Bremen to New Jersey, but also for the transport of the different parts of this car, which may be made in Mexico and Hong Kong before being transported to Germany to be incorporated into the final product.

Trade and transport thus mutually benefit each other – and the intensity of this mutual benefit is increasing. In the ten years from 1985 to 1994, the pace of global economic integration as measured by the ratio of world trade to world GDP rose three times faster than during the previous decade. This is partly due to the reduced costs of transport. Indirectly, through its impact on global income, this reduction it leads to additional trade and further demand for transport services. Finally, apart from becoming cheaper, maritime transport has also become faster, more frequent, and more reliable, which further promotes merchandise trade.

10. Inter modal competition

Freight rates have not only gone down in liner shipping, but also in other modes of transport, especially air transport. In MERCOSUR, for example, railways have been modernized and liberalization has increased frequencies and reduced prices in air transportation. Most of the growth of intra-MERCOSUR trade is being transported by trucks, the reason being partly that coastal shipping within MERCOSUR is still protected from foreign competition (with resulting higher rates), and Customs procedures above all in Brazilian ports seem to be more cumbersome than necessary.

11. Inter port competition

Not all lines call at all ports. Hence, **if inter-port competition is intensified, this also implies that the lines serving different ports are confronted with stronger competition** for cargo from the ports' common hinterland. For a few trades, shippers can even choose between the east and the west coast of South America. In Latin America, competition among ports has increased for five reasons:

First, in-land infrastructure has improved. Railways have been privatized and modernized, intermodal connections have improved, and new road maintenance systems have reduced the number of potholes.

Second, economic liberalization has made imports and exports via foreign ports easier. Chilean and Peruvian ports are competing for Bolivian cargo, Montevideo in Uruguay is handling cargo for neighbouring countries, and half of Central American imports are transhipped in Panama.

Third, new and privatized ports have been established. Ports like MIT in Panamá or Exolgán in Argentina have added new options for shippers.

Fourth, due to increased transshipment, shippers can use different ports and get their cargo to its final destination, even if the chosen port does not receive a direct service.

Fifth, decentralization and commercialization has added incentives for ports to actively seek cargo from shippers and encourage low freight rates from shipping lines.

Table 6: Port traffic in 10 major South American ports, TEU, 1998

Port	Country	Teu
Buenos Aires (including Exolgan)	Argentina	1,139,730
Santos	Brazil	799,476
Puerto Cabello	Venezuela	486,774
San Antonio	Chile	415,001
Guayaquil	Ecuador	407,434
La Guaira	Venezuela	302,333
Cartagena	Colombia	277,686
Buenaventura	Colombia	275,765
Montevideo	Uruguay	265,892
Valparaiso	Chile	255,687

Source: *Perfil Marítimo*, <http://www.eclac.cl/espanol/investigacion/transporte/perfil/index.htm>

Competition between these ports – and the lines that serve them – is being intensified in the context of the ongoing port decentralization and concessioning process.

12. Trade liberalization

Until the beginning of the 1980s cargo reservation protected the Mercosur and other Latin American shipping companies from foreign competition. These cargo reservation regimes are now basically a thing of the past.

Governments and regional organizations are attaching a greater priority to the promotion of trade through improved and less expensive transport services. They are also increasingly **hesitant to protect national maritime industries**. The attitude of governments and their national cartel offices towards mergers and acquisitions has become less adverse because national players have to compete globally.

The government's desire to promote trade thus implies fiercer competition for national shipping companies. On the other hand, it should also encourage governments to allow more vertical and horizontal integration on a national level so as to allow national companies to compete on the international level.

Which points are most important?

The above points are not ranked in any way. On a global and long term scale, probably the introduction of containerization (point 3, page 13), globalization and the competition of cargoes (point 9, page 16), and intermodal and interport competition (points 10 and 11, page 18) have perhaps the strongest long lasting impact.

In the specific case of secondary markets such as Mercosur, the additional option of services with transshipment is probably most important at present (point 2, page 12). In the last decades, the abolishment of cargo reservation regimes in Latin America has had the most important regional impact (point 12, page 19).

Some other points are rather transitory and will become less strong in future. The “over capacity” as perceived by many carriers should go away one day and with it the tendency of marginal pricing (points 4 and 5, page 14) . The expansion of global carriers into secondary markets will automatically stop once everybody is in it (point 1, page 12); thereafter, consolidation may also happen there.

Other tendencies could become stronger in future. If cabotage traffic is liberalized on a national level – including the USA and its anachronistic Jones Act – and on a regional level in MERCOSUR this would again intensify competition. In the very long term future, new technologies (fast containerships, new modes of inland transport, further scale economies in information technologies) could open entirely new playing fields for competition.

Competition now – monopolies later?

The process of concentration is of course not unique to Latin America. In other regions, too, mergers and alliances have led to the disappearance of smaller liner shipping companies. This, in turn, is arousing fears of future monopoly abuses. Even the business friendly journal *Business Week*, in a recent *Economic Viewpoint*, referring to the global process of concentration in general, warned that “*the big problem with these gigantic mergers is the growing imbalance between public and private power in our society*” (*Business Week* 25/1/1999).

In liner shipping, in the past and up to now, the process of concentration has gone hand in hand with fierce competition and lower freight rates. Nevertheless, some argue “*that the resultant pressure on rates could bring a short-term advantage for shippers, but in the long term would destroy the profitability of liner shipping. Smaller carriers would probably go to the wall, conferences would collapse, and only a handful of powerful carriers would survive. The interest of small shippers would probably suffer as a result.*” (ITJ 26/98). Similarly, “*a global alliance of ship owners serving one port on each continent with two or three gigantic vessels...*” is considered to be part of a “*futuristic horror scenario*” (ITJ 21/98). In defence of traditional conferences, it is argued that “*if an all against all situation continues to prevail and co-operation bears, a priori, a stigma of market abuse, the future in global transport is likely to belong to the oligopolists*” (ITJ 5/99).

Similar fears are being expressed by liner shipping executives serving Mercosur and other Latin American countries. Nobody can deny that – up to now – shippers have benefited from lower freight rates and more service options due to transshipment and global networks. However, it is argued that this is not to last, and that in the long term companies such as *Libra*, *Alianca*, *Transroll*, *Di Gregorio* will/ had to either grow themselves, be driven out of the market, or be absorbed by other companies. Once this has happened, the “big” players will be able to abuse their market power and raise freight rates to the detriment of shippers (see quote on page 3).

Organizations such as the European Commission, the US Department of Transportation, or (slightly less influential) ECLAC in Latin America that have contributed to the

disappearance of conferences and thus encouraged mergers and alliances, will find themselves in the situation of the **sorcerer's apprentice who can't control the ghosts he woke up in the first place.**

I believe that this feared future scenario is a possibility, but a very unlikely one. Above, twelve points were described which have so far led to an increase in competition. Liner shipping is unlikely to become a natural monopoly, similar to the software industry (Microsoft), chip production (Intel), or aeroplane construction (Boeing and Airbus), because compared to these industries entry is relatively cheap and easy so long as it is not restricted by oligopolistic agreements. Even if the described developments were to slow down or could be stopped, it would still be a long way from actually reversing the trend, leading to monopoly abuses equivalent to the (bad) old days of liner shipping conferences.

In the future, organizations such as the European Union, the US Department of Transportation, national anti-monopoly commissions, and also the World Trade Organization WTO will have to **follow the process of concentration closely to assure that there will be no limits of entry into the market for liner shipping services.**

A note of caution

One final note for the "big" players: Yes, it is true that this document has argued that alliances, mergers, and global networks are as a whole beneficial for Latin American importers and exporters. Equivalently, ever lower freight rates have so far benefited the regional and global economy. But with this I am **not supporting the common complaints of liner shipping executives** about insufficient freight rates and unsatisfactory rates of return.

The rates of return that can be made in shipping need to be compared to global interest rates, and these have reached historical low levels as well. And freight rates simply have to go down in line with technological progress and economies of scale. Other industries commonly associated with the globalization of the economy have experienced far stronger price reductions. The cost of a three-minute telephone call between New York and London has fallen from US\$ 300 in 1930 to few cents today. The cost of computer processing has fallen by an average of 30% per year terms over the past decades.

Will the process of concentration continue to go hand in hand with lower freight rates and increased competition? As explained above, most underlying trends can be expected to continue. But the more cautious commentators, such as the ones quoted above from the ITJ, also have their point: When shipping companies realized that the previously expected growth forecasts for Mercosur traffic has been overly optimistic, most lines have withdrawn capacities and freight rates have started to go up again and recovered some of the ground lost previously.

Concluding remarks

Brazil has a bigger interest in protecting its national shipping companies, ship yards and national flag fleets than its Mercosur partners. Its market share in world shipping markets is bigger than its market share in foreign trade. In the case of Argentina, Paraguay, and Uruguay, the priorities are different: They depend relatively more on foreign trade, and have less of a national shipping industry to defend. (See Perfil Marítimo, “Perfiles Nacionales”, <http://www.eclac.cl/espanol/investigacion/transporte/perfil/index.htm>). In this regard, it is not surprising to find that Brazil maintains more bi-lateral protectionist maritime agreements than its Mercosur partners.

This paper does not provide a complete argument in favour or against opening cabotage in Mercosur to foreign competition. Many different aspects will have to be taken into account before taking such a decision. The advantages of reducing maritime transport costs will have to be offset by possible disadvantages with regard to employment in the national shipping and ship building industries. Answering the question of whether or not cabotage should be liberalized requires a detailed economic impact study of the entire maritime industry.

However, in no case should the proclaimed desire to protect and promote competition be used as a pretext to actually reduce competition.

Some further reading

- Burkhalter, Larry: **Privatización Portuaria: Bases, opciones y consecuencias**; in Spanish, ECLAC, Naciones Unidas, LC/G.2045-P, Santiago de Chile
Final book of Larry Burkhalter before his retirement from ECLAC's Transport Unit
- Hoffmann, Jan: **How safe are Latin American flags? And why?** 17 pages, working documents of the IMO office of the regional co-ordinator for Latin America, Santiago de Chile, 1996.
Some preliminary comparisons of Latin American maritime safety indicators.
- Hoffmann, Jan: **Concentration in Liner Shipping: Its Causes and Impacts for Ports and Shipping Services in Developing Regions**; 100 pages, ECLAC document LC/G.2027, Santiago de Chile, 1998.
Analyses the causes and impacts of the process in concentration.
- Hoffmann, Jan: **Concentration in Liner Shipping: Causes and impacts**; 7 pages, DRI McGraw Hill World Sea Trade Service, Third Quarter, 1998.
A summary and continuation of the previous document.
- Hoffmann, Jan: **Privatización Portuaria en America Latina**; 88 pages, in Spanish, Working document, Santiago de Chile, 1999
Looks at determinants and results of port modernization and privatization in Latin America.
- Hoffmann, Jan: **In spite of concentration in liner shipping: One dozen points why competition is increasing in secondary trades – the example of Chile –**; 20 pages, presented to Terminal Operation Conference in Genoa, May 1999
Argues that in Chile competition in liner shipping has been increasing in spite of the observed process of concentration
- Hoffmann, Jan: **Latin American Ports after the privatizations**; 10 pages, presented to PDI Port Privatization conference in London, September 1999
Undertakes to identify a "Latin American Model".
- Hoffmann, Jan: **The potential of Hub Ports on the South American Pacific coast**; 12 pages, presented to LLP Port Privatization conference in Lisbon, February 2000
Claims that the potential of hub ports in Chile, Ecuador and Peru is very limited
- Rezende, Sidney: **Course on Port Modernization**; 62 pages, ECLAC, LC/G.2031, available in Spanish and in English, Santiago de Chile, 1998
Document to support a course on port modernization, which is being given in developing countries to promote private sector participation and port labour reform.
- Most of the documents can be viewed in ECLAC's Perfil Marítimo de América Latina y el Caribe, <http://www.eclac.cl/espanol/investigacion/transporte/perfil/index.htm>. Otherwise contact BDonoso@ECLAC.cl



