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Competition from East Bloc Fleets

East European merchant fleets have been undercutting the conference rates of western liner companies by as much as 60 p.c. and are engaging in major expansion programmes, thereby causing great concern to shipowners in the western countries and the Federal Republic of Germany in particular. Are the privately operated western merchant fleets in danger of being ousted by the East bloc fleets?

More Urgent Need for Political Initiatives

by Dr Bernd Kröger, Hamburg *

Western shipping circles are referring more often and more insistently to perilous competitive pressure by the fleets of the COMECON states and, more especially, the USSR. In the Federal Republic, Great Britain, Holland and Norway this discussion about the policy of the state-owned shipping enterprises of the eastern countries and their growing influence on the liner markets is now conducted more and more often in public. The problems involved have even been raised in the Deutscher Bundestag (Lower House of the German Parliament) through a question tabled by the opposition parties. The East bloc media reacted immediately with fierce attacks on western shipping representatives. Apart from complaining

about "transparent anti-communist indoctrination", they denied that there had been any dumping and remarked that the USSR and other COMECON states together owned no more than 7.5 p.c. of the world's merchant fleet at the middle of 1975.

What are the relevant facts? The state-owned shipping enterprises of the socialist countries and the USSR in particular are developing an increasing activity in the cross trade between western countries. They are forcing their way into the liner markets by undercutting the conference rates by varying margins and methods. The OECD liberalization code ensures free access to the markets and ports of the western countries for all fleets. The East bloc states are however at the same time holding on to their

own cargo monopoly and "in the interest of the socialist external economy" making preferential use of their own tonnages.

Intrinsic Cost Advantages

The East bloc fleets are profiting from cost advantages inherent in the economic system of their countries. The state shipping enterprises of the socialist economies have a place in the wage-incentive and performance-control systems of the state-directed economic groupings but their investments are largely financed from budget allocations, amortization rates are low and interest charges on capital mostly a formality because — as Böhme in particular recently pointed out correctly in "Die Weltwirtschaft" (2/1975, p. 138) — sea-going shipping has been zero-rated for the per-

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tinent interest charge. Moreover, special accounting systems apply to sea freight earnings in foreign currency instead of the cost-earnings ratio pertaining in general, with the result that even low rates can yield a profit. The shipping enterprises in the East bloc countries can therefore gear their business policy to factors in no way comparable to the profitability considerations applying in market economies where firms must calculate according to commercial criteria.

It is hardly surprising that this basic difference is reflected by an aggressive rate policy of East bloc shipping enterprises on routes where they find free scope. The Council of European & Japanese National Ship-owners' Associations (CENSA) has carried out investigations showing that the COMECON fleets, and especially the USSR fleet, have undercut the rates in various routes by between 10 and 60 p.c.

Threat of Overwhelming Competition

The East bloc shipping companies reject the charge of rate dumping. Nevertheless it must be said that no matter what economic theory is accepted as valid for a definition of the term "dumping", it makes little change for those directly affected. It is not to be denied that price differentiation and rate undercutting are practised as instruments of market economy competition, that they are part of the free scope allowed in market economies. But as far as the competition from the COMECON and the USSR in particular is concerned, at issue is not the method as such but the extent to which it is being used — competitors may be ousted from the market completely — and the conditions under which the parties engage in the competition.

Anybody who enjoys the cost advantages of a system which refuses to accept the competitive methods of the market economy within the compass of its own system but at the same time claims for himself a right to avail himself of the liberal competitive methods of another system without accepting the cost conditions of this other system is capable of underbidding the cheapest bidder from the industrialized countries by 20 points or more *whatever* the rate level may be. Since the conditions underlying the bid are different, it goes without saying that he can align his offer of services to his own supply potential and his own aims and adhere to this policy for many a long day, if necessary until he has ousted his competitors. Decisive from his point of view is not primarily the ratio of costs and earnings which is crucial to his rivals in the "competitive markets" but the market share which he has independently determined as his target.

Largest General Cargo Tonnage

Starting from this basic point and bearing in mind the quantitative relations of the supply potential of the East bloc fleets, their growth rates and especially that of the Soviet merchant fleet must be a matter of concern even for heedless optimists. Many figures have been quoted in the discussion, and these can of course be arranged in various ways. The often quoted ratio of the total COMECON fleet to the world merchant fleet (of "only" 7.5 p.c.), for instance, bears no relevance to the competitive pressure of eastern shipping enterprises on liner shipping, for the East bloc ratio on the liner routes was 12.8 p.c. at the middle of 1975; with 7.3 mn grt the USSR on its own has today the largest fleet of con-

ventional general-cargo vessels in the world.

If all sea-ships on order in the world are taken into account, it becomes clear that the state trading countries — foremost amongst them again the USSR — have the intention of engaging also in future predominantly in liner shipping. Inquiries last year showed the COMECON countries to account for 4.7 p.c. of the orders on the books of the world shipbuilding industry; for the liner tonnage alone their proportion was 16.9 p.c.

An inquiry into the reasons for this policy of fleet expansion shows a number of disparate and mostly general economic criteria to play a part. There is the aim of carrying the foreign trade merchandise and the economic and military aid deliveries to socialist countries and "friendly" states in Africa, Latin America and Asia as far as possible in own vessels. Besides, the outlays in foreign currencies are to be kept down and earnings in foreign currencies to be increased; the latter in particular are to develop into a copious source of revenue over the long term. Last not least, the merchant fleet is to be employed as an instrument of foreign and security policy and to be made use of for establishing and developing an economic-strategic presence on the oceans of the world.

How greatly such arguments influence the East bloc shipping policy is indicated by the structure of merchant fleet, especially in the USSR. Roll-on/roll-off and container ships and conventional general-cargo vessels are playing a much greater logistic role than bulk carriers. The fact that the USSR is largely self-sufficient in regard to raw material supplies explains why in intra-Soviet sea shipping also more bulk carriers are being used than liner tonnage. About

40 p.c. of the Soviet fleet are reportedly plying between USSR or COMECON ports, but this is certainly not the figure for liner shipping.

The sea-borne foreign trade of the USSR is small in relation to the size and structure of its own fleet, and there are revealing examples indicating the ratio of own cargoes on Soviet vessels to the tonnages carried between third countries. The German Shipowners' Association last year investigated the nature and extent of the East bloc competition on a large number of liner routes. In 1973, the year covered by the investigation, the Soviet line, which at that time operated only a four-weekly service, carried about 94,000 tons of general cargo on the so-called Hamburg/Antwerp range to the West Indies and Central America. The same ships carried during the same period no more than 600 tons from Leningrad. West European lines did not obtain any cargoes in Soviet ports.

Call for Action

In the light of Soviet statements about the new Five Year Plan period it is to be expected that the USSR fleet will grow further. There has certainly been no mention so far of voluntary self-restraint.

These developments have provoked the mentioned reactions from the affected shipping companies and the political authorities. There have been louder calls for "active measures". The initially defensive counter-reaction of spokesmen for the Soviet shipping policy only added fuel to the joint plea for government measures on the basis of extant or if necessary new enactments and ordinances.

Certain instruments are already at hand. The German legislation on external economic relations allows in principle of compulsory licensing of sea-shipment contracts and the subjection of foreign trade licences to certain stipulations as regards the mode of shipment. The US Congress is discussing bills which would impose on "third flag carriers" who undercut the lowest rates offered for ships from the countries of dispatch and destination the duty to prove that the cost of their services is fully covered. National regulations in Great Britain and other European states likewise permit protective intervention. Furthermore, the UN Code of Conduct for Liner Conferences could be used as a lever for tackling these problems. Political instruments however, no matter to what catalogue of measures they may

eventually lead, can only be effective if several countries take them at the same time and move on substantially parallel courses.

Port Objections

It will be seen at this point at the latest that the interests of the shipping industry may conflict with other economic interests in the western shipping countries. Objections may be raised in particular on behalf of the ports. Those concerned with port operations are afraid that they may in consequence of defensive government measures have to bear the loss of transit cargoes from the COMECON states which in Hamburg for instance at present account for about 6 p.c. of the traffic passing through the port. It is certainly difficult to weigh up such different interests and settle political priorities. Nevertheless it may be doubted whether a largely coordinated action by the West European governments against non-commercial methods of competition as desired by the shipping industry would really have a significant impact particularly on Hamburg's transit traffic.

For a port is made attractive and interesting to shippers by the density and frequency of its liner services, by the quality of its harbour, dispatch and forwarding services. On account of these qualitative factors the countries behind the Iron Curtain will in the foreseeable future have to depend on shipments through foreign ports, for instance via Hamburg, for their foreign trade because these provide more numerous and far more frequent liner services than the COMECON ports. A much larger volume of foreign trade than the COMECON countries command would be needed to justify diversion of the shipments to a port in their own sphere of influence and substi-

Table 1
Eastern Bloc Fleets — Analysis by Principal Types

	Oil Tankers Tons Gross	Ore & Bulk Carriers Tons Gross	General Cargo Inc. Passenger/ Cargo Tons Gross	Container Ships (Fully Cellular) Tons Gross	Passenger Liners Tons Gross
Albania	—	—	57,068	—	—
Bulgaria	288,567	187,763	270,395	—	13,581
Czechoslovakia	—	81,993	34,155	—	—
German Dem. Rep.	172,078	152,377	625,988	—	12,068
Hungary	—	—	49,150	—	—
Poland	38,244	824,819	1,105,406	—	15,044
Rumania	150,653	207,065	150,078	—	—
USSR	3,658,025	482,650	6,854,104	48,156	251,690
Total	4,307,567	1,936,667	9,146,344	48,156	292,383

Source: Lloyd's Statistical Tables — November, 1974.

tution of a wide range of own services.

Western governments have often given priority to their interest in foreign trade when considering concrete measures for the protection of their national fleets against discrimination and similar practices in sea-shipping by their trading partners. It is often ignored that the principle of equal participation on a commercial basis can be safeguarded for the shipping industry without detriment to the foreign trade if the governments act with appropriate pertinacity. This is no less valid for the relations with the East bloc than elsewhere.

Code of Conduct for Liner Conferences

The UN Convention on a Code of Conduct for Liner Conferences was adopted with a large majority in Geneva in April 1974. One of the reasons why this was possible is that the shipping interests were given as much consideration in this code as the foreign trade interests of the large majority of the participating countries. As regards the distribution of cargoes the Convention is based on the principle of equal rights for the national fleets. It ensures that third flag carriers receive an appropriate proportion of the cargoes, and should therefore be regarded as a model for cooperation also with the liner operators in the East bloc countries, the more so as important COMECON states like the USSR and the GDR have signed the set of treaties as have France, Belgium and the Federal Republic among West European countries.

A resolution which may be considered to be practically an appendix to the Convention says that the governments are not free to take measures to obstruct competition by outsiders as long as these outsiders

conduct their competition with the liner conference companies fairly and according to commercial criteria. This resolution was adopted unanimously, by the East bloc states together with all others.

Growing Dependence

With all due understanding for the fact that shippers take a certain interest in the quotations of COMECON lines which are in part much more favourable, one must not overlook one crucial point: On most of the routes on which they are operating as outsiders the shipping enterprises of the East bloc go in for the more remunerative cargoes, i.e. general high-value goods for which the conferences are charging higher rates in order to encourage a healthy freight mix. This has the effect of lowering the average remuneration of the conference lines so that the conference members are obliged to raise their rates in order to avoid getting too deep into the red. In different circumstances there would be less or less frequent need for this.

So the first ones to suffer are the shippers of the less valuable

general cargoes. Another consideration needs taking into account for the long term, namely the increasing dependence of western industry on the willingness of East bloc shipping lines to go on carrying its goods at low rates when they have gained a larger share of the market for themselves.

Necessary Political Activities

The Federal Government also seems to take an increasingly critical view of the activities of the East bloc fleets as may be inferred from various statements by public personages including the State Secretary in the Federal Ministry of Transport and is shown in particular by the answer of the Federal Government to the parliamentary question tabled by the opposition parties. In spite of the conditional clause one is probably not going wrong in interpreting the explicit reference to the Government's readiness to take "the requisite measures" if required by developments as a clear political hint that activities — political activities — will be undertaken to avoid such an unwelcome development.

Table 2
Eastern Bloc Fleets: Containerships and other Specialised Tonnage on Order as at February 1975

Type of vessel	Country	No.	Tonnage (DWT)	Capacity	Speed (Knts)	Delivery date
1. Fully cellular ro/ro vessels	USSR	1	13,500	324C	17	?
		4	13,000	304C	19	?
		1	24,000	1,000C	22	1975
		3	15,000	700C	22	?
		10	13,300	798C	22	1975-1979
		2	21,000	1,100C	22	1975
		2	21,650	1,400C	23	1975
		3	17,500	774C	20	1975
		6	16,000	550C	23	1975-1977
		2. Barge/seabee	USSR	2	36,000	26B x 1,300 DWT
3. Semi container-ships	USSR	40	—	9,946C Total	15-23	1975-1976
	East Germany	8	—	1,920C Total	22	?
	Poland	5	—	793C Total	15-22	1975
4. Passenger/car ferries	USSR	38	4,000-15,000	—	12-21	1975-1979
	Poland	3	2,000- 6,200	—	16-20	1975-1977

Source: Fairplay International, World Ships on Order.

The Federal Government is in this context speaking of bilateral shipping agreements and regards these as *one* suitable instrument for the harmonization of the various mutual foreign trade and currency interests with the COMECON countries and the USSR in particular. It may be said that the conclusion of a bilateral sea-shipment agreement with the USSR is certainly desirable as a means of achieving really equal participation by the two fleets in the mutual goods exchanges. For at present we are still far from

having reached such an equal status. It should be noted that the USSR has concluded similar shipping agreements with other West European countries and obtained in these practically unilateral guarantees which give it free access to the ports of the other contracting party also in regard to traffic to and from third countries. A mutual right of free movement can probably be achieved in relation to the USSR, at best, only on a bilateral basis.

In view of the need for coordination of possible defensive

measures at least with the neighbouring states and the fact that such coordination usually involves a political process which is anything but brief, a hesitant approach would be a step backward. The urgency of the problem is shown clearly by the mentioned figures about the development of the liner tonnage of the COMECON states and especially the USSR. It is to be hoped that the authorities concerned will appreciate how urgent this problem is and show themselves willing to draw the appropriate conclusions.

No Cause Yet for State Measures

by Helmuth Kern, Hamburg *

There are people who describe the recent activities of the big German liner shipping companies concerning, or rather against, the COMECON flags as part of a public relations exercise designed to acquaint the German public with the international liner shipping problems and to campaign for the retention of the conference system. In this context, they say an exaggerated account and assessment is given of the activities and the expansion of some East bloc fleets.

I cannot endorse this version nor can I reject it. For there exists no certain information yet about the problem of the competitive situation between eastern and western shipowners although the German liner companies are known to have on average earned good profits again in 1975; according to Hamburgische Landesbank the

past year has actually been an outstanding one for some liner operators. If one reads besides that the large Norwegian shipping company of Wilh. Wilhelmsen has informed its shareholders that the last year has ended with a profit close to that of 1974 and was thus one of the best in the company's history, and that this success was due to its engagement in the liner trade, one will suspect that the German and western shipping companies issue their Cassandra-like warnings largely for prophylactic purposes.

Lack of Precise Information

Statistics are known to make excellent ammunition but many of the figures mentioned in recent discussions need correlating with others or even correcting. That applies to both sides, especially if comparable figures which would cast an unfavour-

able light on the own position are omitted. The interested observer will also note certain inconsistencies. He may for instance wish to ask the liner operators how they account for the 13.5 p.c. hoist of freight rates on the Europe/East Asia route from March 1976 in the light of their complaints about large tonnages being lost to the Trans-Siberian rail route.

The claim that western merchant fleets are facing a growing threat from the COMECON flags should be taken seriously but has not yet been sufficiently proved because of lack of exact data, comparable statistics, neutral studies and conclusive statements by other interested parties. This lack of information makes it in my view at the present juncture impossible to indi-

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