Research of protectionism in shipping policy

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RESEARCH OF PROTECTIONISM IN SHIPPING POLICY

by

JUNG, YOUP-SUB
(REPUBLIC OF KOREA)

A Paper submitted to the Faculty of the World Maritime University in partial satisfaction of the requirements for the award of a

MASTER OF SCIENCE DEGREE
IN
GENERAL MARITIME ADMINISTRATION

The contents of this paper reflect my personal view and are not necessarily endorsed by the University.

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INTRODUCTION

Purpose and Task

As many countries recognized the important role of shipping in economic development, every government has had a great concern related to promote merchant marine. Most government, especially in the developing countries, easily have adopted protectionist shipping policies but experienced the failure of shipping and economic development. Despite of bad result of protectionism, there are still strong trends to follow shipping protectionism.

On the other hand, there are another opinion which is against government intervention and based on basic international economic theory. Since shipping has international characteristic, both policies are discussed internationally to achieve world shipping development.

In the case of policy-maker, it is important to adopt adequate policies which contribute to national interest. Because of this, we have to analyse the effect of past policy and find the future solution.

Therefore the first part of this paper is devoted to comparison between protectionism and liberalism and check the validity of protectionism through economic analysis. Part II concentrates my country’s (The Republic of Korea) policy as a case study.

Accordingly, the primary concerns of this paper go to the following questions regarding shipping protectionism:
Firstly, what are the reasons to support protectionism or liberalism?

Secondly, is it reasonable to adopt protectionism in the developing countries? If not, what kind of solutions are recommended?

Thirdly, what is needed for international shipping development?

Finally, what is the correlation between protectionist policies and S. Korean shipping and what policy is recommended to S. Korea?

Limitation and Scope of the Research

In observation of the major economic and political factors in shipping, the study does not cover all factors involved in protectionism, but concentrate on the theory and effect which are related to the subject matter.

Furthermore, in the discussions any detailed explanation and justification of ideas and thoughts which are generally accepted are excluded in order to avoid the voluminous content of the paper.

There are many limitations in collecting accurate and updated information and data. Much of it was collected from various publications, periodicals and seminar papers.

Finally, the scope of this research is limited to the study of cargo reservation and flag discrimination which are the main debatable areas. Even though subsidies and other protectionist policies distort the division of labour, the study excludes that part. The reason is that
it is not restraints in the proper sense of barriers to cargo access. In addition, it is difficult to get information related to subsidies from various governments. However, I deal with financial subsidies in the case study of S.Korea for which I got proper information.

Methodology

This research has been conducted mainly through two different methods, that is, library research and practical research.

Library research was undertaken mainly at the library in the World Maritime University.

Practical research was fulfilled during various field trips, on-the-job training in several countries. This practical research includes personal interview with many experts, professors and visiting professors from different institutions and organizations as well as colleagues at the World Maritime University.
PART I: PROTECTIONISM AND SHIPPING INDUSTRY

Theoretically, in shipping, especially bulk shipping, there exists the same economic mechanism as in any other economic activity.

According to most economic books, the price of goods is determined by demand and supply. Provided that the demand curve slopes downwards and the supply curve slopes upwards, the curves intersect at point E in Figure 1.1.

(Figure 1.1) EQUILIBRIUM MARKET PRICE

At this point, equilibrium price OP and equilibrium quantity OQ are determined. A higher initial price such as OP1 results in excess supply which forces the price down.
a lower initial price such as OP2 results in excess demand which forces the price up. Only at price OP are buying and supply intentions fully synchronized. (1)

An illustration will show how operative forces work in a miniature shipping market. If for a specific loading date within a limited area there are 10 ships open for employment, but there are only 9 cargoes offered, there it is very likely that none of the vessels will obtain a higher freight rate than the lowest rate and one of the respective shipowners is willing to accept. In the reversed situation, where there are 10 cargoes available but only 9 ships one can expect every ship which is fixed to obtain better terms than the preceding one. (2) Therefore, the equilibrium will change by the law of supply and demand.

However, in practice this market equilibrium could be distorted by the external power. In shipping, there are lots of factors which influence the market as well. A monopolistic situation in the demand or supply side is one of the main factors. However, among these factors I will concentrate on government intervention. The current tonnage surplus situation and dispute at an international level are generated by different shipping policies in respective countries as one of the decisive factors.
Chapter I : THE REASONS FOR GOVERNMENT INTERVENTION IN SHIPPING

Why is every government interested in shipping promotion? The reasons are different due to the situation of each country. However, many governments are adopting promotional policies because shipping has some important functions from an economic point of view.

Without detailed analysis of economic effects, the following functions of shipping are generally accepted.

1.1 Trade Expansion Effect.

According to an estimate by the International Monetary Fund, the costs of sea transport may be taken as accounting for up to 10 percent - on average - of the value of international seaborne trade. Statistically, the amount of goods moved by sea account for 88% of world trade (tons), 92% ton/km and 79% by value. This shows that there is a close relationship between trade and shipping.

The fact that there is no 'original' demand for cargo shipping services underlines the close link between trade and shipping. Not only does shipping serve the demand for cargoes, it actually stimulates demand for shipping by making distant markets accessible, the precondition for international division of labour. (3)

Since shipping services can accelerate the rational use of means of production, for example land, labour and capital, through overcoming natural barriers, it is possible to increase production and decrease cost. At the same time,
it influences the production and consumption of economic factors, thereby facilitates international economic activity. Therefore, countries are able to stimulate the rate of growth of their economies and to raise the welfare of their population through trade.

If there were no international transport services in a country, her economy would become self-sufficient and use of national resources inefficient. In the case of some countries, for example, Japan, S.Korea and Taiwan, which transport most export and import cargoes by sea due to their geographical location and scarcity of natural resources, shipping and trade influence each other enormously.

Some policy-makers in the developing countries are generally of the opinion that their economies are suffering from the lack of and monopoly in shipping services, which hinders their effort to expand trade.

1.2 Balance of Payment Effect

In most cases, suppliers of shipping services require freight payment in foreign currencies and demanders have to pay in foreign currencies. Therefore, certain country can save foreign exchange and solve the problem of the balance of payment by expanding merchant marine services. In other words, merchant marine activities result in the saving and earning of foreign currencies whether used in transporting national export-import cargoes or cross trade cargoes.

This contribution to the balance of payment can be offset
by some cost, such as port charges and bunker costs, as disbursements abroad. According to the UNCTAD report, only 30% of gross foreign exchange savings represents actual net savings on the basis of a conservative estimate. (4)

1.3 Employment Effect

Shipping also creates employment opportunities like other industries. However, it is often claimed that shipping is not in itself adequate for the creation of jobs as it is a capital intensive industry and requires trained personnel.

When the developing countries invest in shipping, they ought to realize that they have comparative advantages in labor costs. Therefore, they can employ a large number of personnel on their own vessels, foreign vessels and in the long run managerial posts.

In addition, shipping development is connected with other industries; for example, shipbuilding, insurance, brokering, finance and banking services, and port services. If we consider these aspects, the overall employment would be far greater than considering shipping activities only.

1.4 Political and Strategic Objectives

Besides the above factors, S.G. Sturmey suggested the following objectives for a national shipping policy:

i) To promote and protect a merchant marine for defense purposes

ii) To establish a merchant marine capable of transporting
the country’s essential trade in order to avoid the disruptions consequent upon wars in which the country is not participating

iii) To satisfy national prestige

iv) To enable an infant merchant marine, which will eventually be able to dispense with assistance, to become established

v) To foster trade and communications between the country concerned and other countries.

In respect with strategic objectives, I do not agree with S.G. Sturmey. It has been argued that a country needs an experienced merchant marine in case of war and that this industry should be fostered by protectionist policies, even though it could be less efficient than that of the foreign competitor.

I feel that the country concerned would be supported by friendly nations in times of emergency. Only a few countries need a fleet for strategic reasons. In most countries the protectionist measures introduced in order to serve defense objectives have in fact little defense content but economic content. Therefore, it is unreasonable to waste the nation’s wealth for a very uncertain occurrence in the developing nations. This kind of concept will underestimate the economic value of shipping.
Chapter II WHAT IS PROTECTIONISM?

Before going on to analyse the validity of protectionism as a topic of this paper, it is important to define accurately the meaning of protectionism in this paper.

2.1 Definition of Protectionism

Generally speaking in international trade, protectionism refers to the protection of domestic industries from foreign competition. Such protectionism may be achieved either by tariffs that raise the price of foreign goods, or by such non-tariff barriers as quotas on imports and subsidies on goods produced for export that make importing difficult or impossible. Protection of industries which come low in the order of comparative advantage distorts the industrial ranking and leads to inefficient resource utilization.

Protectionism in shipping may be defined as state interference in order to promote national shipping service. Government intervention mainly affects the right of free choice of a carrier. In this viewpoint, it may be divided as direct and indirect protectionism.

It is impossible and unrealistic for free competition to exist in world shipping. One of the reasons is that every country has selfish thinking and adopts more or less protectionist policies to promote its merchant marine, even though there are differences among countries. Nowadays it is generally accepted that there are protectionist trends.
2.2 Methods of Protectionism

As I mentioned before, protectionism can be divided as direct and indirect policies. I think that administrative measures affect market mechanism (free choice of carrier) directly, and financial measures affect indirectly.

2.2.1 Administrative protectionism

Administrative policies mean that the government openly intervenes in the choice of carrier. In this category there are flag preference and flag discrimination as a method of establishing national fleets.

Milinowski, W.R. defined that this kind of protectionism is a state shipping policy that discriminates between different flags in giving cargo by preferring or giving priority to the domestic flag in giving cargoes and/or granting privileges. These practices are increasingly used by the developing countries which have insufficient financial funds to support their fleets. It can be regarded as the most important form of protectionism.

Some authors divide protectionist measures into cargo reservation, cargo preference, cargo sharing, cabotage and preferential treatment of own ships in domestic ports. Among these, cargo reservation is the most popularly known administrative protectionism. As the others are derived from cargo reservation, focus is made on this policy.

Cargo reservation is aimed at reserving for the domestic carriers the largest possible share of the country's
seaborne trade. The actual cargo reservation may be subject to various kinds of regulations:

i) Bilateral agreements
ii) Unilateral agreements
iii) Multilateral agreements
iv) International agreements
v) Pooling agreements on a national, conference or operator level
vi) Commodity or cargo form specific reservation policies or agreements
vii) Cargo ownership or control of specific reservation (government owned or impelled cargo) (8)

Some countries reserve 100% of their seaborne trade cargoes and coastal cargoes unilaterally. Through bilateral agreement, the transport of seaborne trade generated between two countries is shared equally.

However, it is meaningful to mention the UN Convention on a Code of Conduct for Liner Conference which entered into force since October 1963. This Code adopted 40-40-20 formula. According to Article 2 in Chapter 2, exporting and importing countries shall have the rights to transport 40% of their liner cargo which carried by the conference individually and third-country shipping lines shall have the right to acquire the remaining 20%.

2.2.2 Financial assistance

Financial assistance can appear in the form of subsidies. As shipping is a capital intensive industry, it is difficult to start a service without government support.
Therefore, the majority of countries give subsidies to their shipping company especially at the initial period.

Other main reasons for financial aid and fiscal relief to shipping are the need to develop merchant fleets (by reconstruction or renovation), to remedy financing problems and to help offset the exceptionally high operating costs, or the need to compensate for special services. (9)

These subsidies may be paid by direct and indirect ways. Professor Ademuni-odeke give the following examples as direct and indirect subsidies.

Direct subsidies:

i) Operation subsidies
ii) Construction subsidies
iii) Modernization subsidy (scrap and build and demolition)
iv) Actual depreciation subsidies
v) Accelerated depreciation subsidies
vi) Loan subsidies
vii) Interest subsidies

Indirect subsidies

i) Investment allowance and grants
ii) Investment guarantee and deferred credits
iii) Tax benefits
iv) Construction deposits
v) Customs exemptions
vi) Compensatory subsidy
vii) Inflation and insurance subsidies
viii) Seamen’s welfare benefits
ix) Ship research grants.
Besides cargo reservation and financial assistance, there exist various kinds of methods: such as Operational controls on shipping, Restrictive trade financing and regulation, Freight rate controls and State-owned company.

It is not my intention here to go into details of the methods of protectionism. Therefore I would restrict to introducing the various protectionist policies.
Chapter III GLOBAL CONTROVERSY BETWEEN
SHIPPING PROTECTIONISM AND LIBERALISM

3.1 Historical Background

Before World War II, the basic theory of shipping was that of the principle of free and fair competition. Under this principle shippers were able to choose carrier, whether it was a domestic or a foreign flag vessel, without any intervention.

This shipping freedom is based on the principle of comparative advantage, the principle of the liberty of the seas which was advocated by Hugo Grotious and the theory of free enterprise under which demand and supply were adjusted automatically by the invisible hand, actually the price.

The principle of free and fair competition was a very convenient theory to justify the control of world shipping by the developed countries. Therefore more than 90% of world shipping was controlled by a few so-called traditional maritime countries at that time, whilst developing countries possessed only several ships which transported coastal cargo.

As the end of the World War II gave political independence to the former colonies, the world changed from colonial one-sided control to the existence of different kinds of nations.

Newly independent countries, in other words the developing
countries, tried to develop their economy in order to get genuine independence. However it was very difficult to develop because they have little capital technology and management skills. Above all they needed capital, especially foreign exchange to buy machinery and parts, goods and food. As the main source of acquiring foreign exchange, they were interested in trade and shipping.

Since the developing countries tried to create their own fleet, the principle of free and fair competition was challenged. There was no room for the developing countries to enter the shipping market through free competition, because they had a lack of competitiveness and the market was dominated by shipping conferences and industrial carriers.

In the context of the general economic and political aims of promoting the developing economies by turning away from the traditional liberal framework, new concepts were developed. These concepts incorporate such notions as "a country's own foreign trade", "national carrier" or "liner shipping as a public unity". Efficiency, profitability, comparative advantage and related criteria were to a large extent displaced by aims of equity, income distribution, etc. The traditional economic criteria have lost ground in shipping as well as elsewhere.

At the beginning the developing countries protected shipping individually, but they pushed this kind of strategy in the international organization after the first UNCTAD conference in 1964. In addition, socialist countries realized the importance of shipping from 1960'. They pushed shipping protectionism by centrally planned economy.
Meanwhile, the traditional maritime countries are in favour of the philosophy of the freedom of the seas and try to negotiate liberalization of service trade in GATT. Consequently, there exists visible clash between the traditional maritime countries and other nations, especially the developing countries. The developing nations are pursuing to change the existing pattern of international division of labour in shipping, while the traditional maritime nations try to abolish restrictive and promotional elements in world shipping.

3.2 Demarcation of Liberalism and Protectionism

As stated above, there are numerous protective measures in shipping policy. Most countries are adopting more than one of these measures as a shipping policy. Even some countries that support liberalism do adopt various forms of protectionism. Therefore it is very difficult to decide which countries belong to the advocates of shipping liberalism or not.

I think there is no country which adopt genuine shipping liberalism, because they decide the policy in accordance with their national benefits. If some countries have a strong position in the world maritime market, they proclaim free and fair competition. On the contrary, certain weaker countries, that depend on foreign fleets to transport their cargo, adopt protectionism.

Though there are no official and universally accepted rules of shipping liberalism, the OECD's Code of Liberalization concerning shipping lays down certain
principles which deserve mention. In broad terms the Code of Liberalization in its sections dealing with shipping can be summarized as follows:

i) Governments should apply no pressure on shippers as to the choice of ship to carry cargoes; this choice should be a matter of a normal commercial consideration.

ii) Governments should restrain from discriminating against those of their importers/exporters who wish to 'ship foreign' by imposing export/import licences, refusing to grant them foreign exchange or force them to employ home-flag vessels.

iii) Even the government-controlled organization should conduct their business on the basis of normal commercial principles.

According to this definition, protectionism should only be concerned with and limited to administrative measures, especially cargo reservation and flag discrimination. Other financial subsidies belong to the liberal policies.

I do not fully agree with this Code, but this Code gives guidelines in determining the countries having a protective or liberal policies.

As a matter of fact, the contemporary controversy between the traditional maritime countries and the developing nations is related to cargo reservation. The reason for this status quo is that cargo reservation is explicit and visible. In addition to above, the market situation is directly influenced by cargo reservation policy. While the payment of subsidies distorts the division of labour, it does not restrain in the proper sense the barriers to access. On the other hand, most of the developing nations have no ample funds to give financial assistance to their shipping industries. Because of this, they are not
Figure 3.1: INTERACTION OF RESTRICTIVE SHIPPING POLICIES AND EFFECTS ON CARGO ACCESS

source: E.G. Frankel, ‘The World Shipping Industry’
Croom Helm, P.44
interested in the discussion of financial subsidies.

In my opinion, most protectionist policies have the same goal which secure cargoes directly or indirectly for national flag. It means that every protectionist policy is related to the cargo reservation as shown in figure 3.1. Therefore I will concentrate on cargo reservation.

From the next section, I intend to introduce the grounds of the controversy from each side point of view.

3.3 Logics as Supporter of Protectionism

In this section, I intend to explain the general opinion of the developing countries. The two superpowers, the US and the USSR, are seen as following a little bit protectionism in some sense. As their policies are based on a global security strategy, it is beyond my subject.

Firstly, in order to promote shipping, the developing countries are unable to follow the normal methods. If they follow the economic principles of establishing economic enterprise, it is impossible to change the current situation which is dominated by the traditional maritime nations. Liner trades are still under the control of the conference system, though recently it is being threatened by the outsiders. Therefore the developing countries are paying more foreign currency as compared with the competitive market situation.

Bulk trades are controlled by transnational corporations, in other words the industrial carriers. When they enter into contracts to buy bulk cargoes, they insist buying on
FOB terms. As a result, they get the right to control transport. Since these large corporations are connected with the developed countries' shipowners, there is no room for the developing nations to participate in transporting bulk cargoes.

Secondly, the developing countries' fleets have unfavourable position in every respect. Their shipping companies can not compete with foreign companies without government support. This is related to the infant industry theory of D. Ricardo. Most of the developing countries recognized that national fleets are important. Despite their having potential comparative advantage in shipping, a lot of problems are faced due to the lack of maritime infrastructure. Furthermore, since the cost to a developing country of owning ships is higher than that of an industrialized nation, its fleet may have a handicap at the initial stage.

Professor El. A. Georgandopoulos gave some instances during the lecture at the World Maritime University. Maritime transport requires the availability of a great variety of services. For instance a vessel needs maintenance and repair work; she also needs fuels and all types of supplies. Agency services, banking services and telecommunication services are requisites for the modern operation and management of shipping. The availability of port and/or terminal—including cargo handling facilities—is also a requisite for the smooth operation of the maritime transport system. On the other hand, the availability of well-educated and/or trained management personnel and seagoing personnel are of crucial importance for a merchant marine. However, most of the developing countries except newly industrialized countries are
inferior to traditional maritime nations in all respects. Because of this, governments tend to intervene in order to cover these disadvantages.

Next, the developing nations have a legitimate right to transport their export/import cargoes. As can be seen from table 3.1, about 50% of the volume of seaborne trade is generated by production in the developing countries. On the other side, their fleets currently amount to about 20% of the total world tonnage according to table 3.2. Excluding a few leading developing countries, such as China, S.Korea, India, Brazil and Argentina from the developing countries, their portion was slightly increased as compared with 20 years ago. Therefore, the majority of the developing countries have to bear a heavy burden of freight costs associated with transport by sea of their foreign trade.

(Table 3.1)

Percentage of Cargo Loaded in developing countries

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<tbody>
<tr>
<td>total</td>
<td>61.4</td>
<td>62.7</td>
<td>56.3</td>
<td>47.7</td>
</tr>
<tr>
<td>crude oil</td>
<td>97.0</td>
<td>94.9</td>
<td>88.6</td>
<td>79.9</td>
</tr>
<tr>
<td>products</td>
<td>71.1</td>
<td>64.7</td>
<td>58.2</td>
<td>55.3</td>
</tr>
<tr>
<td>dry cargo</td>
<td>35.0</td>
<td>33.4</td>
<td>29.1</td>
<td>27.7</td>
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source: UNCTAD Review of Maritime Transport (several issues)
As a result of the high cost of maritime transport, competitiveness of their products on the foreign markets would be reduced. For this reason, the term 'New International Economic Order' was used in 1977 by the Ivory Coast President Mr. F. Houphouet-Boigny to change this state of affairs.

The New Order includes 3 major objectives:

i) The guarantee in the long term for each country, particularly for each developing country, of a significant and equitable participation in all shipping operations relating to the transport of cargo generated by its international trade.

ii) The guarantee in the long term for each country,
particularly or each developing country, of a significant and equitable participation in the effective determination of the transport costs of the cargo generated by its international trade.

The guarantee in the long term for each country, particularly for each developing country, of the freedom to carry out a significant rationalization of equitable principles of the shipping which serves its territory. (11)

Finally, the developing countries insist that they imitate shipping protectionism from the traditional maritime nations. Historically, even traditional maritime nations like the U.K. adopted protectionism when her fleets were situated in a weak market position in comparison with other nations. In addition, protectionism has an enormous political appeal and is supported by nationalism. It would be difficult to throw away protectionism without acquisition of a concession from the developed nations. The developing countries insist that it would be quite reasonable for a country to reserve a certain portion of cargo sufficient to create and maintain her flag.

Eventually, the developing countries might push protectionism to change the current situation that the shipping activities are unevenly spread among the nations.

3.4 Logics as Supporter of Liberalism

This contention starts from the basic theory of economics. Liberals point out of the losses resulting from protectionism. They regard cargo reservation as removing
Figure 3.2: THE RESULT OF CARGO RESERVATION

- The loss of commodities' competitiveness
- Reduction of the trade volume
- Finally, the damage for national economy
incentives to efficiency and cost control, diminishing the flexibility of ships and raising costs for shippers and related sources of employment.

In other words, most forms of cargo reservation, or other methods limiting access to cargo, interfere with the rational use of resources and as a result increase cost, reduce service quality, and obviously limit competition. (12) As is shown in Figure 3.2, cargo reservation would bring about damage to the national economy.

Theoretically, free market system without any intervention is the best way to expand trade and promote world economy. As the market price to which the perfectly competitive firm responds is set by the forces of demand and supply in perfect competition, shippers are able to use vessels with the most favourable freight rate.

A next simple model, which is shown in Figure 3.3, shows the negative impact of sharing on the basis of a 40 - 40 - 20 (one type of cargo reservation) or any other share allocation. Given D1 is the demand curve on the liner route under consideration and D2 = 0.6 D1 is the 60% demand curve. If P1 was the conference freight rate before entry of the national shipping, and if because of higher costs of the national shipping members, the conference agrees to raise the freight rates to P2 > P1, then (P2 - P1) Q1 = additional profit of non-national shipping conference members who earlier accepted P1 which included marginal profit and (P2 - P1) Q3 = additional cost to the country’s trade of carrying Q3. Finally (Q2 - Q3) is the reduction in trading volume resulting from the increase in freight rate.(13)
It would be harmful for the shippers and the national economy. In relation to trade, a competitive manufacturing industry requires a flexible and open international shipping system in order to reduce cost.

Next, the developing countries should have a stronger position in the long run. As comparative economic advantages in providing shipping services are heavily in favour of the developing countries, a major shift from the developed to the developing economies is inevitable. Participants in the shipping industry, such as government, banks and owners in the developed countries have begun to recognize this fact. Thus the EEC Report on Common Transport Policy (Bulletin of EEC Supplement 5/85) identified the erosion of the comparative advantages of European ships in the traditional areas of shipping activity. As can be seen from the Figure 3.4, the fleets of the traditional maritime nations are decreasing and losing their shares in the market.
Professor P. Bauchet gave a lecture at the World Maritime University that the oldest industries of today's most advanced societies relocate to other because these activities no longer correspond to the country's age of development. And their requirements give an edge to the new nations, making the move inevitable.

In 1979, W.W. Rostow divides these industrial activities into three categories according to their degree of industrial complexity and the elasticity of demand for their products. There are those which appear at the early
stages of industrialization in countries where the per capita income is about $200 (I think that it has to be adjusted to $400 in 1989): especially textile, food, shoe and leather industries. Next is the more advanced stage of heavier industries such as metallurgy and shipbuilding. And finally a post-industrial stage of more recent activities including new activities in the service sector, but also high-tech industries and durable consumer goods. This implies that shipping industries including transport services belong to the "middle-age" of development in countries whose per capita income is between $400 and $2,000 (adjusted to $800 and 4,000) (14)

Therefore, some countries which reached in second stage increased their market share rapidly during last 10 years. Other developing countries will join to this stage upto their economic development because comparative advantage of shipping is moving to the developing countries. As a result, liberalism will give more benefits to the developing countries in the future.

Finally, shipping should allow free entry because it has international and commercially-oriented characteristics. If one country reserves its cargoes, foreign flags could be excluded from the transport market. In addition, lots of countries follow protectionism to complement their fleets' weakpoints. For these reasons, shipping would change the internal business and vessels could not find cargoes on inbound voyages. It is harmful for the national and world economy, because there is a close relationship between a transport system and economic development. If one country discriminates certain flags, it is clear that the discriminated country should adopt countervailing action, such as retaliatory flag discrimination. This is
also harmful for expanding world welfare through the trade.

Therefore, liberalists insist that free and fair competition is the best way to increase efficiency in shipping, because any national and international interventions distort market situation.
Chapter IV ECONOMIC EFFECTS OF PROTECTIONISM

4.1 Current Shipping Environment

The legislative trends of the developing world in recent years have been towards more international regulation of shipping through multilateral conventions, bilateral government-to-government agreements, and unilateral measures to favour and support national carriers. (15)

On the other hand, the reality of the freight market and shipping practices have been leading towards a more highly competitive international environment in shipping.

Firstly, I intend to observe demand for shipping. Between 1967 and 1974 seaborne trade grew by 12% per annum. As shown in Figure 4.1, from 1974 to 1988 there was a slight growth (2-3%) in seaborne trade.

Demand for shipping has continued to fall since 1980 in the oil trade, iron ore and several sectors of the general cargo markets. Even though there is a slight increase of seaborne trade from 1986, the aggregate transport task measures by tonne-miles has dropped by 3.5 thousand billion since 1979.

The reasons for reduced demand are economic recession, energy conservation, reduced trading distances (especially the oil and EC market), land bridges and diversions of cargoes from sea to land and air modes.

The supply of shipping has not appreciably diminished over this period. Figure 4.2 give general trends in the
world fleet.

(Figure 4.1)

**WORLD ECONOMY AND SEABORNE TRADE**


Though the world tonnage has been reduced by 21 Mill. gt since 1982, it is not enough to solve the current surplus situation. The reason for this problem is that the sea transport has been made more efficient, and requires fewer ships, as a result of economic of scale, unitisation and improved port turn round.

In addition, under the prevailing conditions in the shipping markets better times are expected, bringing activity for newbuilding up and demolition volume down.
Accordingly, the world fleet might expand slowly again at least from 1989 onwards. (16)

(Figure 4.2)

World Fleet
(figures at start of year)


Therefore it would be forecasted that imbalance between supply and demand will continue for a long time. Protectionism in shipping and shipbuilding have all contributed to this imbalance.

Consequently, most of the shipping companies have gone bankrupt due to the low freight rates. As shown by Figure 4.3 and 4.4, there have been recurring periods of very low freight rates in the dry bulk cargo and tanker markets.
(Figure 4.3) TANKER FREIGHT MARKET

(source: Fearnleys Review 1985 - 1987)

(Figure 4.4) DRY CARGO FREIGHT MARKET

(source: Fearnleys Review 1985 - 1987)
Statistically, the last 10 years have shown how difficult it is for shipping companies to survive in an extremely competitive market. Shipping is a very capital intensive industry, so intensive that lack of profitability can undermine the national economies of small nations.\(^{(17)}\)

It is understandable to wish to have a national merchant fleet, but all these changing environment render it more difficult to hold cargo for national flag.

### 4.2 Economic Analysis of Cargo Reservation

From an economic viewpoint, restraints such as cargo reservation may affect negatively numerous aspects of shipping operation.

Since this policy aims at a deviation from a market-oriented system, it is inevitable to distort efficiency of shipping services. In this part, I intend to analyse economic effects of cargo reservation focused on 3 aspects, namely, operating costs, freight rates, and supply tonnage.

When I describe these, some explanations are similar to the logics as a supporter of liberalism.

**Effects on operating cost**: Closure to competition should generate cost-raising disadvantages. There are many reasons to back up above statement.

Firstly, available cargo volumes are limited to country’s own cargo in the protected conditions. This will result in more ballast voyages or low utilization during off-season.
Because of the shortage of inbound cargo shipowners may employ small vessels with higher unit-costs.

Another reason to increase cost is the elimination of foreign-flag operators who are able to offer lower freight rate. Since national carriers could be protected from participation of competitive newcomers, they can enjoy monopolistic situation and do not feel any need to rationalize.

In the longer term, there may also be a tendency of protectionist policies to interfere with technical and organizational progress. An example is Brazil: introduction of the container system was held up considerably. Also the step into intermodalism may be hampered by government intervention. A tendency towards larger ships which could offer lower unit costs may be blocked if cargo reservation and market segmentation keep available cargo volumes artificially small, and insufficient to fill large vessels. In general, such policies will conserve obsolete fleet structures or operational patterns, associated with inefficiency, complacency, and a lack of progress on the side of shipping operators. (16)

Effects on freight rates: As I mentioned in the previous chapter, the price of monopolistic firm is higher than competitive condition. Cargo reservation measures will raise rates because market access is restricted to higher-cost protected fleets. Above cost-raising aspects will also enforce higher rates.

It has to be noticed that subsidies lead towards downward pressure on freight rate, while cargo reservation or
sharing measures contribute to higher shipping rate.

Consequently, it will give damage to trade and economy because the burden of high rates are imputed to shippers.

**Effects on supply tonnage**: Under the restrictive conditions, the theory of supply and demand can not be applied other than perfect competition. Every developing country which adopts cargo reservation intends to increase their fleets mostly through new building in order to replace traditional maritime flag vessels. It creates apparently excess supply of world tonnage, but it can not be adjusted by market mechanism. Because of this, structural crisis of world shipping can not be broken off permanently.

Therefore, it can be concluded that cargo reservation prevents a contribution to rational allocation of resources and makes shipping become unprofitable business. Cargo reservation can not be justified to promote shipping because it might give loss to the national economy.

There are other negative aspects like retaliatory action besides above. In general, it is accepted that protectionism might diminish the efficiency of shipping services. On the other hand, there are a number of arguments which are put forward by the supporters of protectionism as I mentioned in Chapter III. Although I recognize the legitimacy of protectionism to a certain extent, I think that negative effects are more in protectionist policies.
4.3 Standards of Value in Policy Decision - Making of the Developing World

4.3.1 Policy decision and national interest

In general, when every government adopts and carries out certain policy, there are backing theories to rationalize that policy and every government recommend the adoption of that policy to other countries. However, if we deeply researched the background, we find some facts why certain government adopted that policy. The reason is that it is most favourable to maximize her national interests. In other words, ostensible reasons are only the ways for rationalizing policy.

Though the traditional maritime nations advocate shipping liberalism, they actually adopt indirect or invisible protectionism to complement their fleets' weakpoints because it is helpful to their interests.

As a natural consequence, adoption of shipping policy depends upon which policy is most desirable to promote shipping and economy. No matter how excellent the theory and logic may be, any policy is useless unless that policy supports to promote shipping or contribute to national interests.

A country which is adopting 'Flags of Convenience' or open registry is a good illustration. In the case of some countries, such as Panama, Liberia and Bahamas, maybe their governments decided that it was difficult to develop their own fleets by themselves considering their economic, geographical circumstances and etc. whether they adopted liberalism or protectionism. Therefore, they must have
adopted Flags of Convenience as a revenue-generating policy.

As the same way, we can imagine why the U.K. and Norway changed their registry system to off-shore registry (captive open registry). Instead of controlling the process of flagging-out, these government are ready to equalize the conditions between closed and open registry systems in order to protect the shipping-related industry.

In conclusion, it is clear that every policy-maker is considering national interests above all others when considering to adopt any policy.

4.3.2 Relationship between protectionism and the developing economy

In relation to protectionism, especially cargo reservation, what decision is beneficial to the developing nations? It is sometimes dangerous to think that cargo reservation is always helpful for national interests. One of the reason for this is that shipping is not profitable business under the current severe competition and tonnage surplus situation.

First of all, we have to consider the possibility of growth in shipping and the economic effects of cargo reservation. As a rule, protectionism is seldom advocated to protect industries that are extremely inefficient compared to foreign industries: it is usually advocated to protect industries that can just compete, but not quite.

Therefore, it is quite unreasonable to adopt shipping protectionism in the case of very inefficient situation.
For example, we can assume a small country which has a little cargo and unfavourable port situation. This country might pay a lot of foreign capital to own vessel. Even if she adopted restrictive shipping policy, her vessel would never gain profit because of low space occupation and high voyage cost. In this case, it may be more beneficial to create new employment by building roads, schools and research laboratories through investing foreign capital.

In other words, it is difficult to envisage a country with insufficient oceanborne trade of its own being able to establish, develop and sustain a national merchant marine fleet purely on the basis of restrictive practices.

Table 4.1 shows that such countries which have sufficient oceanborne trade are favourable to own their fleet among developing countries.

(Table 4.1) Merchant Fleet by Flags in the Developing World

<table>
<thead>
<tr>
<th>country</th>
<th>No. of ship</th>
<th>1,000GRT</th>
<th>1,000DWT</th>
</tr>
</thead>
<tbody>
<tr>
<td>China</td>
<td>1,427</td>
<td>12,464</td>
<td>19,029</td>
</tr>
<tr>
<td>S. Korea</td>
<td>640</td>
<td>7,052</td>
<td>11,618</td>
</tr>
<tr>
<td>Singapore</td>
<td>468</td>
<td>6,990</td>
<td>11,404</td>
</tr>
<tr>
<td>Hong Kong</td>
<td>245</td>
<td>6,314</td>
<td>10,670</td>
</tr>
<tr>
<td>Brazil</td>
<td>372</td>
<td>5,824</td>
<td>9,771</td>
</tr>
<tr>
<td>India</td>
<td>342</td>
<td>5,815</td>
<td>9,703</td>
</tr>
<tr>
<td>Taiwan</td>
<td>246</td>
<td>4,853</td>
<td>7,241</td>
</tr>
<tr>
<td>Saudi Arabia</td>
<td>133</td>
<td>2,095</td>
<td>3,604</td>
</tr>
<tr>
<td>Indonesia</td>
<td>730</td>
<td>1,811</td>
<td>2,686</td>
</tr>
<tr>
<td>Argentina</td>
<td>141</td>
<td>1,643</td>
<td>2,619</td>
</tr>
</tbody>
</table>
Next, I used simple calculation to analyze the economic effects of cargo reservation in table 4.2. The objective of this calculation is to confirm the balance of payment effect through cargo reservation.

Suppose that there is one commodity (price 1 US$, quantity 100) whose freight rate is 10 US$ transporting by national vessel or 9 US$ transporting by foreign flag. The difference of freight rate (1 US$) between national and foreign vessel is originated from my experience in Korea Maritime and Port Administration (KMPA). Government officials in KMPA used to recommend shippers to use national flag until the difference reached 10%. As I mentioned before, only 30% of gross foreign exchange could be saved in shipping according to the UNCTAD report.

Result of calculation proved that we can save 2 US$ by using national flag. However, it is ambiguous considering the reduction of commodity selling. It can be seen from the Table 4.2 that benefit of foreign currency saving disappears when the price elasticity of demand is over 2.

Considering most of products in the developing countries are situated in high competitive market, we can guess that their products have high price elasticity of demand. As a result, I doubt the foreign exchange saving effect of cargo reservation.

In addition to this, we have to consider that the employment effect of production industry and its spreading effect are enormous as compared with shipping industry.
The reduction of commodity selling could result in heavy unemployment and the damages of national wealth.

(Table 4.2) Analysis of the Balance of Payment Effect

<table>
<thead>
<tr>
<th>commodity</th>
<th>freight rate</th>
<th>total commodity price in market</th>
<th>actual saving</th>
</tr>
</thead>
<tbody>
<tr>
<td>national $1</td>
<td>10$</td>
<td>110 $</td>
<td>3$ -1$</td>
</tr>
<tr>
<td>flag</td>
<td></td>
<td></td>
<td>= 2$</td>
</tr>
<tr>
<td>foreign $1</td>
<td>9$</td>
<td>109 $</td>
<td></td>
</tr>
<tr>
<td>flag</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Reduction of commodity selling

<table>
<thead>
<tr>
<th>price elasticity of demand</th>
<th>change in selling foreign currency losing</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>99</td>
</tr>
<tr>
<td>2</td>
<td>98</td>
</tr>
<tr>
<td>3</td>
<td>97</td>
</tr>
</tbody>
</table>

cf. Price elasticity of demand means a measure of the degree of responsiveness of demand to a given change in price:

\[
\text{Elasticity of demand} = \frac{\% \text{ change in quantity demanded}}{\% \text{ change in price}}
\]

Then, the long-term economic value of a high degree of cargo reservation is questionable. Once inefficient merchant fleet of large enough size to meet flag share policies has been created, continuation of large-scale
cargo reservation may lead to a decline in competitiveness and efficiency. In this case, there is no doubt that national flag neither intends to increase competitiveness nor is based on commercial concept. It means that this policy distorts the rational utilization of resources.

If so, it is unreasonable to try to promote national fleet in the developing country. In this paper, I would like to show the disadvantageous situation, such as scarce capital resources, lack of manpower and experience. The reason is that the opportunity cost of capital in the developing countries is higher than other nations at the time of entering the market. Especially in the current market situation, it is explicit for them to lose money. They have to weigh the cost of investing in their merchant marines against other needs because there are a lot of urgent needs to invest capital resources in the developing countries.

(Table 4.3) Developing - Country Vessel Ownership:
Potential Losses in 1984

<table>
<thead>
<tr>
<th>Commodity</th>
<th>Iron ore</th>
<th>Grain</th>
<th>Coal</th>
<th>Bauxite</th>
<th>Phosphate</th>
<th>Alumina</th>
<th>Rock</th>
</tr>
</thead>
<tbody>
<tr>
<td>Time</td>
<td>1.92-2.75</td>
<td>1.74-1.82</td>
<td>1.74-1.92</td>
<td>1.74-1.82</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>charter</td>
<td>0.48-4.56</td>
<td>0.86-1.16</td>
<td>0.79-0.44</td>
<td>4.10-0.38</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profit</td>
<td>2.79</td>
<td>2.09</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

(US$ million)
a) Represents least and most possible losses for the selected trade routes.

* the selected trade routes
  o Iron ore Monrovia - Rotterdam
  o Grain New Orleans - Tampico
  o Coal Norfolk - Iskenderun
  o Bauxite/Alumina Kamsar - Port Alfred
  o Phosphate Rock Casablanca - Visakhapatnam

b) 'Least' figure represents one-way voyages and assumes return cargoes at equal freight revenue.
'Most' figure assumes return voyages made with ballast leg.

source: Drewry Shipping Consultants Ltd.
"Protectionism and the Bulk Shipping Industry" 1985

Drewry Shipping Consultants Ltd. researched the potential losses when the developing countries own vessel under the market situation in 1984. Table 4.3 gives an indication of potential losses incurred by the developing countries. From this Table, we can imagine that shipping is unprofitable business for the developing countries.

In this research, Drewry Shipping Consultants Ltd. mentioned that the key to developing countries' future success in shipowning and operating lies in (i) the purchase of used vessels to reduce short-term capital costs, (ii) the assurance of return cargoes to reduce ballasting and increase revenue-earning time, and (iii) a stepped-up investment programme in the developing countries' ports and infrastructure to improve economies of scale, reduce non-revenue earning time spent in port.
and reduce wastage and spoilage of poorly handled commodities.(19)

Among these recommendations, (i) will help to prevent excess supply of world tonnage, and (ii) needs the unfettered foreign shipping market. And then (iii) represents that the investment of infrastructure is the precondition of shipping development. In other words, Drewry recommends free market condition and basic investment rather than shipping protectionism.

If a developing country intentionally protected their fleet in order to achieve profit, it is clear that her export cargo would lose the competitiveness in world market because of the cost increase.

4.3.3 Recommended solution for the developing countries

Now we face the following question: Is it favourable for the developing countries to protect their fleet and promote shipping from the economic point of view?

In my opinion, the answer is "NO" under the current unfavourable situation. Of course some developing countries which have sufficient cargoes or staged in the middle-aged of development, according to W.W.Rostow theory, have some advantages. Their fleet could be developed without government protection, because of the comparative advantages.

At this stage, I would like to mention what the solution is for the developing world. Since the developing countries are situated in unfavourable conditions, such
as foreign exchange problem, untrained man-power and insufficient capital, it is difficult to solve their problems. However, we can find some solution because shipping has international characteristics.

First of all, the developing countries have to throw away economic nationalism. (I don't want to comment on political nationalism) The reason for this is that the regional cooperation is essential for them. If they form bigger market, and allow free capital and man-power movement within their geographical region, it is easier to establish competitive shipping company and efficient port facilities and to overcome market segmentation. It is generally accepted that EC integration will be beneficial to member countries. I expect similar kind of regional cooperation will be started from other developing region.

Next, the developing countries should not hesitate to cooperate with traditional maritime countries. Considering international characteristic of shipping, cooperation between the developing and the developed is necessary to supplement weak-points each other. This concept is based on interdependence theory. Any country could not survive in modern society without international cooperation.

Joint venture and joint services are good examples. Most developing countries lack the technology, know-how and even capital. These problems could be solved through joint venture.

And then, we have to consider that shipping has existed to assist trade in the initial stages of development. As the developing countries need proper circumstances to promote trade and economy, shipping industry has to contribute to
make this situation. 

If so, which investment has the priority between fleet possession and port and other infrastructure construction? Uncompetitive national fleets increase the cost of sea transport as I analysed before, while an efficient port could lead to the reduction of transport cost.

UNCTAD secretariat studies indicate that port charges, cargo handling costs and the cost of ship’s time in port, typically represent about 5%, 25%, and 35% respectively of liner freight rates between developed and developing countries. In other words, almost two-thirds of the shipping costs initially borne by the ship operator are actually incurred in ports, and this takes no account of port charges for cargo handling and storage borne directly by the shipper.

In view of the fact that such a high proportion of shipping costs is incurred in ports, improved port performance can be the key to a reduction in the cost of sea transport. (20)

I, therefore, think that prior port investment is the better policy than possession of fleet for economy. In the case of port investment, regional and international cooperation could, in certain cases, be necessary. Port and related infrastructure will contribute to establish competitive national fleet in the future.

It may be concluded that the developing countries need cooperation and liberalism other than protectionism, even though the developing countries are situated in unfavourable conditions.
Chapter V  A DIRECTION OF PROTECTIONISM

5.1 A Tendency in UNCTAD

In order to establish a New International Economic Order, which would substitute a Old Economic Order (21), the United Nations General Assembly resolved in 1974 that "all efforts should be made to promote an increasing and equitable participation of developing countries in the world shipping tonnage". Finally, and most importantly, UNCTAD has presented proposals to regulate international rights to carry liner and bulk cargoes.

Originally adopted at the end of 1971, UNCTAD's proposed Code of Conduct for Liner Conferences was amended and re-submitted every year until it finally entered into force in October 1983 after being ratified by the required 24 countries, accounting for at least 25% of world general cargo tonnage. The deciding votes cast by industrialized countries were only possible after the inclusion of the Brussels Package that allowed signing with contingency reservations. What the Brussels Package submits, basically, is that the Code of Conduct applies only to trade with the developing countries but does not apply to trade that is exclusively between industrialized countries.

As mentioned before, the result of UNCTAD's Code of Conduct is the requirement that all UNCTAD member countries divide their liner trade between importers and exporters (40% each) and the cross traders (20%), now referred to as the cargo sharing formula (40-40-20).
UNCTAD's developing country members see the ratification of the Liner Code of Conduct as only the first step in a long trek toward the liberalization of all shipping internationally.(22)

However, the current shipping environment is completely different from the situation when the Code of Conduct was adopted. Because of the outsiders, the conference has no monopolistic power in many trade routes. In addition, as a result of developments in trade and technology, such as containerization, the emergence of consortia, the concept of round-the-world service, the door to door service and other organizational and structural changes, there appeared some arguments related to the efficiency of the Code. The implementation of the Code is still lagging behind due to the fundamental difference in attitude among countries. So UNCTAD are reviewing the Code as of 1988.

Nevertheless, there is not the slightest piece of evidence that the principles governing and the basic concepts adopted in the Code has lost their significance or that any of the basic stipulations of the Code have become obsolete.(23)

Though the developing countries acquired legitimate right to participate in liner trade according to the Code of Conduct, most of them were not able to create liner fleet because of lack of finance and insufficient cargoes. Since their exports are often dominated by staples with low value relative to bulk and with good storage properties, they changed their concern to the bulk trades. The developing countries are trying to apply cargo-sharing principles in bulk trades through multilateral conventions. As there exist wide differences of opinion
among the developing countries, socialist countries and the developed countries, it is not clear what will happen in UNCTAD in connection with bulk cargo sharing.

Furthermore, it is being proposed the elimination of flag of convenience or open registries in order to increase developing countries' share in bulk trades.

Consequently, the developing countries are trying to change the existing international shipping structure, which is dominated by the developed nations, through UNCTAD. On the contrary, the traditional maritime nations do not support radical changes of the existing structure.

5.2 New Trends Related to Shipping Policy

Apart from what is happening with UNCTAD, there are new trends towards the support of liberalism in the developed countries.

First of all US maritime policy will be dealt, because the USA influences significantly the international maritime scene as the single most important world economic power.

Everybody knows that the US maritime policy adopts protectionism to some extents, in spite of their basic economic philosophy which is based on the principles of liberalism. For instance, the US reserve coastal cargo and have bilateral cargo sharing agreement with Latin American countries. In addition, they have operating and construction differential subsidy programs.

However, since the Reagan administration took office in
1981 there has been a tendency to diminish the role of subsidies and to decrease the degree of government regulation of shipping. The Shipping Act of 1984 which accepted independent action, open conference, etc., is also considered as a mechanism to accelerate competition in the US market.

Next, we have to notice that EC Common Maritime Policy came into force in 1987. Following years of negotiations, the member states of the European community have agreed on a common shipping policy. Four regulations have become part of European Community Law.

These regulations include:

(i) Restrictions on freedom of services between EC countries and third countries will be phased out. All bilateral cargo sharing agreements involving EC countries will have to phased out, and new agreements are prohibited.

(ii) In case of restrictions by third countries on free access to cargo, the European Community can organize coordinated action.

(iii) When unfair pricing practice by third country shipowners in liner shipping causes injury to EC shipowners, redressive duties may be imposed.

(iv) Conference agreements are allowed.

Although (iii) has protectionist characteristic, overall actions are clearly bound to create a more liberal regime in maritime sector.

And then, US, EC and other developed countries try to remove non-tariff barriers in service industry including maritime industry through GATT. Although this movement; so
called Uruguay round negotiation, has met the strong resistance of the developing countries as well as UNCTAD, it could be regarded as new trends for shipping liberalization.

Since a clash of interest seems to be visible between the traditional maritime countries and certain developing countries, I imagine that the international confrontation about shipping will be more and more complicated in the future.

5.3 A View for International Shipping Development

Why do the developing countries keep shipping protectionism despite of the economic losses? Since protectionist's idea is related to income distribution rather than efficiency of production, I think that it is not rational but legitimate.

And then, most developing nations feel that they are suffering from the effects of shipping practices by the traditional maritime nations and multi-national corporations. It is said that this is one of the primary factors of increasing the gap between the developed and developing nations. This feeling is strongly backing the logic to make a negotiating and bargaining power for promoting national fleets.

The wide range of direct and indirect protectionist practices by the traditional maritime nations and industrial carriers makes it more and more difficult for the developing countries to participate equitably in their own trade. Therefore, it is unreasonable to criticize
restrictive policies like cargo reservation of the developing nations which have unfavourable conditions in every aspect, in spite of the indirect assistance in the developed countries. The developed countries have to abandon indirect protectionism in order to realize shipping liberalism: but it is difficult to expect.

As long as the developing nations feel the barriers which hinder economic development on account of the structural disequilibria in shipping, they will pursue arbitrary cargo sharing. Since this results in the reduction of international trade and recession of world economy, both sides will face the mutual danger in which nobody wins: but I hope it will not happen.

As a matter of fact, the developing nations have reached the limit of their power. In 1974, the General Assembly of the United Nations adopted a Declaration on the Establishment of a New International Economic Order. The developing nations tried to increase their share in the world wealth through NIEO proposals, but little major redistribution of wealth has resulted. In addition, though the UNCTAD Liner Code came into force in 1983, only in limited trade routes it is being applied.

On the other hand, the developed countries are feeling the threat from the developing countries which want to change the world economic order by using political power.

If this is the case, what could be the solution? I think that effective competition is the best way to expand world economy. If it is impossible and not accepted by one party concerned, cooperation and negotiation are needed between the developing and developed countries. As one-sided
solution can not be applied to world shipping, international solution which is agreed by both sides is needed. Eventually it should be necessary to receive concession from both sides or one side-persuaded.

As far as shipping policy is concerned, some developing countries realize the failure of protectionism and change their policy to more flexible one. The traditional maritime countries should convince the developing nations about the advantages of liberalism before both parties follow the concept. Otherwise, it should not be forgotten that world development was led by free shipping and trade. Looking at the past trend of events, it would not be surprising to see countries which hold on the controlling role of government in shipping will be backwards in the future.

It is therefore, required to remove the transport barriers and unfavourable factors in the developing world in order that these developing countries become genuine companions in the world economy. For this reason, both sides have to make a joint effort in order to improve maritime infrastructure like ports and get rid of unfair practices for the purpose of improving the developing countries' trade and economy.

In addition, there are some comparative advantages in the developing world. If both developed and developing countries used these advantages, they could increase mutual benefits. Kiribati is a case in point; West Germany is supporting the maritime training center in Kiribati and employing more than 1,000 seamen from Kiribati. As a result, West Germany has overcome a handicap of crew cost and this will contribute to
promoting shipping industry in Kiribati.

It may be concluded that cooperation is the best way to avoid mutual danger and increase mutual benefit.
PART II ANALYSIS OF PROTECTIONISM IN S. KOREAN SHIPPING

In this part, I intend to explain my country (the Republic of Korea) shipping industry and analyse shipping policy.

S. Korea like other Newly Industrialized Countries (NICs) is the most successful model of the developing country from an economic point of view. Consistent with economic development, S. Korean shipping industry is expanding her fleet and market share rapidly and being regarded as one of the leading shipping country in the developing world. Therefore, I think that it is valuable to look at the primary factors of Korean shipping development and correlation with shipping policy.

Chapter VI GENERAL OVERVIEW OF S. KOREAN SHIPPING

6.1 Economic Growth and Shipping Development

In S. Korea, it is generally accepted that a well-developed shipping industry is very important for the country. The reasons are that it is virtually an island state, though being a peninsular in the Far East, with its northern border with the Asian Continent having shut off by a cease-fire line and, furthermore, a scarcity of natural resources has forced the country to choose an export-oriented economic development strategy.
Still more, in time of a national crisis, because of its geographical situation, sealanes will become the only access remaining open to the nation as a nation's lifeline.

All these facts justify why the country places a high priority on the promotion of its shipping industry. (26)

During the past two decades, Korean merchant fleet has rapidly expanded keeping step with the nation's economic development. Until 1960, Korean shipping held a small conventional fleet, serving only Japan and a part of Southeast Asia.

With the nation's foreign trade expanding, the government which had come to recognize the important role of the shipping industry, formulated fleet expansion policies including the Planned Shipbuilding Program under which the Korea Maritime and Port Administration was established in 1976 as a central government agency to decide and implement policies.

(Table 6.1) Trade and Fleet Expansion in S.Korea

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>fleet 1) (1,000 tons)</td>
<td>----</td>
<td>108</td>
<td>1,104</td>
<td>2,975</td>
<td>6,386</td>
</tr>
<tr>
<td>trade 2) (billion US$)</td>
<td>-</td>
<td>7.5</td>
<td>27.7</td>
<td>50.6</td>
<td>107.0</td>
</tr>
<tr>
<td>cargo volume 3) (million tons)</td>
<td>4.5</td>
<td>39.2</td>
<td>75.4</td>
<td>118.2</td>
<td>196.3</td>
</tr>
</tbody>
</table>
Such government measures as well as trade volume increase brought a rapid growth to the Korean merchant fleet from a mere 108 thousand grt. in 1963 to 7.9 million grt. in 1988. Table 6.1 shows that there was a dramatic increase in Korean shipping and trade.

6.2 Primary Factors of Shipping Development

What are the primary factors of shipping development in S.Korea? Before I Mention, it is better to clarify essential elements of shipping. In order to enter the market, every shipping company primarily needs vessel, cargo and sea-going personnel. In addition to these, government assistance and port and inland transport system are requisites considering shipping characteristics.

I intend to research main factors of Korean shipping development as I bear in mind above essential elements.

6.2.1. Trade volume increase

First of all, I would like to point out trade volume expansion originated from rapid growth of economy. From 1970, Korean economy have achieved 8.4 % annual growth rate of gross national product. As the export-oriented
industries were leading this growth through import of natural resources, export/import volume has increased more rapidly than GNP.

(Table 6.2) Trade Volume and Fleet in S. Korea

<table>
<thead>
<tr>
<th>Year</th>
<th>Trade Index (mill. ton)</th>
<th>Annual Increase</th>
<th>Fleet Index (1000 gt)</th>
<th>Annual Increase</th>
</tr>
</thead>
<tbody>
<tr>
<td>1970</td>
<td>22.4 100.0</td>
<td></td>
<td>798 100.0</td>
<td></td>
</tr>
<tr>
<td>1971</td>
<td>29.7 132.6</td>
<td></td>
<td>837 104.9</td>
<td></td>
</tr>
<tr>
<td>1972</td>
<td>30.6 137.5 13.0%</td>
<td>1,004 125.6</td>
<td>1,236 154.9</td>
<td></td>
</tr>
<tr>
<td>1973</td>
<td>39.2 175.0</td>
<td></td>
<td>1,973 247.2</td>
<td></td>
</tr>
<tr>
<td>1974</td>
<td>40.8 182.1</td>
<td></td>
<td>2,237 280.3</td>
<td></td>
</tr>
<tr>
<td>1975</td>
<td>41.3 184.4</td>
<td></td>
<td>2,907 364.3</td>
<td></td>
</tr>
<tr>
<td>1976</td>
<td>50.9 227.2</td>
<td>2,907 364.3</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1977</td>
<td>68.3 304.9</td>
<td>3,377 423.2</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1978</td>
<td>75.4 336.6 17.9%</td>
<td>4,164 521.8</td>
<td>4,625 579.6</td>
<td></td>
</tr>
<tr>
<td>1979</td>
<td>90.8 405.4</td>
<td>4,625 579.6</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1980</td>
<td>94.0 446.4</td>
<td>5,175 648.5</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1981</td>
<td>105.3 470.1</td>
<td>6,216 778.9</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1982</td>
<td>108.5 484.4 7.5%</td>
<td>6,806 852.9</td>
<td>7,030 881.0</td>
<td></td>
</tr>
<tr>
<td>1983</td>
<td>118.2 527.7</td>
<td>7,303 915.2</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1984</td>
<td>125.7 561.2</td>
<td>7,079 887.1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1985</td>
<td>133.0 593.8</td>
<td>7,294 914.0</td>
<td>2.1%</td>
<td></td>
</tr>
<tr>
<td>1986</td>
<td>153.8 666.6 11.9%</td>
<td>7,502 940.1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1987</td>
<td>178.0 794.6</td>
<td>7,930 993.7</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1988</td>
<td>196.3 876.3</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

1) Index 1970 = 100
In relation to this expansion, Korean fleet has been increased sharply from 0.8 million grt in 1970 to 7.9 million grt in 1986 the annual average increasing rate is 14 %. As can be seen from the table 6.2, we can observe the correlation between trade volume and fleet.

As I have already mentioned, the basic problem of merchant marine in developing country is related to cargo volume. If she has enough cargo generated from own territory, it is easy to create and expand national fleet.

In the case of Korean shipping, fleet has increased in accordance with trade volume. Before the trade volume reached upto 50 million tons, fleet increased 22.9 % annually as compared with 13.0 % of trade volume. The reason for this, there was not enough vessel to transport her cargoes at that time. Share of the Korean fleet of import and export cargo was only 26 % in 1972. This share was highly dependent on the short-sea trade with Japan. Therefore, Korean merchant marine fleet expanded to enter the long-distance market.

Table 5.2 shows that there was similar trends between fleet and cargo expansion during 1976 - 1984. Since 1985, Korean shipping has increased slightly because of government policy. I will explain about this phenomenon in Chapter VI.

6.2.2 Easiness of vessel acquisition
As far as vessel acquisition concerned, there are two kinds of acquisition; namely, new building and purchasing of second-hand vessel.

In relation to purchasing of second-hand vessel, Korea had very favourable geographical location because her neighboring countries, such as Japan and Hong Kong were two of the world pivots of financial operation and shipping business in 1970'. For this reason, Korean shipping industry could get second-hand vessels easily during last two decades.

(Figure 6.1)

**ANNUAL S.KOREAN FLEET INCREASE**

source: Korea Maritime Institute.
However, it is meaningful to mention about the Planned Shipbuilding Program supported by government. The Planned Shipbuilding Program is a combined shipping and shipbuilding promotion measure through which selected shipowners build their ships at local shipyards with government loans. Under the program designed to provide the shipyards and shipowners with an opportunity to build and operate modern ships, 3,620 thousand grt of new ocean-going ships has been built since 1976 when this program started.

These vessels make up 46% of the Korean fleet. In short, I think that this program has boosted the expansion of Korean fleet and pushed Korean shipbuilding to 2nd position in the world. It can be seen from the Figure 6.1 how significant the planned shipping program is in Korean shipping.

6.2.3 Competitiveness of crew

The rapid development of Korean shipping industry is due largely to the contribution of its seamen.

The Korea Maritime University was founded in 1945 and Korea had no ocean-going ships at that time. Many graduates, therefore, sought employment on foreign merchant ships where they accumulated on-board experience and navigational skills. As Korean seamen have succeeded winning a reputation for their expertise and diligence in the world maritime community, over 47,000 Korean seamen were aboard foreign ships as of 1988.
### Monthly Crew Costs According to Selected Flags

(Average compensation including pay and fringe benefits in USD)

<table>
<thead>
<tr>
<th>flag</th>
<th>master USA=100</th>
<th>second USA=100</th>
<th>seamen USA=100</th>
</tr>
</thead>
<tbody>
<tr>
<td>USA</td>
<td>17,387 100</td>
<td>8,212 100</td>
<td>3,301 100</td>
</tr>
<tr>
<td>Japan</td>
<td>9,705 56</td>
<td>4,820 59</td>
<td>3,643 110</td>
</tr>
<tr>
<td>Sweden</td>
<td>8,695 50</td>
<td>4,813 58</td>
<td>2,605 79</td>
</tr>
<tr>
<td>W.Germany</td>
<td>7,401 43</td>
<td>4,174 51</td>
<td>2,200 67</td>
</tr>
<tr>
<td>S.Korea</td>
<td>2,800 16</td>
<td>905 11</td>
<td>644 19</td>
</tr>
</tbody>
</table>


In spite of their quality, their wages are considerably lower than the developed country's crew. It can be seen from the Table 6.3 that there is huge difference between traditional maritime flag and Korean flag relating to crew costs.

Crew costs are one of the most important factors influencing the efficiency of shipping operation. Korean shipping industry, therefore, could compete successfully with other flags.

6.2.4 Other factors.
Besides the above factors, there were some other factors which affected shipping development both directly and indirectly.

First of all, I would like to state port development and inland transportation system. In order to handle increasing export/import cargo efficiently, major port development projects were established from 1966. Most of these projects were carried out by using IBRD, ADB loans and other sources due to the lack of domestic capital. Through the successful port development, Annual cargo handling capacity increased 8 times in 1987 than in 1972 as shown in Table 6.4.

(Table 6.4)  
Annual Cargo Handling Capacity in S.Korean Port  
(1,000 tons)

<table>
<thead>
<tr>
<th>Year</th>
<th>1972</th>
<th>1977</th>
<th>1982</th>
<th>1987</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>22,313</td>
<td>41,000</td>
<td>95,512</td>
<td>168,774</td>
</tr>
</tbody>
</table>

It seems likely that the Korean economy would not develop devoid of port construction. In addition, Seoul-Pusan expressway was opened to traffic in 1970. All these transport facilities facilitated shipping and economic growth indirectly.

Next, the government has taken an active role to support the development of the Korean shipping industry. Cargo
preference, financial support, shipbuilding and taxation constitute the government policy. This is reviewed in the next Chapter.
Chapter VII  ANALYSIS OF POLICY EFFECT

7.1 Main Policy in S. Korean Shipping

This section reviews current and past S. Korean government policies relating to the development of the maritime industry. Like any other developed or developing country, S. Korean adopted and is adopting various forms of assistance programs.

7.1.1 Cargo reservation

In relation to bulk shipping, Korea uses a system of waivers for carriage of bulk cargoes on foreign flag vessels, with major bulk commodities basically reserved for Korean shipping. And then, S. Korea reserved 40% of liner cargo following the UNCTAD Liner Code.

However, there are a lot of exceptional clauses and no punitive sanction clauses in the law. S. Korean government experienced the difficulty to apply cargo reservation policy in practice. Therefore, there are some argument whether cargo reservation policy contributed to the shipping development or not.

7.1.2 Financial support

Operating subsidies were authorized under the Shipping Promotion Act of 1967, and a total of 834.9 million Won (S.Korean currency) was disbursed during the 1969-1973
period against requests from operators totalling 3,091.2 million Won. In 1973 the subsidy programs discontinued.

However, in 1979, a program of grants to the operators of full container vessels was instituted with the objective of encouraging the development of container shipping. Major container operators received 3,756 million Won, but this program also stopped in 1985.

In 1981, a Shipping Promotion Fund was established to support the building of vessels in Korean shipyards that would expand Korean shipping activity into new trades. However, this fund only reached a maximum of 1 billion Won in assets in 1981 and was discontinued in 1983. (28) Prior to 1982, Korean shipping companies were exempt from corporate income tax, but this was also discontinued.

It means that most financial subsidy programs were abolished.

In addition to the above arrangement, the government provided two financial supports: Financing of short-term working capital needs. Special loans to shipowners to assist in the payment of principal and interest payments on ship mortgages. The latter was also discontinued in 1979 and then recommenced in 1982 but only for payments on foreign currency loans. These financial supports strongly are related to commercial decision of bank.

In addition, there is the planned shipbuilding program as already mentioned. I think that this program was prepared for the shipbuilding industry. Because shipowners can build ship in foreign shipyard with similar conditions.
7.1.3 Shipping industry rationalization plan

General S. Korean government economic policies since 1980 contain the enhancement of competitiveness and reduced government intervention to industry. Exceptionally, government carried out Shipping Industry Rationalization Plan (SIRP) from 1984 to 1986.

The reason for this policy was strongly related to world shipping recession from 1981. Most of shipping company experienced deficit due to the freight rate decrease as shown in Figure 7.1. Furthermore, it was foreseen that shipping recession would be continued for a long time.

(Figure 7.1)

![General Freight Index](source: based on data from Maritime Research Inc., Parlin, New Jersey.)
If this situation had been continued, S. Korean shipping would have faced a series of bankruptcies. These bankruptcies would indirectly have an adverse impact on the banking sector, as a result it would have damaged the national economy. Therefore, government intervened to restore shipping industry by adopting SIRP.

Its aims are to prevent excessive competition among Korean shipping firms to increase their international competitiveness, to eliminate the huge deficits of shipping companies and to promote orderly development of the industry. As a result of this program, 111 companies were integrated into 20 groups. If companies which concentrate on Korea/Japan and Korea/Southeast Asia route are excluded, only 6 ocean-going companies remained.

Next, the financial assistance consists basically of (a) postponement of repayment of principal and interest related to ship purchase loans for a period of up to 5 years until the market improves, and (b) loans in amount not exceeding a company’s freight claims to cover temporary needs attendant to rationalization, such as operating costs and other expenditures arising from the suspension of sailing rights. In addition, government urged to convert inefficient tonnage into energy and manpower saving ships, and prohibited to import secondhand vessel. For this reason, S.Korean fleet is increasing slightly since 1985 as is mentioned in Chapter V.

SIRP policy was a revolutionary way to save the shipping industry. There were lots of argument relating to the effectiveness of this policy. However, this policy was in line with the government’s objective to provide support to industry where such support will increase long-term
competitiveness. S. Korean government expect that shipping industry will recover their strength to serve Korean economic development from 1989.

7.2 Evaluation of Policy Efficiency

S. Korean government support to the shipping industry has been substantial. It is adopting both policies; i.e. cargo reservation which is prevailing in the developing countries and financial assistance which is used in the traditional maritime nations.

Normally, policy decision-makers incline to have too much confidence in the effect of policy. In other words, they ignore the fact that the external or other factors could give strong influence to the development of certain industry from time to time. If considering the correlation between Korean shipping development and policy, we could observe the limit of policy. In this section, I intend to estimate the efficiency of shipping policy in the case of S. Korean merchant marine.

7.2.1 Cargo reservation and shipping development

Main purpose of cargo reservation is to encourage the development of national-flag fleets. If so, is cargo reservation contributing to Korean shipping development? I am on the side of the people who doubt the effect of cargo reservation.

This policy needs government intervention in trade and transport contract and penalty to a violator, but this
policy has restrictive elements when it is applied.

Firstly, it is difficult to acquire cooperation from the shippers. In the export-oriented economy like S. Korea, it is generally accepted that competitiveness of trade cargo is more important than shipping. Most government organization except shipping organization agree with shipper's opinion which insists cargo reservation is unfavourable policy to increase trade. For this reason, there are lots of exceptional clauses not to interfere trade.

As far as shippers think that there are no advantages when they use Korean flag, they do not follow cargo reservation policy. Furthermore, shippers do not feel any obligation due to the lack of punitive sanction clauses.

(Table 7.1)

Application Status of Waiver in S.Korea

<table>
<thead>
<tr>
<th>Year</th>
<th>1982</th>
<th>1983</th>
<th>1984</th>
<th>1985</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cargo Volume (million ton)</td>
<td>108.5</td>
<td>118.1</td>
<td>125.7</td>
<td>133.0</td>
</tr>
<tr>
<td>Applied Cargo (million ton)</td>
<td>25.1</td>
<td>32.2</td>
<td>39.9</td>
<td>44.2</td>
</tr>
<tr>
<td>%</td>
<td>23.1</td>
<td>27.3</td>
<td>31.7</td>
<td>33.2</td>
</tr>
</tbody>
</table>

Source: Korean shipowner's association

According to Table 7.1, we can observe statistically around 30% of cargoes applied for receiving waiver. However, the important fact is that in most cases cargoes
which applied received waivers which means government allows to use foreign vessels.

In this situation, the following can be said:

i) Shippers applied when they could receive waivers.

ii) If they could foresee that it was difficult to receive waivers, they did not apply, or abandoned their transport rights because no waiver was necessary if a foreign carrier was nominated on the Letter of Credit.

Next, there are about 200 foreign shipping agents in S. Korea. They are doing business on commercial basis without any interference. They have no duty to apply waiver in law. As far as the government recognizes them, it is impossible to interfere in the commercial transport contract.

Let's assume that a foreign shipping agent made a contract to transport certain cargo which would have been transported by the national flag in law. Can the Korean government break up this contract? If Korean government disturbs the foreign shipping company's business, it would suffer from retaliatory action. S.Korean government realizes this dangerous situation, as a consequence, it controls itself against the discrimination of foreign flag.

In addition, it is practically impossible to confirm whether or not the waiver is issued because there are a lot of unspecified shippers in liner trade. Furthermore, S. Korean shipping companies are outsiders in main trade route such as Far East / Europe and Far East / North America. It means that the liner code is not applicable...
in practice.

As a whole, it can be regarded that cargo reservation system is not applicable considering the many restrictive elements above. I can not find any evidence that this policy contributed to Korean shipping development.

The reason for Korean shipping development is connected with other competitive factors as was mentioned in chapter V. Among those factors, trade expansion is most important. Trade expansion creates the demand of shipping, therefore, it naturally leads to supply increase: it is the basic theory of shipping economics.

As far as general economic policy concerned, cargo reservation is contrary to the spirit of the current Korean liberalization policy, a particular objective of which is to reduce foreign trade control. In addition, it is quite obsolete policy considering the scale of Korean fleet.

Because of this policy, S. Korea is recognized one of the countries which adopt severe protectionism. As a result, cargo reservation restricts Korean flag participation in cross trade. For example, the European Council of Ministers decided to impose heavy duties on container traffic carried from Europe to Australia by S. Korea's Hyundai Merchant Marine Co. on Jan. 5 1989. According to EC, the main reason for this decision was that Hyundai had non-commercial advantages over its European competitor. Korean government plans for the rationalization of its shipping industry gave it tax benefits and cheap loan refinancing, and the line has the right to carry all Korea's imports. (30)
Thus, it is my opinion that cargo reservation brings about negative effects in the long-term.

7.2.2 Validity of financial assistance

On legal basis, S. Korean shipping company can receive a lot of financial support from government, but most subsidies did not put into practice. The reason is that Economic Planning Board (EPB) and Ministry of Finance (MOF) do not give any priority to the shipping industry. As a developing country, S. Korea has lots other more pressing areas in the economy needing investment. Therefore, subsidy program for certain private industry is not justified unless EPB recognizes it as vital for the national economy. I think that subsidy program could not be actualized if S. Korea was to become well-developed or other government organizations recognized the importance of shipping industry.

During the past 1970s, government supported shipping industry through subsidy and financial assistance. Consequently, the shipping industry enjoyed profits, but never was it prepared for recession. When the shipping recession started from late 1981, the government was faced with shipping companies’ demand for financial support. In other words, the shipping companies showed the propensity of their dependence on the government.

This fact, that the board assistance encouraged inefficiency and widespread government interference weakened incentives of private companies, gave a lesson to
the government. This was the worst negative effect of financial assistance.

As a result, it becomes more and more difficult for government to force bank to make loans to the shipping industry. In accordance with the progress of political democratization, banks would not agree to government forced loans unless they are commercially justified.

Financial assistance is good policy if you can avoid international criticism which are against protectionism, but this more brings restrictive elements and negative effects against promoting competitiveness.

7.2.3. Effect of shipping industry rationalization plan

During the preparation for SIRP policy, S. Korean government had admitted for the first time that its past policies of encouraging owners to buy in large quantities of old but expensive second-hand ships - and accumulative freight revenue with scant regard for profitability - had led to the crisis. (31)

In other words, the government started to consider a qualitative turnabout towards international competitiveness of S. Korean fleet. Therefore, government aimed not only to overcome the faced crisis, but to increase international competitiveness through mergers and dissolution of small companies. Japan had something similar to this. The Japanese government carried out similar program in 1964 under the "Law for Provisional Measures concerning Rehabilitation and Development of the Shipping Company".
As this program was an extraordinary policy in the market-economy system, there were a lot of arguments and opposing views, such as infringement of private properties, lack of democratic discussion, misuse of national wealth and strengthened protectionism.

All government policies have both positive and negative effects. If positive effects of a certain policy are more than the negative effects, policy-makers have to adopt that policy in order to promote the national interest. Of course, it is very difficult to estimate how many are the negative or positive effects. In the case of SIRP, effects can be estimated by assuming that S. Korea did not adopt the SIRP.

If the S. Korean government had not intervened in the shipping industry by 1984, most Korean shipowners would have been bankrupt within 2 years. The answer to this opinion is clear. Most companies were willing to participate in the merging program when government suggested 2 options; one was that government would give financial assistance when companies merged, another was that each company should be able to do business independently without financial assistance.

Therefore, I think it gave positive benefits and incentives to the shipowners and shipping industry. But there are also other negative aspects. Considering the national economy, as a whole, it needed lots of funds which could have been used for other purposes. It is very difficult to evaluate the effects of SIRP at this time, because S. Korean government aimed to develop its fleet's competitiveness in the long-run.
This policy was to remedy the failure of the past policy: i.e. fleet expansion through government intervention. We learned something new here that policy which ignored market mechanism generated dangerous result. We also have seen a lot of cases of bankruptcy in the developing countries during a past decade. S. Korea was the lucky case, because it had an ability to remedy the problems within the NICs. However, this was not an easy task.

I fully agreed with the S. Korean government opinion that this policy was the internal and temporary measure to cure the urgent shipping problem and promote shipping industry qualitatively. In my opinion, this kind of policy is necessary to move from the status of a developing shipping nation to the developed considering Japanese case as I mentioned earlier on.
Chapter VIII RECOMMENDATION TO S. KOREA

Before I recommend new direction of S. Korean policy, I would like to feature Professor Ademuni Odeke's description of S. Korean shipping:

"South Korea is one of the emerging NICs with a good economic performance, she is also one of the many developing maritime nations (DMNS) relying heavily on maritime subsidies and flag discrimination. She has achieved a marked expansion in her foreign trade with a corresponding expansion of her merchant marine and shipbuilding to match that trade boom. It is not clear how much of that establishment and expansion is attributable to maritime subsidies and flag discrimination, generally, and essential trade routes designation in particular. Despite this, most other DMNS, who are not also NICs have not achieved similar expansions in their merchant marines, despite heavy dependence on maritime subsidies and flag discrimination. Although South Korea's expansion in the maritime sector can be linked directly to her better overall economic performance, yet there might be some correlation between the flag discrimination, trade performance and expansion of the merchant marine sector. It could be the case of the flag 'following' trade rather than vice versa."(32)

According to above comment, he emphasized that economic performance is most important factor than protectionist policy. I also do not deny the correlation between protectionism and expansion of the merchant marine, but the negative effects can not be ignored as I mentioned in previous Chapters.
In the past, S. Korean government intervened too much in private commercial sector and hindered autonomous discipline of shipping companies: for example, government approval of sale and purchase and designation of liner trade route. Despite of this, sale and purchase of ships are important business as well as cargo carriage, private companies have been obliged to follow government intention. In addition, liner shipping companies have had no flexibility to change their vessels and routes, even though that is essential in liner shipping.

It is needless to say that government has to lead in some aspects, such as education of seafarers and shipping management and development of effective shipping financing strategies. However we have to realize from past experience that the other commercial part should be left to the private sector in order to achieve better performance.

Now, let us check the current S. Korean economic level in the world: S. Korea is ranked 11th trading and 2nd shipbuilding nation, she possesses 12th largest fleet and her 47,000 seafarers are employed in foreign ships.

From this, it can be easily seen that S. Korea has comparative advantage in shipping industry. Furthermore, the S. Korean fleet is big enough to compete in the world market. In this case, government intervention in the commercial area is an obsolete policy and hampers qualitative development.

Nobody denies that S. Korean fleet is doing an important role quantitatively in world shipping, but we need
qualitative turnabout and development of shipping related industry such as finance, brokering, classification, insurance and etc.

In addition, if we want to penetrate in world market, it is necessary to expand the liberal economic atmosphere in international shipping policy. We can not ask others to open their doors unless we open ours. Practically speaking, most of S. Korean protectionist policies should not be implemented properly, but lead counter action from foreign countries because they regard S. Korea as one of the countries which adopt severe protectionism.

Considering above comments, this is the time to minimize government intervention and throw away ineffective policy. In order to prevent repetition of past mistakes, more autonomy should be given to the private sector and decision-making by shipping companies should be purely based on commercial interests.

As there are strong demands for economic liberalism after political change in S. Korea, I have a fine view that S. Korean policy will be changed to liberal direction in near future. This is only one way to revitalize Korean shipping and to match with the changing shipping environment.
CONCLUSION

In this paper, I stressed the negative aspects of shipping protectionism, because policy-makers in the developing countries have a misconception that protectionism is helpful to their national interest. This concept can not be accepted whether we consider only the shipping industry or overall economy.

Protectionist policies naturally remove incentives to efficiency and cost control, as a result its fleet might lose competitiveness. Furthermore, it gives damages to trade and economy because uncompetitiveness fleet raises the cost of shippers.

It is meaningful to remind that this policy distorts the rational utilization of resources. The reasons is that the opportunity cost of capital in the developing countries is higher than others. In other words, there are other urgent areas which need money

I accept that protectionism has an enormous political appeal, but national pride with economic loss can not be justified in current global economic situation. Therefore we have to find sustainable solution.

These are examples of solutions I gave : i.e.

i) Regional cooperation in order to form bigger market.

ii) Cooperation with the developed countries through joint ventures and services in order to cope with capital and technical problems.

iii) Giving priority to infrastructure development than shipping.
Besides above, I think that there might be other reasonable solutions to promote economy and shipping.

And then, we need cooperation and negotiation between the developing and developed countries to increase global welfare and avoid a dangerous situation when a country adopts a selfish policy. Countries should make an effort to remove unfavourable factors in the developing world and cooperate each other in order to increase mutual benefits.

In addition, S. Korea, which is relying heavily on cargo reservation and maritime subsidies as a policy, is regarded as a successful example from the viewpoint of shipping development.

As a matter of fact, her development can be linked to her better economic performance and other comparative advantageous factors than government intervention. On the contrary, government misled her shipping industry, as a consequence, it faced big crisis in the middle of 80'.

It is ironical that government intervenes too much in the private sector, even though the S. Korean fleet has a lot of favourable elements. Therefore I think that this is the right time to minimize government intervention and throw away ineffective policy. If more autonomy is given to the private shipping company, its her shipping industry should contribute to the world trade in a liberal atmosphere.
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