

SPEECH

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Competition developments affecting the maritime sector

European Maritime Law Organisation

London

14 October 2005

Check Against Delivery
Seule texte prononcé fait foi
Es gilt das gesprochene Wort

Mr Chairman,
Ladies and gentlemen,

Introduction

I am very grateful for this timely opportunity to talk about the application of the competition rules to the liner sector, and in particular about the review of Regulation 4056/86. This Regulation contains an exceptionally generous block exemption for liner shipping conferences, and contains the only procedural exception to the enforcement of competition rules as regards cabotage and tramp vessel services.

Context

Let me outline how we see the markets so that it's clear why reform of this sector is relevant in terms of the Lisbon Strategy.

The Commission is bound to ensure that the rules in place reflect today's market conditions. The last nineteen years have seen considerable changes in the liner market. There is a continuing trend towards full containerisation and an increase in co-operative arrangements between shipping lines in the form of consortia and global alliances. We have seen average growth rates of world container trade close to 8% during the last 10 years.

The sector is important for the economy as a whole. Scheduled services in container transport account for about 40% of the EU's external trade by sea in value terms. Today, conferences are allowed to fix prices on all major shipping routes, and these prices are generally assumed to act as a benchmark for the prices actually applied in the market.

In addition to the benchmark effect of the conference tariff, an average of 30% of the price of transport is made up of charges and surcharges jointly fixed by lines participating in conferences. The same levels of charges are very often applied by non-conference carriers.

In overall terms for the European economy, this means that 18% of imports and 21% of EU exports are affected by carriers' ability to jointly fix prices in the liner conference block exemption.

The legislation setting out how Articles 81 and 82 apply to international maritime transport cannot continue to be anchored in the market scenario of the 19th Century. The review is necessary because the block exemption has no end date and it will remain in force until positive action is taken.

Market developments

The rules may have been in standstill, but the market has not. Globalisation of international production has had huge impact on container trade, resulting in massive growth in deep sea volumes especially from Asia.

On the demand side, we understand that shippers are looking for customer focused relationships, reciprocal performance related compensation and integrated logistic solutions.

On the supply side, carriers have tripled capacity in the last 10 years to cope with the growing demand coming from the increased trade flows.

In a more recent development, there has been a series of mergers in the liner sector in the past six months. The consolidation process is positive because the liner shipping industry still has a low concentration rate - at the level of individual lines - and a greater rationalisation should help the European industry to compete more efficiently on the global market.

When assessing the impact of these mergers, in particular possible co-ordinated effects on the market, the Commission takes into account the parties' membership of conferences, consortia and any other co-operative arrangement entered into with competitors. Carriers often cumulate the benefits of the Conference Block Exemption with those arising from the Consortia Block Exemption Regulation on the same trade.

After an extensive market investigation, the Commission cleared the acquisition of P&O NL by AP Møeller, subject to conditions, in July. This week, the Commission cleared the acquisition of CP Ships by TUI, which controls Hapag Lloyd, also subject to conditions.

There is vertical integration taking place as well, with shipping lines becoming terminal operators and entering the market for stevedoring services. A recent example is the Euromax joint venture between P &O NL and ECT container terminals. There are cost related considerations in these transactions but they also reflect a response to the market's need for high quality integrated logistic solutions.

From a regulator's point of view the objective in vetting these vertical mergers is to ensure that there is no foreclosure effect for other port services operators, or other carriers.

The review process

The changes in market conditions and the modernisation of the competition rules of procedure were the two main driving forces behind the decision to review Regulation 4056/86.

The process is transparent. Our belief has been that a public debate could cast some light on the polarised views of shippers and carriers.

In the three years since we started the review process, we've had three rounds of public consultations, a public hearing, and several discussion documents and a White Paper have been published. Member States have input into the process so far throughout.

The review is due to end with a legislative proposal to repeal Regulation 4056/86. In the Commission's Work and Legislative Programme, this proposal is foreseen for the last quarter of 2005.

Tramp and cabotage

Let me say a few words about tramp and cabotage, which are currently excluded from the competition enforcement rules.

It is hard to advance any justification for the fact that these sectors are the only ones to which Regulation 1/2003 does not apply. The rules of substance set out in the Treaty in Articles 81 and 82 already apply to cabotage and tramp vessel services. The debate is only about whether the general procedural rules should also apply. The tramp industry has asked for the Commission to provide guidance on how competition rules would apply to their sector, in particular in relation to agreements such as pools that are common practice in this and other industries.

The Commission privileges substance over form. It is only when we will have understood more about the issues on which guidance is said to be required that we can debate the most appropriate form in which to provide it. We are therefore discussing with industry with a view to identifying the issues to which the Court's jurisprudence and the Commission's decisional practice provide no answer. We will be pressing industry to focus on the substance of their agreements and to come up with more specific information so as to allow us to determine how they fit in the general framework of competition law. And in particular, whether any novel issues arise.

A repeal of the conference block exemption

After three years of reviewing this sector, our view is that the structure of the liner market is only as unique as that of any other transport sector. And price fixing is unheard of elsewhere.

There is a significant amount of market data in the thousands of pages posted so far on our website. Much of it was volunteered by carriers themselves and we are grateful for their input. I would like to highlight a few significant findings so far:

Conferences today agree voluntarily on formulae for certain surcharges and ancillary charges, in particular currency and bunker adjustment factors (CAFs and BAFs) and terminal handling charges.

The same level of charges, or adjustment factors, is often applied by non-conference members.

It is far from clear that the joint fixing of terminal handling charges falls within the scope of the conference block exemption regulation. It is very clear that the joint fixing of charges and surcharges by lines that are not members of a conference do not. It will be difficult to advance a case that such price-fixing is compatible with the competition rules.

If we look at the liner sector at the level of individual lines, concentration is low. However, if account is taken of all the co-operative arrangements entered into by carriers – as we must to assess the competitive picture - we find that most trades from Europe are very concentrated markets (above 2000 HHI) and the remaining ones are concentrated markets (between 1000-2000 HHI).

Removing the conference block exemption means that competition rules will apply to liner shipping just as they apply to all other sectors. Price fixing and capacity regulation on a trade basis will be banned.

This said, we know that the sector already has another generous block exemption. Since 1995, the Commission has accepted that co-operation amongst liner shipping companies for the provision of a joint service improves the quality of the service that would be offered by the lines individually.

This consortia block exemption (Regulation 823/2000) was recently found to be working well and extended until 2010. This means that – apart from price fixing – carriers are able to enter into very extensive co-operation provided that it results in a joint service. Consortia and global alliances have flourished in the past years, often servicing 40-50% of the entire market.

So, if conferences are abolished, co-operation between liner shipping companies will continue to take place in consortia and alliances. The concentration ratio would then diminish significantly in major East West trades, less so in North South trades where conferences and consortia members are often the same.

As the reliability of services is in function of the competitive situation in the trade, it appears unlikely that it will be affected by the removal of the conference system. Service innovation and service quality are only spurred by competition.

Need for a successor regime?

Nowadays price fixing as such is becoming less and less relevant to many carriers' business strategies. In the main trades to and from the EU, we see the increase of individual service contracts as a preferred option to the conference tariff.

This said the position between shippers and carriers is still polarised.

We are grateful to the ELAA (European Liner Affairs Association) for having come forward with a proposal to replace the conference system with an exchange of information system that does not involve the setting of a common tariff. According to the ELAA this information exchange system is necessary so that lines can make investment decisions for new ships, and so they can better understand market conditions to make short term adjustments.

Shippers on the other hand are adamant that the conference system is a relic of the past and that to meet the challenges of a global market place, carriers must embrace competition fully. They consider the consortia block exemption regulation sufficient to guarantee a sustainable and reliable supply of shipping services, and are pressing for the abolition of the conference system.

Information exchanges in the EU

There are no hard and fast rules when it comes to the analysis of information exchange schemes. Often, exchanges of information do not constitute a restrictive practice at all. To determine whether an information exchange between competitors is a restrictive practice, a case by case assessment must be carried out.

Information exchanges – case by case assessment

The Commission focuses its analysis on (i) the characteristics of the information exchange itself and (ii) the characteristics of the environment in which it takes place.

When looking at the characteristics of the information exchanged, we will consider the nature and type of the information, so whether it is publicly available or commercially sensitive data, current or historic data for example. We also take account of the level of aggregation and, generally speaking, exchanges of individual data are considered problematic. The frequency of the exchange and the institutional arrangements are also considered. Data may be shared by the participating firms directly or processed via an independent third party. Other issues that are looked at are the extent of market coverage and the homogeneity of products. The bigger the market coverage of the information exchange, the greater the potential for anti-competitive effects. Similarly, collusion will be easier if products are homogeneous.

Broadly speaking, an information exchange system will be prohibited when its effect is to replace the normal risks of competing by practical co-operation, or when it allows competitors to observe each others' market strategies and to adapt behaviour accordingly.

Information exchanges – compatibility criteria

The ELAA requests that its proposal for an information exchange system be endorsed by the Commission.

In order for the Commission to endorse anything that is restrictive of competition, we must be confident that the four cumulative conditions of Article 81.3 are met. And the burden of proof to demonstrate this is for the industry to discharge.

In other words, once we determine that an information exchange is likely to have an appreciable adverse impact on competition, we need to be sure that it generates efficiencies and that there is a direct causal link between the restrictive practices and the efficiencies generated. In addition it is also necessary to determine that such efficiencies cannot be achieved by less restrictive means, and that consumers obtain a fair share of the overall benefits. Finally, it is crucial that competition is not eliminated.

Assessment of the ELAA proposal: potentially positive

One of our main difficulties with the ELAA proposal is that in many instances we do not understand at present how it relates to the purposes it is supposed to achieve.

There are some features however that appear less problematic from a competition point of view. This is the case in particular of exchanges of information on capacity, provided adjustments are made with regard to the level of aggregation and frequency of exchanges.

But even in these aspects of the proposal there is much that is unclear. For example, if the declared objective of the exchange is to ensure security of investment, how indispensable are monthly exchanges of data when there is usually a two to three year gap between the decision to order a new container vessel and its delivery?

Carriers are now developing further, new arguments to justify their case. We welcome their acceptance that new arguments were needed. And we will examine them closely.

Assessment of the ELAA proposal: Negative

The features of the proposal with which we have the most problems are the price index, the joint fixing of charges and surcharges, and the discussions amongst competitors in the trade committee.

We are told by carriers that they will only invest in new capacity if they have a reasonable expectation that such investments will be profitable. And that is why they say they need the price index. But it seems questionable whether a price index containing 3 month old price data is indispensable in the context of investment decisions into new capacity that will only be available two years after.

More worryingly, the price index may reveal the average of confidential service contracts on trades where these types of contracts make up a significant proportion of the trade. This quarterly price index could operate as a signalling system to the market and enable an individual carrier to benchmark its own pricing so as to not deviate excessively from the current pricing level of its competitors. This would be much in line with what happens now in conferences through the periodic announcements of general rate increases (GRIs) .

We tend to think that it's likely that carriers engaged in liner shipping would look to the index for guidance because this is how the market has always operated up to now.

With regard to charges and surcharges, which constitute on average 30% of the price of transport, we find it difficult to accept that price-fixing is indispensable to the achievement of any efficiencies. Why should all shippers pay the same fuel surcharge when ships have different fuel consumption rates? And as terminal operators charge carriers individually why is it that shippers have to be charged collectively by all lines?

Most importantly, even if carriers decide to pass on standard commercial risks to shippers, it still does not explain the need for carriers to fix surcharges jointly through a common formula. In the airline industry for example, airlines frequently impose fuel surcharges on passengers but they do so on an individual basis without collective agreements with other airlines.

A trade committee where competitors discuss, interpret and evaluate market data looks in principle like a scheme aiming at eliminating uncertainty as regards their future market conduct. It necessarily implies that each of them takes into account the information obtained from its competitors and acts on that information on the market. The trade committee would obviously provide a potential forum for anti-competitive agreements between carriers. Given the history and the concentration ratio on a trade basis, the likelihood cannot be dismissed that a trade committee fed with regular, precise and updated market information could lead to or facilitate collusive practices.

It remains unclear to us why there is an additional need for discussion of factual data. Trade managers are industry experts who should be capable of independently interpreting and evaluating factual market information without discussing it with their competitors.

What concerns us most about the ELAA proposal as it stands is that it does not differ in principle from the practices of the conferences today. It actually constitutes an expansion of

the scope of conferences because it extends the geographic scope to world-wide, with potentially 100% coverage by the industry, and relying on extremely accurate data derived directly from bills of lading.

Continuing dialogue

Let me conclude by reasserting the Commission's intention to continue our dialogue with industry. We will be seeking clear indications from the liner industry of what it needs in order to function effectively.

If the industry thinks it needs to go beyond the established legal framework - and I am thinking of the consortia block exemption, the horizontal co-operation guidelines, and the exchanges of information that can take place without breaching Article 81 - it must provide substantiated facts and arguments. Above all there must be a direct causal link between any restrictive arrangements and the claimed efficiency.

We find some aspects of the industry's current proposal to be innovative and potentially beneficial – I refer in particular to the idea of an independent data clearing house that could provide for better quality, updated information on the market that could in turn allow for better planning. If designed properly, this could benefit the whole industry – carriers and shippers alike.

We will also continue our dialogue with the tramp industry so as to understand if the agreements they traditionally enter into, or the practices of the industry, constitute novel questions requiring specific guidance from the Commission.

Over the next few weeks, we'll be working to produce the impact assessment of the repeal of Regulation 4056/86, and the impact assessment of the proposals of both the carriers and the shippers about what should come then.

Commissioner McCreevy will then make his proposal to the Commission.

Thank you for your attention.