

Market Distorting Factors from Korean Shipbuilders' Perspective

First of all, I would like to thank Mr. Chairman and the Secretariat for the efforts to organize this special session. We hope that this session will contribute to the deliberations for the WP6's future direction, especially relating to market distorting factors and an approach to deal with them.

As noted in background paper of special session(C/WP6(2012)15), OECD WP6 has dealt with factors that could distort normal competitive conditions in the shipbuilding industry since its creation. Government, shipbuilders and experts also have participated in lots of discussions on market distortions through shipbuilding negotiations, regular WP6 meetings and workshops with non-economies for the last 20 years.

We therefore understand that the Secretariat's paper on market distorting factors can serve as the launching pad in the efforts to discuss WP6's work program for the next two years, especially on whether or not there are market distorting factors in shipbuilding.

Firstly, let me explain current market status of world shipbuilding industry. According to data released by Clarkson, world new orders for the 1st 3 months this year was just 3.8 million CGT worldwide, a down of 40% over the same period of last year owing to economic downturn, oversupply in shipping side and ship financing crunch caused by Euro zone's economic uncertainties, etc. Even new orders of commercial vessels were dramatically dropped. Also notable is the fact that this weakened market will be continued for the time being.

And Korea shipbuilding is no exception, which is under an approximately 40% drop in new orders over the same period of last year. These are no different from an inevitable flow-effect.

In relation to newbuilding demand of long term perspective, recently most reports indicate that decrease of newbuilding demand seems to remain for another year to come and its recovery seems uncertain at this stage. However, the "base" case forecast from Clarkson projects that there will be a gradual upturn in contracting of the medium term as followings.

**Long-Term Newbuilding Requirement 2014-2021
Scenario Summary**

	Average Requirement Per Year		
	No. Ships	Mill. GT	Mill. CGT
Avg. 1996-2011	1,911	65.6	36.1
Avg. 2012-2013	1,386	53.4	30.0
Avg. 2014-2021			
Low Case	1,241	48.0	28.4
Base Case	1,694	66.2	38.5
High Case	2,321	87.4	50.9

However, market forecasting is very difficult work. For example, previous forecast of supply & demand have turned out to be far from the reality and revealed the structural weakness from the complexities and uncertainties of various factors. Therefore, reference to the forecast on supply and demand need to be cautious and limited in regard to the policy making process.

Forecasting Time	Forecasting Period(1996-2005, m cgt)		
	Forecast(A)	Delivery(B)	A/B
Koshiya 1996	16.5	20.8	79%
CESA 1996	15.8		76%
SAJ 1996	13.4		64%
Forecasting Time	Forecasting Period(2006-2010, m cgt)		
	Forecast(A)	Delivery(B)	A/B
Koshiya 2001	22.4	40.2	56%
CESA 2001	18.3		46%
SAJ 2001	19.3		48%

From now, we will address possible restructuring & downsizing of capacity in world shipbuilding. Even if it is the fact that world shipbuilding market is inflexible industry from the supply side and there has been chronic overcapacity for a long time because of continued participation of new emerging countries, lots of facilities were constructed and world capacity has increased for the last shipbuilding boom. Therefore, there is a possibility that overcapacity could be seen in the future given the recent falling of new orders. However, many shipyards are now seriously

experiencing financing difficulties. As noted before, lots of shipyards were already withdrawn from the market.

Shipbuilding associations of each country, shipbrokers and consulting companies have evaluated world shipbuilding capacity at times. Those evaluations are clearly showing significant divergence and different projections on future capacity. That is why there's no common methodology to evaluate capacity in the shipbuilding industry.

It means that it might have much of subjective views in calculating shipyards' productivity. Capacity evaluation is a time consuming and tricky work and it's hard to get cooperation from shipyards. It eventually could trigger inaccuracy in capacity evaluation.

(Unit : Mil. CGT)

	OECD 2003	KOSHIPA 2007	SAJ 2008/11	CESA 2012	Clarkson 2012	Actual Output
'06	-	38.9	-	-	-	32.1
'07	27.9	-	35.0		-	35.4
'08	-	-	-	-	-	43.0
'10	56.6(2011)	-	57.0			52.2
'11						49.8
'12	-	50.0	-	-	52.0	-
'15	-	-	70.0	57.7	41.0	-

And also, world shipbuilding industry is carrying out a restructuring globally. There will be a change in the shipbuilding capacity. It doubts that capacity will be increase even if the demand is going to be sluggish. The shipbuilding sector, like any other manufacturing, is controlled by the market principles of supply and demand.

In principle, KOSHIPA agrees on Clarkson's forecast and we believe there will be no capacity expansion at least in the future. It's so doubtful that there will be a big gap between capacity and demand continuously.

Secondly, we would like to focus on market distorting factors from shipbuilders' perspective. It is well known that there has not been a consensus on the definitions of market distorting, normal competitive conditions, its impact on market and regulating method, etc., in the last negotiations, meetings and expert workshops.

Therefore, even if WP6's reports on market distorting factors for this session identified issues for discussion, we still concern whether in-depth discussion of each will be really productive.

For instance, para. 4 of Background Paper[C/WP6(2009)17,] titled "WORKSHOP ON MARKET DISTORTING FACTORS IN THE SHIPBUILDING SECTOR" correctly summarized that

there was never an agreement on the actual meaning of the terms "market distortion" indicated that it would be impossible to establish ex ante whether a subsidy was market distorting or not, as this could only be decided ex post.

And Para. 33 of this paper for Workshop, which was last workshop on market distorting, correctly indicated that

It is a very difficult issue on which to provide background and guidance, because throughout the SNG negotiations there were two distinct schools of thought on this aspect of the draft Agreement. One maintained that there were pricing and other practices that seriously distorted the market. The other maintained that it was unlikely that there were such market distorting practices in shipbuilding, and that the real cause of price distortions should be dealt by eliminating government support measures through effective and comprehensive disciplines.

With this, we don't think that it is meaning to here discuss what is market distortion and its impact on market and regulating method, etc,. We all have to avoid these time-consuming activities any more considering current severe market condition, change of market climate etc.

However, with respect to market distorting factors, it has been widely understood that we all have to join forces to eradicate anti-competitive measures such as reckless supports of the government which could distort the shipbuilding market.

As noted in Worldyards' report, market distortion is essentially linked to government action. In short, any individual enterprise could not exert sufficient market power to distort the shipbuilding market. These arguments mentioned in this report are exactly same as Korea has said numerous times at the shipbuilding negotiations, WP6 meetings and workshops. We here once again support this analysis. Worldyards reports ;

Worldyards' position is that the nature of the shipbuilding market makes it quite difficult to achieve market manipulation by private sector market participants, from either the supply side (the shipbuilders) or the demand side (the shipowners).

Even if the shipbuilders had a higher degree of ownership concentration, the general tendency for shipbuilding overcapacity would make it difficult for even the most dominant builder to achieve pricing power in the market shipyards are unable to individually or collectively distort market conditions in their favor. In contrast, we contend that only governments are capable of influencing the price of the production factors or institute other measures to shift the competitive outcome in favor of its home industries. The framework contends that governments, unlike market players, can – and do -- influence the demand/supply curve, even if that is not their main policy objective.

Therefore, recent government assistance to increase capabilities and government policies for their own shipbuilding and shipping industry such as local contents and home building for domestic shipping demand would be problems that can distort imbalance in the shipbuilding market. In particular, we all have to be cautious about government intervention in the middle of market depression.

However, on the other hand, we know that not all subsidies used by a country to achieve its policy goals are market-distorting. In this sense, WTO ASCM reads that :

It is recognized that government assistance for various purposes is widely provided by Members and that the mere fact that such assistance may not qualify for non-actionable treatment under the provisions of this Article [ASCM Article 8] does not in itself restrict the ability of Members to provide such assistance.

In retrospect, Korean shipbuilders have participated in a lot of discussions of WP6 so as to establish normal competitive conditions in world shipbuilding for the last 20 years through two rounds of shipbuilding negotiations, regular WP6 meetings and workshops with non-economies.

However, as all of you can see, this is a time of great hardship and in this reason lots of shipyards now stand at the crossroad of survival. Most small and medium-sized shipyards closed already its door. It expects that world shipbuilding industry will be on very severe reorganization for 3-4 years from now. And shipping industries are no exception.

Here, let me introduce Korea's case on small and medium-sized shipyards. As you may know, most small & medium sized shipyards in Korea were already closed. Many shipbuilders in the field do not think that today's difficulties result from external factors such as financial crisis is not policy issues but market issues. In other words, it is not easy to address this problem with policy in a short period of time. In realty, volume for new orders, especially commercial ships, disappeared from the market. It means that it will take more time to deal with it efficiently than we expected.

In these difficulties, it understands that our discussion could allow fruitful exchange between WP6 members and industries on market and government policy without repeating similar issues. In this perspective, we need to note that the final ranking of priorities for WP6' 2013-2014 work program(para. 11/Table 2 of C/WP6(2012)8) indicates many issues related with market distortion issues(approximately 4 among 8) in white area.

Instead of doing so, it is more natural for all to discuss and address ways and means to create new demand considering recent difficulties on market. Discussion has to be future-oriented reflecting structural change of market globally.

The recent shipbuilding climate has changed dramatically over the past years such as a shift of major shipbuilding country, change of market share between them, a rapidly developed technology, innovative building method, and introduction of new regulations. Along with this big change in world shipbuilding, discussion has to be

reshaped in accordance with these new trends. Otherwise, it is just time for all to deliberate seriously on its function.

Finally, to address market-distorting factors, the involvement of non-member countries is essential since they rank high in production capacity and market share in the global market. Without their participation, discussions on identification and progressive reduction for market-distorting factors don't work out.

In light of the above, government should give first priority to policy discussion to increase shipyards' workload instead of providing subsidies, protecting domestic shipyards, which could trigger market imbalance. Shipbuilders also should create a climate in which their yards can increase their international competitiveness in these difficulties by the medium of increase of productivity, diversification and reshape of portfolio.