

OECD Council Working Party on Shipbuilding

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WP6 Workshop on Maritime Clusters and Global Challenges

Paris, Thursday 1 December 2016

In the 19th and 20th century shipbuilding grew as an important and strategic industry in a number of economies around the world. Britain was the world leading shipbuilder for a long time and important capacities existed all over Europe. Through a phase of heavy industrialization several of the now leading economies developed in the second half of the twentieth century their production technologies and human capital. Shipbuilding was one of key pillars, along with important spill-overs to the iron and steel, electronic, and machinery manufacturing industries. Largely motivated by a strong maritime tradition Japan used in the fifties and sixties shipbuilding to rebuild its industrial structure and surpassed in shipbuilding everybody. In the seventies South Korea started to make shipbuilding a strategic industry and China repeated these models more recently with large state-supported investments. However unlike Japan and Korea, whose growth took a couple of decades to complete, China's growth in shipbuilding consisted of huge increases in deliveries during the last decade. A number of developing economies are at present trying to follow the Japanese, Korean and Chinese examples but here some skepticism about their success might be appropriate.

As a result serious excess capacity existed most of the time and the shipbuilding capacities in a number of European countries went into serious decline and came often practically to a stop. On the whole the world shipbuilding market suffered over-capacities, depressed prices, low profit margins, trade distortions and widespread subsidization. It is difficult and problematic to single out and pinpoint one particular source of additional capacity – such as military conversion, structural adjustment or building of new and additional capacity. It is also difficult to pin point any particular region or country in the world as a cause of emerging global surplus. Overall the center of gravity moved during the last fifty years away from Europe to the Far East.

This broadly shows the history of the industry during the last fifty/ sixty years, it was a permanent fight for competitive conditions against surplus and its consequences. In our market economies, where governments do not normally interfere with the decisions of the business sector, there is, in the final analysis, no other judge than the buyer of a ship and his assessment of the product and the service he can obtain from a particular builder. However this does not dispense governments from examining very carefully the international

competitive conditions in which their industry is operating and to direct their efforts at establishing measures respecting normal competitive conditions.

It was in the early sixties that expansion of world shipbuilding showed first serious signs of overcapacity. Governments, anxious to see their countries' shipbuilding capacities fully employed, significantly increased and outbid each other for subsidies of all kind in particular subsidies for export credits. This led in sixtysix the OECD Council to create the OECD Council Working Party on Shipbuilding mandated with the restoration of normal competitive conditions in the shipbuilding industry. The way of operating of the Council Working Party was and still is through increasing transparency, exchange of information, monitoring, peer review and moral persuasion and has taken the form of various OECD instruments which its members have adopted.

The Council Working Party started with work on subsidies aimed at reducing the volumes of subsidies, which OECD countries provide to shipbuilding. This activity resulted in sixtynine in the Understanding on Export Credits for Ships setting rules to be applied to publicly supported ship export credits. These rules were subsequently revised several times during the years till now. They now constitute an Annex to the “Arrangement on Officially Supported Export Credits”, the so-called “shipping protocol”. It sets out the following provisions;

- 12 years maximum repayment term;
- minimum 20% cash payment by the purchaser no later than delivery date,
- repayment of the loan to be in equal instalments at regular intervals
- interest periods to be at least 6 months, maximum 12 months and
- a Credit Agency premium to be adjusted to reflect credit and the political risks incurred.

The Arrangement is a “gentlemen’s agreement” among participants and should enable exporters to compete on equal terms with other exporters with access to national export credit schemes. A key element for the effectiveness of this instrument is however membership to the Arrangement and its protocol. Unfortunately new and emerging main player sometimes show great reserves to adhere to these rules and, through this, water down the effectiveness of the arrangement.

The work on subsidized export credits was in the following extended to a broader range of subsidies. The shipbuilding crisis, which was emerging in the early seventies, lead to a gradually recognised excess capacity of a permanent nature. The Working Party consequently focused its attention on the issue of shipbuilding capacities and deployed its

efforts to make contributions to problems that were considered not to be resolved by countries individually.

As a result the “General Arrangement for the Progressive Removal of Obstacles to Normal Competitive Conditions in the Shipbuilding Industry” was concluded in 72. It was renewed, revised and strengthened in seventy six and eighty three. In its last revision - known as Revised General Arrangement – OECD governments state that normal competitive conditions in the shipbuilding industry are disturbed, *inter alia*, by:

- Government subsidized export credits;
- direct subsidies to the shipbuilding industry,
- customs tariffs or any other import barrier;
- discriminatory tax policies,
- discriminatory official regulations or internal practices;
- specific aid for investments,
- subsidies for restructuring of the domestic shipbuilding industry and
- all other forms of indirect public aid which are obstacles to normal competitive conditions in the shipbuilding industry.

The Arrangement called upon all governments to do their utmost to ensure their progressive removal – unless there were imperative reasons for doing so, in which case assistance should be short, digressive and accompanied by remedial action. However, unlike the 76 version the revised 83 version did not contain a deadline for elimination of subsidies.

A third type of task emerged for the Council Working Party with the beginning of the crisis and to which many OECD governments initially responded by means of measures to stimulate the industry. However, the crisis turned quickly out to be of a longer-term nature and revealed the existence of significant excess shipbuilding capacities in the world – in the order of 50% of the total. The Working Group set up subgroup on Demand and Supply to be better informed of the surrounding market development. The aim was to try to ensure a balanced allocation of new ship orders among the member countries to avoid concentration of orders in one country or a group of countries and in the long term to adapt production capacities to new market conditions. To this extent it set up a system for the continuous collection and exchange of information on new orders, order book, ships delivered, capacities and labor force.

The risk of “free riders” called for close international co-operation to ensure that every country took a share in the burden of capacity reduction. The consensus of governments to cooperate in this field found its expression in the General Guidelines for Government Policies in the Shipbuilding Industry calling in particular for close co-operation to eliminate excess capacity and to restructure shipbuilding industries. They were agreed by the Working Party in seventy six and strengthened and revised in eighty three.

As to the policy impact of the Guidelines/Arrangements, compliance was explicit not made. Experience showed that they had only a limited impact on government policies. Repeated reference was made in government papers invoking principles of solidarity, fairness and international responsibility that each shipbuilding country plays. In fact national considerations most often ruled out international ones so that these Guidelines/ Arrangements - as said - hardly helped to solve problems of excess capacity in the shipbuilding industry.

In view of this and upon the request of the United States, negotiations were launched in 89 to create a binding mechanism for the elimination of all government support to shipbuilding and – upon the request of the EU - of dumping practices- called “injurious pricing”. These negotiations went on and on and were finally concluded in July ninetyfour. The entry into force the agreement stipulated that all countries which participated in the negotiations had to ratify the agreement. In a nutshell the ninety four Agreement - called “Agreement Respecting Normal Conditions in the Commercial Shipbuilding and Repair Industry” - created, in a legally binding manner, a level playing field for competition in shipbuilding of the OECD countries and Korea, which together made at that time up to 80 per cent of the world market. It did so by three basic elements;

- a) a subsidies discipline, which bars direct and indirect subsidies as well as official regulations and practices in favor of the shipbuilding industry;
- b) an injurious pricing instrument which makes anti-dumping applicable to shipbuilding; and
- c) a binding dispute settlement before an international panel in case of violation of the subsidy discipline an/or the injurious pricing instrument, backed by remedies and sanctions

When the agreement was signed in Dec.94 the target date for entry was January 96 but by that date only the European Union, Norway and Korea (which was at that time not yet a Member of the OECD) concluded the necessary procedure. Japan followed suite during the first half of 96 while the coming into force of the Agreement was stuck in the US Congress.

In June 96 the US House of Representatives voted on the implementing legislation and approved a bill which contained the following amendments:

- a) an extension of the period for terminating guarantee provisions and providing that vessels that have obtained guarantees under the old terms of the Title XI be delivered by January 2002;
- b) clarifying language that nothing in the Agreement would have the effect of changing the US built requirement of the Jones Act, and
- c) an exception for defense features, clarifying those such features in commercial vessels would not be subject to any provisions in the agreement.

These provisions were clearly in conflict with the terms of the Agreement. A large number of meetings were held in the OECD but also in the US Congress to find a way out but none of the participants was unfortunately prepared to compromise. Also was the coming into force of the agreement among the four discussed but also here the participants were not prepared to accept this.

In the years after 96 the whole shipbuilding market changed. Shipbuilders in various parts of the world increased their capacities by reactivation of capacities removed previously from the building, conversion of former naval installation, restructuring of outdated capacities and the building of new capacities. In particular Korea significantly increased its capacities and China entered the market at a large scale. At the turn of the century and after endless debates about possible alternatives, the judgment was made that it would be most unlikely that the 94 Agreement would ever come into force. The Working Party consequently called on the OECD to consider the commencement of a new round of negotiations. In September 2002 a Special Negotiating Group (SNG) was created and invited all non-OECD economies with significant shipbuilding industries to participate in the negotiations on an equal footing with OECD member countries. Together, with the OECD members, participants in this round of negotiations represented around 95% of world shipbuilding capacity.

The negotiations continued until September 2005, when the Chairman of the Special Negotiating Group "paused" them for an unspecified period, in order to allow the parties to reflect on their positions, to talk to each other and to observe developments in the market. It was intended that the negotiations would be resumed when the environment for success had improved.

The negotiations resumed in 2007 but despite strenuous efforts by all parties

participating in the negotiations, the differences between some of the participants could not be bridged. The issue of a pricing mechanism was central to some key participants, who believed that this was a crucial element of any workable Shipbuilding Agreement. However, others held the view that it would be better to focus on government subsidies and other support measures, without which such pricing distortions could not be sustained.

No one of the participants could be blamed for such failure. There were new important participants and the market environment was largely different to the one earlier. It was therefore that in December 2010, the OECD Council terminated the negotiations. In terminating the negotiations, the OECD Council noted that this would not affect the Working Party on Shipbuilding, which would continue to carry out work in fulfillment of its mandate.

During the negotiations of an agreement and especially after 2010 the Working Party, often in collaboration with non-member economies and industry, considered a large number of issues aimed at informing governments about developments and helping them in formulating their policies. These concerned changes to the policy landscape in member and non-member economies, the global demand and supply balance of the world shipbuilding industry and the impact of technological and environmental developments on the shipbuilding industry. Furthermore there were a large number of workshops on, such as, supply and demand, market distorting measures, green growth, the global value chain in shipbuilding etc. The purpose of these was to provide transparency of trends and developments to member and non-member economies and thus to contribute to some orderly development of the industry.

This brings me to the future of the Working Party and its activities. Is the Working Party still providing a useful role in spite of the fact that it did not succeed entirely in its main task to establish normal competitive conditions in the market? Experience has recently so far shown that national political and micro and macro economic interest were just too divergent to achieve legally binding agreements. It can on the other hand probably be said that without the WP6 subsidies to shipbuilding would have been even higher as they were at that time. The Working Party was and is the only place where OECD Member and non-Member economies work together in order to, inter alia, review world-wide the effects of government subsidies, developments in shipbuilding capacities and ship demand, examine their impact on the market, receive reports on pricing and are regularly informed on the findings of shipbuilding specific studies.

In my personal view the Working Party should, even if subsidies and uncompetitive pricing methods distort normal competitive conditions, have a very careful examination of the overall situation before they revert to what we have done in the past i.e. guidelines,

arrangements or even legally binding agreements. To be effective any such instrument needs a large percentage of the world's total shipbuilding capacity. However the composition of shipbuilding countries has changed dramatically and the new and important players show little willingness – as far as can be seen at present - to adhere to any sort of agreements – binding or not binding.

This does on the other hand not signify that the Working Party should not deal with issue like subsidies, injurious pricing or oversupply. On the contrary the Working Party should, in collaboration with all non-member economies having an important shipbuilding capacity, have an exchange of on these phenomena.

In more detail I see the Working Party, in permanent collaboration with non-members, to keep under permanent review and exchange views on phenomena affecting the industry such as

a) macro factors; economic performance and political stability; world seaborne trade, oil prices having effect on shipbuilding and the maritime industries as a whole;

b) market and non-market factors; subsidies to shipbuilding by the government and local authorities, capacity of shipyards, vessels on order, pricing, the working of ‘shipping protocol’ of the Export Credit arrangement, local content of vessels, availability of vessels for scrapping, charter rates and its influence on shipbuilding;

c) innovation; technical and economic; technical and environmental aspects of vessels,

d) political considerations: strategies pursued by individual or group of countries, energy and environmental policy questions;

e) human capital: intensify work in collaboration with relevant trade unions on exiting and future manpower, new skills requirements, and programmes for shipbuilding management; analysis of the employment relationship and its influence on health and safety;

Besides such items of a more permanent nature I see a number of special studies on maritime industries as a whole inter alia containing information and analysis about the state of the art in member and non-member countries, existing patents held by member and non-members, the application of Intellectual Property Rights (IPR) on shipbuilding, the specific competitive situation for certain products and solutions and the application of WTO rules on shipbuilding. In addition the holding of workshops with non-member economies on issues of common interest should continue.

In the longer term the Council of the OECD might examine to create a focal point where economic and political aspects of all maritime industries and their relation among each

other as well as other related industries could be considered.

To sum up. Working Party 6 on Shipbuilding is and remains – even after 50 years of existence – an important place where governments can exchange views on important issues which are facing the industry and develop – if they are convinced that they are necessary – common approaches to these. As for today I wish you all a fruitful and informative workshop on maritime clusters and their economic challenges.

Thank you
