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## EAST WEST SHIPPING

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My last port of call, if one may use that expression, before your country was Copenhagen, where I had spent two days in close discussion with the Danish administration about the shape of our work programme in the next six months, a period in which Denmark carries responsibility for the management of the European Communities affairs. Clearly we spoke of many matters. But in the maritime domain two issues dominated our discussions. One was an important but purely internal issue relating to the use of our canals, our internal waterways, significant stuff but for internal consumption. The other was more far reaching and indeed more fundamental in its significance and its potential impact. It relates to the actions which must be taken if our shipping lines are to be protected from exploitative action by the so called state trading countries of Eastern Europe.

### East-West Problems in Shipping

I should like to make a few remarks about how we in the Commission of the European Communities see the problem of competition in cargo liner shipping from certain state-trading countries, in particular the Soviet Union. This is, of course, a problem whose effects are felt on both sides of the Atlantic; the United States and the Community have a common interest in tackling it.

The Soviet Union's merchant shipping fleet has been expanding rapidly since the early 1970s. The Soviets now have the sixth largest merchant fleet in the world, and have already overtaken the United States, which ranks eighth. The emphasis lies clearly

on general cargo ships, where the Soviet Union has been number one since 1974. Half its fleet consists of general cargo ships. The Soviet Union itself generates only about 1.6 % of internal seaborne trade in general cargo, but it has a carrying capacity of five and a half times as much. Thus Russian competition has made itself most felt in the liner trades. In a period of only five years, from 1970 to 1975, the USSR doubled its deep sea liner carryings from 4 million to over 8 million tons. In comparison, world seaborne trade grew by only about one third during that period.

The Soviet fleet expansion wave shows no signs of abating yet. According to Russian sources it is planned to add, during the current five year plan which will be completed in 1980, one million deadweight tons to the merchant fleet. Most of this tonnage will be highly specialised roll-on roll-off, Lash and container vessels. These ships are clearly designed to capture a significant share of the lucrative western transport markets, since the nature of Russian exports and imports does not require such sophisticated transport technology.

The rapid growth of the Russian fleet and of its carryings means that somebody has to give way to allow the Russians a larger slice of the cake. The statistics show clearly that US, EEC and Japanese shipping companies have suffered most from Russian competition. In the bilateral liner trades between western and state-trading countries, Russia and its COMECON partners have managed to establish virtual monopolies. There they control up to 95 % of the market. In the cross-trades with third countries their competition methods are hitting the established liner conferences hard. For instance, it is estimated that in the North Atlantic trades USSR ships alone, operating outside the liner conferences, already carry 28 % eastbound and 25 % westbound of the traffic volume carried by the conferences. It is also estimated that COMECON liners have captured about 35 % of the comparable conference cargo transported between Northern Europe and the Mediterranean, 25 % between Northern Europe and the West Coast of South America, over 20 % between Gulf of Mexico ports and the Mediterranean, about

20% in the Europe-East Africa traffic and 12% between Japan and the West Coast of the United States. Add to this that the Transsiberian Railway siphons off about 15% of the East Asia-Europe traffic. What makes the situation even worse is that Soviet vessels are often able to skim off the cream of high-rated traffic and leave western companies with the scraps

Faced with this situation we are tempted to ask: First, what motivated the Soviet Union to step up its activities in merchant shipping so significantly? Second, what makes it so successful? And finally, why should we be concerned about it? I don't think that the first question can simply be answered with a statement like they want to make money, just like everybody else. Certainly, they also want to make money but this objective needs to be seen against the background of the overall economic and other policy objectives of the state. This is what makes a Soviet shipping company so different from a western one: like all other economic activities, the merchant marine is an instrument of the state for achieving its political and overall economic objectives, whereas a western company in fulfilling its transport functions wants, in competition with others, to work as profitably as possible in a private enterprise system. Undoubtedly, the USSR merchant marine fulfils the rôle of a reserve fleet for military transport purposes. This became clear during the Cuba crisis, during the Vietnam war and again during the Angola war. Many of the merchant ships are equipped with electronic and other sophisticated gear, far in excess of normal commercial requirements. Naval officers and crew are known to serve also in the merchant marine and crews are largely interchangeable. I will not say more now about the strategic aspect of this question, since it is not directly a matter for the European Commission. But it clearly needs to be taken into account in any overall assessment of the situation.

Another reason for the Soviet merchant marine build-up was the realisation in the sixties that the USSR depended too much on non-COMECON shipping services for its exports and imports. This was coupled with an awareness that a greater economic link-up was needed with western industrialised countries in order to achieve the ambitious economic objectives laid down in the long-term development plans. So the Soviet merchant marine had and still has to fulfil the double economic function of import substitution - aiming at the transport in Russian or COMECON ships of a major share of the national foreign trade - and of export diversification through the export of shipping services. In Eastern Europe they call it the foreign exchange objective of their merchant marine, and it is viewed as the

primary economic motive of the current phase of fleet expansion.

After all, Soviet foreign trade must expand in order to pay for the rapidly growing imports of Western technology. As you know, a large proportion of Soviet exports consists of raw materials, the production of which is not easily increased and which are particularly sensitive to the ups and downs of the business cycle in Western countries. Therefore, the obvious answer is an increase of finished products and services in order to increase earnings of hard currencies. While in the finished products sector the Russians have not been particularly successful due to problems about meeting western demand and product quality standards, they have been singularly successful in the provision of shipping services. It is difficult to quantify the foreign exchange income of the Soviet fleet, since no official USSR statistics are available on this subject; but western shipping circles estimate Soviet foreign exchange income from shipping at about 600 million dollars in 1976. This is a major contribution to their balance of payments.

What, then, makes the Soviets so successful in merchant shipping? Well, for one thing the Soviets know how to exploit Western economic freedoms for their own ends while denying reciprocal rights to our Western companies. Moreover, Western shipping consists of hundreds of individual, independent companies, all competing with each other and facing on the other side one huge state-supported organisation. Thus, while a western company must be profitable in order to meet its current and replacement costs, a Russian shipping company doesn't have such worries. A large share of the costs which a western company must absorb itself, such as insurance, social overhead costs and depreciation, are covered by the state. And thanks to the absence of hard-bargaining labour unions, Russian seamen are reported to earn about 120 dollars a month, while a western seaman makes five times that much.

In these circumstances it would be naive to expect that somehow our open western economic system would let the more efficient companies survive. On the contrary, the winner in this economic game is <sup>liable to be</sup> already determined before the match has started. The tactics used to ensure dominance of their national trades by state-trading countries and the desired penetration of western cross-trades are simple <sup>in their own terms</sup> but highly effective. In their national trades there is close coordination between the state export/import monopolies and the state shipping companies. Priority is given to shipping Russian foreign trade in Russian ships. Second in line

are the COMECON partners and last the other companies. All this is coordinated by a central freighting bureau with headquarters in Moscow. With developing countries the Russians like to conclude bilateral agreements based on 50 : 50 cargo sharing provisions. A subtler method is used in trades with western countries: there the Russians buy FOB and sell CIF, which gives them complete dominance over the transport part of the transaction. In the economically more important and profitable cross-trades, of course, these methods would not work. Additionally, entry into those markets is more difficult because a good deal of them are served by liner conferences. This is no problem in the relatively loosely-knit/operating to and from the United States, but in other parts of the world it may not be easy to gain, as a newcomer, rights to become a conference member and to participate in its traffic. The Russian solution to the problem is a classic capitalist one. They first operate outside the conference system, heavily undercutting conference rates and also the rates of other western outsiders, in order to gain a share of the market. The undercutting can be general or selective depending on the trade involved. In particular cases Russian quotations are up to 50% below comparable western freight rates, on the average they are about 15 to 20% below. I mentioned already that they also like to skim off the high-paying cargoes and leave the rest to the conferences. Once a firm position is established in a specific trade, conferences are accepted as a price-leader which Russian shipping companies follow closely by maintaining a certain percentage differential. Since Soviet shipping companies can easily match all possible commercial defence measures of the liner conferences simply by quoting even lower tariffs, it is evident that western shipping companies can hardly fight back at commercial level. In some trades, such as the Europe-East African or Europe-North American trades, the Russians are not only a threat to the conference system but they are also slowly eroding the economic health of our shipping companies. The situation is bound to become worse once all the specialised tonnage now being built is seeking employment in the international trades.

From the point of view of the western shipper - as opposed to shipowner - it could, of course, be argued that competition helps keep freight rates down and provides the shipper with a genuine alternative means of transport. The phenomenal success of the Russians shows that many shippers must take that attitude, at least in the short term. But shippers are clearly as concerned as shipowners about the long term implications of Russian competition. This was demonstrated during a joint conference

of European shippers' councils and shipowners held in Switzerland last year, when a joint declaration was issued warning that continued COMECON penetration of western trades could result in the long run in destruction of the conference system, serious deterioration in the quality of shipping services, and restriction of freedom of choice among alternative shipping services.

This is already part of the answer to the third question I posed at the beginning: why should we be concerned about this build up of Russian shipping competition? There are other reasons too. Obviously the huge Soviet merchant fleet can become a security risk for the West in times of instability anywhere in the world. Paradoxically, this fleet is nourished by our own international trade. Moreover, an ever-growing Russian fleet which is completely removed from our influence threatens the economic health of our shipping companies and can make international seaborne trade more and more dependant on non-western shipping services. This would bring us into undesirable economic dependency and would make us very vulnerable to economic pressures.

In spite of these dangers the countries of the European Economic Community still have a long way to go towards defining and agreeing on a coordinated and coherent set of objectives against which to judge where action may be necessary in the face of Soviet and other COMECON country participation in our international trade. There has been a tendency to think that these countries would somehow behave according to our rules of the game if only we held on to them tenaciously. But I think it will be necessary for us to establish vis-à-vis the state trading countries a new set of rules of the game taking into account their economic system and not ignoring it.

First steps have already been taken. Some of the Member States of the Community most hit by Soviet competition have tried to negotiate satisfactory arrangements bilaterally. This approach is still being pursued, but experience so far has been disappointing. This is not very surprising, because the Russians suspect that a single country would have difficulty in implementing unilateral defensive measures for fear of losing trade and traffic to its neighbours. This is no doubt the basic reason why the counter measures powers which exist in almost every Member State of the Community have never yet been applied to them. Of course, the Russians are aware of this weakness of European countries. Ministers from Community countries have returned from visits to Moscow with the clear impression that the Russians believe the West lacks the resolve to apply sanctions in its own defence.

Faced with this situation, the Council of Ministers of the Community has decided that a serious examination must now be made of the scope for taking action not only at national but also at Community level, and in association where possible with other like-minded countries. In response to a request by the Council of Ministers the Commission's services prepared last autumn a working paper on shipping competition by East European state-trading countries, which analyzed the situation and its implications and reviewed alternatives for common action at Community level. The options considered include:

- A Community message to Eastern bloc countries spelling out EEC concern and suggested principles for the orderly development of maritime trade;
- Imposition of FOB terms of shipment on Community imports;
- Limitations on the right of establishment of Eastern bloc shipping agencies in Community Member States;
- Imposition of a levy on the freight rate charged on imports discharged by Eastern bloc shipping companies operating outside conferences;
- Regulation of Eastern bloc freight rates;
- Introduction of quota restrictions on sailings and landings of cargo;
- Coordination of the application of Member States' counter-measure powers.

The Commission's services' paper was intended to provide a basis for discussion in the framework of the Council of Ministers; The Commission did not pronounce itself firmly in favour of any of the options reviewed. The Commission must first discuss this complex problem further with the Member States and in doing so the possible implications of a common defensive strategy in shipping on trade and foreign policy must be carefully assessed.



The Council of Ministers had already reacted favourably to the Commission's services' report and asked it to present to the Council concrete proposals for action by spring 1978. At present we are working on these. I want to emphasize, however, that neither the Commission nor the Member States want to provoke a confrontation with the Soviet Union or its fellow COMECON members, nor do we want to exclude them from our trades. All we want is to put our defences in order and to coordinate them while still expecting that negotiations will ultimately lead to a solution of our problems. But we want to negotiate from a position of strength, and in establishing this position it seems to me that the Community has an important part to play.