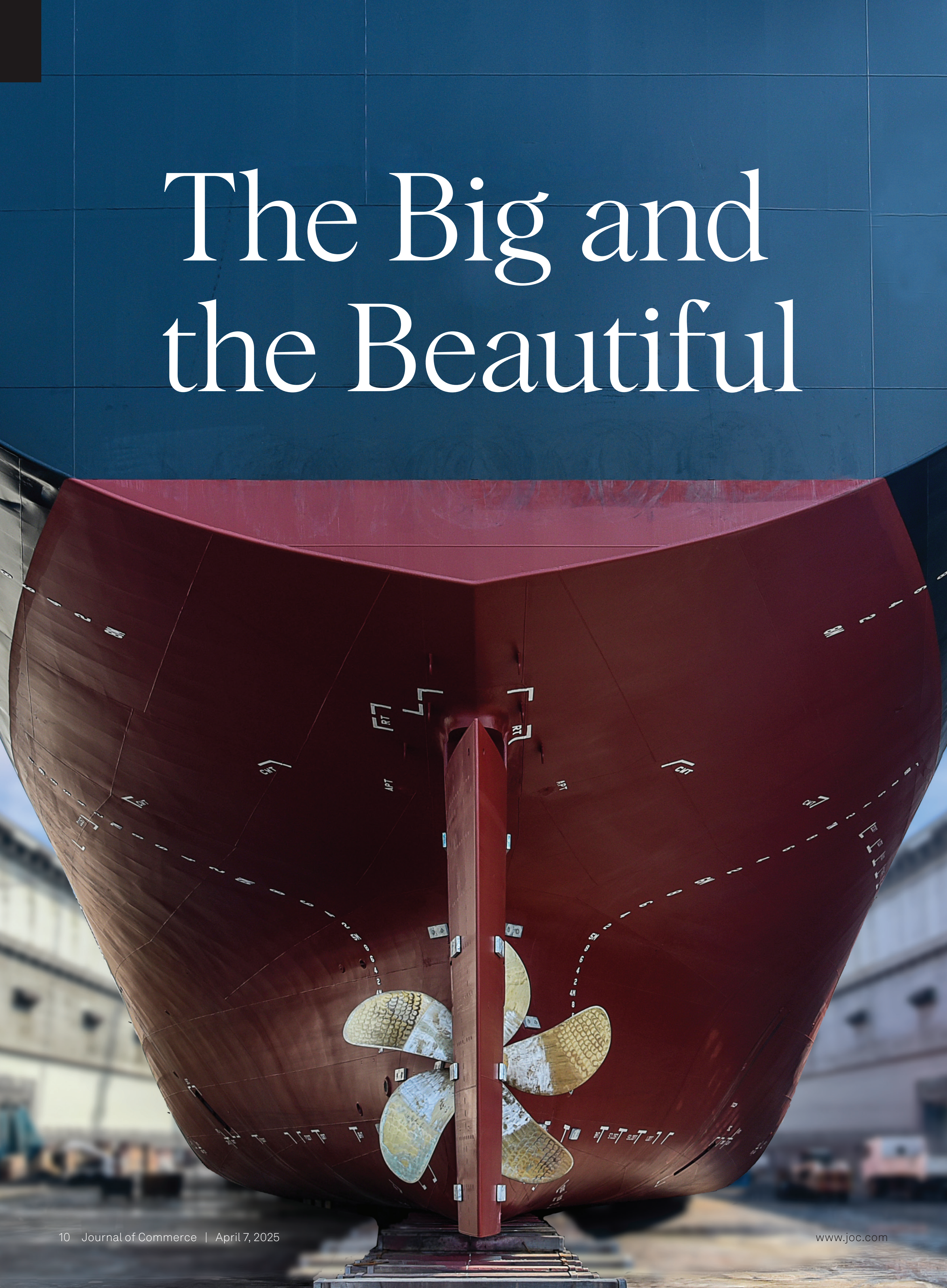
The Big and the Beautiful



Trump's plan to restore US shipbuilding would upend supply chains

By Michael Angell and Greg Knowler

The sheer ambition of US President Donald Trump's plan to restore domestic shipbuilding to its 1940s heyday is, to borrow a phrase from the president, "huge."

Whether policy changes enacted by the Trump administration will be enough to make his vision of "bringing this industry home to America" a reality after the US intentionally ceded those capabilities during post-World War II reconstruction is an open question. But according to industry stakeholders, the short-term implications are clear.

Container lines, cargo owners, port authorities, railroads and industry analysts alike say a proposed set of port fees targeting vessels built in China of up to $1.5 million per call would force carriers to cut calls to smaller US ports — or exit certain US trades — and drastically increase the cost of moving goods in and out of the country.

"A lot of the marginal ports — the peripheral ports — will be at risk."

"In California today, we typically call at Long Beach then proceed to Oakland, but we can't proceed to Oakland if that costs us another $1 million," Soren Toft, CEO of Mediterranean Shipping Co. (MSC) and chair of the World Shipping Council (WSC) board, said during the *Journal of Commerce*'s TPM25 conference in early March. "A lot of the marginal ports — the peripheral ports — will be at risk, and we will have to adapt our services."

At least one carrier said the fees, if enacted as proposed, would push it out of the US market entirely.

"ACL would be forced to terminate its US service, close its American offices, lay off its American staff and redeploy its ships to non-US trades, because the proposed action would render us totally uncompetitive versus the other carriers in the US trades," Andrew Abbott, president and CEO of Atlantic Container Line (ACL), a subsidiary of Italy's Grimaldi Group based in New Jersey, wrote in a public comment to the USTR. "US manufacturers would lose their only USA-headquartered North Atlantic carrier."

The resulting consolidation of calls would reduce service and raise costs for shippers, particularly exporters; pose an existential threat to smaller ports, thereby threatening hundreds of longshore jobs; and create bottlenecks at major load-centers and in inland rail networks.

In addition, carriers would divert some US-bound cargo to gateways in Mexico and Canada, resulting in "increased truck and rail traffic," "less work for American longshoremen," "less capital available for infrastructure" and "higher costs for consumers," Cary Davis, president and CEO of the American Association of Port Authorities (AAPA), said in a written comment. "If American ports are to compete well in the North American market and around the globe, we cannot make it more expensive to do business at American ports."

Executives from US Class I railroads CSX Transportation and Union Pacific, speaking at the J.P. Morgan Industrials Conference on March 11, said intermodal rail networks could accommodate carriers consolidating US calls at larger load-center ports, but it would not come without "significant" disruption.

"This potential port fee that could come into play would have a significant disruptive impact," CSX CFO Sean Pelkey told the event. "If there's more consolidation at ports that we serve and there's more volume that wants to come into those ports, that's a good thing. We can be a part of the solution for that. But it could also result in more congestion as well, which could have significant disruptive effects."

On the hook

The proposals, which stem from an investigation conducted by the USTR under President Joe Biden, include a $1 million port entrance fee for each US port call by a ship operated by a Chinese carrier. For all other carriers, the USTR proposed a sliding fee of up to $1.5 million per Chinese-built vessel based on the percentage of the carrier's fleet built in China. An additional fee of $1 million per vessel could also be assessed based on the amount of newbuild tonnage a carrier has on order at Chinese shipyards.

Stakeholders across the board warned that carriers would pass those additional costs on to cargo owners in the form of additional surcharges, and shippers would likely pass them on to consumers via higher pricing.

"The ships already built of Chinese origin will not disappear from the world fleet if the proposed port fees are introduced," Lars Robert Pedersen, deputy secretary general and director of regulatory affairs at shipowner association BIMCO, wrote in a public comment on the USTR docket. "Rather, the shipping industry will seek to avoid paying [the] fees."

US anti-trust law prohibits ocean carriers from conferencing when setting rates and surcharges. Instead, container lines would publish fees individually and the market would eventually settle into a standard range, much like during the rollout of international low-sulfur fuel regulations in 2020.

"If this moves forward in any way, shape or form, especially as it's currently proposed, it will be a cost that will not just be absorbed by the owner-operator," Ashley Craig, chair of the international trade and logistics group at law firm Venable, told the TPM25 audience. "It will be passed down. Believe me, ultimately, a consumer will be paying it."

Maritime consultant Drewry estimates 80% of container ships calling the US would be subject to the fees, but the cost impact — and, in theory, carrier surcharges — would vary by trade lane.

According to Toft, a typical Asia–US East Coast service with four US calls carries about 10,000 TEUs per voyage. If those ships incur $4 million in USTR port fees, that equates to an additional $400 per TEU in operating costs.

In the trans-Atlantic, vessels move roughly 4,000 TEUs through four ports, translating to an additional cost of $1,000 per TEU, "which more or less eliminates the freight rate," Toft said. "The trans-Atlantic will be uneconomical if we can't pass on the costs."

Still, questions remain as to when the proposal would be implemented, as well as how the fees would be calculated and collected.

"There's some interpretation of this thing that still needs to be done," Peter Friedmann, executive director of the Agriculture Transportation Coalition (AgTC), said during TPM25. "For example, if you're not a Chinese company, and you are not bringing a Chinese-built ship here, but you have some Chinese ships in your fleet operating somewhere else, are you also subject to the penalty for that non-Chinese-built ship coming in? These are things that aren't clear now, so they're not ready to implement."

Missing the mark?

According to the Trump administration, the proposed fees — along with federal legislation known as the SHIPS Act and other measures soon to be announced — aim to revitalize the US shipbuilding industry and merchant marine fleet, both of which have been in decline for the better part of 80 years.

Having built a dominant maritime fleet in the lead up to World War II, the US divested more than 1,000 vessels to its allies via the Merchant Ships Sales Act of 1946 to accelerate post-war reconstruction by facilitating and lowering the cost

Got ports?

Hutchison deal reveals carriers' thirst for terminal assets

By Peter Tirschwell

Container lines going back to Sea-Land Service Inc. have seen value in controlling marine terminals, but the advantages — and the competition to acquire key facilities — are intensifying in line with growing port congestion, finite port capacity and the growing dominance of a top tier of mega carriers.

Securing port access and the efficiencies it brings, while allowing competitors to be blocked out, was the major victory that Mediterranean Shipping Co. (MSC) achieved by participating via its terminal operating unit in the $23 billion deal with BlackRock to acquire the non-China assets of Hong Kong-based conglomerate CK Hutchison's terminal portfolio.

The acquisition itself could be in jeopardy due to opposition in Beijing, but the reasoning behind the attempt is no less revealing. For its part, the Chinese government is concerned that the sale of the Hutchison's terminals in Panama would allow the Panama Canal to be "Americanized" and "politicized," with the US using the canal for "political purposes and pursuit of its own political agenda," according to commentary published March 13 in the China state-backed Hong Kong newspaper *Ta Kung Pao*.

For large carriers like MSC, the ability to align their growing share of the global market — forged through consolidation and organic growth — with capacity at the ports has become a significant competitive differentiator.

"The aspiration of major carriers and alliances today is the ability to control their own destiny with regard to port and terminal operating capability," said Peter Levesque, advanced leadership fellow at Harvard University who has led terminal operating businesses, including Modern Terminals and Ports America.

"This deal with Blackrock speaks volumes as to what MSC looks to achieve."

If the deal is completed, MSC, through its Terminal Investment Limited (TiL) unit, will gain access to terminals at 43 ports in 23 countries totaling 199 berths — although some of those terminals may be divested pursuant to antitrust review in Europe — making it the world's largest terminal operator.

"The fact that TiL is involved in this deal with BlackRock speaks volumes as to what MSC looks to achieve in global terminal operating capability and competitive advantage," Levesque said.

The competition among carriers for prized port assets is evident on multiple fronts. Hapag-Lloyd last year announced the creation of a terminal operating unit, reflecting its commitment to "expansive terminal operations," and on March 10 announced the acquisition of a majority stake in a Le Havre terminal operator. Maersk, CMA CGM and Ocean Network Express have also been growing their respective terminal portfolios.

"There is a tendency for each shipping line now to build their own terminal portfolio," said Robbert van Trooijen, head of consultancy Inception Partners LLC Inc. and the former Maersk head of Asia-Pacific and Latin America.

Carriers are growing increasingly aggressive in pursuit of ports. In its winning bid to acquire Global Container Terminal facilities at Bayonne and Staten Island, CMA CGM agreed to the surprise terms of sharing detention and demurrage revenue with the Port Authority of New York and New Jersey, and to helping fund quayside improvements.

CK Hutchison said the TiL/BlackRock deal resulted from a "competitive process in which numerous bids and expressions of interest were received," which reportedly included other carriers.

Driven by capacity constraints

Carriers' urgency in acquiring terminals reflects concerns about growing port

ambient_pix / Shutterstock.com

of international trade. Under the Economic Recovery Act of 1948, now known as the Marshall Plan, the Congress appropriated $13.3 billion for European recovery, some of which went toward rebuilding shipyards in Europe and Japan.

In the 1980s, the US government terminated subsidies for domestic shipbuilding and began construction of 600 Navy warships, which supplanted commercial vessels in domestic yards.

"We lost our way," Trump told reporters on March 6. "For many years we didn't do anything. We used to build a ship a day," he said, adding that he would unveil the details of a larger US shipbuilding program in the coming weeks.

Those comments came during an Oval Office meeting with CMA CGM Group Chairman and CEO Rodolphe Saadé, who announced the Marseille-based carrier will

Claudine Van Massenhove / Shutterstock.com

congestion globally combined with limited greenfield port projects.

"Globally, terminal capacity is under significant constraint. Globally, port congestion is growing," said van Trooijen. "There is a lack of greenfield projects out there that will deliver expansion, so getting your hands on existing capacity, and especially a portfolio of this size, was a once-in-a-decade opportunity."

The ratio of a ship's time at sea versus time in port has grown from 80-20 to 70-30 in recent years, said Johnson Leung of Linerlytica. China in recent years has stopped building port capacity ahead of demand as it did for many years, leading to growing congestion at Shanghai and Ningbo.

Controlling terminals enables carriers to control costs at the terminal, tightly coordinate port calls and ensure its ships are guaranteed priority on arrival and departure. Control of hub ports is deemed the essential ingredient in delivering the 90%-plus schedule reliability promised by the hub-and-spoke Gemini alliance.

"Controlling key port infrastructure provides carriers with cost and operating efficiencies that are difficult to achieve with non-carrier-affiliated terminals and government port authorities," Levesque said.

The growing dominance of the top tier of carriers, where MSC crossed the 20% market share threshold and the top five carriers control 65% of capacity, according to Alphaliner, is forcing third-party terminal businesses to align with key carriers able to provide the volume needed to keep terminals profitable.

"For a big terminal operator, you increasingly need to have a long-term relationship with carriers with whom you have more than average cooperation if you want to safeguard your future for the long term," van Trooijen said. "Terminal operators who are successful are the ones who have developed long-term carrier relationships."

Special Correspondent Keith Wallis contributed to this report.

email: peter.tirschwell@spglobal.com

An estimated 80% of container ships calling the US would be subject to the proposed USTR port fees.
ambient_pix / Shutterstock.com

invest $20 billion in the US maritime sector over the next four years, including expanding its US-flag fleet and increasing capacity at key US ports.

However, AAPA's Davis and others say the scale of investment needed for US shipyards to compete with shipbuilders overseas will be prohibitive.

"The American shipbuilding industry … needs major infusions of capital, workforce talent and innovation to begin competing with shipbuilders abroad," Davis wrote. "A fee on foreign vessels will simply not bring back American shipbuilding."

> "It's a vision we'd love to see of making 'big, beautiful ships' and so forth, but we don't have the capacity."

The National Retail Federation (NRF), in a response last year to the Biden administration's investigation of China, said USTR would have to impose a fee of $5 million per port call to offset the estimated $50 billion cost of adding necessary US shipyard capacity.

ACL's Abbott said even if carriers were to stop ordering vessels from China, US yards would continue to be undercut by shipbuilders in other countries.

"Chinese shipyards do indeed offer much cheaper prices than American shipyards today, but so do the shipyards of virtually every other country around the globe," Abbott wrote. "None of this turmoil inflicted on American exporters and importers would help the American shipbuilding industry. It would only reshuffle the cards, with Korea, Japan and Taiwan grabbing the new vessel orders instead of China."

Ordering a newbuild 3,600-TEU container ship from a shipyard in Korea would cost roughly $50 million at today's prices, compared with around $333 million from a US yard, according to BIMCO.

"It's a vision we'd love to see of making 'big, beautiful ships' and so forth, but we don't have the capacity to do it," Friedmann said. "And I think, eventually, [Trump] will have to back off."

Friedmann further noted that the USTR could still adjust the fee proposal based on public comments and pressure from longshore unions, given that Trump has already shown a willingness to intervene in contract talks on behalf of longshore labor. At the time of writing, the International Longshoremen's Association (ILA) and International Longshore and Warehouse Union (ILWU) had yet to comment publicly on the proposal, despite widespread speculation that they would oppose the fees due to the potential impacts to dockworker employment.

"A lot of companies are thinking this will never happen, [that] it'll just fall of its own weight," Friedmann said. "I think everybody in the trade community has got to convince the ILA and ILWU: regardless of what these other unions say, you need to protect your own jobs."

email: michael.angell@spglobal.com
email: greg.knowler@spglobal.com