

Hong Kong Liner Shipping Association

**Response to Hong Kong Competition Commission's Public Consultation
under Section 16 of the Competition Ordinance**

Case Number: BE/0004

NON-CONFIDENTIAL VERSION

14.12.2016

1. Executive Summary

- 1.1 The Statement of Preliminary Views of the Competition Commission (the “**Commission**”) dated 14 September 2016 (the “**Statement**”) proposes, on a preliminary basis, to issue a block exemption order for vessel sharing agreements (“**VSA**s”), subject to certain limitations, but excludes voluntary discussion agreements (“**VDA**s”) from the scope of that order.
- 1.2 The Hong Kong Liner Shipping Association (“**HKLSA**”) welcomes the Commission’s preliminary proposal that a block exemption order be issued in respect of VSAs. In this submission, HKLSA provides additional substantive information and evidence (where available), in support of the Commission’s preliminary view on VSAs, to demonstrate further how the VSA activities suggested to be exempted by the Commission’s proposed block exemption order (the “**Proposed Order**”) meet the conditions in section 1 of Schedule 1 to the Ordinance (the “**Efficiencies Exclusion**”). HKLSA also outlines its views on the proposed conditions (the “**Conditions**”) included in the Proposed Order, including the proposed market share limit.
- 1.3 As regards VDAs, HKLSA is disappointed to see that the Commission has not recognised the significant efficiencies VDAs bring to the market in Hong Kong and has adopted a narrow interpretation of the exemption standards pertaining to “*improving production or distribution*” and “*promoting technical or economic progress*”. HKLSA’s original application for a block exemption order (the “**Application**”) contained substantial support for the position that VDAs meet the standards for an exemption on a reasonable reading of the criteria. Specifically, HKLSA showed with supporting data that VDAs promote competition by supporting market stability, with benefits to carriers’ customers, Hong Kong consumers and the wider Hong Kong economy. The Commission risks applying the Ordinance in a manner that hampers, rather than promotes, competition in Hong Kong and HKLSA firmly believes the Commission should re-evaluate its analysis with respect to VDAs.
- 1.4 To assist the Commission in its consideration of VDAs, HKLSA provides additional arguments and data in this response to explain further how VDAs meet the Efficiencies Exclusion to the Competition Ordinance (Cap. 619) (the “**Ordinance**”) for a block exemption order under section 15 of the Ordinance.
- 1.5 In summary, this response covers:
 - (A) certain introductory remarks and an outline of the particular relevance and significance of the Application in light of the importance of international ocean shipping to Hong Kong and the prominent Government policy to position Hong Kong strategically within the One Belt One Road (“**OBOR**”) initiative of the People’s Republic of China (the “**PRC**”);
 - (B) additional data regarding the efficiencies associated with VSAs to assist the Commission in reaching a final decision to grant a block exemption order for VSAs, as well as HKLSA’s views on the Commission’s proposed Conditions;

- (C) detailed explanation regarding why the Efficiencies Exclusion should allow for the recognition of broad efficiencies arising from VDAs in promoting Hong Kong: (i) as an international maritime centre and “super-connector” with an impact on the broader Hong Kong economy; and (ii) as a transshipment hub, with benefits to all consumers, rather than just shipper customers of carriers, as well as further information and submissions on previously described efficiencies; and
- (D) why the Commission should not place an unduly pronounced emphasis on surcharges in its review of the Application, given their limited relevance to VDAs.

2. Introductory remarks

- 2.1 HKLSA begins with a few general observations with respect to the Commission’s Statement and initial position on VDAs.

Transparency and procedure

- 2.2 The Commission mentions in the Statement that it has consulted an industry expert to obtain and verify certain information in relation to the liner shipping industry, yet it gives no details as to the identity of this “industry expert”, nor does it outline the specific information obtained, nor give HKLSA (as the applicant) the opportunity to validate such information. HKLSA submits that the Commission’s explanation of this third party is insufficient to give confidence that the Commission has been correctly advised in coming to its preliminary conclusions. HKLSA has not been made aware of any evidence or data that has refuted the detailed conclusions of HKLSA’s own economic and industry expert, Drewry Maritime Consultants (“**Drewry**”), who provided comprehensive and substantiated data in support of the Application.
- 2.3 In the interests of procedural fairness, transparency and factual and legal accuracy, the Commission should publish the information it has obtained from the “industry expert” and identify which particular elements it has relied upon in coming to its preliminary conclusions. HKLSA as the applicant and all other interested parties should be given an opportunity to review, comment and, if necessary, rebut such published information.

Data submissions point to VDA efficiencies

- 2.4 HKLSA provided the Commission with various data and information in the Application to support its request for a block exemption order for VDAs. That data and information demonstrated why VDAs meet the criteria under the Efficiencies Exclusion.
- 2.5 Data submitted thus far has included, among other things: copies of VDAs, market research and trade press articles, as well as consultancy reports from well-known sources such as the World Bank, United Nations Conference on Trade and

Development and Alphaliner. It has also included historical data on rate trends in major shipping trades and current rate data from sources like the China Containerized Freight Index and Drewry demonstrating that rates in the Hong Kong trades, even with the presence of VDAs, were not only not artificially high, but in fact have been declining for several years and currently sit at all-time lows. [...]

2.6 [...]

2.7 To this point, HKLSA notes that in response to all of the data and information it provided, it is not aware of any evidence or contrary data that was presented to the Commission (either by its own industry expert or another third party) that has contradicted any of the data which HKLSA has provided. Whilst the Commission has proposed certain theoretical possibilities, HKLSA is not aware of any data substantiating: the Commission's theory that VDAs might "*give rise to the possibility of higher rates compared to the situation where carriers make pricing decisions independently of each other*"¹ in any trade; that factors other than VDAs contributed to the negative results in the EU; or that VDAs in any way disadvantaged Hong Kong shippers or consumers generally. In short, based on explanations in the Statement, all of the available data and evidence (as opposed to hypotheses) in this case shows that VDAs promote efficiencies and meet the criteria for an exemption.

Not granting a block exemption order for VDAs will not enhance competition in Hong Kong, but rather will risk damaging it

2.8 [...] ² VDAs have served the Hong Kong trades for decades. In that time, Hong Kong has become one of the leading international maritime centres and key transshipment hubs in Asia. Hong Kong importers and exporters have over the years had access to numerous competitive carrier options, numerous services, and extremely competitive pricing.

2.9 In short, the *status quo* in Hong Kong with VDAs has been a highly-competitive environment that has yielded many benefits to shippers. The Commission has not given sufficient consideration in the Statement to: (i) how competitive the current environment is today with VDAs; and (ii) the overall risk to the Hong Kong port, the Hong Kong economy, Hong Kong importers and exporters and Hong Kong consumers if it ultimately decides to disrupt this *status quo* by declining to provide a block exemption order covering VDAs.

2.10 As the Commission is aware, the liner shipping industry has continued to suffer huge economic losses since the submission of the Application. Most notably, in September of this year, South Korea's Hanjin Shipping Co., one of the world's largest container shipping companies, filed for bankruptcy. Hanjin operated approximately 140 container and bulk vessels worldwide and transported over 100 million tons of cargo per year. Hanjin's collapse was by far the largest container shipping bankruptcy in history.

¹ Paragraph 4.82

² [...]

- 2.11 In addition to Hanjin's bankruptcy, there have been several mergers and acquisitions. Most notably, in the past year: the third largest carrier in the world, CMA CGM, acquired APL; COSCO acquired China Shipping; Hapag-Lloyd announced its plan to acquire United Arab Shipping Company; and on 1 December 2016, Maersk Line announced that it had reached an agreement to buy Hamburg Süd. Finally, three Japanese carriers (NYK Line, K-Line, and MOL) recently announced that they would merge their container shipping businesses. That announcement was made on the same day that these carriers recorded a collective half-year operating loss of US\$484 million.
- 2.12 All of these developments demonstrate that there is highly effective competition between carriers operating on tight margins in a difficult environment. VDAs help to moderate the extremes of fluctuations in rates without preventing consumers and customers benefitting from that competition. If the Commission declines to grant a block exemption order for VDAs, this would accelerate the negative market conditions that the industry is already experiencing today and reduce carriers' ability to continue serving the Hong Kong trades.
- 2.13 It is against this backdrop that HKLSA urges the Commission to give due consideration to the benefits brought by VDAs to the broader Hong Kong economy and all consumers, not just shipper customers of carriers.

3. Importance of the Application for the maritime industry in Hong Kong

- 3.1 To put the Application in context, the importance of the maritime industry and the port of Hong Kong to the wider Hong Kong economy is undisputed. Shipping, terminal operations, professional services, marine engineering and other support services all form part of the maritime sector. A recent consultancy study by BMT Asia Pacific reports that, in terms of direct economic contribution, the maritime sector contributed approximately 2.1% of Hong Kong's GDP in 2010, with approximately 57,000 people engaged, or 1.6% of total employees.³ This does not yet take into account the indirect benefits of the maritime sector, including, for example, its vital support to trading and logistics activities. In fact, the Hong Kong Government is fully aware of the positive impact of the maritime industry – one of its goals is for Hong Kong to become an international maritime services hub for China and the Asia-Pacific region.⁴
- 3.2 Given Hong Kong's international status and its potential as a super-connector transshipment hub, Hong Kong can aim to be the maritime centre for the OBOR initiative, allowing Hong Kong to attract shipping players and other stakeholders, for example, banks, insurers, lawyers, retailers, consumers. These are key ingredients if Hong Kong is to establish a strong international maritime centre, but before Hong Kong can compete successfully against regional competitors for this role, it requires a business-friendly regulatory environment for shipping that is consistent with the wider region.

³ BMT Asia Pacific, Consultancy Study on Enhancing Hong Kong's Position as an International Maritime Centre, April 2014

⁴ See 2015 Policy Address of the Chief Executive.

- 3.3 At the OBOR summits and conferences held throughout this year, delegates have considered how Hong Kong can place itself at the heart of the initiative. Consistent with this objective, at the first meeting of the Hong Kong Maritime & Port Board (“HKMPB”) on 6 May 2016, the Chairman of the HKMPB and Secretary for Transport and Housing, Professor Anthony Cheung Bing-leung, emphasised the Government’s commitment to growing Hong Kong’s maritime services and maintaining the competitiveness of the Hong Kong port, stating that the Government: *“attaches great importance to the development of the maritime and port industries”*; *“will work closely with the trade to create a maritime business-friendly environment”*; and *“will implement measures as necessary to spur the growth of Hong Kong’s maritime cluster and to create a business-friendly environment for the maritime industry”*.⁵
- 3.4 If the Government is to achieve its aims of building a new type of maritime super-connector centre and fostering a business-friendly environment for the maritime industry, legal certainty as to the regulation of both VSAs and VDAs will be crucial. VSAs and VDAs are inter-linked; they both play a critical role in promoting Hong Kong as a transshipment hub and can allow Hong Kong to play a defining role in the OBOR initiative. Both types of agreements are critical to carriers, their customers and the Hong Kong economy. A block exemption order covering both will be required to help Hong Kong establish its competitiveness in the international context.
- 3.5 In particular, the use of VDAs is crucial for Hong Kong to achieve the wider goal of the HKMPB and Government to: *“promote professional services towards high-end and high value-added development”*; *“spur the growth of Hong Kong’s maritime cluster”*; *“nurture new blood and build up a talent pool”*; and *“step up efforts to promote Hong Kong’s role as a ‘super-connector’ in overseas and Mainland markets”*.⁶
- 3.6 The Government’s ambition to boost Hong Kong’s status as a leading global maritime centre by focusing on high value-added shipping services, with a resulting benefit to the Hong Kong economy, employment and consumers, cannot be fulfilled without the information exchange that is only achieved through VDAs. As noted by the Acting Chief Executive of Hong Kong, Mrs Carrie Lam, at the Asian Logistics and Maritime Conference on 22 November, 2016, Government is:
- “keen to maintain [...] competitiveness in the logistics and maritime sectors - by promoting high value-added maritime services... ..over 700 companies are already offering a variety of maritime services - from ship management, ship broking and chartering, registration, finance, maritime insurance, to maritime law and arbitration.”*⁷
- 3.7 If VDAs were not covered by the Commission’s block exemption order, this would seriously threaten Hong Kong’s opportunity to become a strong international maritime centre. The two types of liner shipping agreements covered by the Application offer different efficiencies; VSAs provide a framework for operational cooperation and

⁵ <http://www.hkmpb.gov.hk/en/pressreleases/20160506.html>

⁶ Ibid.

⁷ <http://www.info.gov.hk/gia/general/201611/22/P2016112200289.htm>

VDAs provide a framework for market-related communication. They are complementary and both are needed to push forward the Government's agenda.

- 3.8 As the Commission noted in the Statement, VSAs and VDAs are permitted by the legal regimes in a number of jurisdictions, including countries with competing ports along the trade routes covered by the OBOR initiative. Shenzhen, for example, allows VDAs and VSAs covering relevant trades, as does Taiwan, South Korea and Singapore etc. As was noted in the recent HKMPB meeting, Hong Kong is "*faced with keen competition from other major ports in the region*".⁸ In order to compete effectively against regional rivals for a position in the OBOR initiative, the port of Hong Kong will need to draw on the experience and efficiencies that VDAs and VSAs bring to Hong Kong as a transshipment hub.
- 3.9 So long as carriers are able to continue to use VSAs and VDAs, a strong shipping industry can form the lynchpin of Hong Kong's strategy. As explained in the Application, the two forms of liner shipping agreements complement each other so that VSAs allow the efficient allocation of resources and deployment of assets by carriers and VDAs enable the exchange of perspectives and ideas, as well as the collation of industry data and development of market recommendations, which are so integral to building a strong maritime centre of excellence in Hong Kong.

4. VSAs

- 4.1 HKLSA is pleased to see that the Commission has recognised the efficiencies associated with VSAs and proposes to grant a block exemption order to exempt VSAs from the application of the First Conduct Rule. An exemption in Hong Kong would be consistent with the rest of the world's treatment of VSAs, including the EU. HKLSA is not aware of any country in the world that does not permit VSAs to operate in their trades. As a result of that and of the undisputed efficiencies created by VSAs, virtually every major ocean carrier currently operates through VSAs in the world's major trade lanes.
- 4.2 In its Statement, the Commission has accepted that there are economic benefits associated with VSAs, whilst identifying certain areas where further information would assist it in reaching a final decision. While HKLSA believes that ample data has already been presented in its Application to allow the Commission to finalise its preliminary decision regarding VSAs, HKLSA nonetheless provides below the additional data it has collected regarding the efficiencies associated with VSAs, which should assist the Commission in reaching a final decision to grant a block exemption order for VSAs.
- 4.3 In addition, HKLSA outlines below its views on the Commission's proposed Conditions, including why it believes that the proposed market share limit is unhelpful and should, at the very least, be raised from 40%.

⁸ Ibid.

Additional empirical evidence

- 4.4 HKLSA provides below additional empirical evidence to assist the Commission in reaching a final decision that the relevant VSA activities meet the conditions of the Efficiencies Exclusion, demonstrating with additional data: the expanded service options and frequencies available through VSAs; the cost savings available through VSAs; and how VSAs enable smaller carriers to compete. HKLSA also provides supporting arguments and third-party commentary on these and other efficiencies.

Expanded service options and frequencies

- 4.5 In relation to the efficiency of expanded service options and frequencies associated with VSAs, HKLSA provides the Commission with further empirical evidence demonstrating that VSAs allow carriers to obtain access to offer a wider range of services to their customers than would otherwise be the case. HKLSA provides at confidential Annex 1 average figures for the proportion of a carrier's cargo on particular trades or routes which are carried on the vessels of other VSA members. These averages are calculated from data taken from [...] carriers.
- 4.6 As can be seen from Annex 1, the proportion is significant, with an overall average of approximately [...]%. This demonstrates clearly that a carrier's scope of offering is greatly expanded through VSAs in practice. In a hypothetical scenario where there were no VSAs in place (i.e. the counterfactual), it would not be possible for a carrier's cargo to be carried on another carrier's vessel, which in turn would lead to each carrier offering a much reduced service to its customers. In such a situation, an individual carrier would have to keep its cargo on the dock until the next arrival of one of its own vessels heading for the required destination. This would have negative consequences for customers, who would not be able to benefit from more frequent sailings. This would also make it more difficult for the smaller carriers in particular to compete in the market, as some customers (such as those needing to transport perishable goods) will need their cargo to be transported as quickly as possible.
- 4.7 It is not possible to provide an actual counterfactual example to demonstrate exactly what would happen if carriers could not take advantage of VSAs, since VSAs are so ubiquitous in the shipping industry that there are no existing counterfactual examples. As noted in the Application, [...]% of capacity in the Europe to Far East trade is carried through VSAs, and [...]% of the capacity in the Transpacific trade is carried through VSAs as of 2015. Without VSAs, only a few very large carriers would be able to survive, which is why VSAs are so prevalent in all trades.
- 4.8 However, as a purely hypothetical illustration, if a carrier were not part of a VSA and was forced to carry cargo only on its own ships, there would be a number of negative results. That carrier would be forced to reduce the number of total ports called, particularly eliminating many smaller ports from its service. Even the number of port calls to major ports would be reduced, if not eliminated in some cases. The services that remained would also be less frequent. For Hong Kong, the number of services

between it and other countries would be reduced drastically, which would further diminish Hong Kong as a major international port.

4.9 To illustrate this through an example, if two lines of equivalent size were party to a typical VSA in which they each contributed 50% capacity and called at the exact same ports, and they were then to terminate that agreement such that they no longer shared capacity on each other's vessels, there would be a number of likely knock-on effects to the service they would be able to offer customers:

- (A) The frequency of their vessel calls would likely be reduced;
- (B) The number of destinations they offered would likely be reduced;
- (C) They would each be less easily able to fill larger and more efficient vessels, leading to increased shipping costs per TEU, possibly rendering the continued provision of that service uneconomical/loss-making; and
- (D) From an environment perspective, the use of smaller vessels would be more harmful to the environment. Larger vessels are reported to produce fewer emissions per TEU of cargo transported.⁹

4.10 The same principles apply in relation to the Commission's request for empirical evidence showing the extent to which VSAs have allowed carriers as a whole to offer a broader overall service coverage and higher frequencies to customers (rather than from the perspective of an individual carrier only). The same dynamic, which permits a specific carrier to increase its offering, also works in the broad and applies across the whole industry when multiple carriers are involved. It therefore follows that VSAs increase the overall number of options (in terms of both destinations and frequencies) available to customers.

4.11 We provide below a hypothetical scenario to demonstrate the increased choice that VSA are able to offer to customers in Hong Kong. Taking two carriers, Carriers A and B, each of which operates a weekly service to a trade servicing the same 10 ports. By combining the vessels of Carriers A and B in a VSA, a twice weekly service can be offered to all 10 ports and/or (as is often the case) the lines might operate the two services with slightly different schedules, so that one unique port is offered on each string, for example, it would be reasonable to expect a potential outcome along the lines of eight ports receiving a twice-weekly service, and four lower volume "niche ports" receiving a weekly service, widening the "reach" of the overall network by adding two additional ports to the service.

4.12 This hypothetical example demonstrates how VSAs create efficiencies and, as illustrated by the "niche ports", can allow capacity to be allocated for alternate use to achieve broader coverage. As a practical example, Tables 8.6 and 8.7 of the

⁹ World Shipping Council: Observations on Port Congestion, Vessel Size and Vessel Sharing Agreements, July 2015, page 5: http://www.worldshipping.org/industry-issues/transportation-infrastructure/Observations_on_Port_Congestion_Vessel_Size_and_VSAs_Updated_July_6_2015.pdf

Application show the number of weekly services that two carriers, [...] and [...], were able to offer after joining a VSA increased by [...] % and [...] %, respectively. Thus, in the absence of joining those VSAs, [...]’s weekly services in Asia-North Europe would have remained at [...] instead of [...]. Its Asian port calls would have remained at [...] instead of [...] (a reduction of [...] %). [...]’s Asian port calls would have remained at [...] instead of [...] (a reduction of [...] %). Without VSAs, carriers simply would offer service that is substantially reduced from what they are able to offer today through their participation in VSAs.

- 4.13 Not only does this provide the shipper customer with an expanded service network but, as HKLSA has previously explained to the Commission, VSAs are also critically important in allowing many small to medium sized carriers to compete with larger carriers with respect to service. Specific examples of this are provided at paragraphs 4.28 and 4.29 below.
- 4.14 The size of most carriers active in Hong Kong makes it difficult for them to compete effectively with the larger operators on their own, both in terms of service strings and ports of call. Through VSAs, smaller carriers are not hindered by the lack of their own capacity and are able to compete fiercely on parameters such as service quality and quantity.
- 4.15 In the modern shipping industry, a carrier of any size would not be able to operate at all outside of a VSA. In order to operate, a carrier has to be able to compete with numerous other carriers in the market and, as noted, every other carrier operates within VSAs, consequently achieving the described expansion of service and economies of scale. A single carrier cannot afford individually to invest in a sufficient number of vessels, particularly the larger vessels that are in use today, to compete with other groups of carriers operating in VSAs. The only practical option for carriers is to join a VSA.
- 4.16 In this regard, if the Commission were not to provide a block exemption order for VSAs, creating regulatory uncertainty for carriers as to whether they could operate their VSAs in Hong Kong trades, it would not be feasible for carriers to operate separately in the Hong Kong trades, outside of VSAs. The only alternative would be for carriers to eliminate Hong Kong as a port of call in their VSAs. Given the abundance of geographically close and business-friendly alternatives for VSAs in the region, Hong Kong would lose out to competing ports, adversely affecting consumers.

VSAs facilitate transshipment

- 4.17 The Commission accepts in its Statement that VSAs may facilitate transshipment through, for example, the ease with which transshipment cargo may be loaded onto and unloaded from different carriers’ vessels, but requests further evidence of this. As a basic concept, it can be seen that as VSAs allow individual lines to access an increased number of vessels through their VSA partners, they increase the scope for quicker and more effective transshipment.

- 4.18 There are other efficiencies in transshipment that are facilitated by carriers' participation in VSAs. For example, the arrival of fuller vessels (due to the increased utilisation rates arising from VSAs) allows VSA members to spread the costs of moving cargo onto a connecting vessel across a greater volume of cargo, thus reducing unit costs which is reflected in lower charges to the customer. To illustrate this with a practical example, VSAs greatly streamline supply through barge feeder traffic. A high proportion of the cargo transhipped through Hong Kong originates in the Pearl River Delta region of the PRC and is floated down to Hong Kong on barges. Barges are loaded according to the vessels to which they will be supplying feeder services. VSAs therefore allow cargo of multiple carriers to be loaded onto the same barges headed for a particular vessel. This reduces the number of barges required (thus reducing the unit cost to the carrier which is passed on to the customer), reduces congestion in the port of Hong Kong and speeds up transfer times onto ships offering capacity to other VSA partners.
- 4.19 As noted in the Application, there are certain similarities between VSAs and airline code-sharing agreements. Both code-sharing agreements and VSAs can bring about network efficiencies for customers of a qualitative and quantitative nature, improving existing services by increasing frequencies and leading to better connections and potentially creating new services by connecting services that would otherwise be operated separately.
- 4.20 From a transshipment perspective, the benefits of VSAs, like code-sharing agreements, include the efficiency of facilitating network connections to better enable the link between service offerings of different operators routed to different destinations. Customers benefit from the provision of a seamless service of a consistent quality, without having to communicate with multiple providers, and are able to access more frequent services to a more extensive international network with greater convenience and ease of arrangement.

VSAs result in cost savings

- 4.21 The Commission has requested further empirical evidence demonstrating that VSAs have led to or lead to cost savings from the use of larger vessels and/or as a result of higher utilisation rates on particular vessels. In addition to the practical example of savings on barge feeder traffic at paragraph 4.18, HKLSA provides costs data demonstrating this at confidential Annex 2. These data compare estimated costs of two similarly-sized carriers, one that participates in a major VSA alliance and one that does not.
- 4.22 These data demonstrate the cost savings available to the carrier that is party to the VSA alliance through the fact that its estimated costs are, consistently lower than the other carrier's in most trades. Across the three trades where we have a complete dataset, and over the most recent three year time period, the VSA alliance carrier's slot costs are cheaper than the non-VSA alliance carrier's by: [...] % on the Asia-East Cost North America trade; [...] % on the Asia-Mediterranean trade; and [...] % on the Asia-West Coast North America trade.

4.23 The cost savings shown at Annex 2 are generated due to economies of scale – i.e., pooling multiple resources onto fewer and larger vessels creates cost efficiencies. This means that a carrier party to an alliance (i.e. a collection of VSAs) on the relevant trades, generally has cheaper operating slot costs than a carrier not a party to an alliance on the relevant trades. This demonstrates the cost-reducing efficiencies of VSAs, which carriers are able to harness to offer customers lower prices.

4.24 To demonstrate this with third-party analysis, HKLSA points to the chapter in the Boston Consulting Group's *Transformation Imperative in Container Shipping* report, entitled "Extracting more Value from Alliances", which states that:

"[e]conomies of scale are a crucial aspect of reducing slot costs to enable competitiveness on rates. Our models show that, depending on the trade, relative vessel size, and cost level, carriers can typically achieve slot cost savings of 15 to 20 percent by doubling the size of vessels. Vessel-sharing agreements (VSAs) and firmer alliances let carriers jointly deploy the most economic vessels to serve specific trades, provide more departures in key ports, and achieve wider network coverage. Moreover, sharing spreads the utilization burden of larger vessels among more companies and clients, and carriers can, therefore, offer a good product at low cost".¹⁰

4.25 As further evidence of the efficiencies arising from VSAs, a McKinsey and Co. report of April 2015 opens by stating that there are cost (and environmental) advantages of using larger ships on the main trades, particularly:

"[g]iven that a vessel with 14,000 twenty-foot equivalent units (TEUs) can be 30 percent more fuel efficient per box than a 7,000-TEU vessel, the savings quickly add up".¹¹

4.26 Additionally, as the chart at confidential Annex 3 shows, carriers' costs are reduced with increased vessel size. For example, a carrier's slot cost per TEU for a [...]TEU ship is roughly \$[...]. By comparison, a carrier's slot cost per TEU for a [...]TEU ship is less than \$[...]. Without access to VSAs, carriers struggle to fill the more efficient [...]TEU ship, with their own customers' cargo alone. Cooperation through VSAs gives rise to the efficiency of greater utilisation, in turn driving down cost per TEU. Absent any such cooperation, the carrier would be forced to deploy smaller, less efficient ships, and charge greater slot costs.

VSAs increase competition by allowing smaller carriers to compete and increasing choice of carriers

4.27 In the Statement, the Commission asks for examples of carriers, particularly small ones, expanding their service offering by entering into VSAs. As noted, HKLSA has already provided the Commission with such an example (referred to in paragraph

¹⁰ The Boston Consulting Group: *Transformation Imperative in Container Shipping* (March 2015) Page 27

¹¹ McKinsey and Co.: *Landside operations: The next frontier for container-shipping alliances* (April 2015), Page 2

4.33 of the Statement) and maintains that smaller carriers are able to benefit disproportionately through VSA membership. To quote the McKinsey and Co report:

*“alliances have allowed the larger lines to achieve some further measure of resource rationalization, but the main beneficiaries have been the smaller lines. The allied smaller lines have been able to serve more destinations without spending billions on a larger fleet of ships”.*¹²

4.28 As further evidence of this, HKLSA provides at confidential Annex 4 and 5 two practical examples of the expanded service offering available to small lines when entering into VSAs. In Annex 4, it can be seen that, through various VSAs, the smaller carrier in question has leveraged its ability to service multiple destinations with sufficient regularity of vessel calls to have a commercially-viable frequency of service. Overall, this allows an individual carrier to serve more destinations, as it can spread its fleet more thinly between trades without compromising the regularity and frequency with which it will be able to offer sailings to customers.

4.29 The extract of relevant text from a VSA Memorandum of Understanding between a small carrier and a large carrier at Annex 5 shows that VSA slot and deadweight allocation is apportioned according to how much capacity is contributed by a particular carrier, i.e. on a “what you put in, you take out” basis. In this example, the smaller line benefits greatly from an expanded service offering by putting up [...] of its vessels for access to [...] vessels of its VSA partner. All [...] vessels in this agreement will service the same route so, in this particular VSA, there is no expansion of the scope of ports served as a direct result of the VSA (which is often the case in other examples), but the frequency of sailings available to the smaller carrier is improved [...]. As such, the smaller carrier is able to offer its customers a more frequent service and, in doing so, is able to compete with larger carriers, which might have the resources by themselves to offer such a regular service to shippers.

Cost savings passed onto consumers

4.30 The passing on of cost savings to consumers (including shippers, consignees, freight forwarders, logistics companies and other customers) is recognised by the Commission in the Statement as a matter of general economic principle. The incentives for carriers to pass on cost savings is supported in the Boston Consulting Group paper of March 2015, which outlines a “Cost-Out Model” and holds that:

*“given the weak market fundamentals and fragmentation in the industry, to fill their ships, carriers will likely stick with a price floor at the level of marginal costs. Consequently, their cost savings will be passed on to customers in the form of lower rates”.*¹³

4.31 Under this theory, the ability to take out costs can be seen as a strong proxy for estimating future freight rates. The Boston Consulting Group bases this on a model

¹² Ibid.

¹³ The Boston Consulting Group: *Transformation Imperative in Container Shipping* (March 2015) page 9

showing that unit costs decline as cumulative volume increases over time. This model thus predicts cost reductions by carriers if they can rationalise operational processes, enhance efficiencies and improve scale.

- 4.32 The evidence already provided to the Commission by HKLSA is consistent with this theory. Rate trends clearly show that shippers currently enjoy vastly lower rates on routes via Hong Kong than they have done for many years and VSAs have continued to operate in all Hong Kong trades during this period. Even before the current rate reductions, rates in recent years have been at consistently low levels, and have not materially increased over the past 10 years. Applying the Boston Consulting Group theory, this is, at least in part, a result of VSAs. The fact that such low rates are possible in itself suggests that carriers pass on any cost savings from VSAs to customers. It also demonstrates how competitive the current market is, thus satisfying the fourth condition of the Efficiencies Exclusion.

Certain issues arising from the Commission's proposed market share threshold

- 4.33 The Commission states that the benefits of VSAs may be "*less likely to be generated or fully exploited, and passed on to customers, if the VSA members are not subject to effective competition from outside the VSA*".¹⁴ On this basis, the Commission has taken the preliminary view that the Proposed Order should apply only where the combined market share of VSA members does not exceed 40% (or 45% over a period of two consecutive years).
- 4.34 The Commission does not explain how it arrived at the proposed 40% threshold. The market share limit is first mentioned in the Statement when discussing the efficiency of broader service coverage and higher service frequency.¹⁵ The Commission notes that a number of parties which participated in the preliminary consultation, including users of liner shipping services, agreed that VSAs do indeed give rise to these efficiencies and increase service coverage. The Commission then cites a "*limited number of parties*"¹⁶ which have voiced concerns that these efficiencies are not necessarily generated where there is a high level of market concentration. The Commission however quotes only the submission of a single party in suggesting that carriers in larger VSAs may have *de facto* control over supply in the market and consequently refrain from deploying larger vessels at certain ports. This is not supported by any evidence or facts. The Statement does not contain any justification either for: (i) requiring a market share threshold; or (ii) setting the threshold at 40%.
- 4.35 In terms of lower pricing, carriers are flexible in their provision of shipping services and, as explained at paragraph 5.27, they constantly evaluate where vessel sailings should be scheduled. Market share on any particular trade will never be static and even carriers operating a high proportion of the capacity on a trade at a given time are subject to downward pricing pressure from potential entrants to that particular trade, which operate vessels elsewhere. There is no barrier to entry for a carrier to allocate

¹⁴ Paragraph 4.47

¹⁵ Ibid.

¹⁶ Paragraph 4.46

more tonnage to a different trade and, as such, there is always pressure on pricing, regardless of market share. Leaving aside the fact that it is unclear what the Commission means by “*de facto*” control, given the nature of the shipping industry (with very high fixed costs and low variable costs), carriers will always be incentivised to lower prices to increase utilisation. Therefore, unless a carrier is operating consistently at high utilisation rates (which is not the case for any carrier on any trade in current market conditions), the cost savings arising from VSAs will be passed on to customers.

- 4.36 In terms of other efficiencies resulting from VSAs, the Commission’s argument that “*the benefits of VSAs in terms of a broader service coverage and/or higher service frequencies may be less likely to be generated or fully exploited, and passed on to customers if the VSA members are not subject to effective competition from outside the VSA*”¹⁷ is illogical. These efficiencies, by their very nature, pass benefits to consumers in the form of increased breadth of destinations served and a more regular scheduling of vessels passing through Hong Kong. The proposed market threshold will not impact on the degree to which consumers enjoy broader service coverage or higher frequency.
- 4.37 In view of the above arguments, the Commission has not adequately substantiated with facts and evidence the assertion made by the single third party described at paragraph 3.4 regarding larger VSAs having *de facto* control over supply in the market. If no evidence is available to support this assertion, there is no justifiable reason for imposing a market share threshold as a condition to the proposed block exemption order for VSAs.
- 4.38 Furthermore, should the Commission remain of the view that such a threshold is necessary, there are good arguments as to why this threshold should be increased. A threshold of 40% is too low, as it potentially catches VSAs that cannot realistically exercise “*de facto* control over supply in the market”, thus leading to a greater chance that existing VSAs might already fall outside the block exemption and create unwarranted legal uncertainty.
- 4.39 The Commission should instead consider the approach taken by the Competition Commission of Singapore (“**CCS**”), given the similarities with the Hong Kong port.¹⁸ Hong Kong, like Singapore, is a transshipment port used on various trades, rather than a significant regional end destination in itself and HKLSA suggests that the Commission should be guided by the position in Singapore, where the CCS uses 50% market share as an indicator of VSAs that need to be brought to its attention through filing. Given the close parallels between Singapore and Hong Kong, HKLSA believes that the Commission should be comfortable that effective competition between all carriers would still be retained on the relevant trades with a sufficient degree of certainty that the claimed efficiencies arising from VSAs would be generated and

¹⁷ Paragraph 4.47

¹⁸ In Singapore, exceeding the limit of 50% does not take a VSA outside of the block exemption, it merely requires the VSA in question to file the relevant agreement with the CCS. By contrast, the Proposed Order would remove the protection of the block exemption altogether for VSAs above the limit in Hong Kong, representing a harsher approach than the CCS.

passed on to customers, without affording carriers the possibility of eliminating competition, at a market share level above 40%.

5. VDAs

5.1 HKLSA is disappointed at the Commission's position on VDAs in the Statement and considers the Commission's legal interpretation of section 1 of Schedule 1 to the Ordinance to be overly restrictive, in particular by not recognising the broad efficiencies which VDAs give rise to in Hong Kong.

5.2 HKLSA calls on the Commission to reconsider its position over the particular types of efficiencies arising from VDAs that can fall within the Efficiencies Exclusion and to recognise, as it did with VSAs, the important efficiencies which VDAs give rise to in Hong Kong that results in clear benefits to the broader Hong Kong economy and all consumers, not just shipper customers of carriers.

5.3 HKLSA notes that, in its assessment of VSAs, the Commission took account of: (i) the qualitative efficiencies in promoting Hong Kong as a maritime centre for shipping-related services; and (ii) the broader cost efficiencies to all consumers in Hong Kong of promoting Hong Kong as a transshipment hub. As noted above, VSAs and VDAs are linked, and therefore these efficiencies flow equally from VDAs as they do from VSAs.

5.4 In relation to this argument, HKLSA sets out below:

(A) how broad efficiencies can apply under the scope of the Ordinance at section 1 of Schedule 1, where the drafting of the Efficiencies Exclusion is wider than the approach that has been taken by the Commission in the Statement, as further considered at paragraphs 5.14 to 5.19 below;

(B) details of the two broad efficiencies to which VDAs give rise in Hong Kong allowing Hong Kong to compete against other regional ports as both: (i) a super-connector shipping centre (considered at paragraphs 5.20 to 5.25); and (ii) a transshipment hub (considered at paragraphs 5.26 to 5.33). These efficiencies respectively enhance shipping-related industries in Hong Kong and increase the volume of vessels routed through the port, consequently resulting in economies of scale and reduced costs per TEU. This in turn lowers the costs and thus the retail prices for all consumer products that are transported to Hong Kong in this way; and

(C) the benefit should be assessed with greater emphasis on "consumers", specifically in Hong Kong, comprising a broader definition than "*users of liner shipping services such as shippers, consignees, freight forwarders, logistics companies and other customers*",¹⁹ due to the significant impact of the shipping industry on ordinary everyday consumers in Hong Kong, as further

¹⁹ Paragraph 4.43

considered at paragraphs 5.34 to 5.39 and then also at paragraphs 5.58 to 5.64 below.

- 5.5 HKLSA then examines in more detail the three efficiencies which were specifically cited in the Application as contributing to improving production / distribution and promoting technical / economic progress, i.e. rate stability, service stability and rate and surcharge transparency efficiencies to customers.
- 5.6 In this section, HKLSA would like to emphasise that the Commission should consider VDAs as a whole when reviewing the Application, including the information-sharing aspect of VDAs for which further information is provided below.

Information-sharing aspect of VDAs

- 5.7 The Commission has looked in detail at VDA pricing discussions in the Statement, but has also acknowledged that, in addition to discussing freight rates, VDAs also provide carriers with improved access to trade information. The types of market information that may be exchanged within a VDA include statistics, reports or other information relating to market trends, economic forecasts, operational or technological developments, and policy or legal issues. HKLSA is of the view that, when assessing the application of VDAs to the Efficiencies Exclusion, these aspects should also be considered in full.
- 5.8 The exchange of market information between carriers is a key part of VDAs and falls under the scope of activities requiring a block exemption order. The Commission has suggested in the Statement that:

“some of the relevant information can be exchanged regardless of whether VDAs meet the conditions of the efficiency exclusion and/or regardless of whether the Commission issues a block exemption order for VDAs”²⁰

- 5.9 HKLSA disagrees with this statement; these discussions are not able to fall under the self-assessment regime as they could potentially give rise to competition concerns in so far as they relate to sensitive topics, such as supply and demand trends, costs (general and Hong Kong specific) and vessel utilisation levels. Given the difficulties with self-assessment when it comes to information exchange between competitors and the need for legal certainty for the shipping industry, a block exemption order is required just as much for these elements of VDAs as for pricing discussions.
- 5.10 Whilst, as the Commission pointed out, publicly-available information sources on the shipping industry do exist, they tend to be less useful for carriers and are inferior to the information that can be obtained from VDAs for various reasons, including that:

²⁰ Paragraph 4.99

- (A) the collection of publicly available information can be a time-consuming and costly process;
- (B) data from publicly available sources are generally available only on a historical basis and are therefore at least several months out of date by the time this is available to carriers;
- (C) the format of data is often not helpful, e.g. Government statistical departments might refer to cargo value, rather than cargo volume. Information provided by VDAs is more specifically tailored to carriers' specific needs;
- (D) public information based on Government statistics is not always complete in terms of its scope, whereas information from VDAs does not obscure the origin and destination of cargo, giving carriers a complete picture of movement data, which allows them to accurately model the geography of future demand; and
- (E) capacity and utilisation data from public sources is usually limited and does not include smaller, niche trades that carriers participate in, and to which volume data is perhaps even more necessary. These trades include the intra-Asia trades, which are quite significant for Hong Kong, and which when considered cumulatively, are the largest trade in the world. On the other hand, VDAs collect and disseminate information on the relevant trades on which their members operate, thus increasing the geographic coverage.

5.11 For these reasons, information exchanged through VDAs is needed for carriers to effectively operate on the market and is of a markedly different quality to publicly available information. As stated in the Application and set out further below at paragraph 5.27, the exchange of market information within a VDA leads to numerous efficiencies, such as the ability of carriers to have accurate and timely trade data which allows them to make more informed business decisions, for example, which port to direct its transshipment cargo through. Carriers, particularly the smaller players on the market, would struggle to deploy operations efficiently if they had to base movements only on publicly available sources of information (which are not sufficiently timely or accurate), making these discussions indispensable to the achievement of the efficiencies described above.

5.12 The Hong Kong shipping industry needs legal certainty to ensure that the information exchanged within a VDA is permitted under the Ordinance. Having conducted a lengthy and detailed review, the Commission should be in a position to provide this clarity. Without such specific guidance from the Commission, it will be difficult for carriers to be sufficiently certain of what information can be exchanged under the First Conduct Rule, which in turn means that carriers will struggle to meet, discuss the industry and exchange information at all. This will mean that the industry will lose the benefit of the information exchanges, which in turn will harm the industry and have adverse effects on competition and consumers.

- 5.13 Furthermore, the Commission cannot ignore the fact that such discussions are permitted in almost all other jurisdictions in Asia Pacific. It is therefore important for carriers to have legal certainty that they can continue such discussions without risk of being in breach of the Ordinance. HKLSA would welcome the Commission exploring an alternative outcome rather than simply proposing not to issue any block exemption order for VDAs at all.

The broad efficiencies arising from VDAs in Hong Kong

Efficiencies Exclusion test in the Ordinance covers broad overall efficiencies

- 5.14 The Efficiencies Exclusion is capable of covering broad overall efficiencies to consumers in Hong Kong, not just narrow direct efficiencies to immediate customers of carriers. Having taken this into account in its assessment of VSAs (for example, paragraph 4.25 of the Statement), the Commission has failed to give this adequate weight in its assessment of VDAs. HKLSA sets out below why the broader interpretation is justified as a general principle, for both VSAs and VDAs.
- 5.15 First, section 1(a) of Schedule 1 to the Ordinance refers to “*improving production or distribution*” and “*promoting technical or economic progress*”. Under Hong Kong law, there is no jurisprudence or case law on how these specific terms should be defined. The starting point should therefore be the plain language of the provision and the ordinary meaning of the words based on a “*fair, large and liberal construction and interpretation*”.²¹
- 5.16 Second, the title of section 1 of Schedule 1 to the Ordinance, “*agreements enhancing overall economic efficiency*”, demonstrates the legislative intent for a breadth of efficiencies to be encompassed by the Efficiencies Exclusion and indicates a wider test than the equivalent provisions of some other jurisdictions, such as the EU, where no such wording exists at Article 101(3) of the Treaty on the Functioning of the EU. The Commission therefore has scope to find efficiencies on a broad basis.
- 5.17 The Commission dismisses HKLSA’s argument regarding the broader efficiencies that arise from VDAs as a mere assertion that: “*shipping lines find a consistent or particular approach to regulation to be a relevant consideration in assessing whether a given location might serve as a transshipment hub*” and concludes that this argument “*does not concern any particular efficiency created by VDAs*”.²² The Commission has not fully appreciated HKLSA’s argument here – it is not consistent regulation *per se* which gives rise to the efficiency, but how this plays out specifically in the liner shipping industry, which is responsible for transporting a significant proportion of the goods that are sold to consumers in Hong Kong. We explain this in further detail at paragraphs 5.20 to 5.33 below.
- 5.18 The question that should be asked in the context of the Efficiencies Exclusion is whether an efficiency (including contributing to promoting economic progress) is created in for the benefit of consumers in Hong Kong and, in considering this question,

²¹ Interpretation and General Clauses Ordinance (Cap 1), section 19

²² Paragraph 4.115

the Commission should not ignore the fact that exemptions for VDAs represent the global regulatory norm and VDAs will continue to be acceptable in other jurisdictions, regardless of the Commission's decision. In this context, the industry in Hong Kong should not be disadvantaged to the detriment of the economy and consumers because of a failure to recognise the economic progress that has been promoted by VDAs and enjoyed by Hong Kong to date.

- 5.19 As the Application represents the first case in applying the Efficiencies Exclusion criteria in Hong Kong and there is an absence of any legal confirmation from the Court as to how efficiencies should be interpreted, the Commission should take a natural and broad interpretation of the scope of the Efficiencies Exclusion taking into account the legal and factual context in Hong Kong.

Broad efficiency to the Hong Kong economy of VDAs promoting a super-connector maritime shipping centre and Hong Kong role in OBOR

- 5.20 As set out in section 3 above, VDAs and VSAs are inter-linked; both are crucial for Hong Kong to fully achieve its potential as a super-connector shipping hub and maritime centre. This efficiency gives rise to quality improvements and other benefits of a qualitative nature by facilitating and enhancing Hong Kong's ability to provide maritime services, which would otherwise struggle to exist, without the Hong Kong-specific data collated through VDAs. In other words, the information efficiencies to which VDAs give rise, promoting Hong Kong as a maritime centre, can be seen as "*improving production or distribution*" or "*promoting technical or economic progress*".

- 5.21 VDAs provide the forum necessary for the exchange and review of market data, supply and demand forecasts, international trade flows and industry trends, which feed into the various industries that survive on the back of shipping in any maritime centre. VDAs are the only platform for this kind of information exchange in the industry and the absence of any form of block exemption order covering VDAs would harm the wider industries that rely on VDA data, e.g. banks, insurers, lawyers, retailers, consumers.

- 5.22 This would also harm Hong Kong's ability to play a key role in the OBOR initiative, which relies heavily on the flow of information between carriers to efficiently connect vessels with cargo emanating from southern China. Without VDA information sharing in Hong Kong, carriers would be operating in the dark for Hong Kong trade flows and Hong Kong's port would be isolated from the rest of the global shipping industry, hampering its ability to operate as a transshipment hub and play a role in OBOR. VDA information sharing is crucial; being merely a port will not be sufficient to realise Hong Kong's role in the OBOR initiative.

- 5.23 The importance of both forms of liner shipping agreements, VSAs and VDAs, in establishing a strong maritime centre, encompassing businesses beyond just shipping, has been recognised elsewhere, for example in Singapore when the liner shipping block exemption order was first extended in 2010. The CCS' consultation paper stated then that the order was "*recognised as important in maintaining Singapore's*

position as a premier international maritime centre, which was consistent with the promotion of economic progress.”²³ In particular:

“[a]s a small and open economy, the presence of an extensive network of liner shipping companies has played a large part in contributing to Singapore’s status as a premier international maritime centre for liner shipping operations. In particular, the concentration of activity within Singapore generates considerable benefits, both directly and indirectly to Singapore... ..the presence of a large number of major shipping companies has important flow-through benefits for the Singapore economy.”²⁴

5.24 Other Asian countries have also recently renewed exemptions for VDAs, considering the broader benefits these agreements contribute to all stakeholders and the economy at large. In June 2016, the Japan Ministry of Land, Infrastructure, Trade, and Tourism (“MLIT”) considered the following factors when renewing its block exemption that has been in place for over 50 years: (1) anti-trust immunity systems in other countries; (2) impact on customers; and (3) impact on the Japanese economy as a whole. In light of these broad factors, MLIT determined that a continued exemption for VDAs would keep Japan’s legal regime consistent with that of its trading partners and competitors for liner shipping services, and would be beneficial to all consumers and the Japanese economy.

5.25 There are also significant “flow-through benefits” to consumers, industry and the whole Hong Kong economy of building a centre of concentrated support services and activity around the operations of carriers and shippers, as outlined in more detail at paragraphs 3.4 to 3.9 above. The related infrastructure accompanying a maritime centre in Hong Kong also supports expanded and more efficient shipping services that will ultimately be pro-competitive for Hong Kong and will promote Hong Kong within OBOR. In order for this to be achieved however, a block exemption covering VDAs, as well as VSAs, will be necessary.

Broad efficiency to the Hong Kong economy of VDAs promoting transshipment services in Hong Kong

5.26 The broader benefits of VDAs in facilitating transshipment result in a greater number of vessels calling at the port of Hong Kong, which in turn results in increased options and higher shipment frequencies for customers that need to transport goods to Hong Kong. This leads to clear benefits to the Hong Kong economy and consumers, which is evidence of “*improving production or distribution*” or “*promoting technical or economic progress*”. As stated above, HKLSA seeks in this section to provide further explanations to demonstrate how VDAs give rise to transshipment efficiencies for Hong Kong.

²³<https://www.ccs.gov.sg/~media/custom/ccs/files/public%20register%20and%20consultation/public%20consultation%20items/2010%20public%20consultation%20on%20ccss%20proposed%20recomen/publicconsultation2010final.ashx>, paragraph 13

²⁴ Ibid.

- 5.27 As a commercial matter, carriers are constantly having to undergo a process of internal decision-making and strategy to decide which particular ports to call when routing a vessel, in order to best serve the needs of their customers. This includes the choice of port through which to facilitate transshipment traffic. VDAs are crucial to this decision as carriers rely on the up-to-date and relevant statistics and trade projections discussed at a VDA meeting to facilitate these commercial decisions.
- 5.28 The exchange of commercial information through VDAs are critical to carriers. This includes discussions on: trade growth and development, cargo flows, supply and demand trends, regulatory developments and compliance issues, costs (general and Hong Kong specific), current and historical rate trends, vessel utilisation levels and best practices (general and Hong Kong specific), including service contract rules, terms, conditions, all of which provide the information structure around which transshipment is based.
- 5.29 As explained previously to the Commission and explained in part at paragraph 5.10, there are no substitutes for the quality and relevance of VDA data on which carriers place by far the most weight; Government and publicly-available sources are not a reliable or useful proxy for VDA data.
- 5.30 At VDA meetings and through VDA secretariats, carriers discuss specific cargo flows and weekly statistics, outlining which ports have declining or increasing cargo throughput, both currently and forecast. Taking Hong Kong as an example, this enables carriers on an individual basis to have the relevant information to hand in order to calculate how many ships should be allocated to serve Hong Kong at any given time and how much space should be allotted on each vessel for goods to be picked up in Hong Kong. For example, if a seasonal harvest of fruit from southern China led to a sudden glut of perishable cargo moving through Hong Kong, carriers could allocate project-specific capacity to Hong Kong, holding back on filling vessels with non-urgent cargo from other ports.
- 5.31 If there is no longer any legal certainty for VDAs, carriers would lose an important information sharing platform for Hong Kong, such that they would no longer have access to the commercial information and statistics (e.g. projected demand through the Hong Kong port) that are important in deciding whether to transport their transshipment cargo through Hong Kong.
- 5.32 It is crucial to appreciate that such information on other regional ports will still be available, which means that carriers would have much better visibility over these other ports. Given the very discretionary nature of transshipment traffic, there would be a clear commercial incentive to call at these other ports, where VDAs have more market intelligence to support a business case for that routing, instead of Hong Kong. It does not make business sense to choose a transshipment hub that involves a greater degree of risk (due to the lack of credible market intelligence ordinarily provided by VDAs) and therefore carriers would find it more difficult to route vessels through Hong Kong if the Commission were not to grant a block exemption order for VDAs. This would lead to a shift of carriers to ports where VDAs are exempt or otherwise have

immunity, ultimately losing Hong Kong the critical mass of shipping frequency necessary to operate as a transshipment hub, let alone a maritime centre.

- 5.33 As discussed in detail in the Application, and as recently reinforced by countries like Singapore and Japan, both VDAs and VSAs facilitate investment in vessels, equipment and vessel services, which in turn provide more and higher quality service options for Hong Kong stakeholders. Consumers benefit in the form of cheaper goods as the cost of importing cargo to Hong Kong is reduced. Without a block exemption for VDAs, Hong Kong's shipping industry will ultimately suffer and consumers will be faced with higher costs for everyday items.

Efficiencies Exclusion test should be applied on the basis of Hong Kong-specific benefits to "consumers"

- 5.34 In the context of a regulatory environment across most of Asia and the world, where VDAs are permitted and are the only legal forum at which carriers can meet to hold discussions, VDAs contribute to an important efficiency in promoting the future of shipping in Hong Kong for the benefit of end consumers as well as shippers.
- 5.35 Unlike the position taken in the EU, where individual competing European ports all adhere to the European Commission's position on liner shipping agreements, Hong Kong would be a regional anomaly as a significant Asian port without any form of exemption for VDAs and would be at a great disadvantage when compared with its competitors for international transshipment. Carriers can much more easily afford to bypass Hong Kong if it does not have a business-friendly regulatory environment.
- 5.36 The Commission should consider the specific efficiencies that VDAs give rise to in Hong Kong and for Hong Kong consumers, taking into consideration Hong Kong's position as a transshipment hub set within a strong production/manufacturing region.
- 5.37 In this regard, the approach adopted in Singapore is useful as Singapore is, like Hong Kong, a single port and transshipment hub. Neither Hong nor Singapore has a large presence in global trade itself and neither is a significant point of origin and destination for shipment. The Commission should, as part of its analysis, look to the analogous situation and essentially identical block exemption criteria (as regards the first condition of the Efficiencies Exclusion) in Singapore and the CCS' own recent statement that:

"[g]iven the size of the domestic economy, Singapore is not a major port of origin or destination unlike other major ports and a very large proportion of Singapore's container cargo throughput involves transshipment and Singapore's container port is the world's largest transshipment hub. The connectivity and concentration of liner shipping services available in Singapore generates considerable benefits, both directly and indirectly to Singapore, including providing a higher degree of connectivity and service choice for Singapore's importers and exporters, beyond what might ordinarily

be expected if the port had simply developed as a gateway facility.”²⁵
[Emphasis added.]

- 5.38 Many of the factors the CCS took into account in recommending the extension are equally applicable in the context of Hong Kong, including the fact that liner shipping agreements, both VSAs and VDAs, result in higher connectivity and concentration of liner shipping services. These are broad efficiencies that have been recognised by the CCS. In particular, the CCS stated that it had assessed:

“that liner shipping agreements contribute to improving the production of liner shipping services and the distribution of goods in Singapore. In particular, they enable the connectivity of Singapore’s container port with consequent broader benefits to the Singapore economy, and facilitate cost savings for the liners from resultant economies of scale.”²⁶ [Emphasis added.]

- 5.39 For the same reasons given by the CCS, the Commission should support a finding that VDAs, like VSAs, give rise to efficiencies, which would be sufficient to satisfy the first condition of the Efficiencies Exclusion under the Ordinance. A broad concept of efficiencies taking into account Hong Kong’s specific position should demonstrate to the Commission that VDAs give rise to efficiencies for the Hong Kong economy and wider Hong Kong consumers adequate to satisfy the Ordinance’s test for a block exemption order.

VDAs contribute to improving production / distribution and promoting technical / economic progress

- 5.40 In addition to the above argument on the broad efficiencies to which VDAs give rise, HKLSA remains of the view that the other three efficiencies which were cited in detail in the Application (rate stability, service stability and rate and surcharge transparency) are able to satisfy the conditions of the Efficiencies Exclusion. HKLSA sets out further explanations and arguments below to support this view.

VDAs promote rate stability, not higher rates

- 5.41 In examining whether rate stability amounts to an efficiency, the Commission notes that *“carriers coordinate on prices... ..[and] such coordination gives rise to the possibility of higher rates compared to the situation where carriers make pricing decisions independently of each other”*.²⁷ The description of “coordination” through VDAs, as opposed to discussion only, is misleading, but the Commission also does not engage with HKLSA’s explanations as to why shipping as an industry is unique in requiring the maintenance of a sustainable level of rates.

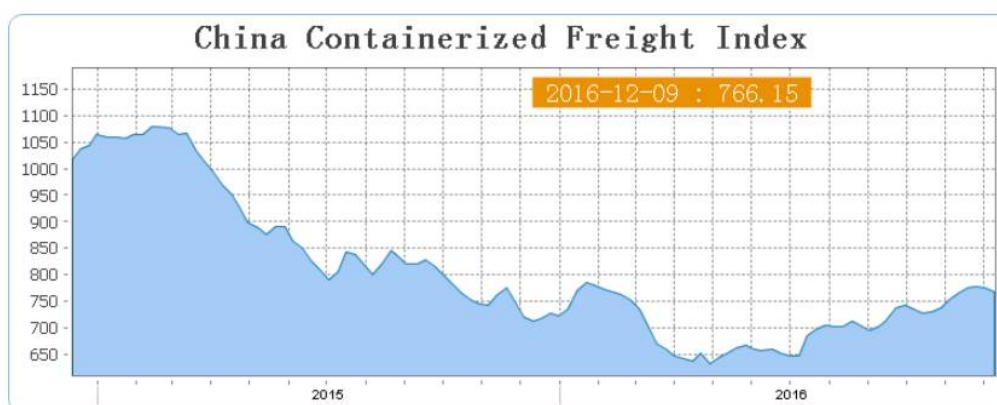
²⁵ Paragraph 18 of the CCS’s consultation document published on 25 May 2015, available at: <https://www.ccs.gov.sg/media-and-publications/media-releases/ccs-consults-on-proposed-recommendation-to-extend-beo-for-liner-shipping-agreements>.

²⁶ Paragraph 5 of the CCS response to the public consultation of May 2015 on the proposed recommendation to the Minister on the Competition (Block Exemption for Liner Shipping Agreements) Order available at https://www.ccs.gov.sg/public-register-and-consultation/public-consultation-items/2015-public-consultation-on-proposed-recommendation-to-extend-beo-for-liner-shipping-agreements?type=public_consultation.

²⁷ Paragraph 4.82

- 5.42 The Commission examines HKLSA's argument that, absent VDAs, freight rates could fall below a level that would ensure an appropriate level of investment and/or allow carriers to remain in the market, thus negatively impacting service stability. However, the Commission places its sole emphasis on the implication that VDAs allow for the possibility of higher prices for customers than would otherwise be the case. The Commission has not said that it has found any evidence to support its view or that this "possibility" has in fact led to higher prices.
- 5.43 Indeed, the Commission's theoretical concerns are contradicted by historic data, as can be seen in publicly-available figures from the Shanghai Shipping Exchange (the "SSE"), which currently shows a China Containerised Freight Index which has reduced markedly in recent years.²⁸ Freight rates are significantly less than their 2010 levels, and have declined every year since that time. The level of 2016 rates is significantly lower than the level in preceding years, demonstrating that the "possibility" of higher prices (as suggested by the Commission) does not materialise in actuality.

Figure 1
SSE China Containerised Freight Index



Source: SSE

- 5.44 In addition, the Commission appears to confuse the concepts of "inflated" rates with "stable" rates in its analysis. As noted in the Application, VDAs act to moderate rate volatility, which includes both excessively high and low rates, rather than to check against low rates. VDAs arrive at voluntary rate guidelines only after a review and discussion concerning market data. The adopted guidelines are reflective of the market data, but do not seek to artificially increase rates beyond what the market can bear. The purpose of VDAs is to allow carriers to achieve sustainable and stable rates, which in turn supports carriers' ability to continue to operate, maintaining a higher level of competition generally. VDAs are needed in Hong Kong to promote rate stability for the benefit of both carriers and shippers, as well as ultimately consumers.

²⁸ <http://en.sse.net.cn/indices/ccfinew.jsp>

- 5.45 It is relevant to note that this is unique to the shipping industry. The Commission's comments that "*any form of price coordination between competing undertakings (including cartel conduct) might be argued not to contravene the Ordinance on the basis that it gave rise to price stability from the perspective of the customer*"²⁹ shows that it has not fully appreciated the distinguishing features of the liner shipping industry. These characteristics (which are set out in full in the Application) include: high capital and fixed operating costs; the provision of a fixed regular service and an obligation on the ship to sail whether it is full or not; fluctuating and inelastic demand; lumpy supply and downward pressure on freight rates, which together mean that when there is spare capacity on vessels, there will be a continuous downward pressure on freight rates, often to a level below fixed and variable cost. That the shipping industry is unique in this regard is borne out by the fact that it is generally the only industry in other jurisdictions that has been provided an exemption from those countries' competition laws to allow for both VSAs and VDAs.
- 5.46 As discussed at paragraph 5.70 below, the Commission suggests that there exist other "*economically practicable and less restrictive means*"³⁰ of achieving rate stability. In particular, the Commission points to the possibility of shippers entering into fixed rate contracts. Whilst this is possible for some shippers, it is not always beneficial for shippers to be locked into fixed rate contracts and very few customers choose this option, despite it being currently available. In any event, fixed rate contracts would do nothing to address the wider issue of the specific industry characteristics, which predicate shipping towards regular fluctuations in pricing, exaggerating actual changes in supply and demand.
- 5.47 Furthermore, it is of note that the rate stability benefits to shippers in Hong Kong (and Asia generally) arising from VDAs are greater than they might be in other jurisdictions. As Hong Kong's position in Asia puts it in a primarily manufacturing/export market, there is a significant difference between Hong Kong and consumer/import markets. There are significant VDA advantage of rate stability for manufacturers consistently exporting goods globally on a "Free On Board" basis.
- 5.48 In terms of demonstrating that VDAs contribute to rate stability, the Commission has considered whether VDAs actually undermine rate stability by facilitating rate increases. This fails to take into account the economic driver for carriers to accept low rates in order to fill vessels. The Commission's cited example at paragraph 4.94 in the Statement of the difference between a recommended GRI and the resulting effect on actual pricing demonstrates that, although an individual recommended GRI may not result in long term stability, regular GRIs through VDAs are a means of reducing volatility.

VDAs promote service stability

- 5.49 HKLSA welcomes the Commission's acceptance that the maintenance (or improvement) of service levels could be considered to contribute to "*improving*

²⁹ Paragraph 4.84

³⁰ Paragraph 4.122

production or distribution" for the purposes of the Efficiencies Exclusion. We demonstrate below how the specific role of VDAs in maintaining service stability falls within this efficiency.

- 5.50 As VDAs are the global norm, there are, in many instances, no other data points for referencing the improvements which they offer. The EU is the only data point that exists of a major shipping centre removing a block exemption for VDAs and HKLSA has pointed to the relative decline in services in that jurisdiction since the removal. Whilst the Commission concludes that there could be other factors influencing the conditions on EU trades before and after the repeal of the EU Conference block exemption, and between conditions on the EU and Transpacific trades, as mentioned at paragraph 2.7, the Commission has not suggested that it has seen any evidence that this is the case and rejects HKLSA's comparisons out of hand as insufficient to establish that VDAs result in service stability.
- 5.51 HKLSA reiterates its previous arguments that pricing discussions through VDAs also contribute to improved service levels for shippers and generate efficiencies. As stated in the Application, exchanging and reviewing market data on trade flows, supply and demand forecasts and business trends allows carriers to make better individual carrier investment and deployment decisions that reflect true supply and demand trends, avoiding waste and inefficiency, ultimately leading to lower cost and better service to shippers.
- 5.52 In the absence of specific data, the Commission should be able to accept the logical conclusion that VDAs, including information exchange discussions, result in both improvements in vessel deployment and the promotion of investment in tonnage and infrastructure (including new technologies).

VDAs promote rate and surcharge transparency

- 5.53 Discussions through VDAs contribute to transparency for both carriers and shipper customers with regard to market trends and pricing practices. General discussions at VDA meetings promote transparency on industry updates and voluntary rate guidelines published by VDAs act as a reasoned, data-supported starting point for rate negotiations between shippers and carriers.
- 5.54 As mentioned at paragraph 5.45 above, HKLSA does not agree with the Commission's statement that any price recommendations by associations of undertakings might be argued not to contravene the Ordinance so long as they were issued publicly and therefore gave rise to increased price transparency from the perspective of the customer. This comment fails to take account of the unique nature of the shipping industry, whereby customers, e.g. freight forwarders, need significant visibility over rate forecasts to anticipate pricing for their own contracts with end-user customers, to be executed often a significant period of time before the actual cargo will ship. In order to be in the best position to negotiate a fair price for a forward-looking delivery contract, shipping customers are best served by the provision of

advance information on forecast rate movements, not just historic information such as that provided by other sources, such as the SSE.

- 5.55 The Commission's argument that there is no transparency for customers because parties can and do deviate from recommended VDA rates is flawed. The fact that GRIs are not generally charged as actual rates is representative of the healthy and effective state of individual negotiation for each contract between carriers and shippers. However, this does not mean that there is no transparency efficiency generated for customers by GRIs. More often than not, these negotiations will reference GRIs as a benchmark, but the reality of commercial positions between two parties will ultimately dictate the final price reached.
- 5.56 This transparency is useful for the customer, but, as mentioned at paragraph 5.11, is also useful for smaller carriers without sufficient scale and resource to have access to the same degree of market information and data on the basis of their own operations alone. As such, the transparency offered by VDAs assists carriers as well as shippers and contributes towards the efficiency of maintaining competitiveness among the smaller members of VDAs.
- 5.57 For the above reasons and contrary to the Commission's position in the Statement, HKLSA is of the view that there is good evidence and clear logical arguments to support the view that VDAs do meet the first condition of the Efficiencies Exclusion. The subsequent requirement then is for consumers to receive "*a fair share of the resulting benefit*" under the second condition of the Efficiencies Exclusion.

VDAs allow consumers a fair share of the benefit

- 5.58 In considering the second condition of the Efficiencies Exclusion, in light of the clarifications that HKLSA has made above, all of the efficiencies set out in paragraphs 5.20 to 5.57 result in a fair share of the resulting benefits being passed on to consumers.
- 5.59 As stated at paragraph 5.4(C), the Commission has taken a narrow definition of consumers to comprise "*users of liner shipping services such as shippers, consignees, freight forwarders, logistics companies and other customers*".³¹ In this context, it would be more constructive when assessing the efficiencies of VDAs to consider how the shipping industry has a significant impact on ordinary everyday consumers and not just customers, as further considered below. The Commission's own definition of consumers in the Guideline to the First Conduct Rule (the "**FCR Guideline**"),³² is relatively broad, i.e. "*all direct and indirect purchasers of the relevant products including businesses acting as purchasers (e.g. manufacturers purchasing inputs, retailers etc.) and final consumers*". [Emphasis added.]
- 5.60 The shipping industry, by its nature, impacts consumers in virtually every sector by transporting a very high proportion of all cargo into Hong Kong. End or "final"

³¹ Paragraph 4.43

³² Paragraph 2.14 of the Annex.

consumers in Hong Kong are direct beneficiaries and will receive a fair share of the broad efficiencies resulting from VDAs. These efficiencies, primarily resulting in the lower cost of consumer products, but also more intangible benefits, such as promoting Hong Kong abroad and increasing employment, are passed through the supply chain to consumers across Hong Kong in general.

- 5.61 As explained at paragraphs 5.26 to 5.33, it is only through ensuring a high volume of throughput and connectivity that Hong Kong remains competitive as a transshipment hub, allowing the trade, infrastructure, and employment currently brought about by Hong Kong's maritime industry, to be retained. In turn, this allows Hong Kong to benefit from a lower cost of goods and higher employment etc. This is in line with the Commission's FCR Guideline which states that:

*"[w]hile the parties need not demonstrate that consumers receive a share of every efficiency gain, the overall impact for consumers must at least be neutral and...[t]he key consideration is the overall impact on consumers of the products within the relevant market as a whole."*³³

- 5.62 The benefits arising from VDAs are not limited to final or end consumers. Shippers in particular, as a subset of consumers, benefit from more specific, industry-focused efficiencies as a direct result of VDAs:

- (A) *A high level of connectivity.* The continued operation of VDAs in Hong Kong keeps Hong Kong's compliance platform aligned with that of most jurisdictions in the world, including Hong Kong's key trading partners (namely the PRC and the United States), and allows carriers to maintain services through the port of Hong Kong. Shippers benefit from the presence of a large number of carriers in the form of the associated connectivity of trade routes. The CCS expressly recognised in its recent response to its public consultation that *"local shippers enjoy the benefits of competition due to the continued presence of a large number of liners and the associated connectivity of trade routes"*.³⁴
- (B) *Lower rate volatility.* This allows shippers to plan their shipping costs and long term strategy more effectively. As outlined at paragraph 5.47 above, this is of particular benefit to Hong Kong shippers organising Asian-manufactured exports to consumer markets.
- (C) *Increased service stability.* VDAs help to ensure continued services from carriers and allow them to improve their vessel deployment and investment decisions, both of which result in more reliable services for shippers.

- 5.63 These benefits to shippers arise through the efficiencies in improving the service available to shippers by facilitating the operation of carriers and easily outweigh the perceived negatives to shippers of VDAs permitting pricing discussions between

³³ Paragraph 2.15 of the Annex

³⁴ CCS 25 November 2015 response to the public consultation, para. 10(d).

carriers and issuing of voluntary guidelines. This is particularly the case as VDAs do not set rates and merely offer guidelines to carriers which can serve as the basis for discussion and individual negotiation with consumers.

- 5.64 Again to use Singapore as an example, the Commission points to a single difference in the statutory test for a block exemption between Hong Kong and Singapore, that Singapore's test does not contain an express requirement for efficiencies to be passed on to consumers. The Commission however does not recognise the fact that, notwithstanding that this is not officially part of the statutory test in Singapore, the CCS nevertheless examines this point and cites "*considerable benefits, both directly and indirectly to Singapore, including providing a higher degree of connectivity and service choice for Singapore's importers and exporters*".³⁵ Taking Singapore as useful and closely analogous precedent, the Commission should be able to conclude that benefits resulting from VDA efficiencies are sufficiently passed on to consumers.

VDAs do not impose restrictions on the undertakings concerned that are not indispensable to the attainment of the efficiency objectives

- 5.65 According to the FCR Guideline, the third condition of the Efficiencies Exclusion requires the parties to demonstrate that the agreement itself, i.e. the VDA, and each of the individual restrictions contained in the agreement, are reasonably necessary to attain the efficiencies. The FCR Guideline goes on to state that the determinative factor in this context will be whether the restrictive agreement and the individual restrictions in it make it possible to perform the activity in question more efficiently than would likely have been the case in the absence of the agreement or the restrictions.³⁶
- 5.66 As HKLSA has pointed out previously, VDAs do not impose any restrictions or obligations on their members to impose (or not impose) specific prices. Any rate guidelines are entirely voluntary and non-binding and parties can enter into and negotiate individual service contracts on any terms as they see fit. Such service contracts are confidential, so there are no means of monitoring or ensuring compliance with the recommendations. In addition, no penalty can be imposed on a party due to its failure to follow the guidelines.
- 5.67 Information exchange and discussions on market trends are also non-binding as they do not commit carriers to a particular business strategy or plan. They are purely to enable carriers to be better informed on market conditions. Also, VDAs allow carriers to withdraw on a reasonable notice period without financial penalty. They are therefore able to exit and compete outside the VDA framework within a very short period of time.

³⁵

<https://www.ccs.gov.sg/~media/custom/ccs/files/public%20register%20and%20consultation/public%20consultation%20items/2010%20public%20consultation%20on%20ccs%20proposed%20recommen/publicconsultation2010final.as>
hx, paragraph 18

³⁶ Paragraph 2.16 of the Annex.

- 5.68 As there are no individual restrictions on undertakings *per se* contained in VDAs, the condition to be satisfied under the FCR Guideline, is whether “the agreement itself”, i.e. the VDA, is reasonably necessary to attain the efficiencies set out in the Application. This is indeed the case as both the market discussions and voluntary guidelines are necessary to attain the relevant efficiencies.
- 5.69 Market discussions improve service stability (e.g. by improved vessel deployment and promotion of investment). As explained above at paragraph 5.28, the sharing of public information is not directly equivalent to the more sensitive market information currently exchanged by carriers and is not a useful proxy or substitute for such information that could be used as a “less restrictive” means of promoting operational intelligence.
- 5.70 Pricing discussions mitigate against unsustainable rates and encourage rate stability and transparency. The use of rate guidelines is the only means by which the specific efficiencies of rate stability, rate and surcharge transparency can be achieved. The Commission proposes an example of promoting rate stability through shippers fixing contract rates, but this has not proved a popular option for shippers, despite the fact that it is currently available. Shippers locked into a fixed-rate contract would not be able to benefit from potentially advantageous movements in rate levels, from which their competitors in the float market could benefit. Clearly this could go both ways if rate levels were to increase on the float market, but shippers tend to demonstrate a preference for shorter-term negotiation of rates based on actual or projected near-term levels in the market. VDAs greatly assist in this regard as they provide both carriers and shippers with a line of sight over how the market is likely to move, rather than just historic movements of the sort provided by the SSE.

VDAs do not afford the undertakings concerned the possibility of eliminating competition in respect of a substantial part of the goods or services in question

- 5.71 Whilst the Commission appears to accept in the Statement that the fourth condition of the Efficiencies Exclusion criteria is met, it does not explicitly state this and its cursory examination of the fourth condition in the Statement does not reach a conclusion.
- 5.72 The Commission also makes the general supposition that “*certain aspects of VDAs may be considered to increase the likelihood that their members have the possibility to eliminate competition*”.³⁷ This is based on the general assertion from its FCR Guideline that pricing recommendations and discussions may be considered to have the object of harming competition, however, the Commission does not provide any specific evidence or examples of competition actually being harmed by VDAs. In fact, the Statement ignores the evidence provided by the HKLSA that there is strong competition in the *status quo* on the market, which is a convincing demonstration that VDAs do not afford carriers the possibility of restricting competition.

³⁷ Paragraph 4.125

- 5.73 According to the Commission's FCR Guideline, whether there is a possibility of competition being eliminated depends on the reduction in competition that the agreement brings about and the state of competition in the market. The weaker the state of existing competition in the market, the smaller any further reduction in competition would need to be for competition to be eliminated. Similarly, the more the relevant agreement causes harm to competition, the greater the likelihood that the undertakings concerned are afforded the possibility of eliminating competition.³⁸
- 5.74 In assessing VDAs against the above criteria, the Commission should be able to quickly draw the conclusion that there is currently strong competition on the market and that VDAs do not substantively weaken competition. VDAs have been present in Hong Kong for decades and in that time have clearly not given parties the possibility of eliminating effective competition in the market for liner shipping services, as evidenced by the current fragmented market, strong degree of existing competition and historically low rates (which are forecast to continue for the coming years). The Commission's lack of endorsement of the applicability of the fourth condition to VDAs ignores actual market dynamics.

6. Clarifications on surcharges

- 6.1 HKLSA would like to clarify the misconception, perpetuated in the Statement, that VDAs might in some way result in or promote the industry's imposition of surcharges. To be clear, with or without VDAs, carriers will impose surcharges as a necessary means of recovering their costs.
- 6.2 As a preliminary point, HKLSA notes that VDAs primarily focus on market discussions and GRIs; the majority of surcharges in the market are not discussed within VDAs and, even where they are, this seldom results in any actual action. Most surcharges are developed and imposed by individual carriers on their own and are in large part dictated by external factors entirely removed from the operation of liner shipping agreements.
- 6.3 Where formulae are given for surcharges by VDAs, e.g. Bunker Fuel Surcharges, they are drawn up to provide a fair and transparent mechanism for agreeing charges at a reasonable level so as to cover the costs associated with shipping, without adversely prejudicing shippers.
- 6.4 Furthermore, on the rare occasion when a surcharge is actually recommended by a VDA, the recommendation is entirely voluntary. The setting of surcharges, as with freight rates, is a commercial matter determined entirely through bilateral negotiations between a carrier and its customer. As such, all surcharges are fundamentally set by the market mechanism and agreed as part of wider contractual discussions.
- 6.5 The Commission has also ignored the example that HKLSA provided of occasions on which a discussion of surcharges in a VDA leads to no surcharge being

³⁸ Paragraph 2.19 of the Annex

recommended, in a situation where carriers might otherwise have charged one. As a result of exchanging views within VDAs, it can sometimes ultimately be decided that recommending a surcharge would not be practical. In this context, VDAs serve a useful purpose in enabling carriers to exchange information and seek others' views to help them reach better business decisions, without resulting in the recommendation of a surcharge.

- 6.6 Fundamentally, the Commission has not taken account of the fact that leaving VDAs outside of any block exemption in Hong Kong will not lead to a reduction or elimination of surcharges in Hong Kong. With or without a block exemption for VDAs, individual ocean carriers will continue, where necessary, to impose certain charges in order to recover their costs and maintain their business operations. This is a standard commercial practice in all ocean trades.

7. Conclusion

- 7.1 HKLSA trusts that the provision of the further data in relation to VSAs will assist the Commission in finalising its preliminary decision to grant a block exemption order for VSAs with a revision to the existing Conditions.
- 7.2 In relation to VDAs, HKLSA has further demonstrated in this submission that VDAs fulfil all the conditions for a block exemption order under the Efficiencies Exclusion. In addition, in the absence of any identified actual harm to competition, leaving VDAs outside the scope of the block exemption order altogether will unnecessarily deprive consumers in Hong Kong of substantial efficiencies/benefits. The Commission's preliminary views regarding VDAs risk harming competition, rather than protecting it.
- 7.3 HKLSA proposes to engage further with and support the Commission with any additional materials, particularly as regards the information exchange aspects of VDAs that might assist in reconsidering its preliminary views on VDAs, in light of information provided during the public consultation period.

CONFIDENTIAL ANNEX 1

Proportion of cargo carried by VSA partners vs. own ships

[...]

CONFIDENTIAL ANNEX 2
Cost savings to carriers participating in VSA alliances

[...]

CONFIDENTIAL ANNEX 3

Vessel size impact on slot cost

[...]

CONFIDENTIAL ANNEX 4
Expanded service offering available when entering into VSAs

[...]

CONFIDENTIAL ANNEX 5

Expanded service offering available when entering into VSAs - extract of example MoU

[...]