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The European Union – Korea Free Trade Agreement

AMEM Position Paper Shipbuilding & Marine Equipment Industry

Introduction

The Free Trade Agreement (FTA) between the European Union and the Republic of Korea is the first of a new generation of FTAs launched in 2007. The agreement consists of 15 Chapters, 3 protocols, several annexes and appendixes, and a number of understandings and joint declarations.

The FTA has been initialled in Brussels on 15th of October 2009 by the EU Trade Commissioner Catherine Margaret Ashton. All 27 countries that make up the European Union (European Council of Ministers) along with the EU Parliament (Lisbon Treaty) must approve the agreement before implementation.

Seen from the Austrian marine equipment manufacturers point of view this agreement is a disadvantage for the industry the association represents and must be improved. All hopes to achieve this goal are directed toward the European Parliament.

The Korean shipping, shipbuilding and marine equipment industry

Shipping

The country's shipping business has practically exploded in the past several years as the number of marine transport companies jumped from mere 73 in 2004 to 177 as of the end of last year. Also, the number of vessels almost doubled over the same period on the back of strong exports, from 471 to 819. More than 95 per cent of Korea's shipbuilding was for export at the beginning of the last decade. There was almost no Korean home market in shipping, while Japan for example had always a very strong fleet of commercial vessels. Even though the Korean economy has shown some signs of stabilizing in other areas, the

shipping industry is expected to have hard times due to enormous overcapacities. In this climate, many shippers struggle to stay afloat because of massive losses. Commercial lenders have curbed shipping loans as vessel prices have slumped to a four year low on plunging trade.

But the Korean Government and SOBs State Owned Banks are massively supporting this ailing industry via direct and indirect forms of financial aid.

Shipbuilding

The Republic of Korea considers itself to be at war – both militarily with the Democratic People’s Republic of Korea and economically with the rest of the world. Korea’s number one position in shipbuilding is at stake! The People’s Republic of China is in the process of overtaking South Korea in terms of order volume, becoming the world’s largest shipbuilding country! One could argue that China has won these orders thanks to low-cost shipbuilding, but this is where the rare orders are currently, while the order book for high value-added ships has almost dried out completely.

Nevertheless Korean shipyards have learned their lessons and are ready to bag every order for any object that floats on water or sits in the water like, wind power plants, at the most competitive price. To be more precise – at any price!

Korean shipbuilders are well supported by the Government and the large state as well as privately owned banks aggressively pursuing niche markets – the domain of

European shipbuilding! What is most crucial, they will not hesitate to take orders from the last niches of European shipbuilding dominance and the arch will span from dredgers, off-shore supply vessels, yachts, RoRos, ferries to cruise ships.

Since 1998, the largest volume in exports was either automobiles or semiconductors. But in 2008, shipbuilding was topping the charts with a volume of 43.157 million USD, followed by petrochemicals. Amazingly enough – Korea had reached one out of the three goals (shipbuilding, automotive and semiconductors) to become the world’s number one supplier in a typical segment of the “old economy”.

Korea’s shipyards, however, are bracing for another year of hardship as overcapacities continue to plague the global shipbuilding industry, with new orders scarce and ship financing still difficult.

To give only one example Hyundai, the world’s largest shipbuilder had suffered a 96 percent drop in new shipbuilding orders in 2009! The company received orders for 10 vessels, worth \$ 440 million, which is in sharp contrast to the previous year’s 109 vessels, and a combined value of \$ 13.6 billion.

Marine equipment

The financial crisis has been teaching us that even the largest companies were hit by the downturn. The critical mass argument does not hold any longer. It therefore looks as if the majority of the subsidies is directed to the huge conglomerates (chaebols), some

of them ailing and operating under Chapter 11 bankruptcy protection. The privately owned SMEs, in particular the thousands of marine equipment suppliers who suffer already from dry order books, cancellations and deferred payments, are by now confronted with a very critical situation! Credit guarantees by state-run funds for small and medium sized companies hit by the global financial crisis, will be extended until the end of the first half of 2010.

Creditors of eight midsized shipyards undergoing workout programs, plan to get these companies to move away from building complete ships and become components manufacturers.

Ironically enough, ailing DSME Daewoo Shipbuilding & Marine Engineering plus other companies and financial institutions have established a guarantee-fund for marine equipment suppliers.

Major industrial shipbuilding projects like the GFEZ Galsaman industrial cluster of shipbuilding in the Gwangyang bay area free economic zone in the South Jeolla province, have come to a standstill.

This hype driven green field investment was expected to be completed under the “3rd Sector Investment Type“ financing programme – what ever that means – by 2013.

Shipbuilding and marine equipment promotion legislation

Korea – the world’s leading shipbuilding nation – how a vision turned into reality

Since the second half of the 20th century shipbuilding has been suffering from the absence of rules and a tendency towards (state-supported) over-investment due to the fact that shipyards offer a wide range of technologies, employ a significant number of workers, and generate foreign currency income, as the shipbuilding market is both global and dollar-based. Shipbuilding was therefore an attractive industry for developing nations. Japan used shipbuilding in the 1950s and 1960s to rebuild its industrial structure. South Korea started to make shipbuilding a strategic industry in the 1970s, and the PR of China is now in the process of repeating these models with large state-supported investments.

As a result, the world shipbuilding market – with a few months of exceptions – suffers from overcapacities, depressed prices, low profit margins, trade distortions and widespread subsidisation.

The global shipbuilding industry is currently dominated by South Korea, which is by far the world’s largest shipbuilding nation and a leader in shipyard technology (block construction) and logistics. For example, the world’s largest shipyard in Ulsan,

operated by Hyundai Heavy Industries, slips a new-built, multi-million dollar vessel into the water every **four** working days!

The Korean Government identified shipbuilding as a strategic top priority industry for the enhancement of the nation's economy. To achieve this goal, late President PARK Chung Hee and the Government of the Republic of Korea established the Special Maritime Administration Committee to render consistent and uncompromising support to reach the goal of leadership in shipbuilding. The development model for the Korean shipbuilding industry is the product of a well orchestrated effort of the Korean Government, the large chaebols, state owned and private banks, entrepreneurs and a very skilled workforce.

Major milestones of shipbuilding promotion laws were

- Shipbuilding Promotion Law (1958)
- Shipbuilding Industry Encouragement Law (1967)
- Shipbuilding Industry Promotion Plan (1975)
- Industrial Development Law (1985)
- Shipbuilding Industry Rationalization Measurement (1989)

and in 2001:

- **“Act for the Promotion of the Component & Material Industries in Korea” – MCT Material & Component Technology 2010 Vision**

The Government of the Republic of Korea has openly announced a 10 Years plan in 2001 with a clearly defined target as an Act of State

“achieving higher than 90 per cent of domestic supply of components & equipment to the shipbuilding industry”

as part of the long term strategy, which was named MCT Material & Component Technology 2010 Vision. The MCT plan covered apart from shipbuilding other sectors of the manufacturing industry like general machinery, precision machinery, components for the automotive industry, rolling stocks, aerospace, electric products, metallic and non-metallic materials, chemicals, textiles and components for the telecommunication industry.

How was the situation in 2001?

Japan had been dominating the shipbuilding market since it took over the lead from Great Britain in the early fifties. European shipbuilders, Germany in the forefront were leaders in the high-tech sectors and so was the equipment industry. Heinrich Lübke, President of the Federal Republic of Germany had offered full technology support in raising the profile of Korean shipbuilding during a state visit to Korea in 1967. Germany is still the leading supplier of technology, know-how and marine equipment for the Korean shipbuilding industry.

How did Korea achieve these very demanding goals?

Taking advantage of a booming market whilst raising the level of technology and quality drastically via

- carrying on the further development of components and equipment imported over the years
- enhancing self-sustainability of those items that were in the stage of technology transfer
- upgrading technology and quality to international levels

What were the most challenging tasks?

- enhancement of the level of R&D activities, test and evaluation skills, and raising reliability of the work done by establishing a specialized institute for research and development of components and equipment for the shipbuilding industry, in other words copying materials, products and processes, strongly assisted by accredited laboratories, test institutes and classification societies
- creation of a friendly environment for joint ventures, tie-ups and all forms of collaboration
- development of core components with high added value
- development of dual use products – commercial and military navy – in close cooperation with both segments of shipbuilding

- expansion into overseas markets by establishing an integrated after sales network
- setting up investments in a strong shipbuilding industry cluster
- building mega-sized shipyards and integrated diesel engine manufacturing plants equipped with advanced production facilities and equipment
- training of a skilled, professional and educated work force

What are the reasons to classify the Korean Government's MCT Vision 2010 as a trade barrier?

Well,

- it is a severe discrimination between trading partners
- it is a brutal injustice as imported and locally produced goods are not treated equally
- it is a camouflaged import ban, a barrier against foreign products and services
- it describes exactly the opposite of an open market philosophy
- it is paving the way for unfair, and distorted competition

It would be the purest cynicism to sign the EU-KOREA FTA Free Trade Agreement in 2010, in the very same year the MCT Vision was focussing on!

State aid to the shipbuilding and marine equipment manufacturing industry

FTA, Chapter 11, Section B Subsidies

The Korean Government has not only a long lasting and well established experience and expertise in subsidising its number one industry – shipbuilding. It has also the necessary punch and strong will to defend these trade practices which contradict the WTO's Subsidies Agreements, Korea has signed. Policymakers and central bankers support the strategy of continued expansionary fiscal and monetary policies, vowing to facilitate the industry's recovery through aggressive fiscal spending, low borrowing costs and other pump-priming steps.

“Commando-capitalism” is forcing Korea's SOBs state-owned banks like KEXIM Korea Export-Import Bank, KAMCO Korea Asset Management Corporation or KDB Korea Development Bank, to assist shipping companies pay for new vessels and shipbuilders to sell ships for less than construction cost.

The Korean Government is in the process of using parts of its massive foreign currency reserves – an all time high \$270 billion – and national wealth to offer major credit support and other financial aid, primarily

backed by state-run banks, to the nation's shipbuilders.

Safeguarding of jobs might be a convincing argument when looking at these massive subsidies financed from the taxpayers pocket, nevertheless it is in strong contrast with Korea's membership in organisations like WTO and OECD and their principles! However, so be it, one could develop some understanding for this kind of state aid, but not for a simultaneous export promotion campaign financed from the same sources! This is definitely destroying any sense for fair competition and a level playing field – if any existed!

Here are a few examples:

Korea Asset Management Corporation KAMCO

The Corporate Restructuring Fund with an initial volume of 20 billion is intended to buy idle vessels from shippers or financial companies in order to help them to cope with short-term liquidity problems. The KAMCO is currently purchasing vessels through its fund, which will be increased to as much as 4 trillion Won!

Korea Development Bank KDB

Shipping fund up to 2 billion won based on the “sell and lease” principle. KDB has received proposals to help finance at least 44 ships.

Korea Export Insurance Corporation

A package of 500 billion won loans to shipyards to build and launch new ships was offered.

Export-Import Bank of Korea EIB

500 billion Won (USD 432 million) in loans to the shipbuilding industry to help develop new vessels were planned to be provided.

Bad Bank

6 privately owned banks – Kookmin, Shinhan, Hana, Woori, Industrial Bank of Korea and Nongyup have founded a “bad bank”.

Resumee

The dispute on illegal yard aid in Korea has been rumbling on in one form or another on WTO, OECD and European levels since the late 1990s. Not only the CESA Committee of European Shipbuilders Association’s initiative should be mentioned in this context, but also the fact that Pascal Lamy has shared all the discussions both in his function as EU Trade Commissioner and as Director General of WTO over a period of almost 10 years!

Europe’s shipbuilding and marine equipment industries might have accommodated to the unfair trade practices in daily day life.

But AMEM does not want to stay mute! Although the smallest association of marine equipment suppliers in Europe, AMEM can’t develop an understanding for the European Commission’s initialling a Free Trade Agreement with the Republic of Korea in general and the Chapter 11, Competition and Subsidies in particular, being fully aware about the fact that this form of direct and indirect state aid is not only illegal, has a distortive effect, constitutes an unfair

practise and forms a massive obstacle for settling such an Agreement!

The current text of the Agreement gives an unfair advantage to the Korean shipbuilding and marine equipment industry and sets a dangerous precedent for FTAs between the EU and other major trading partners.

In the light of the worst crisis in European shipbuilding, it must be feared that an import surge from Korea will occur. AMEM likes to join forces both with industry and unions being extremely concerned about the fact that the FTA would further deteriorate the already difficult situation in the European shipbuilding and marine equipment manufacturing industry, where it might result in significant losses of jobs and contribute to a silent exodus of companies from the marine market!

See Attachment
OECD WP6 Shipbuilding
(page 12-15)

The Social Aspect

An unchanged Free Trade Agreement with Korea will conflict with the European Parliament's topping agenda – the creation of jobs as a major element of the exit strategy from the recession with skyrocketing unemployment figures in many areas of Europe – both West and East!

An unchanged Free Trade Agreement with Korea will also conflict with the major priority issues of the Spanish Presidency of the European Union as outlined in the speech of Jose Luis Rodriguez Zapatero at the plenary session of the European Parliament on January 20, 2010. With regard to social cohesion, Zapatero stated very clearly that this economic crisis is the most serious crisis, Europe has suffered for eighty years! The most serious effect it has caused: eight million more people without jobs, many of them in Zapatero's own country! This has an effect on public accounts and as a consequence of that, on the financial stability of the Euro zone! Zapatero concludes – we now need new sources of growth to replace the jobs lost in the crisis!

The FTA with Korea might contribute to an additional trade obstacle!

Zapatero being a Spaniard and being familiar with the situation in the Spanish shipbuilding industry, should develop a proper understanding not only for the sectoral but also for the regional dimension! It should not be too big a problem for him to communicate that to the chief negotiator of the FTA his fellow countryman (compañero) Ignacio Garcia Bercero.

Europe does not need a smarter, greener social market, it simply needs a responsible-minded social policy, as a joint European strategy to manage the social crisis was absent until now! US President Barack Obama has learned his lesson in Copenhagen: people who are so strongly hit by an economic crisis care about jobs first, and are relatively immune to environmental issues and smart strategies for achieving world governance! Internationalising Europe's mature marine equipment manufacturing industry – the majority of enterprises being SMEs – is not the order of the day! They have been acting internationally since decades if not centuries!

The economic importance of the maritime cluster in Europe is best reflected by the fact that in this sector more than 1.3 million people generate an added value of € 70 billion, according to EMF European Metalworkers' Federation findings.

The EMF is the representative body defending the interests of workers in the European metal industry. The EMF has a mandate for the external representation of the metalworkers' union and a mandate to engage in bargaining at European level.

The EMF Shipbuilding Committee has developed its own strategies for the shipbuilding sector within the context of an overall European maritime policy in order to ensure a competitive industry with high levels of high quality employment. Representatives from the key European shipbuilding nations – France, Italy, Germany, Finland, Spain, the Netherlands, Denmark, Norway and Great Britain – were discussing the consequences of the financial

and economic crisis of the European shipyards on the 25th and 26th of June 2009 in Berlin.

At the end of this conference the so called “Berlin Declaration” was adopted featuring the motto:

**Avoid Redundancies –
Safeguard Competitiveness –
Enter New Markets**

In a letter sent to President Barroso with regard to the FTA EU – KOREA in September 2009, EMF General Secretary Peter Scherrer stated that an agreement reached with partners who do not fully respect human and trade union rights and which, in addition, is unbalanced in terms of economic benefit, should not be concluded.

The economic indicators showed very clearly that economic gains for the European Union were small and that the FTA was imbalanced! The EMF had drawn the European Commission’s attention to the possible negative effects the draft for the FTA could have. Admittedly shipbuilding was overshadowed by the automobile industry at that time.

In the light of a continuation of a very dull order entry – if any – in European shipyards, and progressively increasing numbers of unemployed workers, it is most likely that other forces will be joining AMEM.

The Regional Aspect

The effects of any economic and financial crisis in European shipbuilding are first felt at local and regional levels as shipyards are located along the coast lines of a country, quite often in less developed areas, thus representing the single, major employer in the region. The crisis bears the overwhelming risk of unemployment reaching 27 million by spring 2010! European citizens expect the new European leadership to focus on jobs and to respond to tomorrow’s social challenges. This can only be achieved in a bottom-up process between the European Institutions and national, regional and local governments!

The Committee of the Regions (CoR), the EU’s Assembly of regional and local representatives provides institutional representation for all the European Union’s territorial areas, regions, cities and municipalities. The European Union’s maritime policy will have to focus more on the interface between land and sea and on promoting sustainable maritime competitiveness. This will only be achieved with the full involvement of local and regional authorities. Cooperation with the Committee of the Regions, the European Parliament’s Committee on Regional Development (REGI) and Directorate General for Regional Policy (DG REGIO Commissioner Johannes Hahn, Austria), will be a prerequisite to strengthen economic, social and territorial cohesion, thus giving an important expression of the EU’s solidarity.

Conclusion

Progressive trade opening accompanied by fair and transparent conditions following the principle of a plain level playing field, are legitimate policy objectives. New Free Trade Agreements therefore could quite well serve as a stepping stones for multilateral liberalisation. Free Trade Agreements are considered to contribute substantially to the goal of stimulating growth and creating jobs in Europe as long as they are not negotiated on an unbalanced level and abused as an instrument for the expansion of global governance! In combination with non effective protection and enforcement of the intellectual property, they become a threat to suppliers of high technology products and systems. To make it perfectly clear: European shipbuilding, marine equipment and services are high-tech industries, they are much more complex than aerospace!

Growth and jobs were at the heart of the European Commission's renewed Lisbon Agenda. The core criterion by which citizens judge whether Europe is delivering positive results in their daily lives is at stake! European citizens expect to see such positive results from economic and structural changes. Economic and structural changes are not new to the European shipbuilding and marine equipment manufacturing community, as shipping and shipbuilding since centuries were global and European companies have been adjusting themselves to ever changing competition patterns. Global supply chains were established as a result of outsourcing parts of the production to lower cost economies.

Seen from the Austrian marine equipment manufacturers' point of view, the European Commission's Free Trade Agreement with Korea in its present form, should not pass the European Parliament, the only direct-elected body of the European Union, among others because of the "local content" legislation in Korea, which will have severe consequences on jobs in the entire shipbuilding and marine equipment industry of Europe!

In addition to this social aspect, the European Union – Republic of Korea Free Trade Agreement will not only be sharply felt in particular sectors of the European industry, to mention only the automotive industry apart from marine equipment, but also in particular in mostly less developed regions of Europe and their workforce, as thousands of jobless feed political opposition to open trade and foster social unrest!

EU - South Korea free trade agreement (debate)



Current speaker

Regner Evelyn
 Group of the Progressive Alliance of Socialists and Democrats in the European Parliament
 Republic of Austria

+ Additional information
 See profile of this speaker

Speakers on this subject

Zalewski Pawel	22:58:50
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EU – South Korea free trade agreement (debate) · Wednesday 10 February 2010
<http://www.europarl.europa.eu/wps-europarl-internet/faces/vod/research-by-date.jsp>

The FTA Free Trade Agreement between the European Union and the Republic of Korea was debated in the plenary of the EU Parliament due to an oral question of the committee on International Trade of the European Parliament on Wednesday, 10th of February 2010 late in the evening.

The majority of the speakers were addressing deficiencies in the agreement. As long as these weaknesses were not sorted out satisfactorily, the EU Parliament should not ratify the FTA with Korea. Mister Gianluca Susta from the Progressive Alliance of Socialists and Democrats, Italian Republic, summarized the most critical sectors of the industry mentioned by his previous speakers as follows

- automobiles
- electronics
- textiles

A speaker from a landlocked country – Austria – MEP Evelyn Regner, was drawing the attention of the Commissioner Karel van Gucht, Vice-President Miguel Angel Martínez Martínez and her colleagues in a 1.5 minute contribution to the debate when she said:

“Ein weiterer bis jetzt noch nicht so beleuchteter Sektor ist der Schiffbau, mit dem es Probleme gibt. Korea hat es sich in einem 10-Jahresplan – in einem „Act of State“ – zum Ziel gesetzt, dass mehr als 90 Prozent der Zulieferindustrie für den koreanischen Schiffbau aus Korea stammen sollten, was es sehr, sehr schwierig für europäische Mitbewerber und insbesondere auch für die Beschäftigten in diesem Sektor macht.“

OECD Inventory of Support Measures in the Shipbuilding Industry Republic of South Korea

Source: OECD WP6 Shipbuilding

Measure	Description	Responsible Authority	Beneficiary
Pre-shipment loans to Korean shipyards	6-12 month pre-shipment loans provided to Korean shipyards for the construction of vessels.	The Export-Import Bank of Korea (KEXIM)	USD 2.2 bn committed under the scheme in 2009. USD 480 m committed in 2008
“Let’s Go Together Shipping Programme”	The fund operates under a “sale and lease back” scheme for second hand vessels and newbuildings	KAMCO (Korea Asset Management Corporation) USD 3 bn	62 vessels for 16 companies
		KDB (Korea Development Bank) USD 1.72 bn	17 vessels for 5 owners in 1st phase
Funds for exports	USD 1.19 bn to sustain exports from SK yards to avoid cancellations (Seatrade Asia Sept. 2008)	KEXIM (Korea EXport IMport Bank)	(4) LNG and (2) container-vessels from SHI, STX see next page >>>

Measure	Description	Responsible Authority	Beneficiary
<p>Buy and lease back USD 3 bn scheme</p>	<p>Buy and lease back vessels from local owners; Providing refund guarantees for shipbuilders and loans for owners</p>	<p>KDB, KEXIM KEIC (Korea Export Insurance Corporation)</p>	
<p>Government Package to assist shipping and shipbuilding WON 21 trn EUR 12 bn</p>	<p>WON 9.5 trn EUR 5.4 bn in loans and guarantees for blue-chip yards, small and medium size shipyards and their subcontractors</p>	<p>KEXIM KEIC</p>	<p>see next page >>></p>
<p>WON 11.5 trn EUR 6.6 bn in direct loans and “debt guarantees” to shipowners to build at Korean yards (Kaiji Press, May 2009)</p>			

Measure	Description	Responsible Authority	Beneficiary
<p>Liquidity supply programme for shipbuilders similar to construction companies (Lloyds List, Nov. 2008)</p>	<p>Providing liquidity under certain conditions – creditor banks will roll over debt for 12 months.</p>	<p>Korean Gov.</p>	<p>Local shipbuilders and shipowners</p>
<p>FAST TRACK Programme</p>	<p>Assesment of yards and classification into A, B, C, D categories: provide assistance only to A- and B- “viable” yards. Under the scheme, the shipbuilders will enter into an agreement with the creditor banks to have the debt rescheduled or receive new loans.</p>	<p>Korea Federation of Banks and Financial Services Commission</p>	<p>C category: NokBong, Jinse, TKS and SEKO – to undergo “workout” procedures</p> <p>D category: YS Heavy Industries, C&Heavy Industries – withdrawal from the market</p> <p>see next page >>></p>

Measure	Description	Responsible Authority	Beneficiary
Debt rescheduling programme WON ~ 240 billion	Feb. 2009 WON 70 bn in emergency operating funds from creditors PLUS funding WON 170 bn from KDB only KDB MoU: defer the settlement of obligation until 2013; provide interest exemptions and reductions.		Daehan SB
Workout programme and debt rescheduling programme	WON 35 bn “pumped” in August 2009 Debt rescheduling programme ~ WON 45 bn in December 2009 or January 2010		21 st Century Shipbuilding
Galsaman Reclaimed Land The Project for the development of Galsaman Industrial Cluster of Shipbuilding	The Development Project of Industrial Shipbuilding Cluster in Galsaman, Hadong District, Gwangyang Bay Area Free Economic Zone	Amended by AMEM on the 6 th of April 2010: <ul style="list-style-type: none"> ▶ Ministry of Knowledge Economy Free Economic Zone Planning Task Force www.gfez.go.kr ▶ Gwangyang Bay Area Free Economic Zone Authority ▶ Galsaman Industrial Cluster of Shipbuilding 	