CASE BE/0004

DECISION TO VARY (RENEW) THE COMPETITION (BLOCK EXEMPTION FOR VESSEL SHARING AGREEMENTS) ORDER 2017

NOTICE OF VARIATION

7 JULY 2022

競爭事務委員會 COMPETITION COMMISSION

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I. INTRODUCTION AND EXECUTIVE SUMMARY

1. On 8 August 2017, the Competition Commission ("**Commission**") issued the Competition (Block Exemption For Vessel Sharing Agreements) Order 2017 ("**Order**") pursuant to section 15 of the Competition Ordinance (Cap. 619) ("**Ordinance**").

2. The Order declares that certain activities of vessel sharing agreements between liner shipping companies ("**VSAs**") are excluded agreements, which means that those activities satisfy the exclusion from the first conduct rule for agreements enhancing overall economic efficiency ("**efficiency exclusion**") in section 1 of Schedule 1 to the Ordinance.

3. The Order, a Guidance Note explaining its terms, and a Statement of Reasons detailing the basis for the issuance of the Order, are available on the Block Exemption Orders Register on the Commission's website.

4. The Order is due to expire on 8 August 2022. It specifies that the Commission shall commence a review of the Order no later than 8 August 2021 ("**Review**").

5. On 5 August 2021, the Commission commenced the Review by launching an initial consultation and subsequently pursued various avenues of assessment. The purpose of the Review was to inform the Commission's decision on whether to renew the Order, renew the Order subject to amendments, or let the Order expire.

6. On 5 May 2022, at the conclusion of the Review, the Commission published a notice which set out the Commission's proposal to renew the Order on the same terms for a period of four years, pursuant to the variation process in section 20 of the Ordinance ("**S.20 Notice**").[1] This launched a public consultation on the proposal and invited interested parties to submit representations ("**S.20 Consultation**").

7. The Commission has carefully reviewed the representations received in the S.20 Consultation and considers that they generally support the findings and conclusions from the Review. Accordingly, the Commission has decided to renew the Order for a period of four years, as proposed in the S.20 Notice.

[1] See the Notice issued under section 20(2) of the Competition Ordinance (Cap. 619), *Commission Proposal to Vary (Renew) the Competition (Block Exemption for Vessel Sharing Agreements) Order 2017*, available on the Commission's website.

8. To achieve the renewal, the Commission has varied the expiry date and the review periods in the Order pursuant to the variation procedure set out in section 20 of the Ordinance.

9. This variation is effected by the Competition (Block Exemption for Vessel Sharing Agreements) (Variation) Order 2022 ("**Variation Order**"), which is published to the Commission's Block Exemption Orders Register available on the Commission's website and at its offices during ordinary business hours.

10. In accordance with the Commission's Guideline on Applications for a Decision under Sections 9 and 24 (Exclusions and Exemptions) and Section 15 Block Exemption Orders, the Commission issues this Notice of Variation to explain the reasons for the variation.[2] The remainder of this Notice of Variation sets out:

    (a) an overview of the Order (Part II);

    (b) details of the Review and the S.20 Consultation conducted by the Commission (Part III);

    (c) the Commission's findings on relevant developments since the issuance of the Order (Part IV);

    (d) the basis for the Commission's variation (renewal) of the Order (Part V); and

    (e) details of the variation (renewal) of the Order (Part VI).

II. OVERVIEW OF THE ORDER

11. The Order concerns VSAs, which are defined in paragraph (5) of the Order as "*an agreement or a set of interrelated agreements between liner operators in which the parties to such agreement or agreements discuss and agree on operational arrangements relating to the provision of liner shipping services, including the coordination or joint operation of vessel services, and the exchange or charter of vessel spac*e".

[2] Guideline on Applications for a Decision under Sections 9 and 24 (Exclusions and Exemptions) and Section 15 Block Exemption Orders, paragraph 14.8.

12. The following activities of VSAs have benefited from exemption from the first conduct rule pursuant to paragraph (6) of the Order since the issuance of the Order in August 2017:

    (a) the joint operation of liner shipping services including any of the following activities: (i) the coordination and/or joint fixing of sailing timetables and the determination of ports of call; (ii) the exchange, sale or cross-chartering of space or slots on vessels; (iii) the pooling of vessels and/or port installations; (iv) the use of one or more joint operations offices; (v) the provision of containers, chassis and other equipment and/or the rental, leasing or purchase contracts for such equipment;

    (b) capacity adjustments in response to fluctuations in supply and demand, which may be necessary for the operation of a joint service;

    (c) the joint operation or use of port terminals and related services; and

    (d) any other activity ancillary to those referred to in (a), (b) or (c) above and which is necessary for their implementation.

13. Such exemption is subject to certain conditions in paragraphs (7) and (8) of the Order, including that:

    (a) the parties to a VSA do not hold in a market a combined market share of more than 40% (or more than 45% for a period not exceeding two consecutive years) ("**market share limit**"); and

    (b) the agreement does not authorise or require price fixing, limiting capacity or the allocation of markets or customers.

14. The Guidance Note accompanying the Order provides further details on the Commission's interpretation of the Order's provisions, including guidance on market definition and the calculation of market shares for the purposes of the market share limit.[3]

[3] The Commission has published a slightly updated version of the Guidance Note along with this Notice of Variation (though the guidance it contains is unchanged in substance).

III. DETAILS OF THE REVIEW AND THE S.20 CONSULTATION

The Review

15. In the Review, the Commission conducted an initial consultation seeking information, views and evidence from interested parties on a series of issues, including on market and other developments since the issuance of the Order, to assist it to formulate a proposal on the future of the Order.[4]

16. The respondents to the initial consultation included local, regional and global liner shipping industry associations, industry associations representing shippers, port operators and ship owners; chambers of commerce; a legislator; and governmental and public bodies.

17. In the 18 submissions received:

(a) 13 respondents expressly supported the renewal of the Order;

(b) five respondents did not indicate whether or not they supported the renewal of the Order; and

(c) none of the respondents opposed the renewal of the Order.[5]

18. In addition to this initial consultation, the Commission benefited from, among others, industry data and analytics gathered by an independent industry expert appointed by the Commission for the Review (BMT Asia Pacific); discussions with counterpart authorities responsible for enforcement of competition law in the liner shipping industry; meetings with key industry representatives; and responses to the Commission's requests for information submitted by the Hong Kong Liner Shipping Association ("**HKLSA**") (which submitted the original application for a block exemption order in this matter).

S. 20 Consultation

19. Based on the Review, the Commission provisionally concluded that the basis upon which the Order was issued remained satisfied (i.e., that VSAs within the scope of the Order continue to satisfy the four cumulative conditions of the efficiency exclusion) and that the

[4] See the Notice of Commission initial consultation regarding the review of the Competition (Block Exemption for Vessel Sharing Agreements) Order 2017, available on the Commission's website.
[5] The Commission also refers to relevant points from the submissions in Parts IV and V of this Notice of Variation.

Order continued to be merited and effective. This finding was further outlined in the S.20 Notice.

20. In response to the S.20 Notice, the Commission received 11 representations, which have been published on the Commission's website.[6]

21. Eight representations were fully supportive of the Commission's proposal and did not raise any issue requiring further discussion.

22. The remaining three representations were supportive of the Commission's proposal but raised a limited number of concerns, namely those from the Hong Kong Container Terminal Operators Association Limited ("**HKCTOA**"), Hong Kong General Chamber of Commerce ("**HKGCC**"), and Hong Kong Shippers' Council ("**HKSC**"). These issues are addressed more specifically below,[7] but do not cause the Commission to change its position as expressed in the S.20 Notice.

23. The remainder of this Notice of Variation sets out the findings from the Review, supplemented with discussion of any points raised in the S.20 Consultation. Where no respondent to the S.20 Consultation raised any contrary views or otherwise discussed the Commission's provisional findings from the Review, the Commission has adopted those findings as its final findings in this Notice.

IV. FINDINGS ON RELEVANT DEVELOPMENTS SINCE THE ISSUANCE OF THE ORDER

24. This section sets out the Commission's findings on developments since the issuance of the Order in relation to:

   (a) VSAs;

   (b) exemptions from competition law for liner shipping agreements in other jurisdictions;

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[6] The representations were from the following organisations: The Hong Kong Shippers' Council; Hong Kong Container Terminal Operators Association Limited; A.P. Moller – Maersk; HKLSA; World Shipping Council; Asian Shipowners' Association; Hong Kong Shipowners Association Ltd; Transport and Housing Bureau; The Hong Kong General Chamber of Commerce; The American Chamber of Commerce in Hong Kong; and International Chamber of Shipping.

[7] See paragraphs 52 to 58 (regarding market composition), paragraph 78 (regarding the fair share condition), paragraphs 82 to 86 (regarding the market share limit), and paragraphs 99 to 101 (regarding the duration of the Order) of this Notice of Variation.

(c) developments in the liner shipping market since the issuance of the Order (including those related to the COVID-19 pandemic); and

(d) other matters raised by interested parties.

(a) VSAs

Form and terms of VSAs

25. Based on the information and views obtained in the Review, the Commission has reached the finding that the form and terms of VSAs today are fundamentally the same as they were when the Order was issued.

26. In particular, VSAs continue to consist of agreements on operational arrangements relating to the provision of liner shipping services, ranging from simple agreements to purchase or reciprocally exchange capacity between members of the VSA, to more extensive agreements to coordinate the parties' respective sailing schedules and port calls and/or operate a joint service through pooling of vessels. In addition, VSAs in the form of 'alliances' continue to be in use, which cover multiple trade routes rather than one trade, so that liner operators manage several joint shipping services worldwide.[8]

27. VSAs also continue not to authorise joint marketing or pricing of services.[9] The information and views gathered by the Commission, including from users of liner shipping services, suggest that VSA members still compete with each other (as well as with non-VSA members) on price and other competitive parameters such as customer service.

Usage of VSAs in Hong Kong

28. VSAs have continued to be widely used by shipping lines providing services calling at Hong Kong since the issuance of the Order.

29. As set out in the following table, the liner shipping services calling at Hong Kong are, in the large majority, operated under VSAs.

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[8] See Statement of Reasons, paragraphs 2.27 to 2.30.
[9] See Statement of Reasons, paragraph 4.11.

Table 1: Proportion of services calling at Hong Kong operated under VSAs (2021)

Trade	Number of services	Services operated under VSAs	Percentage of VSA services
Transpacific	16	15	93.8%
Asia to Europe	7	7	100%
Asia to Australia / New Zealand	[●]	[●]	[80-90%]
Intra-Asia	[●]	[●]	[70-80%]
Others	[●]	[●]	[80-90%]
Total services calling at Hong Kong	[●]	[●]	**[80-90%]**

Source: Commission calculations based on BMT Asia Pacific analysis and data provided confidentially by HKSLA

(b) Exemption of liner shipping agreements from competition law in other jurisdictions

30. As noted in the Statement of Reasons accompanying the Order, a number of other jurisdictions offer exemptions from competition law for liner shipping agreements, which presently include Australia, Canada, the European Union, Israel, Japan, Malaysia, New Zealand, Singapore, South Korea and the US.[10]

31. Since the issuance of the Order, these jurisdictions have maintained, issued or, following a review, renewed their exemptions for VSAs (subject to certain conditions). The jurisdictions which have issued or reviewed an exemption include the following:

(a) **Malaysia:** In 2019, the Malaysia Competition Commission issued its third block exemption order for certain VSAs, for a period of three years,[11] following the expiry of its second block exemption order and a public consultation.

(b) **European Union:** In 2020, the European Commission renewed the Consortia Block Exemption Regulation for another four years until 25 April 2024.[12]

[10] Statement of Reasons, Part 3. With respect to India, the Commission understands that the prevailing exemption for VSAs expired in 2021 and is currently under review.
[11] See Gazette No. P.U. (A) 314/2019: Competition (Block Exemption for Vessel Sharing Agreements in Respect of Liner Shipping Services through Transportation by Sea) Order 2019.
[12] See Commission Regulation (EU) 2020/436 of 24 March 2020 amending Regulation (EC) No. 906/2009 as regards its period of application; and European Commission, Press release, *Antitrust: Commission prolongs the validity of block exemption for liner shipping consortia*, 24 March 2020.

(c) **Singapore:** In 2021, following the recommendation from the Competition and Consumer Commission of Singapore, the Minister for Trade and Industry, extended Singapore's block exemption order for three years from 1 January 2022 to 31 December 2024, covering VSAs and price discussion agreements between feeder services.[13]

(d) **Australia:** The Australian Competition and Consumer Commission has proposed to develop a class exemption for liner shipping agreements that meet a minimum standard of pro-competitive features, which would replace the existing broad exemption for liner shipping agreements under Part X of the Competition and Consumer Act 2010.[14] The proposal is currently under consideration.

(e) **New Zealand:** In 2019, New Zealand repealed the broad exemption for liner shipping agreements in the Commerce Act 1986 and replaced it with a narrower exemption to permit vessel sharing activities.[15]

(c) Developments in the liner shipping market since the issuance of the Order

<u>COVID-19 pandemic</u>

32. As has been widely reported, the COVID-19 pandemic has caused severe disruption to the global supply chain since its onset in March 2020. Among other issues, there have been:

(a) **Significant changes in demand**. The first half of 2020 was characterised by a sharp drop in consumer demand due to, among other reasons, the introduction of lockdowns in many jurisdictions. From around the third quarter of 2020 to the date of this notice, demand has recovered and there has been sustained levels of high demand. This has included a significant increase in demand for recreational goods and electronics being shipped from Asia to the US and Europe, exacerbating trade imbalances.

(b) **Congestion at the ports and inland**. The significant increase in demand during the pandemic has led to increased amounts of vessels and cargo at ports, while at the same time there have been labour shortages due to illness and quarantine

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[13] See Competition (Block Exemption for Liner Shipping Agreements) (Amendment) Order 2021; Competition and Consumer Commission Singapore, Press Release, *CCCS Recommends Three-Year Extension of the Block Exemption Order for Certain Liner Shipping Agreements*, 15 November 2021.

[14] See ACCC, Class exemptions register, *Ocean Liner Shipping Class Exemption*, 3 December 2019.

[15] See Commerce Act 1986, sections 44A and 44B.

requirements as well as occasional port closures. Lack of trucks, railcars and storage space have also resulted in congestion for inland transportation of cargo. Though not related to the pandemic, the blockage of the Suez Canal after the grounding of a container vessels for six days in March 2021 also exacerbated congestion issues.

(c) **Container shortages**. Container production was initially reduced in the first half of 2020 due to the impact of COVID-19 in Asia. In addition, due to fewer shipments back to Asia, empty containers remained in North America and Europe, and were not transported back to Asia for re-use for exports.

33. During the pandemic period, the liner shipping industry has been and continues to be characterised by exceptionally high freight rates and additional surcharges, and by increased delays and reduced service reliability. Several industry bodies raised concerns around these developments during the initial consultation.

34. In the Review, the Commission carefully considered whether these developments have been caused or exacerbated by VSAs or more generally by collusion by shipping lines (for example, by shipping lines agreeing in the context of VSAs or elsewhere to deliberately withhold capacity or skip port calls to achieve higher freight rates). If that were the case, it would call into question the continued appropriateness of the Order.

35. The Commission notes the following information and views which it obtained in the Review:

(a) Several organisations, including users of liner shipping services, opined to the Commission that the current market issues were the result of exceptional circumstances beyond the shipping lines' control and did not refer to any specific collusive action by shipping lines (whether or not through VSAs) during the pandemic aimed at achieving higher rates.

(b) The information and data obtained in the Review suggest that shipping lines have added capacity and services to certain trades during the pandemic, particularly the Transpacific and Asia to Europe trades, that vessel utilisation remains high, and that the number of new ships being ordered has increased (see further paragraphs 40 to 43 below). This would not be consistent with a collusive attempt to obtain higher rates by deliberately withholding capacity.

(c) As noted in paragraph 27 above, the information and views gathered during the Review suggest that, while members of VSAs may offer their services jointly, they continue to compete on other competitive parameters such as price and customer service with each other and with non-VSA members. The Order does not in any event authorise VSA members to coordinate on price.

(d) Finally, it was suggested to the Commission that VSAs may contribute to the port congestion which has been seen in the pandemic, since they allow the use of larger vessels and concentrate the services of the VSA parties on a smaller number of ports. While this thesis appears plausible to the Commission, it is also possible that VSAs would alleviate port congestion by permitting the use of a smaller number of vessels (albeit larger ones) and the joint use of particular port terminals. More generally, the reasons for port congestion would appear to vary depending on the specific infrastructure of the port. As such, the Commission has been unable to verify the suggested link between VSAs and port congestion.

36. None of the representations in the S.20 Consultation provided evidence suggesting that the market developments during the pandemic (as described in paragraphs 32 and 33 above) were caused or exacerbated by VSAs or more generally by collusion by shipping lines. Certain representations sought to demonstrate that VSAs had alleviated the negative impacts of the pandemic,[16] though the Commission does not make any finding on this.

37. In light of the foregoing, the Commission has reached the finding that, while the market developments during the pandemic are concerning, they do not cast doubt on the appropriateness of the Order itself. The Commission will in any event remain alert for any evidence that VSAs or more generally collusion by shipping lines are causing or exacerbating the current issues in the liner shipping market.

<u>Market conditions</u>

38. During the Review, the Commission obtained data on market conditions since the issuance of the Order from BMT Asia Pacific, the industry expert appointed by the Commission for the purposes of the Review.

39. In light of the developments described in the previous section, it is necessary to

[16] See the representations from the HKLSA, 31 May 2022, and the International Chamber of Shipping, 6 June 2022.

distinguish between (i) the period following the issuance of the Order but prior to the onset of the COVID-19 pandemic, from August 2017 to the fourth quarter of 2019 ("**pre-pandemic period**"); and (ii) the period since the onset of the pandemic, from the first quarter of 2020 to present ("**pandemic period**"). In its representation, the HKSC agreed that such a distinction was appropriate.[17]

Service provision, capacity and deployment

40. In Tables 2 and 3 below, the Commission sets out information relevant to service provision, capacity and deployment on the Transpacific and Asia to Europe trades, shortly prior to and since the issuance of the Order.[18]

Table 2: Service provision, capacity and deployment on Transpacific trade (2016 to 2021)

	2016	2017	2018	2019	2020	2021
No of Weekly Services	58	58	56	57	58	84
Of which VSAs	47	48	48	48	49	52
Annual Shipping Capacity (Million TEU[19])	15.4	16.1	16.9	16.7	17.2	22.0
No. of Weekly Services Calling At Hong Kong	21	21	22	19	16	16
Of which VSAs	19	19	20	18	15	15
Service Frequency – Weekly Direct Calls at Hong Kong	26	25	22	20	17	20
Weekly Liner Shipping Capacity Deployed at Hong Kong	194,423	189,665	209,419	188,382	181,820	174,120
Service Coverage – No. of Destinations in N. America	17	17	18	20	19	17
Connectivity – No. of Weekly Direct Transits to Destinations in N. America	55	57	60	52	45	37
Annually Blanked Capacity (TEU)	337,290	361,893	309,278	362,465	561,464	790,509

Source: BMT Asia Pacific analysis

[17] Representation from the HKSC, 18 May 2022.

[18] The information obtained by the Commission in the Review suggests that other trades involving Hong Kong (such as intra-Asia) tend to be considerably more fragmented and thus less likely to give rise to competition concerns. As such, the data obtained by the Commission focuses on the two largest trades involving Hong Kong (the Transpacific and Asia to Europe trades).

[19] 'TEU' refers to Twenty Foot Equivalent Unit and is the standard size of a 20 feet long container.

Table 3: Service provision, capacity and deployment on Asia to Europe trade (2016 to 2021)

	2016	2017	2018	2019	2020	2021
No of Weekly Services	31	33	32	30	29	32
Of which VSAs	30	30	29	30	29	30
Annual Shipping Capacity (Million TEU)	17.1	17.1	18.0	18.2	16.6	20.2
No. of Weekly Services Calling At Hong Kong	11	8	9	8	8	7
Of which VSAs	11	8	8	8	8	7
Service Frequency – Weekly Direct Calls at Hong Kong	14	10	12	9	12	9
Weekly Liner Shipping Capacity Deployed at Hong Kong	165,979	157,015	178,402	135,008	153,617	124,454
Service Coverage – No. of Destinations in Europe	16	13	15	16	15	15
Connectivity – No. of Weekly Direct Transits to Destinations in Europe	52	32	37	32	34	37
Annually Blanked Capacity (TEUs)	260,600	328,540	243,001	572,553	819,550	441,844

Source: BMT Asia Pacific analysis

41. According to this data, the number of frequencies offered, and the number of destinations served, by shipping lines on the Transpacific and Asia to Europe trades generally remained stable during both the pre-pandemic and the pandemic periods. In addition, the volume of capacity made available by the shipping lines on these trades remained broadly stable, and indeed increased significantly in 2021.[20]

42. The tables also include figures on 'blank sailings' (that is, the cancellation by a shipping line of a scheduled call at a particular port). In line with the feedback received by the Commission during the initial consultation, the volume of capacity subject to blank sailings increased noticeably in the pandemic period (though conditions improved on the Asia to Europe trade in 2021). Certain respondents in the initial consultation suggested that this increase may be explained by a scarcity of containers or the need to bring a delayed vessel back on schedule during the pandemic period. The Commission also notes that, in the pre-pandemic period, blank sailings generally remained at around the same

[20] The Commission understands from the Review that while capacity has increased significantly on the Transpacific and Asia to Europe trades, this has not been the case on the intra-Asia trade. This is in line with the trend of 'capacity shifting' which has been mentioned to the Commission in the initial consultation. Much of the additional capacity on the Transpacific is accounted for by shipping lines which are independent of the alliances.

level as when the Order was issued and refers to its findings on the reasons for the market conditions in the pandemic period in paragraphs 32 to 37 above.

43. In addition, the capacity made available by the shipping lines has generally be utilised at a high level. The data obtained by the Commission from its industry expert indicates that the utilisation rates have been above 90% on the Transpacific trade and above 85% on the Asia to Europe trade in each year since the issuance of the Order. Industry data also indicates that shipping lines have been ordering above average numbers of new vessels in light of increased demand, with orders for container ships in the first half of 2021 almost eight times of those in the first half of 2020.[21]

Pricing

44. During the Review, the Commission obtained data on average spot rates on an 'all in' basis (i.e. inclusive of surcharges) on the Transpacific, Asia to Europe, and intra-Asia trades since the issuance of the Order.[22]

45. With respect to the pre-pandemic period, this data indicates that average spot rates generally remained stable. Although one respondent in the initial consultation suggested that spot rates had increased even prior to the onset of the pandemic, this was not borne out by the data obtained by the Commission.

46. During the pandemic period, however, there has been a very marked increase in the spot rates on these three trades (in line with widespread reporting), though the information obtained by the Commission in the Review suggests that 'contract rates' have increased by a lower proportion.[23] One respondent in the initial consultation suggested that the most cargo is carried pursuant to contracts (and thus subject to a lower level of rate increase). However, the data obtained by the Commission regarding the proportion of cargo carried under a spot rate as compared to that based on a contract rate did not permit such a conclusion to be drawn. Moreover, the Commission understands that certain shipping lines are at present less willing to conduct business with customers on a contract basis.

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[21] UNCTAD, Review of Maritime Transport 2021, November 2021, page 40.
[22] 'Spot' rates are those made publicly available by shipping lines and which customers wishing to transport cargo on an occasional basis (that is, without a contract) will pay.
[23] As an alternative to obtaining services on a 'spot' basis, a customer may commit to obtaining services from a particular shipping line under a confidential service contract, which will make provision for the freight rates and surcharges to be paid by the customer over the period of the contract.

47. As to whether these rate increases have been caused or exacerbated by VSAs or more generally by collusion by shipping lines, the Commission refers to its findings in paragraphs 32 to 37 above.

48. Table 4 below provides a high level summary of the pricing data obtained by the Commission.

Table 4: Average spot rates on the Transpacific, Asia to Europe and intra-Asia trades (August 2017 to September 2021)

Trade	August 2017 to March 2020	March 2020 to September 2021
Transpacific (US$/FEU[24])	Ranging from $1,500 to $3,000 (approx.)	Ranging from $2,000 to $9,000 (approx.)
Asia to Europe (US$/TEU)	Ranging from $700 to $1,200 (approx.)	Ranging from $900 to $7,600 (approx.)
Intra-Asia (US$/FEU)	Ranging from $700 to $900 (approx.)	Ranging from $900 to $1,700 (approx.)

Source: BMT Asia Pacific analysis

Service quality

49. The data obtained by the Commission during the Review suggest that schedule reliability and the average number of days of delay per vessel arrival were broadly stable in the pre-pandemic period. In the pandemic period, however, schedule reliability has decreased significantly while the average delays have increased significantly.

50. For example, global average schedule reliability ranged from above 70% to below 85% from 2013 to 2019, but dropped to below 65% in 2020 and below 40% in 2021. The global average number of delays for all vessels ranged from above 0.5 to below 1.5 days from 2013 to 2019, and increased to above 1.5 in 2020 and above 3.5 in 2021.[25]

51. These trends are consistent with the information and views received by the Commission in the Review. For the reasons previously discussed, the Commission's view is that these

[24] 'FEU' refers to Forty Foot Equivalent Unit and is the standard size of a 40 feet long container.
[25] BMT Asia Pacific analysis.

developments are likely linked to the ongoing global supply chain issues caused by the pandemic.

Market composition

52. In the Statement of Reasons accompanying the Order, the Commission found that the degree of concentration on major trade routes and with respect to Hong Kong was relatively moderate.[26]

53. There has been some consolidation in the industry since the issuance of the Order. For example, Maersk acquired Hamburg-Süd, NYK, MOL and K-Line formed the ONE joint venture combining their respective containerised services, COSCO acquired OOCL, while Hapag-Lloyd and the UASC merged.

54. Nonetheless, the Commission's assessment is that the liner shipping industry remains only moderately concentrated. For example, the global market shares by capacity indicate that there are seven shipping lines with market shares of above 5%, while the highest market share is 17.1%.[27]

55. Insofar as the Asia to Europe and Transpacific trades are concerned, the large majority of cargo on these trades is accounted for by the eight shipping lines which belong to the three major alliances (the 2M, OCEAN and THE alliances). The data obtained by the Commission indicates that combined market shares of the parties to each alliance have remained broadly stable since the issuance of the Order.

56. Insofar as the other trades involving Hong Kong are concerned (such as Asia to Australia/New Zealand and intra-Asia), the information obtained by the Commission in the Review suggests that these remain considerably fragmented.[28]

57. The HKSC indicated in the S.20 Consultation, in relation to the Commission's finding that the relevant liner shipping markets are only moderately concentrated, that the three

[26] Statement of Reasons, paragraph 4.81. The trades in question were the Transpacific, Asia to North Europe, Asia to Mediterranean, North-East Asia to Australia and intra-Asia trades. For further guidance on the Commission's approach to market definition where trades are concerned, see the Guidance Note, paragraphs 20 and 21.

[27] Public Alphaliner data, as at 3 May 2022. The market shares are as follows: Mediterranean Shipping Company (17.1%); Maersk (16.7%); CMA CGM Group (12.9%); COSCO Group (11.5%); Hapag-Lloyd (6.8%); Evergreen Line (5.9%); and Ocean Network Express (ONE) (5.9%).

[28] [●]

largest shipping lines have accounted for over 50% of capacity in most of the main trades.[29]

58. In response, the Commission notes that:

(a) On the Asia to Europe and Asia to North America trades, at least eight major shipping lines, making up the three major alliances, are present, each of which competes with the other shipping lines in their respective alliance and outside. As noted, the Asia-Australia and intra-Asia trade routes are more fragmented still.

(b) Even with markets where the three largest shipping lines account for over 50% of capacity,[30] the presence of a number of other shipping lines with significant operations would still render the markets only moderately concentrated, as opposed to very concentrated, in competition law terms.[31]

59. Finally, in terms of entry and expansion, the submissions received in the initial consultation contain a number of examples of shipping lines commencing port calls at Hong Kong or services on the main trades involving Hong Kong since the issuance of the Order. The submissions include examples of smaller shipping lines active on the intra-Asia trade commencing services on the Transpacific and Asia to Europe trades during the pandemic period. This may suggest some ease in the extent to which shipping lines may redeploy vessels from one route or trade to another, though the Commission cannot conclude from these examples that competition or services in the market have increased overall.[32]

(d) Other matters

60. During the initial consultation, certain respondents referred to alleged practices in the liner shipping industry which cause difficulties for shippers (such as the introduction of surcharges without consulting shippers and poor communications to shippers regarding delayed or cancelled sailings) and suggested that an industry body be created to oversee the liner shipping industry. While the Commission has not received evidence to suggest that any such practices by liner shipping companies are the result of collusive or other

[29] Representation of the HKSC, 18 May 2022, point 2.

[30] The HKSC has not provided the source for their statement to this effect.

[31] See, for example, the Commission's *Guideline on the Merger Rule*, paragraph 3.15.

[32] In other words, it would need to be considered whether the new services merely represent a temporary redeployment (for example, to take advantage of the increased profits caused by exceptional demand), and also whether the addition of such services is offset by exits from the market elsewhere.

anti-competitive conduct under the Ordinance, it notes these concerns and will remain alert for any such evidence.

V. BASIS FOR THE VARIATION (RENEWAL) OF THE ORDER

61. This section examines whether the basis upon which the Order was originally issued remains valid (and whether thus the renewal of the Order is justified). In particular, it deals with the following matters:

    (a) whether there have been any changes to competition concerns associated with VSAs compared to those identified when the Order was issued;

    (b) whether there have been any changes to the efficiencies associated with VSAs compared to those identified when the Order was issued;

    (c) whether the market share limit in the Order remains appropriate; and

    (d) whether the Order remains merited and effective.

(a) Competition concerns associated with VSAs

62. In the Statement of Reasons, the Commission found that VSAs could lead to the following competition concerns under the first conduct rule:

    (a) reduction in service variety as between parties to a VSA where the parties could otherwise provide services independently, potentially leading to fewer choices in terms of for example port calls and frequencies;

    (b) reductions in the capacity in the market and thus higher rates, where the parties to a VSA together have market power and jointly decide to allocate less capacity to their joint services;

    (c) sharing of competitively sensitive information between VSA members on matters such as costs, capacity and vessel deployment.[33]

63. It considered, however, that the competition concerns identified would be unlikely to give rise to significant harm to competition unless the parties to the VSA enjoyed a sufficient degree of market power. In the absence of such power, the foregoing concerns would be

[33] Statement of Reasons, paragraph 4.8.

prevented or mitigated by effective competition from outside the VSA. In addition, the Order would only offer exemption to those VSAs where the combined market share of the VSA parties was below the market share limit and would not permit coordination on pricing.[34]

64. Based on the Review, the Commission has reached the conclusion that the competition concerns associated with VSAs have not become more significant or otherwise changed since the issuance of the Order.

65. For example, the data in Tables 2 and 3 above suggests that the number of port calls and frequencies has generally remained stable on the Transpacific and Asia to Europe trades, where services are mostly provided through VSAs. In addition, the level of capacity made available on the trades has remained stable and indeed increased in 2021. This suggests that any concerns that VSAs would lead to fewer choices in terms of port calls and frequencies, or reduced capacity, have not become more pronounced.

66. With respect to the possible reasons for the significant increases in pricing and decreases in service reliability during the pandemic period, the Commission refers to its findings as set out in paragraphs 44 to 51 above. In addition, the Commission notes that pricing and service reliability were broadly stable in the pre-pandemic period, which suggests that any competition concerns with respect to such issues were unchanged prior to the onset of the pandemic.

(b) Efficiencies associated with VSAs

67. In this section, the Commission considers whether VSAs continue to meet the four cumulative conditions of the efficiency exclusion, which require that the relevant agreement:

(a) contributes to improving production or distribution or promoting technical or economic progress ("**efficiencies condition**");

(b) allows consumers a fair share of the resulting benefit ("**fair share condition**");

[34] Statement of Reasons, paragraphs 4.9 and 4.11.

(c) does not impose on the undertakings concerned restrictions that are not indispensable to the attainment of the objectives stated in paragraph (a) ("**indispensability condition**"); and

(d) does not afford the undertakings concerned the possibility of eliminating competition in respect of a substantial part of the goods or services in question ("**non-elimination of competition condition**").

Efficiencies condition

68. In terms of the efficiencies condition, based on the Review, the Commission has concluded that VSAs continue in principle to allow shipping lines to offer broader service coverage and higher service frequency, and decrease the costs of entry and expansion on particular trades, than if shipping lines were operating alone.[35]

69. The HKLSA has provided updated data to support its claims that VSAs lead to these efficiencies. This includes the following example of the increase in services which arose after [●] entered into a VSA with [●] as of [●].[36]

Table 5: Example of increase in services following entry into VSA

	Access to services before joining VSA	Access to services after joining VSA	Change (%)
Number of weekly services	5	10	100%
Asia port calls per week	28	51	82%
North America port calls per week	15	33	120%

Source: data provided by [●]

70. The HKLSA has also provided updated data on the proportion of certain member lines' cargo which was carried pursuant to VSAs on the Transpacific and Asia to Europe trades, for the calendar years 2017 to 2020. The relevant proportion of cargo has remained at a high level since the issuance of the Order (ranging from [●]% to [●]% depending on the

[35] See Statement of Reasons, paragraphs 4.22 to 4.40.

[36] Another respondent in the initial consultation provided several examples of additional connections offered by shipping lines through VSAs since the issuance of the Order, based on Alphaliner data.

trade and year in question), suggesting that VSAs continue to be heavily relied upon by the sample of shipping lines in question.

71. The Review also does not cause the Commission to change its assessment that VSAs may result in cost savings, to the extent that they permit shipping lines to operate larger vessels, which tend to have lower costs per unit of cargo carried.[37]

72. A recent UNCTAD report confirms generally that "[l]arge ship sizes are associated with economies of scale on the sea-leg and potentially lower transport costs" and that "companies that have invested in larger ships are aiming for economies of scale which should reduce unit costs".[38] One respondent in the initial consultation referenced certain recent orders of ultra large container vessels by alliance members. In addition, the average capacity of vessels employed on services calling at Hong Kong has increased by 5% from [●] TEUs in 2017 to [●] TEUs in 2021, suggesting that shipping lines have been operating from increasingly large vessels.[39]

73. The Commission has therefore found that, while it has been unable to verify fully the efficiency claims with empirical evidence, so long as VSAs do not exceed the market share limit, they would in principle give rise to the above efficiencies and satisfy the efficiencies condition.[40]

Fair share condition

74. With respect to the fair share condition, the Commission found at the time of the issuance of the Order that the above efficiencies should in principle offer customers (i) higher service coverage and frequencies, and (ii) lower rates due to cost savings from use of larger vessels, with respect to VSAs which did not exceed the market share limit.[41]

75. Certain respondents in the initial consultation and the S.20 Consultation raised concerns around the extent to which such efficiencies are in fact passed on to customers. For example, the HKSC referred to the Commission's finding in the Review that freight rates

[37] See Statement of Reasons, paragraphs 4.41 to 4.48.
[38] UNCTAD, Review of Maritime Transport 2021, November 2021, pages 93 and 98.
[39] Data from Drewry Shipping Consultants Limited.
[40] This is consistent with the conclusion reached by the Commission when the Order was issued. See Statement of Reasons, paragraph 4.56.
[41] See Statement of Reasons, paragraphs 4.60 to 4.71.

remained stable in the pre-pandemic period and indicated that savings from VSAs have never been passed on to the users of liner shipping services.[42]

76. Nonetheless, based on the evidence it has obtained, the Commission has concluded that its assessment at the time of issuing the Order remains valid for the purpose of the fair share condition.

77. With respect to the benefits of broader service coverage and/or higher service frequencies, VSAs on the Transpacific and Asia to Europe trades, for example, have continued to offer broadly the same numbers of destinations and frequencies to customers in the pre-pandemic and pandemic periods. This militates against the suggestion that parties to VSAs no longer pass on the benefits of broader service coverage or higher frequencies to customers.

78. With respect to the pass-on of cost savings through freight rates, the Commission notes that rates remained broadly stable in the pre-pandemic period. This suggests that, all other things being equal, the Commission's finding at the time of issuing the Order that cost savings should be passed on to consumers in the form of lower freight rates would remain valid for the pre-pandemic period. As for the pandemic period, the Commission has discussed above the possible reasons behind the exceptional increases in such rates during that period. Finally, with regard to the HKSC's indication that shipping lines have in fact never passed on cost savings to customers, without any further elaboration on this point, there is not a sufficient basis for the Commission to revisit its original finding in the Statement of Reasons.[43]

Indispensability condition

79. With respect to the indispensability condition, the Commission has found that, since the form and terms of VSAs remain fundamentally the same, its original conclusion that VSAs are unlikely to impose restrictions on their members which are not indispensable to the attainment of efficiencies would also remain valid.[44] The Review did not reveal other less restrictive means of achieving the same efficiencies.

[42] Representation from the HKSC, 18 May 2022, point 4.
[43] That is, that shipping lines would in principle be likely to pass on cost savings from VSAs to users of shipping lines, where they fall within the market share limit in the Order.
[44] See Statement of Reasons, paragraphs 4.73 to 4.79.

Non-elimination of competition condition

80. As noted in paragraphs 52 to 58 above, the degree of concentration on major trade routes and with respect to Hong Kong remains relatively moderate, and the market shares of the alliances on the Transpacific and Asia to Europe trades remain broadly the same. The Commission will also retain the market share limit in the Order (see paragraphs 82 to 86 below). These factors suggest that the parties to VSAs which fall within the scope of the Order will comply with the non-elimination of competition condition.[45]

Conclusion on efficiency exclusion

81. Based on the foregoing and noting its assessment of competition concerns in the preceding section, the Commission has reached the conclusion that VSAs continue to meet the four cumulative conditions of the efficiency exclusion, provided the parties do not exceed the market share limit set out in the Order.

(c) Market share limit

Appropriateness of market share limit generally

82. Based on evidence and views gathered during the Review and the S.20 Consultation, the Commission has decided to maintain the existing market share limit in the Order upon its renewal.

83. In particular, the Commission maintains the view that the existing market share limit is necessary and appropriate. The market share limit ensures that each VSA is subject to competition from at least two other VSAs or independent parties in each relevant market in order to benefit from block exemption. At this level of concentration, the Commission considers there is sufficient certainty that no VSA would enable its members to exercise market power individually or jointly, such that they would be unable for example to achieve rate increases by jointly deciding through the VSA to withhold capacity from the market and/or would be incentivised to pass on efficiencies to consumers.[46]

84. Certain respondents in the initial consultation and the S.20 Consultation supported the maintenance of the market share limit, including the HKSC,[47] and referred among other

[45] See Statement of Reasons, paragraphs 4.80 to 4.84.
[46] See Statement of Reasons, paragraphs 4.14 to 4.19.
[47] Representation from the HKSC, 18 May 2022, point 1.

reasons to the position of the alliances in certain markets and the recent consolidation in the industry. The HKLSA indicated that it did not consider the market share limit to be necessary but did not oppose its inclusion in the Order.[48]

85. On the other hand, the HKGCC advocated for the removal of the market share limit.[49] It suggested that the Commission had adopted a hypothetical *ex ante* presumption in the Order, by selecting in advance a market share limit above which it is presumed that the balance between potential harm to competition and actual efficiencies will be reversed. It posited that the Commission should instead follow a factual approach, by availing of the mechanism in section 20 of the Ordinance to vary or revoke the Order if it considers based on empirical evidence that the efficiency exclusion is no longer met. Among other reasons for this suggestion, the HKGCC indicated that the self-assessment required above the market share limit would involve expense and undermine legal certainty.[50]

86. In response, the Commission notes that the approach suggested by the HKGCC would appear to require the Commission to keep the BEO under continual monitoring and review, to determine whether the efficiency exclusion continues to be met, and would largely negate the administrative efficiency associated with issuing a block exemption order in the first place. In addition, the Commission does not agree that above the market share limit, the balance between potential competitive harm and efficiencies is reversed. The market share limit does not create a presumption that the efficiency exclusion no longer applies where the combined market share of the parties to a VSA exceeds 40% or 45%, or that there is a contravention of the first conduct rule. Rather, it proceeds on the basis that above the market share limit there is *insufficient certainty* that the efficiency exclusion applies to justify an industry-wide exemption, and parties should instead self-assess whether the exclusion applies.

Application of market share limit on intra-regional trades

87. In its Guidance Note, the Commission indicated that where intra-regional trades were concerned, it would apply the market share limit by reference to the trade as opposed to on a particular point to point route within the region, but that it would revisit the appropriateness of this approach in its next review of the Order.[51]

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[48] Representation from the HKLSA, 31 May 2022, section 4.
[49] See representation from the HKGCC, 6 June 2022.
[50] Representation from the HKGCC, 6 June 2022, section 3.
[51] Guidance Note, paragraph 21(b).

88. The Review has not brought forth any evidence to suggest that this approach is no longer appropriate. In the initial consultation, the submissions that addressed this issue favoured maintaining the current approach, while in the S.20 Consultation, no respondent raised a contrary view or otherwise discussed this issue.

(d) Whether the Order continues to be merited and effective

89. While the Commission has concluded above that the activities of VSAs falling within the scope of the Order continue to meet the efficiency exclusion, it remains to be considered whether the Order continues to be merited and effective.

90. In this respect, the Commission considers that a block exemption order may be merited and effective, for example, where it concerns a category of agreements that are representative of agreements in wider use in one or more industries, where legal certainty as to the compatibility of such arrangements with the Ordinance is desirable, where there is a greater need for cooperation between undertakings in a particular sector as compared with other sectors in the economy, and/or where the order brings other public benefit.[52]

91. The Commission has reached the conclusion that the Order remains merited and effective, for the following reasons.

92. First, as noted previously in the Statement of Reasons, a block exemption order for VSAs can be expected to provide greater legal certainty for parties covered by the order. Without such an order, there may be a risk that parties would refrain from participating in VSAs due to concerns about their legality, which would mean the efficiencies associated with VSAs would not be realised in such cases.

93. Second, as noted in paragraphs 28 and 29 above, the evidence obtained by the Commission in the Review suggests that VSAs continue to be widely used by shipping lines calling at Hong Kong. This suggests that there continues to be a need for legal certainty as to the compatibility of such services with the Ordinance. The Order may be of particular

[52] See Guideline on Applications for a Decision under Sections 9 and 24 (Exclusions and Exemptions) and Section 15 Block Exemption Orders, paragraphs 5.3, 5.4, 5.7 and 11.3. The matters in section 19(3)(a), (b) and (c) of the Ordinance, which the Commission must consider when deciding whether or not to review a block exemption order, may also be noted.

value to the parties to smaller-scale regional VSAs, such as those on the intra-Asia trade, which may be less well placed to engaged in self-assessment.

94. Third, in terms of the need for a sector specific block exemption, the Commission notes the particular features of the liner shipping industry which have led to capacity sharing and the other forms of operational cooperation which occur in VSAs, which have not changed since the Order was issued.[53]

95. Fourth, the Commission notes that the submissions received in the initial consultation and the representations received in the S.20 Consultation generally suggest that the Order continues to be merited and effective. Importantly, none of the respondents in either consultation opposed the renewal of the Order.

96. Fifth, the Commission has taken into account the suggestion in several of the submissions and representations received that the renewal of the Order is necessary to ensure that Hong Kong port remains an attractive destination for shipping lines in a context where other jurisdictions continue to exempt VSAs from competition law. The Commission acknowledges in this respect the global nature of the liner shipping industry and that the other jurisdictions which offer exemptions for VSAs have generally renewed (following a review) or maintained their exemptions since the issuance of the Order, including those which attract significant liner shipping services.

97. Finally, certain submissions in favour of renewal of the Order have emphasised that VSAs may entail environmental benefits. As the Commission has already reached the conclusion on other grounds that the renewal of the Order is merited, it is not necessary to further discuss this point.

VI. DETAILS OF THE VARIATION (RENEWAL) OF THE ORDER

98. Based on the Commission’s conclusion that the activities of VSAs falling within the scope of the Order continue to meet the efficiency exclusion and that the Order continues to be merited and effective, the Commission has decided to renew the Order.

[53] See also Statement of Reasons, paragraphs 4.87 and 4.88.

99. With regard to the duration of the Order, the Commission has renewed the Order for four years under the Variation Order, while the Order as originally issued had a duration of five years.

100. In the S.20 Consultation, the HKSC supported the proposal to renew the Order for only four years.[54] On the other hand, the HKGCC indicated that the Commission had not adequately explained the benefit of renewing the Order for a shorter term and did not need to follow the practice of other jurisdictions.[55]

101. In response, the Commission notes that:

(a) In light of the prevailing market conditions during the pandemic period, there is benefit in allowing the Commission to review market developments and making a decision on whether the basis for issuing the Order remains valid within a shorter timeframe.

(b) While the Commission does not need to follow the approach of other jurisdictions, it is relevant that the other jurisdictions which decided to renew their equivalent exemptions for a shorter term than previously did so against the same backdrop as the Commission (i.e., the exceptional conditions in the liner shipping market during the pandemic period).

102. Neither the Review nor the S.20 Consultation have revealed a need or basis to amend any other terms in the Order.[56] Thus, the Commission has decided to adopt the position proposed in the S.20 Notice and renew the Order on the same substantive terms and conditions for a further four years.

103. To achieve the renewal of the Order, the Commission has issued the Variation Order pursuant to section 20 of the Ordinance to vary:

(a) the existing expiry date in paragraph (4) of the Order, so that it expires on 8 August 2026; and

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[54] Representation from the HKSC, 18 May 2022, section 3.

[55] Representation from the HKGCC, 6 June 2022, section 4. The representation from the HKCTOA, 23 May 2022, also indicated that it was unnecessary to shorten the term of the Order to four years, though it did not provide further information or analysis to support this position.

[56] See also paragraphs 25 to 27 above regarding the absence of material changes to the form of VSAs since the issuance of the Order, and 82 to 86 regarding the continued appropriateness of the market share limit.

(b) the deadline for commencing a review in paragraph (2) of the Order, so that the Commission must commence a (second) review by **8 August 2025**.

104. Finally, the Commission notes that, while it has decided to renew the Order and conduct a second review as set out above, it is not obligated under the Ordinance to do so or to further renew or review the Order upon the expiry of the Order on 8 August 2026.