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Canadian Shipbuilding Industry Stakeholder Consultations Preliminary Report

October 16, 2000

Introduction

Description of the Stakeholder Consultations

The following is a preliminary report on the results of Industry Canada's bilateral consultations with a broad representation of some 30 shipbuilding industry stakeholders. These stakeholders included: senior representatives of large and small shipyards; organized labour groups; ship owners and shippers; offshore oil and gas vessel fabricators and service providers; various industry and business associations; and provincial and municipal governments. A list of the firms and organizations consulted is attached as Appendix A.

The consultations were undertaken from May to September 2000, to gain new perspectives on the challenges and opportunities for workers, industries and governments, and to explore avenues to pursue. The consultations provided an excellent opportunity for the Government of Canada to:

- discuss the state of the Canadian shipbuilding industry candidly with stakeholders;
- develop a common consensus on the facts surrounding the industry; and
- obtain valuable insights, information, and ideas about how best to approach not only the challenging circumstances facing the industry, but also about how to capitalize on the opportunities.

The House of Commons Standing Committee on Industry Recommendations

The consultations also respond to the Industry Committee's recommendation that the Government of Canada consult with stakeholders to explore niche markets. The Report is preliminary at this stage, as summaries of individual bilateral consultation meetings are not yet finalized with some of the stakeholders. A final report will be available in the near future.

The Methodology of the Preliminary Report

Every effort has been made to reference comments representative of the majority of each stakeholder group. However, individual firms and organizations consulted did not all share in the comments or opinions associated with a particular group of stakeholders. While some stakeholders were agreeable to being quoted on their views, others indicated they did not wish to be quoted or to have their names attributed to any particular positions. Accordingly, the report has aggregated the information in order to protect the

confidentiality of stakeholders by avoiding any direct attributions.

Stakeholders expressed a broad set of views. All of these views, whether they reflect consensus or illustrate differences, are represented. The report attempts to cover all areas of convergence and divergence.

Overview of the General Findings of the Consultations

The consultations enabled Industry Canada not only to share its information with stakeholders, but also to considerably add to and, in some cases, update or correct its information.

While consensus was not unanimous, there was broad agreement on the substantial issues facing larger yards (i.e., those capable of larger commercial and naval newbuild construction) and on the emerging opportunities for small- and medium-sized Canadian yards in niche markets. It is clear from the consultations that the problems and challenges of the shipbuilding industry (and of related heavy marine industries including fabrication of offshore oil and gas vessels and modules), and potential solutions as well, vary considerably depending on the size of yard and the types of niche markets on which the yards are focussed. There is clear consensus on the stark realities posed by competition in the international shipbuilding and repair and heavy marine industries marketplace.

Broad, but again not unanimous, consensus emerged regarding impediments and possible solutions to address the issues and capitalize on the opportunities. Stakeholders generally acknowledged the government's commitments under international agreements, which limit its ability to act unilaterally to provide relief and remedies against foreign subsidies and other elements which distort the markets.

It was noted that there were real opportunities for new growth in some niche markets, but there was also broad agreement as to areas where the Canadian industry shows little possibility of growth, such as in larger commercial and naval vessel newbuilds.

Stakeholders generally agreed on the current state of the industry in Canada, and on the issues facing both domestic and international shipbuilding. Key issues include subsidization by other shipbuilding nations as well as other factors of advantage, such as high investments in technology or low labour costs, trade barriers that limit market access, current imbalance between supply and demand both internationally and in Canada, and the need to re-focus traditional approaches to shipbuilding, in order to capture emerging specialty markets.

Stakeholders were generally divided on the solutions to these issues. Some groups felt that the industry's future was best left in the hands of industry itself, while others felt that government should play a lead role in re-establishing the competitiveness of Canadian shipbuilding. Some groups were diametrically opposed on points related, for instance, to the need for better access to financing.

Another point that emerged from the consultations is that the shipbuilding regions have a range of shipbuilding capacities, interests, and successes in a variety of different markets, and consequently face diverse challenges. Therefore, they differ in some respects on measures needed to strengthen shipbuilding and repair, and associated heavy marine industries.

Another point of variance is between the small- to medium-sized shipyards and the larger shipyards. The smaller yards seem better able to adapt to demands for new products and, therefore, new markets as well, while larger yards are more affected by current international market conditions. In general, smaller, more innovative yards are operating at a significantly higher capacity than the larger traditional yards where there is

a serious overcapacity problem.

Throughout the meetings it was evident that, despite the challenges currently facing Canada's shipbuilding industry, there are many examples of innovative approaches and resulting success stories. Several yards have captured substantial business in specialized product areas such as luxury yachts, tug boats and modules for offshore exploration.

There is also optimism with regard to new opportunities for marine industries, especially in the development of offshore oil and gas. Stakeholders feel that action is required by all concerned to maximize the benefits related to emerging opportunities for Canadian industry.

The industry is in transition. Certain domestic market segments, such as federal government newbuilds, have declined and some traditional global market segments for small- and medium-size ships are threatened by global overcapacity. New domestic and international opportunities are emerging that could be considerable, but will take time to develop. Smaller but no less important opportunities in certain niche markets such as smaller aluminum vessels, higher-tech tugs and luxury yachts are filling capacity in some smaller yards.

Issues Emerging from Shipbuilding Stakeholders Consultations

Assessment of Current International and Domestic Situation

With regard to larger commercial newbuilds, stakeholders generally agreed with the assessment of the current situation facing major shipyards both in Canada and abroad. There is substantial overcapacity world-wide, the market is overwhelmingly dominated by southeast Asian countries, and there are few prospects for Canadian yards to participate in this portion of the market (i.e., larger commercial newbuilds).

Participants recognized that traditional shipbuilding has migrated to emerging industrial economies. Many national shipbuilding industries, including the Canadian industry, are currently impeded by serious global overcapacity, soft markets, varying and unpredictable degrees of subsidization by other shipbuilding nations, and prohibitive trade barriers. In short, the industry is struggling in a spoiled market where the normal forces of supply and demand have become distorted.

The majority of stakeholders recognized that the shipbuilding industry is moving away from some traditional commercial and government markets and towards higher-technology and more specialized niche markets. Many stakeholders saw the need for the industry to focus on niche markets and new opportunities, and to adjust and capture these opportunities. Measures which would assist in capturing emerging opportunities could include: widening the definition of shipbuilding to include heavy marine industries (such as offshore oil and gas vessels and modules); investing in new technologies and research and development; sharing best practices; renewing the work force; and, industry rationalization to better adapt to present and projected demand.

Most but not all stakeholders generally favoured one or more of the policy elements which are proposed in Bill C-213. Stakeholders noted that the main areas where improvements could be made to industry conditions include: more assertive federally-sponsored export promotion; greater access to international markets, particularly the United States (U.S.); the maintenance of tariffs on vessels imported into Canada; improved export financing and tax credits; reduced foreign subsidies; and, predictable federal procurement practices. It was widely recognized, however, that many of these challenges are difficult to overcome.

On the State of the Industry Today

Provincial governments recognize that the shipbuilding industry is in transition, and feel that federal assistance should be provided to help it restructure and prepare for new opportunities. It was not clear whether provincial governments were disposed to provide further assistance or support to their industries. There was general agreement on the need to focus on value-added shipbuilding products such as luxury yachts and other niche markets. To achieve this, the issues of an aging shipbuilding workforce, the need for skill enhancement and technology adaptation must be addressed.

Most **shipbuilders** see the future for Canadian shipbuilding in niche markets such as specialty-type vessels, often built using proprietary designs. But in order to compete in specialty niche markets internationally, Canadian yards must invest more in new technology and skill enhancement for workers.

Canadian **shipyard owners** recognize that efficiency is as important to competitiveness as pricing and quality, and felt Canadian yards need to continue to focus on increasing their levels of productivity.

The consultations revealed that Canadian shipyards may not be using Canada's world-class domestic marine research facilities to their best advantage. Moreover, few make use of the Scientific Research and Experimental Development tax credits and other federal programs to encourage innovation.

From the perspective of **shipowners**, on-budget and on-time production reliability are of extreme importance. Some of these stakeholders noted that Canadian shipbuilders sometimes lag behind other countries, notably Japan, in this regard. **Shipowners** observed that the sometimes lower productivity and efficiency of Canadian **shipbuilders** were issues that greatly affect their competitiveness. This situation is viewed by some stakeholders as attributable to the lack of sufficient investment in new technologies and modernized skills.

On Trade Policies and Trade Promotion

Many of the **mid-sized shipyards** indicated that greater government support for the promotion of their products and capabilities on the international market is needed. They also feel restricted by the taxation regimes and inter-provincial trade regulations that vary from province to province.

Provincial governments also feel that the shipbuilding industry could benefit from more active promotion of its products and capabilities by the federal government. They would like to see Canadian consulates and embassies made more aware of regional shipbuilding capabilities and products, and would like to see shipbuilding included in trade missions.

Provincial governments are united in their concern over protectionist trade barriers, and believe the federal government should more actively advocate changes to trade policies that keep Canadian shipbuilders out of major international markets.

Some **provincial governments** believe that Canada should not refrain from subsidizing the industry, while other countries appear to contravene the Organization of Economic Co-operation and Development guidelines on shipbuilding subsidies.

Ship owners were divided on whether the 25 per cent tariff on imported ships should be eliminated, while **shipbuilders** feel that the elimination of the tariff would effectively close down Canada's shipbuilding

industry.

On Financing and Bill C-213

Many **shipyard owners** were pleased with the support received from the Export Development Corporation (EDC). Some suggested that EDC financing could be made more effective by shortening the turnaround time for approvals. More importantly, they feel that longer financing terms, perhaps up to 20 years, are necessary in order for them to be competitive internationally. Also, tax credits would help offset the subsidies provided by other shipbuilding nations.

On Bill C-213, many **shipyard owners** indicated that the financial elements of the Bill would help the industry be more competitive, but that they alone would not be sufficient to overcome the problems of a distorted international marketplace, nor would they create sufficient domestic demand to re-establish the Canadian shipbuilding industry to its former levels of activity.

By and large, Canadian **ship owners** do not consider access to capital for domestic newbuilds as being an issue. Most **ship owners** that were interviewed do not consider subsidies to shipyards to be an effective way to revitalize the shipbuilding industry.

Labour firmly supports Bill C-213, and would encourage Canadian ship owners to buy Canadian-made vessels.

Provincial governments feel that it would be helpful to consider a financing package similar to the U.S. Title XI.

On Federal Procurement

Shipyards that rely on government newbuilds and repairs indicated that the unpredictable nature of federal procurement makes it difficult to manage their businesses. Many of them suggested that the government adopt a 10-year business plan for its marine newbuild and repair/refit work. In addition, many **shipyards** expressed frustration with the complexity and costs associated with the federal procurement process.

Also noted was a desire by the industry to have the federal government enforce its 'Buy Canadian' element of the federal shipbuilding policy, and to increase the contracting of federal ship repair to the private sector.

Notwithstanding this, stakeholders generally recognized that even stabilized government purchasing would not be sufficient by itself to sustain the industry at its current capacity.

On Best Practices and Future Prospects for Shipbuilding, Repairs and Refits

Most stakeholders across the country noted with interest the emerging opportunities associated with offshore oil and gas exploration, development, production and servicing, and for replacement of the Great Lakes fleet.

All of the **shipyards** recognized that some degree of product specialization is necessary to regain competitiveness, and many have either adopted this practice or are looking toward niche markets as a way to sustain their operations. New market opportunities may include new marine technologies and components, specialty vessels such as tugs, luxury yachts, specialized repairs, and the offshore oil and gas market. Many

expressed the need for the industry to work cooperatively and share information on best practices, and to consider strategic alliances amongst yards and other marine industries.

Ship owners mostly agree that the future of shipbuilding is in specialty or niche markets, and they feel that shipyards should be assisted in their attempts to diversify into specialty production or improved repair/refit capabilities, with an increased focus on high-quality niche market ships. Some **ship owners** expressed the view that the ship repair and refit market in some regions is an untapped market; frequently they go abroad for repairs, which they would rather do in Canada. This is particularly true of the industry on the East Coast.

All **shipbuilding provincial governments** recognized the importance of seizing new opportunities in order to maintain a national shipbuilding industry. In addition to the niche markets mentioned above, the offshore oil and gas industry is reputed to hold huge economic potential on both the East and West coasts. **Provincial governments** urged the federal government to act quickly to ensure adequate levels of Canadian content are required by corporations undertaking oil and gas exploration for the benefit of Canadian industry, its workers and our communities, but appreciate that this must be done within the constraints of Canada's international obligations, shared federal/provincial jurisdiction, and the Agreement on Internal Trade.

Most stakeholder associations (i.e., groups representing the interests of various stakeholders, including those of municipalities where shipbuilding is present) expressed concern about declining employment levels, but support the necessity for the industry to seriously explore niche markets and diversification opportunities to thrive in an increasingly globalized marketplace.

On the Need for More Dialogue

Stakeholders unanimously felt that the increased dialogue between government and the shipbuilding community was a very positive step. **Stakeholder associations** generally believe that increased dialogue is necessary to share information on best practices, and to help design the future direction of the industry, and that the federal government should play a leading role.

Some stakeholders, including **shipyards**, felt a bilateral approach to consultation was the preferred way to initiate an industry-wide dialogue, while others, notably **labour organizations**, felt strongly that solutions can only be determined through broader multi-stakeholder meetings.

Seizing Opportunities

One overall theme remained constant throughout the shipbuilding stakeholder consultations. Emerging opportunities will define tomorrow's shipbuilding industry, and how they will define it depends on the collective ability and willingness of all stakeholders to rise to these new challenges. Many of these opportunities are not immediate and some, such as those associated with offshore oil and gas, are particularly unpredictable.

Stakeholders involved in the offshore oil and gas industry agreed that the principal shipbuilding industry opportunities appearing on the horizon include the offshore oil and gas exploration industry. Many stakeholders noted the predictions of ongoing significant economic impact especially for the East Coast, but also for the West Coast and the Arctic in the future. The impact is expected to be diverse, as the offshore oil and gas industry requires such things as additional ships, supply bases, supplies and exploration components. These demands are increasing and creating opportunities not only for shipyards and offshore oil and gas vessel and module fabricators, but for other industrial and manufacturing sectors as well. Opportunities for larger

East Coast oil and gas projects over the next five years is estimated at about \$2 billion.

Offshore oil and gas stakeholders made several important observations and suggestions. Many expressed the view that Canadian content, including design and engineering elements, is the key issue to securing higher percentages of work on Floating Production and Storage Offshore vessels, semi-submersible and gravity-based platforms, and the modules associated with them. The market for anchor handling and supply vessels, and for the services they provide to the offshore, was cited by many as being important to their future prospects.

The views of **stakeholders involved in offshore oil and gas** products and services varied somewhat in regard to tariffs and subsidies, with some indicating they were of less importance. Others suggested that amendments to the *Coasting Trade Act* to remove the exemption for vessels allowed entry "where there is no Canadian-flagged vessel available in Canada" would be of great benefit.

Many of these stakeholders felt the **offshore oil and gas** vessel and module fabrication industry should be included with the shipbuilding industry for federal policy purposes. Their view was that many of their interests are identical or similar to shipbuilders who favour such things as federal refundable tax credits and higher capital cost allowances for leasing. Measures to assist offshore oil and gas stakeholders to improve and facilitate technology transfer from abroad were also recommended.

The replacement of many Canadian vessels in the **Great Lakes' fleet** is expected in the coming years. This fleet of some 150 vessels, of which about two-thirds engage exclusively in coastal shipping in the Great Lakes only, could provide a potential market of \$1.3 to \$1.7 billion for large yards. It was widely recognized that most of these ships will not be replaced in the near term, and that competitive pricing will be a major factor in determining how many of these vessels are built in Canada.

Acknowledgement

Industry Canada wishes to express its appreciation to all stakeholders who participated in the consultation process. Their assistance and advice to the Department has enabled the development of this report. While there are a variety of views on the issues facing the industry, the process has provided a broad representation of stakeholders and the government with an opportunity to share, compare and exchange valuable information and ideas with a view to improving the prospects for the industry and its workers.

Explanatory Notes

The Jones Act - A number of maritime laws (collectively known as the "Jones Act") impose a variety of limits on foreign participation in the U.S. domestic maritime industry. Under these laws, the carriage of cargo or passengers between points in the U.S. is restricted to U.S.-built and U.S.-documented vessels owned and operated by U.S. citizens. In international shipping, there are limitations on foreign ownership of vessels eligible for documentation in the U.S. These and other restrictions limit Canadian participation in U.S. markets.

The Jones Act does not entirely bar foreign shipyards from participating in the U.S. shipbuilding market. For instance, certain types of ships such as research vessels and offshore platforms may be procured from non-U.S. yards, and foreign yards are also allowed to do some repair and overhaul work. As a result of a commitment made in the North American Free Trade Agreement (NAFTA) negotiations - virtually its only undertaking in the maritime sector - the U.S. has clarified that work involving the replacement of less than 7.5

per cent of the hull and superstructure of a vessel can be done without forfeiting its Jones Act status, and up to 10 per cent with prior approval. Having fulfilled its NAFTA commitment to clarify the rebuild determination, there is no expectation at this time that this allowance for repair and overhaul work will be liberalized.

Although Canada and other trading partners have sought to enhance access to the U.S. market in this sector through trade negotiations, the U.S. has refused to negotiate improvements. At this time, there is no viable recourse available to Canada against the Jones Act.

Title XI- The U.S. Maritime Administration provides financing for the purchase of new, U.S.-built ships under its Title XI program. Title XI of the *U.S. Merchant Marine Act* of the 1930's is administered by the Maritime Administration (MarAd), and provides a 'full faith and credit' government guarantee for 25-year commercial loans to finance 87.5 per cent of the cost of U.S.-made vessels. In 1993, under the Clinton administration, it was revised and extended to include foreign transactions.

In the case of a U.S. export to Canada that benefits from Title XI financing, the industry has the option of initiating a countervailing duty (CVD) case. Similarly, the industry may initiate an anti-dumping (AD) case if it believes U.S. exports to Canada are being sold at below cost or for less than fair market value. If a CVD and/or AD investigation were conducted, and it was found that the Canadian industry was being injured as a result of dumped and/or subsidized imports, duties could be imposed. Under the NAFTA, Canada has the option of imposing quantitative restrictions on the importation of U.S.-built ships so long as the Jones Act remains in effect.

Bill C-213, *An Act to Promote Shipbuilding* - A private member's Bill (Dubé, Bloc Québécois) introduced in response to industry demands, contains three main elements: (1) subsidized loans through a loan guarantee program; (2) improved tax treatment of lease financing; and, (3) a refundable tax credit. The Bill was referred to the Standing Committee on Finance for examination. On October 5, 2000, the Standing Committee voted unanimously in support of all of the Bill's clauses, and the Bill has been reported to the House of Commons for Third Reading.

Appendix A

List of Organizations Consulted

Allied Shipbuilders Ltd. Vancouver, British Columbia
Canada Steamship Lines Inc. Montréal, Québec
Canadian Committee on Shipbuilding Policy Saint John, New Brunswick
Canadian Shipowners Association Ottawa, Ontario
Chamber of Maritime Commerce Ottawa, Ontario
CP Ships Calgary, Alberta
Federation of Canadian Municipalities Ottawa, Ontario
Fednav International Ltd. Montréal, Québec
Friede Goldman Newfoundland Marystown, Newfoundland
Gouvernement du Québec Ville de Québec, Québec
Government of British Columbia Victoria, British Columbia
Government of Ontario Toronto, Ontario
Government of New Brunswick Fredericton, New Brunswick
Government of Newfoundland and Labrador St. John's, Newfoundland

Government of Nova Scotia Halifax, Nova Scotia
Government of Prince Edward Island Charlottetown, Prince Edward Island
Industries Océan Inc. Ile-aux-Coudres, Québec
Irving Shipbuilding Inc. Saint John, New Brunswick
Les Industries Davie Inc. Lévis, Québec
Marine Workers Federation Halifax, Nova Scotia
PCL Industrial Constructors Inc. Bull Arm, Newfoundland
Peter Kiewit Sons Co. Ltd. St. John's, Newfoundland
Point Hope Shipyard Co. Ltd. Victoria, British Columbia
Port Weller Dry Docks Port Weller, Ontario
Seaspan (Cyprus) Limited Vancouver, British Columbia
Secunda Marine Services Limited Dartmouth, Nova Scotia
Shipbuilding Association of Canada Ottawa, Ontario
St. John's Dockyard Limited (Newdock) St. John's, Newfoundland
Vancouver Shipyards Co. Ltd. Vancouver, British Columbia
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