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The Influence of Cabotage Policy on Price Disparity between Peninsular Malaysia and Sabah

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Abstract: *The Malaysian government introduced a cabotage policy in 1980 to protect and enhance the competitiveness of the Malaysian shipping industry. The policy requires all foreign vessels to unload at Port Klang, the designated national port, after which only Malaysian-flagged vessels can carry cargo to other ports in Malaysia. The policy was criticised for creating additional freight costs to importers and for allowing domestic shippers to monopolise the market. Critics claimed that the higher rates for transhipment services were subsequently passed on to the consumers resulting in higher prices of goods and services. This study examines the influence of Malaysia's cabotage policy on prices and competitiveness of the shipping industry in the state of Sabah. This study used stakeholders and force-field analysis to examine the influence of the cabotage policy. The stakeholder analysis identified four different stakeholder groups, examined their positions, and rate their positions on the influence of cabotage policy using force-field analysis technique. The analyses show that the cabotage policy was not the only factor causing high prices. Port conditions, efficiency, level of infrastructure, trade imbalance, and political will must also be addressed to remedy the issue.*

Keywords: Price disparity; cabotage policy; force-field analysis; Sabah; stakeholder analysis
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1. Introduction

A cabotage policy imposes restrictions on the operation of sea, air and other transport services within and into a country to protect domestic suppliers of transport services from foreign competitors. Normally, the policy is applied to shipping services along coastal routes and between ports. It has, however,

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developed to cover aviation, railway, and road transportations (Hodgson & Brooks, 2004; Kusumaningrum, 2015). In the case of Malaysia, cabotage sea regulation limits foreign ships in Malaysian waters, where it only permits Malaysian-owned shipping companies with vessels flying Malaysian flags to trade between ports in Malaysia. The policy was introduced in 1980 to minimise Malaysia's dependence on foreign vessels, which had caused an outflow of foreign exchange in the form of freight payments (Khalid, 2008). The policy is administered by the Domestic Shipping and Licensing Board (DLSB), under the purview of the Maritime Division of the Ministry of Transport Malaysia.

The cabotage policy, however, has been heavily criticised by many parties. It has been blamed for causing price hikes in the state of Sabah and Sarawak (East Malaysia) compared to prices in Peninsular Malaysia (West Malaysia), which is separated by the South China Sea by approximately 1200 km. The policy prohibits foreign ships from the Far East such as South Korea, Japan, Taiwan, and China to dock at East Malaysian ports directly. Instead, ships from the Far East have to unload their cargo in Port Klang in West Malaysia. Subsequently, cargo meant for East Malaysia has to be reloaded onto Malaysian vessels and transported across the South China Sea again in order to arrive at their destinations in East Malaysia. The overall impact on the cost of import and prices of goods has been argued to disproportionately affect small and medium enterprises (SMEs) and low-income earners in East Malaysia[1]. Some parties also contended that Malaysian shipping companies are exploiting the policy by charging high shipping rates.

There are, however, other distortionary policies such as value-added taxes, subsidies, price controls and development policy which also contribute to the price disparity. In addition, prices in Sabah are affected by the high cost of inland transportation in the vast and rugged landscape of the state. Price distortion is also caused by the lack of competition and inefficiency of distribution channels, which is not limited to transhipment activities but also ports' efficiency, operational costs, surcharges, truck rental, and warehouse charges. Furthermore, protection due to cabotage restrictions resulted in weak incentives for operators to modernise and become more competitive.

This study examines the influence of the cabotage policy on price disparity between West Malaysia and the state of Sabah by taking into account different aspects of the maritime industry up until the latest announcement of its abolishment in June 2017. Stakeholders and force-field analysis are used to examine the influence of the policy. The force-field analysis is conducted by giving scores for each force based on the view of stakeholders, indicating their emphasis on certain issue for or against any action or policy; after weighing up pros and cons on the issue of cabotage policy and its relevance to price disparity.

2. Cabotage Policy in Malaysia

Malaysia introduced its cabotage policy on 1 January 1980. The policy limits the transportation of goods through domestic waters to ships flying Malaysian flags. Accordingly, the Merchant Shipping Act 1952 (MSO 1952) was amended to allow the policy to take effect (Khalid, 2008). The 1980 cabotage policy determined Port Klang as the only national off-loading centre, where vessels not belonging to Malaysian shipping companies or not registered in Malaysia must unload their cargo at Port Klang before it can be shipped to other ports in Malaysia. The Domestic Shipping Licensing Board (DSLB) was set up to regulate and control the licensing of ships engaged in domestic shipping routes. Companies that intend to obtain unconditional licences must have 30% local equity participation. Additionally, the shipowner must be Malaysian, and 75% of the board of directors and office staff members must be Malaysian. Also, the company has to (i) be incorporated in Malaysia, (ii) have its principal office in Malaysia, and (iii) carry out a majority of its management activities in Malaysia (Khalid, Ang, & Hasan, 2010). The Minister of Transport, however, may grant an exemption to Malaysian companies that operate foreign-flagged vessels, provided that no suitable Malaysian-flagged vessels are available for the route. The main purposes of the cabotage policy are to increase registration of ships in Malaysia and encourage the incorporation of new local companies. The policy shelters Malaysia's shipping industry by restricting access of Malaysian ports to foreign companies. The 1980 cabotage policy is an essential part of the government's strategies towards (a) making Malaysia a maritime nation; (b) reducing the country's dependence on foreign ships by increasing the level of local participation in shipping industry; (c) engaging in shipping commitments through bilateral, regional, and other trade agreements; (d) training and development of Malaysians in technical, professional, and commercial aspects of shipping business, especially in terms of increasing the number of Malaysian in the shipping industry (Suffian, Rosline & Karim, 2015).

In 1994, the Merchant Shipping (Extension and Amendments) Act 1994 was introduced to spur the growth of Malaysian-flagged vessels further. The amendments relaxed certain conditions of the original cabotage policy, whereby foreign-flagged vessels are allowed to carry out transhipment activities between the Port of Penang and Port Klang. By mid-2000, Malaysia was considering further liberalisation of the policy to allow foreign lines to carry transhipment cargo between designated ports in East Malaysia and Port Klang. On 3rd June 2009, the government further liberalised the shipping industry by allowing[2] foreign-flagged ships to perform transhipment activities between Port of Sepanggar and Port of Kuching in

East Malaysia and Port of Tanjung Pelepas in West Malaysia without the need for a shipping licence (Suffian, Karim, Rosline & Fadzil., 2013). This means that foreign-flagged vessels are no longer prevented from calling directly at any of the five major ports in Malaysia. Further liberalisation of the shipping market was partly ignited by discontentment of different parties in Sabah and Sarawak who claimed that the cabotage policy impeded their competitiveness and caused the price of goods to be unnecessarily higher relative to West Malaysia (Khalid, 2011). These parties maintained that opening up of domestic sea routes would create healthier competition among shipping companies leading to better shipping services, lowering freight costs, and eventually lower the cost of goods (Khalid, 2011; Metcalf & David, 2015).

Despite the 2009 liberalisation, support for local shipping industry such as tax exemption grants was still in place (Khalid, Ang & Hasan, 2010). Recently, the Malaysian government announced the complete abolishment of the cabotage policy for shipment between East and West Malaysia beginning from 1 June 2017. Nevertheless, the cabotage policy still applies to cargo shipping operations within East Malaysia.

3. Freight Rate, Cabotage Policy and Price Disparity

The main aim of the cabotage policy is to increase the level of local participation in Malaysia's shipping industry. The price disparity between East and West Malaysia blamed on the cabotage policy, may not reduce even if cabotage protection is lifted as freight rate depends on a multitude of factors. UNCTAD (2015) and Wilmsmeier (2014) classified the factors determining international maritime transport cost into trade flows, maritime industry structure, position within global shipping network, operating cost, trade facilitation, shipped products, and port infrastructure. Furthermore, other domestic distortionary policies and inefficiencies may lead to price disparity.

3.1 Trade Imbalance

Trade imbalances led to the need for empty container management, position adjustment at different geographical areas, as well as handling of storage and containers accumulation in major importing regions. The imbalances along trade lanes led to imbalances of empty containers supply and demand, a structural and widespread issue in trading (Li & Da Costa, 2013). Empty container repositioning is needed to balance demand and supply, although it is non-revenue generating and expensive (Sheng, 2014). The imbalances affect freight rates. In the case of European countries, De Oliveira (2014) shows that on average inward freight rates are 23% higher than outward freight rates, hence the cost of repositioning empty containers is borne by European importers. With regards to regional trade, the "average freight cost per TEU from Asia to the United States is about 1.78-fold that in the opposite direction and the cost from Asia to Europe is about 1.33-fold that in the opposite direction" (Tanaka & Tsubota, 2017).

In Malaysia, trade between East and West Malaysia is heavily imbalanced. Most container ships from Sabah and Sarawak towards Peninsular return empty, thus forcing shipping companies to double charges to cover the cost. In fact, for every two laden containers bound for East Malaysia, one will return empty[3]. Since the volume of cargo is limited, domestic shipping operations are constrained when the shipping cargo to Sabah and Sarawak is not enough to cover costs (Khalid, 2011).

3.2 Industry Structure: Competition and Collusion in the Shipping Industry

Public trade-restrictive policies, such as a cabotage policy, and private trade-restrictive practices, such as shipping conferences[4], have been shown to cause high maritime transport costs (Amjadi and Yeats, 1995; Francois and Wooton, 1999). In the case of Malaysia, in addition to a cabotage policy which has restricted competition in the maritime sector, Malaysian shipping companies have also been blamed and accused of oligopolistic behaviours by charging high shipping rates[5]. For example, freight charges between Port Klang and Hong Kong stood at RM55 per TEU while goods that were moved between Port Klang and Sepangar Port, Kota Kinabalu were at a staggering RM850 per TEU in 2009[6].

Globally, private collusive behaviours are deeply rooted in the history of maritime transportation. Liner-shipping companies cooperate on decisions with regards to price settings, capacity and schedule of maritime routes (Premti, 2016). In fact, the U.S. Merchant Marine Act of 1916, allows shipping conferences. By joining shipping conference agreements, shipping companies retain their juridical independence but consent to common practices with the other members regarding pricing, traffic distribution, and/or vessel capacity utilisation (Fink, Mattoo & Neagu. 2002). Nevertheless, studies have shown that both public and private trade-restrictive policies are becoming less important (Franck & Bunel, 1991). The power of conferences has eroded due to the entrance of more efficient shipping companies (Dollar et al., 2002). Containerisation and other forms of technological progress have made it possible for outsiders to supply the same services as the conferences at lower costs to consumers. Changes in regulations also affect international shipping, for example, the U.S. Ocean Shipping Reform Act of 1998, while preserving the antitrust immunity of the rate-setting conference system, allows for the confidentiality of key terms in contracts between shippers and carriers (Fink, Mattoo & Neagu, 2002).

As the main feature of the evolution of the shipping industry is increased concentration, recent studies pay more attention to competition intensity on specific trade routes. However, several questions remain, in which one of them is how market power is reflected in the components of freight rates (De Oliveira, 2014). The level of competition in the market is one of the important factors in determining freight rate. For example, in order to estimate the determinants of the transport costs, Fink, Mattoo and Neagu (2002) use a reduced form price function, which takes into account the technological effects of containerisation, the distance between countries, the public trade policies, the existence of economies of scale and private anti-competitive practices followed in various countries. Public trade policies and private anti-competitive practices are crucial in their analysis since they highlight the impact of competition rules in the liner shipping sector. The importance of private anti-competitive practices suggests that eliminating the cabotage policy in Malaysia does not guarantee a reduction in freight rates.

3.3 Port Infrastructure, Accessibility and Trade Facilitation

Various types of services are provided in the transportation of goods, such as trucking, carriage (forwarding), terminal handling services and storage (Medda and Trujillo, 2010). Often, governments regulate the prices for vessels to ports but not these other services. Several studies also point to certain aspects of service quality, such as frequency of services (Klovland, 2009; Puckett, Hensher, Brooks & Trifts, 2011), economy of scale (Dinwoodie, Tuck, & Rigot-Müller, 2013; Lindsey, Mahmassani, Mullarkey, Nash, & Rothberg, 2014; Medda & Trujillo, 2010) and transhipment services (Meng, Wang, & Wang, 2012; Wang et al., 2013) as some of the determinants of freight rates. Furthermore, the two-tier maritime network shows that the connectivity to shipping routes can vary compared between a direct and indirect link through hubs or transhipment ports (Laxe, Seoane, & Montes, 2012; Le, Minford, & Wickens, 2010; Sun, Rangarajan, Karwan, & Pinto, 2015). Reserve and distant location to main international liner-shipping networks also have a higher effect on maritime transport cost compared to geographical distance (Tierney, Áskelsdóttir, Jensen, & Pisinger, 2014).

Generally, ocean carriers utilise the flexibility of leasing arrangements and extensively use leased equipment by employing them in areas of high demand. Table 1 summarises the characteristics of the different container leasing arrangements. Leasing companies and ocean carriers, however, have different and conflicting goals in managing business. In principle, carriers are made to handle containers. The synergy between these two main players are complex (De Oliveira, 2014). At times, empty containers can be inter-regionally repositioned through a depot or an intermodal terminal. Through intermodal transportation and last mile drayage, empty containers can also reach consignors' premises. A container is normally drayed to an intermodal terminal or a marine terminal for export once filled at the consignor's premises. Once off hire by an ocean carrier, empty containers can also attain storage depots and be temporarily stored before overseas repositioning takes place (Ko, 2013). From storage depots, aged containers, specifically those stored over a long period, may be sold out of the transportation network to the secondary market. Empty containers may move between different storage depots for balancing purposes or between marine terminals and storage depots (Kavussanos & Alizadeh, 2001). There are also terminals operating satellite empty container depots to avoid congestion at gates, gain additional storage capacity, and provide dedicated service to ocean carriers (Koekebakker, Adland, & Sødal, 2007).

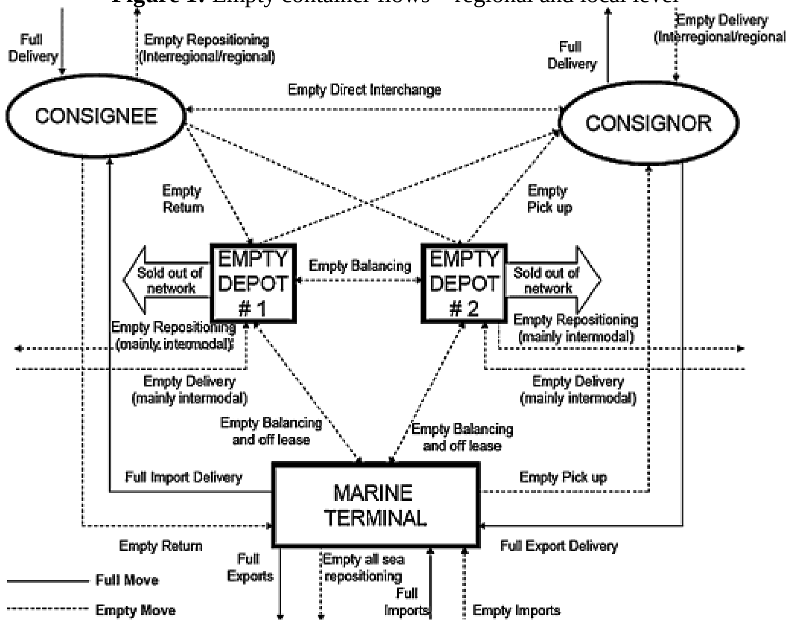
Table 1: Characteristics of the container leasing arrangements

Lease type	Lease type Duration	Repositioning	Maintenance and repair	Other arrangements
Master lease	Short to medium term	Leasing company	Leasing company	• Variable number of containers (min/max) • Variable lease duration • On hire and off hire credits/debits (depending on location and equipment condition)
Long term lease	5–8 years	Lessee	Lessee	• Fixed number of containers • Predetermined delivery schedule
Short term lease	Short period/ trip/ round trip	Lessee	Lessee	-

Source: Theofanis and Boile (2009)

The dynamics and linkages among stakeholders at the local and regional level, with influence from the interregional level, is depicted in Figure 1, where, ocean carriers, consignors, consignees, depot operators, marine terminal operators, drayage operators, depot operators, and possibly, transport intermediaries are all shown to be involved. A full container can reach a consignee's premises by truck either intermodally or directly through a marine container terminal. The empty container can be either returned to the marine terminal, or a storage depot once stripped, or directly "street turned" to a consignor's premises to be filled with backhauling load or an export (Russo & Musolino, 2013). The accumulation of empty containers in storage facilities at major importing regions with substantial import-export imbalances under certain circumstances may become a crucial problem under certain circumstances. The process of empty container aggregation follows the dynamics of container shipping which include diverse costs such as the cost of repositioning empty containers from surplus to deficit areas, container rates imbalances, cost of inland transportation, imbalances in type of containers available and demanded, cost of manufacturing and purchasing new boxes in relation to the cost of leasing containers, marginal and volatile profitability of the leasing industry, cost of inspection and maintenance for aged containers and the cost of disposal and terms of leasing contracts between leasing companies and ocean carriers (Veenstra, 2005). These complexities suggest that the abolition of the cabotage policy may not reduce the price disparity.

Figure 1: Empty container flows – regional and local level



Source: Theofanis and Boile (2009).

4. Research Method

This study used stakeholder and force-field analysis to examine the influence of the cabotage policy on prices in Sabah. There are many definitions of stakeholders (Mitchell, Agle & Wood, 1997; Agle, Mitchell, & Sonnenfeld,1999; Brugha & Varvasovszky, 2000; Lam, Ng, & Fu, 2013). This study defines stakeholders as any groups or individuals who can affect or are affected by Malaysia's cabotage policy. The relevant stakeholders were identified as individuals or groups that made tender or are involved in the shipping industry, those who performed any transaction in the shipping industry, and those who are directly or indirectly impacted by shipping regulations. Identified stakeholders were then classified into specific functional groups and subsequently, the position of each group is described. The steps involved in the stakeholders analysis is described in Table 2, where initially stakeholders are identified and classified, then interviewed about the relevant variables. The analysis stage extracts important points and categorises the responses from the interview and lastly, force-field analyses are done.

Force-field analysis is used to get a comprehensive view of all the forces for or against a plan so that a fairly justified decision can be made[7]. It is a technique where findings from the stakeholder analysis computed from the findings of all stakeholders are extended such that the magnitude of the direction can be analysed. It is used to evaluate cabotage policy and other factors that lead to the price differences between the two parts by combining the stakeholder analysis with the list of pros and cons for cabotage that intended to be done. The results of this analysis will indicate whether there is a balance of forces supporting the policy or against the policy. Several sensitivity tests will be undertaken with this result, by varying the scores (weights) given to each of the forces. As this analysis will be undertaken by a representative range of stakeholders, it suggests that a different set of forces or different scores will arise to each of the forces. Nevertheless, the force-field analysis can be declared as the most practical and supports the earlier stakeholder analysis by adding robustness to the evaluation of the present cabotage policy to Malaysia's maritime industry, particularly to the shipping and port sector as well as Sabah citizens.

Table 3 depicts the process of force-field analysis in this study. The force-field analysis and stakeholder analysis are interlinked. Interviews were conducted with various stakeholders in both West Malaysia and Sabah. The stakeholders included entities in the shipping and port industries, logistic chain industry, and regulatory agencies. Identity and position of interviewees are kept confidential to ensure the objectiveness of the study.

Table 2: Stakeholder Analysis

Item	Step
1a	Develop stakeholder map with major groups
1b	Classify the submission of individual or organisation under specific group
1c	Develop stakeholder impact matrix by i) summarising views on effects of cabotage policy; ii) determining suitable variables to be included such as employment, competition, rates, export competitiveness, and cargo type; iii) analysing the stakeholder views as either positive, negative, or irrelevant
1d	Analyse the stakeholder impact matrix in Item 1c
2	Classify pros and cons of cabotage policy by evaluating Item 1
3	Conduct force-field analysis

Source: Cavana (2004).

Table 3: Force-field Analysis

Item	Step
1	Qualitative technique to evaluate stakeholder analysis in Item 1 of Table 1 and pros and cons of cabotage policy as per Item 2 in Table 1
2	Obtain views consisting of forces for or forces against the policy
3	Classify and weigh the pros and cons of each view
4a	Equal driving and restraining forces result in equilibrium or inertia
4b	Imbalance between driving and restraining forces prompts the occurrence of change

The interviewed stakeholders include representatives from Malaysian Shipowners Association (MASA), Malaysian Institute of Maritime (MIMA), and Association of Marine Industries of Malaysia (AMIM) which represent shipping providers. The Sabah Department of Ports and Harbours represents the port authorities. The Ministry of Transport (MOT) and Ministry of Development and Infrastructure, Sabah (MDIS) represent relevant federal and state government agencies and Consumers Front of Sabah (CFOS). Table 4 summarises the views and attitudes of the different stakeholders on the influences of cabotage policy through different variables of interest on economic competitiveness and prices in Sabah. The variables of interest are in the columns, whereas the stakeholders are in the rows. How the cabotage policy effect prices through the variables of interest were classified into:

a) Positive effect thru the variable of interest is indicated by "+"
b) Negative effects thru the variable of interest are indicated by a "–"
c) Nil, minimal, uncertain, unknown, or not explained by the stakeholders are indicated by "un".

For example, MASA was of the view that the cabotage policy had effected prices positively through the quantity of domestic cargo by Malaysian ships, but SDPH, MDI, Sabah and CFOS opined that the cabotage policy affected prices negatively through the quantity of domestic cargo by Malaysian ships.

The questions asked during the interviews include the effects of cabotage policy on prices through cost and efficiency, frequency and quality of transport service, accessibility from manufacturer site to port, employment on Malaysian coastal ship, number of Malaysian coastal ships, technology of Malaysian ships, competition in transport service, financing accessibility, role of charterers in transporting products, domestic freight rates, domestic port rates, condition of ports in East Malaysia, domestic cargo by Malaysian ships, domestic cargo by rail/roads, domestic cargo by international ships, international freight rates, export-import volume imbalance, strategic plan (incentives and other policies), bureaucracy and political issues, technicality and infrastructure, and economic situation. Additionally, Table 5 details the arguments supporting and opposing the continuation of the cabotage policy.

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In order to add “richness” of perception, scores were given to reflect the “force” or emphasis of responses from the interviewees, based on his or her choice of words, tone, or repetition of the same point. Each force was rated from 1 (weak) to 5 (strong), then the total points from both sides, negative and positive, were compared. Criticism of the force-field analysis usually focuses on the subjectivity of attributing scores to the driving or restraining forces.

Table 4: Stakeholder Analysis

Stakeholders/ Variables of interest	**Cost and efficiency**	**Frequency and quality of transport service**	**Accessibility from manufacturer site to port**	**Employment on Malaysian coastal ship**	**Number of Malaysian coastal ships**	**Technology of Malaysian ships**	**Competition in transport service**	**Financing accessibility**	**Role of charterers in transporting products**	**Domestic freight rates**	**Domestic port rates**	**Condition of ports in East Malaysia**	**Domestic cargo by Malaysian ships**	**Domestic cargo by rail/roads**	**Domestic cargo by international ships**	**International freight rates**	**Export-import volume imbalance**	**Strategic plan (incentives and other policies)**	**Bureaucracy and political issues**	**Technicality and infrastructure**	**Economic situation**
MASA	–	–	–	–	–	–	–	–	+	–	–	–	+	+	+	+	–	+	–	–	–
MIMA	–	un	–	–	un	un	–	–	un	un	un	–	un	–	un	un	–	un	–	–	–
AMIM	un	un	un	–	–	un	–	un	un	un	un	un	un	un	un	+	un	+	–	–	–
SDPH	–	–	–	–	un	–	–	–	–	–	+	+	–	–	–	un	–	+	–	–	–
MOT	–	–	–	–	–	–	–	–	un	+	+	–	un	–	+	un	–	+	–	–	–
MDI, Sabah	un	–	–	un	un	–	un	–	un	un	+	+	–	–	+	un	–	+	–	–	–
CFOS	–	un	–	un	un	un	–	un	un	–	un	un	–	–	un	un	–	+	–	–	un

Notes: (1) Positive effect thru the variable of interest is indicated by "+". (2) Negative effects thru the variable of interest is indicated by a "– ". (3) Nil, minimal, uncertain, unknown, or not explained by the stakeholders are indicated by "un".

Table 5: Arguments Supporting and Opposing the Continuation of the Cabotage Policy

SUPPORTING ARGUMENTS	OPPOSING ARGUMENTS
Government Support	
1. Policies to protect the industry were insufficient and were still required. Competition from international "big players" and declining global trade volumes were few of the challenges faced by the local companies. 2. Shipping operators still faced difficulties in getting funding despite the industry being extremely capital-intensive because bankers and insurers were not familiar with the industry. Several ship operators had to apply for funding overseas to obtain the required assistance.	1. A lot of government initiatives to support the maritime industry such as exemption of income tax and domestic shipping licence were already in place. 2. The government had already provided several incentives such as RM 1.3 billion to upgrade Sepanggar Port in Sabah, the formulation of Malaysian Shipbuilding and Ship Repair Masterplan 2020, and Malaysian Shipping Masterplan.
Shipping Costs	
1. The trade imbalance was mainly caused by low cargo volume coming from East Malaysia which resulted in higher freight charges. Hence, removal of the cabotage policy may not change this situation. 2. The operations and scale of activities in Sabah's Sepanggar Port was relatively less efficient.	1. The cost of freight which was higher than the free market value was often blamed for price disparities between East Malaysia and West Malaysia. The cost of freight may be reduced if the monopoly created by the policy was removed.
National Interests	
1. As Malaysia was very reliant on trade to lead its economic growth, it must have strong maritime industry to curtail the outflow of currency due to the massive bill for foreign freight charges. 2. Several counter-profiteering measures were set by the government to ensure that domestic shippers did not charge exorbitant rates. 3. Employments in the shipping industry and its downstream operations may suffer from negative impact if the policy was removed. 4. Shipping companies had long gestation period before recovering their capital and increased competition will result in even longer gestation period. Foreign ship operators can offer lower freight charges because of their economies of scale. 5. Technology upgrades were costly but must be undertaken. Nevertheless, these upgrades will not be performed without guaranteed market demand for their services.	1. The policy was only benefitting the ship owners. They should be allowed to fail if they were inefficient or unable to penetrate into regional and international markets. 2. All decisions regarding the policy was made by the federal government without considering the effects on local economy in East Malaysia.

Table 5: (Continued)

SUPPORTING ARGUMENTS	OPPOSING ARGUMENTS
Intramodal Support	
1. All domestic transport modes – land, sea, and air – would benefit from higher cargo volumes. 2. The infrastructure in East Malaysia was underdeveloped while land accessibility from port to manufacturer, wholesaler to retailer, and to the end customers was difficult. This was a major factor that influenced the high prices in Sabah.	1. The underdeveloped infrastructure was mainly caused by insufficient government funding to cover the vast expanse of the state. Thick forest reserves and the remote location of certain settlements increased the transportation costs.

5. Results and Analysis

5.1 Stakeholders Analysis

The analyses of the interviews indicate that Malaysian ship owners, maritime think tanks and associations, port operators, and government agencies agreed that the cabotage policy is important. Cabotage policy promotes nation sovereignty; as it is essential for Malaysia to have a strong presence in the maritime services market for both economic and security reasons. The protection of domestic companies against foreign competitors assists them to grow and compete in domestic waters and, eventually, international waters. The policy also ensures that Malaysians are more favourably considered for employment in the industry, including as seafarers and in the maritime support services. Furthermore, the industry is extremely capital-intensive and, therefore, it is susceptible to financial vulnerabilities without government support. This is evidenced by the declining trend in registered tonnage carried by Malaysian-flagged vessels. For example, the period from 1998-2014 shows the biggest decline of registered tonnage for “general cargo” fleet, which declined at 65%, meanwhile “bulk” fleet reduced by 70% in 2004-2006. From a macroeconomic perspective, while the Malaysian shipping industry grew by 700% from 1980 to 1999, the balance of payment for transportation continued to be in deficit, reaching RM28.012 billion in 2012 alone[8]. This means that the capacity of Malaysian local carriers was unable to accommodate the demands for shipping sufficiently and that it was not growing in tandem with its demands.

Competition disparity, financing accessibility and the preference of charterers to grant contracts to foreign shipping companies are also issues that affect Malaysia shipping industry. These ship owners faced difficulties due to firms’ preference to charter foreign vessels to carry their shipments. Firms are more inclined to charter foreign vessels to carry their cargo for several reasons, namely (i) competitive rates, (ii) efficiency, (iii) frequency, and (iv) quality of service. Foreign vessels are often equipped with more advanced technology compared to domestic vessels. However, without any form of control, the outflow of currency to international shippers would be massive as payment for freight services can be substantial, and this may affect Malaysia's export earnings and balance of payment adversely. A solid decision is needed involving all related stakeholders[9]. Any initiative, however, cannot be realised unless the mechanism of the maritime industry and its dynamic and inter-relation with one another are fully understood. It is important for Malaysian Shipping Master Plan MSMP to be aligned with other national plans and agendas which include the Shipbuilding and Ship Repair Master Plan undertaken by the Malaysia Industry-Government Group for High Technology (MIGHT) to ensure that targets recommended by MSMP will be in line with the nation's aspirations and policies[10].

Some groups also raised doubts claiming that measures to 'level the ocean' between the Malaysian coastal ships and international ship operators are insufficient. The issue of competition disparity, financing accessibility and the role of charterers in granting contracts to the shipping companies are the major issues that could affect the shipping industry since this industry itself is a capital-intensive industry. On the other hand, taking into account cost and efficiency, frequency and quality of transport service and number of Malaysian coastal ships available, it is also comprehensible to relate on the motivation for most charterers to incline towards international ships in transporting their cargo as these ships are relatively bigger, more technologically advanced, and offer more competitive rates than the domestic ships.

With regards to the issue of price disparity, several perspectives have been argued, mostly referring to the conditions in Sabah. This includes the condition of ports, the existence of trade imbalance, the lack of economic activities, the lack of accessibility from port to retailers, the lack of infrastructure and technical facilities, and political sentiments.

5.1.1 Port efficiency

Ship operators and federal government agencies expressed similar opinions concerning the condition of ports in the Sabah. They indicated that many shippers are reluctant to berth at Sabah ports due to its inefficiency and lack of standards in handling cargo. However, this argument is dismissed by the Sabah port operator and Sabah government agencies by arguing that the issue of comparing the technicalities is not relevant due to the reason of development disparity in land infrastructure compared to West Malaysia. This causes goods that land at the port to face problems of distribution across the state as most of the roads are not well paved, which, in turn, causes other land transport to adjust to that state of condition.

5.1.2 Level of infrastructure

Most of the interviewees from Sabah argued that poor infrastructure is a more significant contributing factor. In particular, unsatisfactory road quality and low connectivity for delivery of the goods to wholesalers and retailers hindered robust economic activities. They claimed that government funding in East Malaysia is insufficient to support the trading value chain with adequate roads and bridges as compared to West Malaysia. On the other hand, other decisive factors also need to be addressed as they can directly affect the price, particularly infrastructure development by bringing more industrial activities to Sabah. Doing so would mean that they will not have to rely on the outputs coming from West Malaysia and would further improve the issue of the trade imbalance. Others advocate improving the facilities for transportation, especially for land transport to ensure seamless connectivity can be provided throughout all towns, cities and areas. Finally, it is very important to have a strong political will as to get every related stakeholder to realise the potential of the maritime industry to spur the nation's growth by linking everybody under one "roof". This would ensure that any procedure or process in getting financial assistance, licence, approval, and other technical support related to the industry can be done successfully without facing much bureaucracy issues.

5.1.3 Trade imbalance

All stakeholders agreed that trade imbalance between East and West Malaysia is a critical reason contributing to the higher rates that ship operators have to charge when performing transhipment services to East Malaysia. It was arguably due to the freight rates, which resulted in imbalanced trade pattern between East and West Malaysia. There is less backhaul cargo from East Malaysia to West Malaysia[11]. On average, return trips from East Malaysia usually carried 70% less cargo (backload) than trips to East Malaysia from Port Klang. In addition, since most container ships that arrived from Sabah and Sarawak to Peninsular are returning empty, it is thus forcing shipping companies to double charge customers; as their 'compensation' to cover the cost of the return shipping[12]. Since the volume of cargo is limited, domestic shipping operations are scarce in sending cargo to Sabah or Sarawak as the output of export is not convincing enough to bare their loss of profit. Shipping companies have to compete with each other to get reasonable cargo density, as well as paying out 'fairly good' carriage charge outcome. Similarly, since many vessels returning from Sabah were either carrying smaller cargo or no cargo at all, the expected changes such as lower freight costs and large-scale shift to foreign-flagged vessels did not occur despite the cabotage policy's partial liberalisation in 2009. A majority of Sabah stakeholders blamed this on the overall lack of manufacturing and industrial activities in the state. They felt that the situation is ironic, given the vast amount of natural resources in the state compared to West Malaysia, and its strategic geographical location in the South China Sea.

5.1.4 Political Will

Most stakeholders agreed that the government's role in supporting the maritime industry is necessary, be it in terms of policy and regulations as well as market intervention. Ship owners cited several cases of firms which had ceased operation under tough economic environment and high competition from international shippers. This means that the Malaysian fleet size was shrinking despite the cabotage policy. Conversely, several stakeholders from Sabah claimed that they are the ones who need to bear the costs for the government's support of the local maritime industry. This was because the cost of production and cost of living in Sabah are more expensive, whereas infrastructure and facilities were relatively lacking when compared to West Malaysia. Notably, the federal government's nationwide measure to help low-income groups through initiatives like Kedai Rakyat 1Malaysia, Coop1Malaysia, Agrobazar Kedai Rakyat, and FAMA13 stores were not extensive albeit beneficial as this did not entirely address the causes of structural weakness in the state's economy. Also, there are many more private retailers compared to government initiative stores.

On the other and, despite being vocal, the special interest group did not elaborate much on the cabotage policy and how it affected prices, although they did indicate that the cabotage policy needed to be abolished as it promotes monopoly among domestic shipping providers. This claim, even though it is supported by the port authority, is refuted by shipping providers and federal government agencies, having cited several counter-profiteering measures that have been carried out to curb this activity. The group suggested that the price in Sabah needed to be standardised before deliberately trying to regulate it nationwide.

5.1.5 Summary

Overall, the stakeholders' opinions on the cabotage policy and price disparity in Sabah can be summarised with the following quote from Interviewee A of the Ministry of Development and Infrastructure, Sabah on the trading processes involving domestic maritime industry:

> "…there are the entry ports...entry points so that all goods coming to the state, especially imported goods...so of course Sabah is not reliance in economy, in which we import a lot of goods from abroad...and definitely the port plays an important role in this. But of course, the chain movement…the port plays an integral part in the supply chain movement...but the only problem is relatively speaking…if you look at the other ports in the world of (…) Malaysia, to certain extend, the port inefficiency including relating to port charges…relating to waiting time...related to all this services provided by the port and also most important thing is the policy...so called cabotage policy, which a lot of people are really blaming all the high cost here in Sabah. The ports in Sabah seem to be doing the state a favour in a way, because it seems to be related to issues which have escalated the cost of living in Sabah."

Interviewee B from the Malaysian Shipowners Association has a different view and is clearly exasperated by the prolonged squabble about the cabotage policy:

> "…It's a simple thing. This factor lies in all cost of transportation whether on partial container or fully container. They have to factor in all the cost of transport. They call it the transportation cost. It might go up and go down. So, talking about the cost, I think this thing has been deliberated too long…too much... I think the case is already finish [dah lah kan... dah] slow down everything. Actually transportation cost take only 4 percent of the total… So when you mention about price... Actually [yang] profiting [ni] is not shipping, it's the industry. And the problem is that they don't have the infrastructure…they don't have the industry…Only in Sabah. And Sabah [ni] actually their FSI, [orang] industry [punya] manufacturing, they are making this thing, this noise is because of they all want the government to pay attention to them, because of their business. They want to get all the transportation. But they do not directly go to Port Klang, and let say go to Europe or what so ever, so transportation is quite a problem to them also. But one thing is, they should not say that shipping is the culprit of everything...they just want to take attention [je] all this while..."

It can be concluded that each stakeholder holds a different view based on the role that they represent. This translates into mixed arguments depending on the issue raised. Nevertheless, all of them agreed that the cabotage policy should be retained but with improvements in execution to ensure smooth operation as mentioned by Interviewee C of MOT:

> "If you ask me, I will say in terms of policy [ ] because if we compare with Singapore, we see that they actually don't have that many ports [pun] compare with Malaysia [ ], they don't have really coastal areas…but why many want to go there, especially those who works in bunkering what not...it can be maybe their government...in terms of management [ ]. If in Malaysia, even though we have bigger and better coastal areas than them, but maybe of their policy... in terms of their incentives that they give to the players...like us, our lack is on our policy [ ]. I'm not sure about that...but looking at these two different countries [ ] I think it's because of the policy [ ] I don't know the other parts but for cabotage policy, we will not abolish it, it's just that we will continue study on it..."

5.2 Force-field Analysis

Table 4 presents the direction of the impact but not the magnitude. For example, from the perspective of shipping providers, the impact of the cabotage policy through the quantity of "domestic cargo by Malaysian ships" is positive while the impact due to "competition in transport services" is negative. Since the magnitude is unknown, the aggregate effect is unknown.

Table 6 provides the force-field analysis, providing weight to the opinions, judgements and experience of the maritime industry in Sabah. It can be concluded that the stakeholders were divided on the implementation of the cabotage and "financial, fiscal and regulatory regime" to provide an equitable trading environment for Malaysia in both coastal and international trades. Although, liberalising the cabotage could potentially increase the participation in shipping for both local and foreign players. The balance of forces that supported change in the policy (including its complete removal) was 34 against 58 that restricted changes to the policy. Items in the left column refer to situations that could compensate or substitute the cabotage policy in terms of promoting the national maritime industry or the economic competitiveness of East Malaysia. Hence, the removal of the policy is not going to be detrimental. In contrast, items in the right column refer to situations or reasons for the policy to be preserved, mostly because the benefits outweigh the weaknesses.

These forces indicate that the high price of goods in East Malaysia is not due solely to the cabotage policy. Hence, there is an argument supporting the cabotage policy. Lifting the cabotage may not change the differences in price because of the problems are deeper than the cabotage policy and include infrastructure, efficiency and trade imbalance and as such, removing of the cabotage policy may not reduce the disparity of prices between West and East Malaysia.

Table 6: Force-field Analysis Opposing and Supporting the Cabotage Policy

Forces Driving Change in Policy	**Score**	**Forces Restricting Change in Policy**	**Score**
Incentive to increase local employment on coastal ships and maritime services industry	2	Limited choice/competition in transport services	4
Improved future supply of maritime workforce	3	Practice of cartel was already rooted in domestic shipping industry	5
Strengthening of Malaysian shipping fleet	2	Higher freight costs and lower profits for domestic shippers	5
Allow higher volumes carried by domestic transport operators	2	Cargo volume for domestic offshore vessels was already relatively small	4
More competitive freight rates and returns for Malaysian transport operators	3	International freight rates were lower compared to domestic rates	4
Lesser dependence on international ships	2	Trade imbalance was significantly evident in East Malaysia due to lack of industrial activities	5
Guidelines for domestic charterers to prioritise domestic ships	2	Growth of SME sector in East Malaysia was limited because of dependence on imported raw materials	4
Competitive differences between Malaysian and international vessels in terms of costs and practice	2	Less manufacturing jobs were available compared to West Malaysia	4
Solid regulation of policy for every stakeholder to get a clear understanding on the flow of industry	3	The local banking sector were not keen enough to support the shipping industry	5
The ongoing project of Pan Borneo Highway	5	Inefficiency in port operations	4
Incentive to open more industrial activities in East Malaysia	2	The sea and land transport systems were not integrated	5
Brought mainline operators to do business in Eastern ports	2	Insufficient technological upgrade for port facilities	5
Incentive to improve Sepanggar Port	4	Lack of assistance to shipping industry	4
Total supporting change	34	Total against change	58

6. Conclusion

A cabotage policy was imposed by the Malaysian government on the shipping industry starting in 1980 with the primary aim of boosting Malaysian firms' participation in the shipping industry. The policy protects Malaysia's shipping companies by limiting foreign access to Malaysian ports in both West and East Malaysia. The cabotage policy, however, was blamed by many parties, especially consumer groups for price disparity between East and West Malaysia, where prices in East Malaysia were higher than those in West Malaysia.

Analyses based on stakeholders and force-field analysis show that the cabotage policy was not to be blamed for the price differences. Weak distribution channels, high handling charges and inefficient inland transportation in addition to other various interrelated factors had increased prices in Sabah to be higher than West Malaysia. Specifically, the higher prices in Sabah were mainly due to the inefficiency of port operations, underdeveloped infrastructure in Sabah which limit access to many parts of the states and trade imbalance between Sabah and West Malaysia which resulted in less cargo when ships were to return to West Malaysia after delivering cargo to Sabah. These issues increase the cost of transportation for products shipped to Sabah. These issues which were not related to the cabotage policy mean that termination of the policy will not solve the price disparity problem.

Numerous factors must be addressed in order to equalise prices in Sabah and West Malaysia. For example, in order to improve the trade imbalance, Sabah needs to produce products that are demanded in West Malaysia. Some critics argued that the policy had given the government a monopoly over the power to decide whom, how and when applicants receive the shipping licence and access to the domestic market. However, as suggested by some of the stakeholders, the anti-competition policy can easily be used if the shipping industry is using monopolistic power to increase prices.

Price transmission, which is the process in which upstream prices affect downstream prices for Sabah, cannot be fully understood without empirical evidence. Upstream prices comprise the cost of freight together with the prices of main inputs for processing, manufacturing, or trading, or prices quoted on higher market levels such as import price or wholesale price. Anecdotal evidence depicted two opposing views. The freight component is merely a small proportion of the final consumer price, while others claimed that it is larger. However, inadequate statistical data on coastal shipping and port distribution of goods in Malaysia prevented the study from justifying such claims. Nevertheless, it can be generally concluded that the domestic maritime industry needs more than the cabotage policy to revive and grow in this challenging time. Additionally, Sabah needs more than the removal of the cabotage policy to spur it on a more sustainable and robust economic growth path.

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Notes

1. The Borneo Post, 14th July 2013: "Why the Discrimination". http://www.theborneopost.com/2013/07/14/why-the-discrimination-2/

2. Gazetted as P.U.(B)179

3. The Star, 10th July 2009: "Move to address trade imbalance". https://www.thestar.com.my/business/business-news/2009/07/10/move-to-address-trade-imbalance/

4. Liner conferences are "formal or informal private arrangements between carriers or between shipping lines which enable them to utilise common freight rates and to engage in other cooperative activities on a particular route or routes" (OECD, 2002: 16).

5. Borneo Post, 18th June, 2017: "Is Cabotage Policy Driving Up The Cost of Goods?" http://www.theborneopost.com/2017 /06/18/is-cabotage-policy-driving-up-the-cost-of-goods/ Daily Express, 6th July 2014: "Offset cabotage's effects' call" http://www.dailyexpress.com.my/news.cfm?NewsID=90305

6. The Edge Markets,9th July, 2009: "Cabotage policy between West and East Malaysia liberalised" http://www.theedge markets.com/article/cabotage-policy-between-west-and-east-malaysia-liberalised

7. Force-field analysis is a specialised method of weighing pros and cons. It was originally developed by a social psychologist, Kurt Lewin (1945, 1947, 1951) as a method for analysing general problem situations and determining future courses of action.

8. Malaysia Fleet Tonnage: UNCTAD STATISTICS; Balance of Payment for Transportation: Ministry of Finance Malaysia 1998-2014.

9. The Star, 12th March 2016: "Revival hope floats on shipping master plan" Currently, a new masterplan has been drafted named "Malaysian Shipping Master Plan" (MSMP) to revive and improve the current challenge facing by domestic shippers to further revitalising the shipping industry and maritime sector in Malaysia through structured strategies from holistic representatives, in order to strengthen and ensure a dynamic and sustainable industry.

10. Hellenic Shipping News Worldwide, 2nd Nov 2015: Malaysian Shipping Master Plan to be completed by end 2015"

11. The Star, 5th April 2014: "Leveraging on Logistics Strength"

12. The Star, 10th July 2009: "Move to address trade imbalance"

13. Government initiatives to help low cost shop.

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Appendices

Appendix 1: The guided questions asked during interview

No.	Question
1	Based on your knowledge and information at your disposal, what are the main developments in the maritime industry since 2009 with respect to: a. Domestic seaborne trade, the number of containers transported the overall tonnage of the nation fleet; what were the effects from the economic crisis and are there already signs of recovery? b. Market position of the Malaysian maritime industry? How would you describe the current competitive situation of the various shipping companies in the maritime sector?
2	What are the legal, technical or administrative barriers to register a ship?
3	What characteristics are making the maritime sector unique from the perspective of governmental aid? What are the substantive governmental aid rules which you judge necessary in view of these characteristics?
4	Which are in your opinion the market failures present in the maritime transport industry, which have been successfully addressed by the current government measures and which are the ones that have not been addressed successfully? What is in your view the most effective way to address the market failures present if it is happen in the maritime transport industry?
5	Do you think that there are positive or negative externalities associated with flagging-in vessels under Malaysia flags?
6	Do you consider that governmental aid measures are necessary improve the current maritime industry period?
7	Is competitive price can be considered as one of important factors to select a shipping company?
8	How do shipping companies impose the freight rate or carriage cost? (destination/ volume/ type of goods)
9	Can you explain about the phenomena of trade imbalance happened between East and West Malaysia? Is it because of the market power between shipping companies or other factors? (policy, exporter-importer’s demand etc..)
10	What is your opinion on cabotage policy? To what extent did the cabotage policy contribute to/ hamper the evolution in maritime industry and the domestic trade?
11	How has maritime companies’ business models evolved since the adoption of cabotage liberalisation in 2009?
12	Which are, in your view, the likely developments and where do you see the major challenges for the maritime sector in the short (during the next year) and medium term (in the next 3 years) future. Do you see possible implications regarding the cabotage policy?