



China's Use of Maritime for Global Power Demands a Strong Commitment to American Maritime



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EXECUTIVE SUMMARY

The importance of a strong American commercial maritime industry has been a constant throughout our nation's history. Laws, policy and practices have been instituted since the earliest days of our country to keep U.S. waters more secure. The case for laws like the Jones Act, the fundamental law of the American domestic maritime industry, has only gotten stronger as rivals like China have publicly built their strategies for global power around control of the maritime sector.

INTRODUCTION

America has been guided by the waterborne trades and the laws of maritime commerce since its founding. Shipbuilding and the generations of mariners in the shipping trades are pillars of our maritime and naval heritage.

In that spirit, Americans have always gone to great lengths to protect the nation's ports and sea lanes. Early on, American merchants abided by Navigation Acts fashioned by the English government to protect British Colonial interests. Today, American maritime law and the commercial maritime trades are informed by a set of laws, including the Jones Act.

In 2020, the Jones Act, also known by its formal title, the Merchant Marine Act of 1920, celebrated 100 years of enduring success. The law has effectively protected the nation's 95,000 miles of coastline and inland waterways, limiting inland access by foreign vessels and crews, while U.S. mariners serve as its eyes and ears to strengthen border and homeland security and ensure a strong national maritime industry infrastructure.

The Jones Act, by definition a type of cabotage law, ensures that only American-built, American-owned and crewed, and American-flagged vessels can operate in domestic commerce. This requirement, in return, strengthens and supports U.S. sovereignty and security while driving economic benefits to local communities. It is worthwhile to note that cabotage, or the notion of protecting domestic coastal trade and restricting foreign maritime activity, is a common practice throughout the world, its roots dating back to the 14th century. Today, cabotage laws are widespread and exist in nearly two-thirds of United Nations maritime states, which amounts to 91 countries representing 80% of the world's coastlines. And while a fewer number of countries require ships in domestic trade be built domestically, the governments of South Korea and Japan, two of the world's leading shipbuilding countries and free-market democracies, are heavily invested in shipbuilding. South Korea has invested hundreds of billions of dollars to keep its shipbuilding industry on top over the past decade in a

whole-of-government approach, so much so that Japan sued in the World Trade Organization over unfair practices. As maritime nations, these countries clearly believe in the strategic importance of their maritime industries.

Military leaders, administration officials and bipartisan members of Congress have long supported the Jones Act and, in particular, the 130,000 men and women working directly in the domestic maritime industry. America's maritime trade is a safe and valued industry that provides capacity and manpower upon which the nation's armed forces can draw during a conflict. It guarantees that America's domestic maritime industrial base is not outsourced, but is instead benefiting the U.S. economy by sustaining \$41.6 billion in labor compensation, more than \$154 billion in annual economic output and, by extension, 650,000 U.S. jobs, according to a study by PricewaterhouseCoopers.

Because of the Jones Act, America's domestic trades are thriving, its trade lanes are healthy and the supply chain is moving, undisrupted. But times are changing. The Jones Act has endured without controversy until recently, as free-trade purists neglect the importance of logistics and a healthy defense maritime industrial base when considering future conflicts.

Opponents of the Jones Act would see the law revised or even repealed in the name of economic competitiveness and globalization. In addition, global competition is on the rise, particularly in light of China's vast military and subsidized industrial buildup for the past decade. Global markets and the supply chain have been challenged in new ways with events since the start of 2020 that brought with it a devastating pandemic, exposing the importance of keeping critical industries and supply chain partners within the domestic sphere. In short, the United States is faced with addressing its own vulnerabilities in global shipping and shipbuilding, while assuming an offensive approach in how to counter against uncertain and potentially dominant rivals and policy antagonists.



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SECTION I: AMERICA IS A MARITIME NATION

To understand what it means when we say America is a maritime nation is to take a close look at the remarkable history of domestic laws and regulations in maritime commerce that set out to benefit America's military and commercial interests and its economic security.

Today's Jones Act is rooted in practices that began when colonists started to trade in American waters. Before and after the American Revolution, the laws that governed trade were constantly evolving in order to reduce risk and economic loss. The notion of restricting all but U.S.-flagged vessels from trading between U.S. ports was introduced when American merchants began expanding their commerce around the world after the Revolution, having learned quickly that foreign vessels — largely British — needed to be restricted from America's coastwise trade.

America has also been a prolific shipbuilding country. American shipbuilding dates to the mid-1600s when shipyards along the Atlantic seaboard were constructing wooden ships for the British and, ultimately, for their own combatant and commercial ship supply. This production of vessels was paramount in preparing for rebellion against the British, helping the Colonies and American privateers prevail in the Revolution.

By the end of the 19th century, less than 100 years after the Revolution, the United States would become the world's largest economy, a designation that has not changed for almost 150 years. Today, America is regarded as the world's preeminent economic and military superpower. The U.S. Navy remains the largest, most innovative and most powerful in the world.

Between the lines, it is commerce, trade and an expanding military industrial base that lead the way. It is also the long-standing laws that guided them — laws that mandated secure coastlines and waterways; that called for strong demand for the construction of boats, barges and ships in shipyards; and laws that guaranteed secure jobs for Americans.

At the center of these laws today is the Jones Act.

THE JONES ACT: 100 YEARS LATER

A century ago, the Merchant Marine Act of 1920 was signed into law, and, with it, that legislation's Section 27, known more commonly the Jones Act. Conceived after World War I, the Jones Act sought to bolster the nation's shipbuilding and maintenance capabilities and to ensure manpower and logistics during times of conflict.

At the time, lawmakers in 1920 acted on a classic "lesson

learned” after the Great War, having realized the nation’s merchant fleet was not independently robust enough to neutralize German attacks. They established simple yet sweeping statutes that would govern the future of the domestic U.S.-flag fleet. Under the Jones Act, all vessels transporting cargo between U.S. domestic ports were to be built, owned, crewed and registered — or flagged — in the United States.

The Merchant Marine Act, including the Jones Act, was a corollary of the world’s first modern war. Lawmakers sought to establish a vision for how best to protect North America’s coastlines and trade routes, its people and its economic security. The Jones Act would serve as a guarantee for safeguarding the nation in the name of national security, utilizing and relying solely on the nation’s own resources.

NEXUS OF COMMERCIAL FLEET AND NATIONAL SECURITY

If the U.S.-flag Merchant Marine can be defined broadly as having two unique U.S.-flagged commercial fleets — the domestic commercial fleet and the international commercial fleet — both fleets, which today comprise 40,000 vessels, serve in the interest of national security, but differently. The U.S.-flag oceangoing fleet of about 184 ships includes transoceanic, or blue water, ships such as large cargo and container ships and their crews. These vessels function as carriers in surge sealift operations for moving equipment, supplies and U.S. military personnel during wartime or contingencies. From this fleet, 98 vessels, such as container and bulk cargo carriers and large oceangoing tankers, serve as Jones Act-compliant ships.

The U.S. domestic component of the fleet, guided by statutes of the Jones Act, provides thousands of skilled mariners who, during surge sealift operations, can operate government-owned sealift vessels and provide supplemental crews on international fleet ships. The remainder of the domestic fleet is made up of the smaller commercial vessels like fishing trawlers, dredging ships, coastal cargo carriers, barges and tugboats — the variety of vessels and barges seen operating along American coastlines, through the Great Lakes and traveling over inland waterways.

The thousands of smaller vessels of the domestic fleet that make up the lion’s share of Jones Act vessels ply the nation’s coastlines, ports and waterways, creating something of a commercial maritime “ecosystem” that includes the mariner workforce, shipbuilding and ship operating. The diverse mix of vessels serve, collectively, as a strategic buffer that both supports the U.S. shipping industry while also providing a host of critical maritime services in our ports and waterways, as well as important national security protections.

In shipbuilding and maintenance, these vessels support and sustain the country’s small- and medium-sized shipyards.

The shipyards that build most commercial vessels ensure that capacity is available for the construction of smaller U.S. government ships, such as non-combatant military, research and law enforcement ships.

The mere presence of the U.S.-flagged vessels in the domestic fleet helps reduce the threat of illegal entry into inland waterways and deter foreign ships and mariners. They also secure the trade lanes between the contiguous United States and its noncontiguous domestic markets of Alaska, Hawaii, and Puerto Rico and guard against adversaries and foreign shippers from gaining influence and control over shipping to U.S. territories.

Without the Jones Act, foreign-flagged ships would be free to undercut competition with unfair labor practices, including dangerous onboard conditions, low pay and no controls over work hours. While Puerto Rico does import oil from the Caribbean on foreign-flagged ships, the vast majority of manufactured goods come from Jones Act routes. Hawaii also gets many goods directly from Asia, because it is more logical to do so than obtaining those imported goods through West Coast ports. In fact, a study by the Hawaiian firm TZ Economics, compiled with Reeve & Associates, found no impact on the price of consumer goods in Hawaii. The same can be said for the domestic dredging industry. The important functions of work boats like the dredgers and the salvage operators are in looking after the nation’s waterways and shipping lanes. The robust domestic dredging industry sees to the maintenance of more than 400 ports and 25,000 miles of navigation channels throughout the U.S. Because the U.S. does not have to depend on foreign companies to dredge in the harbors of, for example, its naval facilities, the requirement for U.S.-built, U.S.-operated and U.S.-crewed dredging vessels prevents a possible sabotage situation, avoiding the prospect of having foreign actors gain access for underwater surveillance of U.S. military vessels and stations.

It is the current mix of laws and policies that help preserve our place in the world. Were the Jones Act to be repealed, the U.S. Coast Guard and Customs and Border Protection (CBP) would be required to ensure foreign mariners are properly vetted at hundreds of inland waterway locations — a prospect that is, at best, highly complex. Currently, foreign-flag vessels may enter inland waterways but can only dock at ports with a CPB facility and must provide a minimum of 24 hours of prior notice to the Coast Guard. In fact, no comprehensive legal framework has ever been considered to address a significant flow of foreign-flag vessels in U.S. inland waterways. Presumably, foreign commercial vessels, according to a number of industry experts, would need to abide by U.S. shipping regulations and laws, thus, giving rise to another cumbersome layer of enforcement by the CBP and Coast Guard.



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SECTION II: GLOBAL COMPETITION IS ON THE RISE

If the United States is the world's largest economy, China is the world's No. 1 trading nation. Ninety percent of the world's global trade travels by ship, and nearly two-thirds of global container traffic moves through Chinese-owned or invested ports. With a massive economy that is expected to exceed \$22 trillion in 2020, America is increasingly dependent on foreign countries to carry goods to its major coastal ports.

In today's interconnected and more competitive world, there are many nations that would opt out of relying on the American marketplace for reasons to do with cost, prescriptive trade regulations and geographic inconvenience. There are adversaries who may wish, for political reasons, to see America fail or succumb to another rising global superpower. And still, there are other developing nations across the globe looking to improve their economies and livelihoods that are willing to establish stronger ties with closer trading neighbors like China and India.

America's unrivaled allure has dissolved in an increasingly unsettled international system. Add to that the fact that 2020 marked the year in which citizens across the globe were faced with a virus pandemic the scale of which the world has never seen. What was once but a narrative in military scenario planning, the SARS-CoV-2 pandemic devastated governments and communities on every continent and brought to their knees more than half of the largest countries in the world (SARS-CoV-2 is the virus that causes the disease known as COVID-19).

With no end in sight but for resignation to the "new normal," the past year has been wildly unpredictable. Americans are facing massive unemployment and the prospect of a depressed economy akin to the 1930s. Furthermore, the recent behavior of China, including its increasing aggression in the South China Sea and the Chinese government's much-touted Belt and Road Initiative (BRI), demonstrate that China's intentions are intensely competitive.

SECTION III: CHINA, A CASE STUDY IN MARITIME COMPETITION

Critics have stated that the SARS-CoV-2 outbreak underscores the dangers of depending on China for pharmaceuticals or its capacity to keep the supply chain from being disturbed if factories abroad become idle. In a congressional hearing about China's Maritime Silk Road Initiative before the House subcommittee on Coast Guard and Maritime Transportation in October 2019, Carolyn Bartholomew, chairwoman of the U.S.-China Economic and Security Review Commission, said, "China is the world's largest exporter and second-largest importer, so its investment in ports helps facilitate China's global trade footprint. By owning and/or operating a network of logistical nodes across Asia, Europe and Africa, China can control a significant portion of its inbound supply chain for essential commodities and outbound trade routes for its exports. ... In the event of a conflict, China could use its control over these and other ports to hinder trade access to other countries."

Analysts have recently shed light on the Chinese government's investment in global shipping and shipbuilding, showing how far the U.S. government has fallen behind in promoting and investing in its own domestic maritime industry, particularly in building oceangoing vessels. In a brief released by the Center for Strategic and International Studies (CSIS) in June 2020, "Hidden Harbors: China's State-Backed Shipping Industry," the combined state support to Chinese firms in shipping and shipbuilding between 2010 and 2018 totaled about \$132 billion through about \$5 billion in state subsidies and \$127 billion in financing from state banks. Importantly, CSIS makes clear in its brief that, given China's inherently opaque practices with regards to banking, regulatory and financial disclosures, the figures presented, while stunning, are most likely conservative estimates drawn from facts and data available.

To China's way of thinking, the country is poised to become a global superpower in part by dominating the global maritime supply chain and, subsequently, competing head-on to become one of the world's most modern and powerful naval forces. However, while China continues to grow its shipping and shipbuilding exponentially, its heavily government-subsidized investments run afoul of what most other industrialized nations would do to bolster a global shipping industry. In other words, it is difficult to compare subsidized industry investments to those that are not subsidized.

Bartholomew cites the industrial policy that informs China's growth: "The Chinese economy is not a free market. It is a state-managed economy with an industrial policy. The Chinese government is transparent in its plans and goals. When it identifies strategic sectors, it uses a whole-of-government approach to build them up."

Meanwhile, America must grapple with how best to strengthen its much smaller, independent and privately owned shipbuilding industry in the name of national security. Moreover, it must do so while competing with a nation that has explicitly written into its Communist Party Constitution a decree outlining the BRI, which is, in essence, an unyielding vision for global expansion of its own domestic maritime industry.

China's escalation in the past decade into global shipping and shipbuilding is astonishing. Since the Chinese gov-



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ernment rolled out its BRI in 2013, little expense has been spared by China's President Xi Jinping in terms of carrying out what business experts see as a "global shopping spree" of ports and shipping service industries around the world. According to CSIS' Hidden Harbors brief, "China's Belt and Road Initiative ... has deepened pre-existing market access and secured new beachheads for Chinese shipping companies abroad. Led by state-owned shipping operators COSCO Shipping Corporation and China Merchant Group, Chinese companies have invested an estimated \$11 billion into overseas ports between 2010 and 2019, including 25 projects across 18 countries."

It is hard to deny China's rise as a global superpower, central to which is the building up of its naval forces. Experts agree that shipbuilding is one of the areas where the Chinese have made massive investments as a national security strategy. Much like the Japanese after World War II and Korea a generation later, where they invested in heavy industries, steelmaking and shipbuilding to boost their economy and propel them into the powers they have become, the Chinese are, in the context of building up their industrial base, notoriously known for mimicking the strategies of successful nations — in this case, America's rise by means of its maritime power.

Regardless, the Chinese have been immensely successful. According to industry observers, China understands it is critical as a national security issue to maintain a heavy industry in shipbuilding, in particular because it drives a range of other industries that are necessary to maintain a high level as a producing nation. Furthermore, the capabilities to build commercial ships are the ones that the Chinese are using to be able to mass produce their Navy ships.

Where the United States is concerned, China's maritime

power has far-reaching implications. With the majority of world trade traveling by sea, and in the event of a contingency with China, states CSIS, "The United States could face maritime logistics challenges during a major contingency given the shrinking size of the U.S. merchant fleet. China, in contrast, could draw upon superior numbers of state-owned vessels and the world's largest maritime workforce. COSCO is widely recognized as the maritime supply arm of the People's Liberation Army [PLA]."

Furthermore, China has not ceased to expand its maritime footprint into the South and East China Seas, adopting a more hardline approach. In the past few years, China has deployed naval bases more or less without conflict or interruption to its own military infrastructure buildup, despite unanimous arbitration against the Chinese government in 2016 for encroaching on the Philippines' Exclusive Economic Zone by occupying land features in the Spratly Islands. Ideally, according to Gregory Poling, director of CSIS' Asia Maritime Transparency Initiative, "China would transform both of these seas into Chinese lakes based on the boundaries of the Nine-Dash line, giving China complete control over the two regions."

Between 2008 and 2018, according to CSIS research, China became the world's most powerful shipping financier. Prior to 2008, there were no Chinese banks among the world's top shipping investors, and by 2018, three of the top 15 shipping portfolios were held by Chinese banks. The "Hidden Harbors" report reveals, furthermore, that China not only uses direct subsidies to fund and expand its shipping industry, the government has conceived of increasingly sophisticated financial tools, among them equity infusions, lending and leasing programs. As of 2018, the business volume of China's state-owned banks and leasing companies totaled an estimated \$127 billion.

Among some of its programs, China, since 2014, as a way of encouraging fleet upgrades and the demolishing of older vessels, instituted a "scrap and build" program that allowed companies to receive a subsidy even before they commissioned a new ship. The subsidy, which has since been phased out, served its purpose, according to a CSIS brief, "While in operation, it helped boost not only China's fleet modernization but also domestic shipbuilding and shipbreaking yards, which were the downstream recipients of government support."

China is not alone in providing subsidies to boost shipbuilding. India, France, Japan and South Korea have used subsidies in recent years to sustain, protect or bailout shipyards and shipping investments. The United States, meanwhile, plays



by completely different rules, as subsidies for commercial shipbuilding ended nearly 40 years ago. Only small loan guarantees and grants for smaller shipyards exist today.

China's goals, beyond creating jobs and expanding its economy, are aimed at dominating the shipping industry and world trade. Through its state-owned enterprises, China has, in the past two decades, managed to dominate the world's core maritime industries, namely shipbuilding, majority ownership of oceangoing commercial ships and ownership or part ownership of marine terminals at key ports on strategically important trade lanes. China can shape global trade to its liking in times of peace and, in times of conflict, leverage an overwhelming advantage in global maritime logistics built up primarily at the expense of U.S. importers.

U.S. maritime stakeholders are well aware of the challenges America faces in shipbuilding and in global shipping. The U.S. has seen a sharp decline in its international maritime fleet, whereby less than 200 U.S.-flagged vessels are represented in an oceangoing cargo fleet of more than 41,000 ships.

The U.S. trails 16 countries in shipbuilding by a disparate proportion. In 2019, China ranked highest with 1,291 ocean-going ships under construction, while Japan and South Korea were the next largest shipbuilders but with each having roughly half of that number of vessels in production. The U.S. was building only eight oceangoing vessels in 2019. The

loss of blue-water U.S.-flagged vessels over the last decades has also resulted in the loss of thousands of mariner jobs.

Historically, China's maritime dominance has focused on international shipping. Recently, however, there has been a growing recognition that the Jones Act is central to deterring inevitable efforts by China to enter U.S. domestic maritime markets if the U.S. coastwise laws went away.

In a comprehensive 2020 study by the Center for Strategic and Budgetary Assessments, “Strengthening the U.S. Defense Maritime Industrial Base: A Plan to Improve Maritime Industry’s Contribution to National Security,” the Jones Act is described as guarding “against the ability of China ... to take over shipping to U.S. territories and to gain local influence during peacetime, only to threaten or deny shipping to CONUS [contiguous United States] during a crisis or conflict.”

As this investigation demonstrates, China is investing heavily in its maritime capability to support its goals of global, geostrategic dominance. There is reason to believe that China's progress would not be as effective if it ignored the maritime sphere. China's investments in all aspects of the maritime domain, from shipbuilding to international shipping, are a challenge to the United States, if not a warning that America cannot rest on its history and must continue to prioritize, invest in and protect its own domestic maritime industrial base.



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RECOMMENDATIONS FOR A MARITIME NATION

The United States is a tapestry of rivers, waterways and coastlines. It is not lost on America's allies — and adversaries — that its wealth of natural resources have afforded the nation unparalleled growth, as well as physical and economic autonomy. The demonstrable conclusion is that government policy continues to vigorously protect our coastlines and inland ports, harbors and waterways, and one way by which the U.S. manages to do this is through the Jones Act.

Opponents of the Jones Act suggest the U.S. shipping industry would save millions of dollars a year by turning over domestic cargo to foreign fleets. Likewise, they state that the cost of doing business in the U.S., particularly in the shipbuilding arena, is expensive, and, likewise, that opting for less-regulated “flags of convenience” over U.S.-flagging is cheaper and easier.

Where shipbuilding is concerned, the challenge is complicated. Opponents of the Jones Act have long complained about the costs of building vessels in the U.S. and would just as soon see the industry become fragmented. In the context of China’s state-sponsored investments in shipbuilding, the CSIS brief raises the question: “Compared to what?”

In other words, state-supported shipbuilding by China and the other top shipbuilding nations make cost comparisons to the U.S. shipbuilding industry incongruous at best. But U.S. strategy has been to rely on these shipyards to be converted to military use whenever necessary.

Military leaders understand the critical security ramifications of maintaining U.S. shipyards. One need only look to Canada, Australia and the United Kingdom as examples of what happens if a nation does not protect its domestic shipbuilding industry. These NATO-allied countries saw their shipbuilding industries shrink so much that they were confronted with having to reconstruct and, at massive expense, recapitalize their naval and coast guard fleets.

It is clear that the Jones Act plays an important role in keeping American shipyards operational when competing against heavily subsidized foreign yards. The Jones Act also ensures a healthy domestic inland water fleet, thousands of mariner jobs and a strong defense maritime industrial base.

By prioritizing the defense maritime industrial base, maritime stakeholders are conceiving possible approaches for counteracting America’s apparent vulnerabilities. In context, any weakening of the Jones Act would diminish

the nation's seafaring and shipbuilding industrial base and make America less secure.

To stem the decline of U.S. shipping in foreign trade, boost mariner employment and provide additional work for U.S. shipyards, military and shipping industry experts must focus on reinvigorating the blue-water vessel industry. Stakeholders should look closely at recent projections, for example, that indicate a need for at least 60 new military-useful oil tankers that would be required in a future contingency with China to support dispersed forces and advanced bases — a major undertaking that would begin to revitalize U.S. shipbuilding.

Moreover, current cargo preference laws should not only be continued, but expanded. By exporting a percentage of liquefied natural gas (LNG) and crude oil on U.S.-built and U.S.-registered ships, this approach can stem the decline of U.S.-flag ships. Such is the case with pending bipartisan legislation in Congress, known as the Energizing American Shipbuilding Act. The bill, sponsored by Rep. John Garamendi (D-Calif.) and Sen. Roger Wicker (R-Miss.), seeks to recapitalize the U.S. domestic shipbuilding industry through a requirement that a percentage of LNG and crude oil volumes be transported on U.S.-built, flagged and crewed vessels. The legislation aims to spur the construction of new ships, which, by extension, could generate thousands of new shipyard jobs, while positively impacting the domestic production side of the U.S. manufacturing and maritime industries.

Another alternative previously explored by the Navy is the option of supporting the development of coastwise services of dual-use vessels, or commercial ships with military utility, including roll-on/roll-off (RoRo) vessels, trailerships or the hybrid ConRos, which are vessels that combine features of RoRos and container ships. Such ships would alleviate ground transportation congestion while also being quickly available to support a major deployment of military equipment through participation in the Voluntary Intermodal Sealift Agreement program — a program in which 73% of the non-tanker Jones Act fleet participates.

In the context of China's goal of dominating the global maritime supply chain, the United States and its allies must develop and implement a strategy to deny China success. It must be a whole-of-government and whole-of-industry approach. We must take inventory of today's American maritime industry, preserve what we have, identify what we need and chart a path forward. It is not a question of matching dollar-for-dollar Chinese government financial support. It is more a question of how we and our allies scale up our defense maritime industrial base to prevent China from achieving the hegemony it seeks through its maritime investments.

The Navy League of the United States is a nonprofit organization dedicated to educating our citizens about the importance of sea power to U.S. national security and to supporting the men and women of the U.S. Navy, Marine Corps, Coast Guard, and U.S.-flag Merchant Marine and their families.



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