



Maritime Piracy: Implications for the Emerging Market Countries

As the global economic crisis continues on its unpredictable path, the Emerging Market (EM) countries are still waiting to see what will be the full extent of the economic backlash on their economies. In the meantime, one issue in particular seems to be clawing its way to the top of several EM countries' list of priorities- Maritime Piracy- which appears to be greatly affecting countries such as Brazil, China, India, Indonesia, Malaysia and the Philippines.

The issue of piracy is quite an old one, existing for as long as trade has been conducted across territories. However its recent revival is of major concern given the fact that the industry threatened by pirates is now worth over US\$7 trillion annually. In January 2009, a Saudi Arabian supertanker carrying two million barrels of oil and twenty-five crew members was released for a ransom of US\$3 million after being held captive for almost two months by Somali pirates. The hijacking proved to be the most ambitious and successful undertaking to date (the largest and most valuable vessel ever hijacked), but more importantly it alerted the world to the reality that the strength and reach of the pirates was increasing. That particular attack required the pirates to travel for three to four days out to sea, and revealed their operating scope to be in an area of over one million square miles. The Somali pirates' scope of operation placed them beyond the range of the international patrols in the Gulf of Aden where this particular attack occurred, and further proved that today's pirates were in fact an efficient and well-equipped group of organized criminals capable of disrupting the free flow of global trade and costing the rest of the world billions of dollar each year.

Maritime Piracy: the Current Situation

Maritime Piracy can be simply defined as an attack by a non-governmental vessel against another vessel on the high seas or even in port, with the intent to commit theft or any other crimes for private gain. At its core, piracy is economically driven and emerges as a viable option especially in impoverished and destabilized countries that are unable to effectively combat these acts. Acts of piracy have continued to occur in the five main regions of the World (West Africa, East Africa, Indian Ocean, Central and South America and the Caribbean). These regions not only contain several of the World's emerging economies, but also several of the more socio-economically challenged countries with enough political instability to create an adequate window of opportunity for pirates to make a profit that sufficiently outweighs the risks involved in these criminal acts.

The world's pirates have been very busy generating a total of 1,845 actual or attempted attacks between 2003 and 2008. This figure is only a glimpse of their activity since a significant number of attacks are not reported in an effort to avoid increasing maritime insurance premiums and the costly investigations associated with such an incident. The estimated

financial losses for the shipping industry as a result of piracy now average US\$8 to US\$16 billion annually; while the annual value of maritime commerce is US\$7.8 trillion dollars. When compared, the losses are not a significant portion of the industry's total value; however they are quite significant to the individual shipping companies and ship owners who then have no choice but to pass on these costs to consumers.

Economic Implications of EM Countries

In 2008, the total world merchant fleet comprised 44,553 ships and the average tonnage growth from the previous year was 6.5%. These ships have become increasingly more vulnerable as the volume of commercial freight transported via ocean has continued to grow annually. This mandated that ships continue to make the trek through congested and ambush-prone maritime passages such as the Malacca Straits, Gulf of Aden and the Suez Canal that have become pirate hotspots.

The EM countries play a major role in the Maritime supply chain as several of them are key natural resource suppliers (Brazil), food suppliers, manufacturing giants (India and China). Southeast Asia (Philippines and Malaysia) is home to one of the busiest shipping lanes in the world (Malacca Straits); while China, India and Russia have insatiable imports due to their immense size. The most obvious economic implication for EM countries and the world at large is the passing on of costs to consumers due to the losses directly incurred by the attacks. Once attacked, the shipping company incurs the cost of the stolen cargo and often stolen ship, or payment of ransom for crew and ship. Aside from these losses there are also the costs associated with delays in port while the attack is investigated, and the replacement costs for the disrupted shipment.

When the company resumes its shipping operation there are often increased maritime insurance rates. For example, the current premium for a ship transiting the Gulf of Aden near Somalia is estimated at \$20,000 per ship per voyage excluding injury and ransom coverage; while a year ago insurance premium for the area was \$500. Further costs are picked up in pre-emptive actions such as hiring private security services, equipping ships with non-lethal deterrent equipment and the additional training and technology provided to crews to combat the threat.

The other option in the fight against pirates is to avoid these hotspots altogether, however this is also quite costly. In an industry where time is highly valued, rerouting high value consumer goods leads to costly delays to the consumer, in addition to the added fuel and operational costs generated by simply increasing a voyage by a few days. Overall there is a reduction in the delivery capacity for the ship which may force a shipping company to acquire additional ships in order to maintain their service frequency. In the cruise industry there is an extreme case of rerouting as several companies are now disembarking passengers at safer ports before the ships pass through pirate hotspots, and flying the passengers to re-join the ship once it has safely passed through the particular area. While the costs incurred still outweigh the risks, the increase has to be passed on to the consumer.

Another direct economic impact of piracy on those EM countries that exist with hotspots is the undermining of their trading ability. Pirate attacks within their jurisdiction make trading with these countries more expensive and therefore less favorable. These countries also tend to sustain damages to their overall international relations, since the issue of piracy often highlights the presence of elements such as corruption, fraud and instability amongst the country's government

officials and bureaucrats. The EM countries often lack the human and monetary resources to truly combat piracy. In order to mitigate these new risks, these countries are now being forced to seek out and re-allocate resources to improving their ability to protect their waters, their assets and their people. These costly upgrades usually include new boats, weapons, training, surveillance technology and the costs associated with creating new policies and treaties to aid in the fight against piracy.

Finally, the impact of the human costs associated with maritime piracy is climbing. Pirates are becoming more violent and the trend of hostage taking is also becoming more prevalent. Since 1995 at least 350 sailors have been killed, along with the casualties of military personnel and civilians related to pirate attacks.

Conclusions

When it comes to the problem of maritime piracy, the stakes are very high for the EM countries. Their reliance on maritime commerce for the sustenance and expansion of their economies is non-negotiable, but the rising costs associated with piracy are threatening to wreak havoc on the industry, and by extension, the world economy. While the United States and the European Union have already formed Combined Task Forces to protect their various interests, it is necessary for the EM countries to continue and increase their support and involvement in these combative exercises in order to help mitigate the costly implications piracy is having on their economies.

FINANCIAL & ECONOMIC INDICATORS

As at 18 June, 2009

<u>Exchange Rate/US\$</u>	<u>Closing Value</u>	<u>Previous Week</u>
Yen	96.35	97.63
Euro	1.40	1.39
Jamaica	89.13	88.73
Guyana	204.90	203.20

<u>Commodity Prices</u>	<u>Closing Value</u>	<u>Previous Week</u>
Crude oil (US\$/bbl)	71.09	72.68
Natural Gas (US\$/mmbtu)	4.01	3.51
Gold (US\$/Troy Ounce)	933.96	953.95

Eurobond Indices (As at 18-June-09)

Lehman Brothers Global Aggregate Index (Return % YTD)	0.50
JP Morgan EMBI+ (Basis points)	435
JP Morgan Central America and Caribbean Index (CACI) (YTD return %)	19.02

<u>Policy Interest Rates (%)</u>	<u>Closing Value</u>	<u>Previous Week</u>
United States	0.25	0.15
Euro Zone	1.00	1.00
Japan	0.10	0.10
Brazil	9.25	9.25
Trinidad	8.00	8.00
Jamaica	17.00	17.00
Barbados	3.00	3.00

<u>Market Interest Rates (%)</u>	<u>Closing Value</u>	<u>Previous Week</u>
US 90-day T-Bill	0.17	0.17
US 10-Yr Treasury	3.82	3.86
3-month UK Libor	1.25	1.25
Japan 90-day T-Bill	0.33	0.33
Brazil 90-day T-Bill	9.29	9.68
TT 90-day T-Bill	2.60	2.60
Jamaica 90-day T-Bill	19.21	19.21
Barbados 90-day T-Bill	3.96	3.96

Sources: Bloomberg, CMMB, Central Bank of Trinidad and Tobago, Bank of Jamaica, Central Bank of Barbados, www.lehman.com

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