

Statement of

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Supporting Improvement of and Funding for the Title XI Loan Guarantee Program

Before the

Subcommittee on Seapower and Expeditionary Forces
Committee on Armed Services
United States House of Representatives
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Mr. Chairman and Members of the Subcommittee:

I am Chuck Raymond, President and CEO of Horizon Lines. Horizon Lines is the nation's leading Jones Act container shipping and integrated logistics company. We operate 16 U.S.-flag vessels on routes linking the continental United States with Alaska, Hawaii, Guam, and Puerto Rico. All Horizon Lines vessels are U.S. citizen owned and crewed.

Our vessels are enrolled in the VISA program, which is a Marad run readiness program that makes private U.S.-flag vessel capacity available to the Department of Defense. We also proudly carry cargo for DOD, other government departments, and numerous commercial customers.

Horizon Lines appreciates the Subcommittee's invitation to discuss how the program of loan guarantees for ship construction, established by Title XI of the Merchant Marine Act, 1936, relates to our ability to construct new U.S.-flag vessels for use in commercial trades. The short response is that the Title XI program is critical to the long-term viability of the Jones Act fleet and the program could work far better than it does today.

Horizon Lines supports a well functioning and well funded Title XI program. A strong Title XI program will strengthen the national defense by strengthening the circumstances of ship operators, shipyards, maritime labor, and shipyard workers. New vessel construction means more modern U.S.-flag vessels and U.S. shipyards – both better able to face future challenges and assist DOD. To have these positive impacts, the program needs to be consistently funded and the terms and conditions of its use should be made less daunting to its private sector customers. It is not enough for the program to receive sporadic drips of funding. In recent years it has not received funding, period.

The current state of the Title XI program makes it difficult for shipyards or vessel operators like Horizon to plan commercial vessel construction programs. In the rest of my statement I will comment on these problems and suggest steps to improve this situation.

The Record Shows that Title XI is Very Important To the Jones Act Containerized Trades

Mr. Chairman, Title XI is very important to a commercially successful shipbuilding program for all Jones Act operators.

Title XI loan guarantees supporting a new vessel construction program provides a company like Horizon Lines at least three distinct benefits over commercial financing. First, Title XI provides a longer payback period better matched with new vessel life. Second, Title XI provides a higher advance rate, reducing the equity requirement to a manageable level. Finally, Title XI results in a lower interest rate.

At Horizon Lines, we put a lot of effort into business planning as well as execution. We are often looking at possibilities for new vessel construction. What we've found in our business modeling is that potential building programs will not work well for us without Title XI financing. Title XI financing would allow us to accelerate potential newbuilding programs and make any such programs more competitive.

We don't see this as any kind of aberration. A few years back, when the Title XI program was funded and loan guarantees were available, other major Jones Act carriers in the containerized trades acquired new vessels with Title XI support. We do not recall seeing, in recent years, any major vessel construction program in those trades that did not include Title XI support.

This pattern shows us that the availability of Title XI support is important to the future of the Jones Act containerized trades and our nation's ability to build large commercial vessels.

So, action should be taken to revitalize the Title XI program. Here are our suggestions.

A More User Friendly Program

In preparing for this hearing I took a look at the Marad website entry under the Title XI program. As of last Friday it set forth the following under the heading "Purpose of Program":

The primary purpose of the Program is to promote the growth and modernization of the U.S. merchant marine and U.S. shipyards. The Program enables owners of eligible vessels and eligible shipyards to obtain long-term financing with attractive terms.

We need to get back to actually implementing that purpose. And, in saying that, I want to be clear that we recognize that Administrator Connaughton and Secretary Peters have

been in office only a short time and that the circumstances we are in as to title XI developed over a longer period of time.

One of the first steps in revitalizing the Title XI program should be an effort to make the program more user friendly. We all recognize that the government has a fiduciary duty to the taxpayers to run the program well and carefully. Accountability in the program is important. But it seems to us there is also a duty to help strengthen the merchant marine, the shipyards, the economy and the national defense. We must pursue those goals and can do so while being careful with the taxpayers' money. It is our sense that the Title XI program is now suffering from an overreaction to one program default in 2001.

In particular, we see a risk that applicants for Title XI support will face inflexible application of debt equity ratio and other unrealistic financial standards in the review of requests. The profitability of the company, its track record, and whether the line of business has been long established, rather than new, could receive inadequate weight. Applications from companies with a long standing track record of success and profitability, in established trade lanes and lines of business, should not get caught up in an application process that may be skewed towards risk avoidance to the point of loan guarantee avoidance.

We believe that applications for replacement of older, increasingly obsolete vessels of established operators, with terms that would protect against overtonnaging a market (to help limit default risk), do not present risks that warrant new or unusual review or review outside of Marad. Marad has many years of expertise and experience with the existing U.S.-flag vessel owners and operators to administer a program for replacement of old tonnage. Applications for Title XI support for such replacement vessels would represent a logical starting point for revitalization of the program; they should be given priority consideration under the Title XI program. Amending the law to specify that such applications would receive priority could do this. While Marad must review them carefully, they should not be subject to inflexible standards as to how a company must structure its finances. Replacement vessels for established Jones Act carriers of containers received Title XI support in the relatively recent past and do not present a meaningful default risk. Yet, in today's environment, it is not clear that comparable applications could be approved. We think that a new legislative priority provision, focused on established operators, in established trades, for the replacement of older, obsolete vessels, would be a prudent way to get the ball rolling and generate new construction at low risk. It would advance the program's goals of strengthening both vessel operators and shipyards.

Regular Funding for Title XI is Essential

Even if the Title XI program is made more user friendly, the defense and other benefits of the program will not be realized without regular funding at an adequate level.

Without annual funding for Title XI, effective planning and execution of vessel construction programs is close to impossible, at least in the containerized Jones Act

trades. It is not reasonable for the Federal Government to assume that U.S. shipyards can develop plans to build vessels, or series of vessels, not knowing when, if ever, the financial support will become available that will enable a carrier to place an order. A vessel operator like Horizon Lines needs to develop its acquisition plans carefully, with a close eye on marketplace conditions. We want to build when it makes sense to build commercially. We can't readily jump to sign contracts for newbuildings because, all of a sudden, Title XI money is available on a one shot basis. We need a program that is functioning regularly that carriers and shipyards can count on. That framework will encourage carriers to plan to renew their fleets and shipyards to invest in modernizing their infrastructure.

Defense Benefits

Before closing let me emphasize that there will be real benefits from making the Title XI program more user friendly and providing it regular funding.

Shipyards and shipyard workers are important components of the defense industrial base. They build and repair ships for the Navy. By building major vessels for the merchant marine, they expand the pool of vessels available to assist DOD. In addition, those operating ships provide an important pool of trained sailors and shipboard personnel, available for support of DOD. A more modern Jones Act fleet is able to support DOD more efficiently. A modernized fleet can give planners greater confidence that the merchant marine will be there for the long term to assist DOD.

A stronger Jones Act fleet for the long term provides a base of customers that will enable shipyards to modernize, both with respect to Navy and commercial buildings. In turn, more modern shipyards are better equipped to respond effectively to DOD's needs.

What we see, Mr. Chairman, in a decision by Congress on whether to fund and improve the Title XI program, is a choice between a descending spiral and an upward trend. Developments in the Jones Act fleet and in the shipyards interplay with each other. A step up can lead to other steps up. Failure to invest is another story altogether.

Vessel operators and shipyards, including their workers, are a tremendous resource to the national defense. We should strengthen them through revitalization of the Title XI program.

Conclusion

I have outlined today that Title XI support is very important to the renewal of the Jones Act container trades. The record shows that. Yet, today, the program is a proverbial ship that has run aground. We don't know if it will be there when it is needed.

To refloat the ship, we need to make the program less daunting to its customers and provide it regular funding. We can be careful with the people's money and still pursue Title XI guarantees that will revitalize both vessel operators and shipyards. Failing to

fund the program is not the answer. In particular, we see providing statutory priority to applications for replacement of older, increasingly obsolete vessels, by established operators, in established trade lanes, as an approach that can produce high benefits at low risk. This -- and funding -- is a logical first step to get the program going again.

Thanks again for the opportunity to appear. I'll be pleased to respond to any questions you may have.
