

Submission

by

Business|NZ

to

Charles River Associates (Asia Pacific) Ltd

on the

Ports – Market Power Study

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PORTS – MARKET POWER STUDY
SUBMISSION BY BUSINESS NEW ZEALAND

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1. Introduction

- 1.1 This submission is made on behalf of Business New Zealand, incorporating regional employers' and manufacturers' organisations. The regional organisations consist of the Employers and Manufacturers Association (Northern), Employers and Manufacturers' Association (Central), Canterbury Manufacturers' Association, Canterbury Employers' Chambers of Commerce, and the Otago-Southland Employers' Association. Business New Zealand represents business and employer interests in all matters affecting those sectors.
- 1.2 One of Business New Zealand's key goals is the implementation of policies that would see New Zealand retain a first world national income and to regain a place in the top half of the OECD in per capita GDP terms. This is a goal that is shared by the Government. It is widely acknowledged that consistent, sustainable growth in real GDP per capita of well in excess of 4% per annum (and probably closer to 7-8%) would be required to achieve this goal in the medium term. Continued growth of around 2% (our long-run average) would only continue New Zealand's relative decline.
- 1.3 New Zealand is a geographically isolated group of islands far away from all our key markets, with a mountainous terrain and a small, generally thinly spread population. These characteristics have made transporting goods and people a challenging undertaking throughout New Zealand's history. Efficient and competitive domestic and international transport services are therefore critical to the New Zealand economy.
- 1.4 Around 85% of New Zealand exports by value and over 99% by volume are carried by sea, and imports carried by sea account for around 75% by value and over 99% by volume¹. Ports are therefore a significant component of transport infrastructure, arguably no less important today than in the early years of settlement when shipping was the quickest and most reliable mode of transport even between proximate towns and cities.
- 1.5 Business New Zealand therefore welcomes the opportunity to contribute to the Ports Market Power Study. We are constrained, however, by having strongly held membership interests on both sides of what has been, and is likely to remain, a hotly debated issue between port companies and coastal shipping operators. As a result, this submission contains the views of both sides and does not make specific recommendations or take a formal position on the contentious issues. Nor do we seek to answer the detailed questions posed in Charles River Associates' 28 January letter to stakeholders.

¹ New Zealand Official Yearbook 2000, p 479.

2. Shipping Industry Review and Ports Market Power

- 2.1 Business New Zealand notes that the Ports Market Power Study has arisen from the Government's Shipping Industry Review, which reported to the Minister of Transport in December 2000. The Review considered that port companies had a *prima facie* case to answer with respect to anti-competitive practices and monopoly pricing and it recommended the Government to ask the Commerce Commission to investigate. The Government has responded by commissioning Charles River Associates to provide an overview of the ports market power issue to assist Ministers in making an informed decision on the merits of a Commerce Commission investigation.
- 2.2. While Business New Zealand welcomes the opportunity to contribute to the study, we are concerned that the Government has been very slow to respond to the report of the Shipping Industry Review. Over a year has now passed since the Minister of Transport received the report of the Review and to date the only decision to have been made has been to commission this further study. We will be watching very closely for further decisions, particularly on the contentious issues of special tax treatment for shipping and the re-imposition of cabotage restrictions, proposals that the vast majority of our membership would strongly oppose.

3. Views of Business New Zealand Membership

- 3.1 The following sections outline the views of coastal shipping companies, port companies, and shipper interests, following consultation with our membership. We strongly urge that you contact individual companies and organisations directly for more detailed information.

4. Coastal Shipping Companies' Views

- 4.1 Shipping companies hold strongly held views on the issue of ports market power. The Port Company Reform Working Group² has stated that "the abuse by some ports of their market power is becoming increasingly evident with members of this working group being totally frustrated at what they see as a monopoly service provider demanding unjustified increases in fees and charges"³.
- 4.2 Coastal shipping companies are particularly concerned about those port users that they believe are 'captive' to certain ports because of their geographic location, the type of product that is carried (generally bulk and roll-on roll-off), and the type of service that is provided. For example, a Cook Strait roll-on roll-off ferry service between Nelson and New Plymouth would not be viable

² Members of the Port Company Reform Working Group include the New Zealand Shipping Federation, New Zealand Shippers Council, New Zealand Association of Shipping Agents, and Southern Cross Stevedores.

³ Quote from a paper presented by LL Stevens QC to the Ports and Shipping Conference, Auckland May 2001.

as the only realistic choice is a service between Marlborough and Wellington because that is what the customers want.

- 4.3 Therefore, according to coastal shipping companies, port companies are, in some areas, 'virtual monopolies'. They submit that significant revenue from non-contestable pricing can be a 'cash-cow' for shareholders or used to cross-subsidise lower rates for contestable services, such as international container trade. They believe that there is evidence to support their view that dominance of ports' position is reflected by anti-competitive conduct, and coastal shipping operators consider that a lack of detailed information disclosure by port companies prevents users from being able to accurately assess the fairness and equity of pricing regimes and financial returns.
- 4.4 Concern was expressed particularly with respect to the Cook Strait trade. According to some coastal shipping operators, some port companies price their services unreasonably to those customers that have no practical alternatives. For example, one coastal shipping company complained to us that a port charges it on the basis of assets valued on replacement cost, even though there are no plans by the port to invest in new infrastructure.
- 4.5 Coastal shipping companies concede that the containerised and international trades would appear to be competitive and that many ports appear to go out of their way to compete for this cargo. In doing so, however, coastal shipping companies are of the view that these ports cut their prices for contestable ship calls and recoup their losses by charging non-contestable trade at higher rates (i.e., cross-subsidisation).
- 4.6 They also concede that while rail and road transport is effective in stimulating competition between proximate ports, particularly for international trade, this is not always practicable for certain types of coastal cargo, especially for cargo travelling between the two islands, which must in any event be transported by sea across the Cook Strait at some point in the journey.
- 4.7 Overall, coastal shipping companies consider that the generic provisions of the Commerce Act 1986 are insufficient and have failed to act as a check on ports market power. They submit that a form of industry-specific regulation is now needed, particularly for ports' 'non-contestable' business, including information disclosure and a requirement to consult users when setting prices – presumably a similar regime to that which exists for airports under the Airport Authorities Amendment Act 1997.

5. Port Companies' Views

- 5.1 Port companies strongly disagree with the assertion that they have a significant degree of market power and that they abuse what power they do possess. Ports do not consider themselves to be natural monopolies, as they see ships and cargo as being very mobile. Containers, for example, are regarded as a very contestable cargo – they can (and do, according to the port companies) move between ports. Furthermore, port companies submit that shipping companies are often major customers and have strong negotiating powers.

- 5.2 According to the port companies, there is vigorous competition between port companies and between stevedoring operations. Recent examples include Port of Tauranga's new inland port in South Auckland competing head to head with Ports of Auckland, and newcomer Mainland Stevedoring competing for business within some South Island ports.
- 5.3 Port companies advise us that they do not talk among themselves, and nor do they have any national representative organisation, as they are afraid of being accused of collusion. On the contrary, many consider that ports are actively 'stealing' each other's business.
- 5.4 Furthermore, port companies submit that the cost of alternative modes of transport often dictates the prices they charge as much as the prices set by other ports. Most port companies consider that they are competing with all other modes of transport as well as each other.
- 5.5 Responding to claims by coastal shipping companies that ports seek to attract international ship calls at the expense of coastal shipping, one port company advised us that it provides discounts on wharfage to those operators using its facilities most frequently – mainly coastal operators. Therefore, it considers that its pricing actually discriminates in favour of coastal operators.
- 5.6 Several port companies have advised us that they, or other ports, have been subject to Commerce Commission scrutiny, and most ports consider that the existing generic competition law has proved to be adequate and has sufficient 'teeth'. For example, section 36 of the Commerce Act (misuse of dominant position) was successfully tested in 1990 and resulted in Port of Nelson being heavily fined.
- 5.7 Port companies state that they have made major efficiency gains since the port reforms of 1988 and the Employment Contracts Act from 1991. As a result, Ports of Auckland, for example, has said that it has been able to postpone major port development by extracting greater capacity from existing infrastructure. It has also been able to generate returns to shareholders whilst reducing prices to its customers and paying increased taxes and rates to central and local government.
- 5.8 Regulation of ports' activities to confine them to a landlord role would, in many ports' view, be inefficient, stifle competition, and increase the power of unions. Furthermore, independent stevedoring operators believe that the current regime (where ports may provide operational services) provides adequate competition and they do not want to see a situation where two or three multinational stevedoring companies monopolise the business (as is the case in Australia).
- 5.9 Port companies also consider that requiring information disclosure would compromise commercially sensitive information, and that using Optimised Deprival Value as a valuation methodology would provoke a return to a 'cost-plus' mentality in ports management, to the detriment of both ports and their customers.

- 5.10 Some, but by no means all, port companies are of the view that further port company rationalisation is the best way to achieve further efficiencies and cost reductions for customers. In aggregate, New Zealand ports are considered by some to be over-capitalised and under-utilised. A significant reason cited is the continued local authority majority ownership and control of all New Zealand ports, which has meant parochial political interests can take precedence over what might be the best commercial option regarding a port's future.
- 5.11 Overall, port companies consider that the sector is competitive and that the existing generic competition law has been proven to be sufficient to deal with any alleged cases of abuse of market power. Port companies are strongly opposed to any industry specific regulation for the ports sector.

6. Shippers' Views

- 6.1 Few shippers chose to make their views known to us on this issue, and most that chose to respond to our consultation did not consider ports market power to be a high priority, particularly compared to other shipping policy issues. Individually and as a group, they are very much more concerned about any moves to re-impose cabotage restrictions, for example.
- 6.2 Some large exporters have advised us that they do not have any significant problems with ports, presumably because they have a significant degree of market power in their own right.
- 6.3 Some South Island manufacturers have advised us that they have encountered high costs for shipping their products between the two islands. Specifically, they report that the cost of shipping their products the short distance by sea across the Cook Strait is more expensive than the total land transport cost of the 1,350 kilometre road or rail journey between Dunedin and Auckland. Ports pricing may be only a part of this problem, however.

7. Conclusion

- 7.1 As discussed in paragraph 1.5 above, Business New Zealand is not in a position to take a formal position on the issues covered by the Ports Market Power Study, nor answer the detailed questions on market definition, market characteristics, competition, and market outcomes posed in Charles Rivers Associates' 28 January letter to stakeholders.
- 7.2 That said, however, we would be most concerned at the imposition of additional regulation on the ports sector that would put at risk the efficiency gains and cost reductions that resulted from the port and employment reforms of the late 1980s and early 1990s. There is already evidence of this occurring in the labour relations area – for example, we are particularly concerned about proposed stress and fatigue wording for the Code of Practice for Health and Safety in Port Operations, which would have the potential to severely impact upon employment arrangements and manning levels in New Zealand ports.

- 7.3 Although we would not necessarily be opposed to any form of light handed industry specific competition regulation of ports, we consider that it must first be clearly proven that the generic provisions of the Commerce Act have failed. We submit that only in that instance should the Government seriously consider such a significant move.
- 7.4 Business New Zealand therefore welcomes the Study and the opportunity it presents for a robust and principled analysis of the market conditions in the port sector. We look forward to the release of the Study report and the Government's response in due course.