House of Representatives Standing Committee on Infrastructure, Transport, Regional Development and Local Government Inquiry into Coastal Shipping Policy and Regulation CSR Limited Submission

Introduction

CSR Limited is a 152 year old leading diversified manufacturing company operating throughout Australia, New Zealand, China and South East Asia. The company operates within four divisions; Sugar, Building Products, Property Development and Aluminium.

CSR Sugar is the 5th largest sugar company in the world and operates seven sugar mills in North Queensland. In partnership with Mackay Sugar Cooperative Association Limited, it operates sugar refineries, in Melbourne, Mackay and Auckland. The division also includes CSR Ethanol which produces fuel and industrial ethanol in north Queensland and Melbourne.

CSR Building Products division is the home of Bradford Insulation™, Gyprock™ plasterboard, Cemintel™ cement sheeting, Monier™ and Wunderlich™ roof tiles and PGH™ bricks and pavers. The building products division recently expanded acquiring Pilkington Australasia and DMS Glass (now rebranded as Viridian TM).

Gove Aluminium is the owner of CSR's share in the Tomago aluminium smelter in the Hunter Valley

The role of shipping

Coastal and international shipping are key components of CSR's raw material supply chain. The company's Australian flagged shipping operation is Australia's oldest. Its first bulk carrier was bought in 1873 to carry coal from Newcastle to the sugar mills in northern N.S.W. and raw sugar on the return journey to Pyrmont in Sydney.

In 2007 the company sold its two ageing Australian-flag bulk carriers, Ormiston and Kowulka. On time charter, replacing Ormiston and Kowulka, CSR currently has the Bahamas flag bulk carrier mv Clipper Trust. She carries raw sugar and gypsum to our sugar refinery and plasterboard factories. Clipper Trust is operated under the permit system.

CSR retains ownerships of mv Pioneer, an Australian flagged BIBO (bulk in, bag out) ship which transports refined sugar on the Australian coast and internationally.

CSR Freight Task and Fleet

CSR's annual aggregate domestic freight task comprises approximately 2.55 million tonnes of dry bulk commodities and 90,000 tonnes of liquids and 65,000 tonnes of containers. These include alumina, gypsum, raw sugar, refined sugar, ethanol and molasses.. About 150,000 tonnes of refined sugar is exported annually in mv Pioneer. On ballast legs CSR seeks cargoes from shippers such as BHPB

There is potential for the dry bulk task to increase should capacity expansions be undertaken but decisions are being delayed by uncertainty about the rules relating to the proposed Australian emissions trading scheme.

In late 2006 CSR was planning the replacement of its two ageing Australian flag bulk carriers Ormiston and Kowulka with an Australian flagged Australian crewed self-unloading ship to carry gypsum and iron ore. During 2006 prices for ships (new and second hand) escalated rapidly and rendered the proposal uncompetitive. As an interim measure mv Clipper Trust was chartered at short notice on a rising freight market. She carries all of CSR's requirements for sugar and gypsum under permit. To comply with permit conditions she travels empty to Noumea four times each year

The liquids or chemical tanker market has historically been the most difficult for CSR. From about 1970 to 1985 CSR operated two chemical tankers with Australian crews. These ships carried aqueous ammonia, acid, molasses and ethanol in the coastal trade

CSR exited this trade in 1985 when volumes were insufficient to justify further employment of the ships. Since then molasses has moved by rail or in a mix of voyage-chartered ships, under permit, and a single Australian flag chemical tanker mv Stolt Australia.

Molasses is a low-value product servicing the Australian cattle feed industry and yeast industries. Although rail has been the preferred transport mode, a growing market in Melbourne has increased the demand for ocean freight. The ethanol market is evolving with growth in fuel grade product and requiring a certainty in shipping from Sarina in North Queensland to Melbourne. CSR had been a monopoly supplier in both molasses and ethanol markets and in this context the position occupied by the Australian flagged vessel was less important. Once these markets were open to competition, freight cost became an important factor in meeting the product market price.

In the thin trades for liquids the lone Australian flag chemical tanker, Stolt Australia, struggled to achieve viable volumes. The low volumes available simply meant that competitive freight rates weren't achievable. This coupled with the complexities and uncertainties in the permit system were such that CSR Ethanol invested in truck loading facilities and shifted a substantial part of the freight task from sea to road. A perverse outcome, but one this review needs to address. Product is still moved by road from North Queensland to the south. However, as expansions occur and the fuel ethanol market grows, there is potential for this task to shift back to sea. Port facilities and logistics need to be developed for this to be realised and sea freight services will need to be competitive on price, frequency and reliability.

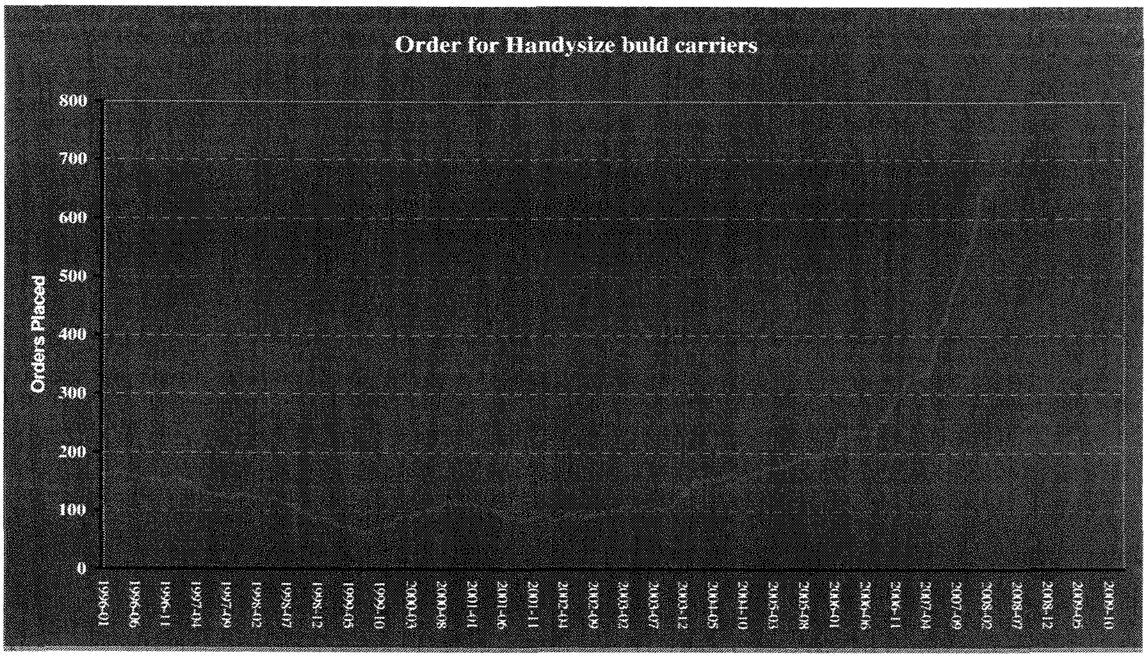
It is highly unlikely that there would be sufficient business to attract a dedicated coastal vessel – either the volume is too small or the cargo value too low to utilise a bulk chemical tanker. For instance, freight can comprise 50% of the molasses selling price. Uncompetitive freight in this market could also lead to the untimely closure of manufacturing facilities in those markets reliant on ocean freight for supply. This would lead to a concentration of production in northern states – solely on the basis of a protected shipping environment. While this could be taken into account as a public interest matter, the Ministerial (permit) guidelines are not clear on what constitutes public interest. The impact of the protection afforded the lone tanker in the bulk liquids business was such that it was more attractive to import product from Thailand, than to ship around the Australian coast.

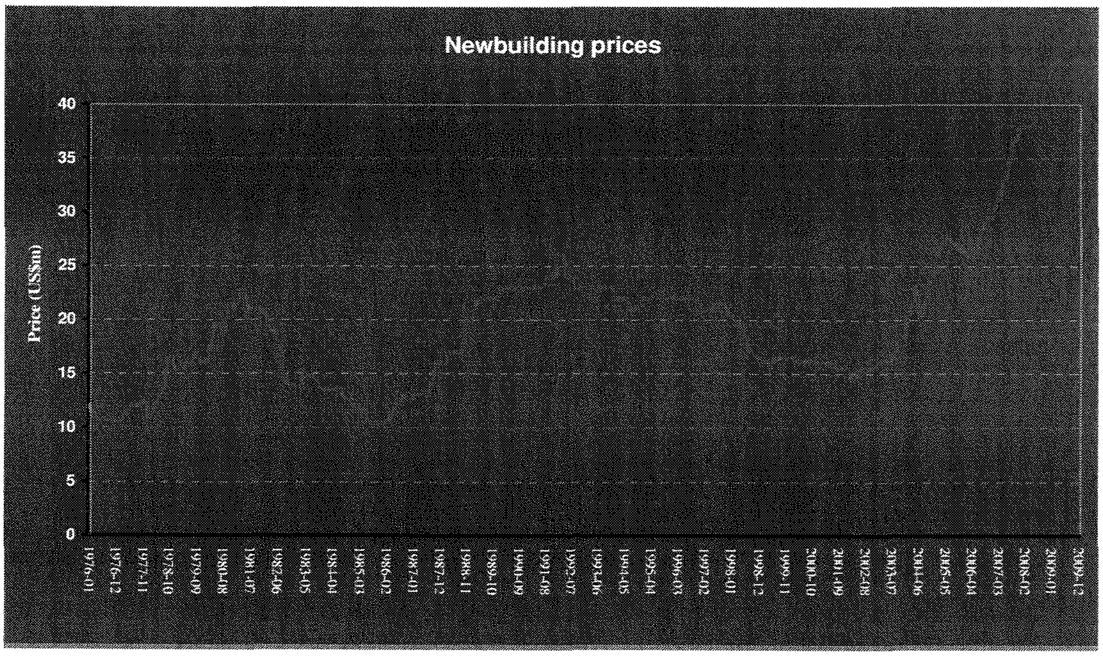
Furthermore it was more attractive to export ethanol to Indonesia and import Australian needs back from Indonesia than to ship around the Australian coast. This was seriously examined as an alternative to coastal shipping. Clearly there have been unintended consequences from the protection afforded Australian flagged vessels when the market is too thin to justify a competitive operator. Where protectionism becomes the issue, other potential participants in the market lose interest in trades and the overall level of service suffers.

Ship replacement & impact of international markets

Prices for new ships rose dramatically during 2006-2007. Prices are a function of the demand for ships and available shipyard capacity and capability. Components of the price rise are also attributable to higher cost of steel and ship equipment, higher wages, currencies and a tight market. Demand for ships during the period was driven by world economic activity and in particular the bulk import needs of China.

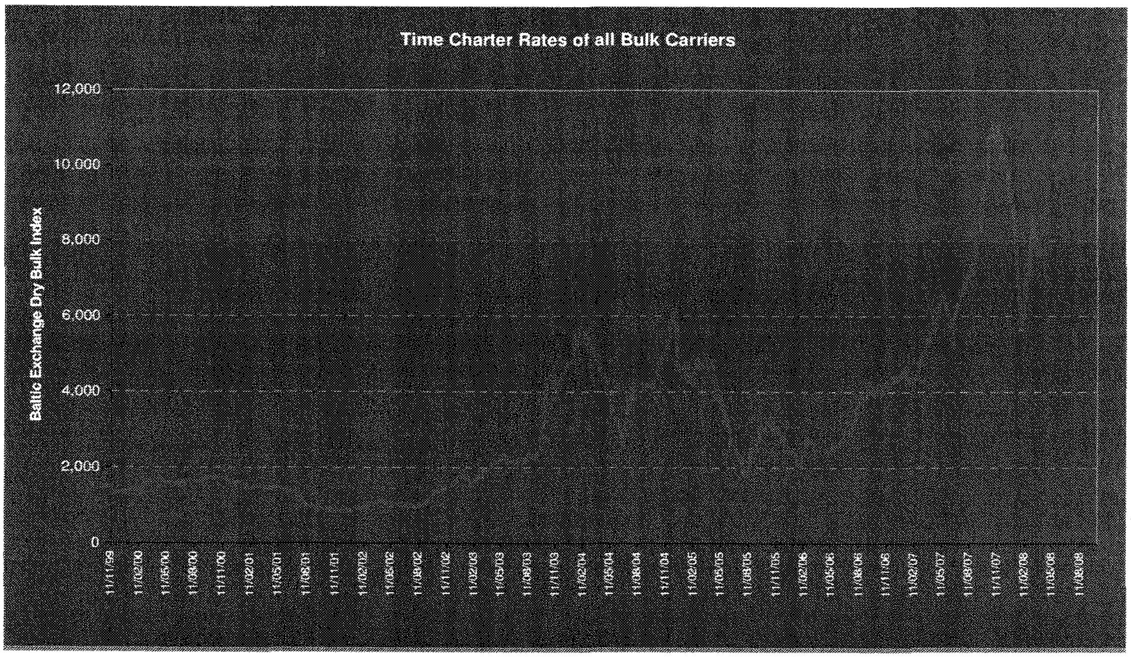
While shipyard capacity is growing, demand is outstripping capacity and, in some places, capability. Shipyard order books are currently at all time highs and it is said that there are few berths available in shipyards able to deliver new ships before 2010-2011. In 2008 the price for new ships remains at all time highs.



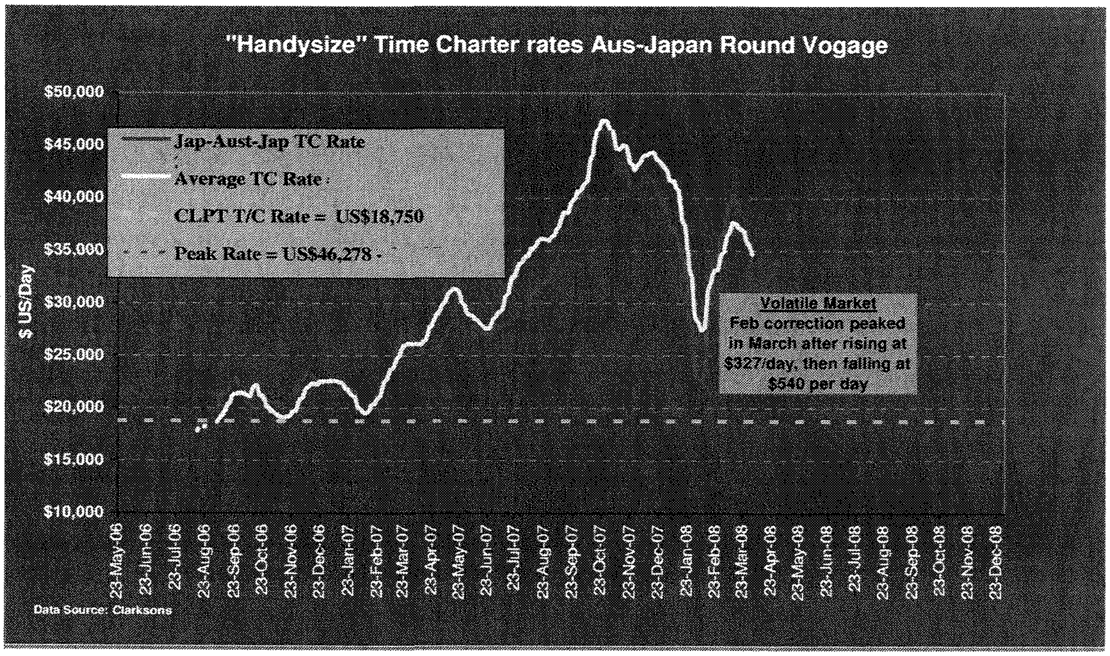


The cost of new builds is also reflected in the market for second hand ships and in the cost of modifying bulk carriers.

As expected, the shortage of vessels and long lead time for new launchings is reflected in the time charter markets. These markets are also showing signs of volatility coincident with the US sub prime market fall out.



Of specific interest to the Australian industry are the charter rates within this region. In particular CSR especially follows the Australia-Japan-Australia routes. These markets have essentially tracked the global average market for bulk carriers. The volatility is best demonstrated by examining the low of 2006 and the highs of 2007 where rates rose by over $US27500 per day – an increase of 150%. The rate of rise and fall in the market has been between three and five hundred dollars per day. Future policy making must recognise the unprecedented volatility in the market for ships.



Charter or build replacement decisions on ships for CSR's domestic bulk commodity needs will be shaped by the state of charter markets for ships, prices for new ships and shipyard availability. There is a high risk that the market will end up being over built with speculation driving the increased orders placed. Consideration of this along with the cost of crew and flag, will be significant determinants of the competitiveness and risks associated with the acquisition of a new ship.

Final decisions will of course always be subject to board approval.

Future Policy Making

CSR's interests are in moving freight in the most cost effective manner to service the needs of our business and our customers.
To achieve this we support arrangements which are:

- Market based
- Competitive
- Cost effective
- Administratively efficient
- Transparent
- Designed to produce predictable outcomes
- Fair to all parties

The Existing System

Permit system

The permit system is bureaucratic, open to misinterpretation, abused by shippers and shipowners, and exploits the time sensitive nature of cargoes.

It provides no clear outcomes in planning the shipping task, gaming the market under the protection of regulation, and with a lack of transparency, under these scenarios, fails the policy principles outlined above. Volatile offtakes and early notification and application rules reduce flexibility and planning capability.

Notwithstanding the shortcomings it does have considerable merit. In fact, where no suitable Australian flag ship is available it works reasonably well in most cases.

Clearly where the shipyard price of Australian flag replacement ships is prohibitively high or, shipyard slots hard to find, access to ships operating under permit remains critical to commodity shippers.

The flexibility to use voyage (spot) or time (period) charters with foreign flagged/foreign crewed ships is crucial to the ongoing delivery of dry bulk commodities to Australian manufacturing industry.

Furthermore unexpected changes in vessel schedules, break downs or other delays, on top of seasonal variation, necessitate the use of foreign vessels – the industry has no alternatives. Running a shipping network with excess capacity to simply retain vessels on the register is damaging to Australian industry and the economy. It's an abuse of the SVP and cabotage system to require Australian flag ships to be available to cope with these marginal fluctuations in demand.
The situation in the new build and time charter market still remains critical and the permit system should be retained and where possible improved.

Competition

Most of the prominent or large maritime jurisdictions offer fiscal incentives to shipowners along with flexible crew employment terms and conditions. Attractive tax incentives are offered by maritime nations across the spectrum from "First World" to "Third World"

The Seafarers Rehabilitation and Compensation Act doesn't apply to the foreign crews of permit ships operating in the Australian coastal trade. Insurance costs to cover crew are high (higher than Australian industry generally). This can add over $100,000 per annum per ship to alternative P and I cover. The challenge is to find ways to provide suitable coverage at a lower cost. This is one example where Australian vessels are less competitive.

Improving the competitiveness of Australian shipping operations is vital to the ongoing desire to maintain an Australian registry. Many of the issues associated with the issuing of permits and the arguments regarding protectionism would disappear largely if Australian shipping was made more competitive by the elimination of some of the differentials.

Thin Markets

The cabotage provisions of the Navigation Act and the guidelines for the issuing of permits are complementary and for the reasons outlined here should remain complementary.

Australian flag vessels are best suited where they are fully integrated and fully utilised in one or two supply chains. Where an Australian domiciled company / potential shipowner has sufficient cargo volume to justify the building of a dedicated ship there are some compelling reasons for him to do so. Not the least is stability in freight rates; a form of hedging. In this case a short term spike in demand can only be met by hiring in another Australian ship (a rare commodity, for reasons explained elsewhere) or a foreign crewed permit ship. Without a permit system manufacturing industry growth would be stifled.

Where demand for ship capacity is thin (eg chemical tanker trade) there are few logical reasons for a cargo shipper or a pure shipowner to build and supply a ship. The trades are semi-regular and are not fully integrated into one company's supply chain, but need to service multiple shippers. Anecdotally there is evidence though that in this case an owner with considerable resources might view the cabotage (and permit) provisions as a mechanism for applying monopoly freight rates to the captive cargo shippers. To overcome this, the permit system should take into account the supply and demand in each segment of the market rather than being applied in a blanket fashion across all sectors and segments.

The current failure to recognise this kind of abuse of the permit system will reduce economic efficiency by imposing service shortfalls on customers, stunting business growth and lead to perverse outcomes such as switching to less efficient forms of transport such as road.

Remedies

A ship operating in the domestic trade under permit is required to travel offshore (to a foreign port) at regular intervals; usually in ballast or empty. This simply adds to the freight cost of Australian industry. If the ship is in Australia for a "period" then the costs of the offshore jaunt are simply added to the total cost of the ship and passed on to the (domestic) charterer.

If it was designed as a deterrent its efficacy as such, in markets where Australian cargo shippers must resort to SVP for the reasons explained earlier, is inefficient and simply adds to costs for Australian manufacturing industry.

Longer CVP periods

CVPs should be issued for periods of up to 12 months. CVPs were originally issued for 6 months, but the time frame was reduced to be consistent with changes to maritime visas for the ships foreign crews. If for example, the crew on a foreign flag ship were all Australians, there would be no visa requirement. The maritime visa regulations were repealed in 2007 and there is no reason to not revert to 12 monthly CVPs and longer period SVPs

This has the additional benefit of reducing greenhouse gas emissions, where fuel is burnt off to merely satisfy a regulatory requirement.

Principle for fast track appeals

Fast track appeals allowing parties to present full evidence regarding unfavourable decisions could be introduced to deal with the stale mates encountered where government, with rather vague or poorly defined ministerial guidelines, becomes the arbiter between the parties. Such an appeal process must be rapid as ships will usually only wait for 2 days obtain a permit.
The appeal should take into account vessel suitability, contamination, prior history, refusals to carry once permit not granted, price, loss of market, customer impact and previous behaviour.

Stimulating the Australian Industry

Previously government has assisted the industry in the form of accelerated depreciation for a fixed time frame. The evidence confirms that growth in the industry occurred at time of tax concessions or capital grants. CSR's last three ships were built with accelerated depreciation. The company would take such a policy into account in its considerations for a build or time charter decision. Depreciation of 20% is very attractive and is reflected in lower finance charges and reduced lease costs. In some instances the first 20% is allowed in the year before delivery, which assists with down payment to the shipyard. However one off injections do not amount to sustainable policy and other solutions may improve the attractiveness of the local industry in the long run.

Skill Shortages

Skill shortages are apparent within the Australian and international fleets. While Section 457 visas can be used for ships officers, they are not available for Integrated Ratings. While the application of Section 457 visas is being studied elsewhere by Government, there are a number of barriers to the use of these visas. Processing times can be slow at the Australian office of application, unfavourable tax regimes are a disincentive and recognition of qualifications is not necessarily straightforward.

CSR examined the use of s457 visas in relation to its recent charter, but found the provisions quite unworkable. Providing for mixed crews may alleviate the shortages to some extent, but will not totally solve the problem. There is now an internationally competitive skills market and Australia needs to remove the impediments to the recruitment of seafarers. A training commitment from shipowners could be a condition for granting concessions, fiscal or otherwise, however some means of addressing the brain drain to the offshore oil industry should be developed.

Tax treatment of seafarers and skills recognition are two areas which warrant further examination. Tax concessions might be granted to individuals based on time at sea to induce people to join the industry.

The complete topic of training needs to be addressed to ensure that our Australian training programs are not compromised, but they must become more productive. The models that were designed for low turnover are not suited to today's skills market. With 40 vessels on the Australian register the cadet program is a choke on the number of qualified people that can be produced. Training should be skill and competency based, without time based requirements. Perhaps there is an opportunity to be qualified by task, providing some on board flexibility with crewing.

CSR supports the concept of riding gangs on the coast to reduce maintenance costs and vessel downtime during re-fits.

Improve Competitiveness

Where Australian legislation imposes costs on Australian flag ships and not foreign ships the differential should be remedied by placing Australian ships on a similar competitive footing. Ideally this would involve reducing the costs imposed on Australian vessels, such as the high cost of insurance cover for crew rehabilitation and compensation costs.

Safety performance in the Australian industry remains poor. The cost of poor performance is a tangible hurdle for local owners seeking to be competitive. A concerted effort should be carried out across the industry to remove this and raise the standard of safety. Poor safety performance adds cost to the business.

We support the introduction of a form of tonnage tax as an option. This has been successful in other jurisdictions in stimulating the industry.

The creation a second register might stimulate some growth and create some employment. If one can make arguments for a second register that is more cost effective then why wouldn't all owners register on the second register? Lessons could be learned from jurisdictions which have second registries as to how our own register might be operated at lower cost. We believe the concept appears to have little merit in the domestic shipping trade but may trigger growth in international trades.

There have been suggestions and it is ALP policy to introduce an Australian Coast Guard. We have no view about the relevance of a Coast Guard for Australia other than to the extent that the cost of AMSA might be lowered if some its roles were performed by or shared with the coast guard. It is likely that the Coast Guard will assume roles currently undertaken by the Navy and as such should be funded in the interests of the whole community, not by the shipping industry. AMSA is an effective organisation and we would not want to see the introduction of another agency add to the cost of Australian shipping.

Conclusions

CSR sees advantages in an efficient and competitive Australian Flag regime operating in combination with a permit system on the Australian Coastal Trade. Overall a vibrant coastal trade is critical to the performance of our Australian businesses. An effective and efficient supply chain is critical to retaining competitive manufacturing in Australia. As the country heads for the imposition of a carbon price through emissions trading and with high exchange rates, imports from Asia, where there will be no such carbon price, will become increasingly competitive. These factors, combined with the international market for charters and new builds will be influential in how we equip for the future freight task.

Peter Bremner

General Manager, Shipping

Martin Jones

General Manager, Government Relations

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CSR