Submission 016
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AUSTRALIAN DRY BULK SHIPPING USERS*

SUBMISSION

13 April 2012

Submission to:

PARLIAMENT OF AUSTRALIA HOUSE OF REPRESENTATIVES

STANDING COMMITTEE ON INFRASTRUCTURE AND COMMUNICATIONS

INQUIRY INTO THE SHIPPING REFORM BILLS

Key Points

Coastal trade can only exist if there is demand from customers. Dry bulk shipping users are the customers for 60% of the coastal trade.

The Government's proposed *Coastal Trading Bill 2012* should NOT be passed through the Federal Parliament until it has been properly scrutinised as to whether it is an economic and productivity reform as it:

- Promotes protectionism of Australian shipping without concern for the impact it will have on Australian manufacturing and industry;
- Will significantly impact on Australian manufacturing and industry costs;
- Will encourage foreign product imports over Australian industry;
- Is being incorrectly promoted as an environment and security reform; and
- Provides too much discretion to the Minister which can lead to further instability and uncertainty than the current arrangements of single voyage and continuing voyage permits.

Background

The Minister for Infrastructure and Transport introduced five Bills into the Parliament on 22 March 2012. This submission addresses the *Coastal Trading (Revitalising Australian Shipping) Bill 2012 and the Coastal Trading (Revitalising Australian Shipping) (Consequential Amendments and Transitional Arrangements) Bill 2012*.

Dry Bulk Shipping Users are Australian manufacturers and industry that are highly dependent on domestic sea freight to move either their inputs for value-added processing or their final products that are moved to market for sale. They include Australian industries such as sugar, fertiliser, cement, gypsum, retort coke, soda ash, bauxite and iron ore.

The proposed *Coastal Shipping Bill 2012* represents a very heavy handed approach given that 70 per cent of the Australian coastal shipping task is already undertaken by domestic vessels.

It is difficult to justify the regulatory environment that will result from the proposed *Coastal Shipping Bill 2012* when domestic coastal shipping is currently covered by approximately 17 Australian vessels[i] and a small number of foreign vessel equivalents.

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Approximately 60 per cent of the coastal shipping task is comprised of dry bulk goods (with liquid bulk goods comprising 26 per cent, containers 9 per cent and non-bulk 5 per cent.

As a group of Australian manufacturers and industry, dry bulk shipping users are concerned that the proposed *Coastal Trading Bill 2012* will have a significant negative economic impact as freight costs make up 30 per cent of their total costs.

As a result, **Australian Dry Bulk Shipping Users** commissioned Deloitte Access Economics (DAE) to analyse the specific economic impacts of the reforms on the Australian industry and manufacturing, and the economy more broadly.

The Government's own Regulatory Impact Statement (RIS August 2011)[ii] and the Deloitte Access Economics study (February 2012)[iii] demonstrate a loss of net economic activity that increases as the number of domestic vessels replace foreign vessels to freight around Australia's coastline.

Government Regulatory Impact Statement

The Government's RIS demonstrates that even with a 10 percent increase in the change to current coastal shipping arrangements, there is a significant economic cost to the Australian economy, with the greatest burden falling on 'other dry bulk users'.

The Government RIS analysed four scenarios that may eventuate from the reforms (pp vi-vii):

- Scenario A – no replacement of foreign temporary licence ships with Australian ships. The same quantities of freight carried by permit ships in the base case are carried by temporary licence ships in the policy case. No AISR ships are assumed to come into existence.
- Scenario B – for 'other dry bulk', petroleum products and 'other liquid bulk' sectors, Australian ships gain an additional 10 per cent of total freight tonnage from foreign temporary licence ships after five years. AISR ships are used in the triangular trades carrying coastal freight and coal to Asia, carrying a one-third share of coastal freight carried on triangular voyages with foreign ships accounting for the other two-thirds.
- Scenario C - as for scenario B but Australian ships gain 20 per cent of the total freight tonnage in the 'other dry bulk', petroleum products and 'other liquid bulk' sectors. AISR ships achieve two-thirds shares of the bauxite and iron ore triangular trades.
- Scenario D - use of foreign ships in the 'other dry bulk', petroleum products and 'other liquid bulk' sectors is phased out altogether over the first five years. The quantities of freight carried by foreign temporary licence ships fall linearly to zero over in 2016/17 and remain at zero thereafter. AISR ships gain all the bauxite and iron ore triangular trades.

Scenario A is a reflection of the status quo, so the reduced net present value in scenarios B, C and D represent an indisputable economic loss from the status quo (whether the number is positive or negative).

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The following table published in the Australian Government's Regulation Impact Statement published August 2011 provides details:

Market segment		Forecast growth rate	A	B	C	D
		(% pa)	Net present value ($m)			
Dry Bulk	Bauxite (AISR ships on triangular voyages)	3.5	0	-16	-33	-49
	Iron ore (AISR ships on triangular voyages)	0.0	0	-10	-16	-25
	Other iron ore	0.0	15	15	15	15
	Other dry bulk	2.0	130	96	61	-80
Liquid Bulk	Petroleum products	1.0	30	18	5	-63
	Other liquid bulk	1.5	16	13	9	-1
Total NPV			**192**	**116**	**42**	**-202**

Source: Department of Infrastructure and Transport (2011), Regulation Impact Statement: A Framework to Revitalise Australia's Shipping, August, page vii.

The reason that many of the scenarios in the table show a positive NPV is because the Minister's announcement of 13 August 2010 indicated that the reforms would be conditional on industry and unions entering into a compact to deliver productivity and efficiency reforms to better align practices in the Australian shipping industry with international practice. This has not yet occurred even though this productivity improvement has been factored into the Government's RIS analysis upfront.

Deloitte Access Economics Study

A number of dry bulk shipping users gathered together following the public release of the first draft of the *Coastal Trading Bill 2012* in December 2011 as they were sufficiently concerned that the Bill could have major implications for their competitiveness and that the Government was continuously dismissing their concerns.

The group commissioned Deloitte Access Economics to undertake a general computable equilibrium model analysis of the economic impacts of the reforms using actual data provided by the companies.

The report which examined the impact of the replacement of foreign vessels with domestic vessels on the coast, was made publically available in March 2012.

Headline findings include:

- That changed licensing arrangements proposed will lead to an increase in the cost of coastal shipping and, by extension, freight rates of up to 16% if domestic vessels replace foreign vessels.

- A variety of factors, such as the competitiveness of downstream industries and the scope for import competition, suggest that these cost increases are likely to be borne predominantly by the users of coastal sea freight. Not only will this diminish competitiveness, it will also impact negatively and potentially significantly on future investment decisions.
- The precise magnitude of the long term economic impacts is difficult to determine given the myriad of factors at play. However, the modelling undertaken here suggests that, in net present value terms, the aggregate impact on gross domestic product over the period to 2025 will be between -$242 million and -$466 million.
- The associated loss of employment over the long term is, in net terms, 200 full time equivalent employees as it is assumed the labour market will remain buoyant and most of the displaced labour will be absorbed in other sectors. In the immediate term, the displacement is considerably higher, with an estimated peak loss of 570 FTE employees. These job losses will mainly be in regional Australia.

Following the public release of the DAE report, the Australian Government has incorrectly claimed that the report compares international wages with domestic wages. The Minister has used this incorrect claim as a basis for the Government to dismiss consideration of the DAE report findings.

The Australian wages of the Seagoing Industry Award have been payable to employees operating a coastal voyage under permit since 2011 under the Fair Work Act. As per the Government's Regulation Impact Statement, Australian wages are also used in the modelling of the DAE report.

However, The Government must acknowledge that Australian flagged vessels do face higher crewing costs than international vessels operating on the coast as a result of the 'conditions' outlined in the Seagoing Industry Award that do not apply to foreign vessels.

These conditions include some very generous elements including:

- Approximately one day off for every day worked (including travel from home to port); and
- An additional five weeks annual leave.

These conditions represent expenses that are faced by Australian Flagged vessels only.

The Deloitte Access Economics report makes the assumptions used very clear. They are very similar to the Scenario D assumptions outlined in the Government's Regulation Impact Statement.

Given the lack of information available at the time (which still exists), the productivity dividend from the promised 'productivity compact' has not been included in the DAE study. Also, the DAE study has not assumed any benefit pass through of the tax incentive measures, as the pass through from shipping companies to consumers is assumed to be minor as a result of the reduced flexibility and competition among coastal shipping companies.

Productivity Gains of the *Coastal Trading Bill 2012*

A thorough economic impact and productivity analysis of the impact of *the Coastal Trading Bill 2012* has not occurred despite the long consultation period outlined by the Government which began with a House of Representatives Inquiry in 2007. The House of Representatives Committee noted that the potential cost increases from tighter cabotage should be examined due to potential relocation of Australian production offshore. No assessment of the impact of these reforms on users has occurred.

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The cement industry notes that it currently costs the same to move product from China to Australia as it does to move one Australian port to another.

There has been no analysis of the *Coastal Trading Bill 2012* by either the Treasury or the Productivity Commission and the original timeline outlined by the Government for the development of the Bill has been truncated by 12 months while the outcome or progress of promised 'productivity compact' between Unions and the shipping industry is yet to occur. It would be preferable to understand what productivity gains are to be made through a compact between Unions and the shipping industry prior to the Parliament being asked to vote on the *Coastal Trading Bill 2012.*

It should also be noted that dry bulk shipping users have not been invited to be a party to these discussions.

No need to rush the reforms with lack of analysis

As there has been no analysis of possible consequences from a reduction in competition and flexibility of shipping on coastal routes, the **Australian Dry Bulk Shipping Users** propose the *Coastal Trading Bill 2012* not be legislated.

The current system is not broken, a case for change has not been made, and there is absolutely no reason to rush the bills through.

The impact on the customers of the shipping services has not been well considered, particularly for Australian manufacturing and industry of dry bulk products that are highly reliant upon coastal shipping to remain internationally competitive.

Australian dry bulk shipping users have been consistently raising concern with the draft Bill since it was first made available in December 2011. Earlier consultations have not provided sufficient detail upon which to form a view and the RIS was only made available to the public in August 2011. The Government certainly did not undertake draw the RIS to the specific attention of those most impacted.

There remain significant unanswered questions about the decision framework the Minister, or his delegate, will use to determine whether a temporary licence application will be accepted or rejected.

There is also no justification provided for the sweeping discretionary powers afforded to the Minister in administering the Act that would result should the *Coastal Trading Bill 2012* be passed.

Objects of the Bill

The objects of the Bill fail to include an object to ensure coastal shipping services in Australia become more internationally competitive. Such an object is necessary to ensure the customers of shipping services can remain internationally competitive.

The absence of such an objective ignores the possibility that an Australian shipping industry out of step with international freight rates could suffer a decline due to the disappearance of its customer base.

If the Bill does not ensure Australian shipping becomes more internationally competitive, imports of commodities, likely delivered on foreign vessels, may replace those Australian commodities which are highly reliant on efficient coastal shipping.

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Missing detail in the Bills

Since the release of the Deloitte Access Economics study, which came after a number of submissions by Australian dry bulk shipping users made to the Government raising concerns, the Government has sought to assert that the legislation will build the Australian fleet through incentives and not through protection.

If this were the case, there would be little need for a significantly increased regulatory burden for obtaining a temporary right (Licence) to move cargo on a coastal route.

There is no satisfactory guidance provided to potential temporary licence applicants as to the basis the Minister or his delegate will decide on accepting or rejecting a temporary licence application. Rather, there is listed a very wide range of matters that may be taken into account (at the discretion of the Minister).

One such provision that seems inconsistent with a 'non-protectionist' approach would be that the 'Minister may take into consideration whether a temporary licence has been applied for in the past.' This should be an irrelevant factor in the Minister's decision. The only relevant factor should be whether or not a general licence vessel is able to carry the cargoes to the shipper's specifications.

Further, if temporary licence applications and the voyage information of temporary licence holders are to be made publically available to allow for greater transparency, then all of the proposed coastal shipping movements (including domestic vessels) should be made available to ensure Australian shipping users are able to ascertain the availability and freight costs to move their cargo.

Environmental reform

The Australian Government continues to assert that the shipping reform bills are required for the future protection of the environment.

Frequently, the Minister has sighted shipping accidents that have occurred around the globe, including that of a coal ship that grounded on the Great Barrier Reef. The accidents sighted are not foreign vessels operating coastal voyages; they are international vessels carrying international cargo, a practice that will remain relatively unchanged as a result of these Bills.

The truth of the matter is that of the 27,000 voyages that occur within Australia each year, only a few hundred are coastal voyages and only one third of these are foreign vessels operation on the coast.

Despite the Government's constant reference to the need for a reserve pool of 'Australian' labour from which to draw Australian regulators, there has been no case made that the small number of Australian flagged vessels the Government hopes to see on the coast will provide any reduction in the need to access the international market for qualified mariners to fill vacancies in a multitude of shore based positions.

There seems to have been a lack of consideration of alternative methods of training and retaining marine pilots and other marine specialists who have been traditionally employed as a consequence of their maritime qualifications and experience.

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Possible bulk shipping monopoly

Due to the relatively small size of the dry bulk coastal trade, particularly when specialised ships are required, it is difficult for a large number of ship owners to exist viably in a commercial sense, thus the market has naturally developed with a dominant provider. Typically vessels are being provided on long term (more than 10 year) affreightment contracts.

The draft legislation will encourage the current provider to register their vessels as general licenced vessels, providing them with automatic and legislated priority on the cargoes that they currently carry on the coast. This change will be placed before the expiry of the term of the current shipping commercial arrangements with the dry bulk shipping users and therefore, by default, give the current provider a monopoly on all cargoes.

The proposed *Coastal Trading Bill 2012* will ensure that a third party will have difficulty in entering the Australian market as the current provider's general licensed ships may automatically be allocated the dry bulk cargoes irrespective of the commercial cost difference.

This potential would not simply mean increased costs as a result of using Australian flagged vessels, but also potentially higher costs as a result of a lack of competition. Such outcomes have not been included in the modelling analysis of either the RIS or the DAE study.

Conclusion

Australian Bulk Shipping Users create the demand for coastal shipping when they move inputs or their final product to market within Australia. However, their concerns continued to be disregarded, even though the Government realises an economic cost will most likely be transferred to them if the *Coastal Trading Bill 2012* is passed in its current form. This means Australian manufacturing, industry, farmers and regional Australia will be traded off to enable to a handful of domestic vessels to be placed on Australia's coastline. Australian vessels already carry 70 per cent of Australia's product around Australia's coastline.

It is recommended

1. ***That the Infrastructure and Communications Standing Committee request the Coastal Trading Bill be referred by the Australian Treasurer to the Productivity Commission to ensure the productivity and economic consequences of the Coastal Trading Bill 2012 are properly scrutinised;***
2. ***That the Coastal Trading Bill 2012 be deferred until a full economic and productivity assessment can be made, and***
3. ***That the existing systems for the provision of single and continuing voyage permits continue to operate in the interim.***

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Endnotes

[i] Albanese, A. (2012), Coastal Trading (Revitalising Australian Shipping) Bill 2012 Second Reading Speech, March.

[ii] Department of Infrastructure and Transport (2011), Regulation Impact Statement: Reforming Australia's Shipping, Commonwealth Government, Canberra, August.

[iii] Deloitte Access Economics (2012), Economic Impacts of the Proposed Shipping Reform Package, February.

*** Australian Dry Bulk Shipping Users**

The Australian Dry Bulk Shipping Users are an informal group that represent Australian industries that are highly dependent on coastal shipping to move dry bulk products around the Australian coast.

Products that may be impacted include cement, gypsum, sugar, fertiliser, soda ash, retort coke, iron ore and bauxite.

The companies and industry associations involved include the Cement Industry Federation, CSR, Penrice, Pacific Carbon, the Fertiliser Industry Federation of Australia and the Minerals Council of Australia.

The Business Council of Australia and the National Bulk Commodities Group have also provided in kind support to the DAE project.