Australian Paper

PRODUCTIVITY COMMISSION INQUIRY INTO TASMANIAN FREIGHT ASSISTANCE ARRANGEMENTS

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EXECUTIVE SUMMARY

Economic Impacts

70% of Australian Paper's Tasmanian production is unique in the Australian context in that it can't be produce anywhere else in Australasia due to that fact that it is machine coated (and no other coater exists or is likely to be constructed). The remaining 30% could be produced our Maryvale plant (however it may displace more profitable grades) thus is would most probably be imported.

With considerable spare production capacity in the global context, any production shortfall will be made up through increased imports from Indonesia and China.

In this regard TFES assistance is vital to sustaining Australian Paper's Tasmanian mill operations, especially in the current price and demand depressed market. The loss of the company's Tasmanian mill operations would have a conservatively estimated $1.3billion negative impact on Australia's balance of trade over the next ten years. This would be primarily through the loss of import substitution production (87.5%) but also the loss of exports (12.5%).

Australian Paper's Tasmanian mills, either through direct employment and/or sole customer suppliers, provide employment for 780 people on a full-time basis. The broader employment consequences are conservatively estimated at 2,400 full time jobs.

The Australian Government's return is 6.5 times the assistance provided to address the sea freight cost disadvantage incurred in shipping across Bass Strait.

Supply Chain Impacts

In Australian Paper's case TFES addresses the sea freight cost disadvantage for the annual southbound movement of 1,150 TEUs of clay[1] and the northbound movement of an estimated 11,610 TEUs of finished paper. These movements are undertaken using customised containers and highly efficient Ro/Ro shipping operations. The supply chain is continually being examined for any scope for additional efficiency and productivity improvements.

Under the current approach to the calculation and payment of TFES assistance Australian Paper has not identified any instances where the freight task would be undertaken differently in the event that it had additional resources equivalent to TFES assistance. That is, there is no evidence of distortion in market behaviour.

However, marginal reductions in the level of TFES assistance would have significant impacts on supply chain efficiencies and costs through the potential loss of economies of scale and the varying impacts this would have at different points of the supply chain. E.g. there is a point at which the capital cost of maintaining a heavy lift capability for unloading containers will not offset the higher freight costs that might be incurred in using side-loading container trucks and or non-containerised vehicles.

[1] Clay is used as white pigment and coating material in the manufacture of paper.

Assistance Parameters

It concerns Australian Paper that notwithstanding the recommendations of the TFES Review Authority and the Ministers Directions for TFES during a period of rapid productivity improvements for road vehicles (better than 15% since the current method of calculation was instituted) there is no evidence that the key assistance parameters have been reviewed since the revised scheme was implemented in 1999

Australian Paper has investigated some of the key parameters pertinent to its operations and these investigations point to the current Road Freight Equivalent rate of 66.9c/TEU equivalent/km being substantially higher than the company's experienced rate.

There are also indications that the current calculated estimate for Fixed Intermodal Costs understates the true burden of intermodalism for Bass Strait Shippers. The Fixed Cost allowance should be increased to $139.40.

While Australian Paper recognises the need for incentives to reduce transport costs, this must be based on equitable consideration of enterprises' capacity to negotiate lower rates. To some extent this notion has been captured in the calculation model's declining rates of compensation according to the relationship between actual and median disadvantage.

However, of acute concern to Australian Paper is that the recent Australian Government approved rationalisation of shipping service providers on Bass Strait will diminish the company's negotiating power with respect to maintaining low sea freight rates.

Accordingly it is recommended that the proportion of notional wharf-to-wharf entitlement paid to claimants with a wharf-to-wharf disadvantage lying between 0.5 and 1.0 times the median wharf-to-wharf disadvantage be set at 85%.

TFES Rationale and Issues

The Tasmanian Freight Equalisation Scheme was instituted as a tool of economic development in response to the underlying trade barrier that Bass Strait presents. The rationale for its existence is the requirement that all Australian States be treated equitably with respect to accessing the benefits of interstate trade. To do so, States require comparable and cost equivalent access to transport infrastructure. This rationale remains as pertinent today as ever.

However, it is observed that the policies of successive Federal Governments have continued to entrench practices that impose a disproportionate cost on the transport of goods across Bass Strait when compared with similar movements on the mainland. These include:

- Investing in improving land transport infrastructure, coupled with the development of national standards etc. for vehicle operations;
- Facilitating and supporting significant restructuring of stevedoring activities through measures such as the funding

mechanisms provided through the Stevedoring Levy and associated support;

- Perpetuating high operating cost structures in Australian coastal shipping; and
- Endorsing the rationalisation of Bass Strait operators with consequent loss of competition in key market segments.

While some initiatives, such as the first two, are applauded it is apparent that with respect to transport across Bass Strait these investments are having perverse impacts. These investments are improving the distribution efficiencies of importers in the Australian market and progressively eroding the competitive advantage of Australian production facilities located in Tasmania. The latter approaches are inhibiting and/or reducing the scope for competition and the accompanying cost savings that might accrue to Bass Strait shippers.

In this economic and policy environment TFES has proved to be a focussed and highly targeted program that addresses a specific objective, “the reduction of the sea freight cost disadvantage”, in a highly effective manner. That there is scope for improvement is apparent. Parameters need to be adjusted regularly, certainty needs to be improved etc. but the underlying model is regarded as being particularly robust. Any departure from the current model on the basis of simplification e.g. through flat rates of assistance, would only increase the discrepancies between shippers in terms of assistance received and lead to market distortions.

Australian Paper does recognise that allegations of scheme abuse are damaging to the integrity of TFES and measures to ensure compliance with the moral intent of the scheme will, subject to an impact assessment, be strongly supported.

In examining the eligibility of inputs to production and subsequent outputs to receive TFES assistance, Australian Paper regards that the underlying principle should be what the notional disadvantage is that the shipper is incurring in moving product. As such the movement of mini-bulk movements should be assisted according to how the product might best be moved over a comparative distance between mainland states. On this basis the competitive relativities between the modes would be re-established.

Without the Australian Government’s continuing commitment to addressing the interstate “sea freight cost disadvantage” the company experiences in trading across Bass Strait, Australian Paper would be considering how, where and when it should scale back its operations.