By Email: tasmanian.shipping@pc.gov.au

Mr Daryl Quinlivan
Head of Office
Productivity Commission
GPO Box 1428
Canberra City ACT 2601

3 February, 2014

Dear Mr Quinlivan,

The comments below relate primarily to the Productivity Commission's draft findings and recommendations concerning the Tasmanian Freight Equalisation Scheme, TFES.

Regrettably, there is a sense of déjà vu in reading the Productivity Commission's Draft Report into Tasmania's Shipping Costs and Competitiveness of Tasmania's Freight Industry. Moreover, there is a sense of frustration and despair that the Commission appears intent on ignoring the overwhelming body of factual evidence presented by Tasmanian industry concerning the ongoing freight cost disadvantage of shipping across Bass Strait.

Throughout the draft report, the Tasmanian Freight Equalisation Scheme is referred to as a 'subsidy'. The deliberate and repeated use of this terminology is offensive as it seeks to undermine the legitimacy of the scheme. Much mischief is also made of the historic accumulated and current cost of TFES, yet the amounts quoted represent only a fraction of the construction, maintenance and debt servicing costs associated with the road infrastructure servicing other remote parts of Australia. Indeed, the case could be put that Tasmania has been significantly 'under-equalised' rather than overcompensated.

In many areas, the Draft Report reads as if the Productivity Commission believes it is working with a blank canvass (with a view to create a better future for the Tasmanian economy) rather than dealing with immediate real world issues and challenges, real jobs and people's livelihoods. Likewise, many comments and recommendations in the Draft Report appear to ignore or challenge existing Government Policy and the bipartisan support which TFES has received since its inception.

There is no acknowledgement of the critical issue of Sovereign Risk or recognition that Tasmania's traditional industries and participants in the Scheme remain the backbone of the State's economy. This approach leads to naïve conclusions and recommendations which would produce serious consequences if implemented.

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We will leave it to others to determine whether the Commission has gone outside its terms of reference by suggesting a whole range of socio-economic policy reforms for Tasmania. We simply make the observation that while some of the suggestions may have merit, they would take 10 years or more to implement which does nothing to assist Tasmanian businesses right now in trying to overcome the very real freight cost disadvantage associated with Bass Strait.

From our perspective, the greatest deficiency in the Draft Report is that the Commission invited public submissions concerning the freight cost disadvantage associated with shipping across Bass Strait and then completely ignored the evidence presented and based its conclusions and recommendations on untested desktop work by another Government agency.

In terms of the suggested adjustments to payment rates to reflect current BITRE estimates, the Commission notes that considerable savings to the Commonwealth Budget would result. This must mean a lowering of the scheme's support levels, or a shrinking of the scheme's footprint, or both. How then will this do anything to assist those businesses in Tasmania who are struggling with domestic freight cost disadvantage associated with the Bass Strait crossing? We also note the Commission correctly recognises that "appropriate transitional arrangements will be necessary". However, we respectfully suggest that the mentioned arrangements being over 2-3 years would be way too short and represents another significant 'Sovereign Risk' issue. The timeframe and nature of strategic investments and commercial commitments already made, based on the current scheme's support levels, would require a transition over more like a decade than the short period suggested by the Productivity Commission in their Draft Report.

Norske Skog Boyer Mill can categorically state from our experience as one of the major Tasmanian manufacturers and shippers across Bass Strait, that there is a significant freight cost disadvantage compared to road freight and the current assistance provided does not fully compensate for that disadvantage. As shown in our confidential submission, there is still a significant cost disadvantage which in Norske Skog's case is 27% (net of TFES). In the case of smaller shippers, this disadvantage is most likely even greater.

It is our experience that TFES has never fully compensated the Boyer Mill for the freight cost disadvantage and in fact the gap is increasing. We absolutely reject any assertion that we are currently being over compensated under the current TFES parameters.

In the short time since their release, we have reviewed the BITRE reports which are the basis of the Productivity Commission's conclusion that the freight disadvantage has significantly reduced over time and thus TFES payments currently overcompensate for any cost disadvantage. It is BITRE's contention that since the last parameter review in 1998, that the increase in the cost of equivalent road transport has outstripped the increase in Bass Strait shipping costs thus resulting is a significantly lowering of any freight disadvantage.

Our review has identified a number of inconsistencies and significant concerns in relation to the methodology, assumptions and data used by BITRE. These concerns relate to both the major components in the calculation of the sea freight cost disadvantage, the Bass Strait Shipping Cost, Road Freight Equivalent Cost (RFE) and Intermodal costs.

Bass Strait Shipping Cost

This is determined by BITRE by calculating the median rates, using the TFES claims data for all Wharf to Wharf full container load shippers on the Victoria – Tasmanian routes. Although we do not have the full sequence of yearly data the last five years are shown below.

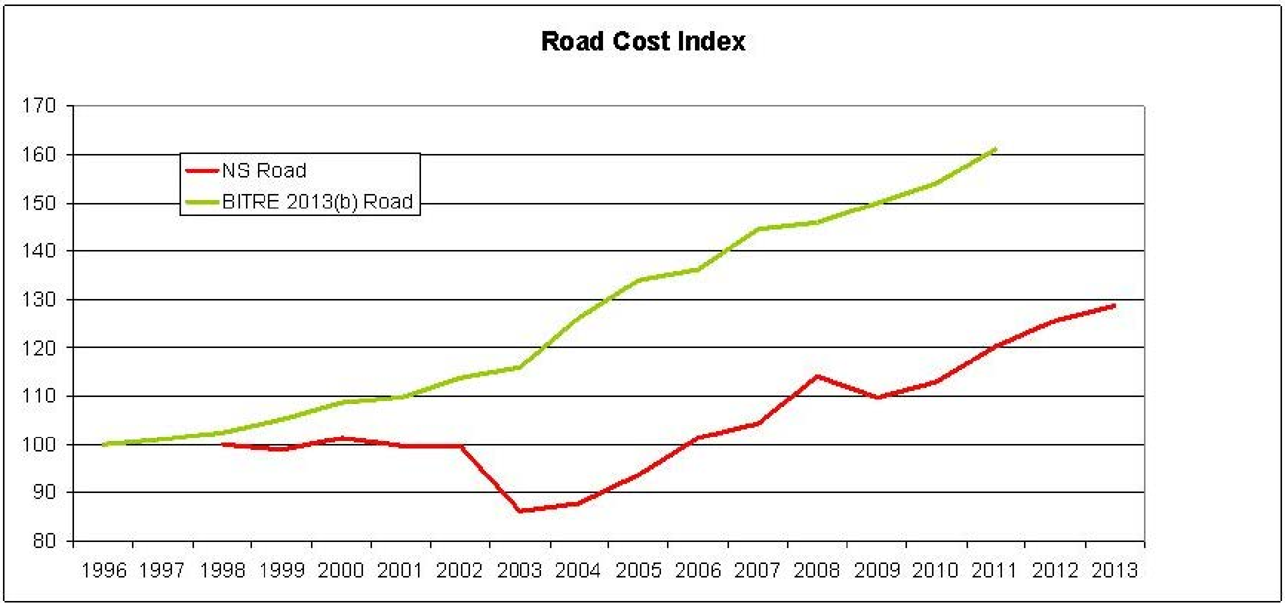
Year	"Median Cost /TEU"
2007/08	$1,166
2008/09	$1,121
2009/10	$1,127
2010/11	$1,047
2011/12	$1,098

The data infers that shipping costs have come down by 5% over this period of time, which has definitely not been the case. Over this period of time, Norske Skog have experienced a 10% increase which is in line with BITRE's own shipping data which shows a 9% increase and we are sure that all shippers have had at least similar increases . We are obviously not privy to the underlying data but it is clear that the calculation of the "median rates" does **not** reflect the real movement in shipping costs paid by Tasmanian shippers and in this case significantly understates the actual shipping rates by 15%..

It is also worth noting that the full impact of the significant lift in the charges by the Port of Melbourne will become evident in higher median costs in the 2012/13 year. These are real costs, are significant in nature and need to be included in the calculation for future comparison purposes.

Road Freight Equivalent Costs

This is the area where Norske Skog's real world experience diverges significantly from BITRE's analysis of costs. Below is a graph showing the change in road transport costs that Norske Skog has actually experienced at our Albury Mill for newsprint deliveries between Albury and Melbourne. The distance is 350 kms and industry standard B – Double trucks with tautliner trailers are utilised. These are compared against the BITRE 2013a Road Cost Index as shown in Figure 2.6 in the Productivity Commission's Draft Report.



There is a significant difference in the rate of increase over this period. The actual Norske Skog Albury costs increase has been 40% less than that outlined in the BITRE report. It is our view that the BITRE data significantly overestimates the actual commercial increases that have occurred and that have been experienced by our Albury facility.

On closer examination of the BITRE calculations on the RFE, we obverse the following which we believe significantly inflates the RFE cost.

1) BITRE have increased the trucking rates provided by their consultant (SKM) by a factor of 30% because they feel it would be an applicable allowance for empty running rate. Given that the information from SKM "generally reflects actual rates negotiated and paid" then wouldn't the typical industry empty allowance already be factored in the SKM rates? If there were a connecting road corridor between Tasmania and Victoria then it is hard to see why empty returning rates would be any different than experienced currently on the mainland.

2) BITRE has indicated that the appropriate RFE rate for 2011-12 is 13.46 c/t/km, which then equates to a dry freight cost (DFC) of $650 per TEU. Yet the SKM report indicates that a typical rate for a similar distance on the mainland is 11.78 c/t/km. As indicated above, if there is a connecting road corridor then we do not see any reason why mainland rates would not apply. If this change is made, then the DFC would reduce to $569. If correct, this represents a 14% overstatement by BITRE of the RFE.

3) BITRE assume in their calculations that there is net payload of 11.5 tonnes per TEU. This is based on an assumption that the tare weight of an average TEU is 1.5 tonnes. It is not clear how this average TEU tare weight has been determined. Actual TEU's weigh between 2.2 and 2.4 tonnes (and Norske Skog's "purpose built" TEU's are 3.2 tonnes) and FEU's between 3.6 and 4.0 tonnes. So, it is likely that the average TEU equivalent weight is at least 2 tonnes and possibly more. Based on an assumption of 2.0 tonnes, this would drop the DFC further to $544 /TEU. (Note if one assumed 2.2 tonnes which is a typical tare for TEU container, the DFC would be $534). Again, this significantly leads to a further overestimate of the DFC by 4.5% (or 6.5% if 2.2 tonnes tare weight is used).

4) Actual Road Rates:

   BITRE rely on advice from SKM on the actual road rates. As noted above, they have indicated that a typical B-Double rate carrying 39 tonnes is 11.78 c/t/k. This equates to a rate of $4.59 per km. It is Norske Skog's (and others) experience that this is considerably higher than we are currently able to achieve in a real world commercial environment.

   a) In 2013, Norske Skog transported newsprint on B- Doubles from the Boyer Mill to Burnie (320 kms) for a short time for a rate of $2.15 /km. Although we acknowledge that these were "spot" pricing rates and probably a permanent operation would have higher costs, we firmly believe that rates of $2.50 /km would be achievable. This is particularly true if one assumed that there was a road connecting Tasmania to Victoria and the distance increased to 755 kms. Using this rate, the DFC would only be $310

/TEU (assuming a TEU tare of 2.0 tonnes). We note this is substantially lower than $650 estimated by BITRE, in fact less than half!

b) Our analysis above is consistent with the information provided in the Aurecon Report completed for the FLCT that indicated that a rate of $2.30 /km would be commercially achievable.

Therefore, in conclusion Norske Skog believes that the current BITRE calculation of an RFE of $650 is significantly inflated to what could actually be achieved and therefore results in a dramatic underestimation of the overall freight cost disadvantage. At a transport rate of $2.50/km, the DFC would be $310 / TEU which is only an increase of 10% over the RFE of $281 determined in 1998 and the basis of the current TFES. Note that even at an elevated rate of $3.00 /km rate the DFC would be only $355/TEU or an increase of 26 % over the 1998 base.

Intermodal Costs

Another important parameter of the TFES is the intermodal costs. This has not been mentioned much in the Productivity Commissions Report but is a significant additional cost that Tasmanian shippers bear. Since 1998, this has been determined to be $100 per TEU with no review or escalation. As Norske Skog has indicated in our confidential submission, intermodal costs have increased and are currently $145 /TEU. There is therefore a significant shortfall in the Scheme's assistance on this parameter. To be clear, this doesn't include the additional transport costs due to the short transport leg from the Melbourne Wharf to our customers in Melbourne. The current cost of $228 /TEU for the 15 km trip would be significantly reduced (by at least $150 /TEU) if this leg was excluded and we supplied customers directly by truck from the Boyer Mill, as is done on a daily basis from our Albury facility.

The recommended move to a single flat rate of assistance per TEU is not substantiated and was universally rejected the last time it was proposed by the Commission. While Norske Skog has no strong objection against this, we understand that smaller shippers would be most disadvantaged by such a move.

On a positive note, we welcome the discussion in the Draft Report concerning the possible inclusion of international-bound freight in north-bound shipments. We strongly support such an initiative as the best way to address the current lack of international shipping from Tasmania. We note however, that the Commission has not included a specific recommendation on this matter and would urge it to do so in its Final Report. Such a recommendation should not however be at the expense of reducing existing TFES support in another area. Each issue should be considered independently and on its merit.

We would also like to commend the Productivity Commissions support for the Federal Government's review of Coastal Shipping Regulation as soon as possible, specifically their impact on shipping efficiency and cost across Bass Strait and on coastal shipping routes more generally. We strongly agree that as an island state, Tasmania is especially vulnerable to regulation and regulatory change that increases the cost of engaging in coastal trade.

I would like to repeat our previous offer to the Productivity Commission representatives to visit the Boyer Mill at any time to review our freight arrangements and to raise any technical, commercial/financial or any other questions that you may have. Indeed, I would encourage Commission staff to visit a range of both large and small Tasmanian exporters to see firsthand the continuous steps taken to achieve the lowest possible freight costs in order to compete and survive in open, competitive world markets.

Please do not hesitate to contact me or Arnold Willems at any time if we may be of further assistance.

Yours sincerely,

Rod Bender
General Manager
Boyer Mill