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

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

24 February 2014

Dear Mr Quinlivan,

This submission largely seeks to address the response by the Bureau of Infrastructure, Transport and Regional Economics (BITRE) to Norske Skog's submission to the Productivity Commission draft report. We believe that in many cases, BITRE have sought to paint Norske Skog's real world data and actual experience as a special case (because we are a large shipper who can negotiate low road rates) rather than acknowledging it as being reflective of the situation generally, where we are also able to negotiate lower sea freight rates. We firmly believe that the *relative difference* (ie the cost disadvantage) between our sea and road rates would be similar (or at least no more) to the *relativities* between sea and road rates paid by most other (albeit smaller) shippers. The important issue for the Productivity Commission surely centres on the *relativities* of each Scheme participant's comparative and actual rates, and not simply the specific rates for either sea freight or road freight equivalent rates for any particular freight task of individual participant in the Scheme. Rather than seek to confirm or repudiate Norske Skog's proposition, the BITRE have sought to dismiss each matter and have chosen to continue to support the use of non industry peer reviewed assumptions that we believe do not reflect reality. Surely the Productivity Commission's view must be informed by the reality of the situation facing shippers throughout Tasmania. Only at this point, informed by a real world perspective, can the Commission's review of the Scheme be seen to be executed effectively with any recommendations aimed directly at dealing with the real challenges businesses in Tasmania face with regards to the disadvantages associated with freight costs across Bass Strait.

We urge the Productivity Commission to rigorously examine this matter and not to base its conclusions and recommendations on BITRE's flawed viewpoint and approach.

Bass Strait Shipping Cost

Norske Skog has previously raised the fact that the median rates, using the TFES claims data for all Wharf to Wharf full container load shippers on the Victoria – Tasmanian routes between 2007/08 and 2011/12, does not reflect our own and others experience in the actual real movements in shipping costs over the same period of time.

We referred to BITRE's own shipping data which shows a 9% increase and we are sure that all shippers throughout Tasmania have had at least similar increases. BITRE in their response have indicted that they are not aware of the data series from which Norske Skog drew this conclusion. This information was in fact derived from BITRE's own information. As the BITRE parameter review (2013) did not show the nominal freight rates, we had to make our observations based on the graph in the Review. See the graph attached below. This shows that the 'non-bulk freight rate' index moved from approximately 120 in 2007/8 to approximately 129 in 2011/12. A shift of this magnitude represents an absolute movement in rates of around 7%.

Norske Skog Paper Mills (Australia) Limited
Boyer

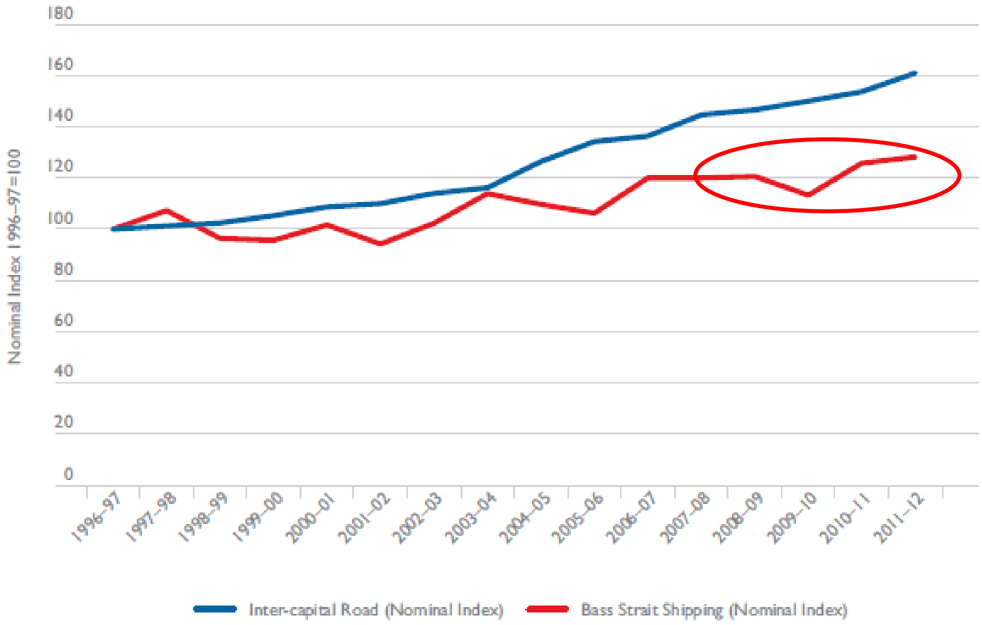
Boyer
Tasmania 7140
Australia

ABN: 84 009 477 132
Phone:+61 3 62610111
Fax: + 61 3 62613247

Non-bulk freight rates since 1996–97

Figure 3 illustrates freight rate trends using a nominal index. Road freight rates had increased 24.8 per cent more than sea freight rates by 2007–08. By 2011–12 this difference had increased to 32.7 per cent.

Figure 3 Nominal freight rate indices: road and Bass Strait shipping, 1996 to 2012



Note Estimated Bass Strait freight rates are weighted average nominal freight rates per tonne for wharf-to-wharf full container loads in the TFES database. Inter-capital road rates assume zero empty running.

Source BITRE Information Sheet 28, BITRE Estimates based on TFES data and SKM 2013 Road Rates.

Further supporting information that the "median" clearly doesn't reflect the real changes in the sea freight rates is shown in SKM Freight Rates update 2013 Table 4.4 (work undertaken specifically for BITRE) that shows that the Northbound TEU Bass Strait freight rates between 2008 and 2012 moved from 9.5 c/ntk for dry freight to 13.96 c/ntk. A change of 4.46 c/ntk which represents a massive 47% increase. See below a copy of the table from the 2013 SKM Report.

Copy of Table 4.4 from SKM Report 2013 (undertaken directly for BITRE)

Table 4.4 : General Bass Strait freight rates between Melbourne and northern Tasmania (c/ntk) 2006 – 2010

	Distance	*2011/12 average net mass*		2006		2007		2008		2009		2010		2011		2012	
		Dry	Reefer	Dry	Reefer	Dry	Reefer	Dry	Reefer	Dry	Reefer	Dry	Reefer	Dry	Reefer	Dry	Reefer
	km	*t*	*t*	c/ntk	c/ntk	c/ntk	c/ntk	c/ntk	c/ntk	c/ntk	c/ntk	c/ntk	c/ntk	c/ntk	c/ntk	c/ntk	c/ntk
TEU																	
Northbound	**420**	**14.5**	**11.3**	8.5	9.6	9.2	9.8	9.5	9.9	10	11.8	11.9	12.6	12.93	15.52	13.96	18.44
Southbound	**420**	**17.9**	**15.9**	7.1	9.6	7.8	9.7	7.7	9.9	8	11.2	8.2	12.9	9.82	13.08	11.44	13.25
Trailer load																	
Northbound	**420**	**15.0**	**20.0**	14.1	14.6	14.7	14.8	14.9	14.9	15.1	18.1	15.4	18.3	21.19	19.57	26.98	20.83
Southbound	**420**	**25.0**	**24.0**	15.7	16.2	15.4	17.1	16.2	17.4	15.2	20.1	15.3	20.2	15.84	18.88	16.38	17.56

Source: SKM. Rates and trailer mass from shipping company discussions; container mass from BITRE (TFES database)

In conclusion, Norske Skog remains significantly concerned with the conclusion drawn by BITRE that because the median shipping costs across Bass Strait have reduced over recent years, so has sea freight. We don't think this is the reality for any single shipper participating in the scheme, in fact quite the opposite. We have asked ourselves on many occasions since the Draft Report was issued for comment, "Is there some flaw or quirk with the use of the statistical median? Could it be the data set that informs the calculation of the median has changed significantly over time?" We are now concerned that there may be a perverse impact of increasingly higher shipping costs for many shippers in Tasmania on the statistical calculation of the 'Median Wharf to Wharf Median Cost per TEU'. Claimants at the higher cost end of the Scheme, which in many cases may be smaller volume shippers, may well have (over the same time period) stopped making 'Wharf to Wharf' claims, and have instead made the (administratively simpler) claims as 'Door to Door', because seeking additional information (the Wharf to Wharf component) from shipping companies does not attract any additional payment. The effect of this would be that these shipper's volumes would not be included in the statistical calculation at all as they aren't any longer in the 'Wharf to Wharf' claim category.

This may be one component of the explanation on how it is that all shippers have experienced relatively significant increases in shipping costs across Bass Strait, yet despite this fact, the calculation of the statistical median shows a figure indicating that costs have become lower over the same period.

Road Freight Equivalent Costs

1) Actual Road Rates:

In response to information Norske Skog provided on the Actual Freight rates, BITRE response was :-

17. Norske Skog's road rates cited at point (a) a spot rate that reflects marginal cost pricing for a very large shipper. This rate is not suitable for benchmarking as it is not indicative of general market rates that are available to most shippers.

18. Norske Skog points out that its spot pricing rates— for a very large, specialised shipper on a short term marginal basis –are "consistent with" (unsourced) industry rates used by Aurecon for its benchmarking analysis.

19. Norske Skog submission suggests that the 'industry sourced' freight rates underpinning Aurecon Report's "benchmarking" analysis is a low spot rate. That is not a representative 'market benchmark'.

To be clear, Norske Skog strongly believes that a road rate of between $2.50 /km and $3.00 /km is achievable based on our actual experience with road transport for very similar tasks on the mainland at our Albury Mill (and not marginal costing or spot rates). We are in quite a unique situation because we can directly compare our Tasmanian operation's transport costs to our Albury Mill's transport costs (based largely on road transport) where we make identical products, in almost identical volumes for the very same customers in the same locations.

We have already acknowledged in previous submissions, and acknowledge here again, that we are one of the larger organisations shipping from Tasmania and therefore our transport cost may be lower than some others. Some argue therefore that our experience on the specific freight cost disadvantage would be different to medium to small shippers. We believe however that the relative freight cost disadvantage (in other words the specific difference in rates that represents the cost disadvantage borne) would not be significantly different (or at least their disadvantage would not be any less than large shippers) since the ability to negotiate lower rates (based on volume/scale etc) would similarly apply to both sea and road transport and so the "relative difference" (and therefore the freight cost disadvantage) would remain similar. This view is backed up by what other shippers, including many smaller shippers, have presented in their written and verbal presentations to the Productivity Commission's Inquiry.

Further consideration on the matter of what is a "suitable/representative" road transport rate raises the question for Norske Skog on whether in fact SKM 's (2013) rate of 11.7c/ntk is a representative road rate for a "median" shipper (as defined within TFES). Norske Skog has not been able to find any information or discussion that demonstrates this. SKM promotes that the typical rates are relevant for a shipper of goods spending about AUD $60,000 - $120,000 per month (SKM 2013 pg 31).

2) Tare weights of TEU's

Norske Skog raised concern that the tare weight of a TEU used by BITRE, namely 1.5 tonnes, was too low for use in their calculation for the net payload in the Road Freight Equivalent (RFE) calculation. BITRE responded that this was based on half the weight of a standard 40 ft dry container, being 3,064 kgs. Norske Skog absolutely rejects that this should be the basis of the determination of the "representative tare for a TEU". First, the majority of containers (approximately 85% ….pers comm. with large shipping company) are TEU's not FEU's. Standard TEU's vary between 2 - 2.5 tonnes (see BITRE's own table 7 Parameter review 2008) and in fact high cube 20 ft (tare 2.4 tonnes) and 2 Pallet wide 20ft containers (tare 2.56 tonnes) are heavier again. Note 95% of domestic 20ft on Bass Strait are two pallet wide.. Secondly, BITRE's suggested tare is inconsistent with the assumptions used when the parameters were first established in 1997/8 when they were based on "two TEU's" not one FEU. (TFES 1988 p 11. ….." The Standard 6.1 metre (20 ft) container provides a convenient unit and is the transport unit adopted for two thirds of all freight shipped under the scheme"…)

Thirdly, even if standard 40ft containers were to be considered as the basis for the TEU tare, and even though this would represent a shift away from the long standing and common sense basis for the Scheme's calculation, then it should be recognised that the average 40 ft container is not 3.064 tonnes but somewhere between 3.5 – 4.0 tonnes (see BITRE's own information - table 7 Parameter review 2008) and other references below

Sources and corresponding weights of a Standard FEU for Dry Freight

http://en.wikipedia.org/wiki/Intermodal_container = 3,800 kgs

http://www.bluefreight.com/containers = 2,800 to 4,000 kgs (simple average = 3,400 kgs)

http://www.carelogistics.com.au/sea-container-sizes.html = 3,970 kgs

http://www.australiatrade.com.au/Shipping/ContainerSizeSales = 3,980 kgs

http://www.wwcf.com.au/Container-sizes = 3,800 kgs

http://www.paccon.com/webfiles/Paccon/files/SEA_CONTAINER.pdf = 3,980 kgs

http://answers.yahoo.com/question/index?qid=20090425155416AADAL0C = 3,800 kgs

http://www.seaplus.com/container.html = 3,900 kgs

http://www.vantagefreight.com.au/wp-content/uploads/2013/01/Container-Dimensions.pdf = 3,980 kgs

http://www.griffinlogisticsco.com/reference/container_info.pdf = 3,900 kgs

Surely this again highlights the need for real world data to be used as the basis for a Scheme that seeks to address the real world cost of business challenges faced by Tasmanian shippers under this Scheme. BITRE should be encouraged to use real world figures for their assessments, and nothing less.

3) Road Transport rates - empty running assumptions.

Norske Skog previously questioned why BITRE increased the trucking rates provided by their consultant (SKM) by a factor of 30% to make allowance for empty running time. BITRE’s response is somewhat confusing as on page one they indicate the rates “are typical rates for large shippers, <u>excluding back loading rates and do not allow for empty running</u>” and yet on page 4 they indicate that SKM’s (rate) includes a 20% empty running time. They then, contrary to SKM’s suggestion, (which is based on actual rate experience (SKM 2010) of 20%) adjust the rate back to a 30% unloading factor. Was this assumption tested with industries’ actual experience? Does the Weight In Motion data,that BITRE relies on accurately reflect the “empty running rate? It is also not clear whether the SKM rate of 11.7 c/ntk includes back loading rates, as would be the reality in the real world.

In summary with relation to BITRE’s recent response to the Productivity Commission, and specifically with regards to BITRE’s comments related directly to questions Norske Skog raised in its previous submissions, we remain unconvinced that BITRE have fully understood our questions and feel that many remain unanswered.

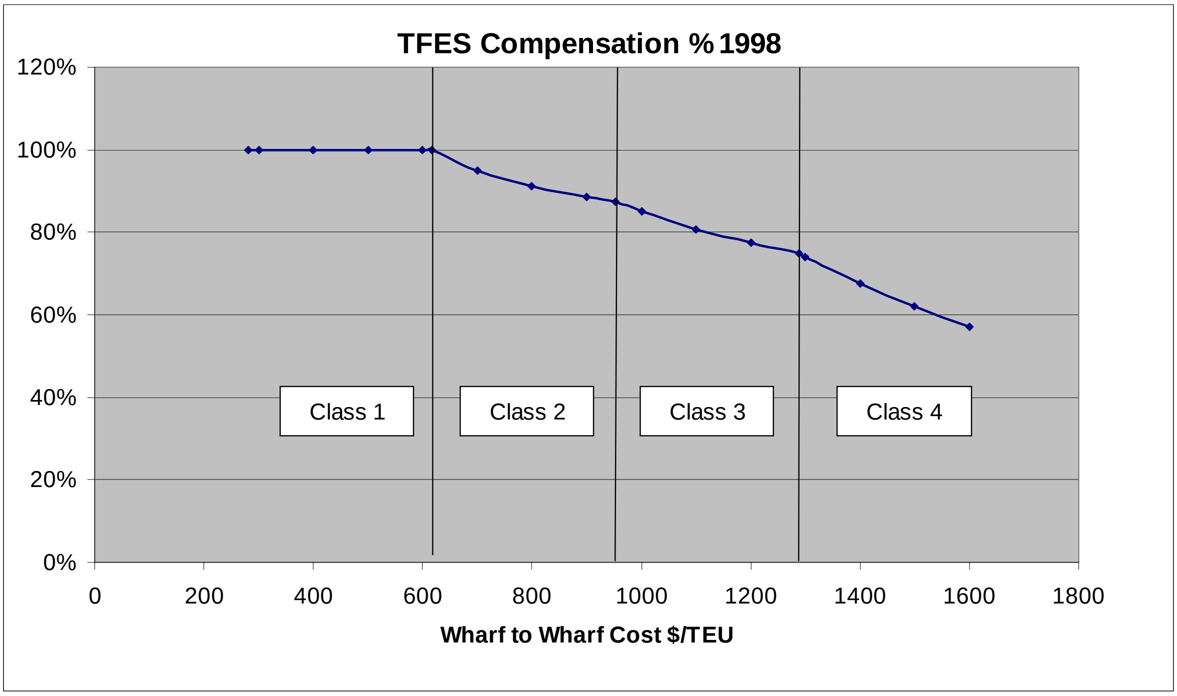
Finally on the matter of BITRE’s input into the Inquiry, and at the risk of repeating a now common message from many Scheme participants, Norske Skog absolutely rejects any conclusion which indicates that any level of ‘over compensation’ is occurring within the existing Scheme. The fact remains that many participants, if not all, have seen benefits from the Scheme eroded over time, and in Norske Skog’s case the current level of ‘under-compensation’ is around 27%. This also relates to the inter-modal allowance which remains steadfastly fixed at $100/TEU.

<u>TFES Underlying Design Compensation Level</u>

At the Public Hearing in Hobart on 4 February 2014, the Productivity Commissioner indicated she would appreciate a view on what level of compensation had been 'built into the scheme back when the last parameter review was conducted. Norske Skog has prepared the following material. It clearly shows (after excluding the inter-modal component of $100 per TEU) that for shippers who's costs (wharf to wharf $/TEU) were at the lower end of the spectrum, compensation was available at the 100% level, with compensation reducing (almost linearly) to around 60% for shippers who had higher transport costs across Bass Strait.

Importantly, for the 'median shipper' the level of compensation was 88%. It is clear from this that the system was designed to encourage shippers to drive efficiencies (and therefore lower costs) in their freight arrangements across Bass Strait.
Also of interest is that while the median shipping cost in 1998 was $952 wharf to wharf per TEU, it is now approximately $1,100 wharf to wharf per TEU, effectively reducing the scheme’s level of support for a median shipper by 7% (a 7% erosion of benefit just as a result of the passage of time, without inter-modal and other cost increases on top of that further weakening the Scheme’s support for business in Tasmania).

We would further point out that in 1998, all of the Boyer Mill's freight movements fell into the 100% compensation bracket - while now on average we are at a much lower level of 87%, an erosion of 13% in the level of compensation to Norske Skog’s Boyer Mill since 1998.



<u>TFES Application to Northbound Export Freight</u>

In Norske Skog's 'Commercial in Confidence' Submission to the Inquiry, we indicated our strong support for the Scheme to be expanded to provide 'TFES like' assistance to freight bound for international destinations through the Port of Melbourne. This was further reiterated at the Public Hearing held in Hobart on 4 February 2014.

Norske Skog would like to be very clear that it has no need for a direct international shipping service from Tasmania. In fact, Norske Skog believes that there are several significant factors that would lead to such a freight solution limiting Tasmania's opportunities in linking Tasmanian businesses with key overseas markets. These factors include both immediate and longer term issues. The most salient factors from our perspective are:

- No single freight provider services all destination ports currently used by Tasmanian exporters, requiring trans-shipment arrangements and associated costs for many/most.
- No single freight provider offers the most competitive rate into all destination ports that they do service.
- No single freight provider will be able to offer the intervals of service required by many of our exporters to satisfy their need to be responsive to market expectations.
- A single freight provider will not provide a sound basis for ongoing competition on those routes, increasing the potential for longer term rate escalation.

Comments from Norske Skog relating to BITRE's comments on the Aurecon Submission

Norske Skog would also like to comment on BITRE's response to the Aurecon Report to the FLCT.

Shown below are excerpts from the BITRE Submission followed by Norske Skog's commentary.

BITRE has identified the following issues with the Aurecon 'TFES benchmarking' (Table 36 page 90):

*1) **The Export container does not require a 'further road leg' of $100 (local Melbourne delivery)**.*

If Norske Skog understands this correctly, BITRE are suggesting that once export bound freight has arrived in the Port of Melbourne, there is no additional freight leg required. This is in fact not correct. There is in fact an additional transport leg directly associated with moving the export bound freight by truck from the domestic wharf facility to the international export facility.

*2) **Aurecon incorrectly states on page 89 that the TFES definition of 'notional wharf to wharf' freight rate includes 'lift on lift off' costs**.*

- ⇨ *As defined in the TFES, the notional wharf to wharf cost is 'blue water' only - by definition this excludes intermodal costs including lift on and off costs.*

BITRE are not necessarily correct. It depends where the lift on/off occurs. If it is done at the wharf (within the wharf gate) and is part of the shipping company's invoice then it is included in the wharf to wharf component. If it occurs external to the facility then it is not included in the wharf to wharf cost. (see TFES Ministerial Directions of 2008 – Guidelines – November 2013) The majority of lift on/lift off from land transport modes to shipping modes from Tasmania is done within the wharf gates.

For reference the TFES definition (Page 62 of the Guidelines)for wharf to wharf freight bill is:

> "The wharf to wharf freight bill is defined as including the relevant parts of those onshore costs incurred at the wharf that are incorporated in the freight rates charged by the shipping company. The wharf to wharf freight bill can include *stevedoring*, container hire, terminal and cargo related port authority charges (i.e. wharfage), where these items are charged and paid separately by the shipper.
> The wharf to wharf freight costs used in the calculation of assistance are not to include other transport services that extend beyond the terminal area"
>
> "Wharf" for the purposes of TFES means the wharf gate. (page 32 of the Guidelines)

Conclusion

Norske Skog is still strongly of the view that we and other Tasmanian shippers are not being overcompensated for the freight cost disadvantage under the current TFES parameters. The Productivity Commissions conclusion in the Draft Report, which is based on information from BITRE has confounded us as were have been unable to conclusively identify what has driven such a dramatic and important difference in the level of equalisation currently available. We have at every stage attempted to raise any questions that we thought might lead to a better understanding of these issues, most notable the dta and submissions made by BITRE (and SKM as a consultant contributor)

From our perspective, and no doubt the same many other manufacturing industry stakeholders operating in Tasmania, any changes to the TFES as a result of this Inquiry that reduces the Schemes benefit (without there being an evidence based, conclusive foundation for over-compensation) will prove pivotal in reducing how sustainable, or not our businesses will be into the future. It is clear then, that it is in the interest of all Tasmanians that this Inquiry be based on the best and fairest assessment of what freight cost disadvantage exists, and how best to design the Scheme and its parameters to ensure this the right level of equalisation occurs.

We remain open and willing to assist in any way possible with this end in mind.

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