



Submission to the New Zealand
Productivity Commission

**On the International Freight
Transport Services Issues Paper**

By the Meat Industry Association

31 August 2011

Introduction

The Meat Industry Association of New Zealand Incorporated ('MIA') is a voluntary trade association representing New Zealand meat processors, marketers and exporters. It is an Incorporated Society (owned by members) that represents companies supplying virtually all of New Zealand sheepmeat exports and all beef exports.

In the year ended June 2011, the meat industry exported more than one million tonnes of product, generating \$6.2 billion in export revenue, which was 13% of our nation's exports by value (and 23% of New Zealand's primary sector export revenue).

The meat industry is highly export-focused, and relies on cost-effective, reliable and timely international freight transport services to distribute products to the 119 countries it exported to in the year ended June 2011.

Attached to this submission is an article that MIA prepared for the Journal of the Chartered Institute of Logistics and Transport NZ, which provides further information in addition to the responses to the questions raised in the Issues Paper.

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Questions

MIA is not in a position to provide information on all the questions raised in the Issues Paper, and has concentrated on questions particularly relating to shipping services and transit times.

Question 4. What environmental considerations should fall within the scope of this inquiry? What issues are of particular importance?

MIA believes that the inquiry should consider the impact of the Emissions Trading Scheme (ETS), given the absence of similar action by overseas competitors, and a lack of tangible progress in international climate change negotiations.

MIA also believes that the inquiry should consider environmental policies that are being introduced by other governments, as these are likely to have an impact on New Zealand's international freight transport services.

For example, the EU is planning to include international aviation services in its ETS, and may also include shipping services. It was also reported earlier this year that the European Commission is considering the possibility of implementing a mandatory speed reduction for all ships entering European Union ports. These actions have the potential to increase the costs and transit times for New Zealand exporters sending products to Europe.

Another concern is the push by NGOs, via the Clean Shipping Coalition, to require mandatory slow steaming under the aegis of the International Maritime Organisation.

Q19 From the perspective of New Zealand importers and exporters, to what extent is the international shipping industry competitive?

At a national level exporters have choice between carriers. However, choice is increasingly cosmetic as most vessels are shared across multiple carriers limiting choice in service delivery (transits etc). Carrier ability and propensity to constrain supply has meant in reality choice has been negated particularly during the peak demand period.

At an individual port level exporter choice is significantly more limited or non-existent. For example, Bluff is only served by one carrier. Only exporters with ability to present cargo to the "hub" ports of Auckland, Tauranga, Lyttleton and to a lesser extent Port Chalmers and Napier enjoy significant choice in carrier and vessel.

Q20 To what extent have collaboration agreements between international sea carriers been helpful or harmful to the interests of New Zealand importers and exporters?

Collaborative VSA agreements between shipping lines have enabled an increase in the average vessel size calling New Zealand, reducing the average cost per unit of capacity to the carrier. However, this has been at the expense of freight owner choice in service delivery. Carrier collaboration has also arguably been used to artificially constrain capacity creating an environment whereby a reduction in the cost to serve has rarely translated directly to a price to serve reduction for freight owners.

Q25 How do international shipping conferences permitted under the Shipping Act 1987 affect the accessibility and efficiency of sea freight services available to New Zealand exporters and importers? How strong or weak is the case for the exemption of conferences from the competition provisions of the Commerce Act?

The conference exemption permits collaboration in both the supply of capacity and the setting of price levels. There is ample evidence of this exemption facilitating capacity control through the proliferation of Vessel Sharing Agreements (VSA's) or "code sharing" for ships between carriers which have enabled an increase in the average vessel size calling New Zealand, reducing the average cost per unit of capacity to the carrier.

This has been at the expense of freight owner choice in service delivery and while there is little evidence of deliberate price fixing between carriers, cost to serve reductions have not necessarily translated to a price to serve reduction for freight owners, as under the exemption carriers have been able to artificially constrain capacity further limiting choice.

While the international shipping exemption has the potential to benefit New Zealand through lowering the cost to serve, the potential for abuse of the exemption to artificially constrain capacity and reduce competition has shown the case for exemption in its current form to be weak.

Questions 27-45 (covering airports and air services)

Only a very small proportion of the meat industry's exports are transported by air, approximately 0.5% by volume, so MIA is not in a position to make detailed comments on these questions.

However, while only a very small volume of meat is transported by air, what is air freighted is generally high value, time and temperature sensitive product – so having reliable and competitive air freight services is still important for the industry.

Do New Zealand's Customs and Biosecurity systems deliver the required outcomes efficiently? What initiatives might improve efficiency and effectiveness?

While government agencies have been undertaking steps to improve the efficiency of border processes, through projects such as the Joint Border Management System there is still the potential for greater efficiency, as much of the information and many of the assurance required by government agencies are common.

For example, under the China FTA goods exported to China require a Certificate of Origin, issued by a designated non-government organisation.

For the meat industry this is extra, unnecessary, cost as nearly all the information required for the certificate of origin is already produced on other official documents that accompany meat exports. Any extra information required to certify origin could simply be included in one of these documents.

While rationalised government systems can reduce duplication and cost, it is important to ensure that the costs involved in introducing a new systems (such as IT development costs) do not outweigh the potential benefits.

There is also the need to balance a focus on efficiency with the need to ensure the effectiveness of New Zealand's biosecurity systems - particularly with regard to imports.

Question 49. Are there any measures that New Zealand could undertake to reduce the security-related costs imposed on exporters and importers?

Security-related requirements being imposed by governments, particularly in Europe and the US, increase costs and transit times for New Zealand exporters.

These security-related requirements take a 'blanket' approach rather than a risk-based approach to security measures, and do not recognise that cargo from some countries, such as New Zealand, poses very little risk.

New Zealand has over the years developed robust and well-respected border and security systems and scientifically based assurance systems and processes, which the government can use in the negotiation of equivalency arrangements, in order to mitigate the impact of these security requirements.

Question 53. What are the costs of transit times for exporters and importers?

For both exporters and importers lengthy transit times adds cost - the opportunity cost of capital tied up in goods while in transit. For exporters this cost generally cannot be passed on, given the competitiveness of international trade.

For exporters of perishable goods that have a limited shelf life, such as chilled meat, long transit time also reduces an exporter's ability to service a market with confidence, and if transit times are too long, the export of chilled product is not a viable business model.

As a significant, and growing, proportion of the industry's exports is premium priced, time-sensitive, chilled product, transit times are becoming increasingly important for the meat industry.

Over the last 10 years, both the volume and value of chilled lamb exports have doubled to 67,856 tonnes and \$877 million respectively, in the year ended June 2011. Exports of chilled beef have also grown over the period to 25,025 tonnes, worth \$262 million.

Europe is the industry's major market for chilled products, in particular chilled lamb. The shelf life of chilled lamb is in the region of 70 days but can be as little as 63 days.

The transit time from New Zealand to Europe has normally been in the region of 30 to 32 days and so about half of this shelf life has been used in the actual sea voyage. Before shipment, time is required in New Zealand to consolidate and equilibrate product before loading. On arrival in the market the product has to clear customs, move to facilities to finish processing, packaging into a retail ready form, weigh price labelling before being distributed to the retail outlet.

Generally, remaining shelf life once product actually gets onto shelves in the UK and Europe is around 15 to 16 days. This allows enough time to enable the product to be displayed, purchased, taken home by the consumer and refrigerated for a day or two before being safely consumed without the shelf life having expired.

However, there is little margin for error, and any delays can be costly. The shorter the remaining shelf life, the less leverage the industry has with customers in the market, and the greater likelihood that the exporter will have a distressed product on their hands. This will often require a significant discount to move or the product will need to be frozen down, with a significant reduction in value.

Question 54. What sources of delay contribute to transit time? How might those delays be efficiently reduced?

Slow steaming and security requirements contribute to delays in transit times.

In recent years shipping lines have reduced the speed of ships operating on a significant number of services globally, a practice known as slow steaming. Operating cost savings, augmented by a stated environmental benefit, appear to have been the main motivations for the introduction of slow steaming.

However, as slow steaming increases transit times, it has a negative impact on industries, such as the meat industry, which export time-sensitive products.

Most cargo to Europe is trans-shipped via a hub port in Asia, and slow steaming generally only occurs on the second leg from Asia to Europe.

With slow steaming on the Asian to European leg the transit time has been extended by around five days. It must be stressed that there is a big difference between the carriers in the actual transit time and between the various European destinations. Based on information from carriers the current actual transit time is between 31 and 45 days. This is a wide range and depends very much on the port rotation and the individual carrier's service profile.

There is therefore the danger in looking at averages, but the important factor is that slow steaming, by definition, generally will mean a longer transit time.

As noted in the answer to question 53, there is currently no margin for error when exporting chilled lamb to Europe, and any further utilisation of slow steaming has the potential to put this trade at risk.

Slow steaming was introduced with very little consultation with customers about the impact that it could have on their businesses. Carriers need to talk to customers about the ongoing place of slow steaming in their service offering, particularly as customers require certainty about whether or not it is a permanent development, so they can plan their own business accordingly.

With regard to the increase in transit time related to security requirements, as noted in answer to question 49, the meat industry would like to see government agencies more actively negotiate equivalency type agreements in order to mitigate the impact of the security requirements.

Q64 Does the imbalance of container use create significant costs? What practical measures might efficiently reduce these costs?

Imbalance of container use at both national and regional level (coupled with the prevailing use of closest port by NZ importers and exporters) creates significant supply chain wastage/cost necessitating “empty running” by both international and domestic transport assets E.g. approximately 1 in 2 containers are positioned into NZ empty with the exception of import dominant ports such as Auckland and Lyttleton, almost all are repositioned empty around the coast to serve smaller regional ports.

Regional empty positioning could be addressed by consolidating cargo to ports that have natural container inflows, though this would need to be combined with a change to moving product to containers, packing closer to the natural supply of containers.

Question 65. What are the potential benefits and risks for New Zealand from a move to hub-and-spoke configuration for international shipping? Are there actions New Zealand can take to increase the likelihood of benefits or to manage the risks?

A move to a hub and spoke configuration among NZ ports has the potential to reduce flexibility for exporting industries such as the meat industry with widely distributed processing facilities – increasing domestic transit times and costs.

However, if some NZ ports do not undertake preparations to become capable of handling bigger ships, there is the danger that the shipping lines might hub out of Australian ports, which would significantly increase the transit times and costs for NZ exporters.

Question 71. Is there a role for government to require the disclosure of performance measures in specific components, and to collate and publish this data?

We believe that there is a role for the government to collect and publish some data – as long as this does not impose significant costs or time commitments on the parties that are required to collect and report this data.

For example, in its report on Big Ships¹, the New Zealand Shippers' Council found that data on overall container throughputs and volumes was difficult to obtain, and recommended that the Ministry of Transport establish a regime to collect this data.

¹ The Question of Bigger Ships, New Zealand Shippers' Council, August 2010 - http://www.shipperscouncil.co.nz/documents/The_Question_of_Bigger_Ships.pdf

MEAT INDUSTRY

An internationally competitive supply chain?

by Tim Ritchie

FOR AN industry that exports some 90% of its production, international competitiveness is absolutely crucial. The New Zealand meat industry has been in the export business since 1882, and since then has been shipping a perishable food product from one side of the world to the other. A key enabler was the combination of refrigeration technology and ships, as important now as it was when introduced 129 years ago.

In most of our markets we face competition from domestic producers who do not face our shipping costs. Similarly, we face competition from other exporters, such as Australia. We are not low-cost producers and as such cannot live with an uncompetitive supply chain.

For much of those 129 years, we had bespoke shipping services dedicated to servicing Australasia's importing and exporting needs. For much of our trade, that is now no longer the case, and therefore our ability to control, let alone even influence, our destiny has reduced. That has become very evident in recent years.

Important factors

What do we mean when we talk about competitiveness? Cost is clearly a major factor, domestically for the collection of livestock and transport to plant, the marshalling of the resulting products to the port of departure, transfer onto vessel and then transport to market.

Then there are a number of other factors relating to the service quality, such as temperature integrity for chilled meat (plus/minus half a degree) which has a major influence on shelf life.

Finally, the transit time to market and the frequency and reliability of services are significant factors in the competitiveness of our supply chain.

These have become increasingly important as a growing proportion of the trade is with time-sensitive, premium-priced, chilled product. Chilled lamb is now a billion-dollar business, and distant Europe remains the most important destination for chilled lamb, running at almost \$900 million each year, and with annual growth in double digits.

This trade requires the regular arrival of vessels with a timely transit in order to ensure a continuous supply of quality product on supermarket shelves. That product needs to be displayed with sufficient shelf life, enabling the consumer to purchase, take home, leave in the fridge for a few days before cooking and consumption.

Slow steaming

So on this basis, how do our shipping service suppliers currently perform? Aside from cost, there are several areas of particular concern to the meat industry, including 'slow steaming' by carriers and a reduced responsiveness to the needs of the shipper – their customer.

As an outcome of the international financial crisis and downturn in international trade, carriers decided to slow the vessels down from around 24 knots (full throttle) to 18 knots and bring more vessels into the service, thereby utilising some of the excess capacity that would otherwise have remained tied up.

Slow steaming provided significant benefits to carriers in terms of fuel savings and reduced CO₂ emissions – good PR in being seen to help save the planet – but with little consultation with their

customers and the impact on their business. Nevertheless, it seems to be here to stay.

There has been a clear collision between this major shipping trend and our industry's 30 years' steady development of the premium chilled meat business. There will be other exporters of perishable goods, such as fruit and vegetables, in the same position.

Adding cost

For most shippers, whether exporters or importers, increased transit time adds cost – the opportunity cost of capital tied up in goods while in transit and, given the competitiveness of commerce, a cost that generally cannot be passed on.

For shippers of perishable goods, such as chilled meat, seafood, fresh fruit and vegetables – in total about \$3 billion annually (and think about the financing costs of five days' deferred payment on that) – the increased transit time for each voyage eats into shelf life, reducing ability to service the market with confidence.

While the carriers subsequently adjusted their port rotations to try and contain the impact, it is nevertheless a development which our industry remains very wary of. It has reduced by around a third chilled lamb's remaining shelf life on arrival in Europe. This seriously reduces the margin for mishaps and will inevitably result in product being downgraded.

Around the corner

While, in theory at least, slow steaming does have a positive impact on schedule reliability – given a vessel has the ability to speed up when required to maintain schedule – the real worry is what may be around the corner.

That is super-slow steaming, which has been proven to be technically possible – around 12 knots, which is slower than the 19th century clippers like the *Cutty Sark* (14–17 knots), and saves even more fuel. We fear super-slow steaming may be the carrier's response to another major downturn in trade or an oil price crisis.

The point might come when the business model just won't work. In the case of chilled lamb exports to Europe, super-slow steaming would leave only a third of the normal shelf life on arrival – clearly insufficient time to safely service that steadily expanding market.

Another concern is the push by NGOs, via the Clean Shipping Coalition, to require mandatory slow steaming under the aegis of the International Maritime Organisation. They have been rebuffed twice, but are unlikely to give up.

Interestingly, in terms of lamb's carbon footprint, the ocean freight component is relatively small. For our lamb trade to the UK, it accounts for only 5% of the footprint.

Service vulnerability

Unlike the bespoke services of the past, most of our trade to Europe is now serviced by trans-shipment over Asian hubs. On that second leg, generally much larger vessels are deployed, on which the New Zealand cargo is dwarfed by cargoes from other destinations.

Therefore it is perhaps understandable that New Zealand's influence on scheduling and other decisions on that second leg are very limited. While we may be small in comparison to Chinese exporters, this is still a million-tonne-a-year business, and a very important part of the New Zealand economy.

PRODUCTIVITY COMMISSION

Inquiry into international freight transport services

HIGH PRICES for our primary products will only be of maximum benefit to our economy if the international freight services (sea and air) which move these products to their overseas destinations are efficient and effective.

In recognition of this, the government has requested the newly formed Productivity Commission, chaired by Murray Sherwin, to undertake an inquiry into international freight transport services.

Instigated by Bill English, the Minister of Finance, Simon Power, the Minister of Commerce, Steven Joyce, the Minister of Transport, and Rodney Hide, the Minister for Regulatory Reform, the commission has been asked to evaluate the factors influencing the accessibility and efficiency of international freight transport services available to New Zealand firms, and opportunities to increase the accessibility and efficiency of these services.

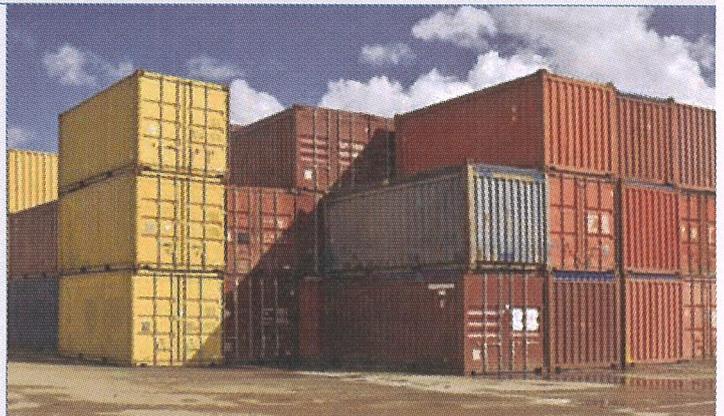
"Increasing international trade is a critical part of achieving productivity growth in New Zealand," said Mr English at the time of announcing the inquiry. "Given that freight transport costs (including port charges) currently represent a sizeable proportion of international trading costs for New Zealand firms, it is important to ensure that New Zealand's infrastructure and regulatory regimes are effective in promoting accessibility and efficiency in international freight transport services, while continuing to meet New Zealand's international obligations."

Currently, certain aspects of international carriage by air and sea are exempted from parts of the Commerce Act 1986 and subject to industry specific regimes under Part IX of the Civil Aviation Act 1990 and Part 1 of the Shipping Act 1987 respectively.

Supply chain components

For the purposes of evaluation, the commission will identify and analyse the cost of all components of the international freight transport supply chain for New Zealand importers and exporters; identify any impediments to the accessibility of the international freight transport services, and to competition within and between the components of the international freight transport supply chain; and identify mechanisms available to improve the accessibility and efficiency of the international transport supply chain.

It will pay particular attention to:



The newly formed Productivity Commission will undertake an inquiry into international freight transport services

- a) the nature of New Zealand's international trade, including the effects of distance from overseas markets and reliance on overseas providers of international freight transport services;
- b) factors influencing the accessibility, cost and efficiency of New Zealand's international freight transport supply chain, with international comparisons;
- c) the level and growth of productivity in all components of New Zealand's international freight transport supply chain, with international comparisons;
- d) the effectiveness of current regulatory regimes (including those noted above in the Civil Aviation Act 1990 and the Shipping Act 1987) affecting international freight transport services in promoting accessibility and competition, and the potential costs and benefits of alternative regulatory arrangements with international comparisons.

In undertaking the review, the commission will consult with key interest groups and affected parties. A draft report and/or discussion paper(s) will be made available for public comment, followed by a final report, which must be submitted to each of the referring ministers by 1 April 2012.

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Despite this, a major carrier has announced changes to its Asia-Europe services and port rotation which will have a major and negative impact on transit times from New Zealand to Europe.

As a result of this change, the 31-day transit time from Port Chalmers to Zeebrugge, the major entry port for chilled product into Continental Europe, will now increase by seven days. Although Rotterdam will be available with a transit of 35 days, its port costs are higher, there are not the regulatory authority relationships, and our industry's infrastructure and European supply lines have all been developed around Zeebrugge.

Coming on top of slow steaming, these scheduling changes further add to the challenges faced by New Zealand's exporters.

New Zealand is increasingly but just a pawn on the chess board, and decisions are being made by carriers with little or no consulta-

tion with their customers. Those decisions are having a major and increasingly negative impact on our competitiveness and ability to grow the premium chilled business.

At the very least, there needs to be a better and more responsive strategic partnership between the parties. A consultative, collaborative relationship between cargo owner and shipping service provider should enable each to better plan their business, and which must ultimately be to mutual benefit.



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