April 17, 2023

Att: The New Zealand Productivity Commissioner

Thank you for the opportunity to submit on the "Improving Economic Resilience" Issues Paper (February 2023), which explores the economic resilience of industries and communities in New Zealand to persistent supply chain disruptions.

In our submission below we have commented on all four of the questions posed by the paper.

A bit about NZTE and its interest in the issues raised by the paper

New Zealand Trade and Enterprise (NZTE) is the government's international business development agency. Our purpose is to grow companies internationally for the good of New Zealand.

NZTE engages with over 6,000 New Zealand exporters (our "customers"). Of these, approximately 1,400 customers are in our "Focus" portfolio, which means they receive a more intense (relationship managed) level of support. Our customers are based across all regions in New Zealand and operate in markets around the globe. They range significantly in size and market stage and include a large number of small and medium sized businesses. To support these customers, NZTE maintains a global team of around 800 people, spread across 41 countries.

The Covid-19 pandemic has highlighted that New Zealand has a serious supply chain vulnerability. During the height of the pandemic, over 60% of the nearly 300 NZTE customers that undertook supply chain reviews, sought assistance due to issues over freight and shipping. A swift and extremely costly Government intervention was required to avoid the collapse of many businesses, and potentially whole industries, because of these issues. Further, our customer surveys continued to identify supply chain issues as the most serious challenge for customers until the start of 2024, surpassing other high-profile challenges like inflation and skills shortages. Even now, supply chain challenges continue to be one of the greatest challenges identified in those surveys. New Zealand's geographic isolation means supply chain issues are felt acutely by many New Zealand businesses, and create strong pressures for exporters to relocate their operations outside New Zealand. Consequently, NZTE has a strong interest in the work the Commission is currently doing.

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Question 1: What supply chain disruptions and trends are you worried about?

There are two broad categories of concern that we have about supply chain disruption. We are concerned about:

(a) any event that disrupts sea freight – because New Zealand exporters (and importers) are particularly vulnerable to sea freight disruption; and
(b) any event that makes the navigation of supply chains more complex – because many exporters are ill equipped to manage significant supply-chain complexity.

Sea freight vulnerability

New Zealand is highly dependent on the global shipping sector. About 99% of NZ goods exported (by volume) are moved by sea (about 84% by value).

The number of shipping lines in the world has reduced significantly over the last two decades – creating strategic connectivity risk. (https://www.supplychaindive.com/news/ocean-shipping-consolidation-five-years-from-Hanjin/604803/)

A decade ago, there were around 20 global carriers. Industry commentators project that this may reduce to 6-8 in coming years. The risk this poses to New Zealand is that there are less 'suppliers' for us to negotiate with to secure the required shipping capacity to bring imports in and exports out. Reduced capacity (as shown during Covid) creates increased likelihood of higher costs and lower service levels.

New Zealand is not a high priority for global shipping companies. After global shipping rates, which had become artificially high during the peak of the Covid crisis, began to reduce again, New Zealand was one of the last markets in the world to see that reduction in rates. This suggests a reluctance to service New Zealand (requiring a price premium to service it) while there are any capacity constraints. It is reasonable to assume that future shocks that affect shipping prices will also have an extended impact on New Zealand, compared with other countries.

New Zealand has a large number of ports with disparate strategies. New Zealand ports are either operated solely by local government, or a combination of local government and the private sector, and we understand there is pressure on ports to keep investing in infrastructure to meet growing sizes of international container ships. By comparison, Australia is more consolidated in their ports – which on top of Australia's larger economy and population means those ports can more easily invest in enabling themselves to receive larger vessels. The risk to New Zealand is that, should the growth in container vessel sizes continue, New Zealand may be unable to host certain services. This may force New Zealand into a potentially slower and less frequent network. For example, it may lead to New Zealand being serviced via a hub and spoke model centred in Australia or elsewhere overseas. That said, some shipping lines have indicated that they prefer to use average sized ships with more frequent journeys, given the perishable profile of many of New Zealand's key exports.

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It is important to note that this is largely for container shipping, while bulk shipping will still rely on regional ports in a point-to-point shipping operating model.

Coastal shipping is critical in the absence of a strategy and suppliers in supporting New Zealand's resilience. This has been highlighted during recent natural disasters (e.g., when the Gisborne road and rail connection was cut after Cyclone Gabrielle, the only way to get large and consistent volumes of freight into and out of the region, was via the port and coastal shipping).

This all means that New Zealand is particularly vulnerable to sea freight disruption.

Complex challenge vulnerability

New Zealand has a high proportion of exporters that are SMEs. This creates significant risk because:

- SMEs typically do not have scale or resources to cope with significant global supply chain disruptions.
- Our experience during Covid was that most SMEs adopted a more reactive than proactive approach to supply chains, making them more vulnerable to disruption.
- SMEs lack the leverage to obtain shipping capacity during a crisis. (In contrast, for example, when shipping capacity for New Zealand was reduced by 30% during Covid, Fonterra still had the leverage to secure capacity for its largest ever volume of exports. Other large enterprises chartered break-bulk vessels to offset the shortage of container capacity and services.)

When NZTE stepped up its support for supply chain management during Covid, it became clear that most SMEs had not previously appreciated the level of their supply chain risk. Most did not appear to have considered in any depth the optimal way to manage their supply chain, nor where their main exposures were and how they could build resilience.

The relatively low sophistication of New Zealand supply chain management that existed before Covid is likely to persist because there appears to be only limited private sector (or public sector) support available to help build that sophistication.

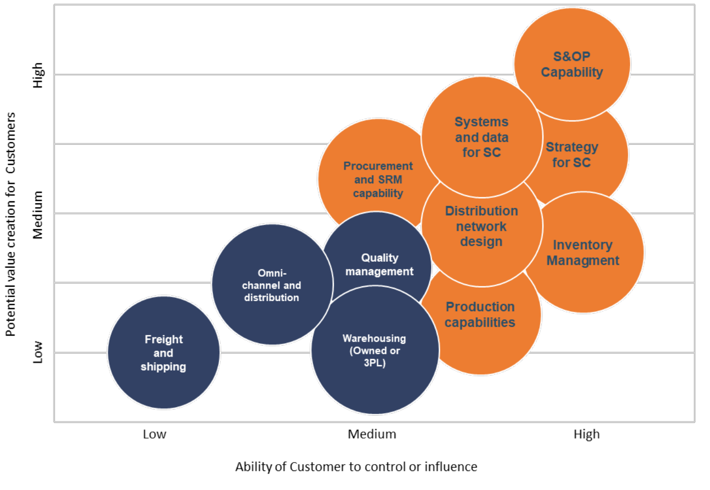
Question 2: What is your industry / community currently doing or planning to do to address your supply chain concerns?

NZTE has made a few changes in response to supply chain concerns. In particular, it has established a Supply Chain Team that provides several capability building services:

- Education: Online tools, articles, and webinars (available to all exporters)
- Intervention: 1:1 support including Supply Chain Reviews and Coaching by senior business advisors to engage on bespoke areas.

NZTE has also been one of several Government agencies that have worked to get more cross-Government collaboration on these issues.

In our interventions, we have aimed to focus on actions that will have high impact for our customers and are within their ability to influence. The chart below gives an indication of where such value for customers is likely to lie.



Question 3: How can the government help to enhance the resilience of your community / industry to supply chain disruptions?

In our view there is potential in the following ideas.

Invest in capability building for SMEs. In our view, resilience could be significantly improved if businesses had greater supply chain management capability. Such capability building would be best aimed at SMEs because they are the most vulnerable to supply chain disruption and the least likely to have been able to invest in their supply chain capability.

As Skilling (2022) says, "The remote geographic location and economic composition centred on primary production means that Aotearoa is more exposed to supply chain disruptions compared to other advanced economies". Being a small economy, at the last bus stop at the end of the world, means greater supply chain understanding, knowledge and capability is a critical enabler of future success. By being able to better plan and prepare for supply chain disruptions, we will be able to better respond, absorb and recover from them – as a nation, as regions, as industries and as individual firms.

There is also opportunity here, to not only grow supply chain capability, but importantly develop and offer relevant tools and solutions which help organisations make their supply chains more resilient. Such tools translate the 'what' into the 'how.'

A part of this investment could be in the education system. Most tertiary institutions offer supply chain courses and there are several supply chain training entities who offer courses – but these are all disparate and dispersed.

Target upskilling towards under-represented areas, in particular Māori Business leaders – These companies tend to be smaller and earlier stage, heavily regionally represented (esp. in Gisborne, Hawkes Bay, Waikato), and heavily Food & Beverage weighted (so facing more acute issues around time sensitive exports like fresh/frozen products). They are also more often capitally constrained or less likely to be able to manage supply chain related working capital issues.

Understand and map the interconnectedness of New Zealand's critical infrastructure and identify vulnerabilities in the supply chain ecosystem domestically and internationally. A more detailed understanding of this will help New Zealand to better plan for, and build resilience against, supply chain shocks.

Establish a coordinated Government approach: The Commission's Issues Paper, Part 4, outlines a portfolio of impacted government agencies and cross-sectional strategies. NZTE identified around 17 different government agencies and over 45 different strategies. This demonstrates the breadth and depth of the impact of this issue. Although there has been some good cross-agency collaboration, NZTE believes it would be beneficial to strengthen the co-ordination, alignment and prioritisation across these agencies and strategies. There may be some opportunity to use the Government's Industry Transformation Plan framework to address these issues in a coordinated way.

Question 4: What should the Commission study to learn more about the economic resilience of industries and communities?

Mapping of New Zealand's supply chain ecosystem: As noted above, NZTE believes there would be real benefit in mapping out New Zealand's supply chain ecosystem and its connections with the global supply chain ecosystem to better understand the points of vulnerability and potential Government intervention.

The trade-off between diversity and aggregation for building resilience: The Commission's Issues Paper talks at length about how diversity provides a natural hedge against disruption and therefore is an enabler of resilience. In contrast, however, diversity (or disaggregation) can also diminish scale and buying power, which are often underlaying principles in improving productivity and efficiency. Logistics hubs (like Ruakura Superhub in Hamilton or KiwiRail's planned Freight Hub in Bunnythorpe, Manawatu) are based on the principles of centralising disparate freight volume flows, aggregating them across common infrastructure and driving improved efficiencies for users, as well as lower carbon emissions. Being more efficient and cost effective, is one way of achieving economic and environmental resilience.

This illustrates that there is a natural tension between the benefits and vulnerabilities created by both diversification and aggregation. NZTE believes there would be benefits in studying this tension further and better understanding the circumstances in which each approach is better than the other.

Complete case studies of a sample companies across NZ: NZTE believes that some analysis done at the individual company level will deepen the understanding of the effects of, and vulnerability to, supply chain issues.

Study and collaborate with global peers: As outlined in the Commission's Issues Paper, other advanced economies are taking steps to improve their supply chain resilience. Keeping abreast of the progress and success of such initiatives is likely to help New Zealand to find ways to address its own vulnerabilities.

Tim Green, General Manager Strategy Performance and Partners

New Zealand Trade & Enterprise