Submission of the
New Zealand Council of Trade Unions
Te Kauae Kaimahi
to the

New Zealand Productivity Commission
on the

Issues Paper: International Freight Transport Services

P O Box 6645
Wellington

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1. **Introduction**

1.1. This submission is made on behalf of the 39 unions affiliated to the New Zealand Council of Trade Unions Te Kauae Kaimahi (CTU). With over 330,000 members, the CTU is the largest democratic organisation in New Zealand.

1.2. The CTU acknowledges Te Tiriti o Waitangi as the founding document of Aotearoa New Zealand and formally acknowledges this through Te Rūnanga o Ngā Kaimahi Māori o Aotearoa (Te Rūnanga) the Māori arm of Te Kauae Kaimahi (CTU) which represents approximately 60,000 Māori workers.

1.3. The NZCTU welcomes this opportunity to comment on the Issues Paper published by the Productivity Commission, and will be happy to provide further information and assistance to the Commission in relation to matters covered in this submission.

2. **General Orientation of the Issues Paper**

2.1. While we appreciate that the Issues Paper is only a first step in the Commission’s inquiry, there does appear to be a lack of balance in the emphasis placed on particular topics, in the references listed in the
bibliography (which appear to show a selective bias towards consultancy studies supportive of privatisation and offshoring), in a tendency to underplay the crucial strategic issues arising from the presence of dominant firms with the ability to exercise holdup (such as port concerns that a dominant shipping line will threaten to use another port, wasting their investment in specialised assets), and in the very limited discussion of the potential gains from centralised strategic planning as a means of coordinating the domestic components of the logistic chain¹.

2.2. It would be unfortunate if the Commission were to move towards recommending industry micro-reforms on the model adopted for industry reform in the 1980s and 1990s without taking full and careful account of the downsides of that approach, and of the reasons why it failed to result in a sustained improvement in productivity growth for the economy as a whole. In particular, we hope that in its inquiries, the Commission will take seriously its statutory purpose, “to provide advice to the Government on improving productivity in a way that is directed to supporting the overall well-being of New Zealanders, having regard to a wide range of communities of interest and population groups in New Zealand society” by implementing the full meaning of the word “well-being”, and genuinely taking into account the implications of any actions on the whole of New Zealand society.

2.3. As a consequence we suggest that it must consciously strive to avoid:

- Confusion of cost-cutting with productivity improvement

¹ “Regional or centralised planning” makes a one-line appearance on p.30 of the Issues Paper, with no further discussion and no question inviting comment. On p.8 where “efficiency at the interface” and “efficiency of the whole logistics chain” are discussed, there is not even a mention of the potential for centralised planning to improve outcomes – only vague optimism that “exchange of information and contractual linkages” among firms may improve outcomes. Similarly p.18, discussing “the right balance between coordination and competition”, reflects on the advantages and disadvantages of “a single transport operator [who] is in the best position to coordinate actions so as to optimise technical performance of the supply chain” but does not even mention in passing the ability of a centralised planning institution to accomplish this task without the anti-competitive consequences of monopoly. On page 54, Question 57 raises the possibility of an overall strategic plan but with little substantive discussion.
- Failure to distinguish clearly between changes that raise productivity and those that simply shift costs and profits amongst economic agents or sectors

- Failure to take proper account of externalities and spillovers, which the market mechanism is unable to manage efficiently and which are inherently difficult to measure with the available official statistics

- Failure to consider explicitly the welfare (well-being) implications of transfers of income and wealth within the New Zealand community, which are too often masked behind the incorrect claim that such transfers are welfare-neutral, or set aside on the basis that the issues are “too hard”

- Failure to confront directly the strategic consequences of market power, particularly where such power can be exercised by dominant suppliers to raise prices at essential-facility bottlenecks, and/or by dominant purchasers to exercise holdup and force a “race to the bottom” among competing suppliers

- Any tendency to assume the existence of perfect or workable competition in situations that are actually characterised by seriously imperfect competition, and where regulatory intervention is required to counteract opportunism and holdup by key players with market power or dominance

- Any preconceived view favouring private over public ownership as a matter of principle in settings where the interests of the New Zealand community at large arguably point to the superiority of the latter

- Mis-characterisation and value-laden characterisation (e.g. as “inflexible” in terms of the discussion on p.33 of the Issues Paper) of labour-market institutions that protect workers’ rights and job security, ensure proper training and workplace safety regimes, and develop and maintain a skilled labour force in key industries
Any tendency to discount in principle the value of central planning and coordination of key industries, and hence to miss genuine opportunities for collective action to improve on unregulated and uncoordinated market outcomes

3. Narrow scope of the inquiry

3.1. At the outset the Issues Paper poses two general questions (numbered Q1 and Q2), asking whether an “economic efficiency perspective”, and the framework developed under that perspective in section 3.2 of the Issues Paper, is appropriate for this inquiry. On p.3 of the Issues paper the inquiry’s scope is narrowed radically in two successive steps, first restricting the analysis to the so-called “efficiency” perspective, and secondly identifying “New Zealand importers and exporters” as the target group whose gains are to be prioritised, on the vague and poorly-articulated premise that gains for that target group “should” translate to lower prices for consumers and firms and “likely …. better wages and opportunities” for employees. Experience with previous rounds of micro-reform conducted under the “efficiency” approach indicates that neither set of outcomes necessarily follows, because the necessary conditions for gains to a particular sector or group to pass through to gains in general wellbeing have not been met by the policy design. It needs always to be borne in mind that the wellbeing of a particular sector or party can be advanced by wealth transfers and cost-shifting measures at the expense of others, with no overall productivity gain for the nation as a whole.

3.2. In the NZCTU’s view, the efficiency perspective as it has been applied in New Zealand since the 1980s is too narrow to satisfy the terms of reference for this specific inquiry, as well as inadequate to advance the Commission’s general mandate to promote “the best possible improvement in the wellbeing of all New Zealanders”.

3.3. The Terms of Reference for the inquiry (Issues Paper p.1 and pp.71-72) focus on “accessibility” as well as “efficiency”. Particular attention is to be paid (p.72) to issues of distance, reliance on overseas suppliers, and the effectiveness of regulatory regimes, in addition to costs, efficiency,
productivity and growth, and this list is stated to be “without limitation” on other matters that may be covered. The framework proposed in section 3.2 of the Issues Paper effectively sets aside most of that wide-ranging agenda by reducing the wide range of issues to the single metric of “economic efficiency”, narrowly defined. This inevitably gives the impression that the Commission may be contemplating a 1980s-style drive for narrowly sector-focused cost-cutting and privatisation with little or no attention paid to issues of income and wealth distribution, welfare impacts of transfers within the New Zealand community, workplace safety, development of a skilled and experienced national workforce, effective provision of public goods, national planning and coordination of essential services, or key concerns regarding the exercise and abuse of market power. This concern would be alleviated if the Commission were to adopt at the outset a more expansive conceptual framing for its inquiry.

3.4. Wellbeing is not reducible to the narrow concept of economic efficiency set out in section 3.2 of the Issues paper. In a long-run perspective, productivity growth is hindered, not helped, by policies that sacrifice social capital and political goodwill in pursuit of short-term gains, especially when those short-term gains benefit particular sections of the community at the expense of others.

3.5. Wellbeing is a multidimensional matter. It involves New Zealanders' sense of themselves and their place in the world – something that is directly affected by the extent to which overseas providers are allowed to dominate segments of the international freight transport chain, however notionally “efficient” such dominance might seem. It involves a socially just distribution of income and wealth across the community, something which is conventionally excluded from economic efficiency analysis because of the need for judgements to be made that lie outside the scope of economics *per se*. Previous rounds of micro-reform in New Zealand have resulted in large wealth and income transfers which have not received due attention because of the neoliberal doctrine that transfers are welfare-neutral, provided only that they occur within the national community. That doctrine is an arbitrary matter of
convenience, not an outcome of principled reasoning. An analysis that focuses on well-being and “effectiveness of regulation” cannot avoid the need for transfers to be explicitly considered so that policymakers can make appropriate political judgments.

3.6. Efficiency cannot be reduced to the costs of particular sectors or parties. The Issues Paper is focused on achieving gains from the perspective of “New Zealand importers and exporters” (p.3). Where such gains are achievable at no cost to other sectors and parties in the New Zealand economy, that sectoral perspective may well coincide with the general wellbeing of the community. Where gains in the form of lower costs for exporters and importers are achieved at the expense of other sectors or groups, the resulting welfare tradeoffs need to be taken into account. A narrowly-focused cost-cutting approach could result in exporters’ costs being driven down by, for example,

- Driving down wages and working conditions of workers employed in various stages of the logistics chain, with likely flow-on effects for workplace safety and the maintenance of a skilled workforce;

- Imposing spillover costs onto other sectors of the community via environmental and social externalities that are not charged to the exporters and importers. As several studies have found, externalities from road transport substantially exceed those from rail (especially as road rigs become larger and heavier), and both of those greatly exceed those from coastal shipping. A coordinated maritime transport strategy would require the sort of rebalancing exercise contemplated in the Sea Change document;

- Squeezing local-body revenues from their port and other operations, with flow-on effects to local services and rates;

- Reducing expenditures on training and licensing of specialised occupational groups, leading to reduced recruitment of New Zealand residents and an increasing need to source skills offshore.
3.7. “Accessibility” cannot be reduced to “efficiency”. “Accessibility” features in the terms of reference but the term then disappears from the Issues Paper until a brief, noncommittal paragraph on page 61. Accessibility is separable from efficiency as defined in Box 2 p.7 and encompasses a wide range of matters (going beyond these noted in Question 68 p.61), many of them with important regulatory implications\(^2\). Examples include

- The role of logistics “hubs” in facilitating or obstructing transfers of cargo amongst transport modes;
- Open or restricted access for third-party competing suppliers to key infrastructure assets such as oil unloading and storage facilities at major ports\(^3\);
- Dredging programmes and port facilities installation to increase the size and/or range of ships that can be handled at particular ports (often leading to excessive competition and stranded investments);
- Role of competing pilotage and stevedoring operations at the ports;
- Allocation of landing slots at international airports.

3.8. Effectiveness of regulatory design cannot be reduced to “efficiency”. Regulation properly encompasses a wide range of issues beyond the narrowly economistic conception of efficiency in the Issues Paper:

- Workplace safety, job security, driving hours, size of road transport rigs, and numerous others are properly regulatory matters, which should not be encroached upon in the name of cost-cutting “efficiency”.

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• As noted below, biosecurity at ports and airports is a matter of meeting absolute standards of performance, not a matter of cost/effectiveness tradeoffs. It may be legitimate to seek to achieve the same or better biosecurity outcomes at reduced cost, but a deliberate tradeoff of effectiveness against cost would render the New Zealand economy hostage to exporters’ and importers’ short-run bottom lines.

• Equally, the exercise of market power by owners of essential facilities to extract undue profits and prop up otherwise-unsustainable asset valuations draws attention to the very weak disciplines imposed on use of market power under the Commerce Act 1986. The history of regulatory inquiries into major airports and of legal cases involving port companies points to a need for the Commission’s inquiry to extend beyond simply rolling other regulatory procedures into the existing Commerce Act (as foreshadowed on page 19 of the Issues Paper), and to consider a substantial refashioning of the regulatory access regime for essential facilities in the Commerce Act 1986 as it currently stands.

3.9. Considering the range of issues that are apt to be omitted or downplayed under the “efficiency” approach, it would have been helpful if questions 1 and 2, and the accompanying discussion, had provided clearer acknowledgment of the existence and legitimacy of alternative ways in which the inquiry could have framed its analysis, rather than setting up a take-it-or-leave-it presentation of its “efficiency” paradigm. The Commission will have to do

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5 See for example Pacifica Shipping v Centreport [2003] 1 NZLR 433.

better than this if it is to retain credibility with, and broad support from, the
community and the relevant industry stakeholders, especially given its stated
goal of privileging the interests of exporters and importers relative to other
sectors. Insofar as that goal is expected to improve the general well-being of
New Zealanders, as distinct from advancing the interests of particular sector
groups and political groupings, the Commission will need to articulate clearly
the basis on which any such expectation rests.

3.10. Obviously, given its limited resources and tight time constraints, the
Commission will be obliged to prioritise its work, as p10 of the Issues Paper
notes. In response to Question 3 on that page, the view of the NZCTU is that
areas of research which ought to be given explicitly high priority include

- careful empirical analysis of outcomes from the previous round of
  industry reform in the sector, with time-series data assembled on the
cost of insurance and freight through the CIF-VFD differential,
comparison of the role of the sector in the economy’s input-output
matrix before and after the previous reforms, and the basis on which
Statistics New Zealand’s measurements of sector-specific productivity
growth are calculated, to determine the extent to which surpluses
created by restructuring were actually passed to the target
exporter/importer group as distinct from being captured within the
logistic chain

- thorough review of the options for centralised planning and
  coordination across various transport modes and logistic interfaces,
and consideration of how to develop and implement the institutional
arrangements for such strategic planning

- a thorough consideration of the wider impacts on wellbeing, including
distribution of benefits within New Zealand, and regional and
environmental impacts.
4. **Cost of the logistic chain**

4.1. If a central aim of the inquiry is to be to reduce “inefficiently high trade costs” (Issues Paper p. 4) for the benefit of exporters and importers, there is a need for proper empirical investigation of how trade costs have in fact evolved in New Zealand over the past few decades, and rigorous analysis of the origins of any identifiable trend breaks. The Issues Paper on p.29 notes, for example, that “it has been suggested to the Commission that … there were substantial gains following the port reform programme of the 1980s and 1990s” but makes clear that to date the Commission lacks data to test this proposition. If those suggested gains in ports (and others elsewhere in the logistic chain at the same time) took the form of reduced costs to exporters and importers, those cost reductions ought to be manifest in the relevant price indices, in the economy-wide input-output tables, and in the CIF-VFD margin over time. The last of these has been estimated for imports (Issues Paper p.19 footnote 9) and that calculation should be carried back to the 1970s. It is not obvious that the data are insufficient to conduct a similar exercise for exports (as footnote 10 asserts).

4.2. Similarly, the decomposition of logistics costs as at 2008 in Table 2 is informative, but needs to be given historical context by conducting similar exercises for the mid-1990s and mid-1980s to detect any changes resulting from the previous industry reform process.

4.3. This highlights a gap in the terms of reference and the study framework: the lack of an explicit instruction or commitment to review the historical evidence of outcomes from previous industry-level restructuring⁷. In response to Question 2 p.9 of the Issues paper, the NZCTU encourages the Commission to undertake such a review on a rigorous, empirical basis, to test against the evidence the various claims often made about the scale and nature of net gains from the reforms of the 1980s and 1990s. While cross-country contemporary comparisons of port performance along the lines of Figures 13-15 (pages 26-28), and Table 11 (page 57) of the Issues Paper are clearly

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⁷ This is not to say that the issue is excluded from the Terms of Reference; simply that it falls under the “without limitation” provision - see 72 of the Issues Paper.
useful (provided that any analysis has controlled carefully for factors such as the small size of New Zealand ports relative to huge global terminals, country size, distance, commodity composition of cargos, imbalance of inwards and outward container traffic, and average size of ships), they are not a substitute for a careful review of country-specific historical experience. The decomposition of logistics costs in Table 2 of the Issues Paper provides a template that could be utilised for such a review; if similar cost decompositions were to be conducted for the mid 1980s and mid 1990s, and compared with the current picture given in Table 2, the outcomes of the post-1984 restructuring in terms of impact on the costs faced by importers and exporters would be placed into clearer focus.

4.4. It is true that tradable goods producers have faced a price-cost squeeze over recent decades in New Zealand, but the predominant source of that squeeze has come from monetary policy and the high level of the New Zealand dollar exchange rate, rather than from the freight transport logistics chain. Micro-level policy interventions to attempt to offset the consequences of macro policy settings are notoriously fraught with difficulty. An important piece of research that the Commission could contribute would be to track the long run trends in the share of international freight transport as a deduction from New Zealand’s export receipts overseas, and as an add-on to the overseas price of imports, over the past several decades. In particular this would illuminate the outcomes from the previous round of micro-reform at ports, airports, the railways and the road transport industry, from the standpoint of exporters and importers. The 1989-1999 rise in productivity calculated by Statistics New Zealand for the Transport and Storage industry (see below, paragraph 6.4) will have created some surpluses, but it is not clear which parties were able to appropriate those surpluses; certainly workers were losers, not gainers, in the process. Insofar as productivity gains from previous micro-reforms in Transport and Storage were captured by firms within the sector rather than passed through to exporters and importers, the result would have been to strengthen anti-tradables bias in the New Zealand economy as a whole.
5. **Ownership and control of New Zealand infrastructure**

5.1. The Issues Paper at several points hints at further privatisation of key parts of the freight transport chain that have remained in, or been returned to, community/public ownership since the “micro-reform” drive of the 1980s and 1990s. Of particular concern are the sections on port ownership (pp.30-32 and Questions 15-16 of the Issues Paper) and airport ownership (p.39 and Questions 28-29) both of which find fault with the LGA classification of council-owned ports as “strategic assets” and with the requirement for local authorities to balance multiple objectives rather than focus single-mindedly on “operating as a successful business”. The Issues Paper perceives (p32) “a risk” of an incompatibility between public ownership and “the long-term efficient operation of ports”. The NZCTU strongly submits that there is no necessary incompatibility and that the particular issues identified on pp.32 and 39 would not be resolved by privatisation.

5.2. It is vital in addressing the issue of ownership or ports, airports, and railways, that the Commission carefully reviews all alternatives to the status quo – not just privatisation. Before recommending any change to the status quo there must be

- A proper review of the outcomes from the previous round of corporatisation and privatisation, including the catastrophic record of ideologically-driven rail privatisation and subsequent renationalisation at huge cost to the nation and the taxpayer

- Careful review of the empirical record to ensure that the Commission does not make the error of sliding into easy sloganistic recommendations to “change ownership” when the problems to be addressed are not related to ownership. This applies especially to “slower productivity growth” in recent years, especially in the ports sector, which in the view of the NZCTU is attributable not to public/community ownership but to perverse incentives under deregulation leading to excess competition, over-investment, asset stranding (such as a dominant shipper abandoning a port, leaving it
with unusable, costly specialised equipment), and consequent falling returns on capital. The malignant effects of those perverse incentives has been compounded by the uncontrolled ability of large shipping operators (particularly Maersk) and major exporter companies (particularly Fonterra) to subject port companies to “hold-up” as a result of their dominant position in key markets, resulting in a competitive “race to the bottom” amongst ports combined with a “race to the bottom” in labour practices within individual ports.

- Full consideration of the ownership implications of the need for effective planning, coordination and regulation at national level to optimise the structure and performance of the domestic components of the logistics chain (the sectors to the left of the border in Figure 2 in the Issues Paper). Planning and coordination in the national interest points to the strong advantages of public or community ownership of essential facilities such as ports and airports, as well as of infrastructure assets with major public-good characteristics and large spillover effects, such as railways and roading.

- Engagement with the overseas literature on the consequences of privatisation of ports and other infrastructure.\(^8\)

5.3. If ports were to be privatised with no barrier to overseas ownership, the likely outcome would be takeover of key ports by one, or possibly a couple, of the large transnational operators such as Dubai and Hutchison, whose record elsewhere in the world indicates that gains from rationalisation across ports and within ports will tend to be captured offshore rather than passed to domestic exporters and importers, once dominant positions have been established. Port privatisation with the assets passing into overseas hands would deprive New Zealand of control over key strategic assets that are crucial to long-run trading success and potentially to national security.

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5.4. It is noticeable that the extensive discussion of port ownership on page 32 engages in extensive hypothetical speculation about the possible outcomes from local authority versus private ownership on the basis of abstract, and highly contested, propositions drawn from the economic literature on industrial organisation (though without relevant citations to that literature). Completeness would require more systematic coverage of the hypothetical outcomes from private ownership under conditions of imperfect competition and market failure.

6. **Failure of wages to track productivity**

6.1. On page 29 of the Issues Paper, Questions 9 and 10, the Commission invites comment on productivity performance in the ports sector. At the outset it is important to note that a distinction has to be drawn between “higher productivity across the economy generally” (Issues Paper p.22) and sectoral productivity performance as measured by Statistics New Zealand.

6.2. A key feature of New Zealand experience since the micro-reforms initiated in the 1980s has been the failure of productivity gains (as measured by Statistics New Zealand) to be passed through to wages. This is directly attributable to asymmetry of market power in the labour market, with employers in strongly oligopsonistic positions taking advantage of extremely weak bargaining and organising rights for the labour force, the consequent weakness of labour organisations, and the fragmentation and casualisation of the labour force, to drive down wages.

6.3. Statistics New Zealand collects data for the Transport and Storage sector of the economy. Detailed productivity and wage data are not released for lower levels of industry disaggregation, but may be available to the Commission on a confidential basis, and if so ought to be accessed and analysed.

- Labour productivity in the Transport and Storage sector is available as a SNZ series;
- Figures are available from 1989 for total hourly average wage from the Quarterly Employment Survey;
• “Compensation of employees” in the Transport and Storage sector is available from the national accounts;

• Labour Volume for the Transport and Storage sector is available as an index published by SNZ as part of its productivity series\(^9\); dividing compensation of employees by this index gives a series for labour income per labour volume unit;

• Various deflators are available to bring these nominal wage measures into real terms: the two most relevant are the economy-wide CPI, and the Producer Price Index (Outputs) (PPI-O) for the Transport and Storage sector. The latter is available at sectoral level only from 1994Q2; but the PPI-O for all industries closely tracks the Transport and Storage sector PPI-O over the period 1994Q2-2010Q2, and is probably a good proxy for earlier periods;

• Real labour unit costs are available as a new experimental SNZ series;

• Labour share in value added is in the National Accounts and published by SNZ as part of its productivity series.

6.4. Using these series results in the following chart. The failure of productivity gains to be passed to wage-earners since 1989 is immediately apparent. It is equally apparent that up to 1989 there was a tendency for real wages to track productivity. The dating of the de-linkage of productivity from wages coincides conspicuously with the micro-reforms of the late 1980s and 1990s and the passage of the Employment Contracts Act 1990, which effectively stripped workers of their ability to bargain effectively in a labour market characterised by strong market power on the employer side. In the absence of such pass-through, there would appear to be little basis on which workers can see themselves as stakeholders in future attempts to revive productivity growth.

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6.5. The trend of labour productivity in the chart seems consistent with a history of a one-off shift in the distribution of value added between 1989 and 1997, from wages to profits (see chart below), as the labour force in Transport and Storage was slashed, de-skilled, and de-unionised. Between 1989 and 1996 the labour share was driven down from 70% to 60% and the capital share up from 30% to 40%.

6.6. The significance of this is that a one-off structural shift is not to be confused with an upward break in trend. The long-run trend in labour productivity since 2000 looks close to the trend in the period 1978-1988. The intervening period of upheaval and restructuring is likely to represent only a transition, achieved at substantial costs in terms of spillovers, deferred maintenance in key infrastructure such as the railways and roading network, and downgrading of worker rights and conditions,

6.7. It is not clear how much of the reported rise in productivity over the period 1989-1997 was genuine and how much reflected short-run gains to sectoral operating surplus (the key rising component of value added in the sector) at the expense of other sectors, given the pervasive spillover externalities.
associated with transport logistics and the widespread tendency in the 1990s to defer infrastructure maintenance and development with the costs to be borne by a later cohort of New Zealanders.

6.8. The growth accounting exercise conducted by Statistics New Zealand for Transport and Storage 1978-2009\textsuperscript{10} identifies clearly the dramatic shakeout of labour from the sector between 1989 and 1994, concentrated heavily in 1989-1990, coinciding with the period of elevated multifactor productivity growth as measured by the Statistics NZ methodology. (See the chart below.) Since the further labour-force shakeout in the recession of 1998 there is no sign of significant further ability to shed labour. Any suggestion that major productivity gains could result from a renewed assault on employment, wages and conditions under cover of slogans about “labour market flexibility” (Issues Paper p.33, Question 18) would clearly be unsustainable in the absence of compelling evidence. We trust that the Commission will refrain from going down that path.

6.9. As noted earlier, the crucial empirical question in evaluating the outcomes of the previous round of micro-reforms is the extent to which reduced operating costs and increased productivity were passed back to exporters and importers within the New Zealand economy. This requires empirical tracking of components of the producer price index, and comparison of input-output tables for years before and after the reforms.

7. Productivity and labour force development

7.1. Concepts such as “economic efficiency” and “competition” are often used far too casually to justify short term policies and lack of strategic planning in the New Zealand maritime and transport industries. From a long term perspective, productivity growth requires the development and maintenance of a skilled, secure workforce. Permanent jobs, training, and a high level of health and safety on the job, are all important parts of a productive maritime industry. Currently there is an ageing workforce due to lack of a national training plan and lack of interest from employers. Many young workers are employed on a casual basis, which does not encourage a commitment to the industry. Casualisation undermines a stable workforce and destroys career...
paths for young people, which in the long run inhibits the building up of human capital in the industry and hence places a drag on productivity growth. A central area of concern with regard to the long-term productivity consequences of casualisation is stevedoring at the ports. The NZCTU will be happy to provide the Productivity Commission with evidence of the negative consequences of casualisation of the labour force, and urges the Commission to undertake its own study of the record on workplace safety and the injury rate since so-called “flexible working practices” have been imposed at ports. Department of Labour data on injuries and accidents should be accessed by the Commission as part of its inquiry.

7.2. The present pattern of a small permanent workforce at each port supplemented by a much larger pool of footloose casual workers is not well adapted to ongoing productivity growth, although as noted earlier it is apparent that the transition in the 1990s from the previous waterside labour force to the new regime made possible a once-for-all reduction in labour costs for employers. It is less clear whether eliminating watersiders as a workforce and replacing them with casual labour had a positive or negative effect on productivity as distinct from costs. Looking ahead, the need to improve workplace safety and job training, and the advantages of building up an experienced permanent workforce at each port who are familiar with the particular conditions prevailing there, point to future productivity gains coming from a more sophisticated approach to labour force development.

7.3. We are aware of privatised ports overseas which have brought in low paid, low-skilled labour from other countries. This would further undermine any long term approach to skill and workforce development and would be strongly opposed.

7.4. The confidence expressed in the Issues Paper that (p.3) “higher returns for exporters are … likely to benefit employees through better wages and opportunities” looks more like a casual remark than a well-grounded prediction. It should nevertheless provide a key benchmark against which all proposals emerging from the Commission’s inquiry ought to be judged.
8. **Excess competition amongst ports**

8.1. On page 25 the Issues Paper raises in Question 5 the issue of “effective competition for customers between ports”. In raising the issue in this context the Commission risks losing sight of the wider competition environment within which New Zealand ports operate. There is extensive evidence (mentioned on pages 54-55 of the Issues Paper) of ports being “held up” by international shipping lines and dominant domestic trading operations such as Fonterra and Solid Energy, to undertake large investments in port works and facilities which have subsequently been stranded, at substantial cost to the national economy. The evidence goes well beyond the status of a “suggested risk” (Issues Paper p.29) and is not rebutted by the NZIER finding that capacity has grown more slowly than trade volume (p.29 again).

8.2. In this as in other areas of economic analysis the early sections of the Issues Paper tend to stray into unwarranted assumptions about market efficiency and to downplay the ability of dominant players in one segment of the chain to exercise holdup and opportunism at the expense of players elsewhere in the chain. On p.17, for example, the Issues Paper notes the phenomenon of “small numbers competition” but discusses only its implications for pricing behaviour within the market or sub-market where the small numbers prevail, thereby overlooking the practices by which market power in one market can be leveraged into advantages in other related markets.

8.3. On page 10 the Issues Paper argues that if analysis of a particular component of the logistic chain “indicates a healthy state of competition, then there are already likely to be efficient outcomes in that segment”. This is an entirely unwarranted conclusion to draw in the context of holdup and opportunism originating outside the sector concerned. The issues of commitment problems and holdup are usefully canvassed on pages 51-52, and pages 54-55 of the Issues Paper, and need to be borne in mind when making claims of the sort referred to on page 10.

8.4. Competition among New Zealand ports to secure premier status with shippers has been intense and highly wasteful. To characterise the outcomes
as “efficient” simply because the port segment itself is highly competitive involves a straightforward non sequitur. Here as elsewhere in the Issues Paper, the logical case for a national planned strategy on ports and transport modes is sidelined by defective a priori economic theorising.

9. **Need to revitalise coastal shipping**

9.1. Coastal shipping in New Zealand operates under a number of severe handicaps that limit its ability to play its potential role in raising productivity in the freight transport chain. Coastal shipping is a growing part of the logistics mix and provides a low impact, low overhead and environmentally sound transport mode.

9.2. A recurrent issue in the regulation of shipping services on the New Zealand coast is the legal definition of “coastal cargo”, which must be carried on New Zealand-domiciled vessels except to the extent that international shipping lines calling at New Zealand ports to deliver and collect international freight are able to provide inter-port freight service as a by-product. There is substantial evidence of this provision having been “gamed” by international shipping operators through strategic rearrangement of their schedules of port calls, to the detriment of the national coastal shipping industry. The prospect of litigation by an international shipping line seeking to legitimise its breach of the conditions in section 198 of the Maritime Transport Act (1994) was an important motivating force behind the Sea Change strategy in 2008. The section permits the carriage of coastal cargo by foreign ships only as part of an ‘international voyage’. But poor drafting of the section means that its original intent (ie that the coastal cargo could only be “incidental” to the international cargo, and the vessel must head in one direction and not double back) is not reflected. This lack of adequate boundaries is being exploited by foreign vessels to the detriment of New Zealand shipping companies and seafarers. Though not the full cabotage desired by the unions, clarification of the intent behind section 198 is still required.

9.3. Section 198 of the Maritime Transport Act (1994), which has opened the way to increased dependence on foreign flag-of-convenience vessels at the
expense of the local shipping industry, has as its downside a number of threats to biosecurity, frequency and regularity of shipping schedules, industry standards, and New Zealand’s security of transportation service at times of crisis. The strategic importance of New Zealand’s coastal shipping operators was apparent, for example, in the aftermath of the Christchurch earthquake when vital supplies had to be delivered at short notice.

9.4. In response to Question 25, p.37 of the Issues Paper, therefore, the NZCTU points the Commission towards S.198 of the Maritime Transport Act as an important area where enforcement of the law has been inadequate to date, and where international experience – including the pros and cons of a move back towards cabotage as practiced in many seafaring nations around the world - is relevant.

9.5. A maritime nation needs a skilled maritime workforce and viable industry. In recent years there has been a steep decline in the resources devoted to workforce training. International competition has progressively driven the New Zealand coastal and international fleet down to a tiny coastal shipping industry. The New Zealand workforce engaged in domestic sea freight, and from which the wider maritime infrastructure workforce is drawn, is ageing – one third are over 60 years old. Recruitment is difficult because of the unique conditions that relate to seafaring. Financial support for students does not address practical sea-based training. There is also strong international competition for qualified personnel. Training opportunities are now ad hoc, with ship owners reluctant to carry the cost of training amongst such a small number of them. Workforce development was a key element of the Sea Change initiative in recognition that a revitalised domestic sea freight industry will need more skilled people. 11

9.6. There is a great deal of useful information to be gleaned from the past history of work towards a fully developed maritime transport strategy. The bibliography of the Issues Paper references the 2009 Rockpoint study for NZTA but omits the 2000 report of the Shipping Industry Review12, the 2005

9.7. Central to the Sea Change strategy was the planning and coordination of investment in interfaces between different transport nodes.

10. Effective regulation and nationally coordinated planning

10.1. A central structural feature of the surface transport freight chain is the dominant position of a major overseas shipping line, Maersk, which is able to leverage its market power to hold up port owners and other participants in the domestic segment of the chain. Because Maersk is an offshore entity, the only way to countervail its holdup power is to present a coordinated national strategic front that specifies the ports to be utilised and forestalls excess competition amongst individual ports responding to Maersk demands for investment that are not backed by binding long-term commitments and hence are open to post-investment opportunism, which leaves stranded assets and wasted investment.

10.2. The issue of market power exercised by major overseas shipping lines is a longstanding one in New Zealand and predates the entry of Maersk and its rise to dominance. Extensive previous research and policy development work has been done over the decades, including experiments with a national shipping line to enter the market to compete directly, and attempts to break collusive behaviour by other means. While the issue is not an easy one, it is

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clear that policies which increase competitiveness in the domestic segment of the transport chain while failing to countervail the holdup power of international shipping lines expose the national economy to heavy costs. A task of the inquiry should be, in the context of our proposals in 3.10, to review the previous experience of a national shipping line and consider the design of one that would effectively contest the dominance of the major overseas lines.

10.3. Similar comments are relevant to the issue of collusion among airfreight carriers, discussed on p.45 of the Issues Paper. In response to Question 44, there seem to be clearly overlapping issues between the regulatory position on sea and air freight services, which suggests a common or harmonised regulatory framework, as part of a coordinated national transport strategy, would make sense.

10.4. The opportunity clearly exists for the New Zealand Government to coordinate a planned approach to port development and the location of logistic interface hubs at ports and inland. The success of such a planned strategy, however, depends on the ability and willingness of the New Zealand authorities to hold international shipping lines captive to the resulting plan, in order to forestall opportunist conduct which would continue the recent problem of stranded assets and maintain excess competition among ports. Such a regime would have a family resemblance to the restrictions on airfreight carriers’ access to landing slots, mentioned on p.43 of the Issues Paper.

10.5. The success of a strategic plan would also depend on the ability and willingness of Government to secure compliance by domestic investors in infrastructure assets. Left to itself, the market mechanism will waste resources – for example, in the pending installation of multiple competing inland transport hubs along the line of the Main Trunk railway south of Auckland, which is an example of “competition for the market” by players committing actual real resources to an economically inefficient number of ventures, most of which will later exit the industry leaving behind financial losses and problems of site rehabilitation.
11. **Need for national planning and coordination**

11.1. A recurrent theme in the freight logistics chain since the late 1980s has been the lack of coordination across transport nodes and ports at national level. Uncoordinated investment under conditions of excessive competition among operators in certain segments of the chain, while players in other segments were able to exploit dominant positions in their markets to hold-up the competitive segments, has resulted in much wasteful expenditure that has placed a deadweight burden on the national economy. Competitive programmes of dredging, crane installation, and other investments by port companies have left an inevitable legacy of underperforming assets, given that only a very few ports could emerge as winners from the process. The primary beneficiaries of this overcommitment of scarce New Zealand investment resources have been overseas shipping lines, in particular Maersk. Other major beneficiaries have included Fonterra which, due to its monopsony power in the markets for transport and port facilities, has been able to load onto other sectors the costs of providing a socially unproductive range of choice, primarily serving to underpin its ability to exercise holdup;

11.2. The CTU is pleased to see the issue of coordination and planning across ports and transport modes raised by the Issues Paper (page 30, page 54 and pages 62-63). The issue of uncoordinated and wasteful investment is not, we submit, reducible to the issue of port ownership, as page 30 of the Issues Paper seems to imply; nor would merely contractual arrangements between ports be an effective means to counter the hold-up power held by large overseas-owned shipping lines. Forcing the privatisation and possibly merger of port companies would be no more than a recipe for passing these strategic assets into overseas hands as the large transnational port operators such as Hutchison and Dubai moved in to take control, thereby removing New Zealand control over its strategic trade gateways and subordinating regional and national development priorities to the private strategies of profit-driven outside interests.
11.3. The record overseas of those large transnational port operators has to be borne in mind in evaluating the consequences of port privatisation. We are compiling further information on these experiences.

11.4. In response to Question 57, therefore, the NZCTU strongly supports the notion of an overall strategic plan, and stands ready to participate in formulation of such a plan. In response to Question 58, the NZCTU believes that a planning approach is superior to the alternative of vertical integration and cross-port consolidation unless this is done under public ownership with New Zealand control assured.

11.5. The lack of coordination and planning is entirely unrelated to ownership and would not be remedied in any manner by further privatisation. What is lacking is a national planned strategy for long-run development of the logistics chain, seen as a whole. Such a strategy would serve to countervail the ability of Maersk and similar outside parties to dictate outcomes to the New Zealand community simply on the basis of their market power. An appropriate model would be a national authority with a mandate to maintain oversight over investment and access arrangements in rail, road, coastal shipping, ports and airports, to formulate a national strategy for locating logistical hubs, and to regulate where appropriate to secure coordination across transport modes and locations. The NZCTU would be strongly supportive of the establishment of such a national authority and would anticipate participating directly, as a major stakeholder, in its deliberations and activities. A quadripartite arrangement that brought together tradable goods producers, government, employers and unions would in our view be the most productive way forward.

11.6. The NZCTU strongly supports a move to centralised planning mechanisms to develop and implement a national transport strategy, with a representative structure encompassing employers, unions, exporters/importers, domestic transport stakeholders and government. This is our central response to Question 51, page 49 of the Issues Paper, and to Question 31, page 40.

11.7. On page 53 the Issues Paper raises the question of whether vertical integration might provide a solution to port coordination problems, but again
fails to canvass the relevance of coordinated national mechanisms as a means to secure the advantages without surrendering ownership control to a monopolist, which would be likely to end up in overseas ownership. The prospect of overseas firms acquiring dominant positions in even more of the logistics chain, with strategies in conflict with New Zealand’s national interests, are the primary disadvantages of vertical integration under private ownership – the issue raised in Question 55, page 53.

12. **Biosecurity and customs**

12.1. There seems to be some confusion in the Issues Paper between natural monopoly, as understood in economic theory, and statutory arrangements to promote the public good. Biosecurity arrangements at the border do not fit the economic concept of “natural monopoly”, as the Issues paper suggests in Figure 2 and on p.7. Those arrangements supply vital public (non-rival, non-exclusive) goods that underpin the wellbeing of New Zealanders. The benefits are inherently impossible to measure accurately in conventional monetary terms, both because those benefits are diffuse, and because most of them consist of preventing the occurrence of biosecurity breaches, the economic consequences of which could be catastrophic. It is extremely unwise to venture into attempts to calculate a trade-off between cost and effectiveness of services of this kind, as the Issues Paper proposes to do at the bottom of p.45. We strongly urge against any recommendation that contemplates, on cost-cutting grounds, a “loss in the effectiveness of [these] services” given that their “purpose is to safeguard the security and integrity of New Zealand’s inward and outward trade flows” (Issues Paper p.45).

12.2. Similar comments apply to customs services, which perform an important role providing a public good. Pursuing cost reductions at the expense of the effectiveness of New Zealand’s border controls ought not to be up for consideration as a potential tradeoff.

12.3. The Issues Paper remarks (p.19) on “the large number of individual charges imposed by New Zealand customs and biosecurity”. This does not seem to be a criticism of the level of the charges (which is presumably the issue from
the exporters/importers point of view) but simply of their relatively high degree of transparency and user-pays targeting. Unless some link is perceived between that transparency and the overall level of charges, the issue does not seem worth pursuing.

13. **Environmental issues**

13.1. The Issues Paper is very light on environmental issues. They are discussed in a brief section on p.18 under the heading “environmental costs”, and canvassed in Question 4. The section makes the correct point that properly-designed environmental policy is fully compatible with a “quest for improved productivity”, but its substantive discussion is confined to an uncritical reference to the Emissions Trading Scheme. Quite apart from the fact that the ETS in its current form is subject to widespread criticism on grounds of ineffectiveness and inefficiency, the range of environmental measures that fall within the scope of the inquiry is far wider than this. In addition, many of the costs of international freight are, or can be, purchased overseas in jurisdictions where environmental costs are even less integrated into pricing than New Zealand and will not pay the costs of negative externalities occurring in this country.

13.2. The Issues Paper acknowledges in principle the importance of including externalities and spillover effects in any calculation of “efficient costs”\(^\text{16}\), but has not consistently carried this principle over into its detailed work plan. Page 18 notes the importance of including environmental externalities in any calculation of efficient costs. Box 2 on p.7 notes the allocative-efficiency requirement for “buyers to face prices that reflect the social marginal cost of production” (emphasis added). But in the detailed review of individual components of the chain (Issues paper section 4) there are no subsections and no questions relating to environmental externalities surrounding ports, airports, international sea and air freight, and only token mention of externalities in relation to road, rail and coastal shipping on pp.48-49.

\(^{16}\) Page 12 notes the spillover effects of “logistics decisions made by the largest firms”. Page 17, Table 1 identifies externalities among the “economic characteristics of transport networks”. 
14. Conclusion

14.1. This Inquiry covers a crucial aspect of New Zealand’s economy. Shipping and air freight are particularly important to an island nation, and have a pervasive effect on our wellbeing. It is therefore all the more important that the Inquiry is much broader than simply economic efficiency applied to a narrow sector and takes into full account the Commission’s statutory responsibility to consider the wellbeing of New Zealanders in all its dimensions.