

Cadbury Schweppes Pty Ltd  
(Confectionery Division)

Submission  
To the  
Tasmanian Freight Equalisation Scheme  
Review Authority

June 2006

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## **Summary**

Cadbury Schweppes' costs in transporting product between its Hobart operation and its National Distribution Centre in Melbourne are around double that of comparable transportation distances on mainland Australia.

As well as transportation costs, Cadbury's Tasmanian operation is disadvantaged through product damage as a result of increased handling and increased product transit time necessitating higher inventories to maintain customer service levels.

Any decision to reduce the level of "Freight Equalisation" assistance would impact adversely on Cadbury's product development, capital investment and potential employment in Tasmania.

Cadbury produces a specific range of products at its Hobart plant and any decision which effectively increased freight cost would inhibit further new product development. The company has invested over \$35 million in new capital development over the last 4 years, so any significant reduction to the scheme will adversely impact this and other previous investments. In fact, without the TFES at its current level, it is unlikely the company would have invested in any new capital development in Tasmania, and the \$35 million would have been invested in Victoria and/or New Zealand.

The company provides direct employment for up to 800 Tasmanians and indirectly supports a further 2,000 jobs. Any reduction in assistance through the TFES would inevitably lead to a reduction in this level of employment and jeopardise any new employment opportunities.

## **Introduction**

This submission has been prepared by Cadbury Schweppes Pty Ltd (Confectionery Division) in response to an announcement by the Treasurer in March 2006 that a review of the Tasmanian Freight Equalisation Scheme (TFES) was to be undertaken.

The submission deals specifically with the cost of transporting Cadbury Confectionery Division products from Hobart to Melbourne compared with similar length journeys by road on the mainland.

## **Review of the TFES**

This review should attempt to quantify accurately the penalty incurred by shippers in Tasmania to transport their goods to 'the market' compared with companies operating on mainland Australia. The detail in this submission clearly demonstrates the actual penalty incurred by Cadbury in operating in Tasmania. Further, this penalty is compared with the current rate of assistance actually paid to Cadbury by the TFES Authority and the likely impact of any negative change to the scheme.

Should the levels of assistance be reduced, the effect to Cadbury would be to add a significant cost to the company's annual transportation costs.

The original (and clearly stated) Commonwealth Government objective in establishing the TFES, was to remove the disadvantage suffered by Tasmania and its people by reason of its lack of access to road or rail transport services to mainland Australia. In Cadbury's case it can quite clearly be demonstrated that

the current level of assistance does not fully compensate for this disadvantage. Therefore, it makes little sense to reduce the level of assistance. Any action which further reduces the level of assistance provided under the TFES would have the effect of marginalising the company's Tasmanian operations.

## **Description of Cadbury Operations**

Cadbury products produced in Hobart, Tasmania include a range of moulded block chocolate, boxed assortments, food drinks, some confectionery bars and some children's lines. The Tasmanian operation also produces the Confectionery Division's majority requirement for the partly finished chocolate product, 'crumb' – a key component used in the manufacture of Cadbury Dairy Milk Chocolate. It must be pointed out that most of the products made in Tasmania are currently not duplicated in either of the company's Melbourne factories and that 96% of all production is exported from Tasmania to the mainland for Australian or export consumption.

Finished product is moved from the Hobart factory to the Cadbury National Distribution Centre located in Melbourne. Orders are assembled for Cadbury customers throughout Australia in the National Distribution Centre and then forwarded to destinations by road or rail.

Shipments from Hobart, Tasmania are moved mainly through that state's northern ports, using all three of the main shipping companies. All finished goods are palletised and shipped in enclosed 6.1m refrigerated containers and also in 8.8m refrigerated Tasealinertrailers. Crumb (milk solids, sugar and cocoa mass chocolate pre-cursor) is bulk loaded into specially constructed 6.1m containers for transport to Melbourne. Under current arrangements, when emptied these containers are reloaded with bulk sugar for return transport to Hobart.

Table 1 below details the annual volumes being moved in and out of Tasmania by Cadbury.

Table 1 (information current as of 16 June 2006)

### **Annual North and Southbound Tonnage & Container Movements**


N.B. Confidential data removed.

Note:

- Under current arrangements, the freight cost for most sugar, raw materials and packaging is included in FIS price.
- The Crumb containers have been specially designed to facilitate reuse by back loading with sugar to Hobart. Under current arrangements these containers are back filled with sugar for shipment from Melbourne to Hobart.

### **Comparison of Freight Costs – Hobart to Melbourne vs Melbourne to Adelaide**

An examination of the relative transportation costs between Hobart and Melbourne and Melbourne and Adelaide (similar distances) provides a fair and reasonable cost comparison and a clear demonstration of the disadvantage suffered by Cadbury's Tasmanian operation.

Toll Tasmania holds the current contract to transport Cadbury's finished product from Hobart to Melbourne (distance 620 km). Under current arrangements, charges are made on a door-to-door basis and averaged over summer and winter. (Note: Confectionery must comply with temperature requirements during transportation and storage).

Cadbury uses the company Collins Transport for transport from Melbourne to Adelaide by road (distance 725 km), employing temperature controlled 14m pantechicons. For comparison purposes, the transport distance is 105km more to Adelaide and the current costs for transportation using 14m pantechicons are shown in the accompanying table.

Table 2 following compares the current charges applying.

Table 2 (information current as of 16 June 2006)

#### Comparison of Freight Costs – Hobart to Melbourne vs Melbourne to Adelaide


N.B. Confidential data removed.

Note:

- All costs (except the cost of loading and unloading) are included in the above figures.

Cost components included in the Hobart to Melbourne freight figures are:

- Road freight from door to wharf
- Road freight from wharf to door
- Sea freight across Bass Strait or from Hobart to Melbourne
- Container and trailer handling charges by the freight forwarder or shipping company
- Power and monitoring costs of reefer equipment during the summer season
- Container or trailer hire costs as appropriate
- Repairs to equipment (usually higher for sea freight than road freight)
- Freight insurance
- Security door seals

Many of the above cost components do not apply for the road journey from Melbourne to Adelaide, essentially because the freight forwarded is not required to make the additional transfer to sea freight.

An examination of the freight charges (as shown in the table below) provides a clear and unambiguous demonstration of the cost penalty incurred in transporting product from Hobart to Melbourne compared to transportation over a similar distance from Melbourne to Adelaide.

Table 3 following highlights the cost penalties and compares these with the current Equalisation rebate paid under the existing TFES.

Table 3 (information current as of 16 June 2006)

Freight cost Penalties compared to Rebates under current TFES


Confidential data removed..See paragraph below.

Note:

- The 'penalties' shown in the above table are calculated by comparing the cost per Pallet or per Tonne for the Hobart to Melbourne route with the same costs for the Melbourne to Adelaide road journey (refer Table 2)

As shown in the above table, on either a pallet or tonnes basis, the freight penalty for product moved from Hobart to Melbourne (compared to Melbourne to Adelaide) is higher than the rebates paid to Cadbury under the current TFES arrangements. In summary, the withheld data shows that CS still incurs a 14% freight cost disadvantage after application of the TFES when comparing our costs for the Adelaide-Melbourne route vs the Hobart-Melbourne route.

In addition to the penalties already highlighted, there are a number of other disadvantages which add significantly to the costs Cadbury are required to meet to maintain a manufacturing base in Tasmania. These include the cost of additional product damage resulting from the change of transport mode (from road to sea to road), and increased transit times from Hobart to Melbourne compared to a similar length journey by road on mainland Australia. These are further explained below.

## **Product Damage**

Due to the number of times that product must be 'handled' on the journey from Hobart to Melbourne, and because part of the journey is by sea over notoriously rough waters, the amount of product damage incurred is significantly higher on this route than for a similar length trip by road only. Whilst it is difficult to place an actual dollar value on the cost of stock damaged on this route, it is a cost which is nevertheless additional to the overall cost of manufacturing in Tasmania and should reasonably be taken account of in the calculation of any fair 'Freight Equalisation' rebate.

## **Transit Time**

By way of example, on a 'road-only' journey from Melbourne to Adelaide (a total distance of 725 km, compared with a total distance of 620km from Hobart to Melbourne) the transit time is normally in the order of 10 hours. Product in Melbourne can be loaded onto a truck early in the morning, road freighted to Adelaide, and delivered to a customer on the afternoon or night of the same day. Unfortunately, the same cannot be said for product travelling between Hobart and Melbourne. Normally the best that can be achieved is that product loaded in Hobart by 8am can be received in the Cadbury Melbourne Distribution Centre at about 12 noon the following day: a transit time of about 28 hours. However, product manufactured in Cadbury's Hobart factory and loaded after 8 am will not be shipped until the following day, and therefore cannot be in the Distribution centre until about 12 noon on the third day – the transit time for the majority of product is approximately 48 hours.

Cost pressures, demands from customers, and 'World's Best Practice' techniques demand that manufacturers not only keep inventory levels down, but also continually improve the level of service to customers. In order to maintain an appropriate level of customer service, the increased transit time for product originating in Tasmania demands that inventory must be held at a higher level for that range of products. In all fairness, these costs should also be taken into account in the 'Freight Equalisation' calculation.

## **Other Factors to be considered**

There are many other factors which should be considered as part of a comprehensive review of the TFES. From the Cadbury perspective, some of these are as follows.

### *Cadbury Product Costing*

As previously stated, the Tasmanian factory currently produces a certain range of products, none of which are duplicated in factories on the mainland. In costing the manufacture of existing products and any new products that the company decides to produce, all costs, including the cost of transportation to the Distribution Centre are taken into account.

If the cost of transporting product effectively rises, the extra cost may jeopardise that product being made or continuing to be made in Tasmania. Ultimately this may lead to a reduction in products that are made in Tasmania and a consequential reduction in the number of people employed in that state.

Further, if by reason of the nature of the product, it were not feasible to make the product in one of the two mainland factories, it is possible that the product could be imported from an overseas operation, resulting in a loss of employment to Australia as a whole.

### *Capital Investment*

Over the past ten years, Cadbury Australia has invested many millions of dollars in new capital equipment for its Tasmanian operation. Not only has this investment supported the Cadbury operation in Tasmania, but it has also created significant full time and temporary jobs for people in Tasmania.

Specifically, the two major investment decisions (\$25m in 2001, \$24.5m in 2005) would have been made in favour of the Ringwood (Victoria) plant in 2001 or the Dunedin (New Zealand) plant in 2005 if the TFES had not been applicable to these investment discussions. Collectively, the loss of these two investments would have resulted in an approximate employment reduction of 30% in 2001 followed with a further 8% – 10% reduction in 2005. More importantly, with the start of contraction in the size of a manufacturing plant, overhead costs inevitably need to be redistributed over remaining volume leading to further competitive pressure from other plants.

Any reduction in levels of assistance from the TFES may affect future major capital investment by Cadbury in the State of Tasmania and jeopardise any new employment opportunities.

### *Employment*

Cadbury currently provides direct employment for up to 800 people in its Tasmanian operation. Using an accepted industry multiplier of 2.5, up to a further 2,000 jobs are sustained in Tasmania through the presence of the Cadbury operation. For example, Cadbury sources all fresh milk required for production of its chocolate from Tasmanian farmers.

A reduction in levels of assistance may lead to a reduction in these numbers. The long-term effect this may have on the economy of Tasmania and the net effect on the Commonwealth Government's overall budget through increased social security obligations should also be considered in a comprehensive review of the TFES.

## **Conclusion**

This paper clearly demonstrates that the current levels of assistance to Cadbury under the existing TFES does not fully compensate for the disadvantage incurred as a result of the lack of alternative road or rail transport to move material to and from Tasmania.

If the interests of true equity are to be served and the original intent of the Tasmanian Freight Equalisation Scheme is to be realised, rather than reduce the levels of assistance further, Cadbury strongly recommends the scheme is maintained at its current rates and in an uncapped way to promote growth and development of our manufacturing base in Tasmania.

In this way, the Review Authority would help to ensure that the best interests of Tasmania and its people are served, and that all users receive adequate, fair and reasonable assistance.