

**PRODUCTIVITY COMMISSION INQUIRY INTO INTERNATIONAL LINER CARGO
SHIPPING: REVIEW OF PART X OF THE TRADE PRACTICES ACT 1974**

SUBMISSION BY THE BROKEN HILL PROPRIETARY COMPANY LIMITED - JUNE 1999

1. Introduction and Overview

This Submission is made on behalf of The Broken Hill Proprietary Company Ltd. We wish to comment on a number of the issues raised in the Issues Paper relating to the Commission's Review of Part X of the Trade Practices Act 1974.

The views expressed in this Submission include the following:

- The operation of market forces in the Australian liner trades during the 1990's, particularly the level of competition between Conference and independent lines, has resulted in substantial improvements in freight rates for shippers, and in access to adequate and reliable shipping services.
- In view of the trends being experienced in global freight markets, abolition of Part X would probably result in added turbulence and volatility in the liner trades servicing Australia.
- The outcomes might include further downward pressure on freight rates, which would be welcome.
- Given the effective operation of market forces currently, and the general level of satisfaction amongst the major participants in Australian importing/exporting with the present state of equilibrium under Part X, any move to make fundamental change should be preceded by a careful evaluation, and balancing, of anticipated benefits and risks.
- Under any amendment of the Part X regime which preserves the entitlement of shipping lines to engage in cartel activity (particularly in relation to pricing), whether by means of authorisation or otherwise, it would be important to explicitly maintain the elements of Part X which enable collective actions by shippers.

Our BHP Transport business ("BHPT") is a diversified transport organisation offering integrated logistics solutions worldwide. It moves approximately 80 million tonnes of cargo annually and earned revenue of A\$1.7 billion in 1997/98. The operations of BHPT include:

- Vessel Chartering
- Liner Shipping Services
- Fleet Ownership
- Land Transport and Logistics
- Ship Management
- Marine Fuels
- Ship's Agency
- Towage
- Stevedoring
- Warehousing
- Project Consultancy

As part of its network of global services, BHPT has an interest in issues relating to the provision of liner shipping services to and from Australia. These services are critical links in many of the supply chains which it manages on behalf of its clients.

A major business objective is to ensure access to services for BHP Group liner cargo movements into and out of Australia which are reliable, efficient and cost effective, and underpin the competitiveness of our products in world markets. The BHP Group operates in competitive commodity markets where prices are under constant pressure.

As a major Australian shipper, BHP is particularly concerned to ensure that liner shipping services are provided at the lowest possible cost.

2. Trends in Liner Freight Markets

Through the 1990's we have observed significant changes in traditional conference arrangements, including the growth of independent operators in the Australian trades. With the erosion of the strength of market share positions previously enjoyed by some operators, many of the traditional boundaries between conference and non-conference have changed. Independent lines have joined with other independents and new entrants have joined together to create consortia arrangements. Our export trade routes have a mixture of conference, independent operators and consortia providing services to Australian export shippers. All lines have demonstrated an improved and sustained ability to meet our requirements regularly.

Another major trend observed throughout the 1990's has been the generally downward direction in freight rates in all trades. For example, the following table depicts the direction in BHP's freight rates (with Conference and independent lines) for export shipments over the past 3-4 years, using 1995 rates as a base index :

	Singapore	Bangkok	East Malaysia	Hong Kong	Taiwan	Japan
1995	100	100	100	100	100	100
1997	85	84	100	89	98	94
Jun 98	60	58	68	83	90	76
Dec 98	48	45	63	75	71	72

Today, in all trades, all rates are negotiable. Traditional practices have given way to more open approaches where all Australian exporters have access and can negotiate "blue water" freight rates with shipping lines of their choosing. This is the result of the increased competition that exists for export shipments from Australia, particularly the competition between Conference and independent lines.

A further trend is the emergence of global operators. This is driven by the fact that exporters are now purchasing their liner shipping overseas as part of the global liner market. No longer are Australian liner shipping services dominated by the shipping lines with historical ties in trade with Australia. There are now a kaleidoscope of liner shipping companies, from global operators to regional carriers, and these provide a full range of sea freight options to Australian exporters. Routing options now available to a particular destination are many, providing Australian shippers with greater access to markets on competitive terms, where once we were reliant on the service of a few.

Australia's liner trades, and indeed world shipping markets, are poised for a period of rationalisation of services, with likely outcomes including the increased concentration of power into the hands of fewer lines servicing Australia. Market forces are at work in an open, complex and frequently chaotic environment. Shipping lines can be expected to adjust their strategies in servicing Australian exporters in line with the global market forces applying to them. The services offered will increasingly be driven by the requirements of world shipping markets.

Over the past five years we have also seen the development of transshipment operators who are now providing reliable and efficient hub and spoke networks around the world. These operators are a competitive alternative to direct operators and are extensively used by BHP.

Traditional boundaries between liner shipping companies and NVOCC's, freight forwarders and third party logistics providers are blurring, with the latter group in particular poised to take over some of the functions which have been the domain of the shipping company. For example, shipping lines have been known to provide freight forwarders volume based discounts to secure market coverage (instead of the shipping line providing the service through its own infrastructure). In this environment, the distinction between the "blue water" component of rates and charges and other ancillary and land-based charges, never clear, will become even more clouded.

Technology has led to the development of larger and faster vessels, resulting in improved transit times and schedule integrity. These improvements have enabled shipping lines to take their services to a new

level, offering weekly sailings and fixed day services for certain trade routes. Such features have been used in marketing to clearly differentiate services from rival offerings.

An unmistakable trend has been the decline in the contribution of the Australian flag shipping fleet to the carriage of Australian export and import cargoes. The "Australian Maritime Transport, 1998" report prepared by the Apelbaum Consulting Group and published by the Australian Shipowners Association in January 1999 indicates that :

"Despite an increasing Australian seaborne market, the cargo carried by Australian registered shipping continued to decline (a reduction of 9% compared with the previous year and 25% relative to 1995/96) to 10.3 million tonnes in 1997/98. As a result, the market share achieved by Australian shipping diminished to 2.2% in 1997/98, the lowest contribution since the analyses commenced in 1988/89. Despite a growing indigenous market the demand for Australian Shipping has declined."

Liner freight volumes are sensitive to changes in the shipping demand/supply balance, and commodity market conditions. For example, over the past 6 years, particularly in the last 2 years, BHP has effected, in relation to its containerised liner shipments:

- A shift in emphasis from containerised to break bulk exports, as market offers and shipping arrangements are adjusted in response to Asian economic conditions. (With the size and task of our export steel cargoes, we have the ability to achieve critical mass by converting cargoes that once would have moved in containerised form on liner services to larger parcel sizes utilising our own break bulk charter services.)
- Some refocussing of Australian steel manufacturing towards the domestic market rather than export markets, together with development of new downstream steel production capacity within Asia.

3. The Effectiveness of Part X and Implications of its Abolition or Modification

The decade of the 1990's has seen Australian exporters well served by competitive and efficient liner shipping services:

- Service levels have been high, and have improved
- Freight rates have declined substantially, and
- Shipping capacity levels to and from Australia have grown.

Whether or not these outcomes would have been achieved anyway without Part X, or achieved faster, are moot points; they arguably would have been, due to the operation of market forces.

It is difficult to predict with any certainty the precise way in which shipping services will develop in the future, if Part X is no longer in operation or is substantially modified.

Abolition of the existing Part X may have the effect (subject to the scope for authorisations to be obtained) of exposing international liner shipping to the full force of Part IV of the Trade Practices Act. This would probably result in added turbulence and volatility in the liner trades servicing Australia. Some of the following outcomes might be anticipated:

(i) Acceleration of the trend to mega-carriers.

An inability to engage in collaborative behaviour to provide high quality service schedules will drive some shipping operators to seek to establish stronger positions in the Australian trades through "taking out" other players. Either through the impact of competition and aggressive pricing, or through takeovers and mergers, a more limited number of players with very strong market shares would be likely to emerge in the Australian trades.

(ii) Changes in the nature of services provided to/from Australia.

The advent of "hub and spoke" services has been pronounced over the past five years. The development of Australian liner services in the direction of being feeder services to the major Asian

regional ports, linking into major East-West trunk routes, will accelerate. Many traditional point-to-point liner services (historically offered by Conferences) could collapse and be fundamentally restructured. Some erosion of service levels, and loss of direct services to some major Australian export destinations, would be likely. It is problematic whether this would be more than compensated for by freight cost savings.

(iii) More volatile freight rates.

If Conference lines were no longer permitted to reach agreement on freight rates, there would naturally be a downward pressure on freight rates, at least in the medium term. It could be expected that rates might be more volatile and opportunistic (compared to the relatively stable levels encouraged by the Part X framework) as, for example, shipowners seek to capitalize on any periods of shortage of cargo space. BHP would welcome outcomes which involve further downward pressure on freight rates, though we are conscious of predictions that have been made that there would be offsetting negative implications for service levels.

Many of the developments outlined above are already occurring, and are perhaps natural consequences of globalisation. An outcome to this review which exposes liner shipping arrangements to the full force of Part IV of the Trade Practices Act would be likely to hasten the advent of added turbulence in the liner trades servicing Australia, and drive a realignment of many aspects of the shipping services which have applied in those trades over the past decade.

Given the effective operation of market forces which is currently occurring, any move to make fundamental change should be preceded by a careful evaluation, and balancing, of anticipated benefits and risks.

There seems to be a generally high level of satisfaction amongst the major participants in Australian importing/exporting (including a range of shipowners, both conference and non-conference, shippers and importers) with the state of equilibrium which exists under the current system. There does not appear to be a groundswell within the shipping or trading communities calling for the abolition of Part X.

In our view, under any amendment of the Part X regime which preserves the entitlement of shipping lines to engage in cartel activity (particularly in relation to pricing), whether by means of authorisation or otherwise, it would be important to explicitly maintain the elements of Part X which enable collective actions by shippers. These elements include the provisions which enable shippers to negotiate collectively to obtain assurances of adequate minimum levels of outwards liner cargo shipping, and to determine common terms and conditions for bills of lading.

There are numerous recent examples of instances where shippers, acting collectively in accordance with Part X, have been successful in avoiding attempts by shipping lines to impose ancillary charges, covering items such as Port Service Charges ("PSCs"), Terminal Handling Charges ("THCs") and Currency and Bunker Adjustment Factors ("CABAFs"). Whether or not decisions to impose such charges fall within the jurisdictional boundaries of Australian regulators has, in the past, proven to be a difficult issue. As a member of the Australian Peak Shippers Association, BHPT has been active in ensuring that such charges can be justified, relate to the actual costs being incurred by the shipping lines and, most importantly, ensuring that lines are not passing on and expecting Australian exporters to bear all the risks (and losses) associated with international liner shipping. For example, attempts to immediately pass on all the risks associated with Australian dollar currency fluctuations on world markets through unfair CABAF regimes, have been successfully avoided by collective action. An equitable process currently exists for reviewing CABAF triggers and formulae for reviewing PSCs. These outcomes have been of great benefit to Australian exporters.