*Australian Journal of Agricultural Economics*, Vol. 27, No. 2 (August 1983), pp. 139-144

# TRANSPORT ISSUES

J. H. E. TAPLIN and F. D. GALLAGHER
*Office of the Co-ordinator General of Transport, Perth, W.A. 7000*

Being asked to comment on Chapter 8 of the Report, presented us with an awkward problem. It is, in a sense, difficult not to be unfair to the Group in any critical and in-depth review of the issues and options raised: or indeed, if a similar approach is taken to issues and options not raised in it. This is because, in its terms of reference, the Group was simply asked to 'identify major policy issues and options'. The Group does seem to have been more successful in identifying the policy issues than the options.

We appreciate that it would be difficult in a short chapter to provide more than an annotated treatment of the many policy options which relate to transport, storage and handling of Australia's rural exports. This general observation has influenced our commentary. It is not as iconoclastic as it might have been in other circumstances.

In our remarks we have opted to comment on the emphasis (or lack of it) given to the policy issues and options which have been raised in Chapter 8. Following that, we discuss a few of the key transport issues identified in the Report. Finally, we comment on a few issues which we think were either neglected or given less than adequate treatment.

## *Matters of Emphasis*

The Group (para. 1.11) '. . . regarded the agricultural sector as extending beyond the farm gate to include a range of activities directly and indirectly related to the production, processing and marketing of food and fibre'. Meat, dairy products, canned and dried fruits and vegetables, fruit juices, malt and wool are the base cargoes for outbound liner shipping services.

The annual freight bill for Australian exports carried on liner services may exceed $A1 billion. The economic behaviour of the operators of these liner shipping services and the characteristics of the market they operate in have excited considerable interest and argument. In our view, the Group has quite rightly focused attention on the relationship between liner Conferences and shippers of export liner cargoes than any other policy issue.

Other transport, storage and handling issues raised by the Group can be categorised as 'major' or 'minor' according to the treatment they are given in Chapter 8.

Issues treated as 'major' were:

(a) costs and productivity on Australia's waterfront;
(b) co-ordination, costs and investment in the bulk grain storage and handling system (including port facilities); and
(c) the implications of revitalising Australian shipping, particularly in regard to manning levels on Australian-crewed ships and cargo reservation.

Issues treated as 'minor' were:

(a) the role of charter shipping in moving Australian agricultural produce, particularly grains and sugar;
(b) the pricing of rail freight services and the need for railways to pursue commercial objectives; and
(c) air freight, the high-priced alternative for moving high quality and perishable rural-based exports.

We agree that each of these six issues is important. However, we disagree about the relative importance the respective issues seem to acquire in Chapter 8. The three issues classified as 'minor' received only cursory treatment. Deeper analyses would reveal that there may be greater gains for the agricultural sector in identifying and pursuing appropriate economic objectives in these three areas than in either the grain storage and handling area or in the revitalisation of Australian shipping.

What the emphasis given to the 'major' issues may reflect is distortions in popular industry perceptions of their relative importance. The policy implications of linking cargo reservations to revitalisation of Australian shipping can be used to illustrate this point. Frightening though the prospect might be, in economic terms, reservation of 40 per cent of cargoes (or even of one type of cargo, say, wool) for Australian flag vessels is a very long way off. The size of the Australian fleet is such that only about three per cent of Australian exports are carried in Australian flag vessels. If Australian shipping were revitalised to the extent that this could be doubled to six per cent, in the next five years, the economic threat from cargo reservation according to the UNCTAD 40:40:20 formula would still be a long way off. It would be extremely difficult for a Federal Government to embrace cargo reservation and turn the 40:40:20 formula into an effective policy within a decade. In fact, in the immediate future, Australia has much more to fear from the inefficiencies of cargo reservation in Third World countries than from within (see Brooks 1983).

Through building up national fleets, reserving 40 per cent of trade for those fleets, and becoming an integral part of the Conference network, governments in Third World countries seek to gain at the expense of the developed industrial economies, particularly the traditional maritime nations of Europe and Japan. In a global sense, there are obvious economic inefficiencies in the implementation of these constraints on competition in world shipping markets. Indeed, it may be argued that, as a group, Third World countries may gain little, in the long run, from these restrictive policies, except in terms of favourable flows of foreign exchange. Nevertheless, it is conceivable that individual Third World countries, for example Malaysia and Taiwan, may stand to gain considerably from pursuing these policies.

### *Freight Rate Negotiation*

The hard line of the Third World countries contrasts sharply with the somewhat weaker stance taken on freight rate negotiation by the Group. What is sought is a 'balance of advantage' (whatever that means!) among the parties conducting commercial negotiations (para. 8.32). The approach, in typically Australian Government negotiating style, seeks 'equity' rather than advantage for Australian shippers, most of whom have, for decades, negotiated from a position of disadvantage. The

Australian farmer has been a price taker in shipping as well as export markets (para. 8.1).

The same sort of criticism can be levelled at the pan-Australian approach to freight rate negotiation. It seeks equity and a quiet life for administrators, rather than advantage for exporters who are in a position to gain from their relative proximity to markets. This may apply, in particular, to exporters located on the Indian Ocean near to markets in South-East Asia and the Arabian Gulf.

It is our firm opinion that, for too long, Australian exporters as a whole have been at a disadvantage in negotiating freight rates with operators of liner services vessels. It is true that some shippers, in particular the Australian Meat and Live-stock Corporation, have sharpened up their negotiating techniques in recent years. It is also true that the presence of non-Conference operators and excess capacity in some trades has led operators to be more competitive in their bidding for shippers' cargoes. The competitive activity of ABC Lines in the Australia-Europe trade is a case in point.

Nevertheless, the fact remains that shippers need to be armed with more facts at the negotiating table. They need to know more about shipping costs; more about the freight rates which shippers of cargoes imported into Australia are paying; and, importantly, more about what alternatives to existing services are available and the state of the shipping market. We suggest that shippers, actively supported by government, need to build up a sophisticated and readily accessible intelligence service in these areas.

### *Excess Capacity*

The Group did not mention excess capacity in transport, storage and handling systems and the costs this may impose on agricultural and pastoral producers. Excess capacity is manifest in the liner trades through overtonnaging of shipping routes. Thus, there may be not only a higher quality of service than is really required, in the form of ships which are more capital intensive and sophisticated than necessary (this is recognised in paras 8.18 and 8.19), but also too many of these ships. The recent fracas on ANSCON routes, where the ANL vessel 'Australian Endeavour' was withdrawn from service and the non-Conference operators Fesco, Hong Kong Island Line, and Zim were put under pressure from both the Conference and the maritime unions to reduce services, provide ample evidence of this problem. Further, our own research indicates that overtonnaging on liner shipping routes linking Australia to South-East Asia (from Taiwan to Malaysia) may cost shippers more than $30m per annum (based on 1981 trade flows).

The notion of what is the 'right' resource input, in this case the 'right' amount of shipping capacity required to service a particular trade, illustrates the advantages and disadvantages of the Conference system. As a general rule, it could be stated that the Conference system is seen to advantage shippers when there is some scarcity of shipping capacity. It can ensure that adequate services are provided and that cargo loadings and service frequencies are rationalised. Shippers gain from this situation provided their bargaining position is strong enough to prevent shipping lines forcing up freight rates to levels where monopoly profits are made.

We would suggest that there is little to be gained from the Conference

system when world liner shipping capacity exceeds the requirements of the markets for their services. This is the situation in 1983 and particularly applies to Australia where the physical dimensions of export cargoes have been affected by both the world-wide recession and the results of recent widespread drought. In such times, Conferences are reluctant to withdraw ships from trade, particularly where they can influence shippers to negotiate freight rates on an incremental cost plus basis, even though this allows them to bid, in a competitive market, for cargoes by offering large discounts on formally negotiated freight rates. At present, the Conference apologia (as put in paras 8.16 and 8.17 of the Report) does not hold much water. In fact, withdrawal of some capacity from some trades may be, in an economic welfare sense, the best thing that could happen.

### *Transport and Storage of Grains*

Arguments on excess capacity are relevant to Australian ports and container terminals and also to the grain storage and handling system. In the latter, the interesting problem of providing for peak demands is relevant. The ramifications of providing for peak flows, all too familiar to transport planners, are not really given an airing in the Report. Harvest peaks and the requirements for peak loadings and optimum rates of handling on all or parts of the rail haul and/or storage system may be so far apart that costs will be minimised in a system which is designed to cater for much less than maximum flows.

In relation to grain storage and handling, the Group claims (para. 8.73) that there is a case for rationalising and co-ordinating the system. They advocate achieving this per medium of a National Grains Co-ordinating Committee and, presumably, a proliferation of clones of that committee at state level. There is no hint as to the basis for this claim and we feel that it may be somewhat overstated. We suspect that its genesis may lie, at least partly, in a somewhat misplaced fear that Panamax-type bulk carriers/tankers (around 50 000 dwt to 70 000 dwt) will come to dominate grain shipping within the next few years. We think it is safe to predict that large quantities of a wide assortment of grains will continue to be carried in smaller conventional dry bulk ships (upwards of 10 000 dwt) up to the end of this century.

### *The Transport Policy Viewpoint*

The Group paid scant regard to some key economic issues in the world of transport policy (as opposed to agricultural policy). This has been done at the risk of ignoring the impact of transport policy on the handling of agricultural products.

One of the main thrusts of transport policy is to ensure proper recovery of the costs incurred in providing transport facilities. This has two implications for people in agriculture. First, they may well find that chronic under-recovery of the direct costs imposed on the road system by heavy trucks will be rectified. This could have many implications, for instance, hauling grain to other than the nearest rail siding may become unprofitable. Second, agricultural pressure groups may be well advised to reconsider pressing for more and better port facilities, more wheat rail wagons and so on; objectives which are reflected in the Report. In most

states, it is only a matter of time before it becomes standard practice to recover fully the costs from the industry for which the investment is made.

What the Group may have only partly perceived is that the name of the game currently in transport is to get the most out of existing resources and facilities. Where there is a peak load, operators of transport utilities will tend to charge the users who impose the peak load for virtually the entire capital cost. This is a simple extension of marginal cost pricing principles (Williamson 1966). Thus, in the case of wheat, it will be in the producers' interest to ensure that the peak load on the rail and port system is minimised. Of course, the peak load must be borne somewhere but it is probably better to cope with it in the storage system, rather than in the transport system as recognised by the Group.

A topic receiving a great deal of attention is setting charges to allocate the joint costs of joint-user transport facilities. This has not been mentioned explicitly by the Group. However, it underlies the discussion of liner Conference rates, where the joint costs are normally allocated according to what the traffic will bear, an approximate second-best pricing principle. What the major commodity groups, themselves, have begun to realise is that their commodities can bear very heavy charges unless alternative shipping can be found. Formalised negotiations are of little relevance unless the shipper can threaten confidently to take his commodity to an outside carrier.

In rail transport there are improved ways of identifying a higher proportion of separable costs and thus reducing the need to allocate the seemingly joint costs on the principle of what the traffic can bear. An exercise carried out for Victorian Railways some years ago showed that the truly separable or 'avoidable' costs associated with the carriage of wheat involved the possibility of closing down the whole wheat branch-line system and all of the rolling stock and facilities directly associated with the carriage of wheat. This, and the direct costs of haulage, constituted the attributable wheat freight cost and was found to be higher than the rate actually being charged. That is not the whole story because Victoria's method of handling the wheat peak was not optimal. Nevertheless, it shook the belief that agriculture generally pays too much for rail transport.

### *Other Issues*

We were surprised that a number of other relatively important policy issues in the transport, storage and handling areas were either not mentioned or lightly skimmed over in the Report.

(a) Chapter 8 is almost totally export oriented, yet a significant proportion of the transport, storage and handling of rural produce relates either to the domestic market, or to the internal movement of produce to secondary processing centres: grain to flour mills, fruit and vegetables to canning works, wool to wool dumpers, live animals to abattoirs, and so on.

(b) As a consequence of (a) there is no mention of the regulatory and economic problems (and physical hazards in the 'wet') related to road-based cattle trains.

(c) Live animals are also neglected through failure to mention the

topical and lucrative live-sheep export trade and the controversy which surrounds it.

(d) Another area of omission, as the road train example illustrates, is the special problems faced by existing and potential producers in northern Australia, such as isolation and restrictions on the movement of perishable produce out of Australia on chartered aircraft.

(e) There is no mention of the special problems presented by refrigerated cargoes and why they are particularly sought after by operators of shipping lines. Nor is there any mention of the interesting trade-off between frozen and chilled meat, which becomes, in effect, a trade-off between the relative costs and speeds of delivery via the sea and air transport modes.

(f) The rural implications of the failure and, on some parts of the continental coastline, the demise of Australian coastal shipping are not discussed.

(g) The implications of the trend toward containerisation of export cargoes are also neglected. So is the important related issue of packaging and its relationship to quality and reliability of presentation in the market place.

(h) The existing role of cargo centralisation and the potential of both the existing east-west (Perth-Adelaide) landbridge, and future north-south (Darwin-Adelaide) landbridge are not discussed.

(i) The economic implications of c.i.f. versus f.o.b. sales of grains or other exports are not discussed in a transport context.

(j) A very serious omission is a failure to discuss the economic implications of the movement toward deregulation of land transport which has characterised the Australian transport scene over the past decade. The movement will continue for at least another decade. Before the state railways can operate on 'a more commercial basis' (as suggested in para. 8.57), they need the freedom to do so. This can only be guaranteed through deregulation and the consequent eradication of common-carrier obligations.

## *References*

Brooks, M. R. (1983), 'Canada and the liner code of conduct: consumerism and public policy', *Maritime Policy and Management* 10(2), 77-85.

Williamson, E. D. (1966), 'Peak load pricing and optimal capacity under indivisibility constraints', *American Economic Review* 56(4), 810-27.