

File Note: M2003/360
Meeting with Importers Association of Australia (IAA)

Tuesday December 9 2003
11:00 – 12:30 am

Present: Mr Zoran Kostadinovski – Commercial Operations Manager
Scalzo Food Industries

Mr Tony Beaver – Secretary
Food and Beverage Importers Association

David Salisbury - ACCC
Steven Eddie - ACCC
Matt Amor - ACCC

RE: IAA submission to the ACCC on the Part X investigation into the AADA

The IAA agreed to put the meeting notes on the public record and it will form part of its submission to the ACCC.

The IAA will also be making a written submission to the ACCC.

David S outlined the procedure of the Part X investigation and described the nature of the criteria used in the investigation and how the ACCC came to its decision to launch the investigation. He talked about the role of the ACCC and the legislation and testing of the potential public benefits of a discussion agreement against the potential competitive detriments of a discussion agreement. David stated the Commission has no direct precedent for its role in investigating import trades.

Steve E asked a series of questions that are related to the issues brought up in the Issues Paper and Zoran and Tony replied.

The first set of questions related to demand / supply of the southbound liner trades from North East Asia

Zoran and Tony stated that there has been a big move towards China as a source of imports world wide. The demand increases that Australia has experienced on this trade are expected to be permanent, in the wake of China joining the WTO. There is an increase in demand for imports from China which is largely due to the growing Australian economy.

Australia liner trades are small by comparison with those of EU and USA. It is a low profit operation and is considered low priority by the carriers.

The carriers have not monitored trends in supply and demand on the China - Australia trade. The IAA believes that the increase in volumes from China was evident before this year. There is talk about chartering costs increasing significantly, but many of the lines own their vessels.

About 80% of liner supply carrying imports from China to Australia is transhipped through Singapore and other hub ports such as Pusan, Chiwan, Qingdao etc. Only the supply sourced from Shanghai is shipped direct. According to Zoran there is only one vessel per week arriving in Australia.

There is very little consultation in setting freight rates, these are set by principals overseas in China (Hong Kong). Responsibility for freight rate setting has been transferred from Australia to the principals overseas. There is currently no discretion for local (Australian) offices of carriers to set rates for importers.

Freight rates

Zoran said that the IAA will provide the ACCC with an example of current market freight rates. He stated that current market freight rates for imports from China are in the \$US1300 - \$US1450 range. Rates in June were in the range \$US500- \$US700 max, an increase of between \$US800 and \$US900 per TEU. Forty foot box prices had climbed by about \$US1300 per FEU. There was also the \$US200 peak season surcharge for which the importers get no extra service. Admittedly, rates were previously extremely low.

By comparison the transshipment rate for imports from Europe is of the order \$US1000 per TEU.

The importers do not believe costs have risen, but container repositioning costs undoubtedly play a part. But it is proportional, so the extra revenue from an increase in boxes shipped southbound pays for the extra empties shipped northbound.

There is no certainty of service and contracted prices do not guarantee space on a vessel. Zoran gave an example of a contracted supply of \$US1200 not being honoured as the cost and freight (cfr) price was \$US1400. The lines are pricing what the market can bear.

There are fewer and fewer contracts offered by carriers to importers due to shortages of space. It is very difficult now to get a firm quotation for a container 30 days in advance.

The impact of the rate rises on food importers is that it is very difficult to pass on costs into a competitive supermarket industry. Many food companies experience sales losses of between \$300,000 and \$400,000, not counting write offs of stock due to delays / spoilage. The importer firms will bear these losses in order to maintain their customer base.

Not just the food industry, Harvey Norman has stated that the increased freight rates are affecting profitability.

Service standards

Service standards have fallen because the lines have not responded to the increase in demand by changing their service structures and amount of tonnage on the route. They are still transshipping 80 per cent of volumes through hub ports and the increase in volumes has led to increased delays and congestion at these ports. Delays of up to 3 to 4 weeks, with containers sitting on the wharves are common. The lines cannot reconfigure their services back to direct because they need agreement amongst them all. It is estimated that the storage at transit ports would cost the lines up to \$US100 per TEU per day.

This makes JIT systems and inventory management difficult and leads to the importers experiencing imposition of penalty clauses in contracts with retailers. It is difficult to use force majeure in this area. It also leads to large stock write downs and increased rates of spoilage for reefer products. There is very little service from the lines, cargo tracking breaks down and often the line loses control of the logistics, and experiences of missed connections between vessels are increasing. Moreover, for lines going to Singapore from China there is shortage of space due to increases in shipments bound for Europe.

Zoran could not comment on how much extra supply would be needed to satisfy the current level of demand.

The deterioration in service is seen by the IAA as worse than the increase in freight rates.

There is a lack of forward planning by carriers and they do not cater for their customers needs as logistics providers. Carriers are only concerned with raising rates.

Shipping line entry into this trade

The IAA do not have a feel for why so far there have been no new entrants attracted into this trade and suggested that foreign carriers may face barriers to entry in accessing Chinese ports – there may be licensing requirements or may be limits on the number of foreign carriers allowed. There may be hidden costs for independents outside the AADA to enter the trade. It is also difficult to go against 16 incumbents.

It could also be that in the current climate of generally increasing freight rates that, opportunities for profit are greater on other Chinese export / import trades.

Competition between the parties to the AADA and other carriers

Zoran stated that freight rates for independent transshipment services to Australia have increased in line with the freight rate increases implemented by the AADA, but the importers are not attracted to use their services as they are facing the same space shortages and lack of service. Transit times are often long and connections can be tenuous. The AADA services are more direct.

There have not been any increases in slot space made by the South East Asian lines to cater for the increase in demand for transshipment through Singapore for cargoes sourced from China.

Meaningful negotiations between the IAA and AADA

The AADA and IAA only really discuss minimum service levels and not freight rates. The IAA do get to comment upon new proposals for agreements, but they are given very short time frames to reply and the agreements are registered by the Liner Registrar in any case. The agreements are written by lawyers and are quite complex for the layman. It is all about a bureaucratic process rather than any commenting about benefits.

Counterfactual: what would happen if the AADA was deregistered?

The IAA is concerned that supply would dry up as the carriers would abandon Australia so the AADA is necessary. Liner supply to the export trades out of South America has fallen despite high freight rates due to more profitable routes elsewhere and because of high trade imbalances.

Instead of seeking deregistration of the AADA, the IAA would like to see service levels on the liner trade improve, with better carrier / customer relationships and efforts by the lines to facilitate service levels in this period of booming demand, rather than just increasing rates. The latter policy is short sighted.

Future direction for Part X

Zoran stated that the EU is currently reviewing its anti trust immunity arrangements and that they are also conducting an investigation into the market conduct of a major conference. This is due to the Australian example of the current Part X investigation.

The IAA would like to see an OSRA style of reform for Australian liner trades which they see as workable. They are in favour of consortia agreements such as VSA, slot share etc as they lead to lower costs, improved service configuration and network economies, but they are not in favour of talking agreements.