Patrick Terminals
Gate B105A Penrhyn Road
PORT BOTANY NSW 2036
AUSTRALIA
ABN 33 065 375 840

10 December 2020

Mr Praveen Reddy
Executive Director
Freight Victoria
Department of Transport
GPO Box 2392
MELBOURNE VIC 3001

praveen.reddy@transport.vic.gov.au

Dear Praveen,

Notice pursuant to the Voluntary Pricing Protocols

I refer to the new Voluntary Pricing Protocols and our recent discussions on fee matters.

The purpose of letter is to notify you that Patrick will be increasing its Landside charge from $82.50 to $84.90 per export full container and from $125.80 to $129.50 per import full container, with effect from 1 March 2021.

The Landside charge per full container of $84.90 (export) and $129.50 (import) partially recovers the following costs:

- Investment and committed capital expenditure to dedicated landside infrastructure by Patrick at East Swanson Dock. This investment and committed capital will continue to drive tangible improvements in the efficient landside operations of the terminal;
- Property costs primarily consisting of the rent imposed by Port of Melbourne under the terms of our lease agreement;
- Maintenance and operational costs associated with providing our landside operations

Patrick continues to absorb significant costs associated with providing landside services. These unrecovered costs are substantial and continue to grow notwithstanding the partial recovery through the Landside charge.

The methodology from which Patrick determines its Landside charge at East Swanson Dock is consistent with our approach nationally and is based on a cost recovery methodology. Patrick provides further detailed information on a confidential basis in Appendix A outlining the cost recovery methodology. Patrick is proposing to continue to absorb a proportion of these costs within its business and recover $84.90 per full export container and $129.50 per full import container delivered / received.

We are targeting to apply this charge from 1 March 2021 (Monday 1 March has been chosen as it this is the beginning of our weekly billing cycle). To achieve our targeted application date of 1 March 2021 we respectfully request Freight Victoria to respond to us on or before 29 January 2021. This will enable us to provide at least 30 days' notice to our customers of the increased Landside charge.
To provide additional context to support the changes in charges we attach in Appendix B details of current market themes along with the well-known industry challenges being faced by stevedores in the current market.

Patrick reiterate our commitment to the Voluntary Pricing Protocols and working with Freight Victoria to transition to the new industry administrative requirements.

Please let me know if you require any further information about the charge.

Yours sincerely,

Michael Jovicic
Chief Executive Officer

Appendix A

Patrick's Landside charge at East Swanson Dock is currently based upon three main categories as outlined in the table below:

	Charge / Full Container
Investment in infrastructure	$37.56
Property costs	$24.33
Operating costs	$63.12
Total potential Landside Charge (average)	**$125.01**
Proposed Landside Charge (to apply from 1 March 2021)	
Export	$84.90
Import	$129.50
Weighted Average Charge	$112.50
Weighted Average Charge (prior year)	$110.00

Investment in Infrastructure

Patrick has made significant capital investment at East Swanson Dock, to the benefit of landside operations. This includes more recently the delivery of two new ZPMC cranes, four new straddle carriers and an upgrade to the Terminal Opearting System (TOS). In addition Patrick has committed approximately $20 million to an adjacent Rail Terminal at East Swanson Dock to support the Government's Port Rail Transformation Project. Patrick seeks to recover part of this investment through the landside charge.

Capital invested	$'m
Investment and Committed capital (allocated to landside)	111.1

An effective rate of return of 10% on the above investment has been applied to determine the required annual recovery. This equates to a potential recovery of **$37.56 per full container**.

Required annual charge (investment repayment model with 10% return)	13.7
Forecast full containers received per annum	365,000
Potential Landside charge relating to Investment in infrastructure	**$37.56**

Property costs

Patrick's property costs comprising rent payable to Port of Melbourne have increased significantly over the last 9 years. Patrick's total property costs at East Swanson Dock have increased by approximately 175% or the equivalent of 19.4% per annum every year for the last 9 years.

The privatisation of Port of Melbourne by the Victorian Government has led to a significant increase in land rents and property related costs which have considerably increased the costs of Patrick's operations. Patrick has been left with no option but to seek to partial recovery these significant increases in property costs through its Landside charge. Patrick had limited bargaining power in negotiating the lease terms.

If these annual operating costs were passed on via the Landside charge on a cost recovery basis only (i.e. no margin) it would justify a recovery of **$24.33 per full container**. Please note that this excludes rent on the Coode Road site which is currently subject to a rental abatement whilst the Rail Terminal is developed.

Property costs	$'m
Annual Property Costs	17.8
50% allocation to Landside charge recovery	8.9
Forecast full containers received per annum	365,000
Potential Landside charge relating Property costs (per full container)	**$24.33**

Annual Operating costs associated with the Landside Operations

Patrick incurs significant operational costs in servicing its landside operations. These costs are necessary to ensure efficient landside operations. If these annual operating costs were passed on via the Landside charge on a cost recovery basis only (i.e. no margin) it would justify a recovery of **$63.12 per full container**.

It is important to note that Patrick employs approximately 325 employees at its East Swanson Dock terminal with Labour Costs by far its largest cost of operation. In determining the Landside charge Patrick has only allocated Labour costs that specifically relate to servicing the Landside operations. Where labour cost increases have been taken into considerations for other ancillary charges these are dealt with independently, with these costs excluded from the Landside charge calculation.

Landside operating costs	$'m
Annual Landside operating costs	23.0
Forecast full containers received per annum	365,000
Potential Landside Charge relating to Landside operating costs (per full container)	**$63.12**

Unrecovered costs associated with the provision of Landside Services provided by Patrick

Further to the above, it is important to note that Patrick has historically absorbed a significant proportion of the costs associated with the provision of its landside service offering, and continues to only partially recover these costs. For the period from FY2012 to FY2020 using the above noted methodology Patrick has underecovered approximately **$140 million**.

Appendix B : Key Market Themes and Challenges

- **COVID-19 impacts** – Patrick has remained operational through the 'lockdown' period to ensure cargo continued to move into and out of the country. It has been a very disruptive period with a significant number of void (blank) sailings with reduced container volumes and challenges faced in managing the pandemic risks. The productivity of operations has been impacted by increased number of off window vessel arrivals resulting in increased yard congestion and loss of productive work hours resulting in overall loss of productivity. Patrick has increased its cleaning, sanitization and PPE costs to mitigate the risk. Patrick has received minimal to no financial relief or support from government or port landlords during the period. It is disappointing that monopoly landlords have not extended any rental relief given the challenges being faced by stevedores.

- **Negative Market Growth** – Negative market growth for the year, with negative market growth pre-COVID-19 of circa 4%, exacerbated by the COVID-19 pandemic with market growth dropping to circa negative 10% YoY, with potential for further deterioration. The soft market conditions have been aggravated further by the global shipping lines pricing pressure on Australian stevedores

- **Service Consolidation** – Following a wave of shipping line consolidation in prior years, the 2020 financial year saw an unprecedented level of service restructuring and consolidation with approximately 50% of Patrick's services changing across the year. This has led to significant renegotiation of contracts and terms with the shipping lines. Through this re-contracting period, Australian stevedores were exposed to the material increase in the bargaining power of global shipping lines with substantial market power - the top eight global shipping lines control close to 80% of global capacity. This has led to a further reduction in stevedoring rates with the ability of Australian stevedores to maintain contracted pricing levels decreasing further as shipping lines exercise their power over the market.

- **Vessel Upsizing** – Through this period of service restructuring and consolidation, the shipping lines have also changed the size and mix of vessels calling in Australia, with the global trend of upsizing to post-panamax vessels penetrating Australian trade. Of particular significance has been the impact on competitive market dynamics in Melbourne given the physical port constraints of Swanson Dock, which has created a monopoly market for certain larger vessels at VICT. VICT has used these service changes to quickly secure over 30% market share in Melbourne, to the detriment of long-standing operators Patrick and DPW. Vessel upsizing and service consolidations have and will continue to result in less service calls into and out of Australia and increased container exchanges, creating more pronounced peaks and troughs in operations. Vessel upsizing requires additional investment in operator capability, including larger cranes. Larger vessels result in significant operational savings for shipping lines. Larger vessels result in certain operational inefficiencies for terminals, particularly when combined with inflexible labour arrangements. Fewer shipping services coupled with capacity overhang has delivered lower stevedoring tariffs to shipping lines. A reduction in overall shipping capacity has seen prices for blue-water freight increase significantly (despite lower operating and stevedoring costs). Whilst shipping lines have deployed larger vessels and consolidated services, the overall volume of trade in/out of Australia does not necessarily require or warrant these larger vessels. The number of services calling Australia continues to decrease i.e. fewer / larger services.

- **Stevedores are price takers** – The combination of increasing shipping line power and excess capacity in the market means stevedores continue to be price takers and do not possess market power.

- **Fierce competition and excess capacity in market** – There is fierce rivalry amongst stevedores to secure volumes across a national platform. Delivering superior services for shipside and landside and record low returns for stevedores. There is significant excess capacity across all ports in Australia, which diminishes stevedore bargaining power. Excess capacity has been exacerbated with negative market growth in 2019/2020.

- **Port of Melbourne proposing to add further unrequired capacity** – PoM is proposing to increase import wharfage fees to fund its 'big ships strategy' with a significant part of the proposed investment to be funded by port users to remove the 'knuckle' at Webb Dock across 2021 to further upgrade VICT's terminal capacity. Removal of the knuckle at this time will exacerbate issues of excess terminal capacity, undermine effecitive competition between stevedores and lead to inefficient utilisation of Swanson Dock including the Port Rail Transformation Project. A reduction in volumes away from Swanson Dock will undermine the Government's rail strategy and lead to an inefficient use in rail capacity. The proposed investment is clearly nor prudent or efficient given the current state of the market.

- **Essential Services Commission findings** – In mid-October (shortly after Patrick extended its tenor at the Port of Melbourne until 2066), the Essential Services Commission (ESC) released their final report into the Port of Melbourne Market Rent Inquiry. Both the existence of PoM power in setting and reviewing rents and material detriment to Victorian consumers were found by the ESC. This behaviour noted by the ESC was consistent with Patrick's dealings with the Port of Melbourne. Similar deficiencies have been noted in the engagement to date in respect to the PoM Rebalancing application.

- **Low profitability for stevedores (even with infrastructure charges)** – Port privatisations have driven up rents and property related costs, this combined with increasing labour and energy costs, subdued market growth and fierce competition within the market has led to stubbornly low profitability for stevedores. The consequent decline in profitability has led to unsustainably low rates of return on investment. Although industry profitability increased slightly in 2019/2020, Patrick's profitability declined and still remains significantly below the required level to achieve a reasonable rate of return on investment.

- **Stevedores continue to invest in delivering new, upgraded capacity** – Enabling deployment of larger vessels by shipping lines and record productivity on shipside and landside. At East Swanson Dock, Patrick is investing approximately $20 million into Rail Development, in conjunction with the Port of Melbourne. In FY20 East Swanson Dock terminal received delivery of two new ZPMC cranes, 4 new straddles and upgraded its Terminal Operating IT System, further enhancing Patrick's capability and service delivery.

- **Improved access and superior outcomes for landside customers** – Competition and investment by stevedores has resulted in superior shipside and landside productivity. Access continues to be provided on a fair and non-discriminatory basis. Capital investment in terminal capacity and the physical interface between truck and terminal has delivered a superior service to the customer. Inability to recover costs from the landside will ultimately lead to sub-optimal investment behaviour and have a negative impact on supply chain efficiency.

- **Long history of investment under recovery** – Patrick has invested $880 million nationally in the last 6-years, improving the efficiency and effectiveness of supply chains, however Patrick has under recovered on this investment, with sub-optimal rates of return.

- **Declining overall supply chain costs** – Total supply chain costs have fallen. Synergies (expert supply chain consultant) estimates that the real costs of exporting to China have fallen by approximately 18%, and the costs of importing from China have reduced by 23% over the past 5-years. i.e. It is now cheaper than ever before to move a container from overseas to Sydney.

- **Stevedore charges are a small part of total supply chain costs** – Stevedores represent one link in a highly complex supply chain. Total charges levied by stevedores represents less than 6% of total supply chain costs.

- **All terminal charges are borne by the shipper** – All terminal charges are ultimately borne by the shipper. The shipper has influence over which terminal it ships its cargo through. Shippers supply chain costs have declined materially in recent years.

- **Industrial relations** – Patrick has been unable to reach agreement on a new Enterprise Agreement to date, with the current agreement now expired (from 30 June 2020). DPW and Hutchinson have been in negotiation with the Union across the year, and as we understand it have been unable to reach an agreement on a new Enterprise Agreement. The lack of industry-wide progress on agreeing new enterprise agreements can be partially attributed to the CFMMEU national agenda which has run a long-standing position on various threshold matters including prohibitions on automation, outsourcing of labour, recruitment decisions and an employer's right to manage its employees. For its 2020 enterprise agreement, Patrick is seeking terms that provide for the restoration of management discretion that would be considered ordinary in most workplaces facing similar challenges, including increased flexibility in the supply and deployment of labour, and the ability to pursue technological advancement without industrial barriers. Such changes are being strongly resisted by the MUA. To the contrary the MUA is seeking further reductions in flexibility and increased manning for status quo tasks. Further sustained industrial disruption, will contribute to a protracted period of suboptimal productivity, and economic harm from the resulting interruptions to Australia's supply chains. It is important that the incentives for stevedores to undertake future investments, and achieve further productivity gains, are not lost nor undermined by Australia's industrial framework.