

## Memorandum

29 May 2012

To: Peter Alsop, General Manager, New Zealand Productivity Commission  
From: David Moore, Director  
Re: Comment on international freight transport services inquiry

### Process of review

#### My terms of reference are to:

*“Undertake an evaluation of the Commission’s overall performance on the International Freight Transport Services inquiry, based on the final inquiry report, focusing particularly on;*

- 1. the relevance and materiality of the final inquiry report;*
- 2. the quality of analysis of information in the final inquiry report and the quality of the report’s findings and recommendations; and*
- 3. the effectiveness of the Commission’s engagement and delivery of message, as evidenced in the final inquiry report, summary report and “cut-to-the-chase” summary.”*

**The deliverable is to be ...** *“A report summarising the independent expert evaluation, in the key areas of scope above, which the Commission can publish or quote in reporting its performance (such as in any inquiry assessment the Board may publish, or in the Annual Report), and use to improve its performance.”*

I have been asked to report using the Commission’s draft indicator framework – this framework and my comments against it are set out in the summary statement overpage.

My process of review has been:

- detailed review of the final report
- high level review of the work in progress documents such as the draft report
- interviews with two Commissioners and with the Inquiry Director
- brief review of the Issues Paper and the Draft Final Paper.

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## **Summary statement (under the Commission's headings)**

### ***Right focus***

The final inquiry report meets the standard that I would expect for relevance and materiality of findings. The report restarts an important debate around the institutional structure and governance of ports, helps point the policy compass on issues related to the long-standing conference in sea freight and helps affirm the current (correct) practice in infrastructure planning. The report identifies and evidences a material fall in productivity improvement from the mid 1990's.

### ***Good process management***

The inquiry process is a robust and proven one. The process of progressively moving from issues identification to a draft view, and then to a final statement, is a proven process. The Commission kept to its promised timeframes. There is a clear expression of issues raised by stakeholders in the final report and, generally, a discussion of those views, particularly if the underlying logic or evidence is being challenged.

### ***High quality work***

The appropriate "lens" was applied to most of the issues. Taking into account the breadth of the issues, there was sufficient comment to follow the logic of the final views. There could, at times, have been a more explicit statement of options and a more formal weighing of costs and benefits. At times, the micro-economic analytical basis seemed to be "just enough", in some instances not quite enough. If I was to make a suggestion for the subsequent enquiries, it would be to move towards a more standard policy approach of problem identification, option analysis and recommendations to ensure that the full costs and benefits of any proposals are well worked through..

### ***Effective engagement***

I examined the stakeholders that were engaged. My feeling was that there was good engagement at a number of levels. First, departments were engaged in the process, which is important as they would then need to take up the mantle for change from the Commission. Secondly, clearly, the forums had been attended by the appropriate industry bodies. There were, however, fewer submissions than I would have expected and there was less engagement on some of the issue topics (e.g. from local government on port ownership and management).

### ***Clear delivery of message***

I found the report hard to read and hard to access. For me, the report starts on Page 272. I felt the need for a strong integrative chapter. I found sections of analysis in areas separate to the issue being discussed. I found decisions had been made implicitly about prioritisation of issues but could not find an overall statement of what and why issues were kept, disregarded, or treated lightly. I would be keen to see a more formal expression of the materiality of the different recommendations.

### ***Overall performance***

Overall, the document is useful and relevant. I found the Freight inquiry a difficult document to access but, in the end, I found my way through the issues presented and came away thinking that it was a good job of work with material and relevant recommendations that are likely to have a durable effect. I found

the thematic chapters from Chapter 6 on highly interesting and recommend starting the report with those thematic chapters and then working back to earlier background and context setting sections.

### **More detailed comment**

**I presented the Commission with a less formal statement of issues and themes as well as some detailed feedback. I have not revised this material for an external audience. However, I have retained it as a record for the Commission.**

### **Organisation context – building the organization while drafting**

This is the first inquiry of the Commission undertaken contemporaneously with the inquiry on affordable housing. The interviews emphasized that the Commission and consequently the Inquiry team capacity and capability was being developed at the same time that the Inquiry was underway. As a result, in the background of the reports, there is a tale to tell about recruitment of staff, interactions with external advisors, developing relationships with the project team and with Commissioners, and development of the “brand” (purpose, presentation, analytical content) of the institution. I do not touch on these points as they are outside the brief but I do acknowledge the environment in which the Commission developed these first two Inquiry reports.

Without doubt, it is a considerable achievement to get a report out with the breadth of this particular report - under any circumstance. For the organisation at its current stage of development, the task of generating a 300 page report was clearly “like climbing a mountain”.

In future, the job will get easier; quality will improve, processes of analysis and report writing will become more natural, processes of inquiry management will develop and mature, as will the experience of the staff. In short, the productivity of the Commission will improve and these and other reports will become both easier to produce and will be of higher quality. I therefore make a number of detail comments that I would not expect to be making of Commission’s reports in, for instance, one year’s time.

### **The Inquiry is relevant to the productivity debate and offers material content**

The review of Freight inquiry traverses solid “middle ground” for productivity studies. My first question was, therefore, whether it sufficiently show-cased a productivity study of this nature. My feeling is that, yes, it did so. It demonstrated a clear focus on efficiency. It gathered sufficient evidence to justify that there was a productivity problem. And it presented a clear set of issues and possible responses. In short, it achieved its ostensible objective, of indicating where there could be regulatory or institutional changes that would enhance productivity.

It was important to do so because, by doing so, it achieves what to my mind is the primary purpose of the first two Inquiries, of stating the usefulness of an institution such as the Productivity Commission and establishing its place and role in the identification, analysis and recommendations for change of long standing important productivity issues. To my eye, there is no other public sector body which could undertake this study, in this way, or that could come up with the process and recommendations that might lead to progress in the area under inquiry.

The report is essentially an inception report; there is a great deal more time spent explaining the economic “lens” that is being brought to bear on each subject. One Commissioner indicated that this is partly deliberate to lay a trail for future reports. To me, it felt like the report was being used to showcase the type of thinking that I would expect of a Productivity Commission. The absence of a labour market framework and adoption of an industrial relationship framework therefore stood out (Chapter 6).

More directly, there are a number of major contributions. For me, the main areas are:

- highlighting the lack of productivity growth over the last decade and the need for that productivity growth;
- surfacing the issues around sea freight and the processes used in an era when there was much less trade – these issues have been known as long as there has been a transport section in the Treasury – but they tend to be forgotten; and
- addressing the institutional issues around port management which is possibly a root cause of the industrial situation that the Port of Auckland finds itself in.

Also, the report nicely silenced one contentious area in an authoritative manner, being the central planning debate, relegates other issues such as input regulation of airports and associated disclosure regimes to the agencies that appropriately dealing with them. Other issues are put in context and put on notice (border management) or identified for others to deal with (airport queuing issues).

I am less convinced of the section around the RMA and identified that the drafting was driven by a concern about the manner in which the Environment court thinks about trade-offs versus environmental bottom-lines.

***The quality of analysis of information in the final inquiry report and the quality of the report's findings and recommendations – good with room to improve***

The study scope is very broad. There are a cluster of major topics covered and the question is whether the topics were touched on too lightly. For instance, there are issues of sea freight competition, cabotage, border management, air freight, port infrastructure and adequacy of ownership, etc. This breadth is a double edged sword. On the one hand, it allowed the Commission to look simultaneously at a number of issues and to draw out the landscape of the transport issues. On the other hand, the breadth clearly stretched the capacity of the team to follow through on all issues to the level of detail that is found in Australian productivity reports. Would it have been better to position the Commission more explicitly for a stream of work rather than attempting to cover all issues at once?

If not, and if landscape reports are to be a product line for the Commission, then there needs to be more discipline around the presentation of the analysis. The analysis needs to be described in a way that is replicable and that can be evidenced. I did not always find this to be the case; the work may have been undertaken, but it did not make it into the report.

Following overpage are the issues that I identified.

**1. Relative materiality of recommendations**

The report does not distinguish between the relative materiality of its various recommendations until page 272 and then does not express them in a way that I can tell how important they are. I thought that this was an opportunity lost – it felt to me that the conclusions might be important. It's not clear which offer the highest net benefit (where are the biggest gains) or are the most critical. I also wasn't clear how the recommendations fit together as a whole package or whether the recommendations are independent of each other (e.g. NPS with investment co-ordination and planning recommendations).

Related to this, is a lack of evidence of the manifestation/size of the problems at the component or "theme" level (there is for the need to take action), and of the likely costs and benefits of the options considered and preferred. For example the recommendation that a registration scheme

should be implemented – there is no discussion of the costs of this (p.238). Ditto the recommendation regarding the Commerce Act (recommendation 12.2), which would impose costs on applicants; I assume that there was a weighing of costs and benefits but that is not clear from the report.

I would also liked to have known more about the materiality and importance of freight to different sorts of firms. For instance, what does the report mean for a Kiwifruit orchardist, for a manufacturer of advanced manufactures, etc. For me, there was an opportunity to demonstrate effects of status quo, and of the proposed changes, through case studies. Case studies are mentioned but then are not used.

I thought that there was a possible metric that the Commission mentioned and could have developed further. The Commission identifies the impact of distance from market on competitiveness of products by relating it to the effect of a tariff. If, for instance, port ownership and governance was improved, how much would be be reducing the “tariff” and what implications would it have for the Kiwifruit orchardist or for, for instance, a Scott Technology (which exports 90% of its production, to around 80-90 countries).

My major concern was that there was no “proof of the pudding” - how will the world be different. There is reference to the need for better monitoring, but no “punt” on whether this would make a difference, or not. I was left wondering how I would know that the world was going to be better – particularly if the Ministry of Transport did not take up the mantle left it by the Productivity Commission and repeat the analysis in several years. I think that setting out the bones of a monitoring framework on material issues could be important. I found it difficult to get an explicit statement about proportionality of issues presented and, also, the likelihood that following any of the recommendations might lead to material change.

Another way of doing showing important effects may be to set out how you would like to see the world different in, say, 5 years.

## **2. Further industry analysis and scenario forecasting?**

I also wondered what the future outlook is for the transport sector, in the absence of further intervention. I appreciate the difficulty around forecasting, but even some scenarios would have been interesting. Also, some sort of environmental scan – what are the big issues looming – for NZ and the sector worldwide – that will need to be dealt with? My concern was the depth and breadth of the transport system analysis. Gaps that I would have liked addressed would have been something around long-range forecasting for freight volumes and modes, forecasting of technical change, possible scenarios, changing freight mix. In short, I would have liked to have known more about the transport industry.

## **3. Need for a strong integrative chapter**

I felt that the most important messages were a gestalt from the introductory analysis (the hole in productivity growth), the institutional analysis and comment on competition effects/ labour market dynamics, and a discussion on dynamic efficiency that comes on page 143. I personally felt that the combination of these might possibly be the bones of a strong integrative chapter. I have classified this as an analytical issue rather than a presentation issue because, I think, other than the snappy few pages on page 272, I am not sure that the whole of the picture has been drawn together.

### **Scope too large?**

I felt that there was a trade off in terms of breadth and depth of material. I felt that some issues were dealt with too lightly. For instance, in the EVA analysis, I could not easily tell how big a problem the mismanagement of ports was without additional information. I would look for a simple summary table (like a prospectus) showing a summary financial and operating statistics – turnover, EBITDA, fixed asset value – and possibly some through put statistics. I felt that this additional information was needed given the CTU's appropriate challenge ( and the Commission's appropriate response) to the application of the methodology. Similarly, I would seek additional information in the important Chapter 6 on Improving workplace productivity. For instance, taking into account the delicate situation that the Commission found itself in, with a major dispute in the Ports of Auckland, it would still have been possible to write a focussed case study on the positive work changes in the Port of Tauranga.

I wonder if, psychologically, it may have been better to have a short integrative paper and longer and more separable papers on the thematic issues. The thematic issues could follow a more straightforward structure of - background, issues, analysis, comment and reflection, findings and recommendations. Further, words were used without the accompanying statistic (e.g . on page 143, “volumes will substantially increase”, made me go looking for the forecast, but I could not find it, as well as the later assertion about scenarios where port capacity may not be a problem if productivity increases).

### **Costs benefits and options more fully debated?**

I thought that the costs and benefits of recommendations could be more fully debated; this was particularly poor for the RMA chapter e.g. what is the evidence that s.5 is a problem – what impacts is it having? Likewise, I wasn't sure that all options were reviewed in the manner that options for co-ordination and planning were explored. This option analysis may have been undertaken somewhere else but it would have been good to have it in the paper.

I was a bit surprised that there was, in general, a lack of evidence from overseas regarding costs and benefits of options. I was left wondering what other countries do, and do they have similar problems? It may be that the NZ context is so unique that initiatives/measures employed in other jurisdictions are not comparable, but this is not explained. The exceptions are chapters 10 and 11 which do cite international examples (though I was left wondering what the outcomes from the privatisation in Queensland have been).

### **Report structure and presentation – thematic chapters work but more need for signposting and closer attention to structure**

There are clear decisions about prioritisation of effort implicit in the document that I would prefer be explicit. For instance, there is a decision to focus on the competition effects that might reveal price effects on containers, and there is a decision to focus more on shipping than on air, and a decision to focus on the main ports rather than the 14 referenced on page 107. The prioritization of effort decisions appear to be the right ones – there is less that can be done about bulk shipping or reefers (tends to be point to point or on commission), air is a relatively small component of traffic and it is not clear to me that a lot of time should be spent on, for instance, the Port of Timaru. I would find it more helpful to have these prioritisation decisions stated in a process or context section at the start. In another example, on page 106, there is reference to a decision that the Commission took in terms of narrowing its focus. This decision should be located with other decisions, somewhere close to the front of the document.

I found some of the report “lego blocks” were out of place. For instance, the EVA analysis is a useful piece of work. But it needs to be more closely associated with the institutional analysis; in fact, it is the major evidence for the lack of transparency and the mixed ownership incentives that may be the root cause of the drop off in gains in port productivity. Likewise, there is comment on the framework for the Commissions analysis, but then a series of alternative economic lens applied through different chapters. The section following the framework analysis is the start of something quite different; a review of supply and demand features. I found the conclusions on page 272. Another example is on p.193, finding 10.2 – while this seems reasonable and even obvious, there is no evidence provided for this actually creating a problem at the moment without clear reference to the EVA work, and a further link between the implications of the EVA work and implications for investment, and therefore for productivity enhancement.

I have a suggestion for how a report as complex as this one could be presented. I was not convinced that transport was a system so much as an important input to other systems (as the report notes, derived demand). The term system is used early on the report but then is not then used to unify the report; I suspect the report could have been written without that paragraph referencing transport as a system. I think, in future, where there is an important intermediate activity such as transport under inquiry, that it could be important to show the effects of marginal changes in terms of firm level activity and the cost and production functions describe wealth generating firms. Thus, for instance, where there is reference to quotes for shipping rates to a range of ports in the Inquiry report, I feel there needs to be a framework that takes firm level case studies, takes those quotes, and amplifies the results, which would give some indication of proportionality and materiality of proposed changes and effects. This firm level focus could provide a unifying framework for the report as a whole.

I struggled with the sign posting in the report. For instance, on page 108, I was referred chapters 8, 10, 6, 13 (three times). Likewise, in table 8.2, I am referred to Chapters 9, 13, 11, 10, 7 and section 8.4, sometimes several times. Apart from anything else, this must create a large proof reading issue in the production of the document.

I felt that the connection between problem analysis, discussion of consultation material and response was an excellent approach. If you do this, as the Australians do where the product is an inquiry, there is a need to be clear why views/evidence from submitters has been dismissed/rejected or one option favoured over another. Having said that, from time to time, I felt the need to take up a pen and write a little bit more. In particular, in the context around recommendation 10.7 which seems to dismiss a submitter’s statement that overseas models may not work in NZ (p.222). I am not sure this recommendation is well supported by the evidence presented in the report. Ditto finding 11.5 (p.235). All that being said, the process of review – from issues paper to draft to final means that there is a strong impression that submitters have been listened to.

The inquiry looks to have engaged with a large number of interested/affected stakeholders but a question whether it engaged with enough (possibly enough for the purpose but not enough on each specific issue). Without seeing the submissions themselves, the various views appear to have been impartially reflected in the report. The Commission has explained why they have stuck to their guns on a number of points; other recommendations have been adjusted in light of feedback. This is transparent generally; however, talking with one of the Commissioners, I think that there was more impetus to the need to write about the RMA than is written in the document. I personally feel that all material elements in the Commission’s “lay lines” need to be recorded.

There are various levels of summaries, to appeal to different groups of reader. The writing is generally clear. The glossary is helpful.

## **Chapter specific comment**

I will comment on each chapter in turn ending at the start of the last recommendation chapter as the most important chapters appear to be the last chapters. And I will do so from the back of the document forwards.

- Appendices, if you are going to have them, then include them. I went looking for them and decided to not waste my time. I understand that there was a hiccup in the timing of getting them on to the website but I personally would prefer to see the Appendices published with the Inquiry report.
- Engagement meetings, for the size of the enquiry, there was not enough engagement – for instance, there is an engagement meeting with Local Government NZ but not with, for instance, the super city, or the other cities that sit within the so-called transport “golden triangle”.
- Chapter 14: Key insights and action points – is the best chapter of all with the key notes from the report emerging on page 272 - although my comments on materiality, etc are concerns for me.
- Chapter 13: Other regulatory issues – could be left out and I am not sure that anyone would notice.
- Chapter 12: Regulation of international air freight services – appropriately at the back given the other issues raised.
- Chapter 11: Regulation of international sea freight competition – I felt that this was a complex chapter with appropriate recommendations but the evidence for the recommendations lies elsewhere in the document.
- Chapter 10: Governance and ownership – will sponsor strong debate and issues identified needed to be set out – I was pleased to see it covered off – a minor issue that I think that there needs to be an unbundling of governance issues and ownership issues. Some of the discussion related to market failures is a bit tangled e.g. in the governance and ownership chapter.
- Chapter 9: Investment coordination and planning – I found the chapter on investment co-ordination and planning particularly murky and disjointed. But it does enough to pull teeth on an important issue – I liked the way that this chapter challenged some urban myths – I was less convinced that the case studies were case studies – or just issues posed.
- Chapter 8: Encouraging efficient investment and innovation – I tripped up over the title and preferred the subtitle in 8.1 – and found myself wondering why dynamic efficiency did not feature in the framework discussion in the Commission’s expression of primary purpose; namely efficiency.
- Chapter 7: Customs, security and biosecurity - does not come up with any recommendations – but I felt that it was a very strong chapter – with a clear expectation of improvement and change.
- Chapter 6: Improving workplace productivity - , as related above, I understand why an industrial relations approach is taken. With the context of the interviews, the section is deliberately poised to encourage debate, but I would be keen to get more detail around work practices. I would have been interesting in knowing how much of port (and sector) labour force is unionised. Finally, as an semiformed thought on ports, is there some sort of club good angle to port assets?

## **Detail notes from the early part of the document – turn the document on its head to aid accessibility**

I provided my detail notes to the Commission to assist with identifying why the front end of the document is a difficult read. I had expected to be gripped by the document but needed to start at a random part of the document and then work out rather than reading in a linear fashion. I then decided to start at the beginning and record some of my dialogue.. My conclusion is that, in fact, the document could be “turned on its head” (started from page 272), re-sorted and, without much effort, could deliver a much more straight forward message.

Approximate margin notes (a sample):

- The glossary is useful. There are particular words there that are useful to know, such as “cabotage”. I have not heard that word used for some 20 years. It might be useful to think about splitting the document into two parts – one part dealing with industry specific language (“TEU”) and the other dealing with standard economic terms (“externality”) – to help to cut to the chase.
- Figure 0.2 is a diagram trying to say a lot and not quite succeeding. On inspection, it raises more questions than it answers, or that it clarifies. I would have been tempted to separate out the components of the main freight routes and show their materiality (in what context) and then move to looking at issues separately. The description of the chart also introduces a competition policy lens. This may or may not be the right lens, and a more set of themes (rather than a single lens) then emerge through the paper (eg. issues of ownership incentives, regulatory issues, etc) while the competition lens is kept at a relatively high level (e.g. does not get into market segments).
- Page 4 notes use of case studies. These will be useful. I would go looking for them in the document.
- The report has a large span of issues. The sea freight issue is touched on in two bullet points on page 4 and 5. But then, rather than drilling down into the issue, the next bullet point is about airfreight – is this an issue with the span of the topic generally. On shore costs look competitive but the issue seems to be around costs of getting to and from NZ.
- On page 6, there is a good discussion of ratemaking and non-ratemaking agreements. The discussion about the market segments is, however, a bit weak. Are we only concerned about containers? Or what are we concerned about? For myself, I would need to dig into the document beyond the executive summary to find out.
- The executive summary raises the questions about ports and indirect costs such as delay. The four main ways of improving port performance are listed and I note that one of them “more productive workplace relationships” is the subject of a very major dispute in Auckland. I think that it might have been useful for the executive summary to note the current context of some of these issues such as maritime seaworthiness issues (are they included or excluded?) and comment on a matter that lies before the employment court. (Pg. 7).
- There is much more detail around governance and ownership of ports – possibly because it is a topic that we are so familiar with. However, the question is whether we can afford to support a network of 16 ports, all with a main highway running down to them, or not? And how does that play out in terms of, on the one hand, port efficiency and, on the other, systems resilience. Are these issues all linked with the state owned enterprise / COE issues that we have been playing with for 25 years, with the labour market issues, or are they separable? I will go digging for further insight. Pg.8/9. The discussion on suggestions of an IPO for ports is one way to go – a trade sale is another – and if the EVA is negative then it could be a better way to go, if councils were willing to let explicit subsidies become apparent.
- Again, on page 11, the issue of rail, road freight, changes in truck loadings etc. Again, this feels like another report. On the top of page 13, it is clearly signaled as another report. Good. There is too much here already.
- On page 12, would it have been possible to come to such a solid view on border management issues in the space of the time for the report?
- A question of scope of the report – the air freight, at page 10, feels like a sideline – but could be an entire report. I am not sure that the summary comments do it justice. I am not sure that, in some market segments, that air freight would be seen as a sideline or a by product! Eg, in inshore fisheries, where high value fish such as Tuna is delivered overnight, or in high value flowers, usually going to Asian markets.

- I appreciate the paucity of useful data, and note the limits this places on the analysis. For example, much of the statistical analysis in early chapters looks at figures for containers, which comprise only 30% of the total weight (though I'm not sure how much of the value). The report recognises the need for non-container measures.
- With respect to figure 1.3, I wondered if this is partly due to NZ coming off a relatively high base? Understanding this trend is critical to the findings that NZ's growth is lagging behind (and that there is a problem).

END

