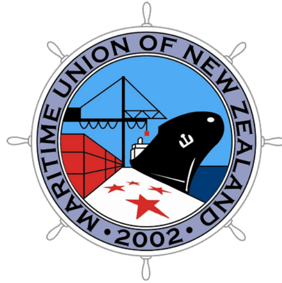

The costs and risks of privatising Ports of Auckland operations

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Executive summary

Privatising the operations of Ports of Auckland would result in increased costs of at least $70m a year to New Zealand businesses to meet the investor's return on equity.

Privatised port operations in Australia saw surcharges of over $100AUD a container imposed on users, who have no other options.

The failed automation experiment shows there is no fat to be cut at the Port, a private operator's extra profit would come from the Port's business customers, who could expect similar increases in container charges as seen in Australia.

In late 2022, rumours began to be reported that offshore firms DP World (ultimately owned by Dubai's ruling royal family) and Caisse de dépôt et placement du Québec (the Quebec public pension fund) were interested in acquiring an operator lease over Ports of Auckland.[1]

At the time, Auckland Mayor Wayne Brown categorically ruled out such a move stating: "There are no circumstances in which the Auckland Council Governing Body would ever agree to sell the port land or enter into a lease agreement that would lock it into used-car and container port operations for decades – and it is well known I am utterly opposed as Mayor."[2]

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1 https://www.nzherald.co.nz/nz/dubai-company-eyeing-takeover-and-lease-of-ports-of-auckland-business/NI2A3EYVKLVGLUZCAGJ22FLSKY/
2 https://ourauckland.aucklandcouncil.govt.nz/news/2022/10/mayor-says-no-to-long-term-port-operator-lease/

However, Mayor Brown quickly reversed his stance. In March 2023, it was revealed that the mayor's office was funding a three-part review of options for the future of Ports of Auckland, including commissioning Australian firm Flagstaff Consulting to "seek expressions of interest from investors or port operators" for involvement in running the Port, including a possible sale or lease of the operating rights.[3]

This report estimates the costs of privatising port operations by conservatively calculating the return that the private operator would need to generate in addition to the minimum rent that Auckland Council would require to make the deal economic compared to alternatives such as borrowing.

Privatising Ports of Auckland's operations would increase costs to the businesses that use the Port by at least $70m a year, and possibly much more. Put simply, if the Council tries to avoid low-interest debt by selling part of the Port's profit stream to a private operator, the Port will need to generate higher profits to meet that investor's return on capital.

Privatisation advocates have pointed to Ports of Auckland's low profitability in recent years as a reason for reform. This analysis fails on two grounds.

It is a mistake to view Ports of Auckland solely through the lens of its financial performance

Firstly, Ports of Auckland has been a reasonably profitable and, more importantly, a highly efficient port in the past. The reason profitability fell in recent years was the failed attempt at reform through automation; an attempt to increase profits and decrease labour costs, which ended up consuming hundreds of millions of dollars of capital investment, crippled the Port's throughput, and slashed dividends to the Council. This project has since been abandoned and the port efficiency is increasing. The failure of one experiment is not justification for another.

Secondly, it is a mistake to view Ports of Auckland solely through the lens of its financial performance. Ports of Auckland is a strategic infrastructure that operates as an effective

monopoly. As such, its principal economic role is not to maximise profit but to enable New Zealand businesses to trade, making profit by importing and exporting goods, and moving goods around the country. The Port should cover its costs however, delivering a commercial rate of return for a multinational private port operator that can only come at the expense of increased costs for New Zealand businesses and the broader economy.

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3 https://www.stuff.co.nz/national/politics/local-government/131601064/wayne-brown-launches-new-review-of-aucklands-port-future

Privatisation of Ports of Auckland's operations would mean more profits for the port operator, who would generate higher income by imposing greater costs on Auckland businesses to use the Port, while cutting labour costs, and underinvesting in infrastructure.

International experience of port operations privatisation and New Zealand's own experience with privatisation of other strategic infrastructure provide salutary lessons. Privatising the Port's operations would lead to higher costs for port customers through the exercise of market power, reduced accountability, under-investment in infrastructure, and the risk of a private investor using its political power as controller of a strategic asset to renegotiate more favourable terms for itself - and worse for Aucklanders.

A private port operator would have a strong financial interest in opposing capacity expansion at other ports, such as Northport, and could use its political power to try to stymie such investment.

Privatisation is a seductive option for a Council looking for quick cash, but it is Auckland that will pay in the long run. As the recent Australian experience has demonstrated, moving from a low-profit port model, which covers the public owner's cost of capital while enabling trade, to a private equity model focused on maximising profit for an offshore investor inevitably drives up costs for businesses and causes regional, and national, economic harm.

New Zealand has experimented with privatisation in the past. Despite promises that competition and regulation would ensure that owners of privatised monopolies don't abuse their market power, they do, time and again. The only effective tool for ensuring that core public infrastructure is managed in the public interest is public ownership.

This is a well-worn path, strewn with the costly, failed privatisations of the past; we do not need to walk it to know where it leads.

Note: at the time of publishing the mayor's office released uncosted plans for waterfront development that included repurposing non-container port land and/or reducing wharf space. While this is not taken into account in the following figures it should be noted that non-container cargo (multi-cargo) makes up more than 20% of the Port's revenue. Removing these operations would devalue the return on the sale of port operations and/or require a potential private operator to increase freight container cost by more than the modelled amount to offset the loss of this income stream.

Background

The Port's role

Ports of Auckland is a vital transport infrastructure. Every day, an average of $100m worth of cargo flows through the Port. The lion's share of this is imports that supply Auckland businesses - everything from cars to clothing, computers to food. 60% of New Zealand's roll-on, roll-off vehicle imports and 25% of its containerised cargo goes through Ports of Auckland.

It is also effectively a monopoly and likely to continue to maintain that status for some time due to the closest major ports being at or near capacity with little likelihood of significant expansion in the near future, and because of the lack of resilience of road and rail connections between these ports and Auckland city. The addition of a second port in Auckland, such as an expansion of Manakau port, is also unlikely given the planning and capital barriers such a project would face.

While the Port is operated on a commercial basis and the Council expects it to cover its operating costs, and the Council's opportunity cost of asset ownership, its primary purpose is to enable the transport of goods so that the wider economy can flourish.

Transport infrastructure, at its best, serves to facilitate trade while imposing low costs. It is the advent of low-cost transport that has enabled much of the growth of the global economy in the past two centuries. In particular, it has enabled the New Zealand economy

to grow to developed world status, despite our distance from trade partners. The timely, affordable, and reliable flow of trade through the Port is absolutely essential to Auckland businesses and the broader economy.

A port, like any piece of strategic infrastructure, works optimally when its focus is on enabling the economic success of its customers, rather than on maximising its own profit. If a port seeks to maximise profit and uses its market power to do so, it becomes a trade barrier, effectively functioning as a tax on trade that leaves the economy as a whole worse off.

The push for Port privatisation

Partial privatisation of the Port has been suggested as a way to make the Port more profitable and to free up capital for Auckland Council.

The new push for privatisation follows hard on the heels of the failed automation project, which itself followed the failed attempt to deunionise the Port through "competitive stevedoring" in the early 2010s. Each of these ideas have been pushed under the guise of efficiency and profitability, which have, in fact, relied on cutting employees' pay and conditions.

None of these previous moves have succeeded and, in actuality, came at a large cost to Auckland businesses, through lockouts and strikes during the deunionisation attempt and through slow throughput and safety incidents during the automation project. Projects that were supposed to be more efficient and profitable actually made it slower, less reliable, and more costly for customers.

In late 2022, rumours began circulating in businesses circles that offshore state-run equity firms Dubai World (through its DP World arm) and Caisse de dépôt et placement du Québec (the Quebec public pension fund) were interested in acquiring an operator lease over Ports of Auckland. [4]

At the time, Auckland Mayor Wayne Brown categorically ruled out selling or leasing the Port in any form. Brown said: "There are no circumstances in which the Auckland Council Governing Body would ever agree to sell the port land or enter into a lease agreement that would lock it into used-car and container port operations for decades – and it is well known I am utterly opposed as Mayor."[5] A long-term proponent of moving Ports of Auckland's operations to Northport, Mayor Brown initially pushed for the Port land to be, at least partially, returned to the Council to be converted for other purposes, as Wynward Quarter has been. That idea, though, has been, in part, shelved.

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4 https://www.nzherald.co.nz/nz/dubai-company-eyeing-takeover-and-lease-of-ports-of-auckland-business/NI2A3EYVKLVGLUZCAGJ22FLSKY/

5 https://ourauckland.aucklandcouncil.govt.nz/news/2022/10/mayor-says-no-to-long-term-port-operator-lease/

Since then, Mayor Brown's view has changed. The reasoning for this change has not been provided, but Brown now appears open to a privatisation of the Port's operations, which would give the Council an up-front cash boost in return for losing future dividends. This bears strong similarities to the partial sale of the Council's Auckland Airport shares, which Mayor Brown recently received majority support in the Council to implement: reduced control over a strategic piece of transport infrastructure and reduced future dividends, in return for money up front.

It has been reported that DP World has offered a billion dollars and an ongoing annual lease payment for the right to run the Port operations. It is also understood that DP World's proposal would include looking to close down some Port operations and return land to the Council for development, which would also accord with Mayor Brown's desire to close as much of the Port as possible and move its operations to Northport.

The Mayor's Office has commissioned a three-part review into the issue and is looking at a model that would see the operations of the Port sold. The review includes work by Australian firm Flagstaff Consulting to "seek expressions of interest from investors or port operators" for involvement in running the Port, including a possible sale or lease of the operating rights.[6]

The Port's profitability

The push for privatisation assumes that the Port is underperforming and that higher profitability is desirable, however, analysis of the port's role in the context of the Auckland economy indicates otherwise.

Analysts TDB Advisory Ltd have suggested a partially privatised model, whether through joining public-private ownership of the asset or through public ownership of the asset with operations leased to a private operator, would increase the profit levels.[7]

This analysis contains two critical flaws.

The first flaw is that it compares the profitability of Ports of Auckland to other New Zealand ports during Ports of Auckland's disastrous automation experiment, which resulted in lower throughput, higher costs, and reduced profitability.

Prior to the automation experiment, Ports of Auckland was posting profits averaging $70m a year and was rated the best container port in Oceania, with high throughput. It was making a modest return for the Council but, more importantly, it was providing a reliable and affordable service for businesses moving goods in and out of Auckland.

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6 *https://www.stuff.co.nz/national/politics/local-government/131601064/wayne-brown-launches-new-review-of-aucklands-port-future*

7 *https://www.tdb.co.nz/wp-content/uploads/2023/04/TDB-Ports-A-Comparison-of-Mixed-and-Government-Ownership.pdf*

From 2018, profitability collapsed as automation costs rose and throughput declined as the automated straddle cranes failed to deliver on their promise. While the former Port leadership promised lower costs, greater capacity, and more productivity, the reality was exactly as has been found in other countries - automation does not move more cargo faster. In fact, cargo moved slower, congestion choked the Port, ships were forced to divert to other ports and shippers and trucking companies imposed congestion charges on port users.

In 2022 that failed automation project was shelved and losses written off. Little more than a year later, Ports of Auckland is targeting a $52m net profit and $35m dividend in the 2023/24 financial year, with a 5.1% return on equity (net profit after tax).[8] This equates to just over $1.50 of profit for every $1,000 worth of cargo that the port handles. This is projected to rise to a net profit of $70m and return on equity of 6.6% in 2025/26.

The second flaw in TDB's analysis is the assumption that maximising profitability is a desirable outcome for the Port. This ignores the Port's value as an enabler of business and the economy. At a regional economy level—the level at which any council should be focusing its decision-making—Port profits are effectively a tax on trade. While it is reasonable for the Council to make a modest return on its asset, changing to a private model that makes profit the sole aim of the Port would mean higher port charges for customers, that would flow through into higher prices throughout the economy.

Maximised profits for the Port would come at the expense of the businesses and economy it serves.

Profit does not appear by magic. In the case of a mature piece of monopoly infrastructure like the Port (which has just gone through a failed experiment in lowering labour costs through automation), extra profits come from higher charges on customers. Maximised profits for the Port would come at the expense of the businesses and economy it serves.

8 https://www.poal.co.nz/about-us/Documents/Ports%20of%20Auckland%20DRAFT%20SCI%20FY24%20to%20FY26%20-%20amended.pdf

The impacts of privatising the Port

What a private operator model would mean in practise

Ports of Auckland has a simple, relatively cost-effective structure whereby Ports of Auckland employs or contracts the staff who load and unload vessels and move goods on the Port.

In a privatised model, the Council would retain ownership of the land, likely through a holding company. The port operator company would own the right to manage the operations at the Port in return for a payment to the Council, which could be a one-off or a series of lease payments, or a combination of both. The port operator would likely be responsible for the construction and maintenance of infrastructure on the Port.

It is possible that the current management and board, Ports of Auckland Limited, would remain in place. The new operator would slot in between Ports of Auckland, which runs the Port day-to-day, and Auckland Council, which would own the land. This new layer of management would be primarily concerned with ensuring that the private investor parent company recoups its investment and, so, would be focused on minimising costs on the Port and maximising revenue.

In Australia, getting the price right in these port operation privatisation deals has proven notoriously difficult. If the port operator pays too much, it has to force charges up to recoup its investment. If the deal is too low, the port owner rapidly finds its foregone profits outstrip the money it receives on the deal.

Estimating the costs of a sale to Port customers

It is understood that DP World's offer to the council is similar to the arrangements it has to operate in Australia where it is one of two companies (the other being Patrick's), which contract with port landowners to run port operations. Known in Australia as 'stevedoring companies', the port operators pay an up-front price to the port owner as well as an annual lease.

It is understood that DP World has offered a billion dollars for the initial payment for the Ports of Auckland operating lease over a 15-45-year period, along with an annual lease. Using this figure, and information from DP World, Ports of Auckland, and Council financial documents, it is possible to estimate the shape of a deal.

From the port operator's perspective, it needs to make a return on its capital investment and recoup that investment over the course of the investment period.

Private port operators tend to operate on relatively high margins compared to the cost of

council borrowing. For instance, DP World's earnings before interest and tax in 2022 were 8% on its capital employed, and it made similar returns on average over the past decade. [9] DP World noted that it expected its return on capital employed to grow higher than 8% in the future. DP World's EBITDA margin—essentially, operating profit as a percentage of revenue—is over 30%, including a 33.6% margin on its Australian and American operations in 2022.[10]

That means a private operator like DP World would have to generate significant additional revenue to earn the profits that would be needed for the investment to stack up.

We can calculate the impacts of a scenario where the private port operator pays a billion dollars for a lease for a standard 15-year period, putting aside any commitments to make investments or release land to the Council. In this scenario, the private port operator would need to realise net dividends of $115m a year to both make an 8% return on the billion-dollar investment and gradually release that billion-dollar capital investment over the course of the lease.

On top of that, the port operator would need to pay an annual rent to the Council.

Auckland Council would logically not sell the right to profits from the Port for a price that works out to less than the interest rate on its borrowing (selling the Port profit stream can be seen as equivalent to borrowing the money and paying for it with foregone profits, rather than interest). The lease would be not perpetual, so there would be value to the Council in still having the billion dollars once the lease has expired and the Council regains the Port's full profit stream but, offsetting that, the Council should also price in the loss of control and the added complexity that the arrangement entails compared to borrowing. Netting these factors out, the Council's borrowing cost serves as a good indicator of how much profit it would be willing to sell for a billion dollars. Conservatively, with the Council's forecast average borrowing cost at 4.6% according to its latest Budget (which is also similar to its average borrowing cost over the past decade),[11] it would not make sense for the Council to part with any more than $46m a year in profit from the Port in return for a billion dollars.

Ports of Auckland forecasts its profits will rise to $60m in 2024/25 and $70m in 2025/26.[12] Projecting profit growth of 4% per year, in line with the Port's revenue growth forecasts, the Port would return an average annual profit of $95m over the 15 years starting in 2025/26.[13] Therefore, the Council would need an annual rent of at least $50m a year to not be financially worse off in terms of foregone profits compared to the alternative scenario

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9 *https://www.dpworld.com/-/media/project/dpwg/dpwg-tenant/corporate/global/media-files/investor-relations/financials-and-presentation/financial-reports/financial-results/2022/2022_08_18_dp-world-1h-2022-interim-results-presentation.pdf?rev=69c5306432e34bbabf844496bb8bb50f*

10 ibid

11 *https://www.aucklandcouncil.govt.nz/externalcontentdelivery/consultations/budgets/annual-budget-2023-2024/annual-budget-2023-2024-supporting-information.pdf*

12 *https://www.poal.co.nz/about-us/Documents/Ports%20of%20Auckland%20DRAFT%20SCI%20FY24%20to%20FY26%20-%20amended.pdf*

13 The assumed rate of profit growth does not affect the additional revenue that would be needed as a result of the modelled sale - that is driven solely by the private port operator's need for returns compared to the Council's cost of borrowing.

of more debt - and should charge more to cover its other costs associated with a lease arrangement.

Put together, this means the Port would need to generate profits of $165m a year to cover both the $115m return for the port operator and the $50m rent to the Council. This compares to an estimated average annual profit of $95m over the lease period under current forecasts.

In other words, the private operator would need to squeeze an extra $70m a year in profit from Ports of Auckland.

That means a 25% increase on current revenue and additional costs to the Port's customers of $70m a year. That money would ultimately come from Auckland businesses and flow offshore to the private port operators' owners.

The logic of this is unavoidable: the port operator's profit margins would need to be wider than the Council's cost of borrowing. Effectively, selling the operating lease on Ports of Auckland is an expensive form of borrowing, except that the additional cost would fall to the Port's customers—i.e., Auckland businesses and households—in the form of port charges, rather than rates.

This is a best-case scenario. As experience in Australia has shown, increases in costs to the businesses that are the ports' ultimate customers tend to grow and grow as the port landowners' interest becomes focused on profit maximisation and the private port operator exercises its market power to realise ever greater profits.

The separation of the port as a piece of strategic transport infrastructure from the port as a revenue stream encourages the landowner to increase rents, which the port owner then passes on to the customers, along with their increased operating profit requirements.

As one sector expert told the Herald:[14]

> ***"That lease is generally set on what the landowner could get for an alternative use. Terminal charges in Australia are much higher than here. So any attempt to put in the model here raises the fundamental question of what is the landowner going to want in terms of a lease return on the land?***
>
> ***"At the moment the landowner is getting nothing from the lease of that land. The landowner would presumably want a market rate, otherwise ratepayers are subsidising the operation. Which raises the question: why would ratepayers subsidise a third party coming in? They might as well keep it as it is now.***

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14 https://www.nzherald.co.nz/business/how-would-leasing-out-aucklands-port-work-and-who-would-pay/GRVUXZSORWYFF2WR7DXISXVISA/

> ***"If they charge a market rate [for the land lease] then the operator is going to be faced with a significant cost increase over what the current port operator is bearing. Anyone interested would be looking to recover the costs through additional charges to port users. If costs have to increase to reflect the market rate then users of the port - shipping companies and freight owners - would end up footing the bill."***

The lease model drives the landowner to seek to maximise rent and the port operator to maximise its return. Both of these are drivers to increase cost for businesses moving cargo through the port and drags the port away from its purpose as a trade enabler, turning it into a monopoly rentier, instead.

Additionally, to squeeze more profit from the businesses, private port operators are incentivised to under-invest and run down infrastructure. This negatively affects the speed and reliability of cargo handling but, as an effective natural monopoly, customers have little other choice.

On the private port operators' books, these additional charges to customers and the running down of infrastructure appear as higher profits and upgraded asset valuations. Higher valuations in turn justify higher charges to achieve the target return on equity. To Auckland, it would look like a port that imposes more costs on trade and is increasingly unreliable.

Effectively, the lease model adds a second layer of profit-taking and makes both layers focus on maximising returns, rather than ensuring the port is acting as a minimal-cost transport enabler for New Zealand businesses.

DP World's 'terminal access charge' at Botany has increased almost six-fold since privatisation in 2017, from $21.16 to $112 per container

Lessons of failure of port management privatisation in Australia

The private operator model was introduced in Australia in the 2010s. Currently, state governments own the major container ports and, apart from Fremantle, lease the land to private investors. These investors, in turn, charge port operators (referred to as stevedoring companies) for the right to move cargo on the port. The port operators are responsible for the construction and maintenance of port infrastructure, employing the workforce, and all aspects of operating the port.

Australian experience has shown that privatisation of port operations does not improve the throughput of the ports and increases costs for customers. From the perspective of Auckland/NZ Inc, higher costs and no improvement in the quantity of goods moved is not a good outcome, even if the additional profit layers extract more profit from the process.

Dr Greig Taylor, a lecturer in the School of Management and Governance at UNSW Business School, has analysed the effects of port privatisation in depth and finds that they have resulted in higher prices for customers, but not in improved throughput at the ports. The result has been higher costs to and supply chain vulnerabilities.

> ***"The privatisation of Australia's major container ports, as well as failed competition measures and cartel-like behaviour from major shipping lines, are putting significant pressure on supply chains – all of which are being passed onto the Australian public.[15]***
>
> ***"Where port authorities pass into the hands of private entities, these can exercise formidable market power and have no real responsibility to broader stakeholders beyond shareholders. This has manifested itself in large rent increases for stevedores at the major ports. For example, at Botany (Sydney) and Melbourne, Patrick Stevedores claimed that its rent had increased 140% since privatisation. DP World also reported a 60% increase in rent at its Melbourne terminal when due for renegotiation in 2018, with rents per square metre for all stevedores increasing 15% on average in 2018-19 alone compared with the previous year…***
>
> ***…Escalating rents have had a series of consequences for other port stakeholders. Stevedoring companies have considerable leverage over their landside customers (i.e. importers and the transport companies they hire to deliver/collect their cargo), whose patronage is dictated by the cargo owner and shipping line. Stevedores have been accused of using increased property overheads as justification to introduce***

15 https://www.unsw.edu.au/news/2022/11/australian-port-reform-has-failed-miserably--here-s-how-to-fix-it

disproportionate supplementary fees for terminal access, and in turn these are passed down the supply chain. For example, since Patrick introduced the industry's first 'terminal infrastructure levy' at the Port of Brisbane in 2010, the price has ballooned by over two thousand per cent, from $4.95 to $110 per container. This is mirrored at its Melbourne terminal, where the charge has increased from $3.50 at its inception in 2014 to $125 as of June 2020. Meanwhile, DP World's 'terminal access charge' at Botany has increased almost six-fold since privatisation in 2017, from $21.16 to $112 per container" [16]

Such a scenario is very plausible in Auckland. For example, the Port's infrastructure levy is currently $20 per container. If the port operator needed to raise a further $70m a year in revenue, it could lift that charge to over $100 per container, similar to the increases in Australia. Indeed, if speculation that the bulk freight and roll-on, roll-off portions of the Port would be closed under a private operator comes to fruition, container surcharges would be the only way for the operator to redeem its investment and make its profit. As Dr Taylor found:

"The proliferation of port infrastructure/access fees has attracted heavy criticism. Aside from newspaper reports that characterise them as detrimental to the good of the economy (see, for example: Lucas, 2018; Wiggins, 2019a), other industry stakeholders are apoplectic. One haulage representative described the charges, and the frequency at which they are raised, as 'wholesale price gouging', enabled through the 'golden cages... [and] captive market'.

Kingspan, a major exporter of insulation products, conducted a benchmarking survey across ports it used worldwide and 'found that Melbourne was '... one of the most expensive ports in the world for terminal handling and port service charges', also complaining that it 'could not compete against overseas rivals until charges were cut' (Kingspan Insulation Australia, 2018). Kingspan's concerns are shared by other major Australian exporters such as Bega, Visy and K-Mart (ACCC, 2018). In fact, the mounting port access fee furore encouraged the ACCC to put stevedoring companies 'on notice' of enforcement action if anti-competitive behaviour is suspected (Wiggins, 2019b). Ultimately, importers and exporters are 'forced to pass this on to the consumer through higher prices in the shops' (Author's interview with importer/exporter #1, 2020). [17]

16 https://journals.sagepub.com/doi/10.1177/10245294231181967#table1-10245294231181967

17 Ibid

The Australian Competition and Consumer Commission (ACCC) raised concerns about the impact of privatised port operators:

"The ACCC was most concerned about:

- **sustained high profit margins earned by the 2 stevedores**
- **lack of investment in infrastructure, particularly to increase capacity, by the 2 stevedores**
- **lack of incentives for stevedores to efficiently respond to the requirements of their customers.**

The ACCC was concerned that these observations indicated that cargo owners, and ultimately consumers, paid too much for stevedoring services."[18]

Despite attempts to introduce more competition (not an option at Ports of Auckland) bringing some improvements, the ACCC found that "the profit margins of all container stevedores in Australia substantially increased in 2020–21".[19]

Another group of Australian academics found that the experience from that country shows that selling port operation rights generates money up front on the sale, but results in worse outcomes for businesses that use the port over time.

"Although the Australian port privatisation has positive effects on State Governments' balance sheets in the short term, it may result in a risk of undervaluing port assets, increased port charges, impeded port competition, less port investment, and less concern for the public interest in the long term."[20]

Furthermore, a private port operator would have a strong interest in other New Zealand ports not adding capacity that could reduce its cargo volumes. A large multi-national port operator, with billions of dollars at stake, would be incentivised to leverage its market and political power to stymie capacity investment at other ports, such as Northport.

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18 https://www.accc.gov.au/system/files/Container%20stevedoring%20monitoring%20report%202021-22.pdf

19 https://www.accc.gov.au/system/files/Container%20stevedoring%20monitoring%20report%202021-22.pdf

20 https://www.researchgate.net/publication/309688231_The_latest_trend_in_Australian_port_privatisation_Drivers_processes_and_impacts

Other risks from privatisation of port operations

Privatising the operations of a piece of strategic transport infrastructure has ramifications beyond the mere finances of the deal.

Lack of accountability

Any privatisation of Ports of Auckland's operations would reduce accountability. Currently, the elected Auckland Council exercises direct oversight of the Port, with the Port's Board regularly reporting to the Council.

Auckland Mayors have called Port management in to explain issues - such as the deaths on the Port during the automation programme, the failure of which resulted in Port workers being driven to work faster, resulting in safety lapses. The Council was able to compel the Port to commission a report into its health and safety issues and monitor the progress the Port made in actioning the recommendations[21].

Privatisation removes that accountability. Port operations would now be in the hands of an overseas-owned company, only accountable to the lessor of the land through the terms of the contract. Political oversight would be effectively removed.

Likewise, 'soft' accountability would be lost. The current Port management are members of the Auckland business community. They are answerable to their contemporaries for the

21 https://www.stuff.co.nz/business/300265032/significant-health-and-safety-changes-needed-at-ports-of-auckland-review-finds

performance of the Port. They have an interest in the functioning of the Port as residents of Auckland.

A multinational overseas port operator, with a natural monopoly and a long-term lease, has no such interests and responsibilities. The Port would merely be a profit centre for them; they are incentivised to spend as little as possible and take as much as they can. If that has negative effects on the broader New Zealand economy and increases costs to Auckland businesses, that is no concern to the private port operator.

The automation project shows what happens when Ports of Auckland loses its focus on serving the economy and becomes focused on profit maximisation instead. The needs of customers were overlooked and in the resulting chaos, businesses faced extra costs from congestion surcharges totalling $150m, and delays in receiving goods estimated to have cost over a billion dollars. As International Transport Workers' Federation study into the automation project states:

> ***"Emeritus Professor of Economics at the University of Auckland Timothy Hazledine has analysed the costs of the congestion charges, disruption, and delays at the port.***
>
> ***He estimates that congestion charges levied by the shipping lines for containers at Ports of Auckland amount to around $150 million.***
>
> ***Additionally, delays in moving goods create economic costs. Based on a study carried out for Waka Kotahi, the New Zealand Transport Agency, Professor Hazledine estimates that delays in receiving goods have an average loss of value of approximately $1 per hour per tonne to businesses. 3.4m tonnes of containerised goods were imported through the port in FY 2021. From November 2020 through to April 2022, wait times for ships to get berths of as long as 22 days were being reported. Assuming a conservative average delay of five days, Hazledine estimates a cost to the New Zealand economy of $1 billion over this period.***
>
> ***This analysis puts the cost of automation project write-offs, combined with congestion and delays induced by the automation project and exacerbated by COVID, at over $1.2 billion."***[22]

Transfer of market power and asset-stripping

The equity fund model is to have the business take on more debt to pay a return to the investors, up to the point where the business can barely maintain its interest costs. Capital investment is often neglected to maximise short-term profits. Once this approach has run its course, the fund will frequently flip the asset to a different fund whose focus is cost reduction, increasing prices, and closing down or spinning off loss-making parts of the business.

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22 https://www.munz.org.nz/wp-content/uploads/Lessons-in-Failure-Automation-at-the-Port-of-Auckland-%E2%80%93-ITF-Report.pdf

At all times, the investor knows that they can walk away but that the council/government cannot. The Port is vital infrastructure for the country that cannot be allowed to fail. That gives the power advantage to the investor.

This scenario has played out many times in New Zealand and abroad, where a government or council has let a private investor have too much power over a piece of strategic infrastructure and the political fortunes of the politicians making funding decisions. They can always demand more money and politicians acquiesce because the investor has a chokehold on their political interests and the public interest. In the case of the Port, this could take the form of demands for public funding for infrastructure that benefits the investor or renegotiation of payments and other terms to favour the investor.

Privatisation abroad has resulted in asset-stripping as successive investors seek to minimise their investment and maximise their returns. The result is ports with poor infrastructure and heavy debt burdens.

> ***"The international academic literature demonstrates that port authority privatisation contributes little towards port efficiency and can often be vulnerable to hedge fund profiteering,"*** [23]
>
> ***The PE [Private Equity] exit strategy is to sell-on port assets, often to other PE owners, implying that ports concerned may continually carry a high debt burden, yet will have few new assets to show for it. This perennial debt burden is not connected with the creation of new port assets which might be expected to benefit port users and the wider economy. Thus, it is doubtful if the PE model of port ownership, operation and regulation is conducive to creating a competitive national economy. Indeed, the opposite outcome is more likely."*** [24]

Proponents of privatisation like to claim that 'market discipline' will unlock unspecified 'efficiencies'. However, these efficiencies have failed to materialise when ports overseas have been privatised.

> ***"Early analysis of the UK's program of port privatisation in the 1990s, albeit an extreme manifestation which involves the permanent (not leased) sale of port authority responsibilities and all associated land/assets, found it to be a case of 'private profit, public loss', with reforms proving 'costly… ineffective, and in many respects counter-productive' (Saundry and Turnbull, 1997: 332). This initial assessment is supported by more recent research that has highlighted the fully privatised model to be increasingly vulnerable to hedge fund involvement, and as such prone to a series of undesirable consequences such as 'a primary focus on high profits, a lack of investment in creating new port assets, high debt levels… high***

23 https://www.unsw.edu.au/news/2022/11/australian-port-reform-has-failed-miserably--here-s-how-to-fix-i

24 https://www.sciencedirect.com/science/article/abs/pii/S221053951300076X

related interest payments'. In turn, this inevitably leaves 'little or nothing left from port surpluses which might have contributed towards investments in future new port infrastructure and capacity' (Baird, 2013: 164), leading to calls for a national ports regulator to be introduced in the UK (Baird, 2016; Monios, 2017).

The international literature on port privatisation has demonstrated that privatisation often does little to improve efficiency in the container ports of mature economies (Pyvis and Tull, 2017; Cheon, 2008; Cullinane et al., 2006) or to encourage investment in port infrastructure (Pallis and Vaggelas, 2022; Baird, 2013) and is usually unduly influenced by the political ideology of the government of the day (Brookes et al., 2017; Monios, 2017)." [25]

In reality, 'efficiencies' often take the form of borrowing from the future by cutting maintenance and new infrastructure. In many instances, such as the re-nationalisation of rail in New Zealand, the cost of remedying this underinvestment is eventually paid (or overpaid) by local or central government desperate to relieve the productivity burden that it is placing on other parts of the economy.

Health and safety risk

Successive attempts to increase the profitability at the port have come in the form of attempts to undermine the pay and conditions of workers and extract greater productivity per work hour. Deunionisation and automation tried this and failed, and it was the workers who suffered as management expected the workers to make up for these failures.

A private port operator would undoubtedly also see personnel costs as a major area to target for cuts.

The automation experiment provides a warning for what happens when health and safety is made secondary to profit. When the automated straddles failed to deliver the promised throughput, the management put pressure on workers to move faster in the manual operations to pick up the slack. They introduced a bonus scheme for the fastest crane drivers, encouraging workers to take more risks, and ignored safety warnings. This led to deaths, as the ITF report records:

"Laboom Midnight Dyer died after his manual straddle carrier toppled over on 27 August 2018. He was the first worker to die in a straddle incident since 1976. Dyer had received the bonus for high productivity. That he achieved this while also having a high tip alarm rate, should have concerned management.

25 https://journals.sagepub.com/doi/full/10.1177/10245294231181967

An investigation by government workplace health and safety regulator WorkSafe into his death found faults with Ports of Auckland's practices including: "... the following gaps in training orprocesses for straddle drivers:

- *Insufficient monitoring of tip alarm activations;*
- *Operating a bonus system based on productivity which would cause drivers to feel that they had to work as fast as possible. Mr Dyer had a high tip alarm activation record. Despite that record he consistently received his bonuses..."*
- *And that POAL had failed to ensure "the bonus scheme incorporated parameters that promoted safe driving, to counter any incentive to achieve greater productivity at the expense of safety".*

In the sentencing over the incident in 2020, Justice Thomas said: "There was a systemic failure to instil and maintain a culture of safety and compliance.... The bonus scheme departed from the industry standard. The hazard was obvious.".

POAL pled guilty to failing to ensure the health and safety of its workers and was fined $540,000. The port was ordered to pay a further $136,000 to Dyer's family.

Despite this record, in 2019, POAL told Auckland Council: "Our entire management team is focused on ensuring [automation] is delivered successfully".

Workplace deaths at the Ports of Auckland have become a regular feature on New Zealand televisions in the years since the automation project began, with three workers killed in just four years.

In August 2020, Pala'amo Kalati was killed when a container fell on him. Such was the pressure for productivity, an unnamed stevedore said that a manager told the workers they had to keep working while his body was still lying on the port: "The boys refused and his comment was 'look at it like it was an accident on a motorway, you see it and you carry on'."[26]

After the harrowing experiences that port workers have endured over the past decade of experiments in trying to squeeze more profit from the Port, they are naturally weary that their safety will again be compromised in the search for profits.

26 https://www.munz.org.nz/wp-content/uploads/Lessons-in-Failure-Automation-at-the-Port-of-Auckland-%E2%80%93-ITF-Report.pdf

Responding to pro-privatisation arguments

Privatisation advocates cannot argue that a private port operator wouldn't need to extract greater profits from the Port, that is a simple fact. Instead, they will argue that greater profits would be enabled by enhanced productivity, that competition would contain rentier behaviour, and that regulation could ensure the Port continues to work in the wider economic interests of New Zealand. These arguments are not credible.

Ports of Auckland as a natural monopoly

New Zealand ports are effectively natural monopolies. While there is limited competition between Ports of Auckland, Port of Tauranga, and Northport to be the offload points for imports into the upper North Island, capacity constraints in the ports as well as road and rail network, and extra cost and time that extra land transport entails limit this competition.

In fact, the reduced capacity at Ports of Auckland's disastrous attempt to introduce automation, quickly led to congestion at Port of Tauranga and Northport as they could not handle the portion of cargo diverted to them from Ports of Auckland. Port of Tauranga CEO Mark Cairns called on Ports of Auckland to sort out its automation mess, saying "Unfortunately, the threat of congestion remains and is unlikely to dissipate until Ports of Auckland sorts out its operational problems." [27]

When attempts were made to move higher volumes of imports from Port of Tauranga and Northport into their primary market in Auckland, capacity constraints on rail lines, highways, and inland ports were quickly hit, with trucks lined up around the block at the inland ports. Since the automation project was abandoned, the value of goods flowing through Ports of Auckland has rapidly returned to previous levels.[28]

In a model market with multiple players, competition limits a business's market power. However, as discussed above, competition is not really a solution for Ports of Auckland. While Ports of Auckland has lost export market share to other ports, particularly Port of Tauranga, over the years, it remains the main import port for the country and the primary export port for Auckland. There is not the capacity to seriously threaten Ports of Auckland's cargo volumes with competition from other ports. In fact, other ports are struggling to grow capacity to keep up with rising cargo volumes, let alone to undercut Ports of Auckland and take substantial shares of its volume.

This reinforces the fact that Ports of Auckland is not in real competition with the neighbouring ports. For most of the cargo that must move in and out of Auckland, Ports of

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27 https://businessdesk.co.nz/article/logistics-chain-reactions-lead-to-port-congestion-across-nz

28 https://www.stats.govt.nz/topics/imports-and-exports

Auckland is the only choice. Competition is marginal and, for all intents and purposes, Ports of Auckland is a natural monopoly. The Australian Competition and Consumer Commission has come to similar conclusions regarding its ports stating container ports "are regional monopolies with substantial market power".

Where competition exists, it may be effective in preventing excess profits, but where it doesn't, there is little to stop excess profiteering, which increases costs to businesses.

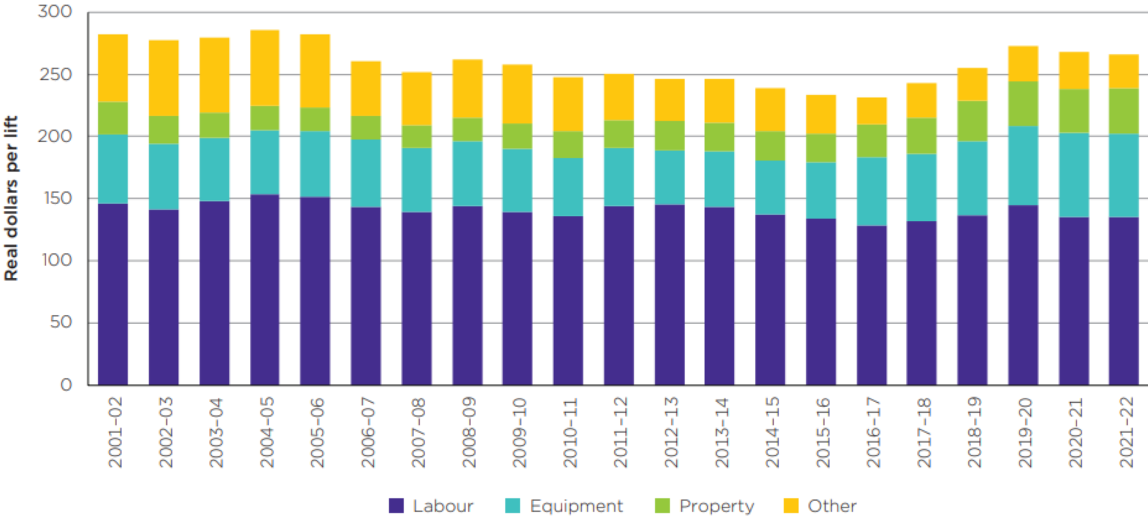
> ***As the ACCC found:***
>
> ***The strength, or lack, of competition between stevedores is a critical determinant of their ability to earn excess returns. Effective competition is likely to drive stevedores' returns towards a level closer to the market cost of capital (accounting for industry risk) in the long-term. Stevedores may hold substantial market power in the absence of effective competition. Substantial market power would allow stevedores to charge prices that enabled them to earn supernormal returns on a sustained basis.*** [29]

29 https://www.accc.gov.au/system/files/Container%20stevedoring%20monitoring%20report%202021-22.pdf

The productivity argument

It is a regular refrain that privatisation will unleash 'market forces' that will drive higher productivity. The evidence for this in real life is more scant, particularly at ports.

In Australia, 20 years' experience of privatisation has seen little change in the real cost of moving cargo.



There is even more room to question whether productivity improvements are available at Ports of Auckland. As the ITF report found, the Port was formerly the best container port in Oceania, with leading productivity rates that well outstripped those of its Australian counterparts with their private operators.

> ***Prior to the push for automation, Auckland was a stand-out example of a productive port. Container movements per labour hour had grown from 55 in 2009 to 80 in 2014 – the best labour rate performance of New Zealand's container ports and well ahead of the five largest ports in Australia. In June 2016, the Ports of Auckland was recognised as the 'Best Seaport in Oceania' at the Asian Freight, Logistics and Supply Chain Awards, a title it would retain in 2017 and 2018[30].***

It was an ill-advised effort to increase productivity while cutting labour costs that led to the disastrous automation programme. Because of the failure of the automated straddle cranes, shipping lines and trucking companies imposed congestion charges on containers delivered to Ports of Auckland. Those extra costs were passed straight on to the customers of that cargo, costing New Zealand businesses on the order of several hundred million dollars even before the cost of delays is accounted for.

30 https://www.munz.org.nz/wp-content/uploads/Lessons-in-Failure-Automation-at-the-Port-of-Auckland-%E2%80%93-ITF-Report.pdf

... Within six years, with the implementation of POAL's automation project, all that changed. The World Bank's Container Port Performance study resulted in Ports of Auckland receiving the unenviable moniker of the 'worst container port in Oceania' in 2022 in response to suffocating port congestion and collapsing productivity.[31]

The automation debacle is not a reason to try yet another experiment at the Port.

Rather, it gives a taste of what happens when costs at the Port rise. Just as the failure of the automation experiment cost businesses through increased charges, so higher port profits would have to come from higher costs to businesses. The failure of the automation project and past deunionisation attempts at Ports of Auckland have shown that there are not significant cost savings to be made by any responsible port operator - so, the only route to higher profits is higher charges on customers.

New Zealand's fraught experience with strategic asset privatisation

Advocates for privatising the Port's operations will say that competition and regulation would keep the port operator from exercising its market power to make super profits at the cost of Auckland businesses.

As discussed above, competition does not truly impact Ports of Auckland - the other ports in the region are unable to handle a significant portion of the cargo from Auckland in addition to the cargo they already handle, and they rapidly became congested when the automation debacle sent more freight their way in an effort to avoid the mess in Auckland.

New Zealand does not have a strong record of regulating privatised natural monopolies. There is a history of ad hoc legislative interventions and expensive re-nationalisations by governments but only after the situation has declined dramatically, through rising prices, increased costs to government, and worsening service.

Transport has been particularly vulnerable to failed privatisations. As noted, transport systems deliver the most benefit to the wider economy and society when they are operated in the public interest first, rather than to maximise profit.

The failure of rail privatisation was rooted in exactly this problem - the private owners wanted to maximise profit, not maximise service provision. Therefore, they underinvested in infrastructure, closed unprofitable or low-profit lines, and shrank the service to its most profitable elements. This led to declining services for train users and more trucks on the road creating more damage - but these are externalities to the private owner of the railways. Eventually, the Government was forced to buy back the railways at significant cost because the Government could not afford to see this strategic infrastructure wither any further.

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31 Ibid.

New Zealand does not have a strong record of regulating privatised natural monopolies.

The Public Transport Operating Model [PTOM] is another example of failed privatisation. This policy banned councils from operating bus services directly and forced them into long-term contracts with the lowest bidder. Across the country, this has led to declines in service quality as low-cost operators have underinvested in drivers and vehicles. The Government has been forced to step in and deliver additional funding to boost drivers' pay to competitive levels to try to stop the industry from haemorrhaging drivers. After barely more than a decade, the PTOM experiment is being brought to an end, with new legislation that will replace it and allow councils to return to operating public transport services in-house.

Transport isn't the only sector in which privatisation has failed in New Zealand. Again and again, government and councils have had to put money into privatised sectors when the private owners would not make the investment themselves (e.g., the broadband fibre network), make legislative changes to prevent monopolistic behaviour (e.g., telecommunications unbundling), front up more cash when demanded (e.g., Transmission Gully PPP), or reinvest to prevent the collapse of a strategic asset (e.g., Air New Zealand purchase).

Public ownership provides a tool to ensure natural monopolies work in the wider interests of 'NZ Inc'. While Ports of Auckland is a limited liability company and is intended to return a profit to its owner, Auckland Council, it has a council-appointed board and, so, must maintain its social licence and the support of politicians whose interests are in the health of the Auckland economy more broadly than just Ports of Auckland's bottom line.

Conclusion

Ports of Auckland has historically been a relatively efficient port, rated the best in Oceania until the disaster of the automation programme, and returning a dividend to Auckland Council that covers its cost of finance.

Privatisation of Ports of Auckland's operations would lead to higher costs for the businesses that move cargo through the Port. Any private operator is going to require a higher rate of return from their investment than the Council does currently.

Those returns cannot be gained by squeezing costs down, as the recent automation failure has shown. They would have to come from increasing charges. This has been seen across Australia, where privatisation of port operations has seen charges increase by $100 per container.

Effectively, to reduce the Council's debt, Auckland businesses would instead be forced to pay more on port charges.

It is estimated that a private port operator would need to increase charges by at least $70m a year to make its return on investment - increasing charges on port users by 25%.

This estimate is conservative. Once a multinational private port operator is in place, it would have significant market power and power over political decision-makers due to its control of a natural monopoly that is vital transport infrastructure for Auckland's economy, and the lack of accountability that comes with public ownership. As we have seen in New Zealand time and again, it would likely use that power and unaccountability to increase its profits further, with New Zealand businesses bearing the cost.

Privatising Ports of Auckland is a 'solution' in search of a problem. The Council would be better advised to return the Port to concentrating on what it used to do so well, and is starting to do again, now that the automation project has been abandoned: providing reliable, efficient cargo services for the Auckland economy at a reasonable price.