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14 September 2015

Mr Keir Delaney
Secretary
Port of Melbourne Select Committee
Parliament House
Spring St
MELBOURNE VIC 3000

Dear Mr Delaney

Inquiry into the proposed lease of Port of Melbourne

The Victorian Employers Chamber of Commerce and Industry (VECCI) welcomes the opportunity to provide a submission to the Inquiry into the proposed lease of the Port of Melbourne.

VECCI has been a consistent supporter of the further development and leasing of the Port of Melbourne in order to fund investment in new infrastructure and improve Victoria's productivity and trade competitiveness. In our 2014 State Election business agenda: *Taking Care of Business,* we applauded the bipartisan support for the privatisation of the Port of Melbourne and reinvestment of the proceeds into new infrastructure.

We would like to provide comments on several of the key points that the Committee is examining:

The duration of the lease

In our view, the proposed 50 year lease term is appropriate. It provides the purchaser with a clear timeframe to maintain and improve the port's operations, raise efficiency and boost competitiveness. It also ensures the government of the day can maintain control over the long-term ownership of the Port of Melbourne.

Our understanding is that the option for an extension to the initial term of up to 20 years is designed to incentivise the leaseholder to invest in port infrastructure towards the end of the initial 50 year term, while maintaining the state's flexibility to pursue alternative land uses for the site. VECCI supports the option for a lease extension of up to 20 years on the basis that it is made explicit (either through the legislation or lease agreement) that any extension:

- is entirely at the discretion of the state;
- delivers a clear financial benefit to the state;
- is linked to port infrastructure investment.

We note that the proposed term is shorter than the duration of the recent port privatisations in NSW, with Port Botany and Port Kembla both leased for a term of 99 years.

The potential impact on the development of a second container port

The main element of the proposed lease structure that is likely to impact on the development of a second container port is clause 69 of the Delivering Victorian Infrastructure (Port of Melbourne Lease Transaction) Bill, which allows for the government to make a payment to the leaseholder should another international container port be developed during the term of the lease. VECCI has no prima facie objection to the Port of Melbourne lease arrangement including a provision for compensation to the leaseholder in the event that this occurs.

The proposed compensation arrangement has been framed in terms of a requirement for the state to compensate the leaseholder in the event that the state develops a second container port that detracts from the international container capacity at the Port of Melbourne.

VECCI understands that Port of Melbourne container capacity, for the purposes of determining any possible compensation, will be defined through the bid process, but will be capped at an amount that is less than the full natural container capacity of the Port of Melbourne. Thus, if a new port is developed and the Port of Melbourne is operating below this capacity, compensation will be payable. If a new port is developed and the Port of Melbourne is operating above this capacity, then no compensation will be payable.

The main rationale for including a compensation provision would be to maximise the proceeds of the lease, as it would reduce an element of risk that would otherwise be borne by the leaseholder. However, a compensation provision would create a contingent liability that needs to be managed by a future government.

It is difficult to comment more specifically on the implications of including a compensation provision without knowing:

- the amount of compensation proposed;
- the Port of Melbourne container capacity that would be used to determine whether the compensation provision is triggered.

These factors will determine whether the inclusion of compensation represents a fair proposition for potential bidders, the government and Victorian taxpayers.

Ports are complex pieces of infrastructure. The development of a new port and associated road and rail infrastructure is costly and has very long lead times. In this context, VECCI is keen to avoid a situation where a future government, in order to avoid triggering a large compensation liability, postpones the development of a second port resulting in businesses being disadvantaged by capacity constraints at the Port of Melbourne.

We are also keen to avoid a situation where the new Port of Melbourne leaseholder, anticipating the completion of a second container port, modifies operational behaviour in order to trigger the compensation clause, for example by restricting investment or productivity in order to limit the growth of port throughput.

The timing, container capacity and amount of compensation needs to be set so that there is no risk of Victorian business being disadvantaged by capacity constraints at the Port of Melbourne. This could be achieved by:

- setting the level of container capacity used to determine whether compensation is triggered at a level which provides an appropriate buffer before the full capacity of the port is reached;
- capping the compensation at a level that will not deter a future government from developing a second port.

It will also be important to ensure that the assumptions used to determine the full natural container capacity (for example regarding the size of vessels that will use the port in the future or the scope for future port capacity upgrades) are robust and rigorously tested.

Performance monitoring safeguards could also be put in place to ensure the leaseholder does not seek to restrict the growth of port throughput in order to trigger compensation, for example by limiting productivity or investment.

The government will need to carefully evaluate whether the benefit of including compensation (i.e. an uplift in the sale price) is proportionate to the amount of compensation and likelihood of it being paid. If an arrangement favourable to the state can not be reached, the government should take compensation off the table and accept a lower sale price and finance its infrastructure program through alternative funding sources.

Potential impacts on the cost of goods

VECCI supports the role of the Essential Services Commission (ESC) in its regulatory oversight of the Port of Melbourne. The ESC is already an important regulator of the port as well as Victoria's other essential services and is required to have regard to not only price, but service quality and reliability considerations.

The leasing of the Port of Melbourne will require the proposed expansion of the ESC's role to include the pricing of all trade charges for cargo and shipping movements, which we consider to be appropriate.

VECCI supports the proposed 15-year price cap (at the Consumer Price Index) for cargo and shipping movement charges as it will provide a degree of certainty for users of the Port of Melbourne in the short to medium term.

However, the Committee should consider whether the regulatory powers of the ESC will be sufficient to protect port users over the full duration of the lease, and to respond to all foreseeable market developments. The regulatory framework must be established upfront in order to provide confidence and certainty to both port users and the potential leaseholder.

The Committee should also consider whether regulatory oversight of port rents is needed, to ensure that they remain competitive. While rents currently comprise only around 14 per cent of port revenue, and are determined through a commercial rental review process (with independent valuation where agreement can not be reached), the Committee should consider whether this process is likely to be sufficient into the future.

It is also important that the Victorian Government continues to play its role in the provision of associated port road and rail infrastructure to allow for the efficient transport of goods to and from the Port of Melbourne. Congestion can add considerable delay costs, in turn limiting the efficiency of the movement of freight to and from the port, impacting on port user costs and competitiveness.

Potential impact on the Victorian economy

Victoria's export performance has been a key feature of the state's economic performance in recent years. Victoria exported almost $24 billion in goods during 2013-14 (along with $13 billion in services), with total exports growing at an average annual rate of 3.2 per cent over the previous five years.

With the expanding network of Free Trade Agreements that Australia has either entered into or is currently negotiating, Victorian businesses will have further opportunities to access new markets and expand trade in existing markets.

An efficient and competitive Port of Melbourne is key to securing export growth for Victoria over the longer term. As previously stated, we would be concerned if the Port of Melbourne lease included a compensation clause that was so significant as to cause the government to delay the development of a second international container port in Victoria.

This would give rise to capacity constraints that could in turn lead to higher prices or lack of access, harming our exports, and thus, Victoria's broader economic performance.

As we have indicated, the compensation clause must not be so significant as to create a situation where the new Port of Melbourne leaseholder modifies its behaviour in order to trigger the compensation clause, for example by restricting investment in order to limit the growth in port throughput.

The lease of the Port of Melbourne provides an important opportunity for Victoria to release capital that is currently tied up, making way for investment in important productivity-enhancing infrastructure across the state.

A decision to act soon to lease the Port of Melbourne would also ensure that Victoria benefits from the Federal Government's Asset Recycling Initiative, which could provide the state with up to $1 billion in additional funding from the Federal Government for investment in new infrastructure.

Level-crossing removals, Melbourne Metro rail, the West Gate Distributor and the Murray Basin Rail Project are all examples of state-shaping infrastructure projects that could benefit from the proceeds of the lease of the Port of Melbourne through the proposed establishment of the Victorian Transport Infrastructure Fund. These projects will create jobs and provide an important boost to the broader Victorian economy over the long-term, and deliver benefits to a broad range of industries across the state.

Should you wish to discuss any aspect of VECCIs submission please contact Steven Wojtkiw, Chief Economist, VECCI on telephone [redacted].

Yours sincerely

[redacted]

Mark Stone
Chief Executive