THE CONTAINER MARKET: THE VIEW FROM THE PORT OF PIRAEUS[1]

By Harilaos N. Psaraftis[2]

Ladies and gentlemen,

It certainly gives me great pleasure to address this audience, together with my former colleague from MIT Hank Marcus and my former students at MIT Tassos Aslidis, Costas Bardjis, and Hauke Kite-Powell. I would like to thank them all, along with Arlie Sterling of Marsoft, for their invitation to be here today.

Other speakers in this session have talked about the container market and its perspectives. I will attempt to do the same from the point of view of the Port of Piraeus, a port that interacts with this market on a 24-hour basis, and depends on it for about 70% of its revenue.

Speaking about 'interaction', I have heard a leading European port executive claiming that interaction with container lines is like being thrown into a swimming pool full of alligators. As the Port of Piraeus CEO for the last five years, many times I feel the same, and I will try to give you a flavor of what I mean.

As you may well know, the Port of Piraeus is by far the largest port in Greece. By comparison, Thessaloniki is a distant second, being about a third of Piraeus in terms of annual turnover (in Piraeus, on the order of 45 billion drachmas, or $110 million). Our revenues come from cargo handling, port dues, storage, and generally any charge to port users for services rendered to them. Expenditures go to salaries of port personnel (about 1,800), construction and maintenance of port infrastructure, purchase of equipment, and other port operating expenses. Historically, we have never received any funding from the Greek State, but we are obliged by law to financially support the City of Piraeus and four other adjacent municipalities. Some of the port's infrastructure development is financed in part from the European Union's Cohesion Fund and by a long-term loan from the European Investment Bank.

Each year about 12 million passengers go through the port, which is among the top three in the world and the top in the Mediterranean in terms of passenger traffic. The port is at the crossroads of three continents: Europe, Asia and Africa. In addition to passenger traffic, it has also a quite substantial volume of cargo traffic, in areas such as drybulk, general cargo, and, most important, containers.

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About this time five years ago, when I started my tenure at the port, things were a bit unsettling in the container area. Container lines Evergreen and Lloyd Triestino had decided a few months earlier to move their transshipment hub from Piraeus to Gioia Tauro in southern Italy, and this was certainly bad news. And indeed, after several years of growth, 1996 saw the volume of container traffic through Piraeus decline by approximately 3% vis-a-vis that of 1995, to about 585,000 TEU. This reduction was solely due to a reduction of *transshipment* traffic through the port, as local traffic of imported and exported containers continued to grow as in previous years.

As you probably know, the market for container transshipment is one of the most dynamic ones in liner shipping. With the economies of scale realized by large (up to 8,000 TEU) container vessels deployed on trunk routes worldwide, it is not cost effective for these vessels to make direct calls in many ports. For this reason, lines develop "hub and spoke" systems, in which smaller "feeder" vessels distribute containers to and from smaller ports, whereas larger "mainline" vessels connect only to larger ports (the so called "hub ports").

Which ports establish themselves as hub ports worldwide is up for grabs, and the Mediterranean is no exception. The main trunk route of the Med is the one connecting the Far East with Northern Europe, through the Suez Canal and Gibraltar. Some of the traffic on this route makes no Mediterranean port calls, going all the way to Northern European ports and then being distributed to various destinations across Europe. In that respect, ports such as Genoa or Naples compete with Rotterdam or Hamburg for cargoes from the Far East to countries such as Austria and vice versa. As currently many cargoes completely bypass the Mediterranean, it is expected that the development of intermodal connections in Med ports will help reverse this trend.

Of course, another part of the traffic on the Far East – Northern Europe route comes to or from markets close to Med ports or markets in the Black Sea, and therefore has to pass through a Med port, either as local traffic, or as transshipment traffic. Container line Maersk-SeaLand has a huge transshipment terminal in Algeciras (Spain), where containers are switched not only between a mainline and a feeder vessel, but also between two mainline vessels (the latter practice is called "interlining"). Other lines use ports such as Marsaxlokk (Malta), Valencia and Genoa as hub ports. The story of the Medcenter Container Terminal in Gioia Tauro is indicative, as this port was not even on the map in 1995, but via an aggressive expansion and pricing policy is now the top Med hub port (and, by the way, still our biggest competitor).

Back in 1996, the question was whether the 3% decline in container traffic was a "statistical glitch" or something more serious. We felt we did not have the luxury to assume it was a glitch. Transshipment had never accounted for more than 25% of the volume of container traffic through Piraeus, the bulk of the latter being local (mainly incoming) traffic. However, with the completion of a new 700-m length, 16.5-m depth quay and the delivery of four new Post-Panamax gantry cranes (all of which were targeted for completion by mid 1997), the box throughput capacity of Piraeus would about double. The question was who would bring in enough traffic to fill in the new capacity.

That was not a trivial question to answer. In fact, I soon discovered that the analysis behind the decision to acquire the new capacity was based on debatable assumptions. For instance, it was assumed that the investment cost for this new capacity would be paid off by revenue generated by new *local* container traffic, and that our tariff structure would remain unchanged.

I was amused to think that for a professor looking for opportunities to apply his sophisticated knowledge of hierarchical decision models, the fact that such a strategic decision had been made in prior years certainly made things easier: There was no need to justify such a decision. Nonetheless, there was a real need to find a way to make it work!

The problem was that to fill in the new capacity by a substantial increase in *local* container traffic would involve factors that went beyond marine transportation. Much of local traffic through Piraeus goes to or comes from the Athens greater metro area, and only moderate growths were predicted for it. The only way to increase local traffic as a step function would be to divert the substantial traffic that came into or left Athens via other routes (for instance via Bulgaria onboard trucks) so that this cargo could be shifted to containers that pass through Piraeus. Given the myriads of possible routes to and from Athens, this problem was considered too complex, so this possibility was dropped, at least as a short-term prospect. We wanted something fast.

This left the transshipment market as the only one to consider. With at least 5 million TEU annually transshipped within the Mediterranean, the pressing question was "can we at least grab some of it?" In the fall of 1996, and with two lines having just quit Piraeus, that was not an easy question either.

We knew that Piraeus enjoyed several advantages over rivals such as Malta or Gioia Tauro, none of which had a serious local market potential, or was close to the expanding Black Sea market. For a shipping line interested in transshipment, having also a local market is an incentive, so that costs could be spread over more traffic. Of course, with the fluid situation in the container scene and with the cutthroat competition among carriers globally, we realized that it would take more than wishful thinking to lure such traffic to Piraeus. It was clear that having a good geographical location, some local potential, and some spare capacity were not enough.

The approach that we followed was void of sophisticated econometric and scientific models, but went back to fundamentals. Customers complained that our transshipment tariffs were not competitive. They were right, so we drastically reduced them, bringing them close to those of the competition. We established a new scale for the new rates, which were «flat», that is, the same for a 20-ft or 40-ft container, empty or laden. The new rate structure was substantially simpler than the old one. In calculating the rates, we went through the exercise of computing the marginal costs of the terminal, something that was never done before and was not as easy as it looked at first glance.

Customers also wanted guarantees of immediate berth and crane availability in order to use Piraeus as a hub. The spare capacity available provided a necessary condition for these guarantees. But we had to change our regulations to provide priority and enough equipment to companies in return for a guaranteed volume of transshipment traffic.

Last but not least, customers wanted to be able to sign a legal contract with the Port in which all mutual obligations would be spelled out. So we changed our regulations so that the Port could sign such contracts (before that, it could not).

All of these reforms went on in parallel with (and to some extent were driven by) negotiations with Mediterranean Shipping Company (MSC) and Norasia Line, two carriers which cooperated on a worldwide basis at the time. These companies were using Malta as a hub, but seemed to want something closer to the Black Sea. They were very demanding. They began talks with us in November 1996. I actually remember that when they first came to Piraeus, our biggest labor union was on strike. The lines were not enthused, but we signed a two-year contract with them a year later, after going some extremely tough negotiations.

A difficulty in these negotiations was how to decouple the negotiation process (which was quite specific) from the process of regulatory and tariff reform (which was quite general). We wanted the contract to be compatible with the new regulations, while at the same time we wanted these regulations to be general enough so that a variety of other agreements could be signed in the future.

The effects of the MSC-Norasia deal were very positive. In fact, 1997 closed around 680,000 TEU, a modest increase because the deal started in November. Traffic jumped to 933,000 TEU in 1998, and to 965,000 TEU in 1999. In year 2000 we signed a similar contract with another carrier, China Shipping Container Line, and traffic rose to 1,157,000 TEU, breaking the 1-million TEU mark for the first time in our history. Actually, traffic in year 2000 was about double that of 1996. According to "Lloyds List", Piraeus put itself on the hub map. Since 1998 we are the top container port in the Eastern Mediterranean and we entered the list of the top 50 container ports in the world.

There was a piece of semi-bad news in all this. We lost Norasia, who in 1998 decided to join forces with CMA and go back and hub in Malta. However, MSC, who was the biggest partner in their alliance, more than compensated for the loss, and in fact renewed the contract twice: In 1999 and this year (in fact, last week), each time increasing their minimum commitment for transshipment traffic. The latest renewal is for ten (10) years.

This turn of events, coupled with some other measures we took, improved the Port's financial situation significantly. After two years marginally in the red, 1996 and 1997, we are steadily in the black since 1998.

What are the prospects for the future?

Well, as you may know, in 1999 the Port of Piraeus was transformed into a Corporation, and in fact we are right now in the final stretches of floating a portion (most probably 25%) of our stock at the Athens Stock Exchange. The stock is now solely owned by the Greek State. It is a very complex procedure, and one that requires great care if we want to do it right. We certainly would not be engaged in this procedure if our financial situation and our future prospects were not positive.

Be that as it may, let me try now to highlight some of the things that are going on and which I think are important.

In terms of competition in the container scene, things are fluid. Our biggest competitor, Gioia Tauro, now faces home competition both from Taranto (the new Evergreen terminal) and Cagliari (managed by P&O Ports). These new terminals are adding pressure on all ports in the region and may actually create domino effects in the future: In act, Evergreen switched from Gioia Tauro to Taranto, and the CMA-CGM alliance is being lured away from Malta to Cagliari, being offered rock bottom prices and all kinds of privileges. Suddenly everybody is becoming very nervous with all this extra capacity, especially knowing that Port Said East is also coming on line very soon (to be managed by Maersk- SeaLand and ECT).

From our standpoint, the fact that we recently renewed with MSC is positive, but we know we have to stand up to our end of the deal if we mean to keep them in Piraeus. China Shipping's contract (a much smaller volume of traffic but still very important) ends this year, and we have still not renewed with them. China Shipping is among the emerging giants in container shipping. They are very different from MSC in terms of philosophy and negotiating tactics. When they first came to hub in Piraeus end of 1999, they did not ask for anything, they just came. Their demands came later, and very gradually. We signed a contract in 2000, after long talks where at each stage they came with more demands. At some point they even *ordered* their agent in Piraeus to convince me to accept their new terms! (I did not). Now we are in the process of negotiating an extension to their contract, but it will not be easy. They are bringing in a new service that will link the Far East with North America via the Med. We know they are being courted very aggressively by Gioia Tauro, who lost Evergreen to Taranto and seem to be very anxious to win another big Chinese customer. We cannot predict the outcome of all this, but the flip side of it is that we are also engaged in talks with another line (whom I will not name) who is also interested to hub in Piraeus. If lines look for alternatives, so do we.

My own view is that our position will be strengthened with the link of the container terminal with the railway network, which is planned to be completed in 2005. This will expand our effective hinterland and increase local traffic.

Also, the so called 'Pier III' is an interesting project. Pier III is the planned extension of the container terminal, one that would add about 800,000 TEU to its capacity. The critical question is, should we build it and operate it ourselves, or as a joint venture with somebody else (e.g., via a concession to a private terminal operator). My own opinion leans more toward the latter option, as less risky and more in line with what's going on elsewhere. But this issue is open at this moment.

Leaving all this aside, perhaps the most important development that will likely impact, perhaps significantly, the way we do business in the future is the European Commission's proposed Directive on market access to port services, also known as the 'port package'.

The story with the Directive has been brewing for some time now. In 1997, with the Green Paper on Seaports and Maritime Infrastructure[3], the European Commission has issued principles to be adhered to as far as port pricing is concerned. One of these is the 'user pays' principle, meaning that prices that are charged to port users should reasonably reflect the full costs of the services rendered. A related principle is that of 'transparency' in port charges, meaning that a port charge should be clear as to what it entails and how it is calculated. Elimination of state aids, or other forms of subsidy, is considered a desirable goal.

The port package comes as a continuation to the Green Paper approach. It is governed by the following principles:

- Member States shall take the necessary measures to ensure that providers of port services have access to the market for the provision of port services.

- Member States may require that a provider of port services obtain prior authorization.

- The number of authorizations can only be limited for reasons of constraints relating to available space or capacity or, for technical-nautical services, maritime traffic related safety. These constraints must be justified and Member States must carry out a transparent, objective and non-discriminatory selection process of the service providers. Key aspects of the selection procedures will be harmonized.

- Ports in which no limitations exist, are not bound by the rules on limitations, selection procedure, duration of authorisations and on transitional measures.

- Member States shall take the necessary measures to allow self-handling.

- Where the managing body of the port provides, or wishes to provide, port services in competition with other service providers, it must be treated like any other competitor. This requires that the managing body must not be involved in the selection procedure of service providers, must not discriminate, in its function as managing body of the port, between service providers in which it holds an interest and other service providers

[3] COM(1997) 678 final of 10.12.1997

and must, in particular, separate its port services accounts from the accounts of its other activities.

- Member States will have to ensure full transparency of all procedures in relation to the provision of port services, as well as the availability of appeal procedures, including a judicial review.

- Where a selection of service providers is made, the period during which the chosen provider may operate will be limited in time.

- Transitional measures take account of legitimate expectations of current service providers but, at the same time, require that within a reasonable time frame, existing authorisations which were not granted in conformity with the Directive's rules be reviewed.

- The Directive and its implementation by Member States must not jeopardise safety in ports.

- The Directive and its implementation by Member States must not jeopardise environmental protection rules in ports.

Together with the proposed Directive, the Commission produced a Communication to the Parliament and Council, outlining the rationale of the Directive and also addressing some other related issues. This Communication is attached here as Annex A.

The principles of the proposed Directive seem very much laudable, at least theoretically. The question is, how will they work in practice. My own initial feeling is that the proposal is very much in line with shipowners requests for more competition in the port sector so that costs are brought down. This seems fair, but its technical implementation may be difficult and may have serious consequences for ports. For example, in Piraeus, which is a port that in terms of size qualifies to come under the Directive, we have only one grain terminal. Should we have another one built just to comply with the Directive? Should we also split our single container terminal into at least two parts so as to comply? Should we split our passenger port?

There is no question that if the Directive passes as is, it will impact us in a serious way, breaking the monopoly we have on all operations in the port. We would have to do major adjustments in the way we do business to adapt to such an environment.

The question is, will the Directive pass as is, or nearly as is? It is not clear. For one thing, there is a widespread movement by Northern European ports to exclude cargo handling from the Directive, something that would radically alter its scope. This movement is endorsed by the Mr. Georg Jarzembowski, Rapporteur to the European Parliament for the

Directive. Mr. Jarzembowski argues that there is insufficient justification to include cargo handling in the Directive and in fact has proposed limiting the scope of it only to technical- nautical services such as pilotage, towing, and mooring. In fact, he renamed the proposal from *"Directive on market access to port services"* to "*Directive on conditions for fair competition and technical-nautical services in ports*".

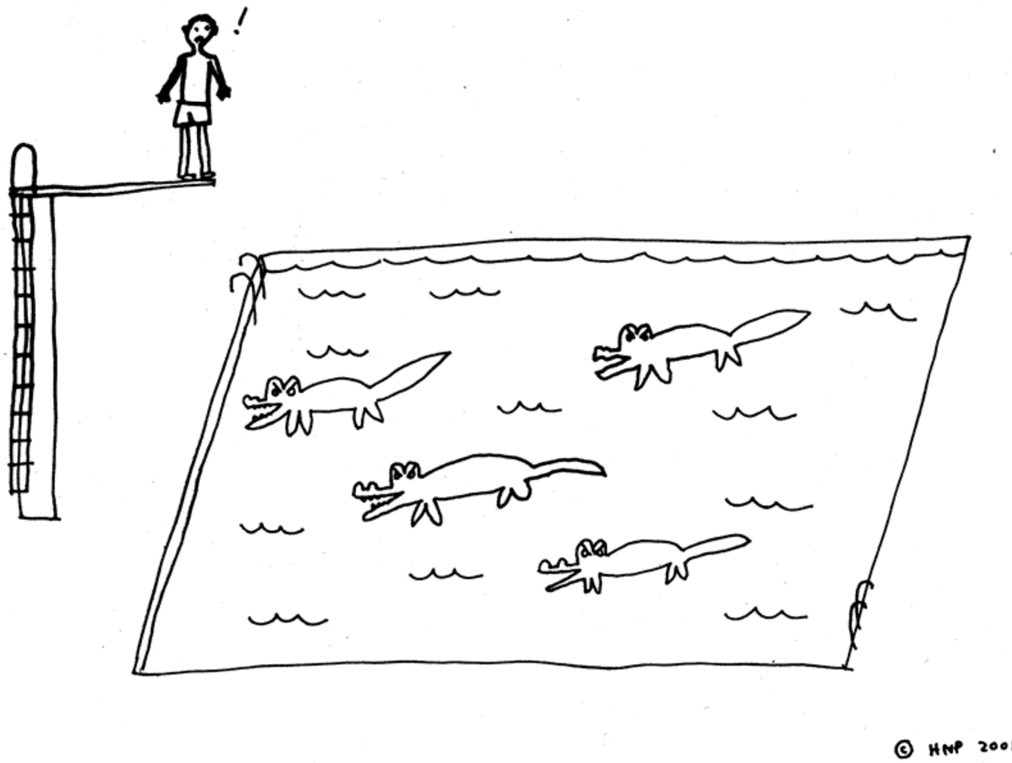
The European Parliament's Committee on Regional Policy, Transport and Tourism (RETT) met on 19-20 June. MEPs held a one-hour exchange of views on the Commission's proposal on market access to port services, based on the report that Mr. Jarzembowski' presented to the Committee. The Chairman of the Committee set the deadline for amendments until 28 August (which by coincidence is today!). Vote in Committee should take place in September and in Plenary in October. The idea is to have an EP position in 1st reading before the Transport Council in October.

So in fact everything is fluid at this point and everybody is very anxious to see how this issue will be settled. We also have something important to look forward to.

Ladies and Gentlemen,

This is the end of my presentation. I have tried to give you a glimpse of the container market, as we see it from the Port of Piraeus. The alligators are at full swing at the pool, but so far we have managed to swim along and survive.

Thank you very much.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