Greg Smith: Tauranga shows the way for Auckland's port

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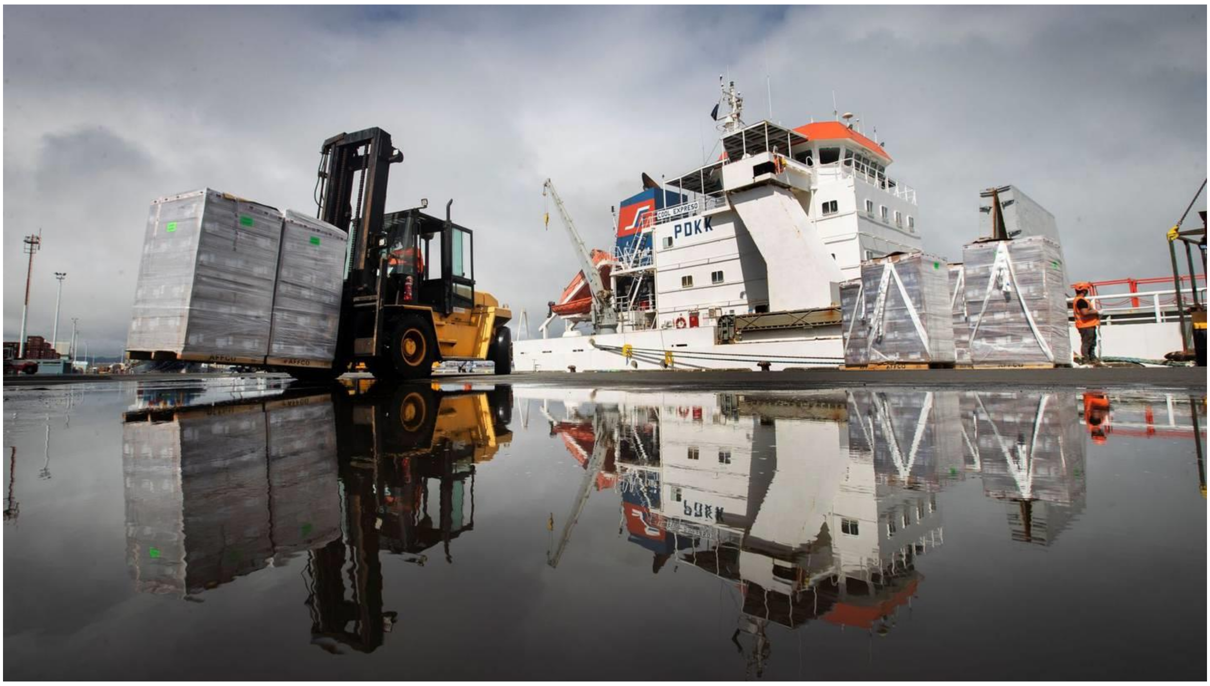

Tauranga has the advantage of land for expansion, so Auckland needs to use its assets better. Photo / Alan Gibson

NZ Herald
By Greg Smith
OPINION:

With the Kiwi sharemarket set to say goodbye shortly to yet another blue-chip in the form of Z Energy, we've had cause to remember another departee of yesteryear — Ports of Auckland (POA).

The port company was originally listed on the NZ Stock Exchange (NZX) in 1993, when the Waikato Regional Council sold its 20 per cent stake, and it remained on the NZX for 12 years before it was taken over by what is now the Auckland Council in a deal that valued the port at $848 million.

Over the past week, it has emerged that the Auckland Council is running out of money to fund many services. The port is however "safe", evidently, and is not going to be put on the block. However, this has raised questions once again — against the backdrop of a mayoral race in full swing — around the value destruction that appears to have occurred since councillor Mike Lee pushed for 100 per cent ownership by the Auckland Council and the port delisted from the NZX in 2005.

Modelling has shown that port ownership models do matter, particularly as they relate to the return on capital invested. Listed port companies have in recent years generated higher returns on capital employed than those with a mixed ownership model, while those under 100 per cent council ownership have performed the worst. The latter result has played out in spades with POA.

Full public ownership at Auckland appears to have not only coincided with a period of sustained financial underperformance, and questionable execution of capital-intensive projects, but also with an appalling safety record. Sadly, the latter issue has been added to, with another tragic death at POA over the past week, marking the fourth fatality since 2017.

The port company seems to regularly make the headlines for all the wrong reasons, and of course the attention always tends to intensify (as it has recently) around the time of local body elections. We believe this is explained in part by the somewhat sporadic governance oversight that appears to have been in place since the port left the stock exchange in 2005.

Somewhat ironically, in 2007, POA had the opportunity to merge with its southern rival but chose to go in another direction, and in more ways than one.

Tauranga has since overtaken Auckland to be the largest port in the country by container volume, revenue, earnings and market value. Last financial year, Tauranga chalked up revenue of $338m, net profit after tax of $102m and container volume of 1.2 million TEUs (twenty-foot equivalent units). In contrast, the once-mightier Auckland delivered revenue of $226m, net profit after tax of $45.6m and container volume of 818,238 TEUs. This is while Tauranga's port also has less debt. The relative comparisons are similar in the pre-Covid years.

The relative paybacks of late have been equally stark. Ports of Auckland has paid out $130m in dividends over the past five years, against the $555m distributed by Tauranga.
Looking at things from a wider and longer-term valuation perspective, POA had a valuation of $848m when it delisted in July 2005, versus around $630m for Tauranga at the time. The latter currently has a market value of $4.4 billion. Opinions vary over what POA is now worth, but its equity value today may not be much more than the port was originally privatised for in 2005.

Ports of Auckland. Photo / Michael Craig

Auckland's port has been beaten to the punch on just about every measure by Tauranga, which at one point was considered to be a small regional port, with only modest expansion prospects. It is sadly ironic that in a City of Sails, Ports of Auckland has not had the wind in its sails for a long, long time.

So where did it all go wrong for the Ports of Auckland?

Whereas the mixed ownership model has been a huge success for Tauranga, the period of council ownership has been hugely problematic for Auckland. The port's management team appear to have been largely unaccountable to anyone (including the council), it seems. Arguably, management has focused on building assets, rather than any imperative to focus on the return on capital employed, at the ratepayers' expense. Rising property values have only highlighted the underlying situation.

Governance at the port would appear far from satisfactory. A number of major initiatives have not gone according to plan, including the multi-year container terminal automation project. This has come at a real cost and meant the port hasn't been able to operate optimally and has effectively exacerbated supply chain blockages that have arisen due to Covid-19. The new carpark building is just one project that doesn't appear to have made anything like a commercial return.

Publicly listed companies tend to be held to greater account than those in most other spheres, and since delisting, the port appears to have been run with an increasing lack of accountability. Problems also appear to be repeatedly pushed down the line.

The chair and chief executive's review at the interim report in February reflected on how tough business was due to "the challenges of Covid-19" and said, "traffic light settings were putting pressure on the automation timetable". Planning on the initiative began back in 2016.

In contrast, Port of Tauranga's interim statement at the half-year was headed "POT improves performance as Covid disruption continues", with the chair reflecting on the port's resilience over the period. The differing tones in language are telling.

Ports are dangerous places, and governance issues at POA appear to have contributed to a poor record on safety. An independent safety report last year (which ultimately hastened the departure of CEO Tony Gibson, who has been replaced by Roger Gray) has seen 21 actions completed but the remaining 24 are still "in progress". Again, the lockdowns have been cited as having contributed to the delay, despite the port quite clearly being an essential business.

The focus on "volumes" for what is a land-constrained operation has also been part of the problem. This has also arguably compounded a strategic misstep in Auckland seeking to compete with Tauranga on price (as opposed to any notion of profit maximisation). This was never a fair fight, even allowing for some reclamation, as Tauranga has always had much greater capacity to expand its geographical footprint. Running a higher-value, lower-volume model would have appeared to have been a far better call for the port to make.

While commanding much political attention at the moment, POA appears to have been mismanaged for multiple local government election cycles. The long-term question of where the port should be based also continues to bubble away and has been the subject of conflicting, and often parochial, reports. Options for relocation include moving to Northport, Manukau or elsewhere. The Auckland Council has already said it has no equity to invest in infrastructure for a relocated port.

The port occupies 77 ha of prime waterfront land, and many Aucklanders would like to see lower-value activities moved and a revitalisation of the waterfront for future generations. The waterfront could be regenerated in the manner that the Viaduct was developed and the removal of heavy traffic from central Auckland would also be welcomed. A financial windfall could also be forthcoming. Based on Viaduct-style square metre rates, the land alone has a value of billions more than an operating port company.

The latter also highlights the extent to which the port has failed to generate an adequate capital return. Even going on the approximately $50m in annual dividends that were paid out in the pre-Covid years, the return on current market values likely equates to a paltry yield of around 1 per cent on the true value of assets, including land.

If the port stays, something clearly needs to be done. A separation, whereby the port is sold but the council keeps the land and charges an economic rent, is one potential solution. The rental income would be at a market rate and would clearly deliver a better rate of return than the current structure. The question would then be whether any potential buyer could make the port work commercially if it had to pay rent.

Another option? How about going back to where it all started to go wrong, and partly relisting POA on the NZX? Publicly listed companies demand greater investor scrutiny and greater management accountability, and POA could well perform much better if thrust back into the focus of stock market investors.

Selling the story of underperforming business that can be turned around may be one angle. Relisting POA on the stock market would go against the current Government's opposition to asset sales but is certainly not the craziest of ideas, and one that could be well received by the NZX. It certainly hasn't worked out that well under 100 per cent council ownership.

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