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Reforming Ports:  
Issues in the Privatisation Debate

by

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**TITLE:** Reforming Ports: Issues in the Privatisation debate

**ABSTRACT:** Privatisation and corporatisation strategies are part of an ongoing microeconomic reform program aimed at commercialising and raising efficiency in the public sector. Within this ethos, ownership and efficiency are perceived to be inextricably linked.

This paper examines port reform strategies implemented in Australia in recent times in particular in light of efficiency improvements. It raises also some unresolved social and policy issues associated with public ownership of commercial and profit oriented business and the provision of public good.

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## 1: INTRODUCTION

There is nothing particularly new in privatisation initiatives of one sort or another from governments of various persuasions - and as Wettenhall has argued so disparagingly, the current moves in Australia represent, '....the umpteenth wave in a long series of efforts to make government business behave commercially'<sup>1</sup>

Privatisation is about ownership - a privatised port like a privatised electricity authority or airport or shipping line or telecommunications agency - is one in which ownership passes from the public to the private sector.

But in the conventional wisdom - or more accurately the public perception - there is an implication that privatisation impacts positively on efficiency. Efficiency is perceived to 'suffer' because governments are concerned with serving masters other than the market - pressure groups and vested interests and constituents; and because there is the responsibility of governments to serve the 'public good' or the 'public interest'.

The privatisation of ports, then, is seen not simply in terms of transfer of ownership but as the transition of port authorities from statutory authorities or bodies of one sort or another serving 'the public good' to corporations seeking competitive advantage in a free-wheeling, unconstrained and competitive market place delivering significant efficiencies to the market.

In effect, **ownership and efficiency outcomes** are perceived to be inextricably linked.

In the Australian context reform initiatives for ports have taken on a variety of forms - from outright sale and transfer of ownership of the port *per se*, to the sale of particular assets or infrastructure or services, or to long term leasing arrangements; or in some cases state governments, unable to relinquish welfarist concerns and/or some measure of control, have opted for corporatisation or commercialisation strategies. These frameworks are variants of the privatisation model - perhaps not quite the bastard children of privatisation but certainly a corruption of a market focused model. In any case there is some considerable way to go to achieving the market-focused corporations which might be the end product of the privatisation process and to which we have referred above.

It is not surprising that in periods of significant policy change and the institutional instability that accompanies such change, it is all too easy to lose sight of principle for detail and to fail to distinguish between what can and cannot be achieved under varying reform scenarios.

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<sup>1</sup> Wettenhall, R. 'Public Administration Newspeak', *Current Affairs Bulletin* 66 (12) May 1990.

This paper is part of an ongoing research programme into microeconomic reform in the Australian ports and shipping industries<sup>2</sup>. It is the first of what is likely to be a series of papers assessing ongoing reform initiatives in Australian ports. It focuses, therefore, on the

actual and proposed changes to port authorities in various states; **and in so doing it attempts to define the central issues in the privatisation and corporatisation debate.**

## 2: BACKGROUND TO CHANGE

### 2:1 Pressures for change

In the Australian context the moves to privatise and corporatise ports emerged more or less simultaneously from two directions - from the perceived urgency to achieve significantly improved efficiency in the nation's ports; and from the need for governments, and particularly state governments, to rationalise structures and budgets. Government Business Enterprises (GBEs) came under particular scrutiny in Commissions of Audit in a number of states<sup>3</sup> and tended to be the focus of continuous monitoring<sup>4</sup>.

Ports, or more accurately port authorities, have been caught in the crossfire - as the nation's cargo handling agencies, they are expected to deliver operational efficiencies to their key players or stakeholders and particularly to shippers/cargo owners and shipowners; and as statutory authorities and GBEs they must conform to Treasury, Ministerial and Cabinet demands for financial viability.

It is hardly surprising then, that the reform outcomes of these competing pressures have been complex and varied and the resultant policy frameworks reflect the conflicts inherent in the two positions.

### 2:2 The reform process and port privatisation

In the context of the general process of microeconomic reform in the ports and shipping industries in Australia the moves to corporatise and privatise ports followed as more or less inevitable consequences of earlier maritime reform measures. Shipping reform, initiated by the federal government along the lines recommended by Crawford<sup>5</sup>, introduced measures to revitalise the Australian shipping sector. Shipping reform, however, was widely recognised as only a partial solution to an uncompetitive and costly national flag carrier as an inefficient waterfront also had a major impact on the efficiency of shipping.

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<sup>2</sup> The authors gratefully acknowledge the assistance of the Australian Chamber of Shipping and the award of the Chamber's Research Grant for 1995.

<sup>3</sup> Report of the Victorian Commission of Audit (1993)

<sup>4</sup> Steering Committee on National Performance Monitoring of Government Trading Enterprises

<sup>5</sup> Crawford, J.G. (1983) *Revitalisation of Australian Shipping: An Overview*, AGPS, Canberra.

The waterfront, and in particular waterfront labour, was subsequently reformed along the lines recommended by the Inter-State Commission (ISC)<sup>6</sup>. Waterfront reform led to a perceived, if not a totally effective, deregulation of the labour market with the introduction of enterprise based agreements and company based employment. The aim of the Commission was, in effect, to create a more competitive environment - an environment in which firms, particularly but not only stevedoring firms, could more effectively control the costs and conditions of their labour inputs.

The Commission also recognised the impediment to efficient port and shipping operations which was posed by inefficient and monopolistic port authorities and focused on their roles as effective administrative agencies. The Commission raised questions about whether or not there was an effective and legitimate role for the public sector in ports and, if so, what that role should be. The Industry Commission (IC) subsequently argued that port authorities should be granted autonomy from government and bureaucratic interference; that the role of the port authority was essentially that of a landlord and that commercial operations were best left to the private sector.

The port authorities themselves had, for the most part, begun to explore these issues more vigorously and some had taken initiatives not only to rationalise costs and pricing but also to examine more closely structural issues.

The upshot was that port administration and the structural and organisational frameworks of authorities - including questions of ownership - were locked into an agenda for change<sup>7</sup>.

### 2:3 Privatisation: ideology of the '80s?

In Australia, the 1980s was a decade where governments at both federal and state levels came under increasing pressure to perform. This coincided with widespread speculation and examination of the role of governments in commercial operations and focused in particular on the efficiency and cost effectiveness of GBEs. It was part of a philosophy held particularly in the private and commercial sectors, that Australia was over-governed and over-regulated. Governments were seen to be inefficient and costly. This changing philosophy reflected, by and large, economic recession, increasing unemployment and growing competition within the manufacturing sector from newly emerging industrialising nations in East and Southeast Asia.

State governments were under severe economic pressure and drastic reduction in government spending was called for. An ethos subsequently emerged accompanied by a strong push for deregulation and governments at both state and federal levels came under considerable pressure to withdraw from commercial activities or to make them profitable.

Particularly within the area of GBEs the push for reform intensified throughout the 1980s and early 1990s. Commercialisation, corporatisation and privatisation became widely accepted government strategies - that government enterprises had to be exposed to market conditions

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<sup>6</sup> Crawford, J.G. (1983) *Revitalisation of Australian Shipping: An Overview*, AGPS, Canberra.

<sup>7</sup> Industry Commission (1993) *Port Authority Services and Activities - Draft Report*.

and to competitive forces in order to make them efficient. Within the maritime environment, ports which had previously been seen as providing a service by public sector authorities now had to become efficient and competitive business operations. Ports were pressured to be profitable businesses operating under 'user pays' principles in order to ensure appropriate returns and maximum cost recovery.

### 3: STATE GOVERNMENT RESPONSES

What, then, have been the policy outcomes to date from these pressures for change?

Australian states have, as we have suggested above, subsequently embraced a number of different but closely related strategies - privatisation, corporatisation and commercialisation. Note briefly the fundamental differences between these rather broadly defined strategies -

- Privatisation is the transfer of public assets to the private sector. This can be accomplished by outright sale or lease. It can refer to the sale of an entire port, a port service or part of a port operation - a terminal, for example, or a tug or pilotage operation. Note well, in this context, that there will be significant differences in the complexity of procedures as well as in the implications and impacts.
- Corporatisation constitutes a corporate restructure. A public presence in the port is maintained, albeit much reduced. A government owned corporation is established essentially to undertake landlord functions. The adoption of private sector business principles becomes mandatory and, in most instances, all commercial operations in the port are transferred to the private sector.
- Commercialisation is that process where government retains ownership and control of the ports. The private sector undertakes many, but not all commercial activities. A port authority is maintained - one which operates not exclusively as a landlord but undertakes trade facilitation and other marketing and promotion roles.

All Australian states are presently undergoing port authority reform. Victoria is privatising its regional bulk ports and corporatising the port of Melbourne. With the exception of Western Australia and Tasmania, all other states are adopting some form of the corporatisation model. The following section will discuss briefly what strategies are being adopted in each state.

**Victoria.** Reform of Victorian ports began when the Port of Melbourne Authority and the port authorities of Geelong and Portland were declared Reorganising Bodies under the State Owned Enterprises Act 1992. Under this Act the state's ports were transferred to the Office of State Owned Enterprises.

In 1994 the Victorian Government announced that all four commercial ports would be privatised, but following intense opposition to the proposed sale of the port of Melbourne,

government's revised strategy was a dual policy approach - the corporatisation of the port of Melbourne and privatisation of the ports of Hastings, Geelong and Portland.

The impact of this strategy is that the port of Melbourne will be a public sector landlord with responsibilities for land within the port boundary. Onshore port assets in the ports of Geelong, Portland and Hastings will be sold outright although the underwater assets and associated navigational controls for these ports will be retained as public property.

Victoria's fourteen Associated Ports will be separated from the commercial ports and all non port related assets, such as the World Trade Centre, will be sold. Regulatory responsibilities will be undertaken by the Office of the Regulator General to ensure that non-competitive or monopoly practices are not abused.

The passing of the Port Services Bill in October 1995 by the Victorian state parliament divided the responsibilities of the Port of Melbourne Authority into three newly formed companies - the Victorian Channels Authority with responsibility for all channels in Port Phillip Bay and the ports of Melbourne and Geelong; the Melbourne Port Corporation, a public sector landlord with responsibility for land and berths within port boundaries; Melbourne Port Services with responsibility for the provision of ancillary services within the port such as cleaning, docking and security.

In January 1996 the Marine Board of Victoria took over responsibility for coordinating the clean up of oil spills in Victorian waters - this will be contracted out to the Melbourne Port Services. The responsibility for dangerous goods and responsibility for marine pollution investigations and prosecutions was transferred to the Environment Protection Authority in March 1996.

The first of Victoria's ports to be sold was Portland in February 1996 for \$30m. The successful bidder for Geelong is expected to be announced in April 1996 and industry sources indicate it will reap approximately \$90m - \$30m for the outright sale and \$60m held in reserve.

**New South Wales.** Reform of NSW ports began in 1989 with the introduction of the State Owned Corporatisation Act designed to commercialise the public sector. Under this legislation state owned corporations were to be established operating with minimum political and bureaucratic control similar to any other business in the private sector. They would be subject to Corporations Law and registered with the Australian Securities Commission. Under this legislation, each corporation was to have its own Memorandum and Articles of Association and have an individual share register. Their responsibility was to operate as efficient businesses, maximising the net worth of the state's investment, and exhibiting a sense of social and community responsibility in undertaking operations.

The introduction in 1989 of the Marine Administration Act created the commercial ports as separate authorities - the MSB Hunter Ports Authority, MSB Illawarra Ports Authority and the MSB Sydney Ports Authority. These authorities were designed to operate relatively

independently on a day to day basis but remaining under the umbrella of the MSB for capital borrowing and development planning.

The Board, since the passing of the Marine Administration Act 1989, has divested itself of non core activities and has seen itself increasingly focusing on landlord functions. It has, for example, withdrawn from commercial operations - since the closure of the Carrington Basin loader in Newcastle, the Balmain coal loader and the privatisation of the Port Kembla coal loader, all commercial operations in NSW ports have been undertaken by the private sector.

In July 1995 with the passing of the Ports Corporatisation and Waterways Management Bill, the ports of Sydney, Port Kembla and Newcastle were corporatised. This has meant the abolition of the MSB and the three port authorities. The further introduction in July 1995 of the State Owned Corporations Amendment Act has established ports not as state owned corporations but as statutory state owned corporations. Under this amended legislation port corporations are exempt public authorities for the purposes of Corporations Law.

The legal and administrative framework for the port corporations is designed to closely mimic that of a private sector company - a board of directors, share capital, issues shares and a memorandum and articles of association. But they are not subject to Corporations Law but to the statute under which they were enacted. This means that they do not have the freedom to operate as private sector operations and the political and bureaucratic control, rather than being lessened has, in fact, increased. But the amended legislation has also meant that the corporations are not unlike the former statutory authorities and less like a private company - this is evident in the scope of Ministerial direction, for example, the application of public sector employment, employee board representation and assigning to the Governor-in-Council the power to appoint chief executive officers etc.<sup>8</sup>.

**Queensland.** The Queensland Government embarked on a programme of corporatisation in May 1993 with the passing of the Government Owned Corporations Act and the Transport Infrastructure Act 1994.

The ports of Brisbane, Gladstone and Ports Corporation of Queensland were corporatised in July 1994 and in July 1995 the ports of Bundaberg, Rockhampton, Mackay, Townsville and Cairns were corporatised.

Corporatisation for Queensland ports means restructuring them to gain improved performance by adopting or expanding on business concepts used widely in the private sector.

Unlike NSW ports, the operation of Queensland ports is more aligned with those of private sector companies and there exists some ability to operate independently. Being government owned some government supervision must be maintained, however, but industry sources indicate that this is normally restricted to strategic directions and business activities of the corporations and the monitoring of performance.

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<sup>8</sup> Symonds Travers Morgan *Alternative Structural Models for the Management and Operation of the Port of Fremantle*, October 1995.



Under the Government Owned Corporations Act each corporation has two Shareholding Ministers representing the owners of the organisation - the government. In the case of port authorities, the Treasurer and the Minister for Transport assume this role. Shareholding Ministers oversee the government's interest in the corporation but independent Boards of Directors are responsible for the operation of the corporation.

Unlike the NSW model, the Queensland port authorities are not exclusively landlords - while the Port of Brisbane Corporation has transferred most of its commercial functions to the private sector, some of the bulk ports - Gladstone, for example - continue to be engaged in bulk handling operations.

The emphasis of reform in Queensland has been somewhat different and more commercially oriented, compared with some other states, and government has distanced itself from operational matters. Ports do require government approval for capital development but they can, after negotiating with users, set prices. The proviso does exist, however, that if they are under monopoly or near monopoly conditions they will be subject to a level of Shareholding Ministerial reserve power'.

Another area in which the Queensland model has differed from other states is its focus on trade growth, rather than on an increase in the rate of return achieved by either a considerable reduction in staff or by the sale of assets. Staff at the Port of Brisbane Authority, for example, was reduced by approximately 15 percent between 1988/89 and 1992/93. This compares with staff reductions of 54 percent at the PMA; 61 percent at MSB; 47 percent at FPA and 44 percent at SA Department of Marine and Harbours.

This does not mean that the Port of Brisbane Authority has been indifferent to financial returns. It does mean, however, that it has relied on revenue growth rather than cost reductions to drive improved performance. It also means that revenue growth has come from increases in trade and changes in trade mix rather than price increases.

**South Australia.** Corporatisation of South Australian ports followed the passing of the Public Corporations Act 1993 and the South Australian Ports Corporation Act 1994. Unlike, both the NSW and Queensland models, South Australian ports have been corporatised under a single corporation - the South Australian Ports Corporation (PortsCorp). PortsCorp was established in 1994 and is now responsible for all South Australian commercial ports taking over all commercial assets of the former Marine and Harbours Agency and the commercial operation and development strategies of the former Department of Marine and Harbours. Government has minimum day to day involvement in the running of PortsCorp although, being a corporation, it is subject to the control and direction of the Minister.

The Board of Directors, which is not elected but nominated by the Minister, is the governing body and answers directly to the Minister for Transport. Unlike other states, where reform has been almost exclusively Treasury driven, Treasury is not represented on the PortsCorp Board - although there is a Treasury observer present at Board meetings.

The Board is currently undertaking a series of reviews of PortsCorp activities. One of the early recommendations to the Minister for Transport has been the privatisation of grain loading facilities.

**Western Australia.** The Western Australian Minister for Transport has rejected both the privatisation and corporatisation models and is pursuing a strategy of commercialisation. Under this strategy ports will remain statutory authorities with trade facilitation being a major role - landlord responsibilities, however, will also be retained. Investigations are currently underway whether some commercial operations should be privatised. While statements on the role of ports and strategies have been released by the Minister, details of administrative and structural change are not yet available. The emphasis on port authority reform has focused on a coordinated approach amongst a number of relevant government departments, with the Minister and central government agencies retaining control.

In all states and under all reform strategies there has occurred a separation of commercial from non commercial operations. This will mean a more cost reflective pricing system. It also means that some non commercial loss making activities will no longer be cross subsidised, as has occurred in the past. In the future they will be funded separately by Treasury.

### **Tasmania**

At the time of writing Tasmanian ports continue to operate as statutory authorities. Tasmanian ports are intensely competitive and, in many instances, resources are under-utilised. Rationalisation of ports has been Labor Party policy in the past but the issue has been too sensitive politically to implement. The current state government is investigating whether or not to corporatise the state's ports but final strategies have not been decided upon.

## **4: REAL AND UNREAL EXPECTATIONS**

Privatisation and corporatisation strategies of one sort or another, proposed by or adopted by Australian states, represent something of a quantum leap, at least conceptually. For a long period of entrenched bureaucratic control and power centralised in state government departments or ministries have left a legacy of organisational and operational rigidities that are not easily exorcised.

How effective have these policy changes been, or are likely to be, given the relatively short time since implementation? Have they achieved the goals that might be expected from such strategies? Or at least, the goals as set out in the policy statements? In this section we focus on these issues.

### **4:1 'You can't have it both ways': limitations of the policy framework**

Recognise two broad policy prescriptions for port privatisation and related strategies -

- that the government - in the Australian context, state governments - or the public sector is involved, in some way or another, in the administration and control of ports. In effect, the policy framework will be either that of corporatisation or commercialisation. The private sector will play a greater or lesser role in ownership of particular assets, or services or segments of business activity; but control will be in the hands of government; or
- that the private sector, or 'business', will own and control 'the port'. Government's role will be restricted to that of 'governing' - it will act to preserve 'the public interest'; it will regulate where it thinks it appropriate for the common good; and it will pay an appropriate amount to preserve the social benefits of port operations - community service obligations, for example; or in some circumstances it may choose to induce trade and/or regional development by fiscal or other measures.

In any case, the choice of policy frame is clear - either the government or public sector is involved in the **direct control and ownership** of ports; or it is not.

In this context the important points are

- that the role of government will be different in the different prescriptions and
- that the operational and efficiency spinoffs will be subject to differing constraints under the different prescriptions

**It is important, therefore, in assessing the likely benefits or otherwise of privatisation and related strategies to fully recognise the limitations of the policy frameworks; and to note that once the policy frame has been set in place the options for better outcomes will be circumscribed.** In short, corporatisation by definition means public sector involvement; and public sector involvement means that the public interest criterion is the overriding issue and of central importance. Privatisation means private ownership; and private ownership means that the market place is the arbiter of corporate behaviour.

Note, however, that **the actual mechanism and framework of corporatisation** - how corporatisation is to be implemented or achieved - will also circumscribe the outcomes.

It is important, therefore, to bear this distinction - between the characteristics of the **ownership model** and the characteristics of **model implementation** in mind.

In a later section we will look in detail at the state outcomes of the implementation of these strategies; but in the next section we will explore in more general terms the perceptions of, or actual outcomes of, privatisation and related strategies.

4:2 Ownership - public or private?

The rationale for private ownership has been that private owners operate a port more efficiently because economic survival depends on long-run profitability. Private ports, consequently, are perceived to be more responsive to user needs, more aware of costs and more innovative than public sector ports where operating losses are absorbed by governments in any event.

Arguments for the retention of ports as public sector operations, on the other hand, point to the fact that governments traditionally play a developmental role in ports and provide facilities and services which may or may not realise full cost recovery except in the long term. In addition, in order to generate and sustain trade and associated economic activities, governments are held responsible for the provision of essential port facilities and services - it is frequently argued that this is more appropriately provided by the public sector. Indeed the Industry Commission argued that

‘seaports are integral parts of the nation’s transport system. Their location has had a major influence on the development of Australia’s capital infrastructure. Their operation then and development have implications which extend beyond the interest of any single entity or group of firms and as such there is a public interest in the development and maintenance of the major ports and facilities. This public interest in ports is the overriding rationale for the establishment and/or maintenance of public port authorities’<sup>9</sup>.

Nor are the concepts of privatisation and corporatisation new - despite the rhetoric of the 1980s and 1990s. Privatisation, in its many forms and guises, has occurred for much of this century. What is new about the current trend is the extent of government assets sales and the ideology that drives it - that private sector ownership is inherently superior to that in the public sector. What is also new about the latest developments is that it may be driven by the dire economic straits of the state government - the sale of government assets has become the means of government, not only ridding itself of the burden of loss making operations, but of lining government coffers.

Nor is corporatisation new - it has, in fact, existed since the nineteenth century. It can be traced back to the 1880s when state railway enterprises which had, until then, operated as ministerial departments were vested in a new kind of administrative body described as the statutory or public corporation. They were incorporated under its statutory charter as a body corporate and the action was a clear move to distance government business enterprises away from the rigidities and hindrances of standard public service and governmental processes and to allow them freedom and flexibility of private businesses.

What **is** really new about the current developments is the concept of a single jurisdiction-wide statute to provide the general framework for the establishment and operation of all public enterprises. In NSW the passing of legislation - NSW State Owned Corporations Act 1989 - was followed in every other Australian state and territory - the State Owned Enterprises Act 1992 (Vic), for example, and the Territory Owned Corporations Act 1990 (ACT). What is novel also is that governments of all persuasions are pursuing this trend.

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<sup>9</sup> Industry Commission (1993) *Ibid.*

Underlying the current developments is the belief that there is some homogeneity in all government activities that they can be, indeed require, similar treatment - they can and should all be reformed into commercial businesses. Whether they are ports, airlines, banks or electricity suppliers, they are treated in an identical manner - that, provided we subject them to the right treatment, all will be well.

Economic health and well being, however, are not the prerogative of private sector management practices nor a guarantee of success. Nor, as Wilenski<sup>10</sup> suggests, can we assume that private sector management is intrinsically superior to that in the public sector - we can learn from the private sector but cannot simply transfer those ideas and values from one sector to the other.

Indeed, private sector management strategies may not necessarily be what is needed to successfully undertake a government business. Public sector management, and public enterprise demands 'all the qualities, such as administrative flair, energy, readiness to accept responsibility, and knowledge of the principles of business organisation, that private enterprise requires of its people, plus something else ...' public good'<sup>11</sup>.

Nevertheless, it is clear that the track record of the public sector in the control of ports in Australia is not a felicitous one and among a range of inadequacies we note the following - though by no means an exhaustive list.

- **the failure to separate and distinguish between commercial and non-commercial operations.** Profitable operations have frequently subsidised loss making and non-commercial operations in Australian ports. The Port of Melbourne Authority, for example, cross subsidised losses incurred in Associated Ports in 1991 in the order of \$10.5m<sup>12</sup>; and over a long period of time NSW bulk exporters, particularly coal shippers, cross subsidised other, less profitable, areas in the ports;
- **the failure to identify community service obligations and to remove them from port authority budgets for direct funding from Treasury;**
- **the failure to remove non-core assets from port authority budgets and/or control.** The transfer of the World Trade Centre in Melbourne to the Victorian Department of Finance pending sale, for example, will relieve the Port of Melbourne Authority of a considerable burden. The Centre had an estimated market value of \$30m in 1992 despite the fact that the Authority had borrowed \$90m for its construction. Not only was there a significant gap between the market

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<sup>10</sup> Wilenski, P. 'Social Change as a Source of Competing Values in Public Administration', *Australian Journal of Public Administration* 47 (3) September 1988

<sup>11</sup> Wettenhall, R. 'Public Enterprise in an Age of Privatisation' *Current Affairs Bulletin* 69 (9) February 1993, p 9.

<sup>12</sup> Port of Melbourne Authority, *Annual Report 1991/92*.

value of the site and the actual cost of construction, but the Centre was a chronic loss maker incurring a loss in any one year in the order of \$14m<sup>13</sup>;

- **the failure to control staffing establishments and conditions and to pursue other than ‘soft’ labour policies.** The more recent shedding of labour by the Maritime Services Board in Sydney is indicative of the large number of employees in excess of needs and restructuring - from 3388 in 1984/85 to 650 in 1994/95. Substantial productivity improvements occurred - revenue earned per employee between 1984/85 and 1994/95 increased from \$79,500 to \$344,100 - an improvement of some 332 percent<sup>14</sup>. Operating losses of \$30m in 1988/89 were turned around to an operating surplus of \$90m in 1992/93<sup>15</sup>.

But are these problems a function of, or directly attributable to, public ownership?

The simple answer is that they are not; ownership is not the critical issue at all. The first three problems are pricing problems; they are a function of an inadequate pricing policy, not of who runs or operates the authority.

Nor is the fourth problem a function of ownership; it is certainly related to national industrial relations policies and to inadequate management policies and to entrenched practices - but it is not a direct function of ownership *per se*.

**There is, in fact, one fundamental attribute of public sector or government ownership - it is the assumed responsibility of social obligations; of delivering ‘the public good’; of organising and managing the totality or the resources of a port in such a way as to maximise the social benefits.**

But what is the ‘public good’? How is it defined? And how is it measured? And by whom? And clearly there will be conflicts between economically rational solutions and socially effective or acceptable solutions. It may be possible to induce ports to act ‘more commercially’ or more like ‘private enterprise businesses’; but they will not act as private enterprise businesses would act because they will not be subject to an unconstrained market place.

If government is to be involved in port ownership and control, then, the policy challenge is to ensure the ‘public good’ and at the same time to achieve the highest levels of operational and competitive efficiency. **Satisfying these dual objectives requires exceptional policy tuning.**

Private sector firms are, however, constrained by the market place; but they are not the least bit concerned about delivering the ‘public good’ (not that they may not be concerned about social obligations, it is simply not their prime responsibility or *raison d’être*.)

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<sup>13</sup> Report of the Victorian Commission of Audit 1993.

<sup>14</sup> Hayes, J.C. ‘Benefits of Port Reform in NSW’ paper presented at the Chartered Institute of Transport *Transport 1995 Seminar*, 8 August 1995.

<sup>15</sup> MSB Illawarra Ports Authority, *Government Micro-economic Reform Program 1994* and Maritime Services Board *Annual Report 1993*.

In this scenario, the policy challenge for government is to ensure whatever level of social equity and justice is seen to be appropriate without distorting market place mechanisms and the efficacy of the market. Again, careful policy formulation is clearly required.

In the next section we examine state policy outcomes for port privatisation and related strategies in the light of these issues.

## 5: ASSESSING OUTCOMES OF PRIVATISATION AND RELATED STRATEGIES IN AUSTRALIAN PORTS

### 5:1 Seeking efficiency?

The demand for micro-economic reform in Australia has been driven by economic necessity, ideology and political dogma and this push has intensified as the country's economic performance has deteriorated. The nation, and all states, have been under pressure. Governments, politicians and bureaucrats alike are committed to reform. Indeed, bureaucrats, particularly the 'new' breed of bureaucrats - the rational economists - have played a very significant role in the reform agenda. The demand for reform in Australia followed developments overseas and has been intensified by a general move to the right in the prevailing economic orthodoxy and the increasing numbers and political strength of economists in the bureaucracy. Gregory<sup>16</sup> argues that it has been the predominant element of economic rationalists within the bureaucracy that has convinced politicians and the public of the desirability of the policy - indeed, we are inclined to agree with Pucey's wry comment that Canberra was, over this period, 'swept by a locust strike of economic rationalism'<sup>17</sup>.

When governments want to privatise or corporatise or commercialise ports what is it that they really intend? It is not unlikely that they will have a number of agenda - an ideological agenda that suggests that all utilities should be run by government to ensure the 'public interest'; or alternately, an industrial relations agenda that 'buys out' of labour market rigidities by encouraging private sector ownership to 'rationalise' labour inputs; or a budgetary agenda that sees asset sales reducing public debt. One or all these agenda, and numerous others for that matter, may be embraced.

But governments will also argue for efficiency, for competition or for a more competitive market place; they will see 'efficient' ports as key elements in effective trading policies and in helping to create and sustain international competitiveness.

Conceptually, and in the best of all possible worlds, state governments will be seeking what is described in theoretical economics as Pareto optimality - an allocation of resources such that no consumer can be made better off without making another consumer worse off. It is a

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<sup>16</sup> Gregory, R.G. 'An overview of microeconomic reform' in P. Forsyth (ed) *Microeconomic Reform in Australia*, Allen & Unwin, Sydney.

<sup>17</sup> Cited in Gregory, R.G. *ibid.*, p306.

condition which, in a perfectly competitive market, achieves the optimal allocation of resources - or optimal allocative efficiency.

There are, of course, quite rigorous and unrealistic assumptions underlying the construct and the competitive model<sup>18</sup>. Nonetheless, the notions of economic or competitive efficiency as a function of competition and 'efficiency optimality' as an ideal condition of the market place, are important in establishing a normative or reference framework for discussion of the outcomes of privatisation and related strategies in ports.

Whether or not governments own or control the ports in one way or another or whether the private sector owns the port, the government will seek to achieve competitive efficiency.

In either case, any departure of the market from Pareto optimal allocation - or market failure - may (or may not) require intervention in the market place depending upon whether or not intervention will correct the misallocation and whether or not there is benefit in so doing<sup>19</sup>.

Imperfections in the market place associated with *entry barriers* - levels and structure of prices, conditions of entry and quality of service for example, *externalities* - which impose costs on other players - and *internalities* - where prices do not reflect costs for example - may invite regulation.

But there may be a dilemma - if the port is in private sector ownership the government will act as a regulator; if the government is involved in port ownership then self-regulation is called for - which raises the issue of who it is that regulates the regulator **for it may be entirely possible that the port ownership framework *per se* or its operating rules actually work against competitive efficiency.**

In the following section we will attempt to assess efficiency and other outcomes of the privatisation and related strategies and examine whether these conform with economically rational criteria.

## 5.2 Efficiency and competitive efficiency?

Aiken and Capitanio<sup>20</sup> argue that Pareto efficiency dictates that governments attempt to conduct their businesses through entities adopting private sector precepts. GBEs, however, operate frequently in monopoly markets providing essential goods and services. Community service obligations are imposed by parliament to ensure the general population has at least some form of equal access. And appropriate adjustments to "corporate behaviour" may need to take into account the purposes for which these entities were established by government.

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<sup>18</sup> See Samuelson P.R. *Economics, McGraw Hill, Tokyo*, Tenth Edition 1976, p 634 "under perfectly perfect competition where all prices end up equal to all marginal costs, where all factor-prices end up equal to values of marginal-products and all total costs are minimised, where the genuine desires and well-being of individuals are all represented by their marginal utilities as expressed in their dollar voting - then the resulting equilibrium has the efficiency property that you can't make any one man better off without hurting some other man".

<sup>19</sup> See D.S. Spulber, *Regulation and Markets* (1989) MIT Press, Cambridge Mass, p 3; but see also the Introduction and Chapter 1 for a useful discussion.

<sup>20</sup> Aiken, M. and Capitanio, C. 'Accrual Accounting Valuations and Accountability in Government: A Potentially Pernicious Union' in *Australian Journal of Public Administration* Vol 54 (4) December 1995.



The authors suggest that ‘if any of these entities can exist without any government intervention for welfare, then they may legitimately be privatised’<sup>21</sup>.

According to this reasoning there is a valid argument in favour of privatising some ports and they are likely to become more efficient as a result. Victorian regional ports, for example, consist essentially of privately owned and operated bulk facilities, often vertically integrated with other associated corporate activities and dedicated to a relatively small number of trades. These facilities are already efficient operations and the retention of a public sector port authority does little to enhance internal efficiency - it simply adds one more tier to decision making in the port hierarchy.

But in the case of corporatised ports the issues are not straight forward and while corporatisation should enhance internal efficiency of the corporation itself, it is not clear whether this will enhance efficiency in the port generally. Corporatisation is about the reform of port authorities - public sector bodies which have been transformed into government owned businesses. But irrespective of reform and the manner in which management has been restructured, they remain public sector agencies and retain ‘a public interest in the development and maintenance of the major ports and their facilities’<sup>22</sup>. Irrespective of how they are restructured, corporatised ports **are** government responsibility, they **do** have social and welfare obligations and they **cannot** be absolved from the responsibility relating to the ‘public good’. The reform of port authorities into private sector replicas cannot negate these responsibilities.

Port authorities were reformed and corporations created so that they could operate as businesses - independent from bureaucratic and political interference and the landlord port model was considered, in most states, the most appropriate strategy.

But have port corporations been established as effective landlords? And what is the relationship between ‘landlordism’ and efficiency? What is the role of a landlord and how does a corporatised port fit this role?

A landlord traditionally is the owner of assets which are leased out for a fixed rent<sup>23</sup>. NSW port corporations were established under the Ports Corporatisation and Waterways Management Bill 1995 ‘.....to operate the State’s port facilities in the major ports’<sup>24</sup>. The corporations, under this legislation, are not, in a strict sense, the owners of the ports, nor of port assets, but controllers of leases on behalf of the state.

Under the present system, however, they are landlords operating under some severe restrictions. They are not free to operate with any degree of independence; they cannot dispose of assets, they cannot embark on further development or improvements of assets or on new developments - at least, not without Ministerial approval!

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<sup>21</sup> *Ibid.* p566.

<sup>22</sup> Industry Commission 1993 *op.cit.* p39.

<sup>23</sup> The Concise Oxford Dictionary of Current English, Reprint of Fifth Edition 1975, Clarendon Press, Oxford.

<sup>24</sup> NSW Ports Corporatisation and Waterways Management Bill 1995

The rather restricted landlord role that has emerged is much more closely aligned with that of a service provider - port corporations generally now provide essential port services on behalf of government - but they are established as untenured service providers. There is no guarantee of permanence under present legislation as port corporations operate under a five year licence.

Traditional port functions such as the 'provision and maintenance of navigation aids, vessel traffic control, pilotage services, the dredging and maintenance of channels and hydrographic services' are undertaken by the port corporations under a five year licence issued by the Governor on the recommendations of the Minister<sup>25</sup>. The licence can be revoked at any time if performance is deemed substandard and offered to some other person or agency under contract<sup>26</sup>. This has presumably been to remove the comfort of a 'job for life' the public sector enjoyed in the past and to ensure the internal efficiency of the corporation. It will also establish the level playing field by removing benefits of government ownership, in accordance with Hilmer recommendations and conform to government competition policy. This will encourage corporations to provide an operationally efficient service.

The landlord model, then, is expected to deliver a revamped or restructured port corporation plus a number of commercial operators on leased port assets and a number of service providers. Effective competitive structuring of the submarkets - the terminal, towage, pilotage, stevedoring operations - should arguably provide a sound basis for operational efficiencies.

But there are two important problems.

First, there can be no guarantee that the requirements of the 'public good' or public interest constraints will not conflict with the private sector needs for corporate efficiency. Indeed, we can be quite certain that conflicts will arise; so that a company requiring more land, or particular infrastructure or different ways of operating will be confronted by decisions which may be determined by 'public interest' considerations.

This need not be a problem; companies will always face constraints for whatever reasons, on their activities. But the crucial issue is then not that a port corporation or a Minister must make a decision; but that the decision is, in fact, for the 'public good' - and not for short term political gain or expediency. In short, it is the quality of decision-making that is crucial.

Second, there is some considerable danger that 'landlordism' is a reactive rather than proactive framework for strategic development; that the landlord, with a preoccupation with a user-pays pricing framework and an almost exclusive focus on short term bottom-line results and with limited ability to do other than exhort private sector operators to be 'entrepreneurial', will pursue conservative investment and growth strategies. In fact, there has been altogether too little critical assessment of 'landlordism' as the appropriate model, particularly for regional ports. Effective port development in non-metropolitan and smaller metropolitan regions requires the ability to act proactively and to implement strategies that will capture growth. A

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<sup>25</sup> Ibid.

<sup>26</sup> Minister for Ports -Second reading speech

‘hands off’ landlord model in which the landlord has no detailed understanding of particular operations - which is certainly the case under many lease arrangements in Australian ports - is in fact likely to severely constrain effective strategic development.

It need not, of course, be so; but we will return to this point in the following section

### 5.3 Competition between ports

Many of the arguments in favour of reform focus on competition - that, quite simply, privatised and corporatised ports will be more competitive.

Indeed an essential feature of micro-economic reform is the concept of competition. Competition and the striving for it has become the driving force for change in Australian industries, including ports. Australian industries, the Hilmer report argued

‘have no choice but to improve the productivity and international competitiveness of its firms and businesses ... Competition provides the spur for businesses to improve their performance, develop new products and respond to changing circumstances. Competition offers the promise of lower prices and improve choice for consumers and greater efficiency, higher economic growth and increased employment opportunities for the economy as a whole’<sup>27</sup>.

The Australian governments’ competition policy has not recommended ownership changes *per se* nor has it included strategies to corporatise ports as such. What it is attempting to achieve is the establishment of government instrumentalities within the context of a more competitive environment generally. Ports within this context are encouraged to be competitive and by creating a non-protectionist environment<sup>28</sup> generally, place them on a similar footing as any other private sector organisation.

In what way can privatisation and corporatisation strategies enhance competition between ports? How much competition exists between Australian ports and how competitive can they really become?

Some competition does already exist between Victorian ports - up to 20 percent of Geelong cargo is ‘discretionary’ - that is it can be shipped through either Portland or Melbourne. Portland competes with Geelong and Adelaide for cargoes such as woodchips, grain, fertilisers and live sheep - each port using different marketing and pricing policies to attract trade. Geelong also competes with Hastings for some petroleum products. Privatisation of these ports and the adoption of more aggressive marketing strategies should intensify competition between them.

In other states there are also some instances of inter port competition. In Western Australia where Bunbury and Fremantle compete for alumina and steel billets and Port Hedland and

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<sup>27</sup> Report of the Independent Committee of Inquiry (1993) *National Competition Policy*, AGPS, Canberra (Hilmer Report).

<sup>28</sup> By the imposition of tax equivalent payments, for example, and the expectations of profitable performances.

Dampier compete for iron ore exports and the servicing of offshore oil and gas platforms. Some competition between NSW ports also exists but tends to be restricted to break bulk cargoes such as timber which can be shipped through either Newcastle or Port Jackson.

Clearly, bulk cargoes will, for the most part, move to the closest terminal - accessibility to ports and the cost of land transport will determine this. But the increasing flexibility of movement for containerised cargoes provided by new intermodal and shipping arrangements is inducing some competition between capital city ports.

But there is a more important issue - privatisation and corporatisation and commercialisation strategies engender competitive actions. Indeed, good business practice itself - quite apart from particular ownership frameworks - rests upon aggressive commercial posturing.

To what extent, then, has corporatisation in NSW provided the framework for competitive port managements?

It is arguable, again, that the constraints of the 'public good' or the public interest will inhibit competition - will, in fact, provide a framework for anti-competitive strategies. Legislation determines that it will be the Minister who determines resource allocation and infrastructure developments; it is the Minister, rather than the market, who will determine the competitive positioning of ports; it is the Minister who will determine what initiatives may or may not be taken and when.

Is it not likely, then, that the overriding guideline for development strategies in NSW ports - and perhaps ports in other states - will be risk aversion? Will the focus on politically correct economic rationalism result in too-conservative strategies that may be 'safe' in the short run but will depress long-run dynamism?

It need not necessarily be so; and again our argument underlines our earlier position - that the problem is not with a legitimate concern of government for the protection of the 'public good' or public interest but with whether or not the **decision** itself does in fact reflect the 'public good' - and not short term political expediency or political interest.

#### 5.4 Administrative structure simplified?

Reform in virtually all states has meant that ports, rather than operating independently and without undue political interference, are now subject to an intensification of central government control. Indeed, widespread concern has been expressed by most former port authorities on their diminished role; that reform is driven almost exclusively by Treasury and central government bureaucracies.

Reform in most states has meant that ports, rather than operating under a simplified bureaucratic structure, are in fact operating within a more complex one and this is impacting on internal efficiency and profitability. In NSW, for example, prior to corporatisation, all ports were under the umbrella of the former MSB. This comprised a head office with responsibility for corporate strategy and planning, finance and marine safety. The Board was managed by a Chief Executive who reported to the Portfolio Minister. Within this structure

there existed four subsidiary authorities functioning on a day to day basis with relative operational independence - there was one political master and one bureaucratic tier in the system.

The corporatisation of NSW ports and the separation of operational and policy responsibilities has meant the creation of a number of bureaucracies. Besides the three port corporations, a central controlling body has been established, the Office of Marine Safety and Port Strategy, which is the conduit between the port corporations and the Portfolio Minister. This office determines how port corporations operate. It issues licences to the port corporations to undertake navigation and other functions - licences which are presently, but not necessarily, issued to port corporations.

Apart from the additional bureaucratic structure, corporatisation in NSW has meant that ports now have two political masters - the Shareholders and the Portfolio Minister and within this structure the potential for conflict is inherent. The Shareholders, one of whom is the Treasurer, are concerned with profitability and return on government assets while the Portfolio Minister is responsible for efficiency and the operations of the port. But it is the Portfolio Minister who, in a sense, determines profitability for the Shareholders as it is the Portfolio Minister who sets port prices.

Industry sources indicate that conflict already has emerged between the Shareholders and the Portfolio Minister over profitability and return on assets. Conflict has also arisen over the size of the Office of the Marine Safety and Port Strategy. This is considered a top heavy, largely superfluous bureaucratic structure with numbers far exceeding requirement, costly and eroding profits<sup>29</sup>.

The establishment and maintenance of a large bureaucratic structure, such as the Office of Marine Safety and Port Strategy has also eroded revenue of port corporations. A newly imposed charge, the Port Cargo Access Charge, will be levied to maintain the Office. This, however, is not an additional charge on shippers, but replaces, in part, wharfage which previously was revenue flowing to the port authorities<sup>30</sup>. This has meant that some income of port corporations has been hived off in order to support a newly created, inflated bureaucratic structure.

Further fragmentation and separation of responsibilities has occurred with the establishment of the Marine Ministerial Holding Company to which has been transferred all 'non-core' port related assets. The establishment of this Company has also restricted the revenue base of the corporations. A rather narrow definition has been adopted as to what constitutes 'core' - this is almost exclusively cargo related. This definition has meant a loss of revenue for the corporations as revenue generating assets, such as the casting basin in Port Kembla and the cruise ship berths in Darling Harbour have been transferred to the Marine Ministerial Holding Company.

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<sup>29</sup> Personal communication

<sup>30</sup> *Ibid.*

Apart from financial, this also has marketing and promotion implications for the corporations. There is no surplus to which the corporation has immediate access. Indeed if port land is vacant for more than a year it is transferred to the Holding Company. Should the port corporation at some future date require the land for expansion it must then be purchased from the Holding Company.

Has port authority reform by way of corporatisation legislation thrown the baby out with the bath water? As far as ownership of port assets are concerned have we moved from one extreme to another? The former port authorities held vast quantities of assets. Industry sources have indicated that they were widespread; in some instances it was not known precisely what assets the MSB held. In other instances some assets had very little relevance to the operations of a port - the World Trade Centre developed by the Port of Melbourne Authority, for example. In other instances assets were derelict or land was held for decades or more, on the speculation that it may be required one day - these all had very serious pricing and asset valuation implications.

But under the present system, port corporations do not hold land for future development. Being expected to operate commercially they must have the responsibility for business development and expansion and it has been argued that not only has this development restricted their revenue generation but has impacted on their ability to market and promote the port.

## 5.5 Independence and control of ones destiny?

Can ports, given the legislative and political constraints, operate commercially and competitively? Have ports been granted the autonomy from government and bureaucratic control recommended by the Industry Commission? Are ports free to operate independently as businesses in the private sector?

Privatised ports, such as the Victorian bulk ports, will be able to operate independently from political and bureaucratic control and it is anticipated that, once the process is complete, they will be subject to regulatory constraints identical with those imposed on any other private sector operation. In corporatised ports, however, the degree of independence and control of one's destiny is determined by and written into the legislation. It is also dependent on whether the model adopted is interventionist or not. The Queensland model, on the one hand, appears to allow ports relative operational independence. The NSW model, on the other hand, is interventionist and has the Portfolio Minister in a pivotal role.

The NSW Minister for Ports, for example, has argued in Parliament that corporatisation of ports was 'about giving the ports a regional and commercial focus ... and the independence to allow them to control their own destinies'<sup>31</sup>. But corporatised ports in NSW do not control their own destinies; they cannot set prices; they cannot enter into contractual arrangements;

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<sup>31</sup> Minister for Ports Second Reading Speech

they cannot dispose of assets; they cannot develop new infrastructure - these issues all require Ministerial and central government approval.

If ports, then, cannot operate independent of government intervention, if they cannot be entrepreneurial in approach, if they cannot control their own destinies how commercial can they, in fact, be? And if they are not free from political and bureaucratic interference can we expect them to operate like a private business venture? Is it in any way meaningful to compare them with business operations in the private sector?

NSW ports, under present corporatisation legislation, cannot operate like private companies and it is a nonsense to suggest that they can. They were not established as private companies. Indeed amended legislation in NSW specifically determined that political control would be maintained - in some instances it has been intensified. The independence ports were to enjoy and their ability to control their own destinies were removed by the amended legislation and this was to maintain, or strengthen, and not reduce, political control. There is no doubt that this constraint will impede commercial operation and success.

## 5.6 The baby and the bathwater: a cautionary note

Self<sup>32</sup> has argued that the pruning of government activities along market lines, has led to the division of government into 'a host of public agencies, each providing a "service" to a particular set of "consumers" according to tests of business efficiency, and with a financial incentive to avoid any contribution for which it is not formally responsible'.

But, as Plowden<sup>33</sup> points out, these agencies are to provide public services with the authority and the resources of the state; and at the end of the day it is the citizens of the state - the broad polity and not some particular subset of it - that are the recipients of the so-called 'public good'.

There is some considerable danger that ports, operating within an inadequately defined and poorly implemented corporatisation framework and in a concerted and even well-meaning attempt to 'become efficient', may dispense with the baby as well as with the bathwater - that in the chase for short-term efficiency, medium to longer term benefits will be sacrificed. It is imperative that this should not be the case; and that appropriate mechanisms are set in place to prevent it from happening.

There are a number of reasonable propositions that suggest that if ports are profitable and efficient they will be contributing to the public good; and likewise, that if assets remain in the public domain, that if there is a reasonable return on assets, that if revenues and rewards of efficiency are redistributed to the citizens at large then ports will be operating in such a way as to be contributing to the public good.

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<sup>32</sup> Self, P. 'The consequences of reorganising government on market lines' in *Australian Journal of Public Administration* 54 (3) September 1995.

<sup>33</sup> Plowden, W. 'Public interests the public services serve: efficiency and other values' in *Australian Journal of Public Administration* 53 (3) September 1994.

But the public interest must also be served by defining for ports - both for individual ports as well as for clusters of ports or port systems - strategies which will be effective in enhancing both regional as well as trade development over the medium to longer term, strategic issues which are most likely to conflict with the pressures for short run efficiency and balanced annual budgets.

## 6: CONCLUDING COMMENTS

Privatisation models such as those being implemented in Victoria, remove government from ownership responsibilities and operations of the ports. In ports where trades and users are limited and there is no impact on public interest concerns, the sale of these operations and the complete withdrawal by government may be most expeditious.

Under a corporatisation regime, government has specifically chosen to retain ownership; but policy prescribes that government businesses will be profitable. A chronic potential problem in this strategy is that the ports must be operated as profitable businesses, but businesses in which politicians retain considerable control. Government ownership *per se* demands that ports are operated in the public interest - or that they are operated in such a way as to deliver the 'public good'; and it is this public interest criterion - not efficiency or competitiveness or any other attribute for that matter - that is the fundamental, distinguishing characteristic of the strategy.

Once this policy prescription is set the critical issue is how best to deliver the public interest or the public good? What sort of legislative and administrative framework will ensure appropriate outcomes?

Interventionist models - in which bureaucratic and ministerial control effectively remove the ability of ports to operate in the market place and, in fact, impose significant constraints on achieving competitive efficiency - do not deliver the 'public good'.





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