

Negotiation and Survival Strategies



Sam Ruda
Chief Commercial Officer

October, 2014

Topics for Discussion

- Trends in the Container/Port Industry
- Labor, Healthcare, Pensions and Fuel
- Some Financial Grounding
- Coping Mechanisms and Strategies



Key Trends in Container Shipping/Port Sector

Larger Vessels
and Alliances

Environmental
and Permitting

Financial Woes
of Some
Shipping Lines

Panama Canal
Expansion

Labor Costs
and
Productivity

Slower Trade
Growth

Cost of Fuel

Rail Economics

North America
Energy



The Top Carriers

	Operator Rank	Deployed TEU (owned/chartered)	Number of Ships
1	APM-Maersk	2,608,176	563
2	MSC	1,038,181	485
3	CMA-CGM	1,496,370	419
4	Evergreen	881,209	200
5	COSCO	766,094	154
6	Hapag Lloyd	754,994	154
7	APL	649,999	122
8	China Shipping	601,174	132
9	Hanjin Shipping	598,536	105
10	MOL	580,713	115
11	Hamburg Sud	474,077	106
12	NYK Line	470,869	105
13	OOCL	448,770	85
14	Yang Ming	384,320	87
15	Hyundai	364,584	61
16	PIL	357,053	164
17	K-Line	352,294	68
18	Zim	330,343	85
19	UASC	275,834	51



Top 3 Global Container Carriers

**-No
American
Company
in Top 30
Global
Carriers**

**-Europe
based
carriers
now
dominate**

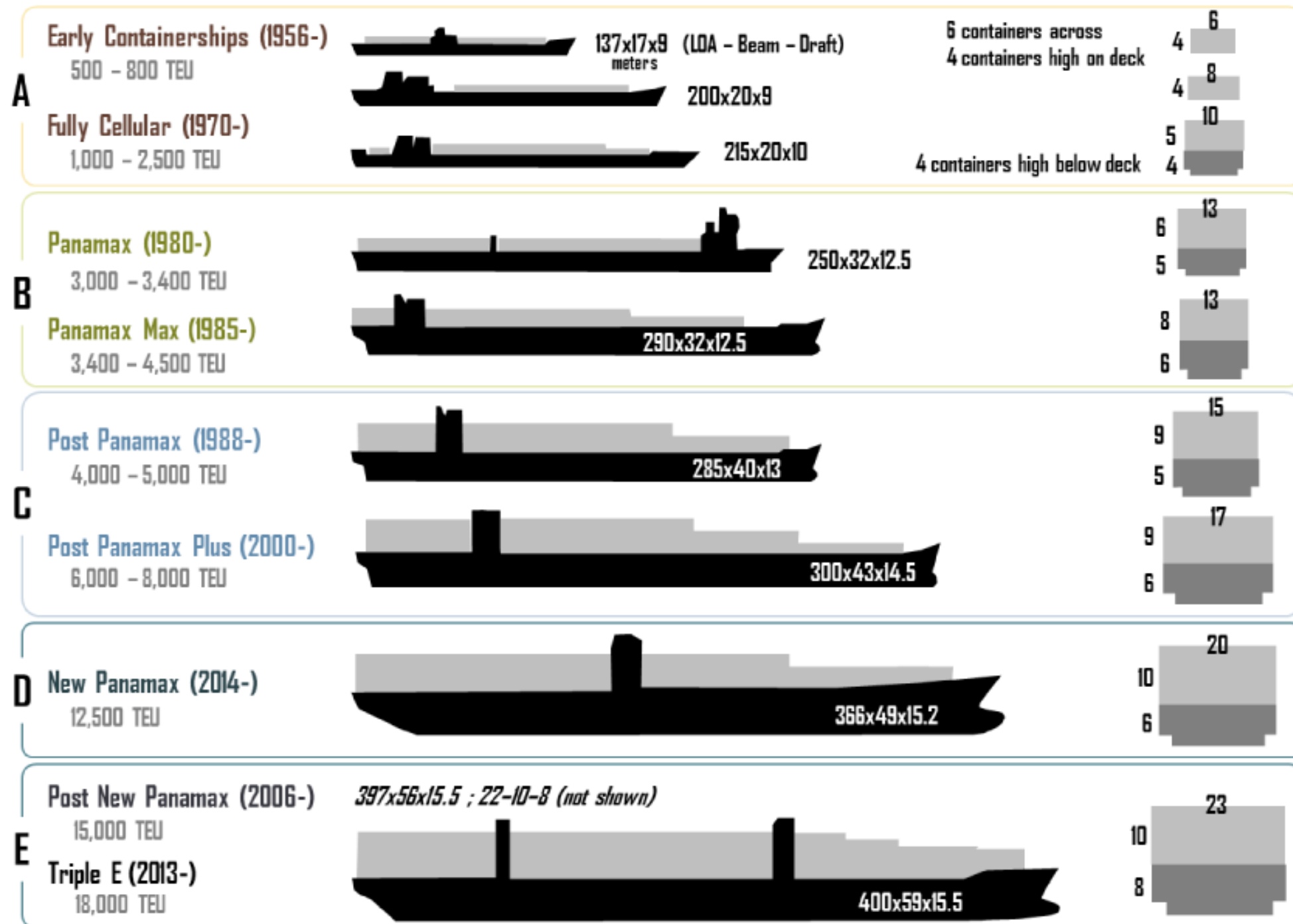


The Top Container Ports

Port Rank		2013 FY TEU	Growth % 2013/12
1	Shanghai	33,617,000	3.3
2	Singapore	32,578,700	2.9
3	Shenzhen	23,278,528	1.5
4	Hong Kong	22,352,000	-3.3
5	Busan	17,685,991	3.8
6	Ningbo	17,326,800	7.1
7	Qingdao	15,520,000	7.0
8	Guangzhou	15,309,200	3.8
9	LA/LB	14,599,145	3.4
10	Dubai	13,641,000	2.7
11	Tianjin	13,010,200	5.7
12	Rotterdam	11,621,249	-2.1
13	Port Kelang	10,350,139	3.5
14	Kaohsiung	9,937,719	1.6
15	Dalian	9,912,000	22.9
16	Hamburg	9,302,219	4.6
17	Antwerp	8,578,269	-0.7
18	Xiamen	8,007,900	11.2
19	Tanjung Pelepas	7,627,835	-1.2



Evolution of Container Vessel Size



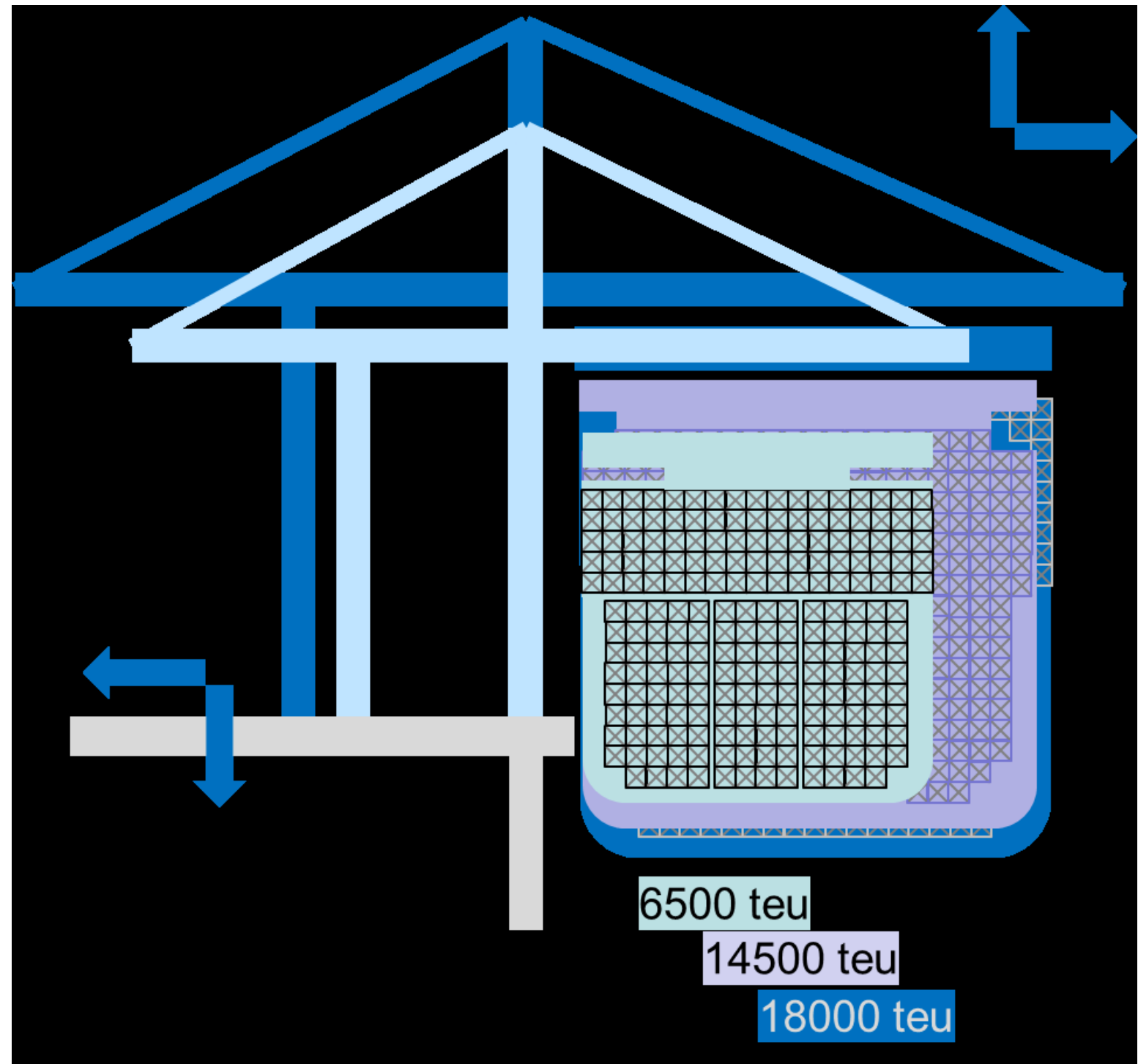
Vessel Size Particulars

Ship Size	Length (m)	Width (m)	Max Draft (m)	Rows Wide
12,000	365-380	48-50	15.5	19-20
15,000	400	56	16	22
18,000	400	59	16	23
20,000-25,000?	450	59-61	16.5	23-24



The Challenge of Ship Size for the Industry

- ☐ Taller Cranes
- ☐ Deeper Berths
- ☐ Longer Out-Reach
- ☐ Longer/Stronger Berths
- ☐ More cranes
- ☐ Air Draft
- ☐ Upgraded docks



Why larger vessels?

- Consistent and rapid rise in bunker fuel costs: fuel as a percentage of total costs are greater than 50%
- Speed no longer a key driver in service delivery
 - ✓ **Slow steaming to reduce fuel consumption**
- In theory, you reduce your per unit slot or TEU costs
- Ship building co
- Obtain greater efficiencies by calling fewer ports: load center concept
- Opportunity to reduce costs further through alliance agreements



New Alliances/Consortia Forming

■ P2 Alliance



+



■ G6 Alliance



+



+



+



+



Summary Observations For Ports

- Suddenly too many container ports (but not everywhere)
- Carrier landscape is shifting fast
- Cost of fuel is game changer
- For some Ports, the container business is driving risky investments
- Unresolved labor issues in the U.S. have long term implications
- Port leases, rates and charges are under pressure



West Coast Labor 101

- **Pacific Coast Longshore Contract Document (PCLCD): 2008-2014**
 - ✓ contract expires July 1, 2014 @ 5 PM
 - ✓ still negotiating
 - ✓ ILWU-PMA can keep current agreement in effect through mutual agreement as good-faith negotiations continue
 - ✓ ILWU consists of approx. 13,600 registered workers plus:
 - 4,105 pensioners
 - 959 on disability
 - 3,165 surviving spouses



ILWU Benefits 101

- ILWU benefits package includes health care coverage, a pension plan, a 401(k) savings plan, and vacation and holiday pay.
- For health coverage, registrants and retirees (and eligible dependents) generally have a choice between HMO coverage and a self insured PPO plan; new registrants enter a HMO for the first 24 months.
- **In either case, workers pay no premiums**
- **Total 2013 costs at nearly \$1.29 Billion**
- **Costs per active registrant is approx. \$93,200**

source: PMA 2013 Annual Report



How ILWU benefits are paid for?

Hourly Assessment		Tonnage		Assessments		
			Per TEU	General Cargo	Autos/Truck	Bulk
2005	\$15.71		\$14.79	\$0.870	\$0.065	\$0.017
2006	\$15.96		\$14.18	\$0.834	\$0.068	\$0.017
2007	\$ 17.72		\$16.46	\$0.968	\$0.078	\$0.019
2008	\$19.99		\$18.44	\$1.085	\$0.088	\$0.021
2009	\$27.01		\$24.40	\$1.435	\$0.116	\$0.120
2010	\$27.94		\$24.91	\$1.465	\$0.119	\$0.028
2011	\$28.40		\$24.57	\$1.445	\$0.117	\$0.029
2012	\$28.85		\$25.68	\$1.510	\$0.112	\$0.030
2013	\$33.98		\$29.38	\$1.728	\$0.140	\$0.034

- Tonnage assessments for containers do not apply to empties
- General Cargo is per revenue ton (2000 lbs/40 cubic feet/1,000 board feet)
- Autos are applied per cubic meter (average car=16 cubic feet)
- In 2012 container tonnage assessments contributed: \$474 million to the health and welfare costs
- In 2012 man hour assessments contributed at minimum: \$830 million to the health and welfare costs

Source: 2012 PMA Annual Report



ILWU Pension 101

	2012 Plan Year	2011 Plan Year	2010 Plan year
Valuation Date	July 1, 2012	July 1, 2011	July 1, 2010
Funded Percentage	61.1%	57.6%	58.6%
Value of Assets	\$ 2.869 B	\$ 2.633 B	\$2.522 B
Value of Liabilities	\$ 4.697 B	\$ 4.573 B	\$ 4.306 B

- Long-term structural issue of concern and one that is not unique to waterfront labor
- Near-term coping mechanisms **do exist**
 - raise man-hour assessments
 - raise tonnage assessments
 - portfolio gains in stock market (45% of portfolio in common stock/15% in real estate)
 - growing cargo volumes and increased labor hours?
 - rising stock market?

Source: ILWU-PMA Benefits Plan: October 2013
2012 Plan Year: July 1, 2012-June 30, 2013
Annual submission to PBGC



So labor is expensive: So What?

- Perhaps less a pure cost issue than a structural issue
- Costs are incurred by the move: Revenue is incurred by the box
 - ✓ Labor is paid by the hour/shift
 - ✓ Built-in system favoring low productivity
 - ✓ Less productive = more work
- Dispatching labor through hiring halls is inefficient and does not always match skill level with skill need
- Shift structure is inefficient and oddly inconsistent with “casual labor” concept
- Skill level that is needed is increasingly favoring craft trades



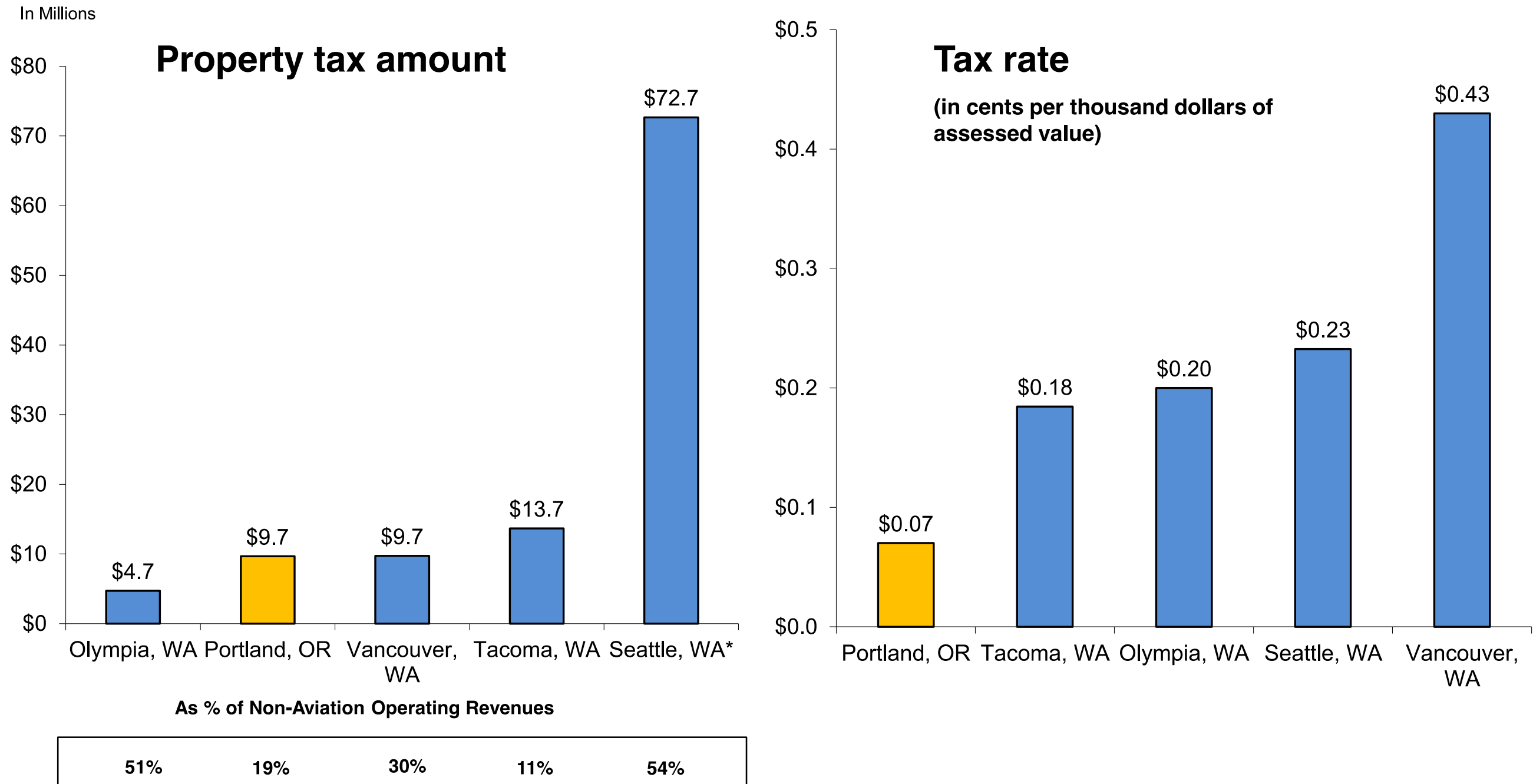
If we have time.....

- Let's talk about chassis in the U.S.
 - ✓ A good idea runs aground
 - ✓ Exposes major fault lines in labor jurisdiction
- Why can't carriers make money with chassis?
 - ✓ Airlines did not get out of the luggage business



Port's Property Tax Comparison

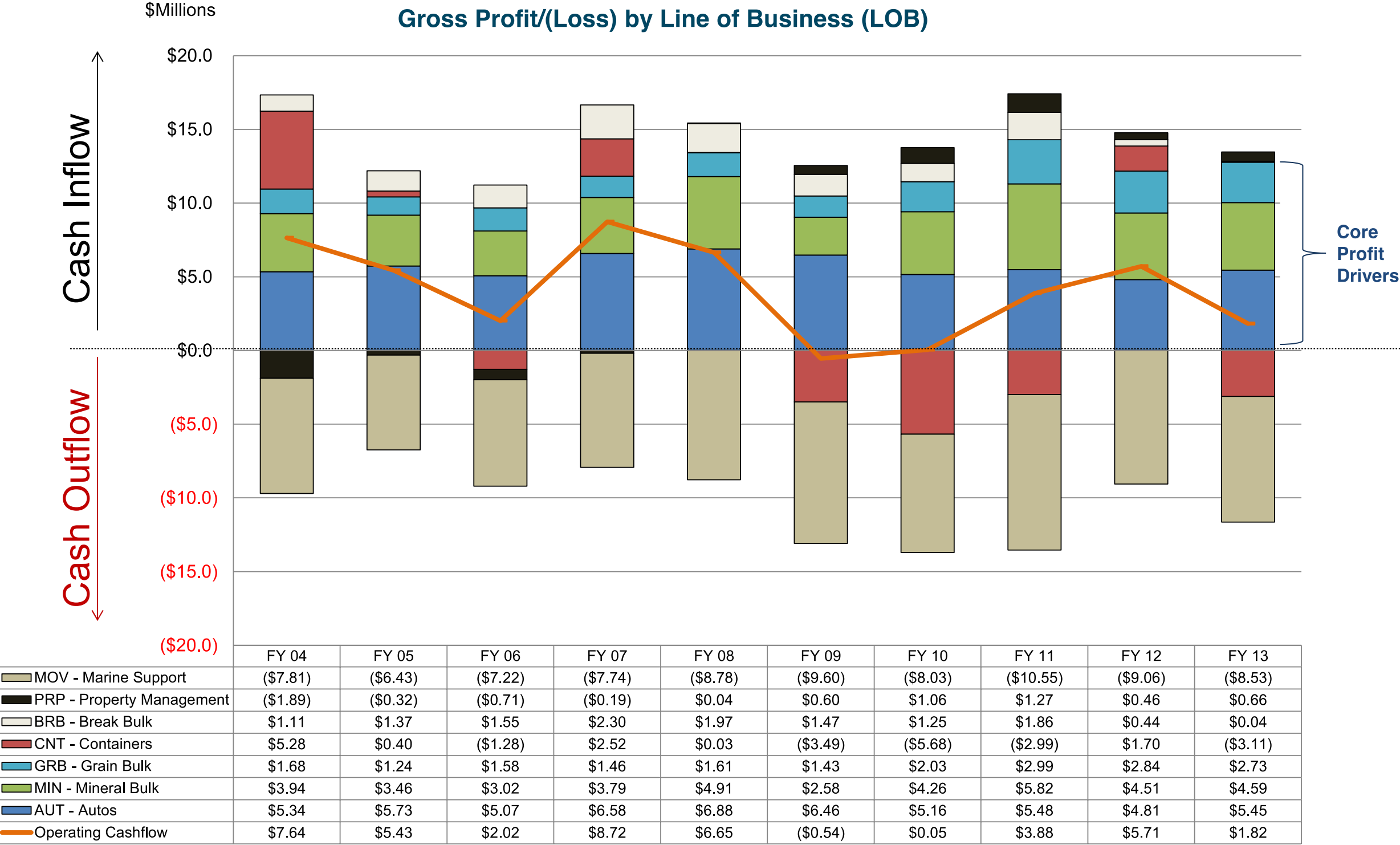
(Port of Portland's fiscal year July 1, 2012 to June 30, 2013; Washington Ports' fiscal year Jan. 1, 2011 to Dec.31, 2012)



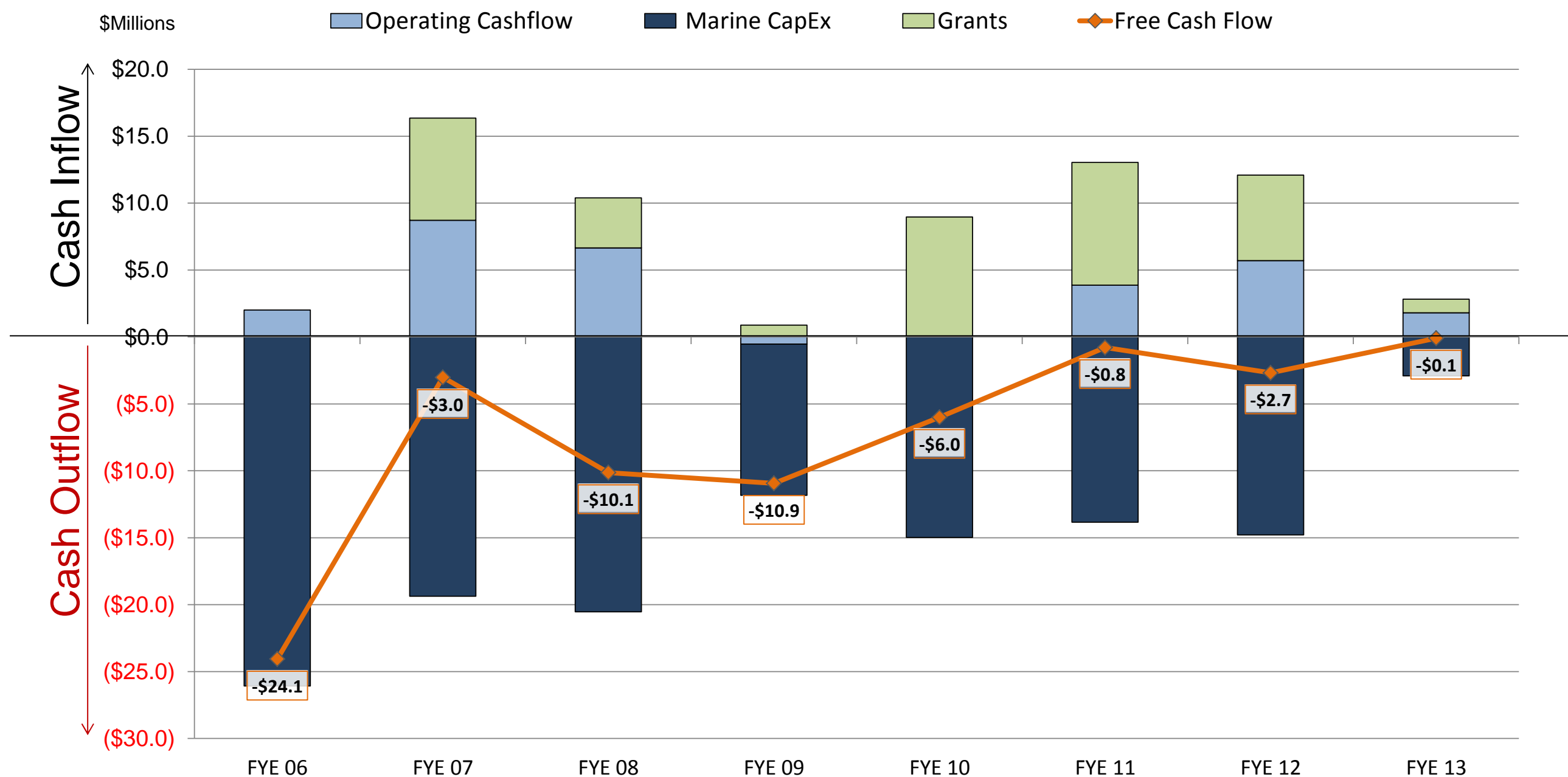
* Seattle FY14 maximum tax levy is \$93M



Cashflow Variability Largely Driven by Containers



Marine is Capital Intensive; Property Taxes Offset Negative Free Cash Flow



Summary

- Marine operating cashflow is positive but not sufficient to meet capital needs.
- Marine has to rely on property taxes and grants for investments into existing and new assets.
- Marine financial performance has stability from diversification.
- Marine's landlord operating mode results in high operating leverage, which means that with a high ratio of fixed costs to variable costs, a small percentage change in revenues will lead to a large percentage change in operating profits.
- Current leases present limited opportunities for revenue growth; but some growth opportunities do exist.
- Marine will benefit from new sources of stable revenues with high gross margins.



Strategic Response

- Focus on new business opportunities
- Grow with existing customers
- Leases must be based on “fair market” land basis
 - ✓ leases will have land rent component
 - ✓ leases will have dockage component
 - ✓ leases will have wharfage component
- Identifying Natural Growth Opportunities: Canada
- Energy Opportunities
- Let tenant invest



