

THE NORTHWEST SEAPORT ALLIANCE
MEMORANDUM

MANAGING MEMBERS
ACTION ITEM

Item No.	<u>5C</u>
Date of Meeting	<u>November 5, 2019</u>

DATE: October 22, 2019

TO: Managing Members

FROM: John Wolfe, CEO

Sponsor: Tong Zhu, Chief Commercial Officer and Chief Strategy Officer

Project Manager: Tom Bellerud, Director, Business Development

SUBJECT: **The 2020 Northwest Seaport Alliance (NWSA) Rail Cargo Incentive Program**

A. ACTION REQUESTED

Request Managing Members of the Northwest Seaport Alliance (NWSA) authorization for the Chief Executive Officer or their delegate to fund an IPI Rail Cargo Incentive at an initial level of \$2,000,000.

B. SYNOPSIS

The NWSA is experiencing a softening of container cargo in general, and specifically in the area of intermodal activity. Overall container cargo is tracking ahead of 2018 volumes by 4.1%. However, September volumes declined YOY by (7.1%). NWSA intermodal volumes have also experienced declines over the past two months, with August (5.1%) and September (7.9%). Further concern is brought to this topic through recent announcements by the major shipping alliances that The NWSA will be impacted by 17 void sailings in Q4, 2019.

C. BACKGROUND

Retention of cargo volumes is a primary objective of West Coast ports during this period of uncertainty which is seeing unprecedented tariff threats and shifting of manufacturing plants from China to S.E. Asia locations.

Sean Heaney, Senior Manager container research at Drewry and editor of Container Forecaster recently stated, “the weight of risks pressing down on the container market seems to be getting heavier by the day.”

In addition to tariff and trade implications on international traffic, The NWSA is also feeling the pressure of significant terminal expansions in both the Port of Vancouver and Prince Rupert, all designed to grow their intermodal rail cargo volumes.

The proposed IPI rail cargo incentive program, designed to be a year-long program, is a tool we can use to help stabilize our cargo volumes.

Depending on the degree of success achieved with this program it may require funding beyond the original \$2,000,000 request in order to be in place for the full twelve months. Staff will provide a mid-year update and advise if a request for additional funding will be required. Staff proposes this program would go into effect January 1, 2020 and run through the full year.

The need to offer the incentive plan for a full year has been a strong and consistent message from the ocean carriers. They have called out the lengthy and cumbersome challenges of changing cargo routings, only to see the incentive terminate after a couple months.

Projecting an all-in cost of this program is quite difficult during these uncertain times of international shipping, but staff consensus is the maximum payout should not exceed \$3,200,000, which will be offset by the incremental revenue generated.

If we were fortunate enough to approach these levels of pay-out, it would mean we have seen our IPI rail cargo volumes increase by well over 80,000 lifts annually, while other ports are currently struggling to retain their current volumes.

The NWSA staff is recommending an incentive package defined as follows:

- Each ocean carriers rail lifts from the previous year (2019) will be stated on a monthly basis to establish the base line for each.
- When the monthly rail lift volumes exceed the previous year total by 100 lifts, then each lift beyond the 100 growth will receive a \$40 incentive.
- Rail lift volumes will be measured quarterly, and incentive payouts will also occur quarterly.

D. FINANCIAL IMPLICATIONS

The NWSA generates variable income from intermodal volume through equipment rental and intermodal revenue in the South Harbor and through density MAG payments in the North Harbor. Additionally, the NWSA receives rail incentive funds from Tacoma Rail based on certain levels of throughput volume.

The proposed rail incentive is estimated to provide enough incremental income to cover an incentive program of approximately \$40 per incremental intermodal box. This is based on the historical pattern of cargo between the two harbors and forecasted profitability. There is risk if historical patterns are not maintained or if incremental volumes do not exceed certain volumes.

The Commercial team recommends that a \$40 per incremental intermodal box be implemented to improve our competitive position with other gateways offering similar incentives.

Source of Funds

Proposed rail incentive is estimated to provide enough incremental income to cover the incentive program. Actual expenses will vary, but no significant change in income is expected.

E. ALTERNATIVES CONSIDERED AND THEIR IMPLICATIONS

- **No Action Alternative:** Concern that further deterioration of our valuable IPI rail cargo product will occur. Current trends and outside influences indicate further decline would be likely.
- **Recommended Action:** Approve and implement the proposed IPI Rail Cargo Incentive with the goal of retaining and growing international cargoes through The NWSA gateway.

ATTACHMENTS TO THIS REQUEST

- Computer slide presentation.
- Draft Program
- Draft Agreement
- Memo

THE NORTHWEST SEAPORT ALLIANCE
MEMORANDUM

MANAGING MEMBERS
STAFF BRIEFING

DATE: September 25, 2019

TO: Managing Members

CC: John Wolfe, CEO
Don Esterbrook & Kurt Beckett, Deputy CEO

FROM: Tong Zhu, Chief Commercial & Strategy Officer
Project Manager: Tom Bellerud, Director, Business Development, Commercial

SUBJECT: The 2020 Northwest Seaport Alliance (NWSA) Rail Cargo Incentive Program

The on-going China-US trade war has caused a shift in production and sourcing from China to Southeast Asian countries as importers seek to avoid negative impacts from the tariffs. There is a considerable risk that importers may redirect more cargo through East Coast gateways with this geographic shift in markets. To retain our share of Transpacific trade and attract new discretionary cargo, staff would like to recommend a year-long rail cargo incentive program targeting ocean carriers starting January 1, 2020.

Attached please find a draft program description. Commercial staff is preparing a more detailed commission memo and plans to present the final draft to Managing Members for consideration on November 5th, 2019.

Two million dollars is the initial funding request for this program. Additional funding may be required to fund the program for the entire year. Staff intends to provide a mid-year update and will make a request for additional funding based on the actual rate of disbursement. Staff estimates the total funding request to be in the range of \$2 million to \$3.5 million.

For your convenience, below is a summary of the key elements of the proposed rail cargo incentive program.

The 2020 NWSA Rail Cargo Incentive Program

Term: January 1st, 2020 – December 31st, 2020

Target: International container ocean carriers

Qualifications (for international container ocean carriers):

- Be current in all accounts with NWSA
- Sign the participation agreement

Incentive: All Inland Point Intermodal (IPI) volumes in excess of the 100 incremental rail lift threshold over the base measurement (IPI volume during same month in prior year) will receive \$50 per lift, through December 31, 2020.

Payment Schedule: quarterly

Program Release Date (tentative): November 5th, 2019

Participating Agreement Due Date: December 15th, 2019



Item No.: 5C-supp
Date of Meeting: November 5, 2019

The 2020 Northwest Seaport Alliance Rail Cargo Incentive Program

Presenter: Tom Bellerud
Director, Business Development

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Background

- Retention of cargo volumes is a primary objective of West Coast ports during this period of uncertainty which is seeing unprecedented tariff threats and shifting of manufacturing plants from China to S.E. Asia locations.
- Sean Heaney, Senior Manager container research at Drewry and editor of Container Forecaster recently stated, “the weight of risks pressing down on the container market seems to be getting heavier by the day.”
- In addition to tariff and trade implications on international traffic, The NWSA is also feeling the pressure of significant terminal expansions in both the Port of Vancouver and Prince Rupert, all designed to grow their intermodal rail cargo volumes.
- The proposed IPI rail cargo incentive program, designed to be a year-long program, is a tool we can use to help stabilize our cargo volumes.

Background

- Depending on the degree of success achieved with this program it may require funding beyond the original \$2,000,000 request in order to be in place for the full twelve months. Staff will provide a mid-year update and advise if a request for additional funding will be required. Staff proposes this program would go into effect January 1, 2020 and run through the full year.
- The need to offer the incentive plan for a full year has been a strong and consistent message from the ocean carriers. They have called out the lengthy and cumbersome challenges of changing cargo routings, only to see the incentive terminate after a couple months.
- Projecting an all-in cost of this program is quite difficult during these uncertain times of international shipping, but staff consensus is the maximum payout should not exceed \$3,200,000, which will be offset by the incremental revenue generated.

Background

- If we were fortunate enough to approach these levels of pay-out, it would mean we have seen our IPI rail cargo volumes increase by well over 80,000 lifts annually, while other ports are currently struggling to retain their current volumes.
- The NWSA staff is recommending an incentive package defined as follows:
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 - Rail lift volumes will be measured quarterly and incentive payouts will also occur quarterly.

Financial Implications

Source of Funds: Proposed rail incentive is estimated to provide enough incremental income to cover the incentive program. Actual expenses will vary, but no significant change in income is expected.

The NWSA generates variable income from intermodal volume through equipment rental and intermodal revenue in the South Harbor and through density MAG payments in the North Harbor. Additionally, the NWSA receives rail incentive funds from Tacoma Rail based on certain levels of throughput volume.

The proposed rail incentive is estimated to provide enough incremental income to cover an incentive program of approximately \$40 per incremental intermodal box. This is based on the historical pattern of cargo between the two harbors and forecasted profitability. There is risk if historical patterns are not maintained or if incremental volumes do not exceed certain volumes.

Financial Implications

The Commercial team recommends that a \$40 per incremental intermodal box be implemented to improve our competitive position with other gateways offering similar incentives.



Alternatives Considered and Their Implications

- **No Action Alternative:** Concern that further deterioration of our valuable IPI rail cargo product will occur. Current trends and outside influences indicate further decline would be likely.
- **Recommended Action:** Approve and implement the proposed IPI Rail Cargo Incentive with the goal of retaining and growing international cargoes through The NWSA gateway.

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