



Commentary: Cato Can't Have It Both Ways

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The Cato Institute took issue with my recent commentary on the flaws in a 40-page study by a consultant concluding that container rates to Puerto Rico would decline 88.9% if there were no Jones Act. In neither the Cato rebuttal by Colin Grabow nor the companion commentary by Michael Hansen is any objection raised to my analysis that, when corrected for math and logic errors, the study would support only a 9.1% decline in rates. Indeed, Mr. Hansen fundamentally agreed with my critique and noted the rate reduction claimed in the study "can't possibly be true."

Their overriding issue was that I should have directed my concerns to the consultant who authored the study and that Cato shouldn't be held accountable for its errors. The distance Cato is now putting between itself and a consultant it gave 15 minutes of airtime — more than any panelist at its "Unnatural Disaster: Assessing the Jones Act's Impact on Puerto Rico" event at its D.C. headquarters on April 30 — is unusual. Prior to the event, they were fully aligned as Cato viewed the study as supporting its Jones Act agenda.

Mr. Grabow took umbrage with me saying Cato promoted the study, but he promoted it to me. In April 11 email to me responding to my points on his New York Post editorial, Mr. Grabow said, "Recent economic analysis found an economic cost to Puerto Rico of around \$1 billion" and included a link to the study. My understanding is that many folks received similar promotional emails from Cato. I reviewed the report and said the claimed savings looked fairly ludicrous, but I would have more to say after a closer read. In an April 16 email to Mr. Grabow, I outlined in detail four flaws evident in the study. My email concluded, "This is another example of why an analysis on hard and tangible cost differences from the Jones Act is preferable to a speculative — this is what the rates may be' approach."

That conclusion was a recurring theme in 18 email exchanges with Mr. Grabow, all of which also included his colleagues Mr. Ikensson and Ms. Manak, from July 2018 to June 2019. These three are the team involved in Cato's Jones Act project from the outset. I initiated my emails following statements, publications or events that mischaracterized costs known to me. Many were long, going into granular detail on actual costs based on my experience.

I repeatedly took issue with Cato's claimed building cost multiple, offering tangible actual examples to support my position. In fact, those multiples and related operating cost multiples were the only numbers Cato was putting forth as its "analysis" of the Jones Act. In addition to using a building cost multiple twice what could be proven in an apples-to-apples comparison, my larger point was that Cato should look at all of the costs in container shipping as the large

majority are unrelated to the ship. In an April 12 email to Mr. Grabow, I ended with: "Please become more acquainted with all the numbers in the domestic container shipping business, particularly cargo handling and terminal costs. Do your own detailed analysis, come up with conclusions based on that analysis and own those conclusions without referring to someone else's unsupported or dated report."

After I detailed for Cato five actual examples in which the average build multiple was 3.9, Cato continued to refer to a 6-8 multiple and indicated to me as long as it was in the CRS report, it would use it. I presented the same evidence to the author of the CRS report, and he formally retracted the 6-8 multiple as being too high. While I had hoped I wouldn't see that number referred to again, it was used in a June 4 presentation that is on the Cato website. They know better, and they knew better before the author retracted the number based on the same facts I gave them. The positions of a research think tank should be based on its own analysis of primary data and not on a daisy chain to someone else's conclusion. Throughout its Jones Act project, Cato has done too little of the former and too much of the latter.

When Cato chooses to incorporate the work of others into its crusade against the Jones Act, that work and all its foibles becomes theirs. That is particularly the case for a work product presented at an anti-Jones Act conference at Cato's headquarters. To embrace it when it works for you and then have nothing to do with it when it doesn't is disingenuous, and Cato can't have it both ways. I'm therefore missing the point that by not going into detail on the identity of the consultant, my commentary was somehow misleading.

Cato had the study for months before the event and my detailed observations on its flaws for weeks before the event. It had plenty of time to vet the study and presumably would have looked at it again following my observations. By moving ahead, they further embraced the study. The only response to my observations was an April 16 email from Mr. Grabow that said, "Thanks for your comments and critique. Just so you know, John Dunham will be speaking at Cato on April 30 about the Jones Act's impact on Puerto Rico. You are more than welcome to attend in person and make some of these points during Q&A." Obviously, Cato was fully aware of and aligned with the study. My observations weren't challenged, nor was I requested to provide the same to Mr. Dunham. Upon reading the study, I sent a LinkedIn invite to Mr. Dunham with a message that I had some observations on his study. No response.

I'm confident my own facts are in order and my commentary included no inaccuracies. Mr. Grabow knows that I have always viewed changes in costs as a percent of revenue as the most objective benchmark upon which to determine the rate impact of any Jones Act repeal. Costs are hard and tangible and verifiable. The differences in the annual capital cost and crewing cost of the vessel as a percent of annual revenue is the best window into that impact as those are the costs impacted by the Jones Act.

One reason I see a direct connection from cost change to rate change in the Puerto Rico trade is the low profit margins historically. As I've shown Cato, the one Puerto Rico carrier with audited results publicly available has reported an average profit margin of 1.5% over the last five years. You can't give up what you don't have. To depart from using tangible and verifiable cost change numbers to hypothetical rate scenarios is speculative at best and often sophistry. That is a philosophical divide that has separated me from the studies Cato has referenced.

Mr. Grabow will recognize that this divide is the basis for me claiming that Cato sees the rate impact going beyond the cost change. Of note, in response to an email I sent to Mr. Grabow on December 18 (In part it said that "maybe Cato would still be against the Jones Act if it saw it adding just 10% to total container costs, but I suspect its passion on the subject would dissipate. However, the 10% is in fact close to economic reality and as I've noted before, it will also come with potential unintended consequences."), his response seemed to agree with my cost estimate. His response said in part that "as for your 10% Jones Act premium, that certainly seems within the realm of possibility in some instances."

Both of the rebuttal commentaries latch on to a view that my estimate of a 12% decline in costs flowing through to a 12% decline in rates with no Jones Act is somehow incompatible with an immediate shift to foreign carriers. Their logic is that if I believe the latter will happen, I must really think rates will go down more as a "minor" rate decline of 12% couldn't result in that much upheaval. That view belies their understanding of the economics of the Puerto Rico container shipping market. For instance, a 12% rate decline for a carrier with an average profit margin of 1.5% over the last five years is a major and permanent structural change that challenges their viability.

Based on my experience, I don't believe any existing business model would survive a repeal of the Jones Act. In terms of which foreign ships would replace the displaced carriers, the boxes will go to the services with the best underlying relative cost economics. That will be largely driven by vessel size, minimal deviation to add a San Juan call and how existing deployment imbalances fit with the Puerto Rico trade. All of those tangible cost metrics clearly favor South American carriers over Caribbean carriers.

Following the April 30 presentation, I left a summary and worksheets with Mr. Grabow and the panelists that included details on the points I made. In the days following the conference, I sent two detailed emails that included observations on what was presented at the conference. Those emails included expansive worksheets that laid out in a transparent and auditable fashion the key points I was making. Until last week's rebuttal in *American Shipper*, none of the points I made about the Puerto Rico container market had been challenged by Cato.

I'm a strong proponent of solid fact-based analysis, and my view is that such analysis should be grounded in verifiable numbers. My direct observations on factual mistakes in the study would seem to fit squarely within the category of rigorous debate that Mr. Grabow said Cato embraces. However, on the Jones Act, Cato's publications and events have been long on adjectives and short on relevant numbers. Issues related to the Jones Act are too important to let inaccurate analysis miss the mark by a nautical mile.