CANEGROWERS

COMMENTS IN RESPONSE TO

PRODUCTIVITY COMMISSION

DRAFT REPORT on

Impact of Competition Policy Reforms on Rural and Regional Australia

and

ISSUES RAISED AT THE 12 JULY 1999 HEARING

It is encouraging that there is the opportunity to provide comment on the initial report and findings of the Productivity Commission as it is the experience of CANEGROWERS that open lines of communication most often lead to the best achievable outcome of mutual benefit to all stakeholders. This opportunity to continue an open line of communication is particularly important for an issue as topical and controversial as the impact of National Competition Policy on rural and regional Australia.

CANEGROWERS believes that some of the draft report and findings reflect the current situation and it would be encouraging if some of the recommendations were accepted. However CANEGROWERS believes that there are significant areas and findings in the draft report which it is necessary to further explain and adjust to reflect the experiences of rural industry, particularly the sugarcane growing industry.

In providing these comments to the Productivity Commission, CANEGROWERS will concentrate on three main areas, namely the marketing issues raised in Chapter 7 of the Draft Report, the water issues raised in Chapter 5 of the Draft Report, and the assistance measures raised in Chapter 14. Comment will also be provided in response to specific issues requested by the Productivity Commission in the draft report and at the hearing attended by CANEGROWERS at Toowoomba on 12 July 1999. Where appropriate, reference will also be made to CANEGROWERS original submission to the Inquiry.

WATER ISSUES (in Chapter 5 of Draft Report)

Sugarcane growing is the largest user of irrigation water in Queensland, making use of approximately 40% of this state's irrigation water resource. About 75% of the sugarcane crop tonnage is irrigated. CANEGROWERS, as the representative organisation of the 6500 sugarcane producers, is therefore able to provide well informed comments in relation to water issues in Queensland, specifically related in this case to national water reforms.

Table 5.3 provides a reasonable assessment of the current position and level of progress. Although it may appear that this state lags behind others it is important to emphasise that progress is being made and any attempt to rush or curtail the progress would have undesirable and inequitable outcomes. To arrive at outcomes which are mutually acceptable will take time, and much longer than originally intended when the reform agenda was established.

Further comments on the Rural Water elements in Table 5.3 are as follows:

full cost recovery - this is in the process of implementation; there has been the first round of negotiations with all districts by the Water Reform Unit; the first tranche of the price increase to full cost recovery will be around August - September.

rate of return - for this to occur there is the need to determine costs of the scheme. State Water Projects, irrigators and the Water Reform Unit are negotiating on costs and expect to finalise these with the next two months

Water property rights - a trial is occurring in the Mareeba - Dimbulah area;

Water trading - water trading is available in the Mareeba - Dimbulah area; temporary trading has been available in all areas for around five years.

CANEGROWERS therefore supports a slightly amended Recommendation 5.1 of the Draft Report which states that "*All benefit - cost studies of major new water infrastructure investments should be publicly available and should clearly identify the nature and magnitude of any social (including environmental) benefits* and costs", with the amendment that costs as well as benefits should be clearly identified. However it is recognised that intergenerational environmental costs are difficult to establish and incorporate.

The Commission has invited comment, through the draft report, on the issue of depreciation and infrastructure refurbishments. **CANEGROWERS believes that depreciation should not be included**. To include depreciation as well as a provision for infrastructure refurbishments would in essence be costing twice.

CANEGROWERS believes that to maintain the infrastructure at a standard acceptable to customers, it will be appropriate for provision of a cost of refurbishment charged on an ongoing tax free annuity basis. It is noted that currently there are no arrangements in place for tax free arrangements. Further, elements such as these are often incorrectly treated at income.

CANEGROWERS resubmits the recommendation on page 14 of this organisation's submission to the inquiry, that **a review be established to properly identify the actual cost for rural irrigation water.** This is particularly important to establish community service obligations and head office overheads.

Further, such a review could encompass an identification of the benefits of irrigation schemes. It is important to realise that there are many beneficiaries of irrigation schemes, not just the primary industry users of the water. A review would be valuable input into the reform process.

Given the input of a review of costs and benefits of rural irrigation water into the review process, it therefore follows that further time is required for water reforms. **CANEGROWERS therefore strongly supports an amended recommendation 5.2** which states that "*COAG should give consideration to the formal extension of the rural water reform timetable for the implementation of water property rights and environmental allocations* which would allow for the formal consideration of adjustment assistance and/or compensation". As well as the extension of the timetable, say by five years, there should also be recognition of adjustment assistance and compensation.

At the Toowoomba hearing on 12 July, CANEGROWERS was requested to provide some information in relation to irrigation schemes. The information which was able to be obtained within the short timeframe from the hearing date to the date of submission of these comments is provided in Attachment 1. Current water prices can be obtained by the Commission from the Queensland Government Gazette.

In response to the request of the likely price for water at the end of the reform process, it is not possible at this time to provide an indication because the costs are currently undefined. However a more clear indication may be able to be obtained by the start of the new year.

MARKETING ISSUES (Chapter 7 of Draft Report)

As mentioned in CANEGROWERS 6 November 1998 submission to the Inquiry, the Sugar Industry Review Working Party examined aspects of the Queensland and Australian raw industry, particularly legislative aspects, guided by the principles of National Competition Policy. In carrying out the Review and in implementing the Review Recommendations the sugar industry has experienced what can be described as a great deal of pain.

This pain has been felt to different degrees in the different sugarcane growing areas of Queensland. For example, the removal of the pool price differential has been most adversely felt in the North Queensland sugarcane growing areas. This area has also experienced the effects of low productivity, cane grub damage and exceptional weather conditions. The changes from the Sugar Industry Review, which stemmed from NCP principles, are viewed by many growers in that area as the straw which could break the camel's back.

A positive outcome from the Sugar Industry Review has been the acceptance of the recommendation that there be no further reviews of the sugar industry for at least 10 years. This is viewed favourably by the sugar industry as it gives transition and adjustment time as well as reasonable time to view the effectiveness of the new arrangements in the raw sugar industry.

While that recommendation has been accepted, there is still anxiety in the raw sugar industry over the Sugar Industry Review recommendation for the continuation of the single desk seller arrangements for marketing of Queensland raw sugar. Mention on page 184 of the Draft Report of doubt about the single desk adds to the anxiety.

It appears as if there is a perception by certain groups that the sugar industry got in wrong in recommending continuation of the single desk, and that is should have to continue to justify the public benefit of this action again and again.

CANEGROWERS remains wary of the Hawker Committee recommendations on page 182 of the Draft Report that reviews should be conducted completely independently. We believe that the Queensland Sugar Industry Review process is was a good model which allowed consultation and input. There was industry involvement to provide explanatory advice, and there was the backup of independent consultant advice.

However there was some confusion, particularly in relation to status recommendations.

The Commission on page 192 states "In practice, it is difficult to demonstrate that single desk selling arrangements have (or have not) increased export returns." CANEGROWERS disagrees with that statement as applied to the Queensland raw sugar industry arrangements. The process and outcomes of the Sugar Industry Review have clearly identified that there are benefits. This has been a very costly process, though.

Another comment in relation to marketing issues concerns a statement on page 192 of the Draft Report: "*In principle, if a single desk seller is to extract a premium for export markets it must be able to control export supplies to the extent that it can influence world prices*". CANEGROWERS believes this statement is not completely correct. The Queensland raw sugar industry situation is able to extract a premium for export markets, however by no means does the Queensland industry influence world prices. It should be understood that premiums can be extracted if certain elements of the world market, and not just world prices, are influenced. For the Queensland raw sugar industry, there is the ability to influence supplies and therefore price of raw sugar in Far East (Asia) region.

The draft report goes on to state "*removal of single desk seller arrangements would not have a significant effect on the prices realised in overseas markets or producers' returns and the regions in which they reside*". This statement appears to ignore the existence of customer relationships.

Specifically in relation to costs, CANEGROWERS notes that there is not any mention of transaction costs for the NCP influenced reviews and associated implementation of recommendations. CANEGROWERS estimates that direct costs for its review were in the order $2 million, with an additional $2 million at least in meeting costs borne by the participants. Implementation since then could cost up to an additional $1million. This is significant when it is considered and compared with modelling done by Monash University which suggested that removal of the tariff resulted in an increase of economic welfare by $1 million per year.

Further, CANEGROWERS believes that there is an assumption that markets transfer benefits. As shown in the following section with the attached chart this is debatable (note that this section is in response to a Productivity Commission request on page 198 in the Draft Report)

<u>Sugar price transmission appears to be inelastic</u>

Prior to July 1997 domestic purchasers paid the tariff component of the import parity price, at that time about AUD 35 per tonne (after taking account of the Developing Country preference).

Leaving aside the (relatively minor) movements in the difference between notional import freight and actual domestic freight, and leaving aside the significant benefit to domestic producers which has flowed from the removal of the tariff, domestic raw sugar purchasers have directly benefited from the fall in world sugar prices of approximately A$170 per tonne, a fall of some 52 per cent since July 1997.

There is no publicly available data on industrial refined sugar prices, nor is there a comprehensive, practically available database on the prices of sugar containing products. However casual observation of retail prices would suggest that little, if any, of the substantially lower prices now being received by raw sugar producers for their domestic sales is flowing on to domestic consumers. Attached is data relating to retail prices of refined sugar, chocolate and biscuits (Attachments 2, 3 and 4). Additionally a graph of world raw and white sugar prices and domestic raw prices, together with Australian retail white sugar prices is attached for information (Attachment 5).

On the basis of this data, the transmission of falls in the world sugar price to domestic retail prices and prices of sugar containing products appears to be highly inelastic. The benefits of reform in the raw sugar price setting mechanism, switching from import to export parity appears to be captured in the downstream processing sectors and not by final consumers.

Further comments

While the Queensland raw sugar industry has struggled during the NCP influenced Sugar Industry Review and implementation of the recommendations, it is imperative the NCP process continue to other sectors. Particular focus should be on the textiles/ clothing/ footwear and motor vehicle industries.

Assistance (in Chapter 14 of the Draft Report)

The Commission has considered the effectiveness and appropriateness of current assistance measures. CANEGROWERS has provided comment in response to some of these issues at the 12 July hearing at Toowoomba. Re-emphasising and extending on these, CANEGROWERS has concerns about the existing assistance measures, particularly in respect of eligibility.

CANEGROWERS does agree with the summary point on page 343 which states "*it is important to recognise that adjustment assistance should focus on helping individuals to meet a changing environment. It is not about stopping change or maintaining all existing communities*". This is specifically in relation to adjustment for managing change associated with NCP influenced reforms.

However, give the experience of CANEGROWERS and other groups with existing assistance measures other reasons (such as for managing assistance required as a result of weather influenced conditions), it is debatable whether these schemes would be suitable to manage adjustment for NCP influenced reforms.

CANEGROWERS therefore does not support recommendation 14.3 which states "Governments should rely principally on generally available assistance measures to help people adversely affected by NCP reforms". An approach should be to develop new initiatives to deliver assistance which would improve the eligibility criteria and be more targeted in line with the focus of the assistance being on managing change.

CANEGROWERS notes that the Queensland Farmers' Federation has made comments in relation to assistance. CANEGROWERS concurs with those comments.

Bulk Fuel

At the hearing at Toowoomba on 12 July, CANEGROWERS was requested to advise if it is possible for sugarcane growers to access bulk fuel depots. Based on the responses received in the short time from the time of the hearing to the time of the written submission, it appears though generally growers do not have access to depots due to the various licensing and other requirements in respect to fuel transport.

Concluding Comments

CANEGROWERS looks forward to continued communication with the Productivity Commission and welcomes the opportunity to further explain issues in these comments and in the submission to the original inquiry.

July 1999

ATTACHMENT 1 - Responses to Irrigation Questions Raised at 12 July 1999 Hearing

Area	Progress of Reforms	Water Price Now	Expected Water Price at Conclusion of Reforms
Burdekin	Interim Local Management Committee formed and this is discussing the 5 year price path with the Water Reform Unit. Waiting on revenue cost data for 1997/98.	$38.60/ML	The Committee believes this should be less than $38.60/ML if based on full cost recovery however Water Reform Unit indicates that there will be no reduction where the price is in excess of the full cost recovery. Concept of cost recovery is agreed to be appropriate provided it is based on actual figures for operational, maintenance and refurbishment costs. Should be zero rate of return and no head office overheads or sums to cover inefficient management should be included.
Proserpine	Hoping to meet soon with Water Reform Unit. Would need to go through WAMP process before local management can be introduced. Currently the Proserpine River Irrigation Area gives an ROI to the State.	For 1999/2000: Allocation charge - $3.00/ ML Water Usage Charge - $8.70/ ML Mill area levy (paid by growers) - $1.60 per ML Total - $13.30/ ML	Similar to current, increased by CPI if there is any change. Current price covers operating, maintenance, administration and refurbishment costs.
Mackay	Pioneer Valley Water Board (Teemburra Dam) - Operates on a full cost recovery basis ie the Water Board purchases the bulk water from DNR; no mill levy involved; trading in water occurs but is restricted by the limitations on the system and the different pricing structures. Eton Irrigation Area (Kinchant Dame) - have had ongoing discussions with DNR re: local management; limited trading in water; currently not paying towards capital or refurbishment costs; loss of mill levy will increase prices by $6.90/ML	available on request	Pioneer Valley Water Board - will not significantly alter because this is a modern system on a full cost recovery basis Eton Irrigation Area - Price will increase by $6.90/ML due to loss of mill levy. There may be the opportunity to save on administration costs with the move to local management, however operation and maintenance costs will always be high for Kinchant because of the high pumping costs of the system

Area	Progress of Reforms	Water Price Now	Expected Water Price at Conclusion of Reforms
Bundaberg	An Interim Local Management Group is very active with draft documentation prepared for Water Trading/ Ownership. Possible introduction of tradeability in the year 2000. Mill water levy was not paid for 1998/99 and will not be paid for in 1999/2000. For the current year \$2.15/ML has been added to the allocation charge to offset part of the mill levy/ full cost recovery. Local representatives argue that the mill levy amount should not be used in the full cost recovery debate as these amounts previously went to Consolidated Revenue and did not reflect on profitability of individual systems	available on request	Local representatives argue that full cost recovery will occur with the next \$2.00/ML nominal allocation charge increase. DNR personnel consider that the price increase should be \$2.00/ML plus a further 3 x \$2.15 increases. The BIA is considered to be a Category 1 Scheme with full cost recovery by 2001. Members consider that as the BIA is an unfinished scheme the date for full cost recovery should be further out. Representatives are reluctant to predict any price level for five years as this may be used to set prices for the scheme and not relate to the full cost recovery requirements.