

Productivity Commission Inquiry

As the Member for Riverina, an area dominated by broad acre cereal cropping, and with a significant interest in the growing, marketing and exporting of wheat, I have taken this opportunity to submit to the Commission the sentiments of the growers who have approached my office since the *Wheat Export Marketing Act 2008* (the *Act*) came into effect.

This inquiry has been asked to address the “operation and effectiveness of the current wheat export marketing arrangements.” I note the original objectives of the *Act*, as outlined in the Bill’s explanatory memorandum, were to:

- promote the development of a bulk wheat export marketing industry that is efficient, competitive and responsive to the needs of wheat growers; and
- Provide a regulatory framework for exporters participating in the bulk wheat export trade.

It is the view of the majority of growers I represent that the current operation of the *Act* and the new marketing system is seriously flawed, and it is ineffective in achieving higher returns for growers.

It is my belief that it is unfortunate this inquiry will not compare the current arrangements against the former arrangements, when the objectives of the *Act* are to “promote the development of a bulk wheat industry that is efficient, competitive and responsive to the needs of wheat growers.”

In not comparing the arrangements, the Government is washing its hands of any applicable criticism. It is impossible to judge or measure the “operation and effectiveness of the current...arrangements” in a vacuum. I believe the new system needs to be measured objectively against the specific former export marketing arrangements.

I would like to submit to the Commission’s inquiry issues that have been raised constantly with me regarding the new deregulated system, and where this system is not promoting an efficient and competitive marketing structure.

One of the key issues raised has been the future grading of Australian wheat. The Golden Rewards scheme introduced by the AWB, encouraged growers to produce, incrementally, better wheat. Before the season began, growers could confidently justify the application of larger volumes of fertiliser or chemical, knowing there is an incremental reward at the end of the season. This has now been lost.

All grain markets in Australia rely on Grain Trade Australia’s (formerly NACMA’s) grading system to formalise commodity standards, contracts, and trade rules. Various grain traders have various grading systems, however, stripping growers of the confidence to grow better grain and be rewarded for it. This will continue to result in lesser quality of Australian wheat overall, because there are no rewards for improvement in quality, and will continue to mean losses in returns to growers.

It is a fact, Australia produces 4% of the world's volume of grain, but equates for 15% of the world export market. Our grading system was one of the many reasons we were such a powerful player on the world market, and why Australia was deemed to be one of the most reliable suppliers of grain worldwide.

The effect the National Pool had on the price of domestic wheat is also an important issue. The Pool created a floor in the domestic market, because domestic buyers would have to better the current pool price if they were serious about acquiring wheat. A farmer would deliver his wheat to the silo, and if seeking a cash payment had the potential to consult the daily price list and choose the strongest buyer. If the Estimated Pool Return was substantially greater than this, wheat would be put into the pool.

As an example of how the new system is not competitive, one buyer, AWB has openly made it very clear to growers pools will open and close as they please, and sellers should lock in early to avoid missing out. This provides no sense of security to growers decimated by drought and who have also been hurt severely in recent years through forward selling grain. A large National Pool would have carried stock from previous years into a weaker harvest, but not leave growers exposed to the weaker position they now find themselves in. All growers would concede, whilst the highs of the pool may not be the one off extreme highs buyers or risky futures swaps might offer, the plummeting lows we are heading for could certainly have been ridden out and cushioned.

The price of Australian grain fluctuates around a 'basis,' substantiated by domestic consumption and demand. During the drought this demand has been worth \$100 per tonne to the grower, which effectively means grain has been worth more than the US futures price. Our 'basis' has gone from positive to negative, however, and is now negating our grain significantly in comparison to US futures pricing as there is a global over supply of about 10% (660 million tonnes). The single desk was able to ride these troughs more effectively, due to an ability to forward sell or hold grain over a longer period.

The single desk was securing 60-80% of the grain in Australia, depending of course on the state and the season. The accumulated grain could control the 'basis' and most importantly ride the projected futures prices. There are buyers now simply accumulating grain in order to obtain a transaction fee because the futures price is so bad!

Grain reached record prices in Australia during 2008. Wheat was trading above US\$12 per bushel - a highly inflated price - but was not able to be capitalised on through hedging by domestic buyers. Wheat at US\$8.50-10.50 per bushel still realises a price of around AUS\$400 per tonne. The market today is sitting around US\$5.00 per bushel. The speculators punt on a 3%-4% production change, so with a 60 million tonne increase in export trading this year, supply has been forced above consumption, which has resulted in a 30-40% market price change.

This basically means buyers are now in a position where they do not have to outbid the world price. In fact, it has been made abundantly clear to me buyers are actually not even in the marketplace or offering prices at many receival sites. It is an absolute sham then for the Government to be vainly spruiking there are now twenty five

accredited exporters, when my growers are struggling to even find serious buyer for hard wheat at any particular receival site in the Riverina.

In a letter dated 8 September, 2009 sent to me by the Minister for Agriculture, the Hon. Tony Burke MP, the Minister stated “the system provides growers with a significant increase in selling options...” This is simply not the case! For example, as of Friday 13 November there is one cash buyer for prime hard grain operating at ABA The Rock, which is one of the biggest receival sites in southern NSW!

Page ten of the *Explanatory Memorandum of the Wheat Export Marketing Act 2008* states “competition among traders for market share will ensure prices do not fall below export parity.” This is a completely false statement. Just because there are twenty-five accredited exporters does not mean there are twenty-five buyers competing at receival sites. As I have demonstrated, in fact, sites may only have one buyer “competitively” operating.

With regard to the effectiveness and competition in storage, as well as pricing, prime hard grain is currently valued at an incredibly low AUS\$202/tonne delivered locally in the Riverina on the main Sydney/Melbourne railway line. If growers were to hold this grain for 6 months in order to capitalise on a potential higher demand for wheat, it would cost them 10% interest on their overdrafts, which takes off \$13.50/tonne. Six months warehoused at receival sites would cost \$1.25/tonne/month in storage fees, which equates to about \$7.50 per tonne. In general, most of these sites also charge about \$12.50/tonne for receiving grain and out turning it, as inbuilt cost. So the growers need to be looking at AUS\$260/tonne in order to profit by holding on to grain.

Simplistically, it would be easy to argue that growers should simply store on farm. In relation to farm business management, however, there are immense costs involved with on farm storage. Not only is there significant capital development costs, there are a variety of issues to contend with such as weevil infestation and the overall management of running farm storage. It is essentially very hard to guarantee the quality of out turned grain from the farm.

Wheat futures prices quoted 10 November, 2009, put a Chicago Board of Trade price of grain at \$224/tonne, July 2010. There are simply no market indicators to hold onto grain. Futures trends and the current quantity of grain in storage is thus forcing growers to trickle grain into the market. The growers cannot afford to pool grain, they cannot afford to store it on farm, and they certainly cannot afford to warehouse it for great lengths of time, because the coming financial year will be geared entirely on next year’s harvest. What they are facing is truly a hand to mouth situation. I can guarantee you regional bank managers right across Australia are making some very tough phone calls this very day as they watch the futures price come down, buyers exit the market, and growers go up against the wall. The new system is simply not offering the competition that was promised, which my growers believe is leading to lower prices.

In *The Land* on 12 November, 2009, Malcolm Bartholomaeus reported on the impacts of the new deregulated marketplace and the effect this was having on pricing in the absence of AWB’s pools. (*Learning from Pools, The Land* pg 89) The article dealt

primarily with the impact of the basis on Australian wheat, and the premium growers were now forced to seek out without the security of AWB's pools. Importantly, Mr. Bartholomaeus made specific mention of the fact that in the absence of incremental rewards, growers were trying to find premiums in a positive basis that simply didn't exist. Mr. Bartholomaeus stated "with no quality increments, the basis in the cash market should have been closer to +\$20/tonne to match what AWB used to deliver via their pool." Mr. Bartholomaeus goes on to say "as we enter the peak harvest period this year, basis levels are running at about \$0/t to \$5/t, or up to \$20/t lower than what we would have expected from the old single desk.

Ironically, this is coming from one of the staunchest deregulators from 2008! To continue quoting from the article, Mr. Bartholomaeus states "if changes are not made, most growers will be worse off, the industry will be worse off, and the country will have lost valuable export income.... we need to begin replicating what AWB used to do."

Growers are now being forced to wear the risk of grain pricing, rather than a national pool weathering the ups and downs. Daily cash prices are being replaced with daily contract prices, which put growers at the behest of the buyers who will contract a tonnage for that day as opposed to a load by load sale scenario. This does not allow for variations in receival quality and forces growers to commit and bear the risk.

Locality is providing some benefit in the sense some eastern Riverina growers can access four export ports by road and rail, as well as larger receival sites. There are domestic end users buying some grain also. Others are being hamstrung due to geography. A situation noticed by many across the state is that buyers are essentially agreeing to not operate at multiple sites, which again grossly manipulates prices with less competition – another much heralded benefit proven untrue.

A potential increase in costs of freight was another point raised during the 2008 inquiry. Domestic freight rates have now increased dramatically, not simply due to the increase in diesel, but because there are small parcels of grain being collected by buyers at different sites, and so the movement of these smaller parcels becomes more expensive. Transport logistics between receival sites, branch lines, main railway lines and port are proving to be cost inhibitive, and buyers are picking and choosing as they go.

All sense of security and confidence in the system has gone. In the past, wheat was virtually going from the header to the silo, into a train and onto a boat in port, all controlled by the holder of the single desk. More grain is going to have to be moved by road, which again was foreseen by growers throughout the inquiry, and where the Government has boasted about efficiencies developing and contestability in service provision ensuing, quite the opposite is unfolding.

There is very little competition in freight rates from site to end user and the current grain freight network is grossly inefficient. Receival sites are posting flat freight rates, e.g. \$41/tonne ABA The Rock to Melbourne. This is based on the premise it will have to be trucked, because smaller buyers cannot accumulate enough grain for a train.

Graincorp have a more competitive freight rate for their pools out of their own receival sites at \$31/tonne by rail. There is, however, no competition in the transport supply line. The network is complicated further by the fact there are freight rates between buyers, sites, and within grades at the sites themselves! Quite simply, costs are not being driven down as the *Act* set out to do.

As an example of the transport supply chain breaking down, the CEO of Graincorp, Mark Irwin, gave a presentation in Wagga during September, 2009, where he discussed the Camurra-Weemalah rail line in northern NSW. It was detailed by Mr. Baylis that 23,500 extra trips hauling grain grown in northern NSW would come about over the next year unless the State Government spent \$700,000 to upgrade and reopen the Weemalah rail line. In one month alone, there were 2000 extra truck movements carrying 100,000 tonnes of grain through Moree's main street. As a flow on impact, growers would experience much higher transport costs, due to the fact the grain had to be moved by road and not trains, and increased council rates as the Shire would be forced to foot astronomical bills to maintain local roads.

Another anomaly in the transport supply chain is the discrepancies between receival sites in particular areas. There is currently up to a \$20 difference in freight charges between sites in my electorate, because there is more wheat expected in Geelong than Port Kembla due to a better season in Victoria this year. AWB is pricing grain south of the Murrumbidgee, and has determined it will be shipped out of Geelong port, thus they are offering the price ex-Geelong. Wheat prices north of the Murrumbidgee are being priced according to freight out of Port Kembla. So for a grower who has to deliver to The Rock, which is geographically closer to Port Kembla than Geelong they are being grossly penalised simply because AWB has chosen to train the grain to Geelong. Interestingly, wheat from The Rock has generally been \$8 cheaper to train to Port Kembla. AWB's freight rate north of Murrumbidgee is currently \$6.50 cheaper than southern side of Murrumbidgee going to Geelong. So even though sites are in similar geographical proximity to each port, farmers are beholden to particular pricing structures.

Another facet of the new arrangement growers are concerned about is that blending and dynamic binning are not being carried out, thus making the new deregulated system less competitive. Due to the fact there are smaller parcels of grain being 'pooled,' benefits stemming from blending and dynamic binning on-site or at port cannot be utilised. It remains to be seen whether buyers can cooperate in the marketplace to stock swap between receival sites. One would think logistically, however, that a site with a bin of prime hard with greater percentage protein than another bin on another receival site will not be swapped, as no premium can be found for the trader.

In speaking to the regulatory framework for exporters participating in the bulk wheat export trade, I wished to raise the issue of the granting of export licenses. Graincorp CEO, Mark Irwin, has admitted that WEA only granted Graincorp a one year accreditation, up until 30 September, 2009. Graincorp now has a two year license, which was only approved 1 October, 2009, weeks before the northern harvest had begun. Mark Irwin openly admitted and offered moderate criticism of this, as it meant Graincorp, along with most other companies had not hedged quantities of grain, just in case they were not granted a license. This definitely led to a reduction of

competition in the marketplace and lower returns for growers. Every single exporter would have faced the same scenario, with all licenses expiring on 30 September, 2009. For exporters to forward sell grain past this point would be akin to developers building a house on a block they do not own.

In conclusion, I would simply like to reaffirm that if the objectives of the *Wheat Export Marketing Act 2008* were to promote an efficient, competitive and responsive marketplace, the *Act* is failing. The growers I represent feel let down by the new system, as the competition promised by the Government has simply not developed. Growers understand there is a global oversupply, the Australian dollar is high, and the global financial crisis has impacted on demand. The fact remains, however, that the growers have lost elements of the single desk arrangements that helped to provide higher average returns.