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The Pastoralists and Graziers Association of
Western Australia (Incorporated)

Submission to the
Economic Regulation
Authority

*Statutory Review of the Grain
Marketing Act 2002*





Over-regulation of grain marketing in Western Australia

Western Australia grain growers are being disadvantaged by a lack of competition in coarse grain marketing.

PGA Western Graingrowers

Western Graingrowers is a commodity association of the Pastoralists and Graziers Association of Western Australia (PGA). Western Graingrowers represents professional growers operating at all levels of the grains industry – farmers whose principal goal is to advance their business opportunities.

The PGA is mainly funded by our members' contributions which are voluntary. PGA members grow approximately three million tonnes of various grains annually, and are major stakeholders in the CBH Group.

PGA members are committed to the establishment and maintenance of a rigorous competitive environment in all aspects of grain production and trading.

The failure of single desk principles in grain marketing

In the aftermath of the Great Depression, industry and government adopted centralised, coercive regulatory regimes over most agricultural commodities being exported from Australia.

It has been a recurring theme in Australian agriculture that entrenched agri-political forces have sought to protect monopoly and statutory marketing schemes, even in the face of overwhelming evidence of their imminent collapse or detrimental impact in the industry.

Following the election of the Rudd Labor Government in late-2007, and their stated policy of introducing competition to bulk export wheat marketing, in excess of 90 per cent of grain traded, both domestically and internationally, will do so in open and competitive markets.

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Some industries have embraced the move to deregulated markets and have not looked back – the deregulation of the WA Lamb Board, or grain marketing deregulation in Victoria being examples. Other industries, such as wool, dragged out the reform process and suffered years, if not decades, of turmoil and poor prices.

There is little or no evidence that compulsory marketing schemes have ever delivered benefit to agricultural producers. To the contrary, centralised marketing embeds inefficiencies, massively increases costs, and cannot deliver price premiums. Perhaps worst of all, compulsory schemes establish and entrench an unhealthy level of political patronage in agricultural industries.

The evidence from other comparative industries is clear. The deregulation of the Australian domestic wheat industry was portrayed as potentially devastating to wheat growers – in fact it has resulted in a dynamic market which growers had a clear preference for over the heavily regulated export market. Barley marketing in Victoria was deregulated without the dislocation or financial disasters predicted. In South Australia, the freeing up of the barley marketing arrangements has occurred without problem.

The economic constraints of over-regulation have been demonstrated again and again in the grains industry.

With the move towards a more open export wheat marketing environment, it is now time to view the GLA as a worthwhile period of transition to a fully open and competitive market

The transition to deregulation - the GLA in operation

The GLA was established by the State Government in order to comply with its obligations under National Competition Policy (NCP), with the goal of accessing competition payments through compliance with the nationally agreed process of unwinding government regulation of industry.

The *Grain Marketing Act 2002* as originally drafted was considered to conform to NCP guidelines – the principle invoked was that the onus was on the Main License Holder to demonstrate a benefit (or premium) in a market. If such a benefit could not be shown, then consideration to other traders was meant to be given.

Whilst this was fine in theory, it must have been thought to be too big a challenge to the Main License Holder. In reality the guidelines drafted by the Minister and Department, and their application by the GLA, effectively unwound the competitive rigour of the Act.

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These guidelines included requirements to consider:

- Seasonal condition and production levels
- Main License Holder's marketing strategy
- Main License Holder's ability to enter long term contracts
- World supply, demand and price trends.

Nevertheless, even though somewhat restrained by the guidelines, the competition introduced by the GLA has delivered benefits to the industry in WA:

- The GLA has achieved greater returns for growers – this was confirmed by internal inquiries by the GLA, including the June 2006 Regression Analysis¹
- Competitive pressures have encouraged better performance and lower costs from Grain Pool (both in terms of pool and cash markets)
- At times Kwinana cash prices have been available in all port zones – something that we would anticipate would be a regular feature in a fully competitive market
- Growers who sold to the trade for cash, not only achieved better price, but vastly improved their liquidity position – by receiving cash up-front rather than waiting for pool distributions
- Whilst South Australia retained its barley single desk, WA barley growers held a competitive advantage over their SA counterparts

With the end of the barley single desk in South Australia, the market anomaly that had been of benefit to WA growers was reversed.

South Australia growers, able to gain export parity price, found cash bids jumped by up to \$25 per tonne, while WA cash bids seemed to be around \$10 under parity (taking into account the freight advantage of shipping from WA ports). Anecdotally the trade's explanation for this was that SA became a much more attractive business opportunity than WA.

The operation of the GLA has not been without problems. The GLA's decision making process is inherently bureaucratic, when the market is dynamic and fluid. This results in decisions which, despite the best efforts of the GLA, are arbitrary and subjective. Existing structures and

¹ Department Of Agriculture and Food WA, "Analysis of the Impact of Special Export Licenses on Prescribed Grain Cash Prices in Western Australia", June 2006.

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commercial habits have been allowed to dominate the market, at the expense of innovation, competition and market development.

The GLA decision making is predicated on the idea of price premiums being demonstrated by the Main License Holder. At best this is a problematic concept – there is little to no evidence of premiums being delivered by monopoly marketing arrangements. A string of studies into grain marketing (most notably the AWB wheat single desk) have revealed that the price premium is a myth.² Where premiums in certain markets, at specific times, were evidenced, they came at a significant cost to growers.

A particularly egregious example would be the retention of claims of monopoly premiums for canola, when canola was only under regulation in one state. It is not credible for the Grain Pool to argue that it achieves premiums in a particular market, when it is competing with Australian grain freely exported from the Eastern States and South Australia.

Claims of price premiums being largely illusory, the decision by the GLA to restrict SEL tonnages (to 20% of production) and apply market restrictions, should be seen as effort to protect the position of the Main License Holder regardless of cost.

One of the issues confronted by the GLA is this question of what constitutes a 'market'. Does it mean a particular country, a geographical area, or a relationship with a particular buyer? Should a Main License Holder's market be protected when another trader is supplying that market with Victorian and South Australian barley?

This question, coupled with the requirement for the GLA to consider the export programme of the Main License Holder, limits as to tonnage, a reluctance to grant early SELs, and a reluctance to grant multi-season markets, all place severe restrictions on the development of the rest of the industry in WA.

Whilst the GLA has attempted to address some of these issues by taking a more liberal view of the guidelines, they are hamstrung by some of the core assumptions within the *Grain Marketing Act 2002* and the operational guidelines of the GLA. The GLA are working from an unfounded presumption that protecting the Grain Pool delivers net benefits back to the growers at the farm gate. This is not a criticism of the GLA, but an observation on practical operation of a flawed system.

² For Example:

- National Competition Council 2000, *NCP Review of Wheat Marketing Arrangements*
- Accenture 2002, *Grains Industry Review*
- Allans Consulting 2000, *The Wheat Marketing Act 1989: The Economic Impact of Competitive Restrictions*
- Joint Industry Submission Group 2000, *Australian Wheat, Its Time for Choice*
- Kronos Corporate 2002, *A Review of Structural Issues in the Australian Grains Market*
- ACIL Tasman 2005, *Marketing WA Wheat*

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Wheat Marketing Reform and the Sunset Clause

At the insistence of the National Competition Council, it was envisaged that reform of the wheat marketing arrangements would have a flow on effect to the State coarse grain and oilseed marketing arrangements. As a result a sunset clause was included in the Grain Marketing Act 2002, that retired the Act on relevant Commonwealth legislative change:

GRAIN MARKETING ACT 2002 - SECT 49

Expiry of Act

49 . Expiry of Act

(1) If the Minister makes an order under subsection (2), this Act, other than subsections (4), (5), and (6), expires on the day specified as the expiry day in that order.

(2) The Minister may, by an order published in the Gazette , specify as the expiry day a day that is —

(a) not before the order is published in the Gazette and not before the Commonwealth has passed legislation to make a relevant Commonwealth legislative change; and

(b) as soon as practicable after the 30 April next following the day on which a relevant Commonwealth legislative change comes into effect.

(3) In subsection (2) —

“relevant Commonwealth legislative change” means a change to Commonwealth legislation as a result of which there cease to be restrictions under Commonwealth legislation on the export of wheat, whether under the Commonwealth Wheat Marketing Act 1989 or another Commonwealth Act imposing similar restrictions.

Whilst it cannot be predicted if the Federal Government’s reforms will be in place before the 30th April, their intentions are clear. They have stated their model will encompass:

- *Growers will be able to directly participate in bulk exports through Grower Cooperatives and/or Alliances;*
- *Traders and marketers currently operating in the domestic market will be able to apply for export accreditation;*
- *AWB International’s veto power will not be reinstated;*

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- *The 'general exemption' from control of the Export Wheat Commission currently held by AWB International will also be removed;*³

In our opinion this clearly constitutes an end to the single desk restriction under Commonwealth legislation, and should trigger the sunset provisions.

In our view this sunset clause was particularly insightful as WA is a very attractive origin to accumulate grain for the world wheat market. It is estimated that WA will produce up to 8 to 10 per cent of the world's internationally traded wheat. With the presence of multiple traders this volume of grain will attract, and the investment we wish to encourage in the industry, it would make sense to have all of our barley, lupins and canola available for competitive buying.

GLA is an impediment to trade

With little to demonstrate in the way of benefits, it is hard to see why the Main License Holder should be shielded from competitive pressures and retain a privileged position in the market.

Whilst the GLA seems to have developed a satisfactory system for the apportionment of costs between the Main License Holder and the SELs, in aggregate these are still costs that have to be funded at the expense of grower's grain returns.

These costs can no longer be regarded as trivial, now that the cost of doing business in South Australia is relatively low.

However the greatest costs of the GLA are opportunity costs. By necessity decision making in a fluid market, such as grain, where trades can be made and communicated at the speed of light, are not compatible with the time taken to make application to, and await decisions from, the GLA

By default the operations of the GLA entrench a privileged position for CBH / Gain Pool in the grain trade. It is far from clear that this position results in benefits to growers through better net prices. Indeed it can be observed that perverse incentives exist for CBH to take advantage of its position and generate revenues for CBH at the expense of pool participants, in particular, and growers more generally. We note that contributions from Agracorp's trading activities to CBH revenue cannot be

³ Australian Labor Party, "Australian Wheat Export Marketing", 2007 Election Policy Document.

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derived from CBH's consolidated financial statements, but they are significant.

Growers also need correct incentives and information to make good business decisions. There is little doubt that market generated information about prospective wheat prices will be of better quality than that determined by the Grain Pool in the form of projected pool prices. The greater the competition, the better the indicator for growers, particularly early in the season, in making planting and marketing decisions.

The clear spirit of the *Grain Marketing Act* 2002 is to see that any observed benefits in prices are returned to growers, and not to expanding CBH's reserves.

The protection of the marketing activities of CBH will continue to have a negative influence on attracting skills and investment to the WA grains industry.

Access to Infrastructure

CBH's legacy storage and handling assets have been funded by all growers, whoever they wish to trade with, now and in the future. We believe that CBH has an obligation to provide equitable access to their storage, handling and fobbing facilities to all their customers.

The CBH system was built to deal with two grain accumulators acquiring their stocks through statutory fiat. It is expected that there will be adjustment issues as CBH confronts changed market demands. This adjustment will be made all the harder for CBH as they are heavily involved in grain trading, with an obvious conflict of interest that results.

The trade, justifiably or not, views every frustration in dealing with CBH as an attempt to impede their business and protect CBH's trading operations. However, we do not believe this problem should be resolved by regulation or legislation.

If the trade in wheat, barley, lupins and canola is open to competitive buying and accumulation, commercial pressures will over time force CBH to come to terms with the needs of restructured grains industry.

This process of 'normalisation' will be facilitated by remembering the lessons of the past. One of the most important findings of the McColl Royal Commission into the Grains Industry in the 1980s was the need to maximise competitive pressure in storage, handling and transportation of grains. There seems to be some risk that the State Government is planning to repeat the mistakes of the past by trying to force grain onto

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rail. We believe that this would be a significant retrograde step, and if the ERA is able to comment upon this, we would respectfully ask that it does so.

There should be some obligation on CBH, and possibly others, to report the following information to the Australian Bureau of Statistics:

- aggregated stock levels
- grades
- and location of various grains in the system.

This aggregated information (not the commercial details of any one company) should rightly be in the public domain.

Western Graingrowers, having seen the destructive potential of over-regulation, would always prefer commercial solutions (such as the Melbourne Port Terminal Access Undertaking) over costly and heavy-handed government regulation.

Conclusion

*“Growers are looking for a framework that provides them with the **competition, transparency and direct market access** they need to maximise the value of their wheat.”*

This quote, from Dr Andrew Crane⁴ of the CBH Group, is referring to the upcoming changes to the wheat marketing arrangements (see Appendix A for full media release). This principle should also inform the current inquiry into the state grains marketing arrangements

Western Graingrowers believe that it is clear that an immediate move to an open and competitive coarse grain and oilseed marketing environment would be in the interests of all growers.

The GLA has been a transition phase for growers and the industry of five years duration. There is no need for another period of transition, and the industry should now deregulate immediately.

Costs of further transitional arrangements will be at a direct cost the industry. Any restriction on competition via licensing arrangements will continue to foster market distortions, limit competitive behaviour, reduce investment, and limit commercial opportunities for grain growers.

⁴ Dr Andrew Crane was General Manager of Grain Pool Pty Ltd, before recently becoming GM of Strategy and Business Development for the CBH Group.

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Protecting the position of the Main License Holder, at the price of reducing competition and the flow-on benefits to the industry, is not a sound basis for economic policy.

It is therefore imperative that open competition, transparency and direct market access by multiple grain exporters, be introduced to WA by repealing the *Grain Marketing Act 2002* and the winding up of the Grains Licensing Authority.

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Appendix A – CBH Media Release regarding wheat marketing and the importance of competition:

CBH Group supports changes to wheat marketing

The CBH Group has rejected calls from the Western Australian Government for a delay in the introduction of the new accreditation system of export wheat marketing.

General Manager Strategy and Business Development, Dr Andrew Crane said any further delays would only serve to create more uncertainty for growers.

“Growers are looking for a framework that provides them with the competition, transparency and direct market access they need to maximise the value of their wheat.

“The CBH Group is ready now and well positioned to deliver this value to growers,” he said.

“The CBH Group, as well as other current exporters of coarse grains, pulses and oilseeds, has customers who want to buy wheat tomorrow, and we’ll work with the Federal Government to establish the new system as soon as possible.

“Grain Pool, the CBH Group’s marketing arm, has some 80 years experience in marketing grain and is geared up to take part in the process that will allow all bulk handlers to tender for the big contracts with buyers including Pakistan, India, Egypt, Sudan, Iraq and Iran.

“We have also worked to secure demand for Western Australian wheat through our investment in flour mills throughout Asia, with an annual requirement of more than 3 million tonnes of wheat.”

Dr Crane said the CBH Group had received strong interest for some time from customers looking to source wheat directly from growers.

“At the same time, growers have also demonstrated that they want a system that provides them with available alternatives and have expressed their interest in the CBH Group marketing their wheat.

“We are confident that a reformed wheat marketing system can be implemented by the Federal Government and industry for the 2008-09 season, providing some much needed certainty for Australian grain growers.”

Dated: 22nd January 2008