# Australian Grain Exporters Association

## Submission to the Senate Standing Committees on Rural Affairs and Transport inquiry into Operational issues in export grain networks

## Introduction

The Australian Grain Exporters Association (AGEA) was formed in 1980 and is the representative body for exporters of Australian grain. AGEA represents its members to facilitate an efficient and effective export industry. Members are active in grain accumulation, storage, handling and processing, as well as risk management and hedging strategies involving commodity futures, foreign currency and counterparty risk. AGEA member companies also have substantial investments in non-grain sectors of the rural economy, such as meat processing and intensive livestock production, oilseed crushing, fertiliser distribution, cotton trading and ginning, ocean freight ownership and bulk and container shipping.

AGEA supports open and contestable markets. As such, AGEA does not support the presence of national or regional monopolies in any part of the grains industry value chain. AGEA's focus is on assisting Australia to grow its exports of grains and oilseeds. It brings the export sector together to focus on pre-competitive issues that underpin the position of Australian grains and exports in world markets and to ensure that the export supply chain operates efficiently.

The outcome of industry arrangements should be to shape an industry where there is a profitable supply chain for all and benefit for the industry is maximised. AGEA believes this will be achieved where there is a value chain that:

- Does not hinder or impede exports from Australia. A key element of this is an environment where exporters have the ability to execute sales with certainty
- Is driven by commercial customer and supplier relationships aligned to the ongoing enhancement of an efficient supply chains
- Is globally efficient with measurable benchmarks for key performance indicators such as port capacity, rail usage, access, etc.
- Creates maximum competition amongst exporters in purchasing, transporting, storing and marketing Australian wheat
- Creates incentives to develop new products and services across the entire supply chain and drives innovation
- Has effective industry structures for the management of precompetitive activities such as market access policy, quality construction and facilitation of trade which is separate from the commercial market activities; and for responsibility for industry stewardship functions
- Creates an attractive investment environment to encourage investment in the Australian wheat industry, including infrastructure investment, from domestic and international sources

AGEA believes that the industry can, and should be encouraged and enabled to, move to a point where it is self-regulating but this will require development of a commercial framework that is enduring i.e. able to operate when regulatory oversights are removed with moving back to uncommercial behaviours.

However to achieve the above, a number of operational issues arising across the export grain storage, transport, handling and shipping network need to be addressed.

## Deregulation has delivered opportunities

The grains industry has responded favourably to the new marketing environment. Australian wheat remains in strong demand globally and growers now have more flexible access to a selection of accredited buyers, offering a variety of marketing options. Product differentiation provides opportunities across the value chain and a competitive deregulated system can best deliver this need, while also servicing large volume customers.

### Export program has been maintained

Grain exports have continued unabated since deregulation. Average exports in the two full years since deregulation were 13.43 million tonnes, compared to 12.56 million tonnes in the five years prior to deregulation and 13.75 million tonnes in the 10 years prior to deregulation.

Container exports have grown 420% since 2000/01 and have consistently reached levels in excess of 2 million tonnes since deregulation of non bulk exports. Container exports represented 17% of total exports in 2009/10.

In 2008/09 12.3 million tonnes were exported to more than 40 countries, while in 2009/10 12.1 million tonnes were exported to 36 countries. In the first six months of 2010/11, 7.8 million tonnes of bulk wheat have been exported to 30 countries, up 2.6 million tonnes on the same period last year.

### More buyers and more choice for growers

In 2008/09 there 17 accredited exporters and 18 in both 2009/10 and 2010/11 (year to date).

**Table 1: Australian wheat export performance indicators**

| Measure | 2008/09 | 2009/10 | 2010/11 YTD |
|---|---|---|---|
| Wheat production (mt) | 20.9 | 21.7 | 26.3f |
| Bulk wheat exports (mt) | 12.3 | 12.1 | 16.0f |
| Accredited exporters (No.) | 23 | 27 | 26 |
| Active exporters (No.) | 17 | 18 | 16 |
| No of export destinations (No.) | 42 | 36 | 24 |
| Volume shipped by top 8 (%) | 90 | 89 | 91 |

### Grower benefits: larger range of marketing options, growers have been paid and expansion in grower advisory services

The introduction of competition to the Australian wheat market has provided significant benefit to growers including an expanded range of marketing options; continuation of wheat pools that offer improved features and greater flexibility; improved pricing options that have enhanced market signals to growers; and greater opportunities for growers, exporters and customers to work more closely together.

### New entrants and continuing investment across supply chain

Local and global companies continue to invest in infrastructure as they establish a broader presence in Australia. By way of example, since the Cargill acquisition of AWB, Cargill has committed to spend several million dollars on the Grainflow sites to upgrade for the 2011 harvest.

### But industry performance can improve to capture potential gains from deregulation

Whilst deregulation has delivered market based objectives, industry performance can be improved, in particular, supply chain performance lags behind world's best practice. This has the potential to reduce Australia's competitiveness vis a vis other origins.

Some of the key areas where industry performance can improve are:

- Shipping stem: improved execution and better use of port capacity
- Movement of grain to port: inefficiencies are created through the bottleneck in movement of grain to port and consolidation and management of grain at port
- Infrastructure investment, in particular, rail
- Information and transparency

## Issues raised in the inquiry terms of reference

### Access to essential grains infrastructure/the shipping stem (Reference (a) and (f)

The objective of the 2008 Wheat Export Marketing Act (WEMA) was to remove the marketing monopoly, but not to create access monopolies.

WEMA was designed to increase the number of exporters and the port access provisions recognised that some regulatory oversight was necessary to ensure that those new entrants had continued access to the export supply chain so that they would be able to deliver competitive bids to growers. The WEMA established market oriented regulatory tools to ensure that the market operates efficiently. This is consistent with all parties in the supply chain being able to receive a commercial return on the assets they own.

The grains industry has developed in a historical context where assets were built under regulation by State Governments or Grower Cooperatives to provide an open access conduit for grower's grain to reach export markets, recognising that the variability of grain production would inhibit investment in facilities capable of handling high crop years. Tools to ensure fair and reasonable access to assets such as port terminals are required as the industry moves to a fully commercial environment. This will be achieved when the industry is a point where is does not revert to a position that was not the intent of the WEMA.

The 2008 Act was designed to create a competitive market for the wheat industry. The Act recognised that to achieve this that there needed to be contestability in service provision if the benefits of deregulation were to be delivered. According to the *Wheat Export Marketing Act 2008 Explanatory Memorandum,* the access test was intended to ensure that accredited wheat exporters that own, operate or control port terminal facilities provide *"fair and transparent access to their facilities to other accredited exporters.* This aims to avoid regional monopolies unfairly controlling infrastructure necessary to export wheat in bulk quantities, to the detriment of other accredited exporters.

Bulk handling companies are largely monopoly providers of port terminal services for bulk grains within geographical areas. Access to port terminal services is essential to export bulk wheat from Australia. Australian wheat exporters have no option but to use BHC services where they wish to export bulk wheat.

The integrated handling and storage companies dominate many parts of the grain supply chain and have developed extremely powerful positions across the supply chain, including grain export port terminals, up country grain storage , logistics (rail freight), information (particularly grain quality and stock), and trading/marketing.

This position highlights the need for use of regulatory tools during the transition period until the market is operating fairly, competitively and commercially.

**Port Access**

The objective of the current access provisions is to ensure that Australian wheat growers have access to real competition that is provided on a level playing field and to reduce the overall cost of the supply chain in order to maintain and improve competitiveness of the Australian wheat industry.

The port access undertakings should establish a set of minimum requirements that meet industry needs in relation to fair and reasonable access; provide mechanisms that achieve an equitable allocation of capacity and ensure that the services are provided on commercial terms.

AGEA is seeking a globally efficient supply chain in which exporters have certainty and the ability to execute sales; where relationships through the supply chain are commercially based; and where a 100% of port capacity is contestable.

Core principles that should be reflected in all port access undertakings that will assist to ensure effective competition to the ultimate benefit of all supply chain participants are:

i. *100% of port capacity should be contestable*

   Shipping slots should be transferrable - Shipping slots should be transferable across port; time/elevation period; grain; and owner (approved counter parties). Increasing the flexibility and transferability will reduce the potential for speculation around the stem

ii. *Shipping slots should be allocated via a process that is:*

   - *Transparent/visible* - AGEA has supported a 'first come first in' approach on the east coast, but the experience of the current season where demand exceeds supply has highlighted some limitations to this. AGEA recognises that the auction system may be a more effective tool for allocation in periods of high demand. AGEA was not opposed to the auction system proposed by CBH as a mechanism, but had concerns around a number of the business rules accompanying the auction

   - *Price is the only determinant when capacity is limited* - where demand for capacity exceeds supply, price should be the only determinant of the quantity of capacity allocated to each applicant. Subjective allocation of programs and terms and conditions (T&C) should not be used to ration capacity. As such, if BHC offers (T&C) or a program, the same T&C/program should be available to all shippers with a service agreement (i.e. eligibility criteria for access should not be determined by BHCs).

   - *Cost impact of not using capacity is incurred by all players* - the allocation process should provide exporters with certainty to acquire and execute slots without having to speculate. All parties should incur a 'real cost' for capacity booked and not utilised. Agreed slot fees for all participants across all BHC ports should be paid into a trust account. The fees resulting from non-performance by an exporter result in forfeiture to the incumbent BHC, while fees resulting from non-performance by a BHC result in forfeiture to fund. The fund would be redistributed to all parties who shipped grain in the designated period e.g. annually or less. The mechanisms are slightly different for the various BHCs, for example in the case of Viterra and Graincorp, this would be the downpayment (prepayment) of a part of the fobbing charge which is forfeited if capacity is not used; and in the case of CBH's auction premium it is the prepayment of a premium to secure capacity at CBH auction, accompanied with the commitment to pay all/part of the fobbing charge(s) if the slot is not used (or lost capacity charge)

iii. *BHCs are accountable for performance*, particularly where a bundled service is offered - Where the incumbent BHC offers a bundled service, the capacity of the bundled and third party components should be nominated.

The bundled service capacity should be accompanied by commercially realistic load rates and the payment of demurrage/despatch at prevailing market shipping rates. Greater transparency and greater incentives for port terminal operators to maximise efficiency could be achieved if there was a requirement for BHCs to report on performance indicators for their storage and port businesses separately from the integrated entity.

iv. *Measurable performance criteria* - Currently the incumbent BHC has the ability to set benchmarks in non transparent way and there is no risk/loss for non performance by the BHC. Key measurable performance indicators should be defined against which BHC performance can be measured and disputes initiated in the event of non performance. Measurable performance indicators for the port terminal businesses (separate from the integrated entity) would provide greater clarity in relation performance of the stem and encourage increased efficiency in the port business i.e. throughput of the port terminal.

### Transparency in storage and handling of grain (ref. (b))

The ability of the BHCs to use information to the advantage of their trading arm is of key concern and is impacting the development of an open and competitive marketplace. BHCs should be required to put in place mechanisms that avoid vertically integrated companies from advantaging their trading arms through access to information/ services that are not available to other exporters i.e. anything that a BHC trading team sees/receives should be made available to the market.

Information that all parties should have access to includes:

- Receival/Storage
  - Up to date/regular (daily) receival data by site by commodity by grade by tonnes
  - Zone average quality data by port zone by commodity by grade by tonnes
  - Receival profile summary post harvest by commodity by grade by tonnes
  - Full warehouse stock (i.e. that stock which is in the BHC system under the grower warehouse option i.e. uncommitted grain) availability
  - Access to up to date fumigation details and plans to ensure compliance with PRF and MRL
- Ports
  - Daily reporting of stocks in port by commodity
  - Vessel quality information (e.g. access to sampling, laboratory testing, quality results) prior, during and on completion of loading of vessels

### Equitable access to the lowest cost route to market (ref (c))

Infrastructure investment and operation are key issues for the industry. In general, all rail infrastructure is in need of upgrading and trains commonly move at sub-optimal speeds due to track inadequacies. Such inefficiencies reveal themselves throughout the supply chain in the form of higher costs as assets (and the capital tied up in them) and less efficient use of assets which ultimately leads to lower net returns to growers for their grain. There have been many reviews of infrastructure issues and needs in the Australian grains industry, largely as a result of infrastructure throughout Australia having been run down significantly over the past fifteen or more years. There are ongoing concerns about both the quality and ongoing viability of grain rail lines. Many lines are in need of significant capital investment if they are to continue to operate. An inland rail link connecting Victoria to Queensland would add to efficient market action and reduction in interstate road traffic. The current environment is not one that provides incentive for private sector investment.

The wheat export monopoly has influenced the way the storage, handling and transport system for grain has evolved in Australia.   This has seen the Australian system built primarily as a storage system, whereas in overseas countries the grain handling systems have been built for fast and efficient throughput of grain.  Cost savings in other countries are shared between growers and end users in contestable markets, through competition to accumulate and market grain.

It is expected that competing upcountry facilities will be built and in fact are already occurring through both on farm storage and private facilities.  The extent of this will vary from region to region based on crop and market characteristics, but will also be influenced by BHC charging practices.

A significant challenge for the Australian grains industry is the ongoing sustainability and maintenance of an infrastructure system. Logistical constraints, rail transport and port access are ongoing issues that need to be resolved.

Some specific issues for the industry relate to the bundled service offer by BHCs and the port access provisions for third party supply chains.

Bundled service offers from the BHCs should be optional and where a bundled service is offered, the capacity of the bundled and third party components should be nominated.  The bundled service capacity should be accompanied by commercially realistic load rates and the payment of demurrage/despatch at prevailing market shipping rates.

AGEA believes that Grain Express has had the effect of substantially lessening competition through other exporters being prevented from building alternative supply chains; freight negotiations for road and rail concentrated in the hands of one party (CBH); and the lack of transparency and accountability.  AGEA believes that Grain Express has impacted adversely on the efficiency and cost of the wheat industry supply chain in WA.  AGEA supports the recent decision by the ACCC to revoke the Exclusive Dealing Notification (N93439).

In AGEA's view, there is no clear non-discriminatory pathway and opportunity for wheat from private third party upcountry facilities to be delivered into the port terminal facilities controlled by BHCs.  This is inhibiting alternative transport and storage arrangements from being developed and stifling innovation in development of specialty supply chains.

Pricing practices by the BHCs should be non-discriminatory to third party supply chains and charges should reflect the services being delivered and used.  This would enable and promote the most efficient supply chains to develop in a competitive environment without any need for rationalisation or intervention from the Government.

Port terminal services should not discriminate between Australian wheat exporters based on where grain was stored (i.e. whether it was stored in the bulk handling companies' up-country storage and handling network, a third party storage network or on-farm) or how it was transported to the BHCs' facilities.  All grain should be tested and assessed on arrival port and then managed according to its suitability and compliance.

Third party storage arrangements should not be subject to standards that are higher than the requirements placed on the bulk handling company's own storages.  Any auditing and accreditation of third party storages should be undertaken by an independent party not the bulk handling company; and grain placed at port for shipment from third party storages is should not be hindered or discriminated against in operational terms.   Differentials in pricing between grain from third party storages and bulk handling company storage should be justified as currently it is not possible for exporters to know if the price differential between approved and non approved third party storage accurately reflect the additional costs of managing risks associated with receiving wheat from non-approved third party sites.

### Access to grain purchased and quality (ref (d) & (e))

There are a number of competitive issues relating to quality and outturn of grain.

There a number of important industry functions that assist to maintain Australia's quality reputation including wheat classification, receival standards and industry monitoring. In addition, there are a number of industry codes of practice in various sectors of the industry; and individual industry participants have quality management programs and processes in place.

Trade in the Australian grains industry is based on a set of grain receival standards and contracts that enable buyers to have clarity and confidence in the products that purchased. GTA plays a key role in establishing industry-wide grain standards and contract terms and conditions. Buyers and sellers can agree to use these standards or develop other standards to suit their own particular needs. The GTA Grain Standards are underpinned by industry classification and accreditation systems via Wheat Quality Australia (WQA).

AGEA is a member of WQA and brings valuable market intelligence to this forum. It is very important that the industry has a process in place to provide integrity around industry standards and grades.

Wheat varietal classification together with wheat standards aim to deliver grain of consistent physical quality, processing performance and end-product quality to customers and end-users in a differentiated form (grades) allowing exporters to optimise value capture from markets for the benefit of industry.

Under the regulated system of the past, BHCs have played a role in ensuring compliance with industry standards. As the industry transitions to a fully competitive environment, changes are required to the industry's quality management activities to ensure varietal segregations are not lost where those segregation clearly meet customer requirements for finished product performance. This is necessary to ensure that system continue to support and promote the development of quality grain production.

Current practices, where BHCs receive and out-turn the grain to buyers on the basis of quality parameters set by GTA, do not provide any assurance that exporters can access at outturn the quality they've paid for. Currently the BHCs only guarantee outturn at minimal receival standards although some endeavour to give average port zone quality and/or the quality a marketer owns. This has a number of implications:

- exporters can pay for grain of a quality which is greater than what they receive on out-turn with the cost difference incurred by the exporter, or in other words a disincentive to reflect quality premiums available in the market back to growers
- exporters have greater risk when negotiating sales/participating in tenders as they cannot guarantee the quality that they will receive on out-turn (contracts/tenders are virtually always at a specification above the receival standards)
- BHCs have the opportunity to access the better quality grain that they sell at premium, an opportunity that is not available to other exporters
- if the BHC is only obliged to out-turn to a minimum standard instead of what is received, then buyers will only pay growers to the minimum standard and over time this may see growers produce lower quality product

This practice is not sustainable in a commercial market place and is based on historical practice when there was a single desk in place. Exporters need the ability to achieve greater integrity in management of quality from farm to port including guaranteed outturn against quality specifications and/or the ability for exporters to access stock of equivalent quality purchased.

Other operational issues that impact on the exporters' ability to assure quality to their customers relate to supply chain practices such as:

- Inability to gain access to bulk handling facilities by exporter's nominated Superintendent Company to carry out services associated with quality and quantity determination which are fundamental to successful trade; and can be necessary to comply with contracts that are standard in international trade. This is standard custom and practice throughout the world. These companies require access to those parts of the bulk handling facilities where samples need to be taken, such as belt loaders, warehouses or silos and to where weight determinations are made
- Inability to have exporters' (receiver/owner/vessel) shipping agent appointed and not be forced to use bulk handlers (shippers) agent
- Lack of access for competitive stevedores and shipping agents

## Summary

- Deregulation has been successful: grain exports have been maintained, number of buyers has increased, more choice for growers, grower payments have occurred unimpeded, increased investment across the supply
- However, industry performance is not achieving optimal performance and supply chain behaviours are limiting the full opportunities of deregulation from being captured
- Market oriented regulatory tools are required to ensure the transition to a fully deregulated market that operates efficiently and that there is fair and reasonable access for all players
- Industry self regulation is achievable in the longer term and the industry is making significant steps with the expanded role of GTA in trade facilitation activities, the transition of wheat classification to WQA and the establishment of the Grains Industry Market Access Forum (GIMAF)
- There are a number of supply chain issues that need to be addresses to enable the industry to maximise performance including:
  - Shipping stem to deliver greater execution certainty for exporters and better use of port capacity
  - Movement of grain to port to remove inefficiencies are created through the bottleneck in movement of grain to port and consolidation and management of grain at port
  - Grain quality to enable exporters to access the quality of grain purchased and to promote the continued focus on quality grain production
  - Information and transparency to provide a fair and contestable market for all exporters
- Lack of investment in infrastructure, particularly rail, is a critical issue and requires industry/ Government partnership to address this.