



17 November 2014

Mr Tim Watling
Committee Secretary
Senate Standing Committees on Rural and Regional Affairs and Transport
PO Box 6100
Parliament House
Canberra ACT 2600

By email: rrat.sen@aph.gov.au

Dear Mr Watling

Re: Offer to Wilmar Sugar Australia to provide further information on matters raised relating to Wilmar's proposed approach to sugar marketing.

Thank you for the opportunity to provide further information for the Committee's inquiry into the current and future arrangements for the marketing of Australian sugar.

There have been a number of issues raised in other submissions relating to Wilmar's proposed approach to sugar marketing which I would like to address in this supplementary submission.

This includes submissions by Queensland Sugar Limited, New South Wales Sugar Milling Co-operative Limited, Burdekin District Cane Growers Limited, a joint submission from Canegrowers and Australian Cane Farmers Association, in addition to submissions from individual growers which have been provided in response to a campaign directed by Canegrowers.

This supplementary submission addresses the following issues in particular:

- Claims that Wilmar's decision to undertake marketing activity for its own sugar beyond 2017 is some kind of improper action;
- Assertions that millers will be in a position of market power and will behave in an uncompetitive way and seek to exploit a so-called 'monopoly' position in the market or that there is an imbalance of market power;
- The incorrect notion that growers have some kind of legal title or ownership of the sugar produced by millers and or should have the ability to dictate how a miller markets its sugar (presented in some submissions as 'grower' economic interest' and as 'grower' choice');
- Claims that Wilmar has failed to engage or negotiate with growers to find a commercially agreed outcome on its proposed future marketing arrangements;
- Suggestions that there needs to be a greater regulatory role for bodies such as the ACCC to ensure competitive conduct in the industry.



Wilmar's plans for sugar marketing post-2017

Wilmar's decision to leave the Queensland Sugar Limited (QSL) voluntary marketing system is comprehensively covered in Section 5 of our original submission. It has been suggested in some submissions that by deciding to undertake the marketing of its own sugar from 2017 onwards, this represents a unilateral decision taken by Wilmar at the expense of growers.

Since 2006, when export marketing was fully deregulated, all Queensland sugar millers have had the right to determine how 100 per cent of their sugar production was marketed and sold, just like any other manufacturer has the right to sell and market the products they make.

Wilmar's announcement on 3 April 2014 that it would exit the QSL voluntary marketing system and directly undertake the sale and marketing of its own sugar from the 2017 season onwards is entirely consistent with the principles of the 2006 deregulation of sugar marketing. It also followed more than two years of discussions with sugar industry leadership about how greater returns could be generated for growers and millers from the sale of raw sugar.

Wilmar's proposal is permitted under the *Sugar Industry Act 1999*. The announcement was made in full compliance with company's legal and contractual obligations to growers and QSL. This includes giving three years notice.

Any suggestion that Wilmar has acted inappropriately or is out of step with the regulatory regime for sugar marketing is incorrect. Wilmar is not the only miller who has given notice to QSL and decided to market its own sugar as a result of determining it can deliver better returns to growers than under the current QSL system. In addition, other mills (Maryborough, Mossman and Mulgrave) have already marketed their own sugar outside QSL at some stage.

The reference to a 'misuse of bargaining power' in the Burdekin District Cane Growers (BDCG) submission (BDCG, Submission no. 13, pg. 6) is a misrepresentation of the discussion regarding Forward Pricing Agreements in 2012 and 2013. The Forward Price Agreement that was in place from 2008-2012 was introduced as a voluntary mechanism for growers to choose to take part in forward pricing. It was a single agreement for all growers to utilise if they chose to, and this approach was necessary given the technical, administrative and information technology system complexity associated with administering multiple agreements.

In 2012, the agreement required updating, mainly to cater for an increasing array of pricing methods and pools.

The 2012 forward price agreement was provided to growers for comment on 16 August 2012. Feedback on the agreement was received from the various Canegrowers collectives and the Pioneer Cane Growers Organisation, which is now part of the BDCG. Wilmar consulted and engaged with the relevant parties in relation to the feedback provided and where appropriate Wilmar incorporated the feedback received into the agreement, with the objective of finalising a single standardised agreement with all collectives.

Consensus and agreement on the terms of the 2012 forward price agreement was reached shortly afterward with the various Canegrowers district collectives, however discussion and negotiation with Pioneer Cane Growers continued throughout 2012. Wilmar finally issued the documents for use by growers on 18 January 2014. This final version incorporated changes to terms and conditions based on feedback from both the Canegrowers and Pioneer Cane Growers collectives.



The issue raised by the BDCG in their submission does not, as BDCG state, represent any form of resistance to negotiation. Indeed, the fact that Wilmar did not finally issue the documents for use by any growers until some five months later (despite having agreement from other collectives) indicates Wilmar's willingness to continue to consult and engage with Pioneer Cane Growers in relation to the terms of the agreement.

It should also be noted that Wilmar has also put arrangements in place to facilitate the ongoing forward pricing for the 2017 season on a "business as usual" basis until June 30, 2015. A form of these agreements was successfully, efficiently and commercially negotiated with the BDCG earlier this year.

Wilmar considers that by marketing its own sugar, it can achieve better results for the company and its growers. This will be achieved by drawing upon Wilmar's global marketing expertise and capabilities as one of the world's leading sugar traders. The better returns achieved by Wilmar and returned to growers will both improve farm viability and have positive flow-on effects to local area economies.

Misuse of market power

A number of submissions have raised concerns about the potential for millers to misuse perceived market power or carry out anti-competitive actions. Our original submission comprehensively addressed issues around regulation and competition (see Section 8, The Role for Government).

In particular, our submission highlighted the institutional safeguards to protect all participants in the sugar value chain, including the legislative regime through the *Sugar Industry Act 1999*; the authorisation of collective bargaining between growers and millers; the role of the *Competition and Consumer Act 2010* consumer law, and transfer pricing rules.

Wilmar recognises that due to the structural requirements of the industry and the dependence of growers on their regional mill (and vice versa), most growers only have a choice to supply their local miller. However, growers and local mills are dependent on each other.

Mills are critically dependent on cane volumes for profitability and overall viability. It is estimated in Wilmar's case that a five per cent decrease in cane volume translates to a reduction in earnings before interest and tax (EBIT) of more than 20 per cent. Wilmar currently has over 17 million tonnes of crushing capacity, but only crushes around 15 million tonnes of cane. It is clearly in Wilmar's commercial interests to work with its growers to increase the supply of cane, not reduce it. The long-term sustainability of cane supply will only ever be achieved if cane farms remain viable and profitable ventures for cane farmers. That is why Wilmar is committed to marketing its own sugar and delivering better returns to Wilmar cane farmers. Wilmar's milling viability is intrinsically linked to farm profitability.

Wilmar's proposal is about delivering a win-win outcome. Wilmar and its cane growers are both exposed to sugar price. If growers are paid more for cane because of a higher sugar price, it doesn't impact negatively on our profit, because we receive exactly the same sugar price on the sale of that portion of our sugar production that we use to pay growers for their cane. Today, growers can undertake their own price risk management independently from the price risk management decisions of the milling company. When our cane farmers do better, our business is stronger. That's why we say our proposal is a win-win.



As noted in our original submission, millers face higher risks than growers in all areas:

- Millers depend on growers' production decisions, with no offsetting obligation on growers to grow or supply a defined quantity of cane each year;
- Millers are 'downstream' from growers and assume risks related to the quality of incoming product and the volume of cane;
- Millers have high fixed costs associated with their milling infrastructure and face higher risks of plant obsolescence than growers;
- Growers' assets are fully negotiable and can have a substantial value in alternative farming use, whereas millers' assets are highly specialised and there are no alternative uses for a sugar mill.

The purported market power of millers or imbalance of power has long been used to justify retention of regulation for the Queensland sugar industry, or as evidenced in other submissions to the inquiry, to call for an expansion of regulatory involvement.

In this context, it is worth revisiting the 1992 Industry Commission report on the Australian sugar industry which is referenced on page 40 of our original submission which noted:

'... in the past, there may have been some potential for mills to exploit market power. However, growers have now formed strong organisations to negotiate on a collective basis. In some regions, growers have purchased their local mill. Growers also have far greater access to information to allow them to assess whether terms offered by a mill are reasonable. The development of trade practices legislation also provides some protection for growers against the misuse of market power by mills. While the Act limits collusive agreements to reduce competition between suppliers, an exemption may be provided if 50 or more parties are involved. These developments, coupled with millers' dependence on growers to supply sufficient cane to allow the mill to operate at satisfactory levels of capacity, raise the possibility that it is growers rather than millers who possess the greater market power '

The BDCG submission notes 'there is no competitive market for cane' which is a perishable commodity and the majority of growers must sell their cane to a single miller (BDCG, Submission no. 13, pg.5). While this is generally correct, the significant industry reforms of 2004 and 2006 were undertaken with full knowledge of the structure of the industry. At the time, it was agreed by government, millers and cane grower representatives that the proposed reforms were necessary to ensure the future of the industry and in conjunction with the interdependencies between millers and growers, and existing legal structures, the proposed reformed regulatory structures provided adequate protections for industry participants. Since the reforms were implemented, there has been no evidence of market failure or millers misusing their market power. In particular, there is no evidence of mills misusing a market power by fundamentally altering the cane price formula that has been in place since the early 1900s.

The only change being proposed now is that Wilmar (and two other milling companies) will undertake its own marketing activity from 2017. In fact, Wilmar's actions are totally consistent with the primary objective of the 2006 marketing deregulation reforms that was to provide a regulatory framework to allow mills to determine how their raw sugar production was marketed. Wilmar is undertaking to deliver better returns for growers through its future marketing arrangements and has guaranteed that the cane price formula which determines returns to growers will not change.

The BDCG submission also claims there is an 'obvious conflict of interest and bias of Wilmar Sugar acting as the marketer and sole determinant of the net sugar value' (BDCG, Submission no. 13, pg.7). This statement is incorrect. Wilmar is not the 'sole determinant' of the net sugar price. Pricing issues are addressed in detail



in our submission (Section 3, Cane Price and Sugar Price) but in summary, the ICE#11 price represents approximately 99 per cent of the net sugar price. Marketing premiums represent approximately 8 per cent of the net sugar price, and marketing costs represent approximately 7 per cent of the net sugar price. Growers are able to make their own price risk management decisions, which determine the ICE#11 price, independently of the decisions that the miller makes.

The BDCG submission also claims that in 2010 Wilmar 'withheld or failed to pay growers \$4.25 per tonne of cane (currently subject of a legal dispute between some growers and Wilmar Sugar)' (BDCG, submission no. 13, p.20). This statement is incorrect. It relates to the significant \$106 million hedging losses incurred by QSL in 2010 that were passed back to all millers and growers via a lower sugar price. The QSL losses resulted in QSL paying mills a lower sugar price in all of its pricing pools. The cane price formula links the price paid for cane, to the net sugar price received by millers, and as a result cane growers were paid a lower price for their cane. It is important to note that Wilmar did not pass through the full effect of this lower sugar price and effectively provided growers with a credit in recognition of the difficult and unusual circumstances of the QSL loss. This was at a cost of \$4.67 million to Wilmar.

The notion of misuse of market power is also referenced in the QSL submission (QSL, Submission no. 16, p. 17) with claims that Wilmar has been looking at ways to remove QSL from the marketing of Queensland raw sugar. This is incorrect.

Wilmar has a commercial contract with QSL for the export of Wilmar's raw sugar. Wilmar does not need to "remove QSL from the marketing of raw sugar" to change its raw sugar marketing arrangements. Changes can be made by changing the terms of the raw sugar supply agreement between Wilmar and QSL, or by Wilmar terminating its contractual relationship with QSL in accordance with the terms of the agreement.

QSL claim that 'it was initially proposed that QSL should subcontract Wilmar to conduct all its marketing operations'. What QSL neglected to note was that QSL was amenable to such a concept and in 2012, voluntarily entered into an agreement with Wilmar to explore a phased transition to a marketing model whereby QSL would subcontract physical marketing and trading of all Queensland sugar to Wilmar. QSL entered into this agreement with a view to demonstrating to other QSL suppliers that Wilmar undertaking the physical sales and trading would maximise returns for raw sugar produced in Queensland.

In fact, QSL's voluntary participation in such a plan supports Wilmar's claims that it can deliver better returns for itself and its growers by undertaking the marketing and sales of its own sugar.

Delivering a commercially negotiated outcome

In its submission, QSL notes its preference for a negotiated contractual outcome for future sugar marketing arrangements, but comments that 'at this point, that unfortunately seems a very unlikely outcome' (QSL, Submission no. 16, p. 2). This theme is also carried in other industry collective submissions.

This comment overlooks the fact that discussions between Wilmar and growers on post-2017 marketing models have only recently commenced and final agreements are not ultimately required until the 2017 crushing season. Wilmar has already undertaken significant engagement with growers on the future marketing model, and will be continuing to discuss this matter with growers and their representatives in coming weeks and months with a view to reaching agreement on the concept and detail of marketing arrangements beyond 2017.

Wilmar acknowledges that it is yet to achieve grower consensus to an agreed marketing model and has committed to undertaking an extensive, open and transparent engagement process with growers and grower



collectives over the coming months. This engagement process will seek to table a number of alternative Wilmar marketing arrangements and forward pricing exposure options for consideration by grower collectives.

The principles underpinning these models will be absolutely focussed on transparently delivering better returns for Wilmar growers. Growers will have full independent audit rights, contractual and regulated protection measures and formal dispute resolution processes.

Wilmar looks forward to providing the Senate Committee with further information on the proposed engagement program in due course.

Further information on our previous and ongoing engagement activities are described in more detail below in this supplementary submission.

It should also be noted that Wilmar has given three year's notice of its intention to leave the QSL voluntary marketing arrangement, which only becomes effective from 2017, in accordance with the Raw Sugar Supply Agreement. This enables sufficient time for the negotiation of new Cane Supply Agreements. Wilmar has also put arrangements in place to facilitate the ongoing forward pricing for the 2017 season on a "business as usual" basis until June 30, 2015. A form of these agreements was successfully negotiated with the BDCG earlier this year.

Growers' Economic Interest (GEI)

There is a fundamental misunderstanding in a number of submissions around the concept of 'Grower Economic Interest' or GEI. In some cases, the concept is being deliberately misrepresented to confuse growers' and stakeholders' understanding about future marketing arrangements.

Changes were made to the Raw Sugar Supply Agreements (RSSAs) in 2013 to introduce into the contract a formal mechanism for QSL to supply part of millers' raw sugar production back to them, in order to permit them to undertake their own marketing. The amendments to the RSSA introduced the concepts of 'Supplier Economic Interest' sugar and 'Grower Economic Interest' sugar, in order to draw a distinction between that part of a miller's raw sugar production that would be supplied back to the miller, and that part which would not.

Nothing in these amendments to the RSSA created, or was intended to create, any form of grower control over Wilmar's raw sugar production.

Wilmar purchases cane from cane growers which is used to manufacture raw sugar. There is no dispute about the ownership of the sugar that millers produce from cane purchased from growers. The sugar is unequivocally owned by the miller. Under the current QSL voluntary marketing arrangement, the miller sells its sugar to QSL which then undertakes the marketing.

This is recognised in the submission from BDCG, which acknowledged that growers 'do not have legal title to the notional sugar utilised for payment purposes', and 'Wilmar Sugar had the legal right to terminate its voluntary contractual arrangements with QSL' (BDCG, Submission no. 13, p.4).

Prior to deregulation in 2006, millers were required to sell all of their sugar production to QSL. Since 2006, arrangements for QSL to market millers' sugar were entirely voluntary. Wilmar is choosing to exit its voluntary marketing agreement with QSL. It is consistent with this arrangement that Wilmar is proposing to



undertake its own marketing of its sugar from 2017. Wilmar is unaware of any like industry in Australia where the manufacturer does not have absolute discretion over how it sells the product it manufactures.

Wilmar is not proposing any change to the cane price formula, and indeed considers it fundamental to the future sustainability of the Queensland sugar industry.

As outlined in detail in our original submission (Section 3, 'Cane Price and Sugar Price') Wilmar accepts and supports the relationship that has been established between the sugar price and the cane price formula which is used to calculate the payment to growers for their cane and underpins the operation of growers' independent price risk management options.

However, this does not change the fact that millers retain the legal title to the raw sugar they have produced. It does ensure, however, that the price paid to growers for their cane is linked to the price paid to millers for their raw sugar. Therefore, growers receive the full economic benefit of the marketing premiums that millers can earn for their sugar via higher net sugar prices.

Delivering 100 per cent of the achieved 'better returns' to growers

The Canegrowers / Australian Cane Farmers submission and the QSL submission to the Inquiry both state that Wilmar's proposed new arrangements will see only 50 per cent of trading profits returned to growers. As neither submission defines what is meant by the term "trading profits", Wilmar is concerned that these statements may be easily misinterpreted, and give a totally false and misleading impression about how marketing premiums flow back to growers via higher sugar prices under Wilmar's sugar marketing proposal.

Wilmar has guaranteed to transparently return 100 per cent of the marketing premiums achieved for its Australian sugar to growers. In referring to marketing premiums, we refer to all components of the sugar price over and above the ICE#11 price. This includes physical premiums, freight premiums, polarisation premiums and spread gains¹.

Under the proposed marketing model, these premiums would be allocated to pricing pools in the same manner as is currently the case with QSL, so growers will receive exactly the same net premium as Wilmar per tonne of sugar exposure.

That means growers will receive the same marketing premium as Wilmar does, on a dollars per tonne basis. Wilmar Sugar Trading will receive no benefit from net premiums on Wilmar Sugar Australia-supplied sugar and make zero profit in respect of the net premiums on Wilmar Sugar Australia sugar.

In addition, growers will also receive 50 per cent of any arbitrage benefits involving Wilmar Sugar Australia sugar and other-origin sugar (i.e. sugar sourced elsewhere, e.g. from Brazil, or Thailand) traded by Wilmar Sugar Trading. Arbitrage benefits are those which are captured through the unique synergy that Wilmar can bring through having a significant 'book' of non-Australian sugar as well as its 'book' of Australian sugar. The arbitrage benefits are therefore a benefit available to growers that is over and above a return of 100 per cent of the marketing premiums.

¹ Spread gains are the gains that result from pricing physical sugar against an ICE#11 contract month that is different to the ICE#11 contract month under which the raw sugar is actually sold and shipped to the customer. That is, a producer might price sugar against the ICE#11 October position, as the basis of the original sale from the producer to a marketer. The marketer might then "roll" the ICE#11 October position to the following March, as the basis of the sale from the marketer to the end consumer. If the March ICE#11 contract is trading at a premium to October, the roll (buying October and selling March) makes a gain.



It is proposed to share the arbitrage benefits 50/50 with Wilmar Sugar Trading because these are benefits that only accrue because of the existence of other-origin sugar traded by Wilmar. These benefits are not available to growers in the current QSL system because QSL does not trade any material quantities of other origin sugar.

In demonstration of our commitment to transparency, Wilmar has openly committed to a series of 10 core principles which have been conveyed to growers, grower collectives and Governments.

As noted in our original submission, Wilmar's Principle #6 (outlined below) confirms that 100 per cent of net premiums will be returned to growers on a dollars per tonne basis.

6. Growers will receive the full economic benefit from the marketing and sale of sugar.

Wilmar will ensure that growers receive the full benefit of all marketing premiums earned by Wilmar on the sale of sugar, net of associated marketing costs incurred in storing and selling the sugar and making payments to growers (i.e. storage and handling, advance payment finance costs, marketing services costs etc.). In marketing its sugar production, Wilmar will act at all times to ensure that marketing premiums and costs are negotiated on a commercial arm's length basis to maximise the net sugar price on which growers' cane prices are based.

Grower independent price risk management choices

The QSL submission claims that Wilmar's marketing proposal attempts to remove the choice and influence that growers have in regard to their sugar price exposure and force the grower to accept the risk appetite of a single marketer (QSL, Submission no. 16, pg., 16). This statement is incorrect.

Wilmar has clearly outlined in its previous grower engagement materials and its submission to the Senate that growers will continue to be able to independently manage their own sugar price exposure and that Wilmar will provide them with a choice of pricing mechanisms of different risk profiles managed at the growers' discretion. In addition, in consultation with Wilmar, growers may also elect to appoint a third party pricing manager. Growers will be able to choose from a range of generic risk profile pools. Wilmar is in no way forcing growers to accept Wilmar's risk profile, or any particular pricing mechanism risk profile. However Wilmar will make available to growers, to use at their choice, at least one pricing mechanism which is managed by Wilmar in a similar manner and risk profile to that used by Wilmar to manage its own sugar price exposure. Further, QSL remains the single marketer until 2017, so currently its risk appetite must be accepted.

QSL's comments in relation to risk management are somewhat ironic given the hedging losses of \$106 million incurred by QSL in 2010 when they aggressively over-hedged the seasonal pool, (which was intended to manage production risk and variability), very early in the crushing season and consequently did not have sufficient sugar to cover their hedged positions. These hedged positions subsequently had to be closed out by QSL on the futures market which incurred significant financial losses. QSL then passed these losses back to millers and growers via a lower sugar price across all pricing pools.



Wilmar's engagement with growers on future marketing arrangements

A number of submissions make reference to Wilmar's apparent 'failure' to engage with growers or their representatives on future marketing arrangements. Furthermore, it is suggested that Wilmar is not interested in further negotiation or achieving a commercial negotiated outcome.

These claims are demonstrably incorrect.

Consistent with the terms of its agreement with QSL and the *Sugar Industry Act 1999*, Wilmar announced in April 2014 its intention to leave the QSL voluntary marketing arrangement from 2017. This was consistent with the requirement to provide three year's notice of the change.

This decision was preceded by two years of discussions with sugar industry leadership about ways in which a greater return could be achieved for growers and millers from the sale of raw sugar. A number of proposed marketing models were discussed, but rejected by Canegrowers and the Australian Cane Farmers Association. The best interests of Wilmar and its growers were best served by withdrawing from the QSL voluntary marketing arrangements.

Wilmar proposed a new marketing partnership with growers based on the establishment of a new company to oversee sugar marketing and provide returns to growers in a fully transparent manner. This proposed marketing model has been the subject of extensive consultation with growers and their representative bodies, including:

- 25 grower information sessions, covering every region and attended by the more than 500 growers;
- Group meetings with the leadership of grower collectives from each region;
- Group meetings with large growers, including those not part of collectives;
- Meetings with collective boards in each region;
- Meetings with Queensland Canegrowers Limited;
- Meetings with the Burdekin District Cane Growers (which is not aligned to Canegrowers); representing 20 per cent of Wilmar growers and 30 per cent of Wilmar's total cane supply;
- Briefings with government departments and regulatory bodies (including Queensland Department of Agriculture, Forestry and Fisheries, and the ACCC and FIRB);
- Launch of a new website that provides detailed information on the proposed sugar marketing arrangements.

We have also produced a number of information updates and bulletins for growers to help growers understand the proposed model and the opportunities to deliver better returns.

Wilmar is committed to ongoing open and transparent consultation and engagement with our growers as we progress our discussions on future marketing arrangements. We have engaged an additional three people to work as part of our Grower Pricing Team who will be able to meet with individual growers. We are developing a series of fact sheets, videos and online materials to help growers better understand fundamental issues associated with cane pricing and sugar marketing. The first of these fact sheets, covering the Cane Price Formula, Net Sugar Price and Nominal Sugar Exposure have now been published online and distributed to growers, and are attached for the Committee's information.

Wilmar is also finalising a program of engagement with grower collectives in coming months. This engagement will be focused on discussion and agreement of interim forward pricing arrangements and a future marketing model that will deliver better returns to growers and provide growers with increased flexibility over sugar price exposure management.



In its submission, QSL asserted that Wilmar 'had made it clear to Minister McVeigh (the State Minister for Agriculture, Fisheries and Forestry) and other industry participants that it is not willing to negotiate or participate' in discussions around future marketing arrangements. This is a reference to an offer of discussions around a marketing model based on Wilmar remaining with the QSL arrangement and whereby Wilmar was not free to determine how to market its own sugar production in accordance with the current industry regulation. As Wilmar had already announced its intention to leave QSL, it respectfully declined that offer.

Wilmar remains committed to progressing discussions with government, industry representatives and our growers on future marketing arrangements based on its right to independently market and sell its own sugar production consistent with the terms of the *Sugar Industry Act 1999* and the incorporated principles for export sugar marketing deregulation that was agreed by all industry participants in 2006.

Wilmar will be participating in the Queensland Government's Agricultural Cabinet Committee review of sugar marketing arrangements, and welcomes any opportunity to provide Ministers with further information on its future grower and grower collective engagement plans and objectives.

Wilmar recognises that new contracts (including a new cane supply agreements) reflecting an agreed marketing model need to be negotiated and ultimately finalised with growers and their representatives and is committed to a process of engagement and negotiation to achieve this outcome in a timely manner prior to the commencement of crushing in 2017.

Claims of 'anti-competitive' behaviour

Wilmar is a 75 per cent participant in the Sugar Australia Joint Venture (SAJV), an unincorporated joint venture operated by the manager, Sugar Australia Pty Ltd. Mackay Sugar Limited is the second participant in the SAJV, owning 25 per cent. The SAJV has sugar refining, storage and packing operations in Australia. The refining of sugar produces food-grade products such as white sugar, brown sugar, caster sugar and syrups, supplying a broad range of industrial and consumer products which are distributed in both bulk and packaged forms.

Claims have been made by the New South Wales Sugar Milling Co-operative Limited (NSWSMC) in its submission (NSWSMC, Submission no. 6) of apparent 'anti-competitive' behaviour in the market by Wilmar, through the SAJV. These claims are refuted.

The SAJV operates in a competitive environment, including competition from two local refiners and multiple import suppliers. Australia produces more refined sugar than it consumes and has several importers selling in the domestic market therefore significant competition exists in the domestic market.

NSWSMC claim that Wilmar, through SAJV, have 'refused access' for NSWSMC to the raw sugar market (NSWSMC Submission no. 6, pg. 3). This claim is refuted; raw sugar is available on commercially negotiated terms from Wilmar to any refineries and any interest is welcomed.

According to the NSWSMC submission, Wilmar, through the SAJV, offered to buy NSWSMC raw sugar, implying 'shutting an industry refinery asset' (NSWSMC Submission no. 6, pg.9). SAJV requires raw sugar for its two refineries in Australia. The business is in continual dialogue with local and foreign suppliers of raw sugar for its future needs. While SAJV does use some imported raw sugar, over 80 per cent of our refined sugar is produced from Australian raw sugar. Since deregulation in 2006, SAJV has held a number of raw sugar supply contracts with several millers in Queensland and overseas to secure its supply at the most



competitive price. Without exception, discussions on raw sugar supply have taken place with all Australian milling suppliers including NSWSMC.

NSWSMC also claim that SAJV is acting in an anticompetitive manner in respect to various matters including; selling into futures expiry positions which are lower in order to attain market share; buying contracts and locking in customers for extended periods of time; undertaking marketing activities which lower domestic premiums. These claims are refuted. SAJV sells into futures contracts according to its customer pricing requirement and delivery timing and otherwise conducts its sales and marketing activities consistent with competitive commercial practice and in accordance with all competition laws.

NSWSMC raises concerns about the proposed marketing changes restricting the ability of NSW Sugar to export and refers to Wilmar Gavilon being in control of the Brisbane Sugar Terminal which NSW Sugar refers to as an essential piece of infrastructure (NSWSMC Submission no. 6, pg. 2 and 8).

Wilmar Gavilon Pty Ltd was formed in 2007 to invest in the sourcing and distribution of a variety of feed ingredients and oils and fats and is a 50:50 Joint Venture between Wilmar International Limited and Gavilon Group LLC. In 2009, Wilmar Gavilon acquired the Brisbane Sugar Terminal from Sugar Terminals Limited (STL). As stated in NSWSMC's own submission, NSW Sugar left the QSL pooled export arrangements in 1989. We understand that the last shipment of sugar from the Brisbane Terminal occurred in 2005 and was arranged by QSL, who managed the terminal at that time. The Brisbane terminal was in effect a disused and surplus asset until its sale to Wilmar Gavilon in 2009. Since that time, we are advised by Wilmar Gavilon that they have shipped one million tonne of products and provide grain producers and other exporters a competitive alternative to other Brisbane based storage and handling providers.

Wilmar Gavilon advise that they have no record of being approached by NSW Sugar to access the terminal for the purpose of raw sugar exports.

Greater regulatory oversight or intervention

A number of submissions argue for greater regulatory intervention in sugar marketing, including greater powers for the ACCC to regulate anti-competitive behaviour. This includes suggestions for a mandatory industry code under the *Competition and Consumer Act 2010*.

Our original submission provided a comprehensive overview of the regulatory and competition environment, which included additional reports by Minter Ellison and the Centre for International Economics. It was objectively demonstrated that the current regulatory arrangements are considered to be adequate, and indeed expansively so, to protect the interests of industry participants and there are no grounds for additional regulatory intervention.

Furthermore, since the final stages of industry deregulation which commenced in 2004, there has been no market failure. Wilmar's proposal for the future marketing of its sugar is entirely consistent with the terms of sugar marketing deregulation agreed by all parties in 2006 and Wilmar has conducted its affairs in full compliance with all legal and regulatory requirements.

QSL's submission (QSL, Submission no. 16, pg. 23) seeks to argue that a miller that does not wish to give its cane suppliers a right to determine how the miller sells and markets its sugar production is refusing to decouple cane acquisition and crushing services from marketing and export services, and is therefore likely to be misusing market power. Wilmar finds this a very strange conclusion as milling services are not being acquired by the growers; the growers are selling cane to the mills, who in turn manufacture a product (raw sugar) which is then sold to refining customers. Millers pay growers for cane on the basis of sugar price and



as a service to growers, facilitate grower price risk management in order for growers to independently manage their sugar price exposure. The process of transfer of title to cane from grower to miller and title to sugar from miller to marketer and sugar is clear. In simple terms, QSL's proposition is that a raw material supplier should have rights to determine how a manufacturer should sell the manufacturer's finished product. Wilmar refutes this concept.

In its submission, QSL also asserts that complaints have been made to the ACCC by grower groups about Wilmar's conduct 'with no apparent action having been taken to date' (QSL, Submission no. 16, pg. 2).

Wilmar has a policy of open and constructive engagement with the ACCC. We have kept the ACCC briefed on our proposal for future marketing arrangements. The ACCC, to our knowledge, has not initiated any formal investigation of Wilmar in relation to its conduct. Wilmar is committed to proactively updating the ACCC on the details and status of future pricing and supply agreements, industry engagement and commercial negotiations.

Thank you for the opportunity to provide this supplementary response to submissions by other parties, and I would be happy to assist the Senate Committee with any further information it may require to assist its inquiry.

Yours sincerely

Shayne Rutherford
Executive General Manager
Strategy and Business Development

CANE PRICE FORMULA



History of the cane price formula

The formula has a long history dating back to the early 1900s:

$$\text{Cane Price} = \text{Sugar Price} \times 0.009 \times (\text{CCS}^* - 4) + \text{Constant}$$

*The recoverable sugar content from sugar cane crushed by a sugar mill is termed the Commercial Cane Sugar (CCS) content of cane.

With very minimal adjustment (in fact, only to the value of the Constant), this formula is still in use for most Queensland mills. The linkage of cane price to sugar price underpins the operation of today's grower price risk management choices.

The original formula was introduced in the early 1900's when CCS was around 12 and mill efficiency (Coefficient of Work, or COW) was around 90%. In effect, the formula divided the revenue earned from the sale of raw sugar into approximately 2/3 for the grower and 1/3 for the miller.

Since the early 1900's, cane quality and milling efficiency have both significantly improved. However despite these changes, and the fact that neither the formula nor any specific division of sugar revenue has been legislated, the cane price formula has endured.

One of the reasons for this is that the formula cleverly incentivised the parties to improve their individual sections of the industry. If growers' grew sweeter cane they would keep the value of any additional CCS above 12. If the mills were to invest in better equipment and technology they would keep efficiency gains above 90% COW. This is exactly what has happened.

Commercial Cane Sugar (CCS)

CCS is a measure of the sucrose that is commercially obtainable from cane. The CCS content in cane varies across the crushing season. Today, the CCS used in the cane price formula is a grower's 'relative CCS'. Relative CCS is used as opposed to actual CCS of delivered cane so growers who harvest and deliver at different times during the season are not disadvantaged relative to other growers.

Sugar Price

The sugar price used in the cane price formula is the net sugar price received by the miller for the sale of sugar after the inclusion of marketing premiums and costs. Marketing premiums include polarisation premiums and physical premiums. Marketing costs include sugar storage and handling costs, finance costs for advance payments, pricing and marketing administration costs.

Internationally traded sugar contracts are based on raw sugar of 96 degrees polarisation as measured by the International Polarisation Scale (IPS), which is the equivalent of saying that the sugar contains 96% sucrose. These contracts also specify standard payment adjustment factors to account for sugar with different sucrose content or polarisation. The Queensland sugar industry typically produces sugar which has a polarisation close to 99 degrees which results in an additional polarisation premium of approximately 3.7 per cent. In addition to polarisation premiums, Queensland sugar also attracts physical premiums because we are closer to Asian markets than other suppliers such as Brazil.

To align industry payments on a similar basis to internationally traded sugar, the Queensland sugar industry has also developed a standardised method for converting tonnes of sugar at its typical production quality of 99 degrees polarisation, to an equivalent amount of tonnes of sugar at 96 degrees polarisation, or tonnes IPS. Sugar price in the Queensland industry is therefore expressed in dollars per tonne IPS (AUD/IPS tonne).

WILMAR'S CANE PRICE FORMULA

Wilmar's cane price in AUD/tonne of cane is determined by:

SUGAR PRICE is based on the weighted average outcome resulting from a grower's pooling and forward pricing decisions for the season and is expressed in units of AUD/IPS tonne.

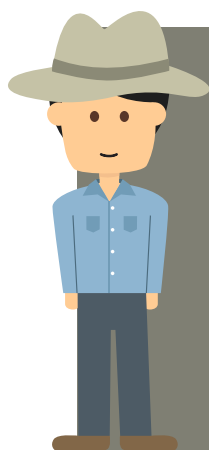
THE CONSTANT is the result of changes over time, expressed in cents per tonne of cane.

$$\text{CANE PRICE} = 0.009 \times \text{SUGAR PRICE} \times (\text{CCS} - 4) + \text{CONSTANT}$$

CCS is the grower's relative CCS determined in accordance with the methodology specified in the grower's Cane Supply Agreement which varies slightly from region to region.

Mick and Tony

Let us introduce two cane growers* with different pricing decisions and growing conditions. Through a series of factsheets we're going to track Mick and Tony's decisions on their farms, to see how each element of the pricing process affects their cane revenue.



MICK

manages an irrigated cane farm in the Burdekin area. Mick started cane farming 20 years ago having firstly bought a 150 hectare farm in the Burdekin Irrigation Area auction scheme. He's since purchased additional land and now farms 267 hectares. Mick had no prior knowledge of cane farming until his original farm purchase 20 years ago. He was previously a cattle and cotton farmer from Emerald and has a high level of understanding on how commodity hedges can help with managing price risk. He has a low appetite for risk and uses hedging mechanisms conservatively.

Mick's farm produces 25,000 cane tonnes (5 year average) on an 85% rotation. His average cane yield is 110 tonnes per hectare. His cane consistently measures above mill average CCS. Last season his relative CCS was 14.9. It is assumed the Constant for Mick's cane price formula is 0.6.

Mick's sugar price is \$466.50/tonne based on the weighted average outcome of his pooling and forward pricing decisions.

Mick's cane price

Based on the information above, Mick's cane price is:

$$0.009 \times (14.9 - 4) \times \$466.50 + 0.6 = \$46.36/\text{tonne of cane}$$

TONY

farms in the Herbert River district and runs a 166 hectare farm producing 12,000 tonnes of cane at 85 tonnes per hectare (85% rotation). Tony is a third generation cane farmer. He has low debt levels, though his cane performed below expectation last season when the relative CCS in his cane was 13.45. Tony's farm was badly affected by last season's excessive wet weather.

Despite the wet weather impact on the cane crop, his farm has recovered well after being battered by Cyclone Fran in 2012 when it only produced 9,600 tonnes of cane (equivalent to a 20% production loss from average production). Sugar price risk management is a new subject to Tony; he is not fully across the subject but thinks it is a good idea. It is assumed the Constant for Tony's cane price formula is 0.6

Tony's sugar price is \$481.50/tonne based on the weighted average outcome of his pooling and pricing decisions.

Tony's cane price

Based on the information above, Tony's cane price is:

$$0.009 \times (13.45 - 4) \times \$481.50 + 0.6 = \$41.55/\text{tonne of cane}$$



*hypothetical case studies, not based on any individual farm or cane grower.



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NOMINAL SUGAR EXPOSURE



Nominal sugar exposure

As a result of the linkage between cane price and sugar price in the cane price formula, growers have an underlying exposure to sugar price.

As the sugar industry has progressively deregulated, growers have been provided opportunities to individually manage their sugar price exposure independently from the price risk management decisions of their miller.

Grower price risk management is enabled by Wilmar calculating a grower's Nominal Sugar Exposure (NSE) and facilitating the grower making decisions about how the risk on this exposure is managed. Wilmar enables the grower to 'allocate' their Nominal Sugar Exposure to various forward pricing mechanisms (Call or Target pricing) or fixed-tonnage pools. In doing so, Wilmar agrees that the pricing outcomes achieved in each of these pricing methods will determine the price Wilmar receives for that portion of its sugar. In turn, this same price will be used by Wilmar as the basis for determining the grower's cane payment.

A grower's Nominal Sugar Exposure may be derived from the cane price formula and the tonnes of cane that a grower supplies the mill. As growers do not produce raw sugar, Wilmar refers to a grower's Nominal Sugar Exposure to indicate that the sugar tonnes are 'in name only' and therefore 'nominal'.

A grower's 'Nominal Sugar Exposure', expressed in units of tonnes of nominal sugar, is determined from the following formula:

$$\text{Grower's Nominal Sugar Exposure} = \text{Tonnes of cane} \times 0.009 \times (\text{CCS}^* - 4)$$

* CCS is a grower's relative CCS.

Allocation of Nominal Sugar Exposure

Until the finish of crushing in any particular season the NSE is just an estimate. This is because the final cane quantity and the relative CCS for the grower are yet to be determined. Nevertheless, subject to various restrictions in order to prevent over-pricing, a grower has the opportunity before a season commences to allocate portions of their estimated NSE to different fixed-tonnage pools or to use Wilmar's Target or Call forward pricing mechanisms.

As an example, under Wilmar's current forward pricing arrangements, the proportion of the grower's NSE that can be forward priced is:

1st forward year (i.e. as a season becomes 'current')	60% of estimated NSE
2nd forward year	40% of estimated NSE
3rd forward year	30% of estimated NSE

The primary reason for limiting the amount of a grower's NSE that can be committed in forward seasons is because growers are subject to production risks caused by weather and disease (e.g. Orange Rust outbreak, Yellow Canopy Syndrome, cyclone damage or persistent wet weather during crushing) and may not be able to supply sufficient cane to cover the full amount of their estimated future NSE.

Meeting committed NSE

A grower must supply Wilmar with sufficient cane to cover that portion of their NSE which has been forward-priced or committed to fixed tonnage pools. Wilmar needs to have the cane to produce the physical sugar underlying the sugar futures contracts that have been entered into in respect of this NSE. This is because these positions need to be closed out to achieve the hedged price. Failure to supply the same amount of physical sugar that has been hedged can result in financial losses.

The tonnes of cane required to cover a grower's committed NSE will depend on the CCS of the cane the grower supplies to the mill.

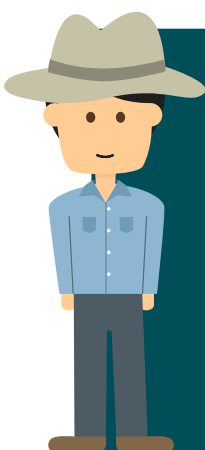
The quantity of cane required to cover the grower's committed NSE may be calculated using the formula below.

The following table demonstrates the relationship between cane tonnes and Nominal Sugar Exposure.

NSE Tonnes	Farm CCS	Cane Tonnes
300	12	4,167
300	13	3,704
300	14	3,333
300	15	3,030
300	16	2,778

So, a grower who produces 13 CCS cane will be required to supply 3,704 tonnes of cane for every 300 tonnes of NSE committed while a grower who produces 15 CCS cane will require only 3,030 tonnes of cane to be supplied for every 300 tonnes of NSE committed. That is, the CCS will determine the amount of cane required to be supplied for any given amount of NSE that is committed to these types of pricing methods.

$$\text{Cane Tonnes} = \text{Nominal Sugar Exposure} \div [0.009 \times (\text{CCS} - 4)]$$



TONY AND MICK*

Mick manages an irrigated cane farm in the Burdekin area, which produces 25,000 tonnes of cane (5 year average) on an 85% rotation. His average cane yield is 110 tonnes per hectare. Last season his relative CCS was 14.9.

However, to calculate Mick's estimated NSE it is necessary to initially use his 5 year average relative CCS, which is 14.85.

Mick's NSE = 25,000 x 0.009 x (14.85 - 4) = 2,441 nominal sugar tonnes

Mick's forward pricing (Target and Call pricing mechanisms) and fixed tonnage pool limits are then 1,465 next season (i.e. 60%) and then 976 and 732 nominal sugar tonnes in the next two forward seasons, respectively.



Tony farms in the Herbert River district and runs a 166 hectare farm producing 12,000 tonnes of cane at 85 tonnes per hectare (85% rotation). To calculate Tony's estimated NSE his 5 year average relative CCS 13.36 is used.

Tony's NSE = 12,000 x 0.009 x (13.36 - 4) = 1,011 nominal sugar tonnes

Tony's NSE is 1,011 nominal sugar tonnes and thus his forward pricing sugar limits are 607 (i.e. 60%), 404 and 302 nominal sugar tonnes, respectively.

*Hypothetical case studies, not based on any individual farm or cane grower.



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NET SUGAR PRICE



Net Sugar Price

Under the cane price formula, the price of cane is a function of the sugar content of the cane (CCS) and the Net Sugar Price received.

The Net Sugar Price on which any individual grower's cane payments are made is based on the ICE #11 outcome of that grower's individual price risk management decisions and the marketing premiums and costs which are averaged across all QSL managed sugar sales.

Based on the average of the last five years of data from QSL and using the QSL Harvest Pool price as the reference:

- The ICE#11 price represent approximately 99 per cent of the Net Sugar Price
- Marketing Premiums represent approximately 8 per cent of the Net Sugar Price
- Marketing Costs represent approximately 7 per cent of the Net Sugar Price

This is outlined in more detail below.

ICE#11 Price

Raw sugar is traded in a global market. The Intercontinental Exchange No.11 contract (ICE#11) is a futures contract for the physical delivery of raw cane sugar and is the benchmark and basis for the price risk management and physical trading of raw sugar around the world.

The ICE #11 contract is based on free on board (FOB) sales of raw sugar assuming 96 degrees polarisation (i.e. equivalent to 96% sucrose) and is measured in US cents per pound. The ICE#11 contract terms specify standard payment adjustment factors to account for sugar of different polarisation.

Grower price risk management is effected via management of the ICE#11 component of Net Sugar Price.

Growers can exercise choice, either directly (e.g. using forward pricing) or indirectly (through pool and pool manager selection), which determines the ICE#11 price outcome for their Nominal Sugar Exposure on which the price of their cane is based.

The ICE#11 price makes up approximately 99 per cent of the Net Sugar Price. Therefore, via grower price risk management, growers exercise choice that determines ~99 per cent of the Net Sugar Price used to calculate the price of their cane. As growers make hedging choices individually, net sugar price outcomes will vary between growers. Importantly, growers exercise the price risk management choices independently of the price risk management choices that millers make on their own price exposure.

Net Sugar Price can be expressed as:

$$\text{Net Sugar Price} = \text{ICE\#11 Price} + \text{Marketing Premiums} - \text{Marketing Costs}$$

Marketing Premiums

Physical raw sugar sales contracts are typically quoted with reference to a particular ICE#11 sugar futures contract. The invoice price reflects the underlying settlement price of the ICE#11 contract, plus adjustments for sugar polarisation, plus any additional price components negotiated between the buyer and seller.

Marketing Premiums = Physical Premiums + Polarisation Premiums

The additional price components over and above the underlying ICE#11 future price are referred to as Marketing Premiums and consist of physical premiums and polarisation premiums.

Physical Premiums arise for Queensland sugar producers because we are closer to Asian markets than other suppliers such as Brazil. Sometimes the Physical Premium might be referred to as the 'Regional Premium' or the 'Far East Premium'.

Polarisation Premiums are price premiums paid, as specified under the ICE#11 contract, for sugar that has higher sucrose purity (or polarisation) than the ICE#11 reference of 96 degrees polarisation. The Queensland sugar industry typically produces sugar close to 99 degrees polarisation. As an example, 98.95 degrees polarisation would give rise to a polarisation payment adjustment of an additional ~3.7 per cent*. The Polarisation Premium is by convention applied to the sum of the ICE#11 price plus the Physical Premium.

Marketing premiums typically contribute approximately 8 per cent of the Net Sugar Price.

Marketing Costs

Marketing Costs are incurred in managing the physical sale and associated price risk management activities of sugar marketing. Queensland mills have traditionally delivered sugar to QSL on a free in store (FIS) basis, at the bulk sugar terminals. Marketing costs include items such as:

- Storage and handling costs in Queensland sugar terminals
- Finance charges for advance payments to the industry ahead of sugar sales
- Indirect marketing charges/costs for sugar quality sampling and management
- Marketing services charges for managing the pricing and pooling, physical sales, operations, funding, advances and administration

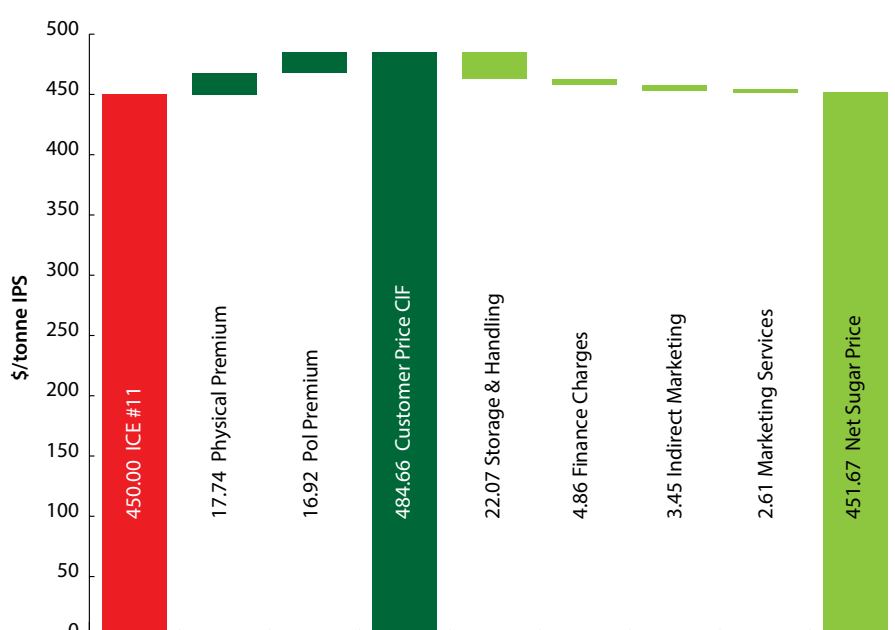
Marketing costs typically account for approximately 7 per cent of the Net Sugar Price.

Net Marketing Premiums and Costs

Marketing Premiums and Marketing Costs are of similar magnitude and have tended to net each other out. Over the last 5 years, QSL's Marketing Premium net of Marketing Costs has averaged \$1.67/tonne IPS, representing approximately 1 per cent of the Net Sugar Price. Marketing Premium net of Marketing Costs over that period has ranged from minus \$1/tonne IPS to plus \$6.50/tonne IPS of sugar.

Figure 1 shows the average marketing premiums and costs from the Table 1, using an example ICE#11 price of \$450/tonne. The net premium in this instance is \$1.67 resulting in a net sugar price of \$451.67/tonne IPS, of which the ICE#11 is 99.6%.

Figure 1



QSL 5 Year Average Data (2009 – 2013 seasons)

Table 1

	A\$ per tonne IPS
Marketing Premiums	34.66
Physical Premiums	17.74
Pol Premiums	16.92
Marketing Costs	33.00
Storage & Handling	22.07
Finance Charges	4.86
Indirect Marketing	3.45
Marketing Services	2.61
Net premium / (cost)	1.67

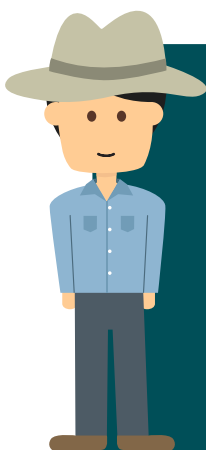
*Please note that Physical Premiums and the Polarisation Premium are calculated across all raw sugar.

How does the International Polarisation Scale for the sale of raw sugar work?

The International Polarisation Scale specifies premiums and discounts applied to the trade of raw sugar on the basis of polarisation. The thresholds and premiums applied are:

Degrees Polarisation	96 to 97	97 to 98	Above 98
Premium	1.5% of the underlying value of the raw sugar	1.25% of the underlying value of the raw sugar	1% per degree of pol, pro-rata, of the underlying value of the raw sugar

As a result, for raw sugar of 98.95 degrees polarisation the premium is calculated as $1.5\% + 1.25\% + 0.95\% = 3.7\%$.



MICK AND TONY*

Mick's Burdekin farm produces 25,000 tonnes of cane, and has forward priced the maximum Nominal Sugar Exposure for his production; a total of 2,441 nominal sugar tonnes.

The ICE#11 price he has locked in is an average of AUD465/tonne IPS.

Tony's farm in the Herbert produces 12,000 tonnes of cane, and has also forward priced the maximum Nominal Sugar Exposure for his production, 1,011 nominal sugar tonnes. The ICE#11 price he has secured is AUD480/tonne IPS.

A standardised method is used to convert tonnes of sugar at its typical production quality of 99 degrees polarisation, to an equivalent amount of tonnes of sugar at 96 degrees polarisation or tonnes IPS.

In the harvest year the marketing premiums and costs achieved are:

	Mick	Tony
ICE#11	465.00	480.00
Marketing Premiums	35.00	35.00
Physical Premiums	18.00	18.00
Pol Premiums	17.00	17.00
Marketing Costs	33.50	33.50
Storage & Handling	22.10	22.10
Finance Charges	5.00	5.00
Indirect Marketing	3.40	3.40
Marketing Services	3.00	3.00
Net premium / (cost)	1.50	1.50
Net sugar price	466.50	481.50



*Hypothetical case studies, not based on any individual farm or cane grower.



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