Grain Producers SA

20th February 2015

Grain Producers SA (GPSA) Submission to the Senate Standing Committees on Rural and Regional Affairs and Transport re Grain Export Networks, including the on- and off-farm storage, transport, handling and export of Australian grain.

GPSA would like to make reference to the following events which have occurred during the Senate RRAT committee Inquiry into grain export networks, including:-

- Harvest 14/15, including formal harvest survey of our members
- The enactment of the Mandatory Port Code of Access
- Response to Glencore submission to the Senate RRAT committee Inquiry into grain export networks

GPSA wish through this submission to address these events:-

1) **Harvest 2014/15:**

a. There is an estimated $400m to $600m supply chain cost in SA (Minister for Agriculture Leon Bignell media release 24 January 15 and 6 August 2014). These supply chain costs include vessel loading charges, storage and handling charges (Free on Board - FOB costs) and upcountry freight costs charges primarily via the monopoly bulk handling company Viterra, which is a wholly owned subsidiary of Glencore. Viterra dominates the South Australian grain handling industry through ownership of all bulk grain loading port facilities in South Australia and over 10 million tonnes of grain handling capacity.
   - This is a huge uncontested and unsubstantiated cost to the South Australian community and farmers in particular requiring independent review by the Essential Services Commission of South Australia (ESCOSA) as per the recommendations from the SA Parliamentary Select committee investigating the grain handling industry in South Australia. GPSA believes that the oversight of monopoly service providers should extend beyond those of privatised government corporations to also include commercial entities providing essential services that hold monopoly powers. Indeed, it could be argued that Viterra has greater market share of grain handling services in South Australia than SA Power Networks in electricity distribution or SA Water in water supply infrastructure.
   - GPSA estimates that $43 of the $72 (Australian Export Grain Innovation Centre (AEGIC)'s report "The Cost of Australia's bulk grain export chains", January 2014) of supply chain costs are FOB and outside the control or influence of South Australian grain producers. In addition Viterra provides grain logistics services from its up country storage and handling infrastructure to the ports via its packaged services "Export Select" which reduces the incentive for grain exporters to arrange alternative, competing

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logistic services. Again, this expense is also outside of South Australian grain producers' ability to influence as the fees are charged to exporters and then passed onto growers.

- Some exporters are hesitant to negotiate fees with Viterra due to their market dominance and ability to "squeeze" them in the market. An exporter contacted GPSA in January 2015 to complain about the increase in "Transfer In-Store Administration Fee" from \$0.25/tonne to \$0.50/tonne (Viterra Reference Prices 2014/15 section 3.15). For this small to medium sized trader the fees amounted to around \$300,000 per annum to effectively electronically transfer ownership of grain (a very expensive bank charge). The exporter was not going to proceed to arbitration under the Mandatory code for fear of retribution.

b. GPSA 2014/15 harvest survey confirms farmers in SA have limited on-farm storage (Table 1). This is due to substantial historical investment by growers and government in a centralised bulk handling system established to provide an efficient and cost effective supply chain for the export of grain. Currently there is no benefit in farmers investing in on-farm storage for more than harvest efficiencies as the cost to enter the monopolised supply chain doesn't vary throughout the year to account for the value added though on-farm storage and/or off season transportation.

Table 1: Grower response (GPSA grain producer survey, 278 responses from 2000 business surveyed)

Approximately what percentage of your grain did you store on-farm post harvest this season?		
Answer Options	Response Percent	Response Count
0	41.2%	106
10	38.1%	98
20	7.8%	20
30	3.9%	10
40	1.6%	4
50	0.4%	1
60	1.9%	5
70	0.0%	0
80	1.6%	4
90	0.8%	2
100	2.7%	7
	answered question	257
	skipped question	21

- 87% of respondents deliver all harvested grain direct to a storage and handling facility during harvest and are therefore reliant on harvest grain logistics;
- Only 13% of respondents store more than 20% of their crop on farm postharvest

c. Grain growers on the Eyre Peninsula have raised concerns around market transparency and contestability in the Canola market in 2014/15 harvest. Concerns relate to the export of canola by Glencore from its Viterra facility at Port Lincoln in early November. Growers question whether Glencore at that time had complete ownership of the export parcel at the time of shipping. Growers feel that it was early in the season and that the canola stock held in warehouse was owned by growers and had at that time not been sold or transferred to grain buyers. It is of concern that for potential logistic efficiency that stock may be transferred and shipped without first buying the grain.

2) Mandatory Port Code of Conduct:

Support of the Code is support for the grain producing farmers of South Australia (SA) because;

There is no current or likely material competition at any of the six operational bulk grain exporting ports around SA, which has contributed too;

- FOB costs are the largest single production expense for SA grain producers, $43/t or a total cost of up to $300m p.a. from SA Farmers who have had very little power to negotiate these fees.
- Cost from farm gate to ship hold have risen rapidly from $38 to $72 per tonne.

The Code commands a level of "stocks" transparency that will likely increase competition for grain from grain buyers.

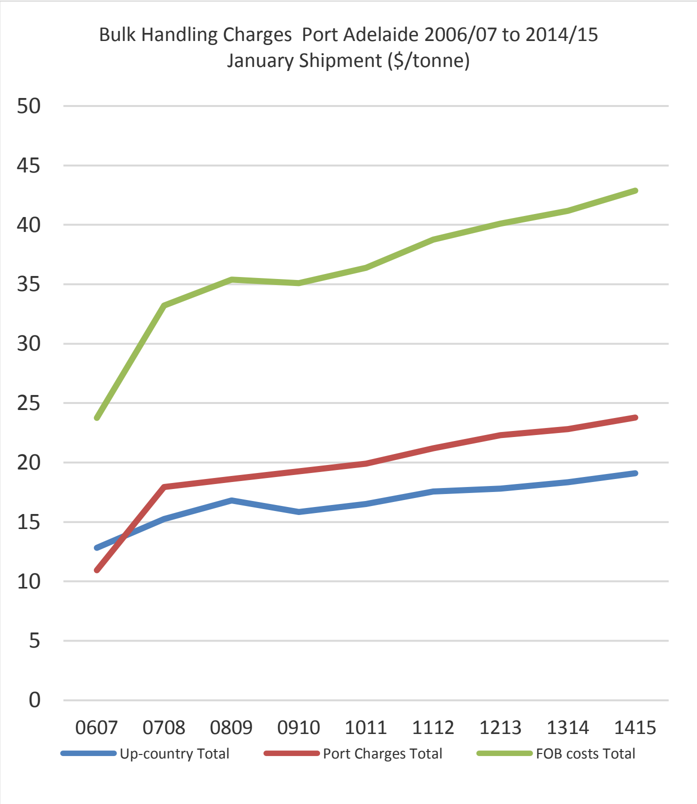
The investment of implementing and administering the Code is insignificant compared to the potential benefit.

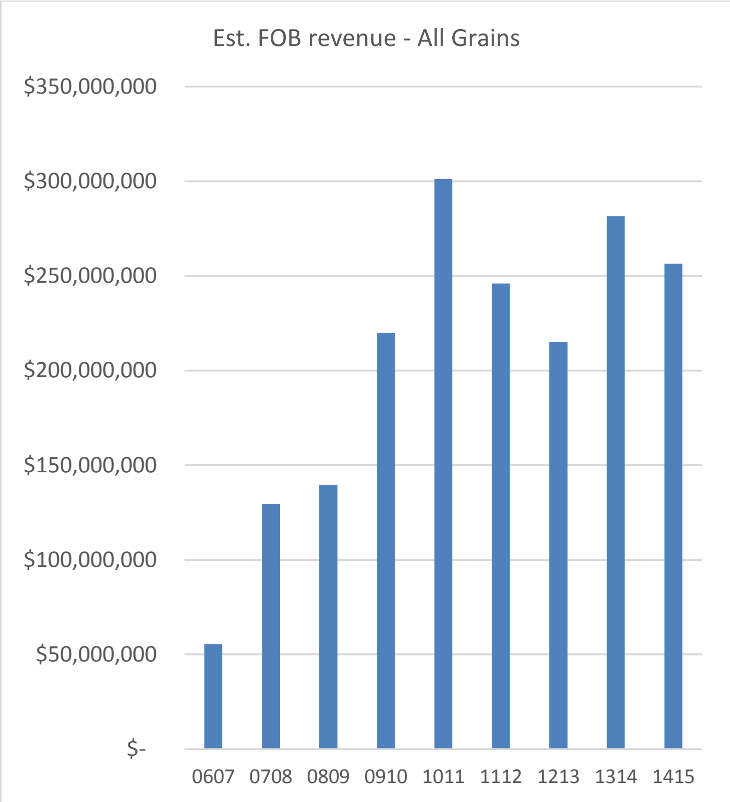
a. Competition; as all grain port terminal facilities in South Australia are owned by the same company, there is no competition between these ports. When the costs to use the ports are analysed, there is just $2.25/t difference between the ports Free on Board (FOB) costs or under 5% difference. It is unlikely we will see additional grain exporting infrastructure created in the foreseeable future as it is difficult to envisage a compelling business case for additional capacity in an over supplied area of the logistics chain therefore a non-competitive environment is likely for the foreseeable future. This monopoly needs to be overseen by a regulatory body (ACCC) through the Code until any material competition is established. The value of competition was demonstrated with a recent change of allocation of shipping slots from "first in, first served" to a competitive auction system for shipping slots. This system has generated increased competition, resulting in an extra $90 million for grain producers across South Australia from last harvest. (GPSA December/January 2014/15 Newsletter) [1].

[1] http://grainproducerssa.rvrapid.com/?i=GPSA%20Newsletter%20-%20February%2015a#folio=1

b. Cost; the above environment is not new to SA. It has been in place for more than five years. Over that time there has been limited effective regulation leading to unjustified cost increases for grain farmers. Since 2006/07 season we calculate from publicly available information FOB has increased by 80%. Last season alone this was an expense of $270 million to the grain producers of SA. (See graphs below).

Table 2: Extraordinary Increases in storage and handling costs





Source: Publically available Viterra Fee Schedules & PIRSA Crop & Pasture Reports

In addition, Location Differentials (LD's) the cost from farmers local silo to port we calculate again from publically available information has increased by 19% over just the last 5 seasons. In SA LD values are set each season at Viterra's 1st October rates for the whole industry. These massive increases are despite significant efficiency gains over the same period of time in "mass management" arrangements with logistics companies and regulatory authorities. LD's in SA are approximately 33% higher in areas where there is no competition e.g. Lameroo $0.126/km vs. Wolseley $0.93/km.

These are examples of why, farm gate to ship hold costs are now the single largest individual expense incurred by grain producers as reported by AEGIC ("The Cost of Australia's bulk grain export chains" January 2014) and why support the Code which allows the ACCC to explore these charges and therefore could and should lead to a reduction in these costs.

c. Stocks; "Knowledge is power. Information is power. The secreting or hoarding of knowledge or information may be an act of tyranny camouflaged as humility" Robin Morgan. In this business situation information likely leads to profit. Commercial markets only operate effectively and efficiently in the presence of information and if information is known by one commercial party and not others the knowledgeable one stands to profit. In SA, Glencore, the trading company and owner of Viterra that stores and handles approximately 90% of SA's grain harvest has knowledge of grain inventories that other traders don't. Without the Code it is unlikely there would be any significant knowledge of grain stocks held by Viterra for other traders putting them at a very significant commercial disadvantage. Indeed, if that was the case we would anticipate a number of the nineteen current grain traders operating in SA, at least reducing their buying activities or possibly leaving the states grain market altogether. This would lead to less competition for our member's grain and likely lower prices.

The Code is the only tangible reason the port operator in SA provides any stocks information which is essential and a bare minimum for a healthy grain trading environment.

d. Investment; GPSA estimate the cost of implementing and administering the code to be $340k, just $0.05 cents per tonne per annum vs total supply chain expenditure by SA Farmers of more than $400 million. This expense of $340k is less than the dust charge levied against SA grain producers of approximately $0.45 per tonne. The code is likely to save a great deal more than this $340k for our farmers and offer upsides of greater opportunities to sell their grain at prices driven by a freer and fairer market place.

GPSA support the code however it needs to be strengthened in the following areas:-

- Currently the code does not cover potential upcountry "collusion" including freight rates, location differentials and stocks information. GPSA strongly support the VFF submission recommendations #3 & #4 on this subject; pages 7-11 of their submission.
- The Code does not currently have significant provisions for grain producers to be a part of logistics costs that are passed onto them. Farmers that produce grain in South Australia pay for the cost of getting grain from farm gate to the ships hold e.g. FOB & LD charges. Until the introduction of the Code on 30 September 2014 farmers who pay the bill were excluded from the negotiating table of these arrangements. Under the immediate past regime only an accredited wheat exporter got a seat at the table which farmers are not as they typically sell grain to grain trading companies that are accredited exporters. GPSA recommend that farmers or their representatives have the opportunity to be involved directly in these negotiations rather than reactively.

3) Response to Glencore/Viterra submission:-

a. GPSA refute their assessment on page 11 of their submission, that "*The number of inquiries and reviews of the grains industry that have taken place since deregulation risk creating a negative perception that there are problems with the Australian grain industry. This perception has the potential to drive international exporters, customers and investors away from Australia to the detriment of growers and the industry*." GPSA proffer that the issues being addressed by these inquiries are real at various levels of government and industry and are yet to be resolved satisfactorily, thus the number of inquiries.

b. GPSA challenge their assessment of “increasing returns to farm gate” on page 6 of their submission where they state their *“IT systems and processes that support the operations streamline stock management and control and give growers the ability to transact with these buyers in real time.”* GPSA proffer that this is at an extraordinary cost. E.g. just one of their fees “Transfer In-Store Administration Fee” of 30 to 50 cents per tonne (dependent on location) we conservatively estimate yielded Glencore/Viterra $3m this past season alone.

c. GPSA further challenge their assumption on page 6 of their submission that “*According to the latest Australian Export Grains Innovation Centre report into the Cost of Australia’s bulk grain export supply chains released in June 2014, “Export grain supply chain costs currently area lesser proportion of the wheat FOB price than was the case in the late 1980s.” This has been achieved by increasing the efficiency and cost effective operation of the supply chain and has provided greater farm profitability for growers.*” This is at best miss leading if not deceptive behaviour when quick research reveals that during the mid-80’s wheat prices were at one of the lowest points for the last 50 years. (CBOT 31st Oct ‘86 was 260 cents/bu.)

d. It is incorrect to assert *“In South Australia, there are no constraints on new entrants being able to provide grain transport, storage and handling services.”* As per page 4 paragraph 6 of their submission. GPSA find the operations and third party pricing structures offered by Viterra are set to dissuade new entrants and so far have seen the demise of at least one contender namely EP Storage at Taragoro on the Eyre Peninsula and the mothballing of the Naracoorte Graincorp site.

Other:-

Breaks in infrastructure reduce efficiency, competition and subsequently increase costs. E.g. differing railway gauges, unconnected railways Pinnaroo/Murrayville & Eyre Peninsula. (Refer GrainCorp submission) GMO restrictions in SA. (Refer CropLife submission).

Recommendations:-

- The Senate write to the Treasurer of South Australia and request he call on ESCOSA to immediately review the SA Grain Supply Chain costs from Farm Gate to Vessel as per SA Parliamentary Select committee investigating the grain handling industry in South Australia – Final report September 2012, recommendations.
- The Senate support the Mandatory Code for port access and the benefits it provides to grain producers in lifting farm gate grain prices.
- The Senate support the retention of the auction system to allocate the shipping stem in South Australia.

Appendix One: Excerpt from Grain Producers SA Newsletter, December/January 2014/15

Grain Producers SA

News

DECEMBER / JANUARY 2014-15

Auction system attracts price premium

Auctioning shipping slots from South Australian ports is creating competition in storage and handling for producers. A prime location and time - such as Port Lincoln (pictured) in February - would command a premium from exporters.

SOUTH Australian grain producers will have an extra $90 million in their pockets after harvest 2014-15 because of changes to the way shipping slots are allocated at South Australian ports.

The previous 'first in, first served' policy meant the shipping stem was quickly booked. However, the auction system – now operating in South Australia – has generated increased competition for shipping slots.

ProFarmer claims prime shipping slots sold for $60/t. This means marketers were keen to secure grain to fill their shipping and rail arrangement obligations, rather than have the space booked and not have any grain to outload.

Grain Producers SA chief executive Darren Arney says the auction system means any trader can compete for shipping slots in an open and transparent process.

"The changes mean there is now a value on the ability to move grain and it has supported demand for grain out of SA this year," Mr Arney said.

"Exporters who see the most value in exporting from certain ports at certain times of the year will pay a premium for access.

"For producers, the quick booking of the shipping stem has increased demand for grain to be exported, which has pushed up prices."

Since GPSA started in 2011, it has called for an auction system to give producers competition in the storage and handling system. It was also a recommendation of the South Australian Grain Handling Select Committee Inquiry and the Senate Inquiry into Grain Handling.

GPSA's continued communication with the Australian Competition and Consumer Commission helped bring about the change.

Mr Arney said the success of the new system was in the fact that South Australian wheat prices had been $10-$20/t higher than Western Australian prices, when in the past they had been $10/t lower.

"GPSA will look to strongly support the auction system moving forward under the new mandatory code for port access," he said.

How it works ...

- Access to South Australian ports to export grain is auctioned by Viterra using an independent auctioneering group, Trade Slot.
- The structure was approved by the Australian Competition and Consumer Commission through extensive industry consultation.
- All shipping slots are available by auction. Some slots are in higher demand than others - such as outloading from Port Lincoln in February - and so attract a higher price.
- Money paid as part of the auction system is held in trust and is repaid back to the companies involved, depending on the tonnages exported as a proportion of the total. If the slot is not used, the money is not repaid.

> See over page

> continued from page 1

The industry says...

There is no doubt the auction system has created additional competition in the marketplace. We've had times this season where the SA wheat market has been trading at parity or over the Victorian market. We have even seen Victorian grain moving into SA, when Victoria should be trading in a drought market given the Wimmera's tight finish. Victorian prices are often $15-$20 higher when they are in drought, attracting SA grain. But this year, because of the early booking, there's a desire to get a large amount of grain into SA to fill the slots.

Chris Heinjus,
Rural Directions, Clare.

The auction system has allowed all buyers, large, medium and small, the opportunity to secure shipping. Over the past three years, we have seen above-average pricing at harvest due to all buyers having the opportunity to participate. This creates more competition, which has led to more volatility through early harvest as marketers look to cover shipping needs. In the past three years, there have been some good harvest prices but that has been against the 10-year trend. The world is increasingly in need of reliable food sources and SA has a great reputation, we don't have the domestic markets and it has created interest internationally.

Stephen Whillas,
EP Integrated Commodities

What we see is the cost of not doing business – marketers are keen to meet these shipping slot obligations, rather than risk foregoing the upfront cost. There are not the same premiums for shipping slots on the east coast. Some merchants may have 'take' or 'pay' rail arrangements that need to be paid for even if they are not used. This can encourage buyers to enter the market when they otherwise may not have.

Hannah Janson,
ProFarmer