CPC

# Submission to the House of Representatives Standing Committee on Agriculture and Water Resources

## June 2018

Consolidated Pastoral Company Pty Ltd

P.O. Box 332

Wilston QLD 4051

The Secretary
House of Representatives Standing Committee on Agriculture and Water Resources
PO Box 6021
Parliament House
Canberra
ACT 2600

Dear Secretary,

Please find **attached** Consolidated Pastoral Company's submission to House of Representatives Standing Committee on Agriculture and Water Resources inquiry into the superannuation industry and agriculture.

This inquiry provides the opportunity for the parliament, and other stakeholders, to explore policy options to facilitate an increasing share of Australian Super funds flowing to the agriculture sector.

Consolidated Pastoral Company welcomes the opportunity to participate in this important debate.

Yours sincerely,

Troy Setter

Chief Executive Officer

Consolidated Pastoral Company

**Consolidated Pastoral Company (CPC)**

CPC is the leading private producer in the Australian beef industry.

Our 16 stations have a carrying capacity of 400,000 cattle and cover 5.5 million hectares.

The company's investment strategy is built around positioning our business to capture a share of the growing demand for protein in the Asian region.

Since CPC was purchased by Terra Firma, a UK based Private Equity Fund, in 2009 the company has focused on reducing the age profile of our herd, increasing turnoff, introducing cattle segregation on breeder blocks and holding sustainable stocking levels to create better market opportunities.

We have also been building our relationships with key customers such as Indonesia, export and domestic processors, domestic retailers and feedlotters, and strengthening our input over key supply chains.

The key components of the strategy are focused on improving the quality of CPC's assets, building and retaining a skilled and experienced workforce and growing a genetically robust herd.

Importantly, everyone at CPC is continually working to ensure the company's animal welfare standards are world's best practice.

**Summary**

Agriculture is a major contributor to the Australian economy.

Agricultural commodities are worth over $60 billion annually and over 60 percent of that production is exported.

To realise its full potential, the sector will need access to substantial amounts of capital.

A potential source of funds is $2.6 trillion held by the Australian Superannuation industry on behalf of its members.

However, many funds choose not to invest in agriculture, many are not maximising returns for their members or contributing to national wealth generation through strategic investments because their decisions are not fully informed.

This inquiry, coupled with the Productivity Commission inquiry into the Superannuation industry, presents an opportunity to address both the lack of capital available to agriculture, the suboptimal performance of sections of the super industry and the relationship between the two sectors.

Barriers to a productive alliance between agriculture and the Super Funds include:

- A complex foreign investment regulatory regime;
- A lack of detailed knowledge of the sector by fund trustees, executives and asset managers;
- A lack of investable agricultural products;
- A lack of performance data for the sector through time;
- Difficulty in achieving investment scale and operational size for 'corporate' farms;

- Investment returns varying considerably between agriculture industries;
- Capital appreciation being a material component of overall returns in agriculture; and
- Illiquidity of agricultural investments.

These barriers may be addressed through:

- A closer alignment between the investment strategies of both sectors; and
- A better alignment between the regulatory system that governs Australian superannuation and the policy and regulatory framework that overlays agriculture.

The terms of Reference

On Thursday, 24 May 2018, the Treasurer, Hon Scott Morrison MP, asked the Committee to inquire into and report on superannuation fund investment in agriculture.

Specifically, the Treasurer asked the Committee to report on the following matters:

- Whether there are any regulatory requirements imposed on superannuation funds by ASIC, APRA and any other relevant regulators, which are acting as a barrier to superannuation fund investment in Australian agriculture;
- The information required by the superannuation funds in order to invest in Australian agriculture is readily available, and if not, what statistical performance reporting of the agricultural sector is necessary; and
- There are any other practical barriers to superannuation fund investment in Australian agriculture.

**Overview**

To respond properly to the Treasurer's terms of reference CPC proposes that the Committee consider the following four matters:

- Agriculture and its investment strategy;
- Government policy and the agriculture sector;
- The investment principles and strategies that underpin the super industry, and
- Government policy and the superannuation industry.

The closer the alignment between the investment strategies for superannuation and agriculture and the policy framework that overlays both sectors the greater the return to the agriculture sector, members of superannuation funds, the economy and our standard of living from a national savings pool with a current value of $2.6 trillion.

## Australian Agriculture

Agriculture is a key sector of the Australian economy.

According to the Australian Bureau of Agricultural and Resource Economics and Sciences (ABARES) Agricultural Commodities for the June Quarter 2018 the value of farm production will be around $61 billion in 2018/19.

ABARES expects export earnings for farm commodities to be $47 billion in 2018-19, down 2 per cent from $48 billion in 2017-18.

The gross value of cattle and calf production is $12.7 billion and the value of Australian beef exports is above $7 billion.

The Australian herd currently numbers some 25 million head and the area covered by pastoral leases is around 338 million hectares.

The industry employs around 200,000 people (including processing) and produces around 2 million tonnes of beef and veal.

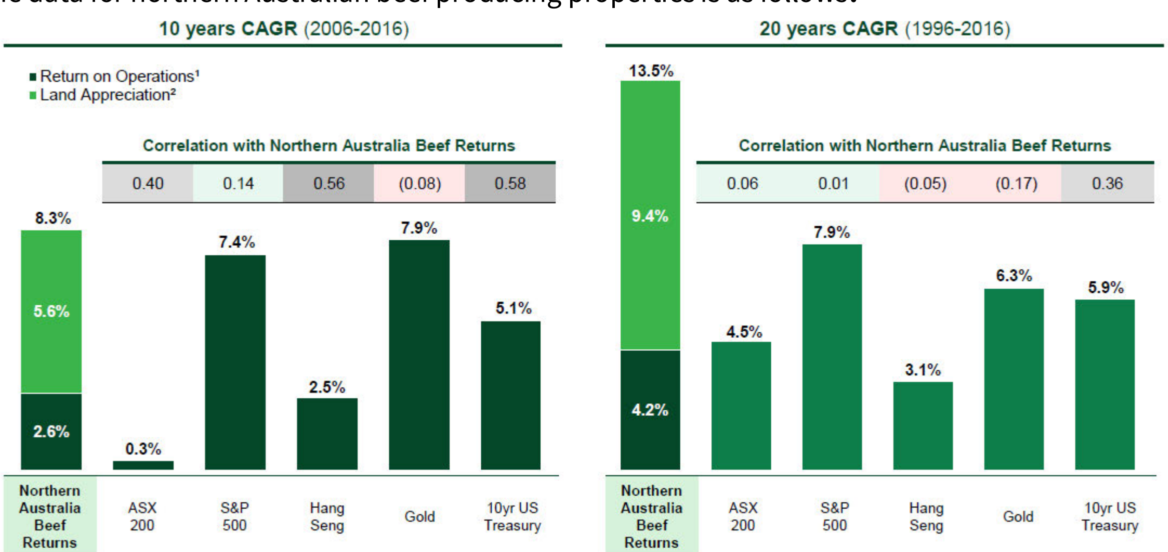
## Investing in Agriculture

CPC believes that Australian agriculture offers a great investment opportunity for Super Funds to earn strong financial returns for their members, contribute to the economic development of regional Australia and, importantly, strengthen the nation's food security.

Agricultural returns

CPC notes data from Bloomberg and Meat and Livestock Australia that suggests total returns from agricultural properties have outperformed all other asset classes and show favourably low correlation with other asset classes.

The data for northern Australian beef producing properties is as follows**:**




*Source: Bloomberg, MLA. All data calendarised to a Jun-YE.*
*Note: Northern Australia is defined as a subset of regions (MLA definition) comprising properties in QLD, NT and the Kimberley and Pilbara region of WA.*
*[1] Return on operations defined as average financial rate of return across sample (northern Australian beef producing properties with >5,400 head of cattle), excluding land capital appreciation. This is representative of the returns from the herd. [2] Land appreciation defined as average across sample (northern Australian beef producing properties with >5,400 head of cattle).*

As shown above a significant component of the returns to Australian agriculture is capital growth. This partly reflects productivity gains and the development undertaken.

CPC also notes a key challenge for Australian agriculture is the variability of returns.

In that context it should be noted:

- Australia does not enjoy the government support for farmers that exists in the United States of America and the European Union;
- Australia is a country with one of the most variable rainfalls in the world; and
- with the majority of production exported is subject to the variability of international markets.

Industry diversification

CPC notes the transformation of Australian agriculture from the traditional primary industries such as wheat, beef, sheep and wool into increasingly sophisticated farming practices including more intensive production techniques and marketing.

CPC also notes the increasing sophistication of intensive industries such as chicken meat production.

This shift in agriculture to elaborate food production demands more investment in technology and therefore more capital but also offers more attractive investment options.

For example, beef production is not only a major agricultural industry in Queensland generating thousands of jobs and focused on investing in enhanced technology along the supply chain red meat processing is now the biggest manufacturing industry in the state.

Meeting growing demand

CPC is of the view that Australian agriculture generally, and the beef industry, have a key role to play in sustaining economic growth in this country and meeting the growing global demand for protein.

CPC notes the BDO paper - An analysis: Australian superannuation fund investment in agriculture 2014/15 - (Australian superannuation fund investment in agriculture 2014/15
27 April 2015 BDO Australia) (The BDO paper) states:

"Australia's agriculture sector has an incredibly important role to play in the continued growth and success of our economy."

The BDO paper states:

...between now and 2050, the world's population is expected to increase from about 7 billion people to almost 9.3 billion people, an increase of around 35 percent.

The net effect, as forecasted by the Food and Agricultural Organisation (FAO), is that agricultural production in 2050 needs to increase by around 70 percent.

The BDO paper predicts that Australia could more than double the real value of annual agricultural exports by 2050 to capture an additional A$710 billion in revenues.

**Government policy and the Agriculture sector**

The Agricultural Competitiveness White Paper

The Agricultural Competitiveness White Paper represents the most recent articulation of the Government's policy framework for the agriculture sector.

In the White Paper the Government states that it is committed to strengthening the sector and ensuring it remains as competitive as possible, "because stronger farmers mean a stronger Australian economy."

It states:

"Our vision is to build a more profitable, more resilient and more sustainable agriculture sector to help drive a stronger Australian economy."

In the Paper the Government identified five priorities:

- Strengthening the Australian Competition and Consumer Commission and cutting red tape;
- Investing in infrastructure through a $500 million National Water Infrastructure Fund and roll out the $50 billion infrastructure fund;
- Strengthening the approach to in-drought support and risk management;
- Farming smarter by investing in RD&E, improved skills, better labour reliability and improved emergency pest and disease control; and
- Improved access to premium markets.

In relation to the Government's commitment to cut red tape CPC welcomed the reference given to the Productivity Commission and the report that followed.

The Commission produced a detailed work program.

CPC also welcomed the appointment of Dr Wendy Craik to undertake independent review of the interaction between environmental law and the agriculture sector building on the Commission's work.

Consideration should be given to a similar approach to other sectors covered by the Commission's report such as transport, biosecurity and animal welfare.

**See attachment A**

Access to capital

A key to Australian agriculture realising it potential is access to capital.

Research undertaken on behalf of the ANZ Bank estimates that there is a capital investment requirement for agriculture in Australia between now and 2050 of $600 billion to enable production growth.

To attract the required capital, the agricultural sector must be able to attract funds from the massive pool of domestic funds held by the Superannuation industry on behalf of its members.

Agriculture must also be competitive in the international capital market if it is to attract the necessary financial support.

Foreign investment rules

As access to capital is fundamental to building a robust and competitive agriculture sector any policy that hinders the flow of capital, whether domestic or foreign, may put at risk the Government's broader policy framework.

It is not only CPC's view but also CPCs' experience that the complexities and inconsistencies in the current foreign investment regime have the potential to stifle foreign investment in Australian agriculture and damage the Government's broader policy agenda.

Secondly, reforming the domestic regulatory environment has limited value if the foreign investment regulatory regime is complex and deters potential investors.

Thirdly, a complex and inconsistent foreign investment regime can also deter domestic institutional investors who are concerned the regime will limit the size of the market when they wish to exit.

**The Superannuation sector**

CPC notes the draft Productivity Commission Report, Competition in the Australian Financial System, (Superannuation: Assessing Efficiency and Competitiveness, Productivity Commission Draft Report April 2018) (PC report) released last month.

The PC report said with super being compulsory for most workers and with nearly 15 million members collectively owning over $2.6 trillion in assets.

The Commission noted as the super system is both complex and compulsory the Government has a role in regulating the system so that people can trust it with a significant portion of their savings.

The PC report states that an efficient super system would offer members a range of products and services suited to their needs and would ensure members could readily access good quality information to inform their decisions.

It states there has been a proliferation of little used and complex products — over 40,000 in total — which complicates decision making and increases fees without boosting net returns.

CPC also notes the BDO Paper reference to 271 superannuation entities with four or more members as at 30 June 2013.

At that time these entities offered 25,838 investment options. BDO found that at the upper extreme, one entity offered 2,899 investment options.

This complexity must also impact of the ability of Super Funds to understand let alone properly analysis all investment options on offer.

The Commission's draft report makes the following key points:

- Australia's super system needs to adapt to better meet the needs of a modern workforce and a growing pool of retirees.
- Currently, structural flaws — unintended multiple accounts and entrenched underperformers — harm a significant number of members, and regressively so.
- Fixing these twin problems could benefit members to the tune of $3.9 billion each year.

While the PC inquiry is focused of the performance of funds in relation to their members it also provides the Government, the parliament and other stakeholders with the opportunity strengthen Super Funds role in growing the Australian economy generally and agriculture in particular.

**Superannuation Funds and Agriculture**

CPC notes that a number of barriers stand between the Super Funds and the agriculture sector.

Some of these barriers are identified in the BDO Paper and by Industry Super Australia in Discussion Paper: Driving Super Fund Investment in Agriculture, published in July 2017.

(Driving super fund investment in Australian agriculture Discussion Paper 34 www.industrysuperaustralia.com) (ISA paper)

<u>The BDO paper</u>

The BDO paper cites a number of factors that may impact on the viability of agriculture assets as potential superannuation fund investment options.

The BDO paper states barriers are:

- Assets consultants generally not focusing on agriculture;
- A lack of investable agricultural products;
- The lack of asset managers specialising in agriculture;
- Rates of return, the cost of investment and volatility; and
- Illiquidity of agricultural investments.

The BDO paper rightly concludes that Australia, with a strong competitive advantage in agriculture, has a role to play in global agricultural investment portfolios.

The ISA paper also identifies a number of issues its argued discouraged investment by the superannuation sector,

They are:

- General farming conditions in Australia are tougher and less predictable that other major agricultural producing countries;
- Our soil is less fertile;
- Funds trustees and their asset advisers cannot readily identify the top quintile of producers in terms of their risk-return profile;

- The structure of farm industries is typically fragmented; and
- Institutional investors in Australia have tended to adopt a very hands-on, direct approach to farm investing when it would be better for them to partner with experienced operators.

**See attachment B**

CPC notes that the ISA paper proposes a number of policies to promote institutional investment:

- Establishing performance benchmarks for commodity producers;
- Infrastructure supply chain audits;
- Agricultural industry policy focused on price transparency;
- Promote the development of international linkages for Australian businesses;
- Adopting a more strategic approach to foreign investment; and
- Establishing a Rural and Regional Development bank.

**See attachment C**

CPC supports the following proposals as worthy of further consideration by the Committee;

- Better benchmarking of agricultural production to underpin a broader strategy to attract more capital to the sector;
- Infrastructure supply chain audits to better inform investment decisions;
- A broad industry policy framework that focuses on lowering production costs and opening market opportunities;
- Tax policies that recognise the variability of earnings in Australian agriculture being available for all investors; and
- Tax policies to encourage people to live and work in regional Australia.

CPC does not support any further restriction on the flow of foreign capital into agriculture, price controls or the establishment of a new Government owned bank.

**Proposed Actions**

It is CPC's view that Australian agriculture is well placed to enjoy sustained growth for decades if the sector adopts the right investment strategies, the super industry builds the capacity to manage agricultural investments and government builds an appropriate policy framework.

<u>Proposed industry actions</u>

Clearly, a key to Australian agriculture realising its potential is access to capital.

To attract the required capital, the agricultural sector must be able to attract funds from the massive pool of domestic funds held by the Superannuation industry.

Agriculture must also be competitive in the international capital market if it is to attract the necessary financial support.

To be competitive in the capital markets the sector must be competitive in the domestic and global commodity markets.

That requires the industry to invest in:

- On farm infrastructure;
- Skilling its labour force;
- Improving its production performance, for example, through better animal genetics;
- Employ world's best practice animal welfare and environmental management standards; and
- Educate both domestic and international capital markets about its business.

Proposed actions by government

It also requires government policy settings that;

- Drive down regulatory costs;
- Improve transport systems through strategic infrastructure investment;
- Properly regulate markets;
- Open international trading opportunities; and
- Work with the agriculture sector, the superannuation industry and government financial regulators to make agriculture's performance more transparent and easier to measure.

Proposed actions by Super Funds

CPC finds it difficult to understand why there is little detailed knowledge of a multibillion dollar sector of the Australian economy within the Australian Superannuation industry.

Particularly given agriculture is thirsty for capital, and enjoys an international comparative advantage.

CPC believes it would be in the commercial interest of the Super Funds to remedy that weakness as a matter of priority.

The industry should also look to engage asset managers with a good, long term record in the sector.

Finally, the Super Fund sector should engage with the relevant government agencies to address the lack of performance data.

**Attachment A**

**The Agricultural Development White Paper**

**Priorities**

The White Paper, released on 4 July 2015, sets out the Australian Government's roadmap of practical actions to grow our agriculture sector because stronger farmers mean a stronger economy.

In the Paper the Government identified five priorities:

**1. A fairer go for farm businesses**

Helping farmers achieve a better return at the farm gate and ensuring fairer competition for farm produce through a strengthened ACCC.

- Reducing red tape;
- Streamlining agricultural and veterinary chemicals approvals;
- A Productivity Commission review into reducing regulation for the Australian agriculture;
- A better tax system for farm businesses;
- Opt back into income tax averaging after 10 years;
- Double the Farm Management Deposits (FMD's) to $800,000;
- Banks can allow farmers to use FMDs as a loan offset, reducing interest costs; and
- Accelerated depreciation for fencing has been simplified.

**2. Building the infrastructure of the 21st century**

- $500 million National Water Infrastructure Fund for farmers' future water security;
- Applying CSIRO's TRAnsport Network Strategic Investment Tool (TRANSIT) to support future decisions on transport infrastructure investment to benefit agriculture;
- Investing $50 billion for current and future infrastructure; and
- The $29.5 billion National Broadband Network (NBN) rollout.

**3. Strengthening our approach to drought and risk management**

- Preparing for drought;
- $3.3 million to give farmers more accurate, more local and more frequent seasonal forecasts;
- Immediate tax deduction of the cost of new water facilities for farmers;
- Depreciation of capital expenditure on fodder storage assets over three years;
- $29.9 million over four years for farm insurance advice and risk assessment grants to help farmers evaluate options.

In-drought support:

- Up to $250 million in Drought Concessional Loans each year for 11 years;
- $22.8 million to increase Farm Household Allowance case management for farmers;
- Increased financial counselling services and improved access to community mental health;
- Additional advice and help from the Australian Taxation Office;

- $35 million for local infrastructure projects to help communities suffering due to drought; and
- $25.8 million over four years to manage pest animals and weeds in drought-affected areas.

**4. Farming smarter**

- $100 million extension of the Rural R&D for Profit Programme to 2021–22 to get research onto the farm;
- New RD&E priorities to direct levy funds to areas that will improve farm gate returns;
- $50 million to boost Australia's emergency pest and disease eradication capability; and
- $50 million to give farmers better tools and control methods against pest animals and weeds.

Help farmers access skilled and reliable labour by:

- Focusing on better training through the $664.1 million Industry Skills Fund;
- Making visa programs more flexible by expanding the Seasonal Worker Program Australia-wide, and the Working Holiday Maker (417 and 462) visas in northern Australia;
- Establishing a new Ministerial Advisory Council on Skilled Migration to review the list of occupations available for sponsorship under the 457 visa;
- Supporting farmers and other land managers to tackle practical environmental projects.

**5. Accessing premium markets**

- $30.8 million to break down technical barriers to trade and appointing five new Agriculture Counsellors;
- $200 million to improve biosecurity surveillance and analysis nationally, including in northern Australia;
- $12.4 million to modernise Australia's food export traceability systems to further enhance our food safety credentials.

**Attachment B**

The Industry Super Australia Discussion Paper: Driving Super Fund Investment in Agriculture, published in July 2017.

(Driving super fund investment in Australian agriculture Discussion Paper 34 www.industrysuperaustralia.com)

This paper identified a number of issues that discouraged investment by the superannuation sector:

1. General farming conditions in Australia are tougher and less predictable, relative to North America and some other global locales, and so farm businesses are riskier. Land fertility is more variable in Australia when compared to the United States, driven in large part by climatic conditions (frost, drought, flooding and cyclones) but also the prevalence of pests, disease, fires etc. United States producers can also access government subsidies and farm income insurance. Of course, these differences should be reflected in lower Australian land values relative to the United States which should help equate risk adjusted returns.

2. Funds trustees and their asset advisers cannot readily identify the top quintile of producers in terms of their risk-return profile. Indeed, most have little understanding of the sector at all. It doesn’t help that there are just no statistically meaningful and independent data series publicly available that allow experts to compare the performance of agricultural and other investments on a like-for-like basis.

3. The structure of farm industries is typically fragmented, with the clear majority of farm businesses held in either small 'family sized' blocks or locked away in private hands. Typical family holdings are small or debt laden and so cannot achieve significant expansion without the assistance of patient equity partners. Raising farm productivity and returns demands aggregation, innovation and/or the deployment of further capital, along with securing water rights where possible.

4. Institutional investors in Australia have tended to adopt a very hands-on, direct approach to farm investing. This has inherent agency and execution risks. It is also very difficult for institutional investors to time property purchases so they can achieve the necessary scale (by commodity and across regions) required by diversification models. As such it may be better for superannuation funds to partner with experienced family or corporate operators with established track records running successful operations.

5. Australian agricultural policy since the mid to late 1980s has handed the relatively small local food and grocery markets to monopolists and foreign investors. Once producers faced ‘more or less’ competitive wholesale markets - or were subject to pragmatic domestic and international marketing arrangements.

**Attachment C**

Industry Super Australia Discussion Paper: Driving Super Fund Investment in Agriculture, published in July 2017

(Driving super fund investment in Australian agriculture Discussion Paper 34 www.industrysuperaustralia.com)

The Paper proposes "the federal government could move agricultural policy settings onto a more competitive basis for domestic producers" to facilitate greater agriculture investment by Australian and global institutional investors.

The policies include:

- Establishing a statistically robust survey of farm performance to independently measure rates of return across various crop and livestock producers building upon the existing ABARES farm survey.
  - Over time the survey would help investors to allocate capital to highest value uses and so help raise productivity and probably rates of return in the sector. The survey could be funded by industry levies.
- Undertaking an infrastructure audit of each of the major commodity supply chains to ensure the adequacy and competitive operation of transport, processing and storage facilities across regions to ensure high quality produce can get to local and export markets in a timely and cost-effective fashion.
- Establishing appropriate regulatory arrangements to help achieve effective price discovery and transparency in wholesale agricultural markets.
  - For example, it may be desirable to compel large producers to sell their produce into centralised markets and or via other marketing arrangements, on a no disadvantage basis.
  - The idea is to help neutralise the impact of duopsony buyers (Coles and Woolworths) in local markets and the distortionary impact of subsidies on the prices received by growers in international markets. It would be useful to have the Australian Competition and Consumer Commission (ACCC) investigate these issues.
- Employing targeted industry and trade policies to incentivise domestic operators to form consortia with local and foreign processors and distribution networks to reduce offtake (agricultural sales) risk.
- Requiring a more strategic approach to foreign investment from the Commonwealth Treasury to ensure core assets are not being dealt away to foreign investors.
  - This entails more effective monitoring, oversight, public reporting and evaluation of foreign investment in agricultural land holdings, farm businesses and agribusiness.
- Establishing a rural and regional development bank to provide advisory services to rural producers and arrange long term finance to more efficiently intensify their operations, extending on the concept of a publicly owned and operated rural investment corporation, announced as part of the 2017-18 Budget.

- A development bank may be a means of delivering government support for fencing, irrigation, renewables, etc. while acting as a counterweight to the Big Four Banks' market influence and short-term perspective.
- A panel of suitably qualified independent experts would assess the proposal's feasibility which, ideally, would operate independently of executive government (to avoid politicisation) and mainly draw on institutional funds.