



**Submission to Senate Rural and Regional Affairs and
Transport References Committee
Inquiry into the Ownership Arrangements of Grain
Handling**

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NSW Farmers' Association Background

The NSW Farmers' Association (the Association) is Australia's largest State farmer organisation representing the interests of its farmer members – ranging from broad acre, Livestock, wool and grain producers, to more specialised producers in the horticulture, dairy, egg, poultry, pork, oyster and goat industries.



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1 Introduction

NSW Farmers directly represents the interests of farming businesses in NSW, with members from the broadacre cropping, mixed farming, meat, wool and dairy commodities, as well as more specialised producers in horticulture, egg, pork, oyster and goat commodities. Our policy is established by grass roots members and their representatives with specialist advice from standing committees and professional staff.

NSW Farmers appreciates the opportunity to provide the Senate Rural and Regional Affairs and Transport References Committee with a submission in response to its inquiry into the ownership arrangements of grain handling.

In considering the terms of reference of the inquiry, NSW Farmers has focused on the proposed change in ownership of GrainCorp that has arisen as a result of the takeover bid by giant American agribusiness Archer Daniels Midland (ADM). NSW Farmers has formally adopted the position that it does not believe that the proposed sale is in the National Interest and therefore that the Treasurer should not approve the takeover.

If the Treasurer is to approve the takeover, NSW Farmers argues that appropriate conditions should be applied to the sale to ensure that operational decisions made by a new controlling entity of GrainCorp is not contrary to the national interest with respect to maintaining and growing competition in the market for farmers' grain.

a. Process of Reviewing the National Interest

Upon the announcement that as a result of due diligence ADM would continue with its proposed takeover bid for GrainCorp, NSW Farmers wrote to the Federal Treasurer requesting he direct the Foreign Investment Review Board (FIRB) to undertake formal public consultation on the sale as an exercise of ministerial discretion. While FIRB will make available an audience with impacted stakeholders at the request of those stakeholders, the only consultation that it initiates under 'Australia's Foreign Investment Policy' is with agencies of the Commonwealth or State and Territory Governments.

In contrast, the approach proposed by NSW Farmers would provide greater transparency to the process undertaken by the Government when considering whether the proposed purchase is in the national interest. It would also engage the public to assist the Government in the consideration of what are the appropriate conditions that may be placed on such a sale to ensure that it is not in breach of the public interest.

2 GrainCorp

GrainCorp is a vertically integrated agribusiness focused on grain commodities. Its business model has developed as a result of its ownership of the major infrastructure servicing the grain supply chain in eastern Australia. This infrastructure was developed as part of a monopoly supplier of grain handling and storage as part of the policies of successive state governments during the era in which the marketing of grains was heavily regulated. It is the view of NSW Farmers that the operation of this monopoly infrastructure in the eastern Australian grains supply chain, and more specifically in NSW, already acts to distort the market for farmers' grain.

GrainCorp's business model focuses its operations on its:

- Grain storage and handling network operating across eastern Australia. GrainCorp reports that it handles 75 percent of all grain grown in eastern NSW and 90 percent of bulk grain exports. The network comprises of:
 - Over 280 grain receival sites. 70 of these sites are high capacity sites on branch lines or major rail lines. In NSW GrainCorp operates 90 percent (160 plus) of the upcountry receival facilities.



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- The operation of up to 24 trains with an annual capacity of 6 million tonnes. GrainCorp is the primary operator upon NSW's Country Rail Network.
- Seven of the eight bulk grain export grain elevators in eastern Australia.
- Grain marketing operations. GrainCorp directly markets approximately 35 percent of eastern Australia's exported grain and 25 percent of that used domestically. It is also increasing its grain marketing presence in South Australia and Western Australia.
- Grain processing operations in flour milling, malting and oilseed processing.

3 Terms of Reference (a), (b) and (c)

NSW Farmers has sought to address the terms of reference (a), (b) and (c) below. The submission has been structured this way because NSW Farmers has formed that view that the impacts of the present grain supply chain in eastern Australia and the availability of stocks information (and any changes that may arise due to the change in ownership of GrainCorp) upon grain traders and farmers are inter-related.

a. Impact upon competition for farmers' grain

In seeking to ensure that the grain market operates efficiently to the benefit of farmers, NSW Farmers policy is focused on how to remedy the impacts of GrainCorp's monopoly infrastructure upon the market's ability to capture and distribute value. In implementing this policy, NSW Farmers has called for arrangements within the supply chain to facilitate the opportunity for all traders to bid for farmers' grain in the execution of accumulation plans to fill domestic and export contracts. This is through ensuring:

- that all traders receive non-discriminatory access to up country receival and storage and port terminal facilities;
- competitive logistical services between the site of grain accumulation and where the contract executes, be that at export port or domestic end user; and
- the disclosure of grain stocks information, including volume and quality of grain, such disclosure will facilitate the efficient price discovery in the trading of grain in the futures, cash and pools markets.

If implemented properly, these positions enable grain producers to be able to choose more profitable sales options, particularly the timing of sales for grades in short supply and traders will have better control of the risk they face in the development and execution of grain accumulation strategies. With less risk and strong competition better prices will be offered for farmers' grain.

The major barrier to such a competitive market within the operation of the grain supply chain, that NSW Farmers has identified, is the incentive that exists for bulk handling companies to undertake self preferential treatment towards their related grain marketing entities.

(i) Incentives for self preferential behaviour

To assist the Committee's consideration of the impact of the proposed acquisition of GrainCorp by ADM, NSW Farmers recommends that care is taken to consider the impact of the interrelated nature of GrainCorp storage and logistics operations with its grain marketing operations on competition for farmers' grain. Of major concern to NSW Farmers is the ability of GrainCorp to use its dominant market position in the provision of port terminal services and up country storage and handling to the interest of its grain trading entity; and conversely the detriment of other grain marketers and traders.



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While it is acknowledged that a countervailing incentive to optimise throughput of GrainCorp's storage and logistics assets exists; this is not exclusive to behaviour that can impede competition for farmers' grain by increasing the costs of competitors. As part of a previous inquiry, the Committee has received evidence regarding a range of behaviour that integrated bulk handling companies, such as GrainCorp, may undertake that reduce competition in the market. The undertaking of these types of behaviour would not preclude a bulk handling company from optimising its asset utilisation.¹

Specifically the Committee quoted the following types of behaviour:

- Charging a higher fee for deliveries to port from an upcountry storage not belonging to the port storage owner;
- Charging growers an extra fee for direct delivery to port.
- Using information systems to the benefit of their trading arm;
- Locking up rail capacity on over-burdened lines, requiring competitors to use road, usually at a higher cost;
- Leaning on port authorities to make it hard for competitors to find suitable alternative arrangements. This occurs as a result of the port authority not wanting to upset a major customer, and deals on volume;
- Reducing competition by keeping up-country fees lower, but then overcharging where they have the monopoly at the port; and
- Offering a rebate of about \$2/T to buyers who allow the handler to ship from any site rather than the grain specifically bought by the buyer.
- Booking out sections of the shipping stem.

NSW Farmers also believe that the following behaviour are also examples of an exercise of monopoly market power:

- Scheduling maintenance and fumigation to suit their sales and marketing requirements.
- Warehousing contract terms which limit the remedies available to grain farmers under the Personal Property Security Register.

As a result of the evidence before it at that time the Committee found, subject to regional variations, that there are 'monopolistic tendencies' displayed in the behaviour of the major bulk handling companies within their regions.²

In considering the above factors, NSW Farmers is concerned that the integration of this monopoly infrastructure with ADM's substantially stronger balance sheet and its international trading division will increase the incentive to maximise preferential behaviour towards its own trading and marketing operations. The likelihood of this outcome would, in the view of NSW Farmers, be to the detriment of deeper competition within the market.

(ii) Measuring Impact on Competition

NSW Farmers has provided a submission to the ACCC as part of its informal review of the proposed purchase of GrainCorp by ADM. As part of these submissions the question of what behaviour is likely to result in a substantial lessening of competition, in accordance with section 50 of the *Competition and Consumer Act 2010* was considered.

¹ Senate Rural and Regional Affairs and Transport Committee, Parliament of Australia, *Inquiry into operational issues in export grain networks* (2012) 26-28.

² Ibid 28.



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In developing its position, NSW Farmers reviewed the explanatory memorandum accompanying the Trade Practices Legislation Amendment Act 1992, which defines the test on whether the acquisition results in substantially lessening of competition as being:

[A]n effect on competition which is real or of substance, not one which must be large or weighty.³

The ACCC's Merger Guidelines further clarify that the test requires the lessening in competition to be 'not merely discernible but material in a relative sense and meaningful'.⁴

In considering what type of impact would be meaningful on competition within the market, NSW Farmers recommended to the ACCC that it should consider changes in the relative price passed onto by a bulk handling company to other traders (that is either through direct charges to competitors, or subsidised charges to related entities), even if only small on face value, to be meaningful in their impact. This is because of the nature of the margins that exist within the grain producing and trading segments of the supply chain.

Likewise behaviour that impedes the operations of competitors that drive up transaction costs and the need for risk premiums should also be considered anti-competitive.

With regard to the consideration of whether the proposed sale of GrainCorp to ADM is in the national interest, NSW Farmers argues that the Australian Government, through FIRB and ultimately the Treasurer, should not confine its consideration to short term impacts upon competition. Rather with a growth in competition essential to grasping the opportunities provided by growing food demand in Asia, it should also consider whether the purchase is likely to have a detrimental impact on growing competition within the grain supply chain.⁵

In reviewing the competition in the market for port loading services in eastern Australia, deficiencies in the competition regulator's powers have been identified. At the time that GrainCorp, and its predecessors in Queensland and Victoria, acquired its port terminal facilities they were confronted with an industry dominated by the market power of the Australian Wheat Board as the principle user of its port terminal services. However since the deregulation of the single desk marketing arrangements, the market power of GrainCorp as a port terminal service provider has been maintained, while the users of its port services have become a diverse group dominated by GrainCorp itself. The *Consumer and Competition Act 2010* does not explicitly allow the ACCC to consider such changes when considering the takeover of GrainCorp by ADM. NSW Farmers is unsure if the ADM ownership interests will allow the ACCC to review competition for infrastructure more generally, and as a result are required to rely upon the review of the acquisition by FIRB to balance any deficiencies of the ACCC's powers in this instance.

b. Upcountry Grain Facilities

In NSW the up-country grain receival networks available for the delivery of grain from farmers, either off the header or from on-farm storage are as follows:

- GrainCorp – 160 (dispersed across regional NSW)
- AWB GrainFlow – 10 (plus Talwood which receives some grain from northern NSW)

³ Explanatory Memorandum, Trade Practices Legislation Amendment Bill 1992 [12].

⁴ Australian Competition and Consumer Commission, 'Merger Guidelines' (November 2008, updated 2011) [3.5].

⁵ See Port Jackson Partners 'Greener Pastures: The Global Soft Commodity Opportunity for Australia and New Zealand' (ANZ insights issue 3, Australia New Zealand Banking Group Ltd, October 2012) 38, 48.



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- Australian Bulk Alliance – 6 (mainly in the south of regional NSW)

Despite what may appear to be an abundant provision of upcountry receival and storage sites across NSW, NSW Farmers agrees with the assessment of Malcolm Bartholomaeus (Senior Commodity Analyst for NZX and Editor of Profarmer Grain), that this does not ultimately translate to choice for growers and competition in the sector. Rather, 'most growers will find that one [receival site] is really only available from a freight cost point of view'.⁶

Much has been made about the utilisation of closed loop marketing by ADM's grain origination network globally. This is a practice by which ADM does not allow third parties to post prices and warehouse grain at its receival and storage facilities. ADM has made public the view that it is in its best interests to optimise the throughput of grain in GrainCorp's upcountry receival and storage network. However, the strong balance sheet position of ADM and the needs of its integrated marketing may lead to circumstances in which profit maximising by ADM may mean that the optimising the use of its assets may not be the same as maximising their use.

(i) Integration with ADM's international marketing network

For example, where grain with specific characteristics may only be sourced in specific localities, it may be profit maximising behaviour for ADM to not enable third parties to access a receival site in that region in the execution of their accumulation plans. Instances where this may arise could be where ADM's established international marketing network has identified a niche international market. Alternatively it may arise as a result of ADM's need to fill existing contracts with grain of a specification, where an alternative international origin has failed.

For example when Russia banned grain exports in 2010, ADM reported a reduction in the operating profit of its agricultural services division as a result.⁷ The ban, which came as a result of weather related crop failure, led to grain traders seeking alternative sources to fulfil their trading requirements.⁸ In its first quarter 2013 Earnings Conference Call, ADM included the diversification of its crop supply as being an example of how the purchase fits within its core model and strategy.⁹

If in utilising the acquisition of GrainCorp to meet such a need, ADM closed specific sites to competitors, it is likely to result in a lessening of competition for grain farmers within that region due to the freight cost advantage that the site provides to GrainCorp.

(ii) Impact of ADM's balance sheet position

In its submission to the Senate Inquiry into the Wheat Export Marketing Bill 2012, GrainCorp submitted that one of the key impediments to it engaging in self preferential treatment was its lack of ability to:

⁶ Malcolm Bartholomaeus, Submission No 21 to Senate Rural and Regional Affairs and Transport References Committee, Parliament of Australia, *Inquiry into Operational issues in export grain networks*, 30 August 2011, 2.

⁷ Archer Daniels Midland Company, 'ADM reports first-quarter earnings of \$ 345 million' (News Release, 2 November 2010) 3
<<http://www.adm.com/lists/pressrelease/attachments/269/Q111%20earnings%20release.pdf>>.

⁸ See Jacqut Fatka 'Russia bans grain exports' *Feedstuffs* 9 August 2010, 1; and Jacob Gronholt-Pedersen 'Russia's grain export ban begins' *Wall Street Journal* (Brussels) 16 August 2010, 3.

⁹ Archer Daniels Midland Company 'First Quarter 2013 Earnings Conference Call' (Presentation, 1 May 2013) 16 <<http://origin.adm.com/en-US/investors/Documents/2%20ADM%201Q13%20Conf%20Call%20with%20GNC.pdf>>.



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purchase all of the grain received and handled within the company’s network, nor willing to assume the risk associated with owning or trading this quantity of grain; ...¹⁰

In further articulating this argument GrainCorp also pointed to the countervailing market power held by international agribusinesses that are engaged within the grain supply chain. The example provided by GrainCorp in the table below included a listing of ADM as the third largest global agribusiness with net assets of A\$18 billion.

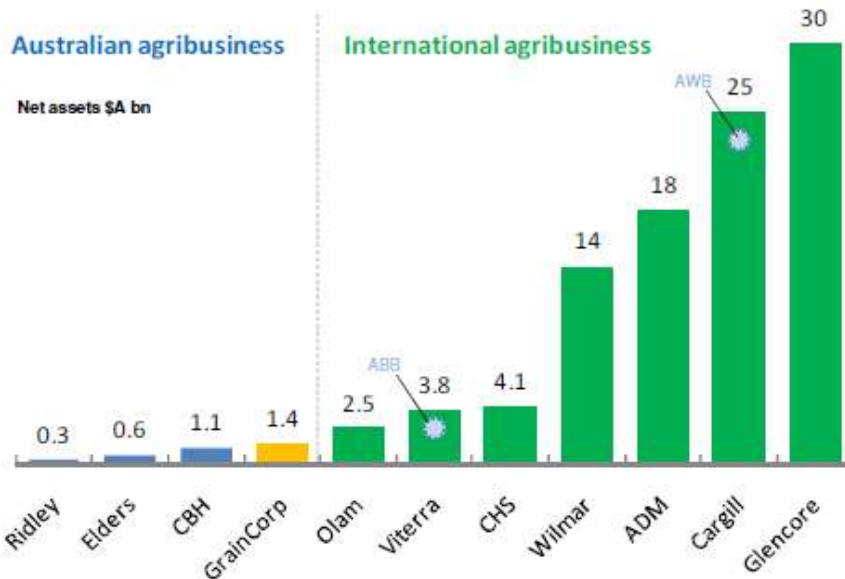


Figure 1 International Agribusinesses by net assets¹¹

NSW Farmers does not accept the argument from GrainCorp that the operation of its monopoly infrastructure has not impacted on the competition for farmers’ grain. Notwithstanding this, the implication of this specific argument by GrainCorp is that competition from better resourced participants within the market prevents such self preferential dealing. However a logical inference that may be drawn from this argument is that if GrainCorp had access to a stronger balance sheet and international marketing networks the impact of this countervailing influence is lessened. In the view of NSW Farmers this is what the acquisition of GrainCorp by ADM will achieve. On this basis the conditions that NSW Farmers recommend to be applied to the sale are required to ensure that the merged entity will not adversely impact upon competition, and the development of further competition, for farmers’ grain.

c. Port Terminal Grain Facilities

With approximately 80 percent of Australia’s grain sold to export,¹² the international market for grain underpins the floor price in Australia. As such access to reliable port terminal services on fair and transparent terms to grain traders who are not bulk handlers is crucial for maintaining and growing competition within the market for farmers’ grain.

¹⁰ GrainCorp, Submission No. 10 to Senate Rural and Regional Affairs and Transport Legislation Committee, Parliament of Australia, *Inquiry into the Wheat Export Marketing Amendment Act 2012*, April 2012, 11.

¹¹ Ibid 14. Note ADM net assets reported in its half yearly reporting (March 2013) was US \$19.1 billion. At the time of reporting this net value was equated to A\$18.3 billion

¹² See Australian Bureau of Agricultural and Resource Economics and Science *Australian Crop Report* series.



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At the time that the single desk export marketing arrangements for wheat were abolished, the importance of export bulk grain elevators on upstream competition was acknowledged by the Parliament. This can be seen in the Minister's contribution to the second reading debate:

So we have decided to impose specific requirements on accredited exporters that operate bulk grain terminals at ports, as these are the facilities with natural monopoly characteristics and are the infrastructure bottleneck in the export supply chain.

Unless all exporters can obtain access to these critical facilities on fair and reasonable terms then one of the major objectives of the policy could be frustrated.¹³

More recently the Government's Wheat Export Marketing Amendment Bill 2012 sought to replace the requirement for exporters operating port terminal facilities to have access undertakings with the ACCC with a non-regulatory voluntary code of conduct. The abandonment of this requirement without appropriate compulsion to remain a party to, nor to comply, with such a code, concerned NSW Farmers. As a result of the Parliamentary process, appropriate amendments requiring the development of a mandatory code of practice for port access were incorporated into the Bill.

Further, during the Parliamentary debate over the amendments inserting the requirement for a mandatory code, the Minister made representation to the Australian Greens that the code would include the requirement to report wheat stocks information to the market.¹⁴ Specifically the Minister outlined in this correspondence that he agreed that the Code will require the disclosure of this information by port zone, by grade, weekly during harvest and monthly outside of the harvest period. Alternatively the Minister agreed to require this information by other means 'if the port access code proves to [be] [sic] an unworkable vehicle'.¹⁵

(i) Code of Conduct for Port Access

The position of NSW Farmers during the above debate was that an evolution of the regulation of export grain terminals would strike the balance between the needs for protecting existing competition and fostering future investment and competition. This evolution would include a focus on the impact of the upstream market on competition for slots at port elevators. The practical measure of providing the market place with valuable information on warehoused grain stocks formed a key plank in this position.¹⁶

The Government commissioned report, '*Information requirements for an effective bulk wheat export market*', stated that the provision of this information will lead to better competition between grain trading entities regardless of whether they are an entity related to a bulk handling and storage operator. This is through enabling all 'industry participants to 'start on a level playing field' in developing pricing and accumulation strategies'.¹⁷

¹³ Australian Parliament, *Parliamentary Debates*, House of Representatives, 29 May 2008, 3857 (Tony Burke, Minister for Agriculture Fisheries and Forestry).

¹⁴ Australian Parliament, *Parliamentary Debates*, Senate, 29 November 2012, 10270, (Christine Milne; Joe Ludwig, Minister for Agriculture Fisheries and Forestry).

¹⁵ Letter from Senator the Hon Joe Ludwig to Senator Christine Milne, 27 November 2012.

¹⁶ In considering what valuable information on grain stocks would be, NSW Farmers believes that this should include volumes of the grain in question by the segregation grade. This should be weekly during the harvest period, and monthly at other times and should be reported at a minimum at the port zone region.

¹⁷ Peter Reading (2012) 'Information requirements for an effective bulk wheat export market' (Report commissioned by the Department of Agriculture, Fisheries and Forestry, Australian Government, May 2012) 29 <
http://www.daff.gov.au/__data/assets/pdf_file/0011/2157770/information-req-for-an-effective-bulk-wheat-export-market.pdf>.



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On this basis, NSW Farmers believes that it is appropriate to consider the current development of the mandatory code of conduct by the Australian Government, as required by the *Wheat Export Marketing Amendment Act 2012*, in any approval process for the sale. NSW Farmers has made submissions to the ACCC that if the provisions within the proposed code are not considered adequate, or alternatively not in a form at which the ACCC is able to make such a determination, that the ACCC should reserve any findings it makes within this review. In such a case it would also be appropriate for the ACCC to publicly state what the appropriate conditions within the code would be.

(ii) Port Terminals: Competition and Other Policy Objectives

In its recent report for ANZ, Port Jackson Partners identified the monopolised grain supply chain, which arose as a result of privatising government assets, as constraining the full potential of the grain sector and its affiliated industries up and down the supply chain.¹⁸ This has particular relevance in NSW where presently there are only two major grain elevator terminals in operation, both operated by GrainCorp.

In considering the impact of the lack of competition within the two NSW based port zones, NSW Farmers brings attention to GrainCorp's 2012/13 Port Elevator Fee Schedule Summary. This outlines GrainCorp's practice of charging an additional fee for road intake for NSW and Queensland, however not in Victoria where it faces more direct competition from the Port Melbourne facilities.

With this in mind, it is appropriate to consider whether greater diversity in the ownership of grain elevator capacity across eastern Australia is in the national interest, with port terminal facilities the gateway to the export of Australian produced and manufactured goods.

4 Term of Reference (d)

Conflict between interests of shareholders and the best interests of Australian producers and consumers

In the process of NSW Farmers' development of policy on the proposed sale of GrainCorp to ADM, one of the major concerns raised by members was ensuring adequate expenditure in maintaining existing assets in operable conditions; as well as investment to improve the network. While theoretically foreign direct investment may enable capitalisation required to undertake maintenance and investment in capital assets, it also pits expenditure and investment in Australian assets against that in other global regions. For example, while ADM has outlined a desire to maintain an Australian based management team for GrainCorp, the purchase would drastically reduce the proximity of those ultimately responsible for approving capital maintenance and expenditure plans to the Australian assets. This may result in sub-optimal investment.

5 Conclusion

NSW Farmers policy on the grain supply chain seeks to ensure that the grain market operates efficiently to the benefit of farmers. This focuses on how to remedy the market failure caused by the impact of GrainCorp's monopoly infrastructure upon the market's ability to capture and distribute value. In implementing this policy, NSW Farmers has called for arrangements within the supply chain to facilitate the opportunity for all traders

¹⁸ Port Jackson Partners 'Greener Pastures: The Global Soft Commodity Opportunity for Australia and New Zealand' (ANZ insights issue 3, Australia New Zealand Banking Group Ltd, October 2012) 48.



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to bid for farmers' grain in the execution of accumulation plans to fill domestic and export contracts.

NSW Farmers believes that the ownership of grain handling networks has a significant opportunity to influence the nature and magnitude of these networks upon competition for farmers' grain. This is because the financial resources and the commercial imperatives of larger international agribusinesses, such as ADM, reduce the 'countervailing influence' which has been pointed to in arguments against the case for market failure in the supply chain.

Further, NSW Farmers is concerned that reducing the proximity of the ultimate decision makers on capital maintenance and expenditure plans may result in lower appropriations targeted to improve GrainCorp's operations to improve the efficiencies of farmers and grain traders who hold grain at those sites.

For these reasons, NSW Farmers' does not believe that the sale of GrainCorp to ADM is in the national interest, and has called upon the Australian Government not to approve it. If however, the Australian Government was to approve the sale, NSW Farmers believes that specific conditions must be placed ADM requiring access provisions for up country and port assets, the ongoing disclosure of grain stocks on hand, and a capital expenditure plan.

NSW Farmers also believes that the Australian Government should consider requiring the divestment of some of GrainCorp's port terminal facilities to increase competition across eastern Australia in the provision of these services.