SUBMISSION

Senate Rural and Regional Affairs and Transport References Committee

OWNERSHIP ARRANGEMENTS OF GRAIN HANDLING

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1. EXECUTIVE SUMMARY

This submission comments on:

- Ownership structures in Australia's grain industry, including GrainCorp's current and historic ownership structure.
- The commercial imperatives that drive GrainCorp's approach to the operation of its supply chain assets, including up-country grain receival sites and its bulk grain export terminals.
- The ongoing industry discussion of the potential provision of additional stocks information.

Noting that GrainCorp is currently subject to a takeover offer from Archer Daniels Midland Company (ADM), GrainCorp is not able to comment on ADM's intended operating model for the business.

GrainCorp has operated as a public company since the NSW government's decision in the 1990s that its storage and ports assets would more productively owned and operated by the private sector.

Since its listing, the company has been able to access additional shareholder capital in a period marked by drought and other challenges to improve its operations; upgrade its assets; strengthen the supply chain and facilitate domestic and international growth. Over this period, many of the company's shareholders have been overseas institutions and, prior to ADM's interest in the company, foreign ownership of GrainCorp was approximately 30%.

GrainCorp does not accept the proposition that the interests of its shareholders and those of Australian growers or consumers are somehow mutually exclusive. Regardless of ownership structure, without Australian growers and the grain they produce, and without consumer demand for the products the company handles and processes, GrainCorp's business would not be able to generate a return for its owners.

The company's assets are expensive to operate and maintain. In addition to the substantial capital GrainCorp has invested to grow the business, it also invests $40-60 million each year in its assets and another $40 million annually in take-or-pay rail capacity. To get an adequate return on these significant investments, GrainCorp must act in a way to maximise the amount of grain passing through the network.

GrainCorp's country storage and receival network competes in an environment where there is substantial excess capacity – enough to hold the average winter harvest (17 million tonnes) approximately 2.3 times over.

There is also a large amount of excess capacity at GrainCorp's ports, with 15 million tonnes of annual elevation capacity comparing with an average export task of just over 5 million tonnes. Over the past 10 years, GrainCorp's ports have operated at an average 35% capacity. It would make no commercial sense for GrainCorp to reduce the utilisation of its ports further by restricting access to the ports to other grain exporters and third parties.

GrainCorp

2. ABOUT GRAINCORP

GrainCorp is an ASX100 listed agribusiness focused on efficiently connecting Australia's high quality grain growers with the businesses that process their grain and oilseeds into food and ingredients.

GrainCorp's business has been built around a network of grain storage and logistics assets in Queensland, NSW and Victoria. Across this footprint we operate up to 280 country receival sites. This network serves international buyers of Australian grain through seven bulk grain export terminals, in addition to a large number of domestic customers.

In recent years GrainCorp has built on this grain network of facilities to become an integrated and international leader in connecting the high quality grain grown in eastern Australia with food and ingredients processing:

- Our Marketing business is the largest exporter of grain from eastern Australia and has a global network trading to 25 different countries; and
- We have three downstream processing businesses:
  - Allied Mills is Australia's largest wheat flour miller for human consumption (which we own as a 60% joint venture partner with Cargill Australia holding 40%);
  - GrainCorp Malt is Australia's second largest barley malt business and the fourth largest in the world – with 18 plants servicing leading brewers and distilleries in Australia, Asia, Europe and North America; and
  - GrainCorp Oils is Australia's largest integrated edible oilseed crushing and refining business.

2.1 ARCHER DANIELS MIDLAND COMPANY (ADM) TAKEOVER BID

GrainCorp was informed on 18 October 2012 by ADM that it had acquired 15% interest in GNC through equity derivative contracts. On 22 October 2012 GrainCorp confirmed it had received an indicative, non-binding proposal from ADM to acquire the outstanding shares in GrainCorp at a price of $11.75 per share in cash.

On 15 November 2012 GrainCorp announced that the proposal materially undervalued the company. GrainCorp also announced it had a clear strategy for growth to deliver incremental growth in underlying EBITDA over the next four years.

This was followed by a revised, non-binding conditional proposal announced on 4 December 2012 at a price of $12.20 in cash. ADM informed GrainCorp it had received FIRB approval to acquire a further 5% interest in GrainCorp and that it had acquired this interest.

On 13 December 2012 GrainCorp announced that the revised proposal materially undervalued the company.

Following a period of negotiation, GrainCorp and ADM reached agreement on a further revised offer, where GrainCorp shareholders will receive payments of $13.20 per share in cash (inclusive of $1.00 per share in dividends) if the offer becomes unconditional.

The cash payments of $13.20 per share represent a significant premium to GrainCorp's recent trading prices, including:

- a 49% premium to the closing share price of $8.85 on 18 October 2012, being the last trading day prior to the announcement of ADM's initial takeover proposal;
- a 48% premium to the 1-month volume weighted average price to 18 October 2012 of $8.90; and
- a 44% premium to the 3-month volume weighted average price to 18 October 2012 of $9.14.

GrainCorp's Board carefully considered this third proposed offer from ADM and on 26 April 2013 GrainCorp announced it had entered into a Takeover Bid Implementation Deed, under which the GrainCorp Board would recommend that shareholders accept ADM's offer, subject to there being no superior proposal and it continuing to be in the best interests of shareholders; an independent expert determining that the offer is fair and reasonable; and certain regulatory conditions being satisfied or waived by 31 December 2013.

In reaching this position, GrainCorp's Board remained very conscious of its fiduciary duty to shareholders and obligations under Australian law, in particular the Corporations Act 2001.

GrainCorp does not accept the proposition that the interests of its shareholders and those of Australian growers or consumers are somehow mutually exclusive. Regardless of ownership structure, without Australian growers and the grain they produce, and without consumer demand for the products the company handles and processes, GrainCorp's business would not be able to generate a return for its owners.

2.2 CONTENT OF THIS SUBMISSION

This submission provides information on:

- Ownership structures in Australia's grain industry, including GrainCorp's current and historic ownership structure;
- The commercial imperatives that drive GrainCorp's approach to the operation of its up-country grain receival sites;
- The commercial imperatives that drive GrainCorp's approach to the operation of its bulk grain port export terminals; and
- The ongoing industry discussion of the potential provision of additional stocks information.

Noting that GrainCorp is currently subject to a takeover offer from ADM, the company is not able to comment on ADM's intended operating model for the business. ADM is best positioned to respond to questions relating to its intended operating model for the company.

3. GRAIN INDUSTRY OWNERSHIP STRUCTURES

Over the past 25 years the Australian grain industry has transitioned from a regulated structure, characterised by government-owned grain handling authorities and statutory marketing authorities; to a less regulated environment.

Today there are a number of business models successfully operating in the Australian grain handling sector, including publicly listed companies (such as GrainCorp); many privately held businesses operating in storage, transport and export; a major grower-owned co-operative and public and private foreign-domiciled companies.

Over this period international demand for grain and oilseeds has grown with the increase in population and wealth, particularly in Asia, the Middle East and North Africa. Combined with new grain varieties and improved farming practices, this has led to an underlying growth in Australian grain production. The industry's positive growth has been delivered in the face of one of the most devastating droughts of the past century.

Underlying increase in grain production and exports in eastern Australia is demonstrated by the following:

- Total grain exports have increased from an average of 6.5 million tonnes for the 10 years before 2008 to an average of 10 million tonnes per annum from 2008[1]; and
- In 2011-12, a record 14 million tonnes of grain was exported from eastern Australia by over 20 exporters to 52 countries.

3.1 GRAINCORP OWNERSHIP STRUCTURE

GrainCorp has changed substantially since its 1916 origin as a branch of the NSW Government's Department of Agriculture.

The business has operated as a public company since the early 1990s, when in 1992 the NSW government decided that the company's storage, handling and ports assets would more productively be owned and operated by the private sector. The NSW Grain Corporation was privatised in April 1992 and sold to the grain grower-owned Prime Wheat Association.

The Prime Wheat Association listed GrainCorp on the Australian Securities Exchange (ASX) in 1998. GrainCorp's public listing has allowed the company to access additional capital in a period marked by the most significant drought of the past century.

Since its listing in 1998, the company has issued around 200 million shares (around 90% of its current issued shares) to fund its growth, primarily through mergers and acquisitions as shown in Figure 1, to secure:

- Scale, so as to better manage variability that is inherent in agriculture; and
- Integration, so as to capture additional value along the grain supply chain.

[1] Attributable to a number of factors, including two large harvests following drought.

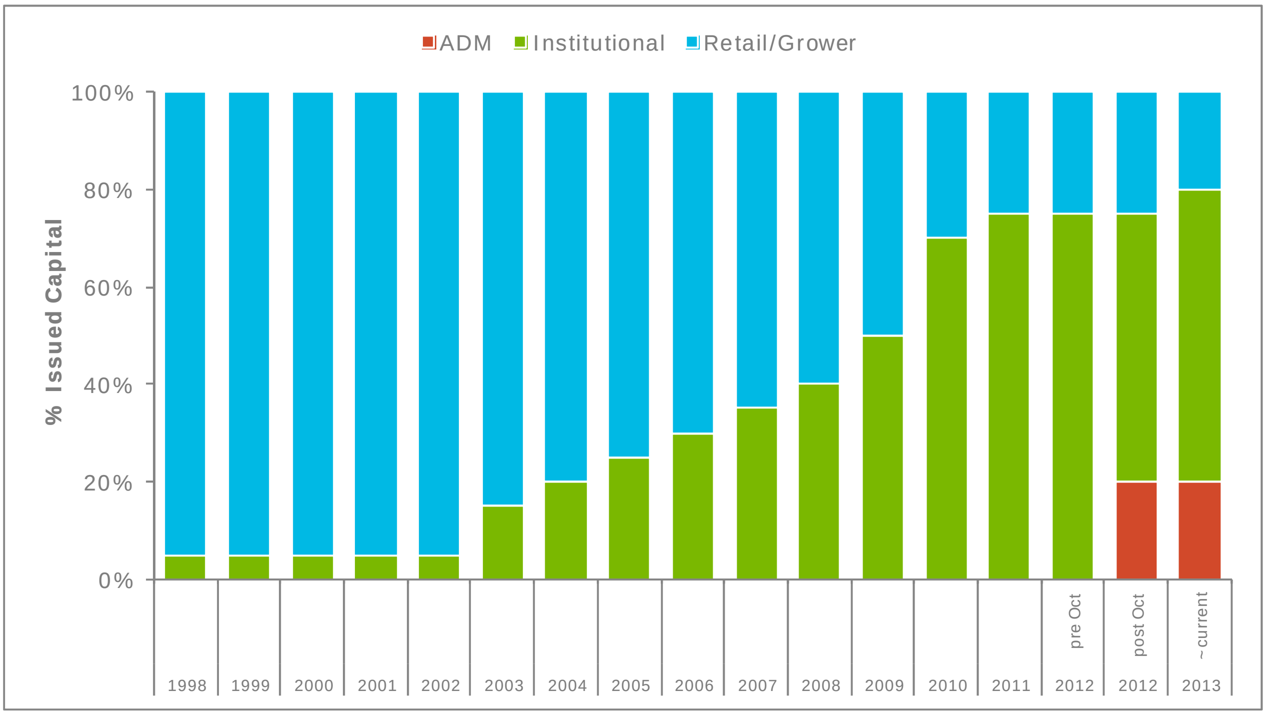
Figure 1: Key milestones in GrainCorp's growth

Year	Milestone
2000	Merger with Vicgrain (Victorian-based grain handler)
2002	Allied Mills joint venture with Cargill Australia acquired from Goodman Fielder (flour milling)
2003	Merger with Grainco (Queensland-based grain handler)
2009	International malt businesses acquired from United Malt Holdings
2011	Acquisition of Schill Malz (malt)
2012	Acquisition of Gardner Smith Group and acquisition of Integro Foods from Goodman Fielder (oilseed crushing and refining)

To fund this growth GrainCorp's has primarily sourced new capital from local and overseas institutional shareholders, away from its original retail/grower shareholder base, as shown in Figure 2.

GrainCorp has had overseas institutional shareholders on its register since 2000. The level of foreign ownership of GrainCorp prior to ADM's initial approach in October 2012 was estimated to be approximately 30%.

Figure 2: GrainCorp Register Composition[2]



[2] Ownership proportions used in Figure 2 are indicative, based on best estimate of register analysis.

4. COMPETITIVE PRESSURE IN SUPPLY CHAIN

GrainCorp's supply chain infrastructure and business is expensive to operate and maintain. In addition to the substantial capital GrainCorp has invested to grow the business and keep it competitive, it also invests $40-60 million each year to maintain its grain assets and business. To ensure an adequate return on this significant investment, GrainCorp must seek to maximise the utilisation of its grain network.

There is significant competition at every stage of the grain supply chain in eastern Australia. This competition provides a powerful commercial incentive for GrainCorp to operate its supply chain infrastructure in such a manner as to attract as much grain into its network as possible, thereby increasing the utilisation of its assets.

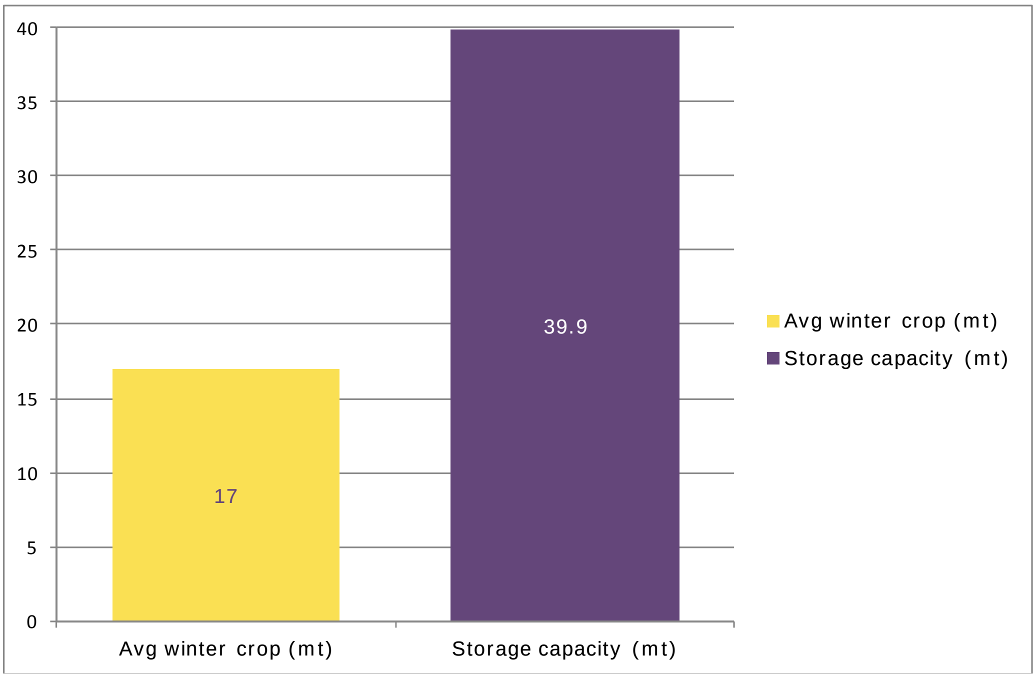
4.1 COUNTRY RECEIVAL SITES

GrainCorp's country storage and receival network competes in an environment where there is substantial excess capacity – enough to hold the average winter harvest (17 million tonnes) approximately 2.3 times over:

Figure 3: Grain Storage Capacity in Eastern Australia

Provider	Estimated storage capacity (tonnes)
GrainCorp	20 million
Other bulk handler (Cargill, Emerald, Viterra)	3.7 million
Merchant/end user	5 million
On-farm storage	11.2 million
TOTAL:	**39.9 million**

Figure 4: Grain Storage Capacity in Eastern Australia



In order to make a return on this substantial investment, GrainCorp has a strong commercial imperative to act in a manner to attract as much grain as possible into its silo and port network. This imperative has steadily increased as new capacity has been added by other industry participants, escalating the competitive pressure on GrainCorp.

Accordingly GrainCorp pioneered the principles of 'open access' to attract grain into its network from all grain participants, as demonstrated by the following:

- GrainCorp was the first bulk handler to introduce co-mingling rules for the common storage of grain for different customers in the same stack after the domestic grain market was deregulated in 1988. This allowed GrainCorp to provide growers with new marketing options for their grain.
- GrainCorp was the first bulk handler to introduce grower warehousing in its country storage network when the domestic grain market was deregulated in the early 1990s. This allowed grain growers to store their harvested grain in GrainCorp's network under their own name and have control when and who to sell their grain after harvest.
- In the early 1990s GrainCorp developed third party cash prices at its country receival sites, allowing the Australian Wheat Board and other grain buyers to post prices and bid for growers' grain at each of these locations.
- In 1996 GrainCorp was the first bulk handler to put in place an integrated grain business model by buying and selling grain at its silo network to service domestic consumers and then overseas consumers as the export of different grains was deregulated from 2000.

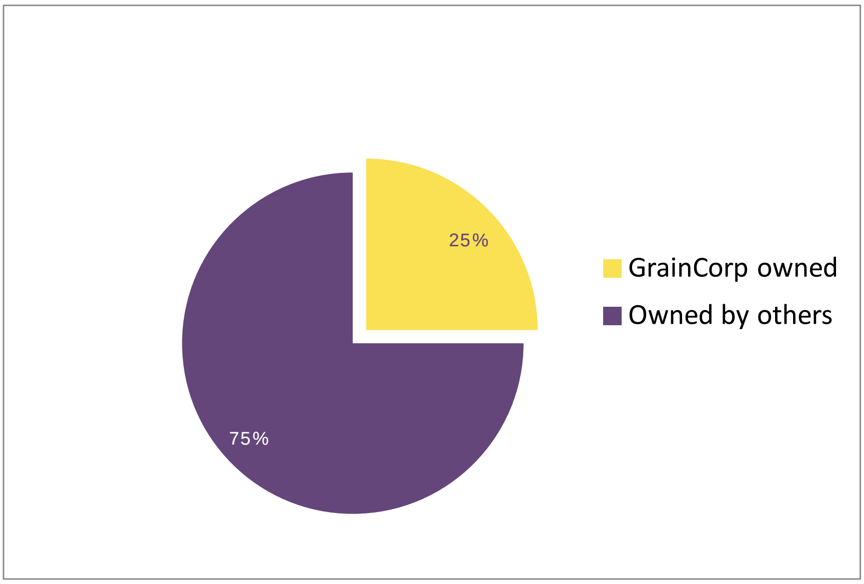
These innovations underpinned the current 'open access' grain business model in operation at GrainCorp's country network, where GrainCorp operates both as a storage agent for growers and other buyers and as grain principal for its own grain through the silo network.

The success of the 'open access' business model, and its importance in driving grain volumes through the company's silo and port network, is demonstrated by the following:

- Around 80% of grain delivered into GrainCorp sites is warehoused (stored) by growers, rather than being sold immediately off the header. This demonstrates growers are choosing to take advantage of the flexibility and the competition for their grain within GrainCorp's network. GrainCorp provides an on-line platform that allows growers to track grain prices, their grain stocks and quality held in warehousing and facilitates the sale of their grain to GrainCorp and other buyers.
- GrainCorp serves up to 100 grain buyers through its network, creating a competitive marketplace for growers' grain once it is delivered. The number of international grain companies posting prices at GrainCorp silos – and consequently the trading options for growers – increased significantly when the wheat export market was deregulated in 2008.
- The open and competitive nature of GrainCorp's network is demonstrated by the fact that GrainCorp accumulates approximately 25% of the grain in its network in its name, with the remainder held by other grain buyers (see Figure 5).

GrainCorp

Figure 5: Grain Ownership at GrainCorp Country Sites



4.2 ROAD / RAIL TRANSPORT

Once grain has been sold by the grower and is ready for transport to end-user, there are numerous transport options available to industry participants. GrainCorp offers road or rail transport as part of the services it provides to customers, but also offers them the flexibility of making these arrangements for themselves.

GrainCorp is committed to transporting as much of the export crop as possible by rail – however this task is proving increasingly challenging due to capacity constraints and the poor condition of many "grain only" rail lines. Nonetheless, GrainCorp's commitment to rail is demonstrated by the company's decision in 2008 to invest in long term "take or pay" rail contracts with rail operators, following the decision by these companies to withdraw from hauling grain.

Under these contracts, GrainCorp spends around $40 million annually, bearing the entire risk of a poor crop or crop failure, in order to provide growers and customers with certainty that rail capacity will be available. Similar to the investment in our up-country infrastructure, the substantial amount of money GrainCorp spends on rail each year means the company actively encourages customers to access its trains. Should a customer prefer to use their own train, GrainCorp sites also load trains provided by others.

Road transport also plays an increasingly critical role in the efficient transport of the eastern Australian harvest, particularly given capacity constraints on some parts of the rail network. A competitive road transport sector provides all grain industry participants with flexible and accessible means to transport grain to domestic destinations and to port.

4.3 PORT INFRASTRUCTURE

Similar to its country storage network, GrainCorp operates an 'open access' model at its port terminals.

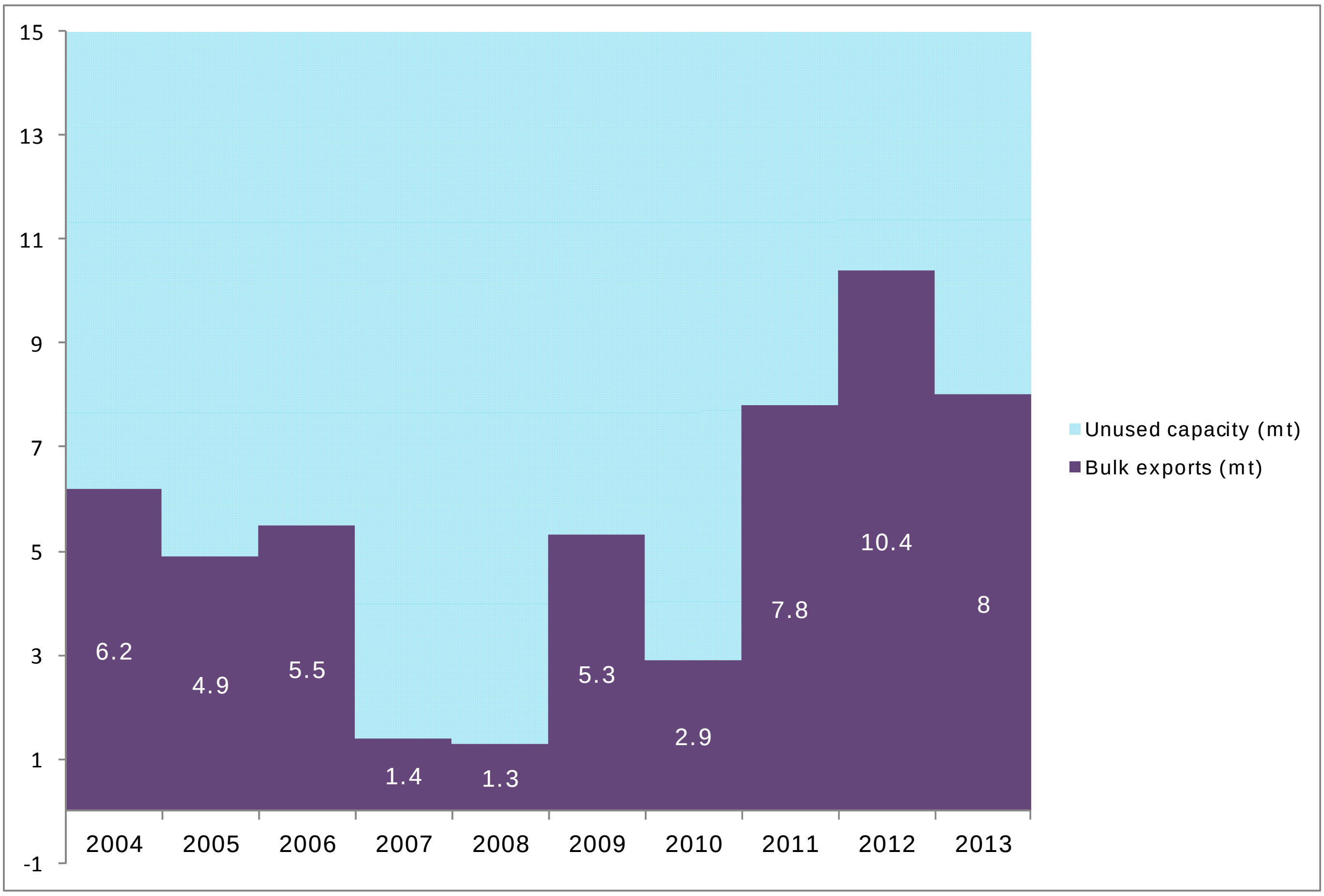
While access to third party wheat exporters is now required by government regulation, GrainCorp has consistently demonstrated it is prepared to provide open access to third party exporters without the need for cumbersome regulation that reduces port efficiency:

- Open access to Victorian ports was provided from 2000 to barley exporters when barley export market was deregulated.
- Open access to Queensland ports was progressively provided from 2003 as sorghum and barley exports were progressively deregulated from that state.
- Open access to NSW ports was provided for barley, canola and sorghum exporters from 2005.
- For the period from 2008 between the deregulation of bulk wheat exports and prior to the introduction of its Access Undertaking regime with the ACCC, GrainCorp offered open access to wheat exporters at all its ports.

This approach to port operation is driven by the substantial excess capacity at GrainCorp's ports.

GrainCorp operates seven bulk grain terminals in eastern Australia, with a combined elevation capacity of approximately 15 million tonnes per annum. Over the past 10 years, these terminals have operated at an average 35% capacity, as reflected in Figure 6.

Figure 6: GrainCorp Port Capacity Utilisation



To generate an acceptable return on its port assets, GrainCorp seeks to maximise their utilisation by elevating as much grain through them as efficiently as possible. It would make no commercial sense for GrainCorp to reduce the utilisation of its ports further by restricting access to the ports to other grain exporters and third parties.

The substantial (and growing) competition from alternate export pathways from eastern Australia provides an additional barrier to such uncommercial behaviour. These alternatives include:

- Bulk grain export terminals at Melbourne Port Terminal (owned by Emerald Grain which is 50% owned by Sumitomo), Newcastle (owned by Louis Dreyfus) and Brisbane (owned by Gavilon/Wilmar);
- A third additional bulk grain export terminal currently under construction at Newcastle port (Newcastle Agri Terminal) owned by Glencore, Olam and CBH;
- Approximately 50 country and city based packers that pack and export over 2 million tonnes per annum in containers.

5. STOCKS INFORMATION

The Committee will be aware of calls from some industry participants for the provision of additional information on grain stocks held up country.

GrainCorp is unsure of the precise market failure these calls are seeking to address, as there is strong price discovery in the eastern Australian grain market:

- On any given day there are a large number of buyers posting prices for grain in GrainCorp's network.
- Most grain offers are usually within a close range of $5/tonne. Grain prices closely benchmark to global grain markets, indicating strong price discovery.
- Pricing information is also available through CLEAR bids and offers, broker and market reports and ASX futures.

In addition, grain production forecasts by region are provided by regular government reports (ABARES) and regular private reports (Australian Crop Forecasters).

5.1 INFORMATION GENERATED BY GRAINCORP IS INCOMPLETE

GrainCorp does generate stock information from its up-country operations. However, the company has neither the incentive nor the ability to use this information to the disadvantage of other participants, because it is substantially incomplete:

- We have no visibility of the 40-50% of grain in eastern Australia that is stored outside GrainCorp's network;
- 80% of grain is acquired and sold by traders through private contracts where GrainCorp is not privy to the contracted price and terms;

- GrainCorp has no information on the trading position (long or short) of the other grain owners in our network;
- GrainCorp has no information on the destination of the grain until an outloading order is placed after it is sold; and
- Ownership information is generally out-of-date as stored grain is usually transferred up to two times, traded online and with no involvement of GrainCorp personnel.

GrainCorp notes there is an ongoing industry discussion relating to this issue and it is a particular focus of the Wheat Industry Advisory Taskforce. The company intends to participate in the Taskforce's process and remains open to a constructive discussion of workable and equitable solutions that:

- Have a clear market benefit to growers and industry participants, and
- Are applied equally to all participants in the grain industry.

5.2 INFORMATION ALREADY PROVIDED BY GRAINCORP

It is noted that GrainCorp already provides substantial stocks information to the market. This information includes:

- Weekly grain receivals by region, with commentary, during harvest;
- Posted cash prices at all GrainCorp silos, available on-line;
- Quality reports to owners of grain of the average grain quality at that site, by grade, pest control and other data to assist customers with their grain execution;
- Annual crop report on the eastern Australian harvest that provides buyers and growers information on grain properties, end use performance and major varieties included in grades;
- Daily shipping stem volumes by port and grain type and weekly disclosure of stocks at port; and
- Total grain metrics (from our investor publications).

In addition to this, market participants can offer grain production forecasts by region and aggregate demand for grain, provided by regular government reports (DAFF) and regular private reports on grain production, shipping and demand (Australian Crop Forecasters).

6. CONTACT INFORMATION

Requests for further information in relation to this submission should be directed to:

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