

**NATIONAL COMPETITION
POLICY REVIEW OF THE
*WHEAT MARKETING ACT 1989***

**Mr Malcolm Irving AM
Mr Jeff Arney
Professor Bob Lindner**

December 2000

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FOREWORD

This review of the *Wheat Marketing Act 1989* (the WMA) was conducted under the National Competition Policy (NCP), which was agreed to by all Australian Governments in 1995. Under this agreement, Australian governments are to review all legislation that affects competition, and to complete these reviews by the end of 2000.

On 4 April 2000 the Honourable Warren Truss MP, Federal Minister for Agriculture, Fisheries and Forestry, announced the NCP review of the WMA. When announcing the review, the Minister directed the Committee to focus on those parts of the legislation which restrict competition, and impose costs or confer benefits on businesses involved in the Australian wheat industry and the community generally.

The independent review Committee appointed by the Minister comprised Mr Malcolm Irving, Mr Jeff Arney and Professor Bob Lindner. The Minister directed the Committee to deliver their final report by 15 December 2000, which was extended to the end of December.

The Committee consulted widely throughout the review process. Stakeholders were given the opportunity to provide submissions, to consult privately with the Committee and to make their views known in open public forums. The Committee travelled to representative towns across the wheat belt in the five mainland States to consult at first hand. Many individuals travelled long distances and the Committee wishes to thank all those involved. Similarly, the Committee thanks all those involved in drafting submissions.

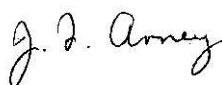
The Committee also commissioned technical assessments from the Allen Consulting Group, took advice from leading academics in Australia and overseas, and examined the public literature on wheat marketing and the NCP. In doing so it sought evidence on those effects of the WMA on competition able to be evaluated within an NCP framework. The Committee also visited a number of countries which either import Australian wheat, or compete with Australia in the international marketplace. These visits provided a valuable perspective on the Australian system and the Committee thanks all those who made their time available.

The Committee released the draft report on 13th October 2000 and received comments from stakeholders that proved invaluable in the formulation of this report.

The Committee would like to thank the Secretariat for their tireless support in the review process.



Mr Malcolm Irving AM
Chairman



Mr Jeff Arney
Member



Professor Bob Lindner
Member

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TERMS OF REFERENCE – REVIEW OF THE *WHEAT MARKETING ACT 1989*.

1. The *Wheat Marketing Act 1989* (the WMA), and associated regulations, are referred to an Independent Committee for evaluation and report by 15 December 2000. The Independent Committee is to focus on those parts of the legislation which restrict competition, and/or which impose costs and/or confer benefits on businesses involved in the Australian wheat industry and/or the community generally.
2. The Independent Committee is to report on the appropriate arrangements, if any, for regulation of wheat exports taking into account the following:
 - a) legislation and regulations which restrict competition should be retained only if the benefits to the community as a whole outweigh the costs; and if the objectives can only be achieved by restricting competition;
 - b) in assessing the benefits and costs in (a), regard should be had, where relevant, to ecologically sustainable development, welfare and equity, occupational health and safety, economic and regional development including employment and investment growth, and social issues, consumer interests, the competitiveness of Australian businesses including small business, and efficient resource allocation; and
 - c) compliance costs and the paper work burden on small business should be reduced where feasible.
3. In making assessments in relation to the matters in (2), the Independent Committee is to have regard to the analytical requirements for regulation assessment by the Commonwealth, including those set out in the Competition Principles Agreement.
4. The report of the Independent Committee should:
 - (a) identify the nature and magnitude of the economic, social, environmental or other issues the WMA seeks to address;
 - (b) assess the objectives of the WMA and the Wheat Export Authority arrangements, structure and functions;
 - (c) assess the effectiveness of the separation of regulatory and commercial functions in the WMA;
 - (d) identify whether, and to what extent the WMA restricts competition, including the appropriateness of granting a monopoly to a private company;
 - (e) identify any relevant possible alternatives to the wheat export arrangement in the WMA, including non-legislative approaches;

- (f) analyse and quantify the benefits, costs and overall effects on businesses involved in the Australian wheat industry and/or the community generally (the public benefits test), of the existing WMA arrangements; compared to the alternatives identified in (e) above; and identify the impact on different groups likely to be affected by either the continuation of the WMA arrangements or implementation of viable alternatives;
 - (g) determine a preferred option for regulation, if any, in light of objectives set out in (2) above;
 - (h) examine mechanisms for increasing the overall efficiency, including minimising the compliance costs and paper burden on small business, of both the WMA and, where it differs, the preferred option; and
 - (i) list the individuals and groups consulted during the review and outline their views, or reasons why consultation was inappropriate.
5. Part of the review will involve the Committee advertising in national and major rural media, consulting with key stakeholders, other affected parties and rural communities likely to be affected by any reforms, and publishing a report.
6. The Committee should also take into account it is the Government's intention to announce its responses to its recommendations. It will do this after obtaining advice from the Minister and if appropriate, after consideration by Cabinet.

EXECUTIVE SUMMARY

Under the National Competition Policy (NCP), Australian governments are reviewing and, where appropriate, reforming legislation that restricts competition. The NCP review of the *Wheat Marketing Act 1989* (the WMA), announced on 4 April 2000 by the Minister for Agriculture, Fisheries and Forestry, is part of this process.

The review was conducted by an independent Committee consisting of Mr Malcolm Irving (chair), Mr Jeff Arney and Professor Bob Lindner. The Committee's terms of reference included assessing whether the current legislation provides a net benefit to the Australian community compared with alternatives, and determining preferred options for regulation, if any.

The Committee received over 3,300 submissions from stakeholders, and also consulted widely both in Australia and overseas. The Committee then released a draft report outlining its preliminary views, and undertook a further round of domestic consultations. The Committee delivered its report to the Minister for Agriculture, Fisheries and Forestry on 22 December 2000.

The legislation

Australia is a major wheat exporter after the United States, Canada, and the European Union. Most of Australia's wheat is exported to countries in Asia, the Middle East, Africa, and Oceania. Australian wheat exports have increased in recent years following a number of large wheat crops in excess of 20 million tonnes.

Past legislation governing wheat marketing set out the regulatory and commercial functions, powers and objects of the former statutory Australian Wheat Board. This legislation covered both export and domestic wheat. The current legislation differs from past legislation in that it deals with the relationship between the Wheat Export Authority (WEA), the former statutory Australian Wheat Board's legal successor and organisation to which regulatory functions have been transferred, and AWB (International) Limited (AWBI), a wholly owned subsidiary of the grower owned organisation to which the Board's commercial objectives have been transferred. The current legislation also covers export wheat only.

The objectives of the current legislation are not explicitly stated in the WMA. The Committee considered that the lack of any explicitly stated objectives will make it unnecessarily difficult for any future industry group, forum or review working on wheat marketing arrangements to agree on a common reference point. For the purpose of this NCP review, the Committee took the view that the objectives could best be summarised as 'for the Australian Government to use its control of wheat exports to ensure direct grower access to marketing services and export markets, and to ensure that growers receive the highest net return from sales of wheat in export markets.' However, the Committee considered it would also be useful for the Government itself to explicitly state the objectives of the WMA.

Recommendation 1:

The Committee recommends that the WMA be amended so that the objective(s) of the legislation are stated explicitly, to provide a common reference point for future work on wheat marketing arrangements.
(Chapter 5)

In terms of how the WMA restricts competition, the Committee saw two primary effects. First, by restricting the entry of firms, the legislation gives one firm an effective monopoly on the export of bulk wheat. Second, by excluding choice, the legislation discriminates against various groups, including growers who do not, or do not wish to, market their wheat through the monopoly exporter. There are also flow-on effects on competition. Since export bulk wheat constitutes a significant proportion of the volume of grain produced and traded in Australia each year, the Committee considered that giving one firm an effective monopoly on the export of bulk wheat affords that firm a dominant position in Australian grain marketing. Using that dominant position, this firm may be able to influence domestic wheat prices and production, quality standards, the level of product promotion and innovation, the development of new markets, and markets for inputs, including marketing services, grain storage, handling and transport, plant breeding, and seed sales.

The Committee's terms of reference also require it to consider the appropriateness of granting a monopoly to a private company. The WMA grants a monopoly to the subsidiary of a private company (AWB Limited). This subsidiary, AWBI, is responsible for the wheat export pools and has an obligation under its constitution to maximise returns to growers who deliver to the pools. The Committee believes this arrangement raises a number of issues for the Government, as the owner of the export monopoly rights, and for wheat growers, as the main intended beneficiaries of the commercial exercise of these rights. Both these parties have an interest in ensuring that AWBI, as operator of the export monopoly, is being run commercially and at arm's length from the private company from which it is utilising staff, and purchasing services. The Committee makes the *observation* that the Service Level Agreement between AWB Limited and AWBI and the relevant constitutions should be clarified in consultation with WEA to ensure the definitions and operation of the Agreement and constitutions are clear and consistent with the objectives of the WMA.

The Committee believes both government and wheat growers may also wish to further explore some of the other issues raised by stakeholders in the context of the granting of a monopoly to a private company. The Committee also believes the current arrangements may have some implications for the Government's international trade negotiations under the World Trade Organisation (WTO) since, despite it being a private company, AWBI may fall within the definition of a 'State Trading Enterprise'. The Committee makes the *observation* that the Government may need to consider the implications of any change to the 'single desk' within the wider ambit of trade negotiations aimed at reducing agricultural support and protection.

The WMA also created the WEA, and set out two functions for it: to control the export of wheat from Australia, and to monitor the performance of AWBI and report on the benefits to growers from that performance. In its domestic consultations the

Committee heard frequent and severe criticism of the WEA's export consent system, variously characterised as being cumbersome, bureaucratic, time consuming, non-transparent, not adding value, and stifling innovation.

The Committee is of the view that the legislation has not achieved a clear separation of the regulatory and commercial functions of the statutory former Australian Wheat Board, and that the significant exceptions and overruling powers the legislation grants the nominated 'single desk' exporter effectively gives that exporter more control over exports than was actually envisaged when the legislation was originally framed. In addition, the current structure of the WEA board as set out in the legislation does not appear to sufficiently emphasise business skills, or grant the WEA sufficient independence to carry out its legislated functions.

Recommendation 2:

The Committee recommends that the WMA be amended to ensure that the WEA is totally independent in carrying out its functions, and recommends consideration of the following:

- **the system of administering non-AWBI exports of wheat be simplified; and**
- **board members be selected with an increased emphasis on business skills such as finance, marketing, and business management.**

(Chapter 6)

The Committee reviewed in detail many of the options for simplifying the system of administering non-AWBI exports of wheat. The Committee concluded that there are at least two possible solutions to the problem: one being to reduce the number of stages in the decision process, and the other to reduce the frequency with which decisions are required. The first could be realised by giving the WEA more autonomy to grant export consents by modifying or removing the requirement in the WMA for the WEA to consult with AWBI before granting applications for the export of wheat in containers or bags or to obtain written consent from AWBI before granting applications for the export of wheat in bulk. The second could be realised by the WEA replacing its current export consent system with an export control system where the exporter is licensed.

The Committee considered there to be many good reasons for working toward the first option (see Recommendation 7). However, because this option would require change to the legislation, in the Committee's view the second option, which could be taken up immediately without necessarily changing the legislation then continued if and when the legislation were changed, should be adopted as soon as practicable.

Recommendation 3:

The Committee recommends that the WEA introduce a simplified export control system for a three-year trial period where:

- **it issues annual licences on a fixed-fee basis to exporters who can demonstrate that they meet certain criteria including integrity, competency, financial standing, and a commitment to providing required information;**
- **such licences include appropriate penalties for non-compliance with the terms of the licence; and**
- **there is an appeal mechanism against rejection of a licence application, or the withdrawal of a previously approved licence.**

(Chapter 6)

The WMA also requires the WEA to conduct a review, before the end of 2004, of nominated company B's (that is, AWBI's) export operations, the conduct of nominated company B in relation to consultations for export consents, and the granting or withholding of approvals for export consents. Stakeholders provided the Committee with often conflicting suggestions as to the scope and process of the 2004 review. The Committee believes the scope and process of the review should be clarified as soon as possible, and that as part of the review there should be annual progress reports against performance criteria established by the WEA, in consultation with industry and government.

Recommendation 4:

The Committee recommends that:

- **the process of the 2004 review should be clarified within 90 days after the Government has announced its response to the NCP review's recommendations, and this process clearly communicated to the Minister and stakeholders, followed by annual progress reports as well as the final report as scheduled in 2004; and**
- **the review incorporates NCP principles in its assessments.**

(Chapter 6)

On the scope of the 2004 review, the Committee considered there was a need for a formal consultative process which would include all sections of the industry. During the domestic consultations a number of participants in the wheat industry identified to the Committee the need for an industry-government forum to bring key industry organisations together with government to discuss industry policy issues and processes. The Committee considered that relevant performance indicators for the 2004 review could be one of the issues to be addressed by such a forum.

Recommendation 5:

The Committee recommends that:

- **the Government convene a continuing joint industry-government forum to discuss industry policy issues and processes, including relevant performance indicators for the 2004 review, under the leadership of an independent chair; and**
- **this forum would be jointly funded by industry and Government, and would not exercise regulatory powers.**

(Chapter 6)

The ‘public benefit’ test

Under the guiding principle set out in the Government’s Competition Policy Agreements, legislation should not restrict competition unless it can be demonstrated that the benefits of the restriction to the community as a whole outweigh the costs, and the objectives of the legislation can only be achieved by restricting competition. The principle requires that net benefits be demonstrated relative to the situation likely to pertain in a fully competitive market. Furthermore, even if it can be reasonably established that such a net loss of community benefit would occur if the current legislation were removed, the principle also requires consideration of alternative ways of achieving the objectives of the legislation that are less restrictive of competition.

On the basis of the written submissions received as well as views expressed during domestic consultation, it was obvious that AWB Limited has very strong support from a majority of Australian wheat growers. Equally, the Committee received favourable comment during overseas consultations from an overwhelming majority of customers who were interviewed on the expertise of AWB Limited as an international marketer of bulk wheat. However, these views were not universal, as some stakeholders indicated that AWB Limited was not meeting their needs, and others that the WMA was not serving the best interests of growers.

In order to “analyse and quantify the benefits, costs and overall effects on businesses involved in the Australian wheat industry and/or the community generally (the public benefits test), of the existing WMA arrangements”, the Committee sought tangible evidence on the magnitude of such benefits, costs and overall effects.

The main arguments put to the Committee for not changing the current arrangements were that:

- some or all of the perceived export price premiums would be lost under a fully competitive system;
- economies of scale and scope would be lost;
- storage, handling and transport costs would be higher;
- domestic wheat users would lose from being more directly exposed to fluctuations in the world market; and
- there would be adverse social consequences.

Conversely, the main arguments for changing the current arrangements were that:

- storage, handling and transport costs would be lower;
- the price to users of domestic wheat would fall;
- the flow of information would improve, together with increased transparency and accountability;
- there would be increased innovation, flexibility and development of niche markets;
- financial management options such as price risk management would improve; and
- social effects may be positive if, for example, there were more than one marketer in a country town.

Regarding the public benefits test, the Committee was not presented with, nor could it find, clear, credible, and unambiguous evidence that the current arrangements for the marketing of export wheat are of net benefit to the Australian community. As the NCP guidelines place the burden of proving that the current system delivers demonstrable net benefits to the Australian community on those arguing for the retention of the legislation, this suggests that the WMA should now be modified, or repealed. However, two points need to be acknowledged.

The first is that the estimation of the impact of deregulation on net returns to wheat growers, as well as on net benefit to the broader community, is a complex and difficult exercise, and that actual outcomes cannot be predicted with certainty. On the 'single desk price premiums' claimed to be earned by AWBI under current arrangements, conflicting evidence was presented to the Committee. Despite some claims that substantial premiums are being earned, most of the evidence the Committee was able to obtain supported the view that, averaged across all markets, such price premiums were likely to be small.¹

At the same time, the Committee received convincing evidence that the current restrictions on competition have had an inhibiting effect on innovation in marketing, the identification of new marketing opportunities including small, niche, or specialised export markets, and ongoing development of existing markets for Australian wheat.

Furthermore, considerable evidence was provided that the 'single desk' has had an anti-competitive effect on the grain supply chain, constraining vertical integration and impeding the realisation of least cost grain paths and potential cost savings in grain receipt, storage, handling and transport. Again, though, various submissions made assertions that were conflicting. AWBI claim that economies of scale and scope provided by the 'single desk' enable it to negotiate with principal service providers to lower supply chain logistics costs and charges. Much of the evidence to the contrary was provided on a confidential basis by organisations directly involved in grain handling logistics.

¹ See chapter 7 for a discussion of premium estimates.

The Committee was also provided with compelling evidence from overseas that open competition in grain handling generated significantly greater cost savings than coordination by a dominant marketing organisation. In the case of Australia, it is difficult to quantify the level of foregone cost savings due to the WMA with any certainty, in part because grain handling and transport have until relatively recently been the responsibility of Statutory Authorities. Many constraints on achieving reform in this sector have now been removed, and some cost savings are almost inevitable irrespective of continuation of the ‘single desk’.

Because of uncertainty about the magnitude of these three key effects (‘single desk price premiums’, innovation in marketing, and grain supply chain costs), there also is some uncertainty about whether there are or are not net benefits to Australian wheat-growers and to the Australian community from the WMA. On balance the Committee came to the view that the introduction of more competition into export wheat marketing in the future would more likely deliver net benefits to growers and to the wider community than continuation of the current arrangements without modification.

The second point is that continuation of the ‘single desk’ for a further few years, in a slightly modified form, should provide much better evidence about the capacity of the current system to deliver significant and sustainable cost savings in the grain supply chain to wheat growers, as well as allowing more time to assess the ability of the ‘single desk’ to generate price premiums and further market development. Much of the data in this area related to sales by the former Australian Wheat Board. The Committee was conscious of the fact that considerable progress has been made in recent years toward putting export wheat marketing on a more commercial basis. Australia no longer has a statutory marketer for wheat exports, and Australian wheat growers receive negligible government support. Hence, while the Committee believes that the introduction of more competition would most likely deliver additional net benefits to growers and the wider community, it does acknowledge the possibility that the new more commercial arrangements for wheat marketing might achieve more clearly demonstrable net benefits than was evident during this review. Partly for this reason, and partly because of residual uncertainty about whether the WMA does or does not pass the net public benefits test, the Committee believes that it would be premature to recommend the repeal of WMA prior to a further relatively short evaluation period.

Nevertheless, the Committee is of the view that some change should be introduced during this period, but in a controlled way that does not jeopardise what has already been achieved to date. The recommended changes outlined below should allow the industry to tap into the wealth of innovative and entrepreneurial drive that has been unleashed in other areas of grain marketing, as well as to introduce a limited degree of competitive pressure for AWB Limited and other organisations in supply chain logistics.

Recommendation 6:

The Committee recommends that the ‘single desk’ be retained until the scheduled review in 2004 by the Wheat Export Authority (WEA) of AWBI’s operation of the ‘single desk’. However, the main purpose and implementation of this scheduled review should be changed so that it provides one final opportunity for a compelling case to be compiled that the ‘single desk’ delivers a net benefit to the Australian community. In particular:

- **the WEA review would allow further information to be gathered about the level of ‘single desk price premiums’ and about the ability of AWBI to achieve significant and sustainable cost savings in the supply chain for the benefit of growers; and**
- **if no compelling case can be made by the time of the 2004 review that there is a net public benefit, then the ‘single desk’ should be discontinued; but**
- **if a compelling case can be made by the time of the 2004 review that there is a net public benefit, then the ‘single desk’ should continue with ongoing regular WEA reviews of AWBI’s performance in managing the ‘single desk’, and if necessary, a further NCP review in 2010.**

(Chapter 7)

The Committee believes that ongoing innovation and exploration in the development of new markets for Australian wheat is essential for the continuing prosperity of Australian agriculture. It believes that multiple sellers may be better able to service many small, specialised or niche markets than a single seller could, and is of the view that the legislation should be amended to remove the current impediments to competition on the export of wheat in bags and containers. With the exception of exports to Japan, the Committee believes that the freight rate differential between bulk exports and exports in containers and bags provides a high degree of protection to bulk exports by AWBI. Therefore, changes to open up the export of wheat in containers and bags to all markets except those with minimal freight rate differentiation should facilitate highly desirable innovation in the discovery, development and expansion of markets for wheat exports while maintaining the protected position of AWBI.

Recommendation 7:

The Committee recommends that the WMA be amended to suspend Section 57 (3A) (which requires the WEA to consult with nominated company B (AWBI) before giving consent to applications to export in containers and bags) to enable a three-year trial of more competitive arrangements for the export of wheat in containers and bags to all markets except those markets where there is minimal freight rate differential between containers and bags, and bulk wheat.

(Chapter 8)

The Committee also received convincing evidence that the current restrictions on competition have had an inhibiting effect on further market penetration and growth in new markets for wheat. The Committee considered a number of options for changes which would open up new markets to greater competition, while maintaining the protected position of AWBI in its traditional bulk wheat export markets. The Committee examined arguments for the opening up of designated ‘non-core’ markets (that is, markets in which it can be unambiguously demonstrated that AWBI can not, and has no potential to, obtain a ‘single desk price premium’) to competition, but considered there would be a number of problems with implementation at this stage, including unambiguously identifying such markets, and ensuring that wheat exported to these markets was not redirected to ‘core’ markets. Similarly, the Committee received suggestions that the export of wheat in bulk to Papua New Guinea (PNG) and New Zealand (NZ) should be opened up to competition, on the argument that for the Australian milling industry, these two markets effectively represent an extension of the Australian domestic market. While the Committee has sympathy for the stakeholders who raised these issues, it concluded that satisfying their aspirations was incompatible with retention of the ‘single desk’.

The Committee also examined arguments by stakeholders for the opening up of markets for ‘specialty’ wheats, such as noodle wheat, soft wheat and durum wheat, to competition. In the case of noodle wheat and soft wheat, the Committee believes there would be a number of problems with implementation at this stage, the main one being to ensure separability from other wheats. In the case of durum wheat, however, the Committee believes separability can be achieved. Durum wheat has a distinctly different end use from bread wheat. The principal market for Australian (durum) wheat is in the Mediterranean region, where Australia has a freight disadvantage vis-à-vis many other exporters. In addition, the Committee has been unable to find any evidence of ‘single desk price premiums’ for durum. The Committee believes the trial opening to competition of the durum market would also create an observable, alternative set of arrangements for the bulk export of wheat. The Committee notes correspondence from AWBI advising it that AWBI may not run export pools for durum during such a trial. The Committee believes that whether or not to run such pools is a matter of commercial judgement for AWBI.

Recommendation 8:

The Committee recommends that the WMA be amended to suspend, for durum wheat only, Section 57 (3B) (which requires the WEA to obtain prior approval in written form from nominated company B (AWBI) before giving consent to applications to export bulk wheat), and Section 84 (1) (which states that nominated company B (AWBI) must purchase all wheat that is offered to the company for inclusion in a pool), to enable a three-year trial of more competitive arrangements for the export of durum wheat.

(Chapter 8)

Concluding remarks

Although there is uncertainty about the magnitude of ‘single desk price premiums’, the inhibiting effect on market development, and supply chain cost savings, and consequently on whether there are or are not net benefits to Australian wheat-growers from the WMA, on balance the Committee has come to the view that the introduction of more competition into export wheat marketing in the future would deliver greater net benefits to growers and to the wider community than a continuation of the current arrangements.

Overall, the Committee believes that adoption of the above recommendations would better achieve the objectives of the National Competition Policy.

1. INTRODUCTION

Under the National Competition Policy (NCP), Australian governments are reviewing and, where appropriate, reforming legislation that restricts competition. The *Wheat Marketing Act 1989* (the WMA) was listed on the Commonwealth's schedule for review commencing in 1999-2000.

The NCP review of the WMA was announced on 4 April 2000 by the Honourable Warren Truss MP, Federal Minister for Agriculture, Fisheries and Forestry. The review was conducted by an independent Committee following NCP review guidelines. The Committee's final report was to be delivered to the Minister by 15 December 2000, which was extended to the end of December.

Key sections in chapter:

- Terms of reference
- Structure of the report

1.1. Terms of reference

The terms of reference cover six areas:

- review timetable and focus;
- appropriate future arrangements for the regulation of wheat exports;
- requirements for assessment of regulation by the Commonwealth;
- required material to be included in the Committee's report;
- consultation with stakeholders and publishing a report, and
- delivery of the report.

1.1.1. Review timetable and focus

'1. The *Wheat Marketing Act 1989* (the WMA), and associated regulations, are referred to an Independent Committee for evaluation and report by 15 December 2000. The Independent Committee is to focus on those parts of the legislation which restrict competition, and/or which impose costs and/or confer benefits on businesses involved in the Australian wheat industry and/or the community generally'.

Under the Competition Policy Agreements, all Australian Governments have undertaken to review all legislation within their particular jurisdiction which restricts competition. Any restriction implicitly alters the matrix of community costs and benefits and notionally results in net welfare losses. Thus the terms of reference direct the Committee to focus on those sections of the WMA which may restrict competition and affect businesses involved in the Australian wheat industry and the community in general. These businesses can include wheat producers, wheat users, service providers and input suppliers.

1.1.2. Appropriate future arrangements for the regulation of wheat exports

‘2. The Independent Committee is to report on the appropriate arrangements, if any, for regulation of wheat exports taking into account the following:

- a) legislation and regulations which restrict competition should be retained only if the benefits to the community as a whole outweigh the costs; and if the objectives can only be achieved by restricting competition;
- b) in assessing the benefits and costs in (a), regard should be had, where relevant, to ecologically sustainable development, welfare and equity, occupational health and safety, economic and regional development including employment and investment growth, and social issues, consumer interests, the competitiveness of Australian businesses including small business, and efficient resource allocation; and
- c) compliance costs and the paper work burden on small businesses should be reduced where feasible’.

The guiding principle set out in the Competition Policy Agreements is that legislation (including Acts, enactments, Ordinances or regulations) should not restrict competition unless it can be demonstrated that the benefits of the restriction to the community as a whole outweigh the costs, and the objectives of the legislation can only be achieved by restricting competition. Legislation which is found to restrict competition is to be reformed, unless benefit can be demonstrated. Additionally, any new legislation that restricts competition is to be accompanied by evidence that it is consistent with the guiding principle.

The “Guidelines for NCP Legislation Reviews” prepared for the National Competition Council indicates the conditional statements in the guiding principle form a sequential test (CIE 1999). If it cannot be demonstrated that the restrictive legislation provides a net community benefit, the legislation is to be reformed. Even if a net community benefit can be demonstrated, for an existing approach to be retained, it must then be shown that there are no less restrictive ways of meeting the legislation’s objectives. If these can be demonstrated, an alternative approach must be adopted. The burden of proof rests with those defending the anti-competitive legislation.

The terms of reference thus require the Committee to suggest how (and if) wheat exports might be regulated if the WMA is found to restrict competition and the legislation does not pass the ‘public benefit’ test.

When applying the ‘public benefit’ test, the Committee is to take into account the same broad set of possible costs and benefits detailed in the Competition Policy Agreements.

1.1.3. Requirements for assessment of regulation by the Commonwealth

‘3. In making assessments in relation to the matters in (2), the Committee is to have regard to the analytical requirements for regulation assessment by the

Commonwealth, including those set out in the Competition Principles Agreement’.

The Competition Principles Agreement sets out five key areas an NCP review of legislation should cover:

- clarify the objectives of the legislation;
- identify the nature of restriction on competition;
- analyse the likely effect of the restriction on competition and on the economy generally;
- assess and balance the costs and benefits of the restriction; and
- consider alternative approaches for achieving the same result, including non-legislative approaches.

The terms of reference direct the Committee to have regard to these general requirements for regulation assessment.

The principles for structural reform of public monopolies within the Competition Principles Agreement are also relevant. These state that before a Government introduces competition to a sector traditionally supplied by a public monopoly, it will remove from the public monopoly any responsibilities for industry regulation. The Government is to relocate industry regulation functions ‘so as to prevent the former monopolist enjoying a regulatory advantage over its existing and potential rivals’.

These principles were taken into consideration when the former Australian Wheat Board was privatised and its regulatory and commercial functions divided. The terms of reference (see 4 (c) below) require the Committee to revisit this issue.

1.1.4. Required material to be included in the review Committee’s report

‘4. The report of the independent Committee should:

- (a) identify the nature and magnitude of the economic, social, environmental or other issues the WMA seeks to address
- (b) assess the objectives of the WMA and the Wheat Export Authority arrangements, structure and functions
- (c) assess the effectiveness of the separation of regulatory and commercial functions in the WMA
- (d) identify whether, and to what extent, the WMA restricts competition, including the appropriateness of granting a monopoly to a private company
- (e) identify any relevant possible alternatives to the wheat export arrangement in the WMA, including non-legislative approaches
- (f) analyse and quantify the benefits, costs and overall effects on businesses involved in the Australian wheat industry and/or the community generally (the public benefits test), of the existing WMA arrangements, compared to the alternatives identified in (e) above; and identify the impact on different groups likely to be affected by either the continuation of the WMA arrangements or implementation of viable alternatives

- (g) determine a preferred option for regulation, if any, in light of objectives set out in (2) above (the paragraph dealing with appropriate future arrangements for the regulation of wheat exports)
- (h) examine mechanisms for increasing the overall efficiency, including minimising the compliance costs and paper burden on small business, of both the WMA and, where it differs, the preferred option
- (i) list the individuals and groups consulted during the review and outline their views, or reasons why consultation was inappropriate’.

The terms of reference list more specifically the required material to be included in the Committee’s report.

Note that 4 (f) explicitly requires the Committee to undertake its own assessment of whether the benefits to the community as a whole of restricting competition outweigh the costs, and whether the objectives of the legislation can only be achieved by restricting competition.

1.1.5. Consultation with stakeholders and publishing a report

‘5. Part of the review will involve the Committee advertising in national and major rural media, consulting with key stakeholders, other affected parties and rural communities likely to be affected by any reforms, and publishing a report’.

The terms of reference direct the Committee to deal with stakeholders in an open and transparent fashion, and to publish a report. The Committee has adopted the view that this report should be available to the public, and that important reference material used in preparation of the report should also be available. The Committee has taken the initiative to integrate a dedicated Internet site into its overall communications strategy (www.affa.gov.au/wma).

1.1.6. Delivery of the report

‘6. The Committee should also take into account it is the Government’s intention to announce its responses to its recommendations. It will do this after obtaining advice from the Minister and if appropriate, after consideration by Cabinet’.

The terms of reference advise the Committee that the Government may or may not accept its recommendations, or may accept them in a modified form.

1.2. Structure of the report

The structure of the report is largely determined by the required material to be included in the Committee’s report as set out in paragraph 4 of the review terms of reference.

This introduction has touched briefly on such topics as the National Competition Policy, the NCP review process, the legislation under review (the WMA), and how the NCP Review of the WMA is being conducted. More detailed material relevant to this review on these topics is set out in **chapter 2**.

The wheat industry is a major Australian rural industry. Its size and significance, its contribution to farm incomes, Australia's wheat supply and disposal, world wheat trade and Australia's wheat export markets, and government involvement in Australian wheat marketing are discussed in **chapter 3**. Paragraph 4 (a) requires the Committee to identify the nature and magnitude of the main issues the WMA seeks to address. These are also discussed in this chapter.

As required by paragraphs 5 and 4 (i) in the terms of reference, the Committee consulted widely with stakeholders to obtain their views. These stakeholder views are set out in **chapter 4**, which includes views obtained through face to face consultation, and by an examination of stakeholder submissions.

Paragraph 4 (b) requires the Committee to assess the objectives of the WMA, and the arrangements, structure and functions of the WEA, Paragraph 4 (d) to identify whether, and to what extent, the WMA restricts competition, (including the appropriateness of granting a monopoly to a private company), and Paragraph 4 (c) to assess the effectiveness of the separation of regulatory and commercial functions in the WMA. These assessments are undertaken in **chapters 5 and 6**.

Paragraphs 2 and 4 (f) require the Committee to analyse and quantify the benefits, costs and overall effects on businesses involved in the Australian wheat industry and the community generally of the existing arrangements, compared to the alternatives. This, the 'public benefit' test, is contained in **chapter 7**.

Paragraphs 2 and 4 (e) require the Committee to identify any relevant possible alternatives to the wheat export arrangement in the WMA. These alternatives are identified and discussed in **chapter 8**.

Paragraph 4 (g) requires the Committee to determine a preferred option for regulation. This is discussed in **chapter 9**. Paragraph 4 (h) requires the Committee to examine mechanisms for increasing the overall efficiency, including minimising the compliance costs and paper burden on small business, of the existing arrangements, or viable alternatives. This is also discussed in this chapter.

References

CIE (Centre for International Economics) 1999, *Guidelines for NCP Legislation Reviews*, Prepared for the National Competition Council, CIE, Canberra.

2. NATIONAL COMPETITION POLICY REVIEWS

National Competition Policy (NCP) reviews are conducted using a common framework established by the Commonwealth, State and Territory governments. This chapter briefly describes the National Competition Policy, the legislation under review (the *Wheat Marketing Act 1989*), the NCP process for reviewing legislation, and how this review of the WMA was conducted.

Key sections in chapter:

- National Competition Policy
- The *Wheat Marketing Act 1989* (the WMA)
- NCP process for reviewing legislation
- Conduct of the NCP Review of the WMA

2.1. National Competition Policy

In 1995, Australia's nine governments agreed to implement the NCP reform program. The resulting Competition Principles Agreement (CPA) builds on a process that was launched with the *Trade Practices Act 1974* (TPA). The TPA established rules to limit the abuse of market power by businesses, promote fair trading and efficient industry practices and to protect consumers (NCC 1999).

The NCP reforms consolidated a number of other reforms which governments were already in the process of developing or implementing. Under the CPA, Australian Governments agreed to:

- extend the reach of the anti-competitive conduct laws in Part IV of the TPA to virtually all private and public sector businesses;
- improve the performance of essential infrastructure through implementing reform packages in the electricity, gas, water and road transport industries; and establishing third party 'access' arrangements for the services of nationally significant monopoly infrastructure;
- review and, where appropriate, reform all laws which restrict competition, and ensure that any new restrictions provide a net community benefit; and
- improve the performance of government businesses through structural reform, introducing competitive neutrality so that government businesses do not enjoy unfair advantages or disadvantages when competing with private business.

While the NCP builds on some elements of earlier reforms, it is also different in that it addresses a number of areas of the economy which, by virtue of regulatory or legislative protection, or due to the complexity of the task, hitherto had not been considered for reform. Additionally, many of the NCP reforms touch on complex areas of social and economic regulation. For these reasons, the NCP incorporates a public interest test to assess whether a particular reform is in the interests of the community as a whole. The test is intended to take into account the interests of each

affected group and to assess in an open and objective way whether a particular reform should proceed (NCC 1999).

The public interest test, set out under clause 1(3) of the CPA, covers a wide range of factors:

- Government legislation and policies relating to ecologically sustainable development;
- social welfare and equity considerations, including community service obligations;
- Government legislation and policies relating to matters such as occupational health and safety, industrial relations and access and equity;
- economic and regional development, including employment and investment growth;
- the interests of consumers or of a class of consumers;
- the competitiveness of Australian business; and
- the efficient allocation of resources.

The public interest test therefore covers a wide range of factors, giving equal weight to economic and social considerations.

According to the National Competition Council (1999):

‘In essence, most NCP reforms are measures designed to reap the benefits that competition, properly harnessed, can bring. The objective is not to pursue competition as an end in itself, but, where appropriate, to inject competition into previously sheltered areas of the economy to boost economic performance and provide benefits to Australian consumers and households’.

2.2. The Wheat Marketing Act 1989

Soon after the end of World War II attempts were made to continue the national wheat marketing and stabilisation arrangements which had been put in place as a wartime measure. In 1948 the Commonwealth and States passed complementary wheat marketing legislation which reconstituted a statutory Australian Wheat Board with power to acquire in its own right all wheat produced in Australia, to market that wheat both within Australia and overseas, and to control the export marketing of wheat products. The legislation also provided for guaranteed prices to growers and, later, for administered pricing of domestic wheat.

Statutory wheat marketing with ‘single desk’ selling through the Australian Wheat Board was continued with support from growers and successive governments for over fifty years. During this time there were a number of reviews, and various changes to the legislation relating to the Board’s guaranteed price, underwriting, administered domestic pricing, and the pooling arrangements. In 1989 the domestic marketing of wheat was deregulated, and the Board’s compulsory acquisition powers withdrawn. Through this period, however, the powers accorded the Board under the legislation for ‘single desk’ selling of export wheat have remained.

Statutory marketing of wheat ceased on 1 July 1999 with the transfer of the commercial functions of the former Australian Wheat Board to a grower owned and controlled company, AWB Limited. The former Australian Wheat Board was continued as a legal entity but with a new name (the Wheat Export Authority - WEA) with limited regulatory functions. 'Single desk' selling of export wheat was retained by the legislation exempting AWB (International) Limited (AWBI), the subsidiary of AWB Limited responsible for pooling matters, from the requirement for WEA consent, and by giving AWBI a veto over bulk wheat export applications to the WEA. This right is on-going unless the legislation is amended by Parliament.

The legislation changed extensively with the cessation of statutory marketing for wheat. The original *Wheat Marketing Act 1989* set out the objects, functions and powers of the statutory Australian Wheat Board. The Act was extensively amended in 1997 to effect the restructure of the Australian Wheat Board and the transfer of its commercial functions to a grower owned and controlled company. This transfer was completed in a second amending Act in 1998. The current version of the *Wheat Marketing Act 1989* came into force on 1 July 1999, and has the long title 'an Act relating to the export of wheat, and for other purposes'. The long title reflects its focus on regulatory arrangements for export wheat. The amended Act is the subject of this NCP legislation review.

2.3. The NCP process for reviewing legislation

As mentioned in the introduction, the CPA sets out five key areas an NCP review of legislation should cover:

- clarify the objectives of the legislation;
- identify the nature of restriction on competition;
- analyse the likely effects of the restriction on competition and on the economy generally;
- assess and balance the costs and benefits of the restriction; and
- consider alternative approaches for achieving the same result, including non-legislative approaches.

In 1999 the National Competition Council commissioned the Centre for International Economics (CIE) to set out as clearly as possible a framework covering the NCP legislation review and reform process, including implementation of recommendations (CIE, 1999). The report noted three key phases of an NCP legislation review:

- establish a review;
- undertake a review; and
- implement the review's recommendations into policy.

In phase I the review's scope and structure are established, the terms of reference determined, the review Committee chosen, and stakeholder involvement sought. In phase II, the subject of this report, the review itself is undertaken. Following this, in phase III, the review's recommendations are examined by government, and legislation may be reformed.

In some public consultation hearings, stakeholders asked the Committee to conduct a grower vote to determine the future of the 'single desk' arrangements. Whilst a popular vote does not form part of the NCP framework, the Committee is certain that the wide consultative process detailed below enabled all sectors of the industry to directly express their views to the Committee.

The great interest shown in the review process by all sectors of the industry, including large numbers of individual producers, processors, bulk handlers, marketers and end-users, has contributed to a robust policy debate over the future of the wheat industry.

2.4. Conduct of the NCP Review of the WMA

The Honourable Warren Truss MP, Federal Minister for Agriculture, Fisheries and Forestry, announced the review on 4 April 2000 in his speech to Grains Week 2000. The Minister appointed an Independent Committee consisting of Mr Malcolm Irving AM, Professor Bob Lindner, and Mr Jeff Arney, to undertake the review. The Department of Agriculture, Fisheries and Forestry (AFFA) provided secretariat support to the Committee.

The Committee called for submissions by stakeholders and met with major groups in early May to advise them the review had commenced. The Committee also released an issues paper to assist stakeholders in preparing submissions and set up an Internet site containing information on the review.

The review was conducted in an open and transparent manner, giving all stakeholders ample opportunity to participate and contribute. Key communication and consultation activities included:

- advertising widely to stimulate public submissions, resulting in the Committee receiving over 3,300 public submissions from interested parties by the closing date on 17 July;
- maintaining an Internet site at www.affa.gov.au/wma that received commendation in the press for openness and transparency in a legislation review;
- publicising an e-mail address to facilitate comment and informal communication, resulting in almost 600 e-mails received;
- disseminating regular media releases and reports to an e-mail distribution list of almost 400 stakeholders; and
- consulting with key stakeholders throughout Australia and overseas through almost 170 public and private meetings.

In early July, to assist in the preparation of its draft report, the Committee appointed a consultant, the Allen Consulting Group, to undertake a technical assessment of the economic and social effects of the WMA. The Committee also commissioned leading academics to prepare a paper on methodology to be used in the 'net public benefits' test.

In mid-July the Committee undertook overseas consultations, meeting government authorities, growers, traders, and end-users in Argentina, Canada, the United States, Japan, and South Korea. Committee members individually undertook further

consultations in Egypt and the European Union.

The Committee then travelled within Australia in the first half of August to seek input from stakeholders in private and open public forum meetings. The locations for this first round of domestic consultation were Emerald (Qld), Moree (NSW), Griffith (NSW), Horsham (Vic), Dalwallinu (WA), Lake Grace (WA), Merredin (WA), Cleve (SA), Wudinna (SA) and Nuriootpa (SA).

The Committee released a draft report for written comment and further consultation on 13 October. The report contained nine 'preliminary views' and invited comment from stakeholders by 13 November. The draft report was available on the Internet site, where it was downloaded over 2,360 times (making it the second-most popular document on the AFFA site), and a number of print copies were distributed free of charge. Subsequently, over 60 supplementary submissions were received and their comments analysed by the Committee.

On 13 October the Committee also released the technical assessments of the economic and social effects of the WMA prepared by the Allen Consulting Group. Subsequently, the Committee requested further technical analysis, specifically of the 'single desk price premium', to identify the source of any such premium in detail.

The Committee then undertook a second round of domestic consultation with stakeholders and public meetings in November and early December. The locations for the second round of public meetings were Swan Hill (Vic), Forbes (NSW), Moree (NSW), Toowoomba (Qld), Balaklava (SA), Kimba (SA), Katanning (WA), Merredin (WA), Newdegate (WA) and Mingenew (WA).

Great care has been taken to reflect as fully as possible the broad diversity of views considered by the Committee in reaching the recommendations contained in this report. However, limitations on the preparation time and length of the report may have resulted in the evidence presented here not comprehensively reflecting all the evidence relied on by the Committee in coming to its decisions.

The Government will consider the Committee's report before formally responding in 2001.

References

CIE (Centre for International Economics) 1999, *Guidelines for NCP Legislation Reviews*, Prepared for the National Competition Council, CIE, Canberra.

NCC (National Competition Council) 1999, *National Competition Policy: Some Impacts on Society and the Economy*, AGPS, Canberra.

NCP WMA Secretariat 2000, *Issues Paper for the National Competition Policy Review of the Wheat Marketing Act 1989*, <http://www.affa.gov.au/wma>.

3. AUSTRALIAN WHEAT INDUSTRY

Australia is the world's fourth largest wheat exporter after the United States, Canada, and the European Union (EU). Sales of export wheat contribute significantly to the Australian economy. The importance of export markets for wheat has also been instrumental in determining the nature of government involvement in Australian wheat marketing. This chapter describes the size and significance of the Australian wheat industry, durum wheat, wheat's contribution to farm incomes, Australia's wheat supply and disposal, world wheat trade and Australia's wheat export markets, and government involvement in Australian wheat marketing.

Key sections in chapter:

- Size and significance of the wheat industry
- Durum wheat
- Wheat's contribution to farm incomes
- Australia's wheat supply and disposal
- World wheat trade
- Australia's wheat exports
- Government involvement in Australian wheat marketing

3.1. Size and significance of the wheat industry

3.1.1. Gross value of production and exports

Wheat contributes significantly to the gross value of Australian farm production. In 1998-99, production from Australian farms was valued at just over \$28 billion. Of this, crops contributed nearly \$16 billion, including \$4 billion from wheat and \$3 billion from other grains and oilseeds (ABARE 1999a). With up to 80 per cent of the wheat crop exported, export wheat thus accounts for around ten per cent of the gross value of national farm production.

Wheat also provides a large share of the value of Australian farm product exports. In 1998-99 wheat exports were valued at \$3.5 billion or 15.6 per cent of total farm exports of \$22.4 billion (ABARE 1999a).

3.1.2. Wheat area and production

At 12.3 million hectares, wheat plantings in 1999-2000 were the second largest on record, exceeded in area only by the 12.9 million hectares planted in 1983-84. By state, 4.6 million hectares were planted in Western Australia, 3.5 million in New South Wales, 1.9 million in South Australia, 1.2 million in Victoria, and 1.1 million in Queensland. The 1999-2000 crop was a record 25.0 million tonnes (ABARE 2000).

Wheat plantings reached an estimated 12.1 million hectares in 2000-01, but wheat production fell as a result of significant crop losses due to dry conditions in Western Australia, southern Queensland and (until recently) northern New South Wales, followed by heavy rains and flooding in northern New South Wales. In its

5 December 2000 *Crop Report*, ABARE estimated 2000-01 state plantings at 4.4 million in Western Australia, 3.5 million in New South Wales, 2.0 million in South Australia, 1.2 million in Victoria and 1.0 million in Queensland. ABARE currently estimates the 2000-01 wheat crop at 19.6 million tonnes.

3.1.3. Field crop production by state

Wheat dominates field crops production. In the period 1994-95 to 1998-99, wheat accounted for on average 57 per cent of Australia's combined production of grains, oilseeds and pulses. Coarse grains accounted for 30 per cent, pulses for 7 per cent, and oilseeds for 6 per cent (calculated from ABARE 1999a).

Table 3.1 shows average Australian field crops production by state from 1994-95 to 1998-99. In this period Australia's production of wheat averaged 18.1 million tonnes a year, while production of coarse grains averaged 9.3 million tonnes. Pulse and oilseeds production averaged 2.1 and 2.0 million tonnes, respectively.

Table 3.1: **Australian field crop production: (kt)**
Five-year average, 1994-95 to 1998-99

	Wheat	Coarse grains	Oilseeds	Pulses	Total
New South Wales	5331	2465	1064	169	9029
Victoria	1702	1409	185	316	3612
Queensland	1309	1266	403	56	3035
South Australia	2627	2013	90	330	5059
Western Australia	7165	2028	250	1273	10717
Australia	18127	9317	1993	2145	31583

Source: Calculated from ABARE 1999a, *Australian Commodity Statistics*.

The five mainland wheat-producing states differ in their respective dependence on wheat.

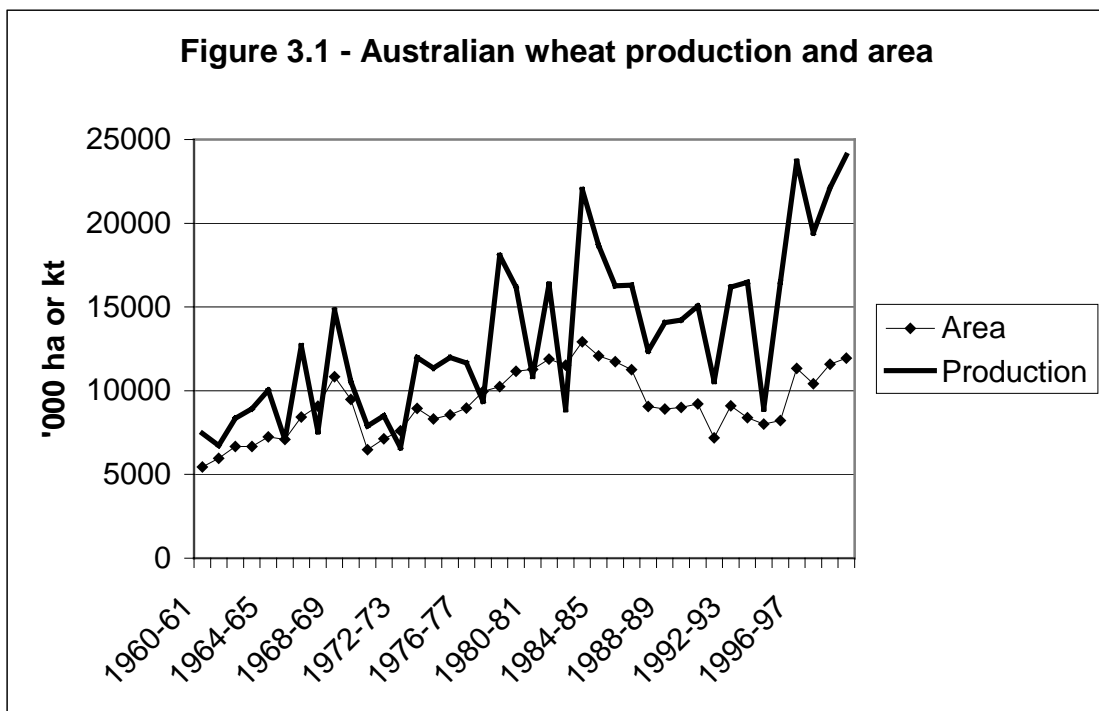
- In **Western Australia**, the largest wheat producing state, wheat accounted for 67 per cent on average of that state's combined production of grains, oilseeds and pulses in the period 1994-95 to 1998-99. Coarse grains accounted for 19 per cent and pulses for 12 per cent. Western Australian wheat production averaged 7.2 million tonnes a year, and represented 40 per cent of Australian production. Western Australia also has a greater reliance on wheat exports than most other states, has less access to the deregulated domestic market, and does not have much competition in the logistics sector.
- In **New South Wales**, the second largest wheat producing state, wheat accounted for 59 per cent of field crops production, coarse grains for 27 per cent, and oilseeds for 12 per cent. Wheat production averaged 5.3 million tonnes a year, representing 29 per cent of Australian production.
- In **South Australia**, the third largest wheat producer, wheat accounted for 52 per cent of field crops production, coarse grains for 40 per cent, and pulses for

7 per cent. Wheat production averaged 2.6 million tonnes a year, representing 15 per cent of Australian production.

- **Victoria's** production profile is similar to South Australia's. In Victoria, wheat accounted for 47 per cent of field crops production, coarse grains for 39 per cent, and pulses for 9 per cent. Victorian wheat production averaged 1.7 million tonnes, representing 9 per cent of Australian production.
- In **Queensland**, wheat and coarse grains production are roughly equal. In the period 1994-95 to 1998-99 wheat accounted for 43 per cent of field crops production, coarse grains for 42 per cent, and oilseeds for 13 per cent. Queensland wheat production averaged 1.3 million tonnes a year, representing 7 per cent of Australian production.

3.1.4. Trends in wheat area and production

Australian wheat area and production are highly variable from season to season (Figure 3.1). However, behind these seasonal fluctuations, broad cycles of expansion and contraction can be made out. These can be seen more clearly when the annual data is expressed as five-year averages (Figure 3. 2).

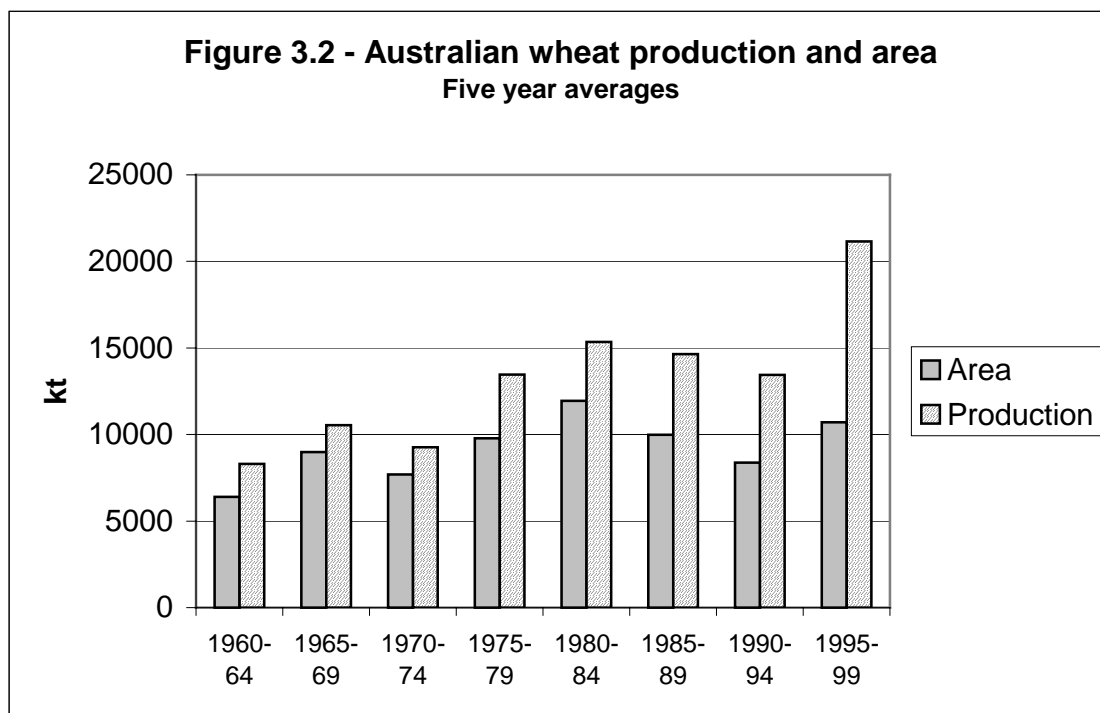


Sources: ABARE 1999, *Australian Commodity Statistics*; ABARE 2000, *Australian Crop Report*, 5 December.

Australian wheat area reached a peak of 10.8 million hectares in 1968-69, but in 1970-71 only 6.5 million hectares were planted. The expansion and subsequent fall were driven by world market conditions. Wheat supply had been rising worldwide, but began to run ahead of demand. Wheat stocks held by the major exporters – Canada, the United States, and Australia – built up. World wheat prices collapsed, and supply control programs were put in place in Canada, the United States, and Australia.

In Australia's case, the chosen method of supply control was delivery quotas. In the last years of delivery quotas, production was also cut by poor seasonal conditions.

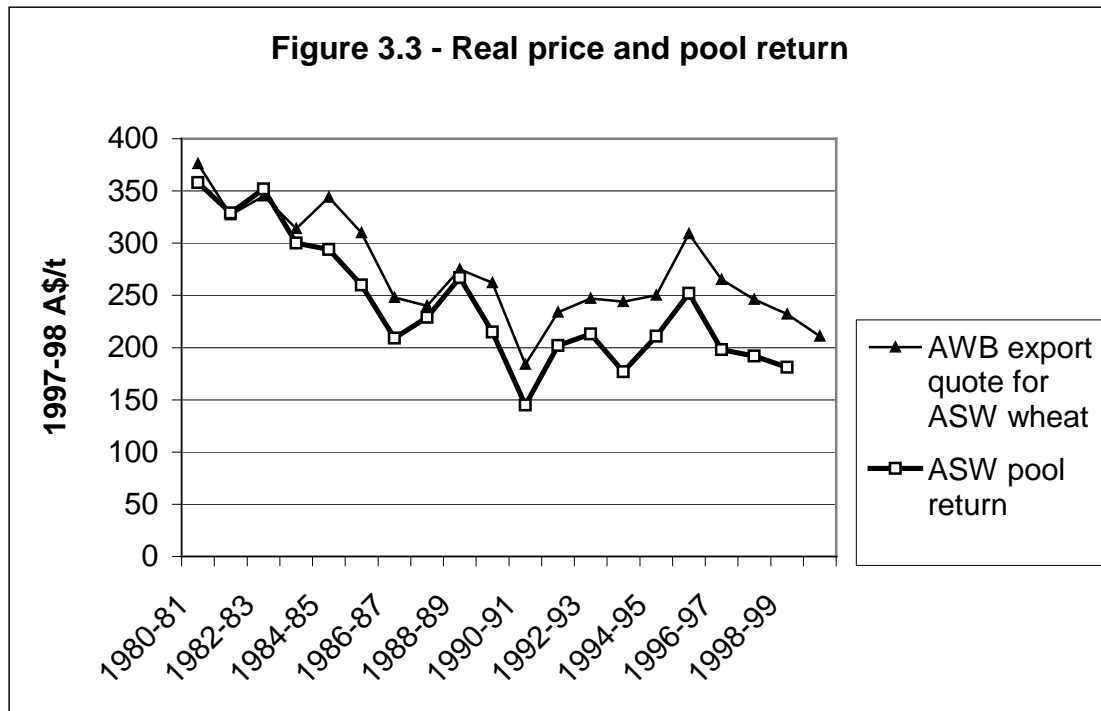
In the early 1970s the supply picture abruptly changed from surplus to shortage. A surge in world import demand in 1973 caused a sharp spike in world wheat prices, and wheat exporters began to increase production once more.



Source: Calculated from ABARE 1999, *Australian Commodity Statistics*; ABARE 2000.

Australian's wheat area expanded again, peaking at 12.9 million hectares in 1983-84. However, as before, world wheat supply began to run ahead of demand, putting downward pressure on world wheat prices (Figure 3.3).

Some exporters supported, and even raised, prices in this period by accumulating stocks. But when these stocks were finally released, prices collapsed. After a drastic fall in the export pool return in 1990-91, Australian wheat producers planted only 7.2 million hectares of wheat in 1991-92.



Source: Calculated from ABARE 1999, *Australian Commodity Statistics*; ABARE 2000.

World wheat prices surged again in 1995-96, pushing Australian export pool returns back up. Lower wool and beef prices further increased the relative attractiveness of wheat. As shown in Table 3.2, in the period 1995-96 to 1999-2000, wheat prices on average were at their highest point relative to livestock prices than at any other time since the early 1980s, when Australian wheat area last peaked.

Table 3.2: Australian wheat and livestock prices a

	Wheat b	Cattle c	Wool d	Cattle/ wheat	Wool/ wheat
	\$/t	c/kg	c/kg	Ratio e	Ratio e
1980-81 – 1984-95	165	139	280	1.00	1.00
1985-86 – 1989-90	177	190	515	1.27	1.71
1990-91 – 1994-95	184	211	384	1.36	1.23
1995-96 – 1999-00	202	180	394	1.06	1.15

a Five-year averages of nominal prices. b Unit value. c Weighted average saleyard price, dressed weight basis. d Auction price (greasy). e Relative to the period 1980-81 to 1984-85, which is set at 1.

Source: Calculated from ABARE 1999, *Australian Commodity Statistics*.

As a result, growers have increased wheat plantings to near-record levels. Combined with higher wheat yields, this has appreciably increased Australian wheat production, and export availability. Despite world wheat import demand remaining largely static (the higher imports by the developed and newly industrialised countries being offset

by reduced imports by Russia and China), Australia's export share in the world market has risen along with production.

Whether Australia's wheat exports and export share will continue at this new higher level will depend on a number of factors, not the least being the area of Australian wheat planted. As history has shown, wheat area can expand quickly when prospects appear good, but contract just as quickly if prices collapse or if alternatives such as livestock become relatively more attractive.

With wheat prices having fallen away in real terms from their recent peak in 1995-96, producers may now be re-evaluating wheat's prospects relative to alternative field crops and livestock. However, the large wheat plantings being undertaken in 2000-01 suggest wheat remains an attractive option for many growers.

3.2. Durum wheat

Durum wheat for manufacturing into pasta products is derived from a subspecies of wheat (*Triticum turgidum ssp. turgidum*) which is separate and distinct from bread wheats (*Triticum aestivum*). Durum wheat is not suitable for the manufacture of bread products.

Australian No.1 durum as classified by AWB Limited consists of selected wheat varieties with vitreous, amber coloured kernels with a minimum protein of 13.0 per cent and capable of achieving high yields of superior quality semolina with minimal residual flour production. The semolina produced from this specialised wheat exhibits high levels of stable yellow pigment and high water absorption, making it ideally suited to the production of a wide range of high quality wet and dry pasta products with excellent colour and shelf life. Australian No.2 and No.3 durum grades are received at 11.5 per cent and 10.0 per cent minimum protein respectively.

Segregations for lower grade durum are also implemented in some years to take account of weather damage, fungal staining or other problems.

3.2.1. Production and trade

World production of durum averages around 33 million tonnes. The main producers are the EU (8-9 million tonnes), Canada (5-6 million tonnes), Turkey (4 million tonnes) and the United States (3.5 million tonnes). Annual world trade in durum is around 7 million tonnes. Canada (4 million tonnes), the United States (1.2-1.5 million tonnes) and the EU (0.4 million tonnes) are the main durum exporters.

In Australia, durum is produced primarily in northern New South Wales (about 75 per cent of Australian production) and South Australia (around 15 per cent). Small amounts of durum wheat are also grown in Queensland and Western Australia. Until the mid-1990s Australian durum production was well under 100 000 tonnes. However, durum production rose sharply in the late 1990s. According to AWB Limited, production exceeded 400 000 tonnes in 1998-99 and reached almost 700 000 tonnes in 1999-2000. NSW Agriculture estimates put 1999-2000 season production even higher.

Australian durum exports have also increased. According to AWB Limited, exports exceeded 200 000 tonnes in 1998-99 and reached almost 500 000 tonnes in 1999-2000. The main export destinations are Italy and North Africa.

3.2.2. Prices

Pool returns for No.1 durum are usually around \$A50-60 per tonne above returns for Australian Premium White (APW) and \$A20-30 per tonne above Australian Prime Hard (APH). However, in 1997-98 the pool return for durum returns was \$A142 per tonne over APW. When making such price comparisons it should be noted that production costs for durum are higher than for wheat, and the yield for durum may be lower in some situations.

Since Canada is the largest exporter of durum, the Canadian export price may be viewed as a 'world indicator' price for durum. In recent years the Canadian export price for durum has averaged around \$US35 per tonne above prices for top quality Canadian spring wheats.

Movements in the indicator world export price of durum are relatively independent of those of wheat. However, there is some broad correlation between movements in the prices of all grains (Table 3.3), reflecting the various possibilities of substitution in use and in production. There is around the same correlation between movements in the prices of durum and high protein wheat as there is between those of ordinary protein wheat and corn. As may be expected, movements in the price of durum are more closely correlated with movements in the price of high protein wheat than with those of ordinary protein wheat.

Table 3.3: **Correlation between monthly export price quotations of selected grains**

	Durum a	High protein wheat b	Ordinary protein wheat c
High protein wheat	0.82	-	-
Ordinary protein wheat	0.70	0.89	-
Corn d	0.65	0.85	0.86

a Canada No.1 CW Amber Durum (fob St. Lawrence). b US No.2 Dark Northern Spring 14% protein (fob Gulf). c US No.2 Hard Red Winter Ordinary protein (fob Gulf). d US No.2 Yellow Corn (fob Gulf).

Source: Calculated from International Grains Council 2000, *World Grain Statistics 1998-99* (including market updates and previous issues), using monthly price quotations from July 1986 to December 1999.

3.2.3. Marketing

Durum wheat is marketed by growers through:

- a direct contract with a domestic pasta manufacturer, such as San Remo in South Australia;

- producer co-operatives such as the Australian Durum Producers Cooperative Ltd in NSW, which may organise domestic or export sales; and
- the relevant subsidiaries of AWB Limited via pools or on a cash sale basis; or
- private traders.

Durum wheat is subject to the export control provisions of the *Wheat Marketing Act 1989* (the WMA) even though it is a different species to bread wheat. The WMA does not define 'wheat' and hence all wheat is taken to be included in the 'single desk' arrangements. AWB (International) Ltd (AWBI), which holds the 'single desk' under the WMA, is the sole exporter of durum in bulk. Since 1999 AWBI has not agreed to any other applicant being given a bulk consent for durum. The Wheat Export Authority (WEA) can issue consents for durum exports by container or in bags after consultation with AWBI.

3.2.4. History

The durum wheat industry developed through direct contracts between growers in New South Wales and millers/users. By the late 1960s specific research and breeding programs were being conducted by the New South Wales Department of Agriculture.

The industry expanded throughout the 1970s and 1980s (including to South Australia and Western Australia) largely based on meeting domestic demand and with minimal involvement from the then Australian Wheat Board. In the early 1990s export surpluses became available and the then Australian Wheat Board issued permits over several years for bulk exports by private traders from New South Wales. The maximum amount exported this way in any one year was around 65 000 tonnes.

By 1996-97 the then Australian Wheat Board was operating specific pools for durum wheat and by 1998 a specialist position of durum merchant was established within the Board to identify and exploit opportunities for durum.

Some parts of the New South Wales industry have sought over the last few years to have durum wheat excluded from the 'single desk' arrangements. It is claimed that better returns would be available from export sales through private traders. This has been disputed by AWB Limited. A New South Wales trader refused a bulk export consent for durum from the 1999 harvest has taken action, with the support of some growers, against AWBI and the WEA in the Federal Court, but was unsuccessful.

3.3. Wheat's contribution to farm incomes

3.3.1. Number of crop farms

Wheat is produced in conjunction with other crops and livestock on broadacre farms. ABARE estimates there are just over 70 000 broadacre farms in Australia (Knopke, O'Donnell and Shepherd 2000). Some 31 000 of these derive the bulk of their income from cropping. In its survey statistics ABARE distinguishes between 'crop specialist' and 'mixed livestock-crops' producers.

In the period 1995-96 to 1998-99, there were 14 100 crop specialist producers. These received 61 per cent of the nation's crop receipts in the period examined. The average crop specialist farm derived four fifths of its gross receipts from cropping (half from wheat) and devoted nearly half of total area operated to grain crops.

Australia's 17 400 mixed-crops livestock producers received a further 33 per cent of the nation's crop receipts in the period examined. The average mixed crops-livestock farm derived half its gross receipts from cropping (half from wheat) and devoted around twenty per cent of total area operated to grain crops.

3.3.2. Rates of return

In the period 1995-96 to 1998-99, reflecting the relatively high returns obtainable from wheat and other crops, crop farms earned relatively high average annual rates of return: 6 per cent for crop specialist farms, and 2 per cent for mixed-crops livestock farms. In contrast, the rates of return on sheep, beef, and sheep-beef farms were negative (ABARE 2000b).

3.3.3. Regional characteristics

The Grains Research and Development Council (GRDC) identifies three broad 'agroecological' regions for grain cropping: 'western' (Western Australia), 'northern' (central and southern Queensland and northern New South Wales) and 'southern' (southern New South Wales, Victoria, and South Australia).

In the 'western' region grain farms tend to be larger than in the 'northern' and 'southern' regions, to devote more of their total area to cropping, and to use slightly more labour per farm. Western region grain farms earned an average rate of return of 4.3 per cent from 1992-93 to 1996-97, and 4.9 per cent in 1997-98 (ABARE 1999b).

In the 'northern' region grain farms are slightly smaller, devote relatively less of their total area to crops, and earned an average rate of return of 1.9 per cent from 1992-93 to 1996-97, and 2.1 per cent in 1997-98.

In the 'southern' region grain farms are smaller than in the west and north, devote less of their total area to crops than in the west (but more than in the north), and earned an average rate of return of 3.0 per cent from 1992-93 to 1996-97, and 2.5 per cent in 1997-98.

3.3.4. Differences between farms

While there are some broad differences between grain farms in each region, the ABARE data suggest there is a much wider variation in performance between farms within each region than there is in the average performance of farms between regions.

In the western region the top performing 25 per cent of farms averaged a rate of return of nearly 11 per cent (1992-93 to 1996-97). In the southern region the corresponding figure was 10 per cent, and in the northern region, 8 per cent. In comparison, the bottom performing 25 per cent of farms in each region all experienced negative rates of return.

In all three regions the top performing 25 per cent of farms tended to be relatively larger, to devote a relatively larger proportion of their area to cropping, to use relatively slightly more labour, and to have a relatively younger operator.

3.4. Australian wheat supply and disposal

Australia produces wheat well in surplus of its own domestic requirements and has therefore developed a strongly export oriented wheat industry. The amounts of wheat sold on the export and domestic market are summarised in Table 3.4.

Table 3.4: **Australian wheat supply and disposal:** (kt)

	Production	Domestic use	Exports	Closing stocks
1991-92	15066	3239	11990	3164
1992-93	10557	4095	7122	2504
1992-93	16184	4186	10345	4157
1993-94	16479	3905	13805	2925
1994-95	8961	3963	6342	1581
1995-96	16504	4127	13298	660
1996-97	23702	3512	19189	1661
1997-98	19224	5012	15679	195
1998-99	22108	5285	16391	628
1999-00	25012	5770	17557	2312

Sources: ABARE 1999, *Australian Commodity Statistics*; ABARE 2000, *Australian Crop Report*, 5 December.

(Note that exports include bulk wheat, wheat in containers and bags, and the wheat equivalent of domestically produced flour.)

3.4.1. Export market

Up to 80 per cent of Australia's wheat is exported. In 1998-99 wheat exports reached 16.4 million tonnes (October-September), the third largest level on record. As in previous years the main export destinations were in the Middle East and Pacific Asia. The five largest individual destinations in 1998-99 were Iran (1.62 million tonnes), Egypt (1.5 million), Indonesia (1.44 million), Iraq (1.23 million) and Japan (1.16 million) (ABARE 1999a). Exports to some destinations are quite variable from year to year. On a five year average basis (1994-95 to 1998-99), the five largest individual destinations have been Indonesia, Iran, Japan, Egypt and India (Table 3.5).

Table 3.5: **Australian wheat exports to principal markets: (kt)**
Five year average, 1994-95 to 1998-99, October-September

Indonesia	1866
Iran	1599
Japan	1185
Egypt	928
India	824
Korea, Republic of	800
Pakistan	751
Iraq	725
Malaysia	714
China	666
Yemen	411
Thailand	245
Oman	238
Bangladesh	224
Turkey	209

Source: Calculated from AWB Limited 2000, *Annual Report 1998-99*, table 4.

3.4.2. Domestic market

Demand for wheat in the domestic market has expanded following the deregulation of that market in 1989. Domestic use of wheat is currently estimated at 5.8 million tonnes. In 1999-00, an estimated 2.25 million tonnes of wheat was used for food, and 2.8 million tonnes for feed. The balance was used for seed and on-farm.

3.5. World wheat trade

3.5.1. World

There are five major wheat exporters - the United States (US), Canada, the European Union (EU), Australia and Argentina. Other countries such as Saudi Arabia and Turkey also export wheat (Turkey both exporting and importing wheat).

Statistics on world trade in wheat (and other grains) are published by the International Grains Council (IGC) in London. The analysis in this section of the report uses IGC statistics for 1997-98 and previous years (July-June basis). According to these statistics, in the six-year period 1992-93 to 1997-98, the US supplied on average 33 per cent, Canada, 20 per cent, the EU, 17 per cent, Australia, 13 per cent, and Argentina, 8 per cent, of world wheat exports.

3.5.2. Asia

Asia (including West Asia) is the world's largest wheat importing region. In the period 1992-93 to 1997-98 this region accounted for 45 per cent of world imports. The largest importers in the Pacific Asian sub-region were China, Japan, South Korea, Indonesia, the Philippines, India, Bangladesh, and Malaysia. The largest importers in the West Asian sub-region were Iran, Pakistan, Yemen, Turkey, Iraq and Israel.

The Asian region is of particular significance to Australia for three reasons. First, most of Australia's wheat exports go to this region (82 per cent in the period 1992-93 to 1997-98). Second, Australia competes directly in the region with the US and Canada, the two other exporters most likely to be offering similar wheats. Third, Australia has significant freight advantages exporting to many Asian markets.

In the period examined, the US supplied on average 36 per cent, Canada, 23 per cent, and Australia, 24 per cent, of Asia's wheat imports. The EU supplied 6 per cent, Argentina 3 per cent, and other countries (principally Saudi Arabia and Turkey), 8 per cent.

3.5.3. Africa

Africa is another major importing region. On average, Africa accounted for 23 per cent of world wheat imports in the period 1992-93 to 1997-98. All the North African countries – Egypt, Algeria, Morocco, Libya and Tunisia – are large wheat importers. In Sub-Saharan Africa, the largest wheat importers are Nigeria and South Africa.

Australia's market presence in Africa has traditionally been strongest in Egypt. Even so, exports to other African destinations have been increasing. Some 11 per cent of Australia's wheat exports went to Africa in the period 1992-93 to 1997-98.

The African market is by and large divided between the US (37 per cent of region share) and the EU (37 per cent). Other suppliers include Canada (11 per cent), Australia (6 per cent), and Argentina (3 per cent).

3.5.4. Europe, the Former Soviet Union, North and South America

Relatively little Australian wheat is currently shipped to Europe, the Former Soviet Union, or North and South America. Australia exports about 150 000 tonnes of durum wheat annually, mainly to Italy and also to North Africa. The Former Soviet Union remains a net wheat importer, although its imports are much reduced on Soviet era levels. The EU and other European countries are currently the major suppliers to the Former Soviet Union.

In North America, one to two million tonnes of Canadian wheat is shipped annually to the US. In South America, Brazil is the largest wheat importer, and Argentina a large supplier to this and other South American markets under the Mercosur Agreement.

3.5.5. Oceania

Australia is the major wheat exporter to Oceania, supplying 81 per cent of the region's wheat imports in the period 1992-93 to 1997-98. New Zealand, Papua New Guinea, and Fiji are the region's main wheat importers.

On a world scale, and even as a destination for Australian wheat, the Oceania market is small, accounting for only 0.5 per cent of world wheat imports and 3 per cent of Australian wheat exports.

3.5.6. *Wheat export prices and export values*

The IGC collates and publishes monthly export price quotations for wheat for the major exporters. Movements in fob export price quotations for ASW wheat closely follow those for competitor wheats. An examination of over 13 years' data reveals movements in ASW fob export prices (in US\$ per tonne) are most closely correlated with movements in the fob export prices of similar US export wheats, such as US No. 2 Hard Winter Ordinary fob Gulf, and US No.2 Hard Winter 13 per cent protein fob Pacific Ports. Movements in ASW fob export prices are also correlated, to some degree, with movements in fob export prices for Canadian and Argentinian wheats, and US soft and white wheats (Table 3.6).

Table 3.6: Correlation between monthly average export price quotation of ASW and selected competitor wheats

US No. 2 Hard Winter Ordinary (fob Gulf)	0.96
US No. 2 Hard Winter 13% (fob Pacific North West)	0.96
US No. 2 Western White (fob Pacific North West)	0.90
US No. 2 Soft Red Winter (fob Gulf)	0.86
Canada No. 1 CWRS 12.5% (fob Pacific Ports)	0.87
Argentina Trigo Pan (Bread wheat)	0.90

Source: Calculated from International Grains Council 2000, *World Grain Statistics 1989-99* (including market updates and previous issues), using monthly price quotations from July 1986 to December 1999.

While movements in ASW fob export price quotations appear closely correlated with movements in the export prices of US competitor wheats (Figure 3.4), from around the start of the 1990s, there appears to have been a progressive upward shift in the ASW quote relative to US export prices (Figure 3.5). If the Australian quoted (that is, asking) prices were being realised, this suggests ASW may be being re-positioned upward in the market, based on, for example, perceptions by buyers that Australian wheat is of relatively higher quality than US and other competitor wheats.

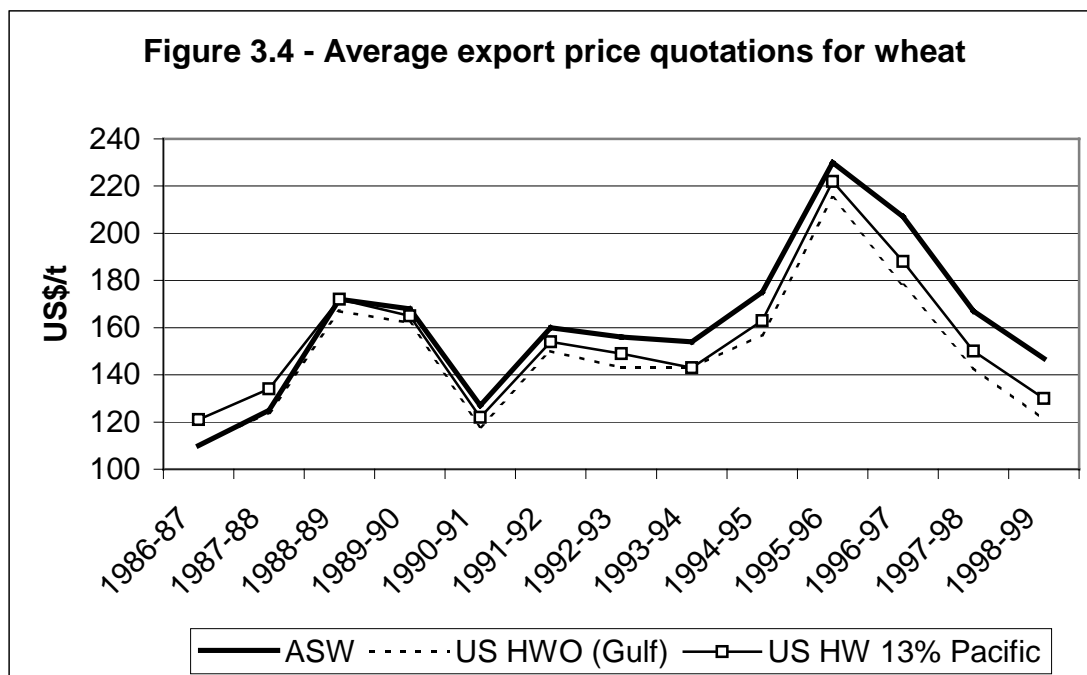
However, there is little evidence that this upward re-positioning of the quoted price of ASW is being reflected in higher actual export returns. Consistent data on actual export prices are difficult to obtain. However, one source of information is the food and Agricultural Organisation of the United States (FAO) trade data base for agricultural commodities. These data, which include the export volume and value of a comprehensive range of agricultural commodities (including wheat), are supplied by national governments. All export values are expressed in US dollars, allowing straightforward across-country comparison of the unit export values.

Figure 3.6 shows the average export unit values for wheat for the US, Canada, and Australia as calculated from the export volume and value data obtained from the FAO data base. From the graph, there appears little difference between these values – even though both Canadian and Australian wheat is sold by ‘single desk’ sellers aiming to obtain an export premium for their respective export pools, and US wheat by grain traders operating in the open market.

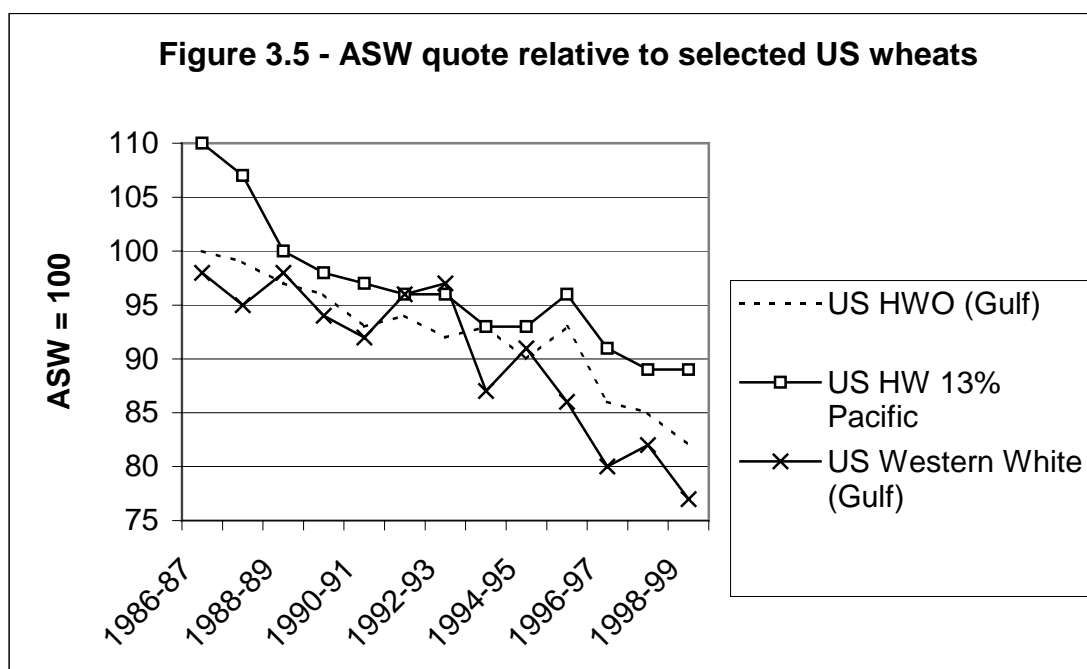
Admittedly, the average unit value aggregates wheat of different quality and grades.

However, this should work in Canada's and Australia's favour, given the relatively high proportion of high protein wheat exported by these two countries.

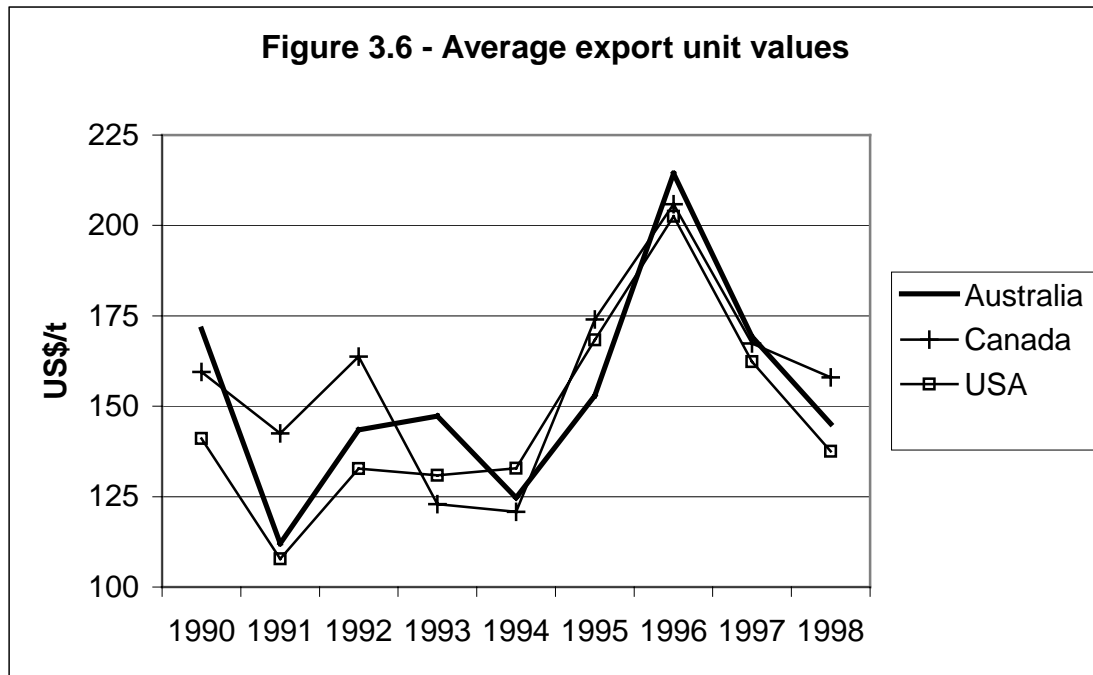
Subjecting the data in Figure 3.3 to more rigorous examination, a statistical test of the data failed to find any statistically significant difference between the annual average realised export price for wheat obtained by Canada, Australia, and the US over the 1990s (see Box 1).



Source: Calculated from International Grains Council 2000, *World Grains Statistics 1998-99* (and previous issues)



Source: Calculated from International Grains Council 2000, *World Grains Statistics 1998-99* (and previous issues)



Source: Calculated from FAO Statistical Data Base – Agriculture (www.fao.org)

BOX 1

Statistical test of realised Canadian, Australian and US export prices

One view of Australia’s dominant marketing strategy for exporting wheat is that it operates as a ‘stock disposer’. That is, it attempts to clear each season’s stocks of wheat within, or as close as possible to the end of, each season, so as to minimise stock carryover. In this view, Australia attempts to direct its exportable supplies first to the highest paying market, then to the next highest paying market, on so on, until the season’s wheat is cleared. In years of low production, because a relatively high proportion of the total export crop is sold into ‘high paying’ markets, the average annual Australian export return for wheat of that season may be above the average annual return obtained by its North American competitors. However, in years of high production, Australia may be obliged to ‘discount’ some of its wheat to clear all stocks, so its average annual export return for wheat of that season may be below the average annual return obtained by its North American competitors. In this view, any ‘single desk price premiums’ Australia may be able to obtain in some markets may be offset by the ‘discounts’ it is obliged to offer in order to promptly clear stocks. Thus it is doubtful whether, *over time*, Australian average export prices have been any higher than those obtained by its two North American competitors.

To explore this question further, the average annual export prices (unit values) realised by Canada, Australia, and the US for wheat over the 1990s were tested statistically using an F-test. As can be seen in Figure 3.6, in some years Australian export prices averaged higher than North American export prices, while in other years they averaged lower. The relevant question, however, is whether Australian average export prices have been any higher *over time* than those of the two North American competitors.

To simplify the test, the average export prices were standardised by expressing the Canadian and American average export prices as a proportion of the Australian average export price (Box Table 3.1).

Box Table 3.1: Export prices for wheat, Australia = 100.

Unit value	Australia	Canada	USA
1990	100	93	82
1991	100	127	96
1992	100	114	93
1993	100	83	89
1994	100	97	107
1995	100	114	110
1996	100	96	94
1997	100	99	96
1998	100	109	95
Mean	100	104	96

The test of the (null) hypothesis that the column means are equal was carried out by a comparison of the between-column mean square and the between-row mean square, that is, $F(2,24) = 138.86/83.35 = 1.666$. Assuming we wish to test the (null) hypothesis at the 0.05 level of significance, an F value of 3.403 would be exceeded 5 per cent of the time if the (null) hypothesis were true.

However, the computed F-ratio is 1.666, which is less than 3.403. Therefore, we cannot reject the (null) hypothesis that the column means are equal, and can conclude that there is no significant difference between the means of the standardised average annual realised export prices (unit values) obtained by Canada, Australia, and the US for wheat over the 1990s.

3.6. Australia's wheat export markets

3.6.1. Markets by region

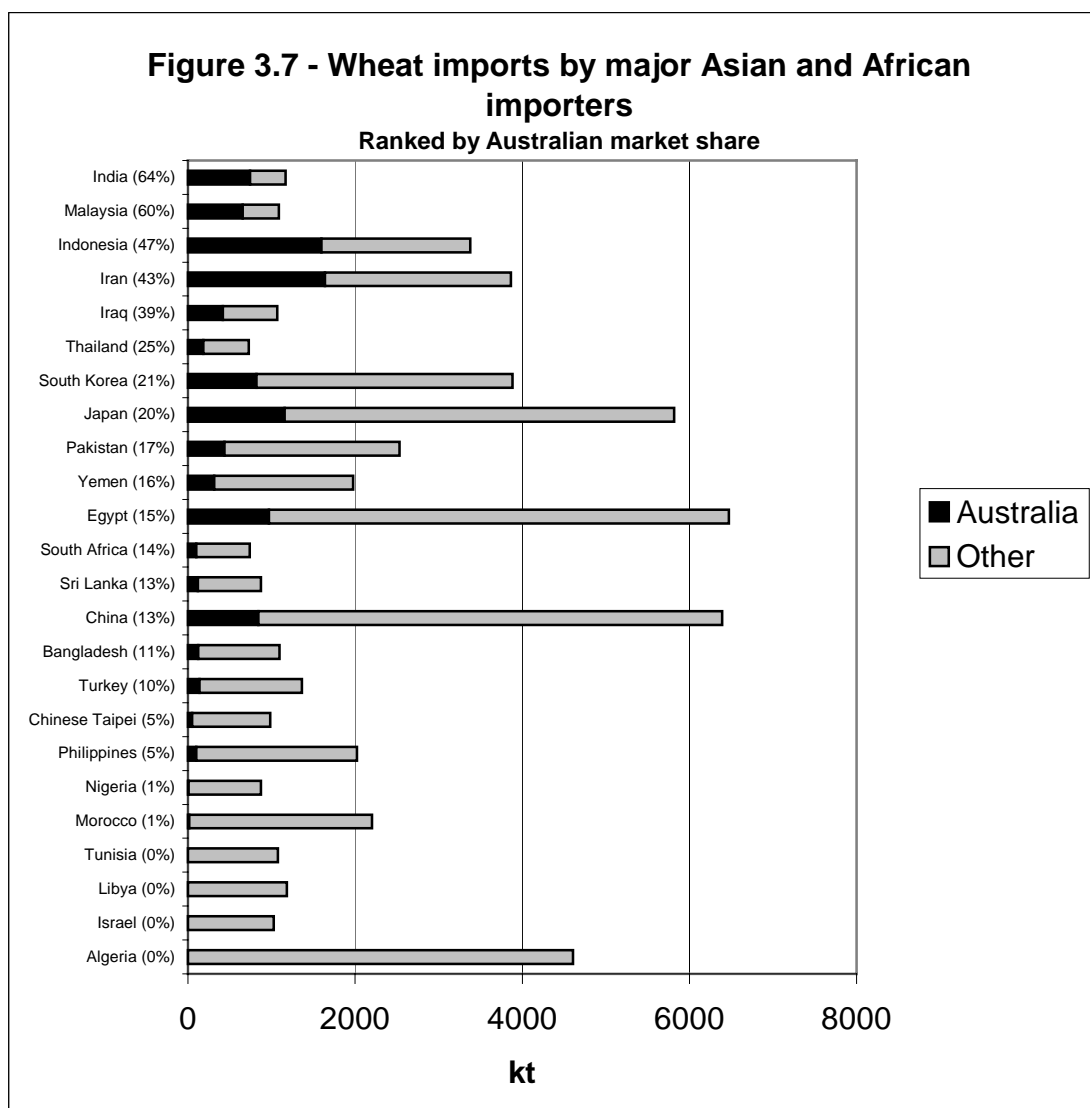
Asia and Africa together accounted for around two thirds of world wheat imports in the period 1992-93 to 1997-98. They also accounted for the bulk (93 per cent) of Australia's wheat exports. Twenty out of the twenty two countries whose wheat imports averaged more than a million tonnes in this period are in Asia or Africa.

The twenty four largest wheat importing countries in Asia and Africa imported an average of 59 million tonnes in the period 1992-93 to 1997-98, representing 61 per cent of world wheat imports and 89 per cent of total Asian and African wheat imports. In the period examined, Australia's market share averaged around 40 per cent or more in five markets: India, Malaysia, Indonesia, Iran and Iraq (Figure 3.7). Between them, these five markets took 40 per cent of Australia's wheat exports in the period 1992-93 to 1997-98. Canada is the main competitor in Indonesia and Iran.

Australia is a middle-ranking exporter (supplying 10 to 25 per cent of total imports) to eleven other large Asian and African markets: Thailand, South Korea, Japan, Pakistan, Yemen, Egypt, South Africa, Sri Lanka, China, Bangladesh and Turkey. The US is the major competitor in most of these markets, while Canada is a major competitor in China, Japan, South Korea and South Africa, and the EU is a major competitor in Yemen.

Australia also exports some wheat to Turkey, Chinese Taipei (Taiwan) and the Philippines. The US is the dominant exporter to the Philippines and Chinese Taipei, while Turkey draws supplies from all five major exporters as well as other sources.

Australia exports relatively little (or no) wheat to the four non-Egyptian north African importers (Algeria, Morocco, Libya and Tunisia), or to Israel and Nigeria. The US and the EU compete strongly for market share in North Africa, while the US supplies nearly all wheat imported by Israel and Nigeria.



Source: Calculated from International Grains Council 2000, *World Grain Statistics 1998-99* (and previous issues).

3.6.2. Size and stability of Australian market share

Australia exports wheat to many of the major Asian and African wheat importing countries, mainly in competition with Canadian and American wheat. The size and stability of its share in each market varies.

If Australia has a large share of a market, this may indicate that the importing country may have a definite preference for importing Australian wheat. However, if the importing country has shown by its past actions that it is willing to swap suppliers – presumably to obtain the best price or conditions – it may be harder to argue that it has such a preference.

Looking at other possibilities, a small but stable market share may indicate a market niche or definite preference for a particular type of Australian wheat. However, it would seem difficult to argue that Australian wheat has any unique advantage in markets where Australia’s market share is both small *and* unstable.

Estimates of market share and stability of market share may be calculated using IGC data on trade in wheat (origins and destinations). A reasonable indicator of Australian wheat market share may be wheat imports from Australia as a proportion of total wheat imports over the period examined, while the stability of market share may be indicated by some standard statistical measure of dispersion such as standard deviation. For comparisons across markets, it may be preferable for the latter to use a relative measure such as the coefficient of variation (the standard deviation divided by the mean). The interpretation of the indicator would be that the higher the calculated coefficient of variation, the more unstable the market share is likely to be, and vice versa.

In the period 1992-93 to 1997-98, Australia’s mean market share was 5 per cent or more in 18 of the 24 major Asian and African markets. In Table 3.7 these 18 markets are ranked from highest to lowest in terms of both market share and stability of market share, and then assigned to one of four possible quadrants.

Table 3.7: **Characteristics of Australian market share in Asia/Africa**

		Stability ^a	
		Low	High
Market share	High	Iran, India	Malaysia, Indonesia, Iraq, Thailand, South Korea, Japan, Yemen
	Low	Pakistan, Sri Lanka, South Africa, Bangladesh, China, Turkey, Philippines	Egypt, Chinese Taipei (Taiwan)

^a Stability – as indicated by coefficient of variation. A high coefficient is taken to indicate low stability of market share, and vice versa.

Source: Calculated from International Grains Council 2000, *World Grain Statistics 1998-99* (and previous issues).

Of the markets examined, those in which Australia obtained the relatively highest and most stable market shares were Malaysia, Indonesia, Iraq, Thailand, South Korea, Japan and Yemen. In Iran and India, Australia’s market share appears to be relatively large, but unstable. In Egypt and Chinese Taipei (Taiwan), market share appears to be relatively small, but stable. Finally, Australia’s wheat market share appears to be relatively most small, and least stable, in Pakistan, Sri Lanka, South Africa, Bangladesh, China, Turkey, and the Philippines.

Using the IGC data, it is possible to repeat the analysis conducted for Australia for any of the other major wheat exporters. Tables 3.8 and 3.9 detail such an analysis for Canada and the US, the two most likely alternate large suppliers to Asia and Africa of wheats similar to Australia’s. Canada and the United States both exported wheat to 22 out of the 24 largest Asian and African markets in the period 1992-93 to 1997-98.

Table 3.8: **Characteristics of Canadian market share in Asia/Africa**

		Stability a	
		Low	High
Market share	High	India	China, Iran, South Korea, Algeria, Indonesia, Japan, South Africa, Libya, Malaysia, Thailand
	Low	Philippines, Morocco, Turkey, Pakistan, Tunisia, Nigeria, Israel, Sri Lanka, Chinese Taipei (Taiwan), Yemen	Bangladesh

Source: See Table 3.7.

Table 3.9: **Characteristics of US market share in Asia/Africa**

		Stability a	
		Low	High
Market share	High	Sri Lanka, India, Bangladesh	Chinese Taipei (Taiwan), Nigeria, Philippines, Pakistan, Egypt, Israel, Japan, South Africa
	Low	Yemen, Tunisia, Morocco, Turkey, Algeria, Malaysia, Iraq, Indonesia	South Korea, Thailand, China

Source: See Table 3.7.

Those markets assessed as being ‘high market share, high stability’ from the respective viewpoints of Australia, Canada, and the US are set out in Table 3.10. Country order is based on average annual wheat imports. The Table may be useful as a point of departure for consideration of how other exporters may view their interests in any particular market, and therefore, how (and which) competitor may react to any attempt by Australia to increase its share in a particular market.

Table 3.10: ‘High market share, high stability’ markets, from the perspective of individual wheat exporters

	Average wheat imports a	Australia	Canada	United States
Egypt	6.5			▲
China	6.4		▲	
Japan	5.8	▲	▲	▲
Algeria	4.6		▲	
South Korea	3.9	▲	▲	
Iran	3.9		▲	
Indonesia	3.4	▲	▲	
Pakistan	2.5			▲
Morocco	2.2			
Philippines	2.0			▲
Yemen	2.0	▲		
Turkey	1.4			
Libya	1.2		▲	
India	1.2			
Bangladesh	1.1			
Malaysia	1.1	▲	▲	
Tunisia	1.1			
Iraq	1.1	▲		
Israel	1.0			▲
Chinese Taipei	1.0			▲
Sri Lanka	0.9			
Nigeria	0.9			▲
South Africa	0.7		▲	▲
Thailand	0.7	▲	▲	

a In million tonnes. Average 1992-93 to 1997-98. The symbol ‘▲’ indicates a ‘high market share, high stability’ market.

Source: Tables 3.7, 3.8 and 3.9.

One observation that can be made from Table 3.10 is that in many of the markets which Australia may regard as ‘high market share, high stability’ it is Canada, rather than the US, which appears to be the main large alternate supplier. Also, there are a number of the major Asian and African markets where neither Australia, Canada, nor the US appear to have maintained a relatively large and stable market share. These include Morocco, Turkey, India, Bangladesh, Tunisia and Sri Lanka.

3.7. Government involvement in Australian wheat marketing

The current wheat marketing legislation (the *Wheat Marketing Act 1989*, as amended) differs from previous legislation in that it is now solely concerned with the regulatory control of wheat exports by the WEA and provisions for the operation of the ‘single

desk'. Previously, dual regulatory and commercial functions were assigned to the former statutory Australian Wheat Board.

Commercial marketing and financing of the wheat crop are now undertaken by AWBI and other companies in the AWB Group. The NCP legislation review provides an opportunity to assess whether continued government intervention in Australian wheat marketing through the provision of the 'single desk' and export control is justified, and if so, what is the most appropriate form of intervention.

3.7.1. History of government involvement in agricultural product markets

'Orderly marketing' of agricultural products, backed by government legislation, has a long history in Australia. The Productivity Commission (2000) recently reviewed this history, drawing on Shann (1948), Sieper (1982), Watson and Parish (1982), Lloyd (1982) and Industry Commission (1991).

As noted in the Productivity Commission's staff paper, at the turn of the century, agricultural producers in several industries began to form state or regional cooperatives. These voluntary collectives, however, were susceptible to 'free riding' by non-members. In the crisis that followed the supply-driven collapse of prices in the early 1920s, state governments began to introduce arrangements in many industries to make membership of the formerly voluntary cooperatives compulsory.

The Commonwealth's ability to implement national price or production arrangements was limited by the need for agreement by all the states. However, its international trade and quarantine powers were used to control exports and imports of various commodities.

Fearing a collapse in world prices after World War II, producers in many industries embraced nationally-based statutory price stabilisation and marketing arrangements. These schemes guaranteed average producer returns by underwriting export receipts, (where the Government made up any shortfall in the stabilisation fund) and by setting domestic prices.

3.7.2. Formation of the Australian Wheat Board

The Australian Wheat Board was formed in 1939 to control wheat marketing during World War II. Its powers included a marketing monopoly for both domestic and export markets. After the war, growers lobbied for the continuation of these 'orderly marketing' arrangements.

In 1948 the Australian Wheat Board became a statutory authority backed by the *Wheat Stabilisation Act 1948* and complementary state legislation. The Act allowed for:

- compulsory acquisition and 'single desk' export and domestic marketing, and administered domestic prices (from 1953), allowing differential pricing across markets;
- a price stabilisation (buffer) fund supported by government subsidies if industry funds were exhausted; and

- pooling of sales revenue and marketing costs.

The principal objective of these arrangements (if not always their effect) was to increase producer returns. From the 1970s, however, the negative impacts of statutory marketing arrangements on resource allocation and industry efficiency and the attendant income transfers from taxpayers and consumers to producers began to receive more attention.

3.7.3. Evolution of Australian wheat marketing arrangements

Wheat marketing arrangements were reviewed at regular five year intervals, and new wheat marketing legislation enacted in the years 1979, 1984 and 1989. Each new Act contained various changes aimed variously at improving price signals to producers, increasing industry efficiency, freeing up parts of the domestic market, and reducing government exposure to payouts. The 1979 legislation's focus was changed from stabilising income to underwriting prices. Subsequently the AWB's focus turned to marketing wheat so as to maximise net returns to growers.

Fifty years after the formation of the original Australian Wheat Board, the 1989 legislation included provisions that:

- ended government underwriting of prices and deregulated the domestic market;
- allowed the AWB to trade in grain other than wheat, and to engage in value-added activities;
- terminated, in 1999, government guarantees of the AWB's borrowings to finance advance payments to growers delivering to its pools; and
- established the Wheat Industry Fund (WIF), to eventually become a capital base when the borrowing guaranty ceased.

Through the 1990s, wheat growers and the Government worked toward establishing a new commercial structure for the AWB. In 1997 the Government agreed to the establishment of a grower owned and controlled company to assume responsibility for wheat marketing and financing from 1 July 1999, when the Government guarantee of AWB borrowings was to cease. The *Wheat Marketing Amendment Act 1998*, transferred the former statutory Australian Wheat Board's regulatory export control functions to a new Wheat Export Authority, terminated government control over AWB Limited and its subsidiaries, and transferred the WIF and ownership of AWB Limited to growers.

Some question how much Australia's wheat marketing arrangements really have changed. There is still 'single desk' marketing of export wheat, and pooling of grower returns from export markets. On the other hand, there has been no government funding since July 1999, in either a direct or indirect sense, apart from government contributions towards the costs of research and development. Nor is there legislative control of AWB Limited's marketing, pooling and financing operations. Finally, shareholders now provide the capital base for the grower owned and controlled company, and bear the risk of commercial operations.

3.7.4. Issues in wheat marketing

With up to 80 per cent of Australian wheat being exported, the marketing arrangements for export wheat may have the potential to impact on the domestic market for wheat, on the market for other grains, and on the service industries such as grain handling, storage and transport. It is relevant, therefore, to examine the issues underlying past government involvement in wheat marketing.

Some of the perceived issues the creation of a statutory marketing authority for wheat was intended to address included:

- falling or fluctuating wheat producer incomes (and later, any sharp, unexpected decline in prices);
- unsatisfactory producer access to markets, marketing services, and grain storage, handling and transport services;
- lack of individual producer bargaining power on world markets;
- poor grain handling, storage and transport infrastructure, leading to high grain wastage and poor quality control;
- growers' desire for greater control of the marketing chain;
- the need to compensate agricultural producers for the impact of manufacturing tariffs; and
- the need to develop Australia's agricultural industries.

However, over the last decade the grains industry has recognised that many of these matters were better addressed by commercial rather than statutory means. On the other hand, there remains a strong perception that 'single desk' selling on export markets offers substantial benefits to growers. Australian wheat producers have perceived they lack bargaining power in export markets. This vulnerability is further exacerbated by the fact that most of their export markets are in countries in which the Australian government has little direct power to assist them if they were to try to sell into these markets as individuals. 'Single desk' selling has been seen as a means of remedying this perceived lack of bargaining power by having one organisation:

- aim for economies of scale, by acquiring the whole crop;
- gather, and disseminate, market intelligence on growers' behalf;
- facilitate government-to-government sales of wheat;
- administer exports to markets where quantitative import restrictions are imposed by foreign buyers;
- undertake generic market promotion of Australian wheat; and
- control the quality of export wheat, ensuring Australia's good market reputation is maintained.

As export markets represent the largest destination of Australian wheat, both growers and governments have been concerned that new export markets be developed, and that the reputation of Australian wheat in these markets be maintained. The Australian Government is also concerned to satisfy Australia's international obligations under world phytosanitary agreements, which prohibit the export of plant and animal pests and diseases and to ensure that the various chemicals used to control pests and diseases and how they are used on farms, in farm storage, and in the central storage and handling system, do not breach domestic and international regulations. Many

grain importing countries specify imported grain must be free from pests and chemicals, and both growers and governments view the current system (under which export wheat is marketed by only one seller) as being able to ensure that Australian wheat meets such expectations.

Governments also have been generally supportive of industry initiatives which may increase export returns. Many government export promotion programs over the years have been explicitly aimed at promoting exports of Australian product. Again, the activities of a 'single desk' seller for wheat have been seen as useful in this role.

3.8. Summary

3.8.1. Wheat is grown widely across Australia

Wheat is the most widely grown field crop in the five mainland states. Therefore, whatever export marketing system is adopted will affect growers in all the states, particularly in Western Australia and South Australia, which have a relatively high dependence on export wheat.

3.8.2. Australia's wheat area and production are variable

Australian wheat area and production is currently at record or near-record levels. But it should be borne in mind that some of the reasons for the recent interest in wheat include the spike in wheat prices in 1995-96 (now well past), the relative weakness of livestock product prices, and the high yields being achieved with wheat. Wheat area and production has reached high levels in the past (for example, in the late 1960s and the early 1980s) but has then declined. Therefore, whatever export marketing system is adopted will need to handle, and export, not just large but also small crops.

3.8.3. Financial performance of crop farms does not depend on region

Adding weight to 3.8.1 from an examination of ABARE survey data for Australian broadacre farms, it is apparent that the physical and financial structure of crop farming operations are broadly common across Australia. That is, what seems to influence farm financial performance most is the scale of operation and the skill of the operator, rather than the region in which the operation is located. Thus, there would not seem any particular need to try to segment the marketing system or tailor it only for particular regions – a national approach should suffice.

3.8.4. The bulk of crop production comes from a relatively small number of farms

Another conclusion to be drawn from the ABARE survey data is that the bulk (just over 60 per cent) of the nation's crop receipts are generated from just 14 000 crop-specialist farms. While not playing down the valuable contribution of the small or occasional wheat grower, it should be borne in mind that if industry output and value of output is to continue to increase, the export marketing system should not hold back innovation by the relatively small number of crop-specialist producers who produce the bulk of the crop.

3.8.5. Domestic wheat market deregulation apparently helped boost domestic wheat use

An examination of Australian wheat supply and demand data for the past decade reveals that wheat use by the domestic market has grown significantly over the 1990s. While it has not been conclusively demonstrated that the market growth resulted from the increased opportunities for direct wheat producer and domestic wheat user interaction following the deregulation of the domestic wheat market in 1989, this deregulation is now generally acknowledged to have had a positive effect on the industry. Thus the question may be asked if there may not be a similar positive impact on the industry from more direct wheat producer and export wheat user contact.

3.8.6. Durum and bread wheats – are they different products?

Durum wheat production (initially in New South Wales and now in South Australia and the other states) has grown to the point where an exportable surplus is now regularly being produced. It needs to be seriously considered, when discussing export wheat marketing, whether durum is a sufficiently different product from bread wheats to contemplate a different marketing system for durum, if this is what durum growers want. As just one illustration that durum and bread wheats are different products, an examination of movements in world indicator prices for durum and bread wheats reveals that there is no more correlation between price movements for these products than between, say, bread wheats and corn (maize).

3.8.7. Australia does not appear to have sufficient market share in the world market as a whole, or in any key wheat importing region, to have much power to influence other wheat exporters' policies

Australia is one of five major world wheat exporters. Australia's wheat export marketing arrangements need to maintain an awareness of the policies of these other exporters. However, with a long term wheat market export share of no more than perhaps 15 per cent, it appears very doubtful whether anything Australia does in the market would have much impact on the other exporters' policies - however these other exporters' policies may be perceived to be negatively impacting on Australia's wheat industry.

3.8.8. In Asia and Africa, Australia faces strong competition from the United States, Canada, and the European Union

Australia's export wheat marketing arrangements also need to take into account the characteristics (both buyers' demand and exporters' supplies) of the main regions into which Australia sells wheat. The bulk of Australian wheat is sold into Asia and Africa, but Australia does not have a dominant market share in either of these regions (Australia's market share is 24 per cent in Asia, and 6 per cent in Africa). In Asia, Australian wheat is sold in direct competition with Canadian and US wheat, and in Africa (particularly north Africa), EU wheat adds further to the competition. Australia has a large market share in the Oceania region, but the amount of wheat imported by this region is very small relative to that imported by Asia or Africa.

3.8.9. *Australia's average unit export return for wheat does not appear to have been any different from those obtained either by Canada, or the United States*

Movements in quoted prices for ASW closely follow those of comparable US export wheats. Over the 1990s the asking price for ASW has been progressively shifted upwards relative to the price quotations for these American wheats. However, there is little evidence that this upward re-positioning has been reflected in higher actual realised export returns. In fact, an examination of wheat export volume and value data supplied by national governments to the FAO reveals no statistically significant difference between the average export unit values for Canadian, Australian, and US wheat over the decade of the 1990s.

3.8.10. *Australia has a large presence in some of the major Asian and African markets, but little presence in others*

In Asia and Africa, in the 1990s, Australia has had a strong market presence in the three largest wheat importers (Egypt, China and Japan), and a large market share in many middle-ranking importers such as Indonesia, Iran, and South Korea. There are, however, some large importing countries where Australia has had little market presence to date. Whatever export wheat marketing system is adopted will need to be flexible enough to ensure potential access to the widest possible range of markets.

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4. STAKEHOLDER VIEWS

This chapter summarises the views expressed to the Committee by stakeholders in their meetings and submissions. While space does not permit discussion of every meeting and submission, the Committee has drawn extensively on individual communications to synthesise the main themes and ideas discussed in this chapter.

Key sections in chapter:

- Who was consulted
- Companies and organisations
- Government and research
- Farm partnerships and private individuals
- Overseas consultations

4.1. Who was consulted

The emphasis of legislation reviews is on community-wide benefits. As stated in the guidelines for NCP legislation reviews (CIE 1999):

‘If legislative restrictions on competition are to remain, it must be demonstrated that there are benefits to the Australian ‘community as a whole’ – not just benefits to vested interests or regional interests’.

These guidelines specify groups and interests which may need to be considered, including:

- those likely to be most directly affected by any changes, such as producers, traders, processors, wholesalers, retailers and consumers;
- those likely to be indirectly affected, such as input suppliers, other industries and other community groups; and
- wider community interests such as environmental concerns, health and safety issues, and international relations.

All interested parties should be given genuine opportunities to contribute to a review.

In seeking stakeholder views, the Committee invited stakeholder submissions through advertisements in national and regional newspapers, and provided an issues paper to assist stakeholders in preparing submissions. The Committee also conducted private meetings and open forums in wheat belt towns, met in capital cities with other key stakeholders, and while overseas, met with customers, international traders, foreign government officials, and other organisations involved in the wheat trade.

By the deadline of 17 July, the Committee had received over 3 300 submissions. The Committee undertook to make all submissions available once the draft report was released, except those presented ‘in confidence’ or subsequently withdrawn.

Note that the use of organisation names to identify submissions in this chapter is done for clarity and should not be taken to indicate the Committee has any view on the authority of any person to make a submission on behalf of that organisation, or on how representative the submission is of the collective view of its members.

4.2. Companies and organisations

4.2.1. *AWB (International) Limited*

AWB (International) Limited (AWBI) is the AWB Limited subsidiary responsible for the export wheat pools. As ‘nominated company B’, AWBI is not required to obtain a permit from the Wheat Export Authority (WEA) for the export of bulk wheat from Australia. The submission made on behalf of AWBI argues that the current legislation should be retained in its current form, as it provides a net benefit to the Australian community and is the only effective means of achieving the objectives of the *Wheat Marketing Act 1989* (WMA) (AWBI 2000).

The submission argues that the ‘single desk’ benefits growers through:

- the opportunity to take wheat out of being a commodity to a branded differentiated food product, which assists in obtaining a premium for Australian wheat, both in dollar terms and via market access;
- strong integration in the marketing chain, allowing AWBI to provide and guarantee overseas customers with a consistent product they demand throughout the year, year in year out;
- ensuring the grains industry is customer driven rather than production driven like some international competitors, resulting in increasing stockpiles of wheat;
- utilising a superior negotiating position to capture access to a wider range of overseas markets;
- gaining an overall price premium of A\$8.72 per tonne resulting in higher returns to growers who deliver to the National Pool;
- enabling a national approach to marketing and brand promotion improving Australia’s reputation for producing a high quality product with a superior international reputation for quality and reliability of supply;
- increasing Australia’s exports of wheat from 13 million tonnes to 18 million tonnes in the last decade, while world trade has remained static at around 90-100 million tonnes and while stocks increase to near record levels in exporting countries;
- guaranteeing access for all Australian wheat growers to the international market.
- Ensuring all growers have an opportunity to sell their wheat, as AWBI is required to receive all wheat that meets established quality standards;
- establishing National Pools to the benefit of all growers;
- assisting Australia’s wheat export industry performance in an environment where government subsidies grossly distort international markets;
- providing efficient risk management to all growers across time and markets;
- maximising financial returns to growers who deliver to the National Pool, as required under AWB Limited and AWBI’s constitution;

- developing the quality profile of the Australian wheat crop through industry initiatives such as 2x10x2000 and the Golden Rewards national payment scales for quality;
- providing a national approach to consistent customer focused priority setting for research and development across the industry;
- ensuring long-term quality control of Australian wheat through clear market signals and appropriate pricing structures which reflect quality;
- generating cost efficiencies in wheat freight, storage and handling;
- assisting other exporters whose activities complement those of AWBI to sell into niche markets; and
- recognising that most customers express a clear preference for dealing with a farmer owned centralised marketing body (eg. China, Japan, Iran, Iraq, Pakistan and Sudan).

The submission also argues that the ‘single desk’ does not impact adversely on the domestic market for wheat, stating:

- the domestic market for wheat is fully deregulated and economic analysis indicates there is no distortion of the domestic market caused by the ‘single desk’ export arrangement;
- if the ‘single desk’ returns a higher price to growers and domestic buyers buy at the export parity price, the removal of the ‘single desk’ will then subject the domestic market to the direct volatility of the international market;
- domestic buyers have ready access to large wheat stocks through the AWBI pools, and may also benefit from the pools’ effect in stabilising domestic wheat prices and in maintaining the general quality of Australian wheat;
- there is no correlation between the price consumers pay for end products and the price of domestic wheat; and
- the price of feed wheat for the domestic feed sector is affected much more by general supply of domestic feed grains than by the operation of the ‘single desk’. Feed wheat received into the AWBI pool would only be exported if it was produced in an area divorced from local consumption demand.

The submission suggests some of the more general benefits to the community are:

- growers own and control the organisation which operates the ‘single desk’, so any benefits from its operations are returned to growers through the national pool;
- participation in the national pools enables growers access to a significant cash flow in advance of physical sales of wheat; and
- many regional communities are underpinned by the farming businesses which grow wheat, and the cash flows generated by these businesses.

4.2.2. Grains Council of Australia

The **Grains Council of Australia** (GCA) is the peak body of the Australian grains industry. The council’s member and associate member bodies consist of the farmers’ federations and associations in the six Australian States. The submission argues that to remove the ‘single desk’ would weaken Australia’s position in the international market, reduce grower returns and overall economic activity, negatively impact on rural and regional Australia, and reduce Australia’s export earnings (GCA 2000).

The submission argues that the benefits to Australian wheat growers and the Australian community from the 'single desk' export arrangements significantly outweigh any costs. The arrangements are seen to provide:

- price premiums for Australian wheat in the international market, which are passed back to growers;
- market information, crop financing and other services to growers;
- cost savings from the economies of scale and scope generated by AWBI's large throughput;
- employment opportunities in regional areas due to the services required by wheat growers;
- promotion of wheat breeding and the development of varieties suited to the customer requirements;
- the ability for AWBI to operate successfully in international markets; and
- manage payment risk and exchange rate risk on growers' behalf.

Regarding the latter, the 'single desk' is seen to allow AWBI to:

- effectively coordinate and manage the complex logistics involved in delivering wheat to international markets;
- develop brands of wheat suited to specific customers;
- invest in promotional activities and processing facilities in markets where the demand for wheat is growing, then return the profits to Australian growers;
- maintain tight quality control and high quality standards over Australian wheat sold internationally;
- develop long-standing and solid relationships with overseas customers;
- enforce compliance with signed contracts, backed by the credible threat of non-supply; and
- possess the 'critical mass' required to compete effectively in international markets.

The submission considers the argument that the legislation may impose costs on domestic wheat users and non-AWBI wheat exporters, but argues that:

- the domestic market for wheat, deregulated in 1989, is very competitive;
- many of the companies involved in the processing industries also operate in the domestic market as buyers in their own right; and
- many small wheat traders successfully export wheat in containers using the current export permit system.

4.2.3. State farmers' federations

The Committee received submissions from farmers' federations and associations in the five mainland wheat-growing States. The submission made on behalf of the **New South Wales Farmers' Association** (NSW Farmers 2000) argued the 'single desk':

- obtains premiums from the international marketplace and returns these to growers;
- allows AWBI to operate as a 'buyer of last resort';
- is attuned to the needs of overseas customers;

- provides incentives to growers to increase their quality through a combination of incremental payments and segregation of grades;
- provides a single set of consistent quality standards for the export crop;
- has allowed the development of overseas markets and returned the benefits to Australian growers;
- enhances AWBI's reputation as a reliable supplier, despite Australia having one of the most uncertain production climates in the world; and
- is the basis for a system of marketing based on branded products.

The submission made by the **Victorian Farmers Federation Grains Group** (VFF 2000) supported the 'single desk' marketing of wheat through AWBI. The submission argued that the 'single desk' ensures reliability of supply, efficient and effective marketing. This ensures AWBI is able to:

- maximise grower returns, thereby maximising returns to their rural communities;
- offer services to growers such as international market forecasts, decreased freight costs, multiple segregations and secure seasonal funding;
- ensure market development through investment in national and international projects, also ensuring the benefits from these projects return to growers and their local communities;
- maintain the quality of Australian wheat from receipt site through shipping to end user;
- secure a 'critical mass' of product which gives them negotiating power to ensure an equal footing when dealing with large 'single desk' buyers and private traders in the world market;
- accumulate enough wheat across a large variety of grades and markets to meet overseas customer requirements;
- efficiently collect and utilise world market information; and
- coordinate the logistics of handling wheat the year round.

The submission made on behalf of the **South Australian Farmers Federation** (SAFF 2000) by that organisation's Grains Council argued that the 'single desk' delivers price premiums and enhanced services to Australia's wheat growers, enabling them to market their product at minimum cost, and to maximise the returns they receive. The system assists growers to sell their wheat efficiently into the 'highly distorted' international market, and allows the industry to:

- generate cost savings through economies of scale and scope;
- effectively coordinate its logistics;
- develop overseas markets for its products;
- capitalise on its high reputation for quality; and
- develop long term relationships with customers.

The submission made on behalf of the **Western Australian Farmers Federation** submission (WAFF 2000) saw the issue of distortion in international markets as being of particular importance to Western Australia, which exported 95 per cent of its wheat crop. The 'single desk' was seen as the most efficient way of marketing wheat into export markets and ensuring that growers' profits were not 'captured by middlemen or foreign owned multinational trading companies'. The submission pointed out that

AWB Limited is now privatised and owned by its grower shareholders, ensuring that the profits generated by the company are returned to growers.

The submission made on behalf of **AgForce Grains** (the successor to the Queensland Grain Growers Association) argued that ‘single desk’ exporting ensures:

- export customers receive grain of consistent quality;
- the ‘critical mass’ needed to market Australian grain internationally;
- effective development of foreign markets;
- market reputation and relationships are maintained; and
- the benefits are returned to farmers and their communities.

The submission also argued that while Australia relies on the export market to sell its grain, this market ‘is dominated by corrupt and trade distorting practices of many different governments’. The ‘single desk’ provides the ability to successfully compete in such a marketplace (AgForce Grains Ltd 2000). AgForce emphasise the long-term consistent support that growers have of retaining the current wheat export ‘single desk’ system.

4.2.4. Farmer cooperatives and associations

The Committee received submissions from a number of farmer cooperatives and associations in the wheat-growing States.

The submission made on behalf of **Grain Growers Association Limited** (formerly Prime Wheat Association Limited, and a major shareholder in the bulk handling company GrainCorp), argued that AWBI’s requirement to receive all wheat delivered gave all growers the opportunity to export their wheat irrespective of their location, or seasonal vagaries. However, the current arrangement lacks an independent process for determining grain quality and varietal standards. Also, there was limited power to ensure that the domestic grain industry is competitive from farm to export position, and no facility for third party review of export market development. The submission suggested an enhanced role in these areas for the WEA, particularly to assist in establishing independent national grain quality standards and to monitor AWBI’s performance in maximising grower returns for both premium, and feed, quality wheat (Grain Growers Association Limited 2000).

The submission made on behalf of **PGA Western Graingrowers**, the grain commodity group of the Pastoralists and Graziers Association of Western Australia, argued that the ‘single desk’ of AWB Limited is a buying monopoly, not a selling monopoly, as there were many sellers of wheat on the world market but effectively only one buyer of wheat for Australian wheat growers. The submission argued there was no proof the current system obtained any premium returns. It also stated the current arrangements act to:

- increase costs in the logistics chain between the farm gate and port;
- disrupt the free flow of information;
- limit the opportunity for pricing and hedging;
- suppress innovation; and

- deny individual growers and groups the freedom to develop their own skills, knowledge and ability to market their own produce successfully. (PGA Western Graingrowers 2000).

The submission made on behalf of the **Durum Wheat Growers' Association (NSW)** (DWGA 2000) argued that prior to 1993 the durum industry has been basically a domestic market with contracts between growers and millers. However, after 1993, there was a significant surplus to domestic requirements. Growers are aware of export markets which offer better prices, but have been frustrated in their attempts to export by the Australian Wheat Board. In 1999 there was a serious dispute with the new AWB Limited over pool prices and receival standards for fungal stained grain and, as a result, there has been a loss of confidence in durum growing in northern New South Wales and southern Queensland. The submission suggested the WEA should have the power to issue export permits independently of AWB Limited, and that if durum growers were satisfied with AWB Limited's performance, that organisation would not require monopoly export powers to accumulate and market durum. The submission also suggested the current arrangements might distort the domestic market for durum, stating the AWB Limited 'is a price and quality setter' in the Australian domestic durum market.

The submission made on behalf of **Netco Grain Cooperative Limited** (2000), a grouping of farmer cooperatives, argued that:

- greater transparency and accountability is required from AWB Limited in the conduct of the export monopoly and from the WEA in granting export permits;
- cooperatives are currently denied the opportunity to expand any niche markets they develop;
- risk management via AWB Limited is limited since due to the volume of wheat it received, not all is able to be hedged;
- there are unnecessary limitations on the basis pool and lack of transparency on how the basis is arrived at; and
- more competition is needed in the storage, handling and financing of wheat to reduce costs from farm gate to fob.

The submission made on behalf of **Capgrains Cooperative Associated Grains Limited** (2000) based in central Queensland (and a Netco member) argued that the 'single desk' status of the AWB Limited should be removed, because:

- grower groups such as Capgrains were unwilling to invest in developing markets for specialised wheats only for the market to be 'captured by the AWB';
- most central Queensland grain is exported, but the AWB's basis pool failed to provide many growers with a satisfactory means of forward pricing their wheat;
- the AWB itself was restricted in its ability to forward price using the CBOT; and
- there was no competitive pressure on AWB Limited costs.

The submission made on behalf of the **Western Australian Noodle-Wheat Growers' Association** (WANGA 2000) argued that an orderly deregulation of wheat marketing should commence starting with the Japanese noodle-wheat market and that growers be allowed to market their own grain as well as develop niche marketing opportunities through a more competitive marketing system.

WANGA has built its submission around experiences and examples of the group's efforts to develop noodle-wheat markets in Japan and has identified major shortcomings of the former Australian Wheat Board and the monopoly marketing system.

WANGA's call to have the 'single desk' removed is based on its claim that both growers and markets 'are held hostage to the monopoly by compulsion and as a result growers are frustrated and the markets restrained and in some case under developed'.

The submission made on behalf of **Pea Growers Co-operative Ltd (PeaCo)**, a cooperative marketer of pulses (grain legumes) and Netco member, argued that the possession of an export monopoly in one grain gives a major competitive advantage to the holder in the trading of other grains (PeaCo 2000).

The submission made on behalf of **Shepherds Producers Co-operative Limited** (2000), a Netco member, argued that AWB Limited's diverse activities on behalf of producers such as hedging, forward selling and a longstanding international presence provided advantages to growers. However, the submission argued that as the niche market for specialty wheats was growing, producers required assurance of reasonable and cost effective access to these markets.

The submission made on behalf of **Walgett Special One Co-operative Limited** (WSOC 2000) stated that its membership had increased appreciably over the past four years due to the successes and value that WSOC has created for growers and the dissatisfaction with the level of service provided by AWB Limited. The submission argued that under current arrangements:

- if AWBI does not run a pool for a particular grade, growers are not able to access the international market for that grain, and may have to deliver into another pool at a significant discount;
- full price risk management cannot be undertaken;
- access to international pricing is restricted;
- markets cannot be accessed in an efficient manner;
- cost paths are not minimised;
- the avenue for appeal if an export permit is rejected is considered to be onerous;
- value is not retained by the original producers and those who actually generate this value;
- AWBI have imposed additional restrictions beyond the WMA, in the form of the 'ticket by ticket' policy; and
- the WMA in its current form does not encourage innovation or entrepreneurialism as benefits from such activities are socialised across a national pool.

4.2.5. State-based marketers and bulk handling companies

The Committee received submissions from a number state-based grain marketers and bulk handling companies.

The submission made on behalf of the **Grain Pool of WA** (2000) stated the Grain Pool supported the retention of existing arrangements for the bulk export of regulated

grains ‘to facilitate orderly marketing in highly competitive export activities’. The submission noted that a recently-finalised National Competition Policy (NCP) review of Western Australia’s Grain Marketing Act had recommended the State’s ‘single desk’ arrangements for exports of barley, lupins and canola be retained. Regarding the export of grains in containers (non-bulk exports), the submission argued that following the deregulation of domestic grain markets, the export of grains in shipping containers had increased, and that the removal of all restrictions for the export of containerised wheat from Western Australia would bring economies of scale to containerised wheat and provide a basis for the lowering of costs and the expansion of containerised exports of wheat, lupins, barley and canola. This would also make wheat comparable to containerised exports of lupins, barley and canola from Western Australia.

The submission made on behalf of the **Australian Bulk Alliance Pty Ltd (ABA)** (formed in July 1999 as the joint venture between Grainco Australia Limited and South Australian Cooperative Bulk Handling Limited to develop and operate new bulk commodity facilities in Victoria and New South Wales) argued that by trying to control the supply chain from silo to the fob position, AWB Limited was not allowing the system to operate at maximum efficiency for all grain growers (ABA 2000). The submission stated that the ABA was in favour of an industry structure where AWB Limited concentrated on its most important task, marketing Australian wheat onto the world market. ‘The AWB should receive this wheat fob and allow the efficiency gains that would come through true competition in domestic logistics’.

The submission made on behalf of **Grainco Australia Limited** (2000), a grower-owned bulk commodity logistics and trade facilitation company, supports the continuation of the wheat export monopoly and AWB Limited’s role in marketing export wheat to prescribed markets, provided AWB Limited adheres to the primary objective in its constitution of maximising returns to growers.

The submission argues that there may be benefits derived by the ‘single desk’ seller status for the export of Australian wheat. However many practices of AWB Limited appear to be reducing grower options and stifling innovation within the grains industry. It argues that the refocussing of the AWB Limited on being a ‘best practice’ export marketing business and its withdrawal from the domestic market and interior logistics market would encourage competition, innovation and promote efficiency gains through lowered logistics costs that would deliver supply chain savings for producers.

The Grainco Australia submission also argues that the two AWB Limited objectives of maximising returns to growers who deliver wheat to the national pool and maximising returns to commercial shareholders potentially conflict. Under the current structure, the bulk of AWB Limited income is derived by providing non-contestable services to the national underwritten pool, so AWB Limited has an incentive to try to maximise pool tonnage to the pool and preclude others from providing lower priced services to growers.

The submission contended that the only export markets that should remain exclusive to AWB Limited are those where a premium price can be achieved. The WEA should

be permitted to operate the ‘single desk’ and allow additional competition into non-premium markets through the issue of export permits.

The submission made on behalf of **GrainCorp Operations Limited**, which operates grain storages in country New South Wales and export terminals at Port Kembla and Newcastle, argued that AWB Limited is able to use the ‘single desk’ to leverage financial advantage in selling wheat into the international market, and in the provision of domestic services to AWBI (GrainCorp 2000). But while obtaining a monopoly premium from the international market creates a net benefit for growers and the Australian economy, obtaining a monopoly premium from the deregulated domestic market and the grain supply hinders the ability of the domestic wheat market and the grain supply chain to provide the best service and cost package to growers.

The submission made on behalf of **Vicgrain Limited** (2000) argued that the ‘single desk’ enables AWBI to regulate the quality and supply of Australian wheat to extract premiums from international markets. However, it was claimed that AWB Limited is manipulating supply chain prices and charges, and using the export pool to cross-subsidise its own grain handling activities. The submission suggests changing the point where regulation is applied from the original classification ticket as grain is received to the port terminal, and requiring AWB Limited to purchase wheat in the fob position, as the Canadian Wheat Board does in Canada. ‘This would not jeopardise the ability to market grain internationally, would remove the potential for cross subsidisation, and hence provide the financial benefits and efficiency gains that producers are seeking’.

4.2.6. Joint Industry Submission Group

The submission made on behalf of the **Joint Industry Submission Group** argues that there are less restrictive and more efficient ways to deliver the intended benefits of the legislation, as well as additional benefits for the Australian community (JISG 2000). The submission argues that in order to pass the ‘net public benefits’ test, proponents of the existing restriction need to demonstrate that:

- AWBI has market power in major markets and is using this power as a price discriminating monopolist to achieve a higher average export return from all pool wheat sales, compared with a competitive market system;
- costs to growers and other sectors of the community are not higher; and
- there are no other alternative, less restrictive ways of achieving the implicit objectives underlying the legislation.

The submission examines the argument that having a single seller of Australian wheat allows the seller to secure a higher average price from export sales than if there were many sellers, but concludes the conditions required for such a strategy to be successful are unlikely to exist for Australia. It also illustrates why an observed ‘price premium’ does not necessarily prove either the existence of market power or that higher average export returns are being obtained.

The submission suggests there are in fact no demonstrable net public benefits and several alternative ways of achieving apparent objectives. Rather than having no regulation, however, the strong points of the current system should be maintained by

appropriate regulation. AWBI would likely would remain as a major player, but growers would have the choice of a number of buyers and pools rather than just the national pool for export wheat.

Regarding the grain supply chain, the submission suggests that the introduction of greater competition may result in cost savings and higher net returns to growers of up to \$5 per tonne or more. On pooling, the submission argues that pooling restricts growers' capacity to manage their own price risk, leaving growers individually exposed to falls in the pool price, even though the pool is hedged to a degree. The pooling system has prevented the establishment of effective risk management markets in Australia. If pool managers set conservative prices early in the season and around harvest, this sets a low benchmark for domestic market prices, to the potential disadvantage of growers selling for cash or forward into the domestic market. Any advantage this may confer on domestic grain-using industries may disappear later in the season when supplies are tight, and AWB Limited is the only market player with stocks.

The submission argues the need for an independent body or mechanism for some of the regulatory tasks previously performed by the former statutory Australian Wheat Board, such as setting wheat breeding directions, registering new wheat varieties, classifying wheat types and assigning new varieties to particular categories, setting receival standards and tolerance limits, testing and certification of quality specifications for export wheat, and control of market information. It also suggests alternative export marketing arrangements be considered, such as allocating only specified markets to AWBI and allowing private traders to access the rest, or establishing an independent licensing authority to sell export quota by tender or auction to test the extent and value of any market power.

4.2.7. Grain trading companies

The submission made by **Cargill Australia Ltd**, a subsidiary of Cargill Incorporated, argued that most of the small number of government-regulated buyers which once dominated the import side of global grain trade are now gone, replaced by a large number of private importers (Sims 2000). Competition, the submission argues, reduces costs, spurs innovation, and provides openness and transparency in markets. Regarding farmer management of price risk, the submission mentions Cargill's revenue assurance contract for US maize growers (Performance 90) which, in providing upward price adjustments to farmers whose revenue drops more than 10 per cent from the level anticipated at the time the contract is signed due to declines in either yield or price, is stated to guarantee per hectare revenue will be at least 90 per cent of what had been expected. The submission also mentions Cargill's 'A+' contract in North America which is stated to guarantee growers the average price established in specified public markets, plus the opportunity to earn more if Cargill's hedging efforts achieve higher than average prices. As an example of innovation, the submission mentions the joint venture internet-based marketplace recently established by Cenex Harvest States, DuPont and Cargill for farmers in North America (Sims 2000).

4.2.8. Domestic wheat users and processors

The Committee received submissions from a number of domestic wheat users, including flour millers, stock feed manufacturers, and intensive livestock feeders.

The submission made on behalf of the **Flour Millers' Council of Australia**, an industry association representing flour milling companies in Australia, stated that:

- the majority of members on balance support the retention of the 'single desk' for export marketing of Australian wheat;
- a 'single desk' AWB Limited must not invest in cereal food processing in Australia;
- Australian millers want the ability to accumulate and export bulk wheat to their own mills in New Zealand and Papua New Guinea;
- a strong AWB Limited presence in the market assists domestic millers to achieve their requirements regarding access, supply and quality - however, a monopoly may put AWB Limited in too dominant a position, with little recourse on abuse of market power within the domestic market;
- access to pool wheat needs to be more flexible – the Pool Tender System has not worked; and
- millers are concerned that access to the wheat varieties for which the AWB Limited has commercialisation rights may be restricted if the AWB Limited were to lose its 'single desk'

(FMCA 2000).

The submission made on behalf of **Aust Farm Grain** (AFG) stated that AFG has been able to attract previously disinterested grain processors in South East Asia via reduced container freight rates into the region (AFG 2000). With increases in production capacity, some of these processors now required more wheat than was able to be supplied in containers. However, applications to the WEA for bulk export consent had failed. At times, AFG had been unable to meet customer demand for grain of particular grain quality and quantity and had made bids to AWB Limited for bulk wheat. However, none of these bids had been accepted, even though the offers were made when the AWB Limited was holding large stocks of wheat and selling wheat on the export market at below AFG's bid prices.

The submission made on behalf of **Goodman Fielder** (2000) saw no need to disband AWB Limited's 'single desk' status. However, the submission raised a number of issues with the current structure and operation of AWB Limited and the WEA:

- the WEA should operate as a statutory authority independent from AWB Limited intervention, which to date has forced exporters to export in containers, causing inefficiencies in the supply chain;
- the offshore markets of strategic importance to AWBI should be scheduled, and AWBI should not have a right of veto for bulk wheat shipments to those not considered strategic;
- New Zealand, Papua New Guinea and the Pacific Islands should not be scheduled markets as the amount of Australian wheat exported to these markets is small and the main flour and feed millers are Australian based companies wishing to access Australian wheat;

- AWB Limited's Pool Tender System, through which domestic users can access pool wheat stocks, allows AWB Limited to exercise undue market power, which is also evident in the conduct 'pool swaps' and sales of wheat for export flour, and
- AWB Limited is able to use its operation of the export pool to impose policies such as 'active stack management';
- AWB Limited should give more consideration to domestic wheat consumers (customers) when determining quality and logistic issues;
- the AWB Limited Pool Tender System does not in reality allow domestic consumers access to pool wheat post harvest; and
- the WEA should have a membership representing a broader constituency than at present.

The submission made on behalf of the **Chicken Meat Industry** (Larkin 2000) argued that the Australian export and domestic grain markets are closely interrelated, and any assessment of the benefits and costs of retaining the current arrangements should take this into account. Feed costs are of importance to the competitiveness of Australia's intensive livestock industries, and Australia's domestic feed costs needed to be reduced to at least international benchmark levels.

The submission made on behalf of the **Pork Council of Australia** (2000) argued that the 1990s were a decade of dramatic marketplace change for the pork industry, with revised regulatory regimes opening traditional domestic markets to aggressive competition from imports, while regulations affecting feed grain supply remain restrictive. From the industry's point of view, the main impacts of wheat market regulation are:

- increased feed costs, which reduces the competitiveness of Australian pig meat products in Australian and export markets;
- loss of pig production and processing viability when wheat and other grain prices 'spike' under current regulatory arrangements; and
- piggery decline, closure or non-development due to this risk and to distorted market messages, with loss of high-multiplier effects through a value-adding chain from regional farming to processing and export.

The submission argues for balanced change in line with NCP principles to ensure that Australian wheat users, such as the pork industry should never have to pay more for Australian wheat than overseas competitors. It argues that there are costs to the Australian community and consumers as a whole and regional areas particular, through distorted marketplace messages that encourage marginal wheat and grain production and deter some investment in higher value-adding intensive livestock production and processing, as well as specialised feedgrain supply.

The submission made on behalf of the **Confederation of Australian Pork Exporters** (CAPE 2000) argues that pig production is highly sensitive to grain prices, in that feed grains represent some 60 per cent of the cost of production. Access to wheat at export parity prices is vital to the success of the pig industry and its associated industries. The industry is now directly exposed to both import and export competition with foreign producers having the advantage of export parity priced grain. Indeed, the recent recovery in the Australian industry and its future viability are both directly tied to success in export markets. Therefore, any new regulatory

arrangement should provide for export parity pricing for domestic buyers, and support for re-sale into Australia of Australian wheat purchased by overseas buyers.

4.3. Government and research

The Committee also received submissions from a number of government authorities and research organisations.

4.3.1. Wheat Export Authority

The submission made on behalf of the **Wheat Export Authority** (WEA) noted that under the WMA, one of the functions of the WEA is to monitor, and report on the performance of AWBI, and the benefits to growers that result from that performance (WEA 2000). The WEA is establishing a performance monitoring network which in the first instance will analyse and assess:

- AWBI power to change domestic and export quantities to maximise returns from different markets;
- logistics efficiency, business and operations performance; and
- overall business performance.

The WEA noted that in considering applications seeking to export wheat, the WEA's own guidelines required it to take into account whether granting the permit would jeopardise sales achieved, or premiums obtained, by AWBI in the relevant market, and whether granting the permit would adversely affect the prevailing export marketing strategies of AWBI. Specifically, the WEA may consider:

- the value of the relevant market and the extent of the AWBI sales to that market over a reasonable period of time;
- the quality profile of wheat in the relevant market;
- the reasonable potential for consented exports to adversely affect the price or quality of wheat being supplied by AWBI to the market in question;
- any long term agreements or specific plans AWBI may have with customers in the relevant market;
- historical data on wheat shipments to certain markets that may be relevant (eg previous quality claims, payment issues);
- any long term agreements or specific plans AWBI may have with customers in the relevant market;
- the investment AWBI has made in building and developing customer relationships in the market in question;
- previous quality claims or payment issues; and
- any other relevant matters.

4.3.2. Grains Research and Development Corporation

The submission made on behalf of the **Grains Research and Development Corporation** (GRDC 2000) argued that if current marketing arrangements were to be altered, consideration would need to be given to the continuity and consistency of the various arrangements for quality assurance, receival standards, quality standards and

grading and the flow of information from marketers to researchers and breeders. There are several complex issues requiring further economic and policy analysis, including the relationship between centralised risk management (in a ‘single desk’), competition and sustainability-oriented decision making by growers. Also requiring careful analysis are the potential implications for maintenance of national wheat quality advantages and Australian grower access to technology and germplasm, through ensuring close marketer-researcher-breeder-grower links. If a ‘single desk’ were to be retained, the holder should have certain community service obligations including the provision of market information to the Australian wheat research community, the coordination of wheat levy collection and associated source information and requirements with regard to transparency in costing and charging of end point royalties.

4.3.3. Productivity Commission

The submission made on behalf of the **Productivity Commission** (2000) argues that marketing arrangements for Australian wheat have changed substantially over the past decade or so, and these changes have improved the efficiency of marketing. The relevant question now is whether the remaining monopoly over wheat exports is helping or hindering the industry.

Some of the claimed benefits of ‘single desk’ selling derive from the potential to raise wheat prices by controlling the quantity sold on export and domestic markets. Others derive from potential for economies of scale and scope, or from grower control of wheat market. The submission argues it is important to separate these arguments.

‘Single desk’ export selling compels individual wheat growers to export via AWBI or with the permission of the WEA, in consultation with AWBI. But these arrangements can act as a mechanism for exploiting Australia’s market power in international markets only if the potential for such power exists. Market power is not created automatically by the establishment of a ‘single desk’, which can control the volume and characteristics of Australian exports, but not foreign supplies of wheat or substitute products. However, arbitrage across export markets is unlikely to be perfect, possibly giving Australian wheat producers a degree of market power in some markets which, in turn, the ‘single desk’ could exploit. Examining this possibility, the submission notes:

- if Australia has certain advantages in supply from location or season, Australian exporters could capture some ‘premium’ by controlling supply - however, market share could fall if this encouraged increased competition from rival exporters;
- some observed ‘premiums’ could result from the supply of special services such as guaranteed supply, and there may be additional costs involved in such a guarantee;
- a strategy of countervailing the buying power of large importers by restricting supplies would not succeed if the buyer could switch suppliers without incurring higher prices; and
- wheat prices may be ‘distorted’ by the grain subsidies paid to European and US producers, but Australia has negligible power to do anything about it by directing its own wheat exports to particular markets. The ‘single desk’ may attempt to

divert supplies to the highest-priced markets – but so would any commercially astute exporter.

If there are markets where Australia faces restricted competition from rivals and higher than normal returns on a continuing basis, capturing these returns need not require a monopoly over all exports via the ‘single desk’. For example, the rights to export to these markets could be auctioned, and the proceeds distributed to producers directly as, for example, an annual cash payment apportioned according to the value of production.

Regarding the argument that the ‘single desk’ generates cost savings in areas such as financing of payments, freight, storage and shipping, the submission suggests that this be put to the test by removing AWB Limited’s monopoly. If AWB Limited were the most efficient provider, growers would continue to trade through AWB Limited and its dominant position, and scale and scope of operations, would not be affected.

The submission also suggests that current marketing arrangements may lead to higher domestic prices for wheat and impair long-term performance of the wheat industry itself by reducing competition in handling, storage and distribution activities and by precluding development of alternative market structures.

4.4. Farm partnerships and private individuals

The Committee received a large number of submissions from farm partnerships and private individuals. Many supported the retention of the ‘single desk’ as it is currently operated by AWBI. The large number of such submissions precludes their individual discussion. However, the reasons many farm families wish to retain the ‘single desk’ can be summarised as follows:

4.4.1. Perceived Advantages of the Current Arrangements

(a) Direct benefits to growers delivering to the export pools

- price premiums are obtained from ‘single desk’ selling, which add to average export returns;
- storage, handling and transport costs are minimised through economies of scale and coordination of logistics;
- all profits from the export pools are returned to growers;
- delivery to the export pools saves growers the time and expense of undertaking their own marketing and managing their own price risk;
- growers are offered a number of different options for payment, including credit on competitive terms;
- the export pools act as a buyer of last resort, particularly if, for example, large quantities of weather-damaged grain are produced and private traders are unwilling to enter the market to this grain;
- growers are guaranteed they will be paid when they deliver to AWBI;
- banks will lend to growers on the strength of AWBI’s harvest payment; and
- delivering to the pool is administratively simple for growers.

(b) Benefits to all grain growers from the dominant market position AWBI enjoys as a result of operating the ‘single desk’

- the harvest payment sets a price floor for wheat in the domestic market;
- the harvest payment provides a benchmark price for other grains in addition to wheat;
- AWB Limited is grower controlled and accountable to growers;
- there are no ‘weak sellers’ in the market;
- there is a uniform set of receival and quality standards;
- growers receive market information which enables them to effectively manage their businesses and produce the right products; and
- the activities of AWBI are more transparent to growers than those of the grain traders.

(c) Social benefits for regional Australia

- growers trust the system and have grown up with it;
- AWB Limited is a good corporate citizen;
- the money paid to growers is spent in rural towns and provides employment in these towns;
- the wheat export marketing system is Australian owned; and
- growers are not forced to compete with each other in the market place.

(d) Benefits to Australian trade and the economy

- overseas customers perceive AWBI as a reliable supplier of quality grain;
- AWBI holds stocks for customers and provides security of supply;
- AWBI develops overseas markets for Australian wheat;
- AWBI supports research and development; and
- wheat growers are able to sell their product into the ‘highly distorted’ international market.

4.4.2. Perceived disadvantages of the current arrangements

These views as to the positive aspects of the ‘single desk’ were not universally shared, however. Some of the contrary views expressed by other farm families and individuals may be summarised as:

(a) Requirement for growers to deliver to export pools in order to export wheat

- at best there is weak evidence the existence of significant price premiums over and above those attributable to quality and freight;
- the evidence that the ‘single desk’ delivers cost minimisation in storage and handling is problematic. In fact, AWB Limited’s dominant position as a buyer of storage and handling services may discourage the entry of new sellers, and reduce the potential for realising further cost savings in the system;
- the pool provides marketing services to growers. But growers are also charged for these services. Growers who wish to undertake their own marketing or to purchase export marketing services elsewhere should be able to do so;

- in the past the export pool has been able to absorb and eventually market large quantities of weather damaged grain which no individual trader appeared willing to purchase. But with a limited domestic market, and no access to the export market, what incentive was there for a trader to purchase anyway?
- the WMA includes a system which in theory allows some wheat to be exported by firms other than AWBI. But in practice, only a small amount of wheat is exported under this system because:
 1. It imposes administrative costs on non-AWBI exporters through its cumbersome, bureaucratic, time-consuming, and non-transparent procedures.
 2. It imposes additional freight and handling costs on non-AWBI exporters by effectively stopping them from shipping in bulk.
 3. It discourages non-AWBI exporters from investing in, or developing markets, because there is no certainty that they will continue to have export permits issued to them.

(b) AWB Limited's dominance of the market by virtue of its operation of the 'single desk'

- the harvest payment may provide a floor or benchmark, but it is an inappropriate one, lacking any direct link with the current export parity price. To take advantage of any perceived lower domestic wheat prices at harvest, grain buyers have to be prepared to purchase and store grain;
- AWB Limited provides growers with information, but there are alternative sources;
- the possession by AWBI of a monopoly on export sales of wheat effectively allows the AWB Group to restrict competition in the domestic market for wheat market by conferring cost advantages in freight, handling and supply on AWB (Australia) - the AWB Group's domestic trading arm – which are not available to other domestic traders; and
- the possession by AWBI of a monopoly on export sales of wheat appears to restrict competition in the market for the provision of grain storage, handling and transport services by giving the AWB Group a dominant position when negotiating with suppliers of these services.

(c) Perceived social benefits

- there would be adjustment costs if the current system were changed. But these would not necessarily be great if changes were phased in over time;
- growers adjust to changing market conditions and prices as part of the normal business of farming; and
- employment in towns may in fact increase if there were more than one marketer wishing to purchase wheat from growers for export.

(d) Perceived benefits to trade and the economy

- many of the functions currently performed by AWBI in respect of R&D, and quality control, are residual functions inherited from the statutory Australian Wheat Board, and could be handled equally well by other organisations;
- there is no reason to suggest private grain traders would not be as anxious to maintain as good customer relations as AWBI;
- small companies had been unable to expand their business beyond container wheat, as all applications to the WEA for bulk export consent had failed; and
- there is no actual mechanism by which the AWBI 'single desk' can countervail the agricultural policies of the US and EC. The distortions these policies impose on the market can only be taken as given.

4.5. Overseas consultations***4.5.1. Argentina***

In Argentina the Committee consulted with a former Minister for Agriculture, several trading companies, the grain exchange, a farmer co-operative, and a consultant. The wheat industry in Argentina has moved from a highly regulated to a deregulated structure over the past decade. Comments on some of the effects of this deregulation included:

- the availability of suitable credit facilities for growers assumes greater importance;
- research and development has declined since the associated compulsory levy system was abolished;
- wheat grades have declined, but yields have increased substantially as farmers chase quantity rather than quality;
- grower supply chain charges (eg freight, handling and storage) have declined markedly (ie in some cases by up to 50 per cent) with increased competition; and
- market information (eg Internet) assumes far greater importance.

4.5.2. United States of America

The Committee met with a high ranking member of a former US administration, a range of government officials and wheat grower organisations in Washington and also several trading companies, researchers in grain marketing and supply, and co-operatives across the US. Comments from government included:

- the US believes in an open, competing and transparent system which results in a comparative advantage for industry;
- while Australia appears to have tried to move towards this with the formation of AWB Limited, compared to Canada, the US still finds it contradictory that Australia retains a 'single desk' as part of this structure;
- the US Government's public position is that the 'single desk' remains a core disagreement and the changes to AWB Limited, vis-à-vis the Canadian Wheat Board, make no difference as to how the US views AWB Limited;

- there is a strong view in the US that AWBI costs (eg handling charges) would fall if opened to competition;
- given the large reduction in central buying agencies worldwide, the US seriously questions AWBI's ability to extract premiums from the market;
- US farmers both *produce* and *market* grain, whereas Australian farmers hand over the marketing task to AWB Limited; and
- in spite of changes to Australia's 'single desk' structure with AWB Limited, there is a strong belief that if AWB Limited encountered financial difficulties, the Government would 'bail them out'; although US farmers receive well over \$US15 billion in direct income support, this is seen as 'decoupled' from production – consequently, the support cannot be seen as a counter argument to the continued operation of the 'single desk'.

Some of the comments from industry across the US echoed points made by government above, but some conflicting views were also put to the Committee. In addition, it was suggested to the Committee that:

- improved communications, particularly the Internet, has completely changed the dynamics of marketing wheat as a product not just a commodity;
- the Australian wheat marketing 'system' had a lot of strong points, such as varietal management, strategic selling, good customer service and guaranteed supply of high-quality wheat, that should not be discarded in any proposed change;
- in an environment of consolidation in the wheat trade, it is an advantage for growers to be represented by a large company in the international market;
- the US subsidises production, and consequently has to deal with large carry-overs, which depresses world prices – it is naïve for the US government to complain about 'single desk' marketing;
- the North East Asian market is now stable, with AWBI marketing activities having minimal effect;
- government regulation of the wheat industry has more of an effect on the domestic market, as not only does competition result in cost-savings up to export position (fob), there are always alternative suppliers on the world market;
- the US wheat industry model is for partnerships between companies specialising in either origination or marketing, capturing many of the strengths of the 'single desk' system including specialisation, pooling and risk management;
- removal of the 'single desk' gives growers much more choice in marketing their grain with minimal 'cross subsidy' from efficient to inefficient growers, in contrast to compulsory pooling; and
- although high quality wheat will always attract a high price, there was a high degree of scepticism as to whether the Australian 'single desk' system is able to generate price premiums, particularly into optional origin bulk markets.

4.5.3. Canada

In contrast to the US free market system, the Canadian market is highly regulated with the 'single desk' operated under the auspices of the Canadian Wheat Board (CWB). The Committee met with the CWB, government agencies, co-operatives and grain trading companies. Comments from CWB included:

- the CWB is confident it can capture a price premium in markets while at the same time reducing costs, for similar reasons as those advanced by AWBI (eg co-ordination of the freight network resulting in lower costs);
- there is still majority support amongst growers for the CWB, however this is highly dependant on farmers' ages with younger producers tending to be less supportive of the 'single desk';
- unlike Australia, it was noted that less than half of Canadian wheat exports are directly handled by CWB; and
- the high quality of Canadian wheat is due to the Government's regulatory framework.

Comments from co-operatives/traders included:

- handling charges had fallen markedly following freeing up of the market;
- an agency like CWB can only extract a price premium if they have a supply monopoly, and CWB does not have that monopoly;
- there are many fundamental differences between grain marketing systems in the US and Canada, and Australia, eg the water transport system via the lakes and having such a huge market (USA) on the Canadian doorstep;
- the number of central grain buying agencies in the world is declining and so the power of a 'single desk' agency to extract price premiums is also greatly reduced; and
- with agencies like CWB and AWB Limited, access to key data is limited and hence it is difficult to assess whether there are in fact benefits in having a 'single desk'.

4.5.4. South Korea

In South Korea, the Committee held discussions with the Government and with major millers. As Korean millers have diversified supply away from the US, Australian wheat market share has increased from 10 per cent in 1989 to 38 per cent in 1999 (KFMIA 2000).

Comments included:

- praise for the marketing efforts of the former Australian Wheat Board in working closely with customers to develop the market for high-quality noodle wheat varieties, which has had a significant impact on increasing Australia's market share;
- noting that AWB Limited understands the Korean way of doing business and responds to this;
- the importance of the direct customer relationship with AWB Limited, particularly in resolving problems or providing technical advice and market information, compared with business dealings with traders;
- raw material quality and price competitiveness are important, with Australia supplying high-quality wheat at the same price as other originators;
- acknowledgment that the Korean market is now relatively mature, with stable or slightly increasing market share for Australian wheat, resulting in an inevitable decline in marketing activities;

- preference for dealing with a ‘single desk’ exporter for Australian wheat, as substantial deregulation will throw up the same quality control problems experienced in the US market; and
- noting that the ‘single desk’ status of AWBI is a cause for concern in a WTO context, as this limits the number of suppliers and hence increases the price to buyers.

4.5.5. Japan

Until 1995, the Japanese market had a ‘single desk’ importing system whereby the Japan Food Agency (JFA) allocated import quotas to licensed traders, who participated in weekly tenders for specific shipments. Import quotas were abolished in 1995 and replaced with a system under which importers are required to pay the tariff equivalent (tariff and mark-up). The JFA ‘entrusts’ the import of wheat to approved importers and, as under the former quota system, calls weekly tenders for specific shipments.

The Committee consulted with the AWB Limited regional office, Japanese trading companies and millers. Discussions were also held with the JFA. Comments from industry included:

- recognition that Australia is seen as a long-term constant stable supplier of high-quality wheat, particularly the ASW varieties used for *udon* and *ramen* noodles, with segmenting varieties a good strategy for Australia;
- AWB Limited has done an excellent job of understanding and catering for the Asian market;
- stability of supply of an agricultural commodity is particularly valued;
- that each origin has specific characteristics in demand for different reasons, resulting in little direct competition between origins, and no impetus to change the market mix. However, in some markets there is a lot of competition between companies selling the same origin wheat;
- blending, stable moisture content, quality and stability of supply are the most important factors for millers, with quality and contract performance important for traders;
- technical support is also important, particularly in developing new varieties, and this is a strength of ‘single desk’ exporters, although information flow could be improved;
- because AWB Limited has been the only source for buying Australian wheat, customers can not make any judgments about potential cost savings under deregulation; and
- there is a difference between importing ‘single desk’ arrangements and exporting ‘single desk’ arrangements, as exporting nations have significant power over importing nations.

4.5.6. Italy

During a visit to Italy to attend a conference, one member of the Committee held meetings with selected representatives of organisations involved in the domestic market for durum, including a seed supplier, a grain trader, a flour miller, and a pasta manufacturer. Arguably Italy is the premium market in the world for durum wheat,

and it is illegal to sell pasta in Italy that is made out of any other type of wheat than durum. The durum industry in Australia started exporting to Italy when production outgrew demand in the domestic market, and a surplus became available for export. Comments made during these meetings included:

- the market for high quality durum in Italy will continue to expand due both to growing demand for pasta and declining domestic durum production;
- government regulations are inhibiting research and the development of improved varieties, the amount of land available for farming, and improved farming practices to increase production;
- Italy is a quality conscious market, and significant price premiums are paid for quality;
- ‘desert durum’ from Arizona is regarded by the Italian pasta industry as the most consistent source of top quality durum wheat;
- Australian durum is of comparable quality in some years, but quality is not consistent from year to year. Market prospects for Australian durum would improve markedly if growers could achieve more consistent high quality production;
- markets can often be found for lower quality durum, but only at a price discount; and
- the Italian industry generally has good relations with AWBI, and regards its marketing of Australian durum as satisfactory now that individual firms can deal directly with AWBI rather than through an Italian agent. However, they would prefer it if they could source Australian durum from a range of sellers.

4.5.7. Egypt

One member of the Committee travelled to Egypt as part of an overseas trip for other purposes. While in Egypt, he held meetings with Australian Embassy staff in Cairo, representatives of the Egyptian government including the Minister responsible for Supply and Home Trade, the head of the General Authority of Supply Commodities (GASC), and a senior manager of Holding Company for Food Industries. Meetings also were held with executives of private organisations involved in the Egyptian wheat market.

Information obtained during these meetings included:

- Egypt has a population of about 65 million people, and is one of the largest markets in the world for wheat;
- in 1998, consumption was about 13 million tonnes, of which about half is locally produced and half is imported;
- the USA share of the market has increased significantly over the last 5 years, and reached nearly 5 million tonnes (60 per cent of total imports) in 1998;
- prior to 1992, Government owned virtually all flour mills in Egypt;
- in 1992, the Government initiated privatisation of the milling and grain industry, and established free market policies;
- the situation has evolved over time, and now the market for wheat consists of the following three distinct sectors:
 - one sector is for wheat retained by Egyptian farmers for on-farm milling and consumption (about 30 per cent).

- the largest sector (about 46 per cent) is government controlled and produces subsidised low quality (“82 per cent extraction”) flour that is used to produce basic bread sold at controlled prices, as a key component of Egypt’s social security policy for the large part of the population that live in poverty. Wheat for this sector is procured by GASC at public tenders. Price is the only consideration, quality is virtually irrelevant, and AWBI has to compete against the US and European trade on the basis of price in a fiercely competitive market.
 - the smallest sector (about 24 per cent) comprises both public and private sector mills that produce high quality (“72 per cent extraction”) flour. This type of flour is not subsidised and the government does not control the price. At present, government controlled mills belonging to the Holding Company as well as private mills are both producing this type of flour. Capacity of the private mills is growing rapidly as a result of construction of new flour mills as well as expansion of capacity and increasing storage facilities in existing mills. This sector is quality conscious, and includes a joint venture investment by AWB Limited in the Five Star Flour Mill that is successfully marketing high quality flour produced from Australian wheat.
- Five Star Flour Mill claimed that it paid a price premium for Australian wheat; and
 - other private sector mills are critical of the fact that they have to purchase high quality Australian wheat from Five Star Flour Mill rather than on the open market.

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5. OBJECTIVES OF THE LEGISLATION AND EFFECTS ON COMPETITION

The Competition Principles Agreement states that a legislation review should clarify the objectives of the legislation (CPA, 9 (a)). Thus, the review's terms of reference require the Committee to assess the objectives of the *Wheat Marketing Act 1989* (the WMA) and the Wheat Export Authority's (WEA) arrangements, structure and functions. The review's terms of reference also require the Committee to identify whether, and to what extent, the WMA restricts competition, including the appropriateness of granting a monopoly to a private company. The objectives of the WMA and its effect on competition are discussed in this chapter, while the WEA's arrangement, structure and functions are discussed in the following chapter.

Key sections in chapter:

- Procedure for clarifying the objectives of the Act
- The current Act
- The original Act and later amendments
- The Minister's second reading speech
- Annual report of WEA, ministerial statements, and evidence of those affected by the legislation
- Inferred objectives of the Act
- Effect on competition
- Appropriateness of granting a monopoly to a private company

5.1. Procedure for clarifying the objectives

According to the guidelines for NCP legislation reviews (Centre for International Economics 1999), objectives may be explicit in legislation but may also be implied by the impacts of restrictions to competition. Objectives may be identifiable from:

- the legislation directly;
- second reading speeches in parliament introducing the legislation;
- subordinate legislation;
- management plans and annual reports of institutions empowered by the legislation;
- Ministerial statements; and
- the actions, impacts or evidence of those affected by the legislation.

The original *Wheat Marketing Act 1989* (Act No. 58 of 1989) was significantly amended in 1997 and 1998. The current Act as consolidated in force in July 1999 bears little resemblance to the original. The original Act stated a number of objectives but the current Act has no such equivalent statement. Thus the Committee was required to infer the current Act's objectives.

To do this, the Committee:

- reviewed the current Act, the original Act and later amendments, and the Minister's second reading speech for the current Act;
- reviewed the WEA Annual Report 1998-99, Ministerial statements and the evidence of those affected by the legislation;
- considered various inferred or stated objectives; and
- identified the most consistent to emerge.

5.2. The current Act

The current Act is the *Wheat Marketing Act 1989*, Act No. 58 of 1989 as amended and consolidated as in force on 7 July 1999.

The long title of the Act is 'an Act relating to the export of wheat, and for other purposes'. Section 4 states that the Australian Wheat Board that previously existed under this Act continues in existence as the Wheat Export Authority. Section 5 (1) states that the Authority has two functions:

- to control the export of wheat from Australia; and
- to monitor nominated company B's performance in relation to the export of wheat and examine and report on the benefits to growers that result from that performance.

Other key sections of the Act are as follows:

- Section 5 (2) states that the Authority (the WEA) has power to do all things that are necessary or convenient to be done in connection with the performance of its functions.
- Section 57 (1) states that a person shall not export wheat unless the Authority has given its written consent to the export of the wheat, and the export of the wheat is in accordance with the terms of that consent. However, Section 57 (1A) states that this prohibition does not apply to nominated company B.
- Section 57 (3) states that before giving a consent, the Authority must consult nominated company B. Furthermore, the Authority must not give a bulk-export consent without the prior approval in writing of nominated company B, with any consent considered to be a bulk-export consent unless it is limited to export in bags or containers.
- Section 57 (7) states that before the end of 2004, the Authority must conduct a review of certain matters, and give the Minister a report on the review. These matters are nominated company B's export operations, the conduct of nominated company B in relation to consultations for export consents, and the granting or withholding of approvals for export consents.
- Section 84 (1) states that nominated company B must purchase all wheat that is offered to the company for inclusion in a pool operated by the company, and

meets the standards required by the company. Section 84 (3) states that this obligation by nominated company B (subsequently AWBI) to purchase wheat would not apply if Section 57 (1) were to apply to the company, effectively tying this obligation to the bulk export ‘single desk’.

As mentioned, there are no stated objectives in the current Act. However, from the Act’s key sections, it may be inferred that the intent of the Act is to enable continuation of key features of the ‘single desk’ arrangements for wheat exports for the benefit of Australian wheat growers by the following arrangements:

- to reserve bulk wheat exports for nominated company B (from section 57 (3));
- to give nominated company B a role in the issuing of consents for bagged and containerised wheat (from section 57 (3A));
- to make the WEA the relevant authority for approving all Australian wheat not exported directly by nominated company B (from section 57 (1));
- to give the WEA a role in reviewing the operations of nominated company B (from section 57 (7)); and
- to ensure that all wheat growers potentially have access to the bulk wheat markets being reserved for nominated company B (from section 84).

Note that while section 57 (3) does not automatically exclude other companies from exporting bulk wheat, in giving nominated company B a veto over exports by other companies, the Act gives nominated company B an effective monopoly on bulk wheat exports. Furthermore, section 5(1)(b) requires the WEA to “monitor nominated company B’s performance in relation to the export of wheat and examine and report on the benefits to growers that result from that performance”.

Considering the key sections of the Act, the most striking impression is that they are operational aims, rather than expected objectives. Nominated company B clearly has a key role, one apparently exceeding that of the WEA itself, and yet the reason for this key role is not explicitly spelled out in the legislation. The fact that the WEA is required to monitor the performance of nominated company B and report on the benefits to growers suggests that the objective of the Act is to maximise returns to growers from the export of bulk wheat. However, it is necessary to examine further sources to clarify the objectives of the current Act.

5.3. The original Act and later amendments

5.3.1. *The original Act*

The original *Wheat Marketing Act 1989* (Act No. 58 of 1989) covered a number of areas including:

- the continuance, functions and powers of the Australian Wheat Board;
- control of wheat exports;
- operation of the Board’s wheat pools;
- Commonwealth underwriting of borrowings; and
- the Wheat Industry Fund.

Section 4 of the Act continued the existence of the Australian Wheat Board.

Section 5 stated the objects of the Board as being:

- to maximise the net returns to Australian wheat growers who sell pool return wheat to the Board by securing, developing and maintaining markets for wheat and wheat products and by minimising costs as far as practicable;
- by participating, in a commercial manner, in the market for grain and grain products, to provide Australian grain growers, and especially wheat growers, with a choice of marketing options; and
- to participate in value adding activities for the purpose of benefiting Australian grain growers.

Section 6 stated the functions of the Board. These functions included to export wheat from Australia (Section 6 (a)), to control the export of wheat from Australia (Section 6 (d)), and to control the marketing overseas of Australian wheat (Section 6 (e)).

These functions included both commercial and regulatory functions, the export of wheat being one of the former, and control of the export, and overseas marketing, of Australian wheat, two of the latter.

5.3.2. Later amendments

In April 1997, the Government agreed to industry's recommendation for the establishment of a grower owned and controlled company to assume responsibility for wheat marketing from 1 July 1999, when the Government guarantee of the Australian Wheat Board's borrowings to finance the first advance ceased.

Section 55A of the *Wheat Marketing Amendment Act 1997* (Act No. 194 of 1997 as assented to on 8 December 1997) stated that the first step toward the new structure for the Australian Wheat Board would be the establishment of several companies to take over the commercial activities of the Board. These companies would comprise a wholly-owned subsidiary of the Board (nominated company A) and a number of wholly-owned subsidiaries of nominated company A (the main ones being nominated company B and nominated company C).

Nominated company A's role would include borrowing for the purposes of on-lending to other designated companies. Nominated company B's role would be to conduct pooling and marketing of new season wheat. Nominated company C's role would include trading in wheat and other grains.

The constitution of nominated company B (clause 55K) set out the following as objects of the company:

- to maximise the net returns to Australian wheat growers who sell pool return wheat to the company by securing, developing and maintaining markets for wheat and wheat products and by minimising costs as far as practicable;
- to export new season wheat from Australia;
- to trade in new season wheat in Australia;
- to make arrangements for the growing of wheat for trade in Australia;

- to promote or fund the marketing of wheat;
- an object approved in writing by the Minister; and
- to do anything incidental to or conducive to any of the above objects.

In relation to the current Act, the key role accorded nominated company B might be seen as confirmation that the legislators regarded the objectives of the amended Act as largely synonymous with those of nominated company B.

The constitution of nominated company B (AWB (International) Ltd) requires it to secure the maximum net return for Australian growers participating in its pools and to export wheat.

What would happen with the former Australian Wheat Board's export monopoly was spelled out in the 1998 amendments in the next section.

5.4. The Minister's second reading speech

The *Wheat Marketing Legislation Amendment Act 1998*, Act. No. 103 of 1998 assented to on 30 July 1998, put in place the final details for the new wheat marketing arrangements to commence on 1 July 1999. The main areas the amending bill addressed were the conversion of the Wheat Industry Fund to shares to provide the capital base of the new company structure, and the continuation of the export monopoly.

Regarding the latter, the Minister for Primary Industries and Energy the Honourable John Anderson MP reported to parliament in his second reading speech on 14 May 1998:

‘The bill also provides for the retention of the wheat export monopoly from 1 July 1999. Specifically, the bill provides for an independent statutory authority, to be known as the Wheat Export Authority, to manage the export monopoly on wheat. To give growers the certainty they have been asking for, the bill also provides that the new grower company pool subsidiary, called company B, have an automatic right to export wheat for five years. Requests to export wheat from other than the grower company pool subsidiary, as currently happens, will be managed by the Wheat Export Authority in consultation with the grower company pool subsidiary. The Wheat Export Authority will also oversight the pool subsidiary's use of the export monopoly to ensure it is being used in accordance with the intentions of parliament.

‘The government is committed to the principles of national competition policy. Continuation of these arrangements for the export monopoly for the full five-year period will be subject to the outcome of a comprehensive and independent national competition policy review in 1999-2000.

‘Assuming the national competition policy review in 1999-2000 recommends continuation of the export monopoly, it is envisaged that before the end of the prescribed five-year period in 2004 an export monopoly performance review be held. Specifically, the review would assess the performance of the pool

subsidiary in its use of wheat export rights and advise government on the future operation of the export monopoly, including whether that company should continue to have special export rights. Such a review would probably be linked with a national competition policy review process. It would be up to the Government to decide who would receive any special export rights beyond 2004 and for parliament to amend the legislation as necessary.’

The Minister’s statement in effect says the Government decided to not let lapse the export wheat monopoly it had given the former Australian Wheat Board, whose operations in running wheat pools for growers the Government had underwritten. Instead, the Government had decided to keep the monopoly, and create a new legal successor to the former Board (the WEA) to manage it.

However, the WEA would not have the same day to day management role for bulk wheat as the former Australian Wheat Board. Instead, the WEA’s main role would be to monitor and report on the performance of the company to which the Government had sub-contracted the export monopoly for a five-year period, this company being the new grower owned and controlled nominated company A’s pool subsidiary, nominated company B.

The reasons for giving the export monopoly to the new grower company emerge from the phrase ‘to give growers the certainty they have been asking for’. The Government guarantee on borrowings was being removed. Possession of the export monopoly was to give the new grower group of companies the best prospect of commencing to operate commercially without the Government borrowings guarantee.

The Minister acknowledged, however, that the continuation of the ‘export monopoly’ could bring the Government into conflict with its own National Competition Policy (NCP). He therefore emphasised that continuation of the monopoly would be subject to the outcome of the NCP review in 1999-2000 – in other words, subject to the NCP review concluding that the arrangements were likely to provide a net benefit to the Australian community as a whole. The Minister added that if the review in fact reached this conclusion, then, the purpose of the 2004 review would be to assess AWBI’s performance in managing the Government’s export monopoly on the Government’s behalf – in other words, that AWBI was using the wheat export rights granted to it under the legislation ‘in accordance with the intentions of parliament’. The Minister then added that the 2004 review ‘would probably’ be linked with a national competition policy process, and ‘it would be up to the Government to decide who would receive any special export rights beyond 2004 and for parliament to amend the legislation as necessary’.

Overall, the direction of the Minister’s statement appears clear. However, during its discussions with stakeholders, the Committee heard a number of different interpretations over what this particular paragraph of the Minister’s speech meant exactly, and considers it may assist the process of the 2004 review for the Government to clarify the following at the earliest opportunity:

- whether the 2004 review would assess AWBI’s performance on behalf of all growers (including those who did not deliver to the export pool), or specifically

only those growers who delivered to the export pool (the Committee believes that all growers should be included); and

- whether there would be a further NCP review in 2004, or the WEA would include consideration of net benefits to the Australian community in its review of AWBI's performance on behalf of growers (the Committee believes that a full NCP review is not required but that the NCP principles should be used in the scheduled review)

It was suggested to the Committee by a number of stakeholders that current uncertainty as to the scope and process of the 2004 review may adversely impact on the value of AWB Limited shares when these shares are listed in 2001. A number of growers also commented on the manner in which they had acquired (or had been compelled to acquire) equity in AWB Limited, and expressed the view that if the value of shares were adversely impacted by any action by government (including the review), some compensation may be in order.

There appears to be significant opportunity for the AWB Group to generate profits for its shareholders from sources other than the operation of the 'single desk'. Any assessment of AWB Limited's B class shares as an investment opportunity will include the 2004 review as well as growth potential from other activities.

The Committee concluded that the fact that there will be a review in 2004 has been well known for some time, and there would always have been potential for uncertainty over the review to affect the value of AWB Limited shares. The Committee also notes that the 3 November 2000 meeting of the Council of Australian Governments (COAG) unanimously agreed to an ongoing commitment to the National Competition Policy, in order to safeguard the benefits that this policy is delivering to all Australians, and takes this as an indication that the 2004 review will, as foreshadowed in the Minister's speech, be conducted in accordance with NCP principles.

As to the question of compensation by the Government for any perceived negative effect of the 2004 review on the value of AWB Limited shares, the Committee believes the financial process by which growers acquired equity in AWB Limited is complex (see the more detailed discussion later in this chapter) and merits further examination.

5.5. Annual Report of the Wheat Export Authority

The WEA Annual Report 1998-99 also lends support to the contention that the objective of the legislation is to maximise net returns to growers. The Report mentions in a number of places the role of the WEA in monitoring the performance of AWBI in relation to the export of wheat and examining the benefits to growers that result from that performance. Furthermore, the outcomes statement within the Annual Report defines operational success as allowing the WEA to "contribute to the development of market opportunities for Australian wheat which benefit Australian wheat growers; and understand the impact of the 'single desk' arrangements on the wheat industry, in particular growers".

5.6. Ministerial statements

Subsequent Ministerial statements confirm the importance of maximising net returns to growers as an objective of the legislation.

At the Queensland National Party's State Conference in July 2000, the Deputy Prime Minister, The Honourable John Anderson MP indicated support for the wheat 'single desk' "while ever there is a benefit to Australian wheat growers and the nation's export performance". He reiterated this view of the objectives of the legislation in a speech in November 2000.

The Minister for Agriculture, Fisheries and Forestry, The Honourable Warren Truss MP, has also indicated that the 'single desk' was established in the interest of Australian wheat growers.

5.7. Actions, impacts or evidence of those affected by the legislation

The overwhelming majority of submissions, written comments and statements in consultation hearings by grain growers indicated their support for the 'single desk' is based on a perception of the ability of the current arrangements to secure, develop and maintain markets for wheat and wheat products and, by minimising costs as far as practicable, provide the best net return to growers.

Notwithstanding this support, during the Committee's consultations many growers both publicly and privately expressed concerns about aspects of the management of the 'single desk'. It was apparent that there is a lack of understanding amongst many growers of the AWB Group structure, and what activities are for the sole benefit of the pool, as opposed to those which would flow to the AWB 'B' class shareholders (for example, underwriting margins on financing, and domestic wheat marketing and related activities, as well as the provision of management and other services to the national pools). The Committee observes that this misunderstanding could be addressed by greater disclosure to AWB Limited shareholders (through the AWB Annual Report and Annual General Meeting), and also to growers who deliver to AWBI's pools.

5.8. Inferred objectives of the Act

The objectives of the current Act which most consistently emerge from this review are a mixture of social and economic, which may best be summarised as:

'For the Australian government to use its control of wheat exports to ensure (i) direct grower access to marketing services and export markets, and (ii) that growers receive the highest net return from sales in export markets'.

This objective is consistent with the wording of the current Act, with the Minister's statements of intent regarding the Act, with the role of 'nominated company B' in the Act, and with current arrangements, structure and functions of the WEA.

The Committee considered that to provide a common starting point for future work on wheat marketing arrangements it would be useful for the Government to explicitly state the objectives of the WMA in the legislation, and has made a recommendation to this effect at the end of this chapter.

5.9. Effect on competition

The guidelines for NCP legislation reviews (CIE 1999) note that the NCC has suggested seven main ways in which legislation may limit competition.

Legislation could restrict competition if it:

- governs the entry or exit of firms or individuals into or out of markets;
- controls prices or production levels;
- restricts the quality, level or location of goods and services available;
- restricts advertising and promotional activities;
- restricts price or type of input used in the production process;
- is likely to confer significant costs on business; or
- provides advantages to some firms over others by, for example, shielding some activities from pressures of competition.

5.9.1. Governs the entry or exit of firms or individuals into or out of markets

The current legislation does not specifically limit the entry of firms into the export wheat market. However, it clearly protects one firm (AWBI) by exempting it from the requirement to follow the same administrative procedures for exporting wheat as are applied to all other firms. This effectively places limits on market participation on a sale-by-sale basis. Furthermore, as discussed later, the current arrangements allow AWBI to oversee the activities of the other firms who wish to export wheat, and to veto bulk exports by other firms.

Although the WMA includes a system which in theory allows some wheat to be exported by firms other than AWBI, in practice, little wheat is exported under this system because:

- it imposes administrative costs on non-AWBI exporters through its cumbersome, bureaucratic, time-consuming, and non-transparent procedures;
- it imposes additional freight and handling costs on non-AWBI exporters by effectively stopping them from shipping in bulk; and
- it discourages non-AWBI exporters from investing in, or developing markets, because there is no certainty that they will continue to have export permits issued to them.

5.9.2. Controls prices or production levels

The current legislation does not restrict wheat production. Indeed, it requires AWBI to accept into its export pools any wheat offered to it which meets its standards. Some have argued that this requirement may not be onerous, since AWBI is free to close pools or change its standards at any time. Nonetheless, so far as growers are concerned, AWBI differs from many other potential buyers in that it does not contract with them for a specific product, but undertakes to market on their behalf whatever wheat they can produce and deliver to its pools and which meets AWBI's standards. Growers see this as necessary for them, given that they cannot control how the weather may affect the quality and quantity of their crop.

The current legislation allows one organisation (a private company) to set the prices at which almost all Australian export wheat is offered. Some have argued that this makes little difference to the realised price, since AWBI faces keen competition from non-Australian exporters, and must accept whatever wheat price is current on the day. This may be substantially true. However, AWBI itself argues that it can set a 'premium' in many markets for Australian wheat since it controls all Australian export wheat supplies. Rather than having to sell on the day, for example, it can (within limits) hold stocks and wait for a better price, knowing no Australian competitor can enter the same market and undercut it.

Further, AWBI's influence over the export price, and claimed control over many supply chain costs, effectively allow it to control the receival price of export wheat, and hence the net farm gate return to growers.

The current legislation also most likely allows one organisation to influence domestic wheat prices, although not necessarily in one consistent direction. The legislation does not provide AWBI any direct role in the domestic market. However, it does allow AWBI, as the single bulk wheat exporter, to receive and hold large stocks of wheat. These stocks are able to be drawn on for both export and domestic market sales, through weekly tenders. On the other hand, domestic buyers do not readily have the option of importing wheat as an alternative to using AWB Limited stocks. It would be difficult to argue that AWBI's pool activities do not have at least the potential to affect domestic wheat prices.

The domestic wheat market may also be affected by the restrictions applying to export wheat, because buyers of domestic wheat have to compete with the export pools for supply.

As wheat is a partial substitute for coarse grains in feeding, domestic coarse grains markets may also be affected. Stocks of wheat controlled by the export pool are not necessarily quarantined from the domestic market, so these also have the potential to influence domestic grain prices.

AWB (Australia) – the AWB Group's domestic trading arm – may also be able to avail itself of freight, handling and supply on favourable terms not available to other domestic traders, increasing its ability to compete in the domestic market to the disadvantage of other domestic traders (see below).

5.9.3. *Restricts the quality, level or location of goods and services available*

The current legislation allows one organisation to set the quality standards for virtually all Australian export wheat. Many growers would argue this is beneficial, since by virtue of the pool's large size, its receival and quality standards become the de facto standards for all wheat. However, the arrangement does restrict competition in that it allows a single marketer to impose its own set of standards on virtually all Australian export and domestic wheat, regardless of whether these standards are necessary or appropriate in some particular markets.

5.9.4. *Restricts advertising and promotional activities*

The current legislation does not restrict any firm from advertising the virtues of Australian export wheat. In that it effectively restricts all firms but one from exporting bulk wheat, however, there would not seem to be a lot of reason for firms other than AWBI to want to advertise Australian wheat in export markets.

5.9.5. *Restricts price or type of input used in the production process*

The current legislation does not specifically prevent any firm from offering financial, marketing, storage, handling or transport services for grain. As already discussed, however, by effectively giving one firm an export monopoly for bulk wheat, the legislation may implicitly grant that firm significant power in the market for these services, or significant advantage over other firms should it choose to offer these services itself. Again, as discussed, many growers argue they benefit from AWB Limited being able to wield its considerable marketing power on their behalf. Nonetheless, the existence of one dominant buyer (and seller) of these type of services may prevent innovation, distort input prices, and discourage investment by other firms in new infrastructure.

The Committee does consider that recent initiatives by several banks to provide harvest finance at rates which are competitive to those of AWB Limited will be of benefit to growers.

As the bulk of the wheat crop is exported, the possession of a monopoly on export wheat may give AWB Limited a dominant position when negotiating with suppliers of grain storage, handling and transport services. This dominant position is likely to also directly benefit other parts of the AWB Group, particularly AWB (Australia).

It may be argued that if AWBI were to continue as a major exporter of wheat in a deregulated export market, it would be able to influence the domestic market in a similar manner to that described above. This may be true. However, it would not be in a position to do so directly as a consequence of a legislated monopoly.

5.9.6. *Is likely to confer significant costs on business*

The current legislation specifically requires all potential wheat exporters other than AWBI to apply to the WEA for an export permit for their wheat. Some argue there may be significant delays in being granted an export permit, and little assurance such

a permit will be granted, particularly for bulk wheat. These delays may impose high administrative and compliance costs.

5.9.7. Other discriminating advantages

The current legislation explicitly discriminates in favour of one firm. As a consequence, it also discriminates in favour of one group of growers (those delivering to the export pool) and implicitly against another group (those not delivering to the pool). It may be argued that all growers have the option of delivering to the pool, and therefore those choosing not to deliver have no right to feel aggrieved. Some growers argue, however, that they do not believe AWBI and its export pools offer them the best deal, but are prevented from seeking the best deal because under the current legislation they are not allowed to export their wheat in bulk except through the pool.

5.10. Appropriateness of granting a monopoly to a private company

5.10.1. Structure of AWB Limited

One of the main reasons given for granting a monopoly to AWBI, a private company, is that the company is grower owned and controlled. The parent company (AWB Limited) has a requirement to provide a reasonable commercial return to shareholders (presently primarily growers), while the subsidiary company which holds the ‘single desk’ has as part of its charter a requirement to maximise net returns to growers delivering to the pool. Further, the subsidiary company has a buyer of last resort obligation imposed by legislation.

As noted in AWBI’s submission to the review (AWBI 2000), AWB Limited is the service provider to the various subsidiaries, which include AWBI (responsible for the wheat export pools), AWB (Australia) Limited (responsible for domestic wheat and other grain trading and the export of non-statutory grains), and AWB (Finance) Limited (responsible for pool return price underwriting and loans to growers). AWBI contracts with growers and makes distribution of pool returns to growers directly, where they are participating in the pools as a stand alone product, or to AWB (Finance) Limited, where growers have participated in AWB (Finance) Limited underwriting.

The subsidiary companies in the AWB Group do not employ specific staff or acquire resources. Instead, service agreements are entered into between AWB Limited and specific subsidiary companies, pursuant to which staff and other resources are provided by AWB Limited to these companies. According to the AWBI submission, ‘these arrangements reflect the manner in which many groups of companies operate in the Australian commercial environment’.

The Committee received, on a confidential basis, a copy of the service agreement between AWB Limited, AWBI and AWB (Finance) Limited. The agreement includes expressions such as “a reasonable commercial rate of return”, “key performance indicators”, “a margin on working funds” and “performance benchmarks”. Whilst these terms certainly appear appropriate for such an agreement, in the Committee’s

opinion they should be explicitly defined, so that there is no uncertainty in their application - particularly in light of the related party nature of the arrangements.

Furthermore, the Committee observes that the outcome of this agreement, whether it be the pool management fee or the margin earned by any member of the AWB Group (for example, AWB (Finance) Limited or Agrifood Technology Pty Ltd), should be clearly stated in the Annual Report of AWB Limited and in AWBI's reporting to growers who supply wheat to the pools. This reporting would be consistent with the principle of transparency, and the appropriate corporate governance of related party transactions. As the arrangements between the parties are to be on a contestable basis, in the Committee's view AWBI should also state in its reporting what steps it has taken to satisfy this requirement.

During its discussions with stakeholders, it was suggested to the Committee a number of times that the current structure of the AWB Group is likely to be of benefit to growers generally so long as growers retain control of the Group and its direction.

According to AWB Limited (1999), there are a number of mechanisms to ensure grower control, including:

- a dual class share system – 'A' and 'B' class shares;
- rights attached to the 'A' class shares give growers the power to elect a majority of the Board of Directors of AWB Limited;
- growers are able to exercise their control directly through this majority of the Board;
- controls over Directors' powers, in particular, a requirement to run pools so as to maximise returns to growers; and
- the constitution of AWB Limited precludes 'A' class shares being issued to non-growers.

Each grower is entitled to one 'A' class share. Until 31 December 1999 no payment was required. From 1 January 2000 the issue price for an 'A' class share has been \$1. A 'grower' is a person who produces, in Australia, an annual average tonnage of at least 33 and one third tonnes of wheat a year. This is not restricted to people who deliver to the AWB Group. However, the number of votes an 'A' class shareholder can cast in excess of one depends on the amount of wheat the grower has delivered to the AWB Group. 'A' class shares are redeemable preference shares, that is, they are redeemable if the 'A' class shareholder (or the relevant grower) dies or ceases to be a grower. 'A' class shares are not entitled to any dividend.

'B' class shares were issued to Wheat Industry Fund (WIF) unit holders on the basis of one 'B' class share for each WIF unit held. 'B' class shares have one vote per share, with 'B' class shareholders able to vote on any resolution other than the election of 'A' class directors or any resolution at a class meeting of 'A' class shareholders. 'B' class shareholders are entitled to dividends, if and when declared. 'B' class shareholders may be owned by non-growers as well as growers. However, the maximum percentage of 'B' class shares which any one person can own is 10 per cent. It is intended that 'B' class shares will be listed on the Australian Stock Exchange, giving growers a large market through which to trade their shares, and also enabling AWB Limited to raise further capital if required.

5.10.2. Contestability of service provision

In the Committee's view, it is possible that as greater numbers of 'B' shares are sold to non-growers, the interests of the grower-clients of AWBI and the grower (or non-grower) shareholders of AWB Limited may begin to diverge significantly.

The Government, as the owner of the export monopoly rights, and growers, as the main intended beneficiaries of the commercial exercise of these rights (as identified in the previous section), both have an interest in ensuring that the company to which the operation of the export monopoly has been granted is operating commercially and at arm's length from the private company from which it is employing staff and purchasing services. This affects the appropriateness of granting a monopoly to a private company.

Therefore, the Committee observed a clear need for clarification of the Service Level Agreement between AWB Limited and AWBI, including an emphasis upon the notions of demonstrated transparency and contestability

5.10.3. 'Buyer of last resort' obligation

Section 84 of the WMA currently obliges the nominated company B (AWBI) to accept all wheat offered, so long as it meets the standards for a pool operated by the company. This is referred to as the 'buyer of last resort' obligation, and applies regardless of location or seasonal variation.

There is widespread grower concern that without the 'single desk' arrangement, marketers would trade optional-origin wheat, and Australian wheat would have to compete with other origin wheat to be sold.

This obligation is seen as an important safety mechanism under the 'single desk' system for ensuring that growers can dispose of weather-damaged or poor-quality grain on the export market. There is a general industry consensus that AWBI has consistently honoured the spirit of the "buyer of last resort" obligation, and this is obviously of considerable value to growers.

However, a few points need to be made regarding this obligation.

AWBI's obligation is limited by its ability to close pools and alter standards to exclude some wheat. While farmers may still access other pools, these may not return an optimal return for their wheat.

Wheat accepted under the buyer of last resort option may be sold in a separate pool, and the return to growers would reflect the market value of their grain. This would be little different from disposing of grain under competitive marketing arrangements. However, there is concern that producers in logistically disadvantaged areas would face significant hurdles marketing this wheat even at a substantial discount.

The Committee believes that that retention of the "buyer of last resort" as a Community Service Obligation (CSO) is an essential condition of retention of the

‘single desk’ for bulk wheat exports, and justifies the granting of a monopoly to a private company so long as there is a net public benefit. However, no such obligation may apply to the bulk durum market should the recommended trial of the durum marketing arrangements go ahead.

5.10.4. Conversion of Wheat Industry Fund units to shares

The WIF was established in 1989 through a levy on sales of wheat by growers. The WIF was managed by the former Australian Wheat Board, and growers’ levy contributions and their proportional share of earnings (ie their equity in the WIF) was recorded for each equity holder.

The 1997 amendments to the WMA included new provisions to make clear the legal position that equity holders did not have a proprietary interest in the WIF or its assets. Equity holders only had those rights in the WIF which were conferred by the WMA or the associated regulations, that is, to transfer or cash-out equity in certain circumstances.

These new provisions in the WMA spelt out that equity holders did not have a beneficial interest in money or investments of the WIF, or in assets acquired using the WIF. The explanatory memorandum made clear that these changes were part of a wider scheme to give equity holders rights in companies that were broadly equivalent to their existing rights (regarding the WIF) under the WMA.

Total WIF equity reached \$607 million at its conversion on 1 July 1999 to B Class shares in AWB Limited. Approximately \$419 million of this amount was grower levy contributions with the balance being retained earnings by the WIF. Each shareholder was allocated B Class shares in proportion to their equity in the WIF. On conversion of WIF units to B Class shares the legislation provided that each shareholder was taken to have consented to become a member of AWB Limited and for the issuing of B Class shares to be protected from legal challenge.

WIF earnings were not taxable in the hands of the AWB because of the tax exempt provisions in the legislation. Depending on the tax rate that would have otherwise applied, this concession could have been worth around \$50 million or more to equity holders. Levy contributions to the WIF were tax deductible for growers. Assuming a 20 per cent marginal tax rate, this would have provided an estimated benefit for growers of about \$84 million over the life of the WIF.

The Committee discussed the taxation treatment agreed to by the Government for the conversion of WIF units to B Class shares by which B Class shares in AWB Limited were treated as capital for taxation purposes, and provision of rollover relief from capital gains tax on conversion of the WIF units to shares meant that capital gains tax on the shares would only apply when they were sold.

The conversion of the WIF into a capital base for the AWB Group enabled the Group to continue to borrow money to fund harvest loans to growers after the removal of government underwriting. The value of the ‘B’ class shares, when they are publicly listed, will be influenced by a range of factors considered by the market to impact on the stream of earnings and future dividends from AWB Limited, which will include

the timing and scope of the 2004 review into the operations of AWB Limited's subsidiary, AWBI.

5.10.5. Implications for international trade negotiations

Trade policy issues, including compliance with WTO rules as well as any possible effects of the WMA on foreign producers and/or consumers, are ostensibly outside the scope of this review, which is being conducted under the National Competition Policy.

Despite this, during its overseas consultations, the Committee was informed by several government representatives that the future of 'State Trading Enterprises' (STEs) is an important issue in WTO trade negotiations for major competitors such as the United States and the European Union. The former statutory Australian Wheat Board clearly came within the ambit of being a STE. However, statutory marketing of Australian wheat, and the statutory board, ceased on 1 July 1999.

The following is the working definition of a STE as agreed in the Uruguay Round:

'Governmental and non-governmental enterprises, including marketing boards, which have been granted exclusive or special rights or privileges, including statutory or constitutional powers, in the exercise of which they influence through their purchases or sales the level or direction of imports or exports' (source: Understanding on interpretation of Article XVII of the General Agreement on Tariffs and Trade 1994).

The WMA grants an exclusive and special right to a subsidiary company of the AWB Group which allows that company to influence the level and direction of wheat exports. Therefore it could be argued that AWBI may still be considered a STE for WTO purposes. Therefore, the Government may need to consider the implications of any change to the 'single desk' within the wider ambit of trade negotiations aimed at reducing agricultural support and protection.

A number of submissions received by the Committee argued that the world wheat market has been 'corrupted' by agricultural policies in other major exporting countries and that the 'single desk' provides benefits to growers by acting as a 'countervailing' force. The Committee accepts that these policies may have resulted in substantial overproduction of wheat, and consequent oversupply of wheat to international markets. However, the Committee does not believe that the 'single desk' can in any meaningful manner remedy this situation of oversupply, nor significantly offset depressed world wheat prices.

Recommendation 1:

The Committee recommends that the WMA be amended so that the objective(s) of the legislation are stated explicitly, to provide a common reference point for future work on wheat marketing arrangements.

References

AWB Limited 1999, *What does AWB's Privatisation Mean for You?*, May 1999, Melbourne.

AWBI (AWB (International) Limited) 2000, *Review of the Wheat Marketing Act 1989*, Submission to the NCP Review, Melbourne.

CIE (Centre for International Economics) 1999, *Guidelines for NCP Legislation Reviews*, Prepared for the National Competition Council, Canberra.

6. WHEAT EXPORT AUTHORITY

This chapter assesses the effectiveness of the separation of regulatory and commercial functions in the *Wheat Marketing Act 1989* (WMA). It first examines the regulatory functions and powers the WMA confers on the Wheat Export Authority (WEA) in relation to wheat exports. It then examines the intention of the new export arrangements, and whether the functions and powers accorded to the WEA appear consistent with this intention. Finally, the chapter examines how the new export arrangements have worked in practice.

Key sections in chapter:

- What regulatory functions and powers does the WMA confer on the WEA?
- Intention of the new export arrangements
- How have the new export arrangements worked in practice?
- Changes to the export licensing system
- Scope and process of the 2004 review
- Expanded role for the WEA
- Industry-Government forum

6.1. What regulatory functions and powers does the WMA confer on the WEA?

The former Australian Wheat Board, which operated under Commonwealth legislation with State legislative support, exercised both commercial and regulatory functions. However, this duality could not continue when the activities of the former Board were privatised. On 1 July 1999, all of the commercial wheat marketing and associated functions of the former Australian Wheat Board were transferred to AWB Limited, a grower owned and controlled company. The former Australian Wheat Board continued as a legal entity but with a new name (the WEA) and with limited regulatory functions and powers.

The WMA as amended gives the WEA two functions (Section 5(1)):

- to control the export of wheat from Australia; and
- to monitor the performance of AWB (International) Limited (AWBI) in relation to the export of wheat and examine and report on the benefits to growers that result from that performance.

Other sections of the WMA, however, limit the WEA's powers to perform these two functions.

Section 57(1) states that a person shall not export wheat unless the Authority has given its written consent. This prohibition, however, does not apply to AWBI (section 57(1A)). This removes the WEA's power to control any more than a small fraction of the nation's wheat exports. In relation even to this power, the WEA must not give a bulk-export consent without the prior written approval of AWBI (section 57(3B)); and

before giving a consent for the export of bagged or containerised wheat, it must consult AWBI (section 57(3A)). Thus, AWBI has the power of veto over the export in bulk of any wheat outside its own export pools, and potentially may also influence the WEA's decision on wheat exports if bagged or containerised.

While in theory the WEA might approve bagged or containerised shipments against AWBI advice, the WEA stated to the Committee that it was responsive to AWBI views about the need to protect key 'established' markets.

The WEA must also depend on AWBI to provide the data for it to monitor AWBI's performance.

It could be argued that because of these significant limits placed on the WEA's power to perform its specified functions, the WMA *effectively* retains AWBI as the regulator of Australian wheat exports. The WEA may be seen as an administrative agent for approving the export of small parcels of wheat outside the AWBI system and for reviewing AWBI's performance.

6.2. Intention of the new export arrangements

It is well established that to avoid potential conflicts of interest, regulatory and commercial functions should be clearly identified, and ideally kept separate and transparent.

It is clear from the discussion in the previous chapter, however, that the new export arrangements have the effect of continuing, more or less, the old arrangements under which the former Australian Wheat Board allowed the export of some wheat outside the pools, so long as (in the Australian Wheat Board's view) this did not compromise the Australian Wheat Board's own market position, or the reputation of Australian wheat.

The new arrangements aim to ensure that AWBI will continue to service and develop the main bulk markets for Australian wheat, while leaving open the possibility for other exporters to develop small or specialised (niche) markets.

There is a view (albeit one not shared by the Committee) that these limitations to the WEA's powers appear consistent with the idea that the WEA's only real function is to administer non-AWBI exports. In this view, it is not only desirable, but also necessary, that AWBI should oversight non-AWBI wheat exports, as well as being in a position to advise the WEA if the activities of other exporters are compromising AWBI's own market position, or the reputation of Australian wheat. This view is consistent with the idea that the grower owned and controlled AWBI should be the effective regulator of Australian wheat exporters.

However, this view is in conflict with the idea that regulatory and commercial functions should be kept separate, and that the WEA should be in a position to directly regulate exports.

6.3. How have the new export arrangements worked in practice?

In its domestic consultations the Committee heard frequent and severe criticism of the WEA's turnaround times to applications for export consents. The Committee also heard that the WEA 'never' approved bulk export consents.

It is important to distinguish between which of these problems might be attributed to the WEA's own internal administrative processes, and which might be attributed to the legislation.

The WMA requires the WEA to consult with AWBI before issuing each consent for bagged and container wheat exports, and to obtain the approval of AWBI before issuing consents for bulk wheat exports.

Under its own charter, AWBI is required to maximise returns to those growers who deliver to its export pools. This may in effect give AWBI an incentive to attempt to restrict non-AWBI export wheat sales in any form: bagged, container or bulk. In the case of bulk wheat, AWBI may restrict bulk sales simply by withholding export approval from the WEA. In the case of bagged and container wheat, the consultation process itself could potentially be used to slow approvals and discourage exporters from applying for consents in the first place. The fact that few people apply for consents could then be put forward as evidence there is little interest from non-AWBI exporters in servicing niche markets.

However, WEA processes for considering applications for export consent have been developed on the basis of legal advice and are considered by the WEA to be consistent with the requirements of the WMA.

The WEA's first Annual Report (WEA 2000) notes that in the three months from 1 July 1999 to 30 September 1999 (the first three months of the WEA's operation), 91 per cent of applications seeking a consent to export wheat were granted. The Committee noted that this information does not indicate what volume the remaining 9 per cent that were rejected may represent, or as noted above, how many potential applicants may have been discouraged from lodging applications in the first place by the perceived delays and biases associated with the new export arrangements.

Figures relating to a longer time period forwarded to the Committee by the WEA in September 2000 showed that approximately 87 per cent of applications for export in bags and containers were successful. The WEA's recent Annual Report 1999-2000 states that 74 per cent of all applications are processed within 5 working days, and the overall average turnaround time for decisions is 4.5 days.

Other detailed (unpublished) information supplied to the Committee by the WEA indicated that, broadly, the volume associated with those applications that were successful was significantly smaller, on average, than the volume associated with those applications that were not successful.

In accordance with the WMA, the WEA process for administering each application for consent to export wheat involves:

- receipt by the WEA of a completed application form (available on <http://www.wheatexpauth.com.au>); incomplete details require follow up by the WEA Secretariat;
- dispatch for consultation comments to the AWBI an abridged application form providing details of destination, tonnage, grade and shipping period (all other application information is treated as commercial-in-confidence);
- receipt by WEA of AWBI consultation comments on the relevant application;
- provision of material to the WEA members or CEO/Manager for an assessment against the WEA guidelines for considering applications for consent to export;
- a decision by the WEA; and
- notification of the decision to the applicant, and where a rejection is the outcome, the provision of advice for the rejection against the guidelines.

In order to expedite the processing of applications for export consent, almost all application correspondence is handled by facsimile.

To assist with the process of considering applications AWBI is provided the opportunity to supply market briefs, which include AWBI's strategies in a market. At regular intervals the WEA reviews the AWBI market briefs and requests an update as appropriate. The WEA also relies on information obtained from the exporter making the application.

The WEA also uses other sources to gain market information such as the Department of Foreign Affairs and Trade (DFAT), Austrade and overseas posts, Australian based trade commissions, Australian Bureau of Statistics (ABS), Australian Bureau of Agricultural and Resource Economics (ABARE), Australian Quarantine and Inspection Service (AQIS), and embassies and High Commissions.

Overall, the Committee came to two main conclusions about how the new export arrangements have worked in practice.

The first is that the current system of granting export consents on a case by case basis has introduced delay and uncertainty into the process of clearing non-AWBI wheat for export. Such delay – apparently small in most cases but with the potential to be large – appears to act as an impediment to the development by non-AWBI wheat exporters (largely grower owned and operated) of small or niche markets for wheat outside the main bulk markets being maintained or developed by AWBI. As a consequence, there may be a loss of business for Australian companies and export income for Australia.

The second is that, whereas staff in the former statutory Australian Wheat Board may have had the authority to grant applications 'on the spot' and so give a potential exporter a quick decision, the new exporting system (intended to be more impartial and more 'arm's length'), in fact introduces more decision stages into the assessment process and consequently, greater potential for delay.

Both of these aspects are likely to increase the compliance costs and paper work burdens on small businesses wanting to export wheat.

6.4. Changes to the current system

The Committee considers there are two options to deal with the problems evident in the current system: reduce the number of stages in the decision process, and reduce the frequency with which decisions are required. In chapter 8, the option of reducing the number of stages in the decision process by giving the WEA more autonomy to grant export applications is explored in more detail. In practice the Committee sees this being achievable by modifying or removing the requirement in the WMA for the WEA to consult with AWBI before granting applications for the export of wheat in containers or bags or to obtain written consent from AWBI before granting applications for the export of wheat in bulk.

The option of reducing the frequency with which decisions are required is also explored later in this chapter. In practice the Committee sees this as being achievable by the WEA replacing its current export consent system by an export control system where the exporter is licensed. Appendix One contains some suggestions for an export licensing regime that would focus on maintaining quality control, exporter reputation and destination discipline in the interests of the entire industry.

6.5. Scope and process of the ‘2004 review’

Section 57 (7) states that before the end of 2004, the WEA must conduct a review of certain matters, and give the Minister a report on the review. These matters are nominated company B’s export operations, the conduct of nominated company B in relation to consultations for export consents, and the granting or withholding of approvals for export consents.

In chapter 5, the Committee recommended that the process of the ‘2004 review’ should be clarified by government.

Growers now have substantial equity in AWB Limited, but have had limited opportunity to divest this equity. Since 15 January 2000 there has been an interim share trading mechanism administered by the AWB Limited Share Registrar (the Matching Facility). Grower equity in AWB Limited can also form the basis of loan collateral, and would then be independently valued by the financial provider. The perceived value of this equity can be affected by the financier’s assessment of the value and business performance of AWB Limited. Indeed some share offers have been substantially below the Matching Facility’s weighted average trading price. The net present value of the ‘single desk’ arrangements to AWB Limited is currently capitalised in this evaluation, discounted by the perceived risk of AWB Limited losing the ‘single desk’. In other words, as the *perceived* risk of losing the ‘single desk’ goes up, the share value may go down, and vice versa.

AWB Limited has stated that it plans to float its B-class shares in either 2001 or 2002. This will give growers the much-awaited opportunity to either hold shares as a commercial investment, or divest them on the open market and realise their equity. It is therefore important for the process of the 2004 review to take into account the need to preserve as much of the value of grower equity as possible.

The 2004 WEA review is the most appropriate vehicle for post-float reassessment of the 'single desk', and should therefore be expanded in scope and resources. This would create a stable environment for liquefying grower equity through the float process, but would not artificially extend the 'single desk' beyond that period required to achieve this objective without first reviewing the cost/benefit involved according to criteria established by this review.

The Committee is of the view that the nature and scope of the expanded 2004 review should be settled within 90 days of Government accepting this recommendation, and strict deadlines imposed on the process. The current review has provided detailed evidence and consultation-based recommendations that allow the WEA, in consultation with Government and industry, to set out the framework for the review and guide the parties to a acceptable set of performance indicators by early 2001. The WEA would then be able to assess AWBI's performance on an ongoing and transparent basis against these agreed indicators, and reporting on an annual basis on AWBI's progress. Following float of the B-class shares, the market would be able to use the WEA reporting to assess the risk of AWBI retaining or losing all or part of the 'single desk' in 2004. The market's assessment of the subsequent capital gain or loss to AWB Limited will be reflected in the share price on an ongoing basis.

There are a number of benefits to growers in this approach:

- instead of the outcome of the 2004 review being seen as non-transparent 'sovereign risk' (caused by government), clear and transparent performance targets would allow growers and the market to assess AWB Limited's actual business performance on an ongoing commercial basis ('commercial risk'); and
- the share value of the 'single desk', currently capitalised, would come to reflect the discounted net present value of AWB Limited's business performance against targets related to retention of the 'single desk' benefit. The market should continually assess this with the share price being adjusted accordingly. Grower equity exposure should therefore depend on transparent and commercial perceptions of AWB Limited's business performance and not on the perceived risk of a non-transparent government decision in 2004.

The performance indicators should address at least the following areas:

- single desk price premium performance; notwithstanding that the Committee notes there are conceptual problems in using various methodologies, such as premium pricing, market mix, pricing discipline, fob comparison, pricing to market;
- marketing performance, including market development, share and penetration assessed against marketing costs, and customer satisfaction;
- hedge performance for commodity and foreign exchange risk;
- level of carry-over stocks;
- maintenance of quality standards for bulk exports;
- discharge of Community Service Obligations tied to the 'single desk' such as providing information to the R&D sector and performance as the "buyer of last resort"; and
- demonstrated transparent contestability of services provided to AWBI, including administration, finance, bulk handling and logistic services, to minimise pooling charges and thereby maximise returns to growers.

The Committee regards it as important that the performance indicators assess each area as part of the creation and operation of the Australian wheat marketing value chain rather than assessing each area in isolation. The WEA should state which of these performance indicators it intends to use, hopefully building upon the knowledge database established in this review.

The Minister's second reading speech indicated that the 2004 review, whilst not part of the NCP legislation review process, should be conducted in accordance with NCP principles. The Committee strongly endorses this approach.

The Committee is also of the view that the Government should ensure that there is a legislative mechanism to guarantee that WEA receives accurate and relevant data on a timely basis so that the organisation can discharge its performance monitoring responsibilities. The Committee noted the delay in agreeing on a mutually acceptable basis for the WEA to be supplied with the AWBI-AWB Limited service agreement, and observes that an independent regulator should have absolute power to receive such information as it deems necessary to carry out its statutory function. The Committee believes that *Part 4 – Inquiries and Reports of the Office of the Regulator-General Act 1994* (Victoria) provides a good model for these powers.

The 2004 review process must be independent, open and transparent. It should have a commercial orientation to ensure that the review focuses on the future strategic and commercial of the 'single desk' export marketing arrangements, and is not merely compliance-based. The review should be paid for by AWBI, and should encompass the entire industry rather than just the 'single desk'.

6.6. Expanded Role for the Wheat Export Authority

As a consequence of the improvements recommended in this report, the WEA would have the following responsibilities:

- annual assessment and reporting of the marketing performance of AWBI through established performance criteria;
- issuing export licences for container and bag exports during the trial period;
- issuing export licences for bulk durum exports during the trial period;
- monitoring the performance of licensed exporters; and
- dispute arbitration in the first instance when applications are unsuccessful.

This could require an expansion in the resources available to the WEA as well as a reassessment of the skills base of the WEA Board and Secretariat. The Government should take into account in making future appointments to the WEA Board the need to ensure its complete independence.

The Committee understands that \$6 million has been made available to the WEA until 2004, which includes the costs of the 2004 review. Given the Committee's recommendations relating to the 2004 review, and the licensing arrangements, this will not be sufficient, and should be addressed by the Government.

Any activity relating to the 'single desk' should be funded by AWBI, with any other activities funded on a cost-recovery basis.

6.7. Industry-Government Forum

A number of participants in the wheat industry have identified the need for an industry-government forum to provide a flexible and adaptive framework for bringing key industry organisations together with government to discuss industry policy issues and processes, under the leadership of an independent chair. There is a clear role for government to provide such a policy leadership role within the industry.

This forum would discuss and report to government on issues such as relevant performance indicators for the 2004 review, wheat classifications, quality standards, hygiene and quality assurance, as well as working with government to develop the broader strategic direction of the industry. It would include consultative and communications mechanisms to enable all stakeholders to participate in the future of the industry.

The work of the forum could be facilitated through prepared papers and reports as well as meetings. The views and expertise of the membership would be vitally important, as would the involvement of outside specialists as required. The forum could include several technical sub-Committees to further facilitate the input of relevant experts.

Such an industry forum would not need enabling legislation, as it would have no regulatory powers, and would be funded jointly by industry and government. Initially its membership would include the Commonwealth (AFFA and the WEA), State agriculture departments, AWB Limited, other exporters and cooperatives, processors and domestic users, growers and grower representative groups such as the Grains Council of Australia (GCA), bulk handling and logistic companies, and researchers such as the Grains Research and Development Council (GRDC).

Initially an independent person with strong business credentials should be appointed to chair the industry forum. While the WEA should participate in this forum, it would not be appropriate for it to lead the forum given its regulatory role.

Recommendation 2:

The Committee recommends that the WMA be amended to ensure that the WEA is totally independent in carrying out its functions, and recommends consideration of the following:

- **the system of administering non-AWBI exports of wheat be simplified; and**
- **board members be selected with an increased emphasis on business skills such as finance, marketing, and business management.**

Recommendation 3:

The Committee recommends that the WEA introduce a simplified export control system for a three-year trial period where:

- **it issues annual licences on a fixed-fee basis to exporters who can demonstrate that they meet certain criteria including integrity, competency, financial standing, and a commitment to providing required information;**
- **such licences include appropriate penalties for non-compliance with the terms of the licence; and**
- **there is an appeal mechanism against rejection of a licence application, or the withdrawal of a previously approved licence.**

Recommendation 4:

The Committee recommends that:

- **the process of the 2004 review should be clarified within 90 days after the Government has announced its response to the NCP review's recommendations, and this process clearly communicated to the Minister and stakeholders, followed by annual progress reports as well as the final report as scheduled in 2004; and**
- **the review incorporates NCP principles in its assessments.**

Recommendation 5:

The Committee recommends that:

- **the Government convene a continuing joint industry-government forum to discuss industry policy issues and processes, including relevant performance indicators for the 2004 review, under the leadership of an independent chair; and**
- **this forum would be jointly funded by industry and Government, and would not exercise regulatory powers.**

References

WEA (Wheat Export Authority) 2000, *Annual Report 1998-99*, Canberra.

7. THE PUBLIC BENEFITS TEST

The guiding principle set out in the Competition Policy Agreements (CPA) is that legislation should not restrict competition unless it can be demonstrated that the benefits of the restriction to the community as a whole outweigh the costs, and the objectives of the legislation can only be achieved by restricting competition.

The review's terms of reference 4(e) and 4(f) require the independent Committee to:

- analyse and quantify the benefits, costs and overall effects on businesses involved in the Australian wheat industry and the community generally of the existing *Wheat Marketing Act 1989* (WMA) arrangements compared to relevant possible alternatives to the wheat export arrangement in the WMA, including non-legislative approaches; and
- identify the impact on different groups likely to be affected by either the continuation of the WMA arrangements or implementation of viable alternatives.

This, the 'public benefit' test, is undertaken in this chapter.

Key sections in chapter:

- Framework for evaluating benefits and costs and their impact
- Main benefit/cost areas
- Estimated changes in net welfare
- Impacts on stakeholders

7.1. Framework for evaluating benefits and costs and their impact

7.1.1. Overview

The National Competition Policy (NCP) recognises that there are significant advantages provided by competitive markets and hence requires clear proof that any regulatory restrictions on competition generate sufficient benefits to compensate for the loss of these advantages. The onus of proof for retaining anti-competitive legislation is placed on those favouring retention of the legislation - it must be demonstrated that the benefits of the restriction are greater than the costs if retention is to be recommended (Productivity Commission 2000).

The current legislation restricts the entry of firms into the export market for Australian wheat and essentially allows there to be only one receiver and seller of export wheat in bulk. The Committee is being asked to assess whether the Australian community as a whole would be better off with such a system, or with a system in which there are multiple buyers and sellers of Australian export wheat in bulk, *including* the existing single seller, who would be obliged to compete with new entrants to obtain wheat to be sold on the bulk export market.

7.1.2. Benchmark for comparison: a freely competitive scenario

The guidelines for NCP legislation reviews (CIE 1999) state that to assess the benefits and costs of restrictions, it is necessary to identify their theoretical or ‘in principle’ impacts. This requires being able to establish a framework for assessing what commercial environment may exist without the legislation (the ‘counterfactual’ situation). The difference between the current ‘with’ situation and the more hypothetical ‘without’ situation will identify the ‘in-principle’ impact.

The guidelines suggest that establishing the ‘without’ framework is the most important and difficult task in conducting a review, since the ‘without’ situation by definition does not exist, and must be constructed from theoretical evidence or from observation of similar situations in other industries or countries.

The guidelines also caution against underestimating the benefits of the ‘without’ situation which, although possibly large, are likely to be diffuse throughout the community and often difficult to detect and appreciate. On the other hand, the negative effects, even if small, may be more concentrated and obvious.

AWB (International) Limited (AWBI) claimed that the Committee should have adopted the criteria used by the Australian Competition and Consumer Commission (ACCC) for assessing anti-competitive conduct under the *Trade Practices Act 1974* (TPA). However, this fails to recognise that the current review is being conducted under the National Competition Policy, according to specific NCP guidelines. Section 57(6) of the WMA specifically authorises the export of wheat and anything that is done by AWBI under s.57 for the purposes of the TPA, making reference to TPA guidelines completely irrelevant. Also, the ACCC is more concerned with competitive situations rather than legislated monopolies.

7.1.3. Restrictions to competition

The Australian market for export wheat in bulk is not competitive. Commonwealth legislation, the WMA, restricts competition, primarily by:

- Restricting the entry of firms – the WMA gives one firm an effective monopoly on the export of bulk wheat; and
- Creating discriminating advantages – by excluding choice, the WMA discriminates against various groups, including growers who do not, or do not wish to, market their wheat through the monopoly exporter.

Since export bulk wheat constitutes a significant proportion of the volume of grain produced and traded in Australia each year, giving one firm an effective monopoly on the export of bulk wheat affords that firm a dominant position in Australian grain marketing.

Having one firm dominate Australian grain marketing may further restrict competition, in a number of ways:

- domestic prices and production – the dominant firm may be able to influence domestic prices through its purchasing activity and stock holding, and its

access to information on stocks, and to influence production through the price signals it sends to growers;

- quality standards – the dominant firm’s standards may become the de facto standards for all Australian wheat;
- promoting Australian wheat – there may be little incentive for firms other than the dominant firm to advertise or promote Australian wheat, to innovate, and to develop new markets; and
- market for inputs – the dominant firm may be able to influence the market for wheat marketing services, crop financing, and grain storage, handling and transport, plant breeding, and seed sales. In particular, there is the potential to leverage its monopoly position as a marketer in the supply chain to compete unfairly with other participants in the supply chain.

If the firm were dominant solely by virtue of its superior performance, this may not be an issue under NCP. However, if that firm is assisted to maintain its dominant position by virtue of protection afforded by legislation, this is an issue.

7.1.4. Factors affecting revenue and cost streams

In any assessment of benefits and costs, the CPA requires a very broad range of economic and social factors be considered.

The guidelines suggest an NCP review should attempt to quantify the positive or negative impact of removing the legislation by considering the likely effects of any removal on:

- revenue streams – likely changes to industry output, producers’ gross revenues and consumers’ incomes;
- costs streams – likely changes to the supply of inputs and costs of production
- Government – likely changes to the Government’s fiscal position;
- the community overall – the net balance after considering producer, consumer and taxpayers impacts; and
- other – other qualitative or quantitative impacts.

The Committee engaged the Allen Consulting Group (ACG) to undertake two technical assessments of the economic and social effects of the legislation. To provide an indication of economy-wide effects, ACG also undertook a sensitivity analysis of key benefits and costs using a general equilibrium model of the Australian economy. These economic and social assessments covered:

- the effect on producers’ revenue streams;
- the effect on consumers’ revenue streams;
- the effect on cost streams;
- other effects (social and environmental); and
- the effects on the community overall.

The technical assessments are available as companion documents to this report.

7.1.5. *Effect on stakeholder groups*

The guidelines suggest the key groups which should be considered in the impact analysis include producers, processors, retailers, consumers and the community as a whole.

In the context of wheat marketing arrangements, the Committee has concentrated its attention on:

- producers (distinguishing, where necessary, between those who deliver wheat to AWBI's export pools, and grain producers generally, including those selling wheat on the domestic market or exporting wheat in bags or containers);
- consumers (distinguishing, where necessary, between intermediate product consumers such as flour millers and stock feed manufacturers, direct users of grains such as stock feeders, and final consumers of wheat-based and intensive livestock products); and
- the economy generally (distinguishing, where necessary, between effects specific to regional and rural Australia, and more effects on the whole economy, particularly export activity).

7.1.6. *Benefits and costs considered in detail in this chapter*

In considering which benefits and costs to assess in detail, the Committee was guided in large measure by stakeholder submissions, expert reports and the consultation process. Many submissions argued that wheat growers and the Australian community as a whole would be better off with a system which permits only one receiver and seller of export wheat in bulk (the existing system, with some selected modifications to improve its administrative efficiency). Submissions which argued this point of view included those from AWBI – the current holder of the bulk wheat export monopoly – the Grains Council of Australia (GCA), and State farmers' federations.

Other submissions argued that wheat growers and the Australian community would be better off with a system in which there were multiple buyers and sellers of Australian export wheat in bulk, including the existing single seller. Submissions which argued this point of view included those from the Productivity Commission, and the Joint Industry Submission Group (see chapter 4 for a summary of the main points made in these and other submissions).

In considering benefits and costs, the Committee also sought guidance from previous NCP assessments, past economic studies, commissioned research, and extensive consultation and discussion with stakeholders (see Chapter 2).

Above all, the Committee was concerned to try to evaluate the merits (by weighing up the benefits and costs) of alternative marketing *systems*. For example, in its first submission to the Committee, AWBI (2000) argued that the current *system* (under which growers wishing to sell wheat for bulk export are required to deliver to the export pool of a single receiver) provides net benefits to growers because, as the current manager of the system, AWBI believes it is able to obtain higher gross returns for export wheat in bulk, through:

- capturing the value added through the vertical integration of market operations;
- obtaining price premiums through better marketing, and also some price discrimination;
- promoting Australian wheat;
- maintaining market access for all growers, through direct customer relationships, and also through using agents in some markets; and
- maintaining superior access to information, enabling it to know where its wheat is, and what quality it is (logistics), match supply with demand (market intelligence), know competitor pricing and customer preferences (commercial intelligence), calculate the least cost path to market (transport options), and capture freight spread differentials (marginal costs).

The AWBI submission also claims that the ‘single desk’ system is able to reduce growers’ marketing costs by:

- helping growers better manage risk;
- providing competitive crop financing and funding;
- enabling long term quality control of Australian wheat;
- generating cost efficiencies in freight, storage and handling; and
- supporting niche marketing.

By obtaining higher gross returns for export wheat in bulk and reducing growers’ marketing costs, AWBI claim to be able to maximise net returns to growers. By maximising net returns to growers, the community as a whole benefits from the income flow-on effect to rural towns and communities.

Regarding possible costs imposed on other sections of the community, such as domestic wheat consumers, AWBI argued that its operations on behalf of growers had no, or negligible, negative effects on wheat processors and final consumers. If some costs were imposed, these were more than outweighed by the net benefits being obtained by wheat growers so that the overall community effect was positive (AWBI 2000).

AWBI, in its supplementary submission, also brought the Committee’s attention to its views as to the marketing advantage and export benefits to Australia from permitting only one Australian seller of bulk wheat in the international market. These benefits include:

- access to the world market ‘despite massive government intervention causing distortions’;
- avoidance of annual carry-out and associated costs;
- continued increase in market share and opening up of new markets; and
- access to ‘superior outcomes’ in terms of risk and position management for sales.

The GCA and State farmers’ federation submissions largely echoed and reiterated the view that a system which permits only one receiver and seller of export wheat in bulk provides net benefits to wheat growers and the Australian community overall. These

submissions also drew the Committee's attention to the benefits of having control and ownership of the single receiver and seller reside in growers' hands.

In preparing to assess the list of claimed benefits above, the Committee had first to separate those which it considered are unique to a single seller system (and which would be lost under a multiple seller system) from those which are not unique to a single seller system, and which the existing single seller should still be able to obtain – albeit in the face of more competition – within the context of a multiple seller system.

For example, regarding the argument that benefits are obtained through the vertical integration of market operations, the Committee would expect that any large firm in a multiple seller situation would actively seek to control as much of the marketing chain as it assessed to be cost effective, to obtain price premiums through better marketing, promote its product, maintain customer relationships, gather information, and shield its own information from commercial rivals. A monopoly is not necessary for a firm to seek to increase its gross returns through any of these means. In the Committee's view, the main means through which AWBI (as a single seller) may be able to obtain higher gross returns which may not be available to it (and to those growers choosing to deliver to it) in a multiple seller system would be price discrimination - discussed in detail later in this chapter.

Concerning growers' marketing costs, the Committee could not see why a single seller should necessarily be in any better position than multiple sellers to offer services such as risk management products, crop financing and underwriting, to obtain cost efficiencies in grain storage, handling and freight, or to promote niche marketing. The Committee sees the benefits of an integrated strategy to enable the long-term quality control of Australian wheat, but considers there are ways to implement such a strategy other than devolving control to a single seller. Regarding grain storage, handling and freight, the Committee received a number of submissions which argued there were good reasons to believe these costs would be lower in a multiple seller system than in a single seller system, rather than the reverse, as argued by AWBI and others. These submissions argue that the privileged position of AWB Limited restricts the opportunity to vertically integrate without infringing trade practices legislation. In view of the large cost savings potentially obtainable for growers, the Committee examines this question in some detail later in this chapter.

Regarding possible costs imposed on other sections of the community, such as domestic wheat consumers, the Committee received a number of submissions which argued that the operations of the monopoly wheat exporter did in fact impose costs on consumers, and examines this question in detail later in the chapter.

In looking at social costs, primarily the income flow-on effects to rural towns and communities, the Committee's view is that the net effect will be dictated largely by whether the single-seller system acts to increase or decrease grower net returns relative to an alternative multiple-seller system. The Committee examines this question in detail later in this chapter, primarily through the results of sensitivity analyses conducted by ACG using a general equilibrium model of the Australian economy.

On the stated marketing advantage and export benefits to Australia brought to the Committee's attention in AWBI's supplementary submission, the Committee has the following views. There is ample evidence that government support schemes for grain production and exports by some of the main grain exporting countries has probably resulted in a different pattern of grain production, consumption, trade and prices than would have occurred had this government support not occurred. The net result is an oversupply of grain resulting in distorted prices. In all likelihood, Australian wheat growers' returns may have been higher had this government support not occurred. However, the real question is whether Australia is able to influence other exporters' policies by any means other than those already being pursued – namely, active participation in world trade negotiations. As noted in chapter 3, with a long-term wheat market export share of no more than approximately 15 per cent, it appears very doubtful whether anything Australia does in the market would have any impact on the other exporters' policies. The Committee fails to see how the current single seller system provides any means to 'countervail' other exporters' policies, except perhaps by offsetting the lower world prices through the 'single desk price premium'. The Committee also considered that so long as the current single seller continued to attract sufficient supplies from growers wishing to use its services to sell their wheat, then the current single seller's market access, market share, and ability to manage risk or sales should not be adversely affected by it operating as one seller within a multiple seller system.

Furthermore, in chapter 3 it was noted that the recent increase in Australia's wheat export availability has resulted from an increase in wheat production in the latter half of the 1990s. Possible reasons for this increase included the spike in wheat prices in 1995-96, the relative weakness of livestock product prices, and the high yields being achieved with wheat. AWBI has made the point that it has been able to sell this increased export availability into a static world market and thereby avoid building up Australian wheat stocks and incurring the associated costs of stock carry-over. The Committee is of the view that the decision as to whether or not to hold or carry stocks should be a commercial decision based on weighing the expected present costs of stock carryover against the expected present value of the grain. Again, the Committee does not see why a single seller necessarily would be able to make any more informed decision in this regard than a number of sellers acting independently.

In summary, the main areas of benefit and cost the Committee has decided to examine in the remainder of this chapter involve the central propositions that, relative to the commercial environment that may exist if the current legislation were removed, the current arrangements:

- allow a single seller to obtain 'single desk price premiums' and to pass these back to growers, so that growers would 'lose' if the current legislation were removed;
- force domestic grain consumers to pay higher prices, on average, so that domestic grain consumers would 'gain' if the current legislation were removed;
- either allow a single receiver and seller to take advantage of economies of scale and scope to realise savings for growers across a range of grain marketing services, so that growers would 'lose' if the current legislation were

removed, or alternately, raise costs in the supply chain by discouraging competition, innovation and change in grain handling, so that growers would ‘gain’ if the current legislation were removed; and

- provide revenue and services which allow growers to continue wheat farming, supporting regional income and employment in the wheat belt, so that rural communities and towns would ‘lose’ if the current legislation were removed.

7.2. Main benefit/cost areas

7.2.1. ‘Single desk price premiums’ – do they result in additional export revenue?

Definition of terms

The ‘Single Desk Premium’ Defined

The Committee defines the ‘single desk premium’ as the difference in the cif price in a given market for the exact same parcel of wheat bundled with an identical set of marketing services and special conditions of sale, between current arrangements with a ‘single desk’ and those that would exist without a ‘single desk’.

There are various factors that affect the price obtained for grain, including numerous ‘quality’ attributes, conditions of sale (eg rebates, credit arrangements), and bundled marketing services. The costs associated with providing any or all of these factors affect the net farm-gate return to growers. These price factors also may exist under competitive arrangements, but the trade-off between price and associated costs that may impact positively or negatively on realised market price is not transparent under the ‘single desk’ marketing system. Factors that may impact on price include:

- **Variety:** Some varieties have particular characteristics for which customers are willing to pay extra, for example milling characteristics such as flour colour. This is increasingly important where Australian wheat is sold as a branded food ingredient rather than a bulk commodity.
- **Characteristics:** Other characteristics of the grain can impact on price, for example pesticide-free and disease-free status (clean), environmentally sustainable agricultural practices (green), organic status, biotechnological advantages, etc.
- **Moisture content:** Australian grain is characteristically dry, which may increase its inherent value. Consistency of moisture content is an important factor for some buyers.
- **Protein content:** Wheat is partly graded and priced according to protein content. However, if a high grade is sold for a lower price, protein over-delivery to specification can occur, resulting in a lower return.
- **Cleanliness:** Lower “dockage” (extraneous materials) could result in a higher price, but this must be measured against the cost of cleaning.
- **Strategic Supply:** Markets such as Japan require a steady supply of grain regardless of seasonal variation, meaning that sufficient stocks of that quality of grain must be carried over from year to year. While this may result in a higher price, it also transfers the cost of storage to the seller and imposes an opportunity cost.

- Segregation: Closely related to varieties, moisture content and protein content, segregation of the crop may yield a premium because it tailors wheat to the needs of the buyer. However, each new segregation imposes a cost in bulk handling and logistics, as it reduces storage efficiency relative to undifferentiated wheat. Therefore, assessment of a new segregation must balance the improvement in price against the increased cost of storage.
- Grade Dependence: End-users may become dependent on certain grades of wheat for their requirements, and as this lessens the potential for easy substitution, they may be willing to pay more to ensure supply. Downstream investment in milling facilities may assist this, as would close cooperation to meet customer requirements. The extent of any price increase must be carefully judged so as not to encourage the development of effective substitutes or alternative originators.
- Freight differential: Australia is closer to certain markets than our major competitors, allowing us to take advantage of lower shipping costs to competitively price our wheat. While the freight differential would be available without the 'single desk', the issue is whether it maximises the advantage.
- Freight costs: Whether the wheat is sold fob or cif affects the price. cif sales can achieve better returns where there is significant control over shipping, but assume significant risk.
- Seasonal advantage: Because the Australian harvest is counter-cyclical, Australian wheat may be in demand at times when other origins are not available, thus commanding a higher price due to lack of effective substitutes. This depends on effective marketing, timing sales and position management.
- Restricted imports: The importing arrangements of some countries, in particular quota based imports, may provide preferential or pre-determined access for Australian wheat. With import competition reduced, there may be scope for increasing the price. However, this must be measured against the cost of maintaining preferential market access. It is more likely that the 'single desk' can maximise this advantage.
- Financial arrangements: The provision of favourable credit terms can attract a higher price. This may be compensation for an increased credit risk assumed by the seller or the cost of finance.
- Pre/post sales service: Australia provides a high level of before and after sales service, guaranteeing prompt attention to and resolution of any problems. However, this costs money. Customers may pay less for wheat from other countries, as they are taking risk upon themselves. Any higher price obtained by Australia is the cost of transferring risk from the buyer to the seller, and by extension to growers.
- Demurrage: Delays in loading can incur penalties, known as 'demurrage'. 'Single desk' control of port logistics can transfer the risk of demurrage away from the buyer to the seller. The issue is whether there is a price premium or other advantage in return for the acceptance of this risk.
- Market Power: The theoretical potential for a 'single desk' exporter to raise the price of certain grades of wheat by controlling the quantity sold to a particular market. This power is determined in part by lack of other sellers of the same grade, aided by imperfect arbitrage across markets, and inhibited by the existence of close substitutes such as other similar grades of wheat, alternative originators or substitute non-wheat products. In other words, the ability to increase prices through the exercise of market power is enhanced to the extent that the 'single desk' seller holds stocks of the wheat grade in demand, and is inhibited to the extent that the buyer can choose other grades or origins of wheat or non-wheat products.
- Countervailing Power: The exercise of seller's market power in negotiations as a defensive measure against the exercise of buyer's market power (the ability to lower the price of certain grades of wheat by controlling the quantity bought from a particular origin).

- **Negotiated Advantage:** The seller's ability to negotiate a higher price, based on their understanding of markets, information inequality, the exercise of market power, personal relationships, timing of sale, negotiating ability etc. It costs money to acquire marketing expertise and negotiating ability, access market intelligence and maintain personal relationships. Therefore any negotiated advantage must at least compensate these costs.

In considering submissions on the issue of price premiums, the Committee noted differing definitions for key terms including 'market power', 'negotiated advantage', 'countervailing power', and 'price premium'. Consequently, some discussion of definitions is warranted at this point.

The Committee sees 'market power' as the theoretical potential for a 'single desk' exporter to raise the price of certain grades of wheat by controlling the quantity sold to a particular market. This may be possible because the demand in some markets for imports of Australian wheat is less than perfectly elastic, and there is imperfect arbitrage across markets. Market power is likely to be reduced by the existence of substitutes such as other similar grades of wheat, alternative originators or substitute non-wheat products.

By comparison, the Committee notes the AWBI definition of 'negotiated advantage' as the actual increase in the price received for grain which is due to the seller's ability to negotiate a higher price, based on a number of factors which include their understanding of markets, information inequality, personal relationships, timing of sale, negotiating ability, and finally, the exercise of market power. Since it costs money to acquire marketing expertise, negotiating ability, access market intelligence and maintain personal relationships, any actual negotiated advantage must at least compensate for these costs.

The Committee sees the term 'countervailing power' as referring to the exercise of a seller's market power in negotiations as a defensive measure against the exercise of buyer's market power (ie the ability to *lower* the price of certain grades of wheat by controlling the quantity *bought* from a particular origin).

Finally, a pivotal issue is whether allowing only one seller to export Australian bulk wheat allows that seller to capture a 'price premium' that would be lost if more than one seller were allowed to export bulk wheat. Debate on this key question has been confused by use of the term 'price premium' to refer to different concepts. For example, as discussed in more detail later in this chapter, the AWBI submission uses the term 'price premium' to describe the difference between the fob price for exports of wheat from Australia and the fob price for exports of an equivalent grade of wheat from the Pacific North West of the United States (US). The Committee recognises that such use of the term 'premium' is commonplace in grain marketing. However, when discussing benefits and costs, the Committee prefers to use the term 'single desk price premium' to refer *specifically* to the difference in the price that would be received from the export of a specific parcel of wheat under the current single seller system vis-à-vis the price that would be received from the export of the same parcel of wheat bundled with the same services and conditions of sale under an alternative multiple seller system.

Competitiveness of the world market

Under the current arrangements, AWBI is both the only buyer of wheat for export from Australian growers, and the only seller. As the only buyer, it accepts the obligation to be the buyer of last resort, and so does not control the aggregate volume of each grade of wheat for export. However, it effectively controls the characteristics of all Australian wheat sold for export, as well as the allocation of the volumes between sales to different destinations. Because it is the only seller of Australian wheat, that marketer will be able to set the asking price for Australian wheat in each market without other Australian exporters being able to undercut it. However, the single seller cannot control other exporters' supplies of similar wheats or close substitutes, or domestic grain production in grain importing countries. If the single seller sets the asking price for Australian wheat too high, it runs the risk that its customers will switch to other suppliers.

As noted in chapter 3, there are five major wheat exporters - the US, Canada, the European Union (EU), Australia and Argentina. Other countries such as Saudi Arabia and Turkey also export wheat. Thus, any wheat importer should have a ready choice of alternate suppliers. Special circumstances where Australian wheat may have an advantage over the competition because it is the only seller are discussed below.

Potential for 'single desk price premiums'

- **Taking advantage of location or season**

In some markets, Australia may have a geographic or seasonal advantage, which could translate into lower transport or storage costs for Australian exporters. If there were many Australian exporters, they may undercut each other and compete the 'premium' away, whereas a single exporter may be able capture the premium by limiting exports to a particular market to the point that its selling price was just below that of its foreign competitors. However, to do so would involve selling less wheat to what is most likely a high priced market for Australia, and consequently having to sell more wheat to other possibly lower priced markets. Moreover, there is a risk that foreign competitors may in fact be able to cut their costs, and bid lower to achieve the sale. An Australian exporter would then have to match these lower prices. This may happen irrespective of whether there was one Australian exporter, or many.

- **Differentiating the product**

By creating a differentiated commodity or product type for which there is no close substitute, a supplier could dominate a particular, narrowly defined market. However, if higher than normal profits are being made, overseas suppliers will try to copy the successful product. For instance, wheat breeders in the US are trying to breed white wheats that match the quality attributes of Australian white wheats. Some 'brand' products may be able to be sold at consistently higher prices if they offer better quality or other characteristics for which consumers are prepared to pay. However, producing a higher quality product generally requires more processing or other 'value adding' activities, which in turn increases the cost of production. It is difficult to see that a single exporter would have a better chance of making the right quality/price choice than any other exporter with a good knowledge of the market.

- **Taking advantage of the importer's trade restrictions**

Some importing countries try to protect their (often high-cost) domestic producers by restricting imports, pushing up the domestic price to consumers. They may then allocate a share of the protected market to particular exporters, who may be able to capture 'quota rents' – the difference between the high domestic producer price and the lower world export price. While it is relatively easy for the importing country to capture these 'quota rents' itself, it may in fact allow them to flow back to its foreign suppliers, possibly in return for assurance of supply.

- **Countering importer buying power**

If a large importer restricted its purchases of Australian wheat in order to push down the export price, a single seller could respond by constraining its own exports in an attempt to push prices back up ("countervailing power"). However, if the large importer could simply switch suppliers without incurring higher prices, the single seller would simply lose market share.

Even though there are single purchasers in some markets to which Australia exports wheat, in the main, these single purchasers use competitive processes to acquire wheat. Therefore the price for Australian wheat is not necessarily depressed by the existence of 'single desk' importers. There are many alternative outlets, therefore the ability to lower price is at best very limited. Moreover, such markets, which can be characterised as price sensitive, will by definition purchase from the lowest price supplier. Only in exceptional circumstances will the lowest price on offer be an inflated price set by a 'single desk' seller, as there are a number of competing exporters.

- **Participating in exporter 'cartels'**

If Australia shared a market with another large exporter, both exporters could attempt to influence prices in that market by jointly agreeing to limit supplies. However, as already discussed, if the importer could simply switch to a third supplier without incurring higher prices, the 'cartel' would just lose market share. Even if there was no third supplier in the short run, history suggests cartels tend to break down in time as their members start to 'cheat' on each other.

The existence of 'stable' market shares appears to be the exception rather than the rule, however. For example, while the US, Canadian and Australian shares of the Japan market have been relatively stable over a number of years, in other markets such as Iran and India there are large shifts in major exporter shares from year to year. The Committee found no credible evidence of the existence of exporter cartels.

- **Countering export subsidies**

Some large international exporters have used targeted export subsidies to try to expand sales to particular markets, for example, the US Export Enhancement Program (EEP) through the early 1990s. Exporters such as Australia, which does not have such schemes, have an incentive to try to divert supplies to unsubsidised markets and receive higher prices. However, other foreign exporters have the same incentive, and it may be expected that buyers in the 'unsubsidised' markets would be able to bid prices down.

Other sources of 'premiums'

Any wheat exporter has the option of bundling additional services with their product and then trying to ask a higher price for the 'package'. Such services may include:

- flexible and reliable delivery;
- quality assurance;
- product differentiation;
- guaranteed security of supply;
- meeting product specifications;
- financial assistance (such as credit sales); and
- holding reserve stocks offshore.

Buyers may be willing to pay for additional services, but a single Australian seller is unlikely to have more advantage in this regard than many Australian sellers.

Some services may exhibit public good characteristics, such as promotion of an 'Australian' brand with certain quality and other characteristics. In this case, there may be an argument for ensuring all those who benefit also contribute to the cost of these programs, although interest in such 'generic' promotion appears less likely in a multiple seller system where sellers may be less able to individually capture the benefit from 'generic' advertising. However, there are a number of ways this could be arranged. For example, a voluntary producer association could authorise a 'brand' on a commercial basis to exporters, or the Government could organise an industry levy scheme. At the other end of the scale, there may be a problem with some exporters trying to pass low quality wheat off as high quality wheat. Again, there are a number of ways to combat this problem, such as compulsory licensing of exporters.

Empirical Evidence

Methodology

To obtain unambiguous evidence of a 'single desk price premium', it would be necessary to demonstrate that the 'single desk' seller obtained higher cif prices than competing suppliers for exactly the same quantity and quality of grain, and with exactly the same associated bundle of services and conditions of sale built into the price. Unfortunately such evidence was not available to the Committee. The best that could be substituted was to try to deduce whether a 'single desk price premium' is being obtained on the basis of fob prices.

Piggott and Edwards (2000) suggest there is no single analytical approach for carrying out the evaluation that is required for the review. MacAulay (2000) examined a number of methods for investigating the presence of price premiums associated with 'single desk' selling, and suggested that alternative approaches may need to be tried, and significant sensitivity analysis carried out.

Watson (1998) notes that the multi-dimensional nature of agricultural prices, reflecting absolute prices and margins for each transition, makes it easy to understand why empirical analyses of the benefits of the 'single desk' are so unrewarding. In Watson's view, trade data is not precise enough to distinguish premiums for 'market power' from other reasons for price variations.

Nevertheless, statistical studies have been undertaken. According to Piggott and Edwards (2000), the procedure outlined by Knetter (1989), following work by Krugman (1987) provides a reasonably robust direct statistical test. The approach (known as the ‘pricing to market’ test) was used by Carter (1993) to analyse the Canadian Wheat Board’s (CWB) ability to extract price premiums for barley.

The Committee regards the ‘pricing to market’ test as an appropriate methodology but notes the qualifications discussed in Piggott and Edwards regarding the requirements for appropriate data to conduct this test.

The economic principle behind the ‘pricing to market’ concept is that, in a non-competitive environment, a ‘monopoly’ with significant market power exporter can price discriminate by charging different prices in different markets at the same time (see earlier discussion of ‘market power’). According to Carter (1993), ‘to better understand the basic idea behind the pricing to market concept, consider Canadian Wheat Board (CWB) exports to Japan and assume the barley is priced by the CWB in \$Cdn. If the Japanese currency (that is, the Yen), appreciates vis-a-vis the Canadian dollar, then under perfect competition (the absence of pricing to market), Japan would pay lower prices (in its home currency) for imports. If the CWB continued to ask the same price in \$Cdn, then the price in Yen would adjust down by the full amount of the appreciation. In turn, the lower Yen prices would raise Japanese imports from Canada. However, under imperfect competition, if the CWB decides to raise its price quoted to Japan (in \$Cdn) as a result of the appreciation, then pricing to market has occurred.’ Carter states that with Knetter’s test, market power is revealed by measuring how export prices to different destinations adjust over time.

An alternative approach is to use the model of a profit maximising price discriminating monopolist used by the Centre for International Economics (CIE 1997) to examine the price premiums obtained by the Australian Barley Board to determine the premium specifically attributable to the use of the ‘single desk’ by AWBI. For a price-discriminating monopolist to maximise total returns, it must equalise the marginal return in every market. That is, the extra revenue earned from one more tonne sold to a particular market must be the same for all markets. This applies irrespective of whether or not the monopolist can control *total* supply. So long as the price elasticity of demand differs between *some* markets, the monopolist potentially is able to increase revenue by redistributing product among markets.

The equalisation of marginal returns implies a relationship between elasticities of demand and prices in different markets. Appendix B of the economic study (ACG 2000a) contains a detailed mathematical explanation. The returns that would have been obtained if marginal returns had been equalised in every case can then be compared with the average price that would have emerged under a competitive market to calculate the maximum premium that could have been achieved by the use of the ‘single desk’.

The ability to successfully price-discriminate will depend on the extent that the price elasticity of demand differs between markets; that there are impediments to arbitrage; and that the price elasticity of demand is known by the monopolist. ACG (2000a) point out that in reality it would be very unlikely that AWBI would know the exact

price elasticity in every market, so ACG modified their basic model in an attempt to simulate uncertainty (see Appendix B of ACG 2000a).

The Committee noted that the need to simulate the effect of imperfect knowledge on the part of a price discriminating monopolist is controversial, and considers estimates obtained assuming perfect knowledge to be more reliable than modified estimates obtained using a method to simulate uncertainty.

International Studies

The fact that the two main North American grain exporters, the US and Canada, have contrasting grain marketing systems has provided much scope for the study of whether 'single desk' marketers such as the CWB are able to exert market power and extract price premiums in export markets. As discussed in Johnson (1999), various authors have obtained a range of different results. Carter (1993) found demand for Canadian barley to be extremely elastic in major offshore markets, which if true would undermine the ability of the CWB to act as a price discriminating monopolist. On the other hand, Schmitz et al. (1997) found significant differences in fob prices paid for Canadian feed barley in Japan, the US, and the rest of the world, leading the authors to claim that the CWB is able to successfully price discriminate. In fact (in the opinion of the Committee) all this study demonstrated was that the CWB was able to price differently in different markets, not that it was able to obtain any advantage from doing so.

Examining the results obtained by Schmitz et al, Johnson (1999) pointed out that the apparent ability of the CWB to price discriminate was strongest for the period when the US Export Enhancement Program (EEP) was in effect. However, in the absence of targeted subsidies by competing exporters, the ability of the CWB to charge different prices in different markets may be much more limited. Johnson used an optimisation model to demonstrate that the Schmitz et al. results were sensitive to assumptions on price spreads and marketing costs. When there were no binding constraints on price spreads, and no extra marketing costs associated with CWB sales, single-desk selling was estimated to raise Canadian producer revenue by Cdn\$95.8 million relative to a multiple seller (competitive) solution. However, under assumptions least favourable to the CWB (inability to price discriminate and extra marketing costs), Canadian producers lost revenue.

During the overseas consultation process, the Committee heard evidence from Professor Wilson of North Dakota State University that US growers close to the border with Canada receive significantly higher prices for wheat of equivalent quality relative to Canadian growers in comparable regions on the other side of the border. In recent years, Professor Wilson has found that net prices paid to US growers have been higher by US\$0.50/bu to US\$0.75/bu (ie about US\$17.50 per tonne to US\$26.50 per tonne) than net prices paid to Canadian growers despite the fact that Canada has lower shipping and rail costs. As discussed below, part of this difference may be explained by the fact that handling costs are about US\$0.25/bu lower in the US than in Canada. However, there is a further difference of at least US\$0.25/bu that is very difficult to explain except to conclude that the 'single desk' CWB receives lower prices in world markets than free market US grain traders; and/or that marketing costs in Canada are dramatically higher than in the US.

Australian studies – Booz Allen and Hamilton

The Booz Allen Hamilton (1995) study was carried out for the Grains Council of Australia. The main conclusions of the study were that Australia needed to deliver a world class competitive industry, in order to improve farmer returns and maintain control of its own industry. The study suggested that this could only occur against a background of increased international competition, continued pressure on prices, growth in bulk markets, changing customer requirements, well positioned competitors and doubtful sustainability.

Australian studies – AWBI

Explaining how price premiums are generated for Australian wheat and returned to growers, the submission by AWBI to the review (AWBI 2000) states (p. 30):

‘The analysis of over 2000 AWBI sales contracts by Hirschberg over a three year period shows an average premium of US\$6.17 per tonne. Premium is defined as the difference between the AWB(I) fob price and the Pacific North West wheat price in the U.S. The premium in Australian dollar terms is the equivalent of approximately A\$8.72 per tonne or a premium value to Australian growers each year of approximately A\$141 million.

While several factors may explain how this premium was obtained, the ‘single desk’ is certainly one. This points to AWB(I), as the sole seller of Australian wheat in overseas markets, returning a far greater proportion of the total premium generated to growers, rather than being competed away or expatriated to (non-grower) shareholders or offshore by traders’.

A footnote to the AWBI submission explains ‘Prices of wheat at the Pacific North West (US) are used as the benchmark against which prices are measured because this is the most directly comparable source of competition for Australian wheat’.

The Committee does not accept that merely demonstrating that there is a difference between the average price obtained for Australian wheat and a particular type of US wheat necessarily means that additional revenue is being obtained, much less that even if it were, it is only able to be obtained from AWBI being ‘the sole seller’.

It can be confirmed by statistical analysis that movements in the quoted price of ASW wheat are highly correlated with movements in the reported prices of US hard winter ordinary wheats fob the Pacific North West, and the Gulf of Mexico. However, this does not mean that the wheats are exactly the same. The price a buyer will be prepared to pay will vary with his estimate of its value to a miller, which will in turn depend on the miller’s estimate of (among other things) the likely flour yield per tonne from the wheat when milled. If a trader believes millers may be able to obtain a higher yield of flour from a tonne of Australian wheat (with its general characteristics of being low moisture, white, and clean) than from a tonne of the nearest comparable American wheat (which may be higher moisture, red, and contain a higher proportion of unmillable material) then it would be reasonable for the trader to conclude the Australian wheat represents better value to the miller, and try to obtain a higher price.

As a trader, AWBI may be able to obtain a higher price. But it is not clear why any other competent trader of Australian wheat would not be able to obtain a similar price in similar circumstances.

Concerning AWB's statement that a 'premium' of A\$8.72 a tonne represents 'a premium value to Australian growers each year of approximately A\$141 million', ACG (2000a) note that the estimated annual total premium calculated over the three year period to which the contracts relate would actually be only A\$105 million. They also note that while there are clearly differences between the fob prices obtained by the AWBI and the PNW prices, the important question is to establish whether these differences are due to the export monopoly, or to other factors.

An econometric analysis undertaken by Gans and Hirschberg for AWBI (appendix 4 of the AWB submission), examined two of the more obvious possibilities, namely that the variation in the price difference could be explained by the distance advantage accruing to Australia and the precise grade of wheat being offered.

The Gans and Hirschberg analysis concluded that some 60 per cent of the percentage variation in the premium was attributable to these two factors, leaving some 40 per cent of the variation unexplained. Gans then stated 'This amount could in principle be attributed to the activities of the AWB and potentially the 'single desk' increments to bargaining power. However, it is also possible there could be other unexplained factors in the international wheat market that could account for such variation'.

The Committee notes that the statement that '60 per cent of the percentage variation in the premium was attributable to these two factors' is not equivalent to a claim that 60 per cent of a measured difference in fob prices is a credible estimate of the magnitude of a price premium solely attributable to the 'single desk'. There is no reason why any part of a geographically based price differential should be a measure of a price premium earned by a 'single desk' even if there were absolutely no differences in the quality of the wheat or the supporting services associated with its sale.

Nevertheless, the Committee does not disagree with Gans that some part of the price difference *may* be attributable to the 'single desk'. The question to be answered empirically is 'how much', if any.

Australian studies – ACG Results

ACG, as part of its report for the Committee into the economic impact of the WMA, undertook its own analyses of the pricing data made available by AWBI. Given AWB's claims that it uses the 'single desk' to price discriminate, ACG used a model of a profit maximising price discriminating monopolist to derive an estimate of the premium attributable to the 'single desk'. ACG (2000a) states that, 'for a price-discriminating AWB to maximise total returns from the sale of a given wheat crop it must equalise the marginal return in every market. That is, the extra revenue earned from one more tonne sold to a particular market must be the same for all markets. If this is not the case, then it would be possible for a third party to reallocate sales between markets and increase total returns. The equalisation of marginal returns also implies a relationship between elasticities of demand and prices in different markets.

This relationship is relied upon with the average quantities and prices in different markets over the past three years to compare the average price achieved by the AWB with the average price that would emerge under a competitive market’.

ACG analysed the data first making the assumption that AWBI had perfect information, then using a procedure which simulated a situation of imperfect information. Within each test, ACG also considered two alternative scenarios, these being that wheat is a highly differentiated product, and that wheat is somewhat differentiated. In the first instance, ACG considered wheat as a differentiated product and hence considered the AWBI would seek to maximise profits across eight different wheat types. However, given the possibility that some of these eight types could be considered substitutable, ACG also simulated the situation of greater substitutability by aggregating the eight types into four classes, drawing upon information supplied by AWB Limited as to different Australian wheat types and their nearest US equivalents.

ACG concluded that the maximum premium that AWBI could have achieved over 1997 to 1999 inclusive, acting as a perfectly informed profit maximising price-discriminating monopolist, is in the order of US\$21.5 million if wheat is considered to be a differentiated product, and US\$39.5 million if it is assumed that wheat is less differentiated. Using their method of simulating uncertainty, ACG obtained estimates of US\$12.3 million if wheat is considered to be a differentiated product, and US\$13.1 million if it is assumed that wheat is less differentiated.

Based on the ACG results the Committee’s initial view was that only a relatively small proportion of the A\$8.72 a tonne price difference between Australian contract prices and US Pacific North West wheat prices in the period 1997 to 1999 could convincingly be attributed to the ‘single desk’. In the early part of its submission (p.30), AWBI does not explicitly claim the full amount either. The submission merely states that ‘while several factors may explain how this premium was obtained, the ‘single desk’ is certainly one’ and points to the conclusions by AWBI’s economic consultants that ‘there is evidence that Australian wheat commands real premiums beyond which that would be explained by distance advantage and particular mix of grades’ and that ‘such premiums might be eroded somewhat if ‘single desk’ restrictions were removed’. However, the full amount is claimed elsewhere in the submission (for example, on p.53, on which it is stated, ‘The premium obtained through the ‘single desk’ [is] estimated at up to A\$7.10 per tonne in BAH’s 1995 report and more recently at approximately A\$8.72 per tonnes in Gans’ economic analysis on ‘single desk’ selling’).

In the Committee’s view, the question of the size of the ‘single desk price premium’ is pivotal, since much of the argument for the single seller system providing a benefit appears to depend on the idea that the system provides significant additional export returns to growers over and above what would be provided by a multiple seller system. Therefore, the Committee requested further technical analysis specifically of the ‘single desk price premium’ to analyse the source of any ‘single desk price premium’ in detail.

The further technical analysis concentrated on three questions:

- What is the sensitivity of the model used in the ACG analysis to changes in the assumption about the functional form of the demand curves?
- Do pricing to market models yield significantly different estimates of the ‘single desk price premium’ than the profit maximising price discriminating monopolist model used by the ACG?
- Which countries are the primary sources of the ‘single desk price premium’ (if any)?

The main conclusions from the further technical analysis are as follows:

- If linear demand curves are used rather than the constant elasticity demand curves assumed in the ACG analysis, the estimate of the premium generated by the simulation model, for the data used in the analysis, can be increased by a factor of 2-3 times. *A priori* there is no reason to assume that any specific functional form is correct.
- There appear to be statistically significant country specific effects for most classes of wheat traded which suggest some ability to price to market. For the contracts considered (that is, those for countries for which the ability to price to market was found to be statistically significant), the average value of the premiums was calculated to be US\$10.7 million a year. The average premium per tonne across all classes and years was US\$1.02 per tonne.
- There appeared to be a very high degree of concentration of positive premiums being earned within a small number of countries, with most of the positive premium coming from sales to Japan.

Whether the price premium in the Japan market is due to the wheat single seller’s ‘market power’, or whether it is because of the specific nature of the import arrangements in Japan is a moot point. If it is the latter, the structure of the equilibrium model may be inappropriate, and the price differentials for Japan may not represent information about relative price elasticities of demand. As noted in chapter 4, Japan’s system of import quotas ceased in 1995. However, the exporter shares of wheat imports into Japan continue to show a remarkable stability. For example, exporter wheat market shares in the period 1992 to 1998 were: United States, 52-57 per cent of imports; Canada, 23.5-27 per cent of imports; and Australia, 17.6-21.8 per cent of imports. For no other major importing country are import shares so stable. The *de facto* evidence suggests that there is little competition for market share in Japan.

It could be inferred from these facts that any observed price differentials between Japan and other markets can be attributed mainly to the Japanese strong preference for security and stability of supply, and would still exist if there were multiple exporters of Australian wheat as there is of US wheat. However, there is a further issue of the capacity of the exporting country to capture most or all of the benefits from such price differentials. While in Japan, the Committee was presented with convincing but confidential evidence that the ‘single desk’ may well enable much of the price differential to be captured by Australia, and that this “premium” would be dissipated

if there were multiple exporters of Australian wheat. Furthermore, it is noteworthy that apart from Japan, the results suggest that the degree to which the wheat single seller can obtain premiums in other markets is very limited.

In summary, the results of the further analysis confirmed the Committee's initial view that, on average, the 'single desk price premium' which Australian single seller of bulk wheat was able to obtain from export markets in the period 1997 to 1999 markets was relatively small (of the order of US\$1 per tonne).

Summary of Estimated Premium Values

SOURCE	PREMIUM	NOTE
AWB (INTERNATIONAL) LIMITED	Approx A\$145 million per year; average A\$8.72 per tonne (US\$6.17 per tonne)	<ul style="list-style-type: none"> Figure claimed to be derived from Gans and Hirschberg's analysis of over 2 000 AWBI sales contracts. Uses a multiple regression model which allows the identification of what proportion of the variation in price premiums is due to location of the market, the grade of wheat sold to market and the ability of the AWB to extract a profit due to the institution of the 'single desk'. AWB argues that the 'single desk' is a significant factor in explaining how this premium was obtained.
ALLEN CONSULTING GROUP	Range from US\$12.3 million per year to US\$40 million per year (=US\$0.79 per tonne to US\$2.56 per tonne)	<ul style="list-style-type: none"> Maximum obtainable premium from price discrimination alone (ie the 'single desk'). Uses the price discriminating monopolist model.
BURTON*	Average estimated premiums range up to US\$2.14 per tonne	<ul style="list-style-type: none"> Figure derived by "re-solving the simulation model" using only estimates of price differentials. Average value of premiums for the contracts considered is US\$10 million per year. Average premium across all classes and years is US\$1.02 per tonne. However, there is a high degree of concentration of positive premiums being earned within a small number of countries.
BOOZ ALLEN HAMILTON	Range of A\$1.75-\$7.10 per tonne, average of A\$2.68 per tonne; US\$10-80 million per year	<ul style="list-style-type: none"> Using separate "bottom up" and "top down" approaches; average A\$2.68. "Bottom Up" approach based on 3 arguments: 'single desk' enabled premiums to be achieved by better marketing (price premium); 'single desk' enabled better allocation of wheat into higher paying markets (market mix); and 'single desk' enabled complete capture of ocean freight advantages (pricing discipline). The bottom up approach produced a value of US\$0.12-US\$7.96 per tonne. The "top down" approach involved a comparison between Australian fob prices and fob prices that would have been achieved without a 'single desk'. BAH concluded that the value of the 'single desk' under this approach was to US\$13.30 per tonne.

* Professor Michael Burton, from the University of Western Australia, was engaged to review various economic studies and to estimate price premiums by analysing the AWBI data set, using pricing to market methodology.

Other Premium/Costings-Related Comments

STAKEHOLDER	COMMENT
ALLEN CONSULTING GROUP	The impact of the pool on domestic wheat prices is A\$1.38 per tonne.
AWB (INTERNATIONAL) LIMITED	The 'single desk' provides increased ability to coordinate wheat movements, with benefits estimated at between US\$0.88 - US\$1.45 per tonne ("transparency benefit").
LINDNER AND MCLEOD	In Western Australia, moving to a system of grain handling where charges reflected resource costs and were disaggregated and transparent could save West Australian wheat growers of A\$12.5 - \$23 million annually.
JOINT INDUSTRY SUBMISSION GROUP	The Milling Wheat Project report used flawed arguments and methods of analysis to estimate net benefits to be between minus A\$3.35 per tonne and plus A\$8.72 per tonne. Disallowing the estimated benefits from 'market mix' and allowing for second round effects in the estimation of benefits from freight premiums would tip the scales decisively in favour of a competitive marketing system.
JOINT INDUSTRY SUBMISSION GROUP	Supply chain costs are A\$45-\$55 per tonne.
GANS	Most variation in the percentage regional price differentials is explained by the distance advantage accruing to Australia and the precise grade of wheat offered. However, 40 per cent of the variation was unexplained by these factors. This amount could be attributed to the activities of the AWB and potentially to 'single desk' bargaining power. However, there could be other unexplained factors in the international wheat market that could account for some or all of the observed variation.
JOINT INDUSTRY SUBMISSION GROUP	More competition would provide cost savings and higher net returns to growers of up to A\$5 per tonne.
-	The Committee's "further technical analysis" suggested that the average premium per tonne across all classes and years was US\$1.02 per tonne.
-	Various submissions estimated the savings from moving to a more efficient handling system as being from \$5 - \$15 per tonne, depending on location (although there could be additional logistical costs implementing this).

7.2.2. Domestic grain prices - do the current arrangements raise prices?

Theory/discussion

Influence of export returns on domestic grain prices

Domestic marketing arrangements for Australian wheat were deregulated in 1989. However, it has been argued that the current arrangements for export wheat may still influence the domestic market.

When selling their wheat, Australian wheat producers are unlikely to accept a lower net return at farm gate from domestic sales than they can receive from delivering the same wheat to the export pool. If the single exporter is obtaining additional revenue from export markets, average unit export value will exceed the world export parity price. If a country is a net wheat exporter, then in a competitive market (that is, buyers are able, among other things, to import wheat), it would be expected that domestic consumers would pay no more than the world export parity price.

Of course, if the single exporter has not succeeded in obtaining additional revenue from the export market, then average unit export value may be little different from the world export parity price, and the scope for domestic prices to be above world parity would be correspondingly low.

If, for whatever reason, the activity of the single exporter were to raise domestic grain prices, the upper limit to the producer price for domestic sales should be the world import parity price (assuming wheat imports are permitted). This can be expected to be higher than the world export parity price due to the combined effect of tariffs, quarantine restrictions, and inward transport costs (Productivity Commission 2000).

Influence of large sellers on domestic prices

There are other ways in which the single export seller may be able to raise domestic prices than simply through bidding supplies away from domestic consumers by offering growers a price that is higher than the expected pool price.

For example, because they are prevented from spreading risk and costs across both export and domestic market sales, domestic traders may be unwilling to enter the market, or willing to do so only when they can obtain higher grain prices. To the extent that favourable arrangements with input suppliers negotiated by AWB Limited's export subsidiary (AWBI) may also be available to its domestic marketing subsidiary, AWB (Australia), this may allow the domestic marketing subsidiary to increase its market share on the domestic market and reduce the competitive pressure to offer lower prices in this market. Access to the export pool's stocks of wheat may further advantage AWB Limited's domestic marketer.

If the perceived advantages enjoyed by the AWB Group on the domestic market result from economies of scale then these advantages would accrue to any large seller even if the current legislation were removed.

Influence of the harvest price

Domestic grain prices may fall below the world export parity price, particularly around harvest, because the expected pool price with which producers compare cash price offers from domestic traders is the harvest price rather than the estimated pool price. (The harvest price is a 'first advance' whereas the estimated pool price includes the expected value of subsequent pool payments).

It may be reasonable to expect that when considering traders' price offers, producers would want to discount the value of subsequent pool payments to a net present value, or to compare the cash prices offered by traders with AWB Limited's own cash price offer (which in theory should equal the harvest payment plus the discounted net present value of estimated subsequent pool payments). It is difficult to believe many producers would simply ignore the expected value of subsequent pool payments and be willing to sell for cash at the harvest price, unless faced with a severe cash flow problem.

Stability of prices and access to stocks

Domestic consumers may obtain benefits from the operation of the export pool in that they are not exposed to the day to day price fluctuations of the world market, and have available to them the pool's stocks of wheat without incurring any stock holding costs themselves.

It is not clear whether this introduces any systematic bias upward or downward in domestic grain prices. If domestic consumers did pay higher prices it is possible a component of this may reflect the additional costs incurred by AWB Limited in providing additional services (including stock holding) or in providing wheat of a particular type or quality.

The argument has many similarities with the argument over whether the current arrangements result in any additional revenue from export marketing. In both cases it is possible the customer pays higher prices but does so because the product includes some component of 'bundled' services.

Countervailing natural monopolies

Another argument for active intervention by the single seller in the grain supply chain relates to the postulated market power of downstream domestic users (Productivity Commission (2000), p. 28-29). It has been argued that because there are greater numbers of producers compared with end users, domestic users may have excessive market power. However, the fact is that there are many domestic users, and there is little credible evidence that single domestic users have any significant degree of market power and/or ability to influence prices on the domestic market. Furthermore there are other possible forms of producer association for producers who do not wish to negotiate directly with processors, for example, voluntary cooperatives. For wheat, the fact that the bulk of wheat is exported and that the domestic price is determined in international markets means that there is negligible if any scope for domestic processors to exercise buying power.

Evidence/studies

ACG (2000) noted that a number of wheat consumers have undertaken studies that demonstrate they are vulnerable to higher domestic wheat prices. For example, benchmarking of the Australian and US chicken meat industries suggested that despite a high level of technical efficiency compared to the US industry, Australian producers have a cost disability of 27 per cent of total production costs. Nearly 40 per cent of the difference in production costs is attributed to higher feed costs (Joint Industry Submission Group 2000). For pigs, the CSIRO's model of production costs suggests that a 40 per cent increase in domestic wheat prices would have a proportionately greater impact on profitability, reducing it by one half. While quantifying the likely impact of higher grain prices, however, these studies do not in themselves demonstrate that domestic wheat prices are higher due to the existence of the 'single desk'.

To investigate whether the export pool return had any apparent influence on domestic wheat prices, ACG (2000) examined domestic wheat prices and compared them with

the pool return, but were unable to observe any seasonal pattern. ACG suggested that the influence of the pool on domestic wheat prices may not be general (and easily observable), but more likely, is limited to specific occurrences. For example, in times of production shortfall, domestic users need to compete with international markets. Since the statutory obligation to meet domestic users' needs no longer applies, the pool may be virtually the only source of supply.

ACG (2000) suggest that if only small premiums are being achieved on average for export sales, it follows that the likely impact of the pool on domestic wheat prices is also small. They conclude that AWBI's 'single desk' export monopoly is likely to raise domestic wheat prices above those which would arise in the absence of the 'single desk', but were unable to determine the precise degree of this impost on the consumer.

The Committee concluded that the main impact of the "single desk" on domestic consumers depends on the impact it has on net returns to growers. If the desk raises net returns, domestic prices would rise by an equivalent amount, and vice versa. While domestic wheat consumers might be disadvantaged by the presence of a single dominant wheat marketer, if this market dominance resulted from superior levels of service offered by the marketer then removal of the legislation should have little effect on the marketer's dominant position.

7.2.3. Market development – do the current arrangements help or hinder?

Many stakeholders expressed concern about the impact of the 'single desk' on market development, and provided evidence that the following factors will play a major role in defining wheat markets in the future:

- globalisation pressures, forcing marketers to increase efficiency and lower costs in order to remain competitive;
- technology, including the impact of e-commerce and biotechnology on supply chains;
- trade liberalisation, including accessions to the WTO and the rise of private buyers; and
- increasing customer focus and the rise of market specific supply and sale of wheat as a branded food ingredient.

Over the decade prior to the next NCP review, the role of competing value chains is likely to increase relative to the traditional spot-trade commodity market. Preservation of the current wheat export marketing system or any suggested improvements must therefore provide a framework to successfully address these issues in order to preserve the net public benefit of Australia's marketing arrangements through the uncertainty of the next ten years.

Bulk Marketing

Many submissions claimed that "orderly marketing" through the 'single desk' enables coordinated development of bulk markets. It is claimed that the Korean market is an excellent example, with the marketing activities of the former Australian Wheat Board increasing Australian market share (see chapter 4). However, while in Korea,

the Committee heard that AWBI provided Korean customers with outstanding, and presumably costly, marketing and support services.

It also is claimed that the ‘single desk’ system recognises that a number of customers express a clear preference for dealing with a farmer-owned centralised marketing body. However, the Committee found many cases where these same customers also willingly purchased wheat from competitors that were not farmer-owned. Notwithstanding strong support for AWBI marketing activities from overseas customers, as well as recognition by a number of competitors that the ‘single desk’ system provides strong competition in bulk export markets, it needs to be recognised that customer loyalty and market share can be the result of subsidised over-servicing of export markets. Since there is no facility for third party review of export market development, it is difficult to assess these claims objectively.

In some cases, marketers other than AWBI have created demand for Australian wheat, but have either been denied bulk export permission or have not been able to purchase wheat from AWBI pools, even at higher than bid prices. Controlling the bulk export market may force other marketers into the container trade, which may create inefficiencies in the supply chain.

While AWBI, and before it the Australian Wheat Board, have been very successful at bulk exporting bread wheat, they do not seem to have shown the same success in specialty wheats such as noodle or durum wheat, nor in niche markets.

Niche Marketing

AWBI claims that it assists other exporters whose activities complement those of AWBI in niche market development. However, the Committee found ample evidence that the current system is not conducive to maximising grower returns from niche marketing.

Niche marketing, including identity preservation, increases costs as small elevations, segregated storage and small shipments lose the benefit of economies of scale. Therefore it is important that these costs be minimised, and the price obtained in the niche market outweigh any added expense.

For example, the Committee is aware that the conversion of 60 000 tonnes of horizontal storage from single segregation to double segregation could result in the loss of 6 000 tonnes of ‘loss per division’ capacity, which at \$75 per tonne is a total one-off capital cost of \$450 000 borne by the bulk handler and passed onto the supply chain.

The shift from wheat sold as a bulk undifferentiated commodity to wheat as a branded food ingredient has been embraced by AWBI’s marketing strategy, and is one of the success stories of the ‘single desk’. This is recognition of the gradual development of the culture of “market-specific supply”, where ever more detailed consumer demand leads to small shipments of wheat prepared to tight specifications. This is ideal territory for container exporters to identify and develop niche markets in areas where bulk exports cannot obtain competitive advantage.

The global wheat industry is changing at an accelerated rate, in ways that were not envisaged when the current arrangements were put in place. In an environment of constant change and adaptation, small exporters servicing niche markets form the vanguard for the entire wheat industry, as lessons learnt on a small scale can then be applied more broadly to the bulk export trade and enable it to learn and adapt at a rate more appropriate to the risks involved.

The introduction of biotechnology is one such challenge, where logistic requirements such as identity preservation and segregation will allow niche marketers to introduce varieties and test market demand on a small scale prior to the industry making the infrastructure investment decision necessary for bulk exports of GM wheat.

However, the uncertainty in the current system acts as a disincentive for niche marketers to invest in developing markets where there is no certainty that they will continue to have export permits issued to them. Stakeholders identified the issue of “cherry-picking”; that is, the legislated appropriation without compensation by AWBI of niche markets that develop beyond a certain size, and the disincentive this imposes on niche market development.

Container and Bag Exports

The higher freight costs of the container and bag export trade provides a significant degree of protection to the bulk export market. Although freight rates vary over time, as well as in response to particular circumstances, most of the submissions to the Committee estimated the freight cost differential to be about \$25 per tonne on average. Nevertheless, trading wheat in containers and bags is more appropriate for markets with a limited capacity to unload, store and transport bulk shipments. It can be easier to arrange finance for smaller shipments, and there is enough flexibility in the trade to identify and develop new niche markets. Exporters can achieve higher sale prices because it can enable end-users to extract a margin by not dealing with bulk importers. In addition, the container and bag trade may be more appropriate to meeting new challenges and developments in the industry such as biotechnology and identity preservation.

Currently, the guidelines governing the container and bag export market, the tonnages and markets involved, are not dissimilar from the situation prior to the privatisation of AWB Limited and establishment of the WEA.

Although some stakeholders described AWBI as “lazy marketers”, it is fairer to say that the ‘single desk’ encourages AWBI to focus on bulk exports to the detriment of niche markets. The extent to which container sales undercut AWBI sales while still offering a market competitive price to growers in order to source supply of grain would reflect identification of new marketing opportunities and/or efficiencies in logistics, administration or marketing costs relative to AWBI.

Following deregulation of the domestic wheat market, the export of wheat in shipping containers increased. The removal of all restrictions on the export of containerised wheat could bring economies of scale to containerised wheat and provide a basis for the lowering of costs and the expansion of containerised exports of wheat, lupins, barley and canola.

Relationship Management and Downstream Investment

In order to develop long-term markets and bring customers into the Australian wheat marketing value chain, a 'single desk' can invest funds into relationship management, after-sales service and downstream investment.

Overseas stakeholders, both customers and competitors, identified this as a major advantage of the 'single desk' system. Customers in particular were impressed by the efforts of the former Australian Wheat Board in working with them to develop wheat varieties to meet customer requirements. Knowledge of particular customer requirements is retained, and information is provided to customers on the national crop that assists those customers in planning purchases with AWBI.

Customers in Korea and Japan were quick to note that the former Australian Wheat Board consistently demonstrated a greater understanding of Asian business culture than its competitors and made genuine efforts to understand target markets. While those customers realised that it was natural for this effort and investment to diminish as their markets matured, it is reasonable to assume that AWBI will continue to develop new markets with the same skill and customer orientation as the former Australian Wheat Board.

AWB Limited also has investments in downstream processing overseas, which can assist in tailoring Australian wheat varieties to customer requirements and ensuring continued demand for Australian wheat.

However, relationship management costs money. For example, in the US it is conducted by the taxpayer-funded US Wheat Associates (USWA) because it is not marginally profitable. In Australia, growers are forced to pay the market development costs of relationship management in lower pool returns, and do not have the choice between 'relationship sales' and 'spot-market commodity sales' into each market.

In addition, there is anecdotal evidence that the end-user information requirements of AWBI have resulted in some buyers refusing to deal with AWBI and instead buying from the deregulated US market. The Committee makes no judgment as to the reasons that this may occur, or the cost it may impose on the Australian wheat industry. However, it is worth exploring in the context of assessing the overall costs and benefits of relationship management.

Contract Management

Stakeholders claimed that the marketing discipline of the 'single desk' allows AWBI to enforce compliance with signed contracts, backed by the credible threat of non-supply of Australian wheat. In turn, this provides farmers with greater certainty of payment when they deliver to the pools, lessening the impact of customer default on the pool return.

It should be noted that enforcing the threat of non-supply merely reduces Australian market share. Non-performance is properly a contract risk that should be reflected in the price.

The threat of non-supply could provide an incentive that would encourage leakage of wheat into non-target markets, undermining AWBI's marketing strategy. This problem currently exists in both bulk and non-bulk markets as a result of using agents and selling to third-parties rather than end-users.

Security of Supply

Control of the national crop through the 'single desk' allows AWBI to coordinate the marketing chain to deliver the wheat varieties in international demand. This means that AWBI can accumulate enough wheat across varieties and grades nationally to meet customer demand.

This control allows AWBI to provide security of supply to key customers, enhancing Australia's reputation as a stable supplier despite the regional production risk caused by our extreme climate variability. Indeed, some customers indicated that they were prepared to pay a higher price to ensure this security.

In return this security of supply requires substantial strategic carry-over of stocks, which imposes a storage cost of around A\$2 per tonne per month. It also imposes an opportunity cost as the wheat could potentially be sold to other customers for an equivalent or higher return. Therefore any claimed price premium resulting from security of supply should be discounted by the cost of providing carry-over stocks.

7.2.4. Grain supply chain logistics and costs - do the current arrangements realise savings for growers across a range of grain marketing services?

Theory/discussion

Economics of scale and scope in marketing, storage, handling and transport

It is claimed by AWBI and others that a 'single desk' exporter can provide services and/or buy inputs at a lower cost than would be possible if there were a number of exporters. The basis for such claims include negotiating power, economies of scale and scope in grain marketing, financing, risk management, and coordination of the logistics of storage, handling and transport.

For example, the submission to the Committee by AWBI (2000) argued that, 'The national scale of operations of AWB(I) provides considerable operational efficiencies, which are passed on to growers. Through the economies of scale and scope provided by the Single Desk, AWB(I) has been able to negotiate with principal service providers such as state based Bulk Handling Companies to lower costs and charges. There has been, in per tonne terms, significant reductions over a 20 year period' (p.52).

However, it also has been argued that in the absence of competitive pressure, the 'single desk' exporter may be a less efficient provider, or buyer, of services than providers in a competitive market. Potential economies achievable through internationalisation of investment decisions also may not be realised under current arrangements. Furthermore, some of the economies of scale generated by compulsory marketing of a generic commodity may not be cost-effective if they are achieved by under-providing services.

For example, the submission to the Committee by Australian Bulk Alliance (ABA 2000) argued that ‘bulk handling and transport charges in Australia are higher than they need to be and this is partially because of the way the AWB operates within the Australian supply chain’ (p.5). The submission further states, ‘the logistics costs incurred in the Australian grains industry between farm gate and loading on-board an export vessel amount to approximately \$1.4 billion per annum, equivalent to 35 million tonnes at A\$40 per tonne. The AWB has a responsibility, on behalf of growers, of paying over half of this cost each year. Yet the AWB has not been able to achieve any significant inroads into achieving efficiency savings to reduce these costs, despite the efficiency gains achieved in the last ten years in many other Australian bulk commodities’, and concludes, ‘The AWB intervention in this process is preventing efficiency gains and actually increasing costs’ (p.2).

If a ‘single desk’ exporter was the most efficient provider, or buyer, of services, it could be expected that the organisation would out-perform all competitors and continue as the dominant provider or buyer in a multiple seller environment.

Innovation and productivity growth over time

It has also been suggested that since AWB Limited organises the entire supply chain and directs bulk handlers and rail companies on all facets of grain storage, handling and transport, this may discourage competition, innovation and change in grain handling systems (JISG 2000). For example, there may be little incentive for bulk handling companies to make investments in fast train loading or rail sidings that would reduce train cycle times and hence freight rates. There may also be little incentive for rail companies to undertake reforms that reduce the operational costs of bulk handlers. Confidential submissions to the Committee from several organisations provided specific examples where the failure of AWB Limited to address this issue had resulted in foregone potential cost savings.

Evidence/studies

International studies

Supply chain management has escalated in prominence in recent years in both the US and Canada. In particular, with industry and market maturity, efforts are being made to reduce costs through managing the vertical market system. This has become an important problem in the US grain industry as it becomes more vertically integrated. It is also a challenge in Canada where firms are already vertically integrated, but have relatively little control over their own logistical functions (Wilson, Dahl and Carlson 1998).

Wilson, Dahl and Carlson point out that there are a number of different ways to manage uncertainty through the supply chain. These include stockholding throughout the system, and/or contingent contractual relationships to induce forward planning and supplier performance. Logistical risks are inevitable and the challenge is to manage them. Trade-offs also exist in formulating marketing (sales) and logistical strategies. In general, conservative sales strategies relative to expected system performance may result in lost sales opportunities, but would minimise demurrage and other costs associated with system under-performance. In contrast, aggressive sales strategies

relative to capacity would result in an escalation in logistical risks. These are not unique to the CWB or the Canadian marketing system, but are a challenge to all grain exporters.

The issue of systemic costs associated with single-desk selling has also been examined extensively in overseas, particularly Canadian, studies. For example, Carter and Loyns (1996) and Carter, Loyns and Berwald (1998) have identified numerous extra costs in the Canadian grain handling, transportation and marketing system, and argue that they are directly or indirectly linked to the activities of the CWB. In these studies it is estimated that higher marketing costs (potentially as high as Cdn\$16 per tonne for barley) would offset any advantages of single-desk selling of Canadian grain, and lower the net return to Canadian producers.

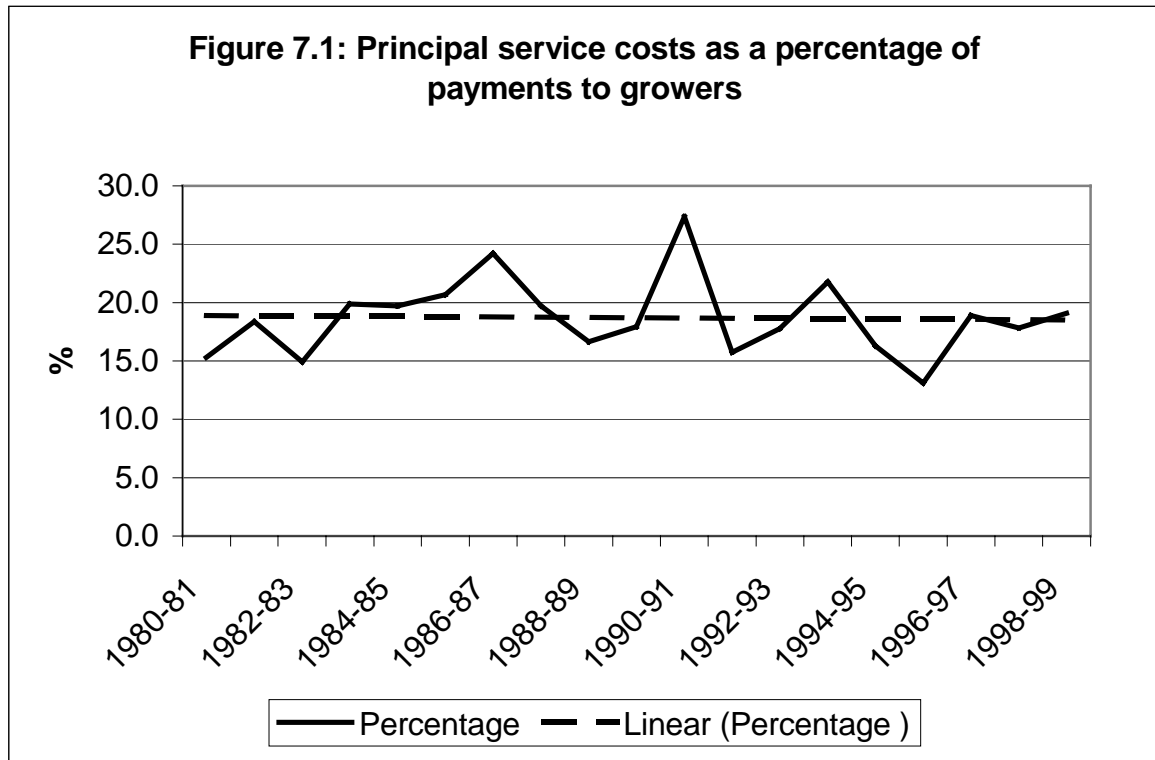
Further evidence that the Committee found particularly compelling was provided by Professor Wilson of North Dakota State University, and involved studies that compared grain handling costs in otherwise comparable wheat growing regions that were on either side of the Canada/US border. Because the regions were virtually identical with respect to geography, climate, and almost all other determinants of grain handling costs, it is difficult to avoid the conclusion that measured differences of about US\$0.237/bu (ie US\$8.70 per tonne) were due to the difference between the 'single desk' system of marketing in Canada and the freely competitive system in the US. For instance, in 1998 grain handling costs were US\$0.421/bu in Canada but only US\$0.184/bu in the US. Measured costs were the sum of country elevation, terminal elevation, and cleaning costs. If cleaning costs were excluded, the results were US\$0.354/bu in Canada but only US\$0.139/bu in the US. On the other hand, while Eastbound rail freight rates are similar in both countries, Westbound rail freight rates in the US are higher than in Canada (by about US\$20 per tonne). Many other costs that are "hidden" in the Canadian system (eg demurrage, identity preservation required to provide large numbers of segregations, etc.) were estimated to be much higher than in the US.

Australian studies – AWBI

In its submission to the review, AWBI states that the 'single desk' provides it with an increased ability to coordinate wheat movements and hence allows savings to be made and delivered back to producers. The benefit is estimated to be between US\$0.88 and US\$1.45 per tonne, based on a US study using a theoretical bidding model which calculated information advantage to be worth US\$1 to US\$2 per tonne. This model made unrealistic assumptions about the nature of the bidding process and also was constructed to analyse a different market to that being discussed in the AWBI submission. Therefore, the Committee rejects the relevance of the particular US theoretical bidding model cited in the AWBI submission to real world markets, as well as the application of this type of analysis to estimation of cost savings in logistics and grain handling in Australia.

The Committee believes that savings from coordination of logistics are more likely to be achieved in a competitive environment that would exist in the absence of the 'single desk' arrangement. It is vital that upstream competition exist within the wheat industry, in areas beyond the 'single desk' arrangements - for example, rail to port delivery and delivery contracts. There is anecdotal evidence to suggest that the 'single

desk' has an anti-competitive effect on the supply chain, and that if AWBI were able to receive wheat fob, this would result in cost savings. Many of AWBI's decisions in the areas of grain receipt, storage, transport and handling have a wheat-specific focus, which lacks the "whole grain network" perspective of bulk handlers.



The AWBI submission also presented a graph (p.52) to illustrate that 'significant reductions' in principal service costs had been achieved over a 20 year period. The Committee noted an apparent inconsistency in the way in which grower costs and grower returns were treated in the submission. The graph of principal service costs was in constant dollars (that is, the nominal costs were adjusted for inflation), while later graphs showing payments to growers by AWB Limited were in nominal terms (that is, not adjusted for inflation). Thus, while it may appear that costs had been reduced significantly over time while grower payments had been maintained, in fact it can be seen from Figure 7.1 (drawn from the data in Table 7.1) that there has been virtually no downtrend in the principal service costs as a percentage of payments to growers over the past twenty years.

Table 7.1: **Principal service costs and payments to growers a**

	Payments to growers b	Average BHA	Average rail freight	Principal service costs	Percentage
	\$/t	\$/t	\$/t	\$/t	%
1980-81	147.42	10.92	11.62	22.54	15.3
1981-82	149.92	12.73	14.80	27.53	18.4
1982-83	178.23	12.77	13.83	26.60	14.9
1983-84	162.38	14.73	17.56	32.29	19.9
1984-85	165.70	15.29	17.36	32.65	19.7
1985-86	159.32	15.08	17.88	32.96	20.7
1986-87	139.83	16.90	16.97	33.87	24.2
1987-88	164.32	16.20	16.20	32.40	19.7
1988-89	205.96	17.03	17.28	34.31	16.7
1989-90	179.28	16.36	15.77	32.13	17.9
1990-91	127.00	17.64	17.11	34.75	27.4
1991-92	180.00	14.97	13.35	28.32	15.7
1992-93	192.55	18.20	16.02	34.22	17.8
1993-94	162.3	18.15	17.19	35.34	21.8
1994-95	200.00	15.85	16.73	32.58	16.3
1995-96	249.00	18.44	14.19	32.63	13.1
1996-97	198.45	20.43	17.06	37.49	18.9
1997-98	192.15	19.57	14.67	34.24	17.8
1998-99	183.00	20.37	14.57	34.94	19.1

a Nominal A\$ per tonne. **b** For ASW.

Source: Calculated from ABARE 1999, *Australian Commodity Statistics*.

Australian studies - various

In its discussion of grain service costs, the ACG examined claims that economies of scale and scope provide the single seller with the ability to use its domestic market power to negotiate lower charges with principal service providers, notably the state based bulk handling companies. ACG noted that these claims that AWB Limited have been responsible for cost savings in the supply chain were disputed by a number of bulk handlers. For example, in their submission to the review, Grainco Australia estimated that a storage and handling saving of up to 20 per cent could be achieved if AWB Limited were to change the way it manages its logistics and make the storage, handling and transport part of the supply chain more contestable.

A submission to the Committee by the Joint Industries Submission Group (JISG) noted that in the US, where monopolies or public utilities have been opened up to competition, prices to consumers have fallen. Additionally, in Australia, where competition has been introduced into markets previously controlled by monopolies, there have been substantial reductions in costs (JISG 2000).

The submission stated that, following the Royal Commission (into Grain Handling, Storage and Transport in 1988) one would have expected significant innovations, increased competition and lower charges in grain handling. This has not occurred to the extent predicted. On closer inspection, essentially the same organisations exist today as before the Royal Commission. While most have changed from statutory organisations to grower owned private companies or cooperatives, they are still basically state based with effective regional monopolies on grain handling services for export grain (p.35).

Some of the problems with the current grain handling system as seen in the JISG submission are summarised in Table 7.2.

Table 7.2: **Typical existing grain export supply chain**

<u>Farms</u>	<u>Farm to depot</u>	<u>Local depot</u>	<u>Rail to port export terminal</u>	<u>Port export terminal</u>
	<ul style="list-style-type: none"> Expensive harvest period road transport 	<ul style="list-style-type: none"> Low product turnover Over capacity Aging infrastructure Poor intake rates Poor outturn rates Inefficient rail access 	<ul style="list-style-type: none"> Low traffic density Poor cycle times Excessive rolling stock Poor industrial relations and work practices Lack of appropriate investment 	<ul style="list-style-type: none"> Excess capacity due to poor management of shipping program Lack of investment in new technology Poor industrial relations

Source: JISG 2000.

The JISG submission also stated that supply chain costs (including local cartage, receival charges, storage charges, freight charges, and ‘fobbing’) represent up to a third of gross pool returns to growers. Based on interviews with grain handling companies, the JISG submission suggested savings could be achieved by:

- more accurately forecasting shipping programs and supply movements;
- making better use of on farm storage over the season by having price incentives for storage;
- rationalising the number of local silos;
- improving the coordination between rail and bulk handling services;
- increasing investment in state of the art facilities; and
- in the long run, rationalising the entire structure of the supply chain.

The principal technical elements of a ‘new’ grain export supply chain have been identified for many years and may be summarised as:

- greater use of good quality (eg welded steel bin) storage on-farm to allow the grower greater choice as to when to harvest and what to subsequently market;
- a system of shuttle trucks for delivering grain from farm storage to high

- throughput rail transfer depots;
- unit trains to link these rail transfer depots to the port export terminals; and
- disaggregated and transparent charging regimes that reflect true marginal costs.

The greatest impediment to moving to a new, more efficient system appears to be not the technology (which is well known) but to provide the firms with the right incentive to invest in this technology. The main impediments appear institutional, rather than technological.

In its discussions with stakeholders the Committee was presented with a range of commercial-in-confidence estimates of possible cost savings to growers from moving to a new, more technically efficient handling system ranging. These estimates ranged between A\$5-15per tonne, depending on growers' location, but assumed farmers already had on-farm storage available. The Committee considered that these cost savings from investing in more efficient infrastructure are likely to be achievable, but noted that where additional on-farm storage may be required, the cost of this would need to be factored into any overall estimate of cost savings.

The Committee also considered that where the right incentives can be provided (such as through increased competition in the system) it should also be possible to achieve some cost savings through the more efficient use of existing infrastructure. For example, a study of least cost grain paths in the Western Australian grain handling system found that moving to a system of grain handling where charges reflected resource costs and were disaggregated and transparent could result in savings in net supply chain costs to WA growers of between A\$12.5 million and A\$23 million per annum (Lindner and McLeod 1996).

Overall, the Committee believes that supply chain cost, including marketing, storage, handling and transport would fall faster if wheat marketing were opened up to greater competition. It is not convinced that Australian wheat exports are so small that there is room for only one seller for economies of scale and scope to be realised. Anecdotal evidence from overseas consultation suggests that the minimum critical volume required to achieve such economies is only in the range of 2 to 5 million tonnes of wheat traded. Because the current arrangements tend to reduce competition in the market for the above services, it appeared more likely to the Committee that the 'single desk' may be contributing to higher supply chain costs that reduce net returns to growers rather than lowering such costs. Therefore growers would benefit from the introduction of more competition into the grain supply chain.

7.2.5. The 'single desk' system – what are the other economic costs/benefits?

The Pooling System

Many submissions noted the benefits to growers of the pooling system in reducing risk and price uncertainty. The pooling system allows returns from the sale of wheat over time to be averaged across participating growers, and equalises returns across growers, although the latter aspect can reduce efficiency by distorting incentives for investment and production decisions.

Pooling is not dependent on the existence of a ‘single desk’, as pools are often run by marketers and cooperatives in competitive markets, precisely because of the risk management benefits to growers identified by stakeholders. Under more competitive marketing arrangements, there would continue to be strong demand for pools, including those run by AWB Limited.

In the consultation hearings, many growers stated that the current “mandatory pooling” arrangement eliminates the impact of “weak sellers” on receival prices. This was identified as one of the major issues leading to formation of the Australian Wheat Board in 1948. However, “mandatory pooling” arrangements also restrict growers’ capacity to manage their own price risk, leaving growers individually exposed to falls in the pool price, even though the pool is hedged to a degree.

Some stakeholders claimed that a ‘single desk’ marketer pooling returns to growers is almost immune from the risk of losing its own money, as they do not take ‘principal risk’ but merely deduct various administration and marketing costs from whatever price is achieved and distribute the remainder to growers. With an 80 per cent advance on harvest payments, this would give AWBI a 20 per cent margin for managing the risk of low prices or high costs. However, the case of the NSW Grains Board demonstrates that even this margin does not provide immunity from losses.

Another criticism of the current system is that because AWBI alone controls the standards for entry into a pool, even through the buyer of last resort obligation, should wheat not exactly match these receival standards, growers may not be able to access international market prices for their wheat. They may instead have to deliver into a lower quality pool at a significant discount, notwithstanding that active stack management would ensure that their wheat is blended into the higher value pool and sold overseas, with the marketer or bulk handler taking the margin.

Indeed, the membership of grower cooperatives is increasing because of dissatisfaction over the operation of AWB Limited pools. AWB Limited have indicated to the Committee that they plan to introduce greater contestability into the pooling operations by providing for cooperatives and other organisations to run pools as authorised agents of AWBI. These agents could acquire, quality assure and eventually undertake marketing functions without sacrificing the pricing discipline of the ‘single desk’. Growers would be able to choose between pools on the basis of services provided by the agents.

These developments would introduce a welcome degree of choice into pooling arrangements, but illustrate that the significant and recognised advantages to growers of pooling should be distinguished from the net public benefit of the ‘single desk’.

National Crop Risk Management

In the absence of adequate commercial insurance options such as multi-peril crop insurance, the ability of a ‘single desk’ seller to manage the risk of climate variability to the national crop is significant.

The recent floods in New South Wales and their impact on national production are a timely reminder of Australia’s high regional production risk. A ‘single desk’ seller is

able to manage climate risk on a national basis, with the risk premium attained for selling forward returned to all growers through the pool.

The 'single desk' provides a method of managing Australia's extreme climate variability that is highly valued by overseas customers and envied by competitors. In addition, the income stability it provides enables growers to plan in a manner consistent with environmentally sustainable development (ESD).

While this form of risk management is theoretically possible through national pooling in a more competitive environment, in practice, less national coordination would expose a large number of growers to an unacceptable level of regional production risk in the absence of commercial insurance or substantial government intervention.

Grower Risk Management

Growers need to manage a number of risks, including climate variability, the threat of disease, unstable currency and access to overseas markets. AWBI can manage payment and exchange rate risk on behalf of growers, centralising expertise and allowing growers to concentrate on growing. Delivery to the export pools saves growers the time and expense of undertaking their own marketing and managing their own price risk: it provides certainty and is administratively simple for growers.

Under more competitive arrangements, other organisations can also take on the task of managing payment and exchange rate risk. This function is unrelated to the 'single desk', and indeed the current arrangements limit further investment in this area.

The capacity of growers to manage their own risk according to their individual circumstances is restricted because the majority of growers are forced to deliver to pools, and have limited access to other risk management mechanisms. This denies individual growers and groups the freedom to develop their own skills, knowledge and ability to market their own produce successfully.

On the other hand, evidence provided by AWBI on the US market would indicate that only a minority of growers would actively manage their individual risk.

Crop Financing

As discussed by the Productivity Commission (2000, p.27), 'single desk' sellers emphasise access to cheap finance as a major advantage accruing to growers from their activities. Indeed, provision of harvest finance to growers provides access to a significant cash flow in advance of physical sales of wheat. This has positive flow-on effects in areas such as land values.

However, even if possession of monopoly exporting powers reduces financial risk for the single exporter and leads to lower debt costs which can be passed back to growers, this raises the question of why wheat growers should receive a form of assistance not available to many other Australian agricultural producers.

It also has been argued that the single exporter may choose to bear higher (or lower) levels of risk than those which would have been acceptable to individual growers.

Producer returns from the pool are not guaranteed and will fluctuate with market conditions. Thus producers may save on finance costs but are compelled to bear a level of risk which will not reflect the risk preferences of all growers. The development by the financial sector of new products aimed at managing risk may also be inhibited.

Further, earlier assertions by some stakeholders that banks would not provide harvest finance on terms competitive to AWB Limited appear to have been addressed by banks such as Westpac and the National Australia Bank providing harvest finance on competitive terms. The downwards pressure exerted by these competitors has resulted in significant savings to growers, which reinforces the Committee's belief that greater contestability of financial services will increase net returns to growers.

Quality Control and Hygiene

Industry cooperation combined with a highly centralised structure has facilitated uniformly high standards for wheat quality and hygiene. Any changes to wheat export marketing arrangements must therefore address this issue by encouraging continued industry cooperation.

A related issue is the effects on crop hygiene of increased on-farm storage under deregulation. The Australian marketing system, characterised by staggered timing of export cargoes and climatic conditions conducive to insect survival, benefits from high-standard centralised grain handling and storage that implements pest management practices. Whilst phyto-sanitary control is not unique to the 'single desk', the current arrangements favour bulk storage over on-farm storage, and as a consequence are more likely to lead to better hygiene. At a minimum, HACCP (hazard analysis critical control point) certification would be required of on-farm storage in order to maintain hygiene standards.

A fully competitive market would also reward quality to the extent that customers were willing to pay for it. However, high quality specifications may not be necessary in all markets, and if customers are not willing to pay for higher quality, AWBI is currently either missing sales or over-delivering to contract specifications, and therefore not obtaining the best price for wheat.

There may be an incentive in a deregulated environment for companies to sacrifice grain quality in order to be able to offer competitive prices on world markets, and so achieve short term profitability. Although there could be collateral effects on the reputation of Australian grain exporters that would act to the detriment of all in the industry, repeat customers are likely to be sufficiently sophisticated to discriminate between sellers who do, or do not, meet sale contract specifications. Hence customers in a competitive "market" would punish such behaviour by ceasing to deal with that marketer if the sacrifice in value from lower grain quality was not at least fully compensated by a reduction in price.

Access to Information

A number of growers claimed that AWBI provides them with central access to information such as international market forecasts. Despite the promise of easy access

to information over the Internet, poor communications infrastructure and lack of time impose practical limits on some growers seeking market information. The current arrangements allows AWBI to consolidate and distribute this information to growers.

AWBI also provides overseas buyers with access to information on the crop that assists them in planning their purchases to meet blending requirements. Buyers have told the Committee that this is one of the customer advantages of the 'single desk'.

Other submissions argued that with the Internet and modern communications capacity, growers can access up-to-the minute prices directly from CBOT, and a wide range of market forecasts. If AWB Limited is the sole source of information, it increases the risk that they may get it wrong and prejudice all growers rather than just those who rely on their information.

Other companies can provide marketing information services. Although this would cost farmers, the current cost is deducted from pool returns with no contestability.

Research and Development

The Grains Research and Development Corporation (GRDC) is responsible for planning, investing and overseeing research and development in 25 crops including wheat, delivering improvements in production, sustainability and profitability across the Australian grains industry. Wheat is the only national 'single desk' crop.

Research is directed towards four 'investment objectives': meeting quality requirements, increasing productivity, protecting and enhancing the environment, and delivering outcomes (uptake of research and technology). It is carried out by 'research partners' including state Departments of Agriculture, the CSIRO, universities, private organisations, technical advisers and growers. GRDC is also involved in a number of joint ventures or alliances, including Graingene which is a biotechnology venture, and has recently announced more commercial arrangements for investing in wheat breeding.

Funding is provided through a levy on grain growers, currently 1 per cent *ad valorem*. This is determined each year by the GCA. The Commonwealth Government matches this funding, up to an agreed ceiling of 0.5 per cent of gross value of production (GVP), currently around \$33 million.

It is claimed that guidance provided by the 'single desk' to the GRDC on international market requirements ensures that the only varieties to go through the expensive and time-consuming process of development, trial and implementation are those that can be sold on the international market within an existing segregation. The national coordination of wheat research is facilitated to an extent by this partnership, minimising inefficient duplication of resources.

Whilst effective restrictions on varietal development ensure that unsaleable varieties are not developed, there is a danger that they could limit innovation and market development. Improving export licensing arrangements would have the benefit of allowing more innovation in varietal development for niche markets, and for markets with different needs. It is instructive that in North America, R&D has achieved much

greater rates of yield increase in the US than in Canada where the focus of the plant breeding programs has been on quality.

The costs of any misjudgment by a single decision maker over future market demand could be very costly to wheat growers. According to the JISG (2000), these costs could arise both from decisions made about what varieties to register and commercialise, so as to fit into AWBI's grading system, and also from decisions about varieties that are not approved. Further, AWBI may refuse to receive a particular wheat variety because it does not fit into its marketing strategy, leading to a potential conflict of interest in the increasingly likely scenario where varieties in which AWB Limited controls property rights are in competition with other varieties being marketed by competitor organisations. In many areas, such a variety might be very high yielding and able to be sold into the domestic or niche markets.

Consideration needs to be given to the continuity and consistency of the various arrangements for quality assurance, receival standards, quality standards and grading, and the flow of information from marketers to researchers and breeders.

The GRDC have highlighted the importance of industry cooperation in coordinated research and development. If the 'single desk' is to continue, GRDC has suggested that the holder should have Community Service Obligations (CSOs) including:

- provision of market information to the Australian wheat research community, particularly through the GRDC;
- the coordination of wheat levy collection and associated source information; and
- the collection of end point royalties of wheat varieties.

7.2.6. Social impacts - do the current arrangements support regional income and employment in the wheat belt?

Theory/discussion

Throughout the review, and particularly during the consultation process, there was a strong sentiment expressed by stakeholders that the 'single desk' does indeed offer a social benefit. The AWBI system of payments and marketing clearly provides growers with a sense of security, which subsequently underpins confidence within the business community and rural communities at large.

In its inquiry into the effect of the National Competition Policy on rural Australia, the Productivity Commission suggested that the reform of some statutory marketing arrangements could also create concentrated adjustment problems for certain communities (PC 2000). If, for example, the removal of these arrangements were to result in greater efficiencies, there may be some structural adjustment as farming jobs are lost and supply chain providers shed jobs.

Given that wheat is primarily grown in a narrow belt through the south east and south west of Australia (the wheat/sheep zone) any changes in regional employment that result from a change in export wheat marketing arrangements are likely to occur in this zone.

ACG (2000b) point out that structural adjustment based on greater efficiency would likely lead to changes in the production mix on farms and could in fact result in a higher value of production overall as other grains and oilseeds compete with wheat. In some circumstances, there could also be increases in employment, for example, if some functions that are currently centrally administered by AWB Limited become decentralised as producers choose to market and distribute their wheat.

The Committee noted that many growers appear to fear this alternative marketing arrangement. Indeed, during the public forums, numerous growers requested that a popular vote be taken on the future of the 'single desk'. Whilst such a vote was clearly outside its terms of reference, the Committee undertook to express these concerns in this report.

ACG also point to the difficulty in distinguishing between any changes which may specifically result from changes in wheat marketing arrangements and those operating more broadly, such as changes in Australia's terms of trade, the reduction in industry assistance, the development of new metropolitan industries, and so on.

One broad demographic change is a long-term population loss across much of the Australian wheat belt. Coupled with this change is the redistribution of the remaining population, with some medium sized country centres (known as 'sponge cities') tending to increase in size while smaller centres shrink. ACG conclude that there are clear existing patterns of rural consolidation that are likely to continue to occur anyway. Thus any employment loss may reinforce ongoing changes in regional employment and service delivery patterns. Conversely, any employment gain is, at best, likely to ameliorate these same inevitable changes in regional employment and service delivery patterns.

ACG also examined a list of social benefits for regional Australia from the 'single desk' based on the consultations conducted by the review Committee. ACG concluded these benefits were largely independent of the 'single desk' arrangement and could be achieved in the absence of the 'single desk' arrangement.

Evidence/studies

To obtain some idea of the likely flow-on impacts throughout the economy from the removal of the 'single desk', ACG conducted sensitivity analyses using Econtech's MM600+ model of the Australian economy. Both the economic and social effects are discussed in the following section.

The Committee noted in its overseas consultations there was anecdotal evidence that the competitive situation prevailing in the US had increased employment in the grain service industries through greater localised competition to purchase growers' grain, but could not obtain any definitive studies.

7.2.7. Ecologically Sustainable Development

Australian export marketing arrangements for wheat interact with the natural environment in two ways: managing the crop in accordance with climatic conditions, and encouraging environmentally-sound agricultural practices.

Australia has a highly variable climate, and the ‘single desk’ provides a basis for national crop risk management (dealt with above) in a manner consistent with ecologically sustainable development principles.

The Committee found evidence that on-farm environmentally-sound sustainable agricultural practices are more likely to occur where there is enough stability in farm income to allow growers to plan ahead and invest accordingly. Therefore, whichever marketing arrangement best provides for income stability and maximises returns is likely to best encourage sustainable agriculture.

The Committee believes that its suggested improvements to the wheat marketing arrangements will improve grower returns and maintain relative income stability, and in that way contribute to ecologically sustainable development of the wheat industry.

7.3. Estimated changes in net welfare

7.3.1. Scenario analysis

Four scenarios were considered in the ACG analysis. Each of these scenarios simulated the effects on the economy of changing from a single seller system to a multiple seller system by changing wheat returns to growers and grain supply chain costs. The implications for the Australian community overall were then calculated by comparing the resulting changes in annual economic welfare (defined as the maximum amount consumers would be prepared to pay to have the ‘single desk’ abolished without them being worse off – see ACG 2000a p.67).

To simulate the possible effects of foregoing the ‘single desk price premium’ in changing from a single seller system to a multiple seller system, wheat returns were reduced by either US\$105 million a year (based on ACG’s re-calculation of AWBI’s estimated total premium), or by US\$13 million a year (ACG’s own estimate of the maximum premiums a price discriminating monopolist would be able to obtain, after allowing for uncertainty).

To simulate the possible effects of reducing grain supply chain costs in changing from a single seller system to a multiple seller system, ACG reduced grain supply chain costs in the model by the US\$5 per tonne, based on the 1995 Booz, Allen and Hamilton study. ACG argued that without the benefit of a more recent industry-wide benchmarking exercise, the Booz, Allen and Hamilton estimate of US\$5 per tonne in domestic efficiency savings was a reasonable estimate of the efficiency gains obtainable from the introduction of greater competition into the grain transport and storage sector. Although this study was conducted in 1995, the results are consistent with confidential information from several other sources.

In scenario one, it was assumed that the removal of the ‘single desk’ could result in the loss of additional export revenue from premiums of US\$105 million a year (based on ACG’s re-calculation of AWBI’s estimated total premium). However, it was also assumed that greater domestic competition in the storage and transport of wheat results in a US\$5 per tonne productivity gain, equivalent to an average productivity

gain of US\$110 million a year. Thus, the aggregate impact on net returns to wheat growers in scenario one would be to increase net returns by US\$5 million, equivalent to US\$0.23 per tonne for a 22 million tonnes wheat crop.

In scenario two, the same assumed productivity gain in storage and handling was combined with a loss of additional export revenue from premiums based on ACG's own estimate of the loss (after simulating the uncertainty effect) of the maximum premiums a price discriminating monopolist would be able to obtain (US\$13 million a year). The aggregate impact on net returns to wheat growers in scenario two would be to increase net returns by US\$97 million, equivalent to around US\$4.40 per tonne for a 22 million tonnes wheat crop.

Scenarios three and four included the same two losses of export revenue as in scenarios one and two, but assumed lesser cost savings from greater domestic competition in wheat storage and handling, equivalent to only half the cost savings assumed in scenarios one and two.

In ACG's view, scenario three represented the 'worst case' scenario, combining a possible US\$105 million loss of export revenue (from the loss of price premiums) with gains of only US\$55 million from cost savings from greater competition. Scenario two represented the 'best case' scenario, combining a possible US\$13 million loss of export revenue with gains of US\$110 million from cost savings from greater competition. A more detailed discussion of the scenarios is contained in ACG's report (ACG 2000a).

7.3.2. Results of analysis

In scenario two the cost savings in grain services, combined with the lower domestic price of wheat, flow through to the economy in the form of lower domestic prices. This results in a decreased cost of living for Australians, an appreciation of the exchange rate, and higher private consumption. In scenario three these effects are reversed.

In scenario two, the international competitiveness of Australian wheat exports rises resulting in increased demand for Australian wheat exports. In scenario three there is a loss in international price competitiveness resulting in a reduction in the volume of demand for Australian wheat exports.

ACG stated that based on the sensitivity analysis conducted, it is difficult to draw an overall conclusion as to whether the economy would gain or lose from the removal of the 'single desk'. ACG calculate the gains in annual welfare which would represent the maximum amount consumers would be prepared to pay to have the 'single desk' removed without them being worse off (the compensating variation measure of gain from economic reform). Overall, ACG estimate that moving from a single seller to a multiple seller system may result in a long term change in economic welfare varying from between a net loss of A\$71 million to a net gain of A\$233 million.

Examining the output and employment impacts by region, the results from the ACG general equilibrium modelling suggest that in the best case scenario (scenario two), the main gains are concentrated in non-capital city regions. Increased employment

and output are good indicators of the economic benefits associated with reform. That is, increased employment and output suggests that there will be increased resources flowing into non-capital city regions with a subsequent increase in activity, output and employment.

7.4. Impacts on stakeholders

The following summarises the Committee's conclusions, which are consistent with the main findings of the AGC and evidence collected from submissions and through the consultation process with respect to the impact on particular groups if the 'single desk' is removed.

7.4.1. Producers

Producers delivering to the export pool

ACG estimates that, at most, the loss of AWBI's monopoly 'single desk' would result in a decrease in export returns of US\$13 million a year. ACG also estimate that the most likely logistic supply chain cost savings would be at least US\$55m. While accepting this as a general indicator of the magnitude of possible losses, the Committee also considers it important to consider further evidence on the likely impact in specific markets, particularly those from which AWBI may be obtaining the bulk of its export premium.

If AWBI is forced to compete for supply for export wheat then increased competition will most likely reduce costs along the market chain to appear attractive to wheat producers. Thus, while there may be a possible decline in revenue, the degree to which growers delivering to the export pool are better or worse off will depend on changes in supply chain efficiency and the extent to which they are captured by producers.

If AWBI is forced to compete for supply this may also lead to a re-evaluation by that organisation of the value of further developing specific markets. For example, some potential markets may have been missed, but others developed (or serviced) to a greater extent than would have occurred under a competitive environment. A re-evaluation of marketing effort may lead to the obtaining of additional revenue or the achievement of additional cost savings.

Producers generally

To the extent that net returns received by growers delivering to the export pool might increase domestic wheat prices, even producers not delivering to the pool but selling only to the domestic market may be better off if the 'single desk' were to be abolished. If the impact on net returns from the export pool is small, however, then the extent to which producers outside the pool have been receiving higher domestic prices is also likely to be small.

7.4.2. Consumers

Flour millers, stock feed processors, and intensive livestock feeders

These groups may gain slightly from a reduction in domestic wheat prices, and vice versa. However, they would not get world parity price throughout the year.

Final consumers

The degree to which these gains will flow to final consumers will be a function of competition in individual markets.

7.4.3. The economy

Rural and regional economies

General equilibrium modelling conducted by ACG suggests that regional communities will be better off in the long term in income and employment terms if the AWBI 'single desk' is removed.

The economy generally

Under three of the four scenarios modelled by ACG, total national welfare improved. This implies that Australia as a whole would be better off economically.

7.5. Concluding remarks

Based on the assessments examined by, and undertaken for, the Committee in its consideration of the 'public benefit' test, the Committee concludes it has not been presented with, nor could it find, clear, credible, and unambiguous evidence that, on balance, the current arrangements for the marketing of export wheat are of net benefit to Australian wheat growers or to the Australian community. The NCP guidelines place the burden of proof of net benefit on those arguing for the retention of anti-competitive legislation. This suggests, therefore, that the WMA should now be modified, or repealed. This said, however, several points need to be acknowledged.

The estimation of net benefit is a complex and difficult exercise. On balance, the Committee has come to the view that the introduction of more competition into export wheat marketing would have a greater chance in the future of delivering benefits to growers and the wider community in the future than a continuation of the current arrangements. On the 'single desk price premiums' claimed to be earned by AWBI under current arrangements, conflicting evidence was presented to the Committee. Despite some claims that substantial premiums are being earned, most of the evidence the Committee was able to obtain supported the view that, averaged across all markets, such price premiums were likely to be small. At the same time, the Committee received convincing evidence that the current restrictions on competition have had an inhibiting effect on innovation and the development of new markets for Australian wheat. Furthermore, considerable evidence was provided that the 'single desk' has had an anti-competitive effect on the grain supply chain, constraining

vertical integration and impeding the realisation of least cost grain paths and potential cost savings in grain receipt, storage, handling and transport.

However, the Committee was also concerned that the information base for assessment pertained only to the former statutory Australian Wheat Board era rather than to the new privatised arrangements, and sees the need to allow the new manager of the 'single desk' - AWBI - to gather more information on the 'single desk price premiums' it may be able to achieve in the new global market characterised by more differentiated product, and the potential efficiency savings which may be able to be achieved for growers using the new domestic market grain supply chains being formed by the privatised bulk handling companies. In this context, the scheduled 2004 review (discussed in chapter 6) may offer one final opportunity for a more compelling case that the 'single desk' delivers a net benefit to the Australian community to be compiled.

Recommendation 6:

The Committee recommends that the 'single desk' be retained until the scheduled review in 2004 by the Wheat Export Authority (WEA) of AWBI's operation of the 'single desk'. However, the main purpose and implementation of this scheduled review should be changed so that it provides one final opportunity for a compelling case to be compiled that the 'single desk' delivers a net benefit to the Australian community. In particular:

- **the WEA review would allow further information to be gathered about the level of 'single desk price premiums' and about the ability of AWBI to achieve significant and sustainable cost savings in the supply chain for the benefit of growers; and**
- **if no compelling case can be made by the time of the 2004 review that there is a net public benefit, then the 'single desk' should be discontinued; but**
- **if a compelling case can be made by the time of the 2004 review that there is a net public benefit, then the 'single desk' should continue with ongoing regular WEA reviews of AWBI's performance in managing the 'single desk', and if necessary, a further NCP review in 2010.**

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8. ALTERNATIVES

The guiding principle set out in the Competition Policy Agreements is that legislation should not restrict competition unless it can be demonstrated that the benefits of the restriction to the community as a whole outweigh the costs, and the objectives of the legislation can only be achieved by restricting competition. The terms of reference direct the Committee to submit a view of future arrangements for wheat exports which are consistent with this guiding principle. Accordingly, this chapter identifies relevant possible alternatives to the wheat export arrangement in the *Wheat Marketing Act 1989* (WMA), including non-legislative approaches.

Key sections in chapter:

- Full repeal of the WMA
- Modification of the WMA

8.1. Full repeal of the WMA

This section discusses the type of marketing systems which may evolve in the short term if the WMA were to be repealed.

8.1.1. Overview of effects

Under the WMA, the export of wheat in bulk is effectively restricted to one seller (currently AWB (International) Limited (AWBI)), while other companies are permitted to export bagged and containerised wheat, provided they are granted an export consent by the Wheat Export Authority (WEA). The WEA is required to consult with AWBI on each occasion it is considering an export consent application. If the WMA were repealed – that is, multiple sellers were permitted to export bulk wheat as well as bagged and containerised wheat – it is likely a number of other companies (including bulk handling companies, State grain marketing organisations, grower cooperatives, and domestic and international grain traders), would compete with AWBI to purchase wheat for export or provide competing pooling arrangements through which wheat would be sold.

How significant a share of the market these new players would acquire would depend on AWBI's ability to retain grower loyalty, to offer comparable returns to growers, to supply market services to growers at competitive rates, and to maintain sound relations with their international customer base. Given the dominant market position from which AWBI would be starting, and the high regard in which it is held by many growers and customers, it is expected that AWBI would continue as the dominant player in the export marketing of wheat at least in the short to medium term.

Australian customers consume more than eight million tonnes of grain annually, with wheat accounting for about five million tonnes. AWB (Australia) Limited's grain trading activities have diversified from the early 1990s when milling wheat accounted for around 80 per cent of business. In 1999 about 50 per cent of AWB (Australia)

Limited's revenue was generated from feed grains, oilseeds and pulses (AWB Limited 1999).

It is likely some of the new entrants in an expanded wheat market would seek to concentrate on specific market niches, possibly as specialised receivers and accumulators of grain for resale to the larger export marketers such as AWBI and international grain traders. A large trader such as AWBI may find it economic to buy or to allow entry of some wheat into its pools in the fob (export) position rather than to receive all export wheat directly from farms as is now the case. Having more players in the market would give growers a greater choice in selling their grain. As is the case now with the domestic market, growers would need to satisfy themselves as to the business credentials of any new traders.

New entrants could be expected to seek out the most economic providers of grain storage, handling and transport services, increasing competition for these services and reducing costs. As with marketers, it is likely that many grain storage, handling and transport providers would concentrate on specific market niches and act as accumulators of grain on behalf of either marketers or larger handlers.

Effects at receipt

Currently growers have a number of choices at delivery, including cash sale to domestic traders (including AWB (Australia) Limited), or delivery to AWBI's export pools. It is likely that in a market where more buyers were able to sell for export, there may be more emphasis on cash sales as buyers compete to accumulate marketable parcels of bulk grain. It is also possible AWBI as well as other traders would offer a greater number of more specialised export pool options. To manage this greater range of options, many growers may decide to utilise the services of a specialist grain broker to sell export wheat on their behalf in order to ensure that they receive the highest possible price. Such grain traders presently trade in other grains and oilseeds, and as livestock producers use stock and station agents to market their cattle, sheep and wool.

Effects through the marketing chain

Currently most grain storage and handling is conducted by the bulk handling companies. Historically many of these organisations have had statutory monopolies within state boundaries. In recent years most States have moved to privatise these organisations and reconstitute them as grower-owned companies. As a result, some of these organisations have begun to extend their operations outside their traditional state base, and into other areas of business activity.

It is likely that in a market where more buyers were able to sell for export there would be more potential purchasers of storage and handling services, with more scope for the current bulk handling companies to diversify their activities. At the same time, there would be more competition from new entrants into grain storage and handling, and more pressure to cut costs (see chapter 7). The current trend to consolidate storage into fewer and larger facilities more suited to rapid intake and outturn may also be accelerated.

Effects at point of export

The most obvious effect of moving to a more deregulated export market structure would be a likely increase in the number of sellers able to offer Australian wheat to overseas buyers. As mentioned, AWBI would most likely remain dominant in the short to medium term, provided it continued to offer superior service and attractive payment options to growers.

8.1.2. Effects on AWB Limited

If new players entered the export wheat market, it is likely the structure and functions of AWB Limited and its subsidiaries would also change to counter the new competition.

Company structure

If AWBI no longer held the 'single desk', 'A' and 'B' Class shareholders in AWB Limited would as soon as practicable (under the constitution) have to vote separately on whether AWB Limited should continue to operate pools and maximise net pool returns to growers, and on other restrictions in the company constitutions designed to protect pool growers. A vote against continuing these arrangements could in turn lead to the object of AWB Limited being altered (although this would require a separate vote passed by at least 75 per cent of 'A' Class shareholders: Clause 4.1, AWB Limited constitution) so that it was no longer primarily involved in grain trading and carrying on the current pooling arrangements. If this was to occur, AWB Limited would cease to be a grower owned and controlled company (all 'A' Class shares would be automatically redeemed: Clause 4.2(a), AWB Limited constitution) and the company would possibly then become more like any other major grain marketer/trader. In addition, AWBI would no longer be bound by the obligation of buyer of last resort.

AWB Limited 'B' Class shares are intended to be listed on the Australian Stock Exchange in the latter half of 2001. This will inevitably lead to a reduction in current, almost total, grower ownership of these shares. However, the present limit on any person or entity holding more than 10 per cent of 'B' Class shares should prevent competitor companies obtaining a controlling interest in AWB Limited.

Joint ventures

AWB Limited has a number of joint venture/alliance arrangements in place, including:

- the Melbourne grain export facility with Australian Bulk Alliance (Grainco and AusBulk);
- AWB Seeds (with Revell, IAMA) and Graingene (with CSIRO and the Grains Research and Development Corporation) for developing and commercialising new varieties and seeds; and
- Agrifood Technology (quality testing) and an alliance with SGS Australia for seed testing and seed certification.

In addition, AWB Limited has an arrangement with the Adelaide Bank for administration of pool harvest payments and additional financial products and services to growers. It also has a long term agreement with Australian Transport Network (owners of Tasrail) to provide rail services in NSW and Victoria.

Investments

AWB Limited also has other investments such as in the Dimboola (Victoria) grain receival facility; and in overseas facilities including Five Star Flour Mills in Egypt, and Shenzhen Grain milling in China. It also is involved in ship chartering.

8.1.3. Potential new market entrants

There are a number of organisations which could compete for supplies of export wheat with AWBI, or alternately, offer services to new wheat exporters (Table 8.1).

Table 8.1: Some potential players in a multiple seller wheat export market

ORGANISATION	ACTIVITY	COMMODITY	STATE	LEGISLATION
ABB Grain Ltd	Marketing, Financing; Seeds	Coarse Grains; Oilseeds; Pulses.	Export, SA, Vic, Interstate.	Grower company. SDS through delivery for export restrictions SA and Vic.
Grain Pool WA	Marketing, Financing; Seeds	Coarse Grains; Oilseeds; Pulses; Wheat	Export, WA	Statutory authority. SDS through compulsory acquisition Barley, Canola, Lupins - WA.
Grainco Australia Ltd	Marketing, Financing; Storage and handling; Port operations; Seeds; Crop Insurance; Container services; Risk management.	Coarse Grains; Oilseeds; Pulses; Wheat, Mining, Forestry, Manufacturing and processing products.	Export, Qld, NSW, Vic, SA	Grower company. Vesting Barley and wheat – SDS Barley - Qld. SDS through vesting Barley, Sorghum, Oats, Oilseeds – NSW.
Cargill	Marketing, Storage and handling; Value adding.	Any, incl. Coarse Grains; Oilseeds; Pulses; Wheat	Export, Any State	Nil. Private company.
Bustan International Pty Ltd, Oceania Australia Pty Ltd, Louis Dreyfus Australia Pty Ltd	Marketing	Any, incl. Coarse Grains; Oilseeds; Pulses; Wheat	Export, Any State	Nil.

Alternatives

ORGANISATION	ACTIVITY	COMMODITY	STATE	LEGISLATION
GrainCorp/ Vicgrain	Storage and handling; Marketing financing; Rail/road transport	Wheat, Coarse Grains; Oilseeds; Pulses; Woodchips; non-agric. commodities	NSW, Vic, Qld, SA.	Merged grower company. Vic – Office Regulator General determines export charges.
Australian Bulk Alliance	Storage and handling; Port terminal (Melb.) Marketing.	Coarse Grains; Oilseeds; Pulses; Wheat	NSW, Vic	Nil. Grainco-SACBH Joint venture.
AusBulk Ltd (formerly SACBH)	Storage and handling; Marketing, Financing; Port operations; Road transport;; Grain processing; Containerisation; Engineering.	Wheat; Coarse Grains; Oilseeds; Pulses.	SA, Vic, NSW.	Nil. Grower company from former statutory SACBH.
WA Cooperative Bulk Handling Ltd	Storage and handling, manufacturing, grain hygiene; Grain terminal developments; Seeds.	Wheat; Coarse Grains; Oilseeds; Pulses.	WA	Statutory receival rights but restructure possible as grower company.
FreightCorp	Rail	All freight incl. Wheat; Coarse Grains; Oilseeds; Pulses	NSW	Government corporatised body but sale announced. Access regime in place.
Freight Australia	Rail	All freight incl. Wheat; Coarse Grains; Oilseeds; Pulses	Vic	Privatised company structure. Access regime in place.
Australian Southern Rail	Rail	All freight incl. Wheat; Coarse Grains; Oilseeds; Pulses	SA	Privatised company structure. Access regime in place.
Wesrail	Rail	All freight incl. Wheat; Coarse Grains; Oilseeds; Pulses	WA	Government corporatised body but sale announced. Access regime in place.
Qld Rail	Rail	All freight incl. Wheat; Coarse Grains; Oilseeds; Pulses	Qld	Government corporatised body. Access regime in place.

NB: An access regime allows third party access to the infrastructure and facilities of a natural monopoly. SDS = 'single desk' seller.

Grain marketers

ABB Grain Ltd

ABB Grain Ltd (the successor to the former Australian Barley Board) is a grower owned company operating in South Australia and Victoria. ABB Grain Ltd investor shares are traded on an exempt market. Mirror legislation in South Australia and Victoria provides that exports of barley produced in those States can only be made through ABB (Grain Export) Ltd, a wholly owned subsidiary of ABB Grain Ltd. This provision is due to expire on 30 June 2001 in Victoria, with South Australia facing an NCP review in two years.

ABB Grain Ltd's main activity is marketing and financing grower payments for malting and feed barley through pools, on export and domestic markets. Domestic marketing is kept separate from export activity. The company also offers cash options for barley and markets barley interstate. ABB Grain Ltd also markets other coarse grains, oilseeds and pulses, through pools and cash purchases, with the majority of sales on export markets.

The company is increasingly involved in C&F sales involving ship chartering.

ABB Grain Ltd does not have joint venture arrangements with storage and handling companies although it was a foundation shareholder in VicGrain when that organisation was privatised.

ABB Grain Ltd is a partner in Graintrust, an integrated grain management company principally involved in development multiplication and distribution of new seed varieties. Other partners are Australian Field Crop Association, Combined Rural Traders/Town and Country, Grainco, NSW Grains Board, Paramount Seeds (a subsidiary of Elders) and the Grain Pool of WA.

ABB Grain Ltd also has a shareholding in the Five Star Flour Mill in Egypt (AWB Limited is also a shareholder) and with a company including European and US trading interest.

Grain Pool of Western Australia

The Grain Pool of Western Australia is a statutory marketing authority under the WA *Grain Marketing Act 1975*. It has 'single desk' selling rights for barley, lupins and canola produced in WA although the domestic market is in effect deregulated. The 'single desk' arrangements were recently extended and the outcome of the NCP wheat review will have a major effect on the future of those arrangements.

The Grain Pool of WA also markets wheat, other grains, oilseeds and pulses domestically and/or for export through a wholly owned subsidiary AgraCorp. Pooling and cash options are also offered to growers. The Grain Pool finances pool payments for statutory grains.

The Grain Pool makes C&F sales and is therefore involved in ship chartering.

The Grain Pool is a partner in Graintrust, an integrated grain management company principally involved in development multiplication and distribution of new seed varieties (See under ABB Grain Ltd).

The Grain Pool is looking at a possible more corporate structure including a possible merger with Cooperative Bulk Handling (CBH) in that State (although AWB Limited and CBH have already announced an alliance).

New South Wales Grains Board

The New South Wales Grains Board operates under the *Grain Marketing Act 1991* and has vesting powers over barley, sorghum, oats, oilseeds and any other declared grains, although domestic trading is generally deregulated (an agency fee is payable to the Grains Board). The vesting and 'single desk' powers were recently extended for a further five years to allow the Board time to recover from recent large trading losses. The Grains Board was formed from the merger of separate Barley, Oats, Grain Sorghum and Oilseeds Boards that operated in the 1980s.

The Grains Board operates and finances pools, largely for export. The Board also trades in NSW and interstate in wheat, coarse grains, oilseeds and pulses on a cash basis or through other trading options.

The Grains Board has alliances and partnerships with storage and grain cleaning/grading/packaging organisations and it is a member of Graintrust, an integrated grain management company principally involved in development multiplication and distribution of new seed varieties (See under ABB Grain Ltd).

Following the recent announcement of trading losses the vesting powers of the Grains Board has been sold to Grainco, still retaining its 'single desk' status for at least five years.

Grainco Australia Ltd

Grainco Australia Ltd is a grower owned unlisted public company developed from Grainco Queensland Co-operative Association Limited. The latter was formed through the merger of three statutory marketing boards with two associated cooperatives and one major grain handling authority. Grainco shares are traded on an exempt market.

Grainco holds vesting powers for wheat and barley through the *Grain Industry (Restructuring) Act 1991*. However, the domestic market is effectively deregulated. Grainco operates and finances pools for barley while wheat exports are handled through AWBI. Grainco Australia's core business includes the accumulation, trading, storage and handling of grains, oilseeds and pulses and the sale of winter planting seed, crop credit and winter crop insurance.

Through its wholly-owned subsidiary Globex International Pty Ltd, the company also owns and operates four Queensland based import/export port terminals at Brisbane's Fisherman Islands and Pinkenba and at Mackay and Gladstone. The company is expanding its operations to service non-grain industries, including mining, forestry, manufacturing and processing.

Another wholly owned subsidiary, Agricultural Risk Management Services provides commodity risk management, brokerage and education services to growers.

Grainco formed a joint venture company Australian Bulk Alliance (ABA) with AusBulk (formerly SACBH) in July 1999. ABA owns and operates grain receival and storage facilities in NSW and Victoria and receives and trades in a range of grains. Further interstate facilities are likely.

ABA is a partner with AWB Limited in the new \$40 million multi-bulk commodity facility in the Port of Melbourne.

Grainco provides a specialist range of container packing and unpacking services to importers and exporters of bulk and bagged products including grains, oilseeds, pulses, meals, fertiliser and industrial minerals through Chalmers Commodities Pty Ltd. Chalmers Commodities is a joint venture company, formed by Globex International Pty Ltd (a wholly-owned subsidiary of Grainco Australia Limited) and Victorian-based transport company, Chalmers Industries Limited.

Other marketers

Bustan International Pty Ltd is a middle east owned Australian company with grain trading and other diversified agricultural interests in Australia, chaired by a former Chairman of the Australian Wheat Board.

Cargill is a major multinational grain trader with horizontal and vertical integration in many related sectors. Cargill is a private company. Cargill and GrainCorp have a joint venture to develop storage and handling facilities in NSW. Cargill has another joint venture with a NSW grain merchant to build grain storage facilities in NSW.

Louis Dreyfus Australia Pty Ltd is an Australian subsidiary of a major multinational grain trader.

Oceania Australia Pty Ltd. is a major grain exporter in Australia.

Storage and Handling

GrainCorp/Vicgrain

GrainCorp and Vicgrain (the privatised grower companies formed from the former statutory storage and handling authorities in NSW and Victoria respectively) merged in October 2000. GrainCorp is listed on the Australian Stock Exchange, as will be the new entity.

The only remaining legislative control is in Victoria where the Office of the Regulator General has a role in determining rates for grain services through the grain export terminals at Geelong and Portland to ensure competitive access.

The new entity will have storage and handling operations in States other than NSW and Victoria and be involved in grain marketing and seed services. Pooling and cash options for a range of wheat and other grains are offered. Vicgrain also handled woodchips and other non-agricultural commodities.

GrainCorp and Vicgrain were both partners in Nugrain (with CBH, AusBulk, Nufarm and Wesfarmers Dalgety) to develop biotechnology and new varieties. Nugrain may form other alliances eg with Monsanto.

GrainCorp formed a joint venture with Cargill to develop grain storage and handling facilities in NSW. GrainCorp also has an agreement with FreightCorp in NSW to operate grain rail transport on some branch lines. GrainCorp and Vicgrain are involved in road transport including on farm pickups.

Grainco Australia Ltd

Grainco is a potential competitor in storage and handling, including export ports in Queensland and through the Australian Bulk Alliance with AusBulk.

AusBulk (formerly SACBH)

Until recently AusBulk operated under legislation giving it exclusive rights over the storage and handling of SA grain (mainly wheat, barley, pulses and oilseeds). AusBulk is now a grower owned company with possible listing on the Australian Stock Exchange.

AusBulk will be in a position to expand current activities which in addition to storage and handling include grain marketing and financing, freight, quality services, grain processing and cleaning, containerisation and engineering.

Through the Australian Bulk Alliance (ABA) with Grainco, AusBulk owns and operates grain receival and storage facilities in NSW and Victoria and the port terminal at Melbourne with AWB Limited. Further interstate facilities are likely.

AusBulk is a partner in Nugrain (with CBH, GrainCorp and Vicgrain, Nufarm and Wesfarmers Dalgety) to develop biotechnology and new varieties.

WA Co-operative Bulk Handling Ltd (CBH)

WA CBH members recently rejected a proposal to restructure from a statutory body with legislative storage and handling rights over grain in WA to a grower owned privatised company without legislative backing.

The proposed new structure would have allowed WA CBH to make alliances with AWB Limited (already announced) and a possible proposed merger with the Grain Pool of WA. WA CBH is the only storage and handling body not involved in grain

marketing. The alliance with AWB Limited may have achieved potential efficiencies in acquisition, receipt, transport, storage, marketing, trading and financial services for grain. WA CBH has been largely operating in the storage and handling sector, including manufacturing, grain hygiene and grain terminal developments.

WA CBH is a partner in Nugrain (with AusBulk, GrainCorp and Vicgrain, Nufarm and Wesfarmers Dalgety) to develop biotechnology and new varieties.

Cargill

Cargill and GrainCorp have a joint venture to develop storage and handling facilities in NSW. Cargill has another joint venture with a NSW grain merchant to build grain storage facilities in NSW.

Transport

Grain rail freight services in South Australia, Victoria, NSW and Western Australia have been or are in the process of privatisation. Qld Rail remains as a corporatised statutory entity. Access to infrastructure under National Competition Policy has been implemented in each State leading to a number of regional or private operators.

In addition, GrainCorp has an agreement with FreightCorp to operate grain trains on some NSW branch lines and Austrac (a private) company operates regional grain (and other commodity) trains in NSW.

AWB Limited has a long term agreement with Australian Transport Network (owners of Tasrail) to provide rail services in NSW and Victoria.

8.2. Modification of the WMA

Repeal of the legislation is only one of the alternatives. Other alternatives include possible changes or amendments to the legislation to achieve the objectives of the legislation in a manner which is less restrictive of competition. These may include:

- changed arrangements which would introduce more competition into the export market; and
- other changes to introduce more competition into the domestic market for wheat marketing services where AWBI remains the sole, or the dominant, exporter of bulk wheat under legislation.

8.2.1. Alternative export arrangements

The Committee considered the merits of a number of possible changes to export arrangements suggested by stakeholders, including export licences, allowing multiple exporters for specialist wheats and separating 'non-premium' markets, and also auctioning or selling off the 'single desk' in its entirety, as happened with the NSW Grains Board.

Export licences

An export licence may involve the issuing at fixed price, or auctioning, of a licence to sell either to a specified country or countries, or to sell on the open market, with some specific countries excluded. Alternately, the licence may be to sell a specified volume.

Selling export licences by auction has an advantage over, for example, imposing export taxes, in that it is not necessary for the Government (or WEA) to estimate the degree of market power Australia may have in each market (if any). If a licence is auctioned, it is the bidders who must assess the potential net revenues from the export market, and the risks involved, and tailor their bids accordingly. Provided bidding is competitive, each bidder should be prepared to pay up to the expected monopoly premium for the export right. An auction would have the added advantage of revealing the size of the expected 'single desk price premium' to the auctioning agency.

There are also potential disadvantages in attempting to auction export licences, however. One would be the administrative cost of holding regular auctions. There would be further administrative costs involved in tailoring each licence for the specific market and licence holder. Finally, there would be the practical difficulty of trying to exert control over sales to any particular market. While the Committee received evidence of systems for doing so in other countries and for other produce, such systems would nevertheless incur costs of ensuring compliance with the terms of the licence. Finally, there would remain the problem of how to distribute the proceeds of the auction of the export licences in order to achieve the objective of the legislation to maximise net returns to growers.

In view of these difficulties, the Committee considers that auctioning export licences would not be a cost efficient method of overcoming some of the current delays associated with case-by-case assessment of applications for an export consent. Instead, any system for issuing these licences should be kept as simple and as transparent as possible. The Committee considers a system of fixed-fee annual licences issued to exporters to sell on the open market (possibly with some specific countries excluded) would be reasonably simple to administer, and has ample precedent in existing systems of export licensing for some other rural export products.

Allowing multiple exporters for specialist wheats or 'non-core' markets

A number of stakeholders suggested to the Committee that they had recently expanded production of specialty wheats in an endeavour to increase their returns, and wished to have the option of exporting these wheats directly to their export customers if they chose. These wheats included durum wheats, noodle wheats, and soft wheats. Further, these stakeholders suggested to the Committee that as growers, they would consider continuing to expand plantings of these wheats if they could be assured the possibility of being able to directly access a market beyond the limits of the Australian domestic market.

The Committee observed that durum wheat growers, for example had in recent years expanded production well beyond domestic market requirements of a specialty type of wheat which has a distinctly different end use to bread wheat (see chapter 3). In the

Committee's view, there may be an opportunity to give durum wheat growers expanded marketing choice and the opportunity to increase net returns through specialty marketing, without prejudicing the current arrangements for the marketing of bread, soft and noodle wheats. The Committee considers that if this were done, there would be no reason why AWBI should not continue to run export pools for those durum growers who continued to wish to deliver to AWBI, though without the obligation of buyer of last resort.

The Committee considered that in principle, a somewhat similar argument could be made for providing more marketing options for producers of noodle and soft wheats. However, the Committee also noted the increased practical difficulty of distinguishing these wheats from other types of bread wheat, and also that AWBI has developed the export markets for noodle and soft wheat. More importantly, there is convincing evidence that such premiums as might be being earned by the 'single desk' are largely confined to these classes of wheat. Accordingly, the Committee is not recommending trials at this point for these other specialty wheats.

Allowing multiple exporters to access 'non-premium' markets

The Committee also considered the case for giving growers expanded choice in exporting wheat to bulk markets in which it could be convincingly demonstrated that AWBI had not, and had no prospect of, achieving a 'single desk price premium'. An advantage in allowing multiple exporters to access 'non-core' markets would be that this would inject more competition into the marketing chain by allowing non-AWBI exporters to accumulate reasonably large parcels of wheat for export, without reducing any 'single desk price premium' currently being obtained by AWBI.

However, there are a number of aspects which require further consideration. For example, firms that only have access to non-premium markets would only be able to offer a fob price to wheat growers equal to the competitive cif price in those markets less the cost of insurance and freight. On the other hand, unless it ran separate pools for wheat destined for different markets, AWBI should (and would be obliged) to offer a higher fob price because of the monopoly price premium earned in premium markets. To compete, other firms would need to be more innovative and discover opportunities for cost savings that more than offset the higher prices earned by the exporter for which the 'premium' markets had been reserved.

Auctioning the 'single desk'

An alternative to auctioning licences to single markets or for specified volumes would be to auction or sell the 'single desk' in its entirety. A recent example is the sale of the NSW Grains Board vesting rights to Grainco for \$25.2 million for five years. This may prove administratively less complicated than regularly auctioning off licences for small quantities, but many of the same drawbacks would still apply to this option.

8.2.2. Domestic arrangements

A number of alternative arrangements have been suggested to try to introduce more competition into domestic arrangements for the provision of grain services in an environment where AWBI is the sole, or the dominant, exporter of bulk wheat. These

suggestions have addressed the appropriateness of granting a monopoly to a private company.

One criticism of current arrangements is that the domestic arm is given an unfair advantage on the domestic market by its association with the much larger export pool. It has been suggested that rather than taking possession of wheat at point of receipt, AWBI should purchase at export terminal, thereby allowing other organisations to trade in 'export' wheat up to the actual point of export.

Another criticism is that growers want the holder of the 'single desk' to market their wheat, not merely offer to buy it selectively on contract.

Criticism has been levelled at the AWB Group's acquisition or planned acquisition of storage and handling facilities. AWB Limited claim that the financial arrangements for the provision of these services are internal and not clearly separable from other system costs.

It has been suggested that the Board of AWBI be separate from the Boards of other AWB Group companies, in order to assist transparency and contestability in service delivery to AWBI. AWB Limited provides services to AWBI in the areas of pool administration, finance and bulk handling and logistics.

The Committee considers that transparent contestability of service arrangements overseen by the WEA through appropriate performance indicators in the context of the 2004 review would address these criticisms without unduly interfering in AWB Limited's internal arrangements.

Relating to this, the AWB Group's internal compliance Committee may be a further issue for the WEA to address in its 2004 review.

Other Issues

There were a number of other issues relating to possible alternatives to the wheat export arrangement which were drawn to the Committee's attention. These included:

- the export of wheat in bulk to Papua New Guinea and New Zealand;
- the sale of wheat by Australian millers to their overseas operations, such as in Papua New Guinea and New Zealand;
- AWB Limited investment in flour mills either in Australia or overseas (which are competitive to Australian-owned mills); and
- access to national wheat pools by domestic consumers.

While the Committee has sympathy for these stakeholders, it concluded that satisfying their aspirations was incompatible with retention of the 'single desk'. AWB Limited has assured the Committee that it can resolve these issues within the 'single desk' system. This view is not shared by various stakeholders, who informed the Committee that, despite repeated discussions with AWB Limited, some of these matters have remained unresolved to their satisfaction for a number of years. One major stakeholder suggested (unsuccessfully) passing its own wheat inventory through the AWBI pool for export to its overseas milling operation in New Zealand (ie a sale and

purchase from AWBI at the same level). This would, in their view, remove costs from the chain without AWBI losing control of bulk wheat exports from Australia.

In chapter 6 the Committee recommended the establishment of an industry forum. Issues such as these could be discussed at such a forum, and the Committee also suggests that the WEA take matters of this nature into consideration in its 2004 review process.

Recommendation 7:

The Committee recommends that the WMA be amended to suspend Section 57 (3A) (which requires the WEA to consult with nominated company B (AWBI) before giving consent to applications to export in containers and bags) to enable a three-year trial of more competitive arrangements for the export of wheat in containers and bags to all markets except those markets where there is minimal freight rate differential between containers and bags, and bulk wheat.

Recommendation 8:

The Committee recommends that the WMA be amended to suspend, for durum wheat only, Section 57 (3B) (which requires the WEA to obtain prior approval in written form from nominated company B (AWBI) before giving consent to applications to export bulk wheat), and Section 84 (1) (which states that nominated company B (AWBI) must purchase all wheat that is offered to the company for inclusion in a pool), to enable a three-year trial of more competitive arrangements for the export of durum wheat.

References

AWB Limited 1999, *Annual Report 1998-99*, Melbourne.

Productivity Commission 2000, *Single-desk Marketing: Assessing the Economic Arguments*, Productivity Commission Staff Research Paper, AusInfo, Canberra.

9. OPTIONS FOR REGULATION AND MECHANISMS FOR INCREASING EFFICIENCY

This chapter sets out a preferred option for regulation in light of both adherence to National Competition Policy (NCP) principles and the results of the ‘net public benefits’ test. It also examines mechanisms for increasing the overall efficiency, including minimising the compliance costs and paper burden on small business, of the existing arrangements, or viable alternatives.

Key sections in chapter:

- Options for regulation
- Mechanisms for increasing efficiency

9.1. Options for regulation

9.1.1. Retention of the ‘single desk’ at least in ‘core’ markets until 2004

In chapter 7 it was noted that, based on data from 1997 to 1999, researchers commissioned by the Committee had not been able to identify ‘single desk price premiums’ of any more than around US\$13 million a year. The Committee was concerned, however, that the data used had not been gathered specifically with the objective of assessing ‘single desk price premiums’ in mind. Also, virtually all of the data related to sales by the statutory former Australian Wheat Board, rather than AWB (International) Limited (AWBI). Additionally, on the question of grain storage, handling and freight costs, the Committee noted that there had been a significant move toward the formation of new domestic market grain supply chains in the last few years. Thus, although the ‘public benefit’ test was not satisfied by the evidence presented in chapter 7, the Committee was of the view that further information may need to be gathered before it could be concluded that the post-1 July 1999 system had no potential to demonstrate a net benefit to the Australian community.

Therefore, one option may be to retain the ‘single desk’ at least in ‘core’, or ‘premium’ markets until the scheduled review in 2004 by the Wheat Export Authority (WEA) of the operation of the ‘single desk’ by AWBI. A review of the net benefits to the community of the ‘single desk’ at this point would have the advantage of access to at least three years’ data on AWBI’s export sales performance. The 2004 review would also be able to examine whether AWBI had been able to obtain significant and sustainable supply chain costs savings for growers. By ‘significant’ the Committee means reductions in nominal national average supply chain costs of the order of \$A5-10 per tonne. By ‘sustainable’ the Committee means the supply chain costs should be able to be sustained in the future, and not merely achieved by the transfer of supply chain costs from AWBI to other parties in the supply chain, or by the deferral of necessary capital expenditure in the short term.

9.1.2. Export of bagged and containerised wheat

As discussed in chapter 8, to encourage further development of small niche markets, and remove some of the administrative impediments currently seen as hindering such development, the Committee recommends the trial suspension of the requirement in section 57 (3A) of the *Wheat Marketing Act 1989* (WMA) for the WEA to consult nominated company B (AWBI) before giving consent to applications to export bagged and containerised wheat. Associated with this, to remove the need for sale-by-sale approval of exports of bagged and containerised wheat, the WEA should introduce a system whereby it issues licences to approved exporters.

The trial period for improvements in the export licensing of bagged and containerised wheat would be for 3 years, and would be reviewed by WEA in 2004 against clear and transparent performance indicators, to be established by the WEA in consultation with industry and Government. It would contain no guarantees as to continuation of the trial beyond 3 years, precluding any claims for compensation on the basis of infrastructure investment decisions made on the basis of the trial improvements.

The Committee recognises that, as a consequence of the limited period of the trial and the lack of certainty over extension of the trial period, infrastructure investment decisions in this area may be deferred until WEA decides to continue or discontinue the export licensing arrangements. This risk is far outweighed by the potential benefits of conducting the trial.

The Committee notes that AWBI would retain a significant market advantage due to its size and international reputation, and that a competitive response by AWBI would be to the benefit of growers.

9.1.3. Export of durum wheat in bulk

As discussed in chapter 8, to encourage further development of the durum wheat industry, the Committee recommends the trial modification of the requirement in section 57 (3B) of the WMA for the WEA to obtain prior approval in writing from nominated company B (AWBI) before giving consent to applications to export durum wheat in bulk. The WEA could approve bulk exports of durum wheat through a system of licences similar to that suggested above. The trial would have the same conditions as the recommended trial for bagged and containerised wheat. The 'buyer of last resort' facility would be suspended during the trial period.

The Committee recognises that whilst a durum trial would provide an indication of the effects of competition, these effects would not necessarily be duplicated if full competition were introduced across the entire wheat industry.

Indeed, AWB Limited have indicated to the Committee that they plan to introduce greater contestability into durum marketing by providing for cooperatives and other organisations to run durum pools as authorised agents of AWBI. These agents could acquire, quality assure and eventually undertake marketing functions without sacrificing the pricing discipline of the 'single desk'. Growers would be able to choose between durum pools on the basis of services provided by the agents. Whilst these developments would introduce an increased degree of choice into durum

marketing arrangements, the Committee still believes that the proposed trial is a better approach to address the issues raised by durum producers.

9.1.4. Review in 2004 of the management of the 'single desk' by AWBI

The Committee has also recommended that to remove uncertainty, the process of the 2004 review needs to be clarified as soon as possible and clearly communicated to the Minister and stakeholders.

9.1.5. Obstacles to competitive marketing arrangements

As mentioned, although it has been suggested that the changes to the export licensing of bulk durum and container and bag exports would provide a precedent for full deregulation, these changes are intended to improve the current arrangements, as the Committee does not intend for them to provide an appropriate model for deregulation of the 'single desk' in bulk wheat exports.

However, the improvements will enable the proponents of deregulation to provide practical demonstrations of the claimed benefits of deregulation that will inform future debate on the 'single desk'.

The Committee has observed that, at a minimum, the following are necessary as preconditions to any successful moves towards deregulation:

- improvement in telecommunications infrastructure to allow most growers to access mobile communications during harvest, as well as affordable high-speed Internet access to assist in low-cost market research;
in public meetings the Committee was informed that there were areas in the wheat belt not covered by standard electronic transmission, but understand that telecommunications are improving, and that the technology is evolving with recent developments likely to somewhat address these deficiencies before 2004
- grower access to education in risk management and financing options to allow growers to reap the benefits of increased competition in these areas;
- mechanisms to ensure maintenance of the high quality of Australian wheat;
- appropriate comparisons with deregulated Australian grains industries and overseas markets to identify and plan for likely costs, benefits and distributional effects;
- sound industry-government planning processes to manage smooth implementation of any deregulation over a number of years; and
- demonstration and articulation of the net economic benefits to the Australian community of deregulation.

9.2. Mechanisms for increasing efficiency

The question of change to regulation aside, the Committee is of the view that the administrative costs of complying with the current 'export permit' system may be detrimental to the efficient operation of the marketing system, particularly the costs to small business.

9.2.1. Compliance costs under the WMA

It was evident to the Committee that exporting bagged and containerised wheat involves various costs. One of these is the administrative cost of providing detailed information to the WEA on a sale-by-sale basis. These costs are largely incurred irrespective of whether the export application is successful. Another potential cost is the loss of sales which may incur because of delays in approvals.

The Committee's view is that while the WEA has made significant progress in streamlining the administration of the export permit system (and reducing costs to potential exporters), the rationale for actually having the current export permit system needs to be examined. An option for reducing compliance costs would be to replace the current export permit system by an export control system where the exporter is licensed, as recommended by the Committee.

Under the current arrangements, aspiring exporters of bulk wheat also face the same type of costs faced by potential exporters of bagged and containerised wheat. In fact, these costs are likely to be greater, particularly if (as suggested to the Committee by several potential bulk wheat exporters) there is little likelihood that an application for export of wheat in bulk will be successful.

9.2.2. Paper burden on small business

The Committee found that compliance with the current export permit system places a considerable paper burden upon small business. There was little evidence that moving from a single seller system to a multiple seller system would appreciably increase the paper burden in delivery imposed on small businesses. Growers utilising a number of sellers for export wheat may have to spend more time to keep track of deliveries and payments than if they delivered only to AWBI's pools. However, as noted elsewhere in this report, delivery to AWBI's pools would continue to be an option for growers under a multiple seller system.

APPENDIX ONE – SUGGESTED EXPORT LICENCE REGIME

LICENCE CRITERIA

- Applications for licences for the export of Australian wheat in bags and containers and or durum wheat in bulk by exporters should be considered against a set of prescribed criteria that should be publicly available. Such a set of criteria should include the following elements:
 - the financial standing and reputation of the applicant;
 - the integrity of the applicant;
 - whether the Wheat Export Authority (WEA) has previously cancelled a licence held by the applicant; and
 - commitment to provide required information

LICENCE CONDITIONS

- Licences should be non-transferable.
- A change in the licence holder's circumstances should be advised to the WEA as soon as practicable. The WEA should be able to revoke the licence holder's licence if the adverse change of circumstances is substantive.

LICENCE REVIEW

- Licences should be renewed on a twelve monthly basis.
 - Licence renewals should place the onus on the licence holder to demonstrate effectively to the WEA that they have complied with the conditions of the licence.

REQUIREMENT TO CONSULT

- There should be no requirement to consult with AWB (International) Limited (AWBI).

FEES AND SECURITY OF PAYMENT

- Licence applications and renewals should both be subject to the payment of a prescribed fee to the WEA by the applicant.
 - These fees should be set on a cost recovery basis.

INFORMATION PROVISION

- Licence holders should supply the WEA with a *Return of Wheat Exported* form at the end of each quarter in order to ensure that the WEA has appropriate information about the export of wheat from Australia.
 - It may be possible for the WEA to develop an export certification system that interfaces with AQIS's EXDOC certification system, which would mean that data required would be minimised (note that the EXDOC system already

interfaces with the Australian Customs Service's EXIT system for this purpose).

LICENCE SUSPENSION AND CANCELLATION

- Licences should be subject to suspension or cancellation at any time in certain prescribed circumstances to be set by the WEA in consultation with all sectors of industry and Government.
- For the 3 year trial, breaches of licence conditions should result in licence cancellation and the applicant be prohibited from holding an export licence for the remainder of the trial period, or such other period as determined by the WEA.
- Export of wheat significantly in breach of the licence conditions would attract the penalties currently provided for breach of s.57(1) of the Wheat Marketing Act 1989 (WMA).

APPEALS

- An appropriate appeals system should be put in place to deal with licence application or renewal decisions by the WEA.

APPENDIX TWO – REVIEW COMMITTEE

Mr Malcolm Irving AM (Review Chair), is Chairman of Caltex Australia, the Australian Industry Development Corporation and a number of other organisations. He is also a director with Telstra, a member of the Supermarket to Asia Council and was Chair of the Australian Horticultural Corporation for nine years.

Mr Jeff Arney is a South Australian grain grower, Chair of the South Australian Farmers Federation Grains Council and a past President of the Grains Council of Australia.

Professor Bob Lindner is Executive Dean of the University of WA's Faculty of Agriculture. He was also the faculty's inaugural Professor of Agricultural Economics. He is Chair of the WA Herbicide Resistance Initiative Board and a member of the Export Grains Centre Advisory Council.

Secretariat

The Review Committee was supported by a Secretariat provided by the Department of Agriculture, Fisheries and Forestry: Rob Newman, Graham Love, Christopher Swain, Catherine Haas, Bronwyn Davis and David Williamson.

APPENDIX THREE – TIMETABLE FOR REVIEW

(4 April 2000 - 31 December 2000)

The timetable for this review was:

NCP Review announced	4 April 2000
Issues paper released; call for submissions	15 May 2000
Preliminary discussions with interested parties	May 2000
Consultation hearings - overseas	8 - 21 July 2000
Deadline for submissions	17 July 2000
Consultation hearings - domestic	31 July - 11 August 2000
Draft report released for comment	13 October 2000
Deadline for written comments on draft report	13 November 2000
Draft report consultation hearings	VIC/NSW/QLD 13 - 15 November 2000 SA/WA 29 November - 1 December 2000
Final report delivered to Minister	22 December 2000

A Class Shareholders (growers) elect 7 Directors

B Class Shareholders elect 4 Directors

AWB LIMITED
(Nominated Company A)

- Holding company
- Sole shareholder of AWB (International) Limited
- Responsible for services to other member companies of the AWB Group
- Obligation to ensure AWBI is managed to maximise net pool return to growers
- Service Level Agreement with AWB (International) Limited and AWB Finance Limited

Unlimited Guarantee

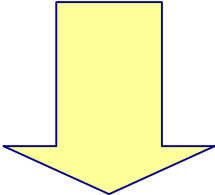
A\$100 million subordinated loan

AWB Finance Limited
(Nominated Company C)

- A\$5 million nominal capital
- Responsible for providing finance to growers delivering to AWBI
- Borrows from global capital markets to provide working capital loans to AWBI, AWB Asia and AWB US.
- Service Level Agreement with AWBL and AWBI

AWB (Australia) Limited

- A\$5 million nominal capital
- Responsible for domestic grain trading and commercial activities
- A\$200 million committed bank facility



AWB (International) Limited
(Nominated Company B)

- A\$5 million in nominal capital
- Responsible for the export pooling of wheat and maximising net pool returns to growers
- Service Level Agreement with AWB Limited and AWB Finance Limited
- Pays AWB Limited a fee for administrative, human resources, marketing, risk management, funding, shipping and treasury services.

AWB US Ltd

- A\$5 million nominal capital
- Responsible for a range of AWB group activities in the US

AWB Asia Ltd

- A\$5 million nominal capital
- Responsible for coordinating all sales and marketing in Asia

Agrifood Technology Pty Ltd

- A\$5 million nominal capital
- Responsible for quality assurance and testing services

AWB Research Pty Ltd

- A\$5 million nominal capital
- Responsible for research and development services