Response

Interim report of the review of the Competition and Consumer (Industry Code – Port Terminal Access (Bulk Wheat)) Regulation 2014

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1. Regulation must reflect maturing industry

The Port Terminal Access (Bulk Wheat) Code of Conduct (“the Code”) has provided a stable mechanism for the wheat export industry to transition from full regulation to a lighter level of regulation and ultimately, towards regulatory alignment with other industry sectors.

The period since deregulation has been notable for the significant level of investment in supply chain infrastructure in eastern Australia – up-country and at port – by multiple industry participants. It has also seen product and process innovation to improve efficiency and service levels. There has never been more competition or choice for grain growers or grain traders in this region.

Australian grain exports are also subject to intense competition in global markets from much larger exporters such as Canada, (which has recently deregulated grain exports) and the United States. More recently, this pressure has intensified through a material escalation of competition from the Black Sea region, notably into key Asian markets. Grain from Ukraine and other Black Sea origins has historically enjoyed a substantial cost advantage over Australian grain, however these origins have also made substantial quality advances – making it even more crucial that the Australian grain industry is positioned to respond to global competitive pressure.

In this context, it is critical that Australia minimise unnecessary regulation and continue to encourage supply chain investment, innovation and efficiency.

GrainCorp notes the proposal made in the ACCC’s submission to extend the Code’s application to all grains and up-country infrastructure. Increasing regulatory burden in this manner would be a regressive step for the industry and would have significant consequences, including increasing cost and reducing the competitiveness of Australian grain exports in global markets, reduced incentive to invest in improving efficiency and constrained ability to innovate and improve customer service.

The Australian grains industry has demonstrably made a positive transition following deregulation, yet faces an increasingly competitive global trading environment. GrainCorp reiterates its recommendation that the industry should continue the deregulation process and move to a more industry self-regulated model for the Code, where governance and administration rest with an appropriate industry body. This is consistent with Productivity Commission recommendations made in 2010 and is how the overwhelming majority of industry transactions are already successfully handled. This transition could include provision for further review to ensure there were no unintended consequences.

2. Strong competition in eastern Australia: no case to extend Code provisions up-country

GrainCorp is proud of its track record as an open-access provider of storage, logistics and port terminal services over many years.

As outlined in our original submission, there is significant overcapacity and strong, countervailing competitive pressures in eastern Australian grain markets, from country storage through to export.

We note the acknowledgement in the ACCC’s response to the Department’s Interim Report that “the upcountry storage and handling market is more competitive on the east coast where there are strong domestic and container trade markets to complement the bulk export market...”

This is consistent with the ACCC’s position in various reviews of grain markets, most recently the Bulk Wheat Ports Monitoring Report of 2016-17:

Compared to WA and SA, many growers in eastern Australia may have access to alternative and competing markets for their grain, such as domestic markets or a significant export container market....

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7 ACCC response to DAWR Interim Report, p.5
Where demand for port terminal services is below supply as per the situation on the east coast (in part due to the oversupply of capacity) PTSPs have some incentive to provide access on fair commercial terms to drive use of their infrastructure.

Growers in eastern states have greater choice when marketing their grain and greater incentive to invest in on farm storage.\(^2\)

This competition was also recognised by the Productivity Commission in its 2010 Inquiry into wheat export marketing arrangements:

*Consumption of grain by the domestic market...is likely to represent a significant constraint, particularly on the behaviour of port terminals in the eastern states. If the costs of exporting grain are too high, selling it at home will be more attractive to growers.*\(^3\)

The existence of strong competition is demonstrated by the following facts:

- There is a significant surplus of country storage capacity (an estimated 41.5 million tonnes of storage capacity to handle average production of 18 million tonnes).
- Annual domestic demand of 8-10 million tonnes provides a strong competitive draw and generally has first call on the grain, meaning a substantial portion of domestic grain never touches a bulk handling network.
- A strong container packing sector has emerged that generally accounts for between 15-20% of production and acts as an additional draw away from bulk handling networks.
- Over the past four years, GrainCorp’s up-country share of production has averaged 42% (see Figure 1 below).
- GrainCorp’s crop receivals at the most recent harvest totalled 35% of production (see Figure 1 below).
- The clear majority of grain production is stored outside GrainCorp’s network (including most of the domestic and container demand outlined above):
  - Approximately one-third is stored on farm;
  - Around 28% is stored with other providers.
- There are approximately 220 active buyers posting prices for grain within GrainCorp’s open network. There is clear price discovery in Australian grain markets, with global prices visible at ports, and translated into competing bids posted by multiple traders in locations throughout the country – at GrainCorp’s sites, in competing networks, at container packing sites and on-farm via online trading platforms.
- Over the past four seasons, GrainCorp has only purchased between 9.9% - 12.3% of eastern Australian production from growers. The vast majority of the crop is being purchased by other market participants. Within its own open network, GrainCorp generally purchases only around 30% of stock.
- Over the most recent three completed shipping years, an average of only 21% of total production was exported in bulk through GrainCorp’s ports (see Figure 1 over the page).
- In addition to the investment in new bulk ports, the use of mobile bulk loaders at port is a significant recent competitive development and there is no barrier to similar competition emerging in other port zones, such as central Queensland.

The competitive environment in the eastern Australian grain market is visually represented in Figure 1 over the page.

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\(^{2}\) ACCC 2016-17 Bulk Wheat Ports monitoring report, pp. 9, 14, 15

\(^{3}\) Productivity Commission – Inquiry into Wheat Export Marketing Arrangements, No. 31, July 2010, p. 202
Figure 1: Eastern Australia’ competitive market for grain

Avg. Eastern Australian grain production
~18mmt*

~30% on-farm storage
~42% GrainCorp’s open network
~28% export

Total winter production (mmt)
GNC receivals (mmt)
Bulk exports GNC ports (mmt)

*GrainCorp’s open network
~20 bulk exporters
~200 domestic customers
GrainCorp purchases around 10-12% of total production directly from growers

Figure 2: ECA grain production: GrainCorp country and bulk export share

<table>
<thead>
<tr>
<th>Year</th>
<th>Total winter production (mmt)</th>
<th>GNC receivals (mmt)</th>
<th>Bulk exports GNC ports (mmt)</th>
</tr>
</thead>
<tbody>
<tr>
<td>14/15</td>
<td>14.8</td>
<td>6.6</td>
<td>3.0</td>
</tr>
<tr>
<td>15/16</td>
<td>16.8</td>
<td>7.1</td>
<td>2.9</td>
</tr>
<tr>
<td>16/17</td>
<td>27.1</td>
<td>12.1</td>
<td>6.8</td>
</tr>
<tr>
<td>17/18 *YTD</td>
<td>15.4</td>
<td>5.5</td>
<td>1.8</td>
</tr>
</tbody>
</table>
Figures 1 and 2 show GrainCorp does not have significant power or influence over grain flows. Grain prices are set by global markets and grain will sell if growers are prepared to sell their grain at the market price.

This information clearly demonstrates that claims of “market failure” are not substantiated by the facts in eastern Australia. In this light, the Department of Agriculture & Water Resources is justified in its finding that there is no basis on which to argue for extending the Code to cover up-country grain services in eastern Australia. No compelling evidence can be provided by any party of a “market failure” or “monopoly” up-country or indeed at any point of the supply chain.

2.1 Importance of flexibility in complex & competitive supply chain

Grain supply chains must be flexible and able to respond to a series of variable and competing demands, which increase complexity:

- Grain production is highly variable in eastern Australia, meaning demand can be intense in ‘peak’ seasons, and there can be extended periods where there is little demand on the network. Further, Australian grain exports generally peak during a window of 3-4 months after the harvest of the winter crop, before larger northern hemisphere crops become available.

- Grain quality is also highly variable and is generally segregated into different quality parameters, to ensure customer requirements can be met. Segregation is important to allow industry participants to extract value from grain, however it does increase complexity and cost in the supply chain.

- GrainCorp operates an open network, in which many customers own and store co-mingled grain. This generates many competing demands on grain availability, for example:
  - Exporters accumulating cargo from multiple sites using their own rail – going to GrainCorp ports or external ports;
  - Exporters accumulating from multiple sites using GrainCorp’s rail;
  - Exporters accumulating from multiple sites using road;
  - Exporters accumulating using port zone-based trade contracts;
  - Exporters arranging for grain to be delivered by road from farm direct to port.
  - Exporters accumulating to port from an external storage provider (not farm), GrainCorp may have a physically delivered contract with our exporting customer as part of their accumulation.
  - Domestic customers sourcing stocks via road and rail. Domestic customers often like to have grain available ongoing, even during the harvest period;
  - GrainCorp accumulating for its own export or domestic purposes.

- Grain is subject to insect infestations and requires regular fumigation, generally going under gas every 2-3 months for up to 28 days (including treatment and ventilation time). This means grain is not always immediately available at the location it was purchased.

- Given the high variability of demand, it is not economic to keep every grain site open every day of the year.

Notional stocks systems play a critical role in managing these various demands on co-mingled networks – and in ensuring grain is available for customers at the time when they need it. A notional stocks system has become particularly important in eastern Australia since the advent of multiple users of rail assets.

The ACCC’s submission raises generic concerns regarding notional stocks systems and whether they are used to disadvantage traders or whether the site swaps can be “used to discourage traders from purchasing grain above minimum specifications from growers in particular areas, as they may get swapped to another site where the quality of the same grade is lower”.

* ACCC submission
The ACCC further suggests that dispute resolution provisions at port may be underutilised because parties “may be reluctant to raise a dispute regarding port access if they also require services in other parts of the supply chain where the PTSP has market power”\(^5\).

GrainCorp makes the following observations in response to these matters:

- No data has been provided to support the above comments.
- Within Australia, grain is traded on the basis of industry-agreed commodity standards. While there are inevitably slight variances in stack quality from site to site, grain is bought and sold at an agreed GTA commodity standard, not at a stack, site or region standard – this is clearly understood by all market participants. GrainCorp’s Country Storage & Handling Agreement plainly expresses that a customer’s interest “represents an ownership right to stored grain of the grade that was classified on receival and not the same physical grain that was delivered.”\(^6\)
- GrainCorp has a strong commercial interest in acting in a manner that maximises volume throughput in its infrastructure, given the competitive alternatives our customers enjoy and the low utilisation rates of our fixed asset base. We want our customers to benefit from using our supply chain so they return to use it again. Behaving in the manner speculated would be damaging to our commercial interests.
- The suggestion that dispute resolution provisions at port may be underutilised because parties “may be reluctant to raise a dispute regarding port access if they also require services in other parts of the supply chain where the PTSP has market power”\(^7\) ignores the possibility that dispute resolution provisions at port are underutilised because they are either not required, or commercial resolutions have been reached.

GrainCorp acknowledges that periodically issues can emerge up-country (or at port) where a customer or their transport contractor may be dissatisfied. Occasional disputes are inevitable in a complex and highly contested supply chain. However, we note that such instances are, relative to the volumes handled, extremely rare and each instance has been able to be commercially resolved, without arbitration or legal action. Further, since the commencement of the Code, GrainCorp has successfully loaded 442 grain vessels\(^8\) with cargoes totalling over 14 million tonnes at our ports and handled over 31 million tonnes for export and domestic customers through our country network – without the need to resort to arbitration.

### 3. Unintended consequences of regulatory creep

Extending certain provisions of the Code up-country is likely to have several undesirable, unintended consequences:

- There would be a significantly reduced incentive for industry participants to invest in supply chain infrastructure – up-country and at port. Over recent years, GrainCorp has made major investments in its country network through its Project Regeneration initiative. There has also been significant investment from competitors throughout the supply chain. Regulating up-country infrastructure would act as a substantial deterrent for businesses considering further investment.
  - GrainCorp notes that it plans to invest in a significant grain receival site at Yamala, near Emerald in central Queensland. The business case of its proposed investment could be materially impacted by a move to apply access regulation to the site.
- Eastern Australian grain would become less competitive in international markets. Australia is already viewed as a high cost producer and is under substantial pressure in Asian markets from lower cost origins like the Black Sea, which have made substantial quality improvements. This is largely due to substantial investment in improved storage and transport infrastructure in the Black Sea region, meaning the quality premium Australian grain receives...

\(^5\) ACCC submission p. 10  
\(^6\) GrainCorp Country Storage & Handling Agreement Part D 2 (a) (ii), p.21 – emphasis added  
\(^7\) ACCC submission p. 10  
\(^8\) As at 16 May 2018
is narrowed. Imposing further cost and flexibility burdens on the Australian supply chain would be a serious restraint on the industry’s ability to continue competing.

› Reduced ability for country storage operators to innovate and improve their services to individual customers, for fear of triggering a regulatory response.

› Tying up-country regulation to particular port zones would generate substantial confusion and potentially distort grain flows, particularly as production is variable and unevenly distributed. The evolution of the industry means there is already substantial overlap in the drawing arcs of Portland, Geelong and Port Kembla. Additionally:

• Recent grain shortages due to drought in southern Queensland mean that grain in that port zone is drawn from NSW or other regions far beyond the ‘traditional’ arc.

• Additionally, grain has flowed from the regulated port zones of central Queensland to meet demand from the domestic market in southern Queensland.

› A likely acceleration in rationalisation of less efficient country sites, due to regulatory cost and complexity.

› Possibility of further supply chain complexity as separate “domestic only” supply chains evolve to avoid being captured by the Code.

4. Other matters

4.1 Stocks information
GrainCorp notes the ongoing discussion of stocks information disclosure and we reiterate we are open to equitable models that provide meaningful data for industry.

Along with other industry participants, GrainCorp agreed to participate in a stocks disclosure model that would recognise the market differences between eastern Australia (where there is strong domestic demand and competition) and the export-dominated states of Western and South Australia.

Eastern Australian market participants agreed to a model that would involve:

› Quarterly disclosure of total stocks held by state (monthly during harvest) by all commercial storage providers;

› Stocks held in on-farm storage included based on a sample survey;

› Additional disclosure of wheat and barley stocks, (wheat separated into milling vs. feed; barley into malting vs. feed);

› All information consolidated and de-identified by independent third party prior to disclosure;

› Proposed disclosure framework to be reviewed 2-3 years after it commences, to ensure it is providing information that creates value for all industry participants.

GrainCorp already provides weekly harvest updates of deliveries into our system during harvest.

4.2 Proposal to extend Code to cover all grains
The ACCC has recommended the Code cover all grains. This additional regulation is not necessary, because at GrainCorp’s ports, all grains are already effectively treated as if they were covered by the Code. This is the case because it is simpler and more efficient to have one process in place for all grains at a port.

Regardless of the grain, pulse or oilseed carried by a vessel, all vessels using GrainCorp ports are subject to the same Port Terminal Services Agreement and protocols; and all vessels are disclosed on our shipping stem in the same manner. Additional regulation to “enforce” a change in behaviour is not required.

Further, we do not accept the basis of the ACCC’s claim that GrainCorp (along with CBH and Glencore) has “market dominance” through its shares of non-wheat exports. It is misleading to link GrainCorp’s market share with that of other operators in other states to make this argument.
The data in Figures 5, 6 and 7 of the ACCC’s submission clearly show that GrainCorp’s market share of non-wheat exports in each jurisdiction is not “market dominant”. During 2016-17, GrainCorp’s market share for non-wheat exports is shown as follows:

- All Australian port-zones: 9.36% (and a six-year average of 10.13%);
- Queensland 12.73% (smaller share than both COFCO and Glencore);
- NSW 28.63% (smaller share than COFCO);
- Victoria 22.35% (comparable with Emerald); and
- Non-exempt ports: 4.02%.

These market shares clearly demonstrate that GrainCorp does not have “market dominance”.

5. Alignment of reporting under the Code

GrainCorp notes the suggestions made in the Department’s Interim Report and the ACCC’s response. We worked closely with the ACCC to develop our reporting when the Code was introduced and believe our reporting is aligned with expectations. We remain open to discussing opportunities to improve or streamline reporting.

6. Conclusion

The Port Terminal Access (Bulk Wheat) Code of Conduct has met its regulatory objective – it has provided a stable mechanism for the wheat export industry to transition from full export regulation to a lighter level of regulation.

Ultimately, the objective should remain regulatory alignment with other industry sectors, consistent with the clear recommendation of the Productivity Commission, which found that grain port terminals should be subject to the regular declaration provisions of Part IIIA of the Competition & Consumer Act. To extend regulation as has been proposed would undermine competitiveness, investment and would be in direct contravention of the Productivity Commission’s recommendations.

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9 Productivity Commission: op. cit. Recommendation 5.2 p. 16