RICEGROWERS' ASSOCIATION
OF AUSTRALIA INC

Submission to the Productivity Commission's Inquiry into the Regulation of Agriculture

Draft Report

AUGUST 2016

Introduction

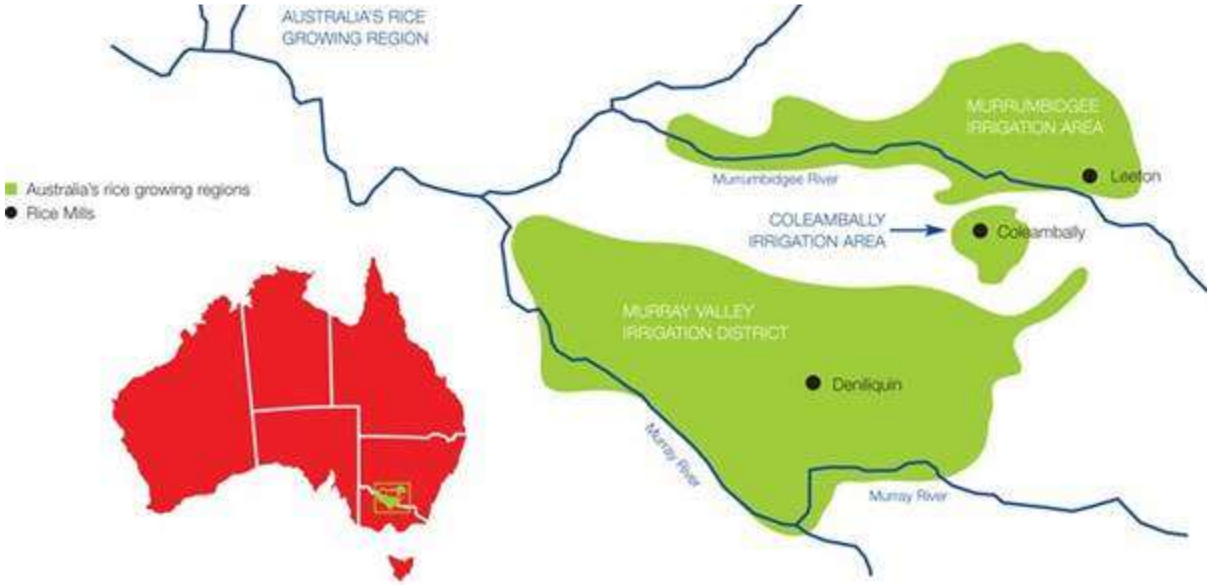
Thank you for the opportunity to make a submission to the Productivity Commission's (the Commission's) Inquiry into the Regulation of Agriculture - Draft Report.

The Ricegrowers' Association of Australia (RGA) represents the interests of around 1200 voluntary members, based in the main rice growing areas of the Riverina region of south western NSW.

RGA is a member of the National Farmers Federation, National Irrigators Council and NSW Irrigators Council, and support their submissions to this inquiry. Our submission is focussed on matters pertaining to the rice industry specifically.

Industry information

In Australia, rice is grown in the Riverina region in the south-west of NSW, predominantly across the irrigation areas of the Murrumbidgee and Murray valleys. The industry is also currently expanding into North Queensland to diversify climate and water availability risks. However, the vast majority of Australia's rice will continue to be supplied out of the Riverina as it is one of the best rice growing regions in the world, provided water is available. The temperate climate ensures high yields from extended and clear daylight hours, and a largely pest and disease free growing environment requiring minimal chemical use during production and storage. The soils are ideal heavy clay for rice growing and gravity fed irrigation systems deliver water to the crops efficiently.



In a typical year the industry produces around eight hundred thousand tonnes of paddy rice with a farm gate value of over $300 million. Our ability to continue to produce rice is due to the returns per ML our growers are able to attract. This is due to the clean, high quality niche varieties we grow, consistently high yields, the world's most efficient rice watering practices, an integrated rice farming system enabling mutual benefit between rotating crops, world's best practice storage and milling, and highly sophisticated branded marketing into over 60 countries around the world.

After value adding by the grower-owned milling and marketing company SunRice, total industry value is well over $1 billion each year. This makes the rice industry a significant economic contributor to the Riverina region of NSW. The towns of Griffith, Leeton, Coleambally, Finley, Jerilderie, Deniliquin, Wakool and Moulamein are highly dependent on rice production for their social and economic wellbeing.

RGA comments on the inquiry draft report recommendations

The RGA provides the following response to the Productivity Commission's (the Commission's) draft recommendation 11.1: The New South Wales Government should repeal the Rice Marketing Act 1983.

The Commission's recommendation is based upon two main arguments. RGA's response will address each of these arguments separately:

1. "It is unclear whether Australian rice exporters receive a price premium for their rice."

The Commission's report, by its own admission above, is inconclusive. The Commission should not be making a recommendation for change that could have huge ramifications for a whole Australian agricultural industry, and the many communities reliant upon that industry, based on inconclusive evidence.

Nevertheless the appropriate jurisdiction to assess the benefit or not of the single-desk rice export marketing arrangement (Rice Rice Vesting) is the NSW government. The RGA is supportive of the NSW Government's process of undertaking regular statutory reviews of the Rice Vesting arrangement. The RGA believes that this process is much more robust than the process implemented by the Productivity Commission. The clear lack of consultation with the Rice Industry has resulted in the Commission neglecting many critical facts when conducting their analysis of the Rice Vesting.

Nevertheless, the NSW Government reviews to date have found that the benefits of Rice Vesting do outweigh the costs and hence Rice Vesting should be continued.

For the RGA, the inconclusiveness of the Commission's report, the lack of consultation with the main rice industry stakeholders, and the fact that the report disregards many critical facts, means that the report of the Commission is considered unreliable. For these reasons, in assessing the costs and benefits of Rice Vesting, the RGA relies upon the more robust, independent reports prepared by Grant Thornton Australia.

Grant Thornton Australia's most recent report provides that the benefit of Rice Vesting equals $116.65 per tonne for growers (based on Export Price Premium of $82.4M plus a Freight Scale Advantage of $14.3M). Grant Thornton Australia's similar reports prepared in each of the preceding three years have also demonstrated a significant price premium for growers[1].

With respect to the cost of Rice Vesting, the Commission provides the following:

> *"Competing marketing companies would have an incentive to retain grower loyalty by maximising price premiums without incurring the costs of statutory marketing"*

However this argument is inconsequential taking into account that the cost of the RMB in 2014-15 was $564 000 or 68c per tonne (based on a total C14 crop size of 829,000 tonnes). This is considered a small price to pay to receive a price premium of $116.65 per tonne. We further note that the cost of the RMB is fully funded by growers (not taxpayers).

The Commission's report also glossed over the fact that the NSW domestic market for rice is deregulated, and that this is by far the most profitable market for NSW growers.

[1] 2013/14 (C13) additional $97.93 per tonne delivered to growers (based on Export Price Premium of $95.2M plus a Freight Scale Advantage of $18.5M and a total crop size of 1,161,000 tonnes); 2012/13 (C12) additional $82.44 per tonne delivered to growers (based on Export Price Premium of $65.9M plus a Freight Scale Advantage of $13.5M and a total crop size of 963,166 tonnes).

The importance of this price premium to not only growers, but to the local regional communities who are often solely dependent upon agriculture, should not be underestimated. For this reason governments must proceed with caution when questioning the value of Rice Vesting.

2. "Repealing the Rice Marketing Act 1983 (NSW) will create incentives for innovation and cost savings in rice marketing that could increase premiums for some rice growers."

The key to the above statement is the reference to "some rice growers". While a small minority of growers may establish successful niche export markets, the benefits of these opportunities are unlikely to extend to the majority of growers who collectively do not have the ability to establish and maintain export markets that would be more profitable than those established and maintained by SunRice. Nevertheless, any attempt to do so risks jeopardising SunRice's current marketing success, as explained below.

<u>Cost savings in rice marketing</u>

The Commission has failed to identify the following characteristics of NSW rice production, which set the rice industry apart from other NSW grain industries, and which result in Rice Vesting being critical to NSW growers obtaining the best price for their rice product:

A. While SunRice is not subject to export competition in NSW, the fierce competition for irrigation water requires SunRice to deliver its growers the best possible return, otherwise face losing these producers to other irrigation industries who potentially offer a greater return per megalitre. The obvious competitor for SunRice in this regard is the cotton industry; however SunRice also faces fierce competition from the grains and oil-seed industries.

   In addition, the fact that water trade allows water to freely move to crops that generate the highest return, means that SunRice must try to ensure that the return per megalitre for rice is greater than the market value of that water. For the 2015/16 season many growers chose not to plant rice as water prices, particularly in the Murray Valley, were considered too high to justify a rice crop.

B. Total NSW annual rice production is significantly smaller than other like grain industries. Taking into account a number of factors, it is unlikely that total production will consistently reach 1,000,000 tonnes in the near future. Furthermore, total NSW annual rice production is extremely unstable. For example, for the 2014/15 crop NSW rice growers harvested 244,184 tonnes of rice; this is less than half the rice produced the previous season, being 690,272 tonnes.

   The main factor driving this instability in total production is the variability of general security water allocations, which in turn is driven by rainfall. To this end it is unlikely that the NSW rice industry will see more stable levels of production in the near future.

   The smaller crop size and the instability set the rice industry apart from other NSW grain industries. These other industries are generally reliant upon a mix of irrigated and dryland farming enterprises and located across a large and diverse part of NSW. The variability in farm production methods and the geographical diversification mean that these grain industries experience much larger annual production with much less variability between seasons.

C. In comparison to other grain crops, significant investment in infrastructure is required to efficiently store, process and transport rice. Fortunately for growers, SunRice now owns a majority of its infrastructure outright, including all rice receivals. These efficiencies are also partially reflected in the freight advantage obtained by SunRice. In 2015/16 this freight advantage was valued at $14.3 million (2013-14: $18.5 million).

D. The NSW rice exports operate within a unique, challenging and often corrupt international trading environment, dissimilar to any other trading environment experienced by an Australian agricultural commodity.

The reason for this is simple; rice is the world's most important basic food staple and therefore critical to the security of many nations. This means that Rice continues to be one of the most highly protected agricultural commodities internationally. These protections include not only tariffs and trade barriers, but also onerous bio security policies, single desk buyers and cultural resistance.

The Commission also failed to mention that rice has been omitted from Australian Free Trade Agreement negotiation on three occasions: Japan, Korea and China. And while the Commission mentions Californian rice markets as having no market regulation, it fails to mention the distorting influences of the US Farm Bill and the Free Trade Agreement's for US agriculture.

E. The NSW rice industry must compete against subsidised product from other key exporting countries. Considering SunRice is a relatively small international player, its international success is credited to the strength of the Australian rice as a premium product. This brand recognition is due to SunRice's continued investment in branding, marketing, research and development and through SunRice's vertically integrated structure, as explained below. To SunRice's credit, it has maintained the power of this brand in key markets despite strong competition.

In addition, SunRice's ability to maintain a continuous supply of rice to key export markets, even throughout the millennium drought when annual production reached a low of 19,000 tonnes, is a testament to the benefit of the economies of scale created by Rice Vesting. SunRice's' understanding and experience in export markets, its ability to procure stock globally, and its investment in off shore facilities provides SunRice with an international trading advantage unlikely to be obtained by other local competitors.

F. The Commission has also failed to differentiate between international market characteristics for medium and long grain rice.

The RGA strongly believes that these characteristics of the rice industry mean that SunRice operates in the most cost efficient manner possible. The fierce competition for water, coupled with the rice industries small total crop size, the lack of stability of production, the investment required to store, process and transport rice, and most prominently, the difficult international rice trade environment, mean that economies of scale are particularly important to the rice industry.

The Commissions claim that deregulation will result in marketing efficiencies is incorrect and does not adequately factor in these industry characteristics.

<u>Innovation</u>

The Commission argument that repealing the Rice Marketing Act 1983 (NSW) will create incentives for innovation is based on the following

> *"The experience in other grain industries is that deregulation leads to innovation and reduces inefficiencies associated with single-desk marketing, which improves industry performance."*

However, again the Commission has failed to recognise that the rice industry is not like other grain industries. Other grain industries, despite deregulation, continue to export bulk unprocessed product. However SunRice exports a majority of its product as value added product (including rice cakes, rice flour, microwave rice and microwave meals). The value of this form of innovation and marketing to achieving a price premium is outlined in the Commission's own report:

> *"Price premiums can also be achieved by producing a product with intrinsic quality and service characteristics that consumers are prepared to pay more for, relative to commodity-grade alternatives."*

SunRice recognised this many years ago and for this reason has continually invested in research and development to add further value to its rice through the production, manufacturing, marketing and distribution of its products.

The ability of SunRice to invest large sums of money into research and development is reliant upon the maintenance of the Rice Vesting arrangement. Rice Vesting provides SunRice the confidence to make large R&D investments, even when the returns on these investments are unlikely to be realised for many, many years. This is particularly pertinent to the Pure Seed Scheme operated by RRAPL (a wholly owned subsidiary of Sunrice) and the Rice Breeding and Grain Quality Program, to which SunRice is the only private partner.

RRAPL also carries out a portfolio of other R&D projects to deliver higher yields, lower water usage and better market returns. The environmental sustainability of the industry is something SunRice treats with the highest regard, and hence continually invest in through its R&D program. It is unlikely that other similar organisations will have the economies of scale to invest in these types of programs and deliver the same level of return to growers.

SunRice Grower Services also offer growers a range of information, services, crop testing and technical advice to ensure growers maximise their production. This is a service SunRice is able to maintain partly due to the scale of its business.

SunRice's total supply chain control has also been critical to its continued innovation and strong performance, in addition to enabling SunRice to ensure the quality of its product and brand. SunRice's ability to oversee production from "paddock to plate" ensures that its varieties and products are developed specifically to service the needs and tastes of the most high value international markets. Its ability to use price signals to ensure levels of supply for specific varieties, coupled with its understanding of market demand, means that these high value markets are adequately serviced without excess.

In addition, SunRice's oversight of the production, milling and packaging process ensures the quality of the final product and again the value of its brand. The introduction of additional exporters who do not apply the same level of oversight to this process will potentially jeopardise the perceived value of Australian rice in overseas markets.

Taking into account the relatively small size of the industry, efficiencies of scale are also important to every aspect of the paddock to plate model outlined above.

The Commission further provides that:

> *"price premiums are not necessarily evidence that single-desk marketing is working — price premiums can also be a result of normal commercial innovation."*

However a new entrant to the market will not be able to compete with the level of commercial innovation that SunRice is currently delivering.

Taking into account the sensitivities attached to rice in the international market, by allowing individuals to export rice not subject to SunRice's total supply chain control system, we risk causing irreversible damage to the value of Australian rice internationally. Taking into account that a majority of NSW rice is exported, this risk far outweighs the minor innovation benefits that may be obtained from the deregulation of the rice industry.

Other benefits of Rice Vesting

The Commission's report has failed to account for other benefits of Rice Vesting not directly related to the price premium.

One of those main benefits is the buyer of last resort provisions of the Sole and Exclusive Export Agreement, which obligates SunRice to purchase every last tonne of rice produced by NSW rice growers, at the variety specific price, provided it is of merchantable quality.

Conclusion

The RGA asserts that the Commission findings are both inconclusive and incorrect and for this reason the Commission is not in a position to make recommendation 11.1. In addition, the RGA reiterates that the Commission is not the appropriate jurisdiction to review the Rice Vesting arrangements, and that this is the responsibility of the NSW government.

The NSW government has found on a number of occasions to date that the benefits of Rice Vesting for the State do outweigh the costs and for this reason the Rice Vesting arrangement should be continued. Taking into account that the process implemented by the NSW government is much more robust and reliable than the process undertaken by the Commission, the RGA is inclined to rely upon the findings of the NSW government rather than the Commission.

Nevertheless, the RGA notes the following discrepancies and omissions in the Commission's report:

- That the cost of the RMB is fully funded by growers (not taxpayers);
- That the deregulated NSW domestic market is by far the most profitable market for NSW rice;
- That Rice Vesting and the resulting price premium has significant benefits for rural rice growing communities, in addition to the growers themselves;
- That fierce competition for irrigation water drives SunRice's cost efficiencies;
- That the small size and variability of the NSW Rice industry means economies of scale are critical to the storage, processing, transport and marketing of NSW rice;
- That significant investment in infrastructure is required to efficiently and effectively store, process and transport rice in comparison to other grain industries;
- That Rice is the world's most important basic food staple and therefore critical to the security of many nations. This means that there is significantly more distortion faced in the international rice market than any other agricultural commodity;
- The difference between long and medium grain rice markets;
- The level of commercial innovation that SunRice is delivering in all aspects of rice production, storage, processing, transport and marketing, and the confidence that Rice Vesting provides for in Rice Vesting in long-term research and development programs.
- The benefits of SunRice's total supply chain control system;
- SunRice's strategic approach to developing the status and value of its brands internationally, and the risks deregulation causes for the value of these brands; and

- The buyer of last resort provisions of the Sole and Exclusive Export Agreement.

Rice Vesting within the NSW rice industry is an extremely sensitive and complex issue, not least due to the consequences that the current arrangements may have on returns for growers.

Thank you again for the opportunity to submit to this draft report. If you require clarification about any of the matters raised in this submission, please contact the RGA's Policy Manager, Rachel Kelly.