

Queensland Sugar Limited
ABN 76 090 152 211
Level 14 348 Edward Street
Brisbane Queensland 4000
GPO Box 891 Brisbane
Queensland 4001 Australia

Telephone +61 7 3004 4400
Facsimile +61 7 4004 4497
info@qsl.com.au
www.qsl.com.au



Mr Paul Lindwall
Presiding Commissioner
Regulation of Agriculture Inquiry
Federal Productivity Commission

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Dear Mr Lindwall

Regulation of Agriculture Inquiry – Post-draft submission

Thank you for the opportunity to provide feedback on the Productivity Commission's draft report on the Regulation of Agriculture.

Introduction

Queensland Sugar Limited (QSL) is a not-for-profit company whose members comprise each of the Queensland mill owners and representatives of Queensland cane growers. We are currently the entity responsible for marketing to export customers, the majority of raw sugar produced in Queensland and operating the six bulk sugar terminals used for storage and handling of all raw sugar produced in Queensland.

QSL has a constitutional objective of promote the sugar industry in Queensland and maximise returns to members, and as such, seeks to ensure fair, transparent and competitive outcomes in respect to raw sugar marketing. That includes growers being able to freely choose for QSL to continue to market raw sugar on their behalf and millers being able to ensure a fair return on their investment.

Feedback on the draft report

QSL respectfully opposes the Commission's recommendation that sugar marketing legislation passed in December 2015 be repealed, on the basis that we believe such an action would effectively prevent competition for raw sugar marketing services for many Queensland growers and have a significantly detrimental effect on the industry we serve. Only in the circumstance where competitive sugar marketing arrangements, not reliant on legislation, are put in place in all sugar producing regions, could QSL support the repeal of the legislation.

We agree with the assertion on page 410 of the report that the competitive process drives efficiency improvements by encouraging the entry of new, or the expansion of existing, more efficient businesses, but that markets may not always result in efficient outcomes because of a lack of effective competition. We believe the Sugar Industry (Real Choice in Marketing) Amendment Act 2015 promotes such competition in raw sugar marketing in Queensland by enabling choice in what is a monopsony market for the majority of the sugar-producing regions of the state.

The importance of competition

Competition in raw sugar marketing has been in place for some time, so while the report's assertion that under the Raw Sugar Supply Agreements, millers supply 100 per cent of their raw sugar export

production to QSL (page 422) is correct with regard to logistics services, it is certainly not the case from a marketing perspective.

MSF Sugar left the QSL marketing system back in 2008 and subsequently commenced its own export marketing program while continuing to use QSL's logistics services.

In December 2013, Queensland's seven mill owners members entered into new Raw Sugar Supply Agreements with QSL, which provided those mills with the right to elect to market the proportion of the raw sugar they supply to QSL for which the mill retains the pricing exposure under the cane payment formula in their cane supply agreements with their growers (known as 'supplier economic interest sugar'). The option for a mill owner to market its supplier economic interest sugar has subsequently been exercised by Wilmar, MSF Sugar, Mackay Sugar, Tully Sugar and Isis.

QSL sells back to the supplier (or a related body corporate) a volume of raw sugar reflecting its supplier economic interest sugar, which they can then market themselves or on-sell again to others to market. The grower economic interest sugar has remained marketed by QSL, except in respect of some transitional arrangements for MSF Sugar, which were put in place when this miller returned to the QSL system in 2014.

As a result, there are currently a number of entities marketing raw sugar from Queensland, including:

- QSL;
- Wilmar (through marketing Wilmar's own supplier economic interest sugar);
- Alvean (a trading company that is a joint venture between Cargill and Brazilian Sugar producer that is doing so through marketing Mackay Sugar's supplier economic interest sugar);
- MSF Sugar (through marketing MSF's own supplier economic interest sugar); and
- China Foods (through marketing Tully Sugar's supplier economic interest sugar);
- Itochu (a Japanese sugar trader that is doing so through marketing Isis's supplier economic interest sugar)

Each of those entities competes with other international raw sugar traders, such as Bunge, Czarnikow, Alvean, Louis Dreyfus and Sucres et Denrées, for the sale of raw sugar into the global market.

QSL believes that the extension of Marketing Choice to growers at a 'retail' level is a natural progression of this marketing competition and the commercial evolution of the industry deregulation commenced in 2000.

Pricing and marketing performance

QSL welcomes the opportunity to address claims regarding performance, both with regard to marketing and pricing returns, as featured in the report.

It is important to note that while the Queensland Productivity Commission's (QPC) suggestion that millers will provide supplying cane growers with "comprehensive information" regarding premiums,

notionally allowing the comparison of the premium and cost performance from year to year, (page 420), such information is of no practical consequence if the cane grower has no alternate provider should they subsequently deem their current marketing provider's performance to be unsatisfactory. Unfortunately, the monopsony milling arrangements in place throughout much of Queensland's sugar producing areas mean that prior to the legislation, there was no alternate marketing service provider for the majority of Queensland growers beyond the current crushing season. This lack of choice and the need to foster competition lies at the heart of the Sugar Industry (Real Choice in Marketing) Amendment Act 2015 and the concept of Marketing Choice.

Claims that Millers can innately generate higher returns for growers through alternative marketing arrangements (page 422) have already been tested to some extent and found to be unsubstantiated. For example, Wilmar Sugar ran its own grower pricing pool for the first time in direct competition with QSL during the 2015 Season. Despite having unlimited pricing discretion as opposed to QSL's offerings, the Wilmar Sugar pool was outperformed by six of the seven QSL pools available during the period, with the Wilmar pool's final result equalling that of QSL's lowest-performing pool (the Harvest Pool), where the primary function is management of production risk rather than to maximise returns. Current performance of the Wilmar Sugar pool for the 2016 Season appears to again be lagging behind all of QSL's current pool offerings, however it must be noted that it is difficult to track Wilmar's pool performance due to a lack of public information or regular detailed reporting regarding the results achieved.

It is important to note that MSF Sugar has also run alternate pricing pools for its growers during recent years, and some of these have surpassed the results of QSL pools during this period, while QSL pools outperforming comparable MSF products on other occasions. Such results illustrate that the inherent superior performance of one marketer over another can never be guaranteed. A competitive market for such services – as underpinned by the new legislation – is the ultimate test of performance, determination of success and subsequent driver of wider innovation and industry efficiencies.

Price vs risk and its implications

While the price achieved and associated returns for sugar are always of high importance, it is not the only determining factor when considering a marketer's performance or offering. The repeal of the Sugar Industry (Real Choice in Marketing) Amendment Act 2015 and subsequent removal of a grower's choice and influence over grower economic interest sugar would effectively force that grower to accept the risk appetite of a single marketer.

Global agribusinesses are heavily exposed to trading risks and have very different appetites for risk compared to some family owned cane farms. Large multi-national agribusinesses typically have a strong balance sheet, access to debt funding, a portfolio of assets (which can be both geographically diverse and diversified across industries) and control of the level of dividend returns to shareholders, which allow them to handle volatility far more effectively than a typical grower (who has a much lesser ability to withstand adverse short term changes). Some of the key reasons growers are attracted to QSL's marketing approach include:

- through structures like limits on raw sugar which can be forward priced or sold without physical delivery, there is a more cautious approach taken to managing downside risks;
- through the RSSA providing some parameters around how QSL will market and price raw sugar and calculate the returns provided to mill owners (which can then be referred to in cane supply agreements), there is greater certainty and transparency for growers; and
- QSL does not have the conflict of interests that other international sugar traders do as a result of their non-Australian based trading businesses.

The early impacts of Marketing Choice

The suggestion on page 425 of the report that the new legislation would in some way inhibit investment or innovation in the Queensland sugar industry has not been borne out in practice. In fact, the opposite has occurred to date, with competition between Millers and QSL for the provision of marketing services to Queensland cane growers in the 2017 Season already leading to innovations in both grower pricing products and payment options.

Suggestions that the new legislation has also resulted in a complex redrafting process and inhibitive administrative burden (page 422) has not proven to be the case for QSL's current negotiations with MSF Sugar, where we have reached commercial terms on a Marketing Choice On-Supply Agreement (OSA) with minimal change to current arrangements. QSL's standard OSA Terms are detailed on our website and aim to deliver a smooth transition to Marketing Choice while leverage existing systems, maximising efficiencies and minimising costs. We believe further efficiencies could be secured by incorporating key OSA terms when defining and enabling a grower's right to Marketing Choice within their Cane Supply Agreement. This alignment between these important documents would certainly help to expedite current negotiations by providing a clear and fair contractual platform to deliver Marketing Choice as dictated by legislation, provided for by the CSA and ultimately delivered by the OSA.

Queensland cane growers and sugar millers are highly exposed to international competition every day and so to deny their access to competition for marketing services would seem at odds with the intent of the wider deregulation process. QSL firmly believes the repeal of the Sugar Industry (Real Choice in Marketing) Amendment Act 2015 would stifle this competitiveness within the marketing sector, to the detriment of Queensland cane growers and the wider industry.

QSL sincerely thanks you for taking the time to address this important sugar industry issue. Should you require clarification of the points raised above or any further information, please do not hesitate to contact QSL's Chief Executive Officer and Managing Director Greg Beashel.

Yours sincerely

Greg Beashel
Managing Director/Chief Executive Officer