Market mechanisms for recovering water in the Murray-Darling Basin

TANDOU LIMITED

Submission to Productivity Commission

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Abbreviations

CEWH	Commonwealth Environmental Water Holder
COAG	Council of Australian Governments
CPGs	Commonwealth Procurement Guidelines
DEWHA	Department of the Environment, Water, Heritage and the Arts
GL	gigalitre
LTCE	Long Term Cap Equivalent
MDBA	Murray-Darling Basin Authority
MDBC	Murray-Darling Basin Commission
NSWIC	New South Wales Irrigators Council
ML	megalitre
RTB	Restoring the Balance

Tandou Limited (Tandou) is pleased to present its submission to the Productivity Commission on market mechanisms for recovering water in the Murray-Darling Basin.

Introduction

Tandou is an ASX listed agribusiness with agricultural operations producing food and fibre, centred at Menindee in NSW. Tandou has over 30 GL of mixed security regulated water entitlements sourced from three rivers in the Murray Darling Basin.

Tandou's entitlements are largely located on the Lower Darling, a regulated supply from the Menindee Lakes storage scheme with additional entitlements located on the Murrumbidgee and NSW Murray.

Tandou is an advocate for an active and transparent water trading market which delivers water to its highest and best use including the environment. Due to our unique location in the basin and water portfolio structure Tandou was involved in some of the earliest intervalley water trades in the early nineties and understands the mechanisms involved.

Our volume of well located water, storage capacities and carry over provisions are a highly valued asset.

General Comments

Tandou believes that RTB is a necessary process however it could be better organised with more transparency and clarity with a detailed strategic purpose.

RTB has secured some well publicised, high profile entitlements but the remaining buy back funds should be utilised in a much more coordinated, focussed approach which clearly shows strategic purchases that can be linked to specific environmental needs and goals.

The combined effects of the buyback on the environment, irrigators and affected wider communities should be considered and analysed prior to establishing a purchasing strategy.

Responses to questions

1. *Is the focus on acquiring entitlements the best way of achieving the environment's needs?*

The Australian Government's RTB plan does not indicate or explain fully what the environmental needs are.

A healthier river should be a win/win for the environment and irrigators who remain in partnership.

Acquiring entitlements in isolation or without strategic focus is unlikely to be the best or only way to achieve the environment's needs.

The Basin plan due in 2011 and its enclosed "watering plan" should help to focus the requirements for purchases and infrastructure upgrades. These two tools must be used in a coordinated way to provide lasting value. For example it is not a value proposition to acquire 80% of entitlements located on a specific channel and also spend money on infrastructure upgrades. A coordinated approach here may see the nominal purchase price of this water seem high at face value in order to rationalise the infrastructure and maximise savings.

This example highlights the rationale for purchasing at real value not market value which is purely production priced. Real value can and should be justified to the community by explaining the purchases specific environmental use and or savings made by rationalising infrastructure and avoiding improvement costs.

2. *Is a 'no regrets' presumption a reasonable basis for purchasing entitlements, and at what point does this cease to be the case?*

Tandou's view is that a "no regrets" presumption is not a reasonable basis for purchasing entitlements. The purchasing programme should be focussed on the appropriate access to water to supply the identified environmental needs.

3. *What are the arguments for continuing the buyback after the new Basin Plan is implemented in 2011, and associated state water sharing plans start to be implemented in 2014?*

Continuation of buybacks from willing sellers beyond the implementation of the new Basin Plan will always be preferable to an approach that compulsorily acquires or reduces security levels of entitlement as a way of reaching the sustainable extraction limit.

Having said this we recognise that the buyback cannot continue forever and share the NSWIC concerns on how this scheme will be wound back.

4. *What implications do environmental demands across the Basin have on the targeting of purchases and the mechanisms and instruments that should ideally be used?*

Tandou strongly believes that specific environmental demands should be more closely linked to the targeting of each purchase or acquisition.

Key factors to consider for each purchase should be:

1. Location or proximity to environmental sites. Losses incurred in providing water to sites. The CSIRO sustainable rivers report suggests targeting stressed sites or systems.

2. Security of water in relative terms. For example LTCE and history of actual allocations are two methods of measuring this and demonstrates how general security on the Lower Darling is as reliable as other 'high reliability' products on many other systems and a superior product compared to all other general or low reliability entitlements elsewhere.

3. Deliverability - entitlements situated below storages whether schemes or on farm offer flexibility of supply and timing for proposed flows. Ability to carry over large volumes due to on farm storage also enhances these advantages and adds value to the entitlement. Therefore land and water packages should be considered in the right circumstances.

For these reasons and the previously mentioned need to rationalise some irrigation systems Tandou believes water properly targeted for buybacks should be priced for its ability to effectively deliver environmental outcomes, not the current market price which is a reflection of its current agricultural or industrial use and earning capacity.

It is assumed that there is a single market for water; however, since the introduction of 'buy back' arrangements for environmental needs the market has been distorted. Whilst there are clear and unambiguous pricing mechanisms for water used for agricultural or industrial use (primarily linked to the value of the end product) no such analysis applies for environmental water. In fact there are two distinct markets and to price environmental water using pricing signals for productive water does not value environmental water appropriately.

In many cases environmental water is required at different times of the year than water for

production. Therefore, its availability and deliverability to meet specific environmental objectives can be counter seasonal to productive water.

In the case of Lower Darling general security water has a much greater reliability than much of the high security water elsewhere in the MDB system. In addition Darling flows are countercyclical to flows from the Murray and Murrumbidgee and, together with the ability to store actual water in the Menindee system, its value to the meeting environmental, production and critical human needs is therefore much greater. This does not translate into higher prices as would be the case in a proper transparent market, as the clear attributes attached to counter seasonal water are not recognised by an average pricing mechanism across the system.

The reality is that the Commonwealth Water Holder is purchasing a significant quantity of entitlement without being able to deliver actual water. In the case of Lower Darling water entitlement there is a much greater ability to attach actual flow to entitlement than anywhere else in the MDB system.

Strategic purchases taking account of a wider range of pricing mechanisms would meet Commonwealth objectives in a more targeted approach. For transparency we believe a considerable amount of water could be acquired using open market trading platforms. This would help to provide the correct market signals.

Transactions for large and or unique parcels of water entitlements and the ability to properly assess environmental value of water will need to be developed and occur concurrently.

5. *How should environmental water be allocated across competing projects and sites?*

Tandou advocates that allocated environmental water must where possible attempt to mimic natural flow conditions, that is wet/dry cycles and flood events.

A solid base of well located "quality environmental water" (high security and "highest reliability" general security) should be acquired to provide the more common small to medium flow events and localised icon or high value site watering schemes while a combination of lower reliability and leased or on call (optioned) water could provide the top up water to simulate high flow events.

A lease/option strategy may be a more effective way to provide for this whilst also leaving water available for irrigators at other times.

6. *What impact has the Restoring the Balance program had on the price of water entitlements to date? What, if any, impact has this had on the market for seasonal allocations?*

Tandou believes the combination of drought induced low allocations and the RTB programme has lead to record high entitlement prices.

The RTB process has had minimal impact on seasonal allocations to date. Tandou does have concerns with possible future impacts on seasonal allocation markets. At the programmes conclusion the Federal and State Governments will collectively own a large parcel of water earmarked for the environment. The question remains: what will the Environmental Water Holder do with this water when all environmental needs are addressed naturally, i.e. in the wet years that will come again? Will the Environmental Water Holder feel obliged to realise some financial value from their investment via the allocation or temporary market? This has the potential to substantially alter these markets.

We are concerned that there appears to be no mechanism for dealing with all this water in high flow or wet years. The use of pre existing buy and leaseback and or option arrangements instead of a strategy focussed solely on acquisition of entitlements should be developed and communicated.

7. *DEWHA is now publishing average prices paid for entitlements. What impact is this likely to have on bids in subsequent tenders or one-off purchases?*

Specific transactions should be individually detailed to give timely transparency.

8. *What impact is the 4 per cent limit having on the market for water entitlements?*

Tandou opposes any artificial impediments to water trade. The 4 percent limit and the current NSW embargo on trade to the environment is affecting the market.

In the Lower Darling valley the imposed restrictions on trading out into the Murray must be amended to give flexibility and ability to provide water for highest value and best use including the environment by trading allocation water. Allocated water is granted fully assuming it can be delivered and must be allowed to be traded out of the system whilst ever the rivers physically are connected.

It is counterproductive to have a provision in the Murray Darling agreement that embargoes the trading of water from the Lower Darling – this legislative prohibition does not apply elsewhere in the MDB system. This prohibition limits trade and means high reliability Lower Darling water is not available to meet environmental, production or

critical human needs and distorts the trading and pricing mechanisms.

On September 15, 2009 the NSW Government announced a 25 percent general security allocation in the Lower Darling – this being the highest general security allocation anywhere in the Murray Connected Basin. However, the existence of the trading prohibition means this water may not go to its highest and best use within the basin.

9. *Is the Commonwealth–Victorian agreement on the 4 per cent limit a satisfactory way to allow a greater quantity of entitlements to be purchased in Victoria?*

No, refer to earlier discussion, these deals validate the restrictions to trade and should be removed entirely.

END OF SUBMISSION