

Submission to the Productivity Commission Inquiry into Export Wheat Marketing Arrangements

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Introduction

The Wheat Quality Objectives Group (the Group) was set up in 1993 to independently advise the Grains Research and Development Corporation (GRDC) and Australian wheat breeding programs on quality issues that affect the marketability of Australian wheat. All Group members are recognised experts in their fields, which include wheat quality, wheat breeding, wheat marketing, research and development, storage and handling, and flour milling and end-use technology in both the domestic and discriminating export markets. The Group has over 300 years of accumulated experience working in the Australian wheat industry.

The Group, through me as its Chairman, is currently providing Technical Support to the Wheat Classification Council. I am also a member of the Current Wheat Variety Classification Panel, as are other members of the Group, therefore the Group is well qualified to comment on a number of quality-related issues raised in the Commission's discussion paper.

The development and maintenance of a structured variety classification system coupled with the application of soundly-based grain receival standards have been the key factors that have underpinned Australia's strong position in the international wheat market, particularly in Asia and the Middle East. That position is now under threat as a result of the efforts of some of the newer marketers on the scene, who have failed to recognise the importance of specific wheat varieties in determining processing quality and suitability for end-use.

For those marketers who elect to have their wheat stored and shipped separately, or exported in bags or containers and therefore outside the control of the major bulk handling companies, currently there are no systems in place to control and protect the Australian "brand". The "brand" comprises the eight established export marketing categories:

- Australian Prime Hard (or APH);
- Australian Hard (or AH);
- Australian Premium White (or APW);
- Australian Standard White (or ASW);
- Australian Standard White Noodle (or ASWN);
- Australian Soft (or ASFT) and;
- Australian Durum (or ADR)

The Group will also comment on a number of key technical functions that have been successfully introduced for the betterment of the industry as a whole, and should be retained in the current deregulated environment.

These will be handled under the relevant headings in the Commission's Discussion Paper –

1 Accreditation of exporters

WEA was established under the Act to formulate and administer an accreditation scheme for bulk wheat exporters, to replace the arrangements that followed the removal of the AWB monopoly over wheat exports.

Why accredit bulk wheat exporters?

Section 3 of the Scheme states that its purpose is to establish a system of accreditation for companies to export bulk wheat, as evidence that they are 'fit and proper' to export wheat from Australia.

WQOG Comment: The Group believes that accreditation is a prerequisite in a deregulated export market in order to protect Australia's reputation as a reliable supplier of quality wheat. However, a shortcoming of the current accreditation criteria is there is no need for the applicant to have market knowledge or technical competence. Given the importance of wheat processing quality in meeting the needs of discriminating buyers, and the lengths to which reputable marketers must go in order to achieve this, this is a serious omission which needs to be addressed. If accreditation does not continue into the future, there needs to be some custodianship of quality in its broadest sense to ensure that the quality reputation of Australian wheat is not further eroded. As was stressed in the Group's submission to the Wheat Export Marketing Consultative Committee of February 2007, it is important that "any potential marketer of Australian wheat can demonstrate an adequate knowledge of the critical quality factors that exist in the market place".

Is there an ongoing role for accreditation of some form or is it needed only for a transitional period?

WQOG comment: An ongoing accreditation process will be essential in order to protect Australia's reputation as a reliable supplier of wheat that is consistent in quality and ideally suited to many of the popular food products consumed in our key markets in Asia and the Middle East.

Is it appropriate that bulk wheat exporters be subject to an accreditation process when those in industries such as the following are not:

- *non-bulk exports of wheat and other grains*
- *domestically traded wheat and other grain*

WQOG comment: On quality grounds alone, one could argue that there is an equal need for accreditation of non-bulk wheat exporters and domestic suppliers, given the damage that can be done to Australia's "brand" image by the supply of poor quality grain that fails to meet customer's expectations.

That said the domestic market is in a somewhat better situation in that buyers can deal directly with the grower, seller or grain handler and ensure that their precise needs are accommodated.

In the absence of accreditation, would regulation of other aspects of bulk wheat exporting still be required? If so, which aspects?

Is there anything particular about the wheat industry that requires additional regulations that other grains and commodities are not subject to?

WQOG comment: Contrary to popular opinion, wheat is not a commodity. It is a highly differentiated product that through the expert classification of varieties into one of the major categories (see above), and the separate segregation and handling of grades throughout the bulk handling system, Australia has been able to establish an enviable reputation as a reliable supplier of quality wheat.

Criteria and conditions

In addition to the existing eligibility criteria, the Group strongly recommends that a prospective exporter should also be required to demonstrate a level of market knowledge and technical expertise. This would ensure that marketers/traders operating outside the traditional bulk grain handling/marketing chain do not, unwittingly, jeopardise Australia's hard-won reputation by supplying grain that might otherwise meet physical grain receival standards (such as protein, screenings or test weight), but because of the absence of any form of controls on varietal composition, fail to meet millers' and food manufacturers' processing expectations. Feedback from the market place is also important to the industry and it is essential that exporters have a good understanding of the influence of wheat quality on products and processes, to negotiate higher prices for better quality, and to ask the right questions on quality to assist in market development.

Role and funding of WEA

The role of WEA is to regulate exporters of bulk wheat from Australia by managing the accreditation scheme. Preliminary discussions with stakeholders suggest a wide range of views about the ongoing role for WEA, with some suggesting it be abolished and others suggesting its role should be expanded.

WEA is funded through the Wheat Export Charge (WEC) and accreditation fees.

The WEC is currently set at \$0.22 per tonne, and is levied on all wheat exports (both bulk and non-bulk). The expectation is that WEA will be fully funded by the wheat industry (DAFF 2009a).

Is there any ongoing role for WEA? If so, what should the nature of that role be and how should ongoing functions be funded?

WQOG comment: As will be outlined later under "Industry good functions" many of these functions would benefit from being centrally run by a Peak Industry Body, and one approach that has been proposed is that the WEA could be restructured to become such a body. Funding could be via an increase in the current levy of \$0.22 per tonne, some additional

Government contributions as is the case in Australia's major competitors, the US and Canada, or by a combination of these.

Are the current funding arrangements for WEA appropriate and sustainable?

WQOG comment: Yes, wheat farmers have a long history of being prepared to support essential industry functions, and a modest increase in the levy would be sufficient to support those generic functions previously undertaken by AWB Limited, which are now largely in limbo due to a lack of funding and coordination.

Can Australia learn from the approach that other countries take?

WQOG comment: Absolutely. In the US and Canada, a combination of grower and government support ensures that the respective wheat industries of these leading wheat exporters are able to conduct targeted, coordinated and well supported market development and promotional programs. Previously Australia had similarly well organised and conducted programs, but since deregulation many tasks have become uncoordinated and lacking in funding.

That said the Wheat Classification Council (WCC) has started to address some issues but only has a life span until June 2010. The concept of WCC as an industry coordinator has merit, similar to the activities of the Australian Oilseeds Federation and Barley Australia, but very much depends on industry players participating, and addressing the issue of funding.

In consideration of international models the funding of US Wheat Associates needs to be clearly understood. The major financier of US Wheat Associate, based on recent annual reports, is the US government. Through the USDA the government has funded 73% of the US Wheat Associates annual budget US\$15.4 million for the last few years.

5 Wheat classification and market segmentation

Prior to deregulation, AWB was responsible for wheat classification, and established all wheat classes. Wheat classification activities are currently conducted according to the principles described in the Wheat Classification Guidelines. After deregulation, the Wheat Classification Council (WCC) was established by the Grains Research and Development Corporation to provide structure and market direction for wheat breeding, classification and research activities in Australia. It has until June 2010 to develop a model for the future operation of wheat classification in Australia, and oversee current classification operations, including a review of the Wheat Classification Guidelines.

Is the WCC adequate for ensuring wheat quality and the usefulness of wheat classifications?

WQOG Comment: The basic structure and mode of operation of the WCC is workable, and its composition with representation from the main stakeholders, breeders, marketers,

exporters and domestic end-users, ensures that the key issues are on the table for debate. However, the task of making variety classification decisions is a highly technical process and in order to operate effectively the Council needs strong input from those with the required level of expertise. Currently the WQOG through its Chairman, provides advice and technical support, but given the nature of the decisions to be taken, the Group would prefer to have formal representation on the Council.

There is also a need for the members of the Variety Classification Panel (VCP), who are the individuals who actually undertake the classification process, to be part of the decision making process. This could be readily achieved by a consolidation of the WCC and the VCP, with the Panel members contributing to the Council's deliberations, and meeting separately to undertake the assessment of new lines submitted for classification.

Could the market deal with these issues without such a body?

WQOG Comment: No, given the highly competitive nature of most aspects of the deregulated wheat market, it is difficult to see a ready means by which the various stakeholders could independently achieve workable solutions to the numerous and often highly technical issues that underpin the production, segregation and marketing of Australian wheat.

Grain Trade Australia (GTA) develops wheat receival standards. It takes information from the Wheat Classification Guidelines and aligns them to GTA's set of consistent receival standards used in contracts. Wheat is sampled and tested at storage facilities, and co-mingled with other wheat varieties within the specifications for a particular wheat standard. As a result, the quality characteristics of an individual farmer's wheat are no longer discernable when it is co-mingled. Blending decisions are made by the storage facility operators in accordance with the supply of grain in the region, and demand from exporters or end users for classes of wheat. In some cases, more narrowly defined segregation of varieties can occur where there is sufficient demand from a buyer to justify a non-standard class of wheat.

WQOG Comment: The opening lines of this paragraph are a little misleading. GTA has taken the receival standards previously developed by AWB Limited and reviews them annually, refining them in light of seasonal and market conditions. These standards govern all the physical aspects of the grain such as grain density, protein and moisture content and the presence or otherwise of various grain contaminants that can be readily measured at receival. However, the key to the grain receival process is the segregation of deliveries according to variety into one of the broad marketing categories (described above). This is achieved via the Variety Master List that reflects the decisions of the Variety Classification Panel for every production or port zone. The finished products that are ultimately marketed are mixtures of varieties with quality characteristics that collectively guarantee the suitability of the grain for particular markets and specific end-uses, and provide the necessary consistency in quality from season to season.

Does the market differentiate adequately between qualities of grain? Is the

current level of co-mingling activity appropriate?

WQOG Comment: Yes, provided the receival standards and variety master list are applied correctly, however circumstances can dictate that grades of wheat must be commingled at receival. Once that has occurred, owners of that stock cannot be confident that they will receive grain of a similar quality as that which was delivered.

Is there adequate scope for marketing of particular types of wheat to service niche markets that are more narrowly specified than GTA standards?

WQOG comment: Yes, buyers can either negotiate a specific set of requirements with one of the major bulk handling companies, or can accumulate grain privately and market it in bags or containers to satisfy particular niche markets.

Does exporting through containers and bags provide a satisfactory way to exploit non-standard marketing opportunities?

WQOG comment: Yes, figures recently released by the Australian Bureau of Statistics show that over 2.2 million tonnes of wheat has been shipped in bags and containers in the 11 months to September 2009. Much of this was shipped to traditional markets for Australian wheat including Vietnam, Indonesia and Malaysia, suggesting that a number of new opportunities have been explored.

Are growers able to extract an adequate value for the quality of their wheat?

WQOG comment: This has been the most disappointing feature of the market that has developed post-deregulation. In the absence of a single desk marketer to control the supply of grain onto the international market, the market has seen competing marketers bid prices down to unforeseen levels, with Australian wheat being traded at a discount to its traditional competitors, and at prices comparable to those exporters whose wheat is of lower quality. This is particularly so in importing markets controlled by government, or institutional tendering – those conducting the tender looking for the lowest price. Hopefully this is a short-term phenomenon, as it has the potential to undermine the traditional quality/price relationships that have previously applied, and are essential for many wheat farmers to remain viable.

Wheat is again tested upon transportation out of the facility and at port to ensure that it meets the minimum contract specifications.

In addition, customers usually require exporters to provide independent samples from shipments before they leave Australia. The Australian Quarantine Inspection Service also provides export inspection and certification services to ensure that there is minimal risk from insects, pests and noxious weeds (DAFF 2009b).

GTA has drafted a grain industry Code of Conduct to cover both bulk and container trade to facilitate quality control across the industry.

Can quality control be left to market-driven forces, with commercial incentives

placing a check on the quality delivered to overseas buyers?

WQOG comment: Not from an holistic Australian perspective. Inadequate knowledge of quality requirements of markets can lead to a focus on price at the expense of quality and substitution of inferior or inappropriate categories of wheat. In the long term this could lead to Australian wheat being down-valued in the international market.

Has deregulation affected the reputation of Australian export wheat?

WQOG comment: Unfortunately yes. Presentations by buyers at the recent Australian Grains Industry Conference held in Melbourne clearly demonstrated their concerns about the developing trends post-deregulation, Speakers highlighted

- Larger price fluctuations,
- Large quality fluctuation especially for container shipments,
- Less reliability of supply,
- Lack of stock through the end of the crop year,
- Little or no information on crop quality, and No technical support.

One of the few positive comments was that prices were cheaper due to competition for the business, and the preparedness of smaller sellers to take a reduced margin – All bad news for Australian wheat farmers.

Is quality control more of an issue for container wheat exports than it is for bulk wheat exports?

WQOG comment: Quality control is important for both bulk and containerised wheat. As previously noted, some 2.2 million tonnes of wheat, or around 16% of the total wheat exports from Australia in the 11 months to September 2009, was shipped in containers, and it is essential that this wheat be subjected to the same levels of quality control as bulk wheat.

Is quality control an issue in the domestic market?

WQOG Comment: No, as mentioned previously, the domestic market is in a somewhat better situation in that buyers can deal directly with the grower, seller or grain handler and ensure that their precise needs are accommodated.

6 ‘Industry good’ functions

‘Industry good’ functions can be defined as services to the industry that support trade and industry development. Many of these functions were previously carried out by the single desk operator.

There has been debate in the past as to what constitutes an industry good function (WIEG 2008). On the one hand, they can be considered legitimate development

functions affecting the entire industry (having public good characteristics). On the other hand, they can be considered as purely commercial activities carried out to maintain strong customer relationships for individual firms. This distinction was blurred under the single desk arrangement because one firm represented the entire bulk wheat export industry.

Industry good functions can include the following (WIEG 2008):

- industry strategic planning
- research and development
- wheat variety classification
- wheat receival standards
- information provision
- crop shaping activities
- technical market support
- wheat promotion
- branding
- trade advocacy
- regulatory advocacy.

Some of these functions have been discussed separately above, including classification, standards and information provision.

Does the list above represent legitimate ‘industry good’ functions?

WQOG comment: In some cases yes, although obviously some, like crop shaping, and technical market support are commercial issues to be conducted by individual marketers, and others like industry strategic planning is the responsibility of the wheat industry itself.

How should ‘industry good’ functions be defined?

WQOG comment: Vital, on-going activities needed for long-term industry improvement. Functions that can be most effectively and efficiently conducted in a coordinated, pre-competitive, centralised, manner to deliver a positive outcome for the wheat industry as a whole and the economy of the Nation.

Are there currently gaps in the provision of ‘industry good’ functions? If so, can these be left to the market to provide? Or is government involvement required? If so, how should these be funded?

WQOG comment: Yes, the most obvious being wheat variety classification as it is a cornerstone of the Australian export wheat industry and a solution must be found to continue the current arrangements, or another similar version, beyond 2010. Other considerations are needed around generic market promotion, market development, the branding of the product and the protection of that “brand”.

Is there scope to use other grains or other agricultural industries as case studies for how 'industry good' functions could be delivered for wheat?

WQOG comment: Yes. Barley Australia and the Australian Oilseeds Federation are worthy examples that warrant close evaluation, however as always, funding will be the major challenge.

Is there potential for synergies in shared provision of 'industry good' functions across industries?

WQOG comment: Unlikely. Wheat is a specialised and highly differentiated product that requires specialist knowledge and facilities in order to demonstrate its capabilities. Its closest relative, barley, is used primarily for malting and stock-feed purposes, thus requiring a totally different set of skills and milling/malting/feeding facilities.

Is there anything to learn from the way that other countries deal with the provision of industry good functions in the wheat industry? Or other industries?

WQOG comment: Yes, as mentioned previously market promotion and market development activities are being carried out most effectively in both the US and Canada by joint industry and government funded programs to the overall benefit of the wheat industries in both competing countries. This work includes the training of customer technical staff in how to best exploit US/Canadian grain, industry orientation visits for the executives of key customers etc. Importantly, the government in both countries funds a majority proportion of these activities.