SUBMISSION TO THE PRODUCTIVITY COMMISSION

REVIEW OF WHEAT EXPORT MARKETING

Submitted by: Helen Newell

Title: Director, Strategy & External Relations, Asciano

Date: Thursday, 3 June 2010

Asciano Submission to the Productivity Commission

Review of Wheat Export Marketing

1. Background

Asciano is a major operator in Australian transport markets through Pacific National, Australia's largest private sector rail operator, and Patrick stevedoring operations.

Through its Pacific National business, Asciano supplies bulk export grain rail haulage services in SE Australia, primarily though contracts with the major grain storage and handling organisations and domestic bulk grain rail haulage services to millers and other users of grain, such as Manildra. Through its Patrick business, Asciano supplies containerised export grain rail haulage services into Port Botany in NSW.

Previously Asciano had operated the Victorian rail network under lease from the Victorian Government, and therefore has experience in the grain business on rail both "above" and "below/integrated" rail.

Asciano has had the opportunity to participate in a number of reviews of grain rail infrastructure in New South Wales including the Grain Infrastructure Advisory Committee and the NSW Grain Freight Review.

This submission will focus on the rail related aspects of the Commission's Draft Report.

2. Improving the Efficiency of the Grain Rail Network

The Commission's draft Report proposes that the efficiency of the grain only network could be improved by de-regulating these assets, and allowing for the restoration of a vertically integrated rail and track operation.

Asciano agrees that improved management structures for the NSW grain network are needed, but does not consider that the changes proposed by the Commission would deliver the benefits expected.

Such changes could also act as a barrier to competition in the up-country storage and rail line haul markets.

A number of factors result in this situation:

a) Road: Rail Cost Recovery

The principle vehicles used in the road carriage of grain over extended distances are B doubles and where allowed, road trains.

The NTC in its third determination on road user charges assessed that the charges for heavy vehicles of this type did not recover their average costs of road infrastructure maintenance, and put in place a programme to increase registration charges for these vehicles. That programme was agreed by the ATC in February 2009.

The NTC noted that “The Productivity Commission independently audited and endorsed NTC’s charges methodology noting that it is “conservative” by international standards (i.e. resulting in lower charges).”[1]

The under-recovery on road grain haulage is exacerbated by the need for these vehicles often to use lower standard rural roads which incur higher rates of damage from heavy vehicles than is the case on better constructed routes, and by the exclusion of the costs of externalities.

A key assumption of the Productivity Commission’s analysis that grain road haulage is fully recovering its costs and rail should therefore be able to do the same is therefore placed in doubt.

Until a fully efficient market for grain haulage services involving full recovery of all costs on road is in place, Government support for rail network maintenance will be required if there is a desire by government to have competitive neutrality between modes, recognising the safety and congestion at port benefits of rail.

A similar view was reached by the NSW Grain Freight Review which commented “it is far from clear that a full “user pays” approach would produce the desired result”[2]

Today, greater than 90% of export grain is transported to port by rail in NSW. Grain producers (through prices paid for their product) do not pay the majority of road or rail costs required to maintain the branch line tracks and regional roads at current levels. The rail government subsidy has been provided in the form of very low access charges by RIC to rail operators (and thus passed on to handlers / growers). If a privately owned company (such as grain handler) was to be required to earn a commercial rate of return on the track, as well as other assets they controlled in the supply chain, prices would have to increase significantly. Unless road access charges were also increased to reflect full cost recovery, this would likely drive significant volumes of grain to road from rail.

This resulting modal shift would further decrease the viability of keeping the rail tracks

3

[1] NTC Website 21.4.10

[2] NSW Grain Freight Review 2009 Page 40

open, and therefore probably result in significant line closures. This dramatic and sustained increase in truck movements would then necessitate additional expense by government in the form of greater road construction and maintenance, as well as result in additional social costs of safety and congestion at port, particularly in a bumper harvest year.

b) Alignment of Risk with control

The Commission refers in the paper to the changed arrangements for “above rail” where the efficiency of these operations has been greatly improved by introduction of “take or pay” arrangements. These largely transfer the risk of inefficient scheduling and demand variability to the grain storage and handling organisations who are the parties best able to manage this risk.

Since the establishment of take or pay arrangements between GrainCorp and Pacific National, utilisation of the asset base used on the main line network (e.g. between Werris Creek and Newcastle) has more than doubled. By aligning the interests of the handlers, loaders, rail operators and port operators through commercial arrangements which favour maximising throughput of the entire chain, decisions have been made by all parties that have resulted in increased asset utilisation and therefore lower unit costs. These changes have included opening hours at the port, upgrading of loading equipment, better staging of trains for unloading at port up country ,e.g. using the larger storage capacity at Werris Creek to stage trains for efficient movement and loading at Port of Newcastle.

A comparable transfer of risk is required for the “below” infrastructure. Currently Government funds the road and rail network maintenance without any assurance that the investment and pricing strategies of the grain handlers, and rainfall, will actually result in use of that element of the network for grain haulage. While this is easier to determine, and therefore potentially manage contractually with rail track owners, it is true for both road and rail networks. Further, if financial obligations are imposed on below rail infrastructure owners only, it will again likely drive risk averse parties to favour road, with no obligation for assurance.

c) Vertical Integration with rail operators

Vertical integration of track and rail operations, for the reasons which led to operations being on a “take or pay “ basis, does not transfer the risks for ineffective use of rail maintenance expenditure, since network usage is determined in large part by the grain storage and handling organisations, and not by rail operators.

d) Vertical Integration with Storage and Handling Companies

Alignment of risk with control requires a greater involvement and commitment by those responsible for determining grain flows with the investment needed for this to occur on road or rail.

To achieve this through de-regulated vertical integration however raises major issues particularly if Government is a significant provider of funding.

As multiple storage and handling entities are involved, the structure of such vertical integration appears complex.

Accountability for Government funding and the setting of the social goals justifying that funding would be dubious, and could act to prevent the very purpose of vertical integration of increasing economic efficiency e.g. keeping lines open which have limited economic benefit.

While rail remains the predominant mode of transport to Port for export grain, deregulated control of the rail network by one handler would create a significant barrier to entry for other market participants planning to enter the grain storage market on that part of the network.

3. Implications for management of the Grain Rail Network

Pacific National considers having regard to the above that:

a) Government subsidy of rail maintenance for the grain networks will continue to be required until full cost recovery including externalities is in place for road, if the government wants to have competitive neutrality between modes, recognising the safety and congestion at port benefits of rail.

b) Grain storage and handlers have through their investment and pricing strategies significant influence over the storage location and modal choice for on-delivery from that site. They therefore should be fully engaged with the Government over investment in network maintenance, and potentially carry part of the usage risk on that investment as long as it does not distort the competitive balance and drive volumes to road with no equivalent risk burden.

c) Vertical integration of track management with rail operations is an ineffective way to create that engagement, while competition concerns make vertical integration with grain handlers an inappropriate model.

4. Contacts:

Helen Newell
Director, Strategy & External Relations
Asciano
P: 02 8484 8115
E: helen_newell@asciano.com.au

David Attlee
General Manager, Infrastructure Strategy
Asciano
P: 02 8484 8060
E: david_attlee@asciano.com.au