MARKETING AUSTRALIA'S CROP: THE WAY AHEAD

Timothy J Ryan

INTRODUCTION

It is 9 years almost to the day that I presented a paper on Wheat Marketing (Ryan (1964)) here to this very conference at the University of Sydney. Quite a deal has happened over these intervening 9 years. The 1989 Wheat Marketing Act (WMA) changed irrevocably the framework within which the AWB operates by deregulating the domestic market and establishing the Wheat Industry Fund (WIF).

The international market place has seen

- the incessant rise in production within the European Community (EC) and its inexorable spillover into rising exports,
- the build-up in grain stocks within the US and the introduction in May 1985 of the Export Enhancement Program (EEP) ostensibly to bring the EC to the bargaining table, but more in reality to clear stocks,
- the resultant price wars between the US & EC in 1986 mitigated by a Northern Hemisphere drought in 1988 and resumed in 1990,
- the break up of the Former Soviet Union (FSU) and the collapse of Eastern Europe, the consequences of which are still to be fully revealed,
- the near conclusion of the GATT Uruguay round of trade negotiations in 1992,
- the increasing development of the economies of the Asian countries with a corresponding growth in demand for grain for food (wheat) and also for feeding to livestock.

Observing these changes the Grains Council of Australia (GCA) convened a seminar entitled Grains 2000 in September 1991 (See GCA (1991-92)) to assess the challenges ahead and to plan for the future.

* A paper prepared for the 37th Annual Conference of the Australian Agricultural Economics Society, Sydney, 9 - 11th Feb 1993. Despite being Senior Manager Corporate Affairs, Australian Wheat Board (AWB) the views expressed herein are my own and not necessarily those of the AWB.

1 The People's Republic of China (PRC) appears poised to increase grain demand over the next several years and is making efforts to liberalize grain trading patterns (See Garnaut & Ho, (1992))
What I propose to do in this presentation is to discuss some of the major changes which occurred in the 1989 WMA, some of the changes which have occurred since Grains 2000 and to try and place these into perspective within the world wheat marketing environment. I will then challenge you as Economists to think through the type of marketing structure which may best position Australia to carry the grain industry into the 21st Century.

I do not intend to provide you with an historical overview of the various Wheat Marketing Acts nor of a detailed description of the AWB. A number of articles such as Miller & White (1980), Longworth & Knopke (1982), Myers et al (1985), various IAC & ABARE (or BAEC (1983)) reports which are well known to you already provide that information. Also (Whitwell & Sydenham (1991)) provide an excellent up to date history of the Australian Wheat Industry.

1989 WHEAT MARKETING ACT

The 1989 WMA was the culmination of the Commonwealth Government’s policies for the Grains Industry interacting with the political realities of the day. Possible directions had been canvassed by Miller (1984) and in general in the White Paper on Statutory Marketing Authorities (DPIE (1986)). It was a move away from regulation towards more open policies and a move for SMA’s to become more commercially responsible and responsive.

The change, introduced irrevocably altered the marketing environment for grain in Australia. The three major changes were

1) the deregulation of the domestic market for wheat.
2) the introduction of the Wheat Industry Fund
and 3) the explicit objective for the AWB to trade wheat and other grains in order to provide growers with a choice of marketing options.

Other important changes were made. These included a move from a Guaranteed Minimum Price (GMP) applicable to growers on a per tonne basis to a Government underwriting on AWB borrowings. The level of underwriting was to decline over time and was put in place only to June 30th 1994. The maximization of net farm returns to producers is emphasized with the consequent obligation for the AWB to minimize transport, handling and storage costs and port and shipping costs wherever possible. The AWB was freed to have more than one receiver of grain in a State. There is an obligation to pass costs back to the individual producers wherever possible rather than having those costs pooled. The WMA changed the Board composition from one of a Board which consisted mainly of growers to one comprised of people with particular commercial expertise including production expertise. The WMA also removed the sunset provision on the life of the AWB.

2 The Davis report (1991) further adds to the current philosophy on SMA’s although the recommendation (Annual General meetings, policy councils) have not been fully implemented for the Grains Industry.

3 The significance of this alteration became apparent in Nov 1990 when world wheat prices collapsed and AWB pool return estimates and hence harvest payments to growers followed down the world prices. The underwriting did not provide a floor in the way the GMP did.
WHEAT INDUSTRY FUND

The deregulation of the domestic market and the exclusion of the Government underwriting from funds used for trading activities necessitated the establishment of a capital base for the AWB. In the past the AWB, unlike other marketing organisations or Bulk Handling Authorities (BHA's), had not been permitted to build up capital reserves of any significance. All proceeds from a pool, net of costs were returned to growers. The trading activities required a capital base and the WIF levy was set at 2 per cent of the farm gate value of all wheat sales. The Wheat Industry Fund (WIF) is unique among the reserves held by grower organisations in the sense that growers have certificates of equity issued each year and these certificates are transferable. The WIF is managed in accordance with regulations which were drawn up after consultations between the GCA and the AWB. Included in those regulations is the requirement for an annual WIF business plan to be approved by the GCA. The WIF monies may be used for any sound commercial investment subject to GCA approval although until now it has been used essentially for funding the AWB's trading activities. Separate accounts are kept for the use of WIF monies and each equity holder receives an annual financial statement.

Because of the need to keep trading activities and its funding arrangements separate from the pool, a Trading Division was established within the AWB. The Trading Division acts as an agent for the pool on the domestic market and for Papua New Guinea and New Zealand and is responsible for all cash grain trading and pooling of grains other than wheat. Domestic customers and suppliers of the AWB therefore see one face of the AWB, but the range of services may ultimately be provided by different Divisions within the AWB and be separately accounted and audited as pool or trading activities. At present all profits from the Trading Division activities go back into the WIF.

The WIF has been used for two investments so far. (Its' primary purpose whilst being built up was to fund the Trading activities.) One investment involved buying shares in a firm in Western Australia (Moora). The other involved a joint venture project with companies controlled by the Kuoks (a prominent Asian business group and major customer of the AWB) and by Caroll Food, the PRC grain importing (and exporting) organisation. That project is a feed and flour mill in Schenzhen in Southern China and is a highly strategic investment given the rapid developments occurring there.

POST 1989 DEVELOPMENTS

Grains 2000

The Wheat Industry had resisted the deregulation of the domestic market. Deregulation had been supported by a number of growers favourably located in relation to domestic markets. Some if not many of these growers believed that they could appropriate in a deregulated environment the monopoly rents achieved by the AWB under the regulated regime. Many were subsequently disappointed as prices were competed down to estimated pool return levels in many areas. Growers who are favourably located may be better off under a

4 The drought in the Eastern States in 1991/92 did see the domestic market move significantly away from export parity as it took on a life of its own driven by local supply and demand factors
deregulated system, but the size of that benefit is much smaller than many initially believed. Furthermore some of growers now see the AWB, in its Trading Division guise as a competitor to themselves and at times agitate for the AWB to keep away from their cash markets.

Change had occurred with the 1989 Act and fundamental change at that. The GCA responded by calling for a seminar on the challenges facing the grain industry. Grains 2000 was initiated. With funding provided by the Grains Research and Development Corporation, the GCA commissioned Hassall and Associates to prepare a set of background research papers (see Hassall and Associates (1991)). The 3 day seminar offered a plethora of speakers. The proceedings may best be summed up by Don McGauchie (1992):

‘Almost without exception speakers at the Grains 2000 conference advocated that critical changes to our research, development and extension, production, processing, marketing and the industry’s institutional arrangements are inevitable and necessary.’

Following Grains 2000 a joint GCA/AWB/DPIE Working Party was established to investigate a possible corporate, legal and financial structure for a successor to the the AWB. The Minister for Primary Industries and Energy, Simon Crean was also keen to have suggestions from the Industry and was keen to pursue value adding aspects in future arrangements. The Working Party report (1992) was presented to the Industry at Grains Week in Melbourne for consideration and discussion. The report suggested a framework codenamed NEWCO.

**NEWCO**

NEWCO would be established under its own Act of Parliament as a private corporation. It would be owned and controlled by grain growers through a broad and diverse base of shareholders. NEWCO would be free to utilize capital from outside the grains industry through joint ventures and if approved by grower shareholders by issuing shares to non-grower minorities. NEWCO would replace the AWB and WIF continuing the AWB’s activities with potential to expand into grains processing and grain related manufacturing industries. On the presuppositions that the current pooling and harvest payment arrangements would continue to be offered by NEWCO, approximately $400 - $500m of shareholders funds would be required to become financially independent of the Commonwealth Government.

WIF monies, if supported by the Industry, could be converted to issued shares in NEWCO (the WIF levy could cease on establishment of NEWCO). The shares would have the rights attached to them usually accorded in other large Australian companies, e.g. voting, dividends and capital growth potential. The Board of NEWCO would be accountable to the shareholders and would comprise of a majority of growers together with independent and executive directors and a director appointed by the Commonwealth. NEWCO would seek to retain the single export status of the AWB.

Meetings were held across the Australian wheat belt in July 1992 to discuss the proposal. Ultimately the NEWCO proposition was not accepted by growers. The reasons varied. Some growers felt there was no need to change, others were concerned about the investment dangers and about possible competition...
between Newco and their own local State board marketing entities. Others felt that a change in Government at the forthcoming Federal election would solve any difficulties such as declining levels of Government underwriting or the possible cessation of underwriting. Some felt that a company holding an export monopoly was unlikely to be a viable structure if the Coalition won the election and that the proposed structure may increase the likelihood of losing that single desk facility.

The GCA took note of the Industry concerns. They believed if a satisfactory outcome could be achieved with the Labor Government it made sense to conclude an arrangement rather than place all expectations on a particular election outcome. A driving factor also was the need to have in place the financial arrangements, which were due to expire on 30th June 1994 for the AWB as soon as possible. The AWB funding activities go out some 15 months or so ahead for some facilities and the financial institutions needed to be provided with a firm indication in early 1993 of the likely arrangements. The GCA negotiated an arrangement which culminated in amendments to the WMA (1989) in late 1992.

1992 AMENDMENTS TO WMA

In October 1992 amendments to the WMA (1992) were presented to Parliament. The key elements of the amendments included a specific object of the Board to participate in value added activities and the power to do so. These are deemed to be activities which increase the value of grain or grain products. The amendments included an extension of the underwriting of AWB borrowings until June 30th 1999 combined with a level set at 85% (compared with 82.5% previously set for 93/94) and a continuation of the WIF levy to accumulate funds until June 1999 to provide a capital base for the AWB and for investment in value adding activities.

A subsidiary company may be formed for investment purposes. The WIF funds may be used for investment in commercially sound projects, for equity in joint ventures and for funding the Trading Division's activities. The WIF uses will continue to be in accordance with a business plan approved annually by the GCA and any profits from the activities will be credited to WIF equity holders on a pro-rata basis. At the end of the capital build up period, the Government intends to withdraw its underwriting of the AWB borrowings. By then the capital base should be sufficient for the AWB to operate without the Government facility. The Government also has the view that the AWB may be corporatised at that time.

The Government decided to maintain the single export desk status of the AWB, although the export powers may be reviewed if and when there is a clearer outcome of the GATT round and as any successful reforms become effective.

In summary then, the amendments envisage an AWB which has the objectives of

1) maximising net returns to farmers from the marketing of pool wheat

ii) of providing marketing options for wheat and other grains and

5 See the Second Reading Speech (1992) by Minister Crean for further elaboration
III) of providing returns from value adding activities into the WIF.

It will have a sufficient capital base to enable it to invest in value adding activities and may be corporatized after mid 1999 by which time the Government underwriting facilities will have ceased. The AWB may start to look a little like its competitors, Cargill, Louis Dreyfus, Continental, Conagra, Bunge, and the other grain trading houses it encounters in the international arena (and also domestically in some instances).

How does this structure fit into the international grain marketing scene and from an economic perspective how does this structure assist or impede resource allocation and the generation of national income and the income of producers?

To consider these questions properly it is necessary to provide a brief description of the international grain market, particularly wheat, because wheat is by far the major grain in Australia. Also a brief description of the activities of the AWB is required.

INTERNATIONAL WHEAT MARKET

Highly concentrated

The world grain market is dominated by a few major countries on the supply side. There are a larger number on the demand side, but the market is still reasonably concentrated. In coarse grains, corn is the predominant grain traded and the export side is dominated by the US (80%) and the import side by Japan (30%) and the FSU (15%). In the wheat market 5 countries, the US (35%), Canada (25%), EC (20%), Australia (10%), and Argentina (5%) account for over 90 per cent of exports (around 100m tonnes each year). On the importing side a much larger number of countries are involved. The FSU and the PRC account for nearly one third of imports although they vary considerably from one year to the next. The 12 major importers account for approximately two thirds of imports and most of these countries buy through a single desk.

Government intervention in wheat production and trade is endemic. The EC operates a high internal price system protected by a variable tariff and disposes of its surpluses onto the international market through a system of export subsidies (restitutions). The US has long had a farm programme in place which provides target prices, deficiency payments, loan rates, storage programmes, area set aside programmes and the well known EEP. Canada has had stabilization schemes, special payment schemes (approx $1 billion each) which have operated for periods of time and the current Gross Revenue Insurance Plan (GRIP) scheme. Canada also has a single desk, the Canadian Wheat Board (CWB). Australia has virtually no Government involvement, but the AWB has single desk status on the export market. Argentina used to have a Grain Board, along with export taxes, but now is an open market.

Oligopolistic Marketplaces

Economists have long postulated that the international wheat market was not a perfectly competitive, price clearing market (see McCralla (1966), Alouze et al (1978)). Some empirical support for an oligopolistic market structure is provided for in Kolstad & Burriss (1986) in which a US - Canada duopoly model performed somewhat better than a US - Canada - Australia triopoly model. Paarlberg & Abbott (1986) combined consideration of market power in international wheat trade with the endogenous treatment of domestic policies and concluded that US, Japanese and EC policies were insensitive to other nations' policies, but that Canadian and Australian policies were sensitive to policies elsewhere. Ahmad-Esfahani & Carter (1987) also note the dominance of the US in wheat trade and how the loan rate may be used to affect the position of other exporters. These results are hardly surprising to people familiar with the trade. These studies were undertaken prior to the EEP introduction in 1985. A more recent study, Anania et al (1992) demonstrates the influence of EEP as well as concluding that EEP is basically a failure in meeting any of its stated criteria.

Targetted Subsidy Programmes

Even the most cursory of casual empiricism suggests that in matters of price determination and trade flows, the USDA in Washington and the European Commission in Brussels play pivotal roles. The export subsidy programs operated by Washington and Brussels are targeted programmes. The level of subsidies vary quite considerably from country to country so that the decision makers have a great deal of flexibility and control over the quantity and prices which a country needs to pay for wheat imports. A country, for example, such as Japan which is a non-targeted EEP country (Japan does not import EC wheat) is faced with the non-subsidised or US commercial wheat price as its world price. Countries such as Egypt, the FSU and the PRC may face prices up to US$60 per tonne lower than the commercial US price with other targetted countries falling in between. Countries which are not targetted for EEP and/or which do not import EC wheat but which are potentially eligible will also face a price below the US commercial price.

As a result of these export subsidie programs there is no single world price for wheat of a particular grade. Rather there is a whole schedule of prices depending on which country one wishes to consider. Add this to the varying premia, discounts for different types and qualities of wheat and for varying locations and there is a whole complex of prices facing any given importer. Wheat from one country or one type is not an homogeneous commodity, there are differing degrees of substitution for technical as well as preferential reasons.

The Grain Traders

In this mix of administratively and market determined prices and traded quantities we have the international grain traders operating. Morgan (1979) provided probably one of the first insights into the way in which this small and highly concentrated group operate. Essentially 5 or 6 almost all privately owned companies dominated the world grain trade. Caves (1977-78) provides a very interesting economic analysis as to why an industry which is highly competitive (in the US) has such a presence of large traders and high concentration in export sales. He concluded that the large scale nature of these firms seemed to result from scale economies in co-ordinating information.
and risk. He also noted that profit margins in large traders depended on the instances of disturbances that create opportunities for a good deal of non-routine arbitrage. In other words, when events are happening quickly, grain trading firms are in a position to capitalise on their strengths. The profits have little to do with price levels, with which producers particularly are concerned, only margins.

Gilmore (1982) in a very comprehensive piece of work provides an even more detailed description of the large grain traders and their activities. Gilmore provides insight into the ways in which these large companies which all have affiliates in key areas around the world position themselves from an international perspective, not a national one to maximise profit. He describes how they not only take advantage of opportunities but create opportunities for themselves through inter company transfers across borders and hence administrations, through striving to gain every advantage from the various farm grain programmes and administrative procedures and through the use of optional origin contracts as well as in many other ways. Gilmore (1982, p29) notes the vast amounts of money or capital required to fund a large and diverse trading company.

THE AWB

I wish to make a few points about the AWB and its activities and I will confine my remarks to addressing issues which may be of concern to economists. These relate to getting the appropriate price signals back to producers, the ways of providing the marketing and ancillary services and the opportunities for innovation and developing new markets or new market niches. I also will comment on the likely role of WIF investments and their place in enhancing the marketing function. More detailed descriptions of the AWB activities and various statistical series are available in the AWB Annual Report (various issues) and in Whitwell and Sydenham (1991). A number of these activities and some of the economic arguments in favour of a single desk seller were advanced in Ryan (1984) and even allowing for changed legislative arrangements and circumstances are still valid. The AWB financing, hedging (risk management) activities have developed in line with the increased sophistication of these facilities. The economies of scale identified by Caves (1977-78) continue to flow to the AWB from information and from logistics. The ability to accumulate grain Australia wide and to programme shipments from all ports with minimal search and co-ordination costs is one of the major advantages for the AWB.

Australian Wheat Characteristics and Markets

I need to briefly state some facts about Australian wheat before going further. Australian wheat has a reputation for being clean and very dry (see US Congress Office of Technology Assessment (1989 p.109)). This reputation is in contrast to the reputation of US wheat, which has been the subject of infestation and high levels of admixture and continual buyer discontent. Australian wheat is a white wheat, and its protein level is generally 9-11%

/ The US hygiene and inspection system was plagued with scandals in the 1970's with substandard shipments, ghost ships, and falsification of documents. In 1976 (Gilmore 1982, p124) reports that 16 US firms including all the major companies (except Cargill) and 146 individuals were indicted under the Grain Standards Act of 1960, resulting in a total of $1 million in fines, 31 years of incarceration and 111 years of probation for various offenses.
Although it has been declining, virtually all other wheat produced is red grained (red wheat) although some 7 million tonnes of Western White (WW) is produced in the Pacific North West (PNW) region of the US. A comparable grade in a technical sense with Australian Standard White (ASW) is the US Hard Red Winter (HRW) ordinary and its average protein level may routinely be 12% or more. The AWB card price (daily asking price) for ASW wheat is very closely related to the HRW ord price at the PNW. Australian wheat markets range around the Pacific and Pacific Rim through S.E. Asia and up into the Middle East as would be expected given freight differentials from other suppliers. Many of the buyers have a preference for Australian white wheat. The US and Canada are the main competitors of the AWB with the EC in some markets along with occasional forays from Argentina, Saudi Arabia, Turkey and other disruptive fringe marketers. The markets in S.E. Asia and Japan are very quality conscious and noodle demand is increasing in those countries. The bulk buyers, Egypt, FSU, PRC, Iran etc. are less discriminating and are more concerned with price and in some instances credit availability, although quality standards still are important.

**Price Signals: Pools & Cash**

As economists we are concerned that producers receive proper and valid price signals. As explained earlier the international market is subject to discretionary government intervention and it exhibits a large amount of price variability over and above seasonal movements and other market determined differentials within any given marketing period.

The AWB's major pricing mechanism to producers is through pooling. The estimated pool return rates are no longer guaranteed minimum prices and if prices fall then growers returns will decline. The AWB pays a proportion, normally 85% of the estimated return at harvest time with a post harvest payment in the following March. Further payments are made if and as funds become available, generally determined by the returns from credit sales. Under pooling, returns for the same class of wheat (Prime Hard, Hard, ASW, General Purpose, Feed) are pooled over time and over markets. Within these classes, various grades may exist. For example PH14, PH13, Victorian Hard, Noodle Wheats etc., are binned separately and will provide different returns to the suppliers. Normally if a segregation can be made which will return a differential amount, then that segregation is made. This includes regional pools and pools for particular types of off-grade wheat, for example PH varieties or H3, H4, H5 etc. In the 1991-92 season some 44 different segregations were made. Overlying these differentials are payments for protein in 0.1% intervals (over set ranges) and any dockages which might be applicable.

On the cost side specific deductions are made for freight and handling, for port cost differentials and for any other costs incurred which can be reasonably attributed to individual growers. Some silos are located close to end users and therefore a domestic path rebate may apply (fobbing costs are not incurred) or a reduced storage fee is applicable or even a direct farm pick-up or delivery direct to end users storage may be arranged and costed accordingly.

The AWB therefore has a comprehensive pool pricing system and one which I suggest provides meaningful market signals clear of much of the noise associated with spot prices to growers. After all production is an annual decision. Pooling also is a useful risk management tool for producers.
The AWB offers cash prices to growers and forward contracts in a number of instances. It offers fixed price/fixed grade contracts and forward contracts of a multi-grade nature which may be for a fixed price (with fixed discounts/premiums for grades) or a minimum price that is an option type contract. These are offered from sowing time onwards.

**AWB Export Pricing**

One of the major advantages of the AWB’s single desk status is its ability to price discriminate on the international market. Because of the targeted nature of the various subsidy programmes, there is no one world price. The AWB is able to sell the same wheat on any single day at whatever prices the various markets will bear. For example the Japanese market is a non-targetted market and is our highest returning market. If Australia were like Argentina and sold through the trade we would not be able to capture those rents because competition between sellers would drive the price down. All buyers would pay the prevailing Australian fob price as occurs for the Argentinians irrespective of destination, freight or any other advantage that Australian wheat might have for that buyer. That of course, is the market working. Australia, however a Voon & Edwards (1992) point out is likely to be uninterested in these circumstances in the welfare of consumers in other countries.

**MARKET SEGMENTATION AND DYNAMIC CONSIDERATIONS**

**Product Differentiation and Customer Relations**

Other factors also assist in differentiating the product from other origin wheats and therefore in the ability to price discriminate. As ACIL (1992, p.55) point out product differentiation is a very important aspect of successful market segmentation. The AWB differentiates its product by emphasizing the attributes of Australian wheat, it’s clean, it’s dry, and it’s white, by ensuring that customers receive the type of wheat best suited to their needs, (e.g. noodle varieties, wheat varieties from particular regions etc) by service, by promotion and market development.9

The AWB places a high degree of emphasis on customer relationships, on understanding what the customer requires, in undertaking research, market development and training courses for customers both on-shore and off-shore. As Wilson and Preszler (1992, p.557) point out wheat buyers cannot observe all the relevant quality characteristics prior to purchase. A sellers’ reputation depends on past performance and generates repeat business, which they point out reflects concepts embodied in the economics of quality and reputation as set out by Shapiro (1983). Grain traders will also be concerned with relationships, but that relationship is more likely to be transaction based

---

8 See Rae (1978), Martin & Zwart (1987), and ACIL (1992, p 53ff) for discussions on the theoretical and practical opportunities to gain from market segmentation

9 Whitwell & Sydenham (1992, Chapter 13) provide a good overview of developments in the quality area, including noodle market development and the rapid dough method for bread making which is ideally suited to Australian wheat and acts as a barrier to entry to other wheat suppliers
and the emphasis will be on their firm, not on Australian wheat or wheat products. As discussed later, the attention of the traders of US wheat to relationships is at times questionable.

The AWB is vitally concerned with marketing Australian wheat, not simply wheat from whatever origin will give the highest return to the trading company. The trading companies books are controlled out of the US or Europe and the emphasis is on company position and company profit, not on a particular country's product. This represents a considerable divergence in objectives between the grain traders and organisations such as the AWB or the CWB and I believe has relevance when examining marketing from a national rather than a world perspective.

The reason why emphasis is placed on these factors is to differentiate Australian wheat in the eyes of the buyer. Even the fact the wheat is from a non-US origin, from a small country in world political terms or the AWB being regarded as Government agency all helps to get market access and to get a price. As mentioned earlier, if a single seller of Australian wheat did not exist, all buyers would be able to purchase at the same FOB price irrespective of how much value they placed on the differentiated product providing supply exceeded their demand.

**Dynamic Relationships and Growth**

Recent developments in the literature on what determines optimal structure places a great deal of emphasis on competition and rivalry in stimulating innovation and maximising efficiency. The emphasis in Porter (1990) is on domestic rivalry, but surely rivalry on the export market is as important in some circumstances. The domestic market in wheat is small in comparison to the export market. The pressures for innovation, for development, for smarter ways of marketing will come from the highly competitive, international market place in the form of methods and products which are suited to the end users in different countries. There the conditions for contestability are fulfilled.

The AWB is operating in a highly competitive (albeit distorted) international market place with a product which potentially is highly substitutable. If the AWB's product and services are not acceptable or it is not able to differentiate the product then it will lose market share or it will suffer reduced prices compared with other origin wheats. There will be a consequent flow on effect back to national and to farmers incomes. Alternatively if the AWB is able to promote Australian wheat, to form better and stronger relationships with customers in a more efficient way than alternative marketing arrangements then the gains over time may be quite substantial. It may be instructive to consider how the activities are undertaken in the US to gain some possible insight into how Australia might fare under an altered system.

**US Development Activities**

The marketing promotion and development work in the US system is undertaken by US Wheat Associates. US Wheat Associates is funded by growers and by the US Department of Agriculture and is a separate entity from the grain trading

---

10. See ACIL (1992, p 36 & also Appendix 2) for a particularly good summary of the various models and the salient points arising from the literature. Also see Porter (1980).
firms who do the marketing. The grain firms themselves do not undertake market promotion and development because there is no way that they can cover the costs involved or expropriate the benefits. There is a gulf between the firms who market the US grain and the people who take responsibility for quality control and for market development. The buyers are often frustrated about the quality of US grain shipments. Gilmore (1982, p124) describes in alarming detail (for US producers) the problems that buyers face and the lack of attention to their complaints. Whilst there has been considerable improvement in this area, the concerns of lack of consistency and uniformity in wheat from the United States is an ongoing concern of buyers as noted in Wilson and Preszler (1992, p656) and from my own personal experience. The US Wheat Associates are often frustrated by the inefficiencies which result from them having responsibility for promoting the product, developing the markets, but not having control over the supply of that product.

**Australian Experience**

A small supplier such as Australia does not have the luxury of not taking notice of customer's requirements and of any complaints. We have the considerable advantage of being able to service the customer with AWB people. Any problems can and are dealt with immediately. Our technical people can and do work closely with the end users to identify market opportunities which our marketing people then address and co-ordinate research work, for example noodle research.

South Korea provides a case in point. The Government essentially controlled the imports prior to 1984 and the milling wheat requirements were satisfied by Western White (WW) out of the Pacific North West of the US. The AWB became involved in that market by selling feedwheat into it in 1984. The import restrictions were in the process of being relaxed and the AWB technical people began following up the market opening that we had established with the various mills. One of the major uses of milling wheat in Sth Korea is for noodles. Research projects into the needs of the noodle whats were undertaken and continual representations were made to the mills. Feedwheat sales continued spasmodically (depending on the availability) and small sales of milling wheat were commenced about 5 years ago. In the 1991-92 year we have built those up to 450,000t representing 20% of the milling market and we are very confident of continuing to make inroads. The AWB is pleased with the results because Sth Korea is a non EEP market and hence is one of the few high returning markets available. The AWB met the full might of the US system, traders, US Wheat Associates etc. head on and we appear to be beating them. The US Wheat Associates response is to put pressure on the USDA to grant Sth Korea EEP so they can regain their market.

I'd suggest that a properly managed organisation promoting a particular country's wheat and maintaining a close business relationship with many buyers is in a stronger position to identify innovations and get those innovations implemented in a more cost efficient manner than may be achieved under the US model.
SINGLE DESK SELLING : BENEFITS AND EFFICIENCY CONCERNS

What is the likely size of the benefits from the single desk seller status and from product differentiation? The question is a very difficult one to answer partly because data are not readily available and partly because it is very difficult to construct a model to capture the effects, particularly the dynamic and competitiveness effects.

Benefits : Large or Small?

Miller (1991, p.5) states that the AWB has probably extracted higher average prices in world markets than otherwise obtainable, but he feels at the cost of much lower levels of product differentiation and value-adding activities. A study by the International Policy Council on Agriculture and Trade (forthcoming, p.154) also concludes that the CWB and AWB gain price advantages as single desk sellers. The Industry’s Commission (1991, p.48) continue to doubt the ability of Australian marketing authorities to extract consumer surpluses from overseas buyers. Piggot (1992, p.130) recently concluded that returns from market power to a single desk Australian wheat seller were likely to be empirically small. I feel however that his conclusions are not valid because I’d suggest that his model assumptions are not appropriate. I would suggest that when you have a market structure in which price differentials of up to $US60 per tonne may apply there is plenty of scope for price discrimination and for capturing higher returns before turning to other methods of market segregation.

Some internal analysis within the AWB indicates that the benefits from price discrimination vary from one year to the next, as the targeted subsidy levels vary. The average benefits may be of the order of around $20 per tonne or over $210 million per year. These estimates were obtained by going through export markets over a 4 year period, (1987/88 - 1990/91), making a number of simplifying and conservative assumptions and then calculating the difference between AWB returns for various markets and subsidised EC/US prices at the time of sale. A $US5 per tonne discount was made to allow for a premium for any intrinsic qualities of Australian wheat which may exist irrespective of marketing arrangements. These are crude estimates and I stress that, but they are not implausible and may indicate the order of magnitude of the benefits.

Quotas and Pricing Efficiency

ACIL (1992, Chapter 6) does not believe marketing authorities, at least in the New Zealand circumstances are necessary to capture benefits on the export market. ACIL suggests that quotas or licences could be issued and auctioned instead as does Piggot (1992, p.132). The administration of licensing arrangements and auctions are not without cost. Anecdotal experience within the Horticultural Industry indicates all sorts of problems may arise with holding tenders for export licences. These include collusion, uncertainty regarding the number of licences, the frequency of issue etc.. Also how and to whom are these rents returned? Import licences however are a tioned in a number of countries and it would be possible to devise a system. I’d suggest one needs to question how efficient such a system would be in capturing the economic rents available in the international wheat market. The market is dynamic, highly variable, subject to arbitrary Government actions and hence the size and sources of the rents will vary considerably. The current system has one very experienced licence holder who can capture the rents and pass all benefits obtained back to Australian producers. There is no leakage. The
alternatives would appear to be administratively cumbersome and at the very least would not return all benefits to growers and possibly not even to Australian interests.

Another price concern most recently articulated by ACIL (1992, p.xiv) in relation to some New Zealand marketing arrangements centres on a divergence between producer returns and the market return for the marginal unit of output. It's a classic Catch 22 situation where if you're successful at raising returns through capturing rents, you distort resource allocation by averaging prices to producers. This could be of concern depending on supply elasticities for particular grades of wheat although in recent years nature has thwarted planned output, but needs to be watched. Keeping in mind the risky nature of grain production and the likely divergence between private and social attitudes to risk, individuals may require a higher expected, less variable pool price to plan the socially desirable output in any case.

A Judgement

In the final judgement one has to weigh up all the benefits and compare them with any costs the particular marketing system imposes. I'd suggest that people can intuitively identify with market segmentation when targetted subsidies are being widely practiced. This is a plus for a single desk seller arrangement. The other areas of product differentiation and growth (market development and promotion) are more intensely debated and are of particular interest given the focus on what conditions provide a sustainable competitive advantage.

I'd suggest that the model I've outlined here of a properly managed integrated marketer is a strong and a useful model for Australia given the structure of the world grain market.

THE WAY AHEAD

I've provided a description of the amendments to the WMA (1989) which will shape the structure of the AWB into the future. It is a structure which will permit the continuation of the single desk marketing of wheat and its attendant advantages. The arrangements will provide a capital base for the AWB's activities which ultimately will result in the AWB being financially independent of Government. The AWB will continue its product differentiation and market development and in the process provide new and enhanced markets and improved pricing options for grain growers. The value adding activities are currently being assessed and will involve joint venture projects with others. The Schenzhan investment may typify the types of strategic investments which will be undertaken both offshore and onshore. Other sorts of projects may involve consultancies similar to the storage and handling projects currently underway or under discussion in Iran and PRC. The projects may involve activity within the farm gate to better assist farmers in producing the grain. These projects are intended to yield a return in themselves and also to place the AWB in a strong position to market our main product, wheat and other grains by creating strategic opportunities or alliances. Possibly Miller's (1991) view of the AWB may be fairly close to reality by the year 2000, although the single desk status may still be in place.
The structure of the WIF removes a major concern which the ACIL (1992) report on NZ marketing arrangements raised. ACIL were concerned with the effects on resource allocation of pooling off farm investment returns with the price of the product, particularly in the case of the NZ Dairy farmers. Under WIF the investment returns are credited to individual certificate holders rather than being returned to producers through higher product prices.

Interestingly the ACIL (1992, p xxxiv) recommendation to corporatize all the NZ statutory marketing businesses, issue shares to producers and allow shares to be traded freely, may be close to being fulfilled for the AWB in 1999. The Government, as I discussed earlier, has mooted corporatization of the AWB and WIF equity certificates are currently tradeable although a market has not yet been established.

The next few years offer a lot of challenges and opportunities. It is critically important that we have a marketing structure which will permit Australia to take advantage of those opportunities.
REFERENCES


AWB (various years), Annual Report, Melbourne.


Garnaut, R. and Ma, G. (1992), Grain in China East Asia Analytical Unit, Department of Foreign Affairs and Trade, Australia Government Publishing Service.


International Policy Council on Agriculture and Trade (Forthcoming), State Trading in International Agricultural Markets: International Dimension and Select Cases, Washington D.C.


Morgan, Dan (1979), The Merchants of Grain, Viking, New York.


