Agricultural Competitiveness White Paper – Submission IP171
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SUBMISSION

to

AGRICULTURAL COMPETITIVENESS TASKFORCE

DEPARTMENT OF THE PRIME MINISTER AND CABINET

in response to the

AGRICULTURAL COMPETITIVENESS

ISSUES PAPER

"The farmer is the only man in our economy who buys everything at retail, sells everything at wholesale, and pays the freight both ways" *John Fitzgerald Kennedy*

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[redacted]

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Background

This submission is prepared as personal response to the issues paper. Select issues and questions from the issues paper have been addressed in line with primary areas of interest. It is deliberately not referenced. It is intended to provoke deeper thought on the issues raised and provide an honest and unencumbered perspective from the production end of the supply chain.

There is one underlying principle that guides much of this submission. Simply, we borrow what we have today from the future. Agriculture is still the most fundamentally important industry in any civilisation if considered perpetually. The provision of food to the population is a perpetual issue and it is essential that applying a policy timeframe does not distort the perpetual importance of maintaining the productive capacity of our agricultural sector.

In this context, potentially the biggest impediment to Australian agricultural competitiveness is attitudinal. It is impossible to develop or implement necessary policy reform if the ideology that underpins these reforms is wrong.

This attitudinal issue is the stumbling block for meaningful dialogue at many levels both within production sector as well as the decision makers beyond the farm gate. Typically the heat that is generated is borne of ideological belief systems particularly in relation to “dry” economic rationalism versus a “wet” protectionism.

The reality is that the solutions for Australian agriculture are going to be borne out of pragmatism and a deep understanding of why agriculture is important to Australia and of where Australia really sits in the global agricultural trade, regardless of aspiration.

The problem is not as simple as either argument, fundamentally because the business of agriculture is not a business like any other. The current debate about drought support belies a much bigger conundrum in Australian agricultural policy and Australian trade policy that goes to the core of the issue around farmer resilience that is borne out of global expectations on the provision of food, fibre and energy.

Globally we see divergence on balancing agricultural supply excess with farm viability. Some countries argue agriculture is not a business at all because it is a social imperative. Often these countries have a social or cultural “memory” of starvation or at least devastation of their agricultural capacity. On this basis they justify massive public money support to their farmers and in so doing massively distort world agricultural trade.

On the other hand we have Australian agricultural policy based on the notion that agriculture is a business like any other. As a result Australia has pushed, largely unsuccessfully, to rid the world of agricultural subsidies to try and achieve a global agricultural market free of impediment and subsidy. The Australian trade agenda is deemed unsuccessful because every so called Free Trade Agreement (FTA) Australia has negotiated has seen agricultural trade offs that have resulted in the retention of significant distortion and/or restriction against Australian agricultural products. Even the most recent FTA with South Korea saw key Australian commodities excluded. In every negotiation the Australian Government has ultimately been forced to trade off agricultural access to the benefit of the broader economy.

The reality is that agriculture is not a just a business, it is also social imperative. No amount of economic rationalisation has moved, or will move, the rest of the world on this issue.

It is a telling consideration that the chant of the crowd in the 2011 Egyptian uprising was “Bread, freedom and social justice!” It was a bread shortage that was the ultimate catalyst for revolution. As old as the Romans it has been known that the provision of basic needs is the key to stable government and the social and political importance of the food business is evident long before people starve. Unfortunately, as civil unrest escalates, often the provision of food can be further disrupted and political issues escalate to full blown humanitarian disasters and ultimately militant conflicts.

Simply, people need to be fed. Globally, including in Australia, society assumes people have a right to food.

In 2013 the Australian Government launched a National Food Plan that declared it is a Government imperative to ensure all people have access to safe affordable food.

The problem in Australia is that society, through Government, seems to think it is solely the role of the farmer to feed the world. At the same time, society, through government, impinges on Australian farmers through regulation and direct intervention that severely diminishes their collective competitiveness. The reality is that the primary role of the farmer is to feed his or her own family. If society wants agriculture to sustain the global population now and into the future it needs to ensure that there is enough reward in that pursuit for farmers to feed their families, in good times and bad.

The current drought discussion in Australia is important because it highlights the fundamental lack of economic and emotional resilience in the sector that exposes it so profoundly to disruptions in production by weather and disruptions in markets.

The challenge, it would seem, is that the Australian indicators of rising farm debt, declining terms of trade and dwindling farmer numbers allude to agriculture not being a particularly viable business, particularly if it is debt funded. This begs an important question, if the Government is committed to the provision of safe affordable food for all, shouldn’t it also be affordable for those who produce it?

There is a lot of discussion about improving agricultural productivity to meet the global food challenge. Australia is out of step with the rest of the world in terms of commitment to support food producers in the face of global price expectations that do not provide for farm viability. The outcome is that Australian producers have been forced to carry this financial burden. The impact of Australia’s aberrant attitude to the importance of maintaining productive capacity and retaining the human capital in agriculture is now manifest, as farm businesses fail due to a lack of economic resilience in the current drought.

Australia is relatively underpopulated with a perceived abundance of natural resources including arable land and water. Our near neighbours are comparatively overpopulated with significant shortages of necessary natural resources. Our national security will increasingly depend on our reputation as a fully utilised, efficient and reliable agricultural supplier that is recognised as being too valuable to disrupt.

Current Agricultural policy and societal expectation, as reflected through Government, is out of step with the needs of today’s agriculturists and increasingly out of step with the needs of those who depend on our produce.

In any business model the decision to invest must incorporate a risk reward assessment. Typically, low risk investment can be justified on relatively low returns. Conversely, higher risk ventures require higher returns to justify the same investment. Australian agriculture has gradually been wound into a high risk low reward category that belies the value of the sector to society. The market, in part through intervention by other countries, has failed to accommodate the shift in the risk profile of Australian agriculture.

It is the role of government to intervene where markets fail and the Australian Government must derisk agriculture to ensure adequate Australian investment occurs in the sector and to attract and retain the kind of entrepreneurial capacity that is essential for a sustainable future.

Agriculture is not a business like any other and the social value of the enterprise must be properly evaluated in terms of eco services, trade and geopolitical stability. Even the most rudimentary, and more essentially, honest evaluation demonstrates the value of Australian agriculture to the average taxpayer appears grossly underestimated and there is a sound case for increased financial support of the sector.

Ensuring food security in Australia and globally

Food security is a timeless issue. The issue is never resolved truly because we continually consume food and we cannot see far enough into the future to be completely confident that we have enough resource and capacity to supply our needs on an ongoing basis. The context of the issues paper appears to muddy the water in this issue by assuming that what have today is what we will have in the future.

In reality, agriculture is not currently sustainable either within Australian production systems or globally. This presents a serious issue for today's policy makers in regards making assessments and provisions for food security.

That said, it is essential that regional food security be a key objective for today's policy makers for a range of reasons, National Security not least. The current regional political stability is fragile in the context that population growth in Asia, and particularly our near neighbours, will see increasingly prevalent incidences of food insecurity. Hungry people are unlikely to respect or abide by any orderly rule of law. The result of food insecurity will be political instability and a new wave of human migration that simply will not be stopped diplomatically or politically.

Arguably Australia currently produces enough food for approximately sixty million people. Our exportable surplus cannot feed the likely demand. Perceptions of our food security in the face of food insecurity for our neighbours will be a pressure point for public opinion. Australia's track record at being considerate of social and moral norms in other countries, specifically in relation to live animal exports, has already aggravated consumers and created prejudice.

Much economic growth is built on the provision of cheaper food in real terms. In Australia food cost has fallen from 50% of income to nearly 10% in recent decades. This has in effect liberated 40% of income for other discretionary spending and this is the key to establishing and maintaining tertiary industries. If developed economies allow supply and demand to drive food prices in times of shortage, the result will kill their economies as that 40% of income is redeployed in essentials and tertiary industries fail.

It is convenient to ignore the long term impacts of declining agricultural productivity if you have surpluses. It is easy to allow markets to drive price when there are surpluses to keep food cheap. However, the payoff that is promised price upside to agriculture in supply side economics, if Government's allow them at all, will be short lived.

Beyond the indirect ramifications of declining food security, the production challenges are profound. If we try to drive productivity too hard we will in effect exhaust our productive capacity faster,s failing to achieve a sustainable farming system. If we are too conservative in production targets, in pursuit of sustainability, we risk aggravated political destabilisation of the region.

Either scenario undermines the lazy assertion that a rising middle class in Asia will be the saviour of Australian agriculture.

It is important to note that anecdotal evidence suggests that migrating to larger corporate farming systems does not increase gross production or overall sustainability and potentially undermines both aspirations. This indicates that the maintenance of the family farming unit may be essential to the future of Australian agricultural competitiveness. Care should be taken in the assessment of what agricultural demographic best meets the long term demands of agriculture.

- What opportunities exist to expand agricultural production in Australia and how can we take advantage of them?

  There are vast tracts of agricultural land that are as yet underdeveloped. They are not all in northern Australia. Therefore it is essential that 'low hanging fruit' like increasing production intensity in already developed, but underutilised, land is fully exploited before embarking on green field projects.
  It is clear that state and federal restrictions on land development are severely constraining productivity gains even in areas with existing infrastructure and relative environmental safety for further development.
  Extension of geographical regions of intensive agriculture will require significant infrastructure investments, but similarly further intensification in developed regions requires greater reliability and extension of existing infrastructure.
  It is essential that the underlying viability of the sector is addressed in order to foster expansion of the sector.
  Finally it is essential that the unmeasurable value of perpetual production from agricultural land be considered in the assessment of invasive extractive industry encroachment on productive agricultural land.

- How can farm businesses, food manufacturers and the retail sector be more responsive to domestic and global food demand and better integrate into domestic and global supply chains?

  Farm businesses and every other business in the supply chain respond to financial pressures. Unfortunately the farm business is often less able to adapt quickly as they are constrained by production cycles and often generational timeframes in business structures.
  The challenge is that farmers are overwhelmingly small business operators and they are not consummate entrepreneurs, by and large they are good technicians. This is not unique to agriculture, for example a small plumbing business is often run by a plumber, not a sophisticated business manager.
  Typically people are farmers because they are competent producers. There is an absurd assertions that they are somehow incompetent if they are unable to compete at a business level with multinationals in the global food market. I am unaware of any other small business sector

that is expected to be responsive to so many externalities and it is unreasonable to assume this of farmers.

There has been good success with branded products for some producers and typically there is a degree of vertical integration, but this model simply can't work for 127 000 businesses without some form of collectivism.

It is essential that Australia maintain domestic capacity in secondary industries to bridge the gap between production expertise and the rest of the supply chain. In recognising that many farm businesses cannot simply build capacity outside of their existing expertise due to a range of constraints, time mostly, we need to ensure the capacity exists in the supply chain in a way that is complimentary.

Farmer decisions for improving farm gate returns

It is evident that farm gate returns have not increased in line with costs and farm debt is increasing, regardless of where you may sit on the distribution curve of profitability or productivity in the sector. There is a real decline in profitability of the sector and in turn viability is increasingly difficult. The trend data is irrefutable and demands acknowledgement.

The government solution to declining terms of trade has been to encourage improvement in productivity, through increased intensity and or through increased scale. This strategy has been successful to some degree in mitigating the declining terms of trade in the short term. However, the rising cost of inputs and tendency to implement farming systems to meet short term financial pressure which ultimately mine soil nutrients is now slowly undoing the perceived the success of this strategy. As the input cost rises, coupled with the realisation that the efficiency gains have not accounted appropriately for non-cash costs, particularly in the context of the long term productive capacity of the soil, this strategy is doomed to fail.

It is intriguing that this phenomenon of ignoring non cash costs exists also in non-food sectors. For example, people talk about supply of oil as if it were renewable. Technically fossil fuels are renewable, but the rate of production of fossil fuels is measured in millions of years, so our collective extraction is not sustainable. The price people pay and are prepared to pay for oil products does not factor in the fact that it took about 250 million years to make it. We pay for what it costs to extract, refine and distribute oil with a relatively small margin. Because there a relatively few "producers", they can control supply within reason and manage to extract a healthy margin. Increasingly though, there is political instability resulting from concerns around oil supply and exploitation.

Agriculture is remarkably similar in terms of the pricing framework and its implication for sustainability and utilisation of natural resources, albeit with relatively shorter timeframes. However, there are currently too many producers of food and the market is only as strong as the weakest seller so there is little opportunity to limit supply to improve price. However, there is also increasing political concern about agricultural supply.

Additionally governments foster oversupply to ensure excess production. Food is deemed more important than other sectors, as reflected on Maslow's hierarchy of needs. Food is subject to more willing market manipulation to oversupply than to drive up price through undersupply. The result is that producers have little to no influence over price, as opposed to oil.

There is only one way to improve farm gate returns sustainably. The unit value of the product must increase more the unit cost of the product. Logically then there are two levers to pull, one is to increase value of production and the other is to reduce cost of production.

It is important that there is a distinction between increasing gross production and increasing unit value of production, which is where previous Government policy seems to have failed.

The rest of the world and indeed consumers in Australia are reluctant to pay more for food and by the time real supply shortages occur the market is unlikely to be allowed to operate to sustainably drive up prices due to government intervention on humanitarian grounds.

The opportunity in Australia to improve farm gate returns in the short term is to reduce supply side cost.

- What are the drivers and constraints to farmers adopting alternative business structures, innovations or practices that will assist them in improving farm-gate returns?

  Myers-Briggs personality typing suggests over three quarters of rural Australia fit one type, being ISTJ. This group is introverted, learns by experience, struggles with emotion and prefers a structured environment. They are independent, conservative and resist change. The more pressure applied to these people the more they will default to their modal type and the harder they will resist until they break.
  Unfortunately the banking sector that underpins agriculture is also conservative and resists change with the same fervour, but with little to no risk of breaking.
  What is interesting is that nearly every government program is founded on the principle that we must change the farmer. With such a skewed demographic and defined modal type this kind of strategy is costly and unlikely to succeed making it a very poor deployment of tax payer funds.
  Conversely it is not appropriate to allow a business as usual mentality to dictate support systems to a sector that is in desperate need of reform as it too will be a very poor deployment of taxpayer funds.
  Regardless of the modal type, farmers are business people and they will respond to demonstrable financial benefits of practice change. The result is that any strategy to drive practice change must demonstrate conclusive and tangible benefit to warrant the change.
  Experience shows that farmer to farmer transfer of information and experience is one of the best tools for extension of knowledge and uptake of practice change. Typically this has been in production systems, but there is an opportunity to extend this scope meaningfully.
  The farm finance sector also needs a reformation and has a key role to play in this space. It is in the finance sector's interest to see changes in farm business structure as much if not more than the current farmer's because their future business will be underpinned by new entrants.

- What tools, skills and advice do farmers need to effectively adapt and respond to the risks they face?

Notwithstanding the previous answer, the operating environment around the farmer needs to adapt more than the farmer. Fundamentally there is no way to adapt to an unsustainable operating environment of rising costs and plateauing returns other than to exit the industry.

- What alternative actions or measures by governments, farmers or others would result in improved financial performance at the farm gate?

  It is essential to derisk agriculture in the face of unsustainable global commodity prices. Government underwrites workers compensation insurance as a means of protecting workers' livelihoods.
  It is essential that Government ensure there is adequate income protection for agriculture through production and market risk mitigation products similar to those that exist elsewhere in the world.
  Reducing production and market risk should also provide additional incentives to reduce financial risk premiums and lower capital costs. Furthermore private sector investment in the sector should increase in line with a lower risk profile for the sector.

- What approaches could be used to encourage improved drought preparedness?

  Drought preparedness is a function of economic resilience. It is impossible to prepare for drought if the market does not factor in production risk in times of good supply. The reality is that there is little the sector can do to internalise drought, flood or any other kind of risk when operating margins are set externally.
  Australia provides the most volatile agricultural operating environment in the world in terms of market and production variability. Global markets are influenced by heavily subsidised production systems that assume little to no production risk is borne by producers.
  The problem is amplified when agricultural businesses are debt funded.

- How can new farmers be attracted to agriculture and how can they succeed?
  (Deliberately unanswered)

Enhancing access to finance

It is intriguing that there is a lot of speculation about the impending boom in agriculture and constant discussion about the need to lift production to meet the massive increase in demand for agricultural products and yet there is resistance to investment in agriculture in Australia by both private and public sectors.

It is equally intriguing that, from all accounts, PrimeAg ultimately decided it could not provide projected returns to shareholders by operating an agricultural business and the best alternative strategy was to sell the assets.

The best commercial minds are struggling to make the business of agricultural production stack up in Australia under the current policy structures. This problem underpins and impacts access to finance at all levels in Australian agriculture.

Manufacturing is increasingly shutting down operations in Australia and moving them to countries where conditions are more profitable. This reflects on a difficult operating environment created in Australia due to high labour cost, high exchange rates and high regulatory burdens. The challenge for agriculture, which is enduring the same hostile policy setting is that the land is the factory and it just can't be shipped off.

Access to capital is a major challenge for agriculture. At this point in the decline of agricultural terms of trade, the lack of available finance is due as much in the short term to financial products not suiting the industry as the longer term decline in profitability.

There is much comment about the need for farmers to adapt and an expectation that they can magically make a broken system work. The reality is that the banking sector bears as much responsibility in the context of development and supply of finance structures that reflect the needs of the sector. It is not only the farmer who must adapt.

Farm businesses need to be able to manage their enterprise on long timeframes. Typically management cycles are and need to be longer than a single production cycle and rarely correspond to traditional banking or credit cycles.

For example, in a grain cropping business in the northern cropping region of NSW, it is a high risk to plant a crop without adequate stored soil moisture. The single biggest cost in the production cycle is planting followed by harvest. However, short term finance pressures and external cash flow expectations will often force a farmer to plant in poor conditions thereby maximising risk. The result is often a loss crop and increased financial pressure. The better strategy is to not plant and wait for better conditions and adequate stored moisture.

A simple case study in the drought of the early eighties: A sharefarmer is pressured to plant a crop in less that optimal conditions. The sharefarmer compromises and plants a reduced area. The crop is not profitable and produces about one tonne per hectare. The next year the sharefarmer grows a full crop on better conditions although still suboptimal at planting. The area that had grown a crop the previous year yielded about one and a half tonnes per hectare, while the portion of crop that had been left fallow the previous year yielded three tonnes per hectare. The area that had grown two crops had a total yield below that of the area that grew one crop. At the same time the area that grew two crops had cost nearly twice as much to manage due to the extra planting and harvest costs.

The result of short finance cycles that do not match natural management cycles is a compromise of best agricultural management to meet imposed finance constraints. Often this compromise has ramifications for long term viability and is counterproductive. In effect it increases management risk.

Once the management process is corrupted by external financial pressure, the cycle quickly escalates out of control. These external pressures are a major reason why people keep stock too long in dry conditions.

Resolving the mismatch of finance products and external financial pressures will buy some time for agriculture, but it will not resolve the underlying problems. That said it is important that the issue is addressed.

There is a need to establish a new norm in rural finance that recognises the cyclical nature of agriculture. It is more than likely that the reformation will to be driven by an independent structure. The Australian Reconstruction and Development Board as proposed in the current Reserve Bank

Amendment Bill has the potential to develop more suitable finance structures for Australian agriculture.

There are two other parameters that impact on access and utilisation of finance. Exchange rates and interest rates both play a key role in the capacity of agriculture to access finance and attract investment.

Exchange rates have been maintained at historically high levels by Government fiscal policy and an unwillingness by the Reserve Bank of Australia (RBA) to actively intervene. The high exchange rate has affected all export sectors and domestic industry competing with imported products. The problem is not unique to agriculture.

Interest rates are comparatively high in Australia. Interest rates are high as a result of Government fiscal policy and an unwillingness of the RBA to intervene. Again the problem is not unique to agriculture. However as a sector, agriculture appears to be deemed a higher investment risk and is subject to relatively high risk premiums and thereby endure even higher interest rates, adding significantly to capital cost of debt funded enterprises.

Australian farmers are forced to compete with foreign farmers who have low interest rates, directly subsidised production, multi-peril insurance and devalued currency. In the context of Agricultural competitiveness this is absurd.

- How do we better attract private capital into farm investment?

  A repetitive theme in regards to investment decisions is likely reward versus perceived risk. This is fundamental and unchanging. It is possible to trick the model by overestimating reward or downplaying risk, but success of these deceptive strategies is short lived and the impact of reputation damage would be profound.
  The challenge at the moment is that culturally there seems to be a belief that the solution to agricultural competitiveness lies in getting farmers to farm better or alternatively to get better farmers. The problem is that the risks increase relative to the rewards and on this basis the kind of people who would possibly make better entrepreneurial farmers choose other careers.
  Simply, if government will not support agricultural returns directly, it must reduce costs where possible and mitigate associated risks.

- What examples are there of innovative financing models that could be used across the industry?

  Performance based loans provide an opportunity for agriculture. A working example of this concept was the Higher Education Contribution Scheme (HECS). In effect students borrow money to pay for their tertiary education. This loan is paid back over time with payments subject to their income as determined by their tax returns. The program is administered by the ATO. The advantage of the system is that it removed the burden of scheduled payments. It was justified on the basis that tertiary graduates were likely to pay tax and therefore be able to pay back the loan. As a government program the HECS debt was subject to a lower than commercial interest rate making it affordable. This system of lending

avoids short term cash calls on the borrower and in mitigates some of the risk in variable cash flow.
The Clean Energy Finance Corporation provides an industry funding model that effectively reduces perceived risk and effective interest rates in a government private sector lending partnership. Banks were reluctant to fund renewable energy projects. This resulted in either high risk premiums applied to project funding or no funding. Government co lending reduced cost of funds because Government can borrow money cheaper than banks and also because the other result of the co funding was a lower perceived risk by the bank reducing margins and cost of funds considerably.
These two models could provide significant cost saving and improve access to finance if applied to agriculture. Both models provide loan support in place of direct grants, which represent better return for taxpayers' funds.

- What alternative business structures could be developed for farming that also retain ownership with farm families?

Gradually the value of agricultural land is being realised in terms of being a commodity in itself. This means that land prices are extending beyond values that can be serviced from the value of what is produced from the land on an annual basis. This is the beginning of the breakdown of the traditional Australian agricultural model of land ownership.
It is clear that without price support, young farmers will find it increasingly difficult to buy agricultural land and pay for it with the proceeds of the land.
For many years it has been understood that agricultural businesses need to be considered in two parts, one being the real estate component and the other an agricultural production business. It is clear that most of the capital in agriculture is tied up in the land and much of the wealth in agriculture has been created through capital gain on the land assets.
It was this phenomenon that drove many producers to engage in equity lending to expand their business base in spite of the inability of the new assets to pay for themselves on a cash flow basis.
It is increasingly obvious that tenant farming is going to become more common for young farmers. This model of farming is a challenge for existing lenders who cling to land assets for security.
The challenge lies in providing enough autonomy in the business model to attract entrepreneurial young operators to the business with enough financial reward to retain them.

- How can foreign investment best contribute to the financing and productivity growth of Australian agriculture?

It is unclear why there is a perceived need to rely so heavily on foreign finance. Australians hold billions of dollars in superannuation funds and very little of this is invested back into Australian agricultural investments or associated infrastructure assets. It is obvious that Australian agriculture is not a perceived as a good or safe investment by the market on this basis. Contrary to popular belief this is not just because farmers whinge a lot.

Foreign capital can and should be deployed in Australian agriculture, but it is essential that Australian farmers or funds are able to compete with these foreign funds. For example, sovereign funds are often seeking to improve their own food security and investment decisions are not constrained by the same return requirements as a purely commercial operator.
It is obvious that multi nationals investing in Australian agriculture have a natural hedge in play with geographical spread of production risk as well as having the benefit of multi-peril crop insurance programs elsewhere. This significantly reduces the overall risk in their business model in a way Australian farmers cannot match.
At the end of the day it is ironic that the operating environment for Australian agriculture is such that it is easier for foreign investors to enter the sector than for Australian investors or farmers. If the Government does anything to incentivise investment in Australian agriculture it should provide a preferential benefit to Australian funds.

Enhancing agriculture's contribution to regional communities

Agriculture ultimately underpins regional economies in Australia. There is a lot of hype and attention to the benefits of extractive industries, but most of the workforce is transient and the investment is not long lasting, so the real value to regional economies is also relatively brief.

In reality the family farm unit is the key to regional economies as they retain the wealth created in agriculture in their community.

Farmers are the originators of wealth in that they create something tangible from soil, water and sunlight. In effect farmers are the original solar harvesters. The fact is that the productive capacity of agriculture is the key to sustained economic activity in rural and remote areas and ultimately the entire economy also benefits significantly from it.

The point of this is that agriculture is the best source of long term capital inflow, not only for regional economies, but for the nation.

The second important consideration is that for most small businesses, their export income cycles through the local community first. In this way agriculture underpins the regional economy more than any other sector.

Conversely, the more pain experienced by the production sector the more it is shared by those who operate close to the farm gate. As farmers' incomes decline, they are slow to pay, the work force contracts and communities struggle. The decline in agricultural profitability is felt right through the regional economy.

- What impact does the growth of populations in regional centres and the decline in more rural or remote townships have on farming businesses and the agriculture sector?

  This is a chicken and egg scenario. It would be a fairer question to ask what impact is the decline in farm gate returns having on rural and remote communities and townships?
  The reality is that rural towns and services are dying because agriculture is no longer profitable enough to sustain them.

- How do we attract the next generation of farmers?
  (Deliberately unanswered)

Reducing ineffective regulations

The regulatory burden faced by all business in the Australian economy is both intrusive and expensive. Small business of all types spend an inordinate amount of time on compliance and reporting. This time is generally a distraction from core business and rarely contributes to profit or productivity

As a sector agriculture has one of the highest concentrations of small business enterprises. Over 90% of agricultural businesses are small businesses. Importantly many service providers to primary production are also small businesses.

Increasingly agricultural businesses can not comply with the increasing regulatory burden and ultimately do not even try. Agricultural productivity is in decline for a range of reasons, but the disincentive to employ people is becoming a major constraint.

Occupational Health and Safety laws, the cost of workers compensation insurance, general insurance and minimum wages are seeing some businesses no longer employ people. It is not uncommon to find farmers in their seventies operating farms without staff. The rationale is that they are not as productive, are probably as profitable and do not have the worry associated with staff. Simply their cost benefit analysis of employing staff does not stack up.

The result is, we have older people doing work they are simply not capable of sustaining and productivity is declining. This class of producer would often like to retire, but financial pressure and a lack of liquidity in the rural land market preclude this.

Younger operators are also actively minimising their labour cash cost and cutting corners on compliance to save money.

This problem is not unique to agriculture and again small business everywhere is under pressure and the solutions are not specifically agricultural. The main agricultural difference is that it is harder to exit the sector.

Enhancing agricultural exports

The Australian Government has worked hard in recent decades to increase market access and improve the value capture of Australian agricultural exports. The premise has been that we need access to these markets more than these markets need our products and so we have been negotiating from a position of weakness.

Looking forward the global population is growing fast and demand is increasing. At some point quite soon the market will need our product more than we need any particular market. The evolution and rebound of the live cattle trade into Indonesia is a prime example of this phenomenon.

Every Free Trade Agreement (FTA) that Australia has struck has failed to deliver unfettered market access for Australian agriculture. The most recent and arguably successful FTA with Korea still omits some sectors. These FTAs have been struck because there is a perceived economic benefit to Australia generally. However, not all sectors benefit equally from the FTA and it would seem agriculture and manufacturing are the biggest losers.

FTAs are argued for the collective benefit to the economy, but the reality is that while this argument is used in justification, it is not applied in practice. If the FTA agenda is truly about collective benefit then the entire economy should benefit. Yet no one has had the presence of mind to acknowledge that domestic industry has suffered under these FTAs and the globalisation generally.

While some may suggest that there is an element of socialism in this sentiment the reality is that the arguments that prevail against public money being deployed to support agriculture conveniently ignore the contribution of agriculture or its sacrifice in the context of public good. This is not about socialism it is about a fair go.

In a repetitive theme, Australian agriculture is captured within Australia with the land. The economic rationalism that suggests agriculture should fix its own problems belies the fact that some of the hardship faced by agriculture is not of its own doing.

Obviously it is desirable to improve market access, but at the same time trading off our competitive capacity, some of which is dependent on a strong domestic processing and manufacturing sector, is not desirable. Australia has allowed foreign products, produced in conditions that by law Australian farmers and manufacturers cannot match, to compete in Australian domestic markets. This is unsustainable.

The trade-off between enhancing the viability of the Australian food sector and maximising foreign market access has not been well managed. The perceived benefits of removing tariff protections for Australian domestic industries are difficult to recognise in the current landscape of declining manufacturing and agricultural productivity and profitability.

There is a strong and compelling case that Australian exports have also been severely disadvantaged by the sustained high value of the Australian dollar. Similarly, domestic industries that compete with imported products are hurt by a high Australian dollar. Wages are not linked to currency and so a high dollar applies and disproportionately high labour cost to Australian products.

The high dollar is a result of Government fiscal policy and poorly considered economic management that has hurt all export sectors. Enhancing trade is not just about market access it is also about understanding the full impacts of fiscal policy, currency and interest rates.

Globalisation

Economic globalisation is probably best defined as the increasing interdependence of nations' economies and the trend toward borderless trade.

It is intriguing that the notion of economic globalisation completely undermines economic independence. Yet in relation to agricultural policy that underpins the Australian agricultural economy, Australia is fiercely independent and increasingly out of step with the rest of the world.

Unfortunately Australian farmers are carrying the financial burden of this problematic behaviour.

Globalisation theory suggests that there are three key components related to economic success of a nation.

- (Inter)dependent (globalised) economy versus an independent economy
- Democratic society versus non democratic society
- Strong economy versus a weak economy

The catch is that you can only have two out of the three parameters on either side of the line. So if you wish to proceed down the globalised economy path, you forego independence and either democracy or a strong economy. You could argue Greece has an interdependent democratic, but very weak economy. Alternately you could argue China has a fairly globalised economy that is strong but not democratic.

Australian trade and economic policy seem to promote the benefits of globalisation without the necessary checks and balances to provide a strong economy. Simply, if Australia is to maintain a strong democratic economy and its national independence it must look to maintain essential industries within its shores and forego increasing globalisation.

Typically primary and secondary industries should prevail in terms of economic importance to an independent state.

Obviously this an oversimplified summary of an incredibly complex issue. However, the resounding an inescapable fact is that while a little bit of globalisation might be good it does not mean a lot is better. The promotion of trade liberalisation needs to be balanced with the need to preserve essential domestic industries to maintain a strong domestic economy.

Agricultural competitiveness is not easily achieved in global markets because so many countries do not want to risk complete interdependence in food security. As a result there is a propensity to foster over production in the short term to ensure long term productive capacity. These actions undermine true globalisation of the agricultural sector in the long term.

Australia should take note of the prevailing global social constraints to agricultural production and trade and ensure the long term viability of its own agricultural sector.

The necessary decisions cannot be made on a populist basis with short term media and public opinion motives. These decisions must be made with generational considerations or they will fail. It is on this basis that the reform of Australian agricultural policy must be undertaken.

Climate

The biggest omission from the Agricultural Competitiveness Issues Paper is direct reference to climate change and the risk to agricultural productivity within Australia and globally. Regardless of people personal views about anthropogenic global warming, climate is changing and agriculture is completely dependent the prevailing climate.

The Intergovernmental Panel on Climate Change (IPCC) released its latest report and the Federal Government reportedly accepted the findings of the report. The report highlights direct threats to global agriculture and proves declining productivity growth can at least in part be directly attributed to climate change. This impact is likely to increase going forward.

Australian farmers have managed a variable climate comparatively well historically, however the forecast is for increasing incidences of extreme weather events including, dry, heat and flood. The reality is that we are already seeing these impacts and the sector is already struggling to absorb the economic impacts. Commentary around drought is still considered in an historical context, without any apparent acknowledgement that producers are already in unchartered waters in terms of climate variability.

The Issues Paper touches on drought and mentions in passing the potential for increased frequency and intensity. Water is generally the most limiting resource in Australian agriculture. The implications of a changing and more particularly drying climate are profound in terms of productivity and therefore competitiveness. This is particularly important in the context of competition for resources between agricultural, urban, industrial and environmental demands.

Australian agriculture needs much better tools to forecast seasonal weather conditions to maximise resource efficiency and minimise the impact of production downturns. Our current climate forecasting tools rely heavily on historical information and data interpretation, which will be less relevant and reliable as global weather systems change with global warming. It is critical to the preparedness and long term economic resilience of the agricultural sector to have reliable seasonal forecasts that forewarn producers of likely production conditions.

Underpinning every conversation about the future of Australian agriculture is the need to increase production to meet the growing demand. Most farmers hope for the best, the good ones often plan for the worst. The impact of climate change has the potential to disrupt existing agriculture to an unprecedented degree. The impacts of this will not only create hardship in agriculture, but could lead to a complete breakdown of society globally as we fail to meet the global food challenge.

Contrary to popular belief, ignorance is not strength. We cannot afford to ignore climate change in consideration of agricultural policy or any other policy for that matter. The Federal Government has endorsed the latest IPCC report and findings and must act on it.

The impacts of variable and changing climate are not going to be restricted to agricultural enterprise and all sectors of the economy are vulnerable.

Reserve Bank of Australia

The RBA is Australia Central Bank and has a range of powers and responsibilities. Along with a broad preamble it operates with three stated objectives:

a) the stability of the currency of Australia
b) the maintenance of full employment in Australia; and
c) the economic prosperity and welfare of the people of Australia

In order to achieve these objectives the Government and the RBA operate independently, but with combined and supposedly complimentary objectives. There is a written understanding of the scope and charter of the RBA. Typically this has resulted in the RBA targeting inflation figures and manipulating interest rates to ensure stays within a target band generally agreed to indicate a stable economy.

It is clear that the tools the RBA has been given in its undertaking with Government has at best provided a very blunt tools to manage the economy and clearly there is scope for the RBA to do much more in its management of the economy through monetary policy. The RBA was also established with a clear goal to stimulate investment and development in the Australian economy.

The RBA is supposed to be a stabilising agent in the economy and it achieves this in no small part because its members are not subject to the electoral cycle or even the whim of political parties. This is not to say the RBA is not accountable, but it is able to exercise its own discretion in the execution of its duties within its charter.

It is sensible and very necessary to have at least one half of economic management implemented independently by people with appropriate skills and a strong mandate. It is an indictment on our political system that very few politicians appear to possess the requisite skills or political independence to put the needs of the nation above party point scoring.

Recently Legislation was tabled in the Federal Senate to establish the Australian Reconstruction and Development Board within the RBA to facilitate investment in key sectors of the economy including primary industries. This Legislation provides an interesting segue in our expectation of the RBA and more importantly a return to its roots as key driver of economic development with a broader scope of roles and responsibilities.

The Government can improve economic conditions for essential industry and it must review the role of the Reserve Bank as a central bank. At very least Australia must actively manages its currency and interest rates to maximise the competitive advantage to primary and secondary industries. Simply, the RBA must implement strategies that further bring down the comparative value of the dollar and bring down interest rates in a controlled and considered manner.

The memorandum of understanding that exists between the RBA and Government needs to apply more emphasis on the international competitiveness of the Australian economy versus inflation.

The Reserve Bank's charter is not currently being realised by the existing agreement of operational parameters with Government.

An Agricultural Succession Strategy

Australian agricultural succession is a growing, sector wide problem with an increasing average age of producers and a declining number of enterprises. The decline in the sector generally means that there is a need for significant structural adjustment to achieve this succession.

The problem requires a considered response to industry succession that helps retiring farmers exit the industry and provides a sustainable longer term entry pathway for new or expanding farmers. It would be sensible if this strategy was applicable over more than one generation of farmers.

It is clear that there are many farms for sale at this time, either listed or not. It is also apparent that there are not nearly as many willing and able buyers. Some corporate/sovereign investors are active in the market still, but have a select criteria that they are looking for and this means there is a large portion of farm land that does not have a suitable buyer which has undermined the liquidity in the market.

The result is that older farmers are forced to stay on the land or meet the market in a very depressed environment. The flow on effect of realising land devaluation this way is that it erodes perceived equity for farmers who are not willing, or planning, to leave the industry at this time and ramps up credit pressure. This is all very basic and should be well understood by policy makers.

There are willing buyers and there are some able buyers, but there are not enough willing **and** able buyers. This is primarily a concern for younger farmers who wish to enter or expand and do not have sufficient equity to sustainably achieve their aspiration. A significant challenge is that bank credit policy relies heavily on equity and typically requires loan security ratios that are simply unachievable.

Young farmers enter the industry in a range of ways. Often they will engage in tenancy arrangements to either sharefarm or lease country and couple this with contract farming or other off farm income. However there are problems in raising operating capital because these tenant farming models are largely unsupported by the banking sector who do not recognise this kind of private tenure as a bankable security.

The Australian Government/s (State, Federal or both) could enter the market and start buying farm land with a view to leasing it back to young farmers. There are a range of reasons why they should do this, some of which are outlined below:

- Agricultural land is a perpetual asset of the nation and in effect this generation only ever really borrows it from future generations, therefore there is a compelling justification for Governments to buy and hold agricultural land in trust for future generations. Typically, Australian land prices really only reflect a generation of tenure and so the perpetual value of agricultural production from the land is not reflected in the current asset market value.
- If Governments buy back farms these assets sit on the balance sheet to offset the expenditure or any borrowing initiated to execute the purchases. As a result it is a better strategy for Government to buy land than to bail out producers.
- Historically, Crown Leases have been deemed to be bankable security, so Government owned land potentially underwrites agricultural tenancy for young farmers who should then be able to undertake long term and very stable tenancies, which they cannot do on a private ownership basis.
- Government borrowing costs are significantly lower than commercial agriculture costs. As a result the Government could provide profitable lease tenure to provide a sound investment for taxpayers in agricultural land and still provide more affordable tenure for young farmers.
- The timely intervention in the agricultural land market would provide a floor in the land price that would in turn stabilise the operating environment for existing land holders and potentially mitigate the risk perceived by banks in a depreciating agricultural land market. This is a critical step in averting a massive write down in the wealth of the agricultural sector particularly in the broadacre industries.
- It is clear that foreign sovereign investors are seeking to underwrite their future food security and it is essential that Australian Governments recognise that the fundamentals that drive those investment decisions cannot be matched by Australian farmers. Therefore it is necessary to mitigate the investment pressure to provide suitable pathways for young farmers to enter the industry not only in this generation, but on an ongoing basis.
- The Government has a better justification for interfering in agricultural production systems through vegetation laws, etc.... if it takes steps to mitigate either the cost of doing business or the inherent risk in the business. Buying and affordably leasing back farm land is a tangible and responsible way to mitigate cost perpetually.
- Government land purchases will create some liquidity in the farm land market and create some competition for assets that are otherwise stranded. This provides an exit strategy for older and perhaps less productive farmers that will in turn be replaced by more productive participants.

There is compelling evidence that structural adjustment of agricultural tenancies is necessary. Throughout Australian agricultural history there has barely been a generation that has not been subject to some form or structural adjustment by both State and Federal Governments. It is somewhat ludicrous to suggest that in the current of environment of eroded terms of trade, high interest rates and a high dollar that the next generation of producers can achieve the necessary structural adjustment without Government assistance.

This proposal is a strategy that potentially buys time for Australian agriculture, but does not resolve the underlying problems that are impinging on long term agricultural viability.

Conclusion

At a meeting in St George, Qld, in February 2014, the Federal and Queensland Ministers for Agriculture both acknowledged publicly that the problems producers are facing in the current drought are symptoms of deeper structural problems in Agriculture. This public acknowledgement should act as an alarm for policy makers that the current system is failing.

Einstein is attributed with suggesting it is insane to keep doing the same things over and over again expecting a different outcome. He was pretty cluey and it is clear that the sector needs significant policy reform, not just tinkering around the edges.

As a scientist one of the first disciplines in research is to properly define the problem that needs to be resolved. So the challenge in providing the right answers lies in asking the right questions. I am not confident that issues paper does in fact ask the right questions.

Farm viability is the key to improving competitiveness. All the associated problems of employment, productivity, regional economic stimuli, industry succession, capital investment, etc, will be significantly addressed by improving viability of the sector.

Unfortunately the real and tangible solutions to farm viability do not appear to fall within the current ideological remit of Government. Until there is a major shift in political attitude, Australian agriculture will continue to decline.

The Agricultural Competitiveness Whitepaper must tackle the big issues. The White Paper must make a bold and <u>honest</u> statement about the importance of Agriculture to the average taxpayer today and much more importantly to future generations. It will be on this basis that meaningful reform will be achieved and agriculture in Australia will be able to compete both within the Australian economy and also globally.

Inescapably, the solution to sustainable agricultural competitiveness lies in recognising the true cost of undertaking an agricultural enterprise and accepting that sustainable food production is not discretionary.