Agricultural competitiveness issues paper

Submission from Baker & McKenzie

April 2014

Foreword

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Australia's position as a leading agricultural producer is a great achievement but efforts to bolster the industry are welcome, not only because of its importance to Australia's food security but as a key economic driver for the 21st century.

Baker and McKenzie applauds the Australian Government and the Honourable Barnaby Joyce for commissioning the Agricultural Competitiveness Issues Paper (ACIP). Australia's position as a leading agricultural producer is an outstanding achievement but efforts to bolster the industry are welcome, not only because of its importance to Australia's food security but as a key economic driver for the 21st century.

There will no doubt be many issues raised for consideration in submissions provided to government for this ACIP. Baker & McKenzie's submission is intended to be more targeted, focussing on some of the key industry issues we identified in our 2012 report titled Food Security: Fact or Fiction? This report was the result of extensive industry consultation and analysis. It contains valuable insight of direct relevance to "Issue 1: Ensuring food security in Australia and globally" of the ACIP. Briefly, the details of our methodology are as follows.

- We developed a comprehensive research questionnaire and commissioned Beaton Research and Consulting in early 2012 to undertake detailed fieldwork covering a range of issues relating to food security, affordability and quality.
- The research consisted of a mix of telephone and internet- based interviews, with all interviews taking place between 10 – 31 January 2012. Respondents were drawn from a range of senior managerial and legal professionals working in food manufacturing, distribution, supply, regulation or agribusiness. The fieldwork targeted professionals working in Australia.
- A total of 162 respondents were interviewed during this period. These respondents represented 68 separate organisations in government and the private sector. The fieldwork research was complemented with additional desk research and case studies looking at countries across all the major trading markets which helped to provide further insights on key issues contained within the survey fieldwork. The findings were analysed and the report written in February 2012 and published in March 2012.
- The sample included a mix of sectors, with 27% from food manufacturing, 25% from wholesale and retail and a further 24% from retailing and hospitality.

Using the results of this survey for guidance, we have developed a set of submissions for the Australian government, specifically aimed at the issue of food security.

Executive summary

The first message highlighted in our report was the strong desire by respondents for government intervention in, and regulation of, the activities of supermarkets in food retailing (62% of respondents). This intervention could include the creation of a Supermarket Ombudsman and Code of Practice, as proposed by the Australian Food and Grocery Council. This intervention would be greatly supported by food manufacturers for whom the number one challenge is the prevalence of private label products (as highlighted by 59% of respondents).

Our report shows that views on foreign investment in the food sector and agribusiness are polarised, with 26% of respondents "sitting on the fence" or undecided when asked if foreign investment poses a significant risk to food security, whilst 49% agreed that foreign investment is a serious threat, and 26% disagreed. Surprisingly, a similar "protectionist" sentiment exists on the issue of international trade barriers, with 45% of respondents agreeing that trade barriers should be heightened in response to issues like parallel importing.

Overall, availability of water was identified as the greatest challenge to Australia's food supply by the majority of respondents. Some groups saw the challenges differently, with respondents in food retailing and hospitality seeing natural disasters as the greatest challenge. On climate change, the majority of respondents were concerned with the potential for climate change to negatively impact global food security, although only about a third of respondents saw it as a serious issue.

Furthermore, only half of respondents felt their organisation was not vulnerable to the adverse effects of climate change and only about 27% of respondents saw regulation around the environment and climate change as a concern - which is somewhat surprising given the debate over carbon cost pass through in the supply chain. However, those in the financial and insurance sector had a high degree of concern over the impacts of climate change, largely we expect because of their exposure to the losses suffered in the Queensland cyclones and floods.

As indicated by a majority of our survey respondents, there is a strong and unequivocal desire for both government and the private sector to invest more behind innovation and R&D. Biofuels and GM foods were areas identified as important for innovation and R&D spend to improve food security. Contrary to consumer concerns, there is a remarkably strong demand by our industry respondents for GM food to form an essential part of delivering food security (58%).

Based on our survey findings, there is lack of confidence that the current regulatory framework, especially in the areas of parallel importing, marketing claims and food labelling, are adequate. For example, 68% of respondents thought more (or better) regulation was needed for parallel importing (only 8% disagreed). Many respondents said country of origin labelling is critical and should appear on pack (71%). Likewise, respondents said better marketing claims regulation is required (75%).

Our survey findings have shown that Australia's need for food security is actually a fact, not fiction. It highlights the gaps in the food and agribusiness industry which need to be fixed by both government and corporates so Australia can capitalise on the resources already given to us. Our submissions, intended to address these gaps, are as follows:

- 1. Implement a National Plan that deals with the important challenges to food security that we face including population growth, climate change and diminishing resources. Alongside this, should be initiatives to promote government and private investment in water infrastructure and technology.
- 2. Introduce a Supermarket Ombudsman to oversee a Code of Conduct on fair trading that would seek to ensure a level playing field across the supermarket sector.
- 3. Develop ways to address concerns about foreign competition and investment. Ensure an appropriate balance between attracting adequate levels of investment, whilst avoiding potential pitfalls if too much foreign investment was allowed for a strategic industry like agriculture.
- 4. Enhanced investment in innovation and R&D from both the Government and private sector is needed to develop new technology and to improve agricultural productivity.
- 5. A national debate is needed to address legitimate areas of concern with respect to GMOs and to correct misinformation that persists in respect of
- 6. The government must overtly recognise the threat that climate change poses to Australian agriculture and take action to address it. In light of the increasing frequency of extreme weather events, it should ensure that adequate funding is available to fund disaster relief.
- 7. Implementation of food label information needs to be widened and deepened, to include more effective information. There is overwhelming support for the provision of more detailed country of origin information on food labels, as well as stronger regulation of product claims.
- 8. The Government should explore ways to support new industries that will create more opportunities for Agriculture especially in the areas of Bio-fuels and Sustainable Aviation Fuels that support other national objectives such as fuel security.

Biggest challenges to food security

Using the United Nations' (UN) Food and Agriculture Organisation (FAO) definition, food security is achieved when all people, at all times, have physical and economic access to sufficient, safe and nutritious food to meet dietary needs and food preferences for an active and healthy life.

One of the foundations of modern consumer capitalism is the near-universal availability of affordable food in the developed world. This has been made possible by great leaps in agricultural productivity in the 19th and 20th centuries. The most recent and drastic of these is the "Green Revolution", during which improved crop breeding and intensive farming technology accelerated agricultural productivity from the 1940s. As a result, the real price of food fell from the 1950s until the early 2000s.²

This development not only allowed considerable population growth, but also ensured consistently affordable and accessible food as a reality for people in the developed world. Events of the past few years and global socio-economic trends suggest that this situation is likely to come under increasing pressure. This new reality first came to light during the 2008 food crisis where the price of a tonne of wheat rocketed from US\$167 in January 2006 to US\$481 in March 2008.3 This acute price spike has receded for now, and the US Department of Agriculture's near-term forecast is optimistic, but its structural causes have not disappeared. Agricultural productivity growth has slowed, whilst the world will have to feed another two billion (or more) people by 2050, according to UN population estimates.5

Preventing increases in food prices is a key priority for governments and, given the increasingly globalised nature of the food supply chain, it is an area in which global cooperation will be essential. Most Australians would recognise that Australia's level of food security is high. Nonetheless, food security is a key issue for Australia because:

- population increases could constrain food production;
- our food supply and commodity prices are increasingly volatile due to climate changes and economic conditions;
- we are importing more foods which puts the viability of local producers and manufacturers under increasing competitive pressures;

From the Green Revolution to the Gene Revolution: How will the Poor Fare?, FAO, November 2005

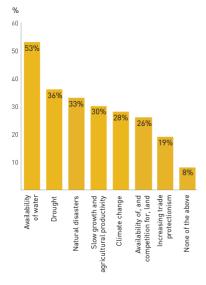
² Rising food prices: A global crisis, ODI, April 2008

³ Rising food prices: A global crisis, ODI, April 2008

⁴ http://www.ft.com/cms/s/0/54cf1176-5e40-11e1-85f6-00144feabdc0. html#axzz1nZb3cU96

UN Population Division, World Population Prospects: 2010 Revision

Fig. 1 Which of the following factors present the greatest challenge to Australia's food supply?



- serious food insecurity in our region could become a national security threat to Australia; and
- there is increasing competition in how we use rural land, between energy resources (such as biofuels and gas) and food production.

A majority of respondents (53%) to our survey felt that the availability of water was the largest challenge (Fig. 1). Availability of water can be impacted by climatic issues and domestic infrastructure, such as dams, irrigation and drainage systems, and water supply technology. A significant minority (36%) felt that drought was the greatest concern. Natural disasters, slow growth of agricultural production and climate change were the third, fourth and fifth.

SUBMISSION #1

Taking the availability of water and drought as essentially one and the same challenge, the message from this result is that governments and business should invest in water infrastructure and technology.

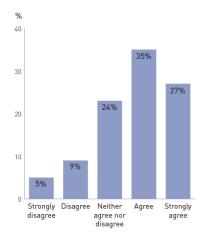
Also, the former government's policy initiative to develop a National Food Plan (which has since been disbanded) is something to be revisited, albeit in an alternative form. The plan identified a number of important areas to address for the good of the nation, including:

- global population growth;
- changes in global growth patterns;
- climate change; and
- finite nature and availability of natural resources.

These are ongoing concerns, all of which impact on Australia's food security that remain to be adequately addressed by government.

Competitiveness and Food Retailing

Fig. 2 Do you agree that Australia needs legislation to proscribe behaviours of retailers and suppliers?



Australia is an example of a market, similar to the United Kingdom and United States of America, where "full service supermarkets" have established leading positions in grocery retail. In Australia, the retail market is highly concentrated, after New Zealand the most highly concentrated, with Coles and Woolworths estimated to have a combined market share of 80% in many categories.⁶

Whilst the popularity of supermarkets attests to consumer enthusiasm for them, their rise is not without risks. Their position in the market creates concern on both the supply and demand side for future food choice and affordability.

On the supply side, supermarkets around the world have been able to reduce the margins of their suppliers. There are questions over the long-term implications, with a possible reduction in viable producers and manufacturers.

2011 saw plant closures of food processing facilities across Australia. For example, SPC Ardmona and HJ Heinz closed facilities in Australia. Earlier this year, SPC Ardmona again ran into financial difficulties and needed to be bailed out by the Victorian government to the tune of \$22 million to pay for upgrades to its facilities. There are well-founded fears that foreign imports could take their place, undermining Australia's food processing sector.

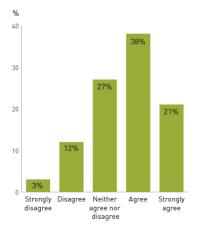
Our research sought the opinion of Australian food industry participants on the food retail sector. Overwhelmingly, respondents were in favour of more government intervention. 62% believed new legislation is needed in the food sector (Fig. 2). In written responses, some were even more vocal, with one commenting that food retailer dominance "challenges the negotiating power of the biggest suppliers". The respondent continued that he felt competition laws were little help, due to "fear of commercial retaliation". Another respondent simply stated that the imperative is to "beat the duopoly". There were a few dissenting voices, with one respondent indignantly noting "Are we running out of food? Protecting suppliers will lead to less competition and higher costs for consumers".

The enduring theme was of an "imbalance of power" between retailers and suppliers, with Coles and Woolworths blamed for putting at risk the future of Australian food manufacturing and processing.

One of the other key concerns relates to the increasing use of private labelling, where products owned by retailers compete with their suppliers' traditional branded goods. Since private label products tend to be slightly cheaper to produce than

http://www.daff.gov.au/ data/assets/pdf file/0003/298002/foodmap-full.pdf

Fig. 3 Do you agree that private labels are the number one challenge for food manufacturers?



other "name" brands, the supermarkets are often able to undercut these brands and offer savings to the consumer, a fact that has fuelled private label growth during the recent economic downturn. Therefore, private label contributes to affordable food for consumers, and its growth is to be welcomed.

However, private label has generated concerns that retailers could obtain information about a supplier's/competitor's product which could be misused to the advantage of the retailer's private label product. Also, some private label products can be said to "look alike" or "copy" established brands.8 This, together with concerns over retail dominance, has led to calls for the introduction of a Supermarket Ombudsman in Australia, to oversee a Code of Conduct on fair trading, which would include rules against "copying" food packaging.

Another concern is the threat that private label plays to consumer choice in the long run. If "name" brands are out-competed by low price supermarket brands, this will give the supermarkets even greater control over pricing and product selection in future, which could be to the long term detriment of suppliers and consumer choice.

Our survey questioned respondents on the threat of private label, and 59% agreed that it is the number one challenge for food manufacturers in Australia today (Fig. 3). Only 15% disagreed. This is an affirmation of the major impact of private label on Australian food manufacturers. One respondent summarised the mood of the survey succinctly, saying that private label could force suppliers to "produce a Woolies or Coles home brand if they want their own product... to get on the shelves".

Our survey demonstrates a strong desire to see appropriate regulation applied to supermarkets. A reduced and weak food processing segment of the food supply chain in Australia is not good for consumers in the long term, where they face decreased choice, and potential price increases through lack of competition.

SUBMISSION #2

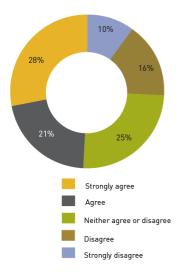
The government should consider introducing a Supermarket Ombudsman to oversee a Code of Conduct on fair trading that would seek to ensure a level playing field across the supermarket sector. Amongst other things, the Code should promote competition and address concerns about private labelling to achieve greater balance between players in the industry.

http://au.nielsen.com/site/documents/ PrivateLabelGlobalReportMar2011.pdf

http://www.ausfoodnews.com.au/2011/11/28/supermarkets-accused-of-%E2%80%98copycat%E2%80%99-packaging-on-private-labels.html

Foreign Investment & Trade

Do you agree that foreign ownership of agribusiness assets is a serious threat to Australia's food security?



Foreign investment in Australian agricultural land and assets plays an important role in maximising food production and supporting Australia's position as a major net exporter of agricultural produce, by financing investment, and delivering productivity gains and technological innovations.

In January 2012, the Australian Parliament released the results of an official inquiry in relation to acquisitions of rural and agricultural land by foreign investors. The inquiry concluded that "Australia's foreign investment policy strikes the right balance between attracting foreign investment into Australia to support [the Australian] economy, and ensuring that investments are not contrary to the national interest. This applies to investments in all sectors of the economy, including agriculture".

Various community proposals have called for possible amendments to the current regulatory regime, such as:

- changing the regulation of foreign investment in "rural land" to be more consistent with the regulation of foreign investment in "urban land"; or
- placing additional conditions on proposed acquisitions of rural land (i.e. for rural land acquired to facilitate mining operations, requiring companies to sell the land back to Australian farmers once mining operations are completed).

Our research sought to probe views and sentiments in this area. We asked respondents whether foreign ownership is a serious threat (Fig. 4). Almost half of the respondents – 49% agreed that foreign ownership is a serious threat. 26% disagreed, and 25% neither agreed nor disagreed.

When commenting on foreign threats to food production, some of the remarks included expressions of concern that foreign ownership:

- might lead to a lack of control of a valuable resource;
- puts pressure on Australian jobs;
- could compromise quality;
- leads to a repatriation of food to the investor's home market.

On the positive side, those disagreeing that foreign ownership is a problem cited a range of factors, including Australia's agricultural surplus, the benefits of capital investment and that foreign investment has been a key feature of the Australian economy for some time.

It is critical that Australia resolves this policy dilemma soon because Australia is increasingly seen as an attractive market for foreign investment in agriculture and food. Transport and communications, and markets for farm inputs and produce, are well developed. Skilled labour and managers are readily available, and sovereign risk is low under Australia's stable and transparent government. Australia also has a number of existing trade links with markets in Asian countries.9

The time is ripe for a clear policy on the issue of foreign investment, particularly in light of the Archer Daniels Midland takeover bid for GrainCorp which appeared to have been blocked on political grounds. Without it, the lack of certainty about how government will approach foreign investment decisions may be factored in as a significant risk for investment in Australian agriculture. There will be continuing strong interest in this area, particularly from overseas investment funds, and it would be prudent for Australia to position itself to benefit from that capital.

One of the most intractable areas for food security is the international trade rules relating to agriculture. Some countries use trade-distorting policies, such as domestic support or subsidies, or market access restrictions. Others worsened the 2008 food price spikes by imposing export restrictions or imposing export tariffs on key commodities, such as wheat and rice.

Another serious issue is the high level of tariff protection on agricultural products, which are overall four times higher than industrial tariffs, and also non-tariff barriers in agriculture and food are generally high. Australia is an exception to this rule and has always maintained a free trade policy perspective.

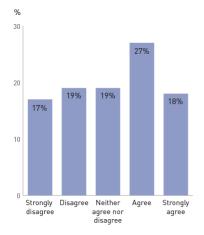
In its recent report entitled FOODmap, an analysis of the Australian food supply chain, DAFF collected the most recent data on the value of Australia's food trade. According to that report, the key features of Australia's current trade in food are as follows. 10

- A high proportion (an average of 31% over the three years to the end of the 2010 calendar year) of exports are shipped unprocessed – either in live form (e.g. livestock), fresh/chilled form (e.g. seafood and horticulture) or as bulk raw exports (e.g. grain).
- Much of the growth in food imports has been in processed foods, with unprocessed foods accounting for less than \$300 million, or 8% of the total growth in the value of food imports.
- Australia's trade surplus in processed food products has declined from \$10.6 billion in 2005 to \$7.4 billion in 2010. Over this period, total food exports have fluctuated but not grown significantly, while processed food imports have steadily increased by about \$3.4 billion.

http://ministers.treasury.gov.au/DisplayDocs. aspx?doc=pressreleases/2012/002.htm&pageID=003&min=mva&Year=& DocType=

Page 16, FOODmap: an analysis of the Australian food supply chain, by the Department of Agriculture, Fisheries and Forestry, 2012

Fig. 5 Do you agree that the Australian Government should impose higher tariff and non-tariff barriers to favour Australian-made commodities. ingredients and foods and slow the rate of food imports?



Our study asked whether the Australian Government should impose higher barriers to favour Australian made commodities (Fig. 5). Surprisingly, given Australia's historical position as a strong "free trader", 45% were in agreement. However, there was also a strong negative sentiment with 36% disagreeing, and 19% neither agreed nor disagreed. Comments in support ranged from concerns about dumping and unfair trade practices, supporting local producers, other countries subsidising their agriculture industries, through to supporting local jobs and the local economy. Those disagreeing with calls to increase trade barriers expressed a range of views, including:

- a free market is essential to Australia's economic growth;
- imports force Australian industry to be more competitive;
- food imports give the consumer greater choice; and
- a liberal trade regime opens up global markets for Australian industry.

SUBMISSION #3

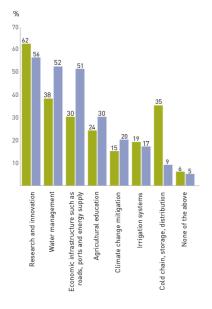
There is a surprisingly high concern about foreign investment, coupled with an equally surprising willingness to move to more trade protectionism, to protect jobs, food quality and local industry.

The government should consider ways to address these concerns and meet an appropriate balance between ensuring adequate levels of investment, whilst avoiding potential pitfalls if too much foreign investment was allowed in agriculture, given its status as a strategically important industry.

Innovation and R&D

Government's top priorities.

Which of the following areas should be investment priorities for government?



well as changing consumption patterns. To investigate where the investment priorities should lie to improve food security, we asked our respondents what the Government's priorities should be to ensure food security (Fig. 6). Over half of the respondents stated that investment in economic infrastructure such as roads, ports and energy supply, investment in water management and investment in R&D and innovation should be the

Historically, productivity growth in agriculture has been a key driving

increasingly apparent that new, innovative technologies will be critical to meet the growing demands of demographic and social developments, as

force in feeding a rapidly growing global population. It is becoming

In addition to exploring what the Government should be doing to ensure food security, our research probed sentiment about what corporate Australia could and should be doing. Research and innovation was again identified as key - 62% of those we surveyed thought that research and innovation should be an investment priority for corporate Australia. Water management again was identified as being a second priority (38%) with investment in cold chain, storage and distribution recommended as the third greatest investment priority for corporate Australia.

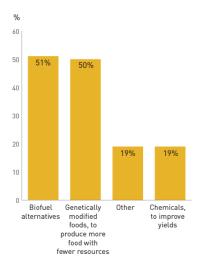
While Australia's IP laws generally provide protection for innovation that equates to that of our major trade partners, use of the IP system is less impressive. While more than 3% of published scientific research worldwide originates from Australia, less than 0.5% of patent filings are Australian.

This reflects well known Australian strengths in primary research and a long identified weakness in commercialisation of that research. How to educate and encourage those involved in research and its commercialisation to best use IP laws to maximise the value and potential of Australian R&D efforts remains a challenge for governments, public institutions (universities, CSIRO, CRCs) and private enterprise.

Fig. 7 shows which subsets of innovation and R&D on which respondents preferred investment. The majority believed that biofuel alternatives (51%) and GM crops (50%) should be promoted and incentivised.

It is curious that respondents in the food sector ranked biofuels so highly because. in an international context, biofuels create new pricing dynamics in commodities and, arguably, distort food markets.

Fig. 7 Which of the following fields of innovation and R&D should be incentivised, to improve food security in Australia?



At the height of the 2008 food crisis, major developed economies deprived the international market of essential commodities by diverting a considerable portion of their products for biofuels. The prices of food crops are now inextricably linked to the price of oil. The more the price of oil increases, the more profitable it is to convert food crops to biofuels.

Among the "other" category, the most common suggestions for fields of innovation that should be incentivised were:

- nutrient application methods;
- sustainable practices e.g. subsurface water irrigation; and
- expanding arable land in Australia.

SUBMISSION #4

Enhanced investment in innovation and R&D from both the Government and private sector is needed to develop new technology and to improve agricultural productivity. Government should consider how to promote local and foreign investment into R&D given the dividends that it can provide, not only commercially, but for the Australian community.

GM foods

Do you agree that new technologies such as GM foods will be essential if food is to be accessible in sufficient quantities?

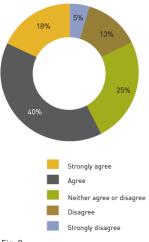
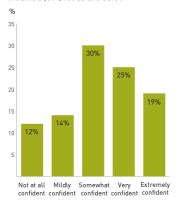


Fig. 9 How confident are you that genetically modified (GM) foods are safe?



Fia. 10 How confident are you that GM foods are safe?



GM foods are foods produced through genetic engineering or containing genetically engineered ingredients. As can be seen from Fig. 7, there was a strong demand among respondents for investment in GM food innovation.

Fig. 8 shows the importance of GM crops in ensuring food is accessible and available in sufficient quantities. The majority of respondents (58%) said they believe that new technologies, such as GMOs, are essential for food accessibility.

It could be said the results on GM foods in Fig. 7 and 8 are surprising, given the level of discomfort and uncertainty amongst consumers on the safety of GM foods. However, it makes sense in light of the scientific evidence surrounding the health implications of GM foods which indicates that this concern is not warranted. The European Commission Directorate-General for Research and Innovation 2010 report on GMOs noted that "The main conclusion to be drawn from the efforts of more than 130 research projects, covering a period of more than 25 years of research, and involving more than 500 independent research groups, is that biotechnology, and in particular GMOs, are not more risky than conventional plant breeding technologies".11

The dispute about the safety of GM foods is most intense in Japan and Europe. where public concern about GM food is higher than in other parts of the world, particularly the United States where GM crops are more widely grown and the introduction of these products has been less controversial.

However, by reviewing Fig. 9 it is clear that Australian industry (as opposed to consumer) respondents are confident that GM foods are safe to eat. Surprisingly, there were significant disparities in perceptions between regions in Australia (see Fig. 10). For example, in New South Wales, 52% were either extremely or very confident whereas in Victoria, 43% were mildly or not at all confident of the safety of GM foods.

SUBMISSION #5

There is a mismatch between community perceptions about GMOs and what the scientific evidence tells us. A national debate is needed to address legitimate areas of concern with respect to GMOs and to correct misinformation that persists in respect of them. GM foods that have been assessed and considered safe should be implemented more widely to ensure the sustainability of the food supply and to meet environmental needs.

http://ec.europa.eu/research/biosociety/pdf/a decade of eu-funded gmo research.pdf

Climate change and natural disasters

Over the last few years the issue of climate change has played an increasingly prominent role in the debate on food security. As the United Nations Conference on Trade and Development (UNCATD) has noted: "climate change has the potential to damage irreversibly the natural resource base on which agriculture depends, with grave consequences for food security".

In Australia over the past few years we have seen an increasing frequency of volatile climate events with floods, drought and cyclones that have impact on both our national food supply and our supply chains, resulting in the need for a greater reliance on imports during such periods.

For many, climate change, regardless of whether there is a link to these events, is viewed through the prism of "natural disasters". In its State of the Climate 2011 report, the CSIRO noted: "Much of Australia may have lurched from drought to floods since the previous State of the Climate, [2010] but this has occurred against a backdrop of steadily increasing air and ocean temperatures and rising sea levels. What's more, the rate of change is increasing".

The 2013 Annual Climate Statement published by the Bureau of Meteorology supports this view, noting that "2013 was Australia's warmest year on record while rainfall was slightly below average nationally.

- Summer 2012–13 was the warmest on record nationally, spring was also the warmest on record and winter the third warmest.
- Overall, 2013 was Australia's warmest year on record: annual national mean temperature was +1.20 °C above average.
- All States and the Northern Territory ranked in the four warmest years on record.
- Nationally-averaged rainfall was slightly below average for the year, with 428 mm (1961-1990 average 465 mm).
- Rainfall was mostly below average for the inland east and centre, and above average for the east coast, northern Tasmania and parts of Western Australia."

The Intergovernmental Panel on Climate Change's (IPCC's) report released in April 2014, concludes that climate change is already damaging food production and increasing food prices, and will have further impacts in the future. This report raises fresh concerns for food security and farming, especially in tropical regions like South Asia and sub-Saharan Africa. The report indicates that crop yields in Asia and Africa could suffer an 8 percent decline by 2050 and yields from tropical fisheries could decrease by as much as 40 percent. Yet during this same period, demand for food is expected to be boosted as diets change and populations rise in the developing world.

Our research sought to assess the extent to which respondents saw climate change and natural disasters as a challenge to Australia's food supply. It also tested the extent to which respondents saw climate change, and its associated impacts, as having an impact on food security, their business and the food supply chain. The data shows that:

- overall, availability of water was identified as the greatest challenge to Australia's food supply by the majority of respondents. Some groups saw the challenges differently, with respondents in food retailing and hospitality seeing natural disasters as the greatest challenge;
- on climate change, the majority of respondents were concerned with the potential for climate change to negatively impact global food security, although only about a third of respondents saw it as a serious issue;
- furthermore, only half of respondents felt their organisation was not vulnerable to the adverse effects of climate change and only about 27% of respondents saw regulation around the environment and climate change as a concern - which is somewhat surprising given the debate over carbon cost pass through in the supply chain that existed at the time; and
- however, those in the financial and insurance sector had a high degree of concern over the impacts of climate change, largely we expect because of their exposure to the losses suffered in the Queensland cyclones and floods.

The results suggest that there is clearly a recognition of the role that climatic systems play in food security, although the degree of concern varies greatly depending on where respondents sit in the supply chain. While many respondents do not necessarily make any direct link between climate change and increasingly volatile weather events or natural disasters, there is little doubt that floods and drought and other natural disasters present a real challenge to food supply.

How the government manages this is a critical factor for the long term viability of Australian agriculture as the climate becomes increasingly challenging to deal with. The \$320 million drought relief package, announced in February this year, is a laudable move that is likely to be repeated more regularly according to the prevailing climate forecasts. In light of this, it would be prudent for the Australian government to have contingencies in place to fund ad hoc relief for when it is needed.

SUBMISSION #6

The government must overtly recognise the threat that climate change poses to Australian agriculture and take action to address it. In light of the increasing frequency of extreme weather events, resilience and redundancy needs to be built into Australia's food supply and related infrastructure (in particular, the supply of water). The Australian government should also ensure that adequate funding is available to fund disaster relief for producers affected by severe climatic events.

Regulation

Fig. 11 What is your opinion of the level of regulation in each of the following areas?

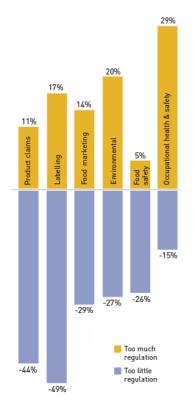
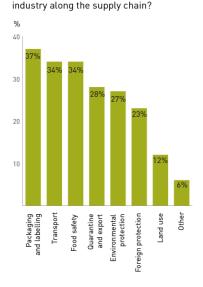


Fig. 12 Which of the following regulatory regimes impose the greatest burden on the food



Countries have long sought food control systems to ensure the health and safety of their domestic consumers. Regulation is seen as critical in ensuring the safety and quality of foods entering domestic food markets and that imported foods meet national standards.

Stakeholders at all levels of the food supply chain are taking an increasing interest in the way that food is produced, processed and marketed, and as suggested by data presented in this chapter, are increasingly calling for governments to accept greater responsibility for food safety and consumer protection.

Fig. 11 provides an overview of respondents' attitudes towards regulation of the food industry. Surprisingly, there was a general belief that there is too little regulation in some areas.

The only area where it was perceived that there is too much regulation is occupational health and safety. On the other hand, there was a belief that there is too little regulation surrounding marketing claims and food labelling.

However, the impact of having more regulations ensuring the safety of the food industry comes at a cost, which has an effect on decision-making along the supply chain. Fig. 12 shows the areas in which regulation poses the greatest cost. Transport (34%), food safety (34%) and packaging and labelling (37%) are the key areas where respondents said they believe regulatory regimes are imposing the greatest burden.

It is a surprising result that 37% of respondents considered packaging and labelling regulation as a high cost, yet under Fig. 11, 49% of respondents believed there is too little regulation. Perhaps the answer lies in the quality, as opposed to the quantity, of labelling regulation.

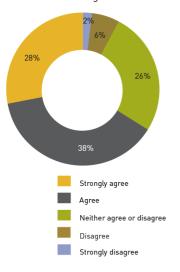
Parallel importing

The global nature of the modern food supply chain has far reaching implications. One consequence is that domestic retailers are venturing beyond their local supplier and sourcing goods from foreign markets at often significantly lower costs.

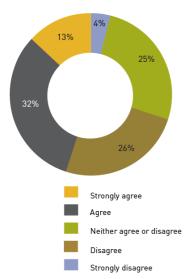
Parallel importers purchase products in one country at a price which is cheaper than the price at which it is sold in another country, import the product into the second country, and sell the product in that country at a price which is between the two prices. Due to the strong Australian dollar, parallel importing has increased in the Australian food retail sector.

On the surface, such importing provides a welcome method of keeping competition healthy and prices down in the food retail sector. However, there are valid concerns

Fig. 13 Do you agree that parallel importing should be better regulated?



Do you agree that parallel importing benefits consumers?



that in markets where large food retailers are already powerful, it skews the balance even further in their favour, and can also hurt domestic food and beverage production in countries where imports are cheap, such as Australia.

Whilst parallel importing happens for a variety of goods, it is a particularly crucial issue for the food industry due to the different food safety and quality standards applied in different jurisdictions.

Parallel imported food products may breach local labelling and food safety regulations when imported from suppliers in other jurisdictions, threatening the reputation of the manufacturer and the health of local consumers.

A recent example comes from the recall in South Australia of a parallel imported product that did not carry accurate allergen warnings. In New Zealand, a consumer recently complained that the Milo chocolate he purchased at a local retailer was made for the Philippines market and tasted significantly different.¹²

In 2010, Coles secured a deal with Foster's for Corona at a price "equivalent" to parallel imports. 13 Woolworths is also engaged in the practice, particularly for alcohol, selling brands like Johnnie Walker at significant discounts due to sourcing of parallel imports. 14

Our research asked the views of Australian food industry participants on parallel importing, specifically asking whether it was regulated sufficiently and whether it benefits consumers. Our results show a majority in favour of better parallel import regulation, with only 8% disagreeing. Some were particularly concerned about buyers being misled, and concerns about the buying power of Coles and Woolworths clearly continue to occupy the minds of respondents.

Fig. 13 and Fig. 14 taken together show the trade-offs that must be made when balancing the short-term price benefits to consumers versus the long term need to have a secure and affordable food supply. A majority of our respondents (66%) said they want better regulation around parallel importing, but at the same time, 45% of them believe parallel importing is beneficial to consumers.

Food labelling

Food labelling is designed to give the consumer useful data to make an informed choice on a food purchase. It can cover a wide variety of factors, such as nutritional value, country of origin, allergy advice, expiry date and ingredients.

In addition to mandatory labelling imposed by regulation, voluntary labelling is one of a food company's many marketing options, to highlight the products' attributes and to differentiate the product from the competition.

http://www.foodnavigator-asia.com/Markets/Parallel-imports-could- trip-Kiwi-food-companies

http://www.theage.com.au/business/retailers-rock-the-boat-with- parallel-imports-20100114-ma5h.html

http://www.theage.com.au/business/retailers-rock-the-boat-with- parallel-imports-20100114-ma5h.html

Fig. 15 How important is it for you that the following information be available on food labels?

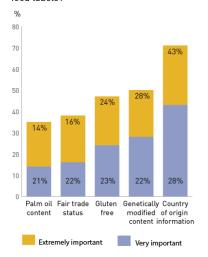


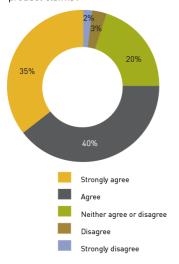
Fig. 15 shows the varying degrees of importance the industry places on various food labels. Results show that a significant proportion of respondents believe food labelling is important, and of these, the large majority of respondents (71%) believe that country of origin information is critical.

This result on country of origin labelling supports the contention that the current rules should be revisited again, notwithstanding that the Forum on Food Regulation (convening as the Australia New Zealand Food Regulation Ministerial Council) (Forum) rejected the reform recommendations of the panel of experts, led by Dr Neal Blewett, in its report Labelling Logic - Review of Food Labelling Law and Policy (2011) (Blewett Report).

Although The Australian Competition and Consumer Commission has very recently published new guidance to assist businesses in complying with the Australian Consumer Law (ACL) when making country of origin claims, it is the required content of those claims that is lacking. The current Australia New Zealand Food Standards Code for Country of Origin Labelling in Australia requires only general information about origin of food ingredients. In some cases, a descriptor such as "contains a mix of local and imported foods", or "contains a mix of imported foods" will be considered a sufficient disclosure to consumers. Furthermore, food for immediate consumption is exempt from the requirements altogether.

Looking at Fig. 16, the overwhelmingly strong support for having stronger rules and/or enforcement for the regulation of marketing claims (75%) is very surprising. As on the country of origin labelling issue, this seems to reflect a view that while there is a significant level of existing regulation, it is not particularly effective regulation in terms of clarity or enforcement so that the desired results of regulation in this area (certainly for industry, consumer confidence in claims and a level playing field for all competitors) are not being delivered.

Fig. 16 Do you agree that stronger rules and/or enforcement are necessary to regulate product claims?



SUBMISSION #7

Proposals for an overhaul of food labelling laws have been considered and debated for many years but nothing substantive has been done. It is time for decisive action to address what is an important issue that will benefit Australian agriculture.

Implementation of food label information needs to be widened and deepened, to include more effective information. There is overwhelming support for the provision of more detailed country of origin information on food labels, as well as stronger regulation of product claims.

A New Opportunity: Sustainable **Aviation Biofuels**

The Government should explore ways to support new industries that will create more opportunities for Agriculture especially in the areas of Bio-fuels and Sustainable Aviation Fuels and support other national objectives such as fuel security.

Agriculture and Energy presents a number of challenges and opportunities for the Australian aviation industry and there is now the ideal opportunity to develop a comprehensive and forward looking co-ordinated energy and agricultural policy on this issue.

Australia is uniquely positioned to benefit given Australia's landmass, a wellestablished agricultural sector and the large areas of non-arable or semi-arable land.

The development of an aviation biofuel industry would provide direct benefits to the Australian economy such as the creation of a new industry that will provide bring new job opportunities and investment, skills and vital stimulus to rural and regional economies. A 2011 study by the CSIRO, supported by the aviation sector, found that such an industry is feasible and, over the next 20 years, could generate more than 12,000 jobs and decrease greenhouse gas emissions by 17 per cent in the aviation sector.

It would also go some way in reversing the decline in Australian refining capacity, while supporting energy security by reducing reliance on imported crude oil and finished products.

If Australia is to seize this opportunity, carefully considered and coordinated policy across energy, agriculture and regional development will be needed. Such an approach would improve Australia's international competitiveness. Australia is already behind countries like the United States where targeted energy, agriculture and defence policy has helped facilitate a large and growing advanced biofuels industry and attracted significant investment. Due to these policy settings (including the Renewable Fuel Standard) over US\$5.79 billion in private capital has been invested in the United States in building an advanced and cellulosic biofuels industry. Furthermore, 28 out of 50 states now have at least one existing or planned biorefinery¹⁵.

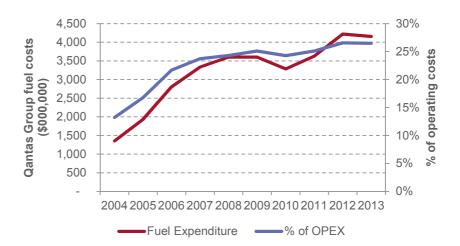
¹⁵ Biofuels Digest, Answers to your questions about the Renewable Fuel Standard, February 4, 2014.

Aviation Industry Challenges

The cost of fuel represents a key challenge facing airlines. With fuel prices close to record highs (as illustrated on the chart below), aviation fuel represents a major, and growing component an airline's cost base.



As a result of the significant increase in the price of oil, aviation fuel now represents the single largest operating cost for Australian airlines. In 2012/13 the Qantas Group spent \$4.1 billion on fuel, accounting for 26 per cent of operating costs. This compares to just 14 per cent of operating costs ten years ago. Fuel also represents 26% of operating costs for Virgin Australia.



The aviation industry has taken significant measures to reduce these costs largely through a strong focus on fuel efficiency. Over the past four decades aircraft fuel efficiency has improved 70%, with 23% taking place in the last 10 years¹⁶.

Typically, an airline's journey regarding fuel efficiency has targeted:

- Continued investments in new, fuel efficient aircraft such as the Boeing 787;
- A focus on fuel use management; and
- Partnering with airports and air navigation service providers to improve the efficiency of aviation infrastructure (including airspace).

However it's important to recognise that unlike other sectors of the economy, including other segments of the transport industry, airlines are subject to a set of unique limitations when addressing fuel management. Airlines are constrained by (1) a single primary source of energy (aviation fuel); (2) the capital intensity of aircraft; and (3) regulatory and infrastructure constraints that are outside the control of an airline, such as air traffic management.

Beyond fuel efficiency, the development and use of aviation biofuel is the only way in which the aviation industry can materially reduce emissions, address fuel costs and price volatility, while continuing to grow the industry. This is in stark contrast to land transport, which in addition to biofuels has a number of options to reduce emissions and address fuel costs (including hybrid-electric technology, electrification and alternative fuels such as LNG, LPG, CNG and hydrogen).

For this reason airlines are investing significant time and effort to understand and help facilitate the commercialisation of aviation biofuel production in Australia.

In 2012, Qantas announced, in partnership with Shell Australia, a feasibility study to understand the economic conditions under which an aviation biofuel industry in Australia could be viable, using existing supply chain and refining infrastructure.

The study, which was supported by a \$575,000 grant from the Australian Renewable Energy Agency (ARENA), was launched in November 2013 and represents the most detailed investigation to date regarding the commercial viability of the end-to-end aviation biofuel supply chain in Australia¹⁷. The study found that, while technically feasible, there are a number of challenges that need to be

¹⁶ Remarks at the World Business Summit on Climate Change in Copenhagen, Giovanni Bisignani, IATA CEO, 24 May 2009

¹⁷ The study assessed the commercial viability of a 3,000 tonnes-per-day reference facility, which would produce approximately 20,000 barrels of renewable hydrocarbons (diesel, SAF, naphtha and refinery gas) per day. Capital expenditure is approximately A\$1 billion (2012), which is consistent with industry cost values when considering that the construction of additional, as opposed to the conversion of existing, refining equipment is required in Australia. Depending on the process configuration and bio-refinery size, the aviation biofuel fraction was between 5% and 35% of Qantas' current domestic fuel demand when certified in a 50:50 blend. A copy of the study can be downloaded at

www.gantas.com.au/infodetail/about/environment/aviation-biofuel-report.pdf

addressed in order to make an aviation biofuel industry in Australia commercially viable. Of particular importance is the need to address feedstock volume and economics as well as supportive policies to help incentivise production of aviation biofuel.

Matters to Consider

In moving forward we would advocate consideration of the following:

The outcomes from the Qantas and Shell feasibility study highlight a number of key areas where the Australian Government has an opportunity and an important role to play in helping facilitate an aviation biofuels industry in Australia. Of particular importance is the role of production incentives and the impact of existing policies that support the production of biodiesel, renewable diesel and ethanol.

At present, producers and importers of biodiesel and renewable diesel are eligible for a grant of \$0.38 per litre under the Energy Grants (Cleaner Fuels) Scheme. Producers of ethanol are also eligible for a grant of \$0.38 per litre under the Ethanol Production Grant program. Both grants provide support for producers equal to the level of excise on biodiesel and ethanol and are scheduled to expire in 2021.

There is currently no such support or incentive for the production of aviation biofuel.

The policy settings as they stand provide a strong incentive for producers to target biodiesel or renewable diesel over aviation biofuel when making investment decisions. The modelling commissioned by Qantas and Shell, and conducted by SKM, illustrates the size of the incentive. The study found that:18

...the Cleaner Fuels Scheme increases the incentive to produce renewable diesel... This analysis shows that the NPV¹⁹ for a bio-refinery is improved by approximately \$1 billion with a grant to renewable diesel when the refinery is configured to produce maximum diesel. This provides a significant incentive for any supplier to maximise renewable diesel over SAF²⁰ when contemplating investment of capital...The Cleaner Fuels Scheme therefore reinforces a techno-economic tendency towards diesel, and thus away from SAF.21

This market distortion represents an important barrier that needs to be addressed if an aviation biofuel industry is to develop in Australia. We believe that a production grant of \$0.38 per litre for aviation biofuel would remove the distortion.

¹⁸ Qantas Airways, Shell Company of Australia (2013) Feasibility Study of Australian feedstock and production capacity to produce sustainable aviation fuel, pg. 8-65, figure 41.

¹⁹ Net Present Value

²⁰ SAF: Sustainable Aviation Fuel

²¹ Qantas Airways, Shell Company of Australia (2013) Feasibility Study of Australian feedstock and production capacity to produce sustainable aviation fuel, pg. 8-64

Despite aviation fuel not being subject to excise²², there is a case to extend a \$0.38 per litre production grant for aviation biofuel for the following reasons:

Excise relief represents forgone revenue and is ultimately a cost to government;

- In the absence of excise on aviation fuel, providing a grant of \$0.38 per litre is equally a cost to government; and
- From a whole-of-market perspective, the production of aviation biofuel competes
 for scarce feedstock with biodiesel and renewable diesel²³. Therefore a litre of
 aviation biofuel produced in Australia, will displace a litre of biodiesel or
 renewable diesel produced, mitigating the impact on the Federal Budget.
- For the purposes of investment certainty, it is important that any production grant provided for aviation biofuel extend well beyond 2021(when existing production grants for biodiesel and ethanol are due to expire).

While it is unlikely aviation biofuel will be produced in Australia within the next 3-5 years, providing a production grant for aviation biofuel will help attract investment and facilitate the planning and development of aviation biofuel projects in Australia. This will also provide new opportunities for Australian Agriculture and drive greater fuel security for Australia.

SUBMISSION #8

The Government should explore ways to support new industries that will create more opportunities for Agriculture especially in the areas of Bio-fuels and Sustainable Aviation Fuels that support other national objectives such as fuel security.

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²² Excluding the carbon price, aviation fuel is subject to \$0.03556 per liter levy, which is collected to fund the Civil Aviation Safety Authority.

²³ The same will hold true for ethanol once the alcohol-to-jet production pathway is certified by ASTM, which is expected in 2014.

Conclusion

Although private industry has a key role to play in maintaining food security, the role of governmental bodies is important in ensuring simplification and harmonisation of regulation, and a focussing of investment into key target areas.

Our findings suggest that governments and corporates can take specific action to address the challenges. Our respondents offer an interesting insight into what the key problems are and the most efficient, innovative and effective ways of dealing with them.

In our interconnected and globalised world, food security is a phenomenon which needs to be tackled by a co-ordinated group effort. Although private industry has a key role to play in maintaining food security, the role of governmental bodies is important in ensuring simplification and harmonisation of regulation, and a focussing of investment into key target areas.

Reforms or policy developments should be considered as a necessary prerequisite to address the following concerns of our respondents.

- A need to regulate a consolidated food retail market in Australia, including how suppliers and retailers interact.
- Enhanced investment in innovation and R&D from both the Government and private sector is needed to develop new technology and to improve agricultural productivity.
- There should be a national debate to address any ongoing concerns about GMOs. GM foods that have been assessed and considered safe should be implemented more widely to ensure the sustainability of the food supply and to meet environmental needs.
- There is a surprisingly high concern about foreign investment, coupled with an equally surprising willingness to move to more trade protectionism, to protect jobs, food quality and local industry.
- Implementation of food label information needs to be widened and deepened, to include more effective information. Country of origin information is cited as being particularly important.
- The Government should explore ways to support new industries that will create more opportunities for Agriculture especially in the areas of Bio-fuels and Sustainable Aviation Fuels and support other national objectives such as fuel security.

Specific actions, in policy and investment, in these areas are not just defensive plays. Food insecurity elsewhere in the world is a major opportunity for Australia's food and agribusiness sector to improve their own and Australia's profitability and productivity, but also to "do well by doing good" for the rest of the world.

For further information

Martijn Wilder AM Partner



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