CHS

CHS Trading Company Australia Pty Ltd
Suite 1, Level 29
126 Phillip St
Sydney, NSW, 2000

Date: 2nd September 2014

Ms Lyn Camilleri
Acting Deputy General Manager
Fuel, Transport and Prices Oversight Branch
Infrastructure & Transport-Access & Pricing
Infrastructure Regulation Division
Email:transport@accc.gov.au

Dear Ms Camilleri,

RE: Co-Operative Bulk Handling Limited's proposed 2014-17 Port Terminal Services Access Undertaking.

CHS Introduction

CHS Trading Company Australia Pty Ltd (CHS Australia) is a wholly owned subsidiary of CHS Inc, a US based grower owned Co-Operative and a Fortune 100 company. CHS Inc is a global energy, grain and foods business with grain origination businesses in all the major exporting origins in the global grain trade. CHS Australia first entered the Australia market in 2009, gained WEA Bulk Accreditation, and has been an active participant in Durum exports from the East Coast. In July 2013 CHS made a 50% acquisition of a grower accumulation business in Agfarm Pty Ltd. The main objective for the Australian business is to develop and build sustainable accumulation supply chain, from the farm gate to the domestic and global end user. The 2014/15 harvest will be CHS Australia's first Australian harvest, accumulating direct from the WA grower and executing through the CBH infrastructure into the export pathway.

Executive Summary

CHS Australia support the ACCC's draft decision on CBH's proposed 2014-17 undertaking published on the 26th June 2014, without the inclusion of the new proposed clause as per CBH's submission of the 22nd August 2014.

The LTA process without the clause has the ability to offer capacity via LTA's when there can be mutual independent agreement by the industry, it also offers the protection of a market based allocation method when this is not possible to achieve, which should provide equal access and true market signals.

The proposed clause completely changes the potential outcomes of the draft LTA and creates a restrictive barrier for new entrants and smaller entrants looking to grow market share.

Is the proposed allocation method appropriate? Does it balance the interests of the industry and efficiency of operation?

CHS Australia believe basing the allocation of LTA's on historical shipping capacity will make it difficult for new entrants and smaller participants to grow market share over the 3 year term of the LTA.

The term of the LTA's being for three years will ensure that the current consolidation that exists in the market share of WA exports will remain unchanged and perhaps even assist in further consolidation.

The level of demand that was displayed for the LTA capacity renders any discretionary process inequitable, leaving the only fair method a market based system like the auctions system.

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Balancing Interests of Industry Participants:
CHS Australia also considers the question of balancing the interest of the different participants. The first and foremost consideration should be the growers and ensuring there is sufficient competition at the farm gate. CHS Australia believes that the system as proposed does not assist the access of smaller or new companies. Therefore does not help to increase competition at the farm gate.

In regards to balancing efficiencies of operation for the facility, CHS Australia cannot comment directly how these operating costs may be influenced by the proposed allocation method. It would seem intuitive that the cost increases due to having more exporters involved in exporting the WA crop would be minimal. It would be reasonable to expect the benefits of increased competition at the farm gate would outweigh the additional costs to the operation of the supply chain facility.

Will smaller or new exporters have sufficient opportunity to obtain capacity via the auction system?
The smaller or newer entrants will be at a significant dis-advantage operating in the auction system. The different cost and risk structure of the LTA's will contribute to distorting the auction results.

CHS Australia believes that by allocating a larger percentage of LTA capacity to one sector of the trade will distort the auction results for the proposed 34% auction capacity. The proposed process will tip the balance in favour of the industry participants who receive a larger percentage of the LTA capacity.

It is clearly understood that the risks associated with capacity undertaken via the LTA process will be significantly lower than capacity undertaken in the auction. The financial risk of LTA capacity will be capped at $10/mt. This is made up of the booking fee of $4/mt and the lost capacity fee $6/mt. The financial risk of capacity taken up via auction will be the average auction premium plus the lost capacity fee. The auction premiums in recent years have been as high as $24/mt, in this case the financial risk of forfeiture for auction capacity would be $30/mt.

Now consider the possible scenario's:
Company A: Allocated 70% of their annual requirements via LTA, balance 30% via auction. Overall financial cost of forfeiture will be $A16/mt

Company B: Allocated 70% of their annual requirements via LTA, balance 30% via auction. Overall financial cost of forfeiture will be $A24/mt.

Therefore in seasons of low production, when exportable surplus of all commodities in WA falls below the supply of shipping capacity that has been purchased by the trade, Company A in the above example will have a lower cost of forfeiture, $8/mt in the above example(See below discussion on Shipping Slot Inverse)

It is worth pointing out that this example is conservative and could be higher and will be dictated by how high the auction premiums finish in the auction.

Having the auction in September will give the market a much better chance of determining the aggregate level of exportable surplus. This should reduce the shipping slot in- balances we have seen in recent years. (See below discussion on Shipping Slot Inverse)

However given there will be some sectors of the market potentially holding 70% of their requirements in LTA's, this could increase their risk appetite to purchase additional auction capacity which could still result in shipping slot inverses.

Company A will have an advantage in the auction system due to having a larger percentage of shipping capacity at a capped risk and financial exposure.

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Shipping Slot Inverse.
The conditions that cause shipping slot inverses is when exportable surplus of aggregate commodities falls below aggregate supply of shipping capacity, referred to as shipping slot inverse.

The only way a company can avoid these costs is to buy grain and ship against the shipping slot thereby receiving the auction premium back and avoiding the lost capacity fee.

Therefore in years when a shipping slot inverse occurs and as the price that can be achieved in the export market is set by factors of global supply and demand, the company will have an incentive to bid up the interior price above what can be achieved in the export market, to save as much of the auction premium plus the lost capacity fee as is commercially possible.

Therefore if the cost of forfeiture was $30/mt the interior price will invert above the value that can be achieved in the export market by approximately $25-30/mt.

From an industry perspective, in the short-run the grower is the winner, as they have received a price for their grain approximately $25-30/mt above the export value.

In the long run the grower could also be the loser, as they may experience reduced competition as exporters will be discouraged from participating in the WA exports due to highs levels of risk.

Causes of shipping slot inverse.
The main reason we have seen shipping slot inverses is due to holding the auctions in July when the levels of production are impossible to determine.

If the auctions were held in September the instances of shipping slot inverses would be significantly reduced. The auction premiums could be high as forecast by CBH in their "Status of Consultations pre and post lodgement of proposed undertaking with ACCC", however the likelihood of receiving them back through the rebate system should be increased, as the trade should have better visibility over the size of the crop.

Is the proposed draft clause sufficiently clear?
The proposed draft clause is very clear, however the major concern is that this specific clause changes the whole LTA process as previously promoted and as we have now seen the actual result. CHS Australia would not support the draft LTA process with the inclusion of this clause.

CHS Australia supported the draft LTA process in principle as there was still the protection of market based system when mutual independent discussions could not resolve the shipping windows that were oversubscribed.

CHS Australia liked the concept that CBH were allocating approximately the long term average production in LTA capacity. CHS Australia also liked the concept that the 34% would be offered via the auction system in September. A September auction for the balance would assist in reducing the instances of shipping slot inverse, which creates the price distortions we have seen in recent low production years.

CHS Australia viewed the draft LTA process as fair and equitable essentially it offered to provide a more mutually beneficial method of allocating capacity, if this was not possible then there was still the protection of a market based system.

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Summary

CHS Australia support the ACCC's draft decision on CBH's proposed 2014-17 undertaking published on the 26th June 2014, without the inclusion of the new proposed clause as per CBH's submission of the 22nd August 2014.

The LTA offers as they have currently been offered, essentially creates a two tiered access to the shipping capacity, putting those companies that received a lower percentage of LTA at a disadvantage.

An auction in September for the full capacity has the potential to provide the trade, as a collective, the most equitable means of access. Having a September auction, when forecasting the levels of exportable surplus will be more feasible, should reduce the risk of shipping slot inverses.

Yours Sincerely,

Jon Bucknall
General Manager Australia
CHS Trading Company Australia Pty Ltd