Submission

In response to the QCA’s invitation for further submissions in relation to the South Western, Western and Central Western systems

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GrainCorp
100 YEARS OF GROWTH

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1. Executive summary

GrainCorp welcomes the opportunity to comment in relation to the Queensland Rail (**QR**) declaration review currently being conducted by the Queensland Competition Authority (**QCA**).

GrainCorp is a major user of rail services in Queensland. We are reliant on access to QR's network for export of wheat and other grains from sites across Southern and Central Queensland, including sites connected to the South Western, Western and Central Western systems.

Declaration has supported strong investment and the growth of competition across grain supply chains in Queensland. The most recent example of this is the decision by Watco to enter above rail markets in Queensland in order to supply GrainCorp with rail haulage across the South Western, Western, Central Western and West Moreton / Metropolitan systems. The entry of an alternative, competitive, innovative operator is likely to support future investment into the Queensland grain supply chain and also other industries. In conjunction with its new haulage arrangements with Watco, GrainCorp is currently assessing business cases for proposed strategic investments in new sites and rail loading capability to achieve greater efficiencies to support the rail to port supply chain. This competitive entry and investment has been underpinned by a stable regulatory framework which provides certainty around the terms of access to below rail infrastructure.

For example, GrainCorp notes that access charges on the QR network are already significantly higher than in other states where GrainCorp operates, and that QR has only been prevented from further increasing access charges by QCA oversight. In its recent review of access arrangements for the West Moreton system, the QCA has reduced access charges by 24% from what was sought by QR. GrainCorp is therefore concerned that, in the absence of declaration, there is an increased likelihood of a material increase to access fees. As supply chain costs ultimately influence haulage prices paid by grain growers, Queensland farmers would face significantly higher costs, impacting the competitiveness of Queensland grain in international markets.

Given the benefits that have been delivered by declaration to date, GrainCorp would be concerned if declaration were to be removed in any part of the QR network. Declaration provides potential entrants with a degree of certainty around the future terms of access to below rail infrastructure, thus supporting long-term investments. In the absence of regulatory constraint, QR would be free to exercise monopoly power in ways that could undermine the value of long-term investments. Given the risk of "hold-up" in future negotiations, the removal of declaration would greatly undermine the business case for future investment. This is in turn likely to be damaging to competition across the supply chain.

More broadly, the removal of declaration would be damaging to the public interest. The terms and conditions of access to rail infrastructure (both below and above rail) have a significant impact on the costs that GrainCorp incur and ultimately on the costs that Queensland grain farmers bear in selling their products on internationally competitive grain markets. GrainCorp is concerned that the removal of declaration would lead to increased costs for both above rail access (due to a diminution of competition) and below rail access (due to the removal of regulation). The "double whammy" of increased above and below rail costs would ultimately be borne by Queensland farmers, and is likely to harm their ability to compete in international markets. This will ultimately be to the detriment of regional communities in Queensland.

Based on our commercial experience, GrainCorp is firmly of the view that declaration:

- has promoted entry by, and competition between, above rail operators for our business; and
- protects the supply chain from the inefficient implications of market power, including hold up risk.

For these reasons, GrainCorp submits that declaration should be maintained across the entire QR network, including the Central Western, Western and South Western systems, for a period that recognises the long-term nature of the investments of supply chain participants, preferably at least a further 20 years.

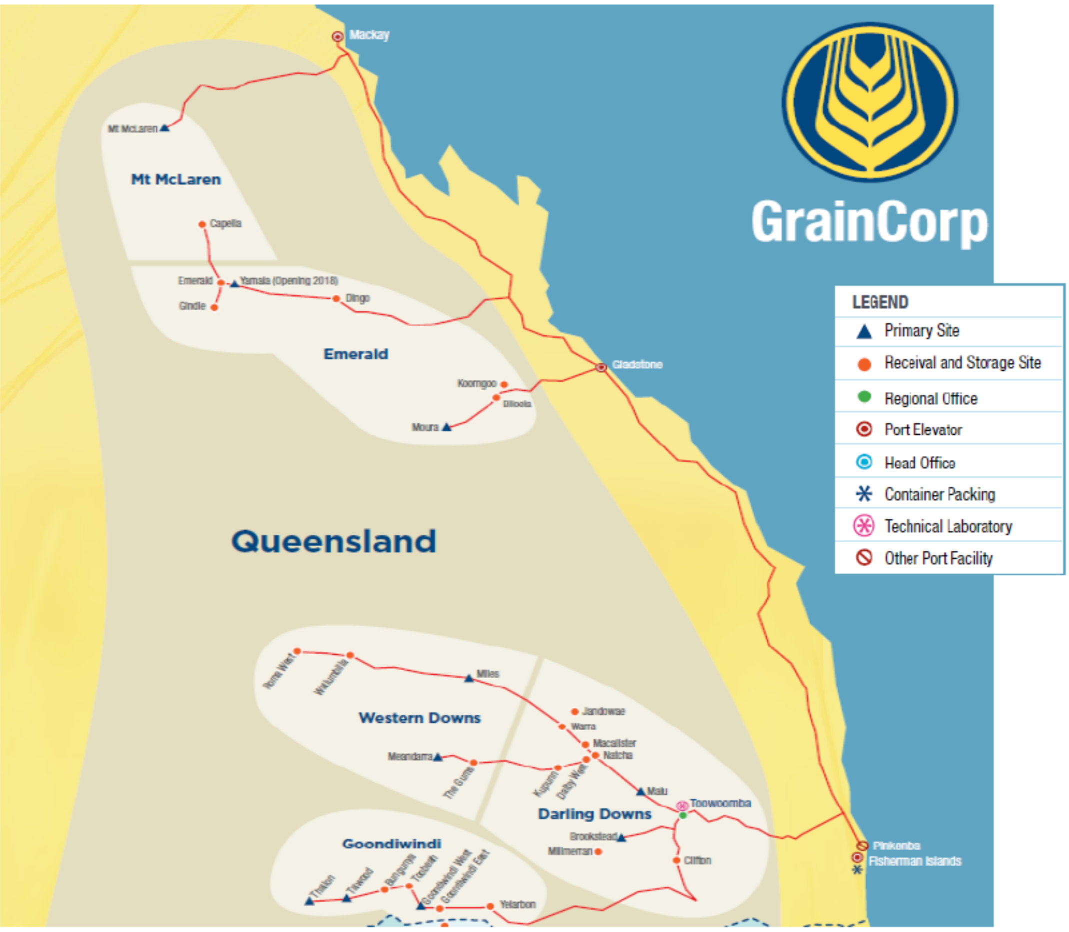
2. Background

2.1 GrainCorp's business in Queensland

GrainCorp is a leading international agribusiness with diversified operations that span four continents and supply customers in over 30 countries. GrainCorp operates the largest integrated grain supply chain in eastern Australia, linking up-country receival and storage sites to seven bulk export terminals.

In Queensland, GrainCorp exports grain through its Mackay, Gladstone and Brisbane (Fisherman Islands) terminals. GrainCorp relies on access to the QR network (including the South Western, Western, Central Western and West Moreton / Metropolitan systems), as well as parts of the Aurizon network, to link its up-country receival and storage facilities to these three export terminals. GrainCorp also transports some grain to these export terminals by road.

Figure 1: GrainCorp Queensland operations



Over the past decade, Queensland grain production has averaged approximately 3.5 million tonnes per annum (**mtpa**). Of this, around 44% is consumed in the domestic market, being for human consumption (flour etc) or for stockfeed and industrial uses. The remainder is exported.

Queensland exports are usually derived from stocks that are surplus to the domestic market or of higher value to the producer than the domestic market is willing to pay (such as high protein wheat destined for the Japanese noodle market). Exports are therefore quite variable, but on average around 2mtpa are exported out of Queensland. The sale of exported wheat and other grains on average generates revenue of around $600 million per annum for the Queensland economy.

GrainCorp accounts for [redacted] of Queensland's grain exports. Over the past 10 years the export task that has been generated out of GrainCorp up country storage sites and exported through the three GrainCorp terminals has ranged from [redacted]. The average GNC export task over the last 10 years was [redacted].

2.2 Reliance on rail access

As noted above, GrainCorp relies on access to the QR and Aurizon rail networks to transport grain to its export terminals. Grain for domestic consumption is not transported over these rail networks.

Due to constraints on road infrastructure at export terminals and loading sites, a significant portion of GrainCorp's grain exports must be transported by rail. While some grain exports can be transported by road, it would not be feasible or practical for GrainCorp to move all of its export volume by road, given these infrastructure constraints. Road transport is typically used to manage "peaking" demand, with rail providing baseload capacity.

Rail access charges make up a significant proportion of the total cost of operating grain trains. Any increase in access charges ultimately has an impact on the costs and returns for farmers on grain exports.

GrainCorp operate contracted trains throughout many rail networks in other states such as ARTC in NSW and Victoria, CRN in NSW, Sydney Metro, and VLine in Victoria. In GNC's experience, the cost of access across these networks is highly variable. [redacted] This is despite the fact that the QR network only allows for the operation of trains up to a 15.75t axle load, while other jurisdictions operate at a minimum of 19t axle load up to 25t axle load, and despite significant recent investment by track owners in NSW and Victoria in network upgrades.

[redacted] The grain trains that operate in NSW and Victoria also operate on a variable GTK charge basis with no take or pay component. This is an important consideration for GrainCorp as the seasonal and inter seasonal variability of grain freight task makes it cost prohibitive to pay fixed access charges.

2.3 Recent developments

GrainCorp currently uses Aurizon for rail haulage. However GrainCorp has recently engaged Watco to provide haulage for its Queensland grain exports from late 2019 onwards.

GrainCorp has committed to a new rail haulage provider on the basis that the new provider had received indicative access arrangements and access pricing that was similar to the current access arrangements in place (confirmed access arrangements could not be established until the above rail provider had established its rail accreditation). GrainCorp understands that at no time during [redacted] negotiations around access arrangements was Watco made aware that QR was seeking to have declaration of its below rail services withdrawn.

On the basis of the new haulage arrangements and the entry of Watco, both GrainCorp and Watco have committed to significant investment in above rail infrastructure and improvements in supply chain infrastructure. Watco will invest approximately [redacted] in new rolling stock and other above rail infrastructure, effectively underwriting this investment with its haulage contract with GrainCorp. As noted above, GrainCorp is currently assessing business cases for proposed strategic investments in the South Western, Western and Central Western systems in conjunction with its new haulage arrangements with Watco to achieve greater efficiencies. In respect of Queensland generally, GrainCorp has committed to significant financial investment in new and existing sites and rail loading capability. These investments will promote greater supply chain efficiency, including through use of longer trains and shorter cycling time. This will not only provide longevity to support grain on rail, but will also introduce an alternative, competitive, innovative operator into the QR market, which is likely to support future investment into not only the grain market but also other industries.

GrainCorp expects to increase its use of rail to transport grain to its export terminals as a result of the new rail contract and its investment in sites. The overall terms offered by Watco (including overall price terms) are considerably better than those under GrainCorp's existing contract with Aurizon, providing GrainCorp with an incentive to increase rail freight volumes. From 2020 onwards, GrainCorp is proposing to operate train services out of 17 strategically located storage sites. Eleven of those sites will be exposed to increases in access charges or other changes to access conditions if declaration were to be withdrawn in parts of the QR network, as contemplated in the Draft Recommendation. The sites in question are on the South Western corridor (Brookstead and Goondiwindi to Thallon), Western corridor (Miles to Roma including Meandarra) and Central West corridor (Capella). These sites represent [redacted] of the annual average task that GrainCorp expects to move by rail to port in Queensland.

3. Promotion of competition (criterion (a))

3.1 The effect of declaration on competition in above rail markets

The QCA notes in its Draft Recommendation that, historically, there has only been one above rail freight operator on the South Western, Western and Central Western systems, and that this operator has been subsidised to provide above rail freight services.[1] The QCA considers that subsidies for above rail freight services on the South Western, Western and Central Western systems are likely to continue even if the below rail services on these systems were not declared. It appears to be on this basis that the QCA concludes that, with or without declaration, above rail freight services would continue to be provided with the support of subsidies, and there would no material increase in competition in above rail markets if declaration were to be maintained.[2]

While subsidies may be provided for transportation of livestock, so far as GrainCorp is aware, no subsidies are provided for grain haulage. This means that there is real potential for growth in competition for grain haulage, including in the South Western, Western and Central Western systems. GrainCorp notes that the subsidisation of some freight tasks in parts of the QR network appears to be a key consideration for the QCA in its Draft Recommendation. GrainCorp therefore considers it important to clarify the extent of above rail subsidies and the implications of this for potential competition in grain haulage.

Recent experience demonstrates the potential for a material increase in competition for above rail services in the South Western, Western and Central Western systems. The recent decision by Watco to enter and supply services to GrainCorp in these systems demonstrates that, where declaration is in place to ensure that the terms and conditions of access to the below rail service are reasonable, this will promote new entry and competition in above rail markets. Watco notes in its submission to the QCA that "*the ability for new above rail entrant like Watco to enter the Queensland market is critically dependant on the stable operation of Queensland's regulatory framework under Part 5 of the QCA Act*".[3]

In this regard, the South Western, Western and Central Western systems are no different to other parts of the QR network. The fact that some level of subsidy is currently offered to the incumbent above rail operator for some freight tasks does not preclude new entry, nor does it mean that competition would not be promoted by ensuring that access to the below rail service is provided on reasonable terms.

Indeed, recent experience demonstrates the potential for declaration and effective regulation of below rail services to promote growth in above rail competition in the South Western, Western and Central Western systems.

3.2 Risks to above rail competition if declaration is removed

The QCA observes that, in other parts of the QR network, there would be a real risk of "hold-up" if declaration were to be removed. The QCA correctly concludes that, where there is a real risk of hold-up by an unregulated monopoly service provider, this will be damaging to competition in dependent markets, particularly above rail markets. The potential for exercise of monopoly power in future contracting periods creates significant uncertainty for potential market participants at the time they are considering investment, raising the hurdle rate required to justify the investment and potentially preventing efficient entry and efficient participation in the market.[4]

GrainCorp considers that the risk of hold-up would exist for potential entrants right across the QR network, including in the South Western, Western and Central Western systems. It is therefore similarly likely that the removal of declaration in the South Western, Western and Central Western systems would be damaging to competition in dependent markets, due to increased uncertainty for potential entrants around the future terms of access.

For example, if declaration were to be removed, Watco would face a very real risk of hold-up in future negotiations with QR. Watco is making very significant investments in rolling stock and other infrastructure to facilitate its entry into Queensland above rail markets. Much of this investment is likely to be sunk, as it cannot be redeployed elsewhere if Watco is forced to exit these markets (e.g. rolling stock will need to be designed to operate on the narrow gauge network). Moreover, most of these assets will have long lives (20 years or more) and will need to be utilised over long periods in order to deliver an appropriate return on investment. This creates a risk that, in the absence of declaration and effective regulatory oversight, QR would exploit its monopoly position by setting higher access prices or offering

[1] Draft Recommendation, p 70.

[2] Draft Recommendation, p 71.

[3] Watco submission, p 5. GrainCorp has had the benefit of reading a copy of Watco's submission to the QCA dated 8 May 2019.

[4] Draft Recommendation, p 48.

unfavourable terms of access in future negotiations. Watco is likely to have very little bargaining power in these future negotiations, given the sunk and long-lived nature of its investment in rolling stock.

GrainCorp itself is in a similar position to Watco. As noted above, GrainCorp is continuing to invest in rail loading / unloading capability and other complementary infrastructure to achieve greater efficiencies across the rail-to-port grain supply chain. Since GrainCorp, due to its access arrangements with Watco, will pay for access to below rail infrastructure, it is similarly at risk of hold-up by the monopoly service provider. GrainCorp's long-term investments to improve supply chain efficiency will only be justified if it can have certainty that, over the life of those investments, access to below rail infrastructure will be offered on reasonable terms. If there is a risk that the value of these investments may be expropriated through future increases in below rail access charges, this would greatly undermine the business case for investment.

GrainCorp is also concerned that, as well as increasing access charges, QR could unfairly preference other users at the expense of GrainCorp or the agricultural industry more broadly. Grain rail volumes are relatively volatile both on a seasonal and monthly basis. In the absence of declaration, QR may have the incentive and ability to give preference in the allocation of train paths to other potential users with a more stable task profile.

To date, investment decisions by GrainCorp, Watco and others have been supported by a stable regulatory framework which constrains the exercise of monopoly power by QR. However in a future without declaration, the risk of hold-up will create uncertainty for potential market participants at the time they are considering investment, potentially undermining the business case for such investment. This is likely to prevent efficient future entry and/or expansion by recent entrants such as Watco.

GrainCorp considers that the risks to future competition from removal of declaration arise in the same way in the South Western, Western and Central Western systems as they do in other parts of the QR network. Accordingly, the QCA can be satisfied that maintaining declaration of below rail services in the South Western, Western and Central Western systems would promote a material increase in competition, for essentially the same reasons as set out by the QCA in its Draft Recommendation for other systems such as the North Coast Line.[5]

3.3 Effect in other markets in which GrainCorp participates

GrainCorp considers that the removal of declaration in parts of the QR network could also distort competition in various markets in which GrainCorp operates, including markets for storage, containerisation and trading of grain.

Grain storage and handling facilities are currently located throughout southern and central Queensland. Some of these facilities are located in areas served by the South Western, Western and Central Western systems, while others are located in areas served by the West Moreton / Metropolitan systems or the Aurizon network. Any new facilities could potentially be located in areas served by any one of these rail systems.

If declaration is removed in parts of the QR network, this is likely to distort decisions around market entry and location of grain storage / handling facilities. Potential entrants may be discouraged from locating facilities in areas where the monopoly rail service provider is not subject to regulation. This would ultimately be damaging to competition in markets for storage, containerisation and trading of grain.

3.4 Relevance of competition between road and rail

In its response to the Draft Recommendation, QR argues that it is constrained by competition from road transport. QR submits that this provides end customers with significant countervailing power as the option of road transport means that they can raise a credible threat to withdraw from negotiations with QR or an above rail provider.[6]

At least insofar as grain freight is concerned, QR has overstated the extent of competition between road and rail transport. Although GrainCorp currently uses both road and rail to transport grain to ports, it is limited in its ability to switch volumes between these two modes of transport. GrainCorp views road and rail as complementary, rather than substitutable – in general, rail is used to provide 'baseload capacity' for grain transport, with road used to provide 'peaking capacity' in times of high demand.

The different roles played by road and rail transport can be seen in the pattern of freight volumes into Fisherman Islands in 2016/17. [redacted]

[5] Draft Recommendation, pp 45-53.

[6] QR submission in response to the Draft Recommendation, [139].

[redacted]

Key constraints on GrainCorp's ability to switch between road and rail include:

- **Road capacity limitations**. Due to road capacity limitations at key ports, GrainCorp needs to move a significant portion of its grain production by rail in order to maintain shipping volumes.
- **Investments in complementary infrastructure**. As noted above, GrainCorp has made significant investments in rail loading / unloading capability. These investments would effectively be stranded if GrainCorp were to switch all (or a significant portion of) its grain freight volumes from rail to road.
- **Road transport cost variability**. Road transport costs and capacity vary significantly from month-to-month depending on broader market conditions (i.e. supply and demand for road transport). This is particularly the case in high volume years where the road transport price can increase significantly due to greater demand for trucks. For example, [redacted]

Given these constraints on switching and the need for GrainCorp to keep a significant portion of its freight volume on rail, neither GrainCorp nor its above rail provider could credibly threaten to withdraw from negotiations with QR.

[redacted]

To the extent that there is scope for end customers to switch between rail and road, this does not appear to place any material constraint on QR's pricing. [redacted] – to the extent that there is greater competition from road in Queensland, this does not appear to have any impact on access pricing. There is also no evidence that QR seeks to compete with road operators for freight volumes, for example by offering price reductions. GrainCorp is not aware of any offer by QR to reduce access charges (or limit access charge increases) in order to maintain or increase freight volumes, where there is the potential for those volumes to switch to road.

Therefore in a future without declaration, competition (or potential competition) from road operators would not constrain QR, and would not mitigate the risk of hold-up in future negotiations around access to its below rail infrastructure.

3.5 Relevance of spare capacity

GrainCorp agrees with the QCA's conclusions regarding the relevance of spare capacity in parts of the QR network. As the QCA correctly observes, while QR may have an incentive to provide access to spare capacity (so long as it is profitable to do so), it will not have an incentive to provide access on reasonable terms and conditions.[7] Rather, as a monopoly service provider, QR may be expected to maximise its profit, which is likely to involve increasing access charges to users such as GrainCorp who rely on access to its infrastructure. Therefore, the risk of hold-up remains for potential entrants (or recent entrants wishing to expand their operations), notwithstanding spare capacity in parts of the network.

Industry experience in Western Australia is that, where parts of a rail network are underutilised and unprofitable, the network operator will not necessarily seek to offer access to the spare capacity on reasonable terms. Rather, in such circumstances, an unregulated access provider may simply shut down unprofitable parts of its network. GrainCorp would want to ensure that this cannot occur in Queensland, where access to the QR infrastructure is critical to offering farmers access to grain export markets.

[7] Draft Recommendation, p 46

3.6 The QR Deed Poll and Access Framework

QR claims that, under its Deed Poll and Access Framework, "there can be no difference in the consequences for competition in dependent markets" because its ability to exercise market power would not be "materially different", compared to the current situation where it is subject to the 2016 Access Undertaking.[8] It is also claimed that the Access Framework would provide "as much regulatory certainty for access seekers and access holders as currently exists".[9]

GrainCorp considers that an access framework administered by QR simply cannot provide as much regulatory certainty as declaration under the QCA Act and proper oversight by an independent regulator. Regulatory certainty cannot be maintained in a world where the regulator is sidelined and administration of the access framework is left to the monopoly service provider.

GrainCorp would be particularly concerned if access to the dispute resolution mechanisms in Part 5 of the QCA Act were to be foreclosed. With declaration, access seekers can have confidence that any disputes with QR will be resolved efficiently by an independent expert regulator with a track record in dealing with complex access matters. Under the QR Access Framework, recourse to the QCA would be lost, and access seekers would have to rely on a much more uncertain arbitration process.[10]

The process for amendments to the Access Framework is similarly problematic. Under the Deed Poll, QR may amend the Access Framework over time, provided that such amendments are consistent with the broad Framework Objective and "appropriate" having regard to various considerations, and subject to consultation.[11] If an access seeker wishes to challenge amendments to the Access Framework, the only way to do this would be through costly (and potentially drawn out) legal proceedings. This may be contrasted with the declaration scenario, in which any changes to QR's access undertakings must be approved by the QCA.

The broad scope for QR to amend its Access Framework over time creates a high degree of uncertainty for access seekers, potential access seekers, and their customers who ultimately pay access charges. Given the absence of regulatory oversight around any changes to the Access Framework, users (and potential users) can have no certainty that the future terms of access will be reasonable.

Even as submitted by QR (and without any amendment), the Deed Poll and Access Framework provide no long-term certainty for network users or potential users. The Deed Poll has an initial term of just five years, at which point QR may elect to either renew or not renew its commitments.[12] This provides little certainty for users needing to make long term (20 years plus) investments in complementary supply chain infrastructure.

Finally, GrainCorp would be concerned if access obligations did not survive any change of ownership of the QR assets. Currently, declaration applies to the services supplied by means of the railway infrastructure for which QR Limited, or a successor, assign or subsidiary of QR Limited, is the railway manager.[13] However it is not clear that the Deed Poll obligations would similarly apply to any successor, assign or subsidiary of QR, including in the event of privatisation. GrainCorp notes that, where privatisation occurred in Western Australia without clear access obligations being imposed on the new owners, this led to lack of investment and the ultimate closure of rail lines, resulting in increased costs to farmers.[14]

3.7 Conclusion

The recent decision by Watco to enter above rail markets in southern and central Queensland demonstrates the potential for declaration to support the growth of competition. Watco's entry has been underpinned by a stable regulatory framework.

The removal of declaration in parts of the QR network would risk forestalling future entry and expansion by recent entrants, since there would be much greater uncertainty around the future terms of access to below rail infrastructure.

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[8] QR submission in response to the Draft Recommendation, [17].

[9] QR submission in response to the Draft Recommendation, [16].

[10] Access Framework, cl 6.1.

[11] Deed Poll, cl 6.

[12] Deed Poll, cl 5.

[13] QCA Act, s 250.

[14] Details of line closures in the WA wheat belt are set out in in the report of the WA parliamentary inquiry into the management of Western Australia's Freight Rail Network (October 2014).

The risks to future competition are not alleviated by the availability of road transport for some freight tasks, nor is the QR Access Framework a substitute for effective regulatory oversight.

4. Natural monopoly (criterion (b))

It does not appear to be controversial that the QR network (including the South Western, Western and Central Western systems) is a natural monopoly facility. It can clearly meet foreseeable demand in the market for below rail services at the least cost compared to any two or more facilities. Indeed, QR notes that it has spare capacity on many parts of its network, meaning that if demand for below rail services were to increase over the declaration period, it could still meet this demand without any need for expansion.

GrainCorp supports the conclusions of the QCA in the Draft Recommendation in relation to criterion (b).

5. State significance (criterion (c))

The QCA considers that each of the South Western, Western and Central Western systems are significant in terms of their size, but not in terms of their importance to the Queensland economy. However in drawing this conclusion, the QCA notes that it did not have access to data on the volumes of freight carried on these systems.[15]

GrainCorp notes that criterion (c) will be satisfied if the facility is significant having regard to its size **or** its importance to the Queensland economy.[16] Therefore it is not strictly necessary to demonstrate that the QR network (and each of its systems) is significant both in terms of its size **and** its economic significance. The QCA correctly observes that it can be satisfied on criterion (c) based on the size of the QR network alone.

GrainCorp therefore agrees with the QCA that the QR network (including each of its systems) can be regarded significant having regard to its size alone.

GrainCorp strongly disagrees with the submissions made by QR regarding interpretation of criterion (c) and its application to each of the South Western, Western and Central Western systems.[17] QR conflates size and economic significance, which are clearly separate considerations under the QCA Act. In this way, QR adopts an interpretation which is manifestly at odds with the plain and ordinary meaning of the statute.

GrainCorp also considers it inappropriate for the QR network to be 'carved up' for the purposes of considering its size or economic significance. The QCA correctly observes that "the facility for the service" is the rail transport infrastructure for which QR is the railway manager[18] – i.e. the network as a whole. The QCA notes that **together**, the eight systems form the facility for the service.[19] Therefore the question under criterion (c) is whether the network as a whole is significant, having regard to its size or its importance to the Queensland economy. The question is not whether each component part of this facility is individually significant, as QR's submission appears to suggest. Such an approach, taken to an extreme, would allow a facility to be carved up into component parts that potentially fall below the significance threshold.

In any event, GrainCorp considers that each of the systems (and the network as a whole) is significant, having regard to both their size **and** their importance to the Queensland economy. As noted above, GrainCorp relies heavily on access to the South Western, Western and Central Western systems for transport of grain to export facilities. Grain export volumes vary from year to year depending on weather and market conditions, but on average around 2 million tonnes per annum are exported out of Queensland, with approximately 40% of this transported by rail to export facilities. The sale of exported wheat and other grains generates revenue of around $600 million per annum for the Queensland economy. As noted above, a significant proportion of grain exports must be carried by rail, given road capacity constraints. The QR facilities are therefore critical to the ongoing viability of this very important and economically significant export industry.

[15] Draft Recommendation, pp 88-91.

[16] QCA Act, s 76.

[17] QR submission in response to the Draft Recommendation, [279]-[284].

[18] Draft Recommendation, p 14.

[19] Draft Recommendation, p 14.

6. The public interest (criterion (d))

GrainCorp does not support QR's position that access to services on the Central Western, Western and South Western systems on reasonable terms as a result of declaration would not promote the public interest. GrainCorp considers that, in light of the significance of grain exports alone to the Queensland economy, and the importance of securing reasonable terms of access to below rail infrastructure for grain farmers, declaration would clearly promote the public interest.

6.1 Effect of declaration on investment

Declaration of services in the South Western, Western and Central Western systems has facilitated significant investment in complementary infrastructure. Continued declaration would promote the public interest by providing long term certainty that access will be available on reasonable terms, thereby facilitating further investment in the supply chains which rely on these systems. Increased certainty would make the market more attractive to potential entrants, leading to more efficient investment and service delivery, the flow-on economic benefits of which will be seen in the regions the systems reach.

Recent experience has demonstrated how a stable regulatory framework for below rail access can support investment across grain supply chains. In 2019, Watco secured the GrainCorp Queensland export rail freight services contract, a long-term contract to transport approximately 1 mtpa of bulk grain for GrainCorp in Queensland.[20] Watco has committed to investing $50 million in new rollingstock and facilities to support its operations on the Central Western, Western and South Western systems in fulfilment of its contract with GrainCorp. This includes the purchase of 8 locomotives and new wagons that are expected to be delivered in late 2019[21] and a new facility at the Warwick Railyard in the South Western system which will create up to 20 jobs in locomotive operations and maintenance in its initial stages.[22] In conjunction with Watco's investment, GrainCorp is currently assessing business cases for proposed strategic investments in the South Western, Western and Central Western systems to achieve greater efficiencies. In respect of Queensland generally, GrainCorp has committed to significant financial investment in new and existing sites and rail loading capabilities to achieve greater efficiencies across the rail to port supply chain. These investments will provide a significant boost to the regional economies that the systems reach.

Declaration is critical for realisation of the public benefits that Watco and GrainCorp's investments will bring. These investments in the South Western, Western and Central Western systems are underpinned by the indicative access arrangements and pricing offered by QR, based on the existing regulatory framework. If declaration were to be withdrawn, Watco and GrainCorp's investments will be put at risk due to the uncertainty introduced by potential changes to the future terms of access. In the absence of declaration, Watco and other potential investors in the dependent above rail haulage market will face a high degree of uncertainty, making rail access a major supply chain cost risk, potentially inhibiting future investment.

6.2 Importance to Queensland grain exports

Queensland grain exports are dependent on access to below rail infrastructure on reasonable terms. As explained above, a significant proportion of grain exports must be carried by rail, given road capacity constraints. The terms of access to essential rail infrastructure directly impacts on the profitability of grain exports and returns to farmers.

Over the past decade, Queensland grain production has averaged around 3.5 million tonnes per annum (**mtpa**). Of this, around 44% remains in the domestic market, while the remainder is exported. On average, the sale of exported grains generates annual revenue of approximately $600 million for the Queensland economy.

GrainCorp's export volumes through its Port of Brisbane (Fisherman Islands) terminal are shown in [redacted] below. Volumes exported through Fisherman Islands reflect approximately [redacted] of GrainCorp's total grain exports in Queensland, and [redacted] of total Queensland grain export volumes.

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[20] 'Watco expands Australian rail freight operations', *Rail Journal* (3 July 2018), available at: https://www.railjournal.com/regions/australia-nz/watco-expands-australian-rail-freight-operations/.

[21] Watco, *Watco signs agreement to move Eastern Australian grain*, The Dispatch – Watco Newsletter (July 2018), available at: http://www.watcocompanies.com/pdfs/Dispatch2018/07July2018Web.pdf.

[22] Southern Downs Council, *Major rail services company Watco invests in Southern Downs*, (20 September 2018), available at: https://www.sdrc qld.gov.au/council/alerts-news-notices/2018-news/major-rail-service-company-watco-invests-in-southern-downs.

[redacted]

Export grain stock is typically derived from domestic surplus stock or stock of higher value to the producer than the domestic market is willing to pay, such as high protein wheat destined for the Japanese noodle market. As such, export volumes are variable: the range of export volumes through the three GrainCorp terminals in Queensland has ranged from [redacted] This volatility can be seen in the pattern of exports from Fisherman Islands, as shown in [redacted] above.

Access to rail infrastructure on reasonable terms both ensures that farmers can obtain the best price for grain exports and minimises supply chain costs. Queensland grain-growers' ability to meet market demands is critical for maximising the value of available stocks and therefore ability to pay the grower the most competitive price. If access is not available (or is not available on reasonable terms), this can create a bottleneck for grain exports, potentially restricting farmers' ability to meet market demand. If market demands cannot be met efficiently, stock must be held until another delivery period, in which case carry costs are incurred and the next delivery period may not fetch as competitive a price (for example, from June onwards Australian grain must compete with northern hemisphere grain supplies, and therefore prices typically fall in the second half of the year). Increases in grain prices in the export market positively affect returns for farmers.[23]

Moreover, supply chain costs are the single largest cost for grain producers (farmers). Cost effective rail transport, being fast and unconstrained by the bottleneck issues of road transport, would therefore have the direct public benefit of enabling grain-growers to meet export market demand and maximise their returns.

6.3 Public benefit associated with transporting grain by rail

To the extent that GrainCorp has some flexibility to choose between road and rail for grain transport, ensuring that the terms of access to rail infrastructure are reasonable will ensure that volumes are not inefficiently diverted from rail to road.

GrainCorp considers that greater use of rail transport would have a number of public benefits, including:

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[23] Ibisworld, *Ibisworld Industry Report A0149: Grain Growing in Australia* (March 2019), p 5.

- it reduces the risk of accidents and road congestion (it is estimated that road transport produces 14 times greater accident costs than rail); and
- it reduces fuel usage and is therefore more environmentally sustainable. GrainCorp estimates that road transport uses almost 250% more fuel than rail over a similar distance. [redacted]

With the recent entry of Watco and enhanced competition for above rail services, GrainCorp intends to increase its use of rail for transport of grain to its export facilities. As noted above, Watco has offered considerably better overall terms (including better overall price terms) and an improved service offering, providing GrainCorp with an incentive to increase rail freight volumes. This shift to greater use of rail will provide the Queensland economy and community with many significant benefits including:

- safer and less congested roads, with an estimated 3,750 less trucks movements on the road compared to today;
- reduced road maintenance costs;
- reduced fuel emissions; and
- reduced transport costs, which will result in higher farmgate prices for farmers and regional communities.

These public benefits are directly attributable to recent emergence of competition in the supply of above rail services in the Central Western, Western and South Western systems, which has been underpinned by a stable regulatory framework for below rail access.

6.4 Administrative and compliance costs

GrainCorp supports the QCA's conclusion that the administrative and compliance costs that would be incurred by QR if services on the Central Western, Western and South Western systems are declared would be relatively minor for the following reasons:[24]

- the QCA levy does not apply to the Central Western, Western and South Western systems;
- ongoing compliance and administration needs of the QCA from QR in relation to these systems are minimal;
- concerns regarding the viability of above rail services on these systems in the absence of Government subsidies are unfounded, as GrainCorp understands that existing subsidies only apply to transport of livestock. The South Western system primarily transports grain and therefore haulage on this system is largely not reliant on subsidies. Haulage on the Western and Central Western systems is only partially reliant on subsidies as they facilitate some livestock transport but also grain, containerised freight and passenger services.

In any case, GrainCorp submits any administrative and compliance costs are far outweighed by the considerable benefits of declaration, as outlined above.

7. Conclusion

GrainCorp's experience demonstrates the clear benefits of declaration, in terms of creating conditions for competition and investment in dependent markets. The existence of a stable regulatory framework has facilitated the entry of Watco to support GrainCorp's rail freight requirements across the South Western, Western and Central Western systems. This increased competition for above rail services will promote greater efficiency across grain supply chains in southern and central Queensland, and will support ongoing investment by GrainCorp in supply chain infrastructure. Increased competition and supply chain investment will ultimately benefit Queensland grain farmers and the Queensland economy more broadly.

[24] Draft Recommendation, section 5.8.2.

GrainCorp is concerned that, if declaration were to be removed, users of the Queensland network (and their customers) would face considerable uncertainty around the future terms of access, due to the risk of hold up by an unregulated monopoly service provider. This uncertainty could forestall further entry and would therefore be damaging to future competition and investment across grain supply chains.

GrainCorp therefore submits that the QCA should recommend declaration of services across the entire QR network for a period that recognises the long-term nature of the investments of other supply chain participants, and preferably a further 20 years.

8. Contact information

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