

REPORT OF PROCEEDINGS BEFORE

STANDING COMMITTEE ON STATE DEVELOPMENT

INQUIRY INTO THE WINE GRAPE MARKET AND PRICES

UNCORRECTED PROOF

At Sydney on Wednesday 13 October 2010

The Committee met at 10.00 a.m.

PRESENT

The Hon. A. Catanzariti (Chair)

The Hon. R. H. Colless
The Hon. S. Cotsis
Reverend the Hon. F. J. Nile
The Hon. M. S. Veitch

CHAIR: Welcome to all of you. Before commencing I need to make a couple of statements. Welcome to the first public meeting of the State Development Committee inquiry into the wine grape market and prices. The inquiry's terms of reference require the Committee to inquire into and report on matters associated with the wine grape market and prices in New South Wales. As such, this inquiry is an opportunity for stakeholders to provide evidence about factors affecting supply and demand for grapes. The Committee will also examine the role of the Wine Grapes Marketing Board, the potential for collecting, bargaining and codes of conduct and whether there are any measures that could improve market signals which would be consistent with competition principles and legislation.

Today we will be hearing from Mr Lawrie Stanford from the Wine Grape Growers Association, Mr Mark McKenzie, Executive Director of the Murray Valley Wine Growers Association, Mr Scott Davenport and Mr Stewart Webster from the Department of Industry and Investment, and Mr Bligh Grant, associate lecturer in the faculty of business at the University of Southern Queensland. Tomorrow the Committee will be holding hearings in Griffith to hear firsthand from wine grape growers and people involved in the wine grape industry in the Riverina.

I would like to make some comments about certain aspects of the hearing. Committee hearings are not intended to provide a forum for people to make adverse reflections about specific individuals. The protection afforded to Committee witnesses under parliamentary privilege should not be abused during the hearings. Therefore, I request that witnesses avoid the mention of individuals unless it is essential to address the terms of reference.

The Committee has previously resolved to authorise the media to broadcast sound and video excerpts of its public proceedings. Copies of guidelines covering the broadcast of proceedings are available from the table by the door. In accordance with the guidelines, members of the Committee and witnesses may be filmed or recorded, however, people in the public gallery should not be the primary focus of any filming or photographs. In reporting the proceedings of the committee the media must take responsibility for what they publish or what interpretation is placed on anything that is said before the Committee.

Witnesses, members and their staff are advised that any messages should be delivered through the attendants or the Committee clerks. I also advise that under the standing orders of the Legislative Council any documents presented to the Committee that have not yet been tabled in Parliament may not, except with the permission of the Committee, be disclosed or published by any member of such Committee or by any other person. Please turn off your mobile phones for the duration of the hearings, including mobile phones on silent mode. Again I welcome our first witness, Mr Lawrie Stanford.

LAWRENCE JOHN STANFORD, Executive Director, Wine Grape Growers Australia, sworn and examined:

CHAIR: Are you conversant with the terms of reference of this inquiry?

Mr STANFORD: Yes, I am.

CHAIR: If you should consider at any stage that certain evidence you wish to give or documents you may wish to tender should be heard or seen only by the Committee, please indicate that fact and the Committee will consider your request. Would you like to start by making a short statement?

Mr STANFORD: Yes. I might just sum up what my main points would be. First of all, I will give you some context about me. I have worked in the Australian wine industry directly since 1997. I worked for 12 years as the Manager of Information and Analysis with the Australian Wine and Brandy Corporation, and since July this year I have taken up the position of Executive Director of Wine Grape Growers Australia. Wine Grape Growers Australia is the national voice of wine grape growers. It has had a turbulent history as an organisation and reformed from a previous form four to five years ago. I took up the position in July of Mr Mark McKenzie, who proceeded to go to Murray Valley and who is the witness following me. He also has considerable knowledge that I am able to impart and in some areas he would be more expert than I, given I have been in this role since July. Nevertheless, I have a long background in the industry and I have come to be very familiar with the nature of the supply and demand situation given my previous job.

The framework of what I would like to say to the Committee largely centres around three of your terms of reference, with that of price formation, including factors affecting supply and demand; the potential for collective bargaining and/or codes of conduct to contribute to an efficient market; and whether there are any measures which could improve market signals which would be consistent with competition principles and law. In terms of price formation and the role of supply and demand, I would make a strong point that the primary source of grief in the industry at the moment is the supply and demand situation. The industry is significantly oversupplied and in a free market situation that creates a very unfavourable environment for which wine grape growers are at the bottom of the pecking order. The belief is that the market will sort it and nothing needs to be done, but on two counts I would say there needs to be consideration of intervention. One is a case I would make for market failure particularly in respect to coastal temperate production, which is all of the production outside of areas like the Riverina, compared to warm inland production—the Riverina, Murray Valley and Riverland in South Australia.

The second reason I see a need for some consideration of intervention is the fact that markets do not always deliver social expectations, and that is why economists do not run the country, politicians do, and economists advise politicians—so, welcome to you all—and there are certain community expectations about ethical commercial behaviour and we see a clear instance in the negotiation of market prices for wine grapes for that to occur. The terms of reference talk about collective bargaining and codes of conduct. Wine Grape Growers Australia is very much involved in the code of conduct and I have some views on that. There are also minimal contract conditions that we would talk about being required, namely, written contracts, notifying of the price or a method of determining price and terms of payment.

The code of conduct that the industry is negotiating, a voluntary code of conduct, deals with these things. But I would have to say that while the code of conduct has not fully gone through the development process it is certainly not being adopted at the rate we hoped it would be and therefore the question of mandatory codes of conduct comes to the fore. In terms of looking at the basics of ethical commercial contracts, we see a place for legislation also. For various reasons both legislation and codes of conduct do not completely encompass all of the circumstances under which the terms of trade for wine grapes can be finalised. We also see a strong need to boost the capacity of wine grape growers to negotiate their contracts, to know what their contract is and to be effective dispute resolvers.

It is a fact that even in an ideal world, with all of those things in place—legislation, codes of conduct and even with ethical commercial behaviour—the best economic outcome for contracting is to get a contract for about five years. Given the lead time for wine grape production, sale and profitability of new plantings, it would be doubtful you could recoup your return on wine grapes in that time. Therefore, beyond even the ideal situation where you have a five-year contract that is ideal, growers need to be capable of managing their own business affairs and that education capacity is important and it is something that Wine Grape Growers Australia has an involvement in through programs like Winebiz.

We see the ways to improve the market signals and the operation of the market to be three in total. That is, to improve market clearing mechanisms by dealing with a market failure that I have mentioned, to regulate for ethical and/or minimal contracting arrangements and to build grower capacity for independence, resilience and flexibility. We would suggest to the Committee as things that are required to assist the industry to understand these adjustment needs so we can correct the supply and demand signals, that for the moment you monitor our attempts to set up a voluntary code of conduct because we are in the process of trying to make that effective, and although we are having doubts about it I think it needs to play out before we call for mandatory codes of conduct. We would appeal to the Committee to consider legislating certain aspects of wine grape commercial exchange. One prime example is terms of payment, where we would point to the arrangements in South Australia that are quite effective in that respect, and also to build into our voluntary code of conduct as an expectation.

We see a need for education and business development amongst grape growers and in order for my organisation to be effective in assisting with the industry to put in place all of these sorts of objectives, we as an organisation probably need some consideration and assistance to pull together resources to represent our membership. So, that would be a summary of what I said. I do not usually write clearly, so hopefully that makes what I wrote a little clearer for you. I am happy to take any questions.

CHAIR: With regard to the code of conduct that you suggested, and the voluntary code of conduct—I know you are working on this and you think it is too early to make it mandatory—what do you see as coming out of there at the moment that you think would be a proper mandatory situation for that code of conduct?

Mr STANFORD: We are not considering a mandatory code at this stage. We are working on it being a voluntary code that works. Whilst there are quite a few examples of voluntary codes that have in the end moved to mandatory codes because they have not worked, we have also had related to us as a management committee for our code, instances where they have worked. We are still working on it being a voluntary code that works; however, the situation is that all of the members of Wine Grape Growers are signatories by default to the code and at the moment there are only about six winemakers that are signatories to the code. As an organisation the Winemakers' Federation has supported the code and it therefore is a conundrum that only six of its members have signed up to it. But in the next steps the Winemakers' Federation is considering a review and modification of the code to make it more acceptable and they have undertaken to promote it to their members in a more active way.

However, I make the point in my submission that basically a resourcing formula that I work on is that we have very modest funds available to us to represent our members. To run an office takes up a very large part—something like 80 per cent—of the funds we have and, of the remaining 20 per cent, about 15 per cent is taken up in administering this code that is basically not working at the moment. Of my discretionary funds I have very few funds left after the code and if it does not become more successful very soon we will simply be moving to the idea that we should have a mandatory code.

CHAIR: Your submission referred to oversupply as a primary driver of unsustainable wine grape prices. What other factors influence prices in wine grapes and marketing at present?

Mr STANFORD: Basically the industry is a free market. If other factors were to be looked at, one is market opportunity. For example, our two major overseas markets at the moment are the United Kingdom and the United States and both of those markets have been significantly affected by the global financial crisis, so consumers have traded down. At the end of the day, what that means is that winemakers are struggling to make margins themselves in a highly competitive market that has been affected by the financial crisis, so there is a demand side imperative there that makes it difficult for everybody. That is a supply and demand factor, of course. The industry is dominated by four majors and in any supply and demand situation they are going to be maximising profits.

Each year in price discovery an important process is played out whereby those four majors are the main price setters in the market, and they of course will be reluctant to reveal to their competitors what their pricing situation is, so the price discovery process means that there is an incentive to announce prices very late in the process. Unfortunately, for wine grape growers, in that situation they take all the risk. Clearly to grow a crop and to find out only at the end of that growing period, having spent money to grow it, what your prices are means that you absorb all of the risk and we would support any move to announce prices by the companies

much earlier in the season before they make management decisions for their vineyards. It leads to a very high-risk factor for growers.

The Hon. RICK COLLESS: In the first recommendation you refer to the issue of stickiness of coastal temperate oversupply.

Mr STANFORD: Yes.

The Hon. RICK COLLESS: Could you explain what you mean by that?

Mr STANFORD: It is easily demonstrated that coastal temperate production—and, just for definition, coastal temperate is by definition anything outside of warm inland—is well in oversupply compared to warm inland. In fact during all of the last 10 years when people talk about oversupply in the Australian wine industry, they are effectively talking about coastal temperate oversupply and for many of those years warm inland production was under-supplied. That was a nuance that probably was not understood widely. What was happening was that coastal temperate producers were selling their fruit down into the shortage that existed in the warm inland areas, but in order for their grapes to go into what is traditionally warm inland product, which sells at lower prices, we have always thought they could not be doing that sustainably. The question always was: Why is it that people would produce grapes in the coastal temperate areas and sell at a loss, and why is it that they never adjusted and in the current circumstances are not adjusting? For that reason we see their oversupply as sticky. For some reason it is not adjusting where logically it should have been for many, many years now.

The Hon. RICK COLLESS: So you are suggesting that the price in those areas should have in fact gone down quite dramatically?

Mr STANFORD: Absolutely, but it does not—although they must have been selling at a loss into warm inland product. Every day I think of a new reason why this might happen. But the problem that the industry has is that it really does not understand which of the multiple reasons why this phenomenon might be happening is occurring—which ones are more significant than others—and until we do understand that as an industry all of our efforts to assist the adjustment process are going to be unfocused and untargeted, so I am arguing that we do need to understand what the reasons are for this because we face the very real prospect that coastal temperate overproduction will push out warm inland production. It will continue to exist, but it is likely that it will be unprofitable, so the industry will get smaller as we desire it to be, but everyone will be disadvantaged in the process. If that occurs, it simply constitutes market failure and from my point of view governments are there to assist the market to work. Some of the reasons I could think of would be industry-owned reasons; some of them are individual business-owned reasons, but some of them also have a role for Government and if we can identify what they are we can sort out who should be doing what to sort the situation.

The Hon. RICK COLLESS: I am going to use the term "lifestyle" versus mainstream producers, if you understand what I mean by that—the smaller hobby-farm type blocks as opposed to the bigger producers.

Mr STANFORD: Yes.

The Hon. RICK COLLESS: Is the proportion of lifestyle blocks higher in those coastal temperate regions than it is in the warm inland regions?

Mr STANFORD: Absolutely. That is definitely the case, but in a sense the lifestylers in coastal temperate areas have a similar problem to a lot of the people in warm inland areas. Warm inland areas are typically independent grape growers and they have small holdings, which in a competitive market tend to be uneconomic. So they have that in common, but a significant difference is that the lifestylers have alternate sources of income or are willing to pay the cost of low returns to pay for their lifestyle, whilst independent growers in the warm inland areas are typically more devoted to wine grape growing. But all of that said, we need to understand the magnitude of effect. By definition, lifestylers will be small and we understand the industry is dominated by four or five major players, so at the end of the day their production is typically uneconomic possibly, but it may not be a major part of the issue.

The Hon. RICK COLLESS: Because lifestylers are not reliant on their income from the grapes as their sole source of income, are they more inclined to sell at a lower price to get rid of their grapes, which in turn forces down the price across the whole industry? Is that what has happened?

Mr STANFORD: Yes, quite so, but whether they would influence the market per se is an interesting question, given the magnitude of effect. But I think I am making a more specific point and that is that they will typically sell their fruit into traditionally warm inland product, so the effect is not so much on the whole market—although it is. I mean these things flow through, but the group that is going to suffer most from this situation is the warm inland growers, such as the Riverina. More particularly, I would identify that as a problem.

The Hon. RICK COLLESS: In relation to the comments that you made about unethical commercial behaviour, is that where the big wine companies will go and screw down individual contracts with some of these smaller people, therefore forcing the price down? I know that in a lot of areas, particularly on the southern tablelands, which I am aware of, there is a group of lifestyle producers that get together and try to market their grapes as some sort of a cooperative. What sort of potential is there for that sort of voluntary organisation to deal with the grape buyers on behalf of their smaller constituency?

Mr STANFORD: I think there is an important issue here that probably the Australian Competition and Consumer Commission is only going to be the expert that will answer your question.

The Hon. RICK COLLESS: They declined to come, by the way.

Mr STANFORD: What is unethical? If you can screw down price and make higher profits, at the end of the day that is the market working unless people like yourselves say that these are not the sort of social conditions we want. In effect, yourselves through organisations like the Australian Competition and Consumer Commission will define what is ethical and what is unethical, but through a voluntary code we make an attempt to say what we think is good commercial behaviour and we try to set standards for that. I have mentioned the three absolute minimum standards that we would notify. I also mention another one and that is that I think that to share the risk of wine grape production between winemaker and grape grower prices need to be announced earlier in the year. That is not in the code, but that is another one that you can throw in. I can talk to you about what good commercial behaviour is so that risk is shared and gains are made by all players in the market, but if you are screwing someone down, that is supply and demand working and we simply have to make a decision whether or not it is decent.

The Hon. RICK COLLESS: As long as it is not monopolistic.

Mr STANFORD: That is true, and you can refer to the Australian Competition and Consumer Commission on that. But there are instances of unethical behaviour we can think of in our recent experience that I do not have a lot of association with at the national level that you can ask the regional representatives about, such as companies that announce prices and simply cancel contracts halfway through the harvest, which seems to be by definition very bad commercial behaviour, and unfair. Those cases are clear and then there is a whole grey area and there are experts that can sort that out.

CHAIR: Are varieties still an issue, particularly in relation to small farms or the lifestyle ones that the Hon. Rick Colless referred to? Are those varieties that may not be as popular in the marketplace still causing concern?

Mr STANFORD: Varieties and regions are a problem that our industry deals with in particular. Wine is a highly differentiated product and in the marketplace consumers will pursue wine possibly but more often a particular variety or region, so demand is split. When you slice and dice demand by variety and region you get a very multiple-faced product that creates at any one time things that are in demand and out of demand. I have put in a list of things here about what causes stickiness in coastal temperate and I think I will just write in another one that you have reminded me of and that is that one of the things that growers do is grow a range of varieties knowing at any one time that some are out of favour and they will make a loss on them and recoup that loss through the varieties that are in favour, and therefore they will be reluctant to pull out this year something that is out of favour but next year might be in favour, so I will write that down when I go out, but it is a problem that our industry has to deal with, yes.

Reverend the Hon. FRED NILE: Following on questions about the voluntary code of conduct, I note in your submission you said that only four majors and two small companies had signed up. What is the total number of wine grower or winemaking companies?

Mr STANFORD: That makes six companies or is your question how much of the crush is covered?

Reverend the Hon. FRED NILE: You say you only have those four majors and two small companies. How many others in your industry have not signed up to the voluntary code—another 10 or 50?

Mr STANFORD: There are a couple of different measures. There are, in effect, more than 2,000 winemaking labels in Australia now. There is a very long tail end to that sort of number because there are virtual companies for example that simply own a label and some of them contract the winemaking and buy grapes from somewhere else, but a more core number that you might work on for winemaking companies, including all of their groups and affiliates, is somewhere in the vicinity of 300 to 400, and I think that is probably the sounder number to work on.

Reverend the Hon. FRED NILE: What is the explanation for such a small number signing up to the voluntary code? They do not wish to be committed at all even to a voluntary code? Are they aware of it? You obviously have publicity or means by which you encourage people to do so.

Mr STANFORD: They would be aware of it. Whether or not the incentives are there for them to sign up is another issue. It is probably a question that is better directed to the winemakers because I represent grape growers and any of my members are signatories to this. What I have done in my submission is to list a whole lot of what I would have called conundrums about the code; some of the simple things like if you are ethical you are going to sign up for the code, but if you are not, well why would you? If you were ethical and you signed up for it and then decided that it did not suit you, you would break the code and what is the punishment? Just expulsion from being a signatory and perhaps a little bit of shame.

Reverend the Hon. FRED NILE: You imply that there is a lot of unethical behaviour going on. Would you put a number to it?

Mr STANFORD: I am not sure that I have implied that.

Reverend the Hon. FRED NILE: Would you say there would be 1, 10 or 100 companies?

Mr STANFORD: No, I do not think I would and I am not sure that I have actually implied that there is unethical behaviour happening. In fact, what I have said is that there is a lot of commercial behaviour happening on supply and demand and I have said that wine grape growers at the moment are taking most of the risk. Now that is a bad situation for grape growers and there are things that you can put around that. One of the conundrums with the sign-up by winemakers is that if we have four of the majors signed up to the code of conduct, in effect the larger part of the grapes crushed in Australia are under the code of conduct but what the management committee of the conduct are seeking is a culture of compliance, a culture of signatories.

We have now identified that we would rather have a larger number of winemakers so that we can say that the winemaking community generally are signed up for the code of conduct rather than saying by having four signatories out of say 300 or 400 most of the crush is covered. It is as much about the perception as the practice in terms of having a code. I do not think I would rate a large number of winemakers as unethical; I do not, but you do need to protect the grower against those that can be unethical and I am sure that from your regional witnesses you can get instances of bad behaviour.

Reverend the Hon. FRED NILE: You have a number of conditions for the voluntary code of what you would call ethical behaviour. If someone does not fulfil one of those items, they would be unethical?

Mr STANFORD: Okay, is that my wording?

Reverend the Hon. FRED NILE: On page 7.

Mr STANFORD: I guess what I have said—and it may be a matter of clarification if my words on paper do not say it clearly—I think those three elements are good commercial behaviour because at the end of the day any operator in the industry can sit on the open market and buy and sell their grapes on spot markets. What these things refer to are the contractual arrangement. If you wish to go into an arrangement whereby you are selling your grapes and you want to share the risk with the buyer, which is a decent, good commercial way of doing things because everybody wins, then those are the three elements that are required. Contracts are strongly supported. If you sign a contract and break the contract, that is unethical, but those conditions, what I am saying, are good commercial practice for contractual arrangements. I am sorry if I have confused the issue of good practice as ethical practice.

The Hon. MICHAEL VEITCH: In your submission you suggest that the South Australian Wine Grape Industry Act of 1991 would be a good model for New South Wales and some of the submissions talk about the advantages. Can you talk about some of the disadvantages of that piece of legislation in South Australia or if there are any flaws because it has had a period of time in which to operate. What are some of the things that have happened out of that legislation that, if we were to recommend adoption of that bill, we would not want to replicate here in New South Wales?

Mr STANFORD: That is a good question and I think I am going to come up short with an answer.

The Hon. MICHAEL VEITCH: You can take the question on notice and get back to us with an answer. People keep talking about the advantages but as legislators we all know that there are often unintended consequences of our legislation and I would like to know what they were, if there were any?

Mr STANFORD: I support your question; I think it is a good one. I have not been in my role long enough to actually have a history or knowledge of that.

The Hon. MICHAEL VEITCH: Perhaps you can take it on notice?

Mr STANFORD: I would certainly be happy to do that.

The Hon. MICHAEL VEITCH: In some of your earlier testimony to the Committee you spoke about the competitiveness of the sector, particularly around setting price. The legislation in South Australia and your voluntary code of conduct, how does that sit or does it conflict with the national competition principles in South Australia?

Mr STANFORD: Your question is: does our code conflict with national competition?

The Hon. MICHAEL VEITCH: Is there a conflict or is there a potential for a conflict with national competition?

Mr STANFORD: I do not believe so.

The Hon. MICHAEL VEITCH: Can you take that on notice and check?

Mr STANFORD: It sounds like I need to.

The Hon. MICHAEL VEITCH: Again it is one of the things that we will need to be aware of. Now that our friends from the Australian Competition and Consumer Commission [ACCC] have not turned up we may have to do our own delving.

Mr STANFORD: Prima facie around the table that manages this code both grape growers and winemakers, and typically the winemakers are represented by legal counsel from three of the majors that I can think of, it would surprise me greatly if anything were to the contrary, plus the fact that the code, as our process of developing it and improving adoption has recently been reviewed by a well-recognised reviewer of these things who made reference to the ACCC for example, so when he reviewed it he reviewed it in the light of his knowledge of the ACCC, so once again it would surprise me greatly.

The Hon. MICHAEL VEITCH: Please take it on notice to make sure because your comments are recorded in *Hansard* and I do not want you to get into trouble.

Mr STANFORD: Sure.

The Hon. MICHAEL VEITCH: Earlier in your testimony you spoke about a five-year contract sometimes not being a sufficient time frame to recoup the original investment. This is regional and market dependent but what would be, on average, the time frame to recoup your investment?

Mr STANFORD: Have you been designated to ask all the hard questions?

The Hon. MICHAEL VEITCH: No, these things interest me and I want to know?

Mr STANFORD: This is going to vary a lot. In the warm inland regions vines become full bearing typically three years. In coastal temperate areas the number I would normally work on is five years by comparison. I am working on some really general understanding here but I would have thought to cover all of your establishment costs and the like it would take a couple of years after each of those full bearing type of scenarios. Once again we come up against the problem of the diversity in our industry; regions and varieties all have differences.

The Hon. MICHAEL VEITCH: That is right, which makes Australian wines quite nice, I say.

Mr STANFORD: It does, it is part of the wine experience, the variety and all the rest of it, but it also makes the job of individual grape growers to understand the business a challenge and we try to assist in that respect through things like VineBis and typically in the wine industry more so than in a lot of other agricultural businesses because of the lifestyle effect because we have grown up during the last 20 years in pretty comfortable circumstances by comparison to the day. There are a lot of operators out there who do not know their business and they really do need to understand it, but there is also the opportunity, and the opportunity is that the consuming public is very interested in all this variety, difference and experience.

Every grape grower should be involved in understanding what the consumer is buying when they buy the end source of their production. We need the circumstance where grape growers are more integrated into understanding the value chain and able to talk to the winemakers about where their product is going and what is going into it so that they can, in the first instance, be selling their product with a knowledge base and knowing what the qualities of their product are rather than just being on a spot market. It is of little wonder to me in these very difficult circumstances in terms of supply and demand that grape growers find themselves in trouble because they are availing themselves to what is, in effect, a spot market, by not knowing what their product is and what the attributes are that they are selling and therefore able to negotiate that. Our ambition as an organisation is not only to put all of the regulation around governing good commercial behaviour but also to assist the grower to be a part of the value chain so that in the long run they are independent and resilient in all these matters.

The Hon. SOPHIE COTSIS: This is an aside but when you were talking about getting a culture of signatories—and you may have done this—have you looked at other peak bodies and how they have campaigned around this issue of getting members or organisations to volunteer and sign up to codes?

Mr STANFORD: I have been to one of the management committee meetings and it is not a broad breadth of experience but through that I am aware that the review process that we went through at the last meeting did draw on other examples and certainly at that meeting, as a part of all the feedback from the review, we had a couple of other industry codes represented around the table who told us of their experiences. As I said earlier, one of those industries that sat around the table gave a very positive experience—if I have got time to develop it.

Grape growing and winemaking is a very integrated function. What happens in the vineyard is very important to the final product that the winemaker makes. It is important that that integration is there. For that reason most issues are in common between winemakers and grape growers but in all of the forums where we can talk about the issues that we have in common they usually get sullied by the fact that we have to argue about prices. If we were able to find a way to separate those discussions about prices from all of the other discussions that we need to have in the industry, I think it would be a positive move.

One of the interesting things that I heard from an industry that did have a successful voluntary code was that the code management committee actually evolved into a forum where they could talk about those adversarial issues and just park the issue over there so that they got on with business in other areas. I think that is a great aim to hang in there for but we cannot wait forever, which is what my submission is saying. So there are positive examples but I have to say that the weight of them falls back by default into talking about mandatory codes and unless things change soon for us that is what we will be thinking too.

Reverend the Hon. FRED NILE: Can you clarify the point you just made about not being able to wait forever? How long has this voluntary code offer been available? When did you design it—five years ago, 10 years ago?

Mr STANFORD: Negotiations started about five years ago but it has been implemented now for about a year. I hope you will forgive me if my times are not strictly accurate, but that is about the dimension of it. At the review meeting the understanding we have is that the Winemakers Federation has undertaken to improve the rate of signatories at a certain rate for one year and to improve that again in two years, so I suppose we are looking at a two-year program for this thing to prove itself. I would say that patience definitely would run out after that and my resources to assist the process will definitely run out.

The Hon. RICK COLLESS: Going back to the issue of the supply contraction and demand expansion model, you would no doubt be aware of the various vine-pull programs that have been sponsored, particularly in South Australia quite a few years ago. Do you see those as a positive or a negative way to approach this problem?

Mr STANFORD: To be honest, I do not contemplate it because I do not think governments in the modern age would even contemplate it. It is an easy fix and it could solve problems, but it could also create problems. As Michael said earlier, the Government does not want to be doing things that can actually do harm. We all think back to the shiraz vines that were removed in the vine-pull, as an illustration. The longer-term benefit for the industry will be for all our members to be knowledgeable about their business and to be making these decisions themselves. That is the way forward to a viable industry and that is the way we can smooth these ups and downs. That would be our ambition and we have things in place to try to assist that process, and the winemakers do too.

If the Government were to do anything to assist, I would rather see an investment in a process which says we do not have to do that thing again in seven years time. In one sense a vine-pull will be useful, which is that the oversupply problem undermines anything we do in the demand arena. We simply have to get back in control with supply in order to promote our demand ambitions. Until we do that, pushing out demand is tremendously difficult. The fact is that if you take a vine out today it is fixed and done and gone, whereas it takes time to develop demand. If a vine-pull is the way to get back in control and we all promise to learn our lessons and not do this again, great, it would work, but it is not the way to learn how to be independent and resilient businesses.

CHAIR: We are out of time, but if there is something you feel you should have brought to our attention you could do that now.

Mr STANFORD: I think I have covered everything I wanted to say.

CHAIR: There will be further questions we would like to put to you. We would like to get answers from you within 21 days.

Mr STANFORD: Sure. When are the questions likely to come—20 days?

CHAIR: Twenty-one days from when you receive them. They may come next week. We are asking the questions so we have to wait for your answers but we would like to get a time frame to fit in with the report we need to make.

Mr STANFORD: I am more than happy to commit to that but of course there is always a risk and if you were to help me get more resources I could promise you I would lower my risk!

The Hon. RICK COLLESS: We are all in that boat!

Mr STANFORD: Yes, I know.

CHAIR: Thank you for your evidence this morning. It has helped the Committee and will continue to help us in preparing our report.

(The witness withdrew)

(Short adjournment)

MARK de LACY McKENZIE, Chief Executive Officer, Murray Valley Wine Growers Incorporated, sworn and examined:

CHAIR: Are you conversant with the terms of reference for this inquiry?

Mr McKENZIE: Yes, I am.

CHAIR: If you should consider at any stage that certain evidence you wish to give or documents you may wish to tender should be heard or seen only by the Committee, please indicate that fact and the Committee will consider your request.

Mr McKENZIE: Thank you, Chairman.

CHAIR: Would you like to commence by making a brief opening statement?

Mr McKENZIE: Yes, I will, Chairman. At the outset I am quite prepared to have our submission made public in full, together with any evidence I give here. I cannot imagine there is anything that we would not be saying in the public realm. But if otherwise, I will indicate clearly. Thank you for the opportunity of meeting with you today. I wanted to give you a little bit of extra background on my background. I note that my associate Lawrie Stanford has just appeared before you. Up until July this year I sat in Lawrie's seat as Executive Director of Wine Grape Growers Australia. I was the inaugural executive director for 4½ years, and as part of that I have been and continue to be a member of the Wine Industry Relations Committee, which is a Federal committee drawn from representatives of Wine Grape Growers Australia for the wine grape sector and the Wine Makers Federation of Australian for the wine production sector.

The committee talks largely about issues around commercial practices, grading quality, and originally around the code of conduct. As part of that I also sit on the Code Management Committee, which similarly is a bipartisan committee drawn from both the peak industry organisations in the two industry sectors specifically to look at the Australian wine industry code of conduct around potential amendments to that code to improve its function. As well as that, I am obviously conversant with national as well as State and regional wine grape and wine production industry politics and the dynamics of the industry.

Obviously I have made a submission formally, and that submission has a significant number of attachments. I have obviously given that to the Committee for its consideration. I wanted to briefly outline a couple of the major thrusts within that submission. Our concern at the moment is that the wine grape market within New South Wales and nationally is in failure. There is very much a lack of clear market signals to growers around prices, volumes, and the intention of wineries in terms of contract arrangements going forward. Effectively what we are seeing here is a reinforcement of the dominant market power in the hands of wineries, with very limited, if any, market power in the hands of growers.

We believe, unfortunately, as was reinforced in the 2005 Senate inquiry into the wine industry, the report of which I have attached as an appendix to our submission, that the same litany that we see in Appendix 4 of that 2005 Senate inquiry report—of exploitative commercial practices by wineries—continues. That is extraordinarily unfortunate, particularly in light of the fact that a direct outcome of that Senate inquiry was the development of the Australian wine industry code of conduct. Our view is that the code of conduct, which is now two years old, is clearly failing and that we need better market signals to be instituted within the industry and a system by which contract arrangements and the signal on indicative prices gives a far better commercial signal to growers—not just about whether they will grow a crop at a particular price but whether, indeed, in the current environment they will grow a crop at all.

Our view is that some of the issues we have raised in the submission are clearly issues for Corporations Law and for the Trade Practices Act at a Federal level. However, our view also is that a large part of this can be supported by the New South Wales Government on the recommendation of this Committee, and that we would see this as the opening move by our organisation in support of what the Wine Grape Growers Australia organisation is doing nationally in trying to get at least a tripartite New South Wales-Victorian-South Australian platform that better protects growers' rights and gives clearer market signals to them about the wine grape market, but also that by way of using the COAG forums this State Government and others may wish to use their influence at COAG, through the ministerial councils, to see national legislation or regulations introduced where that is appropriate. We openly acknowledge that some of the gambit of what we have suggested in the

submission probably does stray into some Federal jurisdictional issues; however, we think it needs to be seen as a whole, and that is why we have put it in that fashion.

Finally, I would like to reinforce that we are not here in any way suggesting that we re-regulate prices in the industry. We believe that the most appropriate system of sending signals in the industry is to have an open exchange of information, through contracts and through annual agreements by way of the open market. The problem for us is that the market currently is being distorted because the information flow to growers is clearly being held up to some extent by the timing of indicative prices and final prices that are delivered to growers. Ultimately, the problem for us is that we believe it is untenable—indeed, it could be unconscionable—for wineries who know they have in the last year taken grapes at well below the cash costs of production to continue to allow growers to put input costs in, 80 per cent of which they put into growing a crop before they even harvest it, full well knowing that they are not going to get anywhere near paying cash or floating costs again in the current vintage.

In our view, the way forward is that we do need regulations that tighten up on some of those contractual issues, but more particularly we need clearer indicative prices earlier in the growing season to allow growers to make a decision as to what they will do, whether under contract or not, and ultimately, whether in the current very difficult operating environment they will grow a crop or not. With those opening comments, I would be happy to address any questions the Committee might have.

CHAIR: Could you elaborate a little more on the regulations that you would hope to see in the future?

Mr McKENZIE: Yes, Chair. Thank you for the opportunity. The first issue for us is that in South Australia, and South Australia alone, there are regulations under the South Australian Wine Grape Industry Act 1991. Two provisions of that Act have set a platform for commercial arrangements in that State. By and large, the schedule of payments included in those regulations has been used by the bigger companies across State borders to set a standard schedule of payments. That schedule of payments is 30 per cent at the end of the month following delivery of the grapes, 30 per cent at 30 June, and 30 per cent at 30 September. We believe there are significant instances in New South Wales and elsewhere of other schedules being used which are a direct disadvantage to growers because effectively the drip-feed of payments to growers, and in some cases no payment until the wines are sold, can mean that growers not only are effectively subsidising the operation of those wineries through taking much lower payments but it means they may well expose themselves to a situation where they are not being paid for a following vintage at all, should that winery get into financial difficulties and fall over.

In the Murray Valley alone, since 2002 we have had four major wine groups fail financially, at a cost of some \$20 million to growers. Part of the issue for us is to institute the second major component of the South Australian regulations, and that is that no purchaser can purchase again in the following vintage until the previous vintage's purchases have been paid for in full. What we are asking the Committee to consider and to recommend to the State Government would be the introduction of a similar Wine Grape Industry Act that would put those two provisions in place.

The second provision is one that is tied up very much with the secured creditor status of growers, and that is the need to have a retention of title clause, as a minimum. We are aware of the personal property securities regulations that are now flowing through in the Federal sphere. That will go partway towards this, but our view is that, even though the Australian wine industry code of conduct—which is not well supported, unfortunately, by wineries—has a provision for a retention of title clause to be clearly stated should there be one, there is no regulation to say that there should be one. We believe the difficulties with personal property securities regulation may well be around the issue of requiring registration of that security, and I think that is potentially difficult in terms of getting the agreement of wineries around those arrangements. We would like to see within contracts the provision for a retention of title clause.

The code of conduct has many provisions for minimum contract arrangements, or minimum contract clauses. We believe that to the heart of this issue there are three clear provisions that assist in market signals back to growers. Firstly, as amazing as it seems, not all contracts are in writing; there are a lot of handshake agreements or verbal agreements around annual purchases as well as longer-term contracts. We believe that at a minimum three things from the code of conduct should form the basis of regulations within a Wine Grape Industry Act. They would be that all agreements be in writing, that a final price be in writing and delivered to the grower before harvest or before delivery of the grapes. Incredibly, we still have a situation in this State and elsewhere where large volumes of grapes are being delivered to wineries without the grower having any idea of

what the final price will be. In this day and age, that is totally unacceptable in our view. The third component of this is that the code provides for either a fixed price or a methodology that is clearly defined as to how the final price or a market price will be determined. We believe that is currently being distorted by wineries because of the open-ended nature of contracts or supply agreements, because there is no consideration in most contracts and we believe those three components should be included.

Finally, in keeping with the main thrust here around market failure, our view is that there needs to be regulation of advice of indicative prices by 30 June every year. The reason for that is, firstly, all major wine companies have their budgets for wine grape purchases in the following vintage done in May. There is no reason, within a few thousand tonnes, why they will not know exactly how many tonnes for which they have provided a budget for purchase, and they can break that down into variety by variety. Within a couple of thousand tonnes, they can go back into the annual market and pick up what they require or buy wine from third parties. So there is no real reason why they should do that. The reason for 30 June is that it sits firmly in the middle of the pruning season between June and July. Pruning must be completed by the end of July in most districts, certainly in the Murray Valley, before we get the beginning of bud burst and the beginning of the next season.

Our view is that indicative prices at that time would allow a grower to make a clear commercial decision about whether they will grow the crop or not, and in the current environment we believe they need the information to be able to do that. So we would like to see regulation and advice by wineries of indicative prices by 30 June, fully knowing that indicative prices are not binding on wineries, and we are not suggesting a final price position, because it is too far out from the vintage to be able to give a final price position, but an indicative price would at least give the grower the ability to make a fairly well informed decision about whether to produce or not.

CHAIR: Just on that regulation then—and for your information we had invited the ACCC representatives to be here this morning but they declined unfortunately— how would that fit in with the ACCC's guidelines?

Mr McKENZIE: Because those indicative prices are not binding on wineries in terms of final price, our view would be that it is not in contravention of the Trade Practices Act, but quite clearly we may need to get some advice there if we thought there was likely to be a conflict. Around that, in terms of competition policy, yes, we have not tested that with them yet, but I think it is certainly worth our while having a look at that, bearing in mind that there is already provision in the code, which the ACCC has no issue with, for indicative prices for code signatories. Bear in mind that Fosters, now Treasury Wine Estates, Constellation Wines Australia and Orlando Wines, three of the five biggest wine groups—the other two are Australian Vintage and Constellation Wines, both New South Wales based enterprises—are signatories to that code and they have to provide indicative prices to growers under that code by 15 December each year, including not just the three inland regions of Riverina, Murray Valley and Riverland, but also the Hunter Valley because of the early harvest nature of that region. Given that they do not appear to have an issue with the code and they have reviewed the code, we cannot imagine that they would have any problem with an earlier indicative price, given that would not be binding on wineries, but simply indicative.

The Hon. RICK COLLESS: In your submission you talk about the oversupply of wine grapes and you give us some figures that come from the Wine Restructuring Action Agenda statement, that it needs to be reduced by between 270,000 and 480,000 tonnes of grapes. You go on to say that between 20,000 and 40,000 of vineyard seems to be unviable and that some 8000 hectares have already been removed. What was the incentive to those growers to remove those grapes from production?

Mr McKENZIE: Some of them did take the Federal Government's small irrigators exit package. In the Murray Valley 80 growers took that exit package and 176 in the Riverland region of South Australia.

The Hon. RICK COLLESS: They were mainly the smaller—

Mr McKENZIE: They were.

The Hon. RICK COLLESS: What size are we talking about?

Mr McKENZIE: Originally it was 15 hectares and then Senator Xenophon negotiated an arrangement to lift that to 40 hectares, but I would have to say that any grower with the cost of establishing a vineyard, a 40

hectare grower who was considering getting only \$150,000 maximum and paying exit fees and potentially capital gains tax out of that, it would not even touch the sides in terms of what their liability would be to banks. Our current information indicates that the average overdraft alone for a vintner in the Murray Valley would be between \$200,000 and \$220,000. It is probably higher than that. That information is about two years old now. So we have got a situation where a lot of people are in far deeper than that was able to do.

In terms of the incentive, I think the incentive frankly was that they could not continue to produce at the sort of prices that they were returning by way of wine grapes. This has been driven mainly by that factor, mainly by the pressures of oversupply and lower prices and changing market conditions, but I think the other key issue is that the drought in 2007 sent a very significant shock wave through, when people had to pay very high prices of up to \$2,400 a megalitre just to stay in business. It was a surprise to us that so many growers borrowed money to do that, to stay in business, and I think the issue is that that just about finished off a lot of them. We have lost 500 growers in the Murray Valley, both sides of the river, in the last five years. We do an annual survey that is very detailed. Our current projections are another 50 growers will go this calendar year and another 1000 hectares of vines. So we are facing a very severe over-correction in the inland region.

The Hon. RICK COLLESS: Those figures relate to the status quo as far as water is concerned I presume?

Mr McKENZIE: Yes.

The Hon. RICK COLLESS: What is going to happen if the Murray Darling Basin Authority's plan comes into existence in that area? These figures are going to be blown out again on top of that, are they not?

Mr McKENZIE: Yes, there are two factors there. One will depend on what the effect is on the long-term price of permanent water, of high security water. I would be amazed if there is not a spike in that, absolutely amazed, simply because taking 3,000 to 4,000 gegalitres out of the system is going to short supply pretty significantly. We are in a good supply position. I can say that as yesterday, as I flew over it, the Murray was running back to Mildura, so we have very good water supply at the moment, about 73 or 74 per cent in the southern basin at the moment. I think we are in for a couple of years of good supply and probably somewhat depressed water prices, but I have to stay in districts like the Riverina—not in my jurisdiction—that is having a direct effect on growers because they have relied very definitely through this period of low and falling prices on selling temporary water to keep in business and that avenue is blocked to them. I think the first issue is that as price goes up a lot of growers are going to consider their future. We have an ageing population in growers and we have a next generation that simply is not putting their foot forward. So we are going to have a crisis in the industry unless the production sector realises it is in their long-term interests to pay viable prices to stop people exiting the industry. That is a very real issue that they privately acknowledge but probably do not publicly acknowledge at the moment.

The second issue is that we still are under draft declaration conditions in the Murray Valley until 31 March. When that goes off on 31 March up to \$50,000 per household will be removed, up to \$29,000 in interest rate subsidies and \$21,000 in household support. Our view is we will have a further collapse of grower numbers at that point because we are aware through the rural financial counselling services that a large number of growers on their books will not survive that hit. We, I think, are in line for a very significant over-correction that is fundamentally against wineries' interests, but we still do not see them giving early enough indication of prices to keep people in the industry. And it will be indiscriminate. It will be about the debt levels. You can be the best grower in the Murray Valley and still be shunted out, simply because you will not be able to survive the financial hit through those factors.

The Hon. RICK COLLESS: In your submission you also talk about the Wine Restructuring Action Agenda statement which said that the greatest area of over supply is in the cool temperate regions.

Mr McKENZIE: Yes, it is.

The Hon. RICK COLLESS: Can you give us any idea how much that cool temperate area needs to be reduced by, similarly to the number of hectares that you mentioned in the inland areas?

Mr McKENZIE: I think probably at the top end, if 20,000 hectares is the bottom figure, and the difference between 20,000 and 40,000 hectares is best case scenario, worst case scenario for future markets at viable prices, I would have thought something in the order of probably 14,000 or 15,000 hectares at the lower

end and a similar proportion at the upper end. To put it in context, the Wine Restructuring Agenda statement factored round about 130,000 tonnes across the three inland production zones that was either unviable—very little of it was unviable at cost because we are very efficient growers, but in terms of lost markets, through loss of cask wine sales market or a ratcheting down of that, which has been happening over many years in the domestic market, unviable fire sale of bulk wine on the export markets and loss of competitive popular premium bottle products, and that is typically around the \$8 to \$10 mark in the Australian market place, equivalent in export markets, about probably 105,000 tonnes of that 130,000 was because of loss of market.

Now, just on the figures prior to the 2010 vintage of decommissioned vines, and I do not talk just about removals, because growers are walking away from vines, they cannot afford to knock them over at \$1000 a hectare, so we do not talk about grubblings, we talk about decommissions, just decommissioned vines in the Murray Valley and Riverland alone took out 8000 hectares. So we have taken out 160,000 tonnes of potential production. So we are already in a voluntary over-correction. You take the other factors that I just referred to and we are going to be in for a significant over-correction, and the danger to wineries is that they are still reliant upon the wine districts producing a particular profile of fruit that they use for the popular premium markets, which is 80 per cent of their bottle total light export markets, but more particularly they are reliant on significant throughput in wineries to keep the unit cost of production per litre down to a reasonable level.

If you start drying up their feedstock, if we can put it as crudely as that, then their cost of production increases exponentially. So they are running a very serious risk. We are also talking about undermining, from a State development perspective, a significant sector in the industry in this State and elsewhere, but we are also talking about undermining the very basis of the economies of scale that the large wineries utilise in our region and elsewhere, particularly in the Riverina.

Reverend the Hon. FRED NILE: Thank you again for coming in. I note that you refer to in your submission, and you have referred to it again today, the problems with the wineries, and you actually use the term "exploitative behaviour". Could you just clarify "the wineries"? You have mentioned some company names. They are completely independent from the growers. You do not have a co-op situation where the growers are putting their grapes into their own wineries?

Mr McKENZIE: There is one example in South Australia, a very large co-operative group, which is about half the Riverland wineries, about 740 wineries out of about 1200. It is a bit below the half now because of a loss of growers from Consolidated Co-operative Wineries, who supply exclusively to Constellation Wines Australia. Murray Valley Wine Growers established, but set up as an independent entity, Vintage Traders Australia, which is a group marketing entity in the Murray Valley, both sides of the river. It simply finds markets for fresh grapes or for bulk wine that is converted under contract for growers. But no, we do not really have a co-operative system. Effectively, you are talking about privately or corporately owned wineries as what we would call takers or purchasers of fine grapes, and they are pretty much the bulk of the market. Around 20 per cent of Australia's wine grape production is controlled by winery vineyards themselves. So they are not just purchasers of wine grapes, they also own, operate or lease quite significant land holdings in their own right.

Reverend the Hon. FRED NILE: So they are a combination of being a winery and a grower?

Mr McKENZIE: They are a combination of being a winery and a grower, and the thing that strikes us is that most of them will openly acknowledge that independent growers so-called, in other words not owned or operated by a winery, because of the age old thing in primary industry of discounting your own labour, our growers can produce far more efficiently on a per tonne basis because of corporate overheads that they have in larger vineyards, particularly the listed companies, where you have environmental managers, you have two or three levels of management. So growers traditionally run very lean and mean from the point of view of cost imports.

We are certainly very efficient, but we clearly cannot operate in a position where our benchmark cost of production on average across all varieties and all vineyard sizes in the last year in the Murray Valley was \$376 a tonne. Our average prices, and the crush survey is contained in the submission as an appendix, our average red grape prices were \$311 across the region and our average white grape prices were \$283 across the region. Whites were still well below that mark in the previous vintage, 2009, and reds were only just above it. So you can see a situation where wineries are saying, if you can get them to make any commitment at all in the current pre-2011 vintage environment, what will the price be. They say use last year's price as a guide. Well, it is giving no hope at all to growers whatsoever. That is why fundamentally we need earlier indicative prices so growers can make really well informed commercial decisions or as best informed as they can be in the current

environment.

Reverend the Hon. FRED NILE: So have the wineries supported your voluntary code of conduct?

Mr McKENZIE: No, they have very poorly supported it, unfortunately. Currently we have a bit less than 50 per cent of wine grape purchases covered by the three major signatories. There are three other signatories, one of whom is New South Wales-based, that is, Tyrrell's vineyards in the Hunter Valley, and two South Australian-based wineries—a very small one, Henry Holmes Wines in the Barossa, which is doing it philosophically because they purchase only small amounts grapes, they believe it is the way forward; and the other one is Balnaves at Coonawarra. So the three key signatories are: Foster's, now Treasury Wine Estates; Constellation Wines Australia, mainly the Hardys brands; and Orlando wines, which of course is Jacob's Creek for all intents and purposes.

Reverend the Hon. FRED NILE: There are wineries that have not signed up?

Mr McKENZIE: There are. In the New South Wales context those three major wineries are Casella Wines, Australian Vintage Ltd and De Bortoli wines. The submission has it, but for the Committee I reiterate the reasons for that. We believe Australian Vintage do not want the code to apply to existing contracts. Our view is you are either a code signatory or you are not, with all that that entails. Frankly, they are asking for the PR benefits without locking into the code provisions themselves. Casella Wines have indicated that they do not wish to use their dispute resolution procedures within the code and that De Bortoli Wines have indicated that they do not believe in written contracts, despite the fact I know they have a number of them.

Whatever they are saying, in April this year we have just gone through a full code review, as was prescribed under the code after the 2010 vintage. The code reviewer made it very clear that he talked to a large number of mid-sized and larger non-signatory wineries, most of whom said, "We don't need to do this because we already do these things for our growers anyway". To which he stated, "If they are already doing it, what harm is there in becoming a signatory?" Unfortunately, we believe that it reinforces, if not explicitly, an exploitative behaviour. It reinforces the fact that if you have all the eggs in your basket and all of the market power in your hands, why would you give it up.

Reverend the Hon. FRED NILE: Are you on that committee?

Mr McKENZIE: I am on the Code Management Committee.

Reverend the Hon. FRED NILE: Are you the chair?

Mr McKENZIE: No, I am not. I am a member of it through Wine Grape Growers' Australia [WGGA]. The WGGA, Laurie Stanford's organisation basically convened that committee.

Reverend the Hon. FRED NILE: Does the committee physically meet at wineries and have discussions?

Mr McKENZIE: Yes, we do. The representatives of the wineries on that committee at this point are: Foster's or Treasury Wine Estates, Orlando and Constellation Wines Australia. The Code Management Committee is a bit different to the Wine Industry Relations Committee, which also has Australian Vintage represented. It also has a Casella representative on it. The reason they are not involved in the Code Management Committee is because they are not signatories to the code. We do not believe it is appropriate that they would sit it around potential amendments to the code if they are clearly not committed to it. Yes, I do physically sit on both those committees.

The Hon. MICHAEL VEITCH: Mr McKenzie, thank you for coming.

Mr McKENZIE: Thank you.

The Hon. MICHAEL VEITCH: I want to talk to you about the South Australian Wine Grapes Industry Act 1991, which is mentioned in a few of the submissions we have received, mainly favourably. My question involves two aspects. One, what are the disadvantages of that Act, which has been in operation for a while? Two, what is not in the Act that you would like to see in it?

Mr McKENZIE: I have to be honest with you that I am not fully across the other provisions. I suppose we have cherry picked those parts of it that are quoted back to us by our South Australian industry colleagues. It certainly does not have anything around price fixing there because, clearly, that is not in the parlance or the desire, I think, of any State or Federal administration. It is simply that the terms of payment—a third, a third, a third, as I call it—has been the accepted terms of payment across Australia by the major wineries. It has delivered certainty to growers and it also has delivered a situation of a fall back through those regulations. To be frank, if there is a prohibition on a shaky winery that has not fully paid for its previous vintages grapes—and that may go back a number of vintages and, unfortunately, we have examples of that in our region on the Victorian side—they know they might not take a crop the next year but at least that prohibition is a fallback for growers to say to a State administration, "These people have not paid us. They are clearly shaky. If we supply them again not only are they getting an advantage in being able to exploit our position as a producer of a perishable crop that we need to deliver, but clearly we are putting ourselves in a frame for it to fall over and to lose that payment." That is why we then segue, in a sense, into the retention of title provision that we are asking to be included in contracts.

The Hon. RICK COLLESS: Is that on a grower by grower basis or does that prevent that winery from buying grapes from any grower?

Mr McKENZIE: That is a good question. I would need to check on that. I think the prohibition, as I understand it, is on it buying any grapes.

The Hon. MICHAEL VEITCH: Can you take that on notice? It is an important point.

Mr McKENZIE: Yes, I would be happy to advise on that.

The Hon. MICHAEL VEITCH: What is not in the legislation that you would like to be in it, other than those matters you have just raised?

Mr McKENZIE: The other things that I outlined really: retention of title, the minimum provisions of the code. We would like to see at the very least a tripartite one industry Act applying, the provisions of which have the flexibility you might need because of legislative framing and provisions in each of the States. We believe it should include those core things we have outlined by way of recommendation here. It goes to our recommendation 5 that we would like the State Government to lead the charge, in a sense, on getting those minimum provisions provided and for us to take a tripartite approach. Clearly, those provisions are already in place in the South Australian Act. We would like to see that replicated here and in Victoria. In fact, I have discussions with the Victorian Government next week along similar lines. I know that Michael O'Brien, the Minister for Agriculture in South Australia, is quite keen to look at some of these issues, including some industry restructuring in the warm inland areas on a tripartite Commonwealth basis as well.

The preferred outcome would be that we would see some mandatory code provisions mandated federally to apply to the whole country. But ultimately the jurisdictions that dictate the wine grape market in large order in this country are New South Wales, Victoria and South Australia. So the fallback position and the basic platform we need to build, even if the State Government might say there are jurisdictional issues here around the trade practices Act and so on that we need to give to the Feds, I think the support of the State Government towards achieving that and progressing that move to a legislative framework and some regulatory action that is going to give some minimum provisions along the lines we have recommended would be very good.

The Hon. MICHAEL VEITCH: Your submission talks about the quasi national industry standard that has been created. I want to drive further into the 30-30-30 payment model you talked about. Has there been any economic modelling around that? Is that the best payment schedule model or should a better model of payment be structured for the growers?

Mr McKENZIE: The best model of payment is the one being paid by the Wine Group, the US-based operation in the Riverina, which is full payment 30 days after delivery. That would be the beacon on the hill. The reason for that is, effectively, and I think I said it in the submission, we have a situation where typically a grower pays for his harvesting and freight costs out of the first third, he pays most of his import costs and some of the repayments to the bank out of the second, he pays the rest of his working capital repayments to the bank out of the third, and whatever margin is left over he puts in his pocket. He clearly has not put anything in his pocket in the last two years. I have to say that even though I believe the market signals are turning and we are up

off the bottom, I would not be confident in saying how off the bottom we are unless you are a gordo grower. There is feeding frenzy going on for gordo at the moment. Thank goodness, we have one funny old variety leading the charge.

We know we are desperately short of chardonnay. The managing directors of Foster's, David Dearie, told me so himself. Their grape liaison officers have told growers that. In their new contract arrangements the only patches of grapes that they have contracted so far are chardonnay. But as one of my growers said to me, "I've got 2½ hectares of chardonnay. That's all they have contracted. They are saying, 'We will attach the other varieties when we decide what we want.'" There is absolutely no surety in that. He goes to his bank and the bank says, "What is your business plan?" He says, "I don't have one." The bank says, "Why don't you have one?" He says, "Because I don't have a minimum price." What we said to Foster's was very true: we know your minimum price was only \$150 but at the very least it covered harvesting and freight costs and it was some surety of a level of cash flow so the grower could leverage some finance out of the bank.

The banks are facing a situation where vineyard values are zip, they are land value only. The only thing of value is their water. Their collateral is being slashed. If we are going to look at the Murray-Darling plan guide, it is going to cause all sorts of difficulties around equity levels, real or implied. So the pressure on growers is getting greater and greater. But I am getting a little off the point. The 30-day payment model is fantastic. They are a significant taker, I think something in the order of 15,000 to 20,000 tonnes of grapes. They are a significant producer. They have a particular model that they have used in California that they use here. I am talking about the Wine Group in the Riverina. Our view is that that current quasi national standard, as we call it, at the very least allows a grower to know that by 30 September under normal circumstances they are pretty much going to be able to cover their costs and financial arrangements. Our view is that at a minimum there needs to be a third paid a month after delivery.

Effectively the winery is lining up and saying, "A month-by-month drip feed over seven or eight months after an initial amount suits our cash flow. It allows us to sell the wine on." Yes, we understand that. It may put the winery under more pressure, but it is better for growers to have a clear impression of who is failing or not than have a situation where they are delivering grapes to an entity where they do not know how viable they are and they are effectively being asked to subsidise the operations of that winery. We do have a circumstance—and unfortunately there are some New South Wales growers who have supplied this particular winery, I will not name it—where we know that at least \$300,000 is still owed from the 2009 vintage to growers in our region, including some New South Wales growers on the Swan Hill side of the river in New South Wales at Kyalite and Toolebuc. We have a situation where those people are swinging in the breeze. We are having discussions with the Victorian Government about that next week.

The Hon. MICHAEL VEITCH: Would you talk the Committee through the impacts on growers of the National Competition Policy? You talked earlier about the code of conduct and in response to a question from the Chair about the Australian Competition and Consumer Commission's [ACCC] guiding statements around that code of conduct. How do the national competition policy principles apply to the code of conduct, the South Australian Act and some of the other aspects of the operation of a business in this industry?

Mr McKENZIE: My understanding is that we have a clean bill of health on all those calls. My understanding is that the South Australian Act has been looked at by the Feds, by the ACCC, and it is considered to be valid. I can only go on that as a guide of what we can take forward. The other issue, and I will go back a little bit in history, relates to a large New South Wales-based wine production entity, now Australian Vintage Ltd, originally McGuigan Simeon Wines, who caused a change in the commercial arrangements in the industry in 2005 and 2006 by suspending contracts. The way they did that was they referred to small print in the Growers Guide, which was not available at the time those contracts were signed. To add insult to injury, having had their supply suspended and no payments made in two vintages, the company then threatened legal action to its remaining growers in the third year when they were short, which was the 2007 year. So we have the situation where effectively they changed the position where they slashed prices and went into what was clearly an exploitative or manipulative contract arrangement.

The ACCC has said there is no issue with the code because there are other voluntary codes. I think that is largely the area that they are interested in: Is it voluntary or not? Does it apply to everybody? If it is voluntary, a winery is signing onto it of its own volition. It is largely why we went into trying to codify this behaviour because of exactly what happened there. We certainly do not see any issue there. However, in the context of McGuigan Simeon, it took the ACCC three years to decide that there was no unconscionable conduct. I know the legal definition of "unconscionable conduct" is extremely difficult. But our view is, and my candid view is,

that we would certainly wish the ACCC was more focused on the rights of producers as well as the rights of consumers, and I would leave it at that.

The fact that the ACCC has allowed Vintage Traders Australia to be registered as a collective marketing group of wine grapes would indicate that they are not, again, a collective action within the industry per se. I think the basis of our submission here would indicate quite clearly to the ACCC that we have not just market failure but we quite clearly have disproportionate market power that is quite clearly being exercised by wineries and, unfortunately, in some cases in an exploitative manner. So I do not really see any issues around national competition policy apart from perhaps wishing that the policemen who are involved with the ACCC were a little more focused on the leverage and the quite clearly different levels of market power that are in the hands of growers versus wineries.

The Hon. SOPHIE COTSIS: I just wanted to understand a little bit better and get more information about the retention of title clause in grape supply contracts. Could you elaborate a little bit more on that?

Mr McKENZIE: The ROT clause, as it is called generally around the traps, is something that is specified in the code, but, of course, we have very low code signatories. Wineries generally—in fact, I am not aware even amongst any of the code signatories, including the three large code signatories, that they have a retention of title clause. On the basis of that, Murray Valley Winegrowers decided, prior to my joining the organisation late last year, to have one developed as a potential guide to growers to negotiate with wineries for inclusion. In fact, it is appendix 4 in the submission, which was the retention of title clause developed by Finlaysons' wine lawyers in Adelaide.

I think it is interesting that the company secretary and legal counsel for Orlando Wines, who is a lawyer, thought it was an excellent clause but they have no intention of inserting it, because traditionally what happens is that title, if it is not defined within a retention of title clause or by another clause or measure within a contract that is agreed between the parties, generally their ownership of the goods changes at the weighbridge. So once it is tipped and it is in that crusher it effectively is assumed ownership by the winery. The reason for pushing this is simply because of the level of disastrous financial failure and the debt owing to growers over the last eight years in our region alone. When you are looking at something in the order of \$20 million that has been owed to growers through the failure of four significant entities then I think we have got to a position where growers are making nothing or only a bit, and then to be in a position where they find themselves without any status as a secured creditor, having delivered the grapes, was, in our view, untenable.

That is why our view is that the code is a good platform. There is provision with the code that if there is a retention of title clause it should be clearly stated. The wineries were clearly not going to move to insert one. Given that our growers tend to deal individually and not collectively with wineries, they have got to be pretty game to put it up, but we are hoping that more and more of them will, and we will certainly be pressuring wineries on the back of this process to take on a retention of title clause as well. But our preference would be to have regulations that have a retention of title clause—either that one or a simpler form, but as long as there is a retention of title clause.

It is clear that an average crush load of 700 litres of wine from a tonne of grapes, certainly in our region—and we really only get paid across two in our region and most inland regions, D or E grade fruit. So there is not an issue around "we have high-value fruit that went into that blend". You can very easily correlate back what is still owed, what that is calculated against by way of tonnes and then by litres, and you can come up with a factored per litre price. We do not see that as particularly difficult.

CHAIR: One thing you just brought up was about the wineries and their stability, if I can put it that way. Is it now time to revisit the fidelity bonds that were once in place particularly for people in, say, the Sydney markets?

Mr McKENZIE: I would probably have to take that on notice. To turn it back in on itself a little bit: I had discussions with senior management of Foster's—now Treasury Wine Estates—last week. We believe they are in breach of the code which they are a signatory to; they do not believe they are. We are going to send it to the Code Administration Committee, which is based here in Sydney, for its view—probably informally—of what the position is about zero-price contracts. Our view is that the code says quite clearly that there should be either a fixed price or a clear statement of how the final price, and particularly market price, is determined. They said to us, "Well, at least we pay". So we do not know what we are going to be paid but they are quite right, they do have a good history of paying and they pay a third, a third, a third. But the fact is that it is not a lot of surety

for growers, and the reason why a significant number of growers have signed their new zero-price contract is probably fundamentally that, that at least we know that they do pay.

The first sign of difficulty quite clearly is when you see either a unilateral or an agreed variant in payment terms. It is the first sign that a winery is in trouble. So part of the role we play is to advise and we stay very closely in touch with what is happening across the grower base. We are getting information back directly from growers on a constant basis and we are then able to advise. The other thing that we have with the three major companies in the region is a grape liaison committee. We have a group of growers who liaise on commercial issues with three major winery groups, not including Australian Vintage unfortunately.

The Hon. SOPHIE COTSIS: In your submission you suggested earlier communication of indicative prices and you were talking about that. What is the current arrangement?

Mr McKENZIE: The current arrangement for code signatories for, I call them Foster's, Treasury Wine Estates, Constellation Wines and Orlando, who are operating in the area, they are bound under the code to give indicative prices—not binding but indicative—by 15 December. That also applies in the Hunter Valley. They then, for the rest of the country, under the code would advise prices by 15 January—indicative again. The final price under the code needs to be advised prior to harvest. In the code we indicate, and it is contained as an appendix to the submission, preferably 10 days before. We know under annual contracts where they are looking to top up that it is not always possible; we understand that. So, from our point of view, the indicative price is just that—it is indicative, it is not binding. But you have effectively done the work on the crop. We have seen earlier and earlier harvests. In the first week of January last year we were into sparkling wine base grapes. So you have got an indicative price on the 15th. If you do not like that price or you believe that it is not appropriate you have got almost no time to dispute it, even under the dispute resolution procedures within the code.

When we negotiated the code with the major wineries we argued for as early as possible. We started with June—no, can't do that. We then went to September—no. October—no. We eventually got agreement, as a compromise, around 15 December. This is the way they have always operated. They sit there and wait for somebody to break from the pack to advise an indicative price or a market price for a variety and then they all fall in line. Generally they line up pretty much with the major companies. Australian Vintage will come in under the major companies because they provide a lot of secondary wine, they process a lot of wine for those major companies or sell it into the bulk market—there is an on-sale to other wine producers as well as their own brands. Then the second-tier wineries generally will drop in underneath that at \$25 to \$50 a tonne less.

That is the way it works. Effectively, by bringing forward the indicative price schedule it not just sends an earlier commercial signal in a failing market environment to growers but I think is going to shake out how wineries look at the way they assess their prices as well. As I said at the outset, the wineries know in May of each year what they have allocated in their budgets and how to approve for grape purchases. They know how much they have got to spend. They know on a per tonne by variety basis pretty much within a few dollars of the sorts of price provision. So by holding onto that price information as long as possible with a perishable product that has to be harvested or it will go off on the vine and it has to be delivered, they really have the whip hand, and that is the difficulty that our growers face. So earlier indicative prices at the very least, although not binding, are going to send a clearer commercial message to our growers.

Reverend the Hon. FRED NILE: It seems as if you are almost arguing for a mandatory code. If we recommended a mandatory code, that would have to be an Act of Parliament to give it the power of enforcement.

Mr McKENZIE: I think that ultimately you would have to say on balance that the voluntary approach of the code currently has failed. We have been asked to give it a further couple of years. I think that the mountain that we are setting, given the very limited uptake of the code at this point on a voluntary basis, is going to be hurdled. The mandatory code would be the most appropriate way forward probably, and what we are asking for here by minimum provisions simply reflects the horticulture code of conduct. So it probably needs to be a Federal instrument. But effectively we are saying we need to mandate some of those provisions, yes.

The Hon. RICK COLLESS: You commented that there is a shortage of Chardonnay at the moment. What is the reason for that shortage? Was it the removal of wine grapes from the industry for Chardonnay?

Mr McKENZIE: The shortage is around particularly in our region and the Riverland, who are the two predominant producers in the warm districts, which forms the major basis of Chardonnay production. The reason for it is we have had four years of savage downturns in prices and signals by wineries, "We've got too much". Faced with water shortages the growers in our region, given that the Murray Valley at its peak was 40 per cent planted to Chardonnay, of the variety they were least likely to water, most likely to top work, most likely to walk away from or to pull out is the Chardonnay. So we have overcooked it.

CHAIR: They have made the decision to say, "We haven't got enough water; Chardonnay is the first to go", or something like that?

Mr McKENZIE: Cabernet gets it, Chardonnay does not. That is simply a factor of the marketplace at the moment. So yes, we have overcorrected and we have overshot the mark and now they are screaming for it and there is not enough there.

The Hon. MICHAEL VEITCH: The code of conduct makes interesting reading. It is reviewed every three years but how long are you a signatory for? Forever and a day?

Mr McKENZIE: You can opt out at any time. Effectively, once you sign it you are in signatory to it until such time as you opt out.

The Hon. MICHAEL VEITCH: Or are kicked out?

Mr McKENZIE: Or kicked out if there is a breach, that is right. But there are provisions in there around breaches and that is why we might go to the administration committee on an informal basis first-up around these zero-price contracts without clear definition of final or market price.

CHAIR: Would you like to add anything that perhaps you were not asked?

Mr McKENZIE: Thank you, Chair, but, as you can hear, I can talk at 100 miles an hour and we have covered a fair bit of territory. I thank you for the opportunity and thank the Committee for its forbearance.

CHAIR: I thank you on behalf of the Committee for your contribution this morning. There will be other questions that we would like to put to you. Could you respond to those within 21 days after you receive the questions?

Mr McKENZIE: Absolutely, Chair. I will give you a cast-iron guarantee of that. I will let my office manager know that is the way it works and she will keep on my tail.

(The witness withdrew)

SCOTT VIVIAN DAVENPORT, Chief Economist, Industry and Investment New South Wales, and

STEWART RICHARD WEBSTER, Manager, Industry Policy, Industry and Investment New South Wales, sworn and examined:

CHAIR: Are you conversant with the terms of reference?

Mr DAVENPORT: Yes.

Mr WEBSTER: Yes.

CHAIR: If you consider at any time that certain evidence you wish to give or documents you wish to tender should be heard or seen only by the Committee, please indicate that fact and the Committee will consider your request. Would you like to make an opening statement?

Mr DAVENPORT: I thank the Committee for the opportunity to present Industry and Investment's submission. Section 1 of the department's submission outlines the changing nature of regulated marketing in the Riverina since the 1930s, which has continually focused on meeting the needs of the large number of small growers in the region. An important feature of these regulatory changes has been ongoing efforts to ensure New South Wales regulation is relevant to wine grape market developments more broadly, hence the move from a one-size-fits-all regulatory framework to one supportive of marketing arrangements suited to the needs of individuals. At the same time, certain safeguards have been provided through the board's minimum term conditions.

In considering the issue of price formation, the department's submission contains information about the demand and supply conditions facing the industry. In regard to Riverina wine grape supply, it can be seen from figure 2 in the submission that prices have been falling over the past 10 years while production has doubled over the same period. Figure 3 shows that in terms of wine grape demand, domestic and export sales of wine have increased steadily over the first half of the decade but then have levelled off. Since the sales peak in 2007, export volumes have steadied and the value of export sales has decreased with the rising value of the Australian dollar and increasing competition in the main United Kingdom and United States markets. The outcome for the Riverina of these changing supply and demand conditions has been a halving of the normal price paid since 1999.

Importantly, with increasing wine grape supply relative to demand, intra-varietal price differentials based on quality attributes have also widened over the past 10 years, as detailed in table 2 in the submission. Much of the intra-varietal price variation can be explained by quality differentials. But even where variable prices have been paid for grapes of the same quality, feasible explanations include inter-winery differences in the levels of stocks on hand or different marketing opportunities. Intra-winery price differentials can also be explained by a willingness to support preferred growers in order to maintain minimum levels of future supplies of preferred grape varieties and qualities. Growers who deliver grapes to the spot market without any form of price assurance are likely to be disappointed with the eventual outcome in the current market circumstances. However, spot market sales should also be viewed as a normal component of most markets. For example, in times of buoyant supply conditions, some growers may prefer to shop around for the best price rather than be tied to a particular contract arrangement. Increased production combined with changes in consumer tastes and preference has therefore given rise to a dynamic and evolving Riverina wine grape market, and one requiring unprecedented levels of business acumen by growers.

In regard to the role of the Wine Grape Marketing Board, the board's industry service functions include the development of a code of conduct for contract negotiations between wine grape growers and wineries, the development of draft contract provisions in respect of the sale of Murrumbidgee **Irrigation** Area [MIA] wine grapes to wineries and the promotion of private contracts for the sale of MIA wine grapes to wineries by wine grape growers. Both the code of conduct and the development of template contract provisions are a recognition of growers who have historically relied upon the board to undertake grape marketing potentially needing initial assistance in negotiating with wineries. Importantly, these tasks assigned to the board are seen as necessary steps in establishing those marketing arrangements that will ultimately offer the best opportunity for a profitable and sustainable wine grape industry.

However, we should not lose sight of the board's other service functions and the critical role they play in strengthening the productivity and competitiveness of growers in the current climate and into the future. Those functions include the provision of marketing industry information, research and development into plant health, education and training in relation to wine grape production and marketing and promotion of MIA wine and the wine industry. There is an ongoing need to ensure that these strategies are all closely considered, monitored and adapted as we go forward.

In regard to collective bargaining and codes of conduct, the department's submission outlines the approach being pursued by the board by way of adoption of the voluntary Australian Wine Industry Code of Conduct, which was launched in December 2008. Collective bargaining is also briefly discussed in terms of the possibilities provided to producers through the authorisation process in the Trade Practices Act. The department's submission also comments on other measures that may be relevant to the inquiry and draws attention to the critical role that good information plays in facilitating industry adjustment. Growers clearly need access to good information about their financial position, both currently and into the future, and about the various adjustment options open to them. The current industry circumstances also point to the need to consider whether there might be new production and marketing strategies better able to exploit all possibilities in the wine grape market over the medium term.

In conclusion, key points made in the department's submission are that the present difficulties being experienced in the wine grape market appear to relate primarily to high levels of grape production in the face of steadying wine demand. This is an environment where grape prices will exhibit wide variation as wineries meet capacity requirements but at the same time seek to maintain strong relationships with those growers who can deliver consistent quality of preferred varieties at preferred volumes. Rather than going backwards to price regulation that insulates growers from contemporary adjustment pressures, there is a need to go forward by maintaining a strong focus on identifying efficient adjustment pathways and, as part of that, considering new production and marketing strategies that might put industry on a more sustainable footing in the future.

Finally, and perhaps of most relevance to the inquiry, it is implicit in the regulation in New South Wales that the Government has placed heavy emphasis on transition by growers and helping them to do that by way of the development of a code of conduct. The Committee has heard some discussion of that this morning. Significant effort has been made by the industry to develop that national code. All of its provisions are generally thought to be very reasonable. We therefore believe that a focus for the review should be progressing thinking, seeking Commonwealth and Australian Competition and Consumer Commission perspectives on how that code can be progressed and garnering greater support from industry. Ultimately, where that leads us is where it will lead us. Codes are very useful in terms of achieving that transition and more temperate bargaining arrangements. Clearly, it would be preferable if that were done at the national level. New South Wales has sought similar approaches for other industries. However, if that fails to achieve anything worthwhile, the New South Wales Government has previously looked at these issues from a fallback perspective.

CHAIR: Are you aware of any existing mechanisms that would allow growers to strengthen their bargaining position?

Mr DAVENPORT: There are clear precedents with authorisation in, for example, the dairy industry, and various other industries have also gone down that path. There are various codes of conduct. Members are aware of the horticultural code of conduct. When it comes down to very direct options around pricing specifically, I think the Trade Practice Act and associated authorisation of sanctions or mandatory codes is a reasonably well-worn pathway and certainly an option that has been used before.

However, if we broaden our thinking, I would like to comment on the longer term prospects of the industry and ensuring that it is picking up on future market opportunities and ways to differentiate its product. For example, there are issues down the track such as water, carbon, environmental sustainability and so forth. From a longer term perspective, putting the price issue aside for the moment, quite a few initiatives have been implemented where growers are looking at formal accreditation processes around their production and marketing strategies and trying to pick up the triple bottom line sentiments that are emerging in the world around social, environmental and economic credentials. For example, the Wine Grape Growers Association has implemented a scheme, as have New Zealand wine grape growers. Growers sign up to do certain practices in the area of social, environmental and economic credentials. Ultimately not only does that exploit all possible profitability opportunities, but one would also like to think there is potential for price premiums within that sort of model.

That is a longer term strategy, but we also have short-term approaches to prices, which largely involve things such as authorisation and mandating of codes of practice. However, we are dealing with a very volatile environment. The MIA grape industry is facing a lot of change; in fact, it is already changing a lot. We need to ensure that it is picking up on all the issues that it will confront, including carbon prices. It must have a process in place to maximise every possible opportunity.

Mr WEBSTER: The Commonwealth Trade Practices Act has provision for the Australian Competition and Consumer Commission to authorise a number of things. Mr Davenport referred to collective bargaining in terms of enabling collective action under that Act. The Act also provides for mandating the code of conduct, which has been done with the horticultural code of conduct. The only other collective action I can think of is the cooperative approach to which the previous witness referred. That would be under State law.

CHAIR: That was going to be my next question. Is the department aware of other industries that have set up successful cooperatives?

Mr DAVENPORT: Not so much cooperatives but I think the examples I gave you is probably the best way I can answer that. There is quite a lot of precedent now for grower associations, growers in particular regions, to be starting to look at these various ways of environmental and social integrity of their product. That is an emerging area and it will be interesting to see how that proceeds and how successful it is. Certainly as well, when you visit some of the key wineries in Australia, they are driving back through those sorts of schemes to their growers as well to try to develop better brand integrity, if you like. Some of the Barossa-based wineries, for example, have quite detailed schemes whereby their growers basically have credit points around the management of the vineyard more broadly, production practices and so forth. It can come as a driver from wineries to try to get a more differentiated product ultimately and a premium in the market or associations, growers themselves as a body, starting to pick up some of these schemes as well

The Hon. RICK COLLESS: Can you tell us what the structure of the existing Wine Grapes Marketing Board is? I understand it is substantially different from what it was previously, since the 1988 Act? Can you describe to us how that operates now and what the structure is, and so on?

Mr WEBSTER: The structure or the powers?

The Hon. RICK COLLESS: I am interested in all of that. Whatever you feel is appropriate. If there is something you have not covered I will ask you another question.

Mr WEBSTER: The structure of the board itself, I believe seven members are elected by constituents. The board is constituted to cover the Murrumbidgee Irrigation Area only in New South Wales. Its functions are contained in the Agricultural Industry Services Regulation 2009. I will not read them out, but they are listed under clause 9. There are quite a few there but they dwell on a number of areas. The first three relate to what we have been talking about: The development of a code of conduct, contract negotiations between wine and grape growers and wineries, contract terms, that kind of thing. Another major area is collection and dissemination of market information, conduct of research and development, particularly in relation to plant health; education and training relating to wine grape production; the promotion of Murrumbidgee Irrigation Area wine and wine grapes; and representation of the wine grape industry in relation to those functions. That is what its present functions are.

Up until 1999 it had vesting powers, which are a peculiar historical instrument that effectively means that wine grapes I think once picked are the property of the board rather than the growers who grew them. That was a mechanism to allow the board to act as a single seller, a single desk regionally. That is the primary difference between what it had then and what it has now. Because it was the single seller, it enabled it to do some other peripheral things like determine the statutory terms of payment, conditions of payment.

The Hon. RICK COLLESS: How does it operate now? Who does it report to? Is it mainly advisory or are there certain regulations growers have to abide by?

Mr WEBSTER: My unit is responsible for the supervision of the State's remaining agricultural statutory authorities of which there are only three left. That is only from the point of view of ensuring that they stick to their legislative functions. The Auditor-General is responsible for their financial auditing. The board itself is responsible to its own constituents in regard to what it does. It provides its constituents at its annual general meeting with a rolling five-year plan and the constituents vote on whether they will accept that plan or

not. In that same process they determine what the board will charge as the per tonne levy on wine grapes for funding its services to growers. So, its sole focus really is the provision of industry services to its constituents.

Mr DAVENPORT: If I could add a bit more conceptual comment, we went from vesting as a traditional statutory body to competition and policy having its way and reform occurring whereby vesting was taken away. Stewart has mentioned, though, what is referred to as industry service functions. Essentially what that means is the market failure, if you like, that was perceived to continue to exist was that certain things would be underinvested in by individual growers, better undertaken by groups of farmers, so the compulsory levy powers were provided to industry to do that. The Agricultural Industry Services Act, as per its name, is essentially a fairly contemporary piece of legislation that tries to address that specific issue. So, if groups of growers agree, there are polling provisions, et cetera, to get a levy up, and Stewart has outlined the rolling five-year plan that needs to be presented to those constituents to have them agree to continue to have that money levied from them, and they get a say in how it is spent. That has been an important change.

The other thing Stewart probably should talk about is the complying contracts. We have not spoken about contracts and their role in that area. Essentially, again, in trying to encourage good contractual arrangements, there is a term called complying contracts. If two parties have a complying contract they become exempt, if you like, from the default provisions of the Act and which the board oversees, and those complying contracts, without going into the detail, have many of the same nice provisions that the national voluntary code has—probably picked up from this Act. So the board will have data, for example, on a number of complying contracts held out there by growers and non-complying contracts, if you like. Those default terms and conditions, unless you have a complying contract, are a bit of a safeguard. Otherwise, it was designed so they would be proactive over and above that with the code and the contract template provisions, if you like. Other than that, they just do their traditional services functions.

The Hon. RICK COLLESS: I could not help but notice in your submission that a feature of the changes under the Agricultural Industry Services Act was to support the development of marketing arrangements suited to the needs of individuals rather than the one-size-fits-all approach. While we all applaud that type of approach what are your comments on the effectiveness of that approach? If we look at the average prices that have been received since 1999, the average price is now a third of what it was in 1999 and the minimum prices have gone down to about a fifth. So, the producers have not benefited by that process, have they? They are receiving much lower prices now than they were 10 years ago?

Mr DAVENPORT: Sure. A couple of things are happening here, though. One is this international circumstance with the market where prices in nominal terms have been going down for 10 years. So we have had a gradually increasing supply situation, finally levelling out demand, so I think we probably need to try to separate out that general price effect that is going on there from what the provisions of the legislation might otherwise enable individuals to do. One of the difficulties we all have at the moment is trying to unravel those two effects. We are possibly looking at trying to strengthen the pricing and contractual arrangements of growers at a time when we all acknowledge that prices are otherwise on the decline a little bit.

Within that, we need to be mindful of whether we are talking about just price declines due to those international market conditions or we are talking about unconscionable conduct. That is a very key distinct point to try to look at to see what evidence there is of unconscionable conduct as opposed to wineries just normally meeting, as was said in our submission, capacity constraints. I think we can all understand they are not going to take in an endless supply of grapes in the current circumstances. They are going to develop preferred suppliers and so forth. So, it is a complicated circumstance we are in where we are trying to see whether there should be better pricing arrangements.

Having said that, I think there is strong industry support for the code. The industry has moved along and from many of the submissions it does not want to go back to regulated pricing, it wants to go down the contractual path, more or less, and it is simply wanting more reasonable approaches on both sides. I take it as a gauge. If industry is keen to go on that path, it is feeling that is where the benefits are for it in this environment.

Reverend the Hon. FRED NILE: I note in your submission—and it has some good information in there—about pursuing the option of making a national code mandatory. Do you feel there is no role at the State level or it is impossible to have a State mandatory code if our Committee recommended that?

Mr DAVENPORT: Nothing is impossible.

Reverend the Hon. FRED NILE: Would that be faster, would that get a quicker response?

Mr DAVENPORT: The problem is whenever you do one thing in one State you always worry that you might penalise growers relative to activities that might then occur elsewhere. If a code is mandated—to take an extreme example—that processors were not particularly enthused about, would that mean that the pricing side of the equation might be a bit more detrimental in New South Wales than elsewhere? There was a bit of discussion this morning about indicative prices, and I will just go off the track here for a moment. New South Wales did have an indicative price requirement earlier.

Mr WEBSTER: It was introduced in 2003, only in the Riverina.

Mr DAVENPORT: This was a fascinating outcome in the sense that we all for the same reason thought that would be a good idea. Again, what happened was the industry became dissatisfied with that because the indicative prices that were being posted were meaningless. The processors did not want to put the actual price so they put fairly low prices. My point here is with national-State we have to be careful that we do not end up penalising our own industry and have adverse outcomes. That is why we have sought in principle to get these things done nationally but it certainly does not preclude the State otherwise obtaining the right to do something.

Reverend the Hon. FRED NILE: In your submission you made reference, while this is an option, if growers fear retribution they may not exercise their rights under a mandatory code either. Have you any evidence of that fear of retribution? Is there any pressure on the growers?

Mr WEBSTER: No firm evidence but we have been told by people on the growing side of the industry over numerous years that there are things like black lists, troublemaking growers will not be dealt with by wineries, that sort of thing. I daresay you will hear the same, and you would not be the first inquiry to hear that. But it is difficult to get firm evidence of it because of its nature.

Mr DAVENPORT: I would have to say we are not directly involved at that level. We have had many direct representations but from an operational perspective we take it as hearsay generally, as you would.

Reverend the Hon. FRED NILE: Is there any strong opposition to a mandatory code? If so, where would that come from?

Mr WEBSTER: The opposition would come presumably from wineries, which have shown a general reluctance to get tied to certain business practices, and I think that is understandable. Trying to run business flexibility is valuable.

Reverend the Hon. FRED NILE: In your submission you quote the review of the voluntary code and Neil Buckton and Associates said they were surprised there has been no effort to develop collective negotiation provisions for the growers to use that; in other words, they combine together against the power of the wineries. Is there any reason why they do not do that? Are they all competing with each other too much?

Mr DAVENPORT: All I can do is refer you to the board's own submission where they basically put a view that growers actually do not seem to want to work closely together. I would have to leave it at that as to how that could otherwise pan out if you did go through the authorisation process and if they could see what was happening perhaps and see the potential benefits there, perhaps that would not be such a problem. I can only refer you to that submission.

Reverend the Hon. FRED NILE: We have had a lot of evidence about prices going down or collapsing from the growers' point of view. Is that reflected in the retail industry in the marketing of wines?

Mr WEBSTER: I am not so sure about the retail industry but certainly on the wholesale side, there is good evidence that the price per litre obtained both domestically and on export markets has fallen dramatically over the last three or so years. There are a number of submissions that have quite a bit of data on that.

Reverend the Hon. FRED NILE: Is it possible, though, that the retail end is still making larger profits then?

Mr WEBSTER: I could not say in that we do not regularly monitor retail prices but there has been a move towards house brands by the large supermarkets and that is often cited but I have no direct evidence of that putting downward pressure on retail prices.

The Hon. MICHAEL VEITCH: Mr Davenport, in your opening comments—and I do not want to verbal you so if I have the words wrong, please correct me—you spoke about the need for efficient adjustment mechanisms within the industry. Can you give some examples of what an efficient adjustment mechanism would be that for this particular industry?

Mr DAVENPORT: Australia has a history in agriculture policy of governments having in place various programs to facilitate adjustment—areas like drought policy are typical. There are a couple of dimensions to that. Adjustment is all about farmers making good decisions so that they are there for the longer term; they make efficient decisions to do other enterprises or leave the industry at the optimum time when equity is not unnecessarily eroded and so forth. So when we think about those normal business decisions they face, first governments have had strong intervention or persistent intervention in the areas of education and training—training programs—programs where farmers can find out exactly what their financial circumstance is and perhaps how that will pan out going forward. I am sure you are familiar with some of those, so efficient adjustment programs to make sure that government and industry are getting those programs into the hot spots at the right time at a nice early stage.

There is quite a lot of discussion around drought policy now and trying to make sure at a very early stage and not just in drought now we are getting farmers well informed about how they are placed in terms of risks and so forth. I think given the circumstances of the wine industry as we all know it now, you have arguably got quite a hot spot in terms of we need to make sure that there are good programs going through there and boards, governments and everyone plays a role there. The Commonwealth plays a role as well. There is exit assistance as well. The Commonwealth—and Stewart may know a little more about that—has traditionally had exit programs in place. For the horticultural industry at the moment we could usefully ask whether those programs have the right settings or could be looked at.

Also in terms of adjustment, I alluded to earlier the pressures that will come to all industries, not just wine, and if we pick a couple like water, carbon or whatever, these are things where you really need to be not only making sure those programs I have spoken of are in place and are right but things like research and development and so forth are focused on those key issues so that farmers in their typical way traditionally in terms of decline in trade have increased their productivity—and I mentioned the words "productivity" and "competitiveness", so that all those things are working. Let us go back to research and development. With the wine industry, just to stick with that example, if carbon and water are going to be an issue, we need to make sure that we have programs that are strategically and proactively very much focused on those issues now and looking at our portfolio of effort there, whether the industry or government are continuing to ask the question: are we getting the right information out there so those production costs can be kept down and our farmers can respond to new technologies and so forth?

The Hon. MICHAEL VEITCH: As part of an efficient adjustment mechanism—and Reverend the Hon. Fred Nile raised it and it is in your submission—the Buckton review spoke about the lack of use by wine growers of collective negotiation provisions. In light of all that, is the department in any way educating or encouraging collective bargaining arrangements?

Mr DAVENPORT: In this particular case we have tried not so much to look at collective bargaining but, through the code development, to try to encourage the industry to look at whether that is going to be a reasonable solution. As I said earlier, it tends to be a step-wise progression here rather than just jumping to an endpoint to make sure we have the least heavy hand that government needs to have to solve the problem. The question was asked earlier about the progression of the legislation. I answer by drawing your attention to that is where the Government or the department most recently has seen the opportunities. Certainly authorisation is consistent with competition principles and I can see no reason why, from a departmental perspective, we would not be happy to see that.

The Hon. MICHAEL VEITCH: You mentioned the code of conduct and the department submission speaks about the horticultural code of conduct around pricing for fruit and vegetables in particular. Is there a variation between the wine industry's voluntary code of conduct and the horticultural code of conduct and, if there is, from an economist's perspective what would you like to see in the wine industry's code of conduct if it

were to be made mandatory? Are there some lessons from the horticultural code of conduct that we can take on board?

Mr WEBSTER: I am not familiar with the terms of the horticultural code of conduct because it is not within my area of responsibility. In terms of the differences between the two, we could certainly take that on notice, if you would like?

The Hon. MICHAEL VEITCH: Yes.

Mr WEBSTER: In relation to your previous question, I would just point out that some of the core functions of the Wine Grape Marketing Board, at least in the Riverina, are for instance the provision of education and training in relation to wine grape production and marketing as well as the code of conduct type activities, so while the department may not be directly providing that kind of training, one of the reasons is that it is the responsibility of the board to do that, at least in the Riverina.

The Hon. MICHAEL VEITCH: To be relying on them to do it?

Mr WEBSTER: That is why they have been given the ability to collect the levy and to conduct these sorts of activities.

The Hon. MICHAEL VEITCH: Your submission talks about the New South Wales reform agenda. I have asked a question of previous witnesses this morning about the national competition policy impacts on the industry. I quote the statement on the last page of your submission where you say, "Finally in relation to the option of returning to regulated prices not only would such an option be in breach of the New South Wales Government's national reform agenda commitments it would also harm the industry." Can you talk through this a bit more? I would like to tease out just where it breaches the New South Wales Government's national reform agenda commitments but also what you would see as some of the issues for the code of conduct and other industry practices in relation to the national competition policy? Feel free to take any of that on notice, if you wish?

Mr WEBSTER: I will have a go at it. My unit has quite a bit to do with national competition policy reviews. There have been a number of agreements but the relevant one now is what they call the national reform agenda [NRA], which New South Wales signed up to, I think in December 2008 or maybe it was 2007. I know it is due for review in 2012. Essentially the agreement itself deals with a number of specific industries and agriculture is not in there but it also reaffirms the commitment of all the jurisdictions to the competition principles agreement, which was a far earlier agreement but was updated, I believe, in 2007.

The thing about competition principles is that to the layperson who reads it, it is not immediately obvious how things like price setting, for instance, would fit into it, but I suppose if you consider its clause 5 and the subsections underneath that, that is the main area of relevance here. Its guiding principle is that legislation should not restrict competition unless it can be demonstrated that the benefits to the community outweigh the costs and that the objectives of the legislation can only be achieved by restricting competition. All of the competition principles sort of rely on the concept that was mentioned earlier on market failure.

The reason that we have AIS committees in New South Wales is because there has been market failure—and there are about half a dozen of them identified, and those committees are seen as the least competition restricting way of dealing with those market failures. The kind of markets you might be interested in here—there are two of them—is what they call imperfect competition, which is your market power discrepancy and there is also possibly an information asymmetry market failure, which is where one side of a deal knows more than the other side.

Competition principles agreements are pretty clear. Governments have a responsibility to first determine if the market failure is great enough to warrant intervention because all intervention has cost associated and, as it says, the costs have to be outweighed by the benefits. Secondly, just because you think that there is a market failure that you could do something about and in doing so derive a benefit for the community, it does not follow that you can pick the most powerful intervention off the shelf. You should pick the one that will deal with the market failure with the least cost associated with it.

That is the basis of the removal of vesting in most cases all around Australia for the old statutory authorities because that was considered to be a great big stick and unnecessary to deal with the market failures

involved and so in terms of, say, the reintroduction of price regulation which is being mooted in some of the submissions, from my personal opinion, based on experience I have had national competition policy reviews, that is highly unlikely to meet the New South Wales obligations under competition policies agreement.

Mr DAVENPORT: If I could comment just quickly and then let Stewart continue, the market failure that we are talking about here is that unconscionable conduct issue, so we can refine our focus to that, and perhaps the comment has basis in terms of all other reviews. The Commonwealth has always taken a strong view that that is what the Trade Practices Act is there for. I suppose if you could otherwise mount an argument that direct price regulation is somehow better than the Trade Practices Act, that is potentially what you would have to do. I think that is sort of getting to the nub of the answer to your question.

Mr WEBSTER: I will just point out that no State has statutory price setting for wine grapes. The South Australian Act, which was mentioned earlier, allows for indicative prices to be gazetted by the Minister, but they are indicative, they do not really hold any weight, and it is no doubt for the reason that direct intervention in pricing would not be consistent with the competition principles agreement—not to mention not a very good idea economically. If you set a price above a market clearing rate then you will end up with what we had in the case of the wool industry—a huge stockpile—and stockpiled grapes do not keep real well.

Mr DAVENPORT: And I think the industry is concerned about the further effects that we discussed earlier. If we can set regulated prices in the MIA, what response is that going to elicit from processors? Are they going to suddenly say, "Well, I will go and buy my grapes elsewhere, thanks very much", so we actually work to the detriment of our own industry? Some of these push and pull issues are very tricky.

Mr WEBSTER: These days the old system of vesting and original defence mechanism will not work because these days there is refrigerated transport and you can trade in must or wine as well as raw grapes. What worked in the 1930s probably will not work now.

The Hon. SOPHIE COTSIS: What is the contribution of the wine industry in New South Wales and how important is it? Do you have figures in terms of jobs, job creation and skills?

Mr WEBSTER: We would have. I do not have those with me, but I could take it on notice.

The Hon. SOPHIE COTSIS: I would appreciate that. There are assertions in several submissions that some winemakers engage in unethical commercial practices. Did you want to make any comment on that?

Mr DAVENPORT: I think we spoke about that earlier. We are not in a position to confirm or deny the fact in this area. We are not an operative in the market, so we get all the same representations you have second-hand. We are not in a position to confirm that. The only other thing I would say is that we do not get many representations, formal representations through the Minister through correspondence, about that issue, but again is it because the growers are worried about the ramifications of that and so forth?

The Hon. RICK COLLESS: You mentioned that there are only three statutory authorities left in New South Wales.

Mr WEBSTER: Agricultural statutory authorities.

The Hon. RICK COLLESS: What are they, and do they still have vesting powers?

Mr WEBSTER: The three are the Wine Grapes Marketing Board under the Agricultural Industry Services Act and Riverina Citrus, which is also under the Agricultural Industry Services Act.

The Hon. RICK COLLESS: Without vesting powers.

Mr WEBSTER: The only one that does have vesting is the Rice Marketing Board constituted under the Rice Marketing Act. The sole reason it has vesting is to ensure the integrity of the single desk for rice exports. The domestic market has been deregulated and the board has very little—practically no—discretion as to who it must license as a domestic buyer. They have an authorised buyer system, but that again is only in place to defend the integrity of the single desk. So vesting in that case is not related to price, as such.

CHAIR: Unless there is anything you want to add, thank you very much for your contribution. Could we have your answers to questions on notice and any further questions that might come to you within 21 days of you receiving those?

Mr DAVENPORT: Certainly, we will get right on to it, and thanks to the Committee for spending the time with us.

(The witnesses withdrew)

BLIGH JAMES GRANT, Associate Lecturer, Political Economy, University of Southern Queensland, Toowoomba, sworn and examined:

CHAIR: In what capacity are you appearing before the Committee?

Mr GRANT: I am appearing as a researcher, as a member of the faculty of business.

CHAIR: If you should consider at any stage that certain evidence you wish to give or documents you may wish to tender should be heard or seen only by the Committee, please indicate that fact and the Committee will consider your request. Before questioning begins, would you like to make a brief opening statement?

Mr GRANT: Thank you, I thought I would provide you with an abbreviated summation of the executive summary that I provided to the Committee, if that is alright?

CHAIR: Thank you.

Mr GRANT: By way of brief introduction, in September of 2010 myself and other researchers from my university were approached by several grape growers—and winemakers, importantly—in the New England, Australia, wine region and alerted to the Standing Committee on State Development inquiry into wine grape and marketing prices. While time constraints have proscribed us addressing the terms of reference of the inquiry fully, by way of the submission of two recent publications which are part of this document and more particularly this executive summary we hope to provide information for the consideration and usefulness of the inquiry. The executive summary is henceforth comprised of two sections and background notes, and I will briefly address the terms of reference for the inquiry.

By way of background, firstly I think it is worth noting that the current inquiry by this Committee forms just one element of the recommendations of the wine restructuring action agenda jointly released last year in November by the four winery industry organisations. According to our research based on these documents, that is the wine restructuring action agenda, the analysis of the financial sustainability of certain regions based on the identification of four grades of fruit quality, namely, A, B, C and D, is questionable to the extent that its conclusions and recommendations ought to be revisited. What I am saying there is that what has been referred to this morning as the financial unsustainability of particular regions in New South Wales is questionable, in particular cool climate regions and those temperate regions, according to the work that we have done.

Despite the conjecture and refutation surrounding the wine restructuring action agenda, previous intervention into the wine grape market suggests that any government intervention ought to be very carefully considered. We point to the first paper of the submission in this regard and, in particular, due to the cost structure inherent in the industry and the divergent comparative profitability of the industry across the State, the Government ought not to conflate welfare and structural adjustment objectives of the intervention. Also I must say that any intervention must be considered on a regional and case by case rather than State base. That is our conclusion and I think that will do as an opening statement, if you would like to ask me some questions.

CHAIR: Several submissions have referred to oversupply as the primary driver of unsustainable wine grape prices. What other factors do you see influencing prices in the wine grape market at present?

Mr GRANT: Well, oversupply is the principal reason for the depressed wine prices, but there are other reasons that are basically out of the control of producers, and that is international conditions, which have led to, as it were, a lag in the picking up of demand, grapes that were planted, say, 10 years ago that are no longer sellable in the international market. That is a huge problem.

CHAIR: Are you aware of particular issues in the wine grape market in the Riverina? How does the Riverina compare to other winemaking regions in New South Wales?

Mr GRANT: I think this is the principal point why myself and my colleagues decided to contribute to this inquiry, and that is that it seemed to us that there was not necessarily bias, but there could be particular flow-over effects from the conclusions of this inquiry—which is essentially about pricing in the Riverina—to other areas in New South Wales. We have heard a lot this morning about the Riverina, but we have not heard about Orange, we have not heard about Mudgee, about New England—

The Hon. MICHAEL VEITCH: Hilltops.

Mr GRANT: Hilltops, of course—fantastic chardonnay—and we are of the point of view that anything that was introduced to affect or alleviate the problems in the Riverina could have an overflow effect on what are quite substantial and running interests. They are not very large in terms of aggregate wine producing, but they are contributing quite significantly to rural restructuring, to the vibrancy of some regions which have been not necessarily depressed but at least not showing new areas of growth, and this tampering with the market in the Riverina, and in particular introducing a regulatory structure for that particular region, could have inverse consequences on these other regions which, while they have been going through a little bit of an adjustment—we have seen a few businesses close in some of the areas that I have done some work in, for example—they are still spilling over into not just a wine growing or grape growing industry, but also a wine tourism industry, which is burgeoning in places like Mudgee, places like Orange, the New England and other areas in the State.

The Hon. RICK COLLESS: Can you give us your views on the way grapes are marketed in those other regions, like Orange, Mudgee, New England and so on, compared to the way that the process operates in the Riverina, and how do they compare in your view across the different systems that operate?

Mr GRANT: The crucial thing is that in regions like Mudgee, New England and Orange—I must say that I have traded quite a lot of wine from these regions as a restaurant manager in my life and I am very familiar with these businesses. The distinction between grape growing on the one hand and wine making on the other is significantly eroded in all of these contexts. And it is not just a matter of individual businesses growing grapes and making their own wine. There is a lot of horse-trading within these regions for specific grapes. They are very, very flexible markets that vary over particular seasons. They are quite small businesses. Just because grapes and wine are not the only things they do does not necessarily mean that they ought to be kicked out of the business, as far as we are concerned. That is a very important point. It is really a heterogeneous model. But the main thing is that there is not a split between grapegrowers on the one hand and winemakers on the other. That is what we have been hearing about this morning, and that is where these regions are fundamentally different from the Riverina, I would argue.

The Hon. RICK COLLESS: In terms of the way the growers in the New England region sell their grapes, does that differ substantially from the way the growers in the Riverina sell their grapes?

Mr GRANT: Absolutely. For example, in the New England and also in Mudgee, growers will grow their grapes, pay a winemaker to make the wine for them, then bring the wine back into their cellar door facility and sell it on, or look for wholesale markets. You might have a grower, for example, in Narrabri who is growing grapes that will search for a winemaker, but that is not a typical scenario. A more typical scenario is that people have other sources of income. They will grow grapes, pay a winemaker to make it into wine, and then bring it back to a cellar door facility. That is just one example of selling the product. It is value-added, it is horizontally and vertically integrated, as well as selling grapes on. It is a very, very different scenario.

The Hon. RICK COLLESS: From an industry perspective, is that a preferable model to the situation in the Riverina, where you have dedicated grapegrowers who try to find a contract with a winery?

Mr GRANT: There are two arguments about that. First, we would say that more substantial efficiencies are generated from specialisation. But the people in the other regions, such as Mudgee, New England and Orange, are not the people who are in crisis at the moment. They are not the people who are calling for this inquiry, precisely because they work with lots of different models I suppose. The Riverina growers, in the Wine Restructuring Action Agenda and the supporting documents around that, argue that from the basis of just grape production and wine production, if you look at what our first presenter this morning called the temperate regions—some of which are not particularly temperate, I can assure you—the areas out of the warmer regions, they can be assessed from a strict winegrowing perspective, from the perspective of just that, that they are inefficient. But that is hardly the point, as far as we are concerned. The fact is that they are still economically viable—they are still producing; they are contributing to excellence in the specific industry. They are also in a position to provide grapes, if there is an increase in demand suddenly. That is the point.

The Hon. RICK COLLESS: One of the submissions this morning suggested that the cool, temperate regions were oversupplied. What is your view on that, in light of the comment you just made about their not feeling the pressure like the Riverina is at the moment?

Mr GRANT: I have spoken to several winemakers in cool climate regions in the last 48 hours. For example, one person yesterday estimated that wines in the New England were selling for \$1,000 a tonne.

The Hon. RICK COLLESS: That is grapes?

Mr GRANT: Yes. That is significantly more than the money we have heard about this morning. My answer to the suggestion that these cool climate regions are oversupplied with wine is: Look at the prices they are getting for their product. If they are getting \$1,000 a tonne average, as opposed to \$150 a tonne, I would say they are not overproducing. The arguments we have heard this morning are looking at the industry as a whole. Our argument in the executive summary is that they need to be looked at at a regional level, because the prices are being determined at that level. That is a very significant point.

Reverend the Hon. FRED NILE: Thank you again for your detailed submission. In your submission you have expressed some criticism that a lot of these proposals favour the larger producers against the small producers, almost to push the small producers out, and possibly that the great influx of small producers is what has now given an oversupply. Would you say that is one of the factors contributing to the oversupply?

Mr GRANT: I would say that it is not really a matter of size of business; it is a matter of what people are doing in the business. There is a divergent regional political economy, if I can put it that way, where you have the Riverina arguing for the propping up of one particular model, on the one hand, and all these other regions—well, I am the only person who is here from another region who has done the research ostensibly. Certainly it is the smaller businesses, but also these divergent regions have led to a diversity in the industry. That has been an affront to the Riverina in particular, in a context where there has been lots and lots of downward pressure on prices, but it is not really the other areas' fault, as it were. What we see in the Wine Restructuring Action Agenda is an argument about getting particular kinds of people out of the wine industry per se. They are quite strong arguments, and they are arguments that we would object to. But certainly the strength of the industry is based on the differentiation that it now has, yes.

Reverend the Hon. FRED NILE: But this whole proposal is also pushing the small producers in the Riverina out of business as well?

Mr GRANT: Yes, but we are facing a massive oversupply. The industry has to adjust one way. If some people have to get out of the industry, that is what they have to do. It is the same with anything, whether it is people growing grapes, or people making wine, or whatever. That is just the way it is. As I mentioned earlier, we have seen some natural market adjustment in the New England where it is not as if we are looking at a straight curve going up. There have been people getting out of the industry precisely because some businesses are unviable, precisely because people have realised that it is just not worth it. They have realised that it is a lot of hard work growing grapes and making wine, as opposed to what the Winemakers Federation of Australia recently called the white shoe brigade—doing this just for something to do. So businesses are getting out. People are not just going broke; they are just stopping it because they just do not like doing it. So there is some adjustment, but it is an adjustment that is caused by the market.

CHAIR: With regard to the wineries in those smaller areas you are talking about now, where the growers are averaging around \$1,000 a tonne, why would not the wineries be, say, making a phone call to the Riverina and saying, "Look, I can double the money you are getting. Rather than \$150, I will give you \$300"?

Mr GRANT: That is something that has been preoccupying my mind for the last week, Mr Chairman: How can you make the market more liquid in between the regions? I think this is a very interesting area—indeed, I would like to write a paper on it. As a result of this inquiry, it is something that has occurred to me. But at the moment, obviously, the market is not that liquid between the regions for particular products. I think it would be quite a good thing to do. If I could work out how to do it, it would be in the submission.

Reverend the Hon. FRED NILE: On page 9 of your submission you put what you said is alarming information—that is, the value of wine now imported. You talk about not only how much it is but how it is dramatically increasing every year. It could be 18 per cent of domestic consumption by 2013-14. What impact would that have on the local product?

Mr GRANT: They are Australian Bureau of Agricultural and Resource Economics [ABARE] statistics; they are not statistics that I have done. They came out in 2006. Probably the statistic I always think of is that wine imports into the country for 2008-09 increased by 48 per cent, which is just phenomenal. It is

obviously a significant challenge to the industry, and it is about the industry responding. I think the problem should be addressed at the collective organisations level; grapegrowers organisations should be doing something about it. But also, the Australian Wine and Brandy Corporation is there, and the Winemakers' Federation of Australia is there. They are organisations that have been looking at these issues strategically for quite some time. The 2025 report that was released a few years ago did not consider the issue in that magnitude, but it is certainly on the board of anyone who is in the industry basically. Going from individual producers right through to large industry organisations, people are working on these problems. But they are scary figures, for sure.

Reverend the Hon. FRED NILE: There were reports that the local wines were becoming more popular with Australians, that they were disregarded some years ago. Has that changed again, so that consumers are now switching to imported wines?

Mr GRANT: It is a very fickle market, yes. With these wine trends, it is very difficult to pick winners. Even as someone who was buying wines for a restaurant over a 12-month period, you might say, "I am going to spend 40 per cent of my summer budget on sauvignon blanc", and then three months later everyone is drinking chardonnay again. You just do not know; it is a very flexible market. One of the points we make is that it is difficult to pick winners in this area. You are better off having lots of different producers; it is better for the industry overall. That is our perspective of it, anyway. The people who grow grapes that I know are getting the highest per tonnage price now for things like Würtz traminer, which is essentially a sweet riesling. Five years ago, let alone 10 years ago, if you said that there would be a really, really big trend towards a sweeter style riesling in Australian wine consumption trends, people would just say, "That is just ridiculous. There is just no way that will happen." But it has in fact occurred that people are getting \$1,600 a tonne for cool climate Würtz traminer. It is a very fickle, fashion-driven market.

The Hon. MICHAEL VEITCH: Some would say it is a fad-driven market?

Mr GRANT: Indeed.

The Hon. MICHAEL VEITCH: I guess the cautionary line you are using here, in attempting to address some of the issues relating to the Riverina, is that we do not impact negatively upon the remainder of the New South Wales wine industry?

Mr GRANT: That is right, and that all we are trying to do here, in light of the other submissions that have been put to the inquiry, is to present the contra prospective, which really has not been on the table this morning. I suppose, coming from a regional university—I am from the University of New England and Southern Queensland—we were taught by agricultural economists, who basically say let the market dominate in these instances. But if you have a look at some of the recommendations that have come out of ABARE, for example, the ambit of this inquiry, to examine the relationship between grape producers on the one hand and winemakers on the other, is only one of several recommendations that were put forward by ABARE in a major report in 2006. The recommendations included considering options for increasing the size of farms—for example, exploring the relevance of different business models, which we have canvassed this morning in terms of cooperatives, and so on and so forth. So the ambit of this inquiry is just one of several things that have been considered by ABARE as mechanisms or means to address the problem of oversupply.

The Hon. MICHAEL VEITCH: If you have had an opportunity to read the submissions you would have noticed that quite a few of them talk about the South Australian legislation. Can I take it that your comments relate to the Wine Grapes Industry Act 1981, which is the South Australia legislation?

Mr GRANT: Unfortunately, not all the submissions to the inquiry are available on the website; otherwise I would have read them all. But regarding the ones I have read, I did not canvass that issue. But I will be looking at it.

The Hon. MICHAEL VEITCH: Do you believe that legislation that applies statewide in some way addresses the issue you raised, that is, looking at one region in isolation to the detriment of other regions, whereas if you have broadscale legislation—

Mr GRANT: Without having a look at the South Australian legislation I would not be in a position to comment, but I would be cautious about introducing State-based legislation because it would apply to the whole of the jurisdiction. You are on far safer ground if you revisit and try to firm up the idea of an agreement between winemakers and grapegrowers, but at the same time why not make that region-based as opposed to it being

mandatory and across the State? There is no reason it has to be like that and it could get in the way of relatively efficient markets.

The Hon. MICHAEL VEITCH: Do you have any comments on the voluntary code of conduct that was discussed this morning?

Mr GRANT: Make it voluntary and make it regional. There are regional organisations in place that can push this. If the State Government needs to get behind them to do that, that is fine, but there is no need to try to roll it out across however many wine-producing regions there are in the State, let alone nationally. It just interferes with the operation of markets.

The Hon. MICHAEL VEITCH: With regard to whether the impacts of the National Competition Policy are negative or positive, which I have been asking about this morning, would your view be to maintain the competitive processes?

Mr GRANT: Yes, absolutely.

The Hon. MICHAEL VEITCH: Without restriction?

Mr GRANT: I do not know very much about the details of the National Competition Policy but I found the comments by Stewart Webster in this regard very interesting, in that there were provisions for cooperatives and collectives within Australian Competition and Consumer Commission policy. I think that shows significant nuance in the policy and it ought to be explored by the wine industry and in particular the grape-growing industry.

The Hon. MICHAEL VEITCH: Are you aware of any cooperatives or collectives in the subregions and regions you have been talking about that are in operation either formally or informally?

Mr GRANT: The ones that I talk about in the papers. The legendary one and the one that Scott Davenport alluded to earlier is the one from the Barossa. They had a situation similar to the Riverina and it took someone to stand up and say, "I'm going to take the lead and we're going to form a cooperative instead of just selling our grapes." Peter Lehman basically said, "I'm going to start making wine and I'm going to guarantee you a price for that." That was the basis of it and that is why he is called the "bishop of the Barossa". That is a common fable in the wine industry in Australia; that is the one everyone points to. In my specific research in Stanthorpe and New England I have found no formal agreements. A lot of politicking goes on with the local people going in and out of the local industry organisations and it is very difficult for us to interview them about that kind of thing because it is very significant.

One of the interesting things about the research we have done is there is always a tension between the two models—on the one hand the idea of an individual going it alone and being an efficient producer and differentiating themselves in their local market and, on the other hand, being involved in regional branding, which they think is really important. For example, people in Stanthorpe and New England think it is really important. They all stand up and say, "We have an individual regional profile", but the extent of that cooperation is very limited or is proscribed to the extent that they compete against one another in the local market or when tourists come to the region. That is an interesting conundrum that they have to work out.

The Hon. SOPHIE COTSIS: Can you elaborate on your submission where you discussed a number of forms of collective bargaining? Can you explain the main differences between these models and whether in your opinion any particular form is more suited to New South Wales?

Mr GRANT: I think the one we have just talked about where you break the system of people who are producing fruit being beholden to winemakers. You integrate vertically and make the product yourself or you combine with others. There are more extended examples of that, which I refer to in the second paper of the submission. For example, a region in France holds back some of their produce and brands it together and says it is what we would call Riverina wine or New England wine or Stanthorpe wine. Because of their pooled capital they can age wines and increase their value. Basically the idea is to vertically integrate instead of just selling your grapes. You do other things to add value. The Winemakers Federation of Australia now talks very strongly about individuals doing that at a marketing level and a regional level, and that we move from just being a grape-producing country, as it were, to a wine tourism industry. That is very strongly embraced. That is the tension I was pointing to earlier: People have to do this on a regional level but they do not want to do it in terms of their

produce. One of the things we talk about in the second paper of the submission is to what extent it is viable for people in one industry to stick to a particular varietal—for example, a cool climate varietal like pinot gris or pinot noir—and say that this is their flagship. The point I am making is that that is still along the continuum of a cooperative. It is branding but those kinds of things have to be looked at and explored between producers to promote regions and wine tourism regionally, as opposed to saying, "I've got some grapes to sell. Who's going to buy them?" That is a very dangerous situation.

The Hon. SOPHIE COTSIS: Do you think there is scope for further partnerships to be built with tourism and other sectors?

Mr GRANT: Absolutely. In regions like the marginal areas you see local governments, as creatures of the State Government, acting with producers to promote their region for tourism and things like that. This is quite a positive experience because it is not just about an agricultural sector. When I moved to the country 25 years ago farmers were farmers and that was it. There was town and country. Now that is integrating. A local council can say it will sponsor a food and wine event. The people growing grapes are also beef producers and things like that, so it is changing the political economy and the sociology of these regions. That is really exciting, in particular for Government and local government. I do a lot of work on that. Those kinds of things—that type of integration—should be encouraged, because it is not just about grapes. It is about place branding and tourism. That is quite an exciting thing that is going on in these regions.

The Hon. RICK COLLESS: You would have heard the discussion earlier this morning about lifestylers versus mainstream producers and how they market differently. I asked a previous witness whether he thought the lifestylers were more inclined to accept lower prices simply to get rid of their grapes because they were not reliant on the grapes as their sole source of income. What is your view on that, particularly in the northern regions?

Mr GRANT: I do not think they are because their income is not fixed around grapes. If you can sell a fine bull as opposed to having to weed a vineyard what are you going to do? It is the people in the Riverina who have sunk massive capital costs into vines that have a production lifespan of 50 or 60 years who are really locked into that economic activity as opposed to doing other things. The so-called lifestylers will do other things because they have other options. Agricultural economists will say that their land is more valuable and that is precisely because they can do other things with it. They are not going to waste their time growing chardonnay for \$150 a tonne; they will do something else, whereas in the Riverina they cannot really do anything else. One of the things the last vine-pull scheme showed was that the various departments of agriculture in South Australia, New South Wales and Victoria said about some of the regions, particularly with respect to water, that there was not much else they could do. If you introduce a structural adjustment program you should be aware that those people cannot go into something else straightaway. Grapes do not need a lot of water, they are weeds and they will grow quite readily in these regions. There is not very much else that the farmers can do and international prices will recover. That is what the departments of agriculture said in 1985-87 about that particular dilemma.

CHAIR: Thank you very much for your contribution. Is there anything you want to add?

Mr GRANT: No, that is all.

CHAIR: If we have any further questions for you we would appreciate your answers within 21 days of receiving them.

Mr GRANT: That is no problem.

(The witness withdrew)

(The Committee adjourned at 1.27 p.m.)