

**Mark Creasy, the eccentric West Australian billionaire** who honed his prospecting sharps chasing bits of the fallen Skylab in the '70s, is an Australian mining legend in the mould of Lang Hancock or Charles Rasp. The 68-year-old still owns more mining tenements than BHP Billiton and Rio Tinto combined. That doesn't include tenements of the numerous mining companies in which Creasy has shares, nor his interests in another skyrocket – this one still aloft – Sirius Resources.

Les Stewart is as hard-bitten as Creasy. He even drives a similar 13-year-old vehicle. For nearly 60 years, Stewart ran a dairy property in the Otways. He reckons before deregulation and the supermarkets wrecked things, you could live a good life with 100 head. He's retired now, likes gardening; his land has been parcelled up and sold off but he kept a couple of hectares. Stewart is content and living a happy retirement, but he's no Creasy.

Creasy is worth nearly a billion dollars and the Sirius project is a big chunk of that. But his wealth is not from the resources that he unearthed being transformed from discovery to production. That's not how mining riches come about. His wealth began with the Bronzewing and Jundee gold deposits, and blossomed when he sold them on to Joe Gutnick, who built his own fortune amalgamating early stage projects and onselling to global giants like Newmont.

That's how mining works: as projects develop beyond the capacity of their founders to fund, they are taken over or merged with larger companies, and opened up to investors with the capital to get them to market efficiently. In the decade to 2012, during the latest boom, nearly \$300 billion was invested in iron ore, natural gas and other major projects, jacking up investment spending from around 2 per cent to more than 8 per cent of Australia's economic output. It's not just small to large: BHP Billiton took over WMC, the former Western Mining Corp, to gain access to the giant Olympic Dam resource in South Australia. (That expansion is on hold, as even a giant like BHP couldn't make the numbers stack up when commodity prices fell.)

Creasy and Stewart are archetypes of Australian legends, miners and farmers. But their approach to the riches of ground could not be more different. Australian mining is world class, Australian agriculture is not. Mining is dominated by global giants funded by global capital, farming by small scale operations that inevitably risk catastrophe when seasons or markets fail.

Yet agriculture has the potential to be the next boom for Australia. ANZ Bank, in a joint report with Port Jackson Partners called *Greener Pastures: The Global Soft Commodity Opportunity for Australia and New Zealand*, outlined a

scenario where agriculture should be the next sector to cash in on Asia-led growth. It estimated an additional \$710 billion in Australian agri-exports to 2050. New Zealand, too, could more than double agricultural exports.

Globally, agriculture and soft commodities are enjoying a boom. One index of 40 global agribusiness companies in the Boston Consulting Group's *Value Creators* sample generated a total shareholder return of 13 per cent annually from 2007 through 2011, higher than every other industry group surveyed and dwarfing the S&P Global 1200 Index, which delivered just 1.4 per cent annually (the long-term historical average for equities is approximately 9 per cent).

"Indeed, agribusiness performed far better in the same period than any of the 21 other industries surveyed in the annual *Value Creators* report," BCG found. The industry group continued its strong TSR performance in 2012 ... increasing by an average of 15.1 per cent in that 12-month period.

The soft commodities boom is no secret. It is linked to the growing wealth and development – and collateral demand for protein and calories – in the developing world and long-term threats to supply. BHP's diversification into potash, although under review, is a play on a key agricultural commodity as the miner surveys a world where the resource intensity of iron ore



or coal will fall as industrialisation matures but demand for food and energy increases.

Former BHP chief executive Chip Goodyear remarked early in this century's first resources boom how, on a visit to southern China, he noticed not only large numbers of apartments being built with steel made from the company's iron ore, but also the apartments' built-in air conditioners. So even when the building rush had wound down, those air conditioners would still demand energy. He might have added those enjoying the air con would be sitting down to bigger and better meals. *Greener Pastures* forecasts rising incomes and changing diets in developing countries mean the world will demand 77 per cent more agricultural output by 2050 compared with 2007.

But opportunity does not guarantee returns and Australia's agricultural sector is losing productivity and competitive advantage. Many initiatives are needed, say ANZ and Port Jackson Partners. At the upper end of possibility, Australia and New Zealand could gain \$1.7 trillion and NZ\$1.3 trillion respectively "with favourable conditions and targeted actions", their report says. But that would require "\$1 trillion and NZ\$340 billion in additional capital needed to drive production growth and support farm turnover in Australia and New Zealand. Agricultural industries in Australia have

lost momentum while New Zealand is heavily reliant on its dominant dairy industry."

The report's author, Angus Taylor, says: "We have to strengthen our competitive position. It has clearly eroded in recent years, and there's a whole series of areas we will need to address if we're to fix that. That means things like getting enough skilled people into agriculture or raising the skills of those in it; it means getting access to capital to grow the industry and to turn over the assets in the industry as our older farmers move out; it means getting access to the R&D and the knowledge out in the field to drive improvements; it means getting our supply chains right. All of these things have to happen if we're to capture the opportunity."

This is a view shared by the Australian Bureau of Agricultural and Resource Economics and Sciences (ABARES), the government's agricultural forecaster. "Australia is now effectively a high-cost supplier of products," says executive director Paul Morris. Australian farmers cannot compete on price with low-cost producers in countries such as Brazil and India, the world's leading exporters of beef. "If agriculture continues to do what it does now, we're probably not going to be able to take advantage of the opportunities for the future," Morris warns. "We need to go through some transformational changes."



**2.4 times**

How much more it costs to slaughter and process a cow in Australia versus the US

**77%**

Forecast growth in agricultural production from 2007 to 2050

**20%-30%**

Rise in average real prices for many agricultural commodities over the next decade



**\$35.6 billion**

Forecast earnings from farm exports in 2013/14

**\$600 billion**

Additional capital needed to generate growth and profitability in agriculture in next four decades

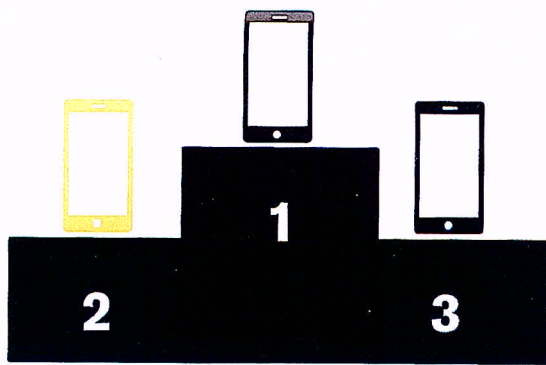
**"Australia's proximity to Asian markets means little in overall competitiveness terms, and any complacency the industry has about Australia having a head start in these markets is not justified."**

Mick Keogh, executive director,  
Australian Farm Institute

Les Stewart's old place rolls through picturesque valleys between massive rainforest national parks. The grass in his pastures is lush, some of it still used to raise a few steers. The machinery in the area ranges from spanking new to dilapidated. It's easy to see the difference between a highly productive farm and one just eking out an existence. For one thing, the better farmers drive around in late model Range Rovers and Audi Allroads. This is part of the challenge. Farming in Australia, like mining, has a romantic history, a narrative of wealth built by farmers working the land. It is a passionate history and every time a bank forecloses on an unviable wheat or sheep farm, it's pretty obvious where public sentiment lies.

The Productivity Commission found that 20 per cent of the most efficient broadacre farms accounted for nearly two-thirds of total production in 2005. The remaining 80 per cent produced only 36 per cent of output. This is where those small farms, often third or fourth generation owned, with rundown machinery exist, parched of capital. They have been saved by various governments and assistance packages, for drought relief, input subsidies, all kinds of industry protection, which in the long run doesn't protect the sector or benefit taxpayers.





Australia ranks second in the world in terms of smartphone penetration. Apps will drive new shopping habits.

Mark Bennett, ANZ's agribusiness head, says even allowing for drought and the high dollar, there is a growing disparity between the leading group of farmers and those that are not doing as well.

"Part of that stems back to the R&D and [debt] extension that has been provided to farmers in the past," he says. "Farmers often lament that this isn't as available to us as it used to be, so I think there's a really big challenge in looking at the middle group of farming to say: it's got to make some big decisions. Does it have the tools? Is it well equipped? Are they running businesses well enough to make good, informed decisions about where they want to take their businesses in order to capture the opportunity that is available to them?"

There is indeed a romantic notion of traditional farming, one which doesn't extend to small-scale mining. The bucolic idyll is deeply embedded – and it's the same one behind the agricultural protectionism of Europe and Japan, which distorts global markets in the interests of supposedly protecting traditional ways of life. But such romantic notions come with their own costs: the Productivity Commission says most of the sediments, nitrogen and phosphorous that wash into the Great Barrier Reef lagoon come from cattle grazing, and a big part of the problem is overstocking by graziers whose activities are fundamentally unviable.

Australia is inherently a high-cost labour market, setting aside for one moment the politics around labour relations. We are a developed economy, we have high health and safety standards, high levels of quality control. In labour-intensive agricultural processing activities such as making potato chips, Australian costs are around \$50 an hour compared with about \$20 in New Zealand and less than \$5 in China. The cost of slaughtering is also high in Australia, in part because it is not a job workers here want to do. Ironically, the crackdown on 457 visas works against bringing in workers who will do those jobs, while the mining boom has drawn away the welders and engineers vital in the abattoir business. It costs nearly two and a half times as much to slaughter in Australia compared with the US, two-and-a-half times the cost in Brazil and one-and-a-half times New Zealand.

The highly regarded agribusiness analyst David McKinna, of McKinna et al, says the lack of competitiveness starts with the high Australian dollar and terms of trade but includes high labour costs and regulation, a lack of scale, higher input costs, higher OH&S costs, higher plant and equipment costs, lack of transport infrastructure, poor productivity, low adoption of technology, and foreign tariffs on Australian exports.

Investment in iron ore, natural gas, other major mining projects in decade to 2012

**\$186 billion**

Forecast for total export earnings for energy and mineral commodities in 2012/13

Meanwhile, proximity in the Asian century can be overrated. Australian Farm Institute executive director Mick Keogh analysed shipping costs in the wake of the annual ABARES agricultural outlook conference. "The advantage enjoyed by the beef shipped from Melbourne to Shanghai is only between about 12¢ and 22¢ per kilogram," he argues. "For beef product with a landed price of perhaps \$5 per kilogram, this represents a landed price advantage of between 3 and 5 per cent. This is a pretty small margin."

"The conclusion from this simple and rough comparison is that Australia's proximity to Asian markets means little in overall competitiveness terms, and any complacency the industry has about Australia having a head start in these markets is not justified."

Where Australia does have an advantage, says McKinna, is in quality derived from our developed status. "Consumers trust Australian foods," he says. "That's a big advantage. The Chinese consumer will pay a premium for foreign foods. That's why Warren Buffett bought into Heinz. Asian luxury hotels and casinos will pay a premium for Australian beef."

McKinna et al's latest well-watched Agrifoods Megatrends survey lists 10 trends: the cost and risk aspects of climate change and the impact of the carbon tax; the cost and scarcity of water; the declining competitiveness of the Australian agri-food sector; the shift in value along the supply chain; corporatised farming and foreign ownership; market access and biosecurity; social values and accountability (largely driven by social media); growing global demand for food; threats to the agricultural supply base; and technology.

"The next boom story is very complex," McKinna says. "Lots of these elements interact in different ways and in some, Australia has advantages but in others, it is a long way behind." Access to markets is a key issue. It is not good enough to have a world-class product if markets are closed – something Australian producers have long experienced in Japan but which is also an issue in China and India.

"What we do see are Chinese firms, many of which are ultimately government-owned, are investing in Australia to ensure supply of product up the supply chain. What we in Australia should be doing is the reverse of that, establishing relationships with Chinese firms that have the government connections to ensure market access – they might be supermarkets or food service companies or processors."

**"If agriculture continues to do what it does now, we're probably not going to be able to take advantage of the opportunities for the future. We need to go through some transformational changes."**

Paul Morris, executive director, Australian Bureau of Agricultural and Resource Economics and Sciences

GRAPHIC SOURCE: ABARES RESOURCES AND ENERGY QUARTERLY, ANZ'S GREENER PASTURES; THE AUSTRALIAN SUGAR COMMODITY OFFICE





### **Generations of Mildura youth, including me, made their**

summer holiday spending money picking Thompson Seedless sultanas, which ended up in the ubiquitous packets of Sunbeam "sulties". The irrigated vines were a giant green moat around Mildura and other towns along the Murray. The "blockies" who farmed fruit blocks were the lifeblood of the local economy. Established in 1926, Sunbeam is now a Shanghai company. It was acquired by the Manassen group, which holds around 70 Australian food brands including Sunbeam, Angas Park, Margaret River Dairy Company, Ryvita and McVities biscuits. Manassen, in turn, was taken over by Bright Food Group, a Chinese company backed by the Shanghai government. As in mining, such investment by foreign capital is crucial to grow the industry. But it's even more controversial when foreign companies buy farms.

Corporate farming is one thing, foreign corporate farming has old-time farmers like Stewart seething. "We don't bloody need them," he fumes. But if Australian agriculture is to boom, we do. ANZ's Mark Bennett argues: "With relatively few large corporations in the agricultural sector and a fragmented structure dominated by either smaller companies or family-run businesses, that discussion is naturally more challenging than in sectors led by larger, international corporations such as mining and energy." As BCG found in its analysis of agribusiness profitability: "The companies that successfully anticipated a trend, undertook a step change in their cost structure, or risked a sector-altering acquisition and made it work, have reaped the greatest benefits."

The characteristics of the Australian market that contribute to its high-cost structure mean the most attractive profit pools are in less labour-intensive, less commodified areas. While broadacre farming and grains have some advantages, there are even more if production is directed towards higher margin, niche opportunities such as gourmet pasta flours, for example. Such niches are less vulnerable to market shifts and a strong currency. The Australian wine industry in China already focuses more on the \$100-plus a bottle end than the bulk end.

But Australia's domestic market structure is also an issue. Unlike in other mature markets, where the retail sector is divided relatively evenly across the price spectrum, the Australian market is dominated by the Coles and Woolworths duopoly, both of which concentrate on a low-price strategy. That drives a relentless push on cost, to the benefit of the supermarket's margin but not that of its suppliers. The economics of the shift by the supermarkets towards home brands has been argued out in recent months, most passionately with the milk industry. Such is the bargaining power of supermarkets that any producer with revenue in the tens of millions of dollars is dependent on the relationship. "That allows the supermarket to push more costs back on to the producer, like freight, and that means the producer cuts back on things like research and development and product innovation," says McKinna.

One doesn't want to emulate the American baseball legend Yogi Berra, who famously said of a restaurant, "no one goes there any more, it's too crowded". Most people shop in supermarkets. But their fixation with cost means anything frozen or with a shelf life must compete with offshore suppliers. Local premium goods don't fit the model.

Coles' ultimate boss, Wesfarmers chief executive Richard Goyder, is unapologetic: "Any business in this country has to be looking at how efficient it is. Our business is not to prop up inefficient suppliers but supply great products to our customers in the best way we can." When value equates with cheapness, however, the market for premium product, which by definition may be seasonal, inconsistent, low volume, highly labour intensive, becomes smaller. Value in the supermarket world equals cheap, but a tomato that doesn't taste like tomato is not good value, no matter the price.

In Europe and the US, the supermarket category includes retailers such as Eataly or Whole Foods, which favour premium products rather than everyday low prices. Their existence, in turn, supports niche but premium producers. In Australia, the share of such competitors to Coles and Woolworths, like Leo's or Harris Farms, or farmers' markets, is a tiny proportion of the market. Some producers, such as the award-winning Bruny Island Cheese Company, have developed a model to bypass supermarkets. Another artisan cheese company, Meredith Dairy, has been so successful it has garnered bargaining power over the supermarkets.

Bruny Island owner Nick Haddow says his industry is at a "fork in the road". Four years ago, he shifted from being a small producer competing in big markets to one working with very high-grade products. Haddow buys from two small local commercial dairies and pays up to 40 per cent more for milk. If his suppliers were forced instead to sell milk to processors for major supermarkets, the size of their operations means they would fail on scale.

"The point I want to make about dairy is that we have an opportunity to help these small producers, who would no longer be viable, to value-add," he says. "It has regional economic development benefits, employing local people, encouraging tourism."

Like Les Stewart, Haddow is a small, passionate dairy man, albeit a cheesemaker. But unlike Stewart, he recognises the global forces at play can't be resisted; the challenge is to find a profitable niche. Australian agribusiness is in a position not dissimilar to its farmers. The global market is indifferent to where it sources its products. Non-differentiated commodities will come from the lowest cost provider. That's not Australia. But Australia can provide high value, high margin, premium products. If it can restructure.

Packaging magnate Anthony Pratt recently called for Australia's food exports to be ramped up to feed 200 million people rather than 50 million, and to use tax incentives and regulation reforms to unlock more of the nation's agricultural and food processing potential. It's an admirable rallying call, but with two major caveats: Australian soils and rainfall patterns just can't support hundreds of millions more hungry mouths. According to Professor Snow Barlow, convener of the National Climate Change Adaptation Research Facility at the University of Melbourne, we can produce food for around 60 million to 80 million people at best.

The other caveat is that aiming for volume is not in Australia's interest. We are high-cost, premium producers in a world where volume gravitates towards an everyday-low-prices strategy. In the global agri-market, we need to be like Bruny Island cheese. ■