INQUIRY INTO THE IMPACT OF THE GLOBAL FINANCIAL CRISIS ON REGIONAL AUSTRALIA

NFF SUBMISSION

March 2009

The Committee is to inquire into the impact of the current global financial crisis on regional Australia and the role of the Commonwealth Government in ensuring that regional Australia is equipped to respond, with particular focus on:

- the encouragement of economic development and employment; and
- the development of sustainable essential services and social infrastructure designed to enhance the liveability of regional Australia.

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The National Farmers' Federation

The National Farmers' Federation (NFF) was established in 1979 and is the peak national body representing farmers, and more broadly agriculture across Australia.

The NFF's membership comprises of all Australia's major agricultural commodities. Operating under a federated structure, individual farmers join their respective state farm organisation and/or national commodity council. These organisations collectively form the NFF.

Each of these state farm organisations and commodity council's deal with state-based 'grass roots' issues or commodity specific issues, respectively, while the NFF represents the agreed imperatives of all at the national and international level.

Introduction

The NFF welcomes the opportunity to provide comments to the House Standing Committee on Infrastructure, Transport, Regional Development and Local Government inquiry into the impact of the global financial crisis on regional Australia.

While agriculture represents approximately 3% of Australia's Gross Domestic Product (GDP), it is estimated that the sector represents more than 40% of the GDP of regional economies. Once multiplier effects are taken into account, this is as high as 70-80% in most small towns. While not all small towns are 'farming towns', a majority of them still are and the fortunes of these towns are aligned with the productivity and sustainability of the farms surrounding them. This dependence on one industry makes the impacts of the Global Financial Crisis (GFC) on the agricultural sector a significant influence on the outcomes for regional Australia.

In this regard the NFF acknowledges that the GFC is bringing a number of both short and long term challenges for the sector that in turn will impact on regional communities. The GFC makes it all the more important to carefully consider the impacts of major policy initiatives such as the CPRS and the water buybacks on regional communities. The resilience of regional Australia, particularly in the Murray Darling Basin is at an all time low. This leaves little margin for error when implementing policy that is likely to result in significant structural change. Further challenges have been outlined within this submission.

However it must be noted that the underlying fundamentals for Australian agriculture remain strong and are underpinned by an Australian banking sector that is in a relatively strong global position. The NFF also notes that while the International Monetary Fund (IMF) has forecast a significant reduction in economic growth within the USA and EU, the Asian region (35% of Agricultural exports excluding Japanese trade) is anticipated to fair much better.

The March 2009 national account figures were a timely reminder of how fundamental Australia's farm sector is to our economy, with agricultural production and growth – in seasonally adjusted terms up 10.9% in the December 2008 quarter on top of the previous quarter's 13.4% – helping to stave off recession. In addition, between November 2007 and November 2008, an extra 17,255 Australians have found work in the farm sector.[1]

As NFF president David Crombie stated:

"Mining booms come and go, but Australian agriculture is the constant that gives the Australian economy the surety it needs during good and turbulent times. That's not a slight against other sectors, just recognition that regardless of the fluctuating fortunes of various industries that, at the end of any day, people still have to eat."

These factors give the agricultural sector some confidence in seeing regional Australia, and indeed the broader economy, through the impacts of the GFC - with the assistance of strong support from the Australian Government.

Short term impacts of the GFC on agriculture

Increased price volatility

The GFC has led to an immediate and significant easing in soft commodity prices. ABARE has stated that slowing world economic growth in 2008 and 2009 is a key contributor to a softening in commodity prices since mid-July 2008. Combined with already low inventories, the pressure from high oil prices and further increases in biofuel production, continued price volatility is expected in the short to medium term.

As seen in mid-2008, a wave of non-commercial speculators began selling their positions in all commodity markets. This came after investors had previously been placing billions of dollars at the soft commodity markets in response to the well publicised Global Food Crisis. This massive influx of funds played a role in pushing up food prices until the middle of 2008. [2]

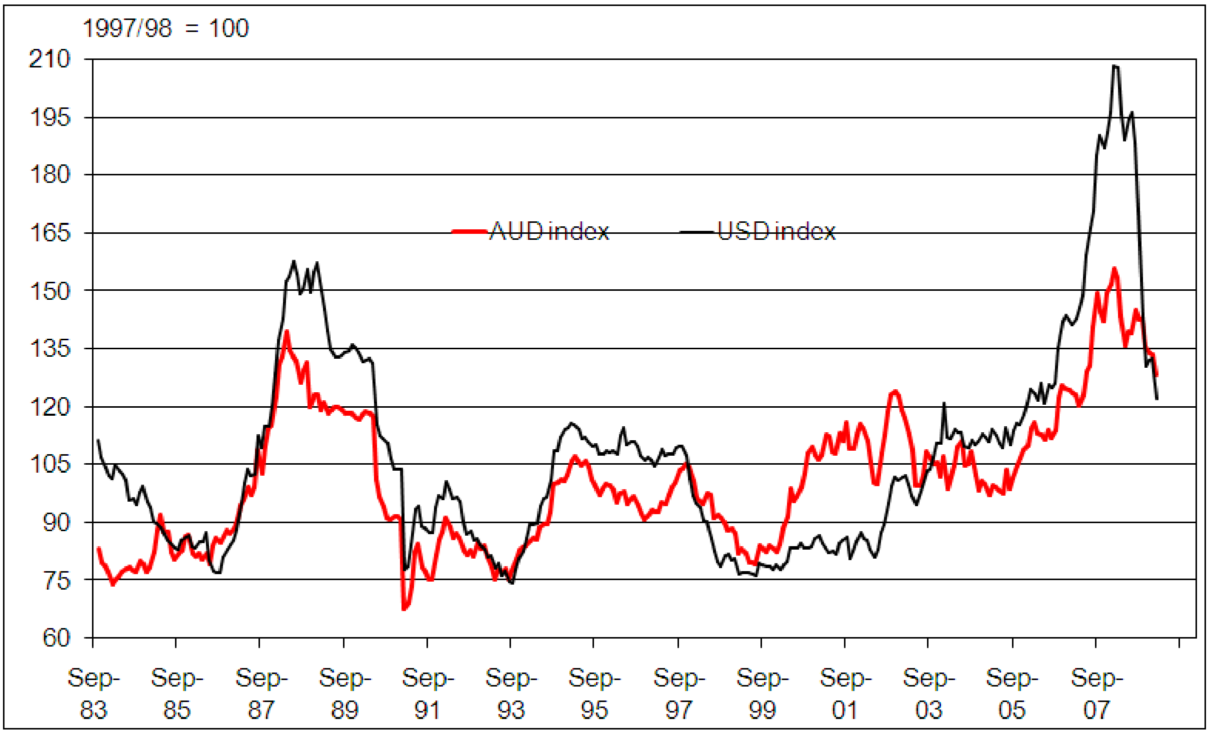
However, as the global credit crisis has become more critical, the number of speculative positions has fallen. For example, from 30 September to 7 October, the US Commodity Futures Trading Commission (CFTC) registered a 73% fall in speculator positions for sugar, free-falling from 43,005 (long positions - a

[1] ABS, Nov 2008, 6291.0.55.003 - Labour Force, Australia, Detailed, Quarterly,

[2] Partos. L, Oct 2008. *Confectioners may benefit as speculators exit commodity markets*. Sourced from www.nutraingredients.com

commitment to buy) to 11,413 (long positions). Long positions for corn also dropped, from 98,244 to 73,297.[3]

Similar trends has emerged in many of the commonly trade commodities, as reflected by the *Westpac/NFF Commodity Index* that monitors the weighted average global price of major agricultural commodities. The chart of the *Westpac/NFF Commodity Index* can be seen below, clearly showing a significant decline in prices since the middle of 2008, despite remaining high on historical terms.



Reduced credit access for farmers

On the most part, it must be acknowledged that the banking sector has been supportive to the agricultural sector, particularly over the past 6-7 years when drought has ravaged large stretches of farming land.

Since the GFC took a hold in mid 2008, this support in the form of access to credit has largely continued although the NFF has received information from members that credit access has tightened. There have been cases where the GFC has had a noticeable impact on banks treatment of loan security requirements, with a clear increased sensitivity by the banks to their financial exposure. Some loans that would be offered prior to the GFC are no longer readily available.

This issue has been heightened for those farmers with finance provided by non-bank lenders, which have been ineligible for the Government deposit underwriting

[3] Partos. L, Oct 2008. *Confectioners may benefit as speculators exit commodity markets*. Sourced from www.nutraingredients.com

guarantee. These non-banks have seen significant amounts of liquidity leave their institutions as customers seek the security provided by Government backed, banking institution deposits. The result has been a lower capacity by the non-bank lenders to offer credit to customers, including farmers. This issue has been exacerbated in Tasmania, where the non-bank lenders have, until recently, held a greater share of the farming customer base.

Reduced credit access for domestic/global customers

Credit access for Australian farmers' major international buyers has been restricted as a result of the GFC, seeing difficulties emerging in buyers accessing Letters of Credit (a letter of credit is a formal document guaranteeing payment by an issuing bank on behalf of a buyer [an importer] to a third party [the producer of the goods being produced] for a specific amount of money, provided certain conditions are met), and in some cases, even reneging on existing contracts.

For an industry such as agriculture that relies on overseas markets to consume approximately two thirds of its total output, such uncertainty in the international trading environment is generating major problems and lowering returns.

Depreciating exchange rate

According to ABARE, the recent depreciation of the Australian dollar both against the US dollar and on a trade-weighted basis, if sustained, is expected to provide support for commodity export earnings because most export contracts are denominated in US dollars.

The Australian dollar is now trading around US65c to US70c, compared with a high of around US98c in mid-July 2008. Concerns about the adverse impact of recent financial market turmoil on world economic growth, and hence commodity demand and prices, have been a key factor contributing to the depreciation of the Australian dollar. While a lower Australian dollar will provide support for export earnings, it can also place upward pressure on the cost of farm inputs such as fertiliser and fuel, many of which are imported.[4]

Reduced official interest rates

In response to the GFC, the Reserve Bank of Australia has reduced the official cash interest rate by a full 4% since September 2008 (from 7.25% down to the current 3.25%). While providing welcome relief, Australian farm businesses have been frustrated that the banking sector has failed to pass on these rate cuts, particularly on small business loans such as those offered to many Australian farmers. The Table below compiled by the RBA shows the per cent changes in small business

[4] ABARE

residentially secured lending rates by the four major banks in response to changes in the RBA cash rate target up to the end of 2008.

	Sept 08	Oct 08	Nov 08	Dec 08	Total since Sep 08
RBA Cash rate	**–0.25**	**–1.00**	**–0.75**	**–1.00**	**–3.00**
ANZ	No change	–0.60	–0.40	–0.40	–1.40
CBA	–0.25	–0.65	No change	–1.00	–1.90
Westpac	No change	–0.80	No change*	–0.80	–1.60
NAB	–0.25	–0.20	–0.40	–1.00	–1.85

*Note: Westpac announced a 0.8 per cent reduction in business credit card rates in November 2008.
Source: RBA Bulletin, ANZ, CBA, Westpac, NAB

Longer term impacts of the GFC on agriculture

Increased protectionism

In response to the GFC a number of OECD economies have announced a series of measures to support key institutions, stabilise markets and bolster confidence. Yet under the guise of economic stimulus packages, increased levels of protectionism are emerging. Indeed, the void between hollow rhetoric and genuine leadership has rarely been as stark as that seen in recent months. World leaders spruik the virtues of trade reform while shielding their economies from international trade.

For example, global dairy prices plummeted 10.4% in January 2009 on the back of European Union's (EU's) export subsidies while the United States (US) also buckled to protectionist pressure within their own stimulus package. In fact, 17 of the G20 countries have implemented some form of protectionist measure since meeting in Washington in November, where they promised not to impose any new trade-restricting measures for 12 months.[5]

The US was also guilty of moving down this route with its 'buy American' dictate as part of the most recent US stimulus package. The US wants to be able to export their goods to others but don't want to import goods from others.

The NFF has noted that the problem with the 'buy America' kind of 'protection', is while it may shore-up domestic jobs in the short-term, it only reinforces the inherent distortions that have plagued international trade and restricted commodity prices for too long. Rather than help the US economy to rebound, it merely compounds and entrenches the inefficient allocation of resources that the global economy can ill-afford – now or over the longer term.

[5] Palmer D. World Bank urges tougher G20 stand on protectionism, http://uk.biz.yahoo.com

Indeed, recent commentary suggests there may yet be another compounding source of the potential tariff war. Recently, the head of the Federal Government's climate change review, Professor Ross Garnaut, highlighted the possible world tariff war driven by Europe and the US over greenhouse gas emissions if no global agreement to prevent climate change is met.[6] This, Professor Garnaut claims, would emerge as countries consider adding additional import duties on products from countries that aren't doing enough on climate change. Such comments have already been heard from the Energy Secretary in the United States. In light of the current uncertainty surrounding the Government's planned 2010 CPRS implementation, these comments may have potential huge ramifications for exporting sectors such as agriculture.

Changed demand profiles for soft commodities

While food is an essential item that is generally less sensitive to income, there is significant variance in the price points available to consumers in this category. With consumers less confident about their income security, they are now showing signs of moving away from the premium end of the market and towards cheaper staples.

In the beef sector for example, reduced demand for prime cuts of beef and a move towards more economical options such as mince and sausages, or even poultry and pork, has contributed to a 9.4% fall in the world price of beef during February 2009. Similar patterns are emerging in the dairy sector, where consumer demand for the high end cheeses is dissipating, with lower dairy prices resulting.

Impact on land values

Rural debt has escalated by over 85% since 2002-03 due to drought conditions, placing the agriculture sector at considerable exposure to increasing credit cost. For this reason, the NFF is cognoscente of the potential for regional land prices to fall, should the banking sector withdraw its support of the agricultural sector and aggressively foreclose on rural debt.

While it should be noted that regional land values have been relatively steady since the GFC, the potential for a 'domino effect' on regional land prices should be avoided at all costs.

The role of Government

Correct inequities with bank deposit guarantee

On 12 October 2008, the Government announced it would guarantee deposits in Australian owned banks, locally incorporated subsidiaries of foreign banks, credit unions and building societies for a period of three years. The Government also

[6] Wilkinson, M. 2009 *Climate deal failure could cause tariff war: Garnaut.* FarmOnline accessed on 30/03/09

announced a guarantee on wholesale debt securities issued by these same institutions, on application, and for a fee.[7] As discussed within this submission, this decision has resulted in a significant outflow of funds from the non-bank financial institutions, severely restricting their capacity to extend credit to new or existing customers.

While the NFF believes that the non-bank sector has made a valuable contribution to the financial markets in adding a healthy level of competition within the sector. The NFF therefore asks that Government examine potential solutions that may help to correct the current imbalance.

Increased transparency on banks passing on interest rate cuts

Unfortunately it is extremely difficult for consumers of credit to keep financial institutions to account for their decisions regarding interest rates. It is all too difficult, particularly for farm businesses, to monitor how much of the official cash rate cut is being passed on by their own financial institution, or indeed to monitor the actions by competing financial institutions.

The NFF believes that, in the interests of enhancing competition within the banking sector, that a mechanism should be created whereby rate change decisions by financial institutions are lodged and publically reported. Transparency in this area (particularly for small business loan rates) is sadly lacking, and therefore detracting from the urgency for financial institutions to pass on rate cuts. In turn, this is subduing the intended market response to monetary policy changes through the RBA.

Economic infrastructure investment

Rarely before has the importance of having efficient infrastructure in regional Australia, particularly in water and transport, been as clearly identified across the broader Australian community. Metropolitan based Australians are now attuned to the fact that regional infrastructure in these key areas has a significant impact on their own access to water as well as the availability and prices of the food they eat. Infrastructure in regional Australia is a key element to enabling agriculture to extend its contribution to the Australian economy and in doing so, help the broader economy emerge from the GFC.

In addition, investment in infrastructure has the additional benefit of having both immediate employment and economic stimulus affects for local areas via the construction activity. More long-term, the benefits of infrastructure development include an increase in regional Australia's supply chain efficiency and capacity to move commodities to markets located both at home and abroad. Moreover, the

[7] Press Release (The Hon Wayne Swan MP), 24 October 2008, Government Announces Details of Deposit and Wholesale Funding Guarantees

majority of short and long term benefits accrued through infrastructure spending are captured by Australian businesses. This increases their ability to employ Australians.

As reported by the Department of Transport and Regional Services, the costs for regional businesses are considerably higher than in metropolitan areas. Over the five years to 2000, the expenditure for every dollar of profit increased for the average regional business by almost 8%, while in the cities, it decreased by 11% in the same period.[8] Therefore, regional businesses are already facing cost pressures not felt by their urban counterparts.

The NFF argues the existing cost challenges of doing business in regional and rural Australia must be acknowledged. We believe that reliable provisions of transport, telecommunications, energy services and water access are all community service obligations (CSO), or basic essential service that government is expected to deliver. Neglecting to do so could be an additional disincentive to doing business in rural and regional areas, placing additional stresses on our already overcrowded capital cities. Importantly in the current environment, a failure to invest in regional infrastructure would be restricting a sector in a growth phase (which in itself is rare at the current time) from maximising its potential. It is vital the Government clearly acknowledge these factors in determining its infrastructure spend agenda.

Bearing this in mind, the NFF has asked that the Australian Government ensure that its nation-building pledge under the 2008 Federal Budget, via the Building Australia Fund, be honoured in full. Specifically, the NFF understands that only $12.6 billion has so far been allocated to the $20 billion Fund.

In addition, within the NFF's submission to Infrastructure Australia, we have called for investment in water infrastructure as a means of building agricultural productivity within the irrigation sector while leading to positive environmental outcomes. Development of utility scale renewable energy has also been identified as offering significant economic benefits to regional areas, particularly in relation to its potential as a complementary measure to assist regional communities to deal with the cost impacts of the Carbon Pollution Reduction Scheme (CPRS).

Telecommunications infrastructure

Information and communication technology (ICT) is vitally important to rural and regional Australia surviving the GFC, but also to set itself up for future opportunities and productivity improvements. ICT allows greater participation and equality in service delivery. But rural and regional Australia has been left behind on the technology front and this gap threatens to grow wider.

At present, many farmers are dealing with satellite broadband that delivers not much more than dial-up speeds. For copper wire broadband, ADSL2+ speeds are

[8] DOTARS, *Regional Business – A Plan for Action*, 2003,

almost nonexistent, and even the Telstra NextG network will have capacity limits on future speed upgrades due to pipeline bottlenecks. These constraints are impacting on rural business today and will only become more exacerbated into the future.

In comparison, our competitor nations are already well advanced and adoptive users of 100MBit internet, whilst this is only just starting to be rolled out in Australian capital cities. Australian metro consumers and Greenfield developments already have access to super fast broadband (100MBits), the speed and pace of technology being deployed into regional Australia is lagging behind not just metro Australia, but the world.

While government plans to deliver a National Broadband Network are welcome, the NFF is concerned that it may be arriving too late and already be superseded by the time it does arrive.

Modern farming is becoming increasingly reliant on ICT. From telemetry, GPS guided tractors, remote sensor irrigation devices, and marketing and risks management needs, ICT infrastructure provision in rural and regional Australia is more important than ever. Modern farming is also part of the international market place. Farmers need globally competitive broadband to offer their products (and in many cases their services) to an international market. Rural businesses, including farmers, therefore require high-speed ICT to remain competitive and responsive. ICT has become a core productivity driver for their businesses.

For this reason the NFF's 2009 Pre-Budget Submission called for the following:

- The NFF expects the pledged $400 million initial commitment recommended by the Regional Telecommunications Review (RTR) to be available under the 2009 Federal Budget. Further, as part of this response, that the Government clearly articulate how its proposed National Broadband Network (NBN) will 'revolutionise' the availability and quality of telecommunications services in rural Australia – both now and over time as technology and service need changes. The Government must address the uncertainty over how future upgrades will be funded, on a guaranteed basis, given its removal of the $2 billion Communications Fund.

Social infrastructure investment

Labour shortages are often a symptom of stifled regional development, requiring the remedy of an effective population strategy. Service delivery in regional and rural Australia is already well behind that of metropolitan Australia. The ability for rural and regional Australians to gain equitable and affordable access to a range of services has been well documented and researched. The NFF therefore contends that Government should commit resources to protecting the infrastructure, transport, health and education and training opportunities for regional Australian communities.

Pursue the trade reform agenda

As the Australian Minister for Trade, the Hon Simon Crean MP, stated at the recent ABARE Outlook conference:

"International trade being impacted by the economic downturn. Trade is not the cause of the downturn: but it is very much a vital part of the solution.... Each successful multilateral trade round has provided a boost to world trade growth. Trade – and our capacity to support it during this downturn – will play an integral role in our efforts to recover from the global financial crisis."

The NFF therefore encourages the Government to maintain a strong focus on driving the international trade reform agenda. Priority should clearly be given to the multilateral trade negotiations and the Doha Round where the potential grains are greatest. However, the Free Trade Agreements, particularly those in North Asia with China, Japan and the Republic of Korea, are also of enormous value to Australia's farming community.

Building labour flexibility

The long-term drought has had a debilitating impact on farm employment and has resulted in rural adjustment as job-seekers move into the mining industry or into metropolitan areas for work. As parts of regional Australia emerge from drought, government assistance to encourage these people back into rural and regional communities would be warranted. University of Sydney data shows a shortfall of approximately 96,000 people over the next six years in agriculture's top seven occupations: livestock farmers (will need another 34,000), farm hands (21,000), crop farmers (18,000),mixed crop/livestock farmers (14,000), general mobile plant operators (4,000), bookkeepers (3,000) and shearers (2,000). These labour shortages are expected to persist despite the Global Financial Crisis and provide good job opportunities for people who may be displaced from other industries by the downturn.

Mobility of the labour force must therefore be facilitated to ensure that these market forces are not inhibited. Measures that government should examine in this regard include the following:

- Farmers are increasingly being encumbered by legislative and regulatory complexity. The workplace relations legislation introduced by the previous Government, removed by this Government, and the new award modernisation process has created widespread confusion in some technical aspects on the ground. There is a clear role for Government to fund industry with a communication and education campaign on the new workplace arrangements so that employment opportunities are not squandered.

- Red tape surrounding many aspects of engaging apprentices, such as the Registered Training Organisations/Government/Employer paperwork, together with the bureaucratic language of Vocational Education and Training System have caused a gross lack of simplicity and consequently deterred farmers from considering this option.
- The Job Network needs greater incentives to place short-term, casual and seasonal work, which are presently commercially unattractive. The ten week waiting period that applies to those on benefits who opt to take a short-term seasonal job but cannot find further work and need to resume benefits, is a major disincentive for employees to do so and a waiver of this is proposed in certain circumstances.
- That farm apprentices to be specifically included on the National Skills Needs List and gain access to the full suite of incentives to allow farming to compete with other trades in the attraction of apprentices. Training packages should be presented with a farmer friendly language that is devoid of the acronyms symptomatic of Education and Training.

Regional tourism

Improving regional services and especially those related to leisure and tourism could provide significant assistance in lessening the GFC effect within Australia. With more constrained leisure budgets, Australians are likely to choose an Australian domestic holiday over an international destination. This has two-fold benefits to Australia. The first is the multiplier effect of domestic spending versus overseas spending and an improvement to our balance of payments as a nation. The second is the ability for tourism to generate jobs.

Promoting this through flexible holiday options, tourism promotions and so on results in more people visiting regional areas. Their broad economic investment into local economies is important and noticeable in the busier tourism destination townships and areas. Equally important is their contribution social and recreational life in towns. Locals are arguably less likely to leave a region if it has a living, breathing social life, particularly one with a strong appeal to youth.

The NFF believes Government can assist at the macro level by encouraging Australians to holiday domestically and at the micro level by grants to rural and regional towns to build or promote their tourism appeal.

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