
VICGRAIN LIMITED



**Submission to Productivity Commission's Inquiry into
Progress in Rail Reform**

**VICGRAIN
LIMITED**

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Progress in Rail Reform

1. Vicgrain Limited

1.1 Background and Operational Details

1.1.1 Overview

Vicgrain is Victoria's premier bulk handling service provider, specialising in storing, handling and shipping cereals, coarse grains, pulses, oilseeds, rice and woodchips.

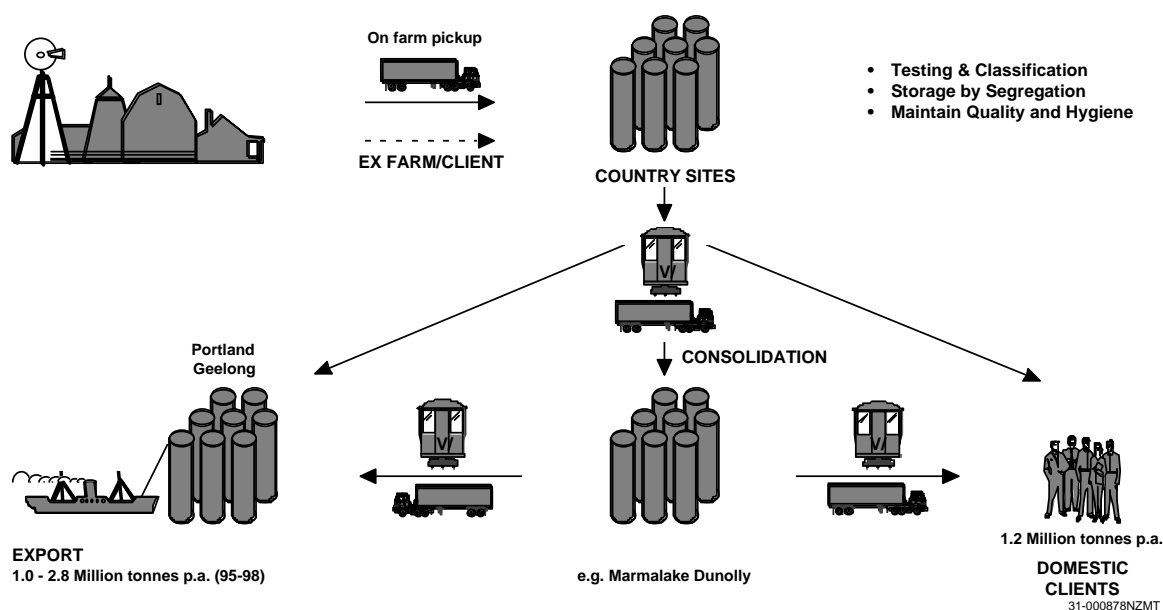
Vicgrain operates 236 storage and handling sites throughout Victoria and southern New South Wales, export facilities at Geelong and Portland, and an inland terminal at Sunshine in Melbourne services the requirements of the metropolitan grain consumers. Of the 236 sites, 190 are directly connected to V/Line's rail network where the majority of the off-rail sites utilise V/Line's trucking services to link with the rail network.

Vicgrain employs over 300 permanent staff and 1,000 casuals and contract staff during harvest. In the 1996/97 year handled over 4.5 million tonnes of commodities, with 2.9 million handled in the 1997/98 year due to the low harvest.

Since the sale of the GEB in 1995 which created Vicgrain, the expenditure on capital improvements is equal to the purchase price of the initial investment.

1.1.2 Vicgrain's role in the supply chain

Vicgrain receive the grain from farms and bulk commodity suppliers and with the V/Line Freight Corporation (VLFC) organise its movement out to export and domestic markets.



Vicgrain facilitate the entire logistics process in the Victorian grains industry. In relation to the rail network this ranges from organising the quantity and timing of wagons, to loading and unloading wagons.

1.2 Ownership of Vicgrain Limited

Vicgrain Limited is 70% owned by Victorian Grain Services Limited (VGS), 20% owned by GrainCorp Limited through its wholly owned subsidiary GrainCorp Victoria Pty Ltd, and 10% owned by the Australian Barley Board.

VGS is an unlisted public company which presently owns 70% of the shares in Vicgrain Limited. The issued capital of VGS currently consists of shares held by over 4,000 growers, the Victorian Farmers Federation and Vicgrain staff and Directors.

2. Vicgrain as Stakeholders in the Sale of VLFC

2.1 Our Objective

In broad terms, our objective is to achieve the lowest cost grain path for the Victorian grain industry by integrating the handling, transport and trading components of the supply chain, while achieving an acceptable rate of return for our shareholders. Vicgrain Limited (Vicgrain) intend to achieve this objective by protecting and increasing the utilisation of the storage, handling and wagon fleet assets and by fully exploiting the inherent synergy benefits available.

Under the existing relationship between rail transport, statutory marketers and Vicgrain (refer to section 2.4) it is not possible to achieve the least cost grain path available as Vicgrain is not a party to the contracts between statutory marketers and VLFC. Additional pressure is being applied by the emerging trends and developments within the grain industry (refer to section 2.5) and integration of the supply chain is essential to growers and end users alike.

Vicgrain has actively pursued discussions with a number of potential bidders, but has not assembled a consortium with any specific proponent at this stage. It should be noted that not all of the proponents who have made public their intent to bid have been prepared to accept Vicgrain as a partner in their consortia.

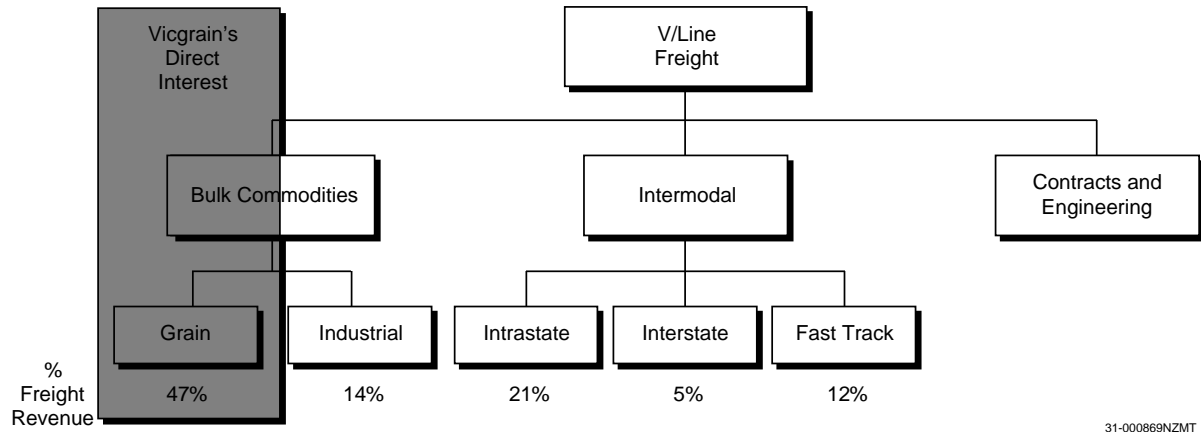
The main reason for Vicgrain not forming a consortium is that an arrangement with only one proponent raises the possibility that Vicgrain could be excluded from the winning consortium, and in turn the efficiencies and benefits available (refer to section 2.6) to a consortium including Vicgrain will not be achievable.

Ideally, Vicgrain should be involved in the sale of VLFC through one of the following:

- an agreement with the successful proponent or other operator allowing Vicgrain control over the grain wagon fleet, or
- Vicgrain organising a *hook and pull* arrangement with a new grain wagon fleet of our own.

Regardless of the outcome of the sale, Vicgrain has the option of increasing the road component of its grain movement operations. Vicgrain envisages that this would occur should freight rates increase or should there not be a suitable level of cooperation between the storage and rail sectors.

Vicgrain's direct interest in VLFC can be illustrated as follows:



Source: TRU percentage revenue based on 1997/98 forecast

One of Vicgrain's objectives is to eliminate the cross subsidisation between the various types of traffic handled by VLFC.

2.2 Historical Relationship Between Vicgrain and VLFC

The Victorian grain handling and transport system from farm to port was substantially in place prior to the modern development of both road transport and harvesting techniques. It is characterised by fixed storage facilities and close spacing of railway routes. The system was developed at a time when the majority of Victoria's wheat crop was exported under regulation, and when the domestic market, unlike the present, was of minor importance. Therefore, there was a very close and secure relationship between the handling and rail transport systems.

This relationship and its importance to the grain industry has been recognised in recent times in the following manner:

2.2.1 CANAC review of transport and handling

During the mid 1980's the Government commissioned the *CANAC Consultants Proposals for the Victorian Grain Handling System* report (CANAC Report). The purpose of this report was to determine the most efficient and cost effective method of handling grain within the Victorian grain handling and transport system from the farms and other sources to domestic markets or into ships at port for export.

The main findings of this report released in 1985 included the following, where the level of service, rates and facilities available to growers was not to be affected and that both capital and operating costs be contained:

- block train movements be adopted
- some line closures occur due to the low volumes utilising rail, where the analysis included costs of transferring tonnages to the rail network from the proposed off-rail sites
- retain traffic on rail and upgrade facilities
- adopt a central receival point (CRP) and consolidation logistical process.

It should be noted that the GEB invested many millions of dollars in making improvements to its own facilities and in constructing higher capacity facilities to improve outloading efficiency and to permit block train movements. The GEB also funded the construction of 50 new grain wagons. V/Line Freight was a major beneficiary of efficiencies gained from this expenditure, however no V/Line capital was ever invested.

2.2.2 Government policy

From the early 1980's until 1992/93 the GEB and VLFC (as well as the ports) were controlled jointly by the Transport Ministry to coordinate the handling function in the grain supply chain. The reason for their coordination stemmed from the need to receive, store, handle and transport grain from country Victoria to both domestic and export terminals for growers, processors, merchants and end-users alike. In 1992/93 GEB was transferred back to the Agriculture Ministry. However, this need for close cooperation has not diminished since the privatisation of GEB and with the impending privatisation of VLFC.

2.2.3 Royal Commission

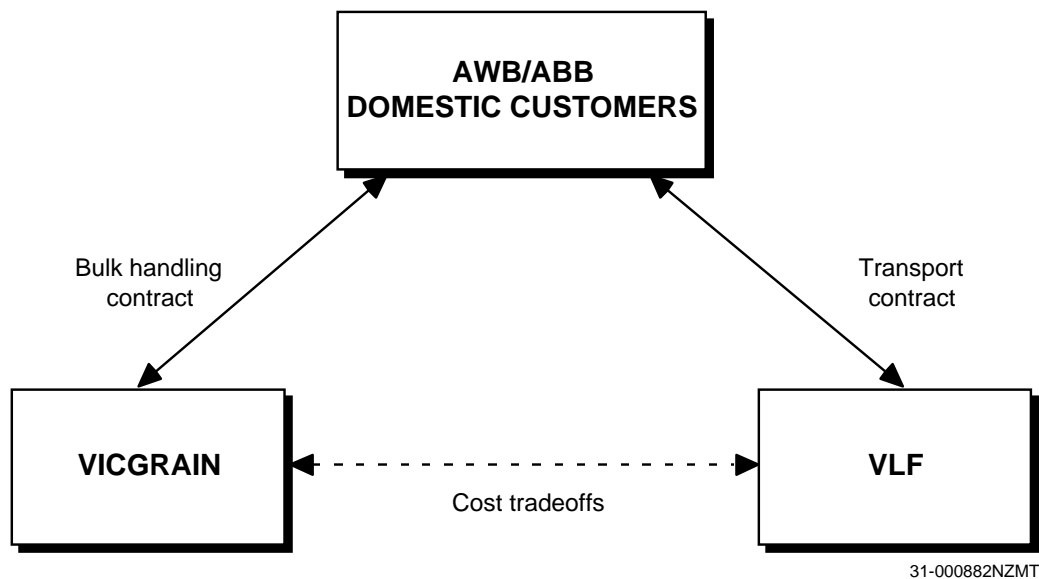
The 1998 Royal Commission into Grain Storage Handling and Transport recognised the very close relationship between the rail transport and grain storage systems in Victoria. It recognised that the lowest cost path for grain could only be delivered where the two systems were able to fully cooperate and had a joint interest.

2.3 Vicgrain Strategic Review of Transport and Logistics

In April 1998 Vicgrain engaged the services of BoozAllen & Hamilton to conduct a major study of the current grain transport and logistics system in Victoria. This study exposed a number of benefits available to both organisations if a coordinated approach be adopted. An overview of these can be found in section 2.6 *Synergy Benefits Between Vicgrain and VLFC*.

2.4 Existing Relationships Limiting Cost Reductions

Initiatives focused on the bulk handling/railway interface will generally increase costs for one or other of the parties even though overall costs are reduced. However, there is no direct commercial relationship between Vicgrain and VLFC. This hinders negotiation of these trade-offs.



2.5 Current Environment - Industry developments and the impact on VLFC

The changing nature of the grain industry and the requirements of the market place now and into the next century mean that the traditional relationship between the storage, transport and marketing sectors are becoming less viable. There are now growing pressures to find ways of achieving better linkages between the three sectors, similar to the type of relationship which exists elsewhere in the major grain producing and exporting countries, notably the USA and Canada.

There are many benefits that are yet to be exploited through close cooperation. Further, changes currently occurring within the grains industry will necessitate closer relationships between the participants in the supply chain. The trends and impacts have been set out in the table below.

Development	Impact on VLFC
Privatisation of the Australian Wheat Board (AWB)	The AWB was corporatised in July of this year and is to be fully privatised in July 1999. As part of this process the AWB has eliminated its 5 State offices in favour of 3 broader regions. This is likely to encourage the use of South Australian ports and rail network to take advantage of the shorter hauls for the Western and Northern districts, resulting in a loss of grain into the Victorian transport and handling system.
Growers & end users requiring a seamless service	Move from a free-on-rail to a free-in-store situation.
Privatisation of the Australian Barley Board (ABB)	The ABB is set to be privatised in July of 1999. Potential involvement by Vicgrain would allow a closer knit of the supply chain as required by both growers and end users.
Deregulation of wheat & barley export	<p>There is increasing pressure by the NCC and WTO to remove single desk status. Deregulation of the export of these commodities will:</p> <ul style="list-style-type: none"> • see greater reliance on notional grain movements and stock swaps, reducing the quantity of grain which is physically moved. Smaller quantities being transported will tend to favour road movement. • encourage international participants into the Australian market who are likely to seek association with bulk handlers. Increased numbers of trading participants in the market will see a greater spread which rail will have to secure to remain viable.
Increase in on-farm storage	Grains stored on farm are moved by road to the rail head and then onto domestic or export terminals, or by road direct to port. Costs of double handling may force more of these commodities to move directly to the terminals by road.

Development	Impact on VLFC
Increase in segregations required by end users	<p>Increased segregations leads to:</p> <ul style="list-style-type: none"> • more mixed trains thereby increasing wagon marshalling and decreasing wagons dropped off at each site. In turn there is an increase in the quantum of rail cycle times and costs; • an increase in the suitability of road transport to facilitate these functions.
Increased use of bunker storage	<p>Grains stored in bunkers require outloading by road and thereby double handling to move by rail. Due to competitive road transport costs (refer to section 2.7.2), an increase in rail costs may make it more economical to move directly from bunker to port by road.</p> <p><i>Note: this harvest Vicgrain will store 1.4 million tonnes of the new crop and 0.5 million tonnes of the old crop in bunkers. Therefore, up to 1.9 million tonnes will have as its initial movement a road based component.</i></p>
Vicgrain rationalising services to facilitate the lowest cost grain path	<p>This could heavily impact on a 24 hour business such as rail if a relationship between rail and handling does not exist</p> <p>Example 1: the imposition of curfews at port or country sites when it is not economically justifiable to operate these hours would increase rail cycle times and rolling stock utilisation.</p> <p>Example 2: not upgrading rail outloading rates at the end of branch lines heavily affects rail cycle times and rolling stock utilisation.</p>

Currently, VLFC transports 85% of the tonnage passing through Vicgrain's system, which represents 40% of the total VLFC traffic. However, the result of the changes occurring in the grain industry, without a link between the rail and storage components, could see an increase in costs for both parties resulting in a reduction in the transport component passing through the VLFC system to between 50-60% of the total tonnes handled by Vicgrain.

Vicgrain is mindful of the political, social and commercial impact of increasing the grain tonnage utilising our road network, and is well aware of the significance of the road funding issue for the State. This provides considerable incentive to ensure that the issues raised by Vicgrain are dealt with as part of the sale of VLFC.

2.6 Synergy Benefits Between Vicgrain and VLFC

2.6.1 Range of opportunities available

With little or no commercial linkage between Vicgrain and the railway, the potential for benefits are modest, perhaps limited to some sharing of costs on silo outloading and shunting. With full integration, opportunities to reduce overall costs could be extended to almost all railway functions, including the following:

- rail wagon loading and unloading
- shunting and marshalling wagons
- maintenance of wagon fleet
- management
- train ordering
- information technology
- corporate overheads.

2.6.2 Multi-tasking opportunities

There are a number of opportunities to utilise our resources more efficiently, which are illustrated in the table below.

MULTI-TASKING OPPORTUNITIES BETWEEN RAIL AND BULK HANDLING FUNCTIONS									
PRIMARY (SECONDARY) POSITION	POSSIBLE SECONDARY (PRIMARY) FUNCTIONS								
	DRIVER	OPERATIONS MANAGER	SHUNTER	CLERICAL	TRAIN EXAMINER	LOCOMOTIVE MAINTENANCE	WAGON MAINTENANCE	TRACK MAINTENANCE	TRACK/BRIDGE INSPECTION
Agent				√	√				√
Road inloader					√	√	√	√	
Rail - sampler					√	√	√	√	√
Rail - loader	√		√		√	√	√	√	√
Rail - wagon release			√		√	√	√	√	
Rail - tractor			√		√	√	√	√	√
Silo cleaning						√	√	√	
Silo sweeping				√				√	
Clerical			√	√				√	√
Operations manager		√							

Note: √ Denotes possible multi-skilling

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2.7 Additional information

2.7.1 Status of Vicgrain negotiations with the main proponents

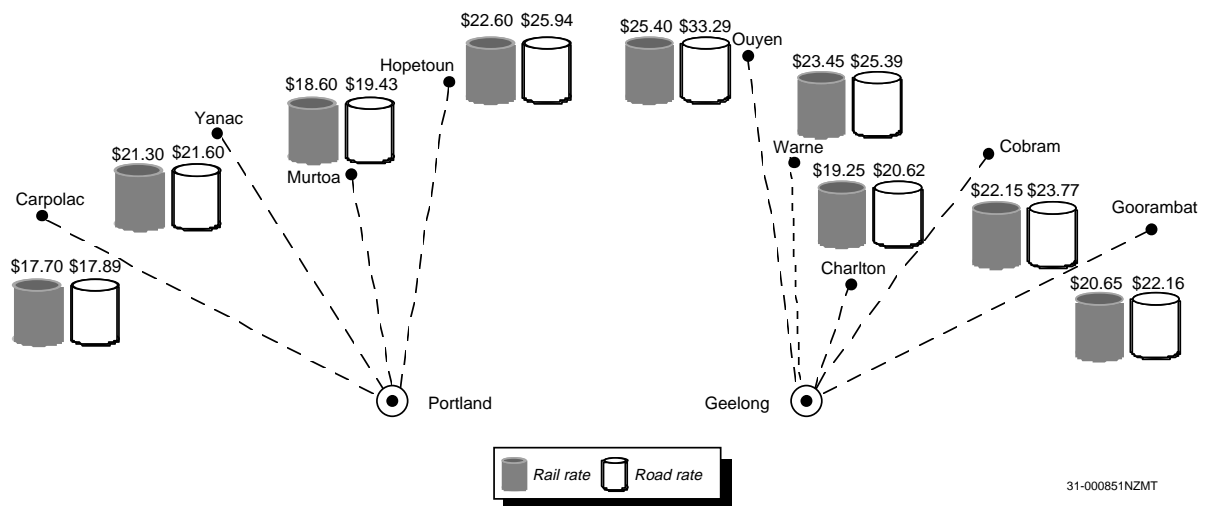
Vicgrain understands that the three main proponents vying for the purchase of VLFC are:

- Freight Victoria (which comprises Rail America and Macquarie Bank)
- Australian Southern Railroad (Genessee & Wyoming USA)
- Australian Transport Network (TranzRail, Wisconsin Central USA).

Due to the importance of cooperation between Vicgrain and the winning proponent for the successful sale and on-going operation of both VLFC and Vicgrain, Vicgrain have initiated discussions with each of the main proponents.

2.7.2 Road competition at various sites

The diagram below illustrates the marginality of the freight advantage of rail over road that is potentially threatened by increased costs resulting from continued inefficiencies and double handling



2.8 Future Relationship Between Vicgrain and VLFC

It is imperative for Vicgrain, VLFC, the State Government of Victoria and the grain industry as a whole that the relationship between Vicgrain and the VLFC (and its successor) is significantly improved as a result of the sale of VLFC.

An isolated response from Vicgrain to the industry changes outlined in this submission would not deliver an efficient grain path to Victoria's grain producers who are also shareholders and stakeholders in the marketing, transport and storage sectors. Both Vicgrain and VLFC have always had close ties, yet further opportunities are available and these should be exploited through cooperation.

3. Investment to Improve Rail Performance

3.1 Improvements in Rail Performance

The Victorian rail network for the bulk transportation of grain could be significantly improved through investment in the following areas:

- improve the rail and storage facilities at Portland to increase rail outloading rates and decrease the need to operate on a just-in-time basis
- purchase of new wagon fleet to increase efficiency and eliminate unsafe work practices
- upgrade 126 rail sidings at Vicgrain sites to increase efficiency and eliminate unsafe work practices
- standardisation of rail gauge to provide greater access to interstate freight
- improve outloading rates at Vicgrain sites by improving the existing elevators, garner bins and outloading spouts
- increase storage capacity at key Vicgrain sites from which shuttle services could be run to ensure 24 hour utilisation of rail fleet.

3.2 Impact of the Existing Relationships of Supply Chain Participants

Presently, Vicgrain has no direct commercial relationship with VLFC. Considering many of the methods to improve rail performance require a capital outlay to the existing bulk handling infrastructure, it appears such expenditure is unlikely to occur while these participants remain separated. Similarly, capital expenditure by VLFC on the wagon fleet and rail sidings to improve the efficiency of bulk handling is unlikely to occur under the current structure.

3.3 Role of Government

Government must play a role in facilitating the most efficient grain path in Victoria through encouraging closer linkages between the bulk handling and rail transport sectors of the supply chain. This will ensure that unnecessary rationalisation of the existing services available to grain growers, marketers and end-users does not occur and will discourage the trend of the increasing road transport component.

4. Contact Details

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5. Glossary

ABB	Australian Barley Board
AWB	Australian Wheat Board
CRP	Central receival point
GEB	Grain Elevators Board (Vicgrain's predecessor)
NCC	National Competition Council
VGS	Victorian Grain (Services) Ltd
Vicgrain	Vicgrain Limited
VLFC	V/Line Freight Corporation
WTO	World Trade Organisation

Appendix A - Map of Vicgrain Storage & Handling System