

SUBMISSION TO THE PRODUCTIVITY COMMISSION INQUIRY INTO GOVERNMENT DROUGHT SUPPORT

Introduction

The Department of Agriculture and Food WA (DAFWA) makes this submission to the Productivity Commission (PC) with reference to data already presented on 16 July 2008. This submission is prepared in acknowledgement of the content of the submission to be provided by the Rural Business Development Corporation (RBDC).

DAFWA has specifically addressed EC interest rate subsidies and their affect on farmers and farm businesses only. The effect on farm dependent rural small businesses and rural communities as a whole has not been discussed within this paper.

This report provides DAFWA's responses to the following issues presented by the PC in their Issues Paper.

1. What is your understanding of preparedness and self reliance?
2. What have been the lessons learnt from the last drought and what strategies are farmers now adopting in response to those lessons?
3. What are the impediments to farmers, farm businesses, farm dependent rural small businesses and rural communities becoming sufficiently self reliant to withstand severe drought events?
4. Is a trigger approach such as an EC declaration a necessary first step to determine individual eligibility for drought relief? Could assistance be delivered on the basis of individual circumstances without an EC declaration? What administrative efficiency issues does this raise?
5. How effective have EC interest rate subsidies been in improving the survival of farm businesses and farm dependent rural small businesses? How are farm business decisions altered by EC interest rate subsidies? Do the current eligibility requirements create adverse outcomes, for example, by creating a disincentive for farming households to seek off-farm income? Would support based on business attributes other than debt be more effective?

This report has been prepared primarily using the north eastern agricultural region (NEAR), a sub-region of the northern agricultural region (NAR), as a case study. As a region, the NAR has received the most EC assistance of all WA's agricultural regions, and the bulk of this assistance directed to the NEAR. Data contained within this report is largely derived from the NEAR, and whole-State data has been provided where appropriate. **Conclusions based on experiences within the NEAR are either applicable elsewhere within WA, or could potentially become applicable to the remainder of WA, if a similar succession of seasons were to occur.**

Most sources of data used within this submission have been provided as Appendices which may be used for further analysis. DAFWA's responses to each issue are provided below.

1. What is your understanding of preparedness and self reliance?

Drought preparedness is now at the forefront for most Western Australian producers and for DAFWA. Preparedness is achieved via the incorporation of drought mitigation plans into risk management strategies through an acknowledgement that drought will occur and will have an adverse effect on business performance. This preparedness may consist of measures to reduce production losses during a drought or establish means to address cash flow shortages that inevitably occur.

Building preparedness of farmers, farm businesses, farm dependent small businesses and rural communities will ultimately improve their self reliance and resilience during future drought events. Self reliance will ultimately enable reduced Government intervention and support during drought events, as farmers are better placed to cope without Government assistance through the measures they have implemented as part of their preparedness strategy.

DAFWA is committed to building both its own drought preparedness and that of its constituents as a means of improving the self reliance of its stakeholders through a range of initiatives. However, improving drought preparedness is an immense task given the nature of production for many Western Australian farm businesses.

Western Australian agricultural production systems are largely unique with regard to the climatic and topographic constraints under which they operate relative to similar enterprises within Australia's Eastern States. Given the nature of agricultural production of farm businesses within WA, the level of drought or dry season preparedness able to be achieved is somewhat limited whilst the means by which drought preparedness may be improved differs to similar producers located elsewhere in Australia. The causes and implications of these differences are discussed below in 2.

2. What have been the lessons learnt from the last drought and what strategies are farmers now adopting in response to those lessons?

Approximately 5,858 of Western Australia's 13,608 farm businesses (Australian Bureau of Statistics, 2007) are involved in broad acre winter cereal production. As an industry, WA grain producers have been the recipients of most of the Exceptional Circumstances assistance distributed in WA, thereby providing a good case study of farmer's responses and preparedness measures to drought. For farm businesses involved in grain production, winter cereal production comprises their major, and in many cases only, income source. Across much of Western Australia's agricultural regions summer rainfall is insufficient to allow diversification into summer crop production, whilst total rainfall and hence pasture production limits significant diversification into viable year round livestock enterprises.

Further compounding preparedness issues is the narrow sowing window available to many cereal growers. In regions such as the NAR, viable production hinges on the availability of adequate sowing moisture by mid to late June. Severe production losses across these enterprises can occur due to reduced rainfall at this key date without the need for a longer term drought event to establish. Preparedness under these circumstances is difficult given the need to commit inputs and expenditure up front in anticipation of suitable growing conditions. Other enterprise types occupying these same climatic conditions are also faced with similar challenges, though their exposure to these preparedness difficulties is not as significant. Livestock enterprises in particular are not as susceptible over shorter duration dry periods as their livestock inventories provide a cash flow source as the season deteriorates.

These challenges in achieving drought preparedness place increasing importance on off-farm investment for most of WA's farm businesses. However, investing off-farm is in itself problematic for many businesses given the liquidity issues associated with diverting funds from revenue and working capital for this purpose. For such businesses the need to source off-farm employment as a means of production risk mitigation may prove an increasing priority. However, the extent of off-farm investment or off-farm employment necessary to adequately offset the production risks that most WA farm businesses are exposed to, is significantly greater than for Eastern States' businesses as demonstrated in Table 1. This table compares the financial position and farm cash flow of the average WA farm business to the national average.

Table 1. Comparison of farm financial position and cash flow of WA and Australian average farms 2006/7

	Western Australian Average	National Average
Farm Capital	\$4,692,810	\$3,612,180
Farm Debt	\$777,350	\$436,520
Farm Equity	\$3,739,430	\$3,064,940
Cash Receipts	\$476,630	\$292,080
Cash Costs	\$378,550	\$250,900
Farm Business Profit	(\$25,960)	(\$49,610)
Profit at Full Equity	\$36,510	(\$12,140)
Rate of Return (excl. Capital appreciation)	0.9%	-0.4%

Source: ABARE, 2008

This data indicates that the average WA farm business is carrying 178% more debt and must meet cash costs 150% greater than the average Australian farm business.

Data presented in the report "Viability of Farming in the North Eastern Agricultural Region" (Appendix 1) suggests NEAR farmers have become more conscious of their need to maintain business liquidity for use during drought and have implemented the following strategies:

- become more conscious of crop potential when applying inputs; and
- reduced plant inventory turnover.

Further observations across the NEAR suggest farmers have become more scrupulous with their application of crop inputs and are now proving more responsive to each season as it unfolds. A universal approach to year in year out crop production seems to have been abandoned. Improved knowledge and more responsible use of price risk mitigation tools have also occurred due to the capacity of such tools to amplify production risks. These measures alone will significantly reduce the financial impact of production losses occurring during dry seasons.

Further impediments to preparedness and self reliance involve potential forewarning of impending drought events. WA does not receive as accurate climate forecasting as the Eastern States given the lack of meteorological investment in researching and analysing Indian Ocean weather patterns. This has proven a key issue in improving drought preparedness, as farmers have been guilty of placing undue priority on such forecasts when the forecast skill is either weak or unknown. DAFWA will continue to focus on extending to farmers the importance of on-ground seasonal conditions and sowing indicators relative to climate forecasts.

To address preparedness issues, particularly in marginal cropping regions such as the NEAR, DAFWA will implement a suite of preparedness enhancement measures including the NEAR Strategy. The NEAR strategy (Appendix 1) will seek to:

“Achieve sustainable and profitable land management in an increasingly uncertain and changing business and climatic environment”.

This strategy was formulated with input from DAFWA staff, agribusiness and farmers and is subject to continuous review and implementation by a ‘working group’ of local representatives.

3. What are the impediments to farmers and farm businesses becoming sufficiently self reliant to withstand severe drought events?

Moving forward, the key challenge for many WA farm businesses is how best to manage low rainfall over key autumn and early winter sowing times. The Bureau of Meteorology and CSIRO report, *Drought: Exceptional Circumstances*, in July 2008 (BOM, 2008) issued the following climatic projections for South West WA:

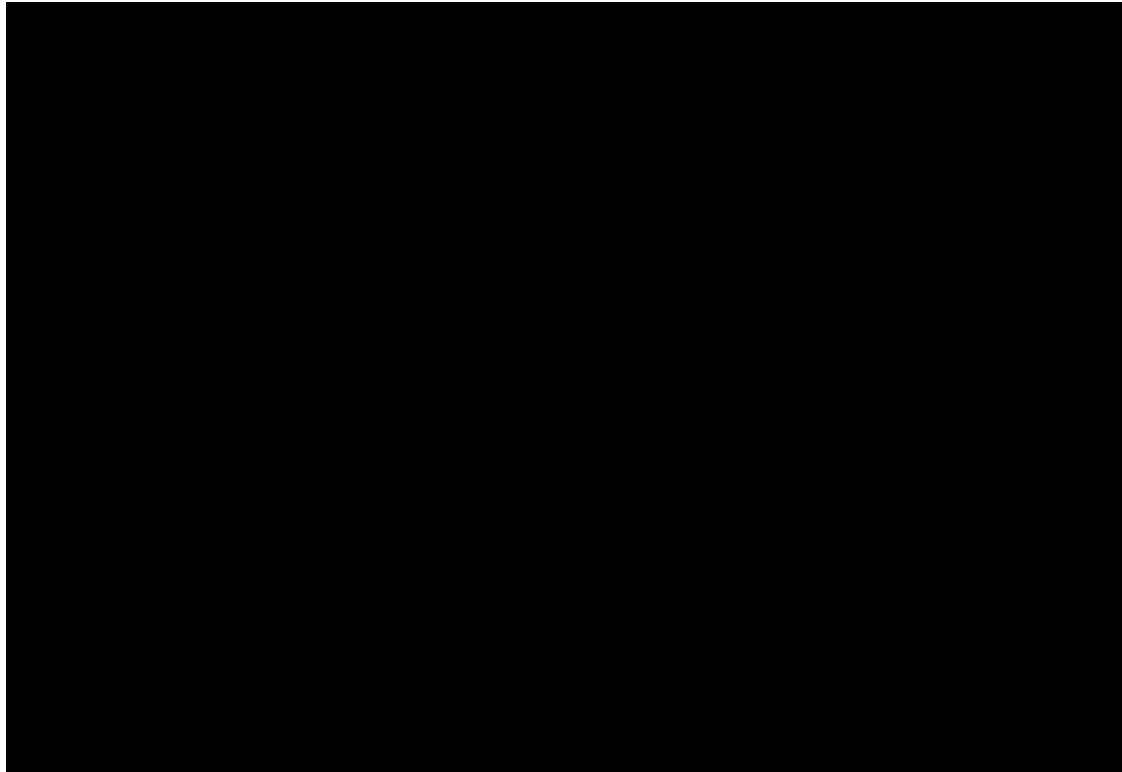
- by 2010-2040, exceptionally hot years are likely to affect about 80% of the region and occur every 1.2 years on average;
- by 2010-2040, exceptionally low rainfall years are likely to affect about 18% of the region and occur about once every seven years on average; and
- by 2030, exceptionally low soil moisture years are likely to affect about 16% of the region and occur about once every six years on average

It is also widely acknowledged that in conjunction with a hotter, drier climate, farmers will also face increasing seasonal variability. Despite these projections, evidence exists that climate change has been an ongoing process in Western Australia. (Appendix 2 p.14 "Viability of farming in the NEAR"). This research illustrates a decline in average monthly rainfall over key sowing dates for the Yuna, Mullewa and Morawa districts of the NEAR over time. This illustration is significant as the months of May, June and July, where rainfall decline has been most significant, represent the most important months of the cereal growing season.

Further productivity growth through technological advances, improved practices, and new crop varieties may potentially offset declines in yield arising from climate change.

Western Australian cereal growers are also facing significant pressure from rising input prices. Figure 1 illustrates change in per hectare crop production costs for the WA Low Rainfall Zone between 2007 and estimates for 2009 (Ward, 2008).

Figure 1. Cropping Cost Comparison for WA LRZ (Ward, 2008)



This table illustrates a 50.90% increase since 2007 in per ha crop direct costs for Low Rainfall Zone farmers in 2009. This has raised the breakeven yield (at a grain price of \$300/t), or yield to cover variable costs, to 0.94 t/ha. The 10 year average wheat yield for this region is 1.41 t/ha. When placed in the context of an increasingly drier and more variable climate, farmers are now forced to risk more capital in a riskier production environment. This trend is consistent across all grain production regions in WA.

Appendix 2 outlines the current cash flow commitments of a cross section of NEAR farm businesses. Using data representative of the average NEAR farm business (p.9) the approximate current fixed, capital and personal costs are summarised in Table 2.

Table 2. Estimated overhead, capital and personal costs for average NEAR farm business 2007/08

Estimated Overheads	\$135,964
Finance Costs	\$115,608
Lease/HP Repayments	\$101,589
Personal Costs	\$79,216
Total	\$432,377

The costs presented in this table represent the costs that the average NEAR farm business must now meet regardless of cropping area planted. These compulsory payment obligations put in context the nature of the financial losses facing WA grain growers in the event of poor seasons. These losses are further magnified when crop income is unable to meet variable costs, a distinct possibility given the increasing breakeven yields described in Figure 1. Given the limited

usefulness of climate forecasting resources in WA, rising breakeven yields triggered by increasing production costs become a challenge for farmers to manage and adjust their cropping programs around. Furthermore, it must be remembered that whilst some inputs will be scaled back in line with crop potential, others are committed too far in advance or are largely independent of yield potential for the necessary adjustments during drought events to be made. This indicates that farmers are walking an increasingly fine line risking variable inputs in marginal cropping seasons, a strategy that will only further erode their preparedness for future poor seasons.

In order to offset these declining terms of trade, farm expansion to realise economies of scale becomes increasingly important. Expansion to achieve economies of scale or spread production risk through achieving geographic diversity is also the most effective long term drought mitigation option. However, based on existing financial positions within the NEAR, analysed in Appendix 2 and 3, there is low capacity for this to be implemented at current land prices. Appendix 5 presents data drawn from a consultancy firm database representing much of WA's agricultural regions (comprising 320 farm businesses). The financial data presented in this appendix gives some indication as to the low current capacity of WA farm businesses to also expand in a financially prudent fashion. Spreading production risk through additional land purchases is also problematic as, given the need to purchase in a suitably removed location, duplication of resources such as plant and labour may be necessary thereby offsetting some of the benefits of an increase in scale.

Expansion or relocation is important as there do appear to be locality factors present in determining the vulnerability of each farm business.

The majority of recipients are located within the NEAR, however, data illustrates that closer relationships between EC recipients may exist as there is a distinct clustering of nearby farms receiving EC assistance in the same year, either 2005, 2006, 2007 and 2008. The clusters of recipients occurring on similar soil types at the same location in the same year indicate that drought preparedness and self reliance are potentially constrained by land system and location within the NEAR. In the event of further droughts in the not too distant future, these localities may be the site of significant structural adjustment given the weakened financial position of many EC recipients outlined in Appendix 3 (NAR EC recipients' data).

For farmers rendered vulnerable due to locality factors or unable to offset production risk by other means, income diversification to spread production risk and improve self reliance becomes increasingly important. However, this is not the sole answer to the problem of drought preparedness as:

- following consecutive poor seasons in 2006 and 2007, the current scale of the average NEAR farm business' financial commitments and overheads equates to an unachievable level of off-farm investment for some businesses to maintain in the event of highly variable seasons and consecutive drought events;
- using debt finance to fund off-farm investment reduces the effectiveness of the investment and may potentially increase the risk profile of the business given the risks associated with the investments themselves;
- off-farm employment may prove impractical given the skills shortage plaguing agriculture and is at best only able to contribute towards funding personal expenditure; and
- viable options for on farm diversification are limited for most WA farmers as many are exposed to the same production risks or are of lower profitability.

4. Is a trigger approach such as an EC declaration a necessary first step to determine individual eligibility for drought relief?

When analysing the impact of the current trigger approach method to EC declaration on the effectiveness of the EC scheme, it must be remembered that:

- approximately 5,858 of Western Australia's 13,608 farm businesses (Australian Bureau of Statistics, 2007) are involved in broad acre winter cereal production; and
- as an industry the WA grains industry has received the most EC funding distributed within WA.

Given the nature of grain production within WA, this trigger method is inappropriate and severely restricts the effect of the assistance in improving the survival of targeted farm businesses within affected areas. The need for an EC declaration and two years production losses to be experienced prior to accessing EC assistance fails to acknowledge the impact of low rainfall over key seeding dates on financial performance. Table 3 illustrates the impact of poor autumn and winter rainfall on crop yield and business performance at Mullewa in 2006 and 2007.

Table 3. 2006 and 2007 annual rainfall, wheat yield and farm business performance at Mullewa, NEAR

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Total
Average Annual Rainfall (mm)	13.1	17.6	19.2	21.7	47.3	64.8	60.6	42.1	21.7	13.3	8.8	7.5	337.6
2006 Rainfall (mm)	32.8	22.9	4.8	25.6	<u>2.7</u>	<u>3.0</u>	<u>21.3</u>	27.6	20.4	1.6	2.0	7.6	172.3
2007 Rainfall (mm)	27.2	3.5	<u>0.3</u>	<u>2.6</u>	<u>14.5</u>	33.3	58.3	11.2	19.1	14.1	0.6	33.1	217.8
6 year Average Wheat Yield to 2001[^]	1.73 t/ha												
2006 Wheat Yield	0.61 t/ha												
2007 Wheat Yield	0.74 t/ha												
Farm Operating Profit 2006* (\$/Eff ha)	\$7/Eff ha												
Farm Operating Profit 2007[^] (\$/Eff ha)	\$3.59/Eff ha												

* Bank West Benchmark data 2006/7 for NEAR (Appendix 6). [^] Viability of farming in the NEAR data (Appendix 2). Farm operating profit is exclusive of finance, capital, taxation and personal costs.

Rainfall Data Source : BOM, www.bom.gov.au

Yield Data Source: CBH Receivals Data

In the 2006/07 season alone, poor wheat yields contributed to debt accumulation for most NEAR farm businesses. This accumulation saw average farm debt expand from \$193/Eff ha to \$248/Eff ha within the NEAR (Bankwest, 2007). Despite this immediate debt increase, Figure 2 presented in section 3.0, illustrates that most EC recipients within Mullewa shire did not access EC assistance until 2007, despite recording negative farm business profit in 2006/07.

Given the severity of the seasonal conditions experienced across the NAR in 2006/07 & 2007/08, farm businesses meeting other eligibility requirements regarding off-farm assets, labour, etc. should have been eligible for immediate assistance. The delay in accessing assistance has contributed to some of the issues to be discussed in 5.

5. How effective have EC interest rate subsidies been in improving the survival of farm businesses and farm dependent rural small businesses? How are farm business decisions altered by EC interest rate subsidies?

Effectiveness of EC Interest Rate Subsidies

Initially Interest rate subsidies may have played a role in reducing debt accumulation and maintaining morale amongst recipients. Recipients perceptions of EC assistance are presented below, these perceptions certainly indicate EC assistance has made a positive contribution to their farm business:

Table 4. Extent to which EC IRS Contributed to Positive Farm Outcomes

Extent to which EC subsidy contributed to positive farm outcomes	At least did something	At least quite a lot	Very Little	Not at all	Don't know /NA
	%	%	%	%	%
Maintain profitable farm	87	67	22	7	4
Retain natural resource base	82	65	17	15	3
Diversify farm mix	52	26	26	35	13

Source: Patterson Market Research, June 2008

However, given the prolonged nature of the drought in many areas of WA, particularly the NAR, evidence suggests that even maximum annual payments of \$100,000 are now insufficient to prevent further debt accumulation and deterioration of the financial position for many WA farm businesses.

Data drawn from Appendices 2 and 4 illustrates the decline in financial position of a selection of NEAR consultancy firm clients from 2001 to 2007. Table 5 illustrates changes in financial position from an average position over 1996-2001 to 2007. This data is presented in page 11 of Appendix 2.

Table 5. Changes in key farm financial data 1996-2001 to 2007 for NEAR farm businesses

	Average 2001	Average 2007
Effective ha farmed	3,943 ha	4,801 ha
% Equity (farm)	86%	68%
Farm debt per eff ha	\$119	\$285
Plant value per eff ha	\$171	\$191
% ha sown to crop (6 yr av)	76%	55%*
% ha sown to legumes (6 yr av)	25%	5%
Wheat Yield (6 year average)	1.68 t/ha	1.12 t/ha
Nitrogen / ha crop (6 yr av)	40.3 kg/ha	11.4 kg/ha
Phosphorous / eff ha (6 yr av)	9.0 kg/ha	4.4 kg/ha
Closing sheep number	2,406	1,332

Source: Planfarm, 2008

The most important data presented above is in the increase in average farm debt from \$119/Eff ha over 1996-2001 to \$285/Eff ha in 2007 and the resulting decline in farm equity %. This decline in equity due to debt accumulation has been slowed by increases in land values over the period 2001 to 2007 (Appendix 7). All farm financial data from Appendices 2 and 4 were drawn from NEAR clients of a WA agricultural consultancy firm, the 2007 data being drawn from 27 NEAR farm businesses; approximately 9 of these farmers have received EC interest rate subsidies. Table 6 benchmarks these businesses in terms of current business equity and is a summary of data contained within page 5 of Appendix 2.

Table 6. NEAR farm financial positions

	Top 25%	Group Average	Bottom 25%
Farm Size (Eff ha)	5,684	4,801	4,165
Land & Improvements	\$4,211,173	\$2,889,997	\$1,836,981
Plant	\$1,116,795	\$917,700	\$686,707
Cash Accounts	\$299,736	\$121,890	\$9,570
Total Farm Assets	\$6,607,722	\$4,513,125	\$2,851,952
Farm Debt	\$1,011,390	\$1,117,021	\$1,148,817
Hire Purchase Debt	\$183,756	\$152,612	\$161,717
Total Farm Liabilities	\$1,195,146	\$1,269,633	\$1,310,534
Farm Equity (\$)	\$5,412,576	\$3,243,492	\$1,541,418
Farm Equity (%)	81%	68%	52%
Net Off-farm Assets	\$2,209,251	\$1,065,748	\$168,097
Total Business Assets	\$8,816,973	\$5,578,873	\$3,020,049
Business Equity (%)	84%	70%	51%
Debt to Income (2008 Budget)	0.79	1.25	1.90

Source: Planfarm, 2008

Table 6 and data contained within Appendix 2 indicate the average financial position of NEAR farm businesses is sound with business equity of 70%. Specifically 15 of the 27 surveyed businesses possess equity of greater than 75%. The financial position of the bottom 25% is poor with equity of only 51%. EC recipients amongst this group occupy the bottom half of businesses when arranged in order of business equity. Therefore it can be concluded that (with reference to data presented in appendix 2 and sections 3 and 4) the assistance has been insufficient to prevent a potentially terminal decline in business financial position. Furthermore, subject to the continuation of traditional lending practices, the ongoing survival of businesses within the bottom 25% is dependent on seasonal conditions as:

- finance obligations now exceed maximum available assistance; and
- further debt accumulation could lead to foreclosure.

These conclusions are applicable to most EC recipients across this region as evidenced by Appendix 3 "Financial position of NAR EC Recipients". Table 7 compares the group average financial position from Appendix 2 ("Viability of Farming in the NEAR") to the group average financial position of all EC recipients within the NAR.

Table 7. Comparison of NEAR average farm financial position

	Appendix 2. Average	All Recipients Average
Farm Area (Eff ha)	4,801	3,688
Farm Assets	\$4,513,125	\$4,111,744
Total Assets	\$5,578,873	\$4,544,758
Farm Liabilities	\$1,269,633	\$1,609,147
Net Business Equity (\$)	\$4,309,399	\$2,860,735
Equity %	70%	63%

As a region the NAR has received more EC assistance than any other WA agricultural region, and the NEAR (sub region of the NAR) has received the bulk of the EC assistance distributed within the NAR.

In the wider context of WA agricultural producers (excluding pastoral enterprises) as a whole, some of these results are not applicable. This is partially as a result of the severity of the drought events in 2006 and 2007 within the NEAR relative to drought events experienced elsewhere within WA. Table 8 presents data sourced from Appendix 5 demonstrating the current financial position of 320 consultancy firm clients situated across the WA agricultural regions. Key financial data from this resource is summarised in Table 8.

Table 8. Whole State farm financial data

	Low Rainfall Zone - Average	Medium Rainfall Zone - Average	High Rainfall Zone - Average	State Average
Farm Size (Eff ha)	2,989	2,970	2,711	2,928
Farm Assets	\$5,017,754	\$6,668,713	\$7,253,871	\$6,341,396
Total Assets	\$5,783,908	\$7,624,107	\$8,176,323	\$7,241,144
Total Liabilities	\$1,488,409	\$1,307,578	\$1,505,343	\$1,390,891
Business Equity (\$)	\$4,295,499	\$6,316,529	\$6,670,979	\$5,850,253
Business Equity (%)	75%	81%	82%	80%

Source: Farmanco, 2008

This data indicates that on average these farm businesses are currently not as vulnerable as those within the NEAR. However, if faced with a severe and prolonged drought event such as that experienced across the NEAR, the financial positions of these businesses could potentially deteriorate to the point of vulnerability, given their existing finance commitments alone greatly exceed the maximum assistance available. Under these circumstances significant and potentially terminal debt accumulation could be expected.

How are farm business decisions altered by interest rate subsidies?

Scope may have existed previously for farm business decisions to have been significantly affected by the availability of interest rate subsidies. Table 9 identifies probable outcomes for EC recipients without EC IRS.

Table 9. Probable outcomes without EC IRS

Probable outcomes without EC subsidy	Net likely	Neutral	Net unlikely	Don't know /NA	%
	N=54 %	N=54 %	N=54 %	N=54 %	
Tighten financial belt	96	0	4	0	100
Seek work off-farm	63	4	31	2	100
Sell off-farm assets	63	13	24	0	100
Sell the farm	44	13	41	2	100
Lease all or part of farm	30	17	54	0	100
Change enterprise mix	30	19	46	5	100
Enter share farm arrangement	26	20	48	6	100
Continue business as usual	24	7	69	-	100

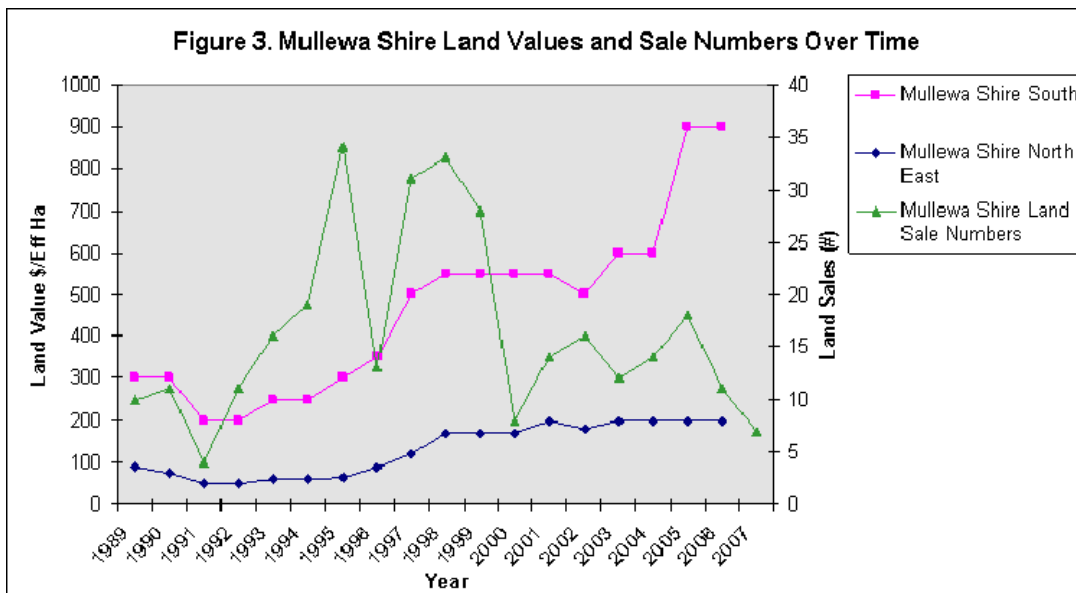
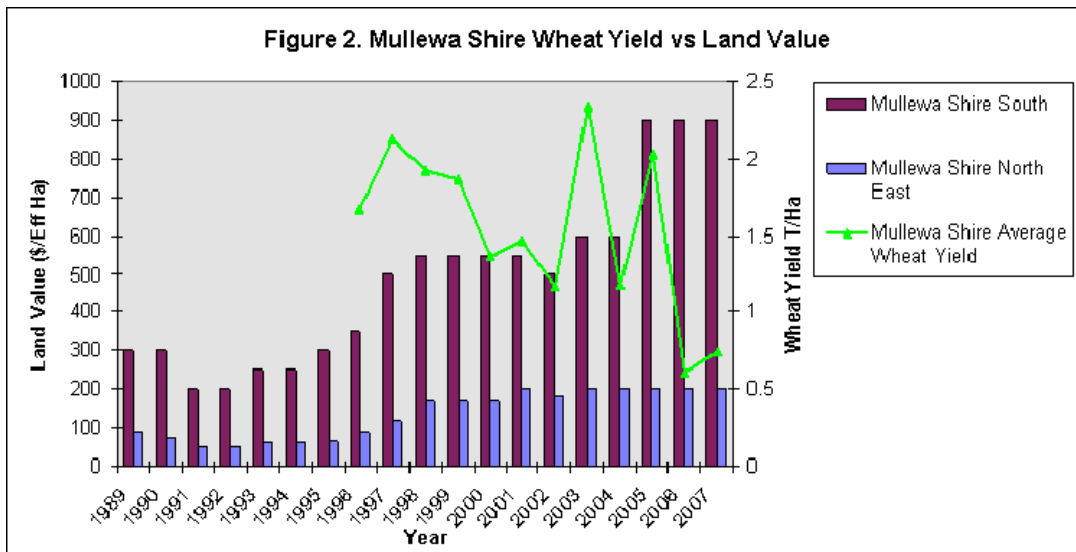
Source: Patterson Market Research, June 2008

The likely responses indicated by this survey predominantly revolve around reducing non-essential expenditure, seeking work off-farm and liquidation of off-farm assets. However, given data presented previously within this submission, these outcomes are now likely to occur *even with* EC assistance, given the amount of assistance available relative to the current financial positions and commitments of recipients in longer term drought affected regions.

Furthermore given the erosion of business equity prior to and following EC declaration, there now appears limited opportunity for farm managers to adjust their approach to business management. This is a result of the somewhat insignificant contribution EC IRS assistance now makes relative to farm expenditure on overheads, personal expenses and financial obligations, without taking into account potential losses on direct crop expenditure.

Any claims as to the role EC assistance has paid in enabling recipients to maintain farm ownership and enable rebuilding is questionable within the NEAR. Given the debt accumulation within this region as described in this submission, the level of assistance received on an individual basis is somewhat insignificant. Instead the assistance appears to have given confidence to lenders and other stakeholders with an interest in the business to maintain their interest. The following trends are able to support this statement:

- Land values across the NAR have failed to reflect the increasingly risky nature of production within the region. (Figure 2.)
- Annual land sales have declined whilst land values have remained constant during a period of increasing production volatility and declining farm financial position. (Figure 3.)



Land Value and Sale
Data source: Valuer General, Landgate WA.

Data for this decade presented within these figures is particularly significant as the period 2000-2008 has seen unprecedented production volatility across the NEAR after a period 1990-1999 of consecutive, consistently good seasons. Based on this data (consistent across the entire NEAR) the following conclusions can be made:

- EC assistance has provided lenders with the confidence to continue lending to vulnerable businesses, thereby assisting in maintaining farm ownership and low sale numbers; or alternatively
- demand for farmland within the NEAR may be uncertain or even non-existent. Ongoing support by lenders is appearing to be provided on a season by season basis, subject to the capacity of the business to generate sufficient cash flow to meet its financial obligations, given potential lack of demand for NEAR farmland. In this case land values and business assets need urgent re-evaluation. Exit strategies for vulnerable farm businesses may be needed, as evidence

presented in this submission suggests some businesses may be verging on insolvency if a fall in land values to a level commensurate with current demand were to occur.

These conclusions are not necessarily the trend across all regions within WA as demonstrated by the stronger farm financial positions presented in Appendix 5.

The potential distortion of land values by EC assistance must be acknowledged as a potential threat to the drought preparedness and self reliance of non-recipient farm businesses as discussed in section 2.

Conclusions

Based on data contained within this submission, the Appendices and data presented to the Productivity Commission in July, DAFWA makes the following conclusions about EC assistance in WA.

Effectiveness of EC assistance

- Current levels of assistance are insufficient to prevent potentially terminal debt accumulation during severe drought events. Given current finance costs and other compulsory obligations such as overheads, \$100,000 is insufficient to prevent significant debt accumulation that may prove unsustainable in subsequent seasons.
- If EC assistance is to continue, more immediate assistance that is not necessarily triggered by an EC declaration should be provided. This should acknowledge the importance of late autumn/early winter rainfall in determining crop performance and hence business cash flow.
- The importance of off-farm investment and off-farm income in offsetting production risk should be recognised. Furthermore, eligibility thresholds for these should acknowledge the significantly greater capital requirements of WA businesses relative to Eastern States' enterprises.
- Despite receiving assistance, many recipients within the NEAR remain vulnerable. There appears limited scope for some farm businesses to recover if the current trend of variable seasons continues. These businesses have limited capacity to prepare for drought and achieve self reliance on the basis of their location (climatic influences), land systems, scale and financial position, each of which dictate managerial responses on a seasonal basis, limiting the necessary flexibility that is required to cope longer term within this environment.

Appropriateness of EC IRS assistance

- Assistance is currently being provided to farmers who are viable on a year to year basis dependent on ongoing favourable seasons. Some of these businesses are potentially on the verge of insolvency if land values were to decline.
- Assistance is provided to businesses carrying debt that may not have significantly diversified their income streams through either off-farm investment or off-farm employment, despite these strategies being considered prudent business management strategies for WA grain growers in marginal regions.
- Some of these businesses will continue to require business assistance given their location, land systems and scale prevent establishment of a sustainable business structure.

- Business management is critical in determining business financial position though this may be dictated by the factors listed above and the financial position of the business. This limits the scope for extension to address the vulnerability of some farm businesses.

Further issues for consideration

- If EC assistance is to continue in its current format, DAFWA's comments regarding its effectiveness and implications for WA farmers are submitted for consideration.
- Assistance based on operating expenditure may prove more equitable and suitable. Assistance which is independent of financial position may also prove less of an impediment to structural adjustment.
- Exit assistance packages need to be targeted at a regional level reflecting the characteristics of farm businesses within each region.
- Investment in improved seasonal forecasting and communication to growers will have a significant effect in improving drought preparedness through improved capacity to manage poor seasons via forewarning.
- Investment in R&D will have a positive impact for the whole farming community and may represent a more efficient support mechanism (refer Appendix 10.), given lack of effectiveness of EC assistance in some regions.
- R&D must be regionally targeted. Evidence presented within this report indicates that research into sustainable business structures within marginal areas such as the NEAR must be undertaken. Many vulnerable farm businesses have limited scope for recovery, therefore sustainable business structures for these enterprises need to be developed.

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