Philipson, Mike (ESCOSA)

From: John Hill [redacted]
Sent: Friday, 7 September 2018 2:14 PM
To: Philipson, Mike (ESCOSA)
Subject: SA Grain Supply Chain
Attachments: ESCOSA PORT CONTESTABILITY.docx; ESCOSA VITERRA PRICING.docx; LUCKY BAY PROPOSED NEW GRAIN PORT.docx; 5 yr average.jpg

Categories: objective done

Attn Mike Philipson and Sean McComish

Dear Mike and Sean

Subject ESCOSA inquiry into the SA Grain Supply Chain

Further to our meeting of 30th August 2018 I attach my submission. Please note there are a few changes to the documents I sent you immediately prior to out meeting. While there are areas of duplication, not all the input in my initial submission are repeated, for example the comparison of charges between incorporated body and a cooperative .

Two scanned docs referred to at the end of the contestability doc in next email

I am happy to discuss any matters arising from this submission.

Thank you
Regards
John Hill
[redacted]

7 September 2018

ESCOSA- VITERRA PRICING

This inquiry was instigated following recent complaints from South Australian grain farmers in relation to high storage and handling charges by Viterra. The justification for referral to ESCOSA is the contention that the export grain supply chain in this state is a monopoly. In their submission Grain Producers SA have indicated an approximate $17 per tonne higher charge by Viterra for basic handling charges when compared with equivalent charges by CBHWA . GPSA have also complained about lack of transparency in pricing due to Viterra's bundling of charges some of which are the passing on of charges by other service providers.

When grain storage and handling providers were simply involved in grain handling it was relatively easy to compare charges between the five grain handling entities in Western Australia, New South Wales, Queensland, Victoria and South Australia. In that period South Australian charges were consistently the lowest of these five organisations. Given the major industry changes in South Australia i.e. Initial development as a cooperative as SACBH , formation of Ausbulk with its expanded roles, merging of Ausbulk with ABB Grain, sale of ABB grain to Viterra and subsequent sale of Viterra to Glencore it is important to find a reasonable basis to assess the fairness of handling charges levied by Viterra.

It is worth noting that Ausbulk was a corporate entity and not a cooperative prior to the acquisition by Viterra [unlike SACBH and CBHWA] yet grain handling charges levied by Ausbulk were still the lowest in Australia at that time and Ausbulk funded the 2005 development of the new Outer Harbour export terminal within that charging structure at a time when average harvests were much lower than those of the post Viterra acquisition era. So we had an incorporated body charging less than a cooperative for similar services.

Viterra was an international company with its headquarters in Canada when acquired by Glencore. Given this it is difficult to establish with a high degree of certainty the level of investment ascribed to the South Australian grain supply chain assets. Glencore is a major international company and was named in recent press reports in relation to 'underpayment' of Australian income tax.

This submission establishes quite clearly that there are very high barriers to entry into the South Australian export grain supply chain. Some of these barriers may not be evident to persons without very detail knowledge of the supply chain. Given this monopoly status it is inappropriate for Viterra to factor proposed higher handling charges into to any acquisition process and in turn for Glencore to do similar.

Based on the above the simplest and most relevant avenue for assessment of monopoly charging is a comparison with charges levied for a similar service by a similar organisation. ESCOSA must compare the unbundled charges for the specific monopoly service to provide a valid assessment of the situation. The obvious and most valid available criteria for comparison being CBHWA where most grain is also exported due to the small domestic market. CBHWA operations are very similar to Viterra's in almost all facets of its operation.

It is noted that ESCOS's Draft Report refers to comparison of charges with 'eastern state grain handling charges', this is not as relevant as CBHWA's due to the much larger eastern states domestic market and climatic zones . Comparisons of bundled charges are very misleading to the point of

irrelevance to this inquiry given the very different distances from port and other components of a bundled charge.

The lack of transparency in Viterra's charges due to its bundling of charges, many of which relate to passing on charges of other service providers disguises its handling charges. The additional $17 per tonne charged by Viterra when compared with CBHWA's handling charges is a very significant difference i.e. approximately double, not some minor variation. This should be the key element under scrutiny.

There are good grounds for contending that charges in SA should not have increased with Viterra's acquisition of the system and even that they should be lower than those of CBHWA these include;

- The SA grain storage industry commenced later than the other Australian systems [refer initial submission] and incorporates better facilities with a higher proportion of less labour intensive self emptying concrete and steel bin storage.
- Due to the multiple ports and distribution of grain production in areas close to ports in South Australia a significant proportion of export grain is delivered from farm to port storages which reduces double handling. This is unique to South Australia.
- Five year averages of grain receivals in SA between 2007/08 and 2016/17 have increased by nearly 50%, refer attached table. This is particularly relevant given that the high component of fixed costs in the handling process. E.g. staffing levels of receival grids do not change with tonnage variations. Electricity is probably one of the few variable costs per tonne.
- There has been no requirement for additional expenditure on port facilities, these were all established prior to the initial sale to Viterra.
- The combination of a 50% increase in average grain receivals in a fixed cost environment and the elimination of a need to develop more port facilities should have seen a reduction in grain handling charges not an increase while still providing adequate returns.
- There has been no further development by Viterra of the prototype Mobile Fast Rail Loading units developed by Ausbulk in 2003. These units increased train loading rates from 150 tph to 800tph and operate on concrete cells adjacent to the rail track. They had signwriting saying 'saving country rail' on one side and 'saving country roads' on the other. They now simply have the name 'Viterra'. A message? This lack of progress in 15 years demonstrates that Viterra has not invested in making rail more efficient despite the fact that nearly all of its storages located on rail lines, whether ARTC track or grain only [Genessee and Wyoming] track, have vertical concrete cells adjacent to the rail line. This is a major failure in its focus on making rail more efficient. This failure encourages more grain freight onto road trucks with consequent addition cost to the community.
- The development of the storage system under SACBH and Ausbulk, including very capital intensive port facilities, was funded via handling charges augmented in decreasing amounts, up to about 1988, by grower refundable tolls. The fact that there was no recourse to external borrowing in this time demonstrates the adequacy of the charges even in a period of development of the system to cover operating costs and major capital expenditure.
- Both Viterra and even more so Glencore will have benefitted by savings in rationalisation of management and administration costs. Simply look at the reduction in levels of South Australian jobs at what was' Grain House' on South Terrace.

- AS a marketer of grain Viterra can benefit significantly from blending of different qualities of grain by virtue of its monopoly storage and unique knowledge of volumes, quality and location of grain in its system.

Conclusions

Viterra's unbundled handling charges should not be more than those levied by CBHWA for all the reasons outlined above. This is identified as approximately $17 per tonnes by Grain Producers SA. This is a very significant amount at approximately double the equivalent charges for this service in WA.

Bundled charges hide any excessive charge components and reduce the ability to identify potential cost savings in the non monopoly components of these services. For example lower overall bundled charges in South Australia due to lower freight costs, as grain is produced much closer to ports than in other states, which more than offsets higher handling charges would give a false impression that the grain supply chain in SA is more efficient.

The consequence of this excessive handling charge is the likelihood of fragmentation in the South Australian Bulk Grain Industry Supply Chain with sub optimal outcomes. This has already commenced on Eyre Peninsula with the Lucky Bay project where cost to the general community will be significant.

There is no yardstick to demonstrate that Viterra has made grain handling more efficient, in fact there are complaints of lack of infrastructure development by Viterra made by the proponents of Lucky Bay. There have been parliamentary inquiries into poor service by Viterra, something that did not occur under SACBH or Ausbulk.

John Hill

7 September 2018

South Australia grain receivals

Year	M/T	5yr av M/t	Average of 5 yr averages
2016/17	9.2	6.9	6.5
2015/16	6.0	6.4	
2014/15	6.5	6.9	
2013/14	7.1	6.2	
2012/13	5.5	6.2	
2011/12	6.7	5.8	4.7
2010/11	8.5	4.8	
2009/10	6.4	4.4	
2008/09	3.9	4.0	
2007/08	3.5	4.5	

VITERRA's CLAIMS ON LACK OF BARRIERS TO ENTRY IN THE GRAIN SUPPLY CHAIN

Viterra makes a wide range of claims in relation to the services it offers to growers. Most if not all of them were in existence even in the 1990's .As an example the 'warehousing' service option was introduced in 1988. It is possible that persons without an in depth knowledge of the various factors influencing the supply chain would not appreciate the lack of relevance of many of these claims to the purpose of this inquiry.

It also claims that 'there are low barriers to entry in the grain supply chain'. This is a key and totally unjustifiable statement in the context of this investigation by ESCOSA.

It also claims that its operational environment is unique. This is incorrect as variability of production is a factor in all Australian and global grain supply chains.

WHY THE BARRIERS TO ENTRY ARE PARTICULARLY HIGH IN SOUTH AUSTRALIA

The system of ports and country silos was designed to be efficient and fully integrated. Each of the geographically separate regions Eyre Peninsula, Yorke Peninsula and the Adelaide catchment area have a fully Panamax capable port and at least one other port of lesser capability. This caters for the minimisation of sea freight costs.

The vast majority of grain produced in South Australia is exported due to the small domestic market. Therefore export facilities that can service export markets efficiently in terms of the vessel sizes that can be accommodated and the speed at which these vessels can be loaded are fundamental to any assessment of barriers to entry.

South Australia has a shallow coastline and the capability of the existing panamax ports has only been achieved by very expensive dredging or a long jetty to achieve deep water even in locations offering the best opportunities. In the case of Outer Harbour the dredging cost has only been viable due to cost sharing with the container industry. Port Giles has a combination of jetty and minor dredging and Port Lincoln has an extensive jetty both are in favourable locations. The lack of easily accessible deep water is a paramount factor in assessing the barriers to entry in respect of ports. The SA Deep Sea Port Committee, that I was a member of for its duration carried out very extensive studies on this subject.

The speed at which vessels can be loaded and the availability of more than one port per catchment area is also a factor in in minimising storage requirement. In a large harvest an intensive shipping programme during the harvest period reduces the need for storage capacity. This is another factor in determining the barriers to entry. The Adelaide catchment area has Outer Harbour, Inner Harbour and Port Pirie. Yorke Peninsula has Port Giles and Wallaroo. Eyre Peninsula has Port Lincoln and Thevenard.

The existing Viterra owned port facilities are sunk costs and comprise significant components of efficient steel and concrete self emptying silo systems, sophisticated computerised central control systems, fast ship loading rates and good grain intake facilities.

These export facilities are very difficult or impossible to duplicate given the limited volumes of grain in each of the three catchment areas and the variability of production when considered on a specific area basis.

Infrastructure pathways, both rail and road as well as electricity are directed [at public expense] towards existing export facilities, in some cases serving other major industries as well.

Studying the attached criticism of the proposed Lucky Bay facility demonstrates the validity of the above comments and the shortcomings of this project.

Inland silos have been developed over time with the size and location being identified after very careful analysis of all relevant factor including levels of grain production, access to road infrastructure for farmer deliveries and subsequent access to road and to rail infrastructure for transfer to port.

Inland silos have a combination of capital intensive concrete and steel self emptying bins and lower capital cost shed and bunker storages. The former are essential for segregation and all weather operation the latter catering for increases in growth of mainstream grain production. Another consideration is proximity of grain production to a port where the option is to increase port storage which allows delivery ex farm.

In 2003 the Mobile Fast Rail Loader was developed by Ausbulk. These mobile loaders enabled much faster loading of rail wagons by introducing a valve in concrete cells that adjoined the rail track at inland silos. It was specifically targeted at eliminating competition from other storage providers at rail sites as, in the absence of trackside concrete bins, they required the construction of very large expensive over track bins to load trains.

This careful development of an integrated supply chain over many years leaves little or no real opportunity for locations for competitive country storage of export grain. Historically the whole grain growing area of the state has been covered given the fact that all capital expenditure on infrastructure has been borne equally by all grain growers on a per tonne delivery basis. In addition to this having a statewide coverage reduces the financial risk of variability of production in specific areas.

The above demonstrates the extremely high barriers to entry in the South Australian grain export supply chain.

In order to illustrate the barriers to entry;

Consider the York Peninsula, it has three major storages in Port Giles, Wallaroo and Ardrossan all with very fast harvest intake facilities, the first two export grain and all three are within a few kilometres of the grain production area. Ardrossan has to export via Port Giles. The only inland silo is at Maitland at the only major key road junction in the middle of Yorke Peninsula with easy access to export via either Port Giles or Wallaroo. There are no other viable port locations. Distances from farm to port are very short.

In the case of the Adelaide catchment area there is no location between Port Augusta and Adelaide with deep water or other infrastructure access suitable for a port facility. There is limited grain

production in the South East as well as a lack of locations with water depth or suitable infrastructure.

The geographic separation of the SA grain industry production and therefore export supply chain into three regions i.e. Eyre Peninsula, Yorke Peninsula and the Port Adelaide catchment area significantly intensifies the level of monopoly control as each region requires port and inland silos specific to these areas. This reduction in catchment increases risk and the difficulty of competitive port development.

South Australia already has more grain export ports per tonne of grain produced than any other state in Australia and almost certainly in the world.

It is totally illogical to deny the existence of a very comprehensive Viterra monopoly of the grain industry export supply chain.

To add further dimensions to this monopoly status. All grain is delivered to the system by growers using a pre-coded delivery card [like a credit card] which identifies the grower and amongst other things the 'hundred' where the farm is located. A hundred is a very small subset of counties. A storage owner such as Viterra then knows exactly where and how much of each grain type and quality is produced and stored even if this grain is owned by a different marketer. This 'production by hundred' information is unique to Viterra, is not shared and provides Viterra with a massive advantage in terms of storage planning, logistics and marketing.

Included in the email are two scanned documents illustrating the level of information available to a storage provider using Eyre Peninsula as an example. Join the two A4 scanned halves together.

PROPOSED NEW GRAIN PORT

LUCKY BAY ON EYRE PENINSULA

THE PROPOSAL

Details of the proposal, based on newspaper reports, are as follows;

A $115 million grain port development at Lucky Bay is proposed by the TPorts Company [the operator of the failed Wallaroo to Lucky Bay ferry] and Rob Chapman. It is financed by Inheritance Capital Asset Management, Duxton Asset Management and Sea Transport Corporation.

It is proposed to use a Chinese built 87m long self-unloader vessel with a 4 m draft to transfer grain to a bulk carrier moored 5 km offshore.

The grain will be sourced from a storage facility at Lock and they have a 30 hectare site at Lucky Bay capable of storing 430,000 tonnes of grain in bunkers.

The construction will be supervised by Ahrens. The first grain is expected to be loaded in October 2018.

COMMENTS

THE LOADING OPERATION

Lucky bay is shallow and a fully loaded 60,000 tonne panamax bulker requires 14.5 metres of water at low tide and is over 250 metres long. As it is not loading in a dredged berth it will not be able to take advantage of the normal twice daily 2 metre high tide which enables sailing fully loaded on a high tide.

A self-unloader with a fully loaded draft requirement that exceeds the berth depth at low tide cannot be used. This size limit implies multiple trips to complete the loading process of a bulk carrier. The exact ship loading method needs clarification, however a self-unloader with the height and reach spout capability of loading an empty Panamax vessel, which stands high in the water [discharge of ballast in this area with its valuable aquaculture is prohibitive], will be required at the point of transfer to the export vessel. This size self-unloader is expensive and will need high utilisation to be economic.

Loading a bulk grain vessel demands filling, or part filling, each hatch in a specific sequence. Usually this is carried out at a berth where there are multiple ship loaders that can fill all the hatches without the ship being moved by simply redirecting grain flow on the conveyor belt to the appropriate loader for the hatch being filled, e.g. Port Giles. An alternative to this is a travelling ship loader usually running on rails at the berth that achieves similar outcomes e.g. Outer Harbour. However, in the case of a self-unloader a process called fleeting is required which entails either moving the bulk vessel or the self-unloader to enable the spout to access each hatch in the required sequence.

Most self-unloader operations in the world, for example CSL in Canada and Jebsens in Norway, involve moving bulk commodities from one shore-based loading facility to another shore-based customer [a flour mill or similar facility that is shore located]. In 1990 a 15,000 t CSL self-unloader was used to transfer grain from the Thevenard and Port Pirie grain ports to the Port Lincoln silos. It was operationally successful, achieving a discharge rate of 1,400 tph, but not economically viable.

Transferring bulk commodities in exposed waters is not an optimal scenario due to the impact and dangers of high seas. Most barge or self-unloading operations are in sheltered waters such as rivers. Good examples being the Mississippi barging to shore-based grain silos pre-export, the Cargill K2 mid-stream transfer operation at Baton Rouge also on the Mississippi, and the European barge network where many flour mills are located riverside given the historical reliance of water driven power.

Transferring grain from a shore-based facility by a self-unloader is a very slow process as it involves loading the self-unloader at berth, travel to the bulker, loading the bulker using fleeting [described above] and then travel back to the berth. This will result in a load rate less than half and as low as a quarter of the loading rate of the self-unloader. This will result in significant demurrage costs given the standing costs of a bulker. Alternatively, there will be a high charter party cost associated with lucky Bay by the ship owner.

Slow bulker loading will encourage use of smaller bulkers, handy [25,000/35,000 tonnes] or handymax [35,000/45,000] class as opposed to panamax class [60,000/65,000] with consequent higher per tonne shipping cost to the export markets.

Using barging or self-unloaders to transfer grain to a bulker at sea exposes the operation to rough water that will cause delays or cancellation of the process while the bulker is standing by to load.

Vessels can arrive for loading out of the planned sequence due to delays at the previous port of call, weather delays or mechanical failures. This requires adequate storage of more than one grain type/grade in a shippable position at Lucky Bay.

STORAGE AT THE BERTH

Bunker storage is a poor source for a ship loading operation for the following reasons;

- Bunkers cannot be operated in high wind or rain. A fatality was recorded in WA during high winds.
- Bunkers, as opposed to steel or concrete cells, do not provided segregation of grain quality and do not allow blending of quality to meet a sale specification. Both factors reduce optimisation of sales revenue.
- All grain exports are subject to Commonwealth [AQIS] testing. If insects are found in the loading process or the grain does not meet the contracted specification the loading stops and all the grain from that storage unit is rejected. In the case of a bunker this would usually be 20,000 or 30,000 tonnes, for a steel bin between 6,000 and 3,000 tonnes and for a concrete cell between 1,500 and 2,200 tonnes. This significantly increases the prospect of a shortage of the available correct grain at the port. Retreatment in a short time frame to suit shipping timeframes is only possible using

methyl bromide. This highly toxic gas requires very strict certification of sealed steel bins with gas recovery facilities.

- The reclaiming speed from a bunker is generally much slower than from bottom self-emptying steel or concrete storages. This can impact ship loading rates and slow the process while a bulker is standing ready for loading.

GRAIN MARKETING

The marketers of the grain normally charter the export vessel and determine the loading port as well as arrange for land transport from a country silo to the port. Some overseas customers prefer to use their own vessels or charter vessels themselves.

Grain growers are fully aware of the aggregate land based charges [not in all cases the detail make up of these costs] in the supply chain. However they will not be aware of the post FOB costs including despatch/demurrage, two port loading and sea freight that go to make up a net price for their grain. In the case of a slow loading port or a port that discourages the use of larger vessels these costs will be higher, in some cases considerably.

GENERAL

South Australia has the highest number of grain ports in Australia and consequently the lowest freight rates from farm or country silo to port of any state. Three of the seven, Outer Harbour, Port Giles and Port Lincoln being full panamax capable.

Australia has the highest number of grain port facilities per tonne produced of any major grain producing nation. Additional facilities will increase unit costs of current ports due to reduced throughput.

WHAT IS DRIVING THIS LUCKY BAY DEVELOPMENT?

The sale of ABB Grain [incorporating Ausbulk] to Viterra in 2005 and the subsequent sale of Viterra to Glencore approx. three years later has resulted in Viterra's grain handling charges [excluding third party charges incorporated in farmer deductions] being approx. double those of CBH WA which is still a cooperative in grower hands. Prior to the sale of ABB Grain to Viterra SA's grain handling charges were the lowest in the country, they are now by far the highest.

Viterra owns all seven of the State's grain ports, Thevenard, Port Lincoln, Port Pirie, Wallaroo, Port Giles, Pt Adelaide Inner Harbour and Port Adelaide Outer Harbour [Ardrossan is not used as a grain export facility and the fixed ship loader is owned by One Steel who load dolomite there] and all but a very few of the 110 country silos. **SA farmers are extremely frustrated with this situation given the current monopoly status of Viterra.**

THE CONSEQUENCES OF THIS PROPOSAL

As the current rail and road systems are focussed on Port Lincoln and to a lesser extent Thevenard;

- Decimation of the rail transport task with the almost certain closure of both the western and eastern sections and the final link to Port Lincoln.

- A significant redirection of grain transport paths towards Lucky Bay with an additional cost of hundreds of millions of dollars on road maintenance and construction to be borne by the State and local councils as well as major additional road maintenance costs and additional truck traffic through Port Lincoln township. Grain trucks are always fully loaded so cause maximum road damage.
- What will happen to the harvest overloading tolerance afforded to grain growers using their own trucks to cart to their 'local silo'?
- **No net incremental economic benefit to the state** as there will be no additional grain exported, simply a redirection.
- Likely underutilisation of existing high quality Viterra grain storages [as the purpose is to avoid their excessive charges] and consequent duplication via on farm storage [with its drawbacks] or other new storage sites.
- A major negative for tourism on Eyre Peninsula due to the increased truck activity.

THE QUESTIONS

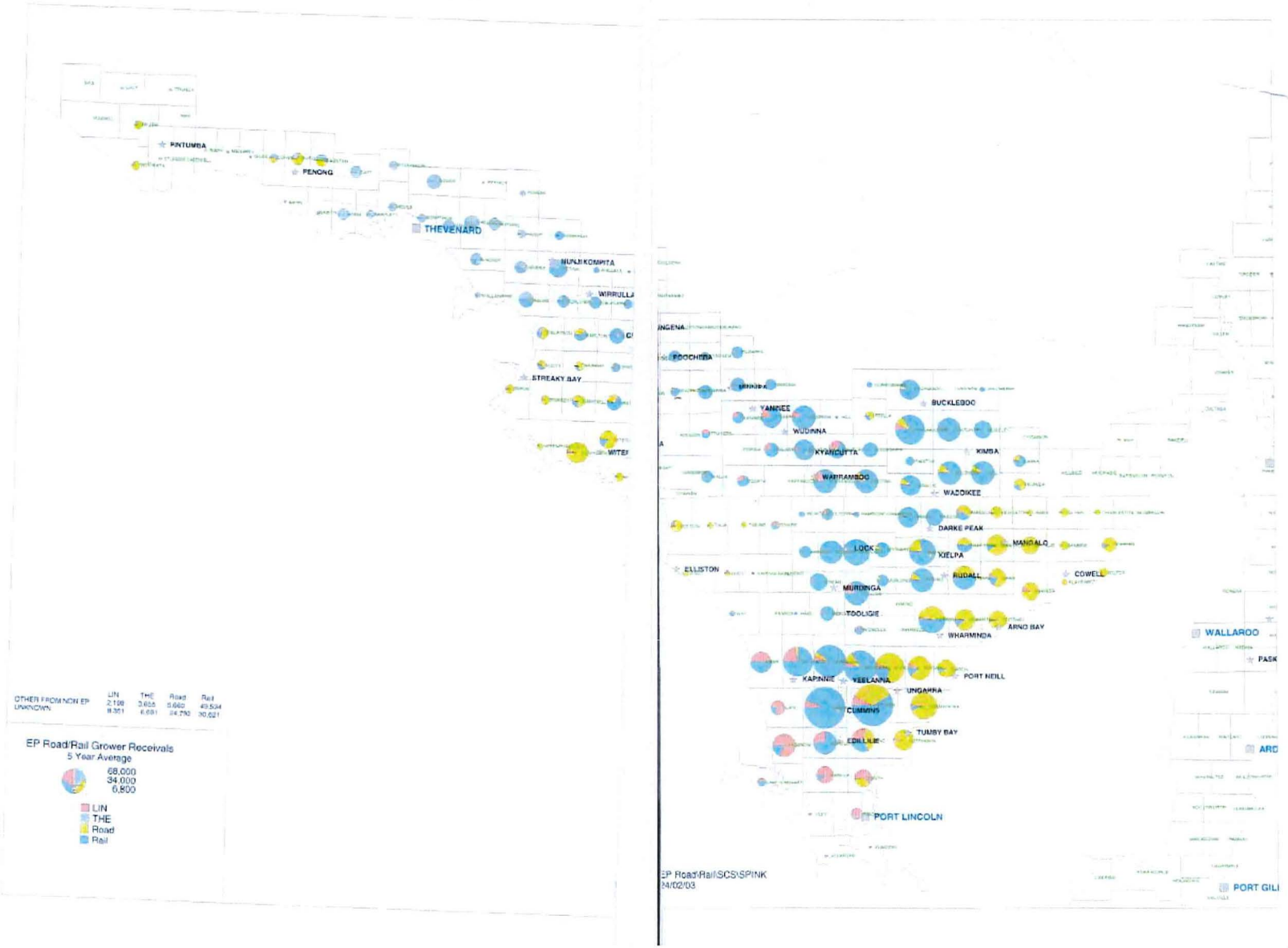
How is the State or Federal Government going to stop this fragmentation of the State's bulk grain supply chain? It is likely that other similar sub optimal grain infrastructure proposals could be developed entirely due to the opportunity provided by the excessive charges of Viterra's monopoly. With charges similar to the obvious benchmark of CBH WA there would be little or no opportunity for fragmentation of an efficient supply chain developed over many years.

Who is aking into account the consequences of additional cost to the state that will arise from this and future potential fragmentation of the supply chain?

Why should the general community have to pay for the extra road damage associated by this or other similar developments that significantly change the direction of grain flow?

John Hill

7 September 2018


PINTUMBA
PENONG
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WIRRULLA
STREAKY BAY
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WUDINNA
BUCKLEBOO
KYANCUTTA
KIMBA
WARRAMBOO
WADDIKEE
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MANGALO
KIELPA
ELLISTON
RUDALL
COWELL
MURDINGA
TOOLIGIE
ARNO BAY
WHARMINDA
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68,000
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Addendum

Philipson, Mike (ESCOSA)

From: John Hill [redacted]
Sent: Tuesday, 2 October 2018 10:36 AM
To: Philipson, Mike (ESCOSA)
Subject: ESCOSA inquiry SA grain supply chain

Mr Mike Philipson
ESCOSA

Dear Mike

Following receipt of a letter dated 24 September from Adam Wilson and our earlier discussions I am summarising a few earlier comments in relation to the basis for comparison of charges for grain handling services.

In the draft ESCOSA report there is reference to comparison with Graincorp charges with Viterra charges instead of a comparison with CBHWA charges. I consider this to be an inappropriate comparison based on the following.

Graincorp, the corporatized and merged entities of Vicgrain, Bulk Grains Queensland and The NSW Grain Authority, cover the three most highly populated states in Australia with a significant domestic market involving regular servicing of small volume transactions when compared with export operations. NSW and Queensland also have domestic summer crops focussed on domestic markets. The larger domestic market encouraged fragmentation of storage including on farm storage. All three merged entities commenced as government organisations in the 1930's with relatively small silos close together reflecting the crop sizes and truck capabilities of those times resulting in inherent inefficiencies.

CBHWA and SACBH both commenced in the 1950's as grower owned entities. Both states are heavily focussed on large scale export operations and have very small domestic markets and only winter crops, predominantly wheat and barley but also some canola and pulses. Both have larger silos spaced further apart than those in the eastern states due to progressive advances in truck capabilities. CBHWA has a major export facility at Kwinana which is both rail and road served, a terminal at Gladstone which is also rail and road served and terminals at Esperance and Albany which are road served. All these terminals have significant concrete cell storage. I am very familiar with the CBHWA operations having visited on many occasions. In 2000 I reorganised all their road freight contracts [while employed by AWB and in conjunction with the WA Grain Pool] and I advised the treasurer of the Gladstone Port Authority on cost justification of dredging from a grain industry perspective having provided similar information for the SA Deep Sea Port Committee.

SA has a major export facility at Port Adelaide and significant exports from Port Lincoln, Port Giles and Wallaroo. There are minimal or nil exports from the Thevenard and Port Pirie and Ardrossan is not used for grain exports. There are similar mixes of transport modes to port as in WA.

Based on the above it should be evident that the CBHWA operations bear an extremely close resemblance to those of Viterra. Consequently I consider this is the only valid basis for comparison of Viterra handling charges in such a monopoly environment.

I would be more than happy to discuss this or any of my other submissions with ESCOSA.

Regards

John Hill
[redacted]