

Strategic Analysis Paper

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Unlocking Our Potential – The Need for Foreign Investment in Australian Agriculture

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Key Points

- Available statistics and recent reports suggest Australian agriculture is experiencing an increase in foreign investment.
- Foreign investors, in particular State-owned enterprises (SOEs), are looking to Australia for long-term, low risk agricultural assets and as a channel to supply their growing populations with high quality produce.
- Such investment is essential for Australian agriculture in the absence of domestic capital sources and government support.
- Foreign capital brings improved access to overseas markets, needed to meet export growth targets, and can build Australia's food processing capabilities to ensure domestic food security.
- Government policy should focus on balancing the sector's need for substantial foreign investment while improving the transparency of foreign involvement in key industries.

Summary

Foreign investment has reemerged as a prominent issue in Australian agriculture. In line with rising global investment trends, SOEs and foreign multinationals have shown greater interest in Australian agricultural assets. This has led to calls for improved transparency and possible restriction of foreign capital. The greater agricultural

community and economists alike, however, champion this influx as an essential tool for the sector's development in the absence of domestic capital.

Foreign investment - in its many forms -will shape the future sustainability of the sector, which is dealing with issues of high debt and high labour costs. Australian agriculture requires long-term strategies to address these issues, while contending with current sector challenges of high labour rates and under-developed processing facilities. By providing long-term, well-funded and environmentally sustainable investments, foreign agribusinesses and SOEs can be hugely beneficial to the sector.

The presence and operation of such agribusinesses must be monitored, however, in consideration of maintaining domestic food security. The role of Australia's Foreign Investment Review Board (FIRB) in this cannot be understated; it plays a significant role in ensuring investments are made according to the national interest. Clear government policy measures must be taken to alleviate public concerns of foreign investment, while delivering more avenues for the production of healthy, ready-to-consume food products for Australians.

Analysis

After decades of under-investment, the 2008/09 food price crisis created an increase in foreign investment in global agriculture. Rapid food price inflation and minimal food reserves prompted countries to invest in agricultural resources in other countries, where land and natural resources are more abundant. Nations with insufficient production to sustain demand are now investing in overseas assets to lessen their reliance on the global food market.

The majority of rising investment flows have occurred in upper-middle and high-income countries. Rising incomes in developing nations are driving demand for an increasingly homogenised range of food products - particularly dairy, beef and wheat. Australia retains competitive advantage in many of these goods. The emergence of non-traditional investors from South-East Asia and the Middle-East in Australia is a significant factor spurring foreign investment in domestic agricultural assets and businesses.

Definition and Extent of Foreign Investment

Foreign investment refers to an investment made by a company or entity in one country, into a company or entity based in another.

Foreign investment in agriculture can take several forms. These include: purchasing portfolio investments, or shares, of an existing domestic company, generally without the intention of influencing management; foreign direct investment, made

with the objective of establishing a lasting interest or long-term relationship between the investor and the enterprise; and re-investment.

Agricultural investments include portions of or entire agri-businesses - including processing facilities, transport and other infrastructural assets - and agricultural land.

Foreign-owned Agribusinesses

On the surface, the level of foreign involvement in the sector appears low. The recent [2013 Agricultural Land and Water Ownership Survey](#) (ALWOS) by the Australian Bureau of Statistics (ABS) suggests 99 per cent of agribusinesses in the nation remain Australian owned. Figures of the proportion of foreign-owned businesses in the Australian economy show similarly low figures - at only 2 per cent.

But this does not indicate the true level foreign influence in the sector. [ABS data from 2013 indicates](#) that among large businesses in the Australian economy employing over 200 people, 27 per cent are partly or wholly foreign owned. Despite inadequate data, agriculture likely shows similar trends (albeit with comparatively smaller workforces) due to the general preference of foreign investors for large-scale operations in the sector.

Foreign-owned agricultural land

The Foreign Investment Review Board (FIRB) [defines](#) agricultural land as land used wholly and exclusively for carrying on a business of primary production. The ALWOS survey suggests 89 per cent of agricultural land is wholly Australian owned, while a further five per cent of is majority owned by Australian interests. Since the last ALWOS survey in 2010, figures show an increase in foreign land ownership of 11 per cent.

The new survey provides little insight into the categorical trends of foreign investment in particular industries. Furthermore, these statistics do not represent the true figures of foreign influence as they fail to show the presence of 'backdoor' stock investments from external super funds and insurance companies into the sector.

Why is foreign investment increasing?

The new wave of foreign investment into Australian agriculture raises a fundamental question: why can't Australia fund the sector itself?

Investment culture

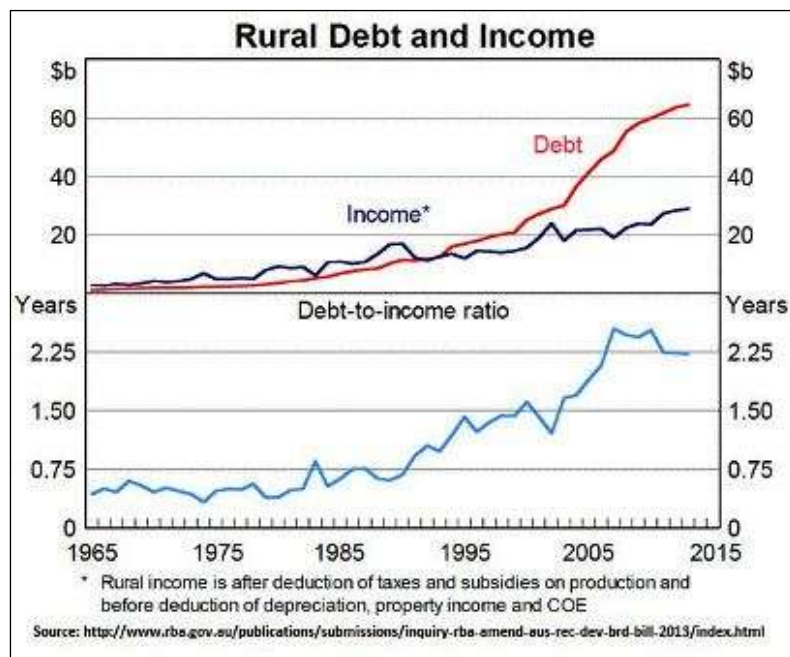
One reason for this is the lack of involvement of Australian capital funds in the agricultural sector.

Australia’s investment culture is geared towards short investment cycles and quick returns. Australian superfund managers, who control the nation’s \$1.84 trillion dollar super pool, typically look for benchmark annual returns of investment to cover the costs of equity¹ for their shareholders. Assets that are liquid² are valued higher than ‘alternative’ assets such as agricultural agribusinesses, land, infrastructure and soft commodities (i.e. raw agricultural product).

Typically, agricultural investments do not fit the short-term benchmark return requirements of fund managers. This is due to climactic risks, volatile food commodity prices and declining terms of trade³ across the sector.

Increasing Rural debt

Poor drought conditions and strict financing requirements following the Global Financial Crisis in 2008 have created rising debt in the sector. Rural debt levels have doubled over the past decade - reaching



\$64.5 billion in June 2013. Furthermore, restrictive loan conditions since 2008 have limited domestic capital flows into the sector. Many commercial lenders operating within the ‘quick return’ business environment fail to offer loan products suitable for the agricultural sector, charging increasingly high premiums. Declining land values in many areas due to variable production levels compound these issues.

¹ ‘Cost of equity’ refers to the return that stockholders require from a company to compensate for the risk they undertake by investing their capital.

² ‘Liquid’ refers to shares in a corporate stock that can be purchased and sold off for a cash value

³ Declining ‘terms of trade’ refer to the decline of export prices relative to imports. Australia’s high exports, relative to production, increase the vulnerability of domestic producers to global commodity prices and market conditions.

Many Australian family farmers are struggling to compete without domestic finance options. Minimal options mean that despite the availability of new efficient technologies for their businesses, these farms often lack the capital to purchase them. Thus, in the absence of domestic capital support, many Australian farmers are increasingly vulnerable to losing ground on larger-scale and more efficient competitors.

Low Government Support

Government support for the agricultural sector has waned since Australia reached food surplus in the 1980s. This includes the [declining intensity of public funding into research and development](#) and the lack of production subsidies.

Many developed countries receive far higher rates of government support into agriculture. A 2013 Organisation for Economic Co-operation and Development (OECD) [report](#) showed that in response to rising demand and higher commodity prices, OECD countries have generally increased support to national agriculture schemes. The OECD average in public support rose from 2011-2012 from 15 to 17 per cent (as a percentage gross farm receipts), while Australian government support is less than three per cent and declining. This ranked Australia 18th out of 20 OECD nations (including the EU 27).

Although the lack of support reduces the financial pressure on the Australian budget, it means that local farmers experience a disparity of capital support compared to competitors. This means Australian farmers must ensure they are at the forefront of production efficiencies to compete in the global market.

Low Domestic Demand

Typically, those looking to sell large Australian farms are dependent on foreign buyers due to low domestic demand. Australian farms that have built up economies of scale often only receive interest from foreign-based investors, who prefer larger assets.

This represents a prevailing trend in developed agricultural systems: production is becoming increasingly centralised. Increasing corporate takeovers of domestic agribusinesses create difficult conditions for the remaining smaller producers, who lack the resources that larger organisations possess.

The independence of the Australian agriculture sector means that sub-optimal farms, which have failed to build adequate efficiencies and scale, or do not supply luxury goods to niche markets, are at risk of default.

Foreign Interest

Foreign interests have long been attracted to Australia's stable investment climate and the safety of high quality Australian food products. Australia's arable land availability is far above comparable high income countries (at over 2 hectares of arable land per capita), thus Australia presents as a suitable investment option for many foreign investors.

Post-GFC, Australian agricultural assets and agribusinesses are particularly valued in their tangibility, as opposed to abstract financial derivatives. These alternative assets appeal as long-term and low-risk investments.

SOEs are not only attracted to these assets as financial opportunities, but also as a means to secure their food supply. These nations, often with weak private sectors, turn to state-run business apparatuses as a means of showing integrity in business operations. South-East Asian and Middle Eastern nations - such as Indonesia, China and GCC states – now seek to secure their food supply through a diversity of international channels in response to increasing domestic populations and changing consumption patterns.

As the global population continues to increase, there will be more state-owned entities showing interest in Australian assets. Foreign agribusinesses are attracted to Australia's proximity to developing markets in Asia, particularly in Northern Australia. These agribusinesses can offer Australian farmers access to pre-existing supply chains; presenting significant opportunities to farmers for business growth.

Foreign Investment – An Industry Snapshot

A range of Australian agricultural industries have been targeted by foreign investors: namely cattle, sheep, dairy and grain.

Cattle

New players from Indonesia and China have emerged in the Australian cattle market. Two Indonesian companies, The Great Giant Livestock Company and SOE Santori, for example, have made large purchases of cattle properties in Northern Australia in late 2013 - the latter purchase totalling 1.3 million hectares.

Meat processing facilities, too, have attracted interest from international firms. Chinese Investment fund New Hope recently bought majority stake in Kilcoy abattoir – the first Chinese investment in the industry since 1992. Other processors include Nippon foods and the largest meat producer in the world - Brazilian

company JBS, who holds a large contract with retail giant Woolworths. Foreign companies now process over 40 per cent of Australia's red meat product.

Sheep

Significant foreign investments of late have been made in Australia's sheep industry. The [\\$1 billion deal](#) between Bunbury-based Meat processor V&V Walsh with Chinese company Heilongjiang Grand Farm Group and an inner Mongolian government has created a huge overseas market for V&V Walsh sheep and cattle. The \$200 million investment into the company is expected to boost the family business' operations by 500,000 lamb and 30,000 cattle per year.

Qatari SOE Hassad Foods continues to expand its sheep producing operations in Australia since its establishment in 2009. The company now exports 110,000 sheep a year from its operations across Victoria, Queensland, New South Wales, South Australia and Western Australia.

Grain

Foreign players have played an increasing role in the Australian grain industry since the deregulation of grain marketing and export arrangements in 2008. Figures from 2009-2010 show American firm Cargill and Swiss firm Glencore controlled 18 and 16 per cent of grain handling in Australia respectively. As of 2011, 50 per cent of the licenced wheat exporters in Australia were foreign owned.

Hassad Australia is also a large player in Australia's grain production industry. In 2009, Hassad invested \$500 million into Australian grain assets. More recently, significant land purchases of over 14,000 ha have been made across South Australia worth over \$73 million. The company's portfolio now includes over 14 major wheat and sheep farms across Australia.

Japanese companies, too, are making new investments in Australian grain. For example, Sumitomo recently bought a majority share in Emerald Grain - Australia's fifth largest grain accumulation company. Mitsui Group is also looking to consolidate its position, aiming to build upon its 25 per cent stake in WA grain trader Plum Grove bought in December 2012. The mega-merchant's chairman - Yashushi Takahashi - [said in April](#) that the company aims to secure at least ten per cent of Australia's grain handling industry to supply the Japanese market and other markets in China and South-East Asia.

Dairy

The deregulation of the Australian dairy sector from 2000 has led to an influx of foreign capital into the industry. According [to 2011 ABARES estimates](#), about 50 per cent of the milk processed in Australia is now processed by foreign-owned firms.

A number of investors from Canada (Saputo), the U.S (Chobani), New Zealand (Fonterra), the Philippines (Monde Nissin), and France (Permalat and Lactalis) have acquired Australian dairy companies, particularly across Victoria and Tasmania. Most notable is the increasing demand from Asian investors, namely China and Japan, for high-value, milk powder producers.

Benefits of Foreign Investment

The domestic agricultural sector must improve its competitiveness to maintain food security and grow its net export surplus. [ANZ Bank estimates](#) \$600 billion in additional capital is needed between now and 2050 to generate growth and profitability. Low domestic investment means that foreign investors could be the most significant source of these funds to 2050.

Australian agriculture faces significant constraints and requires foreign capital to sustain and develop the sector. Inadequate capital and limited market access highlights this need. Benefits include job creation, contribution to the Gross Domestic Product, food exports, taxation, new technologies and improved management systems. The following examples demonstrate how foreign investment can transform the sector:

Land Leasing Arrangements

Farmers are increasingly selling off debt-loading assets, including land, to foreign interests. Foreign investment funds, often in conjunction with specialist asset managers such as U.S firm Westchester, typically look to buy land and lease properties back to local farmers or experienced farming management companies. In these cases, farmers only pay rent to the new owners, ridding themselves of costly interest repayments. This saving is significant; many Australian farmers under financial stress allocate 30 per cent of total revenue to interest.

This grants farmers improved profit margins to invest into, for example: livestock, experimental crop varieties, other technologies and infrastructure.

Foreign capital can be a saving grace for many struggling farmers. The flow-on benefits from such capital includes improvements in skilled labour, infrastructure, technological advantages, and new experimental crop varieties. This can help domestic operations remain internationally competitive.

The emergence of land leasing arrangements and building of dynamic, profitable modern farm enterprises could attract Australians back to struggling regional towns. The exodus of younger rural generations into urban centres and other sectors has long threatened the survival of Australian agriculture. The average age of a farmer is now 52 – 12 years above the national average for other occupations. This trend will

increase labour shortages in the sector dramatically in the near future. An influx of foreign capital is needed to build a more dynamic agricultural sector, helping to retain younger generations in evolving family businesses and sustaining regional economies.

Enhanced market access

Foreign agribusinesses can also assist in developing export markets for Australian farmers. Their influence in the global supply chain presents opportunities previously unavailable due to the small size of the domestic market. Investment into processing and transport infrastructure not only adds value for Australian agricultural products, but allows production bases, previously isolated, to access ports for export. This is a primary reason why the Aboriginal Pastoral Co-operative is seeking a \$40 million take-over arrangement with Chinese company ASF; the co-operative is not in debt, rather they want to improve their access to the Chinese market.

Risks of Increased Foreign Influence

Many of the concerns over foreign interests as an emerging threat in Australian agriculture are misguided and exaggerated. Foreign involvement in Australian Agriculture has historic foundations, most notably through the influence of U.S and the UK interests in the cattle and sheep stations of northern Australia. Foreign investments largely mirror Australia's largest export markets of the time.

Multinational companies can consolidate their position in the sector by vertically integrating through production, processing and distribution chains. These investments in distribution can improve supplier access to consumer markets. Such consolidation can also result in the emergence of 'choke points', however, as seen in the [dominance of the Woolworths and Coles retailer duopoly](#), inducing price pressures on Australian farmers, many of whom are already struggling with marginal returns.

There is also concern over the possibility of foreign multinationals diverting revenue streams to escape Australian tax levies. Policy measures must work to strengthen the Australian tax system and keep foreign companies accountable.

Despite these risks, the Australian food system lacks alternative options. Australia's processing capabilities are poor and must be improved to ensure the domestic availability of healthy, ready-to-consume products.

Australia's reliance on the production of bulk, raw commodities poses a risk to domestic food security. This was highlighted in 2010, when a [survey from the Australian Food and Grocery Council](#) revealed Australia became a net importer of fresh and processed food, beverages and groceries. Rising imports from countries

such as China and India, who maintain self-sufficiency policies, mean that efforts should be focused on securing the domestic food supply to prevent future occurrences of net importer status. Thus, while foreign investment must be encouraged, this should be balanced by a long term-food security strategy aimed at ensuring the domestic supply of healthy food stocks.

Government Policy

Australia's foreign investment policy is administered by the FIRB within the framework of the *Foreign Acquisitions and Takeovers Act 1975*.

The current FIRB threshold for review is over \$248 million for agribusiness and land and \$1 for SOE purchases. In recent FTA and EPA agreements reached with South Korea and Japan, however, the Coalition government indicated it will lower agricultural FIRB thresholds. This is due to agriculture's newly prescribed status as a 'sensitive sector'. Under the new guidelines, all foreign agricultural investment over thresholds of \$53 million for agribusinesses and \$15 million for land will be scrutinised.

The government applies a rigorous national interest test as per FIRB screening requirements. The following conditions are considered during reviews:

- The nature of land access and use;
- Agricultural production and productivity;
- Australia's capacity to remain a reliable supplier of agricultural production, both to the Australian community and our trading partners;
- Biodiversity; and
- Provision of employment and prosperity in Australia's local and regional communities

Policy Outlook

The media's coverage of new actors in the Australian food system has led to public concern over foreign involvement. A [2014 Lowy Annual Poll](#) revealed 60 per cent of Australians oppose foreign investment in agriculture. The opaque nature of foreign involvement accentuates this view. Thus, despite widespread support for foreign investment within the sector, public suspicion negates positive policy outcomes.

Australian Agriculture Minister Barnaby Joyce has stated that the government's policy promise of a foreign-owned farmland register is progressing. This process must be accelerated, however, to quickly alleviate voter concerns. The register would also work to track the foreign involvement of key agricultural industries. This would solidify national interest screening, ensuring that foreign investment works to

benefit domestic food security outcomes (particularly in strengthening processing capabilities) while maximising opportunities for productivity and export growth.

Meanwhile, agricultural economists and domestic investors have [spoken out against](#) the new barriers on foreign investment, suggesting the sector needs fewer restrictions on investment, not more.

There is inadequate evidence, however, that strict foreign investment screening discourages investors. This is highlighted in New Zealand where farmland is categorised as 'sensitive', requiring any purchase of five hectares or more to be scrutinised by New Zealand's Overseas Investment Office. This strict review process did not prevent the country from reaching a Free Trade Agreement with China in 2008, nor did it prevent foreign investors spurring the huge growth of New Zealand's dairy industry.

The Australian government has failed to communicate a clear policy position on much needed foreign investment, while food security planning – such as support building self-sufficiency in processing industries - appears non-existent. The ongoing negotiations and possible Free Trade Agreement with China may yield looser restrictions on foreign investment which could force an overarching policy change to prevent aversion to the 'special treatment' of China by other state-owned and foreign investors.

The Coalition government is unlikely to 'open the floodgates' for foreign investment, in part due to the National Party's protective stance on the issue. Furthermore, public surveys indicate split decision over the prospect. To backflip on policy promises of lowering FIRB thresholds, and signal further easing of restrictions, would thus put the Coalition at risk of losing votes in the next federal election. Policy priorities must change to address the significant issues halting greater growth of agriculture in Australia.

Conclusion

Foreign investment is essential for Australia's agricultural sector and should be encouraged. Constraints in the sector such as high debt, minimal domestic capital and limited access to global markets can be addressed by long-term and well-funded investments.

If foreign investors satisfy this need, abide by Australian regulations and do not encroach on domestic food security or export goals, their capital should be welcomed into the sector. Such investment is essential in building an advanced and profitable sector, which will improve the viability of domestic investment for the future and secure ready-to-consume-food for the domestic market.

Improved transparency and approval processes for incoming foreign investment would simultaneously sustain growth in the sector and alleviate public confusion over the current government's policy position. Such measures should be taken to signal that Australia is open for business yet committed to improving Australia's domestic food security.

Any opinions or views expressed in this paper are those of the individual author, unless stated to be those of Future Directions International.

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