Water trading is the buying and selling of tradeable water rights, allowing water to be redistributed amongst users. Previously, ownership of water required the ownership of the land. Now, in many instances, water can be traded independently of land. There are two types of trading. Permanent (or entitlement) trading is where the ownership passes permanently to the buyer. Temporary (or allocation) trading is where water is leased to the buyer, usually just for one irrigation season. Temporary trading is higher in volume and lower in price than permanent trading.

A trade is where a water entitlement, or part of it, is traded to another person or entity and the water will be taken from another location. For example, a licensee sells their water entitlement to another person who may take the water from another location and potentially use it for a different purpose.

Trades typically occur in fully allocated water resource areas. Trades can only take place within the same water resource area (i.e. same groundwater subarea and aquifer, or same surface water area especially along rivers).

Farmers with permanent plantings such as fruit trees or grape vines buy permanent water so that they have certainty of water supply each year. Farmers who grow annual crops, such as rice, use temporary trading to buy only as much water as they need for each season.

These farmers manage their water risk using temporary water trading. It is argued that water trading can promote more efficient allocation and use of water because a market-based price allows water to move to its highest valued use.

In 2010, the water rights market was valued at $2.8 billion. Various kinds of market intermediaries assist with the trade of water, including water brokers, water exchanges and message boards. A trade may occur between a private buyer and seller, through a broker or through an exchange.

A Western Australian example of water trading

Harvey Water is a fully private irrigation water supply cooperative which has been operating in the Waroona, Harvey and Collie River Irrigation Districts in WA since privatisation in 1996.

Harvey Water is a customer service business, delivering water to cooperative members, small private irrigators and industrial users.

The Harvey Water Irrigation Area (HWIA) is located to the west of the Darling Scarp on the Swan Coastal Plain, around 100 km south of Perth. It covers an area of 112,000 hectares (around 75 km long and 15 km wide) in three irrigation districts Harvey, Waroona and Collie River.

There is currently around 10,000 ha of land under permanent irrigation for dairy farming, beef grazing and horticulture, with a total irrigable area of approximately 30,000 ha.

The HWIA is different from most Australian irrigation areas because it does not have a longitudinal river system from which water is diverted or pumped. Water has historically been supplied by gravity flow from dam to farm along a network of open concrete lined and earthen channels.

Water is sourced from seven dams along the Darling Scarp from Waroona in the north to Wellington Dam near Collie in the south.

The water supplied for irrigation is non-potable, or not suitable for household drinking and consumption. It is however, ideal for providing prime dairy and beef cattle grazing pastures, horticultural irrigation and water for industrial use. The regional economic benefits are enormous, with an estimated $100 million in gross value-added production from agriculture/horticulture from the water supplied.

The open concrete and earth channels which formed the water distribution system from the dams lost approximately 30% of the water released before it reached the farms, mainly through seepage. Harvey Water spent just under $100 million replacing the open channels with 490 km of High Density Polyethylene (HDPE) pipe. This saw losses reduced to 5% or less. The project delivered over 17 gigalitres of water savings. This allowed Harvey Water to trade water from Stirling Dam and Samson Dam (both potable supplies), which they no longer required, to Water Corporation.

As these dams are connected to the Integrated Water Supply System (IWSS), the water traded was used to supply the daily water needs of over 100,000 Water Corporation customers. The IWSS is the system that delivers 291 billion litres of water each year to over 2 million people in Perth, the Goldfields and Agricultural region and some parts of the South West. This is an excellent example of water trading where water is traded to a higher value purpose (i.e. from irrigation water to drinking quality water).