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Date: 23-11-01

Citrus Industry Inquiry – Initial Submissions

Dear Sirs,

Interaust Foods Pty Ltd., as a major Importer of Brazilian FCOJ, herewith makes the accompanying Initial Submission to your Citrus Industry Inquiry in the interest of major importers of Frozen Concentrated Orange Juice, as interested parties, in an attempt to assist the Inquiry in putting the Australian and World Citrus Growing and Processing Industries into their true and relative perspectives. In particular, we wish to help explain the World FCOJ Market.

In addition to comment on the Australian Market situation, we have included a significant number of Independent Reports.

Given that the lobbying, drive and motivation resulting in this Inquiry has obviously come from one particular side of the argument, we are anxious that the Commission is briefed more objectively in some detail on the World Market before reaching the Position Paper.

We were somewhat alarmed to find that in a six month Inquiry period, such a short time only was allowed for Initial Submissions. Thankfully there has been a short extension.

In the period since the Inquiry was announced, various Juice Industry participants have been engaged in such things as the World Juice 2001 Conference in Amsterdam, October 9-11, followed by Anuga World Trade Fair in Cologne, October 13-17, and more relevant, preparation for IFU Sydney Conference, November 13-17. IFU is the International Juice Producers Union and their World Conference is combined this year with the Australian & New Zealand Juice Associations.

All of this inhibits making effective, thorough Initial Submissions against such a short timetable. It also appears that the Commission did not see fit to include any of the major importers in the Visits Program and we have encountered many Juice Bottlers similarly frustrated that they also did not have the opportunity to be included/canvassed.

Yours Sincerely,

Geoff McCormack
Interaust Foods

First, may we address how and why the Inquiry came about?
To begin with, the 2000 Australian Navel Orange season, after several good years including successful export marketing of fresh Navels to the USA at very good returns (a commendable marketing effort) thus having reduced their dependence on processing to low levels (less than 20% of crop the previous two years), the growers encountered a crop with serious quality problems in 2000. Much of it poor quality and especially small sized fruit unsuitable for Fresh Exports, especially to the USA market. The growers then turned to the Processors to regain share of the Cordial/Soft Drink Industries whose applications can utilize Navel Orange Juice. Unfortunately these Industries, having had to make alternative supply arrangements in recent years, were already contractually covered for juice raw material (from mid 2000) through to the end of summer, March 2001. To take the uncontracted, unplanned and unwanted fruit, Processors could offer only very low prices to justify processing the fruit and financially having to carry the inventory for 9-12 months. The Citrus Growers were frustrated and angry and began media campaigns but the Processors and Bottlers (and Importers) could scarcely be blamed for commercially going about their businesses. In the end, much of it got processed at good prices, exploiting Processors contracts for "all available juice fruit" predicated on the expectation of only modest quantities being available. This was largely for debittering some Navel juice for "NFC" (not from concentrate/single strength/fresh juice). These contracts were at healthy Valencia Orange prices.

This situation with Navels may well happen again in seasonal fluctuations every 3, 4 or 5 years however this year's Navel Crop (2001) was back to normal/slightly light and another good year for Fresh Exports to the USA. Obviously for these growers the prospect of the occasional bad year in their business is unacceptable and they would prefer in such circumstances that the community bails them out when it occurs. One might ask, where is the money from the good years to average them through? Surely it is unfair to expect other Industries like Juice Processing and Beverage Manufacturing, however related, to remedy this type of problem to their own financial detriment.

And then, the Australian Valencia Orange Crop of 2000/2001.
Given that the "NFC" Market allegedly accounts for something approaching 30-35% of Orange Juice consumption in Australia, there is therefore a requirement of around 160,000-170,000 tonnes of Valencia Oranges to cover this. In a "normal/average" Valencia crop the growers seek to place, say, 200,000 tonnes +/- to processing which is pretty much in balance with current NFC requirements and anticipated continued growth. To maintain truth in labeling integrity, all the Juice Bottlers also include Australian FCOJ content in their Orange Juices ("a blend of Imported and Australian"), the % of which would vary based on price/quality characteristics. In addition, on the back of the "Dick Smith Nationalist" style of marketing Australian only products, there are now quite a number of Juice Companies with an all Australian content niche brand in long life juice ranges, requiring Australian FCOJ.
So, Australian Orange Juice supply is now relatively tight in a "normal season". In fact, the 2001/2002 Valencia crop is lighter than usual and there is probably barely enough to cover NFC requirements for the next year.
The continuing development of the NFC product category, predominantly fresh orange juice, is "Import proof", (e.g., World NFC prices are currently more than double the Australian price due cost of seafreight and exchange rate), and surely is the future of Australian Citrus Juice and where the growers should be working WITH the Juice Bottlers/Converters to develop it together rather than behaving as adversaries, trying to impose their juice in concentrate form at higher prices in the long life juice market category.

In the USA, for example, NFC from Florida Oranges has reached a market share of 45% from almost nothing over 10 years ago and imports of Brazilian FCOJ have slowed/reduced. You will see from one of our accompanying reports that, in a market known as the largest in the world for media advertising spending, that despite all the money spent on branded juice by the likes of Tropicana (Pepsi), Minute Maid (Coke), Ocean Spray, etc. that the media spend on generic USA Orange Juice promotion by the Florida Citrus Bodies in 1997 was fully 1/3 as much as spent by all the brands combined. It appears that the results speak for themselves.

We think it is called SELF HELP.
Nowadays, the Florida Growers pay US$0.17 per box for advertising alone which gives the Florida Department of Citrus (FDC) a budget of US$60m for advertising and promotion.

For Australian NFC Contracts, we understand that the Growers receive around $150/160 tonne which is not too bad a return for juice fruit, no matter how exaggerated claims have been made as to the cost of production over the past two years. These claims, from one or two grower industry representatives in particular, have jumped around, mainly up, over the past couple of years as $130/140/150/160/200 tonne. One year they agree to contract $140-150 tonne and a year later claim cost of production $200! If $200 as cost of production were true then they should all give up and bulldoze the trees. We've seen staged destruction of trees for TV cameras along with quotes of "cannot grow oranges for these juice prices" when the reality is that few growers actually technically sell any fruit to juice companies, with the exception in the M.I.A. Citrus area of NSW, one of the three major areas, where there are significant direct contracts between Growers and Processors. They generally sell it all to Citrus Packing Companies (the largest of whom are usually larger corporate growers), it is the packers who, having sorted and graded the fruit and then marketed it for fresh domestic and fresh export (usually the best fruit), then sell the remainder to juice. What the grower actually gets is the average of all the markets on the %'s his fruit quality was graded at and the lowest of the three is usually juice fruit. Of course, a low juice price brings that averaged return down but it is a distortion to quote it in isolation when discussing the return/cost of production.

But now, back to the Valencia Crop, 2000/2001.
It turned out to be an "on year" or exceptionally large crop by Australian Standards meaning that the growers would have more like 260/270,000 tonnes of fruit looking to put to processing. (261 MT actually got processed) This would mean some 70-90,000 tonnes of it was "uncontracted fruit" not already destined for NFC. This fruit, if processed, would have to go to concentrate (FCOJ), not NFC. It would therefore compete with Imported FCOJ at ruling market prices. The Australian Valencia season starts in October each year through to March or even a little later. The juice converters/bottlers would have already contracted much earlier for their juice raw material requirements for the Australian summer of '00/01'. Unfortunately for the Australian Growers, there had just been a collapse in the World price of FCOJ in Sept/October '00 when, due to a combination of high inventories and competitive pressures, a short price war broke out amongst the Brazilian FCOJ suppliers. Buyers the world over had naturally capitalized on this, having little choice to do so as, if they did not, their competitor doubtless would, thus having a competitive advantage. The net result in the case of Australia was that the market, already covered until March '01 or more, for those able to utilize some of the Navel surplus of '00, proceeded to buy forward a further 9-12 months. This left the Australian Valencia surplus/bumper crop up against an almost fully covered market. Thankfully for many growers, the market leader in NFC devised a joint promotional plan to "mop up" much of this fruit but nonetheless much of it got processed at low prices and quite an amount remained on trees and perished.

An Australian large crop like this (20% above average) may only happen every 3,4 or 5 years and invariably the crop following is a short one. Financing such inventories of juice for later use is beyond the means of both growers and juice bottlers and that may well be one area where Government assistance can help in the future, if and when similar circumstances arise.

A Brazilian FCOJ Price War is in no-one's best interests least of all the Brazilians but world supply and demand can fluctuate wildly with climate and when market forces are brought to bear. It is very unlikely such things could occur as frequently as the Australian large crops and the chances of such an unhappy coincidence again would be at astronomical odds. It might happen once or twice per decade and usually results in a rationalization of the number of Brazilian processing plants.
In this instance, the timing was very unfortunate from the Australian Growers point of view but an extraordinarily rare coincidence, nonetheless. Surely not a justification for what is being proposed by the growers in this case.

To establish some form of "Safeguards" i.e. break glass and use temporary assistance by imposition of presumably anything from temporary Tariffs, Quotas, etc. for any such future grower circumstances is incomprehensible. It presumes that somehow, in effect the Australian Juice Industry virtually cancels, suspends, interrupts an/or defers pre-existing legally binding commercial supply contracts for juice raw material requirements in favour of expeditiously utilizing the unexpected local availability of lower quality (brix/acid ratio) Orange Juice, presumably at a price level determined by the Australian Citrus Growers, irrespective of the price of the pre-existing Brazilian contracts it displaces. Free trade?

These Australian Juice Companies are usually contracted forward based on minimum 6 month periods or to the end of fiscal years, bridging to crop seasons, etc… depending on market prices. Naturally the cheaper the raw material market price, the further forward a manufacturer would contract. The higher the price the shorter the raw material contract, etc.
The net effect on these businesses of arbitrary imposition of higher input costs is of course to damage their profitability in an industry sector where already profits are marginal and many of them are vulnerable to acquisition or worse. They are innocently going about their difficult business and their owners/shareholders and employees do not deserve to have such penalties arbitrarily imposed. These juice manufacturers are invariably locked into supermarket pricing for anywhere from 6-12 months at a time and have no ability to simply pass on such imposts.
This is NOT an industry where you want to be making it even more difficult.

When you examine much of the press cuttings (several are included in this submission), from the Citrus Growers campaign, it is obviously an organized PR exercise. Many of the statements and allegations were disturbing.
Apart from the more emotive accusations about the evil and unfair foreign imports and attempts to virtually demonise the Brazilian Industry, the more worrying calls are for this "seasonal protection". Calling for "either Tariff or Quotas limiting the quantity of Concentrate at specific times".
One particular article (attached) says it all. "Surviving the big squeeze". It ran in the Melbourne Sun on January 21st '01 quoting a prominent industry "leader". It is absolutely littered with falsehoods, distortions and completely unproven and unsupportable statements and allegations. It would be the lowest point to which the campaign had sunk and all of these tactics, in an Election year, resulted in this Government instigated Inquiry.

They even talk of "inferior quality of imports". We suggest you ask the juice bottlers. The Industry measure of fruit sugar to acid is expressed as the Ratio. The higher the ratio the sweeter, the lower the ratio, the more bitter (acidic). Typically Brazilian imported FCOJ is sweeter at a ratio of 15-17. Whereas Australian Valencia FCOJ would be anywhere from 11-14 ratio, very, very little above 15 ratio. In the M.I.A. area of NSW (Riverina) they struggle to get much above 13 ratio. Juice Companies when packing 100% long life OJ prefer a minimum of 15 ratio.
A major reason that Florida and Brazil each supply 40% & 47% respectively of the World's Orange Juice is because their quality is the BEST in the world. Unique characteristics of soil, climate and geography found in the states of Sao Paulo and Florida provide ideal growing conditions for this high ratio.

Also, the renewed and repeated use of the totally unsubstantiated accusations of the use of Child Labour in the Brazilian Citrus Industry. It is blatantly untrue and the Brazilian Citrus Industry has been clearly exonerated of such allegations by independent World organizations including UNICEF and is a model for other less developed industries in Brazil in that respect. There is a greater chance of finding "child labour" after school on Mum & Dad's family 10 acre Australian Citrus orchards (perfectly legitimate & understandable, mind you) than on a 5000 acre Corporate Citrus grove in Brazil, operated in the most professional, high tech & sophisticated manner.

One further point in the local campaign worthy of addressing is the accusation that the reduction/destruction of Citrus production over recent times is largely or solely due to Brazilian FCOJ imports. Since the rapid growth of NFC has basically now absorbed similar tonnages to that which previously went to Australian FCOJ, which itself had been more exposed to the world market price pressures, that argument does not hold. The "flight from citrus" to the extent it has happened, has been as much driven by the prospect of higher returns offered in the Wine Industry boom times.

In the S.A. Riverland, not only Citrus, but Deciduous fruit like Apricots, & Peaches have been pulled out in favour of Wine grapes.

In the Victorian Sunraysia, it was predominantly Sultana/Vine Fruit Growers plus some Citrus who changed over to Wine Grapes.

And finally in the NSW Riverina, having lost the Deciduous Fruit Cannery, Letona in Leeton, it was again Peach, Apricot & Pear growers in addition to some Citrus who have changed over to Wine grapes.

It is a case of horticultural farmers changing to more lucrative crops. To try to sheet the blame home to Brazil is nonsense.

There may well be more to be gained by Citrus Growers in a review of the returns paid to Growers in the Domestic Fresh Market between the price paid to the Grower and ultimate selling prices in supermarket/retail, to establish if they are being treated fairly.

In our accompanying Reports there is more than enough data to illustrate Brazil's place in the World of Citrus, which is dominated by Brazil and the USA.
However, allow us to make a few comments.
Orange Production is the largest individual Fruit grown in the World at around 63 million tonnes per annum. By comparison, the next largest is Apple Production, a distant second at 46 million tonnes.
Australia therefore grows less than 1.0% of the World's Oranges.
Brazil grows almost 30% or the World's Oranges with the USA producing 15-16%. However, the most critical point is that between them they produce a staggering 87% of the World's Orange Juice (Brazil 47%, USA 40%).
In all countries except Brazil and USA (Florida), the fresh fruit market is the larger and primary focus of the Citrus Growers. Only in these two areas is the fruit grown for the predominant purpose of processing to juice. We know of no other significant variety of fruit in any country where this is the case.
Apple, for example, the second largest world fruit, is grown everywhere for fresh fruit marketing, whether 1st or 3rd world countries. The "juice quality" apples (bruised, blemished, undersized) are sorted out and recovered as juice.
Australia, currently accounts for between 2-2.5% of Brazils FCOJ exports. World pricing is entirely driven by World supply and demand and all pricing works back to a price FOB port of Santos, Brazil. Individual market price variations are basically only reflecting varying seafreight and logistic costs.
It is interesting to note that where in the past the USA/Florida Citrus Growers fought against Brazilian Imports, this is no longer the case. The growth of both NFC and World Orange Juice Consumption has allayed their fears and allowed continuing growth and new plantings in the Florida Citrus Industry. So much so, that these days Florida is a major Exporter of NFC to the nearby European market and now 4 of the largest 5 Brazilian Citrus Processors also own and operate Florida Citrus Processing Facilities.
In summary, we believe that the future of the Australian Citrus Industry lies in further development of Fresh Fruit Export Markets, including planting of appropriate varieties and in the case of Orange Juice, further co-operative development of Fresh/NFC juice markets including Exports within Asia/Pacific. This may also require the planting of more suitable varieties for our conditions and especially in the Riverina (M.I.A.) region of NSW. Lessons learnt in Florida could assist our industries to change and adapt here rather than fall back on stop-gap protectionist temporary solutions, further deferring faxing up to the inevitable realities of structural change.
If time permits in the inquiry perhaps the Commission should visit Brazil and Florida?
Meanwhile the facts speak for themselves.
We are at your disposal to explain or contribute further.

Yours sincerely,

Geoff McCormack
Managing Director
Interaust Foods