

# Australian Food and Grocery Council SUBMISSION

17 APRIL 2014

**TO:**  
AGRICULTURAL COMPETITIVENESS TASKFORCE

**IN RESPONSE TO:**  
ISSUES PAPER – AGRICULTURAL COMPETITIVENESS  
WHITE PAPER



Australian Food and Grocery Council

## PREFACE

The Australian Food and Grocery Council (AFGC) is the leading national organisation representing Australia's food, drink and grocery manufacturing industry.

The membership of AFGC comprises more than 178 companies, subsidiaries and associates which constitutes in the order of 80 per cent of the gross dollar value of the processed food, beverage and grocery products sectors.

With an annual turnover in the 2012-13 financial year of \$111 billion, Australia's food and grocery manufacturing industry makes a substantial contribution to the Australian economy and is vital to the nation's future prosperity.

Manufacturing of food, beverages and groceries in the fast moving consumer goods sector<sup>1</sup> is Australia's largest manufacturing industry. Representing 28 per cent of total manufacturing turnover, the sector accounts for over one quarter of the total manufacturing industry in Australia.

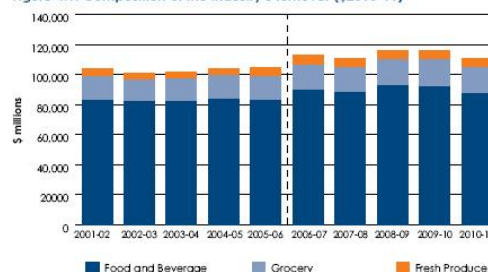
The diverse and sustainable industry is made up of over 25,662 businesses and accounts for over \$50.8 billion of the nation's international trade. These businesses range from some of the largest globally significant multinational companies to small and medium enterprises. Industry spends \$535.8 million a year on research and development.

The food and grocery manufacturing sector employs more than 298,825 Australians, representing about 3 per cent of all employed people in Australia, paying around \$11.3 billion a year in salaries and wages.

Many food manufacturing plants are located outside the metropolitan regions. The industry makes a large contribution to rural and regional Australia economies, with almost half of the total persons employed being in rural and regional Australia<sup>2</sup>. It is essential for the economic and social development of Australia, and particularly rural and regional Australia, that the magnitude, significance and contribution of this industry is recognised and factored into the Government's economic, industrial and trade policies.

Australians and our political leaders overwhelmingly want a local, value-adding food and grocery manufacturing sector.

Figure 4.1: Composition of the industry's turnover (\$2010-11)<sup>a</sup>



Source: Based on ABS, catalogue number 8221.0 and 8159.0

<sup>1</sup> Fast moving consumer goods includes all products bought almost daily by Australians through retail outlets including food, beverages, toiletries, cosmetics, household cleaning items etc.

<sup>2</sup> About Australia: [www.dfat.gov.au](http://www.dfat.gov.au)



The AFGC Agribusiness Forum represents businesses with a role, or interest, in the transformation of raw materials and commodities that are used as inputs to the manufacture of fast moving consumer goods (FMCG).

The AFGC Agribusiness Forum's role is to develop and advocate a policy, regulatory and business environment that facilitates a profitable and internationally competitive agribusiness sector which, in turn, makes a significant contribution to the Australian economy.

The initial priorities of the Forum are to improve the cost competitiveness of the sector, and increase exports of food and beverage products.

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## EXECUTIVE SUMMARY

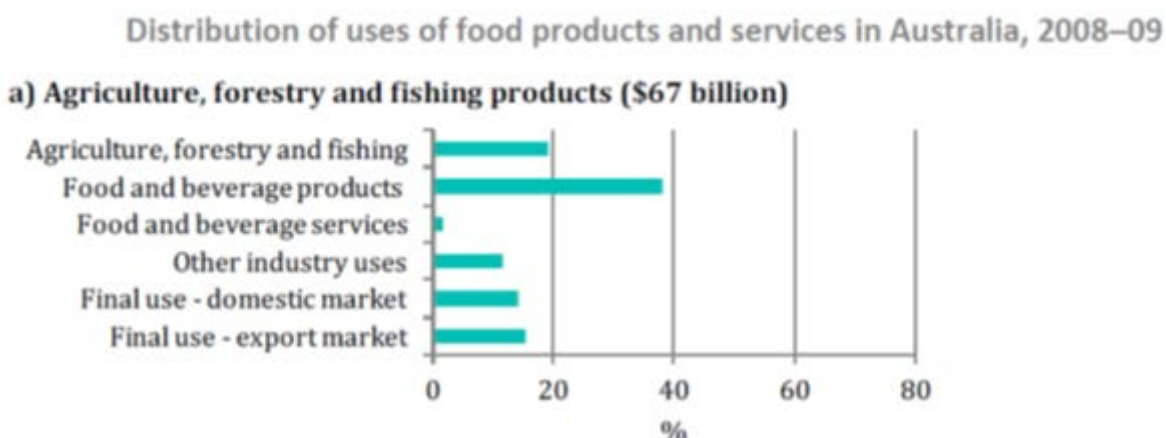
The Australian Food and Grocery Council (AFGC), and the AFGC Agribusiness Forum, welcome the opportunity to provide input to the Australian Government's agri-food policy being developed through the Agricultural Competitiveness White Paper. The AFGC is the leading national organisation representing Australia's food, drink and grocery manufacturing industry and the AFGC Agribusiness Forum represents first stage agri-food processors.

Australian agribusiness plays a vital role by taking often raw agricultural commodities and providing transportation, logistics, storage and processing services before providing products: directly to export markets, to food manufacturers for further processing; back to farmers as inputs such as stock feed; or direct to consumers in the case of fresh fruit and vegetables. Other agribusiness companies provide inputs such as fertiliser and finance to farm operations. Agribusiness is an enabler or connector for the entire agri-food sector: without agribusiness agricultural produce would rot in silos or at the roadside, and food manufacturers would have no product to refine.

The Australian agri-food processing and manufacturing sector is a significant employer across rural, regional and metropolitan Australia, employing approximately 298,825 people. Wherever agricultural production occurs agribusiness is in close proximity. In many rural and regional areas, individual agribusiness facilities and businesses are significant employers that underpin the economic future of towns and regions. In that sense, agribusiness is not only an enabler for the agri-food sector but also an engine room of economic growth for regional Australia.

The Australian food manufacturing sector is a significant source of value adding: by taking raw ingredients and making food staples and luxuries, the food manufacturing sector creates products sought by consumers and adds over \$30 billion to the Australian economy. Approximately 38 per cent of Australia's agricultural production (the largest individual share) goes directly into food processing and manufacturing to produce high value products for consumers in Australia and overseas (see Figure 1).

**Figure 1. Distribution of Primary Production**



Source: 'Infrastructure and Australia's Food Industry: Preliminary Economic Assessment' ABARES 2013

The future of agricultural production cannot be considered in isolation from the agri-food processing sector as revenue, costs and profits are determined by the actions of the entire agri-food supply chain. As has been seen recently, factory closures in the food processing sector have a negative impact on farm returns. The Government's aim of increasing farm profitability and strengthening rural and regional communities therefore fundamentally relies on a strong domestic agri-food processing sector.

The enormous opportunities for Australian agriculture, agribusiness and food industries presented by increasing food demand in Asia have been highlighted extensively<sup>3</sup>. Increasing global population, rising incomes and greater demand for protein and high value foods presents Australian agri-food industries with a platform for growth to 2050.

Australia has a number of strengths in agriculture and food including comparative advantage in the production of specific commodities and food products; broad research, experience and business knowledge in dryland agriculture; and sophisticated food manufacturing capabilities with strong safety and quality systems.

The future of the Australian agri-food sector is in high value added products where we have comparative advantage. This will provide the greatest economic benefit to the industry and Australia more broadly, and deliver the greatest benefit to global food security.

However, the significant global opportunities for the Australian agri-food sector are in stark contrast to the challenges faced. The Agricultural Competitiveness White Paper process comes not a moment too soon as our ability to realise these opportunities is at risk of being lost to competing trading nations. While the Australian agri-food sector is under severe strain with ongoing highly variable seasonal conditions, a persistently strong Australian dollar and fluctuating international commodity prices, the greatest challenges are from policy and regulatory frameworks that impact Australia's competitiveness and export performance.

Increases in regulation, inflexible labour arrangements, and poor infrastructure are the primary causes of Australia's fall from the top 20 competitive countries in the world (as measured by the World Economic Forum). In 2006, Australia was ranked the 16<sup>th</sup> most competitive economy in the world and had an average 11 per cent market share of food exports in key Asian markets<sup>4</sup>. By 2013, Australia had fallen to 21<sup>st</sup> most competitive country and our market share had fallen to an estimated 6.5 per cent (see Figure 2).

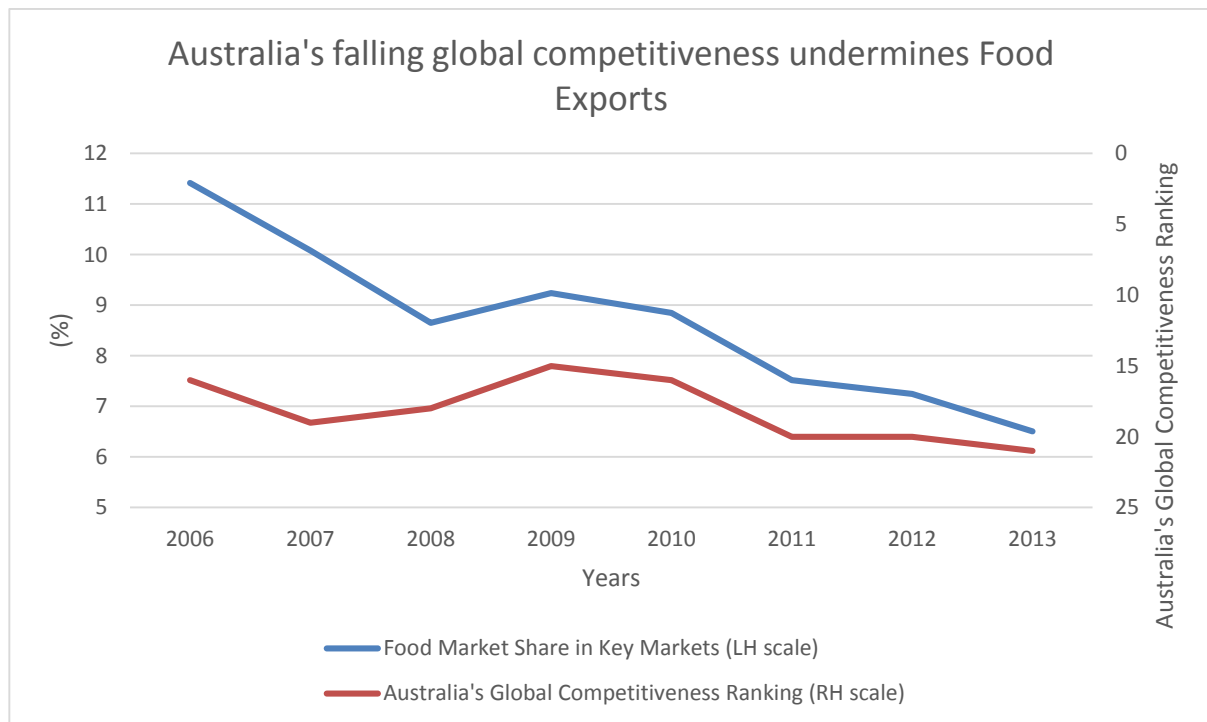
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<sup>3</sup> Including:

Deloitte 'Positioning for Prosperity' Oct 2013;  
ABARES 'Long-term food consumption trends in China' Oct 2013;  
DAFF 'Food Consumption trends in China' Apr 2012;  
KPMG 'Expanding Horizons: Agribusiness in Australia' 2012;  
ANZ 'Global Soft Commodity Opportunity for Australia and New Zealand' 2012;  
OECD 'OECD-FAO Agricultural Outlook' Annual Publication.

<sup>4</sup> 'Food Market Share in Key Markets' is average Australian export share in China, Japan, Korea, Indonesia, Malaysia, and Thailand. As defined, food does not include live animals and bulk grains.

**Figure 2. Australia's Competitiveness and Food Market Share**



Source: World Economic Forum (2013): Global Competitiveness, & calculations from UN Comtrade Database (2014): Food market Share.

Tackling the factors that have contributed to this fall in Australia's competitiveness and export market share is vital to improving the profitability of the agri-food sectors and the viability of rural and regional communities. This requires action on the following issues:

1. **Trade** - The AFGC welcomes the recently concluded trade agreements with Japan and Korea. The Australian Government needs to continue securing free trade agreements that deliver real commercial outcomes, particularly for agribusiness sectors such as dairy and beef and extending to packaged foods, to drive higher returns for the whole food sector, from farmers to food processors.
2. **Promotion** – The Australian and state governments need to collaborate and coordinate their trade promotion activities to capitalise on improved market access. Clean and green is not enough – the development of a national food brand based on the concept of 'Trust Australia' is vital.
3. **Investment** - Just as Australia's surging mineral exports have come as the result of a decade of massive investment, there is a need for similar step-change in investment in Australia's food sector from farm to processor to essential infrastructure. With mining and energy investment now set to fall, stimulating investment into the food sector is a national economic imperative.



4. **Infrastructure** – The agri-food sector is spread across the length and breadth of the continent. Infrastructure planning and delivery needs to reflect the sector’s unique requirements and develop supply chain solutions that create world leading, efficient channels to market.
5. **Competitiveness** - Getting costs down to improve competitiveness is urgent, and regulatory costs and energy costs are two areas where we seem to have a great capacity for self-inflicted damage. Think live cattle export bans, carbon tax and now a doubling or tripling of gas prices on the east coast as examples of how we have managed to sabotage our competitiveness.
6. **Innovation** – There needs to be greater direction of Australia’s R&D efforts into the food sector and greater collaboration between producers, processors, marketers, packagers and designers to drive real innovation in product and process innovation that responds to the demand drivers in key markets.

## Recommendations

### The AFGC recommends that:

#### 1. on Trade Negotiations,

- a. the Australian Government concludes a comprehensive and commercially meaningful trade agreement with China as a critical priority; followed by a focus on negotiations with India and Indonesia;
- b. the Australian Government continues to drive regional trade negotiations (TPP, RCEP) with a view to securing the most liberalising outcomes; and
- c. Australia leads discussions in the WTO to multilateralise trade liberalisation occurring in bilateral and regional agreements.

#### 2. on Trade Promotion,

- a. the Australian Trade Commission (Austrade) is resourced to complete development of a national food brand and to support promotion of Australian agri-food exports;
- b. that the national food brand reflect the message 'Trust Australia' embodying Australia's food safety and quality attributes; and
- c. relevant Australian Government agencies (such as DFAT, Austrade, FIAL, DAFF and Department of Industry), and state and territory government agencies, work cooperatively to promote Australian agri-food exports using the national food brand.

#### 3. on Investment,

- a. trade agreements include provisions that support new investment; and
- b. the Australian Government continues to promote Australia as a destination for global investors.

#### 4. on Infrastructure,

- a. any new infrastructure planning and delivery addresses the specific requirements of the agri-food sector and focusses on areas that deliver the highest returns to the economy.

#### 5. on Competitiveness,

- a. the Australian Government accelerate the national economic reform agenda, focussing on deregulation, greater flexibility in the labour market, and targeted infrastructure expenditure and regulatory reform.

#### 6. on Innovation, Research and Development

- a. the Australian Government clearly define executive responsibility for food policy and research;
- b. initiatives such as Food Innovation Australia Limited, and their role supporting collaboration and innovation, be further strengthened;
- c. the Australian Research Council, through the Industrial Transformation Research Program, continue to prioritise the food manufacturing sector; and
- d. the Australian Government develops new opportunities to support commercialisation in the food industry, particularly with regard to new products from small and medium enterprises (SMEs).

## 1. ISSUE 1: ENSURING FOOD SECURITY IN AUSTRALIA AND GLOBALLY

### 1.1. Global food security

The enormous opportunities for Australian agriculture, agribusiness and food industries presented by increasing food demand in Asia have been highlighted extensively<sup>5</sup>. Increasing global population, rising incomes, and greater demand for protein and high value foods presents Australian agri-food industries with a platform for growth to 2050.

There have been suggestions that Australia will become the 'food bowl' of Asia through huge increases in agricultural and food production. While Australia is a medium sized agricultural exporter, we are a small global producer. A review of the data shows that agricultural production in some countries is many times larger than in Australia: four times larger in Brazil, eight times larger in the United States, ten times larger in the European Union and twenty times larger in China (see Figure 3).

**Figure 3. Agricultural Production in Selected Countries**

| Country                  | Approximate Value of Agricultural Production in 2012 (USD) |
|--------------------------|--|
| Australia                | \$45 billion   |
| Brazil                   | \$188 billion  |
| Canada                   | \$50 billion   |
| China                    | \$930 billion  |
| European Union           | \$473 billion  |
| Japan                    | \$100 billion  |
| United States of America | \$396 billion  |

Source: Calculations from OECD Producer Support Estimates Database

Similarly, a review of Australia's position as a global food exporter shows that we are ranked approximately 16<sup>th</sup> in the world by share of value of global food exports. Recognising our position in the

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<sup>5</sup> Including:

Deloitte 'Positioning for Prosperity' Oct 2013;  
ABARES 'Long-term food consumption trends in China' Oct 2013;  
DAFF 'Food Consumption trends in China' Apr 2012;  
KPMG 'Expanding Horizons: Agribusiness in Australia' 2012;  
ANZ 'Global Soft Commodity Opportunity for Australia and New Zealand' 2012;  
OECD 'OECD-FAO Agricultural Outlook' Annual Publication.

world is critical to realising our potential contribution to global food security, and participating in the economic benefits of growing global demand.

**Figure 4. Australia's rank as a global food exporter**

| Share of World Food Exports in 2011 |                |      |
|-------------------------------------|----------------|------|
| Rank                                | Country        | %    |
| 1                                   | United States  | 10.2 |
| 2                                   | Netherlands    | 6.2  |
| 3                                   | Brazil         | 5.8  |
| 4                                   | Germany        | 5.8  |
| 5                                   | France         | 5.7  |
| 6                                   | China          | 4.2  |
| 7                                   | Argentina      | 3.4  |
| 8                                   | Canada         | 3.4  |
| 9                                   | Spain          | 3.3  |
| 10                                  | Belgium        | 3.2  |
| 11                                  | Italy          | 3.1  |
| 12                                  | Indonesia      | 2.5  |
| 13                                  | Malaysia       | 2.5  |
| 14                                  | Thailand       | 2.5  |
| 15                                  | United Kingdom | 2.3  |
| 16                                  | Australia      | 2.2  |

Source: UN Statistics Division (2012) & DAFF Australian Food Statistics

Even if Australia was to double or triple our exports of agri-food products we are not going to be a dominant global supplier or 'food bowl' in global markets. Australia does have a role to play in food security by providing safe, nutritious and premium food products that supplement domestic food production in many emerging markets, such as in Asia. In this sense, the AFGC supports commentary that Australia should focus on being the 'delicatessen' rather than the food bowl of Asia.

This role draws on Australia's strengths in agriculture and food production including comparative advantage in the production of specific commodities; broad research, experience and business knowledge in agriculture; and sophisticated food manufacturing capabilities with strong safety and quality systems, under the oversight of an advanced food regulatory system.

## 1.2. Domestic food security

In previous government submissions, the AFGC made the following fundamental points about domestic food security:

- food security is not synonymous with food self-sufficiency;
- the vast majority of the food consumers eat is produced by the food manufacturing sector: consumers eat bread, not wheat, steak, not steers, and pasteurised milk and cheese. Very few food products are suitable for consumption pre-farm gate, and most are consumed in Australia with some form (often extensive) of further processing post-farm gate;
- many manufactured food products rely on inputs derived globally;
- for food manufacturing to remain in Australia it must remain competitive against imports;
- given that food manufacturing is a sizeable industry, it is in Australia's best interest that it is not only competitive against imports, but globally competitive and able to drive premium, value-added exports into global markets.

There remains potential for geopolitical events to disrupt supplies of essential food items, particularly given the likely close balance between supply and demand for the foreseeable future. AFGC is of the view that the Australian Government should develop a strategy which seeks to secure food supplies for Australians in the longer term and builds resilience so that short term shocks (i.e. from natural disasters) are minimised. Australia's agri-food policy must:

- recognise that food manufacturing in Australia plays centrally to guaranteeing food security in Australia as true food security is provided by having access to a range of safe, nutritious, affordable foods, not simply a surplus of food commodities;
- acknowledge that Australia's food security (properly defined) is dependent upon international trade in imports of specialist food ingredients, despite Australia having protein and calorie self-sufficiency and indeed surpluses; and
- incorporate strategic policy initiatives combined with encouraging market forces as the best approach for securing Australia's food security.

## 1.3. Continuity of supply during emergencies

The AFGC supports the Australian Government working with the state and territory governments and the food industry to develop strategies to mitigate risks and maintain continuity of food supplies in major emergencies.

The AFGC is part of the Food and Grocery Sector group of the *Trusted Information Sharing Network* (TISN)<sup>6</sup>. AFGC member companies have played a critical role in supporting food and grocery supply

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<sup>6</sup> <http://www.tisn.gov.au/Pages/Food-Chain-Group.aspx>

during the natural disaster emergencies (fires, floods etc.) that have affected the supply chain over recent years.

To ensure continuity of supply during emergencies AFGC considers it is important that governments, as far as possible, facilitate the continued operation of existing market mechanisms. When normal market operations are suspended during emergencies, governments need to engage with food companies, logistics operators and retailers to maintain supply, including through provision of reasonable compensation for additional costs borne by industry to avoid significant disruption.

Further steps to strengthen the food supply chain resilience, or areas that need additional investigation to provide a more reliable indication of areas of threat or vulnerability include:

- examining parallel supply chains such as food services that can contribute to responses to emergencies;
- investigating the advantages and disadvantages of stockpiling food including at the consumer level – i.e. assessing the effectiveness of the 'pantry list' initiative;
- testing business continuity and organisational resilience to determine whether major food companies in particular have contingency plans for dealing with emergencies;
- testing planning arrangements to ensure appropriate responses are prepared for the 'worst case scenario' of a major emergency, including a pandemic;
- periodic tracking and analysis of critical import dependencies and capacity for substitution within Australia;
- analysis of the supply chain to understand weaknesses and tipping points at times of stress; and
- maintaining strong governance arrangements in food supply chain resilience planning to ensure decision making in times of emergency is rapid and appropriate.

It is also very important that the long term resilience of the food industry is considered. Simply put, without a viable domestic food manufacturing industry, basic food items will not be able to be supplied in a timely manner in times of emergency. Supply chains from overseas may be too long, or not flexible enough to meet unusual demand patterns which occur during times of national emergency.

The AFGC currently chairs the Food and Grocery Sector Group under the Trusted Information Sharing Network. As part of ongoing work, the AFGC has recently submitted an application to *the National Emergency Management Projects* program seeking funding to enhance the *National Food Sector Integrated Emergency Food and Grocery Distribution Model*. This work will increase disaster preparedness and recovery resilience for a food emergency, particularly among vulnerable populations.

## **2. ISSUE 2: FARMER DECISIONS FOR IMPROVING FARM GATE RETURNS**

### **2.1. Best practice**

A successful, efficient, profitable and innovative agricultural sector is critical to the ongoing success of the Australian agribusiness and food manufacturing sector. Australia's combination of climate, soils and geography can at times create a challenging environment for agricultural production; agricultural research and extension has been key in raising Australia's agricultural productivity.

Specific practices such as land mapping, crop monitoring and livestock tracking are examples of best practice methods which benefit the environment through improved soil and reduced water use, and benefit the farmer economically through lower input use and machine wear. Adoption of innovative and best practice is a key area of productivity improvement and education is critical to accelerating uptake.

### **2.2. Global commodity prices**

As a small open market in the global marketplace, Australia's commodity prices are determined by international markets. The volatility in global commodity prices has affected producers, processors and manufacturers by reducing predictability and undermining profitability. While the vagaries of international markets can be frustrating for all participants in the supply chain, the market supply and demand are the final drivers of price.

With an expectation of increasing climate variability affecting agricultural production around the world, volatility in international commodity prices can be expected to continue. Previous Australian, and current international, efforts in managing prices through government controlled stockpiling or price setting have ended in failure. All participants in the Australian supply chain must increase their knowledge and understanding of mechanisms to manage price and risk through current and new market-based instruments.

### **2.3. Supply chain integration**

Greater connectivity and integration is required in agri-food supply chains to create efficiencies, reduce waste and input use, and share information on issues such as product attributes and consumer preferences. This will help to improve returns by providing greater value to final consumers. Current supply chain integration initiatives include producer roundtables held by agribusiness companies to exchange information and financing programs provided by agribusiness companies to support producers.

To date, much government funded research has been focussed on pre-farmgate, commodity production issues. Significant benefits would result from government funded research which focussed on commodity specific, and cross-commodity, supply chain issues. Current research gaps include international demand for Australian processed food products, key infrastructure constraints in Australia, and alternative channels to market.

### 3. ISSUE 3: ENHANCING ACCESS TO FINANCE

The Australian agricultural, agribusiness and food industries have been export focussed since the beginning of commercial agriculture in Australia. Today's agribusiness and food industries have been constructed on a strong and competitive agricultural sector with world class practices and productivity. The continued success of Australian agricultural production is essential to the future of the agribusiness and food manufacturing industries.

#### 3.1. New capital required

All businesses finance their operations in a range of ways, including direct equity investment, debt finance and portfolio investment (such as issuing shares). Non-equity investments may take other forms such as contract manufacturing, licensing or franchising. All of these types of investment may be from domestic or foreign sources. While there are advantages and disadvantages of each type of investment, it is important that businesses can take advantage of the type of investment that meets their specific needs and risk and reward profile.

With low Australian savings rates, and the continuing opportunities to grow the economy across many sectors, there is insufficient domestic capital to meet Australia's demands and opportunities for equity investment. Hence foreign direct investment can contribute much needed financial capital to support a domestic food processing and manufacturing presence. This has a direct benefit to the Australian economy and community through employment and economic growth, particularly in rural and regional areas where many of these businesses are located.

In addition to being a relatively stable source of finance, direct foreign investment can provide Australia with access to research, skills, technologies, and equipment that are vital to achieving innovation within the agribusiness and food manufacturing sectors. Innovation and the resulting productivity improvements in these sectors will help increase the international competitiveness of Australia's food supply industry, which is particularly important given the trade challenges the industry faces as a result of the high Australian dollar.

Australia has benefited greatly from foreign capital investment in its food manufacturing sector. Foreign investment can, and does, play an important role in other parts of the food supply chain, such as the post farm-gate agribusiness and food manufacturing sectors.

Stronger export trade will generate income and employment growth and will assist the Australian agri-food industry to gain economies of scale in production. This will improve the competitiveness of Australian manufactured food in the domestic market compared to imports, and Australia's competitiveness in overseas markets.

Without the productivity improvements and relationships with export markets that are stimulated by foreign investment, it will be difficult for Australia to take advantage of growing food demand opportunities in Asia to 2050.

#### 3.2. Innovative approaches

The investment required to drive Australian agri-food production and exports to 2050 will require new and innovative approaches to overcome perceptions of the sector and the fundamental issues around generating sufficient returns in a high cost economy and variability of returns compared to other sectors.



One example of new thinking is the 'Partnerships' program<sup>7</sup> developed by Murray Goulburn Cooperative. The program provides supplier-shareholders with an alternate pathway to farm expansion through leasing of farmland owned by equity funds. This allows farmers to maintain capital for spending on cows and business infrastructure as it has not been sunk into the purchase of new farmland. While leasing of farmland is not a new concept, the structured and systematic approach in partnership with a large Australian company is promising.

A recently formed company, National Land Lease<sup>8</sup>, aims to provide a suite of services around leasing and land management. The benefits of leasing are identified as lower costs of entry for those looking to move into agriculture, opportunities for expansion for existing producers, and the opportunity to free up capital for business expansion for existing landholders.

Murray Goulburn Cooperative is also providing 'Trading Finance'<sup>9</sup> to supplier-shareholders to meet requirements for seasonal operating expenses and dairy equipment investments and upgrades. This financing facility helps producers with cash flow management and business sustainability. Other large Australian agribusiness companies are currently considering opportunities to provide trade finance to clients and suppliers.

### 3.3. Australia: investment destination?

The WEF Competitiveness Ranking lists Australia at 80<sup>th</sup> for the effect of taxation on incentives to invest, indicating that taxes significantly reduce the incentive to invest in Australia. Similarly, Australia ranks 41<sup>st</sup> for the impact of rules and regulations discouraging foreign direct investment in Australia.

The United Nations 'World Investment Report 2013' identifies that Australia's global rank as an attractive destination for foreign investment fell from 6<sup>th</sup> in 2012 to 13<sup>th</sup> in 2013. Vietnam, the Russian Federation and Mexico were all ranked as more attractive investment destinations than Australia and our agri-food competitors Brazil and the United States ranked at 5<sup>th</sup> and 2<sup>nd</sup> respectively.

The United Nations estimates that between 2008-2012 Australia lost \$89 billion in foreign investment (through failed mergers and acquisition) due to regulatory concerns or political opposition – the greatest loss of foreign investment in the world by value.

Between 1990 and 2012, Australia's stock of foreign investment multiplied 7.6 times from \$80 billion to \$610 billion. In comparison, the stock of foreign investment multiplied: more than 11 times in New Zealand, more than 10 times in the European Union and 7.2 times in the United States. While the European Union and the United States are considered economies with good access to internal capital, the increases are in the same range as Australia's, which is considered a capital poor economy. Clearly, Australia's ongoing requirement for access to global capital markets is consistent with the trends in other OECD economies.

As part of the review of investment, the IMD Competitiveness Center measures the threat of international relocation on the future of the Australian economy. Australian business identifies relocation as a serious threat with Australia ranked:

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<sup>7</sup> <http://www.mgc.com.au/media/4743/MG-Partnerships-Fact-Sheet.pdf>

<sup>8</sup> <http://www.nationallandlease.com.au/>

<sup>9</sup> <http://www.mgc.com.au/media/4800/MG-Trading-Finance-Fact-Sheet.pdf>

- 49th on the threat of relocation of production,
- 50th on the threat of relocation of research and development, and
- 43rd on the threat of relocation of services.

The fall in investment attractiveness for Australia is concerning not only for flows of foreign investment but for domestic sources of capital. In a global environment, Australian investors will consider opportunities for investment in any country. Australia needs to maintain an attractive investment environment to attract capital as a critical input to future economic growth.

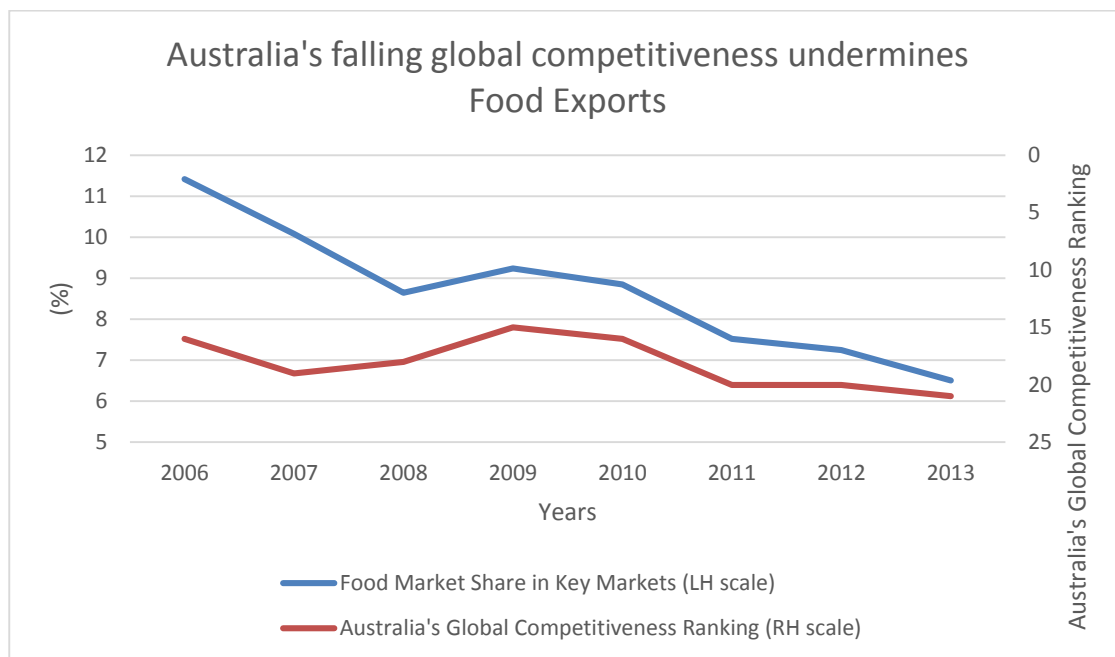
## 4. ISSUE 4: INCREASING THE COMPETITIVENESS OF THE AGRICULTURE SECTOR AND ITS VALUE CHAINS

### 4.1. Australia – a delicatessen to Asia?

The significant global opportunities for the Australian agri-food sector are in stark contrast to the challenges faced. The Agricultural Competitiveness White Paper process comes not a moment too soon as our ability to realise these opportunities is at risk of being lost to competing trading nations. While the Australian agri-food sector is under severe strain with ongoing highly variable seasonal conditions, a persistently strong Australian dollar and fluctuating international commodity prices, the greatest challenges are from policy and regulatory frameworks that impact Australia's competitiveness and export performance.

Increases in regulation, inflexible labour arrangements, and poor infrastructure are the primary causes of Australia's fall from the top 20 competitive countries in the world (as measured by the World Economic Forum). In 2006, Australia was ranked the 16<sup>th</sup> most competitive economy in the world and had an average 11 per cent market share of food exports in key Asian markets<sup>10</sup>. By 2013, Australia had fallen to 21<sup>st</sup> most competitive country and our market share had fallen to an estimated 6.5 per cent (see Figure 2).

**Figure 2. Australia's Competitiveness and Food Market Share**



Source: World Economic Forum (2013): Global Competitiveness, & calculations from UN Comtrade Database (2014): Food market Share.

<sup>10</sup> 'Food Market Share in Key Markets' is average Australian export share in China, Japan, Korea, Indonesia, Malaysia, and Thailand. As defined, food does not include live animals and bulk grains.

Tackling the factors that have contributed to this fall in Australia's competitiveness and export market share is vital to improving the profitability of the agri-food sectors and the viability of rural and regional communities. This requires action on the following issues:

1. **Trade** - The AFGC welcomes the recently concluded trade agreements with Japan and Korea. The Australian Government needs to continue securing free trade agreements that deliver real commercial outcomes, particularly for agribusiness sectors such as dairy and beef and extending to packaged foods, to drive higher returns for the whole food sector, from farmers to food processors.
2. **Promotion** – The Australian and state governments need to collaborate and coordinate their trade promotion activities to capitalise on improved market access. Clean and green is not enough – the development of a national food brand based on the concept of 'Trust Australia' is vital.
3. **Investment** - Just as Australia's surging mineral exports have come as the result of a decade of massive investment, there is a need for similar step-change in investment in Australia's food sector from farm to processor to essential infrastructure. With mining and energy investment now set to fall, stimulating investment into the food sector is a national economic imperative.
4. **Infrastructure** – The agri-food sector is spread across the length and breadth of the continent. Infrastructure planning and delivery needs to reflect the sector's unique requirements and develop supply chain solutions that create world leading, efficient channels to market.
5. **Competitiveness** - Getting costs down to improve competitiveness is urgent, and regulatory costs and energy costs are two areas where we seem to have a great capacity for self-inflicted damage. Think live cattle export bans, carbon tax and now a doubling or tripling of gas prices on the east coast as examples of how we have managed to sabotage our competitiveness.
6. **Innovation** – There needs to be greater direction of Australia's R&D efforts into the food sector and greater collaboration between producers, processors, marketers, packagers and designers to drive real innovation in product and process innovation that responds to the demand drivers in key markets.

## 4.2. Innovation

Innovation is the cornerstone of the food processing industry's return to growth and to its prospects to 2050. Innovation in both product and production holds the key to:

- raising productivity;
- improving competitiveness in both domestic and export markets;
- opening up new markets; and
- responding effectively to consumer trends.

The Government provides comprehensive support to primary industries through the research and development corporations (RDC) and the co-operative research centre programs (CRC). Both of these programs are valuable and they support some post farm-gate research however there is little targeted government support or research in the food manufacturing sector.

The AFGC welcomes Food Innovation Australia Limited (FIAL) and their role supporting collaboration and innovation in the sector. FIAL must continue to build on existing organisations, networks and support mechanisms to begin rebuilding innovation momentum in the food manufacturing sector.

A food industry innovation hub is, however, only part of the answer to maximising the gains from innovation for the food processing sector. A range of other policy issues must be addressed to restore Australia's competitiveness and support the development of more value added manufacturing and high value exports. Certainty in Government policy settings over the short to medium term is also a critical to a business environment conducive to investment, growth and profitability. Frequent changes to policy and/or regulation adds direct costs to business and adds risk premium investment planning.

### **4.3. Policy framework for driving Investment and growth**

#### **Return on investment**

Multinational food companies, by definition, operate around the globe and make investment decisions based upon a range of factors including the most attractive returns on investment (ROI). Currently, Australia's comparatively high cost-base for food manufacturing makes achieving attractive ROI for investment a substantial challenge.

Governments can improve ROI though providing direct incentives to investment including through measures such as special tax allowances on investment in new plant. ROI can also be effectively boosted by reducing business risk through measures such as reducing regulatory compliance burdens, growing a skilled workforce to service the industry, and providing appropriate R&D incentives and research support network. These are increasingly important to offset Australia's comparatively high cost-base in key input costs such as labour, energy and commodities.

#### **Boosting consumer value propositions**

A complementary approach to improving ROI is to drive up the 'value' offering to the market – that is, to manufacture premium products commanding high prices. To achieve this, consumer value proposition must be enhanced.

AFGC considers an opportunity exists to drive food exports into Asia based on leveraging some particular Australian value propositions, such as:

- provenance – unique, remote and pristine food production areas. With a growing number of visitors from Asia the opportunity to leverage the tourism experience of overseas visitors is substantial. Offering tourists the opportunity when they return home to buy the same products and brands from their local supermarket they experience in Australia adds to the overall experience and 'buy in' to Australia;
- premium quality – quality ingredients and advanced manufacturing technologies. By using the best technologies across production, manufacturing and in the supply chain Australian products tweaked to appeal to different markets should become synonymous with 'premium quality', and so command a higher price in the market ;

- assured safety – best regulatory system in the world – government certification. Food safety and food adulteration issues are becoming more of an issue, including in Asia. Australian food enjoys a reputation of being very safe, and very well regulated. This reputation can be leveraged to further enhance the value proposition of Australian food products; and
- environmentally sustainable – low impact, highly efficient agriculture and manufacturing. From production through to all stages of manufacturing Australian should leverage efficiency and drive towards low impact environmentally sustainable food production.

The AFGC supports the work underway by Austrade to develop a national food brand and a strategy for coordinated promotional activities by federal and state government agencies. The AFGC is however concerned that the development of a national food brand is too focussed on ‘clean and green’ and lacks aspiration. ‘Clean and green’ is now becoming a right to play rather than a differentiator, with several competing nations such as Canada and New Zealand also seen as ‘clean and green’. In addition, a limited focus on ‘clean and green’ leaves Australian industry exposed if there is a food safety or environmental incident that invalidates the ‘clean and green’ proposition.

Instead, Australia needs to position its agri-food industry to connect with consumers at a deeper level. Given government policy and industry action are focussing efforts on developing the Australian agri-food industry to be a supplier of premium, innovative value-added products, then this needs to be reflected in our national food branding. In addition, the national food brand needs to consist of a hierarchy of messages – a strong national brand that invites consumers to explore state, regional or local tourism and food experiences, which have their own branding that sits within a national context.

With these elements in mind, the AFGC recommends that the national food brand ‘Trust Australia’ be adopted, with the sub-messaging ‘Trust, discover, be tantalised’:

- ‘Trust Australia’ tells consumers that they can trust the quality and safety of Australian food products. It’s more than just a claim – it builds consumer confidence, given Australia’s reputable traceability and supply assurance systems. In the rare event that there is a food safety or environmental incident, consumers can be confident that it will be detected and remedied quickly and is not a systemic problem.
- ‘Discover’ provides an invitation to consumers to discover the many and diverse regional and local food and tourism experiences within Australia.
- ‘Be tantalised’ speaks to consumers about the premium quality and taste of Australian agri-food products.

The development of a national food brand needs to be backed up by commitment from federal and state governments to adopt the national food branding and for States and regions to be promoted within the context of the national brand. All too often industry relays frustration from their customers about the fragmented Australian promotional activities and the confusion that causes. Unless a more collaborative and coordinated approach is adopted, Australia risks continuing to lose market share to countries that have a more strategic and coordinated promotional approach.

#### 4.4. Farmers, processors, manufacturers and supermarkets

There is no doubt that agriculture, agribusiness and food industries in Australia are particularly affected by a continuing, highly aggressive price war between the major retailers which is squeezing supplier margins.

Against this back drop many companies are struggling to adjust rapidly enough to meet the new market dynamics, and indeed build a business case for continuing investment in manufacturing and innovation in Australia.

The AFGC has previously highlighted to Australian Government its concerns regarding the highly concentrated supermarket retail sector in Australia and the effect of this imbalance in market power on suppliers. AFGC contends that for long term financial viability there must be equitable risk and reward arrangements across of all parts of the supply chain. It is in the interest of suppliers, retailers and consumers.

Detailed financial analysis conducted by the AFGC and KPMG in 2013, and released in the Competitiveness and Sustainable Growth Report 2013, found there has been a significant shift of profitability from suppliers to retailers over the past four years as suppliers have increasingly funded price discounting by retailers. The report also found the profitability of Australian suppliers has fallen well below international comparators.

There are both structural aspects to this problem, related to the concentrated market power of two dominant supermarket chains, and behavioural elements, related to the tactics used in business to business negotiations.

The AFGC welcomes the 'root and branch' review of Competition Law being undertaken by the Government, including the examination by that review of the market power provisions of the CCA, as well as competition issues related to the scale and vertical integration of the major supermarket chains.

With regard to behavioural problems in retailer-supplier relationships, the AFGC has worked with the major supermarket chains (and in consultation with the Australian Competition and Consumer Commission to develop a Food and Grocery Industry Code of Conduct (the Code). Its purpose is to guide all parties in the supply chain to acceptable standards of conduct during the negotiation of trading contracts.

The Code does not seek to impose overly restrictive rules on commercial negotiations and recognises it is not possible to set rules for every set of circumstances in supply agreements. Clear standards are being proposed to ensure those elements in a supply agreement which could be subject to uncertainty and change are discussed up front, to allow both parties to agree on how costs and payments will be allocated. Suppliers are entitled to know where they stand and invest with greater security, as provided for in the Code.

The intent is that the Code be a "Prescribed Code" under the CCA. It will apply to retailers that choose to 'opt in'. Both the major supermarket chains have committed to sign up to the Code as agreed with the AFGC. As a result of a retailer agreeing to be bound by the Code it will automatically cover the retailers agreements with all suppliers with whom that retailer has a trading relationship.

The overarching principle of 'good faith' applies to all industry participants, requiring them to act in good faith, honestly, reasonably and cooperatively in commercial dealings. It also aims to regulate the



behaviour of industry participants in a manner which will allow for long-term consumer benefit in terms of both grocery price and choice.

The Code is based on an agreed set of principles and guidelines. There are ten key principles that underpinned the Code. The principles include:

- bargaining in good faith;
- being fair, just and reasonable;
- taking due care and being responsible;
- showing respect for commercial relationships;
- using simple and easy to understand terms and conditions;
- prior agreement between the parties on all terms and conditions;
- being transparent and ensuring full disclosure of all critical information;
- providing adequate time to consider and review agreements and changes;
- meeting all commitments and making deliveries and payments in full, on time; and
- a confidential and supportive complaints and dispute resolution process.

The Code requires retailers who 'opt in' to incorporate the Code into agreements for the supply of groceries for resale within Australia and to supply a written copy of the agreement and certain information to the supplier.

Retailers are required by the Code to train their Category Managers / Buyers / Commercial teams about the Code and its content. They must appoint a Code Compliance Officer to act as a point of contact with suppliers and to prepare an annual compliance report for review by the ACCC.

Based on principles of fair dealing the Code provides surety of contract for suppliers:

- requirement for retailers to have and maintain supply agreements with all vendors. (i.e. a written contract);
- payment of goods must be in accordance with the agreement;
- prevents retrospective cost claims, except in limited circumstances;
- no payments for shrinkage (theft);
- prohibitions on payments for wastage, except in limited circumstances;
- no payments for better positioning of product in store, except in limited circumstances;
- clarity around promotional activities and funding;
- prevents retailers shifting costs onto suppliers unfairly or without due discussion and negotiation;



- requires genuine commercial reasons for delisting of products;
- obligations relating to retailers own brands i.e. intellectual property, confidentiality, transparency of range/shelf space allocation and exclusivity;
- delivers a time efficient and cost effective dispute resolution process;
- requires retail buyers to be educated and trained in the Code content; and
- requires retail organisations to employ a code compliance manager to oversee complaints.

The Code includes two reciprocal obligations which apply to both suppliers and retailers, namely:

- respect for intellectual property rights (clause 9.1); and
- obligation to deal with each other lawfully and in good faith (clause 10).

A dispute resolution process is included in the Code. A supplier who believes that a Retailer has breached the Code has a number of dispute resolution mechanisms available to them, including direct to the retailer; legal action; arbitration or mediation; or via the ACCC.

The AFGC, Coles and Woolworths agreed to all the Code obligations on Monday 18 November 2013. The Government has agreed to progress the draft Code through a regulatory review process. Treasury will conduct the review, beginning with the release of an options regulatory impact statement and consultation with the broader industry. The process will take some months to complete. It remains the intent of AFGC, Coles and Woolworths that the Code be tabled in Parliament as a regulation under the CCA once the regulatory review process is complete.

## 5. ISSUE 5: ENHANCING AGRICULTURE'S CONTRIBUTION TO REGIONAL COMMUNITIES

Australia is a large continent with a small population mostly located in a small number of coastal regions. Agricultural production and supporting agribusiness operations are spread far and wide across the continent. Australia's sparse population in rural and regional areas creates challenges for the provision of infrastructure such as roads and telecommunications which are critical to 21<sup>st</sup> century efficient business operation. Similarly, the availability of skilled labour is often an issue particularly in areas of significant mining activity. These issues highlight the tension between the provision of infrastructure to support industry expansion, and industry expansion creating demand for additional infrastructure.

Australian agribusiness plays a vital role by taking often raw agricultural commodities and providing transportation, logistics, and processing services before providing products: to food manufacturers for further processing; back to farmers as inputs such as stock feed; or direct to consumers in the case of fresh fruit and vegetables. Other agribusiness companies provide inputs such as fertiliser and finance to farm operations. Agribusiness is an enabler or connector for the entire agri-food sector: without agribusiness agricultural produce would rot in silos or at the roadside, and food manufacturers would have no product to refine.

The Australian agri-food processing and manufacturing sector is a significant employer across rural, regional and metropolitan Australia, employing approximately 192,000 people. Wherever agricultural production occurs agribusiness is in close proximity. In many rural and regional areas, individual agribusiness facilities and businesses are significant employers and underpin the economic future of towns and regions. In that sense, agribusiness is not only an enabler for the agri-food sector but also an engine room of economic growth for regions around Australia.

Using examples of meat and dairy processing, the following sections illustrate the importance of agribusiness and food processing to agricultural production, and the contribution to rural and regional communities.

### 5.1. Meat processing

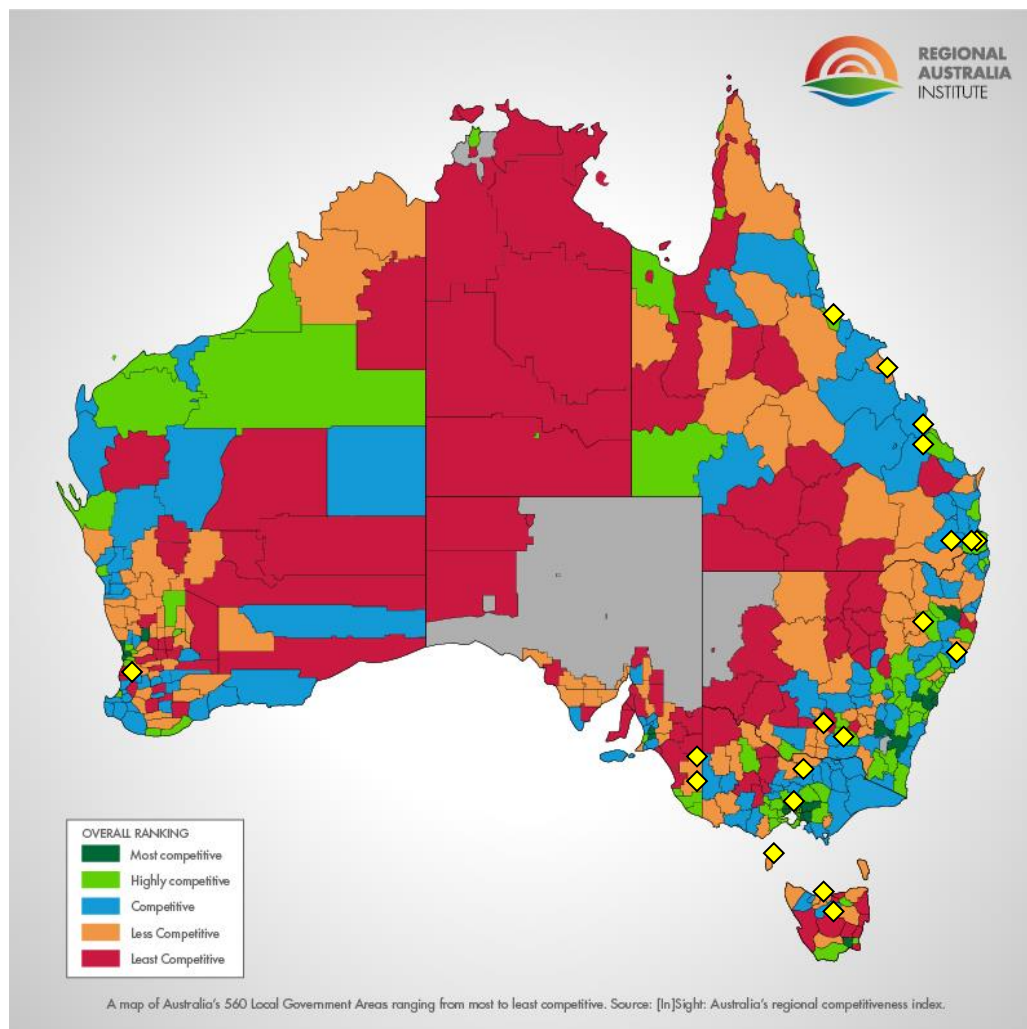
Cattle production stretches the length and breadth of Australia and this is reflected in the widespread locations of beef processing facilities. It is important to note that cattle production in Northern Australia is focussed on the live export trade and this can be seen through the current lack of beef processing facilities in that region.

The beef processing sector employs more than 44,000 across Australia. Queensland and New South Wales each have more than 13,000 employees in the sector, and Victoria has more than 9,000. In the areas immediately west and north-west of Brisbane, more than 4,500 people are employed in the beef processing sector, and more than 1,500 are employed in the Riverina, Bendigo, and New England regions.

The beef processing sector can be characterised as labour intensive with a heavy reliance on access to high quality and reasonably priced product, along with significant capital requirements across the supply chain to ensure the quality of product through refrigeration.

The value of meat processing in Australia was more than \$10 billion in 2013-14, with more than \$7 billion in meat exports.

**Figure 6. Illustrative Locations of Beef Processing Facilities in Australia**



◆ Location of beef processing facilities

## 5.2. Dairy processing

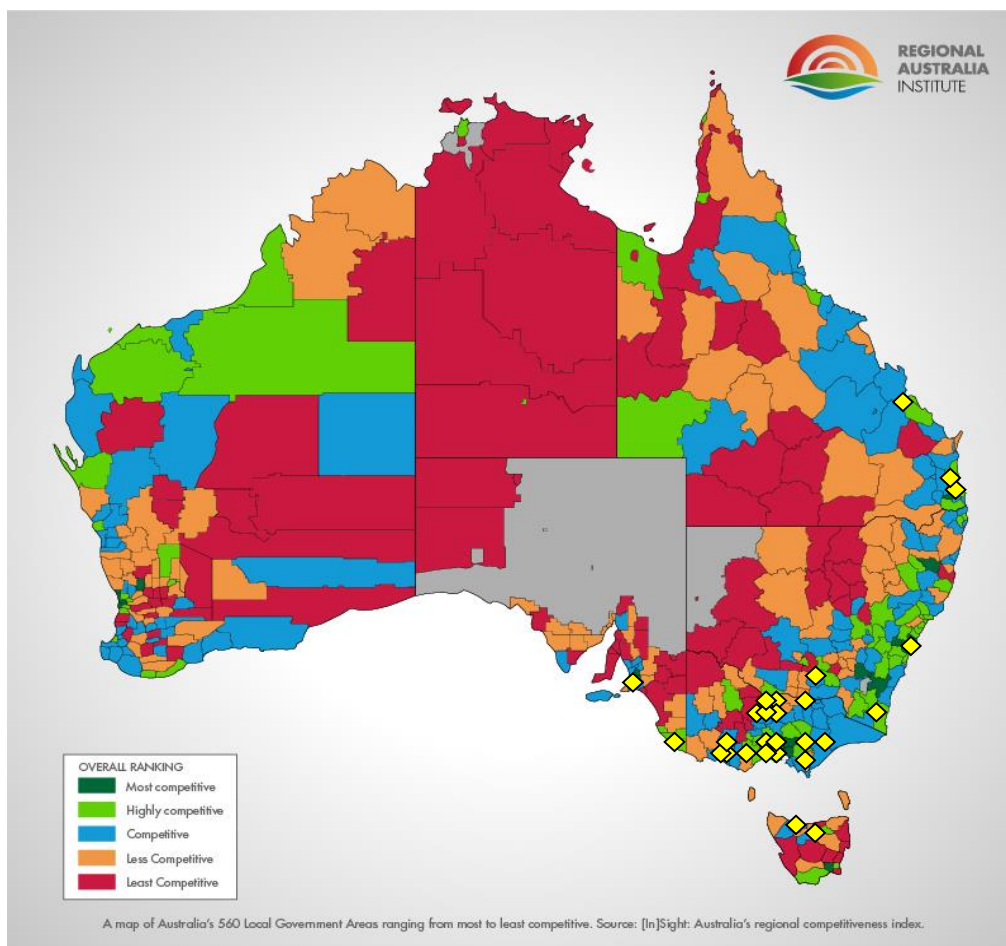
The Australian dairy processing industry is generally concentrated in high rainfall pasture country where dairy cattle are raised and milk is sourced. Some further processing operations are located outside dairy growing regions but broadly, dairy processing facilities are located close to milking sites.

Victoria is a centre of the Australian dairy industry with more than 9,000 of the 16,000 Australia-wide employees located in Victoria. Dairy processing is concentrated across 24 local government areas in Australia with more than 1,300 employees in the Murray region, 1,100 in the Gippsland/Dandenong region, 1,200 in the Barwon region, 600 in the NSW South Coast region, and 500 in North East Tasmania.

The dairy processing industry can be characterised as capital intensive, with a heavy reliance on export markets and therefore supply chain logistics to ensure high quality and timeliness of product delivery.

The value of dairy processing in Australia was more than \$9 billion in 2013-14, with nearly \$3 billion in dairy exports.

**Figure 7. Illustrative Locations of Dairy Processing Facilities in Australia**



◆ Location of dairy processing facilities

### 5.3. Regional solutions

The Regional Australia Institute's 'Regional Competitiveness Index' spans 59 indicators measured across Australia's 560 local government areas, and 55 regional development regions. The maps utilised above highlight the variation in competitiveness across regions with red coloured regions the least and dark green coloured regions the most competitive.

The AFGC Agribusiness Forum has separately reviewed the Institute's competitiveness index for the dairy, sugar, grain, fruit and vegetable, and beef processing industries. The review of specific agribusiness sectors shows that access to and quality of infrastructure, labour market efficiency and the quality of human capital are particularly relevant factors for agribusiness.

While the results vary from region to region, and across agribusiness sectors, there are some consistent findings across more than 100 local government areas. Australian agribusiness:

- is located, and is a large employer, across metropolitan, regional and rural Australia; and
- is a large user of infrastructure given the movement and processing of agricultural commodities across the country.

While often located in areas with strong economic fundamentals, in regional and rural areas agribusiness:

- has variable access to adequate transport infrastructure;
- faces low levels of labour market efficiency and comparatively high labour costs; and
- has relatively poor access to qualified and skilled labour.

## 6. ISSUE 6: IMPROVING THE COMPETITIVENESS OF INPUTS TO THE SUPPLY CHAIN

### 6.1. Highly skilled and trained workforce

The AFGC advocates a more integrated approach to research and training in the Australian Government's tertiary education and innovation policies. Tertiary institutions compete among themselves, including with those overseas, so they optimise their training offerings on that basis, rather than aligning their training with a national strategic agenda.

AFGC has sought to take a leadership role and from January 2012 has supported a Professorship in Food Science and Technology and accompanying student scholarship and industry placement program at the University of Queensland.

Industry supports the continued need for a diverse range of educational opportunities available for both urban and rural communities, ranging from certificates and diploma level training offered through vocational and educational training providers; through to university bachelor degrees in food science and technology.

The delivery of cost-constrained undergraduate food science courses by a variety of universities results in poorly trained graduates that are not work-ready and have little appreciation of real-world requirements. A more strategic approach to consolidate courses and university offerings, and to provide a higher level of funding to produce 'excellence' rather than mediocrity is required.

Much more needs to be done in ensuring that higher level qualifications for masters degree by coursework are also available and affordable for Australian graduates. AFGC understands that the lack of HECS support and the \$50,000 cost of a higher degree, is disadvantaging Australian students.

### 6.2. Energy use within food, beverage and grocery Industry

Energy is essential for manufacturing and transporting food, beverage and grocery products and also for maintaining the quality and safety of food products. Energy in the form of gas, electricity or other fuels is used in various production processes such as drying, sterilisation and baking. Energy is also consumed in processes such as air conditioning and refrigeration for chilled and frozen products, cleaning production processes, storage of products in warehouses and transportation.

ABS data show that agribusiness processors are significant energy users, particularly meat and meat product manufacturing, dairy product manufacturing and sugar manufacturing.<sup>11</sup> Other food and grocery categories that are high energy users include confectionary and paper product manufacturing.<sup>12</sup>

Regardless of the size of the business, rising energy costs are of great concern, particularly given suppliers' limited ability to pass cost increases through to retailers. In particular, the industry is concerned about recent increases in the costs of electricity network charges, the additional cost of the carbon tax and a forecast doubling in the wholesale cost of gas. As the following chart shows, energy costs in the food and beverage manufacturing sector have increased in recent years while industry turnover has

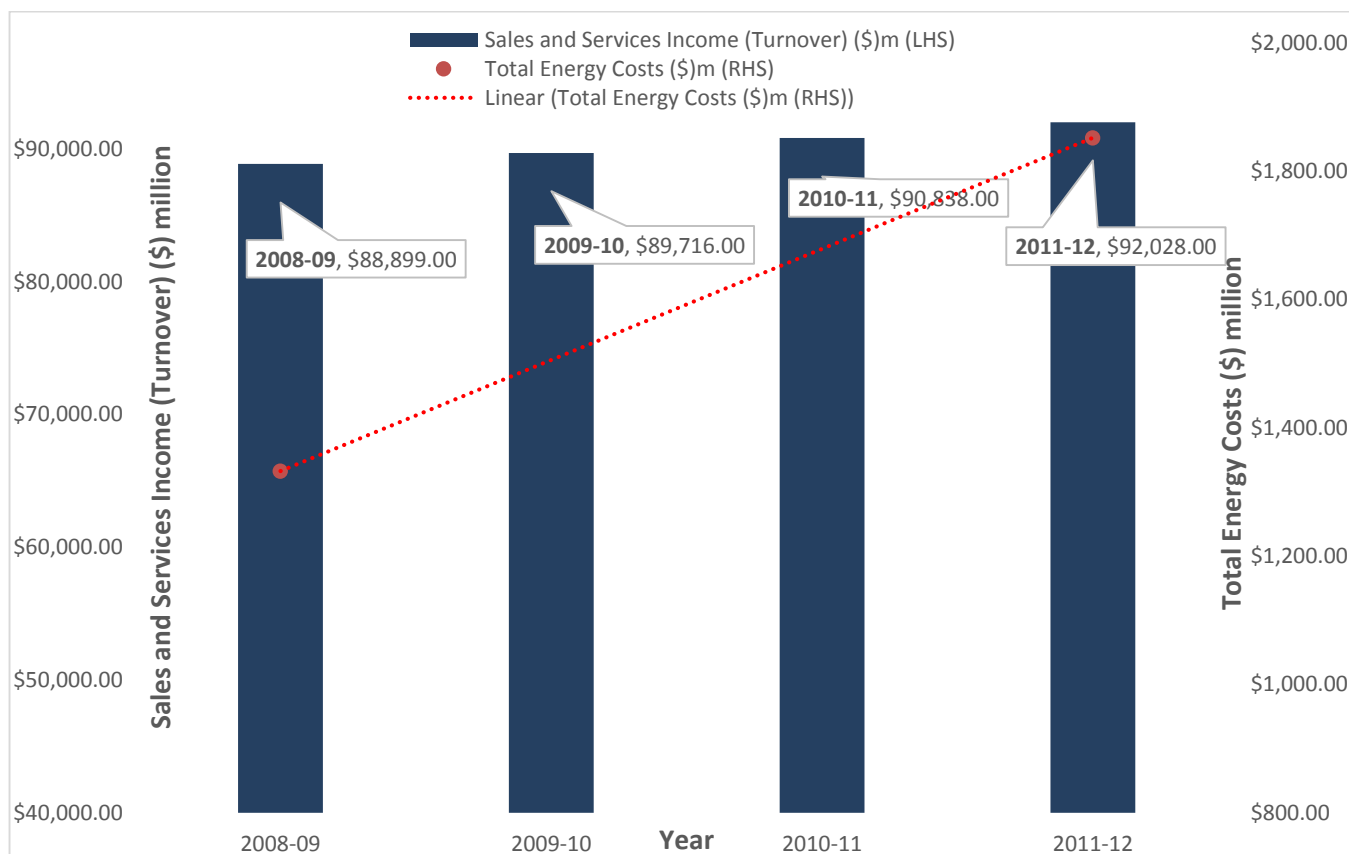
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<sup>11</sup> ABS Catalogue 5209.0.55.001: Australian National Accounts: Input-Output Tables 2009-10

<sup>12</sup> Ibid

remained fairly flat. Total energy costs (including electricity, gas, transport fuel and coal) for the food and beverage manufacturing industry has grown by 39 per cent since 2008-09 compared to its turnover which grew only by 3.5 per cent during the same period.<sup>13</sup>

#### Comparison of energy costs and industry turnover for food and beverage manufacturing<sup>14</sup>



#### 6.2.1. Carbon tax

According to the AFGC's Impact of Carbon Tax Survey conducted in July 2013, about 89 per cent of the respondents experienced increases of up to 10 per cent in their operating costs as a result of the introduction of the carbon tax.<sup>15</sup>

<sup>13</sup> Based on data from ABS Catalogue no. 8155 and 4660 for food, beverage and tobacco product manufacturing. Due to limitations in data, the AFGC has only been able to estimate the direct impact of a gas price increase on the food and beverage manufacturing sector (that is, excluding the impact on the grocery sector and excluding indirect impact on input costs such as packaging). Further, while tobacco is not relevant to the analysis, disaggregated data are not available to remove this product category.

<sup>14</sup> Ibid

<sup>15</sup> AFGC, Impact of Carbon Tax Survey, July 2013 - <http://www.afgc.org.au/tools-guides-.html> (Under general publications section)



The survey found that 67 per cent of respondents were unable to pass through the additional carbon tax costs to customers with a key factor being the non-acceptance of price increases from retailers/consumers. Of those able to pass through some of the additional costs, many companies were only able to pass through a small proportion.

The AFGC welcomes the removal of the carbon tax as a step towards reducing the cost burden on food and grocery manufacturers, which is impeding the industry's competitiveness and viability. The AFGC is concerned that any delay in the passage of the repeal of the carbon tax will add further pressures on the industry and restrain competitiveness and growth.

### 6.2.2. Gas price increase

The Australian Government's Eastern Australian Domestic Gas Market Study estimates that gas prices could more than double over the next few years as LNG exports link domestic gas prices to the more expensive Asian market, domestic supply potentially tightens and producers potentially exercise market power. This transition is unfortunately occurring at a time when existing contracts are due for renewal. Beyond this transitional period, some analysts estimate that wholesale prices will come down slightly, but will still be just under double existing rates.

For indicative purposes, the AFGC has conducted analysis assuming that wholesale gas prices increase from their current level of approximately \$5/GJ to \$11/GJ in the next two to four years, with prices then stabilising at \$9/GJ in the longer term.

Based on this analysis, **the AFGC estimates that the direct impact of rising wholesale gas prices on the food and beverage manufacturing sector alone would be approximately \$170 million *per annum* for the next two to four years (equivalent to 2.3 per cent of operating profit before tax) and over \$110 million *per annum* in the longer term (equivalent to 1.5 per cent of operating profit before tax).**<sup>16</sup>

The direct impact on profitability of food manufacturing alone (i.e. excluding beverages and grocery) will be significantly higher at 4.33 per cent of operating profit before tax in the short term and 2.88 per cent in the longer term.<sup>17</sup>

**The overall impact of rising gas prices would be considerably greater after taking into account the impact on the grocery manufacturing sector and the indirect impacts of a gas price rise on inputs such as packaging.**

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<sup>16</sup> AFGC analysis using BREE (2013), *Australian energy statistics*, Table F; ABS catalogue number 8155 *Australian Industry 2011-12* and based on an existing wholesale gas price of \$5/GJ. Due to limitations in data, the AFGC has only been able to estimate the direct impact of a gas price increase on the food and beverage manufacturing sector (that is, excluding the impact on the grocery sector and excluding indirect impact on input costs such as packaging). Further, while tobacco is not relevant to the analysis, disaggregated data are not available to remove this product category. It is anticipated that excluding tobacco would have the effect of increasing the impact in terms of proportion of operating profit (because gas use in the tobacco industry is likely to be low given product is predominantly imported, yet the profit for the sector is captured).

<sup>17</sup> AFGC analysis using BREE (2013), *Australian energy statistics*, Table F; ABS catalogue number 8155 *Australian Industry 2011-12* based on an existing wholesale gas price of \$5/GJ, increase of \$6/GJ in two to four years and \$9/GJ beyond it.



Once indirect impacts are also considered, it is expected that the near doubling of gas prices will have an impact on the food, beverage and grocery manufacturing sector that is at least equal to the carbon tax, which was estimated to be equivalent to 4.4 percent of operating profit before tax, after taking into account direct and indirect impacts.<sup>18</sup>

**It should be noted that the impact on profitability is an average across the food and beverage manufacturing sector and that certain sub-sectors will face a greater impact on their profitability. This includes gas-intensive agribusinesses such as meat, dairy and sugar and confectionary manufacturing as well as the manufacture of sanitary paper products.**

The AFGC has prepared a separate submission with our views on the impact of the gas price rise and possible policy options. Rather than repeat those comments here, we refer you to our submission to the Australian Government's Eastern Australian Domestic Gas Market Study.

### 6.2.3. Energy efficiency

Rising energy costs have led to significant changes in energy management practices within the food and grocery industry. In addition, various government supported programs such as the Energy Efficiency Opportunities (EEO) program and the Energy Efficiency Information Grants (EEIG) have/ are helping businesses increase their awareness of potential energy savings.

The food processing and manufacturing industry has invested over \$339 million in energy efficiency projects through the CTFFIP, with nearly \$220 million of this contributed by the industry. These projects included improvements to lighting efficiency, upgrading old equipment, installation of solar panels, heat recovery and co-generation facilities.

Despite this high level of investment, the task of energy efficiency is not complete. As indicated by the level of interest in the CTFFIP at the time of closure, there continues to be strong interest from business in incentives to assist business to invest in energy efficiency improvements as a way to mitigate against the impact of high gas and electricity prices and to reduce the industry's carbon footprint. Such programs will improve energy the competitiveness and sustainability of the Australian food, beverage and grocery industry. The AFGC's carbon tax survey found that 61 per cent of the surveyed businesses intend to access capital through government grant programs.<sup>19</sup>

In a review of the EEO program, businesses highlighted "limited availability of capital" and "competition for capital" as major barriers to implementing energy efficiency.<sup>20</sup> Nearly, 35 per cent of the energy efficiency savings in the manufacturing sector do not proceed due to a lack of internal capital and the length of the payback period.<sup>21</sup>

Grant schemes such as the CTFFIP have generated significant uptake from the industry and helped get a business case for investment over the line. In the absence of grant funding, these investments are unlikely to have proceeded.

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<sup>18</sup> AFGC and AT Kearney, Impact of Carbon Pricing 2011: Potential impacts across the supply chain.

<sup>19</sup> AFGC, Impact of Carbon Tax Survey, July 2013

<sup>20</sup> ACIL Tasman, Energy Efficiency Opportunities Program Review Report, 2013

<sup>21</sup> ClimateWorks Australia, Industrial Energy Efficiency Data Analysis, 2013

<http://climateworksaustralia.org/sites/default/files/documents/publications/climatework>

The AFGC notes that it is the Government's intention that the Emissions Reduction Fund will be the mechanism that assists industry to fund energy efficiency projects, through the ability to sell their abatement from these projects. The AFGC is concerned that food, beverage and grocery manufacturers will be unlikely to access the scheme given its complexity; the requirement that projects be ones that would not have proceeded without the grant (i.e. be 'additional', unlike projects funded by CTFFIP); the focus on large scale, low-cost abatement; and the lack of regard for co-benefits such as improving the industry's competitiveness. The AFGC has provided more detail on these issues in its submission in response to the Emissions Reduction Fund Green paper.

The AFGC recommends a nationally consistent approach to energy efficiency based on the following principles:

- focus on improving energy efficiency and achievement of results rather than another compliance/ reporting burden;
- addresses the barriers to energy efficiency by providing assistance for capital investment;
- recognises the co-benefits of improving competitiveness;
- consistent and effectively coordinated across all jurisdictions throughout Australia; and
- encourages innovation and growth within the food, beverage and grocery industry.

### 6.3. Infrastructure

The declining state of Australia's infrastructure is a significant contributor to Australia's falling international competitiveness, as measured by the World Economic Forum (see chart below). Infrastructure planning and delivery needs to deliver supply chain solutions for the agri-food sector. As identified in the previous chapter, Australia's agri-food sector operations stretch the length and breadth of the continent. This creates different infrastructure requirements than single site metropolitan manufacturing facilities or even the often localised operation of mining operations which benefit from high volume infrastructure corridors.

**Figure 7. 2013 WEF Competitiveness Index - Cross Country Comparison**

1' most competitive, '148' least competitive

|   | Australia | Canada | France | Germany | New Zealand | United States |
|---|-----------|--------|--------|---------|-------------|---------------|
| <b>Infrastructure</b>                   |           |        |        |         |             |               |
| Quality of Overall Infrastructure       | 34        | 15     | 6      | 10      | 43          | 19            |
| Quality of Roads                        | 50        | 19     | 2      | 11      | 37          | 18            |
| Quality of Rail Infrastructure          | 33        | 16     | 4      | 7       | 39          | 17            |
| Quality of Port Infrastructure          | 42        | 20     | 25     | 9       | 19          | 16            |
| Quality of Air Transport Infrastructure | 30        | 19     | 10     | 8       | 17          | 18            |

Rail supply chain infrastructure is now critical:

- to support internationally competitive grain exports to over the medium to longer term, as global food demand escalates; and
- to generate operating efficiencies in support of improving returns to the farm gate.

Increased productivity of the grain rail freight network has been identified as the biggest single contributor to increasing the return at the farm gate. Eastern Australia's grain export requires targeted investment in key parts of the existing infrastructure to deliver major efficiency improvements, not a 'shotgun approach' where investment is spread thinly across the entire network.

Rail inefficiency reduces the ability of Australian sourced grain to compete in international markets. While eastern Australia generally enjoys a narrow ocean freight advantage (around \$5.-\$15/tonne) to key export destinations, this advantage is being eroded due to growing rail inefficiencies. For example, a 400km journey for grain shipped in Canada costs approximately \$12/tonne while a similar journey would cost \$40/tonne in New South Wales.

The causes of growing rail inefficiencies are weigh restrictions on branch lines due to underinvestment over many years, and short rail sidings which do not accommodate the length of modern types. The combination of issues means short, under loaded trains are operating well below capacity and increasing cost per tonne of goods transported.

Road infrastructure is critical to all agri-food industries and is usually the first mode of transport for product leaving the farm gate. A modern, efficient and well maintained road network is fundamental to the operation of a modern economy. Given underinvestment in rail over many years, the road network has facilitated much of the growth in the agri-food transport task. Like the situation with the rail network, the need for investment in roads is on targeted projects which support the operation of agri-food facilities in specific locations. The lack of a sealed road to a facility, and roads and bridges unable to carry modern truck configurations are examples of projects requiring attention to improve freight efficiencies to the benefit of the entire supply chain.

There have been recent suggestions that the lack of supporting infrastructure for refrigerated air freight is limiting the export of Australian fresh food. As demand in Asia increases for fresh, premium and safe food it seems inconceivable that we are not able to realise this opportunity due to the lack of an all-weather road or refrigeration capacity.

More broadly, connection to telecommunications, energy, waste and water services are critical for the efficient operation of agri-food facilities. Often the last couple of kilometres to connect a facility to services is the most difficult obstacle with additional challenges with local capacity constraints.

To unlock maximum benefits for growers and the broader industry and economy, infrastructure planning and delivery has to be developed within a holistic supply chain approach which considers the interaction of transport modes for different agricultural and food products; associated mining, passenger and general freight; and the benefits to the broader economy (such as tourism and health industries).

The AFGC acknowledges that funding responsibility for infrastructure is split across Commonwealth, state/territory and local Government jurisdictions. Given agriculture's position as one of the five pillars of the national economy and the unprecedented economic opportunity presented by growing global food demand, the Commonwealth Government has a critical role in leading the response.

#### **6.4. Clear responsibility for food within the Australian Government executive**

Food is a critical part of every Australian's health and wellbeing. Reflecting the important role of food in society, responsibility within government is spread across multiple ministers and departments. Broadly speaking, the Department of Agriculture administers a number of the technical requirements for food production, transport and export, the Department of Industry has general policy responsibility for the sector, and the Department of Health maintains critical engagement on the impact and contribution of food on health. There are a number of government agencies, including Food Standards Australia and New Zealand, which provide technical and policy support for the food industry.

While other sectors face operational requirements from multiple government departments (such as mining companies meeting environmental requirements administered by the Department of Environment) one is hard pressed to find a sector other than food where core business is the responsibility of so many government departments. Acknowledging the role of food in everyday lives it may be unrealistic to propose that a single minister and department be responsible for all food sector issues however a much more reasonable proposition is that a single individual in the Government Executive champions food industry policy.

The AFGC has previously advocated for a Parliamentary Secretary to the Prime Minister to have responsibility for co-ordination of food sector policy. There are credible arguments for the Minister for Agriculture to lead the entire agri-food supply chain, and for the Minister for Industry to drive food industry policy as part of economy-wide industry strategy. Wherever the responsibility falls, sufficient authority and accountability must be provided to drive through the reforms required to turn around Australia's competitiveness.

## 7. ISSUE 7: REDUCING INEFFECTIVE REGULATIONS

### 7.1. General agribusiness and manufacturing perspectives

The food and grocery manufacturing sector is vital to Australia's economic growth, regional trade, rural and regional employment and social fabric. It is of serious concern that a recent Deloitte Access Economics (DAE) report <sup>22</sup> commissioned by AFGC describes the sector as having “*one of the poorest examples of industry regulation in Australia*”: duplicative, cumbersome, burdensome, driving unclear policy agendas, in numerous cases without any scientific basis to match regulation with outcomes.

The Australian food and grocery manufacturing sector is a highly competitive, trade-exposed sector facing significant challenges from a high Australian dollar, retail price deflation, comparatively high labour and energy costs and over-regulation that discourages investment and innovation. The reform of food and grocery regulation can deliver significant benefits and savings to both the Commonwealth Government and to the food and grocery industry, as well as drive growth. The good news is the industry's resilience and ability to capitalise on reform: economic modelling in the DAE Report demonstrates that the removal of \$100 million in regulatory costs will generate an increase of around \$240 million in GDP and create around 220 new jobs. A separate DAE Report identifies agribusiness as one of five potential boom sectors for Australia's post-mining economy.<sup>23</sup>

The food and grocery industry supports appropriate, best-practice regulation which enhances the competitiveness and growth of the sector, and provides a clear point of differentiation in export markets. Current regulation, in contrast, reflects a risk averse and controlling culture, based on a multitude of ideological policy agendas that has transformed the industry from a world-leading innovator into a late adopter of imported technology. This is reflected in the dramatic fall in Australia's ranking in the World Economic Forum's Competitiveness Index.

The Australian Government has policies and programs to ensure that it spends its money wisely, targeting functions that it can deliver better than industry and state/territory governments, and ensuring that in these key areas, programs are delivered efficiently and effectively. Some States, notably Victoria, have in place similar policies. The AFGC strongly supports these commitments to deregulation and regulatory review.

The need for such policies is clearly stated in the World Economic Forum Global Competitiveness Report 2013-14<sup>24</sup>, which describes the current Australian business environment based on a mix of industry surveys and independent data –

*“This edition marks the first time that Australia (21st, down one) exits the top 20 and is overtaken by New Zealand (18th), which jumps five places. Australia delivers a consistent—and essentially unchanged—performance across the board, the highlight of which is its 7th rank in the financial market development pillar, the only pillar where it features in the top 10. The country also earns very good marks for higher education and training, placing 15th. Australia's favorable macroeconomic situation is improving further (25th, up one place). Its budget deficit*

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<sup>22</sup> *Reforming regulation of the Australian food and Grocery Sector*, Deloitte Access Economics, 28 October 2013

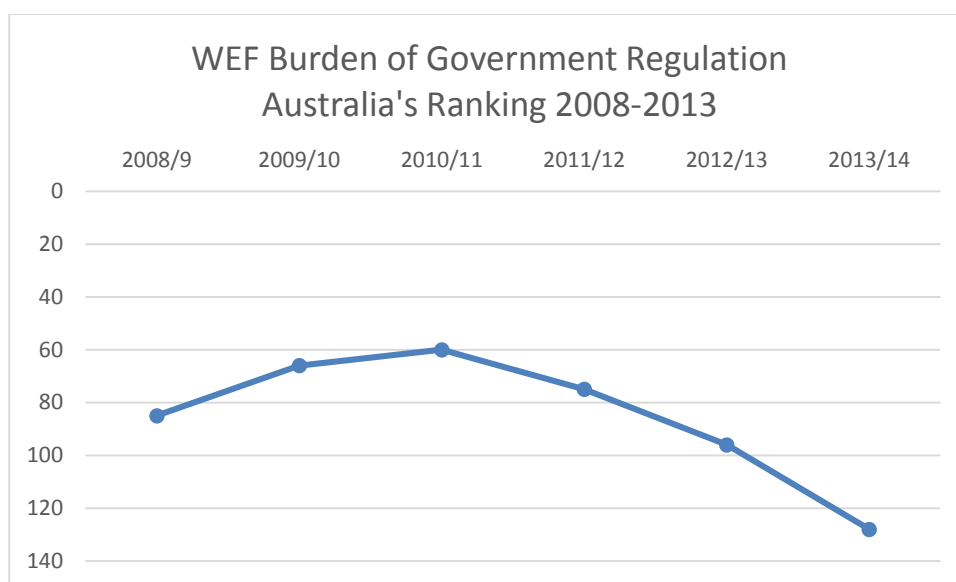
<sup>23</sup> *Building the Lucky Country#3: Positioning for prosperity? Catching the next wave*, Deloitte Access Economics, October 2013

<sup>24</sup> [http://www3.weforum.org/docs/WEF\\_GlobalCompetitivenessReport\\_2013-14.pdf](http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2013-14.pdf)

*was reduced in 2012 and inflation brought to under 2 percent, while the public debt-to-GDP ratio, though on the rise, is the third lowest among advanced economies, behind only Estonia and Luxembourg. The main area of concern for Australia is the rigidity of its labor market (54th, down 12), where the situation has deteriorated further. Australia ranks 137th for the rigidity of the hiring and firing practices and 135th for the rigidity of wage setting. The quality of Australia's public institutions is excellent except when it comes to the burden of government regulation, where **the country ranks a poor 128th. Indeed, the business community cites labor regulations and bureaucratic red tape as being, respectively, the first and second most problematic factor for doing business in their country.***

If Australia's WEF ranking on the burden of government regulation is tracked over the past 6 years, it shows an alarming picture that highlights the urgent need for reform.

**Figure 8. Burden of Government Regulation**



In relation to the White Paper, the need for reform can be targeted to some specific issues as described below.

## 7.2. Australia, state and territory government overlap

The *Australian Constitution* does not confer direct power on the Australian Government to legislate or act executively in relation to food, agriculture or business generally. This means that national policy requires cooperation and implementation by state and territory governments, leading to a multiplicity of regulators and agencies.

While this multiplicity is to an extent unavoidable under the Constitution, the reality experienced by the regulated business is one of competing or conflicting policies, communicated by different people each of whom claims to be “from the government”. The use of agricultural and veterinary chemicals, for example, may require Australian Government approvals to import and register (by the Australian Pesticides and Veterinary Medicines Authority (APVMA)), state and territory approvals to use (under Poisons legislation)



and both Australian and state/territory government approvals (under Food Standards arrangements) in relation to crop residues. Further, different jurisdictions have different rules for “off label use” and none make allowances for spray drift or very low levels of incidental residue.

The need is to simplify and unify, bringing all approvals into a single point of contact that can deliver uniform and consistent policy.

Another example of the perils of Commonwealth and state/territory overlap can be found in the inter-Governmental arrangements for approving food standards. These arrangements provide for a Commonwealth, New Zealand and state/territory Ministerial Council, known as FoFR, consisting predominantly of Health Ministers. Current voting arrangements of the FoFR assign one vote to each jurisdiction, such that the Australian Capital Territory, with minimal food growing and manufacturing industry, has an equal vote to a major food producing state such as Victoria, and an equal vote indeed to the Commonwealth and New Zealand. Further, the health portfolio focus of FoFR makes it a conservative decision maker, including in relation to matters such as residue limits that are primarily issues of agricultural best practice. Reform of the food standards system remains a high priority for the agribusiness industry.

### **7.3. Commonwealth agency overlap and maximum residue limits**

Current regulatory arrangements see Food Standards Australia New Zealand (FSANZ) set maximum residue limits for imported foods, while the APVMA sets residue limits for domestic foods. Both are reflected in one document (Food Standard 1.4.2) that is enforced by state and territory officials.

Maximum residue limits are established to reflect good agricultural practice, meaning that use is limited to the least amount of pesticide or medicine necessary to achieve the intended purpose. In the vast majority of cases, there is no safety concern in question – the residues are expressed in very small amounts such as parts per million – the only issue is proper agricultural and animal husbandry practice.

With this in mind, it is reasonable to expect that different countries, with different climates and different pests and diseases, will set different rules as to what may, or may not, be used, and to this extent it is not unreasonable to set different rules for imported and domestic goods – there are even international standards that deal with residues in internationally traded commodities. The problem that arises where the differing agencies seek to set MRLs for the same chemical used on the same crop (leaving to one side the problem of restricting chemical use to single target crops). In such an instance, where the imported residue level is higher than the Australian one, the imported residue level is said by APVMA to not reflect Australian conditions, while FSANZ is in the position of seeking to allow the imported residue level so as to avoid imposing a non-tariff trade barrier (again in circumstances where there is no significant risk to public safety).

The situation is compounded by the so-called “nil tolerance” for residues, whether presence of astonishingly small levels of a chemical renders a food illegal in the absence of a specific allowance for the specific chemical in the specific food. Such pedantry ignores the efficiency of aerial spraying, wind draft, or other mechanisms for low level incidental transference of chemicals.

Bearing in mind that the activities of APVMA are cost-recovered from industry, a further issue in relation to MRLs lies in the structure of regulation where approvals are granted in relation to a specific crop (e.g. passionfruit) but a separate application is needed to approve the same chemical, at the same level of application and residue, in a closely related crop (e.g. kiwifruit), even though the same pest may be

targeted. Application costs to industry could be decreased, and regulatory efficiency increased, if permissions were granted in relation to target pests rather than target crops.

#### 7.4. Environmental reporting compliance costs

Agribusiness companies face considerable compliance costs associated with environmental reporting under various schemes at Commonwealth and state and territory level. These programs are spread across energy, water and waste.

In common with other manufacturing industries the food and agribusiness sector must report against a number of energy schemes including:

- National Greenhouse and Energy Reporting (NGER) Scheme - Commonwealth
- Energy Efficiency Opportunities (EEO) - Commonwealth
- National Pollution Inventory (NPI) - Commonwealth
- Energy Savings Action Plan - NSW
- Environment and Resource Efficiency Plan (EREP) - VIC

It is clear that there is a degree of duplication across these schemes in their objectives and also their reporting requirements. Whilst companies may package the same data in different ways for each of the schemes, it is still the case that the overall reporting burden is greater than it need be.

Industry is required to report water usage and water quality parameters under different state and Territory initiatives to the following Government agencies:

- Environment and Resource Efficiency Plan (EREP) - VIC
- ongoing Water Efficiency Management Plans (WEMP) - QLD & WA
- Water Savings Action Plans - NSW
- water management action plan (waterMAP) - VIC

In addition water discharge reports are required by:

- State Environmental Protection Agencies, as part of environmental license requirement; and
- water retailers such as Sydney Water and Yarra Water which require information on parameters such as volume in and out, biological oxygen demand (BOD), total solids and dissolved solids.

The industry is also required to report outputs and disposal of waste to State Environmental Protection Agencies and to initiatives such as:

- Environment and Resource Efficiency Plan (EREP) (VIC); and
- Annual Waste Returns (VIC).



Each of these programs has some individual merit, but the cumulative impact on business is unnecessarily high, contributing to the decline in Australia's competitiveness and perceptions of regulatory burden. The message again is to simplify and unify: industry is as conscious as anyone of the need for energy, water and waste efficiency, it does not need over 15 regulators covering the territory.

### 7.5. Country of origin labelling

The AFGC strongly supports Australian production and manufacture of food and grocery products, both for the domestic market and for export. The sector is Australia's largest manufacturer and a significant employer.

The AFGC is aware that the House of Representatives has instituted an inquiry into country of origin labelling of foods, and that this inquiry will likely be the principal forum for exploration of these issues. For the purposes of this submission, however, it is worthwhile to note that the AFGC considers that consumers see origin as a cypher for many things, including food safety, jobs, profits and community, in addition to a simple expression of ingredient provenance, and that these often remain secondary to the issues of price, habit, quality and availability in driving consumer choice.

The AFGC supports clear consumer labelling including with regard to origin: however, adding complexity will add cost with little evidence of consumer benefit.

### 7.6. Cost recovery

A number of agribusiness regulators (APVMA, FSANZ, NICNAS) are entirely or partly funded through cost recovery, imposed as levies or as application fees. In the past, there has been little policy or practical oversight on the cost recovery processes of these agencies. Now, in contrast, we have the Australian Government Cost Recovery Guidelines and Finance Circular directives from the Department of Finance, together with the more transparent cost recovery impact statement process.

Industry welcomes the improved administration in this respect, which for the present appears sufficient to address prior industry concerns. Individual concerns in relation to specific instances of cost recovery can be taken up directly with the agency in question.

The broader question that remains is the extent to which the public good aspects of regulation need to be publicly funded. In the case, for example, of NICNAS there is a significant public safety and environment protection function served by the regulation of industrial chemicals, but the agency remains fully funded by industry levy with little incentive to operate efficiently, and without the strictures of efficiency dividends faced by other Commonwealth agencies. It is in relation to such agencies that some continued cost recovery reform is needed.

### 7.7. Regulation Impact Summary

The AFGC welcomes the new focus by the Australian Government on deregulation, reducing regulatory burden and discipline in considering new regulatory measures. This focus must continue, and indeed spread to state/territory governments and especially extend to inter-governmental creations that typically avoid scrutiny. The opportunity for growth embodied in the reduction of regulatory burden is integral to Australia's future and to any serious policy on Australia's agricultural environment.

## 8. ISSUE 8: ENHANCING AGRICULTURAL EXPORTS

Agri-food exports are critical to the future of the Australian agriculture, agribusiness, and food processing industries. Approximately 60 per cent of Australia's agricultural production is exported and the increasing global trend for processed and protein-rich foods will require greater collaboration and value adding in Australia's food supply chain.

The AFGC encourages the Australian Government to continue to pursue a multilateral trade deal in the World Trade Organisation (WTO), as this presents the best opportunity for trade liberalisation and economic gains for all countries. In addition, the WTO is the only forum where export subsidies and domestic subsidies are addressed: a priority for the Australian processed food and agribusiness industries, which are often at a disadvantage compared to competitors that provide subsidies to their domestic industries. The removal of domestic and export subsidies is vital to free and fair trade in food products.

### 8.1. Conclusion of negotiations with China, Japan, Korea and Trans-Pacific Partnership countries

Given slow progress in multilateral trade negotiations, and the proliferation of free trade agreements (FTAs) around the world, it is essential that Australia prosecutes an expansive FTA agenda, otherwise we risk further disadvantage compared to our competitors. Australian exporters need access to long term growth markets in Asia while maintaining access to mature, high value markets around the world.

The AFGC welcomes conclusion of negotiations with Japan and Korea, and looks forward to timely implementation of those agreements. The immediate priority for the Australian food and grocery industry is now conclusion of the China free trade agreements negotiations with substantive and commercially relevant outcomes for industry. The Trans-Pacific Partnership is also a key priority to secure a high quality agreement with some of our largest trading partners.

Individually, the respective negotiations cover many of Australia's most significant trading partners, and collectively, represent a majority of Australia's international trade. Improved market access through the removal of tariffs and other barriers, and stronger rules which improve the predictability and stability of trade, will strengthen Australia's food and grocery sector.

### 8.2. Increased focus on semi-processed and processed food

AFGC considers it imperative that all aspects of Australia's trade policy – including trade facilitation, liberalisation and promotion – include a focus on semi-processed and processed food products in addition to agricultural products.

The rising population as well as the increasing change and 'westernisation' of diets in Asia (namely more processed and packaged food for the time-poor middle class) creates an opportunity for Australia's processed food products. In 2012, the Centre for International Economics (CIE) estimated that the greatest potential gains for agriculture and processing/manufacturing will flow from increased export demand. More specifically, the CIE estimated that a 1 per cent increase in export demand would lead to an increase of \$246 million in farming value added, and \$418 million in processing/manufacturing value added.

Australia has a strong advantage and reputation in food safety and quality with supply chain assurance in processed food. Moving Australian food exports up the supply chain means more value-add in Australia – more jobs, income and benefit to Australia. In addition, there could be flow on benefits, such as increased farmer returns, if the supply chain focuses on producing premium Australian processed food products.

### **8.3. Commercial outcomes required**

The AFGC considers it essential that new FTAs deliver a change to the trade framework which leads to an increase in trade. It is inadequate to achieve reductions in tariffs but the retention of other barriers that continue to block access for Australian food products.

Where Australia's global competitors secure improved market access through FTAs this can disadvantage Australian exporters, particularly in traditional markets. The reality for Australian exporters is they are fighting an uphill battle if their international competitors gain preferential market access under an FTA. Relevant examples where Australia is at a disadvantage relative to our competitors include access for: US beef into Korea under the US-Korea FTA, New Zealand dairy into China under the NZ-China FTA, and New Zealand processed food into China (with most relevant tariffs eliminated by 2013).

It is essential that Australia's FTAs provide Australian processed food and agribusiness industries with at least the same access as our international competitors in these and other markets. This is even more critical given the disadvantage that Australia faces from a strong currency.

Before finalising any trade agreements, it is essential that the Australian Government assess whether the arrangements will provide commercial outcomes for the processed food and agribusiness industries.

### **8.4. Maximise trade under current arrangements**

There is a need for industry and Government to work together to communicate the opportunities to individual businesses and maximize the gains from existing trade arrangements. Over the years there have been examples of specific markets opening outside trade negotiations and agreements. Recently, significant and coordinated industry and government efforts led to new Australian sheep meat exports to India. The processed food and agribusiness industry need to work with the Australian Government to identify areas of demand for Australian food products.

Communicating the outcomes of FTAs and the opportunities to Australian exporters is critically important. While the tariff reductions under the Thailand-Australia Free Trade Agreement have led to an increase in exports to Thailand for specific food companies, in some cases this was by chance rather than specifically targeting this market because of the FTA. There are likely to be many businesses unaware of the opportunities that exist under FTAs.

### **8.5. Domestic policy reform**

Australia has a strong history of unilateral reform and trade liberalisation which has contributed to the success of Australia today. As a trade-reliant economy, Australia's continued success is based on an economy open to trade, with government policy and regulation supporting internationally competitive industries. Protected sectors within the economy create inefficiencies which create costs across the entire economy.

The AFGC supports government policies that open Australia's economy. There needs to be a renewed process of domestic policy reform that tackles the significant cost pressures in the Australian economy, including excessive regulation, high energy costs and the inflexibility of the labour market.

Without trade liberalisation and domestic policy reform, there is a risk of the Australian food processing sector losing its competitiveness, further factory closures and increased offshoring of food processing, with flow on impacts for the agricultural, plastics, chemical and other important sectors of the Australian economy.

## 8.6. Trade facilitation and promotion

The Australian Government has an important role in facilitating Australian exporter's engagement with export markets. This is particularly important for small and medium sized enterprises making first contact with a potential export market. Austrade, DAFF agriculture counsellors, and DFAT economic representatives are critical elements of Government facilitation of Australia's exports and hence adequate resourcing of these activities is essential.

With state governments also involved in trade facilitation and promotion activities it is essential that there is improved coordination between all jurisdictions of government, for example maximising the exposure that inbound trade missions have to the breadth of suppliers in Australia.

AFGC considers an opportunity exists to drive food exports into Asia based on leveraging some particular Australian value propositions, such as:

- provenance – unique, remote and pristine food production areas. With a growing number of visitors from Asia the opportunity to leverage the tourism experience of overseas visitors is substantial. Offering tourists the opportunity when they return home to buy the same products and brands from their local supermarket they experience in Australia adds to the overall experience and 'buy in' to Australia;
- premium quality – quality ingredients and advanced manufacturing technologies. By using the best technologies across production, manufacturing and in the supply chain Australian products tweaked to appeal to the Asian palate[s] should become synonymous with 'premium quality', and so command a higher price in the market ;
- assured safety – best regulatory system in the world – government certification. Food safety and food adulteration issues are becoming more of an issue, including in Asia. Australian food enjoys a reputation of being very safe, and very well regulated. This reputation can be leveraged to further enhance the value proposition of Australian food products; and
- environmentally sustainable – low impact, highly efficient agriculture and manufacturing. From production through to all stages of manufacturing Australian should leverage is efficiency and drive towards low impact environmentally sustainable food production.

The AFGC supports the work underway by Austrade to develop a national food brand and a strategy for coordinated promotional activities by federal and state government agencies. The AFGC recommends that the national food brand 'Trust Australia' be adopted, with the sub-messaging 'Trust, discover, be tantalised' (see page Section 4.3 on page 22).

The AFGC welcomes and supports recent initiatives to better understand food demand in Asia. The AFGC is working with the Australian Government to conduct research on the opportunities and the relevant capabilities of Australian industry.

Recent reports by government agencies on agri-food demand in Asia have focussed on the demand for agricultural commodities. We need to ensure that the export opportunities for processed food are also a focus for Government and that the particular requirements for individual markets are better understood.

Meeting the rising food demand in Asia will require much broader and deeper connections between industry and government. With Australia's food and agribusiness exports often concentrated in a few markets, disruptions to trade highlight the risks associated with high levels of concentration in export markets. Industry will continue to work closely with governments to identify, develop and maintain new and diverse export markets and opportunities.

## 9. ISSUE 9: ASSESSING THE EFFECTIVENESS OF INCENTIVES FOR INVESTMENT AND JOB CREATION

### 9.1. Incentives for job creation

Incentives for job creation are an important consideration for employment in the agri-food sector however the national employment framework is the primary factor influencing sector employment. A review of Australia's international position provides useful insights on Australia's labour market trends.

The World Economic Forum's Competitiveness Ranking for Australia's overall labour market efficiency fell from 42<sup>nd</sup> place in 2012 to 54<sup>th</sup> place in 2013 (out of 148 countries). Similarly, Australia fell from 25<sup>th</sup> place to 37<sup>th</sup> place (out of 60 countries) in the IMD Competitiveness Center rankings.

On specific labour market criteria in the WEF Competitiveness Ranking, Australia has fallen from:

- 67th to 103rd on the cooperation in labor-employer relations,
- 123rd to 135th on the flexibility of wage determination,
- 120th to 137th on hiring and firing practices, and
- 80th to 113th on pay and productivity.

As highlighted below, the falls in Australia's labour market competitiveness leaves us lagging our key competitors. There is a long term policy imperative to establish a labour market framework in Australia which allows us to compete internationally, and maintain business operations and employment in Australia.

**Figure 9. 2013 WEF Competitiveness Index - Cross Country Comparison**  
'1' most competitive, '148' least competitive

|  | Australia | Canada | France | Germany | New Zealand | United States |
|--|-----------|--------|--------|---------|-------------|---------------|
| <b>Labour Market Efficiency</b>          |           |        |        |         |             |               |
| Cooperation in labour employer relations | 103       | 31     | 135    | 18      | 11          | 42            |
| Flexibility of wage determination        | 135       | 30     | 75     | 141     | 10          | 29            |
| Hiring and Firing Practices              | 137       | 16     | 144    | 118     | 61          | 9             |
| Effect of taxation on incentive to work  | 59        | 28     | 127    | 64      | 13          | 38            |
| Pay and productivity                     | 113       | 28     | 78     | 42      | 16          | 12            |
| Country capacity to retain talent        | 37        | 19     | 57     | 9       | 79          | 4             |

## 9.2. Incentives for Investment

As previously discussed, there are tremendous growth opportunities for the Australian agricultural and agri-food processing sectors as a result of a growing global middle class. In order to capitalise on these export opportunities and compete against imports, there is a need for a step change in investment in the Australian agri-food processing sector. However, the sectors' ability to invest for growth is hamstrung by the dual impacts of short term domestic and global economic conditions, and a tough domestic retail environment, which have eroded profitability and constrain the ability and confidence to invest.

Broad investment in Australia's mining and energy sectors led to a strong Australia economy through the global financial crisis and subsequent difficult global trading conditions. The new level of investment in Australia's minerals and energy sector will support Australia's exports and prosperity for decades to come.

However, the mining boom has contributed to a period of structural change in the economy through its impact on the exchange rate, wages growth and an increase in the cost of inputs such as energy. The resulting structural change has been particularly hard for labour intensive and trade exposed industries, such as agri-food processing.

At the same time, the structure of the Australian retail market has meant that there is significant pressure on the industry's margins from retailers, with profitability of Australian food and grocery manufacturers now significantly lower than international comparators.

The AFGC and KPMG recently released a report, Competitiveness and Sustainable Growth, which shows that that Australia's food processing industry has focused its efforts on cost reduction, productivity improvements and business re-engineering. A significant increase in trade spend (6.4 per cent annual growth) to fund retail price discounting has not increased sales volume but has come at the expense of profitability (6 per cent annual decline) and suppliers' marketing and R & D spend which may have a long term impact on growth, sustainability and innovation.

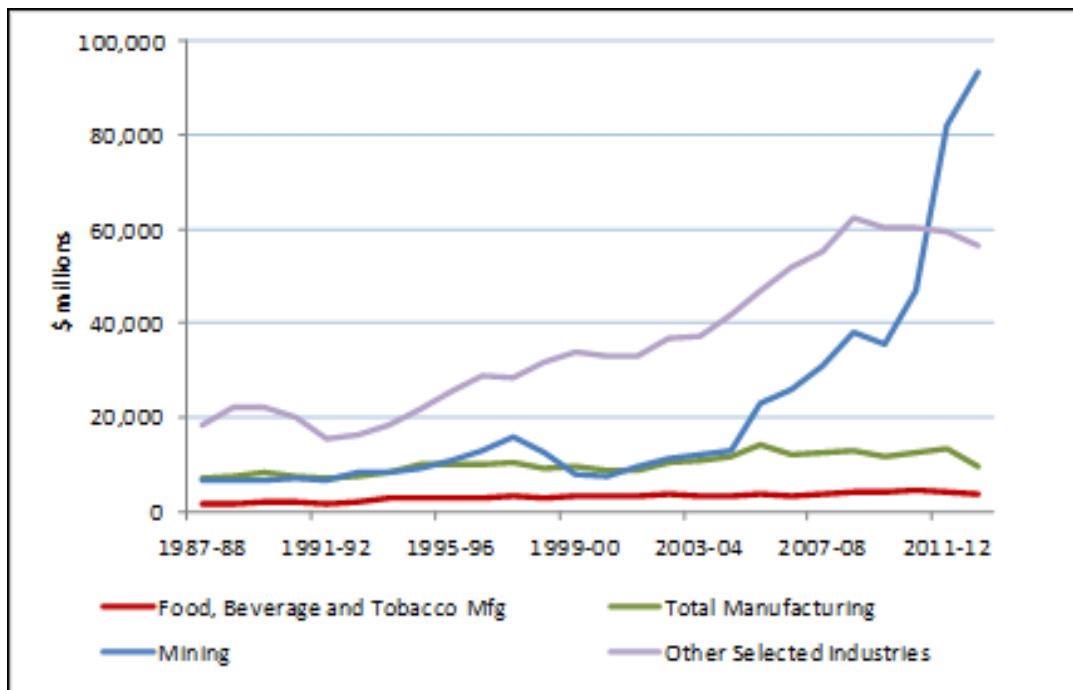
As a result of these domestic and global factors, the food manufacturing industry is facing continued pressure. Manufacturers are taking measures to contain costs and preserve margins, including capacity rationalisation and exploring new channels to market. However, the combination of rising input costs, reducing prices and an increase in low cost imports has negatively impacted profitability, reducing the attractiveness for further investment in the value added food manufacturing sector in Australia.

As Figure 10 shows, total investment (i.e. fixed plus financial capital) in the food, beverage and tobacco manufacturing sector has been relatively flat over the past 10 years, with the amount spent on investment in 2011-12 at an almost identical level as that spent in 2002-3. While there has been recent growth in capital investment in food processing, it is only a regaining of ground lost during the financial crisis and is generally focussed on the replacement of assets rather than investments that are aimed at growth.

In stark contrast, the level of mining investment has increased in nearly every year since 1987-88 (with slight dips in 1999-00 and 2009-10), with the level of mining investment in 2011-12 at eight times (or 800%) its 2002-3 level.



**Figure 10. Total Investment in Industry Sectors**



Source: Australian Bureau of Statistics, *Private New Capital Expenditure and Expected Expenditure, Australia, Dec 2013*, Catalogue no. 5625, March 2014; and estimates.

Note: the ABS defines Other Selected Industries as all other industries except finance and insurance services.

To stimulate growth in the agri-food processing sector, at a time when economic and retail market conditions risk losing opportunities, requires policies that improve Australia's cost competitiveness and encourage a significant step change investment in agri-food processing sectors.

The first step to improve Australia's investment environment is to finalise cost cutting reforms currently underway, such as removal of the carbon tax and substantive deregulation. Over the medium term, economic reform is required coupled with new investment in infrastructure. Most importantly, tax and labour market reform is required over the long term to turn around Australia's falling competitiveness.

In terms of taxation reform, the AFGC considers there is a need for a package of measures that encourages investment:

- R&D tax incentive to promote innovation in products, packaging etc. (e.g. to meet needs of foreign markets, to differentiate from private label products);
- investment incentive – to encourage investment in plant and equipment, i.e. to commercialise on the R & D, to increase scale to supply export demand; and
- reduced input costs, such as reduced taxes on input costs (payroll) etc. – to improve Australia's competitive position compared to our trading partners.

The AFGC recommends consideration of these issues in the Governments review of the R&D tax incentive and the Taxation White paper.

## 10. CONCLUSION

The future profitability and growth of Australia's agricultural, agribusiness and food processing sectors are intrinsically linked and are contingent on three main factors:

- global food demand;
- Australian industry capability; and
- a supportive policy environment.

The AFGC believes that the first two of these factors is in place however urgent action is needed to construct a policy environment that is conducive to, rather than hampers, competitiveness and growth.

The enormous opportunities for Australian agriculture, agribusiness and food industries presented by rising global demand have been well documented. Increasing populations in developing countries, coupled with rising incomes, are a source of unprecedented global food demand that could deliver higher returns to the entire value chain, including farmers, and regional and rural communities.

The Australian agri-food sector has a strong foundation of comparative advantage, productivity and innovation. The Australian agriculture sector has exported agricultural products around the globe despite variable climatic conditions and an uneven playing field competing against subsidised products and trade barriers in all export markets. The Australian agribusiness and food manufacturing industry has sophisticated food manufacturing capabilities with strong safety and quality systems, under the oversight of an advanced food regulatory system. The quality assurance and safety credentials of Australian processed food are sought by health and safety conscious consumers throughout Asia.

However, despite these positive attributes, the agri-food sector is at risk of continuing to lose our market share because of a decline in the competitiveness of the Australian economy, across factors beyond the control of individual businesses.

With a large island continent and a small population, Australia has always faced a number of international competitiveness issues that have posed challenges for policy makers. Australia's fall in the international competitiveness rankings are not due to those factors but are instead due to increased regulation, inflexible labour arrangements and a decline in the quality of Australia's infrastructure.

Urgent changes in government policy are required to reverse Australia's declining competitiveness and enable industry to take advantage of the unprecedented global opportunities available. As highlighted throughout the submission, immediate action is required on trade, promotion, investment, infrastructure, competitiveness and innovation.

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