

Safeguards Inquiry into the Import of Pigmeat: Submission to the Productivity Commission

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Prepared by



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1 Introduction

1.1 Safeguards Inquiry into the Import of Pigmeat

This is a submission by B.E. Campbell (NSW) Pty Ltd (B.E. Campbell) to the Productivity Commission's (the Commission) safeguards inquiry into the impact of pigmeat imports on the Australian pork industry. The inquiry relates to imports of frozen pigmeat, under Australian Customs Tariff Code 0203.29.

Safeguard action is defined as *'emergency action, taken where a surge of imports causes or threatens to cause, serious material injury to a domestic industry. It allows a country to respond to unexpected and unforeseen increased imports which have caused serious material injury. Imports must be recent enough, sudden enough, sharp enough and significant enough.'*

Specifically, the Commission has asked that submissions address at least one of the following questions:

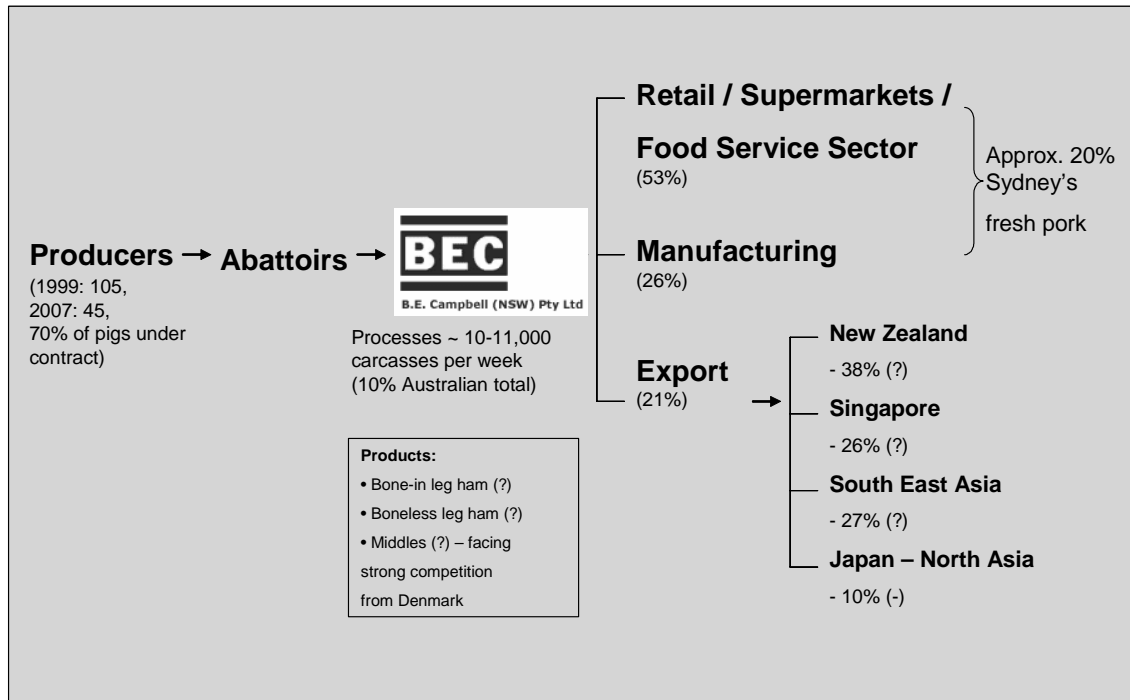
1. Have imports increased?
2. Was the increase in imports the result of unforeseen developments and the result of [WTO] obligations incurred?
3. Defining the industry: who are the producers of 'like' or 'directly competitive' goods?
4. Has the industry suffered, or is it likely to suffer, serious injury?
5. Are increased imports causing serious injury?
6. What safeguard measures would remedy serious injury?
7. What are the impacts on other parties?

This submission addresses questions 3-5. In examining these issues question 7 has also been addressed as we have extensive contact with participants in the supply chain.

1.2 B.E. Campbell (NSW) Pty Ltd

- B. E. Campbell has been operating since 1969
- The company is one of the largest pork processors in Australia and the largest processor that is not aligned with a small goods company
- An outline of B.E. Campbell's supply chain is shown in Figure 1.

Figure 1 B.E. Campbell supply chain

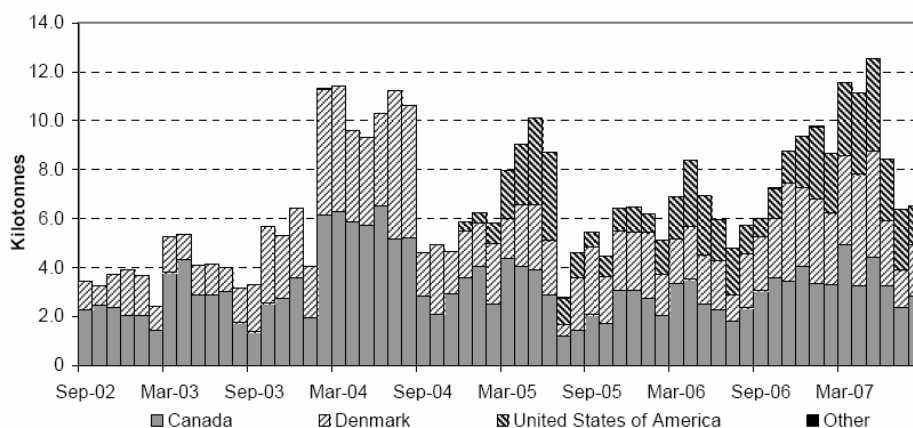


- We have a throughput of 10,000 - 11,000 pigs per week (around 10% of total pigs processed in Australia)
- We source pigs from QAF (Corowa) and growers throughout SA, NSW, Victoria and Qld
- Pigs are slaughtered at Young and Booyong in NSW, Toowoomba and Kingaroy in Qld, and Murray Bridge in SA (part-owner of this)
- Our company supplies several market segments including supermarkets, restaurants and clubs, foodservice industry, butchers, smallgoods manufacturers, and export markets (Japan, New Zealand, Singapore, South Korea, Taiwan, Thailand, Malaysia, Philippines, Hong Kong/China and Pacific Islands)
- Over 50% of the company's output goes to the supermarket/retail and food service segments
- We estimate that we supply approximately 20% of Sydney's fresh pork market
- Smallgoods manufacturers tend to use imported product, therefore the company has been directing marketing away from these processors and increasing supplies to the domestic market (which has placed pressure on prices)
- Our company has no contracts with buyers, however the company has strong relationships with key retailers.
- We have maintained a strong export commitment and focus.

1.3 Production of 'like for like' goods

- The Productivity Commission has stated that this inquiry relates only to imports of frozen pigmeat falling within tariff subheading 0203.29 of the Australian Customs Tariff.

Monthly imports of pigmeat under tariff subheading 0203.29, by source



Data source: ABS unpublished.

Source: Productivity Commission

Table 1 Imports and B.E. Campbell Production

CODE	IMPORTS	DESCRIPTION	SAMPLE OF ACTUAL PRODUCTS INCLUDED IN THIS CATEGORY	PRODUCED BY BEC
203290045	Boneless Frozen Swine Meat	Meat of swine (excl. boneless leg , middle & shoulder cuts), frozen, boneless	Trimnings 65CL Trimnings 75CL Trimnings 85CL Trimnings Loin Outershank Meat Innershank Meat	✓ ✓ ✓ ✓ ✓ ✓
203290040	Boneless Frozen Swine Meat, leg cuts	Meat of swine, frozen, boneless, leg cuts (excl. salted, dried or smoked ham)	3 Piece Ham Fred Insides Boneless Hams C105 Star fat in Boneless Ham C105 Staff fat out 1/18 th IWP Buck Eyes	✓ ✓ ✓ ✓ ✓
203290041	Boneless Frozen Swine Meat, middle cuts	Meat of swine, frozen, boneless, middle cuts	Boneless Rind On Middles Boneless Rindless Middles Muscle back - Loin Short cut backs – Loin	✓ ✓ ✓ ✓
203290042	Boneless Frozen Swine Meat, shoulder cuts	Meat of swine, frozen, boneless, shoulder cuts	Boneless Picnic Shoulder 80CL Boneless Picnic Shoulder 90CL	✓ ✓

- Frozen pigmeat imports tend to be sourced from Canada, the US and Denmark.
- Imported cuts include boneless leg hams and boneless middles.
- Like for like products are defined as *products that are 'identical'; that is, 'alike in all respects ... or in the absence of such a product, another product which ... has characteristics closely resembling those of the product under consideration'*.
- Our products and those of our sources are directly competing with these imports.
- The impacts of this competition across our supply chain are discussed in the next section.

2 Impact of Pigmeat Imports

2.1 Introduction

- The injury that the industry has experienced, and continues to face, is being directly caused by the high volume of imports entering Australia.
- We recognise that other factors influence the performance of the industry, however the most significant impact has come from imports.

2.2 Other factors impacting the industry and our business

- The macro-economy is performing relatively well (high employment, high growth)
- The appreciating A\$ is making imports relatively cheap and Australian pork exports less competitive in global markets. However, shipments to Singapore have not fallen significantly (due to cheap freight costs and market relationships), therefore exporters have not come under too much pressure.
- The industry has managed other droughts in the past. Pigmeat inventories were already high before the drought, due to the volume of imports flooding the market.
- Consumer preferences are not having a negative impact on the industry; rather the consumption of fresh pork is actually increasing.
- The industry acknowledges that consistency is not as good as it could be. This is a function of the scale of the industry. However, industry is addressing this issue, e.g. by investing in new carcass testing technology. Five of the major abattoirs are upgrading technology to improve consistency of output.
- Rising grain prices have been increasing producers' production costs (with the largest impact felt in August/September of this year), however inventories were already significant before high grain prices

2.3 Direct causation

- We believe that increased imports have caused serious injury to the domestic pork industry and this impact may have long term ramifications for the industry over the next 6-12 months. These impacts are addressed specifically in the next section.

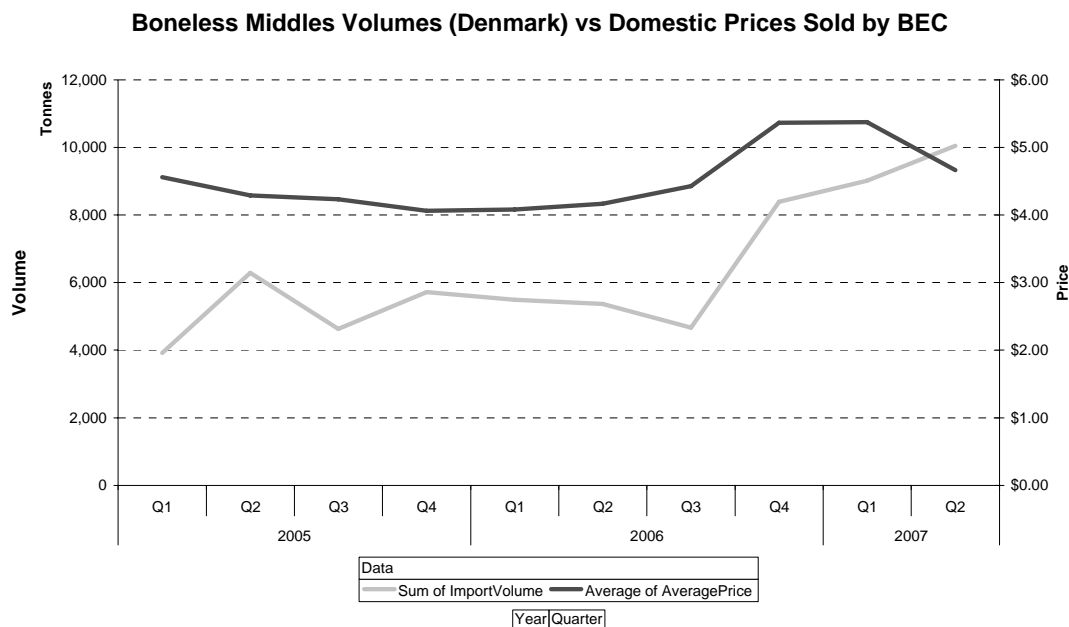
2.4 Impact on B.E. Campbell's business

- B.E. Campbell is a producer of goods that are 'like' or 'directly competitive' with imported pig meat products.
- We have suffered serious injury in the form of lower prices, being forced to change our product mix, and having to vary our customer base (loss of processor customers).
- We produce and report across two lines, middles and legs. The impacts of these are discussed below.

Middles

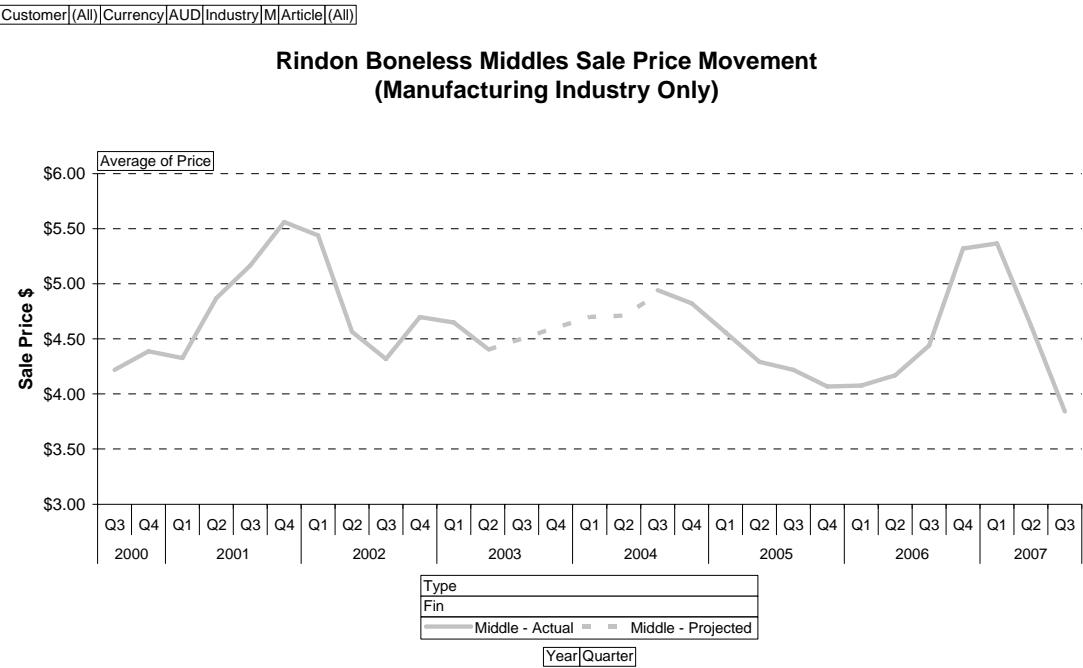
- Figure 2 shows the decline in prices received by B.E. Campbell for boneless middles, arising from a lack of demand due to the over supply of imported Danish product.

Figure 2



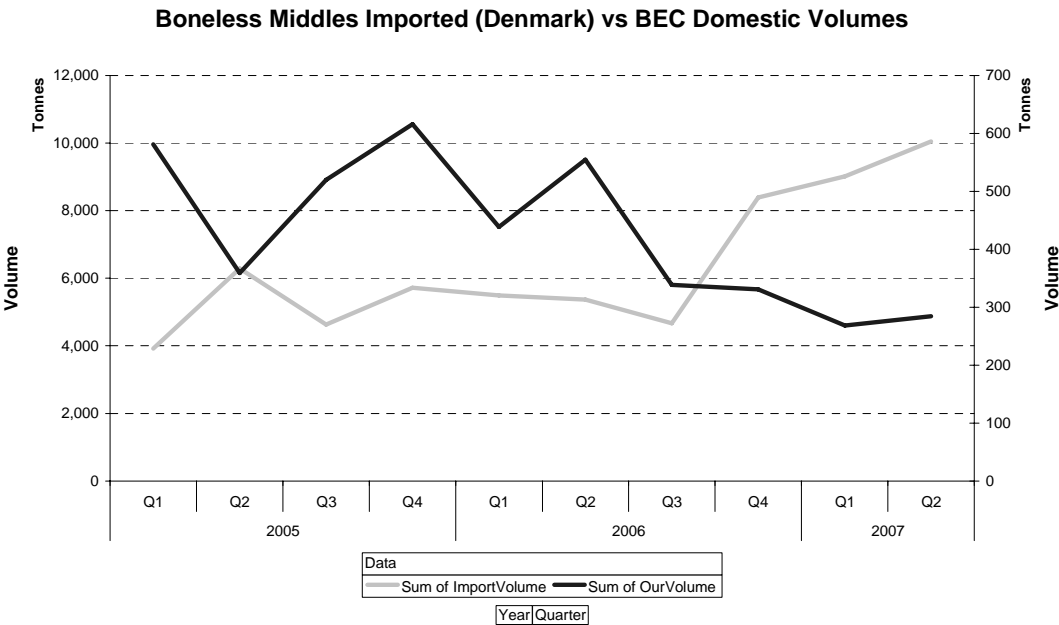
- The difference between the price of Danish middles and local middles is very small – Danish producers stay within a 20c/kg range of local prices. Their main market is the UK, therefore they can afford to offload cheap product in Australia. Even though B.E. Campbell's domestic price has fallen below import levels there has been no increase in purchasing. This is due to the buying practice which can see the major small good processes lock in and book deliveries of imported product 3-4 months in advance. This is a barrier to the market responding to price reductions in the domestic market.
- The price spike experienced at the end of 2006 was due to a shortage of boneless middles out of Denmark, which forced manufacturers back into the local market. In the March 2007 quarter, supplies from Denmark increased which resulted in domestic prices falling significantly (Figure 3).

Figure 3



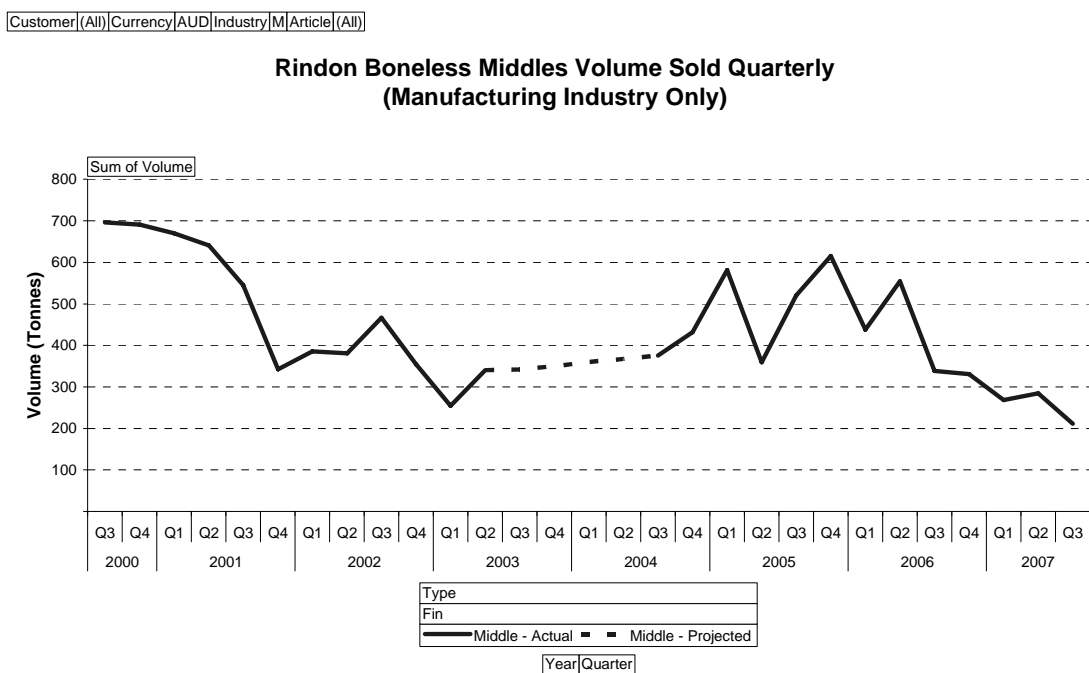
NB: The dotted line in the graph is an estimate due to a loss of data when upgrading a computer system.

Figure 4



- The decline in sales of middles during 2007, due to the increased level of imported product, is shown in Figure 5.

Figure 5



NB: The dotted line in the graph is an estimate due to a loss of data when upgrading a computer system.

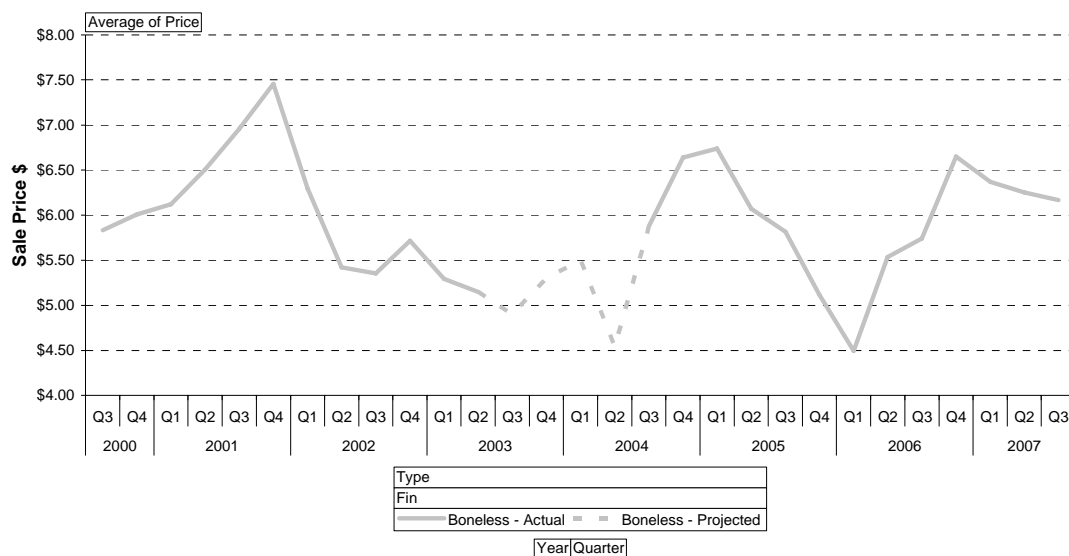
Legs

- Boneless leg meat prices have remained low and due to import prices being consistently under \$A 4.00/kg we are unable to compete (as shown in the costing model provided in the Confidential Attachment - Ref 2). The price shown in Figure 6 is the price received by the company which is not reflective of the going market price, hence the sharp decline in sales volume for the product group shown in Figure 7. Due to imports, sales have significantly decreased over the past 18 months, following a shift towards sales of bone in pork legs. Dumping of this product from overseas has killed this market.

Figure 6

Customer|(All)|Currency|(All)|Industry|(All)|Article|(All)|

Boneless Rindless Legs Quarterly Sale Price Movement

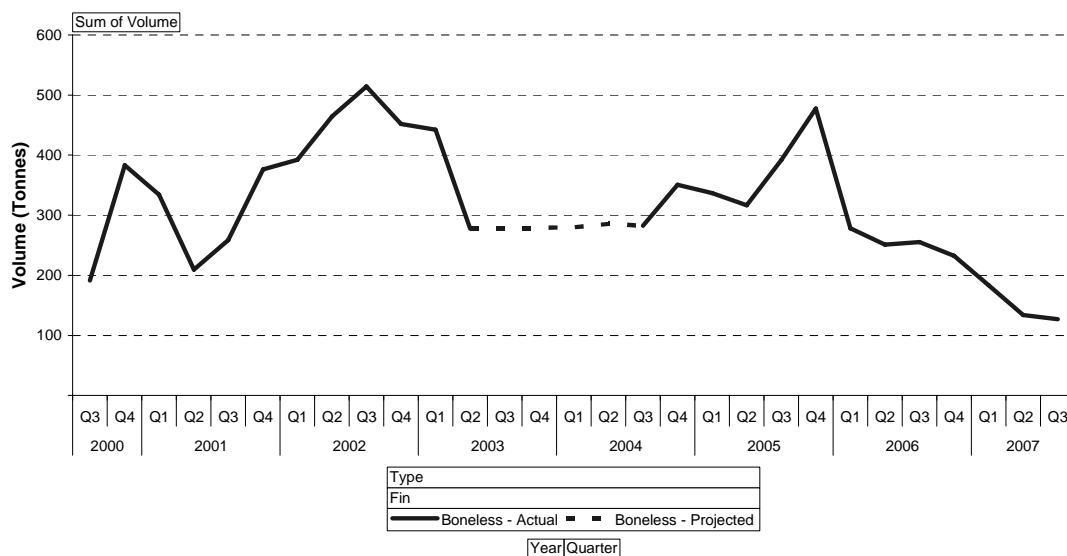


NB: The dotted line in the graph is an estimate due to a loss of data when upgrading a computer system.

Figure 7

Customer|(All)|Currency|(All)|Industry|(All)|Article|(All)|

Boneless Rindless Legs Volume Sold

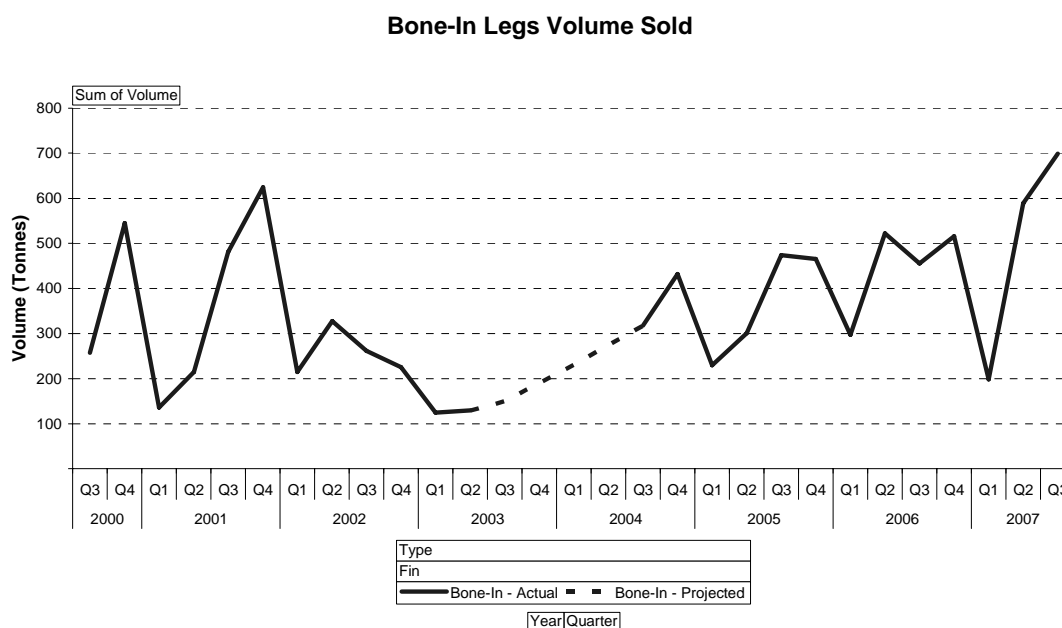


NB: The dotted line in the graph is an estimate due to a loss of data when upgrading a computer system.

- Figure 8 shows the seasonal trends of bone-in pork legs, which are predominantly used for bone-in hams during the Christmas period. The high levels of boneless leg imports has dramatically increased the pressure to boost sales of bone-in legs, which is shown in the sharp rise in bone-in legs sold. This has also required a decrease in pig weights, to ensure that the legs received by the company meet the requirements of the bone-in leg market.

Figure 8

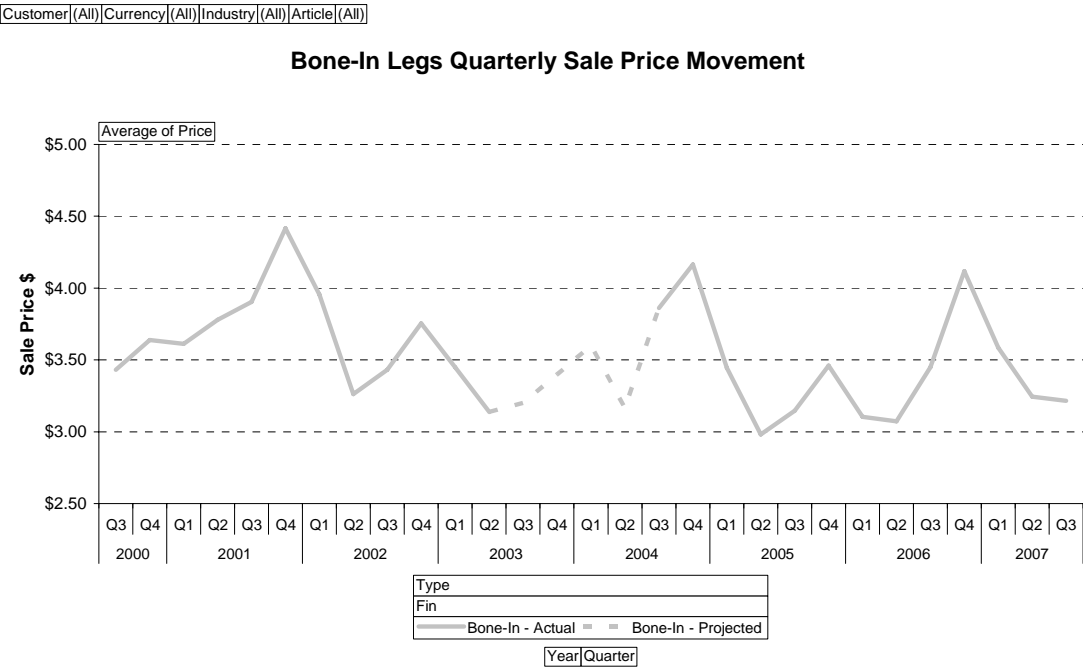
Customer[(All)]Currency[(All)]Industry[(All)]Article[(All)]



NB: The dotted line in the graph is an estimate due to a loss of data when upgrading a computer system.

- Quarterly sale prices for bone-in pork leg are shown in Figure 9. Prices have decreased significantly this year, due to the shift in sales away from boneless pork leg to bone-in pork leg. Characteristically for the September quarter of the year, bone-in leg prices rise significantly due to Christmas preparation demands. However this year, no such increase in price has occurred. This is due to the over supply of bone-in leg, resulting from the shift away from boneless leg meat production to bone-in (due to the high level of imported boneless product).

Figure 9



NB: The dotted line in the graph is an estimate due to a loss of data when upgrading a computer system.

- We continue to suffer serious injury, as prices continue to fall, costs rise and inventories grow.

Summary of Impacts

Product

- We have had an oversupply of middles and have had to increase the volumes frozen in the short run (may lead to a situation where we have to off load this product onto the market below cost)
- We have had to move to bone-in pork leg which will add to the pressures on price in this market as much of the domestic industry is following this option.

Financial

- FY2008 costs (\$/kg) are projected to rise 17% from FY 2007, as a result of a 15% reduction in production volumes. This represents around \$5.1 million in additional costs associated with less efficient plant utilisation.
- These inefficiencies mean that the operation in its current configuration would immediately become unprofitable.
- We expect to suffer further injury and potentially, irreparable damage, in the absence of government intervention:
 - high imports are expected to continue
 - inventories are expected to grow further
 - we will be forced to lay-off staff
 - the company will have reduced capacity utilisation
 - may be forced to dump product domestically that is held in store
 - this will lead to a further reduction in profitability
 - we anticipate a reduced ability to raise finance.
- We note that producers are beginning to exit the industry (drought and grain prices have sped up the process, but imports are the key driver).
- By June 2008, industry data has indicated that sow numbers in the industry could potentially fall by 20-25%. This level is critical as if this translates to throughput in our business this will increase costs of production by at least 29%. On-going operations at this level will not be commercially viable.

3 Measures taken to control the situation

- We have taken a range of measure in the medium term to adapt to the pressures from under priced imports. These include:
 - We have changed our product mix to suit our new customer base
 - Increased the number of growers under contract and changed specifications
 - Invested in new technology and infrastructure
- Even though we have undertaken these measures over time we have had to reduce price to growers

3.1 Customer Base

- We have changed our customer base and product mix to suit
- Over the past 7 years, as imports have increased, B. E. Campbell has had to move pork products into other market segments, to try to maintain sales and margins. The move has seen manufacturing represent 26% of sales volumes in 2007, compared to 54% in 2000 (Figure 10 and Figure 11). This was a direct result of the manufacturing segment using imported products rather than domestic.
- We have been increasing export volumes to New Zealand (quarantine laws stop NZ using Danish product), however this is very risky because the situation could change suddenly. There is increasing speculation that the quarantine regulations are going to be changed in the near term.

Figure 10

[Group]PORK[Currency](All)[Year]2000

Industry Profile (Sales Volume)

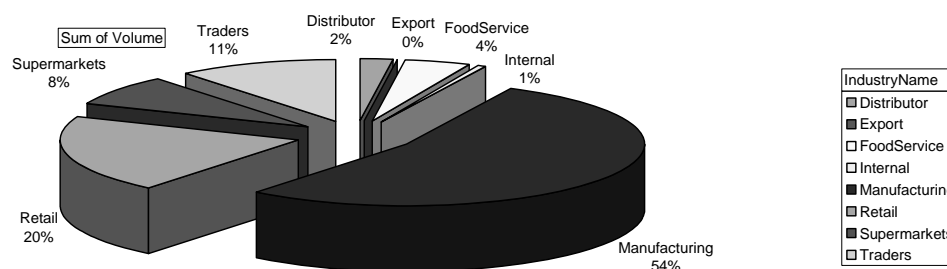
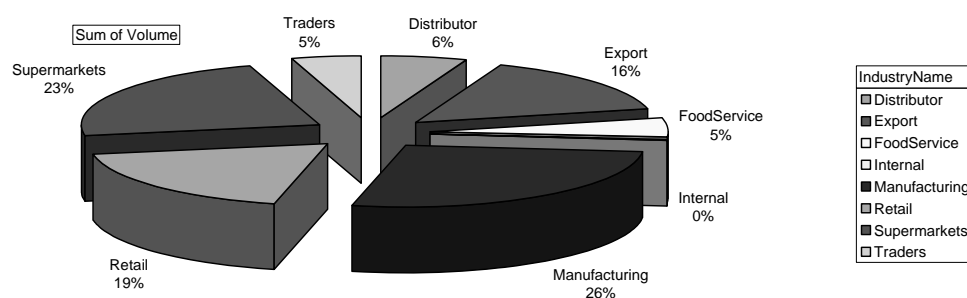


Figure 11

Group|PORK|Currency|(All)|Year|2007

Industry Profile (Sales Volume)



3.2 Contracting

- The company has increased the number of growers under contract – in 1999, the company did not have any supply contracts with growers (see Confidential Attachment - Ref 1 for details). Grower contracts were introduced to assist growers with securing finance and to assist the company in securing supply. As the number of growers has steadily decreased, the majority of the remaining growers have looked to expand their output and need to borrow capital to do so. Many of these growers need to provide evidence to their financial lenders that they meet loan repayments and a supply contract provides them with this assurance.
- Supply contracts are a mechanism to ensure ongoing supply – however, current pressure on production, higher prices in the fresh market and a volatile outlook has placed pressure on our supply relationships. This will impact on future viability across this industry segment and also disrupt feedback processes on quality.
- The company is implementing more stringent payment grids, as an incentive for growers to improve quality. Appendix 1 shows the weight and fat specifications at which growers are paid a premium for bacon carcasses, and the way this has changed over time. As the volumes of imported boneless leg meat have increased, the company has tightened its carcass specifications and reduced the maximum weight paid to growers.

3.3 New technology and infrastructure

The company has increased the efficiency of its operations through various investments in technology, including:

- processing equipment (investment in Danish technology from SFK, worth \$3 million) to provide:
 - improved yield;
 - increased opportunity to provide pork by-products; and
 - decreased labour costs;
- a retail-ready packing plant at Arndell Park to:
 - increase retail market share of pork;
 - value add pork by-products; and
 - improve ability to respond to market
- transport (increased utilisation and efficiency of transport); and
- a new IT system to:
 - improve data flow back to growers;
 - better align sales with livestock purchases; and
 - reduce costs.

3.4 Prices

- We have had to pass on lower prices to growers. These impacts are discussed in the next section.

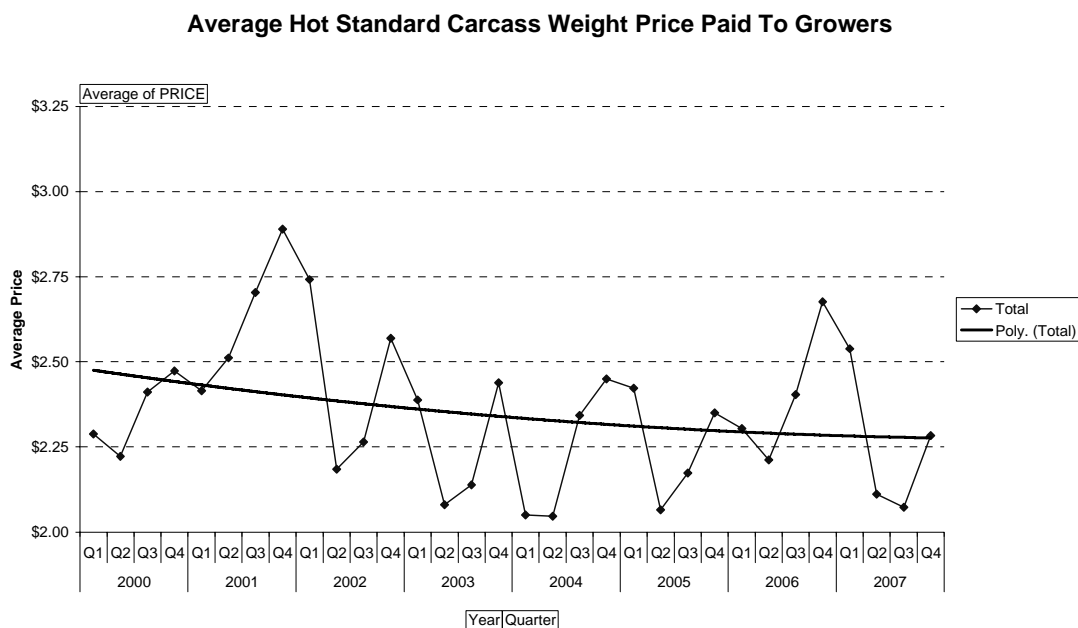
4 Impact on supply chain

- The pork industry has already undergone considerable restructuring. The changes in product mix, specification and prices have impacts along the supply chain.

4.1 Prices

- Figure 12 shows that farmgate price changes are very seasonal. The demand for pork meat increases in the later part of the year as processors prepare for Christmas and summer sales orders. At the same time, the effect of the previous summer's mating infertility results in a decline in supply. These two market forces combine to drive prices higher in the later part of the year.
- During the early months of the year the demand for pork meat is lower, whilst supply remains steady due to good growing conditions. Pork processing limitations during April (no production during public holidays) generally leads to an over supply of carcasses.
- Traditionally, November prices should be higher than the current 2007 price. However the large quantity of imported product has been the key contributor to the current depressed farmgate price.

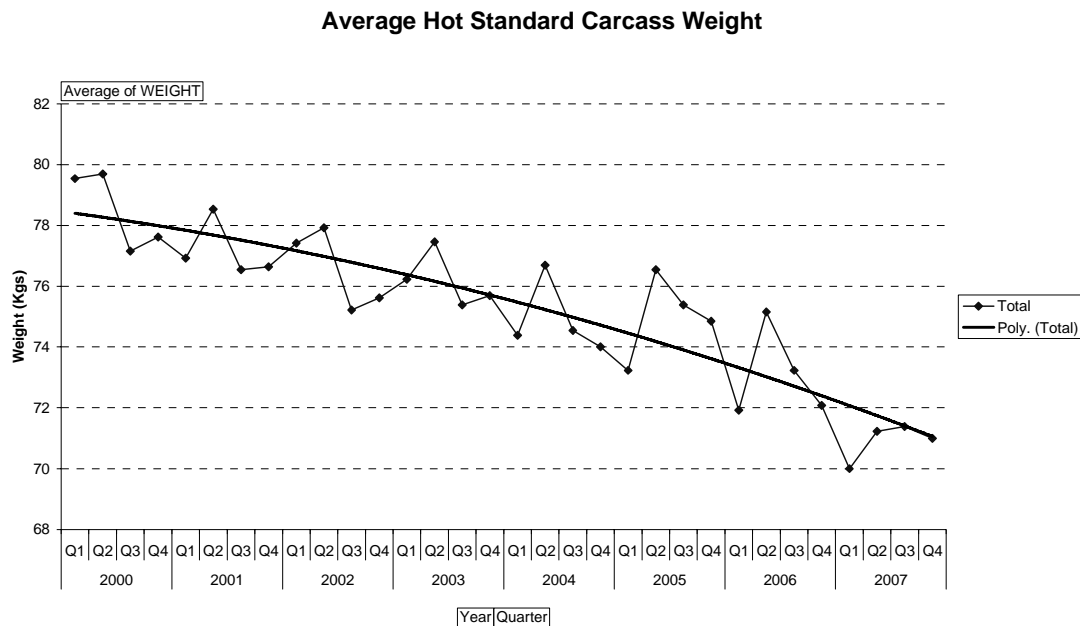
Figure 12



4.2 Production and costs

- Carcass weights have been reduced from 76.5kg in 2004 to around 71kg today (Figure 13), as the demand for heavier carcasses has decreased. Carcass weights have been driven down to ensure the company receives legs that meet the requirements of the bone in leg market. However, this is less efficient for growers.
- Growers have responded and quality (measured by fat score) has also improved by 10-15% since 2001.

Figure 13

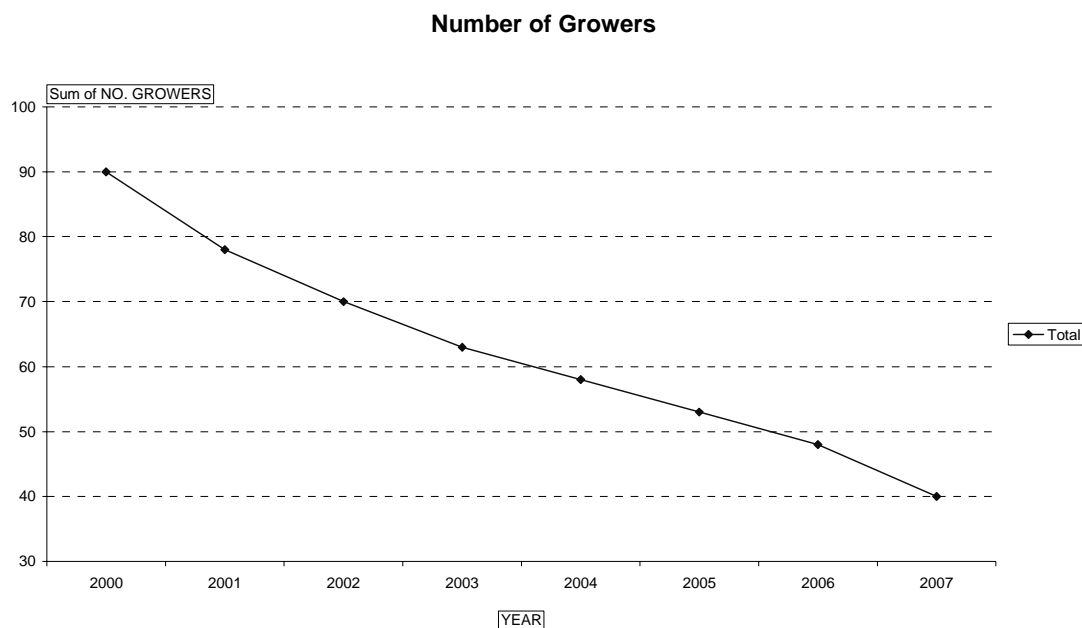


- A lighter pig is preferred because:
 - if it is a larger pig, the leg needs to be boned;
 - it is more suitable for bone-in leg hams (which can not be imported);
 - frozen boneless hams are imported from the US and Canada, and it is too hard to compete with these on price; and
 - quality tends to be lower with a larger carcass, therefore a lighter carcass makes it easier to compete with Danish middles. As carcass weights have decreased, fat score measurements have decreased proportionately. Part of the decrease in the fat score measurement can be attributed to advances in carcass quality, to improve the consistency of the company's product.

4.3 Grower numbers

- Whilst the number of breeding sows has remained steady, the number of growers supplying B. E. Campbell has been declining at a steady rate. The company has lost ten growers over the last 12 months. In 1999, 105 growers supplied the company, however this has since fallen to just 40 (Figure 14). Farm costs continue to rise, making it more difficult for growers to remain economically viable. Many growers who have managed to remain competitive in the market have done so by adapting new technologies, reducing feed costs, and capitalising on economies of scale.

Figure 14



4.4 The outlook for abattoirs

- The profitability of at least two abattoirs that the company deals with is already considered to be 'very borderline' (Booyong and Burrangong).
- Burrangong has a typical throughput of 7,000 a week and it is now 5,000 per week. They report producers in the 100 to 200 sows leaving the industry. They did have 28 staff collecting offal for export to Thailand, Singapore, Hong Kong and Taiwan. These people have been stood down as the scale is not adequate to service the markets. The loss in income and lower economies of scale means that costs per animal have increased by 20%. The next adjustment is a move to part time lines.
- It was commented that the costs of production in the US would have to be significantly lower, at least 40-50%, to justify price differences in the market.
- If the imports continue rationalisation or reconfiguration of the abattoirs could trigger a collapse of the infrastructure needed to support a sustainable industry.

4.5 The outlook for growers

We contacted a number of our grower suppliers as part of this process.

- They have raised concerns that lower prices and the inability to pass on higher costs of production will lead to a sustained reduction in throughput, which will actually counter the improvements in efficiency that have been undertaken within the industry during consolidation over the past 5 years.
- Growers have indicated that will try to reduce costs further.
- Growers may also be able to destock / restock to get rid of disease and reduce costs.
- Most have indicated that they will move towards a carcass that is suitable for the fresh market. They see the lower prices in the processing market and though concerned about the risk associated with the concentration on the fresh market, cannot afford to continue to supply processors while making a 20c/kg loss in the past year (note that this loss was based on a favourable long term contracted feed price).
- Investments in infrastructure have been delayed until the outlook is more certain.
- Growers have reported that they have cut production and this is backed up by abattoirs.
- We are concerned that the pressures of these imports will actually diminish the efficiency of growers as dedicated large scale producers are currently suffering significant losses.

4.6 Summary

- If the imports continue rationalisation or reconfiguration of the abattoirs could trigger a collapse of the infrastructure needed to support a sustainable industry.
- Responses by growers have an impact along the supply chain and on our business as volumes could diminish over 2008 to a point where a significant action is required.
- A move to fresh pork means that the overall market will become more volatile as a smaller local market will be impacted by any shocks to the industry.

5 Future Strategy

5.1 Introduction

- Safeguard action, including a provisional safeguard, is the most appropriate measure because an immediate response is required to prevent irreversible damage. While several strategies have already been implemented and further options are being investigated, a safeguard is required due to the time lag involved before the benefits of industry wide responses are realised.
- It is in the national interest to have a robust and efficient industry, because this is in the long-term interest of consumers (a robust industry provides competition to imported product, and therefore helps to limit market power and keep prices in check)
- Market forces are being destabilised due to the subsidies that overseas competitors receive (which encourage increased shipments to Australia). Therefore producers are more vulnerable to high grain costs, drought, and the appreciating A\$ (unlike previously).

5.2 With the safeguard

- Our company is continuing to work on quality improvements (improving consistency, lean meat yield, belly yield, paying growers for consistency), but there is a time lag involved.
- As an example, an option to improve quality, such as Pork Scan, is currently used in four abattoirs that supply the company. Quality will increase over time via more informed feedback to geneticists, to improve overall herd quality. This will lead to greater yields, increased economies of scale, lower costs of production and increased competitiveness of Australian product.
- We will continue to alter our payment system based on this information, so that payment received by growers is linked to quality (growers will then have an incentive to improve quality). B.E Campbell is integrally involved in this process across the supply chain and fully supports this initiative. This is a medium term response.
- We plan to investigate technology to improve the efficiency of boning.

5.3 Without the safeguard

- In the absence of the safeguard, the company may need to diversify into processing other livestock such as sheep and cattle, however this is not a preferred option due to the significant investment required and the investments made over the past 7 years are highly specialised to the pig industry. It is noted that one competitor has already started doing this.
- Some of the options under a safeguard may still be investigated, however, the time lag before benefits materialise is likely to make many of these options unviable.
- The medium to longer term investments cannot be made when local supply is at risk.

6 Conclusion

Have imports increased?

- B.E. Campbell produces products across all the categories that are subject to enquiry. That is:
 - Boneless Frozen Swine Meat;
 - Boneless Frozen Swine Meat, leg cuts;
 - Boneless Frozen Swine Meat, middle cuts; and
 - Boneless Frozen Swine Meat, shoulder cuts.
- Imports in the categories have increased over the past years, increasing by 87% from 2002 to 2006.
- B.E. Campbell is a producer of goods that are 'like' and 'directly compete' with imports, in particular, middles and boneless legs.

Has the industry suffered, or is it likely to suffer, serious injury?

- Our company has lost market share into the manufacturing sector of the industry. The domestic industry is now becoming more concentrated on fresh market.
- We have been forced to increase production of bone-in product, as we could not compete with the volume of cheap imported boneless product.
- Participants in our supply chain are losing money and the outlook for 2008 is for continued losses due to low prices and reduced volumes.
- Profitability across the supply chain is under threat. If the imports continue it could trigger a collapse of the infrastructure required to support a sustainable industry.

Are increased imports causing serious injury?

- Our loss in market share is a direct consequence of higher imports.
- The increased imports are affecting throughput, this reduced throughput directly threatens our business viability. Estimates of a 15% loss of turnover for 2008 will mean that our business becomes unprofitable.
- Serious injury is being caused through firstly lower prices and the imposition of higher costs as producers have to restructure their production systems to meet our new specifications.

What are the impacts on other parties?

- Our suppliers have been forced to reduce their pigs' carcass size, in order to meet the specifications of the bone-in market.
- This has reduced the efficiency of their enterprises and has forced cost cutting in areas that may result in long-term damage to their companies (e.g. loss of key personnel).
- The reduction in options for producers including the opportunity to maximise productivity and having markets for rejects will see a significant decrease in flexibility and systems will have to be refined as producers change systems to meet the fresh market.
- A move to fresh pork means that the overall market will become more volatile as a smaller local market will be impacted by any shocks to the industry.

- The high level of imports is on top of high grain costs, and the appreciating A\$ which means that the usual responses to these imports are constrained. The industry is sensitive to shocks at this stage and sound investment decisions cannot be made.

What safeguard measures would remedy serious injury?

- Safeguard action, including a provisional safeguard, is the most appropriate measure because an immediate response is required to prevent irreversible damage. While several strategies have already been implemented and further options are being investigated, a safeguard is required due to the time lag involved before the benefits are realised.
- Time to adjust so the industry has surety to invest in actions to reduce costs and improve consistency is critical.
- The industry requires a mechanism (quota or tariff) that will allow access for domestic supply to the processed market in the medium term. Without this access the specialised supply chain to this market is under threat.
- An immediate response by Government is needed to prevent irreversible damage to B.E. Campbell's business and its supply chain partners.
- The future for an Australian supplied process market is positive if we have a chance to improve competitiveness.

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B.E. Campbell
www.becampbell.com.au

Personal Communication:

Mrs Sally Walker 21/11/07

Mr Andrew Jones 21/11/07

Mr Grant Edmonds 22/11/07


Appendix 1 B. E. Campbell payment specifications over time?


Grower Grid Matrix

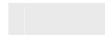
Fat = 1mm increment to 21

Weight = 5 kg increments 0-105

HSCW Trim 1		Fat																					
From	To	0	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21+
0	4.9																						
5	9.9																						
10	14.9																						
15	19.9																						
20	24.9																						
25	29.9																						
30	34.9																						
35	39.9																						
40	44.9																						
45	49.9																						
50	54.9																						
55	59.9																						
60	64.9																						
65	69.9																						
70	74.9																						
75	79.9																						
80	84.9																						
85	89.9																						
90	94.9																						
95	99.9																						
100	104.9																						
105																							

 2007: growers are paid on prime price for bacon carcasses.

 2003: growers are paid on prime price for bacon carcasses.

 2000: growers are paid on prime price for bacon carcasses.

Appendix 2 Images

These images are supplied for discussion purposes if required.

Leg 1



Leg 2



Leg 3



Leg 4



Leg 5



Leg 6



Leg 7



Leg 8



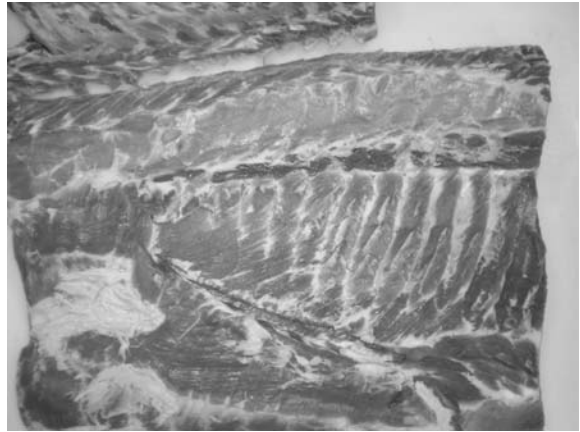
Leg 9



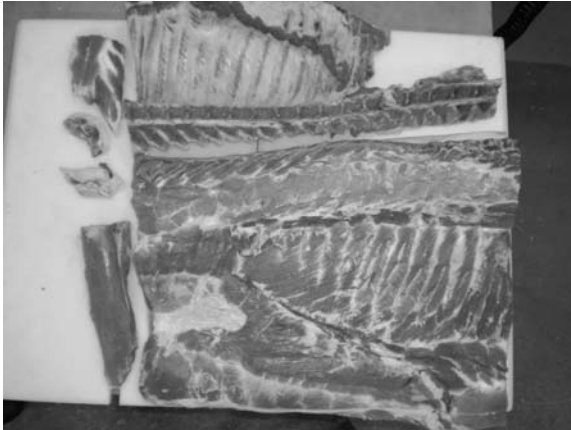
Middle 1



Middle 2



Middle 3



Middle 4



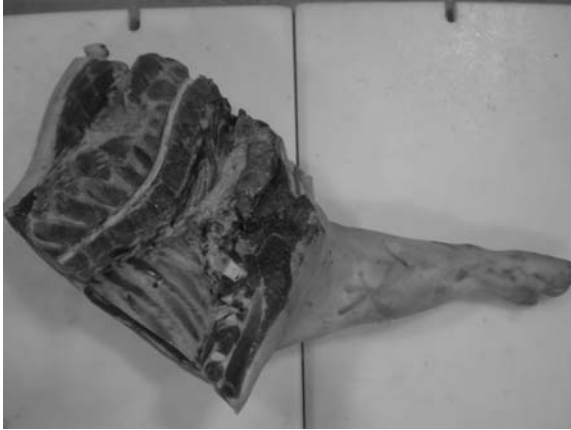
Middle 5



Middle 6



Shoulder 1



Shoulder 2



Shoulder 3



Shoulder 4



Shoulder 5



Shoulder 6



Shoulder 7

