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To whom it may concern:

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

This is a submission from Neil Ferguson of Westpork Pty Ltd to the Productivity Commission Safeguards Inquiry into the Import of Pigmeat.

In this I wish to address the following matters:

- How imports have impacted on the long term average price received by producers supplying the processing sector;
- How as a business we made the necessary adjustments to remain profitable despite the fact that an ever increasing share of the processing sector's pigmeat requirement is being supplied via imported pigmeat.
- How the dramatic jump in imports by the processing sector in recent times is going to impact on our business profitability. How the processing sector fails to effectively communicate it's short and long term buying strategies to producers therefore impacting producer profitability, in turn creating the exact problem the industry is currently facing.
- An implementation of provisional safeguards and general safeguards or a genuine exit strategy targeted at the mid size to large producer with clear directions to the production sector that the safeguards/exit strategy will only ever be offered to the industry once; that they will be phased out over a period of time; and that the industry should look to use this opportunity to reduce its size, should not:
  - a. If managed and communicated to industry correctly be a disincentive for the industry or for our farming enterprise to adjust; or
  - b. Inhibit the international competitiveness of our industry; or
  - c. Impact negatively on consumers in terms of price increases on processed product as the fresh meat market has already made adjustments to it's prices; or
  - d. If managed and communicated correctly slow our farming enterprise or industry restructure.

We can demonstrate what actions we as a company have taken to manage the increasing trend of the processing sector to import pigmeat. We can demonstrate that as an enterprise we are in a far better position today to manage the pressures of imports than what we were 5 years ago. We are willing to show to the commission how our business has changed over the last 5 years.

At this point in time the dramatic jump in imports has not affected our bottom line, however unless something happens to change the oversupply of pigmeat in the Australian market caused by the sudden jump in imports Westpork's profitability will be materially affected over the coming 12 months. We believe that due to the risk management strategies that Westpork has put in place over the last 5 years we are in a far better position than a lot of other producers within the industry to manage the current industry situation.

I would be happy to discuss any matter raised in my submission with the Commission, given the opportunity to do so I can be contacted in (08) 9479 7456 or 0419 041 287.

Your sincerely

Neil Ferguson  
General Manager

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# **1. FARM ENTERPRISE/COMPANY BACKGROUND**

Westpork Pty Ltd was founded in 1985, we are a specialist pig producer, we are not involved in broad acre farming, we do not operate an abattoir nor do we undertake processing in any form. 100% of Westpork's income is derived from breeding and raising pigs for slaughter. We operate in Western Australia, we have 3 company owned farms and one contract grower.

## **2. FARMING ENTERPRISE/COMPANY STRUCTURE, PRODUCTION AND MARKETS**

### **A. PRODUCTION**

Westpork was formed in 1985 by building a 400 sow farrow to finish facility, by 2002 Westpork had grown such that it was selling 98,000 animals. Today Westpork operates 7,500 sows (including unmated gilts) and sells approx. 150,000 animals per annum.

Up until 1997 100% of Westpork production was consigned to one processor who used this meat for manufacturing purposes. Since 1997 Westpork has deliberately focused a large proportion of its expansion program towards the retail/fresh meat area so that now a maximum of 65% of our pigs are destined for the processing sector. Some of the animals we consign to the processing sector are exported by our customers, likewise some of the animals are broken down and sold into the fresh meat market by our processing customers.

### **B. EXPORTS**

Westpork does not export in its own right. Westpork specifically selects export grade animals for two of its customers, consigns them to the abattoir on specific days so that these customers can supply the Singapore market on a regular basis.

### **C. MARKETING STRATEGIES**

Traditionally Westpork sold pigs to its customers on a weight & grade basis. Similar to other producers in WA prices varied from month to month with no guarantee from one month to the next what the price would be. Prices would change on the 1st Monday of each month and we were advised either on Friday afternoon or in many cases on the Mon/Tues what we were going to be paid for that month. It's worth noting that historically WA prices have not varied to the degree they have on the Eastern Seaboard, but the cost of this stability has meant that WA producers on average have received 7-8c/kg less than East Coast producers over any given 5 year period

### **D. EMPLOYMENT AND REGIONAL BUSINESS EFFECTS**

Westpork employs 60 people. With record low unemployment rates in Western Australia finding staff has been extremely difficult. Fortunately we have been able to bring in skilled workers under the 457 visa program to fill the void of local staff.

The Australian Government states that under our free trade policy that as a pig producer Westpork needs to compete in the open market and against imported pigmeat from overseas. As an employer we have been forced to bringing in overseas workers to fill the labour shortage in Western Australia. Here the Australian Government not only forces Westpork into paying higher wages than our competitors (USA/Canada) but also forces us to pay salaries well above the going Australian rates of people for the people we bring in.

### 3. ON FARM PROFITABILITY

As detailed in item 2c - Westpork operates with a number of different long term pricing models, so at any given time Westpork's selling price may be totally different to where the spot market is at. It is worth noting that more and more pigs around Australia are being sold on long term contracts/pricing models similar to Westpork. Likewise a number of the major players in the Australian pig industry either operate or have strategic alliances with abattoir/boning rooms so how they actually portion the value of the pig between their pig enterprise and the boning room can vary from one company to the next depending on the organization's pricing policy.

#### A. PRICES

The difficulty the Productivity Commission will have when matching these numbers to what other producers have received is that our prices are influenced by the long term contracts we have in place. Some producers have the view that they wish to punt the market, they want to ride the highs and make the big dollars, these producers need to be prepared to ride the lows as well. As stated a number of pig enterprises are part of integrated system, how these enterprises allocate prices between the different divisions varies from one company to the next? It is very easy for an integrated operator to manoeuvre profits/losses amongst the different divisions.

#### B. OPERATING EXPENSES

##### i. Feed and Grain Costs

Westpork is fully exposed to the high world grain prices experienced during the 2nd half of 2007. With Western Australia having only one harvest each year, these high grain prices will be felt by the company for a full 12 month period. Assuming it rains many East coast producers have the ability to source grain from the summer crop, which will give them some price relief mid year from the high grain prices.

FCR is as crucial to the success of a pig enterprise as what grain prices are. To this end the company's investment in new feeding systems and tunnel ventilated sheds will improve our overall FCR.

##### ii. Production and other costs

Feed is by far our biggest cost item, followed by wages (inc. super, payroll tax, workers compensation, etc.) with all other costs being much smaller than these two items. Overall there is very little variation from one period to the next in these other cost items. With our investment in new facilities our depreciation charges may be higher than most other producers but this is likely to be offset by lower R&M expenditure on the new facilities.

##### iii. Capital Requirements

Westpork's growing herd has been housed in straw based shelters. In our opinion straw based housing systems are not as animal welfare friendly as they first appear, they are cheap to build but they are labour intensive, high cost facilities to operate.

As a result in 2006/07 Westpork commenced a significant rebuilding program, replacing its straw based growing facility with tunnel ventilated, autosort buildings.

The purpose of rebuilding the grower facility was not only to drive costs out of the business, it was designed around improving the consistency of the carcass that we deliver to our customers. This allowed us to increase the carcass size that we deliver to our customers which further reduces our cost of production per kilogram sold.

iv. Risk Management

Westpork has started discussion with grain producers about long term grain contracts (supply/price), this is very much in it's infancy with minimal tonnage contracted at this stage. In the past we have used Swaps/Forward Deliverable Contracts during the growing season to manage risk.

#### **4. IMPACT OF IMPORTS: Current serious damage and the threat of further serious harm**

With Westpork's rolling average contracts imports have effectively lowered the price that our customers have had to pay for the pork they buy. Imports have effectively placed a cap on the price of Australian pigmeat, whenever the domestic market rises the processing sector has the ability to and has imported additional volumes of product, thus suppressing domestic prices. The fact that Australian processors have the ability to cap domestic prices in turn lowering the long term average price paid to Australian producers is not something the Productivity Commission can invoke safeguard actions against.

Over time the level of imports has steadily risen but in recent times the level of imports has jumped 44% (Moving Annual Total) on where they were 12 months ago, creating what many perceive to be an industry "crisis".

Pig farming is capital intensive, there are moderate lead times (approx. 9 months) from the time we make the decision to mate an animal until we actually sell the progeny of that mating. When faced with the situation of short supply processors are more than willing to encourage capital investment/offer producers incentives to expand when there is an oversupply situation they are willing to cut producer off with as little as one week notice.

A real concern is that if the Productivity Commission instigates safeguard actions, prices suddenly jump as a result of that decision, processors could encourage farmers to expand the sow herd. This expansion could be in the form of investment in new facilities or the repopulation of a number of piggery's that have simply been depopulated due to the current industry situation. When the safeguard actions are removed the pig industry could find it's self in the same predicament as it is currently faced with.

Westpork believes this is a real issue as some processors have now come out and stated that they basically want all of their manufacturing meat to be imported meat with only their fresh meat requirements being locally produced product. Processors encouraging domestic production to overcome safeguard actions in our view would be irresponsible considering their long term strategy of wanting to increase the percentage of imported meat going in the processing sector.

#### **A. WILL THE AUSTRALIAN INDUSTRY PURELY BECOME A FRESH MEAT INDUSTRY?**

Unless the processing sector is willing to change its view and offer Australian producers a fair, long term price rather than subject it to periods of oversupply/ artificially low pig prices due to their own importing strategy, Australian producers will exit the processing market - to the extent that producers purely focus on the fresh meat market.

In terms of being paid a fair price processors will need to engage producers on longer term contracts/pricing models and be prepared to honour the contractual obligations that they enter into, not look to obtain price relief from their producers when they as an industry get their total buying strategy wrong.

#### **B. IS THIS JUST ANOTHER PERIOD OF CONSOLIDATION/CONTRACTION THAT THE PIG INDUSTRY NEEDS TO HAVE?**

For the reasons listed in 4a. Westpork believes this to be the case. The real danger around safeguard actions/exit strategies are that they prolong the inevitable. Processors through their actions/statements are basically looking for imports to fill the process meat market. This being the case the Australian Pig Industry is in for a further period of consolidation/contraction. Managing this situation will not be easy:

- Based on the assumption that the industry needs to contract who decides which entities should exit?
- How do we determine what size the industry should be at?
- How do we ensure that those exiting the industry are genuine exits, not producers simply depopulating/repopulating for commercial/health reasons.
- How do we allow those producers exiting the industry to do so with some dignity whilst preserving the equity they have within their business?
- For those producers who remain in the industry how do we manage the transition so that at the end of the day they are left with viable businesses?
- How do we manage the exits so that not too many producers actually exit the industry leaving us short of fresh pigmeat, so that we can not fully supply our Australian fresh meat/ Export markets?

Purely invoking safeguard actions without facilitating the structural industry changes that the industry needs to go through will result in a further period of pain for the industry once the safeguard actions are removed. Westpork would prefer to see a short period of pain felt by all in the industry here and now rather than invoke policies that would simply delay or prolong a period of difficulty for the industry.

Processors when faced with a period of rising prices or perceived shortages in supply may/will encourage producers to expand production. Some producers suddenly faced with the prospective of profits returning may decide to expand their enterprise, repopulate some of the large facilities that have been depopulated and placed in a maintenance position or simply not exit the industry as planned. These issues need to be discussed and form part of a management plan when deciding on what safeguard action/exit strategies are going to be implemented.

## **5. CONCLUSION**

Westpork accepts the fact that pork will be imported into Australia in the long term. Processors through their buying strategy have basically been telling Australian producers that they don't want our product, they want to rely on imported meat for manufacturing purposes.

Rather than implement Safeguard action Westpork would prefer to see a specific package designed for those producers who wish to genuinely exit the industry (not purely depop/repop). The problem with the exit strategies in the past is that they have been focused towards the small inefficient producer with very little behind them in terms of assets. A simple exit program designed at the small end of the production spectrum will not achieve what it is intended to do or what the industry needs. An exit program would need to be substantial, designed to remove some of the mid size/larger producers from the industry and keep them out for a period of time (suggest 3-5 years). By and large the typical small (efficient/inefficient) producer from 5 years ago has already elected to exit the industry.

Should the Productivity Commission invoke Safeguard actions or structure a specific exit strategy for the industry that reduces pigmeat supplies in Australia, this will have minimal if any impact on the price of fresh pork going to consumers.

Imports already comprise over 65% of the meat going into the processing sector. So from a processing sectors perspective they have already signaled their intention to rely on imported pigmeat, reducing domestic production will have absolutely no impact on the price of the majority of the meat they buy. Potentially they will lose a source of cheap top up meat for their factories, but the reality of the situation is that they are going to lose this anyway because the prices they have been paying are unsustainable, producers will exit the industry rather than supply the processing sector at a loss.

The bigger issue for the smallgoods sector is that they will be completely open to the vagaries of world currency markets and world pork markets. This is something that each company within that sector and as a whole will need to consider, how they are going to manage the relevant risks. As a industry they have basically accepted these risks and have the systems in place to manage the risks as evidenced by how they have gone about increasing the share of imported meat entering their factories, whilst reducing their reliance on Australian pork.