Safeguards Inquiry into the Import of Pigmeat:

Submission to the Productivity Commission

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Prepared by:

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BACKGROUND

QAF Meat Industries is Australia's largest integrated pork production business comprising stockfeed manufacture, pig production, slaughtering and boning, and sales and distribution of pork products both domestically and internationally.

QAF:

- Manufactures approximately 270,000 tons of stockfeed per annum with ninety percent used in its own pig production facilities;
- Produces approximately 950,000 pigs per annum in its own production and contract facilities. This equates to approximately 18 percent of Australia's pork production;
- Slaughters all its own production, primarily in Australia's largest single purpose abattoir at Corowa;
- Bones out twenty five percent of the carcases produced primarily for the fresh retail market;
- Distributes sixty-eight , twenty-six and six percent of its products into the fresh retail, manufacturing and export markets respectively; and
- Employs 1,000 people across the business.

Defining the industry: who are producers of 'like' or 'directly competitive' goods?

As demonstrated above QAF is involved in all aspects of the pork supply chain in Australia. We would argue that commercially the product which is directly competing with imports of foreign pigmeat is Australian produced pigmeat. Therefore in answering who produces these products, we believe it includes all people involved in the supply chain, ie production, abattoir and boning room.

Are increased imports causing serious injury?

The question of whether increased imports are causing serious injury is simply explained by the effect that any sudden increase in supply will have on price when demand is effectively constant.

- ABS data shows an increase of over sixty percent in imported product in the first half of 2007 compared to 2006.
- Domestic supply over this same period has remained constant.
- In order to market this extra product, prices for like products have fallen. Domestic prices for middles into manufacturing have fallen from $5.40/kg at the start of the year to $3.80 currently. Even at this low price, the boning rooms have had to freeze substantial volumes of middles, as they have not been able to sell them.

- The sale of domestic boned leg meat for ham has declined dramatically, with one of our carcase customers reducing sales from 500 ton per quarter to 125 ton in less than two years. The reason given is the increase in imported product at extremely low prices. Legs are now being sold as bone in, the increase in numbers of sales in this category has led to a decrease in price of twenty percent, compared to the same time last year.
- Most boning rooms will sell varying amounts of product into fresh retail, manufacturing and export markets. The more product they sell into manufacturing the lower the carcase price they have offered producers this year compared to 2006.
- QAF sells around 400,000 carcases to these types of customers and are currently receiving on average forty five cents per kilogram less than this same time last year. This equates to a reduction in revenue of $32.50 per carcase.

A number of factors have and will affect the industry's profitability:

- Market Mix within Industry. The industry has invested significantly to increase pork's share of the domestic protein market. We have seen this figure go from 8 to 12 percent in one of our major supermarket chains. This increase in demand has helped ameliorate the effect of increasing imports until the surge in 2007;
- Weather Conditions. The drought over the last two years has affected cost of production via its effect on feed ingredient price;
- Exchange rate increases have affected our competitiveness in the export markets, especially Japan;
- Product Quality. Over the last eight years, the major emphasis in our genetic program has been on product quality. Genetic lines developed at QAF have been successfully marketed in the United States. We therefore reject strongly the assertion that one of the major drivers for imports is improved product quality because of the superior genetics available overseas.

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

QAF has suffered serious injury in 2007 due to the increase in imported product and we have no reason to alter our prediction that this suffering will continue. This belief has led the company to remove sows from production for the first time in its 37 year history. We are currently reducing our sow production base by 16,000 sows for 2008, to minimise our exposure to the manufactured product market. The increase in imports has negatively affected QAF's business in a number of ways:

- Feed milling is basically a volume business. The reduction in our production base and therefore feed required will increase our cost of manufacturing feed by at least 10 percent;
- In 2008 QAF will produce 300,000 less pigs from its production facilities. The weight of the remaining pigs will decrease by four percent as they will be directed more to the retail market which requires a smaller carcase than the manufacturing market. The reduction in both weight and volume will increase our production costs by an estimated twelve cents per kilogram;
- Similarly, the abattoir's efficiency is significantly affected by volume and weight of pigs slaughtered. The forecasted reductions in production will increase our slaughter costs again by at least 10 percent;
- The major effect of increased imports over time on our boning operations has been one of opportunity cost. Up until 2005 our boning operation was based on processing relatively heavy carcases, where the different cuts were marketed into the export and manufacturing sectors. The manufacturers continued switch to imported leg meat eventually made this business unsustainable;
- Our industry is facing a longer term higher cost structure due to constrained carcase weights. A major factor that allows the US industry to compete in Australian markets is the cost reductions that they have been able to achieve in both their pig production and primary processing sectors. This has occurred via a continued increase in their carcase weight which is currently above 100kg. While the Australian manufacturers have taken advantage of the lower prices out of the US, they have restricted the carcase weights in Australia by payment matrices which heavily penalise carcase weights above 70kg and eleven millimetres of fat at the P2 site. These restrictions have been put in place to provide the processors with bone in hams and full rasher bacon products;
- In 2007 the reduction in the relative prices, caused by the sudden supply increase from exports, received for either carcases or boned product destined for manufacturing has cost QAF in excess of twelve million dollars in lost revenue. In 2008 our total revenue will reduce by twenty five percent with our decrease in production;
- The production decreases in 2006 will obviously flow onto reduced capacity utilisation in our feed milling, pig production and abattoir business. Added to this is the loss of experience in all of these enterprises which will occur with the retrenchment of over 200 staff. The downsizing of these businesses will have significant effects on a number of regional communities in Victoria, where we are a major employer and purchaser of local services.

What safeguard measures would remedy serious injury?

QAF supports the industry's call for both significant provisional and longer term safeguard measures. Also we believe there is scope for assistance in the following areas:

- Exit with dignity packages;
- Increased support for innovation. Australia's ability to compete internationally will rely on our continued ability to lower our production costs, especially with respect to feed, and the development of new retail products for both the domestic and high value export markets;
- Continued support for AQIS. We have unanimous agreement that our major competitive advantage in Australia is our health status. The dramatic effect that an introduced disease can have on an industry has been recently illustrated with the Equine Influenza outbreak in the racing industry. AQIS needs the resources to be able to continuously review bio-security protocols in the light of new findings and audit the compliance of current protocols used in the pork industry;
- Government support for APL's suggested changes to the management of our levy system, which will increase the flexibility of the industry to react to emerging issues;
- Government to fund the producer levies for a period of 5 years.