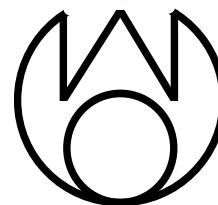


WINDRIDGE FARMS

Po Box 50
Young NSW 2594
Ph: 02 6382 1311
Fax: 02 6382 4280



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Windridge Farms Background

Windridge Farms is owned by a local family. Windridge has 3,500 sows breeding and finishing for domestic and export markets (55 to 95kg carcass weights). We produce 107 tonnes of pigmeat each week.

Windridge also runs 1100 cattle and 17000 sheep and grows about 800 hectares of crop each year. We have our own feedmill, which processes approximately 30,000 tonnes of feed annually.

Windridge has 52 permanent employees, with an annual wage bill of \$2 million. We are one of the largest private employers in the Young District. Many of the other private employers in our area provide seasonal jobs. All our staff are employed on a full time permanent basis.

Improved productivity and reduced costs have constantly been sought through capital improvements, use of the best available technology and management practices, and achieving economies of scale. Not only each piggery built but every new shed that has been built has been different to the last as a result of incorporating new ideas. Industry technology is constantly changing.

Increasing the skill and motivation of our team has also been an ongoing focus of our business. A productivity bonus was introduced in 1996 for managers and staff. We have a system of annual awards for the best performing teams and individuals. We also have a Feel Good Fund for team meals as rewards for teams who have put in extra effort.

In 1998 Windridge began a traineeship scheme, training new staff internally to reach national competency standards. In 2000 we implemented the next level of training, for those who successfully completed the traineeship using APL developed package Prohand. In 2005 Windridge assisted a smaller local piggery to implement a similar system with Windridge as the registered trainer. We are now in the process of adding another level to our traineeship and changing to improved materials provided by the National Centre for Pig Training & Education.

As is clear from this brief history Windridge is a dynamic progressive business. Much of Windridge's growth has been funded with profit surplus. We have been able to borrow to buy additional land but not to build, upgrade or repair piggeries. We have a strong relationship with our bank and with the buyer of our pigmeat – BE Campbell.

Strategic Plans

Windridge is currently part way through a long term strategic plan to expand and renovate. The aim of the plan is to consolidate Windridge's position as a low cost producer of large volumes of consistent high quality pigmeat. This position is critical to maintaining our

attractiveness to the other members of the supply chain and our profitability. We also need to make changes to allow compliance with new laws and ever increasing standards expected by the community and government.

The strategic plan involves:

- Renovation of existing facilities to maximise the use of existing equipment whilst also upgrading. These sites are currently farrow to finish and will be converted to breeder only sites. This will also involve changes to comply with the new animal welfare code.
- Building new facilities for grower pigs.
- Separate site production allowing better management of health and reducing the potential impact of a disease outbreak.
- All sites will use new feed technologies to allow more efficient feeding and use of more diverse ingredients thus lowering cost of feed.
- By moving the bulk of the pigs to new grower sites better environmental management will be able to be achieved.
- Purchase of neighbouring land to increase security of existing sites without enough land.

The total cost of implementing the remainder of this plan, excluding working capital, is approximately \$13 million. It is hoped some of this cost might be borne by contract growers, either with existing piggeries or broadacre farmers wishing to diversify. The end result will be a larger and more efficient operation with a 15c/kg lower cost of production.

Due to the increased levels of imports and our resulting inability to recover the increased costs from ongoing widespread drought, our strategic plan is on hold. Instead of being able to improve our efficiency we are stuck with increasing debt levels and depreciating equipment and buildings. We are made much more vulnerable due to our inability to complete the needed capital works let alone adequate repairs.

Note on capital value: The value of Windridge Farms' business is highly dependent on the viability of the pig industry in Australia. All of the buildings that Windridge Farms owns have been specifically designed to house pigs and are not suitable for housing other animals or for any other use. Thus when the pig industry is not viable, the buildings are worth nothing and the value of the business is reduced to the value of the land we own. The land value is approximately half the building value, thus two thirds of the value of our assets will be wiped out if the industry is not viable.

Competitive Advantages

Windridge has some key competitive advantages that have allowed us to remain in business to date despite some difficult periods for the industry. These are as follows:

1. High carcase weight

Our carcase weight has in the past been 10kg over national average, reducing our cost of production per kg by an estimated 15c/kg. Achieving this higher carcase weight involved significant capital expenditure – approximately \$3 million invested in new housing for pigs and another \$1 million in additional working capital. Additional land was also needed with a value of \$2.5 million. Unfortunately we have not been able to maintain these higher weights as we have been forced out of supplying the heavier weight domestic processing market by imports. In addition the heavier carcase export markets our supply chain had developed have become less profitable due to exchange rate movements. Until now we have maintained a

regular but smaller supply to the export market in order to maintain the relationship and keep the door open for more profitable times in the future. Unfortunately it seems most unlikely our supply chain will be able to sustain this now although the export market viability is still marginal we cannot sustain this due to the lack of profitability in the domestic market.

Our carcase weight is much lower than our international competitors. We cannot increase our weight further without one of the following:

- reduced imports so we can access a proportion of the domestic processing market,
- changes to market specifications from domestic retailers, or
- a drop in the AUD so we can export a larger proportion of our weekly kill viably.

2. Low feed costs - byproducts

We use byproducts from food processing in our feed reducing our costs. Our “normal” feed includes wheat, lupins, triticale, peas, oats. Often we purchase parcels of these grains which do not make premium human consumption standards. We also use canola meal (byproduct of processing for canola oil), millmix (byproduct of flour processing), sunflower meal (byproduct), soya bean meal, and a variety of other products depending on prices and availability. The above products are commonly used by intensive livestock businesses. Diets for pigs are formulated by combining different products to achieve the nutritional requirements at the lowest overall cost. A well-established market for these byproducts and off specification grains is a significant advantage to the original farmers who produced them as it helps maintain higher returns for their crops.

We also use some less common byproducts. For example, wet, liquid or dry human or pet food products in bulk or retail packaging, which are unsaleable for humans for various reasons, such as use by date. We have built special purpose machines to remove retail packaging and hired extra labour in the past to use these products when they are available. This allows us to beneficially reuse products, and recycle packaging that would have gone to landfill and sewerage otherwise. In one of these projects over 2,500 tonnes of product was diverted from Sydney landfill and beneficially reused. In another 8,600 tonnes of product is diverted every year from use as an inappropriate fertiliser and landfill in regional NSW. This is a cost saving to us and to the suppliers but also a significant benefit to society for which we are not rewarded.

3. Low feed costs – own feedmill

We have our own feedmill, which we have spent \$1.1million upgrading in the last few years. This will provide improvements in feed quality, efficiency and capacity but was also necessitated by old equipment wearing out. Due to low cashflow caused by low pig prices as a result of imports this project had to be financed by additional debt. These sort of capital costs are necessary to compete but also need to be able to be recouped eventually for the business to stay afloat.

Feed is by far our greatest input cost. We use approximately 4 kg of feed to create every kg of meat. Any improvements in feed efficiency and costs will have a significant impact on our ability to compete. The focussed research and development as being carried out by the Pork CRC will help but research takes time, particularly to be fully commercialised, and improvements tend to be small and incremental – not enough to make up for depressed prices at a time of high costs.

4. High health status

This means we do not have many of the diseases, which are common in pigs in Australia, or those common in the rest of the world. Particular common Australian diseases that Windridge Farms' pig herd does not have include mycoplasma hyopneumoniae, serpulina hyodysenteriae, serpulina pilisicoli, mange and most strains of actinobacillus pleuropneumonia. Windridge Farms' health status is very important as it minimises our production cost, minimises the use of antibiotics and allows us to market our pork as "clean and green".

We have invested a significant amount of money in developing the high herd health status. 3 of our piggeries have been fully destocked and restocked in the last 12 years. We have built and run a special quarantine site to allow introduction of breeding stock without jeopardising our health status. We have many other practices, which we implement at some cost to protect our health status.

Higher levels of imports increase the risk of importing exotic disease significantly. The biosecurity risks at the level of imports seen in the last 6 months, was not even considered by Biosecurity Australia in its Import Risk Analysis. It is very frustrating to have this surge in the level of risk completely ignored.

5. Strong supply chain relationship

All Windridge's pigs are killed at the Burrangong Abattoir for BE Campbell. The pork is then sold domestically to Chinese restaurants and butchers, wholesalers, supermarkets, processors, and exported to Japan and other countries.

Windridge has a long-term contract for the supply of pigs to BE Campbell. This has been beneficial for both parties in reducing extreme price fluctuations and maintaining consistency. Both businesses try to work closely together to maximise value in the supply chain. However, limits are ultimately set by processors who choose from cheap subsidised imports under pressure from retailers. The retailers make large profits regardless of supply market dynamics and who are often inflexible about specifications and prices. Final consumers are not really given a choice as labelling is misleading at best and compliance with labelling laws is poor.

Unfortunately to date we have found it has not been possible to obtain enough similar contracts from grain producers. Most grain growers were only willing to sign contracts a few weeks before harvest this year. This stems from their significant production risk – unpredictable weather determining if they will have any product to sell at all. We have developed new plans on this front in the last 6 months and hope we will be able to contract a greater volume of grain for longer time periods in the future.

Australia's advantages

- High health status
- Clean green image
- Geographical location
- Relatively low population density.

Australian pig industry and Windridge's disadvantages

- Other countries government's assistance to their pork industries.
- Destabilised local market due to imports. Several factors are important including, subsidies in other countries, which also change from time to time and supply changes in other countries – the changes from one year to the next are often larger than Australia's entire annual pig production. Imports may only be of one part of pig but as the pig is an unchangeable unit, returns for the processor from the whole pig is impacted and hence price of the whole carcass to the producer is affected.
- Apparent ability of countries importing to Australia to absorb exchange rate, input cost and other price changes. Particularly in comparison to an Australian pig producer who has very little control over input or output prices and no subsidies to assist.
- Increased uncertainty caused by changes to quarantine and import levels, impacting both
 - price through increased import levels, price wars between importers and
 - costs through 95% chance of devastating disease (PMWS) introduction in next ten years.
- Corruption of markets in countries we export to, eg gate price system in Japan.
- Adverse movements of exchange rate over last few years.
- High cost business operating environment – particularly high levels of regulation of our key input costs, feed (AWB and ethanol mandates and subsidisation) and labour markets.

International Competition

It is difficult to find accurate figures, measuring like with like, to allow sound international comparisons. However, the figures we have seen reinforce the impression gained in our visits to pig producers in other countries: with a level playing field we should be able to compete with the bulk of the producers in the countries importing to Australia.

Productivity in North American piggeries we have visited is very low by comparison to ours. In fact it would be considered a disgrace and would significantly impact our costs to operate at such levels of reproductive and grower efficiency.

On the other hand European piggeries we have visited, ranging from 200 sows to 6000 sows, had high physical productivity but extraordinarily high capital and operating costs, which could not possibly be afforded in Australia. We spoke to these producers about possible alternate lower cost systems and they were not interested, whereas Australian producers are always trying to find a new way to do every task at lower cost.

The key point is that the playing field is not level. Our government needs to act, as other countries governments do, to help level the playing field within legal WTO limits at appropriate times, not tilt it further against us.

(Please see producer subsidy equivalents for pig industries in Denmark, Canada, USA and Australia.)

Local Economy

Piggeries are capital intensive, labour intensive and input intensive. These characteristics are all good news for regional communities. In 2001 we analysed our costs by location of the vendor. We found that we spent:

79% of our operating costs within 100km of Young.

97% of our operating costs within NSW.

There is no question that Windridge alone shutting down would have a significant impact on the local economy. The impact of other local producers shutting down would further this deleterious impact on the local economy.

Windridge pigs are killed at Burrangong Abattoir. Burrangong is the largest employer in Young, its viability is highly dependent on the local pig industries viability. If Burrangong were to shut down, due to a decimation of its “bread and butter business” in pig throughput, the impact on the Young and district economy would be devastating.

Ability to adjust to short term fluctuations such as those in import volumes

Export markets and processing markets require much larger pigs than the fresh pork market. It is neither easy nor quick for a producer to switch from production for one market to another. Short term changes mean at least one stage of the specialised housing is underutilised and existing stages of housing and feed systems do not match the flow and size of pigs.

Additional housing is required to produce larger pigs, from any given number of sows, as the growing pigs need to be kept for a month longer. Alternatively to change to smaller pigs requires selling down stock to get to lower weights, leaving sheds empty and increasing overheads per kg sold or increasing sow and sale pig numbers to maintain the same kg sold. Increased sow numbers would require increased farrowing housing and increased specialised weaner housing.

To provide the additional housing or significant renovations requires development applications, environmental impact statements, building, possibly additional land, and a period of lower sales and income whilst pigs are bred and grown to the required weights. These things can be changed but only with considerable cost, delay and compromise. It is not possible to change from one market to another in the short time periods that huge variations occur in import levels.

The changes to markets and thus our market requirements in recent times have meant we find ourselves constantly compromising our system to meet the new requirements and then to try to maintain total kg sold to keep our overheads down. There are many resulting losses to efficiency from these compromises. For example we have tried moving sows with their 2 week old litters into lactation pens in nursery sheds to allow us to produce larger number of smaller pigs. Unfortunately this has meant increased mortalities which we have been unable to prevent in the compromised housing in the lactation area and also in later stages where the pigs have to be put in pens designed for older pigs.

Importers are also unable to respond quickly to market changes as producers in other countries have exactly the same issues in making changes to their systems. In addition they have a shipping time lag. The wildly fluctuating levels of pork imports we see in Australia are not based solely on price or market signals from Australia. They are significantly derived from market issues in the source countries. For example, an oversupply in Denmark seems to cause higher levels of exports to Australia. This oversupply is in turn caused by protection of their domestic market and subsidisation. It seems unreasonable that Danish and EC government policies should be allowed to destroy our industry. We believe these countries take advantage of Australia's practice of not responding to their actions.

What have we done to help ourselves?

As has been illustrated earlier Windridge is committed to doing everything possible to help put our business in the best position to compete. Nevertheless we have in the last six months had to increase our borrowings to unprecedented levels which we are most uncomfortable with.

We have taken as much action as possible to minimise outgoing cash whilst prices are inadequate to cover our costs. We have been fine tuning our diet formulation and feedmill processes to allow usage of a wider range of ingredients to reduce costs as much as possible. This has been achieved with several compromises and a lot of extra pressure on staff to ensure deliveries are exactly on time, etc, as we have pushed storage and processes to their limits. This is not sustainable in the long term.

We have reduced our staff numbers by 10% moving staff from our maintenance team into pig attendant positions that became available. Consequently some of our maintenance work is on hold. This situation cannot continue indefinitely. We have also reduced numbers in our office and broadacre farm teams as a direct result of losses from pigs. These teams have a little more flexibility in tasks to be performed than do piggery teams. Now however our staff are stretched to their limit and again the situation is not sustainable.

We have also reduced costs in other areas we can. For example, we have reviewed health and medication programs and costs, and made any changes we can. We are not using as much professional advice as we normally would in order to minimise outgoing cashflow. Again this has its costs.

Likewise the industry as a whole and APL, have continued to take whatever actions are possible to put the Australian industry in the best position to compete. The industry has been in a continuous and intensive restructure program since 1970 when there were 40,000 producers all with very small herds. Now the industry looks very different with something like 4% of producers left, and an average herd size at least ten fold higher than in 1970.

The Australian pig industry is not resting on its laurels waiting for someone else to solve our problems. For example the industry focus on promotion of fresh pork over the last 5 years has seen consistent significant increases in consumption. However this is no guarantee of success. Threats to the industry have multiplied in recent times.

Unforeseen Nature of the Import Levels

In 1994 Australia maintained a strict but legal quarantine regime which rightfully prevented most imports of pork to avoid exotic disease incursions. This was believed to be unassailable and appropriate policy. Relatively little of the worlds pork was traded internationally. Australias pork producers were viewed as competitive with those in Europe or America, due to abundance of local grain, wide open spaces, high health status and reasonable technical performance. It was generally accepted at the time that subsidisation and protection of world agricultural markets would decrease. Indeed it was expected that Europe and America would not be able to afford financially to maintain their programs.

Since then there have been many unexpected developments impacting on pork import levels:

1. Australia has changed to a relatively lax quarantine policy in general. There have been a raft of disease incursions with increasing frequency showing the impact of this change in policy.

The change in policy was not debated openly but rather has happened by stealth. It was not foreseeable and indeed is still not understood or realised by many Australians.

2. Australia has relaxed the pork quarantine policy much further than for many other products. Indeed the current policy is to allow imports of pork even though the Federal Court determined that “no reasonable man” could have made the quarantine decision allowing them, and the CSIRO review of the import risk assessment showed a 95% chance of exotic disease incursion. That an Australian quarantine decision be made on this basis was completely unforeseeable and hard to believe even with hindsight.

3. Australia traded quarantine access in a free trade agreement with America. That this could happen in this country is astounding. It is however, openly recognised as having happened in the USA-Australia free trade agreement by Americans.

4. World trade in pork has increased dramatically in spite of highly corrupt markets. This was not foreseeable. Indeed predictions were generally that this was unlikely to occur.

5. There has been no decrease in agricultural and pork industry protection in Europe and America – quite contrary to expectations.

6. It was not foreseeable that Australia’s small market would be of any importance to large producers such as Denmark, Canada and the USA. This is still hard to rationally explain. We believe this has been enhanced not by prices but by the easy access provided with demonstrated lack of consequences for dumping or making destabilising changes in volumes of product.

7. The movement of the Australian Dollar exchange rate in recent years was not foreseeable.

Serious and Permanent Injury

Our business is currently sustaining a negative cashflow. Our bank is currently supportive but will not fund this situation indefinitely. The pig price needs to increase rapidly to prevent bankruptcy for those who have chosen to stay in the industry till now.

The pressure on owners, management and staff who are all trying to do the best they can to minimise costs and maximise output is also taking a toll and is not sustainable. We have had staff offer to take paycuts to assist in survival of the business.

The current exodus from the industry is significant. We are personally aware of 5,500 sows from commercial family farms exiting the NSW industry mostly just from our area. One local feedmill has said 50% of its producers have already told them they will not require feed after Christmas. Many farms have taken drastic action, such as aborting sows, to reduce their numbers quickly and reduce the cashflow lost. In previous crises this sort of drastic action was never discussed. The reduction proposed by QAF is dramatic and highly significant as they have never taken action like this in previous crises. Our supply chain is already most concerned about a shortage of pork in Australia in the next 6 months – however we are not being offered prices to allow us to stay in business for long as the whole supply chain has to compete with imported product.

It is not just producers who are sustaining serious injury. Abattoirs and boning rooms are also dependent on enough volume of domestic pork to keep them in business. If the immediate reduction in supply is too great some of these businesses will close down even though in the longer term they may be needed. It may not be possible for these businesses to reopen once closed. Even a temporary loss of such a large number of jobs in towns such as Young would significantly damage the economic and social fabric of the town in a way that may take

decades to repair. In addition if some abattoirs close down, the piggeries that are still operating near them will incur greater transport costs to get their pigs to another abattoir.

It is critical there be a safeguard action to allow adjustment to the new market dynamics and give individual businesses time to put in place the necessary changes before they are decimated. If this does not happen we believe the reduction in the productive capacity of the industry will be so great that there will be a deficit of supply to the freshmeat market. The consequences of this are tragic for the industry on three fronts:

1. Domestic consumption of fresh pork will fall. Hard won changes in consumer habits which have been achieved over the last 5 years will be reversed and may never be regained. Evidence of increased consumption is not just the statistics – although these are impressive. Pork is now on more menus than it used to be. It is being featured more now as an accompaniment to wines, and to flavourings, sauces and spices. If there is a shortage this will change and the significant resources used in achieving this will have been wasted.
2. Domestic processors who have remained loyal to Australian pork so far will now have to use imports. Once this change is made it is unlikely we will ever be able to regain the same loyalty again.
3. Export markets – which were initially hard won, and since then have been maintained often at considerable cost will be unable to be supplied.

These outcomes will be tragic because the industry has created, and retained through previous difficult times, so much value in these markets which will now be destroyed.

We might be (we are not certain of this!!!) one of the businesses which survives in the above situation – and thus we might benefit from the shortage of supply for fresh pork and extreme high prices. However, we believe so much damage would be done to our demand base, the industries genetics, suppliers and staff base that this would not be a good outcome. We believe the price and supply levels would also become increasingly unstable which would make long term survival more difficult.

Entrepreneurial producers are unable to ride out this crisis let alone expand as their finances are already stretched by years of drought and poor prices. Investment in the pig industry is costly and high risk due to single purpose assets at the best of times. Banks and investors are not confident enough of the stability of prices, the industry or government policy on imports or grains to support expansion at a time like this. Many who would like to stay in the industry are having enough trouble gaining support to hold on for a few months.

Costs of a safeguard action

Higher costs to consumers are generally quoted as a cost of a safeguard action. It is highly questionable that consumers do actually receive lower prices as a result of imports in the first place. Large retailers generally maintain stable retail prices in spite of lower input prices. This means the only part of the supply chain to benefit from imports are the secondary manufacturers and the supermarket chains. We believe this is the case the majority of the time.

If the safeguard action is not taken consumers will suffer from extreme fluctuation in the price of fresh pork due to the significant shortage expected. They will also face less choice in the processed market – in particular they will be unable to purchase ham or bacon grown to the high standards of food safety, animal welfare and environmental sustainability that are required by the Australian community.

It is also generally assumed that safeguard protection will prevent the industry restructuring. This is not necessarily correct, particularly if the assistance or safeguard is temporary. Given the industries history of dramatic restructuring and the ongoing industry driven plans for restructure in the future it is not reasonable to assume a complete halt to restructuring as a result of any government assistance. Lack of profitability is far more likely to halt constructive restructuring through investment in better technologies and systems.

Also see earlier points about losses of jobs and income in regional areas where there is no alternative employment.

Conclusion

Windridge has a strategic plan, which when implemented will improve our competitiveness. We do have several competitive advantages in the Australian market place but are still struggling to survive. APL and the Pork CRC have programs in place which we support and which, when completed will create further opportunities to increase our competitiveness.

For Windridge, and the pork industry, to survive we need reasonable and more stable pig prices to generate profits to fund improvements to our systems. This is unlikely with the threat of ever increasing and unstable levels of imports in the Australian market.