AUSTRALIAN PIGMEAT INDUSTRY

Productivity Commission Submission

Australian Markets for Pigs and Pigmeat

(Draft finding 2.1)

A statement of fact is that a larger percentage of pig production is in fewer hands with the largest three percent of farms managing over half the breeding stock. This trend will continue as the industry adjusts to competitive pressures from other meats and imported product.

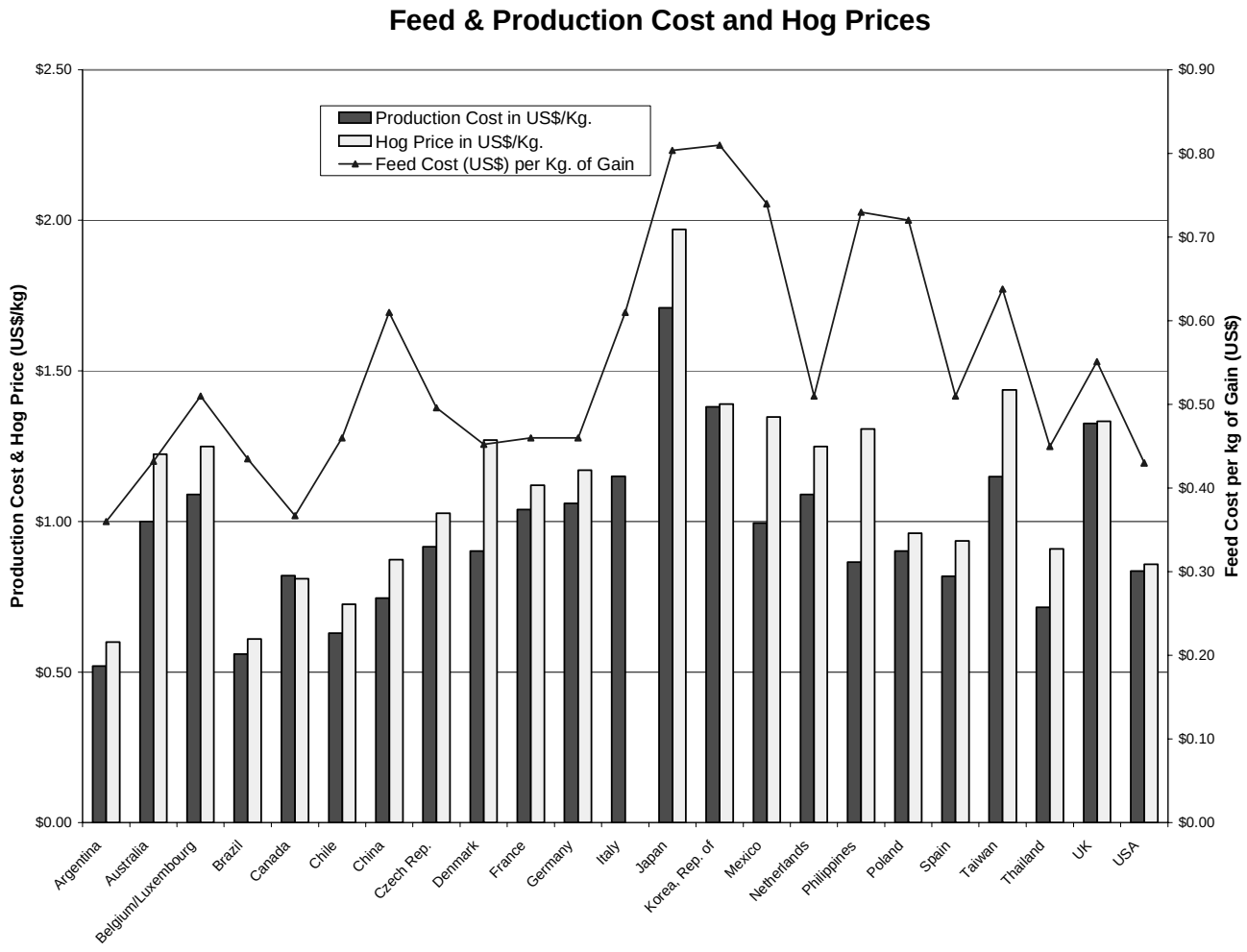
The request is that whilst this adjustment takes place investors in the industry are permitted to exit or consolidate. A safeguard action whereby it allows this process to occur is warranted. This is a SOCIAL RESPONSIBILTY of a government. Its people look to government for protection of sovereignty and social welfare. Current investors in the Australian pork industry

Quote: *"During our recent negotiations with our supply chain partners we continually got barraged with the prices they could buy imported pork for. The threat was not even what they bought for but what they could possibly buy for. This puts a ceiling on our price. This is with our supply chain partners. We buy Australian grain, Employ Australian people, pay Australian wages, pay Australian prices for goods and services and then pay Australian taxes.*

"What does the Australian government receive out of bringing in a product that Australia can supply itself competitively when our grain prices are at world parity?"

See the table 1 on world production costs and feed costs per kg of gain (source PIC USA). The key analysis is not the feed cost itself but rather the efficiency of converting that feed into meat. Australia is competitive and with the CRC funding will pursue further improvements.

Table 1:



The Australian pork industry cannot compete with subsidised imports and the Productivity Commission has admitted that "Pig producers do not receive significant direct subsidies, although pig producers in the European Union, Canada and the United States have benefited from reforms in the feed grain sector."

This submission refutes the allegation that safeguard action would "blunt incentives for producers and processors to adjust to the market environment"

Australia requires a level of imports to supplement and support consumption of pork. Whatever that level is we ask for some 'breathing space' to adjust any increase in consumption by product development and differentiation.

The global market will force adjustment upon the industry. We cannot operate in a vacuum and divorce our economy from global supply and price influences.

There is more than significant economic pressure on local pork producers to continue to stay focused. It seems a naive statement that ”farms need to be well managed and located, targeting markets in which they have competitive advantage”.

The progressive Australian pork investor benchmarks their output and costs of production with national and international pork producers. If there is significant distortion then the investor adjusts, improves or eventually is forced to exit as the required return on funds employed deteriorates below acceptable levels.

Industry Competitiveness

(Draft findings 3.1 to 3.5)

Exchange rates

A high exchange rate can have a major impact on the Australian pigmeat industry via both an increased attractiveness of imported product as well as a reduction in export capability of chilled and frozen products. This can result in an inconsistent return for both the producer and processor. As these rates are uncontrollable, on a short to medium term basis, by government and completely uncontrollable by the industry, alternative strategies to counteract them must be developed. One such strategy that is available is supplying a consistent, quality product that consistently meets the customer’s demands. Whilst supplying such a product is achievable the relationships between customers and producers needs to be well maintained and strengthened such that pricing agreements are more elastic and allow for normal changes in exchange rates.

Exports

The world consumption of pigmeat has increased in recent years (Australian Pig Annual), therefore one would expect the opportunity for increased pigmeat exports should have followed suit however the opposite has been the case.

Australia has seen an increased opportunity for pigmeat exports to Singapore and Japan in recent years due to factors such as the Nipah virus in Malaysia and more lately the substitution of protein sources in Japan as result of BSE domestically and in major beef supplying nations (Canada and the USA). Whilst these market opportunities have not been solely responsible, this time period has seen the value of pigmeat exports rise from $56 million in 1997-98 to $195 million in 2003-04. As a result of Australian exporters

capitalising on these events, the demand for pigs increased. With this competition in pig supply pigs within the required specifications were supplied with less regard to quality. As a result the variation in product has made some of the Asian importers more selective towards Australian product. Coordinated marketing strategies in markets have not fully realised potential.

These export opportunities resulted in a change of production methods for many Australian producers. Heavier pigs were being sought resulting in increased grower capacity being required and producer's increased their level of debt to build more accommodation. However fluctuations in exchange rates have seen a decline in the demand for heavy export pigs resulting in the under utilisation of sheds, leading to a fall in the profitable and therefore debt-servicing capability of producers.

The most economic market for pigs at the current time is the domestic market, which demands a 60 to 75kg HSCW, consequently the majority of pigs are being sold at such weights. It is difficult for the industry to remain competitive in the world market and respond quickly when markets do become available whilst we wait four weeks for the pig to grow to reach the weight required for exports into the Japanese market, 95-100kg HSCW. Whilst we are waiting for our pigs to grow, our competitors, Canada and the USA with an average slaughter weight of 90KG HSCW, have already supplied the correct product. Action: increase Australian slaughter weights.

Profitability

Economies of scale have been achieved with three per cent of producers operating half the national sow herd. In order for the other 97 per cent of producers to become more profitable they seek to form alliances to produce the number of pigs, which can be better marked to meet the requirements of processors.

Although this situation is good in theory, it is impractical in many cases due to the variation seen in environmental conditions, animal health, housing and management techniques. With the interaction of all three factors it is difficult to produce a consistent product.

A group of farmers, if linked, could all grow a similar pig from the same genetic base, they could also own a feed mill (achieving more efficient purchasing of grain and supplements) and so supply a consistent ration, labour savings could also be made by utilising labour units more effectively over the alliances farms at busier times. With careful sorting of pigs

this group could supply several markets at a competitive advantage over a single producer. This is a feasible model, but not applicable across the entire industry due to geography and proximity to markets.

This would be a similar situation to some European countries where the industry is highly vertically integrated with control of genetic and feed supply and pigs being highly targeted to meeting specific markets.

Potential Impediments to Improving Performance Competitiveness

(Draft findings 5.1 to 5.4)

A major goal to improve performance competitiveness in the Australian pigmeat industry is integration between sectors of the industry, with profit taking occurring throughout the system. Some major links in the pork supply chain work independently of each other to maximise returns for their sector, rather than looking at the fortunes of the industry as a whole. Subsequently revenues across the pigmeat industry can be cyclical with periods of high and low profitability rather than a consistent level of income, further decreasing the attractiveness of investment into the industry.

Overseas Trade Barriers

Australia has implemented a Free Trade Agreement (FTA) with the United States of America. This would appear to be disadvantageous to the Australian pigmeat industry, with the reciprocal trading measures and the differences in cost of production and product specifications, this would appear to be a situation where the flow is only one way.

The producers have little or no control over this situation. It is controlled by politicians whose agendas are unrelated to the pork industry and thus producers are often washed aside for further political gain.

As the world becomes more fearful of international terrorism each country wants to become more self sufficient in securing its own food supply for the nation. This situation may be implemented through the use of quarantine procedures and tariffs, leading to more and more breakdowns in the protocols involved with free world trade. In the trading world these breaches of world trade laws are becoming harder to and more expensive to prove.

Domestic

Although the domestic consumption of pork has increased by nine percent, the consumer has become accustomed to a stable price for pork products available in the supermarket. This has become possible by processors importing product, which maintains a stable price. Unfortunately due to the natural variation of product available from producers the secondary processors and the major supermarkets prefer the imported product, bought at specification, to maintain consistent product available to the consumer.

Although the consumer is mainly price driven a labelling system showing the fact that it is produced and processed in Australia would be beneficial to the industry, as consumers have shown a willingness to purchase home grown product.

Single Desk Marketing

A major impediment to profitable pig production is the varying cost of grain. The single desk marketing of grains such as wheat and barley through groups such as the AWB sets an artificial base price for grain. This was evident throughout the drought of 2002-03, when a significant amount of grain was bought through this system, which was being held well above world parity pricing. Producers should be able to purchase raw ingredients for their rations more efficiently but are prevented from doing so by regulation protecting single desk selling.

Measures to Improve Industry Competitiveness

(Draft findings 6.1 to 6.4)

Increasing economies of scale make it possible for producers to be more competitive. They achieve this by forging links within industry to obtain better prices for their product and by having greater purchasing power for inputs such as consumables and basic commodities like grain and milled feed. In most cases the smaller producer, which equates to 97% of those involved in the industry are price-takers.

Single Desk

The single desk market for grain has a virtual monopoly on grain sales. Although larger producers have the buying power to negotiate for large parcels of grain from growers, the majority of smaller producers are faced with operating in an anticompetitive system. The

industry is a small identity, compared with the AWB and would appear to have little or no political power to increase the competitiveness in the grain industry.

The industry has to develop methods of obtaining more cost effective grain. Producers have the option to form alliances and increase their purchasing power. These alliances need to have supply contracts with grain growers restricting their ability to inflate the grain price. It would often be beneficial for grain growers to form alliances with either pig producer groups or feedlotters as the payment terms would be shorter than those presently in place with the AWB under the pool system.

The government needs to monitor the single desk marketing system for grains to ensure that Australian grain users are not disadvantaged by anti-competitive actions. Other methods of securing cost effective feed supplies include increasing the quotas of imported grain, not only wheat and barley but also alternative feed grains such as corn. This in turn would create other issues, such as a review of importation protocols, grain treatments and a greater distribution area for these grains. But at whose cost – grain grower or grain user?

Risk Management

After the recent period of reduced profitability, many producers have sought and achieved long-term supply agreements with processors. Larger units have achieved this more frequently whilst some of the medium to small producers have formed alliances enabling them to market a larger number of pigs. However, difficulties occur due to the natural variation of pigs under this system, through factors such as environment, animal health, feed and management practices resulting in an increased distribution curve. Although this helps the processor with throughput, it does not help with the marketing of the processed pork. Help is required for these producer groups to establish a good supply chain network so every party in the chain makes an acceptable return and the risk is minimised.

Research and Development

The establishment of the Pork CRC will investigate and develop ways to reduce the cost of production. Through research we can lower the cost of production by improving feed efficiency (FCR) and reducing costs per kilogram of pigmeat produced.

Research could also be conducted into utilising different feed sources, which may make the industry more resistant to fluctuations in feed availability and price.

Further Information

Chapter 3 ‘Seeks further information on relative merits of Australian Gene Pool compared with that of international competitors’.

This company has benchmarked its genes and is continuing to do so. The results are commercially confidential. We can indicate that the Estimated Breeding Value (EBV) results were comparable and competitive in terms of progeny growth rate, fat levels and conformation, leg structure, etc.

L02 (n=22) and L03 (n=23) females from North American Nucleus herd were inseminated with semen from five L02 and five L03 boars imported from Australia. Performance information from 1,576 L02 and L03 animals off-tested in weeks 21 through 29 of 2004 (125 AUS and 1451 BLU) from these matings were analyzed to study line and source differences in weight per day of age at the start (wdas) and end of a 13-week test period, average daily gain, days to 100 kg, front (fleg) and rear (rleg) leg scores, teat number, and ultrasound P2 and loin depth.

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PIC Australia **February 2, 2005**