

SPC ARDMONA



**SUBMISSION TO THE
AUSTRALIAN PRODUCTIVITY COMMISSION
SAFEGUARDS INQUIRY INTO IMPORTS OF
PROCESSED FRUIT AND PROCESSED TOMATO INDUSTRIES**

Date: October 2013

SPC Ardmona (SPCA) rejects the findings of Productivity Commission's (PC) reports on provisional safeguards. SPCA believes that the reports are unbalanced (listing every argument against safeguards) and contain many factual, analytical and judgemental errors.

Numerous errors in the report lead SPCA to conclude that the reports are of poor quality, lacking analytical and commercial rigour.

In addition to these errors, SPCA is concerned that the PC reports might have disclosed **commercially sensitive information** which was provided in confidence by SPCA and released without our permission. Examples of these in the processed fruit report include confidential information on SPCA's profit and losses on page 46 and employment numbers on page 46 and sales, market share and capacity data on pages 41, 43, 45 respectively. In the imported tomatoes report, information on company production levels, profit and losses and employment levels (page 26-27) is similarly treated.

SPCA would like an explanation about what might constitute a serious breach of confidentiality with significant ramifications for our company in a fiercely competitive environment.

SPCA is also concerned that the PC's imported tomatoes report refers to the claim that the Australian Government has to apply "higher standards" of evidence and analysis in safeguards than other countries because of Australia's membership of the Friends of Safeguards Procedures group of WTO members (page 7). When SPCA made the submission we were, and to date remain, unaware of this group, the ramifications of being part of the group and its role in the PC's assessment of our application.

SPCA would also like to know if Australia's membership of this group is disadvantaging Australian companies in that they have to achieve a higher standard of proof to secure a positive outcome from a PC review.

SPCA believes that the report has many factual errors.

Some examples are given below.

Example 1: Supermarket ALDI's information ignored in the assessment

- Aztec scan sales data has been used in the reports to indicate retail market information such as market size, market shares and market growth. However Aztec scan sales data does not include sales of products through ALDI.

- ALDI has doubled the number of stores from 2007 to 2013 and now has over 300 stores on the Eastern seaboard. This is equivalent to approx. 19% increase in stores per annum over the past 6 years. In addition to this ALDI's average turnover per store is also increasing at approximately 6% pa.
- ALDI is a significant part of the market for our categories and our products. We have information from Aztec Home panel data to support this along with our knowledge from ALDI's tender documents.
- Sales of processed fruit through ALDI stores are predominantly sold as private label; therefore growth of private label products has been understated in the PC's reports.
- The implication of omitting this data is profound. By including ALDI increases the level and rate of import penetration increasing the justification for safeguards.
- The PC has had access to all of SPCA financials and import data insights to have corrected this.
- The information provided in the report for the retail market is incomplete and the conclusions drawn from it cannot be substantiated

Example 2: SPCA's cost of production: SPCA data ignored

- The PC report on processed fruit states *"There is some evidence that the increase in SPC Ardmona's costs of production was driven partly by increased variable costs, in particular factory labour. SPC Ardmona previously reported that labour costs had been rising and reached approximately \$33 per hour in 2012 (CFICA 2012). The Canned Fruits Industry Council of Australia also previously reported that growers have experienced increased labour costs, due in part to legislative changes related to orchard labour (CFICA 2012)."*
- The PC report commented on variable costs when no information on the breakdown of fixed and variable costs in the cost of production was provided by SPCA. On what basis has the PC been able to verify the variable costs without SPCA's data?
- Information provided on some key variable cost components indicates the opposite to the PC's conclusion above. For example, for fruit costs, prices paid for the raw fruit to growers was submitted to the PC. These highlight prices being flat or declining, yet this has been ignored in the above assessment.

- Labour cost increase has been cited as the reason for cost increases. However, average increases given to the Food Preservers (the key labour force for production) Enterprise Bargaining Agreement (EBA) by SPCA during 2010–2013 was 2.4% pa, which is much lower than the food industry average of 4% pa and the national average of 3.4% pa.

The conclusion is also flawed as the same report (page 46) highlights that: “*The data shows that the number of casual workers employed on a weekly basis has decreased by about 30%, while the number of salaried employees has decreased by about 19%.*”

Example 3: Domestic production volumes: Historical production volumes based on unverified source (CANCON data)

- The reports have cited unverified estimates provided in CANCON conference data for commenting on capacity utilisation and historical domestic production.
- The PC reports use this information for trend analysis despite SPCA indicating that these are estimates and are inappropriate for use in this context (refer email to the PC dated 6th August 2013).
- Apart from above, historical information provided in the CANCON data cannot confirm to be aligned with the products that are relevant to this inquiry.

Example 4: Impact of imports on unit prices

SPCA believes that the analysis carried out to establish the impact of imports on unit prices is flawed.

- The analysis carried out is at aggregate level and does not highlight the dynamics of sub-markets within each tariff code.
- Products within each tariff code do not necessarily compete with each other.
- The PC has ignored the evidence examples submitted by SPCA on 12th August 2013 to highlight that:
- SPCA disagrees with the PC’s statement on page 49 of the fruit report that “*the persistent unit value gaps between SPC Ardmona’s private branded products and both imports and private label products have fluctuated largely due to the changes in the retail prices for SPC Ardmona’s products, not prices of imports.*”
 - The PC report provides no evidence to support this assertion. Such an analysis would need to be carried out at product level not aggregate level due to the impact of varying product mix.

Example 5: Analysis of production volumes to assess increase in imports

The PC Fruit report states in section 2.2 findings that “*The ratio of import volumes to domestic production has increased substantially over time, growing from a low base, but recently at a slower rate than the longer term trend. This calls into doubt whether the WTO standard can be met*”

- SPCA disagrees with the methodology of using ratio of imports to production to derive the findings.
- The ratio analysis fails to take into account:
 - Impact of stock carry over in the domestic production number from year-on-year.
 - Massive stock write-offs that SPCA has had in recent years and had informed the PC about.
 - Timing differences between domestic production, imports and sale of goods.
- As stated earlier, production data from previous years is unverified and inconsistent with SPCA submitted data for recent years

SPCA has concerns that inconclusive and anecdotal evidence has been used to support the arguments in the reports.

Example 1: The PC report highlights on page 55 of Processed Fruit report that “*There is evidence of a long term reduction in overall consumer demand for processed fruit, whether imported or domestically produced.*”

- Evidence provided by the PC to support the above argument is incomplete as it does not include the sales of products through the ‘food service channel’.
- The food service market is a very significant part of the total processed fruit domestic market. This channel covers the sales of products through restaurants, canteens, schools, industries (i.e. mining), and Government departments including Health and Aged Care facilities, Corrective Services, Defence Force and Immigration
- Confidential evidence was submitted by SPCA on 8th August 2013 to the PC highlighting examples of import penetration in this market, yet this has not been taken into consideration to draw conclusions on market dynamics.
- In addition to the above, retail market size is also inaccurate as market information of key retailer ALDI has also been ignored in analysis as highlighted above.

Example 2: PC report for Processed fruit highlights in the report on page 55 “*this evidence of decreasing export volumes should be considered in conjunction with evidence of SPC Ardmona’s corporate strategy to use its processing plants overseas to supply the company’s branded products in export markets (Hattersley, Isaacs and Burch 2013; South African Fruit and Vegetable Canners’ Association, trans., p. 74, sub. 59).*”

- Why was the statement made by the South African Fruit and Vegetable Canners’ Association taken as substantiated proof of SPCA’s strategy?
- What facts were submitted to support this statement?
- Why was SPCA not asked to provide evidence of its operations in other markets to validate the above statement?
- **Example 3:** The PC report for processed fruit on page 61 states evidence from Ken Wilson (an Australian importer of processed fruit, appearing at the Commission’s public hearing as part of the South African Fruit and Vegetable Canners’ Association). “*For the two years immediately after the merger the prices went up in Australia by 40 per cent*”
 - Has the PC validated if this information is factually correct before taking this as evidence?
 - Aztec scan sales data over the period will highlight that the above statement is erroneous. Prices did not go up by 40% post the merger of the SPC and Ardmona businesses.
- **Example 4:** The PC report for processed fruit states on page 61 states that the South African Fruit and Vegetable Canners’ Association argued “*SPC Ardmona’s strategy is to push its own brands, whereas retailers are pushing their own private labels ... Until recently SPC Ardmona did not want to supply a product (branded) as required by the retailers.*”
 - Why was the statement made by the South African Fruit and Vegetable Canners’ Association taken as substantiated proof of SPCA’s strategy?
 - What facts were submitted to support this statement?
 - Why was a statement given by SPCA in the public hearing on 30th July 2013 (page 49 of the transcript on the PC’s website) not taken into consideration?

“I am actually not aware of us walking away from any private label contract. In fact we’ve won a few small ones of recent time. In fact we’ve been perhaps too aggressively trying to go after them, to win them, in a desperate attempt to keep this scale in the business, so one of the reasons we had such losses is that we’ve tried to keep pace with some of the import prices, much to our economic loss.”

Both PC reports list all the reasons why provisional safeguards should not be given, yet in the concluding sections the PC acknowledges two of the three key tests to satisfy the requirements for safeguards are actually met. However the PC identifies two key reasons (page 68 of the fruit report and pages 44-45 of the tomatoes report) for rejecting safeguards:

1. PC Finding 2.1 - Injury to the domestic industry has not been caused by an increase in imports.
2. PC Finding 2.11 - No compelling evidence of critical circumstances that would warrant provisional safeguard measure

SPCA disagrees with the PC judgement that the imports did not cause damage to the industry

The PC report states on page 63 *“Based on the evidence and analysis to date, the injury to the domestic industry has not been caused by an increase in imports of processed pears, peaches and fruit mixtures. It appears to have resulted from a combination of the following factors:*

- *reduced export volumes*
- *Rising costs of domestic production, driven by increased labour costs, and by declining economies of scale due substantially to reduced export volumes*
- *Long term reductions in the domestic demand for processed fruit products*
- *domestic retailers promoting private label brand products to compete with the sole domestic producer and with each other, as well as to improve reliability of supply and meet the shortfalls in domestic production”*

The PC’s analyses are based on incomplete or erroneous data as per the examples cited above. This means its conclusions cannot be justified.

- The PC report’s conclusion on impact of export volumes cannot be substantiated as no evidence was requested or provided by SPCA relating to this.
- As indicated earlier the PC analysis on labour costs is erroneous and its statements are contradictory.
- The PC report’s analysis of domestic demand is incomplete as it fails to capture key channels such as food service and key retailers such as ALDI.
- The PC has ignored evidences supplied by SPCA highlighting that in recent years supply of raw fruit and capacity to process has exceeded the demand.

The PC's analysis uses data selectively to produce erroneous conclusions. The PC report on processed tomatoes for example claims that while imports and domestic supply enabled certain supermarket pricing strategies to take place, it implies these did not cause injury because the price of imports themselves did not vary (when expressed in Euros).

- When the Australian dollar appreciated against the Euro by 45% from 2007 to 2012, it facilitated cheap imports to be used in private label brands hence impacting share of domestic products and causing damage.
- Why has the PC selectively chosen to cite price movements in foreign currency, while simultaneously acknowledging elsewhere in the reports that the appreciation of the Australian dollar was a factor in driving imports?

Finally the PC's conclusions on causation are convoluted and in fact give no clear rationale for the conclusion reached. They acknowledge that there have been persistent high levels of imports (e.g. Tomatoes on page 44) but it appears the key test the PC has adopted for rejecting provisional safeguards is an absence of "recently surging imports". The PC has not clearly identified the damage caused by the persistent high level of imports, nor separated the damage caused by imports from that caused by other factors (as it is required to do by the WTO Safeguards Agreement).

The PC also measures causation in terms of the ratio of imports to domestic production, which it cites as the test required in Article 2.1 of the WTO Safeguards Agreement. However the PC totally ignores Article 4.2 (a) which states:

*"In the investigation to determine whether increased imports have caused or are threatening to cause serious injury to a domestic industry under the terms of this Agreement, the competent authorities shall evaluate all relevant factors of an objective and quantifiable nature having a bearing on the situation of that industry, in particular, the rate and amount of the increase in imports of the product concerned in absolute and relative terms, **the share of the domestic market taken by increased imports** (emphasis added), changes in the level of sales, production, productivity, capacity utilization, profits and losses, and employment".*

SPCA provided detailed information on the ratio of imports to consumption in the domestic market, which included the data on ALDI referred to above. This demonstrated how import penetration had risen in recent times. The PC appears to have completely ignored these conclusions.

The PC's assessment of causation is therefore seriously flawed.

SPCA disagrees with the PC findings that no compelling evidence of critical circumstances that would warrant a provisional safeguard measure was provided.

The PC claims:

- SPCA did not provide compelling evidence to *“support its contention that its manufacturing facilities would be closed if provisional safeguards were not applied.”*
 - SPCA did not contend *“its manufacturing facilities would be closed if provisional safeguards were not applied”*. In fact the PC processed fruit report itself quotes only on page 64 what SPCA actually did say - namely that *“Closure of SPCA’s facilities is a prospect unless provisional safeguards provide a “breathing space”, followed by full safeguards measures accompanied by an adjustment plan”*.
- On page 66 of the fruit report that *“SPC Ardmona’s position as a subsidiary of Coca-Cola Amatil — a listed company which reported net profit after tax of \$215.9 million for the six months ended 30 June 2013 (CCA 2013) — suggests that a three month delay pending a definitive safeguards determination is unlikely to lead to circumstances that would be difficult to repair.”*
 - On what basis did the PC make this commercial judgment? Did the PC check this judgment with Coca-Cola Amatil before releasing its report?

Fruit growers are pulling out fruit trees because they cannot afford to spray against diseases – spraying which must be done now. A delay in safeguards of three months does make a difference to hundreds of growers and to the biosecurity of the horticulture industry.

The PC ignored this, despite SPCA and many fruit growers urgently bringing this to its attention.

Concluding remarks

This submission has identified only a sample of the factual, judgemental and analytical errors contained in the safeguards reports.

SPCA made representations to the previous government emphasising that we were opposed to the PC being given task of evaluating our request for safeguards. This was based on the PC's previous track record of opposition to tariff protection. We felt we wouldn't get a fair hearing. This too, was the view of many politicians we spoke to.

SPCA reluctantly agreed to participate in the PC Inquiry and did this in good faith and supplied comprehensive and compelling information that the application of safeguards was warranted. SPCA's original concerns have been vindicated by unbalanced and poor quality reports from the PC.

SPCA has accordingly urged the Federal Government to reject the PC's accelerated reports.

SPCA also calls on the Productivity Commission to review its accelerated reports on safeguards and urgently produce revised reports and recommendations and incorporate the findings of those revised reports in its reports on full safeguards.