

Submission
By Ridley Corporation Limited
to the
Productivity Commission

*Terms of
Reference
No. 3:*

The Factors affecting the Profitability
and Competitiveness of the domestic
pig farming and pigmeat processing
industries

Foreword:

With reference to the Productivity Commission Issues Paper dated July 1998 - Pig and Pigmear Industries: Safeguard Action Against Imports, this submission relates solely to the Terms of Reference No. 3. Ridley Corporation through its subsidiary Ridley AgriProducts is Australia's largest stockfeed miller, providing nutritional products across the entire range of animal species. It is Australia's largest manufacturer of specific diets for our pig industry, as well as a major distributor and supplier of specific ingredients and medicants to producers of all dimensions.

Ridley AgriProducts, as a major stakeholder in the pig industry, also supports the industry through the provision of technical advice and training to its customers, as well as numerous research and promotional activities.

Ridley both endorses and supports the introduction of measures to assist the Australian pig industry in attaining world-class competitiveness to enable a viable domestic industry to be maintained with export potential. For this to occur, there is a need to firstly stabilise the domestic market to create a base for the realisation of such an export market.

This submission has not sought to comment on the question of safeguard measures - Terms of Reference No.'s 1 and 2.

1.0 Executive Summary

The Australian pig industry, like others globally, is in the process of rapid and fundamental change. In Australia, the industry has been forced to very quickly adjust to world market influences, and has moved from a “protected” domestic industry, subject only to changes in domestic supply and demand interactions, to a more “open” market. The demanded rate of change for the Australian pig industry has exceeded its response rate, given its small scale by world standards. Imports of good quality products at relatively low prices may be expected to increase. This open market for pig meat is consistent with that of most other agricultural commodities such as fruit, flowers, fibres, etc.

Evidence from our feed operations in the United States and Canada, supports the contention that only those customers who meet high standards of uniformity and quality are able to survive in the pig industry which is now globally competitive.

The pig industry is changing structurally as the number of farms has reduced. As the number of participants has fallen, the industry has tended to adopt a defensive position as total output has remained stagnant. The “new wave” of pressure placed on the industry as a result of declining pigmeat prices must be met through initiatives targeted at structural and operational changes. Market information held by Ridley indicates that over the past six months there has been a marginal decline in its number of customers in Victoria and South Australia. There has, however, been a more significant decline in customers numbers in Queensland, which has a greater number of smaller producers.

In Queensland and South Australia over the same six month period, there has been an

increase in average debt per customer as well as an extension in the number of days the debt is outstanding (ie greater than 60 days). No real deterioration has been identified in Victoria, although 120 day debtors have increased. These figures do seem to indicate that the smaller segments of the industry, which normally excludes Victoria, are suffering financially.

The continued existence of a viable pig industry in Australia is assured as well as the potential for sustainable growth both domestically and in export markets if those producers that remain are able to supply a consistent, high quality product to compete against other meat products. The importance of Quality Assurance must also be stressed, as the focus of producers is not only to increase market share domestically but to increase the competitive ability to export Australian pork into new international markets.

Although the Australian industry per se is not at a competitive disadvantage when compared to overseas producers, it is evident that many individual businesses are. There is, therefore, a need for the pig industry in Australia to formulate a vision for the future setting achievable growth targets, and a plan of implementation to encourage the uptake of available improved technologies and systems to increase the efficiency of producers and quality of product. If this cannot be achieved, the high rate of attrition amongst small producers will continue. There must also be greater integration/strategic alliances of the various sectors of the industry so that pig producers are able to regularly supply processors with the required volume and uniform quality as a means to improve the pre- and post-farmgate performance of the industry. The improvement in productivity of the industry can only be achieved once

this integration is in place, and will result in the removal of many of the constraints which are now evident along the industry value chain.

None of these initiatives will be sufficient, however, to prevent a consolidation in the number of pig producers and nor should they. This highlights the need for adequate transitional arrangements to be put in place so as to encourage the removal of less efficient producers to allow competitive producers to meet the challenges of the ever changing global industry.

2.0 The Australian Pig Industry

2.1 The Domestic Market

Key Point: *There is a movement toward larger herd sizes as the number of small producers in the Australian pig industry declines. Sow numbers and output have remained relatively constant.*

The Australian pig industry has been characterised by declining farm numbers over the past twenty years as high cost producers have been compelled to exit. Over this period, the number of pig producers has declined from 22,000 in 1976 to 3,522 in 1996. To illustrate the shift to larger units, over this period the average herd size increased from 13 to 82 sows, as the level of attrition occurred largely within the sub-100 sow producers.

Although the trend of attrition continues, with the Australian Pork Corporation estimating that the number of farms with pigs fell by around 32% during the four year period December 1993 to December 1997, the national sow population has reduced only marginally over this period (around 2%). This statistic seems to indicate the improvements in productivity which have been made by the more efficient producers.

Table 1: Australian Supply and Use of Pig Meats

	Unit	1988	1989	1990	1991	1992	1993	1994	1995	1996 Prelim.
Pig numbers	'000	2,706	2,670	2,648	2,531	2,570	2,646	2,775	2,653	2,526
Breeding sows and gilts	'000	359	348	337	312	330	315	316	319	305
Slaughterings	'000	4,962	4,940	4,949	4,942	5,138	5,082	5,174	4,995	4,670
Average slaughter weight	kg	60.7	63.0	64.5	63.1	65.4	64.5	66.7	69.7	69.4
Production	kt	301.4	311.1	319.0	312.0	336.0	328.0	345.0	348.0	324.0
Total consumption	kt	293.4	304.0	313.5	311.8	335.5	321.6	342.7	346.9	327.0

Source: *Australian Commodity Statistics, 1997 (Page 155); ABARE*

2.2 Per Capita Consumption

Key Point: *Consumption of pig meat in Australia is low compared to other countries. The Australian industry has potential for growth.*

When considering the potential for growth in the domestic pig meat market, it is instructive to look at the respective consumption rates of competing meats. Outlined in Table 2(a) is a comparison of such meats, whilst Table 2(b) shows the consumption rate of pig meat in Australia compared with other selected countries.

Table 2(a): Per Capita Consumption of Meats in Australia

	1992 kg	1993 kg	1994 kg	1995 kg	1996 kg
Pig Meat	18.8	18.3	19.2	19.3	17.8
Lamb & Mutton	20.6	19.9	18.6	16.8	15.6
Beef & Veal	36.7	36.3	37.8	35.5	33.0

Source: *Australian Pig Industry Handbook: Pig Research & Development Corporation and Australian Pork Corporation, March 1997*

Table 2(b): World Per Capita Pig Meat Consumptions (Selected Countries)

Country	1994 kg	1995 kg	1996 kg
Australia	19.2	19.3	17.8
Denmark	66.4	67.9	65.7
Netherlands	43.7	44.2	43.0
Taiwan	41.4	40.3	42.9
United Kingdom	23.2	22.8	23.6
United States	31.0	30.7	28.8
China	26.9	30.3	30.0
Japan	16.8	16.7	16.7
Philippines	10.0	10.4	11.0

Source: USDA - extract from Australian Pig Industry Handbook: Pig Research & Development Corporation and Australian Pork Corporation, March 1997

As discussed in greater detail in Section 3, Table 2(a) illustrates the potential for growth in the domestic pig market if market share was able to be gained from competitive meat products. Table 2(b) also illustrates the scope for increased market share if the per capita pig meat consumption rate was to approach those of many other countries.

2.3 Export/Import Market

Key Point: *Over the past two years imports of low cost, higher quality pig meat have increased. Australian producers have lost market share in the high margin segment.*

Table 3: Australian Imports and Exports of Pig Meat

	Unit	1994	1995	1996	1997
Imports	kt	2.5	4.9	6.9	11.0
Value	\$m	10.6	17.9	27.7	44.9
Exports	kt	7.0	6.3	7.9	11.2
Value	\$m	24.1	29.7	35.9	44.3
Net Exports	kt	4.5	1.4	1.0	0.2
Net Exports	\$m	13.5	11.8	8.2	- 0.6

Source: Australian Pork Corporation - Pigmear Import/Export Summary

Imported pig meat products first entered Australia in 1990 and have rapidly increased in recent years. Canada is the major supplier of imported pig meat and although Denmark currently ranks seventh, it is expected to increase substantially.

Whilst up to 1996 Australia had been a net “exporter” of pig meat, the value of exported versus imported product differs markedly. The volume of exports had been relatively steady up to 1996, however, volumes increased by around 40% in 1997. Evidence from the industry suggests that the majority of this volume sold overseas is secondary cuts and at relatively low value and margins. With respect to imports, the volume has been increasing at a greater rate, rising around 60% in 1997. However, more importantly from the domestic producers’ viewpoint is the composition of those imported products. The imported product consists largely of the higher value and higher margin leg products. From Table 3, it can be seen that the unitised value of the average export price has fallen from around \$4.70/kg in 1995 to around \$3.95/kg in 1997, a fall of 16%. Over the same period, the unitised value for imports has increased by 12%. This exacerbates the impact on Australian producers who lose market share

in the higher margin domestic segment whilst selling export product in lower margin segments. As noted in Section 3 below, once steps are taken to improve Australian production processing facilities and techniques, the Australian industry should be able to compete more strongly with imported products on the basis of cost and quality, as well as have the potential to grow via exports. This should reverse the anecdotal evidence which suggests that the reduction in supply in Australia created by the attrition in smaller and/or less financially strong producers has largely been filled by imported products.

In addition, and in spite of the current financial difficulties experienced by many Asian countries, there are considerable opportunities to service key Asian markets as their consumption of pigmeat increases from the current low levels outlined in Table 2(b).

2.4 Financial Considerations

Key Point: *There is indication of economic distress in the industry. A new wave of pressure is causing small producers to leave the industry.*

2.4.1 Profitability Measures

It is obviously difficult to use nominal profitability figures for the pig industry to provide an insight into the profitability of individual producers. Based on a limited sample forming part of the study within PigStats '96¹, the expansion of group herd size contributed positively to the overall average profit result in 1996, with overall profit per sow increasing \$103 from one year prior. This means that the attrition of smaller producers has had a "positive" financial effect on the industry. However, this period

¹ Australian Pig Industry Handbook: Pig Research & Development Corporation and Australian Pork Corporation, March 1997

also covered a substantial increase in pig meat prices at the farmgate. The then favourable pricing situation has now been reversed in light of changes in supply and demand in Australia, prices of competitive meat products, as well as the situation of excess supply in the international market.

3.0 Analysis of the Components of the Australian Pig Industry

Key Point: *Value chain analysis may assist in identifying improvements which can be made across the industry.*

In order to develop an efficient and competitive industry, there is a need to review the operations up to the farmgate as well as those beyond the farmgate. By utilising a value-chain analysis, it is possible to review the pig industry from a vertical perspective so as to recognise the inter-relationships which can exist from the producer through to the retailer. Horizontal relationships across producers have also commenced as smaller individuals attempt to increase their bargaining power with suppliers and processors and achieve efficiencies of scale and high quality products.

3.1 Producers

Key Point: *To maintain the viability of small producers, various pre-farmgate initiatives should be undertaken including the adoption of the Australian Pork Industry Quality Program.*

It is generally acknowledged that in terms of key farmgate performance parameters (herd productivity, unit cost of production, etc) the best operators in Australia are competitive with those overseas, but on average, Australian producers are not. If this situation does not change it may result ultimately in the industry being dominated by a small number of large producers.

There are some farmgate initiatives which must be considered as a means to further improve productivity of smaller (and larger in some cases) producers:

- a move to lower cost, durable housing systems;
- opportunity to acquire, and the broad scale application of advanced genetics;
- improved husbandry through better trained personnel;
- improved health and disease minimisation practices;
- elevated knowledge on nutrition and nutrition x environmental interaction; and
- greater adoption of multi-site production, with independent farrow-to-finish farms encouraged to form alliances/networks with other producers.

Although each of these initiatives is important, the one that has proven to be the most difficult has been the introduction of advanced genetics into Australia so as to enable producers to better meet the requirements of the processors/retailers. AQIS has undertaken to commence a review of the issues surrounding the importation of porcine semen into Australia. However, as a result of many delays, a decision is not expected for at least another twelve months. Such delays have retarded the ability of “non-corporate” Australian producers to maintain their position against imported products which have characteristics better suited to the demands of producers, retailers and the consumer.

Another major initiative which will enable producers to improve the quality of products and respond to the demands of the domestic and international market, is the Australian

Pork Industry Quality Program. As producers seek to establish and compete in export markets, they must satisfy consumers' quality demands and assure those customers that their products are clean and wholesome. Although most producers will require at least three years to implement the three stages of the quality assurance system, the program is extremely important as export competitiveness is critical to the growth of the Australian pig industry.

3.2 Raw Material, Feed Suppliers

***Key Point:** The formation by producers of horizontal relationships will assist in obtaining economies of scale, cost reductions and improvements in quality.*

Australia's position as a globally efficient grower of soft grains and vegetable proteins provides the intensive animal industries with a potential inexpensive, clean and abundant choice.

As stated earlier, there are a substantial number of smaller, independent pig producers who are very efficient. The competitiveness of the Australian pig industry is, therefore, enhanced if such producers can be assisted to form horizontal relationships with like producers and obtain greater economies of scale and quality through multi-site production. These relationships, together with the formation of contract production, has been instrumental in the increase in productivity and output of herds in the United States.

Ridley and other members of the value chain, eg. processors, are very supportive of such producer alliances.

3.3 Processors

Key Point: *Improvements funded by new investment must be made post-farmgate, in the processing industry, to allow Australian products to be competitive in export markets.*

Despite Australia's relative competitiveness at the farmgate, it is post-farmgate, at the processing stage that the Australian industry is relatively uncompetitive.

The processing operations in Australia are considerably smaller than those in competitor nations such as Canada and the United States, whose operations can be more efficient through greater mechanisation and labour specialisation.

Similar to the rationalisation which has occurred at producer level, rationalisation and additional investment is needed before fresh cuts and processed products can be internationally competitive. In this regard, it will be important that the Australian Government's assistance package to the pig industry be focused inter-alia, on specialist pig meat processors to allow them to cater to the particular/peculiar requirement of potential export markets and generally improve the competitiveness of producers' products post-farmgate.

There is also a strong need to translate current technical knowledge of factors, both pre- and post-farmgate, which impact on pig meat quality parameters, into a commercial quality grading programme which boosts domestic and export consumer confidence.

Issues such as boar taint and P.S.E. remain as significant concerns to the industry and pig meat consumers.

3.4 Retailer Prices and Consumption

***Key Point:** The pig meat industry must take steps to improve its competitiveness against substitute meats in the domestic market to ensure a stable and viable industry. A co-ordinated industry plan is required.*

As noted in Section 2, the demand for pig meat is affected by the price for substitute meat products particularly beef and chicken. Over recent years, pig meat consumption has remained static within a relatively narrow band between 17.8 to 19.2 kg per capita, whilst consumption of beef is roughly double this level - refer Table 2(a). The relationship between the various meats can be easily shown. When, as is currently the case, there is a weak export market for beef, there is a decrease in domestic beef prices which results in downward pressure on pig prices. However, where there is a strong domestic market for pork, historically it has tended to attract import competition as well as competition from other meats.

This inter-dependence between the various meat producers inevitably leads to fluctuating demand and consequently periods of over-supply. These cycles will have an

impact on the price of pig meat, and when considered in the light of over-supply in the world pig meat market, has led to greater reductions in prices and prolonged low prices for producers. Based on industry retail data, these downward pricing pressures faced by producers are not always reflected in the retail prices faced by consumers.

Similarly pig meat has not been able to sustain its early promotional successes, with its previous campaigns being copied by lamb, beef and chicken meat. As a result, per capita pig meat consumption has remained relatively flat, or fallen, at the same time as overall per capita meat consumption has risen.

Summary

Whilst staying within the natural forces of industry consolidation and supply and demand a peak body representing and co-ordinating the changes to the industry must manage this rapid transition to not only global competitiveness but positioning into the premium end of the market. This is essential to ensure the long term viability of the Australian industry.

Australia has the array of elements to meet select consumer demands but has been isolated from Northern hemisphere developments and advancements. A policy to initially gain parity must be quickly defined and implemented to allow this important Australian industry and element of society to have a viable future.