



**APL Submission 4**

**Productivity Commission Australian Pig Meat Industry  
Public Inquiry**

**1 February, 2005**

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# 1. Executive Summary

This is the fourth submission APL is providing to the Pig Meat Inquiry. This submission addresses in detail APL's response to the Pig Meat Inquiry draft report whilst also providing more information on the draft pork industry restructure plan. APL had as previously advised that this submission would include a section outlining the competitiveness of the Australia's pork supply chain relative to key international pork trading nations within this submission. Instead, APL will be forwarding this information to the PC at the earliest possible date in February following the completion of the commissioned work.

APL wishes to acknowledge that it believes the very broad terms of reference as well as the particularly short period the PC was given for this inquiry was a significant restraint on the PC. Perhaps as a result of this pressure the PC has done what it could. Nevertheless, APL is of the view that the draft report falls well short of the technical standard usually expected in the PC's reports, which is surprising given the sound reputation of the PC with respect to such investigations. In its current form it is an ordinary work on matters of critical importance to people and their livelihoods; however as it is a draft report the PC has the opportunity to redress these inadequacies.

The draft report suffers principally from constrained terms of reference (over which there was no consultation with industry), a brief that was far too comprehensive for the time provided for the Inquiry and a failure by the writers not to adjust that nature of the analysis to the wholly inadequate information base they had to work on.

The current state of the draft report, therefore, is of great concern to APL due to the fact the Government, the industry and the broader community places much weight on the PC's capacity to provide robust, objective analyses of the competitiveness of the industry and what industry and the Government can do to change these circumstances. In its current form the draft report does not fulfil this purpose; the PC must first properly and accurately characterise the state of the industry before conclusions and recommendations can be made.

- Of considerable concern is the fact there is no investigation of the link between the structural change in the industry and the structural forces that have caused it and contributed to the continual erosion of the industry's competitiveness. The PC has not accurately defined the situation facing the industry and until this is done, relevant recommendations to enhance industry competitiveness cannot be developed.
- No assessment has been made of the way in which the surge in imports has fed through the economic structures of the industry and the

attitudes of businesses to invest and risk. The PC's treatment of the relationship between imports and competitiveness is deficient in that it does not analyse the relationship between major increases in import penetration (however measured) and depressed prices, inadequate returns, higher risk, and reduced investment, which have fundamental impacts on the long term competitiveness of the industry.

- The PC's failure to reflect APL's data properly and to consider profitability against the capital employed in the industry reveals a lack of appreciation of the commercial factors that affect decisions about production and investment. Evidence has been provided by APL which clearly shows that over the last 10 years there have been only three years where profitability has approached what could be regarded as adequate levels for long-term business sustainability, not the purported several years reported by the PC.
- The PC's finding that the case for industry-specific adjustment assistance is weak ignores the long-term structural changes in the industry and the consequent surges in imports that have caused so much damage to it. Critically, the PC restricts its examination to existing "key government and industry programs", not what instruments are available to government; also the methodology used to assess prospective policy instruments is incomplete and inconsistent in parts. Notably missing are other traditional tools – direct industry assistance payments and trade measures (and not just Safeguard measures). Border measures are legitimate instruments to facilitate structural adjustment. The PC should also in examining industry specific adjustment measures should take into consideration APL's draft industry restructure plan strategies proposed Government role, particularly into relation to animal health and trade.
- APL believes draft finding 4.4 that 'reducing the few regulatory impediments is unlikely to make a significant improvement to the competitiveness of pig meat businesses' is a misnomer and undermines the very real and significant impact that regulatory impediments such as the single desk arrangement can have on the industry's future competitiveness. Pig meat production is a low margin business; therefore any cost saving, no matter how small, that can be achieved both from improving business management practices and on farm production as well as redressing regulatory impacts resulting from public policy will have significant positive flow on effects to the competitiveness and profitability of Australian pig producers. The PC acknowledges that feed costs are a key ongoing competitive disadvantage for the industry, yet its findings concerning grain availability that the government keeps a 'watching brief' with respect to the single desk is deficient.

- APL is greatly concerned by the draft reports failure to properly characterise and quantify the impact of support arrangements on the global pork markets. Attachment 1 in the report clearly shows both the direct and indirect effect of such support arrangements in providing our competitors with an iniquitous competitive advantage; subsidised competition impedes the efficiency of the market to allow price signals to determine market behaviour. These market distortions add further downward pressure on world pork prices and shift much of the resulting pressure for adjustment to unsubsidised industries with open markets such as the Australian pork industry. Highlighting this fact are the comments of Professor Clair Nixon, that the 'EU maintains a two-tier pricing structure: internal and external (exports)' whereby quarantine restrictions are effectively restricting imports that has the effect of maintaining 'a high price domestically, with the surplus being sold in foreign markets'.
- APL is particularly concerned by comments made in draft finding 5.2 seeming to indicate that the PC considers trade distorting behaviour of international competitors is acceptable, if it leads to lower prices for consumers, even if that behaviour has adverse effects on Australian pork producers and by implication the rural and regional communities that depend on them. The PC has again failed to undertake any detailed analysis including a net cost benefit analysis to prove this statement.
- The PC has not addressed the request by APL for an investigation of the need for safeguards against imports as the primary mechanism to facilitate restructuring and hence address the competitive challenges faced by the industry. The PC states that it will not address the matter of safeguards for fear of prejudicing later consideration, but then proceeds to produce a judgment on this matter. The PC's analysis is seriously flawed. Rather it appears to be a simple commentary of the prospective generic impact of such measures and does not seem (again) to be formed by an empirical assessment of the impact of imposition of specific border measures.
- APL's fundamental concern is that in the time available, a proper (technically-sound, methodologically consistent) assessment of the condition of the industry has not been undertaken and that the options for assistance have not been properly analysed. Conclusions have been reached without supporting analysis and adequate data whilst some discussion lacks technical support. The only intellectually defensible approach in this case would have been to indicate where the factual base was too thin to draw conclusions rather than proceed if that were not the case.

- The issue here is whether reported consideration is adequate in serving the consultative elements of the process, which are important in their own right to the credibility of the report, as well as to prospective demonstration of compliance with the processes of administrative review, that may become relevant to any executive decisions taken in the exercise of administrative discretion by government authorities on the basis of analysis in this report.
- Taken together, these deficiencies mean that the PC has failed to adequately analyse key factors that it must take into account in respect of its Term of Reference number 1, and hence mean it cannot adequately assess the need for Government measures under its Term of Reference number 2.

APL contends that these matters need to be adequately addressed so as to ensure the final Pig Meat Inquiry Report provides for well-substantiated conclusions or at the very least these conclusions are adjusted to reflect the inability to provide such analysis due to the inadequate information and/or timeframe available. The conclusions are dangerous for leaving an impression they are better based than they are.

## **1.0 Key Recommendations**

### ***Recommendation 1***

APL recommends that the Productivity Commission seek an extension on the deadline for completion of the report. This action is necessary in order to ensure that both a proper (technically-sound, methodologically consistent) analysis of the condition of the industry is undertaken and that the options for assistance have been properly analysed.

### ***Recommendation 2***

The PC properly and accurately characterise the state of the industry to ensure substantive conclusions and recommendations are made. The final report should include an investigation of the link between the structural change in the industry and the structural forces that have contributed to the continual erosion of the industry's competitiveness, including the relationship between major increases in import penetration (however measured) and depressed prices, inadequate returns, higher risk, and reduced investment.

***Recommendation 3***

APL and the broader pig meat industry have provided a substantial amount of information about the condition of the industry, but is concerned that it has been set aside because it was produced to support the imposition of safeguard measures. APL requests that this information be taken into account including the data provided in relation to industry profitability in order to present a more accurate analysis of the industry including its financial position.

***Recommendation 4***

The PC should examine all policy instruments available to government including traditional tools – direct industry assistance and trade measures (and not just Safeguard measures). Border measures are legitimate instruments to facilitate structural adjustment. A full and proper assessment should then be undertaken to determine the relative merits of prospective measures in respect of structural adjustment and improving industry competitiveness.

***Recommendation 5***

The PC set out a methodology at the beginning of the report so that it is possible to assess the relative merits of prospective measures or make findings on such measures, particularly in respect of structural adjustment.

***Recommendation 6***

APL recommends the PC cease the selective use of data in critical areas of analysis. For example, a longer time frame should be considered when assessing the impact of imports so as to present a more accurate picture of the extent of increases. APL advocates a ten year period be covered which will also provide a level of assessment consistent with the time frame used to discuss profitability of pig producers.

***Recommendation 7***

It is well understood that the PC may feel a general reluctance to consider using trade measures as a tool to support industry assistance, however, they are not precluded from Government policy and they are a legitimate measure in a multilateral trading environment. As the PC is not excluded in its terms of reference from examining the impact of imports, it should therefore assess the option of safeguards including the impact of such a measure on all parties and reach a recommendation on whether a safeguard investigation is warranted.

***Recommendation 8***

The PC's must also extend its analysis to properly characterize and quantify the impact of support arrangements enjoyed by our competitors and provide substantive solutions to these impediments to industry competitiveness. These arrangements are not insignificant in their effect on the Australian pork industry nor quickly remedied through multilateral trade negotiations as the PC's report suggests. These market distortions add further downward pressure on world pork prices and shift much of the resulting pressure for adjustment to unsubsidised industries with open markets such as the Australian pork industry. Attachment 1 in the report clearly shows both the direct and indirect effect of such support arrangements in providing our competitors with an iniquitous competitive advantage.

***Recommendation 9***

The PC must undertake the detailed technical analysis required to prove draft finding 5.2, which indicates that trade distorting behaviour of international competitors is acceptable, if it leads to lower prices for consumers, even if that behaviour had adverse effects on Australian pork producers and by implication the rural and regional communities that depend on them. The test must be empirical, not theoretical and in the absence of such analysis this finding should be adjusted to reflect this.

***Recommendation 10***

The PC reassess its draft finding 4.4 that 'reducing the few regulatory impediments is unlikely to make a significant improvement to the competitiveness of pig meat businesses' due to the fact that in a low margin business such as pig meat production, the collective impact of regulatory issues such as the single desk arrangement, animal welfare and environment matters can in fact have a significant impact on production costs and by implication the industry's future competitiveness. In particular, the PC's findings with respect to grain sufficiency and affordability, including that the government keep a 'watching brief' with respect to the single desk, are deficient. At the very least the PC should investigate earlier recommendations put forward by APL with regard to investigating mechanisms to deliver feed grain security.



## **2 Response to Pig Meat Inquiry Draft Report**

### **2.0 Overview**

The draft report seems to fall short of the technical standard usually expected in the PC's reports, which is surprising given the sound reputation of the PC with respect to such investigations. In its current form it is an ordinary work on matters of critical importance to people and their livelihoods; however APL acknowledges that this is a draft report and that therefore the PC has the opportunity to redress these inadequacies.

Essentially, APL's fundamental concern is that in the time available, a proper (technically-sound, methodologically consistent) analysis of the condition of the industry has not been undertaken and that the options for assistance have not been properly analysed. Conclusions have been reached without supporting analysis and adequate data whilst some discussion lacks technical support. Typically the draft report tends to take a generalised discussion of issues and then proceed to consider potential impacts but ultimately falls short by not taking the next step by attempting to assess these. The test must be empirical, not theoretical.

There is no investigation of the link between the structural change in the industry and the structural forces that have caused it and contributed to the continual erosion of the industry's competitiveness. No assessment is made of the way in which the surge in imports has fed through the economic structures of the industry and the attitudes of businesses to invest and risk.

The current state of the draft report, therefore, is of great concern to APL due to the fact the Government, the industry and the broader community places much weight on the PC's capacity to provide robust, objective analyses of the competitiveness of the industry and what industry and the Government can do to change these circumstances. In its current form the draft report does not fulfil this purpose; the PC must first properly and accurately characterise the state of the industry before conclusions and recommendations can be made..

Although, the terms of reference authorises the PC to consider what Government or industry measures may be necessary to enhance the competitiveness of the industry, the PC has only addressed "key government and industry programs" relevant to the pig meat industry. Notably missing are other traditional tools such as direct industry assistant payments trade measures (and not just Safeguard measures). Border measures are legitimate instruments to facilitate structural adjustment; naturally, the PC would need to assess the impact of such measures on all parties. However, the PC fails to undertake this and other unnecessary analysis.

It is also striking that the PC does not set out a methodology at the beginning of the report. While the structure of the report seemingly implies one and elements of it are found through the report, nevertheless it has to be deduced. Without a full assessment such as this it is not possible to assess the relative merits of prospective measures or make findings on such measures, particularly in respect of structural adjustment.

Taken together, these deficiencies mean that the PC has failed to adequately analyse key factors that it must take into account in respect of its Term of Reference number 1, and hence mean it cannot adequately assess the need for Government measures under its Term of Reference number 2.

The pig meat industry has provided a lot of information about the condition of the industry, but is concerned that it has been set aside because it was produced to justify the imposition of safeguard measures. In particular, the draft report inadequately deals with the issues of:

*i. Profitability*

The PC's failure to reflect APL's data properly and to consider profitability against the capital employed in the industry (especially one like pig meat which is a capital intensive industry) reflects a lack of appreciation of the commercial factors that affect decisions about production and investment. As highlighted in APL's first submission, over the last 10 years there have been only three years (2000, 2001 and 2002) where profitability has approached what could be regarded as adequate levels for long-term business sustainability (not the purported several years reported by the PC), one of which was principally due to the FMD outbreak in Denmark and the resulting temporary ban on these imports. Further to this, and as previously noted in APL's first submission, the recent Ernst & Young survey of pork producers highlighted how the larger producers have lost equity of approximately 40% over the 2001-2003 period.

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*ii. Imports*

The PC's treatment of the relationship between imports and competitiveness is deficient in that it does not analyse the relationship between major increases in import penetration (however measured) and depressed prices, inadequate returns, higher risk, and reduced investment which have fundamental impacts on the long term competitiveness of the industry.

The PC's approach does not address the long term in assessing the industry's situation and hence its longer term prospects. The PC should examine the long-term structural forces that have impacted on the industry and which influence the direction and nature of structural change.

*iii. Industry assistance & structural factors*

The PC finds that the case for industry-specific adjustment assistance is weak because many of the difficulties experienced by the industry relate to essentially cyclical factors – the “*ongoing variable nature of world pig meat markets, climate and currency markets*”. This ignores the long-term structural changes in the industry stemming from the decision by Government in the mid 1990's to review and change the quarantine arrangements for pork imports, and the consequent surges in imports, which have caused so much damage to it.

*iv. The Safeguard Question*

The PC has not addressed APL's request for an investigation of the need for safeguards against imports as the primary mechanism to facilitate restructuring and hence address the competitiveness challenges faced by the industry. The PC states that it will not address the matter of safeguards for fear of prejudicing later consideration.

Nevertheless the PC then proceeds to produce a judgment on this matter; it raises a number of reasons why safeguards, even if they were justified under the WTO, would not be appropriate to assist the industry. But it ignores the dramatic surge in pig meat imports in a relatively short period of time, (which surely must also be considered in any objective assessment of the competitiveness situation of the industry).

The PC's analysis is seriously flawed. Rather it appears to be a simple commentary of the prospective generic impact of such measures and does not seem to be informed by an empirical assessment of the impact of imposition of specific border measures.

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This Report suffers principally from constrained terms of reference (over which there was no consultation with industry), a brief that was far too comprehensive for the time provided for the Inquiry and a failure by the writers not to adjust that nature of the analysis to the wholly inadequate information base they had to work on.

APL contends that these matters need to be adequately addressed so as to ensure the final Pig Meat Inquiry Report provides for well-substantiated conclusions or at the very least these conclusions are put right to reflect the inability to provide such analysis due to a lack of available information/data and/or limited timeframes.

## **2.1 The Approach and methodology of the Report**

The draft report falls well short of the technical standard usually expected in PC reports. The weaknesses raised below are detailed in the sections that follow:

- It is recognized that in Chapter six additional material is invited on what measures warrant consideration to improve industry competitiveness. Alarming, the draft has reached conclusions on this front despite having limited technical information and imperfect analysis.
- Conclusions are drawn without supporting analysis and without adequate data. Part of the analysis is technically inaccurate, but the methodology used to assess prospective policy instruments is incomplete and inconsistent in parts.
- In one very important respect, consideration of safeguards (p.166), the report intrudes with a judgment on a matter it previously stated it would not address for fear of prejudicing later consideration.
- Very important contentions made by APL appear not to have been given any regard, particularly in respect of the financial health of the industry and measurement of competitiveness. The complaint is not that the comments were disregarded, but that there was no evident consideration of the material provided on key factors concerning the competitiveness of the Australian pig meat industry.
- The issue here is whether reported consideration is adequate in serving the consultative elements of the process, which are important in their own right to the credibility of the report, as well as to prospective demonstration of compliance with the processes of administrative review, that may become relevant to any executive decisions taken in the exercise of administrative discretion by government authorities on the basis of analysis in this report.

- The terms of reference constrained the PC, particularly the short period it was given for the Inquiry. Perhaps as a result of this pressure, the PC has done what it could. In many cases the analysis would seem to warrant no conclusion without further analysis.
- This report suffers principally from constrained terms of reference (over which there was no consultation with industry) and a brief that was far too comprehensive for the time provided for the Inquiry. Even so, the failure by the writers not to adjust that nature of the analysis to the wholly inadequate information base they had to work on is unwarranted and imbalanced.
- The only intellectually defensible approach in this case would have been to indicate where the factual base was too thin to draw conclusions rather than proceed if that were not the case. The conclusions are dangerous for leaving an impression they are better based than they are.

### **2.1.1 Methodology**

It is striking that the PC does not set out a methodology at the beginning of the report. The structure of the report implies one, but it is not stated.

This becomes clear when one searches for the methodology by which the PC analyses what tools are available for consideration by government to assess what the impacts of various measures will be.

One would expect a summary matrix setting out the problems identified, what impacts (costs and benefits) each measure would have and then a comparative assessment of how each measure stacks up.

However, it would be difficult to construct such a matrix because the analysis in the report is not systematic or consistent enough to create one.

### **2.1.2 Interpretation of terms of reference**

The Inquiry authorizes the PC to consider what Government or industry measures may be necessary to enhance the competitiveness of the industry.

The PC appears to have interpreted this to mean, “key government and industry programs” relevant to the Pig Industry. (Introduction to chapter 4). That chapter and Annex D are deficient as they only summarize existing programs, not what instruments are available to government. Notably missing are other traditional tools – direct industry assistant payments and trade measures (and not just Safeguard measures).

It is noted that the PC’s report into the citrus industry does discuss use of tariff measures as prospective instruments to support structural adjustment.

Given the similar terms of reference for this inquiry it would appear reasonable that the PC would examine similar matters as it did in the citrus industry inquiry, which could include what effect measures such as increased tariffs or quotas could have for the Australian pig meat industry and, possibly whether a safeguards investigation is warranted.

It is well understood that the PC may feel a general reluctance to consider using trade measures as a tool to support industry assistance.

However, it is not precluded from Government policy and it is an instrument available and identified for sound reasons to support structural adjustment in the multilateral trading system. This point goes beyond use of Safeguard measures. (The treatment of the Safeguard provision is considered later.) They are not the only tools available under international trade law to Governments to support structural adjustment.

We are not aware there are any provisions in the Productivity's Act which prevent it from considering utilisation of border measures as instruments to facilitate structural adjustment, although it is fully appreciated that in so doing it should also assess the impact of such measures on all parties. Without such assessment it is not possible to assess the relative merits of prospective measures or to draw robust conclusions.

APL believes the terms of reference given to the PC provides appropriate scope for the Inquiry to consider the evidence that industry has been injured by imports and hence that there is basis for a recommendation that a separate inquiry be undertaken in respect of potential safeguards. APL has obtained legal advice, forwarded to the PC at the start of this Inquiry, that confirms this course of action can be undertaken within the Inquiry's current terms of reference.

Secondly, APL notes the comment that safeguards would not create incentives for pig meat businesses to adjust.

*'In many cases, the benefits to pig producers of restricting pig meat imports are short term because, while such restrictions may bring immediate improvement to pig prices in Australia, they would discourage or delay the ongoing restructuring, which is critical to industry performance in the long term'. (P.129)*

APL questions this assertion on the basis that it is an acknowledged requirement of the WTO that in order to introduce safeguard measures a country must have an accompanying measure of restructure reforms. The PC provides no evidence that safeguards would provide a disincentive for change. Importantly, given their ostensible purpose and the nature of safeguards (i.e. they are temporary and phased out), and the fact there is an obligation of the Government (and industry) to ensure adjustment measures

are undertaken to facilitate competitiveness, it would seem that they would provide considerable incentive for change.

APL highlights that in advance of any potential introduction of safeguard measures the Australian pork industry has already commenced this process as detailed in the draft Australian Pork Industry Restructure Plan due to be finalized at end February 2005. This Restructure Plan is discussed in detail in section three of this submission.

### **2.1.3 Testing the case for support for structural change**

On page 74 and 75 in Chapter 6 of the report, the PC sets out the terms of the case for assistance to industry. APL provided substantial information to the PC on the difficulties being faced by the large number of small holders in the industry, yet the draft refers only to one fact of an empirical nature which might be used against those tests and that would not appear to have been provided by APL.

## **2.2 Inaccurate representation of industry situation**

The PC has not accurately defined the situation facing the industry and until this is done, relevant recommendations to enhance industry competitiveness cannot be developed.

### **i. APL's submissions**

In its first submission (date 19 October 2004), APL pointed out that one of the biggest financial challenges for Australian pork producers has been the combination of ongoing lower prices received for pork and the high cost of feed inputs. Recent industry analysis has highlighted that there have been massive swings in profitability over the last 10 years and that during this period there have been only three years, (not the purported several years reported by the PC), - 2000, 2001 and mid 2002, where profitability has approached what could be regarded as adequate levels for long term business sustainability. One of those three years was the direct result of a ban on Danish imports due to the European Foot and Mouth Disease outbreak.

These factors have created an extremely high level of financial uncertainty. A higher risk environment normally requires a higher return on investment than that required in a low risk environment, but this has not been the experience of Australian pork producers. Feedback to APL from processing companies indicates that most of the meat "displaced" by imports in the manufacturing sector is sold into fresh meat sectors causing an oversupply and hence falls in wholesale prices.

### **ii. The PC draft report**

The PC's draft report deals inadequately with the profitability and competitiveness situation facing the industry. It argues on page 35 that, "*The competitiveness of a business is difficult to measure — there is no single indicator of*

*competitiveness. Insights into the competitiveness of businesses can be gained, however, by considering a variety of indicators, including profitability and market share. The continued survival of businesses without significant government assistance can also demonstrate the competitiveness of businesses.”*

It concludes its analysis of these factors by stating on page 37 that, “*Changes in profitability and market share can reflect changes in competitiveness. Many pig producers appear to have made losses during 2002-03, following several years of above average profits. The share of imported pig meat used by secondary processors increased between mid-2002 and the end of 2003. Exports of pig meat declined during that period”.*

The PC’s analysis of the critical issues surrounding profitability and imports will be discussed in turn.

**a. Profitability**

The draft Report cites APL survey data as indicating that pig producers made a profit in eight out of the 10 years from 1993-94 to 2002-03 (page28), referring to Table 2.2 on page 29).

However APL’s submission using this data noted that:

- There have been massive swings in profitability over the last 10 years.
  - During this period, there have been only three years (2000, 2001 and 2002) where profitability has approached what could be regarded as adequate levels for long-term business sustainability. One of those three years was due principally to the FMD outbreak in Europe resulting in substantially reduced Danish imports.
  - As previously noted in APL’s first submission, the recent Ernst & Young survey of pork producers highlighted how the larger producers have lost equity of ~40 percent over the 2001-2003 period.
- CONFIDENTIAL INFORMATION REMOVED**

- In evaluating these figures, it also needs to be noted that more recent financial survey work indicates that the PigStats data underestimates current asset values and financing costs.

The PC’s failure to reflect APL’s data properly and to consider profitability against the capital employed in the industry (especially one like pig meat which is a capital intensive industry) reflects a lack of appreciation of the commercial factors that affect decisions about production and investment. This information was detailed in APL’s first submission (p. 43).



### ***b. Imports***

In analysing the impact of imports on industry the draft Report states that, “Australia has become increasingly integrated into the world pig meat market over the past six years” (page 27). On page 153, it notes that Danish and Canadian imports arriving in Australia are boneless, so the tonnage cannot directly be compared with Australian pig meat production, which is calculated on a carcass weight equivalent basis. To compare pig meat imports with domestic production, therefore, the two must be converted to a comparable basis.

Table B.11 indicates that Canadian legs accounted for about 28–38 per cent of legs supplied to the Australian secondary processing sector in 2003-04, while Denmark supplied about 32–33 per cent of middles (Table B.12). The PC notes that this analysis needs to be interpreted with caution, because the results are sensitive to the assumptions made about meat yield and the proportion of domestic production entering the manufacturing sector.

These percentages for import penetration are smaller than those identified by APL in its analysis of imports (19 October 2004, Tables 1 and 2) because APL calculates imports as a percentage of production whereas the PC for this report calculates imports as a percentage of legs used by the processing sector.

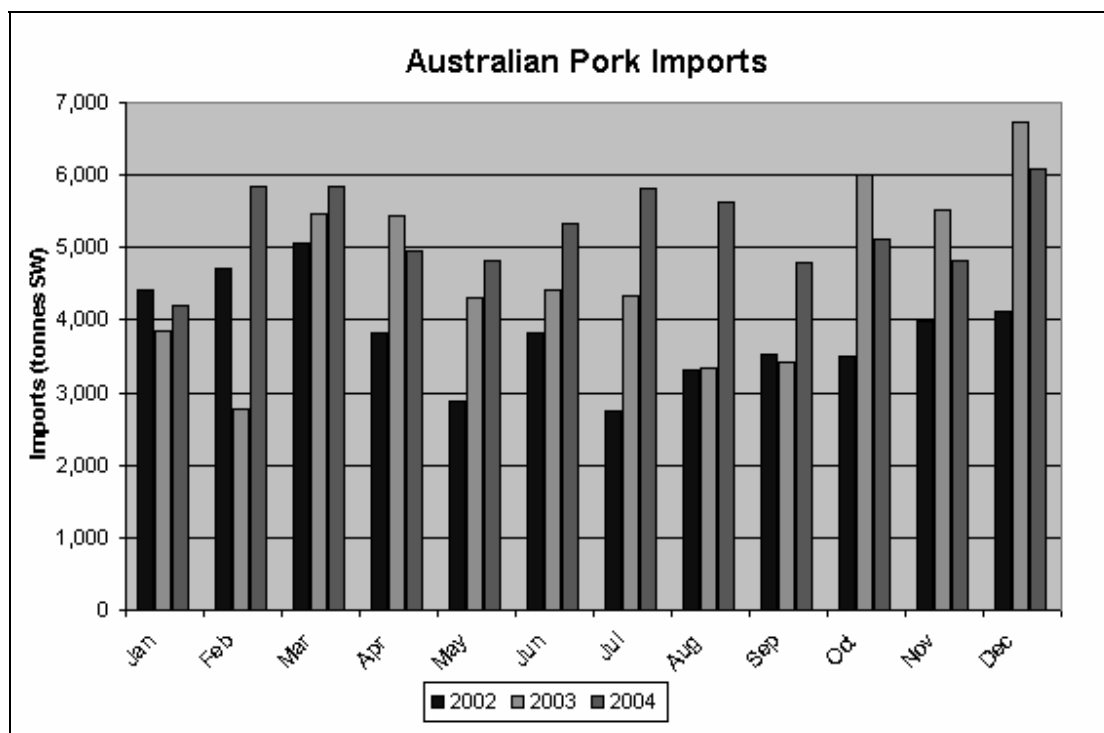
The following points need to be made about the PC’s method:

- If the PC is seeking by its method to indicate imports as a share of consumption then it must also deduct any exports of the relevant products.
- The PC used imports as a share of production in its 1998 Report but here uses a method which produces a lower percentage. Also, the PC only considers the period up to the end of 2003 when considering the growth in imports, despite the fact imports have continued to grow at a rapid rate from 1999 to the latter part of 2004, for which the most recent data is available (see Chart 1 below)<sup>1</sup>. The PC therefore fails to complete and accurate picture of the impact of imports on the industry and factors that lead to its current state. One may legitimately ask whether the PC has done so to deliberately underplay the role of imports in the domestic industry.

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<sup>1</sup> The most recent figure for exports is \$177m (October 2004) as opposed to \$195 m documented in the draft report.

**Chart 1 Pork imports**



- Between mid 2002 and the end of 2003, pig meat imports increased by 73% whereas the Australian market increased by only 8%, indicating a significant surge of imports in a relatively short period of time.
- The PC only calculates percentages from 2001-02 to 2003-4. This suggests imports as a percentage of usage have only increased marginally. It ignores the dramatic rise in import penetration (measured any way) over the past decade, which surely must be considered in any objective assessment of the competitiveness situation of the industry. Using the PC's method for assessing import penetration, but data used in APL's first submission, imports of legs have risen from 10% in 1997-98 to over 28% in mid-2004, and for middles have risen from nothing to over 36% over the same period. The past decade is the time period the PC itself uses to discuss profitability of pig producers (albeit in a selective fashion as discussed earlier in this section).

The PC's treatment of the relationship between imports and competitiveness is deficient in that it does not analyse the relationship between major increases in import penetration (however measured) and depressed prices, inadequate returns, higher risk, and reduced investment which have fundamental impacts on the long term competitiveness of the

industry. Further, no assessment was undertaken by the PC as to whether exports were at dumped prices or received countervailable subsidies.

The PC's approach does not address the long term in assessing the industry's situation and hence its longer term prospects. This is demonstrated by its singular focus on a few recent years of imports in its analysis.

### **iii. Response**

In its draft Report the PC has:

- Used data provided by APL on profitability which inaccurately portrays the industry as relatively profitable. We again refer the PC to the information provided in APL's first submission, in particular section 4.
- Inadequately assessed the relationship of imports with the Australian industry situation, outlook and competitiveness, as described earlier in this submission and in Appendix A of this submission.
- Inadequately specified the timeframe and data commenting that the competitiveness of the Australian pig meat industry 'appears to be recovering' (p.XXII). Whilst general overall conditions may be improving, the negative effects of some cyclical factors may mean it is some time before individual entities financial positions have changed for the better. The recent Ernst & Young survey of pork producers highlighted how the larger producers have lost equity of approximately 40% over the 2001-2003 period.

Taken together, these deficiencies mean that the PC has failed to adequately analyse key factors that it must take into account in respect of its Term of Reference number 1, and hence mean it cannot adequately assess the need for Government measures under its Term of Reference number 2.

In revising the report, the PC should:

- (i) cease selective use of data in critical areas of analysis; and
- (ii) more accurately reflect the role that imports have played in profoundly destabilising the industry and undermining its competitiveness.

### **2.3 Industry assistance and structural factors**

The PC's finds that the case for industry-specific assistance is weak because many of the difficulties experienced by the industry relate to essentially cyclical factors – the “ongoing variable nature of world pig meat markets, climate and currency markets”. This ignores the long-term structural changes in the industry stemming from the decision by Government to change the

quarantine protocols for imports, and the consequent surges in imports which have caused so much damage to it.

The PC fails to identify those structural factors that have contributed to the continual erosion of the industry's competitiveness notwithstanding past Government measures to improve the industry's productivity, for example, the historical pattern and linkages that go to explaining substantially rising import penetration as well as the massive price and volume swings in imports - 68% increase in one year.

#### **i. APL's submissions**

APL's first submission clearly outlines the link between increased imports and damage to the industry. It is clear that imports are increasingly dominating key segments of the Australian market.

In the case of Canadian imports, these dominate the leg market. Danish imports have a substantial share of the middles market (primarily used for making bacon).

Both leg and middles imports have had a noticeably adverse impact on the domestic pig industry. This operates primarily through the impact of imports on prices for pig meat products in the domestic market. Notably the cuts of legs and middles together constitute almost two-thirds of the animal.

Prices (measured as unit values) of imports from both Canada and Denmark have been on a downward trend over the period of the import surge dating from mid-2001. The high levels of imports over the past three years are reflected in the downward trend in producer prices over the same period.

It is important to note that this pattern of increased imports and depressed prices has occurred since the changes to quarantine arrangements for pig meat imports was first removed overnight by the Government in the mid-1990s. The earlier period of import penetration and damage to the industry was acknowledged in the PC's 1998 report.

#### **ii. The PC draft report**

The draft report begins by acknowledging that the industry's production and processing sectors continue to experience significant structural change. And as stated, it finds that the case for industry specific assistance is weak because the industry suffers from ongoing variable nature of world markets, climate and currency – in other words the normal ups and downs of being in the pig meat business.

No assessment is made of the way in which imports have surged since the opening of the Australian market, or the way in which these surges have fed

through the economic structure of the industry and the attitudes of businesses to investment and risk.

There is no investigation of the link between the structural change in the industry and the structural factors which may have caused it. These connections can be conceded without drawing to an inexorable conclusion that the only response is to impose safeguard measures. They undoubtedly are creating adjustment pressure.

The PC should examine the longer-term structural forces which have impacted on the industry and acted to influence the direction and nature of structural change. In particular, it should examine what impact the import surges experienced by the industry have had on the structural composition of the industry since quarantine arrangements concerning meat imports were first changed.

### **2.3.1 Government assistance – Clarifying APL’s position**

Putting aside for the moment APL’s request that ‘the PC makes a recommendation for the imposition of provisional safeguards’), APL notes that assistance has been sought on four separate strategic initiatives only, all of which are key components of the draft Restructure Plan. These initiatives consist of:

- 1 Financial support for the development and implementation of the HomeGrown initiative. *This support has been obtained.*
- 2 Funding approval for a Cooperative Research Centre addressing feed cost issues as part of the Industry Restructure Plan. *This support has been obtained.* This is generalized assistance available to most agricultural industries and many other industries.
- 3 Assistance on animal health envisaged being possibly regulatory in nature as well as funding support for this initiative. This initiative is estimated to represent a \$25 million saving to costs of production. Indeed the Productivity PCs’ own draft report identifies the crucial importance of the industry’s unique health status as a competitive advantage, particularly in relation to our ability to capture niche markets. *‘Many submissions highlighted that the disease free status of Australian pigs is a key factor differentiating Australian pig meat from that of its international competitors’* (p.32).
- 4 Trade measures including Government assistance establishing a framework to collect and track real time national and sub national assistance received by exporting nations’ pork producers and their supply chain.

### **2.3.2 Adjustment assistance criteria - Unsubstantiated conclusions**

The PC has determined that the industry does not meet its criteria for specific adjustment assistance. However no conclusions are warranted on the basis of the information presented by the PC in its draft report.

On page 74 and 75 in Chapter 6 of the report, the PC sets out the terms of the case for assistance to industry. APL provided substantial information to the PC on the difficulties being faced by the large number of small producers in the industry, yet the draft refers only to one fact of an empirical nature which might be used against those tests and that would not appear to have been provided by APL.

The fundamental concern about this draft is that in the time available, a proper (technically-sound, methodologically-consistent) analysis of the condition of the industry has not been undertaken and that the options for assistance have not been properly analysed.

APL and the broader pig meat industry have provided a substantial amount of information about the condition of the industry, but is concerned that it has been set aside because it was produced to justify the imposition of safeguard measures. Similarly, the pig meat industry has provided analysis on the types of assistance measures that would be appropriate to address the competitiveness challenges facing the industry. It is concerned that this analysis may similarly have been set aside because it was produced in the safeguards context.

The industry's analysis is reproduced in Appendix A with the specific request that it be taken into account in assessing the needs of the industry and for determining the mode of assistance most effective for enhancing long-term competitiveness in the industry

The PC has indeed noted on page 138 that it is interested in receiving further information and feedback on the government assistance measures discussed, and any other relevant government measures. The industry requests that the analysis it has provided be considered as such further information.

## **2.4 The Safeguard Question**

### **2.4.1 The PC's capacity to discuss the Safeguards issue**

#### **i. APL's submissions**

APL formerly requested the PC on 19 October 2004 to make an immediate request to the Government to restrict imports. This would create a breathing space for the industry to stave off further financial injury from the continuing rise in imports while the Inquiry can be undertaken and a restructuring

program can be properly designed and implemented in an orderly way. The case was presented in the submission that injury has occurred and a case for provisional safeguards exists.

In our second submission APL proposed that the PC conclude that temporary import controls under the terms of the WTO provisions would be the most effective means to facilitate restructuring. It was further proposed that the PC seek approval to undertake a formal safeguards inquiry so that the Government has the option of adopting this approach promptly after it receives the PC's report.

#### **ii. The PC draft report**

The draft report does not refer to these requests. It notes on page 136 that the PC has not been asked to comment on a safeguards (or preliminary safeguards) assessment, and nor could it undertake such an assessment without a formal request by the Australian Government. The PC *“does not want to prejudice any potential assessment (if one were to be announced), and therefore does not comment on whether safeguard measures could presently be justified under WTO rules”*.

#### **2.4.2 Is the PC excluded from discussing the option of safeguards?**

Any comments by the PC can only have validity in respect of a decision by the Government to impose Safeguards if the Government formally charges the PC to assess if grounds exist to impose a safeguards measure as the agency nominated for that purpose under the WTO Safeguards Agreement.

Unless the PC is formally requested by the Government to do an assessment in that capacity, nothing it has to say on the subject has legal standing. This is not in dispute.

What is critical to this inquiry and its terms of reference, however, is that in no way is the PC prevented from discussing the applicability of a Safeguards measure in its capacity as assessor of the state of competitiveness of an industry or the impact of such measure. Since any border measure, which can be legally imposed by the Australian Government, must fall within the definition of measures available to it to assist industry, there is nothing to prevent it from discussing a safeguard measure under the terms of reference.

The terms of reference given to the PC provides appropriate scope for the Inquiry to consider evidence that the industry has been injured from imports and hence there is a basis for a recommendation that a separate inquiry be undertaken in respect of potential safeguards.

### 2.4.3 Does a well -worked analysis support the general comments on the impact of Safeguards?

The PC comments that regardless of whether a case exists for safeguards measures, *“it is far from clear that such actions would be the most appropriate”*.

On first appearance, this seems a reasonable comment; but how these specific measures that might apply have not been analysed. The PC has not yet arrived at a well-based analysis of the condition of the industry, let alone modelled the impact of various levels of temporary border controls.

But this does not seem to inhibit the author of the draft. It then restates the analysis made in the 1998 report, which was principally a policy account of the different impact of a safeguard border measure compared to other forms of assistance. The 1998 report reflected no detailed analysis of the impacts on various players. It was a policy analysis only. Yet this was deemed a sufficient basis for the 2005 draft Report to conclude safeguard actions would be “a blunt and indirect” way of providing assistance. While safeguards may be blunt, their aim is to assist an industry and not individual producers, by providing the industry with a relatively short period of time to restructure.

Such general policy prescriptions are only as good as the empirical testing of them. They are “blunt and indirect”, but this may not matter for specific results sought. The test is empirical, not theoretical.

The Report goes on to state, *“safeguard actions would not create incentives for producers to adjust”*. This is an astonishing comment. The PC and its predecessors have always stressed that the one of the most effective tools of adjustment are fixed, phased tariff reductions. For example, APL notes the comments from the 1998 PC Pig Meat Inquiry that, *‘A 10 per cent tariff, phasing to 5 per cent after one year and zero after 2 years, would provide short-term price relief to relatively efficient producers but would not provide a fortress for relatively high-cost producers’*<sup>2</sup>. Commitments to such a phase down are a legal requirement under the WTO Safeguards Agreement as a condition for imposing a border control measure. What therefore is the difference? Equally and as highlighted earlier, the PC has provided no empirical evidence or substantive analysis that safeguards would provide a disincentive for change.

APL argued that one of the reasons it sought a safeguard measure was to impose such a framework on the industry to let the market achieve the adjustment in the industry in a way that minimized the risk of sudden change and optimised social stability.

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<sup>2</sup> Productivity Commission, *Pig and Meat Industries: Safeguard Action Against Imports Inquiry Report*, Report No 3 (11 November 1998) p.64



If the PC had assessed the impact of several models of phase down border controls under a safeguard scenario compared to the use of other types of targeted assistance, and found the later superior on all the criteria, then there would be a basis for assessing the virtues of one model against the other. There is no evidence it has done this.

The PC's discussion of this matter on page 136 of the draft Report is the sort of generalized discussion of the issue one would expect in an introductory issues paper, not in a draft which is the conclusion of several months work analysing the financial condition of the industry and assessing what the impact of various measures would be.

Finally, the Report states that negotiating prospective compensation packages with other countries (a possible consequence of imposing a safeguard measure) might be hard to negotiate and might harm Australia's capacity to seek reduction of the trade barriers of others, and with the potential to adversely affect other exports and incite retaliatory action. However, whether or not this would be the case would depend upon the countries affected, the safeguards measures imposed and Australian exports to these countries. Further these are manageable risks and a normal part of the routine of international trade negotiations.

Noticeably, trade negotiation is not a responsibility of the PC, nor an area of its expertise. The PC should therefore refrain from asserting such opinions.

#### **2.4.4 A better informed process of analysis is warranted**

This is especially demonstrated when the case of the impact of special adjustment measures on other parties is considered. The traditional argument for using subsidies rather than tariffs is that the tariff imposes a higher cost on a wider set of parties.

Restricting imports of pig meat would only adversely affect pig meat consumers, retailers and manufacturers if the increased domestic output, which resulted, was uncompetitive in replacing imports over the long term.

This demonstrates why the specific impact needs to be assessed in the case of tariffs on pig meat. The industry is integrated so the negative cost on processors will be offset to a degree. The imports are on special pig meat parts. Generalized conclusions about the impacts on consumers and processors will not provide an accurate picture of the effects.

Again, the basic concern about the draft is that in the time available, a proper (technically-sound, methodologically-consistent) analysis of the condition of the industry has not been undertaken and that the options for assistance have not been properly analysed.

As previously stated, the pig meat industry has provided much information about the condition of the industry, but is concerned that it has been set aside because it was produced to justify the imposition of safeguard measures. The data is reproduced in 'Appendix A.'

## **2.5 CONFIDENTIAL INFORMATION REMOVED**



## **2.6 Key Issues: Inconsistencies and Unsubstantiated Conclusions**

### **2.6.1 Benefits to trade distorting behaviour**

APL questions the PC conclusion that trade restrictions would harm pig meat consumers and manufactures. APL is particularly concerned by comments made in draft finding 5.2 seeming to indicate that the PC considers trade distorting behavior of international competitors is acceptable, if it leads to lower prices for consumers, even if that behavior has adverse effects on Australian pork producers and by implication the rural and regional communities that depend on them. It could equally be argued that the lower prices for processed product currently enjoyed by Australian consumers is to a large extent artificial and short term, achieved via overseas assistance schemes. Once removed, market forces would operate to potentially increase these prices.

The PC has again failed to undertake any detailed analysis including a net cost benefit analysis to prove this statement.

Curiously the draft report proceeds to consider what potential impacts should be considered but has not gone the next step and actually attempted to assess these.

*'In addition to examining the aggregate benefits and costs of overseas subsidies for Australians, however, the distribution of these benefits/costs across the community is important in considering possible policy measures. In particular, if the costs to producers (and their families and employees) are high and concentrated, they may generate additional non-financial adjustment costs for some people (such as adverse impacts on emotional and psychological health), or significant adjustment problems in some regions. Equivalent non-financial or regional benefits to pig meat consumers or manufacturers are unlikely to offset these costs (if they occur), which need to be considered in policy decisions'. (p.132)*

Draft finding 5.2 is fraught with dangerous implications not just for the pork industry, but for Australian agriculture in general. Effectively this is condoning our trading competitors to undercut our costs of production through subsidies and other forms of support so long as it results in lower retail prices for consumers.

### **2.6.2 Multilateral Agreements – Long road to reform**

The PC's remedy for existing subsidy arrangements and their impact on the competitiveness of both the global pork and the Australian domestic market is resolution through the WTO multilateral trade agreement. However, it is clear from the current rate of progress of these negotiations (without even

considering the time required for implementation once agreement is reached) that this is unlikely to be resolved in the near term and in the interim industry's such as the Australian pork industry continue to suffer injury and unfair competition from subsidised product in local and export markets.

APL is concerned that to date such measures have not tangibly improved the degree of free trade in the context of the international pork market. It would appear that recent enthusiasm by many national governments towards establishing bilateral agreements provides evidence of a similar level of frustration with the rate of progress with multilateral agreements. It is not APL's intention that the Australian Government should in any way reduce its efforts in contributing towards achieving multilateral trading agreements.

APL holds strong reservations as to likelihood of progress on this front providing significant improvements within the types of forward time frames justified by the PC's conclusions and in which most producers plan future strategies. The PC's conclusion is deficient and is not an answer to the short and medium term trade impediments, which inhibit the industry's ability to restructure and achieve competitiveness.

### **2.6.3 Overseas assistance - Apparent reduction in government support measures**

APL notes the draft Report's reference to international trends towards decoupling of government support from current production. APL highlights that contrary to the idea that there has been a reduction in support measures, the same draft report demonstrates in its Appendix C.2 and also in the report by Professor Nixon Attachment 1 that these have in fact increased in recent years. Appendix C.2 shows that between 1986/88 and 2001/03 the OECD price support estimate (PSE) increased from 18% to 21%. This analysis also shows that Australia and the USA were the only nations not evidencing an upward movement in PSE for the period measured. ABARE have highlighted how an estimated \$A11.8 billion in assistance was provided to EU pig producers in 2002<sup>3</sup>.

Hence, whilst there may well be a 'general international trend towards decoupling government support from current production, in the context of the pork production, Government assistance has in fact been increasing.

In reference to 'Box 3.5 Government Assistance and Danish export prices for pig meat', in order to present a more comprehensive analysis of the situation with Danish export prices APL suggest that a longer time frame than a single year needs to be analysed. This is especially the case in light of the fact the PC

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<sup>3</sup> Economic Assessment of the Effects of Pig Meat Imports on the Australian Industry; Sheales, T.; et al.; ABARE; May 2004

uses three years for assessing imports and a ten year time frame for profitability. The PC should ensure a consistent and methodology is applied.

#### **2.6.4 Grain prices, availability and market distortions**

APL believes that the draft report findings with respect to addressing the difficulties relating to accessing internationally competitive feed is deficient given that the report clearly acknowledges that feed costs are a key ongoing competitive disadvantage for the industry.

*‘Unless the relative profitability of growing feed grain increases, Australian grain producers will continue to produce grain for human consumption, and the pig meat industry will remain at a competitive disadvantage in this area (p.XXI Box 1 ‘Feed grain’).*

*‘Given the potential impacts of single-desk grain export arrangements on domestic grain-using industries, the Australian and relevant State governments should regularly review such arrangements to ensure their benefits outweigh the costs’. (Draft Finding 6.2)*

Pig meat production is a low margin business; therefore any cost saving, no matter how small, that can be achieved both from improving business management practices and on farm production *as well as redressing regulatory impacts resulting from public policy* will have significant positive flow on effects to the competitiveness and profitability of Australian pig producers. As detailed in APL’s previous submissions and in section of this submission, the Australian pork industry continues to finance research and undertake strategic activities to address these issues on farm and in conjunction with other grain end users as well as the grain industry.

Given these considerations the PC’s findings concerning grain availability that the government keeps a ‘watching brief’ with respect to the single desk is incongruous. At the very least, the PC should address the recommendations put by APL with regard to investigating mechanisms to deliver feed grain security.

##### **i. Single desk**

APL notes the comments by the PC relating to the implications of the single desk arrangement in Australia in respect of pork producer’s inability to access cost competitive feed grain. As noted in the PC’s draft report, in 2003 Australian pork producers paid a much higher price than the international price. As documented in APL’s second submission to the Inquiry, this issue must be addressed if producers are to maintain profitability.

Whilst the draft report states on one hand that Government actions to reduce impediments to performance and competitiveness would not be as significant as a factor such as drought, there can be no doubt that the report also recognises that existing legislative arrangements in effect critically influence

the domestic versus export price differential at times of grain shortage. Significantly, Professor Nixon found, *'the challenge Australia faces in the international pig market is being competitive from a feed cost standpoint..... there are significant quarantine restrictions on the importation of feed grain into Australia...This policy has left pig producers in a difficult position because it drives up the cost of feed grain. If Australia wants to pig exporter it needs to look closely at its grain program – it is all about low cost feed. (p.208)*

Therefore the draft finding 4.4 reference to *'reducing the few regulatory impediments is unlikely to make a significant improvement to the competitiveness of pig meat businesses'* is a misnomer and undermines the very real and significant impact that regulatory impediments such as the single desk arrangement can have on the industry's future competitiveness.

#### **ii. Sufficiency and affordability**

Considering the PC's views on the importance of feed costs to industry competitiveness, APL is disappointed that the draft report does not provide any robust recommendations on grain storage. In light of the fact there currently exists tax relief for water storage for drought risk management, the draft report should also canvass making a similar recommendation for grain storage tax relief.

APL also notes the acknowledgement by the PC of the potential for increased future ethanol production resulting in increased demand for feed grain and in turn a potential increase in price. Again, the PC fails to address the risk the current government policy on ethanol subsidies poses to future grain availability and affordability and the future competitiveness of the Australian pork industry.

#### **iii. Impact of overseas grain support measures**

Indirect subsidies for feed in the EU pork sector provide an ongoing competitive disadvantage to the Australian industry. In relation to this APL notes Professor Nixon concluded that, *"The European Union enjoys certain competitive advantages... beneficial crop production policies that have reduced the cost of feed and will continue to be an important benefit to pig production and enable them to remain competitive in the global market"*.

However, in the draft report the PC infers these are seemingly insignificant. Yet Professor Nixon categorically states that it is these very production policies that enable EU pig producers to remain globally competitive.

APL's draft Restructure Plan proposes the ongoing monitoring of this situation. As described in section 3.4, APL believes there is a role for Government in assisting industry where subsidised competition exists and is impeding the efficiency of the market to allow price signals to determine market behaviour. By identifying and quantifying its impact, this will enable a better understanding of the dynamics of the global pork industry and the

impact benefits conferred by such subsidy arrangements, (whether they are direct or indirect or WTO compliant), have on the Australian industry's ability to trade cost competitively.

### **2.6.5 Retailer pricing strategies**

In reference to the price sensitivity of pork, '2.3 Consumption of pig meat', the PC has failed to consider the pricing practices of the major supermarket chains in its analysis. Although the average price of pork at wholesale level has been very competitive versus beef and lamb, due largely to the impact of the drought, this has not translated into a similar advantage in retail prices. This is due to two common pricing practices used by retailers. Firstly, retailers have increased the retail prices and accordingly their margin on pork to compensate for reduced margins on beef and lamb for which they have not passed on the full wholesale cost increases. Secondly, despite a cost advantage to the retailers for pork, retailers have also commonly used a "line pricing" approach where all meats are the same price for a particular cut, for example for stir fry or diced cuts.

Consequently, the retail price differential between pork and competing meats is not a direct equivalent of the wholesale market, and the wholesale advantage of pork pricing has not been fully translated to the consumer. This highlights how the price of pork cuts sold to consumers is often more complicated than the draft reports assessment that *'Pig meat retail price....., generally trend with long term pig prices and domestic wholesale prices'* (p.21).

### **2.6.6 Effectiveness of marketing campaign**

In relation to assessing the effectiveness of APL's marketing campaigns, (section 4.2 - Government programs to improve competitiveness and economic efficiency – Market Development/Marketing' p.79), the PC should be aware that APL undertakes ongoing market research on the changing levels of fresh pork consumption per capita. Whilst arguments can be put forward as to how to accurately determine the relative contributions of marketing versus price as key determinants of consumer decision to purchase pork, the difficulties in apportioning these factors is not unique to the pork industry.

Regarding the Mounter, Griffith and Piggot modelling conclusions about which of APL's marketing efforts provided the greatest returns to producers, APL has reservations about the accuracy of this conclusion as many of the bacon/ham products sold are branded items and consequently individual processors also conduct their own marketing. APL's primary marketing spend is on fresh product, which is overwhelmingly not a branded product; and importantly where all the ingredients are identifiable as entirely Australian origin. (Unbranded processed product can not be distinguished as 100% Australian origin since it contains large amounts of imported product.)



### **2.6.7 Labeling difficulties**

The draft Report argues that in respect of country of origin labeling, existing institutions and regulatory arrangements, together, seem to be sufficient to limit misleading labeling of pig meat products in Australia. APL is not disputing this. What the PC has failed to appreciate, and as was stated in APL's second submission to the Inquiry, is the problematic situation of consumers being unable to make informed purchasing decisions under the current labeling laws, an assessment backed up by the Australian Consumer Association (ACA). The ACA state that there is considerable confusion in Australia surrounding the TPA terms "Made in" and "Product of". This inhibits product differentiation and subsequently puts Australian product at a competitive disadvantage. This problem has been one of the key triggers for APL initiating the HomeGrown campaign.

APL re-iterates that existing legislation regarding country of origin labeling has not enabled consumers to adequately identify the country of origin of produce they are purchasing, which in turn has restrained Australian producers from being able to properly inform consumers of the imported content of the processed and smallgoods. Consumers have a right to know what they are consuming and need to have sufficient information made available to them on which to base a purchase decision.

Currently the label "Made in Australia" allows for significant amounts of imported raw materials to be sold in processed pork products to consumers under the guise of being of Australian origin. The result of this system is that consumers are unaware that such products are actually made from imported pork products.

The confusion that surrounds "Made in Australia" and "Product of Australia" needs to be addressed by appropriate Government legislation; country of origin labeling must be introduced or at the very least labeling that clearly identifies the percentage of imported product contained within a good.

### **2.6.8 Importation of vaccines**

Regarding section '5.9 Other Potential Impediments' APL notes the comment that production costs will rise unless a cost-competitive alternative to antibiotics can be found. APL highlights that regulations regarding the importation of vaccines is a regulatory impediment that involves time consuming evaluation and in-country efficacy trials as mandated by APVMA.

In relation to the numerous references throughout the draft to Australia's favorable health status, in order to further develop this as a competitive advantage the Australian pork industry is undertaking proactive steps to further reduce antibiotic use. The increased and timely availability of effective vaccines would reduce the need for antibiotics reducing both the risk

of transfer of resistance to humans and the risk of any residues occurring in the marketed product.

## **3 Draft Restructure Plan**

### **3.0 Overview**

As briefly documented in Australian Pork Ltd's (APL) second submission to the Productivity Commission's Pig Meat Inquiry, APL has developed a draft five year Industry Restructure Plan with the key objective of radically restructuring the pork industry and its supply chains. The strategies within the draft Restructure Plan primarily seek to secure reduced costs and/or increased revenues across the whole of the pork supply chain, driven from the top down, with ongoing benchmarking against our competitors and international standards, to ensure the industry takes advantage of new market opportunities and grow existing markets. To secure the support and commitment of the whole of industry, from producer to retailer, for this plan, APL has undertaken a nation-wide industry consultation process that has encompassed the whole of the supply chain including face to face meetings with producer and supply chain participants, a survey of APL delegates conducted by an independent consultancy, and also sought, and in turn received, written submission from producers.

### **3.1 Industry Vision**

The draft Restructure Plan envisages a future Australian Pork Industry where:

- Production & supply chains are aligned with global production and trading systems resulting in reduced costs and increased industry competitiveness against imports
- Increasing efficiency & utilisation of feed including grain
- Significantly lower producer price volatility
- Rising domestic market sales of fresh meat
- Reduced penetration of processed goods by imported product
- Steadily growing niche export markets, capitalising on key competitive advantages of low disease status & geographical location
- Meeting consumer & society standards of ethical food production
- Increasing levels of regional employment & value adding

Should all strategic goals identified in the Plan be successfully achieved, APL's analysis demonstrates that by 2009 the Australian pork industry will be characterized by:

- 51% increase in domestic fresh consumption: fresh domestic sales increase from 41.2% to 51.5% of overall domestic sales, from 185.467 tonnes kg pa to 295.330 tonnes pa
- Increased export volumes from 55,884 MT MAT to 64,785 MT MAT
- 31% increase in total volume of production, from 405.898m kg to 531.906m kg

- Average 17% increase in carcass weight from 72.6kg to 84.9kg
- 12% increase in annual pig slaughter numbers from 5.591m to 6.258m
- 12% increase in sow numbers from 340,284 to 368,101
- Improved animal health, a cost saving of 7.3 c/kg = \$28.8m p.a
- Reduced feed costs by 10% equating to 13.3 c/ per kg or \$52 m p.a
- Reduced average cost of production from \$2.15 to \$1.80

However, the successful achievement of these strategies is contingent upon resolving key structural-efficiency issues within the industry. These issues, confirmed by stakeholders in APL's extensive nationwide consultations, include:

- Import penetration and impact cause the industry to be price takers not price makers
- Free versus fair trade; the notion of free trade does not appear to exist in today's markets, so let's look at securing fair trade;
- Feed cost volatility and supply: including improved grain varieties, feed conversion and efficiency and improved methods of processing;
- Supply chain efficiency: excess capacity and throughput is critical to improve the efficiency of abattoirs and boning rooms, while too many processors in the supply chain is impeding competitiveness
- Carcass measurement and payment system: P2 fat depth measurement and lean meat yield
- Transparency of pricing systems: improvement in grading and pricing arrangements based on a lean meat payment system
- Price discovery and contract negotiation to assist in managing price transparency and volatility
- Improve eating and product quality and quality assurance systems, including odour, boar taint and meat quality issues and food integrity
- Improved genetics while protecting the Australian pig herds world's best health status
- Quarantine and animal diseases (endemic and exotic): biosecurity both on and off farm is critical
- Product labeling: identification of country of origin for processed pork product ingredients
- Product development and innovation to meet consumer, retailer and food service needs
- Utilisation of legs and middles: increasing total carcass value of Japanese export specification pigs through product innovation and increased utilisation and value of remaining cuts
- Export markets – examining new potential markets and addressing barriers to these and existing markets

## **3.2 Specific Strategies**

The section below broadly covers the seven key strategies identified in the draft Industry Restructure Plan that are imperative to securing a globally competitive and sustainable Australian pork industry.

The proposed restructure strategies, in order of prioritization as agreed through the industry consultation, are:

1. Increase fresh domestic consumption from 8kg to 14kg carcass weight per head of population
2. Reduce feed costs by 10%
3. Increase average carcass weights to 85kg
4. Enhance animal health with at least two major regions free of major eradicable endemic diseases
5. Fair trade – leveling the playing field with no sale of subsidised or dumped product in Australia and improved market access for exports
6. Build loyalty for 100% Australian small goods with 85% dairy cabinet sales and 45% of deli sales identified and labeled as 100% Australian product
7. Create new pricing systems with 80% of supply on longer term pricing contracts and 85% of supply on carcass merit systems

Each of these strategies is elaborated on below.

While APL, through its consultation process, has prioritised these strategies, many of the strategies are interrelated, particularly those that relate directly to the food chain. Their success is therefore interdependent and in many cases need to be undertaken simultaneously.

The strategies identified obviously have financial and human resource implications in order to be successfully implemented. APL is currently undertaking a cost benefit analysis, with the assistance of Ernst and Young, to facilitate the prioritisation and resource allocation of the strategies relating to the draft Industry Restructure Plan as well as other key operational activities currently undertaken by the company on behalf of the industry. This analysis will be completed in late February 2005 and will provide direction for the development of APL's strategic plan for 2005/08 as well as the realignment of APL's operational activities.

### **3.2.1 Increase fresh pork sales in all markets**

#### **i. Rationale**

Increasing demand for fresh pork in the domestic market, key export markets of Japan and Singapore and targeted (new) export markets is a key driver to lifting margins and returns across the supply chain by increasing the proportion of production sold into the higher margin sectors. To facilitate

volume and margin growth in the Australian domestic market, a continued increase in consumer demand is required. Strategies need to cover retail, food service and product development programs. Most importantly, strategies to grow fresh pork demand in the domestic and export markets must be integrated.

#### **ii. Impact on Industry - High**

- The domestic market must be market driven. It is estimated this strategy will have a high impact by increasing demand for fresh pork, (as opposed to shifting pork destined for the processed market to the fresh market). This will lead to increased sales, and in turn increased average revenue, and subsequently the value and margins in fresh meat. In addition, the extra volume flows may reduce costs for some businesses.
- The impact on export markets is medium to high as the Australian industry strives to capture a greater profitable share of the targeted export markets.

#### **iii. Goal**

Increase domestic fresh meat consumption from 8kg per capita to 14kg per capita by 2008

#### **iv. Milestones**

- Increase domestic fresh meat consumption to:
  - 10.8kg per capita by 2005
  - 12kg per capita by 2007
  - 14kg per capita by 2008
- Increase fresh pork sales from 18% to 25% of total meat sales by 2006

#### **v. Key Strategic Programs**

- Export market: Drive exports to achieve long-term profitable growth of export returns
- Domestic Market:
  - Maximise returns from whole of carcass across the market mix includes eating and product quality, product development, innovation and specification
  - Increase demand for fresh pork in domestic market
  - Grow fresh pork category

### **3.2.2 Increase carcass weight**

#### **i. Rationale**

- Carcass weight is one of the key cost determinants of pork production from the farm to the consumer. On farm, an extra kilogram of pork produced does not carry any of the fixed costs of the business. This

includes the total costs of the breeding herd i.e. labour, sow costs, feeding of the sows, building costs and some other minor fixed costs such as consultants fees and accounting fees. At the abattoir the costs of slaughtering an 85kg carcass are essentially the same as slaughtering a 70kg carcass. In the boning room, costs of boning an 85kg carcass are similar to that of boning a 70kg carcass. Our key competitors in North America are now achieving carcass weights averaging 90kg, but are also producing larger pigs of up to 130kg for their domestic processing sector. This puts the Australian pork industry at a distinct cost disadvantage to our competitors.

**ii. Impact on Industry – extremely high throughout the supply chain**

- Reduces costs at production level by approximately 15c for 10kg (an additional cost saving not included is reduced feed costs per kg sold)
- Reduces costs in abattoir and boning rooms
- Enhanced cost competitiveness against key pork trading nations, (US & Canada) in both the domestic and export markets.
- Increases revenue for export market if the extra cuts not going to Japan receive a higher value in domestic market
- Engage support of retailers and consumers
- Critical that it is phased in over time to ensure increase in supply matches consumer demand
- The industry is acutely aware that great care needs to be taken so that meat quality is not impaired otherwise value per kilogram will be reduced.

**iii. Goal**

- Increase average carcass weight to 85kg

**iv. Milestones**

- Engage at least one major supermarket in consumer product trials resulting from heavier carcasses by June 2005
- Carcass specifications (i.e. from a minimum 85kg carcass) in two supermarkets and 50% of retail butchers by December 2006; and in all supermarkets and 80% of retail butchers by December 2007
- 60% of carcasses boned domestically are 85kg or more by December 2006
- Higher proportion of middles utilised in the higher margin sectors for fresh meat resulting in increased profits across the supply chain by June 2007
- Improved genetics and feeding for heavier carcasses thereby reducing costs of on farm production 7.5% by December 2009.

**v. Key Strategic Programs**

- Improved genetics and feeding for heavier carcasses

- Identify consumer drivers for negotiations with retailers regarding meals size and portion, to drive the type of cuts offered at retail and the size of the animal at trade level
- Deliver boxed pork and case ready on shelf with pork cut to consumer portion size prior to delivery to retailer
- Develop new product range of individual muscle cuts - meet consumer, retailer and food service needs, including eating and product quality, product development and innovation

### 3.2.3 Reduce feed costs

#### i. Rationale

##### **Pork CRC:**

The cost of production, and thus profitability of the industry, is largely determined by feed prices (63% of total costs in 2001/02, 68% in 2002/03) and the efficiency of feed conversion to pork product. Feed costs are close to those in the USA and Canadian pig industries in good years, but are more prone to large increases in poor harvest years than in competitor countries due to a lack of ability to import supplies at world parity prices. Feed prices are heavily influenced by a lack of dedicated feed grains suited to the pig industry, high and variable prices of cereal grains in times of drought, increasing scrutiny from domestic and export markets over some traditional protein sources used in pig diets (e.g. animal protein meals) and the transport costs of feed ingredients.

##### **Grain importation:**

An alternative strategy is to develop a quarantine protocol, approved by Biosecurity Australia, which allows for the cost effective importation of grain and shipment to production areas when needed, based on a new fumigation process developed and patented by CSIRO. This would have the effect of dampening price rises in years of low grain supply, thereby reducing the average cost of feed.

##### **Strategic Procurement:**

This commercial service has historically been the responsibility of producers and it is likely that there may be little pull from producers to establish such a function, as well as APL reservations about becoming involved in such a service. However, when the Australian pork industry is compared to the US/Canadian pork industries approach to the purchasing of feed ingredients, it is clearly fragmented and hence faces a cost disadvantage of at least an estimated \$40 per tonne<sup>4</sup>. The Australian

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<sup>4</sup> Based on ProAnd study comparing the value chain for pork production in Australia with that in Western Canada (ProAnd 2000) quoted in Economic Assessment of the Effects of Pig Meat Imports on the Australian Industry; Sheales, T.; et al.; ABARE; May 2004



pork industry must address how it can best leverage its feed volumes to lower costs; this may be through a more strategic approach to feed ingredient procurement.

**ii. Impact on Industry – very high particularly for producers**

This strategy will significantly reduce the cost of production because feed costs represent 55% to 65% of total production costs at farm gate, depending on season.

**iii. Goals**

- Reduce average cost of pig feed by \$ 30/tonne (10%)
- Increase mean energy yield from feed grains by 1 MJ DE/KG
- Increase the efficiency of feed conversion from 4.2 to 3.5 kg of feed for every 1 kg of carcass weight
- Reduce volatility in feed prices - collaborative purchasing arrangements (leveraging feed volumes to lower costs) and improved producer risk management tools and skills
- Capability to import grain cost effectively and transport to regional Australia

**iv. Milestones**

**CRC**

- Enhanced existing triticale varieties and agronomic recommendations provided annually from 2006
- Management practices and quality assessment practices to effect improved barley supply to pig producers by 2007
- Field pea and pearl lupin varieties for northern cropping regions from 2007 onwards
- Initial near infrared reflectance spectroscopy (NIRS) calibrations for pig ileal DE, faecal DE, intake of available energy, chemical and physical characteristics of cereal grains completed by June 2006
- Initial NIR calibrations developed for protein rich ingredients by June 2008
- Novel or improved methods for processing cereal grains, including enzymatic treatment, to increase economically their nutritional value for pigs from June 2008
- Method for the practical and continuous measurement of feed disappearance in groups (i.e. a pen of pigs at least daily) by 2009
- Evaluation of methods to assess individual feed intake by 2009
- Release of first new non-antibiotic probiotic-based products that control specific disease from 2009
- Cost-effective applications for Ractopamine from 2008

- Existing industry reproduction manual to incorporate strategy for gilt breeding developed to maximise life-time reproductive performance by 2009
- Validation of a model that can be applied to reduce seasonal infertility by June 2009.

#### **Grain Importation**

- Proven technology that enables the cost effective importation of grain by 2006

#### **Strategic procurement**

- Improved feed buying practices by December 2005
- Protein hedging by December 2006
- Producer feed risk management is an ongoing business practice in three states by 2006
- Strategic procurement of grain through industry collaborative purchasing arrangements by 2007

### **v. Strategic activities**

- Pork Co-operative Research Centre
  - Innovative grain and pulse production and quality assessment;
  - Optimise herd feed conversion efficiency through better health, reproductive capacity and metabolic efficiency;
  - Better value and versatility of pork product;
  - Improved flow of technical information and technology adoption
- Grain importation – capability to cost effectively import grain and move to regional production areas where needed
- Strategic procurement of feed
  - Improved feed buying practices including industry collaborative purchasing arrangements
  - Producer feed risk management tools and skills to manage price volatility
- Build effective working relationships with feed industry - research feed grain varieties; develop dedicated feed grain industry

### **3.2.4 Create new pricing systems**

#### **i. Rationale**

The current method for predicting carcass value (P2 fat depth) no longer predicts lean meat yield with sufficient accuracy to support payment systems. It is inherently prone to unacceptable operator error and does not have the confidence of producers. A new measurement and payment system is needed

that better reflects one of the two components of true commercial value of carcasses (i.e. lean meat yield).

As the pork industry continues to rationalise and consider vertical and/or horizontal co-ordination arrangements, there is a pressing need to establish market price discovery mechanisms to provide greater transparency of market pricing. Enhancing price transparency will encourage the development of long-term supply contracts ensuring greater supply chain stability.

#### **ii. Impact on Industry - High**

- Whilst unlikely to change the average price per carcass, this will reward suppliers with more commercially valuable carcasses and support improvements in carcass lean meat yield over the longer term (e.g. genetic improvement). This strategy will also eliminate the work that goes into pricing decisions each week by identifying the key drivers of domestic pork prices so that appropriate strategies can be developed to reduce the volatility in pork prices. However success is dependent on industry agreeing on the mechanism that is adopted; the current system of uncertainty is untenable.

#### **iii. Goals**

- 80% of production in long term pricing arrangements
- Lean meat yield based payment grids replace P2 in carcass assessment

#### **iv. Milestones**

- All key stakeholders sign on to AUSKEY as the official carcass measurement system in Australia by March 2005
- AUSKEY installed in all major pork abattoirs by March 2006
- 60% of pork kill covered by AUSKEY carcass evaluation by March 2006
- 85% of pork kill covered by AUSKEY by end 2006
- 40% of production in long term pricing arrangements by December 2005
- 80% of production in long term pricing arrangements by December 2007

#### **v. Key Strategic Programs**

- Carcass measurement and payment system includes commercial validation of AUSKEY and direct belly measurement to predict lean meat yield (LMY)
  - Installation of AUSKEY in all major abattoirs
  - New LMY based payment grids designed and in use, including profitability indicator for abattoirs and boning rooms
- Price discovery and contract negotiation – develop mechanisms to assist in managing price volatility and price transparency

### **3.2.5 Enhancing animal health**

#### **i. Rationale**

This goal is driven by two key principles: that consumers are going to be demanding reduced use of antibiotics in pork production and that disease is one of the key cost components in pork production. Costs in PigStats are 10c/kg DW but these are only the direct costs. Indirect costs are estimated to be 20 to 30c/kg DW due to reduced growth rate loss, feed conversion loss and mortalities. Disease also contributes to yearly variation in profitability and within the ability for herd conversion to meet in slaughter specifications and product quality.

The primary aim is to eliminate mycoplasma pneumonia, pleuropneumonia and mange from the country. Switzerland is currently looking to produce country freedom from mycoplasma pneumonia and the USA is examining the possibility of eliminating PRRS from the country. A secondary aim would be to create regions that are free of endemic diseases. The continued control, eradication and surveillance programs for feral pigs are also important to the success of this strategy.

#### **ii. Impact on Industry - Medium**

- This strategy has the potential to achieve large cost reductions at a farm level. It will also improve market opportunities by producing antibiotic free pork. It is critical that strategies are designed to ensure minimal disruption of supply to the abattoirs and market (i.e. by targeting April to June quarter). This will also have the additional positive affect of stabilising prices during this period.

#### **iii. Goals**

- To reduce costs at farm level through reducing endemic disease levels

#### **iv. Milestones**

- 80% of eligible producers destocked and restocked by 2008 (i.e. 20% of eligible producers destocked and restocked each year over the next four years)
- A minimum of two pork producing regions are free of endemic respiratory disease by December 2007

#### **v. Key Strategic Programs**

- Develop options and appropriate strategies for herd disease and regional eradication
- Implement eradication program with minimal supply disruption to abattoirs and market
- Improved farm and national biosecurity and surveillance
- National livestock identification and product traceability

### **3.2.6 Build consumer loyalty for 100% Australian smallgoods**

#### **i. Rationale**

Labeling has been of concern to the pork industry for much of the last 10 years. APL has been actively pursuing Country of Origin Labeling (CoOL) for some years and although FSANZ is currently undertaking a review of this matter, the likelihood of successfully extending CoOL to ingredients is highly unlikely due to opposition from a number of major agricultural industries. While it is likely that CoOL will be extended to the cover all deli cabinet products, unless it includes identification of the country of origin of ingredients (and thereby addresses one of the major weaknesses of the Made in Australia label), CoOL will still leave consumers unable to clearly differentiate imported product. Given that domestic ham, bacon and smallgoods contain a significant portion of imported pig meat it is imperative to create a commercial solution to this regulatory problem - the creation of an industry sponsored consumer recognized point of difference.

To provide this differentiation and to address the capacity to partner this across a range of other Australian food producing industries, APL has created and initiated the commercialisation of what has become known as “Australian HomeGrown”. APL’s intention is to facilitate consumer loyalty for 100% Australian ham, bacon and smallgoods through the HomeGrown initiative. To ensure HomeGrown’s integrity, it is proposed that the program is audited.

#### **ii. Overall Impact - High**

If successfully executed and funded, this program has the potential to make a significant contribution to the domestic pork and smallgoods industries.

#### **iii. Goals**

- 85% of smallgoods sold in dairy cabinet are 100% Australian origin
- 45% of smallgoods sold in the deli cabinet are 100% Australian origin

#### **iv. Milestones**

- Ham and bacon promotions in dairy case of one leading retailer utilising HomeGrown by 2005
- Three major small goods manufacturers utilising HomeGrown branding on prepackaged small goods for display in dairy case by June 2005
- Ham and bacon promotions in deli section of two leading retailers utilising HomeGrown labeling by September 2005

#### **v. Strategic activities**

- HomeGrown used as country of origin labeling mechanisms across a range of products

- HomeGrown promotion & uptake by supply chain and consumers

### **3.2.7 Trade Measures - Levelling the playing field**

#### **i. Rationale**

Falling import prices and increasing import volumes when combined with market distortion, structural inefficiencies in the supply chain and the composition of the pork market, have effectively capped domestic prices and limit producers' ability to recover costs.<sup>5</sup> The Australian pork industry operates in a heavily distorted international market, particularly in respect of the level of EU assistance and indirect support arrangements in place in other pork producing competitor countries. Unlike other countries such as the US, Canada and the EU, Australia does not have either an export subsidy program or a farm income support system.

The market distorting practices of competitors diminish the industry's capacity to fairly compete in both the domestic and international markets. These support arrangements provided to our competitors are a major challenge to the Australian pork industry.

For example, over two thirds of the imported pork sold in Australia comes in the form of legs and middles, with the latter being overwhelmingly supplied from Denmark. As the processed market and the fresh market are inextricably linked, any artificial downward pressure placed on pork product supplied into the processed sector in turn has a similar price lowering effect on the Australian fresh pork sector. Whilst Danish middle cuts may only compete directly with Australian middle cuts, the price distortion impact of EU support measures flows through to the Australian fresh pork market. ABARE reports that EU producers receive 26% of their earnings from the government, mostly in the form of market price support. The Canadian and US pork industries also benefit from indirect and/or WTO legitimate subsidies.

Critically, the impact of EU assistance to Danish pork producers in the form of export subsidies, production support and market access restrictions places an artificial cap on prices by not allowing price signals to determine market behaviour. Such behaviour exacerbates the downward pressure on world prices, adds to their volatility, and shifts much of the resulting pressures for adjustment on to unsubsidised or lightly assisted industries in countries such as Australia that have relatively open markets. The same is true of indirect subsidies and other support arrangements to both grain and fresh pork; they distort the global market for pork.

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<sup>5</sup> This is documented in APL's first and second submissions to the PC Pig Meat Inquiry.

In principle, the industry can undertake trade measures. However, trade measures such as countervailing and/or antidumping actions are extremely complex, difficult to prove, very slow to progress and costly.<sup>6</sup>

## **ii. Overall Impact - High**

If fairer trade arrangements can be achieved, this has the potential to ultimately impact on price received by Australian producers in both the domestic and export markets.

## **iii. Goals**

- No sale of subsidised or production supported commodity into the Australian market
- Improvement in market access in export markets

## **iv. Milestones**

- Provision of Australian Government resource support to the industry to collect and analyse information and data on support arrangements a in pork producing nations by 2005
- Establish framework to track real time national and sub national assistance received by exporting nations' pork producers and their supply chain by December 2006
- Completion of the updated industry Export Strategy by June 2005
- Recognition of injury to industry from imports (where proven) through the implementation of appropriate trade measures such as tariffs, quotas, import levies and/or government assistance by June 2005
- Key government departments and members of parliament (state and federal) sound understanding of Australian pork industry trade position by December 2006
- Zero for zero tariff global pork in WTO multilateral trade round

## **v. Strategic activities**

- Reduction in trade and non-tariff barriers in key export markets
- Advance Australian pork industry interest in collaboration with the government in bilateral and WTO trade negotiations
- Secure appropriate trade actions to protect industry from injury from imports and/or unfair competition
- Develop monitoring mechanisms and analysis of direct and indirect support arrangements and non tariff barriers in key competitor markets
- Real time data collection, price monitoring and analysis of pork imports

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<sup>6</sup> These problems are documented in more detail within APL's second submission

### 3.3 Programs underway

A number of programs in the draft Restructure Plan have already commenced. Key amongst these are: the Homegrown campaign; the Pork Cooperative Research Centre (CRC); research into new carcass measurement systems; research into alternative pork cuts; assessing global best practice in the pork supply chain; identifying potential new markets; export market evaluation and selection; and identifying production specifications for future export markets. More specifically these respective programs entail the following:

- **Homegrown:** As previously documented in earlier submissions, the Homegrown campaign has received an initial \$4m in matching funding from the Australian Government over two years. The newly established Homegrown Executive is now in the process of arranging further funding from various agricultural and non-agricultural organisations. An official launch of the program occurred on Australia Day 2005 throughout all Coles' supermarkets in Victoria.
- **Pork CRC:** In late December 2004 the Pork CRC proposal was successful in obtaining Australian Government funding to the extent of \$25m. The CRC will address the need to reduce feed costs, look at better utilisation of that feed which is available, promote the development of value-added products for domestic and export markets thereby providing the pork industry with the ability to compete on criteria other than just price, and provide an education and training program allowing the industry to recruit more scientists into the industry.
- **APL Carcase Evaluation Program:** APL has commenced a program to evaluate, and possibly improve, the accuracy of a relatively new carcase measurement system from the USA for predicting lean meat yield in pig carcasses using hand-held, real-time ultrasound imaging equipment. Since APL funded a demonstration of this system in three major abattoirs during 2004, 9 processing companies have expressed interest in trialling or installing the new system. As part of this program, APL is working with the USA company to develop new prediction equations of more relevance to the local market. One hundred and fifty carcasses from a local abattoir have been imaged in various locations with the ultrasound scanner. One half of each carcase has been boned out to give a wholesale saleable meat yield, whilst the other half has been scanned through a CAT-Scanner designed for human medical applications to give highly accurate estimates of body composition, including muscle yield. Any new calibrations developed will be validated in 2005 under commercial conditions in abattoirs using commercial yield estimation techniques and then used to develop new payment systems for pig carcasses based on a more accurate prediction of their actual market value.



- **Pork Market Improvement Program**
  - i. **Research into Alternative Pork Cuts:** As part of the Pork Market Improvement Program (PMIP) APL is undertaking a global carcass fabrication analysis. This entails trialling and reporting on alternative carcass fabrication techniques and yield variations from carcasses. Specifically it is intended that a commercial trial be undertaken using the identified cutting lines from major competitors (Canada, USA, Denmark) to determine improvements that can be made on current carcass specifications. This project will involve reviewing and training boning staff on cutting techniques and designating a boning room for a specific trial.
  - ii. **Assessing Global Best Practice in the Pork Supply Chain:** This program involves benchmarking the entire Australian pork industry supply chain against global best practices of leading pork producing and exporting nations. It seeks to identify the necessary actions that need to be undertaken to improve the competitiveness of the Australian pig meat industry. In turn, gaps evident within the Australian industry's supply chain cost structures, quality and reliability will be clearly identified.
  - iii. **Identify Potential New Markets: Global Trade Barriers and Freight Costs Analysis** - This involves research into the identification of potential new (mainstream and niche) markets, including those in Asia (eg. Taiwan), North America and Europe. It will identify trade and non-trade barriers and other access issues preventing entry into specified markets including freight costs; unique characteristics of Australian fresh pork cuts; and the ability for Australian pork products to be price competitive
  - iv. **Export Market Evaluation and Selection: Identify Production Specifications for Future Export Markets** - Based on the global supply chain information gathered export market opportunities will be evaluated and selected for Australian pork access based on Australia's unique product offerings and possible new product development with demand opportunities in global markets including the ability for Australian pork to be price competitive.

### 3.4 Government involvement

Whilst industry is the primary driver for the implementation of the draft Industry Restructure Plan strategies and related programs, the Plan entails two key areas in which the Government has a key contribution to make,

namely animal health and trade. In addition to this, APL views Government efforts to address the ongoing difficulties faced by the pork industry resulting from the current single desk arrangement as critically important in respect of achieving a more internationally competitive feed arrangement. (APL considers that further assistance with respect to other strategic areas of the Restructure Plan is likely to be sought from existing Government programs.) The specific nature of Government assistance sought is detailed below:

- **Animal health:** Assistance is envisaged being possibly regulatory in nature as well as funding support for this initiative. In order to successfully achieve the objective of eradicating several endemic pork diseases, a regional destock– restock process needs to be undertaken which can best be achieved through a Government coordinated approach.
- **Trade:** As detailed previously in APL’s second submission to the inquiry, APL believes that there is a role for Government in assisting industry where subsidised competition exists which impedes the efficiency of the market to allow price signals to determine market behaviour. These market distortions add further downward pressure on world pork prices and shift much of the resulting pressure for adjustment to unsubsidised industries with open markets such as the Australian pork industry. The Government has available traditional tools – direct industry assistant payments and WTO legitimate trade measures (and not just Safeguard measures) to ensure Australian industries have an equal footing in domestic and international markets. The government has the resources and capability to assist with the tracking, collection and analysis of data with respect to direct and indirect assistance measures apparent amongst key competitor markets. This could be similar to the steel monitoring currently undertaken by the Australian Customs Service and reporting to a Monitoring Committee established in 2002 by the Ministerial Task Force on steel imports.

More specifically, there needs to be ongoing real time monitoring of domestic agricultural support programs (both at a national and sub-national level), including the evaluation of the benefits such support programs have on goods produced in those key competitor markets and exported to Australia. In short, appropriate mechanisms need be put in place at a governmental level to ensure Australian industries are able to take advantage of WTO sanctioned trade measures so that they can compete in the market against products that receive the benefit of overseas domestic support policies, whether in the form of direct or indirect subsidies or both.

- **Trade (anti-dumping):** The interpretation of legislation concerning “like goods” needs to be made simpler. The issues raised here are not unique to the Australian pork industry but are a shared concern across many different sectors. The Government has the opportunity to be proactive and to engage industries to address this impediment to enabling industries to undertake actions where injury is being caused.

## **4 Conclusion**

In summary, this report suffers principally from constrained terms of reference (over which there was no consultation with industry), a brief that was far too comprehensive for the time provided for the Inquiry and a failure by the writers not to adjust that nature of the analysis to the wholly inadequate information base they had to work on. The current state of the draft report, therefore, is of great concern to APL due to the fact the Government, the industry and the broader community places much weight on the PC's capacity to provide robust, objective analyses of the competitiveness of the industry and what industry and the Government can do to change these circumstances. In its current form the draft report does not fulfil this purpose; the PC must first properly and accurately characterise the state of the industry before conclusions and recommendations can be made.

APL contends that these matters need to be adequately addressed so as to ensure the final Pig Meat Inquiry Report provides for well-substantiated conclusions or at the very least these conclusions are adjusted to reflect the inability to provide such analysis due to the inadequate information and/or timeframe available. The conclusions are dangerous for leaving an impression they are better based than they are.

### **4.0 Key Recommendations**

#### ***Recommendation 1***

APL recommends that the Productivity Commission seek an extension on the deadline for completion of the report. This action is necessary in order to ensure that both a proper (technically-sound, methodologically consistent) analysis of the condition of the industry is undertaken and that the options for assistance have been properly analysed.
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#### ***Recommendation 2***

The PC properly and accurately characterise the state of the industry to ensure substantive conclusions and recommendations are made. The final report should include an investigation of the link between the structural change in the industry and the structural forces that have contributed to the continual erosion of the industry's competitiveness, including the relationship between major increases in import penetration (however measured) and depressed prices, inadequate returns, higher risk, and reduced investment.
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***Recommendation 3***

APL and the broader pig meat industry have provided a substantial amount of information about the condition of the industry, but is concerned that it has been set aside because it was produced to support the imposition of safeguard measures. APL requests that this information be taken into account including the data provided in relation to industry profitability in order to present a more accurate analysis of the industry including its financial position.

***Recommendation 4***

The PC should examine all policy instruments available to government including traditional tools – direct industry assistance and trade measures (and not just Safeguard measures). Border measures are legitimate instruments to facilitate structural adjustment. A full and proper assessment should then be undertaken to determine the relative merits of prospective measures in respect of structural adjustment and improving industry competitiveness.

***Recommendation 5***

The PC set out a methodology at the beginning of the report so that it is possible to assess the relative merits of prospective measures or make findings on such measures, particularly in respect of structural adjustment.

***Recommendation 6***

APL recommends the PC cease the selective use of data in critical areas of analysis. For example, a longer time frame should be considered when assessing the impact of imports so as to present a more accurate picture of the extent of increases. APL advocates a ten year period be covered which will also provide a level of assessment consistent with the time frame used to discuss profitability of pig producers.

***Recommendation 7***

It is well understood that the PC may feel a general reluctance to consider using trade measures as a tool to support industry assistance, however, they are not precluded from Government policy and they are a legitimate measure in a multilateral trading environment. As the PC is not excluded in its terms of reference from examining the impact of imports, it should therefore assess the option of safeguards including the impact of such a measure on all parties and reach a recommendation on whether a safeguard investigation is warranted.

***Recommendation 8***

The PC's must also extend its analysis to properly characterize and quantify the impact of support arrangements enjoyed by our competitors and provide substantive solutions to these impediments to industry competitiveness. These arrangements are not insignificant in their effect on the Australian pork industry nor quickly remedied through multilateral trade negotiations as the PC's report suggests. These market distortions add further downward pressure on world pork prices and shift much of the resulting pressure for adjustment to unsubsidised industries with open markets such as the Australian pork industry. Attachment 1 in the report clearly shows both the direct and indirect effect of such support arrangements in providing our competitors with an iniquitous competitive advantage.

***Recommendation 9***

The PC must undertake the detailed technical analysis required to prove draft finding 5.2, which indicates that trade distorting behaviour of international competitors is acceptable, if it leads to lower prices for consumers, even if that behaviour had adverse effects on Australian pork producers and by implication the rural and regional communities that depend on them. The test must be empirical, not theoretical and in the absence of such analysis this finding should be adjusted to reflect this.

***Recommendation 10***

The PC reassess its draft finding 4.4 that 'reducing the few regulatory impediments is unlikely to make a significant improvement to the competitiveness of pig meat businesses' due to the fact that in a low margin business such as pig meat production, the collective impact of regulatory issues such as the single desk arrangement, animal welfare and environment matters can in fact have a significant impact on production costs and by implication the industry's future competitiveness. In particular, the PC's findings with respect to grain sufficiency and affordability, including that the government keep a 'watching brief' with respect to the single desk, are deficient. At the very least the PC should investigate earlier recommendations put forward by APL with regard to investigating mechanisms to deliver feed grain security.

**Appendix A - The financial condition of the pig meat  
(from first submission)**

CONFIDENTIAL INFORMATION REMOVED