

Beef Levy Review 2009 – summary



Letter from the Chair

Right now, the Australian beef industry is facing perhaps some of its toughest challenges.

Low livestock prices are hurting all producers. Lingering effects of BSE in our most valuable export markets, the impact of long-running drought on supply and costs, high grain and fertiliser prices, and an oscillating Australian dollar are all affecting our industry. We've enjoyed the windfall of the exclusion of US beef from our key North Asian markets, but we've also suffered the challenge from Brazil with its advantageous currency position for much of the last decade. And now we're challenged by the contraction of the credit necessary for global trade, by the financial crisis being felt in all key markets and by the prospect of greater environmental regulation.

On the positive side, demand for Australian beef, both at home and in export, has continued to be strong, aided by improving consumer appeal and the growing reputation of the Australian industry as a safe and reliable supplier of quality beef. While production issues and costs will always be a challenge for producers, the Australian industry appears to be well positioned to benefit as the world emerges from this recession.

The Australian industry will never succeed in the global market by relying on cost competitiveness alone. We have higher labour costs, higher standards, greater expectations from the community and larger distances to our main export markets than most of our competitors. Australia can only succeed by out-performing competitors on quality and consistency, on reassurance of safety, on reliability of supply, on consumer appeal, and on overall value for money.

So I was pleased to accept an invitation to chair a committee of industry leaders to review just how well the programs we fund are doing that, and to consider

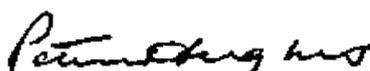
the future program and funding needs for marketing Australian beef.

The Beef Marketing Funding Committee, comprising 14 people from levy paying enterprises across Australia, met on six occasions, and considered the following questions:

- a) Has the 2006 increase of \$1.50 per head in the beef marketing levy delivered benefits to our industry?
- b) What have been the major influences on livestock prices since 2006?
- c) What are the key challenges and opportunities likely to face the industry over the next five years?
- d) What would the marketing program scenarios be under a range of funding levels?
- e) What is the appropriate level of spending on these programs?

To assist us in answering these questions, we commissioned independent expert analyses from Warwick Yates and Associates and from the Centre for International Economics. We invited and received insightful submissions from levy payers, large and small. We also sought information from and challenged the staff of Meat & Livestock Australia.

I am pleased now to present this report of our deliberations and recommendations, and sincerely thank the members of the Committee for their time and contributions to this important task.



Peter Hughes
Chair of the Beef Marketing Funding
Committee
May 2009



Beef Marketing Funding Committee members

Mr Peter Hughes (Chair), cattle producer, North Queensland

Mr Don Heatley, cattle producer, North Queensland and Chairman, Meat & Livestock Australia

Mr Jim Cudmore, grain-fed cattle producer, South-East Queensland and President, Australian Lot Feeders' Association

Mr Peter Hall, cattle producer, North Queensland and member of Cattle Council of Australia

Mr Bill Bray, cattle producer, Victoria and Immediate Past President, Cattle Council of Australia

Mr Mike Introvigne, cattle producer, southern Western Australia

Ms Jen Munro, cattle producer, north-west New South Wales

Mr Ian McCamley, cattle producer, central Queensland

Mr Warren Barnett, grain-fed cattle producer, southern New South Wales and Vice President, Australian Lot Feeders' Association

Mr Brad Teys, CEO, Teys Bros Pty Ltd

Mr Terry Nolan, Director, Nolan Meats Pty Ltd and Chair, Australian Meat Industry Council

Mr Michael Carroll, cattle producer, western Victoria and Director, Meat & Livestock Australia

Mr Don McDonald AM, OBE, cattle producer, north Queensland

Mr Gary Tapscott, Commercial Manager Sheep & Cattle Operations, Elders and Director, Australian Livestock Exporters Council and President, Australian Livestock & Property Agents

Beef Levy Review 2009



Why was the review conducted?

The review was conducted to evaluate the effectiveness of the increased marketing component of the cattle transaction levy since 2006, and also to determine the appropriate level of funding for beef marketing and trade development to ensure Australia's beef industry is competitively positioned.

What was the process?

An independent committee was formed under the chairmanship of Queensland cattle producer Peter Hughes. The Committee sought submissions from the industry and MLA, and also commissioned independent analyses on the benefits to industry from previous marketing expenditure.

What were the Committee's findings?

- a) The additional marketing levy has delivered five times the investment back to producers.
- b) The major impacts on livestock prices since 2006 have been high exchange rates and high grain prices until late 2008, and now credit restrictions on global trade and the collapse in demand for co-products. Without these impacts, livestock prices would be at or near record levels.
- c) Our industry faces critical challenges, such as mounting attacks on our environmental integrity and increased competition in our major markets; as well as valuable opportunities, such as our world leading systems in product quality, safety and industry integrity, which stand us in good stead to grow existing and capture new markets.
- d) The industry must continue to invest in a broad range of programs to consolidate its position in beef markets and address the challenges and opportunities that lie before it.
- e) The \$5 levy is a modest but appropriate investment in the future of the industry.

What does the Committee recommend?

1. That the current \$5 per head cattle transaction levy rate be retained.
2. That a minimum return on investment to producers be set at three times the overall marketing levy as the performance yardstick in future reviews.
3. That future reviews of the levy be undertaken as a result of industry need, triggered by the peak councils, and not according to a pre-determined timeframe.

How do producers have a say?

The findings and recommendations of this review will now be the subject of industry debate in forums across the country leading up to a vote of all levy payers to be conducted in conjunction with MLA's AGM in November 2009.

Key findings of the Beef Marketing Funding Committee



a) Has the 2006 increase of \$1.50 per head in the beef marketing levy delivered benefits to our industry?

The Committee concludes that the additional marketing levy has delivered five times the investment back to producers.

The independent review conducted for the Committee by Warwick Yates and Associates concluded that the \$1.50 increase to the cattle transaction levy for beef marketing since 2006 has been invested wisely and is returning significant financial benefits to the Australian beef industry.

Specifically, the increase in beef marketing investment has made important contributions towards:

- helping Australia capitalise on the absence of our major beef competitor (the US) in Japan and Korea, and positioning us to compete with the US as they return;
- helping maintain very high levels of consumer expenditure on beef within the domestic market in the face of calls to reduce red meat consumption on environmental and health grounds;
- establishing offices and personnel in Russia and China to support and help position Australian beef within these emerging markets;
- strengthening Australia's livestock export market position, particularly within Indonesia; and
- enhancing the evolution of the Australian industry from the status of a commodity supplier to that of a trusted source of quality beef products.

The analysis by Warwick Yates and Associates, supported by the Centre for International Economics (CIE) Global Meat Industry Model, calculated that the additional \$1.50 is returning between three and eight times the levy payer investment, with the most likely return being five times.

b) What have been the major influences on livestock prices since 2006?

The Committee concludes that the major impacts on livestock prices since 2006 have been high exchange rates and high grain prices until late 2008, and now credit restrictions on global trade and the collapse in demand for co-products. Without these impacts, livestock prices would be at or near record levels.

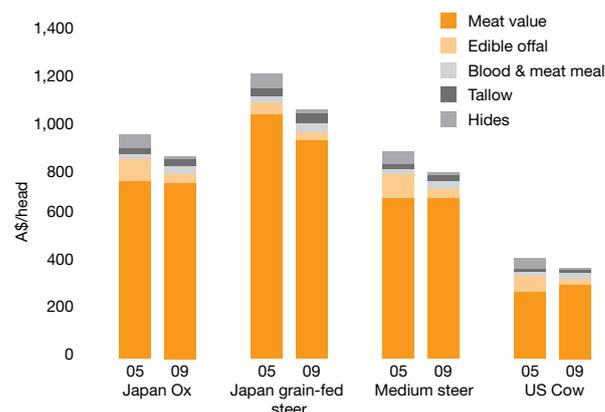
With Australia's competitiveness in global beef markets impacted significantly by the very high Australian dollar (A\$) in 2007-08, and now with the global financial crisis disrupting international trade, the marketing component of the \$5 cattle transaction levy is helping cushion Australian livestock prices from the worst of these negative forces.

Livestock prices have fallen by around 11% from the levels recorded in 2005, due to three very significant factors that more than negated the positive impact of the industry's marketing investment:

- The Centre for International Economics (CIE) concluded that the biggest single issue impacting on Australian cattle prices over the period 2005–2008 was the very high A\$. In 2008, if the appreciation of the A\$ had not occurred, cattle prices would have averaged 16% more than those observed.
- The dramatic fall in the A\$ at the end of 2008, together with the global financial crisis, has caused a severe disruption to global trade in beef, which means the price benefits likely to flow from a relatively low A\$ have not yet been realised.
- A potentially longer term impact from the global financial crisis has been substantial falls in demand for hides and offal. The decline in values of these co-products accounts almost entirely for the decline in livestock prices between 2005 and today. In fact, excluding grain-fed steers the meat value of the carcass is actually higher today than it was in 2005.

In the Committee's view, based on the evidence we have accessed, cattle prices are stronger today than they would otherwise have been, and the marketing activities funded by the cattle transaction levy have been a significant contributor to this outcome.

Estimated components of saleyard cattle value



Source: MLA calculations based on co-product prices and advice from Kurrajong Meat Technology and NLRs average saleyard prices

c) What are the key challenges and opportunities likely to face the industry over the next five years?

Challenges

- Countering increasing misinformation in the community, both domestically and in overseas markets, about our environmental impact
- Continuing to defend our position in major North Asian markets in the face of the return of the US
- Reinforcing red meat's nutritional position as an important part of a healthy diet
- Competing with significant volumes of cheaper product entering our overseas markets from South America and India
- Addressing the threat of reduced beef demand in our major markets from the current economic crisis

Opportunities

- Capitalising on our world leading systems in product quality and safety
- Claiming our share of the increased demand for beef expected to be delivered by longer term global population growth
- Developing new markets and identifying market niches for Australian beef around the world
- Building greater recognition of our industry's strong credentials in health and nutrition, environmental stewardship, animal welfare and consumer appeal

d) What would the program scenarios be under a range of funding levels?

The Committee determines that the industry must pursue a broad range of programs to consolidate its position in beef markets and address the challenges and opportunities that lie before it.

i. Without current funding levels, the position of Australian beef on the global market would be compromised.

A reduction in funding would necessitate cuts in marketing activities, such as:

- discontinuing some key domestic consumer campaigns;
- scaling back international programs designed to promote Australian beef's points of difference – trust, integrity, trade and consumer reputation; and
- reducing the industry's capacity to manage and respond to issues and crises that may arise.

ii. With additional funds, MLA could strengthen the industry's defences against known challenges and further exploit expected opportunities in domestic and global markets.

The key areas that would attract additional funding were it available are:

- stronger positioning of Australian beef in Korea and Japan as competition from US beef ramps up;
- further promotion of the industry's environmental and animal welfare integrity in the domestic and increasingly overseas markets; and
- more aggressive promotion of both chilled and frozen beef and cattle exports in South-East Asia.

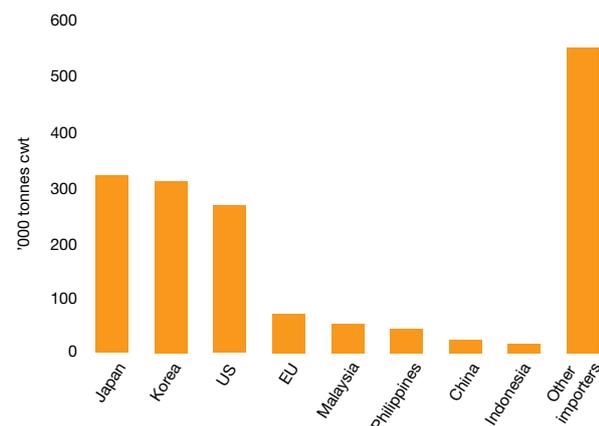
iii. Barring unforeseen issues emerging, the current marketing levy should generate sufficient funds for MLA to consolidate the market position of Australian beef.

In order for the Australian red meat industry to continue to 'punch above its weight' on the global beef market, a coordinated approach is required to undertake those important activities that help position the industry, which cannot be reasonably pursued by commercial enterprise alone.

Australia's market access to global beef markets may be improved via opportunities for free trade agreements (FTAs) with Korea, Japan and China. On the other hand, we may face competitive challenges if other supplying nations develop their own FTAs with these key markets before Australia does.

Greater understanding of our systems such as the National Livestock Identification System (NLIS), Livestock Production Assurance (LPA) and Meat Standards Australia (MSA) can play a vital role in protecting the access we currently enjoy as well as advancing penetration into global markets.

Projected beef import growth by country 2008–2015



Source: Centre for International Economics, OECD/FAO



Key findings of the Beef Marketing Funding Committee



In **Japan** and **Korea**, our industry faces a formidable competitor in the US as it seeks to recapture its share of these valuable markets.

MLA's programs in Japan and Korea are aimed at achieving four critically important objectives for the industry:

1. defending the current strong foothold to maintain our leading market share;
2. continuing to develop the image and experience of Australian beef as a high quality, safe, wholesome, good value product;
3. expanding beef exports by contributing to continued beef consumption growth; and
4. reassuring an increasingly concerned Japanese market about the environmental integrity of Australian beef production systems.

We endorse MLA's focus in these markets on:

- further strengthening trade relationships and attitudes, maintaining retail distribution and expanding product offerings;
- expanding collaboration with exporters through partnership programs (ICAs);
- further promotion of Australia's systems (NLIS, LPA and Eating Quality Assured) to build trade loyalty; and
- promotion of the health benefits of beef to consumers.

The domestic market is seeing increasing calls to reduce red meat consumption on environmental and health grounds ...

The **domestic** market is seeing expenditure levels on beef threatened, particularly in the current economic environment, along with increasing calls to reduce red meat consumption on environmental and health grounds, however the recent trend back to more structured and wholesome family meal times provides opportunities for further growth.

We believe the priority areas in the domestic market to be:

- promotion of good value, high appeal family meals;
- reinforcing the important role of red meat in a healthy diet;
- countering adverse environmental and health claims; and
- continuing progress on raising retail standards.

In the **US**, our leading supplier status in ground beef remains critically important to help balance demand across the carcass. Australian exporters have also been

successful in building a significant niche market for our chilled beef in the US, and this can expand as an alternative premium market for Australian exporters as the US comes out of recession.

In **Europe** and **Russia**, gathering and sharing market information, building trade relationships, building awareness and understanding of Australia's products and systems, and again developing partnerships with exporters to leverage industry funds and assist market penetration are endorsed.

In the **Chinas** and **South-East Asia**, growing populations and affluence mean demand for high quality, fresh protein will only increase, and Australia is well placed to meet these needs. MLA's programs focusing on 'Brand Australia' – promoting our industry's systems via educational activities and promotions – together with partnership marketing programs with exporters, appear valuable and are endorsed by the Committee.

The **livestock export** market provides a crucial outlet for predominantly northern cattle as well as for locking in overseas markets for Australia through inter-dependent business relationships.

Given the strong presence of Australian beef and beef from Australian livestock in the Indonesian market in particular, we endorse joint programs aimed at increasing consumption through building consumer awareness of the nutritional benefits of beef, and appreciation of the variety of cuts and cooking styles. In addition, the Committee supports investment in improving beef retailing standards and hygiene at both traditional and modern markets, and supporting the development of local brands based on beef from Australian cattle.

We note the industry's consultative processes that take place each year in refining and evolving these programs to meet market needs and opportunities.



e) What is the appropriate level of spending on these programs?

The Committee finds that the \$5 levy is a modest but appropriate investment in the future of the industry.

At an average steer value of \$800 per head, the marketing component of the levy (\$3.66 for grass-fed and \$3.41 for grain-fed cattle) represents 0.45% and 0.43% of the sale value of the animal respectively. This compares with 1.2% for lamb and 1.05% for pork.

In considering the purchasing power of the levy today, \$5 in 2009 holds roughly the same value as the original \$3.50 levy in 1998. Looking forward, assuming an inflation rate of 2%, we would require a levy rate of \$5.63 in 2015 to maintain the value of the current \$5.

Notes on livestock prices



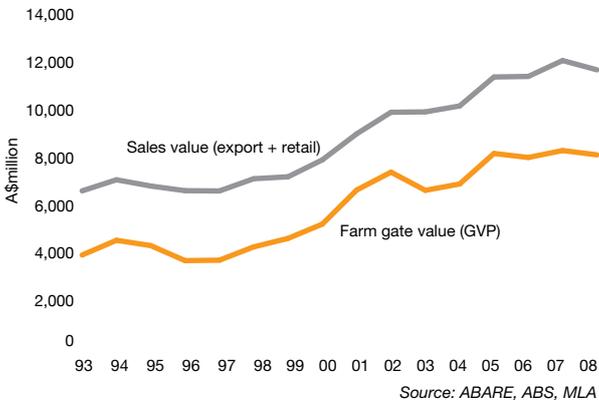
During the Committee's deliberations, we sought much information on livestock prices and the factors influencing them. In addition to the CIE assessment of impacts since 2005 (*Drivers of Livestock Prices*), the following information was presented to us that we felt useful to share with all levy payers.

Q. Why does MLA focus on growing consumer demand at retail rather than on increasing livestock prices?

A. MLA's programs are based on the premise that by driving overall industry revenues, through both export values and domestic consumer expenditures, the benefits of those revenues ultimately flow through to levy payers.

We found that this premise is largely supported by the industry data. The chart below shows that while there are periods when the two lines diverge, there is a correlation between farm gate values and overall industry revenues over time. This demonstrates that producers ultimately gain the benefits from increases in consumer demand.

Australian beef sales and farm gate values



Q. Why is fillet steak retailing at around \$40/kg when producers only receive \$3.50/kg?

A. Retailers balance prices to ensure they sell every cut of meat from the carcass. They do this by charging premiums for cuts that are in high demand and using those premiums to offset low prices necessary to move cuts in low demand. In spite of all the processing, packaging, distribution and retailing costs incurred throughout the supply chain to deliver a consumer ready product, over half of the carcass does not even recover its carcass value. As demonstrated in the table, only 9% of the carcass achieves premium prices at retail.

Cuts	Typical retail value	% of carcass
Loin cuts (fillet, cube roll, striploin)	\$26-\$48/kg	9%
Other cuts (rump, blade, knuckle, topside, silverside, chuck, brisket)	\$9-\$19/kg	37%
Trimming	\$3-\$4/kg	27%
Fat and bone	no value	27%

Source: MLA

Q. Why aren't livestock prices in Australia the same as in the US?

A. Great care should be taken in comparing Australian and US livestock prices as there are significant structural and cost differences that need to be taken into account. These include:

- Distance to market – Australia incurs high transport costs relative to the US, given that around two thirds of our production is exported while 90% of US production is sold in its home market.
- Smaller, leaner animals – Australia produces a greater proportion of grass-fed and short grain-fed beef than the US, incurring higher processing costs per kg of beef and less fat sold as meat. This is particularly true in our domestic market where nearly all beef is now sold as fully trimmed.
- Economies of scale in processing – Australian plants are generally smaller and less utilised than US plants.
- Differences in feed grains – while there are differences in the types of grain used (US predominantly corn, Australia predominantly barley, wheat and sorghum), feed grain prices have historically been lower in the US.
- Herd sizes – Australian herds are generally larger, helping offset some of the dis-economies of scale in other areas.

Q. Why do we see different cattle prices in different states and regions?

- A. Cattle prices are ultimately driven by:
- the nature of the livestock produced;
 - competition from the market for those cattle; and
 - the costs of processing and delivering that beef to the market.

Caution should be exercised in comparing livestock prices given the vastly different production environments across Australia. An industry supported study into these and other unique factors specifically impacting on WA livestock prices is underway with findings to be communicated to industry on completion.

Beef marketing funding requirements and performance goals



We recommend increased emphasis and funding for market access activities, boosting our efforts in emerging markets such as South-East Asia and Russia, and more aggressive promotion of the industry's environmental and animal welfare credentials, particularly in the domestic market. We believe that with ongoing review and realignment of MLA's priorities, as well as productivity gains, these funds should be sourced from within MLA's current program budgets.

However, overall program costs are forecast to increase by 2% per year over the next five years. But with forecast growth in cattle transactions, levy income at the current levy rate will reach \$55.2 million by 2014-15. This means that, provided transaction forecasts and inflation forecasts prove reasonable and productivity gains are achieved, increases in program costs should be covered.

Therefore, we conclude that the current marketing levy rates are appropriate to address the challenges and opportunities likely to be faced by the industry over the next five years. We are also mindful of the need for MLA to experience the sort of pressure producer and processor levy payers encounter as they strive to do more with less.

Performance goals

We believe that producer funds should only be invested in beef marketing programs if that investment can be shown to return real benefits to levy payers.

Independent expert analyses by Warwick Yates and Associates and by CIE have identified an annual return to producers of the \$1.50 increase is in the range of three to eight times the investment of the \$1.50 per head levy increase. We recommend that a minimum ongoing return target of three times for the full marketing investment should be set. This means the full \$3.66 marketing levy must produce a minimum of \$11 per head contribution to livestock prices in future performance reviews.

How do producers have a say?

Clearly, any proposal regarding the cattle transaction levy will require broad industry and levy payer support. As such, all cattle levy payers will have the opportunity to vote on the recommendation to maintain the cattle transaction levy at \$5 per head.

MLA members will be able to vote on a resolution regarding the cattle transaction levy at the 2009 MLA Annual General Meeting. In parallel to this vote, cattle transaction levy payers who are not members of MLA will have the opportunity to participate in a non-member poll.

Details of the 2009 Beef Levy Review, as well as the full report of the Beef Marketing Funding Committee and related documents, are available at www.mla.com.au/beeflevyreview

The Committee recommends:

1. That the current \$5 per head cattle transaction levy rate be retained
2. That a minimum return on investment to producers be set at three times the overall marketing levy as the performance yardstick in future reviews
3. That future reviews of the levy be undertaken as a result of industry need, triggered by the peak councils, and not according to a pre-determined timeframe



RED MEAT
We were meant to eat it

beef get into it

