MLA Red Meat Industry Forum,

Alice Springs.

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Information will drive red meat competition, productivity and growth.

According to statistics, more than a third of people in this audience directly own shares, and virtually everyone indirectly owns shares through their superannuation fund.

Despite our high level of share ownership, we rarely think about what it is that gives us the confidence to invest our hard-earned money in a listed company over which we have little control, we will probably never do business with, and that is run by people we are never likely to meet.

Government financial regulators have pondered this question for decades, because investor confidence is absolutely critical to the effective operation of the share market.

They have identified two main factors that underpin investor confidence in share markets.

These are firstly, the rules that specify listing, trading and company reporting requirements, and secondly, the market reporting system, which provides instantaneous and comprehensive share market information that is universally available to anyone, investor or not.

These two factors – market governance and transparency - are globally recognised as important features of efficiently operating markets, and this is not just confined to the Australian share market.

Most markets that operate effectively have these two features, be they for equities, agricultural commodities, minerals, water, government bonds, or even real estate.

The red meat sector here in Australia, and specifically livestock markets, is no different.

Farmers and processors who are participants in the red meat sector routinely make investment decisions, often involving business assets that have an economic life extending over decades.

They are more likely to decide to increase their investment in the industry if they have confidence in the information available to them about the market, and they trust that the rules that govern the market make it fair for all involved.

This investment will be crucial to the future competitiveness and growth of the sector, given the relatively high-cost business environment in which livestock producers and processors operate.

In the rest of my talk today, I will explain why I very strongly believe that the future growth and profitability of the red meat sector in Australia will be dependent on the investment confidence of sector participants, which will in turn be facilitated by the fairness and transparency of markets, and the quality of information flows up and down the value chain.

Maintenance of competition.

Competition is a critical factor that drives innovation and associated productivity growth, both of which will be essential to sustain future competitiveness.

In earlier times, most livestock transactions in Australia occurred via the saleyards, and various state governments' maintained market reporting systems that provided market participants with a good understanding of prevailing prices.

These market reporting systems were considered an important way to reduce the information imbalance between livestock sellers and buyers, and to discourage anti-competitive behaviour.

In more recent times, the industry has moved to a much greater reliance on direct sales, with the best estimate being that currently some 90% of slaughter cattle and 60% of prime lambs are sold direct, and bypass saleyards and their associated public price discovery.

This has occurred against a backdrop of continuing consolidation in the meat processing sector, as major processors expand to achieve greater scale efficiency.

Increased reliance on direct sales creates advantages for both livestock producers and processors.

Livestock producers can reduce marketing and transport costs, reduce their exposure to price risk, and gain a more accurate understanding of the processing performance of their livestock.

Processors can better manage plant throughput, more accurately target superior livestock, and develop stronger relationships both up and down the value chain.

However, in the absence of comprehensive market reports for these direct sales, there is obviously an increased risk that anti-competitive behaviour could be occurring, or that livestock farmers will make poor production and marketing decisions, meaning the entire market will operate less efficiently.

If anyone needs a reminder of the cost associated with producers receiving poor or incorrect market signals, I suggest they study the history of the Australian sheep industry post February 1991.

In overseas livestock markets including the USA and Europe, governments have implemented mandatory market reporting, as livestock producers have become increasingly concerned about a lack of transparent market information.

In the case of the USA, major meat processors are required to report slaughter numbers and prices on at least a daily basis, as well as provide information on by-products and forward market positions.

As many will be aware, we recently examined the operations of the cattle and beef market in Australia, specifically to consider competition issues.

While many of the livestock producers we spoke to or received submissions from expressed concerns about the lack of competition and transparency, we were not convinced that mandatory market reporting, such as occurs in the USA, should be recommended for the Australian cattle market.

The main reason for this was that, unlike the USA where the processing sector is highly concentrated, and most cattle are feedlot-finished under forward contract to a uniform weight, there is considerable variation in the type of cattle turned off in Australia, a less concentrated processing sector and less vertical integration.

This is due to our much greater reliance on export markets, and our different regional production systems. This complicates market reporting, and potentially makes any mandatory system costlier and less accurate – although I note that technology is greatly reducing such costs. Given the high cost nature of the sector, we were certainly aware of the need not to impose additional regulatory costs.

The ACCC was also aware that a voluntary system of reporting direct Over-the Hooks (OTH) price estimates and slaughter numbers was operating and managed by MLA, and that this system was likely to be more cost effective and better suited to industry needs than a government-designed system.

We did, however, recommend that improvements should be made to market reporting, in particular that actual OTH prices should be reported, and that MLA should better align reports to enable comparisons to be made between OTH and saleyard prices. We recognised that MLA could not achieve this on its own, and relied on information from the processors to improve the quality of market information.

I should note that MLA was undertaking a review of its market reporting systems while the ACCC study was underway, and subsequent improvements to the system have addressed the issues the ACCC raised and reportedly been generally well received by livestock producers.

It will not come as any surprise to those present, however, that the recent decision by some processors to temporarily stop providing even basic information such as weekly slaughter numbers raises very real concerns about the future transparency and competitiveness of the cattle industry.

I personally think this decision was short sighted, and could be detrimental to confidence along the entire value chain.

The reason given by some processors for not supplying this information, let alone the improvements in market reporting recommended by the ACCC, is that the resulting market reports have been inaccurate, and used by overseas customers to argue for lower prices.

If the real issue was the accuracy of weekly slaughter numbers reported by MLA, then it would not seem to be difficult to modify the system to prevent future inaccuracies. But it seems that the real issue is a desire by some processors to limit information flows to both livestock producers domestically and overseas customers, presumably to improve processor margins.

What these processors want the rest of the industry to believe is that their overseas customers will pay higher prices if they have less market information.

If this is correct, then it tells us that these processors are competing for market purely on price rather than on quality.

It also assumes that their international customers will be unable to source any market information via other avenues, which appears naïve given recent developments in digital information and telecommunications. It seems far better to provide overseas customers with reliable information, than have them confused by gossip and rumours.

Finally, if the logic is correct that restricting market information will convince customers to pay higher prices when the market is falling, then presumably these same processors will be agitating for increased market reporting next time the market is rising!

The decision to reduce, rather than improve market reporting has certainly come to the attention of the ACCC, and will be a focus of the review of progress on the ACCC Beef and cattle market study recommendations, that we will be conducting in the coming year.

Future industry productivity growth.

In my opinion, a more critical issue for the sector to consider is the critical role that information and data will play in achieving the productivity growth needed to remain competitive.

In a mature industry that does not have the ability to expand by using extra resources such as land, growth is most likely to occur via what economists refer to as “capital deepening” – that is, increased capital investment by existing businesses.

That can take the form of investment in additional fencing, watering points, improved genetics and pasture improvement by livestock farmers, or investments in plant upgrades and new technology by processors.

The confidence of industry participants will be a key factor that encourages this necessary investment. As noted previously, critically important factors in maintaining the necessary industry confidence are the transparency of market information, and the robustness of rules governing market behaviour.

Given the recent period of relatively high livestock prices, some complacency about the need for productivity growth might be understandable.

However, numerous reports produced by the Australian Meat Processors Corporation and MLA have highlighted that the red meat sector in Australia is a high cost sector in comparison with virtually all international competitors.

In recent times these high costs have been exacerbated by rapidly increasing energy costs, and labour costs remaining persistently high in Australia compared to overseas.

There is not much that can be done in the short-term to reduce these costs, which were highlighted as long ago as 1993 in a detailed comparison carried out by Booz, Allen and Hamilton.

The main ways in which the sector has remained competitive has been through productivity growth, and by developing world-leading integrity systems.

Improving productivity through the entire supply chain allows the industry to use less labour and energy, while at the same time increasing carcase weights, and improving the yield of high value cuts.

Improving industry integrity systems associated with food safety and biosecurity enables the sector to promote a critical point of difference between Australian livestock products, and those offered by our international competitors.

This has been the reason that Australia has maintained access to critical high-value markets such as Japan, Korea and the EU, and more recently has been able to secure good access to emerging markets such as China.

Information – be it farm level information about production systems and chemical use provided by producers to processors, or feedback information on carcase performance provided by processors to producers – will be absolutely critical in achieving future improved productivity through the value chain.

More objective carcase information, such as will be available when Dexa technology is deployed in processing plants, has the potential to lift both farm and processor productivity.

A comparison of the productivity performance of the beef and dairy sectors in Australia over the last 50 years provides a useful indicator of the gains that may be possible.

If we index Australian milk yield per dairy cow and average beef cattle slaughter weights at 100 in 1970, in 2016 the dairy index was at 220, while the beef index was only at 160, meaning the rate of dairy productivity growth has been double that occurring in the beef industry.

There are multiple reasons for this, but one is undoubtedly that dairy farmers have available objective milking data, which they can use in combination with comprehensive genetic information to select and breed superior cattle better suited to their farming system.

Objective carcase data has the potential to boost productivity in the beef industry to a similar extent, especially by enabling livestock producers to link genetic information and management decisions to objective carcase performance.

It also has the potential to ensure that the production and processing sectors can better align with market and consumer requirements, and maintain the premium prices that are currently achieved by Australian livestock products.

Ultimately, the propensity of the farm sector to make the necessary investments in farm improvements, genetics and technology will depend on the confidence they have in the way that livestock markets operate in Australia, and the quality and transparency of information on which they base their production and marketing decisions.

If the Australian livestock sector is to grow and continue to prosper in the highly competitive international market environment in which we operate, the availability of transparent and objective market and performance data will be critical.

Whether they are aware of it or not, those seeking to restrict market information flows and reduce the availability of objective performance data in Australian livestock industries are really attempting to consign the livestock industries to a no-growth future.

The choice before the sector is quite stark.

A stagnant future characterised by low productivity, mistrust and inadequate levels of investment, or a profitable and growing industry with efficient information flows that engender confidence and encourage the investment needed to remain competitive.

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