

STUDY ON THE IMPACT OF GOVERNMENT
ON INDUSTRY COMPETITIVENESS

Prepared for

MEAT AND LIVESTOCK AUSTRALIA

By

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FOREWORD

This research study, funded by Meat and Livestock Australia, breaks new ground in quantifying the level of government influenced costs and charges on the beef and sheepmeat industries of Australia, New Zealand and the United States. Having regard to the qualifications which must necessarily accompany a "first" research project of this kind, the overall findings are significant.

The US government at all levels is only lightly involved through cost and charges interventions in its beef and sheepmeat industries. In contrast, Australian and New Zealand governments intervene (negatively) much more – and thus damage the competitiveness of their industries. To make matters worse for Australia, the US government is much more generously involved in dispensing subsidies and assistance.

To date Australia's concern over international competitiveness has focussed on how US subsidisation and assistance to agriculture is unfair. This Study shows that in the crucial area of domestic economic efficiency/cost competitiveness Australian governments collectively (Commonwealth, State and Local) are unwittingly working against, rather than for, the beef and sheepmeat industries compared to the situation in the United States.

This is an important finding. This Study quantifies for the first time the long held feeling of the meat industries that the government "take" from the industry in Australia is excessive, and this retards our international competitiveness. In other words, the government "take" has a cost.

Strategies must be implemented by the Australian meat and livestock industries to "pull back" the level of government-influenced costs and charges in Australia to internationally competitive levels. Failure to halt, and reverse, the inexorable increase in these costs and charges must inevitably contribute to the long-term decline of Australia's industries.

The researchers wish to thank those organisations, companies and farmers in Australia and overseas who assisted with commercially confidential data, and for their insights and guidance on the issues addressed in this Study.

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EXECUTIVE SUMMARY

Meat and Livestock Australia (MLA) commissioned SG Heilbron Economic and Policy Consulting to undertake research on the impact of Government charges/costs and assistance/subsidies on the Australian meat industry's competitiveness particularly in comparison with the United States and New Zealand. This report represents the results of the research undertaken.

The research brought together the livestock, feedlot and processing sectors of the industry and this enabled analysis of data along the value chain. The research drew upon data sources at national, sub-national (State and Local) and international levels, and both public and private data. It has produced valuable new information for the industry on its competitiveness position that can be used to improve the prospects in all parts of the value chain.

The research goes beyond the traditional focus of the meat industry on areas such as inspection charges by encompassing a wide range of costs and charges that are influenced directly or indirectly by Government. This includes labour on-costs, utilities and fuel, meat-specific costs/charges (licenses, meat inspection charges and levies), and others (including environmental costs).

KEY FINDINGS

- Australian livestock and meat producers generally have *higher Government-influenced costs and charges* overall than their key international competitors, and *receive less assistance* from Government.
- To illustrate the charges/costs situation for livestock producers - an *Australian* mixed sheep-beef producer pays around *one-third* of their livestock revenue (excluding wool) and around *one-fifth* of their livestock revenue (including wool) in Government-influenced costs and charges. By contrast, the average *New Zealand* mixed sheep-beef farmer pays around *one-sixth* of their livestock revenue (excluding wool) and *one-tenth* of their livestock revenue (including wool) in such charges. *US sheep farmers would pay least of all*, around *one-eighth* of their livestock revenue (with little wool being produced).

- To illustrate the situation for feedlots - private data from a number of *large Australian commercial feedlots* indicated Government-influenced costs/charges account for 3.1 to 3.3 per cent of revenue. However data from a large *USA feedlot operator produced a far lower percentage* of just 2.1 per cent, indicating a significant advantage.
- For processors, the largest *Australian (non-service) works pay around 4 to 5 per cent* of their revenues in Government-influenced charges and costs. *Smaller works pay upwards of 7 per cent*. Whilst the percentages above seem small, two points must be remembered:
 1. Whilst these percentages as a proportion of total sales revenues may be small, they are *very large in absolute dollar terms*. The beef and lamb processing industries have revenues estimated at around \$A6.6 billion (*Australian Bureau of Statistics Consultancy Stats*), so even the low figure above of around 4 to 5 per cent of revenue implies *the payment of up to \$A330 million in these charges/costs*.
 2. *Relative to meat industry profitability*, the above percentages of sales are very significant. The *profit margin for the meat processing industry is only 2 per cent* (measured as the percentage of operating income available as operating profit in 1998-99 – *Australian Bureau of Statistics Consultancy Stats*).
- *US processors pay significantly less as a proportion of revenue* in Government-influenced charges/costs. Overall, the largest Australian processors pay over *twice* as much as US processors, and smaller Australian processors over *four* times as much as US processors. If Australian low cost processors were to experience the same level of government influenced costs and charges as their US counterparts it would mean *a saving of over \$A200 million in costs to the Australian industry*. If Australian high cost processors were to achieve US low cost levels it would mean *a saving of over \$A400 million*.
- Based on analysis of the major cost categories, the Australian *livestock sector* should focus its strategies in seeking reduction in Government-influenced costs/charges in the areas of *oncosts; other costs (mainly rates); and utilities and fuel*.
- For Australian *feedlots*, the major areas of disadvantage relative to the USA are in respect of *oncosts and meat-specific charges* (cattle and grain levies).

- The key challenge for the *Australian processing sector is to close the gap on the far lower proportion of costs/charges experienced by its United States competitors*. The Australian processor is clearly being handicapped with a government imposed competitive disadvantage. The meat industry needs to develop strategies – to make governments aware, and - to remove this cost handicap, across all categories of government imposed costs.
- On the assistance side, this report finds that *Australian producers and processors overall receive less assistance than their major competitor, the United States, and similarly low levels to New Zealand*. The USA is far less of a subsidiser of its sheep and beef industries than the EU, and it provides relatively little assistance to these products compared to others in agriculture.
- Nevertheless the USA heavily subsidises lamb production, and *Federal and State Governments provide a range of programs* available to livestock producers and processors. State assistance is provided through tax and other regulatory concessions, and business assistance programs.
- It appears that *the internationally accepted measures of government assistance do not adequately capture State and Local (or sub-national) government assistance*. In the United States (and of course in the EU and in many other countries) this is apparently large. In Australia's case it is also significant.
- The full extent of State and Local assistance remains unknown by even the major international organisations (the OECD and WTO) responsible for monitoring assistance. The current estimate is that *\$US2 billion out of the \$US54 billion in assistance to US agriculture comes from various States*, and some of this would be available to sheep and beef producers. These subsidies can affect downstream parts of the value chain too.
- Progress on resolving the sub-national government assistance measurement problem can clearly *best be progressed in a trade policy context through the Australian Government*. Pushing for action on this front by the established international trade research and policy analysis organisations.

STRATEGIC RECOMMENDATIONS

Basic Principles

1. The Australian meat and livestock industry (livestock, feedlotting and processing) must *give greater weight and attention in its dealings with Government* (Federal, State and Local) to reducing the adverse impact of Government-influenced costs and charges on its international competitiveness.
2. The industry should not seek to redress the fact that it pays more in cost/charges and receives less assistance by simply seeking more government assistance. The priority should be on improving the industry's efficiency and hence its international competitiveness. This should be achieved by *getting Government influenced cost/charges down so as to enhance efficiency* rather than retard it.

Focus on Key Charges/Costs Categories

3. A priority for the industry is to address the impact of oncosts. The major focus for this should be developing *a campaign aimed at State Governments that are responsible for excessive payroll tax and workers compensation costs.*
4. Another priority for the industry is to ensure that utilities and infrastructure costs reflect the need for efficiency in the industry. The industry should assess the extent to which it should *become involved in the price determination processes of Federal, State and Territory utility and infrastructure regulatory bodies to reduce those key input costs. This will require effort and persistence – but over a period cost-reducing results can be achieved.*
5. Regarding meat-specific costs/charges, and consistent with recommendation 2, the industry should *aim for meat inspection charges to reflect orthodox economic efficiency pricing principles – that is marginal cost pricing.* The present “full cost recovery” regime based on accounting principles should be terminated. Inspection charges could be reduced substantially as a result, potentially saving the industry at least around \$A15 million.

6. The industry should make *a strategic assessment as to whether it should seek to negotiate directly with Government to achieve recommendation 2 or whether it should seek the introduction of a Regulator-General into the inspection system* (in common with the situation in utility and infrastructure regulation). Current potential changes to the inspection system that might see AQIS inspection outsourced could affect the strategic choices to be made in this regard.
7. The industry should undertake a *review of State Government licensing charges* to assess whether they are being determined in accordance with economic principles that encourage efficiency.
8. Recognising the growing importance of environment driven policies the industry should *undertake more research into the area of comparing environmental charges and systems internationally* to deepen its understanding of the extent to which the Australian industry is being over-regulated or over-charged relative to its international competition.

Trade Policy

9. The meat and livestock industries should *bring a new emphasis into Australian trade policy on increasing the scope and accuracy of information on assistance provide by State and Local (or, in other words, sub-national) Governments internationally* to ensure that international trade negotiations to reduce subsidies can properly and accurately take such assistance into account. This potentially massive form of subsidy at sub-national government level has apparently not been a focus of trade policy officials to date. The Australian meat and livestock industry should urge the Commonwealth Government to ensure that organisations such as the OECD and the WTO have sufficient financial and research resources to accomplish this aim.

Further Initiatives

10. The industry should build upon the foundation of this research by *continuing to update and monitor regularly the government influenced charges/costs situation*. This should aim to deepen the analysis and discover how the situation has changed (has it improved/deteriorated?) over an appropriate period of time.

11. The industry should encourage *the improved collection of data of costs/charges by management of farms, feedlots and processors* which can be used to identify and track the various costs/charges, and hence feed in to the updating and monitoring process recommended above. This could be facilitated by purpose designed interactive electronic data information collection from industry stakeholders.