Submission to ACCC Grocery Inquiry

Market and Trading Options for Beef Producers

by

Australian Beef Association

A submission prepared in response to a request by ACCC.

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The objectives of the common agricultural policy shall be:
(b) to ensure a fair standard of living for the agricultural community, in particular by increasing the individual earnings of persons engaged in agriculture;
(d) to assure the availability of supplies;
(e) to ensure that supplies reach consumers at reasonable prices.

From: Article 39.1, The Treaty of Rome, Founding document of the EU

Duopsony:
A market condition wherein two rival buyers exert a controlling influence on numerous sellers.

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Introduction

Efficient, low-cost beef production requires producers to target specific markets segments. Each market segment has defined carcase parameters.

Higher priced market segments tend to have narrower weight and quality specifications.

Targeting higher value markets requires long-term planning. The producer must manage:

- the genetics
- the carcase weight at slaughter
- the fat cover at slaughter
- the age at slaughter
- calving, weaning and finishing time to match seasonal conditions and market cycles
- streamline the sale and transfer process to minimise loss of weight and carcase quality

It takes cow-calf operators a minimum of 3-5 years to produce a line of cattle for a specific market.

Targeting Markets

There is almost always a buyer for all classes of cattle - but at a price.

Professional producers target particular markets because they offer a higher unit price and it is usually more efficient to produce lines of cattle and direct them to specific market segments.

Cattle that miss a target specification can usually be sold to a secondary/discount market.

In some cases, it is possible to redirect young cattle to an alternative market that is not a discount market. This involves additional time and cost and an equally uncertain economic outcome.

Market Segments

The table beef markets for Australia and Japan usually pay the highest unit price for cattle. They also have higher costs of production. These higher prices usually apply to store/feeder cattle and to cattle for slaughter. They are not necessarily the most profitable for producers as costs of production and environmental factors can be over-riding factors.

The EU market pays a high unit prices but the costs and administration are substantial and Australia often fails to fill its 7000 tonne quota.

The manufacturing beef segment will accept all classes of cattle, at a price. Bulls and heavy stock usually attract the highest unit price because they offer the processor processing-efficiencies (greater yield per animal slaughtered).

Table Beef Markets

The table beef markets for Japan and Australia are almost completely separate market channels. They have different genetic requirements and separate production pathways. Best quality product for the Australian domestic market would be discounted in Japan.

Some cuts destined for Japan can be diverted to the Australian top-end food service industry. Diverting product is a decision made by processors/traders and has no bearing on returns to producers.

Producing for Japan

Feedlots servicing Japan pay a premium price for feeder cattle that have the potential to meet their market specifications, particularly the capacity to marble. These cattle are grain-fed from 100 to 300 days to achieve the Japanese specifications.

Cow-calf operators servicing Japan breed Angus feeder steers that enter feedlots at 450-kg liveweight.

If not sold to the feedlot, these cattle do not usually have adequate fat cover for the domestic slaughter market, even thought they may be in the weight range. They would require further feeding on grass or grain to achieve an adequate fat cover for the domestic market, but this would make them too heavy for a premium price.

They can always be sold for slaughter for manufacturing beef at about 70-80% of their price as feeder steers for Japan.

Producing for the Australian Market

Cow-calf operators producing for the Australian market would aim to have an animal with the potential to be slaughtered at 15-18 months of age with a live weight of 380-450 kg. These animals can be finished on grass or grain.

Angus cattle can be used for this market, but it is more efficient to use other breeds or crossbred animals that have higher growth rates and carcase yields. Crossbred cattle are discounted by the Japanese market chain.

Biology

Cow-calf operations produce a range of cattle products. They often identify their business by the premium animal they produce. For example a breeder producing feeder steer for Japan would produce the following range of animal products.

Targeted premium product (About 50% of sales)

- Feeder steers for Japan, 450 kg steers at 18 months of age

Natural by-product lines: (About 50% of sales)

- Empty cows (sold for manufacturing beef and/or mince for local consumption)
- Dry cows (sold for manufacturing beef and/or mince for local consumption)
- Empty heifers (sold as 2nd grade feeders/stores for fattening)
- Off specification steers, from premium line (sold as 2nd grade feeders/stores for fattening)
- Runts (sold as 3rd grade feeders/stores for fattening)
- Aged bulls (sold for manufacturing beef)

These classes of cattle are an essential “by-product” of the natural outcomes and variation inherent in biological systems. Most secondary production is sold to make beef for manufacture for domestic and export markets.

Cattle are a Perishable Product

Time and specifications

The age, weight and fat specification for premium markets are quite narrow. Under ideal conditions cattle will remain on spec for several weeks. In a uniform line of cattle there is natural variation. The line is ready for sale when the average/median animal is on spec. At that time the heaviest/fattest will be at the upper end of the specification and the lightest/leanest will be at the lower end. As time progresses, some cattle in the line will move off the spec and be discounted.

Time and stress

The moment cattle are moved from their growing environment, paddock or feed pen, they lose weight and they stress. Initial weight loss is gut contents but is quickly followed but loss of carcase weight. (Cattle are very sensitive. In a feedlot, when an animal is taken from its pen, walked 200m and weighed and returned to the pen it records no weight-gain for the day, despite consuming their normal ration.)

Animals moved to a holding paddock or stockyard stress. Stress damages meat quality. Cattle should be slaughtered as soon as possible following removal from their growing environment to minimise loss. Stress lowers body energy levels that affect meat pH, meat colour, tenderness and shelf life. The effects are incremental. Following prolonged or acute stress beef becomes unacceptable (dark cutting/high pH). Five per cent of domestic grade carcases are rejected because of dark cutting meat costing the industry more than $20 million per annum.

Producers pay the costs

The perishability of cattle puts the producer at a great disadvantage. Buyers know delays will devalue the cattle. Yarding cattle for an on-farm inspection takes time and degrades them. Repeated yarding for inspections, by different buyers, in an effort to generate competition or to attract a higher price substantially degrades the cattle.

When these cattle are processed the processor pays on the weight delivered and discounts the carcases for quality.

Either way, the loss due to stress or the lower price is at the cost of the producer.

Saleyards stress cattle and degrade meat quality. Cattle traded through saleyards are not eligible to be graded under the national MSA grading system because of the stress and consequent variable eating quality of the meat. Most domestic trade cattle in southern Australia are sold through the saleyards at an enormous cost to the industry.

Method of Cattle Sales

Cattle producers have several options:

Send direct to a processor (over the hooks)
Send to a saleyard for auction
Sell on-farm gate to a processor/lot-feeder/other farmer finisher

Send to processor

Producers can send cattle direct to a processor. In Queensland this is the main mode of business.

Producers contact the processor advising they have cattle for sale. Processors normally advise the producer there is a three-week delay till they can process the cattle. The producer then books a place in the queue for a specified number of cattle for delivery on a certain day. The week before the delivery day, the processor publishes a price grid. If the producer does not like the prices offered he can withdraw from the transaction. He can then apply for a new delivery date three weeks out and wait for the grid for that week. Queensland processors pay on price per kilo Hot Standard Carcase Weight (HSCW), the carcase weight after slaughter with discounts based on carcase weight ranges, dentition, fat cover and other parameters.

In Queensland mustering is a major logistical exercise. Mustering/yarding and holding costs are substantial. Once mustering teams including helicopters are engaged pastoralists have little choice other than to proceed through to sale or face significant cash and loss of weight and quality costs. Processors are fully aware of the vulnerability of producers in this situation.

In Victoria, most cattle are traded through saleyards. Victorian processors will buy cattle direct from producers. Some Victorian processors vascular flush - pump a proprietary solution into the vascular system of the animal immediately post slaughter. The solution adds 2% to the carcase weight and adds to the weight muscle sold from the carcase. These processors do not pay producers, who sell direct, on HSCW. They pay on a live weight estimate. Processors sell carcase beef and cuts on the flushed carcase weight but choose not to reveal the carcase weight to the producer. Vascular flushing is not permitted for beef destined for the US and Japan.

Send to saleyard for auction

Producers can send their cattle to saleyards where agents will sort them into market categories and auction them to the highest bidder.

It costs between 9-13%, of the gross value to sell animals at a local saleyard. This method of sale is widely used in Victoria where lots sizes are small.

Not accepting the auction price and taking the cattle home is not an economic option. The cost of returning the animals to the property plus the fixed costs of the auction and the additional cost of sending them to market again is most likely greater than the possible additional price that may be achieved at a later sale. Cattle are severely stressed by this process and lose significant weight and meat quality. The agency industry and municipal and private saleyard operators operate the saleyard system.

Selling at the farm gate

This is an option for producers who sell stores/feeders and cattle ready for slaughter. Buyers insist cattle are yarded for inspection and then the buyer will nominate the pick-up day and there will be a negotiation to establish the method to weigh and/or value the stock and the rules for discounts for off-spec animals.

Buyers know about the seasonal pressure on producers, the effects of stress and handling costs and dark cutting. All these factors are used in the negotiation by the processor. Buyers push for every cent to lower their buy price knowing the producer is losing value every moment slaughter is delayed.

A cattle buyer may be involved in 10 such transaction in a day and will use these strategies to lower the buy price every time.

Stock agents tend to defer to the wants of the buyer (processor), as they have to deal with them every day as opposed to the producer who they see two to three times a year.

Stock agents charge the vendor (producer) about 5% of the sale value for services and guaranteed payment. Elders and Landmark dominate the agency industry. Their single biggest customers are Coles and Woolworths.

Producers vs Merchants

Beef producers negotiate from a weak position every time:

- Vendors are always small compared to the buyers
- Producers trade infrequently as opposed to processors who trade many time a day
- Cattle are “perishable”. There is a limited window of on-spec time. Producer must sell when cattle reached the market specification
- Handling cattle for sale costs the producer time and weight-gain and carcase quality
- Producers face feed costs and seasonal pressures
- Selling direct to a processor puts the processor in control of weight determination, price and delivery terms, and discounts for quality
- Selling through saleyard concludes a transaction, but is a high cost and high risk option

Processors negotiate from a position or power every time:

- Processors are many times (1000) bigger than most producers
- Processors have access to the wider supply/demand picture
- Processors know the vendor must sell as his cattle are on spec
- Processors know the seasonal condition/outlook
- Processors control the time of delivery
- Processors know handling and delays will cost the vendor (producer) money

Summary

Preparing cattle for a specific market is a long-term project and can take up to five years.

When cattle achieve a premium market specification they only remain there a short time 1-10 days. Cattle “perish” quickly with time and handling.

The premium Australian and Japanese table beef markets are separate channels. There is little interchange of product at the producer level.

Alternative cattle markets are secondary or discount or distress-sale options, returning at least 20% less than table beef markets.

There are substantial costs for producers when cattle are committed for sale - selling direct, at the saleyard or at the farm gate

Producers have little negotiating power. Their only option is to withdraw from the sale.

Irrespective of price levels, buyers (processors) always have more negotiating power than sellers (producers).

Competition among cattle buyers alone is in insufficient to ensure producers can negotiate competitively with buyers. The true level of competition among buyers for stock for the domestic market is unknown

Processors pass the cost of poor handling/stress back to producers.

At the point of sale producers have little or no power to increase their returns by seeking alternative buyers.

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