INSTATE
PTY LTD

INTERNATIONAL
STRATEGIC
ANALYSIS TEAM

EXPORTING AUSTRALIAN PROCESSED FOODS

ARE WE COMPETITIVE?

INSTATE
PTY LTD

INTERNATIONAL
STRATEGIC
ANALYSIS TEAM

EXPORTING AUSTRALIAN PROCESSED FOODS

ARE WE COMPETITIVE?

INSTATE PTY LTD

ACN 003 933 604
7th floor
5-9 Harbour View Crescent
MILSONS POINT
NSW 2061
Tel: 02 9955 2711
Fax: 02 9955 2275
sydney@instate.com.au

Acknowledgements

This report is the result of a consultancy commissioned by Agriculture, Fisheries and Forestry — Australia (AFFA). It examines the export competitiveness and market development issues affecting manufacturers of processed foods.

The consultancy was funded by AFFA with contributions from the Victoria Department of State and Regional Development (DSRD) and Supermarket to Asia Ltd (STAL). Victoria and South Australia also contributed to the project by funding separate state-based studies.

The report was prepared by INSTATE Pty Ltd with inputs from many individuals in the company, but principally Ross Maddock, Denis Gastin and Rohit Pathak. INSTATE Pty Ltd accepts sole responsibility for the views and comments expressed herein.

The project was overseen by a Steering Committee chaired by Michael Wilson of AFFA. Members of the committee were Carol Bate (DSRD); Jim Kennedy (STAL); Graeme Thomson (Department of Foreign Affairs and Trade): David Morgan (DFAT); Andrew Mitchell (DFAT); Lyndel Jack (Austrade); Terry Spencer (Australian Government Analytical Laboratories); Bev Clarke (AFFA); Alan Edwards (AFFA); and Juliet Lautenbach (AFFA).

Significant contributions to the work of the consultancy have been made by Loyalty Research Pty Ltd, Ms Monica Richter and MS Management Service AG of St. Gallen, Switzerland.

The generous contribution of time and information from a wide range of processed food manufacturers is gratefully acknowledged.

ISBN 0 642 43253 8.

Foreword

Australia has a wealth of natural advantages, a clean environment and a strong, stable economy. We should be a significant exporter of processed food products, proudly branded Australian.

The Prime Minister's Supermarket to Asia (STA) Council reflects the Government's recognition of the industry's contribution to the national economy and regional development, and of its export potential.

Agriculture, Fisheries and Forestry — Australia (AFFA) maintains its strong commitment to food throughout the value chain, including processed food, and the States and Territories promote and support the industry. Other Commonwealth agencies such as the Department of Foreign Affairs and Trade and Austrade devote significant resources to food industries and, along with AFFA, work closely with food industry associations in developing policy.

AFFA commissioned INSTATE Pty Ltd to investigate the issues surrounding our international market share in processed food, with guidance and advice from key government agencies and STA.

The study brings together information from across the industry, revealing perceptions of the factors that affect companies' ability to export successfully. The consultants undertook an extensive survey of the processed food industry and over 100 face to face interviews, supplemented by desk research. They then shared their findings with local and international networks of food contacts to shed further light on the issues and refine their conclusions and recommendations, which are presented in this report.

Not surprisingly, the consultants found no single solution which will enhance Australia's export competitiveness. Instead, the study revealed a myriad of issues that affect each company differently. Issues internal to each business — such as funding capacity, skills and attitude to risk — were as important as external issues such as market access. The study identified some strong, innovative exporters and many companies that are optimistic about exporting and enthusiastic about industry growth and development. Notwithstanding the significant improvement in export performances of some firms in the industry, it also identified that a large number of companies simply do not have a deep and functional knowledge about the complex task of exporting.

I believe it is important that the findings about Australia's largest manufacturing sector be presented candidly where they can benefit industry and Government, and provide insight into our competitiveness.

I commend this report to you and look forward to the healthy debate it should stimulate. AFFA is refining its policy approach to the industry and would be pleased to hear any views on the matters raised. As the department with lead responsibility for the food industry, AFFA is committed to helping businesses achieve their export potential — taking a leadership position where necessary.

Michael J Taylor
SECRETARY
Agriculture, Fisheries and Forestry — Australia
17 February 2000

Table of Contents

EXECUTIVE SUMMARY

The food industry in Australia has great significance in terms of its contribution to the national economy, its crucial importance in regional development and its place in our history and culture.

The creation in 1996 of the Prime Minister's *Supermarket to Asia Council* was a signal to the industry that the government recognised its significance and its potential in markets to Australia's north. It also gave expression to the hypothesis that Australia ought to be able to increase exports of highly processed foods rapidly.

State governments recognise the significance of the processed food industry and promote and support it. Some make it a centrepiece of their economic development strategies.

However, while Australia's exports of *unprocessed* food have grown and individual food manufacturers are generally optimistic about export opportunities, the more experienced and globally-minded industry participants are not complacent about the real challenges of succeeding in export markets for *processed* foods.

In terms of growth and market share Australia is already lagging other exporters of processed foods. International Trade Centre statistics record Australia's processed food exports as having grown by just 1.8 per cent in the period 1994 to 1998, compared with 21 per cent for the United States, 9.9 per cent for Germany and 9.2 per cent for France.[1] Australia's own official figures show a more encouraging growth performance over the same period, at 5 per cent. Exports of unprocessed food, however, grew by 40 per cent.[2]

This study addresses a large number of questions relevant to the industry's export performance. The objective is to provide insights into:

- The factors which determine the propensity of Australia's processed food companies to be export-oriented; and
- The relative seriousness of various impediments to Australia's exports of processed foods.

This is a study of attitudes and opinions, concentrated on finding out what firms in the industry think are the factors which determine their ability to export, and what firms think are the impediments to an improved export performance and how they might be overcome.

Opinions and attitudes were collected in a mailed survey of 316 firms and during in-depth interviews with owners or senior managers of 103 food processing companies representing a spectrum of the industry: from state-of-the art to antiquated factories, from top-flight industry leaders of vision and ability to battlers with low prospects of survival.

1 International Trade Centre, UNCTAD/WTO, 1998 (based on over 100 reporting countries representing more than 90 per cent of world trade).
2 Department of Foreign Affairs and Trade (DFAT), *Composition of Trade Australia 1998*.

INSTATE began the study having completed a number of related studies over the previous ten years. Extensive desk research was carried out to give the subjective judgements supplied by firms in the survey and interviews a frame of reference. Conclusions were tested in a series of industry Focus Groups and through INSTATE's international network.

The information gathered during this process indicates the following areas are of prime concern in building the export capability of the industry.

Mixed outlook for exports — and the industry

The industry is dominated by a small number of large firms and foreign ownership exceeds 50 per cent of industry manufacturing capability. Many of the larger Australian-owned firms are controlled by primary producer cooperatives.

Generally speaking, the larger firms (and particularly the foreign-owned firms) are less committed to exporting at the higher end of the value chain than the industry as a whole. The main reason appears to be that the owners of the larger firms, including the foreign enterprises, see few opportunities for profitable investment in exporting highly processed food from Australia. A further explanation is the strategy of some foreign-owned companies to manufacture as close as possible to, or inside, the markets they supply. The owners of the smaller firms are more likely to be investing in high value product innovation and more likely to be seriously interested in expanding exports. But they lack the scale to sustain exports or make a significant contribution to the sector's overall export performance.

While most of the firms are optimistic about their own short-term export prospects, they are not complacent about the overall outlook for the industry. Some are pessimistic, believing that import penetration could increase. Some industry leaders fear that the food processing industry, like manufacturing in general, may be under serious threat from foreign competitors, partly because it receives too little effective support and recognition from the government and the community.

Tough competition in foreign markets

The firms perceive that they face very tough competition in foreign markets.

Protection and export subsidies are seen to be substantial impediments. But domestic impediments — firms' own operational inadequacies, lack of effective government support and residual inefficiencies in the Australian economy — are generally seen to be more serious obstacles to exporting.

Many raw materials too expensive

Almost half the firms in the sample identified the high cost of raw materials as a serious impediment to exporting. In a few cases, Australian raw materials confer a distinct comparative advantage on Australian processors. In most cases, Australian processors pay the same price (world price) for their raw material inputs as their competitors. In some cases they pay more. Foreign governments focus export subsidies in sectors and markets where competitor countries, such as Australia, compete strongly on price terms.

The main reasons for uncompetitiveness in raw materials are lack of scale at primary producer level and relatively less developed vertical integration with the food processors, compared with some competitor countries. Benchmarking studies suggest that competitiveness of primary producers is also hampered by the relatively high cost of some agricultural inputs — for example, labour and feed. Regulatory structures, in some cases, impede the flow of raw materials to processors and increase the cost of some raw materials.

Little competitiveness gained through value adding

The successful food processing firms know that it is **total** competitiveness along the value chain which determines whether they can export successfully. Total competitiveness depends on how creatively and cost-effectively firms augment raw materials, not just in processing and packaging, but also in quality, uniqueness of product, service, market positioning, channel development, promotion and brand development and support.

A substantial majority of the firms interviewed agreed that very little cost competitiveness is gained during the intermediate stages of the value chain in Australia — in manufacturing, packaging, financing, freight, and international marketing.

Labour productivity and investment in innovation too low

Benchmarking shows that labour productivity in some segments of the industry lags what competitors achieve in the United States, Europe and some other competitor countries. Investment in R&D is declining.

The more globally-minded firms see the link between these trends and the Australian industry's frequent inability to meet world benchmarks in value-adding. They acknowledge that, too often, the Australian product is not price-competitive, not highly differentiated and not often enough successful in capturing the 'value of values'; for example by promoting products, where appropriate, as 'eco-efficient', clean or safe.

The industry generally agrees with the proposition that, as things stand, the more value is added in Australia the less cost competitive in foreign markets the final product is likely to become. It also understands that differentiation and total competitiveness come from investment in R&D and other forms of innovation and that Australian firms under-invest in these things.

Corporate capabilities below world benchmarks

On balance, firms also agree that management, technical and export skills in the industry are often not world-competitive and limit their export ability.

There is little evidence of genuinely innovative approaches undertaken by firms for export market development. Fewer than might be expected have a conscious focus on value chain or demand chain management issues for export markets.

Ambivalence towards government efforts to support exports

The firms interviewed or participating in the Focus Groups had limited knowledge and understanding of many federal government policies and programs designed to support exporters, including those in processed foods. At interview, the firms generally expressed greater familiarity and higher levels of satisfaction with the services provided by state governments.

Companies are not convinced that the government is fighting hard enough to reduce foreign protection and export subsidies. Most are fatalistic, believing that things are not likely to get much better, especially in the short and medium term.

They have an equivocal attitude to the services provided by Austrade and AQIS. The Austrade fee structure is considered inappropriate and AQIS is seen to be too concerned with its role as 'policeman' and not sufficiently interested in helping exporters. This suggests at least a failure of communication on the part of the two agencies.

Firms are exporting through 'accumulators'

The study revealed that many firms are not *directly* involved in exporting. Rather, they are selling their product to trading companies or other intermediaries — 'accumulators'. Intermediaries often feel that the role they play is under-valued and misunderstood — by the industry as well as the public sector. Some accumulators are export agents working for a commission. Many act as principals, accepting the costs and risks of exporting in return for a margin which the manufacturer surrenders to them. Generally, firms exporting through accumulators had little functional knowledge of foreign markets and even less of the practicalities of exporting.

Conclusion

In the light of these findings, there should be no complacency about the prospects of substantially increasing, or indeed maintaining, Australia's exports of highly processed foods. There is substantial work to be done, at both government and industry levels.

The survey showed no clear pattern of concern within the industry which would indicate simple policy solutions. However, the interviews brought issues into sharper relief and led to the principal conclusion that what is required is coordinated policy leadership across a broader spectrum of the food industry. These issues fall into three key areas:

- Competitiveness up and down the value chain;
- Corporate capability building; and
- Access to foreign markets and export market development.

Governments and the community have high expectations of the food sector and the contribution it can make to the national economy through exports. The study confirmed serious constraints on the sector's ability to perform to expectations.

For much of the sector, raw materials confer little competitive advantage. Down the chain — in processing, packaging, branding and marketing — Australian firms do not often perform well against world benchmarks. Innovation is the key to improved performance as products with 'intrinsic value' do not rely excessively on price for their marketability. However, firms feel that they under-invest in all forms of innovation.

Overall, while there is a small cadre of very talented proprietors and managers with global business experience and perspectives, firms acknowledge weaknesses in their capabilities to initiate and sustain exporting. They also perceive weaknesses in public sector efforts to assist them with exporting and feel that Australia could more energetically and effectively fight foreign protection and export subsidies.

The Supermarket to Asia Council has done a great deal to focus attention on the practicalities of exporting processed food and has highlighted many of the broader issues which must be resolved if the industry is to perform to expectations. However, the problems identified by the study require a wider focus than can be addressed within the current Supermarket to Asia charter. It is now time to extend its charter to address these issues in a broader industry and market context.

An appropriately structured and resourced Prime Minister's Food Industry Council, building on the current Supermarket to Asia Council, would achieve effective coordination of the efforts of the various state and federal agencies which have the power to influence the industry's performance throughout the whole food chain. It would provide the easiest mechanism to address the multiple domestic and export issues identified in the study, and would build a wider constituency for the organisation, enhance its authority and reinforce a global rather than a regional focus.

An Immediate Action Agenda

Not everything can be done at once. Indeed, some of the issues are at the heart of industry culture. Fundamental change will be achieved only over time. The responses that would assist in making the earliest possible start form the Action Agenda outlined below:

Action Agenda

1. Create an appropriate sense of urgency and a better understanding of the totality of the challenge by forming the Prime Minister's Food Industry Council.
2. Carry out systematic benchmarking of Australian food industry sub-sectors, to identify where competitiveness lags international standards and where improvements must be made.
3. Commission a study of better ways to assist the industry more effectively to draw down resources from the national innovation system.
4. Through the Food Industry Council, set priorities and orient programs to improve corporate capabilities and the contribution of food industry 'accumulators' to the facilitation of exports.

1: THE STUDY

Agriculture, Fisheries and Forestry — Australia (AFFA) commissioned the *Australian Highly Processed Food Export Competitiveness and Market Development Study* (the study). Other commonwealth and state public sector agencies supported the study. The Project Steering Committee comprised:

- AFFA (Chair);
- The Department of State and Regional Development, Victoria (DSRD);
- Supermarket to Asia Ltd (STAL);
- Australian Government Analytical Laboratories (AGAL);
- Department of Foreign Affairs and Trade (DFAT); and
- Austrade.

Purpose of the Study

The main purpose of the study was to determine the factors which affect the performance of Australia's processed food industry and its exports. A second goal was to collect and collate information about the barriers and impediments to exports which firms in the industry consider to be significant. These included tariff and non-tariff barriers, export subsidies provided to foreign competitors by their governments, domestic constraints on competitiveness, including inefficiencies in the firms and their operating environment and problems with export market development and supply chain management.

This was a study of the **attitudes** and **opinions** of the firms in the industry. In that sense it presents a subjective reality. In conjunction with a survey and interviews, extensive desk research was carried out. The purpose of the desk research was to provide a context for the subjective information generated from the survey and the interviews.

The findings about the industry's performance and the impediments to its exports were used to formulate a set of recommendations for policies and programs for public sector agencies and the industry to strengthen the firms, overcome the barriers and increase exports.

The study was divided into two parts:

- The National Study; and
- Case studies at the State level, commissioned by the Victorian and South Australian Governments.

Methodology

Concepts, hypothesis and desk research

The methodology was developed from the study brief and several iterations with the Project Steering Committee.

Once there was agreement about the scope of the study and the main questions to be investigated, a research hypothesis was developed. The purpose of the hypothesis was to help shape the component parts of the study and to provide a benchmark against which new ideas and insights generated in the course of the study could be measured.

At the completion of the Victorian Case Study, a revised version of the research hypothesis was produced, taking into account the findings of the study to that point and helping to reshape the remainder of the work.

At the commencement of the study, a program of desk research was commenced. It continued throughout the study. The desk research was scoped to cover the questions in the study brief and other questions and issues that arose during the course of the study. A bibliography is included at Appendix 1 of this Report.

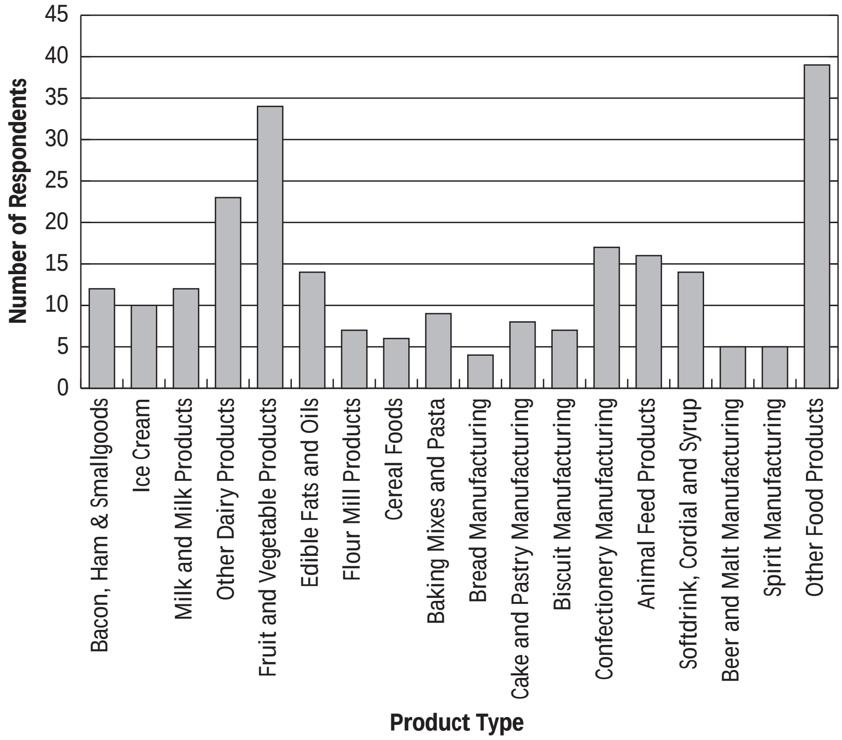
Selection of the firms to be surveyed

The sample included firms from the following product categories:

Table 1: ANZSIC Codes and Product Categories

ANZSIC Code	*Product Category*
2113	Bacon, Ham and Smallgoods Manufacturing
2122	Ice Cream Manufacturing
2129	Dairy Product Manufacturing nec
2130	Fruit and Vegetable Processing
2140	Oil and Fat Manufacturing
2151	Flour Mill Product Manufacturing
2152	Cereal Food and Baking Mix
2161	Bread Manufacturing
2162	Cake and Pastry Manufacturing
2163	Biscuit Manufacturing
2172	Confectionery Manufacturing
2174	Prepared Animal and Bird Feed Manufacturing
2179	Food Manufacturing nec
2181	Soft Drink, Cordial and Syrup Manufacturing
2182	Beer and Malt Manufacturing
2184	Spirit Manufacturing

Figure 1: Number of Respondents for Each Product Type



The objective was to achieve a total of at least 150 valid responses. The sample was also constructed to reflect as closely as possible the size of the industry in each of the states, with a reasonable representation of small, medium and large firms and a good balance between exporters and non-exporters. Care was taken to ensure a balanced product coverage in the survey.

It was estimated that the response rate might be as high as 60 per cent and, therefore, that the minimum number of firms to which the questionnaire should be sent was 250. It was later decided to increase the mailing list to at least 300 firms.

State coverage was determined on the basis of each state's share of the industry gross product (see Table 2).

The task of compiling the mailing list was commenced by consulting and reviewing the following sources:

- AFFA contacts database;
- *Kompass Agribusiness, Food & Beverages Export Directory 1997*;
- *Australian Grocery Industry Marketing Guide* and the *Foodweek Industry Yearbook and Directory*;

- State government agencies;
- Australian Food and Grocery Council (AFGC) membership list; and
- Yellow Pages directory.

All the companies on the draft mailing list were telephoned to verify contact details. After several iterations, a final mailing list of 316 companies was agreed.

Table 2: Breakdown of firms by State/Territory, based on proportion of Food Manufacturing Industry Gross Product

	State share of industry gross product	*Numbers to be surveyed, by State*
VIC	32%	99
NSW	26%	81
QLD	20%	57
SA	10%	32
WA	7%	23
TAS	3%	21
NT	2%	3
Total	100%	316

Source: Australian Bureau of Statistics (ABS), *Manufacturing Industry Australia*, Catalogue No. 8221.0 and No. 8221.2,1996–97.

Developing and testing the survey instrument

The aim was to produce a questionnaire that included the right questions and would produce substantial and meaningful results. It was designed around the questions in the study brief and informed by previous experience with similar surveys.[3]

Several drafts of the questionnaire were produced and input and suggestions for refinement were received from the Project Steering Committee and others.

Particular effort was made to keep the questionnaire as short as possible, so as to increase the likelihood that firms, particularly non-exporters, would complete and return it.

The penultimate draft was tested on four industry respondents, three of whom were exporters. Their feedback confirmed that the questionnaire could be completed in a maximum of 30 minutes.

3 The administration of the questionnaire and the basic data collation was carried out by professional market research agency, Loyalty Research Pty Ltd, under INSTATE's direction.

Clearing the survey instrument through the Australian Bureau of Statistics

All Commonwealth Government surveys with more than 50 recipients must be cleared through the Australian Bureau of Statistics Statistical Clearing House (ABS SCH), to manage the burden placed on small business and to ensure quality control.

The questionnaire and associated documentation were sent to the ABS SCH on 11 June. On 25 June the ABS SCH gave clearance, without requiring any substantial alteration to the questionnaire.

Mailing the questionnaire

The then Minister for Agriculture, Fisheries and Forestry, the Hon Mark Vaile MP, provided a covering letter, explaining the purpose of the study and seeking the co-operation of recipients.

The mail-out was completed on 29 June. Reminders were sent on 7 July. Firms that were slow in responding were telephoned and offered assistance in completing the questionnaire. By 25 July, a total of 157 valid responses had been received.

Analysis of the survey data

The analysis of the survey data was carried out in three separate stages:

- The Victorian data (July 1999)
- The national data (September 1999)
- The South Australian data (November 1999).

In the case of the Victorian and South Australian data, separate analytical reports were compiled, setting out the main findings. A separate report to the Steering Committee also contained the detailed analysis, at the national level, of all data obtained through the survey.

In-depth interviews

The study brief required a large number of face-to-face interviews with CEOs or senior managers of firms. The purpose of the interviews was to augment the information, analysis and findings generated from the mailed survey.

An interview instrument was developed to give structure and consistency to the interviews. The structure and content of the interview instrument was determined by the study brief, the research hypothesis and the analysis and findings of the information produced by the mailed survey.

In consultation with the Project Steering Committee, it was decided to interview 30 companies in Victoria and a further 40 in other states. The number of interviews was increased when the South Australian Case Study was added to the study brief. In the event, a total of 103 companies were interviewed. On average, the interviews took between one and one and a half hours.

The interviews were conducted by INSTATE directors. Members of AFFA took part in most of the interviews in Victoria and several of the interviews in South Australia and Queensland.

The interviews in Victoria were completed in August 1999. The interviews in the other states were conducted in October and November 1999.

After the interviews in Victoria were completed and the information from them compiled and analysed, a draft Victorian Case Study Report was prepared and reviewed by the Project Steering Committee. After several iterations, the Victorian Case Study Final Report was completed on 17 September.

When the interviews in South Australia were completed and the information from them compiled and analysed, an interim South Australian Case Study Report was prepared and submitted to AFFA and the Government of South Australia.

Table 3: Interviews by State/Territory

State	*Number of interviews*
Victoria	32
South Australia	30
New South Wales	19
Queensland	11
Western Australia	6
Tasmania	4
Northern Territory	1
Total	103

Focus Groups and international input

After the interviews had been completed, drafts of the National Report and the South Australian Case Study were compiled. In order to test the findings and recommendations of these Reports, Focus Groups were convened:

7 December	Sydney
8 December	Shepparton
9 December	Adelaide

In each case, the Focus Groups were attended by industry representatives as well as members of the Project Steering Committee and relevant state government agencies. Focus Group participation was limited to ensure discussion remained manageable. Other than the Steering Committee members, representatives from nineteen organisations, including ten companies, attended the three sessions.

The Project Steering Committee produced an issues paper for use at the Focus Groups. The purpose of the issues paper was to provide a structure for the discussions and to ensure consistency.

At intervals during the course of the study, and in a concerted manner during the final stages of the study, the draft findings and recommendations were referred to foreign agrifood practitioners or analysts for comments and suggestions. The aim was to ensure, where appropriate, that the themes and overall conclusions made sense in a global as well as an Australian context.

These international agrifood practitioners and analysts included:

- An agribusiness consultancy based in the UK;
- An international business consultancy based in Switzerland;
- The CEO of one of Taiwan's largest food conglomerates;
- Senior managers from two of Japan's larger food companies and one of the largest retail firms; and
- One of the largest catalogue marketing firms in Japan.

Preparation of Final Reports

Taking into account the discussions at the Focus Groups, the National and South Australian Reports were revised. Further desk research was carried out to fill gaps in the information and to give a clearer context to some of the key issues; for example, the international competitiveness of the industry and the role of innovation.

It should be noted that, although the opinions expressed by firms accessed to inform the study were many and various, a significant number of the interviewees, including a substantial proportion of those who were exporters, had limited knowledge and understanding of the broader issues and even the practicalities beyond their particular business, products and markets.

Nevertheless, it was possible to give shape to the outputs of the survey and the interviews and to find common themes. This was partly because of the prior knowledge and experience which INSTATE and members of the Project Steering Committee brought to the study. The desk research was also important in this regard.

2: THE ISSUES

The findings presented in sub-sections 2.2 to 2.4 are derived from the analysis of the survey data, the interviews, Focus Group discussions and international inputs. Footnotes and other annotations indicate where the analysis has been informed by desk research.

2.1 PROCESSED FOODS IN AUSTRALIA

Major role in the Australian economy

Food processing is Australia's largest manufacturing industry. It is also seen to have considerable potential for increased growth, mainly through exports.

In 1997/98, the industry[4] employed 167,774 people and had a turnover of $46.6 billion.[5] Processed food industry output constituted 18.8 per cent of total manufacturing sector Industry Value Added.

Between 1991/92 and 1997/98 the processed food industry's rate of growth (36 per cent) was greater than for manufacturing as a whole (27 per cent).[6] By contrast, growth in manufacturing in the 1980s as a whole was substantially greater than the growth in food processing.

Industry structure

Australia produces a wide range of processed food. In 1997/98, meat processing was the largest contributor to both turnover (21 per cent) and employment (30 per cent). The categories which have experienced the fastest growth in recent years are flour milling and fruit and vegetable processing.[7]

Large firms dominate the industry and at least 50 per cent of food manufacturing capacity is foreign-owned. In 1997/98, Australia's 20 largest food manufacturing companies accounted for nearly half total industry turnover.[8] Of the top 20 firms, only seven are wholly Australian-owned, nine are wholly foreign-owned or controlled and four are a mixture of local and foreign equity (see Figure 2).[9] Three of the seven Australian-owned firms in the top 20 are farmer-owned co-operatives.[10]

---

4 The figures in Section 2.1 include the wine and seafood sectors which are otherwise excluded from the study brief.
5 Australian Bureau of Statistics (ABS), *Manufacturing Industry Australia*, Catalogue No. 8221.0.
6 *ibid.*
7 Australian Food and Grocery Council, *Australian Food*, Agrifood Media Pty Ltd, 1999.
8 *ibid.*
9 INSTATE Pty Ltd, based on data from a variety of sources, including the Australian Food and Grocery Council and the Bureau of Industry Economics.
10 *ibid.*

Exports under-perform

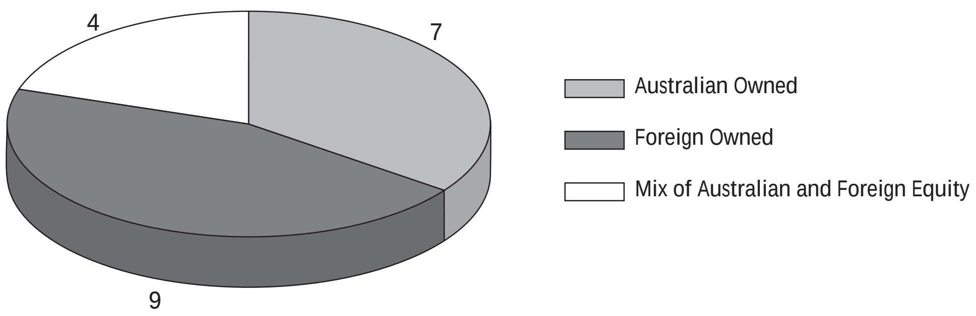
Between 1985 and 1996, world trade in agriculture and food more than doubled, reaching US$464 billion.[11]

Processed foods constitute the fastest-growing component of the world's agrifood trade. World trade in processed food products is growing at twice the rate of trade in primary products[12] and will constitute about 75 per cent of global agricultural trade in the year 2000, compared to 50 per cent in 1985.[13]

By contrast, Australia's processed food exports have grown much more slowly than unprocessed exports. Official statistics compiled by the Department of Foreign Affairs and Trade (DFAT), show that Australia's processed food exports increased from $9,073 million in 1994 to a $9,538 million in 1998 — representing growth of just 5.1 per cent over the period. Unprocessed food exports over the same period increased almost 40 per cent, from $5,067 million to $7,083 million.[14]

Australia's comparatively poor export performance in processed foods is also evident from statistics for global trade from the International Trade Centre (UNCTAD/WTO). While the definitions for processed foods differ slightly between the ITC and the DFAT series, the figures from both organisations nonetheless permit a useful international comparison and show Australia lagging behind the major exporters of processed food, in terms of both growth and market share.

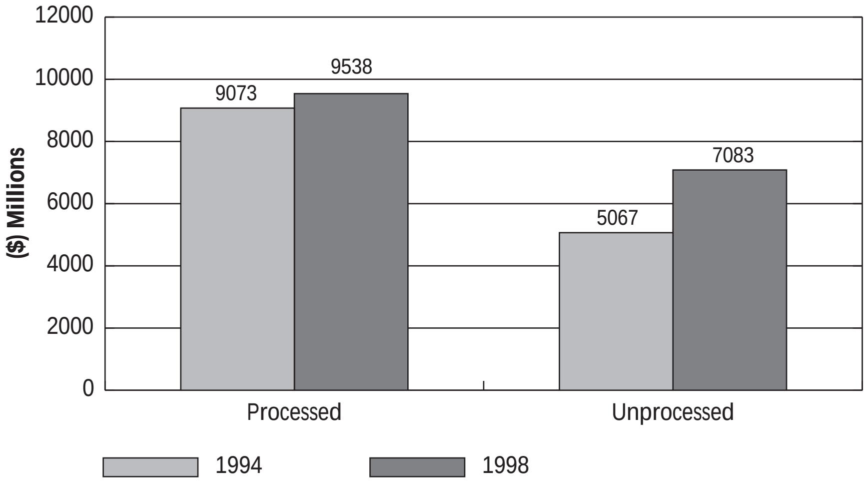
Figure 2: Ownership of Australia's top 20 Food Manufactures



11 Agriculture & Agri-Food Canada, *Canada's International Business Strategy 1999–2000*, June 1999.
12 Viatte, G., *The Changing Role of the Food Industry: Greater Prosperity Through Global Markets*, Agriculture, Food and Fisheries, OECD, Paris, October 1997; and Henderson, D. R., Handy, C. R. and Neff, S. A., *Globalization of the Processed Foods Market*, Agricultural Economic Report No. 742, Consumer Economics Division, Economic Research Service, US Department of Agriculture, September 1996.
13 Charlebois, P. and Schimdhuber, J., "Agricultural Trends and Issues to 2001", *The OECD Observer*, No. 205, April/May 1997.
14 Department of Foreign Affairs and Trade (DFAT), *Composition of Trade Australia, 1998*.

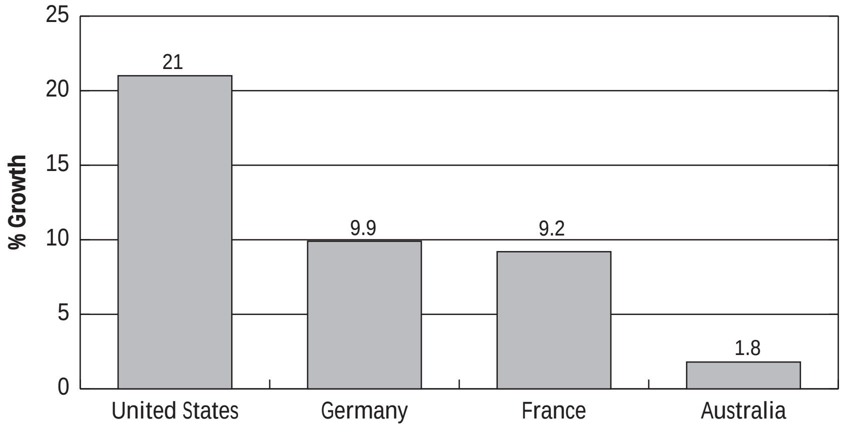
Between 1994 and 1998, world exports of processed food grew 7.9 per cent. The United States' processed food exports grew by 21 per cent, Germany's by 9.9 per cent and France's by 9.2 per cent. Australia's exports, by this measure, grew only 1.8 per cent. This saw Australia's global market share decrease from 3 per cent to 2.8 per cent.[15]

Figure 3: Comparison of Australia's Processed and Unprocessed Food Exports, 1994–98



Source: Department of Foreign Affairs and Trade, 1998.

Figure 4: Growth in Processed Food Exports, 1994–98



Source: UNCTAD/WTO, 1998

15 International Trade Centre UNCTAD/WTO, 1998 (based on over 100 reporting countries representing more than 90 per cent of world trade).

Australia did best in beverages and processed dairy products. Between 1994 and 1998, exports of beverages, mainly wine, increased by 85 per cent and Australia's share in world beverage exports increased from 1.3 to 2 per cent. Dairy exports increased by 30 per cent and Australia's share of world dairy exports increased from 4.2 to 5 per cent.

Australia did worst in sugar and confectionery and horticulture. Between 1994 and 1998, exports of sugar and confectionery decreased by 23 per cent and Australia's share of world trade in these products decreased from 6.4 to 4.9 per cent. Horticultural exports decreased by 22 per cent and Australia's share of world horticultural trade decreased from 0.8 to 0.6 per cent.[16]

Australia's low profile in value-added food markets internationally was commented on extensively by the international experts accessed in the course of this study. The comment was frequently made that Australia has a major asset in the willingness of international consumers to expect quality, natural and 'safe' foods from Australia. Surprise was expressed that, with the notable exception of wine, Australian foods and beverages are not more aggressively exploiting this positive pre-disposition of international consumers.

16 *ibid.*

2.2 EXPORT ORIENTATION

A principal aim of the study is to examine the factors which determine the propensity of Australia's highly processed food companies to be export-oriented.[17]

The survey was a starting point in this analysis. A second starting point was the desk research.

The survey was designed to enable a search for correlations between the export orientation of the firms and a range of variables, including:

- Location of the factories;
- Size of enterprises;
- Capacity utilisation;
- Ownership;
- Investment in R&D; and
- Perceptions of the significance of domestic and foreign impediments to exporting.

The interviews and Focus Groups allowed for in-depth discussion of the main issues, including attitudinal factors which the survey could not adequately assess.

Export profile of respondents

Of the 157 firms which completed and returned the survey questionnaire, 80 per cent identified themselves as exporters. The profile of the respondents is at Figure 5.

Of these, 40 per cent identified themselves as established exporters and a further 20 per cent said they were exporting with some difficulty. Only 10 per cent earn more than 75 per cent of sales from export and 59 per cent earn less than 10 per cent of sales from export.

Of the 103 firms interviewed, less than 20 per cent were more dependent on exports than domestic sales. At interview, it became apparent that one third of the firms might be described as opportunistic exporters, in that exporting did not seem to be central to any business plan, explicit or implicit.

None of the firms interviewed was 'born global'. Even the few very highly export oriented firms were established primarily to capture domestic market opportunities.

The characteristics of export oriented firms

Analysis of the survey data suggests that Australian-owned firms, firms based in South Australia and Queensland, and firms with above average capacity utilisation are most likely to be highly export oriented.

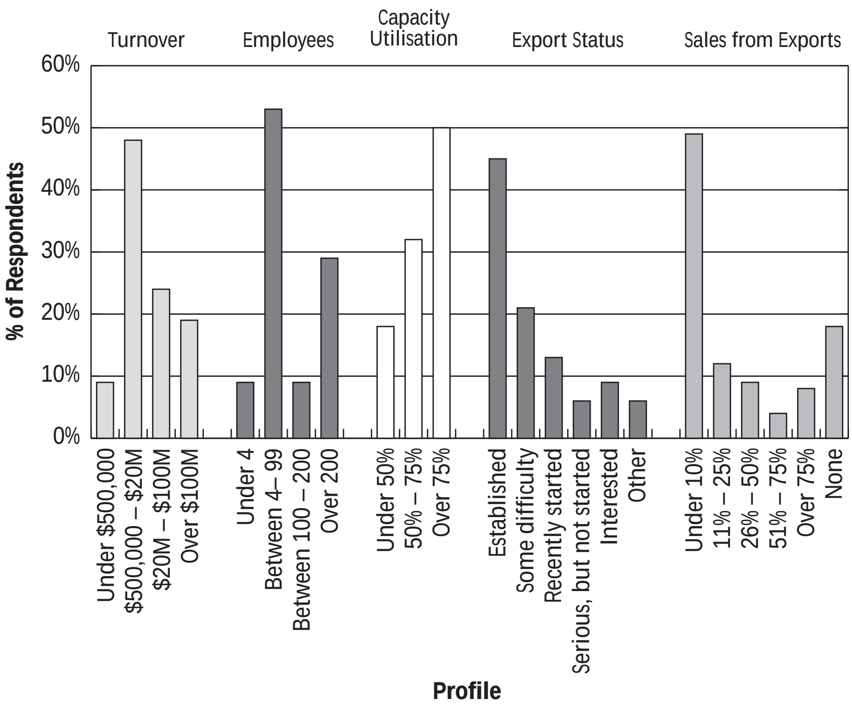
17 In this study, the term 'export orientation' refers to the percentage of a firm's total sales derived from exports.

However, at interviews in South Australia many firms described sales to other states as 'exports'. This tendency has been observed in earlier studies of firms in South Australia.[18] If firms which view interstate sales as exports were excluded it is likely that firms in South Australia (and perhaps Queensland) would be no more export-oriented than the industry as a whole.

A survey-based study undertaken for the Rural Industries Research and Development Corporation (RIRDC) suggests that the explanation as to why some processed foods are more successful in export markets than others might be as simple as the level of commitment of the owners to succeed at exporting.[19]

The desk research and the interviews confirm that attitudes and commitment are important. However, it found there is a range of other, more tangible determinants of international competitiveness of food processing enterprises.

Figure 5: Profile of Respondents



18 INSTATE unpublished work.

19 Philp N., *Why Some Firms Successfully Export Processed Food and Beverages*, Rural Industries Research and Development Corporation, Research Paper 97/33, 1997.

2.3 COMPETITIVENESS

International competitiveness

There are two principal determinants of the international competitiveness of the processed food sector:

- At the front of the value chain, the cost, availability and reliability of raw materials delivered to the processors;
- Along the value chain, the relative efficiency with which value is added — in financing, manufacturing, packaging, branding, marketing and distribution.

Except in the dairy industry and, to a lesser extent, some meat and grains, the raw materials used by Australian food processors don't generally confer any appreciable competitive advantage. Even when foreign competitors are forced to use more expensive raw materials, their governments frequently help them to overcome this disadvantage by providing on-farm intervention and export subsidies.

As companies agreed that competitiveness does not generally improve along the value chain, it follows that raw material input costs are a primary determinant of export potential. The effect of the cost of raw materials on final competitiveness of the processed product can be summarised as follows:

- Raw materials available below world parity prices provide Australian processors with the opportunity to compete in price sensitive markets;[20]
- Where raw materials enter the factory at, or near, world parity price, innovative product development, marketing and a sound understanding of consumer expectations would be essential to compete in value sensitive markets;[21]
- Where raw material costs are considerably higher than in competitor countries, it will be extremely difficult, if not impossible, for processors to develop products for sale in any export market.

The competitiveness of raw material inputs

It was beyond the scope of this study to carry out benchmarking studies of the raw materials used in the processed food sector. Some benchmarking of raw materials has been attempted by various research organisations, but it does not cover the sector comprehensively and most of it is now outdated. The main findings of this benchmarking, though, support the proposition that only in the dairy industry and some parts of the meat and grain sectors, do raw materials confer substantial competitive advantage on food processors. The findings are summarised in Table 4 and a more complete synopsis is in Appendix 1.

---

20 That is, where price is the primary determinant for the competitiveness of the product.

21 That is, where factors other than price are the primary determinant of the competitiveness of the product. Examples would be where quality, branding, organic status or freedom from genetically modified ingredients are of primary importance to the consumer.

Table 4: Summary of Price Competitiveness of Agricultural Sub-Sectors

Raw Material	*Competitive?*
Dairy	Extensively benchmarked. Australia ranks with New Zealand as the world's lowest cost producer.
Chicken Meat	Australian costs are much higher than key poultry exporting nations such as the US, Brazil, Thailand and China, though comparable to the EU.
Pig Meat	Australian costs of production are, on average, higher than the US and Canada and some south east Asian countries. Only Australia's most efficient producers are at or close to world best.
Beef and Lamb	Pasture based production is competitive. Feedlot beef production is less competitive than in the US, because of higher feed-grain cost and low labour productivity.
Horticulture	Australia is considered a high cost producer.
Grain	Production is efficient and Australia trades internationally against subsidised products, though distribution adds inefficiencies.
Sugar	Production is generally efficient. Australia competes against developing countries with weaker currencies that periodically confer competitive advantage.

The views of the firms on raw materials

In the survey, 45 per cent of firms said that the high cost of raw materials is a significant impediment to exports.

Interviewees generally agreed that the raw materials used by Australia's food processors are not notably less expensive than those available to many of their foreign competitors. In some cases — for example, most horticultural products for processing — they are considerably more expensive. If raw materials are no cheaper for processors — or are more expensive — then the development of a strongly export-oriented food processing industry for price sensitive markets would be counter-intuitive.

> *"We get no competitive edge from the raw material, sugar, because of the price we have to pay for it — nor from the colours and flavours, which are supplied by local multinationals. So for us, exporting is marginal, even though we try for product differentiation. Exchange rate fluctuations, government policy changes here in Australia, foreign protection and the foreign competition all make it difficult. There are many more unknowns than in the domestic market. Therefore, it makes sense to use export markets as 'cream'. In, fact, we used just to trade opportunistically in export markets; now we are trying actually to develop export markets. But it will be hard going. My three wishes? One, get the sugar price down; two, fight harder to get the foreign duties down; three, the government should provide more effective assistance to exporters."*
>
> CEO, Australian subsidiary of foreign multinational

Ten percent of the firms mentioned domestic price support measures for some commodities, such as single desk selling, which increase the cost of some raw materials to processors, making them more expensive compared with competitors. A smaller number of firms also mentioned commodity marketing structures focused on export markets which they said limit the volume and even the quality of raw materials available to local value-adders.

Other than those in dairy, interviewees who had not in the survey rated the cost of raw materials as an impediment to exports were generally opportunistic exporters focussed, in the main, on the domestic market and not facing strong import competition.

Manufacturers of niche market products where intrinsic worth is more important than price also considered raw material input costs are not an impediment. These were in a minority.

> *"The juice industry can't achieve a competitive edge deriving from the cost of raw materials, since there's a world price for the concentrates, a highly-traded commodity. So it's what happens after the raw materials enter the factory that determines how competitive our products will be in foreign markets."*
>
> CEO, large Australian juice manufacturer

The effect of foreign export subsidies

A majority of the interviewees were aware that, due to export subsidies, their competitors were often able to succeed in export markets even where their raw material costs were substantially higher. The export subsidies provided by foreign governments are successful in keeping their firms in markets in which Australian firms would otherwise do much better.

Firms in processed dairy were particularly vocal about this "unfair competition". Price distortions in northern hemisphere countries, particularly in dairy and horticulture, generate surpluses which have to be exported. But these exports can only compete against more efficient producers, such as Australia, with the support of export subsidies.

Little competitiveness in value adding

During the interviews, very senior and experienced managers in larger companies said that, in Australia, value-adding (including manufacturing, packaging, branding, marketing and distribution) was unlikely to confer competitiveness and often diminished it. Figure 6 summarises the views of firms on this issue.

Interviewees from smaller firms did not generally volunteer such views. But when they were either shown a version of Figure 6 or told about it, they agreed that it generally reflected commercial realities.

Figure 6: Highly Processed Foods: Can We Compete on Price?[22]

Value chain	*Critical Factors*	*Competitive?*
Raw material (delivered to factory)	Critical factors include price, objective and subjective quality, length of supply season, reliability of supply.	Generally little if any price advantage (except dairy, some meats and some grains).
Manufacturing	Generally, few firms have a competitive advantage. Much of the intellectual property is owned in Europe and North America. Labour productivity is lower than competitors. Capacity utilisation is low.	Firms agree little competitiveness is achieved.
Packaging	Many issues for Australian firms. Australian packaging industry roundly criticised by interviewees as failing to perform on many measures. Many food firms import packaging.	Uncompetitive. Consensus among firms was that costs are in the order of 10 per cent higher than competitors.
Branding	Australian food firms (outside wine) have few brands that are recognised in foreign countries. Establishing and building international brands is beyond the resources of most Australian companies.	Outside wine, few firms achieve any competitive edge through brand building strategies.
Freight	Many problems reported. Geographical fragmentation of the domestic market. High relative cost of domestic and international freight and problems with availability of some services. Distance to markets reduces in-market shelf life for many products.	Difficult for firms to achieve a competitive edge.
Marketing	Distance and isolation increases costs. Capabilities of firms generally weak. Little investment in marketing innovation.	As things stand, only the best firms achieve a competitive advantage.
Financing	Some advantages against some Asian competitors. But cost of debt and equity generally higher in Australia than in most competitor countries.	No competitive advantage.
R&D	A possible source of competitive advantage, for those firms that invest in innovation in processes, products, marketing etc.	The better firms are achieving a competitive advantage but they are few in number.

22 The ideas upon which this table summarises draw extensively on the contribution of Mr Ron McMahon, Queensland Department of State Development, which is gratefully acknowledged.

These findings and observations about competitiveness echo the findings of a study completed in 1995 by McKinsey & Company Australia and the McKinsey Global Institute[23] and a related article in the McKinsey Quarterly, in 1996.[24]

The main finding of the McKinsey study was that productivity in the Australian food processing industry was only 68 per cent of the US level. It identified a range of reasons for this, the most important of which was slow adoption of process, product and service innovation.

Price or value competitiveness?

At the Focus Group sessions, several participants said that, for highly processed foods, the competitiveness that counts comes from finding niche markets for niche products — giving the customers what they want before the competition finds the niche — and backing that up with service.

> *"Australia will have a great deal of difficulty in competing in highly processed foods in Asia. Australia won't be the food bowl of Asia. Asia will be the food bowl of Asia. The role of Australia in the Asian processed foods market will only ever be as a niche player. A possible exception is Japan, though the non-tariff barriers there are enormous."*
>
> Senior manager, large Australian exporter

Several said they avoided price sensitive markets; they made it a rule to concentrate on quality-responsive markets.

A common theme raised by the more experienced exporters is that competitiveness is determined by intellectual property, all along the chain. For highly processed foods, the path to more competitive products and greater success in export markets lies in increasing the intellectual input down the value chain from the raw materials — in particular the quantum and quality of R&D and product or process innovation.

During the interviews and the Focus Group discussions, many of the more experienced and successful exporters emphasised that price competitiveness is only one of the determinants of export success. Innovative and highly differentiated products, well packaged and energetically and skillfully marketed, can command premiums in foreign markets, just as they can in domestic markets. Where they did not derive an advantage from competitively priced raw materials, the good niche exporters said the price of raw materials was not an insurmountable impediment.

23 McKinsey & Company with McKinsey Global Institute, *Growth Platforms for a Competitive Australia*, 1995.

24 Lewis, W., McCann, W., McLean, R. J., "What ails Australia?" *The McKinsey Quarterly 1996*, Volume 1, McKinsey Company, 1996.

"In export markets, we're struggling to be competitive on price. And our margins are much lower than in the domestic market. We try to take advantage of things like the clean, green and safe image that is said to attach itself to Australian beverages: the 'value of values' idea. It works for us in New Zealand, where people think there's something desirable about an Australian as opposed to a locally made soft drink."

Owner-director, medium sized beverage company

R&D and innovation

A substantial majority of the 157 firms which took part in the survey claimed to be investing in R&D, in product development, processing and, to a lesser extent, packaging.

Table 5: Investment in R&D

Category of Investment	*Yes*	*No*	*Unsure/Don't know*	*Not applicable*
Products	82%	7%	3%	7%
Packaging	67%	15%	3%	14%
Manufacturing Process	84%	8%	4%	4%

At the interviews it was also apparent that most firms understand the critical importance of the creation of intellectual property along the value chain. However, further investigation revealed that very few were carrying out R&D of a quality or on a scale likely to reach world benchmarks. Less than twenty percent of the firms had the necessary facilities, personnel or financial resources to manage leading-edge R&D. Those that did were the larger firms, both Australian-owned and Australian-based operations of foreign multinationals.

R&D programs undertaken by foreign-owned firms are likely to be part of a corporate global R&D plan. Intellectual property created by the Australian subsidiary becomes the property of the larger entity. There are specialist R&D staff employed in the Australian subsidiaries, but they are also drawing down resources from the firm's laboratories in other countries. Even so, two such firms in the dairy industry reported that their process and product development was 18 months to two years behind the foreign parent.

By contrast, nearly all the smaller firms, all but one of which was Australian-owned, were putting resources into simple 'kitchen bench' activities designed to improve products, processes and, in a few cases, packaging. The better small firms claimed to be investing heavily in this sort of activity and to be achieving good results.

Overall, it appears that the industry may be carrying out less innovation encompassed by the normal definitions of R&D than was indicated by the survey data. But the picture improves if the 'kitchen bench' activities of the small firms are added to the conventional, 'technicians in white coats' activities of the medium and larger firms.

Decline in R&D expenditure

Desk research indicates that conventional R&D is in decline in the processed food sector.

R&D expenditure in the food/beverages/tobacco manufacturing industries declined by almost 38 per cent between 1995/96 and 1997/98.[25] There was a 21 per cent decline in the number of people in the industry employed in R&D. The study also found that processed foods ranked last among manufacturing sectors in terms of its use of modern technology.

It was not possible to determine trends in investment by the smaller firms in the less sophisticated innovative activities which characterise their efforts at innovation. However, what the small firms said about innovation during the interviews suggests that the trend for them is unlikely to be down.

Overall, the balance of probability is that, since the mid 1990s, the total investment by the industry in R&D and less formal innovative product, process and packaging development has been falling.

Government support for R&D

If investment in innovation is declining, close attention to the industry's awareness and up-take of government support for R&D is warranted.

Relatively few survey respondents knew about government support for R&D and even fewer were enjoying any form of government support.

Table 6: Utilisation of Government R&D Schemes

R&D Scheme	*% of Respondents*
No use of Government R&D Schemes	25
Unsure / don't know	43
125% Tax concessions	28
Co-operative Research Centre	8
R&D Start	5
Food into Asia	1
RIRDC	1
Export Marketing Development Grant	1

Note: some firms use more than one scheme

During the interviews, it became clear that the larger firms were more likely than the small firms to know about and draw down support from government programs. The main reason was that smaller firms felt they lacked the resources to find out about them or to apply for them.

25 Australian Bureau of Statistics (ABS), *Research and Experimental Development, Business*, Catalogue No. 8104.0, 1997–98.

National innovation system

Governments have established and funded 'food centres' — for example the Centre for Food Technology in Queensland, Food Science Australia in Victoria and the Food Centre in Western Australia — where R&D is being conducted and facilitated. But at interview, only about ten percent of firms said they knew about or used these organisations. Eight firms mentioned having worked with a cooperative research centre.

It appears that the firms are not knowledgeable about the national innovation system or how to work with the appropriate parts of it.

Innovative export marketing

At the interviews and Focus Groups, an attempt was made to discover if firms had developed innovative ways to market their products in foreign countries and, in particular, to multinational supermarket chains. In the event, even though experienced exporters acknowledge the importance of innovative marketing, most firms approached the task in a conventional manner. The most unconventional approach was from three smaller firms which had made direct approaches to foreign supermarket chains; each had been surprised at the good reception their overtures had received. Several other firms were exporting to foreign supermarket chains but there was nothing particularly innovative or unconventional about the way they were going about the business.

Few firms showed a sophisticated knowledge of the theory or the practice of 'value chain' or 'demand chain' management: at least, they did not use these or related terms of their own volition. Only with a few companies did discussions about demand chains become animated or illuminating.

> *"What we have not done, but ought to do, is to add value on the 'emotional-functional' plane. Because our products are not clearly differentiated, we are struggling for margins. At the same time, we will have to devote more resources to communicating better with our customers, increasing their awareness of the nutritional and other functions of our product."*
>
> CEO, large exporter

A number of more experienced owners and managers, particularly those with extensive experience in foreign countries and in international business, attributed success in developing new export markets to their networks of friends and professional colleagues in food businesses in foreign countries.

Several of the international advisers commented on what they saw as the weaknesses of Australian processed food firms in export marketing. They observed that many firms were too small to be innovative and effective in marketing and that even larger Australian firms were not resourceful or flexible enough to be successful.

Innovation — the overall picture

Overall, the evidence of the survey, the interviews and the desk research suggests that weakening investment in innovation for product, process and packaging development may be limiting the propensity of the firms to develop products that will compete in world markets.

The larger firms are reducing investment in conventional R&D. Multinational companies tend not to locate key R&D facilities in Australia and the Australian-owned firms rely heavily on intellectual property which is owned outside Australia.

> *"Our customers tell us 'Australia is good at commodities, but as soon as you add value you add too much cost!' Why is that? It's because most of the intellectual property in the business resides in the USA and Europe. The solution is to put more brain power into what we do. But this company is owned by the producers of the raw materials it uses. They have never felt any need to put brain power into the value adding."*
>
> Senior executive, major food company

The better small firms are innovative, but scale and capital constraints limit what they can do to create products that succeed in export markets. Even when they are able to undertake R&D, they are likely either not to know about, not to be interested in applying for or unable to qualify for government support.

Value-adding and the East-West divide

Many entrepreneurs from Asia have settled in Australia and some have technological know-how and useful business links in Asia relevant to processed food manufacturing and exporting. However, for a variety of reasons, very few of them have been able to compete in export markets.[26]

Three of the managers interviewed for this study had come to Australia from Asia. Each observed that the biggest opportunity in Asia was not the niche for food in the Western tradition, but for mainstream Asian processed food. One of them had tried to produce food in the Japanese tradition for export to Japan, but problems with technology and the scale at which he was able to operate led to failure. Of the firms interviewed, only a sake producer owned by a sake house in Japan was succeeding in exporting an Asian product to Asia.

At the Focus Groups, industry participants were extremely interested in the proposition that their industry as a whole looks primarily to Europe and North America as the source of intellectual property, technology and equipment, rather than to Asia, which is the focus of most of the industry's export market ambitions. It was noted that most of Australia's factories are ill-equipped to manufacture food in Asian traditions yet it is food in this tradition which constitutes the mainstream in markets to Australia's north. Even many

---

26 INSTATE Pty Ltd, *Asian Food in Australia: Getting a Bigger Bite*, Rural Industries Research and Development Corporation (RIRDC), 1994.

'global' foods are subtly transformed in taste, texture or packaging to match consumer values in these markets more precisely.

In general, it seems that the more value is added to food by Australian processors, the more the final product is likely to diverge from tastes and needs in the large and proximate markets of Asia. The presence in Australia of a large number of migrants from Asia suggests that this impediment to exporting more Asian-style processed food from Australia might be surmountable.

The inputs to the study received from analysts and practitioners based in Asia strongly supported these points. They observe that Australia's concentration on processed foods in the western tradition is a problem on two counts: not only does it miss the mainstream opportunity in Asian foods but, in many cases, Australian product ends up being viewed by Asian consumers as derivative and therefore inferior to 'authentic' products from Europe and the United States.

Other competitiveness factors

People

The 103 firms interviewed in this study cover a spectrum of the industry — from state-of-the-art to antiquated factories, from top-flight leaders of vision and ability to battlers with poor prospects of survival. Overall, firms acknowledge weaknesses in their capabilities to initiate and sustain exporting and many of these weaknesses relate to people, their skills, motivation, training and outlook.

There is a cadre of talented proprietors and managers with global business experience and perspectives. There are some highly entrepreneurial and innovative proprietors of smaller businesses.

Twelve of the interviewees were senior Australians with lengthy experience in managing agrifood enterprises in countries outside Australia. Three of the people interviewed were people from Asia managing food processing businesses in Australia.

A common perception among the industry leaders with experience outside Australia was that the industry is held back by shortcomings in general management, technical skills and export management. The managers from Asia said that there were other shortcomings in personnel management in Australia; in particular, in developing high levels of attention to detail and positive attitudes of employees and managers to their firm.

> *"One problem is motivating staff: the work ethic. We have no serious industrial relation problems. We take pains to recognise the professionalism of our people and to help them to understand the scope and seriousness of the challenges ahead. One issue is how defensive they tend to be. The west has a 'culture of guilt' while Asia has a culture of 'face'. I am trying to teach our people to consider it a privilege when they are audited and problems are identified. I say 'The problem is not the problem — not admitting, raising and tackling the problem is the problem'."*
>
> CEO, listed manufacturer

Many of the interviewees, including managers of small and medium firms, acknowledged that there were serious shortages of technical skills in the industry; for example, in product and process innovation, packaging design and e-commerce.

Except among the larger companies, there was very little knowledge about the practical issues of strategic planning for export and, in the sector as a whole, a paucity of managers or staff with highly-developed, practical export skills.

One very experienced CEO of a large firm observed that, apart from the wine industry, food processing was not seen by talented young people as an attractive place to start or build a career. Governments made this worse, by creating the impression that manufacturing is less important than service industries. The result is that the food industry finds it difficult to recruit and retain the best people.

> *"It's imperative to lift the status of manufacturing in the community. It used to be seen as essential and honourable: it's not now. People, politicians, new graduates, are more interested in the flashy new industries with the promise of the quick buck. That's fine as far as it goes and for while the finance sector boom lasts, but it's also vital to have an under-belly. We have the agricultural base and we need the manufacturing that should sit between the farms and the tertiary sector. Scholarships and apprentices for the manufacturing sector are disappearing. Then there's the malaise of ageing technology and the weak technical infrastructure. And the skills base is being run right down."*
>
> CEO, large beverage company

Capacity utilisation and scale of operations

Firms with above average capacity utilisation rates (75–90 per cent) were slightly more likely to be highly export-oriented.

On average, firms in the survey reported capacity utilisation rates of about 60 per cent, which participants at the Focus Groups thought was likely to be accurate or even perhaps on the high side.

Interviews revealed a wide disparity in measures of capacity. In some cases, capacity was measured on narrow terms: for example, one and a half shifts, five or six days a week. Others measured capacity more generously. The Steering Committee considers the full capacity of a manufacturing plant to be three shifts a day, seven days a week, less necessary down-time for maintenance and hygiene. Against this measure, utilisation may be significantly lower than 60 per cent.

Interviewees gave a large number of reasons for low capacity utilisation and the Focus Groups discussed the issue in some detail. The most common explanations were the seasonality of supply of raw materials, misjudgments about the likely rapidity of growth of domestic and export markets and the unavailability of 'off-the-shelf' smaller sets of plant and equipment. One very large firm said that it was inhibited from consolidating operations into a smaller number of plants — which would have increased capacity utilisation and achieved capital efficiencies — by the high costs of redundancy payments.

> *"Why is our capacity utilisation so low? Several reasons. First, we got excited back in the early 90s about the export markets we were going to win. Government people were always talking about how Australian companies were often confounded by export orders from places like Japan which challenged the business's capacity to produce. We didn't want to fail like that, so we bought more machines. Some of the volumes being talked about by our foreign customers were 50 per cent of the Australian market. In the end, things didn't go as well in export markets as we had hoped. Second, we import most of the equipment. It used to be made here in this small country town but not much like that is done in places like this any more. We can't buy equipment off the shelf in Europe small enough to suit us. It's designed for use by much larger firms in Europe."*
>
> Proprietor, regional-based exporter

The interviews and desk research suggested that the scale of plants must affect the ability of firms to compete in foreign markets. This tentative observation was reinforced by the observations of interviewees and participants in the Focus Groups. Plants in Australia are generally smaller than in some countries which are strong competitors; for example, the United States and European countries.

The discussants said scale adversely affects the international competitiveness of most Australian food processors, in a variety of ways. For example, it affects their costs of production, their ability to devote resources to R&D and export market development and their ability to go successfully to capital markets.

But being small can sometimes be an advantage. Four firms noted that it sometimes meant that they could succeed with products for which the niches in foreign markets were too small to attract the attention of larger companies.

While the data generated by the survey and the interviews is not conclusive, the sector as a whole seems not to be using its capital efficiently, and probably less efficiently than foreign competitors.[27] If that is the case, overall it must reduce the extent to which many individual firms will be highly export-oriented.

Ownership

The survey data suggests that firms which are Australian-owned tend to be slightly more export-oriented than firms with foreign parents.

The interviews threw a little extra light on this subject. The large firms interviewed were, in the main, owned by foreigners or primary producers. They had very strong interests in domestic markets. The export focus of these firms is oriented towards the lower end of the value chain.

27 McKinsey & Company with McKinsey Global Institute, *Growth Platforms for a Competitive Australia*, 1995.

The interviewees gave several reasons for this focus. Australian simply processed product is more competitive than highly processed product in foreign markets. The market entry barriers in foreign markets are usually lower for simply processed food — reflecting, in many instances, the determination of foreign governments to protect or promote domestic processing industries. The owners see their interests as best served by concentrating on the commodity end of the spectrum for exports and emphasising domestic markets for highly processed products.

The survey data and the interviews did not suggest that restrictions imposed by foreign parent companies explain why their Australian subsidiaries tend to be more focussed on the domestic market. Rather, the survey data — supported by the interviews, the desk research and the Focus Groups — lends weight to the proposition that most foreign entities invest in food processing in Australia mainly to reach the domestic market.

There are enterprises in Australia which were established by foreign investors to supply foreign markets. But these are not numerous. Only one such enterprise was included in the interviews. The Japanese sake house, Konishi, has a plant at Penrith which exports most of its production to Japan.

Packaging

A very large number of the firms interviewed spoke at length about the way the cost and other problems associated with packaging reduced their competitiveness and otherwise made business more difficult. A common concern was voiced about limited glass packaging options, but identified problems were not confined to glass packaging. For example, problems with plastic tubs for use in dairy-based and other related products were mentioned frequently. Some firms are importing these from Italy, to achieve cost savings and because locally-made packaging was considered to be of inferior quality. Interviewees said Australian packaging cost them, on average, around ten per cent more than foreign competitors would pay.

The packaging issue was discussed at the Focus Group sessions, with similar problems and issues being raised by the participants.

One firm succinctly noted the conundrum. The Australian food processing industry is not large and innovative enough to support a thriving local packaging industry. Without a thriving local packaging industry, however, the processing industry will be burdened with extra costs and other constraints that stop it from growing quickly, including through exports. This was confirmed during the Focus Groups.

> *"Packaging is a serious problem. It's too expensive and not competitive with what's available in foreign countries to firms like ours. But as I said earlier, our main problem is inefficiencies in our own operations. If we got rid of them, the problems with packaging wouldn't matter so much."*
>
> CEO, large manufacturer

Machinery

Six of the very experienced interviewees from large companies talked at length about the constraints on competitiveness imposed because a large proportion of the machinery used in the industry has to be imported. For much of the industry's needs there are few local manufacturers. The weaker the local machine building industry, the greater the burden on the processors, because importing is expensive and foreign plant and equipment is not often available 'off the shelf' to match the required capacity and other specifications. Several of the small firms echoed these views.

> *"If the government wants to support the food industry and get it to export more, it should spend money on trapping more processing intellectual property in Australia."*
>
> Senior executive, major dairy company

There was also a view that owning the intellectual property imbedded in the plant and equipment was a key to international competitiveness. This issue is treated earlier in this subsection.

E-commerce

Firms in the survey are using the internet mainly for e-mail and as a tool for searching for information.

During the interviews, far fewer firms than those which said in the survey they were involved in electronic commerce were found to be actually using the internet to conduct business. A number had misunderstood the survey question, which was itself a further indication that many companies are not very advanced in conceiving of the internet as a business tool. As was to be expected, it was the larger firms in the big cities which were most likely to be adopting e-commerce.

The up-take of e-commerce varied from state to state, with firms in South Australia, Western Australia and Tasmania less likely than firms in Victoria and New South Wales to be making use of it.

In the survey, 89 per cent of firms said they would increase their use of the internet. For a majority of firms, the next step would be the establishment of a web site.

The interviews confirmed what the survey had suggested about the reasons given for not making more use of the internet. The main factors cited were concerns about security, costs and lack of understanding of the technology.

Many of the firms said that they had been induced to speed up the adoption of internet based-commerce by the large supermarket chains or their banks, which demanded that they do so. Several firms said that foreign customers, particularly those in Asia, were behind Australian and North American firms in up-take of internet-based commerce.

Small and medium sized companies showed a low level of appreciation for the potential of electronic solutions for value chain management. But some managers reveal a profound reluctance to use information technology: at interview, one manager said that he had bought a computer for the firm some six months earlier, but that it had not yet even been set up.

This is a significant issue, especially given that Australian manufacturing processes are more expensive than in competitor countries. Intelligent application of IT solutions can enable firms to significantly cut costs associated with ordering, invoicing, inventory management, and building and maintaining customer relationships in both domestic and export markets. While it is true that the IT capability in many Asian countries lags Australian infrastructure,

Figure 7: Use of Internet Services

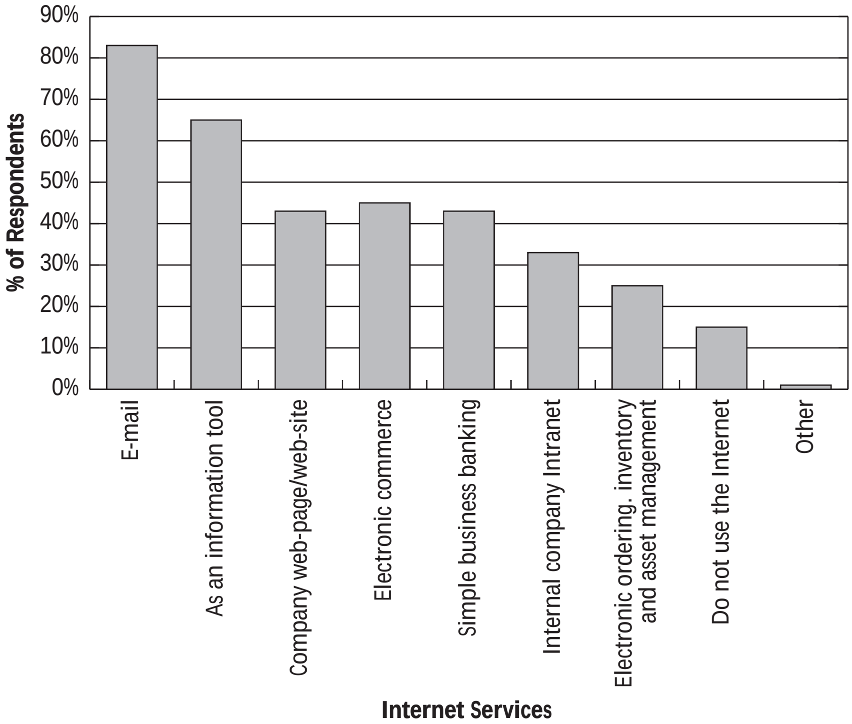


Table 7 : Factors Preventing Firms from Increasing Internet Usage

Factor	*% of Respondents*
Lack of internet security	36
Cost of investment for new technology	33
Level of understanding/education	30
Customers do not have access to it	21
Suppliers do not have access to it	17
Other	17

early up-take of electronic solutions may offer a competitive advantage to smaller companies.

Genetically modified foods

In the survey, firms were asked for their views on the introduction and future use of genetically modified (GM) foods. A large number professed uncertainties about the issue. However, the interviews revealed that there is a good deal of support within the industry for responsible development of improved animal and plant breeding through genetic modification. There is, however, a high level of concern about the public handling of the issue, more pronounced during the interviews conducted towards the end of 1999. The greatest concern is ambiguity. Customers, including foreign customers, are asking manufacturers for assurance that products are GM free. However, manufacturers say they have no way of knowing whether externally sourced ingredients over which they have no direct control — for example soy, pectin, extracts and essences of various kinds — contain GM material.

Tax Reform

As a result of tax reform measures being discussed and implemented while the interviews were in progress, tax reform was raised with the discussants.

Approximately 80 per cent of the firms interviewed said that they knew very little about the changes to the business tax system recommended by the Ralph Committee. Of the 20 per cent who said they knew something, most mentioned proposed changes to the capital gains tax.

Fewer than ten per cent of the interviewees were strongly of the opinion that the Ralph Committee changes would be beneficial to them. There was a high degree of scepticism. A substantial majority of the interviewees said that they would 'wait and see'.

2.4 EXPORT MARKETS AND IMPEDIMENTS

Care was taken in the survey design and during the interviews and Focus Group discussions to assess firms' perceptions of the relative importance of export markets and the impediments which firms feel prevent them from exporting successfully.

In the survey data, few correlations were found between perceptions of export impediments and the export orientation of the firms.

The survey data did suggest that firms which are not highly export-oriented are slightly more likely to rank 'access to distribution networks' as a significant barrier to exports.

The survey data indicates that non-exporters and successful exporters are more likely than inexperienced exporters to rank tariff and non-tariff barriers as significant impediments to exports.

At interview, smaller and less experienced exporters were more likely to say that their lack of knowledge of foreign markets, including distribution networks, was a barrier to their export activities.

At interview, the successful exporters that ranked tariff and non-tariff barriers as significant were more often than not larger firms with sufficient scale and management resources to deal with domestic impediments, which at interview they tended to rate as serious.

Twenty-two of the 103 firms interviewed said they either had not exported or had only 'exported' through an intermediary. These firms had little knowledge and few insights about barriers in foreign markets.

Four such intermediaries, or 'accumulators', were interviewed. Their role was also discussed with several of the more experienced exporters among the interviewees, and by the Focus Groups. The consensus was that the accumulators play a significant role in facilitating exports, particularly for small and inexperienced firms. There was also a view that governments tended to under-rate or otherwise misunderstand their significance and contribution.

Current and future markets

The top four current export markets identified by survey respondents were New Zealand, Japan, Singapore and Hong Kong. Firms identified these four markets as likely to remain equally important to 2001.

Among the top ten export markets, firms identified China, the United Kingdom, and Korea as likely to increase in importance. The interviews suggest that firms are up-beat about China's economic prospects, regard Korea as likely to recover rapidly from the effects of the Asia crisis and looked to the United Kingdom as a relatively easy market to tackle.

The survey respondents identified the Philippines, Indonesia and Thailand as markets likely to become less important. The interviews indicate that the relative pessimism about these markets is related to current issues, particularly the deterioration of their economies resulting from the Asia crisis and, in the case of Indonesia, increasing concerns about political and social instability and anti-Australian sentiments related to the situation in East Timor.

Most firms exporting to New Zealand said that they regarded it as a natural extension of the Australian market. A small number of these firms volunteered opinions which demonstrated that they are aware of the Closer Economic Relations (CER) treaty and its role in creating a single Australasian market for most processed foods.

A majority of the firms is aware that the size and diversity of the market in Japan for processed food creates many opportunities, for niche players as well as exporters of products at the commodity end of the spectrum.

At the same time, few of the firms, apart from the larger ones, claimed to have any detailed knowledge of the market in Japan for their products. Three smaller firms reported they had made unsatisfactory or subsequently aborted attempts to develop markets in Japan. Three small firms and one larger firm in speciality cheeses reported good progress in Japan, against stiff price competition from subsidised European product which Japanese consumers also considered to be more ‘authentic’ than the Australian versions.

Table 8: Current and Future Markets

Rank	*Current Markets (1998–99)*	*Future Markets (1999–2001)*
1	New Zealand	New Zealand
2	Japan	Japan
3	Singapore	Singapore
4	Hong Kong	Hong Kong
5	Philippines	China
6	Malaysia	Malaysia
7	China	United Kingdom
8	Taiwan	Taiwan
9	Indonesia	Philippines
10	Thailand	Korea

Export markets: optimism for the short-term

The survey data and the interviews revealed a generally positive outlook regarding export opportunities. More than seventy percent of the firms in the survey thought their exports would increase in 2000 and 2001. Less than 20 per cent of firms thought that their export markets would decline in the next two years.

It should be noted, however, that optimism was considerably higher among the firms exporting lower value-added products, or in cases where output covered the full value-chain spectrum, in regard to products at the lower end of the value chain.

The interviews suggest that this optimism derives partly from the generally optimistic mind-set of business people. In all probability it also reflects the generally buoyant economic conditions in Australia, Europe and North America and a widely shared belief that the worst of the Asian economic crisis is over and that many significant Asian markets will recover rapidly.

A substantial minority of firms reported finding new markets outside Asia after the on-set of the Asian crisis. One of the international advisers commented that this might suggest under-performance in markets beyond Asia, or an earlier concentration on Asia to the exclusion of other equally or more attractive opportunities.

Domestic impediments to exporting

The general air of optimism notwithstanding, the survey data suggested that respondents were strongly of the opinion that they are at a disadvantage compared with foreign competitors in foreign markets. The survey data also suggested a perception that the disadvantage relates to the overall business environment in Australia, to problems within the firms and to domestic and foreign freight issues.

The following domestic costs were identified by at least 45 per cent of survey respondents as inhibiting their exports:

1. Labour
2. Domestic freight and transport
3. Financing new plant capacity
4. Domestic government charges
5. Raw materials.

Where appropriate, interviewees were questioned closely about these issues. They were also discussed in detail by the Focus Groups.

Labour

Two thirds of all firms in the survey identified labour costs as an impediment to exports. Smaller firms were more likely in the survey and at interview to identify the cost of labour as a factor inhibiting exports.

Interviewees frequently said that labour might not be such a serious cost factor as they had indicated in the questionnaire, indicating that many had ticked ‘high cost of labour’ as a matter of instinct, without really thinking about it. About 25 per cent of interviewees volunteered views about the productivity of labour and the need to train and otherwise improve the skills base. Larger firms with international operations or connections were more likely to have views on these questions. Several drew a direct connection between the cost of labour, labour productivity and international competitiveness. A number of the interviewees mentioned labour on-costs.

Only three firms spoke at any length about industrial relations as an impediment to exporting.

Firms which ranked 'cost of labour' as a very significant factor inhibiting exporting may have been using shorthand for low labour productivity, reflecting issues other than wage rates; for example, management skills. The McKinsey study[28] used labour productivity as a way of coming to grips with the broader aspects of the productivity of the food sector. Its conclusions are consistent with the conclusions of the present study.

Domestic freight and transport

Two thirds of all the firms in the survey indicated that costs associated with domestic freight and transport inhibited exports. At interview, it transpired that in most cases either raw materials, packaging or finished products — or all of these — had to be transported considerable distances within Australia. There was limited time in the interviews to go into greater depth, but there was a general perception that while competition is keeping the cost of road transport down, rail and air are expensive and inefficient.

Three firms noted that some packaging materials, which are light but voluminous, are particularly expensive to transport over long distances.

Financing new plant and equipment

Two thirds of all firms in the survey said that insufficient financial resources inhibited exports. The interviews and Focus Group discussions suggested that medium and small firms are more likely to be hampered by cost and availability of various forms of financing new plant and equipment, product or process development and export market development. Among the medium and smaller firms, a majority acknowledged problems with under-capitalisation.

Small firms are generally confined to financing expansion, or investment in innovation, from retained earnings or by borrowing. Using retained earnings usually slows the process of development, because profitability in this industry is low. Lenders treat small firms conservatively, expecting to secure loans against fixed assets. Small firms find it difficult to raise new equity.

Larger firms usually have fewer problems with borrowing. But Australian investors, including institutional investors, are not enthusiastic about the processed food sector. They see better returns in other sectors. The shares of listed companies languish on low price to earnings ratios. Three interviewees, each with long experience at senior levels in Australia and overseas, spoke at length in these terms.

> *"Australian investors are no longer interested and don't understand the long time-frames needed to build competitive food businesses. If that doesn't change, more and more of the industry will slip into foreign hands."*
>
> CEO, large exporter

28 McKinsey, (1995), *op cit*.

The same three interviewees noted that Australians are generally not prepared to make the investments of patient capital necessary to bring the food processing sector up to world benchmarks.

Foreign food companies are more prepared to buy into the Australian industry, especially where they can acquire assets cheaply. In most cases, they have done so as part of a global strategy, mainly to supply the Australian market.

Domestic government charges

Just over fifty per cent of firms in the survey indicated that mandatory Commonwealth Government charges inhibited exports.

During the interviews, the charges mentioned most frequently were AQIS and Austrade charges. These are discussed in detail later in this Section.

Larger firms mention government charges infrequently and none saw them as a serious impediment.

Raw materials

This issue is examined in detail in Section 2.3.

Other domestic impediments

Firms in grains-based processing, particularly the larger firms, were concerned about single desk marketing arrangements, which they saw as limiting their ability to obtain raw materials at competitive prices and otherwise limiting their flexibility and responsiveness to foreign demand.

Firms large and small in dairy-based processing were in agreement that the further reform and rationalisation of the dairy industry might help encourage processors to move further down the value chain. Smaller firms concentrating on high value-added products, such as speciality cheeses, expect to be able to compete more effectively following industry deregulation.

Lack of innovation is also an impediment — it is discussed in detail in Section 2.3.

Foreign impediments to exporting

Respondents to the survey identified the following as the main foreign impediments to exporting (in descending order of frequency of identification):

1. High freight and transportation costs
2. International competition too strong
3. Access to distribution networks
4. High tariff barriers
5. High cost of doing business in Australia

6. Insufficient knowledge of market place and contacts
7. Non-tariff barriers
8. Asian financial crisis
9. Too risky and costly
10. Domestic markets providing adequate demand.

These factors can be re-grouped, as follows:

Table 9: Foreign Impediments to Exporting

Real foreign barriers	*Market information issues*	*Competing in foreign markets*	*Attitudes*
High tariff barriers	Access to distribution networks	High freight and transportation costs	Too risky and costly
Non-tariff barriers	Insufficient knowledge of market place and contacts	International competition too strong	Domestic market providing adequate demand
	Asian financial crisis	High cost of doing business in Australia	

As appropriate, these issues were discussed with interviewees and with the Focus Groups.

Tariff and non-tariff barriers

Larger, established exporters more frequently identified tariff and non-tariff barriers as significant impediments to exports. For example, at interview, firms exporting simply-processed dairy foods all referred to foreign tariff and non-tariff barriers — as well as to export subsidies. They pointed out that their products were highly competitive in most export markets. This, they feel, probably explains the extent of both the tariff and non-tariff barriers as well as the export subsidies used by governments of competitor countries to support their domestic producers and exporters.

In the survey, the markets most frequently cited by respondents as having significant tariff barriers were Japan, China, Taiwan, Indonesia, the Philippines, Malaysia, Thailand, the US and the UK and Europe. For non-tariff barriers, the markets mentioned most frequently were Japan, China, Korea, Malaysia, the Philippines, Indonesia, Thailand, the US and the Middle East. Of these markets, only the US, Europe and the Middle East are not among the top ten current and future markets identified in the survey.

Most respondents to the survey and most of the interviewees were unable to be very specific about the tariff and non-tariff barriers being encountered by their exports in foreign markets. During the interviews, attempts were made to discover the reasons for this. Non-exporters knew that tariff and non-tariff barriers existed but none was able to be specific about them. Firms exporting through trading companies and other intermediaries were similarly not knowledgeable about foreign barriers to exports — most probably because they do not have to confront them directly. Other interviewees said that while they were not clear about the precise height or nature of the barriers in foreign markets, there were others in the firm who probably were. Some said that their agents in foreign markets looked after these problems.

In the survey, the most frequently cited non-tariff barriers were labelling, export subsidies, documentation requirements of foreign countries, import levies and other import regulatory restrictions or prohibitions.

Table 10: Non-Tariff Barriers

Barrier	*% of Respondents Rating Barriers as Problematic*
Labelling	26
Export Subsidies	18
Documentation Requirements	17
Import/Export Levies	16
Import/Export Restrictions/Prohibitions	16

The interviews confirmed that firms perceive an array of non-tariff barriers. Only a relatively small number of interviewees were able to be highly specific about them. The Focus Groups provided some additional examples and anecdotes. These included difficulties with foreign language labelling requirements in many markets and a large number of references to the export subsidies provided by European governments and the United States to their exporters. Larger companies were generally more concerned and better informed about export subsidies and domestic market support arrangements.

The smaller companies more frequently reported difficulties with non-tariff barriers, rather than export subsidies. One interviewee, a migrant from China, dismissed any suggestion that non-tariff barriers in China might impede Australian processed food exports. He made the cryptic observation that there were informal ways around any barrier. Four of the more experienced Australian interviewees made similar, though more qualified remarks. It is probably the case that the penetrability of barriers depends to some extent on the mindset and the resourcefulness of the exporter. A conventional Australian business mindset is perhaps more likely than, say, a Chinese business mindset, to baulk at barriers.

The Australian Department of Foreign Affairs and Trade points out to exporters that it can take no action on some of the barriers identified by the firms; for example, some labelling requirements. This is because firms which manufacture in the foreign country concerned have to abide by the same labelling requirements.

Market information issues

In the survey and at interview, smaller companies were more likely to be concerned about market information issues than larger companies. Most of these smaller companies are less knowledgeable and experienced and had few resources to devote to export market development. The Focus Groups provided further insights into the extent of the issue of lack of market information — and the role governments play in trying to address these problems.

Generally, larger companies which are serious about exporting can and do deploy themselves the resources necessary to collect the detailed, practical information they need about foreign markets. Usually, they can afford to put time and resources into foreign markets, which is the only place where the practical information which is most important to exporters can be found. In most cases, they turn only occasionally to government for this type of assistance — generally for assistance of a quite specific kind.

On the other hand, smaller companies are less likely to have the financial or other resources, including management time, to solve the market information problem themselves. Often they cannot afford frequent visits to foreign markets or to pay for the less satisfactory alternatives. They turn to government agencies, such as Austrade, for assistance.

Most of the smaller firms had strong views about the market information issue. While they did not have a strong understanding of the role of government, almost without exception, they said that governments ought to help small firms solve the market information problem. A majority thought that fees for Austrade market information services were too high and did not always represent quality and value for money.

Many firms say that Austrade often does not provide what they need most, which is practical information about the markets, including price structures, competitor behaviour and other ‘transaction’ data.

Some firms considered that Austrade does not have sufficient staff with the commercial experience that would equip them to find the market information small exporters want. The firms say that Austrade is good at providing generic market data or local cultural and social profiles but not so good at hard transaction data and facilitating business negotiations on behalf of the Australian seller.

State agencies also provide export services. Overall, firms tended to rate export-related services provided by state governments more highly than Austrade services — although it should be noted that most state services are free of charge.

Competing in foreign markets

International competitiveness issues were discussed at considerable length with all but a few interviewees, and with the Focus Groups.

On **freight**, which was the impediment most frequently cited by survey respondents, a majority of the firms agreed that rates to Asia and elsewhere had come down rapidly and substantially in the last two or three years. Three or four noted that rates to some markets might have started to rise again, with improvements in Asian economies.

However, the interviews made it clear that generally the companies are less likely to be interested in the comparison between freight rates out of Australia now and three years ago. They are more likely to be interested in the comparison between what they pay now and what foreign competitors pay to get product to markets. Several referred to freight subsidies available to foreign competitors, particularly in the United States and Europe.

One firm, an Australian subsidiary of a foreign-owned dairy foods company, said that there was a 'freight barrier' beyond which freight costs rendered exports of liquid milk uncompetitive: this imaginary line was just west of the Middle East.

Only one firm mentioned inefficiencies on Australian wharves as an impediment to exporting. When asked, most companies said that the cost of getting 'boxes across wharves' was insignificant in the cost chain.

On the strength of the **foreign competition** (after freight, the issue mentioned most frequently by survey respondents) almost without exception interviewees outside the dairy industry said that they faced strong price competition in foreign markets, even where the competition was not subsidised. Interviewees and the Focus Groups generally attributed the strength of the foreign competition, where it was not related to export subsidies and other forms of government support, to economies of scale, lower labour costs, lower freight rates and more innovative technology, management and marketing. Several smaller firms and a small number of larger firms said it was due to a lack of, or the loss of, a manufacturing culture in Australia.

> *"I'm very worried about the future of our firm, say in 2–3 years time. The Asia melt-down weakened Asia, but the re-bound is already starting and that's what I'm worried about. For example, new equipment will be installed in Asia. If we don't act fast, we will miss the opportunity. The multinationals who have invested in Asia, they are 40–70 percent cheaper than us. I worry about how we are going to compete with them."*
>
> CEO, listed manufacturer

Three interviewees said they believed Australian governments did not see manufacturing as important to the welfare of Australia in the years ahead; the glamour service industries were the ones that governments were interested in fostering.

Domestic impediments and foreign barriers compared

Overall, survey respondents are significantly more likely to believe that domestic constraints are more serious impediments to exporting than tariff and non-tariff barriers.

Larger firms, particularly established exporters with high capacity utilisation ratios, are more likely to see things the other way: foreign protection and export subsidies are more significant impediments to exports than domestic constraints.

At interview, it was determined that the reason for this difference is mainly that larger firms that are established exporters focus on the foreign barriers more — and are therefore more likely in completing a mailed questionnaire to say that those barriers are more serious. At detailed discussions, most of these larger, established exporters agreed that the improvement of the domestic operating environment, including within the firms themselves, would be at least as likely to improve exports as would reducing foreign protection.

Government efforts to reduce tariff and non tariff barriers

During the interviews and at the Focus Groups, a majority of the more experienced exporters demonstrated a strong and legitimate interest in the Australian Government's efforts, in bilateral and multilateral forums, to reduce foreign tariff and non-tariff barriers and export subsidies. This interest crosses all sub-sectors of the industry and applies in all its major foreign markets.

However, there is a high degree of fatalism regarding outcomes. Furthermore, in the absence of confidence that barriers are about to be lowered, managers are focused on those things they believe can, or should, be changed: most of these are more immediately in their consciousness and relate to their own competitive environment.

"Tariff and non-tariff barriers are high, but the answer is not going to be in trying to bring them down. The answer is to build a global niche business."

Senior manager, large dairy company

Few owners or managers of firms displayed any detailed knowledge of negotiations in forums such as the WTO, APEC and bilaterally. Neither did they know much about the international and domestic political factors which are in play when ministers and senior officials devise strategies and tactics for negotiations and then face foreign counterparts across negotiating tables.

Nevertheless, more than one third of the firms expressed the view that the Australian public sector could do more in bilateral and multilateral forums to fight foreign protection and subsidies effectively. In some cases, firms referred to particular issues, such as Australia's efforts to open the rice market in Japan. In other cases, the criticisms were more general. Three companies complained that, until recently, processed food had not been given much attention in the GATT-WTO negotiations.

"A problem is the powerlessness — or uselessness — of the Australian Government and its slavish approach to the GATT and WTO. To the extent that it is doing a good job in the negotiations it is where it has a commodity focus. Until recently, it totally neglected processed food. Yet this is where the people are employed and incomes generated."

Experienced senior manager, regional-based exporter

It was apparent from the tenor of the comments that interviewees think the Government may not have the right negotiating strategies in place, that it underestimates the strength of its negotiating position and that it is less tough minded and resourceful than some foreign governments.

> *"Australian food exporters are really getting a work-over by the EU, through subsidised exports and there's no hope of relief, given how lame our negotiators are."*
>
> Experienced CEO, large exporter

Government support for processed food exporters

The firms interviewed or participating in the Focus Groups had limited knowledge and understanding of many federal government policies and programs designed to support exporters, including those in processed foods.

The interviewees were asked to name the government agencies which provided export assistance to their firm. They were then asked to comment on the effectiveness of the support provided by the one or two agencies they were able to name.

The agency most frequently mentioned by interviewees was Austrade. The program most frequently mentioned was the Export Market Development Grants Scheme (EMDG). Australian Quarantine Inspection Service (AQIS) was mentioned almost as frequently. Many firms also named state government departments of agriculture, industry and state development.

The EMDG scheme was generally praised though, as was to be expected, many firms which have been excluded complained about tightened eligibility criteria.

> *"When the turnover cap on EMDG was reduced, we had to cancel plans to go into a market with potential for $5 million annual sales — losing the three year New Markets Grant doubled our market entry costs."*
>
> Senior manager, beverage manufacturer

Firms demonstrated greater familiarity with programs run by state government agencies and programs set up to support the food industry. For example, *Food Victoria* and South Australia's *Food for the Future*, *Food Adelaide* and *The Business Centre* were well known by local firms and were generally regarded positively.

Only a relatively small number of firms volunteered or mentioned Supermarket to Asia (STA). There were no strong views either way about its effectiveness.

Small firms complained about the cost of AQIS' services. Many say that they should be provided free, as a resource for the industry in the public interest. Firms large and small complained that some of AQIS's rules and procedures were illogical or 'unbusiness-like' — and more stringent in some cases than the rules and procedures applied to imported food.

"I understand the reasons why AQIS takes its testing so seriously. And given some of the things other manufacturers do, probably for safety's sake every second batch of cheese should be tested. But it's a serious impediment to people like us trying to export speciality cheeses. I think the testing costs should be rebated if the batch is exported. And why should the standard for export be higher than for domestic sales or for imports?"

Proprietor, small speciality cheese maker

A few firms complained about conflicting food standards at the state level and about local standards which were significantly at variance with those which apply in some export markets. Some firms, generally medium and larger ones, referred to actions and policies of the Australian Competition and Consumer Commission (ACCC) which discourage the achievement of scale, which is such an important element in export competitiveness.

Accumulators

A number of firms that knew little about public sector agencies that support exporters were in fact exporting through trading companies and other intermediaries. Several of these intermediaries, the 'accumulators', were interviewed.

Accumulators are a repository of market information and international business skills. Where they act as principals in transactions they take a margin in return for accepting the costs and risks of export market development that manufacturers may not be able, or may not choose, to incur themselves. In other cases they operate as agents in return for a commission allowed by either the buyer or the seller. Whether they act as principals or as agents accumulators generate exports that often would not occur if left to manufacturers alone.

Even for established exporters, the accumulators play a useful role. They source small consignments from large companies and fill export orders that the large firms would not find cost effective. This builds market presence for the manufacturer with minimal risk.

They are playing a valuable role in generating exports that would not otherwise have occurred. Many feel, however, that the role they play in the Australian economy is misunderstood by the public sector.

2.5 THE CASE OF WINE

The Australian wine industry stands out as perhaps the nation's most successful highly processed food sub-sector competing strongly in foreign markets.

How did this situation come about?

The first vines were introduced in 1788, but it is not the long history of the industry in Australia that differentiates it from other sub-sectors, such as dairy and meat, which were started at least as early.

In recent years, the wine industry has attracted investors who have been prepared patiently to invest in innovation all along the value chain. The result is competitively priced, quality raw materials, and value adding which itself is world-competitive and which leads to regional and brand recognition with enormous product differentiation. Healthy regional clusters of producers and supporting industries and institutions enhance the overall competitiveness of the industry, which has done a good job of building horizontal links to related industries, such as tourism.

By world standards, Australia is not a large wine producer and domestic consumption is lower than in most other wine producing countries; nevertheless, industry exports in 1999–00 totalled over A$1 billion, more than 30 per cent of production.

Numerous factors contribute to wine's success relative to other sub-sectors:

- The geographical and climatological diversity of a continent allows a large number of grape varieties to be produced successfully and consistently, each with distinctive regional characteristics;
- Australia's environment is perceived as relatively eco-efficient and wine making practices 'safe';
- Investment in viticultural innovation, including in improving grape varieties and in mechanised growing and harvesting, means that quality grapes can be produced at costs which are world-competitive;
- The industry has not been hide-bound by tradition or unhelpful industry regulation;
- Skilled people have been attracted to the industry, and governments and the industry itself have invested in on-going education and skills development;
- In several regions, clusters of producers and ancillary industries, which co-operate as well as compete, have developed; and
- Most foreign investors have planned from the outset to export through established distribution networks in foreign countries.

For the past three decades, the reputation of the Australian wine industry and the acceptance of Australian wines in major foreign markets has been strengthening.[29] There are several well-established regional brands (for example Coonawarra, Barossa Valley, Margaret River) which have achieved global recognition. Individual labels are now significant global brands.

Several Australian producers are of world scale and totally global in outlook. They have invested heavily in production and distribution inside foreign markets and, in doing so, have reinforced their market positions as well as improved returns for their investments in viticultural and wine making technology. International marketing by individual firms, and the industry as a whole, has been well co-ordinated, innovative and effective.

One of the important lessons is the tiered marketing strategy. The first thing the industry had to do in each of the countries it targeted was to convince consumers that Australia was a wine country, one to which wine lovers should naturally look for quality products. This was necessary because French, Italian, Spanish and even Californian wines had dominated consumer perceptions in all the major markets for decades.[30]

Once that battle had been won, the industry challenge was to avoid confronting foreign consumers with a wave of ‘Australian wines’, all of which might be seen as ‘the same’. Primary points of differentiation were established: region and grape variety. In recent years, foreign consumers have been educated that, in Australia’s case also, certain varieties do noticeably better in certain regions, for example Cabernet sauvignon in the Coonawarra and Shiraz in McLaren Vale — as is the case with Burgundy (Chardonnay and Pinot Noir), Bordeaux (Cabernet) and Rhone (Shiraz).

The third level of differentiation is the quality and flavour of the wine in the bottle from individual producers. But without winning consumer attention on the first two levels of differentiation individual producer marketing would have been much more difficult.

What the Australian wine industry experience proves, above everything else, is that scale matters, even for a relatively insignificant slice of the world market. Australia’s four largest wine companies all rank in Rabobank’s index of the Top 20 Wine Companies globally.[31] But Australia produces only 2.3 per cent of world wine output.[32] The scale of the big players in the Australian industry has enabled the industry to hold a share of world trade (5 per cent) which is more than double its share of world output.[33] This experience suggests that building enterprise scale and industry critical mass ought to be a deliberate objective of government policy for the processed food industry.

---

29 The Economist, *The globe in a glass: a survey of wine*, December 18, 1999.

30 Note that Californian wines have a high reputation yet total exports are relatively modest in value terms: Southcorp’s exports, for example, are equivalent to 60 per cent of total Californian wine exports, according to David Combe, Vice-President, International, Southcorp.

31 The Economist, *op cit*.

32 The Economist, *op cit*.

33 The Economist, *op cit*.

3: CONCLUSIONS AND RECOMMENDATIONS

3.1. INDUSTRY COMPETITIVENESS

Exports of processed foods occur where there is strong foreign demand and it makes business sense to manufacture and ship the product from Australia.

Industry optimism is fueled by bullish demand forecasts that predict rising medium to long-term affluence in populous countries, especially in Asia, and rising concerns about the safety of northern hemisphere food. But Australia's ability to capture this demand is constrained by factors within Australian control which influence relative competitiveness in processed foods, as well as by external barriers which restrict access to markets.

Competitive value-adding and the value chain

The successful food processing firms know that it is **total** competitiveness along the value chain which determines whether they can export successfully. Total competitiveness depends on how creatively and cost-effectively firms augment raw materials, not just in processing and packaging, but also in quality, service, market positioning, channel development, promotion and brand development and support.

One early determinant of international competitiveness for firms is the price, quality, availability and reliability of the raw materials used in producing processed foods. Contrary to conventional wisdom, many raw materials do not confer much, if any, competitive advantage on Australian food processing firms. For some raw materials, domestic price support measures or commodity marketing structures focused on export markets either raise the price, limit the volume, or ration the quality of raw materials available to local value-adders.

As things stand, very little cost competitiveness is achieved in manufacturing, packaging, financing, freight and international marketing of processed food, since Australian firms achieve world benchmarks in few of these activities. More often than not, the more value added to raw materials by Australian food processors, the less price competitive they become on world markets.

There is room for improvement in the extent to which the industry practices 'through chain management' for export markets. Related to this, the industry's up-take of electronic commerce is slow. Competitors, particularly in the United States, are doing better.

Generally, the technology and equipment used in the industry derives from Western food traditions. Most of Australia's factories are ill-equipped to manufacture food in Asian traditions, which constitute the mainstream in markets to Australia's north.

Recommendations: Total Value Chain Competitiveness

1. *There must be stronger focus on creating functional awareness within the industry as a whole of the importance of competitiveness throughout the value chain, building on existing STA themes and programs such as the Food and Fibre Chains Program and the New Industries Development Program.*
2. *Systematic benchmarking of raw materials for the main sub-sectors — dairy, horticulture, grains and meat — should be initiated and used as a basis for setting priorities for public sector support and action. This should be followed by benchmarking of activities further along the value chain.*
3. *State and federal governments should continue their efforts to cause structural adjustment where this will reduce the cost and improve the quality and reliability of raw materials into factories. In the longer term, this will contribute to the prosperity of rural communities — by generating more exports of highly processed foods.*
4. *Linkages between the Australian food processing industry and food processing equipment manufacturers and food research institutes in Asia would assist it to deliver into the value chain products which are more attractive to distributors. Work needs to be undertaken to assist in creating or deepening these links.*

Innovation

Many Australian firms are succeeding in export markets by transcending price competition and developing highly differentiated products with ‘intrinsic value’ which do not need to compete on price and which command attractive margins in export markets.

Industry leaders and small entrepreneurial proprietors agree that investment in innovation in the food sector is a pre-requisite for product differentiation and the creation of intrinsic value.

Innovation can occur all along the value chain and take many forms: process, product and packaging improvement, clever new approaches to brand development and support and imaginative marketing and management of the supply chain. Firms find new ways to encapsulate the ‘value of values’ in their products; for example by promoting them, where appropriate, as ‘eco-efficient’, clean or safe.

A distinction needs to be drawn between conventional R&D — the ‘scientists in lab coats’ kind — and the practical, hands-on activity that goes on in many of the smaller firms doing well in export markets.

Conventional R&D, however, is declining. There is little R&D of a character or on a scale likely to generate leading-edge products which create new markets or enhance market penetration. There are probably fewer than a dozen firms in Australia with the internal resources to carry out R&D of this nature and the majority are subsidiaries of foreign multinational food companies. If these trends are not reversed, the competitiveness of the Australian food processing industry could decline and the growth of exports will be correspondingly limited.

Overall, the industry is not well informed about government programs aimed at supporting R&D. Neither is the industry effectively linked to the 'national innovation system'. The food science organisations are not succeeding in reaching many of the firms which should be using their services; more effort should be devoted to improving communication and marketing to the firms.

Recommendations: Innovation

5. *Improving the R&D and general innovation performance of firms in the processed foods industry should be given a high priority. As soon as possible, governments should convene a Summit on world-competitive R&D for processed foods. Senior business economists and food industry scientists, as well as industry leaders, should be invited. The aim of the summit should be to encourage R&D on a scale and of a technological and business sophistication such that Australia's highly processed foods could achieve a competitive edge in foreign markets.*

6. *In preparing for the Summit, the Government should commission an independent assessment of the potential of larger foreign-owned firms based in Australia to undertake more value-adding and to export more highly processed foods. On the basis of this assessment, the proposed Food Industry Council (see below) should present the larger foreign-owned firms with a range of potential commercial opportunities and a set of 'corporate citizenship challenges' aimed at stimulating more innovation and exporting.*

7. *Several other actions should be taken:*

   - *Federal and state R&D schemes should be reviewed to determine which are more likely to contribute to building a stronger processed food sector and increasing exports. Where necessary, the schemes should be improved and more effectively promoted to stronger, qualified firms.*
   - *There should be an audit of the more innovative smaller firms to devise new ways to motivate and reward the risk-takers and imagination builders.*
   - *A study should be commissioned of ways to ensure that better smaller firms are more effectively linked to the relevant parts of the 'national innovation system'.*
   - *Public sector agencies should re-double efforts to explain the significance of R&D and innovation in building a processed foods sector which is more competitive and better at exporting.*

3.2 CORPORATE CAPABILITY BUILDING

While there is a cadre of talented proprietors and managers with global business experience and perspectives and some highly entrepreneurial and innovative proprietors of smaller businesses, the industry acknowledges its weaknesses. Many of them relate to people, their skills, motivation, training and mindset. There are skills shortages in general management, product and process innovation, packaging design, e-commerce and export marketing.

Except among the larger companies, there is very little knowledge about the practical issues of strategic planning for export and, in the sector as a whole, a paucity of managers or staff with highly developed practical export skills.

Many firms export through trading companies or other intermediaries — 'accumulators'. The role played by 'accumulators' is under-valued and misunderstood by the industry as well as the public sector. Accumulators are a repository of export marketing skills and active market linkages.

Recommendations: Building Export Capabilities

8. *Through the Food Industry Council, a small group of industry leaders with practical export experience should be convened to advise on priorities and actions which could be taken to better promote corporate capability building. This group should comprise Australians with extensive experience in agrifood management outside Australia, innovative owners or managers of smaller enterprises and managers from other business cultures.*
9. *The advisory group should be given a brief to advise on programs or institutional service delivery so as to enhance information sharing, management skills development, technology assimilation capability and export skills in the industry.*
10. *To resource this group, a more detailed study of the skills gap in the sector should be undertaken to assess more precisely the range and level of skills needed by firms in different sub-sectors and with varying degrees of experience in exporting.*
11. *The role of 'accumulators' in developing the export potential of the food sector deserves specific attention. Their role in the food economy needs to be measured and given appropriate recognition.*
12. *A database of 'accumulators', including their services and the products and markets in which they specialise, should be compiled. Where appropriate, the Government should facilitate linkages between accumulators and small firms.*

3.3 ACCESS TO FOREIGN MARKETS AND EXPORT MARKET DEVELOPMENT

Access to markets

Few owners or managers of firms have detailed knowledge of international negotiations in forums such as the WTO, APEC and bilaterally. The industry nevertheless sees that it has a strong and legitimate interest in the Australian Government's efforts to reduce foreign tariff and non-tariff barriers and export subsidies. This interest crosses all sub-sectors of the industry and applies in all its major foreign markets.

There is a high degree of fatalism regarding outcomes. Much of the industry believes the Australian public sector could do more to fight foreign protection and subsidies effectively.

Recommendations: Market Access

13. *The Government needs to understand why firms are ambivalent about its market access efforts in multilateral and bilateral forums and to reflect this in the communication with the industry on trade policy issues. The lack of an outcome at the November 1999 WTO Seattle meeting presents the opportunity for a fresh formulation of strategy and tactics; leaders from the processed food sector should be involved in formulating a new approach.*

14. *The difficulties firms experience in collecting comprehensive and up-to-date information about the barriers they must contend with in foreign markets need to be recognised. Federal and state government agencies should more readily share information about foreign protection and export subsidies and make as much of it as possible available to firms and others who need it.*

15. *The STA-DFAT publication* **Food Exporters Guide** *is an important initiative. It should be kept as up-to-date as possible and widely distributed. Public sector agencies should promote the guide to food processing firms. There should be regular audits of the effectiveness and quality of the advice available through the channels promoted in the Guide.*

16. *The trade negotiation process would be more effectively informed and food exporters more readily convinced of the value of the Government's efforts on their behalf to the extent that it can provide effective intervention in the marketplace when individual exporters experience specific market access difficulties. A 'firefighter' function of the kind provided by DFAT's Market Access Facilitator should be recognised as a legitimate and valuable service to the Australian industry and resourced accordingly.*

INSTATE
PTY LTD

Government support for exporters

The industry is generally not well informed about federal government policies and programs, including those focused on processed foods and those designed to support exporters.

The agency with the highest profile is Austrade. It wins praise for the high standards of service provided by particular posts on particular occasions. The EMDG is regarded as a valuable tool in offsetting market development costs. But disappointment is expressed regarding the quality of information about foreign markets available through Austrade and the lack of hard-edged commercial experience and focus of some of its staff in foreign countries. A common perception is that Austrade is excessively concerned with cost-recovery.

Cost recovery was also raised as a concern in relation to AQIS services. Small firms, in particular, say these services should be provided free, as a resource for the industry in the national interest. Some of AQIS's rules and procedures are perceived to be more stringent than those applied to imported food. The perception often is of AQIS as a 'policeman' rather than an ally in the fight for better access to foreign markets.

Recommendations: Government Support for Exporters

17. *The cost recovery policies for Austrade do impact on the competitive position of Australian food exporters. These policies recover only a small proportion of the agency's costs but aggravate processed food exporters and, occasionally, deter firms from the export effort. These cost recovery policies should be reassessed and alternative means devised to supplement and ration its resources.*

18. *The cost recovery policies for AQIS also put Australian food exporters at a disadvantage compared with many foreign competitors. Firms do not generally perceive AQIS as helping them in market access negotiations; AQIS needs both to perform better for exporters — and to be seen to perform better. Recently, all AQIS programs have been reviewed, in consultation with the industry. Action taken as a result of the review should, as far as possible, reduce financial and other burdens on exporters and potential exporters.*

3.4 NATIONAL PRIORITIES, PURPOSE AND PRIDE

While Australia's exports of *unprocessed* food — and some niche processed foods — have grown and food manufacturers in the survey generally expressed optimism about export opportunities, the more experienced and globally-minded industry participants are not complacent about the real challenges of succeeding in export markets for *processed* foods. In terms of growth and market share Australia is already lagging other exporters of processed foods.

Despite reductions in tariff and other protection, the industry does not fully comprehend the extent of the challenge from foreign competitors, the gap between Australian and world best practice and the need for substantial cultural change.

There was general support for the conclusions of this study and for the major recommendations. In particular, there was strong support for the proposition that the industry should have a national champion. The industry has problems at home as well as difficulties in foreign markets. The firms agree that a national champion should address both — and the connections between them.

Recommendations: Priorities, Purpose, Pride

19. *The significance of the industry and a sober-minded assessment of the prospects for exports of highly processed foods reinforce the need for the highest possible level of national leadership and the need to build on the foundation represented by the establishment of the Supermarket to Asia Council.*

    The Supermarket to Asia Council should be re-formed as the Prime Minister's Food Industry Council with a much broader charter, covering both domestic and export-specific issues across the whole value chain. This would help build a wider constituency for the organisation and would also develop a global rather than a regional focus.

    The Food Industry Council should have five functions:

    - ***Industry champion:*** *Elevate community recognition of the importance of the processed food industry to the national economy and to exports. Promote a wider recognition of the challenges faced by the industry and a realistic set of expectations about its capabilities and likely export performance. Help justify a priority command on national resources, to address weaknesses and boost performance.*
    - ***Benchmarking:*** *Carry out systematic benchmarking along the value chain to identify where competitiveness lags international standards and where improvements must be made.*

- ***Competitiveness and innovation:*** *Encourage the industry to focus on competitiveness issues and innovation along the value chain. Advocate the removal of regulation, such as conflicting or confusing state-based hygiene standards, which militate against developing innovative products.*
- ***Corporate capability building:*** *Help build better managed, more innovative and more export-aware companies.*
- ***Market access and market development:*** *Encourage public sector agencies, state and federal, to communicate more deeply with the industry and respond more effectively to the industry's real weaknesses and needs as it confronts the export challenge.*

A Food Industry Council would encourage the industry to participate in the development of a national vision and a set of goals for the processed food sector — as Food Victoria and Food for the Future (South Australia) have done at the state level.

APPENDIX 1: INTERNATIONAL BENCHMARKING OF RAW MATERIALS

It was beyond the scope of the study to carry out benchmarking studies. Accordingly, the literature was surveyed to identify benchmarking that had already been done. Some useful studies and other information are summarised below.

Dairy

The cost of producing milk in Australia has been quite extensively benchmarked. In 1993, Australian production costs were below those of the major international milk producing countries with the exception of New Zealand. Australia, like New Zealand, is largely a seasonal, pasture-based milk producer without the high costs of feed and winter housing associated with cold climate production in the EU and midwestern US. There was considerable cost variation between the Australian states, with Victoria being the lowest cost state.[34]

Current cost comparisons indicate that Australia has since reduced costs to the level of New Zealand and may now be considered one of the lowest-cost milk producers in the world.[35] However, being cost competitive is only half the battle. Australia must also be *price* competitive with heavily supported milk in competing countries, most notably the EU. As with all sectors, price competitiveness is heavily influenced by exchange rate movements. A 1995 dairy industry export strategy report[36] identified a strong correlation between movements in the Trade Weighted Exchange Rate Index (TWI) and the value and volume of Australian dairy exports.

Meat

Controlled-nutrition meat production systems, such as pig and chicken meat and to a lesser extent feedlot beef production, better lend themselves to international benchmarking than primarily pasture-based meat production, such as beef and lamb.

Chicken Meat

A benchmarking study of the chicken meat industry in 1997[37] examined the contribution of live bird and processing costs in the production of ‘ready to cook’ whole chickens. Overall, Australian costs were found to be comparable to the EU but much higher than key poultry

34 Dairy Research and Development Corporation (DRDC), *International Competitiveness — Opportunities for the Australian Dairy Industry*, December 1993.

35 Senate Rural and Regional Affairs and Transport Reference Committee, *Deregulation of the Australian Dairy Industry*, 1999.

36 INSTATE Pty Ltd, *Strategic Export Market Review: Dairy Industry*, Dairy Research and Development Corporation (DRDC), June 1995.

37 INSTATE Pty Ltd and S G Heilbron Pty Ltd, *The Australian Chicken Meat Industry — International Benchmarking Study*, The Australian Chicken Meat Federation, May 1997.

exporting nations such as the US, Brazil, Thailand and China. The US was the lowest-cost producer in the world, mainly because live bird costs are lower. The US 'meat cost to the plant'[38] was 26 per cent lower than in Australia. The difference was found to be mainly due to higher chick and feed costs in Australia.

When Australia is compared to the average of all other countries, excluding the US, live bird costs were found to be broadly competitive. However, competitive advantage in poultry meat is gained by Brazil, Thailand and China through lower costs at the processing stage.

Pigmeat

Australian costs of pig production were estimated in 1993 to be higher than both the US and Canada.[39] However, the most efficient Australian producers are at or close to world cost levels.

A more recent study[40] highlighted the fact that there are discrepancies in methods of calculating the costs of production of pigmeat and that there is wide variation in costs between Australian producers. According to this report, the industry believes that the most efficient Australian producers are around world cost levels. The Pig Research and Development Corporation (PRDC) has commissioned an updated international benchmarking study, which is currently under way.

Beef

A 1997 meat industry report[41] highlighted the difficulties in comparing the productivity of pasture-based beef and lamb production systems internationally. Issues include differences in production systems and the level and methodology of data collection in different countries.

Raising beef in land-extensive systems in Australia is considered by many industry sources to be internationally competitive due to the low feed costs associated with extensive production systems in Australia. However, the international competitiveness of Australian grain-based feedlot systems suffers due to high feed grain costs.

Cattle feedlotting, as a controlled-nutrition industry more similar to pork and chicken production, better lends itself to productivity comparisons. However, the validity of comparisons such as weight gain and time on feed is questionable due to disparate quality objectives and factors such as price, quality and availability of grain and other feeds. One

38 Live cost adjusted for meat yield.

39 Industry Commission, *Pigs and Pigmeat*, Commonwealth of Australia, 1995, referencing: Boddington,M., "Global Opportunities", *Milne's Pork Journal*, Vol. 16, No. 12, December, 1994. Campbell, R., "$1.50 a Kilo to be Globally Competitive", *Milne's Pork Journal*, vol. 17, No. 4, 1995. Cresap, *The status of the Australian Pork Industry*, A report to the Australian Pork Corporation, Cresap, Melbourne, 1990.

40 Productivity Commission, *Pig and Pigmeat Industries: Safeguard Action Against Imports*, Inquiry Report No. 3, November 1998.

41 AACM International Pty Ltd, *Measurement of Meat Industry Productivity Growth*, Meat Research Corporation, 1997.

measure that is more directly comparable is labour productivity: compared with Australia, US feedlots have half the number of employees per 1,000 head of cattle.

A 1993 comparison[42] of animal and processing costs placed Australia on a par with the US but considerably behind New Zealand and Argentina. In terms of net cost of animal to the plant, Australia was ahead of Ireland and the US but behind New Zealand and Argentina. Australia was found to have the highest processing cost, attributed primarily to lower labour productivity at processing level. Again, exchange rate movements impact significantly on relative price competitiveness.

Horticulture

Australia is a high cost horticultural producer. According to a 1993 Horticultural Research and Development Corporation (HRDC) report:[43]

> *"The cost of raw product at the factory gate is significantly higher in Australia than with our competitors, hence less competitive. This is largely due to significantly greater economies of scale in the US and farm subsidisation in the EU."*

Australia's international competitors can be divided between high-cost producers — New Zealand and the United States are examples — and low-cost producers, such as Chile and Brazil. High-cost producers must overcome cost-price disadvantages through superior labour productivity, use of technology and non-cost factors such as innovation, quality, efficient marketing and promotion and branding in order to compete internationally.[44]

Grains

Desk research did not uncover any recent studies that benchmark the international competitiveness of Australian grain production.[45] However, it is generally accepted that Australian grain growers are among the most efficient in the world. A *prima facie* measure is that Australia trades in grain on international commodity markets against heavily subsidised exports from other countries.

Productivity gains over the last 20 years may not be sustainable, due to declining soil fertility and poorer structure attributable to more intensive cropping systems and a move away from mixed farming systems. A further threat to the competitiveness of Australian grain

42 Booz•Allen & Hamilton, *International Comparisons in the Beef Processing Industry*, Meat Research Corporation, 1993.

43 Horticultural Research and Development Corporation (HRDC), *International Benchmarking of Processing Vegetable Growing — Visit to USA and Europe*, April/May 1993.

44 Horticultural Policy Council, *Winning the Race — International Competitiveness in Australian Horticulture*, 1994.

45 One report (*The Wheat Industry*, Industries Assistance Commission, 1988) addresses competitiveness issues but does not attempt international benchmarking. According to the Productivity Commission this is their most recent report on the grains industry.

production may lie in the rapid adoption of genetically modified varieties in the US and Canada, two major competing countries.[46]

Sugar

Australia is a major exporter of raw sugar, although exports of refined sugar are minor. Queensland is the main sugar growing region and the source of all raw sugar exports.

It is difficult to effectively benchmark Australian competitiveness as many competitors are developing countries with volatile exchange rates.

Industry sources suggest Australia is currently competitive against Thailand, a major competitor in the region, but not against Brazil, due to significant currency devaluations in recent years. In terms of production efficiency, Australia is considered to be a world leader. Capital and labour productivity exceed that of competitors. However, a recent Productivity Commission report points out that growers could realise cost savings by increasing the scale of their operations.[47] Industry sources, however, suggest the aspiration to increase the scale of sugar growing operations is constrained by the high cost of employed Australian farm labour: the use of family farm labour is fundamental to competitive sugar production. State government regulation also limits the consolidation of existing holdings.

46 Sheales, T., *Grains Outlook to 2003–04*, ABARE, 1999.
47 Productivity Commission, *Submission to the Sugar Industry Review Working Party*, 1996.

APPENDIX 2: BIBLIOGRAPHY

A T Kearney Pro & Associates, *Australian Meat Processing — Improving Efficiency and Productivity*, September 1995.

AACM International Pty Limited, *Measurement of Meat Industry Productivity Growth*, Prepared for the Meat Research Corporation, 1997.

Agricultural Policy Unit, European Union, http://europa.eu.int/comm/dg01/trade8.htm

Agri-Food Council Secretariat, *Food Australia — Processed Food and Beverages Industry*, 3rd Ed., Department of Industry, Technology and Regional Development, Australia, 1993.

Australian Bureau of Statistics (ABS), *Innovation in Manufacturing*, Catalogue No. 8116.0, 1996–1997.

Australian Bureau of Statistics (ABS), *Manufacturing Industry Australia*, Catalogue No. 8221.0 and 8221.2, 1996–1997.

Australian Bureau of Statistics (ABS), *Research and Experimental Development, Businesses*, Catalogue No. 8104.0, 1997–98.

Australian Food and Grocery Council, *Australian Food*, Agrifood Media Pty Ltd & Australian Food and Grocery Council, 1999.

Barrett N.J., Wilkinson, I.F., "Export Stimulation: A Segmentation Study Of The Exporting Problems Of Australian Manufacturing Firms", *European Journal of Marketing*, 19(2), 1985.

Booz•Allen & Hamilton, *International Comparisons in the Beef Processing Industry*, Meat Research Corporation, 1993.

Booz•Allen & Hamilton, *Meat Processing Cost Comparison*, 1992.

Business Link, UK, www.businesslink.co.uk/services/abroad.htm

Canadian Customs and Revenue Agency, www.ccra-adrc.gc.ca

Canadian Department of Agriculture, http://atn-raie.agr.ca/public/tariffs-e.htm

Centre for Strategic Economic Studies and Strategic Industry Research Foundation, *Understanding the Benefits of R & D*, September 1996.

Charlebois, P. and Schimdhuber, J., Agricultural Trends and Issues to 2001, *The OECD Observer*, No. 205, April/May 1997.

Connor, J., Schiek, W., *Food Processing & Industrial Powerhouse in Transition*, 2nd Ed., John Wiley & Sons, 1997.

Cooke, P., Hastings, J., *New Industries: Imperative For Agriculture's Survival*, Theme 8, presented at the Regional Australia Summit, October 1999.

Dairy Research and Development Corporation (DRDC), *International Competitiveness — Opportunities for the Australian Dairy Industry*, December 1993.

Department of Foreign Affairs & Trade (DFAT), *Australian Survey of Business Needs for Trade Facilitation*, 1999.

Department of Foreign Affairs & Trade (DFAT), *Trade 1999: Outcomes and Objectives Statement*, 1999.

Department of Foreign Affairs and Trade (DFAT), *Composition of Trade Australia 1998*, 1998.

Department of Industry Science & Tourism, *Food Australia: Processed Food & Beverages Industry*, 4th Ed., December 1994.

Department of Primary Industries and Energy, *Competitive Performance: Australian Food Producers And Processors Achieving Success Through Innovative Business Strategies*, 1997.

Department of Trade & Industry, UK, www.dti.gov.uk/support/index.htm

The Economist, *The globe in a glass: a survey of wine*, 18 December 1999.

EU Market Access Database, http://mkaccdb.eu.int

Export Market Information Centre, United Kingdom, www.businesslink.co.uk/services/abroad/emic.htm

Export Promotion Councils, India, headq@apeda.delhi.nic.in

Food Regulation Review Committee, *Food: A Growth Industry, Report of the Food Regulation Review*, August 1998.

Food Victoria website, www.food.vic.gov.au

Food Victoria, *Bread Basket or Basket Case*, November 1993.

Food Victoria, *Food Industry Statement*, 1998

Food Victoria, *Natural Quality Produce of Australia*, 1998

Frank Small & Associates, "Benchmarking Australia's Agribusiness Performance — a quality perspective", *ABARE Outlook 96*, pp 147–150, 1996.

Gastin, D., "Wine exports — Asia in perspective", ABARE Outlook 98, pp 327–334, 1998.

Gastin, D., "Agribusiness: What do we need to do to compete in Asia?", ABARE Outlook 96, pp 151–159, 1996.

Glauber, J.W., "US Grains policy and the future direction of world grain trade", *ABARE Outlook 99*, pp 275–284, 1999.

GRM International Pty. Ltd, *Input Requirements for Cattle Feedlot Industry*, PDP Australia, Centre for International Economics, and Total Cattle Systems, February 1995.

H.M. Customs & Excise, www.uk.emb.gov.au

Heilbron, Dr S., Larkin J.T., *Corporate Strategies and Structures: Penetrating Asian Markets*, Rural Industries Research and Development Corporation (RIRDC), 1995.

Henderson, D. R., Handy, C. R. and Neff, S. A., *Globalization of the Processed Foods Market*, Agricultural Economic Report No. 742, Consumer Economics Division, Economic Research Service, US Department of Agriculture, September 1996.

Horticultural Policy Council, *Winning the Race — International Competitiveness in Australian Horticulture*, 1994.

Horticultural Research and Development Board, *International Benchmarking of Processing Vegetable Growing — Visit to USA and Europe*, 1993.

Industry Assistance Commission, *The Wheat Industry Report, No. 411*, 1988.

Industry Commission, *Meat Processing*, Commonwealth of Australia, 1994.

Industry Commission, *Pigs and Pigmeat*, Commonwealth of Australia, 1995.

Industry Commission, *Submission to the Sugar Industry Review Working Party*, Commonwealth of Australia, 1996.

INSTATE Pty Ltd, *Agribusiness & Processed Food Development in South East Asia*, Rural Industries Research and Development Corporation (RIRDC), 1993.

INSTATE Pty Ltd, *Asian Food in Australia: Getting a Bigger Bite*, Rural Industries Research and Development Corporation (RIRDC), 1994.

INSTATE Pty Ltd, *Food Market Channel Development in Japan and Korea*, Rural Industries Research and Development Corporation (RIRDC), 1997.

INSTATE Pty Ltd, *Strategic Export Market Review: Dairy Industry*, Dairy Research and Development Corporation (DRDC), 1995.

INSTATE Pty Ltd, *Supermarket & Retailing Infrastructure Development in Indonesia: Implications for Australian Agri-food Exports*, Rural Industries Research and Development Corporation (RIRDC), 1995.

INSTATE Pty Ltd, *The Australian Chicken Meat Industry — International Benchmarking Study*, Australian Chicken Meat Federation, 1997.

INSTATE Pty Ltd, *The Indian Processed Food Market: Tradition and Change*, Rural Industries Research and Development Corporation (RIRDC), 1998.

Instituto per Studi Ricerche e Informezioni sul Mecato Agricolo (ISMEA), *The European Agro-Food System and the Challenge of Global Competition*, June 1999.

International Agribusiness Management Association (IAMA), *Conference papers* 1999.

International Farm Comparison Network, *Comparison of Typical Dairy Farms Worldwide*, 1998.

International Trade Centre, UNCTAD/WTO, 1998.

International Trade Strategies Pty Ltd, *Expanding Processed Food Exports: Priorities and Strategies for Joint Action on Market Access by Government and Industry*, January 1997.

Japan External Trade Organisation (JETRO), www.jetro.go.jp/jp/e/index.html

Japan Tariff Association, www.kanzei.or.jp/english/

Kennedy, I., "Investing in Food: Recent Victorian experience, Regional Australia", *ABARE 99*, Additional papers, pp55–61, 1999.

Lewis, W., McCann, W., McLean, R. J., "What ails Australia?" *The McKinsey Quarterly 1996*, Volume 1, McKinsey Company, 1996.

Massey, M., "Sugar Producers Take on Selling Role", *Business Review Weekly (BRW)*, 15 October 1999.

McGrane, T., *Working Paper: Processed Foods: Trade and Investment Barriers to Australian Exporters in Key Markets*, 1 July 1998.

McKinsey & Company with McKinsey Global Institute, *Growth Platforms for a Competitive Australia: Incentives, Aspirations, Innovation*, 1995.

Ministry of Finance, Japan, www.mof.go.jp/~customs/conte-e.htm

National Australia Bank, *Finance of International Trade*, 8th Edition, 1996.

Peak Councils, *Submission to Livestock Industry Commission*, 1992.

Philp, Dr N., *Why Some Firms Successfully Export Processed Food and Beverages*, Rural Industries Research and Development Corporation (RIRDC), Research Paper 97/33, 1997.

The Productivity Commission, *Pig and Pigmeat Industries: Safeguard Action Against Imports*, Inquiry Report No. 3, November 1998.

The Productivity Commission, *Submission to the Sugar Industry Review Working Party*, 1996.

The Productivity Commission, www.pc.gov.au

Queensland Department of Primary Industries, *Food Service Markets in Thailand & Taiwan*, 1996.

Queensland Department of Primary Industries, *Queensland Value Chain Analysis: Beet, Sugar, Wheat, Horticulture*, Volumes 1–4, 1997.

Queensland Department of Primary Industries, Rural Industries Research and Development Corporation (RIRDC),
"An Overview of Food Retailing in East Asia", *Food Retail 2000 Series*, 1995.
"Food Retailing in Australia", *Food Retail 2000 Series*, 1995.
"Food Retailing in East Asia & Australia", *Food Retail 2000 Series*, 1995.

"Food Retailing in Japan", *Food Retail 2000 Series*, 1995.
"Food Retailing in Taiwan", *Food Retail 2000 Series*, 1995.
"Food Retailing in Thailand", *Food Retail 2000 Series*, 1995.

Queensland Department of Primary Industries, Rural Industries Research and Development Corporation (RIRDC),
"Global Trends", *Agribusiness 2000 Series*, 1994.
"Grain", *Agribusiness 2000 Series*, 1994.
"Horticulture", *Agribusiness 2000 Series*, 1994.
"Laos", *Agribusiness 2000 Series*, 1994.
"Malaysia", *Agribusiness 2000 Series*, 1994.
"Meat and Livestock", *Agribusiness 2000 Series*, 1994.

Rogers, M., "World Grains: An Australian Marketer's Perspective", *ABARE Outlook 99*, pp 269–274, 1999.

Schroder, B, Dr., "Food Processing in the Australian Economy", *Australian Food*, Agrifood Media Pty Ltd and Australian Food & Grocery Council, 1999.

Senate Rural and Regional Affairs and Transport Reference Committee, *Deregulation of the Australian Dairy Industry*, 1999.

Sheales T., "Grains Outlook to 2003–04", *ABARE Outlook 99*, pp 253–267, 1999.

Stayner, R., *Value adding to regional communities and farming industries*, Theme 7, presented at the Regional Australia Summit, October 1999.

Styles C., Ambler T., *Steps to Export Success*, PAN'AGRA Research Programme of London Business School, January 1997.

Supermarket to Asia Ltd,
China Food Market Profile, 1998.
Hong Kong Food Market Profile, 1998.
India Food Market Profile, 1998.
Japan Food Market Profile, 1998.
Thailand Food Market Profile, 1998
Vietnam Food Market Profile, 1998.

Supermarket to Asia Ltd, *Supermarket to Asia*, Vol 3, No. 2, June 1999.

Thorogood, L., "Expansion in the Sugar Industry — a Proserpine perspective", *ABARE Outlook 98*, pp 290–294, 1998.

US Customs Service, www.customs.treas.gov

US Department of Agriculture, *Economic Research Service*, www.econ.ag.gov

US Department of Agriculture, www.fas.usda.gov

US International Trade Commission, www.dataweb.usitc.gov/

US Universities' Agricultural Economics Papers Database, www.agecon.umn.edu

Viatte, G., *The Changing Role of the Food Industry: Greater Prosperity Through Global Markets*, Agriculture, Food and Fisheries, OECD, Paris, October 1997.

White D., *Capturing Opportunities in Asian Food Markets*, McKinsey & Company, 1992.

World Chambers Network, www.worldchambers.com