

BACKGROUND INFORMATION FOR THE RED MEAT SEMINAR BEING HELD ON 13th MARCH 2008

Competing on Price with Low Cost Suppliers:

At current farm-gate prices¹ the current industry set-up cannot continue to compete against the competitive economies of scale of other countries such as some Latin American nations. Given the trends of recent years and the predictions of future years, the industry should not assume that retail and farm-gate prices will rise sufficiently to cover the full costs of the production system and supply chains.

Another price-competing option for the Northern Irish industry is to include the opportunity to sell to other markets which may offer better returns (e.g. Italy for beef). However, the total costs of production in many cases still outweigh the potential returns from these markets and premium European markets are typically focused towards locally supplied products.

Bridging the Gap Between Loss and Profitability at the Farm Gate:

Currently, the beef and sheepmeat industries of Northern Ireland are making losses of over £200m per annum across the industry.

According to the RMTF², the production of beef from calves bred in a dairy herd is close to being profitable at current farm gate prices. It is anticipated that in the absence of any significant market price movement, there will be a decline in the suckler³-based beef herd and hill-sheep flock, and the strategy of the Task Force will seek to facilitate (through diversity and capability building programmes), the transition of producers who choose to leave the industry.

On the basis of the Task Force's market analysis conducted, it is predicted that adding *significant* premiums to the market price of beef in order to increase farm-gate price may not be achievable. This price premium would need to be between 75p-120p per kg of suckler beef and between 65p-80p per kg for dairy/beef-cross animals.

In bridging the gap between loss and profitability at the farm gate price, the Task Force has identified *six strategic strands* to build efficient supply chains in the dairy-origin beef and upland-lowland (grassland) sheep while monitoring and supporting through diversification and capability building programmes) the transition of producers who choose to leave the industry. These include

- Engaging with core customers;
- Investing in trialing new production models and supply chain systems;

¹ Farm-Gate price is defined as: A basic price with the "farm gate" as the pricing point, that is, the price of the product available at the farm, excluding any separately billed transport or delivery charge.

² <http://www.niredmeattaskforce.co.uk/>

³ Definition of suckler - An unweaned mammal, especially a suckling calf

- Aligning and sharpening industry incentives and building strong supply chain relationships;
- Focusing research capability building to drive competitiveness;
- Facilitating diversification and exit for those producers who wish to transition out of the industry;
- Implementing a transition programme;

It will be necessary for DARD⁴ to target funding and research towards supporting the development of commercially viable models of production and review the implications of an increasing number of producers choosing to leave the industry on existing diversification and exit (capability building) programmes along with broader social and environmental consequences.

Production Efficiencies:

There is currently a very highly fragmented producer base in Northern Ireland. About 20,000 farms are engaged in red meat production: over 80% of beef suckler farms have fewer than 30 cows and nearly 80% of beef finishing farms have fewer than 30 head of cattle. The ability of small producers to improve efficiency further and to benefit from economies of scale is constrained, and hence makes it difficult to introduce standardisation and adoption of best practice.

Of the Task Force producer respondents from interviews, over 40% are planning to reduce their herds to stem the losses. However, over the long term the fixed costs would be likely to remain high and the inefficiencies would eventually cause the need for producers to exit the industry. If the industry does not change course then a continuation or acceleration of the current decline is almost inevitable. This is likely to be prolonged and painful for producers who would continue to reduce herds and possibly sell off small amounts of land to keep going and supplement their cashflow.

The Task Force has invested a lot of effort in studying the viability of alternative models. The benchmark of these models would be whether the full costs of production could be covered. These costs of production include the cost of land, farmers' labour, and working capital. The conclusions that they came to from interviews and farm visits from expert panels are that:

- A dairy/beef-cross production model (e.g., for dairy/Aberdeen Angus crosses) may be viable with substantial cost efficiencies;
- Full-bred dairy animal production models may be viable;
- There is no prospect of creating an economically viable model of production for even the most efficient producer of suckler-origin beef;
- An economically viable model for upland-lowland (grassland) sheep may be attainable through increases in scale and/or reduction prices towards levels closer to those on mainland GB.

Unlike the poultry industry, processing is much more consolidated. The five largest processors account for approximately 90% of the red meat processed. Their operations are generally efficient and there has been a long tradition of successful trust built up with the large UK retailers. Northern Ireland currently has 12% share of this market. In terms of their efficiency, it is worth noting that their profit margins of around 5% are in line with industry benchmarks.

⁴ <http://www.dardni.gov.uk/>

Providing Additional Value to Produce:

The overall global demand and supply of beef and sheep meat is projected to increase at approximately 1.5% per annum over the next decade with global meat trade flows forecast to increase significantly. While the current market for Northern Irish red meat is within the Euro zone (particularly Western Europe), countries outside the EU and North America are expected to continue to grow in importance.

Due to the relaxation of current trade restrictions in recent years, the fierce competition from leading exporters such as South America may also become more intense. The UK continues to be the most attractive market for NI's red meat industry due to its size, geographic proximity, existing relationships with UK retailers and some consumer preference for locally produced meat products.

Premium lines, such as organic production are growing in popularity, however, they are still small in size and often premia are not based on production characteristics, but rather, they are based on subsequent processing, marketing or packaging), reducing the upside available to producers.

The major retailers that had been interviewed for the review have stated that, 'while they want to buy from a sustainable local supply, they (and their customers) are not prepared to cover the costs of an inefficient supply chain'.

Diversification Options:

In the current market, suckler-origin beef and hill sheep producers would be dramatically better off if they ceased production and instead used their share of this money to transition to retirement or diversify to other farming activities (e.g., cereals, dairy, and woodland) or exit the industry. If they were to exit the industry or diversify, their economics would be substantially improved by:

- Removing the costs of production (fixed and variable) associated with farming cattle and sheep for food production;
- Retaining the full value of their share of the Single Farm Payment, at least until 2013, by maintaining the land in good agricultural condition;
- Avoiding imputed costs from rentalised land and working capital, and instead creating the opportunity to generate revenue from land rental and interest receipts from the sale of the herd and/or flock and machinery;
- Creating the potential to earn wages from alternative employment