

Public hearing – Perth

Date: 22 April 2008

Time: 10.00am – 5.00pm

Address: Duxton Hotel
1 St George’s Terrace, Perth

Room: Hearing – Duxton Room 1 (Lower Lobby Level)

Witness	Submission	Summons
NOVO Foods Limited Mr Zelko Lendich Director Mr Ian Savenake National Sales and Marketing Manager	166	Summonsed & compelled to appear by ACCC
Mercer Mooney Produce Merchant Mr John Mercer	N/a	Summonsed & compelled to appear by ACCC
Pastoralists & Graziers Association of WA & WA Meat Industry Authority & WA Farmers (Red Meat Focus) Mr Tim D’Arcy Chairman (Pastoralist and Graziers) Mr Alex Burbury Policy Director – Pastoral & Livestock Ms Renata Paliskis-Bessell CEO (WA Meat Industry Authority) Mr Mike Norton President (WA Farmers) Mr John Fry Producer Mr Matt Camarri Producer	82	No
<i>1.30 – 2.30 Lunch</i>		

<p>West Australian Farmers (Grain Focus)</p> <p>Mr Julian Breheny Executive Officer</p> <p>Mr Derek Clauson Producer</p>	<p>106</p>	<p>No</p>
<p>Mrs Mac's Pty Limited</p> <p>Mr Iain Macgregor Managing Director</p> <p>Mr Rob Macgregor National Sales Director</p>	<p>152</p>	<p>Summoned & compelled to appear by ACCC</p>

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ABN 72 110 028 825



Level 10, MLC Court, 15 Adelaide St BRISBANE QLD 4000

PO Box 13038 George St Post Shop BRISBANE QLD 4003

Tel:1300 308 420 Fax:(07) 3503-1199

Email: orders@auscript.com.au Website: www.auscript.com.au

TRANSCRIPT OF PROCEEDINGS

AUSTRALIAN COMPETITION

AND CONSUMER COMMISSION

**MR GRAEME SAMUEL, Chairman
DR STEPHEN KING, Commissioner
MR JOHN MARTIN, Commissioner**

GROCERY PRICE INQUIRY HEARING

CONDUCTED AT: DUXTON HOTEL, PERTH

DATE: 10.00 AM, TUESDAY, 22 APRIL, 2008

THE CHAIRMAN: Good morning, everyone. My name is Graeme Samuel, I am the chairman of the Australian Competition and Consumer Commission and chair of this public inquiry into the competitiveness of retail prices for standard groceries. As
5 chair I welcome you all and declare this hearing opened. I am joined by Commissioner John Martin and Commissioner Stephen King who are the other two presiding members of this inquiry. This hearing is convened under part 7A of the Trade Practices Act. It is held pursuant to a request from the assistant treasurer, minister for competition policy and consumer affairs minister, Chris Bowen, which
10 was received by the ACCC on 22 January 2008.

Matters to be taken into consideration by the inquiry include, but are not restricted to, the current structure of the grocery industry at the supply, wholesale and retail levels including mergers and acquisitions by the national retailers. The nature of
15 competition at the supply, wholesale and retail levels of the grocery industry, the competitive position of small and independent retailers, the pricing practices of the national grocery retailers and representation of grocery price to consumers, factors influencing the pricing of inputs along with supply chains for standard grocery items, any impediments to efficient pricing of the inputs along the supply chain and, finally,
20 the effectiveness of the horticulture code of conduct and whether the inclusion of other major buyers, such as retailers, would improve the effectiveness of that code.

I note that we have received so far over 150 public submissions to the inquiry as well as confidential submissions. We will endeavour to take into account all of the
25 information that has been provided and we thank industry participants for the contributions that have been made. We understand that the competitiveness of retail grocery prices are of significant concern to all Australians. The purpose of these hearings is to give the ACCC an opportunity to investigate in detail the issues raised as part of the inquiry with industry participants. We are organising hearings
30 throughout Australia during April with several hearings occurring in Melbourne in May.

We wish to emphasise the many witnesses of these hearings are not attending voluntarily and have been summonsed to appear under section 95S of the
35 Trade Practices Act. In particular, I note that in general the ACCC has summonsed all supply companies. Therefore no conclusions can be drawn regarding a company's willingness to participate in the inquiry from the fact that a company is appearing at the hearings. Some of the material covered in the hearing sessions will be confidential and commercially sensitive and therefore parts of the hearings will
40 not be open to the public. Questioning will start in public but sessions will move into a confidential phase when the question moves onto confidential material relating to the witness.

We have to be able to investigate issues that are commercially sensitive to witnesses
45 without damaging the witness's competitive position and commercial relationships. We will be questioning organisations about their commercial relationships and about confidential documents that we have obtained for using our information gathering

and powers and clearly this cannot occur in public. In particular, where a witness has not made any submissions to the inquiry and has been summoned by the ACCC to attend these hearings we must be able to hear certain evidence in confidence. Transcript of the public parts of the hearing are placed on our website.

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The ACCC may disclose some aspects of the confidential components of the transcript sometime after the hearing, if we consider that some of the material should be in the public domain, but we will consult with the relevant witnesses before doing this. Where there are industry associations or representatives or organisations who are attending voluntarily, it is more likely most of the hearing sessions will be in public. In terms of procedural issues, all witnesses will have received a document that outlines how we intend to approach these hearings so I won't go through the procedural points in detail. I just wish to emphasise that, although we are not taking evidence under oath at this hearing, it is a serious offence to give false or misleading evidence to the ACCC.

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A transcript of the proceedings, apart from any proceedings held in private, will be made available on the ACCCs website. Now, as I mentioned, we recognise that some witnesses will be asked to give evidence that, if disclosed, would damage their competitive position or which may, for other reasons, be confidential. If a witness believes that a particular question or a series of questions are likely to require him or her to discuss such confidential information, the witness should indicate an objection to answering the question on that basis. I will then consider whether this inquiry should take evidence in private from that witness. I note that although the ACCC is not utilising external counsel at this hearing, witnesses will be questioned by the ACCCs internal lawyers who are Mr Damien O'Donovan and Ms Katherine Freeman sitting over there at the table.

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That concludes my preliminary remarks. I thank all of the witnesses that are attending the hearings, particularly those that have been summonsed to attend. I realise that you are busy people and attending these hearings can be a significant imposition on you and your organisation. Now, the first witnesses are from NOVO Foods Limited. I will ask Mr O'Donovan to take over from here.

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MR D. O'DONOVAN: All right, thank you for coming. Firstly, could you just announce, for the record, your name and the position in the company and the name of the company you are representing?

35

MR Z. LENDICH: Zelko Lendich, a director of NOVO Foods.

40

MR I. SAVENACK: Ian Savenacke, national sales and marketing manager, NOVO Foods.

MR O'DONOVAN: Have you been summonsed to appear here today?

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MR LENDICH: We have, yes.

MR O'DONOVAN: And can you just confirm that you understand that it is an offence under the criminal code to give evidence at this inquiry that you know to be false or misleading or which omits any matter or thing without which the evidence is misleading?

5

MR LENDICH: Yes.

MR O'DONOVAN: Yes, thank you. All right, can you just state, firstly, what NOVO Foods is, how it originated and what it currently does?

10

MR LENDICH: NOVO Foods was basically formed in, I think, 1999. Essentially, it was formed for two major reasons. In response to national retailers moving towards, I suppose, national tendering for supermarket business and also to try and provide some assistance to some of the smaller members in relation to buying, packaging and other sort of inputs into the production process. Basically, it has remained relatively similar in that intervening period. Initially there were, I think, four joint venture partners and there's four now. During the period Farm Pride Foods joined sometime after the initial inception and so there is now, essentially, four joint venture partners. The Western Australian company West Coast Eggs, Farm Pride Foods in Victoria and New South Wales, Pure Foods in Tasmania and Southern Egg in South Australia.

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THE CHAIRMAN: Right, so has Golden Eggs dropped out of the arrangement.

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MR LENDICH: No. Well, Golden Eggs is, sort of, the trading name of, what is now, West Coast Eggs. So it is basically in the transition from being, I suppose, a regulated environment in the Western Australian marketplace with the old Egg Board. It has moved to, essentially, a deregulated environment and West Coast Eggs is wholly owned by a major farmer group in Western Australia.

30

THE CHAIRMAN: Okay, so in terms of the functions that NOVO actually provides. Does it actually acquire packaging and those sorts of things on behalf of or just simply acts as a negotiating agent for those.

35

MR LENDICH: Essentially, it tries to act as a negotiating agent. Over the years, depending upon who we have been able to negotiate with, the packaging industry has changed rather dramatically over the last couple of years. We have gone from, essentially, being able to buy from three packaging companies, one in Malaysia and two in Australia, down to, essentially, one packaging company that operates locally in Australia. That has placed a fair bit of strain generally on packaging requirements of egg farmers and we have had to try and find alternative avenues for packaging to the extent that we have had to actually start our own packaging operation in Australia.

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THE CHAIRMAN: Has that impacted on the price for which eggs can be sold?

MR LENDICH: It probably has marginally. There was a period of time where some of the joint venture partners couldn't get access to packaging locally and had to go internationally to get packaging. That led to a number of issues in relation to both cash flow and price of packaging to be sourced from international sources but, in
5 general I suppose, it has probably meant that packaging has gone up but I'm not sure that it has been excessively difficult. I mean, there had been some influence during the first couple of years where I think the fact that there was one supplier meant that there was a bit of price pressure. I think now it is probably more the case that the competition from packaging coming in from Asia has meant that, I think, pricing has
10 been relatively competitive.

THE CHAIRMAN: At the other end of the process, you negotiate on behalf of the joint venture parties with the major supermarkets and McDonalds. Is that correct?

15 MR LENDICH: That's correct.

THE CHAIRMAN: Is that in relation to the supply of their branded eggs as well as the home brand or the house brand eggs?

20 MR LENDICH: Yes.

THE CHAIRMAN: Firstly, if we could start with the branded eggs, can you explain how you go about negotiating supply to the major supermarkets first?

25 MR LENDICH: Well, essentially we have a range of eggs we sell through the major supermarkets. They have regular range reviews in relation to whether we stay ranged or not, and we put up proposals in relation to wanting to list new products, they evaluate those proposals, and determine a planogram, so to speak, for each store, or sometimes it's across all stores, other times it's not. That becomes then,
30 essentially, our branded exposure nationally in each state.

MR O'DONOVAN: Right. For example, eggs grown in Western Australia, they are all sold in WA stores for the major supermarkets or do they sometimes ship them to different states?
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MR LENDICH: Well, on the whole, you try to move eggs as little as possible. It's expensive and you tend to break them. So in many respects, I suppose, NOVOs philosophy is that we like to have farms and packing operations close to the end market, so hence we tend to supply locally and move eggs very little. So if there's a
40 bit of an imbalance of supply between some of the joint venture partners, we may help each other by moving eggs between the joint venture partners on a sort of an ad hoc short-term basis, but in general, most of the eggs that are actually grown in each state are supplied to the retailers in that state.

45 MR O'DONOVAN: From the retailers' point of view, that they – when they're conducting a range review, there are alternative egg suppliers to the ones NOVO

represents, who are able to – who they're able to, I suppose, leverage price reductions through?

5 MR LENDICH: Yes, they get submissions from another three or four competitors, and they've evaluate, I suppose, what's selling, what isn't selling, and what their plans are in relation to the category, and on that basis, they will determine what is ranged and what isn't.

10 MR O'DONOVAN: Okay. In terms of the supply of branded eggs, do supermarkets have a preference to just offering one supplier of branded eggs? Do you ever get completely delisted or do they provide a range of branded eggs?

15 MR SAVENAKE: There's normally a choice, there's usually a couple of brands in each state.

MR O'DONOVAN: Right.

MR SAVENAKE: So there is a choice for the consumer.

20 MR O'DONOVAN: Okay. But is it possible at a range review that for a period, your, say, farm price eggs won't be represented at all on a Coles or a Woolworths shelf?

25 MR SAVENAKE: Potentially, yes, if they're not performing and not selling, then there's the potential to be delisted.

MR O'DONOVAN: Right, and the other wholesale - the other egg suppliers are capable of meeting that – the demand?

30 MR SAVENAKE: Potentially, yes.

35 MR LENDICH: In most categories, everybody offers a full range. There is some slight differences in relation to some of the very small specialty products that – all competitors won't have the range, but in general, in the mainstream of eggs, each competitor can usually offer an alternative or offer the same product.

40 MR O'DONOVAN: Okay. In terms of the companies that you represent, are they fully vertically integrated, or is there a level of supply below them where they're dealing with individual egg producers?

45 MR LENDICH: It probably varies a little bit. In most instances, there's a high degree of vertical integration. You know, in Western Australia, it's probably relatively high. Let's say, it's probably, you know, in the high 90s. Probably that comes from internally. In South Australia, where they're having the transition between phasing out the old cage infrastructure and putting in place new farms, they've had some issues with getting permits and financing etcetera, so for a period of time probably more eggs are being supplied into South Australia than would

necessarily be the case. On the east coast, it's, you know, usually a sort of a 75 per cent internal, 25 per cent from outside farmers coming into the system. So it varies based on, I suppose, the balance that each particular joint venture partner would like to have in relation to what they provide internally and what they source externally.

5

MR O'DONOVAN: Right. So in terms of that egg supply market to the producer, for want of a better word, there always remain a choice for the egg company of either in house production or going out to, I suppose, a wholesale market for eggs.

10 MR LENDICH: I suppose it depends on how tight egg supply is generally. One of the major drivers of behaviour and certainly price in the egg market is the overall supply and demand. So the market sort of cyclical nature that occurs in agricultural cycles, it's probably been exacerbated over the last, probably, three or four years, due to the changes in cage regulation, so during the period where farmers are phasing in
15 new infrastructure, there's still a high degree of old infrastructure around, and still not being phased out, been some issues, I think, with government acting a bit slowly in relation to legislation, and that means there's excess capacity in the system, which essentially means that if prices are high for a period of time, farmers will tend to put in more birds, and then because of the lag effect, you know, six to nine months later,
20 there's likely to be a lot of eggs on the market, and that will depress prices, force people to kill birds etcetera, and so it will go through a cyclical movement over a sort of about, you know, two or three year cycle, and that will, to a large extent, be a major influence on pricing, and of course, the availability of eggs.

25 So if we're in a tight period, you may not be able to get eggs easily from outside if you're not vertically integrated, in order to supply your customers and hence every company makes a decision on what degree it wants to depend on external supply versus internal in relation to its own customers, and so, often, certainly, we have a scenario where – because of probably large part of our supply is locked into long
30 term supply contracts with Coles or Woolworths or somebody else, we make sure that's covered internally, and then we can buy in to the extent that we supply other customers where it's a little less structured and not contracted in. So it's hard to expose oneself to being fixed on – in terms of your supply contracts, the customers, and being flexible in relation to your egg supply, because what you might have to
35 pay for it, in order to get it, could be very high.

MR O'DONOVAN: In terms of this – the cyclical nature of supply, that presumably produces quite a bit of volatility in wholesale supply market?

40 MR LENDICH: Yes, it can do. I mean, I think the industry has gone through probably a couple of pretty major surplus periods, and prices have been very depressed, and it's a lot of pain in the industry, essentially, I think. That's probably no secret if you have a look at the public accounts of one of our joint venture partners, Farm Pride Foods. It's been less than satisfactory return of shareholders
45 over the last five or six years. You know, highly driven by both the level of competition in the industry, it's a very highly competitive industry, and the sort of cyclical nature in relation to supply and demand.

MR O'DONOVAN: Okay. From your observation, is this volatility in wholesale pricing reflected in the retail pricing?

5 MR LENDICH: Probably not the same degree. I mean, to some extent what drives
our prices to retailers is obviously a combination of both supply and demand and the
cost of our factor inputs. Over the last probably three or four years, since probably
'05/'06 to now, the price of grain has got up by, you know, in some cases, up to 200
per cent. So wheat was trading at say, you know, 170, 180 dollars a tonne back in
10 '05/'06, it's now, you know, in the 440s, 450s and has gone as high as 500. So that's
a massive increase in the cost of grain. Grain is a very significant factor in the
production costs of the farm produced egg. It's sort of 60 to 70 per cent of your
actual variable cost. So obviously that's had a major influence on us wanting,
obviously, more for our egg from retailers, and then the retailers, I presume, have
15 their own competitive situation in relation to other retailers in terms of the margins
they put on and how competitive that is at the retail customer end. But obviously the
cyclicality and supply and demand and our own sort of high input costs will have an
input – will have a – with a starting base of the prices which we submit to them.

MR O'DONOVAN: Sure. But in the circumstances where you're trying to sell a
20 branded egg in a product – in a market where there's a big oversupply of eggs,
presumably your prices have to go down at the wholesale level?

MR LENDICH: Yes.

25 MR SAVENAKE: Normally you have a fixed price on your – with the
supermarkets for a period and you promote, in terms of the price reductions you
have, promotionals, catalogue promos in the stores. So that probably is the valve, if
you like to up and down of a price to reflect supply and demand.

30 MR O'DONOVAN: Okay. So even on a branded egg the price is fixed for a period
for the supply. There's not just a published wholesale price.

MR SAVENAKE: Well, there's a published wholesale price, if you like, to Coles
and Woolies.

35 MR O'DONOVAN: Yes, but not to other retailers?

MR SAVENAKE: Yes, sorry, to other retailers as well, yes.

40 MR LENDICH: We can obviously vary that price, with notice and with justification
in relation to the retailers, but what they actually have is the final price to customers
is obviously their prerogative.

45 MR O'DONOVAN: Yes, but in circumstances where you've found yourself in a
market where you've got an over supply of eggs, generally speaking will that impact
on the wholesale price so there'll be across the board reduction or will there be an
attempt to drive demand through specials?

MR SAVANAKE: Probably the latter.

MR LENDICH: Yes.

5 MR O'DONOVAN: Right.

MR LENDICH: What will happen in the sense of what happened the last couple of times is that for a period of time because people aren't sure how long the surplus will last you tend to lower your box market price, so that, you know, given that eggs have
10 got a certain shelf life you can't store them long, you need to get rid of them and so in the initial stages there'll be a reduction in price outside in the marketplace in the sort of non-supermarket marketplace, that has an influence, obviously on what happens in supermarkets eventually and the question really is how long will the surplus last and if it starts to be a protracted period of time then the normal thing that
15 the industry will do is kill birds to diminish supply, because essentially you're, you know, giving away egg at below cost, in many cases in the box market.

You can only do that for a short period of time before it has to – before it starts to become a significant issue and you tend to cull back your bird flock to reduce the
20 supply of eggs and then some people will not order new birds, depending on how difficult it is, so what you will tend to find is that during a major surplus it'll have a major dislocation on the industry to the extent that, you know, 12 months later there'll be a shortage, because people have taken a whole bunch of actions during that time, which will have implications down the track in relation to both the number
25 of birds in the system and hence the supply of eggs.

MR O'DONOVAN: Right. So an over supply of eggs at the wholesale level won't necessarily have an immediate impact on retail pricing or even the price at which
30 supermarkets are supplied - - -

MR SAVANAKE: Probably increases the frequency of promotions. So rather than doing it once every six to eight weeks you may be doing it every second week to just move that extra volume.

35 MR O'DONOVAN: Yes, and when you agree a promotion with the supermarkets, you're effectively agreeing to subsidise a reduction in the retail price. Is that right?

MR LENDICH: Yes.

40 MR O'DONOVAN: And it's more or less a dollar for dollar direct impact?

MR LENDICH: Yes.

MR O'DONOVAN: Yes, okay. So the consumers will benefit from any – there
45 will be a direct flow through to consumers?

MR LENDICH: Yes, 10 cents off will be reflected in 10 cents off at retail.

MR O'DONOVAN: Right, okay. All right, so then – and in terms of the supply terms, we may have to go into this in the confidential session, but in terms of supply terms, are there differences between supply to Coles, Woolworths, Franklins, or ALDI, or firstly, the first question, do you supply ALDI at all? Does NOVO have
5 any arrangements with ALDI that they can speak of?

MR LENDICH: We do.

MR SAVENAKE: NOVO doesn't, but the joint venture partners individually
10 supply ALDI.

MR O'DONOVAN: Okay and are there differences in the supply terms between Coles, Woolworths, independent supermarkets, Franklins and ALDI?

15 MR SAVENAKE: I mean, they're similar, but there will always be difference in structures, percentages of rebates and DC allowances, but in principle they're very similar.

MR O'DONOVAN: Right, okay. If want to go into specifics, is that a confidential
20 matter that should be done in closed session?

MR LENDICH: Yes, that would be our preference.

MR O'DONOVAN: Sure, yes. Okay, well, then I was – wanted them to ask you
25 about generics or house brand eggs and how those contracts are run. Now, in terms of how the contracts are run is that something you're happy to talk about publicly?

MR LENDICH: In general terms, yes.

30 MR O'DONOVAN: General terms, sure, okay. So and you – well, firstly you represent your joint venture parties in the negotiations for those contracts. Is that right?

MR SAVANAKE: Yes.
35

MR LENDICH: Yes.

MR O'DONOVAN: Okay, can you just then describe briefly how the supermarkets
40 will run a tender for a supply of a house brand egg?

MR SAVENAKE: They'll issue a supply document usually with, you know, some volumes – estimated volumes that they're going to sell over the year of the different varieties and it's probably a two month process where it's issued out to the market and you have the opportunity to either bid by states, by products, by region. For
45 example some of the bigger states, Victoria and New South Wales for Woolies are divided into regions so, you know, you couldn't supply the whole state potentially, so you actually bid for certain regions and certain products.

MR O'DONOVAN: Okay and those prices that you bid for will then be fixed for a 12-month or two year period depending on the - - -

5 MR SAVENAKE: 12 month, yes.

MR LENDICH: For the period of the contract.

MR SAVENAKE: Yes.

10 MR LENDICH: It has sometimes varied, but generally it's 12 months, yes.

MR O'DONOVAN: Okay and then in preparing those tenders are you primarily going to focus on a cost plus – working out your tender price on a cost plus basis or would you look at supply conditions in the market or - - -

15

MR LENDICH: I'd prefer to answer that in confidence if we can.

MR O'DONOVAN: Sure.

20 MR LENDICH: Thank you.

MR O'DONOVAN: Okay, all right. Now, in terms of the overall egg market our – it's been put to us that the retail end of the egg market represents only something like half of the total consumption of fresh eggs, is that consistent – would that accord with your views on the break up of where fresh eggs end up?

25

MR SAVENAKE: So you're including food service and - - -

MR O'DONOVAN: Yes.

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MR LENDICH: It's probably close. I mean, it's very hard to estimate, I think one of the critical issues with certainly in my experience with egg industries that the data is often very wrong, outdated ABS stats are certainly – probably not attuned to what's happening really in the industry in relation to how they present information and data. So sometimes statistics that are based on ABS stats have some issues, but, you know, it's really – there's not much else we have, but certainly I'd say it will be somewhere in the range of, you know 40 to 50 per cent.

35

MR O'DONOVAN: Yes, okay, as in you think that food service might be more than half the market?

40

MR LENDICH: Well, I'd say that it's 40 to 50 per cent in the major supermarkets, so, you know, sort of, I suppose the more national supermarkets, if you count - - -

45 MR O'DONOVAN: Is that just Coles and Woolworths or is that also including IGA?

MR LENDICH: I think probably not all of IGA, but sort of some elements of the sort of central pooling part of IGA, there's a lot of IGA independents that get supplied directly without going through the central system. There are lots of smaller operators, so I would say if you included the major chains like ALDI and Franklins, parts of IGA and Coles and Woolworths should be in that sort of 40/50 per cent range.

MR O'DONOVAN: Okay and then is that 50 per cent that's in food service is that widely dispersed through various customers or is someone like a McDonalds an enormous proportion of that remaining 50 per cent?

MR LENDICH: I think it's pretty widely dispersed. I don't think any one player would have a very large part of that at all.

MR O'DONOVAN: Sure and is there a reasonably close relationship between the price that you get for an egg that's sold into the food service part of the industry as opposed to the retail part of the industry? Or is there a very distinctive retail egg market?

MR LENDICH: Not really. I mean, I think it's probably difficult to classify it as one or the other, because essentially you go through what I believe is range of – you know, IGA and some of the other supermarkets and some of the other larger food service companies operate probably on contracts and on a similar basis as Coles and Woolworths and some of the majors, so it's a grey area where you don't go straight from, you know, a variable price on a day to – in a 12-month contract, it sort of varies all the way through to I suppose the only daily price you'd get is when you're selling the eggs at one of the markets, you know, either at Sydney or Melbourne or Perth markets, where the eggs are cleared on the day.

Otherwise there are a variety of arrangements that could range from, you know, a month, to three months, even to 12 months or longer term. So you know, I think prices will vary based on whatever the supply and demand factors are, given those sort of timing constraints, so you may have to enter into a one month or a two month agreement with somebody at a certain price, rather than it being, you know, daily and/or annually.

MR O'DONOVAN: Right. But there is a functional wholesale market through which, I suppose, egg producers can clear their - - -

MR SAVENAKE: Through the fruit and veg wholesale markets probably in each state.

MR O'DONOVAN: Yes, all right. Is there a reasonable correlation between the daily wholesale price and all the other prices for eggs in the market? As in does it effectively put a control on movements?

MR LENDICH: Well, not always but, I mean, I think it's really a question of lag. So you know, there may be a short term imbalance. Often it's an imbalance in a particular grade of egg rather than being eggs generally so there may be a lot of smaller eggs come on the market at a particular time and will be cleared at a lower price and when they're cleared, it goes back to a more normal scenario. You know, if there's a persistently low price in the box market that will then filter through to other markets over a period of time as, you know, renewal of contracts and agreements comes up there'll be, you know, obviously a downward pressure or an upward pressure.

10 I mean, there's been many instances where the box market price has been higher than the supermarket price, where in fact there's a shortage of eggs and you actually can get a higher return outside the supermarket sector. So it's very much supply and demand driven and, you know, can cycle relatively quickly, depending upon what's happening in the marketplace.

MR O'DONOVAN: Right. If you find yourself in a circumstance where the wholesale markets are showing higher prices than the prices you're getting from a supermarket and there's a range review, does that provide you with, I suppose, an opportunity to improve the terms you have against the supermarket?

MR LENDICH: Not – I mean, the range review's on the branded area and so it's really a question of what are you offering in terms of product as well as price. So you know - - -

MR SAVENAKE: Competition from other suppliers would probably keep that in check.

MR LENDICH: Yes. Because you're looking a bit longer term in relation to branded product and given that it's been – you know, there's been a pretty tremendous change in the balance between private label and branded over a period of time, you know, there's a strong, I suppose, need to retain some branded influence and so we're usually, you know, fairly careful about pricing and retaining branded product.

MR O'DONOVAN: Okay. The other effect we're interested in is egg powder which I understand is a product that can be exported and is internationally traded. Is that right?

MR LENDICH: That's correct.

MR O'DONOVAN: Okay. Does the presence of it as an available option, does it exert an influence on the pricing of egg? Like, if it moves up will generally the price of eggs, shell eggs, sold domestically move as well?

MR LENDICH: Probably not. I think that the major influence in relation to the powder market is really on, I suppose, the sort of processed egg market so the pulp

market. In Australia, in general, product egg has been viewed as a by-product. So essentially, it's the seconds quality eggs that, you know, can't be put into the retail environment that are then separated off and put into the product market and essentially, some are separated into – so they're white or yolk, and other that can't be separated is left as whole egg. Then it's either sold as a fresh whole egg, a frozen product so fresh, frozen and then powder. So essentially, I suppose, Australia is a relatively high cost country in relation to producing processed egg. We can't compete very easily with America or India, Brazil and the EU, depending on the major exporters of powder.

10 So what will happen in a sense is that the large biscuit and cake manufacturers, the Arnotts and those sort of companies, will have an understanding of the international powder market and to the extent that they can substitute powder for local whole or fresh egg, they will do that. Depending on its availability and its price, it will have an influence on the pricing of our processed eggs. When we're selling egg white or yolk or whole egg, whether it's fresh or frozen, into the local market, that'll – the pricing of that will be somewhat influenced by the powder market and will also influence the degree to which that manufacturer can substitute between the two. So I think that's really where the major influences lie rather than actually back into the shell egg market.

Only really during a surplus where you might put a lot of first quality egg into the product plants, there'll be then a surplus of product egg in the market and that price of that will then, you know, obviously go down so that there's an influence there. Right now, for instance, I think international powder stocks are probably at all time lows and suddenly, we're probably more competitive locally in relation to our powder but that's not a very normal occurrence.

MR O'DONOVAN: Right. So would it be fair to say that the normal prevailing condition is that egg powder puts an absolute flaw but a very unattractive flaw on the market price for eggs?

MR LENDICH: Yes. I mean, definitely it influences the degree to which you actually put eggs in to a processed form in the sense that, you know, we can't compete effectively with imports under normal circumstances. So you wouldn't actually produce excess egg to put into the product egg and you'd be blending a little bit of first quality and mostly second quality egg into that market, otherwise you probably couldn't compete and in many instances, the major manufacturers would go outside that into imported powder.

MR O'DONOVAN: So at the point in time at which you are negotiating with Coles or Woolworths, obviously you've got other domestic competitors but does their I suppose 25 per cent, roughly, or probably 20 per cent of the total egg market - it seems Coles and Woolworths have a share something like 20 per cent each of the total fresh eggs sold in Australia go through Coles and Woolworths – does that deliver them a degree of market power that means that they take more of the margins than any other customer is able to obtain?

MR LENDICH: It's a very difficult – essentially, I suppose, as private label has grown and you configure your production system for a particular size of contract with either Coles or Woolworths, when it gets up to a tender period there's a natural inclination to obviously try to retain – at least retain or possibly grow your business.

5 In those circumstances, you have to price competitively and as the size of the potential contract increases so, you know, the risk of losing it is higher and, you know, that's really a normal competitive behaviour. I don't think it's anything to do with Coles and Woolworths. I've been in other industries and I think, you know, the same sort of scenario applies really, where you want to retain volume. You've got

10 economies of scale in retaining that volume and usually you'll price, you know, fairly aggressively and maintain, you know, what margins you think you can afford.

MR O'DONOVAN: Given the level of concentration in the retail market where I think you've estimated, would it be, that 70 per cent of retail egg sales would go

15 through Coles and Woolworths. Is that - - -

MR SAVENAKE: I think it was 70 per cent for Coles, Woollies, Franklins, ALDI, Metcash was just my guesstimate of that.

20 MR O'DONOVAN: Right, okay. So of that 70 per cent how much do you think would be made up of Coles and Woolworths in terms of egg sales?

MR SAVANAKE: Say 45. Metcash is just an unknown. The Metcash private label goes through the warehouse but any other brands are supplied by back yard farmers

25 and go direct to store, so there's no data capture of any of that scan data.

MR DONOVAN: Right. Okay. So the notion that 80 per cent of all eggs sold through retail would go through a Coles or Woolworths; you wouldn't agree that the market share is that high for those two? No? You think it might be as low as 45 per

30 cent of all eggs sold at retail would go through Coles and Woolworths?

MR LENDICH: I think it would be higher than that but it's hard to say just how much higher.

35 MR DONOVAN: Sure. All right. From your observation, is the retail market in eggs competitive? Do consumers get a competitively priced egg?

MR LENDICH: I think it's a very competitive market. I think if you looked at the price of eggs, you know, over the last even 10 or 20 years compared to even just the

40 CPI or any other indicator, I think we're probably going backwards in the sense that I think there's really quite a high level of competition probably at both the retail end and certainly at the wholesale and the farm end in the egg category and it's probably, I think, most of the gains from the economies of scale and certainly the new

45 infrastructure have probably been passed on to consumers rather than retained within either the, you know, any particular chain of the industry so I think it's very, very tight margins and a very competitive industry at all levels and I think it's probably certainly evidenced by, you know, the margins that the retailers can get and certainly

the margins that major integrated farmers and/or producers can get. It's always very, very tight.

5 MR DONOVAN: Okay. It has been put to the commission and based on the ABS figures that in fact there has been a very big jump in the retail price of eggs that has far outstripped the CPI and only a tiny jump in the farm gate price of an egg. Do you have a comment on that?

10 MR LENDICH: Well, I think certainly without looking at the information, it's hard to comment but as I said before, I think there's some issues with the ABS data. I think there needs to be – when I think you look at averages over time, you need to be particularly careful with changes in mix and there's been a very, very significant mix in free range egg over certainly the last five or six years particularly and over the last ten. So therefore, unless it's a closely looked at, weighted average across different
15 sectors, I would say that, you know, it may give you the wrong impression in relation to average egg prices. Certainly, you know, free range category is grown from probably, you know, 10 to 15 years ago it was maybe one per cent of all eggs sold to now it could be very much as high as 20 per cent and certainly in the retail sector it's probably 25 per cent. So that's a pretty significant increase.

20 There's a very different cost structure for free range egg, hence it sells at a different price and that may have an influence obviously in terms of what the overall perceived price change in eggs on the whole has been but I think if you just looked at particular categories - certainly the cage category - you'll find that over time the
25 price has not moved greatly. In fact I think we looked at prices four or five years ago and prices now and I think my looking at it, I would say that it has probably only increased, you know, up to half of what the actual cost increases have been within the farming and processing sector and it would indicate that most of the gains that that sector has made from economies of scale and efficiency in processing have been
30 passed on to the next part of the chain. So I think returns have been very tight and I would question, you know, a scenario where you're thinking that egg prices have moved very significantly at all.

35 MR DONOVAN: In terms of the data that you would look at to get a picture of what's happening at the retail level, what data do you rely on?

MR LENDICH: Well, I suppose we just take a snapshot at different times of what the retail price is. We don't monitor that closely. We're obviously interested at, you know, range review times and at different times to know what the retail price is.
40 Obviously we know what price we sell to the supermarkets at so we don't keep a total sort of eye on what that margin is but yes, we have an indication from time to time of what that margin is, yes.

45 MR DONOVAN: Sure. So do you buy from AC Nielsen, for example, or do you just - - -

MR LENDICH: We buy the Aztec and Nielsen data, yes.

MR DONOVAN: Okay and now presumably that's reliable for Coles and Woolworths in terms of the scan data. Does it also provide information about the rest of the sector, so the independents, IGA - - -

5 MR LENDICH: No.

MR DONOVAN: No. Is there any reliable source that you know of where information about the rest of the retail sector can be reliably obtained?

10 MR LENDICH: Other than sending a rep down the street to check the local supermarket, I don't think there's any, you know, published data.

MR DONOVAN: Sure. Okay. All right now, then in terms of the farm gate price, again it has been put to us that the farm gate price has only moved 6 per cent in 15
15 years. Does that sound right to you? And that's in absolute terms, that's not - - -

MR LENDICH: It has probably moved a little bit more than that but as I said previously, I think the farm gate price has not moved greatly and the economies that have been experienced with, I suppose, the concentration of the industry from a lot of
20 small farmers to fewer, larger farms that have got modern infrastructure. What's tending to happen, I suppose, is that the level of debt of a lot of the farmers has increased so their financing costs have increased in relation to infrastructure but most of the gain, I suppose, that they've made in terms of cost gains have been passed on and they've been sort of significantly squeezed recently by, you know, the large
25 increase in variable costs of feed.

I think, you know, certainly there would be a number of instances where that's occurred in the middle of an actual, I suppose, cycle in relation to discussing terms with the retailers and they've actually helped us out by increasing price partway
30 through a contract where feed prices have moved significantly. So in that regard I suppose they've been somewhat sensitive to the needs of I suppose the farming sector.

MR DONOVAN: Right. So and in terms of the contracts that you have with major
35 supermarkets, there is that ability to pass through those sudden and substantial cost increases?

MR LENDICH: It doesn't actually – it's not imbedded in the contract as such. It's more a question of, I think, appealing to the individual retailer at a time when it's
40 obvious that there's been a major shift in the feed price. I don't think they would entertain small movements or reviews on a general level. I think they view it as being a fixed price for a period of time but where there's an extraordinary change in the input costs and we've appealed to them on those terms, they've been sympathetic to it.

45

MR DONOVAN: Okay and so in terms of, you indicated that roughly 80 per cent of the price of an egg is the feed cost?

MR LENDICH: Oh, probably 60 to 70, yes.

MR DONOVAN: Sorry and that's of the retail price or of the - - -

5 MR LENDICH: Farm gate price.

MR DONOVAN: Farm gate price, which is effectively the wholesale price that you sell for is the farm, we'll call that the farm gate price or do you see there's - - -

10 MR LENDICH: There is a bit of a difference. I mean, essentially I suppose, there's the farm sector and you're buying eggs either off your own farms or of external farms and then there's a whole bunch of processing, whether it's grading and packaging and transport and a whole range of other things that you actually contribute in the chain before it gets delivered to a DC of one of the retailers.

15 MR DONOVAN: Right.

MR LENDICH: So you know, there's an increased cost of that and there's obviously, there's a marketing element to that as well so there's a package of costs that occur after the farm gate.

20 MR DONOVAN: Right. But for vertically integrated egg producers, is that – would it be separately accounted for so that there is sort of a notional farm gate price and then costs added on?

25 MR LENDICH: Well, yes, we don't generally - the only reason we'd know what that is because we're buying eggs from outside. I mean, we don't tend to separate it out diligently, internally. We have an indication of what that would be by the cost of the eggs we buy in from farmers.

30 MR O'DONOVAN: Right, okay. So if we wanted to get an understanding of what a true farm gate price is as opposed to the wholesale price, we could identify what is going on in the farm gate exchange between the - - -

35 MR LENDICH: Yes, it varies, obviously. Some farmers will sell directly to smaller retailers or sell to someone like us who then on-processes and they'll sell in different forms. So it's a bit of a grey line but certainly, you can get some indication.

40 MR O'DONOVAN: All right. Now, I think you did touch on this briefly, but in terms of the shift in the market from, sorry, branded eggs to house brand could you just describe say in the last 10 years what the make up of the market was and how much it's changed in the last 10 years.

45 MR LENDICH: I'm not sure that I'll know exactly 10 years but it's gone from being a small part of the overall composition of eggs sold. Let's say, it's, you know, 10 to 20 per cent to now, I suppose across the whole egg category, it's probably approaching 60 per cent.

MR SAVENAKE: I think probably 20 years it's gone from zero to 70 where that - - -

MR O'DONOVAN: Right.

5

MR SAVENAKE: When it changed, it's obviously been introduced and grown over a period of time.

MR O'DONOVAN: Right. So 70 per cent of eggs sold by Coles and 70 per cent of eggs sold by Woolworths would now be generic.

10

MR SAVENAKE: Yes, Woolworths.

MR O'DONOVAN: All right.

15

MR LENDICH: I think probably 70 per cent, if it's caged eggs. I think if it was free range eggs it'd be a bit lower.

MR O'DONOVAN: Yes.

20

MR LENDICH: So it probably averages at somewhere around that sort of 60 per cent range, depending on, I think, over all eggs. So certainly, in free range and barn laid categories it tends to be less house brand eggs and in the cage category, there's more. So it just – probably because, you know, the price differential is different and so hence, there's been as scenario where, you know, consumers have had a different price point and so the amount of eggs sold through private label has differed between the two categories.

25

MR O'DONOVAN: Right, okay. Now, just looking at the structure of the joint venture, has it really just been set up to address – the increase the geographical spread, I suppose, give these state-based companies an opportunity to tender for national contracts, or is it addressing some kind of market powers your major supermarkets and McDonalds have?

30

MR LENDICH: Look, I think it's really national tendering. I mean, national tendering came in I think in that sort of '98/'99 period and that's when NOVO was essentially formed to primarily address the national tendering issue and allow, I suppose, small states and small – to defray some of their marketing and the costs of essentially presenting themselves and negotiating with the larger retailers, spread it across, you know, more people, more companies. Also to try to obviously get some advantage in buying in relation to some of the inputs like packaging, etcetera. So I think, you know, those are the key drivers and I think that the trigger point would have been probably national tendering as the major trigger point.

40

MR O'DONOVAN: Right. If these state-based members were not participants in the joint venture could they still tender for various components of the major supermarket contracts?

45

MR LENDICH: Yes.

MR SAVENAKE: Yes.

5 MR LENDICH: Absolutely.

MR O'DONOVAN: Right. In terms of the other companies that they compete against, are they organised on a national basis or do they tend to be organised against state-based competitors?

10

MR LENDICH: Well, different competitors have got different models in relation to, I suppose, farms, where their farms are located. Some are, I suppose, larger integrated farms in one location, in a low feed cost area, for instance, and they'll then transport the eggs longer distances whereas others have got farms and grading floors closer to each market. So it varies and the degree to which they will compete in different markets varies, I suppose, on their own individual egg supplies and costs. But, you know, obviously, over time, the two major competitors to NOVO have been successful in a variety of markets outside what might be termed as their home state, so to speak.

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MR O'DONOVAN: All right. Well, that was all I had for the public session.

THE CHAIRMAN: All right. Well, then we had better move into the private session at this point so I will have to ask those not connected with NOVO or the ACCC to vacate the room, if you wouldn't mind.

25

CONTINUED IN TRANSCRIPT-IN-CONFIDENCE

CONTINUED FROM TRANSCRIPT-IN-CONFIDENCE

5 COMMISSIONER MARTIN: Well, we'll continue now with the representative
from Mercer Mooney produce and thanks for coming in, Mr Mercer. We won't go
through all the rigmarole, you've seen the documentation in terms of how the hearing
is conducted. I'm John Martin, I'm a commissioner with the ACCC, and one of the
presiding members of this inquiry, and Stephen King is another commissioner that's
a presiding member as well. We're going to conduct the hearing with the assistance
10 of some our legal staff, and I'll pass over to Mr O'Donovan to start if off.

MR HOWARD: Sir, just before you do, may I announce an appearance with your
leave?

15 COMMISSIONER MARTIN: Yes, sorry.

MR HOWARD: My name is Howard.

20 COMMISSIONER MARTIN: Yes, Damien will go through and identify – get for
identification.

MR HOWARD: Thank you, sir.

25 MR O'DONOVAN: All right. So could you identify yourself and the company you
work for and your position within that company?

MR MERCER: My name is John Mercer, the name of the company is Evered
Nominees trading as Mercer Mooney.

30 MR O'DONOVAN: Okay, and your role within the company?

MR MERCER: I'm a director.

35 MR O'DONOVAN: Okay. If your legal representative could introduce himself.

MR HOWARD: Yes, sir, my name is Howard and with your leave, I'll appear for
Mr Mercer.

40 MR O'DONOVAN: Right. Now, were you summonsed to appear here today?

MR MERCER: I was.

45 MR O'DONOVAN: All right. You understand that it's an offence under the
Criminal Code to give evidence at this inquiry that you know is false or misleading
or omits any matter or thing about which the evidence is misleading?

MR MERCER: I do.

MR O'DONOVAN: Okay. All right, could you just explain briefly what it is that Mercer Mooney does in its Western Australian operations?

5 MR MERCER: In the Western Australian operation, we deal with some five to 700 growers, from far away from Kununurra down to Albany. We've been selling a lot of those producers, we've been dealing with them for two and three generations. Their produce essentially comes to the markets and we market the produce to a variety of customers, and in a variety of forms. We change some of the packaging, we pre-pack some of the goods, we sell it as is on a number of occasions, and generally turn their fruit into money as a basic role.
10

MR O'DONOVAN: Okay. In terms of how you acquire it, is that through direct relationships with each of the growers, or what are the terms on which you acquire it?
15

MR MERCER: There's a number of ways that that happens. There's a lot of grower groups that have sprung up around Australia, and certainly in Western Australia, and we often deal with a grower group as opposed to single growers. In fact, probably up about 40 or 50 per cent of our produce now comes through like, third party arrangements, where grower groups deal with a group of growers, and then we then deal with the body that controls that grower group.
20

COMMISSIONER MARTIN: Mr O'Donovan, you might sort of remind Mr Mercer that if we get into any sensitive areas, we will move to a private hearing.
25

MR O'DONOVAN: Yes, please let us know if there's anything confidential in questions that I'm asking.

MR MERCER: No, that's fine.
30

MR O'DONOVAN: All right. In terms of the arrangements, are the goods given to you for disposal through the wholesale markets or through direct clients that you have, or is it – can you indicate just the break up of - - -

35 MR MERCER: There's no set break up, the majority of the goods are sold on a day to day basis in the wholesale market.

MR O'DONOVAN: Right. Is that the market in Canning Vale?

40 MR MERCER: In Canning Vale, yes.

MR O'DONOVAN: Okay, so that's the operating wholesale market for fruit and veg in Western Australia?

45 MR MERCER: That is correct, yes.

MR O'DONOVAN: All right. Can you describe – could you just describe how goods are cleared through that market? Not necessarily by Mercer Mooney, but generally speaking?

5 MR MERCER: Generally speaking, the goods come in seven days a week on a 24
hour period, they are received, inspected, generally speaking, inspected for quality
assurance, and then the goods are put up for sale in the following – over the
following week, some of the goods are ripened over a one to two week period, like in
bananas and mangoes, the – a lot of the goods are presold coming in, in case we are
10 supplying to one of the supermarkets. We quote them out one and two and three
weeks out, so a lot of the arrangements with the growers are prearranged pricing.
Some of the bigger groups where we do on the – the third party arrangements are
basically sent in, we sell on their behalf to try and maximise the returns. That's our
job at the end of the day, to get the maximum return.

15 MR O'DONOVAN: Okay. In terms of the Canning Vale market itself, does it have
a grower's floor when growers can sell stuff direct to the public, or any retail
operation?

20 MR MERCER: It has a small retail operation, but essentially speaking, the Perth
market is a wholesale market only, there is no grower market. The only markets in
Australia that have grower markets are Adelaide, Melbourne and Sydney.

MR O'DONOVAN: Okay.
25

MR MERCER: This comes from Perth – Perth originally was broken up in the old
West Perth markets, was broken up into two sides. There was a number of grower
cooperatives that operated basically on one side of the markets, and then the private
treaty operators operated on the other side of the road, and through the fullness of
30 time, much of those grower – or all of those grower cooperatives have now passed,
the option system slowly went into decline, disappeared in the early '90s.

MR O'DONOVAN: All right, so it's effectively now just a wholesale operation.

35 MR MERCER: Correct.

MR O'DONOVAN: Okay. How many wholesalers operate within the market?

MR MERCER: From memory it's 22. Give or take one.
40

MR O'DONOVAN: All right. In terms of the lines of fruit and veg that Mercer
Mooney sell, how many lines – does it deal in every line, or are there specific lines it
specialises in?

45 MR MERCER: No, we sell just about every line, with the exception of potatoes.

MR O'DONOVAN: Right. And is that true of most wholesalers, or is that - - -

MR MERCER: No, most of the wholesalers are smaller and tend to specialise in certain lines.

5 MR O'DONOVAN: Okay. Is there more than one wholesaler in every line?

MR MERCER: Yes, most definitely.

10 MR O'DONOVAN: Okay. So in – looking then first at what a grower's options are in terms of getting their goods to market in Western Australia, is it true to say that most growers have to deal through the wholesale market?

15 MR MERCER: No. A lot of growers deal direct with supermarkets and retailers. The bigger vegetable growers, for instance, would deal predominantly off market and some of the bigger – certainly the carrot growers who grows between six and eight hundred tonnes of carrots per week, there would be a maximum of 30, 40 tonne a week would come into the markets, the rest would be done offsite, direct to supermarkets, direct to the eastern states, and to export markets.

20 MR O'DONOVAN: So exporters don't operate through the Canning Vale market?

MR MERCER: There are very few, if any, direct exporting operations in the markets. There's a few, what we call, small niche exporters that are based there, but the old traditional exporter, of which we were one for 40 odd years, are basically disappearing with the cost of production in Australia, certainly Western Australia, there's essentially far too high to compete on the export markets.

25 MR O'DONOVAN: Right. In terms of the sales to the eastern states, how are they facilitated?

30 MR MERCER: The majority of those are done grower direct, the sophisticated growers and the ease of communication in this day and age, everyone knows what the prices are of all the produce around Australia very quickly, the major grower operators deal direct with the eastern states. Some of them deal through us as basically subagents, and that's done on a buying and selling type situation, but we would send small quantities of apples over there at certain times of the year, and strawberries. The rest of the time it's done grower direct.

35 MR O'DONOVAN: Right. Okay, so in terms of your company's position in the market, it's primarily a wholesaler?

40 MR MERCER: Yes.

MR O'DONOVAN: Right. In your business, what proportion of the product that you sell would end up being sold through a major supermarket, either Woolies or Coles?

45 MR MERCER: That's where I'd prefer to answer that in private, thank you.

MR O'DONOVAN: Sure, okay, but you do have – you, yourself have dealings with Woolies and Coles?

MR MERCER: Most definitely and IGA.

5

MR O'DONOVAN: Okay.

MR MERCER: Yes.

10 MR O'DONOVAN: The – and I suppose apart from those operators who were the main buyers in the wholesale markets?

MR MERCER: There are some 120 independent supermarkets basically dealing under the IGA brand in Western Australia and they are supplied in a number of ways. There is – IGA have their own direct set up, where they're based in IGA headquarters in Canning Vale and then there are quite a number of independent wholesalers who are based at Market City, in their surrounds in the warehousing that surrounds there, that buy for and supply those supermarkets, so they build up – they make up the large portion of our business and they buy three or four, five times a week and supply the customers on an as needs basis. We, ourselves, supply, I think it's – through one of our companies supply about eight or 10 of those independent IGA stores.

MR O'DONOVAN: So they're operating as individual buyers and individual supermarket operators as an individual buyer within that - - -

MR MERCER: Yes, or they have – they operate as a small collective and they have a buyer who will buy for four or five supermarkets.

30 MR O'DONOVAN: Right, but the IGA group as a whole doesn't?

MR MERCER: They supply about – and, I mean, it's only a guess, about 30-odd of their stores direct.

35 MR O'DONOVAN: Right, okay and are there other players in the wholesale market - - -

MR MERCER: Most definitely, you then have – then you have a plethora of retail buyers that operate from the weekend markets, Fremantle, Malaga and those various surround markets, they are some of our more interesting customers. There are a number of – of course the grower markets, that's like Herdsman Fresh, Claremont and the specialty stores around Perth of which there is a good number and they buy – they themselves buy direct off growers and off the Perth markets.

45 MR O'DONOVAN: In terms of I suppose the proportion of the market as a whole that runs through these independent customers, would you have any idea what proportion of the market they would make up?

MR MERCER: The market as a whole?

MR O'DONOVAN: Yes.

5 MR MERCER: At Market City you'd be thinking it would be around 50 to 60 per cent would go out to independents, of the goods that go through the Perth markets.

MR O'DONOVAN: Right, okay, and is that a reflection of the market share that those independents would have in terms of fresh produce and I'm talking now about
10 the retail market, so in terms of the retail market share of fresh produce?

MR MERCER: No it would be lower than that, because a lot of the supermarkets deal direct, so the percentage is skewed, but the percentage that goes through Market City is different to the overall percentages.
15

MR O'DONOVAN: Right, and when you say Market City, is that the Canning Vale?

MR MERCER: The Canning Vale markets, yes.
20

MR O'DONOVAN: Right, yes, all right. So roughly half of everything that goes through the market would go to independents? Am I understanding that correctly?

MR MERCER: At Canning Vale? I would think it would be slightly more would
25 go to independents.

MR O'DONOVAN: Yes, all right and that's independent retailers or independents including food service, like restaurants.

30 MR MERCER: Yes, including those.

MR O'DONOVAN: Right, okay and then the remaining share would be broken up between the major supermarket chains?

35 MR MERCER: That's correct.

MR O'DONOVAN: Just the major – just Coles and Woolworths and IGA?

MR MERCER: And the IGA. The IGA – it's very difficult to get a handle on the
40 amount of percentage that's bought through that, because they were bought through sub-wholesalers you're not dealing – you can't actually list them as a supermarket purchase, you just – because it's an individual person you're selling to, you just know the part of their business and it's only part of their business would be supplying those independents - IGAs. They would also be doing other restaurant
45 work, oil rigs, mining sites, which is a very important part of the mix of the business, those wholesalers.

MR O'DONOVAN: Right, okay. So in addition to the – I think was it 21 wholesalers?

MR MERCER: I think it's 22 now.

5

MR O'DONOVAN: Twenty-two wholesalers, okay. There are also subwholesalers, you say, operating in the market?

MR MERCER: They work on the periphery of the markets and they work out of the wholesale – out of the warehouses.

10

MR O'DONOVAN: Right, and are they effectively consolidating?

MR MERCER: Consolidating, yes, and by – under the Perth Market Act they're not allowed to offer goods for sale in the traditional sense, only the central trading area can, but that is very difficult to police and there are – certainly trading goes on in those warehouses.

15

MR O'DONOVAN: Right, and is that a secondary market, or is that actually - - -

20

MR MERCER: Just a hidden market really.

MR O'DONOVAN: Right, okay. So in terms of – when a grower's produce arrives or is consigned to you, it's – how is the price at which that then passes – how is it set by the market, so not so much your – I'm not interested in your arrangement - - -

25

MR MERCER: No, okay.

MR O'DONOVAN: - - - as a grower, but how is the market price set at this point?

30

MR MERCER: The market price is really determined by supply and demand, 101. The information nowadays that's around on pricing on the east coast, we all get access to the east coast pricing, so you know what is happening, I guess the greatest case of pricing just recently, of course, was after Cyclone Larry when North Queensland was basically obliterated and the bananas went up to 140 and \$150 a carton and that was just simply demand and no one could ever have guessed that prices – the demand would on reasonable supply would push pricing of bananas to that extent, except the population then paid 14 and \$15 a kilo for them. I won't say happily, but they did. It's a bit like petrol really, doesn't matter what the price of petrol is people still buy it.

35
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MR O'DONOVAN: Right, and the Western Australian banana market didn't operate like an independent – like a market that was independent from the east coast market?

45

MR MERCER: No, no, it's all one and the same.

MR O'DONOVAN: Right.

MR MERCER: And the pricing of it was – in Western Australia was very similar to the east coast, because what bananas were produced on the east coast, where we
5 would normally supply Western Australia, we'd supply about one third of its needs and import two thirds of its needs from Queensland basically the West Australian supply became almost the only supply.

MR O'DONOVAN: Right, okay.
10

MR MERCER: A lot of Western Australian growers bought big flash boats and they still have them.

MR O'DONOVAN: So in terms of the fluctuations in the market, does it fluctuate
15 within a day – the prices?

MR MERCER: Most definitely and depending on the lines. Some lines fluctuate more than others, tomatoes would be one of the most difficult lines, because they're
20 a short crop and basically if you want to be a tomato grower you can wake up excited in the morning, by lunchtime with a rotary hoe and a bit of trickle tape you can be a tomato grower and for instance three weeks ago tomatoes were 30 to \$45 a carton, Bowen in Queensland and Bundaberg had a bit of a flush along with some of the ones down in Victoria and the price of tomatoes dropped from 35 to 45 back to, I think they ended up back down to five to 15 in a week and they're back up again
25 now to the mid-20s and will go higher than that in the next couple of weeks.

But that's the fluctuations of a tomato market, because one of the big growers over here supplies a lot of fruit to the east. The eastern states collapsed, all the fruit stayed here, price went down by two-thirds and life went on. But that's the thing. Apples,
30 because West Australia is self-sufficient in apples and you can't import apples into Western Australia the apple market is by and large more steady. A lot of apple growers have pulled out over the last 10 years, as price of land has gone up, so we're now in a nice balance where the growers that are left are actually making quite a good – the good growers that are left are certainly making a good living.
35

MR O'DONOVAN: All right. In terms of knowing the price on the day, is published information available before the opening of the next day?

MR MERCER: No.
40

MR O'DONOVAN: No. So if you wanted to find out what the going wholesale price for a crate of tomatoes was, how would you do it if you were operating efficiently in the market?

MR MERCER: You would be discussing it. Most buyers tend to work with a small range of people that supply them and they'd be talking and discussing with them one or two, three times a day about where the pricing is going. Pricing trends are

normally known a few days in advance but they're only trends and they will change dramatically from day to day. So they have a lot of – there's a lot of trust in our industry, trust between the growers and ourselves and then our buyers and ourselves. It's certainly is not perfect but there is certainly a lot of trust.

5

MR O'DONOVAN: Right. Okay. So what would cause a grower to decide to deal with a wholesaler like you through the wholesale market rather than sell direct to the major supermarket?

10 MR MERCER: Normally a bad experience but some of them, as I said, we've been dealing with them for two and three generations and they just trust us to market their produce and we work together as a team to try and plan what they're going to grow, even down to the varietal stage nowadays and the timing of all that so that they can
15 make sure they come out with a profit at the end of the year. So if the growers don't make money, we certainly won't have a business.

MR O'DONOVAN: Sure. Are you in any sense competing with the major supermarkets for the grower's crop?

20 MR MERCER: Yes, we are.

MR O'DONOVAN: Right. Okay. In terms of how the major supermarkets influenced the wholesale market, do you have any understanding on how they price relative – in terms of the growers that they deal with direct, what's the relationship
25 between the contracts they make there and what's happening in the wholesale market.

MR MERCER: Most of them are fairly straightforward. I mean, the same with us. We quote up to three weeks out for the major supermarkets.
30

MR O'DONOVAN: Sorry, when you say you quote up to three weeks out, you give them a price?

MR MERCER: We give them a price up to three weeks out when they need to go
35 on promotion.

MR O'DONOVAN: Yes.

MR MERCER: Then, one and a half weeks when they're just on normal supply.
40

MR O'DONOVAN: Right. Okay.

MR MERCER: That is a strong guide but is not sacrosanct. You can get what they call purchase order variations. I think the record is 72 in one week. Quantity, even
45 pricing, pricing can be changed on a day to day basis but that's normally done for a reason. If there's an oversupply in something, something will change and then by mutual consent we will change it and sometimes it's not always that mutual.

MR O'DONOVAN: Right. So the quote is an indication of price but it's not - - -

MR MERCER: No, it's a firm quote.

5 MR O'DONOVAN: It's a firm quote?

MR MERCER: Yes.

10 MR O'DONOVAN: Okay. If there's a dramatic change in the market - - -

MR MERCER: That's correct.

15 MR O'DONOVAN: - - - both sides realise it's in their interest to be flexible in terms of negotiating that?

MR MERCER: Yes. That's correct.

20 MR O'DONOVAN: All right. So there is a close relationship – at least when they're buying through you to the wholesale price and - - -

MR MERCER: Sometimes even more so when they're dealing direct with the growers.

25 MR O'DONOVAN: Right.

MR MERCER: Especially on the vegetable side, they form long, strategic partnerships with vegetable growers. Fruit is more difficult because fruit comes in many sizes, many grades most times.

30 MR O'DONOVAN: Sure. Again, the nature of these partnerships is still that price will be market price whenever the product is read?

MR MERCER: By and large, yes.

35 MR O'DONOVAN: Right. Okay. Now, the fact that they're buying – that the – seems 50 per cent of fruit and vegetables is absorbed by Coles, Woolworths or IGA, does that impact on the efficiency of the wholesale market? Has it damaged the market in any way that those large volumes going through those - - -

40 MR MERCER: No, it hasn't, no.

MR O'DONOVAN: Right. So it still operates as an effective way of clearing the product.

45 MR MERCER: We have a lot of - especially on the fruit side of it, we have a lot of growers who used to deal, dare I say two bob each way, have now come back to

giving us all their produce and we supply a lot of their specific sizes straight to the chains.

MR O'DONOVAN: Right.

5

MR MERCER: Then market the other sizes that the chains don't want. The chains can only, with their very strict protocols and sizing requirements, can only take a certain portion of the – especially on the fruit side of it.

10 MR O'DONOVAN: Right. Okay. The benefit of that arrangement is that you're effectively better at packing and consolidating to the supermarkets' requirements

- - -

MR MERCER: Yes, yes.

15

MR O'DONOVAN: - - - than a particular individual grower might be.

MR MERCER: Not – we're as good as and some of the growers are better than others, but generally speaking we believe we do a better job if we market the whole growers produce, basically the whole crop management-type set-up.

20

MR O'DONOVAN: Right. Okay. In terms of your obligations to the grower and their crop, are you obliged to take their crop or is each party free to walk away?

25 MR MERCER: Each party is free to walk away at any time.

MR O'DONOVAN: Right. At any time.

MR MERCER: That's the strength of our arrangements, actually, is the fact that because people can walk away, that makes the bond actually stronger because you actually need – we need the grower as much as they need us but there's 22 or 25 of us out there. They can swap between merchants at any stage of the operation or they can deal direct or the ones that are close to Perth, they can deal direct with the retail stores. A lot of the retail stores themselves whiz out there and buy direct off the growers.

35

MR O'DONOVAN: Right. In the last 12 months, what proportion of growers would have shifted wholesaler?

40 MR MERCER: That's – you couldn't answer that. If I was guessing, I'd say there'd be about a 20 per cent of the growers would move around the place. The majority of our customers are very stable; our suppliers are very stable. It just doesn't happen.

45 MR O'DONOVAN: Right. Okay. Then it's been put to us, at least in relation to some product categories that the way in which the supermarkets operate is that on occasions they can effectively manipulate the market by not buying a product for a

few weeks which has the effect of suppressing – sorry, increasing the available supply of it, suppressing the price and then entering the market at that point. Are you aware of that conduct – have you ever seen price shifts that make you think that that conduct might be occurring?

5

MR MERCER: I have but it's not as simple as that. That normally happens at the beginning of the season and it's normally done with quality assurance in mind because, like, at the beginning of the mandarin season, one of the majors actually held out, stopped for a week, because they believed the taste wasn't right which is quite acceptable. So that had an effect, the fact that we ran bang in then to school holidays in the east coast, that had an effect of diminishing the price dramatically and a few people were blaming them for that but that was just on a taste basis and that was quite correct if – from a consumer point of view, it was the correct thing to do.

10

15 MR O'DONOVAN: Right. How – I guess, how easy is it for them to do that, given their size?

MR MERCER: No, it's not because they're competitive beasts and you have all their sales people scouting the markets all the time and if they can get an edge on their competitor, they'll do that through a special buy. They do these, what we call special buys. Even though we contract out the prices a week, two weeks in advance, they'll then come around the markets and buy, as I said, special buys. If something is a bit oversupplied, they will – they'll target that at certain areas, certain sections, where they'll put those out on special.

20

25 MR O'DONOVAN: Right. In terms of cooperation between the major supermarkets have you ever seen any evidence that they were withholding demand at the same time, and like refusing to enter - - -

30 MR MERCER: No, certainly not.

MR O'DONOVAN: Right, okay. All right. The other issue that's been put to us is that they reject stock on a quality basis, or what they say to be a quality basis, at times when what has happened is that the market price has gone down and that there's really nothing wrong with the product but they're not prepared to pay the price when the market has fallen and they want to acquire the stuff at a lower price. Have you seen any evidence of that conduct?

35

MR MERCER: I won't say it's never happened. It is certainly rare. In most cases we will renegotiate a price beforehand because – and the reason we would do that is because we want to sell more produce. Generally, the reason that the price has come down on something is the supply has suddenly gone up, whether it's strawberries or whatever it is, and so you renegotiate another price, a slightly lower price, on the promise then, hopefully, that they will then double the order and that's just a natural mechanism. Their QA sections are at times difficult to understand. They, like ourselves, have staffing issues and some people, I'm sure – some of their staff at times, I would rather they weren't doing their jobs.

40

45

But we mimic. Before we deliver it to any supermarket we actually have a full QA section that actually mimic the arrival procedure and so anything that we're sending out to them, we put through our own QA section as they will review it on the way in. Our target with our main supermarket is to have an under 1 per cent rejection and we're just on the – fractionally borderline above that at the moment.

MR O'DONOVAN: Right. In terms of the things that are often discussed as having had an impact on the price of fruit and veg at the retail level, in your view have you seen shifts in the retail market as a result of the drought or - - -

MR MERCER: The drought has had a small effect. Most of the drought is in the Murray area, it certainly hasn't affected Western Australia. That was – most of the fruits that were involved there was – and from the fruit side of it was citrus and the citrus pricing has gone up a little but very – not as much as it should have done with the – by the effect of the drought which means the public are not concerned about eating citrus as much as they are about eating a banana.

MR O'DONOVAN: Yes.

MR MERCER: Bananas went up to 14/\$15 a kilo and the supply went down. The supply went down on citrus a little bit, hardly affected the price.

MR O'DONOVAN: Okay. So in terms of the West Australian market, have there been increases in wholesale prices as a consequence of any, I suppose, broader events happening in the economy like fuel prices going up or - - -

MR MERCER: Certainly. A lot of our product comes out of Queensland. We are now paying up to \$550 a pallet space for produce to come out of Queensland now. So every box of bananas that's coming out has got a \$7 fuel – transport cost on it before they land here in WA, and that's at the moment. I think the price of fuel went up again today so they now – all the transport companies that we deal with, they have a nominated price plus a fuel levy which is adjusted monthly.

MR O'DONOVAN: Right.

MR MERCER: So that's going to become - from a West Australian point of view, it's going to become more and more of a challenge. But our biggest single challenge is lack of staff, at every level.

MR O'DONOVAN: Right. By the mining boom or - - -

MR MERCER: I think that's the main attributor, yes.

MR O'DONOVAN: Right.

MR MERCER: But that's our biggest challenge, we can't get staff.

MR O'DONOVAN: Right.

MR MERCER: Even at Canning Vale we struggle. Our growers certainly, with
5 some of the big plantings up around Kununurra, in the next few years are going to
really struggle.

MR O'DONOVAN: Is it a case that that market isn't responding well to increases
in salaries and things like that?

10 MR MERCER: You just can't – the people are just not there to do it. They've
made the immigration rules so tough that – this is probably not the place to mention
it, but without a guest worker program in Australia similar to what they were trialling
in New Zealand, there's a number of horticultural things around Australia that are
going to come to a shuddering halt due to lack of staff in the next few years.

15 MR O'DONOVAN: Right. So rather than increasing the costs of production it will
actually have a impact on supply?

MR MERCER: Most definitely.
20

MR O'DONOVAN: Right, okay. Are there any other broader economic factors
which you think might be contributing to increases in the price of food and fresh
food, in particular?

25 MR MERCER: Water is going to be the ultimate challenge, one of the challenges.
Western Australia is fairly well settled with the water scenarios in the main growing
regions. The government has got a lot to – there's a lot of talk about what's going to
happen about the cost of water, growers' dams, you know, is it his water, and it's not
his water, and is he going to have to pay for his own water again? That would all
30 have a big challenge on the cost of production. The cost of land has really made a
difference to our industry over the last 10 years. A lot of areas in the south west,
close to the Bunbury – like Donnybrook, which was originally deemed to be too far
away from anything, is now being sold and chopped up into blocks where people can
buy land at reasonably affordable prices and living and working in the area but
35 commuting to places like Bunbury, where they can get work now.

So a lot of our old traditional growers have gone out of business, sold up, their kids
don't want to go into the business, don't want to work like mum and dad did.
Generally, coming off a farming background, they have a good, broad knowledge of
40 survival skills and general skills and they are the kids who have been really jumped
on in the mining industry and that's where they all are.

MR O'DONOVAN: So have we seen or have you seen as a result of that, upward
pressure on wholesale prices?
45

MR MERCER: Most definitely, yes.

MR O'DONOVAN: Right, okay.

MR MERCER: But it's to a stage where a lot of them – a lot of the places before that were uncompetitive like export, for instance, three-and-a – four years ago we
5 exported through a secondary exporter 160,000 cartons of plums in a year. This year just gone, all we could manage was about 42,000. The way things are going, we'll be doing less even next year.

MR O'DONOVAN: Right. Presumably, exchange rates are an influence on that?
10

MR MERCER: South Africa and South America are just getting better and strong and their supply base and their cost of doing work. So most of those growers have actually pulled the crops – pulled the trees out and are no longer in that business. With a diminution of the grower base you get to that supply and demand balance
15 again where the prices the growers are getting now they can survive on and they're now investing back into new varieties but we're dealing with a small number of better growers at the end of the day. More professional growers is – that's probably a better way of putting it.

MR O'DONOVAN: Right. But are the actual amounts of production declining?
20

MR MERCER: Marginally but what's being grown now is generally better.

MR O'DONOVAN: All right. Now, then in relation to the horticulture code,
25 presumably you're aware of the implementation of the horticulture code?

MR MERCER: It has come to notice, yes.

MR O'DONOVAN: Yes. Could you just describe briefly what you regard as the
30 impact of the horticulture code?

MR MERCER: That's one of those areas I'd rather talk in private, if I may.

MR O'DONOVAN: Sure.
35

MR MERCER: Thank you.

MR O'DONOVAN: Okay, all right. Or one aspect of it you might be able to discuss in public, it was put to us by the Brisbane markets that the effect of the
40 horticulture code made selling by wholesale to someone bound by the code less attractive than dealing with the supermarkets or, sorry, it was an added cost to wholesalers to comply with the horticulture code which wasn't imposed on the supermarkets and gave them a competitive advantage. Do you have a view on that?

MR MERCER: Yes. It's complicated but the net effect would be a diminution of price to the growers to deal in that manner whereas the supermarkets are out in the open. Their systems are very open as I'm sure you've seen. As we do with them, we

quote, the growers quote and they pick out what they want and life goes on. It's not selling that produce that is a supermarket niche, it's selling the balance of it is where the challenges come in.

5 MR DONOVAN: But in terms of the compliance costs of you having to comply with the code, do you see that your practices now are more expensive relative to the practices that the supermarkets routinely engage in in terms of having written contracts in terms of determining price, in terms of your ability to reject produce?
10 Are you now in a position where you've got additional costs that the supermarkets don't have?

MR MERCER: We are still in the favourable position where we're dealing under a number of trading entities. We still have some people who are under the current HBAs. We have a lot who are under the pre-2006 agreements and we deal a lot with
15 third party handlers who are themselves bound by the code but we are not bound with them. So we have an amalgamation of trading scenarios. Certainly the trading as a merchant under the HBAs is more complicated and difficult. Extremely difficult.

20 MR DONOVAN: Right. Is it more complicated, though, than the arrangements that supermarkets routinely enter into?

MR MERCER: Yes, because the supermarket knows exactly what size apple/piece of produce he wants so you're talking about a known entity, a known quantity and
25 quality of product. In the balance of the produce, there could be seven different sizes, three different grades and that's where the challenge is extremely difficult under the horticultural code. Especially in Western Australia as we have the Perth Market Act which sits under the Federal Act, which complicates our life even more.

30 MR DONOVAN: In what respects does the Perth Market Act – how does the Perth Market Act - - -

MR MERCER: The Perth Market Act? Basically if we – because of the size of our company, we have so many different branches and some of those branches buy off
35 our own company and other companies in the markets. Under the Perth Market Act, we can't operate as an agent and sell to yourself for very obvious reasons. So we operate as a merchant under the Perth Market Act.

MR DONOVAN: Right. Now, in terms of retail pricing, presumably you observe product that has gone through your wholesale markets and then you see what it's
40 being sold at at retail. Have you observed that the mark-up in retail has grown in the last five to ten years?

MR MERCER: It's all anecdotal but what I've seen, it certainly has gone up and I
45 know some of my good friends are retail operators and their cost of doing business like ours has gone up dramatically. The rents and wages are going up but I don't

think it's gone up any more in proportion than anything else that has gone up, from what I've noticed. But again I'm not a retailer.

5 MR DONOVAN: Okay, but just looking purely at gross margins, your observation is that the mark-up between the wholesale price that they would have paid for produce and the retail price at which they sell it, your observation is that that gap seems to have widened?

10 MR MERCER: Yes. A little, yes. The rule of thumb is that you buy it at a price and you double it and add a bit on or take a bit off to make it look competitive so it comes out at 4.99 or 3.99 or there's price points at which stuff sells better than others and those price factors are very important. If we want to promote something and work with someone, we'll actually discuss the price that they're going to sell it at before we'll arrive at a price.

15 MR DONOVAN: Okay. In terms of the sensitivity of the retail price to what's happening in the wholesale markets, do you see the retail price responding as quickly now to changes in the underlying wholesale price or is there a slowdown?

20 MR MERCER: They certainly do until things come into, dare I say glut or oversupply situations and that's when we generally get the most complaints from growers. "I'm only getting \$5 a box and they're still selling them at 2.99 a kilo." The fact is that if you gave produce to a shop, to a retail shop for nothing, they still need to charge 2.99 a kilo for it to pay for their staff and all their other things. That's
25 when you get the most complaints in our industry. It's normally in gluts and oversupplies. As for instance, as I said, bananas last week were sold in the Sydney markets at 5 to \$14 a box and the cost of production is around 17-\$18 a carton but they produced 530,000 cartons as evidenced by their website.

30 They put their weekly figures on their website so he doesn't have to be a Rhodes scholar to figure out if you're the supermarket buyer or a small buyer, if you check their website each week and see how many bananas were produced and transported out of North Queensland, you just know that the price of bananas is going to come down, which it did. Now, whose fault is that? Simple answer is, you know, after
35 Cyclone Larry they were all told to be careful and don't overplant and the first thing, they went out and planted twice as much.

40 MR DONOVAN: But in terms of the retail price that you're seeing as a result of that glut, there is some retail reaction?

MR MERCER: Oh most definitely, yes and some of it is silly. There were people selling at 99 cents a kilo last week on the east coast. One person even sold them at 5 cents a kilo. Silly stuff. You know, that has no normal market application. They were just trying to make a name for themselves. At 5 cents a kilo, you're basically
45 giving away stock but generally speaking, these are anomalies that happen when there is an oversupply situation and people do silly things. But there still would have

been bananas being sold on the east coast last week, I'm sure, at 3.99 and 4.99 because that's the price to sell bananas at.

5 MR DONOVAN: Right. Okay. So there often is a disconnection between the retail price at which things are sold and what's happening in the wholesale market?

MR MERCER: That's one of the beauties of living in a free society.

10 MR DONOVAN: But it's not a product of market concentration at the retail level?

MR MERCER: No, I don't believe so.

MR DONOVAN: An expression of power by Coles or Woolworths?

15 MR MERCER: No. Generally speaking, they are more responsible in moving the prices along with supply and demand. In fact, we had some people over here last week and they were complaining that their numbers were down. Their retail dollars were down because the price of bananas had come back so far and the dollars weren't going through the till and they were complaining bitterly about it but they
20 have to follow the competition.

MR DONOVAN: I think that's all I had up to.

25 COMMISSIONER MARTIN: Yes. Just a couple of things, Mr Mercer. You mentioned about acting as an agent, that you couldn't – there were some limitations on you. What is the situation between agency and operating as a merchant in the Perth markets? Can growers access agents?

30 MR MERCER: Certainly. There are a number of firms in the Perth markets that operate on a true agency basis and that has been there since the conception of the Perth Market Act, which is around 2000 and so the buyers – growers – have got a number of options how they can trade in the Perth markets. Some buy what we call merchant-type arrangements, which is a quasi, in the true sense is a quasi-merchant and there's a true agency with 100 per cent transparency and as we've always said, if
35 it was the grower's true belief that they wanted 100 transparency, the firms that offered that, you would think, would then grow and prosper and the others would diminish, which would force a change in the culture and essentially that hasn't happened. Moreover, I think it's gone slightly the other way.

40 COMMISSIONER MARTIN: And that is because?

MR MERCER: At the end of the day, the growers measure – they measure our business acumen on the amount of money that we return to them. It's our job to return to our growers the most money we can, that's our job. If we've been
45 successful, our business grows, and more growers come to us. If we're being unsuccessful, well, growers will leave us and go somewhere else.

COMMISSIONER MARTIN: But is there a difference then in the relationship if it's a bigger grower or a smaller grower?

MR MERCER: No.

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COMMISSIONER MARTIN: In terms of – you mentioned partnership?

MR MERCER: There's some of the big grower groups that operate as grower groups that – like, in Carnarvon, there's one of our grower suppliers groups that has 42 growers, and they trade exclusively with us.

10

COMMISSIONER MARTIN: That's a merchant basis where - - -

MR MERCER: Yes.

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COMMISSIONER MARTIN: In terms of price, you scope prices for them or?

MR MERCER: Yes, we discuss prices with them, but the pricing is all left up to us, we advise them what's happening with pricing on a day to day basis, and the returns then follow.

20

COMMISSIONER MARTIN: Big wholesalers like yourselves, are you directly involved in the growing as well?

MR MERCER: We joined a national company in March last year, and we now are involved in growing. We have a couple of mango farms in Darwin, a couple of banana farms in North Queensland, and side interests, shared interests in potato, onion and citrus growing.

25

COMMISSIONER MARTIN: So is that a common situation with wholesalers, that they're - - -

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MR MERCER: No, it is – there is a number of the larger wholesalers on the east coast who have growing interest, interest in growing areas. In Western Australia it is limited to a few, a few of the people in the Perth markets have interests or grower shareholders, but generally speaking it's more confined to the east coast.

35

COMMISSIONER MARTIN: Right. You mentioned you cover all lines except potatoes, why don't you do potatoes?

40

MR MERCER: That's my pet subject, sir. In Western Australia, we have a thing called the Perth – the Potato Marketing Act, which was originated in, I think in the middle of the second world war to protect the stable supplies of potatoes. In case anyone hadn't noticed, the Second World War ended. So there is as much need for a potato marketing board as there is a turnip board or a carrot board. It's just – anyhow. How long have I got?

45

COMMISSIONER MARTIN: Mr Mercer and I didn't agree on that question, but I recall now, it was probably a silly question for me to ask.

MR MERCER: No, it was a great question.

5

COMMISSIONER KING: I was just wondering, do you think we need a turnip or a carrot board?

MR MERCER: No.

10

COMMISSIONER KING: Just on public issues, you mentioned, you know, if you don't perform for growers then your business doesn't grow and growers move. Given that – I think you said there's 22 wholesalers in the Canning Vale markets and not all of them cover all produce. How realistic is it for a grower to actually move between wholesalers, I mean, am I looking at a choice between, you know, Mercer Mooney on one side or one other party on the other side, or have I got a choice of five, or have I got a choice of 10?

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MR MERCER: If we talked fruit, there would be 15 would handle fruit.

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COMMISSIONER KING: Particular crops, or - - -

MR MERCER: Mostly whole crops, and or parts thereof.

25

COMMISSIONER KING: Okay.

MR MERCER: If you look at the main home fruits, apples, pears, and then citrus, there would be eight or nine citrus handlers, and all the others would handle some, and would have the ability to handle some if they did. What we try and do, our role, of course, is to get as many growers working together in groups so we get continuity of supply and offer. That's where we attract better customers, better price, better returns, life goes on.

30

COMMISSIONER KING: Okay. How much movement is there of growers, I mean, would most growers – I think you said you've dealt with some for generations, but presumably there's others that you've dealt with for one season and then you've gone off somewhere else, is it possible just to get a bit of a feel, would there be, you know, would five per cent of growers tend to move between wholesalers over a, say, a 12 month, two year period, or would it be - - -

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MR MERCER: Generally speaking, the smaller growers move more, back in the '80s, '70s and '80s, there was a very high Italian, Slav mix of growers, and Carnarvon, Swan and – they used to move around a lot, competition was very strong. In the '90s, of course, we had the explosion of the Vietnamese growers, and they still are probably the most moveable bunch of growers at the moment, but that's changing now, we're almost coming through a cycle of those, because the fellas that started off in the '90s leasing land have now bought land, and they're becoming more stable and

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more mature in their marketing, and they now work with us growing, planting crops. Some of them still move around a lot, some of the – a lot of fellas will still lease land off someone, grow short crops, mainly in the short crops where they'll duck around and they'll sell direct to shops, they'll sell at the markets on the weekends. Generally speaking, the supermarkets don't deal with them as much, because there's quality assurance challenges, and so – they tend to move around. But again, as I said, that's maturing now, that's coming to that next cycle. Some of the fellas have made a fortune out of land. One of my strawberry growers I wrote a letter for eight years ago came to me a couple of weeks ago and said, "John, they just offered me 13 million for my land." So he's not struggling anymore.

COMMISSIONER KING: I'm not sure that I'd want to commute up from Bunbury or whatever on a daily basis, but – it's a bit like Sydney.

MR MERCER: Yes.

COMMISSIONER KING: Sorry. Apples, as you said, you can't bring them into Western Australia. Can I conclude from that that apple prices in general are higher in Western Australia than they would be on the east coast?

MR MERCER: They have been this year, last year they weren't, the prices of apples on the east coast were about – around Australia were very similar. They've had a slightly larger crop on the east coast this year, and the prices are down a little bit. Which will mean that we won't sell as many apples to the eastern states as we have done, as – we as a state won't sell as many apples to the eastern states, so that will keep our prices more moderate.

COMMISSIONER KING: I mean, obviously there is a range of reasons why you would restrict interstate and indeed import of fruit and vegetables - - -

MR MERCER: It's only quarantine, pests.

COMMISSIONER KING: Well, mainly quarantine issues, yes. Just in the case of apples, though, does that cost the Western Australia consumer because they can't access, you know, in years, when the price is higher, they can't access the east coast crop, but in years when the Perth prices are low compared to the east coast, well, the stuff gets across the Nullarbor?

MR MERCER: That's what we call a ratchet mentality. It can go out but it can't come in. It has done on a few occasions, yes. It's minimal, but it has happened. Certainly over the last two years when the crops were pretty well whacked around on the east coast, with – they had some really bad weather events, they did – a lot of fruit went over to the eastern states, so the price went up, yes.

COMMISSIONER KING: Now, major supermarket chains, you said that you have fixed quotes – contracts with them - - -

MR MERCER: Contract is a nebulous word, so.

COMMISSIONER KING: Yes, fixed quote agreement with them, depending on whether it's for a promotional week or non promotional week, it can vary in time.

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MR MERCER: That's right, yes.

COMMISSIONER KING: You've then also just noted that it can adjust, for example – the example used was if there's a surplus, it can be adjusted down.

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MR MERCER: Yes.

COMMISSIONER KING: I just wanted to clarify, if there's a shortage - - -

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MR MERCER: It has been adjusted up as well, yes.

COMMISSIONER KING: Okay, thank you. Would that be in a situation where there's an unforeseen shortage for some reason?

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MR MERCER: Most times, yes. That can be an Australiawide situation. We have growers, our friends up in the north in Kununurra who have – we've had a truckload of produce coming towards us, something's happened in Sydney, the prices have gone up, they just ring up the truck, turn left, and the truck that we had booked in and sold and everything, it's just turned around left and headed over east.

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COMMISSIONER KING: I just wanted to check out that it was symmetrical. Final one, actually curiosity, you were discussing mandarins and holding back from the market for just a week, and you said – then hit the east coast school holiday period, does the east coast school holiday period mean higher fruit prices or lower fruit prices?

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MR MERCER: Lower. The same here. The – what happens in school holidays, it's getting more and more pronounced every year, the sophistication of the fast food outlets, supermarkets – sorry, the movies, all these sort of things just are getting so sophisticated, I think any spare dollars that they've got, mum is going into McDonalds and Greater Union, it's not coming to us. Their food – their eating patterns change when the school holidays start. Mum has to entertain the kids, has to do this, has to do that. Well, mum and dad, I should say.

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COMMISSIONER KING: You don't get the apples or mandarins - - -

MR MERCER: No, no, it just hits a – hits the brick wall, it just stops. Not completely, but - - -

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COMMISSIONER KING: Okay, well, we're going to have to ask those that are not associated with Mercer Mooney or the ACCC to leave, just in terms, Mr O'Donovan of letting our next witnesses know you'll be 10 or 15 minutes.

MR O'DONOVAN: Well, hopefully 15 minutes, but then perhaps we might break for lunch.

5 COMMISSIONER KING: Well, I thought we'd keep going. We'll do the next witnesses then which will be about 1 o'clock and we'll keep going.

MR O'DONOVAN: Yes, okay.

10 COMMISSIONER KING: So keep your mind on lunch.

COMMISSIONER MARTIN: I assume you'll be serving fruit?

COMMISSIONER KING: Who knows, it's been random.

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CONTINUED IN TRANSCRIPT-IN-CONFIDENCE

CONTINUED FROM TRANSCRIPT-IN-CONFIDENCE

5 COMMISSIONER MARTIN: Well, we will recommence the hearing. My name is
John Martin. I'm a commissioner with the Australian Competition and Consumer
Commission and one of the presiding members of the inquiry. My colleague, Dr
Stephen King, is another commissioner and member of the inquiry and welcome to
the Pastoralists and Graziers Association of West Australia and the West Australian
10 Meat Industry Authority, we have a representative from that, and the West Australian
Farmers Red Meat Focus. I think rather than go through the background, you've
probably heard and received paperwork relating to the background of the inquiry. I
will pass straight to Mr O'Donovan, Damian O'Donovan, who is from the legal area
in the ACCC to start the questioning and get you to introduce yourselves and your
15 other representatives.

MR O'DONOVAN: Sure. If just each one of you could introduce yourself, state
your name, state your position, and the organisation you're representing?

20 MR T. D'ARCY: Okay, thank you very much. My name is Tim D'Arcy. I'm the
chairman of the meat section of the Pastoralist and Graziers Association.

MR M. NORTON: My name is Michael Norton, I'm the current President of WA
Farmers Federation and have just moved up from the president of the meat section of
25 WA Farmers.

MR J. FRY: John Fry, I'm a producer at Donnybrook Breeding and Feeding.

30 MS R. PALISKIS-BESSELL: Renata Paliskis-Bessell, I'm the chief executive
officer of the Western Australian Meat Industry Authority.

MR O'DONOVAN: If your representative could introduce himself?

35 MR A. BURBURY: Yes, I'm Alex Burbury, policy director for pastoral and
livestock at Pastoralists and Graziers Association.

MR O'DONOVAN: Okay. Now, I will just - - -

40 COMMISSIONER MARTIN: Just, Mr O'Donovan, in terms of the logistics of
microphones there perhaps one or two of the people might be better off sitting over at
the other table, otherwise we're going to be passing the microphone. Would
someone like to sit at the other table, maybe Renata?

45 MS PALISKIS-BESSELL: The way that we've organised it is that Tim or Michael
will be doing a lot of introductory discussion and then John will be talking and I'll
just simply be assisting with the provision of notes along there so - - -

COMMISSIONER MARTIN: Okay, all right.

MS PALISKIS-BESSELL: Yes.

COMMISSIONER MARTIN: Well, look, see how we go. I just didn't want to crowd you all around the mike but see how we go.

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MS PALISKIS-BESSELL: Okay.

MR O'DONOVAN: Right. I just want to confirm that the witnesses understand that it is an offence under the criminal code to give evidence at this inquiry that a witness knows is false or misleading or omits any matter or thing without which the evidence is misleading. Do you understand that?

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MR D'ARCY: Yes, we do.

15 UNKNOWN SPEAKER: Yes, we do.

MR O'DONOVAN: All right. Now, I understand you would like to make a presentation before answering specific questions. Is that right?

20 MR D'ARCY: Yes, if I could, basically a brief overview of the submission that we put forward to you. The reason we've put the submission at very short notice was the fact that we had applied to the previous government for some funding to do a review of the whole meat industry from farm gate to the consumer plate, basically. That money was offered to us by the previous government but however, after the election, the razor gang got into action and that money was taken from us. So at fairly short notice we were offered the opportunity to be able to put a submission through to yourselves and that was predominantly put together by Alex, who is the policy director of the PGA and he has sourced a lot of his information at very short notice, as best he could, from around the traps so that's basically how we've come forward with this submission at this time.

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MR O'DONOVAN: All right. Is there any other introductory information you wanted to give us?

35 MR NORTON: Yes, if I may, Mr O'Donovan. My task was just to give a quick outline on how Western Australia is somewhat different to the east coast of Australia and I guess that will lead into some of your questions and some of the questions you have proposed, as pre this hearing. At a recent rally in Bunbury we asked the Meat and Livestock Australia to come and address us and to do that, they went and did a little bit of analytical research on the Western Australian market compared to the east coast of Australia. Surprise, surprise, we'd been telling them for some time, but they found that the Western Australian beef and sheep/meat industry is somewhat different to the east coast of Australia. We're about the opposite, actually, 60 per cent of turn-off on the east coast of Australia, especially for beef, is exported; 40 per cent of production or turn-off from farm gate goes on the domestic market.

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In Western Australia, it is quite different. In the case of cattle, some 40 per cent of the turn-off is exported live. Some 60 per cent – and that’s probably come down a little bit in recent times – of sheep meat is exported live. Of that – of the balance that’s left for cattle, the 60 per cent, 30 per cent is processed and exported, the other,
5 or it’s about 28 per cent, to be precise – the other 32 per cent is processed and sold domestically into the domestic market. Similarly, with sheep the bulk of the turn-off goes into the domestic market and the export market on the process side.

10 MR NORTON: We don’t have a lot of abattoirs here, but live export is quite pivotal to the red meat industry in Western Australia, which is somewhat different to the east coast, we have a temperate climate, we don’t have green grass all year, there’s only a very small window of opportunity to turn off quality livestock, and that impinges upon some of the dynamics of the Western Australia red meat industry.

15 MR O’DONOVAN: Mr Fry, did you want to?

MR FRY: I was here to – on behalf of PG & WAF. I was asked by them to present our cost of production, because it’s something that I have always been interested in within the industry. I’m a member of the Beef Improvement Association, and we’ve
20 always been frustrated by the fact that growers haven’t know their cost of production, so I probably plucked out as an example of someone who at least can attract the figures for the interests of the submissions. So that’s all I’m here to do, is to present my cost of production, together with a colleague of mine, to give you some idea of where we sit as producers right at the moment.

25 MR O’DONOVAN: Okay. All right.

MR D’ARCY: Could I just add to that if I may. When we asked John to come and put information together for us for this inquiry, we did it in the belief and in the
30 knowledge in Western Australia that John represents, and his friend, Matt Camarri, whose figures he has here as well, represents probably a group of the most efficient producers in WA, so you’ll see in due course the figures that they are presenting highlight the top end of the scale, and we thought that was pretty important, that you get to see how critical the issue is, because as you go further down the line, it’s
35 obviously the results are a lot worse for the lower end producer, if you like, and John will show you those figures in due course.

MR O’DONOVAN: Sure, okay. Look, I mean I think the first issue that we really want to get to is how the price is set at the farm gate, and I suppose – and so the first
40 question is, from a producer’s point of view, how is the price that they receive determined, and what are the options available to them to get a better price, if they’re not happy with what’s offered by one route?

MR FRY: In WA, we have a unique situation that we have a very seasonal supply,
45 because of the seasonal Mediterranean climate that we have. So virtually all the pricing is set, as far as we’re concerned, in the months of October and November, because that’s the peak supply period, and it’s before all the feed letters will move

into the market to source their cattle for the next six to eight months. Usually Woolworths as the primary supermarket will establish the price and then the other processors and IGAs and handlers will set their price very close to but in line with the Woolworths offer. So that determines, to a large extent, where we sit for a large proportion of the year, and this can be despite the fact that we might have massive increases in grain prices or cost of production, they'll say, well, we can source product from the east, we're not going to pay more than this particular price, so it's a bit of a negotiation thing between the one critical supermarket and a couple of key producers. I used to be a Woolworths supplier, so I knew exactly how that operated, I would talk direct with the meat manager for WA at Woolworths, and say, well, this is my cost of production, this is what we need to supply. It in fact was a good arrangement, because I had built in there, basically, 100 dollar a head margin, for the feed industry. Now, I believe it's back to 10 or 15 dollars a head, and it's just not – it's not in the interests of long term survivability to operate at that level.

MR O'DONOVAN: So just could you give us the time frame, the last time you had a direct negotiation with Woolworths?

MR FRY: It would be more than seven years ago, because I now supply out of supermarkets, because my specs don't suit the Woolworths trade, so I've had to move on from there.

MR O'DONOVAN: Sure.

MR FRY: But that's still how Woolworths will – to a large extent – negotiate the price with some key feed lotters.

MR O'DONOVAN: Yes.

MR FRY: Setting the feed lot price determines the store price, the wiener price, for the high quality cattle in the state. The other prices are set by live export and the export market in general, because – and the dollar is the main driver of that of course.

MR O'DONOVAN: Sure. Just going back to that negotiation that you'd have with Woolworths.

MR FRY: Yes.

MR O'DONOVAN: Sorry, can you just give me – what's the window period of negotiation?

MR FRY: It's basically two months, it's the beginning of the selling season of the wieners. Most of the wieners will start the selling in October, November. So those two months are very critical.

MR O'DONOVAN: All right. Why is it that Woolworths would – is ahead of the market in approaching people?

5 MR FRY: Because they are seen to be the better quality purchaser of cattle, so they know that they're going to be at the top end. They basically acknowledge that this is the price that we can go to to supply your cattle, and the others will settle around that.

10 MR O'DONOVAN: Right, okay. So in terms of – their approach to you is, is it, to fix the price at which they will take the cattle off your property that day, or is it to fix it for a period down the track?

15 MR FRY: Yes, fix it for the next six to eight months. Usually though until the end of the feed lot season, and in WA it's usually August, September. So it's virtually from January through until August that they will set the price.

MR O'DONOVAN: Okay. In terms of that negotiation, if you don't make terms with Woolworths at that time, what are your options?

20 MR FRY: You can speculate on the market, which usually means you're close to it, but usually somewhat less. Unless you can read the market and know that there's going to be an oversupply or undersupply, and that's the time in which you can proportion a number of contract cattle, and a non contract cattle. This year we could see the signs that – because of high grain prices, that it would probably be an
25 appropriate year to have non contract cattle, and in my case I had one third non contracted, two thirds contracted.

MR O'DONOVAN: So when you say contracted, a proportion of your herd to be sold over time?

30 MR FRY: That's correct.

MR O'DONOVAN: Over the following season to a supermarket.

35 MR FRY: That's right. We usually build in there the cost of production increases from month to month, which is something like five cents per kilo carcass per month through the selling season. So my weighted average for this year, which you'll see on my figures, is \$3.78 carcass, the price in fact starts at 3.75 and goes to 3.90, and I have heard of prices up to \$4 recently, and the spot market, I think, will go above \$4
40 very soon.

MR O'DONOVAN: Right. So just going back so I can understand how Woolworths determine their price. Their negotiation with you is about your production costs plus a margin for you?

45 MR FRY: That's what it has been.

MR O'DONOVAN: Yes.

MR FRY: But likewise, if it's too out of sorts with the eastern states, they will simply refuse to raise their price, and we will have to drop the store price in order to
5 match their price, and that's what happened this year when grain prices rose 130 per cent or something like that figure, and the margins for feed lotters dropped to zero, so they simply said, well, we have to pay less for the stores, and that made all the breeders jump up and down because they were getting so much less this year from the feed lotters than they have in the past. It sort of flows on through the industry.

10 MR O'DONOVAN: Right. Is that a product of the fact that east coast cattle can be fed on grass for longer periods, whereas - - -

MR FRY: Certainly, certainly.

15 MR O'DONOVAN: So the price of grain impacts much more adversely on a WA
- - -

MR FRY: That's right, and I believe also when drought prevailed in most of the last
20 five years in the eastern states, that depressed the store price, and actually gave the feed lotters in the east a greater margin than what it did in the west, because we had high store prices and we were competing basically in the same national market.

MR O'DONOVAN: When you say "store prices"?

25 MR FRY: Store is the trade – the animal that goes into the feed lot to be fattened.

MR O'DONOVAN: Right.

30 MR FRY: Just a general name of store.

MR O'DONOVAN: Right. When we're talking of farm gate price, are we talking prior to entering a feed lot, the farm gate price?

35 MR FRY: That's correct.

MR O'DONOVAN: So from your point of view, you can either sell to a feed lotter or sell to a supermarket or sell through a saleyard?

40 MR FRY: A lot of people do sell what they call the vealer, straight off mum, into the supermarket at the same time, October – September, October, November, period. Those cattle that are unfinished are usually traded, either to a feed lotter or to a restocker, who is wanting to carry them over for another year, so that there's a small market for that, but nearly all the prices negotiated at that time of the year in Western
45 Australia, it's quite a critical period.

MR O'DONOVAN: Right, okay. But in terms of what are the key drivers of price, it sounds like it's effectively the Australia wide commodity price?

MR FRY: It is, yes.

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MR O'DONOVAN: The expert alternative provides a – I suppose, puts a floor in it, if you can do a live export?

MR FRY: That's correct, because there can be a reasonable amount of substitution with meat. When I mean substitution, I mean, in a pleasant way. They can put more of the heavier bodies into the export market or bring the export cattle back into the local market, depending on supply and demand.

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MR O'DONOVAN: Does the high exchange rate at present mean that the export market is now much less attractive in Australian dollar terms?

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MR FRY: That's right. In fact, I was quoted only yesterday as saying that for the export cow market, export bulls and Fresian steers, which is a fair proportion of the cattle sold in the south west, we're actually on the same price as we were 15 years ago.

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MR O'DONOVAN: That's a product of exchange rate problems?

MR FRY: That's right. Yes.

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MR O'DONOVAN: Yes. All right. So looking at it from the context of this inquiry, would it be fair to say that what we see in the market is not Coles or Woolworths exerting market power but simply responding to the fact that it's a national market in their dealings with you?

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MR FRY: That's absolutely correct.

MR O'DONOVAN: Right. So you don't feel that because - the fact that they have such a high market share is – that's not what gives them the power to tell you that they're not going to pay that for your cattle, it's the fact that they can import it from the east at a cheaper price?

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MR FRY: Largely that is correct. There is some negotiation power there. If they can understand clearly where we sit, we believe we can get more cents per kilo out of them. I feel that we failed in recent years to be able to communicate that cost of production to them accurately.

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MR O'DONOVAN: Sure. Do they compete against abattoirs for you supply or compete, I guess, ultimately with sale through saleyards?

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MR FRY: They certainly do and that's mainly in the vealer market. The people who sell vealers direct to the butcher at the same time as the feedlotters are sourcing

their steers to fatten or their animals to fatten, the prices of both those markets react with each other.

5 MR O'DONOVAN: Right. Okay. So I don't know whether you've seen a copy of the commission's Red Meat Report but it more or less concluded that it didn't think that Coles and Woolworths had a significant enough share of the red meat market to be able to manipulate the market. Would you agree with that?

10 MR FRY: I do agree with that. A lot of people don't.

MR NORTON: Mr O'Donovan, it depends on market forces, it depends on a whole range of things. If Japan and Korea and the US are going well and the only real way that we can exert pressure on the supermarket is to keep them shorter product. If we can keep them shorter product by exporting it offshore, then they have to actively
15 compete. In this year because of drought, because of US product coming back into Japan, there was a lot of product drifting back onto the domestic market which gave them the opportunity to not have to over-exert themselves in the way of price. So it's a very complex thing and one works against the other. Sometimes it works to our favour, sometimes it works against us.

20 MR O'DONOVAN: Now, in terms of, I suppose, the break-up of the margins within the supply chain, there's - I suppose, part of the public complaint that led to this inquiry was that there was now getting - the gaps between what were being paid for commodities at the farm gate was very low and what was being charged at the -
25 by the retailers was very high. Now, the conclusion in the red meat report was that the saleyard prices were not the best ways of determining what exactly the supermarkets were paying for their beef - so, firstly, I guess I'll ask you is - are the saleyard prices a reflection of - usually a reflection of what's happening at the farm gate or is it because Coles and Woolworths buy the higher grade of meat and a
30 higher quality product, that the price that they're paying isn't really reflected in the saleyard prices.

MR NORTON: You should answer that one.

35 MS PALISKIS-BESSEL: Do you want me to answer that one? Yes, if we look the prime product, it's fair to say that saleyards do not put a selling in the market for the trade prime product. That readily goes into the supermarkets. However, with the store product, that is the product that is yet to be fattened, it is fair to say that given the volume of store product that goes through saleyards that saleyards do set the
40 market price for that segment of animal.

MR O'DONOVAN: Right. Am I right in saying a store animal - there's a lot more that needs to be done on a - - -

45 MS PALISKIS-BESSEL: Yes, they need to be finished. In other words, they're unfinished. They might be, say fat score 2 over a range of where, say, fat score 3 would be an acceptable fat score to go straight into retail. A store animal might be a

fat score 2 or fat score 1, so – so they needed to be finished off by put on grass or put on grain to then to be suitable for the trade or for the retail trade.

5 MR O'DONOVAN: Right. Okay. So if I could just take you to your submission, to table 1 in your submission. It reproduces a breakdown of the costs in the meat supply system that the supermarkets have told us that they have and effectively, I suppose, shows the wastage from a live animal at the farm gate through to packaged meat as it's sold at retail. Again the conclusions in the red meat report is that the supermarket margins were not very high but they were actually quite, you know, 10 three, three and a half per cent was the sort of margin that the retailers were getting. Now, do you think that's correct or do you think that the margins – that the gap between farm gate price and retail price isn't a product of all this additional processing but is, in effect, a product of supermarkets charging more because - a larger margin for themselves?

15 MR D'ARCY: Well, firstly if we look at that chart that was 2005 chart. There are some corrections needed on it. Where it says at the top, "Kilograms of saleable meat", in actual fact that is the live weight of the animal so I don't know where they got that from. I think we generally feel there's some inconsistencies in the recording of some of those figures and if you look at the processing factor and the retail sector, 20 there is a doubling up of some of the issues there, processing, boning, primal packaging etcetera, etcetera. If you look, it happens in both sectors and I think there's a question – we have a question mark as to whether there's not a doubling up of activities in that paper that brings the costs of the processing to the final retail shelf, if you like. I think there needs to be a lot more work done on that submission 25 to come up with some actual figures that I think – that we think are probably more accurate than they currently are.

30 MR O'DONOVAN: Right.

MS PALISKIS-BESSEL: Yes, just on that, what we will do is that we will provide a – in our view, a revised table on what we view the prices to actually be, starting from costs of production because we see that there are considerable inconsistencies. For example, if you have a look at the farm gate price, under number 1, we were 35 thinking with those sort of prices, we were thinking they must be steers and cows. That is the older animal that traditionally does not go into the retail trade. So we will submit as a supplementary report to this commission a revised table which will reflect what we believe the prices actually are.

40 MR O'DONOVAN: All right. Now then, looking at, I suppose, the end of the process, the retail level, our assessment has been that something like 50 per cent of the market is still through independent butchers which would seem to place a substantial constraint on the supermarket sellers and would keep the margins within competitive levels. Do any of you have a reason to think that butchers wouldn't 45 operate as a competitive restraint on the major supermarkets given the market share of independence?

MR NORTON: In a lot of the work that Cattle Council has done with meat and livestock of Australia, we've certainly encouraged MLA to support the independent butchers to try and – and MLA have done a lot of work with our levy dollars in making the independent butcher segment of the retailing sector much more cost-effective and proactive than they have been and as we've seen in the past, that those independent butchers have actually taken market share off the bigger supermarkets. Be that as it may, we as producers can't affect in any way, shape or form the retail price and while they may well compete strongly amongst themselves, if there's a big enough margin at the other end for all of them, there's no law on this land that says that they have to repatriate X amount of dollars or cost of production and a profit margin back to producers and the fact that some of the big supermarkets actually set the price, which we think a fair bit of fat in their management level compared to the smaller butchers, there's enough margin in the retail sector for some of those independent butchers to do extremely well with the supermarkets with all their extra overheads and costs, to all get along quite well but as I said, there's no law as to what they have to pay us.

MR DONOVAN: Sure. So in terms of the structure of the market, do you see that there's a weakness in the structure of the market which, if it was changed, would deliver more returns to you?

MR FRY: I personally think the greatest weakness is the transparency. We don't know exactly what margin the retailers and wholesalers are putting in there and I have some doubt about the figures that are presented here. For instance, the yield figure that Coles quoted is 65.33 percent. I rang Woolworths last week and I said, "What was your yield for this week's kill?" and they told me 73 per cent. That's too big a disparity to, you know, for it to be appearing here and I believe that difference adds nearly a dollar a kilo of saleable meat to the cost by underquoting the yields. I can't say that they're deliberately underquoting. I would be shocked if they were but to have that difference really surprises me and yield is such a big factor because we – I mean, we're all used to talking in terms of live weight.

You can see the dollar ninety five up the front there. We now talk in terms of carcass and I mentioned \$3.78 carcass but very few of us will talk in terms of what the producer gets for the saleable yield and my costs of production actually shows that return to the producer and it's something like 5.32. This figure of \$6.26 is three years old so I'm suggesting that it's not correct.

MR DONOVAN: Okay. Now, in terms of your alternatives, if there is money to be made, if there are big margins being earned higher up the chain, are there not alternatives for you in terms of who you sell to, where competition for your product is such that you can get a better return from another sector which earns similar or better returns than - - -

MR FRY: Not really, when supermarkets in WA dominate 70 per cent of the market. The only scope, I believe, is in fact for producers to take ownership of their product further down the chain. In other words, go into the processing, the

wholesaling and the retailing themselves and that's a massive investment and it frightens a lot of producers.

5 MR DONOVAN: Now, in terms of how the independent supply chain works, do you enter into contracts with meat processors who supply the independent butchers or is it the part of your herd that's kept off contract, that then supplies independent butchers?

10 MR FRY: A lot of, in my case, the herd is actually contracted. Both the feedlotter, the stores and the cull cows, the cull bulls, are all at a fixed price before I will sell those animals. Is that what you're asking me?

15 MR DONOVAN: Yes. And will some of those contracted animals ultimately end up in an independent butcher?

MR FRY: Quite likely, yes.

MR DONOVAN: Right. But through a feedlotter or - - -

20 MR FRY: That's right. I in fact supply Johnston Meats and I know that they supply restaurants in Perth. They supply some of the IGA stores and some of the hotels like Burswood Casino and presumably the Duxton and places like that. So there's a big market out there for the meat that is processed by Johnston Meats on my behalf.

25 MR DONOVAN: Sure. And so does Johnston Meats operate an abattoir or do they buy - - -

MR FRY: No. They just bone out and package.

30 MR DONOVAN: Right and so what product do they buy in the market?

35 MR FRY: They buy carcasses from myself or from a shared ownership abattoir. I think the owners of Johnston Meats in fact are the same owners as – or I think he's a brother of Western Meat Packers, who are another big operator – and they share the abattoir so there presumably is a small profit in them for the processing side of it. Johnston Meats will then ship the carcasses to their operation in Midland and from there they're boned out and distributed around the city and around the state.

40 MR DONOVAN: Right and so effectively the abattoir operation is almost a fee for service operation?

45 MR FRY: That's right, yes. We've actually asked them to consider killing the beasts in another abattoir in order to save us freight costs but their margin in processing their own product makes them insist on us supplying their abattoir and not another abattoir.

MR DONOVAN: Right. Okay. So presumably there are a number of these meat distributors that service independent butchers, the food service industry, who compete for meat with the major supermarkets. Is that right?

5 MR FRY: Yes. Probably Mike could answer that better.

MR NORTON: That's part of the problem in Western Australia. There aren't a lot. You know, we have two major export operators being at Harvey and John just referred to one of them, Western Meat Packers but when you go back to domestic
10 abattoirs, there's only about six altogether and one of them supplies Woolworths so there's not a lot of competition out there and growers are fairly fearful to go from one to the other because if you get out of step or you upset them, you're out in the cold and you've got nowhere to go and the sale yard doesn't, unfortunately like it used to, set the price because there's not the amount of competition there and the
15 various markets are quite specific in the type of cattle they need. You know, Tim's a pastoralist and all his cattle go on the live export market. We feedlot and we're all sort of locked into our various market niches and you're fearful to upset anybody or get out of step, otherwise you've got nowhere to go.

20 MR DONOVAN: But at the time the carcass goes through the abattoir, is it owned by someone other than the grower or does the grower sometimes retain ownership?

MR NORTON: Most of the cattle in Western Australia are traded over the hooks, so they're your cattle till they go over the hooks and they're weighed and that's
25 where the change in ownership and most of them are sold on a grid process, so depending on how they grade as they go down the line and how they hang up in the chiller, meat colour and fat colour, will determine what you get paid. So the final payment is not made until they go through that chiller assessing process so that's where the ownership takes place.

30 MR DONOVAN: All right. If in a given year you were unhappy with what you had been given by the abattoir at the end of that process, what are your alternatives?

MR NORTON: Not great.

35 MR FRY: For non-contract cattle, you do have the alternative of going to a processor direct or through an agent to another outlet. So there is the alternative but of course with the contract of cattle, you are obliged to continue to supply and they will, I mean, they've threatened us many times legally if we don't supply with what
40 they want, what we've agreed to supply in other words.

MR DONOVAN: Right. But at that stage the price has long been agreed, has it not?

45 MR FRY: That's right. Yes.

MR DONOVAN: So there's not concern that at the end of the slaughtering process, you're going to – no.

5 MR NORTON: Provided you meet the grid, the grid specifications and sometimes funny things happen with the grid, depending on the grader.

MR DONOVAN: Sure and so if you don't make the grid, what happens?

10 MR NORTON: Yeah. You get heavily discounted.

MR D'ARCY: This year it has been highlighted that people wanting to have service kill for their own product have had to wait any periods up to three months and consequently what happens in that period then, your beast that you're feeding goes out of spec and consequently your price goes down accordingly and there's quite a lot of that happened in this last 12 months or so.

MR DONOVAN: Okay. Is the arrangements the same with the supermarkets, that the change of ownership occurs after it's gone through the abattoir?

20 MR FRY: As Mike said, it actually changes ownership at the point of weighing, where it meets the various specifications which are agreed to prior.

MR DONOVAN: If you're dealing with the supermarket, do they effectively guarantee you a slot in the abattoir at the right time?

25 MR FRY: Yes. Certainly within a day or two any way, it's – they have to because they know just how many animals will fall out of spec if they don't agree to take them when we've agreed to supply.

30 MR O'DONOVAN: Sure.

MR NORTON: Now, that can be a bone of contention at times. If there's a heap of cattle coming out of the feed lots, you will find your killing dates slip backwards. If they're short, you're killing date can come forward, or sometimes you can get a frantic phone call in the afternoon to say that we want them tonight for tomorrow. So it's all about supply and demand at the end of the day, and how good your relationship is with the people you're dealing with.

40 MR O'DONOVAN: Right.

MR NORTON: That's – it's quite critical.

MR O'DONOVAN: Now, the impression that I get is there doesn't seem to be a particular problem caused by large concentration of market share in retail by the supermarkets? Is - - -

45 MR FRY: Except that they don't understand the cost of production.

MR O'DONOVAN: Sure. But viewing it from their perspective, if they can source meat more cheaply from places that have lower costs of production it's not surprising that they do. Would you agree with that?

5 MR FRY: It's not - - -

MR NORTON: It's part of doing business in this state and you either learn to live with it or you go and do something else.

10 MR O'DONOVAN: Sure. If this inquiry is being conducted at a time when the Australian dollar was 45 cents instead of 90 cents, would the industry be in different condition and pricing at the farm gate be different?

MR FRY: I would say no doubt about that.

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MR O'DONOVAN: Right.

MR FRY: Because it is a major driver of a price in Western Australia because our live export markets are to poorer countries, Philippines, Malaysia, etcetera, who simply can't afford to buy the product when it's too expensive with a strong Australian dollar. Of course, it makes us uncompetitive with the US who is our major high quality supplier into Japan and Korea so the involvement of the – having an industry that is so export-oriented, we are very subject to exchange rates.

25 MR D'ARCY: I think if I could just highlight too, there is a fact there that – and we were discussing this earlier, but we talk about the CPI today being at somewhere between 3 and 4 per cent. At the farm gate, it's generally considered your CPI is anywhere between 10 and 20 per cent because of things like your fertiliser, machinery parts, all that type of thing. We all know that, you know, there's no relationship whatsoever to the CPI that's publicly announced all the time.

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MR O'DONOVAN: All right. Now, I suppose I've been given the profit and loss statement for a great southern beef producer. I was wondering whether there was any particular features of it you wanted to bring out because, I mean, as a document it's not easy for me to understand. Was there any things in particular you wanted to bring out about - - -

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MR NORTON: That's why we brought John.

40 MR FRY: What I've tried to do here is demonstrate the mix of product that any one producer might have. So you'll see we actually had 476 weaners and they made up roughly half of the income that our farm earned for the year. But the other proportion is made up of culled cows, culled bulls, mated heifers, some not-in-calf heifers and some traded steers. So when the season is good we usually trade a few more steers, when it's poor we trade a few less. So you can see that there's a mix of animals which means a mix of carcass weights, yields, etcetera, and I've tried to demonstrate that the mixed price that we achieve this year is in fact \$1.42, which should be

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highlighted on that total line as dollars-per-kilo live weight, \$1.42. I hope you can see that?

MR O'DONOVAN: Yes.

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MR FRY: Alongside 316,102 kilos of meat – of, sorry, live animal. Okay? So that's the miss of weaners, culls, etcetera. Further down you'll see heifers.

MR O'DONOVAN: Can I ask one question?

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MR FRY: Sorry, yes.

MR O'DONOVAN: Is there any specific product line that supplies domestic beef to

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MR FRY: Yes, the weaners in fact are the animals that go into the domestic market. Virtually no cows, bulls, mated heifers, not-in-calf heifers, would go into the domestic so they're all export prices. It's reflected in the actual cents-per-kilo. You can see \$1.56 is the live weight price for the weaners, the culled cow price is 85 cents, the culled bulls' price is \$1, the mated heifers \$1.50, etcetera, to average \$1.42 for the mixed bag. Okay? Further down we've got live weight coming off that total which is the purchased animals. In other words, some of the animals that we bought in to trade, in other words, comes off the total production to give us around that 260,000 kilograms of live weight produced by the farm. Okay?

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I've put in the cost of production and it shows a total of \$1.60 in my herd. In the Camarri herd it shows \$1.80, and that's not unusual to have a variation like that. So we believe that we're currently operating in my herd, about a 20 cents a kilo live weight loss and in his herd, something more than that. But that is also taking into account a return on the capital invested in the breeder. But it does not take into consideration any investment we have in the land, which is our major investment. For instance, about \$15,000 per breeder is invested in land but because our land is constantly going up in value – and I think I heard it mentioned earlier that Donnybrook is a lifestyle area, where I live – so we have a five per cent compound rate of growth in our land which keeps us surviving.

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COMMISSIONER MARTIN: Well, thank you very much for that and I appreciate you coming in and giving such a good overview of the situation. The only question that I – remaining question I had: it was put to us in terms of the quality of red meat at the supermarkets being represented as fairly high quality product, that to some extent what you see on the supermarket shelves is then a mixture, that it's maybe not all feed lot type product.

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MR FRY: Absolutely.

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COMMISSIONER MARTIN: Do you have view on that and this whole issue that meats at retail is not really graded? I have met people who have described it in that particular way.

5 MR FRY: It's a real shame that our industry has invested – we as producers have invested in a grading system to Meat Standards Australia which you have probably seen advertised. Three, four and five star quality cuts. So much of our beef will qualify even four or five star and we will never see it promoted as such. It is treated as a threshold, it has made three star and that's it. The supermarkets have their own
10 grading system and therefore have not adopted MSA in order to promote the product as being of such and such an eating quality and, therefore, deserves this price. That has detracted from the consumer's consistency of quality.

15 They will, in fact, use MSA as a means of discounting when they are sourcing the carcasses but they will not promote the cuts on the shelf as being graded to meet this three, four or five star standard and that's a real shame when we have invested so much in the industry.

20 COMMISSIONER MARTIN: And is it also, apart from being a shame in terms of giving the maximum return there, do you think a bit misleading for consumers?

25 MR FRY: It certainly is. People don't understand the cuts. They know that scotch fillet is a very good cut and that will nearly always grade five star but it will very rarely be shown in a shop as being a five star cut. Rump, for instance, is a three star cut which can sometimes grade four star. If they saw that rating, they would treat it differently, I'm sure.

30 COMMISSIONER MARTIN: But say within the scotch fillet there would be some that has been treated differently to other scotch so scotch fillet itself would not all be the same?

MR FRY: No, that's right, you can get scotch fillet out of a cow, of course.

35 COMMISSIONER MARTIN: Of course, yes.

40 MS PALISKIS-BESSELL: And there is the occasion which does occur quite a bit where you might see advertising or a poster for Meat Standards Australia product on a retail shelf. Immediately underneath you would think, as a consumer, that there is Meat Standards Australia product. There is not and quite often there are cases where older product is actually substituted for and described as younger product. That occurs at various components along the – various sectors along the supply chain as well. That results in the consumer being overcharged for their product and that does occur.

45 COMMISSIONER MARTIN: Thank you very much, thanks for coming in.

ADJOURNED

[2.01 pm]

RESUMED

[2.38 pm]

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COMMISSIONER KING: Right, let's get started again. Right, welcome back after the lunch. Now, we have the representatives of the West Australian Farmers Federation (Grain Focus) in brackets afterwards. Now, you've all received a copy of the document we sent out to witnesses at this inquiry? So you're familiar with that. Okay, so without further ado Mr O'Donovan, I'll hand it over to you to ask the witnesses to identify themselves for the record and start asking questions.

MR M. NORTON: Mike Norton, President of WA Farmers Federation.

MR J. BREHENY: I'm Julian Breheny, I'm the Executive Officer for farm business and transport and previously to that I was the Executive Officer for grains

MS C. BRIDGER: I'm Clare Bridger, the current Executive Officer for grains.

MR O'DONOVAN: All right. Can I just confirm that you each understand that it's an offence under the Criminal Code to give evidence at this inquiry that a witness knows is false or misleading or omits any matter or thing without which the evidence is misleading. Do you understand that?

MR NORTON: We do.

MR BREHENY: Yes.

MR O'DONOVAN: Okay, all right, now was there any opening statements you wish to make in addition to the submission that you gave to the inquiry in relation to grains?

MR NORTON: Just a very quick one, if I could, Mr O'Donovan. We thought it was appropriate to do a submission so far as grains is concerned, bearing in mind that 90 per cent of the wheat out of WA is exported, but there is quite a lot of feed grain and feed wheat used in the beef industry, the dairy industry, certainly the pig industry and the chicken – chook industry and so that certainly has flow on effects to those industries which we are members for and the fact – the thing that always galls us when the price of bread goes up we always blame the drought and Julian will talk more in depth on that one.

MR O'DONOVAN: All right, well, just in relation to that, there are some calculations there about the contribution of the price – relative cost of grain and its impact on the price of a loaf, were they calculations that the WA Farmers Federation did?

MR BREHENY: Those calculations there were done by AgForce Grains and they're contained in the AgForce Grains submission, but we have done a calculation similar to that, but our calculations were done in about 2004/2005 and their calculations – our calculations came out very much similar to that as to the
5 percentage of the amount of wheat in a loaf of bread and therefore the cost of the loaf of bread, but probably in relation to the current situation where there has been large movements in the price of grain and particularly in the last 12 months we thought it was probably more relevant to use those figures.

10 MR O'DONOVAN: Sure, okay, but from the information that you have you are satisfied that those calculations are broadly accurate?

MR BREHENY: Yes, we are.

15 MR O'DONOVAN: Okay, all right. Now, in terms of the things that set the price of grain, I mean we've proceeded on the assumption that it's an internationally traded commodity that has a price set internationally. Is that true for WA grain production?

20 MR BREHENY: Yes, well, the – wheat in particular. Wheat is probably anything that's traded through a futures trading board, so wheat, corn, soya beans, they tend to be the price setters for other areas of grain due to the ability to be able to price forward the grain over a long period of time and therefore there's probably greater market information flowing to all participants. I guess as far as Western Australia is
25 concerned the price of grain here as in the Eastern States is set by whatever the import or export parity is.

MR O'DONOVAN: Right and there are no special features of the WA grain market that cause it to depart radically from those - - -

30 MR BREHENY: I think that we can – well, as in the situation last year there was very high prices in the Eastern States, because there's a far larger domestic market in the Eastern States and it is also quite expensive to ship grain from here to the Eastern States, so while you can have exceedingly high prices in the Eastern States that's not
35 reflected in Western Australia due to the cost of transport from here to the east coast and most of our markets are export markets are in Asia. But, we – the size of the West Australian domestic market is as Mike said, is quite small, I think we only – as far as wheat's concerned we only mill about – for flour, about 160,000 tons and
40 between 500 and 600,000 tons goes to feed. So yes, I mean our market is very much set by what our international customers are prepared to pay.

MR O'DONOVAN: Right and in terms of the major customers for wheat are they bread – plant - bakers in Australia, like George Weston Foods.

45 MR BREHENY: In Western Australia probably the biggest milling customer is George Weston Foods, who operate wheat milling operations in Western Australia, Quaker Oats who operate milling operations in Western Australia and most of that

goes overseas and also West Feeds and Mill and Agri Feeds, who are big feed producers. There are a number of other small feed producers, but they're the two major ones in the market.

5 MR O'DONOVAN: As far as you're aware is there a competitive domestic market for flour or is it – is there important competition on domestic flour?

MR BREHENY: Well, there obviously would be some flour imported from the Eastern States, but that figure of 160,000 tons has been a fairly competitive, fairly
10 standard figure for quite some time, it's just – I mean, it doesn't – Western Australian grain supply too has traditionally been quite a bit steadier than the Eastern States due to rain patterns. If you look at the continual – the supply out of Western Australia it's actually been steadier due to seasonal variation sort of over the last sort of 15 to 20 years and only being a small percentage of that supply it's been a fairly
15 steady amount of milling grain.

MR O'DONOVAN: Okay and in terms of the ability, I suppose, of a flour miller to supply its product to manufacturers, there's presumably a competitive – we've got no reason to think there's not a competitive market in the market for supply of flour and
20 fresh food products to manufacturers?

MR BREHENY: Well, no, there's more than one flour miller in Australia, so I can't see why they would be any different to any other market in Australia.

25 MR O'DONOVAN: Sure, all right. Now, I gathered from your submission that there was some desire on the part of the Farmers Federation to see action directed towards, I suppose, smoothing out the volatility in the markets. Is that the primary focus of the submission?

30 MR BREHENY: In the past – well, our organisation has supported statutory marketing based on the need to smooth out pricing and that's been one of the major issues, what I was trying to make the point of and it's been made in a number of the submissions that I've seen both on the website and from people presenting today, is that any time there's a – and I made the point in here as well – is that any time there
35 is something that impacts on the abilities of farmers to produce, whether that be a frost, a flood, a drought, you know, seasonal climatic variations, there seems to be a willingness of both marketers and to a degree the media to reflect any possible cost rises back to those seasonal variations, but from the figures that we produced here it would indicate that those seasonal variations or the farmers – the cost received for
40 farmers due to the actual ingredients, the raw materials in the cost of production, doesn't tell the whole story and I understand that in the new cycle it's particularly easy to just single out one thing. I mean, people – you don't – when they put out a news headline they don't go into an enormous amount of analysis, especially on an evening news bulletin, but unless there's a better understanding of the supply chain -
45 I mean, from the costs that we've got here, we've said that it's – it basically shows that only 14 per cent of the actual cost of the rise is attributable to the raw material.

Our concern is that if people in the community see that cost being sheeted back to something on farm all the time, then they will feel that any cost rises are just responsible in farmer's incomes, and therefore we are seeing there are sort of rising costs, yet farmers aren't benefiting, but I get the picture that perhaps people who are off farm are getting the picture that, you know, any time there's a price rise, it's greedy farmers, and I don't feel that that's – there's a distinct city country divide at the moment, and there's a distinct lack of understanding about farming procedures outside of – from people who are consumers to the people who are the producers, and I think this is just symptomatic of that.

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MR O'DONOVAN: Sure. So apart from the information you've already given us about, I suppose, the relative contribution of wheat to the price of a loaf of bread. Do you have any other specific information, has the WAFF done any specific research on other costs in the chain that have changed or does it have any information that would be of interest to us in terms of assessing the competitiveness in other elements of the chain?

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MR BREHENY: No more than, sort of, has been provided by other producers in terms of the cost price squeeze that we are seeing from inputs, I mean, the rise in the cost of fertiliser, the rise in the cost of fuel, the rise in the cost of pesticides, herbicides and of labour, and that there seems to be, when you look at real returns to farmers, they're actually dropping, yet my concern was that they were – that wasn't being adequately reflected back to farmers, the only time they ever see about farmers is a possible price rise in the city which doesn't actually bear – well, there's not a great relation to the – to what is actually happening. As far as the competitiveness, I don't – I mean, there's all sorts of theories that maybe the supermarkets are price gouging, I don't whether that's the case, and I don't want to make that accusation, all I'm wanting to say that unless there is a – in this report – unless in this report, contained in this report is some way that we can explain supply chains probably a bit more thoroughly somehow, then I don't know whether that there's a great deal of benefit to it.

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MR O'DONOVAN: Sure.

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MR BREHENY: But if you want, we can sort of try and provide some more information, I can probably provide some more information that we had in our figures that we did previous to the figures that I've provided here.

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MR O'DONOVAN: All right. Now, and in terms of the, I suppose, specifics that the WAFF was interested in looking at, in terms of I suppose policy change, was looking at exploring a policy that can smooth the road, as it were, how it's expressed, which I took to mean that there was words addressing in some way the volatility. This is in the – just under conclusions in the – basically the last two lines and then the top of the next page.

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MR BREHENY: Okay.

MR NORTON: Are you talking about education, Mr O'Donovan, or perhaps some other thoughts that we've had in relation to some of your comments on national competition policy and changes and government policy?

5 MR O'DONOVAN: Well, I suppose I'm trying to understand what – whether there was a specific policy proposal that WAFF had in terms of – I think it's specifically directed at alleviating the boom and bust cycle in agriculture.

10 MR NORTON: Yes. I'll answer if you like. We continually get asked for solutions to problems, and it's all very well to have – get the brand – the whinging farmer, the politicians and academics and bureaucrats say well, what's the answer, we're certainly – even though our organisation comes from a supporting of the statutory marketing, quite obviously that's after national competition policy has been in place for some time, you know, all those statutory marketing authorities have basically
15 been wiped out or removed, and we're not complaining, we're not saying you shouldn't reinstate them, but in the discussions that we have had looking for ways and means as to how we can make a more effective, more transparent process between retail and producers, ACCC certainly look after consumers. But there's nobody really that – in Government or within legislation that looks after the poor old
20 suppliers, the producers. It's the law of the jungle out there. We've been to Andrew Murray and the senate had numerous inquiries, you know, looking at this very issue, and we have the data, not with us, but certainly we can get that later. You know, Senator Murray said that, you know, there are recommendations that have made to the parliament of ways and means as to how suppliers can be protected. The major
25 parties haven't seen fit to take those recommendations up from a number of senate inquiries, and we are sort of focusing on those, we are not legislators, we're not experts, we're just farmers that can relate to you as to what the marketplace is doing to us. I think probably – that's probably where we should start to look, look at some of the senate inquiries, some of the recommendations have been made to the two
30 major parties as to how we might, you know, alleviate the inequity that currently exists.

MR BREHENY: Well, if I can just make a point. In regards to the conclusion here, and I wrote it, I think probably in regards to the ACCC, whose imprimatur, as it
35 were, is to – and there's that phrase again – is to be the – sorry, to implement the Trade Practices Act and the things that run the Trade Practices Act. I guess for – in this purpose, this would probably be quite, sort of, femoral to this inquiry, and probably would have been better directed, had it been a Government inquiry at senators, sort of along the lines of the comments that I made in submission that I
40 wrote to the senate to that inquiry on fertilisers which I only just put in the other week. I think the sort of comments that I'm sort of edging towards here is that the – I mean, it's been – it's quite a topical issue at the moment, food, it's the UN came out and made some fairly alarmist hysterical comments last week about how it's unethical that we have biofuels and that, you know, people are starving all over the
45 world. Well, you know, it's not exactly news. But I think that because agriculture seems to suffer from this continual boom and bust cycle, and it's quite volatile, yet we are probably facing a situation in the future where there will be significant

resource issues, then we perhaps need to be focusing on ways to make it more sustainable, but again, I think that's something better directed towards actual members of parliament who can make those decisions rather than to the ACCC, whose job it is just to be the watchdog, as it were.

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MR O'DONOVAN: Sure. All right, just the only other thing I was going to take you to is in Agforce's submission, their assessment of the grains market was this. The market is transparent and works well, there are many marketing options available to farmers from immediate cash sales to forward contracts, and swaps to pools, which suggests that, I suppose, there are privately available options in terms of things that farmers can do to ameliorate grain risks. In broad terms, would you be supportive of that assessment of the grains market?

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MR BREHENY: I – just think about this answer.

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MR NORTON: Do you want me to answer?

MR BREHENY: No, I'm happy to answer it. Our policy in the past has been to support, as I said, statutory marketing, feeling that that was the best way forward for farmers, but the – and in Western Australia, it's a little bit different to Queensland and New South Wales because of the size of the domestic market, but we encourage farmers to manage their risk and to look at all options in the market on the proviso that they take advice or professional advice, and obviously we can't provide that, we don't have financial services licenses. But I think that the market in – for grain now is, well, there's some appropriate checks and balances being put in in the wheat market and so on, but I would tend to agree with the comments made by Agforce, yes.

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MR O'DONOVAN: Okay. All right, well, that's all I have.

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COMMISSIONER KING: My only comment was, before you go, talk about potential policies with politicians. Don't forget what happened with going back to – when was it? In the 1980s, was it, and the mess that ended up with the farmers, but that's gratuitous - - -

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MR BREHENY: Well, that – I guess, yes, I guess that comments relates to – I mean, reserve price and statutory marketing, and we've made the comment a number of times today that we don't want to see that sort of intervention in the marketplace.

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COMMISSIONER KING: When you say smooth?

MR BREHENY: I agree. I know that the reserve price scheme – and I don't agree with the reserve price scheme and you wouldn't find too many farmers who agree with the reserve price scheme but – in hindsight. But - - -

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COMMISSIONER KING: Because of the amount of cost - - -

MR BREHENY: But I just find it interesting and I don't come from a farm. I don't have any farming background but I do find it interesting that while – there's been some fairly brutal changes in agriculture over the last 10 or 15 years and it seems to be, there's a lot of people leaving farming, an enormous amount of people leaving
5 farming and they're not going back and those skills are being lost, that human capital it's being lost. Now, as resources become more scarce and I don't want to be an alarmist or anything like that, I'm not going to – I'm not on the peak oil band wagon or anything like that or global warming. But as these things do become more pressing issues food security will again become an issue and I think that that's
10 something we're already seeing.

COMMISSIONER MARTIN: Thank you very much. Thank you.

15 COMMISSIONER KING: All right. Mr O'Donovan, you're ready again. I'm just noticing very – between the Macgregor's and O'Donovan's and - - -

MR O'DONOVAN: Yes.

20 COMMISSIONER KING: A Celtic themed afternoon.

MR MACGREGOR: That's right.

COMMISSIONER KING: I'm Stephen King and – welcome, gentlemen.
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MR I. MACGREGOR: Thank you.

COMMISSIONER KING: You will, I hope have received a letter about the procedure and processes of the inquiry and of this hearing so I won't run through
30 that. I'll simply ask if you could state your names and positions for the record and then I'll hand over to Mr O'Donovan.

MR I.MACGREGOR: Yes. Fine. Iain Macgregor, Managing Director of Mrs Macs Pty Ltd.
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MR R. MACGREGOR: I'm the National Sales and Marketing Manager for Mrs Macs Pty Ltd.

COMMISSIONER KING: Okay. Firstly, have you been summonsed to appear here
40 today?

MR R. MACGREGOR: Yes.

COMMISSIONER KING: All right. Can you just confirm that you understand that
45 under the Commonwealth Criminal Code it's an offence to give evidence at this inquiry that you know to be false or misleading or omits any matter or thing without which the evidence without which the evidence is misleading?

MR I. MACGREGOR: That's understood.

COMMISSIONER KING: Okay. Great.

5 MR O'DONOVAN: And it's probably worth while just to continue to say if in response to any question you feel that your answer would be – reveal confidential information then please just let us know and - - -

10 MR I. MACGREGOR: Yes, we will. We're aware of that. Thank you.

MR O'DONOVAN: - - - you can keep it to a confidential Okay. All right. Well, can you just describe briefly to us what it is that Mrs Macs does in terms of what it produces and what it sells and who it sells to?

15 MR I. MACGREGOR: Right. Well, the background is Mrs Macs is a third generation family owned business. It's a totally Australian run business and we manufacture, we specialise in manufacturing a wide range of pastry products which we market throughout Australia and New Zealand and into Asia.

20 MR O'DONOVAN: All right. In terms of the marketing of it do you sell it all directly into the outlets that retail it or - - -

25 MR I. MACGREGOR: No. Our and I'll ask Rob to come in from time to time because that's his side of it, the sales and marketing, but essentially we are more aligned towards food service so we often don't, we don't have a direct service outside of Western Australia into food service outlets. That's done by a distribution network. We have some retail business in terms of the major supermarkets but the main influence is on the food service side.

30 MR O'DONOVAN: Okay. In terms of the actual product range that you have, is it just meat pies or is it - - -

35 MR I. MACGREGOR: No, no. We have quite a range of pie products, the usual that you would expect to see and some that you wouldn't but we also have a range of pasties, sausage rolls and some other products which are in the pipeline for development.

MR O'DONOVAN: Okay. Are they all marketed under the Mrs Macs' brand?

40 MR I. MACGREGOR: No. We have two or three different brands that we market under and Bakewell is one, Mrs Macs is another and Red Embers is a third and these are all market specific products.

45 MR O'DONOVAN: Okay. On the retail side is any of it sold through the frozen section of a retail store?

MR I. MACGREGOR: Yes, it is.

MR O'DONOVAN: Okay. In which supermarkets would we find them?

MR I. MACGREGOR: Well, you'll find them in Coles, Woolworths, IGA and some small independent - - -

5

MR O'DONOVAN: Right. Okay. So they're packs of frozen meat pies primarily or is there another product.

MR I. MACGREGOR: Yes, there are and in the local market here in Perth there are some fresh products as well but outside of WA they're frozen. Yes.

10

MR O'DONOVAN: Okay. As a proportion of your business what proportion is sold through that retail line?

MR I. MACGREGOR: I was going to suggest that if we get into market share and prices we would rather deliver that privately if you don't mind?

15

MR O'DONOVAN: Yes. No, that's no trouble.

MR I. MACGREGOR: So I'm quite happy to come back to that question but perhaps in a slightly different environment?

20

MR O'DONOVAN: Sure, no trouble. All right. Then in terms of your - I understand that you supply Coles Express with pies?

25

MR I. MACGREGOR: That's correct.

MR O'DONOVAN: All right. But that's not, I suppose, strict retailing that people don't buy, they're not frozen pies or room temperature pies which the customer then takes home?

30

MR I. MACGREGOR: No. They're sold - I mean, we supply a lot of the P & C sites outside of Coles but they're - - -

MR O'DONOVAN: I'm sorry, "P & C"?

35

MR I. MACGREGOR: Petrol and Convenience.

MR O'DONOVAN: Yes.

40

MR I. MACGREGOR: That's part of the food service area so it's not specific to Coles, we supply Woolworths as well and the products are invariably sold as a hot product.

MR O'DONOVAN: Right.

45

MR I. MACGREGOR: Ready to eat.

MR O'DONOVAN: Okay. Do you supply the oven and the other things that go with - - -

5 MR I. MACGREGOR: Yes. In many cases we do, not all. In some cases some of the bigger stores have their own bakery equipment but in most cases we supply the equipment as well.

10 MR O'DONOVAN: Right, okay. Then in terms of the manufacturing process I assume that the products are manufactured by Mrs Macs?

MR I. MACGREGOR: Correct, yes.

MR O'DONOVAN: Okay. You require raw materials for this?

15 MR I. MACGREGOR: Yes. We have the whole process from start to finish.

MR O'DONOVAN: Okay. All right. Talking then in terms of how you buy firstly your ingredients and particularly your meat products, who do you approach for them or what is the market that's available for that product?

20 MR I. MACGREGOR: Okay. We have several wholesalers that we deal with because of the quantities that we go through which are fairly substantial. This is bought on the spot market, there's no tendering process because of the nature of the industry. In other cases, in other suppliers of raw materials it invariably goes to
25 tender.

MR O'DONOVAN: Right. So in terms of meat are there multiple suppliers who you can switch between if pricing is not keen.

30 MR I. MACGREGOR: We don't have a great choice. We do use multiple suppliers but as I said the volumes are sufficiently substantial that we actually require all those suppliers.

35 MR O'DONOVAN: Right, okay. In terms of where your suppliers fit within the beef supply chain, are they effectively vertically integrated meat producers or do they acquire product from abattoirs and then process it to your requirements?

40 MR I. MACGREGOR: Yes. That's what – effectively what they're doing. They're wholesalers and they have links to different abattoirs and they process the meat from the abattoirs. Yes.

MR O'DONOVAN: Right, okay. Now, in terms of your other products, I assume – are we talking about basics like flour and eggs and milk and those products?

45 MR I. MACGREGOR: Yes. Not so much eggs and milk but flour, margarine, vegetables, et cetera. They're all big material users for us.

MR O'DONOVAN: Right. There are acquired through a tender process, is that
- - -

5 MR I. MACGREGOR: Yes. Outside of meat they do go to tender and we purchase
on that basis. They're quite competitive.

MR O'DONOVAN: Right. Again, are you approaching vegetable wholesalers or
are there specialist consolidators, I suppose, that you can - - -

10 MR I. MACGREGOR: Yes, there are. We normally process through a group who
actually process the vegetables themselves. So we buy the vegetables processed, we
don't buy the meat in processed other than in the sides in the trim and the steak, et
cetera, which we process ourselves because we have to have a very good idea and
understanding as to what the meat consists of so we do it ourselves.

15 MR O'DONOVAN: Right, so you actually – and so the vegetables that you get
aren't in raw form, they've already had something done to them?

20 MR I. MACGREGOR: Yes, sometimes they're – some vegetables are blanched, but
effectively they're in their raw form and they're cooked as a result of our own
process.

25 MR O'DONOVAN: Right, okay. Now, looking at meat first, in terms of the cost of
it as an input to your process, has it changed substantially in the last - - -

MR I. MACGREGOR: Look, meat prices do vary, yes. In most years you will find
literally an up and down movement. Sometimes that's cyclic, depending on the time
of the year. In winter for instance farmers tend to hold their supplies back a little bit
so the meat prices tend to rise and outside of that they come back. The meat prices
30 can also be influenced by demand, of course. If there's substantial overseas export
then that can drive prices up and as I said previously we do purchase on the spot
market, so we are influenced by those prices.

35 MR O'DONOVAN: Right and is it a reasonably transparent market, as in you know
that you're getting the market price?

40 MR I. MACGREGOR: To the best of our knowledge I believe so. I'm not quite
sure what the intent of the question is. If you're referring to potential collusion
amongst suppliers, I've no evidence of that at all.

MR O'DONOVAN: No, no, I guess it was just in terms of whether you could
determine whether a particular supplier was giving you an appropriate market price
it's easy for you to verify it?

45 MR I. MACGREGOR: Yes, we're reasonably confident of that because of the
multiplicity of suppliers, so you can actually weigh one off against another and draw
comparisons like that.

MR O'DONOVAN: All right, is there any relationship between what you see in terms of the retail price of meat and the price that you source it out at wholesale levels?

5 MR I. MACGREGOR: To be honest we pay very little attention to the retail price of meat. We're strictly wholesale and in quantity, so what's happening on the retail side is actually outside of our interest and knowledge.

MR O'DONOVAN: Right, okay, and then in relation - - -

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MR I. MACGREGOR: Sorry, if I can just add there one point to that too. We use a different type of meat to what you would find in say the retail sector. We use a beef trim, we do use steak, etcetera, but it's manufacturing grade not your fillet steaks and your porterhouse steaks, etcetera.

15

MR O'DONOVAN: Right, okay and I suppose – I was going to repeat the question just in relation to your vegetable acquisitions. Again, is that –s there's a market which is transparent and you can I suppose trade one supplier off against another

- - -

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MR I. MACGREGOR: Yes, up to a point. I mean, it's not a case of playing one off against the other specifically. There are limited suppliers of processed vegetables in WA. You've probably heard that the Com Group, who is a major supplier to the local market here, is closing down and moving offshore. They have been a good supplier to us over a number of years, so we'll be looking to alternatives in those circumstances.

25

MR O'DONOVAN: In terms of the trend – in terms of your input prices – actually there's one additional – I assume flour is a big input?

30

MR I. MACGREGOR: It is indeed, yes.

MR O'DONOVAN: All right and in the last two years?

35

MR I. MACGREGOR: Yes.

MR O'DONOVAN: Would it be fair to say the price has doubled?

40

MR I. MACGREGOR: Probably about 40 per cent to be honest, 40 to 50 per cent from our point of view.

MR O'DONOVAN: All right and were you exposed to that market?

45

MR I. MACGREGOR: Yes.

MR O'DONOVAN: Yes?

MR I. MACGREGOR: Yes.

MR O'DONOVAN: So you don't have long term acquisition contracts in flour?

5 MR I. MACGREGOR: No.

MR O'DONOVAN: No.

10 MR I. MACGREGOR: The contracts are relatively short, they'll cover a two year period and that's it.

MR O'DONOVAN: Sure, okay and in terms of vegetable pricing, has that been increasing in the last five years?

15 MR I. MACGREGOR: Yes, it has, yes, vegetable prices have increased and I think now you're getting into the areas of drought affected crops and demand pushing prices up, but yes they have.

20 MR O'DONOVAN: Right, okay and to a level higher than general inflation within – based on published CPI or - - -

25 MR I. MACGREGOR: Look, I – that's a hard one off the top of my head to be honest. I'm quite happy to supply you with the answer, but I just can't – I wouldn't be prepared to say it was higher than CPI.

MR O'DONOVAN: Sure.

MR I. MACGREGOR: I think it is, but I'm not sure how much.

30 MR O'DONOVAN: Right, okay and as a proportion of the ultimate sell price of a product, how much of it is raw materials, just an estimate?

35 MR I. MACGREGOR: Probably about – anything between 25 and 30 per cent of costs are tied up in raw materials.

MR O'DONOVAN: Sure and what are the other major costs.

40 MR I. MACGREGOR: Sorry, but we're getting into some information here again, which I shouldn't be – I'll strike that from the record.

MR O'DONOVAN: Yes, sure, all right. All right, I'll leave specific questions about cost ratios for the time being. All right, now, at the other end you obviously interact with the supermarkets at the retail level?

45 MR I. MACGREGOR: Yes.

MR O'DONOVAN: Now, just in broad terms I don't need to know the specifics of supply terms, but what's the process for setting them, how do you get yourself onto – how did you get yourself onto the supermarket shelves of the major supermarkets?

5 MR I. MACGREGOR: Well, I'm going to let Rob answer that, it's time I had a little break.

MR O'DONOVAN: Sure.

10 MR R. MACGREGOR: Well, some of it's extremely historical and dates back, we've been dealing with the supermarkets here in Western Australia specifically for over 30 years, so times have changed a little bit in terms of the dealings with
15 retailers, but certainly the process now is pretty much a question of submitting your products at various times of the year when tenders are open and by which you obviously include a price and product detail and effectively trading terms, they facilitate that, so and obviously at that point it's open to negotiation, pretty much, from both sides, as to exactly what's required to get your product range within any various retailer and inasmuch as that it's pretty standard through the whole group.

20 MR O'DONOVAN: Yes.

MR R. MACGREGOR: A whole lot of them.

25 MR O'DONOVAN: All right, and is it part of a specific range of view that you submit these things – submit these details?

MR R. MACGREGOR: Yes, more often than not, yes, but on occasions they do make allowances from time to time, depending on their needs, I guess, whereby they might approach us and actually ask us to submit a product or a range of products in
30 between those respective timeframes.

MR O'DONOVAN: Right and when they're conducting a range review are you just competing against other pie manufacturers or is there, I suppose, broader competition for retail space in the freezer section of a supermarket.

35 MR R. MACGREGOR: Yes, a bit of both there. Obviously, you know, whether it's pizzas, pies, anything that's in that sort of frozen food category, everybody's trying to vie for the most – the best facings they can get, so inasmuch as that, yes, but generally when they're looking at the pie category of which we fit into, whether it be
40 pie, pasty, sausage roll, it's all sort of called the pie category for the use of a better term, effectively we're up against our immediate competitors, yes.

MR O'DONOVAN: Right, okay and the – so this way of ranging is primarily associated with the major supermarkets, Coles and Woolworths, is that what you're
45 describing or does it also exist in

MR R. MACGREGOR: No it extends itself to the independents, the IGA Metcash type groups, so some of the – what used to be, I suppose, the smaller retailers and now not so small collectively, so, yes, they pretty much operate on the same basis.

5 MR O'DONOVAN: Right and so when your – when the independents are ranging, do they range through – do you have to deal through Metcash or do you have to persuade sub-groups of the independents or each independent supermarket individually?

10 MR R. MACGREGOR: Yes, you actually do both on that basis with that particular group, you actually apply to head office level with Metcash to get ranging, but that doesn't guarantee you ranging throughout the entire group necessarily, because you do have groups within the group and sometimes they will require you to pay additional moneys, irrespective of what you're paying at head office level to actually
15 range a product.

MR O'DONOVAN: Right, okay and in terms of completely independent retailers, is there such a thing?

20 MR R. MACGREGOR: Yes, there is and that's almost a fine line now between convenience and what we have typically referred to as retail, it's sort of a fine line now between dividing the two, but certainly where you do have – what we call the IBOs, independent business operators, anyone that fits that profile, yes, there is still the ability to deal with the mums and dads at face value and deal on that basis, which
25 is a completely different environment, obviously.

MR O'DONOVAN: Sure, okay and does the concept of a published wholesale price exist for you or do you renegotiate each set of terms specifically with each?

30 MR R. MACGREGOR: No, you pretty much – it's horses for courses. Every case is individual in terms of negotiating, there's no set – we can have a recommended price, obviously, but outside of that it's just – the price can often be the same, but it's really what's coming off the bottom end, you know, in terms of rebates, coops, promotional discounts, etcetera - - -

35 MR O'DONOVAN: Yes, okay.

MR R. MACGREGOR: - - - which ultimately affects obviously the purchase price one way or another.

40 MR O'DONOVAN: Sure, okay. Now, I was wanting to ask you questions about your decision not to tender for generic contracts. Is that something that should be done privately?

45 MR I. MACGREGOR: Yes.

MR O'DONOVAN: All right, I think that was all that I had for the public session.

COMMISSIONER KING: I think it's a good time to head into private session, so if I can ask everyone who's not connected with either Mrs Macs or the ACCC, if they could please leave and some of you we'll see you in Bunbury tomorrow.

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CONTINUED IN TRANSCRIPT-IN-CONFIDENCE