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Policy Forum Article

Australian–Indonesian Live Cattle Trade—What Future?

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Abstract

Australian live cattle exports were a growing \$1 billion trade from northern Australia to Indonesia for finishing and slaughter for Indonesian consumers. This all changed in recent years with the trade being disrupted by a series of constraints which have shrunk the trade and raised uncertainty. Will it ever get back on trend or continue to shrink and disappear? Greater integration between Australia's live cattle trade and Indonesia's cattle feeding and processing industries through investment and technological transfer offers the potential of not only better meeting Indonesia's beef security but also strong processed meat opportunities in rich neighbours to the benefit of both countries. A continuation of the recent volatile and uncertain trade will be detrimental to both countries, with Indonesia losing a food-secure, reliable livestock supply to which value was added, and Australia a significant industry for one more dependent on costlier markets.

Key words: live cattle trade, policy analysis, economic analysis

1. Introduction

Australian live cattle exports to Indonesia were a growing \$1 billion trade of young cattle bred in northern Australia being shipped to Indonesia for finishing and slaughter to provide meat to Indonesian consumers. There was a parallel trade of generally higher quality beef from cattle slaughtered in Australia, mainly supplying premium markets such as international hotels and restaurants.

This all changed a few years back with the trade being disrupted by a series of trade constraints and bans described next which have shrunk the trade, raised its uncertainty and associated costs such as the costs of capital, as well as discounted market prices due to the decreased reliability of supply. The direct costs of the Australian ban have been estimated at over \$500 million just in the short term and would be much larger in the long term, taking into account indirect costs such as on the loss of Australia's reputation as a reliable supplier (DPMC 2011). What is the trade's future? Will it get back on trend or continue to shrink and eventually disappear? These questions are analysed in what follows, which includes evidence-based policy analysis of various recent policy recommendations that have been put forward to overcome the current uncertainty in the trade.

2. Constraints, Bans and the Uncertainty

Although Australia exported live animals much earlier, in the 1980s there was a strong growth in live cattle exports in response to growing Asian meat demand via feedlots and

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the development of associated export infrastructure to handle this trade (Farmer 2011). The main problem in the Australian–Indonesian live cattle trade until recently was that Indonesia began to constrain the trade, administered by restricting the number of import licences and trading ports, along with other non-tariff barriers. Constraining the trade was driven by a cattle and beef self-sufficiency objective that has failed to be achieved on numerous occasions since it was made a key objective in 2005. In Indonesia, imports are often seen as a threat and a failure of government to stimulate domestic production, rather than an opportunity to free up resources to do more of what they do better. The policies used, which also included producer credit subsidies to stimulate production, have been ineffective. To be effective, the policies would need to be exorbitantly costly economically, either from restricting competitive trade and/or the huge size of the stimulating subsidies required (estimated in joint Australian National University, University of Adelaide and Indonesian Ministry of Trade research to be of the order of \$5 billion over 5 years for 90 per cent self-sufficiency (the cost of increasing the subsidy from 2 per cent to 70 per cent of industry production to reduce import demand to 32 per cent of base levels—see Figure 1) (Vanzetti et al. 2010)).

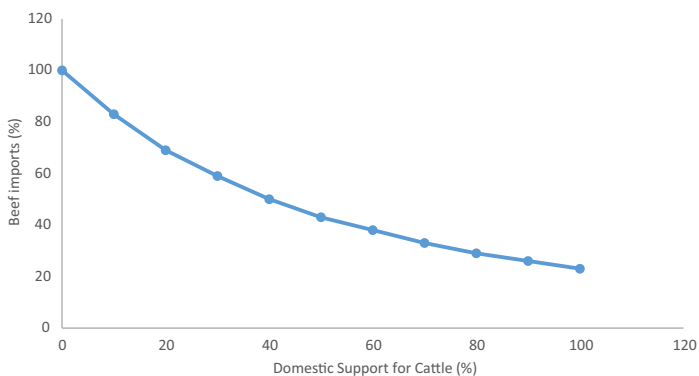
Then in mid-2011, the Australian agriculture minister put a ban on Australian cattle exports to Indonesia following some public

reactions to an Australian Broadcasting Commission program that showed some cruel behaviour towards cattle in Indonesian abattoirs. Like any trade constraint, this had a high cost for both countries, threatening a valuable live trade, but particularly to the instigator, Australia, with its reputation as a reliable supplier of commodities also being destroyed.

Trade constraints and bans often signal a lack of ideas or an attempt to constrain market forces that are driven by the more vocal or influential rather than the majority or evidence-based policy analysis. The recent trade constraints and bans on Australian live cattle exports to Indonesia seem a prime example of this situation (Trewin 2011a, 2011b). These trade constraints and bans are the result of sensitive domestic non-trade issues, like self-sufficiency in the case of Indonesia or animal welfare in the case of Australia, dominating trade policy, a situation that was criticised in Productivity Commission (2010).

The Australian live cattle trade was and, following the ban, is now even more animal welfare friendly than other traders so banning or making this trade harder worsens the overall world animal welfare situation. Moreover, the Australian legislated monitoring approach (DAFF 2013), which mimics approaches that were being undertaken by some of the industry, in conjunction with animal welfare improvement programs, provides more information on the supply chain and improved

Figure 1 Beef Imports (% of Base Level) and Domestic Support (% of Industry Value) for Cattle



Source: GTAP simulations, Vanzetti et al. (2010).

marketing. However, with different cultural norms and traditional practices, the integration of such monitoring, which has failed in Australia on occasions, is not an easy task.

Indonesia's reaction once the ban was removed, following the imposition of specific animal welfare-related conditions and the outcome of a Senate enquiry on the issue, was over 2012 to further cut cattle import licences and maximum weight limits as well as beef quotas, impose new uncertain documentation requirements (e.g. on breeding validation), and to involve Indonesia's logistic agency, BULOG, in the supply chain. These changes increased the rents involved in getting market access and the risks of corrupt behaviour. Few countries will respond positively to threatening and embarrassing bans; in fact, they generally do the exact opposite as Indonesia did in this case with associated high economic costs and worse animal welfare outcomes, as was predicted in Trewin (2011b).

More recently, in the last weeks leading up to Ramadan in mid-2013, when beef prices were rising rapidly and threatening food security, the Indonesian Ministry of Trade overrode the Ministry of Agriculture and increased meat quotas and cattle import licences, at least in the short term, although the late decision meant not all the imports could be delivered. They were also put in charge of a one-stop shop formed to allocate import licences. Following Abbott's first overseas visit as prime minister to Indonesia in October 2013, which involved Australian cattle industry leaders, new licences or permits for 75,000 head over October–December 2013 were announced. This is still short term with little notice (8–12 months would be ideal), and the permits may not all be taken up given the downsizing of the northern cattle industry in response to negative market signals like the lower weight limits and reduced quota, plus the dryer season. It was also announced that a proposed reference price mechanism (import will be increased if prices get too high) is still being determined due to some technical issues, but this will face the same short-term problems unless very good forecasts of the Indonesian market can be made.

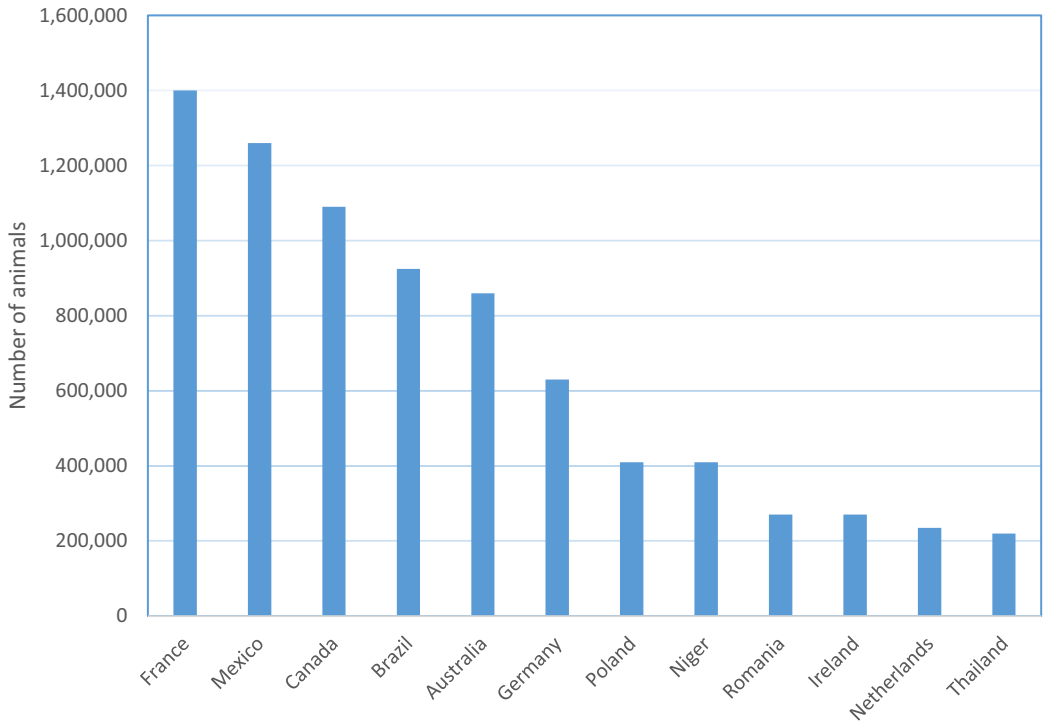
Most recently, it has been suggested that the Indonesian live cattle trade could be used as a bargaining tool, not in some trade deal but inappropriately in non-trade issues like the recent diplomatic sensitivities over phone hacking in Indonesia. The Australian–Indonesian live cattle trade is now a lot less certain than it was before these developments, with confidence and investment having fallen dramatically, right throughout the supply chain, but especially in Northern Australia. The Australian Agricultural Company is planning to build an abattoir in Darwin, mainly driven by moving processing closer to the cattle and a growing Asian market, but in addition such vertical integration offers options for ensuring greater certainty in moving product along and smoothing out peaks and troughs in the supply chain.

3. The Australian–Indonesian Trade and Its Growth in a World Perspective

To give some perspective on the above developments in the Australian–Indonesian live cattle trade, which some opponents give the impression is a unique relic of the past and should be banned, over 100 nations are currently involved in significant live animal trade. France is the main live cattle exporter, holding 13 per cent of the world market (see Figure 2), and exporting mainly within Europe and to Africa, which is one of the major importers along with the Middle East. Australia holds 10 per cent of the world market and exported to 22 countries in 2012, mainly Indonesia prior to recent times and increasingly to countries like Vietnam and PNG.

Not only is live animal trade prevalent among many countries but the trend is that this trade is increasing. This trend is driven by a number of factors, many that are relevant to the Australian–Indonesian trade such as cultural norms; importers wanting more control over product in their markets; the potential for more 'real' jobs (not dependent on support or protection to prop up their employer) and other economic benefits from product that is processed in-country; and natural environment and infrastructure constraints that hinder

Figure 2 Live Cattle Exports by Country, 2010



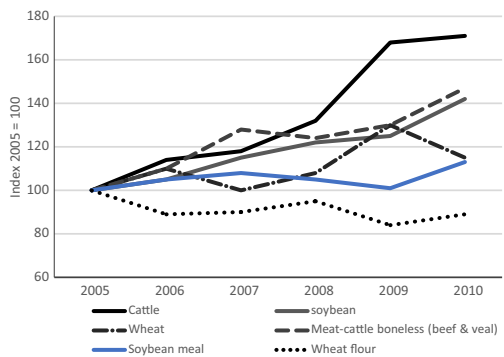
Source: FAO, AFI (2013) analysis.

efficient breeding and early raising of cattle, as well as the transport and storage of beef (e.g. refrigeration). This increasing trade in livestock is having large implications for trade in animal feeds and self-sufficiency in grains used for direct human consumption (see Figure 3 with animal feeds following cattle trade up, although at a slower rate).

4. The Usefulness of an Economic Framework Approach

When looking at the trade’s ideal future, an economic framework that includes evidence-based policy analysis proves particularly useful. An economic framework, unlike some other approaches such as extreme animal rights, can incorporate society’s tradeoffs between what can be competing objectives like animal productivity and welfare (McInerney 1991). These objectives are not always competing. Productive animal husbandry is depen-

Figure 3 International Trade of Commodities and Semi-Processed Commodities



Source: FAO, AFI analysis.

dent on good animal care. Animal production or trade with economic values will induce greater animal welfare to capture such values than if they had no economic value at all (see Figure 4—Point A). But at some point, production or trade might reach a stage where any increase would diminish animal welfare values

from some optimum value (Point B). It could even eventually reach a point where both production and animal welfare values decline (Point C), for example with overcrowding. Society's preferred tradeoff can be reflected in set welfare standards or through aggregate market outcomes driven by consumer sovereignty if they have the necessary information on animal welfare outcomes from specific levels of production or trade. Consumers would include non-market values in their decision, for example as with the purchase of higher priced non-cage eggs. Often, it is the political economy that holds sway over the outcome, but this can be highly influenced by transparent and factual information. For example, Minister Ludwig went against expert, including departmental advice, in his decision to ban the trade, which was not supported in any of the subsequent enquiries, suggesting that this was driven by the political economy which subsequently changed with information on the impacts of the ban on human and animal welfare, as well as the economy.

Another useful economic concept when looking at the trade is that of comparative advantage, defined as the ability to produce a particular tradable at a lower marginal and opportunity costs than another country, and is a comparative or relative concept as countries will still gain from trade even if one has an absolute advantage in all tradables because of the differences in relative efficiencies of production which promotes trade. The Australian–Indonesian live cattle trade has

comparative advantages in both countries trade that would make the trade very efficient. Australia has a comparative advantage in the extensive rearing of young cattle that has been revealed in its trade, especially in contrast to its close neighbour in Indonesia with its limitations of suitable land, appropriately skilled labour, disease controls, related and supporting industries, and conducive conditions. On the other hand, Indonesia with its lower wages and energy costs than Australia has a potential comparative advantage in economically efficient meat processing, not only for its rapidly growing market but for similar regional markets in smaller neighbouring countries without some of the factors favouring live trade or processing. This comparative advantage is yet to be revealed in actual exports, but this could happen quite rapidly with the right policies and know-how coming into Indonesia and drawing on cheaper inputs as has happened in other sectors like electrical products.

5. What Future?

If the Australian–Indonesian live cattle trade situation stays as it is with no policy responses, then the influences of the greater uncertainty and the trends mentioned above will induce a different future. Australia will build up its live trade as it has in recent years with neighbouring countries such as Vietnam (where meat demand is higher and growing more rapidly than in Indonesia, and supply the opposite—see Figure 5) and PNG, and the constrained and more uncertain trade with Indonesia will die away. Indonesia cannot rely on using the trade when it suits them as there will very likely be no cattle available with such an uncertain approach, and its food security will be badly diminished as was the situation leading up to last year's Ramadan. A long-term two-way trade and investment relationship between Australia and Indonesia is required.

Moreover, the trade in cattle cannot be easily converted to one in beef, as suggested by some. Processed meat will not necessarily replace live trade for the reasons given earlier that favour a live trade (see Figure 3 for the higher growth in cattle than in processed

Figure 4 Theoretical Relationship between Perceived Animal Welfare and Livestock Productivity

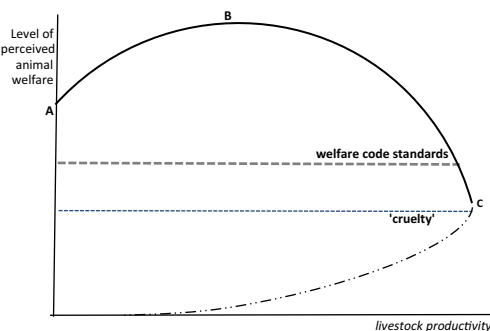
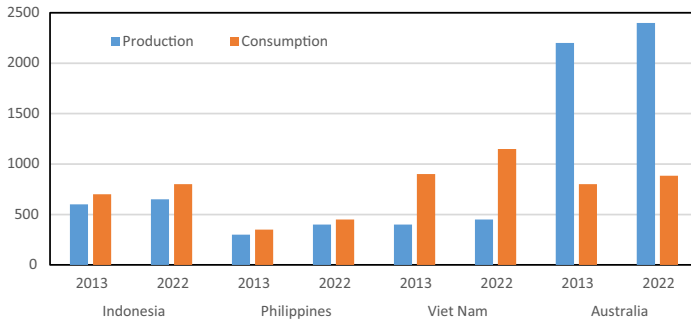


Figure 5 Supply and Demand Outlook for Beef in South East Asia and Australia

Note: p = projection.

Source: OECD-FAO, AFI analysis.

products). For example, beef from live cattle is a different product in a number of respects, including culturally, from that currently exported in boxes to premium markets in Indonesia. Australian unions and animal rights activists are pushing this option out of vested interest. But the economics do not stack up, especially when the animals are not bred for domestic processing, and ‘adding value’, that is not efficient or in demand, will cost markets and aggregate jobs economy-wide. Any differences between live cattle trade and processing in economic multipliers or dollars spent elsewhere in the economy as a result of a dollar spent on a specific activity (WSPA 2013) are irrelevant in such circumstances.

Australian policy should be to ban the bans as only then might its reputation as a reliable supplier be restored. The multitude of submissions to the Australian Senate (2011) and Farmer (2011) enquiries were standard formats from animal welfare groups, saying that the trade should be banned but all enquiries came out with recommendations that the trade continue with stronger animal welfare considerations. The World Trade Organisation is becoming more concerned with the negative impacts of export taxes, bans (an extreme of a constraining export tax) and like policies, and Australia should lead the way in addressing these concerns. Interestingly, Indonesia has constrained live cattle exports in the past as they have with palm oil and some other commodities in more recent times.

A better policy approach than a ban, as suggested in Trewin (2011b), would have been for Australia to remain engaged with Indonesia, trying to improve the situation with education in terms of better treatment of animals and building on decades of collaborative agricultural research between the two countries, including on policies, such as that developed by the Australian Centre for International Agricultural Research (ACIAR). Research funded by ACIAR has shown a high value of returns to both countries on research in improving this supply chain, but the imposition of a ban crudely discarded these gains. This approach is now being implemented.

If Indonesia wishes to persevere with its self-sufficiency policy, then that is their prerogative, but there are better ways than the current policy approach. A policy aimed at improving Indonesian productivity through research and development (R&D) on breeding and feeding was estimated to be far more cost-effective (Vanzetti et al. 2010) and could actually improved animal welfare. Such R&D is quite diverse, for example going beyond the farm into marketing, and could include humane killing, which is in a producer’s own interests, as a traumatic killing generally results in tougher meat sold at lower prices. R&D of this kind has been provided through non-government channels; for example, Australia’s Livecorp, in a world first, has been developing a strategic vision for improving animal welfare in Indonesia, and private companies such as Elders have

introduced animal welfare improvements into various stages of their integrated Australian cattle into Indonesian beef supply chain. Labelling of the resultant beef could capture this attribute and give consumers transparent information on the animal welfare aspects of the product, and they could show their preferences through their purchases.

A suggestion to give Indonesia 100,000 ‘cattle instead of cash’ aid will not be sustainable but just a short-term ‘bandaid’ for problems in Australia and Indonesia of excess supply and excess demand, respectively, that were caused by the trade constraints and bans. But what if these cattle were breeders as some proponents have argued that Australia should do, following New Zealand’s lead? But being breeders does not guarantee that there will be no animal welfare abuses, especially when the animals are eventually slaughtered, which is often sooner than later. Even in the longer term, if the cattle were breeders, this would upset the demographic balance of a sustainable herd where the natural increases in stock numbers equate with the desired turnoff. There are also questions on the relative rates of return of this type of aid versus other types like R&D and infrastructure (e.g. roads), as well as on its equity. Other issues that arise are the moral hazard of not fixing things as there could be another bail out, spillovers on the feed markets (like with biofuels), pressures on land use and so on. Stock numbers currently are strongly associated with imports, and it will be a slow process to replace this with domestic calvings, especially with the earlier mentioned factors that diminish any Indonesian comparative advantage in this activity and the higher pressures on female slaughtering.

Even Indonesia’s logistics agency, BULOG, which has been involved in a fairly unsuccessful pursuit of rice self-sufficiency for decades, has said Indonesia’s ‘ability to provide (cattle) domestically is insufficient’, and is investigating investing in Australian cattle properties as a source of reliable supplies of cattle as some private Indonesian cattle companies like Santori are already doing. This is a sensitive issue, but previous foreign investment in Aus-

tralian agricultural holdings, such as by the Japanese in feedlots, has proved very successful, including in the Australian industry and the broader economy. Prime Minister Abbott made this last point in a speech during his October 2013 visit to Indonesia, in which he encouraged Indonesian joint ventures in the Australian cattle industry.

A similar suggestion has been made in the other direction by ex-Prime Minister Rudd in respect of Australia investing in Indonesian red meat agribusiness, which will make the trade that has become uncertain as a result of various trade constraints and bans more certain. Vanzetti et al. (2010) suggested that joint investment of the two types just outlined could extend an efficient red meat supply chain into growing regional markets.

Greater integration between northern Australia’s live cattle trade and Indonesia’s cattle industry, along with banning the bans, offers the potential of not only meeting Indonesia’s food security objectives but also increasing processed meat export opportunities into rich neighbouring member states of the Association of Southeast Asian Nations, which could benefit all countries. On the other hand, a continuation of the volatile and uncertain trade over the last year or so will be to the detriment of both countries, with Indonesia losing food security-wise what was a reliable supply of livestock to which value was added, and Australia a significant industry to one more dependent on more expensive markets.

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