

INDONESIA AUSTRALIA RED MEAT & CATTLE PARTNERSHIP



Joint State of the Industry Report 2019

Summary

Indonesia and Australia enjoy a unique business partnership with respect to the cattle and beef trade. Feeder cattle produced in northern Australia are fattened and processed in Indonesian feedlots and abattoirs, a supply chain that has functioned successfully for over two decades. The market is underpinned by northern Australia's ability to efficiently produce feeder cattle and Indonesia's ability to fatten and process these cattle at relatively low cost. Australia also exports significant quantities of fresh and frozen beef for high-end markets and trim and offal for low end markets.

The Indonesia-Australia Partnership on Food Security in the Red Meat and Cattle Sector (the Partnership) is a bilateral initiative established in 2013 that aims to develop a competitive, efficient and sustainable red meat and cattle industry as part of a globally competitive supply chain. This Joint State of the Industry Report discusses the status of the industry in 2019, based on industry data, published reports, and consultation with key stakeholders. The influence of international competition from other sources of beef on the Australian-Indonesian red meat and cattle supply chain is also discussed.

Outcomes and factors impacting the industry in 2019

The Indonesia-Australia Comprehensive Economic Partnership Agreement (IA-CEPA) was signed in March 2019 and is due to be ratified for implementation in mid-2020. IA-CEPA is expected to bring numerous benefits to the cattle and red meat sector, predominantly relating to an elimination of tariffs and quota requirements. These are important outcomes for the industry and highlight IACEPA's importance to both countries.

Local beef production in Indonesia supplies about 45% of national demand. The deficit is supplied through imports of live cattle and beef from an increasingly diverse range of markets. Australia currently supplies approximately 75% of the deficit. In 2019, Australia shipped 676,433 head of live cattle, 53,050 tonnes of frozen beef, 4,587 tonnes of chilled beef and 36,821 tonnes of beef offal to Indonesia.

Rainfall Percentile Ranking

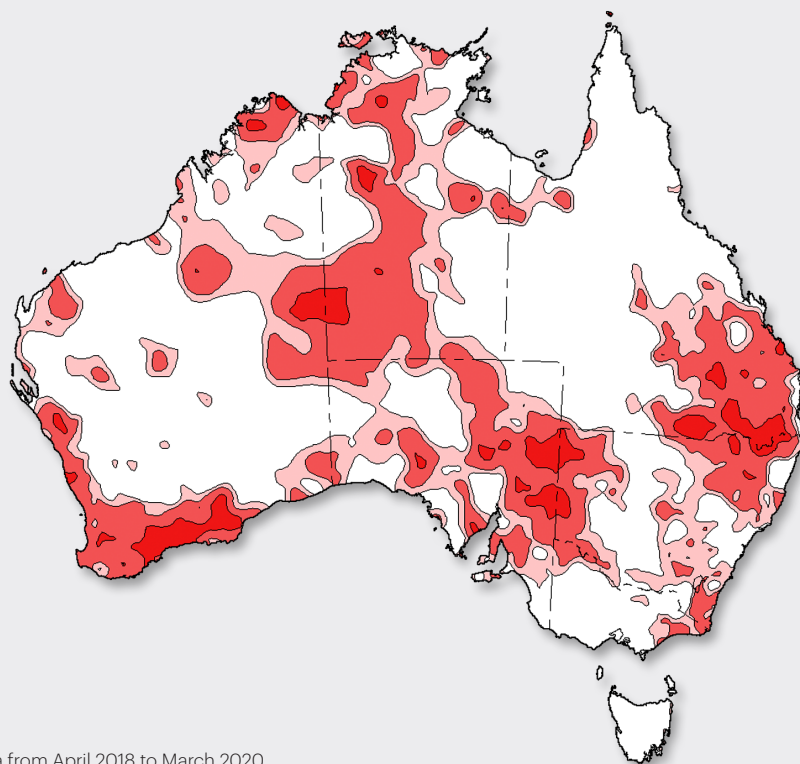
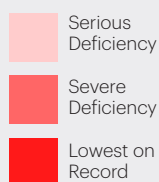


Figure 1: Rainfall deficiencies in Australia from April 2018 to March 2020

Long-term drought across much of Australia, combined with a devastating flood in Queensland in early 2019 significantly impacted the industry. 2019 was the hottest and driest year on record in northern Australia (Figure 1). Producers struggled with feed and water availability, leading to widespread destocking and lower cattle prices. At the same time, the Australian dollar fell against both the Indonesian rupiah and the US dollar, making terms of trade attractive for Indonesian feedlot businesses.

2019 saw the anomaly of a five year high in live cattle imports, whilst the Indonesian feedlot industry contracted, with approximately 25% of feedlots ceasing to operate. Those operators continuing to operate sought to take advantage of the weak Australian dollar and the relatively low price of Australian feeder cattle. This resulted in intermittent periods of oversupply in Indonesia and a flattening of prices for finished cattle, further reducing feedlot margins.

Over the past decade, Indonesia has introduced a range of policies to make the price of beef more affordable to its population. These include a price ceiling on beef, access for low-priced Indian buffalo meat into Indonesia, and a requirement for feedlot operators to import breeder cattle, among other measures. Whilst these policies have been beneficial for consumers, they have reduced operating margins for Indonesian feedlots. The impacts, in 2019, have however been lower than initially anticipated, due to the increasing consumption of beef driven by Indonesia's expanding middle class.

Australia exported large numbers of feeder cattle

Annual total live cattle exports to Indonesia

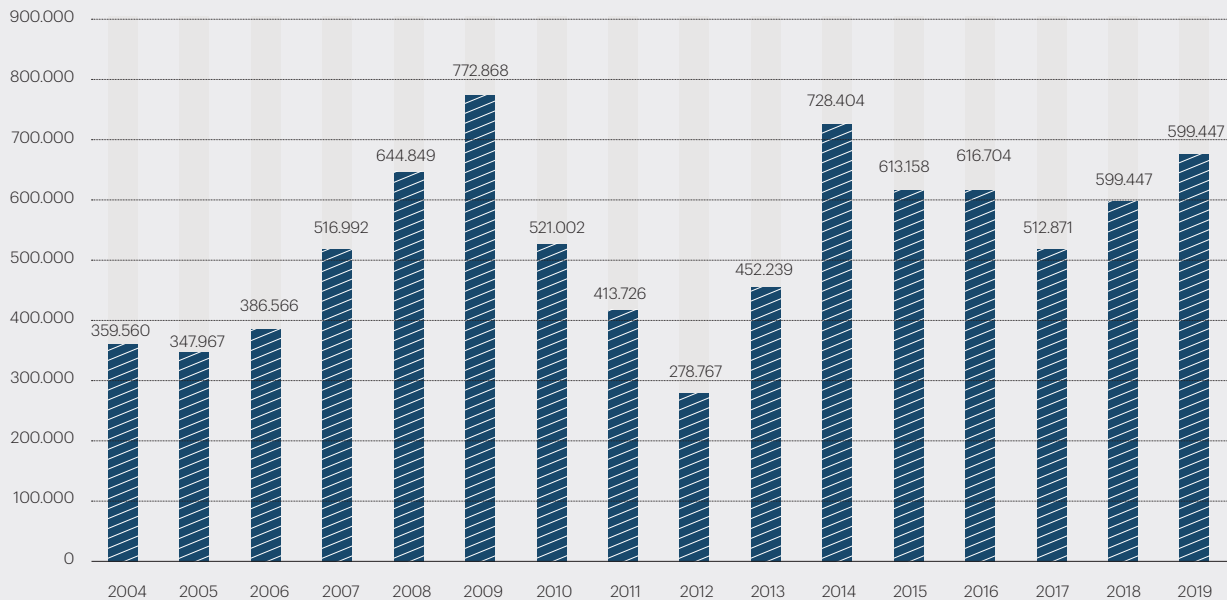


Figure 2: Annual live cattle imports by Indonesia from Australia since 2004

■ Head of Cattle



In 2019 Australia achieved a 5 year high in the number of cattle exported to Indonesia – 676,433 head Figure 2.



Indonesia was Australia's largest market for live cattle exports



Droughts across much of Australia and floods in western Queensland led to widespread destocking and the lowest cattle prices in five years



The depreciation of the Australian dollar against the Rupiah and US dollar favoured Indonesian cattle importers



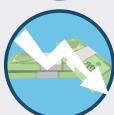
Exports from Townsville reached a similar number to exports out of Darwin, driven by the floods in Queensland.



Approximately 60,000 tonnes of beef were exported to Indonesia - a significant increase on the previous two years, with Indonesia ranking 5th in terms of beef exports.



The value of the Indonesian market was worth over AUD 1.1 billion to Australia



Australia's national herd dropped below 25 million (Figure 3) – herd rebuilding will cause cattle prices to increase and remain high for the next 2 to 3 years.

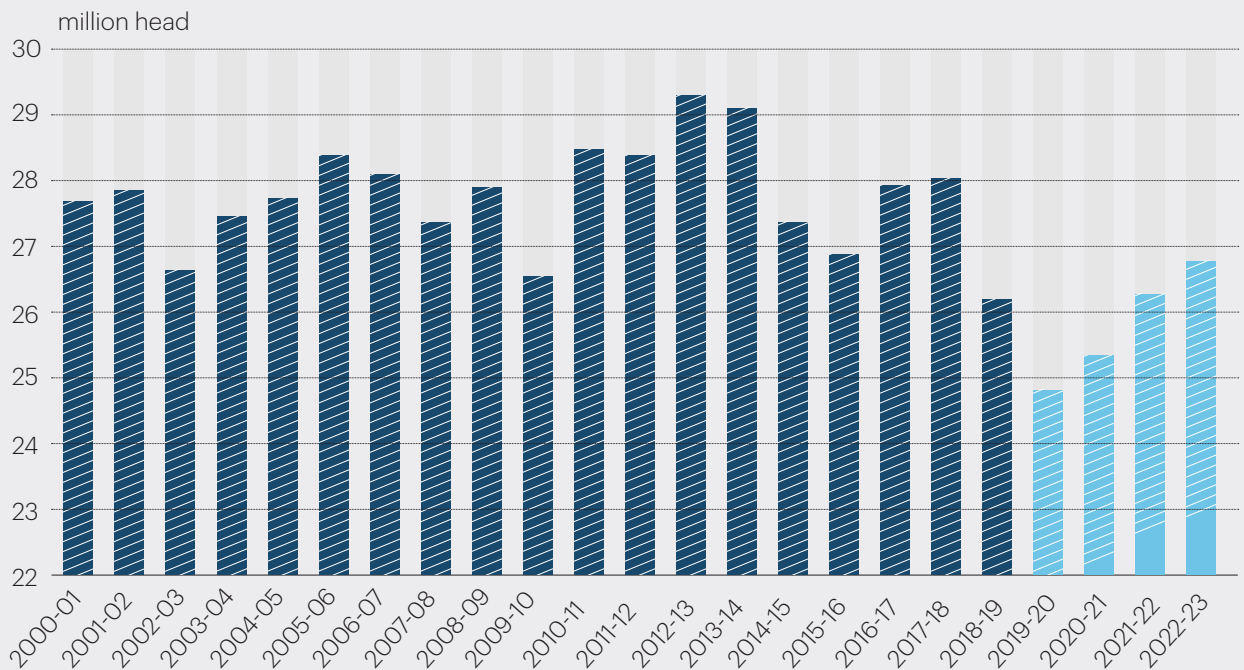
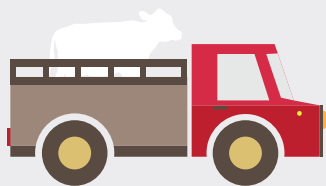


Figure 3: Australian national cattle herd population over the past 20 years and future projections

Indonesian feedlots imported more cattle but were challenged by tight market conditions

Indonesian feedlots imported more live cattle in 2019 than in any of the past five years because:



The price of feeder cattle was low – AU\$2.80 – \$3.00/ kg liveweight ex Darwin

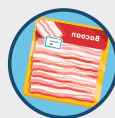


The Australian dollar depreciated against the Rupiah by over 5% during 2019

The number of active GAPUSPINDO (Indonesian Feedlot association) members dropped from 42 to 26 because:



Indonesian feedlots were less profitable than in other years



Frozen Indian buffalo meat is now sold in wet markets at Rp80,000 putting downward pressure on local beef prices



The market price of beef has remained stable over the last 5 years at IDR100-120,000, while the cost of production has increased by over 3% (Figure 4)



The requirement for breeder importation reduces the profitability of feedlot operations.

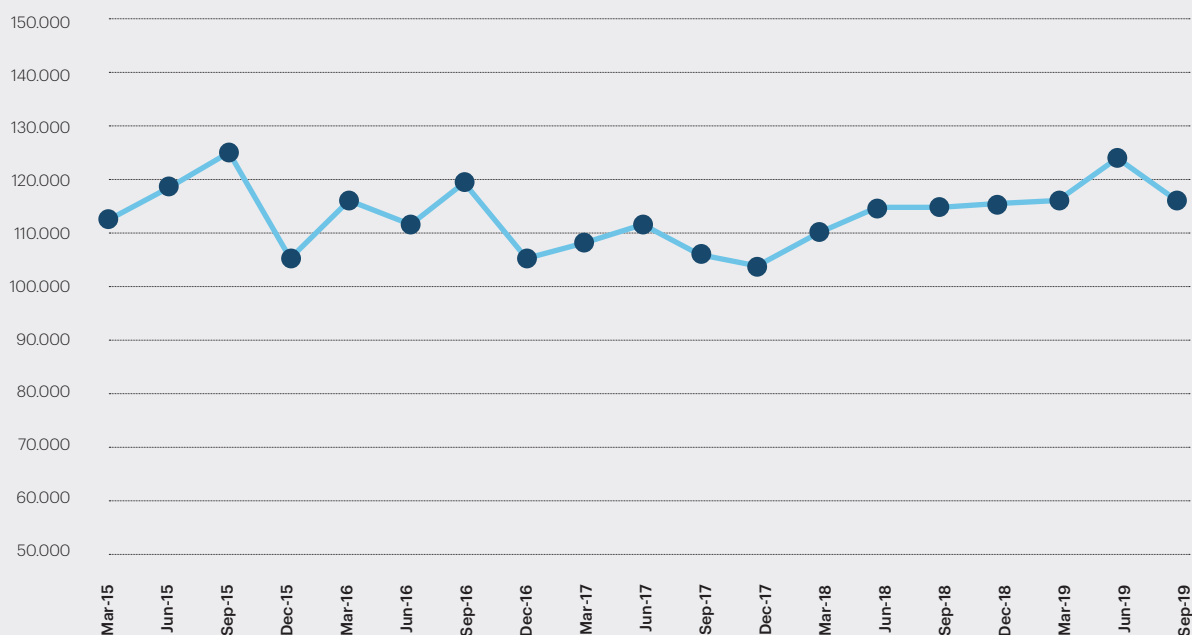


Figure 4: Wet Market price of fresh beef Rp per Kg – Source MLA statistics

Impacts of Indian Buffalo Meat (IBM) and Brazilian beef importation



Around 100,000 tonnes of IBM will be imported in 2019-20 - approximately 40-50% of current beef imports. This low-cost, low-quality red meat has broadened the consumer base, making red meat accessible to lower income Indonesians (Figure 5).

Indonesian Frozen Boxed Beef Imports

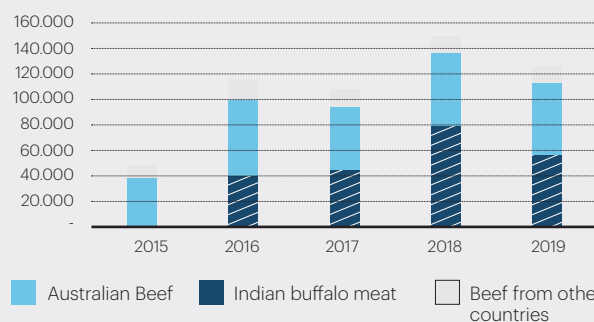


Figure 5: Importation of beef (frozen) from all sources between 2015-2019.



Brazil has also gained access to the Indonesian market and was permitted to ship 50,000 tonnes as of mid-2019.¹



Modelling² suggests that IBM and beef from Brazil will have modest impacts on Australian beef imports and cattle shipments due to growth in Indonesia's middle class over the next decade.

¹ Only 3,500 tonnes had been imported by December 2019.

² Commissioned by the MLA through the Centre for International Economics

Processing is significantly cheaper in Indonesia



The cost of processing and packaging feedlot-finished Australian cattle in ESCAS-approved abattoirs in Indonesia was estimated at approximately AUD 98 per head, compared with AUD 282 per head in Australia.



Labour costs for processing in Indonesia were approximately AUD 55 per head compared to AUD 250 in Australia.

Changes to Indonesia's breeder importation policy



The Indonesian Government's previous 1:5 breeder import ratio policy has impacted many companies. No feedlot companies have been able to meet this quota over the last 2 years¹ and some have had their import licenses suspended for 12 months. Some industry actors have also indicated that increasing land prices close to urban centres were also resulting in the closing of feedlots for other more profitable land uses. In 2019, the Indonesian Government revised the 1:5 breeder import policy to require Indonesian feedlot operators to import 5 per cent of each consignment of feeder cattle for breeding purposes.

¹ Only about 2.7% of cattle imported into Indonesia in 2017-18 have been breeders.

Benefits from IA-CEPA

The Indonesia-Australia Comprehensive Economic Partnership Agreement (IA-CEPA) was signed in March 2019 and is due to be ratified for implementation in mid-2020. IA-CEPA benefits include:



A 0% tariff quota for 575,000 head of live male cattle – which will grow by 4pc per annum over five years to 700,000 head



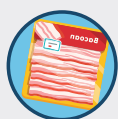
Live cattle import permits issued automatically on an annual basis and without seasonal restrictions.



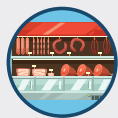
A review after five years to consider future increases in the quota above 700,000 head



No quota or import permit restrictions for female live cattle imported into Indonesia



Boxed beef lines not already benefiting from 0% tariffs will benefit from either a 0% or 2.5% tariff on entry into force (down from 5%)
Elimination of remaining tariffs on boxed beef over five years



The 5% tariff on frozen offal eliminated on entry into force of the agreement.

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