

**AGRIBUSINESS ASSOCIATION OF AUSTRALIA AND
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**Agricultural Marketing:
Why Restrict Choice?**

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AGRICULTURAL MARKETING : WHY RESTRICT CHOICE?

As an inactive environmentalist I am pleased to be able to talk to a group including many endangered species.

The endangered species are, of course, the agricultural socialists amongst you who still believe that government-imposed monopolies and cooperative business structures are good for you and your customers.

The rest of the world has learned that collectivism generally leads to stultification and mediocrity. Free markets are not only good for customers but also producers. Actually, they can be a lot of fun and are certainly better than being the only game in the country, which some of the producer boards want to be.

I will be arguing that New Zealand farmers in their own interests should disown the monopoly powers currently granted producer boards. In doing so I acknowledge that all producer boards are not the same. The Meat and Wool Boards both have regulatory functions, while the Meat Board also has major investments in the industry. The problem here is being both player and referee at the same time. The boards for kiwifruit, apples and pears and dairy products all have absolute control over exports, although the Dairy Board may grant licences to other exporters.

But before discussing agriculture I want to comment on New Zealand's experience in the past 20 years as we dismantled regulatory controls over two major industries, transport and manufacturing, and joined the real world. The regulations were largely put in place in the 1920s and 30s, the same period in which we embarked on extensive controls over primary product marketing. The gains we have made and lessons learned from the changes in other sectors are directly relevant to agricultural marketing.

Ten years ago Railways employed more than 21,000 people. They were protected against most road competition and most road transport operators were also protected against new entrants. Railways and truckies had a symbiotic relationship but neither made much money. In fact Railways accumulated substantial losses and debt. Costs were very high and service was often lousy but we all fought tooth and nail against deregulation. Railways argued that they were highly efficient and that if protection was lost its few captive customers would pay much more. Protection was needed in the interests of an "orderly market". For its part the road transport industry opposed delicensing in order to prevent "weak selling" and "cut-throat competition" by "fly-by-night" operators. Both the Road Transport Association and Railways claimed that everyone would be the loser from deregulation. Despite their best endeavours at a political level, deregulation happened. What has been the result?

The answer, as we all know, is that there has been a revolution in transport with major benefits going to users. Since 1983 rail freight rates have dropped by nearly 50 percent in real terms. Railways now has around 7,300 staff and is heading towards 6,500. Similar changes have occurred in road transport. While there were several bad years, good operators are now making more money than ever and Railways is making an operating profit for the first time.

The manufacturing sector has also undergone a revolution in the past decade. In 1981 our manufacturers tried to produce just about everything this side of jumbo jets. I am told that even Sir Robert Muldoon was startled to discover that jumbo jets were subject to import licensing. In most cases manufacturers produced mediocre goods at excessive prices. However, they too argued that they were efficient, and that the "special" characteristics of the New Zealand market made continued protection through import licensing the only way manufacturing could survive. The manufacturers' lobby certainly had a record for consistency. Way back in 1965 they argued that the NAFTA deal with Australia posed a death threat to manufacturing.

Emotive arguments of this sort paralysed rational decision making. The import licensing system was a sacred cow that no government could attack. Although some politicians understood that the protection arguments were humbug, a bit of heavy breathing from Manfed soon brought them into line.

Amazingly, despite decades of such indoctrination, we finally got governments in the 1980s which were prepared to act. Federated Farmers, of course, was the strongest advocate of change. We now have free trade with Australia, virtually no import licensing and significantly lower tariffs.

The net result of these changes has been dramatic. We have lost many of our hopelessly uncompetitive manufacturers who should never have been there in the first place. But most companies have survived. Manufactured exports are growing, particularly to Australia where our companies are showing they can often out-perform the local competition. I believe manufacturing will be one of the growth sectors in the 1990s. Not even Manfed would now want to turn the clock back.

The lesson we should take from the experience with transport and manufacturing is that arguments for restricting competition are rarely valid and usually involve the protection of special interests at the expense of others. Furthermore, those that argue for protection usually find that after it is removed they raise their game and survive.

All the commercial experience of the last few hundred years tells us that open competition works best in the long run. Monopolies by their very nature tend to become fat, dumb and lazy. Monopolies created by legislation continuously lobby to protect their positions. They spend far too much time in the political marketplace (speaking at seminars such as this) and too little on working out how to improve their efficiency and do a better job in the real marketplace.

There are some who will argue that agriculture is somehow different and requires a special approach - that it is possible, through controls, for producers of agricultural products to obtain higher net returns than would otherwise be the case. It is argued that restrictions on access to overseas markets and the necessity to have large scale operations make monopoly producer boards the best way of selling agricultural products.

These arguments merit close examination. There are some special factors about agricultural markets, but not a lot. The similarities with other trade are much greater than the differences. Situations like the United Kingdom quota for butter are special cases. Sure, this might justify a mechanism which ensures that the quota rents come back to New Zealand and are fairly distributed to producers. But there are ways of doing this which do not require a giant monopoly with absolute powers over the

export of all dairy products, including differentiated and branded items. The world market for cars is also riddled with political interference and import controls. Japanese exporters face quotas in many European countries and import restraints in the United States. When was the last time you heard a Japanese arguing for a 'single seller' organisation for Japanese cars?

The joke is that in nearly all cases New Zealand agricultural exporters are operating in highly competitive markets. They are not a De Beers with exclusive control of the world diamond market. They are subject to competition from all over the world both from other suppliers and from substitute food products.

The second argument for marketing boards is that the outside world is tough and size is needed to foot it with other international sellers. This may well be true, particularly for commodity lines, in which case the industry will naturally tend to large units. But such industry realities do not give rise to a case for state-created marketing monopolies controlling the full product range for all markets. The forestry industry also needs large operators and we have firms that compete very successfully internationally. But would anyone care to argue the case for a state monopoly to sell logs or pulp and paper?

It is competition and the opportunity to test new ideas that drives commercial performance. Firms that innovate and do a better job for consumers gain market share and improve their net worth. If we have a high market share in our business we create our own genuine competition to ensure we stay there. For example, Freightways has about 80 percent of the New Zealand courier market. We couldn't do that with one company. It can only be achieved by having several competing ones which offer different solutions for the customer. Thus we have New Zealand Couriers, Courier Systems, Castle Parcels, Sub 60, Roadrunner Cycle Couriers and so forth, all competing in the same market. Their competition strengthens demand for couriers and ensures that by having multiple teams doing things differently we are constantly filling niches and finding the best solution. That is the sort of dynamism the New Zealand dairy industry needs.

The wealth-creating power of the competitive system depends on choice. If, for instance, 80 percent of apple growers want to export through one giant apple cooperative they should be free to do so, just as the other 20 percent should be free to choose other options and compete with them. Have you ever heard a Japanese saying they are disadvantaged by Toyota competing with Nissan, or Sony with National?

In this area the most absurd situation of all is the monopoly position of the Apple and Pear Marketing Board in the domestic market. I understand that government reviews have regularly concluded that it has no justification but agricultural politics and the marginal seat syndrome have so far preserved it.

I do not argue that the producer boards are incompetently managed. We simply don't know. In the absence of detailed information it is not possible to come to a definitive view about any of them, particularly the boards for dairy products, kiwifruit and apples and pears, because objective information is non-existent. Until their economies fell over, the authorities in Russia and Eastern Europe also told everyone they were doing a great job and a lot of people in the West believed them.

In normal commercial operations ultimate control is exercised by shareholders who can vote directors off the board or even sell the company if it does not perform to their satisfaction. Investors are able to make such decisions because they can compare the performance of their company with others. Analysts and competing management teams are constantly on the lookout for poor performance and ways of doing a better job.

This situation does not apply to producer boards. They cannot be sold and an individual producer cannot sell his or her shares to another producer. It is virtually impossible to assess the performance of a marketing board. There are no comparisons with competing organisations, as they have been outlawed. The producers have to take the claims of efficiency on good faith.

Producer boards are commercial organisations that operate politically. They survive by convincing producers that they are doing a great job, and that without them farmers and growers would earn much less.

The boards have well-honed public relations teams which perform very effectively. Control over information is vital to this process. Thus it is no coincidence that the Dairy and Apple and Pear Marketing Boards enjoy stronger support from their producers than the Meat and Wool Boards where there are alternative sources of information.

One of the very interesting features of the main producer boards is their location. With the exception of kiwifruit, all are within one kilometre of Parliament. The Dairy and Apple and Pear Marketing Boards are the closest. Treasury is even closer than the Dairy Board and for a while, under the previous Minister of Agriculture, it looked as though the Board was in trouble. But the new home for politicians has been moved closer to the Board. They are now so close that you could throw a cow cover over them. My guess is that Treasury is now on the back foot.

You may be wondering what this choice of location has to do with running a commercial business. So do I. I am not a Wellingtonian, but to the best of my knowledge there are not many cows or orchards on Lambton Quay or The Terrace. Something tells me the choice has more to do with politics than business.

The extraordinary socialist nature of the producer boards is highlighted by the ownership of the Dairy Board. The Dairy Board has a net worth of \$1.5 billion. This is effectively owned by no one. It represents \$107,000 of capital for every dairy farmer. There is a fiction among dairy farmers that this asset is capitalised into their farm values. This is not the case. I have a sheep farm next to a dairy farm. I could convert to dairy farming and theoretically get my share of this equity. If you gave me shares worth \$107,000 I would jump at it but I can assure you I would not increase the value of my farm by \$107,000 by switching.

Dairy farmers own the Dairy Board in the same way workers in Russia own their own factories - they don't. To be real, ownership requires transferability of shares. Don't our socialist farmers know the meaning of ownership? I wouldn't think most dairy farmers could afford to have \$107,000 tied up in another business, particularly if they could never get it back.

There is plenty of evidence that people only make above average returns when they invest where they have superior knowledge of manufacturing or marketing. Farmers would do much better to put their money into farms and let other money be attracted into specialised activities.

Why do farmers want to own manufacturing and distribution businesses? Manufacturers rarely own retailers. Tree farmers don't need to own paper mills. It is a total myth that unless farmers own processing and marketing operations they will get exploited. As in the rest of the economy their protection is that if there are competing manufacturers and marketers buying their produce, farmers will get the best price available. By only selling to an ownerless monopoly they are far more likely to get a bad deal.

At the Prime Minister's recent enterprise conference there was a strong view among business sector representatives that the powers of all producer boards should be reviewed and trimmed to the bare essentials. I subscribe to that view. There needs to be a clear separation of commercial operations from the exercise of any control powers that are necessary for restricted markets. It is vital that the private sector companies that are involved with agricultural products operate with freedom and with confidence that the rules are not likely to be changed by a combined player and referee producer board. This is not the case today.

There is no need to abolish producer boards. I do not share the Porter view that fragmentation is necessarily best. A much better approach is to remove barriers to competition wherever possible and let others have a go. Before this is done the existing institutions would need to be corporatised and their shares made tradeable.

Deregulation of agricultural marketing would revitalise the agricultural sector. There would be new investment, new ideas and stronger links with commercial interests overseas. Companies that want to experiment with new apple or dairy products, for example, would know they could do so without the fear of being overruled by a statutory player and referee. The continued existence of these powers is a major deterrent to investment in agricultural processing. Our statutory monopolies are still biasing the product range towards basic commodity lines. Competitors would have both the freedom and the incentive to develop brands and specialised products.

Once the existing operators got over the initial shock they would find life much more interesting and challenging. If they are as good as they tell us they are, then competition will make them stay that way and new entrants may not even get off the ground. Instead of constantly looking over their shoulders at the critics and worrying about the direction of the government, they could concentrate full time on their commercial business.

Anyone who believes that the Wool Board has done a decent job in recent times is not in touch with reality. I think the boards are now the single most important factor holding the agricultural sector back. In my view, a careful approach to deregulation would give us the same kind of gains that we have seen in manufacturing and transport. New Zealand agriculture should have a great future. So, I say unto the agricultural socialists, rise up and overturn your monopolies - you have nothing to lose but your chains. Ten years down the track not even the most conservative farmer would want to turn the clock back.

