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JOINT STANDING COMMITTEE ON FOREIGN AFFAIRS,  
DEFENCE AND TRADE TRADE SUBCOMMITTEE

**Reference: Australia's trade with Mexico and the region**

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**JOINT STANDING COMMITTEE ON  
FOREIGN AFFAIRS, DEFENCE AND TRADE**

**Trade Subcommittee**

**Wednesday, 21 March 2007**

**Members:** Senator Ferguson (*Chair*), Mr Edwards (*Deputy Chair*), Senators Bartlett, Crossin, Eggleston, Hutchins, Johnston, Kirk, Moore, Payne, Scullion, Stott Despoja and Webber and Mr Baird, Mr Barresi, Mr Danby, Mrs Draper, Mrs Gash, Mr Gibbons, Mr Haase, Mr Hatton, Mr Jull, Mrs Moylan, Mr Prosser, Mr Bruce Scott, Mr Sercombe, Mr Snowden, Dr Southcott, Mr Cameron Thompson, Ms Vamvakinou, Mr Wakelin and Mr Wilkie

**Trade Subcommittee members:** Mr Baird (*Chair*), Mr Snowden (*Deputy Chair*), Senators Bartlett, Eggleston, Ferguson (*ex officio*), Johnston, Payne and Scullion and Mr Barresi, Mrs Draper, Mr Edwards (*ex officio*), Mr Haase, Mr Hatton, Mr Jull, Mrs Moylan, Mr Prosser, Mr Bruce Scott, Mr Sercombe, Dr Southcott, Mr Cameron Thompson, Ms Vamvakinou, Mr Wakelin and Mr Wilkie

**Members in attendance:** Senator Ferguson and Mrs Draper, Mr Jull, Mrs Moylan and Mr Prosser

**Terms of reference for the inquiry:**

To inquire into and report on:

Expanding Australia's trade and investment relations with Mexico and the region with particular reference to:

- the nature of Australia's existing trade and investment relations;
- likely future trends in these relations; and
- the role of the government in identifying and assisting Australian companies to maximise opportunities in Mexico and the region.

**WITNESSES**

**KERR, Mr Paul, President, Australian Dairy Products Federation..... 1**  
**PETTIT, Mr Robert John, Manager, Americas and Caribbean Trade and Strategy Group, Dairy  
Australia..... 1**



**Subcommittee met at 11.08 am****KERR, Mr Paul, President, Australian Dairy Products Federation****PETTIT, Mr Robert John, Manager, Americas and Caribbean Trade and Strategy Group, Dairy Australia**

**ACTING CHAIR (Senator Ferguson)**—Welcome to this public hearing of the Trade Subcommittee of the Joint Standing Committee on Foreign Affairs, Defence and Trade's inquiry into Australia's relationship with Mexico, and trade and investment opportunities. Thank you very much for your submission. You will be aware that this public hearing is treated in exactly the same manner as a meeting of the parliament. I invite you to make an opening statement and then we will proceed to questions.

**Mr Kerr**—Dairy is the largest processed food industry in Australia, creating skilled and semi-skilled jobs in farm and factory service industries, manufacturing, distribution, at point of sale, retail and food services. Dairy is also Australia's largest processed food export industry, representing about 30 per cent of Australia's processed food exports. Dairy in 2005-06 was Australia's third most valuable agricultural industry at farm gate, with a value of approximately \$3.34 billion. The industry is also the largest value-adding food industry, with an ex-factory value of \$9.5 billion. Dairying creates jobs; there are just under 9,000 dairy farmers in Australia and 35,000 to 40,000 downstream workers with further indirect employment of about 150,000. The vast majority of these jobs are created in rural and regional communities.

The prosperity and long-term viability of the Australian dairy industry relies on exporting a diverse range of high-quality dairy products and ingredients globally. In 2005-06 approximately half of the national production was exported to over 130 nations, to the value of approximately \$2.7 billion. Australia is the third largest exporter of dairy products in the world, after New Zealand and the European Union, with about a 12 per cent share of the export market on a milk equivalent basis. The domestic dairy market in Australia is very mature and will provide only limited growth through population and through product innovation. Dairy has strong economic linkages throughout the economy ranging from feed and on-farm service inputs to value-added processing of dairy products and ingredients in regional areas to generating turnover of employment in retail food service and institutional sectors. Mexico and the region are long-term dairy export destinations for the Australian dairy industry. The region is defined as countries of Central America: Guatemala, Belize, Honduras, Costa Rica, Nicaragua, El Salvador and Panama.

I should, just to finish my opening remarks, make a couple of comments about the drought. The drought has seriously impacted the dairy industry over the last few years. Production of milk has fallen from 11 billion litres in 2001-02 to probably around about 9.3 billion litres by the end of 2006-07. The dairy industry is expected to grow again and to grow significantly when we have a reasonable season—and let's hope that is very soon. If the drought is over we will expect to see dairy grow again. It has significant potential and the majority of that growth will be into export markets.

**ACTING CHAIR**—Mr Pettit, do you wish to comment?

**Mr Pettit**—No, it has been covered.

**ACTING CHAIR**—Naturally our particular interest in this inquiry is in our trade and investment relationship with Mexico and what opportunities there might be. There has been a lot of activity and movement in relation to trade agreements, particularly with NAFTA, with quotas and tariffs being phased out. What impact is that reduction of tariffs likely to have on our possible trade with Mexico?

**Mr Kerr**—Unless we are able to trade on the same terms as NAFTA, as North America or our competitors—I understand New Zealand is in the process of potentially having a free trade agreement with Mexico—that will make it more difficult for us to compete in those markets. I understand that all US dairy products after 1 January 2008 will be quota and duty free. So, from 1 January 2008, which is not that far away, they will potentially have a significant advantage.

**Mr Pettit**—Particularly when you look at tariff rates. For instance, on cheese, the tariff rates are between 20 per cent and 125 per cent, depending on variety. The US industry has already got zero tariff rates on cheese. Milk powders will go to zero on 1 January. They are the last legacy of the NAFTA agreement. Given our freight disadvantage compared to land transport from the United States and given the huge capacity of the United States industry to grow and be a bigger exporter, we are facing a major competitive hurdle there compared with them. Also, Uruguay and Chile have trade agreements with Mexico. They do not cover all dairy products but they do cover cheese, for instance. New Zealand and the European Union are also joining a queue to have trade agreements. To put it in a broader perspective, Mexico is the world's largest importer of dairy products for a developing country—the fourth largest in the world. There is general consensus that Mexico will remain a major importer of dairy products.

**ACTING CHAIR**—What percentage of the market do we have now?

**Mr Pettit**—The import market over the last few years ranged between about one and two per cent. The total market would be under one per cent.

**Mr JULL**—How hard do you play the relationship with the industry over there? You have said that you have been there a long time, that it is a well established market. Are you continually promoting? Are you convinced that you are going to have these big problems, or is there a sense of good will there? Do you work in with Austrade? How effective is Austrade in helping you maintain those markets?

**Mr Kerr**—The company I work for, Murray Goulburn, has been dealing in Mexico for a long time. We are predominantly an ingredient supplier. We see Mexico as an opportunity, as being a gateway to North America and Central and Latin America. We are seeing North American companies, or US companies, moving to Mexico for processing. Already Kraft have a fairly significant presence in that market, exporting back to the US. Hershey's are setting up down there. So we see ourselves predominantly as an ingredient supplier. Our sales last year to Mexico were about \$40 million, so in the overall scheme of things it is a pretty small market. We have developed that over a long time. We use Austrade from time to time, not predominantly as to opening up markets, but to deal with local issues when they arise because as an importer issues arise with clearing product from time to time. Austrade is very useful in that area. But that is about the extent that we use them.

**Mr JULL**—Can you fill me in. You gave us that list of Central American countries that you use. Places like Nicaragua and Belize—is there much Australian product going into them or is it predominantly Mexico?

**Mr Kerr**—That is a very good question. Murray Goulburn again—I am going to focus on my company—has formed a joint venture and owns retail brands in Central America in predominantly or primarily Guatemala and El Salvador. They are net importing countries for dairy products. We sell ingredients into those markets, and then we repack them under our own brand. The brand is called Aussie Pride. It is totally, 100 per cent Australian dairy products. Our sales into that region last year were about \$33 million and it is growing.

The advantage for Australia and companies like Murray Goulburn is that we are able to be a niche player in a large market. We do not have sufficient product to go into the market and flood the market. We have to compete against a large multinational company such as Nestle, who have a presence in just about every single market throughout Central and Latin America. If you get too big over there, then it is pretty hard to compete. But there is a fairly significant opportunity for us to add value to our ingredients. We formed this joint venture about three or four years ago. We would like to do the same in Mexico—take our ingredients and look for small opportunities to repack them with Australian branding and sell them in the market.

**Mr JULL**—Just for the record, Murray Goulburn is not the only Australian company there?

**Mr Kerr**—It is, predominantly. It is about the only Australian company there. There are other companies in a smaller way in certain parts of Latin America. Our major competitor is Fonterra, the New Zealand dairy company. It has a presence in all those markets.

**ACTING CHAIR**—Fonterra has a big presence here as well, doesn't it?

**Mr Pettit**—Twenty per cent of its milk supply is processed by Fonterra in Australia.

**Mr Kerr**—In Murray Goulburn's case we represent about 36 per cent of the industry. We are by far the largest player here. We are a cooperative. We are owned by our 2,800 farmers. So we are one of the last Australian owned companies in this industry.

**ACTING CHAIR**—Is Fonterra increasing the size of its operations in Australia still?

**Mr Kerr**—It has a very significant operation here in Australia and has expanded rapidly over the last few years, but it is probably difficult to say if it is increasing—

**ACTING CHAIR**—It is mainly Victoria, isn't it?

**Mr Kerr**—It is mainly Victoria. It sells the Bega brand, under licence, and it is heavily promoting its Mainland brand from New Zealand.

**ACTING CHAIR**—Do we have any problems in relation to Mexico and/or other countries in the region in recognition of our quarantine and safety standards for the products that we are selling over there?

**Mr Pettit**—Mainly in Central America.

**ACTING CHAIR**—Nicaragua?

**Mr Pettit**—Yes, I will give you an example. Panamanian inspectors recently came to Australia. We would like AQIS's health and safety standards recognised without having these physical inspections. What happens with physical inspections is that we have at least two inspectors who will come to Australia from a veterinary agency in a particular country such as Panama. We have to pay per diem. We have to do a lot of organisation. They will only register for export approval establishments that they actually visit and only identified products. In other words, if a processor changes its product mix between factories and does not have a particular factory recognised for export to Panama then that basically prevents trade. It is a time-consuming and expensive process involving AQIS as well as the companies who have to fund it. We would certainly like, given AQIS's very high standards, to move to a mutual recognition process.

**ACTING CHAIR**—Bearing all the things that you have talked about in mind, the purpose of this inquiry is to see what we can do to try and improve the trade and investment relationship that we have between Australia and Mexico. What would you see as maybe the most significant contribution the Australian government could make towards boosting our trade and investment opportunities?

**Mr Kerr**—From a dairy industry point of view, the elimination of the VAT taxes on dairy products going into Mexico would probably mean that we would export more dairy products to that market.

**ACTING CHAIR**—Are the taxes applied by the Mexican government as the product enters?

**Mr Pettit**—They are applied up-front and then six months later the money can be refunded. For a small company that can be a considerable cash-flow problem. Again we talked about an importer for Murray Goulburn. It is only a small company; a company like Nestle has massive revenue streams. Maybe, looking at a bigger picture, what would be absolutely critical is progressing the experts group. The Australian government has agreed to an experts group process and we would very much like that to develop into negotiations on a free trade agreement provided those negotiations reach a comprehensive agreement with agriculture at the heart of the agreement and no exclusions applied.

**ACTING CHAIR**—I have to attend that division. Mr Jull will take over.

**ACTING CHAIR (Mr Jull)**—Do you have many dealings with the Mexican government yourselves?

**Mr Pettit**—We have had dealings with Mexican customs. They recently reclassified milk protein concentrate imports from one tariff line to another which doubled the duty. We actually agreed to that process because it was consistent with worldwide customs interpretation. Also we deal with their agriculture department, SAGARPA. We want to build close relationships with them. We visited in November 2005 and we are going to visit them again in April this year. They

have a lot of issues in developing their dairy industry, particularly south of Mexico City where it is more a subsistence type of industry, and we would like to provide technical assistance provided funding is available to do so.

**ACTING CHAIR**—However, basically you do not have too many difficulties in dealing with the Mexican government?

**Mr Pettit**—No.

**Mrs DRAPER**—I noted in your opening statement that you referred to the drought which is affecting all of our rural and regional areas in quite a substantial way. With respect to export, does that affect our domestic market? In terms of continuing supply of your ingredients through to Mexico, does that mean we cut back in Australia? How do you manage it?

**Mr Kerr**—The Australian dairy industry this year will produce around 9.3 billion litres of milk. The domestic market will consume about five billion litres. So, providing the domestic market remains competitive with the world market—and it is today—then there will still be ample products for supply to the domestic market. As I said in our opening statement, we export to well over 100 countries around the world. What determines whether we export to Mexico or to another country will depend on our ability to get the best returns to predominantly our farmer shareholders.

**ACTING CHAIR**—Have you got a sense of optimism in terms of the future market for Mexico, in particular?

**Mr Kerr**—As Robert said, we are about one per cent of the market. Under the right terms of trade we could, potentially, be more. Our key objective, as a company and as an industry, is to get more value out of our ingredients. There is a sense of optimism about Mexico. We have a free trade agreement with the United States, which has given limited access for the dairy industry into the US. Those markets are about adding value to our ingredients, and we see a potential to reemploy into Mexico the strategy which we are employing in a very small way in Central America. It will probably remain a small market for us but it is a market that has some potential to grow. Mexicans are large consumers of dairy products.

**Mr Pettit**—And there is a growing integration of the Mexican and US economies creating that huge economic space which is over 400 million people. There are opportunities to value-add in Mexico, particularly if you transform the product, and export to the United States.

**ACTING CHAIR**—You mentioned companies like Nestle and Hershey's moving in there. Do you have any capacity to sell to them?

**Mr Kerr**—We do sell to those companies. Hershey's are predominantly a North American based company. We sell limited amounts of product under the free trade agreement to Hershey's but we sell to Nestle around the world, including their Latin American companies.

**ACTING CHAIR**—Just for the record, Hershey's is the company that makes the world-famous Hershey's bar, is it?

**Mr Pettit**—Yes.

**Mrs MOYLAN**—I have one question, and it relates to a comment you have made on page 11 of your submission. We just made an inspection—we are doing an inquiry on AQIS—but this is a little confusing to me so you might get us through the technicalities. It says:

The Government also needs to be proactive in ensuring that imports ex-Australia are not, at the very least, disadvantaged competitively by technical barriers, for example physical inspection of factories. In this regard recognition of AQIS food safety regulations by relevant Government authorities in Central American countries ...

Could you just unpick that a little bit because I find that confusing. I do not entirely understand what the barriers are and what the—

**Mr Pettit**—In a large number of export markets AQIS health and safety regulations regarding dairy product exports are recognised by the relevant authority in the importing country. That is not the case in—

**Mrs MOYLAN**—In Mexico?

**Mr Pettit**—No, not Mexico; I am talking more about Central American nations such as Panama, where the Panamanian authorities actually demand that they come to Australia and do physical factory inspections.

**Mrs MOYLAN**—And the industry pays for that?

**Mr Pettit**—The industry pays for it. They have a US dollar per diem which can be \$US250 or \$US300 a day. Usually two inspectors come. Their airfares are covered and it therefore adds up to a considerable cost for the industry and also for AQIS in terms of hosting them, the payment schedule and the time taken out from other work priorities.

**Mrs MOYLAN**—What has been done to try and rectify that and to work with those authorities, because we have some of the toughest food regulations, as I understand it, in the world?

**Mr Pettit**—We have tried, in a number of instances, in South America and Latin America, to sign mutual recognition arrangements or have MOUs but generally there is a reluctance on the other side to move to them. I think it is a matter where the more we can build our trade in these markets, and the greater our presence, the greater authority or weight we will have to suggest we move to mutual recognition of standards.

**ACTING CHAIR**—I thank you both very much for appearing before the subcommittee today. That was most helpful. We will be forwarding you a copy of the transcript to which you can make any corrections, provided the sense of the answer is not changed.

**Subcommittee adjourned at 11.29 am**