

Deer Industry New Zealand
FORMAL GENERAL MEETING
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Chairman's Report: John Scurr
(Chairman Deer Industry New Zealand)

Introduction

Ladies and Gentlemen: I closed my report to you this time last year by saying that we will have a different shape to our industry as we deal with changing land use, lowering volumes of venison exported, and how we market our products to best effect.

Well, the machinations in New Zealand agriculture over the past year have shown that I understated the situation. We are seeing a fundamental shift in New Zealand agriculture due to changes in land use, intense pressure on supplementary feed prices, and low returns from the sheep industries as we work our way through the significant proposals like "The Mega-merger Concept", possible consolidation of red meat industry good organisations, and government-led initiatives like the Emissions Trading Scheme to deal with the highly political climate change debate. Are we understanding what all these issues, along with many more mean to the Deer industry and your business. But, to quote, JFK's line back in the 1960's that farmers are the only business people he knows who buy retail, sell wholesale, pay the freight both ways and expect to make a profit. I raise this, which is old hat, to pose a couple of question: are we producers, really accepting and acting on the challenges of change that we face? Are we really modifying our businesses to become more efficient and therefore more profitable or are we confused as to the magnitude of a changing business environment and finding it all too difficult?

For example, it is crucial that the velvet industry changes how it presents its product to the market. Your board is determined not to replicate the failings of the wool industry which has been plagued by the functions of the auction system and road buyers. The model is outdated. Modern business models are promoted to connect producers directly through the value chain and therefore have a sustainable, tradable business and I have no doubt, that's where we have to be.

Today, Mark and his team will present to you their annual high-level summary of executive activity to achieve industry goals and intent, and I will begin with an update on strategy.

Venison Strategy

We are now four years down the track on the industry's five year strategic intent with many elements as relevant today as when the strategy was first launched. However, we must recognise that the industry's structure has changed significantly over the past four years. The long anticipated bow-wave of venison arrived and passed and now the industry is in a position of having to carefully manage a lowering volume of venison available to it. In considering these changing circumstances, the DINZ Board is using a competitive positioning strategy called "Focus with differentiation". A focus with differentiation strategy is tailored to specialty products – and in particular high-priced specialty products. It advocates treating New Zealand venison as a niche product, marketed in a tight, well organised value chain with good levels of co-ordination and cohesiveness along that chain. It will be particularly effective where there is a slight excess of demand over available supply. These are all characteristics of the New Zealand venison industry. In terms of a one-liner to describe the strategic positioning, the DINZ Board has been using 'New Zealand Venison for every special occasion'. This highlights that New Zealand venison has a unique place in the red meat consumer market as a specialty, high quality item.

Deer Industry New Zealand has two key levers to pull in the implementation of industry strategy. Firstly, generic promotion which is promotional activity funded 100% by DINZ for the implementation of the industry strategy. This is the 'Impress Your Guests campaign' and this positioning works very well to give life to Focus with differentiation. The second key lever is joint promotional funding, where DINZ works alongside marketers to assist funding of promotional activity which has an 'industry good' element to it. The DINZ Board has adjusted the Joint Promotional programme to being more about positioning to ensure that it is catering for New Zealand venison's changed circumstances and its need to be positioned as a niche, specialty item. You see, given the high price of venison in the commodity channel and the significant cost of developing new business, there is a real risk that venison will shrink back to the commodity environment. If that occurs, the work over the past five years could be squandered. We must avoid that happening.

In terms of the relevant measurable aspects of the strategy, I report great industry progress.

Firstly, chilled volumes which we think of as a proxy for retail sales. As you can see here, they have increased significantly as industry has focused business development and promotion on retail. Importantly, despite big increases in production, the percentage of chilled exports has increased, for example chilled exports were 12% of total volume in 2004. Today they are 23%.

Secondly, out of season consumption of venison. We are using chilled volumes consumed from January to July given that venison exported then would need to be consumed outside the game season. As you can see here, the target of 5% of total venison exports has been exceeded for the first time this year.

The third key area is in terms of New Zealand country of origin branding of venison to the consumer. Companies and their customers continue to accelerate work in this area. In the past year, five major companies have developed new products which explicitly include country of origin branding. These companies handle literally thousands of tonnes of venison.

Another interesting area is the growth in some new European markets such as Scandinavia and Finland where volume has grown by 535 tonnes, and Switzerland which has grown by 375 tonnes and to a smaller extent, Eastern Europe by 90 tonnes.

Production Scenarios

There is more capital stock being slaughtered currently than we would have preferred which is being spurred along with the higher schedule price for this time of the year and the effects of drought. The trend here highlights the very significant challenge which changing land use means to our industry. What happens with the fortunes of dairying, or any other pastoral sector for that matter, affects deer farming, primarily around land use but also general competition for supplementary feed. We have rolled out a financial analysis using independent analysis to give financial institutions, and you the producer, as good a handle as possible on relative returns on investment of different land use options.

Reserves

The net effect with best predictions of production between 400 and 500 thousand animals for the 08/09 season will also mean a shift in position with Deer Industry New Zealand's reserves. As previously reported, the Board took a conscious decision to build reserves during the high production period between 2004 and 2006 so that DINZ investments could be maintained without large increases in the levy as venison production dropped. It is proper that the benefit of these funds are returned to those people who have stuck with the business and the draw down on the reserves is budgeted to arrive at our original level of 400k by the year 2012. Cost savings will continue to be investigated; however, some levy increase before that time under the current working environment may be required. That is not yet known.

Industry Consultation

You may have heard various media reports about calls for a Single Red Meat Industry Organisation. In the first instance, this would be merging Meat and Wool New Zealand and the Meat Industry Association to form an Industry Good organisation much in the way the DINZ is. There may be real benefit for deer if it became a part and your Board is open to considering the idea. While the proposal is on the table, DINZ will delay its voluntary industry consultation on DINZ's roles, function and levy until the single red meat industry organisation has been worked through, because that plan essentially provides another option for levy payers to consider.

Velvet; Graph, strategy bullet points

I now turn to velvet and the very difficult season which we have experienced. It is important to consider the difficult conditions and price volatility not in the context of the season, but of the context of the last 10 years. The simple fact remains that an auction-based sales system as the dominant means of sale is no longer an appropriate way to market New Zealand deer velvet. Over two years ago, your board responded to widespread producer dissatisfaction with the Status Quo. The industry structure under the status quo was at that time a mix of Pool operations, road buying and a farmer owned co operative. Across the industry there were unsatisfactory returns from the wider producer perspective, along with the onshore processing sector grappling with the effects of exporting velvet in the green form.

The appetite for a changed business model has fallen short and leaves our fantastic niche product open to abuse.

I am certain that producers think much more of their product than that and the vision of a high level marketing approach already held by a fair percentage of producers and including Velexco must not be lost to the industry.

We must take a position. The strategy of "sitting on the fence then placing a bet when a sure winner appears" will not allow the result in progress for the better.

Velvet Industry Strategy

In terms of other aspects of the velvet strategy, there has been solid progress. Rhys will report on this more fully during his presentation, but there are a couple of topline points which I'd like to make.

Firstly to Asian markets. The recent signing of the Free Trade Agreement with China was very positive for the deer industry. All tariffs on New Zealand deer exports which ranged from 35 to 9% will be eliminated by 2013. No NZ deer products were considered 'sensitive' unlike some cheese, butter and milk which will have a longer phase out time out to 2019 and sheep and beef products which do not have their tariffs eliminated until 2016. DINZ estimates that industry exports to China are probably around \$20 million per annum and growing with demand for co-products and Chinese grade velvet.

In Korea, the Korean Food and Drug Administration has recently begun to allow the sale of velvet as a food category. There have already been some sales of New Zealand sliced velvet outside the traditional pharmaceutical area and this is consistent with a broadening of velvet consumption from being a straight pharmaceutical to also being sold as a healthy food.

In Taiwan, the DINZ executive and New Zealand government continue to engage the Taiwanese Deer Farmers Association to encourage them to see the New Zealand deer industry as a collaborator rather than a threat.

Emissions Trading Scheme

I turn now to the Emission Trading Scheme. Our business is directly related to the price sensitive food consumer market and as producers, we are constantly balancing increasing costs of 'doing business' against a fixed budget and we have no mechanism to hand these increased costs on.

As such, there will be no way to pass on the cost of the ETS to consumers. With competing nations sheltering their producers, New Zealand products, including venison, will be less price competitive. Government figures indicate a very significant negative impact on profits from deer farming of between 30 and 200 percent depending on the price of carbon. In this case, deer farming if this scheme is to be implemented is simply not sustainable until there is a major breakthrough in technology. The recent news that agriculture will be able to emit at 90% through to 2018 is positive, but still does not resolve the underlying threat. DINZ is approaching the issue on a number of fronts.

Firstly, we are working with a pan pastoral sector group including Meat & Wool New Zealand, Fonterra, the Fertiliser Manufacturers Association and Federated Farmers. This group is working to ensure that any ETS works acceptably for agriculture.

Secondly, Deer Industry New Zealand is taking any opportunity to raise fundamental concern with the scheme with government. For example I appeared before the Select Committee for the Climate Change legislation yesterday.

Thirdly, DINZ has begun to make more public statements concerning its concern with the ETS and its likely effect on Kiwi consumers, and that a focus on science is a better solution.

We will continue to work the issue through.

Productivity

Our industry strategy is about growth and to be successful in the NZ pastoral landscape, we must be growing based on increased market demand and at a faster rate than competing land uses. The expanding dairy sector fuelled by increasing payouts in spite of a high exchange rate, is certainly putting the heat on the deer industry to step up and perform. One of the key ways that the industry can compete is by improving productivity. This is one element which is getting significant industry attention and I believe it is one of the keys to our economic sustainability.

Velvet has had fantastic gains with the average weight for three year old velvet increasing by 83% since 1993 - heritability being the major factor. If both venison and fecundity can

improve to a similar extent, the industry will be in a significantly better position. It is one of the few areas which is in our hands. Work has started, and I urge all producers to get involved. It will need a large collective effort from us all, but the benefit makes it well worthwhile. It is the productivity within our sector that determines the land use and therefore drives our future farming enterprise.

Final comment

Ladies and Gentlemen, we have a fine line up of speakers for you this morning. The challenges facing us are in fact opportunities and I am very optimistic that we will collectively make the right decisions for the industry and that we are well positioned as an industry for a bright future.

Thank you.