



News Flash

The Ruminant Slaughter Equity Assistance Program

- Commentary -

By Kevin Grier & Larry Martin

Guelph, ON (November 2, 2005) It is not much of a stretch to assert that if it wasn't for the financial assistance of the federal government, that the Canadian cattle industry could not have survived the BSE crisis. There were flaws that were evident with hindsight in some of the support programs, but clearly the industry needed help and the federal government responded. Most producers were appreciative and Agriculture and Agri-Food Canada (AAFC) received credit.

It appears that AAFC and Minister Mitchell aren't content to rest on their laurels. Rather than just writing cheques to cover an obvious income disaster, AAFC and Minister Mitchell have decided to try their hands at industrial engineering. On October 25 AAFC issued a press release stating, "Further to the June 29, 2005 announcement to support transformation of the Canadian cattle and other ruminants industry, Agriculture and Agri-Food Minister Andy Mitchell today announced details of the Ruminant Slaughter Equity Assistance Program. The Equity Assistance Program requires a minimum investment per producer of \$1,000, triggering a government contribution of \$500. Agriculture and Agri-Food Canada will match up to one-half of an individual producer's investment to a maximum government contribution of \$20,000. The maximum government contribution available for any slaughter facility project is \$5 million."

Someone should have told AAFC and Minister Mitchell that Canada doesn't need any more cattle slaughter capacity. Furthermore, by encouraging producers to build slaughter plants now by subsidizing them, producers are likely to lose their investment.

The premise of course is that Canada needs more slaughter capacity in case the border closes again. In addition, since the border is still closed to cows and cow beef, the assertion must be that Canada particularly needs cow slaughter capacity. In light of the current Lakeside strike, these two arguments are probably making the program's creators feel pretty smart right about now. The trouble is that both of these assertions are wrong and the government's action is going to lead to market distortion and losses for producers.

According to the most reliable data available¹, Canada's current fed cattle slaughter capacity in federal plants is just over 75,000 head per week. Canada's current cow slaughter capacity is just over 17,600 head. Provincial kill on top of that amounts to about 5,000 head per week. Total weekly capacity is around 98,000 head. Weekly marketings in Canada during August and September amounted to fewer than 85,000 (74,000 head federal slaughter plus 10,000 head US

¹ Canfax, October 2005

slaughter exports). So far the math doesn't look too good. To make it worse, by the middle of next year, the capacity is expected to be nearly 106,000 head.

Even if the border was closed, Canada would have enough capacity to handle all fed marketings. By next year the best estimates² show that Canada will have more than enough capacity to handle non-fed marketings. To be fair, some will argue that the capacity numbers are a little inflated due to assumed Saturday kills or that it is impossible to run full out all the time. Even if that argument is accepted, it is important to recall that the border is open to fed cattle. Canada and the US are one market for fed cattle again and the capacity calculation really must include the US capacity that bids on Canadian cattle.

It is of interest to see where the growth in current capacity has come from. Between this fall and last fall, weekly fed slaughter capacity has grown by nearly 6,000 head or 8%. Non-fed slaughter has grown by nearly 8,000 head or nearly 80%. Of the growth in capacity since last fall, over 70% is accounted for by the big three packers, Cargill (including Better Beef), Lakeside and XL Foods. Another six or seven smaller firms account for the remaining 30% of the growth. In fact, those same top three packers have added nearly 17,000 head capacity since prior to the BSE crisis. The top three are obviously more than capable of handling all of federal slaughter currently occurring in Canada.

The top three invested in packing capacity when it was needed most, during the BSE crisis. That investment helped ease the pressure from cattle backing up in the marketing system. The investment occurred due to the exceptional profits during that period of time. Now that the border is open, these existing packers are operating larger, more modern plants. Furthermore, these packers have the financial resources gained during the profitable period.

The newer packers on stream in the last year and those coming on in the next year and those that Mitchell is encouraging have a much tougher row to hoe. Not only are they smaller and less financially liquid due to missing the profitable period, they are now competing for cattle in a market that is open to the US. Cattle will continue to flow to the US even with these new plants because the US market is very strong. Large US packers need Canadian cattle and the cattle will move south. Once the border opens to cows, thousands of cows will flow south for the same reason.

It is questionable whether providing grants to build plant capacity is good public policy. On the other hand, inadvertently doing so in such a way that good supply chain management can be encouraged is better than alternatives that have been tried in the past. In this regard, one can give Mr. Mitchell some good marks. But they should be only partial marks. If this was such a good idea, it should have been done 18 months ago when people were trying to build capacity and the border was closed. Now that the border is open again, Minister Mitchell is likely creating excess capacity. This is not to say that all the new plants will be in trouble. It is never wise to underestimate the creativity and resolve of an entrepreneur. Nevertheless there will be difficult times ahead for most of the new ones. While this government has never shown much hesitation about wasting tax dollars, Minister Mitchell is likely to get really concerned about a year from now when some of his producer packing plants start folding, after coming back to him for a bail-out.

² Canfax, October 2005