Agricultural Competitiveness White Paper – Submission IP78
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Submission re Issues of Drought and Debt in the Northern Beef Industry

Drought and Debt

The "perfect storm" of high debt, the high Australian dollar, overstocking on a State wide basis and drought has brought the northern beef industry to crisis point.

The proposition to establish a Reconstruction and Development Bank within the umbrella of the Reserve Bank has great merit; however this will take a number of months to establish with complicated legislation.

Action is required NOW.

- There was a rural property boom through the 00's despite seven dry years, landholders borrowed heavily for enterprise expansion during this time which has lead to a high level of debt for some in the industry;
- The Australian Dollar has been trading at historically extremely high levels which has made our beef exports less competitive and contributed to a fall in the price per kg. for cattle. Due to the fall in cattle prices and to ever increasing costs of inputs, such as fuel, enterprises were not able to take advantage of several good years to reduce debt;
- Queensland is overstocked with cattle due to the flow on effect of the 2012 shutdown of the live cattle trade with Indonesia instigated by the previous Federal Government and as a consequence pastures and fodder have been depleted at an alarmingly fast rate as the drought has taken hold;
- This overstocking has been exacerbated by the drought management policy of some landholders which is to hold cattle and hand feed and who are now faced with feed and fodder running out and are forced to sell in an already oversupplied market and with prices plummeting;
- 70% of the State of Queensland is drought declared as well as significant areas in northern New South Wales. Unless widespread rain is received before the end of February, 2014 additional areas in both States will be drought declared;
- Many cattle being sold are not suitable for the meat processors or to be taken into feedlots landholders are attempting to sell these cattle rather than shooting them;
- There has been a flow on effect in the market even for cattle that are in good condition as feedlots and abattoirs are close to capacity. Meat processors in Queensland have put through record numbers of cattle in the last year;
- People who had some feed were holding their cattle back until the market picked up but have been under pressure to sell as feed has dried up and cash flow pressures have mounted. Fodder for hand feeding is becoming scarce and expensive.

Financial Problems

- Some enterprises invested in additional land for expansion at the height of the property boom and have been trying to digest the consequences ever since;
- Some enterprises are not sustainable in the long term due to size of operation or less than optimal management

- Banks have pressured some of these enterprises to restructure and or sell, and some who have been hit with a succession of drought, flood and drought again have experienced severe cash flow problems which have them appearing on the banks "watch" or "management" or "sell" lists;
- "Market value" assumes a "willing buyer" and a "willing seller". In the current situation the sellers are "unwilling" and there are very few buyers;
- Some properties are being sold in a "forced sale" or "mortgagee in possession" situation and the banks are concerned that these heavily discounted prices are indicative of the general market value of all property in that particular area;
- There are numerous instances of properties adjacent to those sold under duress being asked by their banks to revalue even though they have not missed any repayments of principle or interest. Often the new value is considerably lower than that pertaining at the time the loan was taken out, and the banks are then concerned that to meet their prudential requirements the "loan to valuation ratio" has to be improved by a reduction in the principle of the loan;
- Given the drought and current cattle prices it is not possible in many instances for enterprises to reduce the principle of their loan. These enterprises are then pressured by the banks to list their property for sale;
- This situation snowballs, as more properties are listed for sale with few buyers the value drops even further, ultimately spiralling out of control and drawing more enterprises into the "loan to valuation" problem;
- While it can be argued that initially "problem loans" may have arisen due to unsustainable levels of borrowing or a lack of relevant management skills, the ongoing drought, decrease in property values and hangover from the shutdown of the live cattle trade (a Government initiative) the situation is now impacting on landholders with good management skills and in intimate knowledge of the environmental capacity of their land. These landholders could be forced to exit the industry and their skills would be lost (and missed) by the northern beef industry;
- These issues are all contributing to a serious, and critical, social welfare and health situation;
- The present Government response of allocating an additional $20 million or even $100 million through QRAA does not really make much difference to many landholders. Some people don't want to take on more debt even at concessional rates of interest. Others don't qualify as they are deemed to be unviable in the long term and this latter group are the people who should be assisted to exit the industry with dignity and in an orderly way rather than being forced to sell immediately and depressing the rural property market even further.
- Banks could be forced to accept losses of capital if properties are sold for ever increasing discounts.

A Possible Solution

All players in the northern beef industry, the State and Federal Governments and the major rural lending banks have a part to play in a "recovery package". The banks made a contribution to the boom in rural land prices due to their lending policies at the time.

- It is proposed that an immediate Moratorium be placed on "rural loans of concern" for 3 years to put a floor under the value of rural enterprises;
- This solution would have to be restricted to enterprises in the drought declared shires in Queensland and New South Wales and enterprises solely engaged in the broadacre beef industry in these States;

- Individual banks would be required to advise the State and Federal Governments of the number of enterprises each bank has with "loans of concern" and the total dollar amount of each banks exposure to these loans (this suggested solution should NOT apply to the "margin" and "secondary" lenders);
- A joint guarantee from the States and the Federal Governments could be given to the banks to support these loans. There is a precedent for such a guarantee, the Federal Government provided a guarantee to the trading banks during the global financial crisis;
- In return for such a guarantee the banks would observe the 3 year moratorium and during that time would not proceed with foreclosures. In addition, interest would only be charged and accrued at the effective rate rather than a penalty rate. Given the Governments guarantees a penalty rate would not be justified. This would be the banks contribution to the crisis;
- Such a Moratorium and Guarantees does not require the Governments to actually contribute money at a time of severe budgetary constraint, however there would be a contingent liability for the Governments;
- The guarantees, moratorium and interest provisions could be implemented quickly with one piece of legislation in each relevant Parliament;
- This would give breathing space to landholders allowing them to calmly assess their situation without the spectre of their bank threatening to force them to sell into a depressed market. It would give time for the Australian Dollar to stabilize around 80-85cents US. A drop in the A$ to these levels would flow through to cattle prices relatively quickly and would alleviate some of the current problems;
- In addition, it would be advantageous for the State and Federal Governments to jointly fund a number of independent financial analysts with a deep knowledge of the northern beef industry to assist the enterprises with "loans of concern" to look critically at their enterprises and to look at their viability and sustainability;
- Such analysis would help enterprises to decide whether they had a long term future in the industry or not, and, if not, to allow for an orderly exit gaining a fair market value for their property without undue pressure:
- A high standard of financial and industry analysis will lead people to make their own conclusion as to whether or not their enterprise is viable and sustainable in the long term;
- There are some landholders who would welcome the opportunity to retire but whose equity at current market prices for property is not sufficient to fund their retirement;
- If people with an unviable or unsustainable enterprise are able to exit with a fair value for their property they are more likely to be able to set themselves up in a new industry or to become self funded retirees and will be less of a drain on the already overburdened social security system.

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